Q&A

MOUNIR GUEN

Founder, MVision

MVision founder Mounir Guen explains why private equity structures will have to change as investment in the asset class grows, why the US remains the world's most important fundraising market, and why managers raising smaller funds are facing challenges.

Private equity fundraising has increased significantly in recent years. Has the industry reached a high-water mark, or is there still potential for further growth? If there is still growth, will that change the way the industry looks?
There is still huge growth to come in the asset class. Just look at Asia, where assets are increasing five-fold each year, and allocations for investors who are in the asset class are still only at two to three per cent of total assets.

It is also important to keep in mind that when people talk about private equity fundraising, they are usually only talking about a single funding structure – the 10-year LP fund.

That does not take into account family money, direct and co-investment of sovereign wealth funds and pension and other plan sponsors, or listed private equity. There is huge growth in these areas.

Private equity's position in the asset mix is established. You can invest in private equity in so many different ways now. So there is a much bigger picture to consider.

The only limiting factors for private equity are skill and ecosystem. The right talent is still limited and the US and Western Europe are the more mature private equity markets. There is a way to go before other markets scale to the same size and activity levels.

As the industry grows in new ways, will GPs that have relied on the classic 10-year LP fund historically have to move across to different structures?
The traditional fund structure will always be popular, but the industry will have to get used to a different model when more of US pensions move toward defined contribution (DC) plans from defined benefit (DB).

The market will follow the pension funds as they transition to DC, and that will mean a different regulatory structure. Private equity will have to evolve structurally – on the DB side more than half of the funding raised globally comes from North America.

You mentioned some of the limiting factors on private equity growth. How serious are those restrictions? How are those hurdles impacting LPs? How are they responding?
Skills and ecosystem are important. There is huge demand for private equity product, but it is like trying to push a 50-foot wave through a small space.

Investors want between 40 and 60 relationships, which is less than half what it used to be, and most investor guidelines limit commitments to no more than 10 per cent of a fund up to a maximum.

By default, that means a manager has to be big and able to absorb these commitments. You need to be looking at a minimum fund sizes of between €1bn and €2bn if you want to start getting in contact with the large investors. There just aren't that many larger managers around in the market.

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In terms of the ecosystem, the US is very mature when compared to the rest of the world. The gatekeepers know the market and are pre-selecting target GPs more than two years in advance at times. The US investors have also worked through multiple J-curves, which makes a big difference

In less mature markets, by contrast, there are only a relatively small number of LPs, even though some of the institutions are massive. And, depending on where you raise, you also have to obtain all sorts of licences and registrations. If you have ambitions to diversify your funding base, you need to give a lot of thought to where you want to do so.

Where does that leave your traditional mid-market GP focused on a particular geography with a decent track record who wants to raise a fund of less than €1bn?
Good managers will always raise funds, but when your fund is under that €1bn number it does become more limiting.

In Europe, mid-market GPs used to raise all their money domestically. They could pull together 20 local investors and raise €600m.

That pool of investors has consolidated and internationalised. There might be, for example, 10 programmes where there used to be 30, and they are investing around the world. The capital available for domestic managers as a result is a fraction of what it used to be.

There is interest for smaller cap funds, but the LP base shifts as programmes evolve to large ones.

Also, for smaller funds the logistics of marketing can be costly and they have to carefully target their investors.