Schroders

Private Assets

Institutional Investor Study 2022

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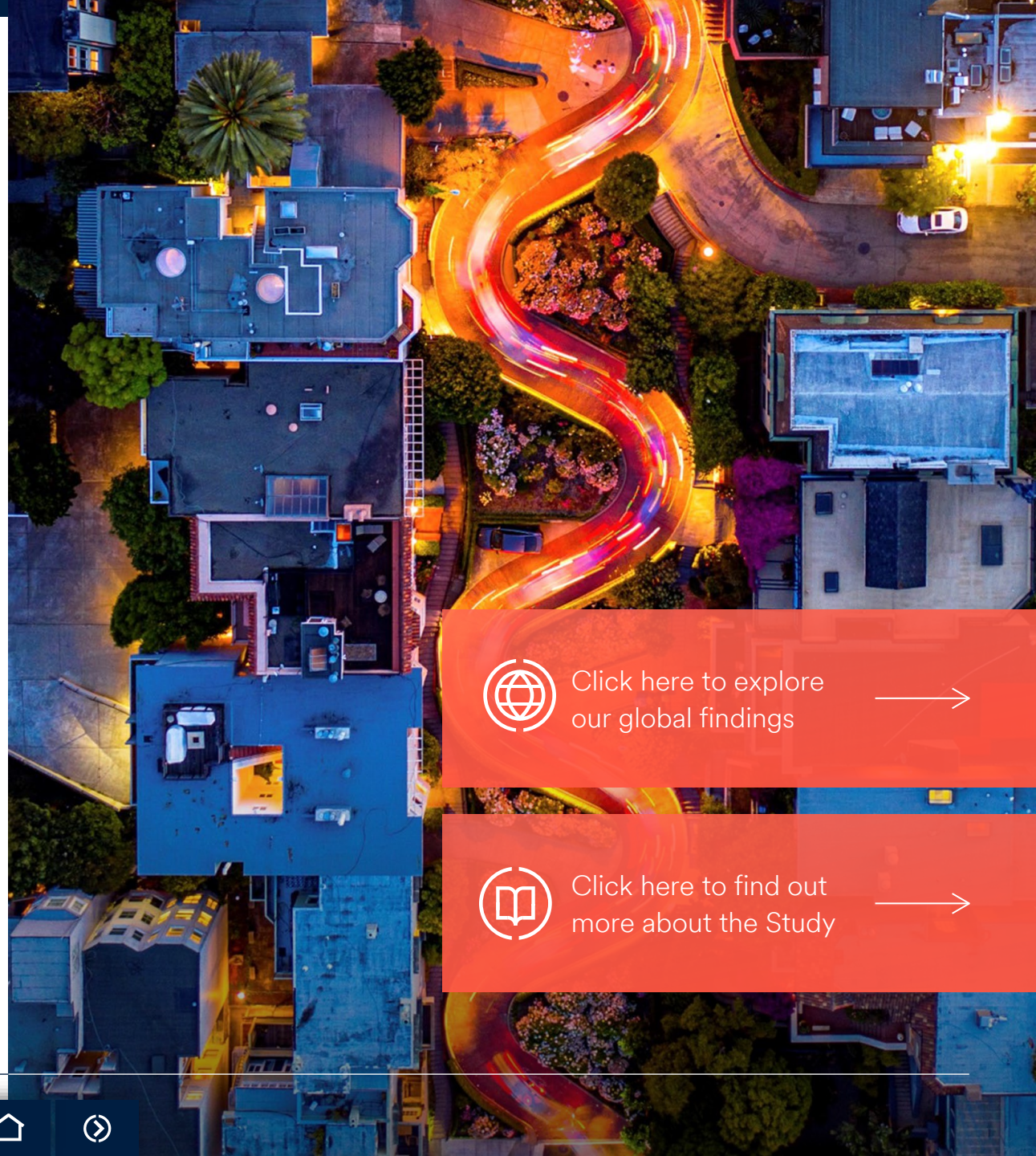
About the Study

The Schroders Institutional Investor Study analyses the investment perspectives of some of the world's most influential investors, every year.
The study seeks to distil the key goals and concerns of 770 global institutional investors, and covers the investment landscape, private assets, and sustainability.

The respondents represent a spectrum of institutions, including corporate and public pension plans, insurance companies, official institutions, private banks, endowments, and foundations, collectively responsible for US$27.5 trillion in assets.

This year's Study was conducted in March 2022, and as such, the responses were collected in a starkly different risk environment than we and our investors face in the final quarter of the year. The responses explored in the following pages should be viewed and considered in light of that markedly changed context.

Even so, the longer investment horizon of private assets means the continuation of the long-running series - and what it can illustrate over time - we feel is warranted and valuable. Certain key themes, such as the comparative resilience of private markets, remain undimmed. Some challenges are as pertinent now as they ever have been.



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Click here to find out more about the Study

Key insights

Click on the panels to view more information on each of our key global insights

How to navigate:

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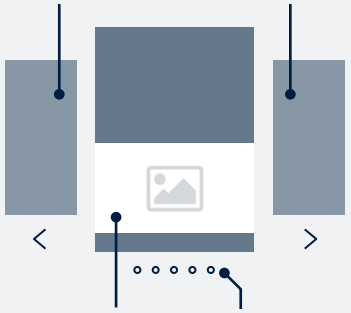

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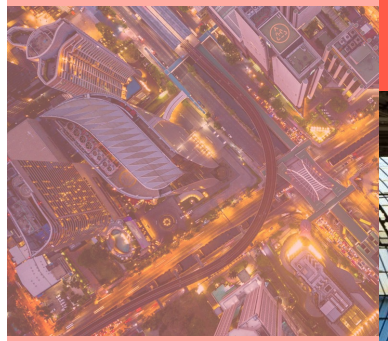
Click on a circle to quickly jump to the corresponding global insight

1

The motivations given for investing in private assets generally remain unchanged over time. Returns and diversification are seen as more important than lowering volatility.

2

1



2

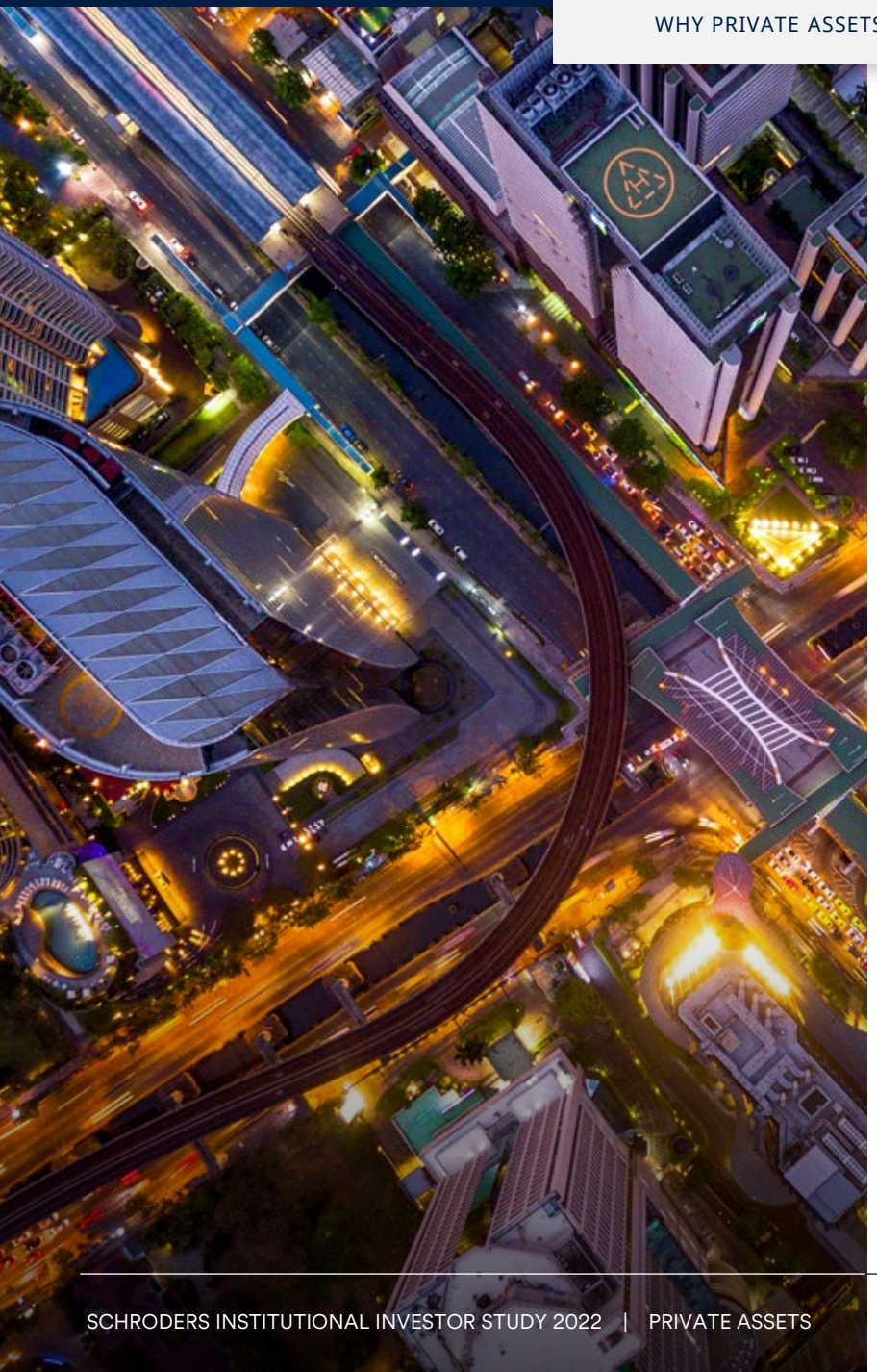
Infrastructure and other real assets are set to play a greater role in investment portfolios. 65% of investors planned to increase exposure to infrastructure equity over the next 12 months.

