Investec

OUT OF THE ORDINARY

Making the call: How often do private funds request investor capital?

The evolution of private capital subscription facilities from 2011 to 2021

Subscription credit facilities, which came into sporadic use more than two decades ago, have become very widespread across private capital funds, particularly in private equity.

One of the key benefits for private capital funds of a subscription credit facility, which is secured against the undrawn commitments of investors, is to bridge the time between when an investment is made and the capital is received from investors. The more a fund needs to call on its investors for capital, the better it is to use a credit facility, as a larger bridge can be created and operationally burdensome capital calls can be avoided.

So how often do general partners (GPs) typically call on limited partners (LPs)? By engaging with GPs on this topic, we realised they often did not have an answer to this question, and, if they did, the answers varied widely from one GP to another.

However, looking back through the 10 years' worth of data we have collected from GPs across the private equity, infrastructure and real estate sectors, through fund reporting and financial statements, we realised we could answer the question ourselves.

In this research, we therefore set out to understand:

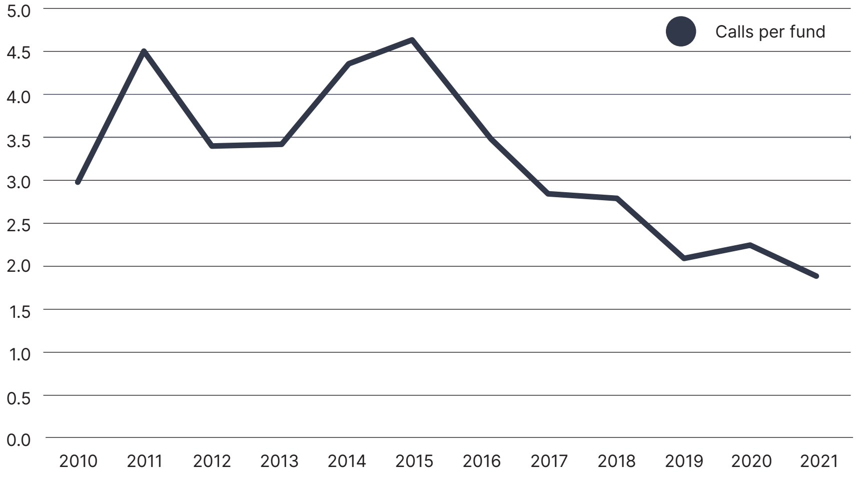
1. How many times does a GP typically call on its LPs per year?
2. How has this rate changed, if at all, between 2011 and 2021 – and why?

A turning point

So how many times per year do GPs tend to call on their LPs? And has this rate changed over time? Looking at the data, two opposing trends are immediately noticeable.

The first trend is that, in the years 2011 to 2015, there was variability in the number of capital calls made each year, with the number both increasing and decreasing during the period.

The second trend tells a different story. After peaking in 2015, the capital call rate fell consistently between 2016 and 2021. As we show in this report, there are a number of possible reasons for this.



	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Calls per fund	3.0	4.5	3.4	3.4	4.4	4.6	3.6	2.9	2.8	2.1	2.3	1.9

Methodology

45 private capital funds

From **€150m** to **€3.75bn** in size

29 GPs, from middle market managers

73% private equity; **13.3%** secondary; **6.7%** real estate; **6%** other

51% European; **47%** UK; **2%** US

2008-2021 fund vintages

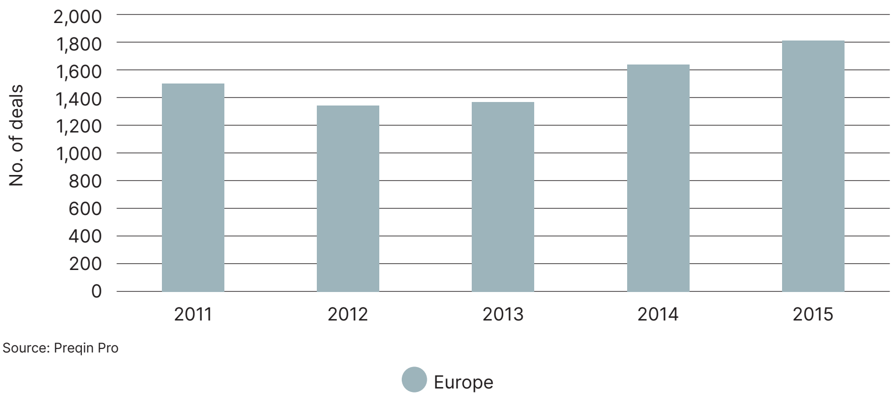
Not all funds had a subscription facility

Going with the flow

	2011	2012	2013	2014	2015
Number of Capital Calls per Fund	4.5	3.4	3.4	4.4	4.6
Increase/Decrease	50.00%	-24.44%	0.84%	27.60%	5.97%

From 2011 to 2015, the number of capital calls varied from year to year – reaching a trough of 3.4 in 2012 and peaking at 4.6 in 2015. We found these oscillations were mirroring investment activity as reported by Preqin over the same time period, demonstrating a clear positive correlation between investment activity and number of capital calls.

