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Capital Markets Update

December 4, 2023

General Market Update

Market Update

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- Shift in narrative as markets are becoming more convinced of a soft landing
- Between 2 and 4 central bank rate cuts priced in for 2024
- Equities and bonds to increase over the quarter

Performance of selected benchmarks as of Dec. 01, 2023:

	ACWI LOCAL	MSCI Europe Local	S&P500	MSCI EM LOCAL	MSCI WORLD USD	MSCI ACWI GBP	MSCI ACWI EUR	US Small Cap	MSCI EM (USD)	US 10 Yr Futures	UK Gilt Index	EM Bonds	HY
MTD Dec 2023	0.5%	0.7%	0.6%	-0.3%	0.5%	0.7%	1.2%	3.0%	-0.5%	0.8%	0.1%	0.4%	0.3%
QTD	5.7%	2.9%	7.5%	2.0%	6.4%	2.8%	4.0%	4.6%	3.3%	3.0%	2.9%	4.7%	3.6%
YTD 2023	17.5%	11.4%	21.5%	6.1%	17.1%	11.5%	15.4%	7.3%	5.2%	1.4%	-1.1%	5.8%	9.7%
12 Months	11.8%	7.8%	14.6%	3.9%	11.7%	8.5%	8.1%	0.6%	3.0%	-0.3%	-5.8%	4.9%	8.1%

	Cons Discr	Cons Staples	Energy	Financial	Health Care	Industrial	InfoTech	Material	Real Estate	Comm Services	Utilities
MTD Dec 2023	1.3%	0.4%	0.5%	0.7%	0.4%	1.6%	0.2%	1.2%	2.1%	-0.2%	1.2%
QTD	7.3%	3.2%	-6.5%	9.0%	2.4%	7.3%	13.0%	6.1%	11.6%	5.6%	7.9%
YTD 2023	35.9%	-1.7%	-0.8%	7.2%	-1.8%	12.1%	52.3%	8.9%	5.5%	48.3%	-7.7%
12 Months	20.8%	-4.1%	-3.3%	2.3%	-3.9%	8.8%	39.4%	2.8%	0.7%	36.3%	-8.1%

Source: Bloomberg, SECOR. Data as of December 01, 2023

Source: Bloomberg, SECOR

Macro and Fixed Income

Macro Developments

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- US Q3 GDP growth was revised up to 5.2% from an initially reported 4.9% rate
- SPX finished its best month in over a year (+8.9%) and best November on record
- Equity volatility has been muted, with SPX 10-day realized vol touching two-year lows and VIX settling (12.6) at its lowest level since September 2020
- Month of November saw the largest easing in US financial conditions of any single month in the past four decades (measured by GSUSFCI Index)
- Market pricing 80% change of first cut by May 2024, with a total of 5 cuts in 2024 (-125bps)
- Data rich period upcoming ahead of FOMC meeting next week – ISM (12/5), NFP & Unemployment (Friday 12/8), CPI (Tuesday, 12/12)

