KEYNOTE INTERVIEW

Evergreen specialisation is on the horizon

Demand for evergreen strategies is spurring the 'evergreenification' of private markets, with a focus on specialisation in the private wealth space, say Pantheon's Michael Hutten and Victor Mayer

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Q What opportunities do you currently see in the private wealth market?

Michael Hutten: After working with private wealth investors and alternative investments for the last couple of decades, it feels like the opportunity set has exploded over the last five years alone.

The opportunity in front of us today, both in the US and internationally, is driven by the fact that a wider range of investors are looking to the private markets for the first time, including advisers and individuals who would never have entertained anything other than stocks, bonds and mutual funds in the past.

We also see certain intermediaries – family offices, registered investment advisers, global banks and financial planners – becoming more sophisticated in their approach to the market. What we are trying to do is take our core competencies and the investment expertise we provide to institutional clients and match that with the best vehicles to meet the needs of these investors.

Victor Mayer: The evergreen opportunity set has become truly broad and global. Investors are becoming more sophisticated, and their investable assets are growing rapidly. Ultra-high-net-worth investors currently have around $4 trillion of total exposure to investments and only around 10-12 percent of that is allocated to private markets. For high-net-worth investors, that percentage is just 3-4 percent.

The global market is expected to triple in size to $10 trillion-$12 trillion by 2034, so we will see a significant acceleration of inflows into the overall asset management industry, with increased allocation to private markets. Those high-net-worth investors will eventually increase their allocations by 3-4 percent up to 10-12 percent.

As the market grows, we also expect to see increased interest from a wider range of geographies. Today, the US market dominates, with 55-60 percent of the current $4 trillion, followed by Europe and then Asia. In the next 10 years, we will see a real acceleration of wealth in Asia and Europe, where investors have been increasingly turning to higher-return strategies such as private markets. By 2034, we expect the global market to be more evenly split between the US and the rest of the world.

Q What types of strategies and structures best cater to these investors as they look to access private markets?

MH: The strategies that are now pervasive in the US are private equity, private credit, private real estate and private infrastructure.

Whereas 10 years ago investors may have combined those investments in a catch-all 'alternatives bucket', in recent years they have started integrating them into their portfolios. Instead of thinking about private equity and public equity separately, it is now all equity.

We continue to see a lot of demand for private equity and private credit, but more recently, we have seen more demand for infrastructure. Many allocators have pulled back from real estate and pivoted into infrastructure for inflation hedging, yield and diversification since these investments typically have less correlation to the rest of their portfolio.

From a structuring perspective, Pantheon has coined the term 'evergreenification', referring to these strategies being put into semi-liquid evergreen vehicles structured to meet investor demand. In the US, 40 Act registered funds are a key driver of that.

VM: That same focus on private equity, private infrastructure, private debt and private real estate is evident internationally, too. The three things wealth investors look for are yield, alpha and inflation protection. As we move forward and interest rates start to come down, we expect to see an acceleration of that quest for yield.

When it comes to structures, the international market is different from the US. If you want to launch a fund that can be distributed across all continents, you are looking at potentially over 40 countries with several regional and

Q What does the private wealth market look for when assessing providers of evergreen solutions?

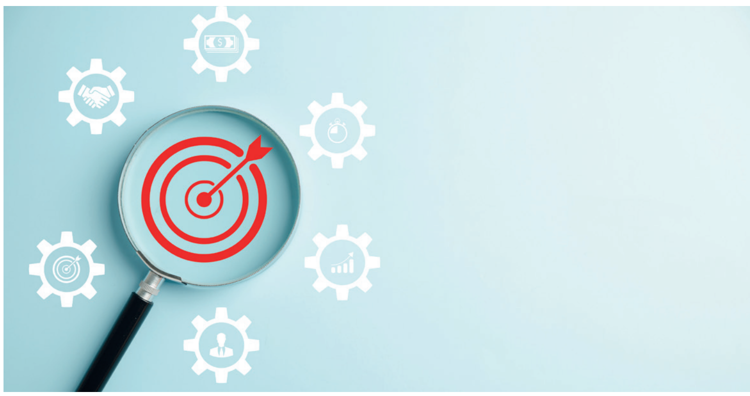
MH: The first thing is experience in managing the relevant investment strategy. Can you show a long-term track record that has performed across different market conditions?

With evergreen strategies, investment expertise needs to be complemented by structuring expertise. Managing an evergreen strategy is very different than managing a traditional drawdown fund. With evergreen strategies, private wealth firms really want to understand your cashflow models, your ability to incorporate that into an evergreen structure, and your ability to navigate across market cycles. Managers of evergreen strategies need to not only invest appropriately but also understand how to manage cashflows and redemptions, something they don't typically do with traditional drawdown funds.

