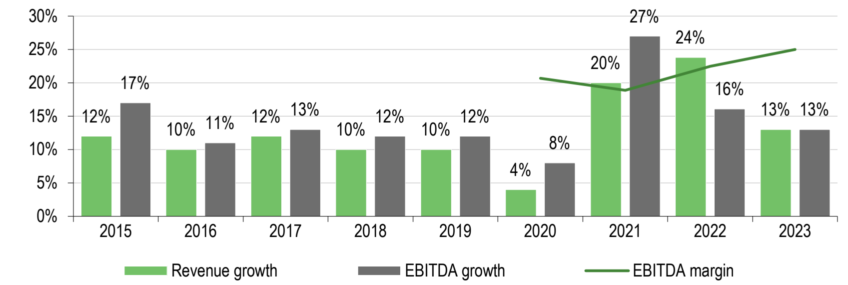
Princess Private Equity Holding

Introducing a well-defined buyback policy

Investment trusts
Private equity

Princess Private Equity Holding's (PEY's) 12-month NAV total return (TR) to end-February 2024 was a modest 0.6% amid low exit activity across private equity (PE) markets. That said, if the pick-up in global M&A volumes witnessed earlier in 2024 continues, it should support PEY's exit activity. This in turn would translate into improved returns if PEY delivers sizeable uplifts to previous carrying values upon exits, as it has done historically. In this context, we note that PEY has a good pipeline of mature investments that are potentially ripe for sale. PEY's shares now trade at a 24% discount to NAV versus a 10-year average of 18%.

Revenue and EBITDA growth across PEY's direct portfolio



Source: Princess Private Equity Holding data. Note: Data from a sample of direct equity investments based on available information and published by PEY in the relevant Q4 portfolio updates. For 2023, the sample represents 40 companies making up 88% of NAV.

PE as a gateway to an expanding equities universe

PE has established itself as an important asset class for institutional investors globally, as it provides access to actively managed, attractive companies not accessible through public markets, and which increasingly tend to stay private for longer. A higher cost of debt is likely to dilute returns across global PE portfolios, but the extent of the impact may be limited by PE's focus on operational improvement of its holdings, good cash generation and earnings momentum across the sectors on which PE places emphasis, as well as covenant-lite debt. PEY has consistently delivered double-digit revenue and EBITDA growth across its portfolio since 2015 (except for 2020, see chart above). We believe that this has been aided by the thematic approach to investing, value-creation experience and the 'buy-and-build' strategy of Partners Group (PG), PEY's investment manager.

Attractive dividend and share repurchase policy

PEY offers a solid annual dividend payment of 5% of opening NAV, which it has been able to successfully deliver since 2021 with few exceptions. Furthermore, PEY's board recently introduced a well-structured framework for conducting NAV-accretive buybacks. This is designed to ensure a significant part of PEY's free cash flow will be allocated to share repurchases in the event its shares trade at a wide discount to NAV (see below for details). In this context, we highlight PEY's good balance sheet headroom, with available liquidity and contracted exit proceeds exceeding all of its outstanding investment commitments.

NOT INTENDED FOR PERSONS IN THE EEA

29 April 2024

Price Ord.	**€10.75**
Price (PEYS)	**907p**
Market cap	**€743m**
NAV*	**€979m**
NAV per share*	€14.16
Discount to NAV	24.1%
Yield (LTM)	6.8%
Shares in issue	69.2m
Code (EUR/GBP quote)	PEY/PEYS
Primary exchange	LSE
AIC sector	Private equity

52-week high/low	€10.90	€9.28
NAV high/low	€15.12	€14.16

*As at end-February 2024.

Gearing

Net gearing at end-February 2024	1.9%

Fund objective

Princess Private Equity Holding is an investment holding company domiciled in Guernsey that invests in private equity and has a minor private debt position. Its portfolio consists mostly of direct investments but may also include primary and secondary fund investments. It aims to provide shareholders with long-term capital growth and an attractive dividend yield.

Bull points

- Focus on building resiliency in portfolio companies and on transformative trends; exposure to resilient sectors (eg healthcare) above listed small caps.
- Good earnings momentum delivered across its portfolio.
- Available at a discount to NAV above historical average.

Bear points

- Interest rate normalisation may reduce prospective private equity returns, put pressure on interest coverage ratios and/or lead to refinancing issues across private equity-backed companies in the medium term.
- NAV TR below peer average in recent years.
- A persistently weak exit environment may further affect PEY's new investment activity and liquidity.

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Princess Private Equity Holding is a research client of Edison Investment Research Limited

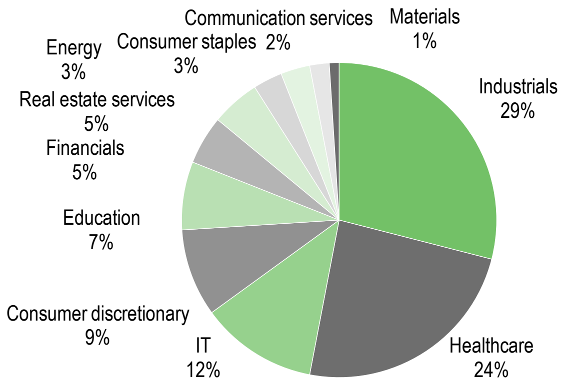
PEY's value proposition

Partners Group: A well-established thematic investor

PEY (or Partners Group Private Equity Limited as per the name change to be proposed at the forthcoming AGM) offers a balanced exposure across private developed markets, with 46% of its end-2023 portfolio value invested in North American businesses and 43% in Europe-domiciled companies (with 7% and 4% in Asia-Pacific and the rest of the world, respectively).

PEY is managed by PG, one of the leading private markets investment managers, with assets under management (AUM) of over US$147bn (of which US$76bn is in PE) across more than 800 institutional investors. PG focuses on identifying attractive transformative trends across 40–60 specific themes in various 'foundational' subsectors of the real economy within four verticals: technology, health & life, goods & products and services. As a result, PEY's portfolio is diversified in terms of sectors (see Exhibit 1), with the largest exposure to a diverse set of industrial businesses (29%), followed by healthcare (24% of NAV, visibly above the MSCI World Small Cap Index at 10% at end-March 2024) and IT (12%, broadly in line with the MSCI World Small Cap Index at 11%).

