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THE FUND FINANCE TRACKER

Key stats on fund finance provision for the private capital markets

3rd EDITION

Editorial

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In demand

Macroeconomic conditions have caused a surge in demand for fund finance, deepening the pre-existing supply and demand mismatch

Over the past six months, since the previous tracker was published, the fund finance market has been characterised by higher demand from GPs for these products. According to fund finance adviser Avardi Partners, “We observed a higher demand from fund managers for bespoke financings tailored to the fund’s strategy and needs, such as hybrid financings, umbrella capital call facilities and co-investment financings.”

However, a supply and demand imbalance had already been growing over the past year or so, with many banks in the fund finance space hitting their exposure levels thanks to a record high fundraising market in 2021. This mismatch has been compounded in more recent months by capital constraints placed on major US banks, who account for the lion’s share of fund finance lending.

Michael Slane of Investec’s fund solutions team notes that, “Changing capital requirements have materially increased the amount of capital banks need to hold for fund finance, and given how large those banks are they have no choice but to reduce exposure. But they want to find ways to support core clients and with that are less likely to be pursuing new opportunities.”

Given how much market share these banks hold in the fund finance space, reducing their exposure is having a major impact on the amount of debt available for these products. “Which has accelerated the move towards the mismatch between supply and demand - a journey we’ve been on for some time now,” notes Slane.

NEW SOURCES

Given that the pressure on banks to meet rising demand for fund finance has been mounting for some time, thankfully the industry has been busily building up new sources of capital in the form of institutional capital. However, the challenging macroeconomic conditions may cause problems here too.

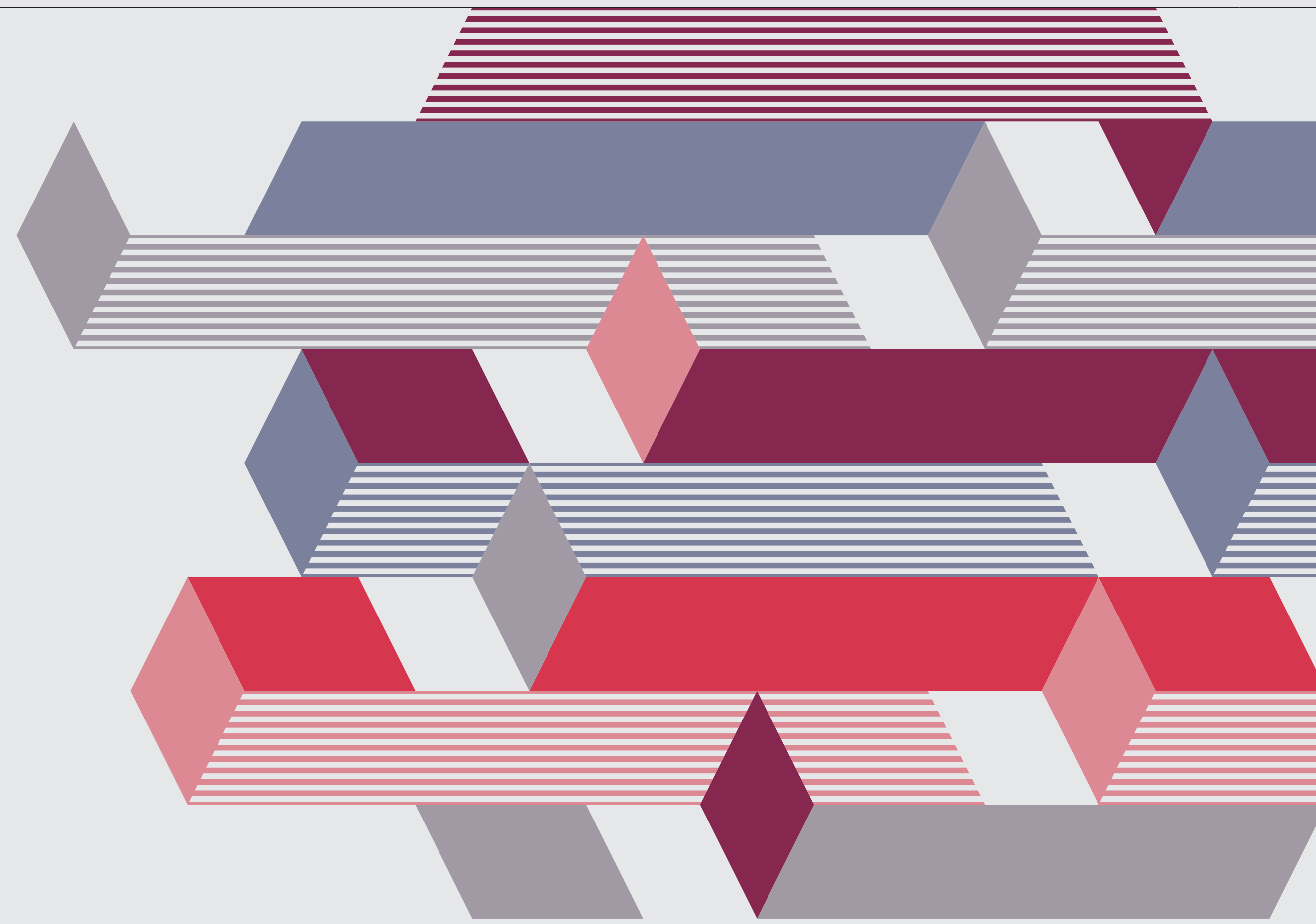
Institutional capital has been flowing into the fund finance market in recent years against a backdrop of low interest rates and a hunt for yields. But, as gilt spreads widen and AAA loan papers become more attractive thanks to recent interest rate hikes, institutional capital has more choice when it comes to where to allocate.

