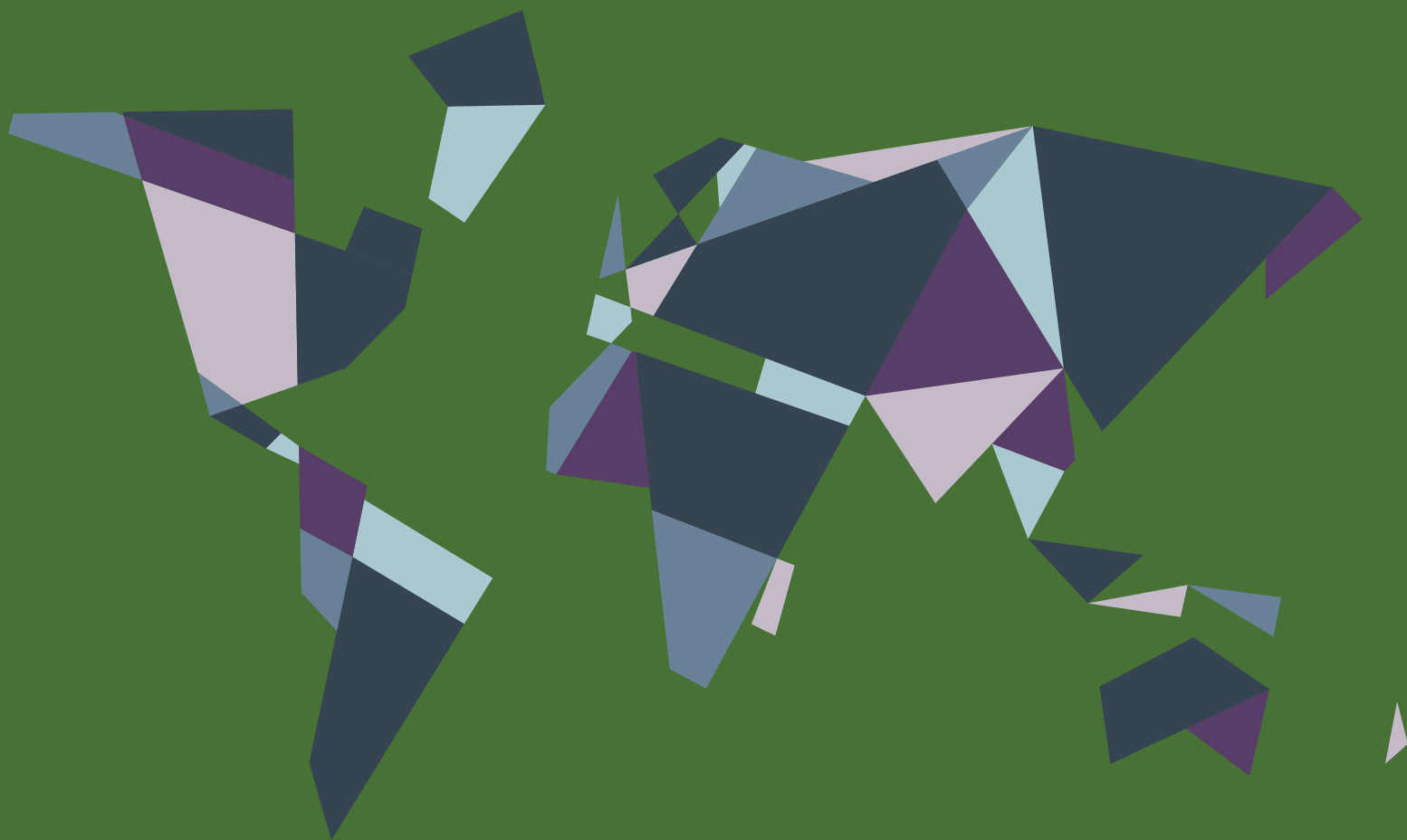


# Global Limited Partners Survey

Investors' Views of Private Equity  
in Emerging Markets

2018



## 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 US\$5 trillion in assets across 130 countries. EMPEA members share the organization's belief that private capital can deliver attractive long-term investment returns and promote the sustainable growth of companies and economies. EMPEA supports its members globally through authoritative research and intelligence, conferences, networking, education and advocacy.

### Editor

Jeff Schlapinski, *Director, Research*

### Lead Contributor

Rae Winborn, *Manager, Research*

### Additional Contributors

Luke Moderhack, *Manager, Research*

Isabelle Diop, *Senior Research Analyst*

Kevin Horvath, *Senior Research Analyst*

Sabrina Katz, *Research Analyst*

### Production Assistance

Zelnar Zingale, LLC

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2600 Virginia Avenue NW • Suite 500 • Washington, DC 20037 USA  
Phone: +1.202.333.8171 • Fax: +1.202.524.6130 • Web: [empea.org](http://empea.org)

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# 2018 Global Limited Partners Survey

## Executive Summary

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The 14<sup>th</sup> annual edition of EMPEA's *Global Limited Partners Survey* features the views of 107 limited partners (LPs) on the current conditions and future outlook for emerging markets private equity (EM PE). This study aims to shed light on the evolution of LPs' investment plans; the issues affecting their decision-making; their return expectations; the factors that LPs believe will drive future performance; and the geographies, fund strategies and sectors that they view as attractive.

Institutions participating in the 2018 survey include pension funds, development finance institutions (DFIs), funds of funds, private markets advisors, family offices, endowments, foundations, banks, asset managers, insurers, government agencies and sovereign wealth funds. These limited partners are based in 36 different countries, and they collectively represent global PE assets under management (AUM) of approximately US\$358 billion and total AUM of US\$5.7 trillion. Additional details regarding survey respondents are available on page 17.

### Key findings from the 2018 *Global Limited Partners Survey* include:

- A higher proportion of respondents\* plans to increase the dollar value of their commitments to EM PE than in any edition of the survey since 2014, suggesting cautious optimism may be in order for EM-focused fund managers.
- LPs' reasons for increasing their commitments to EM PE appear to be evolving. When asked why they plan to commit more to EM PE opportunities, 58% of survey respondents indicated they are seeking greater diversification in their PE portfolio, up from 38% of respondents in the 2014 survey. In contrast, half of respondents in the 2015 survey planned to increase their commitments because they expected PE to outperform other EM investment opportunities, but the corresponding proportion in this year's survey was just 32%. The latter trend may reflect the strong performance of EM public equities in 2017.
- Reflecting the strong growth in fundraising for EM venture capital and EM private credit documented in EMPEA's *Industry Statistics*, the percentage of LPs planning to begin or expand investing via funds employing these strategies has increased over the last two years.
- While the majority of commercial investors\*\* take environmental and social impact into account when making investment decisions, most do not maintain a dedicated allocation to impact investing opportunities.
- Southeast Asia has regained the top spot in EMPEA's market attractiveness rankings, followed by India and China, forming a top three exclusively comprising markets in Emerging Asia. Despite its relative stability at the top of the rankings, Southeast Asia has failed to attract more capital than many markets ranked much lower, though LPs are likely accessing the region through commitments to pan-Asia funds.
- For the first time, EMPEA asked survey respondents to indicate the return premium that would justify their decision to commit to PE funds focused on various emerging markets. The results reveal that higher levels of perceived political risk and currency risk—as indicated by the percentage of LPs citing these factors as deterrents to investing—are associated with larger return premiums.
- Two-thirds of survey respondents plan to form between one and five new EM PE fund manager relationships over the next three years, in line with last year's findings. The majority of respondents may be pursuing fewer new relationships, but LPs appear more likely to expand commitments to sector-specific and country-dedicated fund managers than to multi-strategy GPs, even though the latter would seem better positioned to absorb commitments from institutions writing fewer, larger checks.
- After declining over the last few editions of the survey, the proportion of respondents indicating that EM PE returns have met or exceeded their expectations increased in 2018. Likewise, the proportion of LPs expecting returns of 16% or more from current-vintage funds increased for both emerging markets overall and for each individual EM geography included in the survey. Despite the year-on-year increase in 2018, over a longer timeframe, return expectations have cooled for all EM geographies except for markets in Emerging Asia.
- Higher fundraising for emerging markets in 2017 may have been driven by US\$1 billion-plus funds, but LPs expect middle-market vehicles in the US\$250 million to US\$499 million range to generate the highest net returns in the 2017 vintage.
- LPs expect GPs' ability to drive operational improvement at the portfolio company level to have the biggest impact on the performance of 2017-vintage EM PE funds, followed closely by overall economic growth in emerging markets and entry multiples. However, despite the perceived importance of operational skills in generating returns, nearly half of survey respondents feel EM PE fund managers' value creation abilities are behind those of their developed market peers.
- E-commerce and fintech represent the most attractive technology areas for investment in emerging markets over the next two years, according to this year's survey respondents.

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

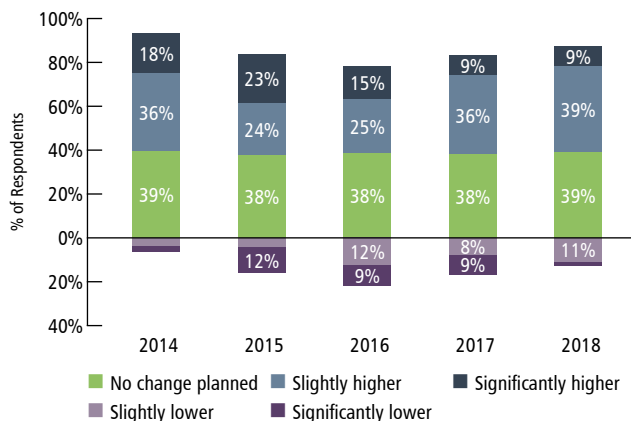
\*\* Excludes DFIs, government agencies and LPs exclusively focused on impact investment opportunities.

# Year-on-year Increases in Planned New Commitments and Allocation Levels Call for Cautious Optimism

The results of EMPEA's 2018 *Global Limited Partners Survey* point to a marginal improvement in overall LP sentiment toward emerging markets private equity. As currencies, economic growth rates and levels of deal activity climb back from recent downturns in many regions, 88% of survey respondents—excluding investors with EM-only mandates—expect to maintain or increase the dollar value of their commitments to EM PE over the next two years. This represents the highest share since the 2014 edition of the survey. Furthermore, the number of investors planning to decrease the pace of their new EM PE commitments dropped slightly from 17% to 13%.

