FAIRPORT WEALTH

Private Market Solutions Webinar

Private Market Solutions – September 19, 2024

John Silvis:

Well first of all, thanks for tuning into our discussion today on the private markets for the markets. For those who don't know me or I haven't met, my name is John Silvas, I'm the chief investment Officer for Fairport Wealth. Just a little bit of a housekeeping. We do encourage you to ask questions and please do, you'll have to do it through the chat. There's a chat button on the screen. But for everybody for this call today, we'll be on mute so we won't be able to hear you. But if you want to ask questions through the chat function, please feel free to do that. So joining me today on the webinar is none other than Robert Picard. Robert is the managing director and head of alternative investments of the Hightower Investment Solutions Group. The Investment Solutions group is available to Hightower's community of advisory businesses, including Fairport Wealth.

Their partnership helps enhance portfolio construction and asset allocation for clients in both the public and private markets, which is what we're going to talk about today. Robert has over 32 years of experience, both on the buy and the sell side, having built out multi-billion dollar alternative investment programs for companies like First Republic Wealth Management and the Carlisle Group. Interesting fact, during Robert's career performing due diligence on manager strategies, he is visited over a thousand firms worldwide. I'm going to guess that's a lot of frequent flyer miles out there. So without any more delay, I'm going to welcome Robert and Robert, thank you for joining us today,

Robert Picard:

John, thank you. And thanks to your team and all of your clients for being willing to sit through today's session. Hopefully it'll be enjoyable. And yes, I do have a number of frequent flyer. I'm a million miler user with at least United. I haven't fortunately accumulated elsewhere per se, and apologies for the attire today. I'm normally more dressed down, but I was at an event which I comfortable to say that right after us was Mr. Tony Robbins was speaking after. The good news was I did not have to walk on any calls and or go through any of those sessions, but it's much better to be with you and your clients.

John Silvis:

So that's a great introduction. So we've talked a lot over the last few years, we've been with High Power, I've seen you give presentations, we do a lot of, Robert and his team do a lot of internal presentations for the advisor groups. But you talk about relationships, right? So you have 30 some years of experience, I'm sure you've built a lot of relationships. I know just from experience within Hightower, you've brought on guys like David Rubenstein from Carlisle Group, very prominent person in the private markets, even Ashton Kutcher, which most of us probably think of as the seventies show, but obviously if you ever watch Shark Tank, he's on there as well. He has been an early investor in a lot of these companies. So, talk a little about the relationship part of the business, Robert. I know there's public and private markets, but I think the private markets really is a relationship type of business.

Robert Picard:

John, you're absolutely right. And just to provide some context, it's a people, it's all about the people, first of all, just as background and context, traditional public equity, I mean stocks that you can buy, you can get the information on your iPhone and it's readily available on the internet, public fixed income, it's readily accessible to research, et cetera. Obviously private markets are, to a certain degree, a little bit less efficient, but it's a huge investment opportunity. And just to put some framework and understanding of what that market looks like of the companies in the United States that generate more than $100 million in revenues, 91% of those companies, 91% of them are still privately owned. And just similar to your clients, most likely they're still operated by founders. The people originally created the business, founded the business, and are generating typically are really a core element of our economy and our ecosystem and a great way to add value to a public equity portfolio of public fixed income by investing in the private markets.

And to get back to sort of what you're alluding to on sort of how we approach and how we have these relationships, as you alluded to, I've been doing this now for 30 plus years, a long time, and it really is about people and relationships, meaning that I still have relationships with fund managers who were the former partners at Drexel Burnham, lamb Bear, former partners at Salomon Brothers who are still either in business and have survived through all these market cycles. And very often that is the source of a lot of our ideas. And one of my biggest focuses has been on longevity, meaning someone who's been doing this and survived through the Asian financial crisis of the nineties, going back some time, I mean it could even go back to the eighties on the first crash, but the nineties, then the internet bubble and invariably the global financial crisis and others that's really proof that they are able to generate long-term consistent risk adjusted returns, which is important to us.

And then of course those people provide us with ideas and opportunities for investments that we think are relevant. And then of course you yourself and the rest of all of our teams that work with us, very often you'll have clients that they too have relationships either with individual firms and or investment opportunities that fortunately cross pollinate and come our way too. So I really like the idea of having sort of a funnel and welcoming all origination and ideas and then ultimately funneling through. Just to give you an idea of the frequency and number, Frank Cordio and myself on the investment solutions team, we've had about 3000 inbound requests from fund managers, some of our wealth managers and potentially clients. Of those 3000 we've met with 350 over the past 12 months. And of those 350 we've allocated to about 27. So really there's a very strong funnel and very strong investment due diligence, investment reviews and operational risk reviews.

