

Private markets: Time to move

Our private markets capabilities can
help with long-term portfolio growth



Is it private markets' time?

Strategies that worked in previous cycles may not succeed going forward. Historically, a balanced portfolio consisted of a traditional 60% equities/40% bonds asset mix. Such an allocation would have performed very well as global financial stimulus packages drove equity valuations higher and bond yields lower. But increasingly, this approach is seen as inadequate. Based on our five-year capital market assumptions, a sub-4.5% return in nominal terms for a traditional 60% equities and 40% bonds portfolio is expected over the next five years.¹ We believe these lower expectations from public markets put investors on a quest for alternative solutions and argue for an allocation to private markets.

Some investors look to private markets when seeking higher returns or better yields. Others desire inflation protection potential. Meanwhile, many family offices, wealth managers, insurers, endowments, foundations and pension plans are in search of assets whose performance is uncorrelated with major equity indices.

Private assets offer access to privately negotiated transactions that are not available through public market investments. They play an important role in diversifying the liquid component of portfolios and potentially earn an illiquidity premium, which acts as a reward for allocating capital over the long term.

¹ Mercer. Five-year assumptions based on Mercer's *Capital Market Outlook* as of October 2021. Expected returns are hypothetical average returns of economic asset classes. There can be no assurance that these returns can be achieved. Actual returns are likely to vary. Please see Important Notices for further information on return expectations.

Core considerations when allocating to private markets

Is there a window of opportunity for private markets?

Investment issue

Rates near historical lows, fixed income and listed equity valuations at highs

There are concerns that equity markets are richly valued, with limited scope for either earnings or multiple expansion. At the same time, bond yields remain low by historical levels.² Unlike in the past, fixed income may not play a stabilizing role for investors during equity corrections.

Potential private markets solution

Private markets may offer enhanced return opportunities, diversification and/or inflation protection. They are less correlated to public equity and bond markets, providing potential diversification benefits and helping smooth out volatility.

Fig 1: What private market investments may deliver in a portfolio context



Opportunity for superior risk-adjusted returns by unveiling alpha potential.



Greater diversification away from listed markets and access to broader opportunity set.



Illiquidity premium may be available to providers of long-term capital.

² Bloomberg; Global Financial Data, TB rates since 1900 to Q2 2021 — US Generic Government 10-year Yield/ Japan Generic Government 10-year Yield/ UK Generic Government 10-year Yield/ Germany Generic Government 10-year Yield.

Investment issue

Sustainability and diversity considerations

In recent years, sustainability has grown in importance and has become one of the key considerations for investors. Private markets can offer opportunities to create a measurable positive impact by engaging with companies that are believed to be making a difference, rather than simply avoiding those that score poorly on ESG measures.

Potential private markets solution

Private equity, private debt, real estate and infrastructure are asset classes in which investors could have a positive impact with their capital, and recent inflows have reflected this. We believe private markets to be a natural home for sustainability strategies, as holding periods are typically longer, and underlying fund managers often have a greater degree of involvement with portfolio companies.



Can private markets play a key structural role in portfolio construction?

Investment issue

Not all institutional investors tap into private markets' potential for higher returns.

Many institutional investors allocate to private markets in search of potential strong risk-adjusted returns versus public markets. According to Mercer's surveys and industry resources, it is the norm for large endowments to have 40%-60% of their portfolios in alternatives.³ Meanwhile, "large public pension plans and sovereign wealth funds typically allocate 5%+ to alternatives and are considering increasing their alternatives allocation."⁴

Potential private markets solution

Private markets have a compelling track record of historically outperforming their public counterparts and proved to be more robust during the financial crisis.

Investment issue

Lessen performance gap after market shocks.

From time-to-time, markets are hit by a shock event, whether it's the bursting of the US housing bubble, or more recently, the COVID-19 pandemic. In times like these, public markets tend to react in knee-jerk fashion, leading to securities falling substantially.

Potential private markets solution

Private markets have historically offered better resilience in downturns.

Private markets are not immune from downturns, yet they have shown resilience during past crises. Why? For one thing, investors in these markets tend to take a thoughtful, long-term approach. Moreover, as they do not require these assets for liquidity, forced selling is not a common occurrence.



