Buyouts

Emerging Manager Report

In partnership with Gen II Fund Services • December 2024 • buyoutsinsider.com

Uphill climb

Fundraising trail gets longer and steeper

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Buyouts

Emerging Manager Report

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Insight

An uphill battle **Winning capital is taking longer and often requires a track record**

It's clear that these are dire times for emerging GPs raising money. With distributions down to a trickle, LPs are in no hurry to gamble on untested groups, ***writes Rob Kotecki***.

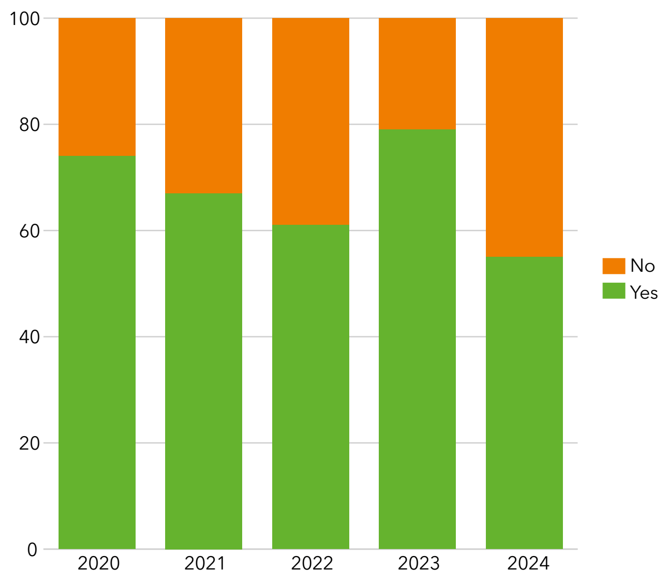
According to *Buyouts* data, $26.7 billion was raised in the first three quarters of 2024, the lowest tally in years. "If things continue at levels we've seen over the past few years, we're at risk of losing an entire generation of emerging managers," warns Brooke Coburn, founder and partner at Capitol Meridian Partners.

However, some managers are raising ever bigger funds. "We are seeing first-time funds raise two billion dollars, which was almost unheard of five or seven years ago," says Sanjiv Shah, a managing director at HarbourVest. So, if the landscape is so dire, how are some groups able to raise billons?

LPs still see the potential of new GPs. Coburn explains that while it is difficult to raise capital, it's also a great time for those that can. "There's been a massive reset in the rate environment, entry multiples at the mid-market can be more attractive, and there's scarce capital, either equity or credit, to go around."

And that's the other consensus – today's emerging managers might deliver truly outsized returns.

Are you currently fundraising? (%)



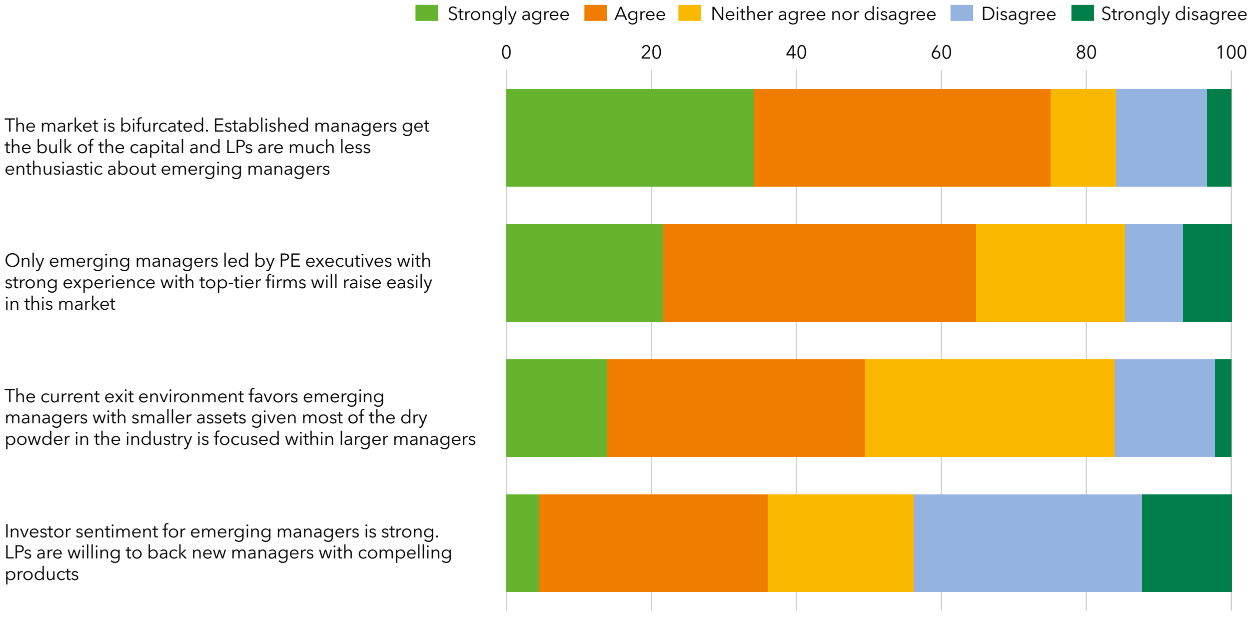
Fewer managers taking the field

Given the market conditions, no one can fault managers for waiting for better weather. Only 55 percent of respondents are currently fundraising, down from 79 percent last year, which seems unexpected given the spotlight that's been shone on the emerging managers of late. "There are countless emails for emerging manager events, seminars and workshops," says Star Strong Capital's founder and CEO, Spring Hollis. "But chances to get substantive access to decision makers able to deploy capital is few and far between."

Dark skies

Only 5 percent of respondents strongly agree that investor sentiment for emerging managers is strong; 34 percent strongly agree that the market favors established players and 22 percent think that only emerging managers from top-tier firms are raising funds easily. But Eric Requenez, partner at law firm Ropes & Gray, sees a silver lining on the horizon: "We still see large institutions going out with emerging manager programs, with a few even launching new ones."

How do you perceive market sentiment around emerging managers right now? (%)

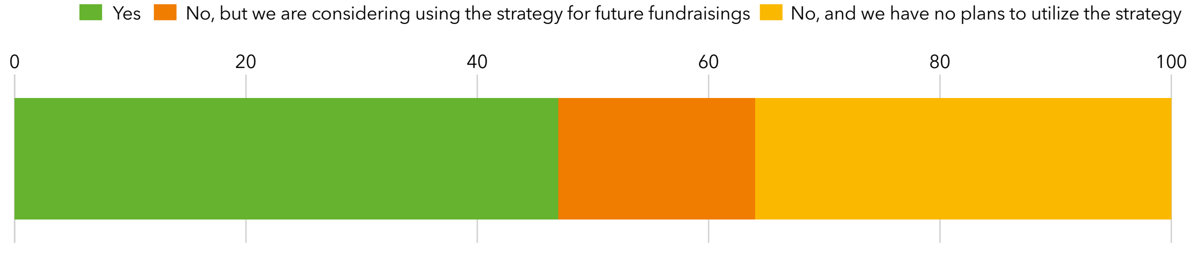


Closing a fund, deal by deal

Track record is vital in landing a commitment and managers are doing deals prior to build one. Sixty-four percent of respondents use, or are considering using, a seeded portfolio strategy, possibly driven by a hunger for smaller deals at better multiples, but not the managers that execute them.

