NB Private Equity Partners

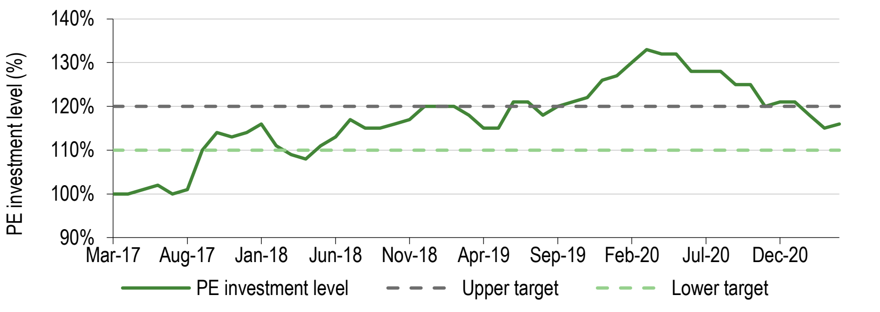
Direct co-investments the key return driver

Investment trusts
Private equity

22 June 2021

NB Private Equity Partners (NBPE) delivered a 12-month NAV total return to end-May 2021 of 52.3% in US$ terms, strongly supported by its exit activity. This includes 10 deals announced in 2021 with an estimated uplift of US$160m (15% of end-2020 NAV), most of which is reflected in the current NAV. NBPE received c US$139m from all its realisations in 2021 until 15 June and expects a further c US$116m once all the above deals have closed. The remaining portfolio also performed well, benefiting from long-term secular trends. The portfolio is currently valued as at end-March 2021 (except for public stocks). Despite the strong returns and a one-layer fee structure, NBPE trades at one of the widest discounts among peers.

Investment level returned to targeted range



Source: Company data. Note: Investment level is total investment portfolio value over NAV.

Why invest in NBPE now?

M&A and IPO markets have picked up, starting in H220, and offer good opportunities to perform exits (as illustrated by NBPE's recent strong realisation activity). At the same time, NBPE's portfolio continues to deliver revenue and EBITDA growth (largely organic). Meanwhile, NBPE has a rich pipeline of potential investments, taking advantage of the broad NB platform. It offers moderately geared exposure, which should benefit net asset value (NAV) returns if economic recovery continues. NB also puts strong emphasis of ESG factors, which is reflected in NBPE's portfolio.

The analyst's view

- Direct co-investments will drive future returns as NBPE's portfolio shift away from income and fund investments is largely complete.
- Its strong exit activity in 2020 and so far in 2021 allowed it to de-risk its portfolio by repaying most of its credit facility, which, together with the NAV uplift, visibly reduced NBPE's leverage. This should ease some earlier investor concerns.
- We note that despite a challenging environment, NBPE maintained its dividend target of at least a 3% yield on NAV. With a wide discount to NAV of c 26%, the first 2021 instalment implies an attractive annualised dividend yield of 3.3%.
- We note that NBPE produced returns above its peers in sterling terms (one-year total return of 32.5% vs peer average of 25.2%) despite its higher weighting to the US and weakening dollar against euro and sterling (9% and 13%, respectively).

NOT INTENDED FOR PERSONS IN THE EEA

Price		**1,340p**
Market cap		**£626.5m**
NAV*		**£837.1m**
NAV*		**US$1,189.5m**
NAV per share*		US$25.43
NAV per share*		£17.89
Discount to NAV		26.5%

*Including income. As at end-May 2021.

Yield		3.3%
Ordinary shares in issue		46.8m
Code/ISIN		NBPE/GG00B1ZBD492
Primary exchange		LSE
AIC sector		Private Equity
52-week high/low	1,400p	886p
NAV* high/low	1,824p	1,356p

*Including income

Gross gearing*	14.8%
Net gearing*	14.4%

* As at end-May 2021.

Fund objective

NB Private Equity Partners invests in direct private equity investments alongside market-leading private equity firms. NB Alternatives Advisers, an indirect wholly owned subsidiary of Neuberger Berman, is responsible for sourcing, execution, and management of NBPE. The vast majority of direct investments are made with no management fee or carried interest to third-party GPs. NBPE seeks capital appreciation through growth in net asset value over time while paying a biannual dividend.

Bull points

- An attractive one-layer fee structure (as opposed to private equity funds-of-funds).
- Higher diversification than direct peers.
- 10-year NAV TR above peer average.

Bear points

- Timing of exits depends on the decision of GPs (but whose interests are largely aligned with NBPE).
- Structural leverage increases NAV volatility.
- Short history as a pure direct co-investment play (but where manager has a 15-year track record).

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NB Private Equity Partners is a research client of Edison Investment Research Limited

Market outlook: Recovery in transaction volumes

Public equity markets performed well during 2020, with the MSCI All-World and S&P 500 posting 14.3% and 16.3% increases despite COVID-19 triggering a broad market sell-off in the initial stage of the pandemic. Nevertheless, growth was not uniform (both in public and PE markets) and was led by sectors that have proven resilient to lockdowns. The competition for quality assets among PE managers remains high, as PE funds have considerable dry powder at their disposal (€294bn in European funds and more than US$550bn in the US at end-2020, according to PitchBook Data). After an M&A standstill in early 2020, deal activity rebounded in H220 pushing up valuations in certain sectors (eg tech, healthcare), which now leads some PE managers to cautiously assume some multiples contraction going forward. Some moderation of valuations has already materialised in tech companies in 2021.

