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Opportunities to Meet Fundraising Goals - Kevin O'Connor, Director, Markit

Preqin's Funds in Market data shows that a third of private equity vehicles failed to reach their fundraising goals in the first quarter of 2014. This is despite a backdrop of buoyant industry fundraising levels which saw a 19% increase from the corresponding Q1 2013 figures on the aggregate amount of capital secured. Given the challenges GPs face in market, Markit recognise the need for private equity and illiquid debt funds to differentiate themselves and alleviate investor concerns.

After a dire few years that witnessed the severe economic downturn, which was sharply followed by increased regulatory burden, Europe's private equity industry is now emerging into a much-improved environment amid heightened investor and political awareness.

The good news is that investor appetite appears to be returning. According to Preqin's data, the first quarter of 2014 saw 199 private equity vehicles reach a final close, raising an aggregate $102bn – equivalent to a 19% increase on the amount of capital raised during the same period in 2013. Of the 199 funds that closed, 51% closed above target and 16% met their fundraising goal.

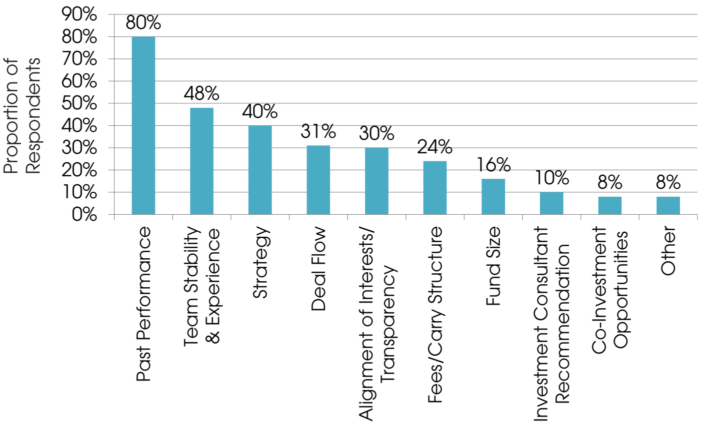
Using the Preqin survey results from the Investor Outlook: Private Equity, H1 2014 report as a basis, we review what investors are really looking for when making allocation decisions, and what differentiates successful fundraising from those that fell short of their goal.

It's no surprise that past performance, and team stability and experience rank highly among factors that LPs consider when looking for a GP (Fig. 1), but private equity funds also need to consider the value and emphasis investors evidently place on regulation, reporting and transparency. In Markit's experience, sophisticated investors are looking for access to market risk, through quality and trusted managers with interesting strategies. However, they are also simultaneously seeking to eliminate exposure to operational risk, e.g. regulatory risk, valuation risk, fraud risk etc.

This presents an opportunity for the 33% of funds that fell short of their fundraising goal to differentiate themselves in the eyes of investors.

The Alternative Investment Fund Managers Directive (AIFMD) has certainly heightened investors' sensitivity to a broad range of topics, such as the safeguarding of assets, valuation risk, transparency

Fig. 1: Key Factors Investors Assess When Looking for a Private Equity Manager



Source: Preqin Investor Outlook: Private Equity, H1 2014

and communication. With a review date due in 2017, it is set to remain one of the most pressing issues for the European private equity and venture capital industry. But, the risk is a perception by the European political class that the private equity industry is not embracing the spirit of the AIFMD, particularly around the areas of independent valuations, transparency and reporting. This could lead to more prescriptive or draconian legislation.

Another regulatory focus is regulation aimed directly at institutional investors, such as Solvency II, the pension funds directive, IORPD, and the transposition of Basel III in Europe. We are already beginning to see this bite. Ten percent of investors in private equity that responded to the Preqin survey said they will reduce their investment in private equity over the course of 2014. The majority of these are insurance companies and banks that are concerned about private equity's failure to address Solvency II and Basel III transparency and prudential valuation requirements.

In the increasingly complex surrounding environment, funds will need to work with their service providers in order to create a comprehensive reporting solution, which meets end investor requirements. The good news for funds is that this is completely within their control, but there is a strong need to allocate resource and management time to it.

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