HOT TOPICS AND TRENDS IN FUND FINANCE[1]

By Zainab Al-Qaimi

The panel's discussion revolved around the growing demand for liquidity in the market, and how participants have responded to this in search of a solution. The increasing influence of LPs in private debt investments was also discussed, as well as the rise in non-bank lending.

Key challenge – liquidity

Many of the recent trends in the market are driven by liquidity issues faced by all participants. With LPs suffering negative distributions, they have turned to fund finance for liquidity given that the macro-economic environment has prevented them from utilising typical exit routes, such as IPOs and M&A. As a result, GPs have turned to lenders for creative solutions in an attempt to generate liquidity and there has been a real push towards finding a solution in the form of a fund finance product.

Evergreen funds

The evolution towards open-ended structures allows LPs to reallocate their capital with greater ease – they are able to vote via asset allocation. These structures are designed to allow LPs to invest in a more liquid manner.

Capital pools

In light of the challenging fundraising environment, traditional institutional LPs cannot be relied on to meet the hard caps of funds. As a result, GPs are having conversations with lenders for smaller ticket sizes in the first instance in order to tap into the secondaries market, with a view of fundraising through private capital from high-net-worth individuals. Blackstone saw the largest inflow of private wealth at $8 billion in Q1 2024.

Valid concerns were raised on the panel as to the impact this may have on the borrowing base and therefore facility amounts as lenders have never been in the realm of lending against high-net-worth individuals in the past. However, it was concluded that the industry will cope given that it is a necessary adjustment to plug the gap in fundraising.

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[1] Panelists included Russell Evans (National Australia Bank); Alex Griffiths (MUFG Investor Services); Bronwen Jones (Reed Smith); Antoine Leboulanger (Ardian); Anthony Lombardi (DLA Piper LLP); and Katie McMenamin (Simpson Thatcher & Bartlett).

The growing presence of non-bank lenders in the market

Views across the panel were split on this point. At its core, the support for alternative lenders depends on what they are able to do – as there are vast discrepancies in this across different providers. As a part of the syndication process, non-bank lenders who are able to execute revolving credit facilities are viewed more favourably as this allows them to slot into existing structures seamlessly given that many alternative lenders are only able to structure tranche loans. However, it was noted that banks have begun adopting tranche loans to enable them to compete in the market, suggesting that non-bank lenders are here to stay.

On the other hand, it was raised that these structuring limitations ultimately reduce the flexibility of GPs as clients. While the insistence of many non-bank lenders on term loan tranches has proven to be a source of additional capital to the service providers of the sector, it is GPs that will have to absorb these increased costs.

NAV facilities

It was noted that while NAV facilities are a hot topic in the market at the moment, they are not a homogenous product (as bad press makes them out to be) nor are they novel. NAV facilities as a product have existed for some time, particularly in the secondaries and credit space – here LPs are well versed in their use. It is not so much that NAV facilities are a new concept, but rather that there is now a wider pool of LPs that are more focused on this and thus are more willing to ask GPs the difficult questions – painting the picture that they have more power.

The current views held by LPs are not unanimous, and there are varying thoughts on the use of NAV across various asset classes. The key to the broadened adoption of NAV facilities is education – not solely among LPs, but also regulators. Lenders recently received letters from the Prudential Regulation Authority to ask questions. It is important to educate the market on the necessity of NAV and how it can be controlled. Communication is crucial on the nuances of NAV as an option and when they may be best suited.