



OMNIGENCE ASSET MANAGEMENT

The Benefits of Investing in GP Stakes: Unique Alpha

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ABSTRACT:

Investing in GP stakes—minority ownership positions in alternative asset management firms—is an emerging strategy within private markets. This paper explores the benefits of GP stake investing, including stable cash flows, capture of long-term growth, access to diversified revenue streams, and resilience in volatile markets. The global GP stakes market has grown from less than \$10 billion in 2015 to over \$50 billion in cumulative transaction volume by 2024, underscoring increased institutional interest in this strategy.

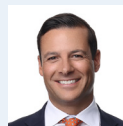
INTRODUCTION:

As the global alternatives industry surpasses \$20 trillion in assets under management (AUM), institutional investors are seeking new ways to access the economics of private markets. One of the fastest-growing strategies involves investing directly in the General Partners (GPs) of these firms. GP stake investing refers to acquiring a minority interest in an alternative asset manager's operating company, thus gaining exposure to its fee-related earnings and long-term carried interest.



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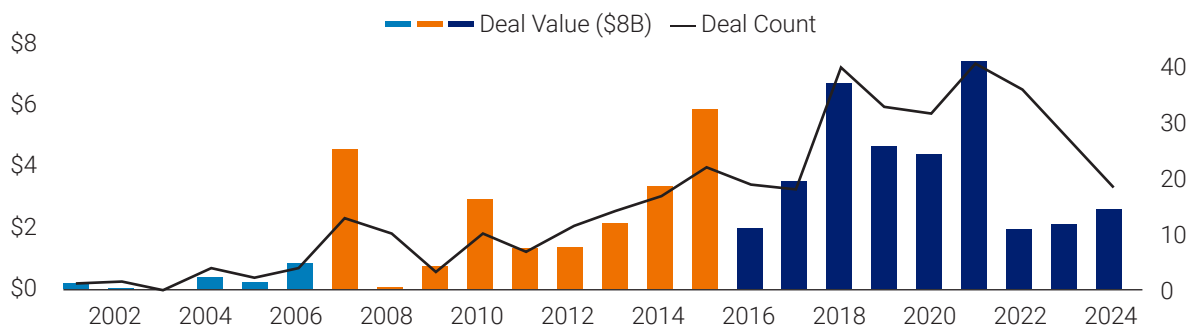


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Global PE GP Stakes Deal Activity (2008-YTD As of 10/09/2024)



Source: Pitchbook

Unlike traditional limited partner (LP) investments, which tie capital to specific funds, GP stakes provide equity-like exposure to the ongoing enterprise value and income stream of the manager.

The strategy has gained momentum among pension plans, sovereign wealth funds, and insurance companies seeking cash-flow generating, low-beta exposures.

KEY MARKET DRIVERS OF GP STAKE INVESTING:

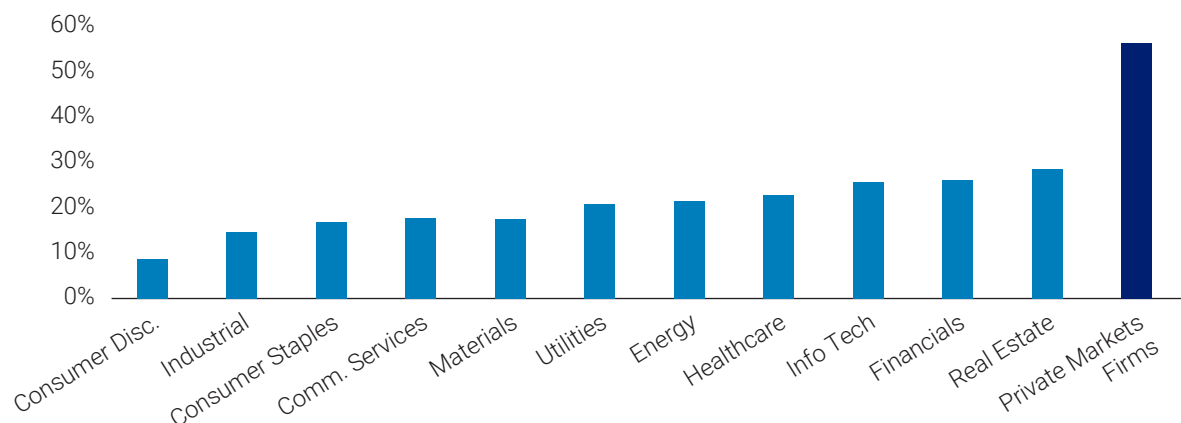
- The primary benefit of GP stakes is access to recurring management fee revenues and performance-based carried interest. These revenue streams are largely uncorrelated with public markets:
- Management Fees: Typically range from 1% to 2% of AUM and are contractually agreed for long-term closed-end funds. For example, a firm managing \$20 billion in AUM at a 1.5% average fee would generate \$300 million in annual management revenue.
- Performance Fees: Carried interest represents a share of profits from successful investments, often 20% after a preferred return. In a strong vintage year, this can significantly boost earnings.