Corporates have faced unprecedented circumstances with worldwide lockdowns and travel restrictions, which has pressured company management teams in several sectors to accelerate the process of digitalisation and implement cost-cutting initiatives. We believe that once the global economy recovers and life returns to normal (or 'new normal'), companies that successfully executed these measures may come out stronger and with higher profitability than prior to the crisis. IMF forecasts released in April 2021 assume GDP growth in the US in 2021 of 6.4% (after a 2020 decline of 3.5%).

We expect a continuation of high PE transaction activity in 2021, which should however be broader based in terms of sectors than in 2020, as illustrated by the deal flow reported by NBPE. We believe that general partners (GPs) will increasingly search for companies that are well positioned for an economic recovery and restrictions easing scenario.

Still, a number of macro risk factors persist that could make the economic recovery protracted and volatile. While the corporate sector avoided a sudden spike in defaults similar to the global financial crisis of 2008 (supported, among others, by record-high fiscal and monetary stimulus as well as the prevalence of covenant-light loans), the defaults are likely to be spread over time, especially once governmental support is phased out. For now, Fitch expects the default rate in 2021 in the US to remain at a moderate level of 4.5% (the same as in 2020). In addition, the optimism fuelled by the vaccination process roll out may potentially be overshadowed by the emergence of new coronavirus variants (which could prove resistant to vaccines) and/or vaccination delays in some countries.

The fund manager: NB Alternatives Advisers

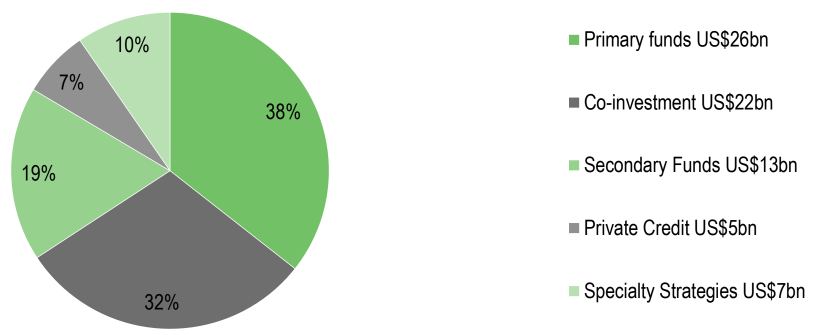
NBPE is managed by NB Alternatives Advisers (NBAA), the PE arm of Neuberger Berman (NB) with over 30 years of experience managing PE investments, with assets under management (AUM) of over US$75bn as at end-March 2021, out of the US$429bn total AUM of NB. NBAA invests across a variety of strategies on behalf of client portfolios, including primary and secondary equity, private debt as well as healthcare credits. In particular, NBAA currently manages US$22bn in AUM in co-investment strategies (see Exhibit 1), up US$3bn since June 2020. Over the past three years, NBAA committed c US$13bn a year to private markets.

NBPE benefits from NB's PE co-investment platform, which offers:

- a 13-person investment committee with average experience of over 30 years (including 18 years on average with the firm), supported by a broad team of around 150 professionals across 10 offices globally within NB's PE vertical;
- long-term co-investment expertise (including a well-established due diligence process), with specialist experience from 2006;

- an extensive deal origination network based on multiple NB PE/debt strategies, including in particular the primary PE platform;
- strong relationships with top-tier PE GPs, often being considered a preferred co-investment partner; and
- capacity to make considerable equity investments across diverse deal types.

Exhibit 1: Neuberger Berman private equity platform at end-December 2020



Source: NBPE

The manager's view: A number of opportunities to invest in

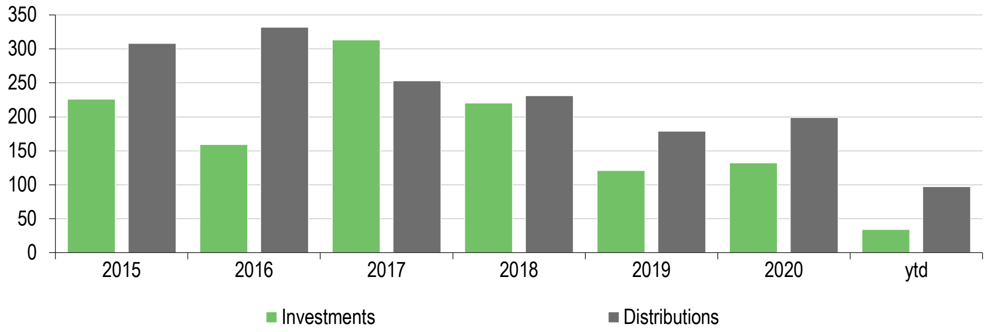
NBPE's 2020 performance is a demonstration of the quality and strength of the underlying portfolio. Looking forward, market conditions for PE, especially in the US, remain robust. NBPE's portfolio continues to produce impressive performance in terms of both growth and realisation potential and NB is seeing strong deal flow of interesting investment opportunities. While there remains some uncertainty about the long-term macroeconomic impact of the pandemic, the investment manager believes the portfolio is well positioned to continue to generate significant value for shareholders. The manager is actively reviewing a high level of attractive new investment opportunities and expects NBPE to be active in new transactions during 2021.

