**www.rsepconferences.com CONFERENCE PROCEEDINGS/FULL PAPERS ISBN: 978-605-73146-5-9/December 2022**

*Pisaniuc, M. & Jomir, E. pp.125-133*

# Analysis of the Activity of Private Equity Funds in Terms of Driving Innovation on the International Market: Prospects for the Republic of Moldova

**Maia Pisaniuc[a] & Eudochia Jomir[b]**
*[a]Ph.D. Associate Prof. Center of Innovation Business Research and Consultation Academy of Economic Studies of Moldova (ASEM), Moldova*
*E-mail: maia.pisaniuc@ase.md*
*[a] PhD student, University Assistant, Academy of Economic Studies of Moldova (ASEM), Moldova*
*E-mail: eudochia.jomir@ase.md*

**DOI:** https://doi.org/10.19275/RSEPCONFERENCES232

## Abstract

In today's world, private equity funds have emerged and are growing rapidly, offering new investment opportunities for the population. In the last decade, this industry has become one of the main investment players acquiring banks and companies both in Europe and globally. The dynamism of their development, the areas in which they direct their capital or risks and the prospects for the development of these structures in emerging countries are the subject of this research. Starting from the elucidation of the concept of the emergence and development of private funds, the analysis of their trends on the European market, as well as the comparative analysis of what they offer in comparison with other investment possibilities, in terms of innovation, efficiency and sustainability of investments. This research topic is of particular interest because private funds are currently not developed in the Republic of Moldova and in this case it is necessary to argue the need for the establishment of this type of structures, their functionality. Comparing the activity of private funds on the Romanian market and clarifying the prospects for their development in the Republic of Moldova are the key aspects of the study. Research methods: analysis, synthesis, deduction, correlation, based on the analysis of factual data.

**Keywords:** private equity, funds investment, innovation structure, investment risk
**Jel codes:** G23, G24

## 1. Introduction

Modern financial markets are very complex. This complexity is compounded by the nature and pace of financial innovation that has emerged under the impact of information technology. The main providers of financial innovation are generally financial intermediaries such as commercial and investment banks, securities dealers, investment funds and insurance companies. One of the innovative structures is private equity, which, due to its rapid growth in recent times, has led to the need to study the forms that these players take, and to analyse the areas and risks to which these new structures are subject on the international financial market. Although "private equity" in free translation means private capital, the term often refers to "private equity funds", which are usually closed-end investment funds whose main purpose is to invest in various private companies for different purposes, either for growth in the case of small companies or for development and expansion in the case of medium and large companies. Although some private equity funds have cash on hand from individuals (as family investments), most come from partnerships with institutional investors such as investment banks, pension funds, insurance companies, various financial institutions and even corporations wishing to promote new products or innovative technologies.

This dynamically growing private equity fund investment vehicle grew by 50% from 2009 to 2019, but significantly less than the 150% growth in acquisitions and mergers, traditional private equity over the same period. The main PE funds known to be in the market are Hamilton Lane, HarbourVest Partners, Pathway Capital Management, Fort Washington Investment Advisors, AlpInvest Partners and Adams Street Partners. Where the dominance of US funds can be seen.

In the literature reviewed on this topic, the capacity of private equity as a tool to drive disruptive innovative activity is not reflected. In this article, we have analysed the trends, the effectiveness of private equity in this respect, as well as the possibility of extending these structures in countries such as Romania, the Republic of Moldova

## 2. Literature Review

The bibliography used in this article has been varied in order to obtain the most complete information, starting with books and academic and journalistic texts. As it is a topic discussed in recent years, we would like to mention several sources were used from the SSRN database, journalistic articles as well as information published by banks and interviews with experts in the field interviews with experts in the field.

Books and academic texts were found through search engines such as Google Scholar and also books and academic articles.To broaden the geographical spectrum, foreign sources such as Pitchbook, Preqin were also used. We were also aided by reports from leading financial firms such as PwC, Cambridge Associates and Mckinsey. Associates and McKinsey, Preqin, Pitchbook, Delloite company reports, Fortissimo Capital. Also some information enlightened in the information of companies, funds in Romania and Republic of Moldova, as well as some aspects mirrored by the author, in previous publications.

