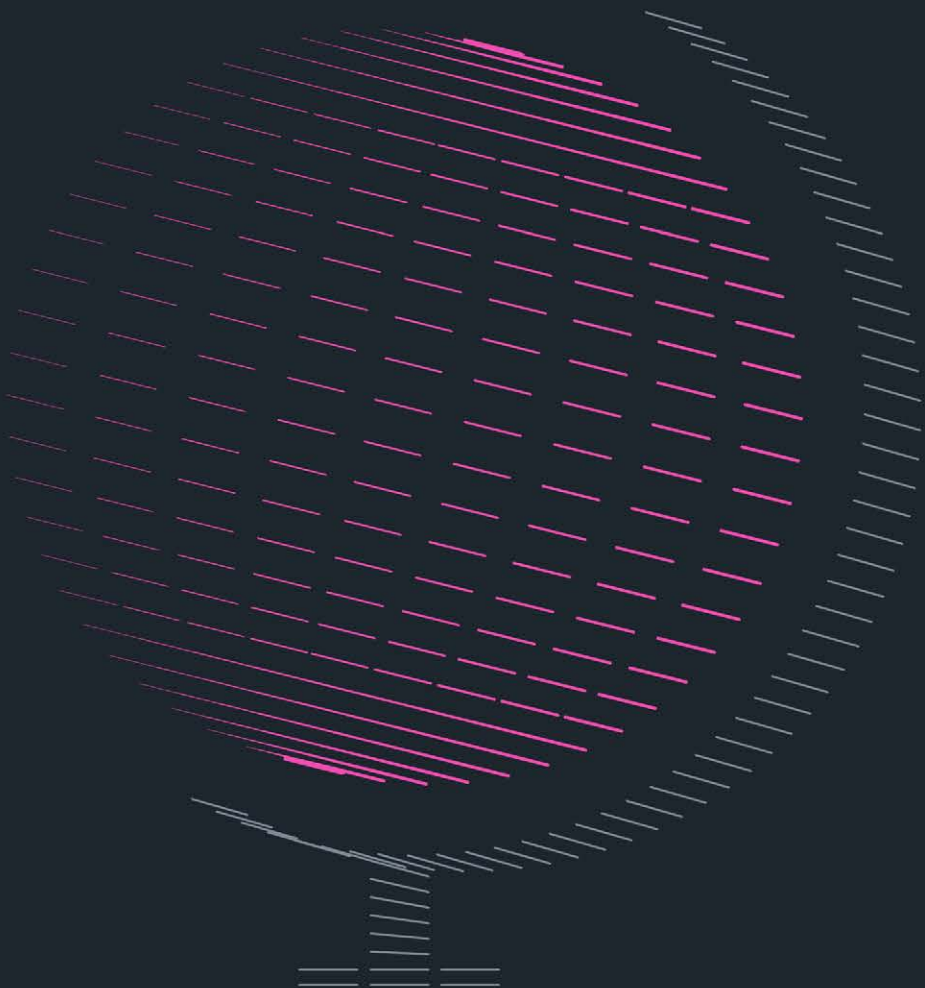
carne

Atlas 2024 report

Exploring private markets
A new world of possibilities

The challenges and opportunities of
201 global private market fund managers
and European asset allocators.



Unity through simplicity™

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Introduction

Private markets - private equity, private debt, infrastructure, venture capital, and real estate - have experienced multibillion-dollar inflows in recent years. With increased opportunity and competition comes pressure on asset managers to deliver products speedily to market while adhering to stringent regulatory demands. This is leading to an increase in fund managers turning to third-party specialists who can support them in navigating and complying with the regulatory regime, enabling them to focus on the core of what they do – driving returns and positive outcomes for clients.

In 2005, total assets under management in global private markets were around $1.6 trillion[1], and by June 2023, this has grown more than eight-fold to reach $13.01 trillion[1], driven by a range of "mega forces" and regulatory changes which indicate further rapid expansion.

The climate transition is forcing an overhaul of the world's infrastructure encompassing travel, energy and technology. Meanwhile, a more varied and competitive financial system and the end of zero-rate borrowing is shifting the private debt landscape.

Digital disruption and the proliferation of AI are giving rise to new markets and opportunities for private equity investment. Finally, geopolitical tensions, ageing populations, remote working and climate change are all creating new demands on the real estate market.

At the same time, the regulatory environment is constantly evolving, making it easier for institutional and retail investors to invest in capital markets.

The US Inflation Reduction Act (IRA) generated more than $110 billion in new clean-energy manufacturing investments in its first year alone[2]. While the EU has improved its European Long-Term Investment Fund (ELTIF) framework to make it easier for retail investors to put capital to work in private markets.

Not to be outdone, the UK launched Long-Term Asset Funds (LTAFs) in 2023 to provide a UK- authorised open- ended fund structure that enables investment in long- term, illiquid assets while offering appropriate structural safeguards.

Given this increasingly positive environment for private markets, we commissioned research with US and UK private market fund managers, and defined contribution (DC) pension schemes and wealth managers across Europe to capture their views on the outlook for this sector, and how they see allocations to it changing over the next few years.

The study looks at the outlook for the different private markets - the challenges facing fund managers in raising capital and their plans for addressing these, to how wealth managers and DC pension schemes intend to invest in these markets.

1. https://www.mckinsey.com/industries/private-capital/our-insights/mckinseys-private-markets-annual-review
2. https://www.whitehouse.gov/briefing-room/statements-releases/2023/08/17/what-they-are-saying-one-year-anniversary-of-the-inflation-reduction-act/

Executive summary

- Research with 201 investors (US and UK private market fund managers, UK and European wealth managers and DC pension schemes) representing $1.93 trillion in combined assets under management (AUM), reveals continued strong growth in private markets. They estimate that the total value of global private market assets will reach $21.08 trillion by 2030 – an $8 trillion (or 62%) increase on todays market which the latest industry data estimates to be $13.01 trillion.
- European DC schemes expect their sector's level of investment into private markets to increase by on average 10% over the next three years. Wealth managers anticipate private market investments to account for around 11% of their sector's AUM by 2030, up from 5% in 2021.

201
global institutional investors

$1.93
trillion combined assets

$21.08
assets by 2030

$8
trillion increase

- When considering the reasons for increasing allocations to private markets, the potential to offer greater risk-adjusted returns is a key factor. Sustainability is another key driver, with 98% of DC schemes and 96% of wealth managers agreeing that private markets enable investors to make more of an ESG impact than investing in public markets.
- Respondents also recognised the importance of innovative fund structures for enabling growth in alternative asset classes. Nearly nine in ten wealth managers (88%) expect the level of investment into private markets by wealth managers in the UK and Europe to increase over the next three years because of LTAF/ELTIF opportunities, with 28% expecting that increase to be 'dramatic'. DC schemes responded similarly, with 78% predicting increased use of these structures and 31% a dramatic rise.

88%
already raising capital

12%
plan to do so

- Nearly nine in ten (88%) of the US-based managers surveyed by Carne Group are already raising capital for private market funds in Europe, and half of the remaining 12% have plans to do so.
- Almost all (94%) of the UK managers surveyed are currently participating in European markets, and the remainder intend to do so within the next 12 to 24 months.
- However, there are several hurdles private market fund managers on both sides of the Atlantic need to overcome to fully seize the private markets' opportunity. private market fund managers see corporate governance, regulation and distribution capability as the three biggest challenges to successfully launching funds in Europe
- More than three-quarters (78%) agree that EU regulations around private assets are more complex than their US equivalents, while 68% believe that navigating these regulations will become even harder in the years ahead.
- Turning to solutions for addressing these challenges, the investment managers surveyed expressed a strong inclination towards external support when it comes to launching and raising funds in European markets.
- The majority (87%) expect their use of outsourcing to increase over the next five years, with 48% of UK managers and 24% of US managers citing reducing regulatory risk as a motivation for doing so.
- Other key reasons that managers identified for increasing their use of third-party specialists include achieving greater speed to market (50% UK; 60% US), the ability to launch different product sets (68% UK; 70% US) and improving transparency for reporting (50% UK; 46% US).

78%
agree that EU regulations around private assets are more complex than their US equivalents

68%
believe that navigating these regulations will become even harder in the years ahead

The view of US private market fund managers

US private market fund managers surveyed think the sector will grow from $13.01 trillion in June last year to an average $20.14 trillion by 2030. However, more than a quarter (26%) expect the market to almost double to reach between $22 trillion and $24 trillion, driven by growing investor appetite for attractive risk-adjusted returns and portfolio diversification.

