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Private Equity Managers Turn to Wealth Market for New Clients

After long dismissing the financial advisor business, alternative managers have changed their tune and recently made big bets in the space, launching their own private wealth divisions to draw new money from advisors across all channels, and create products that are more broadly accessible to individual investors.

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For many years, some of the most sophisticated asset managers in the alternatives space catered to the largest institutional investors in the world—pension funds, endowments and foundations, with hundreds of billions of dollars in assets. Think firms like Apollo, Blackstone, KKR and Hamilton Lane. For decades, that market was so lucrative—with clients allocating large slices of their portfolios to alternative investments and private equity—that the more retail-facing private wealth advisor market was not even on their radar.

But now many of these managers see a more sophisticated channel of distribution among retail advisors and have made big bets on the market, launching their own private wealth divisions, with staff dedicated to distributing to advisors across all channels, and creating products that are more broadly accessible to individual investors.

One of the rationales behind the shift is to take advantage of the growth in private wealth. The mass affluent and high-net-worth investor market accounted for about $177 trillion in assets as of 2020 and is expected to grow to $222 trillion by 2025, according to a PricewaterhouseCoopers report. That compares with about $63 trillion in institutional assets under management as of 2020, which is expected to grow to about $78 trillion by 2025.

These managers see more new ground to till on the retail side. Many institutions are fully allocated to alternatives, with an average 26% of their portfolios committed, according to a CoreData survey. Some endowments have allocations as high as 60%, according to UBS.

Meanwhile, retail allocations are in the single digits but growing rapidly, says Matt Brown, CEO of CAIS, a platform for alternatives.

“That's all new money,” Brown says. “That market opportunity is not lost on asset managers, so what they're doing is they are beefing up their sales teams and innovating products, structures that allow their funds and strategies to be more easily delivered into the wealth management space.”

Institutional allocations may be large, but that's a risk; they can easily be taken away from the managers, Brown says. Wealth management allocations are diversified among different advisors and the underlying investors, and therefore much stickier.

Neil Bathon, founder and partner at FUSE Research, says he has had more conversations with alternatives managers looking to get into the retail space in the past four to five months than in his entire career. FUSE Research found that traditional alternative assets under management at wirehouse firms increased 16.5% to a new high watermark of $200 billion in 2020, up from $175 billion in 2019.

“The evidence is there that there’s greater and greater uptake in these investment strategies for their high-net-worth clients, and [these managers] have to build out some sort of specialist support team to penetrate more fully.”

The Move Into Retail

These firms’ move into private wealth didn’t occur overnight. They first had to solve for some of the barriers preventing advisors from investing; many have created some innovative structures with lower minimums, no drawdowns, simplified tax reporting and regular liquidity windows.

“We looked at that market, and we faced the challenges of trying to solve for getting them exposure in a way that made sense,” says Stephen Brennan, head of private wealth solutions at Hamilton Lane. “So, what really has changed in the last number of years is creating some of these innovative structures that would allow investors to get fully invested at the time that they make their investments, as opposed to going through the capital call process of a traditional private equity fund, providing lower minimums that are certainly much lower than the $5 to $10 million minimums that you would have in a more institutional type product, things like simplified tax reporting."

In 2019, Hamilton Lane launched its Evergreen Fund platform, to bring private equity strategies to private wealth investors through open-ended funds. That includes its Global Private Assets Fund, available to non-U.S. investors, and its Private Assets Fund, a' 40 Act closed-end fund, available to qualified U.S. clients with a minimum $50,000 investment, launched in early 2021. The Private Assets Fund allows for monthly subscriptions and offers a quarterly tender to provide limited liquidity. It features 1099 tax reporting, and invests in a mix of secondaries, direct investments and co-investments in credit and equity across geographies, industries, vintages and general partners. The Evergreen platform now has about $2 billion in assets.

After the firm had the products in place to appeal to the broader audience, executives there realized they needed dedicated resources to market and sell the investments, as well as service the individual investor, Brennan says. So in early 2021, the asset manager penned a deal to acquire Denver-based liquid alternatives provider 361 Capital, Hamilton Lane's third acquisition in its 30-year history, a move that greatly expanded its distribution reach. The 361 team, which is now Hamilton Lane Denver, will be the distribution arm to the advisor market.

One of the biggest challenges in penetrating the advisor market, Brennan says, is building brand awareness.

"We've largely been an institutional firm for our 30 years," he says. "And so while we're very well known in the institutional market, we're much less known in the private wealth space."

Blackstone was an early mover in the private wealth space. The $881 billion alternatives manager was quietly building its private wealth solutions for several years before moving to raise its visibility among retail advisors in 2017 by building out a dedicated sales, service and marketing organization to bring its alternative products to advisors and their clients. The company has about 160 employees dedicated to the private wealth segment, with plans to double that over the next few years, according to Bloomberg.

Apollo, the $481 billion firm, created a business unit dedicated to retail investors last year, and hired Howard Nifoussi, a former managing director at Goldman Sachs, as the head of U.S. wealth management distribution.

"I joined the firm back in February of last year, and really was charged with leading the U.S. wealth build out," Nifoussi says. "This is a global initiative for the firm led by Stephanie Drescher, and she's been hiring in other regions as well. So the launch started about a year ago. We've gone from one or two employees, including myself to about 30 individuals here today in global wealth."

In December, Apollo announced its acquisition of Griffin Capital, a privately held alternative investments asset manager in Los Angeles. The move adds 60 retail-facing distribution professionals and hundreds of distribution agreements. It also adds about $5 billion of AUM in products focused on individual investors, including interval funds in the real estate and credit space.