Jordan Bastable, LongWater Opportunities co-founder, sees LP appetite for direct investments. Ropes & Gray's Requenez says: "It's a great way to build a track record and prove to aspirational anchor investors the deals a team can actually do."

Are you utilizing, or have you utilized, a seeded portfolio strategy to attract investors? (%)



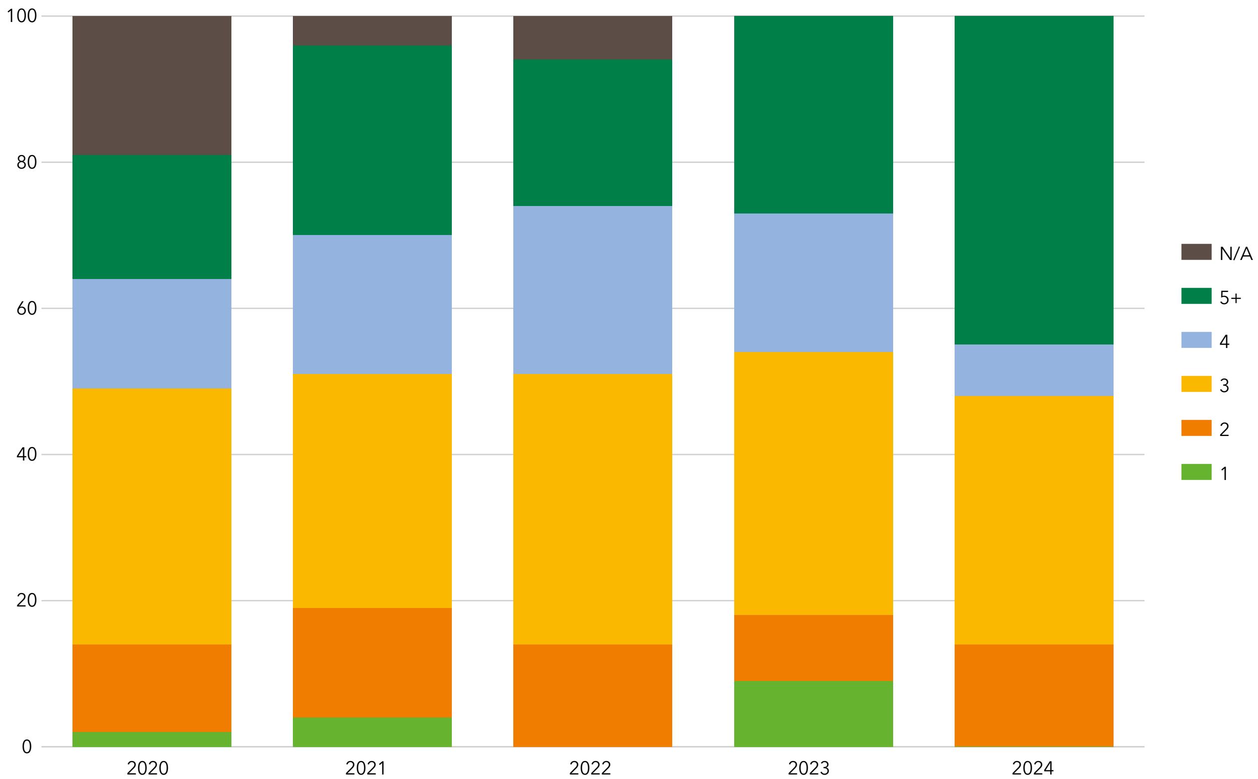
Source for all data: Buyouts Emerging Manager Survey 2024

The meeting game

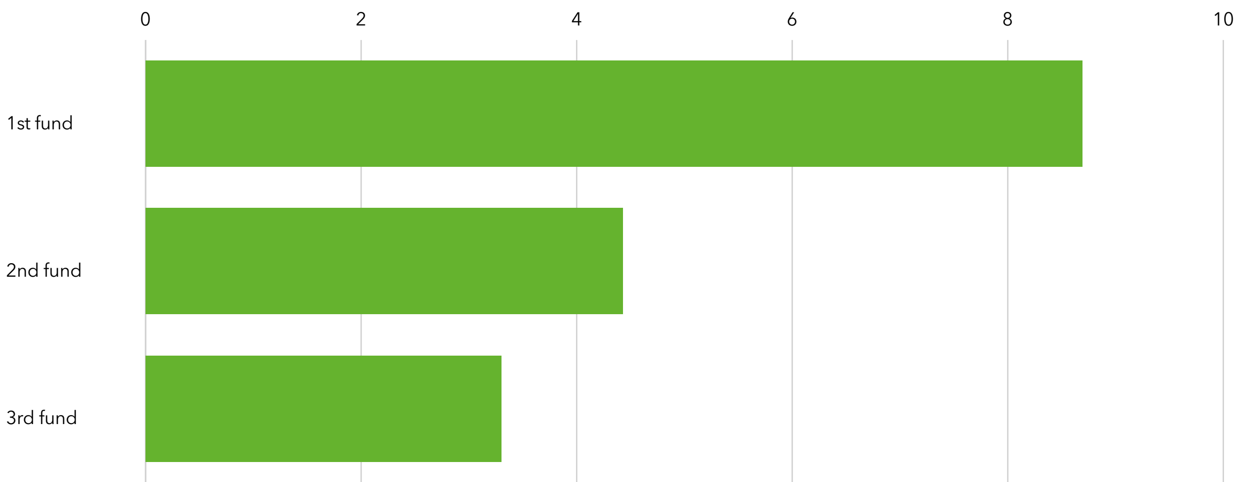
The number of meetings required to earn a commitment from an LP might seem a minor detail, but it speaks to the caution that investors are taking in committing to a new manager. This past year, no respondent earned a commitment off a single meeting, and 45 percent needed more than five, up from only 27 percent last year.

"The time it takes to raise a fund has approximately doubled," says Joseph Suh, partner at law firm Reed Smith.

For investors that ultimately committed, how many meetings (including conference calls) did you have with them on average? (%)



By fund number (Average number of meetings)