³ Mercer, The Foundation Model <https://www.mercer.us/our-thinking/wealth/pavilion/endowment-model.html>

⁴ [Mercer Growth Markets Asset Allocation insights, October 2021](#) and Greenwich Associates — US Institutional Investors 2020.

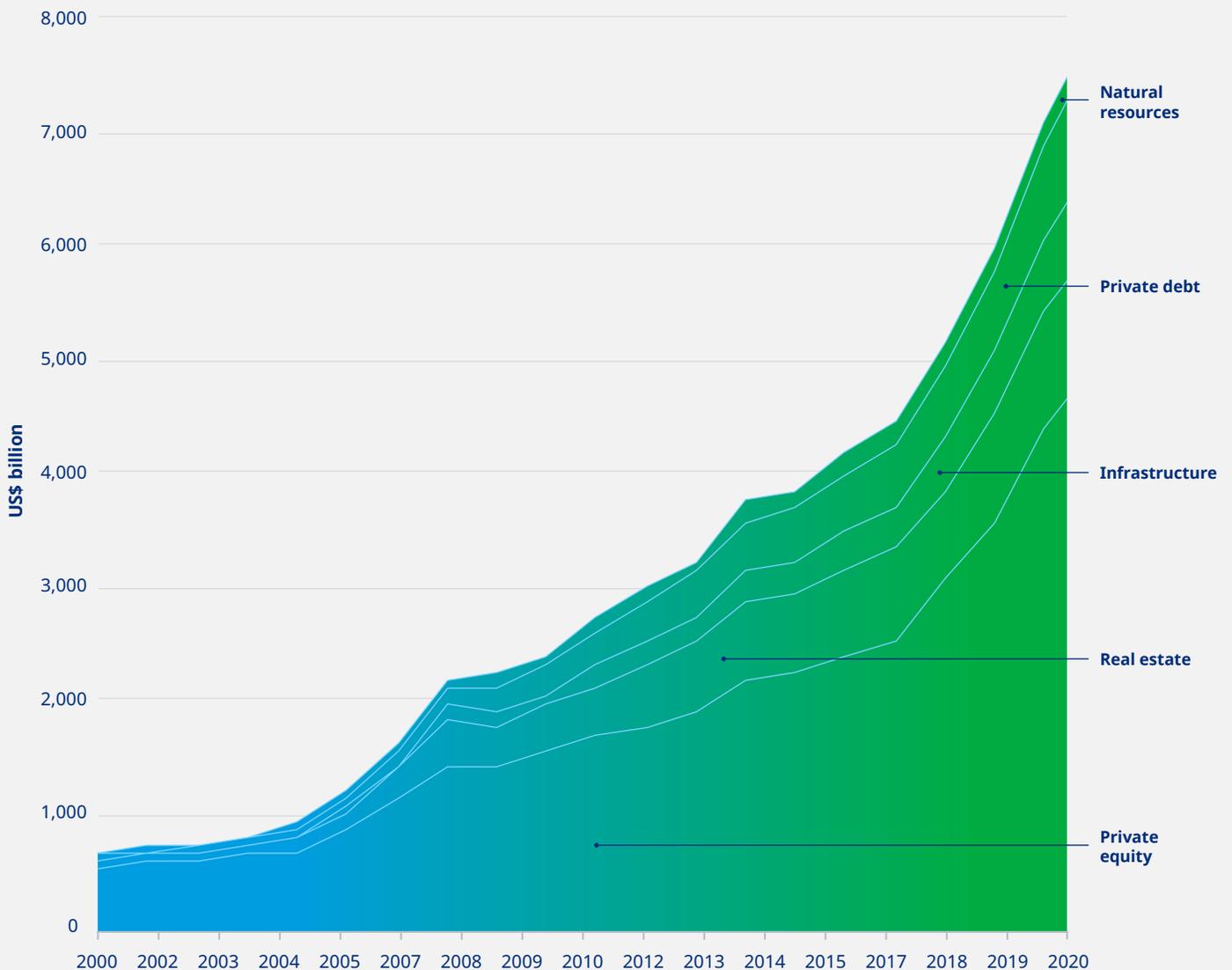
Investment issue

Investors who fail to consider private markets may miss out on future growth in these asset classes.