John Silvis:

It really goes back to that you got to put the legwork in or pound the pavement so to speak, really to get to that position.

Robert Picard:
Listen, I think my belief, and one of the reasons I love what I do and how I can help you find solutions for you and your clients is I do believe that private markets offer some opportunities currently that are not typically available in the public markets. And those opportunities, my role is to not only identify them but then to a certain degree, present them to you and make sure that they fit within a portfolio that could be ideas such as cybersecurity where we've been, it's funny, there are two firms leading firms, that their investment idea for 2024. One of their top three ideas was cybersecurity. We along with your team at Fairport Wealth, we were allocating to that sector throughout last year and earlier this year. And really that view was from the perspective that regardless of the economy, regardless of the spending, corporate spending at the board level of most companies, whether it be private or public at the board level, it's a fiduciary responsibility now to ensure security of your technology systems. And that's where we knew that that's a long-term theme. It's a long-term wave and when we invest we really want to make sure that we're preferably on a wave that we could ride versus an area that won't have such growth.

John Silvis:
So just to kind of take it back to step one, so we have some clients that are very well versed in private markets and private equity and those types of things. And then we have some where really we're just kind of going through that educational process. And I know you've done a lot of work with the high power community on educating people. So how do you define private markets? And I think you talk about cybersecurity, which is probably a niche part of one of those, but like the bigger groups you hear about real estate and other things like that, private credit seems to be the thing you hear on TV a lot. So how do you define the universe in broad terms and then how does that translate into clients? How do you start that process?

Robert Picard:
So first of all, to just provide a little inside view, it's very funny, there can be some confusion. So a lot of people, some people refer to it as alternative investments, some people refer to it as private markets as you're so rightly doing. And it's basically the same thing. And the difference is that we found that a lot of people find the term alternative not very favorable, where people find private markets much more exclusive and more value. And I take the same approach and being that anything that is not a publicly listed equity or publicly listed fixed income interest instrument, anything that's typically privately transacted or investments in private transactions or private funds typically that require subscription documents we would refer to as a private market investments. And that's an area that, to give you an idea, and I think I have a slide here that I can share that gives the difference between the two separate markets.

Lemme see how I can operate this technology. Hopefully it works. You should have on your screen right now, John, do you see it? I see you nodding your head. This is actually an interesting slide where on the left side are the risk, the public return dispersion between large cap equities, global bonds and US core real estate. And what you'll see is there's very limited return dispersion between the top performer, which was 8.8% and the worst performance in equity was manager, which was about 6.8%. What's interesting is on the right side, which is where you see the private markets such as private real estate, private equity and hedge funds, you'll see that there's a much larger risk return dispersion and most importantly typically much higher returns. So as an investor, as one of your clients, provided you have the right team, which is what we do here with you, John, selecting the right opportunities, you can generate much higher returns specifically. The other piece that's really interesting while I'm on this slide is the fact that in the world today, just to give you a framework, the average billionaire in the average university endowment, they allocate more than 50% typically to private markets, which is really an incredibly large.

John Silvis:

I've heard you give this numbers before, but it's very interesting. So go ahead.

Robert Picard:

I always say 50 and five, and in this case on this slide it's 57 and three, but the idea being that the average billionaire on the average university endowment have north of 50% of their portfolio allocated to private markets and the average individual investor has less than 3%. And what we're seeing now, and the reason for that is specifically better risk adjusted returns. We now know over a one year, three year, five year, 15 and 30 year period portfolios with allocations of 20 to 30% to private markets, which is a little higher than we typically would go. We typically at Hightower look to allocate between five, 10 or 20 depending on the client need. We see those returns typically with that portfolio with private markets with a higher and better risk adjusted return. We can higher return with less volatility, which we find to be beneficial. And then just to give you an idea on the strategies is really, I'll break it down to three private equity, which is basically as I alluded to earlier, which is private companies investing in companies that are still privately owned that are not yet public.

