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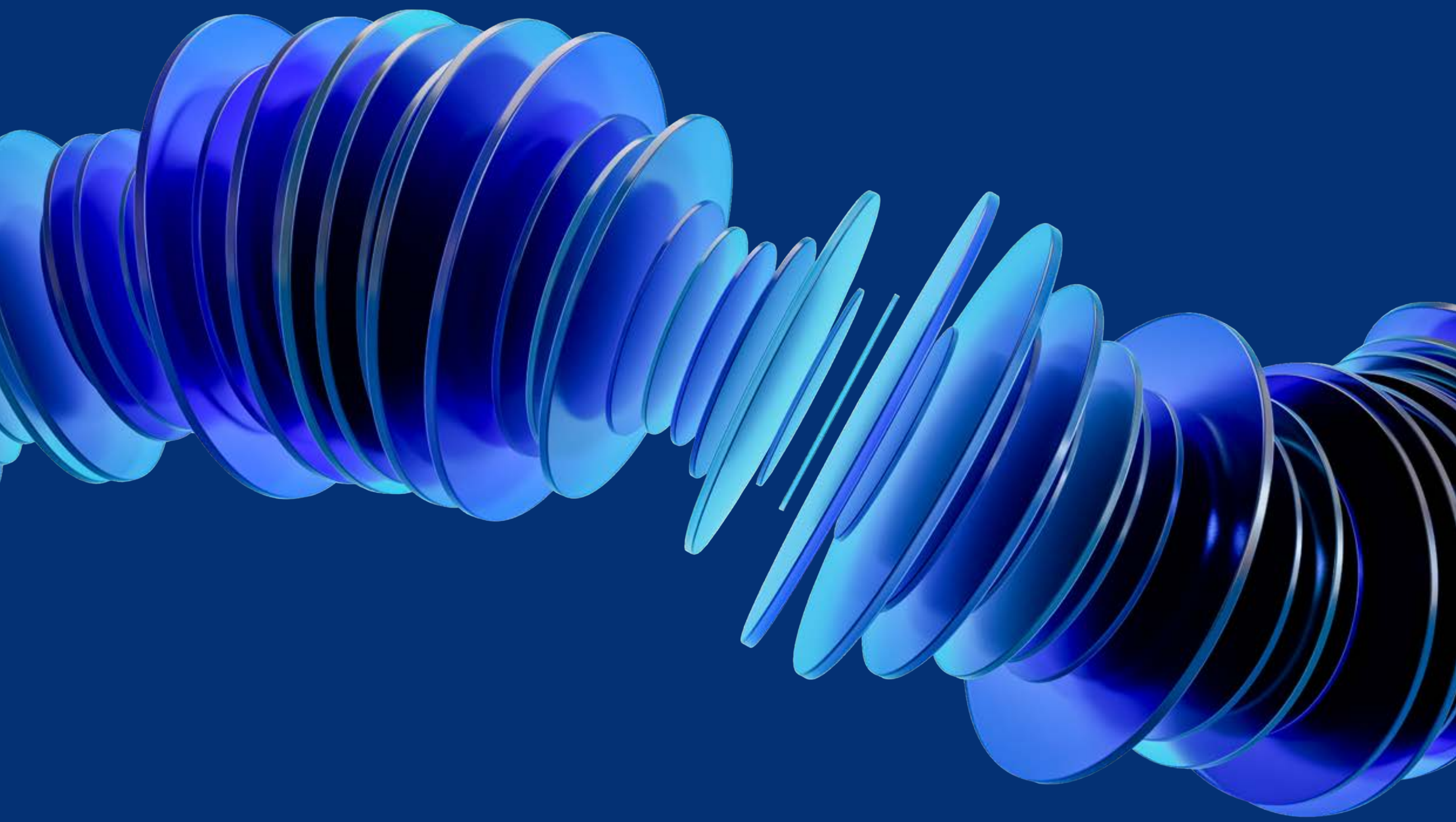
Could Private Markets hold the key to better outcomes for DC members?



Challenges facing the traditional approach

Defined Contribution (DC) schemes, including master trusts, are now the most common type of pension in the UK, with 23.6 million employees enrolled in a qualifying scheme as of mid-2025.[1] Increasingly, people will rely solely on their DC pots for income in retirement.

Unfortunately, contributions to these DC arrangements are often insufficient, resulting in a significant pension savings gap, that will only worsen due to the rapidly aging population.

