mourant

UPDATE

Private Capital – Key Takeaways from the BVCA Summit 2023

Update prepared by Alex Henderson (Jersey)

In October 2023, members of Mourant's global funds team attended the BVCA Summit in London. The theme of the 2023 Summit was 'Private Capital. Public Value', exploring the economic, social, and public contribution of private capital. The Summit brought together leading figures from across the worlds of business, finance, and politics. We're pleased to share some of our key takeaways.

The environment for deals

Whilst deal volumes have been lower than in recent years, they are not significantly lower than pre-pandemic levels. The last couple of years have been record breaking, so don't provide the fairest comparison. It was noted that deals are still getting done, but managers are being more cautious and are, more than ever, looking for good value transactions.

On the sell side, managers want to keep good assets for longer, and may also be reluctant to sell good assets in a challenging market. Several commentators noted this may have fed into the use of continuation vehicles.

Another commentator noted that several private equity houses (particularly in the USA), 'desperately need' to deploy capital. The last two or three years have seen very buoyant fundraising, but not a lot of the capital raised has been deployed. Whilst managers certainly won't be doing bad deals, this undeployed capital (on which fees are accruing) does provide incentive to do deals. It was noted that investments made in the years after the 2008 global financial crisis turned out to be exceptionally well performing, and several commentators drew parallels to the current market environment.

The consensus seemed to be that challenging conditions will persist into 2024, but valuations have stabilised, and buyers and sellers are starting to find common ground.

Portfolio focus

Private capital continues to outperform public markets and provide exceptional growth in comparison. One commentator noted that if the public markets were a private capital fund manager, they'd have been unable to raise a successor fund because the returns would not be acceptable. Perhaps not the fairest of comparisons given the differences in, amongst other things, size and liquidity, but it emphasises the value that private capital can add to an investor's portfolio.

It was noted that competition for deals in the lower to mid-market space remains high and some mid-market managers are looking further down the value chain into growth opportunities, to access value opportunities.

Many noted the continued importance of EBT and other staff incentive schemes in their portfolio. It was noted that such schemes help reduce employee attrition which not only saves wasted effort on recruitment and training, but also helps cement a clear culture and purpose within the employee group.

Hotly tipped sectors for growth in the UK economy were digital, health, and financial and business services.

The environment for fundraising

As noted above, 2020 and the years that followed were buoyant years for fundraising. Investors have committed record breaking amounts of capital, but at the same time have seen a drop in distributions as exits have slowed. This can make for a difficult fundraising environment.

It was noted that as the industry becomes increasingly sophisticated, the barriers to entry for new fund managers continue to increase. Increased regulatory, compliance and reporting obligations/expectations are difficult to manage without the scale of an established manager.

It was also noted that investors are continuing to narrow down their relationships and focus on managers they have previously worked with. Not only is this making it difficult for new managers to raise capital, but it is also increasing competition between existing managers. Some commentators noted that lower to mid-market managers were needing to develop, and offer, sector specialisms to raise capital in a competitive market (see above).

Established managers are still successfully raising funds but it is taking longer to reach their target. Most of the capital is raised quite quickly, but the final third is taking longer. It was again noted that in many ways this is a return to the pre-pandemic normal rather than a cause for any concern.

The role of private capital in the UK's economic recovery

The view of a macro-economist was that inflation is temporary, and that inflation may drop quicker that the markets are currently predicting. That being said, the prevailing view was that interest rates are still likely to settle higher than the very low rates that have been seen since the global financial crisis.

Data was presented suggesting that capital investment by the UK Government has been largely flat since 2016, whilst other major economies (including the US, France, and Italy) have been increasing capital investment. Several commentators noted that further capital investment is unlikely to come from the UK Government, which is budget constrained with limited options to raise further revenue. The capital investment needed must therefore come from the private sector, and private capital has an important role to play. Asset classes such infrastructure and investment to assist the green transition particularly need private capital, but also regionally into the Midlands and the North, which are key battle grounds for the forthcoming General Election.

Whilst there are some concerns that the UK public is not overly supportive of private capital (particularly compared to other markets, such as the US) this may, to some extent, be assuaged if private capital can demonstrate its ESG credentials, particularly by being a good employer.

Democratisation of private equity

No private capital conference would be complete without a discussion on democratisation. The tension between investors needing liquidity and illiquid assets is always a feature but other interesting considerations were also raised.

It was noted that a key challenge of democratisation is privacy and that, for very valid reasons, there is often a need for a lot of confidentiality around assets funded by private capital. The companies can be fast growing, participating in a rapidly developing sector and/or have several competitors. It was noted that for democratisation to succeed, there would be a necessary reduction in transparency and investors can't expect to receive the same level of reporting (and access to portfolio company information) as existing institutional investors do.

One commentator also noted the challenge of the litigious environment in the USA where DC schemes will litigate over high fees, even if returns are strong. This can create reluctance among fiduciaries to allocate DC capital to asset classes (such as private equity and venture) with relatively higher fees.

Contacts

Alex Henderson
Partner
Mourant Ozannes (Jersey) LLP
+44 1534 676 037
alex.henderson@mourant.com

Alex Last
Partner
Mourant Ozannes (Cayman) LLP
+44 20 7796 7604
alex.last@mourant.com

Frances Watson
Partner I Advocate
Mourant Ozannes (Guernsey) LLP
+44 1481 739 331
frances.watson@mourant.com

2021934/88236514/1