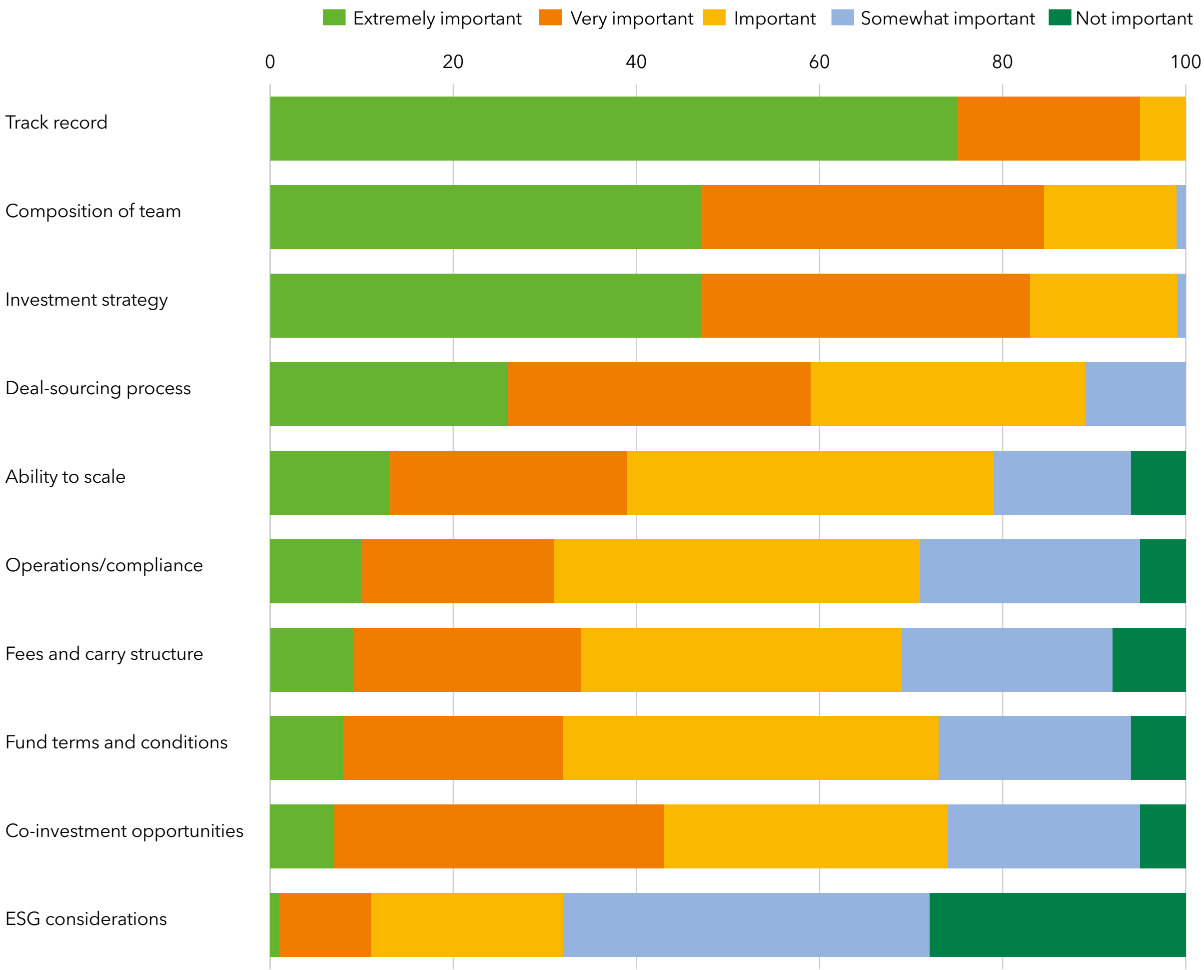


Track record still king

Seventy-six percent of respondents believe track record is the key factor in winning commitments. But what can get lost is that record is not always just a matter of returns, but pre-existing relationships.

"More than half of our investors knew us from our time at Carlyle," says Capitol Meridian's Coburn, "Sophisticated investors liked that the CMP investment team was a spin-out from Carlyle."

How important do you believe the following factors are for LPs evaluating your fund? (%)



55%

Percentage of respondents currently fundraising

8.69

Average number of meetings required with an LP to win a commitment to a first fund

48%

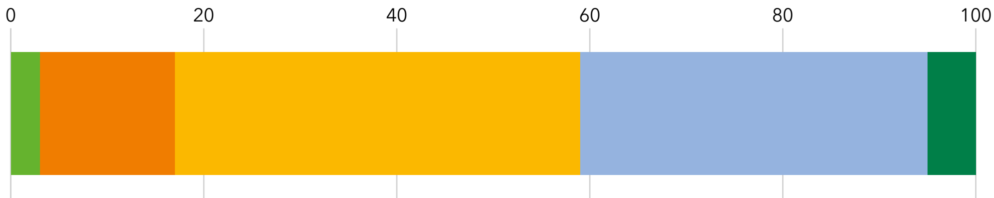
Percentage of respondents using a seeded portfolio strategy

Source for all data: Buyouts Emerging Manager Survey 2024

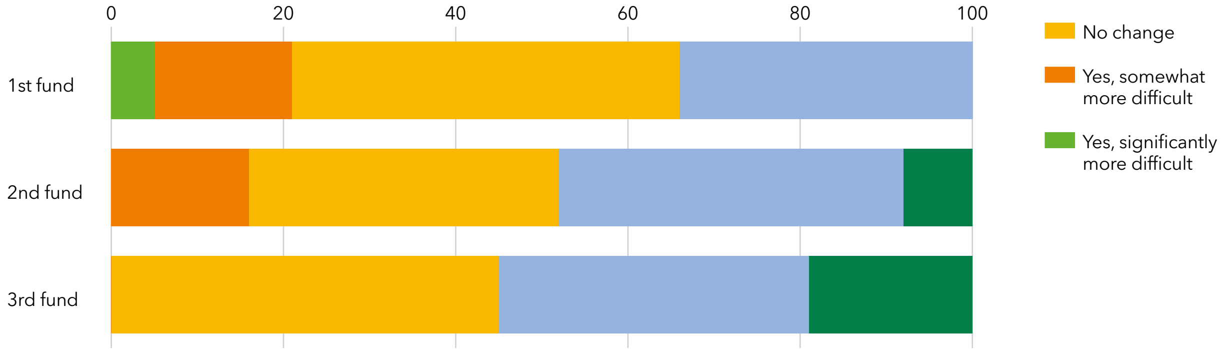
Talent in reach

One of the few bright spots for emerging managers appears to be access to talent, with around 41 percent of respondents arguing that it is now easier to find talent. Add to that the 42 percent that say there has been no change in the degree of difficulty in the search, and there is a clear sense that while it is not always easier to find candidates, it is also not getting harder.

Over the past 12 months, has it become more difficult to attract and hire talent? (%)



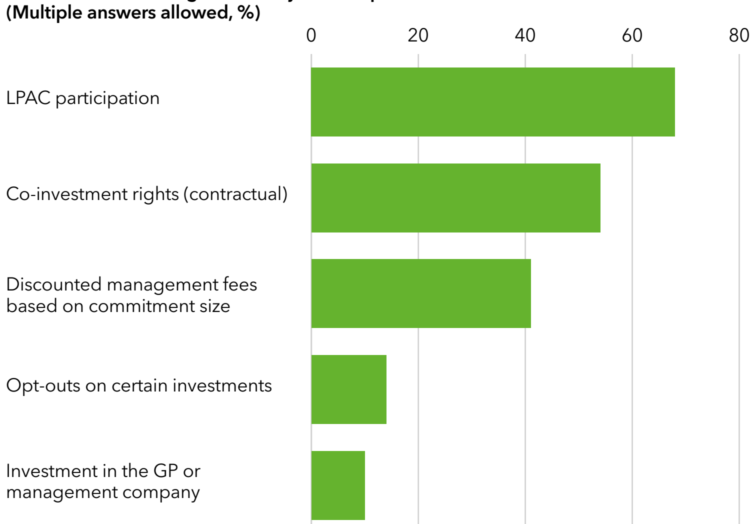
By fund number (%)



Everything's on the table

Market participants frequently stress how much LPs want co-investment rights, and 54 percent of manager respondents to this year's survey offer them. However, while some of them stress that investors are aware that new groups need management fees to function, 41 percent of GPs still offer discounted fees.

Which of the following terms did you offer/provide to investors? (Multiple answers allowed, %)



Source for all data: Buyouts Emerging Manager Survey 2024

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Editor's letter

Prepare to be exceptional

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The fundraising climate of the past couple of years has been underwhelming and not kind to any fund manager, regardless of what rung of the maturity ladder they occupy. For an emerging manager, though, it can be even tougher to persuade investors to trust them with their capital.