But that growing appetite for private markets has coincided with more difficult capital raising conditions. Rising geopolitical tensions, equity market volatility, high inflation and rising interest rates all limit opportunities and consequently, US managers have been forced to look outside their own country to global private markets.

Nearly nine out of ten (88%) of the US managers surveyed raise capital in Europe. Of the 12% who say they don't, half have plans to do so and are split equally in terms of timeframes for allocation; 17% will raise capital in Europe in 12 to 24 months; and the same number will do so in 24 to 36 months; and the remaining 17% will raise capital in three years or more.

Other key drivers of growth in capital raising in Europe by North American fund managers cited by survey respondents include:

- Portfolio diversification
- Attractiveness of private markets in general
- Attractiveness of North American managers in particular

88%
raise capital in Europe

12%
are split equally in terms of timeframes for allocations

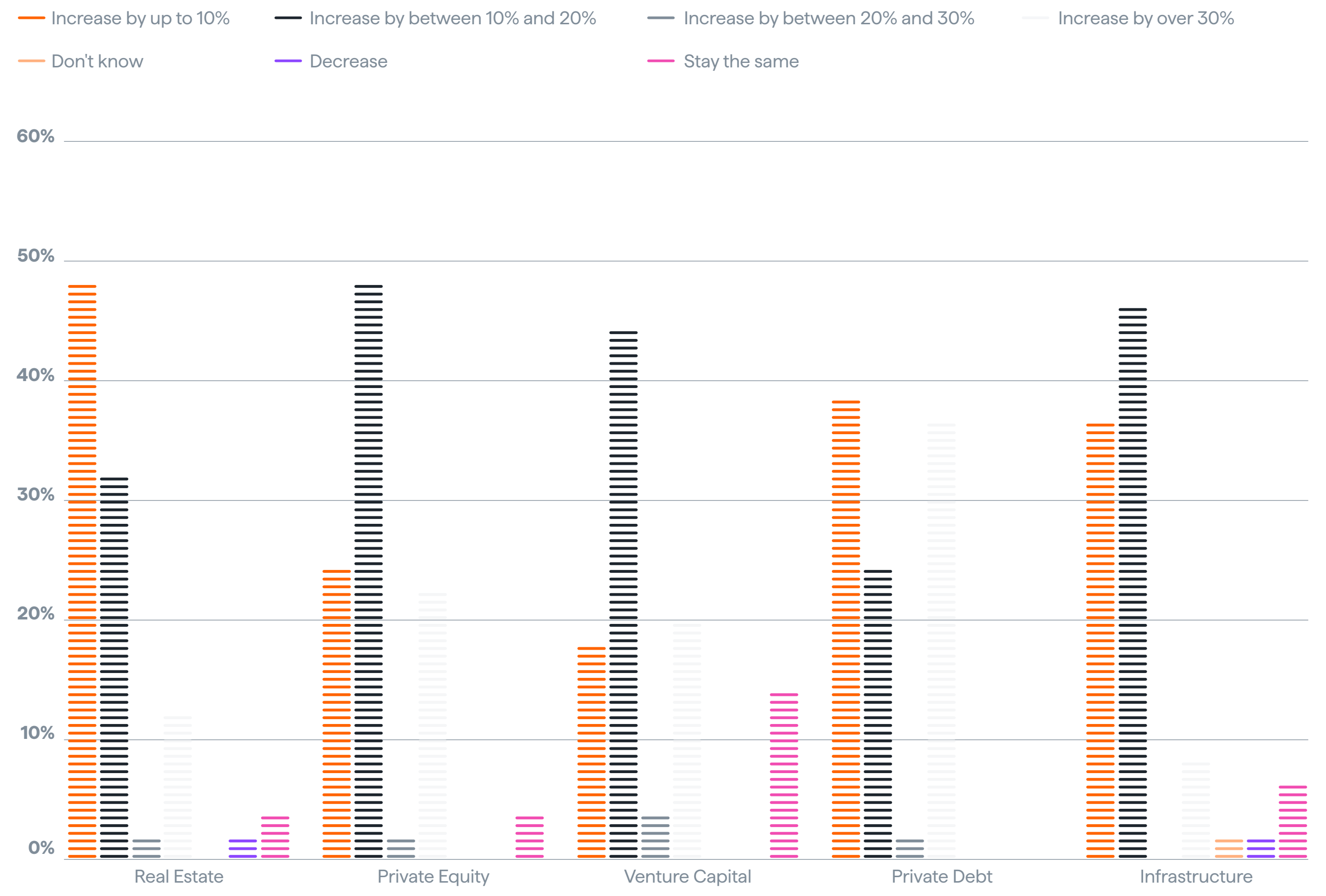
17%
will raise capital in Europe in 12 to 24 months

17%
will raise capital in three years or more

Asset allocation

US managers responding to our survey expect the level of fund raising to increase across all private asset classes over the next two years compared to the previous two years.

Globally, how do you see the level of fund raising by the following private market asset classes changing over the next two years when compared to the previous two years? (US private market fund managers)



How do you see the allocation from the following investor types to the following private markets changing over the next three years? (US private market fund managers)

Pension Funds

	Private Equity	Venture Capital	Real Estate	Infrastructure	Private Debt
Increase by up to 10%	20%	28%	28%	28%	34%
Increase by between 10% and 20%	64%	32%	40%	42%	26%
Increase by between 20% and 30%	14%	36%	22%	18%	32%
Increase by over 30%	2%	2%	2%	8%	4%
Stay the same	0%	2%	8%	4%	2%
Decrease	0%	0%	0%	0%	2%
Don't know	0%	0%	0%	0%	0%

Family Offices

	Private Equity	Venture Capital	Real Estate	Infrastructure	Private Debt
Increase by up to 10%	20%	14%	18%	20%	14%
Increase by between 10% and 20%	16%	38%	46%	38%	44%
Increase by between 20% and 30%	58%	38%	26%	28%	34%
Increase by over 30%	2%	4%	2%	2%	2%
Stay the same	4%	6%	8%	10%	6%
Decrease	0%	0%	0%	2%	0%
Don't know	0%	0%	0%	0%	0%

Insurers

	Private Equity	Venture Capital	Real Estate	Infrastructure	Private Debt
Increase by up to 10%	16%	14%	22%	16%	16%
Increase by between 10% and 20%	50%	42%	40%	38%	40%
Increase by between 20% and 30%	22%	30%	20%	34%	30%
Increase by over 30%	4%	4%	6%	0%	4%
Stay the same	8%	10%	10%	12%	10%
Decrease	0%	0%	2%	0%	0%
Don't know	0%	0%	0%	0%	0%

Wealth Managers / Retail Investors

	Private Equity	Venture Capital	Real Estate	Infrastructure	Private Debt
Increase by up to 10%	12%	20%	14%	20%	18%
Increase by between 10% and 20%	44%	38%	30%	38%	36%
Increase by between 20% and 30%	38%	30%	42%	26%	28%
Increase by over 30%	0%	0%	4%	8%	8%
Stay the same	6%	10%	6%	8%	10%
Decrease	0%	2%	4%	0%	0%
Don't know	0%	0%	0%	0%	0%

Sovereign Wealth Funds

	Private Equity	Venture Capital	Real Estate	Infrastructure	Private Debt
Increase by up to 10%	14%	20%	16%	22%	22%
Increase by between 10% and 20%	48%	46%	28%	44%	36%
Increase by between 20% and 30%	24%	24%	40%	20%	30%
Increase by over 30%	4%	2%	6%	4%	6%
Stay the same	10%	8%	8%	4%	6%
Decrease	0%	0%	0%	4%	0%
Don't know	0%	0%	0%	0%	0%

Working in US managers' favour is the advent of the European Long Term Investment Fund (ELTIF) and the UK's Long Term Asset Fund (LTAF), which are government-led attempts to make it easier for retail investors and defined contribution (DC) pension fund managers to invest in private markets.

US fund managers surveyed say these vehicles will encourage wealth managers and DC schemes to invest in private markets over the next three years. Almost half (48%) of US managers say wealth managers will increase allocations by between 5% and 10%; 44% say between 10% and 15%; and 8% expect an increase of between 15% and 20%.

Looking at DC schemes, 10% of US fund managers say increases will be up to 5%; 8% say schemes will increase allocations by between 5% and 10%, and 78% expect it to be higher than this.

No surprise then that respondents say they are planning on using ELTIFs and LTAFs to target high net worth or retail investors in Europe. Nearly three-quarters (74%) say they will set up a UK-only LTAF and 42% will establish an ELTIF.

