

KEYNOTE INTERVIEW

GPs turn to creative solutions to support new funds



*Both LPs and GPs are getting more sophisticated in their approach to raising capital and addressing liquidity challenges. There are now many more options on the table, says **Sam Kay**, partner and head of investment funds at Travers Smith*

Q What are the current challenges that you are seeing GPs facing in the fundraising market?

The fundraising market is still pretty robust. Certainly there has been a drop in the amount of capital raised for private equity, venture and private debt, so there are some issues, but it has held up well.

We see LPs focusing on the larger platforms and consolidating commitments with a smaller number of GPs to manage relationships, which creates two challenges. First, for in-demand GPs that are able to attract capital, the challenge is to find the right products to meet that demand. It is not just a case of raising the next flagship fund,

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but identifying the right vehicles to meet that need from LPs to consolidate relationships, which might mean raising growth capital funds or credit funds, for example. On the flipside, GPs that are not in that position need to differentiate themselves and find other ways of giving liquidity options to attract the right LPs.

Q What options are open to GPs that may have a more urgent need to raise capital?

That depends on why the capital is needed: whether it's to support an

existing portfolio, or because the GP has used up all its available capital and needs more cash to invest and capitalise on opportunities.

On supporting the portfolio, it is possible that a GP may not need to raise more capital and instead recycle to make the most of its existing assets. That's what a lot of GPs did in April and May last year when they were dealing with emergency funding situations. Rather than raising new pools of capital, many tried to make use of existing funds as efficiently as possible, by recycling or reinvesting proceeds received from the underlying portfolio to support existing investments.

For a GP that does need to raise capital, one option that is difficult and

not common is to re-open a fund. We have seen that done where a fund has been raised quickly with a single close, and then once the GP starts investing they go back and say they could still have been in the fundraising period so they want to increase capital in the vehicle to diversify or build the portfolio. That's possible but hard, because existing LPs are expecting the managers to be investing rather than raising money, and have concerns about dilution. It also requires LP consent to amend the fund documents.

Another option is to raise a top-up fund, going out to the market with a proposition not to make new investments but to support the existing portfolio. That may create issues around valuation, plus how to determine what value the top-up fund is investing in the portfolio compared to the existing fund, and ensuring equity and fairness between vehicles and their allocations. But those challenges can be dealt with, especially if a majority of existing LPs are willing to back that top-up fund.

Q What are the options when liquidity solutions are needed, and what are the challenges with those deals?

On liquidity solutions, GPs and LPs are increasingly working collaboratively to actively manage the portfolio. The options include using some kind of continuation fund to allow investors continued exposure to good resilient assets, with additional capital coming in to continue supporting those assets. GPs are keen to do that, and LPs who want liquidity get the option to cash out.

Another route is an LP tender offer, which instead offers existing LPs the liquidity option provided by a new investor or group of investors, brought in by the GP to buy out those interests. There are also other preferred equity options.

These options play into fundraising because by returning cash to investors it is more likely they will be able to

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commit more cash to a new fund. Generally institutional investors want cash back so that they can make a new decision about investing into a new fund.

Q What can GPs do if timing is an issue, either because a fundraising might take too long, or now is the wrong time to go to market with a new fund?

If the GP needs capital quickly, fundraisings do take a reasonable length of time. We hear about fundraisings done in a matter of weeks, but that ignores the planning that goes into that process before it launches – fundraising is more complicated than it used to be, with so many different regulations in different jurisdictions.

One option for a GP that needs capital sooner is warehousing, namely an arrangement with one or more friendly investors that capital will be available to make investments in the short term and the assets acquired will be transferred into the fund when it is raised. When marketing to new investors, the GP can show the first few assets have already been acquired, giving them comfort and reducing some of their risk going into a blind-pool vehicle.

Another option is raising a short-term fund, an annex or a sidecar, which can be done quickly without the process that goes into a flagship fund and can expressly be used to bridge the gap between where you are today and when you have the new fund in place. All these options are very much in play at the moment.

Q Finally, what steps are you seeing GPs taking to access different pools of capital, such as stapled secondaries or segregated managed accounts?

There are a number of ideas here. One is a stapled transaction where, when doing some kind of liquidity option such as an LP tender offer, a new investor coming in essentially promises to make a commitment to a new fund, thereby stapling the two deals. That's very much in the market right now. In order to achieve that, you want your lead investor coming to with the liquidity option to also have pools of primary investment capital available, so you do not want just secondary players.

As an extension of that, we are seeing GPs actively looking to diversify their LP base to have those types of investors in the flagship fund, giving them the option to approach someone already known to them to underwrite flexible solutions in future.

Segregated managed accounts are also quite common, where certain investors want a longer-term play that can be structured as a segregated managed account or a fund of one.

There is a lot of talk about permanent capital and how GPs can get access to that. We have seen transactions involving the larger GPs acquiring insurance companies to provide a degree of that availability. And then the other theme is around retailisation, which in many ways is the holy grail, getting retail investors into asset classes like private equity. That is also being very actively discussed in the market today. ■