Asset allocation

NBPE performed exits with aggregate value of US$199m in 2020

NBPE made the most of the favourable exit environment in H220 and was thus a net seller in 2020, with realisation proceeds of c US$199.1m representing 18% of its opening portfolio value (broadly in line with its 10-year average of 20%). New investments amounted to US$131.6m, of which close to US$73m was attributable to six direct investments: Action, Duff & Phelps, StubHub and InnovaCare Health, and partial reinvestments following successful realisations (Engineering and ProAmpac). In the first five months of 2021, NBPE remained a net seller. It received US$96.9m in distributions, of which US$20.4m was from income investments, in particular the disposal of Schumacher debt. NBPE also receives proceeds from the continuous selling down of its exposure to public stocks and its public stocks portfolio was recently strengthened by the successful IPO of Agiliti in April 2021. Investments stood at US$34m, of which US$12.2m related to an equity investment into a software and data analytics company for the real estate industry RealPage alongside Thoma Bravo, a leading software-focused private equity fund. In May, NBPE invested US$12.5m in two new direct equity investments Perspecta (an IT company serving primarily the U.S. government), as well as an undisclosed financial services company. This has driven NBPE's investment back to its targeted level (116% at end-May compared to the 110–120% target range), which means that NBPE was fully invested at end-May.

Exhibit 2: NBPE's historical investments and distributions (in US$m)



Source: Company data

The high exit volume continues in 2021

Significant realisation activity is set to continue; as in 2021 NBPE agreed 10 full or partial exits representing expected cash proceeds of US$255m and a US$160m estimated uplift to prior carrying value (part of which was already reflected in the end-May NAV). Four of these realisations are to strategic investors and five to financial buyers, on top of that Agiliti performed an IPO. Telxius and InnovaCare Health are in the process of selling assets representing a portion of their businesses to strategic buyers. We believe that these transactions show that there is an uptick in corporate carveouts on the broader market after a subdued 2020. AutoStore and Edelman Financial Engines are in the process of attracting additional investments from financial investors, which imply higher valuations of the whole entities. Four companies are being fully acquired: West Marine and Ellucian by financial investors and Hivory and Aldevron by strategic investors. Moreover, Holley is being acquired by a listed special-purpose acquisition company, which will make it a public holding that will be sold down over time. The above demonstrates that NBPE has access to various exit routes.

NBPE was fully invested at end-May 2021, with cash at 0.4% of NAV and net gearing at 14.4%. The US$116m disposal proceeds from the above-mentioned exits NBPE is yet to receive represent an incremental cash position of c 10% of current NAV (after full repayment of the drawn part of its credit facility). However, these transactions are expected to close gradually over coming months and based on our discussion with the management, we understand that NBPE has a rich pipeline of potential investments to absorb the additional liquidity. We also note that the disposal gains provide NBPE with a certain runway in terms of NAV returns.

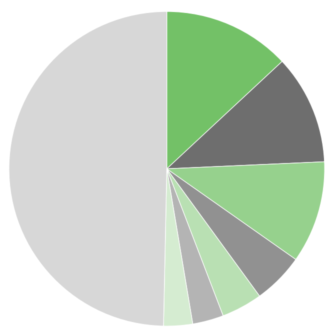
Current portfolio positioning

Around 89% of NBPE's portfolio now represents direct equity investments, with the balance attributable to the steadily diminishing legacy income and fund investments. Direct equity investments also include exposure to listed companies (following their IPOs), which is gradually being sold down. Here, we note that disposals of public stocks are determined by the leading GPs alongside which NBPE co-invests. As at end-May 2021, listed companies made up c 9% of NBPE's NAV.

NBPE's current portfolio is well diversified across industries and sponsors. As at end-May 2021, NBPE holds positions in c 100 companies, with the largest position (automated robotic storage provider for warehouse industry Autostore) making up 5.8% of the portfolio's value. The companies are managed by established PE GPs, including the parent group of its investment manager NB (10.4% of the portfolio value as at end-February 2021, latest available data). Overall, the top five GPs manage 42% of NBPE's portfolio. The portfolio remains skewed towards North America (74%

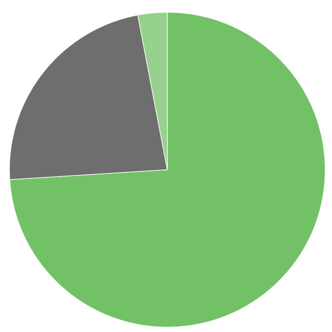
of the portfolio at end-May 2021), though exposure to European companies has been steadily increasing (now at 23% of portfolio vs 8% at end-2016).

Exhibit 3: NBPE's portfolio split by sponsor



Source: NBPE data as at end-May 2021

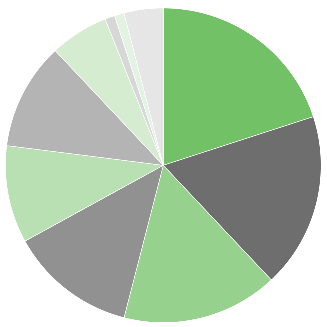
Exhibit 4: NBPE's portfolio split by geography



Source: NBPE data as at end-May 2021

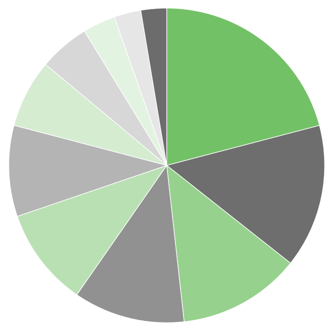
NBPE's portfolio is well diversified by sector, with the largest exposures to the IT and consumer sectors making up 20% and 18% of the whole portfolio, respectively. The sector diversification is broadly in line with that of MSCI All-World Index, with the largest difference being NBPE's 16% exposure to industrials, while it makes up only 10% of the index.