Potential private markets solution

Private markets are on the ascent and continue to attract **sizeable amounts** of capital. This multi-year trend shows no signs of abating (see Figure 2).

Fig 2: Private market assets under management⁵



⁵ Preqin, as of end of 2020.

Investment issue

Find differentiated ways to help deliver manager alpha over the long term.

Potential private markets solution

Private markets can offer a number of avenues of potential added value for investors (see Figure 3).

Fig 3: Investment themes that can drive value in private markets⁶

Initiatives to help improve the way assets and companies invested in are run more efficiently

- Management team (commercial operational expertise)
- Efficiency gains/cost management
- Digitalization

Opportunities arising from secular and cyclical shifts

- Technology disruption reaches an increasing number of business models
- Corporate M&A buying spree will create disposals of non-core assets
- Improved pricing of stressed/distressed assets



Buy-and-build strategies/multiple arbitrage opportunities entry

- Consolidation in fragmented markets
- Entry into adjacent industry sectors

Expansion of business models

- Adding new revenue sources, clients and user channels
- Broadening of product lines
- Geographical expansion (regional/international)

We help investors navigate these challenges to access a wide range of private market managers in a way that complements their portfolio — and work toward attaining their financial goals.

⁶ Mercer cannot guarantee access to opportunities. Access is solely at the discretion of the manager.

Six crucial steps to follow when allocating to private markets

1. Map out your long-term plan and strategy

First, you need to decide how much of your total portfolio you're comfortable allocating to less liquid, long-term investments. You should consider your ongoing cash flow requirements and recognize that the capital you commit to private markets investments will be invested incrementally over time, and you will need to have cash available when a capital call arrives.

2. Choose your managers and secure access

In private markets, the difference between the returns made by the best and worst performing managers can be considerable and are often much wider than in traditional asset classes. We believe capturing the most attractive opportunities with highly rated managers will require active sourcing, research and access to high quality, specialist private markets managers.

But accessing them isn't easy. It takes time, requires extensive research and planning, and can bring additional operational and governance challenges.

Our 30 years, history in this space and local presence across the globe helps us potentially access high-quality opportunities through our network of established relationships. So, make sure you do your research or engage alternatives professionals to guide you. Manager selection is where you need to choose the right collaborator, who understands your needs and has the depth of experience to help you implement a private markets solution.

3. Diversify your risks

Due to the capital-intensive nature of private markets investments, most managers focus on a small number of assets in their portfolios. For example, in private equity or infrastructure, there may be as few as 10 underlying assets in an individual manager's fund.

Allocating to a range of private markets strategies can help diversify your portfolio by number of underlying investments, manager, strategy, geography and vintage year.

4. Ongoing commitment planning

Most private markets managers offer their investment strategies

through closed-end fund structures and raise capital infrequently, with limited capacity. You need to put a robust commitment plan in place to build up and maintain your exposure at your desired target level over time, as illustrated in Figure 4. on the next page.

