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UK Fundraising Report

2019 edition

Contents

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UK fundraising set to weather Brexit storm

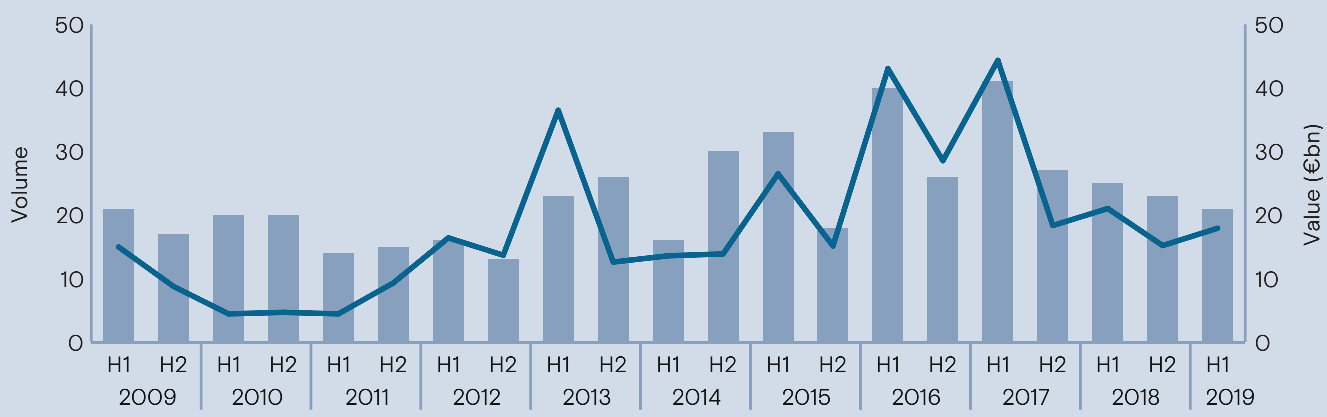
Gareth Morgan
Research manager

Private equity fundraising in the UK over the first five months of 2019 looks set to arrest its decline in 2018, with 21 funds raising a cumulative €17.93bn by the end of May. This compares with 23 funds raising €15.21bn in H2 2018, and 25 funds securing €21.03bn in H1 last year.

2019 numbers to date have been bolstered by the €10bn final close of the Seventh Cinven Fund, which hit its hard-cap in early May. Besides this, only three other funds raised a billion euros or more: Carlyle Europe Technology Partners IV (€1.35bn), Novalpina Capital Partners I (€1bn) and Investcorp European Buyout Fund 2019 (€1bn). Inflexion has also raised more than €1bn during 2019 so far, though across two separate vehicles. This dearth of larger funds continues a trend seen last year; back in 2017, 17 €1bn+ funds held a final close, but in 2018 there were just eight. With 10 €1bn+ funds currently in the pipeline, however, this trend may be the result of cyclicality amplified by the smaller number of managers able to attract this volume of capital.

Whilst fundraising in the UK has stabilised following the sharp drop from 2017 to 2018, buyout activity so far in 2019 has been muted, with 76 deals inked to the end of May at a cumulative enterprise value of €9.99bn. In contrast, H1 2018 saw 115 deals worth €17.05bn

Final closes of UK private equity funds



Source: *Unquote Data*

Fundraising for UK-based private equity firms hit the buffers in 2018 amid significant political uncertainty. Gareth Morgan examines how 2019 is shaping up and finds a resilient market in spite of the continued lack of political clarity

and H2 2018 recorded 118 deals worth €16.74bn, broadly in line with 2017.

Political turbulence and bifurcation

Unsurprisingly, the political situation is chief among investors' concerns surrounding the UK. "So far in 2019 it's been a continuation of 2018, with Brexit dominating the landscape," says Sunaina Sinha, managing partner at Cebile Capital. "There was an expectation that, regardless of a deal being made or not, by now there would be clarity on what would be happening. The fact this hasn't materialised is largely why LPs are putting their UK allocations on hold."