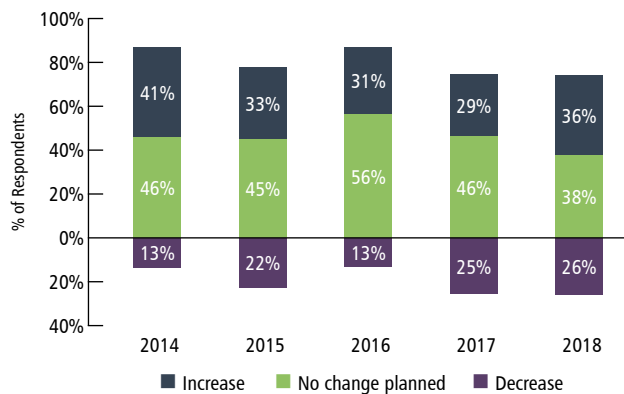
While the number of respondents increasing the dollar value of their new EM PE commitments has risen overall, a breakdown of respondents by PE assets suggests that larger institutions with global PE allocations of more than US\$10 billion appear the most likely to decrease their dollar commitment levels and the least likely to increase them. Conversely, three-quarters of survey respondents with PE assets under US\$100 million plan to increase the value of their commitments to EM PE. The contrast between the larger and smaller ends of the investor spectrum may indicate that less capital overall may flow to emerging markets. On the other hand, it may merely reflect the fact that some large LPs are less likely to increase commitments to EM PE *funds* (specified in the question) and are finding alternative means of deploying capital (see Pages 10-11). At any rate, the influx of interest from smaller investors is likely good news for newer fund managers, which are typically smaller in size.

**Exhibit 1: Anticipated Level of New Commitments to EM PE Funds Over the Next Two Years, 2014-2018\***



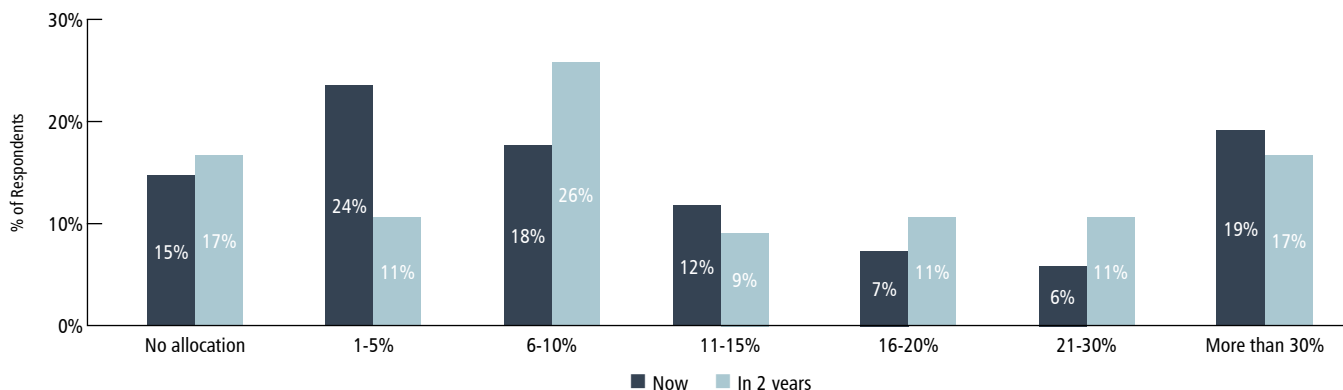
\*Excludes investors with EM-only mandates.

**Exhibit 2: LPs' Planned Changes to Proportion of Total PE Allocation Targeted at EM PE Over the Next Two Years, 2014-2018\***



\*Excludes investors with EM-only mandates.

**Exhibit 3: LPs' Proportion of Total PE Allocation Targeted at EM PE\***



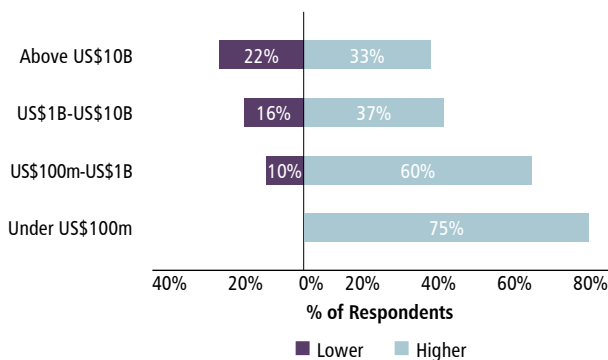
\*Excludes investors with EM-only mandates.

Along with a higher share of LPs maintaining or increasing the *dollar value* of their commitments to EM PE, a higher percentage of respondents plan to increase the proportion of their total PE *allocation* targeted at emerging markets over the next two years. The share of LPs’ planning to increase their allocations has risen from 29% in 2017 to 36% this year. However, 26% of respondents expect to decrease the share of their PE allocation directed at emerging markets, a slight increase from last year’s survey and the highest proportion within the last five years. As EMPEA has previously argued, the findings suggest that even if LPs are putting or intend to put more capital to work in emerging markets, the pace of growth may not exceed that of commitments to alternative investments globally.

The thinking behind LPs’ decisions to begin or increase the value of their commitments to EM PE funds has changed over the last five years. The number of respondents indicating that they expect EM PE to deliver high returns relative to other EM investment opportunities has declined. Most of this drop-off has occurred in the past two editions of the survey, which may reflect the broad gains enjoyed by EM public equities since the beginning of 2017. In contrast, the number of respondents citing greater portfolio diversification or a better risk-return profile relative to developed markets as reasons for increasing their commitment levels has increased. As stories documenting increased competition for PE deals in the United States and Western Europe continue to fill the financial press, some investors may be looking to emerging economies to avoid overexposure to frothy conditions in core markets.

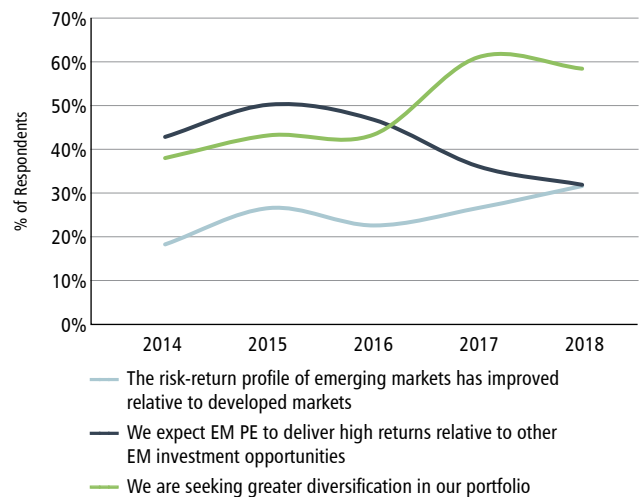
While the improvement in sentiment revealed by LPs’ plans for new commitments to EM PE funds and percentage allocations to EM PE is fairly modest, this may be partially due to the composition of institutions included in this year’s sample. Survey respondents without a current allocation to EM PE accounted for 15% of respondents (excluding EM-only participants), almost double the percentage of previous years.

Exhibit 4: Anticipated Level of New Commitments to EM PE Funds Over the Next Two Years – By PE AUM\*



\*Excludes investors with EM-only mandates.

Exhibit 5: LPs’ Reasons for Beginning or Increasing Commitments to EM PE Funds Over the Next Two Years, 2014-2018\*



\*Excludes investors with EM-only mandates.

“ Emerging markets are attractive compared to the United States, where purchase multiples are high.”

–Family office

“ The more attractive emerging markets possess a combination of large opportunities supported by accommodative political and regulatory bodies. These markets are still very inefficient and provide growth that developed markets do not.”

–Endowment

# Venture Capital and Private Credit Gain Prominence in LPs' Future Investment Plans

For over a decade, EMPEA has tracked the shift in capital raised for EM-focused private capital vehicles from predominantly growth and buyout funds to a broader mix of strategies, including venture capital and private credit. Responses to this year's survey reflect the growing importance of these segments in LPs' investment plans. Over half of respondents (52%) plan to begin or expand investment via venture capital funds over the next two years, more than any other strategy included in the survey. In 2016, the last time EMPEA asked LPs about their investment plans by fund strategy, just 29% of respondents indicated they plan to begin or expand investing in venture capital. Similarly, the percentage of LPs who plan to begin or expand investing in private credit has increased from 40% in 2016 to 47% in this year's survey. EMPEA's fundraising totals mirror this increase in investor interest in credit strategies, with EM private credit fundraising in 2017 surpassing all previous years on record.

While interest in private credit is evident across all types of investors, 72% of DFIs and government agencies indicated they plan to begin or expand investing in private credit, the highest proportion of all institution types. At the other end of the spectrum, banks, asset managers and insurers collectively demonstrated less interest, with only 18% planning to begin or expand investing in EM private credit. Finally, for private credit GPs looking to secure new commitments, the diverse staffing arrangements of LPs in the sample point to the potential difficulty of getting in front of the right decision makers. Across all institutions responding to this year's survey—regardless of whether they maintain set allocations to emerging markets—only 24% have a dedicated private credit division, with the remainder employing private equity, fixed-income or multi-asset class teams to allocate to private credit.