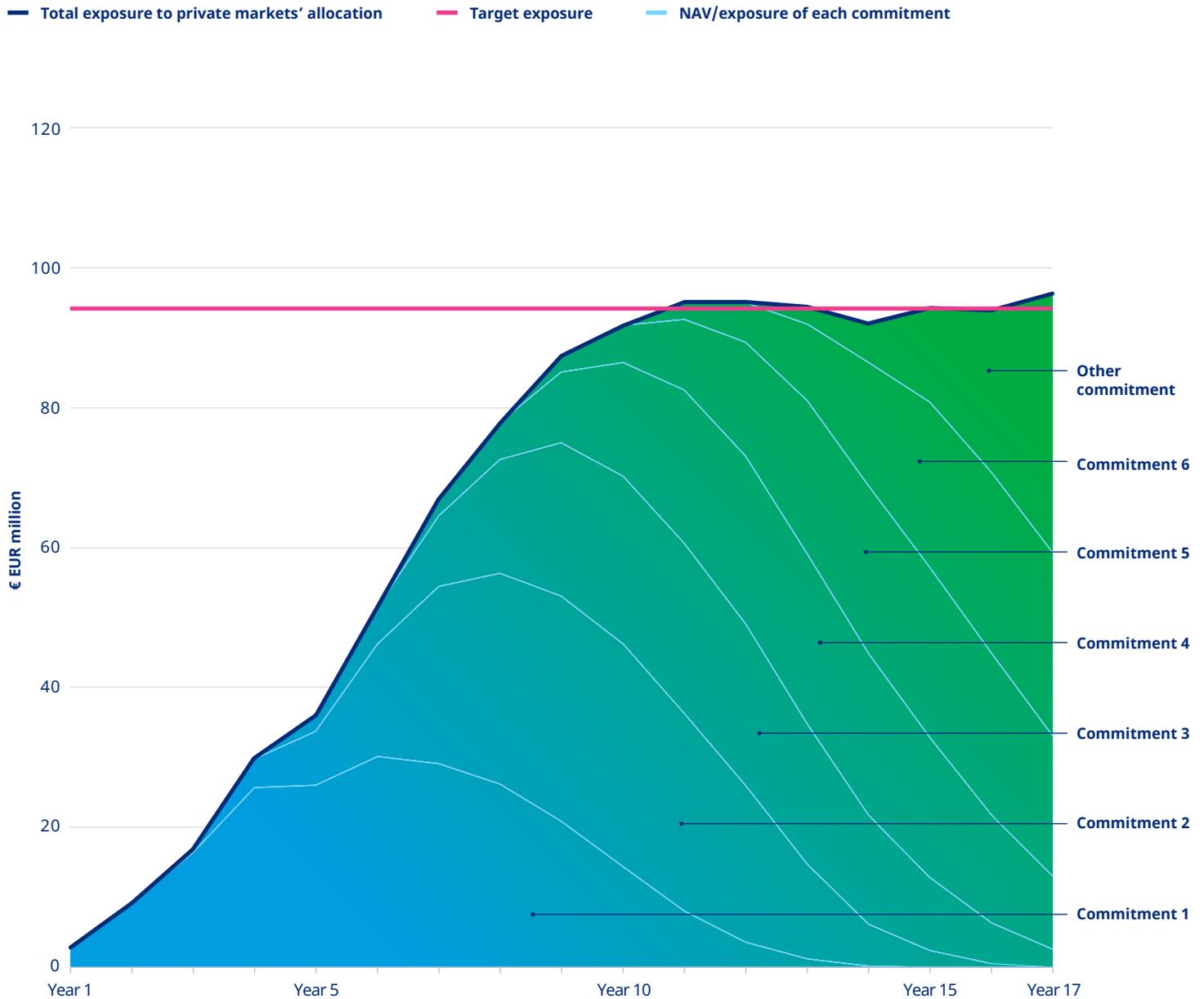
5. Monitor your portfolio carefully

Once you've implemented your strategy, we believe it is vital to monitor underlying investments and ensure you are comfortable that your portfolio is on the right track. It's particularly critical to assess your liquidity budget and commitment plan on an ongoing basis. This helps keep your strategy and target allocation in line with your desired position.

6. Get the details right

Operational, legal and tax due diligence is crucial, given that investment structures are in limited liquidity vehicles, with little option to action any changes after your initial commitment. These areas require careful consideration and rigorous assessment before committing to any private markets investment.

