GCM Grosvenor

PRIVATE EQUITY

In Brief

Q&A: Investing with Diverse Managers

May 2019

Past performance is not necessarily indicative of future results. No assurance can be given that any investment will achieve its objectives or avoid losses.

Derek Jones

Managing Director,
Private Equity Investments

ABOUT GCM GROSVENOR'S DIVERSE MANAGER PRACTICE

+ Invests across alternatives: private equity, hedge funds, infrastructure and real estate
+ First investment in 2002
+ $5.6 billion invested/committed
+ 600+ diverse managers covered
+ 150+ investments

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Ask the Expert: How Investment Programs Can Become More Diverse

What are the key factors to investing with diverse managers? Are the sourcing and investment processes the same as with more established managers? What's to be gained, and what are the risks? In the following, **Derek Jones, GCM Grosvenor Managing Director** and leader of the firm's private equity diverse manager practice, answers these and other frequently asked questions about investing with diverse managers. He addresses important considerations for investors, from the reasons behind the dramatic upswing in the number of fund launches by diverse managers to questions about sourcing, implementation and maintaining a robust pipeline.

Derek has 33 years of private equity investment experience and, for the last 12 years with GCM Grosvenor, he has focused on sourcing, sharing best practices and allocating capital to diverse private equity managers. In this role, he has helped numerous corporate and public pension plans and other institutional investors build diverse manager programs from the ground up. Derek was formerly the Treasurer and currently serves on the Board of the National Association of Investment Companies (NAIC), the largest industry organization serving the interests of minorities in private equity. As an expert in the field, Derek addresses some questions we've heard recently.

Q WHY IS THERE AN INCREASING INTEREST IN INVESTING WITH DIVERSE MANAGERS?

I believe there are three main reasons. First, there is much evidence that investing with diverse managers is good business. Surveys, studies, and our own research and experience support diverse managers' ability to produce attractive risk-adjusted returns and the potential to generate alpha.[*] One recent study conducted by NAIC, to which GCM Grosvenor contributed, notes that its universe of diverse manager funds reliably outperformed relevant benchmarks over long time horizons.[1] The study attributes performance primarily to smaller fund sizes, differentiated deal flow, and managers' investments in first-time funds.

We believe in the efficacy of diverse manager investing; over one-third of our private equity capital commitments in the last three years have been to diverse managers.

Second, diverse managers are receiving more attention because many endowments, foundations, and pension funds (and the entities that govern them) are focused on ensuring equal access to capital in their investment programs. Some investors are influenced by external sources like regulatory requirements. Others may be influenced by C-suites, boards, and trustees who are realizing the diversity of their investment management falls short of the progress they have made toward diversity in other parts of their businesses.

*** Please review the disclosures following this report.**

(continued)

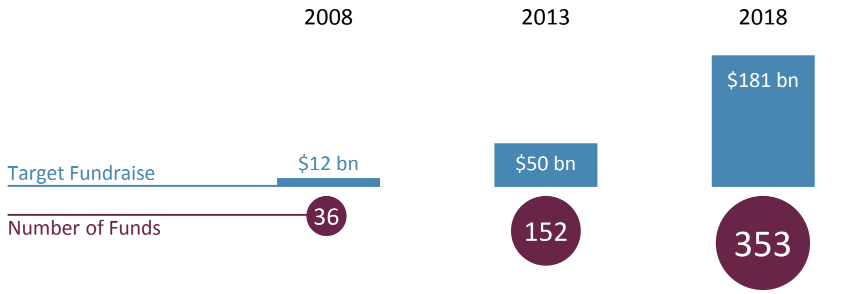
DEFINING:
Diverse Private Equity Managers

Firms in which diverse professionals account for at least 33% of firm economics; diverse professionals are:

+ African Americans
+ Asian Americans
+ Hispanics
+ Native Americans
+ Women
+ U.S. military veterans
+ Persons with disabilities

Third, the population of diverse manager talent is much deeper than in prior years. Diverse professionals have risen to more senior levels of established firms, giving them the experience and track records to launch their own funds. The number of funds launched by diverse private equity managers has increased nearly ten-fold from 2008 to 2018.[2]

Significant growth in funds launched by diverse private equity managers:
Data based on GCM Grosvenor's evaluation



Q ARE THERE PARTICULAR SKILLS OR TRAITS COMMON TO THOSE WHO HAVE SUCCESSFULLY ACHIEVED MORE DIVERSITY IN THEIR INVESTMENT PROGRAMS?