3

2

3

ESG and impact considerations are set to grow in importance for many investors. 44% said it was important or very important for managers to integrate ESG considerations into their strategies.



Introduction

At the time the study was conducted, the destabilising factor of war in Ukraine was already in play. Market events since then have clearly made the issue of liquidity more complicated. The UK's gilt market disruption in October had profound implications for a large number of institutions. No doubt, attitudes in the short-term have changed.

That said, the longevity of the study means we have the benefit of establishing longer-term patterns. From these, we can see that motivations for investing within private assets have in general not changed over time. In March, the study indicated that allocations to liquid equity and bond markets were expected to decline, while private asset allocation expectations had remained steady. Returns and diversification have been consistently prioritised by investors more than lowering volatility.

If we afford ourselves a look beyond short-term market turmoil - which as proponents of patient, long-term investment strategies, we believe we should – we expect the longer-term trends found by the study to be re-established. The majority of respondents to the 2022 Schroders Institutional Investor Study in March were eager to add to various types of private assets.

Infrastructure and real estate were particularly of interest. With inflation the primary concern for investors in most developed markets, any potential insulation from inflationary pressures was highly sought-after, and we have no reason to believe this has changed.

As has been the case for the several years, the importance of environmental, social, and governance (ESG) factors also continues to rise. Indeed, this year's study indicated that the challenging backdrop is spurring a high proportion of responding investors to ramp up allocations to investments with sustainability and impact dimensions.

We have long held the view that ESG and impact priorities align well with many areas of private assets. Further, we contend that certain, highly specialised ways to engage with these priorities, are accessible only via private assets.

As ever, some areas of private markets remain overlooked and – in our view – underappreciated. Many warrant more attention from institutions, especially in the current environment.

Over the next few pages, we will explore these points, and many others. We look at the key themes identified by the Schroder Institutional Investor Study 2022, and explore the risks and opportunities with which institutional investors are most preoccupied.

Asset allocation and future expectations

Despite significant market disruption this year, asset allocation expectations for private assets appear to have changed little overall.

Historic levels of inflation, central bank and central policy actions, and the war in Ukraine have led to public market declines. This has in some instances left investors with higher comparative private allocations (the denominator effect), and many investors have adopted a “wait and see” stance. We have seen evidence of slowing fundraising in the past few months.

Overall, however, the study indicated long-term investor expectations are for private asset allocations to remain steady at 13%. This was the finding when allocations to developed equities and fixed income were expected to cool from last year.

Most respondents expected to see allocations to rise in private equity – especially in venture and growth strategies – as well as in real estate and infrastructure equity. Appetite for insurance-linked securities and securitised products appeared comparatively muted, in spite of a material increase in respondent recognition that private assets can be used to generate a steady income.

While investors in March did not expect to change asset allocations significantly, overall portfolio return expectations had already shifted downwards noticeably when compared to last year. They may have slipped further in the intervening months.

“

As we look to the coming year, we believe investors will be well served by adopting a pragmatic and selective approach. We feel it should come as no surprise that 2023 will be challenging, and those most proactively engaging with the challenges will perform best.

Last year we highlighted the risks that exuberant fund-raising, fuelled by Covid-induced stimulus, posed to vintage year performance. We pointed to late-stage venture/growth capital investments as among the most exposed in this regard . It therefore came as no surprise that these strategies saw significant corrections in 2022.

Added to the reversal of Covid-induced stimulus, the world now faces an energy crisis caused by the Russia-Ukraine conflict. We believe the Western world will experience a deep recession in in 2023.

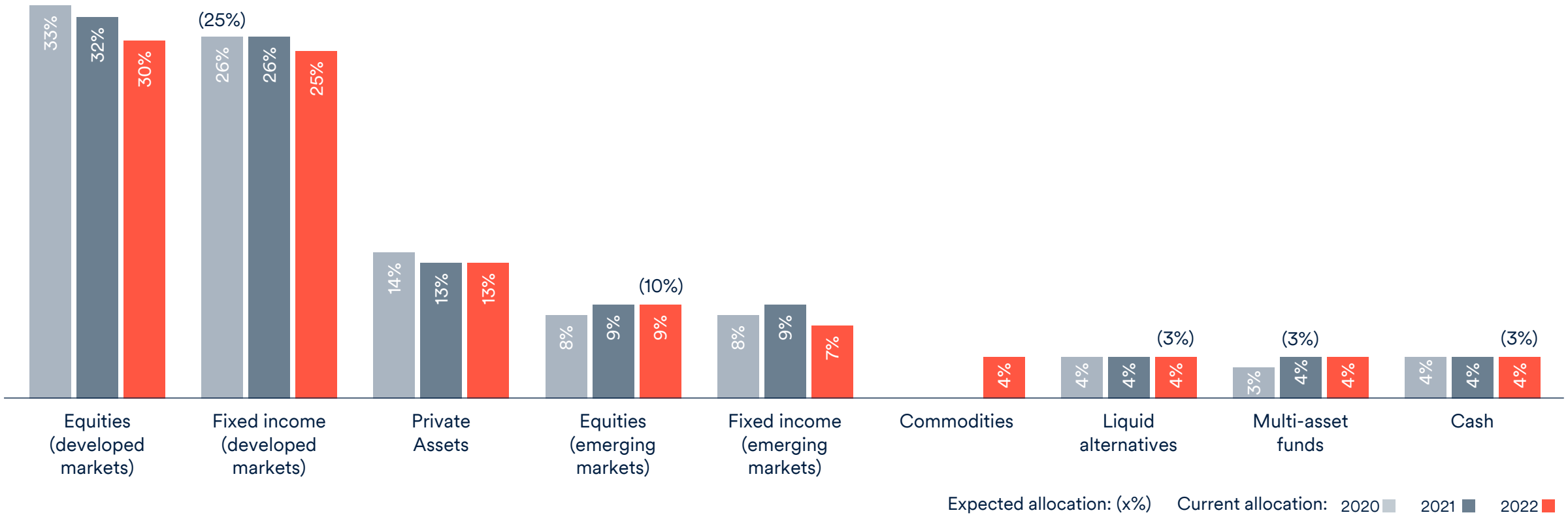
As ever, we believe that investors should continue to adhere to a long-term strategy and strong investment discipline. We believe investors should ensure they maintain a steady investment pace for fund investments, diversification across less correlated strategies, and focus on strategies that are not subject to a major dry powder overhang.

