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Alternative Asset Report
Q3 2019

Highlights

Welcome to the Q3 2019 Alternative Asset Report in which we provide an update on the alternative asset markets covered by Mercer's Alternatives platform ("Mercer"). We will continue to refine this report, with the aim of delivering consistently relevant private markets information to clients.

- **The U.S. Private Equity Market**. Deal flow in the U.S. Private Equity market continued to be strong in Q3. Fund managers deployed over $168 billion in almost 1,600 companies. Of concern is that median valuations in 2019 have reached an all-time high at 12.9x, driven primarily by a significant increase in the equity component. Also of concern is that exits are running well behind the pace of the last several years with only $195 billion being realized thus far in 2019. Despite this, fundraising is brisk with over $86 billion raised in Q3 alone, the strongest quarter of any quarter in over five years.

- **The U.S. Venture Capital Market**. U.S Venture Capital fund managers have also been actively investing and are on pace to match last year's high deployment rate. In Q3, over $28 billion was invested in almost 2,200 companies. In contrast to U.S. PE, U.S. VC's have been very successful in generating exits and have already far exceeded the annual level for 2018, generating over $227 billion thus far although the third quarter was the slowest of 2019. These exits have attracted investors, with fund managers raising $9 billion in over 50 funds in Q3, a solid but not record setting amount.

- **The European Private Equity Market**. Despite the Brexit uncertainty, the European Private Equity market saw some recovery in deal flow in Q3 with over €122 billion invested in the quarter. Despite the increased investment activity, valuation multiples remain low at 8.9x. Exits, however, remain supressed with only €42 billion being realized in Q3, placing 2019 at the slowest exit pace in over five years. Fundraising has also been slow in 2019 for European fund managers, only €10 billion was raised in Q3 bringing the total for 2019 to just over €51 billion.

- **The Asian Private Equity Market**.[1] Asia has experienced a significant decline in investment activity with only $102 billion being deployed through Q3. Exit activity has endured an even greater struggle with realizations of only $41 billion, a 59% decline relative to 2018. However, while fundraising is also down, it has not declined as much. Over $73 billion was raised through Q3 which is only a decrease of 14% versus 2018.

- **The Natural Resources Market**. Fundraising in the Natural Resources market has also been slow with 18 funds raising just over $8 billion, the slowest quarter in over five years. Over the quarter, energy prices did not show much movement. Timber continued its multi-year pattern of generating low but consistent returns. Precious metals, on the other hand, experienced significant increases in prices over the quarter.

- **The Infrastructure Market**. In the Infrastructure market, the number of transactions are comparable to Q3 2018 while the amount of capital deployed is slightly below at $88 billion. In Q3, 19 funds raised over $8 billion, significantly below the amount raised in the corresponding quarter in 2018. However, a greater percentage of funds are reaching their final close within two years of launching.

- **The Private Debt Market**. Fundraising the Private Debt market has also slowed with 24 funds raising $22 billion in Q3. Most of the capital raised was by direct lending funds. Despite the challenging fund raising market, European funds were able to raise $14 billion for 8 funds.

- **The Real Estate Market.** In the U.S. demand for space has been positive but there are signs it is moderating. Canadian investment volumes have slowed in Q3 but remain above average. In the U.K, there has been an inversion of the yields in the industrial and retail markets. Prime real estate yields in

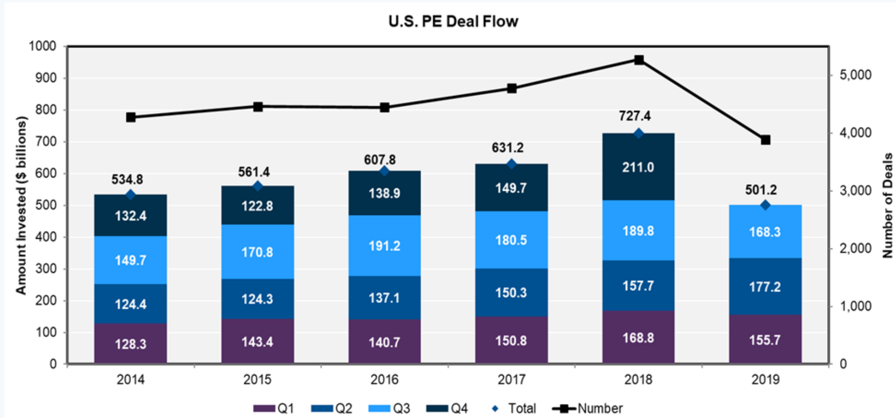
[1] *Statistics on Asian private equity markets are released semi-annually rather than quarterly as in other private markets.*

Europe have fallen to record lows. In the expensive Asian markets, yields have remained flat. Finally, in Australia, there is strong investor demand for commercial real estate.

- **The Hedge Fund Market.** While assets under management are near all-time highs, hedge funds experienced modest outflows in Q3. In Q3, hedge funds underperformed both equities and bonds, however most strategies protected capital in the August market selloff. Of the various strategies, macro had the best performance over the quarter.

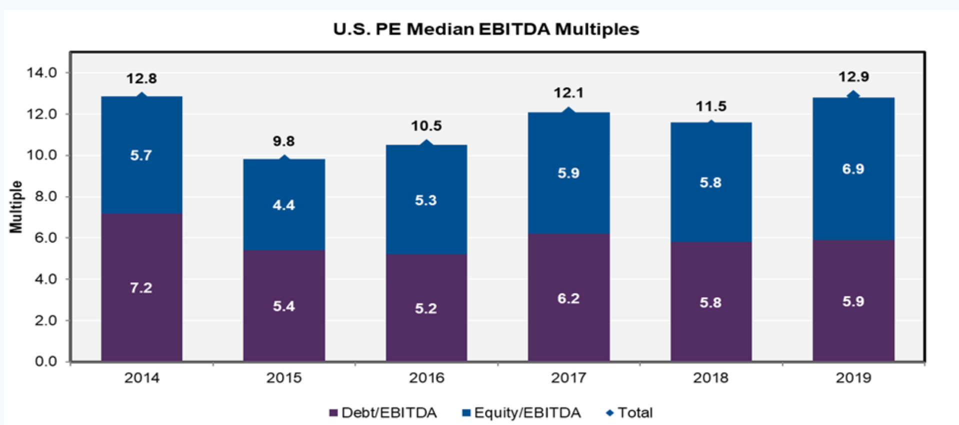
The US Private Equity Market[2]

Deal Flow



Deal making activity across the U.S. private equity market remained strong throughout the third quarter, with GPs investing over $168 billion across nearly 1,600 companies. For the year, total deal flow across the space is poised to eclipse the $600 billion mark for the fourth consecutive year. Investment activity continues to be fueled by the access to cheap debt and the ever-increasing pools of capital raised annually by US private equity firms. Based on recent fundraising figures, managers have access to more than $550 billion in dry powder. An additional contributor of capital into the space has come from sovereign wealth funds and their appetite for co-investments. As the pools of capital get larger, GPs may start focusing on the public markets to fill out their investment portfolios. Through the third quarter, add-ons continue to represent the largest share of activity across the PE landscape, accounting for 54% of all deals since the beginning of 2019.

Multiples



Over the course of 2019, US PE median buyout valuations continued to tick upwards finishing the third quarter at 12.9x EV/EBITDA. This is up significantly from the 11.5x median valuation multiple posted at the end of 2018 and surpasses the high-water mark of 12.8x that was reached at the end of 2014. A number of factors are influencing these

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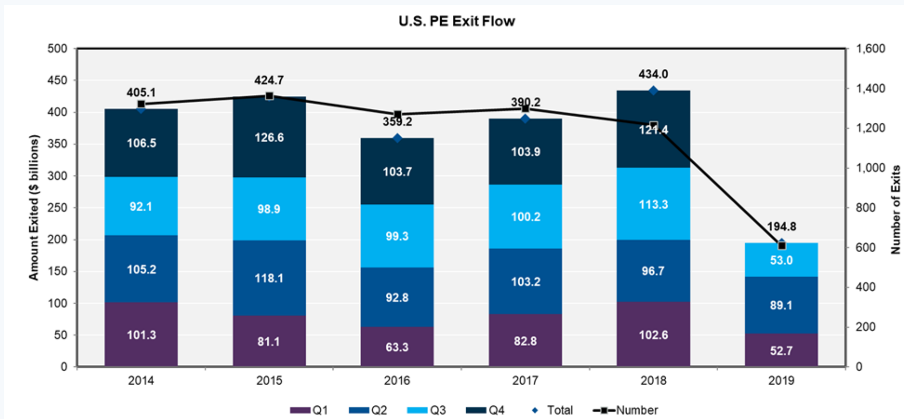
[2] Economic data is from the US Bureau of Economic Analysis and the Federal Reserve Bank of Atlanta. IPO data is sourced from Renaissance Capital - manager of IPO-focused ETFs. Public equity stock indices prices are obtained from Yahoo Finance. Private equity industry data is published quarterly for the US and the following comments are based on recent releases by Buyouts magazine, Private Equity Analyst, Thomson Reuters, Browth Brothers Harriman & Co Business Environment Market Report, Pitchbook and Preqin.

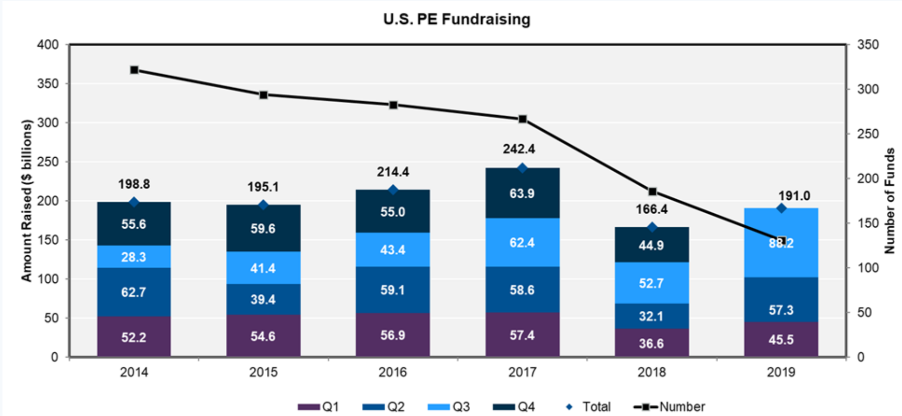
elevated valuations, including double digit gains across the public markets since the beginning of the year and larger pools of available capital leading to increased competition driving values higher. One comforting note about the surge in valuations is that they have largely been driven by the equity component of the multiple. Equity/EBITDA has gone from 5.8x at the end of 2018 to 6.9x as of the end of September. Compared to the previous period of high valuations in 2014, equity/EBITDA only accounted for 44% of the valuation metric. As of the end of September 2019, debt/EBITDA represents 46% of the overall valuation multiple, which is well below the 60% posted in 2013 and lower than the amount of leverage used in deals prior to the Global Financial Crisis.

