EQT AB – Q3 2019 Results

Tuesday, 5th November 2019

Opening Remarks

Kim Henriksson

CFO, EQT AB

Welcome

Thank you so much and good morning everyone. My name is Kim Henriksson, I am the CFO of EQT AB. I am here with Åsa Riisberg, Head of Shareholder Relations Operations and Pawel Wyszynski, Shareholder Relations Officer. It is my pleasure to present EQT's first quarterly announcement as a public company and we will start with a brief review of the presentation material. After which we will have then an opportunity for Q&A, as mentioned. However, before we dive into the material just a brief recap of our reporting concept.

Reporting Concept

As you know, we have a very long-term business model that our fund investors entrust us with their capital for 10-12 years and a typical holding period for a portfolio company would be 4-5 years. In any one quarter there would typically not be significant changes. The key factors impacting our financial performance and the way we also follow the business internally includes that we manage to find and invest client funds in attractive opportunities and that we create value in the portfolio companies by making them into better and more future-proof companies and that we subsequently exit these investments. Such performance then in turn allows us to raise further funds to invest and of course that we manage to recruit the right talent to continue to grow.

Information on all of the above factors will be included in the quarterly announcement presented today. Twice a year, following the year-end and after H1, we will also include full financials in the reporting. We believe that this strikes the right balance between focusing on the right things and on the long-term, and ensuring sufficient transparency towards the shareholders and other stakeholders. Given that this is our first announcement and that our business model is not so familiar to all capital markets stakeholders, the presentation material also includes some more educational slides. Bear with us, we will also cover the details of the announcement.

Q3 2019 Highlights

Let us start with some highlights from the third quarter. There is of course one event in the quarter which has been very visible to the outside world and that is the listing of EQT AB on NASDAQ OMX. We are very humbled by the support and interest in EQT, both from the most respected institutional shareholders in the world and from around 40,000 retail shareholders. We will be working hard to live up to that trust.

For the third quarter the good investment activity continued, roughly with the same pace as year-to-date. Year-to-date the EQT funds have invested approximately €10 billion. The exit environment continues to be supportive with a total of close to €6 billion for the first nine months. Value creation in our key funds remain on plan and let me revert to that later on in the presentation. In terms of headcount we are continuing to grow according to plan with total number of employees at the end of the quarter reaching 675.

The fee-paying AUM, assets under management, has not changed much in the period. The ongoing fundraising is focused on Ventures II and Real Estate II but we are of course continuously in touch with our clients. Such contacts will usually intensify the closer you get to launching a fundraising. We are now 65-70% invested in EQT VIII so we expect to begin fundraising of EQT IX in 2020.

To give a little bit of background, as mentioned in connection with the listing, this is merely a watering station for us. It is business as usual but now with a balance sheet. What is business as usual then? It is future-proofing companies into strong, long-term and resilient companies across the globe.

The Starting Point for our Company

How do we do that? We recruit and train talent driven by a strong purpose. We have a thematic investment approach. We invest with the trends. By making companies better we both create returns and we make a positive impact to investors, to society and the companies. That is how we work towards our vision of becoming the most reputable investor and owner.

Growth is in our DNA

Growth is in our DNA and has been since our inception 25 years ago. You can see that here with long-term growth in the fee-paying assets under management but also in our talent pool, our employees. Our business really is about people. Our employees and network are EQT's main assets and they are people that find interesting investment opportunities. They have angles on how to develop, grow and transform them. At the end of the day, they create strong companies that benefit society as a whole. This creates returns and gives EQT its licence so operate. You can also on this slide see our geographical footprint. We are continuously expanding it, mostly recently with Milan in Italy and currently we have a new office underway in Paris, France.

Our Business Model is Long-Term, Simple and Scalable

You can easily get lost in the details of private markets investing and the model may seem complex so let me take a minute to go through our business model from a helicopter perspective. Our primary focus is on creating attractive returns for our clients. That is the starting point. If we succeed with that, as we have done in the past, they will entrust us with further funds. Assets under management will grow. From those funds we have two integrated revenue streams. We have the contractually recurring management fees and we have the carried interest which is a function of the performance of the funds. All of that on the top line and on the cost side a vast majority of costs are related to our employees.

Key Data for Q3 2019

Åsa Riisberg

Head of Shareholder Relations, EQT AB

Good Investment Activity and Supportive Exit Environment

Investments

Good morning everyone. We are seeing continued good investment activity in Q3 with a total amount of €3.4 billion invested by [inaudible] in the quarter. To pick a few deals, in Private Capital notable deals include Aldevron, which is a US-based manufacturer and supplier of plasmid DNA, which is a mission critical component in, for instance, gene therapy treatment. Another private capital trust action is Waystar, which is a US revenue cycle management software business that helps hospitals and physician offices to manage claims and collect payment from payers and patients.

