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Designed for the Long Term: Illiquidity in Private Equity

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Designed for the Long Term: Illiquidity in Private Equity

In this paper, we aim to help advisors understand illiquidity in private equity and evaluate private equity's place in portfolios.

Investor and Advisor Perspectives

Companies are staying private for longer and a growing share of economic activity is happening outside the public markets. Private equity (PE) is one way advisors can access that private market opportunity set. One feature of private equity is illiquidity, which makes active management and value creation possible. Research from CAIS and Mercer shows that roughly four in 10 financial advisors cite it as a primary reason for limited participation in alternative investments.¹

Yet end-investor sentiment suggests more nuance. [In a recent survey](#), KKR asked individual investors how much illiquidity they would be comfortable with in their portfolio over the next five years in exchange for improved performance or diversification. Nearly half of respondents said they would be comfortable allocating more than 25% of their portfolio, with a majority (57%) comfortable with illiquid allocations exceeding 15%.²

Investors also associated private markets with strong performance potential: "high returns" was their most selected positive association (37%), followed by "improved diversification" and "long-term orientation" (25% each). Many respondents associated private markets with meaningful potential, while still flagging concerns that reflect a desire for clearer expectations.³

Taken together, these responses suggest more uncertainty around illiquidity than outright rejection. We believe that sentiment reflects a broader need to expand advisor education around private markets investing. Roughly 22% of advisors surveyed say lack of understanding limits their participation in private markets, and 42% of individual investors surveyed identify education as the primary barrier.

This creates a practical challenge: how to evaluate and communicate the advantages and risks of illiquidity in private equity with knowledge, clarity, and balance.

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Where Value Is Accruing in Today's Economy

Since 2000, the number of publicly listed US companies has declined by nearly 50%. Today, 85% of companies with over \$100 million in revenue are privately held.⁴ This means a growing share of value creation and growth is only accessible through private markets. Public equity markets have also become more concentrated, more correlated to bonds,⁵ and more uncertain as the lines between geopolitics and economics continue to blur. As a result, portfolios built according to traditional 60/40 construction may capture a narrower set of outcomes than in the past.

At its simplest, private equity refers to equity investments in companies that are not listed on public stock exchanges—or, in some cases, to the act of buying public companies and taking them private. Unlike public equity investing, which generally involves passive ownership, private equity's differentiation is rooted in active ownership and its ability to create—not just capture—value.

That value creation is not always straightforward and almost always takes time. Typically, execution takes five to seven years and is driven by earnings growth from operational improvements and strategic transformation and repositioning. As a result of staying invested over multi-year periods, private equity has the potential to generate more sustained compounding of returns, with the advantage of some insulation from public market volatility.



KKR believes **operational enhancement**—not financial engineering, multiple expansion, or market timing—is the most reliable driver of alpha in private equity.

How Illiquidity Functions in Private Equity

Illiquidity and Value Creation

Illiquidity is a fundamental characteristic of private equity strategies, because returns are driven primarily by a manager's ability to create value in their portfolio companies. True, durable value creation requires long-term strategic planning and heavy lifting from the private equity firm and portfolio company management. The private markets allow for allocation of the time and resources necessary to achieve this, a process that is difficult to replicate in the public markets.

Exhibit 1

How Private Equity Managers Create Value Over Time

Private equity managers typically seek to drive returns through multi-year value creation plans. Initiatives that a general partner (GP) or sponsor might implement within a portfolio company include, but are not limited to:

Operational Improvements

- ✓ Optimizing working capital
- ✓ Improving manufacturing
- ✓ Upgrading technology
- ✓ Streamlining procurement and supply chains
- ✓ Top-grading talent

Strategic Repositioning

- ✓ Shifting toward higher-growth, higher-margin areas
- ✓ Exiting non-core or underperforming segments
- ✓ Refining go-to-market and customer strategy
- ✓ Strengthening competitive positioning