Exit Flow



The third quarter saw a sharp decline in both the number and dollar amount of exits completed compared to figures posted a year earlier. There were 177 exits totaling $53.0 billion completed in Q3 2019, which was a decline of nearly 55% compared to the dollar amount of activity that was generated in Q3 2018. Additionally, the $195 billion in exits since the beginning of 2019, represents the lowest level of activity at this point of the year since 2013. A key component of the decline in activity over 2019 has come from the significant decrease in Corporate M&As. Corporate acquisitions are down 50% compared to the dollar amount of deals completed over the same period in 2018. A number of factors have contributed to the decline in M&A activity: uncertainty around trade and regulation, recent poor performance of IPOs, a reluctance by firms to acquire assets at elevated prices, and possibly deal fatigue from the record level of activity completed in previous years. However, we do not believe exit activity will remain muted as firms are holding large amounts of capital that will need to be put to work in the short-term.

Fundraising



For the year, commitments across the U.S. private equity market were just under $200 billion and will break through that mark for the third time in four years. For the quarter, US private equity funds closed on over $88 billion across 62 funds. Most of this fundraising activity was largely driven by the closings of a few mega funds: Blackstone Capital Partners VIII - $26 billion, Vista Equity Partners VII - $16 billion, and Providence Equity Partners VIII - $6.0 billion, which drove the average fund size up nearly 55% compared to the end of 2018. The total number of funds coming to market continues to decline as commitments are increasingly being concentrated in these mega funds. In addition to larger fund sizes, the average time between fundraises for buyout funds fell below 4 years in 2019 and currently sits at 3.6 years at the end of September. This is shorter than the turnaround mark of 3.8 years that was posted prior to the Global Financial Crisis in 2007.

Economy

According to the Bureau of Economic Analysis, Real GDP increased 2.1% over the third quarter. This was down from the 3.5% posted twelve months earlier and was slightly below its five-year average of 2.4%. Expectations are for a continued decline in growth over the next two years as the effects of a slowdown across the global economy work their way through markets. In response to these concerns, the Fed cut interest rates by 0.25% in August, September, and October.

Each of the major public equity indices saw minimal movement over Q3 with the S&P 500 and DJIA each posting a 1.2% increase, while the NASDAQ registered a slight decrease of 0.1%. However, for the year the NASDAQ has outpaced its two counterparts by posting a year-to-date return of 20.6%. All three of the indexes have seen strong returns subsequent to the end of the third quarter, likely boosted by the expectation of a new trade deal with China and the easing of interest rates by central banks around the globe in response to stagnating growth.

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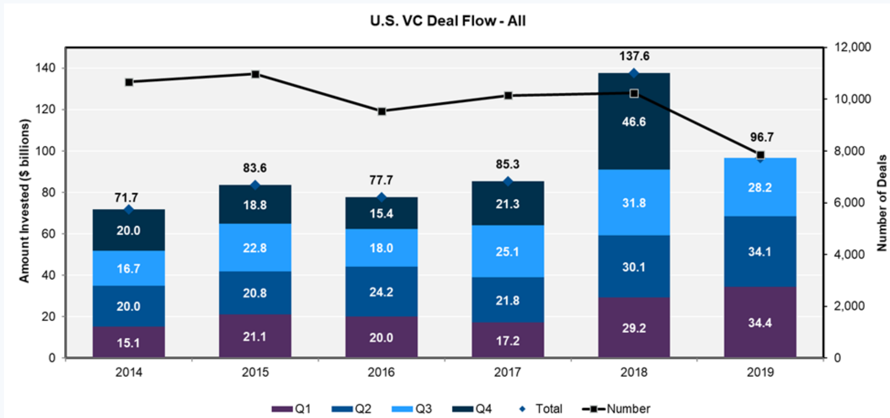
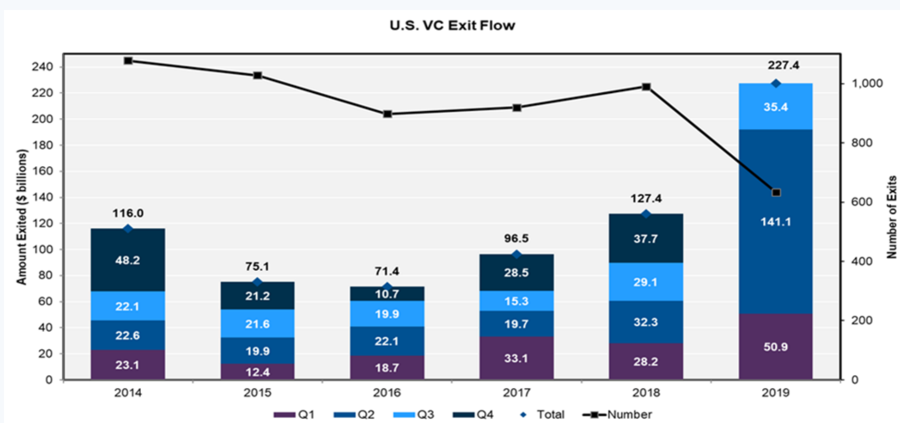
The US Venture Capital Market[3]

Deal Flow



During the third quarter of 2019, the U.S. venture capital market saw $28.2 billion invested across 2,265 deals. For the year, deal making activity is on pace to reach or break the record deal volume that was posted a year earlier. Consistent with its private equity brethren, investment activity across the venture capital space has benefitted from a flood of capital into the space over the last five years, leading to over $195 billion in dry powder available to GPs. As expected, late stage investments continue to account for the largest share of overall dollars invested, with nearly $60 billion (25% of deal count) invested across the segment since the beginning of 2019. Over the last five years, pre-money valuations have remained high, steadily increasing across each stage of the venture capital lifecycle.

Exit Flow

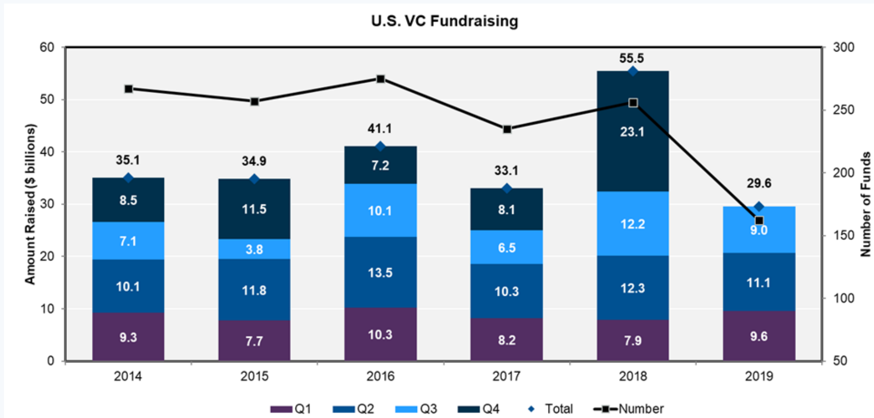


With over $140 billion in exit activity posted during the second quarter, a drastic drop in deal flow was not unexpected during the third quarter. For the three months ending September 30, only 189 exits were completed across the U.S. venture capital market, representing $35.4 billion. However, the deal figures posted over Q3 2019 are illustrative of the level of activity that has occurred in prior quarters, with Q2 2019 representing an outlier due to a number of high profile IPOs. For the year, exits are largely split between acquisitions (437), buyouts (129), and IPOs (67). After a brief lull

[3] *Economic data is from the US Bureau of Economic Analysis and the Federal Reserve Bank of Atlanta. IPO data is sourced from Renaissance Capital - manager of IPO-focused ETFs. Public equity stock indices prices are obtained from Yahoo Finance. Private equity industry data is published quarterly for the US and the following comments are based on recent releases by Buyouts magazine, Private Equity Analyst, Thomson Reuters, Pitchbook and Preqin.*

in the IPO market in 2016 (43) and 2017 (60), IPOs have bounced back significantly since the beginning of 2018 producing 155 new offerings. While we believe the IPO market should remain strong throughout the rest of 2019 and into 2020, concerns surrounding the postponed WeWork offering have caused some companies to place their pending IPOs on hold.

Fundraising



Fundraising totals across the U.S. venture capital market remained relatively steady over the third quarter, with over 50 funds raising $9.0 billion of capital. For the year, over 160 funds venture capital firms have closed, raising nearly $30 billion in capital. While we do not anticipate Q4 2019 to generate as much activity as it did in 2018, there are a number of funds expected to close that should push fundraising totals for 2019 over the $40 billion mark. A key driver behind these fundraising totals has come from the increased exit activity across the space, spurring investors to recycle distributions back into future venture commitments.

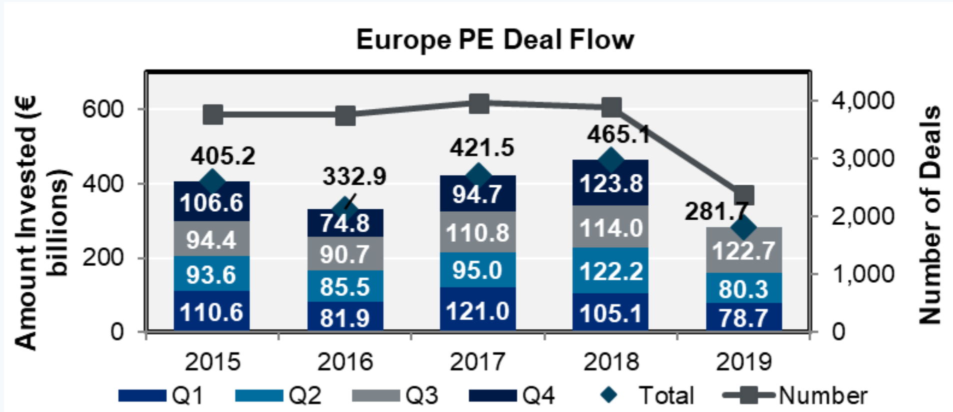
Summary

U.S. public indices remained relatively flat for the quarter as investors cautiously navigated the public equity domain due to trade concerns and a possible slowdown in growth across the global economy. Across the private markets universe, investors continued to pour capital into the space pushing dry powder totals to nearly $750 billion for U.S. PE and VC managers. This influx of capital has driven investment activity and valuations upward, reaching record levels posted a few years earlier. However, there have been a few signs that the private equity and venture capital markets might be leveling off as they digest this additional capital. Within the U.S. venture capital market, the average fund size has decreased from $207 million at the end of 2018 to $182 million at the end of September. While we do not anticipate a drastic drop in investment across the private markets universe, investment activity has dipped across the private equity sector and is on pace to be lower than recent highs posted in 2018. However, we believe this is a small blip across the space, given the level of fundraising activity that has occurred within the strategy, which in turn should drive investment activity and future valuations.

The European Private Equity Market[4]

[4] Private equity industry data is published quarterly for Europe and the following comments are based on Pitchbook as of Q2 19. Pitchbook have updated their methodology and have applied this retrospectively. As such, there may be some discrepancies between figures reported in the Q2 19 market report and previous iterations.