Exhibit 5: Portfolio split by sector



Source: NBPE data at end-May 2021

Exhibit 6: MSCI ACWI Index split by sector



Source: MSCI, data at end-May 2021

NBPE positions its portfolio for a range of possible macroeconomic conditions. It focuses on companies with low cyclicality and/or with long-term secular growth trends, as highlighted by its top 40 investments categorised into three main investment themes. 41% of the value of the top 40 investments represent tech/e-commerce companies, especially with broader tech applications including industrial technology (eg AutoStore). Another 27% in terms of value are allocated to low cyclicality sectors such as P&C insurance (USI) or waste disposal (GFL). Other investments with a thesis depending on long-term secular trends such as healthcare companies (favoured by ageing demographics in the US and Europe), represent 29% of portfolio value.

While NBPE's performance this year was driven by successful exits (with an average estimated multiple on invested capital for closed and pending transactions of 3.5x), we note that the remaining portfolio also performed well recently. We calculate that excluding new acquisitions and exits (also companies that performed partial exits/recapitalisations), the portfolio value increased by c 20% in 2020 (adjusted for any capital inflows from NBPE), which leads us to believe that NBPE still has potential for further successful exits from the portfolio. Some notable examples are PetSmart and Action. PetSmart is a retailer of specialty pet products in North America whose value (NBPE stake) increased to US$44.4m at end-2020 (end-2019: US$12.6m). Its main growth driver was its listed e-commerce subsidiary Chewy, which profited from an uptick in online shopping during lockdowns and more than doubled its capitalisation. Action is a non-food discount retailer with over 1,700 stores across Europe. It is continuing its rapid expansion with 164 new stores opened in 2020 (net of closings) and increasing its operating EBITDA to €0.6bn in 2020 (up 13% y-o-y).

NBPE also has a legacy portfolio of income and fund investments, which currently make up 10% and 1% of the portfolio value, respectively, as at end May. As at end-February (latest available data), the income portfolio consisted of six private debt positions and two NB debt programs. The NB Alternatives Credit Opportunities Program and NB Specialty Finance Program represented 51% of NBPE's income investments exposure.

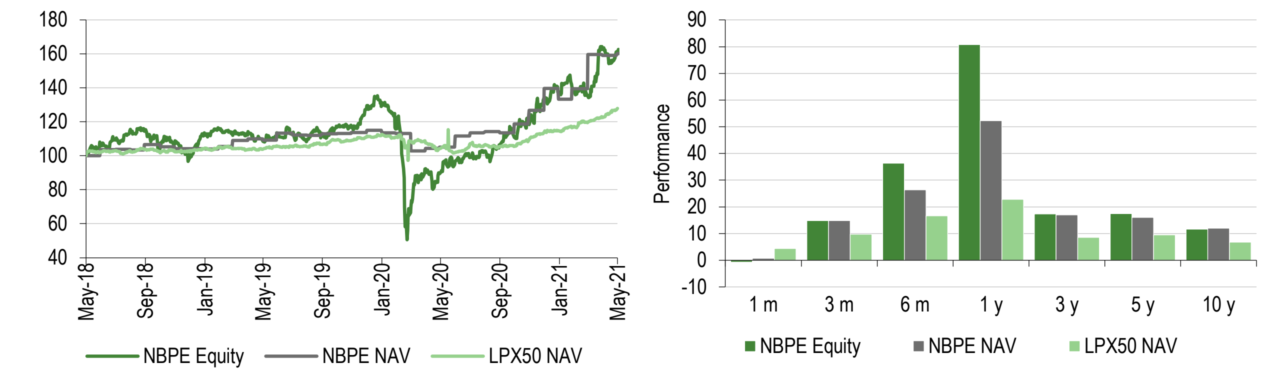
Performance: Driven by direct co-investments

On the back of recently executed and announced exits, paired with the late 2020 public markets rally, NBPE posted an estimated net asset value NAV total return (TR) in the last 12 months (LTM) to end-May 2021 of 52.3% in US dollar terms, clearly ahead of the LPX 50 NAV index posting a 22.9% return and compared to NBPE's five-year average return of 16.0% pa. We note that this performance comes from the low base at end-May 2020 after NBPE's NAV had declined 8.5% since end-2019 amid the broad equity market sell-off at the time. Having said that, the 17-month performance (since end-2019) was still a very strong 39.2% (LPX 50 NAV: 14.8%). We note that NBPE's portfolio valuation is subject to a lag typical for funds relying on third-party GP valuations and as at end-May the portfolio was valued as at end-March 2021 (except for public exposure).

NBPE's long-term NAV TR performance is also ahead of the LPX 50 NAV Index, despite the fact that it covers a period when NBPE gradually reduced its exposure to fund investments and income investments in favour of direct co-investments (see our initiation note for details).