Nils Rode

Schroders Capital Chief Investment Officer

Asset allocation and future expectations

Q. Approximately what percentage of your institution's portfolio is currently allocated to each of the following asset classes? Current and expected allocations



Percentages may not add up to 100% due to rounding.

Regional shifts: North America calling

The most noticeable shift in geographic terms was a planned higher allocation to North America. There was a marked uptick in interest in this region, with 37% of respondents expecting to add more exposure, versus 24% in 2021. There was also a drop in the proportion of respondents planning to decrease allocations, from 17% to 12%.

Europe was the second most popular region, with 30% of investors planning an increase, versus 24% in 2021. However, more investors expected to reduce allocations to the region: 17% of investors expected European allocations to fall, compared with 12% in 2021.

Allocations to India and China were expected to fall for a significantly larger cohort than in 2021: 17% of investors expected to decrease their allocations to the region versus only 7% last year. By extension, 72% of investors in 2021 believed they would increase or maintain allocations to China and India. This had fallen to 63% of respondents answering the same way in 2022.

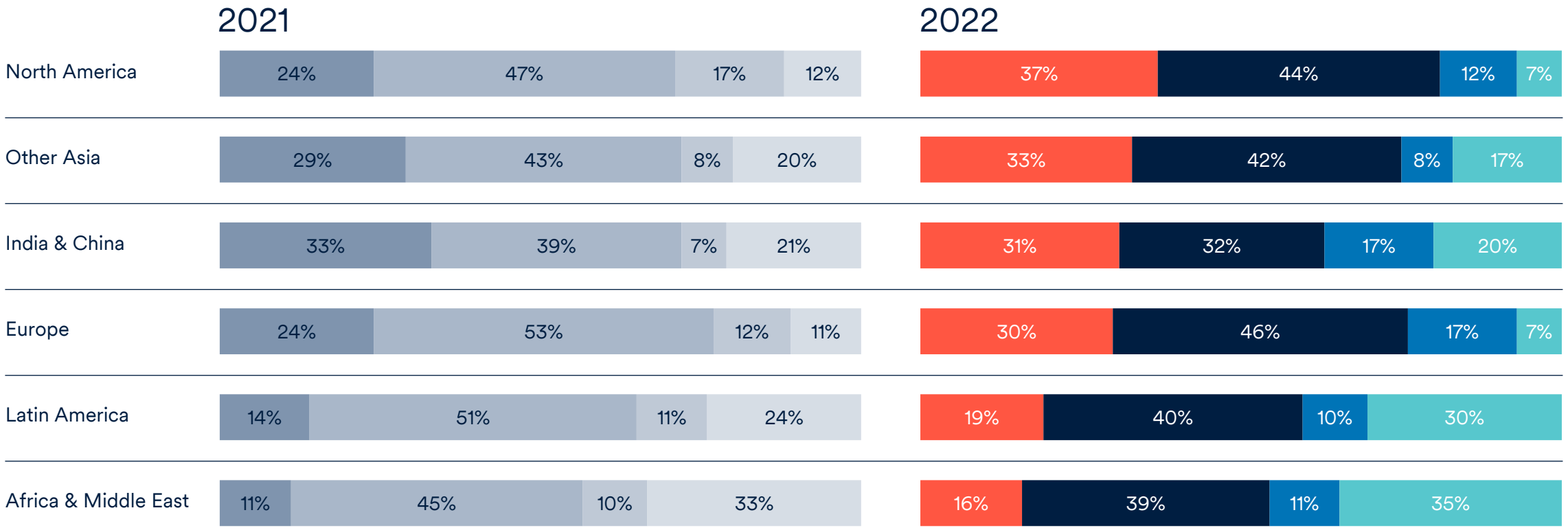
A third of investors indicated that they would increase their exposure to the Asia Pacific region outside of India and China, potentially seeking to gain access to similar long-term trends – attractive demographics and economic growth – while also diversifying geographically. There are also indications that Latin America, Africa, and the Middle East regions are becoming more popular.

"These regional shifts are likely to be indicative of a more prevalent decline in risk appetite. Investors may be looking to limit geopolitical and currency risk by favouring US investments – traditionally seen as a safe haven. A similar trend emerged in 2012 during the European debt crisis.

Emily Pollock
Client Director, Solutions

Regional shifts

Q. Over the next 12 months, how will you adjust your geographic exposure in private assets?



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Why private assets?

Diversification and higher returns have long jockeyed for position as the primary reason investors allocate to private markets, according to this study. These motivations have, in general, not changed over time.

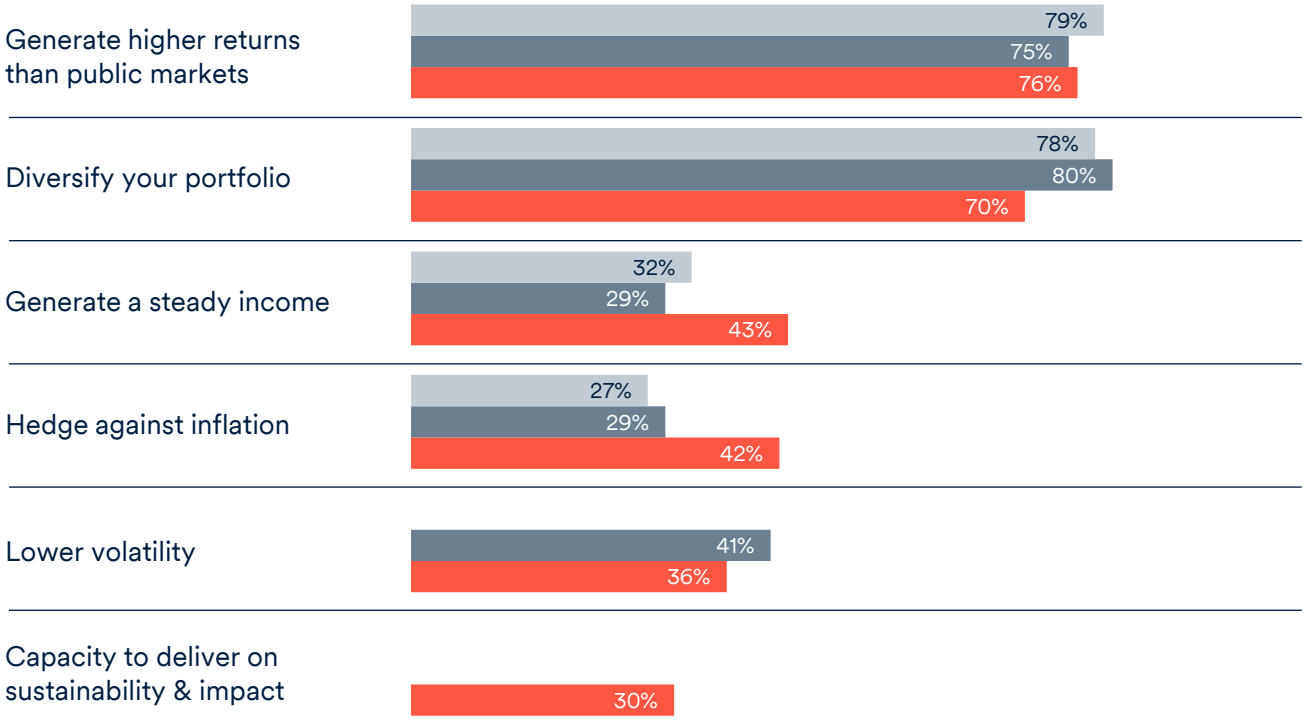
Last year, diversification was ranked as the most important benefit, with investors increasingly recognising the benefits of widening exposure beyond public markets. More than that though, a high number of respondents - 39% - stated in 2022 that they were seeking to secure a complexity premium from private assets. Complexity premium is the return generated when highly specialist skill sets can be deployed in an appropriate operational investment scenario.

