Which fund categories are most likely to appeal to investors in 2019?

DAVID ARCAUZ

Managing Partner, Flexstone Partners

For sophisticated investors, the small and mid-market sectors will remain a focus in 2019 on a global basis. This space offers the opportunity for consistent outperformance in different phases of the economic cycle. Managers tend to pay lower entry multiples than the larger funds and they can use their operating partners and skills to grow and fix the businesses.

While the spread of mid-market returns is wider than for larger funds, the ability to pick the best funds and gain access can lead to significant outperformance. Since we are at the later stages of an economic expansion, managers with the ability to implement operational improvements without using higher levels of financial leverage should continue to be a focus for private equity investors.

In addition, given the concern of record high valuations, investors are increasingly seeking opportunities to create value at lower multiples, even if the initial platform investment is higher, by making add on acquisitions and use operational skills to integrate and build the platform.

RICHARD HOPE

Managing Director, Hamilton Lane

Last year we received approximately 900 PPMs globally. The amount of capital raised in Europe alone was approximately EUR160 billion.

On average, we see around 30 per cent of capital (following exits) coming back into the market, which is a huge amount of money. We see these exits happening but equally we see a huge clamber on the GP to buy deals. That requires real discipline: how much are you willing to pay? How high will you go to complete a new deal? That's the big challenge. When we do due diligence with managers, this is one of the areas we spend a lot of time discussing. What is the GP's investment angle?

How will fee structures evolve in 2019?

JON EDIRMANASINGHE

Partner, Cavendish Corporate Finance

The 2/20 per cent private equity model has been the norm for many years, however there continues to be a shift away from this. Increasing amounts of private equity funds and related fundraisings have led to competition and the need for some to deviate from the norm.

Funds have increasingly become more flexible with their structures, for example reducing the 2 per cent entirely or offering various discounts based on the amount of capital committed. The 2 per cent management fee appears to have come under more pressure, with capital commitment discounts or time-based step-downs now being offered by some funds.

The 20 per cent carried interest rate on an 8 per cent hurdle still appears to be the norm as investors are typically happy to pay for performance.

How far do you think investors will push for further customisation on fees?

DAVID ARCAUZ

Managing Partner, Flexstone Partners

Regarding customisation, the market is bifurcated between the larger investors who are seeking to use their scale to create customised accounts and reduce fees and smaller investors, many of whom are the newer investors to the asset class such as high net worth individuals or family offices, that do not have the staff or access to the best investment opportunities and do not have the scale for customised accounts and fee negotiations.

However, investors do not only seek customised separate accounts to reduce fees as they are often seeking other dimensions such as tenor, liquidity, industry or geographic concentrations, scale, transparency, co-investments, or the ability to opt out of certain sectors or avoid/underweight for ESG or social impact reasons. Therefore, customised separate accounts are increasingly in demand even if fees are not reduced.