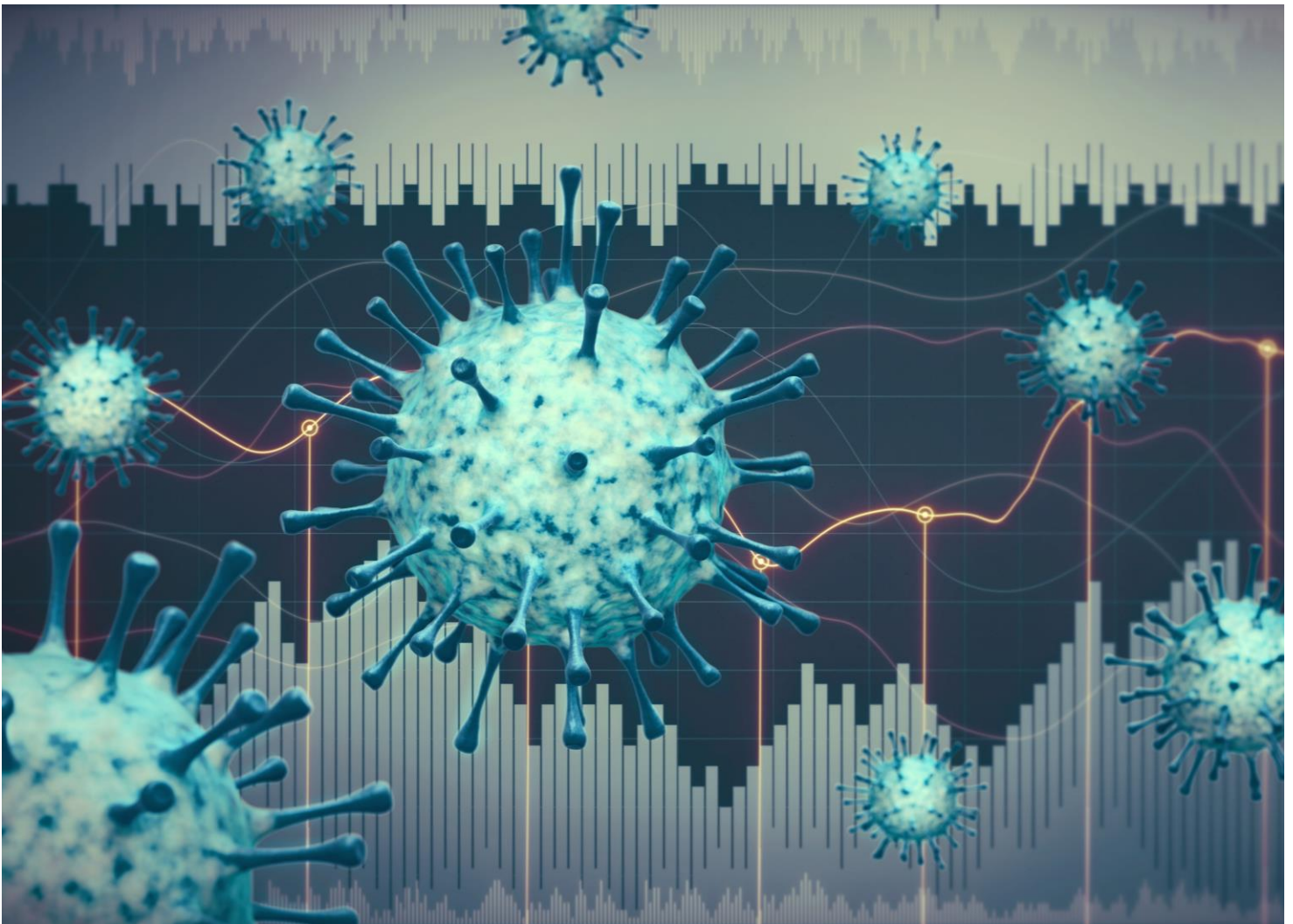


REPORT

THE IMPACT OF COVID-19 ON NORWEGIAN PRIVATE EQUITY



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Foreword

On behalf of the Norwegian Venture Capital & Private Equity Association (NVCA) and Oslo Business Region, Menon Economics has conducted a study of how Covid-19, and its consequences for the national and global market situation have influenced Norwegian private venture capital. The data presented in the report are based on a survey directed at both buyout and early stage funds located in Norway.

Menon Economics is a research-based analysis and consulting company working at the interface between business, economics and business and industry policy. We offer analysis and consulting services to companies, organizations and authorities. Our main focus is on empirical analyses of economic policy, and our employees are highly qualified within their area of expertise.

We would like to thank NVCA and Oslo Business Region for an interesting assignment. We also thank the fund managers that have contributed by replying to our survey. The authors are responsible for all content in this report.

September 2020

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Project manager
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Summary and main findings

The purpose of this report is to study how Norwegian private venture capital has been affected by Covid-19 and infection control measures in Norway and abroad. We have sent a survey to 58 Norwegian buyout and early stage funds asking how Covid-19 has influenced Norwegian private equity. The PE firms the survey is targeted at are characterized by so-called active ownership in the management of portfolio companies and contribute with competent capital directed at unlisted enterprises. The survey was concluded in the beginning of September 2020 and received 26 replies (a response rate of 45 percent). The respondents consist of nine fund managers representing buyout funds and 19 fund managers representing early stage funds.

