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INVESTMENT ALLOCATIONS

How Canada's BCI stays liquid in an illiquid market

The $173bn institution is offloading PE stakes via secondaries as it looks to deploy more capital into directs, global PE head Jim Pittman tells PEI.

Liquidity is at a premium in 2023 as LPs the world over grapple with a comparative dearth of private equity distributions and a congested fundraising environment. It is for this reason that Canadian pension giant BCI finds itself in a rather enviable position.

Under the leadership of global head of private equity Jim Pittman, the C$233 billion ($172.8 billion; €158.2 billion) public pension fund has spent much of the past decade using the secondaries market to cultivate a comparatively liquid portfolio of illiquid assets.

"What we're seeing is a knock-on impact with less liquidity coming back in terms of sales. Those pension plans [that have] allocated heavily to private equity are less liquid themselves, so they don't have as much money to recommit to new funds," Pittman tells Private Equity International.

"The one thing that we've been doing for the past seven years since I [joined] is making sure that we have a continuum of capital coming back. So we've used a secondary market to sell funds that were what we consider to be non-core or lower performing – just not beating strategic or performance benchmarks."

BCI has offloaded C$4 billion to C$5 billion of private equity stakes via the secondaries market since Pittman's appointment. The most recent of these transactions took place in June, with another expected to close by year-end, Pittman says, noting that the pair will

generate "up to a billion-and-a-half" of liquidity. He declined to share the specifics of the two transactions.

"One of the things that… myself and the executive team often say is: 'In an illiquid market, we don't want to be illiquid ourselves'," Pittman adds. "So we always want our own dry powder of a few billion dollars to sort of take advantage, and you never want to be forced to sell."

BCI isn't alone in utilising secondaries to generate liquidity. LP-leds accounted for about 61 percent of the $44 billion of secondaries transactions completed in H1 2023, per data from Greenhill. According to affiliate title Secondaries Investor, notable sales included Kaiser Permanente's $6 billion portfolio sale, New York State Teachers' Retirement System's sale of a portfolio valued at around $6 billion, and Norinchukin Bank's process to sell a portfolio that is around $1.5 billion or more in size.

LP portfolio pricing across asset classes rebounded to 84 percent of net asset value – down 2 percentage points on H1 2022 figures – and up considerably from the 78 percent of NAV seen in the second half of last year, according to Jefferies.

"It not an ideal market to sell," Pittman says. "But you've got to take a view as to, is the NAV inflated? Is that the true value of the portfolio? In our view, we've been taking somewhere in the order of magnitude 15 percent discounts, but we believe our portfolio is 10 percent overvalued in general.

"We don't think we're taking a very large discount, we just think we're reflecting what's going on in the market. And liquidity is an important factor just to be able to have C$2 billion available to continue to do deals."

Deployment drive

BCI deployed a record C$9.8 billion into private equity last year, per its 2022-2023 Corporate Annual Report. Of that total, C$3.7 billion went to 14 direct investments, including additional funding for existing assets. One particularly noteworthy deal was space intelligence business Maxar Technologies, its largest-ever direct private equity investment.

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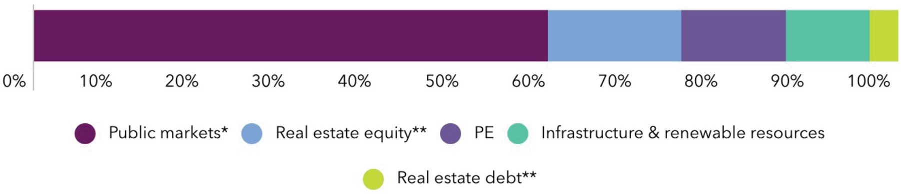
BCI IN NUMBERS

PE was BCI's second-largest alternative asset class exposure as of 31 March 2023



*Comprises public equities, fixed income and other
**RE equity and RE debt are managed by QuadReal Property Group. Gross assets under management are shown net of leverage issued by QuadReal.

Source: BCI

The institution's mammoth deployment was funded in part by cash distributions received from "timely" direct exits and secondaries sales in late 2021 and early 2022, the report said.

"In the more recent sales, we are selling good performing assets, but strategically we want more liquidity to do more directs," Pittman says. "So we're selling some layers of the funds in order to reutilise it in directs."

Directs have been an increasing focus in recent years, and now account for around 42 percent of BCI's private equity C$28.3 billion portfolio. "The benefit of that is the fee load that we carry," Pittman notes. "There's 500 basis points difference between investing through a fund scenario versus direct, and if we're running 42 percent of our book directly, we're saving a lot of that sort of fee burden."

This rationale appears to have been justified: over the last five years, BCI's private equity programme delivered an 18.2 percent annualised return, almost double its five-year benchmark of 9.2 percent. The programme returned 4.7 percent last year against a benchmark of -1.8 percent.

The US is BCI's largest target market for private equity, representing 47.8 percent of its portfolio. As part of its focus on the US, BCI opened a New York office in 2022 and hired an additional 13 investment professionals. It is gearing up to do something similar in Europe this year, affiliate title Buyouts reported in January.

Asia-Pacific represented 9.7 percent of the portfolio as of 31 December, though Pittman says the institution allocates around 15 percent to the region. BCI and its Canadian peers have come under increasing government scrutiny in recent months over their exposure to the region's largest market, China.

"Asia's shifting," Pittman notes. "Obviously, China is a much more difficult arena to do deals, given the sort of friction that's not just US-China, but also Canada-China to some degree. And so we've been very active in Korea and somewhat active in Japan; less active in Southeast Asia and we're not really that active in India in a private equity sense… We still think, you've got to invest in countries that have positive GDP, and it tends to be Asia's got higher GDP than North American markets."

Madeleine Farman and Kirk Falconer contributed to this report