Investments

Private markets

A compelling returns story

Private markets – a compelling returns story

Exposure to assets that are unavailable through public markets.

Potential for excess returns relative to other asset classes.

Long-term historical returns above equities of 3%+[1].

Moving your portfolio from good to great

Following years of strong returns in traditional assets, we believe the forward-looking return expectations from these asset classes are low. Investors looking to meet their objectives need to reposition their portfolios for this new reality. Investing efficiently in private markets can be a tool that helps investors get from a good outcome to a potentially great one.

But what are private markets? Private equity first comes to mind for many investors and forms a significant component however additional examples include private debt, real estate, infrastructure and agriculture amongst other strategies. These assets offer different risk-return drivers and have the potential to outperform traditional assets over the long term. Whilst private equity is looking to generate capital growth, investors seeking yield can potentially benefit too from investing in certain strategies like private debt and real assets. This broad and diverse opportunity set means investors can build portfolios that not only reflect where the market is offering opportunities, but also reflect the specific needs of individual institutional investors.

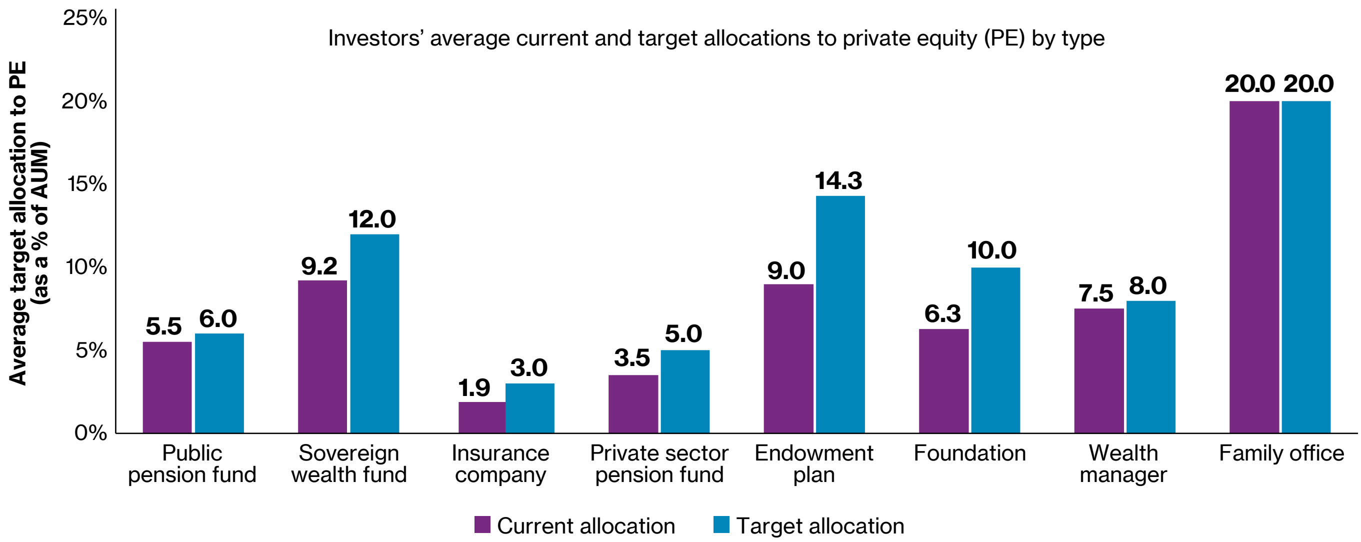
A $7 trillion opportunity[2]

There is a tremendously vast and diverse opportunity set in private markets from which investors can source returns. With fewer and fewer companies choosing to go public[3], investors are potentially missing out on a large portion of the investable universe if they simply invest in listed assets.

This is increasingly recognised across investor types, with private pension funds, public pension funds, sovereign wealth funds, family offices and endowments already allocating significant amounts to private investments. *Figure 1* shows an average 8% of institutional investors' assets currently allocated to private markets. With target allocations 33% greater than current allocations on average, we expect these investors to continue to build up their portfolios.

