GP Solutions

Rothschild & Co Global Advisory

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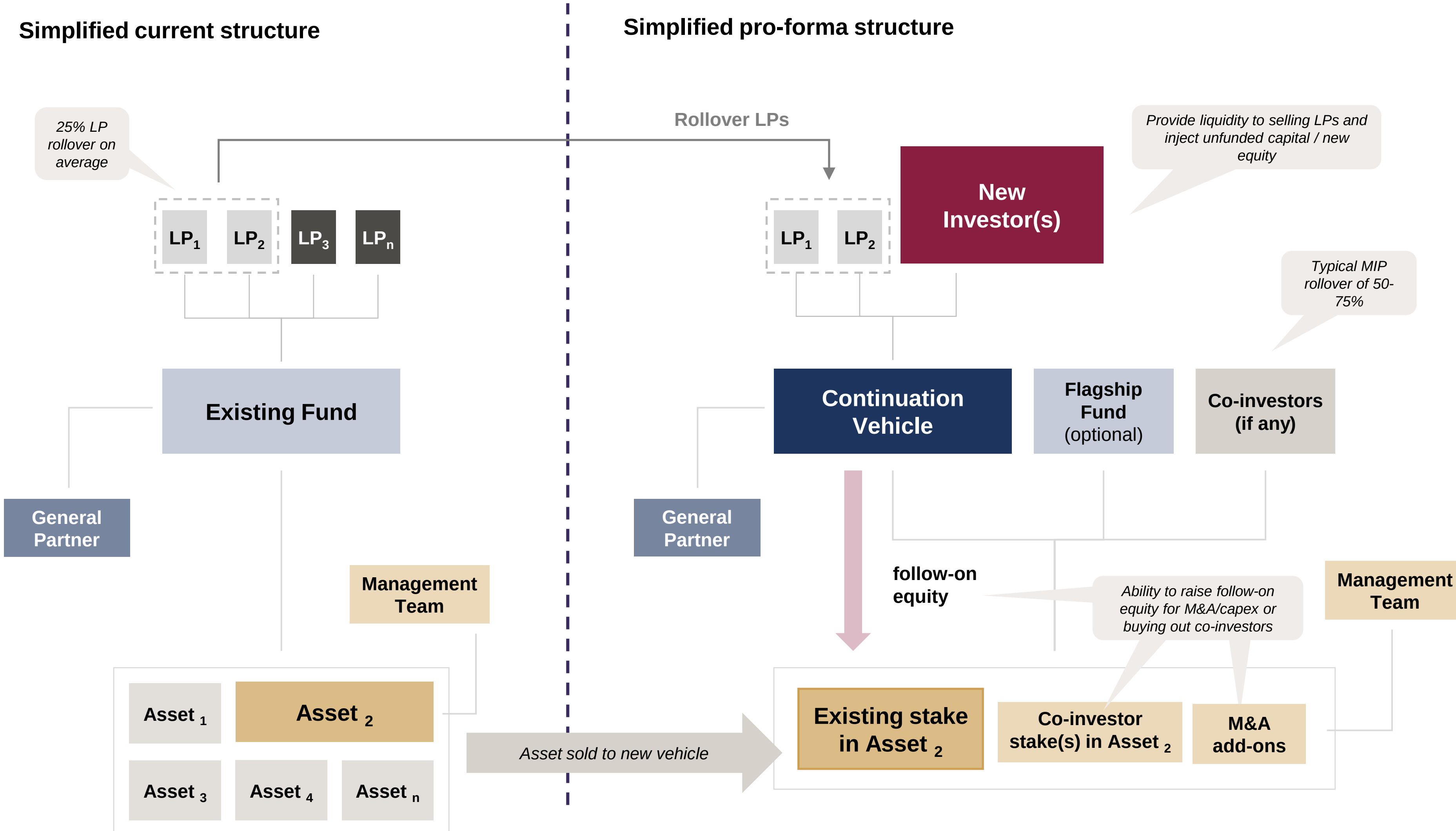
Rothschild & Co

Simplified, illustrative transaction structure

Asset(s) sold from the existing fund to a new GP-managed fund; the existing LPs would be given the option to re-invest; management and co-investors can be offered liquidity too



Stakeholders in a continuation vehicle

In order to create a “win-win” outcome, it is important to consider how each stakeholder approaches the transaction

Existing LPs

- Liquidity needs
- Pricing mechanism
- Buyside participation
- Terms of rollover option
- LPAC conflict waiver
- Discounts to NAV
- Full-cycle return

New Investors

- Target returns
- Alignment with GP
- Follow-on requirement
- Opportunity cost in market
- Deal size
- DD materials

The GP

- Target valuation
- Carry crystallisation and roll
- Follow-on capital
- New GP commit
- New GP incentive structure

Management

- MIP trigger
- Liquidity needs
- Reinvestment terms/alignment
- Coordination on revised business plan

Co-Shareholders

- Liquidity needs
- Buyside participation
- Ownership dilution
- Pre-emption rights
- Compatibility with new investors and alignment on business plan / exit timing

Lenders

- Compatibility of capital structure with new business plan
- Interplay of debt refinancing and CV

Key criteria for a successful continuation vehicle deal

Strong rationale

- Compelling rationale in the eyes of both existing LPs and new investors
- Deal enhances future value creation potential, typically stemming from the need for additional time and/or follow-on capital
- New investors need strong alignment with the GP and will probe whether the GP is a true “net buyer” of the asset

Attractive portfolio characteristics

- Highest demand for non-cyclical assets operating in markets with secular growth trends and potential for future consolidation
- Financial profiles should demonstrate strong margins and cash flow conversion, with the ability to delever over time
- Investors also have a clear preference for majority holdings, and tend to be averse to taking on public market exposures

Strong growth potential with credible business plan

- Investors will target PE-style returns net of carried interest and management fees
- GP base case of at least 2.0-2.5x+ net MOIC and 20%+ net IRR, incorporating follow-on capital
- Assumptions regarding top line growth and margins should be easily defendable and underwritten to flat/contracting multiples

Balanced entry valuation

- Investors will triangulate between various valuation methodologies (e.g. net returns analysis, reference date NAV, comparables)
- Valuation should ideally clear the latest NAV mark, resulting in an acceptable full cycle return for selling LPs
- Suitable valuation to set the basis for the GP’s future management fee as well as the hurdle for future carried interest

Suitable deal size for the target investor universe

- Despite an estimated €50bn of dry powder, there is still limited capital available compared to annual GP-led deal volume
- Investors look to compete for the “lead” position in deals, allowing them to set the price and terms for the transaction
- Competition is highest for transactions with equity tickets of between €100-500m

Strong GP alignment

- Investors are passive, relying on the GP commitment as a measure of the GP’s conviction and comfort in the business plan
- Although a small cash out was historically possible, investors now expect a full reinvestment and potentially a further top-up
- Typically the GP commitment represents no less than 3-5% of the new vehicle

Comprehensive due diligence materials

- Growing expectation for VDD reports to support due diligence as investors become increasingly sophisticated
- FDD commissioned to validate historic trading and quality of earning
- CDD to demonstrate market positioning, depth of buy and build opportunity, as well as underlying assumptions for top line growth

Carefully designed timeline

- Significant preparation phase required and launch timing must be considerate of prevailing market dynamics
- Running a thorough pre-sounding to inform decisions around process design and timing of launch is key
- Giving investors sufficient time in round 1 to conduct their DD will avoid losing numbers early on in a busy market

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