NB Private Equity Partners

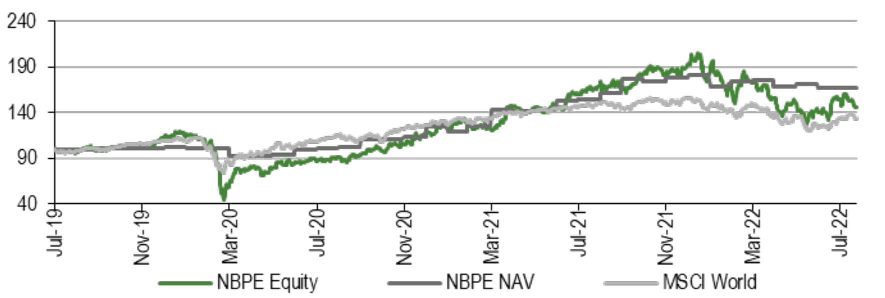
Track record yet to be fully rewarded

Investment companies
Private equity

13 September 2022

NB Private Equity Partners' (NBPE) latest NAV (as at end-July 2022) reflects an update on most private valuations from end-March to end-June 2022, which led to a very limited 2% fall in NBPE's private portfolio fair value. This impressive resilience allowed NBPE to deliver a strong three- and five-year NAV TR to end-July 2022 of 18.6% and 15.3%, respectively (c 2x the return of MSCI World Index), led by co-investments. Despite its strong track record, NBPE's shares still trade at a c 31% discount to NAV, wider than the average for its direct peers (although it also has a single-layer fee structure but a more diversified portfolio), which we find hard to justify. Its shares now offer an attractive 5.0% annualised yield (versus an average of 2.5% for peers).

NBPE has a long-term track record of strong NAV returns



Source: Refinitiv, Edison Investment Research. Total returns in sterling.

Why consider NBPE?

- Strong long-term track record, leveraging the strength of the Neuberger Berman (NB) platform. Direct investments now represent more than 90% of the portfolio and have generated an IRR above 20% over the long term.
- Focus on companies with long-term secular growth and lower expected cyclicality, profitable businesses in resilient sectors. Mainly invested in the US.
- Co-investment strategy provides investors with the benefits of diversification, but with control over the timing of new investments to focus on the best opportunities and respond to market conditions.
- Relatively wide discount despite solid performance and one-layer fee structure.

The analyst's view

NBPE's NAV already reflects valuations after the public market sell-off in H122, with c 77% of the portfolio now based on end-June values received so far from lead sponsors. The resulting 2% fair value reduction in private company positions compares favourably with a c 20% fall in the MSCI World Index in TR terms in Q222. We also note that NBPE expects its five full or partial exits announced in 2022 ytd (c US$110m of expected proceeds) to be closed at a 7% uplift to end-2021 carrying values, suggesting a prudent valuation approach. Its ytd NAV TR decline of 7.3% (vs the MSCI World Index's 14.0%) was largely driven by its listed holdings (14% of portfolio), primarily those floated in 2021 at an average valuation uplift of 125%, on whose partial exits NBPE has already realised a multiple of invested capital (MOIC) of over 1.6x.

NOT INTENDED FOR PERSONS IN THE EEA

Price	**1,605p**
Market cap	**£750.6m**
NAV*	**£1,091.9m**
NAV*	**US$1,329.1m**
NAV per share*	£23.35
NAV per share*	US$28.42
Discount to NAV	31%

*As at end-July 2022.

Yield		5.0%
Shares in issue		46.8m
Code Ord/ISIN		NBPE/GG00B1ZBD492
Primary exchange		LSE
AIC sector		Private Equity
52-week high/low	US$26.18	US$15.61
NAV high/low	US$31.97	US$26.77

Gearing

Net gearing at 31 July 2022 6.2%

Fund objective

NB Private Equity Partners invests in direct private equity investments alongside market-leading private equity firms. NB Alternatives Advisers, an indirect wholly owned subsidiary of Neuberger Berman, is responsible for sourcing, execution and management of NBPE. The vast majority of direct investments are made with no management fee or carried interest to third-party general partners. NBPE seeks capital appreciation through growth in net asset value while paying a biannual dividend.

Bull points

- 10-year NAV TR above peer average.
- An attractive one-layer fee structure (as opposed to private equity funds-of-funds).
- Higher diversification than direct peers.

