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TRANSCRIPT

Trends in Private Equity 2015
With Mounir Guen of MVision Private Equity Advisers

David Snow, Privcap:
Today, we're joined by Mounir Guen of MVision. Moose, how are you doing today?

Mounir Guen, MVision:
I'm very well, thank you, David. It's nice to see you.

Snow: Thanks for joining Privcap. You're a long-time fundraiser. I'm interested in your analysis about what's going on in the fundraising market for private equity. 2015 has been a relatively robust year. It wasn't much bigger than 2014. What do you think were some notable trends in 2015?

Guen: One of the things you have to remember is that fundraising statistics are very related to who's coming to market in a particular calendar year. If the large funds come to market, the numbers will be higher. If the large funds aren't in the market, the numbers will be lower. When I first started in the business, a $500 fund became $1.5, became $3, became $6 and so on. We're rarely seeing that these days.

Snow: By way of just increasing size that dramatically.

Guen: That's correct. And part of that was that the volume of capital within the market, which was new to the asset class, was going from 2% to 3.5%, 5%, 6%, 7.5%, 8%, 10%, 12% or, in some cases, 15%. In some cases, even more, right? So, you had this movement along the side, as private equity was just non-existent as a percentage of total GDP activity and was in a very nascent form.

Now it's accelerated incredibly fast, and the investors—where in those early days took on the exposure and the differentiation and the sets of criteria they used to identify who they would like to build their portfolios with—were still on a nascent format. Today, they're quite sophisticated, so one thing the investors have done is they've decided to reduce the number of relationships and put more money to work.

What they're seeking is deployment velocity to get that money going, preservation of capital, to protect the commitment they've made. They're looking for a certain target return rate, which varies according to program and size of program.

Snow: In general, are the very largest programs in the U.S.—say, the big state pension funds—looking for lower target returns typically than a smaller program?

Guen: Again, each program has its own criteria. There's a range between 2x net and 1.5x net, and it varies. Again, it's to the needs of that particular program in its evolutionary stage. Going back to the investors, what's happened with them—which is, again, very different in today's market—is that they're looking at primaries, secondaries or some form of direct. Co-invest, co-underwriting or direct strategics—there's all sorts of nomenclature. That's actually growing.

What they're doing is saying in a particular calendar year, "I need to generate this type of return profile and I have this variety of products." Then, within that, private equity, real assets, credit and real estate. Now, they're approaching the asset class from a matrix combination, looking at their j-curves and at the capital they need to put to work, identifying a target number they're seeking for that package and working across those products, identifying those general partners with whom they can have the best relationship to execute that target. That's very different from before.

This means that the relationship between a general partner and limited partner is different. The partnership five-year, 10-year structure—"You're over here, I'm over here, there's some form of alignment"—is now shaded or may be transforming. Because now, we're side by side and you have sector expertise. You, the investor, have product knowledge and I can benefit from having such a smart companion making investments with me. That's more prominent on the larger end, but it's going to move down the curve.

Snow: 2015 was probably the biggest year ever for distributions. What are LPs doing with all that cash?

Guen: Ah! It's a problem because they've got to put it back to work because, in a calendar year, they have to put 10% of their total assets in alternatives. And if they get all this cash back, they've got to move their market back.

Snow: Does that create an incentive for them to expand their GP relationships despite their stated goal of reducing?

Guen: It creates an incentive for them to try to commit more. For those general partners that have a good relationship, they'll try to push more. What happens then is, in certain markets like the U.S. or Europe, you've got funds and a spread of funds that can absorb (more in the U.S.). Europe hasn't had any new, large groups for a long time—I'd say almost 10 years now—and that needs to change. Whilst in the U.S., there's this very dynamic, very energetic kind of movement of new groups on a regular basis and scaling of these particular firms on a regular basis, and very impressive ones.

But, in terms of the absorption, this brings us to those two regions and the outside it pushes us more to the Pan-regionals, except for China. Australia is the only one outside of the Chinese, Europeans and U.S., [with] a particular GP that's $3 billion-plus. So, there's something going on in Australia.

Snow: Moose, what do you predict for the private equity market in 2016? What will be the big themes?

Guen: What will be the big themes of 2016? Interesting. I think there will still be continued interest in the U.S. I think Europe will have a good year in 2016 in terms of its activities and that the investors will continue their support to Asia, predominantly China, but also India as they grow. But they'll start looking at some of the other markets that are there. There'll be quite a nice gross and diversification. I think a lot of private-investor programs are going to continue increasing their exposure to the asset class and there will be further capital coming into the asset class.

In terms of performance, depending which investor you are and what the targets are, the general partners will achieve that performance on the whole. They're just getting better at being able to deliver. I also think the investor community is going to look at more creative ways to put their money to work and that there's going to be an emergence of a new type of investor, which is more family groups—so they're not necessarily foundations. These investors are quite flexible and they will look at diversification from their home markets. They'll look at targeting either a relationship with a general partner, a creative relationship with a general partner or a direct deal where they've got knowledge from their home market and feel very comfortable in.

So, I see a new form of capital coming into the market in 2016, which will be quite interesting. The other point I was going to make is that when I did an interview recently with some general partners in Europe, they were talking how robust their exits were and a lot of their exits were trade-oriented. So, I asked them who are the trades, and they were Asian buyers, mostly Chinese.