

Global Limited Partners Survey

2020

*Investor Perspectives on Private
Capital in Emerging Markets*



About EMPEA

EMPEA is the global industry association for private capital in emerging markets. An independent, non-profit organization, the association brings together 300+ firms—including institutional investors, fund managers, and industry advisors—who manage more than USD5 trillion in assets across 130 countries. EMPEA supports its members globally through research and intelligence, investor meetings, education, and advocacy.

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2020 Global Limited Partners Survey

Executive Summary

The 16th annual edition of EMPEA's *Global Limited Partners Survey* features the views of 109 limited partners (LPs) on the current conditions and outlook for private capital in emerging markets (EM). This study aims to shed light on how LP investment plans are evolving and what factors are affecting LP decision-making.

Focus areas for this year's survey include the 🌪️ COVID-19 crisis, policies around climate change and other environmental factors, co-investment and direct investment plans, and venture capital (VC) and technology.

Key Findings

➤ *Pace of LP Commitments*

Given the unprecedented global health and economic crisis, overall commitments to EM private capital funds are expected to decline over the next two years, but will recover in the medium term. Economic conditions and political developments in emerging markets, as well as institutional risk aversion, will be the biggest constraints on additional commitments from institutional investors. Moreover, anticipated distressed opportunities and more attractive valuations in developed markets have changed the risk-return equation for some investors.

➤ *Portfolio Growth & Diversification*

Growing overall private markets portfolios and increased diversification are the biggest drivers of new commitments to emerging markets. Meanwhile, impact and ESG considerations are motivating an increasing share of commercial LPs to invest.

➤ *Climate & Environment*

A majority of LPs are taking climate change and other environmental factors into account when making investment decisions. Though most commercial LPs do not face specific investment restrictions, key stakeholders are pushing for greater consciousness of ESG considerations.

➤ *Co-Investments*

Three-quarters of survey respondents plan to make EM private capital co-investments, and 80% are building internal teams in order to implement this strategy. Standalone direct investments, however, are not being pursued across the board.

➤ *Manager Selection*

LPs are placing greater emphasis on sector expertise for EM fund manager selection. GPs' back-office operations were also prioritized by responding LPs.

➤ *Market Attractiveness*

Southeast Asia and China lead all other markets in perceived attractiveness for EM investment, followed by India. The market attractiveness ranking remains largely unchanged from recent editions of the survey, with Brazil dropping two places.

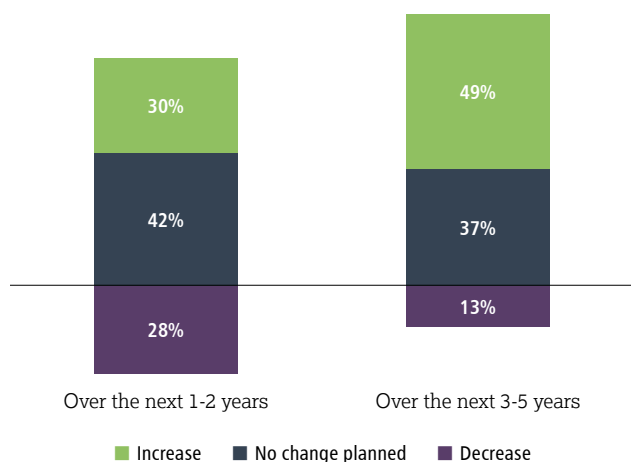
➤ *Venture & Tech*

The proportion of LPs seeking exposure to VC in emerging markets has nearly doubled since 2014, with China and India seen as the most desirable destinations. Fintech, B2B, and health lead all other tech sectors of interest for LPs as VC activity and investors' attention expands beyond consumer internet plays.

Overall LP Commitments to EM Funds Expected to Decline Amidst Unprecedented Global Health and Economic Crisis, with Medium-Term Recovery Anticipated

Responses to EMPEA's 2020 *Global Limited Partners Survey* point to a near-term decline in new commitments to EM-focused private capital funds as the world endures the continued fallout of the COVID-19 crisis. The share of survey respondents (excluding EM-only investors) planning to increase commitments over the next two years has declined from 52% in 2019's survey to 30%. However, 49% of respondents plan to increase commitments over the next three to five years, pointing to a potential rebound as the critical health situation in countries around the world abates and EM economies subsequently recover.

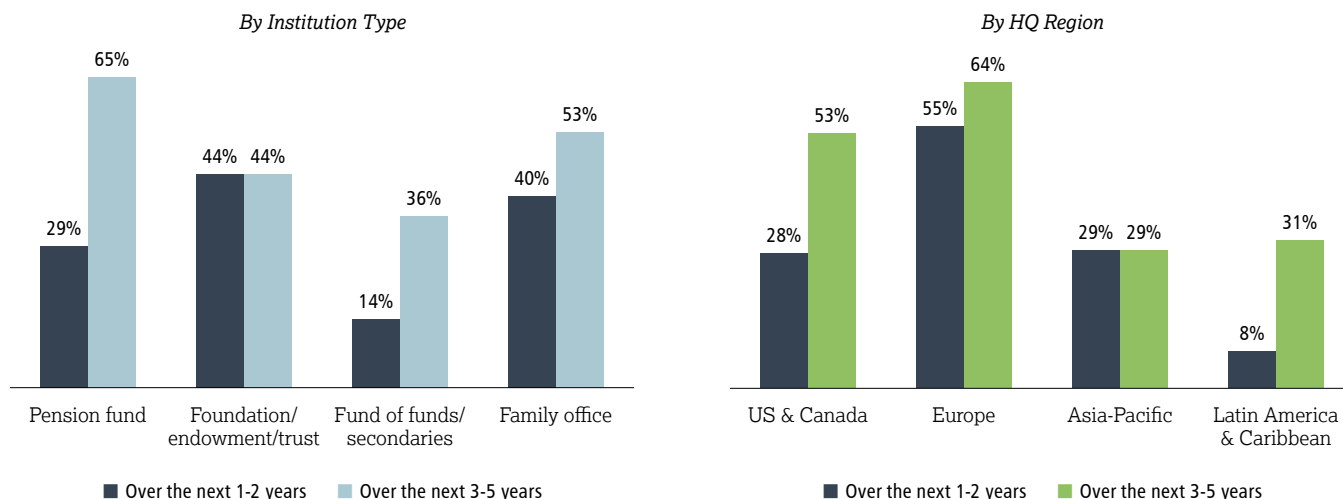
Exhibit 1: Anticipated Level of New Commitments to EM Private Capital Funds*