Exhibit 1: PEY's portfolio by sector at end-2023



Source: Princess Private Equity Holding data

PG leverages its entrepreneurial governance approach in seeking to develop its portfolio companies into market leaders. Its operational improvement capabilities are based on its team of more than 1,900 professionals (including more than 500 investment professionals) across 20 offices worldwide, further supported by a network of over 200 operating directors and industry advisers.

An illustration of PG's experience and thematic investing is its investment in GlobalLogic, a US software development company providing experience design and digital engineering services, in August 2018 (alongside other funds managed by PG, which acted on behalf of its clients). The company was subsequently sold in 2021 at a very strong 5.3x multiple on invested capital (MOIC) and a 76% internal rate of return despite the relatively short holding period. Key investment criteria identified by PG at the time of acquisition included: (1) strong industry tailwinds in the form of corporate investments in digital transformation and IT services; (2) durable financials with high revenue visibility (top- and bottom-line growth of c 20% at a margin of c 20%, key accounts providing 88% visibility of the 2019 budget, a 110%+ net dollar retention rate); and (3) solid organic growth with c 88 accounts added annually coupled with the strengthening of relationships within existing accounts. During the holding period, PG implemented a number of value-creation initiatives at the company (see our June 2021 note and PG's summary for details).

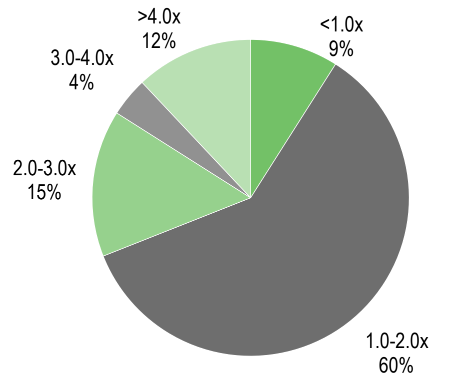
Revenue and EBITDA momentum above public markets average

The favourable sector mix, coupled with PG's value-creation activities and 'buy-and-build' strategy, has allowed PEY's direct investments to consistently deliver double-digit percentage annual revenue and EBITDA growth (combined organic and through M&A) since 2015, except for 2020 amid the COVID-19 pandemic (see above). PG highlights that this is well ahead of the revenue and earnings growth posted by companies included in the MSCI World Index. In 2023, EBITDA growth across PEY's direct portfolio was 13%, compared with the MSCI World and MSCI World Small Cap indices at 4% and -5%, respectively (according to PG calculations). On a sector-adjusted basis (ie after applying PEY's sector split), the 2023 EBITDA growth of listed companies would have been 10%, still 3pp below that of PEY's direct portfolio. PG also notes that this growth was achieved at a higher average EBITDA margin (25% in 2023) than the average in public markets (MSCI World Index at 18%, MSCI World Small Cap Index at 12%).

Maturing portfolio with potential for significant exits

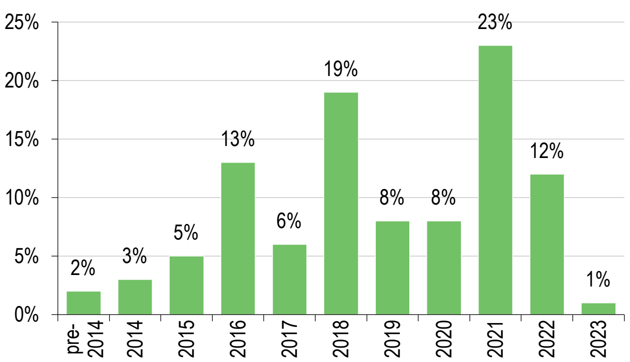
PEY now has a good pipeline of holdings that may be ripe for an exit, arising from the robust operational performance of several portfolio companies, as well as a limited level of realisations in 2022 and 2023 (in line with the low exit activity across global PE markets). This applies in particular to the 31% of PEY's direct investments at end-2023 that are currently held at a total value to paid-in (TVPI) multiple of 2.0x or more (of which 16% is held at 3.0x or more) (see Exhibit 2). Around 60% of its investments are in the value-creation phase and are held at 1.0–2.0x, offering the potential for realisations in the future (only 9% of investments were held below cost). In this context, it is worth noting that around 30% of all PEY's direct exits historically were completed at a MOIC of 2.0–3.0x, and a further 25% and 35% were exited at even healthier MOICs of 3.0–4.0x and more than 4.0x, respectively. The increasing maturity of PEY's portfolio is also illustrated by its vintage profile, with 2019 and earlier vintages making up c 56% of PEY's end-2023 portfolio value (see Exhibit 3).

Exhibit 2: PEY's direct portfolio by gross TVPI*



Source: Princess Private Equity Holding data. Note: *Total value to paid-in capital.

Exhibit 3: PEY's portfolio by investment year



Source: Princess Private Equity Holding data

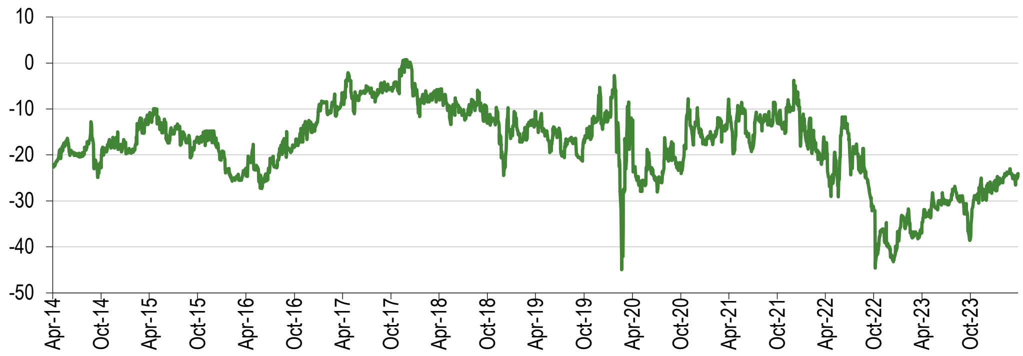
Attractive dividends, well-structured approach to buybacks