Growth Initiatives

- ✓ Expanding into new geographies, organically and/or inorganically
- ✓ Expanding into new product or service areas, organically and/or inorganically
- ✓ Investing in sales and distribution capabilities



Example:

Creating Value After a Corporate Carve-Out

In 2023, KKR acquired a book publisher with strong market positioning and a diverse catalog of titles by carving it out of a larger media conglomerate. Before KKR's acquisition, the business was an under-resourced subsidiary, lacking support for growth initiatives and an optimized operating model. KKR is supporting the company to address these gaps with initiatives like **de-risking supply chain, adding digital and marketing expertise, executing M&A to expand internationally, and launching new publishing verticals.**

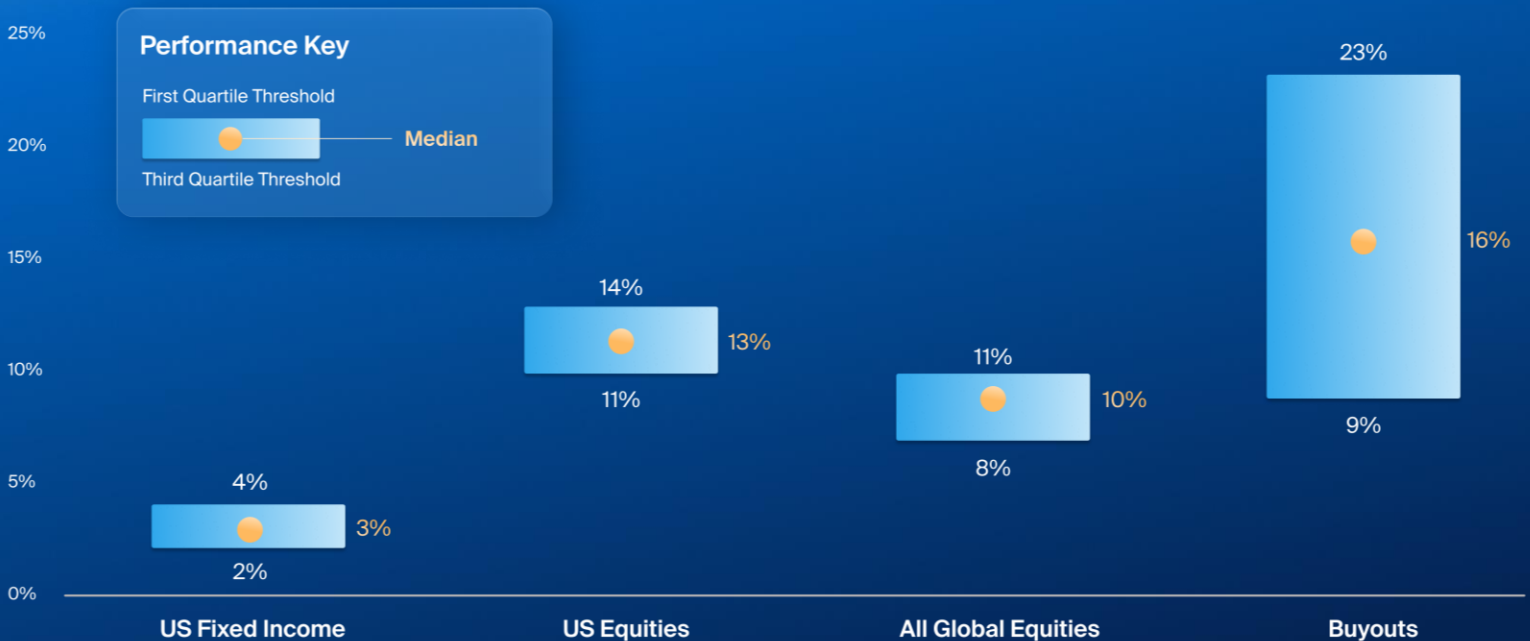
Executing this transaction involved setting up the company as a standalone business, including disentangling shared systems and establishing key corporate functions and processes. Buying complexity and transforming it into simplicity is one of the core differentiators of KKR's value creation tool kit.