Deal Flow

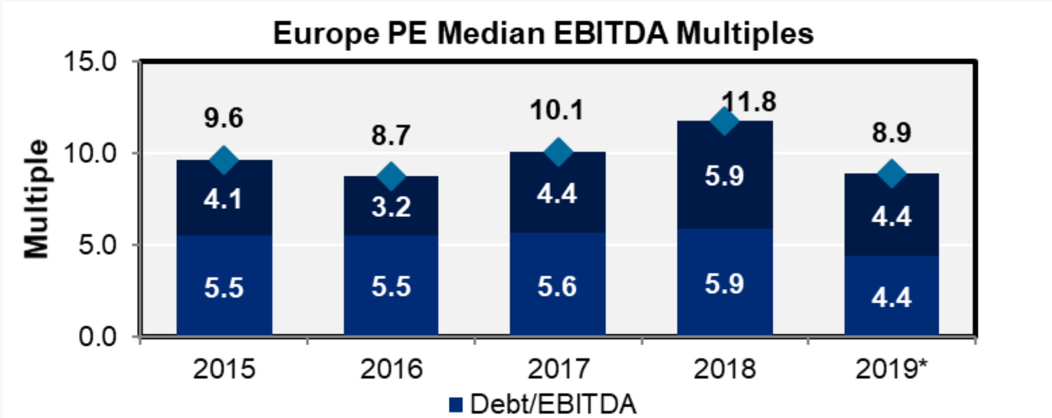


In Q3, European Private Equity deal flow increased substantially – up from €80.3 billion in Q2 to €122.7 billion in Q3. This substantial increase in deal value was partially driven by three transactions over €2.5 billion completed during Q3 2019, and also by the rising median deal size. As was the case in Q2, the median deal size of European investments remained high in Q3 and reached €28.7 million year-to-date which means that the median deal size is expected to reach its highest level in over decade. Additionally, trends such as low cost financing and the increasing prevalence of competitive processes also strengthened deal value over the quarter. Notably however, deal value for 2019, on an aggregate basis, remains low compared to the last two years.

In Q3 2019 the total number of deals completed was 859, which represents a marginal increase from the number of deals recorded in Q2 (710) and Q1 (811). However, similar to deal value, the deal flow recorded in the first three months of 2019 was significantly lower than that of prior years. Indeed, deal volume in Europe has been on a downward trend since 2013. Expectations are that once Q4 results are finalised the total number of European PE deals for 2019 will fall well below that of earlier years and possibly be the weakest year since 2009. As noted in earlier reports, the continued uncertainty around the U.K.'s BREXIT deal continues to weigh heavily on deal volume in the European market.

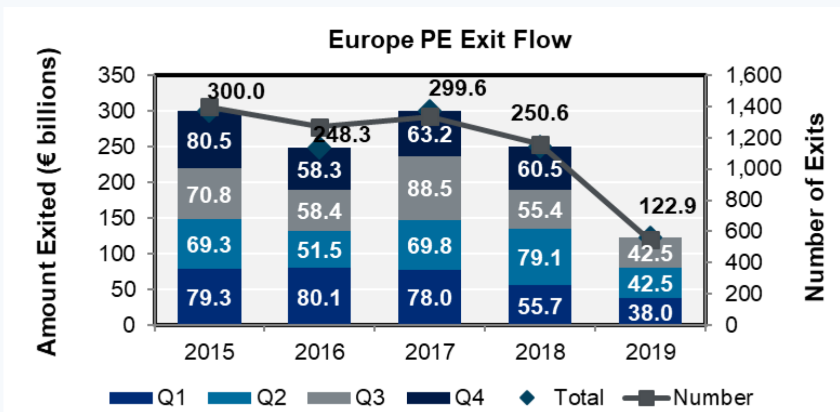
Despite BREXIT, the U.K. (including Ireland) continues to be the largest driver of European deal flow across buyout and growth equity transactions. Specifically, the U.K. and Ireland accounted for 31% of all buyout deals completed in Q3 2019 and 40% of all growth deals. In the buyout market, the U.K. and Ireland were followed by the DACH region as the second largest contributor to deal flow, and in the growth market France was the second largest contributor. Notably however, despite being second, both the DACH and French markets lagged significantly behind the U.K. and Ireland.

Multiples	



Whilst prices remain high, European median EBITDA multiples at 8.9x are well below the record high of 11.8x in 2018. Through September 2019, debt made up 50% of the valuation multiple which was unchanged from that of 2018 and significantly below that of 2016. Not shown in the graph, European valuation multiples remain significantly lower than those in the U.S.

Exit Flow

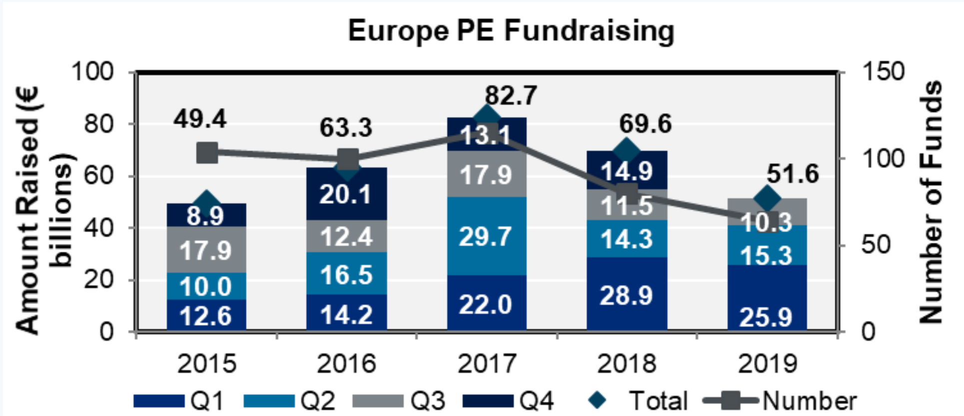


Exit value in Q3 was identical to that of Q2 2019 at €42.5 billion. However, there is still a very clear downward trajectory that has occurred since the peak in 2017. Over Q3 2019, 162 exits were recorded which represented a year-on-year decrease of 38% which translated into a 35% decrease in value. By region, Pitchbook notes that at the current pace, 2019 could be the second consecutive year that France and Benelux companies exceed U.K. and Ireland companies in terms of exit value.

The overall decline in exit activity by volume and value over the quarter can in part be explained by the challenging economic environment in Europe. However, it is also important to recognise that, as we noted several years ago, GPs readily took advantage of the selling environment in 2015-2017 and sold those companies that were could be sold, so this is somewhat a part of the natural cycle.

When looking at exit flow by type, there was a considerable decline in corporate acquisitions (51%) and secondary buyouts (63%) over the quarter, albeit from a high base. IPOs also declined, however by a much smaller margin (6%). Nonetheless, corporate acquisitions and secondary buyouts still account for the lion's share of exit activity, representing 47% and 42% of total Q3 2019 exit activity, respectively.

Fundraising



European fundraising also decreased in Q3 2019, with only €10.3 billion of institutional capital raised across 13 funds. This is the lowest level of fundraising activity recorded since Q2 2015, when €10.0 billion of capital was raised. Notable fund closings over the quarter included CVC Strategic Opportunities Fund II (€4.6 billion) and Oakley Capital Private IV (€1.5 billion). Current expectations are that full year 2019 is set to be the lowest year for fundraising in the last three years. Going into 2020 there are a number of large funds due to return to market which should provide some upward pressure on the fundraising figures.

Economy

The European economy expanded by 0.2% in Q3 2019, the same as the prior quarter. Germany fared better in Q3 as compared to Q2, growing at 0.5%. Meanwhile, France, Spain and Italy recorded the same rate of growth in Q3 as in Q2, expanding by 0.3%, 0.4% and 0.1%, respectively. In the Nordic region, Denmark and Finland recorded slower growth in Q3 versus the prior quarter, growing at 0.4% and 0.7%, respectively, whilst Norway recorded 0% growth. Conversely, Sweden grew at 0.3% in Q3 compared to 0.2% in Q2.

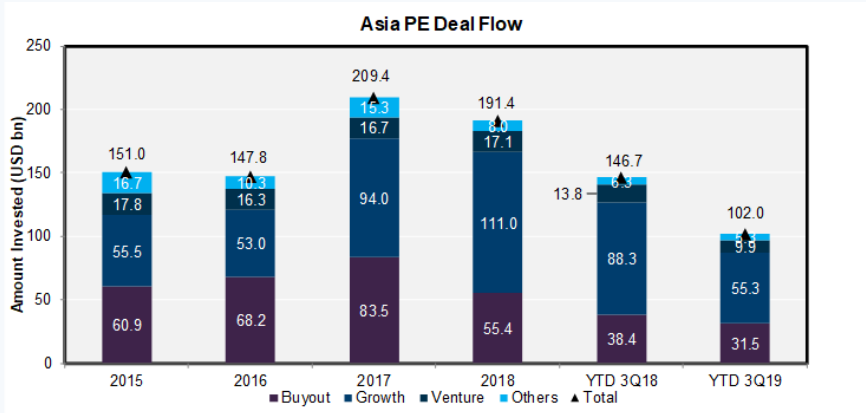
The U.K. economy expanded 0.4% in Q3 2019, a healthy rebound from the 0.2% contraction in the prior quarter. This growth was driven largely by net trade, which is unsurprising given the weak sterling. In addition, this growth was underpinned by household consumption, whilst government expenditure detracted from growth.

Summary

Trends that began at the beginning of 2019, or in some cases several years before, have continued into Q3. Whilst deal volume in Europe continues to remain weak, activity has picked up in Q3. Despite the continued uncertainty surrounding Brexit, the U.K. and Ireland continue to remain dominant in both the buyout and growth equity markets by a considerable margin – a trend that has remained consistent over time. Whilst exit value in Q3 was identical to that of Q2, there is a very clear downward trajectory which has continued for several years now. In Europe, prices remain high but have declined from their peak in 2018 and are still significantly below U.S. multiples. European fundraising also decreased in Q3 with only €10.3 billion of institutional capital raised, which represents the lowest level of activity recorded since Q2 2015.

The Asian Private Equity Market[5]

Deal Flow

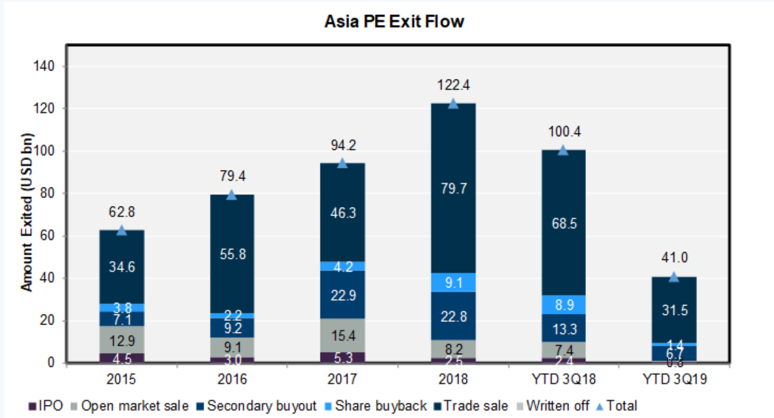


Investment activity in Asia has experienced a contraction, recording a 30% year-on-year decrease to $102.0 billion through Q3 2019. The downward trend is largely attributed to the tensions and market uncertainties arising from the US/China and Japan-Korea trade disputes. Growth deals continue to form the majority of transactions, representing 54% of total investment amount, followed by buyout deals which formed 31%. Compared to the same period last year, buyout deals have moderated slightly by 18%, while growth and venture deals have decreased significantly by 37% and 28% respectively. In terms of countries, China continues to account for the largest portion (37%) of total investments; however, it has declined by 55% compared to the same period last year. It is worth noting that Japan and Korea have seen an uptick in investment activity, recording 254% and 53% year-on-year increase respectively in deal amounts.