In 2022, investors again cited the potential for higher returns. With inflation rising and geopolitical and macroeconomic fears hitting listed markets - and where investors that have not faced liquidity bottlenecks - alternative sources of return are clearly highly prized. More than three quarters of respondents – 76% – said they use private assets chiefly for return benefits, while 70% cited diversification[1] as the main reason for investment in private markets.

An interesting development in the latest study was the notable rise in investors recognising the income-producing qualities of some kinds of private assets. More than two in five (43%) of those asked cited steady income as an important or very important reason to for private market allocations, compared with only 29% saying the same last year.

In addition, 42% of investors recognised the ability to find solutions to inflationary concerns in private assets, versus only 29% in 2021.

Q. To what extent are the following factors reasons for you to invest in private assets?



Option 'None of the above' not displayed.
On a scale of 1-5 (1 being not important at all and 5 Very important. % Important (4+5)

1. Respondents were asked to rank each factor on a scale of 1 to 5, with 1 as 'not at all important' and 5 as 'very important. Our ranking uses all those that selected 4 or 5 for each factor.

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In recent years we have noticed a clear consolidation of manager relationships within the institutional market. Large institutions increasingly want to work with fewer partners across a broader capability set. For many, this has extended into multi private asset solutions.

Communications and technology have made the world a smaller place, but in many respects, this makes asset and security selection even harder. Investors increasingly need help sorting through the abundance of information. Maintaining a portfolio, particularly in private markets, can also be burdensome, with capital calls, distributions, currency, and reporting cycles to consider. Investors want efficiency.

Performing due diligence and, more crucially, gaining access to the best opportunities poses another challenge. We often talk about access-restricted managers, but here the issue is less about high minimums and more about securing any capacity at all.

Investors are well advised to be diversified across many dimensions, including strategy and asset type.

David Seex
Global Head of Private Asset Solutions

The scope of our study has grown in tandem with investor understanding of the details and complexities involved in private assets investment.

The top two concerns amongst respondents were virtually unchanged from last year, with 58% citing each of low transparency and high fees. This is despite recent work by regulators such as the US Securities and Exchange Commission to improve transparency in the private equity sector[2] , and investor-led initiatives to shed light on the fees paid to managers in private assets.

Valuations were clearly on investors' minds, with 54% of respondents concerned or very concerned about pricing. That said, while this is higher than last year (47%), the number of concerned investors remained below the levels seen in 2020 (57%). It is far below the near-70% of respondents that singled out valuations as a worry in 2019.

Illiquidity remained a key factor that deters private asset engagement, with 53% of investors responding they were concerned or very concerned about it. This is a rise of 11 percentage points from last year's study.

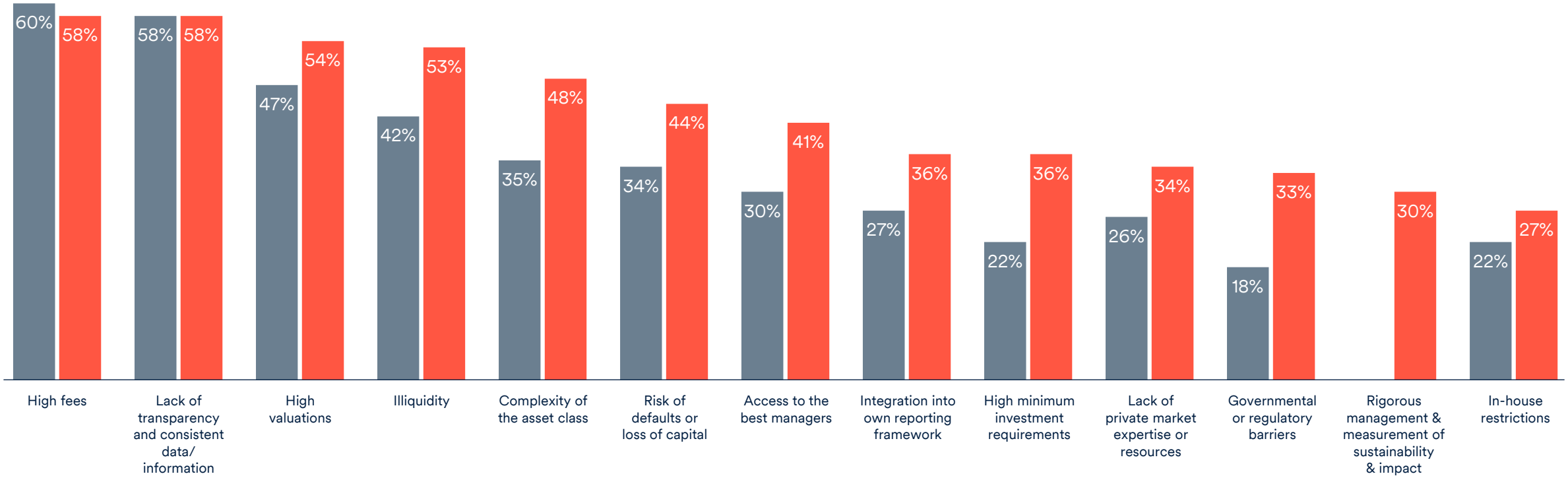
We are seeing a long-term trend in the steadily growing proportion of respondents stating that reporting and regulation is a challenge for them when investing in private markets. This trend makes intuitive sense and is not related to the market environment.

The complexity of private markets is a material issue for almost half (48%) of respondents. Complexity has not, in our view, increased specifically, but it is likely more investors are investing in complex solutions. This tallies with the comment on trends highlighted by our comments from David Seex, Global Head of Private Asset Solutions.

2. 'SEC Proposes to Enhance Private Fund Investor Protection', SEC press release, 9 February 2022. https://www.sec.gov/news/press-release/2022-19

Investors' key concerns

Q. In your experience what are the main challenges of investing in private assets?



Please rate on a scale from 1-5, where 1 = Not concerned at all and 5 = Very concerned. % Concerned (4+5).

Venturing in search of growth

As interest in private equity has grown over the past decade, investors have diversified within the asset class to explore how different types of private equity strategy can benefit their portfolios.

When the study was conducted, venture/growth capital was the most popular of the three sub-categories, ahead of buyouts and secondaries. Three quarters of investors have an allocation to buyout investments, but 82% have committed to venture or growth capital funds.

The least popular sector was secondaries: 68% of respondents said they had an allocation. Those that do not may be missing out on the benefits of the rapidly developing secondaries market, and the potential exposure to long-term value creation in targeted private companies.

The study indicated considerable popularity of real estate equity and infrastructure equity, with 61% and 65% respectively seeking to increase allocations. Debt in real estate and infrastructure is attracting slightly less interest, with around half of respondents considering a higher allocation.