“ The pipeline of illiquid investments coming into Q1 has been put on ice. We won't likely be seeking liquidity from private equity, but we will also likely not lock up capital there either until we have a clearer picture of the liquidity need[s] of the broader organization.

–Pension fund

Exhibit 2: Share of Respondents Planning to Increase EM Private Capital Commitments*

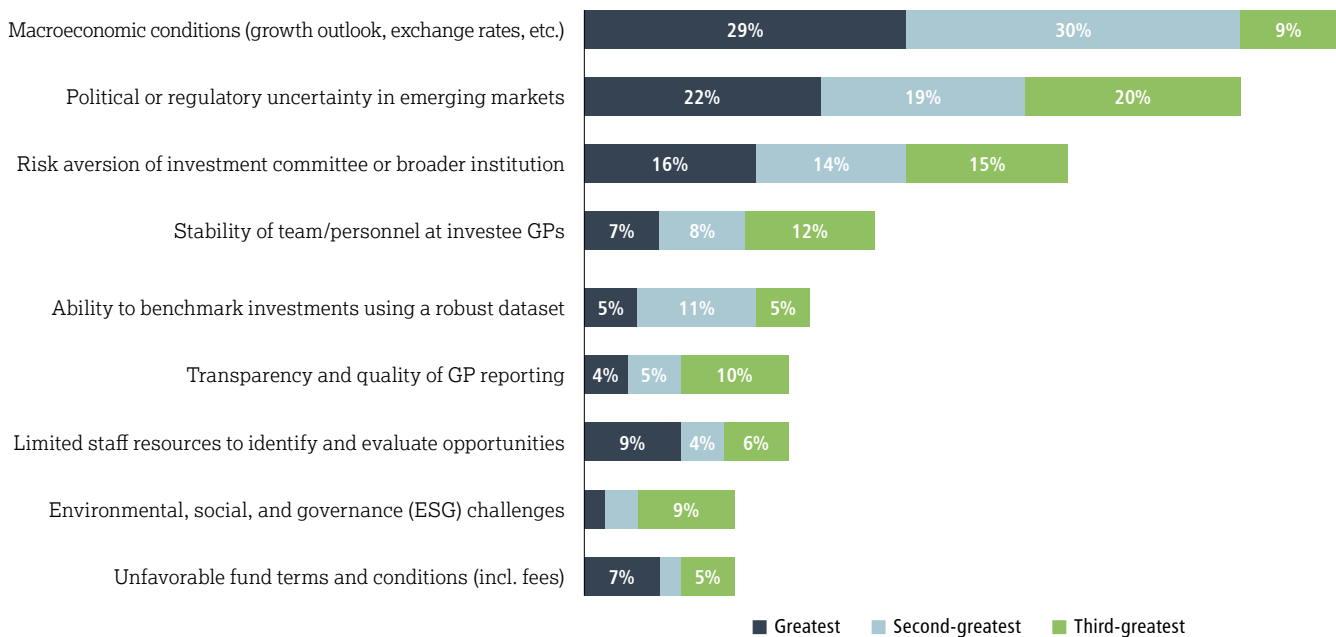


*Excludes institutions with EM-only mandates, including DFIs, EM-focused funds of funds, and others legally mandated to invest in emerging markets.

Overall LP Commitments, continued

Survey responses indicate that pension funds, which must continue to support beneficiaries, and funds of funds, which have their own LPs, are most likely to decelerate the pace of deployment in emerging markets. Geographically, European institutions are most likely to increase new commitments or maintain deployment pace. Overall economic conditions and political uncertainty, which are exacerbated in the COVID-19 environment, will pose the greatest constraints for investors. In addition, investment committees are likely to be exceedingly cautious until more is known about how global markets will recover, though free-form responses point to some optimism and resolve among global LPs.

Exhibit 3: Greatest Obstacles to Allocating a Larger Portion of AUM to EM Private Capital



LP Insights: How LPs Are Evolving in Response to the COVID-19 Crisis

“ We are seeking increased diversification but being highly selective.

–Secondaries investor

“ We’ll commit more capital to private credit funds (as opposed to PE) and play a more significant role in the early-stage/higher-risk impact investing space. We’ll likely back fewer generalist growth equity funds but when we do, we will back with larger checks.

–DFI

“ More investments with peers, more in distressed strategies, more in the US, Europe, and China.

–Family office

“ We are not afraid to allocate to spaces when the rest of the herd is leaving.

–Pension fund

“ No changes [in strategy] resulting from recent world health events.

–Insurance company

Desire for Diversification Drives Additional Commitments to Emerging Markets; More Commercial LPs Targeting ESG and Impact Outcomes

Among LPs planning to increase their commitments to EM private capital in the short or medium term, 66% indicate a need for more portfolio diversification, which is a natural corollary to growing private capital portfolios and overexposure to developed markets, like the US and Western Europe.

A small but growing share of institutional investors cite a desire for greater institutional, social, and economic impact as a driver for increased commitments, led by foundations, endowments, and family offices. Meanwhile, fewer LPs have taken comparative risk-return profiles into account in their decision to expand commitments to emerging markets.