Bear points

- Timing of exits depends on GPs' decision (but whose interests are largely aligned with NBPE).
- Public markets downturn translating into lower PE deal volumes and in turn more limited exit opportunities.
- Structural leverage may amplify NAV decline in a downturn scenario (although net gearing is lower than 12–24 months ago).

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Portfolio value proves resilient to market downturn

NBPE has consistently outperformed public equity markets, with an average annual NAV TR of 16.2% (in sterling terms) over the last 10 years, according to our calculations, compared to the MSCI World Index's 13.6% pa. This is also illustrated by the much more moderate decline in the carrying value of private holdings in Q222 versus the broader equity markets, which likely comes from a combination of NBPE's portfolio composition (see below) and technical factors that smooth out the portfolio valuations of listed private equity companies. The latter include in particular the use of valuation multiples derived from a blend of public multiples and private M&A deal multiples (the latter are usually less volatile and may lag public market downturns in the short term) and the common PE practice of valuing new investments in line with the acquisition price over the subsequent 12 months.

NBPE's performance is slightly higher than the private equity peer average of 15.3% pa over the last 10 years, despite the period capturing NBPE's higher exposure to income investments (with a lower return expectations) in the past. NBPE's NAV already reflects the market downturn in H122, as opposed to its funds-of-funds peers, which (like NBPE) receive portfolio valuations from their general partners with a certain time lag. Even those who released their end-July NAV estimate still have their portfolios valued predominantly as at end-March: HarbourVest Global Private Equity (85% of portfolio value), Pantheon International (70%) and abrdn Private Equity Opportunities (98% excluding new investments). CT Private Equity Trust and ICG Enterprise Trust have their latest NAV estimates as at end-June and end-April. Among NBPE's direct PE peers, Oakley Capital Investments and HgCapital Trust have their valuations as at end-June, while Princess Private Equity's portfolio is valued as at end-July. The above time differences currently limit the comparability of NBPE's returns versus peers. We also note that the ongoing charge comparison presented in Exhibit 1 considers entity-level costs only, which should be higher on a look-through basis among funds-of-funds after accounting for the second layer of fees already reflected in their NAV TR.

We note that discounts have widened generally across the PE peer group recently to 35% on average (from an average 14% in our November 2021 note), likely in anticipation of some downward portfolio revaluations. NBPE currently trades at a discount to NAV of 31% compared to an average 22% among direct investors and 42% among funds-of-funds. Given its updated portfolio valuations, a one-layer fee structure and healthy historical returns, we believe that NBPE deserves to be trading at a narrower discount than its funds-of-funds peers.

Exhibit 1: Listed private equity investment companies peer group at 8 September 2022* (in sterling terms)

% unless stated	Market cap £m	NAV TR 1 year	NAV TR 3 year	NAV TR 5 year	NAV TR 10 year	Discount (cum-fair)	Ongoing charge**	Perf. fee	Net gearing	Dividend yield
NB Private Equity	**748.1**	**23.9**	**68.5**	**121.4**	**349.0**	**(31.3)**	**2.0**	**Yes**	**108**	**5.1**
HgCapital Trust	1,827.9	20.6	92.8	172.0	382.2	(10.0)	1.4	Yes	100	1.8
Oakley Capital Investments	721.6	42.7	104.4	190.7	293.5	(35.1)	2.2	Yes	100	1.1
Princess Private Equity	659.4	(5.3)	26.3	54.7	176.0	(21.9)	1.8	Yes	101	6.5
Direct funds average	**1,069.6**	**19.3**	**74.5**	**139.2**	**283.9**	**(22.3)**	**1.8**	**-**	**100**	**3.1**
abrdn Private Equity Opportunities	630.4	29.8	75.7	118.7	302.5	(42.3)	1.1	No***	100	3.4
CT Private Equity Trust	302.3	22.7	87.8	120.6	274.6	(36.8)	1.2	Yes	100	5.2
HarbourVest Global Private Equity	1,737.0	38.0	88.5	162.0	421.3	(47.3)	1.3	Yes	100	0.0
ICG Enterprise Trust	719.4	27.7	74.0	122.3	364.3	(40.4)	1.4	Yes	104	2.0
Pantheon International	1,420.2	32.8	64.9	116.2	296.1	(43.4)	1.2	Yes	100	0.0
Funds of funds average	**961.9**	**30.2**	**78.2**	**127.9**	**331.8**	**(42.0)**	**1.2**	**-**	**101**	**2.1**
Average (8 funds)	**1,002.3**	**26.1**	**76.8**	**132.1**	**313.8**	**(34.6)**	**1.4**	**-**	**101**	**2.5**
NBPE rank in sector	**7**	**7**	**8**	**6**	**4**	**4**	**2**	**-**	**1**	**3**