The fund managers can be divided into three categories when it comes to how the pandemic has affected their existing portfolio. Almost half of the respondents experienced either weakened liquidity or reduced market opportunities in their portfolio (46 percent), approximately one fourth experience little impact (27 percent), while one fourth state that they have experienced improved liquidity and/or increased market opportunities (27 percent). There is also a difference with regards to stage focus. Norwegian buyout funds say that they are impacted by the Covid-19 situation to a limited degree. Among early stage fund managers, a larger share report that they have been affected negatively, both in the form of weakened liquidity in the portfolio companies and weakened opportunities to raise capital in the market.

The respondents generally state that Covid-19 has not affected their investment level. Only one respondent answers that they have invested less due to Covid-19, while two fund managers have invested more than they would have otherwise done. However, Covid-19 has affected the fund managers' sector focus. Several PE firms say that they will invest less in culture and tourism, the transportation and petroleum sectors as a consequence of Covid-19. The common denominator for these sectors is that they are, either directly or indirectly, impacted by the infection control measures in the form of reduced travel activity or by officially mandated restrictions with regards to the number of people that are allowed to congregate. The culture sector is particularly affected by these restrictions. Travel restrictions impact tourism and the transport sector directly. In addition to geopolitical factors, demand for petroleum products is also affected by Covid-19 due to reduced travel activity and a reduced need for transportation in general.

Covid-19 has also influenced the choice of sectors that fund managers want to invest more in. Amongst the sectors mentioned most frequently in this context are health care and life science, ICT, the technology industry and renewable energy. The importance of the health care sector has become very clear during the pandemic. The ICT-sector has become even more important due to more people working from home and more time spent at home in general, increasing demand for cooperation tools, software and content services. Increased focus on the technology industry and renewable energy are both connected to general trends in society that have been reinforced by economic stimulus packages related to Covid-19.

The fund managers have differing experiences when it comes to how Covid-19 has affected their opportunities to raise capital in the market. Of those who responded that they have experienced weakened opportunities, most had plans to raise capital in the market. The majority of fund managers either state that access to capital is unchanged, or that they are uncertain about effect on fundraising.

Introduction

The pandemic has led to major changes for both businesses and consumers. The capital markets reacted very negatively to the uncertainty in the beginning, but many sectors have recovered during the last six months. The market is however still experiencing large uncertainty and considerable fluctuations. The changes that have happened affect the market outlook and market conditions for private equity.

Covid-19 affects the activities of the PE funds in several ways. As during earlier crises, there is an impact on their existing portfolio companies, but also on the market outlook for future investments. It may also influence the capital markets and the funds ability to raise new money. Earlier crises have shown that private risk capital is resilient in case of a crisis, and funds that have been established during economic downturns have done well.¹ Despite this, the industry is by no means unaffected by crises, as can be seen by the number of transactions falling by 50 percent between 2007 and 2009, during the global financial crisis.²

An important difference between the corona crisis and earlier economic crises is that the fund managers themselves are directly affected by the infection control measures. The infection control measures require drastic changes in human interaction, both in a private and a professional context. Most communication happens via digital platforms, and consumer needs and requirements change quickly due to infection control measures.

In this report, we look more closely at all these aspects of Covid-19. The report is divided into three chapters. In chapter 1, we look at how the Covid-19 situation has affected existing portfolio companies. Chapter 2 consists of three parts and studies the impacts on investment activity, both the activity level and the investment process, before we have a look at the sector focus going forward. Finally, we study Covid-19's influence on access to capital in chapter 3.

¹ *Private Equity Insights (2020). The impact of Covid-19 on Private Equity Markets.* <https://pe-insights.com/news/2020/06/29/the-impact-of-covid-19-on-private-equity-markets/>

² *Bain & Company (2020). The impact of Covid-19 on private equity markets.* <https://www.bain.com/insights/the-impact-of-covid-19-on-private-equity/>

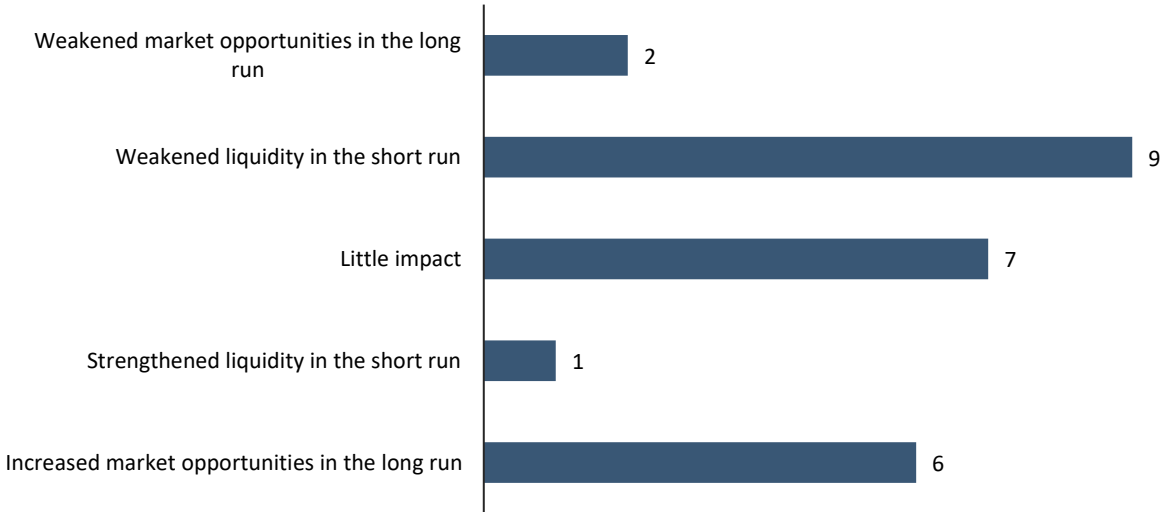
Covid-19 and existing portfolio companies

The fund managers can be divided into three categories when it comes to how the pandemic has affected their existing portfolio. Almost half of the respondents experience either weakened liquidity or reduced market opportunities in their portfolio. The remaining half states in equal parts that either Covid-19 has had little impact, or that they have experienced improved liquidity and increased market opportunities. The buyout funds say that their portfolio companies have been affected by the Covid-19 situation only to a limited extent, while a larger share of the early stage fund managers answer that there has been a negative impact.

