

EMERGING OPPORTUNITIES IN PRIVATE MARKETS

SPECIALIZED STRATEGIES GAIN GROUND

GP stakes investing and portfolio finance are attracting investors in search of stability, diversification and yield.

Private markets continue to be a major focus for institutional investors pursuing diverse sources of return amid an uncertain economic and geopolitical environment. Assets in private markets strategies — including private equity, private debt, real estate, venture capital and infrastructure — are expected to grow at a 9% compound annual growth rate through 2033, when AUM is expected to reach \$59 trillion, according to Bain & Company.¹

Yet in some of the more overcrowded segments, concerns are emerging around liquidity, rising defaults and declining valuations. That's encouraged more institutional allocators to turn their attention to expanded and relatively untapped avenues within private markets investing to access diversification, stability and yield.

Two such areas are general partner stakes investing — acquiring minority ownership interests in private asset managers — and portfolio finance, which refers to senior-secured lending solutions backed by diversified portfolios of private market assets, including corporate credit, real estate debt, secondary portfolios and GP interests. While neither is new, both strategies are benefitting from the explosive growth in private markets amid the heightened demand for liquidity.

"The most powerful secular trend is the growth of private markets," said Dadong Yan, head of Portfolio Finance at Barings. "Over the last decade, we've seen investors increasingly seek to increase their overall allocations to private markets, as well as those looking to diversify and gain exposure to different parts of private markets."

GP stakes investing is "a strategy that's here to stay, because GPs will continue to need capital solutions," said Michael Shedosky, managing director and co-CIO at Azimut Alternative Capital Partners, which focuses on lower middle market GP stakes investments.

For portfolio finance, growth has been driven by both demand and supply factors. Historically, "banks provided portfolio financing from their own balance sheets, but those balance sheets haven't kept pace with the rapid expansion of private markets," Yan said. "As a result, a funding gap has emerged — one that institutional capital is now stepping in to fill."

TAKING OWNERSHIP

GP stakes offer differentiated access to private markets by providing investors with returns generated through ownership in the economics of individual managers.

GP stakes investing offers broad exposure to a private market firm's entire platform and can provide a more stable and diversified return stream with long-term growth potential. "When we acquire a GP stake, it allows us to share in the GP's management fees, carried interest, portfolio company fees and capital appreciation," Shedosky said.

Azimut's GP stakes strategy is focused on the lower middle market, which Shedosky defines as "GPs with fee-paying AUM of roughly \$500 million to \$3 billion." The strategy's appeal lies in its distinctive return profile: stable, recurring income streams from management fees provide credit-like downside protection and consistent yield, while capital appreciation from the GP's growth and carried interest distributions deliver private equity-like upside. This combination positions GP stakes as a compelling option for investors seeking both stability and growth.

Azimut differentiates itself by targeting GP stakes in lower middle-market private markets firms at a growth inflection point. Azimut believes the segment offers several advantages, including the potential for proprietary deal flow, structures that emphasize downside protection and liquidity. Jeff Brown, Azimut's co-founder and co-CIO, indicated that these advantages were in part a by-product of the favorable supply-and-demand dynamics that exist only in the lower middle market, where there are more than 2,500 firms and less than 10% have sold a stake.

That opportunity set is likely to expand. According to Collier Capital's Summer 2025 Global Private Capital Barometer, 38% of LPs surveyed expect new firm formation

to outpace GP consolidation over the next three to five years, suggesting that the universe of potential GP stakes targets will continue to grow, he noted.

The interest among managers to fund growth by selling a minority stake is substantial, Brown said. “If you’re a private equity firm and you see some of your competitors taking on capital from a GP stakes manager to grow, you say ‘I need to look at this and figure out what I should be doing,’” he said. “We like these dynamics. We’re growth investors and we can access many opportunities to deploy capital.”

Selection criteria

Azimut focuses on acquiring 10% to 25% ownership interests in managers that specialize in buyout, growth equity, private credit and infrastructure strategies. To identify the most attractive GP stake opportunities, Azimut targets three key characteristics. “We have an eye on the industry-level trends, but we’re looking for a GP that has three main attributes: alignment of interests, a history of building businesses and production of alpha with ongoing competitive advantage,” Shedosky said.

