



FUND FINANCE FRIDAY

Polishing Up the Crystal Ball

December 16, 2022 | Issue No. 204

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2023 European Fund Finance Market Predictions

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It's that time of year again when conversations are dominated by reflections on our market's performance over the last 12 months and expectations as to what 2023 will hold for our industry.

After a record-breaking 2021, 2022 started with similar levels of activity but was quickly impacted by macro-economic and political turmoil, interest rate hikes and lenders feeling the squeeze after years of deploying huge amounts of capital to find finance. Couple that with a slowdown in fund-raising, a fall in M&A and declines in valuations, and we had a number of factors at play which should have resulted in a significant slow-down in activity in 2022.

It's a testament to the diversity of our industry – both from a product and provider perspective – that most players in our industry on the legal and business side will likely finish the year up on 2021. However, the mood is understandably cautious for next year. As interest rates reach the market implied terminal rates and inflation starts to show signs of tapering, the focus for 2023 will very much be on the extent to which these monetary policies have impacted the global economies, as a recession in multiple regions loom.

Given the above, “liquidity” is likely to continue to be at the forefront of conversations, whether it be for Managers as beneficiaries requiring cash for struggling portfolios and/or for their LP's with cash is tied up for longer in a benign divestment environment, or for the benefactors, with lenders, many of whom are scaling back balance sheets and becoming more selective with capital deployment as provisions start to ramp up and sector limits are hit. One thing is for certain, the Fund Finance industry has seen and will continue to see more growth and innovation than any other asset class.

On that note we again reached out to the industry for their reflections on 2022 and what lies in store for us in 2023.

A huge thank you to all of those across the European markets who contributed their thoughts to this issue and to all of our clients for their continued support this year.^[1] We hope you enjoy the responses below and manage to have a very well deserved rest over the holidays!

Stephen Quinn, 17Capital: 2023 will see another challenging year in terms of liquidity for the private equity industry – the macro events of 2022 will not dissipate quickly. This ‘liquidity crunch’ is quite circular in practice – a tougher exit environment for portfolio companies means lower distributions for LPs and GPs who are both looking carefully at managing their future commitments to new funds and strategies. We have seen areas of the debt markets contract significantly in 2022 which may offer opportunity for the fund finance industry if the right sources of capital and risk appetite are in place.

Shelley Morrison, Aberdeen: Building on a major trend from 2022 we predict that alternative, non-bank lenders will accelerate growth of their market share. Institutional capital will continue to partner with banks to support them in managing counterparty limits and balance sheet constraints whilst forward-looking sponsors will seek to establish long term relationships with non-bank lenders to ensure access to liquidity. Challenging macro-economic conditions have already had an impact on fundraising timetables. As new lenders enter this market and established lenders become increasingly selective about the deployment of their capital, we forecast an increase in the issuance of bespoke and innovative facility structures across both sub-lines and asset-backed fund finance. In 2023 we anticipate funds will take longer to close and expect this to drive increased demand for flexibility - smaller ‘first close’ facilities, accordions and margin/covenant ratchets.

Ahlem Ben Gueblia, ANZ: Despite the uncertainty, volatility and slowdown in fundraising, we believe 2023 will be a strong year. Our clients are rapidly adapting to the current environment and fund financing remains a key tool to their liquidity management. Lenders’ product offerings are under continuous review to tailor to the needs of the sponsors and next year should accelerate the development of new products even further, with the rise of NAV facilities at the forefront. Lastly, 2023 will reinforce sustainability as a key priority in our activity. Sustainability Linked loans will increasingly constitute the vast majority of financings in Europe, seeing lenders working closely with sponsors to support their sustainability agenda and help them transition to a net zero carbon future.

Guillaume Leredde, Avardi Partners: 2023 will be an interesting year for the fund finance market. With the increasing rate environment, changes in balance sheet capital treatment for banks and the rise of non-bank lenders, the purpose and type of fund finance facilities used by fund managers are evolving. We are working on creative ways to optimise financing for our clients and the demand for bespoke solutions is increasing. The main challenge for 2023 will be the lenders’ capacity to satisfy the market demand.

Olawale Ajayi, Bank of China London branch: We expect NAV financing to remain a hot topic in fund finance in 2023 as more banks are beginning to have appetite for the product. Due to the uncertain economic environment, some banks may delay their entry into this space and will prefer to experiment with hybrids. Deal activity across the traditional sublines to remain robust in 2023 despite increasing interest rates.

Wikash Bhagwanbali, Bank of Ireland: Despite the wider market volatility, 2022 was a busy year. For 2023, we expect demand for subscription lines to continue, although banks’ increased

capital requirements will put upward pressure on pricing. Coupled with rising interest rates, it will be interesting to see if there will be any behavioural changes in the usage of subscription lines. Some managers are likely to opt holding assets for longer, or selling to their next generation funds or continuation vehicles, as they see value upside not currently recognised in the market. This in turn should support further demand for hybrid and NAV solutions as a means to free up liquidity. On the LP side, higher interest rates and pressure on public market valuations will impact portfolio allocations. As a result, we expect to see an increase in secondary sales, benefiting secondaries funds who will look to take advantage of likely discounted sales opportunities.

Sabih Hussain, Barings: The European fund finance market will continue to see a strong demand from GPs into 2023 for capital calls and fund leverage. Like the US, European private investment markets are becoming reliant on the use of leverage to fuel the growth of direct lending. With some lenders at capacity, the supply will have to be met by new entrants and non-bank institutions. Non-bank lenders are not just replacing bank capital, they are more flexible in their terms as well. The European markets lack some of the products that the US markets benefit from, such as public perpetual vehicles and mid-market CLOs.