In Real Assets a notable deal amongst others was Inexio, which is a fast-growing provider of high-speed internet to retail customers and businesses in rural Germany. These deals are all good examples of EQT's thematic investment approach to investments. EQT focuses on attractive subsectors that we have followed for a long time in key focus industries, such as healthcare and [Inaudible]. We combine this with a local execution of the local EQT deals teams. These are good examples of how we work at EQT with our investment activity.

It should be noted though that when it comes to EQT's investment activities individual quarters can be lumpy from time to time and with that we prefer to look at the investment phase over a longer time period. As you can see here for the first nine months of 2019 and which also Kim pointed out, total investment in EQT funds amounted to €10.1 billion.

Exits

Turning now to the exit side, we note a supportive exit environment. Total exits amounted to €5.6 billion for the EQT funds for the first nine months of 2019. A few examples here as well, for instance in Private Capital we have exited Press Ganey, which is a provider of patient experience and workforce engagement solutions. This was a first exit by Private Capital in the US. We also exited AutoStore, a warehouse automation systems business. In Real Assets some recent exits include for instance, Charleston, which is a German senior care platform, and GB RailFreight, a UK rail freight operator. This is to give you a flavour of the investment and exit activity of the first nine months.

Key Data for Q3 2019

Kim Henriksson

CFO, EQT AB

Key Funds on Plan for Expected Value Creation

As mentioned, the expected value creation for our key funds is on plan and let me take a moment to explain how some of the numbers here on this page hang together. May I please turn your attention to the second column from the right, the gross MOIC as of September this year? This is the valuation of the underlying portfolio companies at that point in time compared to the initially invested capital. Now, turning then to the column furthermost to the right, this refers to our current assessment of the future performance of the underlying asset, i.e. given our expectations on exit timing, valuation and so on. These are on plan with the exception of Infrastructure III, which is above plan. There is no change from the prospectus on this.

What do we mean by on plan? For Private Equity funds the target gross MOIC is around 2.3x and therefore on plan is a range around that, between 2.0x and 2.5x. For the Infrastructure funds the target gross MOIC amounts to around 2.0x and therefore on plan would mean 1.7x to 2.2x gross MOIC. That should give you a good sense for our value creation expectations.

AUM Remains at Similar Levels as per 30th June 2019

Moving over to assets under management, they remain at similar levels as in the beginning of the quarter. Remember that when we talk about AUM it is always about fee-paying AUM. We have no other definition and do not include any other assets here. Year-to-date the fee-paying AUM has increased by some 11%. The gross inflows have mainly been driven by Infrastructure IV earlier in the year. The Q3 development here illustrates well that not much necessarily happens in a single quarter if there has not been a major fundraising. As mentioned, the fundraising here is currently focused on Ventures II and Real Estate II.

What is the Status of our Key Funds?

What is then the status of our key funds and let me go through this in some level of detail, although some of you have seen this before during the roadshow. Normally you would start investing from a successor fund when you are 80-90% invested in the predecessor fund. If there is such a thing as a normal period it would normally take 4-5 years but more recently the actual period has been more in the region of 2-3 years. Currently, Infrastructure IV has made some additional investment since the date of the prospectus and that has taken the investment level to 50-55%. In EQT VIII it continues to be 65-70% invested but given where we are there, we are intensifying the preparations for EQT IX and we expect to formally launch the fundraising then in 2020. At that point we will of course also communicate to the market.

Timing-wise there is still some room to invest from EQT VIII but we do not want to be in a situation where we are fully staffed and fun out of capital to invest. However, it is also important to remember that it is in the nature of our business that we have multiple business segments and active funds that we will always be buyers of assets, sellers of assets and always be in fundraising or pre-marketing mode.

Furthermost to the right here, in terms of size we will also inform the market when we set a target size for the next fund. On the page here we have indicated what the increases have been in our latest fundraising in the flagship funds. The fund we are currently investing out of on the Private Equity side, EQT VIII, was approximately €4 billion larger than its predecessor fund, EQT VII.

Carried Interest Recognition

Moving to the next slide and the second part of our revenue lines which is carried interest. This is a bit of an educational slide with a fair amount of text but firstly we have a conservative way to account for carry, where we take discount on the unrealised valuations of the underlying assets. It is for an external party. It is not possible to exactly replicate without access to the underlying financials and we will obviously do the exact calculation.