There were fewer landmark deals with transaction sizes exceeding $1.0 billion (20 through Q3 2019 vs. 27 through Q3 2018), indicating cautious investment appetite within the region. Notable deals include: i) the $3.1 billion investment in Healthscope Ltd. by Brookfield Asset Management; ii) the $2.2 billion investment in Vodafone New Zealand Inc. by Brookfield Asset Management; iii) the $2.2 billion investment in Arnott's Biscuits by KKR; iv) the $1.6 billion investment in Geo Young Corp. by Blackstone; and v) the $1.5 billion investment in Grab by Softbank Investment Advisers.

[5] *Comments are primarily based on data from the Asia Private Equity Review ("APER"), Asia Venture Capital Journal ("AVCJ"), Trading Economics ("TE"), as well as Mercer's proprietary research. Chart data from AVCJ Database; fundraising figures exclude real estate, infrastructure and government affiliated funds. Please note that the data from various sources may differ.*

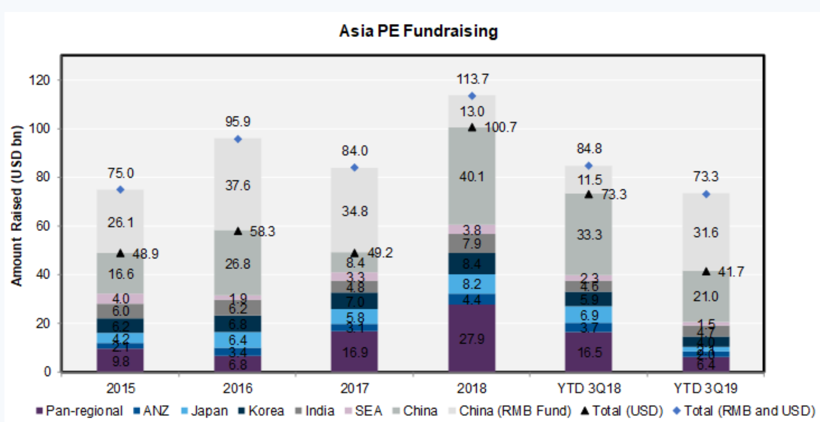
Exit Flow



Divestments across Asia have been sluggish through Q3, reflecting a challenging exit environment. This is also likely due to uncertainty from trade frictions that has negatively impacted the public market. After a record year in 2018, exits through Q3 2019 have generated a total of $41.0 billion, representing a 59% year-on-year decrease. Trade sales, despite recording a 54% year-on-year decrease, continue to dominate as the preferred exit route in the region, representing 77% of total exits. Notably, exits via public market sales have contracted to $1.3 billion, representing an 87% year-on-year decrease. In terms of countries, China has garnered the largest amount of divestment, representing 37% of total exits, but notably it has declined 64% year-on-year. All the other countries have experienced declines in exits, except for Japan, which has increased by 65% year-on-year as a result of several large trade sales.

Divestments via trade sale through Q3 are skewed by: i) the $4.8 billion exit of Marketo KK to Adobe by SunBridge Partners; ii) the $3.5 billion acquisition of PT Bank Danamon by MUFG in Indonesia; and iii) the $2.2 billion exit of Hitachi Kokusai Electric to Applied Material by KKR. Additionally, the IPO market has stagnated in the period, with only two PE-backed IPOs exceeding the $1.0 billion threshold. Notable IPOs include the $4.3 billion IPO of Budweiser Brewing Company and the $1.0 billion IPO of Hansoh Pharmaceutical Group on the Hong Kong Stock Exchange.

Fundraising



Asian fundraising activity through Q3 has declined moderately with $73.3 billion being raised, representing a decrease of 14% year-on-year. The decline is even larger for USD-denominated funds with a decrease of 43% year-on-year. Fundraising activity

	continues to be dominated by the Chinese funds, which accounted for 72% (USD and RMB funds inclusive) of the total amount raised, and 57% of USD fundraising. The closing of RMB-denominated National Integrated Circuit Industry Investment Fund II (the "Big Fund", $29.1 billion) has heavily skewed the total fundraising amount in the period. The Big Fund was designed to promote the Chinese home-grown semiconductor industry and reduce its dependence on foreign technologies amid the China-US trade dispute. Pan-regional funds have recorded a decrease in fundraising of 61% year-on-year in the period, after the record year in 2018. A notable closing of pan-regional funds is TPG Asia VII ($4.6 billion). Most of the Asian countries have recorded significant year-on-year declines for their USD funds: Australia/New Zealand (-45%), Japan (-69%), Korea (-32%), South East Asia (-36%) and China (-37%). India (2%) is the only country to record an increase. Notable Indian fund closings included Edelweiss's latest distressed assets fund (EISAF II Onshore Fund, $1.3 billion), Kotak Special Situations Fund ($1.0 billion) and Brookfield-SBI stressed asset JV Fund ($1.0 billion). In terms of strategy, growth funds remain the most popular fund type, contributing 63% of the amount raised, followed by buyout and venture funds which represented 16% and 15% respectively. The amount raised for growth funds has increased by 17%, as skewed by the Big Fund, while the amount for buyout and venture funds have decreased significantly by 43% and 51%, respectively.
Australia/New Zealand	GDP growth in Australia expanded 1.7% year-on-year in Q3. The slowdown in global economic growth, resulting from the U.S./China trade conflict, has increased uncertainty for businesses, weighing on a potential recovery in investments in Australia. The trade war leaves Australia caught between the U.S., its key strategic ally, and China, its major trading partner. However, there was a slight pick-up in wage growth and signs of the Australian property downturn bottoming out. The Reserve Bank of Australia has cut rates three times between June and October. In view of the external headwinds, the government is forced to transition Australian economy to a more domestic consumption and services-driven economy, led by population growth and the services industry growth. ANZ fundraising activity has decreased from $3.7 billion through Q3 2018 to $2.0 billion through Q3 2019, recording a 45% decrease. A notable fundraise in 2019 was the first closing of Pacific Equity Partners VI ($1.4 billion). Investment activity also slumped 32% from $16.3 billion to $11.1 billion. Investments in 2019 has been dominated by four over-a-billion transactions, including the investment of Healthscope by Brookfield ($3.1 billion), Vodafone New Zealand by Brookfield ($2.2 billion), Arnott's Biscuits by KKR ($2.2 billion) and Navitas by BGH ($1.5 billion). The amount of divestments has decreased sharply from $6.8 billion to $2.1 billion, representing a 69% year-on-year decrease, which is mainly driven by fewer exit activities and smaller transaction sizes in the region.
China	China posted the weakest GDP growth in at least 27.5 years in Q3 at 6.0% year-on-year, softening further from the prior quarter. Q3 marked another milestone in the U.S./China trade dispute, with U.S. imposing tariffs on $550 billion worth of Chinese goods and China setting tariffs on $185 billion worth of U.S. goods. In October, both sides had agreed to terms for a "Phase One" deal but the negotiation dragged on. While both foreign trade and imports contracted further from the prior quarter, exports improved slightly as exporters front-loaded shipments ahead of the tariffs expected to be implemented on December 15. In light of the situation, the Chinese government

	continued to act to stimulate economic activity through measures such as infrastructure spending, improved financial conditions, broad tax cuts and subsidies for consumer goods purchases. China's long-term growth story remains strong, driven by three growth engines, namely domestic consumption, technological advancement and global integration. Expanding at 8.3% year-on-year in Q3, China's retail sales are showing great resilience and continue to support the economy. China is also set to lead the 5G race, with its critical infrastructure built to support technological progress. The investment and divestment activities through Q3 have significantly declined owing to the trade tensions and political uncertainties within the region. The Chinese private equity market registered $38.0 billion of investments, representing a significant decrease of 55% year-on-year. There are six over-a-billion transactions in the period, compared to 15 deals in the same period last year. Most notable investments include the $1.5 billion investment in Chehaoduo (Guazi.com) by Softbank Vision Fund and the $1.4 billion investment in NIO China by E-Town Capital. Exits totalled $15.2 billion, a decrease of 64% year-on-year. While the USD fundraising amount has dropped 37% from $33.3 billion to $21.0 billion, the RMB fundraising amount has skyrocketed for 174% from $11.5 billion to $31.6 billion. The increase in RMB fundraising is skewed by the final closing of the Big Fund ($29.1 billion), as driven by the Chinese government's intention to speed up the development of advanced manufacturing sector in the backdrop of a trade war. Notable USD fundraisings include Warburg Pincus China-SEA II ($4.6 billion), Boyu Capital Fund IV ($3.6 billion) and CITIC Capital Partners IV ($2.8 billion).
India	India's GDP growth dropped further in Q3 to 4.5% year-on-year, primarily attributed to the Non-Banking Financial Companies ("NBFCs") crisis and high interest rates. NBFCs continue to struggle and stopped extending new loans to consumers and businesses. High interest rates have weakened domestic consumption and private investments. The Reserve Bank of India ("RBI") cuts rates for the fifth time this year, reducing the rate by 25bps to 5.15%, the lowest in nine years. On a more positive note, an above-average monsoon and rate cuts should support growth going forward. With increased political stability over the next five years, the government is expected to roll out domestic policies to support rural consumption and increase fiscal spending. Indian fundraising activity has remained intact through Q3, recording $4.7 billion, an increase of 2% year-on-year. The main contributors include Edelweiss's latest distressed assets fund (EISAF II Onshore Fund, $1.3 billion) and Brookfield-SBI stressed asset JV Fund ($1.0 billion). It is of note that special situations funds are gaining popularity and contributing to the increased fundraising. Subsequent to the introduction of Insolvency and Bankruptcy Code in India, the distressed/NPL opportunity set has grown tremendously. The investment pace in India has moderated, with a decrease of 16% from $25.7 billion through Q3 2018 to $21.6 billion through Q3 2019. The divestment activity has slumped in 2019, falling 86% from $28.2 billion to $3.8 billion. This large differential is mainly caused by the landmark $16 billion acquisition of Flipkart by Walmart in May 2018.
Japan	Japan's GDP growth continued at a lower level in Q3, at 1.7% year-on-year. The acceleration in capital spending was not enough to offset impacts from softening global demand which led to weak exports and a slowdown in domestic private consumption. Adding to an already challenging economic outlook, Typhoon Hagibis severely devastated the Kanto region when it made landfall on October 12, 2019. The government drew on $4.6 billion in reserves for natural disasters to cope with the