Tom Glover, BC Partners: We expect that 2023 will bring an increasingly challenging macroeconomic and geo-political environment and are well prepared for that. Further liquidity pressures across the private equity sector will likely manifest themselves in various ways such as even fewer investment exits, more challenging asset-level financings and extended fundraising cycles. Within these challenges, there are always opportunities. Partnering with nimble and capable GPs, we expect to creatively deploy larger amounts of capital in 2023, enabling our clients to capture the compelling strategic and asset level opportunities that present themselves at this stage of the cycle.

Guillaume Hartog, BNP Paribas: It's fair to say that the fund finance market didn't suffer very much from the COVID crisis with retrospect, and when affected, recovered quickly. Fund raising, fund size on various strategies as well as facility terms and pricing quickly went back to pre-crisis level or almost. This was a testimony to the robustness of this market and its players. I hope I can say the same in a couple of years after the current slowdown following the war in Ukraine which sparked global market turmoil comprised of inflation issues, asset value rebasing and possible – whether long or deep or technical – recession-like situations both in the U.S. and EMEA, with the consequential massive rate increase. But this time it could well be different - we don't know how long the challenging global macro environment may last. 2022 has been a transition year, and the global macro and geopolitical situation will continue to impact the fund finance market in 2023. Fund raising processes have and will continue to slow down. LPs will be more selective. Facility terms will tighten after years and years of relaxing. Pricing will continue to increase on the back of the surge of liquidity costs for banks. Additionally, many banks are suffering from capital constraints or are more proactive in capital management (in anticipation of Basel IV for instance, when applicable) leading to less liquidity available from the bank market. But as an essential part of the business model for financial sponsors and the fact that fund financing technologies have proved to be a powerful and flexible tool, there will still be a volume of financings. For the main banks in this space, because of the amount of balance sheet at stake, this should shift toward a more relationship driven business. So for deals well structured and well priced, and with the appropriate syndicate of banks which can play the relationship and through the cycle, there will still be a market and a great deal of financing. If

the fundamentals of the fund finance market are maintained (credit worthiness of LPs, decent overcollateralization, cross solidarity amongst LPs, comprehensive security package, recourse to LPs or assets) the risk profile should remain strong. We could see perhaps shorter tenor to manage cost of funding (compensated with extension options). On a more positive note, we see the secondary NAV facility market growing materially as LPs seek liquidity options. The nascent concentrated NAV facility market (or PE NAV), after a promising start in 2021 and 2022, will continue to develop for the big asset managers but on a more selective basis. Capital regulation and Basel IV will have an impact on the overall shape of the fund finance market but the market is likely to evolve to provide more flexibility to GP's to manage balance-sheet post closing (secondary trades, securitization, public ratings to continue, fronting on behalf of non-bank lenders or insurance companies). For 2023 and beyond, we expect to see a wider use of institutional capital in the market and the development of a syndication market. We expect also that GP financing and LP financing will continue to build across the market. Another transition year but with still business to do and financing resources available for the most agile sponsors.

Rory Smith, Brickfield: *Market conditions in 2023 are looking much less certain than 2022, and as a result we expect fund finance recruitment to be more focused on lenders and law firms alike seeking out innovators and rainmakers, especially on the buy side, who can get the deals done in a more cautious lending market where syndication will become more difficult for capital calls. Second tier funds, for example, will find relationship builders with strong networks particularly valuable. We also expect to see continued lateral moves, although there has very much been a trend recently towards hiring managers having to go that extra mile to get whom they need. The wage spike experienced in 2022 has now largely stabilized so compensation is not the key issue it was a year ago, but candidates on the market are out for positions that have a distinct positive upside, and that now makes it more important than ever to offer the right conditions and strike the right deal.*

Lyn Underwood and Richard Braham, Commonwealth Bank of Australia: *The demand for subscription lines will continue to make up the core portion of the fund market, albeit NAV's and Hybrid facilities will continue to grow as clients continue to seek financing solutions to match the life cycle stage of the fund. ESG linked facilities will remain a key focus in the market, as GP's and LP's awareness around ESG investing/linked facilities increase. In 2022 the fund market saw some lenders refocus their strategies and/or reduce exposures to the sector. Given rising interest rates and the focus on liquidity management, we expect lenders to continue to demonstrate discipline on the deployment of capital for key client names, whereby the relationship can be deepened via a multi-product offering. Despite the current market conditions, we also expect fund raising to remain strong for the top-tier GP names in 2023, as we saw in 2022, the size of funds being raised were getting larger and larger, and often superseding the prior fund capital raising. 2023 is expected to be another busy year for fund financing! It will be interesting to see the pace of M&A given the volatility of asset valuations but we do expect the current environment to bring opportunities to those who are creating strategies to take advantage.*

Michael Peterson and Shiraz Allidina, Citco Capital Solutions: *The more things change, the more they stay the same. Changes for next year will include a significant slowdown in fund raising for mid-tier and bottom-tier managers. There will be another record-breaking year of NAV origination, as borrowers and LPs become more comfortable with the product. What will stay the same: committed, prudent players in the fund finance market will thrive and prosper.*