And for instance, right now what we're seeing, and I keep digressing a little bit, but for instance, the internet started really around 1990, 1992, you could go back to CERN and in Geneva, Switzerland where they created the internet, but the internet started in 92, mobile internet was really over the past 25 years and it's taken 25 years for that market to develop. Artificial intelligence for instance is expected to be only a 10-year growth, meaning that the change isn't necessarily constant, it's the acceleration of that change or a factor of two. So though there were 25 years for the growth of the internet, we think artificial intelligence 10 years. And what I'm getting to is the opportunity in artificial intelligence is much less, in our opinion, in public equities, it really opportunities will be in the private equity segment.

John Silvis:

Those companies tend to stay private longer than they did back in the internet version of growth. So you're seeing those, which I guess would create a better opportunity in the private markets.

Robert Picard:

Yeah, that's one piece and I'm going to get back to private credit and private real estate in one moment, but I just want to add to what you just said. We all live now in a world where you, your clients, my family, my brothers, they're all watching CNBC and there's literally a countdown to the starting bell every morning. It's like rush, rush, rush. I've got friends that I play golf with who are day traders and everything's like immediate and I have to do it now, et cetera. And by the way, for our economy, it means that corporate America listed companies ultimately since they're living on a quarter to quarter earnings cycle, are forced to make often very short-term decisions in order to placate their board of directors and also their shareholders. And one of the benefits of the private markets, both on the private equity side and the private credit side, which I'll get into is that because these companies are private, they don't have that same pressure on a short-term basis of constantly,

constantly delivering returns and can make much longer term business decisions, which I think is actually really healthy for the US economy and the global economy in general.

I think part of the stress for a lot of corporate America is this constant need to please constant need to deliver and ultimately sometimes shy away from longer term, shorter term difficult choices, which would ultimately result in longer term revenues. But now the other piece of this, I talked a bit about private equity, in instance, artificial intelligence or cybersecurity or for instance life sciences like healthcare where there's a huge opportunity, private credit is really exciting. I'll give you one example. And private credit is for instance direct lending. And what I'm getting at is today in this country what's unique to the US economy, we have 4,000 community banks. We all have in our local communities the local community bank, which main business is providing to a certain degree, mortgages to a certain degree, commercial loans to local businesses. And what we're seeing is there's just too many community banks, a lot of these community banks are not necessarily as efficient and as professional and I guess as experienced as some of the leading, most active money managers are in the world. And what we're seeing today are private credit funds are being created to basically step into and take over some of that role of the community banks. And what we're expecting to see over the next five years, and a lot of what I do with John and to share with you all is these changes to the US economy and how we operate and what we're seeing is we expect over the next five or 10 years, 4,000 community banks being reduced to about 2000 community banks.

And what basically is happening are these private credit managers are creating investment funds. We have the opportunity with your investors to invest in these funds. And defacto we are or they are replacing those community banks and these funds will be making loans for direct business loans direct to investors. And I'll give you an example, which I thought was pretty fascinating that came from one of these credit managers where we had a discussion about the economy and why we haven't really had a recession yet. And the comment he made to me I thought was quite brilliant and it was great insight from the private credit space where he said corporate America, the c-level professionals, the CFOs, CEOs, CEOs, these companies that are private who have survived, they've just survived a pandemic, they've just survived huge supply change disruption, they've survived rising interest rates and they've survived to a certain degree labor shortages.

And the reality, what he's getting at was that the c-level professionals, the leadership in corporate America today are some of the highest quality business leaders this economy and our country has ever had historically. And a lot of that is a perfect example of how now they've become much more sophisticated in how they borrow money in how they operate. And that's really where these private credit funds are able to step in to a certain degree, replace the community banks and basically become defacto banks themselves lending money for either single family rental communities to be built or lending money for direct lending, for bridge financing and other opportunities. One area that we've been focusing a lot in asset-based lending in inflationary environment, the opportunity to basically lend using assets as collateral aircraft engines, aircraft lately, seeing healthcare royalties, publishing royalties, there's all these different opportunities that are generating revenue return streams and basically you as an investor become the bank where we're lending the money and then we're getting reimbursed for that capital outlay and we basically become the receiver of the interest from the borrower. So it's really a fabulous, and the same is true for real estate where now there's an opportunity for private investors similar to the average billionaire and university endowment to invest in real estate, large real estate funds and smaller real estate funds to really participate and own those assets.

John Silvis:

Yeah, we had a question come in and I'll get to it in a second. I think it kind of goes to allocation. So, you talk about private credit or private equity, what's the other kind of pillar in that group?

