GENERALI INVESTMENTS

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OUTLOOK FOR PRIVATE MARKETS:
A NEW ERA FOR PRIVATE DEBT AND INFRASTRUCTURE

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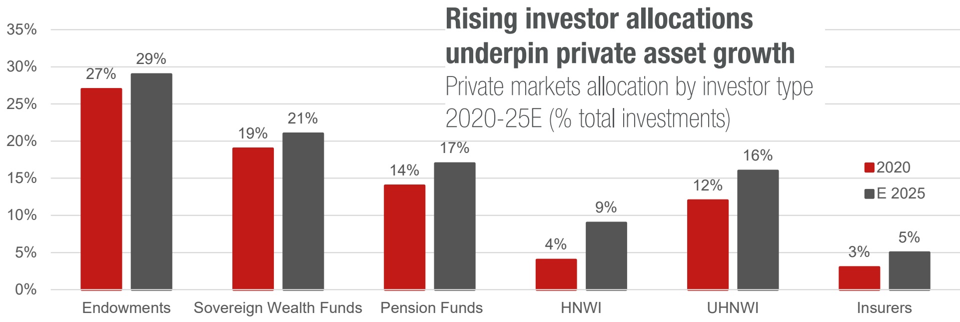

Source: Morgan Stanley, October 2022

We are at the threshold of a new era for investment opportunities in private debt and infrastructure, despite short-term macro headwinds, explains Roberto Marsella.

Private markets remain set for long-term growth

As of 2023, the private markets industry faces some challenging macroeconomic conditions. Higher interest rates, recession concerns, inflation, and tightening financial conditions are raising questions about the risks and durability of momentum in the industry. Short-term headwinds naturally arise when such a rapid increase in interest rates occurs, leading to market dislocations as recently seen in the case of the SVB and Credit Suisse banking failures.

However, it is expected that once private markets adjust to this uncertainty, growth will resume. Morgan Stanley projects the industry to grow from $10 trillion to $17 trillion in AUM over the next five to six years, which is a compound annual growth rate of 12%. One key contributing factor to this is the industry's ability to attract highly talented young professionals who are eager to transform and innovate in private markets, be it private equity, private debt, or infrastructure. This ability to attract young and motivated professionals is crucial to the long-term success of the industry.

An important point for investors to note is that adjustments in private markets generally lag the public markets, with private debt typically repricing a little faster than private equity. So, in the short term, rapid repricing can impact the momentum of private markets growth. The key issue is always the extent to which institutional investors can tolerate illiquidity. Institutional investors have a limit to how much illiquidity they can tolerate, which changes over time and institution by institution. However, the illiquidity premium that comes with investing in private markets remains a key benefit. This illiquidity premium was temporarily compressed but has since re-emerged. As such, private markets are expected to remain attractive for the foreseeable future.

This secular growth thesis is underpinned by the increase to private market allocations across the entire spectrum of investor types, including sovereign wealth funds with a projected 21% by 2025, up from 19% in 2020 (see Chart). This is driven by the intrinsic characteristics of real assets and private markets, such as the opportunity for portfolio diversification due to a low correlation with liquid markets and a good degree of inflation hedging and value reserving. In the specific case of sovereign wealth funds, accessibility is key: investing in private markets enables sovereign wealth funds to access a range of sectors and geographies that they would otherwise be unable to unlock.

Sustainable and renewable energy: The changing face of infrastructure

Higher uncertainty regarding cash flows in the current financial environment is a key challenge for Generali and other institutional investors to navigate. So where do we see risks and opportunities in the private markets landscape today?