Exhibit 4: LPs' Reasons for Increasing Commitments to or Beginning to Invest in EM Private Capital Funds*

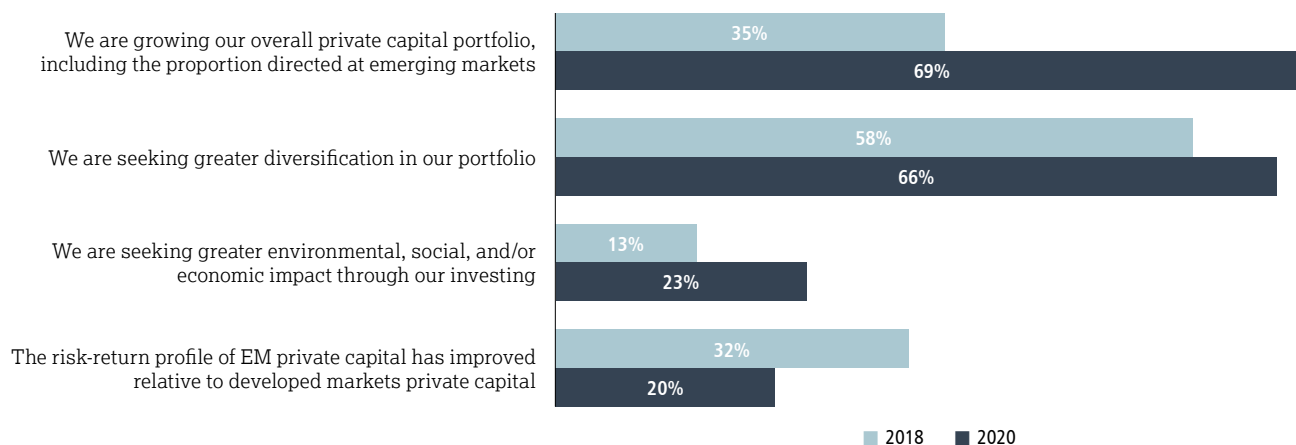
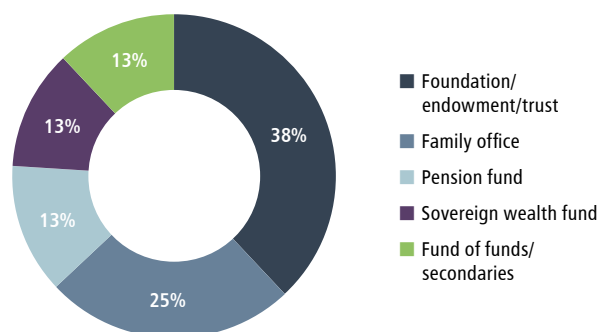


Exhibit 5: Distribution of LPs Citing Impact as a Reason for Increasing Commitments to EM Private Capital*



*Excludes investors with EM-only mandates.

“ In recent years, we have been actively divesting our public stock portfolio in developed markets to increasingly focus on private capital in emerging markets for social/charitable purposes.

–Family office

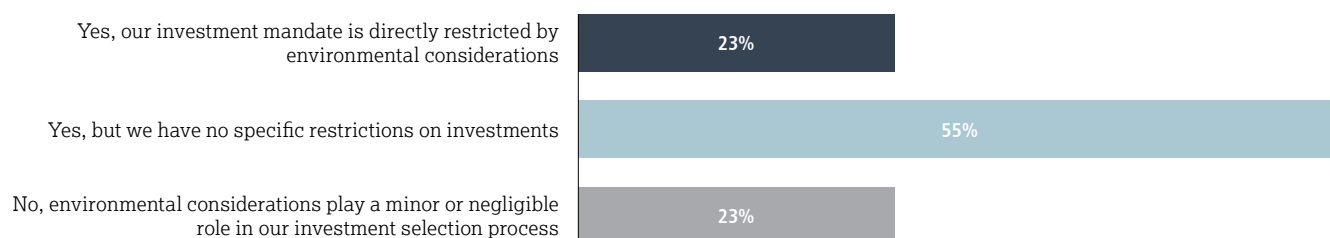
“ We have signed up for the UNPRI, so our whole portfolio will be guided towards ESG/responsible investing/impact investing.

–Family office

Majority of LPs Take Climate Change and Other Environmental Factors into Account When Making Investment Decisions

Climate change and environmental considerations have never been more prominent in conversations throughout the global investment community, not just among DFIs. Over three-quarters of commercial LPs participating in this year's survey cited taking such factors into account when making investment decisions. While most LPs do not yet face specific restrictions on their allocation choices, a multitude of factors—including pressure from boards and beneficiaries and increasing evidence of ESG's role in positive investment outcomes—has generated significant momentum behind sustainable investing.

Exhibit 6: Commercial Investors – Are Climate Change and/or Other Environmental Considerations Affecting Your Investment Decision-Making and Fund Selection Process?



Note: Excludes DFIs and government agencies with an explicit mandate to pursue economic development and social impact.

LP Insights: Perspectives on Climate Change and Sustainable Investing

“ We’ve divested from coal, liquid oil, and gas and are in the process of letting legacy, illiquid oil and gas investments run off of our books. While our stakeholders appreciate this for environmental reasons, we also generally dislike the risk profile (somewhat idiosyncratic; it’s hard to underwrite the oil price five years from now compared to, say, an enterprise software company) and the long-term secular outlook for these investments.

–Pension fund

“ My organization has committed to its shareholders ~10% of assets with impact/additionality, which directly affects decision-making.

–Insurance company

“ There’s a mix of drivers including reputational risk and financial risk related to climate change, and also a growing number of LPs seeking opt-out rights in respect of climate-risk sectors, such as thermal coal.

