

# Alternative Investing In PruFunds

(Information is as at 30 June 2022, updated in August 2022, next update will be as at 31 December 2022, updated in February 2023)

This update from the M&G Treasury & Investment Office (T&IO) aims to provide an insight into the characteristics of the alternatives portfolio within the PruFund range of funds and the strength of various teams within M&G Investments who T&IO work with to create, manage and monitor underlying investments.

This update covers the standard rather than Planet versions of PruFund.

We hope to highlight the key differentiators and strengths including;

- The resource and expertise of the M&G Alternatives team and other teams within M&G Investments
- The global exposure to high quality companies and assets
- Using large scale institutional funds to best capture opportunities in private markets
- Ability to invest in development projects
- The ESG credentials of many alternative assets

The term alternatives covers a broad range of strategies and sub-strategies with different return drivers and characteristics. However within PruFund, we classify alternatives as; Private Equity, Infrastructure, Diversifying Strategies and Private High Yield.

The value of any investment (and any income taken from it) can go down as well as up so your customer might not get back the amount they put in.

## Characteristics of alternative portfolios within the PruFund range of funds

- **A vast opportunity set** – The team look to capture opportunities wherever they arise, leveraging a network of contacts and expertise across the globe
- **Private markets** – Investments are typically in the private markets, which are less liquid than the public equity markets, but often offer enhanced returns
- **Diversification** – the strategies are less correlated to your more traditional asset classes such as listed equities and corporate bonds
- **Expertise** – M&G has over 20 years experience of investing in alternative assets. The market is opaque and difficult to access so the quality of the investment team and their due diligence approach to finding and maintaining managers is critical to return generation and risk management
- **Environmental Social Governance (ESG)** – All new managers are ESG assessed pre-investment and continually monitored. The team actively engage with managers to share feedback from their systematic proprietary scoring model to help their partners improve their processes
- **Performance** – Each opportunity is assessed in terms of risk and reward and would expect to pick up an illiquidity premium
- **Long-term** – investments will often be held for many years and make them ideal for the PruFund range of funds

## Portfolio breakdown of PruFund Growth and PruFund Cautious

### PruFund Growth\*

Asset	Strategic Asset Allocation (% of total fund)		Fund Name	Investment Style	Internally or Externally managed
Private Equity	4.64	1 x segregated mandate	Portfolio of Private Equity	Active	Internal
Diversifying Strategies	1.74	1 x segregated mandate	Portfolio of Hedge Funds	Active	Internal
Infrastructure	2.78	1 x segregated mandate	Portfolio of Infrastructure	Active	Internal
Private High Yield	1.46	1 x bespoke mandate, 1 x segregated mandate	M&G Catalyst – Capital Fund, M&G Private Asset Fund (PAF)	Active Active	Internal Internal

\* source T&IO and Pru Actuarial team as at 30.06.2022

### PruFund Cautious\*

Asset	Strategic Asset Allocation (% of total fund)		Fund Name	Investment Style	Internally or Externally managed
Private Equity	2.38	1 x segregated mandate	Portfolio of Private Equity	Active	Internal
Diversifying Strategies	2.13	1 x segregated mandate	Portfolio of Hedge Funds	Active	Internal
Infrastructure	2.01	1 x segregated mandate	Portfolio of Infrastructure	Active	Internal
Private High Yield	1.59	1 x bespoke mandate, 1 x segregated mandate	M&G Catalyst – Capital Fund, M&G Private Asset Fund (PAF)	Active Active	Internal Internal

\* source T&IO and Pru Actuarial team as at 30.06.2022

## Want to know a bit more about the M&G Alternatives team?

M&G Alternatives is part of the investment division of M&G plc and they manage the private equity, diversifying strategies and infrastructure allocations of PruFunds. The Private High Yield allocation will be covered further on in the document.

They are comprised of 27 investment professionals split into three dedicated investment teams – Private Equity, Real Assets (Infrastructure) and Diversifying Strategies and two functional specialist teams, Operational Due Diligence and Portfolio Management.

Total asset under management for M&G Alternatives was £10.1bn as at 30 June 2022\*.

There are several areas where the team believe they add value;

- Their institutional approach and the brand and scale of M&G plc allows them to receive preferred investment terms and have a strong negotiating hand with their partners

- They enter into what are long-term relationships with strong alignment and the appropriate legal protections
- The ability to be a cornerstone investor of size allows them to access scarce and differentiated opportunities
- Their flexibility, scale and willingness to look at newer opportunities has allowed them to be an early adopter of emerging trends such as solar energy
- There is strong governance surrounding the alternatives portfolio and the Operational Due Diligence team ensures the highest level of quality when assessing managers
- They work closely with the T&IO Manager Oversight team to ensure the investments match the philosophy of PruFund

\* Source M&G Alternatives, estimated NAV for 30.06.2022

Due to the sheer scale and complexity of alternatives we thought it would be useful to provide more detail on each of the component parts.

