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The Pulse of Private Equity – 11/30/2015

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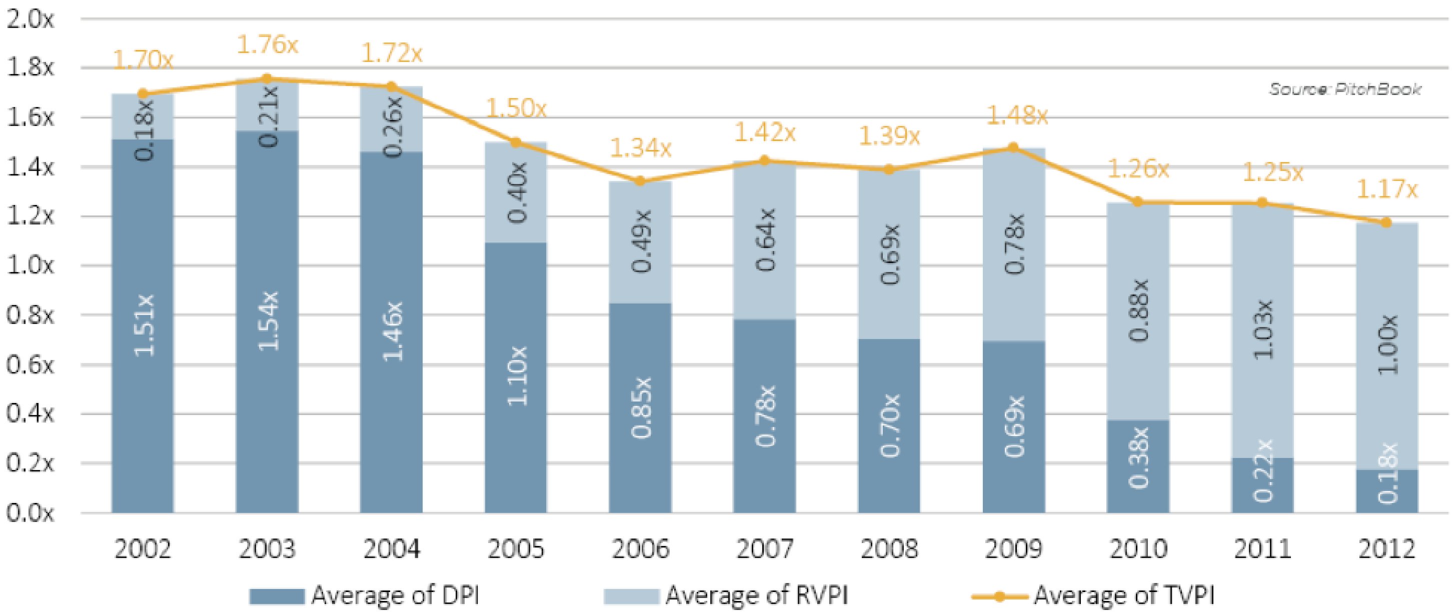
Could PE Return Multiples Begin to Stagnate?

Driven by the seller's market over the past few years, recent private equity fund vintages have seen their return multiples improve considerably. Distributions back to limited partners have risen to staggering levels, with 2014 seeing no less than $467.8 billion alone. Through the end of March, this year has also seen a hefty $168.2 billion returned by fund managers to their backers. In short, LPs have plenty of reason to re-up commitments to their PE fund managers.

GLOBAL AVERAGE PE FUND RETURN MULTIPLES BY VINTAGE



But there are a few disquieting signs on the horizon. PE fund managers are becoming victims of their own success to some degree. Competition for quality assets in a playing field where many investors are sitting on plenty of capital commitments understandably remains high. Overpaying for the best targets is a real concern, especially with some bigger deals finding trouble soliciting strong enough demand for debt financing, as exemplified by the failure of underwriters to fund the purchase of Veritas by The Carlyle Group and GIC. Granted, that deal had unique attributes that led to its financing troubles, but the point that investors are growing wary of high leverage remains, forcing buyout shops to scrutinize bids more carefully. Consequently, putting capital to work may stay difficult for the short term, although pockets of opportunity are still present. Moreover, on the sell side, sponsor-to-sponsor transactions face many of the same issues confronted by buyers, while the M&A boom that has provided much of the liquidity enjoyed by PE shops as of late may not hold for much longer. Overall return multiples for more recent PE funds could stagnate to some extent, accordingly, over the next 12 to 24 months, primarily in terms of realized monetization.

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