Our experience has shown that strategy allocation and long-term thematic investing can add significant value in private markets. While most managers and advisers structure single mandates around traditional asset class definitions, we advocate a global and holistic approach, investing across a wide range of opportunities, and unconstrained by those traditional strategy buckets.

Figure 1. **Many investors are increasing allocations to private assets**[4]



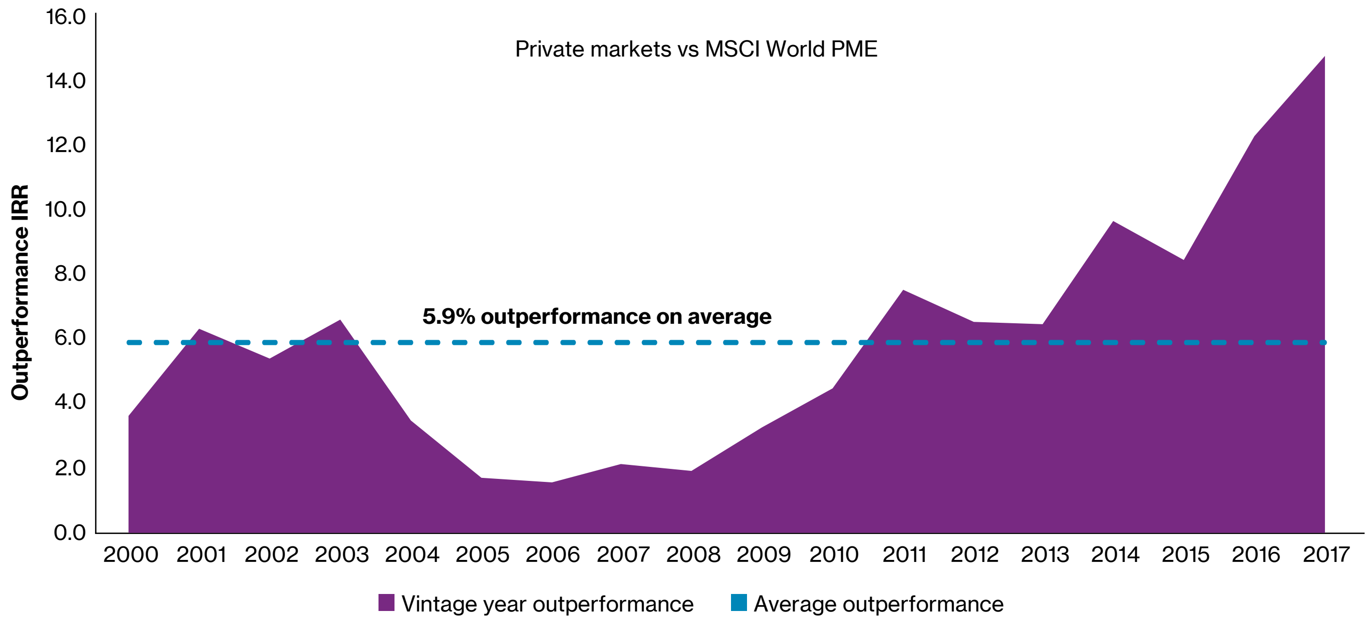
[1]Please see *Figure 2* for more details of outperformance
[2]Preqin, October 2020. Future of Alternatives Report
[3]Thinking Ahead Institute, September 2019. Asset Classes of Tomorrow. www.thinkingaheadinstitute.org/en/Library/Public/Research-and-Ideas/2019/09/Private_equity_markets
[4]2020 Preqin Private Equity & Venture Capital Report

Proven returns

Private markets have a historical track record of achieving excess returns relative to other asset classes such as equities and bonds. *Figure 2* shows the outperformance of the median private markets manager for a particular vintage year, compared to a public equities equivalent.

Private markets investments have outperformed public equities by 5.9% per annum since 2000.

Figure 2. **Private markets outperformance**[5]



Past Performance is not indicative of future results.

[5]Preqin median private markets fund returns compared to listed equities (MSCI World), for vintages 2000 to 2017. 2018 to 2020 vintages are excluded due to immaturity of these investments. Data to June 2020.

Are private markets really right for me?

