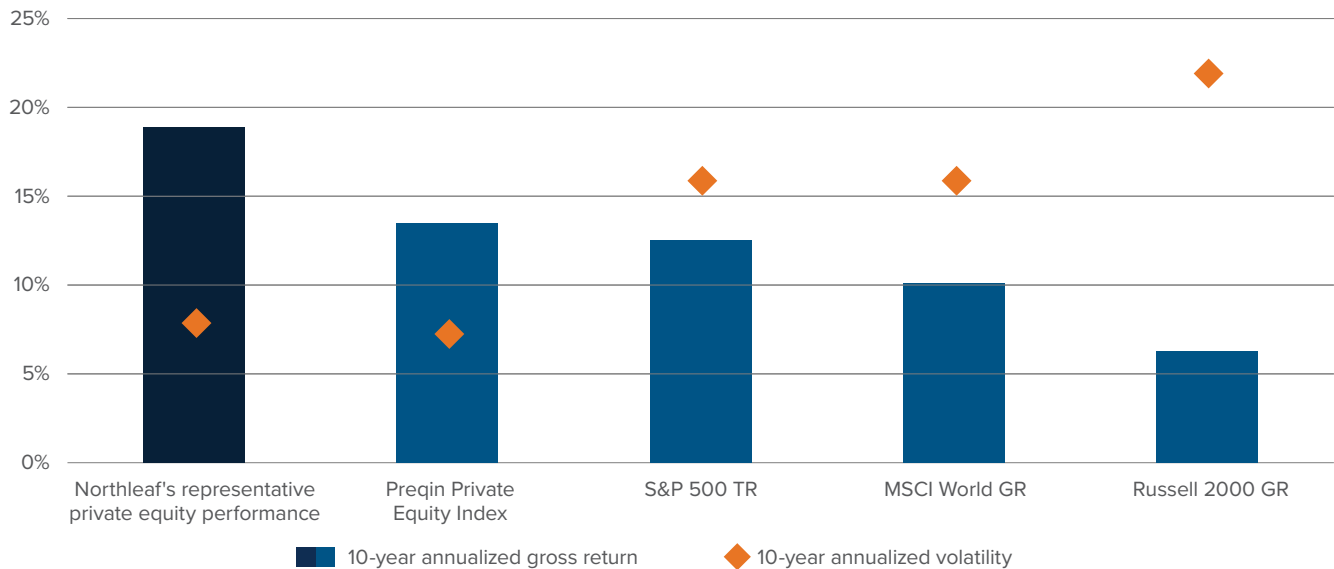


The real reasons private assets exhibit lower volatility

Hint: valuation frequency matters—but the real story goes much deeper

Private investments have delivered higher returns and lower volatility relative to comparable public market investments historically. They also tend to retain their value during bear markets, something that isn't always well understood.

Private equity returns and volatility relative to public equity USD; 10-year annualized gross returns %; as at March 31, 2025



Past performance is not a guarantee of future results. Northleaf program return information is provided for illustrative purposes only and is not indicative of past or futures results of a particular fund. Source: Northleaf, Preqin, Morningstar

Some believe the lower volatility is a result of timing. Because private assets are only priced monthly or quarterly, and because this pricing occurs with months of delay, critics argue that private markets only appear less volatile. If they were priced more frequently, they would be just as volatile to the downside in a panicked market.