Robert Picard:

So it's private equity, which part, there's an element of secondary private equity and also venture capital. Then you've got private credit, which has a whole area of, could be direct lending, it could also be mortgage backed securities, royalties, asset-based lending and other then you've got private real estate where you could be investing in for instance. And one of the areas where we see a lot of opportunity is industrial real estate, specifically with the theme of post pandemic, all the supply chain disruptions. There is an ongoing reshoring of manufacturing in this country, both the current administration and we expect future administrations have invested meaningful amount of money in manufacturing infrastructure to basically bring back not only jobs but bring back manufacturing, robotics, automation to make the economy more efficient. And there on the logistics real estate side, there's a huge opportunity. And then the last one, which I think is really interesting is who'd have thunk?

I mean multifamily has been a great, very successful investment thesis for many private investors. A lot of people have been simply buying residential homes in their local communities and then renting them out. What we're seeing now is that right now there's a supply break in our economy where there's about four to 5 million homes that are missing for single family rental. And that could be for a number of reasons, millennials who are having more children who can no longer fit three, four kids in a multifamily or an apartment. Part of it's because their credit rating might just not be sufficient to get a loan or a mortgage or even worse, they just don't have the capital for a down payment. So what's happening now are real estate firms are creating build to rent communities. So rather than building multifamily communities, they're building build to rent communities.

John Silvis:

They just built on in my neighborhood.

Robert Picard:

And there you go. And then they basically use rent, very nice homes, but they're only for rent of course. And then they pay, the rent is coming straight back to the property manager and the fund investor. So those are exciting. And by the way, I look in my local community, the rentals are way more because there's no single family rental community per se, there's just no homes to rent. So the pricing is just way out of whack and it's very expensive. So I think it's a great, this is one of the areas where that inefficiency in the market, these 4 million homes that are missing, we have the opportunity now to help invest and have these build to rent communities.

John Silvis:

So one of the areas you mentioned briefly there was infrastructure and I think that's something that everybody's can easily understand. They see it's horrible thing, but they see bridges collapsing and they drive the work and they see things, they're on pole roads, they know what a data center is, all these types of things. So it's something I know that it seems to be top of mind. There was a big infrastructure bill that went through, I guess a few years ago now with a trillion dollars. So kind of drill down a little bit, one of the offerings you guys partnered with has an infrastructure fund. Maybe kind of walk us through that due diligence process. I know you have a PPP program you use, just to kind of give us an understanding. We go to the clients and we talk about, hey, there's been the due diligence and this is a recommendation from Robert and his team, how that process, obviously briefly, it's probably a long term, but briefly how that worked and how you got to that point and that relationship in that fund.

Robert Picard:

Okay, so there's a lot to unpack there. I'm going to try to be relatively concise. Let's first talk you and Fairport Wealth and what we try to deliver as solutions for clients. Listen, this world is competitive and with the current wealth management business in the United States, it's extremely important to us to deliver and provide you with differentiated products. We are really, it's very competitive and we want to provide you with what we believe to be the best money opportunities or investment opportunities globally. And in order to do that, we follow what I refer to as my pep talk, PEP. And that means really the first P is performance. We really try to identify leading managers that have top quartile, if not top decile performance. And we do peer group analysis and other quantitative and qualitative analysis to identify those teams.

Then of the PEP. The second is E, the letter E stands for exclusivity. A lot of the transactions that we do very often will partner with firms. For instance, we partnered with the founder of one of the leading private equity firms. We partnered with his family to basically launch a fund in real estate to make real estate investments. So this founder of a famous real estate firm is allocating or anchoring the fund with 50 million and high tower. We're also anchoring that fund with our client investments to basically align our interests and make sure we're getting the same exposure that this founder of a private equity and he's a multi-billionaire investor and we think that's smart money investing for our clients. That's the e. And the final P is preferred terms where part of the benefits of being associated with Fairport, being associated with Hightower as a whole is that because we invest with scale, we have a certain amount of dollars to invest and allocate, we can very often negotiate preferred terms with the underlying fund managers as we did with this family office. And when we do that, any negotiated preferred terms, those terms and that benefit is actually we don't take any piece of that. It's passed straight on to you and your clients. So John and all of your clients at Fairport benefit from those preferred terms. So that's one of the ways that here at Hightower we try to differentiate ourselves. Now talking about one of those other investments, who has an infrastructure fund.