However, we have given the markets here a rule of thumb that the initial recognition would normally take place when you are at around 1.7-1.8x gross MOIC in a fund and usually you also need to have a few exits. Based on experience, this would normally occur 4-6 years after the first investment. That is the general guidance on when carry would be recognised.

On the right-hand side of this page there is the status of the carried interest recognition for our key funds. EQT VI and Infrastructure II, they are already in carry recognition mode. EQT VII and Infrastructure III are illustrated here. You can compare that to the rule of thumb that we are on EQT VII getting close but we are not yet in carry recognition mode. As we have stated earlier, we do not expect to recognise carry from EQT VII during 2019. EQT VIII and Infrastructure IV, they are in the investment period and thus some years away from carry recognition.

Continued Growth in Number of Employees

We said that it is all about people and we are continuing to grow our talent pool. It is according to plan, I would say. As of September we were 675 employees and will continue to grow that as well.

Our Financial Targets and Dividend Policy

Moving on to the last page and the targets, our financial targets and dividend policy. There is no news here really but let me just reiterate them anyway. Our target is that the revenue growth should exceed the private market’s long-term growth rate. The latest available market expectations were about 10% compound annual growth rate, between 20% and 25% but our target is that our revenues will grow faster than the market. Not in every single point in time or every year but over fund cycle, let us say. We have said that we have a profitability target that our EBITDA margin should be at least 55-65%. Our adjusted EBITDA in H1 was at 47%. In terms of dividend policy we will have a steadily increasing annual dividend in absolute Euro terms and the Board of Directors is expected to propose that approximately €200 million will be paid out as a dividend for the current fiscal year in equal instalments next year. With that, the formal part of the presentation is concluded and we open up for questions from the listeners.

Q&A

Magnus Andersson (ABG): Good morning. My first question is around the preparations for the successor fund, EQT IX, where you said that fundraising is expected to begin in 2020. Can you give us some flavour of what we should expect in terms of when you would possibly launch it?

Kim Henriksson: The way you should think about the fundraising is given the guidance of 80-90% invested, at that point in time we want to be able to invest out of the successor fund. When do we reach 80-90%? We do not know. It depends on which transactions will happen and when they will happen. However, based on historical pace we have said that 20-25% per year, it would be well within a year from now. At that point we would like to be ready. Not ready with the fundraising but be able to start investing out of the new fund. How long does it take in between there? The whole fundraising may take anywhere from six months to a year or more but we expect that we should be able to invest out of a new fund in a shorter period of time than that.

Magnus Andersson: Okay, thank you. My second question is on the continued ramp-up in the number of employees from here. You are now at 675 or so in September 2019. What should we expect in the coming year?

Kim Henriksson: We are continuing to ramp-up, you are right. We are ramping up according to plan. What we have said is that the percentage term change in number of employees is likely to go down, whereas the absolute number is probably in the same region as it has been in the recent past, 100+/- some persons on an annual basis. We have also said that in a normal year you would expect the second half of the year to have a slightly higher increase of employees. That has to do with how the bonus structures and other things work in the financial industry.

Magnus Andersson: Okay, thank you. Finally, you were talking there on slide ten about normal commitment period versus the actual commitment period in the last fund generations. Why do you think the commitment periods have been shorter in the last fund generations? Going forward is there still 4-5 that you think is normal or is that more conservative?

Kim Henriksson: If you look at it over even longer time period you could say that the three-year or something around that is not abnormal in any way. Then you will have time periods during recession where that would be a longer period again. On average maybe the normal is 4-5. We feel that the 2-3 year is reasonable currently. It is in line with what we are currently doing.

Magnus Andersson: Okay, thank you very much. That is all from me.

Kim Henriksson: Thanks.

Peter Kessiakoff (SEB): Good morning. A follow-up question on the fundraising. Could you tell us what kind of news flow or comments should we expect from you over the coming year in terms of the EQT IX fundraising, given that you are new on the market? What should we expect in terms of communication apart from what we have got from today?

Kim Henriksson: I think the next step in terms of communication that you should expect is that when we launch the fundraising we will come out and mention that. At that point we will also set a target size for the fund and we will announce that. Then after that it depends a bit on how the fundraising then develops as to what information we will come out with. However, we will ensure that the market is always aware of main aspects that could impact our share price of course and that there is not any difference in information available to the various participants in the capital markets.

Peter Kessiakoff: Okay but will we get any information on how much has been committed of the fund size for how that actually develops?

Kim Henriksson: I will not commit to that. That depends on how the fundraising goes.