PEY has consistently delivered on its policy to pay out an annual dividend of 5% of opening NAV since 2011 with few exceptions, with the FY23 payment of €0.73 per share representing an attractive dividend yield of 6.8% based on the current share price, one of the highest across the listed PE sector (see Exhibit 9). Furthermore, recently PEY's capital allocation policy has been updated to include a well-defined framework for carrying out buybacks. In the event PEY's share price discount to last reported NAV reaches 30% or more, PEY will allocate 75% of the free cash flow it generates (calculated at the beginning of each quarter) to share repurchases. At a discount of 20% or more (but below 30%), it will use 50% of free cash flow. However, even if the discount is narrower than 20%, the board retains the right to embark on share buybacks if it considers it beneficial to PEY. This framework highlights PEY's clear focus on limiting the discount to NAV and performing share repurchases when these are particularly NAV-accretive. We discuss PEY's dividend and buyback policy in more detail below.

PEY's shares currently available at an above-average discount

PEY's share price performed very well in 2023 with a TR of 32.6% (ahead of the FY23 NAV TR, resulting in a narrowing of PEY's discount to NAV) and a further c 4% appreciation in 2024 to date. However, this represents a partial recovery from the 39.9% TR decline in 2022, which was due to a combination of the suspension of one interim dividend and headwinds across the broad PE market. As a result, PEY's shares now trade at a c 24% discount to NAV, wider than its 10-year average of c 18% (see Exhibit 4). In this context, we note that PG manages c €40bn of assets in semi-liquid programmes (invested in the same companies as PEY), where clients can subscribe for and redeem their investments at NAV every month. These programmes saw an average two-year volume of €700m per month (which is not too far away from PEY's entire market capitalisation).

Exhibit 4: PEY's historical discount to NAV



Source: LSEG

This should also be put in the context of the average 50% uplift to fair value one year prior that PEY achieved on its 11 direct holdings (where it invested more than €5m in each), which were fully exited over the five years to end-June 2023. The recent lengthening of holding periods (due to muted PE exits) and higher interest rates could somewhat limit uplifts to previous carrying values for realised investments (as illustrated by PEY's Civica deal – see our previous note for details). Nevertheless, we believe that a continuation of the recent pick-up in global M&A activity (and in turn an increase in PE exits, especially if driven by trade buyers) could prove supportive to PEY's future NAV TR. This is illustrated by its recently agreed sale of SRS Distribution (a US distributor of roofing, landscaping and pool supply products), which made up 5.3% of PEY's end-February 2024 NAV. Its acquisition by The Home Depot, announced on 28 March 2024, implies a valuation of the business of €67m (ie at a significant c 31% uplift to its end-January 2024 carrying value). We calculate that this (together with distributions PEY received from SRS Distribution in 2021 and 2023) translates into a very healthy c 5.7x MOIC on PEY's investment since 2018. The uplift upon exit will add 1.6pp to PEY's total NAV at end-January 2024 and will be reflected in its end-March 2024 NAV.

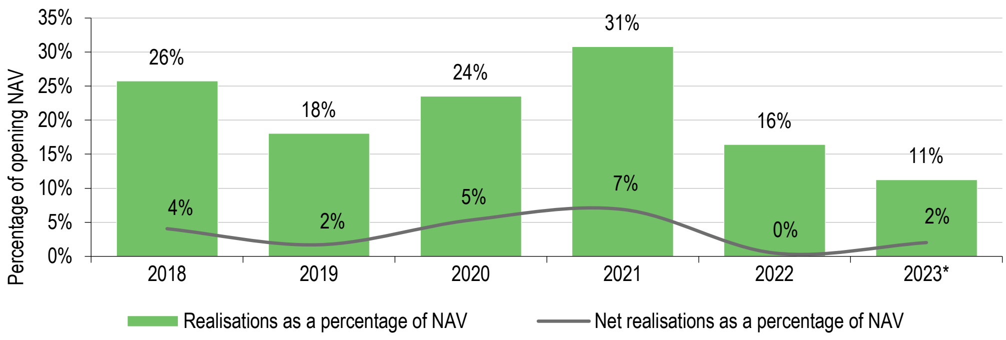
Market outlook: Global M&A activity starting to pick up

PE exits muted in 2023, but M&A markets may help in 2024

Recent activity in global PE markets has been affected by interest rate normalisation and macroeconomic headwinds, with global PE deal volumes falling to c US$1,323bn in 2023, down 25% y-o-y and 40% from the 2021 peak, although close to 2019 levels (based on PitchBook data).

Similarly, global PE exit volumes fell by 27% and 66%, respectively. This has also affected the realisation activity across listed PE companies (see Exhibit 5). However, there have been signs of a revival in M&A activity in recent months, which could bolster PE realisations and returns. Reuters recently indicated (citing Dealogic data) that Q124 global M&A volumes increased by 30% y-o-y to US$755.1m, mostly on the back of a pick-up in mega-cap deals. According to Bain & Company, global M&A activity in 2024 should be assisted by the high volume of assets whose sale was delayed in 2023 due to a weak market environment, including non-core assets of corporates and mature investments of PE funds.

Exhibit 5: Annual realisations as a percentage of opening NAV of listed PE companies



Source: company data, Edison Investment Research. Note: Cumulative realisations of chosen PE-focused trusts (APAX, APEO, CTPE, HGT, HVPE, ICGT, NBPE, OCI, PEY, PIN). *Full-year 2023 realisations except for ICGT (nine months to end-October). CTPE figures based on preliminary results.