	catastrophe. Despite the U.S./China trade dispute impacting Japan's financial markets and exports to China, Japan's exports to the U.S. remains strong and the U.S. is set to become Japan's No.1 export partner this year. Japan experienced sluggish fundraising through Q3, with $2.1 billion raised, recording a decrease of 69% year-on-year over the $6.9 billion raised through Q3 2018. Japanese fundraising market may improve in Q4 2019 or early 2020, given that a number of funds (Carlyle Japan IV, $2.0 billion; Polaris Private Equity Fund V, $1.5 billion; CLSA Sunrise Fund IV, $450 million, etc.) are expected to hold their closings in coming months. That being said, there is a significant increase in investment activity of 254% from $2.7 billion to $9.4 billion. This was driven by the aging demographics and the corporate governance reform in Japan, business succession and corporate carve-out deal opportunities became abundant in the period. The average deal size has increased significantly from $7.8 million through Q3 2018 to $26.6 million through Q3 2019. Significant investments in 2019 include the $1.0 billion acquisition of Ayumi Pharmaceutical by Blackstone and the $1.0 billion investment in Yildiz Holding (Godiva's retail, distribution and production operations in APAC) by MBK Partners. Divestment activity has also experienced a similar rise with $9.0 billion recorded through Q3, a 65% year-on-year increase, largely driven by a few large trade sales, including the $4.5 billion exit of Marketo Japan by Sunbridge Partners and the $2.2 billion exit of Hitachi Kokusai Electric by KKR.
South Korea	South Korea's economy grew less than expected in Q3 at 0.4% over the quarter and 2% year-on-year. Softer growth was mainly attributed to a slower increase in the services sector and declines in the utilities and construction sectors. Being a trade-reliant economy, South Korea has been among the worst hit by the cooling global demand caused by the prolonged U.S./China trade dispute. South Korean stocks were also among the hardest hit with KOSPI dropping 15.6% over the one-year period since August 2018. The months-long trade spat with Japan also added strains on South Korean exporters. As a result, the government has responded with an additional $5 billion stimulus plan while the Bank of Korea cut rates twice in three months to 1.25%. President Moon has proposed to increase spending by 9.3% next year, using fiscal stimulus as a tool to boost GDP growth more actively than in the past. The South Korean private equity market experienced a significant decline of 32% in fundraising activity, with only $4.0 billion raised through Q3 in comparison to $5.9 billion raised through Q3 2018. However, it is expected that fundraising would pick up in the following months, including Hahn & Co III ($2.7 billion) and IMM RoseGold IV ($1.8 billion). The exit activity has also come down from $12.5 billion to $6.3 billion, representing a 50% decrease. On a positive note, there was a pickup in deal activity with a 53% increase from $7.7 billion to $11.7 billion. This is attributed to some notable deals including i) the $1.6 billion investment in Geo Young Corp. by Blackstone, ii) the $1.2 billion investment in Lotte Card by MBK Partners and iii) the $1.2 billion investment in Linde Korea by IMM Private Equity.
Southeast Asia	In Q3 there was an overall slowdown in GDP growth across SEA with the exception of the Philippines and Vietnam. Indonesia recorded a GDP growth rate of 5.0% year-on-year, Malaysia 4.4%, Singapore 0.1% and Thailand 2.4%, while the Philippines grew 6.2%, and Vietnam 7.3%. The economic growth of the Philippines was boosted by increased government spending, decelerating inflation and higher consumer spending, while Vietnam's economic growth picked up due to faster industrial activity driven by an increasingly robust manufacturing sector. Vietnam is now the fastest growing economy in SEA, supported by domestic demand, FDI, manufacturing and a

growing tourism sector. Vietnam has been one of the largest beneficiaries of the trade war as some businesses are shifting their supply chain away from China to avoid U.S. tariffs. Central banks in SEA continued to loosen their monetary policy stances in Q3, with central banks in Indonesia, the Philippines and Vietnam cutting interest rates by 25 bps.

Fundraising activity in the SEA region has dropped significantly from $2.3 billion through Q3 2018 to $1.5 billion through Q3 2019, representing a decrease of 36%. The investment activity has remained consistent, with $10.2 billion invested, representing a slight increase of 3% year-on-year. The divestment activity has moderated slightly by 4%, from $4.8 billion to $4.6 billion. The divestments in the region primarily consist of the $3.5 billion investment of PT Bank Danamon by MUFG.

The Natural Resources Market[6]

Fundraising	Natural Resources fundraising throughout 2019 has been slow, and Q3 2019 was no exception. According to Preqin, only 18 funds held a final close this quarter, bringing the year-to-date total to 79 funds closed. The total capital raised by these funds was $8.2 billion, the worst fundraising quarter in over five years. Energy funds continued to account for the vast majority of this activity: 89% of the closed funds and 96% of the capital raised.
Energy	Energy prices were relatively flat in the third quarter. West Texas Intermediate (WTI) crude declined by 3% to $56.49 per barrel at September 30. Brent crude oil prices fell 9.7% during Q3 to $60.99, as the spread between these two benchmark prices narrowed significantly. Henry Hub natural gas spot prices fell only a few pennies to $2.33 per mmbtu after dropping 13% the prior quarter. Working gas in storage in mid-September was higher than last year at this time, but below the five-year average. Although we don't predict commodity prices, natural gas prices are certainly low and may be nearing the bottom of the cycle. Periods of colder-than-normal weather, should they occur this winter, will likely nudge prices higher. In September, U.S. energy firms reduced the number of active oil rigs for a record 10th month in a row as producers followed through on plans to cut spending on new drilling this year. The rig count declined 17% from 12 months prior to the lowest level since May 2017. Still, oil output from the seven major U.S. shale formations is expected to rise to a record high 8.8 million barrels per day in October, according to the U.S. Energy Information Administration. This demonstrates the great strides in drilling and production efficiencies that have occurred over the past few years.
Timber	The NCREIF Timberland Index returned 0.2% in Q3, continuing an eight-year trend of modest, but steady, positive returns for U.S. timber. Pacific Northwest timber markets have struggled, due to trade uncertainties. They appear to have stabilized, however, thanks to strengthening domestic demand. Fewer log exports to China are depressing the Northern hardwood markets. Southern pine markets saw a decline in solid wood demand over the quarter. However, strengthening panel and lumber markets were reported over the third quarter, with prices rebounding slightly from the three-year lows reported in June. U.S. housing starts for August were revised higher to show homebuilding accelerating to a pace of 1.39 million units, the highest level in 12 years. They then fell back in September, as construction in the multi-family housing segment dropped. However, single-family home construction rose for a fourth straight month, suggesting the housing market remains solid. Notable timberland transactions in the third quarter include Weyerhaeuser's agreement to sell its entire footprint in Michigan—555,000 acres—to Lyme Timber for $300 million. Brookfield announced a sale of its stake in Acadian Timber, with holdings in Maine and Canada, to Macer Forest Holdings for $128 million. According to Forest Investment Associates, these are the only two deals to exceed $100 million in 2019.

[6] *The following comments are based on Preqin, The Financial Times and engineering.com.*

Precious Metals	The value of many precious metals rallied in the third quarter. Silver jumped 11%, platinum climbed 6%, and gold rose 4% for the quarter. As of September 30, gold was up 15% for the year and, barring a fourth quarter collapse, headed towards its biggest annual gain since 2010. Many analysts attributed the rise to low or negative interest rates, which reduces the opportunity cost of holding metals. However, manufacturing data around the globe is signaling a slowdown in activity, so gains could be short-lived. Prices will continue to be affected by trade news and moves in the U.S. dollar.

The Infrastructure Market[7]

Deal Flow	Deal activity during Q3 2019 is in line with the previous year (593 vs 592 opportunities) but deal volumes are slightly lower at $88 billion (compared to $93 billion in Q3 2018). Activity is also broadly similar to the intervening quarters in terms of number and volume (noting that Q2 2019 was unusually high at $176 billion). Europe remained the most active region by deal volume during Q3 2019 (213) with North America second (158). Renewable energy was again the key sector with the highest number of opportunities (301), followed by Transport (84) and Conventional Energy (74). Activity in the telecom sector is increasing, with 40 deals completed over Q3 2019, and 104 deals over the year-to-date (already higher than the total number for 2018). There was a small increase in the number of deals taking place in non-standard sectors (16 in total, with 32 year-to-date). It remains to be seen whether activity here will also increase over time, as infrastructure managers broaden their definition of the asset class. Deal activity in the social infrastructure sector remains subdued (13 deals over Q3 2019), a trend that has continued from 2018.
Fundraising	The infrastructure capital raising market slowed over Q3 2019, after a three-year period of relatively stable quarter-on-quarter development. Over the period, 19 funds raised $8.4 billion at final close, significantly down on the record $44 billion raised twelve months earlier, and also materially lower than the prior two quarters (Q1 2019 – $18 billion and Q2 2019 – $27 billion). However, this is likely to be an anomaly rather than reflective of a prolonged slowdown in the market. It should be noted that 83% of the funds reaching final close so far in 2019 have done so within two years of their launch. This is an improvement from the 77% for funds reaching final close in 2018, indicating that investor demand remains strong overall. In addition, two infrastructure funds each targeting $20 billion+ capital raisings are expected to achieve final close in Q4 2019. A number of infrastructure managers have indicated that they will be returning to market over the remainder of the year and into 2020, so the outlook appears more broadly positive.
Digital Infrastructure	This quarter, we highlight the growth in the digital infrastructure sector as a distinct sub-segment of the market. Over the past 12-24 months, we have seen the establishment of stand-alone digital infrastructure funds targeting the sector, as well as increased interest from generalist infrastructure funds in opportunities across telecommunications towers, fiber-optic networks, data-centres and associated assets. The universe of digital infrastructure funds is still relatively small (approximately 5 compared to a broader universe of approximately 250 currently in the market) but now allows investors to specifically allocate to this particular sector (in a similar way to renewable energy, and also social infrastructure). Telecommunications towers have been part of the infrastructure universe for some time now, with the earliest investments made over a decade ago (such as Arqiva in the UK). Similarly, data-centres have featured selectively in (U.S.) real estate portfolios for a similar period. Opportunities in fiber-optic networks are more recent, but there have already been several high-profile transactions involving infrastructure investors (such as the approximately $14 billion take-private of Zayo Group earlier in

[7] *The following comments are based on Preqin and Inframation.*

	2019). Over the past two years, there have been over 200 deals in the sector overall, more than double the amount in the prior two-year period. The drivers of this growth are multi-faceted, but are all based on the ‘digitalisation’ of economies and societies globally. On the demand side, there has been near-exponential growth in data usage both by individuals and corporates over the past decade, due to rise of the smartphone but also cloud computing amongst others. On the supply side, the significant capital requirement for new digital infrastructure build-out or upgrade has resulted in a growing opportunity set for infrastructure investors. Specifically, governmental initiatives in certain countries to improve fiber-optic network connectivity and the corporate rollout of 5G networks are two of the current sub-themes. As always, the risk/return characteristics of assets in any particular sector will vary on a case-by-case basis. However, in general terms, the majority of digital infrastructure opportunities seen in the market to date have typically had an associated ‘growth’ angle. For example, this may be the physical build-out of a fiber-optic or telecommunications tower network (i.e. the asset base), the ramp-up in the contracted nature of the asset by attracting new customers (i.e. the revenue base), or some combination of both. This ‘growth’ angle and the exposure to a newer sector within the infrastructure market can, if implemented correctly, complement an existing allocation to the asset class.
Notable Transactions	Across the infrastructure opportunity set as a whole, notable transactions in North America included Antin’s acquisition of a district energy business from Veolia Environment, BlackRock’s buyout of GE’s North American solar business, and Brookfield and GIC’s acquisition of North American freight railroad owner Genesse & Wyoming. In Europe, key deals completed over Q3 2019 include the investment by Brookfield into Spanish solar group X-Elio, Macquarie’s acquisition of chemical park supplier Currenta and the Bard offshore wind farm (both in Germany), and Brookfield’s investment into a portfolio of five operational Spanish PPP projects. In Asia, major deals included Stonepeak’s first investment outside North America in an offshore wind project in Taiwan, GIC’s investment in a portfolio of operational and under construction toll-roads in India, and the sale of Vodafone New Zealand to Brookfield and Infratil. Overall, the market remains active in terms of acquisitions and realisations.