John Silvis:

Robert, just to, I didn't interrupt you, but on that last P, the preferred terms, I think, so again, from a client standpoint, if they went to a retail outlet to try to get into the same fund, they would most likely pay a higher premium to get in or a higher fee. And for us, I know that's been one of the differentiating things through your team that, and it's not, you think about it on a compounding basis over the next 10 years, it becomes fairly substantial that you were getting that discount upfront. So just wanted to kind of reiterate that.

Robert Picard:
I think that's a great point. Let me just highlight and it's best to talk sort of and give you an example where recently there was a structure without necessarily going with detail into the name, but there was a structure where if you invested directly as an investor, number one, you'd have to have a $5 million minimum investment, which puts that out of range for most average investors. And for that $5 million investment, you would be charged 2.1% management fee and a 20% carry. What we ended up doing with Fairport is we basically created a structure where we were investing in the fund a much lower minimum investment of let's say a hundred thousand dollars. This is for qualified purchaser, but let's say a lower investment size. But most importantly, we also structured the transaction where we'd invest in the fund, but we'd also be investing alongside the manager into co-investments. And those co-investments would be allocated with no fee, which brought our fees down from 2.1 down to 1.43 and the carry down from 20% down to 10%. So that's just an example. I know it sounds a little complicated and complicated. John can share more information.

John Silvis:

About. Yeah, I'm more happy to get into that. You can talk to your advisor on that one. But I do think, I know you mentioned it as one of the ps, but it is substantial savings. And again, if you look at it over a compounded timeframe and Moe's investments are multi-year investments. So it does start to add a lot of value. And again, that's one of the benefits of working with Robert and his team through Hightower.

Robert Picard:

I was going to get there. I just want to make a quick joke, which was the other P. If we don't like the P preferred terms, you can always use P as people, meaning that we've really got seasoned professionals, Stephanie Link, who we work with, who runs investment solutions, who's on TV pretty much weekly if not daily. And our team on average, we all have north of 30 years experience, which is really important to identify and have a seasoned team of professionals to evaluate those managers. Now evaluating for this *** for instance, they've been doing this for literally more than 40 years and they've been investing in infrastructure for many, many years. And when I talk about infrastructure, this is similar on the private credit side where all this infrastructure, whether it be, we talked about artificial intelligence earlier, well if you're using a lot of artificial intelligence, the amount of bandwidth and data that's going to be used and housed and stored is going to be massive.

And that data is going to be held in what we refer to as data centers, which are part real estate, part hardware, and just part tools that, and these data centers are extremely important and continue to be built all around the world. And that would be one area that firms are making large investments and allocations. And I mean when you look at the numbers and apologies here, John and I can get it to you, but they're literally a numbers of, it's multiplying by 10 to a hundred times the amount of data over the next several years. The amount of growth, the amount of data needed for artificial intelligence, it's just massive. So that's one area. Coal, roads, bridges, wind farms, solar panels, all of that cell towers to a certain degree, and I haven't seen it invested yet, starlink and others, but anything that has to do with communication, anything that has to do with infrastructure for that communication could technically be pulled into these funds and ultimately all will generate a significant meaningful revenue stream for investors by owning that infrastructure.

John Silvis:

So I mean there's multiple funds out there. So you took all those, and I know you mentioned about a meeting, I think you said 300 already this year, you and Frank, but so how did you guys get down to the *** version? So when you went through the PPP process, you probably had a very narrow funnel once you got down to that point. And then does the relationships factor into that availability size? How does all that work?

Robert Picard:

It's really, I like to remove any emotional decisionmaking from it. And it really is less relationship, it's much more for those of you and unfortunately I grew up with Dragnet, for those of you who grew up in the sixties or seventies, which was Detective Joe Friday would always say just the facts. Now I really like to try to keep a balance between just do the hard work of evaluating the factual quantitative history, the track record length, how long they've been running the business, doing the business, the people who are operating that business, and then going to both operational due diligence reviews, which is how they're set up operationally. Can they manage, can they operate or will they have a breakdown of some sort or snafu and the accounting level And then go keep digging further and further into how they operate. Can they make money consistently throughout multiple market cycles?

We had a conversation with them one day when we were just talking about, I got frustrated because they were giving me very much just the traditional presentation about how great the firm is and how they cross pine across all these verticals and they're invested hundreds of billions of dollars. And to a certain degree we know that what I'm really interested in is how do they operate, how do they get along and how do they identify the best ideas? And then we went into a deep dive into talk to me about your mistakes, what went wrong and when it went wrong, how did you handle it? And I'll never forget, I was talking to them and there was a long pause because I became, it was probably later in the day and it's getting a little cranky and I was just like, come on guys, give me something. Tell me about what went wrong. And it was very funny because one person piped up and said, oh, maybe the beaver story. And I'm like, the beaver story?