A considerable number of companies have been directly affected by restrictions in connection with the lockdown of society due to Covid-19, with resulting loss of revenues. PE funds are also exposed to industries that have been negatively impacted by infection control measures. At the same time, other sectors have experienced increased demand for their goods and services as a result of Covid-19, for example suppliers of digital services and online retailers.

The fund managers' experience of how their portfolio companies are affected by the Covid-19 situation can be divided into three main groups (see Figure 1 below). Almost half say that there has been a negative impact on their portfolio companies (46 percent), while the remaining half is split between little or no impact (27 percent) or positive impact on their portfolio as a whole (27 percent).

Figure 1: To what extent have your existing portfolio companies been affected by the situation? (N=26)



The majority of fund managers who say that they have experienced weakened liquidity in the short run are early stage funds. Half of early stage funds report this (see appendix for respondents split by stage focus). Among the fund managers who say that they experience weakened liquidity in their portfolio, all but one answered that they have available capital to strengthen the liquidity of their companies. At the same time, one in four early stage funds states that they see increased market opportunities in the long run. With uncertainty among investors and rapidly changing behavior patterns as a result of infection control measures, opportunities for innovation and growth are emerging for those who seize the chance. Three in nine buyout funds report that they have experienced positive effects. In other words, a larger proportion of the buyout funds see positive

consequences compared with early-stage funds. The buyout funds also state to a lesser extent that their portfolio companies have been affected in a negative direction, while half answer that the situation has not had much effect on their portfolio companies.

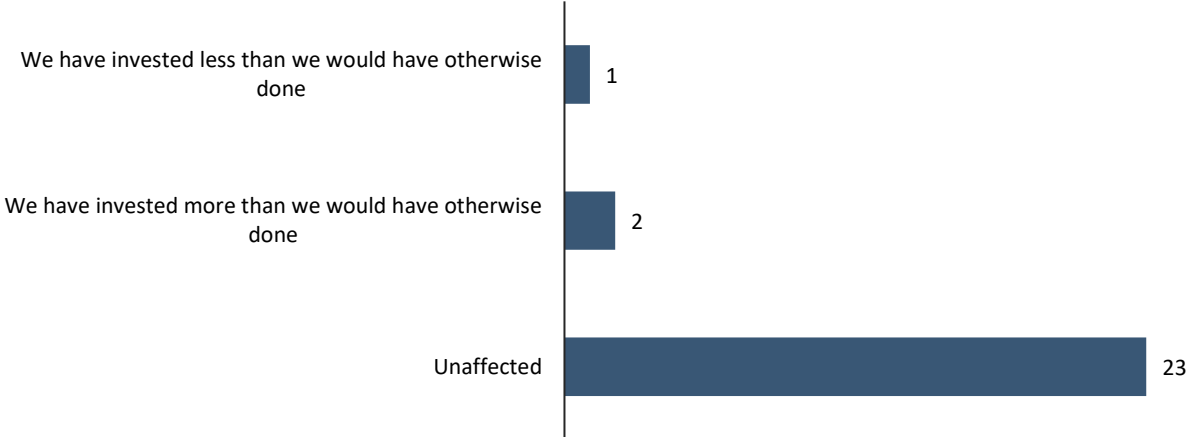
Covid-19 and investment activity

Although fund managers have been affected by infection control measures just like everyone else, investment activity has been maintained. Many PE funds however report a change in sector focus in the future, with a clear shift away from culture and tourism and the petroleum sector and towards health care and ICT.

Activity level and investment process

Despite comprehensive infection control measures in society and a challenging market situation worldwide, the investment level among Norwegian fund managers has been maintained (see Figure 2 below). The majority of fund managers report that their investment activity has not been affected by the infection control measures introduced due to Covid-19.

Figure 2: To what extent have the infection control measures in Norway related to Covid-19 and the global market situation affected your investment activity? (N=26)



Only one early stage fund manager responds that they have invested less than they would have otherwise done. Two funds answer that they have invested more than normal, both early stage funds (see Figure 8 in the appendix). All buyout funds state that their investment level is unchanged, despite the infection control measures. One possible reason for the difference between fund managers in early stage and buyout funds is that the investment process tends to be longer and more complex in the buyout segment. This means that many of the transactions that have been completed after infection control measures were in effect may have been started before the situation occurred. Despite this, the result shows that these transactions only to a lesser extent have been postponed or cancelled because of infection control measures.

Most early stage funds also report that their investment level is unchanged. At the same time, two of 19 report that they have invested more than they would have done otherwise as a consequence of infection control measures and the global market situation. This indicates that some fund managers have identified new opportunities despite the demanding situation we have experienced since March. Uncertainty and potentially reduced access to capital for companies in an early stage, due to uncertainty amongst investors, can create opportunities for lower pricing, as we have seen in earlier crises. In addition, abrupt changes in society lead to innovation and new market opportunities for those who are able to seize them.