There is a silver lining, however. Lenders who have been steadily building inflows of institutional capital for fund financing are more likely to have strong, long term, robust relationships with those investors - meaning there can be confidence in that source of capital continuing to meet the demand for fund finance products. On the other hand, this will make it increasingly difficult for new entrants into the market wanting to develop third party capital solutions.

While that might be the case for subscription lines, when it comes to more bespoke fund finance products, including NAV lines, non-bank lenders are clearly taking advantage of the increased demand for these facilities, and the more attractive economics they offer.

While it has certainly been a very interesting six months since the last tracker, the fund finance market will likely face an even more turbulent time until the next report in Spring.

FUND FINANCE TRACKER



Despite major macroeconomic and political turbulence over the past six months, on the surface, the way in which the lenders included in this tracker are approaching the market remains largely unchanged.

However, what the tracker does not reflect is the increased selectiveness by lenders as to the funds they are willing or able to work with. The supply and demand mismatch in the fund finance space has been exaggerated in recent months, with GPs in need of more liquidity increasingly turning to these products, while lenders find themselves increasingly constrained, either because of high exposure levels or because of new restrictions placed on banks by the Federal Reserve.

Against this backdrop, a major focus for the fund finance market in the coming months will be on sourcing non-bank capital. Not an easy task given that institutional investment had been flowing into this market in the hunt for yield in a low interest rate environment. With those conditions changing rapidly, it will likely become more challenging to find institutional investors willing to increase allocations to the space.

Furthermore, as GPs increasingly seek out liquidity, NAV facilities, continuation vehicles and GP-leds have been on the rise. "These transactions represent a large volume of our activity," notes Michael Slane of Investec. "And we expect them to continue as the exit market continues to be challenging."

Subscription lines

Since launching the tracker, capital call facilities have been coalescing around similar terms, with little differentiation between most lenders. As this product became more commoditised, a point of differentiation emerged through ESG-linked offerings.

And for private equity houses, the adoption of ESG policies has clearly continued to deepen. According to Investec's latest GP Trends Survey, which polled 150 GPs in the UK and Europe, the vast majority (90%) believe that their ESG credentials will influence the likelihood of LPs committing capital to their funds, with 40% of this group expecting it to matter to a 'great extent'.

The report also revealed that the firms most optimistic about their fundraising - those expecting to raise larger new funds - are the ones leading the way in the uptake of ESG-linked debt facilities. These facilities, which rose to prominence since the pandemic, implement margin ratchet mechanisms which can either increase or decrease the costs on borrowings depending on GPs' compliance with pre-agreed ESG performance indicators, such as carbon emission reduction or diversity targets.

"There is clearly a macro medium to longer term trend towards ESG," says Slane. "And we've seen more funds coming to market with ESG investment themes. However, in the short term, because the market has been less stable, there has been a retreat back to basics."

Indeed, as GPs' need for liquidity - whether it be to support existing assets or to provide optionality to LPs - when it comes to fund finance, the priorities have shifted, with ESG seemingly slipping down the list.