Exhibit 6: Planned Changes to EM PE Investment Plans Over the Next Two Years – Fund Strategies

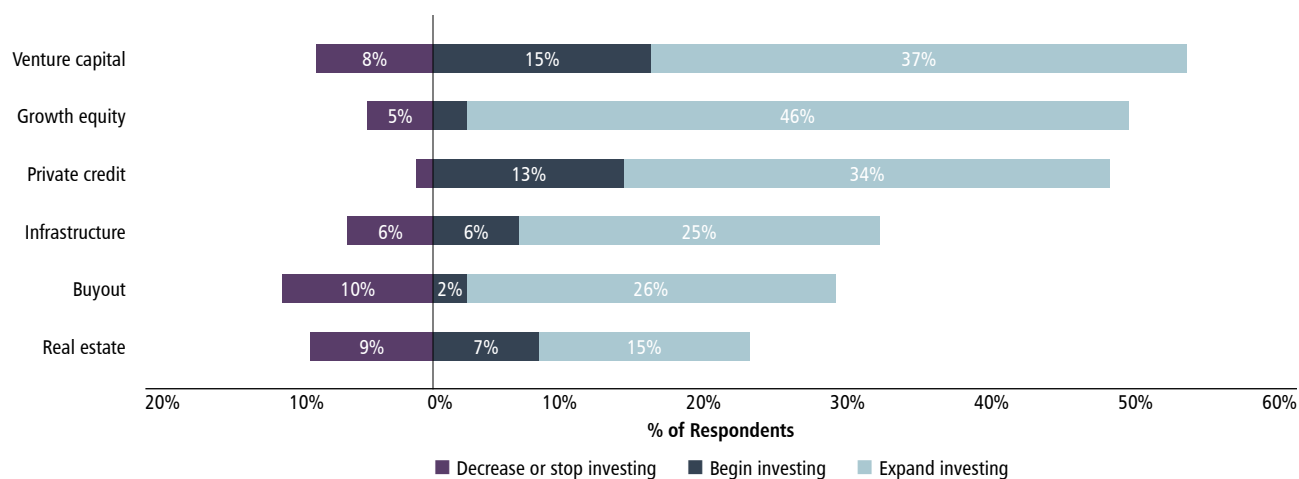


Exhibit 7: Team or Department Responsible for Private Credit Investment Decisions

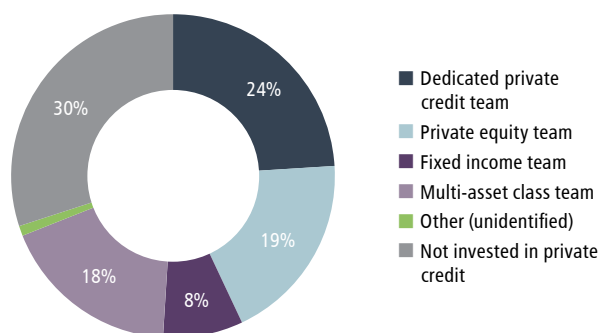
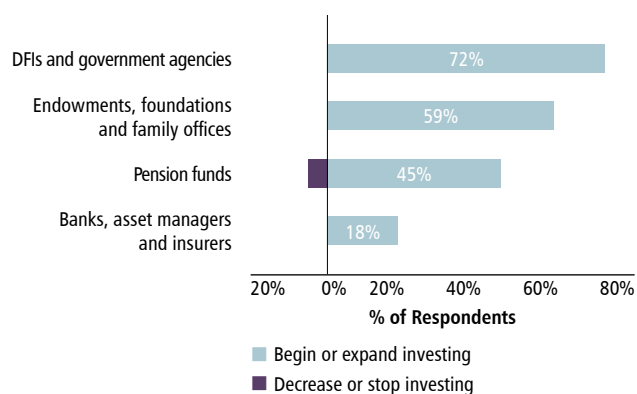


Exhibit 8: Planned Changes to EM Private Credit Investment Plans by Institution Type



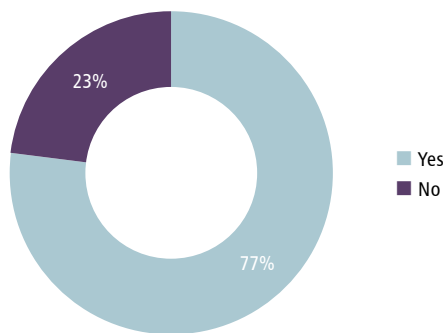
# Most LPs Consider Social and Environmental Impact When Investing, but Dedicated Allocations to Impact Investing Are Much Less Common

EMPEA has long argued that EM PE holds the potential to generate attractive returns for investors and contribute to the development of emerging economies. Moreover, many long-standing investors in emerging markets, such as DFIs, have taken the social and environmental impact of their investments into account since the inception of their PE programs. However, only in recent years has a wider swath of commercial investors explicitly acknowledged the importance of social and environmental factors in their investment decision-making. In an effort to quantify this change in thinking, this year's survey included questions centered on impact.

Excluding DFIs and investors with impact-only mandates, more than three-quarters of respondents take social or environmental impact into account when making investment decisions. Though *consideration* of environmental and social impact when making investment decisions is now apparent, *dedicated* allocations to impact investing are much less common. The majority of respondents (70%) that take environmental and social impact into account have no dedicated allocation to impact investing.

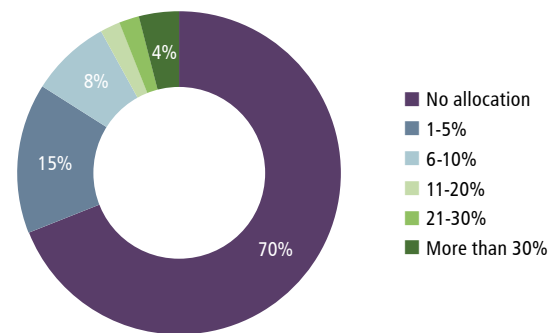
Respondents demonstrate a growing consensus around three key criteria necessary for investments to be considered impact-oriented: the development of a clear thesis at the outset of an investment, measurement of environmental and social indicators and reporting of this data back to stakeholders. However, less than half believe that commercial returns are necessary for a strategy to be considered impact investing. EMPEA has previously argued that the full institutionalization of impact investing demands that *equal emphasis* be placed on market-based financial returns. The diverse opinions of this year's survey respondents suggest that such a consensus is yet to be achieved.

Exhibit 9: Does Your Institution Take Social or Environmental Impact into Account When Making Investment Decisions?\*



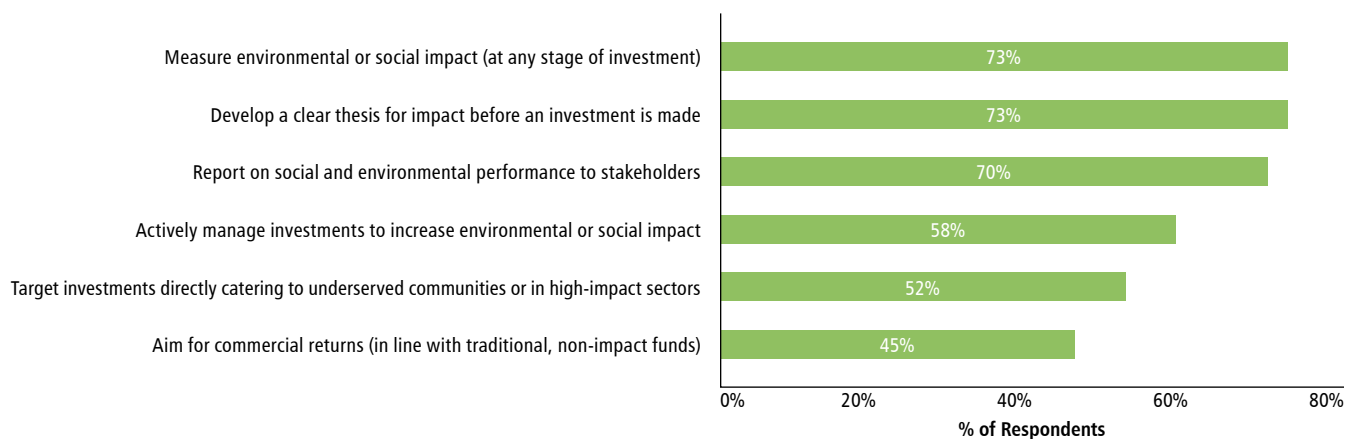
\*Excludes DFIs, government agencies and investors with impact-only mandates.

Exhibit 10: Percentage of PE Portfolio Dedicated to Impact Investing\*



\*Excludes DFIs, government agencies and investors with impact-only mandates.

Exhibit 11: Criteria That Must Be Met for an Investment to Be Considered an Impact Investment



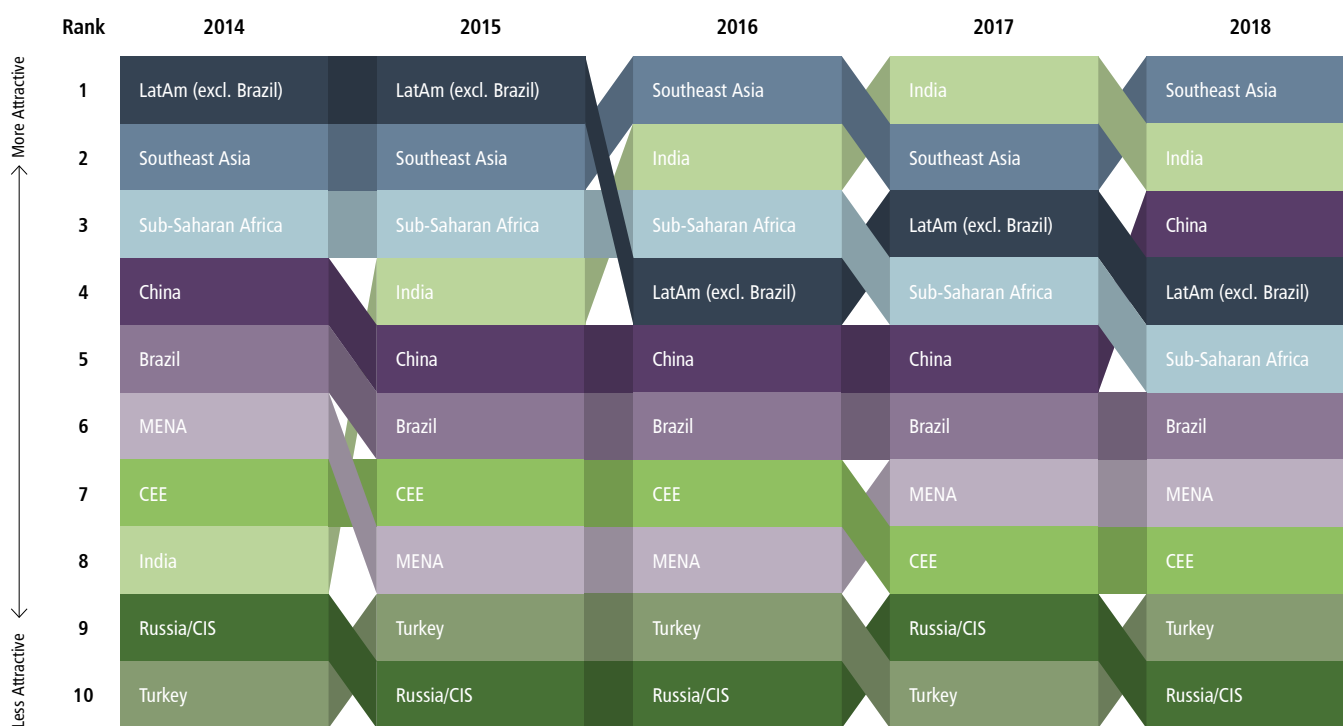
# Investors Remain Bullish on Southeast Asia, but Will Greater Commitments Follow?

