

Why one hedge fund is buying the managers

Following a lengthy period trading at a single digit price to earnings multiple, Navigator Global Investments has started to bounce from its 2023-24 lows as its strategy pivot begins to bear fruit.

We discuss the rationale for the pivot, the early success and contrast NGI's approach to traditional asset management companies. We believe Navigator is a differentiated portfolio of high-quality unlisted assets delivering returns well above its cost of capital and for that reason, it deserves increased investor attention.

The big bet

Navigator Global Investments (ASX: NGI) originated as a corporate vehicle for its Lighthouse hedge fund platform. Its strategic shift began in August 2020 with a major transaction that repositioned the firm into the fast-growing General Partner (GP) staking industry.

At the time, Blue Owl (previously Dyal Capital Partners) were moving upmarket with their latest US\$9bn+ Fund IV, choosing to exit their positions in the sub-\$250m cheque-size market. Blue Owl was key to the commercialisation of the GP staking market and has raised over US\$33bn for GP stakes since 2012.

The transaction with Blue Owl included a diversified portfolio of 6 minority stakes in hedge funds for a 40% equity stake in NGI. This was a major bet for NGI, as the acquired portfolio was generating US\$32m in pre-tax distributable profits, potentially overshadowing NGI's existing US\$25.8m PBT from its Lighthouse business.

The rationale was simple, to diversify the business, and utilising management's deep familiarity with the lucrative economics of a mature GP staking portfolio, having previously worked in the staking industry.

GP staking

Management was drawn to GP staking as a stable avenue for capital redeployment from their more volatile hedge fund business, offering long-dated, predictable management fee cash flows while maintaining the potential for private

equity-like returns. NGI is effectively buying into enduring management fee streams, locking in strong initial yields underpinned by Assets Under Management (AUM) with limited liquidity windows and additional upside from carry (performance fees) and underlying asset appreciation.

GP staking firms take minority stakes into private markets investment firms. These stakes solve critical issues for growing asset managers:

- **Growth Equity Funding:** Financing 2-10% GP co-investments required for a new fund that is 2x to 3x larger than its predecessor fund, which may still be in realisation phase.
- **Succession & Liquidity:** Providing staged liquidity to founding partners and structuring succession plans, thereby supporting talent retention before the next phase of FUM growth.

Often consideration is stretched out across multiple years to manage alignment, and ensure the new funds are raised as expected. The total AUM of the underlying managers in the Blue Owl portfolio has grown substantially, rising from approximately US\$35bn at the time of acquisition to over US\$56bn in FY25.

This 60% increase underscores the fundamental growth potential NGI sought to capture. We estimate the portfolio delivered US\$66.3m in distributions in FY25, an impressive yield of 18.1% on the implied value of the consideration.

Blessing and a curse

Leveraging their remaining liquidity, NGI quickly executed follow-on deals for stakes in Marble Capital (US multi-family real estate financing) and Invictus Capital Partners (US mortgage securitisation). While these proved to be another strong set of deals, the rapid and significant earnings growth from the Blue Owl portfolio triggered an acute liquidity challenge. The company faced an obligation to pay Blue Owl the maximum US\$200m consideration cap on their 5-year earn out.

A successful equity raise resolved a long period of overhang that had been depressing the earnings multiple and allowed investors to finally see the strategy's benefits as the Marble and Invictus stakes matured.

Yield with a growth kicker

The Marble and Invictus deals were expected to cost a maximum of US\$185m in aggregate; however, upwards of US\$140m of the consideration was deferred for 1 to 3-yrs. These acquisitions were highly accretive, with the initial US\$45m of consideration generating an immediate 12% yield in the first full year (US\$5.4m distributions before tax). As the remaining consideration was paid, the yield has been largely sustained, delivering 10% in FY25 (US\$13.8m) while the businesses scale up new funds.

Since investment, AUM has grown 122% from US\$3.7bn to US\$8.2bn. We expect this continued AUM growth will transition these stakes to deliver continued management fee growth as well as performance fees and carried interest, supporting out forecast for mid-to-high teens yields in the next three years. Additionally, the value of these stakes is likely to exceed the conservative independents valuations used for financial reporting purposes.

Comparison to traditional fund managers

NGI holds two critical advantages in the unlisted space. As a listed vehicle, NGI offers founders confidence that their minority investor will not change hands later, avoiding due diligence and operational issues. They also benefit from deal sourcing assistance and credibility from Blue Owl, who are the global market leader in GP staking.

However, NGI operates without a traditional centralised sales team, a key difference from traditional asset class managers. This approach is justified because the underlying private market firms target institutional clients with complex, unique strategies.

Hence, cross selling benefits are minimal, making it more efficient to keep smaller specialised distribution teams embedded within the individual managers. While this may result in slower AUM growth compared to managers with simpler products and broad retail distribution, it is offset by the fact that private markets managers often face less management fee pressure as their track records and strategies are harder to replicate.

Further, the underlying strategies exhibit a low correlation to listed equity markets, resulting in lower performance fee volatility. We note the recent Liberation Day sell-off saw underlying managers report only single-digit drawdowns. Traditional asset class managers also have more frequent liquidity windows increasing sales team intensity. This compares to NGI's managers with locked up capital, lowering the chance of large investor redemptions during market dislocations.

The new normal

NGI is now established in the GP staking market, recently completing its third deal with 1315 Capital, bringing ownership adjusted AUM to US\$10bn across its GP stakes. The demand for GP stakes is robust, supported by the continued global shift towards private assets. NGI with its growing track record, permanent capital and strategic relationship with Blue Owl, will continue to benefit. The company currently generates around \$90 to \$100m of free cash flow each year and has \$50 to \$100m of debt capacity, providing ample firepower for future opportunities.

As described above, NGI is reinvesting its capital into assets generating mid-teens yields, well in excess of its cost of capital. The stock has begun to re-rate from its single digit price-earnings multiple. The combination of removing the earn-out overhang, a maturing portfolio delivering mid-single-digit organic earnings growth, and ample self-funding capacity positions NGI to realise the strategy it set out in 2020, a strategically differentiated and scaling player in the GP staking market.



Sam Cox
Analyst

This material has been prepared by Eiger Capital Limited ABN 72 631 838 607 AFSL 516 751 (Eiger Capital). It is general information only and is not intended to provide you with financial advice or take into account your objectives, financial situation or needs. To the extent permitted by law, no liability is accepted for any loss or damage as a result of any reliance on this information.

Any projections are based on assumptions which we believe are reasonable but are subject to change and should not be relied upon.

Past performance is not a reliable indicator of future performance. Neither any particular rate of return nor capital invested are guaranteed.