82% have allocation of some sort to venture/growth

68% have allocation of some sort to secondaries

"

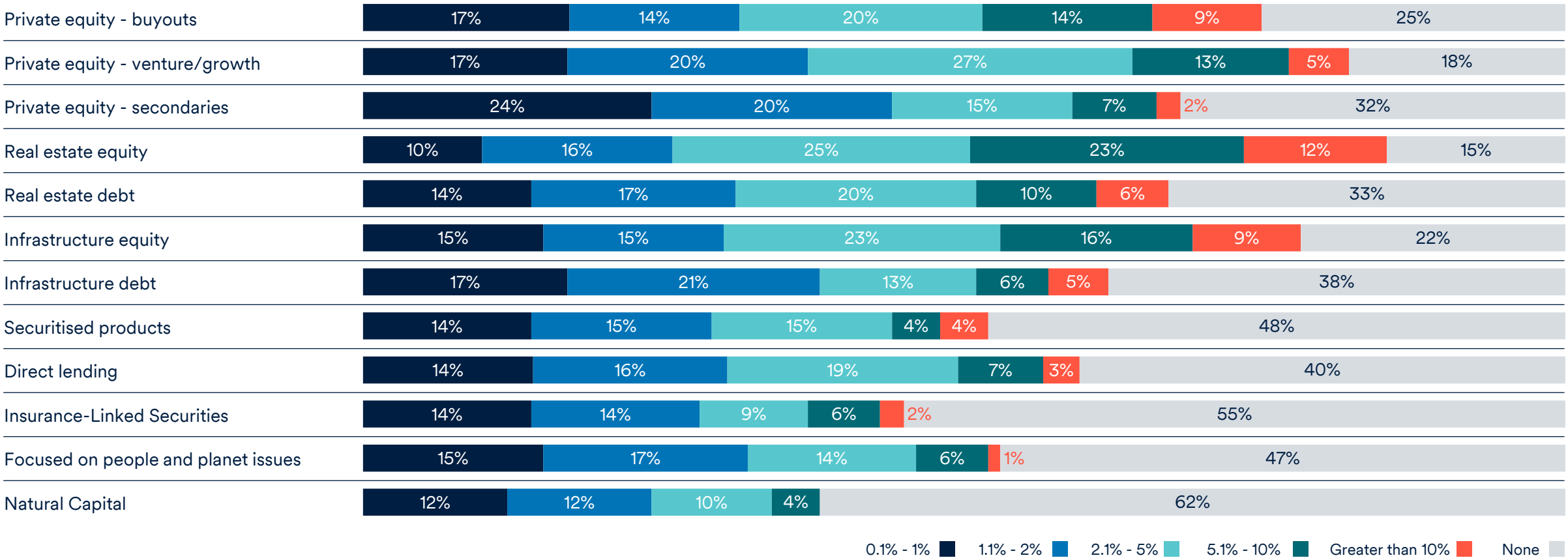
Where we are in the cycle will impact all markets, including private equity and secondaries. What's important when you look at transactions today is finding companies that can endure a down market and a weaker broader economy. Ultimately, a good company that can grow in a difficult environment, bought at a reasonable valuation, can still generate returns that we think will outstrip public markets.

We expect sponsors to continue pursuing GP-led transactions. Our view is that every private equity manager will try to do one to two GP-led deals in their older funds. That dynamic is not likely to change. The need for liquidity for investors will become a bigger challenge if there is a recession, because all other exits become more challenging. GP-led secondaries are quite complicated transactions that allow sponsors to double-down on their favourite companies. It allows the value creation journey to continue for a number of years.

Christiaan van der Kam
Head of Secondary Investments, Schroders Capital

Venturing in search of growth

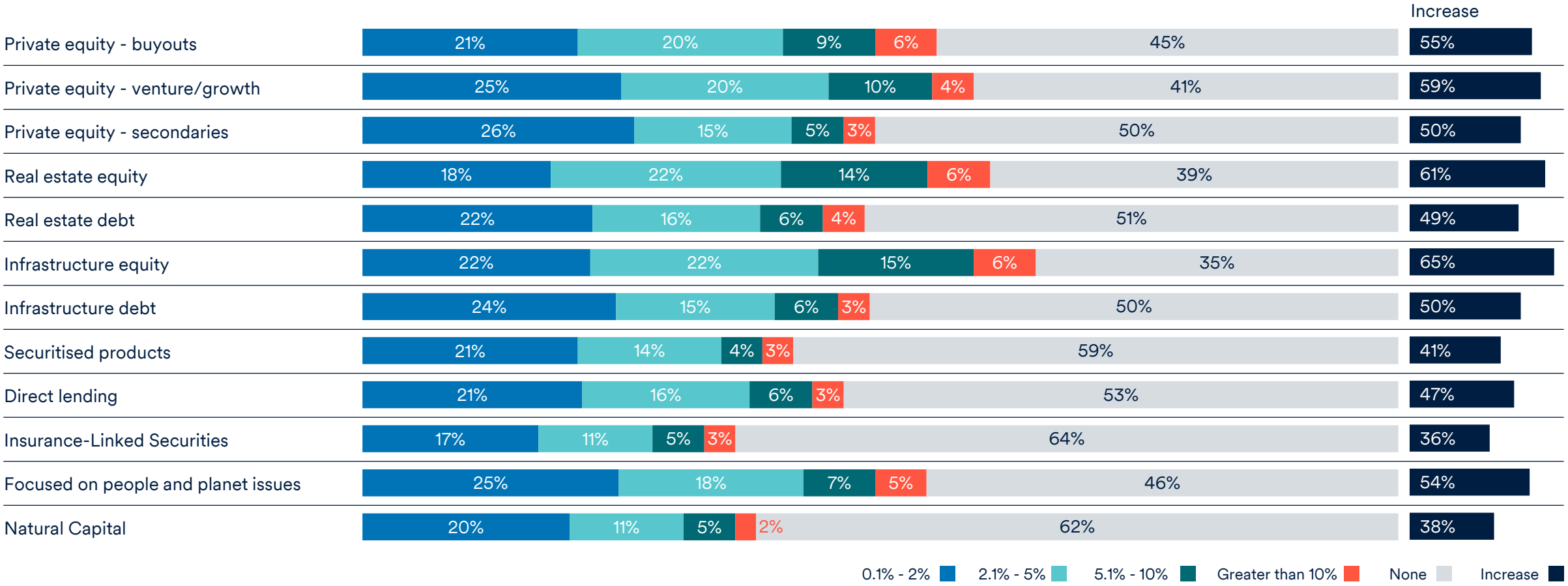
Q. What proportion of your entire investment portfolio do you allocate to these categories of private assets?



Percentages may not add up to 100% due to rounding.

Venturing in search of growth

Q. Over the next 12 months, by what percentage, if any, do you intend to increase your allocation to the following categories of private assets?



Percentages may not add up to 100% due to rounding.

Securitised assets and insurance-linked securities

At the other end of the interest scale are securitised assets and insurance-linked securities (ILS), which are being widely overlooked by investors, according to our study.

Just over half of respondents have an exposure to securitised assets, and for most this is less than 2% of their portfolio. Only 41% expect to increase their holdings over the next 12 months. For ILS, even fewer respondents say they expect to increase their exposures.

We believe this is a missed opportunity, especially in the context of income demand and a clamour for diversifying assets. The asset classes of ILS and securitised are superbly positioned for investors seeking uncorrelated assets and regular income.

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This is an interesting environment. Clients and their managers, across most products/strategies, are challenged by the unfamiliar landscape. Market conditions, including inflation and the retraction of central bank accommodation, haven't been seen in nearly 40 years. Other factors - lower productivity, populism, more persistent supply chain disruption and climate change - are all creating more persistency of inflation. With the general pillars of finance: consumer, corporations and banks, even starting this journey from a healthy and de-leveraged position, navigating markets requires a new play book.

"The triple threat of inflation, rising discount rates and an ever more expensive US dollar have created a global environment of rising volatility, uncertainty and greater idiosyncratic risk. We've seen investors pause and take stock. Ultimately, as it is understood that these conditions are much more persistent than was expected, as these great expectations are dashed, we see diversification, lower duration (lower interest rate exposure), and safe, higher quality, durable cashflows playing a much larger role in portfolios.