Source: Refinitiv, Edison Investment Research. Note: *12-month performance based on latest available ex-par NAV: end-July for NBPE, HarbourVest Global Private Equity, abrdn Private Equity Opportunities Trust, Pantheon International and Princess Private Equity; end-June for Oakley Capital Investments, CT Private Equity Trust and HgCapital Trust; end-April for ICG Enterprise Trust. **Ongoing charge at fund level only; does not capture the second layer of fees in the funds-of-funds subgroup. ***Performance fees paid at underlying funds level. Net gearing is total assets less cash and equivalents as a percentage of net assets. 100 = ungeared.

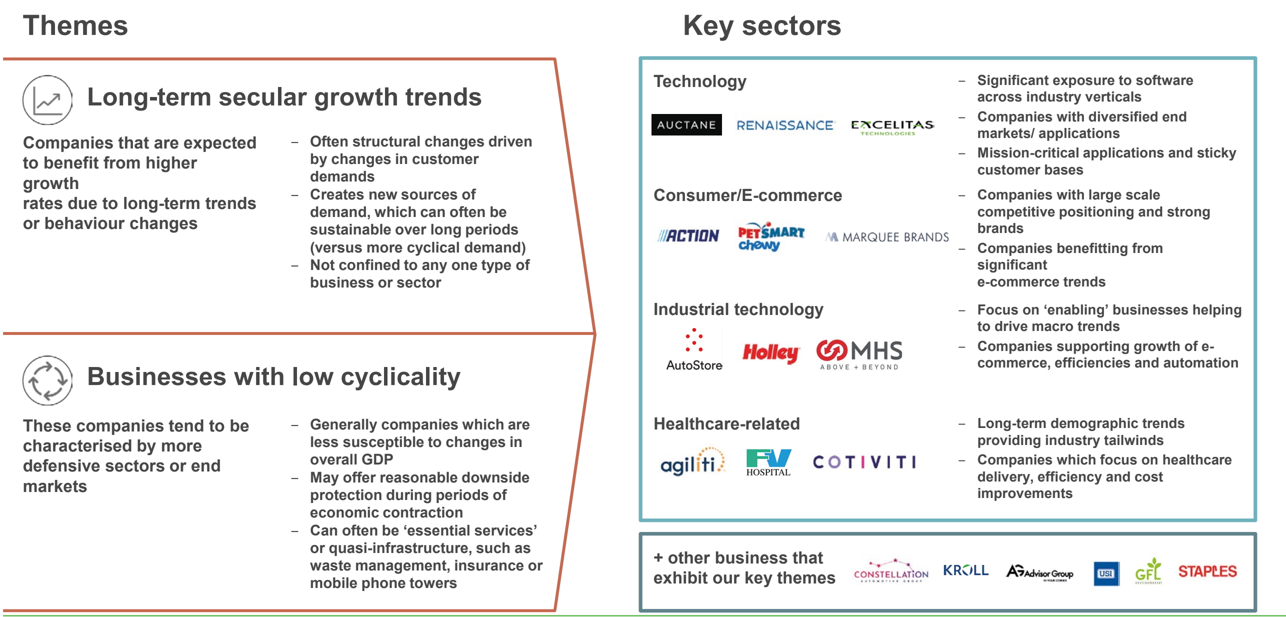
Two core themes: Long-term secular growth and low expected cyclicality

NBPE's portfolio resilience in 2022 ytd has been assisted by its focus on companies which are exposed to long-term secular growth and/or have lower expected cyclicality. NBPE invests in companies that may benefit from structural changes in customer demand and are not confined to any one type of business or sector. The main secular tailwinds recognised by NB are tech-enabled services, automation, e-commerce and ageing demographics. Examples of such investments among NBPE's top holdings are AutoStore (3% of NBPE's portfolio at end-July 2022) and MHS (3%), which provide technology and systems for distribution centres (automated robotic storage and parcel sorting, respectively). These businesses profit from the expansion of e-commerce and the resulting demand for supply chain efficiency enhancements. Agiliti (4% of the portfolio) provides management services for medical equipment, which NB (NBPE's investment manager) expects to grow on the back of ageing demographics and an associated increase in healthcare spending. Finally, Renaissance Learning (2% of the portfolio at end-FY21) also benefits from a long-term secular growth trend as it provides technology solutions for teachers and administrators to plan, teach and help motivate students to learn.

