PRIVATE MARKETS OUTLOOK: INVESTING THROUGH A NEW MARKET CYCLE

Kelsey Butler 00:02

All right. Well. Thanks, everybody. We're lucky enough to follow a soccer legend, but, you know, we have some legends in their own right. So thank you, gentlemen, for joining. Going down the line, we have Jonathan Sokoloff, managing partner at Leonard Green & Partners. We have David Razu, CEO of Afore XXI Banorte, and Bryn Gostin, head of equity strategy at Apollo. Thanks so much for being here. Well, I guess let's start really big picture. Wanting to hear a little bit about what you—like, your diagnosis of the private markets landscape right now, before we dive in a little bit further to some of these key themes. In a couple of sentences, where do you think we are right now? Bryn, I'll start with you.

Bryn Gostin 00:52

Well, maybe I'll just back it up one level even further. So where do we think sort of the macroeconomic backdrop is. It seems pretty clear that we continue to grow. The growth is probably unexceptional. It's also probably a little bit concentrated. But the economy in the US and on a more global basis is growing. The economy does feel—at least within our private equity business—increasingly fragile, and potentially later cycle, right? You have—and you've got central banks, I think that have a very hard job ahead of them because on the one hand, you have sort of the AI and hyperscaler economy that feels like it's still very much in growth mode, and then you have, certainly in the US, some of the more interest-rate-sensitive parts of the economy—whether that's housing or autos or credit card spending patterns—and those are probably more challenged. So what does this mean for the private equity markets and the private markets more specifically? Private and public at the end of the day are not that different, and so they're all affected by the same confluence of factors. I think you've seen some rebound in activity from a deal volume and from an execution and exit perspective in the private equity markets. It's probably more of a story of volume versus count because the number of transactions is still relatively subdued, which probably suggests that private equity as an asset class is much more mature today and requires more scale, more resources, and therefore you're seeing more getting done at the larger end of the market. But overall, I think things feel pretty good, relatively late cycle. So at least for us at Apollo, when we think about the opportunity set today, a little bit more value orientation probably makes sense versus some of the discount rates you have to think about in growth-oriented investing. And also just sort of the ability to pivot, if there is a little bit more of a cycle is probably a good thing to have in your toolkit.

Kelsey Butler 03:01

Okay. David, how about you? Where are we in private markets right now? Big picture.

David Razu Aznar 03:06

Well, I think that, of course, regarding Mexico, what we're seeing right now, it' , I would say it's a moment of growth in the faith of private markets. I think they've been increasingly useful. We AFOREs—particularly, pension funds—we have been going a lot more through private markets. But I would also say that I think we're starting to get to that point where we

need a change of cycle. And what I mean by a change of cycle is private markets seem to exhibit great returns. The problem is a lot of those are on paper. Of course, this has a lot to do with the J-curve, with the fact that they are maturing, that they're ready to deliver. But we're at a point, especially for pension funds, where we want to start seeing those valuations in DPIs rather than in decks or in a new instrument. But at the same time, I would say that the outlook I see coming forward is they're going to keep growing and we're going to keep demanding the different vehicles they can provide, but they're going to have to get more mature and provide with better returns and DPIs.

Kelsey Butler 04:34
Okay. Jonathan, bringing you in.

Jonathan D. Sokoloff 04:37
Okay, nice to be here. And just a quick background. So, managing partner of Leonard Green, a private equity firm in Los Angeles, but 41 years ago, I started work at Drexel Burnham with Mike Milken. [Noise] Whoa. So I really learned my early skills in the business from Mike. So it's particularly great to be here at the Milken Conference in Mexico City for the first time. One of Mike's crazy notions in the '80s was, remember it was the Mexican debt was trading at a big discount, and he wanted to buy all the Mexican debt up and exchange it to the Mexican government in exchange for Baja. And he was very serious about that, and it just gives you a sense of how Wild, Wild West-crazy things were 40 years ago, and just how dramatically they have grown and matured, where the private markets are massive, bigger than we ever dreamed they'd be and continue to be. But it's never a straight line. It's always zigging and zagging and crises and problems and this and that. But, overall, the private equity industry is a giant part of the economy now, continues to grow. We've had three or four years of underperformance versus the public markets. Never had that before, so that's an issue. But overall still a very vibrant part of the economy and a very important asset class for most of our LPs.