NUMBER OF PRIVATE EQUITY-BACKED DEALS BY REGION, 2011 - 2015



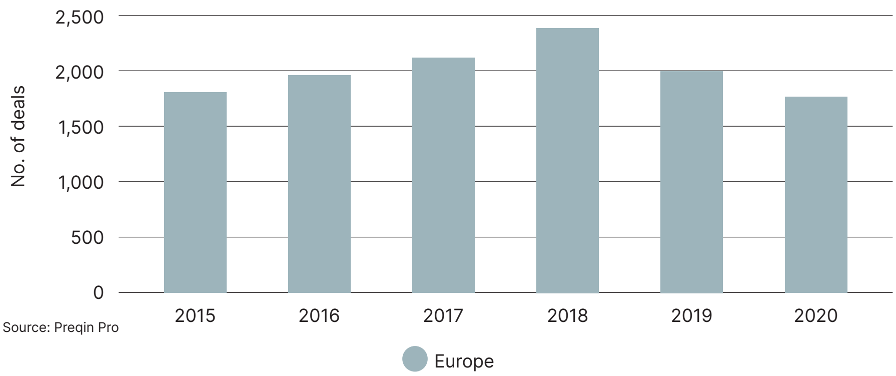
Source: Preqin Pro

The new normal

	2015	2016	2017	2018	2019	2020	2021*
Number of Capital Calls per Fund	4.6	3.6	2.9	2.8	2.1	2.3	1.9
Increase/Decrease	5.97%	-22.61%	-20.37%	-2.78%	-24.00%	6.58%	-15.67%

*data as of 30-June-2021, annualized

NUMBER OF PRIVATE EQUITY-BACKED DEALS BY REGION, 2015 - 2020



Source: Preqin Pro

Despite only having six months of data for 2021, we have annualised the data as it looks like the number of capital calls will not increase further – falling below two per year for the first time. This can be explained by the fact that facilities with a typical borrowing tenor of nine to 12 months, which were largely drawn down in the second and third quarter of 2020, naturally saw a lower call rate in early 2021. Most funds we spoke to directly elected to refinance existing facilities during the second and third quarter of 2021 with a view to making a call in early 2022.

Since 2015 the average number of calls made per year more than halved from 4.5 per year to under 2 times despite relatively plateaued investment activity during the time period (which saw increased activity between 2015-2018 and a reduction between 2019-2020). After falling by more than 20% in two consecutive years and remaining between two and three for four years in a row, the average capital call rate started to level out around two.

The downward trend was slightly reversed in 2020, when the global pandemic saw funds with spare capital calling on LPs to support existing portfolio companies. However, we were surprised at how small the relative increase was –only 6.6%. We estimate that the increase was due to the impact of Covid, and funds with already-maxed facilities calling on their investors.

Unbounded growth

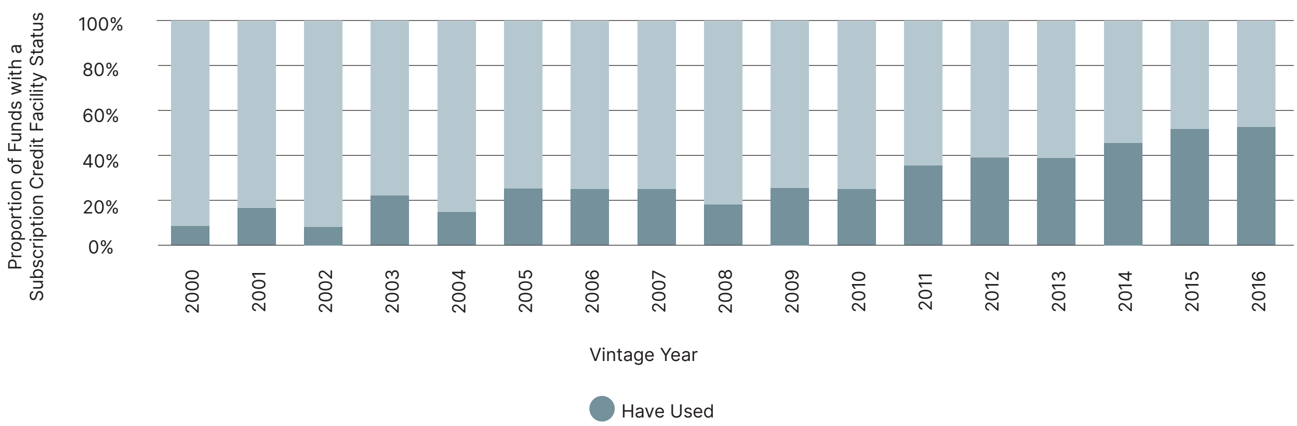
Over the last 20 years, the adoption of subscription facilities among private capital funds has increased almost 20-fold. In 2000, Preqin data shows an adoption rate of 8.7%, with only four out of 42 funds using subscription facilities. The latest data in 2016 shows 87 funds with facilities in place, against 76 without – a 53.4% adoption rate.