Amit Mahajan, Crestline: *This year proved to be an exciting and pivotal time for the Crestline Fund Liquidity Solutions team. After COVID threatened the growth trajectory of countless companies, we developed a unique financing solution that was capable of helping dozens of PE-backed portfolio companies weather one of the most volatile markets in modern history. As the threat of COVID continued to subside, we were grappling with a flood of macroeconomic challenges that forced another wave of uncertainty into the market. The combination of these near-term challenges created an environment in which (a) mature funds in need of more dry powder to support companies for longer term hold as exits are delayed or halted, (b) LP's also looking for liquidity to fund capital calls as they suddenly see their other buckets in Fixed Income and Equities decline in value, and (c) refinancing of existing loans are challenging since new lenders either have stepped away or reduced the size of their loans. As a result, our team was able to leverage its collective decades of investing expertise to increase deal volume and establish a pipeline of actionable deals, many times that of what we saw during Covid. Overall, we expect the NAV loan market to continue experiencing steady growth and volumes to increase throughout 2023.*

Jamie Mehmood, Deloitte: *Whilst the start of a new year may bring a degree of relief against the volatility we have seen in recent months, longer-term indicators suggest that 2023 may follow a similar path. A driving force that has shaped the market this year has been fundraising, which we anticipate is likely to remain challenging given the broader backdrop, with limited investor allocations driving a continued flight to quality and track record. The slowing of distributions from funds has been a big (though not the only) driver of tighter LP liquidity, which in turn is likely to give rise to more continuation fund structures and/or NAV solutions as a means of returning capital to LPs. We are also expecting that macro conditions and the stress that this creates for portfolio companies is likely to drive a continued acceleration in the adoption of NAV within private equity, with direct lenders continuing to gain a strong foothold in this market, made all the more attractive by the shape of the SONIA forward curve in 2023 and borrowers seeking increased flexibility. Whilst there may be some respite in the new year with new allocations and fresh budgets, liquidity within the subscription line space is expected to continue to show an enhanced degree of selectiveness and focus on existing relationships, albeit this is something that we expect to ease as the year progresses.*

James Newns, James Nash, Marco Unti and Amrita Maini, Deutsche Bank: *The changing macro environment that we have seen impact the global financial system in the second half of 2022 has created a perfect environment for the continued growth of structured fund financing, whether this is through NAV Facilities or other bespoke fund level products. Helping to provide liquidity solutions to LPs, support portfolio level borrowing or bridge slower fund raising are all areas where fund level financing will be key in aiding private capital managers to navigate the uncertainty of the coming year. As such, we expect the rapid growth in NAV based financing seen this year to continue and perhaps quicken in 2023 as more GPs access this broad product toolkit. We expect Subscription Line financing to continue to be a foundation of the market in 2023 in volume terms, although the pace of growth will flatten reflecting a slower rate of underlying fund raising. Deutsche Bank sees fund financing in its various forms as a core focus area for the coming year reflecting the growth in the sector and the ability it offers to provide meaningful strategic support to our sponsor clients during difficult times.*

Jack Dutton, Ernst & Young LLP: *We expect that in the first half of 2023 we will start to see the impact of recent uncertainty (such as cost of living pressures and interest rate dynamics),*

most notably with an increase in distressed assets within portfolios. As a result, there will be more pressure on both asset-level and fund-level financing structures, as performance and financial covenants get closer to their test limits. With this in mind, for loans approaching maturity, it may be difficult to simply refinance with the same counterparty, which will present opportunities for alternative credit providers. We expect to therefore see a further rise in private debt lending, not only at asset-level but also at fund-level. Finally, we believe that the assessment of sustainability and ESG factors will become increasingly well-defined, as a number of debt providers work with external organisations to refine their own internal frameworks. This will translate to better qualitative and quantitative analysis, allowing for more dynamic loan pricing frameworks.

Khizer Ahmed, Hedgewood Capital Partners: Like other parts of the financial services industry, the fund finance industry also finds itself dealing with the effects of tightening financial market conditions, a general slowdown in global economic activity and continued geo-political uncertainty. Borrowers and lenders are confronted with multiple challenges that will likely impact the nature and extent of their market activities, at least in the short term. A slowdown in fund raising across the private capital industry, a fall in asset realizations and exits, a potentially significant mark down in valuations, and the general increase in benchmark rates and spreads are likely to dampen borrower appetite. On the lender side, pre-existing capacity constraints amongst subscription line providers are likely to be compounded by risk driven considerations and a greater emphasis on servicing existing clients at the expense of acquiring new ones, thereby leading to a pronounced element of balance sheet rationing. NAV lenders are likely to raise the thresholds at which transactions make sense on a risk adjusted basis. This, combined with an increase in the opportunity cost of balance sheet usage, is likely to feed greater competition for a given pool of capital. However, despite these cyclical pressures, we remain very bullish on the medium to long term prospects for the industry. Certain underlying themes that have driven recent growth in the fund finance industry remain very much intact and will continue to provide tail-winds for secular growth in this industry. These themes include (i) the continued evolution of the subscription financing product, particularly with the growing emphasis on ESG considerations, (ii) the growing acceptance of fund level NAV and preferred equity solutions as flexible and multi-dimensional portfolio liquidity management tools, (iii) continued spillover from other parts of the lending universe e.g. use of risk sharing mechanisms amongst lenders and the growing interest in the use of CFO's as liquidity and fund raising tools, and (iv) the growing recognition of the use of fund level financing as a complement to the more traditional financing of individual portfolio level assets especially in the Private Equity industry.

Shankar Madkaikar, ICBC: We expect the next 12-18 months to be difficult for the PE space especially for small/mid-tier sponsors with limited track-record when it comes to fund raising and launching new funds with expected flight towards quality, large top-tier names and to sponsors with a record of delivering good performance in difficult market conditions. Additionally, we expect reasonable downward correction in portfolio valuations of most funds. That said we remain positive that the Private Equity space will show the same resilience it showed during the Global Pandemic!

