Unlocking the Potential of Private Markets

Sam Clothier, Investment Director, Private Market Specialist Distribution at Aberdeen Standard Investments believes that private markets can deliver higher returns than traditional public market assets, adding a new source of risk premia to HNW investment portfolios and offering lower correlation to returns in the public markets. He gave a fascinating presentation at the Hubbis Investment Solutions Forum, explaining to delegates exactly why he is so bullish on these private market assets.

CLOTHIER BEGAN BY REMARKING THAT in a typical day in Singapore, an individual might have many encounters with private markets, often without even knowing. This might be in the form of waking up in a bed bought from Ikea, using renewable energy lights, ordering a Grab taxi, doing some online shopping, so on and so forth.

The private market's explosion

"The absolute universe of private markets is far bigger than we might think," he observed, "and covers essentially anything illiquid that is not traded on a stock exchange. And globally, professionally managed assets under management in private markets is about USD5 trillion, a figure that has doubled in the last seven years and that by 2020 it will represent 10% of total professionally managed AUM globally."

Armed with an excellent and very focused set of slides, Clothier added that roughly 42% of that number is in private equity, 46% in real assets such as real estate (closed end funds), infrastructure, agriculture, and commodities with a further 12% in funds of funds. "The USD5 trillion size, to give you a context," he explained, "is about the same as the total Tokyo Stock Exchange."

"Actually," Clothier added, "96% of all companies in the UK are private, and the story is similar elsewhere, but of course public markets are visible and easily accessed. But in fact, the number of public companies in the US peaked in 1996, since when the number has fallen by about half, and this is replicating itself globally, so we are seeing fewer listed companies and private

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companies staying private for longer. So today, private markets offer very broad access to the real-world economy."

Adding liquidity risk premium

He then explained that this is essentially an opportunity to add another lever to investment portfolios. "You currently have credit risk premium, equity risk premium and alternative risk premium," he notes, "and we believe that adding a fourth lever, to generate returns via an illiquidity risk premium, gives the investor an extra avenue to generate returns, and we believe private markets have the potential to offer higher returns than public markets, largely from capturing that illiquidity premium."

And that, he advised the assembled wealth managers, is an excellent incremental offering for their clients.

Private = more flexible

Clothier then highlighted how CEOs of listed companies may be less focused on undertaking capex and instead looking towards the next quarter's profit announcement to the markets rather than the delivery of future returns. "Moreover," he added, "affecting major, strategic operational changes in a company is a lot easier in a private ownership scenario."

Using data from historical returns overlaid with Aberdeen Standard's own in-house analysis, he showed the delegates a 5- and 10-year macroeconomic analysis of what different private market assets would achieve across Europe, Asia and North America, factoring in the political outlook, regulations, tax, inflation expectations, valuations and GDP growth.

Higher returns expected

"We estimate that the listed private markets over the next five to 10 years would deliver an average return of around 6%, but illiquid private markets would achieve an average return of 9% via privately held assets. Moreover, this is all achieved with low correlation to public markets and without compromising growth potential."

He then highlighted Aberdeen Standard's particular skills set and record in this segment. "We

offer a very broad range of private market investment capabilities," he told the audience, "as well as a one-stop global solution. We manage USD85 billion in private markets assets around the world and today have over 400 investment professionals in 19 locations globally dedicated to this sector, making us one of the top 10 largest private market asset managers in the world."

He explained that Aberdeen Standard invests across private equity, private debt, real estate, infrastructure, and natural resources. And this is both via direct ownership of assets as well as via third party manager selection.

Your one-stop shop for private markets

Clothier highlighted a simple access point in Aberdeen Standard's Global Private Markets Fund (GPMF), which launched in early 2018 and that has roughly USD213 million AUM. Investing in a diversified portfolio of private market assets such as private equity, debt, infrastructure, real estate and natural resources, the fund targets a 9% to 12% per annum (net of fees) return over a rolling 7-year period.

"This is an holistic vehicle that offers all types of investors access to what has hitherto been the preserve of institutions and UHNW investors. As a listed vehicle, it has outperformed both the MSCI World index and the Barclays Total Aggregate Corporate basket since inception and has done so with 60% lower volatility than the MSCI benchmark."

He closed the talk by noting that the fund is offered in UK Sterling, Euros, or US Dollar share classes and an Australian Dollar share class will soon follow. ■