"Alpha from my listed equity investments can probably do the same job"

We believe diversifying the sources of returns to include illiquidity and greater skill can contribute to a more robust portfolio.

"The illiquidity worries me"

We believe illiquidity in private markets is typically overestimated. Even though lock-up terms are typically 10 years, cash flows are received throughout the term and the value remaining in a fund at year 10 is typically minimal. Furthermore, the significant growth of the secondary market has materially increased liquidity.

Unearthing compelling strategies – relative-value thematic investing

In an increasingly integrated global economy, investors are focusing less on allocating capital based on asset classes and geographies. A thematic investment approach (one that identifies economic, political, industrial, demographic and social trends and then seeks to invest in the most advantageous areas to benefit from them) can be used to help exploit opportunities to generate attractive potential investment returns. This has guided our approach to private markets investing since 2006.

Our approach combines insights from our 70 capital markets research, private markets research, and portfolio management investment professionals[6]. Each investment made is highly focused, attuned to serve the specific needs of our clients and rooted in a common belief: we believe investors that take a long-term view, whilst avoiding mission impairment in the short term, have a competitive edge over others.

> **"A good hockey player plays where the puck is. A great hockey player plays where the puck is going to be."**
>
> Wayne Gretzky
>
> *(Steve Jobs often used this quote to describe Apple's strategy)*

[6]As at June 2020

Case study:
Using technological disruption to our advantage[7]

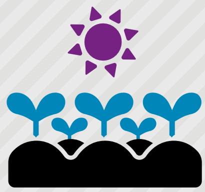
Our thesis:

- Cyber threat has increased dramatically as companies and individuals rely more and more on technology. Mobile devices and online services (such as banking applications) can pose a threat to security and privacy further heightened by the sophistication of the global information network and the ability of cybercriminals.
- The cost of data breaches is expected to increase globally as we become more connected. Companies and individuals need to respond to this by protecting themselves from this risk and the associated spending is expected to increase correspondingly.

Translating this into investible opportunities:

- With increased threats, costs and resulting spending, the space is ripe for innovation and disruption. It is our view that fresh, entrepreneurial thinking that will deliver innovation is best nurtured in small, flexible teams rather than in large corporates.
- We evaluated several technology specialist funds globally and invested in a fund that invests in small, but growing technology companies managed by principals with over 15 years of experience.

Case study:
Positioning portfolios to benefit from emerging trends of sustainable production in agriculture[7]



Our thesis:

- Farming is undergoing a profound shift towards a more cost-effective model that maintains optimal growing conditions in order to meet the demands of consumers and retailers for year-round supply. In addition, the heightened awareness around food safety and sustainability of resource use has only increased the appetite for greenhouse-grown produce. We believe this presents a compelling investment opportunity for asset owners to invest in an emerging sector of agriculture production, by providing finance to develop advanced greenhouses.
- We also believe that this opportunity offers attractive entry pricing and income yield versus other income-producing real assets, however, these returns can be elusive and deep industry insight is paramount.

Translating this into investible opportunities:

- We evaluated the universe and invested with a manager that:
  - Takes advantage of the above opportunities and has a first mover advantage
  - Is an industry-leading grower in the United States, with an advanced agriculture infrastructure platform and has strong relationships with key industry players
  - Has the incorporation of Environmental, Social and Governance (ESG) factors into the heart of the business and engrained in the investment process

[7]This is a sample representation of our work with investment managers. Outcomes will vary and there is no guarantee that we can achieve any particular results with any particular manager in any particular asset class.

Building a high-conviction private markets portfolio

We believe in a fresh approach to private markets investing, which breaks down asset class barriers. By utilising a relative-value, thematic approach, we construct portfolios seeking to benefit from long-term trends that private assets are especially suitable for. We diversify portfolios across industries, sectors and regions, thereby looking to introduce more resilience into clients' portfolios.

The key features of this approach are its adaptability to the rapidly changing economic environment and the prioritising of investment strategies to optimise the risk-return profile of long-term investments. In our view, the flexibility of this approach is essential to achieve long-term success in private markets investing.