Steve Burton, ICG: So... reflecting on my 2022 predictions I think I will give myself a slightly generous 7 out of 10; i) Market growth – yes well, initially, ii) ESG focus– so so as events took over, and iii) NAV - so so slow really), and my wish list slightly less successful ...pragmatic credit departments and easier KYC (to be fair some are trying...), along with simpler docs. Jury

is out on that. To 2023..... Fun times ahead....higher interest rates nudging fund hurdle rates and becoming a large cash cost, Regulators driving bank RWA introspection, non-banks developing their proposition, but even then, can supply meet demand because we will see demand? Will we be still talking about a Pivot? There will be continued bifurcation between larger and smaller sponsors' ability to secure commitments from credit providers: bigger will be better and relationships will become more critical than ever (good or bad for intermediaries? We will see). Pricing up for while at least, and inevitably more jobsworth credit functions. As rates continue to climb, LPs will become much more 'interested' in fund facilities again. If markets stabilise, ESG will be rightly back with vengeance and NAV will continue its inevitable, but slow, acceptance. Sponsors will also continue to build in house teams so dust those CVs off, and finally, England will not win the Rugby World Cup. Sadly, it's Ireland's to lose for me. Still got some growing up for us all to do.....best do it fast...

Ian Taylor, ING: We see the overall relationship lenders have with their sponsor clients to be an increasingly important factor in their decision process to deploy capital for both subscription and NAV finance. Against a challenging economic backdrop, investment strategies for new fund launches will be closely analysed and lenders will be monitoring the asset performance of borrowers within their existing portfolios. In terms of capacity, Fund Finance will continue to be an important sector for lenders, although we anticipate hold levels to be generally lower next year.

James Rock-Perring, Intertrust: Global events and hints of a recession in the short term have had an impact on the European Fund Financing market. For subscription line facilities the current climate has further exacerbated the need for more liquidity and banks will be more selective in 2023 re their allocations - expect this to be the case for both the large end of the market and mid-market. The increase in financing costs may impact how sponsors use these lines, however these facilities are well embedded from an operational standpoint i.e. working capital benefit vs the IRR benefit. For NAV financing the current environment is further fueling the market together with continued adoption by sponsors and an increase in the number of lenders entering the space. From an advisory standpoint as we move into 2023 there appears to be an increased need for the role of an advisor to source liquidity and to navigate the large number of new entrants in the NAV space.

Nicola Germano, Intesa Sanpaolo: We have seen a 2022 with two very distinct trends for the subscription finance market: a strong start in the first quarter of the year followed by a moderate slowdown in the second half, in part driven by a reduced pace in fund raising and higher costs of credit for funds and balance sheet constraints for bank lenders. We don't foresee an immediate come back in early 2023, while we forecast an increase in demand for more tailored financings like NAVs and GP solutions. 2023 might be the year of consolidation after a very long run for the fund finance market due to, inter alia, some participants still facing headwinds and continued macro environment uncertainty. We do expect ESG features to be almost mandatory and new innovative solutions for clients as a key factor of success.

Helen Griffiths and Oli Bartholomew, Investec: In a rising interest rate environment, we will see an increase in LP sales driven by the well-documented denominator effect. There will be a deceleration of utilisation of capital call lines; tighter fundraising will likely yield more concentrated LP bases which together with higher interest rates will put pressure on borrowing limits and advance rates. The slowdown in distributions and fundraising will likely mean

increased conversations around NAV financing, particularly dividend recapitalizations. We will continue to see growth in the secondaries space; both GP-Led continuation vehicles and LP portfolio sales. GP financing will remain a relationship driver and be essential for junior partners given the slow-down in distributions and exits from vintage funds.

Richard Crook, JP Morgan: Fund level financing demand continued to grow in 2022 against a backdrop of rising rates and a significant slowdown in the leveraged finance capital markets. NAV financing has firmly moved from a subject of interest to a real option for a much broader range of PE sponsors, particularly as the newer vintages of funds are set up with this flexibility in mind. Pricing for well diversified secured NAV facilities continues to be well inside of HY spreads so remains a viable alternative for providing liquidity at a portfolio level, either for distributions or to support continued asset level growth. We have also seen an increasing number of enquiries from family offices for financing on their PE portfolios. Continuation funds are also becoming a more mainstream alternative to traditional asset exits, and the hybrid-style financing which these structures lend themselves to are attractive compared to holdco debt, both from a pricing perspective but also with regards to covenant flexibility. There have been some major changes in the make-up of NAV financing providers in the last twelve months, with the exit or significant balance sheet reduction of certain large banks partially offset by the entry of newer participants in the banking and insurance space. We believe that the growth trend experienced in 2022 for demand in NAV and continuation fund financing will continue. The entry of new pools of capital into the space will likely be the primary driver of pricing unless there is a material increase in capital allocated by the existing bank providers.

Yvonne Coughlan, Marie-Alix Schindler and James Stevens, JP Morgan EMEA Funds Finance: 2022 has seen a year of significant change across financial markets. Rising interest rates together with the rising cost of debt brought into question sponsors' continued appetite for leverage. In the Fund Finance space, demand remains resilient. The total cost of subscription debt together with the operational ease of having a facility in place keeps the value proposition intact. In Q4, we have seen consolidation in the market with some banks exiting or reducing hold sizes. This has translated into greater focus on deal pricing and multi-year committed facilities. For JPM and banks still active in the space, this has led to opportunities to step up and support both existing and new clients. Over the next 12 months, we expect the themes from Q4 to continue.