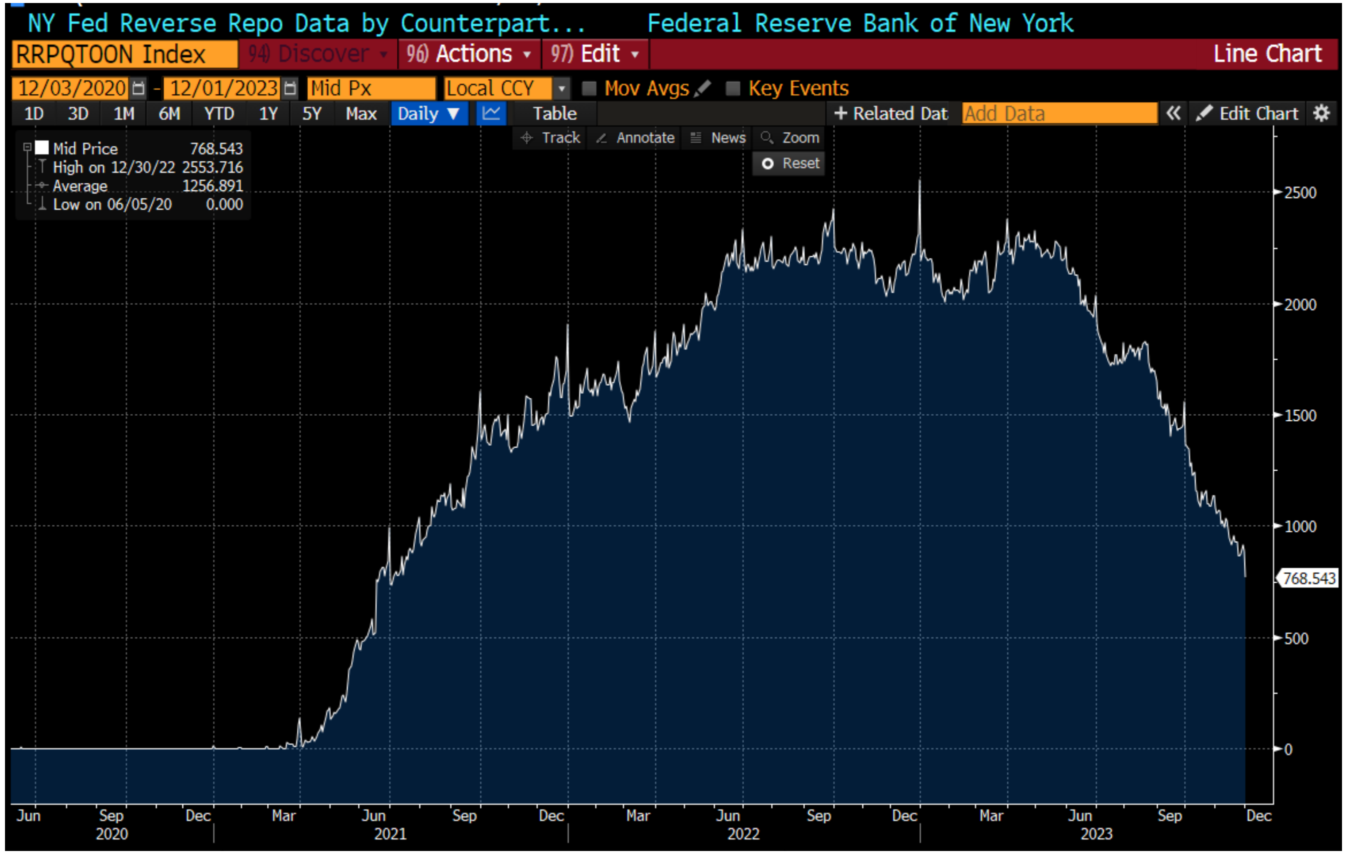
Source: Bloomberg, SECOR

Macro Developments

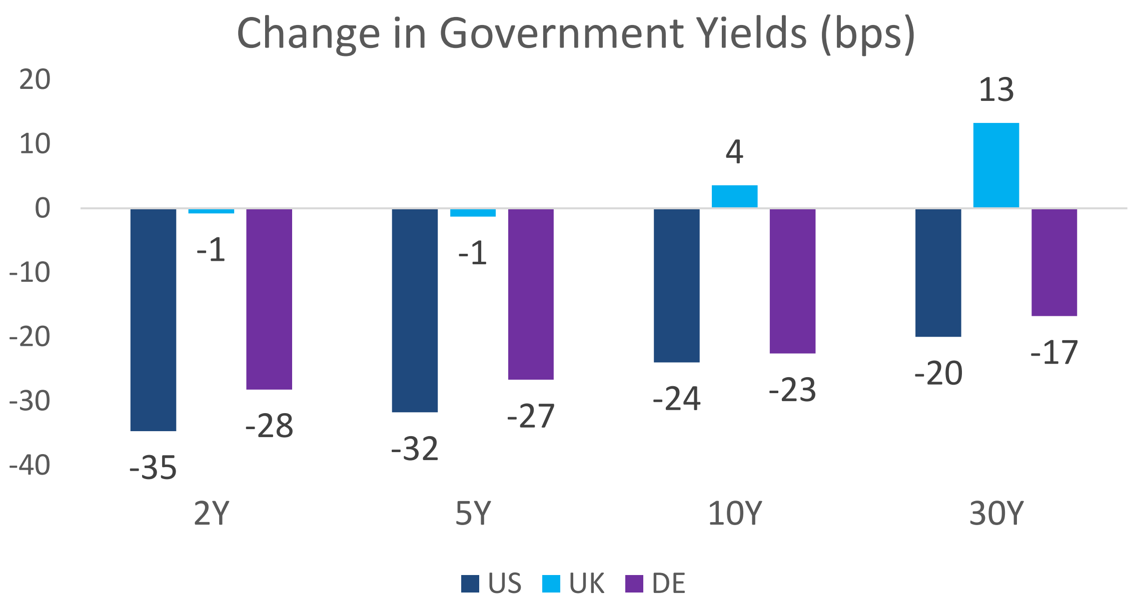
- Reverse repo (RRP) balances fell $250B in November. Cash is moving from RRP into Treasuries (offering slightly higher yield) and risk assets. Decreasing RRP represents increasing liquidity in markets