# Private Equity

Private equity funds typically use either buyout or venture capital strategies. Buyout refers to buying a controlling stake in private companies, often financed through debt. Venture capital involves buying equity stakes in small/young companies with the aim to provide financing and expertise to help them grow.

## Private equity within PruFund

- The team was first established in 2000 and currently manages or advises on £5.7 billion of private equity assets globally\*
- Primarily invests into limited partnerships of buyout, growth equity and venture capital funds with an emphasis on the mid-cap and large-cap segments of the market
- Direct co-investments allow them to increase exposure to attractive companies alongside fund commitments which reduces weighted-average portfolio fees and improves net return, as these are frequently offered on a fee-free, or reduced-fee basis

\* Source M&G Alternatives, estimated NAV as at 30.06.2022

## Case Studies

Some examples of the wide variety of investments held:



Co-investment alongside **Hosen Capital into Kilcoy Global Foods (KGF)**, a global premium food solutions provider with a focus on premium beef and other animal protein products.



Investment into **One Peak Growth III Fund** which targets investments in high growth software and tech-enabled service companies. Highlights of the Fund include, the ability of One Peak to (i) source high growth companies; (ii) source deals on a proprietary basis and (iii) structuring deals with strong downside protection.



Investment into **Summa Equity III**, an Article 9 Impact Fund managed by Nordic headquartered Summa Equity Partners (SEP). SEP seeks to invest for growth in purpose-driven businesses behind long-term secular trends, namely UN SDG aligned themes of 1) Resource Efficiency; 2) Changing Demographics; and 3) Tech-Enabled Transformation.

# Infrastructure

The M&G Alternatives Real Assets team invest globally into Infrastructure, in areas like utilities, transport, and power, as well as Agriculture and Natural Capital, either through funds or as co-investments. The team prioritise defensive assets with natural or contractual protection and investments often have strong cash-flows with a degree of inflation linkage.

## Examples of Infrastructure investing within PruFund:

- Common sectors include Energy (power, transmission, storage), Transport & Logistics (ports, rail, roads, freight), Water & Waste (water treatment, recycling), Telecoms (fibre, data-centers) and Social (hospitals, and schools)
- Investments can be made at different points in an assets life cycle and typically have long hold periods, varying from 5 to 40 + years making PruFund an ideal investor

Some examples of the wide variety of investments held;

- **Ridgewood Water & Strategic Infrastructure Fund II;** a fund focused on investments in water, transportation and energy transition in the US
- **True Green Capital IV,** a strategy focused on distributed (Commercial & Industrial and community) solar. True Green are an experienced developer and operator in this niche part of the renewables markets. Whilst more complex, harder to access and scale than utility scale renewables, the M&G Alternatives team believe that the returns on offer are significantly more attractive
- **Investment into Solum Partners III,** a strategy focused on building vertically integrated, sustainable farming businesses. This is a recently formed General Partner but is a highly experienced team with strong institutional backing

We believe many of the investments into Infrastructure have contributed positively through;

- Developing, constructing and operating offshore wind and solar projects across the world
- Aiding the renewables transition through investing in grid infrastructure, including battery storage
- Supporting businesses through efficient, local power and heat generation solutions
- Roll-out of fibre networks across Europe, the US and Asia, including across rural communities
- Enabling 5G networks through small-cell towers
- Electric Vehicle (EV) charging networks and EV fleets (e.g. buses)
- Building and operating highways in emerging markets
- Supporting the global logistics industry through investments in railroads, and the provision of railcars and trailers

# Diversifying Strategies

The M&G Diversifying Strategies team aim to provide uncorrelated returns through investments in hedge funds and private markets.

## Hedge Funds

Hedge Funds are pooled investment vehicles aiming to generate absolute returns. There are many different investment strategies run by hedge funds, including relative value, event-driven and equity-related. Depending on their strategy, hedge funds may utilise short-selling, derivatives trading and leverage to enhance returns.

Example hedge funds held within the portfolio include

- **Holocene**, a US long short equity platform generating consistent alpha
- **Brevan Howard**, an established macro hedge fund platform that we access via multiple products from their range

## Distressed / Special Situations

Asset class focussed on distressed, dislocations or special situations (e.g. asset sales or capital raises) via equity debt or equity. The COVID-19 pandemic has created an attractive global opportunity set given the stress experienced across many sectors and regions.