Michelle Russell-Dowe

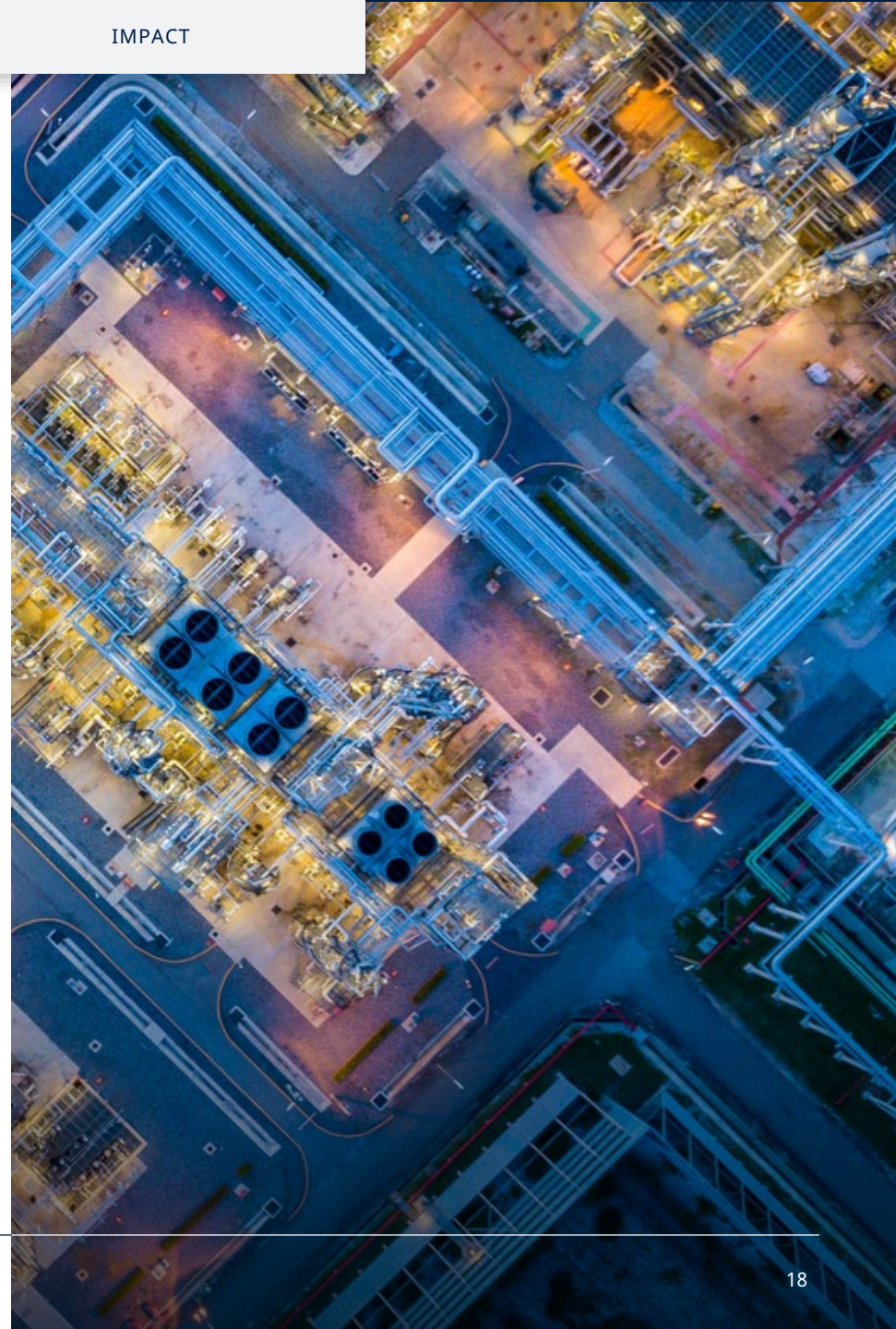
Global Head of Securitised Products & Asset-Based Finance

"

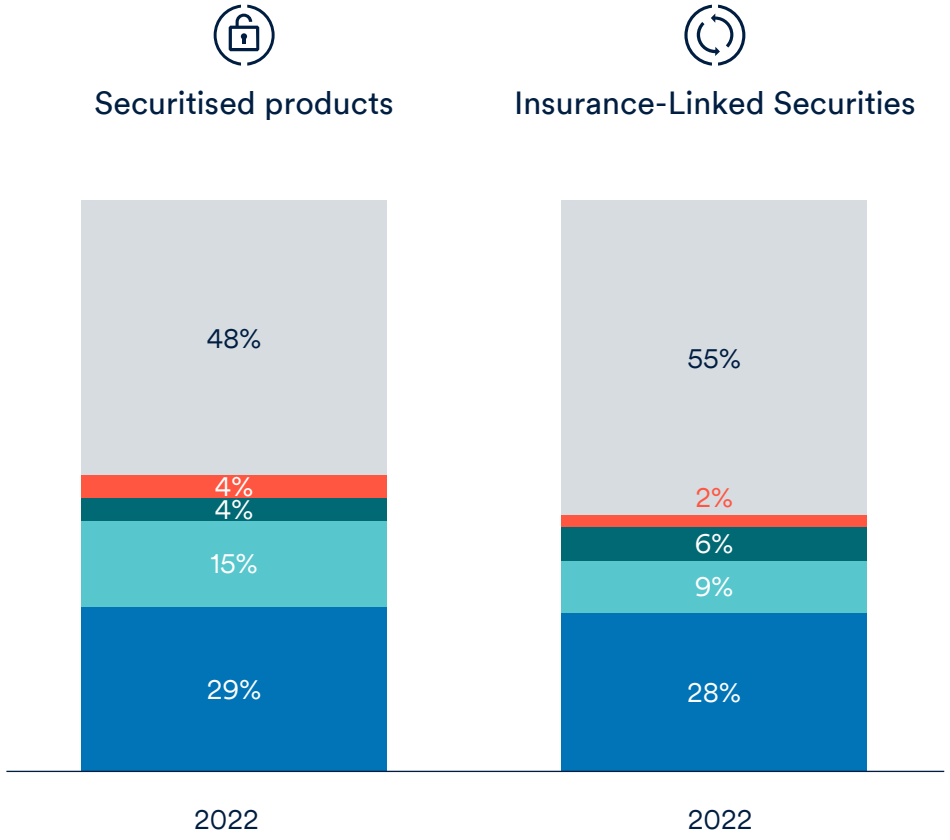
ILS's core attraction for investors is, and will remain, the provision of broadly uncorrelated investments that can enhance portfolio performance. The reinsurance cycle is independent of the credit cycle and is not subject to same recession risks. As floating rate instruments, most ILSs are also not subject to interest rate duration or rising rates in the same way as many other assets. We also factor inflationary expectations into our models to ensure we are underwriting business at the right price.

However, ILS also align very well with ESG considerations. The insurance and reinsurance market globally has large, but ultimately limited, capital pools that protect against extremely large loss scenarios. These scenarios - including natural catastrophes and man-made events - cannot be absorbed by the insurance and reinsurance markets alone. This represents an enormous addressable investment opportunity with a tangible social benefit.

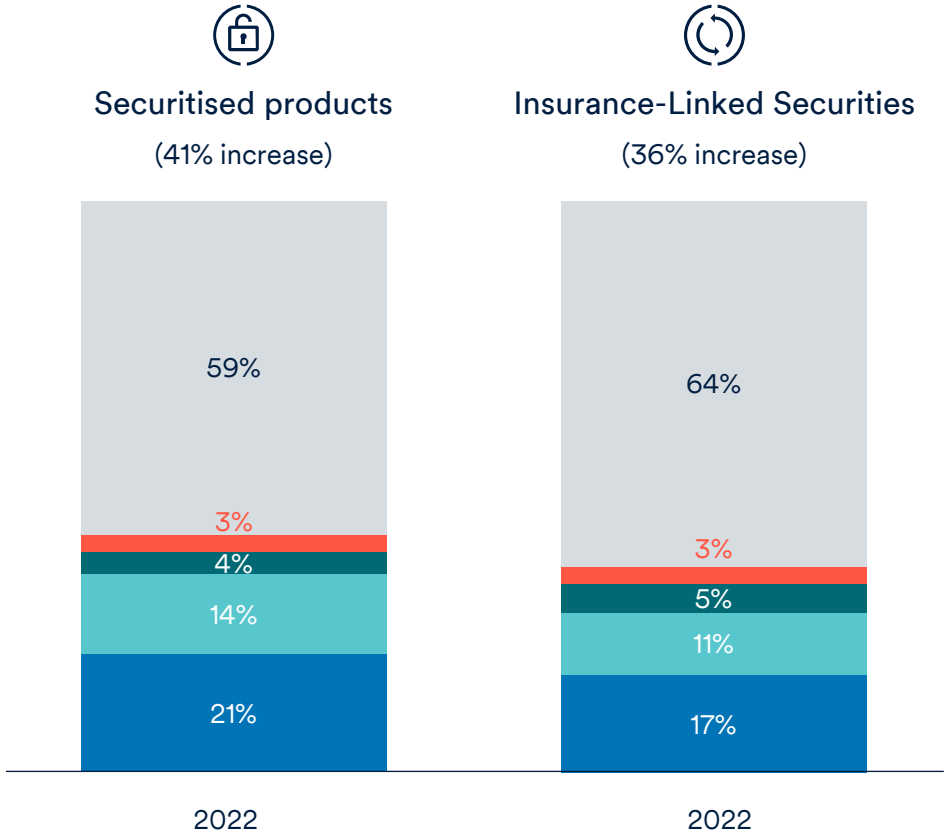
Stephan Ruoff
Global Head of Insurance Linked Securities



Q. What proportion of your entire investment portfolio do you allocate to these categories of private assets?



Q. Over the next 12 months, by what percentage, if any, do you intend to increase your allocation to the following categories of private assets?



