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Elston Insights

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Private market managers' return premium persists

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- Owning managers' shares provides liquid access to the sector
- Growing levels of forecast AUM in private markets fuels growth

Evaluating private market managers' performance

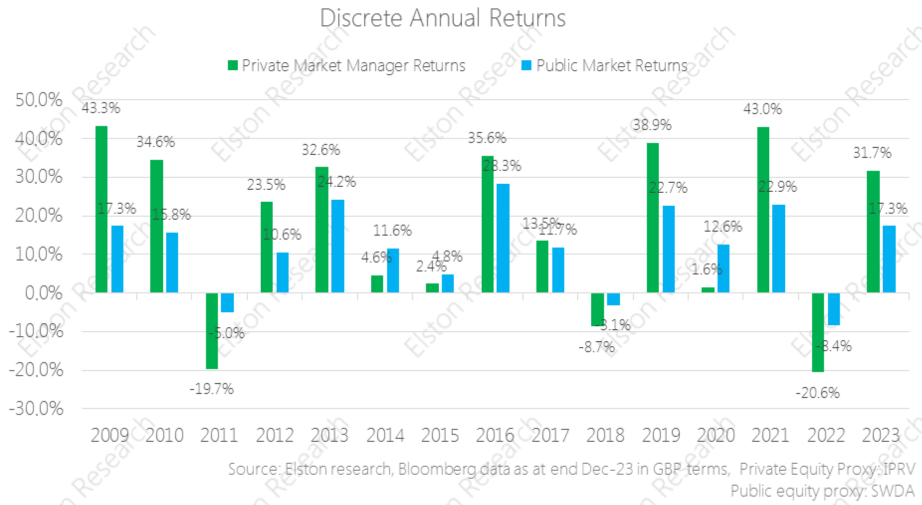
In our Private Market Managers report of 18th February 2022, we looked at the return premium of private market managers (based on listed private market managers' performance) relative to public markets (based on world equity performance). Whilst the characteristics of private market managers are both higher beta and more volatile than world equity markets, the return premium continues and remains persistent.

Why we make this comparison By comparing the performance of listed private market managers (whose shares are publicly traded) to a mainstream public markets benchmark, such as world equities, we can get a picture of the liquid return premium of the sector as a whole, relative to public markets. Any illiquidity premium for a private markets investment should be in excess of the liquid return premium of private market managers, not just of public markets, in our view.

Private markets: high beta

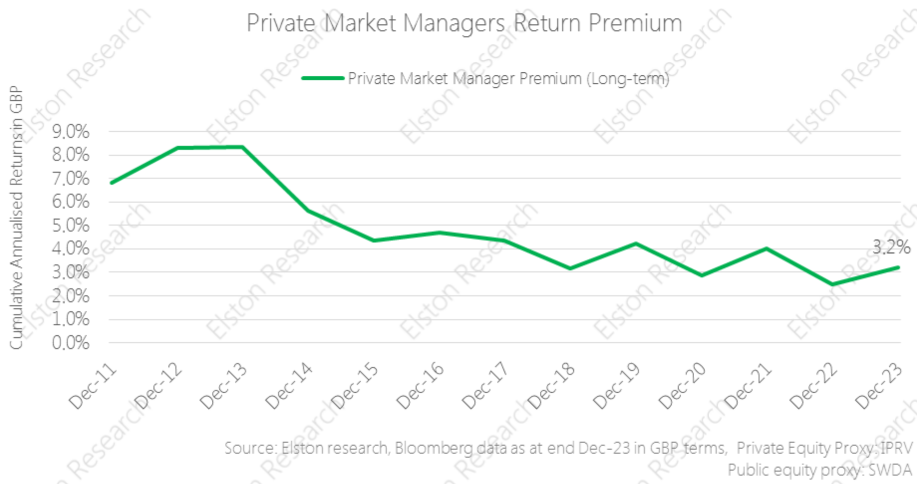
We have updated our long-term public market vs private market manager performance tables. Looking at discrete data, 2022 was a tough year of private market managers as inflation took off and interest rates started their rapid rise. Private Market Managers declined -20.6%, compared to -8.4% for public markets. Conversely, in 2023 despite persistently higher interest rates that could prove challenging for private market funds, the growing level of allocations to private markets and hence fee flows led to very strong performance in 2023, with +31.7% return, relative to +17.3% for public markets, in GBP terms (see Fig.1).