For a majority of LPs, who will already have uncalled commitments to UK-focused funds, further exposure can be difficult to justify. "LPs are inherently conservative," says Sam Kay, partner at Travers Smith. "Investment committees will ask themselves if the UK is the right place to be right now, and will find it difficult to justify adding to any existing UK-focused commitments." This is exacerbated by volatility in the exchange rate of the pound making any sterling-denominated fund more of a risky proposition for international institutional investors.

These factors are contributing to a phenomenon discussed in a recent *Unquote Analysis* piece and podcast; an increasingly bifurcated fundraising market in which larger, more established managers are able to leverage their international LP base, size and scale to significantly accelerate their fundraising, while the rest of the GP community struggles to attract the attention of LPs. "There is a two-speed market," says Sinha. "Larger brand ▶

Impact investing

One space that has continued to grow despite the political headwinds facing the UK is impact investing, with LPs increasingly demanding their assets are used for social good above and beyond simply generating financial returns.

This climate has seen a host of brand-name GPs launching impact-focused strategies, new sustainability- and impact-focused GPs coming to market, and longstanding impact investment firms successfully raising funds.

Notable examples from 2019 include Bridges Fund Management, which raised £80m for Bridges Sustainable Growth IV, and Circularity Capital's European Growth Fund, which held a final close in January on £60m for the GP's maiden private equity vehicle, which targets businesses operating in the circular economy.

Despite this momentum among GPs, the sense in the market is that LPs have much more capital to put to work in the impact space. "There is undoubtedly a supply-demand imbalance for impact funds in the UK," says Sinha. "Globally, GPs are shifting their narrative to tick more boxes to address this, including established firms setting up dedicated impact platforms."

The phrase "ticking boxes" – which in the past has been used in a slightly cynical way – refers to specifically measuring the impact of investments, notably against the United Nations' Principles for Responsible Investment and Sustainable Development Goals, two systems of measurement that are becoming industry standard.

Increasingly, this has meant that GPs are needing to benchmark themselves against these metrics, and many have set up dedicated teams assessing portfolio companies against these every quarter, alongside financial performance metrics, and to drive change within firms with the aim of improving scores.

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UK PE final closes 2019

FUND NAME	AMOUNT RAISED AT FINAL CLOSE (€m)
Seventh Cinven Fund	10,000.0
Carlyle Europe Technology Partners IV	1,350.0
Novalpina Capital Partners I	1,000.0
Investcorp European Buyout Fund 2019	1,000.0
Mayfair Equity Partners II	732.2
Inflexion Supplemental Fund V	686.0
Three Hills Capital Solutions III	540.0
Inflexion Enterprise Fund V	457.4
G Square Capital III	450.0
Cibus Fund	413.2
DouglasBay Capital Fund III	335.0
PIR Equities III	275.0
Investcorp Secondary Fund 2018	161.4
Maven UK Regional Buyout Fund	117.9
Bridges Sustainable Growth IV	92.6
Circularity European Growth Fund	70.4
Blossom Capital Fund I	68.4
VGC Member II	56.9
InReach Ventures Fund	53.0
ProVen VCT	45.4
Playfair Capital Fund II	28.1

Source: *Unquote Data*

"The success of larger managers is not at the exclusion of new GPs, and there is a new wave of GPs in the UK who are doing well despite the headwinds"

Sam Key, Travers Smith

names are able to raise quickly, where smaller firms are facing an anaemic fundraising market."

Examples of the former include the largest UK-managed fund to close so far in 2019, the Seventh Cinven Fund, which raised €10bn after four months on the road; Inflexion's double fundraise, which raised £1bn within 10 weeks of launch; and Bowmark Capital Partners VI, which again hit target within 10 weeks in December 2018.

With competition for space in funds intensifying, it is increasingly important for LPs to maintain relationships with their best-performing managers, and this means that the vast majority of their capacity to diligence funds is taken up by re-ups. In this environment, GPs left behind are having to be creative to kick-start fundraising. "As a placement agent, it's key to be able to point out how GPs are differentiated," says Sinha. "Things like deal sweeteners for coming in at first close, co-investment rights and stapled secondary deals are all levers to pull to build momentum in a raise."