None
Greater than 10%
5.1% - 10%
2.1% - 5%
0.1% - 2%

ESG in private assets: Making an impact

As environmental, social and governance (ESG) issues have become embedded in the management of listed assets, in particular equity, investors have begun to explore how to ensure the same information is available for private assets.

Just over half of respondents already have an allocation to impact investments, while 54% were keen to increase their exposure.

Linked to this, we also asked respondents about their investments in 'natural capital' – a segment previously referred to as forestry and agriculture. This reflects a steady increase in interest in this vital sector as our understanding grows about its importance to global sustainability efforts.

Currently, 38% of investors have some exposure to natural capital and the same proportion expected to increase this. We would expect interest to grow with the advent of the Taskforce on Nature-related Financial Disclosures, which aims to improve the availability, consistency, and quality of natural capital data in the same way the TCFD has done for climate finance[3].

"

More asset managers are moving into ESG and impact investing. As they do, it is important to differentiate between those that are driven to it by regulatory requirements (for example, the Sustainable Finance Disclosure Regulation), and those that really look at it as competitive advantage. The latter can turn sustainability challenges into opportunities.

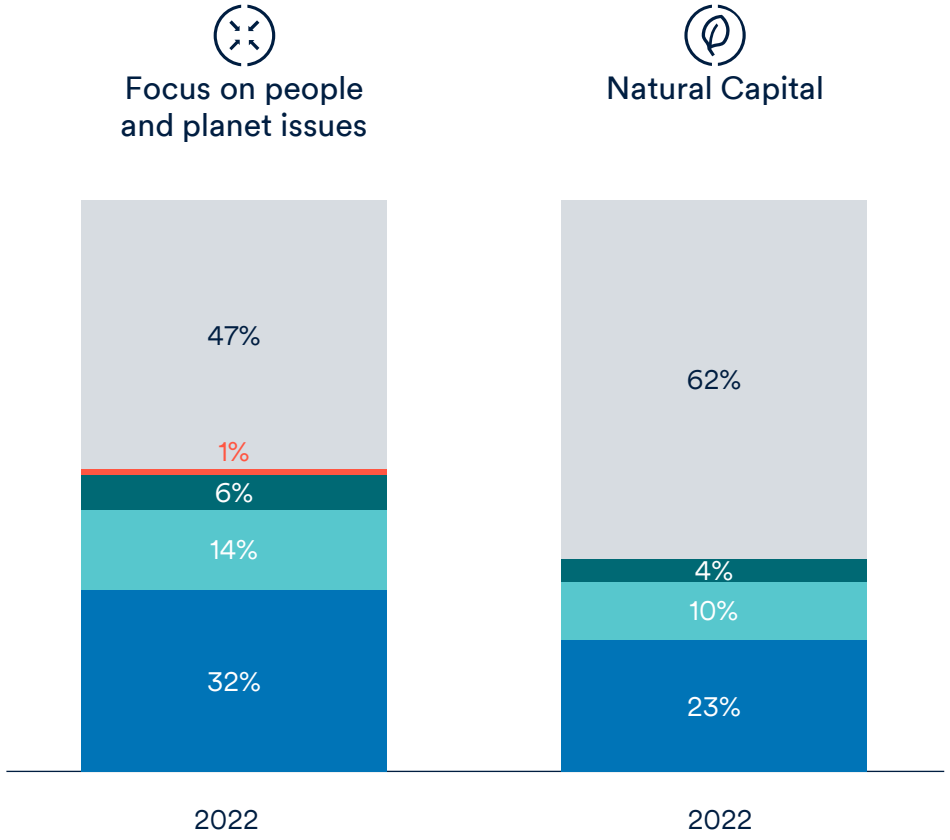
We believe investors seeking positive ESG outcomes should channel their resources towards achieving positive, sustainable, and impactful returns. This means stating and sharing objectives with investors, and being clear when difficulties are encountered in achieving them. Transparency and disclosure are key fiduciary responsibilities. Aspirations don't go very far, and must be backed by key performance indicators, monitored during the life of the investment.

Selecting and engaging with investee companies that lead in sustainable practices is one of the building blocks of our private market investment framework.

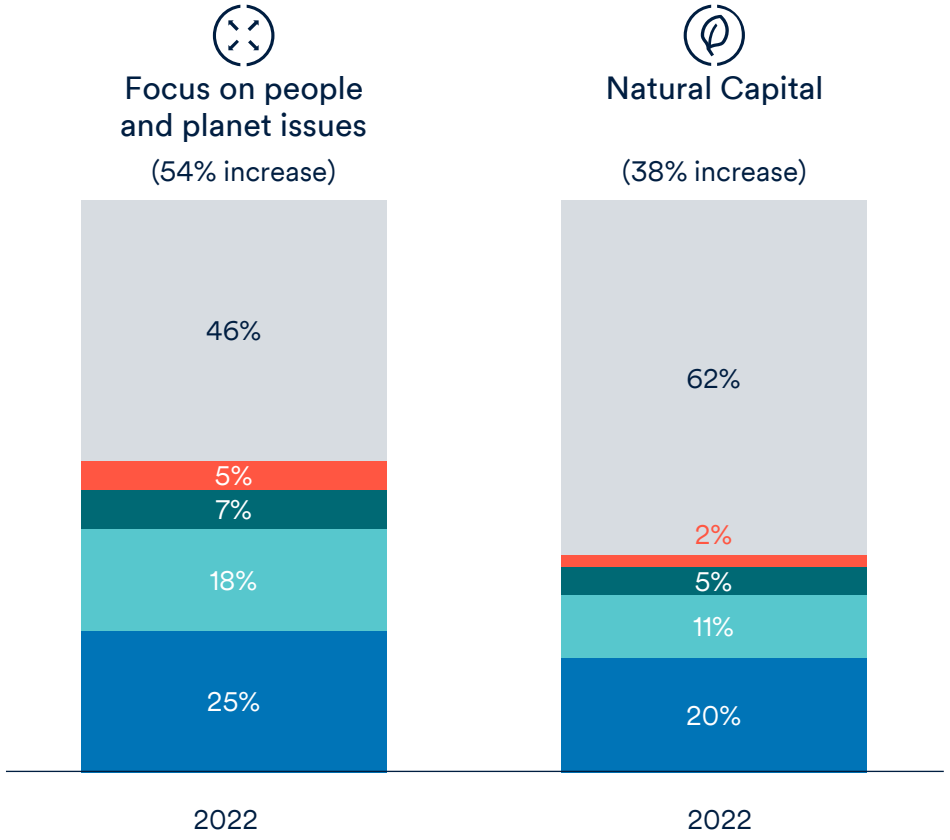
Maria Teresa Zappia
Head of Sustainability and Impact

3. See the TNFD's framework, available at https://framework.tnfd.global/

Q. What proportion of your entire investment portfolio do you allocate to these categories of private assets?



Q. Over the next 12 months, by what percentage, if any, do you intend to increase your allocation to the following categories of private assets?