Exhibit 7: NBPE performance to 31 May 2021 in US dollar terms

Price, NAV and index total return performance, three-year rebased | **Price, NAV and index total return performance (%)**



Source: Refinitiv, Edison Investment Research. Note: Three- and five- and 10-year performance figures annualised.

NBPE's direct PE co-investments (representing 89% of its investment portfolio at end-May 2021) generated a 12-month gross internal rate of return (IRR) of 52.8% (see Exhibit 8) through the end of April 2021, supported in particular by the ongoing exits. The remaining portfolio also performed well, driven by NBPE's significant exposure to TMT and healthcare, as well as its selective approach to consumer and industrials investments (eg high emphasis on consumer companies with significant e-commerce exposure). Consequently, NBPE's investment manager believes that the portfolio is well-positioned for future growth. The weighted average LTM EV/EBITDA of NBPE's 75 private holdings (representing c 80% of its direct portfolio value) reached 15.5x compared to the end-2019 multiple of 12.1x (net debt to EBITDA was 5.8x and 4.8x, respectively). In addition, the weighted average LTM revenue and EBITDA growth was 6.2% and 6.1% respectively. The results growth was driven mostly by companies in TMT, healthcare and financial services sectors and, based on our conversations with management, we understand that growth was mostly organic. We note that the above analysis of operating metrics of portfolio companies was based on latest available data from the underlying sponsors, partially at end-December 2020 and partially end-September 2020 and weighted by NBPE's stake.

Exhibit 8: NBPE's gross IRR pa by asset class at end-May 2021

	1 year	3 years	5 years	10 years
Direct equity investments	52.8%	19.6%	21.0%	19.5%
Income investments	23.3%	12.6%	11.9%	10.8%

Source: NBPE data. Note: Total portfolio performance also includes NBPE's fund investments, which currently represent a minor part of the portfolio (c 2%). Fund investments' one-year, three-year, five-year and 10-year gross IRRs were 56.1%, 1.5%, 5.4% and 6.8%, respectively.

Peer group comparison

We present a peer group comparison of listed PE funds in Exhibit 9. Due to the limited number and comparability of direct PE funds, as well as NBPE's unique business model, we also include a fund-of-funds subgroup, which represents a more distant comparator to NBPE's performance. Recent strong valuation uplifts in NBPE's portfolio have placed NBPE's NAV among the top performers within the group. This is despite some negative currency effects arising from the fact that our comparison is in sterling terms. While NBPE's portfolio is predominantly in North America, most of its peers (except HarbourVest Global Private Equity and Pantheon International) have a 50% or greater exposure to Europe (including UK). Given that over the last year to end-May 2021, the US dollar depreciated c 13% versus the sterling and c 9% versus the euro, currency headwinds dampened NBPE's performance against peers. NBPE's 10-year NAV performance is above the peer group average, despite the fact that over the 10-year period, NBPE's portfolio mix significantly changed to direct co-investments from income and fund investments (which generated a lower IRR, see above). At the same time, NBPE continues to trade at wide discount, as described in the discount section below, currently the highest in the peer group.

Exhibit 9: Listed private equity investment companies peer group at 18 June 2021* (in sterling terms)

% unless stated	Market cap £m	NAV TR 1 year	NAV TR 3 year	NAV TR 5 year	NAV TR 10 year	Discount (cum-fair)	Ongoing charge**	Perf. fee***	Net gearing	Dividend yield
NB Private Equity	**626.6**	**32.5**	**49.9**	**115.0**	**258.3**	**(26.5)**	**2.1**	**Yes**	**114**	**3.4**
HgCapital Trust	1,447.4	43.3	88.0	162.5	286.1	(1.0)	1.8	Yes	100	1.5
Oakley Capital Investments	628.5	18.2	71.6	116.2	157.4	(13.6)	2.5	Yes	100	1.3
Princess Private Equity	769.4	33.8	50.9	113.4	178.2	(12.2)	1.9	Yes	100	4.8
Direct funds average	**948.4**	**31.8**	**70.2**	**130.7**	**207.2**	**(9.0)**	**2.0**	**-**	**100**	**2.6**
BMO Private Equity Trust	299.5	22.7	52.6	98.2	188.7	(16.7)	1.3	Yes	115	4.0
HarbourVest Global Private Equity	1,653.2	22.4	71.7	127.6	323.0	(21.9)	1.5	Yes	100	0.0
ICG Enterprise Trust	701.4	22.5	53.1	109.3	210.8	(26.3)	1.5	Yes	100	2.3
Pantheon International	1,414.4	22.8	45.8	93.4	219.0	(22.0)	1.2	Yes	100	0.0
Standard Life Private Equity	681.1	16.3	48.9	98.5	194.3	(15.9)	1.1	No	100	3.0
Funds of funds average	**949.9**	**21.3**	**54.4**	**105.4**	**227.2**	**(20.6)**	**1.3**	**-**	**103**	**1.9**
Average (8 funds)	**949.4**	**25.2**	**60.3**	**114.9**	**219.7**	**(16.2)**	**1.6**	**-**	**102**	**2.1**
NBPE rank in sector	**8**	**3**	**7**	**4**	**3**	**9**	**2**	**-**	**1**	**3**

