BUYOUTS

LPs lower expectations for PE, fret about deal flow

May 23, 2019 By Dietrich Knauth

- 41 pct of investors are very concerned or extremely concerned about competition for deals
- LPs want to concentrate their PE relationships, while GPs want more diversification
- Two-thirds of respondents expect a downturn in the next year or two

EVestment's Graeme Faulds. Photo courtesy of the firm.

A majority of PE investors expect returns in the asset class to decline in coming years, and a growing percentage are beginning to vet potential partners on their ability to drum up deals.

GPs and LPs expect returns to decline, and both are concerned about competition for deals and high purchase prices for companies, an **eVestment** survey shows.

But LPs are more pessimistic: 41 percent of investors said they were very or extremely concerned with competition for deals, compared with 25 percent of fund managers.

"Competition for deals was the number one concern for both fund managers and investors," said **Graeme Faulds**, director of product-private markets at eVestment. "From the investors' perspective, there is concern about the amount of dry powder [in] the market, and that is probably what's driving this concern regarding competition for deals."

Competition took a much more prominent place among industry concerns compared with 2018, when survey respondents ranked it as the fourth-highest concern.

Given the rising concern about crowding in the PE market, LPs may start to refocus their due diligence on managers' deal-sourcing processes and ability to deploy capital when considering a fund commitment, according to Faulds.

LPs will be more attentive to whether a fund manager is able to tap into more proprietary sources of deals, and whether they can add real value to the deals that they have to compete for, Faulds said.

"For investors [looking] to make new commitments, they're going to really want to focus their due diligence on [ensuring] that they're not going to be adversely affected by very high levels of competition," Faulds said.

The survey also spotlighted a mismatch between GPs and LPs in terms of relationship concentration. Three out of four fund managers indicated they plan to increase their investor bases, while three out of four investors said they planned to maintain or decrease the number of fund managers they work with.

Both LPs and GPs are wary of the possibility of a market correction in the near future, and almost two-thirds of survey respondents expect a downturn in the next two years.

"The current bull market has actually lasted longer than 'Game of Thrones,'" Faulds said. "This feels very reminiscent of the 2007 time frame, where valuations were high, and there was a strong market sentiment that there was going to be a market correction, but nobody could tell when it was going to come or what was going to cause it."

EVestment conducted the survey in early 2019, seeking input from institutional investors, consultants and fund managers. Participating LPs have more than $131 billion in private markets assets under management, and the GPs represent a collective $600 billion in fund values.

Action Item: View eVestment's full survey results here https://bit.ly/2WnmMqO

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