- **Predictability and Durability:** These fees are collected regardless of short-term market volatility, making them highly resilient. In volatile environments, GPs often continue to raise funds, particularly for opportunistic or distressed strategies. According to Preqin, global private capital fundraising exceeded \$1.5 trillion in 2023, with a large share allocated to long-duration, locked-up capital vehicles.
- **Embedded Optionality:** Investors in GP stakes benefit from the embedded call options on future fundraising and carried interest, while enjoying steady base fee cash flows that resemble fixed income in consistency.
- **Enhanced Yield and Return Potential:** GP stakes offer highly attractive cash yields relative to other private market strategies. Base returns typically range from 7% to 10% annually, with the potential to reach mid-teen IRRs as portfolios mature and carried interest crystallizes. For example, a \$100 million stake in a mid-size private equity firm could generate \$7–9 million in annual fee-related earnings (FRE), with additional upside from carried interest realizations over time.
- **Intrinsic Downside Protection:** The management company's fee streams are largely contractual and recurring. Even if a GP does not raise future funds, the ongoing revenue from existing fund vintages can often recoup 70–90% of the original stake investment over the holding period. This embedded downside protection differentiates GP stakes from many other equity-like private investments.
- **Firm-Level Compounding and AUM Growth:** Successful GPs can significantly scale over time. A firm with \$5 billion in AUM today may reach \$15 billion within a decade, either through new fund launches, entering adjacent strategies (e.g., credit, secondaries), or inorganic growth via acquisitions. As AUM grows, so does FRE, which drives up the valuation of the management company and, by extension, the value of the stake.
- **Strategic Optionality:** In addition to cash flows, GP stakeholders often gain access to co-investments, secondaries, and new product launches, providing both strategic value and additional financial upside. These optionalities are difficult to replicate in traditional fund investing.

PARTICIPATION IN THE GROWTH OF ALTERNATIVES:

GP stake investors are well-positioned to benefit from the secular growth of alternatives:

- **AUM Expansion:** Global AUM in alternatives has grown at a CAGR of ~11% over the past decade. Firms like Blackstone and KKR have seen AUM double in under five years.
- **High Operating Leverage:** A \$10 billion increase in AUM might add \$100-150 million in fee revenue with only modest increases in cost, resulting in incremental EBITDA margins exceeding 70%.



Source: Azimut Alternatives, Publicly Traded Private Markets Firms Have Historically Achieved Higher EBIT Margins Than Other Industries

- **Multiple Fund Families:** For instance, a large multi-strategy firm may run private equity, private credit, infrastructure, real estate, and growth equity vehicles—each with its own AUM and fee structure.

This growth dynamic means that a GP stake can behave like a compounder: even without exit events, value accrues steadily via increased AUM, improved margins, and new fund launches.

