

The HUB

NEWS AND VIEWS FOR INSTITUTIONAL INVESTORS

Together at last: DC schemes and private assets

Tipping point in sight as rising demand for private market instruments meets rapid innovation of supply

It has been possible for DC schemes to give their members access to private markets for a number of years now. Yet allocations to private assets are, in aggregate, negligible despite the well-documented boost to returns, diversification and downside protection that they can offer. The reasons for the reluctance are numerous, but include a reticence on the part of trustees, who tend to be cautious on new asset classes in general and on illiquid asset classes in particular.

Price is also an issue. Private assets require considerable expertise and governance, so fees tend to be higher than for the management of listed assets. With fee caps in UK DC schemes' default portfolios set at 75bps, but the competitive consolidating market trading at around 25bps, private market fees have been seen as a difficult fit with DC.

Scheme consolidation calls for wider asset range

But times, as they say, are a-changing. There is an improving momentum on the demand side, as schemes consolidate and create ever bigger pools of assets that can invest at scale to create more diversification and better net returns for the members. This creates an attractive cash-flow that may well bring down fees and makes private assets, in particular, more affordable.

"From perhaps 5,000 single trust DC schemes, we are now moving to the consolidation endgame, which will be perhaps 10-20 large DC master trusts, plus a small handful of very substantial individual company schemes," says Nick Groom, head of DC strategy and sales at Natixis Investment Managers (Natixis IM).

This endgame, Groom notes, is the natural evolution of a process that began with the advent of auto-enrolment in 2012 and the conversion over many years of DB schemes to single trust DC schemes.

These dynamics, which have been playing out for many years, have created massive pools of pension cash which requires a wide range of assets to deliver the returns pension savers need.

"Private markets, with their diversification and performance benefits, will be a sizeable and growing part of the mix required by long-term savers," says Groom.

As schemes get more comfortable with private assets, they will enjoy the benefits of an asset class which has low correlation with other assets, is less volatile than comparable listed assets and in which managers often have more direct control than they have over publicly-traded securities.



Nick Groom
Head of UK DC Strategy & Sales
Natixis Investment Managers

Key takeaways:

- As schemes consolidate and create ever bigger pools of capital, they can invest at scale. This may bring down fees and makes private assets more affordable, but quality can't be compromised.
- Regulatory and political momentum is stimulating demand. The Mansion House Compact encourages DC default funds to allocate 5% of assets to unlisted equities by 2030. In addition, the UK regulator now permits performance fees in DC defaults but outside of the fee cap.
- Supply side innovation, such as evergreen funds, new fee structures and access to emerging managers needs to continue its momentum for the inclusion of private assets in portfolios to become a reality.

Regulatory and political momentum

Demand is also being stimulated by government measures, which are increasingly encouraging the adoption of private market assets, with the dual aim of boosting economic growth and improving private pension outcomes.

A key objective of The Mansion House Compact, a non-legally binding initiative launched in late 2023, is for DC default funds to allocate at least 5% of their assets to unlisted securities by 2030. Currently just 0.5% of UK DC pension assets are invested in unlisted UK securities.

The initiative was announced as part of Chancellor, Jeremy Hunt's, first Mansion House speech, with estimates that his proposed reforms could increase a typical earner's retirement income by over £1,000 a year. The Compact was signed by many of the UK's largest DC scheme providers.

In addition, the government has changed the rules on DC schemes to permit the use of performance fees, which now do not form part of the fee cap. Although there have been many detractors, these fees may be necessary to ensure that the underlying quality of the investments are not compromised by asking a traditional global approach to change the way it gets paid for the sake of the UK DC market; important, but still quite small in a global sense.

Another initiative, by the FCA, has created Long Term Asset Funds (LTAFs), which are designed to provide easier, simpler access for DC investors to long-term private markets investments. Groom notes investors can allocate to private markets without using LTAFs, but the new structures represent another welcome access point. "All initiatives to move the needle are helpful," he says.

Supply side innovation

Supply side innovation is also creating momentum for the inclusion of private assets in DC portfolios. For one, Natixis Investment Managers are innovating to reduce the fee burden for private market strategies.

This includes the flexible use of origination fees in private credit whereby instead of reinvesting the

origination fees which are a transaction cost, members receive a much lower ongoing fee.

Meanwhile, investment firms with a range of private equity offerings can offer lower fee entry point to private equity assets. An example is via co-investment funds, which tend to have much lower fees than primary funds. If co-investments can be combined with private equity secondaries, the lower fees can be paired with higher liquidity (since secondary assets are closer to their maturity dates). "Put simply, shorter durations equal increased liquidity," notes Groom.

