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January 2025

Private market assets in 2025

KEY TAKEAWAYS

- Risk-adjusted returns across many private assets should remain attractive as the world settles into a new normal where inflation and interest rates are likely to be structurally higher than the post-global financial crisis and pre-Covid era world.
- Often a source of stable income, private market assets should help reduce portfolio volatility as well as provide diversification.
- Private assets can play into long-term investment themes, such as the global demographic trends, the burgeoning demand for energy and decarbonization efforts.

FAVOURABLE MACROECONOMIC ENVIRONMENT FOR PRIVATE MARKETS

The Risk assets should find support in the higher interest rate regime. Even though rates may have peaked in many countries, cuts – notably by the U.S. Federal Reserve – are likely to be slower and smaller than many expect, in our view. Real U.S. GDP growth has averaged 2.3% over the last five years (which includes the sharp Covid contraction), which is a much higher level than 1.8% annual average over the 2010 to 2019 period. Furthermore, with the shift in U.S. politics, we expect to see renewed and even expanded tax cuts, which are likely to encourage growth and inflation.

Along with expected returns reflecting higher rates, several medium- to long-term factors are also likely to support private market assets, allowing investors to explore long-term investment themes. The exponential growth of artificial intelligence, particularly generative AI, is creating huge demand for energy and data centres, playing into both infrastructure and real estate. Ongoing plans to decarbonize economic activity and investment portfolios are creating further opportunities in power generation and transmission. Similarly in real estate, tenants and owners are seeking more efficient and environmentally friendly buildings. Along with providing essential food and goods for the world's growing population, natural capital investments are also addressing sustainability concerns.

Fiscal incentives from many governments around the world will also support private market assets, notably policies encouraging energy security and the transition to a low carbon economy. These policies will help drive capital to the sectors in which many private markets operate, and we expect them to remain a focus through 2024 and beyond.

INCREASING INVESTOR ACCESS

As more capital is needed to fund these attractive investment opportunities, asset managers are creating and adapting investment vehicles that meet the needs of smaller-scale investors. These differ depending on jurisdictions. In the U.S., we have seen steady growth in semi-liquid structures such as interval funds, non-traded real estate investment trusts (REITs), business development corporations (BDCs) and tender offer funds.
In Europe, common fund structures for retail investors include European Long Term Investment Funds (ELTIFs), Luxembourg UCI Part II Funds, and Long Term Asset Funds (LTAFs) in the U.K.

With opportunity comes risk, however. Investors need to understand the risks involved with these assets and the role they play in portfolios. Liquidity risk is more significant in private markets than public, and private assets should be considered a long-term investment.

Working with an asset manager with experience and expertise in private markets will help investors understand and manage some of these risks.

PRIVATE ASSETS: INVESTMENT CHARACTERISTICS

Private market assets continue to be a compelling source of risk-adjusted returns, diversification and in many cases income. Private assets are not traded on public exchanges. They can include debt, equity, real estate, infrastructure, farmland and timberland. While covering a broad range of asset types, they share similar investment characteristics in many instances:

Stability: Private assets by definition are not marked to market. Pricing in private markets should help avoid the short-term noise of public markets, reducing volatility.

Return potential: Limited liquidity has often been viewed as a disadvantage, but that same illiquidity creates opportunities. Private markets are perhaps best known for their high return potential compared with similar public assets.

Income potential: Long-term cash flows are a feature of many private real assets often with contractual payments that adjust for inflation.

Diversification: Private real assets generally have low or negative correlations with listed equity and bonds, and bring additional sources of alpha to a portfolio.

ASSET CLASS OUTLOOKS

Real estate

We see evidence of a recovery in the real estate market, with interest rates likely to be on a downward trajectory in many markets. Non-office-related private real estate has bottomed, as the capital and financial headwinds facing landlords have faded. Rent and occupancy growth are healthy, and investor demand is returning for most sectors. The improving climate is driving increased competition for real estate deals, an indicator of an impending recovery for the asset class.

These signals should encourage investors who have been fearful of the asset class amid higher rates to take advantage of opportunities that are underpinned by long-term, structural megatrends. In this regard, we favour global cities that have growing, educated and diverse populations. We see attractive investments across residential, industrial and especially non-traditional real estate sectors. Alternative segments such as medical office, senior and student housing, and self-storage should benefit from long-term demographic trends. The unprecedented demand from generative AI should support data centres.

While the office sector remains challenged globally, there are pockets of opportunity. Select European and Asia Pacific markets are starting to sprout green shoots, with some markets experiencing rental growth and low vacancy rates. Similarly, in the retail sector, which is arguably further along in its recovery and adaptation to consumer preferences, we see opportunity in necessity retail, such as grocery and convenience stores. These examples demonstrate that real estate is not a monolith, making the case for diversification within real estate exposure as well as in multi-asset portfolios.

Private capital

Slower-than-expected U.S. interest rate cuts reflect economic strength, and economic activity bodes well for private capital. GDP growth creates favourable operating conditions for the businesses investors can lend to (private credit) or take ownership positions in (private equity). And even as Europe experiences more tepid growth, the environment remains constructive for private capital.

We expect the investor-friendly private credit terms we have experienced over recent years, namely lower borrower leverage and higher yields, will sustain. Financing costs have reduced and should ease further. This should also help bring private equity buyers and sellers closer together on valuations, narrowing what has until recently been a wide price-expectations gap. Improved valuations are likely to create a virtuous cycle: As more investors realize their positions, private capital fundraising increases, which leads to more deployment.