Optimum distribution

There are three ways in which North American private asset fund managers can distribute their funds in Europe. First is passporting where managers may base their fund in the EU and employ an EU-authorised AIFM, using the latter's marketing passport to undertake distribution activities across the region.

Secondly, the National Private Placement Regime (NPPR) allows AIFs and managers based outside the EU to market to individual member states separately. But, of course, Europe is not a homogeneous region and requirements around NPPR differ from country to country, with some countries not permitting it at all.

The final option is reverse solicitation which involves a direct approach from an investor to a fund or its manager, thereby requiring no direct marketing. This model is coming under increasing regulatory scrutiny.

We asked US managers how the use of the three approaches will change over the next three years. Passporting is the most likely of the three options to increase, largely because it provides the easiest and broadest market access, when partnering with an AIFM. Sixty percent of respondents say passporting will rise by between 25% and 50%, and 16% believe usage will rise by between 50% and 75%.

60%
say passporting will rise by between 25% and 50%

16%
believe usage will rise by between 50% and 75%

Use of NPPR, which offers limited access in a limited number of markets, and is becoming less prevalent in certain markets, is expected to rise by between 10% and 25% according to 34% of respondents; 32% say between 50% and 75%; and 16% say between 25% and 50%.

Looking at reverse solicitation, 44% say increases will be between 25% and 50%; 26% say between 10% and 25%; while 22% say between 50% and 75%.

Outsourcing support

Given the many challenges facing non-domestic managers when entering the European market, 85% of US manager responding to our survey expect to increase the level of outsourcing of their European business over the next five years, with 28% predicting dramatic rises.

When asked to select the three main reasons why they would outsource:

70%
cited it makes it easier to launch different product sets;

60%
cited it delivers greater speed to market;

46%
cited greater transparency in reporting

Opting for AIFM support is by the far the most popular method for raising capital in Europe with 60% of fund managers choosing this option since this gives them the freedom to domicile their fund in any EU jurisdiction. When asked to select the three most important factors when selecting an AIFM provider:

Four fifths (80%) of US managers named distribution support: As the market for illiquids grows and matures, outsourcing should play a critical role in facilitating effective distribution and speed to market, so that investment managers can capitalise on the significant private market opportunity present across the continent.

Half (50%) cited the ability to provide additional services and 46% cited geographic reach.

Regulatory deterrent

Despite recent efforts from policymakers to make it easier for retail investors to allocate to private markets, when asked to rank the challenges to successful fund raising/fund launches for non-EU private markets fund managers in Europe, the top obstacle identified by the US fund managers interviewed was corporate governance followed by a difficult regulatory environment. As the regulatory issues facing fund managers increase, this has made it even more appealing for them to work with specialist third party-solution providers to help them address these challenges.

More than three-quarters (78%) of US managers responding to our survey say EU regulations around private market assets are more complex than corresponding regulations in the US, with 18% saying they are much more complex.

And respondents were pessimistic about the regulatory landscape going forward. When asked how they see the ability of private market fund managers in navigating regulation around private market assets changing, 26% say it will become much harder and 42% say it will become slightly harder.

At the same time, sustainability legislation in the UK and Europe is also making life harder for US managers.

Three-quarters of respondents say EU and UK ESG regulation is a deterrent for when trying to raise capital in Europe. However, 8% say they are not restrictive and 16% say the rules present opportunities.

To help comply with an ever-expanding regulatory regime, US managers say they will increase budgets in this area over the next two years, with just over two-thirds (68%) expecting to do so by between 25% and 50%.

ESG opportunities

While ESG rules may act as a deterrent to US managers when looking at Europe, the trend to sustainable investing is a significant factor in offering investors access to private markets in the region.

As institutional investors face pressure to demonstrate stronger ESG credentials in their portfolios and while retail investors express greater appetite for using their investments to 'do good', almost all (96%) of respondents agree that private markets enable investors to make more of an ESG impact than investing in public markets.

US managers also agree that private markets can play a hugely positive role in the transition to a lower carbon-intensive economy, with 20% strongly agreeing.

However, managers will need to ensure they are demonstrating genuine commitment to sustainable strategies since respondents expect scrutiny of ESG issues to intensify over the next three years.

Looking at environmental issues, 52% of managers say investor scrutiny will increase dramatically; 38% say it will rise slightly and just 10% say it will stay the same.

52%
say investor scrutiny will increase dramatically

38%
say it will rise slightly

10%
say it will stay the same

The corresponding figures for scrutiny around social issues are 40%, 46% and 14% respectively, and for governance they are 40%, 56% and 4%.

This ESG oversight is already impacting managers' ability to retain business and respondents anticipate the trend will continue. Almost half (46%) say the trend of losing mandates from institutional investors because of poor ESG credentials/a lack of transparency around their ESG credentials will increase dramatically; 36% say it will increase slightly.

Operational improvements

Central to managers demonstrating their ESG credentials is robust data. Our survey reveals that there is room for improvement in the level of reporting from US managers – a view shared by European wealth managers and DC pension schemes as outlined later in this report.

When asked to rate the level of reporting and data from private markets fund managers around the ESG credentials of their investments, only 20% of respondents describe it as excellent; 68% say it is good, while 12% believe it is average.

Similarly, when describing their ability to quantify ESG risk exposures in the investments they make, 38% say it is excellent; 52% believe it is good and 10% say they are average at this.

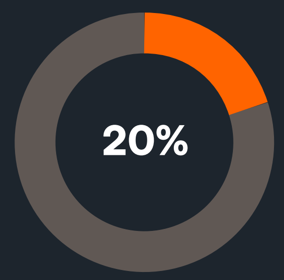
However, improving data management should not be confined to ESG. In an increasingly competitive market, our survey reveals that effective information management and analysis are important differentiators for managers competing for market share.

Just under one-third (32%) of respondents strongly agree and 66% slightly agree that data management and analysis capabilities will become an increasingly important source of competitive advantage in private capital markets. The remaining 2% were unsure.

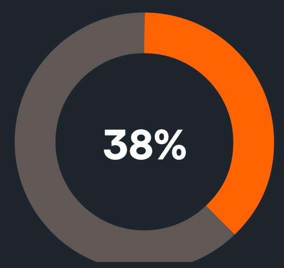
Yet confidence in existing systems could be higher. When asked to describe the data management processes around their firm's work in private markets, just 22% say it is excellent; 70% say it is good and 8% describe it as average.

Further, 92% say the data quality and transparency needs to improve - with 52% saying there needs to be a dramatic improvement.

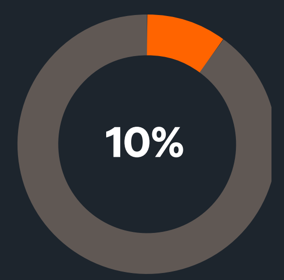
Excellent



Good



Average



Focus on AI

Alongside data and operational improvements, technology is another important competitive differentiator.

The survey reveals notable weaknesses in some US managers' systems, not least of which is an over reliance on manual processes. Two-fifths of respondents say they spend far too much time on manual data management; 44% say a little too much; and just 14% are happy with their reliance on humans rather than technology. Looking at how well their technology is integrated, 84% say it is quite well incorporated and 16% say extremely well.

In an attempt to better streamline processes, US managers are turning to emerging technologies such as AI and machine learning.

All respondents say they will increase investment in AI with 6% saying by up to 25%; 18% by between 25% and 50%; 62% by between 50% and 75%; and 14% by between 75% and 100%.

Among the benefits of moving to AI, 60% say the technology will help with valuations; 44% say with sourcing deals; the same number say it will ease portfolio management; and 42% identify risk management as benefiting from AI.

60%
say technology will help with valuations

44%
say with sourcing deals

44%
say it will ease portfolio management

42%
identify risk management as benefiting from AI

Acknowledging the challenges

The US managers responding to our survey are pragmatic about the challenges for investors when considering private markets.

Almost all (98%) US managers agree that complexity and lack of transparency deter investors from allocating to private markets, with 38% strongly agreeing.

High fees in general are another challenge for US managers with 74% of respondents agreeing they are too high. One-fifth disagreed that fees are too high and 6% were unsure.

Fund managers need to be able to demonstrate the value of their fees in terms of the attractive risk-adjusted returns they deliver, as well as a high level of transparency and reporting. This is particularly important as respondents see fees rising, especially for the most successful managers. Over the next three years 72%, of US managers say fees will increase slightly, and 6% say they will rise dramatically.