Private capital fundraising and investment in Emerging Asia reached US\$50 billion and US\$38 billion, respectively, in 2017, their highest levels since the inception of EMPEA's research program in 2006. These figures are impressive in their own right, but also in comparison to private capital activity in other EM regions. This dichotomy is reflected in EMPEA's 2018 market attractiveness rankings, which capture LP views on the appeal of ten emerging markets for GP investment over the next 12 months. The three Asian markets included in the survey outranked all others. Southeast Asia recovered its spot at the top of the list, pushing India down to second place. China, which for the past five years has held steady at either fourth or fifth place, jumped up to third place in this year's rankings.

Below the top three, Latin America (excl. Brazil) fell to fourth place while Sub-Saharan Africa has continued its slide from first place in 2013 to fifth place in 2018. This drop-off in perceived attractiveness follows macroeconomic downturns and heightened currency volatility in key African markets. However, as documented in the EMPEA Brief, *The Road Ahead for African Private Equity*, many fund managers investing across Africa are adopting new approaches to value creation in order to adapt to tenuous economic conditions, volatile currencies and increasingly competitive deal origination.

The lower rungs of the rankings remained stagnant, with little movement from the prior edition of the survey. Brazil, MENA and Central and Eastern Europe all maintained their positions from 2017. Once again, Turkey and Russia swapped places at ninth and tenth, respectively.

Exhibit 12: The Attractiveness of Emerging Markets for GP Investment Over the Next 12 Months



“ In Southeast Asia, demographics power consumption. There are opportunities to leapfrog to internet-enabled solutions, as well as huge scope for health care investments.”

–DFI

“ We are attracted to the continued growth in Brazil and other Latin American countries. Political instability in certain geographies like Turkey may make for attractive valuations.”

–Pension fund



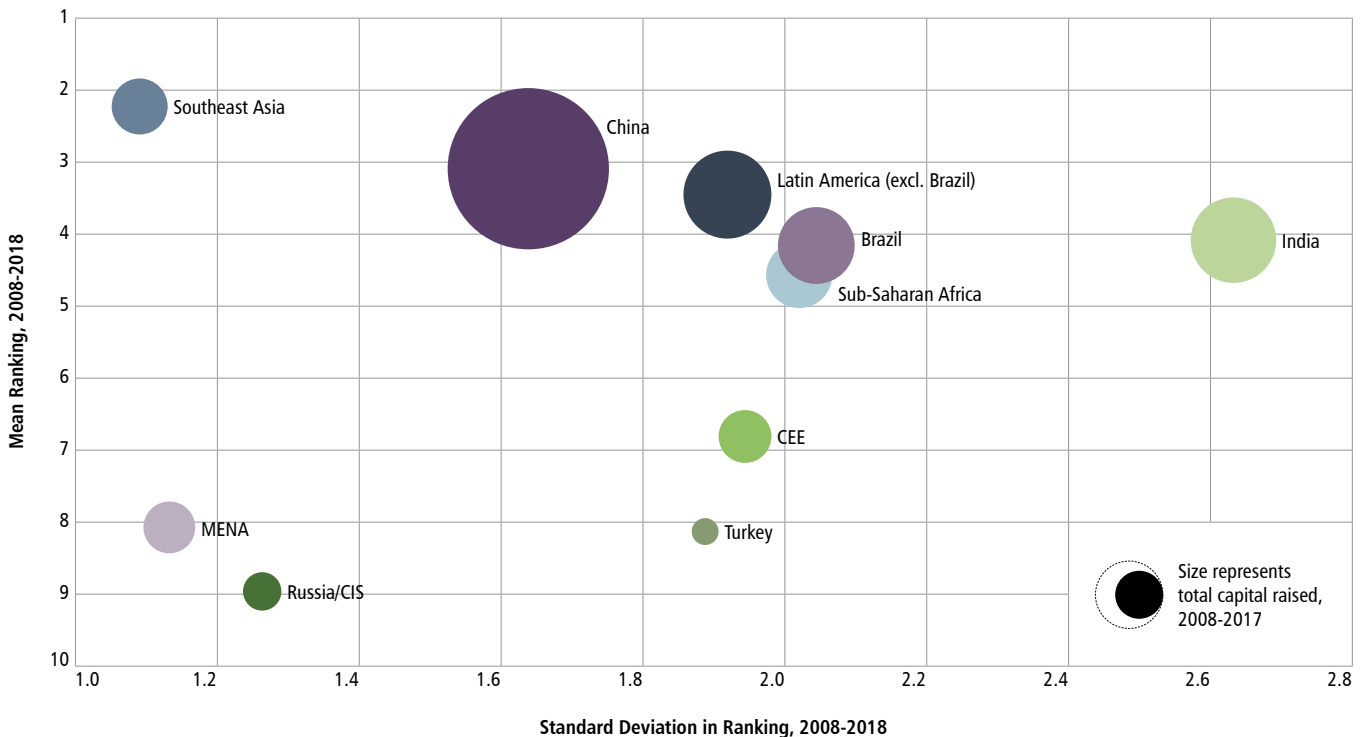
Market Attractiveness, continued

While the top spot in the market attractiveness ranking may seem to be an enviable position, investor sentiment does not always translate into actual capital raised. Southeast Asia has held the first or second spot in the rankings for the last six years, but annual fundraising for private capital vehicles dedicated to the region has actually declined over the same time period, leaving it far behind single-country totals for China and India. Pan-Asia funds may play a role in this story, however. Many fund managers could be expected to allocate a portion of such vehicles to Southeast Asian companies.

Whereas Southeast Asia has experienced relatively little variance in perceived attractiveness on the part of survey respondents, India's position has proven more volatile. The country held the number two spot in 2008 and dipped down to eighth place in 2014, only to jump back to first position in 2017. Unlike Southeast Asia, India has seen influxes in fundraising corresponding to its ranking, with fundraising peaks in 2008 and 2015, respectively. Similarly, Sub-Saharan Africa, Brazil and Latin America have also seen peaks in fundraising in the years at or around their ascent to the top of the market attractiveness list. China, which attracted the most fundraising for private capital vehicles from 2008 through 2017, has held relatively steady in the middle of the market attractiveness rankings.

MENA and Russia/CIS have moved little and remain mired in the lower end of the rankings. In earlier iterations of the survey, Central and Eastern Europe and Turkey fared better in terms of perceived attractiveness, but have since languished in the bottom half of the rankings. For all four of these markets, their position may result more from LPs' institutional mandates or perceived political risk than from fundamental investment potential (see Page 8).

Exhibit 13: Market Attractiveness Rankings Historical Analysis – Mean, Dispersion and Total Capital Raised



Note: Southeast Asia was classified as "Other Emerging Asia" in 2010 and 2011 (and prior to that, not included in the survey). Sub-Saharan Africa was classified as "Africa (excl. South Africa)" from 2008 through 2010 and MENA as "Middle East" from 2008 through 2010. Turkey replaced South Africa (subsequently omitted) in the 2011 survey. "Total capital raised" figures are drawn from the EMPEA Industry Statistics (data as of 31 December 2017).

“ Better growth opportunities, more exits taking place and improved choices in fund managers make China, India and Brazil very attractive.”  
 –Fund of funds

“ Central and Eastern Europe is relatively undervalued. Growth rates in these markets are higher than in developed markets, and exchange rates are expected to be stable over the next two years relative to the euro.”  
 –DFI

# LPs Are Most Likely to Be Deterred by Political Risk, Demand the Highest Return Premiums for Investments in Russia and Turkey

The relative importance of political risk in an LP's decision to invest or not to invest in any given emerging market can vary widely from year to year based on perception of recent domestic events, as well as developments beyond a country's borders, as this year's survey results demonstrate. Turkey and Russia/CIS once again received the highest share of responses citing political risk as a deterrent for investing, which is largely unsurprising considering their prevailing regimes have long provoked caution among many international investors. However, other markets have been more strongly impacted by headlines since the last edition of the survey. Following a disputed election in Kenya last summer and the protracted resignation of President Jacob Zuma in South Africa, a higher percentage (61%) of LPs cited political risk as a deterrent to investing in Sub-Saharan Africa than in the 2017 survey (51%). While Chinese domestic politics have proven more stable, the ongoing trade dispute between the country and the United States may be responsible for the percentage of LPs citing political risk as a deterrent moving from 27% in 2017 to 36% in this year's survey.

LP concerns around currency risk appear to be most acute in Latin America. A higher percentage of respondents cite currency risk as a deterrent for investing in Brazil and Latin America (excl. Brazil) than for any other EM geography at 59% and 53%, respectively. Moreover, the share for both markets increased compared to 2017's results. Nonetheless, when EMPEA asked how many basis points over the developed market PE returns respondents would need to earn to justify the decision to commit EM PE funds targeting these geographies, the mean return premium for Brazil and Latin America (excl. Brazil) was lower than all other markets with the exception of the three survey choices from Emerging Asia.

Exhibit 14: Factors Likely to Deter LPs from Investing in Individual Emerging Markets/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
China	26%	5%	5%	19%	2%	14%	10%	31%	21%	36%	17%
India	24%	17%	17%	7%	5%	24%	24%	24%	17%	10%	29%
Southeast Asia	15%	6%	42%	3%	15%	9%	18%	24%	15%	18%	30%
Russia/CIS	9%	11%	21%	0%	11%	0%	18%	36%	12%	70%	33%
Turkey	7%	7%	21%	0%	14%	2%	18%	26%	16%	72%	42%
Central and Eastern Europe	15%	10%	27%	0%	27%	0%	17%	15%	24%	22%	17%
Brazil	27%	15%	12%	7%	2%	5%	17%	29%	15%	39%	59%
Latin America (excl. Brazil)	13%	13%	34%	0%	25%	3%	25%	25%	16%	34%	53%
Middle East and North Africa	11%	15%	41%	0%	26%	0%	24%	24%	15%	50%	37%
Sub-Saharan Africa	10%	12%	44%	0%	29%	0%	34%	37%	15%	61%	51%

\*Indicates percentage of respondents answering for each region/market.