## 3. Data and methodology

For the purpose of conducting the given study, we used data from global reports such as pitchbook and others mentioned in the literature study. As research methods we used statistical data analysis, synthesis, and comparison of results in European countries by private equity funds, also globally.

We also used inference and interpretation of data, economic forecasting of the possibility of expansion of these financial structures in countries such as Romania, a country where these structures operate in their infancy. The relevance for private equity development, such as in the Republic of Moldova, where there are currently no such funds, but which would certainly contribute to the development of disruptive innovations.

### *3.1. Global private equity trends*

According to Roland Berger (2021), the target industries in 2021 are mainly technology, media and software, pharmaceuticals and healthcare, as well as logistics services. The geographical regions with the highest growth compared to 2020 are expected to be Germany (+4.6%) and Scandinavia (+2.8%) (Roland Berger, 2021). With the economic recovery underway, economic activity has picked up and private equity funds are becoming increasingly proactive in managing the crisis. The net asset value of the private equity industry has grown by 600%, and since 2002 - twice as fast as global public equities (McKinsey Global private markets review 2019) - and it is therefore important to understand how they perform in abnormal economic conditions such as recessions. Like private equity, European venture capital also saw an impressive start in 2021, with startups raising $21.4 billion in Q1, representing a more than 100% increase in funding year-over-year (Crunchbase News, 2021).

Europe-focused private capital AUM has doubled in seven years, rising from €1.3tn in 2015 to reach €2.2tn at the close of 2021. Venture capital is doing particularly well, with COVID-driven innovation attracting investors to the region. However, while venture capital fundraising has held up, private equity fundraising to the end of June 2022 was €34bn, against €136bn across 2021.Another important record was the creation of 16 new unicorns in a single quarter, compared to 15 unicorns that emerged across 2020 (Crunchbase News, 2020).

Since the previous recession, the PE industry has expanded greatly, with assets under management (AUM) expected to reach $5 trillion by 2023 (Preqin,2021). But these changes are not only significant for what is currently happening in the industry, but also for how the industry will react to the next economic downturn. The first major difference is the abundance of capital that has accumulated as private equity has become more attractive; this attractiveness can be attributed in part to the growth of shadow capital. In this study we wanted to look at the financing possibilities of emerging innovative areas of bussines and what private equity offers compared to other players. Alternative assets advanced in 2021, with record levels of fundraising, investment, exits and performance across many asset classes. Preqin expects AUM to grow from $13.32bn currently to $23.21bn in 2026.

**www.rsepconferences.com CONFERENCE PROCEEDINGS/FULL PAPERS ISBN: 978-605-73146-5-9/December 2022**



*3.2. Private equity business concept*

Based on the assumption that these types of funds, invest only in private companies, not listed on a regulated market (stock exchange), and that the assumed investment horizon, in a favourable economic environment, is around 5-7 years, and that common investment strategies in private equity funds include: leveraged buyouts, venture capital, growth capital, distressed investments, we made an analysis of the methods and results achieved by these players in recent years and mapping the future directions, the perspective of these investors in promoting innovation. The activities of venture capital funds can be divided into three main groups: investment, monitoring and withdrawal.

Investments start with the exploration of new opportunities by the venture capital fund and do not end until a contract has been signed. For each investment made, a VC can explore hundreds of possibilities. Of those hundreds, perhaps a few dozen will be worthy of detailed consideration, and an even smaller number will merit a preliminary offer. Preliminary offers are made with a term sheet, which outlines the proposed valuation proposal, the type of security and the proposed investor control rights. If this term sheet is accepted by the company, then the VC conducts a thorough due diligence, looking at every aspect of the company. If the VC is satisfied, all parties negotiate the final set of terms to be included in the formal set of contracts to be signed at final closing. These investment activities - particularly the evaluation and term sheet structure - are ideal topics.