According to the Department for Work & Pensions, 4 in 10 working-aged people (equivalent to 14.6 million) are not saving enough for retirement.[2] Clearly there is a pressing need for greater education on the importance of adequate retirement savings, with higher contribution levels being essential. While investment returns alone cannot close this gap, private markets offer a way to help member assets achieve higher long-term returns and improve retirement outcomes.

Traditionally, DC growth portfolios, designed to save for retirement, have focused predominately on asset classes such as public equities and growth fixed income. These portfolios are aimed at achieving returns significantly above inflation. This contrasts with other institutional investors with long time horizons, who have allocated to private markets to access their potential for higher returns.

This matters because many people will continue to rely on investment returns to grow their pensions and secure good retirement outcomes. Private markets is an asset class that could potentially both increase member returns over the long term while also providing diversification during periods of public equity market stress.

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4 in 10

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The growing opportunity in private markets

Think of private markets as an iceberg: what you see above water, public companies listed on stock exchanges, is just the tip. Beneath the surface lies a vast, hidden world. For example, in the US, 87% of firms with revenue greater than $100m are private, demonstrating the potential significance of exposure to private markets, which represent the hidden part of the economic iceberg.[3]

Private markets used to be seen as a playground for early and growth stage companies. But that's changed. Big-ticket deals (acquisitions of £1 billion+) have quadrupled since 2010, and nearly half of the UK's largest companies (those with revenues over £5 billion) are now owned by private capital investors.[4] Companies that might have previously turned to banks for financing are increasingly tapping private markets instead.

Globally, investors have been putting a lot of money into private tech companies like Anthropic, Coreweave, Databricks, OpenAI, Perplexity, ScaleAI, and xAI with some people now calling these companies the "Private Magnificent Seven." The combined value of these private companies grew by 40% in just six months, much faster than their public counterparts.[5]

According to the British Private Equity & Venture Capital Association's (BVCA) comprehensive performance survey, private equity funds based in the UK delivered a 15.8% internal rate of return (a common measure of performance in private markets) over the ten years to December 2024, compared to 6.2% for the FTSE All Share and 8.0% MSCI Europe Index (a stock market index of 15 developed markets in Europe).

This demonstrates the potential for private markets to enhance returns for investors in the future, despite strong global equities returns in recent years.[6]

For pension schemes, tapping into private markets offers access to a broader and more diverse range of investment opportunities that are not visible in public markets. So, could private markets be the key to better outcomes for DC members?

Nearly half of the UK's largest companies are now owned by private capital investors.

Targeting a private markets allocation

UK pension schemes currently invest less in private markets, compared to their international counterparts. For example, in 2022 five of Canada's Maple-8 (the major Canadian public pension funds) allocated over 50% of their asset allocation to private markets.[7] In Australia in 2025, their super funds, allocated 23% of their total investments to private assets.[8]

In contrast, UK DC schemes allocate approximately 4% (3% to infrastructure and 1% to private equity) to private markets.[9]

The government's Pension Schemes Bill and the Mansion House Accord are encouraging DC schemes to increase their investments in private markets, including into the UK. These investments include backing young businesses; infrastructure projects like improving transport networks and clean energy; and housing developments.[10] These investments have potentially attractive returns; but they also help the economy by supporting businesses and projects that create jobs and encourage innovation.

The 17 signatories of the Mansion House Accord, representing about 90% of active DC savers and currently overseeing £252 billion in assets, have committed to allocating at least 10% of their main default fund assets to private markets. Of this at least 5% will be invested in UK private market assets.

Both the Mercer Master Trust and now:pensions Master Trust have signed the Accord and aim to achieve a 10% minimum allocation to private markets by 2030.

Managing the challenges and leveraging expertise

Managing private market portfolios is more complex than public markets and needs specialist expertise and experience.

For example, one of the challenges with private market investments is that they can't be sold quickly when members want their money, they're "illiquid." Because of this, investors need to be comfortable locking up their money for several years. The good news? Investors are usually rewarded for this patience with an "illiquidity premium", extra returns for accepting less flexibility. This requires careful planning and expertise to balance long-term growth with members' ability to access their savings at retirement or if they transfer out.

Mercer's experience and size make a big difference here. We've been advising on private markets for institutional asset owners for decades across the globe, including managing the Mercer Super in Australia, where private market investing in DC is well established.

Our global private footprint includes around 282 private markets professionals in 38 offices, managing $50 billion in private markets assets, worldwide.[11] We were also an early adopter in the UK, helping a DC client allocate to private markets in its default strategy back in 2017.

