PRIVATE MARKET INVESTING

Whittier Trust

The Opportunities and Challenges

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While it may be easier than ever to participate in private markets, these investments require a different mindset and strategy than investing in public assets.

If you have a portfolio of stocks, bonds and other public assets, you may be intrigued by private market investing. Private market investing—a phrase often used interchangeably with private equity, venture investing and direct lending—offers robust opportunity, said Jay Karpen, investment manager at Whittier Trust.

"Companies are staying private longer and are going public at larger sizes than they were a decade ago," he said. "Because of that, we're seeing more investors who want to participate in the private markets."

But while it may be easier than ever to participate in private markets, these investments require a different mindset and strategy than investing in public assets. "There's more risk due to less disclosure combined with asymmetric information, illiquidity, execution challenges and manager risk," said Karpen, adding that connections to opportunities, extensive due diligence and access to industry experts is essential.

Here are five tips to consider when you're adding private market investments to your portfolio.

An Extension of Traditional Asset Classes

Instead of thinking of private market investments as a brand new type of investment, consider it an extension of traditional asset classes, said Karpen.

"Venture and growth equity have similar characteristics to small and mid-cap equities, private equity buyout is similar to large cap and direct lending is similar to fixed income markets," said Karpen.

That said, private market investing does bring additional considerations for investors. For one, the investment is illiquid, they are loosely regulated and there are often fees associated with private market investments.

"You should expect to be compensated for these risks, otherwise it may not be worth it," said Karpen.

The Right Partner is Essential

Since these investments are illiquid, and private equity vehicles generally require a large financial commitment, it's important to take the time to understand the investment partnership, including the fund and the terms of the obligation, noted Karpen.

Because private investing requires access and knowledge of opportunities, it may be smart to work with an advisor or firm you trust. Working with an advisor may also allow access to managers and investment opportunities that otherwise might not be available to you, and may have lower fees and smaller minimum commitments for opportunities than investing on your own.

For venture funds, access to an advisor may be especially important since top tier managers tend to outperform their peers. This may be due to the "preferential access" a top-tier manager may have to better deals and entrepreneurs.

"Because this is a long-term relationship, you need to invest with someone who you can trust," said Karpen.

Private Market Investments Require Due Diligence

"One of the concerns clients have upon entering private markets is less disclosure than they may be accustomed to," said Karpen. That's why it's helpful to partner with a trusted financial advisor. "For example, when a client comes to us at Whittier Trust and wishes to invest in private equity, it's our job to introduce investment opportunities that have undergone our rigorous due diligence process—where we've assessed the market, asked the tough questions, analyzed the track record, and evaluated the documentation."

Karpen added that Whittier Trust leverages in-house sector and asset class experts who further analyze and contextualize opportunities. Prior to investing, make sure you know what research is being done, and make sure your questions are adequately answered.

Diversification is Essential to Manage Risk

While private market investing, when successful, may carry higher returns than public investments, added risk means that your portfolio needs to be thoughtfully constructed to mitigate potential losses.

"Investors dipping their toes into private markets need to remember that 1/3 of companies that went public did so at valuations below their last round of financing and only around 10% of venture investments are going to generate the outsized returns," said Karpen. The best way to succeed is a diversified portfolio. This can be created either through a fund managed by a professional team or by constructing your own multi-company portfolio.

Beyond Private Equity and Venture Capital

Private market investing may sound like shorthand for venture capital, but the private market encompasses a broad range of assets. These include real estate, infrastructure, energy, distressed debt and direct lending investments. Together, these opportunities can form a private-market portfolio that accounts for your level of risk tolerance and financial goals. And while private equity investments may be relatively illiquid, portfolios can include additional asset classes to generate risk-adjusted returns and high-cash yields.

The bottom line? Private investments may carry more risk—but smart private investments, as part of an overall financial strategy, have an opportunity to create substantial reward as well.

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