Once an investment has been made, the VC starts working with the company through board meetings, recruitment and regular advice. Together, these activities comprise the monitoring group. Many VCs argue that these activities provide the best opportunity to add value and are the main source of comparative advantage for a successful VC. This argument may indeed be correct, but monitoring activities do not lend themselves well to quantitative analysis. Even though loans to PE-backed companies have generally been underwritten by banks, but note that today there is an increasing amount of debt underwritten directly by private credit, in a process called "disintermediation of the banking market".

Also, the secondary private equity market is becoming increasingly popular, which has shown strong resilience during the pandemic, with market value ending 2020 at $60 billion and fundraising down just 6% from 2019. More importantly, in 2020, GP-led secondary transactions amounted to the majority of secondary transactions. These results being recorded because they can buy, or invest in, riskier companies with higher returns in the future, as well as invest in unlisted companies. In 2019 alone, PE funds invested more than $14 billion in healthcare (up from $3.5 billion in 2013), and a significant portion was related to artificial intelligence applications, whose relevance in healthcare and pharma has progressively increased. Currently, the main uses of artificial intelligence are in improving diagnosis, virtual healthcare and data analysis.

**Table 1.** Private equity assets under by fund type globally, în percent%

| Tipuri de investiții PE | 2016 | 2020 |
|---|---|---|
| Boyout | 16,7 | 31,4 |
| Venture capital | 31,3 | 43,4 |
| Growth | 25,2 | 21,0 |
| Other | 24,8 | |
| | | |

**Source :** elaborate by autor, in date Preqin

In addition, the experience of the funds' professional teams is fundamental in accessing high performance opportunities as well as creating partnerships that lead to superior returns for the private equity asset class. Finally, it is worth highlighting the potential for economies of scale that allow, for example, for in-depth business and legal analysis of potential investments that would otherwise be burdensome for a single investor. In the near term, these players can create a closed cycle, from investing, lending, reselling, higher upside than advisory firms, or investment banks that are fairly significantly regulated and operate more on stock exchanges.

www.rsepconferences.com CONFERENCE PROCEEDINGS/FULL PAPERS ISBN: 978-605-73146-5-9/December 2022



### *3.3. Comparative analysis of private equity activity in european countries*

The given study was complicated to conduct due to lack of relevant statistics, but nevertheless we have comparatively analysed 2 European countries, UK and Germany, in which areas private equity is directed in 2019. As a result, we can state that predominantly, private capital was directed towards Information Technology and Fintech in the UK.

In Germany, although more diversified investment area, during Q1 we see a similar trends towards Fintech. From this, we can also deduce the investment trend in PE after the pandemic period in the European market.