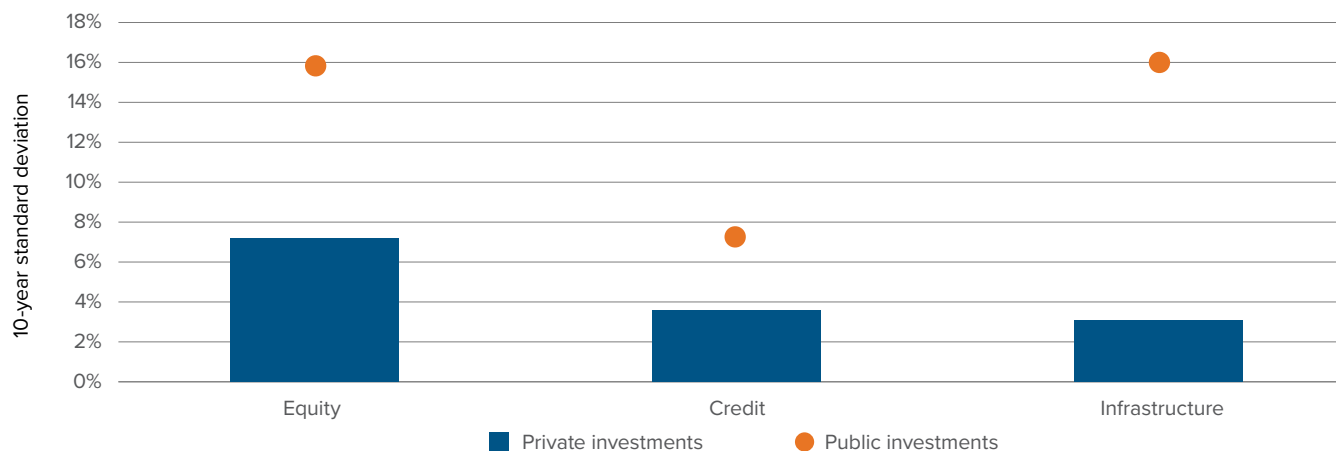
The reality is more complicated.

The data shows that even when you align the valuation periods to match the corresponding months in public markets, private asset valuations still hold up better. Their lower volatility is a result of something other than stale pricing.

The way private markets operate is largely responsible for the reduced volatility. Three features make them different — their valuation methodology, short- to medium-term illiquidity and the sector's unique alignment of incentives.



Aligning valuation intervals doesn't close the volatility gap — public investments still exhibit greater fluctuations than private ones when evaluated quarterly



Source: Prequin and Morningstar. Standard deviation is based on quarterly returns in USD that are aligned over the same period for both private and public investments. Time period: April 1, 2015 – March 31, 2024. Private Investment Indices (Equity: Prequin Private Equity, Credit: Prequin Private Credit, Infrastructure: Prequin Private Infrastructure), Public Investment Indices (Equity: MSCI World, Credit: 50% ICE BofA US High Yield TR + 50% Morningstar LSTA US LL TR, Infrastructure: S&P Global Infrastructure TR)

Valuation methodology

Valuations are made less frequently in private markets, but the methods used to generate them are worth discussing.

Fair value is determined by a combination of four methods:

1. Market approach (comparable public or private company analysis).
2. Income approach (discounted cash flow analysis).
3. Asset-based approach (net assets or the liquidation cost approach).
4. Implied entry valuation (for newer investments).

The weighted valuation of these approaches depends on the type of investment and the availability of comparable companies.

What doesn't get factored into valuation is market sentiment, good or bad. As we know, sentiment can swing wildly and drive short-term pricing for publicly traded assets.

Because sentiment is a non-issue in private markets, valuations reflect only real changes in underlying business conditions that have shown up in a company's operating metrics. By avoiding sentiment-driven price changes, private asset pricing ends up being more stable, especially in market selloffs.

Illiquidity

Private markets are illiquid by nature. Assets tend to be held for years and exits take place after a business plan is concluded. If a private asset encounters challenges, there is simply no readily available market in which to dump it.

This creates two imperatives.