Yes, we do see common traits. For one, these investors have a thorough knowledge of the diverse manager universe. They meet frequently with managers and are proactive in sourcing talent rather than relying solely on placement agents or general partners (GPs) that approach them. Doing so helps build their reputations as investors that are accessible to diverse managers. At GCM Grosvenor, we have an "open-door" approach toward meeting diverse managers, which has allowed us to see hundreds of opportunities and commit more than $1.6 billion to diverse private equity managers over the past three years.

In our experience, successful limited partners (LPs) immerse themselves in the diverse manager community and actively participate in relevant industry organizations. I see firsthand how being involved with associations of diverse professionals can create new relationships and strengthen existing ones. GCM Grosvenor typically sponsors or attends over 25 industry conferences per year and hosts two premier industry events that spotlight diverse and emerging managers.

Established investors in this space also have the ability to consider managers with complex stories or shorter track records. These LPs are prepared to invest early in funds that may be smaller and less well-known and can often move quickly to execute co-investments with managers.

Finally, LPs in this space often have diversity on their boards and investment teams. I don't think this is necessarily a requirement, but there's an element of "walking the walk" in doing so.

> "Over one-third of our private equity capital commitments in the last three years have been to diverse managers.

Q WHAT ABOUT LPS WHO WISH TO INVEST WITH DIVERSE MANAGERS, BUT ARE SHORT ON RESOURCES?

Investors can supplement their efforts by working with an advisor or consultant at varying levels of engagement. For example, LPs in the early stages of diverse investing may look to their advisors for help with sourcing, due diligence, and implementation. Others may play a more active role by participating in deal flow calls to get an advisor's views on managers, or invest alongside the advisor in its commitment to a particular manager.

It is important that the LP holds its advisor accountable by asking the right questions: How many diverse managers did the advisor meet with last year? How much capital did it allocate in the past three years? Is the advisor acting on behalf of all its clients, or just those that request diversity? How diverse is the team

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itself? Which diversity-focused conferences did senior members of the firm attend? How many within the organization spend the majority of their time focused on investing with diverse managers? Answers to these questions may help an LP assess whether the advisor is fulfilling its fiduciary responsibilities by executing broad and inclusive searches.

> When we are asked by LPs, *"Why isn't my manager roster diverse?"* we often answer with another question: *"Are you looking in the right places?"*

Q CAN AN LP APPLY ITS SAME INVESTMENT PROCESS TO SOURCE AND EVALUATE DIVERSE MANAGERS?

Yes and no. Remember, diverse managers are not an asset class based on ethnicity or gender. A buyout manager is a buyout manager and is evaluated by investors on the same criteria – alignment, track record, how long the team has worked together – and nothing should be compromised. LPs are looking for benchmarked performance and, just because it's a diverse manager, the standards for underwriting don't change.

That said, there may be nuances in sourcing – how and where investors are finding diverse managers. LPs must be able to sort through complexity to identify and evaluate managers that may lack a long history or typical track record. But that's a common theme in emerging manager investing broadly. It's about rolling up one's sleeves and doing the work to understand the deals a manager has done and vetting its performance.

So, when we are asked by LPs, "Why isn't my manager roster diverse?" we often answer with another question: "Are you looking in the right places?" Frequently, that answer is "no." But establishing a network of diverse managers does not happen overnight. At GCM Grosvenor, we have been evaluating emerging and diverse managers since the early 2000s and have identified and follow over 350 diverse private equity funds, with over 100 investments in the market today.

