THE AUSTRALIAN

Future Fund: Oaktree bears brunt of $1bn cull

GRETCHEN FRIEMANN THE AUSTRALIAN 12:00AM FEBRUARY 19, 2016

Cooling on private equity? Future Fund managing director David Neal. Picture: Hollie Adams

US investment powerhouse, Oaktree Capital, has borne the brunt of the Future Fund's recent $1 billion cull of its private equity portfolio as the nation's sovereign wealth fund expands its cash holdings amid heightened concerns about the health of the global economy.

In a rare insight into the $118.4bn vehicle's investment moves, *The Australian* can reveal that close to 3.5 per cent of the fund was allocated to Oaktree, although this exposure spanned the LosAngeles-based firm's various alternative asset classes, which include distressed debt and high yield bonds. At the end of last year the Future Fund trimmed back this holding, skimming close to $500m from its near $4bn investment mandate with the firm.

The $1bn selldown, of which Oaktree accounted for close to half, was part of a wider strategy to scale back the Future Fund's exposure to the private equity sector, which faces headwinds following the downturn in the credit and equity markets.

The Future Fund sold its positions, through the Toronto-based advisory outfit, Setter Capital to the Canadian pension behemoth, CPP Investment Board, at close to net asset value, sources say.

In the midst of the GFC, investors in private equity firms, or Limited Partners as

In the midst of the GFC, investors in private equity firms, or Limited Partners as they are referred to, were often forced to swallow discounts of 25 per cent or more in funds. Since then the market has bounced back, with stakes in the funds of well-performing managers often trading at narrow discounts of 5 to 10 per cent.

Leading managers in older private equity funds can often command a premium.

Yet it is the Future Fund's strategic decision to lighten its exposure to private equity that is likely to focus the minds of institutional investment managers. The Future Fund's shifts in asset allocations are keenly watched by the market.

While private equity has generated some of the best returns, the Future Fund's managing director David Neal has echoed concerns voiced by Calpers, the US's biggest pension fund, that the sector is over populated, and claimed the fees are too high to warrant having so many private equity managers.

The fund's annual report highlighted that "many segments of the (private equity) market are not offering sufficient return for the risks we are expected to take, and while attractive opportunities for deploying capital can still be found, when one does arise, there can be fierce competition for it."

It is understood the recent trade did not result in the exclusion of any managers, which include mandates with the US-based Bain Capital as well as Hellman & Friedmann, one of the oldest buyout firms in the world. The fund's exposure to its two Australian managers, Archer Capital and Quadrant Private Equity, were not included in the private equity selldown.

Yet the heightened caution emanating from the influential government-backed vehicle, established in 2006 to provide pensions for public servants, underscores concerns among the private equity industry. Namely after reaping record returns from the buyout sector, investors are increasingly rotating to safer, more liquid exposures.

At a Senate estimates hearing earlier this month, Mr Neal stressed the "private equity portfolio has done extremely well." He said, "that is part of the reason why we needed to rebalance it. It was becoming a large part of our portfolio and it is very illiquid. So we took the opportunity to take a cross-section of that portfolio and sell that in a transaction to relatively modestly rebalance our private equity exposure. So our private equity portfolio has supported our returns."

Ken Licence, a leading placement agent in Australia and Asia, pointed out Limited Partners use "opportunistic realisations for a variety of reasons" and stressed the fund's decision to reduce its weighting reflected the sector's robust performance.

Yasser El-Ansary, the CEO of industry body AVCAL, added the mounting