The fund managers have however not remained entirely unaffected by the infection control measures, although investment levels have not changed. Due to closed offices and infection risk, working from home office and the absence of travel activity have impacted investment processes. When asked how and to what extent the infection control measures have influenced investment processes, most fund managers point towards less travel activity and increased use of video meetings as changes in their processes. Video meetings instead of physical meetings lower the threshold for starting a dialogue, which in itself can improve interaction and communication. Many believe that this shift may be permanent, as they experience it as a good alternative to physical meetings. This is an example for abrupt changes in society in a limited period resulting in permanent opportunities by forcing people to adopt new solutions. As a direct by-product of infection risk and restrictions related to Covid-19, we have seen the first wholly digital IPOs in Norway of Viking Ventures' portfolio company, Merzell. Merzell is the leading European eTender system and was listed on Merkur Market in June.

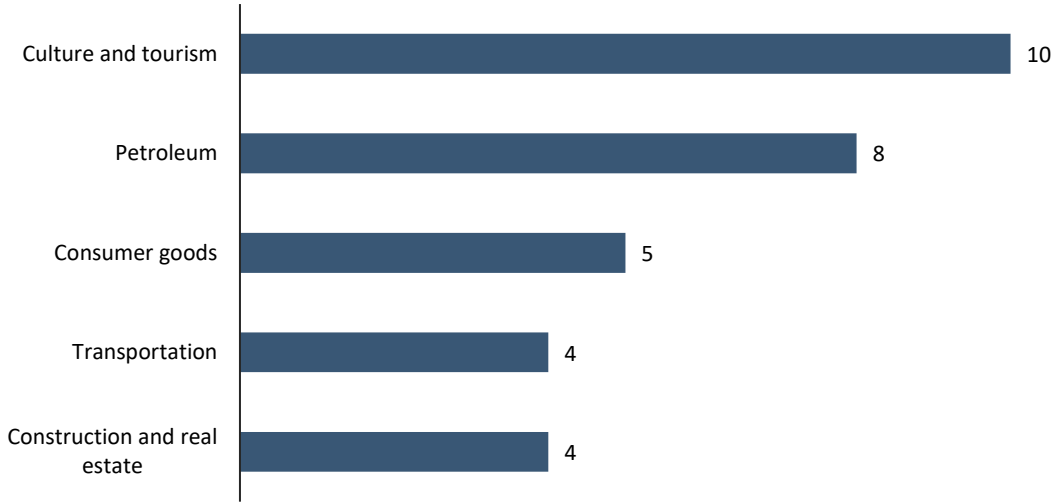
This however does not apply to the whole investment process, especially not when it comes to concluding an investment. Investors still find it desirable to physically meet with the management of the company before they finalize an investment, and equally demanding to not have this opportunity now. Building new relations with is seen as challenging in the absence of physical meetings. At the same time, this is reported to be unproblematic with regards to existing relations.

Sector focus is changing due to Covid-19

Although the level of investment is unchanged, many fund managers report a change in sector focus for their future investments. All actors in the economy are affected by infection control measures, while there are some sectors that have been impacted more than others, both in a negative and in a positive direction. The infection control measures have resulted in direct restrictions for tourism and culture. At the same time, the restrictions increase demand for content services and lead to increased awareness of the need for, and the importance of health care services. From the companies' viewpoint, tools for more digital interaction have become a necessity for their activity.

When questioned if there are any sectors the fund managers will invest less in due to Covid-19 and the global market situation, almost 40 percent respond that they will invest less into culture and tourism, and more than 30 percent answer that they will invest less into the petroleum sector (see figure below). This corresponds to the sectors that have taken the biggest hit from travel restrictions. Tourism has been hit particularly hard by this, in addition to the negative impact on global fuel and energy prices. Retail is also a sector that is regarded as less attractive for investment, according to the fund managers. The retail sector in Norway experienced reduced turnover during the lockdown, but has since recovered. Although we know that these sectors have been affected negatively, it is interesting to see the shift from the fund managers' point of view, as this also implies an expectation for permanent changes due to their long-term perspective on investments.

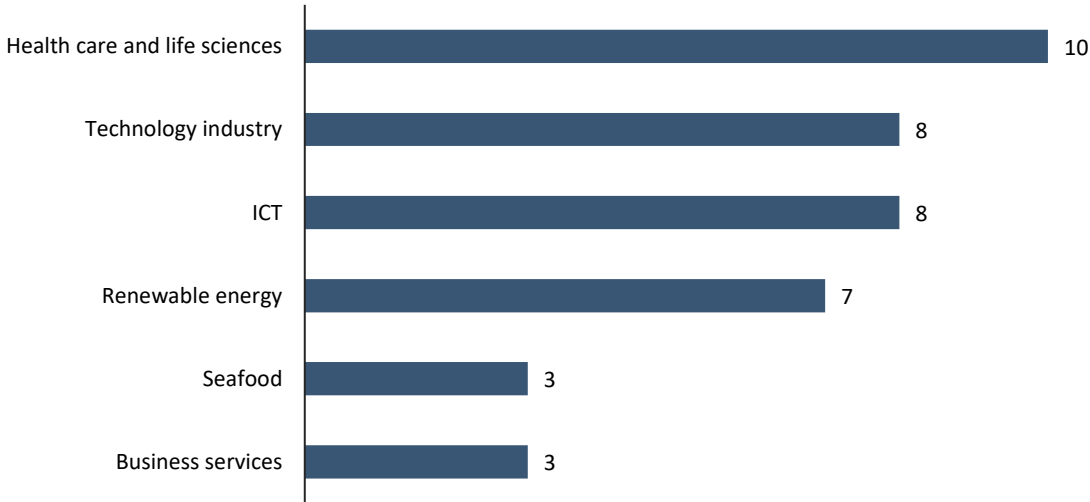
Figure 3: Are there any sectors you will invest *less* in as a result of Covid-19 and the global market situation? [Several alternatives possible] (N=26)



The sectors fund managers will invest less in coincide with the development we have seen in global stock markets. Companies within transport services, traditional retail and petroleum activities have experienced falling market values worldwide. In the case of petroleum, this has reinforced the underlying trend where capital is channeled towards renewable energy sources, also in Norway. At the same time, some fund managers see opportunities due to lower pricing or innovative solutions in these sectors. For example, platforms for e-commerce have experienced an upswing due to infection control measures.