Exceptions to the rule

However, despite the fast, successful raises of brand-name GPs, there are success stories elsewhere in the market that indicate there is demand for UK-based managers. "The two-speed fundraising narrative doesn't tell all of the story," says Kay. "The success of larger managers is not at the exclusion of new GPs, and there is a new wave of GPs in the UK who are doing well despite the headwinds." Indeed, 2019 so far has seen successful closes for Novalpina Capital Partners I (€1bn), Mayfair Equity Partners II (£650m), Three Hills Capital Solutions III (€540m) and G Square Capital III (€450m); all funds with a pan-European investment mandate or significant differentiation through sector specialisation, such as G Square's healthcare focus and Mayfair's TMT and consumer remit.

These examples underline the importance of differentiation mentioned above, and also that broadening investment horizons beyond the UK seems to be looked upon favourably by LPs at the moment.

Domiciling concerns

An aspect of fundraising that has been significantly impacted by Brexit uncertainty is structuring, with UK limited partnerships – once the go-to choice for GPs – increasingly falling out of favour. “While there is no single best structure for a fund, it is more difficult to justify using a UK limited partnership now,” says Kay. “GPs are increasingly looking at Luxembourg or the Channel Islands to domicile funds.”

These structures offer clarity on their status when marketing to EU investors, but do have issues with other factors such as tax, and base erosion and profit shifting. A high-profile recent example of a GP changing domiciles is Cinven, whose first six funds were UK-domiciled, but its latest is registered in Guernsey.

Keep calm and carry on

Overall, although 2019 is highly unlikely to match the stellar 2016 and 2017 vintages for the total value of capital raised by UK-managed funds, indications in the first five months of the year show the market is showing resilience in the face of significant macroeconomic turbulence. “It is testament to the strength of UK private equity that the market has not ground to a complete halt,” says Sinha. “The depth of the local LP base, the second largest in the world, is a key factor behind this, and although allocations to the UK are being trimmed, capital is still being put into the domestic market.”

With a fundraising pipeline that is targeting more than €35bn, and GPs becoming increasingly willing and able to refine their offerings in line with ever-demanding investor expectations, the UK private equity industry looks set to weather the storm and emerge stronger than ever. ■

UK PE final closes 2018 ≥€100m

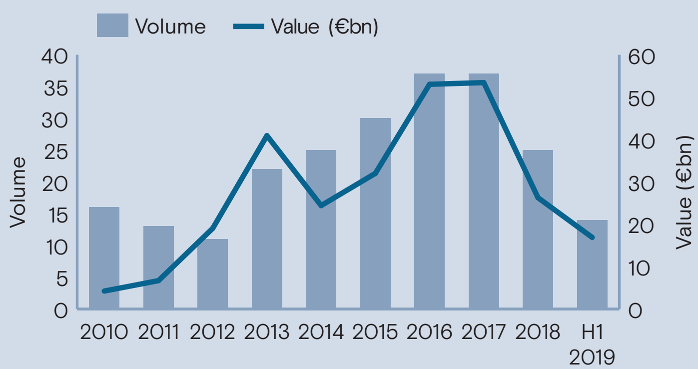
FUND NAME	AMOUNT RAISED AT FINAL CLOSE (€m)
BC European Capital X	7,000.0
Landmark Equity Partners XVI	6,598.9
TowerBrook Investors V	3,548.0
Equistone Partners Europe Fund VI	2,800.0
Hg Saturn	1,710.6
Inflexion Buyout Fund V	1,425.5
Inflexion Partnership Capital Fund II	1,140.4
Alchemy Special Opportunities IV	1,005.7
Epiris Fund II	963.2
Towerbrook Structured Opportunities Fund II	876.6
Index Ventures Growth IV	856.2
ECI 11	796.0
L-Gam II	772.0
Bowmark Capital Partners VI	669.6
IK Small Cap II	550.0
Graphite Capital Partners IX	532.6
PSC III	509.0
Bregal Milestone	400.0
The Dementia Discovery Fund	337.8
Investcorp Technology Partners IV	336.9
Eight Roads Ventures Europe III	307.0
Abingworth Bioventures VII	287.3
Horizon Capital I	227.6
Apiary Capital Partners I	227.1
Draper Esprit Venture Fund	200.1
Apposite Healthcare Fund II	199.1
Dawn Capital III	187.8
Volpi Capital Fund I	185.0
NVM Private Equity Vintage III	168.9
AV8 Ventures	150.0