Investors are also looking for secondaries experience. Secondaries act as an anchor for evergreen investments because they can be used to mitigate the J-curve with shorter duration assets and capital coming back quickly.

Other priorities are a robust valuation team and methodology, because investors want to make sure the NAVs they are buying in at are accurate, and have an equitable allocation policy, providing the same investments as the institutional investors are getting in the firm's drawdown vehicles. Then, of course, there is a big focus on risk mitigation.

VM: The themes we hear from clients are expertise and experience in managing the very different needs of an evergreen investment programme – clients come to us because we have both a performance and liquidity track record they can look back at across multiple cycles and analyse to form an opinion. Another factor is transparency around fees, while the third is education. We have learned many lessons, and we can share those with our clients so they can make better decisions and secure better outcomes in terms of performance and product adequacy.



local regulations. You need to set up a series of access points via platforms and local feeders and that takes months, if not years, to build.

Building the plumbing around a fund requires skill and time. Local entities or feeders are needed to create a sense of familiarity in different markets – considering tax, regulation, language and so on. That is essential to success.

We have two listed trusts on the London Stock Exchange, the first of which was launched in 1983, so we understand how that 'evergreenification' works. We have seen both the UK's Long-Term Asset Fund (LTAF) and the EU's European Long-Term Investment Fund (ELTIF) achieve some adoption, but they are not yet completely established, so we will see how those develop.

"The three things wealth investors look for are yield, alpha and inflation protection"

VICTOR MAYER

Q How is appetite for private investments evolving within the private wealth space?

VM: You can look at this in terms of the strategies that investors are looking for and, within that universe, the kind of risk/reward they want. Most investors, when coming to private markets, are looking for differentiation in returns and diversification from a public equity and fixed income-focused portfolio.

We see a clear trend towards specialisation in private markets investing across a number of factors. First, we spend our time on the origination side in the small-cap and mid-cap segments. The evergreen market has seen an acceleration of launches in the last few years and most have been by large-cap-focused GPs, so we aim to bring a different risk profile. We have built relationships with some of the top 150 GPs globally in that small- and mid-cap space, which gives us exposure to a different part of the market and allows us to offer a different flavour of opportunity to the international wealth channels.

The second specialisation theme we see is that most firms are going for a pure-play approach. Many started as one-stop shops providing multi-asset class products and a single point of access, but we now see the emergence of pure-play private credit or private infrastructure funds. Those structures allow investors to decide the risk profile they want.

Finally, we see the emergence of private market model portfolios, where professional managers are making allocation decisions at scale based on centralised research. We see those model portfolios emerging in multiple jurisdictions across Europe and Asia, and view that as a key element in the future for the industry.

MH: In the US, there is a real broadening of scope to make more strategies available for more people. We have seen firms begin to build models for newer participants in private investments. On the other end of the spectrum, the more sophisticated private wealth firms are looking at more specialisation. We are seeing firms targeting specific sectors and stages, and others looking at different asset classes for secondary investment opportunities.

Q What do you expect the private wealth market to look like five years from now?

MH: There are new funds being created daily as managers and providers sense an opportunity to raise more assets and diversify their client bases. If this pace continues, there may be a point where there is not enough demand to meet the new supply and there could be an opportunity for larger firms to acquire and roll up smaller funds.

At Pantheon, over the next five years, we want to be relevant across all areas we focus on, with an evergreen strategy in private equity, private credit, private infrastructure and private real estate. We are going to continue to really lock into our core competencies on the institutional side, and then lean into our structuring expertise and track record of innovation to build evergreen strategies that meet the evolving and increasingly sophisticated needs of investors, particularly in private equity, private credit and infrastructure.

VM: Internationally, we want to leverage our leadership in the US and bring that track record to local wealth channels. As part of that, our core areas of focus will be Asia, namely Japan, Korea, Hong Kong, Singapore and Australia, plus the Middle East and Western, Northern and Southern Europe.

Lastly, there is a significant opportunity in Europe to access the semi-professional market directly or indirectly through the LTAF in the UK and the ELTIF across continental Europe, so we are spending a significant amount of time looking at the opportunity to leverage those structures and deepen our reach into European distribution. ■

Michael Hutten is a partner and head of Pantheon's US private wealth division, and Victor Mayer is a managing director, head of international private wealth, and member of Pantheon's European investment team

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