Matthew Houlden, Lazard: For perhaps the first time in the recent history of the fund financing market, we are going into a new year with a more uncertain outlook for activity. On one hand, benchmark rates have risen in 2022, fundraising in some parts of the private markets has become more challenging, with a potential knock-on impact on the velocity of demand for subscription lines, and some lenders appear to be scaling back more generally on activity levels. On the other hand, liquidity seems to have become more important for many LPs and GPs, resulting in increasing levels of demand for NAV financing and preferred equity solutions as well as stapled financing alongside continuation funds. Putting these dynamics together, I believe the opportunity set for lenders willing to put meaningful amounts of capital to work in these segments of the market could still be significant in 2023.

Jill Wilson and Scott Turner, Lloyds Bank: We expect the economic and geopolitical headwinds to continue slowing fundraising into 2023 although ultimate demand will remain strong with the best GPs continuing to raise capital for proven strategies as investors seek to

lock in access to the next economic cycle. Demand for capital call products will therefore remain strong but we envisage this may outstrip supply as lenders gravitate towards their core relationships which may make it more challenging for some sponsors to fill their financing requirements. In this context we expect the drive to access and embed institutional capital in the mainstream fund finance market to continue at pace. Hold periods for assets are also likely to extend, augmented by a softer exit market with GPs focused on trying to maintain and grow earnings to support valuations in the context of weaker PE multiples. The need for liquidity solutions is therefore expected to increase on the back of this with lenders benefiting in terms of opportunity to deploy more structured fund finance including hybrids and NAV. We expect to see more established “capital call only” lenders dipping their toes into the structured market and more specialist new entrants emerging. Finally, sustainability linkage in fund finance will continue to grow in importance with GPs and lenders looking for applications across the spectrum.

Christopher Thalhammer and Alison Syré, Macquarie: In 2023, we foresee very strong activity in the secondaries space - both LP portfolios and GP led transactions which will give rise to a significant volume of opportunities in the secondaries space; we see a growing demand for NAV facilities driven by need to optimize overall capital structure and to support additional capital needs and non-core real estate funds looking to seek NAV financing to replace hard to obtain asset level debt.

Suraj Suri, Marlborough Partners: Following a very successful 2022, we expect to see robust growth in the fund finance market, with managers seeking more creative and bespoke solutions across capital call, NAV and GP financing mandates. Managers will look to NAV/hybrid facilities, with a particular focus on more concentrated portfolios, as a key tool to secure additional liquidity and boost returns as liquidity for asset level financing remains challenging. Furthermore, the increasing participation of non-bank lenders in fund finance transactions over the past year has been testament to the growth of institutional demand in the asset class and we anticipate a greater level of syndication and collaboration between banks and non-bank lenders.

Ben Griffiths, MUFG: We see a continuation of themes from the latter half of 2022 where we have seen a liquidity squeeze with numerous banks in all jurisdictions coming out of the market or pausing for thought given capital constraints. We believe banks with strong stable balance sheets will continue to allocate to the Fund Finance space to support current, and develop new, long term relationships across the broader alternatives market. Sponsors will have to continue to widen the net from their traditional lenders and if current trends continue will need to think about the sizing of subscription lines versus the capital raise. The last few years have been characterised by funds looking to maximise size of facility but as rates have blown out we have seen both lower requested sizes and moderation of borrowing levels across the book. We expect relative growth in the private credit, infrastructure and real estate space and continue to see high levels of Separately Managed Accounts alongside comingled funds all requiring credit.

Russell Evans and Kieran Welsh, National Australia Bank: We're expecting the economic slowdown to continue driving greater innovation across the product with managers seeking bespoke solutions that can provide liquidity to continuation vehicles and fully invested funds via asset recourse. We're expecting continued growth in demand driven by record fund raising in to Infrastructure and renewables focused funds, however we're expecting a modest slowdown

in demand for new fund finance facilities as our Private Capital clients take a more conservative approach to their use of more traditional finance solutions as interest rates continue to rise through 2023.

Hamid Aguerbal and Alexandra Robert, Natixis: *2022 demonstrated that banks are struggling to keep the pace and increase their lending capacity to meet the growing market demand on fund financing. Added to this is the regulatory scrutiny around capital call financings which has reduced bank offering. Looking into 2023, one can expect pricings to continue their widening trend, mainly due to shortage and regulatory factors while NAVs and hybrids should become more attractive to banks. Borrowers will still benefit from liquidity although in different forms and higher pricings. Financial engineering will help banks combine the various forms of financing, gaining competitive advantage.*

James York, NatWest Markets: *2022 served to be a year of even more innovation in the Funds Finance market, being somewhat a tale of two halves, with a flurry of activity in H1 and then an active yet more constrained liquidity environment in H2; set against a challenging macro backdrop. Inflationary and broader credit challenges very much remain at the fore as we enter the new year, such that protracted fundraising periods may well prevail for longer as LPs remain more selective in their deployment to the private capital space, particularly in the context of how for many investors, private allocations have inadvertently grown proportionate to broader portfolios which have been hit by material public asset value declines. This should pave the way for further growth in secondary activity and continuation funds, each of which present a host of interesting financing prospects. Meanwhile institutional appetite for fund financing continues to grow, which may further catalyse the use of ratings based solutions. It will also be interesting to see whether facility utilisation trends vary, as GPs are faced with higher all-in borrowing costs that approach ever closer to the cost of LP capital. The importance of ESG continues to be prevalent, with increased scrutiny on the granularity of portfolio level reporting. It is clearly going to be an interesting year ahead, with shrewd risk-taking and due diligence remaining pivotal for lenders; yet no doubt 2023 comes with plenty of opportunity for the market to further build on its resilient and adaptive nature.*