Source: *Unquote Data*

Fund statistics

Buyout/generalist final closes

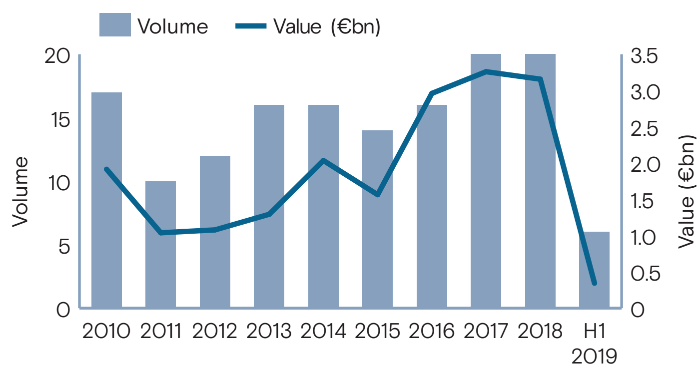
- 2019 set to arrest the 50% decline in UK buyout fundraising value seen from 2017 to 2018.
- Brexit concerns dominate LPs investment decisions.



Source: *Unquote Data*

Venture final closes

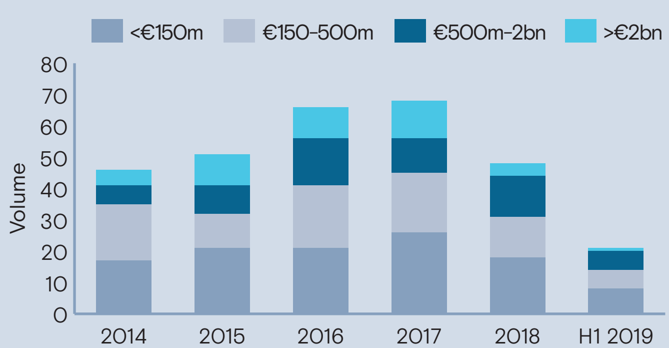
- Venture capital fundraising in the UK is in rude health, with 2018 bucking the downward trend seen in the buyout space.
- Slow start to 2019, with just €344m raised by six funds.



Source: *Unquote Data*

Funds raised by size

- Slowdown in large-cap fundraising continues into 2019, with just one €2bn+ fund holding a final close, although pipeline contains a further five large-cap funds in the market.
- Mid-market could match 2018 in terms of volume, while sub-€150m funds set to be down on last year.

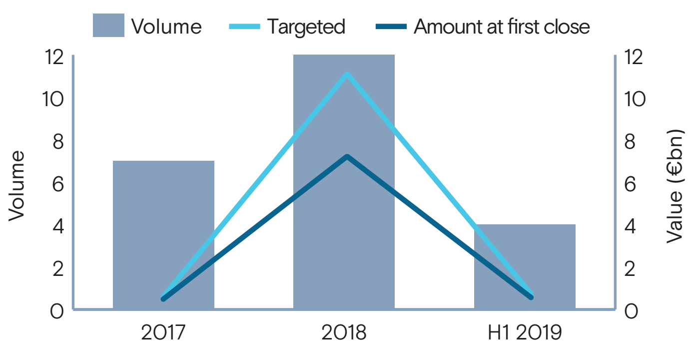


Source: *Unquote Data*

An analysis of UK fundraising data over recent years broken down by strategy and fund size, the annual change, and a look at typical investors