“First, we’re looking for a GP that has great alignment to their business, which means they typically have invested significant personal money into the business,” he said. “We like a GP that eats their own cooking.” It is critical to understand why a GP is pursuing a GP stake transaction. “Are they looking to create a long-term, durable firm through the transaction? If a GP wants to put a valuation on their firm and allow junior partners to buy into the partnership or award certain partners equity, we look at that as increasing alignment overall for the firm.”

Additionally, Azimut is focused on how a GP intends to use the capital they receive, and it has a strong bias towards transactions in which a GP reinvests the capital into the business alongside their LPs in the form of a GP commitment. “When GPs sell a portion of their management fee profits in order to increase the size of their GP commitments, by definition they are becoming more aligned to fund performance and less so to asset gathering,” Shedosky said.

Second, Azimut seeks to invest in managers with track records of building and growing businesses. “We’re looking for a GP that has demonstrated an ability to attract and retain talent, because at the end of the day, these are human-capital-intensive businesses,” he said. “We also want someone that has a good vision for the growth of their business and a vision that we can believe in.” The third key is performance. “We want someone that has an edge in their space that we believe can persist, and that differentiates them from peers,” Shedosky said. “We are looking for someone that’s generating alpha.”

Private markets businesses with those three characteristics typically are firms with the potential for high recurring revenue, contracted cash flows and no debt. “These firms offer the characteristics we seek — strong downside protection with attractive annual yield while maintaining private equity upside potential as the manager grows,” he said.

One area that Azimut avoids is commodities-based strategies, which it believes carry too much risk. “When you look at how many private markets firms are available in the lower middle market, we don’t have to reach for risk to come up with really good returns,” Brown said.

Timing and liquidity

Brown said that Azimut is seeing two types of institutional investors interested in GP stakes deals: those that have already invested in GP stakes with larger managers and see Azimut as a small-cap complement, and those that have never invested in GP stakes. The second group typically has two concerns: the long duration of large capital GP stake fund structures and liquidity. Azimut addresses both concerns through its fund structure, which is a traditional 10-year vehicle, and its successful exits of pre-fund GP stakes positions across multiple liquidity pathways, he said.

“We have proven the liquidity advantage that our segment of the market enjoys. We exited our investment in Kennedy Lewis to another GP stakes fund, and we exited our investment in RoundShield to a strategic buyer. These were full exits, not engineered liquidity,” Brown said. He added that the strategy is one in which “you’re paid to wait” until ultimately exiting the position, because investors earn consistent income through participation in management fees and carried interest while building capital appreciation over time.



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- Michael Shedosky
Azimut Alternative Capital Partners



FINANCING WITH A PRIVATE-MARKETS TWIST

Portfolio finance provides an opportunity to expand a fixed-income portfolio via investment-grade exposure.

With corporate bond spreads trading near historically tight levels, institutional investors have been searching for ways to improve the return potential of their fixed-income portfolios without adding an extra layer of risk. One sector they may have overlooked — perhaps as it falls under private markets investing — is portfolio finance.

“We are seeing investors grapple with the fixed-income or investment-grade portion of their strategic asset allocation,” Barings’ Yan said. The combination of private market growth and investors’ ongoing search for yield — especially given tight public corporate spreads — has created a “collision point.” This, along with heightened credit risk concerns, is prompting more investors to consider private investment-grade credit.

“Recent headlines around defaults and volatility are top of mind for investors,” he said. “We’re in the early stages of a secular shift, with investors seeking to upgrade the quality of their credit exposure. Moving from a single-B-type of credit risk to a triple-B or single-A-type of credit risk can provide greater confidence and better position portfolios to weather potential market corrections or credit downturns.”

Lending against a diversified portfolio of assets, rather than a single borrower, is one way that Barings’ Portfolio Finance team helps address investors’ credit risk concerns. At the same time, this approach offers the potential for higher returns compared to traditional investment-grade credit, especially in today’s environment of tight spreads.

