Competitive Landscapes

We know you think your baby is the cutest, smartest, and most infallible ever to live. We also realize that asking you to critique your baby is difficult, as it would be like criticizing yourself. Outsiders, however, do not bear the burden of genealogical bias when assessing the perfection of other people's babies. This is a roundabout way of depicting the underlying tension-filled realities of relationships between GPs (parents of the babies) and prospective LPs (the outsiders). Prospective LPs do not have the luxury of just reviewing one investment opportunity. A typical day for them involves an unending barrage of buckshot comparisons, requests, reviews, negotiations, and meetings. These allocators would very much prefer to have only the task of assessing the robustness of a single tree, but, unfortunately, for them to perform their fiduciary duties effectively, they must always start with a forest.

As a GP, you might have a fortuitously timely strategy, you might have very well-motivated people, and you may even have achieved decent past returns, but that only represents one side of the coin. Prospective LPs don't look at strategies/funds in a vacuum. In actuality, looking at funds in a vacuum is a guaranteed way to get blinded and then drowned in a pool of cognitive bias. For sheer thoroughness and coherent portfolio construction purposes, prospective investors look at opportunities across a spectrum. Even the investors who promote opportunistic bottom-up investing recognize that their program cannot be continuously successful if blinders are put on every time they encounter a strategy/fund they like.

Fund and deal sponsors need to be cognizant of their place in the investment ecosystem. GPs are not expected to become experts in other people's strategies, but it is prudent to know enough to be able to respond competently to inevitable questions regarding general uniqueness and differentiated value-add skills. Below are a few pointers to help GPs build a narrative about their place in the investment landscape.

- **Direct competitors**: Regardless of how differentiated a GP views its strategy to be, there are almost always other suitors for deals it pursues. The myth of the "proprietary deal" has been relentlessly debunked more eloquently than I could ever attempt. In most cases, the other suitors of a GP's target deals have their own investment vehicles and are also presenting themselves as differentiated to prospective limited partners. Prospective LPs are constantly barraged with claims of uniqueness and must dig deeper to discover the true essence that lies behind the deals that these sponsors are executing. GPs can help with this by putting forth notable information that can stand out when side-by-side comparisons are made. Yes, deals may be similar, but aspects such as deal ownership percentages, fund size (absolute dollars and the number of deals), operational assistance, board representation, historical success, criteria for deal selection, investor relations, etc. are ways in which one GP can differ from another. A GP that is well versed in what competitors are selling as attributes, can get more granular regarding how their strategy is desirably differentiated.

- **Private Portfolio**: Private assets investing encompasses a wide range of sub-asset classes, each with its eccentricities related to duration, typical returns, distribution profiles (yield, disposition distribution, IPO potential, etc.), J-curve depth, and underlying asset age, among others. The presence of some level of illiquidity is a fundamental attribute of private investing, and it provides a basis for comparison across sub-asset classes. GPs should be able to explain how their strategy is either accretive on its own or complementary to other private sub-asset classes to make a compelling case for its inclusion in a portfolio of private assets. Investors are more selective when it comes to illiquid investments, which makes it important for GPs to understand the options available to those who are willing to lock up capital. A clear sense of the illiquid competitive landscape enables GPs to better depict their unique advantages. For example, core infrastructure managers can highlight early yield generation and the hard asset underpinning as ways to circumvent longer duration and the risk of total capital loss compared to early-stage venture managers or opportunistic real estate managers who focus on ground-up development.

- **Broad Portfolio**: Understanding the investment competitive landscape is not only reserved for strategies of the same asset class. A GP must have a working knowledge of the general makeup of most investment portfolios. For example, if most investors have existing portfolios comprising an overweight in long-only domestic equity investments, how is your strategy complementary? Can investors achieve similar returns to what you target from other asset classes (and sometimes without the risk (real or perceived) or duration associated with private investments)? GPs are forced to think more critically about their overall attributes when the "competitive landscape" question is constructed as a contest for a place in the portfolio, rather than just a portion of a specific asset class allocation. For GPs, it is imperative to keep in mind that investment capital is finite, but potential homes for this capital are indisputably more than finite.

- **Above and Below You**: Funds usually have a chosen market space or preferred arena in which they believe they are the most effective. Examples of these spaces include “small-, mid-, or large-cap/market”, “early-, mid-, or late-stage”, “core, value-add, or opportunistic”, “value or growth”, “venture, growth, buyout, or distressed”, etc. GPs must remain aware of the bearings of their strategy regardless of where it lies in the broadly accepted investment continuum, as whatever managers lie directly above or below (or before and after) you are still your competitors. It is common for prospective LPs to prefer specific market spaces at different times and to seek proof from GPs regarding why they believe their strategy to be all-weather or desirable for the near to long term.

- **Worthy of Mention**: There are many other important factors to consider when mapping a competitive landscape. Additional factors include funds’ potential behavior in different economic conditions (e.g., during periods of risk-on and risk-off), deal entry patience, sell discipline, philosophical mindset, geographical strength, operational capabilities, etc. In general, the more detailed the desired map, the greater the risk of discovering and exploring many rabbit holes. GPs should develop a practical understanding of their position in the ecosystem and assess this periodically for any needed adjustments.

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July 28th, 2024.