	Fund strategy	Fund geography	Investor base (Institutional / Non-institutional)	Investor base (advanced on)	Minimum number of LPs	Single investor mandates
BANK OF IRELAND	Agnostic	Main focus is UK, Western Europe (1)	Predominantely institutional (2)		Typically 5	Yes
	1. Have offices in US, but less actively covered. 2. Relationship is important. Will consider FO/HNW on select basis.					
BNP PARIBAS	PE, RE, infra, debt, FoF	Global	Both (1)		One (2)	Yes (3)
	1. Depending on breakdown and credit worthiness. 2. Can do SMAs.					
COMMONWEALTH BANK OF AUSTRALIA	Agnostic	Agnostic but with connectivity to Australia (1)	Both		Agnostic	Yes
	1. Connectivity can be in the form of assets, operations, LPs, fund domicile, prior investments etc.					
DEUTSCHE BANK	Agnostic	Global	Both	Preference for institutional	One	Yes
ING	Agnostic	Agnostic		Only advance on institutional	No (1)	Yes (2)
	1. The more diversification the better, but can work with concentrated bases. 2. Quality of investor is key.					
INVESTEC	Agnostic	UK, Europe and North America	Predominantely institutional		No	Yes
NO LIMIT CAPITAL	Agnostic	UK, Europe and North America	Both (1)		One (2)	Yes
	1. Mainly Institutional and can look at both advance rate or coverage lending approach. 2. Can provide financing solutions to SMAs and highly concentrated LP bases.					
NORDEA	Agnostic (1)	Global, US, Nordics and Europe (2)	Predominantely institutional	Both	No	Yes
	1. Preference towards PE + other equity type strategies. 2. Not typically funds outside of our own geographical remit (Asia, LatAm).					
OAKNORTH	Agnostic	Needs to have a UK Nexus (1)	Both		One	Yes
	1. We only fund in £. NO CHANGE					
SUMITOMO MITSUI TRUST BANK (LONDON BRANCH)	Agnostic	EMEA (1)	Institutional (2)		One (3)	Yes
	1. With the exception of France. 2. Facilities are secured against commitments of externally rated institutional investors (minimum rating of BBB/Baa2). 3. We specialise in providing sub line facilities to SMAs and concentrated funds.					

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Syndicated or bilateral	Structure (Committed / Uncommitted)	Minumum Loan Amount	Maximum Loan Amount	Maximum % of total commitments	Maximum tenor	Structural flexibility	Will consider first-time funds	ESG linked facilities	Hybrid
Both	Both	€10m (3)	(4)	20-30% (5)	Up to 4 years	High (6)	Yes	Yes	No
3. No hard and fast cap. 4. Typically €100m per transaction. 5. No strict rule: guided by LPA, which is typically 20-30%. 6. Familiar to all the quirks of these loans. Cascading call pledge. Have done an umbrella facility whihc covers all previous vehicles, and did it in 3 weeks. CHANGE: Loan amounts changed from £ to €									
Both	Both	Dependent on fund	Dependent on fund	TBD before final close, 40% otherwise	3 years + extension options	High	No	Yes	Yes
3. Where there is strong relationship with manager and the investor. CHANGE: Minimum LPs down to one									
Both	Both	Preference for €50m (2)	Dependent on fund	Dependent on quality of investors	Dependent on fund	Medium	No	Yes	No
2. Assessed on case by case basis. NEW THIS EDITION									
Both	Both	€50m	€600m	Dependent on fund (1)	3-5 years	Medium (2)	No	Yes	Yes
1. Depends upon LP list & fund assets + leverage; no hard cap. 2. Umbrella Structures, Uncommitted Facilities, Letters of Credit. NO CHANGE									
Both	Mostly committed	Generally €25m	€300m (3)	Dependent on quality of investors	4 years	High (4)	No	Yes	Yes
3. Factors considered include diversification of LPs and track record of sponsor. 4. Flexible on advance rates, extensions, making adjustments to the borrowing base, can issue LCs and guarantees, can issue out of different branches across the network. NO CHANGE									
Both	Both	€50m	~€500m (1)	Up to 60% subject to LPA	5 years	High	Yes	Yes	Yes (2)
1. Beyond that will syndicate to banks. 2. Strong NAV experience enables hybrid facilities. CHANGE: Maximum loan amount reduced from €700m									
Both	Both	$/€/£ 100m	$/€/£ 600m (3)	Guided by LPA	Guided by LPA	High	Yes (4)	Yes	Yes (5)
3. Can club with our partner banks to deliver larger facilities. 4. If managed by experienced team with strong track record. 5. Including GP led transaction with single asset and concentrated investor base. NO CHANGE									
Both	Both	No (3)	Dependent on fund (3)	Dependent on fund	Dependent on fund	High (4)	Yes (5)	Yes	Yes (6)
(3) Prefer to be top tier lender, capacity for large tickets 4. Always willing to work with clients to solve their financing needs. 5. Under the right circumstances. 6. On a select basis. NO CHANGE									
Both	Both	£3m	£50m	66%	7 Years	High	Yes	Yes	Yes
Both	Both	$30m (4)	$150m	As per fund leverage restrictions	4 years (including extension options)	High	No	Yes	No (5)
4. We have considered smaller facility amounts to support clients and enhance longer term relationships. 5. We are looking to introduce this in the medium term. NEW THIS EDITION									