None
Greater than 10%
5.1% - 10%
2.1% - 5%
0.1% - 2%

Conclusion

Private assets, while often referred to as 'alternatives', are increasingly a core part of institutional portfolios, providing vital sources of uncorrelated income and absolute return.

As investors into these assets grow more sophisticated and at ease with the idiosyncratic nature of some subsets, more opportunities are opening up. At the same time, challenges remain – not least the supply of cohesive and comparable data.

This has been a year of numerous and complex challenges, from which private assets have not been immune. However, many of the headwinds facing private market allocations in the short term are more technical in nature than fundamental. In our view, the fundamental justifications for private assets remain resilient to short-term factors.

Through fostering collaboration and innovation, we believe investors can meet adversity with pragmatism and real optimism by leveraging the plentiful opportunities within private assets.

At the same time, more and more institutions are investing with purpose beyond just a financial return. We believe private assets can be a force for good and help investors enact positive change, while also enhancing their investment portfolios.

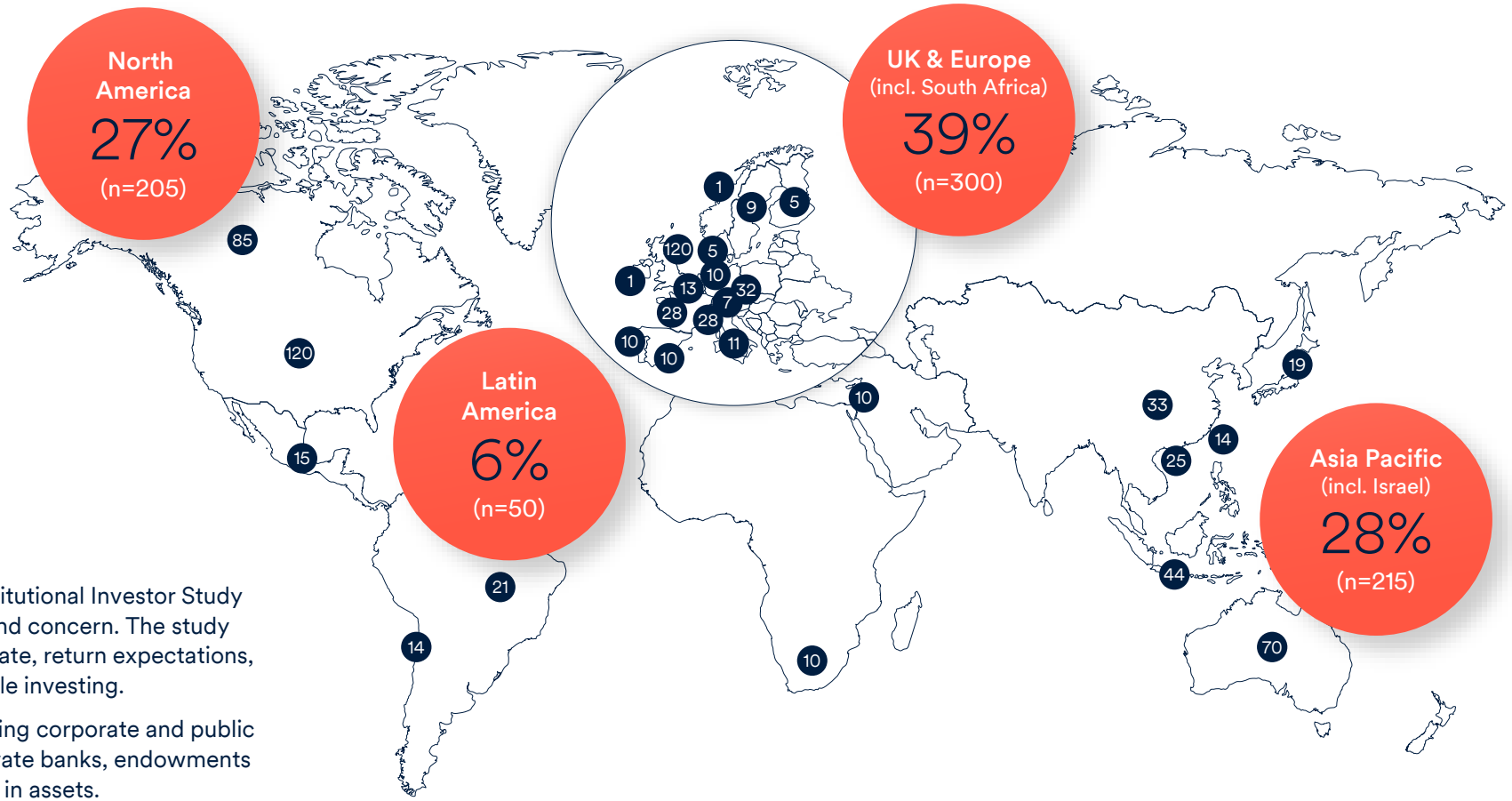
About the Study

Worldwide institutional respondents

770
institutional respondents

28
locations worldwide

US$27.5
trillion in AUM



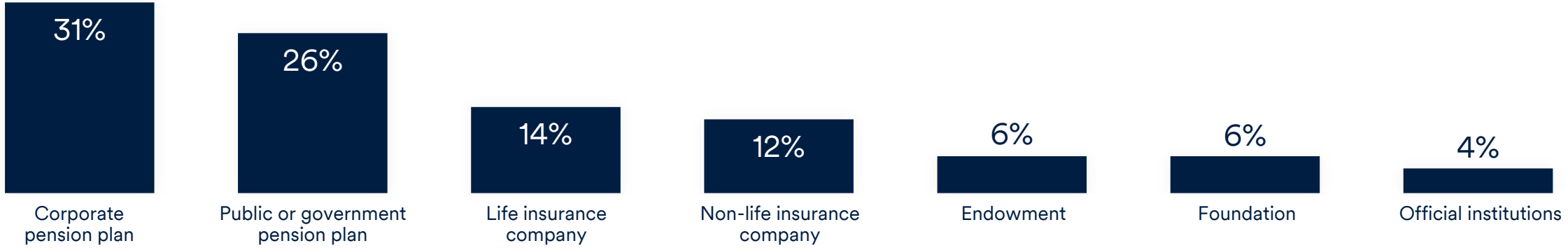
Schroders commissioned CoreData to conduct the sixth Institutional Investor Study to analyse the world's largest investors' key areas of focus and concern. The study captures views on the macroeconomic and geopolitical climate, return expectations, asset allocation and attitudes to private assets and sustainable investing.

The respondents represent a spectrum of institutions, including corporate and public pension plans, insurance companies, official institutions, private banks, endowments and foundations, collectively responsible for US$27.5 trillion in assets.

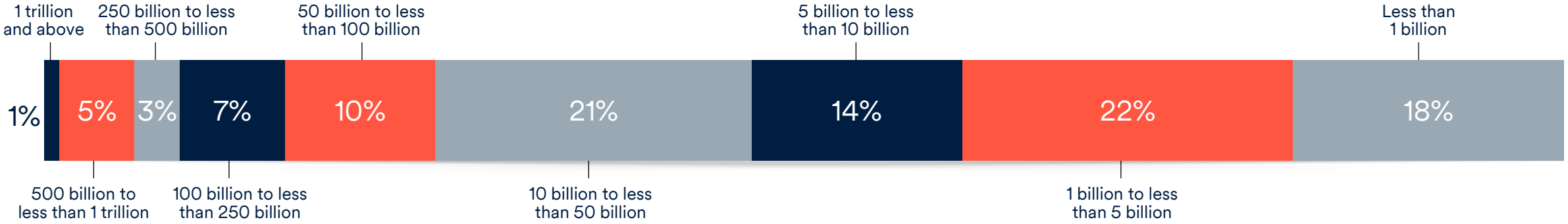
The research was carried out via an extensive global survey during March 2022.

About the Study

Breakdown by institutional type



Assets under management (US$)



Percentages may not add up to 100% due to rounding.

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