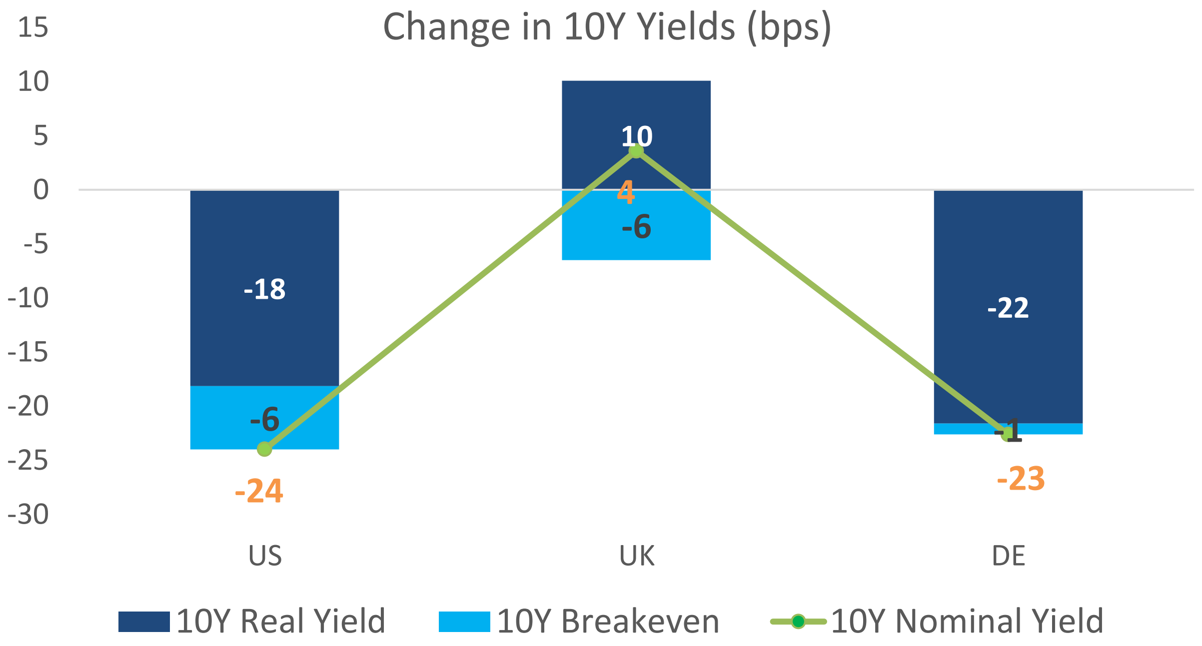
- Treasury has an estimated $1.5Tn of upcoming auctions between now and the end of the first quarter of 2024
  - Reverse repo will soon be drained. If the Treasury keeps the same pace of auctions as the last few months, then RRP could be drained by January

- Look for fixed income volatility to pick up once RRP is drained – Treasury will need new sources to buy government debt



DMRates





- Rates rallied in US and EU and steepend across the board over the past two weeks since 11/17
- US Treasury yields fell led by the front end amid dovish Fedspeak and soft inflation data globally
- Inflation surprised to the downside in the euro area, with y/y headline and core HICP falling to 2.4% and 3.6%

Source: Bloomberg, SECOR

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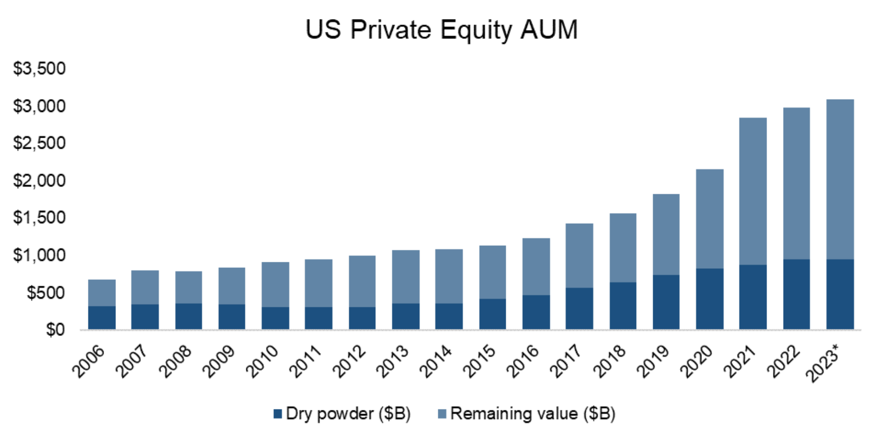
Equity Update

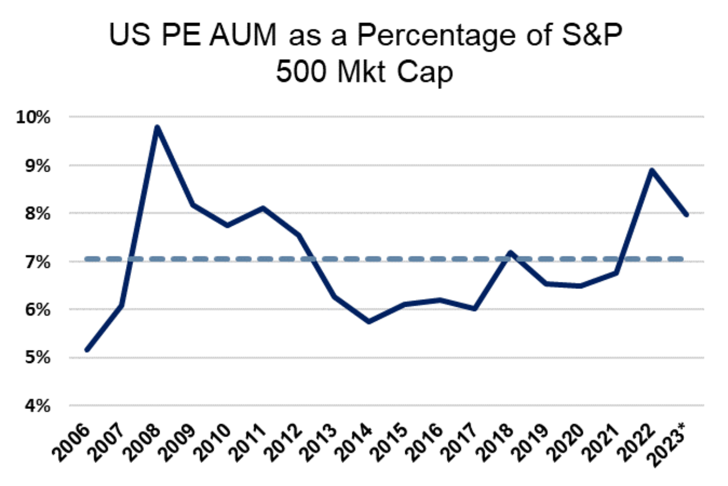
US Private Equity AUM

- **US Private Equity assets totalled $3.1T at Q3 2023.**
  - US PE AUM has grown by 9.8%/year since 2006 or roughly the same pace as the public equity market as the S&P 500 returned 9.3%/year over the same period.
  - Current dry powder of $960B represents 31% of AUM, well below the average of 37% since 2006.

