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# Hedge Funds Gave Startups Billions. What Are They Worth?

A tech rout has frustrated investors trying to pinpoint the value of private companies. A Bloomberg analysis offers clues.

By Hema Parmar, Linly Lin and Noah Buhayar Wealth
Graphics by Mathieu Benhamou and Cedric Sam
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The pain — and then the questions — kept coming last year as prominent hedge funds took turns marking down the value of their stakes in private companies. Every time they wrote down holdings by millions, or even billions, of dollars, investors questioned whether they had gone far enough.

An exclusive Bloomberg News analysis offers a partial glimpse into one of the most opaque corners of the investing world, and the findings aren't reassuring. In many cases, hedge funds and other money managers disagree over how to value private companies, including some of the hottest, such as ByteDance and Discord.

One takeaway is that even after a year of writedowns across the investment industry, more may be in store. By the end of 2022, high-flying ventures known as unicorns lost more than 40% of their value from the year's peak, according to an estimate from private-market data provider Caplight Technologies, a sharper drop than the rout in publicly traded tech stocks and worse than the returns most hedge funds in the space reported. The disagreements over what companies are now worth have profound implications for the ultimate investors – from wealthy individuals to pension plans.

Five mega-hedge fund firms — Tiger Global Management, D1 Capital Partners, Lone Pine Capital, Viking Global Investors and Coatue Management — all ramped up their bets on startups in the past few years, wagering that soaring valuations and a hot market for initial public offerings would reap massive rewards. The gambles paid off handsomely in 2021, when a record number of private companies went public, locking in big gains.

The past year has been a starkly different story, with several hedge funds in this analysis posting record losses.

Dozens of the companies they bought into are also owned by mutual funds run by the likes of Fidelity and T. Rowe Price that are required to disclose valuations regularly. Mutual funds have been marking down some holdings even more severely than the drop in public markets.

Mining data from thousands of mutual funds over the past year, Bloomberg tracked down their valuations for 46 private companies that also count the five hedge fund firms as investors. Of those, about 70% of the private companies had been marked down by mutual funds through September last year, with an average decline of 35%. Some holdings were slashed by as much as 85%.

While this is just a fraction of the private companies the hedge funds invested in — Tiger Global alone has invested in hundreds across its hedge fund and venture strategies — it provides a rare glimpse into an obscure part of the investing world.

In some cases, the data show hedge fund marks haven't caught up.

Take software company Algolia, which Lone Pine first backed in July 2021. Between then and June — as inflation soared and interest rates spiked — mutual funds managed by Fidelity slashed the company's value by 39%, according to Bloomberg data.

Over the same time period, Lone Pine marked its Algolia stake down just 9%, according to investor documents seen by Bloomberg.

By the end of September, Fidelity's markdown reached 43%. It's unclear whether or how much Lone Pine has since adjusted its valuation for the company. Spokespeople for that hedge fund and the four others declined to comment for this story.

Private markets are notoriously opaque, and fund managers have wide discretion in how they value private assets. Though there are basic accounting standards, firms can use different metrics and processes. What's more, managers can price those assets as often as they choose — though most hedge funds opt to mark at least quarterly. Valuing private businesses is now all the harder with funding rounds on hold and IPOs stalled.

It's an art, said Jennifer Liu, a private market strategist at UBS Group AG. Every firm has its own nuance in how it marks holdings, she said. "That's why you could have one manager holding a company at a different valuation than another manager of even the same round" of fundraising.

Mutual funds offer an interesting comparison because they typically give clients more liquidity — the ability to buy and sell anytime markets are open. That incentivizes mutual funds to update asset values quickly, taking potentially more aggressive markdowns, so that clients who withdraw aren't overpaid. In contrast, hedge fund clients can typically pull cash quarterly, and venture and private equity ones may be locked in for years.

Fiercely private, hedge funds keep their asset marks to just themselves and their clients. That makes it difficult to gauge how far they're diverging from each other or mutual funds that hold the same companies.