The Private Debt Market[8]

Fundraising	During the third quarter, 24 funds reached a final close raising a combined $22 billion. This extended a slow fundraising year relative to the last two years, and the third quarter was below the five-year average of approximately $28 billion. Fundraising activity was almost solely driven by direct lending, accounting for $20 billion (90%) of capital raised during the quarter. Mezzanine and special situations each raised $1 billion in capital through six funds and one fund, respectively. After soft fundraising figures in the prior quarter, Europe returned strongly in the third quarter, closing a combined $14 billion (63% of global private debt capital raised) across eight funds. In Asia and other global regions, fundraising remained stable relative to prior quarters. Overall, the global private debt fundraising market remains relatively strong since its apex in 2017 with approximately $80 billion raised through the first three quarters of 2019. As of September 2019, private debt dry powder was approximately $300 billion, with almost two-thirds composed of direct lending ($112 billion) and distressed debt ($76 billion). This compares to private equity with five times the dry powder (approximately $1.5 trillion), suggesting headway for the supply of sponsored debt deals to increase.
Market Trends	As discussed in previous quarterly market reports, investor sentiment is largely focused on late stage characteristics of the credit cycle. In the current environment, bargaining power in the direct lending space has moved in favour of the borrower and this is prominently seen in sponsored deals. For lenders, this has resulted in transactions with less restrictive deal terms and greater financial leverage, often employing creative accounting, and in some cases using proceeds for non-growth oriented objectives (e.g. dividend recapitalizations for the benefit of private equity shareholders). At the same time, a combination of slowing global growth and rising input costs may result in poorer financial performance for businesses going forward. Timing any systemic credit deterioration is difficult, and financial performance will obviously vary by company and by sector. For example, the traditional big-box retail sector remains particularly prone to disruption from online sales and distribution channels. In light of these trends, managers remain increasingly focused on portfolio construction, in particular investing in defensive sectors. Given the continued premium available versus public fixed income markets, sustained fundraising trends in direct lending look set to remain strong. The sustainability of private debt can also be seen through the continued drivers underpinning the asset class from a supply side perspective. Although contrary views on the longevity of the asset class include questioning its resiliency through the next credit downturn and deals are becoming completely commoditized (driving down illiquidity premiums and structural protections). Despite this, private equity sponsors have amassed a large amount of dry powder, which will require complementary debt financing. Also, banks continue to retrench from mid-market lending as regulators continue to scrutinize balance sheets alongside risk-bearing capabilities. This retrenchment extends beyond banks simply reducing and refocusing traditional forms of corporate lending to include seeking solutions in the form or non-performing asset disposals and regulatory capital relief. Associated with larger funds being raised, deal sizes have increased. In some cases, private debt managers are issuing loans to companies that could otherwise receive

[8] *Source of data for the charts is Preqin.*

	(cheaper and more borrower-friendly) debt capital from the broadly syndicated leveraged loan and high yield bond market. Private debt managers are able to win these deals, often at a premium spread and with more lender-friendly terms/structures. They are able to do this through their incumbency with the company, ability to underwrite the whole loan, more flexible terms in-line with the company's growth and other strategic objectives coupled with their speed and certainty of execution. Moreover, Europe in general has seen greater acceptance of non-bank lending and are broadening outside of the core U.K., France and German markets.
Looking Forward	In 2019, global central banks continued to underpin the prevailing low interest rate environment. In the U.S., the Federal Reserve reversed its position and rates were cut from post-financial crisis highs of 2.5% down to 1.75%. Meanwhile in Europe, interest rates remained negative (with a further 10 basis point cut) and the ECB implemented a new wave of quantitative easing due to fears of weakness across the Eurozone. Credit spreads available in public market fixed income compressed from the elevated levels at the end of 2018. The lure of additional returns and investors seeking alternative sources of yield and diversifying assets is supportive of demand in the private debt space going into 2020. However, signs of credit deterioration and the loosening of lending criteria continue to warrant sufficient discipline in the planning stages of a private debt allocation. Absent a systemic downturn event, risk lies at the corporate level, and the ability of managers to assess and price transactions according to their risk remains a key area of focus. At the same time, opportunistic and special situations-focused managers with flexible strategies are expected to capitalise on prevailing idiosyncratic risks. Other opportunistic and special situation private debt strategies, such as non-performing asset disposals and regulatory capital relief, can prove interesting options in portfolio construction. These types of private debt strategies will not necessarily be as correlated with the broader corporate business cycle and typically have desirable competitive dynamics with high barriers to entry due to factors such as complexity, bespoke servicing and/or origination requirements, operational intensity, and existing relationships in niche areas. Where it is accessible, consumer credit is broadly underrepresented in many investor portfolios versus corporate credit risk, and household debt metrics have (generally) been on an improving path contrary to corporate balance sheets. Although, we do note more performance differentiation is also likely to creep into the consumer credit market in recognition that higher quality, lower leverage asset bases will offer greater protection as we move through the later stages of the market cycle. While factors such as complexity can create opportunities, barriers to entry in some markets exist for a reason. However, there are potential risks in terms of valuation, settlement, fund structure variations, and reporting transparency which should be considered. Fund selection remains paramount, and areas of consideration when evaluating a manager going forward continue to include discipline (selection, underwriting and use of fund leverage), market expertise and ability to manage assets during challenging environments.

The Real Estate Market[9]

U.S.	In the U.S., property fundamentals remain healthy and continue to exhibit positive trends. Demand for space remains positive, but has been moderating. According to NCREIF, occupancy levels have remained high over the past year, NOI growth in industrial and office has ramped up while multifamily has started to decelerate. Overall, new supply is more constrained than in prior cycles. With supply at reasonable levels, even slight increases in tenant demand continue to drive high occupancy levels. Year-on-year rental growth for the commercial sector (ex. retail) is forecasted to be between 2% to 4%, depending on property type. Multifamily rent and inventory growth forecasts dropped since the second quarter. Industrial vacancy is at an 18-year low and market fundamental continue to be strong, however, development pipelines are robust across the country which could lead to pockets of oversupply. Closed end real estate dry powder has increased dramatically over the past several years. As of September 2019, debt and value-add dry powder has decreased slightly.
Canada	Canadian investment volumes totalled over $10 billion in the third quarter of 2019. This represented a quarter-over-quarter decrease of 7.3%, but still well above the five-year trailing quarterly average of $9.3 billion. Multifamily cap rates continue to compress over the third quarter of 2019. The fundamentals remain strong for multifamily as the demand outweighs the supply. Office cap rates reversed course during the quarter, increasing 2 bps. Office overall remains stabilized with the suburban Class A category increasing yields during the quarter of 2 bps. CBD office product in the major cities continues to be the lowest cap rate subcategory for the sector. The most active asset class in the third quarter of 2019 was the industrial sector which saw investment volumes total $3.1 billion. Cap rates continued to compress in the sector fueled by strong ecommerce penetration and limited availability. Retail cap rates increased 5 bps during the quarter, however cap rates have remained relatively steady given the growth of ecommerce. Investment activity within the sector has continued to hold and demand for high quality regional malls, anchored strip centers, and urban street front retail assets have remained high across Canada.
U.K.	In the U.K., there has been a steady inversion of traditional sector yield levels, with industrial sector yields now being the highest of all three main sectors, and retail yields being lowest. This is the opposite to the long-run situation and reflects sentiment but also structural change. The key question is whether this is the new normal or a short-term phenomenon. Rental growth has been particularly strong in industrials in the South East although rental growth has softened in 2019 relative to 2018. Office returns have been subdued and the retail sector continues to struggle, both in terms of negative rental growth and investor sentiment. Banks continue to be cautious lenders. Approximately 18-24 months ago banks would offer 60-65% LTV, but now this is falling into the 50-60% bracket. Additionally, banks are lending less to the regions than before, creating opportunities for alternative debt providers. The retail sector is increasingly coming under pressure from online retail. Company Voluntary Arrangements (“CVAs”) due to reduced profit margins are becoming more prevalent, leading to reduced rents in certain cases. Retail assets, shopping centres in particular, are increasingly at risk of significant price corrections which we have started to see occur. The broad story is that the UK market is over-supplied with retail space and that e-commerce, coupled with rising input costs, has led to a significant

[9] *Comments are based on the NCREIF Property Index, REIS and the CBRE.*

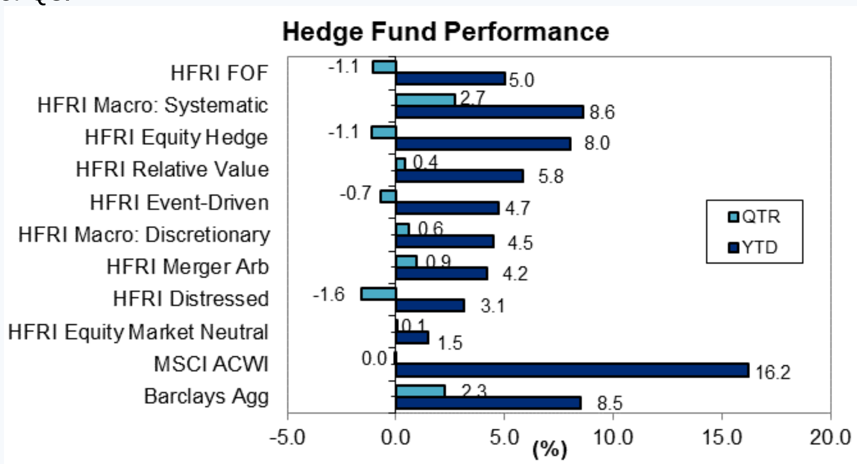
	squeeze on the affordability of physical retail space. Construction since 2016 and over the coming years is above long-term trend levels. This is likely to have a negative impact on areas with particularly high levels, especially London offices. Central London annual take-up has been above long-term trend levels since mid-2018, which should dampen the effect somewhat. There continue to be regions where development has been subdued for the last 10 years.
Europe	On the continent, attractive relative pricing of core, low-risk property versus government bonds has caused prime real estate yields to fall to record-low levels. Approximately 12% of the nearly 100 main European market segments now records NIYs below 3%. While demand for core European real estate remains strong, prime yields are unlikely to fall much further as investors recognize that a floor is being reached. Tight pricing in the prime segment, together with improving economic growth and weak development pipelines has fueled interest in secondary assets. However, continued risk aversion in certain areas (eg. retail) and limitations in debt financing means that the spread between the two segments remains much larger than a decade ago. Search for yield fuels increasing demand for higher risk strategies. High conviction strategies, less likely to correlate with overall GDP growth, are of particular interest. This is also an opportune time for harvesting gains from earlier investments. Low vacancy rates in the office sector and increasing occupier demand for new types of real estate (e.g. last mile logistics, flexible living, data centres) mean that there are both cyclical and structural opportunities to create value. Increasing activity for strategies appear to be turning around secondary assets, with approaches to deal sourcing getting more diversified and forward commitments/funding and manage-to-core approaches getting more relevant.
Asia	Asia Pacific remains expensive relative to other developed markets with its average bond yield gap being one of the lowest for commercial properties. Most markets are expected to see yields remain flat rather than to expand. Debt remains available to core-like assets and accretive to returns in most Asian markets. Positive momentum of the real estate fundamentals slowed with more gateway markets seeing rental growth decelerating or peaking. Office rental grew at a flat rate of 0.2% in the quarter. Overall new supply only marginally affected vacancy with Southeast Asia outperforming the rest of Asia. Retail rental growth remains weak, down -0.1% during the quarter. An additional 51mn sq.ft. of expected completion motivates landlords to negotiate rent. Logistics leasing momentum decelerates due to uncertain US tariff policies toward Asia exporters. Rental growth in China slowed, while cities in Singapore, India and Australia reported no change in rents. Steady investor interest remains in Australia, Japan and Korea driving up capital values.
Australia	In Australia, domestic and foreign investor demand for commercial real estate remains strong and above long-term averages. Scarcity of stock is limiting activity. Although indicative premium yields are surpassing pre-crisis levels in Sydney and Melbourne, values are likely to continue firming through 2020, albeit at a slower rate. Occupier demand remains solid across Office and Industrial; increasing signs of weakness in Retail. In office, occupier demand reflects the two paced economy with Sydney and Melbourne experiencing the strongest growth. Vacancy in both markets is below the long-term averages which supports above inflation rental growth, particularly if incentives continue to tighten from current levels. Other markets are continuing to experience more modest growth. Perth vacancy remains above 20% but is beginning to show signs of recovery. Annual sales growth in retail continues to face headwinds. Both non-discretionary and discretionary are facing challenges from