Slade Spalding, No Limit Capital: *2022 has been quite a year, best described as a year with two halves. The first half we saw record market activity and a number of large facilities being oversubscribed and closed at very competitive terms. H2 brought a very different dynamic. With liquidity drying up, we have seen lenders become increasingly more selective especially in Q4. Getting a subline in place now is harder than it has ever been, even strong GPs with proven track records are struggling to get their lines filled and some are forced to close fund lines below the target level. We would expect the same to continue into 2023. Furthermore, we think that supply demand imbalance will push the pricing higher, and that GPs will have to rethink their sublines and lending clubs. We think that alternative lenders will continue to play an increasing role in the space, however in order to be able to tap into this alternative source of capital, GPs will have to revisit on how they structure their sublines to allow for institutional money to play a part in it. We also expect alternative fund finance solutions like NAV and hybrid loans to play an even bigger role in the market, as those solutions can unlock significant value for GPs by generating distribution events for funds especially in the current environment where traditional exits aren't as attractive.*

Eleonore Codron, Nomura: *The repricing for credit NAV facilities has been very slow throughout 2022. We expect further correction throughout 2023 with lenders looking for adequate relative value vs the CLO market. On the PE side, the weak performance of equity investments throughout 2022 will push exits / divesture by a couple of years. We expect a number of these assets to be transferred to continuation vehicles, financed by a combination of NAV and capital call facilities. With the base rate expected to remain high, cost of financing of PE NAV facilities is moving close to double digit. Additional guarantees / securities might become more frequent in order to cheapen the structures. The denominator effect has slowed down commitments from LP's towards PE strategies, but also increased secondary market activity. With discount of secondary interests potentially increasing, we wouldn't be surprised to see LP's trying to monetise their stakes (instead of selling them) through NAV like structures.*

Gerhard Caspar and Christina Johard, Nordea: *Following yet another record year of business activity in 2022, we expect 2023 to be slower in terms of volume but active in terms of innovation and complexity. Subline volumes will increase moderately during the first half of the year as fund-raising initiated in 2022 begin to complete and thereafter begin to decline on the back of a very slow fundraising market and subdued deal activity. Higher rates will not deter funds from utilizing sublines and commercial terms will stabilize at the higher levels seen in the fourth quarter of 2022. Legal terms will tighten as lenders push to regain ground lost in recent years. The "self-funding" PE-portfolio exists no more and on the back of tightening liquidity LP acceptance for novel fund financing- and liquidity solutions will accelerate. NAV-lending and GP-led transactions will become more prevalent resulting in ample business opportunities for innovative bank- and non-bank lenders alike. 2023 is destined to become an interesting year in our industry!*

Fabien Bonavia, OakNorth: *The fund space will not be immune to the two biggest challenges of 2023: inflation and tight monetary policy. Scrutiny on valuations, particularly in real assets and tech will also make some investors jittery. That said, every challenge presents an opportunity. The more hawkish investment funds may spot "good deals" to be swept into their portfolios. New NAV and sub line facilities to support such activity may very well ensue.*

Brad Mitchell, Pantheon: *The Fund Finance market has experienced a sustained period of strong growth and supply of liquidity, however this has somewhat cooled in Q4-2022. H1-2023 is likely to continue on the same trends, with the sourcing of credit more challenging for subscription lines and time to clear a back-log generated over Q4 2022 due to a sudden shift in credit availability. What is interesting is that the credit availability for NAV lines has remained resilient, with an increased focus from both bank and non-bank lenders on this product with a number of new entrants entering this space – a change in allocation of capital to NAV lines adds further pressures on the subscription line supply but it will be interesting to see if this supply is maintained for what is a higher risk product during economic uncertainty and higher interest rate environment. Time will tell, however these pressure could ease in H2-2023 as: i) banks seek revised capital allocations; ii) new entrants emerge, specifically from the Asia Pacific region; iii) a rebalancing exercise between banks and non-bank lenders; and iv) a cooling of demand, with subscription lines rightly sized for needs and larger syndicates accommodated. The Edinburgh Reforms could also have an impact over the course of 2023, and something to watch closely.*

Matthew Potter, Pollen Street: The macro environment we find ourselves in has led to a slowdown in exits of portfolio companies and we don't expect this dynamic to change in the short-term. Funds can naturally absorb some of this extended holding period but as this starts to impact returns we'd expect to see GPs consider their financing options to be able to provide liquidity where needed, if they haven't already. This would point to more activity in the NAV or other asset focused financing space; as a lender in this market we continue to see it as having very strong risk reward dynamics and those lenders willing to have more flexibility at this time are likely to win out. Even though the environment may not be the most favourable there are still many good opportunities out there. These times often drive innovation and we therefore may start to see funds looking to work alongside their lenders to find solutions needed during this more uncertain period.

