

# Five Questions to Ask When Evaluating Private Market General Partners

You've decided that private markets are right for you and now want to know, "How do I find a great GP?" First, look for a sustainable, two-way relationship. As the managers of private market funds, GPs oversee complex investment transactions, such as capital calls, distributions and redemptions across a variety of private equity strategies. As such, finding a GP, who is transparent about investment decisions, is mission critical to the success of advisors and investors.

Private markets investing requires a long-term commitment of capital to realize potentially significant returns, so advisors and investors should explore everything from a GP's past performance to ways that they monitor a portfolio's ongoing performance. It's also important to keep in mind that, while past performance does not indicate future returns, asking questions about how a GP has managed their previous investments and the relationships they've created with existing investors may help you decide if that GP is a good fit. By carefully evaluating GPs from the outset, advisors and investors can thoughtfully construct portfolios that meet their investment objectives. To get you started, here are five questions that you should consider asking prospective GPs.

## WHAT YOU SHOULD KNOW:

- ▶ Private market investments typically have long-term investment horizons, so it's important that advisors and investors plan to build long-term relationships with general partners (GPs) and their teams.
- ▶ GPs have unique fee structures and different ways of valuing assets that investors should explore in initial conversations to determine how that may affect their investment objectives.
- ▶ During initial due diligence investors should discuss liquidity management with prospective GPs to avoid surprises down the road.

- 1 Team and Track Record
- 2 Trust Building
- 3 Net Return Basis
- 4 Liquidity Management
- 5 Portfolio Construction

## 1 What Can You Tell Me About Your Team and Track Record?

When evaluating GPs, we believe the single most important question you can ask is, “What can you tell me about your team and track record?” The team is the foundation of [private markets investing](#), perhaps even more so than in public markets. When investing in public markets, advisors and investors have access to a trove of market data. Conversely, when investing in private markets, both advisors and investors are highly dependent on their GP partners because private company performance data is not publicly available. So, effective communication across their team is a good measure of how they may communicate that data with you. Additionally, GPs who have mechanisms in place for the full and transparent flow of information with their colleagues and GP partners may have an enhanced ability to execute investments. This is why it’s critical that you ask the investment team questions about their:

- Professional backgrounds
- Contributions to the team
- Investment philosophies, tenure and track records
- Internal organizational and communication tools and processes

But don’t stop there. You will also want to ask about how individual team members are compensated to determine whether the right incentives are in place. It almost goes without saying – but make sure to benchmark the historical performance of the GP you’re considering to their competitors as well as public market returns (more on that below). Benchmarking will help level set your expectations. When all is said and done, maximizing potential returns benefits both advisors and investors, so asking these questions can set you up for success.

## 2 How Does the GP Build Trust?

Trust is fundamental to any business relationship. In the private markets, trust is built through the repeated execution of mutually beneficial investments – a GP’s success is your success, and vice versa. It can take years to build trust and credibility. So, when evaluating GPs, it’s important to ask both qualitative and quantitative questions to determine how you may best work together from day one to year ten, and beyond.

Here are some qualitative questions that you can ask to evaluate prospective GPs:

- How do you build trust among colleagues throughout your firm, as well as externally?
- How do you align limited partners’ (LPs) goals with your areas of expertise?

How do you communicate with LPs in the event of poor performance?

Some quantitative questions may include:

- How many LPs have you worked with in the past five to ten years?
- How many LPs no longer work with you and why?
- How many years have you been managing investments?

Understanding how GPs build trust with their team and work productively with third parties may also help you understand what to expect when it comes to achieving your goals. Why? GPs are just one of the [players](#) in the broader private markets ecosystem, and there are many aspects to consider. In addition to working with colleagues at their firm, GPs also interact with financial intermediaries such as commercial banks, advisors and underwriters. The ways in which GPs manage these relationships may tell you how they might handle yours. So, asking these questions may help you establish a sense of confidence and set you up for a successful long-term relationship.

### 3 What Can I Expect on a Net Return Basis and How May It Affect Investment Objectives?

When it comes to private markets, it's not about what you earn, it's about what you keep. At the end of the day, what looks good on paper is different from what you pocket. For this reason, you should ask questions that help you understand potential profitability on a net return basis. Net returns, or total returns, are what you keep after interest, capital gains, dividends, realized distributions and fees.

Each private markets investment opportunity has its own unique fee structure. There are some general fee categories – such as management fees, performance fees, etc. – that may have an impact on net returns. And there may also be some deal-specific fees. This is why it's so critical that investors ask probing questions about previous deal fees as well as the GP's overarching philosophy concerning fee structures. Some questions you may want to ask include:

- How do you analyze the risk / return targets of individual investments?
- How do individual investments impact the overall portfolio's risk / return targets?"
- How are your fees calculated for a particular [private equity](#) strategy? And why?

### 4 How Effectively Does the GP Manage Liquidity?

When investing in private markets, advisors need to consider their investors' liquidity needs. Of course, we all know that private markets are much less liquid than public markets. So, as you evaluate GPs, remember that their ability to manage liquidity and their track record for selecting the right deals are both important. As you have discussions about liquidity with GPs, here are some of the questions you should consider:

- How do you manage incoming assets and how quickly do you deploy them?
- Are you consistently able to meet fund redemption requirements?
- What is your track record of deploying capital and managing liquidity?

### 5 How Does the GP Construct Portfolios?

The old adage, "Change is constant," should be something that every investor takes to heart. As we've previously mentioned, private market investments typically have long-term time horizons. So, not only should good GPs be thoughtful about constructing their portfolios, but they should also regularly analyze their performance to ensure that each deal aligns with their initial risk / return targets. For example, how do you minimize cash drag, or the holding of cash, instead of targeting higher returning assets? After all, your overall objective is to maximize potential net returns for you and your investors. In order to do this, you will need to have capable GPs on your side who have the right tools at their disposal. Some questions that you can ask to assess this capability include:

- Is your firm's deal flow sufficient to provide a wide array of quality investment opportunities?
- What options are available for rebalancing investor portfolios?
- What is your investment philosophy as it relates to overall portfolio construction?

Whether an advisor or investor is new to the world of private markets investing or has considerable years of experience under their belt, it's always advisable to conduct exhaustive due diligence when evaluating GPs. This will help ensure that your investment objectives have the greatest potential of being met.

[To learn more about private markets, visit Hamilton Lane's Knowledge Center.](#)

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