The team expect to see opportunities for deployment within sectors like travel, hospitality, aircraft leasing and retail.

# Private High Yield

The Private High Yield allocation within PruFund is managed by various teams within M&G Investments. Part of the Catalyst strategy contributes to this allocation, which has the added benefit of 'non-financial returns' – contributing to a sustainable economy.

## Spotlight on Catalyst

The strategy of the Catalyst funds are to provide long-term flexible capital to tackle environmental and social challenges with the key areas of focus being Climate, Health and Inequality.

### The team

- A global international private assets team of 35+\* based in London, New York, Singapore and Mumbai
- Since the launch of Catalyst in 2021, they have committed £1.5bn\* in 30+ investments across 6 continents to several ESG, Sustainable and Impact Investment opportunities
- The team draw upon M&G's extensive resources in: Fixed Income, Equities, Infrastructure, Private Assets and Real Estate

\* As at 31.01.2022

## The strategy

The Catalyst strategy:

- Has an objective to achieve an attractive financial return whilst typically investing in assets that demonstrably contribute to a sustainable economy
- Seeks opportunities across the globe to invest in businesses which might otherwise struggle to access capital to develop and grow
- Will typically invest to improve environmental and social outcomes as categorised by the themes of climate action, environmental solutions, circular economy, social inclusion, better health, better work and education as core components of a sustainable economy. The objective will be to establish a pro-active role in many of the Investments to reduce negative and improve positive impacts

## Example investments

**Greencore Construction:** The Catalyst team acquired a majority stake in the UK's most sustainable housebuilder, whose energy efficient homes lock up more carbon than is emitted over their lifetime, including during construction.

**Storegga:** Investment in a UK based Carbon Capture & Storage business that is pioneering carbon removal and reduction solutions for a net zero world.

**TIER Mobility:** Investment in Europe's leading shared micro-mobility provider. The company provides light electric vehicles which helps cities reduce their dependence on cars and offers a convenient, eco-friendly and cost-efficient transport option.

# Environmental, social and governance factors within alternatives

We believe that alternative assets can lead the way in meeting global sustainability targets. All new investments are ESG assessed pre-investment by the M&G Alternatives team and continually monitored. The team actively engage with underlying managers to share feedback from their systematic proprietary scoring model to help their partners improve their processes.

M&G Alternatives have been investing in renewable energy for close to a decade, and a large part of where they have been investing in recent years already has an environmental or sustainable angle. The team have been continuing to integrate ESG strategies and investments into their processes, for example:

- M&G Alternatives launched 'The Real Impact Fund' in June 2022. Existing investments provide exposure to a broad range of opportunities including renewables, energy efficiency projects, batteries and EV charging infrastructure, rural fibre businesses, sustainable agriculture platforms, and related technologies that can help accelerate the climate transition
- The M&G Alternatives team have continued engagement with the General Partners they work with when considering investments for the new Real Impact Fund to ensure that there is a clear understanding of industry best practice, and GPs implement adequate measurement and reporting initiatives. As an example, the team were able to help shape the Ridgewood II fund strategy to better align it with our impact goals
- The M&G Alternatives team have engaged on various industry working groups and discussions including the IIGCC's Net Zero Infrastructure Consultation

## Case Study

In 2016 the team established a vehicle alongside a specialist investor and operator of European solar assets to invest in operating solar plants in Italy. It was a highly fragmented and inefficient market at the point of investment, with a need for consolidation of various solar plants in order to improve generation, cost of capital and create scale for other future buys. They felt that higher returns were on offer than in other parts of Europe and there was the opportunity to create significant value through the creation of a scaled portfolio.

100+ individual assets were acquired over a 5 year period, with generation capacity of ~150MW, making it one of the largest portfolios in Italy. In the financial year 2019/20 59 kilo-tonnes of CO<sub>2</sub>e was avoided which is equivalent to 19,000 cars off the road or 66,000 UK homes powered.

The solar portfolio was sold in early 2022, generating an IRR in excess of 25% (net of GP fees).



# Summary

The M&G Alternatives team continue to see interest in alternatives assets grow and are seeing increased demand for capital across each of their strategies allowing the team and PruFund to deploy into exciting opportunities. The institutional approach, brand and scale of PruFund as well as the long-term approach makes it an ideal investor for alternatives allowing investors to gain access to an array of alternative income streams.

The flexibility, scale and willingness to look at new and innovative opportunities has allowed the team to be an early adopter of emerging trends which has been beneficial to portfolios for many years and they continue to research new opportunities to introduce into PruFunds.

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