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Creating diversity and change in private capital markets

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Private capital might be predicted to outperform public investment in the next 10 years, but the current environment is not without its challenges. Higher interest rates, lower distributions and uncertainty in pricing have all contributed to the current slowdown.

So, where are the opportunities, how can private equity service providers support investors, and how can the private equity sector become more gender inclusive? These were some of the key questions at this year's Women in Private Markets Summit, which was attended by Investment Funds partner Sophie Reguengo and managing associate Amy Garrod, from Ogier's Corporate team in Jersey. Here are their key takeaways from the event.

Diversity, equity and inclusion

There is investor activism for gender equity, and without diversity, you risk losing out on investors and opportunities.

It's vital to harness the best talent to seek out the best opportunities. This requires open mindedness and commitment from the top down and supportive policies to attract talent and improve retention.

It's important to be the change, create an inclusive environment that allows every voice to be heard. If we want to achieve gender equality, we need to continue to stretch ourselves. If you've never felt like an imposter, then you're not stretching enough.

Private capital and real estate

There is more scrutiny on development finance, with higher build costs and higher debt costs. This is making it harder to stack up a deal. There is also difficulty getting performance bonds given number of contractors who have gone under. That said, there are still opportunities.

Anything with a bed has done quite well, such as hotels and student accommodation. Office space has struggled the most. If the market is cyclical, this should come back, or there could be lower demand in the long term – there's no way to predict. People are going back to the office but the challenges are obsolescence (market research suggests people spend on average 3.1 days in the office versus home working) and ESG.

We're seeing the 'greenification' of real estate. Most buildings are not up to standard and real estate needs to be modernised - and we need private capital to get that transition going. It is still an area where emissions are a problem and policy is critical in UK. The minimum efficiency standards are not sufficient.

Investors are increasingly focused on ESG. In order to safeguard returns/exit values, real estate really has to decarbonise. ESG risk is often priced into lending/investment.

In terms of residential investment in UK and Europe, the UK is being slow to deploy at scale, thereby losing out to more straightforward processes in Europe.

Fund raising

Until 2022, funds were being raised faster and closing quickly as LPs were keen to reinvest their high returns – but in the last 12-18 months, fundraising has slowed to a near standstill.

Fund raising is taking two years for middle market funds. Add to this increased regulation from the US Securities and Exchange Commission, requiring enhanced levels of compliance, and we will likely see higher costs being passed onto LPs. Therefore, more consolidation could be on the cards.

However, this doesn't suit entrepreneurial smaller GPs and being independent means you are better able to remain nimble and deploy capital when there's a good investment to be snapped up.

Are we seeing a return to old school private equity, where you can't rely on leverage as the main form of value creation? The emphasis is now on being an active owner and a focus on value creation, digitalisation, attracting/retaining talent and the importance of good management.

Good relationships with investors are key in difficult times, as investors tend to go back to what and who they know.

Investors also want more data – they are more data savvy and financial services providers need to have this technical knowledge and information on hand.

Deal financing

Despite the challenges, there is still opportunity and appetite to finance good projects. However, rates need to come down and investors need to be confident that will happen. Rates will likely stay elevated for a while but by the end of 2024, activity should pick up again.

Banks are not really looking to foreclose but may soon put more pressure on sponsors which will generate more deal flow.

While it's very hard to get banks to lend on high LTV, there is more flexibility from alternative lenders and financing can move more quickly.

Deal timelines

If the pricing is attractive, the deals happen quickly. But if a vendor does not have a liquidity requirement, the deals are slow. Also, if you need debt, bank processes are slow because of due diligence and ESG requirements etc.

There is less pressure from buyers to close a transaction, and less need to deploy capital. Buyers are much more willing to step back, which leads to longer processes.

Once the spread between buyer/seller positions starts to re-align, we should see transaction volumes pick up. Year-end valuations may help.

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