For this cohort of the market, the capital raising trail continues to be a steep mountain to climb. Data, compiled by *Buyouts*' research and analytics team, show that just short of $27 billion was raised by private equity first-time funds in the first nine months of 2024. And the survey findings in this year's *Buyouts Emerging Managers Report*, conducted in partnership with Gen II Fund Services, conveys that narrative in clear terms too.

> **"Managers are spending more time courting and pitching to potential LPs"**

Now in its eighth year, the survey indicates that fewer emerging managers are actively seeking capital at this juncture – just 55 percent of respondents are in the throes of fundraising, down from 79 percent a year ago. That is the lowest percentage recorded since 2020. Further, managers are spending more time courting and pitching to potential LPs. Forty-five percent of respondents this year say they had to hold five or more meetings before an LP agreed to commit to their fund. Last year, it was just 27 percent.

So, how to gain an edge in this capital-constrained, competitive market? Echoing the words of one of our contributors, it pays to be "exceptional." That means coming to the table ready to hit the ground running with good deals lined up and an experienced team that can execute them.

Helen Lewer

The Gen II View **Emerging managers cannot overlook the 'business of the firm'**

Comment

Expert analysis by **Jeff Gendel**, principal, Gen II Fund Services

The past several years have seen a proliferation of new private equity managers. Whether spinouts from established firms by experienced dealmakers or new ventures by investment bankers, family office-backed groups or industry professionals, these emerging managers bring new ideas and are a welcome source of diversification for LPs eager to deploy funds.

At the same time, these managers are often unprepared for the challenges and obligations of firm operations that they were never responsible for previously. If not planned for appropriately, these functions can distract from dealmaking, undermine LP confidence and derail an otherwise promising fund.

Emerging managers should not be surprised when they are expected to provide reporting and transparency on a par with larger competitors. When they walk into a meeting with an LP or adviser, they will be asked about things they have never had to respond to before. Someone on the other end of the table always dealt with those details at their predecessor firm, but now it's their responsibility, and they need to take it seriously.

When GPs were asked about the factors they believe LPs prioritize when assessing the track record of emerging managers, only 16 percent named transparency and reporting. But when LPs were asked about issues that are most critical to their organization, 41 percent said GPs' reporting format and standards. These two responses highlight the fundamental disconnect between perceptions of the importance of reporting by GPs and LPs, and GPs should take note.

In a challenging environment where economic uncertainty and greater competition have led to long fundraising periods and a slower dealmaking pace, it is critical for GPs to be aligned with LP priorities – especially so for emerging managers, which face greater hurdles. In 2024, 43 percent of emerging managers met with 150 or more prospective LPs in their fund raise, compared with just 27 percent in 2023. And 45 percent of emerging managers said it took five or more meetings for those LPs to commit, up from just 27 percent in 2023.

LPs are well aware of this dynamic. When asked about overall sentiment toward emerging managers, 75 percent of LPs strongly agreed or agreed with the statement that established managers get the bulk of the capital and LPs are much less enthusiastic about emerging managers. Similarly, 56 percent strongly disagreed or disagreed that LPs are willing to back new managers with compelling products.

This data and the operational due diligence questions that we get from institutional LPs investing in private equity make it clear that emerging managers' focus on the 'business of the firm' is as important to their success as great dealmaking. Showing strength in the five areas highlighted below will build LPs confidence that your firm and its fund administration partners can deliver today and scale with them for the future.

1 Transparency & reporting

As the survey results demonstrate, the quality of reporting and overall transparency may be more important than emerging managers think it is. LPs want more details, more frequent reporting, and greater clarity on every aspect of the fund and how performance is measured – the same clarity they receive from well-established private equity firms.

This trend that built slowly over time was accelerated last year when the SEC was pushing for new regulations. While the new rules were never implemented, their invalidation by the courts did not change LPs' minds about the information they want from their managers.

As this is being written, the

Institutional Limited Partners Association (ILPA) is working to finalize a new Reporting Template and new Performance Template that will set a new bar for fee and expense reporting and compliance disclosures. Backed by more than 600 LPs – including some of the largest and most influential – these are likely to become the standard, despite not being enforced by the government. Gen II has been actively engaged with ILPA's Quarterly Reporting Standards Initiative and assisting in the development of these new reporting templates.

While these new disclosure requirements may be somewhat onerous, they also present a rare opportunity for GPs to differentiate themselves. Being slow to enhance reporting, meeting only the bare minimum, or partnering with an administrator unable to support these new disclosure imperatives sends a clear signal that delivering the transparency LPs asked for is not a priority.

Similarly, the emerging manager that can deliver expanded analytics, is responsive to requests for new data and reporting, and can offer a 'single pane of glass' to easily view data, not only stands out from the pack, but demonstrates that they are thinking strategically about the next funds and long-term partnerships with LPs. LPs have told us that they are not willing to trust a crucial process such as fund administration to untested firms that haven't been able to demonstrate proficiency in that side of the business – viewing it as an unacceptable risk.

> “When you walk into a due diligence meeting, being able to confidently say to LPs that not only the dealmaking, but the business of the firm is in good hands, is essential”

2 Cybersecurity

With the continued growth of ransomware and data breaches globally, it's no surprise that cybersecurity is a big focus for LPs these days. While moving to the cloud has dramatically improved industry security and made world-class security more accessible to emerging managers, it also raises new concerns for LPs. They want to know their managers are buttoned up with respect to data protection and have all of the layers of security that they require. Many LPs may be skeptical that emerging managers have the scale or resources to deliver.

The biggest risk when it comes to cybersecurity remains very low-tech: human error. With so many people working from home in the wake of the pandemic, the threat level has only increased. Even the most conscientious employees occasionally let down their guard.

That's why a Zero Trust strategy – a new high-water mark in cyber protection that requires validation for every digital interaction – is a must. It's a shift from the strategy of 'trust but verify' to 'never trust, always verify', and is designed to remove the ability of bad actors from exploiting errors in judgment. And its why Gen II deploys state-of-the-art technology, best-in-class cyber-monitoring and protocols, regular network vulnerability testing, and constant staff training to stay one step ahead of bad actors. It's also why we maintain robust SOC II Type I & II, ISO 27001, NIST-SEC Cybersecurity and NY SHIELD Compliance, among other industry-leading protocols.

By employing continual vigilance, carefully limiting data availability and cutting off avenues for data to 'escape' (no sending of attachments, no printing at home), emerging managers can assuage the concerns of LPs. With so much at stake, and a constantly evolving threat environment, it's incumbent on GPs to choose partners that bring the best possible defenses to bear and relentlessly demonstrate their commitment to cybersecurity excellence through continuous investment in their people, processes and technology.

3 Data accessibility

If quality reporting is job one for LPs, greater access to all aspects of their fund data and analytics is a quickly growing second priority. LPs today have more questions that demand greater data accessibility – we know because we hear from them directly. Even emerging managers are expected to provide transparency that enables investors to track their investments, projections, and returns to streamline communications. Increasingly, that means on-demand access and visualization of fund data in aggregate and drill-down analysis for efficient performance reporting.