Q ARE THERE RISKS ASSOCIATED WITH INVESTING WITH DIVERSE MANAGERS?

There isn't anything unique about the investment risks associated with diverse managers. In general, alternative investments are subject to risks such as strategy risks, manager risks, market risks, and operational risks, but investors with diverse managers are often exposed to a different type of risk: perception risk.

We have come across some investors and consultants that are of the mindset that there is additional risk in seeking investments with people that are somehow different than them. That is a misperception. The fact that some believe they must step outside of their comfort zone to evaluate a person or team whose story is not "typical"– that's perceived risk. In our experience, meeting with and evaluating a team like this is an opportunity, not a risk.

Q HOW CAN LPS HELP KEEP A FLUID PIPELINE OF TALENTED DIVERSE MANAGERS?

When it comes to maintaining a pipeline, LPs should hold themselves and their advisors accountable. It is not about meeting quotas, but LPs may benefit from being more "intentional" in asking themselves questions like: How many diverse managers have we met with this quarter? And if we've not met with many, why not? Who's in the pipeline? It is critical that an investor, its staff, and advisor leave no stone unturned to find the very best opportunities.

It's also important that LPs stay connected to the feeding organizations that supply talent, as there is a need for established managers to have their own diversity of staff and promote growth among diverse professionals. Considering that only 19% of employees at alternative investment firms are female – and just 11% occupy senior roles[3] – investors should help drive change and influence managers by inquiring about their diversity initiatives and stressing the importance of having an inclusive culture. ■

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ADDITIONAL NOTES

1 NAIC, "Examining the Returns," 2017. Full report at http://naicpe.com/wp-content/uploads/2017/10/2017-performance-report.pdf. **Past performance is not necessarily indicative of future results. No assurance can be given that any investment will achieve its objectives or avoid losses.**

2 Data as of December 31, 2018. Information based on GCM Grosvenor's evaluation of the diverse manager universe.

3 Source: Preqin.

BIOGRAPHY

Derek Jones, Managing Director, Private Equity Investments

Derek Jones is a member of the Private Markets Investment Committee and serves on the Global Investment Council. He leads the firm's private equity co-investment team and diverse managers practice. His responsibilities include relationship management, deal sourcing and conducting due diligence. Prior to joining GCM Grosvenor, Mr. Jones was a Managing Director in the Customized Fund Investment Group of Credit Suisse Group AG. Prior to Credit Suisse, he was a Managing Partner at Oncore Capital, as well as a General Partner at Provender Capital. He started his private equity career at Prudential Insurance Company as part of Prudential Equity Investors, which subsequently became Cornerstone Equity Investors, where he was a partner. Mr. Jones received his Bachelor of Arts in Economics from American University and his Master of Business Administration in Finance from New York University. Mr. Jones serves on the Board of and was former Treasurer to the National Association of Investment Companies. He is a recipient of the Pacesetter Award from the National Association of Investment Companies in 2012, and the UNCF Keeper of the Flame Award in 2016. He was also recognized as one of the 75 Most Powerful Blacks on Wall Street by Black Enterprise Magazine in 2011.

ABOUT GCM GROSVENOR

GCM Grosvenor is a global alternative asset management firm with over $50 billion in assets under management in hedge fund strategies, private equity, infrastructure, real estate and multi-asset class solutions. It is one of the largest, most diversified independent alternative asset management firms worldwide. GCM Grosvenor has offered alternative investment solutions since 1971.

Our small, emerging and diverse managers platform is robust, with over $17 billion in AUM and cumulative commitments. We support this platform with an experienced team, network of contacts and broad sourcing capabilities. We host industry-leading events that inform and raise the visibility of managers while providing institutional investors access to these managers. **Read more about Consortium and the SEM Conference:**

New York Hilton
Midtown

Consortium2019
Diverse + Women Managers Conference
16th annual | June 12 + 13, 2019

Fairmont Chicago
Millennium Park

SEM2019
Small + Emerging Managers Conference
13th annual | November 14 + 15, 2019

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