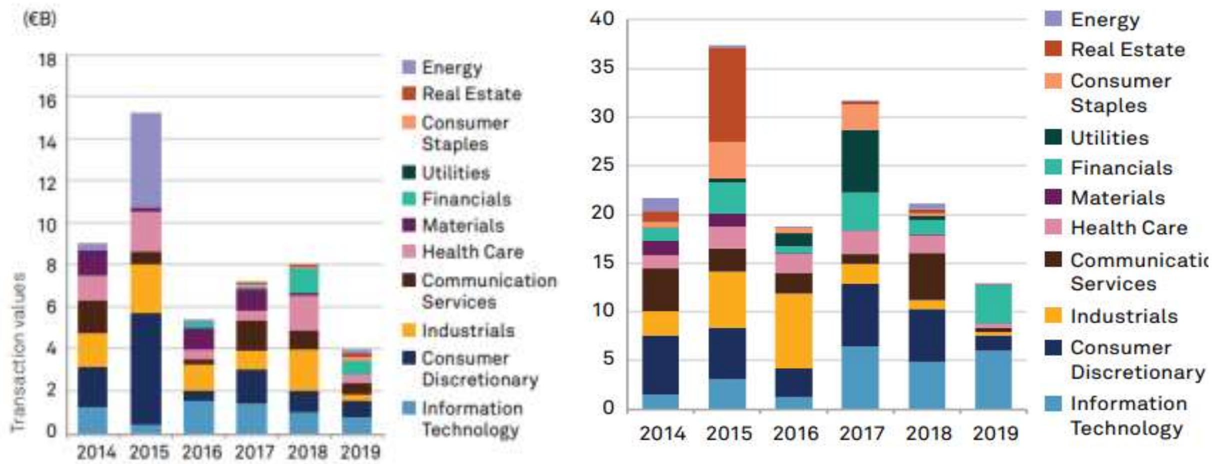


**Figure 1.** Areas of PE investment in the UK, Gemania 2014-2019

**Source:** www.spglobal.com/marketintelligence

The areas of investment over the years 2014-2019, shifted towards information technology, financials, compared to 2015, where real estate and utilities were the main sectors for PE investment. During 2015 the priority areas in Germany being the energy sector, consumer sector, utilities, in recent years information technology, and innovative start-ups in the financial sector. If we analyse by country, where PE funds are developed, the most dynamic in this respect is the UK, the Nordic countries, France and the Benelux countries (see figure 2)

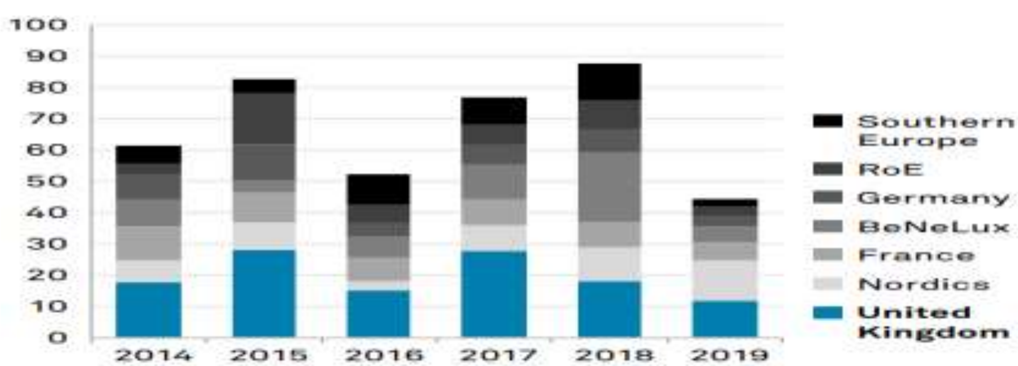


**Figure 2.** Evolution of PE development in Europe 2014-2019

**Source:** www. www.spglobal.com/marketintelligence

www.rsepconferences.com CONFERENCE PROCEEDINGS/FULL PAPERS ISBN: 978-605-73146-5-9/December 2022



One thing worth noting, from the analysis of where German private capital is reallocated by region, we see a huge preference for Latin America, Romania, France.

