

Present Value Comparison by Investment Strategy

Relative carry values differ by investment strategy due to differences in investment profile

Lowest Value

Highest Value



Private Credit

Real Estate

Infrastructure

Private Equity



Factors influencing present value include:

- Time horizon
- Return expectations
- Investment volatility
- Hurdle rates

Carried interest can be valued similarly to stock options via Black-Scholes to approximate present value

- This is useful in comparing relative values between strategies / funds (i.e., private equity carry vs. private credit carry)
- Especially helpful in current environment as firms expand into additional strategies and helps answer question of how much carry in primary focus area should be traded for other strategies
- Allows carried interest to be better communicated / analyzed alongside traditional annual compensation
- Understanding present value helps determine and communicate potential compensation trade-offs. For employees that enter carry programs for the first time, what, if any, trade-offs should there be?

JOHNSON ASSOCIATES, INC.

Comparison of Carry / Equity Vehicles

	<u>Carry Basket</u>	<u>Single Fund Carry</u>	<u>Options</u>	<u>Stock</u>
Economic Value	Upside above hurdle only	Upside above hurdle only	Upside only; should account for hurdle	Downside protection w/ muted upside
Vesting	Typically longer	Typically longer	Typically shorter; should be adjusted	Typically shorter; should be adjusted
Tax Treatment	Often beneficial	Often beneficial	Standard treatment	Standard treatment
Applicability	All firms	All firms	Public alternatives only	Public alternatives only
Compensation Communication	Dollars-at-Work; NPV comparison helpful	Dollars-at-Work; NPV comparison helpful	Easily understood	Easily understood
Collaboration	Yes	No (in isolation)	Yes	Yes

Firms use a variety of ways to provide long-term alignment, motivation, and collaboration in alternatives

- All of the above vehicles are being used to provide competitive compensation
- Carry, either in a single fund or in a basket, is a common approach, but it can be difficult to communicate alongside annual compensation without applying a valuation calculation
- Options are easily understood while functioning similarly to carry, but apply on a full firm basis and do not have beneficial tax treatment
- Stock is also well understood, applies firm-wide, and has the same tax treatment. However, it offers a different value proposition by providing downside protection and more limited upside