

KEYNOTE INTERVIEW

Building enduring franchises



Crafting an exceptional investment track record and building a lasting business are not the same thing, explain Wafra's Adel Alderbas and Jordan Siskin

Q What is driving GP demand for external investment today, and what are these GPs looking for in a partner?

Jordan Siskin: In our view, what drives a GP to pursue a transaction is the desire to partner with a long-term strategic investor that can bring more than just capital to the table. That is exactly how we think about these partnerships.

GPs typically use the proceeds of a GP stakes transaction to reinvest in their firm and to grow their franchise, so they are looking for an investor that can bring both the required capital and a fresh perspective that takes them out of their day-to-day thinking and helps them to see a path towards building a best-in-class business.

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Q As GP commitments climb towards 10 percent, is that fuelling additional GP stakes activity?

JS: In terms of the specific catalysts for a transaction, clearly fund sizes have grown significantly as private markets have matured, and so GP commitments have increased substantially as well. GPs frequently want to invest meaningfully alongside their funds, and a GP stakes investment can help to facilitate that.

Again, it is about providing capital to help grow the business and create franchises that will outlive the founders.

Adel Alderbas: It all comes down to alignment. Historically, GPs aligned with LPs by providing GP commitments. Now the GP stakes market is enabling GPs to align with a group of LPs that want to support them on a go-forward basis.

It is a competitive world out there. We are not in the '90s anymore. Creating that economic alignment with these LPs can be transformative for a GP. This is something that GPs have recognised, and that has enabled the GP stakes market to grow and to flourish.

Q How effective is a GP stakes sale as a route to helping GPs institutionalise?

AA: A big cycle of succession events is only just kicking off. If you think

about the original private equity firms that were launched in the '90s, those founders are now ageing. Therefore, there is significant demand for GP stakes investments that can catalyse generational transitions by equitising the leaving partners and bringing in a new generation of leadership.

JS: A GP stakes investment can be one of the cleanest ways to institutionalise a founder-owned firm without a control sale. That has certainly been our experience. The aim is generally to preserve continuity for the firm's LPs and allow for the formalisation of governance, while creating a path for the next generation of leadership to rise up.

Succession is something we have navigated with several of our partner managers, whether at the point of our initial entry or over time. This makes us well placed to advise firms on this particular milestone in their business journey.

Q As the GP stakes industry continues to expand, how are players differentiating themselves in the market? In particular, what benefits can they bring to their GPs, beyond capital?

AA: GP stakes transactions can support private equity firms across their life cycle, from day-one seeding to providing accelerant capital to mid-market managers, through to the acquisition of stakes in established platforms.

No matter the setting, the value proposition absolutely has to go beyond capital. Capital is a mere commodity in this market.

In our case, we differentiate ourselves through our strategic nexus, which is an ecosystem of asset managers on one side – more than 30 GPs within our platform – and an ecosystem of asset owners on the other side. That economic linkage between asset owners and asset managers has been the most value-additive component for us, and it is one that is quantifiable, with that

Q Are you seeing a change in the size of firms turning to the GP stakes market? How are smaller GPs using stake sales for growth?

JS: The large-cap end of the GP stakes universe has undoubtedly become more institutional and competitive. We are still seeing activity in that part of the market, but we are seeing increased activity in the mid-market and even among very small managers, particularly sector specialists. This is an area where we spend a lot of time within our Capital Constellation platform.

These smaller GPs can really benefit from having a GP stakes partner. It allows them to institutionalise their business earlier in the firm's development. It can accelerate entry into adjacent strategies and can fund team expansion or infrastructure, which can be pivotal for early-stage firms.

We also think this is an area that is undercapitalised relative to the opportunity set. There is a lot of capital at the upper end of the market, but the smaller end tends to be more relationship-driven and can therefore be a very attractive space for partnering with up-and-coming teams.

network of asset owners having supported our GPs with more than \$12 billion of incremental, non-contractual LP capital. That is something that goes well beyond the initial deal, supporting the business on a go-forward basis.