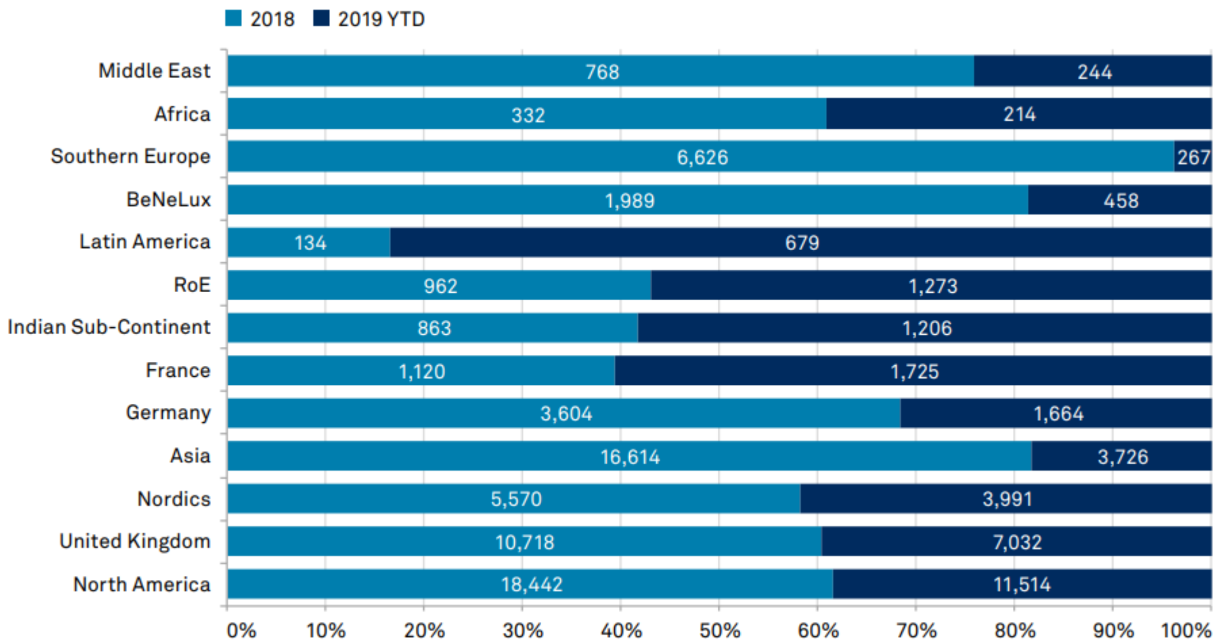


**Figure 3.** Relocation of German private capital by region 2018-2019

**Source:** www.spglobal.com/marketintelligence

*3.4. Analysis of private sector investment areas*

Looking by region, we see much of the Middle East is in turmoil, with some nations establishing themselves as investment hubs. For example, Israel, Saudi Arabia and the UAE are all very active in both the PE and Venture Capital landscape, with over 70% of market participants expecting deal activity to improve in their region for the next year (S&P Global Market Intelligence, 2020). The primary sectors being targeted by Middle East funds are Healthcare, Fintech and Education. Also notable is the increasing participation in venture capital rounds by non-traditional venture capital investors, including not only corporates but also sovereign wealth funds, mutual funds, hedge funds and private equity funds (e.g. buyout funds). To put this period in perspective, we first look at venture capital investment as a percentage of GDP. Between 2000 and 2018, the US economy roughly doubled in nominal terms, from $10 trillion to $20 trillion. Thus, $100 trillion in 2000 represented 1% of the economy, while in 2018 the same nominal amount represents about 0.5% of the economy. However, this is the third highest amount ever recorded, after only 2000 and 1999, so it is significant.

Although venture capital investment in 2018 is about $70 billion in 2000 dollars, compared to $105.2 billion in 2000, it still exceeds all other years on record. In addition to traditional PE fund investment areas such as IT, Fintech, AI, healthcare, another booming area, especially after the COVID-19 pandemic, has become the Global Space Economy which includes a wide range of opportunities that can create value and has multiple benefits for humanity based on the results of exploration, research and use of space. In recent years, the space sector has evolved significantly, increasing its importance to the economy, particularly in sectors such as meteorology, telecommunications, energy, transport and aviation. In terms of the composition of the space economy, we can identify 10 main drivers of the space ecosystem:

- Satellite launch: one of the largest sub-sectors. Companies focus on technology and infrastructure to send satellites.

**www.rsepconferences.com CONFERENCE PROCEEDINGS/FULL PAPERS ISBN: 978-605-73146-5-9/December 2022**



- Satellite Internet: these companies focus on improved connectivity through satellites, wireless broadband, optical communications, etc.

- Deep space exploration: high-level missions to transport people and goods beyond the earth's atmosphere.

- Lunar Landing: Moon missions and products/infrastructure for Moon missions.

- Earth Observation: Imaging, analysis technology, GPS and more.

- Asteroid Mining: Exploiting raw materials from asteroids and other minor planets, including near-Earth objects.

- Space Debris: These companies track and analyze man-made objects in space.

- Space tourism: Developing access to space for private citizens and space explorers.

- Space research: Companies dedicated to space research and education.

- Manufacturing: Design, development of spacecraft, hardware, propulsion systems, engines and other technologies.