- **Current Private Equity assets total 8% of the S&P 500 market capitalization, slightly higher than the 7% average since 2006.**
  - Total US PE AUM is approximately the same size as the market capitalization of Apple.



* Data as of 31 March 2023

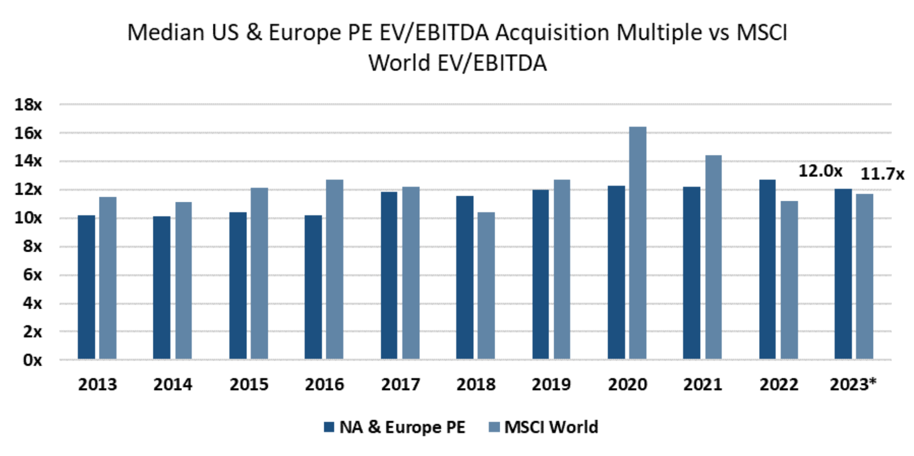


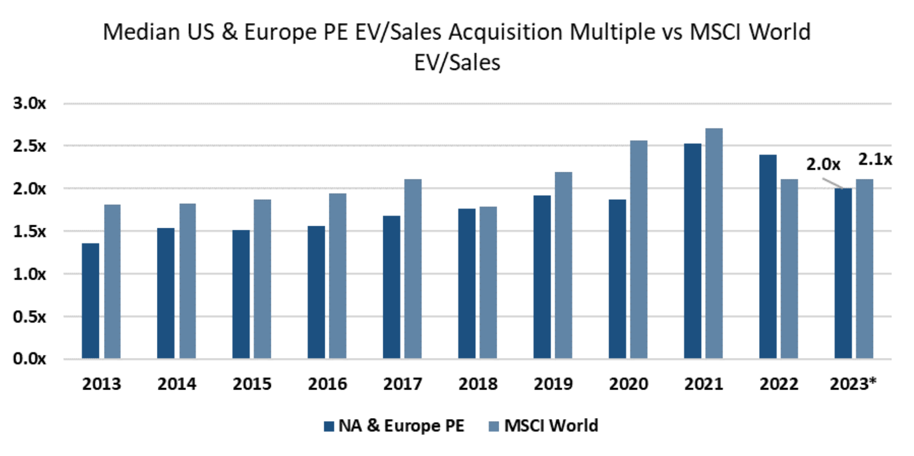
Sources: Pitchbook, Standard & Poor's, Bloomberg, SECOR.

US & Europe Purchase Multiples

- **The median PE acquisition multiple in US & Europe through the first three quarters of 2023 (12.0x) aligns closely with the EV/EBITDA multiple of the public market (11.7x).**
  - Since 2013, the public market has traded at 1x multiple point higher than that of the private market, 12.4x versus 11.4x.

- **A similar story on EV/Sales basis, where current private and public multiples are similar.**
  - Public markets have traded at a 0.3x premium to private since 2013, 2.1x versus 1.8x.