In some ways, emerging managers have an advantage as they are generally not burdened with legacy systems that house data in different formats and don't speak to each other. However, every firm needs to plan for data transportability. A no-code solution that enables managers to effortlessly integrate fund administration data with both in-house and third-party platforms and optimizes data utilization, is required for operational efficiency.

Similarly, a solution that automates data retrieval will ensure everyone on your team is working with current information and that they can deliver responses to ad hoc LP requests easily. Based on our decades of conversations with GPs – understanding their pain points and where they needed better solutions – Gen II developed the Sensr suite of technologies, which set a new standard in on-demand access, visualization, and drill-down analysis of fund data; integration with in-house and third-party platforms; and secure collaboration between attorneys, sponsors, and investors.

4 Technology investment

Cloud platforms, advanced analytics and artificial intelligence are reinventing how business is done across the financial services sector, and the promise for transforming fund administration is no exception. While it's early days for some of these technologies making a true impact, emerging managers must be investing in and incorporating them into their operations. While the core importance of talent and reporting rigor remains unchanged, technology is key to thinking critically about enhancing operations.

Gen II recently won an engagement with an emerging manager that reviewed 12 fund administrators. In their analysis, it was clear we had invested a significant amount in technology that enabled us to solve the major pain points that private equity firms and finance and operations teams have. More importantly, because of our investment in technology, they had confidence in our ability to solve in the future.

Forward-thinking emerging managers know that while they may not deploy a particular technology suite in their first fund, it will be beneficial for fund two, three or four as the reporting bar is raised and they rely more heavily on their fund administration team to efficiently navigate new demands. Gen II will continue investing in efficiencies in our market – prudently incorporating AI or other emerging technologies into our processes.

5 Integration & scalability

With growing demands, and increased complexity due to issues like different terms for anchor investors, continuation funds and secondaries, and expansion into different asset classes and transaction types, the need for all firm operations to be tightly integrated has never been more evident. While the 'core service' may be capital calls and periodic disclosures, effectively executing on the mandate to do more often comes down to the scope of what your fund administration can do and how well your team and outsourced partners play well with others.

> “In a challenging environment, where economic uncertainty and greater competition have led to long fundraising periods and a slower dealmaking pace, it is critical for GPs to be aligned with LP priorities”

Does your fund admin compliance team work well with attorneys? How have they kept up with the sub doc review that is becoming a bigger portion of the work because it is expensive for lawyers to complete and manage the corresponding paperwork? Can your team do the investor onboarding that the legal team isn't interested in? What about tax prep? The integration of these services into one tightly organized and cost-effective machine can make a huge difference in serving LPs and managing the business.

This is more than just technology and talent. Building a partner relationship with your fund administrator vs a mere vendor relationship is critical. True partners go above and beyond paperwork to educate, advise, help build expertise and think through difficult questions such as how much to disclose and which banks to use. Emerging managers recognize this, with 89 percent responding that the ability to provide strategic guidance and advice beyond core service was important. Good fund administrators go above and beyond and provide a competitive edge to their GPs.

When you walk into a due diligence meeting, being able to confidently say to LPs that not only the dealmaking, but the business of the firm is in good hands, is essential. While emerging managers will continue to navigate macroeconomic as well as competitive challenges, they can better meet LP expectations today and build for growth by partnering with the right fund administrator, which can not only equip them with the right platform to meet increased scrutiny, but with the knowledge, insights and best practices that can only come from having been there before. ■

Methodology

The 2024 Buyouts Emerging Manager Survey captures the insights of over 120 fund managers

Now in its eighth year, the *Buyouts Emerging Manager Survey* is again conducted in partnership with Gen II Fund Services. Field work for this year's report was carried out between August 21 and October 3, 2024.

A total of 126 emerging managers participated in the survey, responding to more than 40 questions on a diverse range of topics including fundraising, fees and operations, outsourcing and talent acquisition.

For the purposes of our survey, emerging managers are classified as those that are in the process of raising their first, second or third institutional fund, or those that have recently closed their first, second or third institutional fund.

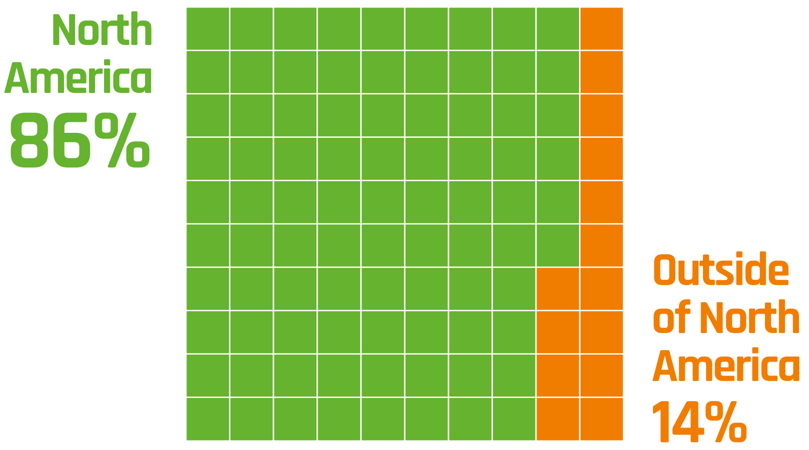
And for the first time, we have also extended the reach of our research beyond North America.

This means that this year there is a small European representation (14 percent) of emerging managers in the sample.

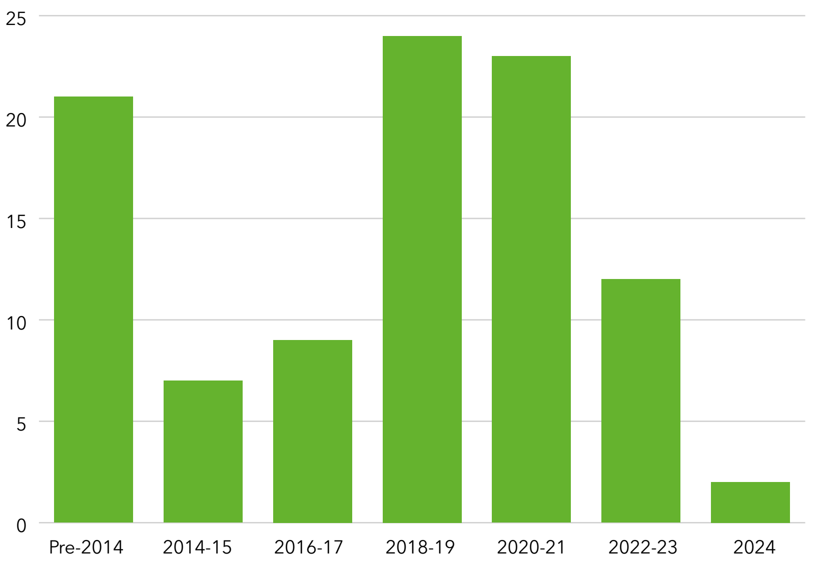
Sixty-five percent of the survey respondents are pursuing a buyout/corporate finance investment strategy, but a range of other strategies are reflected in the data, including venture capital, real estate and private debt.

Incomplete fund manager surveys were reviewed for inclusion in the sample on a respondent-by-respondent basis.

Where are you based?



