4 trends that will have a major impact on private equity in 2021

By Bryan Turner

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Amidst the general chaos of 2020, investors were hit hard. With economies around the world all but shutting down in March, activity ground to a halt. But as people found ways to work around the restrictions of the pandemic, businesses were able to resume operations and most asset classes began to pick up again, recover, and in some cases thrive.

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Private equity (PE) activity, in particular, recovered quickly. Fuelled by ultra-low interest rates in developed markets and stock market uncertainty, investors sought stability and returns in the longer-term focused PE space. And since early indicators suggest that 2021 will offer little more in the way of stability, that's a trend likely to continue through the course of the year.

In fact, some commentators predict fundraising in the US will surpass the $316.9bn high-water mark set in 2019 as institutional investors allocate more to PE.

But even within that context, there are still several key trends that will influence what happens in private equity in 2021. Here are a few of the most important ones.

1. ESG's growth continues

Environmental, social, and governance (ESG)-driven investing saw massive growth in 2020. These investments also generated outsized returns. A FTSE index of global stocks with significant involvement in environmental markets is, for example, up 35% this year, outperforming the global equity benchmark by more than 20 percentage points.

In certain circles, this has led to fears of an ESG bubble. But that kind of thinking ignores the fact that ESG-focused companies are likely to lead the post-Covid recovery. In the wake of the pandemic (and the clean skies that accompanied cities locking down), people have realised that business cannot carry on as usual.

The growth in ESG isn't just a public markets phenomenon either. In fact, private equity might be better geared to foster sustained ESG growth. PE firms focus not only on generating returns for investors but also on contributing to the overall well-being of the companies they invest in. That's a good thing from an ESG perspective, as it means they won't sacrifice long-term vision and values for short-term shareholder gains.

Expect to see further PE-driven ESG growth in 2021.

2. Emerging markets will likely remain underrated

Towards the end of 2020, the political situation in the US and UK was seriously tenuous, with the general election seemingly set to end in chaos and no Brexit deal in sight. Fast forward to the beginning of 2021 and Joe Biden has been elected US president with a slim senate majority, while Boris Johnson managed to finalise a trade deal with Europe.

That said, there are still a number of unknowns in both markets. While investors may feel calmer about these markets, it would be imprudent of them to ignore emerging market investments.

While there are undoubtedly risks in emerging markets, they are well known and understood. Investors can therefore mitigate for them. Post-Covid-19, entities in these markets will be more receptive than ever to investors.

Once trade returns to normal levels, investors could see much bigger gains than in developed markets.

3. Tech stays on top

Prior to 2020, there were rumblings of a second tech bubble, with inflated valuations pricing some investors out of the market.

By the end of the year, however, it had become clear how big a role technology could play in helping us adapt to the changing world around us. The boom in stocks such as Zoom, PayPal, and Amazon is just the beginning, however.

As the second and third-order effects of the pandemic become more evident, more technologies will emerge, while some will find new uses.

PE investors would do well to keep a close eye on potential tech investments, particularly in emerging markets where they could have an outsized impact.

4. Shifts in global trade

In 2020, the major global trade stories concerned the US's relationship with China, and Brexit. While many expect Joe Biden to repair some of the damage Donald Trump did to the relationship with China and Brexit finality to improve the global scenario, there are other emerging trade issues.

China and Australia have, for instance, been mired in a trade war of their own since December. New foreign investment rules set by countries including India, Japan and Australia look set to add new dimensions to trade considerations in the APAC region. Africa's long-awaited free trade agreement, on the other hand, finally kicked off at the start of January.

While these ructions shouldn't preclude anyone in PE from making an investment, they are worth watching.

Beyond the new normal

With 2020 having provided the biggest black swan event of a lifetime, we've now had months to adapt to the new normal. In 2021, PE investors will have to move beyond adapting, embrace the emerging trends, and make the most of the opportunities available to them.

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