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Kristian Zimmermann
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Skin in the game

It goes without saying that 2022 didn't serve most investors quite as well as they may have liked, with heightened volatility dominating the year. However, those with broader horizons who embraced private markets were a little luckier.

In essence, private equity managers use their experience and expertise to create value in the companies they invest in by taking ownership in high potential businesses and transform them by funding initiatives, creating efficiencies, and shaping strategic direction with the goal of increasing revenues and profitability, as well as investor returns.

As MLC Asset Management co-head of private equity Kristian Zimmermann explains, this is because unlisted markets have several distinct characteristics which public markets lack.

Firstly, the private market is larger and the companies within it are highly diverse, he says.

"These companies are also at varying stages of maturity. The opportunity set is vast, with many companies delaying listing on an exchange or not pursuing an initial public offer (IPO) at all, so there are interesting opportunities that are simply not available in the public market at all," Zimmermann says.

Traditionally an asset class reserved for institutional or ultra-high-net-worth investors due to the investment requirements and lack of liquidity, these opportunities are now available for retail investors too. MLC Asset Management's private equity capability is now more accessible with the launch of the MLC Global Private Equity Fund in October 2022. Investors gain access to the fund with \$20,000 and, while the asset class and the fund remain illiquid, the fund aims to provide limited monthly redemptions, seeking to offer 5% quarterly.

While simply having an exposure to private equity can be a benefit to retail investors from a diversification perspective, one of the other things investors benefit most from is the fact that private equity is highly active, he says.

"Private equity managers have a greater ability to influence both the operation and management of a business, to drive change across a company," Zimmermann explains.

Thirdly, despite what the name of the asset class might suggest, Zimmermann says private equity managers have access to a tremendous amount of detailed, internal data on companies before any investment decisions are made.

"Due diligence can take months and managers will routinely spend millions of dollars to better understand a business before making an investment... We believe in private markets it is still possible for managers to have a true informational edge when making those decisions," he says.

"In other words, the highly active and hands-on nature of private equity investing compels change and the potential for significant improve-

ment in investee companies. That's not something even the largest investors in listed companies can ordinarily claim. Of course, there are situations where activist-investors do succeed in provoking change in listed companies, but such occurrences tend to be the exception."

Zimmermann says that MLC Asset Management's private equity team focuses on mid-cap companies, primarily those with an enterprise value between \$500 million and \$2 billion.

"We believe there is an attractive opportunity in this space to influence and grow business value and revenue through active involvement compared to the large buyout space where businesses tend to already be managed much more professionally and where as a result more of the value creation tends to come from increased levels of leverage," he explains.

The mid-cap space provides ample deal flow, he adds, including proprietary off-market transactions. Again, this compares to the large buyout space where most deals take place via highly competitive auction processes, meaning the prices paid in the mid-cap space can be more attractive.

MLC Asset Management likes to partner with specialist managers with a strong track record, with Zimmermann saying their deep sector expertise enables them to work more closely with the companies that they buy, making operational improvement or entering new markets. There must also be a strong alignment of interests in order for MLC Asset Management to consider a partnership or investment, meaning that there must be real skin in the game for private equity managers and the management teams of the companies that are acquired.

As for investing in the current market, Zimmermann notes there are some challenges, with volatility, inflation, rising interest rates, the potential for a recession, and continuing geopolitical uncertainty taking their toll. However, he is confident that MLC's approach helps to buffer against the risks.

Taking rising interest rates as an example, Zimmermann explains that while debt is becoming more expensive and somewhat harder to access, this is less of an issue given MLC's focus on the mid-market space where debt requirements tend to be lower. The managers the firm partners with also don't employ overly aggressive debt levels, he adds.

Another characteristic of the fund's approach that helps protect against these external factors is that it seeks out investments in companies with a sustainable competitive edge – those that have attributes increasing their ability to increase revenues through market cycles, with business models that cannot be easily replicated and deliver a core product or service.

"These types of non-discretionary products

tend to be relatively resilient even when economic times are tough," Zimmermann says.

"Our approach to investing hasn't really changed all that much in the current market environment. We continue to invest in what we believe are great companies and managers."

And Zimmermann acknowledges that MLC Asset Management's profile as a private equity manager has remained relatively low despite its decades of experience, calling it "the best kept secret in Australia" – but there's a reason for that.

"We aren't a high-profile PE manager, because until now MLC's private equity capability has mainly been a sleeve of MLC's diversified superannuation portfolios, with a focus on delivering returns for investors," Zimmermann says.

However, this consistent flow of superannuation contributions has enabled the team – which currently manages over \$4 billion – to hone its craft over the years, gaining a track record of investing through market cycles and building a reputation for being a reliable partner, which Zimmermann says is critical to accessing opportunities.

Private equity investing is an exciting opportunity for investors but, as with any investment, there are risks. Key among these is that while the MLC Global Private Equity Fund does offer some limited liquidity, this is essentially an illiquid asset class and its only appropriate for investors who can take a long-term view.

The fund is available via PDS and will soon be available across several investment platforms. **FS**

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