NBPE also looks for companies with low expected cyclicality by providing essential services, including quasi-infrastructure businesses, such as GFL (2% of portfolio value at end-May), which provides waste management systems and USI, an insurance broker and provider of consulting services (3%), or Telxius (1% at end-FY21, sold in 2022), which operates telecommunications infrastructure including fibre optic cables and telecom towers.

Part of NBPE's portfolio shares both of the above characteristics. For instance, PetSmart Chewy (2% at end-FY21) is a retailer of pet supplies demand for which may be more resistant to a downturn, while strongly focused on the e-commerce channel through its Chewy subsidiary. Further examples include Cotiviti (2% at end-July), which develops payment accuracy and solutions for the healthcare industry, and Kroll (formerly Duff & Phelps, 3% at end-July), a leading provider of diversified professional and business services, including valuation, risk management and bankruptcy administration.

Exhibit 2: NBPE's approach to its two core themes



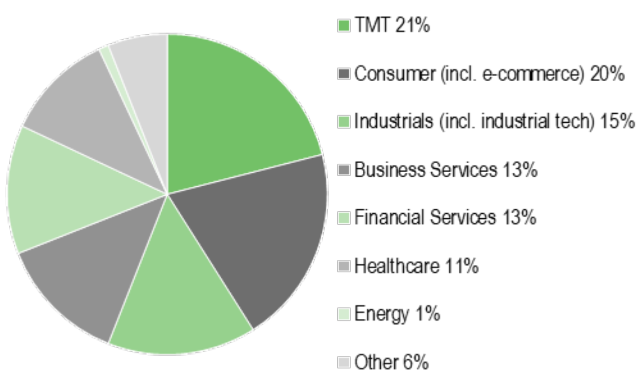
Source: NBPE

High exposure to US and broad sector diversification

As at end-July 2022, NBPE's portfolio consisted of 95 direct co-investments, which made up 91% of its portfolio and are the powerhouse of NBPE's returns. The remainder of the portfolio are gradually diminishing exposures to private debt (8%) and legacy fund exposures (1%). The portfolio is diversified across sectors, with the largest exposures to TMT (21%) and consumer (20%). However, we should highlight that sector exposures are skewed towards the secular growth trends within them. NBPE disclosed that 47% of its TMT holdings at end-May were software companies (including several SaaS businesses) and 18% were tech services businesses. Furthermore, 53% of its industrials exposure was attributable to industrial technology companies MHS and AutoStore (see above). Finally, consumer exposure is heavily skewed towards e-commerce companies.

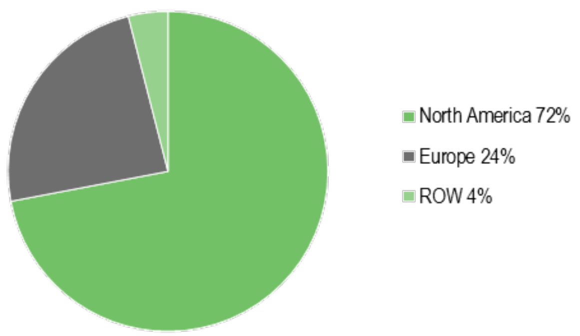
In addition, the portfolio is allocated predominantly to the US (72% of portfolio companies are North American), which may prove beneficial compared to its Europe-investing peers in the current environment. While the impact of the unravelling recession and rising geopolitical tensions is currently difficult to predict, we note that the US is not subject to the same energy security risks as Europe. Nevertheless, amid potentially rising energy prices globally, NB highlights that energy is not a significant input cost across the portfolio and that many of its portfolio companies provide critical solutions to their clients.

Exhibit 3: Portfolio split by sector



Source: NBPE as at end-July 2022

Exhibit 4: Portfolio split by geography



Source: NBPE at end-July 2022

Following its strong performance in FY21, NBPE has US$367m available capital (28% compared to its NAV), which consists of US$67m in cash and a US$300m credit facility (fully undrawn as at end-July). In the bull market, NBPE enhanced its returns through structural leverage in the form of two series of zero dividend preference (ZDP) shares (US$149m in total as at end-July). NBPE intends to repay the first ZDP series on maturity on 30 September 2022 (the other series matures in 2024), which should leave it with ample liquidity to pursue new investments. Although the company has remained cautious so far in 2022 (with only one US$26m co-investment), its investment manager is actively reviewing new investment opportunities.

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