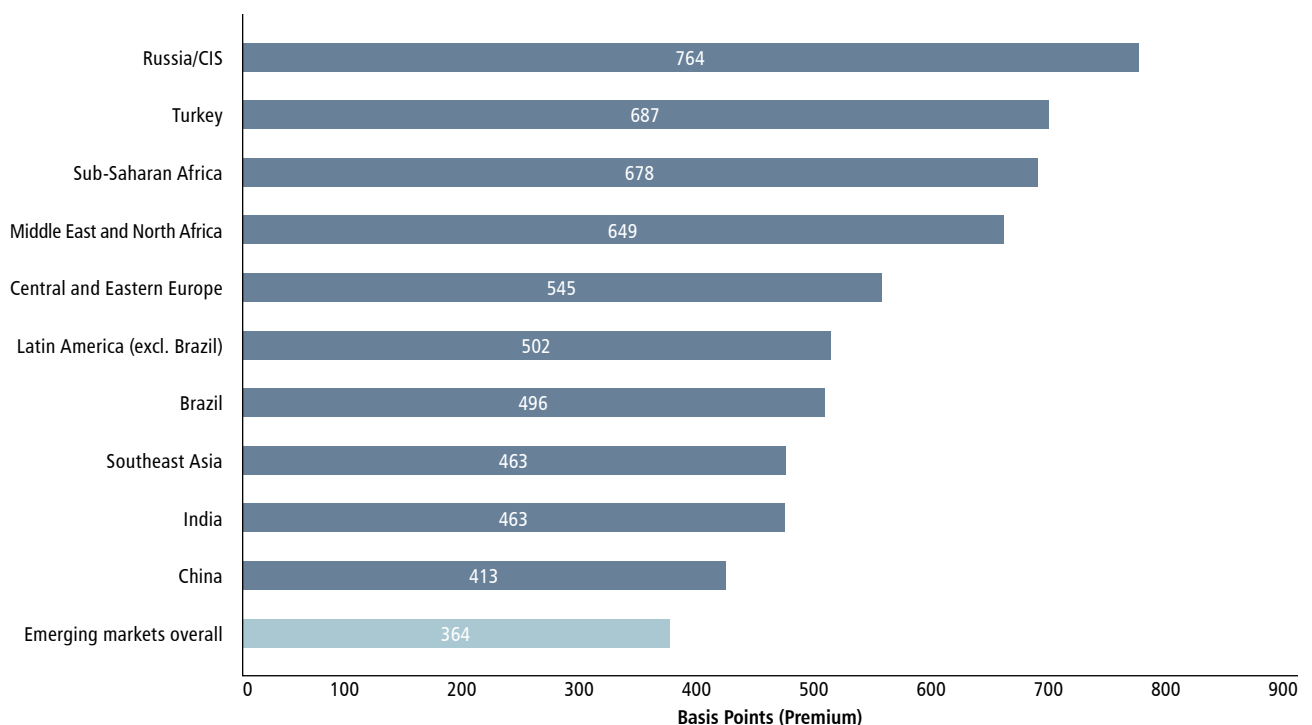
When considering China and India, which regularly attract the largest annual totals in disclosed private capital invested among all emerging markets, LPs are most likely to be deterred by the perceived competitiveness of their local investment environments. China stands apart from other emerging markets in terms of the percentage of LPs’ indicating an oversupply of PE funds as a deterrent at 19%. Meanwhile, the proportion of respondents citing high entry valuations as a deterrent to investing in India doubled from the 2017 survey, overtaking China. Given India’s rapid rise in EMPEA’s market attractiveness rankings from eighth in 2014 to first in 2017, it is perhaps unsurprising that country’s popularity may prove a double-edged sword. India also received the highest percentage of respondents citing historical performance as a deterrent to investing, demonstrating that some LPs retain concerns over how Indian PE’s previous boom era before the Global Financial Crisis unfolded.

Sub-Saharan Africa’s perception issues appear to go beyond political risk. More respondents cited the limited number of established managers; weak exit environments; the small scale of opportunities to invest; and challenging regulatory and tax issues as deterrents to investing in Sub-Saharan Africa than for all other markets. Higher growth forecasts for many of the region’s economies may alleviate some of these pressures, but the range of deterrents indicated by survey respondents captures the difficulties facing managers on the continent.

Central and Eastern Europe is an outlier in this year’s survey with respect to the deterrents named by respondents and the return premium they demand for investing in the region. While only 22% and 17% of respondents cite political risk and currency risk, respectively, as deterrents to investing in CEE—among the lowest for emerging markets—investors expect the fifth highest return premium for commitments to funds focused on the region. As explored in the EMPEA Brief, *The Case for Private Capital in CEE*, the region may lack a natural home among the investment teams and divisions typical of many institutions, and DFIs often prioritize lower-income regions and countries. In essence, Central and Eastern Europe may be too developed to be attractive as an emerging market, but too risky or sub-scale when compared to Western Europe.

Respondents expect a lower return premium for emerging markets as a whole than for every individual EM region and country included in the survey, which at first glance appears somewhat anomalous. However, survey respondents may have considered the concentrated risk of investing in specific regions or countries when completing the questionnaire. The return premium for any given market generally aligns with investors’ perception of an EM region’s levels of political risk and currency risk.

Exhibit 15: Return Premium over Developed Markets That Would Justify Decision to Commit to EM PE Funds (Mean Respondent)



# While Evidence of Relationship Consolidation and Disintermediation Remains, LPs Are Also Looking for Country- and Sector-specific Opportunities

LP responses to this year’s survey questions on manager selection and the use of intermediaries to access EM PE opportunities provide further evidence that many institutions are employing highly selective approaches to backing new managers and expanding their co-investment and direct investment programs. In line with last year’s findings, approximately two-thirds of survey respondents plan to form between one and five new EM PE fund manager relationships over the course of the next three years. Pension funds, in particular, appear more likely than other institutions to pare down relationships, as 26% of pension respondents expect their total number of active EM PE relationships to decline. Another factor at play in LP decision-making may be the growing maturity of survey respondents’ EM investment programs: more than 78% of the full sample have been investing in EM PE for at least six years, and fully allocated institutions may be less likely to pursue commitments to new GPs.

In addition to forming fewer new GP relationships, LPs appear as committed as ever to expanding their co-investment and direct investment programs in emerging markets. Just under 60% of survey respondents plan to begin or expand EM PE co-investment activities over the next two years while 41% plan to begin or expand direct investment programs. These shares are up from 52% and 35%, respectively, in the 2017 edition of the survey. The results suggest that GPs will need to develop approaches for giving their investors access to co-investment opportunities, at least to the extent that their size and deal pipelines allow.

Exhibit 16: Number of New EM PE Fund Manager Relationships Expected in the Next Three Years

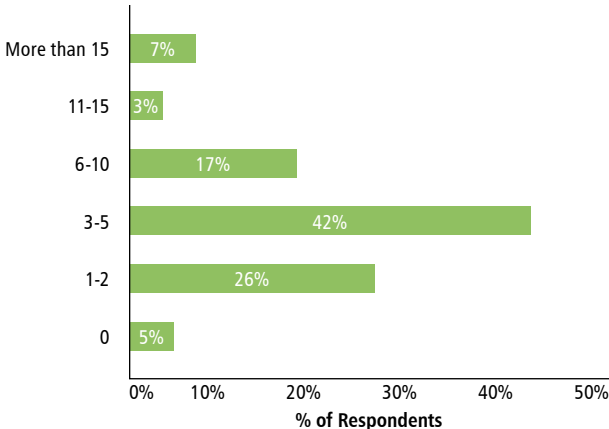


Exhibit 17: Effect of an EM PE Fund Manager's Use of Subscription Credit Lines on Decision to Commit

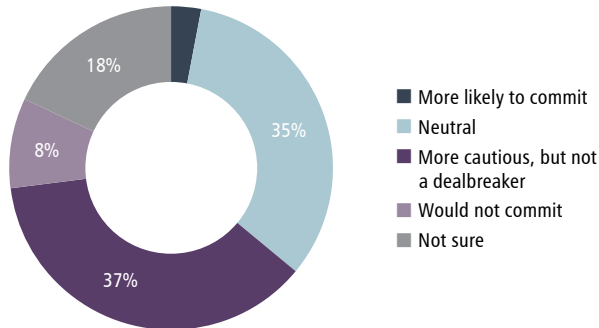
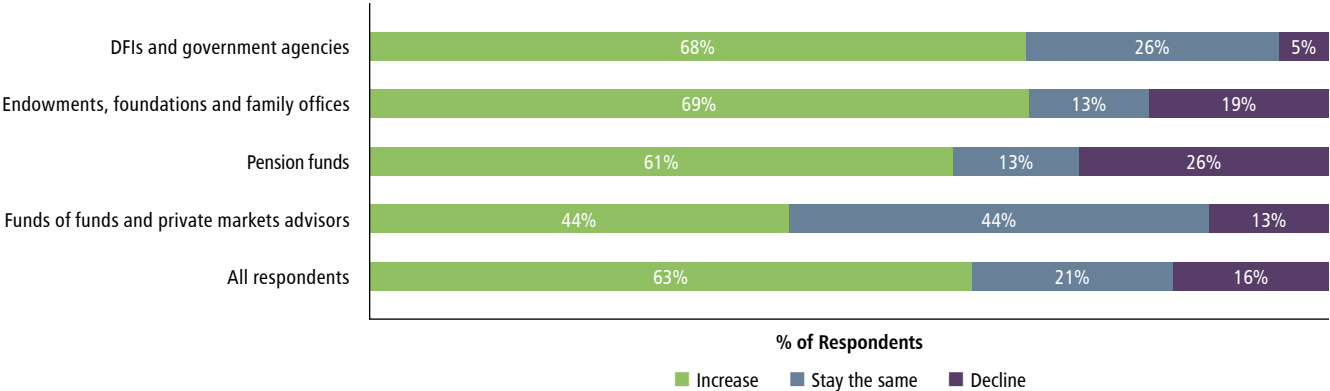


Exhibit 18: Expected Change in Total Number of Active EM PE Fund Manager Relationships