The view of UK private capital market fund managers

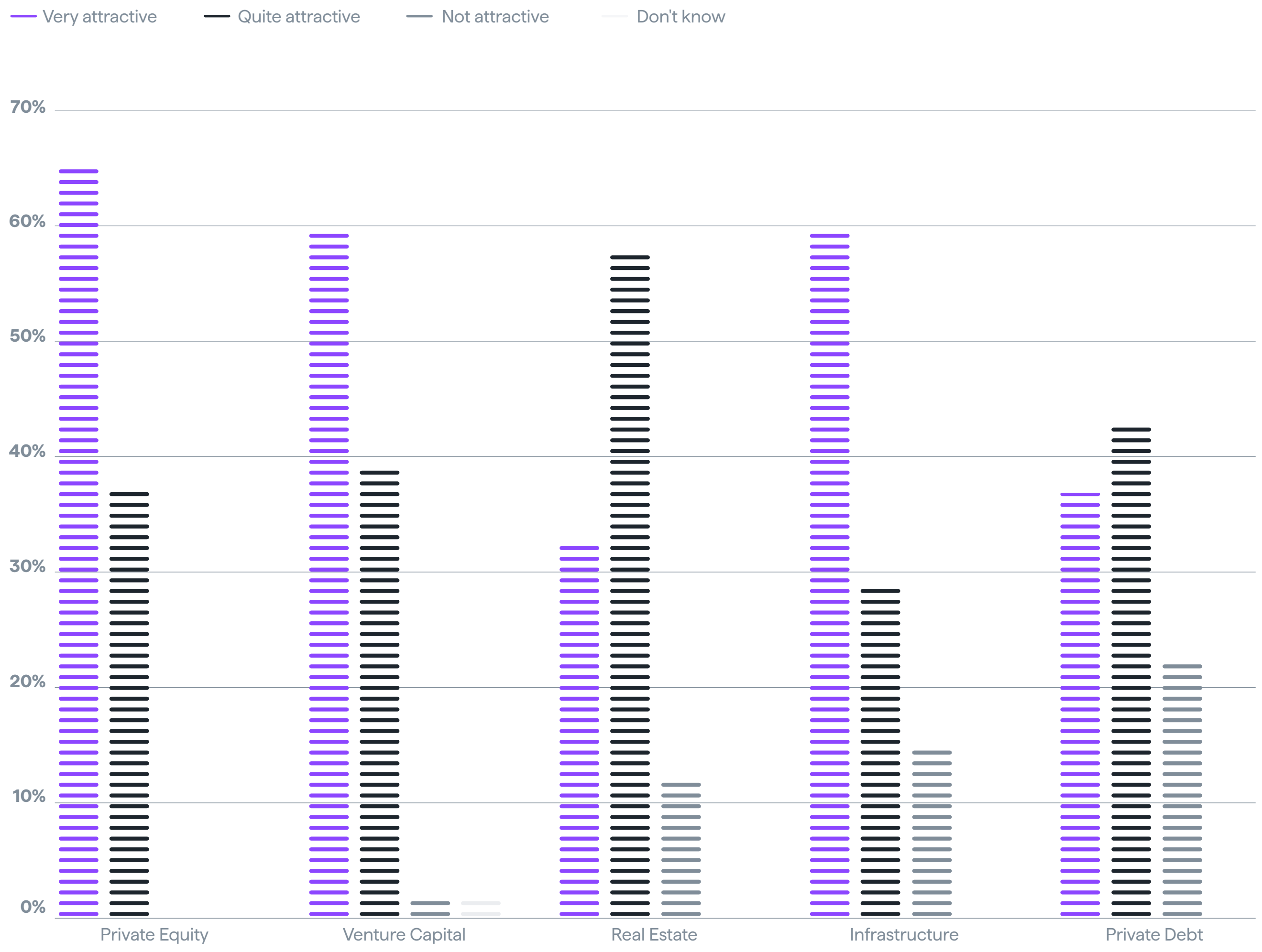
UK private capital fund managers share the optimistic growth views of their US counterparts for the sector.

UK private market fund managers surveyed think the sector will grow from the $13.01 trillion in June last year to on average $22.02 trillion by 2030.

Almost all (94%) UK managers participating in the survey raise capital in European markets and the remaining 6% plan to do so within the next 12 to 24 months.

Attractive risk-adjusted returns across all private markets serve as an obvious draw for investment.

Long-term (over the next five years), how attractive – in terms of risk adjusted returns - do you think investment in the following private markets will be (UK private asset fund managers)



Fund raising trends

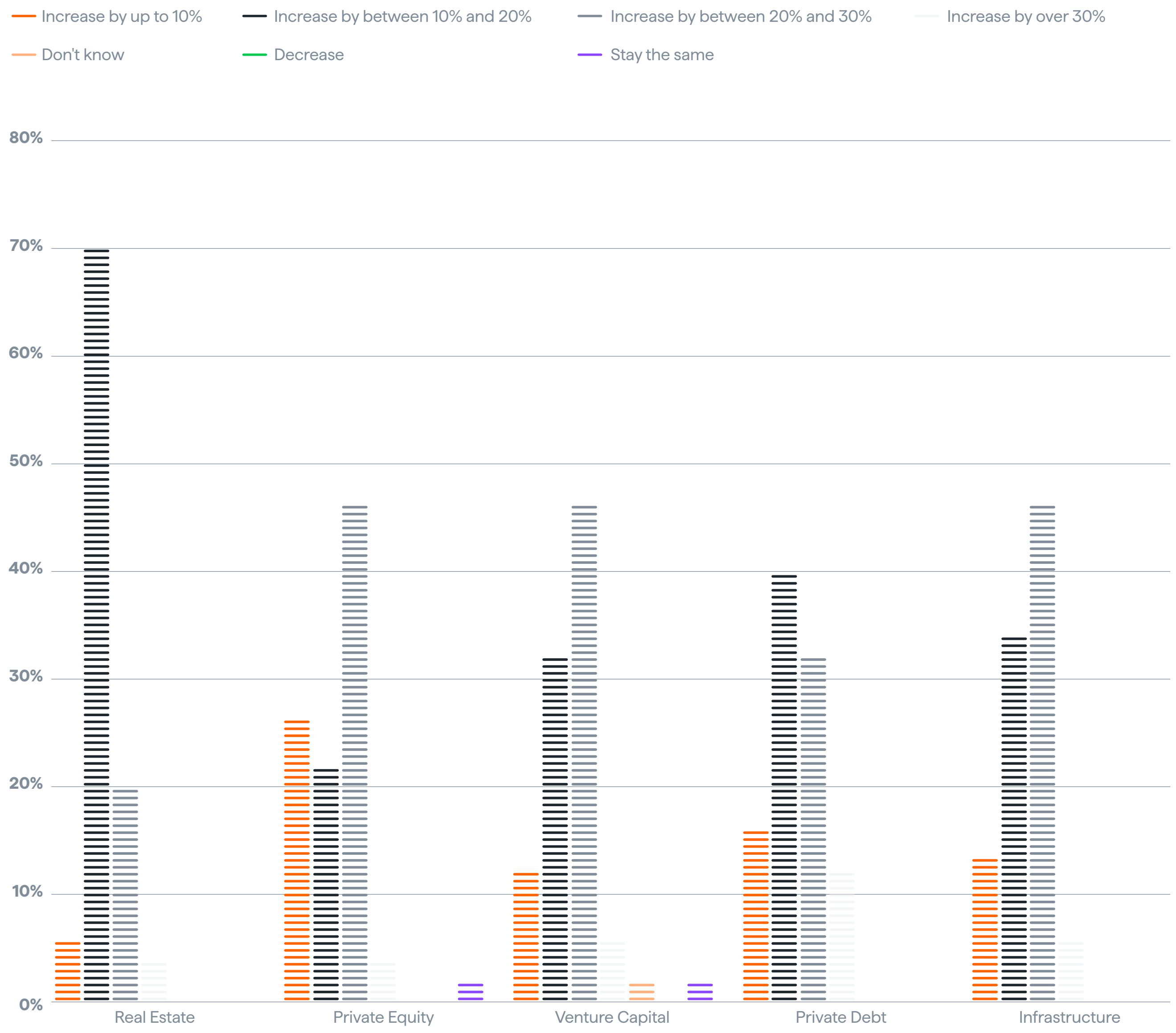
UK asset managers see the level of fund raising increasing across private markets over the next two years compared with the previous two.