Investors can feel stuck when looking at public-market spreads. “They want to maintain high credit quality, avoid dipping below investment grade and aren’t looking to increase equity exposure,” Yan said. “Our platform addresses that pain point by offering an alternative solution by generating alpha within the investment-grade universe, so investors aren’t forced to take on incremental credit risk or pursue speculative-grade investments.”

Yan’s team takes a focused approach to the private investment-grade market. “Our value proposition lies in leading and controlling transactions. We deliver customized financing solutions tailored to the needs of our asset manager borrowers, and through that process, we generate alpha for our investors,” he said.

Control and alignment

A feature that sets Barings apart is its direct origination approach, which allows the firm to maintain control throughout the lending process and potentially reduce the risk for investors. This approach also fosters strong alignment. “We focus on aligning interests with our borrowers, implementing structural protections and prioritizing capital preservation,” Yan said. “These are top priorities for both our investors and our team as we underwrite and structure deals.”

For the Barings Portfolio Finance team, alignment also means customizing solutions to meet institutional investors’ portfolio objectives. But investors first need to determine whether portfolio finance fits within their private credit allocation or overall core fixed-income allocation. Some investors also include the strategy in their absolute return allocation, he said.

Portfolio finance offers a risk profile similar to core fixed income — high quality, investment grade and defensive. “The challenge is understanding that this is a private asset class,” Yan said. “For investors who group private IG within their private credit exposure, the strategy can both enhance their portfolio’s credit profile and add diversification.”

For investors who view portfolio finance as an absolute-return strategy, more akin to a hedge fund replacement, there are other potential advantages, Yan pointed out.

These investors are typically seeking a certain level of return over Treasury yields. “That’s exactly what we aim to deliver in investment-grade portfolio finance.”

Then comes customization. “This is the tailwind behind portfolio finance — the rise of different types of vehicles, the sophistication of LPs and their demand for customized exposures,” he said. “We’re building solutions that directly address our investors’ needs, whether in the private credit or fixed-income part of their portfolios.”

Experience matters

With over \$32 billion invested in portfolio finance, Barings is one of the largest nonbank lenders in the sector. Underpinning this scale is a highly specialized sourcing and underwriting process.

It all starts with experience. “Too often, firms enter a space attracted by the value proposition but lack a proven track record or true origination and underwriting expertise,” Yan said. “That’s a risk we see in the market today. Our platform has over 30 dedicated professionals, and all we do is portfolio finance.”

Barings’ position as a subsidiary of MassMutual also shapes its conservative approach to lending. In portfolio finance, that translates to high-quality transactions with an eye toward capital preservation — characteristics that are especially valuable in today’s investment climate.

“Throughout our history, we’ve had zero losses, no payment defaults and no missed interest payments,” he said. “That’s a testament to our DNA and the differentiated platform we’ve built within an insurance company, where capital preservation is paramount.”

This heritage also influences how Barings sources and structures deals. The firm maintains long-standing relationships with many dozens of borrowers, with approximately 75% of the platform’s deal flow coming from repeat business, Yan said. “This is a defining characteristic of our platform, and the fact that borrowers want to do more business with us is the strongest endorsement of our partnership model,” he said. Still, Yan and his team conduct rigorous due diligence on every deal, reviewing each borrower’s systems, processes, underwriting and controls to ensure their ability to meet debt obligations.

As institutional investors navigate an evolving private markets landscape, both GP stakes and portfolio finance offer differentiated entry points. While GP stakes provide equity exposure to the growth of private asset managers themselves, portfolio finance delivers investment-grade fixed-income alternatives with attractive risk-adjusted returns. Together, these strategies reflect the continued maturation and diversification of private markets — creating new pathways for institutional allocators seeking stable yield and long-term growth.

¹ Avoiding Wipeout: How to ride the wave of private markets, Bain & Co. <https://www.bain.com/insights/avoiding-wipeout-how-to-ride-the-wave-of-private-markets/>



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Barings



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