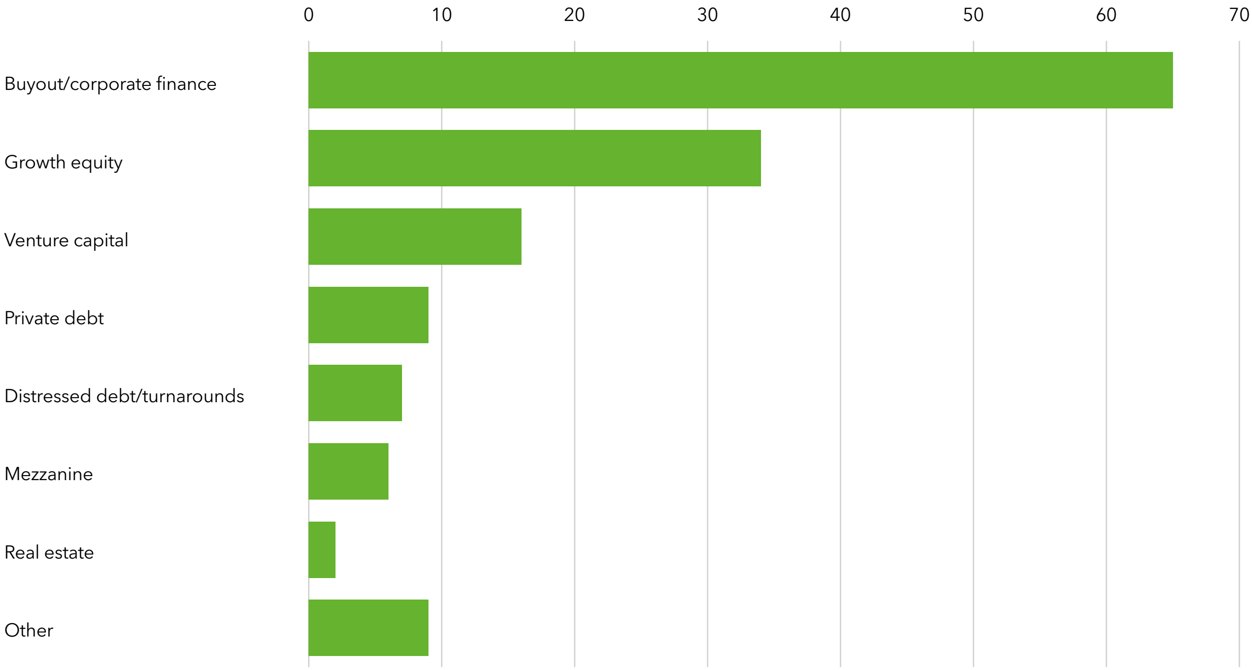
When was your firm founded? (%)



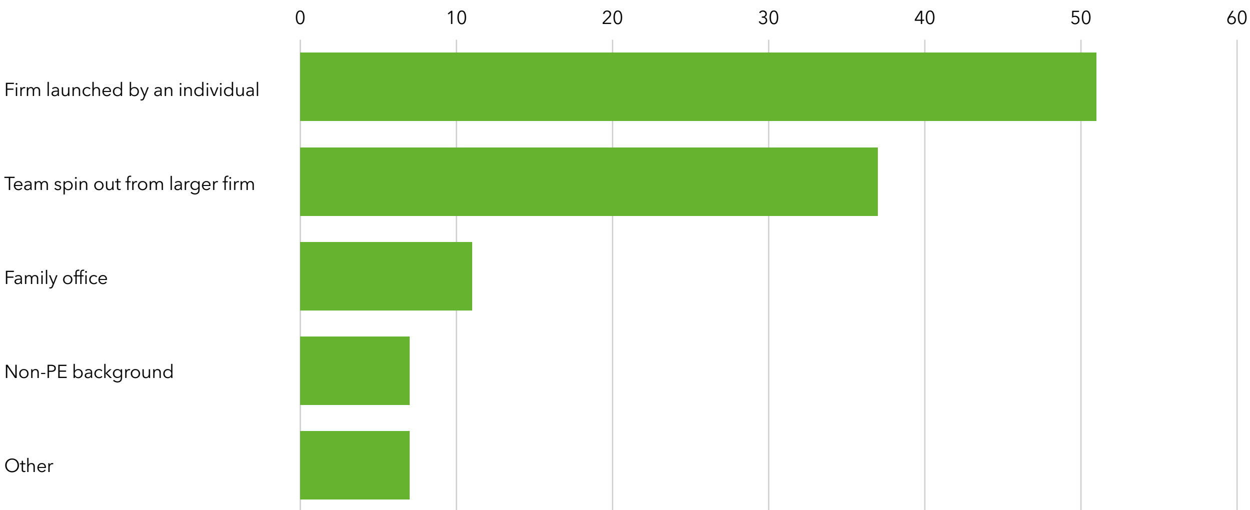
Source for all data: Buyouts Emerging Manager Survey 2024

Analysis

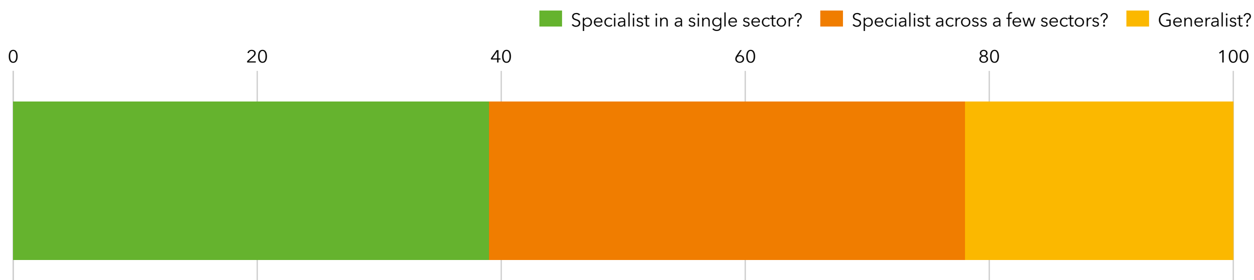
What kind of investment strategy does your firm pursue? (Multiple answers allowed, %)



What is your firm's heritage? (Multiple answers allowed, %)



Would you consider your firm to be a… (%)



Source for all data: Buyouts Emerging Manager Survey 2024

The gloom boom

There is little to cheer about the current market, but emerging managers believe their strategies will eventually deliver a windfall to LPs

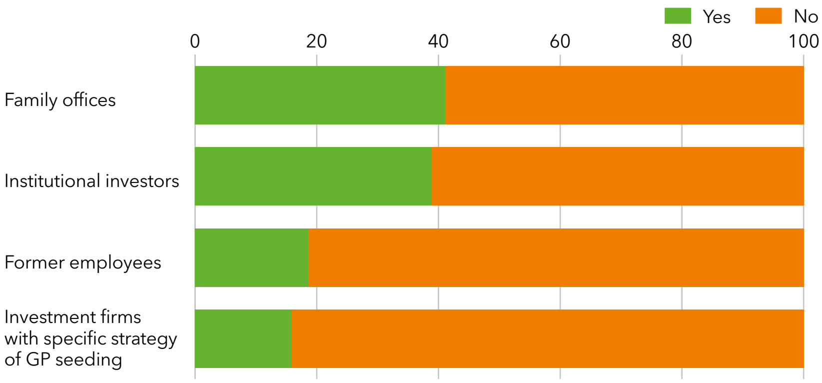
Emerging managers are optimists, believing they have the team, strategy and skills to thrive on their own, often leaving the shelter of a top-quartile firm. But in recent years, the fundraising trail has gotten longer, steeper and more rugged. They accept this fact generally, while working to be the exception – encouraged by continued LP interest.