The fund managers were also asked what sectors they will invest more in due to Covid-19, and as illustrated in Figure 4 below, there are four sectors that stand out: Health care and life science, technology industry, ICT and renewable energy.

Figure 4: Are there any sectors you will invest *more* in as a result of Covid-19 and the global market situation? [Several alternatives possible] (N=26)



Among the fund managers, as many as 10 in 26 answer that they will invest more in health care and life science. This is a sector that already attracts a lot of capital, but has increased even more as a result of the Covid-19 situation. Especially awareness around preparedness in the health care sector, including health care services and

biotechnology, has increased considerably due to the present situation. This is reflected in the sector's attractiveness for the fund managers, and especially among early stage fund managers.

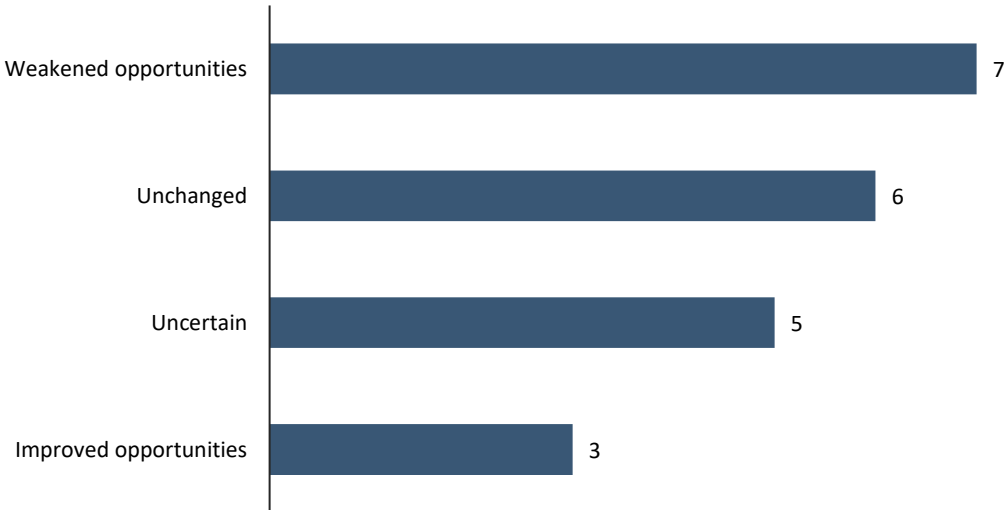
Also, technology industry, ICT and renewable energy are sectors the fund managers are planning to invest more in due to Covid-19. Around one third of the respondents point out that these industries have become more attractive. The ICT industry's services have become more important for both business and industry and for consumers. Less physical presence in favor of digital interaction and communication has resulted in higher requirements on the tools that are used. We have seen stock prices of technology companies increasing considerably because of people working from their home office, for example Zoom. In addition, people spend more time at home rather than travelling or visiting cultural venues. Renewable energy is seen as an attractive sector to invest in and is thus a counterpart to the declining focus on the petroleum sector.

Covid-19 and fundraising

The fund managers have differing expectations for, and experiences with, how Covid-19 affects the opportunities to raise new capital in the market. This is the case for both early stage funds and buyout funds. Amongst those who report that access to capital has been weakened, most have been in the market to raise capital during the last six months, while some early stage funds say that access to capital has improved. The majority of fund managers report unchanged access to capital as a result of Covid-19, or that they are still uncertain with regards to this.

The uncertainty related to the pandemic and how long comprehensive infection control measures and restrictions will continue results in uncertainty in investors. This uncertainty will often manifest itself in reduced access to new capital for fund managers, and consequently also for portfolio companies. The picture of how fund managers report they are affected by the situation is however mixed. We asked the fund managers in which way Covid-19 has affected their opportunities to raise capital in the market. The answers are presented in Figure 5 below.

Figure 5: In which way has Covid-19 affected your opportunities to raise capital in the market? (N=21)



A third of respondents answer that they experience weakened opportunities to raise capital. There is no clear division here between early stage and buyout (see Figure 11 in the appendix). Fund managers who experienced weakened opportunities to raise capital were also asked whether they were planning to raise capital in 2020, and five of seven respondents answer that they originally intended to raise capital in 2020. The fact that most actors reporting weakened opportunities to raise capital actually have been in the market trying to do raise capital makes their answers highly credible. Six of 21 respondents experience that access to capital is unchanged.

There are also some fund managers that experienced improved access to capital in the market due to Covid-19, all of them from early stage funds. Some fund managers see opportunities in the market and have access to investors who support this. Approximately one in five fund managers says that they are uncertain with regards to the effects of Covid-19. This is likely due to the fact that raising capital has not been on their agenda for the last six months.