Kelsey Butler 05:51
Okay. Excellent. All right. Now let's talk about some of the controversial stuff. So, we'll start with a four-letter word: exit. We're seeing a logjam on exits right now. What finally breaks it? What needs to change to actually start seeing some of those occur? I'll start with you, Jonathan.

Jonathan D. Sokoloff 06:14
Well, look. So, I've been in again in the private equity business now for 40 years, and I think the big crisis today is exits and the lack of exits. And Bain Consulting comes out with their report every March about the state of the industry, and they bemoan the lack of exits and that PE firms should have roughly 20 percent of their NAV return to their investors every year for the life cycle to be healthy, and the industry is running half to two-thirds of that. And, this year they mentioned one of the main reasons for that is because GPs have marked their companies too high. The marks are not accurate. They're not real, and they can't sell their companies at their marks. So that is a real problem. Now, over time, it all has to get sold. In our business, we have assets. Our business is to grow companies and then sell the assets and return the money. So, it's a big problem. Just remember the only time in I—everyone talks IRR, IRR all the time, quartile this, that, whatever. The only time an IRR is 100 percent accurate is when you sell. Everything else is kind of fiction. We make it up to the best of our abilities, some more aggressive, some more conservative. And a lot of transactions occur on those privately marked values. And if GPs are going to continue to mark their companies too high, no one is going to buy them at the mark. So, we're not supposed to give commercials for ourselves on this stage, but we've had a lot of exits and all of our exits are at or above our mark, which means on a relative basis, our marks are okay. So I think many GPs have gotten it now, the DPI. They're getting the crap beat out of them by the LPs. They have to send money back, and they're starting to manage their values and their marks so that within a year or two, they'll be able to sell stuff at their mark. Because one of the mistakes a lot of GPs make, including us, is you fall in love with your companies. You think they're worth more than they are. You wait for the dream price, and the dream price comes occasionally in your career, but not very often. And most of our exits have been in prices probably lower than we thought we were going to get, still good enough to transact and still at or above our marks. So that's what has to happen more. There's this huge logjam of companies owned by PE firms that has to be sold in the next five years. And GPs are just going to have to capitulate and start to sell them at a price the market will pay, not a price they think they're worth.

Kelsey Butler 08:49

Yeah. So Bryn, I want to bring you in here to either chat about exits or marks, which is another thing, controversial thing that I wanted to talk about. What do you think needs to change for marks to actually be a little bit closer to the truth? Here.

Bryn Gostin 09:07

Yeah. I mean, look, I think everything Jonathan said is correct. Distribution yields have gone from 20 percent over the past five years to closer to 10 percent. The sort of math on a 10-year term doesn't really work with 10 percent distribution yields. A lot of that is because you had periods of time in which managers were kind of underwriting multiple expansion into their kind of base case for an exit. And that's just very hard today because the deal cost index is very elevated. And the deal cost index is essentially a combination of the multiples that people have to pay to acquire assets, combined with the cost of financing those transactions. It's relatively high, and so what do you need to sort of like work through that? You probably do need some capitulation. The reason it's not happening is, again—also to Jonathan's point and your point—it's unrealized marks are actually something you can fundraise off of. And this is something we need from the LP community to increasingly pressure test. And I think you're starting to see it to pressure for realizations to actually be an indicator of a healthy performing fund versus marks on paper. And, eventually, as you get through fundraising cycles, you'll start to see a necessity to sell assets, and that will happen, over time. But remember, we now have $4 trillion of unrealized assets in the industry and a good distribution year in private equity is probably $400 billion, thereabouts. So you're talking about a substantial backlog that is going to take time. And the last thing I'll say is I just think, what we've seen since rates have gone up is sort of a realization that the private equity industry is maturing. And in a more mature private equity industry, you need, I think, a different toolkit to sell assets. I don't think you can just rely on the idiosyncrasies of any one deal team to sell a business today. Because it is structurally harder, whether you're talking about IPOs, you have to float at a much bigger discount today than you did five or 10 years ago. If you think about sponsors, fundraising is actually down, which means there's fewer sponsors to buy assets from those looking to sell. And then strategics, like look at everything that's going on geopolitically. It's just hard to have the confidence to transact as a strategic today. So what does that mean? I think what you need is really a dedicated team and resource to be thinking about exits through the life cycle of an investment. So that means from the moment you're underwriting an investment, you need a team that is pressure-testing how you're going to exit it during the ownership phase. I think you need, really sort of a team that's focused on actually working with the potential buyers on what is going to make this asset more attractive, potentially be acquired down the road. And then, this is, again, to Jonathan's point, you actually need the real discipline to take a good price and not wait for the best price. And it's easy to want to wait everyone kind of, if it's their baby, they want to wait for that last dollar of value. So it's challenging. I wouldn't bet against the industry. I think we'll figure it out. We saw a lot of this in the aftermath of the financial crisis, but it's going to take some time also.