–Secondaries investor

“ We have no ESG mandate (yet). However, our investment committee does consider ESG. GP practices weigh on our decision-making, mostly from a risk management and exit perspective.

–Endowment

Most LPs Plan to Make EM Private Capital Co-Investments, Building Internal Teams to Fulfill Objectives

Over three-quarters of survey respondents plan to make co-investments alongside GPs in emerging markets over the next two years, tracking a long-term trend of increased desire for direct exposure. Even as fund commitments will continue to account for the majority of capital deployed by LPs in EM private capital opportunities, a majority of respondents across institution types—with the exception of endowments and foundations—are looking for co-investment opportunities.

Most respondents are staffing internal investment teams to fulfill these plans, with just a small share employing outside consultants or setting up additional offices. Relatively few LPs are pursuing standalone direct investments, as only a small number of institutions have the ability and mandate from stakeholders to invest in sourcing and performing due diligence on such deals internally.

Exhibit 7: Distribution of LPs' Planned EM Private Capital Commitments (Median and Interquartile Range)

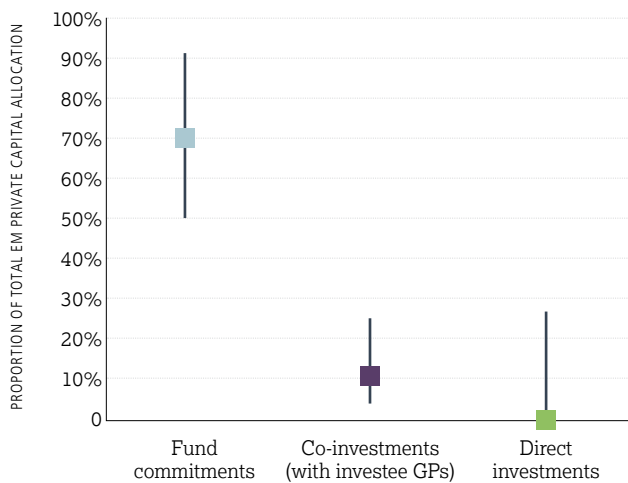


Exhibit 8: Proportion of LPs Planning to Make EM Private Capital Co-Investments and Direct Investments Over the Next Two Years

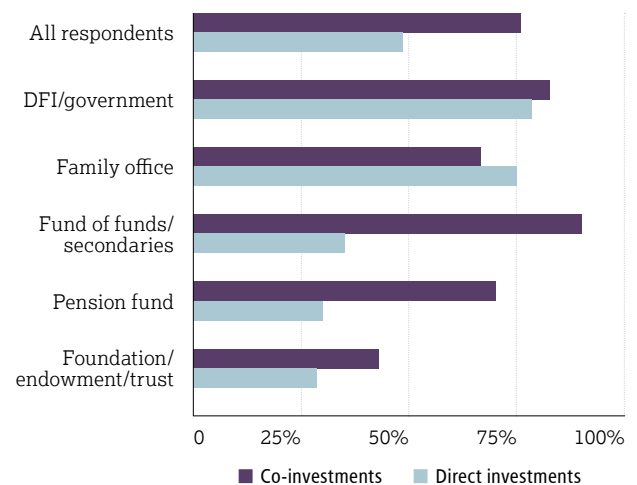
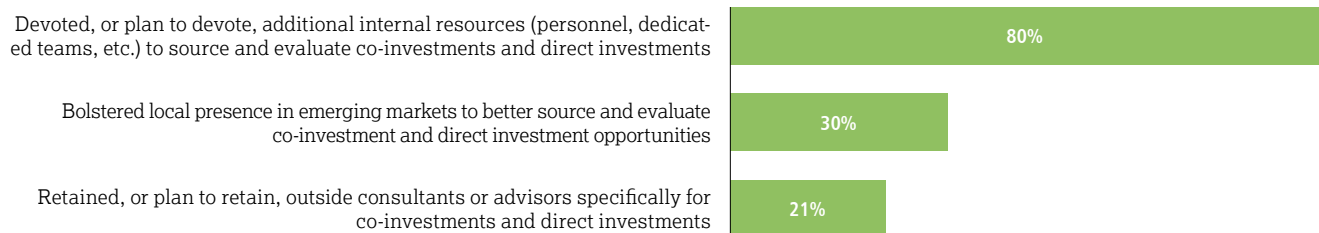


Exhibit 9: Actions Taken to Fulfill Co-Investment and Direct Investment Objectives



Sector Expertise and Back-Office Operations Increasingly Important in Fund Manager Selection

As in past surveys, performance remains the most important factor for LPs in choosing managers, but this year's survey results point to the increasing relevance of deep sector expertise and strong back-office operations. The share of respondents indicating sector expertise as a 'very important' factor in manager selection has increased from 49% in 2019 to 63% in 2020. For back-office operations, the share has increased from 27% to 35%. With fundraising efforts likely to be impacted by the 🦠 COVID-19 crisis, it is critical for GPs to demonstrate a strong foundation across these areas.