LONG-TERM ALIGNMENT AND STRATEGIC INFLUENCE:

While GP stakes are typically minority interests, investors can still gain meaningful influence and strategic benefits:

- **Governance Rights:** Many GP stake transactions include board observer rights or consent rights over key decisions like IPOs or major capital raises.
- **Alignment of Interest:** Founders and principals typically retain large equity stakes, ensuring their incentives remain closely aligned with outside investors.
- **Co-investment Access:** GP stakeholders may gain preferential access to co-investment and secondaries across the platform.
- **Adjacencies:** Investors can sometimes negotiate preferred economics or access to emerging strategies (e.g., continuation funds, NAV lending platforms, etc.) that the manager builds.

RESILIENCE DURING MARKET DOWNTURNS:

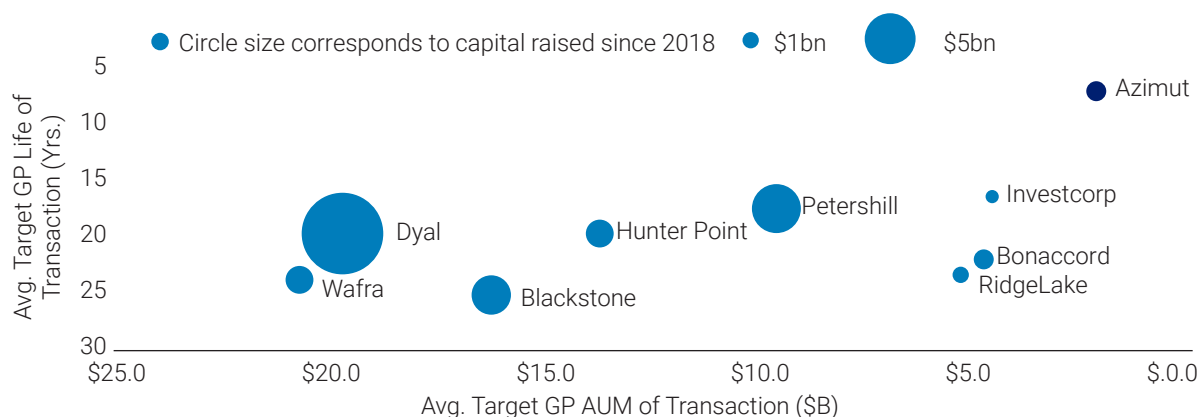
Historical performance indicates that well-managed GPs remain profitable even during economic stress. GP stake investors are also largely insulated from mark-to-market fluctuations in fund NAVs and instead benefit from the durable economics of the GP entity itself:

- **2008 Global Financial Crisis:** Most major private equity GPs retained their fee income and some saw carry realizations post-crisis as asset valuations rebounded.
- **2020 COVID Crisis:** Fundraising dipped briefly but recovered strongly; Blackstone reported record AUM growth in Q3 2020. GP-level fee income remained steady.
- **2022-2023 Volatility:** Top-tier GPs with infrastructure and private credit arms saw record inflows, offsetting declines in equity carry.

GROWING LIQUIDITY AND INSTITUTIONALIZATION:

While GP stakes are inherently long-duration and illiquid, the market has grown more sophisticated:

- **Dedicated Platforms:** Firms like Blue Owl (Dyal Capital), Blackstone GP Stakes, and Petershill Partners have built diversified GP stake vehicles with periodic liquidity. For example, Dyal Capital IV raised \$9 billion and holds stakes in over 50 firms.



Source Azimut, GP Stakes Funds Market Map

- Secondary Markets: Institutional appetite for secondaries has improved price discovery and potential exit options. GP stake sales on the secondary market now exceed \$2 billion annually.
- Transparency: Managers now publish regular financials, NAVs, and investor updates, increasing confidence and pricing accuracy.

CONCLUSION:

GP stake investing offers unique access to the growth engine of private markets—the managers themselves. With recurring, uncorrelated cash flows, alignment with long-term secular trends, and enterprise value creation across fund vintages, GP stakes are growing segment of the alternative investment universe.

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