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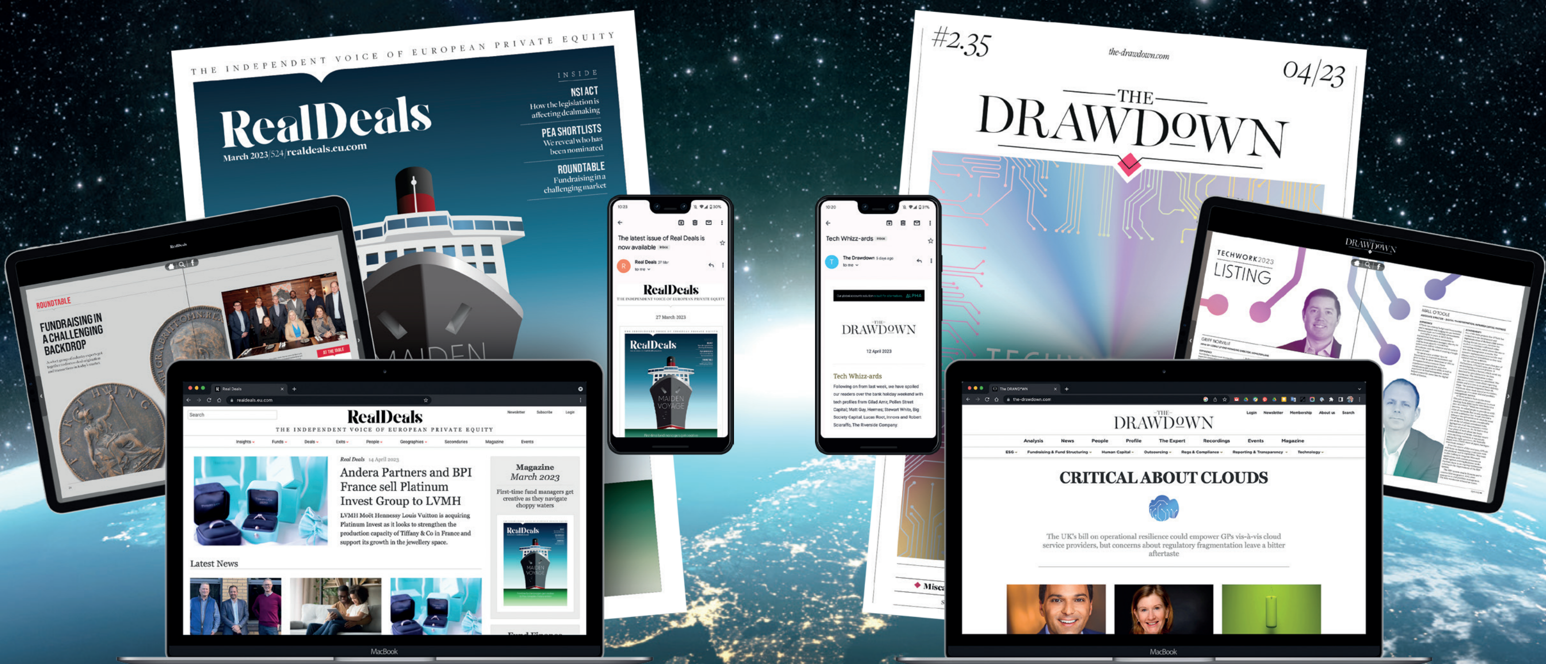
FUND FINANCE TRACKER 5

Key stats on fund finance provision for the private capital markets

September 2023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LEADER *Alice Murray*

Crunch time

Thankfully, the fund finance space has been far more stable since the last instalment of the *Fund Finance Tracker*. During the past six months, there have been no major fallouts or takeovers of key lenders in the sector. However, beneath the relatively calm surface, underlying structural challenges have intensified.

The most pressing concern is of course the continued retrenchment of major banks in the space. During the past six months, banks have continued to rationalise their relationships with sponsors, which means more focus on larger GPs, where there are greater opportunities for cross-selling, and a move away from smaller and mid-cap managers.

