CARTWRIGHT
PENSION TRUSTS

Private Markets

The Pensions Regulator (TPR) has recently issued new guidance and a press release to help pension scheme Trustees consider private market assets as an investment option to boost member outcomes.

The purpose of the guidance, which can be found here, is to make it clear to Trustees that within the right framework and under the right circumstances private market assets can help improve portfolio diversification and return characteristics.

This update aims to summarise some of the characteristics and benefits of these investments as well as draw out some of the reasons why now may be a good time to consider them, particularly in the context of small to medium sized pension schemes.

What are private market investments?

Private market investments are investments in assets that are not publicly traded on stock exchanges. These can include:

- Private equity: Investments in unlisted companies.
- Venture capital: Investments in early-stage companies.
- Real estate: Investments in property.
- Real estate debt: loans to owners of property.
- Infrastructure equity or debt: Investments in, or loans to owners of, infrastructure assets such as roads, bridges, and airports.

Why might private markets be advantageous within a portfolio?

There are a several potential advantages for small to medium sized defined benefit schemes to consider private markets:

- Higher returns: Private market investments have the potential to offer higher returns than public market investments. This is because there is less competition for assets, more work is required to invest in them and to compensate for their less liquid nature.
- Access to new opportunities: Private markets can provide access to a wider range of investment opportunities than public markets. This can include investments in new and innovative companies, as well as real estate and infrastructure assets.
- Diversification: Private markets can help to diversify a scheme's portfolio, which can help to reduce risk.
- Lower volatility: the less frequent pricing of these assets means they can be less susceptible to short-term swings in market price.

- Cashflow – many private market asset classes are cashflow generative, helping Trustees deal with benefit outgoings in a more predictable manner while still boosting returns relative to public market debt.

Overall, it has been estimated that private markets generate c. 1-3% p.a. in additional returns compared to their equivalent public market counterparts while also reducing overall portfolio risk.

However, there are also some important considerations for trustees to be aware of before investing in private markets:

- Liquidity risk: Private market investments are generally less liquid and carry higher risks than public market investments. This means that it can be more difficult to sell private assets and there is a greater risk of losing money.
- Higher costs: Private market investments typically have higher fees than public market investments. This is because it is more expensive to invest in and manage private assets.
- Need for specialist skills: Trustees will need to appoint a manager that has the right skills and expertise to invest in private markets. As there is no "passive" way to access this asset class a higher degree of manager expertise is required.

What types of schemes may be interested in private markets and why now?

Private markets have been invested in by larger pension schemes for many years, with high allocations being made over the past five years in particular. With many of these schemes now considering buy-out in the shorter term they will want to move away from this market.

However for other schemes buy-out is not a short term plan. This can be due to still having a significant funding journey to go until such an event is realisable or alternatively due to not wishing to transfer to an insurer. In particular, the Government's Mansion House reforms, which are designed to enable Trustees to consider alternative paths for their schemes mean that many schemes will want to consider such alternative paths to wind-up. For such schemes a consideration of private markets would serve them well.

Combined with the above, the past few years have seen a plethora of new funds set up to allow smaller schemes to access private markets in a more cost-efficient and lower governance approach. Many of these funds combine several private markets asset classes into a single fund, allowing Trustees of such schemes to allocate to illiquid investments more conveniently.

What is the correct allocation to private markets?

Each board of trustees will have a different answer to this question. To answer it one needs to consider the time horizon of the scheme, its liquidity requirement, and the potential for this to change over time (such as the potential need for liquidity for transfers out and / or collateral requirements for hedging instruments). These factors can then be assessed against the scheme's particular risk and return objectives to arrive at a suitable allocation for the specific circumstances.

At Cartwright we always consider the objectives and time-horizons of each of our clients individually, helping them assess whether such an allocation would be helpful to achieve their goals and what size

allocation is appropriate given the scheme's liquidity needs. Please reach out to your Cartwright investment consultant or to one of the contacts below to explore whether this opportunity is right for you.

If you would like to discuss any of these matters further, please get in touch with your usual contact at Cartwright.

250 Fowler Avenue
Farnborough Business Park
Farnborough GU14 7JP

Marlborough House
Victoria Road South
Chelmsford CM1 1LN

T: 01252 894883
E: enquiries@cartwright.co.uk
W: pensiontrusts.cartwright.co.uk

Cartwright Pension Trusts is a trading style of Cartwright Benefit Consultants Limited. Registered in England & Wales. Registration No: 08283366
Registered Office: 250 Fowler Avenue, Farnborough Business Park, Farnborough, Hampshire GU14 7JP
Investment Services are provided by Cartwright Financial Solutions Limited and is authorised and regulated by the Financial Conduct Authority: Registration No. 607200