NAV lines

The market for NAV lines has sprung into life over the last six months. Despite lots of talk about these facilities for some years now, the increasingly challenging market conditions have meant a slowing down in exits, which is driving GPs to move quickly on securing NAV facilities. "We are definitely receiving a lot of enquiries about NAV lines, from all quarters including LPs themselves," says Slane.

Indeed, another major driver of increased demand for liquidity is the denominator effect, where LPs find themselves over allocated to privates because valuations of public investments have fallen.

As witnessed in the subscription line market, rising levels of demand and finite supply means that NAV lenders are now increasingly selective as to which funds they work with, and this can be seen in the tracker - while there are some new entrants for this report, they are picking and choosing their deals.

	Fund strategy	Purpose	Min Deal Size	Max Deal Size	Max LTV	Maximum tenor	Minimum number of assets
17 CAPITAL	Private Equity	(i) To raise additional capital for portfolio growth (e.g. buy & build) and/or (ii) generate liquidity for investors without selling	~€/$50m	Up to ~€/$1bn+	LTV advance rates of up to 65% (1)	Pref: no maturity date; Debt: ~5-7 years	Three
	1. Depending on counterparty objectives, diversification and structuring requirements.						
BNP PARIBAS	FoF, PE, Infra, Debt, RE	Additional capital for portfolio companies/ add-ons and providing liqudity to LPs	Dependent on fund (1)	Dependent on fund (2)	Dependent on fund (3)	Dependent on fund (4)	Dependant on fund (5)
	(1) (2) (3) (4) (5) Relationship and tailor made approach. NO CHANGE						
CRESTLINE	Agnostic (VC, Growth, PE, Real Estate, Real Assets, Infrastructure)	Loans to funds, loans to portfolio companies with fund guarantee, preferred equity and hybrid offerings	$10m+	$250m+	Depends on collateral	5 years +	One (1)
	1. Prefer portfolios with 3+ assets, but have limited single asset risk.						
DEUTSCHE BANK	PE, RE and Secondaries	Follow-on investments, cover for expenses, investor distributions or additional liquidity support to portfolio investment	€50m	€800m	Dependent on asset class (1)	Up to 5 years	One (2)
	1. PE (10-25%), Private credit/RE Debt (60-70%), RE Equity (20-35%), Primary/Secondary LP interests in funds (35-50%). 2. In the case of a continuation vehicle. NO CHANGE						
INVESTEC	Preference towards PE, Infrastructure and Real Estate	To accelerate liqudity to LPs, to build or defend value in the portoflio or for a GP based on its commitment or carry assets	€10m	€500m+ (1)	30-50% (2)	5 years	No
	1. WIth institutional investor partners. 2. Typically up to 30% for concentrated, and up to 50% on diluted.						
NO LIMIT CAPITAL	Agnostic	Acquisition of diversified portfolio of assets / provide liquidity to LPs	~€/$/£50m	~€/$/£100m	(1)	(2)	(3)
	1. Can be flexible and dependent on diversity of portfolio. 2. Depending on fund life we can be flexible on term. 3. Can be flexible and depends on asset class.						
NORDEA	Private Equity	(i) To raise additional capital for portfolio growth and/or (ii) to provide liquidity to LPs	No set minimum	No set maximum	Not set, but indicatively up to 25%	TBD	Dependent on assets, indicatively 5 for pure NAV
	NO CHANGE						
OAKNORTH	Agnostic	Agnostic	£3m	£50m	30%	7 years	Three
	CHANGE: Maximum tenor increased from 5 to 7 years						

GP facilities

Given these products are driven by the fundraising market, it is unsurprising that there has been a slowdown in deals. According to Preqin, private equity fundraising totals were down around 50% compared with the same period in 2021. And for H1 2022, according to Bain, totals dropped from $284bn to $138bn year-on-year.