Fig 4: Example of commitment planning over time⁷

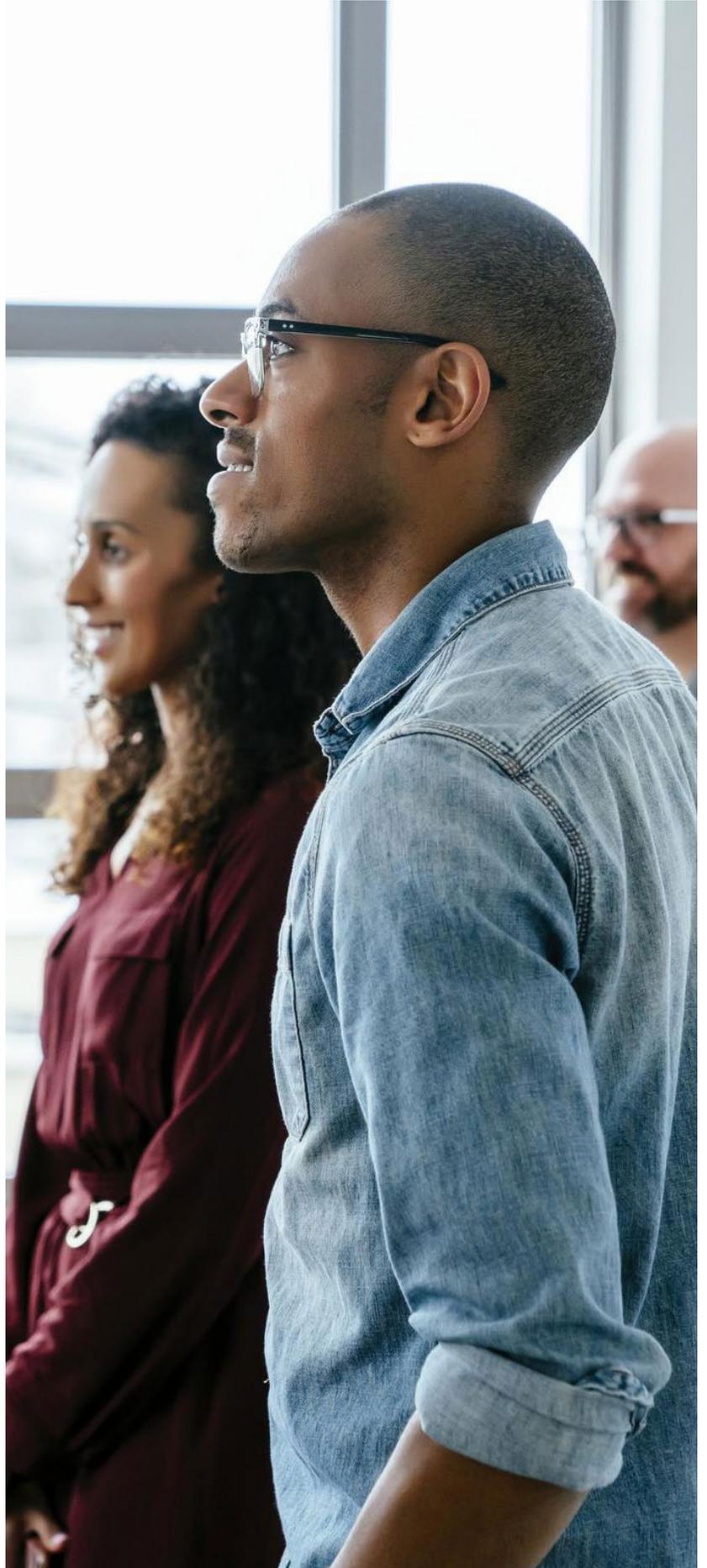


⁷ For illustrative and educational purposes only. Pitchbook, Mercer and Mercer Commitment Planning Model (MCPM), based on long-term average cash flow and valuation life cycle patterns of private market funds which were built up as a cascade including assumptions on the underlying investments of the primary funds, secondary transactions, and co-investments as well as on portfolio construction targets set by Mercer. More specifically, input parameters are distinguished by the risk profile of the implemented strategy, e.g. buyout, growth capital,

venture capital, special situations, etc. For each of these risk profiles, Mercer has assumed a specific investment pace, fee structure, income yield, growth component (reflected in valuation growth) and capital gain. These assumptions are based on our experience and actual data captured in our integrated and customized controlling, monitoring, and reporting system that covers more than 200 active private market funds on a daily basis (since 1996). Target allocation is just the target allocation to private markets.

We are with you every step of the way

Perhaps your organization has long been invested in private markets. Then again, maybe you are considering them now for the first time. While many of the qualities of private assets make them attractive, these markets have also exhibited barriers to entry, with challenges around complexity, illiquidity, fees and governance often cited as reasons for not allocating. Whatever stage you are at in your private markets journey, we are here to offer the advice, research and implementation to help you implement private equity, private debt, infrastructure, co-investment and secondaries, impact and real asset strategies.