And basically there's a long-winded story about a power plant, I believe it was a hydroelectric plant that ran into a problem with beavers creating dams and ultimately upstream created a bunch of issues and then downstream and they had to address. And I think the beavers were protected. I mean it just went into this long-winded discussion, but it was absolutely fascinating because we've got a very deep dive into how they actually mitigated that and how they handled the situation and ultimately managed it. But that's just a good anecdote of how deep we'll go.

John Silvis:

So kind of keep drilling down there. So most of our clients and one of the advisors asked a question, which I think really boils down to asset allocation. So most of our clients, not all of them have that 60 40 portfolio and we're at all-time highs today in the market and the public markets are doing really well. Rates are fairly high. You're getting 5% on your cash. How would you start the process? I know you mentioned was it 3% and you guys go to 10, 15 to 20, let's say, since we're probably in the low end of that, we want to get to that 10% level for a 60 40 portfolio. And you mentioned a couple of different options. I know, and to Robert's credit, he has some slide decks out there that we have had compliance approved, so if people wanted to use them or if you asked your advisor, we could provide those as well. But so how would you kind of start that process from a 60 40, oh, there it is. There you go. So you're at a 60 40 and you want to start getting to that 10% level and there's probably a process to it. Do you start first, how do you build it? I know each client's a little different, so I don't want to put you on the spot, but in generalities, how would you go about that?

Robert Picard:

Yeah, so great question, John, and listen, I'm going to try to make this as simple as possible. Again, you're right, each client is different. Each client has unique, their own unique situation, but generally we look at it as 5, 10, 20 5% for a conservative income oriented portfolio, a 10% allocation to private markets for a portfolio, and then 20% location to private markets for a growth portfolio. Now the question, and this is where it gets more interesting in, let's say we're taking a balanced portfolio, it has 10% private markets, what do we invest in and how do we allocate that 10%? And what we typically suggest doing is both the wealth advisor and the client, however you are expressing the traditional 60 40 allocation, meaning that let's say you're 60% equities and 40% fixed income. I would use that same expression for the 10% allocation to private markets. So that would be a 60% private equity allocation and 40% of that 10% would be in private credit and private real estate.

John Silvis:

So 6% would go to private equity.

Robert Picard:

Yeah, that's correct. And 4%, probably two, correct, 4%. And the 4% would go, let's say 2% to private real estate and 2% to private credit. But again, and then you can go a little deeper because if your client already has, let's say some single-family rentals themselves away from you in their own portfolio, they already own two vacation homes, that's technically real estate exposure. So they kind of have to look at their own situation.

John Silvis:

And that's where you've work with your advisor to figure out those nuances. And I realize, and we have some clients that own their own business, so that's almost like a private equity itself, right? So exactly, I get that. But for the general knowledge, it's kind of following the 60. So if you're at 60/40, you kind of follow the 60/40, but if you were an 80/20 and you wanted to use the 10%, could you still do the 80/20?

Robert Picard:

I would do 80/20. However, you're expressing your philosophy on the public equity and public fixed income side. I'd simply port that over to the private market side. I think that's a fair approach because again, we look at private markets as serving as a compliment or additive to your public equity and public fixed income, meaning that it should have a better risk adjusted returns because you need to be rewarded for the illiquidity of that private market investment, meaning that 10% of your portfolio is going to be less liquid than the rest of the portfolio.

John Silvis:

Okay, no, that makes sense. So, the tougher one would be infrastructure. Where does that one fit? Is that equity?

Robert Picard:
I typically listen, this is open for debate. There's no right or wrong here. I typically put it more in the fixed income component because you're typically receiving some sort of revenue or lease or whether it be data center or other, but some people will consider it to be equity. I consider it more to be an income generating asset.

John Silvis:

Okay. So you talked about the beavers, which I didn't think we talked about today, but that's okay. So one of the questions your colleague, Zach helped you kind of prepare and he asked, so I'll ask you questions since you said it. What is some of your best and worst investment experience in private markets? You can't use the beaver story because you already did.

