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Private markets – a growing presence within UK DC

Laura Blows discusses the role of private market investment within DC schemes with Aviva director of investments, Maiyuresh Rajah

Private markets never used to be considered suitable for DC scheme investment, due to their requirement for liquidity. However, lately private markets are starting to be utilised more within DC defaults. What has Aviva seen, and been doing, in this space?
Our main DC default strategy, which is called My Future Focus and has £35 billion of assets under management, has been investing in direct property for many years.

Over the past three years we have been investing more in private markets to diversify that property allocation, with around a 10 per cent allocation across private credit and infrastructure, as well as property.

We have also launched a new solution called My Future Vision, which will take a major step forward when it comes to investing in private markets, in terms of the scale and sophistication.

What is different about My Future Vision compared to what's already out there in the market, to help provide customers with better outcomes at retirement?
There are three main areas in which My Future Vision is different to a lot of the default strategies that have come to market in recent times. The first one is its level of private market investment. My Future Vision will have between 20-25 per cent invested in private markets, depending on where a saver is on their journey to retirement, which is a significant increase to what you normally see in DC default strategies.

Currently, what you see with a lot of DC default strategies is private market investment primarily within the growth stage of a customer's journey to retirement.

What we are doing is looking to provide better outcomes for all savers by investing in private markets throughout that journey.

The way we are doing that is by investing directly into individual funds across those private market assets – private equity, private credit, infrastructure and property. That is instead of investing in, for example, a multi asset, single fund, which will have fixed allocations to private markets.

The third area where it's different is our multi-manager approach. Rather than having a single manager or two managers who may struggle to deal with the complexities of private market investing, we are using a best-in-class approach, working across the board with a number of managers.

Normally, most DC defaults use a single multi-asset fund to get their exposure to private markets. Why has Aviva taken a different approach, and what are the benefits of doing so?
Most DC default strategies do use a single, multi-asset fund. What that means is that they have fixed allocations to those private markets, and will generally focus just on the growth stage when it comes to which customers can have access to those private market investments.

What that means is that the proportion invested into different private markets cannot be changed, and neither can it be changed across different times of a member's journey to retirement.

So, what we're looking to do is invest in individual funds across those private markets. That allows us to change the amount we invest in each of those private markets and take into account the evolving risk a customer faces as they approach retirement and into retirement.

For example, if a customer is in the growth stage, we want to focus on return-generating assets to maximise outcomes for customers. For this, we may want to invest more in things like private equity.

Once that customer gets to the end part of that growth phase, we still want to focus on return maximisation, but also want to start thinking about protecting the portfolio from significant negative market events and so will look to invest in a more diversified mix of private markets.

Finally, as the member approaches retirement, and is in retirement, we want to invest in the less risky side of the private market spectrum and think about asset classes that will provide a stable income, such as private credit.

Why is Aviva taking the time and effort to partner with multiple managers within each different private asset class – what benefits does it provide for the end member?

Private markets is quite a difficult asset class to invest in. You need the expertise and the knowledge, to be able to provide positive and repeatable outcomes for customers, which is difficult for any single manager to do.

Therefore, we are using the expertise of our in-house asset manager at Aviva Investors, but we are also partnering with five additional external managers who are well known for their investment capabilities in private markets.

That means we can invest in different managers within each private market asset class.

So within private equity, we use two asset managers with different strategies – and so as a simple example, on one hand we can focus on secondaries, which can give us a quicker return on investments and early cash flows, while on the other hand, we can also focus on co-investments, which gives us access to high conviction opportunities with potentially much higher upsides.

I believe you adopt a global focus to private markets – what geographies are you investing in and how does that tie in with the Mansion House Compact and Accord that Aviva signed up to?

We have a global focus with this solution as how we invest is determined by delivering the best outcomes for our customers.

We are diversified across regions, which gives us the opportunity to select the right investments within each asset class. Our private market investments will be in the UK, Europe, the US and the rest of the world.

From a UK-specific perspective, we will have between 5-6 per cent in private markets in the UK. So that aligns well with the Mansion House Accord when it comes to investing in the UK. The other aspects of the Mansion House Accord and Compact are around pension defaults investing 10 per cent in private markets as a whole, and 5 per cent in private equity. The private market allocations will be higher than those ambitions within My Future Vision.

I believe you were in Australia recently, seeing what it has done with respect to private market investments, for instance, having allocations of up to 40 per cent in certain superfunds. Do you see the same future for the UK with respect to the level of private market investment allocation?

In the UK, we're starting to invest more in private markets but to get to the 40 per cent level I think will be challenging.

The more you invest in private markets, the higher the cost of the fund. However, there is a lot of conversation at the moment about moving from 'cost' to 'value', and the government is committed to introducing measures that will help that move to value.

The other area is liquidity. In Australia, they don't generally have the challenge of large schemes moving assets from one provider to another, so they can leave their assets invested in illiquid funds and continue to invest in those over time.

While over here, we do have large schemes moving funds, so we need to make sure there is enough liquidity to handle those types of moves.

The last thing to point out is the journey that Australia has been on. Australian superfunds started investing in private markets about 20 years ago, and that was at a time when the government in Australia was privatising a lot of its assets. Therefore, they were able to get into infrastructure at very competitive prices and receive a very good return on investments.

Other countries trying to replicate Australia's private investment example is obviously difficult because of the specific journey that Australia has been on.

However, Aviva's new My Future Vision solution is investing 20-25 per cent in private markets, which is moving the needle quite significantly in terms of private market investing.

The way we're approaching this solution is using the resources of Aviva, Aviva Investors and five other external asset managers, to give us the knowledge and expertise to invest in private markets most effectively. Hopefully this solution will be a major step forward for DC pension schemes investing in private markets.

This is a shortened and edited transcript. To watch the video in full, please visit pensionsage.com