How we work with clients



Client-centric flexible approach



Comprehensive research platform



Global reach, local resources

Supported by reporting, monitoring and Mercer's operational best practices

Unlike some of our competitors, we offer a **customized private markets service**. Our work begins with the knowledge that no two investors are the same. Whether it's their cash-flow requirements, targeted returns, or familiarity with private markets, every organization is truly unique. Pension providers, endowment funds, insurance companies and wealth management firms will all have their own approaches and needs. With this in mind, we construct **flexible private markets solutions** across all asset classes, designed to help meet each client's particular needs, objectives and risk appetite.

From liquidity budgeting and strategy design to in-depth

operational due diligence and standardized reporting, our dedicated, experienced teams help streamline even the most complex processes for our clients.

How do we differentiate ourselves from competitors?

Our scale is not limited to one or two markets — if it's a manager that we believe has the potential to generate alpha, we research and rate them, and potentially recommend them to our clients based on their specific needs.

We take a broader view rather than focusing exclusively on private markets. We have a **long heritage in both liquid and private markets**.

Our alternatives investment team consists of more than 220 staff in 25 locations,⁸ covering portfolio construction and asset management, and offering insights to clients on how public market components can interact with alternative investment holdings in different market conditions.

And thanks to our **scale and established relationships with managers**, we can help negotiate manager fees often passing possible savings directly to our clients. Additionally, these managers will provide forward-looking visibility into launches across private markets strategies.

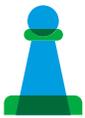
⁸ Mercer, as at September 2021.

What we can offer you

Rigorous fund selection process

Mercer typically reviews over 2,000 fund offerings each year. Following this global research review process, we rank candidates, perform due diligence, assign ratings and make recommendations for investment.

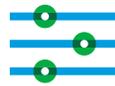
We have four key factors for selection:



1. Strategy



2. Track record



3. Alignment



4. Business management

Our capabilities

Fig 5: Flexible private markets portfolio solutions tailored to each client's needs

Single client advisory

Single client programs and funds

Multi-client funds



Private equity



Private debt



Impact



Infrastructure



Real estate



Co-investments & secondaries

Why consider Mercer for private markets?

We are a trusted collaborator

[Mercer ranks #1 in OCIO assets under management](#) by Chief Investment Officer Magazine's 2021 Outsourced CIO Buyer's Guide Survey. With more than 1,500 clients in Mercer's outsourced chief investment officers (OCIO) assets under management, in a 2021 survey of outsourced CIO providers, Mercer contributed to the \$2.1 trillion among 13,323 clients comprised of the 47 firms that participated in the survey.

We are truly global

Our history and our local presence around the world helps us potentially access high-quality private market opportunities through our network of established relationships.

We are large

Our size and scale by our number of private markets investment professionals and the number of managers we research on an annual basis, helps us find opportunities for clients, and potentially negotiate fees with private equity, private debt, infrastructure, impact and real estate managers.

We are thorough

We scrutinize every manager's team, strategy, performance track record, and alignment with investors' objectives. To implement flexible private markets for our clients solutions, we embed our established research from across the private markets investment spectrum. And we carefully review managers' commitment to environmental, social, diversity and governance practice.

We are independent

We believe we are differentiated as we offer the solutions and advice you specifically need, rather than the products we think you should select.

Find strength in our numbers

~\$160bn

Global alternatives assets under advisement⁹

Private markets	~\$110bn
Hedge funds	~\$50bn

~\$22bn

Global alternatives assets under management⁹

Private markets	~\$14bn
Hedge funds	~\$7bn

~220

Global alternatives professionals¹⁰

Private markets	~180
Hedge funds	~40

25 offices globally¹¹

30 years' private markets experience

⁹ Assets Under Management and Assets Under Advisement as of December 30, 2020. **Please see Important Notices for information about Assets under Management and under Advisement.** Private markets assets based on committed capital. Hedge funds and other alternative assets based on Net Asset Value (NAV). Dollar amounts in USD. Excludes fee compliance assets. Due to rounding, totals provided may not precisely reflect the absolute figures.

¹⁰ As of September 30, 2021, excludes administrative personnel.

¹¹ As of September 30, 2021.

Your strategy, our platform

Building a private markets portfolio can be complicated. However, when executed well, our view is that the rewards are worth it.

We believe our clients choose us because of our scale, well-resourced global team and the quality of our platform. Let us help you design a private markets program tailored to your specific needs.