Other innovative solutions include allocations to emerging private asset managers, which may be every bit as skilled as experienced operators, but can be accessed at a substantially lower price point given their more limited track records.

DC-friendly investments

Nowhere is innovation for DC schemes clearer than in a strategy developed by two Natixis IM affiliates, who joined forces to build low-cost, low-governance exposure to private debt.

Some of the assets are allocated to European private debt managed by MV Credit, while the rest are invested in liquid multi-asset credit portfolios, managed by Loomis Sayles & Co.

Unlike allocations to pureplay private debt strategies, the MV Credit/Loomis Sayles solution can put investors' capital to work from Day One. Initially, investor money can be allocated to the liquid Loomis Sayles portfolio, where it can be deployed rapidly. In the meantime, MV Credit identifies private market investment opportunities to enhance strategy returns. As these opportunities materialise, Loomis Sayles divests some of the assets and the proceeds are used to buy private debt managed by MV Credit.

The process is repeated until all of an investor's assets reach the target allocation. When the concept was launched in early 2021, the split of assets was targeted to be 50:50. But for clients who can manage liquidity at portfolio level, the initial percentage invested in private assets can range from 50% to 100%.

Groom says: "Even with 100% private debt, the strategy still has DC-positive attributes in that it is evergreen, the price point is viable, there is daily pricing although uses a stale price, and investors can trade in and out during regular trading windows."

The allocation to private credit is particularly accretive to performance in turbulent times. The approach proved its worth during volatility in public markets in 2022. While correlation between public assets moved towards one, private fixed income markets continued to track steadily upwards, says Groom.

"As long as the due diligence process is right, private loans from companies will rarely default. MV Credit selects strong companies in defensive sectors with stable and predictable cash flows to ensure interest payment on their loans. Volatility in public markets is virtually irrelevant to them."

Schemes and platforms changing their mindsets

The mindset at schemes and platforms is morphing into concrete action. Natixis IM's public/private debt solution, for one, has already found its way into a large number of DC scheme defaults.

"The tipping point is right here," says Groom. "Trustees are losing their inhibitions and are realising that the real risk is not embracing private markets. The Mansion House Compact spells this out in plain, unambiguous language."

Rather than trying to shoehorn investments into structures where DC members can view the value of their retirement funds 24/7 online, the penny has dropped that members don't need or want this kind of visibility. "If you're talking about a 30-40-year investment why do you need daily pricing and liquidity?" asks Groom.

Liquidity is increasingly being managed at a higher level, allowing movements of cash and allocations to listed and now unlisted assets. "Regulators, government, pension schemes and platforms must all continue to evolve and innovate to ensure more schemes and the members they serve, will benefit from these attractive private assets," Groom adds.

Published in April 2024

This communication is for information only and is intended for investment service providers or other Professional Clients. The analyses and opinions referenced herein represent the subjective views of the author as referenced unless stated otherwise and are subject to change. There can be no assurance that developments will transpire as may be forecasted in this material.

Additional notes

This material has been provided for information purposes only to investment service providers or other Professional Clients, Qualified or Institutional Investors and, when required by local regulation, only at their written request. This material must not be used with Retail Investors. It is the responsibility of each investment service provider to ensure that the offering or sale of fund shares or third party investment services to its clients complies with the relevant national law.

Please read the Prospectus and Key Information Document carefully before investing. If the fund is registered in your jurisdiction, these documents are also available free of charge and in the official language of the country of registration at the Natixis Investment Managers website (im.natixis.com/intl/intl-fund-documents).

To obtain a summary of investor rights in the official language of your jurisdiction, please consult the legal documentation section of the website (im.natixis.com/intl/intl-fund-documents).