"Not everyone is moving in concert," said Logan Bartlett, managing director of Redpoint Ventures, which backs consumer and enterprise startups.

The reasons for divergences are myriad. Compared with mutual funds, hedge funds tend to be more sophisticated investors with greater influence at the startups they buy into. They may negotiate special terms for their stakes, such as representation on boards or preferential treatment in future funding rounds or an anti-dilution clause. Money managers who purchase large stakes or buy directly, instead of in the secondary market, may also get more frequent updates on the venture's performance. All of that can impact valuations.

That means "the value that a hedge fund may be holding an asset at could be vastly different from what I am," Bartlett said, "because of the difference in their investor base, when they got into the investment, how the deal was structured, and the intellectual honesty of their methodology."

In some cases hedge fund marks were even harsher than the mutual funds. Viking marked down both Druva and Impossible Foods by between 25% and 45% through September, according to a person familiar with the matter, while mutual fund managers in Bloomberg's analysis kept both companies practically unchanged for the better part of last year. D1 marked down some companies more than the mutual funds did, a person said.

Disparities exist even among mutual funds themselves. Data show that managers like Fidelity and T. Rowe held TikTok owner ByteDance at starkly different values than BlackRock did for most of this past year. Meanwhile, the seven fund managers that held Databricks haven't agreed on a price over the past year. Valuations for Pine Labs and Gupshup also showed wide differences.

Still, mutual funds sometimes do agree — as was generally the case for Checkr, Stripe, Relativity Space and Nuro.

All five of the hedge funds tracked in this analysis trace their roots back to hedge fund pioneer Julian Robertson. Their managers started out as stockpickers. Then over the past few years, they became whales in the world of venture capital, propelling startups like Stripe, Instacart and Chime to lofty valuations.

But in 2022, most of the group posted their worst performance ever, hit by both plunging stock markets and markdowns on private companies, as startup financing got tougher amid economic headwinds. The Nasdaq fell 33% during the year, the deepest rout since 2008.

Lone Pine wasn't alone in writing down a slew of holdings. Tiger Global slashed its private funds by 24% in the nine months through September, while D1's dropped 23% through October.

While hedge funds each have their own systems for tweaking valuations, they typically examine a company's financials, recent fundraising and a basket of comparable publicly traded stocks. They also engage with outside valuation experts.

Tiger Global also considers prices that private shares are fetching in the secondary market and any special terms of its investment, according to a person with knowledge of the matter. The longer it's been since a funding round, the more Tiger puts weight on other inputs.

Tiger Global has a nine-person valuation team that assigns marks independently from its investing arm. At D1, the investment team assigns marks quarterly that are then reviewed by the firm's finance team, other people said. Ultimately, D1 ensures that final marks fall within a range provided by outside valuation experts.

More scrutiny comes at the end of the year, when auditors review marks – a process now underway.

With the economic outlook for 2023 as uncertain as it is, money managers and auditors may find it all the harder to agree on valuations, said Taylor Rosanova, principal at Marcum LLP, which audits year-end marks for investment firms.

"It's easier when companies are raising money like clockwork or when similar companies are doing exits," he said. "But now, you're relying more on public company multiples, and there's much more leeway for subjectivity."

Conflicts of interest can arise, according to due diligence experts. That's because the relationship can be intrinsically co-dependent: The fund needs the auditor's sign-off, and the auditor doesn't want to lose a multimillion-dollar client. Debates and compromises can result. One due diligence expert suggested watching for a clue: Funds that take longer than the industry norm to share audited year-end marks may have gotten bogged down in such negotiations.

There's no room for such debate in the stock market.

"In the public markets, you get humbled very quickly every single day," said Bartlett, from Redpoint. "But at least there is a definitive truth, and you can't argue with it, and it may even prompt you to revisit all of your assumptions. In private markets you invest in something and you put it in a jar. Psychologically there's a sense of 'What's done is done,' and you can't do much about it."