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Investment funds

How private investors can move into private equity

Until now, investment funds were strictly for professionals only. But now there are new paths for investors—provided they have the necessary seed capital.

In recent years, few asset classes have grown faster than private equity. According to Preqin, an analyst firm, almost 4000 investment funds were active worldwide in the middle of the year, collecting a total of 981 billion dollars from investors. By comparison: At the beginning of 2015, only 1400 private equity funds were working with about 400 billion dollars. One reason for the boom is the low interest rate policy of the central banks. Investors are put off by the negative yields on bonds and are looking for alternatives. At the same time, they fear a slump on the stock exchanges. “Investors notice that private equity has performed well,” says Christopher Beales, analyst at Preqin. 78 percent of investors assumed that private equity will do just as well or even better in the coming twelve months. The private equity industry is advertising with double-digit yields—however, there is one big catch: The global market is dominated by professional investors from insurance companies and pensions funds, because the minimum investments are in the millions. Small investors have been left out in the cold so far—but with the digital revolution, the market is experiencing a shakeup. For over a year, the virtual platform Moonfare has been offering direct access to private equity funds starting at 100,000 euros—and is apparently growing very rapidly. “Assets under management currently amount to around 150 million euros, and by the end of the year this will grow to more than 200 million. The number of investors will have reached about 500 by the end of 2019. We currently have 400 investors and 3000 users who have signed up for our services,” co-founder Alexander Argyros told Handelsblatt. The digital business model bundles customer orders and enables direct investments in funds such as KKR, Permira, Cinven, Oakley Capital, or EQT. These billion-dollar investment funds mainly buy unquoted companies or take minority stakes, and after some years of restructuring and expansion, the assets are sold at a higher price or floated on the stock exchange.

Enormous differences

In an interview with Handelsblatt, the creators of Moonfare announced a broadening of their business model. “Right now we are expanding the product portfolio with an important element. For the first time, we are offering access to a so-called secondary fund. It buys older investments from other funds at a discount, which is usually around 20 percent,” said Steffen Pauls, ex-KKR top manager and CEO of Moonfare. Industry analysts believe the secondary fund is Lexington Capital Partners. Moonfare did not want to comment on this. Secondary funds with mature corporate investments work well in a downturn when investors want to divest from private equity investments. Investors have to be careful that the proportion of private equity shares in their portfolios is not too high in the event of a slump on the stock markets with falling share prices. For example, if the statutes do not allow more than ten percent of private equity in the entire allocation, the investments have to be reduced. Furthermore, a secondary fund avoids the disadvantages of traditional funds. These invest in the early years before the first returns from sales come after an average of four to six years. With a secondary fund, on the other hand, returns flow directly. Private equity should never be the main focus of an overall investment portfolio, but relatively high portions between ten and twenty percent are no exception these days. The disadvantage is that the investment must stay in place for a comparatively long time. “Private investors need to be aware that private equity investments require a long-term investment horizon," says Marcus Storr, Head of Alternative Investments at Feri, an asset management company in Bad Homburg near Frankfurt. "At the same time, the long-term capital commitment leads to an attractive expected return. Ultimately, the decisive factor is access to and selection of the right funds." Indeed, the yield differences are enormous—between 1991 and 2018, the funds in the top quarter of the market yielded an average of 17.6 percent per year, whereas the lowest quarter only achieved 3.3 percent. "Hardly any other asset class has as wide a gap between the best and the rest as the private equity class," states a study by the consulting firm Mackewicz & Partner.

Access to top funds

The digital asset manager Liqid also offers a way to invest in private equity funds. "Although private equity is still not very well known among private investors, we have noticed a strong increase of interest in the past few months," says Christian Schneider-Sickert, cofounder and CEO of the digital asset management company Liqid. "Right now we are about to close our second fund of private equity funds with a target size of 50 million Euros, which is twice the size of the first one, in just half the time." It could offer clients access to top funds such as Apollo, Bain, Cinven, CVC, EQT, Oakley, Permira, and Triton. Anybody not wishing to rely on digital innovations can also buy funds of funds such as RWB or shares in investment companies such as Deutsche Beteiligungs AG (DBAG) or the finance corporations Blackstone, Carlyle, and KKR. These have long stopped investing solely in private equity, and they also invest in infrastructure and non-bank loans. They cover the entire field of "alternative investments", including real estate. The Internet-based business model of Moonfare is also introducing two further innovations in the coming year. The first will be a virtual marketplace for all private equity shares of customers in order to increase the liquidity of the asset class. The second will provide access to a venture capital fund, which does not invest in established companies but provides venture capital for start-ups and young, growing companies.

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