Private equity, venture capital and infrastructure are the most likely to see the biggest percentage gains with 46% of managers expecting these to grow up by between 20 to 30%

Almost three-quarters (70%) of those surveyed say real estate fund raising will rise by between 10% and 20%.

Looking at private debt 40% of managers say fund raising will be up by between 10% to 20%, while 12% say it will rise by more than 30%.

Globally, how do you see the level of fund raising by the following private market asset classes changing over the next two years when compared to the previous two years? (UK private asset fund managers)



Allocations by investor type

When asked to consider how fund raising will change over the next three years by investor type, 56% of UK managers surveyed see pension funds increasing their allocation to private debt by 10% or more for example, and 24% expect an increase of at least 20%.

For pension funds investing in infrastructure, the corresponding figures are 62% and 22%, and for private equity, venture capital and real estate they are 74% and 12%; 76% and 20% and 60% and 20% respectively.

In the UK, how do you see the allocation from the following investor types to the following private markets changing over the next three years? (UK private asset fund managers)

Pension Funds

	Private Equity	Venture Capital	Real Estate	Infrastructure	Private Debt
Increase by up to 10%	26%	22%	38%	32%	40%
Increase by between 10% and 20%	62%	56%	40%	40%	32%
Increase by between 20% and 30%	12%	18%	18%	18%	18%
Increase by over 30%	0%	2%	2%	4%	6%
Stay the same	0%	2%	2%	6%	2%
Decrease	0%	0%	0%	0%	2%
Don't know	0%	0%	0%	0%	0%

Family Offices

	Private Equity	Venture Capital	Real Estate	Infrastructure	Private Debt
Increase by up to 10%	38%	24%	16%	28%	12%
Increase by between 10% and 20%	32%	46%	50%	36%	56%
Increase by between 20% and 30%	28%	22%	30%	28%	22%
Increase by over 30%	2%	2%	2%	2%	4%
Stay the same	0%	6%	2%	6%	6%
Decrease	0%	0%	0%	0%	0%
Don't know	0%	0%	0%	0%	0%

Insurers

	Private Equity	Venture Capital	Real Estate	Infrastructure	Private Debt
Increase by up to 10%	20%	22%	26%	18%	18%
Increase by between 10% and 20%	42%	42%	46%	52%	52%
Increase by between 20% and 30%	30%	28%	22%	22%	22%
Increase by over 30%	2%	8%	2%	4%	4%
Stay the same	6%	0%	4%	4%	4%
Decrease	0%	0%	0%	0%	0%
Don't know	0%	0%	0%	0%	0%

Wealth Managers / Retail Investors

	Private Equity	Venture Capital	Real Estate	Infrastructure	Private Debt
Increase by up to 10%	20%	24%	26%	28%	18%
Increase by between 10% and 20%	62%	28%	34%	44%	52%
Increase by between 20% and 30%	14%	40%	30%	12%	14%
Increase by over 30%	0%	0%	8%	4%	4%
Stay the same	2%	6%	2%	10%	10%
Decrease	2%	2%	0%	2%	2%
Don't know	0%	0%	0%	0%	0%

Sovereign Wealth Funds

	Private Equity	Venture Capital	Real Estate	Infrastructure	Private Debt
Increase by up to 10%	28%	30%	24%	10%	22%
Increase by between 10% and 20%	40%	40%	40%	40%	36%
Increase by between 20% and 30%	20%	16%	26%	30%	26%
Increase by over 30%	4%	8%	0%	0%	4%
Stay the same	8%	6%	8%	18%	10%
Decrease	0%	0%	2%	2%	2%
Don't know	0%	0%	0%	0%	0%

Like their US counterparts, UK managers are optimistic about the positive impact of the LTAF regime in the UK and the revamped ELITF 2.0 framework in Europe.

When asked how they see the level of investment in private markets changing over the next three years as a result of the regimes, 4% of respondents say wealth managers in the UK and Europe will increase allocations by up to 5%; 44% say by between 5% and 10%, and 52% expect it to be more than this.

Looking at DC schemes, 8% of respondents say investors will increase allocations by up to 5%; 10% say by between 5% and 10%; and 80% anticipate it will be more than this.

Entry to market

UK fund managers responding to our survey prefer fund raising through a placement agent, with more than three-quarters (76%) choosing this option. Some 14% per cent of respondents favour using a direct sales team; 8% use a private bank, while 2% opt for a third-party distributor.

When asked to select the three most important factors when choosing an AIFM provider, almost two-thirds (62%) of respondents cite distribution support, more than half (58%) chose demonstrable product knowledge, while half of managers included the ability to offer speed to market in their top three. Almost half (48%) of managers cited reputation, and the same number said an AIFM's ability to provide additional services. Geographic reach was selected in the top three by 32% of UK managers surveyed.

The role of AIFMs then can be important in overcoming the biggest obstacles facing UK private markets fund managers.

When asked to rate the biggest challenges they face, difficulty in distributing cross-border was placed first, regulation ranked second; recruitment challenges were third; fourth was the lack of familiarity with the European market and available fund structures; fifth was the complexity of choosing the right jurisdiction; and managing business in unfamiliar jurisdictions ranked sixth.

The need for support with asset management in private markets explains the high number of UK respondents who say that outsourcing will continue over the next five years. One in 10 respondents say it will increase dramatically, while 80% say it will increase slightly.

When asked to select the three main reasons why respondents think UK private markets fund managers are increasingly outsourcing the management of their business, more than two-thirds (68%) cited that it makes it easier to launch different product sets; half of the respondents selected it provides greater transparency in reporting and 48% included outsourcing reduces regulatory risk.

Further, 44% included outsourcing helps with getting products to market more quickly in their selection; two-fifths selected that it helps with distribution support; more than a quarter (26%) chose that it helps reduce costs and one-fifth included that third-parties have the ability to deliver stronger fiduciary management of the fund in their top three reasons.

Sustainable incentives

Private market investment is seen as central to funding the green transition and in scaling up a plethora of public services, and all UK managers agree that these asset classes enable investors to make more of an ESG impact than investing in public markets.

Further, 26% strongly agree and 74% slightly agree that private markets can play a hugely positive role in the transition to a lower carbon-intensive economy.

As such investors will be paying more attention than ever to the ESG credentials of their private market investments.

When asked how they expect levels of scrutiny to change across the E, the S and the G, 48% of respondents expect the focus on environmental aspects to dramatically increase: 14% expect a slight increase and 38% don't expect any change.

The corresponding figures for social issues are 50%, 12% and 24% respectively.

For governance issues, two-fifths say there will be a dramatic increase in scrutiny; the same number expect a slight increase, while the remaining fifth say the level of scrutiny will stay the same.

This increasing scrutiny will put pressure on managers to retain business, according to respondents.

When asked how they see the issue of private markets fund managers losing mandates from institutional investors because of poor ESG credentials or a lack of transparency developing, 36% expect a dramatic increase; 62% expect a slight increase; and just 2% say it will be less of an issue.

To avoid such business losses, managers will need to be better able to quantify ESG risk exposures in the private markets investments they make. While one-fifth of UK managers say their ability to do this is excellent; 78% describe it as good and 2% describe it as average.

Managing regulation

Given that UK managers see regulatory obstacles as the second biggest challenge they face, it is no surprise that all respondents describe the rules governing UK private markets as complex. Half say they are quite complex, while the remaining half say they are very complex.

Furthermore, respondents also say regulation is the biggest challenge for successful fund raising, followed by corporate governance concerns.

And the regulatory landscape is only set to become more challenging according to survey participants. One in 10 say it will be much harder to navigate regulations around private markets; while more than half (58%) say it will become slightly harder. However, 30% say the regulatory landscape will become easier to navigate, while 2% believe it won't change.

58% slightly harder

30% easier to navigate

2% believe it won't change

No wonder then that respondents are increasing their budgets and resources dedicated to managing regulatory compliance, with the vast majority (68%) spending between 25% and 50% more over the next two years.

Of the remaining respondents, 4% say increases will be up to 10%; more than a quarter (26%) by between 10% and 25%; while 2% anticipate spending between 50% and 75% more.

Poor data management

In common with the US private markets managers, UK respondents say they need to improve their data management.

Just 14% of respondents describe the data management processes around their fund management firm's work in private markets as excellent, although four-fifths say it is good. The remaining 6% describe it as average.

14% strongly agree

6% average

All UK managers surveyed say they spend too much time in data management, and of those 54% say they spend far too much time.

Fund managers will need to overcome data management issues and improve transparency if they are to attract more investors.