In fact, KKR has completed over 70 complex carve-outs. Read KKR's article, [“Unearthing Successful Companies through Corporate Carve-Outs,”](#) for more details.

Choosing the right manager is critical in private equity. We believe managers with proven track records, experienced teams, and repeatable playbooks may be more likely to generate outperformance over the long term. This point is especially important when you consider that the historical dispersion of returns among private equity managers was over 1,000 basis points larger than the dispersion among public markets managers (Exhibit 2).

Exhibit 2

Manager Selection Determines Outcomes in Private Equity Buyouts



Source: eVestment Alliance database for 15-year period through December 31, 2024. US Equities include large and small cap indexes. Preqin online database, performance as of December 2024 (includes vintages for the 15 years to 2022), top quartile, median, and bottom quartile boundary net IRRs. Performance for later vintage funds not available/meaningful. Preqin's database is continually updated and subject to change. You cannot invest directly in an index. Index results assume the re-investment of all dividends and capital gains. There is no assurance that the trends described or depicted above will continue.

Illiquidity and Fund Structures

In recent years, access points to private equity have grown immensely. Notably, newer evergreen structures have expanded access for individual investors, enabling participation in private equity through vehicles that can be operationally easier and more efficient than traditional drawdown structures.⁵ These structures can also support financial advisors in scaling access across their book of business.

Exhibit 3

Comparing Evergreen and Drawdown Vehicles

Feature	Evergreen	Drawdown
Fundraising & Capital Commitment	Perpetual; periodic subscription windows with capital committed and fully deployed immediately	Finite life (typically 10–12 years); capital committed upfront and gradually deployed over time, creating a cashflow J-curve
Investor Illiquidity	Limited, periodic liquidity (subject to terms, caps, and manager discretion)	No interim liquidity; capital returned gradually through monetizations of portfolio companies
Vintage Exposure & Diversification	Continuous exposure across vintages; enables incremental allocation and reinvestment	Vintage-specific exposure; requires multiple commitments to build diversification
Compounding	Potentially higher velocity of return compounding through immediate and full deployment of capital and reinvestment of exit proceeds	Compounding of returns potentially occurs over a longer time period because of episodic cash flow dynamics

Although evergreen vehicles may potentially allow for occasional liquidity, it is important to remember the assets underlying these evergreen vehicles are private, and therefore illiquid. These remain long-duration strategies built around multi-year investment horizons—a simpler operational structure does not change the underlying illiquidity of the asset class.

Like those who manage them, not all evergreen vehicles are created equal.⁶ Advisors are encouraged to evaluate how these vehicles invest and are managed to ensure alignment with client objectives.

To learn more about the various private equity fund structures available to advisors, visit caisgroup.com/insights or kk.com/wealth/strategies/private-equity.

Diversifying Return Drivers in Individual Portfolios

The performance of private equity companies is typically driven by underlying business fundamentals, less so by sentiment or market moves. This can result in less-correlated return patterns, particularly during periods of public market volatility. In fact, private equity tends to outperform when equity markets are less robust—in excess of 400 basis points over the last 25 years.⁷

Exhibit 4

Net Annualized Historical Performance of Global Private Equity Index vs. Public Equities

According to Cambridge Associates, global private equity has outperformed public markets by over 500 basis points on average over the last 25 years, which may be due to the active role private equity investors play as owners and operators of businesses.