Ways to implement a private markets portfolio

Primary investments
Core component of a private markets portfolio. Investors (also known as a Limited Partner or LP) in a fund, commit capital to a manager (also known as the General Partner or GP) who takes this capital and sources and manages several investments to build a portfolio.

Secondary investments
Investing into an existing fund, or a portfolio of existing funds, typically to accelerate the 'ramp-up' of a private markets portfolio. Existing fund stakes can also be sold on the secondary market.

Co-investments
Investing alongside a GP directly into a portfolio company or other asset, typically at no fee or a reduced fee.

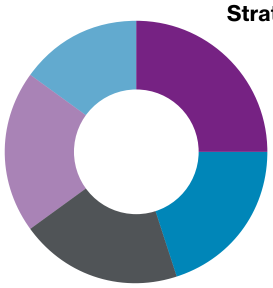
Willis Towers Watson's private markets beliefs

- Access a broad opportunity set and do not view opportunities through the lens of any single asset class
- Be selective – an over-diversified portfolio will deliver expensive market returns
- Adopt a relative value thematic approach to positioning the portfolio; this can harness long-term macro drivers that outlast business cycles
- Advocate for better alignment, securing better fees and terms where possible to reduce cost drag in what is often a high-fee component of the portfolio.

Figure 3. **Illustrative Willis Towers Watson private markets portfolio**

Implementation route

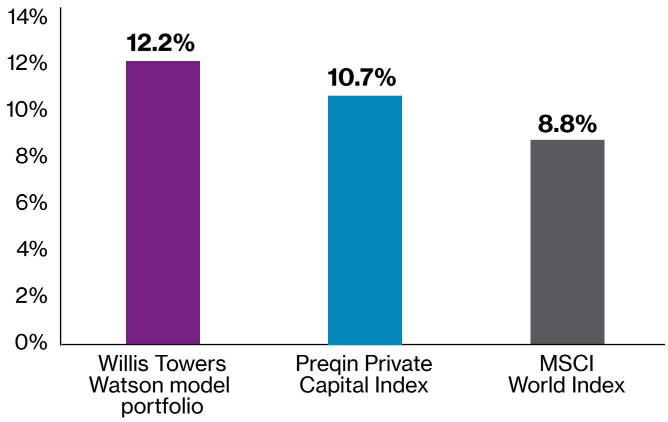
Strategies and styles



A full-service solution

- Willis Towers Watson has been partnering with our clients in private markets for over 20 years. We manage $17 billion of assets across private markets and advise on a further $43 billion[8] for leading investors around the world. Our track record demonstrates the value we have generated for our clients.

Figure 4. **Willis Towers Watson's private markets track record**



Source: Willis Towers Watson, managers, Willis Towers Watson clients, MSCI, Preqin June 2020.

Please note that public equities IRR are calculated using the PME methodology. Vintages from 2006 to 2016. Commitments made in 2017–2020 have not been included in the analysis due to their immaturity. The valuations for each of the funds are as at the most recent available date but adjusted for any cash flow movements (drawdowns and distributions). This data is not audited.

Past performance and simulated performance are no guarantee of future results.

How we can work with you

The implementation of private markets can be complex; however, we aim to make this process as easy as possible for our clients. Our service spans the following areas:

- **Portfolio construction** – building and managing exposures and styles that complement each other and existing investments
- **Investment selection** – research-driven approach to identifying attractive opportunities and high-quality investment talent
- **Operational due diligence and risk management** – evaluating the functions supporting the investment teams at asset managers to detect unforeseen risks
- **Implementation of portfolio management** – legal reviews, completion of subscription and redemption documents, cash-flow management, and the ongoing monitoring of the portfolio

Conclusion

With great uncertainty around how the global economy will recover in the coming years, private markets can offer institutional investors an asset class that has historically delivered returns throughout market cycles. Investors should strongly consider whether they would benefit from these returns to meet their obligations.

A selective, thematic and disciplined approach is, however, required to build a robust, best-in-class class portfolio and we at Willis Towers Watson are well placed to assist clients on that journey.

[8]Data as at June 2020

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- The document contains figures that refer to simulated past performance, which is not a reliable indicator of future returns.
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