More than a third (36%) of UK managers surveyed strongly agree that data management and analysis capabilities will become an increasingly important source of competitive advantage in private capital markets, while 62% slightly agree with this view.

However, 12% of respondents describe the level of transparency around investing in private markets as poor or average. Seventy percent say transparency is good.

Improving data management will be central to overcoming obstacles to investment in private markets since almost all (96%) UK managers agree that complexity and a lack of transparency around private markets is deterring wealth managers, DC pension schemes and individual retail investors from investing in private markets.

Improving technology

When asked about the integration of technology systems, only 16% say they are extremely well integrated; 82% say they are quite well integrated but 2% concede they are very poorly integrated, suggesting more room for improvement.

Alongside getting to grips with existing technology, UK asset managers recognise the need to incorporate AI into their processes. Not only will this reduce the need to rely on manual processing, but managers say the technology can assist across their operations.

AI budgets will increase for all UK respondents in the next two years. Four percent say they will increase by up to 25% at their firm; 48% say increases will be by between 25% and 50%; 46% say increases of between 50% and 75%; and 2% say there will be an increase of between 75% and 100%.

Almost two-thirds of respondents say AI helps with valuations; more than half (54%) say AI creates value; half say the technology helps with sourcing deals; 34% say AI improves risk management and the same number say it helps with fund raising. AI is also seen as beneficial for 24% of respondents in portfolio management and one in 10 use it for exit planning.

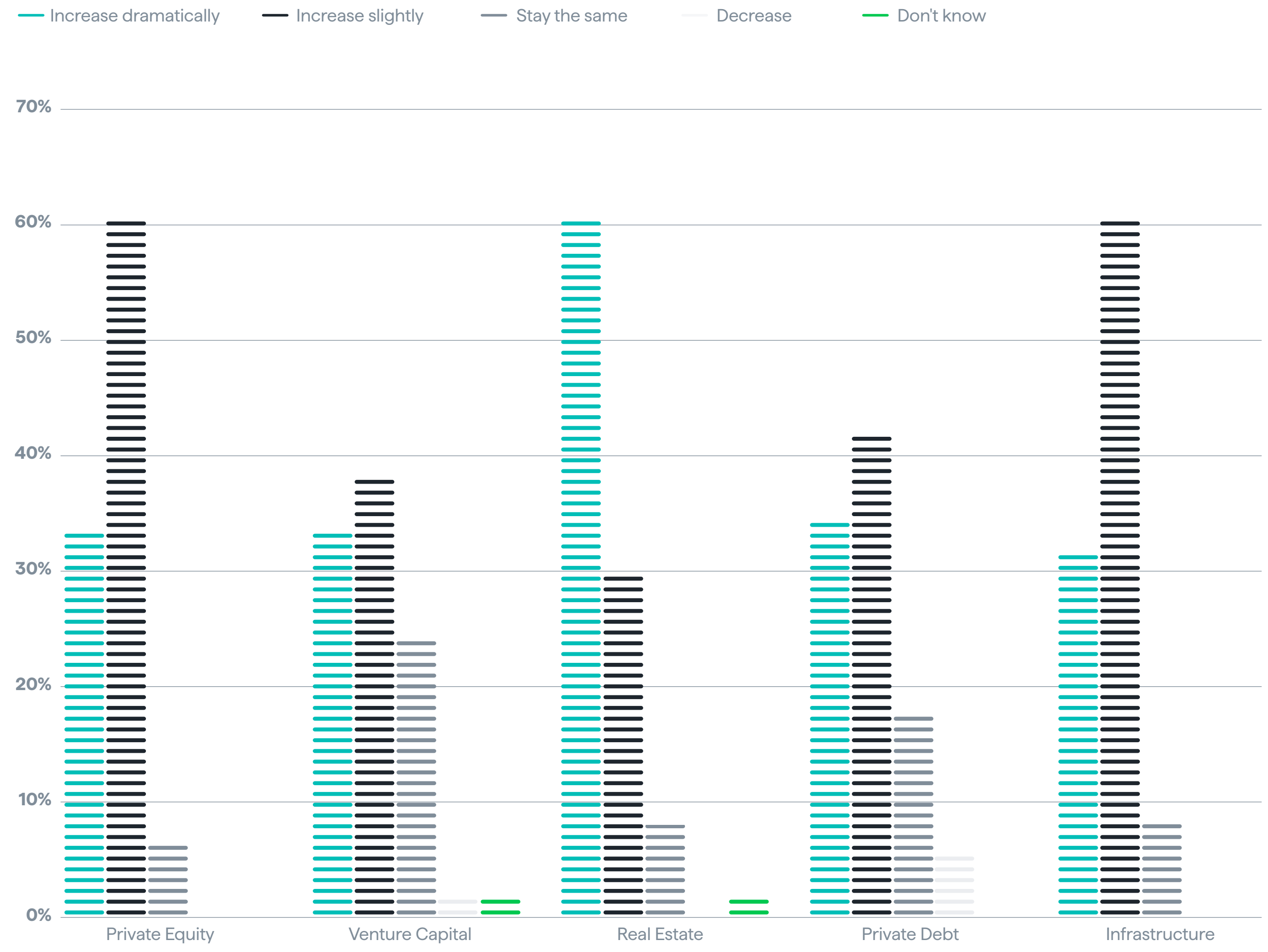
Wealth managers focusing more on private markets

Private markets are not new to wealth managers, but they are becoming more pivotal to client portfolios.

More than two-thirds (68%) of UK and European wealth managers responding to our survey invest between 10% and 15% of their assets in private markets, while 12% say they invest between 15% and 20%. Meanwhile, 6% of respondents say they allocate less than 5% of client portfolios to private markets while 14% invest between 5% and 10%.

Looking to the more immediate future, in three years' time 48% of wealth managers surveyed expect allocations to private markets to be between 15% and 20%, while 12% say they will invest between 20% and 30% of their clients' assets in these asset classes. More than one in ten (12%) say clients' investment in private markets will be between 5% and 10%; while more than a quarter (28%) say between 10% and 15%.

In the next three years, how do you see the focus of the wealth management firm you work in terms of offering clients opportunities in the following private markets? (UK and European wealth managers)



Push and pull factors

Retail investors have historically not invested in illiquid markets either because there were too few entry points, or they were unwilling to veer from the tried and tested public markets.

However, 88% of wealth managers say their clients are increasingly interested in illiquid markets.

There are several factors driving investor appetite interest in private market asset classes which respondents ranked in order of importance.

1 Improve the sustainability record of DC plans

2 Improve diversification

3 Support impact investment strategy of DC trusts

4 Improve marketability and attractiveness of DC trusts

5 Improved risk-adjusted returns

6 Provide income

However, that same illiquidity is seen as the number one barrier to entry preventing retail investors' entry to private markets, suggesting that more innovation is needed to make these asset classes palatable to those with shorter time horizons.

Other barriers to entry identified by the survey in order of importance were a lack of capability on the DC scheme's platform; a lack of products available on the market; high fees; lack of reporting and transparency around private markets; limited in-house experience on private markets; and inadequate in-house governance budget to oversee allocations to private markets.

While high fees ranked third on the barriers to the entry list, four-fifths (80%) of wealth managers say charges are too high for private maker's investment ; 16% disagree and 4% are unsure.

As we have seen elsewhere in the survey, fees are expected to rise according to 80% of wealth managers. Eighteen percent say they will stay the same.

New vehicles – ELTIF and LTAF will see wealth managers increase their allocation to private markets

UK and EU regulators are taking steps to alleviate some of the pressures facing retail investors when it comes to allocating to private markets. The recent LTAF regime in the UK and the reworked ELTIF framework in Europe are aimed squarely at the retail sector.

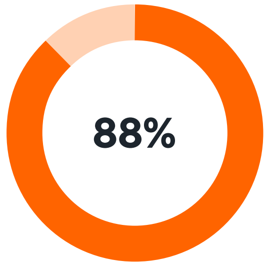
Nearly nine out of 10 (88%) wealth managers expect the level of investment into private markets by wealth managers in the UK and Europe to increase over the next three years because of the ELTIF and LTAF opportunities, with 28% expecting dramatic increases.

At present 24% of respondents say they use an ELTIF or LTAF to allocate to private markets. Meanwhile, 80% co-invest with a private markets fund manager; 44% use a private markets fund; and 38% invest directly.