To manage private markets effectively, we have and will continue to partner closely with highly rated managers, to carefully curate and develop bespoke solutions. In December 2025 we announced the launch of the new Schroders Mercer Private Assets Growth Long-Term Asset Fund (LTAF), a customised LTAF exclusively for members of Mercer's Workplace Savings solutions including the Mercer Master Trust and the now:pensions Master Trust.

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Building a private markets portfolio for long-term growth

The Schroders Mercer Private Assets Growth LTAF has been thoughtfully designed for long-term investing with a focus on the growth phase of members investment journeys where the desire is for higher investment returns and volatility can be better tolerated. At this stage of the journey, we can adopt a long-term view, investing in private markets with higher potential returns and a capacity to accept shorter term losses and variability.

With this in mind the initial allocation of the LTAF in 2026 invests only in the highest returning private market asset classes as below:

- 50% in private equity, focusing on early and mid-stage companies with strong growth potential.
- 25% in infrastructure equity, focusing on vital infrastructure required to support economic growth.
- The remaining 25% will be held in more liquid investments, 23% in listed equities (to retain the growth focus) and 2% in cash, ensuring funds can be accessed when needed.

Getting the allocation to different private markets asset classes right really matters.

Over the 20 years ending 30 June 2025, the internal rate of return for Private Equity was 13.1%, significantly exceeding the 8.3% return for Private Debt.[12]

DC investors need to think very carefully about when to introduce more defensive private markets allocations for members.

Mercer's decades of experience working with institutional asset owners and deep, long-standing relationships with top-tier managers worldwide, combined with our global scale gives us access to attractive deals and co-investment opportunities.

The majority of the LTAF investments will be co-investment opportunities, as investing alongside General Partners in individual deals can reduce fees, accelerate returns, and introduce attractive deals, all for the benefit of our members. We can also be more selective about the deals we access, ensuring that only the best make their way into portfolios.

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Looking ahead to 2026

Looking specifically at the asset classes we are focused on, here's what we see shaping private markets and our investments in 2026:

Private equity

The LTAF will invest in private companies, helping them grow and improve profitability. We expect to hold the private equity holdings for several years, allowing managers to focus on long-term growth without worrying about short-term market swings. In 2026, deal activity is expected to pick up, with greater optimism among private equity firms.[13] The pursuit of higher-growth sectors like healthcare and technology is expected to continue.[14]

Infrastructure

Infrastructure investments include roads, bridges, energy networks, and digital hubs. In 2026, a particular focus will be on clean energy and electrification. This isn't just about switching to electricity; it's about moving to clean, renewable energy. Energy security, keeping data safe, and cutting carbon emissions will be front and centre.[15]

Secondaries and co-investments

Private market investments often follow a "J-curve" pattern, early on, returns might be negative as investments are made and costs incurred, but over time, as companies grow, returns improve.

Co-investments are particularly attractive for DC investors, and we are leveraging the approached used by Mercer Super in Australia in leading their introduction in the UK. Co-investments are also effective at managing the "J-curve" typically associated with private markets.

The majority of our private market and infrastructure assets will be co-investments, with smaller allocations to primary and secondary fund opportunities. Secondary markets let investors buy stakes in existing private market investments, potentially seeing returns sooner. Think of it like buying a fruit tree that's already grown for a few years instead of planting a seed yourself. You get to enjoy the fruit sooner.

UK investing

Through our Mansion House Accord ambition we support investing in UK assets to drive UK growth, as long as it's not at the expense of investment returns to members. The approach within the LTAF is consistent with this, with the fund managers having a wider opportunity set where appropriate but investing in UK assets when investment opportunities are attractive.

Impact investing

More than 80% of UK pension savers want their investments to generate positive social and environmental impact alongside financial returns.[16] This is supported by government ambitions to make the UK a leader in sustainable finance.[17] The LTAF will invest in impact investments where the financial return also stacks up.

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The road ahead for UK pensions and private markets

Private markets provide UK pension schemes with access to a broad and diverse range of investment opportunities unavailable in public markets. This opportunity can play an important role in helping pension savers spread risk, increase returns and improve their chances of better outcomes.

However, private markets are just one piece of the puzzle. Success depends on combining them with other asset classes and working with top-quality asset managers who have strong teams, proven strategies, consistent results, and a focus on environmental, social, and governance (ESG) principles. This is precisely the approach Mercer and now: pensions are taking to support its Master Trust members.

With the right strategy and expertise, private markets can be a valuable part of a diversified investment approach that helps DC schemes move closer to their goal of providing savers with a more secure and comfortable retirement.

Endnotes

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