In the E.U.: Provided by Natixis Investment Managers International or one of its branch offices listed below. Natixis Investment Managers International is a portfolio management company authorized by the Autorité des Marchés Financiers (French Financial Markets Authority - AMF) under no. GP 90-009, and a public limited company (société anonyme) registered in the Paris Trade and Companies Register under no. 329 450 738, Registered office: 43 avenue Pierre Mendès France, 75013 Paris. **Germany:** Natixis Investment Managers International, Zweigniederlassung Deutschland (Registration number: HRB 129507). Registered office: Senckenberganlage 21, 60325 Frankfurt am Main. **Italy:** Natixis Investment Managers International Succursale Italiana (Registration number: MI-2637562). Registered office: Via San Clemente 1, 20122 Milan, Italy. **Netherlands:** Natixis Investment Managers International, Dutch branch (Registration number: 000050438298), Registered office: Stadsplateau 7, 3521AZ Utrecht, the Netherlands. **Spain:** Natixis Investment Managers International S.A., Succursal en España (Registration number: NIF W0232616C), Registered office: Serrano nº90, 6th Floor, 28006 Madrid, Spain. **Luxembourg:** Natixis Investment Managers International, Luxembourg branch (Registration number: B283713), Registered office: 2, rue Jean Monnet, L-2180 Luxembourg, Grand Duchy of Luxembourg. **Belgium:** Natixis Investment Managers International, Belgian branch (Registration number: 1006.931.462), Gare Maritime, Rue Picard 7, Bte 100, 1000 Bruxelles, Belgium. **In Switzerland:** Provided for information purposes only by Natixis Investment Managers, Switzerland Sàrl (Registration number: CHE-114.271.882), Rue du Vieux Collège 10, 1204 Geneva, Switzerland or its representative office in Zurich, Schweizergasse 6, 8001 Zürich. **In the British Isles:** Provided by Natixis Investment Managers UK Limited which is authorised and regulated by the UK Financial Conduct Authority (FCA firm reference no. 190258) - registered office: Natixis Investment Managers UK Limited, Level 4, Cannon Bridge House, 25 Dowgate Hill, London, EC4R 2YA. When permitted, the distribution of this material is intended to be made to persons as described as follows: **in the United Kingdom:** this material is intended to be communicated to and/or directed at investment professionals and professional investors only; **in Ireland:** this material is intended to be communicated to and/or directed at professional investors only; **in Guernsey:** this material is intended to be communicated to and/or directed at only financial services providers which hold a license from the Guernsey Financial Services Commission; **in Jersey:** this material is intended to be communicated to and/or directed at professional investors only; **in the Isle of Man:** this material is intended to be communicated to and/or directed at only financial services providers which hold a license from the Isle of Man Financial Services Authority or insurers authorised under section 8 of the Insurance Act 2008. **In the DIFC:** Provided in and from the DIFC financial district by Natixis Investment Managers Middle East (DIFC Branch) which is regulated by the DFSA. Related financial products or services are only available to persons who have sufficient financial experience and understanding to participate in financial markets within the DIFC, and qualify as Professional Clients or Market Counterparties as defined by the DFSA. No other Person should act upon this material. Registered office: Unit L10-02, Level 10, JCD Brookfield Place, DIFC, PO Box 506752, Dubai, United Arab Emirates **In Taiwan:** Provided by Natixis Investment Managers Securities Investment Consulting (Taipei) Co., Ltd., a Securities Investment Consulting Enterprise regulated by the Financial Supervisory Commission of the R.O.C. Registered address: 34F, No. 68, Sec. 5, Zhongxiao East Road, Xinyi Dist., Taipei City 11065, Taiwan (R.O.C.), license number 2020 FSC SICE No. 025, Tel. +886 2 8789 2788. **In Singapore:** Provided by Natixis Investment Managers Singapore Limited (NIM Singapore) having office at 5 Shenton Way, #22-05/06, UIC Building, Singapore 068808 (Company Registration No. 199801044D) to distributors and qualified investors for information purpose only. NIM Singapore is regulated by the Monetary Authority of Singapore under a Capital Markets Services Licence to conduct fund management activities and is an exempt financial adviser. Mirova Division (Business Name Registration No.: 53431077W) and Ostrum Division (Business Name Registration No.: 53463468X) are part of NIM Singapore and are not separate legal entities. This advertisement or publication has not been reviewed by the Monetary Authority of Singapore. **In Hong Kong:** Provided by Natixis Investment Managers Hong Kong Limited to professional investors for information purpose only. **In Australia:** Provided by Natixis Investment Managers Australia Pty Limited (ABN 60 088 786 289) (AFSL No. 246830) and is intended for the general information of financial advisers and wholesale clients only. **In New Zealand:** This document is intended for the general information of New Zealand wholesale investors only and does not constitute financial advice. This is not a regulated offer for the purposes of the Financial Markets Conduct Act 2013 (FMCA) and is only available to New Zealand investors who have certified that they meet the requirements in the FMCA for wholesale investors. Natixis Investment Managers Australia Pty Limited is not a registered financial service provider in New Zealand. **In Colombia:** Provided by Natixis Investment Managers International Oficina de Representación (Colombia) to professional clients for informational purposes only as permitted under Decree 2555 of 2010. Any products, services or investments referred to herein are rendered exclusively outside of Colombia. This material does not constitute a public offering in Colombia and is addressed to less than 100 specifically identified investors. **In Latin America:** Provided by Natixis Investment Managers International. **In Chile:** Esta oferta privada se inicia el día de la fecha de la presente comunicación. La presente oferta se acoge a la Norma de Carácter General N°336 de la Superintendencia de Valores y Seguros de Chile. La presente oferta versa sobre valores no inscritos en el Registro de Valores o en el Registro de Valores Extranjeros que lleva la Superintendencia de Valores y Seguros, por lo que los valores sobre los cuales ésta versa, no están sujetos a su fiscalización. Que por tratarse de valores no inscritos, no existe la obligación por parte del emisor de entregar en Chile información pública respecto de estos valores. Estos valores no podrán ser objeto de oferta pública mientras no sean inscritos en el Registro de Valores correspondiente. **In Mexico:** Provided by Natixis IM Mexico, S. de R.L. de C.V., which is not a regulated financial entity, securities intermediary, or an investment manager in terms of the Mexican Securities Market Law (Ley del Mercado de Valores) and is not registered with the Comisión Nacional Bancaria y de Valores (CNBV) or any other Mexican authority. Any products, services or investments referred to herein that require authorization or license are rendered exclusively outside of Mexico. While shares of certain ETFs may be listed in the Sistema Internacional de Cotizaciones (SIC), such listing does not represent a public offering of securities in Mexico, and therefore the accuracy of this information has not been confirmed by the CNBV. Natixis Investment Managers is an entity organized under the laws of France and is not authorized by or registered with the CNBV or any other Mexican authority. Any reference contained herein to "Investment Managers" is made to Natixis Investment Managers and/or any of its investment management subsidiaries, which are also not authorized by or registered with the CNBV or any other Mexican authority. **In Uruguay:** Provided by Natixis Investment Managers Uruguay S.A., a duly registered investment advisor, authorised and supervised by the Central Bank of Uruguay. Office: San Lucar 1491, Montevideo, Uruguay, CP 11500. The sale or offer of any units of a fund qualifies as a private placement pursuant to section 2 of Uruguayan law 18,627. **In Brazil:** Provided to a specific identified investment professional for information purposes only by Natixis Investment Managers International. This communication cannot be distributed other than to the identified addressee. Further, this communication should not be construed as a public offer of any securities or any related financial instruments. Natixis Investment Managers International is a portfolio management company authorized by the Autorité des Marchés Financiers (French Financial Markets Authority - AMF) under no. GP 90-009, and a public limited company (société anonyme) registered in the Paris Trade and Companies Register under no. 329 450 738. Registered office: 43 avenue Pierre Mendès France, 75013 Paris.