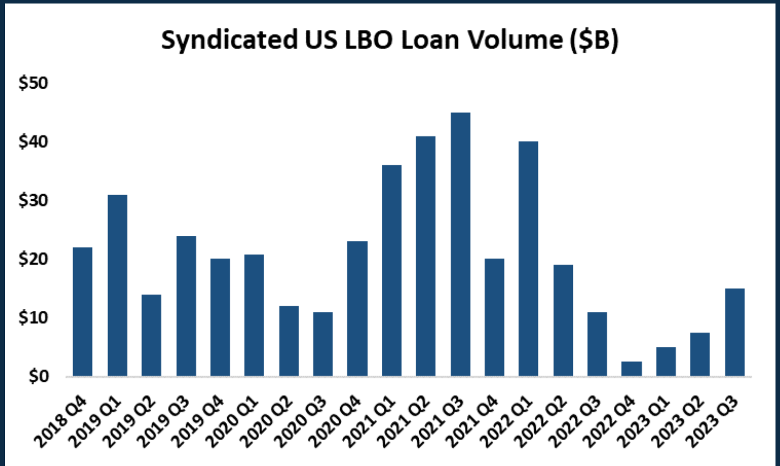


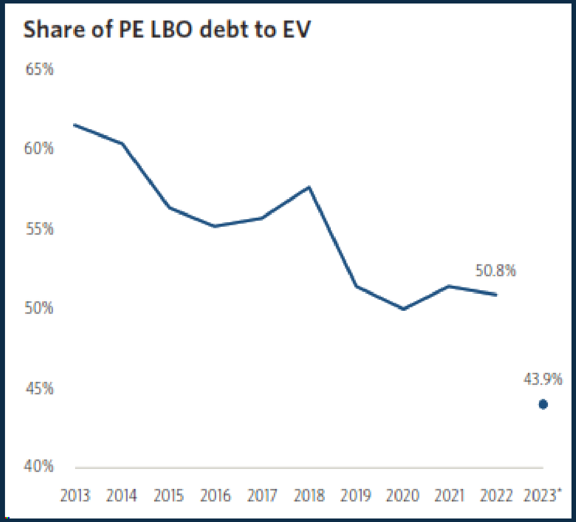
* Data as of 30 September 2023

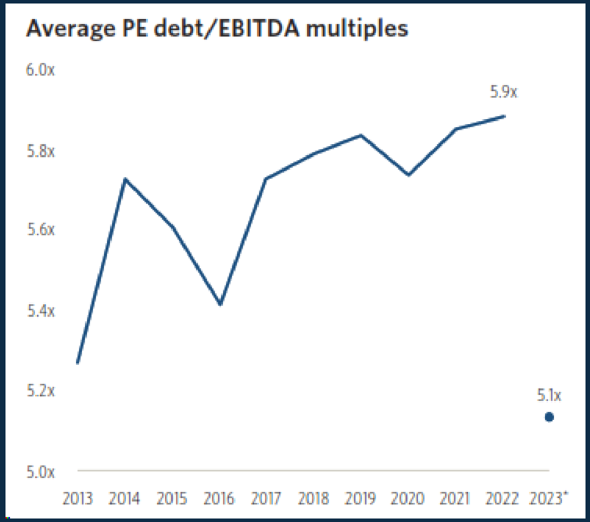
Sources: Pitchbook, MSCI, Bloomberg, SECOR.

LBO Lending Thaws But Less Levered Deals

- **Disruption in the LBO lending market appears to be easing.**
  - Q3 LBO loan volume increased to $15B, still behind the average of $21B over the last five years.
  - Banks are returning to their traditional role as LBO lenders and private credit now dominates the sub-$1B market.
- **Leverage ratios have contracted.**
  - Debt as a percentage of total deal value dropped to 44% in Q3 from 51% in 2022 (10-year average = 55%).
  - Debt/EBITDA has also contracted sharply to 5.1x in 2023 from 5.9x in 2022.





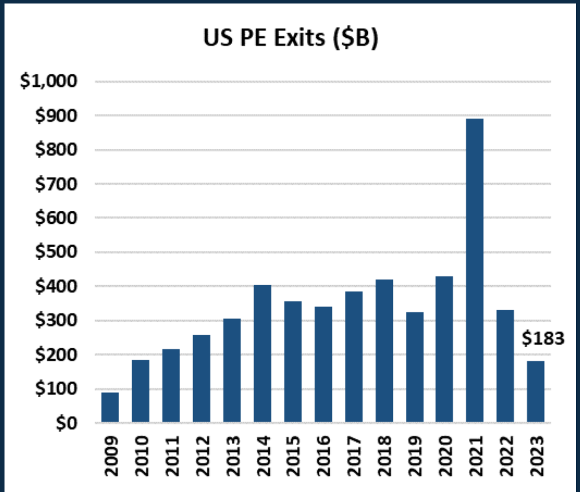


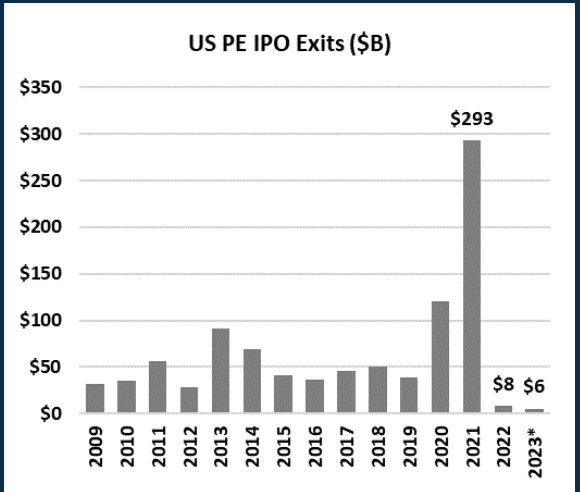
Sources: Pitchbook, LCD, SECOR.