Exhibit 10: Important Factors in Evaluating an EM PE Fund Manager

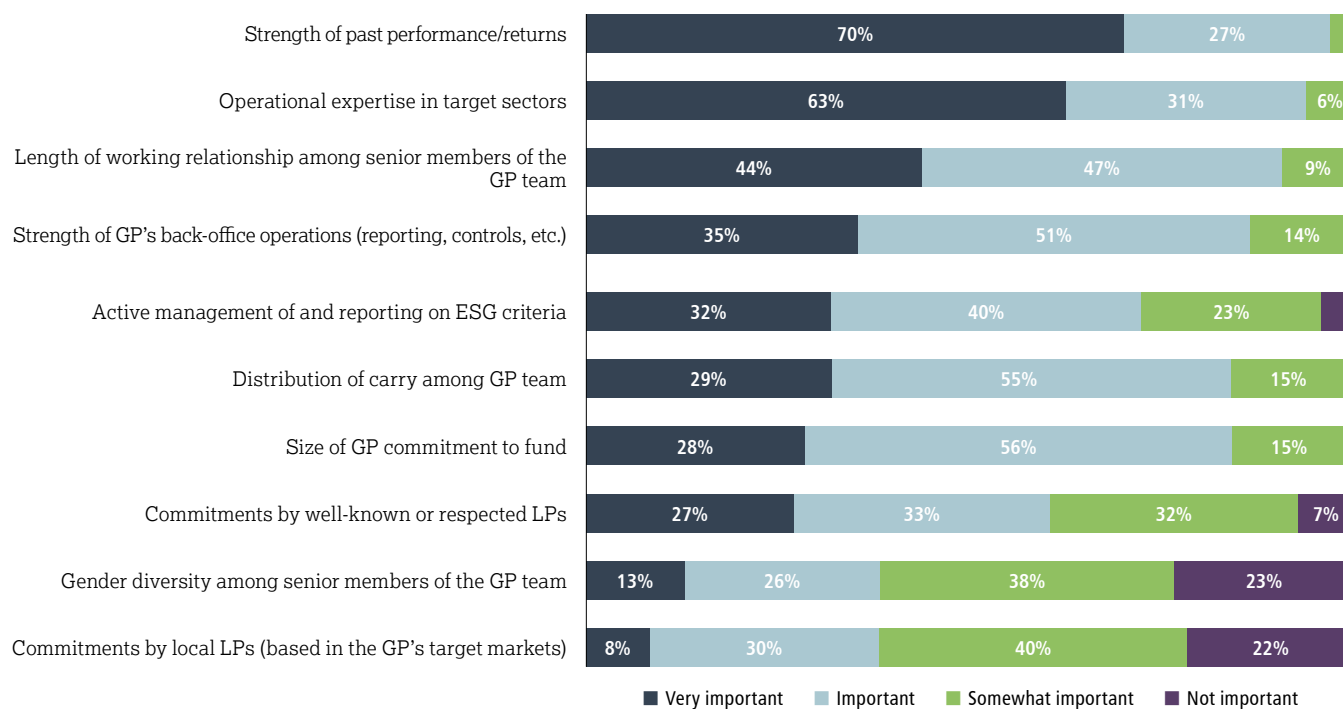
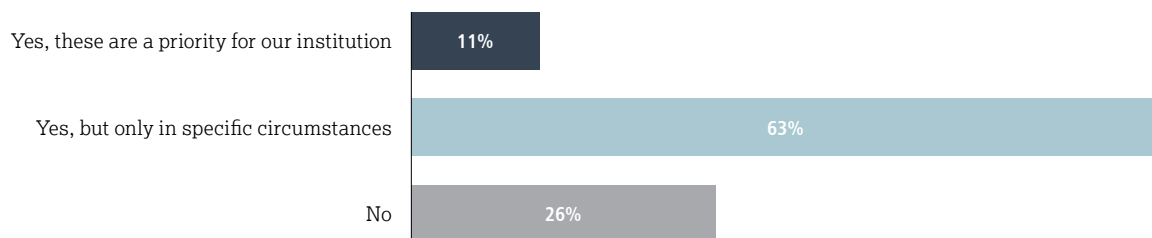


Exhibit 11: Does Your Institution Currently Invest, or Plan to Invest, in New GP Teams?



Southeast Asia and China Lead All Other Markets in Perceived Attractiveness for Investment

Asian markets continue to lead EMPEA's annual market attractiveness ranking. China was the initial epicenter of the COVID-19 crisis, but in the 2020 survey, it has matched Southeast Asia in perceived attractiveness for investment over the next 12 months. Latin America (excluding Brazil) climbed two spots to tie Africa in fourth position, while Brazil has fallen to sixth in the ranking.

Exhibit 12: The Attractiveness of Emerging Markets for Private Capital Over the Next 12 Months

Market	Overall Ranking			Attractiveness Index
	2020	2019	YoY Change	
Southeast Asia	1=	1		47.5
China	1=	2	+1 ↗	47.5
India	3	3		45.6
Africa	4=	5	+1 ↗	37.3
Latin America (excl. Brazil)	4=	6	+2 ↑	37.3
Brazil	6	4	-2 ↓	31.0
Central and Eastern Europe	7	7		24.5
Middle East	8	8		20.4
Turkey	9	9		13.3
Russia/CIS	10	10		4.9

Note: The index (or raw scores) used to compile EMPEA's market attractiveness ranking are calculated by assigning a numerical value to each limited partner's response regarding the attractiveness of each market. A score of 100 reflects a response of 'Very Attractive', 50 of 'Attractive', and 0 of 'Unattractive'. The scores included in the chart above reflect the mean of all survey responses.

LP Insights: Views on Emerging Markets in Light of COVID-19 Crisis

“As we enter a recessionary climate and company valuations decline, there will be potential buying opportunities, but this may not be within the next 12 months, especially if the recovery is more W-shaped than V-shaped.”

–Fund of funds

“We feel that China and India are poised for continued growth in the private market space.”

–Insurance company

“Given the coronavirus, we are going to see deterioration in valuations. Good investment opportunities could arise.”

