

# Capital Constellation's Better Alignment of Interests: Private Briefing

*One-year-old Capital Constellation seeks better alignment of interest between LPs and GPs through long-term ownership stakes in firms launching their inaugural funds.*

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In the 15 months since Capital Constellation launched as an investor in young private equity shops and their funds, the LP-backed firm has deployed about \$500 million, with plans to continue shopping for more deals.

The initial \$700 million raised from its co-owners, The Alaska Permanent Fund, [Wafra Inc.](#), the [Public Institution for Social Security of Kuwait](#) and The Railways Pension Scheme in The U.K. (RPMI Railpen), has been used to invest in four firms thus far.

As firms such as a Dyal Capital Partners, [Goldman Sachs Group Inc.](#)'s Petershill unit, Blackstone Group ([BX](#)) and others dive into deals to purchase minority stakes in GPs,

Capital Constellation is pursuing a different strategy it describes as more aligned with investors and dealmakers.

It's another example of private capital growth by deploying billions in dry powder in different ways. To be sure, Capital Constellation faces challenges of promoting a different GP-LP dynamic in an industry that pursues deals quickly but remains slow to move beyond the traditional model of LPs investing in funds managed solely by GPs.

Capital Constellation typically pledges an anchor investment in a debut fund by new firms launched by experienced deal makers. In return for this stake, it'll also get a minority position in the firm to hold permanently. Capital Constellation will also consider investments in more established firms.

This structure puts both LPs and GPs in the same driver's seat of owning the firm for the long run, instead of selling off the stake that's held in a traditional 10-year private equity fund. It also creates more transparency for LPs and GPs on carried interest and management fee discussions since they both own the firm. Capital Constellation argues that its approach creates a more efficient way to deploy and grow capital, and thereby benefit the economy.

Since its launch announcement in February 2018, Capital Constellation has invested at least \$100 million each into [Motive Partners LLC](#), Ara Partners LLC, [Astra Capital LLC](#), and an unnamed fourth firm.

Capital Constellation may be close to naming more investors as it deploys the remaining \$200 million in its initial capital raising round, according to market sources. The firm has since raised additional capital, but details of this development were not disclosed. A spokesperson for the firm declined to comment.

Daniel Adamson, president of Capital Constellation and senior managing director of Wafra Inc., said Capital Constellation had already studied more than 200 firms before investing in the quartet thus far.

"We've been surprised by the quality of seed-stage PE managers who are new to the market but also by the number of growth-phase managers who see the value in partnering with Capital Constellation," Adamson told The Deal. "Because of the strength of capital behind Constellation—we are backed by close to \$1 trillion of institutional AUM from three continents —and the long-term nature of our partnership, we're able to forge deals not only with new managers but also with more established, rapidly-growing firms."

The four firms that have drawn investments from Capital Constellation thus far share one common thread. Each is a sector specialist in middle-market strategies: Astra Capital in communications, Ara Capital in energy and infrastructure; Motive Capital in fintech and the fourth firm in real estate credit.

The four teams are also experienced in middle-market investments, well versed in the private equity thesis of generating additional Ebitda through cost cuts and revenue enhancement, and experts at generating increased multiples in exits to the buyout crowd, he said.

"If you think about the Capital Constellation revenue streams, it's a combination of an LP return stream from being in the fund, plus an annuity-like payment from management fees and carry of the manger which you can hold forever or sell to a dedicated buyer," Adamson said.

Mark Johnson, co-founder and managing partner of Astra Capital, said Astra and Wafra worked together on transactions prior to the Capital Constellation investment, including a co-investment in Texas-based fiber optics company [Logix Communications LP](#).

Although Astra remains a younger private equity firm with about \$300 million in AUM as disclosed on its Form ADV, the firm's make-up of industry veterans with decades of middle-market experience in communications and technology services appealed to Capital Constellation, he said.

While Johnson declined to comment on specific fundraising activities for Astra Capital, he said the partnership with Capital Constellation has accelerated his firm's growth.

"Getting a large chunk of capital early on allowed us to institutionalize the firm and de-risk the back office," Johnson said. "We were able to see how much revenue was coming in and invest in a predictable fashion."

Having LPs as permanent owners add up to a better overall model for private fund investing, Adamson said.

"The Constellation model helps align interests and encourage transparency," Adamson said. "The most enterprising next generation GPs are seeking meaningful, long-term alignment with LPs. Why does this matter? Historically, when your typical large GP goes public or sells a minority stake in its business, this benefits the founders but not the early investors [which do not typically get shares in a firm to sell]."

Adamson adds, "Every household-name GP was built by LPs too, and capital providers deserve to participate in the enterprise value they helped create. Through Constellation, LPs get a stake in the management company to hold indefinitely while benefiting from equity gains as an investor in the funds as well."

Many GPs want to bring their most important clients into their own structure that took some inspiration from the Berkshire Hathaway (BRKA) long-term holding company model, he said.

"Rather than using only a simple GP or LP structure, Constellation includes a permanent capital entity that allows us to hold strategic business interests for long periods of time and to prevent forced exits," Adamson said. "The entrepreneurs that we work with often don't like the limitations of the fund structure for the kinds of catalytic investments that we're making—they don't want to partner with an entity that will be forced to sell to another owner in five or ten years."

With its pursuit of a more collaborative model between LPs and GPs, Capital Constellation is working to change the power dynamic between GPs and LPs, he said.

"People ask why we named the firm Capital Constellation, and not the other way around—it's because we're putting capital first," Adamson said. "If you talk to large pension investors and sovereign wealth funds, they're frustrated by how dominant large GPs have become in negotiations on fees, ESG, and transparency. We can change that by coordinating among LPs to build a creative, new structure."

While Constellation has no plans to exit stakes in private equity firms, a couple of logical options would be a sale of one or more stakes in the secondary private equity market, or possibly the sale of common stock if Constellation's holdings or management company were to go public.

Prior to its participation in Capital Constellation, Wafra had already invested and continues to invest, in mature GPs on its own. Since 2011, it's partnered with 17 managers, including a stake in [\*\*Siris Capital Group LLC announced earlier this year.\*\*](#) Neither Wafra nor Capital Constellation has any plans to sell any of its stakes, nor has Wafra sold any stakes since embarking on its mature GP investment strategy eight years ago.

"We're not focused on how we'll get liquidity," Adamson said. "We're focused on creating value. We look to hold these stakes indefinitely. Our investors and partners are focused on the long-term, so this is an advantage all around."