Peter Kessiakoff: Okay. Then a second question on the carried interest. As you reiterated, we should not expect that EQT VII goes into carry during this year, even though it is at 1.7x gross MOIC so it could very well start to generate carry. However, the performance there improved another 0.1x in this quarter and assuming that continues to the end of the year, should there be any impact of that to perhaps the carry that comes through is even more front-end loaded than perhaps we have seen in historical funds? Or is this just in line with ordinary development?

Kim Henriksson: No, we do not see that this differs in any meaningful way from ordinary, if there is such a thing as ordinary. As we have mentioned, it does differ quite a lot as to when a particular fund enters carry mode. The range has been between 2.5-6 years or something like that so it can differ quite a lot. However, this should be normal.

Peter Kessiakoff: Okay, thank you. Those were my questions. Thank you for that.

Kim Henriksson: Thank you.

Mike Warner (UBS): Good morning. Thank you for the opportunity to ask some questions. Going back to the fundraising and the expectations for EQT IX, I was wondering if you could provide a little bit of colour as to how long the fundraising process lasted for EQT VIII and Infrastructure IV. I know these cycles will change dependent upon external environments but any colour there would be quite helpful. From when you announced the fundraising to the final close.

Kim Henriksson: First of all, I would say that the final close may not be the right timing to think of. Since we would start charging fees on the fund from when we start investing out of that fund and close the predecessor fund for new investments. Essentially that is they key timing from a financial model point of view and even if we then add to the fundraising after that also those funds would then pay management fees from the first day of that fund opening up for investment. Really the key timing determinant is, when will we close EQT VIII for investment and with that one we do not know. It depends on which transactions will take place, which ones will happen here over the course of the next 6-12 months.

Mike Warner: Okay, thank you. Then in terms of the recently raised primary proceeds from the IPO, you have indicated that you plan to see seed certain strategies. I was wondering if you had any indication as to when we might see those strategies being launched. Whether we should think about that as a 2020 or potentially 2021 event, particularly when it comes to the CLL products, the managed prime product which you guys have indicated. Thank you.

Kim Henriksson: The IPO was concluded about six weeks ago and we had the plans in place at the high level of what we would like to do. Some of them, like the CLLs are fairly well-advanced and good already comments here during the current year or at least next year. Real Estate managed to prime probably earliest next year and then the other part which we discussed during the IPO process is growth or venture growth or growth equity, which also we have developed plans to initiate possibly already during the course of next year. We do not have any specific launch dates on any of these but we are advancing well in our plans.

Mike Warner: Excellent, that is very helpful. Thank you very much.

Gurjit Kambo (JP Morgan): Good morning, a couple of questions. Firstly, in terms of the investing you mentioned a couple of deals you have done in the US. I am trying to get a sense of where you are seeing most opportunities by geography for investing. That is the first question. Then secondly, in terms of the gross exit, I know we should not look at it on a quarterly-by-quarterly basis but exits were slightly lower in Q3 versus what you saw in the first half. Is that just the lumpiness or should we read anything else into the gross exit during the quarter? Thank you.

Åsa Riisberg: Maybe I comment on the investment activity. The way we think about the investment opportunity and the pipeline there, we really apply a thematic investment approach which means that we look at the interesting subsectors that have interesting fundamental growth drivers, non-economic growth drivers like demographics, environmental trends or underlying growth that we like. Then we combine that with the local execution so we have local people in the geographies where we are investing. We have a very strong network of offices in Europe and we are building out our presence in North America. The way I would think about it is that the composition of deals is currently what we expect it to be going forward so we will see a mix of North American and European deals. I do not think there is any major difference in the deal flow. It is more that in the recent time period we have seen a few very attractive opportunities in the North American markets on the Private Capital side that we were in a unique position to acquire. We are very comfortable with those investments and equally on the Real Asset side, the [Inaudible], for instance, that we talked about before. We have been doing fibre investments for 20 years so we are quite well-positioned to do fibre deals whether it is in Europe or in the US. I think the composition that you have seen historically is what you can expect going forward. However, obviously we are still under indexed in North American market compared to many of our competitors.

Kim Henriksson: On your second questions with regards to gross exit I would not read too much into one quarter. We still find the exit environment supportive. Maybe it has grown a bit more selective during the course of the year but I wouldn't say that the Q3 is a materially different exit environment from the rest of the year. I would put it more down to the lumpiness for the time being.

Gurjit Kambo: Thanks very much.

Jakob Brink (Nordea): Thank you and sorry for coming back to the question once again, but EQT IX if I understood it correctly, just to get the data right, you said you want to be ready to invest when the old fund reaches 80-90%. Is that correct?

Kim Henriksson: Yes, that is correct.

Jakob Brink: With the current speed of investment is it not also correct that you should be basically at 80-90% at H1 2020?

