

## Private equity market sentiment continues to cool – investors are much more pessimistic

29 August 2022

Author: Dr Georg Metzger, phone +49 (0)69 7431-9717, georg.metzger@kfw.de

Press contact: Wolfram Schweickhardt, phone: +49 (0)69 7431 1778, wolfram.schweickhardt@kfw.de

- Private equity market sentiment has slid further into the red, weighed down by significantly more pessimistic business expectations
- Sharp decline in fundraising and exit environment
- Indicators of economic activity and interest rate level near record lows

### Private equity sentiment: Losses are widening

The German private equity market experienced a further loss of confidence in the second quarter of this year. The sentiment indicator of the later-stage segment fell by 17.8 points to -24.7 balance points. Business expectations were more heavily affected than situation assessments. The indicator for the current business situation slipped by 13.2 points to -10.9 balance points. The indicator for business expectations plunged by 22.5 points to -38.5 balance points.

### Uncertain macro environment poses challenges

Responding to high inflation rates, international central banks accelerated the interest rate turnaround in the second quarter, catching financial markets offguard. The indicator for the interest rate level dropped very close to its previous all-time low. The last time assessments were this low was at the start of the financial crisis of 2008. In the context of the debate over a halt to natural gas supplies and its consequences for the German economy, economic worries also increased again. The economic environment has deteriorated further but is still well above its previous all-time low. The fundraising climate had cooled already in the first quarter as a result of the rising interest rate level and has now become significantly frostier again. Rising interest rates also lead to lower company valuations. This increases write-down pressure on investors' portfolios. The corresponding indicator has slid into negative territory. Write-down pressure in the private equity market appears to be much lower than in the venture capital market, however. Company valuations there react much more sensitively to interest rate changes because companies are younger and on a steeper growth path. Exit opportunities are also suffering from macroeconomic developments. The IPO window on the stock markets has closed and companies that could take over participations as part of M&A deals are probably reluctant to close such deals because of the great uncertainty. Accordingly, the exit environment has clearly slipped into the red.

### Development of private equity sentiment indicator



Source: KfW Research, BVK and DBVN.

### Key data of private equity sentiment components

Values in balance points

	Q2/22	Δ vs. Q1/22	High	Low
Business climate	● -24.7	↓ -17.8	▶ +35.3	▶ -85.2
Business situation	● -10.9	↓ -13.2	▶ +44.1	▶ -80.9
Business expectations	● -38.5	↓ -22.5	▶ +26.5	▶ -89.5
Fundraising	● -32.6	↓ -25.6	▶ +44.3	▶ -70.2
Entry evaluations	● +20.5	↑ +19.4	▶ +62.0	▶ -32.8
New investment	● -3.1	↓ -9.7	▶ +27.0	▶ -77.3
Exit opportunities	● -28.9	↓ -34.7	▶ +54.8	▶ -88.4
Dealflow quantity	● +5.0	↓ -10.4	▶ +21.8	▶ -29.0
Dealflow quality	● +3.9	→ +4.8	▶ +23.3	▶ -24.4
Taxation framework	● +1.4	→ +0.8	▶ +24.6	▶ -39.0
Write-downs	● -7.5	↓ -14.1	▶ +32.0	▶ -54.1
Economic development	● -76.2	↓ -8.6	▶ +72.9	▶ -92.0
Interest rates	● -76.8	↓ -38.4	▶ +33.7	▶ -79.3

Colour scheme of sentiment indicator dots: values in the lowest tercile are marked 'red', in the medium tercile 'amber' and in the highest tercile 'green'. Indicator design may lead to deviations from previous publications. The indicators of exits, taxes and valuation pressure cannot be compared to the previous quarter's publication due to corrections.

Source: KfW Research, BVK and DBVN.

### Comments on the current trend

#### Dr Fritz Köhler-Geib, Chief Economist of KfW

'After a weak start to the year, private equity market sentiment has cooled further,' said Dr Fritz Köhler-Geib, Chief Economist of KfW. 'Interest rate and economic worries are visibly weighing on the private equity market. This has had a negative impact on the fundraising climate and exit environment in particular. However, it is pleasing to see how well deal flow has held up in this environment so far. Investment opportunities therefore continue to exist. The need for businesses to reassess and reorganise supply chains and energy dependencies may even open up further investment opportunities. After all, funding needs for such strategic realignments may be very high and are likely to come into the focus of many PE investors.'

#### Ulrike Hinrichs, Managing Director of the German Private Equity and Venture Capital Association (BVK)

'The macro environment continues to weigh on the mood of private equity companies. The lower valuations and thus more favourable entry opportunities as well as the robust deal flow are therefore of little consolation', said Ulrike Hinrichs, Managing Director of the BVK. 'So long as the economic uncertainties and the geopolitical conditions remain, investors will focus less on new commitments and instead make their existing participations resilient to crises in the areas of funding, exchange rates, supply chains and energy. The strategic strengths and financial reserves of investment companies as equity holders should pay off here. Nevertheless, they are certain to continue harnessing opportunities that arise for interesting new investments.'

### Calculation of the German Private Equity Barometer

The **German Private Equity Barometer** is based on a quarterly survey of the members of the German Private Equity and Venture Capital Association (Bundesverband Deutscher Kapitalbeteiligungsgesellschaften – BVK), the member investors of the Deutsche Börse Venture Network (since the 2nd quarter of 2021) and further private equity companies with registered offices in Germany. It reports on business sentiment in the German private equity market on the basis of assessments provided by private equity firms with a focus on mature small and medium-sized enterprises. All sentiment indicators represent the average of the balance of situation assessments (share of 'good' minus share of 'bad') and the balance of expectations identified at the same time for the coming six months, adjusted by their respective historical mean balance values. Because of the way the barometer is constructed, positive indicator values point to above-average sentiment and negative values to below-average sentiment.

The **German Venture Capital Association** is the voice in the face of the private equity industry in Germany. The association is committed to improving conditions and facilitating access to private equity so that even more businesses in Germany can benefit from private equity. It has some 300 members. These include around 200 private equity companies and investors as well as some 100 consulting firms and service providers of the industry.



The **Deutsche Börse Venture Network (DBVN)** was launched in 2015 and is now Europe's largest network for growth finance and 'Capital Market Readiness'. It focuses on providing efficient access to capital and has an extensive range of networking and training services. The network of more than 200 fast-growth businesses and more than 450 investors has already enabled 13 IPOs and numerous trade sales.

Deutsche Börse  
Venture Network