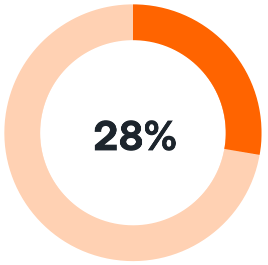
Tokenization is another innovation that will help drive retail investment towards private markets, according to wealth manager respondents. All wealth managers agree that developing liquid digital tokens would make private markets more suitable for retail investors, with one in 10 (10%) strongly agreeing.

All respondents say tokenization will become mainstream within the decade, with 18% predicting seven years; almost half (46%) say eight years; and 36% forecast nine years.

Increase



Increase dramatically



Losing clients

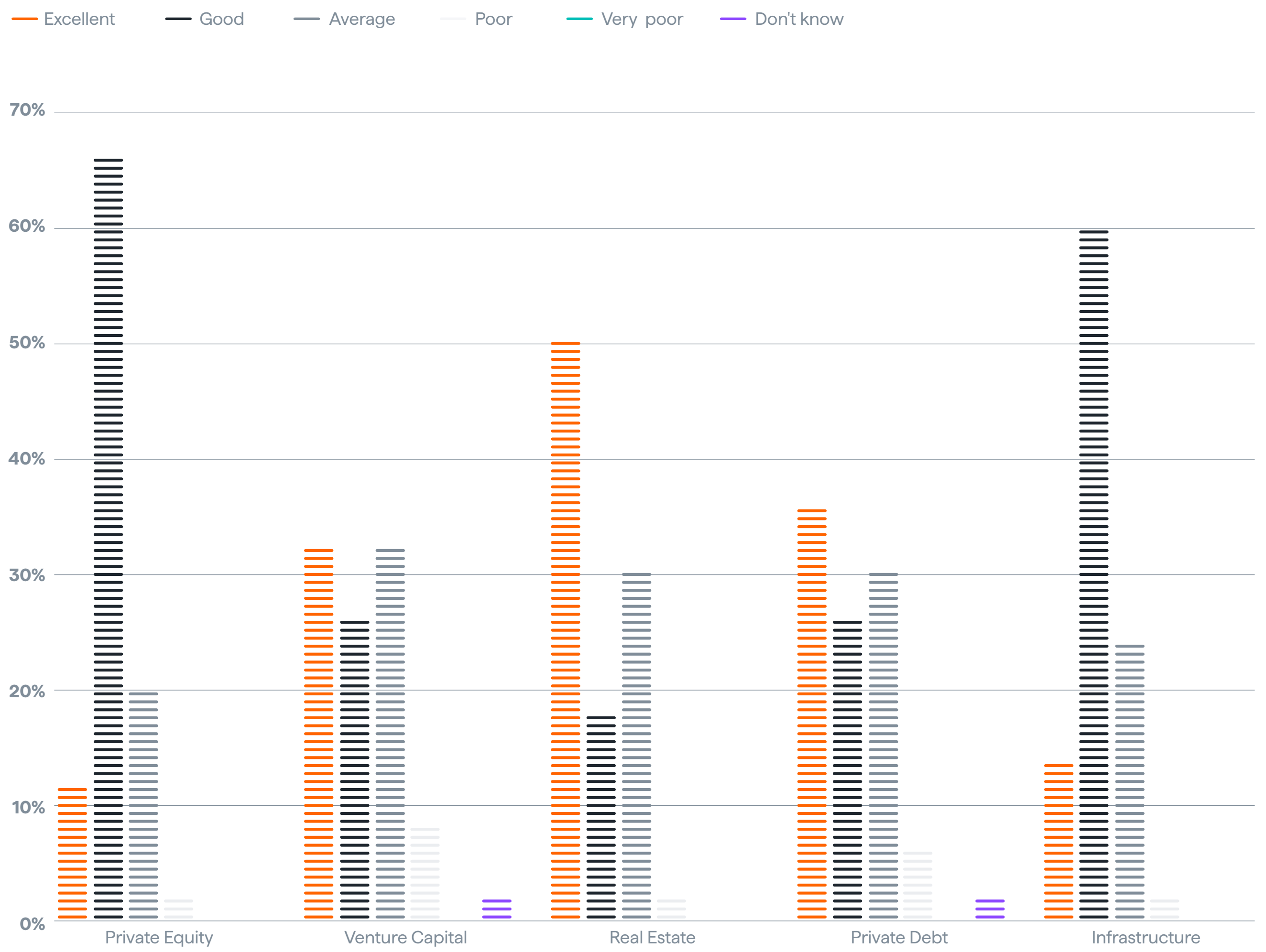
If wealth managers want to capitalise on retail investors' appetite for private markets, they are going to need to ensure they are adequately connected to - and well versed in - these asset classes.

More than three-quarters (78%) of wealth managers say they have lost clients because they could not offer them adequate access to private markets. Third-party solution providers can help wealth managers avoid this by supporting them in the development of products and platforms that enable them to offer their clients access to private markets.

More than four-fifths (82%) say this trend will continue in the future.

The survey also identifies notable gaps in private markets in wealth management firms.

How would you describe the level of expertise in your wealth management firm around the following private markets? (UK and European wealth managers)



Responsible investment

Support for ESG investment strategies is a big benefit of investing in private markets, but the survey reveals more transparency is needed.

Nearly all (96%) wealth managers surveyed agree that private markets enable investors to make more of an ESG impact than investing in public markets, with 26% strongly agreeing.

In line with a greater appetite for responsible investment, wealth managers expect the level of ESG scrutiny by investors in private markets to increase over the next three years.

44% say investor scrutiny will increase dramatically

44% say it will rise slightly

12% say it will stay the same

For environmental issues, 44% of respondents say scrutiny will increase dramatically; the same number say it will rise slightly; and 12% believe it will stay the same.

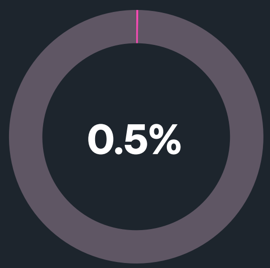
The corresponding figures for scrutiny of social issues are 56%, 28% and 14%.

However, that scrutiny will come at a price for those wealth managers who fail to offer a decent standard of ESG reporting and data management. Just 12% of wealth managers describe their capabilities here as excellent, 78% describe them as good and 10% c oncede they are average.

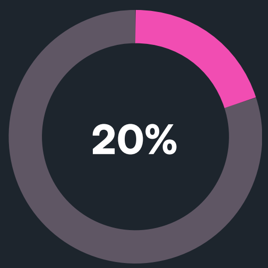
DC pension schemes to become a major driver of growth of capital markets

Private market assets are severely underrepresented in the portfolios of UK-defined contribution (DC) pension investors compared to their global peers. UK DC schemes invest just 0.5% while in Australia allocations are 20%, in the Netherlands 7%, and in Spain and Denmark 5%[3].

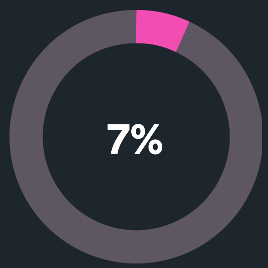
UK



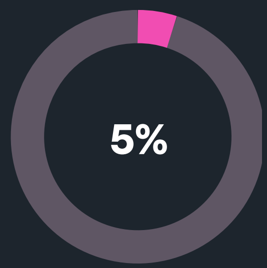
Australia



Netherlands



Spain and Denmark



The UK government is making concerted efforts to encourage more DC investment in private markets through a series of reforms announced in July 2023 including an industry-led campaign committing many of the UK's largest pension providers to the objective of allocating at least 5% of their default funds to unlisted equities by 2030[4].

These reforms will join existing initiatives that our research reveals are already driving DC assets to invest in private markets.