	low wage growth, decreasing retailer margins, the advances of e-commerce and competition from international retailers. Experiential, dominant and grocery anchored assets appear to be best placed to deal with these headwinds. The transport and logistics sector has been dominating take-up of industrial space due to strong demand of goods and increasing e-commerce footprint. This has been supported by high levels of infrastructure investment.

The Hedge Fund Market[10]

Summary

Hedge fund assets under management remain near all-time highs, but funds overall experienced modest outflows in the quarter. This brought industry AUM to $3.24 trillion at the end of Q3.

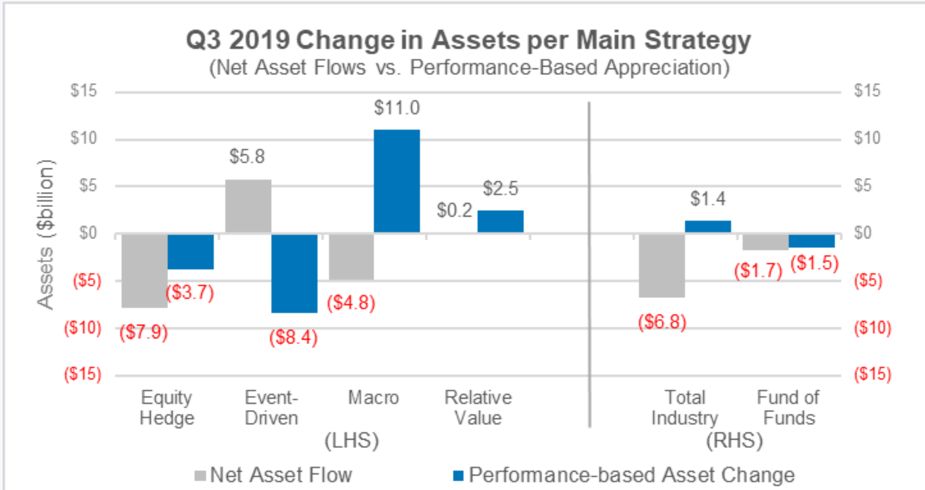


Following a solid start to the year of attractive absolute returns through Q2, hedge funds underperformed both equities and bonds during Q3, as the average portfolio of hedge funds, as represented by the HFRI FOF Index, declined 1.1%. While most strategies protected capital during the August market selloff and several produced solid gains, Q3 overall was challenging for hedge fund performance. Equity hedge managers generally preserved capital through August's volatility, but were hurt by a significant reversal in momentum and ensuing technical unwind. Distressed strategies were stymied by energy weakness, a sell-off in low-quality credit names, and a few idiosyncratic events. Long-biased event-driven strategies suffered from soft-catalyst exposures in addition to distressed positions. Merger arbitrage and relative value strategies continued to post consistent results, and macro strategies posted the strongest gains in an uncorrelated fashion during the quarter.

The market environment continues to face a backdrop of an aging economic exposure with stock prices and valuations near historical highs and government bond term premia near historical lows. Alternative diversifiers to fixed income such as hedge funds continue to remain attractive, and the opportunity set for hedge fund alpha-generation remains robust.

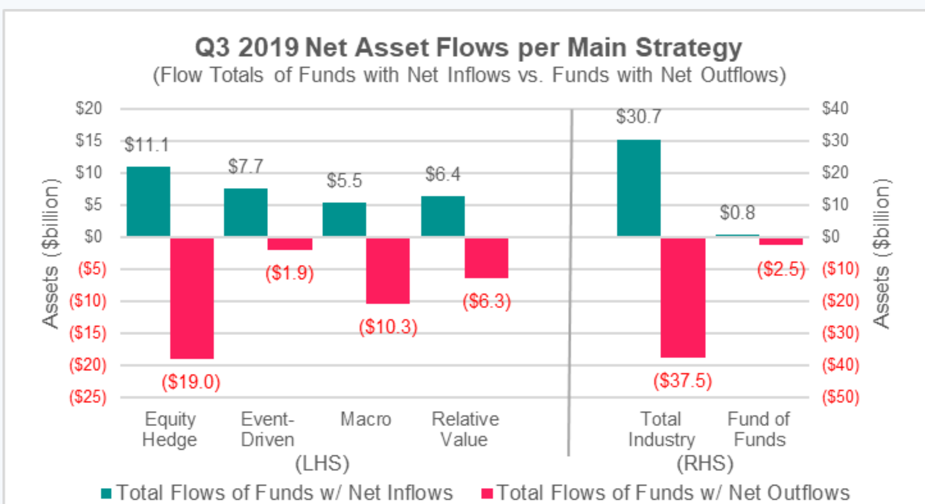
[10] *The following comments are based on data derived from Bloomberg and HFRI as of Q3 2019.*

Fund Flows



Source: Hedge Fund Research

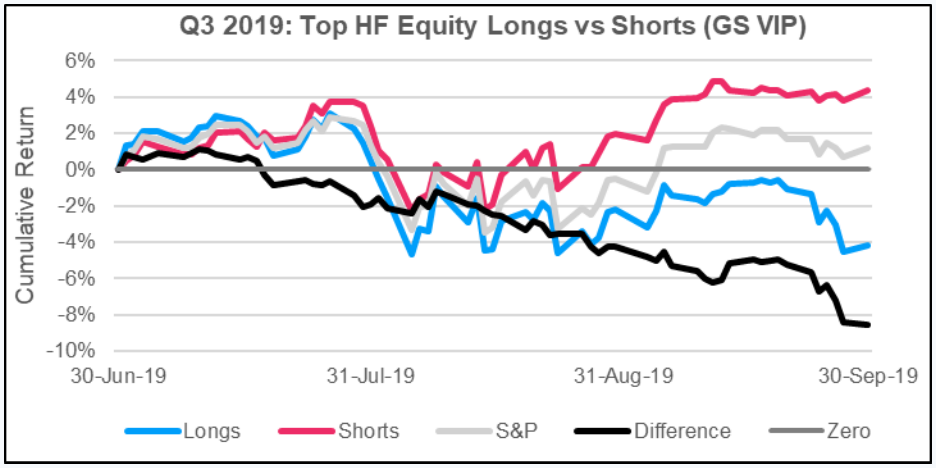
Similar to that of the first two quarters of the year, positive performance (on an asset-weighted basis) slightly offset modest hedge fund industry outflows. Total industry assets fell slightly to $3.24 trillion, still close to all-time highs. Net fund outflows were subdued at -$6.8 billion, or -0.21% of total hedge fund assets. Flows were net negative in two of the four main hedge fund categories. Year-to-date, total outflows have been $29.5 billion net redemptions representing 0.95% of total industry assets at the beginning of the year. Equity hedge strategies fared the worst, followed by macro strategies, while event-driven strategies and relative value strategies experienced inflows (the latter to a small extent). Funds of funds outflows persisted, with $1.7 billion exiting the space. By AUM, smaller funds saw net inflows at the expense of outflows in larger funds, with those having AUM greater than $1 billion in AUM experiencing $8.8 billion in net outflows, while funds with less than $1 billion in AUM experiencing net inflows of $1.8 billion.



Source: Hedge Fund Research

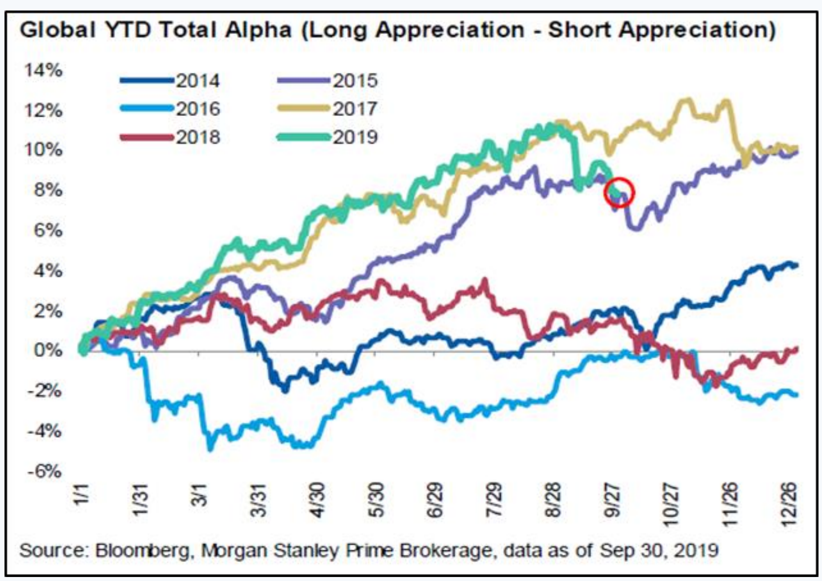
Long/ Short Equity

Equity strategies posted losses during the quarter (HFRI Equity Hedge Index -1.1%) in a reversal of the strong performance of the strategy in the first half of the year. A technical unwind which saw a large decline in momentum names fuelled one of the largest months of long/short equity hedge fund underperformance in recent history, particularly for U.S.-based funds with substantial exposure to crowded names. Other regions were less susceptible to this crowding dynamic but had disparate performance. While stock correlations spiked overall, dispersion among sectors had a disparate impact on managers' portfolios.