PE sector performing a balancing act

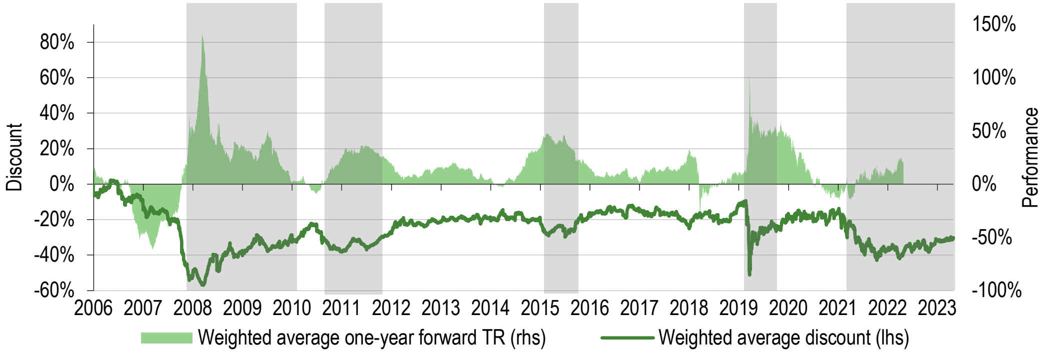
Against the more challenging backdrop, UK-listed PE investment companies recorded more moderate portfolio returns in 2023 compared to previous years. That said, portfolio valuations across the listed PE sector have remained broadly resilient since 2021, as many listed PE players report sustained good earnings growth across major holdings. While average holding periods have lengthened and realisation volumes have fallen below historical averages, many listed PE companies continue to report uplifts to previous carrying values on exit and maintain balanced portfolios in terms of vintage.

A higher cost of debt is likely to dilute returns and increase defaults across global PE portfolios, but the extent of the impact may be limited by PE's active value-creation approach, good cash generation and earnings momentum across the sectors on which PE places emphasis, as well as covenant-lite debt. Future returns on some new investments and bolt-on acquisitions may also be supported by more attractive entry multiples, as the average US and European purchase price multiples for leveraged buyouts stood at 10.8x and 10.1x, respectively, in 2023, down from 11.9x and 10.7x in 2022, respectively (according to Bain & Company, citing Leveraged Commentary & Data).

Discounts to NAV remain above historical averages

Despite the initial signs of an improving market outlook, listed PE companies continue to trade at wider discounts than their historical averages (see Exhibit 6). Moreover, there is a significant discrepancy between current discounts to the NAVs of listed PE companies and the discounts at which limited partner buyout portfolios have recently been priced in the PE secondary markets, which, according to the latest Jefferies' Global Secondary Market Review, stood at just 9% on average in 2023 (vs 13% in 2022 and 3% at the last peak in 2021). See our recent thematic note on listed PE for details.

Exhibit 6: Average discount/premium to the last reported NAVs of listed PE companies (excluding those that completed or are in the process of winding down) over time



Source: LSEG, company data, Edison Investment Research. Note: Weighted by previous year-end NAV. Includes the following companies: HGT, ICGT, PIP, CTPE, PEY (since January 2007), SIHL (July 2007), NBPE (July 2007), OCI (December 2007), HVPE (January 2008), APEO (September 2008) and APAX (June 2015).

Performance has been muted recently

PEY posted a modest 1.8% NAV TR in FY23 in euro terms (after -1.6% in FY22), which is only slightly below the weighted average across the listed PE sector of 4.7% in euro terms in 2023, according to our calculations (PEY's NAV remained flat in the first two months of 2024). Positive portfolio revaluations in local currency terms stood at 5.7%, with three major positive contributors including PCI Pharma Services (a global provider of outsourced supply chain services for the pharmaceutical and biotech companies), Vishal Mega Mart (a franchisor and wholesale supplier for a network of stores in India) and DiversiTech (a manufacturer of components and supplies for the US residential heating, ventilation and air conditioning market).

Emphasis on organic growth rather than leveraged M&A

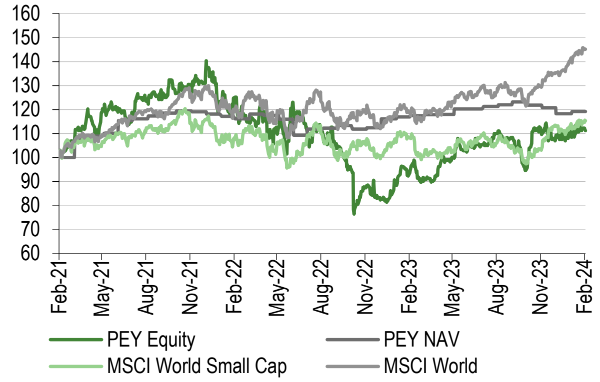
In the current market environment, PG prioritises the acceleration of organic growth and margin enhancement across its portfolio holdings, while deprioritising inorganic growth amid the high interest rates. PG continues to pursue bolt-on acquisitions to existing portfolio holdings as part of its 'buy-and-build' strategy, but will focus on new platform investments where targeted returns can be achieved primarily from organically growing the business. PG's more cautious use of leverage is also illustrated by the decline in average net debt to EBITDA across a sample of PEY's existing portfolio (making up 89% of NAV at end-2023) to 5.0x at end-2023 compared to 6.1x at end-2022 (though the change is likely also due to a different mix of holdings). Similarly, the average equity cushion increased during the year, with a net debt to EV ratio of 34% at end-2023 versus c 40% at end-2022. PG highlighted in Q323 that 97% of debt across its portfolio matures in 2025 or later, with 65% maturing after 2027.

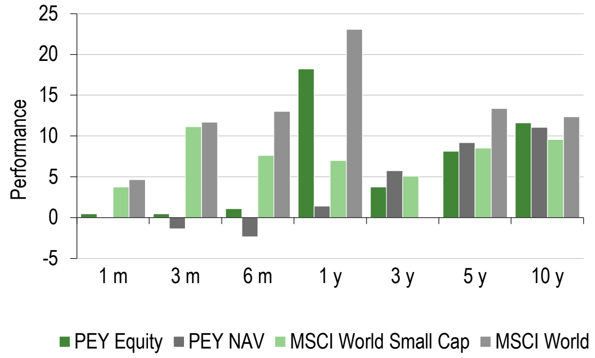
Long-term performance ahead of listed small caps

Over the last five and 10 years, PEY delivered NAV TRs of c 9.2% and 11.0% pa in euro terms, which is ahead of the MSCI World Small Cap Index returns of 8.5% and 9.6% pa, respectively (see Exhibit 7). We consider small-cap companies a better comparator for the PE industry (given the average size of a PE-backed company) than the flagship indices, which are skewed towards large caps. We also note that investors normally demand a higher return from PE as an asset class than from the public market to account for its distinct risk profile. PEY's five- and 10-year performances are behind MSCI World Index returns of 13.4% and 12.4% in euro terms, respectively, which is partly due to the strong rally of the 'Magnificent 7' stocks, fuelled recently by the positive sentiment towards AI.