KEY TAKEAWAYS

- Private markets typically lag public markets, so we expect that once the sector recalibrates to macro uncertainty, growth should resume
- Infrastructure that addresses sustainability and decarbonisation continues to attract capital
- Private debt is an increasingly attractive credit source for SMEs, while private equity remains attractive on a long-term basis

Our [infrastructure] strategies aim to address major societal challenges such as the energy transition, green mobility, digital transition and improvements to social infrastructure. ”

Firstly, we are excited about the enormous potential of infrastructure investing, an asset class that continues to attract capital due to its ability to provide stable cash flows, less correlated returns and a hedge against inflation[1]. In particular, revolutions in energy, mobility and digitisation are currently at the forefront of geopolitical considerations and are changing the face of infrastructure investing, which since the GFC has gradually shifted from traditional infrastructure to a wider definition, in which renewables are a key component.

Crucially, decarbonisation requires vast amounts of new infrastructure and will not be achieved when existing assets simply change hands. Substantial capital spend is not only required for new renewable generation capacity, but also for power grid improvements and energy storage solutions that are vital to the delivery of clean, flexible, and reliable power.

At Generali Investments Partners, we offer distinct private debt and private equity strategies that target sustainable infrastructure and renewable energy infrastructure. Our strategies aim to address major societal challenges such as the energy transition, green mobility, digital transition and improvements to social infrastructure. Indeed, our entire infrastructure product range is Article 8 or 9 under SFDR regulation, with ESG or sustainability at the core of the investment process[2].

> SMEs are the backbone of the European economy, representing 99% of all businesses and accounting. ”

A new era for private debt

In the short term, private debt and infrastructure are likely to have a more favourable outlook than private equity, where deal-making, exits and fundraising have slowed somewhat due to macro forces. However, in the long term, private equity remains highly attractive for long term investors. The extraordinary growth of the private equity universe continues apace at the same time as going public decreases in appeal, allowing more companies to remain private for longer.

Finally, we are positive on the outlook for private debt. The current unfavourable macroeconomic conditions, the continued deterioration of the banking sector, and the trend towards increased regulation should continue to favour private debt as an increasingly attractive credit source of choice, especially for SMEs that may suffer the most from these circumstances.

Indeed, we have recently launched a new direct private debt fund that aims to invest in SMEs in continental Europe that are willing to commit to ESG objectives[3]. The fund focuses on floating rate, senior secured debt in the most protected part of the capital structure, given the evolution of the market and the challenging macroeconomic environment[4]. SMEs are the backbone of the European economy, representing 99% of all businesses and accounting for more than half of Europe's GDP. This breadth of opportunity allows us to be selective as investors while still providing diversification. As with all funds across our private debt range, the strategy benefits from the co-investment synergies of Generali Group's long-term relationships with external private debt and private equity firms.

PRIVATE MARKETS AT GENERALI INVESTMENTS

Generali Group has long invested into private markets for its own insurance portfolios to enhance portfolio diversification and pursue attractive risk-adjusted returns. Today, we offer other institutional clients this same access to our expertise and capabilities. We have over 85 specialist private markets professionals across the Generali Investments ecosystem of asset management firms, which consolidates our skills across infrastructure, private debt and private equity investments.

As a long-term institutional investor, we expect private markets to continue to grow as an increasingly crucial component of defensive, diversified, and stable portfolios. That's why we're continuously strengthening our capabilities at Generali Investments by hiring new talent, nurturing existing talent, and expanding our offering of direct and indirect strategies.

€67.3
BILLION IN AUM

480
ASSET MANAGERS AND SPECIALISTS

#13
SFDR ART. 8/9 CLASSIFIED FUNDS

Source: Generali Investments Holding S.p.A., data as of Q4 2022. Please note the data include Generali Investments Partners S.p.A. Società di gestione del risparmio, Generali Real Estate S.p.A. Società di gestione del risparmio, Infranity which are part of Generali Investments Platform. [1] Investments bear risks. You may not recover all of your initial investment. Investment may lead to a financial loss as no guarantee on the capital is in place. [2] This communication does not relate to these funds which may not be available for distribution in your country. [3] This communication does not relate to this fund which may not be available for distribution in your country. [4] Investments bear risks. You may not recover all of your initial investment. Investment may lead to a financial loss as no guarantee on the capital is in place.