Sources: Bloomberg, Goldman Sachs

As indicated by the Goldman Sachs VIP Index, the differential between long and short performance of popularly held equity positions was negative in every month of the quarter. Performance of both long positioning and short positioning were challenging for managers in Q3. That said, popular long positions have outperformed the market year-to-date, and popular short positions have underperformed, helping drive returns for long/short equity managers. Indeed, anecdotally, short attribution year-to-date, Q3 notwithstanding, has been particularly strong.



According to Morgan Stanley, global alpha generation in 2019 faltered in the third quarter following a strong first half and a sluggish 2018. As was highlighted in previous quarters, de-leveraging events that negatively affect equity long/short strategies tend to be followed by strong performance as risk appetite normalizes.

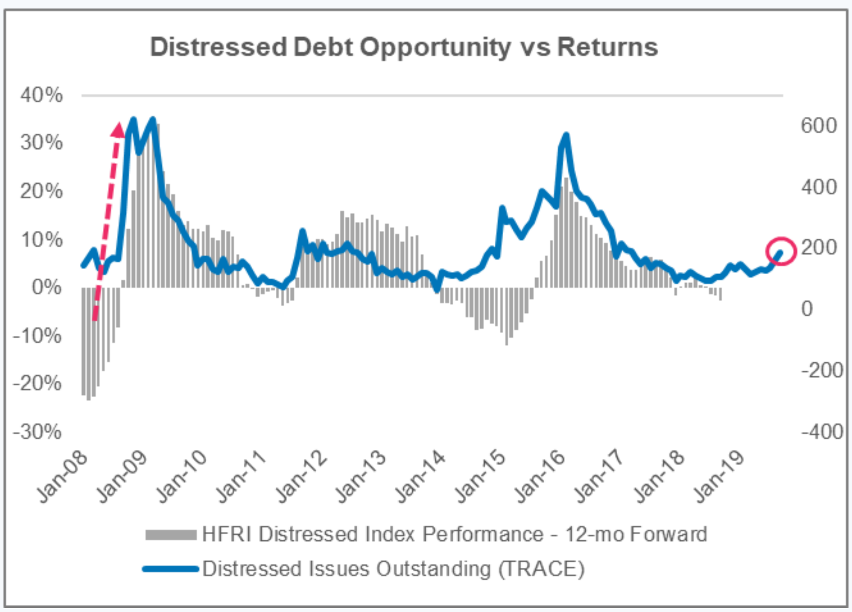
Based on the asset flows as reported by HFR, long/short equity (equity hedge) appears to be in the penalty box since Q1 2016. It is interesting to note that despite the negative sentiment, punctuated by substantial outflows, long/short equity is the best performing of the primary strategies over trailing 3- and 5-years—with two of the last three years representing some of the best years for alpha generation in recent history. While fundamental equity strategies can face periodic headwinds, alpha generation has continued to be robust over time.

Event-Driven

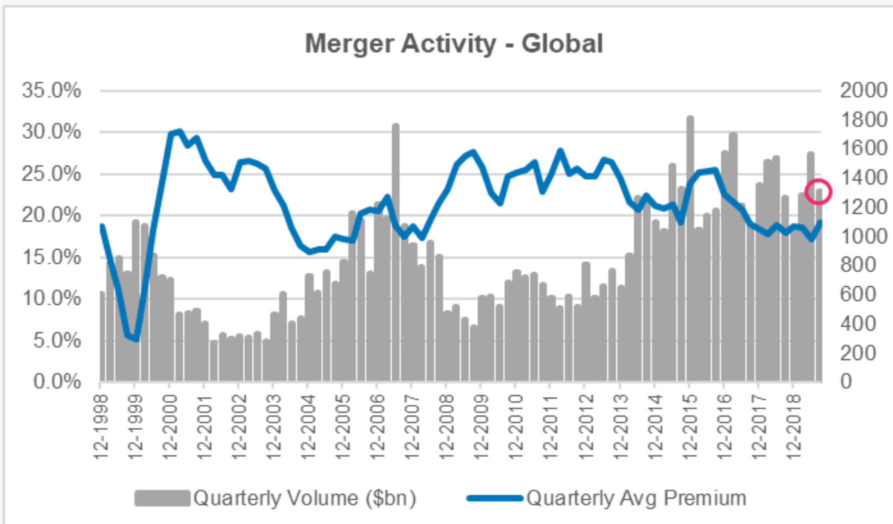
Event-driven strategies were mixed during the quarter (HFRI Event-Driven Index -0.7%). Longer-biased strategies, including special situations equities and activism, were whipsawed by similar dynamics that affected long/short equity managers.

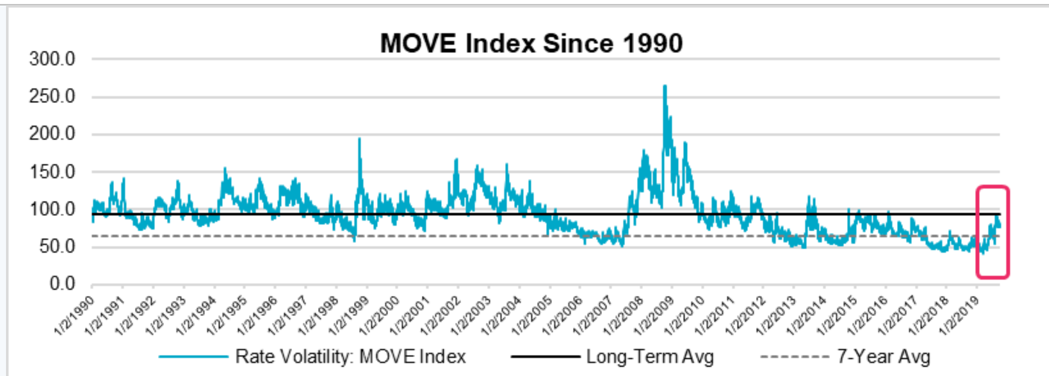
Strategies focused on distressed debt also posted losses during the quarter (HFRI ED: Distressed Index -1.6%), despite the fact that high yield markets gained during the quarter (Bloomberg Barclays HY Index +1.9%). This was partly due to the fact that broad high-yield markets were buoyed by falling interest rates, which had limited impact on distressed debt investors. In addition, distressed strategies were hurt by a collapse in prices of many lower-quality credits, particularly within energy, and due to a few idiosyncratic events during the quarter. An impending jury decision regarding the liability for PG&E caused a selloff in the debt and equity of the widely-held California utility. In addition, losses in Argentine bonds followed President Mauricio Macri's unexpected primary loss to Peronist Alberto Fernandez, sparking concerns that a lack of fiscal restraint will affect Argentina's ability to pay bondholders. Funds with limited exposure to these events were not immune to the broad-based effects on distressed debt pricing, but they tended to fare better.

The number of distressed issues outstanding that currently trade, as measured by TRACE, ticked up modestly in the quarter and remains a bit higher than at any time during 2018, indicating modest opportunities within the space but certainly not broad-based cheapness.

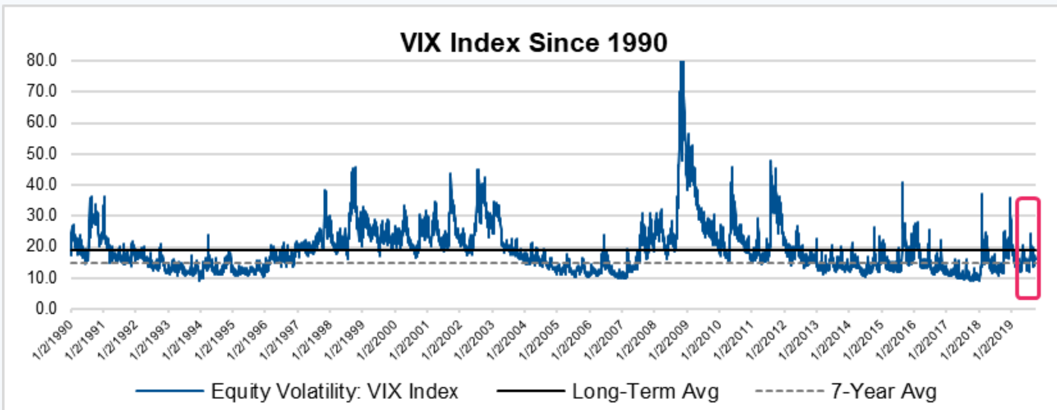


Sources: Bloomberg, HFRI, TRACE

	Distressed credit strategies provide a complexity and illiquidity premium to investors, but investors should recognize their cyclicality. Historically, the supply of outstanding distressed debt is positively correlated to forward-looking returns of distressed hedge funds. Given the low volume of outstanding distressed debt, the opportunity set has waned somewhat recently. The existing supply of distressed debt outstanding has been concentrated in energy and retail, two industries that generally represent lower quality businesses and less attractive distressed opportunities. As a result, nimble distressed debt managers have focused on opportunistic, process-driven, and directly-negotiated lending opportunities. Investors should favour a more opportunistic, multi-strategy approach to the space rather than broad purchasing of a limited supply of stressed/distressed issues. Merger arbitrage strategies gained during the quarter (HFRI ED: Merger Arbitrage Index +0.9%). Continued strong deal volume and size and a shift towards strategic deals drove a healthy opportunity set. Spreads remained attractive, and the closing of the merger deal between Anadarko and Occidental buoyed results.  *Source: Bloomberg*
Macro	Macro strategies on average performed the best during the quarter, as the HFRI Macro: Systematic Index and HFRI Macro: Discretionary Index returned +3.0% and 0.6%, respectively. Returns were strong across all major macro sub-strategies, generally posting gains when equities stumbled in August. While there was dispersion across macro managers, systematic strategies fared the best. Broad CTA indices made money overall (Société Générale CTA Index +3.6%), and were boosted by long bond and equity positioning in trend-following programs. Discretionary managers that were not overly exposed to Argentina posted gains amid global dispersion. Commodity-oriented strategies fared well, protecting capital despite the underperformance of commodities during the quarter.



Source: Bloomberg



Source: Bloomberg

Recent spikes in equity volatility (as measured by the VIX Index) and interest rate volatility (as measured by the MOVE Index) have created opportunities for macro strategies. While they have recently been low relative to history, they moved closer to their long-term averages over the past quarter, indicating a more normal volatility environment for trading. Central bank policies, concerns about global economic headwinds, geopolitical tensions, and trade policies will continue to dictate the opportunity set for macro managers.

Relative Value

Relative value strategies had modestly positive performance during the quarter (HFRI Relative Value Index +0.2%). Returns were mixed across sub-strategies types, as gains in convertible arbitrage, credit relative, and interest-rate relative value strategies were coupled with losses from volatility strategies and other diversified relative value strategies.

A confluence of factors, including idiosyncratic geopolitical events, policy uncertainty, and macroeconomic divergences, were headwinds to performance during the quarter but highlighted an improved environment for trading opportunities among managers. In volatile quarters such as Q3, performance for relative value managers may lag the broader market, but the pricing dislocations across assets has the potential to create a robust opportunity set for future returns.

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