

# IPM monthly blog

Our monthly **insights** into **private markets** – **October 2024**

## Real estate



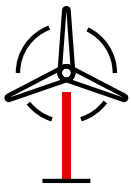
## Bottoming out

Interest rate outlook continues to see-saw. US Treasury yields expanded 50-60bps in the last month after a sharp 100bps decline over April–September. While some buy-the-rumor / sell-the-fact trades were at play after the September US Fed rate cut, the bond sell-off was also partly triggered by stronger-than-expected US macro data recently. Nonetheless, the market continues to expect falling interest rates ahead, albeit with uncertainties around its extent and pace. Listed real estate has done well leading up to the Fed rate cut but started to trade sideways since then.

Across the pacific, China surprised the market with a larger-than-expected stimulus. There were some initial concerns on its potential impact to global prices. For now, however, it's fair to assume that the measures will take time to filter through. The real estate sector is likely to stay soft in the near term, but a supportive policy outlook could reignite investor interest at the margin.

Globally, real estate transaction activity is starting to bottom out as property yield spread normalizes. In the US, capital values have turned the corner based on Green Street Commercial Property Price Index. In Europe, property yields are largely stable with some markets starting to decline. In APAC, commercial property prices are also showing signs of stabilization (perhaps less so in China). We think a favorable interest rate outlook is likely crucial for such recovery to gain further momentum.

## Infrastructure



## Can market dislocations offer opportunities?

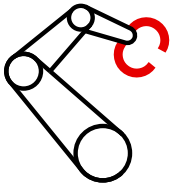
**Recently**, we highlighted that the stars are aligning for private infrastructure. GDP growth in most markets have either met or exceeded expectations from a year ago. Even though infrastructure is generally less GDP sensitive than other asset classes, removing the 'hard landing' risk is still a positive for the industry. Interest rates are also coming down, which is a tailwind for an asset class that employs a fair amount of leverage. Finally, inflation is broadly trending above average around the world – which is a positive for an inflation sensitive asset class like infrastructure.

However, one area that is still lagging are deal flows. According to Inframation, 2023 infrastructure deal flows of ~USD 1 trillion is 20% lower than the record years in 2021 and 2022. Year-to-date in 2024, deal flows are around USD 780 billion, which means we'll likely at most match the 2023 volumes for the full year.

Looking at the big picture, USD 1 trillion is still a large amount of annual deals, when compared to the USD 350 billion of infrastructure dry powder (according to Preqin). The decline in deal activity of ~20% since the 2021 or 2022 peak levels is actually quite modest compared to the declines seen in many other private asset classes. If anything, a bit of market dislocation can actually be good for investors.

The willingness to be contrarian and explore overlooked opportunities can lead to positive outcomes. The big question is, how can investors find these opportunities? There is no right answer, but a combination of outside-the-box thinking, bilateral origination, creative structuring, and avoiding herd mentality or recency biases would be a good start.

## Private equity

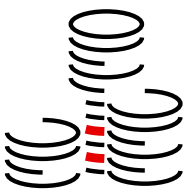


## More exits may be on the horizon

The industry has high expectations that recent rate cuts could boost both IPO activity and exits in the coming quarters. While it is still too early to tell, sponsor narratives have been optimistic, and underwriting cases are beginning to take lower borrowing costs into account. Investors and sponsors are generally unmoved by the upcoming US elections. This reflects the fact that while major races (including the presidency) are considered too close to call, a split Congress resulting in legislative gridlock is considered likely, reducing the odds of significant policy changes. If the polling consensus is wrong, a Republican sweep would probably be better for private company performance. The main reason being that one of the biggest negatives under such a scenario (tariffs) has already been somewhat addressed by near- and friend-shoring in recent years. Conversely, a Democratic sweep is expected to be a drag on performance as the stated policy goals of higher taxes on high-income households, capital gains, and corporations would be within reach.

In Asia, the Chinese economic stimulus package has driven the recent market rally and will most likely be a boon to private equity through lower financing costs and improved market sentiment. This could facilitate private company exits and distributions in the near term. In the long run, the policy shift represents the country's commitment to the next phase of growth and raises the attractiveness of private equity in China. The fundraising environment remains challenging with many investors still in wait-and-see mode, though some deployment is being finalized into year end. Transaction activity remains robust with favorable dynamics for LPs, balanced by the fact that a lot of capital has flowed into co-investments and secondaries in recent quarters. We continue to believe that today's market holds plenty of opportunity for selective investors.

## Private credit



## Compressing valuations

Public credit markets have generated positive total returns in 2024. Over the course of the third and fourth quarters, the pace of spread tightening has accelerated and spreads in many market segments are trading at/near the tightest levels in 20 years. For reference, the US Investment Grade Corporate Bond spread is currently 83bps (20-year tight) and the US High Yield Corporate Bond spread is 293bps (3rd percentile) as of 15 October 2024. While the credit markets are increasingly pricing in a soft landing, public credit has become more asymmetric. At the current valuations, public credit is vulnerable to a correction in the event that there is a deceleration in the economy or a macro-level shock to markets.

As a result of the peak asymmetry of public credit markets coupled with the relatively high base rates, private credit should offer investors a more consistent source of stable income and returns compared to public credit markets. While certain segments of private credit have also experienced some spread tightening, we believe that private credit offers a more favorable return profile compared to public credit on a forward-looking basis. In particular, we're targeting short duration, asset-backed private credit with a specific focus on asset classes that have a favorable fundamental outlook across most market environments. Furthermore, we prefer the asset-backed segment of the market as these assets have a shorter duration profile and are also generally less competitive and have not experienced the same degree of spread tightening over the past 18 months.

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