Kelsey Butler 12:28

Okay. I love the agreement here. You can feel free to disagree, too, later on. We will. So, shifting gears, I want to talk a little bit about private credit. I'm old enough to remember when a $1 billion private credit deal was mind-boggling. Huge. Obviously we've come a long way since then. So, how is the growth of that market impacting things on the PE side? And how do you think it will in the future? Jonathan, I'll start with you.

Jonathan D. Sokoloff 12:55

Well, look. We're a huge user of credit. Our portfolio companies have over 100 billion of debt and we're constantly in the market borrowing, new, repricing, amending, extending all the other stuff. So, the private credit world has been a great addition to us as a source of capital. And generally it's a little more expensive capital with a more certain rate and terms. That's a trade we'll often make. But the term loan B market is still active. So, the more sources of capital we have, the better. And so we hope the private credit market continues to thrive. It's had some zigs and zags this year with redemptions and all kinds of other things. But, overall, it's still a pretty vibrant and an important part of what we borrow.

Kelsey Butler 13:38

Well—go ahead. Are you going to chime in?

Bryn Gostin 13:43

I could jump in quickly. Yeah. So, I would say a few things. The first thing is, so when we think about the private credit market that's in the news a lot, it's mostly sub-investment-grade direct lending. That's about a $2 trillion market, which is relatively small in the grand scheme of things. You know, it's a $40 trillion Treasury market by comparison. So I think the sort of degree to which this is a systemic risk is perhaps a little bit overblown. The much bigger and deeper credit market is mostly, even in the private markets, investment grade. And so, at least to us at Apollo, we don't really think that the big sort of difference between whether a credit is safe or not is whether it's public or private. It really comes down to the individual underwriting of those assets and those credits. And that's probably, in a current market backdrop where, generally speaking, things are still growing. It's probably, a relatively good part of the sort of capital structure to be in. That doesn't mean there aren't aspects of the credit markets that have risks, but I think it applies to equity as well. Software is the one we all know about. You know, software is potentially going to have a revaluation issue. Not all software is going to zero. That's certainly not the case. But some could be impacted. And if those businesses were valued at 15 or 20 times and now they're valued closer to 10 times, call it, if you put 50, 40 percent LTV, loan-to-value, on the business as the equity holder, that's potentially a real problem because there might not be a lot of equity value that's sort of available to you once you need to refinance. And so that's where we think about the risk sitting. It's more about the credit underwriting and the part of the market. We're fortunate—again, we certainly don't want to spend too much time on an Apollo advertisement—but we've been pretty disciplined about that part of the market in particular.

Kelsey Butler 15:57

Okay. Jonathan, I'll use your word zig zags rather than Jamie Dimon's word. But do we think the worst of the private credit kind of turbulence is over? And I'll open that up to anyone that wants to jump in.

Jonathan D. Sokoloff 16:14

Yeah, I'm not sure I know, because the real test is going to come when loans mature—

Kelsey Butler 16:19

Right.

Jonathan D. Sokoloff 16:19

—and they have to be refinanced. And if they're refinanceable. So, if a private lender has something loaned at seven, eight, or nine times, and it's not easily refinanceable, what are they going to do? Are they going to say, pay me back? Well then the issuer has no ability to pay them back. No one's going to give them money. So they're going to have to just kind of kick the can down the road, probably. And also what private lenders live in fear of is losing earning assets because they want to keep their assets out there getting interest paid. So it's this dilemma they have about wanting to keep better credits. But I think as these software loans mature that were based on ARR or whatever, and that's not, we're not in that business, so I don't know much about it, it's going to be a day of reckoning. I'm sure there'll be a lot of carnage along the way, and some huge amounts of money will be lost.