Diana van Lieshout, Rabobank: Despite the Ukraine war, changing political alliances, increasing interest rates, the energy crisis, the re-emergence of inflation etc, 2022 showed plentiful fund finance activity. The first half year was - to a large extent - a continuation of the trends observed in the record year that was 2021. The second half started showing its first cracks and the LBO market came to a temporary (but ongoing) standstill. And to date, buyers and sellers continue to have difficulty to find the new equilibrium and so come to the perfect price for all involved. We foresee that further down the line, for 2023 and perhaps beyond, buyout deal value and exits may slow down meaningfully, with the obvious effect on the pace of fund raising. Alongside deteriorating M&A / LBO market circumstances, we see the denominator effect kick in for LPs and become more picky causing them to concentrate capital into a smaller number of larger funds. Having said that, we foresee that investor appetite in the PE asset class will remain high, for the right sponsor that is. We also see exotic ideas and forms of support rise. Funds are looking for creative (bridge) solutions as current market circumstances dictate longer sale processes. Different solutions such as continuation funds are becoming ever-more popular. Although last year we predicted (and hoped) that ESG would become the 'new normal' across the private capital financing spectrum, we now see an overall market hesitation or at least a postponement of incorporating ESG KPIs from the start of a transaction. New legislation, making sure to be nowhere near green-washing and sizeable bank syndicates each with their own particular ESG standards do not help in growing the green success. For lenders, regulatory capital constraints are having an increasing impact and are compelling some market-leading houses to reduce their presence in the fund finance market. This, in combination with higher funding costs have put upward pressure on pricing. For the new Basel IV future we foresee external ratings becoming a standard part of fund finance facilities, alleviating lenders' capital charges and thus pricing.

Will Lamain, Raiffeisen Bank: On the demand side, we expect GP's will require smaller sublines relative to fund size. With the shrinking level of differential / arbitrage between hurdle rate and borrowing costs, GPs will become more exact on facility sizing to minimise excess cost and improve efficiency. Fundraising in 1H23 will continue to increase, but at a slower rate. This means a lower number of sublines but increased focus on NAV facilities to optimise existing funds (especially for GPs which have had a slower rate of investment in 2022, and for funds with investments having portfolio level turbulence after FYE22 reporting). The secondary market will see more transactions and larger quanta as LPs re-examine their portfolio, which will therefore increase demand for modest financing facilities. Pref Equity trades will increase as LPs will be more likely to prioritise liquidity recycling and take gains off the table. On the

supply side we will continue to see constraints as lenders optimise portfolios, increase selectivity, and implement new capital strategies as each lender reacts to the latest interest rate environment.

Spencer Goss, RBS International: I do not expect the exceptional growth of the fund finance space over the past few years to be sustained through 2023. A slower, more challenging fund raising environment, likely driven by wider portfolio considerations within LP's as opposed to wider concerns with the asset class, could be expected to have a similarly dampening effect in investor backed financing. Additionally, we may see GPs actively managing borrowing costs by reducing borrowings if interest rates continue to climb to a level such that all in costs hover around the hurdle return. That said, with historically significant lenders either said to be leaving the market entirely or simply managing capital allocations with increased levels of discipline, for those lenders that do remain truly open, opportunities to lend can be expected to remain high. In the NAV / asset backed space, general sentiment seems to be that GPs will be looking at this space with ever greater levels of interest, looking to potentially utilise capacity to finance distributions where perhaps exits are taking longer to materialise or support underlying portfolio companies with extra leverage where interest cover covenants at company level may otherwise have the potential to prove challenging. Whether there will be sufficient lender appetite to match demand, however, remains to be seen.

David Cui, Shanghai Pudong Development Bank: 2022 was an exciting year for Shanghai Pudong Development Bank as a new joiner in the European subscription finance market. In view of broader market uncertainty, we may not see the large increase in subscription line volume in 2023 that we have seen over the past few years. The mega managers might encounter increasing difficulties in implementing multi-billion facilities. This liquidity pressure does create opportunities for new and or smaller lenders. As interest rates have climbed, we expect that lenders will pay more attention to the valuation of fund assets. We predict ESG or sustainability linked facilities will continue to grow and ESG-related KPIs will have more material impacts on margin or fees.

Paul Duffy and Stephanie Messac, SMBC: Even though 2022 has been a challenging year across all markets, we are expecting not only a strong LP Secondary Market but also a continued adoption of NAV facilities by Primary Funds ensuring a strong growth in NAV Financing in 2023.

Raghav Wadhawan, Standard Chartered Bank: Predicting next year for the fund finance market is not going to be as straightforward as previous years. Key themes of previous years have been market stability with continued growth in both fund finance demand and supply. Market conditions in both equity and credit have seen some of most volatile moves in 2022, which has had an impact on the broader private capital markets. Against this backdrop we see the following key trends: (1) fund raising to be more mixed across managers and to be more focused on top tier GPs. Overall length of time to raise capital will increase across the board. Despite this, the demand for subscription facilities will remain strong given the significant amounts of undrawn committed capital going into the new year (2) we saw bank lenders come into capacity constraints in 2022 driven by multiple factors from regulatory, cost of capital, to requirements for more nuanced focus on cross-sell. This will likely drive greater selectivity by the bank market and create opportunities for the non-bank lenders. Clearly there is going to be a knock-on impact on pricing and price volatility is likely to continue (3) given that public market

exit opportunities are more limited and not an ideal time for sell-side processes, we expect NAVs to continue to grow. The structuring in the NAV market has also evolved to cater for all different liquidity pools available here. We see the banks, credit funds, and other non-bank lenders notably insurance companies, working closely together to cater for the growth in the market. Apart from these, the key underlying theme of ESG remains a focus especially in the sub-line market.

[1] The views and opinions of the individuals expressed in this article do not necessarily reflect the views of their institutions.

KBRA Releases Research – Private Credit Funds in Pictures: Safety in Numbers

December 16, 2022 | Issue No. 204

KBRA has come out with a recent forecast predicting that the private credit industry will be well positioned to navigate looming macroeconomic headwinds on the horizon. To read more on how structural protections, disciplined underwriting and comprehensive portfolio management have come together to create the perfect middle-market storm shelter, click [here](#).