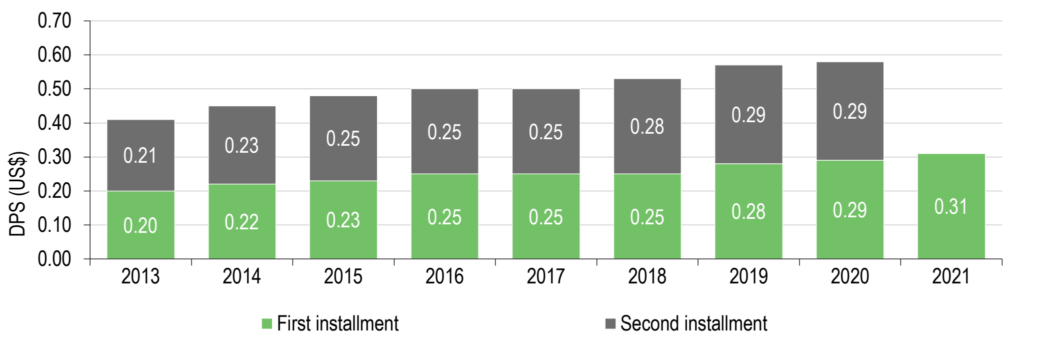
Source: Morningstar, Refinitiv, Edison Investment Research. Note: *12-month performance based on latest available ex-par NAV (end-May for NBPE, end-April for Princess Private Equity, HarbourVest Global Private Equity and Standard Life Private Equity; end-March for HgCapital Trust; end-January for ICG Enterprise Trust; and end-December 2020 for Oakley Capital Investments and BMO Private Equity Trust). **Ongoing charge at fund level only; does not capture the second layer of fees in the fund of funds subgroup. ***Performance fees paid at underlying funds level. Net gearing is total assets less cash and equivalents as a percentage of net assets. 100=ungeared.

Dividends

NBPE pays dividends semi-annually (in February and August) and targets a payout of at least 3.0% of NAV annually. Simultaneously, management does not intend to decrease dividend per share in the event of a short-term NAV decline. Unlike many of its peers, NBPE did not suspend dividend distribution during the turbulent year of 2020, paying out US$0.58, implying a 3.0% yield on opening NAV. Consequently, the first instalment paid out in January 2021 (US$0.31 per share) implies an annualised 2.8% yield on end-2020 NAV and 3.3% yield on the current share price (NAV per share at end-2020 stood at US$22.49 vs end-May 2021 at US$25.43). Shareholders may choose to receive dividends either in sterling or in US dollars, and there is also a dividend reinvestment plan in place.

Subject to board decision, NBPE is permitted to pay dividends as long as it meets requirements under its credit agreements and ZDP coverage tests (see Gearing section on page 10). We calculate that with the current investment level and upcoming disposals, NBPE is well positioned to continue distributing dividends in the near term.

Exhibit 10: Dividend history since FY13



Source: NBPE, Edison Investment Research

Discount: Still wider than before the pandemic

NBPE currently trades at a 26.5% discount, significantly above the pre-COVID-19 level (16.1% at end-2019), despite continuous narrowing from a trough level of 67% amid the broad market sell-off of early 2020. This has been an effect of a share price rally (one-year TR to end-May 2021 at 80.8% in US dollar terms) paired with strong NAV performance (52.3%, analogously).

NBPE trades at discount levels more common among funds-of-funds despite its one-layer fee structure. We also note that NBPE has repositioned its portfolio over time, gradually increasing its direct equity investments (from income and fund investments) and we currently consider NBPE a pure-play direct equity fund. This is underpinned by its recent performance, which is in line with the direct equity funds average, while ahead of most fund-of-funds peers.

The share buyback programme was reintroduced in January 2019 (with previous buybacks conducted in 2008–09 and 2010–12) as an effective use of capital given the prevailing discount to NAV. In the initial stage of the COVID-19 pandemic NBPE focused on capital preservation and the programme was suspended (as described in the Capital structure section on page 11).

Exhibit 11: Discount over three years

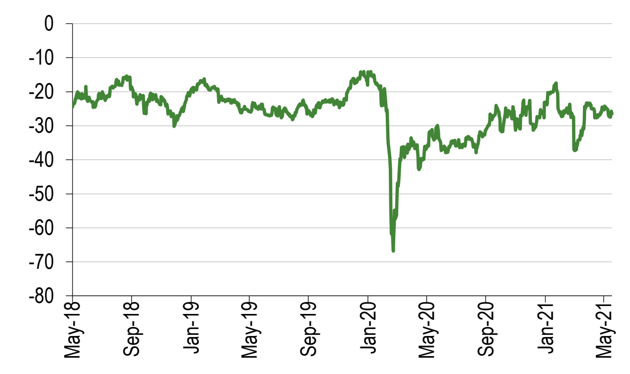
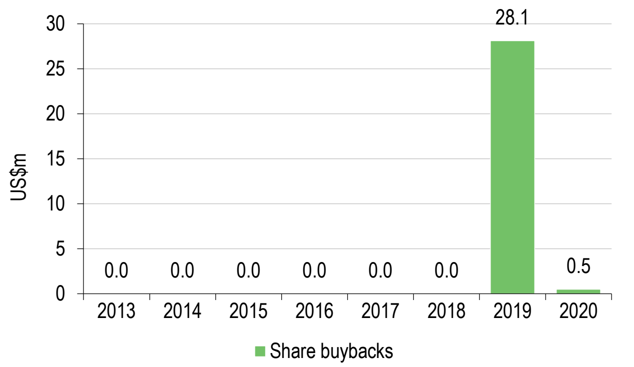


Exhibit 12: Buybacks and issuance



Source: Refinitiv	Source: Morningstar

Fund profile: Focus on direct PE co-investments

NB Private Equity Partners is a closed-end PE investment company incorporated in Guernsey and listed on the London Stock Exchange since 2009. It was established in 2007 as Lehman Brothers Private Equity Partners Limited, raising US$400m from external investors and US$100m from Lehman Brothers (LB). Following the management buyout (MBO) of NB from Lehman Brothers in 2008, the fund was renamed while the manager continued to manage the fund as part of the MBO.

