PRIVATE EQUITY FOR THE MASSES

In practical terms, Private Equity ("PE") is an asset class that is beyond the reach of most investors. Minimum investment thresholds of seven figures (and very often more), multi-year lock-ups, an open-ended commitment to provide further capital at the manager's behest and indeterminate exit time-lines mean that PE investing tends to be the preserve of institutions, foundations, family offices and ultra-high net worth individuals. Those able to participate directly in what is estimated to be a USD4 trillion sub-set of our industry have been rewarded with returns that, by even the most conservative measure, have comfortably outpaced global equity benchmarks. Moreover, this has been achieved with a meaningfully lower volatility than public markets with, by virtue of the manner in which they have been delivered, diversification benefits when combined with conventional asset classes.

For the rest of us mere mortals, access to PE return streams is possible, albeit in ways that come with limitations of some kind.

For those favouring an indirect approach, there are shares in a small number of (mainly US-) quoted asset management companies that specialise in managing PE funds, as well as others whose activities include PE investing among a broader range of activities. These can be accessed individually, or via collective vehicles (including ETFs) that invest in a diversified portfolio of those companies. The main disadvantage of this "first derivative" approach can be seen in performance terms: over the past ten years, for example, only five of these stocks have beaten the MSCI World index on a cumulative total return basis (although it must be noted that a couple have done so by large margins).

The other approach to the asset class is through listed PE vehicles, which can take two forms: companies run by a single PE portfolio manager investing directly into private businesses, or those offering exposure to a portfolio of such companies. This, in our view at least, is the preferable option.

In November 2018, we participated in the launch of an innovative UK-listed vehicle targeting later stage (pre-IPO) private companies, which built on its manager's successful track record of investing in unquoted stocks in the UK small- and mid-cap space within open-ended funds. A stated intention to retain investments after their transition to public markets, along with a specific focus on businesses described as "capital-light, tech-enabled disruptors" were, for us, compelling features that warranted inclusion in client portfolios. Current holdings in its concentrated portfolio include fintech companies servicing both retail and commercial customer bases, e-commerce platform and e-tailing, software as a service, chip design and development.

Continued overleaf

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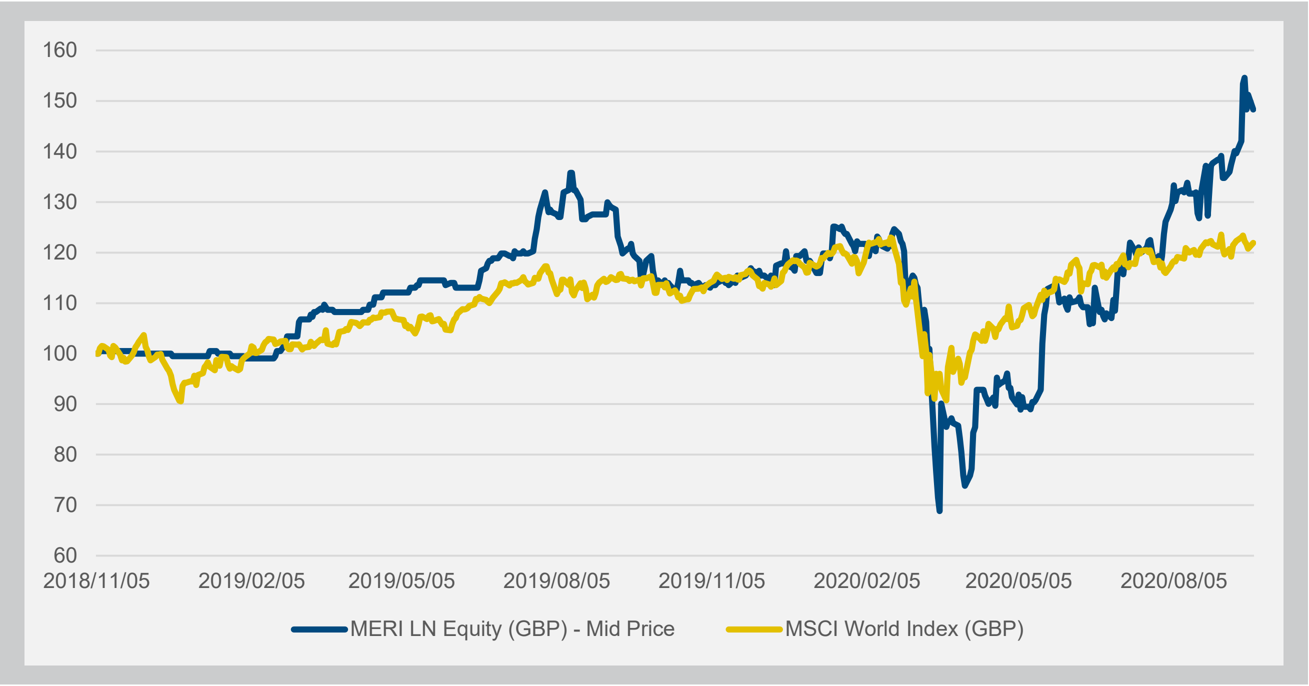
Notwithstanding some nerve-jangling share price movements during the first half of this year*, our first foray into Private Equity has proved rewarding, as the chart below shows. For the vehicle in question, a recent follow-up investment into an existing holding at a significant premium to its original entry price, followed in quick succession by the IPO of another at a multiple of cost, have provided "proof of concept" along with welcome share price strength. Our expectation is that there's plenty more where that came from!

Merian Chrysalis Investment Company vs MSCI World Index (GBP)



Source: Bloomberg

*A notable characteristic of closed-ended funds is the disconnect that can occur between their share price and the Net Asset Value (NAV) of the underlying investments, particularly over shorter periods. This is a reflection of supply and demand for the company's shares, rather than the performance of the assets it holds.

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