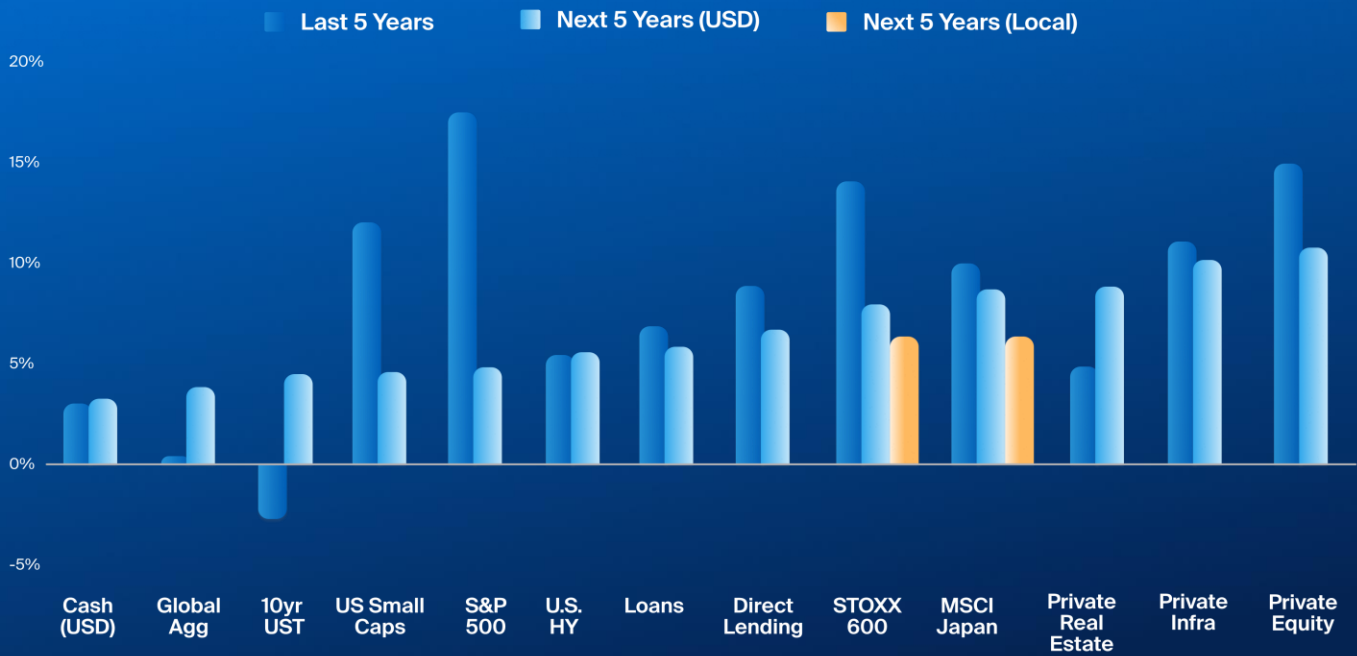
Source: Cambridge Associates, KKR Global Macro & Asset Allocation analysis. Indexes are unmanaged. It is not possible to invest directly in an index. Data as of June 30, 2025. **Past Performance is no guarantee of future results.**

In addition, as mentioned before, private equity expands the opportunity set beyond public markets. Eighty-five percent of US companies with over \$100 million in revenue are privately held and, outside the US, public markets tend to be more limited with a skew towards family/founder ownership. So, private equity provides access to a wider set of companies, sometimes smaller, earlier stage, and/or in underrepresented sectors and geographies. Together, these characteristics can strengthen portfolio diversification.

Such diversification away from traditional public equity allocations may become even more beneficial. Despite the relative outperformance of public equities in recent years, the pace of growth will slow in the five years ahead (Exhibit 5), and private equity is expected to be the best performing asset class over this period. Note that such views are forward-looking, subject to change, and may not materialize.