With easier financing conditions and greater clarity on rates and private market valuations, private capital that has been sitting patiently on the sidelines is likely to come to the market. Participating in deals with the strongest risk-return characteristics will require a focus on building flexible and creative capital solutions that help businesses achieve their current and future objectives. We believe experienced managers with scale, a strong network of established relationships and access to deal flow are more likely to succeed for investors. But they will still need to guard against defaults, which can be done by maintaining a disciplined approach, creating diversified portfolios and supporting value creation in the businesses. Portfolios that focus on defensive sectors and are cautious on cyclicals should be well positioned when growth and rates are volatile. Private capital's active management style and long-term investment horizons should offer investor portfolios shelter from public market volatility, diversification and resilience.

Infrastructure

The long-term thesis for infrastructure assets is supported by steady demand for many of the essential services these assets provide. Economic activity relies on reliable and effective electricity grids and communications networks, waste and water management, and transport links. Inelastic demand and often a monopoly-type market position typically mean that infrastructure investments are non-cyclical, thus providing diversification and an ability to reduce overall portfolio volatility. Many also offer income from long-term contractual cash flows that often adjust for inflation or cost of capital, providing a degree of stability in difficult economic environments.

The AI boom is causing an unprecedented boost in power generation demand, with forecasts outstripping current capacity for generation and transmission in most economies. This creates opportunities in clean energy, including solar and wind infrastructure around the world, and we anticipate demand will also grow for nuclear energy, transmission infrastructure to accommodate new development, natural gas-related investments and data centres to support AI model-training and inferencing. Battery storage, as a critical solution to address solar and wind's intermittency, is another area expected to benefit.

Alongside power generation, investors focusing on sustainability will also see opportunities across other areas of infrastructure. These include environmental assets focused on repurposing waste and recycling necessary materials and minerals in limited supply; decarbonizing and optimizing transportation and logistics assets; and supporting scaling up electric vehicles.

Natural Capital

Long-term structural megatrends also support natural capital investments. Investing in sustainable timberland and farmland taps into the growing global population's demand for resources and supporting environmentally friendly and socially responsible food, fibre and timber production. And against the current backdrop of higher-for-longer interest rates and inflation, natural capital can provide portfolios with a level of inflation protection. Many of its products, such as food and building materials, are components of inflation indexes. Higher inflation means higher prices for many of these goods, which improves cash yields. Should higher prices sustain over the medium to long term, this is likely to be reflected in returns through higher asset valuations.

Timberland and farmland investments can also serve sustainability objectives. They have the lowest average carbon intensity (net CO_2 emissions per dollar invested) among alternative and traditional asset classes, with the ability to sequester and store carbon and to generate verified carbon credits. As environmental markets for climate and nature benefits continue to develop and grow, we expect to see increasing opportunities for private capital to address global environmental challenges through land-based investments. We already see companies seeking ways to combat climate change and nature loss in their supply chains, market-based frameworks that enable investment in nature positive land management practices, and innovative approaches from financial institutions to financing nature-based solutions.

For more information, please visit nuveen.com.

Endnotes

Sources

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A word on risk

All investments carry a certain degree of risk and there is no assurance that an investment will provide positive performance over any period of time. Equity investing involves risk. Investments are also subject to political, currency and regulatory risks. These risks may be magnified in emerging markets. Diversification is a technique to help reduce risk. There is no guarantee that diversification will protect against a loss of income. Investing in municipal bonds involves risks such as interest rate risk, credit risk and market risk, including the possible loss of principal. The value of the portfolio will fluctuate based on the value of the underlying securities. There are special risks associated with investments in high yield bonds, hedging activities and the potential use of leverage. Portfolios that include lower rated municipal bonds, commonly referred to as "high yield" or "junk" bonds, which are considered to be speculative, the credit and investment risk is heightened for the portfolio. Credit ratings are subject to change. AAA, AA, A, and BBB are investment grade ratings; BB, B, CCC/CC/C and D are below-investment grade ratings. As an asset class, real assets are less developed, more illiquid, and less transparent compared to traditional asset classes. Investments will be subject to risks generally associated with the ownership of real estate-related assets and foreign investing, including changes in economic conditions, currency values, environmental risks, the cost of and ability to obtain insurance, and risks related to leasing of properties. Investors should be aware that alternative investments including private equity and private debt are speculative, subject to substantial risks including the risks associated with limited liquidity, the use of leverage, short sales and concentrated investments and may involve complex tax structures and investment strategies. Alternative investments may be illiquid, there may be no liquid secondary market or ready purchasers for such securities, they may not be required to provide periodic pricing or valuation information to investors, there may be delays in distributing tax information to investors, they are not subject to the same regulatory requirements as other types of pooled investment vehicles, and they may be subject to high fees and expenses, which will reduce profits. Alternative investments are not appropriate for all investors and should not constitute an entire investment program. Investors may lose all or substantially all of the capital invested. The historical returns achieved by alternative asset vehicles is not a prediction of future performance or a guarantee of future results, and there can be no assurance that comparable returns will be achieved by any strategy. Impact investing and/or Environmental, Social and Governance (ESG) managers may take into consideration factors beyond traditional financial information to select securities, which could result in relative investment performance deviating from other strategies or broad market benchmarks, depending on whether such sectors or investments are in or out of favor in the market.

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