Fig.1. Discrete annual returns: private market managers vs public markets



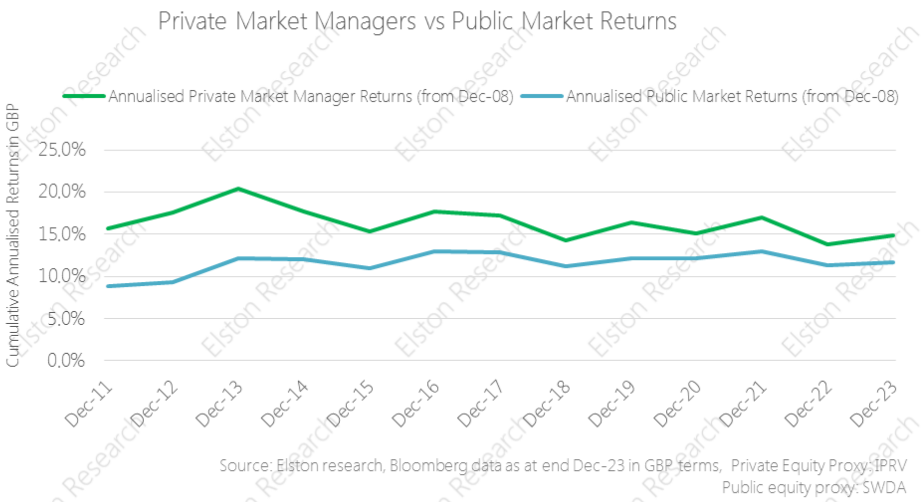
Since December 2008, from when there is sufficient data to enable comparison, the return premium for private market managers over public markets (using world equities as a proxy) is +3.2% per annum annualised in GBP terms as at December 2023. This compares to +4.0% per annum, as at December 2021 and +2.5% per annum, as at December 2022 (see Fig.2).

Fig.2. Private Market Managers Return Premium since Dec-08, as at Dec-23



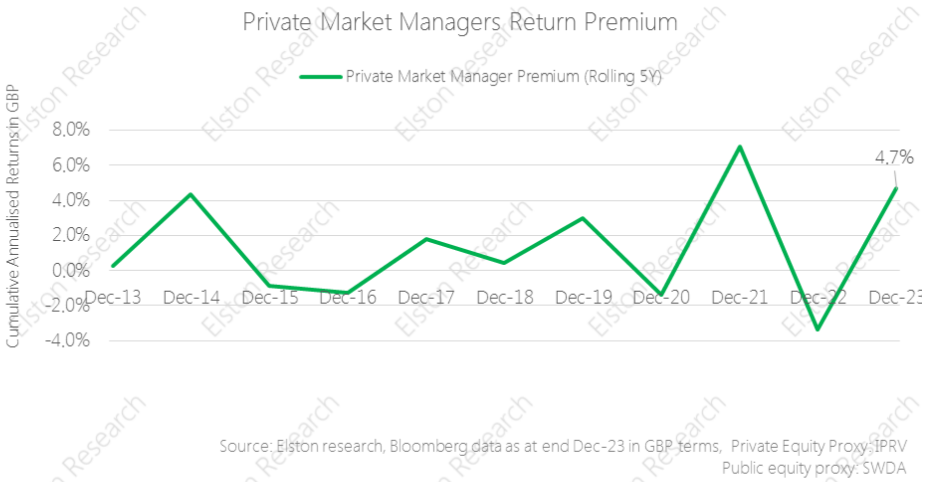
Put differently, since December 2008, private market managers have returned +14.9% per annum, compared to +11.7% per annum for world equities, as at December 2023 in GBP terms (see Fig.3).