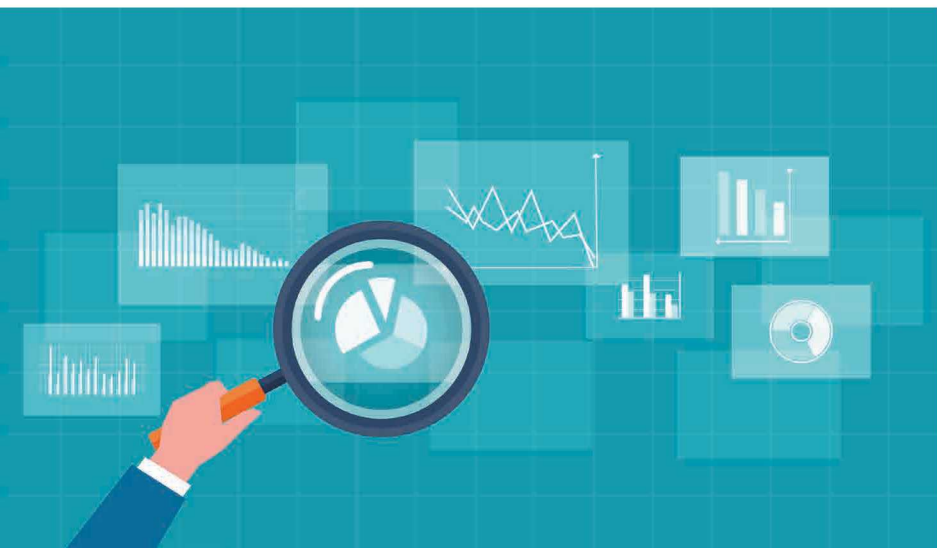
Q Beyond track record and economics, what qualitative factors matter most when assessing whether a founder can evolve from a successful investor to a scalable business builder?

JS: Private markets have produced many exceptional dealmakers and investors with great track records. However, there is a distinct difference between building a great track record and building an enduring institution that will outlast its founder team. The skill sets are not the same, and so what we look to underwrite is the combination of great investors and great business builders – the investor-entrepreneurs.

What that means in practice is looking at how they are building out their teams, particularly how they are attracting and retaining talent. It also means assessing the mindset of the founder team. Do they genuinely want to build something that outlasts them? Are they willing to institutionalise

“A big cycle of succession events is only just kicking off”

ADEL ALDERBAS



processes such as firm governance, decision-making, reporting and compensation philosophy? Do they have a detailed understanding of their clients?

Some of the best founders that we see recognise that they are building a product for someone else's portfolio, and so they will prioritise long-term, durable client relationships over short-term fundraising wins.

We underwrite the quantitative side as well, but for us that is table stakes. What we really want to see is these more qualitative attributes that define who has the potential to build a great firm.

We also tend to establish long-term dialogues with the groups that we back. The conversations we have ahead of a GP stakes transaction can be measured in years, not weeks. That is what enables us to go beyond a quantitative analysis of track record to a qualitative assessment of business-building attributes.

AA: In addition to those business-building attributes, we also prioritise ensuring there is cultural alignment, because that is the foundation for any successful long-term partnership. To that end, we spend a lot of time referencing potential teams.

We also benefit from our existing network of over 30 asset managers that feel part of an ecosystem. That can help us vet potential GPs and ultimately support us in this activity.

Q How would you describe the exit environment for GP stakes investors, and what creative approaches to liquidity are gaining traction?

JS: This is a part of the market that has matured significantly in recent years. There are now multiple viable pathways to realisation, ranging from traditional exit routes to more creative solutions. There continue to be innovative new channels emerging that we are exploring.

But while the exit environment is an important part of the GP stakes world for firms and investors to navigate, for us exits are not a necessity unless it makes sense for the underlying GP. There needs to be a strong industrial logic to execute a strategic business combination with another firm, for example.

Certainly, relative to where the industry was 10 years ago, there are more opportunities for liquidity than was previously the case. Exits used to be somewhat theoretical when we

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JORDAN SISKIN

started out in this business, but now we have a myriad of proof points.

AA: I completely agree. We have been invested in GPs that have gone on to list on public markets, or that have been involved in sales to strategics, to financial buyers and to other GP stakes investors. We have also undertaken financing arrangements. The potential exit menu is wide.

What is fundamental to understand, however, is that buying a GP stake is like buying a utility. The fact that management fees are locked in for 10 years means you are getting a high-single-digit to low-double-digit yield, which helps to create an extremely compelling potential return profile, irrespective of an ultimate exit. ■

Adel Alderbas is chief investment officer and Jordan Siskin is a managing director and co-head of strategic partnerships at Wafra