Coller Capital Publishes Its 37th Global LP Survey

December 16, 2022 | Issue No. 204

According to the Coller Capital *Global Private Equity Barometer*, a global survey on private market investors published last week, a third of North American LPs and 52% of APAC LPs believe public market volatility has made private equity more attractive on a relative basis. Other findings include: a significant share of LPs reporting that the denominator effect is likely to weigh on their private market allocations in 2023 and a growing interest from investors in private credit over public market debt. The survey is available [here](#).

Brickfield's Fund Finance Recruitment Roundup

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Brickfield Recruitment has just published its final major article of 2022, looking back at the year in fund finance from a recruitment perspective and looking ahead to 2023, with commentary from industry players on the lender, asset management and legal sides. The spike in compensation levels experienced in 2022 appears to have receded, but market uncertainty will present a different challenge. A tougher buy-side market in 2023 will mean opportunities for innovators and non-traditional participants.

Read the article [here](#).

Readers looking to receive regular updates on talent acquisition trends in fund finance can follow Brickfield on [LinkedIn](#). Law firms, alternative lenders, asset managers, banks and candidates with specific enquiries should email [Rory Smith](#) or call him at +44 7800 963 594.

PEI Article on Fund Finance

December 16, 2022 | Issue No. 204

PEI this week published a short article addressing LP perspectives on fund finance usage in the current market environment. The article is accessible [here](#).

Pitchbook Article on CFOs

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Since 2008, financial instruments starting with a “C” and ending with an “O” have been treated with suspicion. But should the same apply to CFOs? The main purpose of a CFO is to generate liquidity, and it's been suggested that it can obfuscate the risk of underlying assets. But, with this vehicle only really starting to proliferate in the last 1-3 years, it has not endured the test of time, or more importantly, the stress of today's market. Read more [here](#) to understand how CFOs have gained greater traction with the growth of the private equity secondaries market within a global economy that is seemingly more fragile than it has looked in a very long time.

WFF US: 'Private Equity to Entrepreneur' NY Event January 19

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Women in Fund Finance will ring in 2023 with a special New York event, "Private Equity to Entrepreneur," featuring an evening of cocktails and conversation with Jenn Toyzer, co-founder and CEO of UME Plum Liqueur, who will discuss her career journey from investment banking to business founder. Wells Fargo Managing Director Michele Simons and Cadwalader's Leah Edelboim will serve as moderators. Click [here](#) for more info on the January 19 event.

Cadwalader Fund Finance Attorneys Promoted to Partner

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Attorneys on Cadwalader's Fund Finance team have been promoted to partner, effective January 1, 2023. These accomplished attorneys have distinguished themselves through exceptional legal skills, outstanding client service and their consistent embodiment of Cadwalader's values.

We are thrilled to congratulate:

Patrick A. Calves, New York – Patrick counsels clients on a variety of bilateral and syndicated financing structures, including term loans, liquidity lines, NAV facilities, subscription facilities, hybrid facilities, margin loans and repurchase, securities lending and prime brokerage facilities. Patrick's practice includes work on structures involving a variety of non-standard collateral, such as hedge fund interests, private equity fund interests, capital contribution obligations and restricted stock positions. He also counsels both financial institutions and "buy-side" market participants on a variety of regulatory and compliance issues relating to securities and derivatives trading. Patrick earned his J.D. from Columbia Law School and his B.A. from Muhlenberg College.

Danyeale Chung, Charlotte – Danyeale's practice is concentrated in the area of fund finance, and she represents some of the largest and most prominent lenders in the fund finance industry in structuring, negotiating, documenting and syndicating multi-jurisdictional and multi-currency subscription facilities and other lending arrangements, often across from top-tier sponsors. She regularly advises lenders on some of the largest and most complex subscription financings in the market, ranging in size from \$35 million to \$6 billion in terms of lender commitments. Danyeale advises lenders regarding fund documentation, including governing agreements, and negotiates third-party investor documents. She received her J.D. from the University of North Carolina School of Law and her B.A. from the University of North Carolina Greensboro.

Leah Edelboim, New York – Leah advises banks and other financial institutions on syndicated and bilateral subscription credit facilities as well as NAV, asset-backed and hybrid facilities. She also has significant experience representing private equity, real estate, natural resources, debt funds and other fund borrowers in these transactions. Leah also represents funds in a variety of direct lending transactions. Her finance experience also includes advising lenders and corporate, sponsor, and investor borrowers in all aspects of secured and unsecured financing transactions, with a wide range of lending structures including acquisition and leveraged loans, investment grade facilities, middle market loans, asset-based loans, project finance

transactions, and private placements. She received her J.D. from the University of Miami School of Law, her LL.M. from St. John's University School of Law and her B.A. from Johns Hopkins University.

Mathan Navaratnam, London – Mathan has extensive experience advising banks, alternative lenders and fund managers on the full spectrum of fund finance products, including capital call facilities, GP financings, NAV facilities across all asset classes, GP/Manager liquidity facilities, family office leverage facilities and GP-led financings. Mathan has over a decade's worth of fund finance experience and has advised on some of the largest European fund finance transactions to date. He graduated from the University of Leeds with an LL.B. (Hons).

Welcome Sukhvir Basran

December 16, 2022 | Issue No. 204



We are pleased to welcome ESG finance and investment partner Sukhvir Basran to Cadwalader's London office. Sukhvir advises a range of clients on ESG strategies, policies, frameworks, disclosure and reporting, ESG-related transactions and products, and the integration and alignment of ESG across investment processes. You can read our full announcement [here](#).