Appendix 1 – Survey and sector classification

Table 1: Questions in the survey aimed at PE fund managers

To what extent have your existing portfolio companies been affected by the situation?
Do you have available capital to strengthen the liquidity of existing portfolio companies?
To what extent have the infection control measures in Norway related to Covid-19 and the global market situation affected your investment activity?
Why have you invested less than you would have otherwise done?
Why have you invested more than you would have otherwise done?
Are there any sectors you will invest less in as a result of Covid-19 and the global market situation?
Are there any sectors you will invest more in as a result of Covid-19 and the global market situation?
Can you briefly explain why and to what extent infection control measures have affected your investment processes (e.g. use of digital tools)? Do you think the experiences from Covid-19 will have any permanent effect on your investment processes?
In which way has Covid-19 affected your opportunities to raise capital in the market?
Were you originally planning on raising funds in 2020?

Table 2: Sector classification in the survey

Sector
ICT
Consumer goods
Culture and tourism
Petroleum
Technology industry
Business services
Construction and real estate
Health care and life sciences
Renewable energy
Food industry
Seafood
Process industry
Finance and insurance
Transportation
Other sectors

Appendix 2 – Results by stage focus

Figure 6: To what extent have your existing portfolio companies been affected by the situation? (N=26)

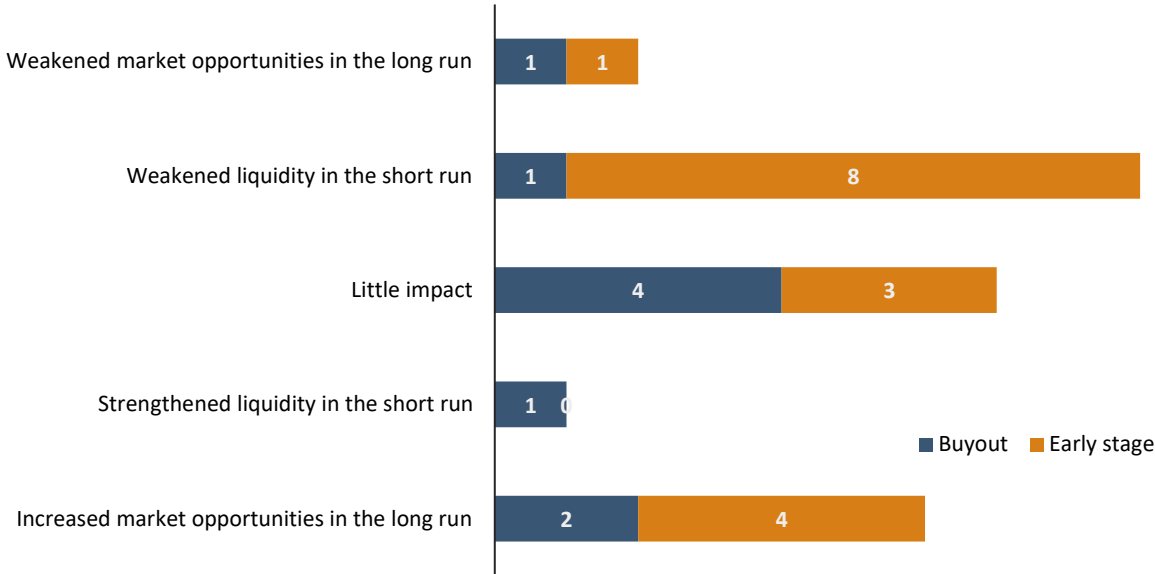
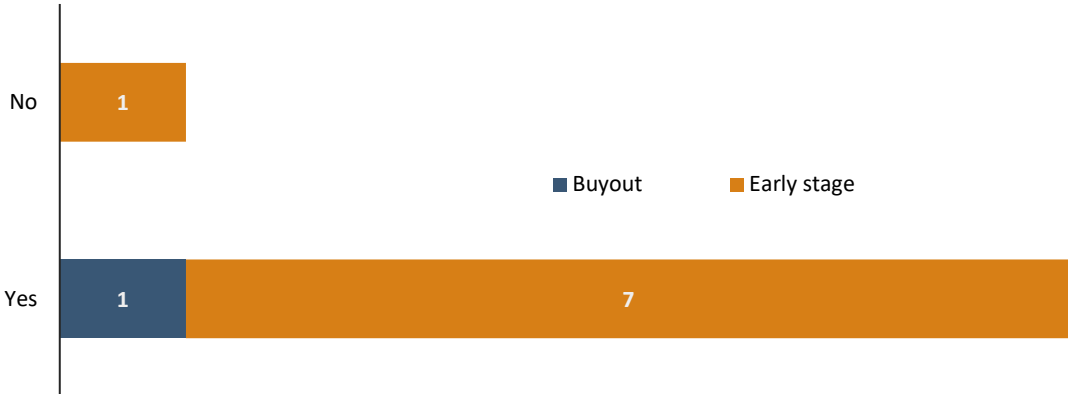


Figure 7: Do you have available capital to strengthen the liquidity of existing portfolio companies? (N=9)³



³ Contingent on having answered “We have invested less than we would otherwise have done” to the question “To what extent have the infection control measure in Norway related to Covid-19 and the global market situation affected your investment level?”

