KEYNOTE INTERVIEW

More innovation on the horizon for private markets

New investor channels, demand for private capital, and structural mega-trends are opening up new opportunities for fast-growing private markets, says Manulife Investment Management's Anne Valentine Andrews

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Q The fundraising market has been challenging of late, but are there any areas where you have seen strong appetite from investors?

We continue to see strong demand for investments that support the major themes of our time. That includes everything to do with protecting the planet: renewable energy generation, of course, but also natural capital (timberland and agriculture) and sustainable real estate.

Shifting demographics represent another important trend, as does the digital transition. The world is increasingly operating online, and that is creating significant demand for capacity, connectivity and related infrastructure.

Credit strategies have also done well given the rate environment and the reduction in banking capacity.

The final point I would make, meanwhile, is that the big firms are continuing to get bigger. Being an incumbent is highly advantageous as investors want to do more with fewer managers.

Q To what extent is the democratisation of private assets taking hold and what opportunities is that creating?

The focus right now is on retail or private wealth capital. We have seen fintech firms coming in to help make the investing process easier, and more innovation will definitely continue. Average private wealth allocations are at 3-4 percent, while they should ideally be at 10-15 percent overall.

However, I think the really interesting opportunity involves retirement capital, which has yet to be unlocked. All that money that is being put aside to fund future retirements is ideally matched by these long-term assets, particularly now that we are seeing more open-end and evergreen funds.

Q What innovations are you seeing in private markets fund structuring?

For the longest time, the closed-end private equity structure dominated. Investors committed capital to a fund, got it back over time, and then looked for another fund to invest in. Open-end funds are not new, of course – they have existed in the real estate world for 25 years or more. But those open-end funds are now being incorporated into other asset classes, including private equity, infrastructure and credit. One of the key advantages is that these funds offer some liquidity. It is not the same as buying and selling listed shares, but these structures do offer redemptions.

The other innovation involves financing at the GP level, as well as NAV financing. Again, these evolutions are designed to enhance the liquidity profile of private markets. I believe the next innovation will involve unlocking retirement accounts and gaining access to that very long-term capital. Certainly, more innovation is inevitable simply because the amount of capital being amassed in private markets is growing all the time.

Q Where are private markets today in terms of their sustainability journey?

I believe we have reached a point where sustainability is table stakes. It is part of everything we do in the same way that modelling cashflows is. It is certainly what our investors have come to expect.

What is interesting, however, is that while the conversation tended to focus on decarbonisation seven or eight years ago, the understanding of what sustainability entails has since broadened and become more nuanced. Yes, we need to reduce emissions to meet net-zero commitments, but we also need to address systemic inequality and affordable housing, for example. Sustainability is about doing the right thing, not only for the world that we live in, but for all our stakeholders. Fundamentally, it is just good investment practice.

Finally, I would add that the 'G' within ESG is also hugely important, although it seldom attracts as much attention as the 'E' or the 'S'. We spend a lot of time thinking about how to instill best practices around governance in the companies that we invest into.

Q What about DE&I, and gender diversity in particular?

Diversity is certainly something that investors are focusing on more and more. They have moved past policies and practices, and now want to see results. It is far more than just a box-ticking exercise, it is seen as a barometer of organisational health.

After all, it is broadly accepted today that diversity of thought, in all its guises, makes for better investment decisions. That relates not just to gender, but to socioeconomic background and education. LPs want to know you have created an environment where debate and challenge are brought to the table.

I don't think we have yet reached a stage where investors would turn a manager down due to a lack of diversity, everything else being equal. But there is an understanding that positive diversity statistics reflect an organisation that is operating correctly and with a long-term view in mind. There has been progress, but we need to see more diverse talent in leadership positions. There is still more work to be done.

Q What are the biggest challenges and opportunities facing private markets?

If you listen to 10 different economists today, they will give you 10 different views on what is coming our way. That type of uncertainty about what the future holds is always challenging. Meanwhile, there is over $4 trillion of dry powder in the market and that has continued to grow each year over the past decade. That means there is a lot of money sitting on the sidelines that needs to be deployed. Finally, in terms of challenges, I would say benchmarking has become more difficult given strong equity returns in a high-rate environment.

"Companies are increasingly turning to private markets for funding"

In terms of opportunities, I would return to those big structural trends, and decarbonisation in particular. That is creating a huge need for capital across not only infrastructure, but also real estate, natural capital and credit.

In addition, companies are staying private for longer. The number of public companies has declined significantly, which is increasing demand for private markets access. Bank retrenchment, meanwhile, means that companies are increasingly turning to private markets for funding, which is driving the growth of the private credit industry.

And then, of course, we are seeing new pools of capital accessing these asset classes, including retail money and private wealth. However, as mentioned, I believe it is retirement capital that represents the holy grail.

Overall, I am an optimist by nature, and so I see the opportunities as outweighing the challenges. The combination of new channels, banks retracting and companies staying private for longer means there is a large amount of capital that needs to get deployed. ■

Anne Valentine Andrews is global head of private markets at Manulife Investment Management