Apollo recently set a target at its investor day of raising $50 billion-plus of organic capital for its global wealth business over the next five years.

Apollo recently launched its first nontraded business development company, Apollo Debt Solutions BDC, with more than $1 billion in assets under management. The fund, managed by an affiliate of Apollo, invests in directly originated assets, including debt securities, and is aimed at the broader investor market.

The firm also has traditional qualified purchaser products with long lockup periods in private equity, private credit and hybrid structures that it has already started to launch on major bank and wirehouse platforms.

"This is an organization that had grown almost 40-fold from an asset perspective over the prior 12 years or so," Nifoussi says. "There was just lots of growth happening in the world of institutions and other strategies, so wealth just wasn't a strategy that frankly was at the front and center. That has clearly changed here. The democratization of finance is increasing the accessibility of alternatives and we want to be at the forefront. And based on our broad-based platform and capabilities, we feel we can deliver many different types of solutions to investors regardless of where they fit in the spectrum."

KKR has been in the private wealth space since 2012; the firm now has approximately $50 billion in private wealth assets, and a dedicated global wealth team of more than 35 executives, including sales, product strategies and marketing roles. But the firm has been ramping up those efforts more recently. The firm just appointed Todd Builione, president of KKR Credit and Markets, as its global head of private wealth, and it expects to more than double the size of its private wealth team in 2022.

Private wealth now accounts for 10% to 20% of new capital raised annually by KKR, and the firm expects that to increase to 30% to 50% of annual fundraising over the next several years.

“Today, KKR’s private equity, credit and real estate investment strategies are accessible for individual investors through a suite of KKR-sponsored and third-party continuously offered registered funds,” the firm said in a statement.

In 2021, KKR launched the KKR Real Estate Select Trust (KREST), a ’40 Act– and ’33 Act–registered REIT that provides access to KKR’s private commercial real estate platform globally across equity and credit investing. In 2020, it offered the KKR Credit Opportunities Portfolio (KCOP), a ‘40 Act fund designed to provide exposure across KKR’s strategies in leveraged and private credit with a single commitment. Also last year, KKR teamed up with iCapital to launch the iCapital KKR Private Markets Fund (iKPMF), a ’40 Act fund managed by iCapital that offers exposure to KKR’s private equity strategies. KKR also acquired a minority stake in iCapital.

“Lower expected returns and yields in the public markets are forcing private wealth investors to turn to the private markets to meet their financial objectives,” a KKR spokesperson said, in a statement. “Innovative investment vehicles are broadening the access of alternative investments to a much larger number of private wealth investors, while also reducing the hassle factor associated with investing in alternatives. Technology is streamlining the process for investors to allocate to alternatives.”

Technology Platforms Pushing Things Forward

These alternative managers say that technology platforms like CAIS and iCapital are making the move into private wealth easier.

Whether it's technology that is built from scratch or purchased as an off-the-shelf component, iCapital has been focused on removing operational bottlenecks so that the entire advisor experience of an alternative asset transaction, from research to execution, is comparable to the experience of buying a mutual fund.

These platforms have revolutionized the traditional feeder-fund structure, says Hamilton Lane’s Brennan. A feeder fund pools capital commitments of investors and “feeds” such capital into a master fund, run by the institutional asset manager, which may have minimums as low as $50,000. The master fund is oversees and allocates the money. Those same investors in the feeder fund might not have access to the direct fund because of the high minimums.

“A private markets manager can create a feeder fund through one of these platforms and raise lots of dollars from the whole number of high-net-worth investors,” Brennan says. “And then that feeder fund is really the only limited partner that they have in their fund. And the platform handles all of the servicing of those underlying feeder fund investors. So some of that structural shift has really caused people to realize that it's not as challenging as it maybe had been historically to tap into the high-net-worth market.”

iCapital, for instance, works with 200 of the largest alternative GPs in the world; it has $105 billion in total assets invested through the platform, used by more than 8,500 advisors.

CAIS works with over 4,400 advisor firms/teams that have transacted over $15 billion in volume since its inception. The company declined to provide asset manager numbers, except to say that it has seen a 36% year-over-year increase in the number of alternative investment funds available.

CAIS has designed a platform that includes a curated menu of alternative investments at reduced minimums and places a lot of emphasis on matching the advisor's needs for their client with the right investment. It also provides independent research and due diligence, automated subscription documents and custodial integration to streamline the investment process for the advisor.

“The manager lists their fund on our platform; our platform's already connected to trillions of dollars of RIA wealth assets,” says CAIS’ Brown. “Now it's becoming visible to that community, and the advisor can now buy the fund across our platform. And so the effort and energy of the manager is substantially reduced to reach this audience.”

Aaron Hodari, chief investment officer and a managing director of Schechter, a $2.2 billion wealth management firm in Bloomfield Hills, Mich., says it’s platforms like CAIS’ that have allowed his firm to scale and grow its client base.

“These platforms coming to you with access, diligence, research, streamlined operations; it's made the process of us investing in alternatives, both from an operational and research perspective, easier,” he says.

Schechter started to incorporate more alternatives into client portfolios about five years ago, and Hodari says the pace has accelerated significantly. Client allocations to alternatives are about 20% on average at his firm. And Schechter is winning new clients because of it; he says one of the main things prospects are attracted to is his firm’s use of alternatives.

“Our clients also appreciate the diversification of not just being in stocks and bonds,” Hodari says. “It's not the majority, but there are some investors who come to us and say, ‘I don't want to own anything in the stock market. But I want return. And I want some level of lower volatility, and bonds can't provide that in this environment.’ The alternative marketplace has been a place that, for those type of investors, we've been able to find solutions that solve a need, an actual need.”

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