KEYNOTE INTERVIEW

A patient approach to private wealth

Easier access points, better education and a good dose of patience are what is required to unlock the potential of the private wealth channel, says iCapital's managing director Kunal Shah

Q How has private wealth appetite for private markets evolved and what do you see as the key drivers?

One of the primary reasons why we are seeing increased demand for private markets asset classes from the private wealth channel is that the traditional asset allocation model that most individual investors have historically adopted is simply not working. The 60/40 split between stocks and bonds that has traditionally been advised is consistently underperforming more diversified asset allocation frameworks that include alternatives as a key component. Private wealth investors are now recognizing this and demanding an upgrade.

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As we saw in 2022, stocks and bonds are increasingly correlated. The expectation, in the past, was that the two would behave differently through the cycle, but that is no longer proving to be the case.

Companies are now staying private for longer. More money is flowing into private markets which means private markets are able to keep companies in their ecosystem, beyond a point at which they may previously have chosen to go public. Private wealth advisers are waking up to the reality that their clients will miss out on the chance to invest in many of the highest quality and fastest growing businesses, if they focus exclusively on public markets.

Q Why have private wealth investors and their advisers historically struggled to gain exposure to private markets and how have new fund structures and technologies helped to remove some of those obstacles?

One of the principal barriers to entry

for private wealth investors has historically been access. Even the wealthiest of individuals would struggle to meet the minimum investment threshold for institutional investors in traditional private equity funds. But new structures and new technologies have helped provide easier access points. Tender offer funds, interval funds and '40 Act funds, for example, have helped private wealth advisers make the transition to alternatives because they are now able to access these asset classes in a way that is much closer to traditional mutual fund structures.

The other important component to all of this is education. Private wealth investors and their advisers will often need support with incorporating alternatives into their portfolios. Institutional investors have in-house staff or use consultants working for them, helping to think through their strategic priorities, but there is an education gap in the private wealth channel and addressing that must continue to be a real area of focus.

Private wealth investors are typically also unfamiliar with the mechanics of how the asset class operates. They are often unacquainted with the capital call model, performance metrics, benchmarking, etc, presenting an opportunity for platforms like iCapital's to educate and streamline the process.

Q What do you consider to be the number one priority when it comes to unlocking the potential of the private wealth market?

I cannot overemphasize the importance of education. The education gap that exists is huge. Most people in the private wealth world don't know what an IRR is, for example. We need to find new ways to explain the way these asset classes work and the metrics that are employed for benchmarking. We are providing a lot of these resources through our educational program called Alts Edge as well as by writing shorter educational pieces, hosting events, etc.

I would just reiterate, that there is no short cut to unlocking the potential of the private wealth market. This is not something that can be rushed. A pension plan or insurance provider is likely to be able to make a decision much faster than a private wealth adviser. It would be wise to factor the extra decision-making time the wealth channel would need into the fundraising process. A patient approach combined with education is what is needed to really make the most out of the burgeoning private wealth channel.

Q What role are secondaries funds playing in private wealth investors' approach to private markets?

Secondaries strategies are proving particularly popular, and this is an area where we are seeing steady adoption. The advantage of secondaries, of course, is that it allows investors to put money to work quickly and in a diversified manner, whilst minimizing the J-curve. Advisers value faster deployment and return of capital as well as the broad market diversification secondaries provide. Similar to institutional investors who considered secondaries as a core allocation in the early days of the PE bucket (and many still do), many wealth advisers are using secondaries as a valuable component of their private portfolios.

There are two ways in which investors can gain secondaries exposure. The first is through feeder funds that offer access to traditional drawdown structures and the second is through the interval funds or tender offer fund structures which offer diversified plays with secondaries representing a significant component in the early years of the fund's life.

Q Are private investors primarily focusing their attention on private equity, or are they also looking to gain exposure to other areas of the private markets universe?

Our iCapital Marketplace platform was built to offer wealth advisers a variety of product choices across strategies, structure and geography. Marketplace simplifies access to these diverse opportunities, allowing investors to build a balanced portfolio tailored to their clients' specific needs and goals.

While private equity, particularly growth capital, secondaries and buyouts, remains popular, we also see significant interest in private credit opportunities, including direct lending and distressed debt. Additionally, investors are keen on real assets, such as real estate and infrastructure, which provide essential diversification and potential for stable, long-term returns.

Q How is this influx of private wealth capital impacting asset managers themselves and are there knock-on effects for traditional, institutional investors in their funds?

Almost all of the biggest private markets fund managers, as well as most of the tier below, are now very much aware of the potential that the high-net-worth channel represents for their businesses. Indeed, many of the largest listed firms have publicly stated that private wealth is representing a fast-growing share of their assets under management and that they have aggressive ambitions to pursue this further. After all, private wealth is a channel that remains relatively untapped and under-allocated to alternatives when compared to traditional sources of capital.

Private wealth investors' allocation to private markets probably falls somewhere in the 2 to 5 percent range today, compared to 20 percent-plus when you consider the average allocation of an institutional investor to private equity, private credit and real assets. We are, however, seeing a steady increase in private wealth allocations and the opportunity that this represents for private markets asset managers is enormous.

At the same time, more wealth is constantly being created. New millionaires are being formed every year as a fresh generation of entrepreneurs make their mark. By contrast, you don't see new pension plans popping up all over the place. That is a relatively static market. So, while the institutional and private wealth markets are currently roughly equal in size, one is under-allocated and growing, while the other is plateauing.

Asset managers therefore recognize the importance of devising a strategy for accessing this capital base in order to provide solutions to a new type of investor and to grow their AUM. Private markets firms are wholeheartedly getting behind this trend but it does require a different playbook. A different fundraising approach is necessary for private wealth investors when compared to the institutional market. Information needs to be presented differently.

"Private wealth is a channel that remains relatively untapped and under-allocated"

"Private wealth is representing a fast-growing share of assets under management"

There needs to be a strategy around communications and marketing. More resources may be required. A framework also needs to be created to ensure deal allocations are fair and appropriate. One concern that we frequently hear from private wealth investors is that they fear they are getting leftovers. They want full transparency to be sure they are getting a similar deal to the institutional investors.

Q Is it realistic for smaller managers to access private wealth capital or is it mainly for the largest firms?

With a platform like ours, it is possible to gain exposure to a wide selection of managers. Obviously, the largest funds are there, but there are also mid-market names and more esoteric strategies. Our goal is to create a robust and diversified menu of options because investors all have different objectives.

Q How significant a role do you see private wealth playing in the future of private markets?

There is no doubt that private markets asset managers are paying close attention to this trend. There is no shortage of people across the private markets spectrum getting smart and creating solutions for private wealth advisers and their clients.

Meanwhile, from the point of view of the private wealth investors themselves, we are seeing clear signals that they are looking to increase allocations to 5, 10 and even 20 percent of their overall portfolios. In the past, this would have been extremely challenging. They would have needed to negotiate reduced minimum investment thresholds on a case-by-case basis, for example. The good news is that they no longer have to rely on exceptions being made because those exceptions have already been built into platforms like ours. These investors have the right products – the right entry points – available to them.

I would add, however, that this isn't something that is going to happen overnight. Managers need to take a long-term approach to their private wealth strategy. This is something that is going to take a decade-plus, rather than one or two years. It will require patience. We need to hold the hands of these private wealth investors and advisers in order to get them over the finishing line. ■