



HOULIHAN LOKEY

# KEY SUCCESS FACTORS TO GP-LED FUND RESTRUCTURINGS

Fund restructurings were initially undertaken to address older vintage funds often with lingering, hard-to-sell assets and impaired general partners. That has been dramatically changing over the last few years into a broader set of transaction types, often called “GP-led fund restructurings,” frequently initiated by high-quality GPs. More and more GPs are looking to the secondary market as a source of strategic capital to address a variety of fund-level issues and opportunities.

But with growth comes a host of specific challenges. Especially since no two GP-led fund restructurings are identical—transaction strategy and structure, asset valuation (both today and future NAV), and accessing the right investors are among the most critical factors to a successful outcome. All of which points to the need for expert guidance each step of the way. Choosing an advisor with deep market knowledge and relevant transaction expertise, as well as a network of specialist investors and traditional limited partner relationships is paramount to a successful outcome.

When used at the right time and for the right reasons, a recap can revitalize a fund and be a “win-win-win” for GPs, LPs, and new investors. This paper examines some of the keys to successfully navigating this new and exciting part of the secondary market.



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## THE APPEAL OF GP-LED RECAPS

There are several reasons GPs look to execute GP-led fund restructurings. A transaction can address the departure of a key manager, correct overexposure to a particular region or sector, extend the hold period for additional value-creation, provide access to additional capital, or alleviate “restless investor syndrome” where some LPs in long-tail funds are seeking liquidity. Restructurings can be an excellent way to expand the investment base and enhance the fund’s franchise, enabling a GP to continue to manage the assets beyond the fund’s prescribed term. At the most strategic level, a transaction can be employed to reconfigure key fund characteristics, breathing new life into an existing vehicle.

## MULTIDIMENSIONAL CHALLENGES

Whether it is simply to provide LP liquidity or a more significant transformational transaction, a GP-led fund restructuring brings with it a wide range of anticipated, as well as unanticipated, challenges for GPs (and LPs). Among these are three core hurdles:

### **1. Upholding the alignment of interests between GPs and LPs.**

Aligning their own interests with their LPs can be among the most complicated aspects a GP faces in executing a transaction. Nevertheless, it is essential to structure the process in a way that navigates inevitable conflicts that arise and maintains alignment of interests between GPs and LPs (both existing and new LPs).

Sometimes early communications with LPs, particularly when first presenting a transaction, can fatally impair a process. The GP must arrive at, and consistently communicate, a solution that harmonizes the strategic rationale with the different objectives of various LP constituencies. Throughout a transaction, full process and information transparency are key to a



successful outcome. This leads to a crucial requirement of almost all transactions—LPs should have options regarding their path forward including a “status quo” option.

## **2. Maximizing value for the assets.**

Optimization asset pricing is often the key to a successful or unsuccessful transaction. Effective pricing requires a deep understanding of each underlying asset in a fund including a comprehensive view of many sectors. During a process, these capabilities allow the fund’s portfolio to be positioned in a way that demonstrates future value to the incoming investors.

How well is an asset positioned in its sector? Does current financial performance properly reflect future prospects? Are exit timeframes and anticipated value justifiable? How does concentration, if any, impact attractiveness of an asset or the overall portfolio? Maximizing value in the course of a transaction demands market knowledge and expertise that is both specific to assets and sectors as well as how these assets are viewed in the context of a transaction.

Additionally, Fund LPs, as a group, historically have not engaged a financial advisor. As such, a GP may wish to obtain a fairness opinion as this could provide comfort to all parties that the consideration offered represents a fair price.

## **3. Identifying and engaging the right buyers.**

In addition to executing an investment program consistent with the fund’s strategy, GPs also must actively manage their existing and future LP relationships. During a GP-led fund restructuring, a GP should access a rich, relevant array of new potential LPs, and understand the individual motivations and interests of each. In addition, the right investor participation should be driven by key characteristics of the transaction—e.g., asset mix, GP capabilities, need for follow-on capital, and targeted LP composition, among others.

Getting the right participation is not only critical to a deal’s success but also is an important opportunity to potentially reshape a GP’s LP base. For these reasons, engaging the right investors has both short-term and long-term benefits that warrant attention at the front end of a transaction.

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## PARTNERING WITH THE RIGHT ADVISOR

Considering the importance and complexities of these transactions, GPs must engage an advisor who can successfully help them navigate a nuanced process involving different stakeholder groups often with conflicting motivations and objectives. The right advisor is one that has a proven track record of successfully executing these deals, in all their forms.

Houlihan Lokey's Financial Institutions Group has been a leader in complex secondary transactions for ten years. The unit was created by 20-year veterans of the private equity secondary business who have acted as both investors and advisors in a sector that has evolved beyond simple LP transactions to a solution provider for various participants in the broader private equity industry.

The Financial Institutions Group can leverage Houlihan Lokey's broad capabilities during a GP-led transaction in ways unlike any other advisor. These capabilities include:

- No. 1 M&A advisor for all U.S. transactions
- No. 1 global investment banking restructuring advisor
- No. 1 global M&A fairness opinion advisor for over 20 years
- A global leader in hard-to-value assets
- 13 sector teams with deep industry expertise
- Private Funds Group with LP relationships across the globe
- Among the largest Financial Sponsors Group and Capital Markets practice with unique access to investors and insights

Source: Thomson Reuters 2018 Rankings

These capabilities are woven together by the Financial Institutions Group with its specific expertise in GP-led fund restructurings to offer an unparalleled offering to the market. Valuation and positioning insights, engaging the right investor universe, broad transactional success, among others, are applied to each engagement.

These advantages, along with senior-banker involvement, distinguish Houlihan Lokey as a trusted advisor to both GPs and LPs navigating the often choppy water of GP-led fund restructurings.

### ABOUT HOULIHAN LOKEY

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