"There are a lot of LPs out there who believe there are inefficiencies in the lower end of the market that can be translated into rewarding transactions," says Beau Thomas, a managing partner at Agellus Capital. "And they also see greater alignment with smaller GPs around the economics and the individuals directly driving the investments, which isn't always the case with large-cap GPs."

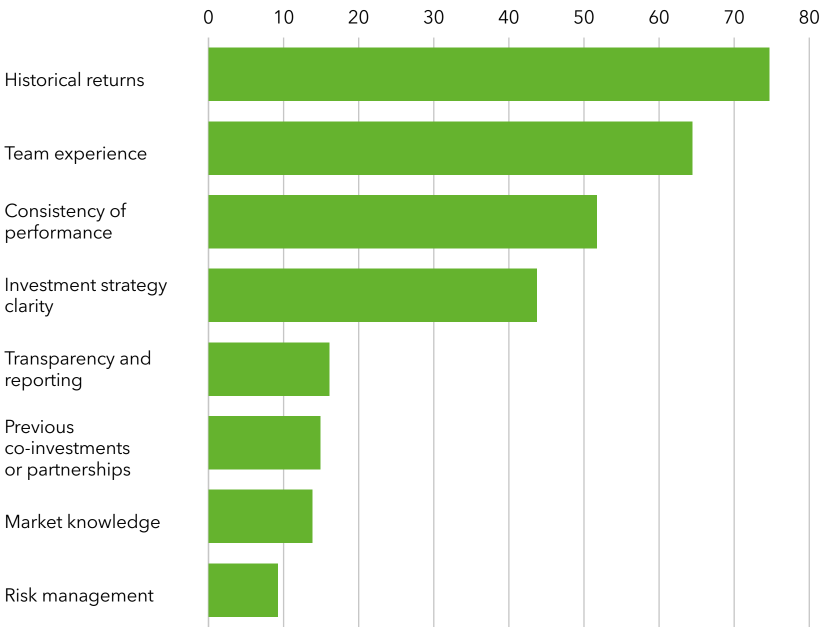
However, structural issues are making things harder. "Institutional investors may find the lower mid-market attractive, but their large investment sizes often exceed the capacity of funds operating in this space," says Jordan Bastable, co-founder at LongWater Opportunities, an alternative asset management firm in the lower mid-market. Indeed, in this year's *Buyouts Emerging Managers Survey*, conducted in partnership with Gen II Fund Services, 64 percent of respondents felt that allocation limits among LPs is one of their main challenges.

Emerging managers believe they face an uphill climb. Only 5 percent of

Has your firm utilized seed funding from the following sources? (%)

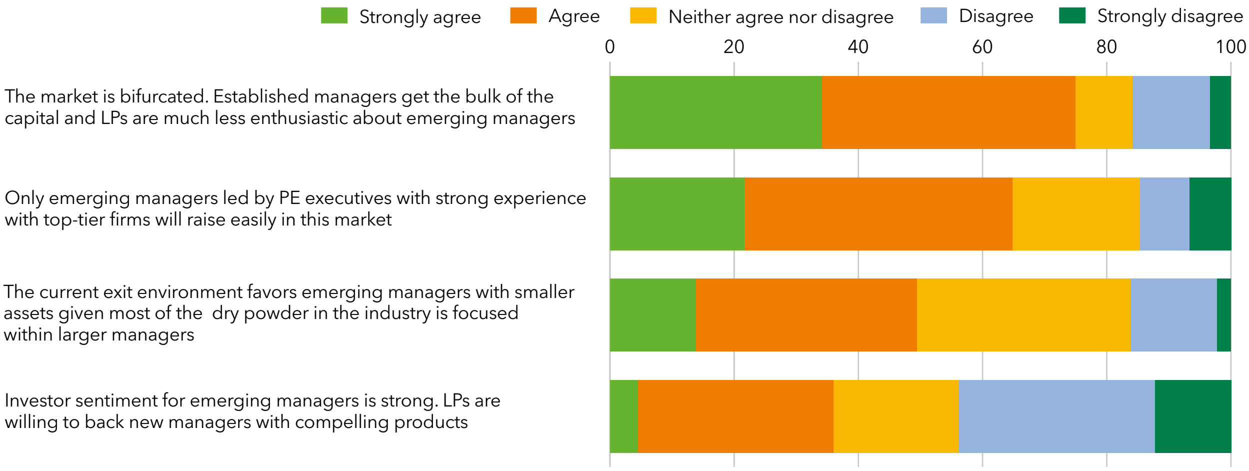


Which factors do you believe LPs prioritize when assessing the track records of emerging managers? (Up to three options allowed, %)



Source for all data: Buyouts Emerging Manager Survey 2024

How do you perceive market sentiment around emerging managers right now? (%)



managers strongly agree that sentiment for emerging managers is strong, while 34 percent strongly agree that established managers are faring better.

However, the picture is complicated; 49 percent agree that the exit environment favors emerging managers with dry powder. It seems that while new funds are hard to close, managers still believe their work can deliver, even if 60 percent of respondents find competition from established managers to be a major challenge, and 54 percent find LPs unwilling to take on the risk of a new manager.

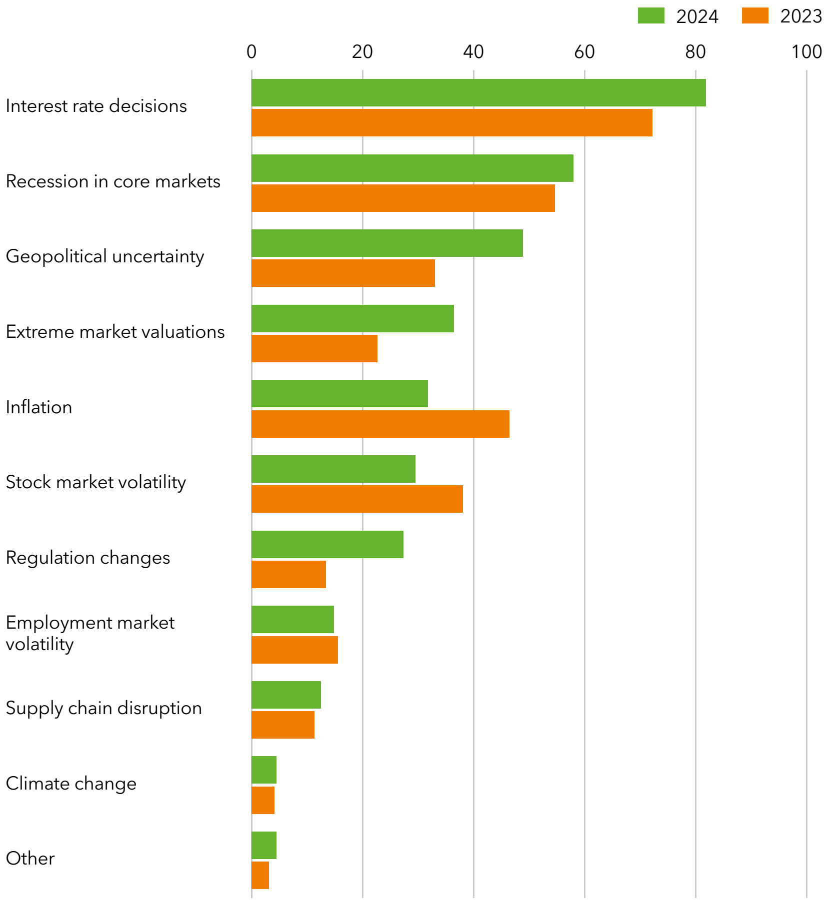
Sixty-five percent of respondents agree that managers spinning out from top-tier firms can still raise funds easily right now. Further, 76 percent view track record as a major factor in earning commitments. And when they say track record, respondents feel that LPs determine that by three key elements: returns (75 percent), team experience (64 percent) and consistency of performance (52 percent).