First closes of funds yet to final close

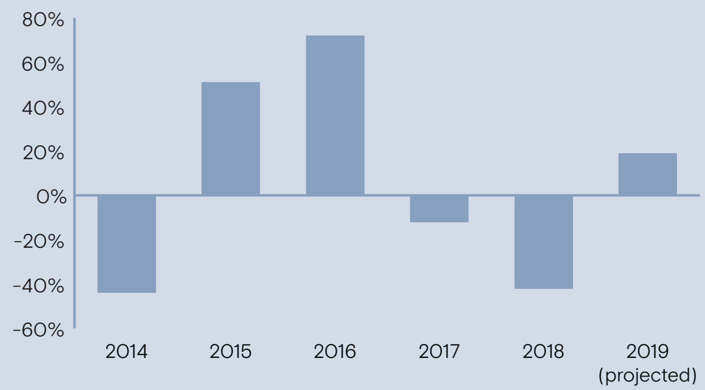
- Funds out in the market having held a first close since 2017 are targeting a cumulative €12.43bn.
- In H1 2019, four UK-managed funds held a first close, securing €564m against a €741m target.



Source: *Unquote Data*

Annual change in fundraising

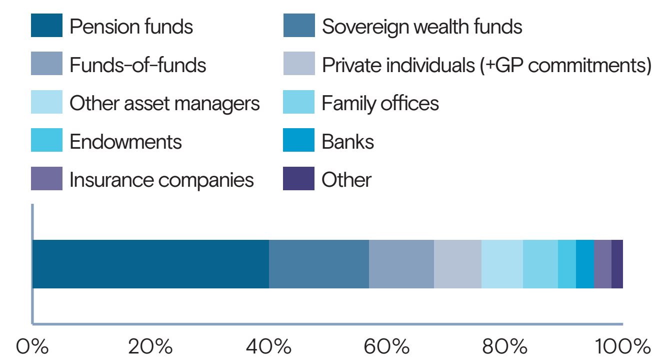
- Straight-line projections for 2019 indicate a year-on-year increase of around 20% from 2018.
- 2018 final value figures were 42% lower than 2017.



Source: *Unquote Data*

Investors in UK PE funds by type (2017 commitments)

- Pension funds committed 40% of the capital raised by UK-managed funds during 2017.
- Family offices, endowments and insurance companies cumulatively contributed 12% of the capital raised.



Source: *BVCA Report on Investment Activity 2017*

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Benefits of outsourced fund administration

Why do fund managers outsource?
Certainly for the larger funds, we've historically seen them established offshore to deliver economies of scale and reduce tax leakage, so the principal driver was substance and physical presence.

Increasingly, fund managers of all shapes and sizes are waking up to the broader benefits of outsourcing and the advantages of adopting a ready-made operating platform with tried and tested resources, systems and controls. And, from a cost perspective, it won't just be the case of the fund manager establishing the operating platform if they opt for the in-house path; they'll need to continually invest in it, too, as technology, regulation and the industry in general evolves.

> "Fund managers of all shapes and sizes are waking up to the broader benefits of outsourcing"
> *James Whittingham, Aztec Group*

The demands of investors are also changing. Gone are the days when investors were updated on a periodic basis through multiple spreadsheets with limited onward dialogue. Now they want quarterly updates, delivered in a clear and structured fashion, with access to knowledgeable and, above all, independent individuals who can answer their queries at the same time. This is, of course, something that a third-party administrator can offer.

What should I look for in an administrator?
To start with: integrity. Any choice of administration partner is a difficult one. It's a position where they'll be representing you to your investors.

You'll want to meet your operational team and be as comfortable with them as you would be if you were hiring them to work in-house. If the

partnership works as it should, you'll also want to be secure in the knowledge that your team will remain consistent as you work together throughout a likely 12-year cycle with the initial fund, and, hopefully, funds to come. The fund administrator should also be able to guide you through best practice reporting, being adaptable should you have particular preferences in what will be

Aztec Group director James Whittingham explains why more GPs than ever are commissioning an external fund administration team, and advises nascent private equity firms on what to look for from potential outsourced services

disclosed to investors. They should also be able to interrogate your limited partnership agreement for you, asking good practical questions as to how the fund will run in 'real life'.

Is that all I should be thinking about?