Kim Henriksson: Whether it is H1 or after H1, I do not know. We do not know that, whether the deals will come through. We have a number of fairly significant transactions happening during the course of this year but if you just do a mathematical exercise you would end up in the latter part of the period you mentioned.

Jakob Brink: If you do not know, which I guess you cannot know, if it is actually going to be in the last part of H1, would it not be prudent to then start of fundraising already just after Christmas? How does that normally work?

Kim Henriksson: Fundraising is a process, not vastly dissimilar to an IPO. First of all we are in continuous dialogue with our fund investors during and between fundraising. Then you start, for lack of better words, using pre-marketing, i.e. start warming them up, telling about how their predecessor fund is doing and how things are going. Then the formal launch is then a further step in that. You accelerate those steps. That you have not started the formal launch does not mean that you are not fundraising or marketing or thinking about the fund, together with your investor base. It is a gradual process, I would say. I do not dispute your comment though.

Jakob Brink: Have you had those pre-marketing meetings?

Kim Henriksson: We are meeting with our fund investors, yes.

Jakob Brink: Okay. Thank you. Then I have seen some news recently that KKR and Carlyle have been out raising record lots of European funds in Private Capital recently. In that light, how does that make you think about the target size for EQT IX?

Kim Henriksson: The fundraising market also continues to be supportive and we have seen some very large fundraising from some of our competitors. Part of the pre-marketing that we are doing is also discussing with our investors about their appetite of course. The second element is that we are making sure that we have the pipeline of deals and the resources available internally to ensure that we can deploy then the fund size that we are after in attractive investments and in a reasonable timeframe. All of these taking together will then determine the fund size. For the time being I do not have any better guidance to give than that the increase in our predecessor funds was about €4 billion.

Jakob Brink: Okay. Many thanks for the help.

Kim Henriksson: You are welcome.

Arnaud Giblat (Exane BNP): Good morning. I have got a couple of questions, please. Firstly, the investment environment has clearly been strong over the last nine months. I wondering looking forward is that something you expect to continue to remain the case, assuming that equity markets remain flat and nothing happens to the debt markets? My second question is, aside from fund IX, is there other areas where you might be looking at raising further funds? I am thinking maybe in mid markets or in credit in 2020. Thank you.

Kim Henriksson: Was the first one about listing environment?

Åsa Riisberg: No, in the investment activity whether you think it will continue to be strong.

Kim Henriksson: Yes, we do. We see no signs of it not continuing to be strong. The pace in the third quarter has been similar to the earlier part of the year and we still see good and attractive opportunities out there. We continue to believe in that. When it comes to other fundraising, the ones that are in the market now are Ventures II and Real Estate II. We are on plan and making good progress on those so let us get them done here in the short-to-medium term. I am not going to give out any specifics on that. Obviously, we have some open-ended funds such as Public Value, which is in continuous fundraising, you could say.

Arnaud Giblat: That is great. Thank you very much.

Bruce Hamilton (Morgan Stanley): Morning, thanks for taking my questions. One on investments and one on fundraising, if I may? I guess we are now at back to peak leverage levels in terms of debt to EBITDA in deals based in Europe and the US. I guess some of your peers have mentioned certain sectors becoming more challenging to find value, including tech and healthcare. I understand your thematic and sector-driven approach but some of those sectors seem to be amongst the hotter ones. What is your level of confidence or how do you get comfortable that you can still drive the MOICs you have achieved historically if that is the case? Or do you think that is not the right way to read the investment environment? Then secondly, on the fundraising the €4 billion increase you saw between EQT VII and EQT VIII, you mentioned that a couple of times. Are you trying to give an implicit guidance to what you see the increase might be in the following fund? That was the way I read it but I do not know if that was an over-read. Thank you.

Kim Henriksson: On your first one, yes we are thematic and I would also say that historically we have experienced that we are great investors in growth companies, in making good companies excellent and that means that we are going to be paying full market price for those companies. If you look at it over a slightly longer period of time of course we need to work harder and smarter to create those same returns but that is also what we are doing. We still think that we can find attractive investment opportunities also in the sectors you mentioned and reached the same MOIC targets as before. That is one thing. Secondly, I am not going to give any formal guidance on the size of EQT IX.

Bruce Hamilton: Okay, thanks.

Kim Henriksson: Thank you so much, great questions. I hope this was useful for you listeners. We had a good first quarter as a listed company. Obviously, there were no major surprises, we hope, in this. It was only six weeks since the listing and we are looking very much forward to continuing the dialogue with all of you over the course of the next quarters and years. Thank you so much.

[END OF TRANSCRIPT]