However, that does not mean large-cap managers are sitting pretty. As evidenced by this edition's tracker, lenders are reducing their ticket sizes in a bid to balance out their exposure. For sponsors, this means more lenders need to be involved in order to raise the size of facilities they are seeking.

The tracker has also picked up on a reduction in tenors. This trend further speaks to lenders' desire to curtail activity in the space. It also comes off the back of the higher interest rate environment, which has seen the cost of fund finance skyrocket.

Against this backdrop, GPs are asking more questions and thinking much more carefully about their use of fund finance products. For subscription lines, as they are increasingly harder to arrange and now more costly, this is resulting in a right-sizing exercise; ensuring these facilities are only as large and long as they need to be.

The past six months have also seen fund managers getting more creative when it comes to sourcing fund finance. As banks focus on what they deem to be more fruitful clients, sponsors are pushing on their relationships with other departments within the banks as a means of keeping the doors open.

Clearly, innovative solutions are desperately needed, and one possible remedy that has been much discussed is the greater involvement of institutional capital in the space. This could present a genuine panacea for smaller and midsized managers, with institutional investors – already well versed in the alternative fund space – stepping in to provide facilities where banks have stepped out.

And here is where another much needed innovation is coming into play – ratings. Our interview with Fitch highlights how ratings can help to bring in more institutional capital. Furthermore, ratings can also help existing lenders to reduce capital charges, and help banks enter the space for the first time.

However, we can already see signs that ratings only really help large-cap managers, which ironically need the least help, as the ratings are based on LP base (quality and diversification) and stability of finance and operations – both of which favour larger managers.

Whatever the outcome, one thing is clear: the fund finance market continues to mature at rapid pace, and I can say with certainty that during the next six months, more innovations and solutions will have come to the fore in response to the current challenges.

FUND FINANCE TRACKER

While the last six months in the fund finance space have been comparatively more stable than the beginning of 2023, the main challenges – namely the liquidity gap – persist.

"The market has definitely settled past that acute fear," agrees Investec's Michael Slane. "But it has settled into a different place to where we were at the beginning of the year."

Indeed, issues around capital constraints, with lenders focusing on relationships with larger funds, have meant that lower and mid-market managers are really feeling a shortage of available capital.

To free up more capital, lenders are increasingly attempting to access institutional capital. "There continues to be an educational piece around that," explains Investec's Sharon Thandi. "Where the fundraising market continues to be challenging, we're seeing a number of dynamics play out. One is the ability to have discretionary capital coming from institutional investors, which is a longer-term form of capital. This is definitely on the cards and more banks are looking to do this."

Another area within fund finance where institutional capital is becoming more prominent is for NAV loans. "We have seen an acceleration in the market for NAV financing with more lenders coming into this space and more managers using NAV financing as part of their toolkit, especially in the current environment to create liquidity. Given where the pricing of NAV facilities are, with the sharp increase in base rates this has become attractive for some investors as they're able to achieve equity-like returns," says Thandi.

While any form of additional capital in the space is welcome, question marks around how long this trend will continue are arising. "Interest rates are driving this trend at the moment," says Thandi. "If rates fall, that would change the return dynamic. And it is really only the NAV, bespoke, complex solutions where it is possible to charge a premium."