Exhibit 7: PEY's performance to 29 February 2024 in euro terms

Price, NAV and benchmark TR performance, three years rebased | **Price, NAV and benchmark TR performance (%)**





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

Exhibit 8: Five-year discrete performance data

12 months ending	Share price (%)	NAV (%)	MSCI World Small Cap (%)	MSCI World (%)
29/02/20	14.9	17.2	1.4	9.1
28/02/21	15.1	12.0	27.9	17.6
28/02/22	25.2	16.1	8.5	20.2
28/02/23	(24.5)	1.2	(0.1)	(1.4)
29/02/24	18.2	0.6	7.0	23.1

Source: LSEG. Note: All % on a TR basis in euros.

PEY's returns were below the listed PE peer averages of c 15.5% and 13.7% pa over five and 10 years, respectively (see Exhibit 9). This may be due to several factors, one of which may be PEY's lower exposure to IT, which has performed particularly well since the COVID-19 outbreak, than some peers. Secondly, PEY's FY21 NAV TR of 19.4%, while solid in absolute terms, was below the peer average, partially due to a material cash drag stemming from record-high disposals (only partly mitigated by a temporary allocation to senior loans). Moreover, PEY's hedging policy also had a minor negative impact on its 10-year performance, as the effect of a stronger US dollar against the euro was offset by hedging losses. Finally, its 10-year performance also captures part of the transitional period when PEY moved away from the legacy fund investments to direct investments.

Exhibit 9: Listed PE investment companies peer group at 26 April 2024* in euro terms

% unless stated	Market cap (€m)	NAV TR 1 year	NAV TR 3 years	NAV TR 5 years	NAV TR 10 years	Latest discount	Ongoing Charge	Perform. fee	Net gearing	Dividend yield (%)
Princess Private Equity	**743.4**	**0.6**	**18.2**	**55.1**	**183.5**	**(24.1)**	**1.7**	**Yes**	**106**	**6.8**
HgCapital Trust	2,564.3	13.7	75.8	161.4	417.8	(4.0)	1.7	Yes	100	1.4
GIMV	1,243.5	13.2	33.3	25.0	101.2	(13.1)	3.1	Yes	116	5.8
Oakley Capital Investments	980.1	6.4	81.2	164.5	261.1	(31.2)	2.8	Yes	100	0.9
NB Private Equity Partners	885.2	(0.2)	54.5	91.7	282.9	(29.7)	1.9	Yes	102	4.9
Deutsche Beteiligungs	517.1	9.4	30.0	54.3	169.8**	(22.1)	-***	Yes	114	3.6
HarbourVest Global Private Equity	2,055.0	1.7	73.2	124.7	349.5	(43.6)	1.2	Yes	105	0.0
Pantheon International	1,778.8	6.9	55.7	90.9	250.1	(33.3)	1.3	Yes	107	0.0
abrdn Private Equity Opportunities Trust	1,033.3	4.9	60.0	108.0	270.4	(24.7)	1.1	No	109	2.8
ICG Enterprise Trust	939.7	2.3	71.1	108.3	240.8	(38.2)	1.5	Yes	108	2.7
CT Private Equity Trust	377.3	5.2	67.2	125.2	262.8	(35.8)	1.1	Yes	119	4.6
Peer average	**1,237.4**	**6.4**	**60.2**	**105.4**	**260.6**	**(27.6)**	**1.7********	**-**	**108**	**2.7**
Rank	9	10	11	9	9	4	5	-	7	1

Source: LSEG, Edison Investment Research. Note: *12-month performance based on end-February 2024 or latest available NAV (end-September 2023 for GIMV, end-October 2023 for ICG Enterprise Trust and end-December 2023 for HgCapital Trust, GIMV, Oakley Capital Investments, Deutsche Beteiligungs and CT Private Equity Trust). **Performance since January 2014 as end-December 2023 data is not available. ***Deutsche Beteiligungs is self-managed and its management fee income charged on third-party capital exceeds its ongoing charges. ****Excluding Deutsche Beteiligungs. Net gearing is total assets less cash and equivalents as a percentage of net assets based on last available data. 100 = ungeared.

Direct portfolio diversified by sector

PEY has completed its transition away from PE fund investments (initiated more than 10 years ago) to direct PE investments, which at end-2023 made up 96% of the portfolio and included mainly investments in companies where PG holds a controlling stake (75%), supplemented by minor exposures to real assets (3%) and private debt (1%). It is a diversified portfolio offering exposure to more than 70 PE direct investments, though its top 10 investments make up a meaningful share at 46.2% of NAV at end-February 2024 (see Exhibit 10).

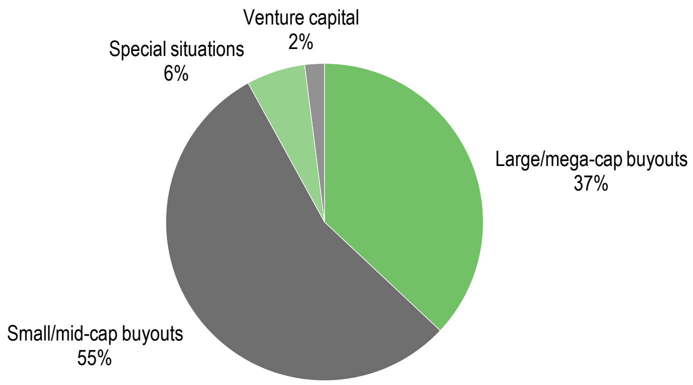
More than half of PEY's portfolio is invested in buyouts classified by PG as small/mid-cap (see Exhibit 11), which we believe have several advantages over large/mega-cap deals in the current environment. Firstly, many of the acquired companies have not been owned by PE before and are low-hanging fruit in terms of value creation. Secondly, portfolio exits are less dependent on the IPO market (with more trade sale and sponsor-to-sponsor opportunities). Finally, small- and mid-market deals are less reliant on funding via syndicated loans (which has been muted over the last year) and also often involve less leverage versus large/mega-cap buyouts.