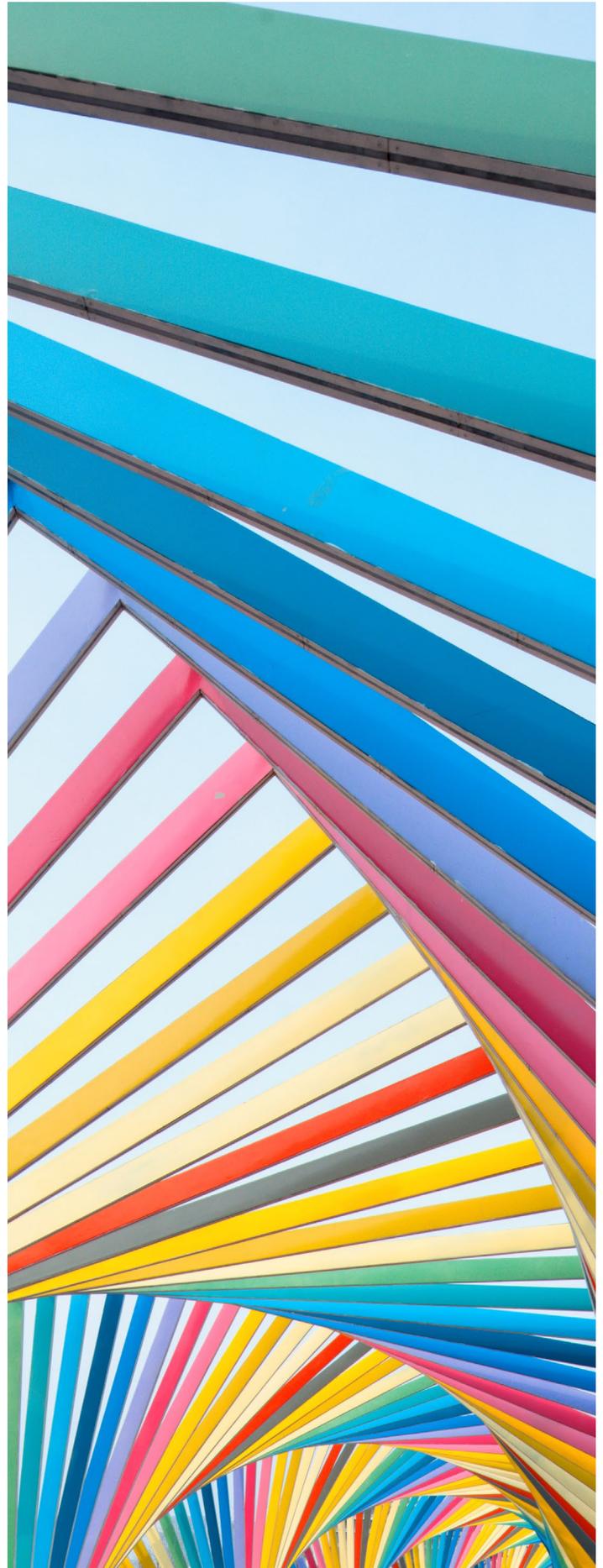
Contact us to explore how we can help you implement your private markets strategy today.



www.mercer.ca/privatemarkets



contact us



Reshaping the future.

About Mercer

At Mercer, we believe in building brighter futures.

Together, we're redefining the world of work, reshaping retirement and investment outcomes, and unlocking real health and wellbeing. We do this by meeting the needs of today and tomorrow. By understanding the data and applying it with a human touch. And by turning ideas into action to spark positive change.

For 75 years, we've been providing trusted advice and solutions to build healthier and more sustainable futures for our clients, colleagues and communities.

Welcome to a world where empathy and economics make a difference in people's lives.

Welcome to brighter.

For further information, please visit www.mercer.ca

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How we can help

Continuously rethinking purpose and priorities drives HR transformation. Shaping the future of work requires improved strategies around investment and retirement, health and wellness benefits, talent and communications. We believe in the value of investing in the future to build resilience for your business and your employees.

Investments and retirement require sophisticated solutions. We approach these with a big-picture view that prioritizes long-term financial wellness. We offer research and advice on assessing risk and designing benefits programs while keeping in mind the need to optimize throughout changing times.

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