Q&A

Emerging managers often provide investors with access to niche strategies that improve diversification, says Argand Partners director of investor relations, Kay Blackwell

Q How would you describe investor appetite for emerging managers?

Investors view emerging managers as a compelling opportunity set and are keen to identify and track new talent. However, it is often challenging to translate this interest into hard commitments due to mature portfolios, stable existing relationships and the comfort that long track records provide. We have recently seen increased traction when an emerging manager has a diverse team. A growing focus on DE&I has increased interest in backing diverse teams, another significantly underinvested part of the market.

Q Why are emerging managers an attractive addition to a private equity portfolio for investors?

We are energized, focused and have strong alignment with our investors. We invest behind differentiated strategies and develop differentiated ways to create value. We must source, invest and manage our portfolio better than the established market to stand out. We are also able to build and structure our firms in an innovative and nimble way that fosters highly effective investment management processes and attracts ambitious and dedicated talent. We prioritize talent management and retention, diversity and inclusion, innovation and long-term alignment. Finally, emerging managers often provide investors with access to niche strategies at the lower end of the market, increasing diversification and the potential for alpha generation.

Q What do LPs look for in an emerging manager? What matters most (ie, track record, differentiation, team composition, terms and conditions)?

Team is probably the most significant diligence factor for investors when reviewing emerging managers – skill set and experience, breadth of bench, history working together, mix of personalities. Along with the investment strategy, this is part of a manager's differentiation – does the investor believe that this team is special? Can it execute successfully on a well-defined strategy?

Q What were the biggest challenges you faced in your most recent fundraising?

We found that it was crucial to have a pipeline of on-strategy investments and to execute deals during our fundraise. This meant securing anchor capital early on to allow us to activate our strategy. We also spent a lot of time with our investors discussing how we create value during the investment process and demonstrating impact.

Q Why do you think you were successful?

We invest in the global middle market in advanced manufacturing and business services companies, and we have a team that has invested together executing the same strategy over market cycles. In our experience, there aren't many private equity firms that approach the mid-market with a global mindset. In addition, we had a robust pipeline of deals sourced by our investment team because of a long history working and investing globally. Sigma Electric, which was sourced by our partner, Joyce Schnoedl, was a deal that we completed during the fundraise. Being able to diligence a deal live and co-invest with us helped investors get to know our team and understand our underwriting and investment approach first-hand.

Q How does LP due diligence differ for an emerging vs established manager?

The process is similar, but formal and informal references generally take on more importance as part of the diligence process for an emerging manager, along with reaching deeper into the team to assess talent. Unfortunately, the pandemic has presented additional logistical hurdles for emerging managers, particularly first-time funds. For many investors, it's hard to invest behind a team you've only met virtually. ■