The initial portfolio was acquired from LB and consisted predominantly of investments as limited partner (LP) into funds externally managed by GPs (fund investments, c 76% of portfolio value), while direct PE investments represented just c 24% at that time. Since then, the fund investments exposure has been steadily reduced in favour of direct PE co-investments, where the leading sponsor retains full control over the company, and NBPE invests alongside as minority shareholder (this investment type accounted for 89% of NBPE's portfolio at end-March 2021). In 2012, NBPE expanded its portfolio to include income investments, covering senior debt (both first and second lien), as well as mezzanine loans issued to PE-backed companies. However, in recent years it has reduced exposure to this asset type to only 10% of portfolio value at end-August 2020 (vs 39% at its peak in 2014). Consequently, NBPE has become a pure-play direct PE co-investment vehicle (investing alongside high-quality lead sponsors), which is intended to be the predominant investment strategy going forward. Since 2015, NBPE has invested over US$700m in more than 80 direct equity investments, and has a supplementary modest exposure to PE debt investments and legacy PE funds.

Investment process: Leveraging expertise of lead sponsors

NBPE leverages NB's broader platform for deal origination (in particular NB's primary PE platform). The investment manager performs an independent due diligence (on top of the analysis conducted by the sponsor) with 10-15% of the opportunities being pursued. The investment selection process is based on evaluating the merits and risks of individual companies as opposed to favouring industries and macrotrends. Moreover, the company normally invests in industries that are 'sweet spots' of the respective sponsor. As a result, it does not impose any target allocations in terms of industry and its sector diversification is a function of opportunities arising with the respective GPs. The deal flow is allocated across NB's PE strategies depending on demand from the respective funds and based on a pre-defined pro-rata allocation policy to avoid favouring any of them. Having said that, NBPE analyses each investment individually and favours industries characterised by more attractive macro trends, as described in the Current portfolio positioning section on page 4.

Once the transaction is completed, NBPE relies on the value creation capabilities of the lead sponsor. While the investment agreement normally covers certain protective and information rights for the company, it is typically not entitled to board representation or any similar control over the investment. The decision with respect to the exit timing is also in the hands of the lead sponsor.

NBPE's approach to ESG

NBPE has adopted a responsible and sustainable investment policy, which is aimed at producing better investment outcomes through incorporating environmental, social, and corporate governance (ESG) considerations into the investment process. According to the manager's assessment framework, 27% of NBPE's portfolio exhibited positive sustainability potential at end-December 2020, while only 1% had an adverse effect on environment and/or society. According to the management, the positions with an adverse effect represent legacy positions and NBPE does not intend to invest in such companies going forward. The remaining part was characterised as neutral, that is having mixed or unknown benefit to people or the environment. Each deal team at NB analyses ESG considerations of each potential investment, supported by specialised PE ESG team members if necessary. Moreover, NB has an in-house ESG committee consisting of NB's president and CIO-equities as well as senior representatives from different verticals, including PE. NB has been a signatory of the Principles for Responsible Investment since 2012 and obtained the highest PRI score of A+ in the most recent assessment. NB has also been ranked first or second in the Pensions & Investments Best Places to Work in Money Management survey (among those with 1,000 employees or more) for five consecutive years.

Gearing: Down and back to targeted level

NBPE applies structural leverage at the company level through zero dividend preference shares (ZDPs, described in our initiation note) and also uses a credit facility to bridge investments and support its liquidity. It intends to maintain an investment level at 110–120% (defined as fair value of investments to NAV), which at end-May 2021 was 116%. The conclusion of already announced exits would, all else being equal, bring the level below the target range (c 100% according to our estimates, but we reiterate that the disposals should arrive gradually and will likely be reinvested over time).

NBPE has two series of ZDPs outstanding, with an aggregate value of US$166m as at end-May 2021. They mature in 2022 (US$85.5m) and in 2024 (US$80.5m). They are subject to a cover test according to which NBPE's gross assets divided by the sum of ZDP final capital entitlement upon redemption and the aggregate amount payable on maturity in respect of any other liabilities due before the ZDP repayment date should be greater than 2.75x. We calculate that, as at end-May 2021, the cover test for 2024 ZDPs stands above 7.0x (over 13.0x for the 2022 ZDPs), well ahead of the threshold level. NBPE has a US$300m credit facility (expanded amid liquidity concerns during pandemic outbreak), of which only US$10m was drawn at end-May. The credit line has a loan-to-value (LTV) covenant at 45% (which does not include ZDPs), and we calculate that it stood at 0.7% at end-May 2021.

All the above provides NBPE with significant headroom to pursue new investments and deploy proceeds from incoming disposals into the portfolio, as well as distributing dividends. Naturally, structural gearing enhances portfolio returns in a bull market and amplifies losses in a bear market. Having said that, NBPE withstood 2020 exceptionally well and given the current expectations of an economic recovery (as described in Market outlook section), NBPE's leverage may amplify its returns going forward.