–Pension fund

Exhibit 13: Factors Likely to Deter LPs from Investing in Individual EM Countries/Regions Within the Next Two Years

	Already at recommended exposure	Historical performance	Limited number of established fund managers	Oversupply of funds (too competitive)	Scale of opportunity to invest is too small	Entry valuations are too high	Weak exit environments	Challenging regulatory/tax issues	Prefer exposure via other asset classes	Political risk	Currency risk
Africa	14%	37%	39%	0%	26%	11%	42%	21%	16%	53%	40%
China	27%	7%	0%	15%	5%	5%	5%	24%	20%	37%	15%
India	27%	21%	8%	2%	6%	13%	17%	17%	25%	19%	33%
Southeast Asia	21%	29%	21%	6%	12%	3%	15%	9%	29%	24%	35%
Russia/CIS	10%	15%	24%	0%	15%	0%	22%	26%	15%	66%	34%
Turkey	10%	13%	23%	0%	20%	3%	21%	13%	18%	59%	48%
CEE	15%	10%	25%	0%	19%	6%	15%	8%	33%	25%	15%
Brazil	24%	16%	16%	2%	12%	4%	12%	8%	22%	31%	47%
LatAm (excl. Brazil)	24%	20%	22%	0%	14%	2%	22%	6%	18%	43%	43%
Middle East	10%	16%	26%	3%	29%	5%	24%	18%	21%	53%	27%

Note: Indicates percentage of respondents answering for each region/market.

LP Insights: Views on Emerging Markets in Light of 🦠 COVID-19 Crisis

“ The debt burden of companies is smaller in emerging markets. At the end of the day, all these countries will be impacted by the global pandemic, and we have to assess in a few months which country/region will be able to recover and what businesses will survive and prosper.
–Fund of funds

“ Due to subdued fundraising, there is less dry powder in emerging markets, as well as devalued currencies and deep-value opportunities due to levered situations.
–DFI

“ Valuations will reset given the COVID-19 global crisis.
–Foundation

Proportion of LPs Seeking Exposure to VC in Emerging Markets Has Risen Since 2014, Though Commitments May Slow in COVID-19 Era

Venture capital accounts for just 13% of the average survey respondents' total current EM private capital commitments, but EM VC fundraising (excluding China) reached a new high in 2019, according to EMPEA data, and the share of survey respondents planning to begin or expand investing in EM VC opportunities has grown since 2014.

Notably, as documented in EMPEA's inaugural *Trends In Global VC+Tech* report, Africa, Latin America, Southeast Asia, India, and CEE & CIS set new highs in venture investment activity in 2019.

However, compared to 2018, a slightly smaller share of respondents in this year's survey intend to begin or expand investing in EM VC. The decline may reflect an anticipated retraction in overall commitments due to COVID-19 rather than muted enthusiasm for EM tech ecosystems. Of respondents that anticipate increases in their total EM private capital allocations in the next two years, half plan to begin or expand VC commitments.

Exhibit 14: Average Distribution of EM Commitments Among All Private Capital Strategies

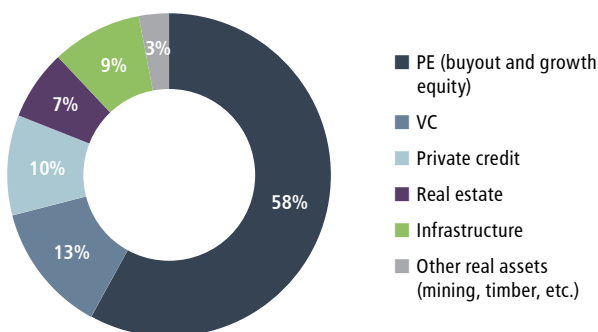
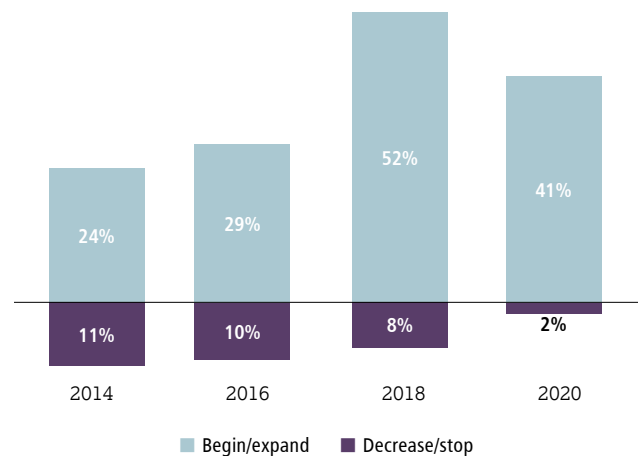


Exhibit 15: LPs' Anticipated Changes to EM VC Investment Plans Over the Next Two Years