Kelsey Butler 17:11

Carnage. I'll write that word down for future use.

Jonathan D. Sokoloff 17:15

Has to be. Yeah.

Kelsey Butler 17:16

Shifting gears, we are at a Mexico-focused event, so I want to drill down a bit into private markets here in Mexico. The government has been very vocal about private capital playing a role in infrastructure development in the country. When you think about that in the private market sphere, what does that really look like? As for you, and Afore XXI specifically, does that mean putting money in private credit funds that are lending to some of these projects? Does it look like other vehicles or other things that haven't maybe been defined yet?

David Razu Aznar 17:51

Yeah. Well, I would just like to go back a little bit, because it was, I mean, there was really nothing much left to be said after what Jonathan said on the exit drought that we've been living. But it's great to—I have to say it's great to hear those words in the mouth of a GP. It's great that there's a realization that this is going on. And I really believe that it's as simple as you put it. It's just a market thing. There's a price for an asset. And if the part selling believes the price is higher, then the exit doesn't happen. What you have is a valuation and a rollover of an instrument. And then you have the GPs split in two: those who deliver cash to the LPs and those who deliver valuations. And the problem for pension funds is workers do not return valuations; they need cash for their retirement. So, I think it's great there's a realization of that. And as David was saying, I truly hope you guys will figure it out soon enough. So we can see an end to this exit drought. I mean, what's been happening in Europe and even in the US, where 78 percent of all the exits were mega exits that you can—there's so many companies and so many assets that are not giving cash back that I think we're getting to a point where we should be concerned. So, let me get back to this. In Mexico, it's even worse. Why? Just for a simple reason: we're pretty new to it, especially in pension funds. And of course, this sort of projects have a pretty deep J-curve, sometimes. So, I mean, it's rather logical that you're not going to be receiving DPIs yet for some of the investments we've made. That accounts for a large part of it. But the problem is we do need to start seeing that in a lot of the vehicles we're investing in. And going back to your question now, let me land where you started, with what's happening. I think it's a great moment for private capital in Mexico, for private equity, and also for private credit. I think the moment Mexico is living right now, where you have a pretty sound macroeconomic history going on. I mean, yeah, you have some concerns maybe with the deficit and some fiscal issues that you have to check. But in the end, when you see that you have roughly half the GDP in debt, which is pretty healthy, I would say. You have a pretty stable rate exchange, record numbers in foreign reserves.

David Razu Aznar 20:47

So, and at the same time, you see a country that it's becoming really indispensable for the distribution chains of North America. Just the last semester, exports from Mexico to the US grew 28 percent. That had never happened. It's a lot, just year on year. And 40 percent, this is a number that I'm going crazy about, 40 percent of all the servers used in the US are built in Mexico. Why am I talking about these things in this part? Because what you see is the new distribution chains and the new supply chains that are taking place need a manufacturing powerhouse and that is Mexico. But for Mexico to become an efficient manufacturing powerhouse, it needs a lot of electricity. It needs water. It needs roads. And all of these things take you to private equity vehicles that can help fund them. What we need from those, and we're seeing a great opportunity in that. We want to invest in that. All of AFOREs are going to be pretty involved in these investments. Actually, the, I guess the state is counting on pension funds to do this. And it's a great opportunity for a lot of GPs to come and create different vehicles. What we need about that is to make sure we have certainty in the contracts. We have very clear rules and guarantees, so we can actually use these vehicles. Because, I mean, the money is going to keep coming and we're going to keep growing our assets under management. And this is, of course, and clearly, one of the best investments we can make, provided we get the right instruments and we start seeing DPIs in the vintage that comes from 2019, when target-date funds started.

Bryn Gostin 22:59

Okay. May I just? You know, it's a really interesting point you make about, it's sort of—it's an unsaid part of what you're kind of like intimating, which is that so these sort of like easy way to think about rates of return is, well, if I'm an allocator, why do I even want my money back? If I'm just getting 20 percent rates of return, then I should just do that in perpetuity. And if you give me my money back, then it just means I have to go and reinvest it. But the truth is, that's just not the way private equity works. The reality is most businesses cannot tolerate 20 percent costs of capital indefinitely. And, as you get later in life, those returns become much more muted. Which is why, exactly to your point, to have a healthy private equity ecosystem, you need these distributions to return more back to historical levels, even if that means some interim period of pain.