That's your 'front line' with an administrator; the additional benefit a manager will achieve with outsourcing is that the administrator's core operational team will be supported internally by specialist teams in information technology and security, legal, compliance, risk and technical areas. These teams will be available to call on should additional support be needed, often directly to the fund manager. Alongside that, the firm you select will have processes and procedures and likely an operating system that it would be wise to interrogate and understand yourself – especially if you'd like the relationship to work a certain way with additional authority checks or control steps above and beyond the administrator's 'core' framework.

It's the expensive option though, isn't it?

That's a question we hear fairly often. If you think about it in purely 'head count' terms, it can feel like that – fund administrators will often have a target revenue figure per employee, which can make it seem an expensive route. The additional benefit (and why it can end up more cost efficient) is in the specialist teams around the 'direct' employee or employees you're liaising with. The cost of administration will include the cost of a specialist private equity IT system, IT support, AML specialists, compliance and risk support, as well as a good window into what other fund managers are doing in terms of structuring and reporting, and investor and industry trends.

Additionally, investors are now so used to third party administration being part of any fund's operational framework that it is expected those fees will be charged through the fund itself and, therefore, is not a cost for the manager to bear out of the general partner share. There's no doubt that the fund manager should be seeking value in any administration engagement, but their charge should not be a direct drain on the manager's resources.

As a first-time fund, is providing administration services to us any different?

No, but I'd want my administration team to demonstrate a proven track record in similar situations and strong background in supporting firms of a similar size.

A suitably qualified administrator will be able to guide you through the whole process of launch and will collaborate with your legal firm to ensure first close is as straightforward as possible, as it can be a fraught time. They'll be able to walk you through the life of a fund and explain the provisions of the limited partnership agreement in a practical way. If the fund manager is very new, the fund administrator should also be able to enhance their service offering, adding accounting engagement for the manager itself, through to company secretarial support, should that be beneficial. ■

Sector specialisation taking hold

Oscar Geen
News editor

European private equity funds have invested in fewer sectors every year since 2012, according to analysis run by *Unquote*. Part of the explanation for this is the emergence of single-sector funds, a phenomenon observed in North America for more than a decade now, but which has been slower to catch on in Europe. However, even generalist funds have been narrowing their focus across vintages in a bid to stand out from the crowd.

In an increasingly competitive environment it is important to have a clear point of differentiation from other private equity firms. However, how this difference should be articulated, and to what extent a sector focus or specialisation should be integrated into it, is somewhat more divisive.

"We are definitely seeing more sector-focused funds, or funds focusing on just one or two sectors, than we have ever done previously," says Janet Brooks, managing director at placement agent Monument Group. "Our take on it is that with asset prices as high as they are and competition so fierce, firms really need to be prepared to make bold calls in terms of which processes they get involved with, and having sector knowledge really increases their chances of getting those calls right."

> "We are definitely seeing more sector-focused funds, or funds focusing on just one or two sectors, than we have ever done previously"
> *Janet Brooks, Monument Group*

Healthy appetite

One sector that has seen the launch of a number of dedicated GPs is healthcare, which had relatively few dedicated investors five years ago.

Nicolas de Nazelle is managing partner at placement agent Triago, which helped launch healthcare specialist Archimed in 2014. "We started looking at sector specialists in Europe in 2012. We had success in healthcare, consumer and technology in the US, so we started looking at those sectors in Europe. Consumer was essentially the only one we could find with the likes of Ergon, Lion, L Catterton and Change Capital."

Undeterred, Triago broadened and continued its search: "The next thing we looked at was whether there were groups that wanted to create a fund that came from healthcare," says de Nazelle. This led to the discovery of the team that would become Archimed, consisting of three ex-3i professionals and senior operational executives from the healthcare industry.

This capitalised on an increased need for operational improvement to drive returns. EY's 2018 report *Creating value throughout the private equity investment cycle in the digital era* claims that 60% of returns are now driven by operational improvement, up from 36% in the early 2000s.