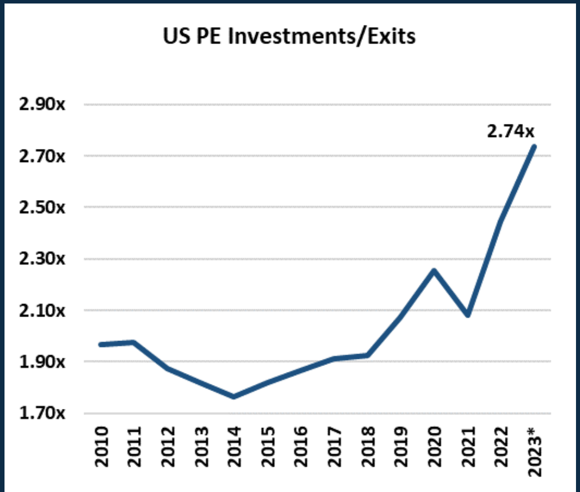
PE Exit Doldrums Continue

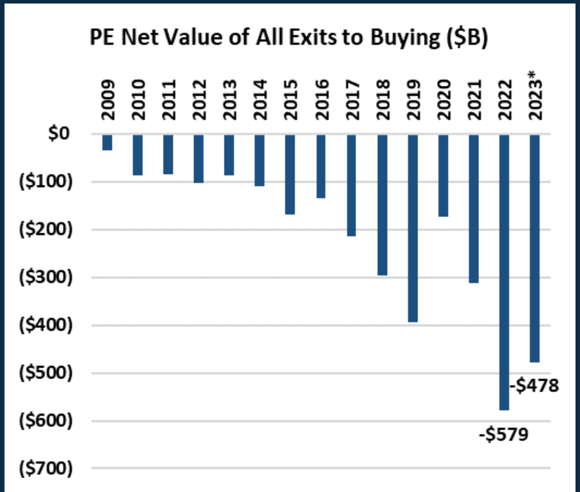
- **Exits remain weak as the IPO window remains firmly closed.**
  - US PE exits of $183B through Q3 2023 are on pace for the weakest year since 2011.
  - After a dismal 2022 that saw only 13 PE exits via IPO for an aggregate exit value of $8B, there have been just 9 PE exits via IPO through the first three quarters of 2023 with an aggregate exit value of $6B.
    - 2021 was a record-setting year with $891B in total exit proceeds, $293b which came from 147 public listings.

- **The imbalance between exits and investments is at an extreme level.**
  - In 2023, there have been 2.74 investments for each exit.
  - 2023 will likely be the second consecutive year with investments exceeding exits by more than half a trillion dollars.









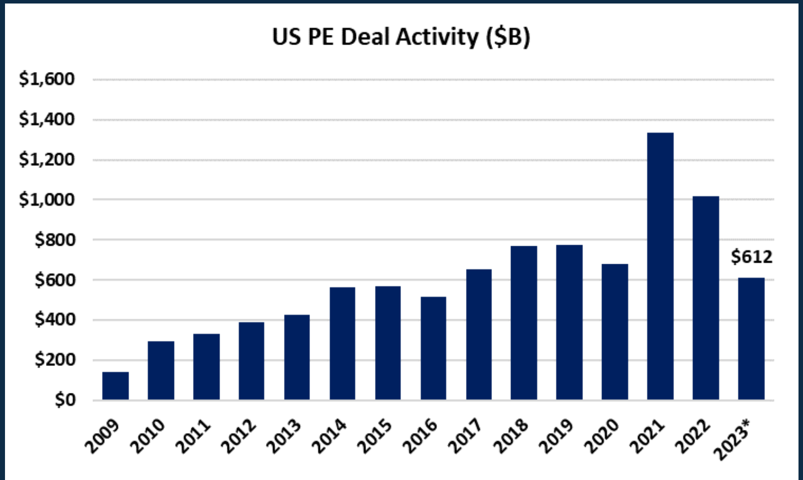
* Data as of 30 September 2023

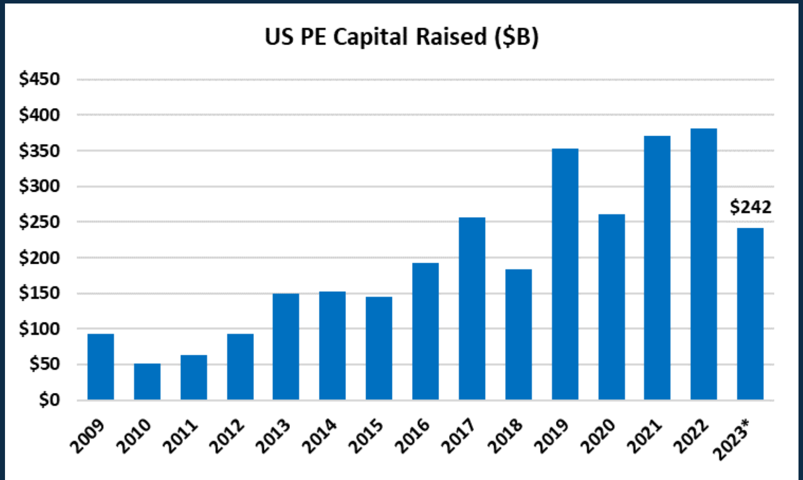
Sources: Pitchbook, SECOR.

