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Strategic growth for asset managers and single investor products

JOHN M. CACCIA

SKADDEN, ARPS, SLATE, MEAGHER & FLOM LLP

Since 2010, around $128bn has been raised by asset managers using private single investor structures, such as separately managed accounts or funds-of-one. This significant figure rivals – and for some asset managers, may exceed – capital raised in commingled private fund products.

These single investor products (SIPs) can take many legal forms. But at their core, they bring together a single investor and a single asset manager in a negotiated transaction. As a private, bilateral deal, an SIP can offer parties mutually advantageous opportunities that are elusive in commingled fund transactions.

This article focuses on one set of those opportunities for asset managers – opportunities for strategic growth and a deeper, stronger relationship with an important investor that can, in turn, be advantageous in commingled fundraising. The simple, 'low tech' nature of SIPs stands in contrast to the strategic results they can secure for managers when they are thoughtfully deployed.

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John M. Caccia is a partner at Skadden, Arps, Slate, Meagher & Flom LLP. He can be contacted on +1 (212) 735 7826 or by email: john.caccia@skadden.com.

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An evolving role for SIPs

During the financial crisis of 2008-09, SIPs played a critical role in fundraising at a time when not all limited partners enjoyed liquidity. Investors with liquidity in the depths of the crisis deployed billions of dollars through SIPs into a wide range of core hedge and private equity strategies offered by leading managers. These transactions bridged a testing fundraising environment, and the challenges for commingled vehicles during the crisis helped highlight the comparative merits of SIPs for both investors and managers. Investors were also reminded that certain problems come from other investors, and there are simple ways to protect against those risks.

SIPs not only survived the conclusion of the financial crisis, they thrived. Today, they still play a critical role in a broad range of the strategies of leading managers – but they are also used by many more types of managers, and for an even broader range of strategies. Setting aside legal requirements for disclosure of SIPs, information about SIP terms can be under-reported when compared to large, pooled funds, which may appeal to investors and managers alike.

Managers and their largest, most liquid investors are typically highly cognisant of the tensions that SIPs may have with the managers of commingled funds at a business and legal level, including conflicts of interests. At the same time, SIPs and commingled funds sit alongside within many manager platforms, and not just for co-investment or 'overage' opportunities. It is not uncommon for larger investors to be both an SIP investor and also a limited partner in the same manager's commingled fund. This pattern reflects the important, distinct commercial objectives served by SIPs.

Negotiations and SIPs

Managers and investors tend to approach SIP negotiations distinctly. There are three special dynamics in these negotiations that point to some of the key opportunities offered by SIPs.

First, large investors seek terms that duly reflect their ability to make very large commitments. These terms include breaks on fees, priority access to co-investments and other opportunities, and a range of other softer benefits such as enhanced reporting. Managers generally see, on balance, a potential win-win despite such requests on terms as long as fees are not driven too low and an SIP structure for a large investor sits comfortably with other products. What is 'comfortable' will depend on many factors, not least of which is the 'most favoured nations' protections that investors have agreed to with the manager to provide the investor with the benefit of certain terms offered to other investors.

In addition, many leading investors are increasingly expressing a desire to do more direct or 'hands-on' investing, where they view the manager as more akin to a joint venture partner. This desire requires governance structures and levels of investor control that do not always work well outside the SIP context but can work well in an SIP.

Finally, the largest investors typically have the greatest interaction with managers over the years. They often have a well-developed sense of what investment opportunities managers hear about or consider that are not strictly within the investment guidelines of the manager's existing products. Those larger investors may be tough negotiators – but they are also among the least likely to default or cause issues for managers of other kinds. That extensive interaction and history, including transaction history on discretionary co-investment, can serve to generate trust and also instil in investors a desire to expand their working relationship with a manager opportunistically.

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SIPs and strategic growth for asset managers

These dynamics illuminate some key alignments of interests between managers and their largest investors that make SIPs important.

By offering SIPs to larger, liquid investors, managers can clearly communicate back to them the special value brought to the table by those investors (while avoiding the risks of marketing to other limited partners who are not in a position to commit). The process can also be curative of some of the frustrations that the largest investors may experience in negotiating and participating in broadly held private funds, by offering truly bespoke arrangements such as the ability to do larger deals that would not be achievable without quick, responsive capital.

Many of the best managers cannot take advantage of a fair number of great opportunities because the opportunities are simply outside the manager's core mandate. The largest investors, whether as members of advisory bodies and similar committees, through diligence and reporting, or even ordinary, periodic interaction, can learn about these opportunities and be well positioned to recognise the value of a neglected 'core-adjacent' opportunity stream. As large investors, they are also likely to have broadly diversified investment mandates of their own. SIPs can produce a win-win in those circumstances, and help managers with a relatively low risk, strategy expansion platform.

Finally, some of the most sophisticated and active investors increasingly regard themselves as focused on direct deals and like more hands-on, active roles, including some discretion on investment decisions. These objectives can be hard to square in a commingled fund context with the needs of other smaller investors who do not look at themselves – or the deals – the same way. SIPs can provide managers with substantial committed capital from investors who might otherwise pass on a strategy of a manager due to the terms of the commingled fund arrangements.

SIPs have become critical to preserving and enhancing the relationships of established managers with their largest investors. Their utility in securing strategic growth is an equally important role served by SIPs for established and growing managers alike. ■