Exhibit 5

Historical and Expected Returns Across Asset Classes



Last 5-Years return from October 31, 2020 to October 31, 2025 for consistency across asset classes. Private Markets as at 2Q25. Capital markets assumptions are average across all quartiles with annualized total returns. Forecasts represent five-year annualized total return expectations. For private asset classes (Private Credit, Private Infra, Private Real Estate, and Private Equity), returns are representative of the median manager return net of fees and carry. Source: Bloomberg, BofA, Burgiss, Cambridge, KKR Global Macro & Asset Allocation analysis. Private Real Estate modeled using the Cambridge Associates Real Estate Index. Private Infrastructure modeled using the Cambridge Associates Infrastructure Index. Private Equity modeled using the Cambridge Associates Private Equity Index. Private Credit modeled using the Cliffwater Direct Lending Index. Model returns are hypothetical in nature and are shown for illustrative, informational purposes only. **Past performance does not guarantee future results.**

Constructing Portfolios With Illiquid Assets

According to KKR’s analysis, over the last two decades, adding private equity improved portfolio efficiency by delivering higher returns for the same risk, or lower risk for the same return (Exhibit 5). For advisors weighing how much private equity would benefit their portfolios over time, the efficient frontier, which accounts primarily for volatility, may be helpful.

Compounding and the Illiquidity Premium

Illiquidity in private equity may feel more familiar to those already accustomed to explaining investing through the lens of disciplined compounding, which prioritizes remaining invested, minimizing unnecessary turnover, and allowing time to magnify incremental return advantages. The principle is familiar in traditional public equity investing and frequently associated with long-term investors who emphasize holding high-quality businesses over extended periods.

Private equity is characterized by lower correlation with public markets as a result of active management, different risk return drivers, and market sentiment, and valuations driven by company fundamentals not market sentiment. Combined with illiquidity, these factors can create a profound compounding impact on portfolios.

Exhibit 6

The Efficient Frontier: Realized Annual Returns and Volatility Comparison With Traditional Assets and Private Equity



Source: Bloomberg, MSCI, Cambridge. KKR Global Macro & Asset Allocation analysis. The above analysis is provided for illustrative purposes only. Returns and correlations are calculated with quarterly returns between 2005 and 2024. Volatilities are calculated with annual calendar year returns between 2005 and 2024. Traditional Assets include Public Fixed Income (Bloomberg Global-Aggregate Total Return Index Value Hedged USD) and Public Equities (MSCI World Index). Private Equity is modeled using Cambridge Global Buyout Index. Data as at December 2024.

Accounting for the risks related to illiquidity is just as important when sizing an allocation. Because these risks are structural—not temporary or unforeseen—liquidity planning becomes a central component of private equity implementation.

In practice, advisors can approach this through a combination of portfolio design and scenario analysis:

- **Segment capital by time horizon.** Distinguish between near-term liquidity needs and long-duration capital that can be committed to private markets.
- **Understand capital call and distribution pacing.** Pay particular attention to how this unfolds in traditional drawdown structures versus evergreen structures.
- **Align fund structures with client cash flow expectations.** Ensure usability does not conflict with the underlying duration of the strategy.
- **Stress-test liquidity scenarios.** Account for delayed distributions, redemption limits, or extended holding periods.

These considerations reinforce a central principle: illiquid allocations are typically most appropriate when funded with capital that is not required for near- or intermediate-term obligations. When that alignment is in place, illiquidity can be accounted for deliberately within a broader portfolio framework rather than treated as an isolated risk.

Balancing Opportunity and Illiquidity in Private Equity

Private equity provides advisors with access to a broad and evolving opportunity set not accessible in the public markets, where value creation is typically driven by active ownership, operational execution, and time. For many portfolios, private equity may provide diversification and a differentiated source of return compared to what is available in public markets.

Illiquidity is a characteristic of these strategies and a consideration when seeking to participate in their return potential. For advisors, the task is to evaluate that tradeoff deliberately by aligning allocations with long-term capital and structuring portfolios to account for extended holding periods and variable cash flow timing. Importantly, manager selection is a critical determinant of outcomes in private equity, so choosing managers with demonstrated execution ability and consistent outcomes is a key task for advisors.

When these elements are thoughtfully considered, illiquidity may shift from a constraint to a potential advantage. In that context, private equity can serve as a strategic allocation that is becoming less of a peripheral asset class and more of a mainstream solution for optimizing returns in client portfolios.

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