3. https://www.wtwco.com/en-gb/insights/2024/01/nine-new-years-predictions-for-uk-pension-schemes-in-2024
4. https://www.gov.uk/government/collections/mansion-house-2023

Increasing allocations

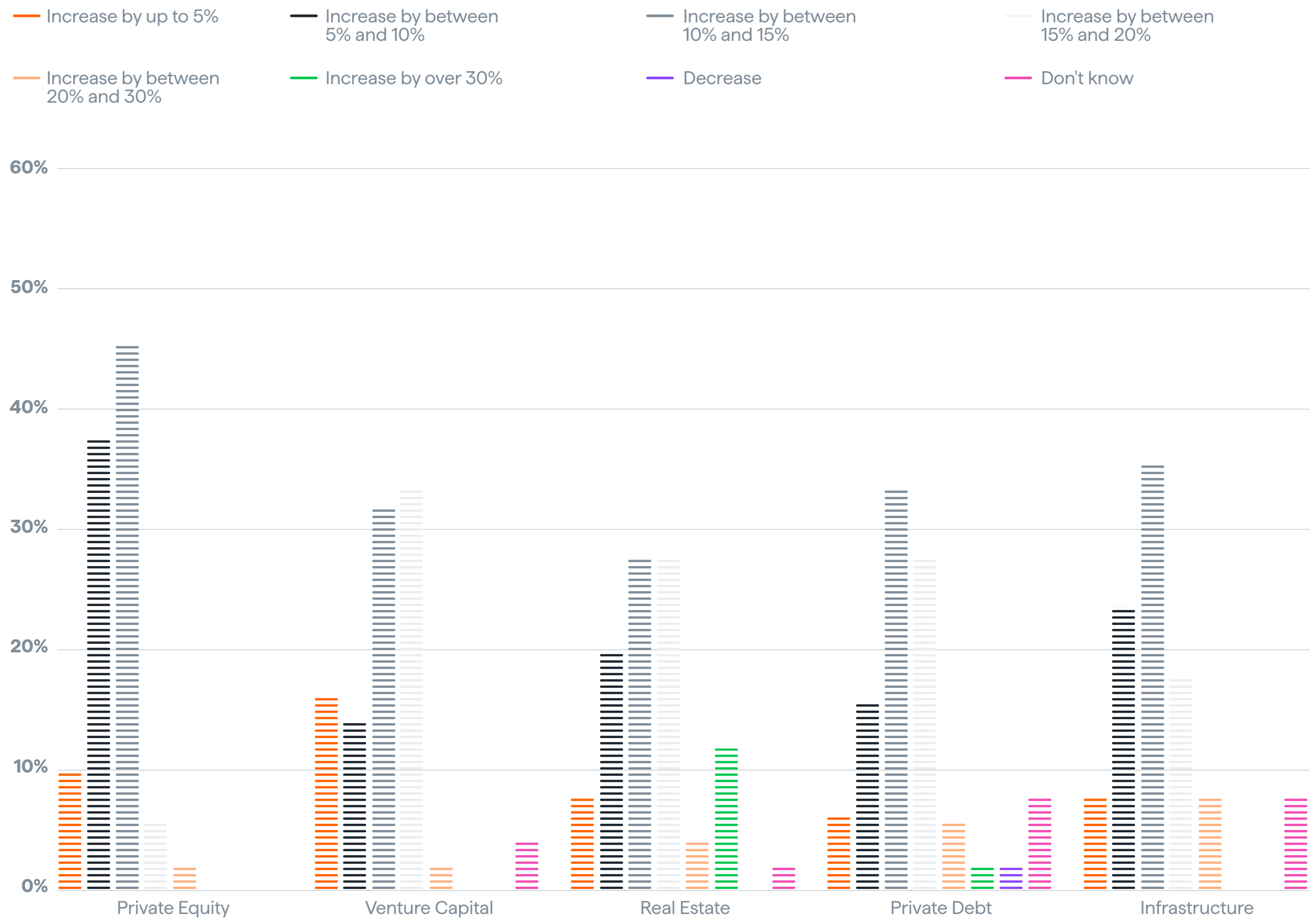
Respondents expect seismic shifts towards the revised European Long Term Investment Fund (ELTIF) and the UK's Long Term Asset Fund (LTAF) in the near future.

Almost half (49%) of the UK and European DC schemes surveyed say that they will increase allocations to private markets using government-created vehicles by between 10% and 15% over the next three years.

Almost a third (31%) say allocations will increase by 5% and 10%, while 10% say allocations will grow by 15% and 20%. The same number say allocations will increase by up to 5% over the next three years.

Over the next five years, DC pension schemes intend to increase their allocations to all key private markets.

Over the next five years, how do you see allocations from DC pension schemes to the following private markets changing? (UK and European DC pension schemes)



Access to market

The most popular way for the DC schemes we surveyed to access private markets was through co-investment with a private markets fund manager with 88% choosing this route. Meanwhile, 45% opt for direct investment while 18% use the relatively nascent LTAF or ELTIF structures.

However, the latter routes to market are set to increase over the next three years according to 79% of respondents, with 31% of those expecting dramatic increases. Just over one-fifth (22%) say they will stay the same.

The more popular current market access options will also continue to grow in the next three years. More than half (57%) say co-investment with a private markets fund manager will increase dramatically while 31% say they will increase slightly. One in 10 (10%) say the usage will stay the same.

Direct investment will increase dramatically according to 37% of DC schemes, while 53% say they will increase slightly . Again, 10% say the usage of direct investment will stay the same.

79%
expected to increase

31%
expect dramatic increased

22%
say it will stay the same

ESG incentives

While the regulatory framework is undoubtedly making it easier to invest in private markets, DC schemes also identify several benefits of diversifying into these asset classes.

When asked to rank the positive characteristics of private market investments, respondents listed improving the sustainability record of the DC plan as the most important.

Below are the main benefits of investing in private markets, listed in order of importance:

1
Improve sustainability record of DC plan

2
Improve marketability and attractiveness of DC

3
Support impact investment strategy of DC trust

4
Improved risk adjusted returns

5
Provide income

6
Improved diversification

Given that a key benefit for more than a third of DC schemes is the ability of private markets investment to improve their plan's sustainability record, it is unsurprising that respondents expect scrutiny of ESG issues to increase over the next three years.

More than nine out of 10 (92%) of DC schemes say focus on environmental issues will intensify, with 43% saying it will do so dramatically.

For social issues, 82% of respondents say scrutiny will increase with 37% expecting dramatic growth.

Governance issues meanwhile will see a dramatic increase in scrutiny according to 26% of DC schemes. Sixty one percent say there will be slight increases and 14% say analysis will stay the same.

When asked how to secure the best risk-adjusted returns from private market investments, the majority of respondents see value in diversifying their portfolios.

More than a third (37%) of DC schemes surveyed say a 60% equities 20% bonds and 20% private markets portfolio split is optimum. One-third (33%) of respondents say about the same between 60/40 and 60/20/20 while 30% believe in the traditional 60/40 portfolio.

Tokenization of private markets

By their nature private markets are illiquid, and as our survey reveals they rely on an infrastructure that is complex, manual, and lacks standardisation and transparency. All of these are hurdles for DC schemes to overcome.

Consequently, private market participants are looking at the benefit of tokenization, which uses blockchain technology to convert an asset or ownership rights of an asset to digital form.

Almost all (96%) of the DC schemes we surveyed agree that the tokenization of private assets would make the asset classes more suitable for retail investors.

However, respondents do not anticipate tokenization of the private markets becoming mainstream anytime soon. Just 2% say it will happen within five years; 18% say seven years; the majority (45%) say eight years; 29% nine years and 6% say it will take a decade.

Overcoming obstacles

Tokenization may go some way to alleviating the challenges for DC investors when considering private markets, but there are still plenty of other hurdles for this sector to overcome.

When asked to rank the challenges facing DC schemes when investing in private markets, respondents say their investment platform lacks the capability to provide and manage these assets.

84%
said they were too high

14%
said they were acceptable

2%
said they don't know

In second place DC schemes say high fees are a problem; while lack of liquidity was third; too few products was fourth; and lack of reporting and transparency around private markets came fifth.

Looking more closely at fees associated with private markets allocation, 84% of the DC schemes we surveyed say that they are too high. Some 14% say they are acceptable while 2% say they don't know.

This picture is set to worsen for DC schemes with 80% of respondents expecting fees to rise, with 10% saying increases will be dramatic. Whilst 14% say fees will stay the same; 2% expect falls; and 4% are unsure.

Conclusion

The financial services sector – with support from policymakers and financial watchdogs – is making life easier for retail investors to capitalise on the opportunities available from private markets.

As our research shows, there is widespread enthusiasm for innovation including the greater use of technology; innovative products; and a more appreciation of the importance of supporting sustainable investment strategies.

Yet this sector is still a work in progress. Survey respondents acknowledge multiple challenges in private markets including the ability to work in non-domestic markets; regulatory complexity; technology limitations; lack of in-house expertise and knowledge; and a dearth of suitable investment products.

The research shows that partnering with third-parties is increasingly seen as a way to overcome such obstacles and to facilitate the successful growth in private markets.

Asset owners and wealth managers need to tap into specialist expertise within all areas of the fund lifecycle and across all relevant jurisdictions, from providers with robust infrastructure and access to the latest technology.

With the right partnerships, fund managers can ensure their investors can safely and easily access the opportunities private markets can provide.