Fees and charges: One-layer fee structure

NBPE is subject to an attractive one-layer fee structure, which means that it generally does not pay any management fees nor carried interest to underlying GPs (as at end-2020, 96% of the direct investment portfolio was free of GP charges), while at the same time it benefits from their expertise. NBPE's charges effectively translate to 1.50% of NAV (management) plus 7.50% of gains in the period. NBAA collects a management fee equal to 1.5% of the PE investments' value. This effectively translated to 1.5–1.9% of NAV annually in 2016–20 mostly due to applied leverage. We note that NBPE generally does not pay any management fees nor carried interest to underlying GPs (as at end-2020, 96% of the direct investment portfolio was free of these GP charges). After accounting for operating costs and administration fees, the ongoing charges amounted to 2.24% in FY20, above its three-year average of 2.03% (2016–19). The investment manager is also entitled to a performance fee, which is set at 7.5% of NAV accretion (including dividends paid), subject to a

7.5% hurdle rate and an absolute high-water mark. In FY20, the performance fee amounted to US$15.2m, which has driven the total charge to 3.80% of average NAV based on our calculations (2.62% on prior three-year average). The higher charge compared to previous years stems from the better performance, as the 2016–19 average NAV uplift stands at 9.1% annually, compared to 20.9% in FY20. In the exhibit below, we compare NBPE to other listed PE funds available to investors.

Exhibit 13: Comparison of fees in vehicles available to investors*

Fund type	Management fee at vehicle level	Performance fee at vehicle level	Underlying fees
Listed fund-of-funds	c 1.0–1.5% of NAV	0–10% after hurdle and exceptions	1.5–2.0% + 20% carry
Listed direct PE	c 1.5% of NAV	15-20% carry	-
NBPE	1.5% of portfolio value	7.5% if hurdle is met	**

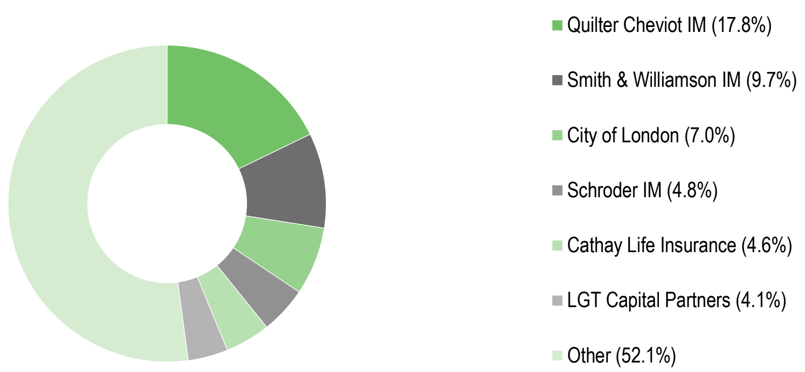
Source: Edison Investment Research. Note: *Based on funds in NBPE's peer group, see Exhibit 9, **NBPE's portfolio is largely exempt from fees.

Capital structure

NBPE's share capital consists of 49.9m class A shares, of which 46.8m were outstanding as at end-May 2021. There are also 0.01m class B shares, which were issued during the IPO to a charitable trust (First Directors Limited serves currently as trustee), which participate in profits equally to class A shares, but ordinarily carry no voting rights. However, if the level of ownership of outstanding class A shares by US residents exceeds 35%, the class B shares will automatically gain voting rights in a sufficient amount to dilute the voting power of US residents below 35% only in respect of director resolutions. According to the company, currently US residents make up far less than that threshold in the shareholder base. NB does not hold any shares in NBPE and company's management's shareholding is marginal: 0.3%.

The management is authorised to buy back up to 14.99% of class A shares within the current programme (started in January 2019), which was temporarily suspended in March 2020 after buying back only 0.08% of shares in FY20 (on top of 4.06% bought in FY19). The potential share repurchase can be carried out at market price.

Exhibit 14: Major shareholders at 21 June 2021



Source: NBPE

The board

NBPE's management board consists of five directors, four of whom are independent. Peter von Lehe is a managing director at NB and did not receive any remuneration from NBPE in 2020. We note that Peter von Lehe will step down at the next AGM and the board will be fully independent going forward. With the recent appointment of Louisa Symington-Mills as a non-executive director, the board will consist of five members after the 2021 AGM.

Louisa Symington-Mills has an extensive experience in buy- and sell-side private equity. She has been active in the industry since 2003, most recently as a COO of LPEQ – an international association of listed private equity companies. She is also the founder and CEO of Cityparents – an organisation supporting working parents in corporate roles. For description of experience and responsibilities of the remaining board members, see our initiation note.

Exhibit 15: NB Private Equity Partners' board of directors

Board member	Date of appointment	Remuneration in FY20	Shareholdings*
William Maltby (Chairman)	21 March 2019	US$89,834	0.28%
Trudi Clark	24 April 2017	US$64,169	0.04%
John Falla	21 December 2015	US$76,983	0.02%
Wilken von Hodenberg	21 March 2019	US$63,388	0.01%
Peter von Lehe	22 June 2007	-	0.19%
Louisa Symington-Mills	15 June 2021	-	-

Source: NBPE. Note: *As at 22 April 2021.

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