SUBSCRIPTION FACILITIES	**Fund strategy**	**Fund geography**	**Investor base (Institutional/ Non-institutional)**	**Investor base (advanced on)**	**Minimum number of LPs**	**Single investor mandates**	**Syndicated or bilateral**
abrdn	Agnostic	Agnostic	Both	Only advance on institutional	c. 10	No	Syndicated
	No change.						
Bank of Ireland	PE	Main focus is UK, Western Europe ***(1)***	Predominantely institutional ***(2)***		Typically 5	No	Both
	(1) *Have offices in US, but less actively covered.* ***(2)*** *Relationship is important. Will consider FO / HNW on select basis.* ***(3)*** *No hard and fast cap.* ***(4)*** *Typically €50m per transaction.*						
BNP Paribas	Agnostic	Global	Both ***(1)***		One ***(2)***	Yes ***(3)***	Both
	(1) *Depending on breakdown and credit worthiness.* ***(2)*** *Can do SMAs.* ***(3)*** *Where there is strong relationship with manager and the investor.*						
Commonwealth Bank of Australia	Agnostic ***(1)***	Agnostic but with connectivity to Australia ***(2)***	Institutional		Dependent on fund	Yes ***(3)***	Both
	(1) *Preference for infrastructure funds, however will consider all strategies.* ***(2)*** *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	Both
ING	Agnostic	Agnostic		Only advance on institutional	No ***(1)***	Yes ***(2)***	Both
	(1) *The more diversification the better, but can work with concentrated bases.* ***(2)*** *Quality of investor is key.* ***(3)*** *Factors considered include diversification of LPs and track record of sponsor.*						
Investec	Agnostic	UK, Europe and North America	Predominantely institutional		No	Yes	Both
NLC Capital Partners	Agnostic	UK, Europe and North America	Both ***(1)***		One ***(2)***	Yes	Both
	(1) *Mainly institutional and can look at both advance rate or coverage lending approach.* ***(2)*** *Can provide financing solutions to SMA and highly concerntrated LP bases.*						
Nordea	Agnostic ***(1)***	Global, US, Nordics and Europe ***(2)***	Predominantely institutional	Both	No	Yes	Both
	(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 or US nexus ***(1)***	Both		One	Yes	Both
	(1) Can look at US deals, can fund in € and $.						
Sumitomo Mitsui Trust Bank (London Branch)	Agnostic	EMEA ***(1)***	Institutional ***(2)***		One ***(3)***	Yes	Both
	(1) *Provide facilities to funds domiciled in EMEA (with the exception of France). Also have offices in the US, Singapore, Hong Kong and Tokyo to cater for their respective jurisdictions.* ***(2)*** *Facilities are secured against the commitments of externally rated institutional investors (minimum rating of BBB/Baa2).*						

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SUBSCRIPTION FACILITIES

The liquidity gap – the difference between levels of supply and demand – is most keenly felt in the sub-line market. According to Slane, not only is capital flowing towards larger managers, there is also evidence of this continued shift in the arranging rule. "We're seeing quality sponsors who would normally have a stable of banks looking for more arrangers."

He has observed the difficulties GPs are facing when bringing lenders into club deals. "We have a large pool on the deals that we arrange, comprising more than 50 counterparties, but the focus on the sponsor and further opportunities they represent has intensified significantly in recent months."

Another notable shift in the sub-line market in recent months is the reduction in ticket sizes. This can be seen in the tracker data, with several lenders reducing their maximum loan size for this edition. "We saw a bit of this in the previous tracker but it is more visible now," says Slane. "The number of banks willing to lend €200m+ is rare now as banks scale back their exposure."

Of course, the reduction in average ticket sizes only puts more pressure on the liquidity gap. Against this backdrop, Slane has observed greater collaboration between sponsors and arranging banks. "Sponsors are pushing their relationships in other parts of the bank such as custody services and wealth management."

This edition's tracker has also picked up on a reduction in tenors, which is another symptom of the weaker fundraising conditions. Says Thandi: "We're seeing shorter-term tenors of typically 12 months. Two-year or plus tenors are less common given where rates are. Overall, we're seeing more right-sized facilities ramping up to mirror the slower fundraising across the market."