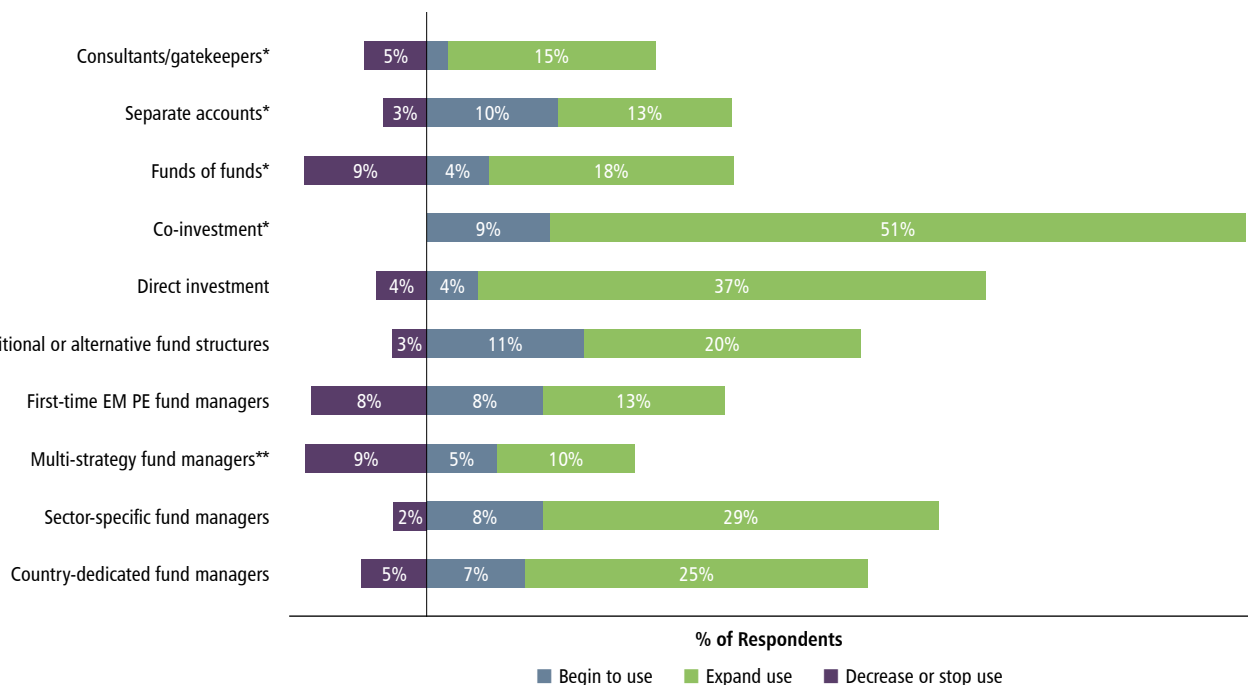


Fund managers looking to employ more creative approaches to investing beyond the constraints of the conventional fund model may be heartened to learn that 31% of survey respondents plan to begin or expand their investments via alternative or non-traditional fund structures. In the 2017 survey, just 18% of respondents indicated they would expand use of such vehicles.

To many observers, survey findings regarding LPs’ plans for new relationships would seem to privilege the largest and most experienced EM PE fund managers—those who can accept large checks, perhaps even across multiple products or strategies. Indeed, just over one-third of respondents either do not invest in first-time EM PE fund managers or plan to decrease or stop investing in first-time funds. Yet a sizeable minority of survey respondents appears poised to expand their commitments to sector-specific and country-dedicated fund managers, who often raise smaller pools of capital. Just over 37% of surveyed LPs plan to begin or expand investing via sector-specific fund managers over the next two years while the corresponding figure for country-dedicated fund managers is 32%. In contrast, just 15% of respondents plan to begin or expand investing via multi-strategy fund managers, and 9% plan to decrease or stop commitments to such managers.

Beyond the number of new relationships LPs expect to form, with this year’s survey EMPEA sought to better understand LP sentiment toward a tool that has gained prominence across the industry: the use of subscription lines of credit at the fund level. Over two-thirds of respondents are neutral or cautious, but not opposed to EM PE fund managers’ use of fund lines of credit. Of the 8% of respondents who would not commit to an EM PE fund manager using such a facility, all are either development finance institutions, government agencies or based in emerging markets, suggesting that acceptance of such facilities is not uniform at the global level.

Exhibit 19: LPs' Planned Changes to Means of Accessing EM PE Investment Opportunities over the Next Two Years



\*Responses exclude funds of funds and private markets advisors.

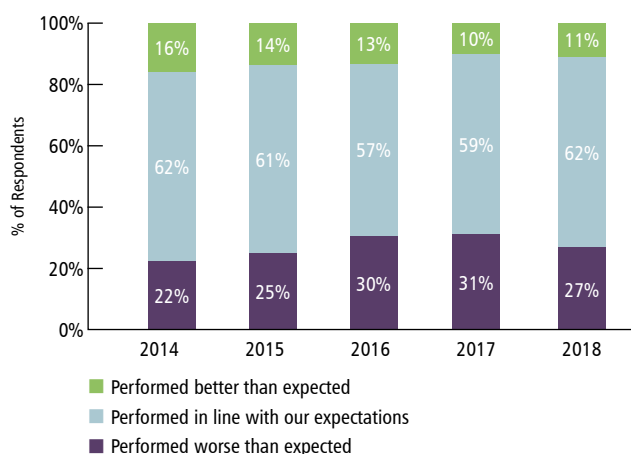
\*\*Multi-strategy fund managers includes GPs with multiple funds dedicated to different asset classes and/or geographies.

# After Declining for Four Consecutive Years, Return Expectations for Emerging and Developed Markets Increase in 2018

A slightly higher percentage of respondents to this year's survey indicate that their portfolios have performed better than expected or in line with expectations, bucking a four-year trend in which satisfaction with the performance of EM PE portfolios waned. Overall, 73% of respondents indicated that their EM PE portfolios had performed better than or in line with expectations. Pension funds were more pessimistic than the full sample, with 42% of pension respondents indicating their portfolios had performed worse than expected, compared to 27% for all respondents.

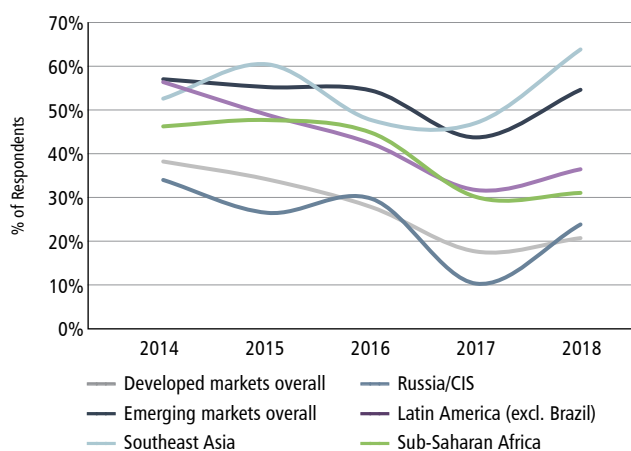
LPs also appear more optimistic in their expectations for future returns than in the 2017 edition of the survey. After declining for four consecutive years, the proportion of respondents expecting overall EM PE to generate returns of 16% or greater increased to 54% in 2018. This year-on-year increase also applied to all individual EM geographies included in the survey and to developed markets overall. However, some historical perspective is in order. A closer look at LPs' return expectations across the last five editions of the survey suggests that LPs' outlook has remained more bullish for some markets than others. Despite a year-on-year increase, the proportion of LPs expecting returns of 16% or more from funds focused on Latin America (excl. Brazil) and Sub-Saharan Africa is actually well below the level in 2014, perhaps reflecting greater currency volatility and economic uncertainty in these regions.

Exhibit 20: EM PE Portfolio Performance Relative to Expectations, 2014-2018\*



\*Excludes LPs that felt it was too soon to assess the performance of their portfolios.

Exhibit 21: Net Return Expectations of 16% or More for Select Markets, 2014-2018



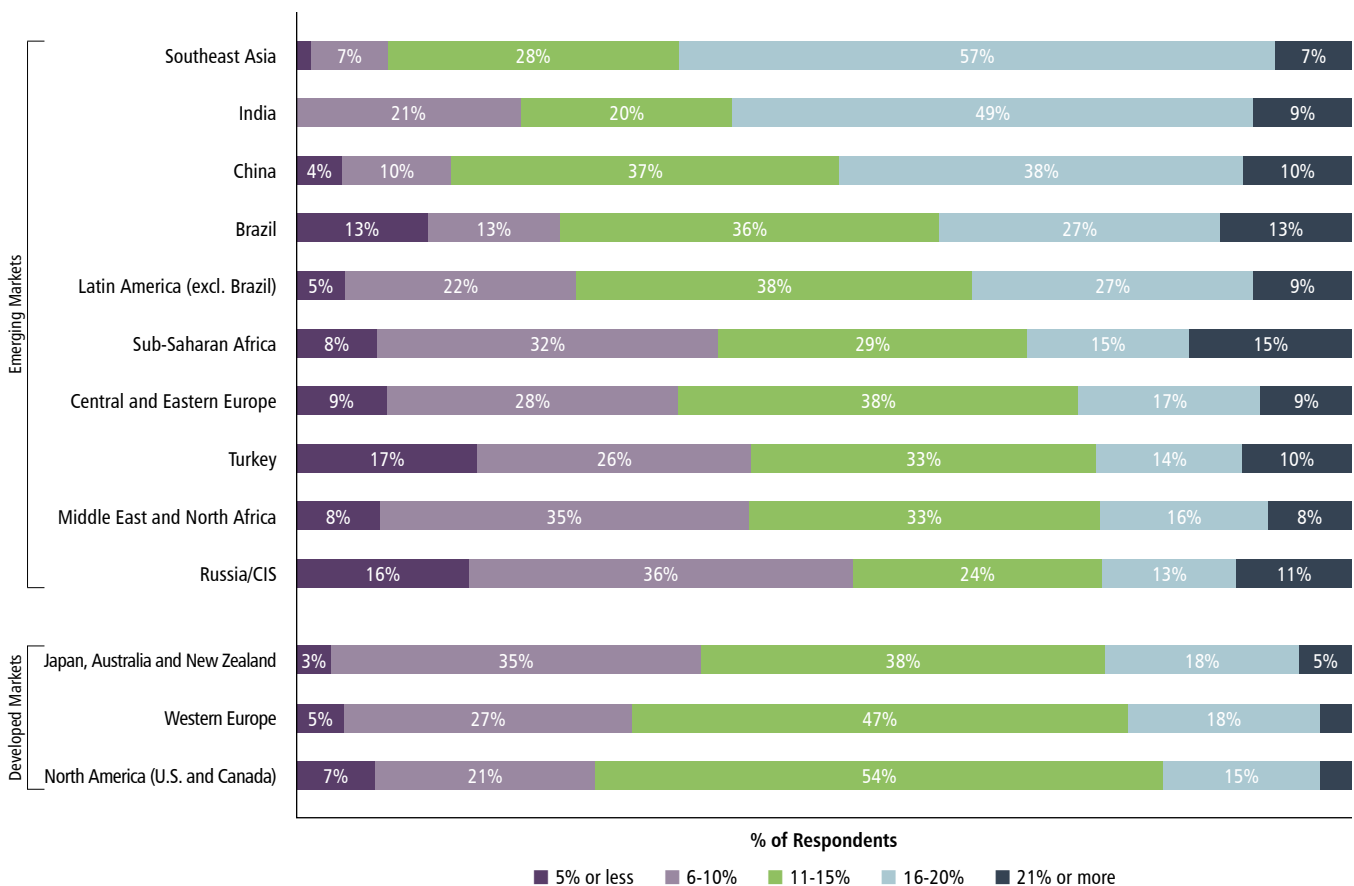
## LPs on 2017-vintage EM PE funds' potential for outperformance:

