The Debrief

European Fund Finance Symposium – a Ten-Point Summary

29 October 2018

On 24 October, Debevoise sponsored and spoke on a panel at the Fourth Annual European Fund Finance Symposium in London, hosted by the Fund Finance Association. We have summarised below a few of the key topics discussed during what was an enlightening day for all those in attendance.

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- **Development of fund financing**. A growing number of fund financing products are being offered by an expanding market of finance providers. As fund structures become more bespoke, banks and other finance providers continue to seek to offer unique and sophisticated financing solutions. Non-banks are now entering the fund-level lending market.

- **NAV/Hybrid Facilities**. Net asset value facilities and hybrid facilities (where the borrowing base is a combination of uncalled investor commitments and fund investments) are becoming increasingly popular, and are now being raised by a range of funds—not just credit and secondaries funds, but also infrastructure, real estate and private equity funds. The terms of these types of financings are bespoke and depend on how the facility will be used, the relevant asset class, the negotiating position of the parties and the relationship between the parties.

- **Relationships**. Despite increasing sophistication and more participants—there are over 30 active subscription facility lenders—fund financing remains a relatively relationship-based industry. Because both sponsors and finance providers view fund financing transactions as partnerships, the creation of subscription facilities is often viewed as an opportunity to build a relationship upon which future transactions can be based.

- **Interest rates**. As interest rates increase, sponsors will continue to balance the benefit of subscription facilities and the cost of accessing subscription line debt. However, the normalisation of interest rates is not expected to affect the appetite for subscription line facilities.

- **Quality of investor pool**. The pool of investors continues to expand, and more and more of them wish to invest in funds through a separately managed account (SMA) structure. Numerous lenders are willing to lend to an SMA despite the increased concentration risk (*i.e.* the ultimate lender recourse is to the uncalled capital of a single investor rather than multiple investors), but lenders commonly request a letter from the SMA investor confirming the investor's funding obligation directly to the lender.

- **Abraaj**. The collapse of the Abraaj Group raises numerous issues, particularly involving lenders' recourse to fund investors. It remains to be seen whether lenders will seek to amend the terms of subscription facility documents to protect against these perceived risks. In any event, lenders can be expected to enhance their due diligence of fund managers. Despite this, the fundamentals of subscription facilities remain robust and Abraaj is (hopefully) an isolated incident.

- **IRR enhancement**. The consensus was that the enhancement to IRR from the use of subscription facilities is a side effect rather than the driving rationale for their use. With respect to the impact of use of subscription facilities, LPs tend to be more focused on transparency and the positive effects on cashflow management.

- **Fund financing process**. There is a broad desire for all parties to establish more efficient processes to expedite fund and finance closings. Sponsors typically require financing in place as soon as the fund is able to invest. The wish to streamline processes applies both to legal analysis of fund documentation and to finance providers' compliance and KYC requirements.

- **Technology**. There is a divergence between funds' practical use of technological platforms and the requirements of establishing certain types of fund financing. For example, capital call security perfection requirements sometimes do not reflect how funds actually communicate with their investors.

- **ESG**. The attention paid to environmental, social and governance issues continues to grow across financial markets. Finance providers, sponsors and investors were encouraged to be aware of how these issues might develop in their business—for example, requests from limited partners for statistics on a fund's employee diversity.

Please feel free to get in touch with the team if you have questions on any of the topics discussed during the symposium.

Alan Davies
Partner, London
+44 20 7786 9087
ajdavies@debevoise.com

Pierre Maugüé
Partner, London
+44 20 7786 9190
pmaugue@debevoise.com

Tom Smith
Partner, London
+44 20 7786 9174
tsmith@debevoise.com

Almas Daud
Associate, London
+44 20 7786 5456
adaud@debevoise.com

Daniel Hoborough
Associate, London
+44 20 7786 5503
dhoborough@debevoise.com

Felix Paterson
Associate, London
+44 20 7786 5454
fpaterso@debevoise.com