Exhibit 10: PEY's top 10 holdings at end-February 2024

Company	Region	Sector	Portfolio weight (%)
PCI Pharma Services	North America	Healthcare	8.2
SRS Distribution	North America	Industrials	5.3
Ammega	Western Europe	Industrials	5.2
Emeria	Western Europe	Real estate	5.2
KinderCare Education	North America	Consumer discretionary	4.5
Vishal Mega Mart	Asia-Pacific	Consumer discretionary	4.4
Techem Metering	Western Europe	Industrials	4.0
DiversiTech	North America	Industrials	3.5
Esentia Energy Systems	Rest of World	Energy	3.1
Breitling	Western Europe	Consumer discretionary	2.8
Top 10 companies	-	-	**46.2**

Source: Princess Private Equity Holding data

Exhibit 11: PEY's portfolio by stage at end-2023



Source: Princess Private Equity Holding data

Four of PEY's top 10 holdings (representing c 18% of total NAV at end-February 2024) are industrial companies: **SRS Distribution**, **Ammega** (a provider of belting solutions), **Techem Metering** (a provider of smart metering solutions) and **DiversiTech**.

PEY's largest holding is **PCI Pharma Services** (8.2% of end-February 2024 NAV), which delivered last 12-month revenue and EBITDA growth to end-2023 of 19% and 26%, respectively, on the back of a strong performance across all business segments. Some of PEY's other healthcare investments include: **Galderma** (2.6% of end-2023 NAV), a Swiss specialist in dermatology treatments and skin care products, which recently went public; **Pharmathen** (2.5% of end-2023 NAV), a contract development and manufacturing organisation for complex generic drugs; **Clario**

(2.3% of end-2023 NAV), a contract research organisation; **Stada Arzneimittel** (1.8% of end-2023 NAV), a German pharma company producing generic and over-the-counter drugs; and **Wedgewood Pharmacy** (1.5% of end-2023 NAV), a provider of custom pet-friendly compounded medications for US veterinarians.

PEY also holds several healthcare services providers that offer the potential for secular growth and 'buy-and-build' opportunities. These include: **EyeCare Partners** (1.8% of PEY's end-2023 NAV), the largest vertically integrated, medically focused eye-care services provider in the US; **Blue River PetCare** (1.6%), a group of veterinary practices; **Forefront Dermatology** (1.4%), a dermatology practice chain in the US; and **Confluent Health** (1.2%), one of the largest (by number of clinics) outpatient physical therapy providers in the US.

PEY invested in education businesses (7% of end-2023 NAV), such as the kindergarten to year 12 education business **International Schools Partnership** (2.5% of end-2023 NAV), as well as **Guardian Childcare & Education** (1.5% of end-2023 NAV), an owner of childcare centres. PEY also invested in a provider of early childhood education and care services, **KinderCare Education** (4.5% of end-February 2024 NAV), which is classified under consumer discretionary.

Examples of PEY's tech investments include: **Cloudflight** (which will be added to PEY's portfolio through the investment in the Partners Group Direct Equity V fund), a digital transformation services provider in Europe (mostly in Germany and Austria); **Forterro** (1.8% of end-2023 NAV), a pan-European enterprise resource planning software provider to small- and mid-sized manufacturing businesses; and **Version 1** (1.7% of PEY's end-2023 NAV), a provider of application modernisation, cloud transformation and cloud-native software development services.

Good balance sheet headroom for new investments

PEY's direct PE portfolio represents a combination of investments through PG's private funds and 'single line' investments alongside PG funds. As a result, PEY's portfolio is broadly aligned with the composition of investments across PG's private funds. Amid the difficult PE exit environment, PEY was cautious with respect to new investments, deploying only €12.1m in FY23 (ie 1.2% of end-2022 NAV), which almost exclusively related to follow-on investments (eg in Breitling, Rovensa or International School Partnership), with €1.1m spent on a new investment in Cloudflight. PEY recently committed €50m (of which €20m was committed post balance sheet date) to Partners Group Direct Equity V fund, which targets around 25 direct lead positions in global mid-cap and upper-mid-cap buyouts (80–100% of portfolio) and growth capital investments (0–20%) across industries, geographies, deal sizes and stages. This commitment provides PEY with exposure to a seed portfolio consisting of the supplier of personal protective equipment SureWerx, Cloudflight, Swiss watchmaker Breitling and US specialist insurance broker Foundation Risk Partners.

At the same time, PEY generated €46.7m in realisations, 4.6% of prior year-end NAV, versus c 20–30% normally expected assuming the usual PE holding period of three to five years on average and exit values in line with previous carrying values. PEY received €35.4m in realisation proceeds from direct investments, most notably the exit from Hofmann (a provider of premium ready-to-eat frozen meals and tailored catering services), from which PEY received €9.3m in 2023, with an undisclosed amount of further proceeds expected in 2024. Other direct realisations included c €13.9m from two industrials holdings (Apex International Corporation and SRS Distribution). Finally, PEY received €11.3m from its mature legacy fund portfolio.