The above referenced entities are business development units of Natixis Investment Managers, the holding company of a diverse line-up of specialised investment management and distribution entities worldwide. The investment management subsidiaries of Natixis Investment Managers conduct any regulated activities only in and from the jurisdictions in which they are licensed or authorised. Their services and the products they manage are not available to all investors in all jurisdictions. Although Natixis Investment Managers believes the information provided in this material to be reliable, including that from third party sources, it does not guarantee the accuracy, adequacy, or completeness of such information. The provision of this material and/or reference to specific securities, sectors, or markets within this material does not constitute investment advice, or a recommendation or an offer to buy or to sell any security, or an offer of any regulated financial activity. Investors should consider the investment objectives, risks and expenses of any investment carefully before investing. The analyses, opinions, and certain of the investment themes and processes referenced herein represent the views of the individual(s) as of the date indicated. These, as well as the portfolio holdings and characteristics shown, are subject to change and cannot be construed as having any contractual value. There can be no assurance that developments will transpire as may be forecasted in this material. The analyses and opinions expressed by external third parties are independent and does not necessarily reflect those of Natixis Investment Managers. Any past performance information presented is not indicative of future performance.

This material may not be redistributed, published, or reproduced, in whole or in part.

All amounts shown are expressed in USD unless otherwise indicated.

Natixis Investment Managers may decide to terminate its marketing arrangements for this fund in accordance with the relevant legislation

Natixis Investment Managers

RCS Paris 453 952 681

Share Capital: €178 251 690

43 avenue Pierre Mendès France

75013 Paris

www.im.natixis.com

MARKET INSIGHT

DOCUMENT INTENDED EXCLUSIVELY FOR PROFESSIONAL CLIENTS (IN ACCORDANCE WITH MIFID)