- “ Assets are overpriced in the United States, so opportunities to add further value are restricted.”  
*–Pension fund*
- “ It's difficult to tell given emerging markets have greater unpredictability vis-à-vis currency, politics, exposure to energy prices, etc.”  
*–Fund of funds*
- “ Emerging markets will perform significantly better overall, primarily due to the opportunity set and ability to buy assets at a much lower price.”  
*–Endowment*
- “ The EM track record for returns is poor, but the amount of dry powder that has accumulated for DM funds makes me feel like it could be a wash.”  
*–Pension fund*
- “ Emerging markets should be in the advantageous part of their economic cycle relative to developed markets. Growth has remained very strong, managers are better and capital markets are more supportive.”  
*–Fund of funds*

In contrast, return expectations for Emerging Asia lead all other EM geographies in the 2018 survey and may be contributing to LPs' buoyant outlook for emerging markets overall. In line with EMPEA's market attractiveness rankings (see Page 6), LPs expect the highest returns to come from Southeast Asia, with 64% of LPs expecting returns of 16% or greater from 2017-vintage Southeast Asia-focused funds. India and China follow at 59% and 49%, respectively.

While a lower proportion of survey respondents express confidence in the ability of GPs to deliver high returns in geographies beyond Emerging Asia, comparing 2018 results with last year's survey reveals the tide may be turning, at least for some LPs. In the 2017 survey, the proportion of respondent expecting returns of 16% or greater for Russia- and Turkey-focused funds was 10% and 12%, respectively. In this year's survey, this proportion has risen to approximately 24% of all respondents for both countries. A substantial share of LPs still expects returns of 10% or less for Russia/CIS (53%), MENA (43%) and Turkey (43%). However, at the more optimistic end of the spectrum, a higher proportion of surveyed LPs expect returns of 16% or higher for these geographies than for all DM geographies. This disparity points to continued confidence on the part of many investors in the potential of these underserved markets.

Exhibit 22: Distribution of Net Return Expectations from 2017-vintage Funds



EM PE funds will underperform because:

“ There are a few pockets of excellence and many mediocre funds.”  
 –DFI

“ History is the leading indicator, and I don't see any changes to conclude otherwise.”  
 –Pension fund

# LPs Expect Sub-US\$500 Million Funds to Generate the Highest Net Returns

Fundraising for US\$1 billion-plus funds, especially in Emerging Asia, drove much of the increase in capital raised for EM private capital funds in 2017. However, the majority of respondents to this year’s survey expect smaller vehicles to generate the highest net returns. Just over 43% of LPs expect 2017-vintage EM PE funds in the US\$250 million to US\$499 million range to generate the best returns, and approximately one-third of respondents expect the highest net returns to come from slightly smaller funds in the US\$100 million to US\$249 million range. Very large (US\$1 billion-plus) and very small (less than US\$100 million) funds, at least by overall EM standards, attracted the fewest respondents. Many of the country-dedicated and sector-specific funds that LPs are expanding commitments to would likely fall in the midsize range (see Page 11).

Not all LPs may find it easy to invest in funds in the US\$100 million to US\$499 million range, however. In this year’s survey, EMPEA asked respondents to provide additional information on the ticket sizes they could write for EM funds. The results of this exercise suggest pension funds may have the most difficulty in accessing middle-market funds. The median minimum and maximum commitment sizes for pensions in the sample—at US\$25 million and US\$75 million, respectively—are noticeably higher than for other institution types. In recent years, the traditional fund of funds model, which has historically enabled larger LPs to access smaller funds, has received more scrutiny from some LPs due to the layering of fees it entails. Moreover, as this year’s survey results indicate, LPs are under pressure to consolidate relationships, which may mean larger commitments to a smaller number of GPs. This confluence of factors suggests more creative solutions may be needed to enable the largest pensions to access middle-market opportunities in emerging markets.

Exhibit 23: Minimum and Maximum Commitment Sizes to EM PE Funds by Institution Type

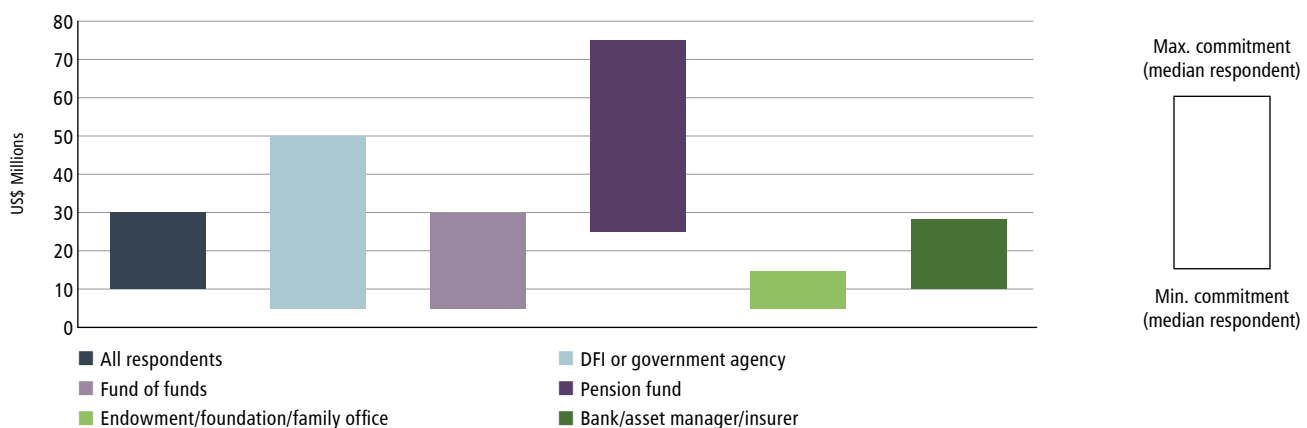
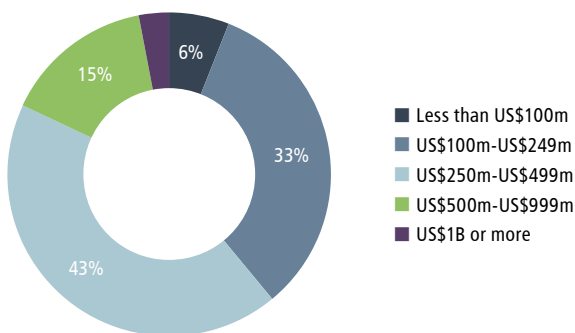


Exhibit 24: 2017-vintage Fund Size Segment Expected to Generate the Highest Net Returns



“We’re looking for fund managers with the ability to deploy capital at scale.”  
*–Pension fund*

“Fund managers need to be able to invest and operate at all points in the economic cycle.”  
*–DFI*



# GPs' Operating Skills to Have Highest Impact on Performance of 2017-vintage Funds

LPs expect GPs' ability to drive operational improvement at the portfolio company level to have the biggest impact on the performance of 2017-vintage funds, followed by overall economic growth in emerging markets and entry multiples. Future exit conditions—in the form of appetite from strategic buyers and public market investors—rank relatively lower, and just 1% of respondents expect the use of leverage, or perhaps its unavailability, to have the biggest effect on performance.

Higher economic growth in emerging markets has long been cited as a potential source of outperformance over PE in developed markets, but LPs' focus on operational improvement as a return driver may reflect the more volatile economic outlook that has prevailed in many emerging markets since 2014. A GP's ability to implement operational improvements is crucial for bolstering returns in otherwise adverse economic conditions.

While LPs are increasingly concerned with EM-focused GPs' operational skillsets, approximately half of respondents believe EM PE fund managers' value creation abilities are behind those of their developed market counterparts. In open-ended feedback, LPs cite talent acquisition; the ability to source add-ons; the use of dedicated teams with local knowledge; the application of replicable strategies; currency hedging; and the ability to manage environmental, social and governance interventions as key parts of an EM PE fund manager's value creation toolkit.

Exhibit 25: Return Drivers Expected to Have the Biggest Effect on the Performance of 2017-vintage EM PE Funds

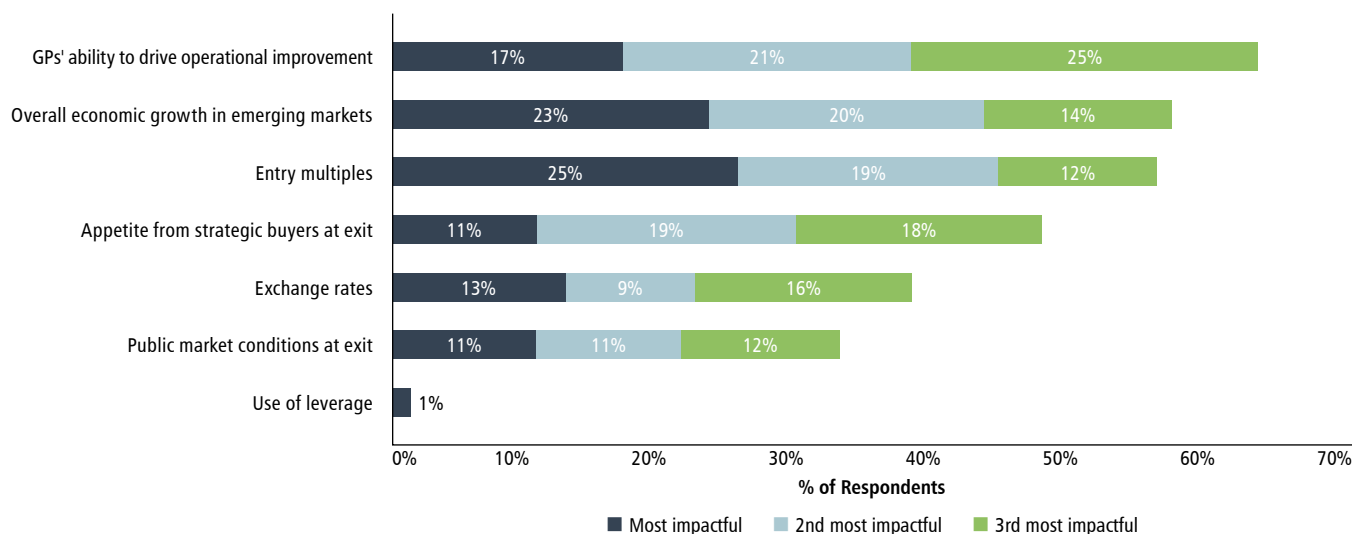
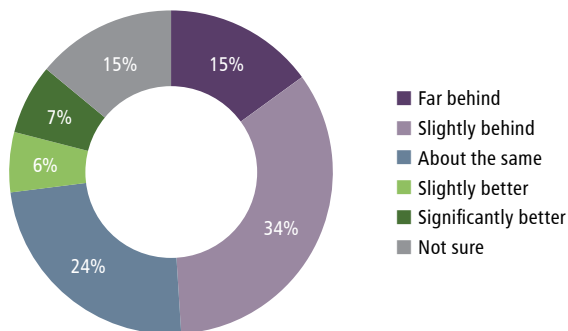