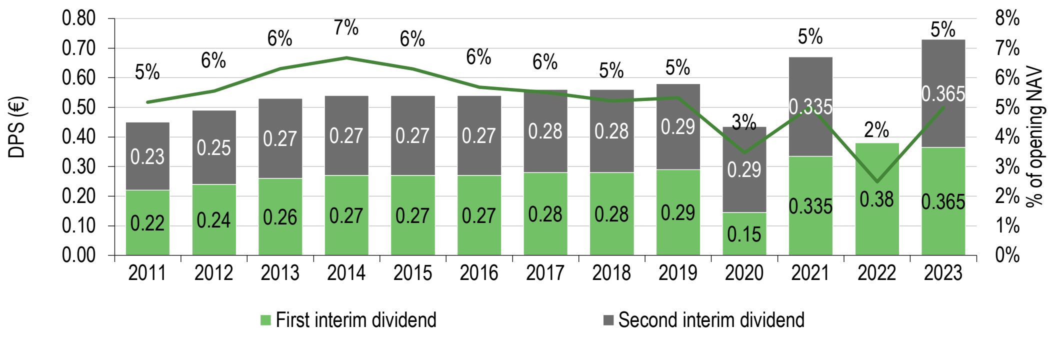
PEY's available liquid resources at end-February 2024 stood at c €121.4m, with €1.9m in cash and equivalents and €119.5m in undrawn credit (out of the €140m total facility size), which will be further bolstered by the exit proceeds from Civica (c €23m, deal closure expected in Q224) and SRS Distribution (€67m, deal closure expected by end-2024). This more than covers its total outstanding commitments to PG private funds/programmes at end-December 2023 of €115.3m (with a further

€20m committed post reporting date, as discussed above), of which PG expects only c €60–70m (c 6–7% of NAV) to be drawn in the next two to four years. Therefore, we believe that PEY has a comfortable liquidity position, assisting its dividend payments, further investments and potential buybacks.

Dividends and buybacks

PEY has adhered to its policy of paying out 5% of opening NAV for more than a decade (with a stable or rising dividend per share, see Exhibit 12), except for the year-on-year decline in 2020 amid the COVID-19 pandemic and in 2022. The suspension of the second interim dividend for 2022 was mainly due to high cash outflows for FX hedges (which PEY subsequently abandoned on 31 March 2023) and subdued M&A markets. PEY resumed regular payments in FY23, with a total dividend per share of €0.73 (5% of end-2022 NAV), which at the current share price represents a healthy 6.8% yield.

Exhibit 12: PEY's historical dividend payments



Source: Princess Private Equity Holding data

As discussed above, PEY announced during the FY23 results call that it has introduced a structured approach to performing share repurchases. The key metric used to determine the scope of buybacks (alongside the prevailing discount to NAV) is free cash flow, and the calculation methodology implies that PEY's gross cash plus contracted distributions and secondary sales will be used to cover (1) a provision for the expected six-month forward ongoing charges, interest expense, dividend payment and full repayment of any drawn debt facilities and (2) a reserve equal to 3% of NAV to cover any capital calls from its existing investment commitments, follow-on funding of existing direct investments, as well as new direct investments at an advanced negotiation stage. Any excess liquidity can be used for share buybacks, subject to the discount to NAV thresholds highlighted above.

In Exhibit 13, we include an illustrative scenario analysis for the buybacks shared by PEY, which we have expanded to include the corresponding percentage of repurchased shares outstanding based on the current share price and share count. We have adjusted the end-December 2023 scenario based on end-February 2024 cash, undrawn credit and NAV, as well as the expected proceeds from the recently announced sale of SRS Distribution (see the 'current' scenario in the exhibit). In the event the free cash flow calculation and the discount to NAV (currently at c 24%) remain broadly unchanged until the start of Q324, PEY should use 50% of the free cash flow (c €9m) for share buybacks (at the current price, the size of the repurchase would represent c 1% of PEY's outstanding shares). The extent of share buybacks will be subject to the limits and terms of the shareholder authority approved at each PEY AGM to repurchase up to 14.99% of PEY's shares.

Exhibit 13: Scenario analysis of share buybacks under the new capital allocation policy

€m, unless otherwise stated	Current*	Scenario 2	Scenario 3
Starting cash	2	50	100
(+) contracted distributions / secondary sales	97	35	50
(-) payment of dividend objective for next 6 months	(25)	(25)	(25)
(-) Fees, expenses and interest for the next 6 months	(15)	(15)	(15)
(-) Repayment of drawn debt	(21)	0	0
(-) Reserve of 3% of NAV**	(29)	(30)	(30)
Total free cash flow (FCF)	**9**	**15**	**80**
FCF for share buybacks (discount of 30% or more)	7	11	60
FCF for share buybacks (discount of 20% or more)	5	8	40
FCF for share buybacks (discount below 20%)	0	0	0
Total portfolio value			
Percentage of outstanding shares bought back (discount of 30% or more)	*0.9%*	*1.5%*	*8.1%*
Percentage of outstanding shares bought back (discount of 20% or more)	*0.6%*	*1.0%*	*5.4%*
Percentage of outstanding shares bought back (discount below 20%)	*0.0%*	*0.0%*	*0.0%*

Source: Princess Private Equity Holding data. Note: *Calculations as at end-December 2023 (as presented by the company), adjusted for SRS Distribution realisation proceeds, as well as end-February 2024 cash and equivalents, drawn credit facility and NAV. **To fund existing undrawn commitments and follow-on investments.

While the reserve for investments of 3% of NAV may seem low at first glance (given that the usual PE investment activity stands at c 10–25% of NAV per year), we note that not all of the free cash flow would be utilised for share buybacks (leaving the remaining funds for further investments) and that, to fund particularly attractive new deals, PEY will be able to tap into its €140m credit facility if required (the repayment of which would subsequently take priority over buybacks). It is worth noting that PEY's credit line is not meant to be used as structural gearing, but rather a facility to bridge the time gap between new investments and realisations.

Fees and charges

PG receives a management fee of 1.5% of PEY's NAV per year (paid quarterly) and is entitled to an incentive fee on direct investments of 15% with an 8% hurdle rate with catch-up (fees are calculated on an investment-by-investment basis). We note that PG does not charge PEY additional fees at the level of private funds, which results in a single-layer fee structure. In FY23, total ongoing charges amounted to c 1.75% (vs c 1.63% in FY22), according to our calculations. The incentive fee amounted to €11.0m (compared to €18.8m in FY22) and the ongoing charge ratio including performance fee was 2.83% (FY22: 3.50%).