Robert Picard:

No, I'll tell you, this is actually a good anecdote. My best investment is actually my worst investment. And this is an unusual story from about 20 years ago where we made an investment, we bought a insurance, we made an insurance investment in the portfolio, so similar to an s and p put option, but it was a structured option to take advantage of potential catastrophes around the world. And we did that with purpose to really have that hedge out, that tail risk of a portfolio and that investment was maybe 1% of our portfolio. And ultimately it was the year of the tsunami, the big tidal wave that decimated East Asia, specifically Thailand, Bali, a number of other resorts. And that ended up going in the money and we made about an 8000% return - best investment we ever made. The problem was the insurance company that sold us the paper or that hedge basically looked at us and said, we don't really have the money to pay you out and you need to sue us because we're not going to pay. We disagree with the evaluation. And it went to a 12-year legal lawsuit. So the learning and why I say it's the best and worst, it was a great return. But the reality in life is that you also have to understand the limitations and there's legal risk and other risks that come into play that fortunately are deeply ingrained in my psyche, in my experience, my life experience, and my investment experience, which I now share with you and all of your clients. That's one. The second-best investment is to quote Bill Conway from the Carlisle Group was chief investment Officer.

He always says the best investment is the investment you don't do. And that's a good story where my name appears in a book with Bernie Madoff, where we met with Bernie Madoff in 1999, my team within seven minutes and basically three or four questions, we knew that he could not possibly be doing what he said he was doing. He was blatantly lying to us. And we ultimately left that meeting and never let anyone in either any of my portfolios or any of my firms ever allocate to Mr. Madoff, which turned out to be, again, the best investment is sometimes the investment you don't make. You just want to make sure you have the right season professionals managing, helping you such as Fairport for those investments.

John Silvis:

So on that one, that should be the first thing you talk about. Everybody unfortunately remembers that. So I guess before we wrap things up, so just to kind of go back to the beginning, I hope this has helped our clients get a better understanding on private markets. And I think for the vast majority, as we were mentioning earlier, we're probably at that 3% level. So we're kind of working the private real estate, private credit private equity buckets that you mentioned, but maybe for those more seasoned clients. And we have a few that have been in the private markets, the illiquid holdings for a while, and there's always new things out there. You mentioned a little bit about AI, but then the data centers and those things are almost just as important, but they're not publicly traded as much. There are some private REITs and stuff like public REITs, but what do you see out there as probably something, if you're looking to round out a portfolio, I know you mentioned cybersecurity, there's a couple of other ones out there, but what do you see is, hey, this is something that we're put a lot of time in and we think there's a long-term theme to this.

Robert Picard:

So it's a great question. And by the way, we are going through a transformational moment in time, and I talked about that this morning with my team. Often in our investment committee, I sometimes have to shake everyone up and just hit 'em and say, listen, the world is changing and now is the time to be planting seeds. And it's important to highlight how this is a transformational moment. So artificial intelligence, it is a game changer. There are some people who say it's overhyped, it is not overhyped. Not only has artificial cells been with us now for a number of years, but it is growing exponentially and the acceleration of the change is frightening. And I say frightening in good and bad, meaning that when I was growing up, I never expected to be like the Jetsons with my iPhone and being able to FaceTime people, et cetera.

This is accelerating and it's increasing productivity. It's actually going to be deflationary to a certain degree because it's going to actually reduce costs for many companies. So it's a really great story. Artificial intelligence, life sciences, healthcare, the aging demographic in our country, healthcare is changing, healthcare is improving. Life sciences, gene editing technology, all these different solutions, the speed at which we're able to get through trials, pharmaceutical pharma trials, we saw recent with Covid with the vaccines and other is increasing. That's good. And that's also technology and to a certain degree, artificial intelligence, which has increased the speed in which we can evaluate drugs. This is all a huge win. Data centers, which is affiliated, is associated with artificial intelligence, single family rentals, the need for build out for single family rentals, which is significant. And of course robotics and automation, which there too is related partially to artificial intelligence. These are all pieces. The last that I think is very much under it hasn't been discussed much are royalties. And that's actually becoming a new asset class in private markets where it's like music royalties.

Like John Sellman book of music royalties, healthcare royalties, pharmaceutical royalties, book royalties, for instance. Stephen King is a perfect example of someone who might want to sell the royalties and the revenue stream, not only from his books but from his films, film royalties, all of these is an emerging massive market opportunity to basically get, is that considered income flow? So you're literally living on every time they play the song?

Robert Picard:

That's right. That's correct. Or every time someone buys the book or downloads the book. And then those royalties, I mean they're literally being new royalty streams are being created. For instance, book royalties really don't exist right now, and that's going to be a multi-billion dollar revenue business.