However, broadly speaking, the space industry is considered to be the next trillion-dollar industry by 2040, with revenues that could reach $1 trillion, according to many analysts. In particular, falling launch costs and technological advances will make reaching into space less expensive, offering opportunities in areas such as satellite broadband, high-speed product delivery and perhaps even human space travel. Space-focused businesses are also finding strong support from investors in special purpose acquisition companies known as SPACS. In the 12 months of 2020, 11 space SPACs have been announced, committing more than $7 billion in investment to the sector and providing companies such as Rocket Lab, the New Zealand-based launch company, and Spire Global, the multi-billion-dollar space data group. Many space start-ups have yet to prove, however, that they can operate profitable businesses, and some critics recall the major collapses of companies like Iridium, GlobalStar and Teledesic two decades ago. Amid uncertainty about the future, many private equity funds in Central Europe are increasingly turning to portfolio management, according to the latest Deloitte Central Europe Private Equity (PE) Confidence Survey.

*3.5. Development private equity for boosting innovation in Romania and Republic of Moldova*

In this context, private equity firms are rethinking their investment plans for promising deals. Romania has gradually become very interesting for private equity funds, many medium and large players are opening offices in Bucharest - Highlander in 2018, Mid Europa Partners in 2019 - and local players are managing to attract funds to invest in Romanian SMEs - Morphosis Capital, Black Sea Fund, Early Game Ventures, ROCA, Gap Minder etc. Large private equity firms, intend to enter the Romanian market as they see the country as a good alternative for investments in the region. Such investments will definitely be influenced by the local economic conditions and legislative climate. The latest deals announced by players such as Blackstone, Mid Europa Partners, Revetas, Innova, Abris Capital, CEE Private Equity or Highlander Partners show that they expect the Romanian business environment to grow in the future and that there is still potential for investment.

One thing we can say is that Romanian Financial Investment Companies are already moving towards private equity. As an example, SIF Moldova in Bacau, transformed into the investment company Evergent Investments, which in its plans aims to move towards unlisted companies, but with higher returns. These are the first steps on the local domestic market, but its financial possibilities and investment areas differ from global players on the private equity market. Prospective research shows, if we look deeper, major differences between developed and emerging economies. Investments are predominantly in traditional banking, energy and real estate.

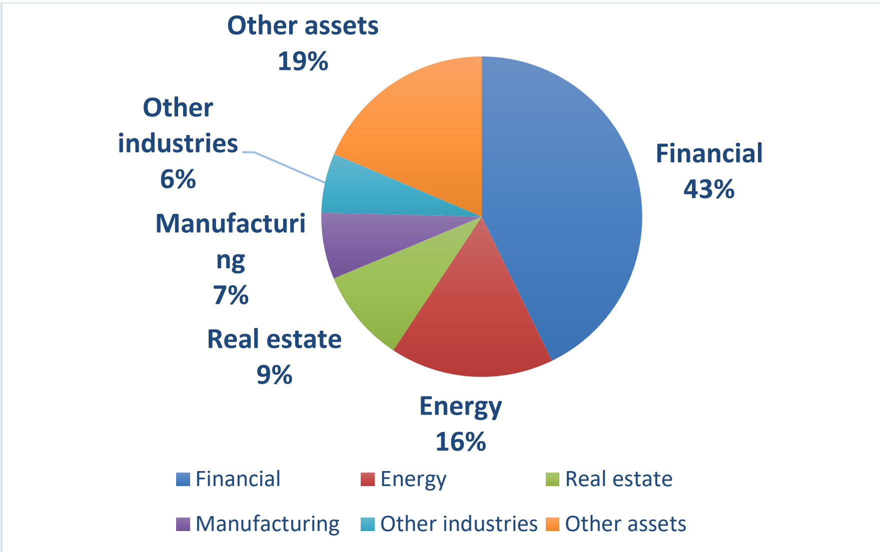


**Figure 3.** SIF Moldova transformed into Evergent Investment, investments by sectors, year 2022

**Source:** Report of the Board of Directors of EVERGENT Investments SA in Q12022

We can mention that both funds are oriented towards the same investment areas, however, SIF Moldova has been reorganized into Evergent Investment and tends to increase investments in private equity in the next period of time.