"It is inevitable that operational improvement drives returns now," says de Nazelle. "Leverage is not really a value add and everyone buys

European private equity firms are sharpening their investment focus by restricting the number of sectors they target. Oscar Geen examines the transatlantic trend of sector specialisation in its European context

expensive, so you had better transform that company. If you buy a company at 16x and don't do anything to it, then good luck making money."

It is not only sector-focused funds that have adopted a more hands-on approach, as a proliferation of buy-and-build strategies will attest. However, Archimed founding partner Denis Ribon argues that sector funds have the edge over the longer term: "On a single deal, a generalist fund could be as good as a specialised fund because they could have a good operations partner or an adviser that focuses on that specific sub-sector, but the challenge is to have a consistent, long-lasting performance because you will not always be investing in the same sub-sector. In a healthcare fund you will have a few team members for each sub-sector."

This logic has led to a proliferation of healthcare-only buyout funds in Europe, from practically none when Triago first started looking in 2012 to a handful today, including UK-based firms such as G Square Capital – which raised €450m for its third fund in April – GHO Capital and Apposite.

Muscling in

The trend towards sector specialisation has driven some of the platform extension funds that larger managers have launched, such as Bain Life Sciences, where GPs use sector funds as an opportunity to raise more capital from their existing LPs. "The issue is that for some LPs it is difficult to find and diligence those smaller managers because they are small and highly sought after."

Says Monument's Brooks: "They may find it easier to access sector funds through their existing managers where they do not have to do the same level of diligence. As long as those teams are high-calibre, well-incentivised and any conflicts are handled well, that can be a valid way to access the sector." However, she adds: "At Monument Group, we want to see thriving, smaller, sector-focused and independent groups, because they are the groups we are more likely to be fundraising for."

This fits into the trend of bifurcation of the European buyout fundraising market. There is hope for the early adopters, though, says Archimed's Ribon: "There are more sector-focused funds, so as a sector-focused fund we become less differentiated. However, if you look at what happened in the US, the pioneers are still leading the race. There will be more but the first movers should keep an edge." ■

The research

We extracted all buyout and generalist funds in the *Unquote* database that had held a final close since 2005, and which had at least three portfolio companies. We then looked at those companies, counting the number of sectors that the fund had invested in and divided by the number of deals to give a concentration ratio.

Therefore, a smaller ratio means a more concentrated portfolio. Three funds had a concentration ratio of 0.17: Alto Capital III (consumer), Main Capital III (technology) and Siparex Midcap II (consumer, industrials). Only three of the 10 most concentrated portfolios were explicitly marketed as single-sector funds: Alto Capital III (consumer), Main Capital III (technology) and Apposite Healthcare Fund II (healthcare).

Placement agents & pipelines

A league table of the most active placement agents since 2014, and a selection of funds currently in the market, sourced from *Unquote Data*

Placement agents' UK fundraising activity Jan 2014-May 2019

Placement Agent	Number of funds raised	Total value of funds raised (€bn)
Rede Partners	10	8.2
Campbell Lutyens & Co	6	6.6
Triago	2	6.2
UBS	2	5.1
Credit Suisse	3	4.7
Quest Fund Placement	4	4.5
Park Hill Group	4	4.3
Asante Capital Group	9	3.8
Evercore Partners	4	3.5
JP Morgan Chase	1	3.3

A selection of UK funds on the fundraising trail

Fund name	Fund manager	Fund type	Fund target (€bn)
Permira VII	Permira	Buyout	10.0
Apax X	Apax Partners	Buyout	8.7
CVC Strategic Opportunities Fund II	CVC Credit Partners	Buyout	4.0
Montagu VI	Montagu Private Equity	Buyout	3.0
IK IX	IK Investment Partners	Buyout	2.5
Pantheon Global Secondary Fund VI	Pantheon Ventures	Secondaries	1.7
CVC Growth Partners II	CVC Capital Partners	Buyout	1.3
Oakley Capital Private Equity IV	Oakley Capital	Buyout	1.2
Trilantic Capital Partners VI Europe	Trilantic Capital Partners	Buyout	1.2
21 Aberdeen Standard Investments	21 Invest - France	Buyout	1.0

Source: *Unquote Data*

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