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	Typically £25m	Typically c. £300m	Guided by LPA	4 years	High	Yes	Yes	Yes
Committed	£10m ***(3)***	***(4)***	20-30% ***(5)***	Up to 3 years	Medium	No	Yes	No
(5) *No strict rule: guided by LPA, which is typically 20-30%.* ***Change:*** *Maximum loan amount was previously €100m. Maximum tenor has decreased from 4 years to 3 years. Previously considered first time funds.*								
Both	Dependent on fund	Dependent on fund	TBD before final close, 40% otherwise	2 years + extension options	High	No	Yes	Yes
Change: *fund strategy, previously PE, RE, infra, debt, FoF - now agnostic. Maximum tenor decreased from 3 years to 2 years.*								
Both	€50m	Dependent on fund	Dependent on quality of investors	Dependent on fund ***(4)***	Medium	No	Yes	No
(3) *Preference for diversified investor base, however can provide financing for a single Australian investor.* ***(4)*** *Preference for 2-3 year tenor.* ***New for this edition.***								
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.***								
Mostly committed	Generally €25m	€200m dependent on fund ***(3)***	Dependent on quality of investors	3 years + extension options	High ***(4)***	No	Yes	Yes ***(5)***
(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.* ***(5)*** *Limited and under the right circumstances.* ***No change.***								
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.* ***No change.***								
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	No ***(3)***	Dependent on fund ***(3)***	Dependent on fund	Dependent on fund	High ***(4)***	Yes	No	Yes ***(5)***
(3) *Prefer to be top tier lender, capacity for large tickets.* ***(4)*** *Always willing to work with clients to solve their financing needs.* ***(5)*** *On a select basis.* ***Change:*** *Will no longer consider first-time funds.*								
Both	£3m	£75m	66%	7 Years	High	Yes	Yes	Yes
Change: Geographical expansion to US, and ability to fund in € and $ (as well as £). Increase in maximum loan size from £50m to £75m.								
Both	$50m ***(4)***	$200m	As per Fund leverage restrictions	5 years (including extension options)	High	No	Yes	No ***(5)***
(3) *We specialise in providing sub line facilities to SMAs and concentrated funds.* ***(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.* ***Change:*** *Minumim loan amount increased from $40m to $50m and maximum loan amount increased from $150m to $200m.*								

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NAV LINES

Sponsor appetite for these facilities continues to strengthen. Says Thandi: "We're very much seeing more managers looking to explore NAV facilities, and that has picked up more recently with transactions being executed in recent months."

According to Thandi, a good proportion of increased activity is coming from managers using these facilities for the first time. "There are several dynamics at play here which are driving increased activity for NAV facilities. A key driver is to create liquidity, perhaps that is to support the existing portfolio of assets, such as financing bolt-on acquisitions."

Another driver for increased NAV activity is coming from the difficulties faced in the fundraising market. "Sponsors are using NAV facilities to create liquidity for their LPs, using the proceeds to facilitate distributions

NAV LINES	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.						
Ares	Agnostic	Investment, distributions, defensive and offensive			up to 70%		Three
	New for this edition.						
BNP Paribas	FoF, PE, Infra, Debt, RE	Additional capital for portfolio companies/ add-ons and provide liquidty to LPs	Dependent on fund ***(1)***	Dependent on fund ***(2)***	Dependent on fund ***(3)***	Dependent on fund ***(4)***	Dependent 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)	Support, grow and protect underlying portfolio companies, acquire new assets and support strategic initiatives	$25m	$500m+	Depends on collateral	5 years +	One ***(1)***
	(1) Prefer portfolios with 3+ assets, but have limited single asset risk. ***(2)*** Flexible based on borrower objectives. ***Change:*** Maximum deal size increased from $250m to $500m+						
Deutsche Bank	PE, RE and Secondaries	Follow-on investments, cover for expenses, investor distributions or additional liquidity support to portfolio investment	€50m	€800m	Dependent on asset class ***(1)***	Up to 5 years	One ***(2)***
	(1) PE (10-25%), Private credit/RE Debt (60-70%), RE Equity (20-35%), Primary/Secondary LP interests in funds (35-50%). ***(2)*** In the case of a continuation vehicle. ***No change.***						
Investec	Preference towards PE, Infrastructure and Real Estate	To accelerate liquidty to LPs, to build or defend value in the portoflio or for a GP based on its commitment or carry assets	€10m	€500m + ***(1)***	30-50% ***(2)***	5 years	No
	(1) WIth institutional investor partners. ***(2)*** Typically up to 30% for concentrated, and up to 50% on diluted.						
NLC Capital Partners	Agnostic	Acquisition of diversified portfolio of assets / provide liquidity to LPs	~€/$/£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	Equity	Support, grow and protect underlying portfolio companies, acquire new assets and support strategic initiatives	No set minimum	No set maximum	Indicatively ~15% ***(1)***	Up to 5 years ***(2)***	Dependent on assets and fund ***(3)***
	(1) Subject to analysis of underlying assets. ***(2)*** Depending on fund lifecycle. ***(3)*** Needs to be well diversified at inception.						
OakNorth	Agnostic	Agnostic	£3m	£50m	20%	7 years	Three
	Change: Maximum LTV reduced from 30% to 20%						