Figure 8: To what extent have the infection control measures in Norway related to Covid-19 and the global market situation affected your investment activity? (N=26)

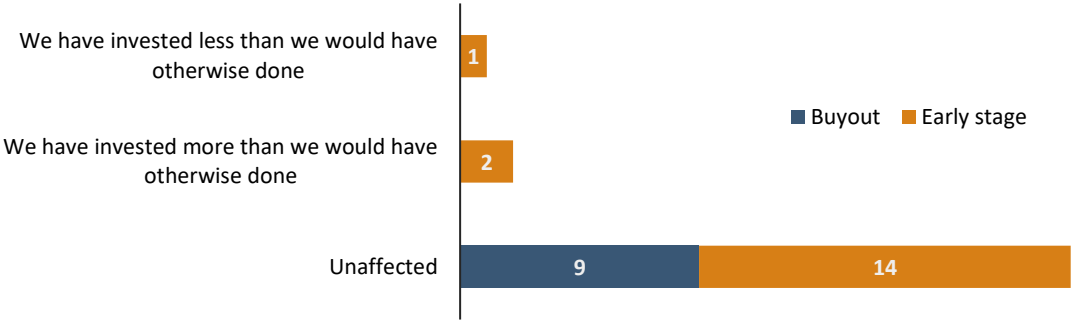


Figure 9: Are there any sectors you will invest less in as a result of Covid-19 and the global market situation? (N=14)

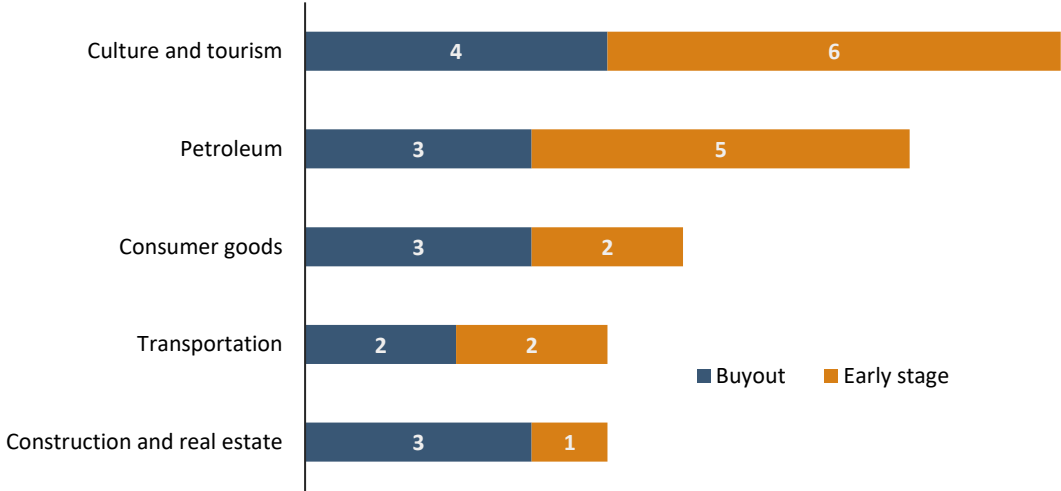


Figure 10: Are there any sectors you will invest more in as a result of Covid-19 and the global market situation? (N=17)

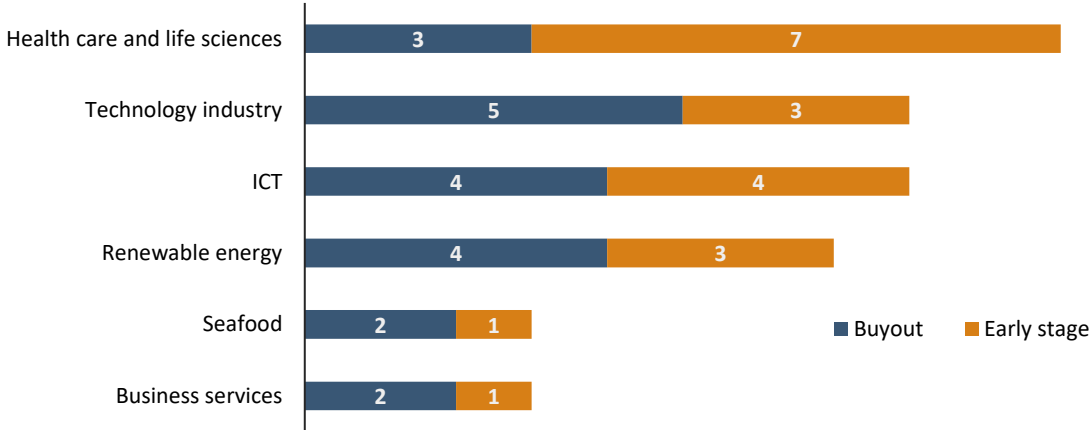


Figure 11: In which way has Covid-19 affected your opportunities to raise capital in the market? (N=21)