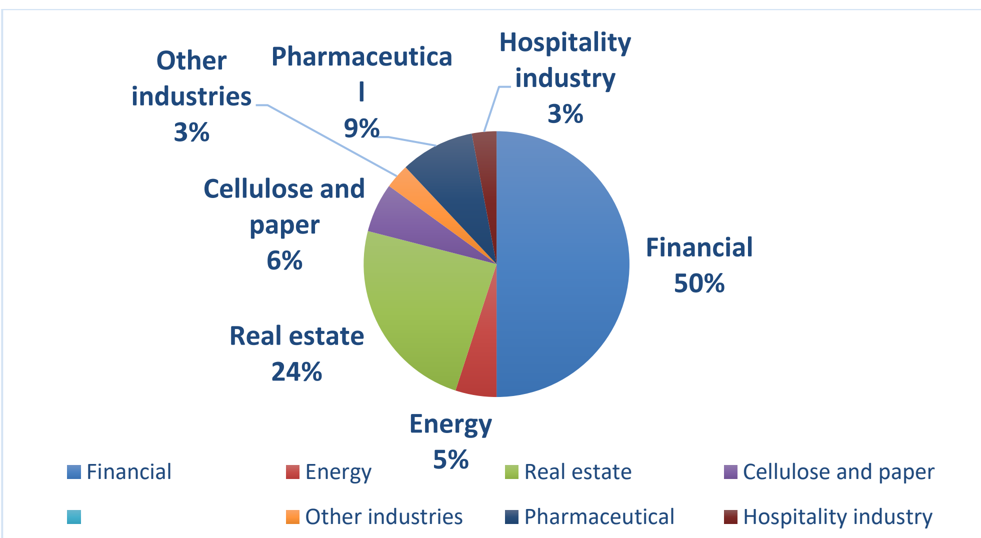


**Figure 4.** Investment by sectors in the SIF Banat-Crisana, 2022

**Source:** Report of the Board of Directors of SIF Banat Crișana Q1

Analysis of the portfolios of these funds shows that they are oriented towards the equity portfolios of Banca Transilvania SA, BRD Romania, Romgaz, Aerostar, BioFarm, SiFimobiliare. Although they differ from private equity preferences in developed countries, they are nevertheless broadly similar directions. In the Republic of Moldova, neither under the legislation are private equty allowed to be established, nor are other funds present on the market. In our country the only methods of financing start-ups are bank loans, which are quite expensive and do not provide much funding, or programs funded by the European Union to promote innovation, but in these cases the amounts allocated are very small, for example, the programs granted by some governmental organizations with the support of the European Union, or non-reimbursable assistance from 12 thousand euros in the form of a grant, or in the form of a loan 88 thousand euros, these programs can not cover the needs of disruptive innovative businesses.The maximum amount being 25 thousand euro grant funding. Increasing the competitive advantage of innovation by 20%. Developing entrepreneurs' skills on planning and implementing business practices friendly to digital transformation of at least 40% of beneficiaries.

The value of the financial package will reach the 15% grant portion and the 85% credit portion. At the moment functional start-ups are from Healtech, - 9 existing, and the invested amounts 700000$, Edtech - are already 8, and the attracted amounts 430000$,- 730000$,in the field of HR Tech are 5, and the amount of attracted investments - 10 000 000$,FinTech are- 5, the maximum amount attracted 430 000$, Social media Tech being 4 - 735 000$ , (based on the data provided by start-up Moldova). There is a direct link now the more innovative the business is as a structure, or the higher its share, the higher the economic level. The given study confirmed these conclusions. Private equity funds can support these companies, develop them. Poor countries are reluctant to take risks, to innovate, they are oriented towards low return areas such as agriculture, industry. Policies are geared towards stability and risk avoidance. And the investment instruments in these markets are bank deposits, or the real estate market.

## 4. Conclusion

The Covid-19 pandemic crisis, the global geopolitical games generated by the war in Ukraine, as well as the economic crisis that the global economy is expected to face, may bring even wider economic gaps between developed economies and the rest of the countries. Because it is precisely countries with innovative, globally oriented economies that will resist shocks. We are today in a period of major transformations, brought about by Information technology, and private equity funds, just show the trends and priority areas in the global economy. These players, which at the moment represent new structures in the global financial industry, are not only oriented in principle towards innovative sustainable areas, but also offer opportunities to invest outside the stock market. We can consider them, at the moment, as locomotives of innovation, as well as those who fulfil the function of strategic financiers, who can contribute to the disintermediation of banks and, in time, to the reduction of the banks' functions in these markets. The funds already offer complex service packages, consultancy, growth investments, start-ups, which although higher risk, cannot benefit from bank funding and cannot be listed on stock exchanges. In this context, they can become in projection, essential players in the mergers and acquisitions market, as well as accelerators of more massive participation of individuals in various investment projects in co-participation with institutional investors.These funds also create competition for banks in attracting deposits as they provide higher returns and the possibility of becoming co-owners of many companies.