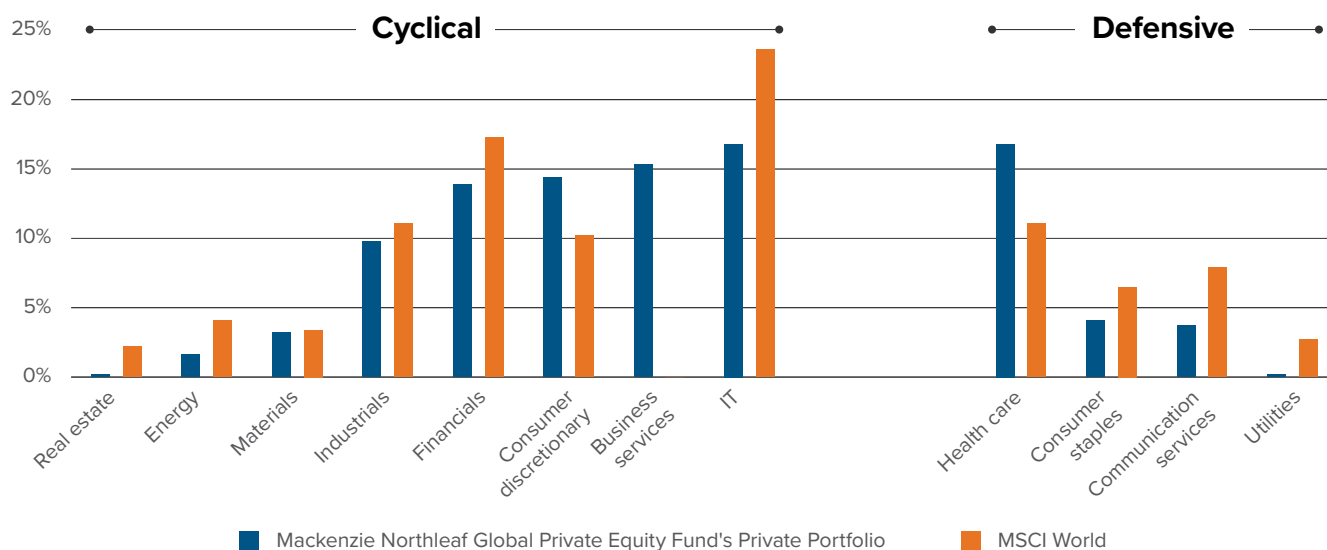
First, visibility into future revenues is essential. Successful low-volatility private investments tend to feature stable and predictable revenues either due to contractual obligations or the delivery of products or services deeply embedded into customer operations, making these revenues relatively impervious to market and economic fluctuations.

Examples include health care, essential/embedded enterprise software and IT services, HVAC/facilities maintenance and, in the case of infrastructure, essential services such as data communications, transportation and energy storage/transmission.

Additionally, many successful private investments avoid highly cyclical sectors such as travel and tourism or those dependent on resource prices, either as inputs or outputs. In fact, the sector exposure of buyout private equity, for example, is unlike the sector exposure of public market benchmarks. And concentrating investments in non-cyclical sectors naturally dampens portfolio volatility in comparison to the public indexes.



Understanding equity sector biases: public vs. private markets



Data as at December 31, 2024. Source: Northleaf Capital Partners, MSCI.

Second, once an investment in a non-cyclical sector is made, there is no easy exit — private investors must act as long-term owners.

This means it's critical to engage in careful initial and continuing diligence on every deal. Private market diligence is as extensive and detailed as any public market investment, if not more so. It often benefits from access to information sources beyond the reach of public investors, all of which enable wise and careful investment decision making.

Incentive alignment

A natural alignment of interest exists among private market investors. Private investment owners — whether general partners, limited partner investors,

management teams or lenders — have an exit mindset. They want the maximum payout, and so they will enact whatever operational improvements are required.

Private market governance models tend to enable faster decision-making. Owners are incentivized to contribute capital and talent to ensure each deal's success and have little incentive to exit companies during market lows.

As we expect US tariff policy to continue to drive the global economic outlook and capital market conditions, ongoing volatility and swings in investor sentiment are expected. The case for private market investments, with a tilt toward services rather than heavily trade-dependent industries, has the potential to provide a degree of insulation for portfolios.

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