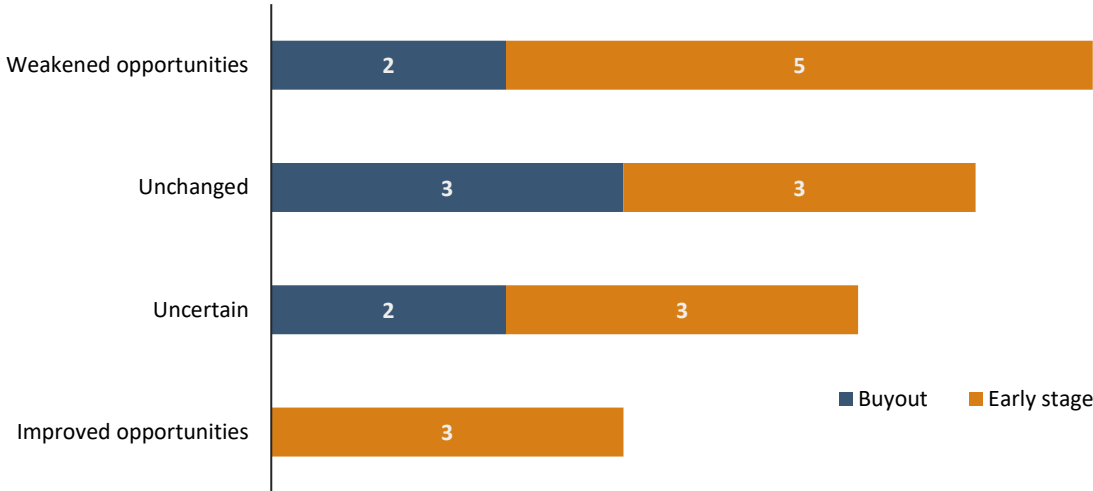
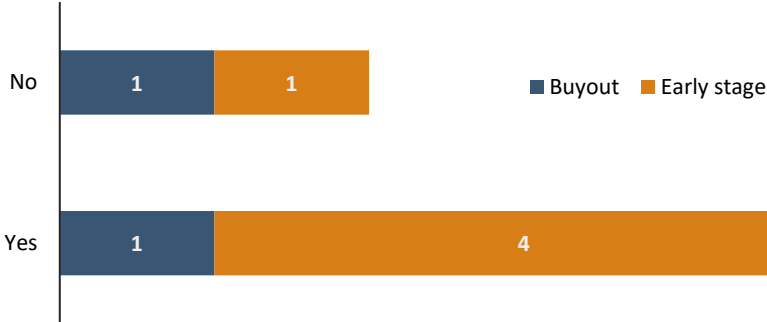
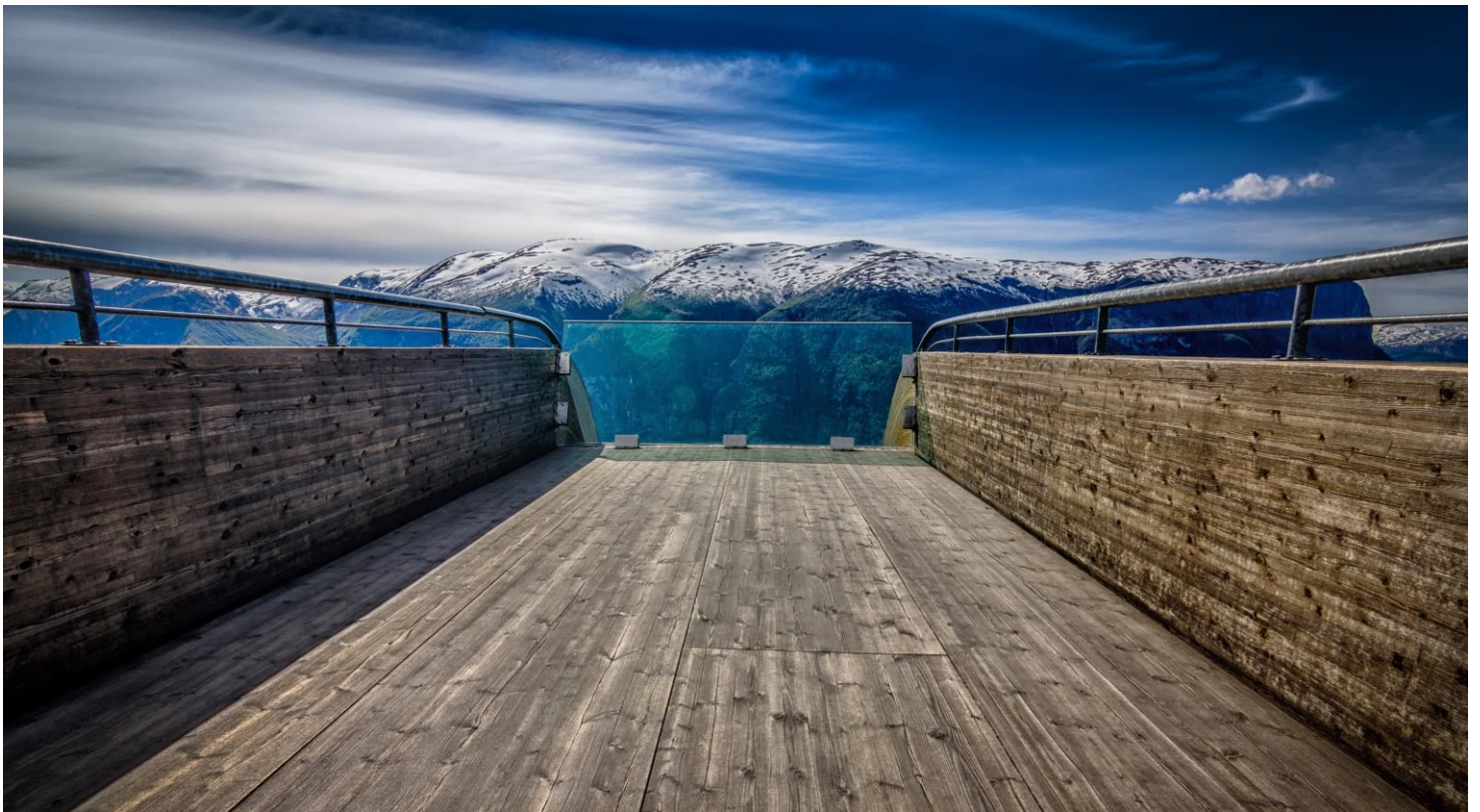


Figure 12: Were you originally planning on raising funds in 2020? (N=7)⁴



⁴ Contingent on the respondent having answered “Weakened opportunities” to the question “In which way has Covid-19 affected your opportunities to raise funds in the market?”.



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