GP FINANCE

As picked up in the previous tracker, GP line transactions haven't been hampered by a weaker fundraising market, as these facilities are also key for continuation vehicles. However, both Slane and Thandi see plenty of drivers when it comes to GP facilities. "It does feel as though fundraising is picking up, albeit more slowly and with multiple closes. But it does feel as though there is more momentum," says Slane. "And of course there is still a lot of continuation vehicle activity. Both events drive GP line activity, so it feels steady on both sides."

"We are still seeing those core reasons for exploring GP financing," adds Thandi. "Such as first-time funds or succession planning, or where there have been fewer distributions coming out of third or fourth funds – all of these factors are driving the use of these facilities." ●

GP FINANCE	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.
Ares	
	New for this edition.
BNP Paribas	Co-invest, carried interest
Crestline	Working capital, commitments, seeding new strategies, management company financing, other strategic initatives
Deutsche Bank	GP co-invest, strategic financing, working capital, new strategies, succession planning
Investec	Working capital support, new strategies, geo expansion, succession planning, liquidity release
	(1) Smaller deals require broader business case.
NLC Capital Partners	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

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With the continued uptick in NAV activity, a range of structures are being used. "At one end, traditional banks are providing secured loans, and at the other end you have preferred equity instruments. We're seeing a real mix in how these facilities are being structured and it depends on what works for the sponsor, their underlying portfolio and who the lenders are," adds Thandi.

In terms of pricing for these facilities, Slane says the shift in mindset from hurdle to return rate has continued. "It takes time to adjust, but that exploration of NAV continues to progress. We're seeing less talk and more action in this space. From speaking with CFOs, they clearly have a better idea of market standards and which type of lenders to approach."

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	Hybridv	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.***								
Fund's valuation	Yes	Yes	Yes	Pref: none. Debt: predominantly focused on prevailing LTV and underlying portfolio diversification	Yes	Yes	Yes	High
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
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	. ***(4)***	Yes	High
(4) Combination based on transaction. ***No change.***								
Fund's valuation, right to call for external valuation under certain circumstances	Yes	Yes	Yes	LTV and diversification based	Yes	Yes ***(4)***	Yes	High
(4) Subject to ceratin restrictions. ***Change:*** Maximum tenor changed from 'TBD' to up to 5 years.								
Mix of 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. ***No change.***					
Both	$1bn	$50m	Pref: no maturity, debt 7 years	High	No
Debt	Dependent on fund ***(1)***	Dependent on fund ***(2)***	7 years	Medium	No
(1) (2) Relationship approach. ***No change.***					
Both	$100m	$25m+	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
(1) Assessed on a case-by-case basis, no hard cap. ***No change.***					
Both	€200m	€5m ***(1)***	7 years	High ***(3)***	Yes
(2) For strategic it varies and we go up to 9%. ***(3)*** 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 ***(3)***	Unlikely for GP lines
(2) Prefer to limit Tenor and extend instead. Typically facilities are 3-5 years + extensions. ***(3)*** Focus on lending against recurring fees. ***No change.***					
Debt	£30m	£3m	7 years	High	Yes
No change.					

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