Deal Activity and Fundraising

- **PE deal activity has slipped from 2021-2022's brisk pace but is on pace for ~$800B in 2023.**
  - Platform deal activity, which is more dependent on leverage, has fallen in 2023 while growth-oriented deals have remained strong.

- **Similarly, fundraising activity has also fallen from 2021-2022 levels but remains strong in the longer-term context.**
  - Average time to close a fund has expanded to 16 months in 2023 versus from 11 months in 2020.
  - Middle market funds ($100M to $5B) have accounted for 58% of fund closings in 2023, an increase of 10pp over the average of the prior decade.





Sources: Pitchbook, SECOR.

Credit Update

CLOs

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- Pros: Attractive relative value compared to other structured product and credit sectors
- Cons: Worsening loan fundamentals, rising default rates

- CLO issuance has been low in 2023 – driven by low appetite from AAA tranche investors
- Typically, demand has been driven by US banks and overseas investors – but bank appetite has been lower as they focus on repairing balance sheets, and higher hedging costs have made it less attractive for overseas investors
- 20% of AAAs are held by Japanese investors – rise in Japan bond yield cap has had negative demand impact
- Floating rate debt, so CLO debt not as attractive when rates begin to fall

- CLO equity – has historically outperformed during periods of credit market volatility
- If loan spreads are volatile but default rates remain reasonable, CLO equity can benefit from re-investing at wider spreads
- CLO equity has the right to refinance CLO debt – with debt spreads near historical wides, this is a potentially valuable option
- CLO equity not affected by rate moves – as the % paid to the debt tranches is also floating rate
- Downside scenario would be a worse than expected default cycle, eroding equity returns
- Likely to see low secondary market liquidity for CLO equity, due to macro uncertainty

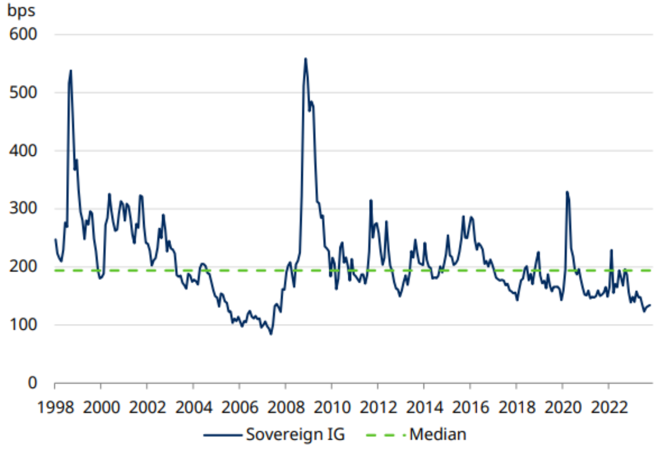
Source: Wellington, Deutsche Bank, Voya

HC EMD Sovereigns

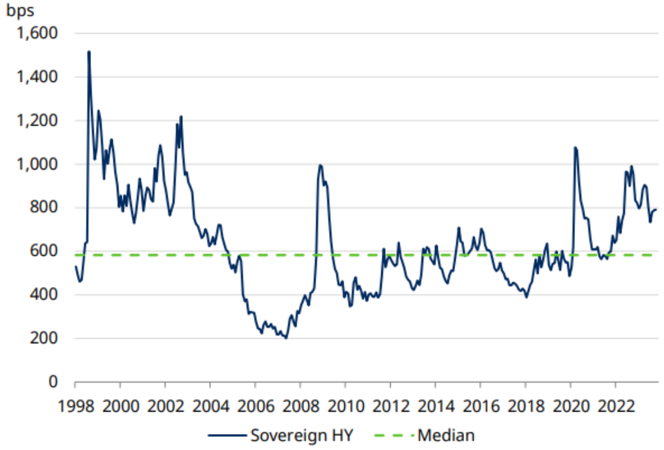
- Yield and spread elevated compared to long-term history
- This is driven by the HY bucket. Spread on IG bucket is close to 15-year lows (partly due to changing index composition)
- Spread dispersion between underlying countries remains wide
- HY HC EMD offers a significant spread pick-up over equivalent rated US HY

	Hard EMD HY	Corporate EMD HY	HY USD
Yield	12.9%	10.5%	9.5%
Spread (bps)	791	553	442
Duration	5.2	3.2	4.1
Rating	B1	B1	B1
Percentage of EMD index	49.9%	40.0%	-