Says Slane: "This has been a relatively quiet part of the market for once. These transactions are challenging and complicated, but in the past few months with the tightening of the fundraising market the core pillar of demand has definitely slowed down."

But that is not to say these deals will dry up completely, and Investec's GP Trends Survey showed there is confidence that capital will be raised. "However, the expectation is that it'll be slower with less of a rush to get them done," adds Slane.

	Purpose of loan
17CAPITAL	GP commitments, co-investments, strategic management company financing, working capital, new strategies, succession planning
	1. Repayment sources include management fees and/or GP commitments and/or GP carried interest from €/$500m to €/$1bn.
BNP PARIBAS	Co-invest, carried interest
CRESTLINE	Variable (working capital, commitments, buyouts etc.)
DEUTSCHE BANK	GP co-invest, strategic financing, working capital, new strategies, succession planning
	1. Assessed on a case-by-case basis, no hard cap. NO CHANGE
INVESTEC	Working capital support, new strategies, geographical expansion, succession planning, liquidity release
	1. Smaller deals require broader business case.
NO LIMIT CAPITAL	GP co-invest, strategic financing, working capital, new strategies, succession planning
	1. Can go longer for the right fund and manager. NO CHANGE
NORDEA	No preference (1)
	1. Would need to look at circumstances for each item: but can do all.
OAKNORTH	Agnostic
	CHANGE: Maximum deal size reduced from £50m to £30m.

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Approach to valuation	Ability to carve out assets from borrowing base	Ability to borrow at different levels	Cash sweep mechanism	Covenant package	Ability to include an accordion	Ability to include a revolving element	Hybrid	Structural flexibility
Fund's valuation	Yes	Yes	Yes	Pref: none. Debt: predominantly focused on prevailing LTV and underlying portfolio diversification	Yes	Yes	Yes	High (2)
2. Not constrained by bank regulatory capital rules / models. NO CHANGE								
Case by case basis	Yes	Yes	Yes	LTV and diverisification based	Case by case basis	Case by case basis	Case by case basis	Dependent on fund
Depends on collateral	Yes	Yes	Yes (2)	LTV and diversification based	Yes	Yes	Yes	High
2. Flexible based on borrower objectives. NO CHANGE								
Fund's valuation + 3rd party valuation	Yes	Yes	Yes		Yes	Yes	Yes	High
Fund's valuation	Yes	Yes	Yes	LTV (3)	Yes	Yes	Yes	High
3. Flexible, but designed around primarly LTV covenant that focuses on the value of the portfolio and the retention of some element of diversity. *NO CHANGE*								
Combination based on transaction	Yes	Yes	Yes	LTV focused	Yes		Yes	High
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Fund's valuation, right to call for external valuation under certain circumstances	Yes	Yes	Yes	Not set; indicatively LTV, diversity	Yes	Yes	Yes	High
Mix of all fund's valuation / own valuation / 3rd party valuation	Yes	Yes	Yes	Min NAV, % of NAV and ICR	Yes	Yes	Yes	High

Structure (Debt, Pref Eq, Both)	Maximum Deal Size	Minimum Deal Size	Maximum Tenor	Structural flexibility	Will consider first-time funds
Both (1)	~€/$1bn+	~€/$50m	Pref: no maturity date; Debt: ~5-7 years	High (2)	Yes (3)
2. Not constrained by bank regulatory capital rules / models. 3. On a case-by-case basis. CHANGE: Maximum deal size increased from €/$50m to €/$1bn +					
Debt	Dependent on fund (1)	Dependent on fund (2)	7 years	Medium	No
(1) (2) Relationship approach. NO CHANGE					
Both	$100m	$10m+	5 years+ (1)	High	Yes
1. Depends on size and Crestline Funding Vehicle. NO CHANGE					
Debt	Dependent on fund (1)	€10m	5 years	Low	No
Both	€200m	€5m(1)	7 years	High (2)	Yes
2. Advance rates, tenor, collateral package and legal structure. We have been creating bespoke GP facilities since 2008. NO CHANGE					
Debt	$/€/£ 100m	$/€/£ 50m	8 years (1)	High	No
Debt	No	No	No (2)	High	Unlikely for GP lines
2. Prefer to limit Tenor and extend instead. Typically facilities are 3-5 years + extensions. NO CHANGE					
Debt	£30m	£3m	7 years	High	Yes