David Razu Aznar 23:51

Absolutely, that's precisely what I'm trying to say. And especially when you're talking about. I mean, because you have a different sources of patient capital, as I call it. But when you talk about retirement funds, when you talk about pension funds, distributions are, in the end, as an LP, our main goal, because we're going to be needing that. And because of the target-date funds, we know that our generations, the generations in our portfolios are growing older and we're going to

have to start distributing. And we cannot wait. We're not like waiting for the market to give us the right price for an instrument. No, once someone gets to retirement age, we have to give them their money, and our mandate is to give them the best replacement rate possible. So, if there are some vehicles that are giving us valuations instead of cash, that really complicates things for us in the retirement horizon.

Kelsey Butler 24:55

Yeah, absolutely. We know that there were some recent regulatory changes in Mexico that opened the door to pensions, investing more in alternatives. But if you look at the data systemwide, the allocations are still in the single digits. So, would love to hear from you about how you expect your private markets, kind of investment bucket to grow in the coming years or change at all. Where are you now? Where do you expect to be in two, five years?

David Razu Aznar 25:24

Yeah. It's great that you say it because, you know, there's been a lot of discussion and a lot of debate about the increasing of the limits of structured investment for pension funds. And what's funny to me—I mean, I'm of course I'm all in for that increase in limits. I think we need more diversification, and I think that the more we can actually allocate to structured instruments is going to be better. But the thing is, we've never even reached the limit that we had before, you know? So it was funny to be talking about the increasing of the limit when we were, as an industry, I'm not talking about XXI Banorte, we were not reaching it. What I think is going to happen, to your question, is I think we're actually going to be allocating, I think we're going to be filling that bucket pretty soon, I hope, because of the conditions I took a while earlier to describe. I think Mexico, it's in a position right now because of geopolitics and because of supply chains and because of expertise and specialization that the country has to create a lot of infrastructure. And that infrastructure can only be financed by—I mean there's no way public money is going to be enough for that infrastructure investment. There's not even a way, and I would say this, that national money, it's enough. You need to have foreign investors coming in, which is also good news because then what you're going to have are, hopefully, best private equity standards investing in projects in Mexico. And I think that's going to give us the chance. These mixed projects, even the mixed projects in Plan México, which I see with very good eyes, I think they're going to give us a chance to actually, for the first time, use this bucket fully.

Kelsey Butler 27:27

Okay. Well, we have two global firms sitting on the stage. Do either of you, Bryn or Jonathan, want to talk about the opportunity, you see to participate in this kind of infrastructure evolution?

Jonathan D. Sokoloff 27:41

Yeah, well, I'm not sure we're the right firm to talk about infrastructure. We do have a portfolio of 50 businesses, and about 10 of them have reasonable operations in Mexico. We have over $1 billion of revenue, over 1,000 employees. And we're growing. So it's a huge and a vibrant market for our companies. But, you know, we haven't invested in companies in Mexico, but our companies in America have invested in Mexico. Because when you invest in a company, you also have to have a clear path to exit. We talk about exits. How do the capital markets function in Mexico? If you want to exit an investment in the public equity markets here, whatnot. Still a challenge. So work to do here in Mexico to get those markets working to the level where international capital will want to come in here because they want to have a way out. But again, look, this is a giant economy. I think most Americans don't appreciate the industrial manufacturing powerhouse that Mexico has quietly become. And it's a hugely important trading partner to the United States. And it's a great opportunity for us as investors. So we're bullish on Mexico. And Mexico has challenges like everybody else, and the government and the cartels and all the other stuff we read about all the time. But in spite of all that, it seems to be doing okay.

Kelsey Butler 28:56

We're doing just fine. Bryn, do you want to talk a little bit about where Apollo sees potential opportunity to participate in that infrastructure play?

Bryn Gostin 29:09

Yeah. So look, I focus on the equity side of our business, so I won't get too much into kind of how we think about investing from an infrastructure and credit perspective, but there's absolutely opportunity to do that within Mexico. It's a growing and vibrant market and I think increasingly a very commercial market. And that's what you want. When I look at it through our private equity lens, what I say to myself is—and what we say to ourselves is—where we're investing in businesses in

Mexico, we want to make sure that what we're doing is leaving better companies than we bought. So we own Aeromexico. The thing that we're proudest about that is today it is, and not everyone knows this, it is one of the best run airlines from both a financial metric perspective and from a customer satisfaction perspective. And so, when you're leaving better companies that you came in and acquired, you're probably partnering pretty well with the local economy.