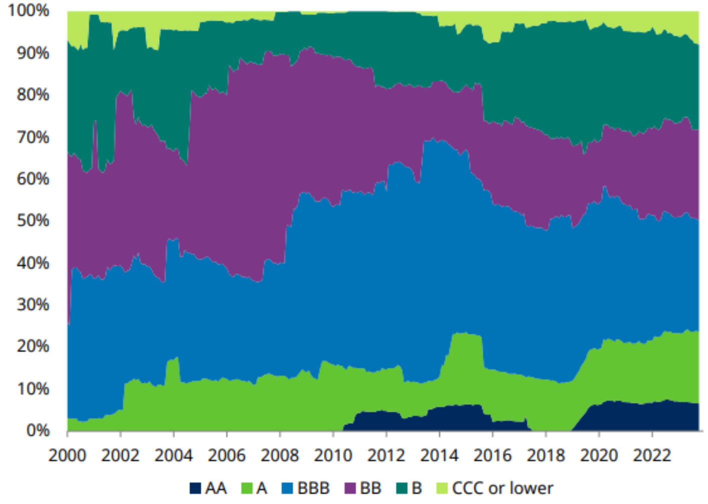
Hard currency sovereign EMD IG spread



Hard currency sovereign EMD HY spread



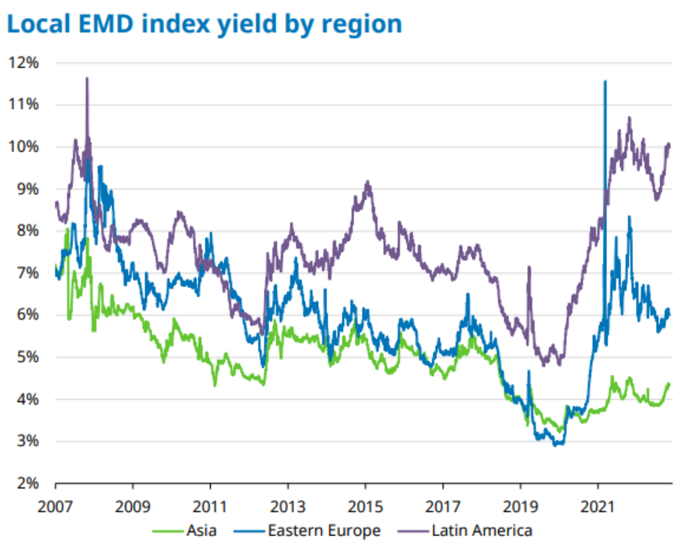
Sovereign EMD ratings split

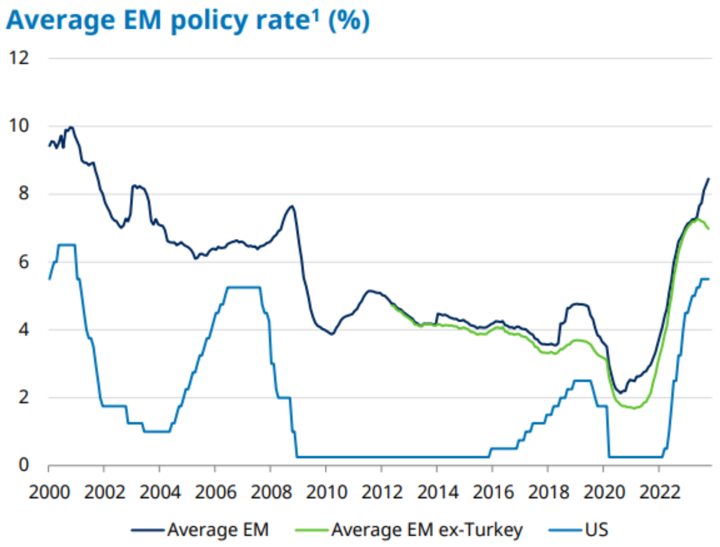


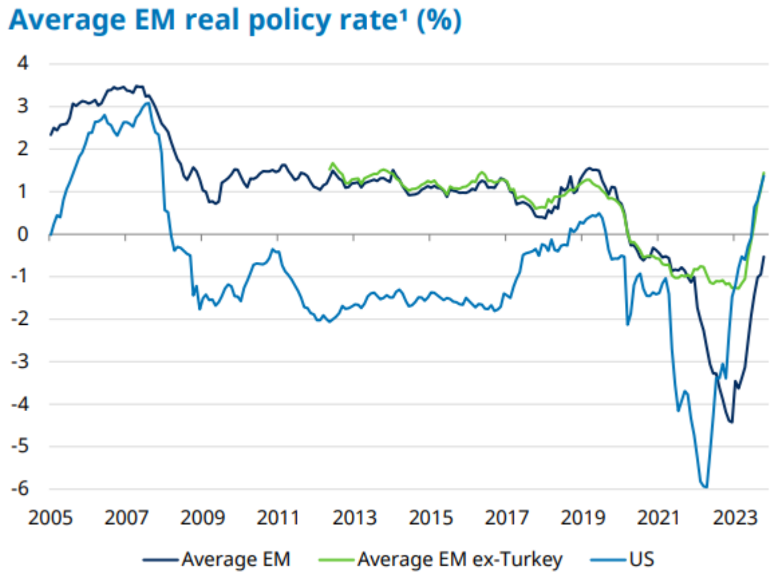
Source: Schroders, JPMorgan, as of 31 October 2023

LC EMD Sovereigns

- EM and DM real yields are both rising. EM real yields are positive, average DM real yield is still negative
- Real yield premium of EM over DM is increasing from a low level
- Significant dispersion in yields by region
- EM FX has depreciated against USD YTD
- There are undervalued currencies in all three regions, but dispersion in degree of undervaluation







Source: Schroders, LSEG Datastream, as of 31 October 2023

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