John Silvis:

So the last question we got really goes along the lines of illiquidity. And then is there a correlation with lower volatility, I assume, and everybody in my experience has no problem with being aggressive or ill liquidity until the market goes the other way. And then it's like I'm very aggressive, investor market goes down 10%, I want to get out. So illiquidity I think is maybe, I wouldn't call it a setback, but it's one of those issues that has to be explained to the client that some of these have, I know some of the evergreen stuff you can get out on a quarterly basis, at least if the gates don't close. But what's the expectation for a client on illiquidity if they step into one of these funds? Or is it a five year commitment, 10 year commitment? What would you recommend that, what expectations would you set, I guess is a better way of saying it?

Robert Picard:

John, great question. And I think we have to be really thoughtful about that. And it really depends on a lot of factors. It depends on the demographic, meaning the age of your client, the revenue streams of your client. It goes back to what I was referring to as number one has to assume that these are long-term investments. Even if you're investing in these new, what I refer to as democratize private market investments, which are technically quarterly liquidity, I think you should really look at this portion of your portfolio as long-term, 3, 5, 10 year that you're planting seeds to ultimately grow and become a meaningful anchor to your portfolio. That's really the way I look at private markets. Now, on that same note I talked about one of the benefits of having that long-term commitment is you need to be able to sleep at night. You need to know that this is going to perform over longer periods of time.

And I always think back to my late father who passed away 10 years ago, and he was the perfect for me, he was the perfect market indicator for when to buy and sell the market. Because every time he'd call me to say, Rob, he had a little bit of a German accent excuse from Switzerland, say, Rob, the markets are not good. I think I need to sell. And I knew I could literally know within 24 to 48 hours it was time to buy the market. And whenever he'd say, I think I need to buy the market, it was always time to sell the market. And what I'm getting at is the benefit of the private market portfolio, that 10 or 20% in your portfolio is that really avoid you timing the market because you can't, it's very difficult to time the market. And the only caveat is not only do you leave that money there to last and plant seeds for longer term, you need to be rewarded for that illiquidity with higher risk adjustment.

John Silvis:

That's the illiquidity premium that you hear about. Exactly.

Robert Picard:

And we insist upon that and that's really important.

John Silvis:

So I'll make this the last question for you. I appreciate your time and I hope this has been helpful for everybody. But one of the advisors we work with, he's actually out of our Princeton office, asked about litigation finance fund. Is that one of the strategies you guys have you looked at or interested in?

Robert Picard:

Yes. Yes. Great question.

Shout out to Lawrenceville Prep where my daughter went to school, love the whole crew in Princeton, some great places to eat great restaurants and obviously a great school. But on the litigation finance side, it's one that we've spent a lot of time, at least I have throughout my career researching. There are unfortunately different levels of litigation finance. There are some that most of 'em are post-judgment, but it's highly risky. It takes a long time to process. And there have been some challenges with that strategy, which I can go into more detail, but there have been firms, there have been some frauds, there have been some bad deals that have not converted. But then there are some that are really good. I mean we towards the lean towards post-judgment deals that are post appeal where simply the law firms are trying to recoup or simply waiting for the payout. For instance, it was recently all of you have heard we were offered, we had the opportunity to participate in, we did not ultimately participate, but I believe it was cap. You may have heard on tv, whether on MBC or CNBC or others, there's a camp illness, fire pits and other. And the government is ultimately paying out a meaningful reward in damages. And that has been a very successful litigation finance transaction. But we have chosen historically to shy away from that strategy.

John Silvis:

Okay. But listen, Robert, I really appreciate you taking the time. I hope this has been helpful for clients and advisors out there. As always, if you have any questions, contact your advisor and as I mentioned earlier, some of the slides that Robert used are already in compliance approved presentation packets. We'd be happy to pass those out as well. And if you have any more questions in the future, either Robert and I'll give a shout out to his team. He's only as strong as his team. We'd be happy to make contact with us and we can get back to you on those answers. But again, appreciate it. First and only time probably I'll see Robert a tie, but maybe I'll see him again. Most of the times he does not have one on, so he dressed up just for us today.

Robert Picard:

I just dressed up for you and your clients. Listen John, absolute pleasure. Thank you so much for having myself and the private market solutions team from Hightower and look forward to speaking anytime.

John Silvis:

Yeah, it's been a great partnership. I really appreciate it. Thanks a lot Robert.

Robert Picard:

Thank you, John.