*Acknowledgement:* This article is part of the research of the project within the state programme "Shaping innovative business in the context of regional competition" with the number 20.80009.0807.42.

## References

Austin M., Thurston D.(2020),, *Venture Capital Positively Disrupts Intergenerational Investing*, Cambridge Associates, , https://www.cambridgeassociates.com/wp-ontent/uploads/2020/01/VC-Positively-Disrupts-Intergenerational-Investing.pdf

Brown, G., Gredil O., and Kaplan, S.(2019). Do Private Equity Funds Manipulate Reported Returns?, Journal of Financial Economics, 132(2), 267-297

Erdogan B., Kant R., Miller A., Sprague K.,(2016) *Grow fast or die slow: Why unicorns are staying private*, McKinsey & Company, https://www.mckinsey.com/industries/technology-media-and-telecommunications/our-insights/grow-fast-or-die-slow-why-unicorns-are-staying-private#

Fortissimo Capital (2021). http://www.ffcapital.com./ https://pitchbook.com/profiles/investor/11466-55#overview

Global private markets review (2019), https://www.mckinsey.com/industries/private-equity-and-principal-investors/our-insights/mckinseys-private-markets-annual-review

Gupta, Arpit and Van Nieuwerburgh, Stijn,(2021). Valuing Private Equity Investments Strip by Strip. Journal of Finance 76(6): 3255-3307.

Gredil, Oleg and Liu, Yan and Sensoy, Berk A.,(2020). Diversifying Private Equity, Tulane University working paper. Available at SSRN: https://ssrn.com/abstract=3535677.

*McKinsey Global Private Markets Review 2021*A year of disruption in the private markets, https://www.mckinsey.com/~/media/mckinsey/industries/private%20equity%20and%20principal%20investors/our%20in

Mena,(2021),MENA-OECD, Ministerial Conference https://www.oecd.org/mena/events/mena-ministerial-2021/

Michael Neubert (2018) The Impact of Digitalization on the Speed of Internationalization of Lean Global Startups, *Technology Innovation Management Review*, 8(5), 44-54.

M.Pisaniuc**,** (2020) Trends in the development of new business models based on advanced technology and their impact on the global economy**,** monografie colectivă, SWorld, Научный взгляд в будущее»**,** Edition N19, г.Odessa, Ucraina ISBN 978-617-7880-05-

M.Pisaniuc, D.Harcenco,(2021)**.** Use of Artifical Intelligence in the Global Economy, Benefits and Risks, in Conference proceeding "Global science and education in the modern realities " ISBN 979-8-4958014-6-2 DOI: 10.30888/2709-2267.2021-7 Published by: «ISE&E» & SWorld, 2021 USA p.10-20 0,9 c.a.

Mooradian P., Auerbach A., Quealy M. (2013) *Growth Equity is All Grown Up*, Cambridge Associates, June, https://www.cambridgeassociates.com/insight/growth-equity/Acces

Private equity and sustainability,Pitchbook, (2021), https://www.investmentcouncil.org/new-aic-pitchbook-report-private-equity-investment-in-clean-technology-rose-to-over-27-billion-in-2021-hitting-record-high/

Raportul Consiliului de administrație al fondului EVERGENT Investments SA în T12022

https://www.preqin.com/insights/research/reports/alternatives-in-2022

www.spglobal.com/marketintelligence

https://www.financialmarket.ro/terms/private-equity-2/

https://www.preqin.com/insights/global-reports/2021-preqin-global-private-equity-and-venture-capital-report

https://blogs.worldbank.org/allaboutfinance/how-win-private-equity-emerging-market-and-developing-econom