Approach to ESG

PG positions itself at the forefront of the sustainability trend in the sector and has been integrating ESG in its PE investing since 2006, when it established its Responsible Investment Policy (now referred to as the ESG and Sustainability Directive). PG has been a signatory of the United Nations Principles for Responsible Investment (UNPRI) since 2008. PG determined a set of goals for assets within PEY's portfolio where it has a controlling stake. Firstly, the aim is to establish an ESG governance framework within the first 100 days from the deal completion date. During the first two years of ownership, portfolio companies develop a meaningful framework to improve ESG performance (called the ESG Journey). This allows PG's team to evaluate the sustainability impact for a given investment until exit. Focus areas include greenhouse gas reduction, the initiation of a stakeholder benefits programme, the development of a tailored employee engagement initiative and the introduction of a diversity and inclusion strategy.

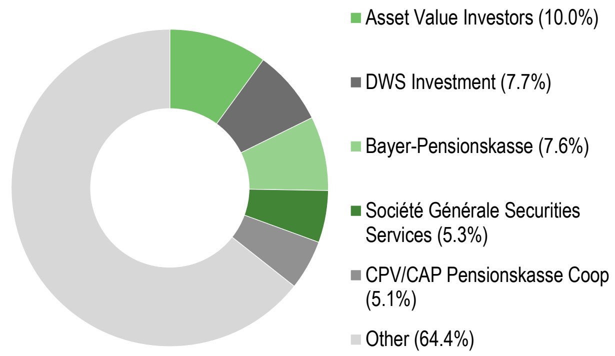
PG has introduced improvements to its sustainability governance framework in 2023, including enhancements to its Sustainability Governance Playbook, improved tracking of transformative value-creation efforts in sustainability by leveraging its bespoke software solution PG Alpha to monitor progress, as well as improved monitoring routines. We also note that PG publicly committed to achieve net zero by 2030 in all of its corporate activities and aims to reach carbon neutrality for its portfolio companies by 2050 or sooner. Finally, a double materiality assessment was performed in 2023 across PG and its portfolio companies to help evaluate the impact of sustainability matters on its business (financial materiality – outside-in perspective), as well as how PG activities affect the society and environment (impact materiality – inside-out perspective). This is aimed at driving the prioritisation of key material topics.

We also note that Peter McKellar (PEY's chairman since November 2023) has recently led the implementation of improvements to PEY's corporate governance: strengthening the board of directors (see below), enhancing shareholder engagement and introducing a well-defined capital allocation policy, as discussed above.

Capital structure

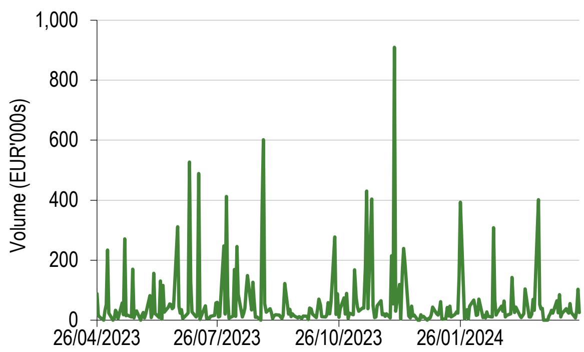
PEY is structured as a limited liability investment holding company domiciled in Guernsey and listed on the Main Market of the London Stock Exchange. It has one class of share, with c 69.2m ordinary shares in issue, although the shares are quoted in both euros (PEY) and sterling (PEYS).

Exhibit 14: Major shareholders



Source: LSEG. Note: At 26 April 2024.

Exhibit 15: Average daily volume



Source: LSEG. Note: 12 months to 26 April 2024.

The board

PEY strengthened its board in recent months by appointing Peter McKellar (on 23 November 2023), Axel Holtrup (15 February 2024) and Gerhard Roggemann (21 March 2024). Henning von der Forst notified the board that he intends not to seek re-election at the next AGM in June 2024 and the nomination committee initiated the recruitment process for a new non-executive director. All current non-executive directors are considered independent.

Peter McKellar (chair) is a non-executive director of 3i Group and Investcorp Capital, deputy chairman of AssetCo, as well as a board member of Scottish Enterprise. He was previously global head of private markets (responsible for £55bn of AUM) at abrdn, the CIO of Standard Life Investments' private equity and infrastructure business, and also lead manager of Standard Life Private Equity Trust (now called abrdn Private Equity Opportunities Trust).

Axel Holtrup is currently an investor in technology start-ups and member of the supervisory board of Deutsche Beteiligungs. Previously he was principal at alternative investments manager Investcorp International (1997–2006), director at global technology investment firm Silver Lake Partners (2006–11), and between 2011 and 2017 he was partner and member of the global management committee at private equity firm AEA Investors.

Gerhard Roggemann is at board member for the Else-Kroener-Fresenius Foundation, deputy chair of the supervisory board for Bremer, as well as an independent business consultant. Previously, he held senior management positions at JP Morgan & Co, Norddeutsche Landesbank and WestLB. Moreover, he was non-executive director of several companies, including Deutsche Boerse, Fresenius SE & Co, Friends Life Group, F&C Asset Management and Resolution Ltd Guernsey. He was also chair and non-executive director of the supervisory board of Deutsche Beteiligungs.

Henning von der Forst joined the board in 2012, while **Merise Wheatley** (chair of the audit and risk committee) and **Fionnuala Carvill** (chair of the management engagement committee) were appointed in September 2018. The directors have professional backgrounds in investment management, insurance, banking and risk management.

Exhibit 16: PEY's board of directors

Board member	Date of appointment	Remuneration in FY23 (£)	Shareholdings at end-FY23
Peter McKellar (chairman)	23 November 2023	10,685	30,000
Fionnuala Carvill	1 September 2018	76,500	-
Henning von der Forst	13 November 2012	55,000	-
Merise Wheatley	1 September 2018	73,000	5,000
Axel Holtrup	15 February 2024	-	-
Gerhard Roggemann	21 March 2024	-	771,867

Source: Princess Private Equity Holding data

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