

## Fund Finance Friday



### Some Thoughts on the Near-Term Impact of the Current Developing Situation on Funds and Fund Finance

March 20, 2020 | Issue No. 69



By **Mike Newell**  
Partner | Financial Services

As the black swan event – in the form of COVID-19 – rips through our world and the impacts on health, society and the economy pile up, we offer some thoughts on the current and likely near-term impact on funds and the fund finance market. We do so with full knowledge that it is impossible to predict the future ... but in the hope that this will help to stimulate your own thoughts.

In terms of business generally, the most immediate and obvious impact on all parts of the fund and fund finance world (as with everything else) are the restrictions on travel, meetings and the switch to working from home. Although there is plenty of virtual contact being maintained, it is inevitable that the lack of face-to-face meetings will slow down fundraising timetables, in particular. This is likely to hit smaller and first-time managers harder and increase the notable bifurcation in the industry between the bigger managers, who typically fundraise quicker and more successfully (and have stronger ongoing relationships with their LP base and perhaps require less facetime for the time being), and the rest. Managers face challenges in hanging onto and converting identified pipelines of investments if there is a delay in fundraising and in their ability to demonstrate that they have the dry powder to potential vendors. On the financing side, we would expect to see a corresponding increase in the demand for warehousing arrangements, including related debt facilities, to bridge any gap between a fund being fully invested and the first close of the successor fund.

The current situation will also have a heavy impact on investors and their teams' ability to work at the same pace, with inevitable disruption to people's working patterns. Investors also face crises across various allocations in their portfolio and may need to reallocate resources away from longer dated alternative investments to ensure they can meet more immediate income requirements. Should all of this result in investment committees making fewer commitments for the time being, again, on the funds side, this potentially favours the larger managers with strong track records. On the finance side, this may lessen demand for some typical fund finance products (perhaps particularly subscription/capital call finance) but at the same time trigger greater demand for more bespoke funding solutions to allow funds to finesse their portfolios.

However, as always in defensive markets, there are likely to be certain niche strategies for funds that look attractive this year. It is likely that infrastructure and renewable energy strategies will be in demand. In the real estate world, we expect that it will once more be asset classes with infrastructure-like characteristics that are in vogue, particularly logistics (especially given the increasing uptake of home delivery services which we are now witnessing), healthcare and quasi-government-backed strategies such as social housing. We are likely to see less focus on development outside of such strategies but, no doubt, an uplift in opportunistic mandates. In private equity, we expect to see cleantech, fintech and biotech strategies continuing to be popular, but there may well be a retreat from emerging market strategies. For more mainstream strategies in developed markets, managers will need to convince investors that there are sufficient solvent targets to ensure deployment of commitments in accordance with current models. We also expect to see an increase in opportunistic strategies for credit, but investors will have concerns about possible impairments to the portfolios of existing funds and credit quality moving forwards in these markets.

We would expect new financing demand to follow and support these niche strategies, but it would be difficult particularly in the current economic climate to predict the extent of any lender's appetite to provide such support. We would also expect to see the defensive nature of the markets mirrored too in existing fund facilities, with funds possibly

looking (depending where they are in the cycle) either to repay some subscription/capital call facilities early or (particularly if earlier in the cycle) for these facilities to be more fully utilised. We may also see some increased demand (again, not necessarily reflected in a lender's appetite to provide) for new or extended subscription/capital call or asset lines to fund and protect existing investments, not least to bridge the potential fund raising gaps referred to above.

And, finally, as in all times when things get difficult, there will be opportunities, as well as a need for all parts of the industry to focus on the specific terms of their funding and financing arrangements, to keep communication lines clear and open, and to seek solutions to the difficulties that will inevitably come together.