LP Insights: What's Needed to Support the Continued Growth of EM VC Ecosystems

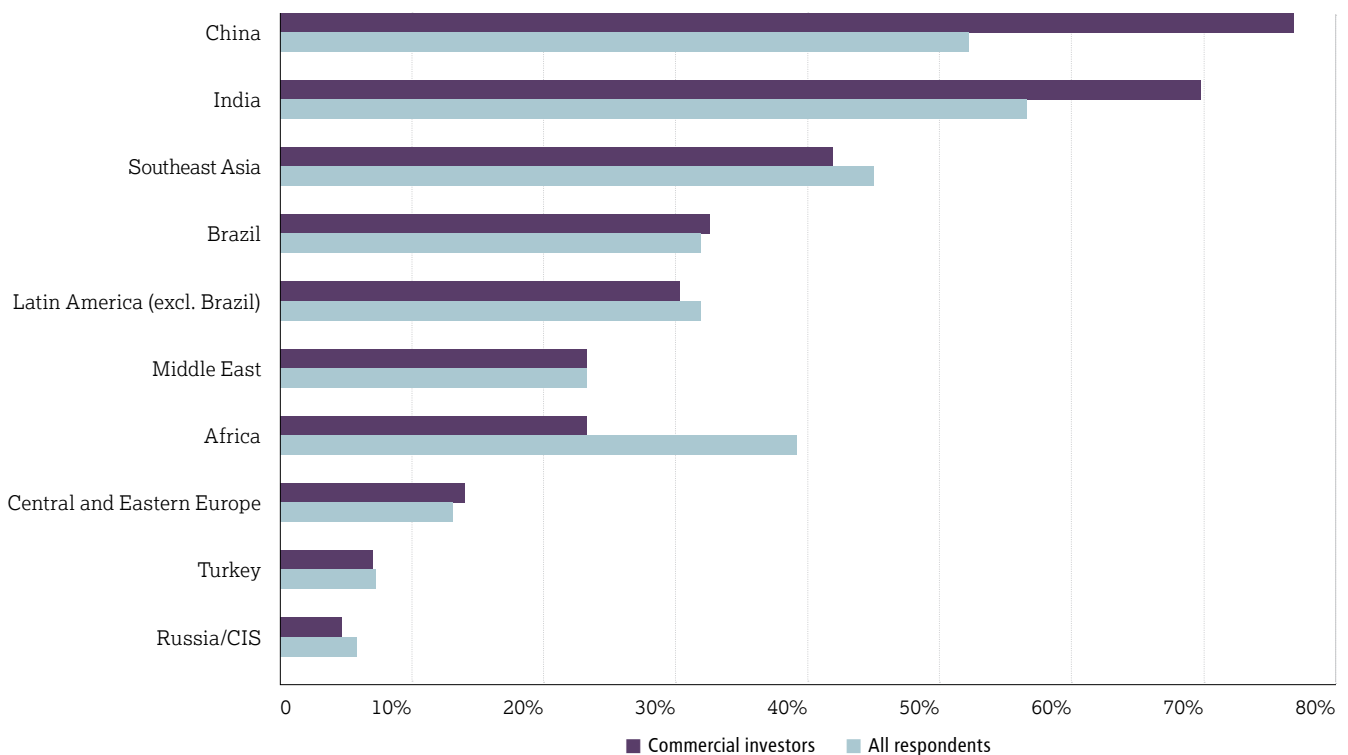
“ Greater participation of global VC for follow-on rounds.
–Fund of funds

“ Attractive exits either through meaningful M&A or successful IPOs.
–Foundation

Commercial LPs Targeting VC in China and India, Followed by Southeast Asia and Latin America

China and India lead other emerging markets in the share of commercial institutions currently investing or planning to invest in VC opportunities, at 77% and 70%, respectively. Their position reflects vast domestic consumer bases and a longer history of institutional VC activity. However, tech ecosystems in Southeast Asia and Latin America are growing rapidly. Meanwhile, early-stage tech activity in markets like Africa is also rising, albeit from a low base, with funds targeting Africa benefitting from additional support from DFIs and local investors, as seen in the higher share of investors currently investing in African VC among all survey respondents.

Exhibit 16: In Which of the Following EM Geographies Do You Currently Invest, or Plan to Invest, in VC Opportunities?



Note: 'Commercial investors' excludes DFIs and government agencies with an explicit mandate to pursue economic development and social impact, as well as investors mandated to invest in only one specific EM geography.

LP Insights: What's Needed to Support the Continued Growth of EM VC Ecosystems

“ Adoption of software and AI solutions to compete with the West.
–Family office

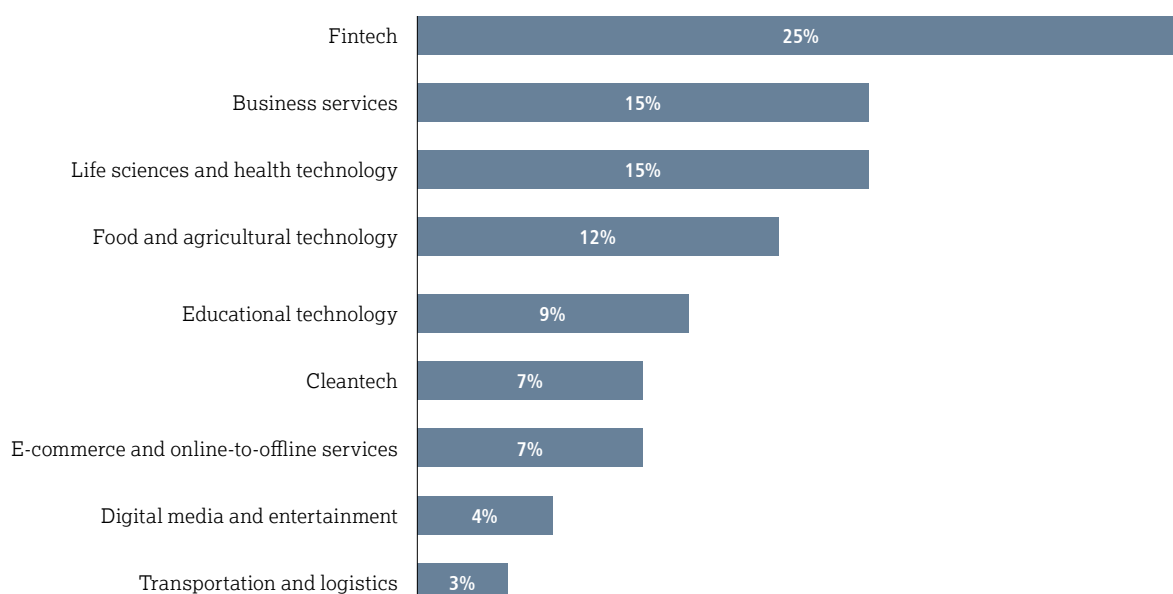
“ Robust capital markets to provide exit opportunities.
–Endowment

Fintech, B2B, and Health Lead Tech Sectors of Interest for LPs

LPs participating in this year’s survey are most interested in gaining exposure to fintech—followed by business services (including enterprise software) and life sciences and health technology—in their target geographies.