Exhibit 26: EM PE Fund Managers' Value Creation Abilities in Comparison to DM Peers



“GPs need to show active involvement on the back of a clear plan or strategy. Dedicated resources also serve as a key differentiator.”  
*–Pension fund*

“We want to see the same tools used by DM PE fund managers and possibly more, as emerging markets pose more challenges.”  
*–Pension fund*

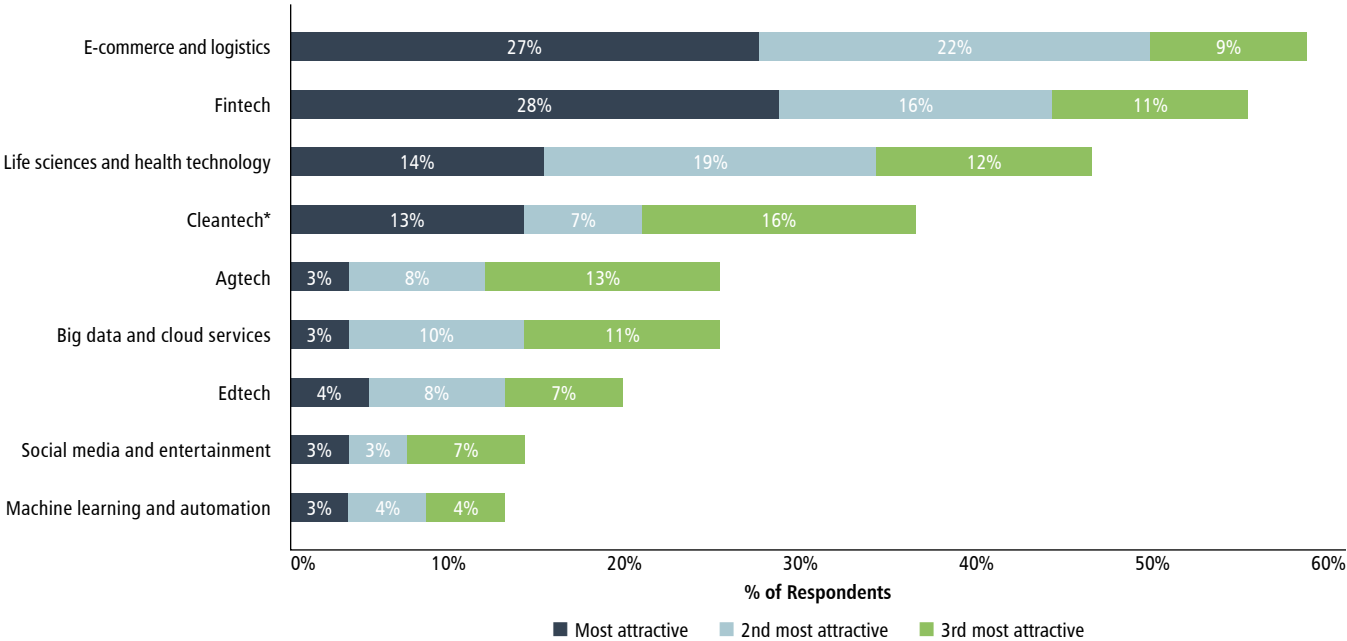
# Investors Rank E-commerce and Fintech as Most Attractive Technology Verticals for Investment in Emerging Markets

Recognizing growing investor interest in supporting technology-enabled business models in emerging markets, this year EMPEA asked respondents to assess the attractiveness of specific technology areas for investment in emerging markets rather than larger industry groups. The results suggest that LPs are keen to access consumer-driven opportunities in the digital economy. Respondents rank e-commerce and fintech as the most attractive technology areas for EM investment over the next two years. These were followed by life sciences and cleantech, respectively, with the latter inclusive of renewable power and energy storage.

LPs’ interest in e-commerce and logistics largely mirrors trends in private investment activity in emerging markets. In 2017, private capital fund managers completed 176 deals and deployed US\$5.8 billion in the e-commerce segment in emerging economies, according to EMPEA’s *Industry Statistics*. The number of deals completed was down from 349 in 2015 as GPs backed a more concentrated group of companies. However, bigger-ticket investments in the likes of Poland-based Allegro and China’s Koubei drove disclosed capital invested in the segment to its highest level since EMPEA’s research program was established.

When respondents ranked the top three most attractive technology areas for investment in emerging markets, e-commerce garnered the most interest. However, a slightly higher percentage (28%) of respondents ranked fintech as the most attractive area for investment among all choices. As new platforms compete with traditional financial intermediaries for the attention of emerging market consumers, the appeal of this space is likely to continue to grow.

Exhibit 27: Most Attractive Technology Areas for EM Investment over the Next Two Years



# Respondent Profile and Survey Methodology

In February and March 2018, EMPEA surveyed 116 representatives from 107 different institutions to gather their views on private equity in emerging markets. The institutions included in the survey are based in 36 countries and collectively represent more than US\$5.7 trillion in total assets under management. Pension funds, development finance institutions and funds of funds constitute the majority of the sample included in this year's survey, with the balance comprising endowments, foundations, family offices, banks, asset managers, insurers, government agencies and sovereign wealth funds. In cases where multiple responses from the same institution were received, only one response has been included for questions pertaining to institutional policies, current allocations and future investment plans. More than 90% of institutions surveyed are currently invested in at least one EM PE fund, and 78% have been investing in EM PE funds for more than five years. EM investments constitute 20% of the current overall PE portfolio of the average surveyed institution (excluding development finance institutions, EM-focused funds of funds and others legally mandated to invest in emerging markets).

Exhibit 28: Respondents by Institution Type

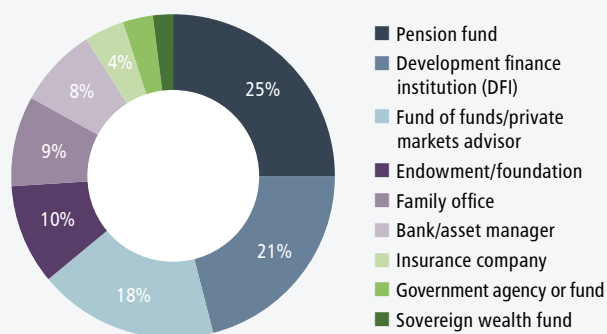


Exhibit 29: Respondents by Headquarter Region

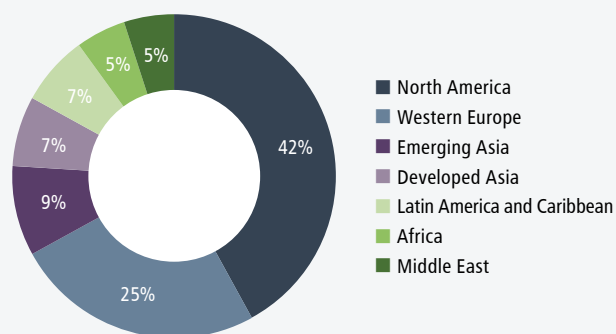
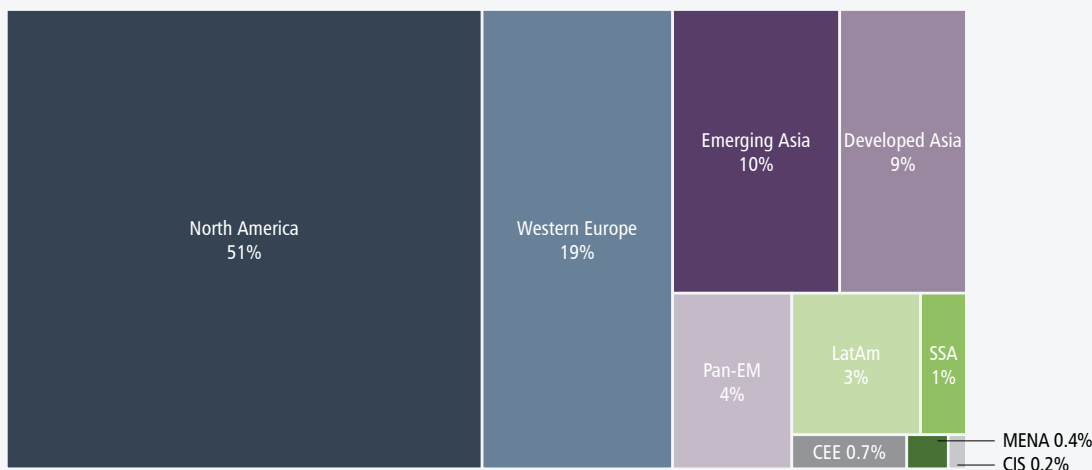


Exhibit 30: Disclosed Distribution of Current Committed Capital in Global PE Portfolio\*



\*Excludes investors with EM-only mandates.

## Survey Definitions

**Emerging markets** ("EM") includes all countries outside of the United States, Canada, Western Europe, Israel, Japan, Australia and New Zealand (developed markets, or "DM").

**Private equity** ("PE") encompasses (leveraged) buyout, growth/expansion, venture capital and mezzanine investment strategies.

**Emerging markets private equity** ("EM PE") funds are PE funds that principally target investments in emerging markets.

**Limited partners** ("LPs") are investors in PE funds.

**General partners** ("GPs") are PE fund managers.

**Development finance institutions** ("DFIs") are independent, government-backed or multilateral financial institutions that promote private sector development in developing countries.

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



2600 Virginia Avenue NW • Suite 500 • Washington, DC 20037 USA  
Phone: +1.202.333.8171 • Fax: +1.202.333.3162 • Web: [empea.org](http://empea.org)

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