Our own data from 2016-2021 supports the theory that adoption levels are still growing. Over the course of the pandemic, we saw utilisation levels climb as high as 75-100%, and this is further supported by the entry of specific fund finance advisors, recruiters and service providers into the market, which is now estimated to be worth over $500bn.

The increased adoption rate of subscription facilities is almost entirely responsible for the dramatic decrease in the number of capital calls over the last decade. As these facilities have become widespread, their terms have also become more advantageous.

We have collected data that shows borrowing provisions for Limited Partnership Agreements (LPAs) are becoming more open in terms of increased borrowing capacity as a percentage of committed capital. In addition, subscription lines are being held out for longer and longer, and borrowing tenors are now extending beyond the traditional 12 month restrictions, peaking at 18 months. Borrowing capacity is also increasing up to 35% of total fund commitments from a historic limit of 20-25%, illustrating the wide use of these facilities.

FIG. 2: PRIVATE CAPITAL FUNDS USING SUBSCRIPTION CREDIT FACILITIES



Calculated credit

With funds reaching record sizes over recent years, this has also contributed to reducing the number of capital calls per fund per year. The larger the fund, the greater the operational burden to make frequent capital calls. Instead, it is much more efficient for large funds to consolidate capital calls into one or two a year. Therefore, funds and Chief Financial Officers (CFOs) are becoming more disciplined and strategic in their approach to calling capital.

Like a virtuous circle, the mainstream adoption of subscription facilities has also increased the level of understanding around this form of financing. CFOs and GPs using facilities as administrative tools can now forward future capital calls well in advance, which allows for smoother operations and better investor relations dynamics between the funds and their LPs.

While typically more of an operational tool, subscription facilities serve to bridge not only fund equity but also underlying asset debt packages and co-investors. In so doing, this reduces the pressure on deal teams to arrange syndication or debt before an acquisition and allows them to negotiate better terms.

Where next?

The fund finance market has experienced significant innovation and growth over the last five years. We have witnessed a proliferation of financing solutions at the fund level, including NAV facilities, secondary facilities and GP-led continuation vehicles, alongside the explosion of GP co-investment facilities.

While the subscription finance market is well established, we expect to see still further growth in this space. For newly raised funds, the adoption rate for these facilities will remain high, around 80-90%. We also anticipate additional developments within off-balance sheet financing, securitisations and the use of institutional capital.

Although there has been a strong downtrend in the number of capital calls over the last decade, we still believe there is a floor to the number of calls a fund makes every year. We broadly expect funds to call on their investors at least once a year, but do not expect this to rise above two times per year, given the professionalisation of GP operational functions and the widespread adoption of subscription credit facilities within the private capital space.

The Investec MFA is designed with this in mind, and we are able to structure solutions that can be tailored to a fund's specific needs, whether single or multiple capital calls per year.

Investec MFA solution

At Investec Fund Solutions, we provide master frameworks with either a fully uncommitted facility or a combination of committed and uncommitted facilities, which allow borrowers and GPs to minimise the number of capital calls they make during a year.

For GPs who like to make regular quarterly or semi-annual capital calls, we can tailor the borrowing terms to allow for a single capital call to repay drawings. Our facilities can also be set up to enable a single annual capital call.

Additional features:

- Facility size linked directly to fund borrowing capacity
- No clean down requirement (unless required by the fund LPA)
- Reduced upfront fees on short tenor maturities and no drag costs on commitment fees for facilities sitting under our uncommitted framework
- Ability to take out LCs, guarantees, revolving facilities and term loans with the ability to make multiple tranches available consecutively
- Ability to bridge management fees, expenses and investments
- SPV level borrowing, with investment specific drawdowns a well-used feature
- Ability to collateralise hedging under the facility with no cash collateral
- MFA term directly linked to the fund's investment period, requiring fewer overall renewals at the framework level. Also allows for post-investment period lending
- Ability to bridge co-investors and underlying debt financing, increasing flexibility and, combined with short tenor maturities, saving on upfront fees and drag costs


QUIETWAY
Q11
Southwark Bridge
3 mins

For more information, get in touch

Helen Griffiths
helen.griffiths@investec.com
+44 (0)207 597 3791

Oliver Bartholomew
oliver.bartholomew@investec.com
+44 (0)20 7597 5333

Michael Slane
michael.slane@investec.com
+44 (0)207 597 3684

Marilia Shewchenko
marilia.shewchenko@investec.com
+44 (0)20 7597 5131