Fig.3. Cumulative annualised returns since Dec-08, as at Dec-23



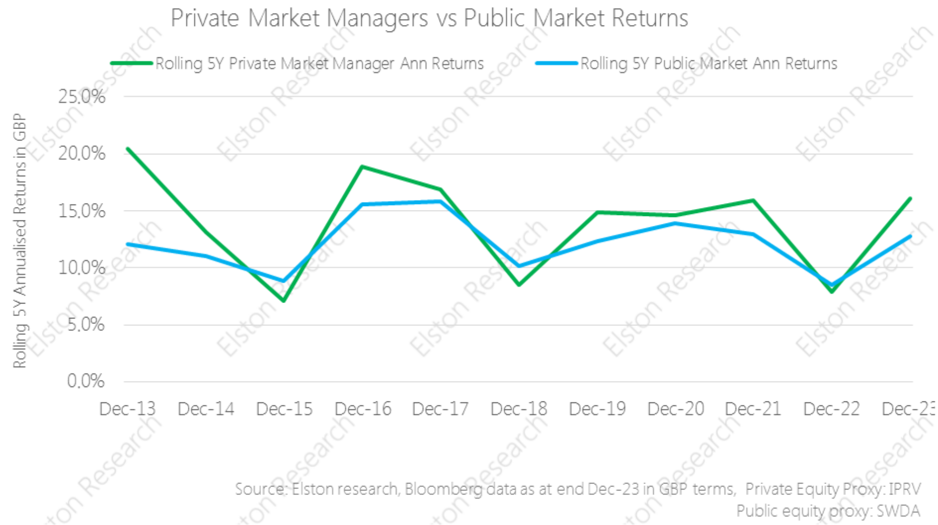
If we look at rolling 5 year periods, following a high of +7.1% as at end December 2021, the private market managers premium moved to a -3.4% discount for the 5 years to December 2022 and has since recovered to a +4.7% premium for the 5 years to December 2023 (see Fig.4). The shorter evaluation time frame means the measured premium will be less stable, compared to the long-term.

Fig.4. Private Market Managers Return Premium (rolling 5 years at Dec-23)



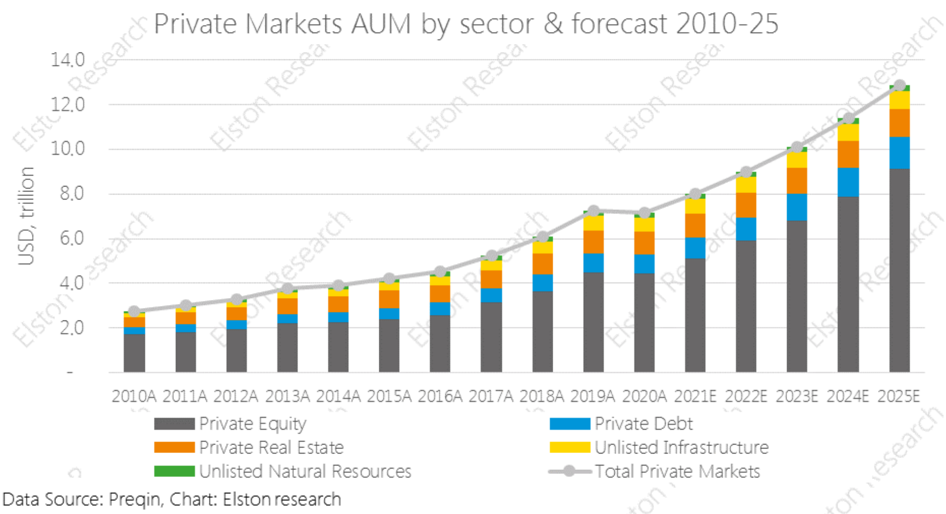
Put differently, for the 5 year period ending December 2023 private market managers have returned +16.1% per annum compared to +12.8% per annum for world equities (see Fig.5)

Fig.5. Rolling 5 year returns, as at Dec-23



Structural growth in private market assets under management should continue to support private market managers' revenues, earnings and hence share price (see Fig.6).

Fig.6. Private market forecast AUM expectations, 2020 to 2025.



Summary

Private Market Managers proved surprisingly resilient in the higher interest rate environment of 2023. The performance pattern of the last two years reinforces the thesis that is worth accepting higher beta and higher volatility of listed private market managers, relative to public markets, given the persistency of their return premium relative to world equities.

Within the Alternatives allocation of client portfolios, a moderate allocation to listed private market managers makes sense to capture the private market mangers' premium in a transparent, liquid and cost-efficient way.

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Further Reading

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