Kelsey Butler 30:05

David, I'm going to put you back in the hot seat a little bit. You know, want to talk a little bit about the dynamic between local managers and global ones when you're deciding to write a check, how are you thinking about that? What considerations are coming into play to make that decision?

David Razu Aznar 30:26

Well, it really doesn't make a difference for us if it's a local or global manager, what we're actually looking at is pretty much what's being put on the table. So, if you have a sound governance mechanism and you can see that—I'm going to start with something I've been saying maybe the whole evening, but—the whole afternoon—but if you have a track record of exits, for example, that's going to be a great point. If I can see that you have been actually providing with returns, I don't care whether you're local or global. If you have a sound internal governance with the proper committees, with participation of independents, if you have proper reporting, standardized reporting, then, I mean, honestly, the fact that it's global or local doesn't make a huge difference. When I was saying, what I was saying before about the good thing that we're going to have foreign investment for all the infrastructure plan, is because I am a true believer that knowledge transfer and good practices transfer between different firms. It's something that actually happens. And it's great to see a landscape in Mexico with more different GPs with different ways of doing things putting forward. And so they can all learn from each other. And honestly, what I believe is that we're going to be seeing in the next few years is an improvement of the practices of both global and local GPs in Mexico.

Bryn Gostin 32:21

It's a really important point, right? Because of course, local investment matters. But what matters just as much is the ability to create a sustainable retirement for your pensioners over time. Right? And if you do that, you're going to transform your economy over generations. And I think—not to backtrack a little bit on private equity for a moment, but I will if that's okay. You know, there's been—even on stage, right?—we've had a fair amount of sort of negative sentiment around the industry. Distributions have been down. IRRs are down. Returns over the past few years have been more muted relative to public equity markets. On the back of that, you've seen challenges fundraising. Well, the last time you put those confluence of factors together private equity delivered some really, really go-forward attractive returns, which was essentially in the aftermath of the financial crisis. And so I still believe that private equity can play a very important role in the pension system for the Mexican people over time. And what we don't want to do, I think, is get too short term in the way that we evaluate it. Because if all we do is look at the past three years of returns, don't even think about public or private equity. If all you ever did is say, how did this asset class do over the last three years? And if it's the best one, that's where I'm going to put all my capital. That's probably not been a winning strategy. And so the way to think about deploying into private equity and private markets more broadly is really to acknowledge the fact that vintage year risk is your single biggest risk, that the best way to do it is to deploy consistently and methodically over time, which it seems like that's how you're thinking about it. Because even if you time the cycle right, deployment in private equity and private markets happens with a lag. So even if you think, you know, I've got exactly the right moment of time to put capital to work in the private markets, the actual deployment will probably lag that. So, overall, I think it continues to be a really, really strong asset class and can play a big role.

David Razu Aznar 34:26

I think it's really important what David just said. I mean, I've been talking all this time about the relevance of distribution, but of course, in no way should, and especially not for pension funds, the short term returns, even if they're in cash, the actual gauge for deciding whether to invest or not in something. When I speak about DPIs, when I speak about distributions, I'm talking about track record, when I see that you have actually delivered in the past. But I'm not going to be only investing, and most likely are not going to be very attractive to me, investments that promise me I'm going to give you a great return just in one year and then I don't know what's going to happen. No, of course not. Because you know that in the waiting, that's what we call patient capital, in the waiting is where you can have the best returns. The problem is when

the waiting is waiting—after waiting—and all you're left with are a lot of crazy valuations that nobody believes anymore. But of course that you have to put on a long-term lens in order to decide where to, where to invest. And just to finish what the question that you started is, you see, sometimes people can find in the way pension funds, at least in Mexico, approach different investments that are brought to us or opportunities that are brought to us is as we're reluctant. It's not reluctancy. It's just fiduciary duty. In the end, what we want is to make sure, and David was saying it, that we're going to get the best possible replacement rate for workers from this. And they're, honestly, at this point, after 29 years of the system, I think we've delivered more than 10 percent return in that period. More than half of the assets under management in the pension system are returns, are not the actual capital that was invested. So I think we've learned to sometimes we make the best investment, sometimes not so good. But I can tell you we have a pretty good checklist, which is what I was talking about before, that can actually tell us if that's an investment that's worthy. And what we want to believe is that in this stage that is coming with all the opportunities that I do believe there are, especially because of infrastructure, GPs are going to be up to the size of it. And they're going to provide us with good vehicles for being part of that project.