Despite accounting for 20% of the USD117 billion invested via VC deals in emerging markets since 2015, e-commerce ranks relatively low amongst LPs’ desired sector exposures. As tech ecosystems across emerging markets mature, LP preferences are shifting away from a concentration in e-commerce and consumer marketplaces to a more diverse set of technology sectors.

Exhibit 17: Technology Areas in Which LPs Are Most Interested in Gaining Exposure



Note: ‘Business services’ includes enterprise software, cloud computing, etc. ‘Cleantech’ includes renewable power and energy storage.

LP Insights: What’s Needed to Support the Continued Growth of EM VC Ecosystems

“ More institutional investors; more flexible financial products to support entrepreneurs; better network connections with Western Europe and the US; more fund managers in the Series B+ space.

–DFI

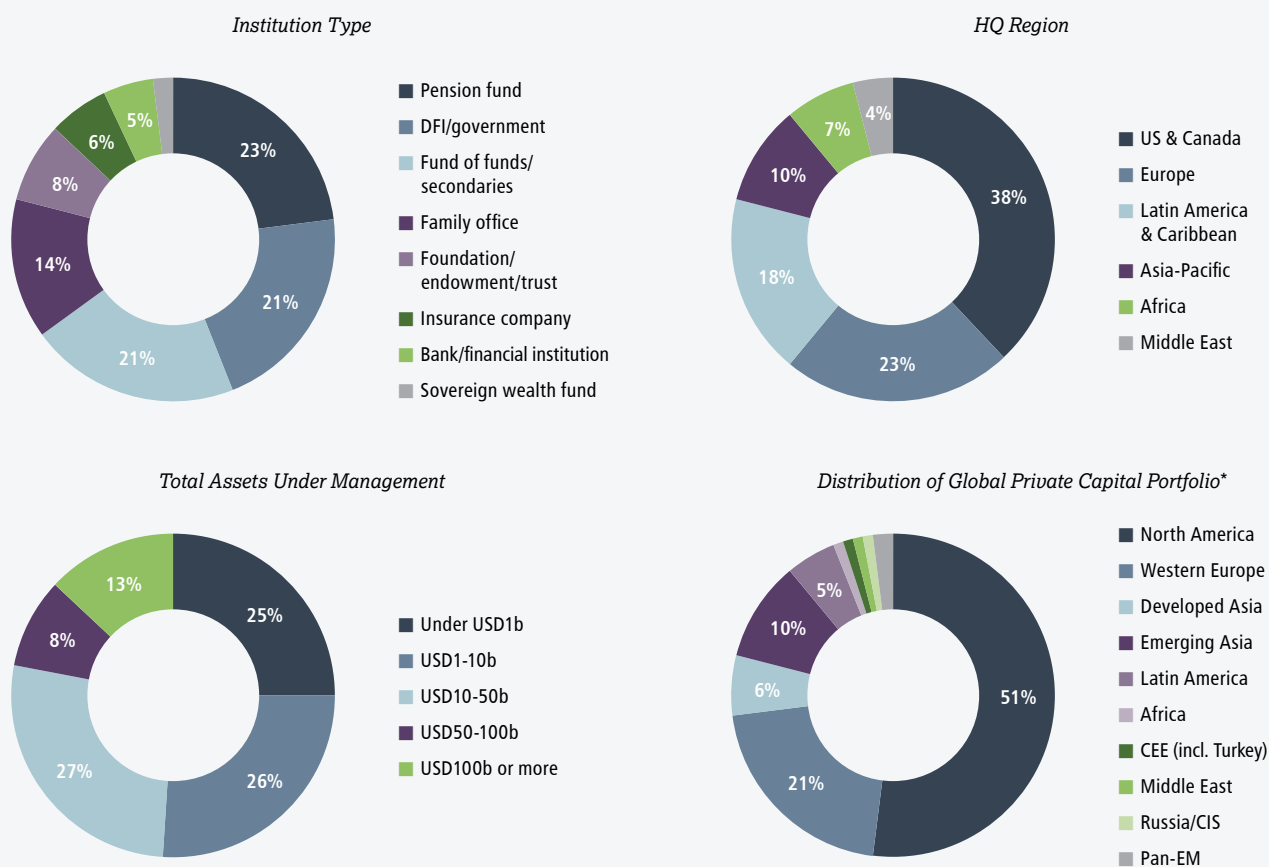
“ Local seed and angel capital; government support, but not government capital.

–Pension fund

Respondent Profile and Survey Methodology

From February to April 2020, EMPEA surveyed 109 limited partners (each from a unique institution) to gather their views on private capital in emerging markets. The survey period coincided with the onset of the global COVID-19 crisis. Pension funds represented the single largest category of respondents, followed by DFIs and funds of funds, with the balance consisting of family offices, foundations, endowments, banks, insurance companies, and sovereign wealth funds. Participants are based in 33 different countries and collectively represent approximately USD4.7 trillion in total assets under management (AUM). EM investments constitute 21% of the average surveyed institution's overall private capital portfolio (excluding DFIs, EM-focused funds of funds, and others mandated to invest exclusively in emerging markets).

Exhibit 18: Profile of Respondents



*Excludes investors with EM-only mandates.

Survey Definitions

Emerging markets ('EM') include all countries outside of the United States, Canada, Western Europe, Israel, Japan, Australia, and New Zealand.

Private capital includes all illiquid alternative strategies, including private equity ('PE'), venture capital ('VC'), private credit, infrastructure, real estate, and other real assets.

Limited partners ('LPs') are investors in private capital funds.

General partners ('GPs') are private capital fund managers.

Development finance institutions ('DFIs') are government-backed or multilateral financial institutions that promote private sector development in emerging and frontier markets.

Note: In some exhibits, percentages may not sum due to rounding.