Kelsey Butler 37:35

All right. We're coming up to the end of our time. So I'm going to ask everybody to get out their crystal balls. So, the year is 2031. None of us will have aged a day, but it's five years from now. So, what do you think we'll look back on as the biggest misstep in private markets? You know, five years from now, what will we look back on and say: I can't believe that happened. That was truly wild. Bryn, I'll start with you.

Bryn Gostin 38:02

I was hoping you were going to start down here so I could think about an answer, but that's fine. So, I think—so let's look at it from two lenses. Let's look at it from the investor's lens, from the GPs' lens, and from the allocators' lens. I think from the investor's lens, what we're going to look back on is, GPs who get too focused on top-down thematic investing. I think that's going to be problematic over the next 5 to 10 years. Because it's not that you don't want themes and understand what's going on in the global economy, but if all you do is sort of say, I want, data centers are hot, so I'm going to go buy data centers. I think you're probably not doing enough underwriting, and you're probably going to find yourself in a place where you are—you just find a data center to buy. You find that thematic investment to buy. It's like a hammer chasing after a nail. You find the nail so you hit it. And I think that's going to create problems. And I think that's part of the reason we've seen people overpaying for assets. Because overpaying actually worked in an era of ultra easy accommodative monetary policy. We're just not in that world anymore. And that's why purchase price matters. But it matters in particular in today's world where you have a higher deal cost index. And then from an allocators perspective, I think it's the sort of—and you're absolutely seeing this—some investors that say, okay, well, you know, public markets are doing really well, so I'm going to shift there and reduce my allocation to private markets. You're probably going to be timing it wrong. And I think there's a lot of reasons to think that public market returns are going to be more muted over the next several years. Even if you just look at the law of large numbers, if you think a lot of those returns have been driven by, you know, the Magnificent Seven, for example, they've gone over the past five or six years from five or 10 trillion to 25 trillion. Do we expect them to go to 100 trillion? You know, it's a pretty linear and concentrated bet. And so stick-to-itiveness, I think, with your private portfolios will probably pay better dividends over time.

Kelsey Butler 40:10

Okay. We are at time. So want to say in two sentences, either one of you chime in, what do you think will be the biggest misstep?

David Razu Aznar 40:18

I'm going to say it in two sentences. Everything that David said, I agree. But there's one other thing that I think that in five years we could be looking at and we're going to be, we could be regretting, which is speed. The speed to which we are actually creating the proper vehicles for investing in the opportunity we have. This to me, there's a window and it's precisely more or less five years. So I hope we move a little bit faster with different opportunities that can be presenting to us.

Kelsey Butler 40:55
Jonathan. Last quick word.

Jonathan D. Sokoloff 40:56
Well, look, I still think private equity in my view, is a better governance model, a better operating model, a better value creation model for corporations. That's what we've done for 40 years. And I think it will continue to be so. But I do think we've gotten over our skis. There's too many firms. There's too many deals. A lot of deals were too expensive. And there's going to be a wrenching Darwinian shakeout in our industry in the next five or 10 years. It's going to be really painful and many firms will either wither or go away. And allocators' jobs is to find the firms, not just that had a good deal or two in the go-go years, but have stood the test of time with whatever cycle, crisis, war, interest rates come, because over time the good firms continue to deliver mid-teens high teens, net returns. And over time, that should be good enough for anybody, no matter what the Magnificent Seven do or the tech world or everything. There's always a flavor of the month, but you have to have a longer time horizon. And look at the AFOREs here, and look at, Australia has 4 trillion in their superannuation funds, they're a huge part of the global capital markets. And Mexico's next up. It's exciting.

Kelsey Butler 42:02
All right. We'll leave it there. "Darwinian shakeout," put it on a T-shirt. Thank you so much, gentlemen. Really appreciate the time. And thanks, you guys, for listening in.

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