A new threat matrix

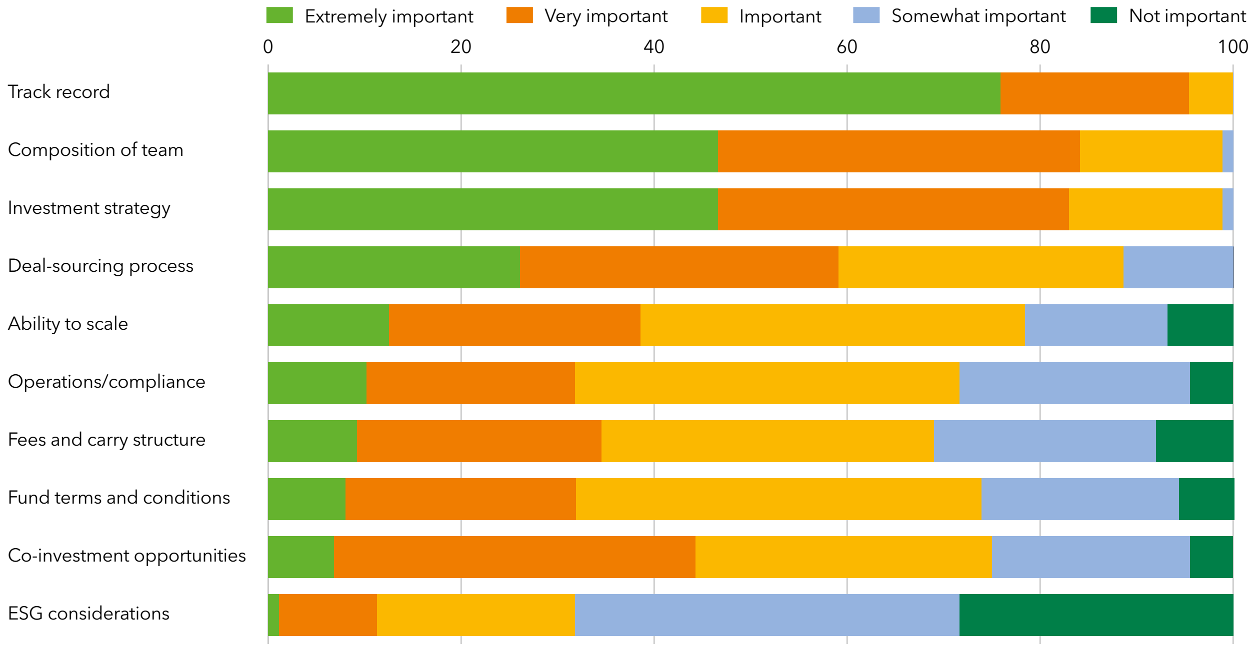
Managers may be pessimistic about fundraising, and optimistic about dealmaking, but their outlook for the broader private capital market is defined by threats that are out of their control, and not the same ones they did previously.

This year, the biggest changes came from their views around interest rates – 82 percent cite this as likely to have the biggest impact on investment performance in the coming year, up from 72 percent last year, while 49 percent cite geopolitical uncertainty, up from 33 percent in 2023. There is less concern around inflation and stock market volatility compared to last year's survey.

Which of the following factors do you think will have the greatest impact on private markets investment performance in the next 12 months? (Multiple answers allowed, %)

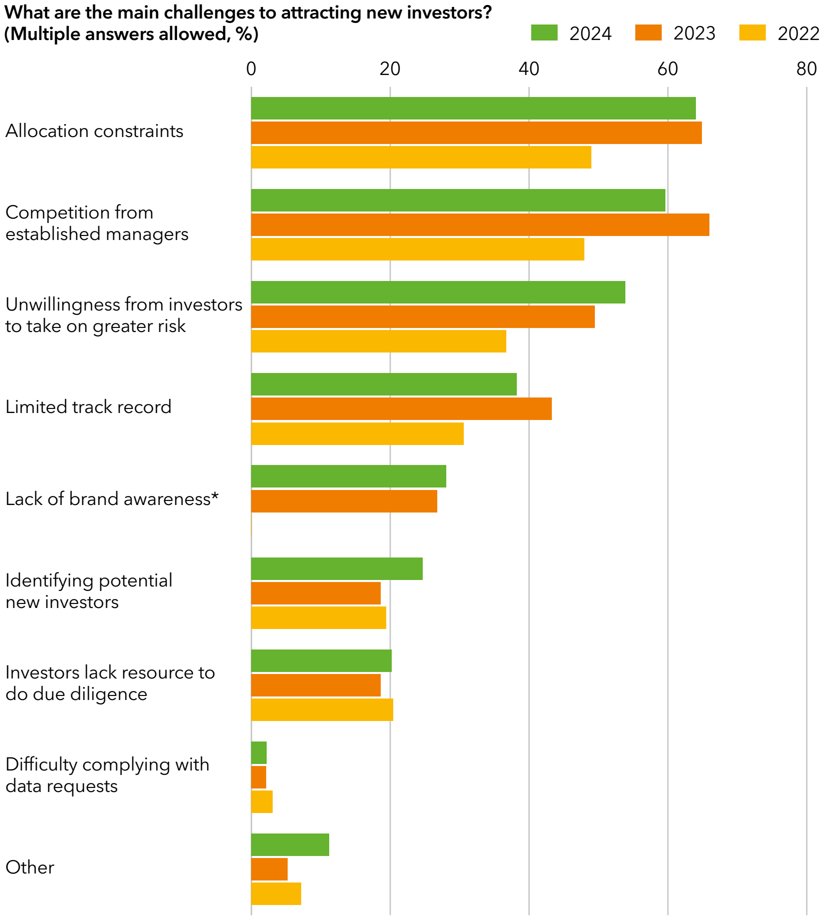


How important do you believe the following factors are for LPs evaluating your fund? (%)



Source for all data: Buyouts Emerging Manager Survey 2024

What are the main challenges to attracting new investors? (Multiple answers allowed, %)



*answer option not included in 2022 survey

Capital origins

The actual mix of capital used to seed funds has not changed much at all over the years, with a slight downturn in interest from family offices. Beyond these broad contours of the market, individual managers are still winning commitments.

"We've seen a surprising amount of inbound, unsolicited interest from larger institutions," says Ryan Anthony, co-founder of Longshore Capital Partners.

"They've looked at the data and come to the conclusion that there are outsized returns to be made in the lower mid-market." And the reality is that many LPs have built expertise to find the winners in this end of the market.

"LPs have long been interested in emerging managers and have devoted real time to develop the specialized expertise to find the best of the bunch," says Matthew Chase, an investment funds partner at law firm Latham & Watkins. Of course, increased LP savvy only supports the idea that this space is more competitive than ever before. ■

Fundraising remains daunting

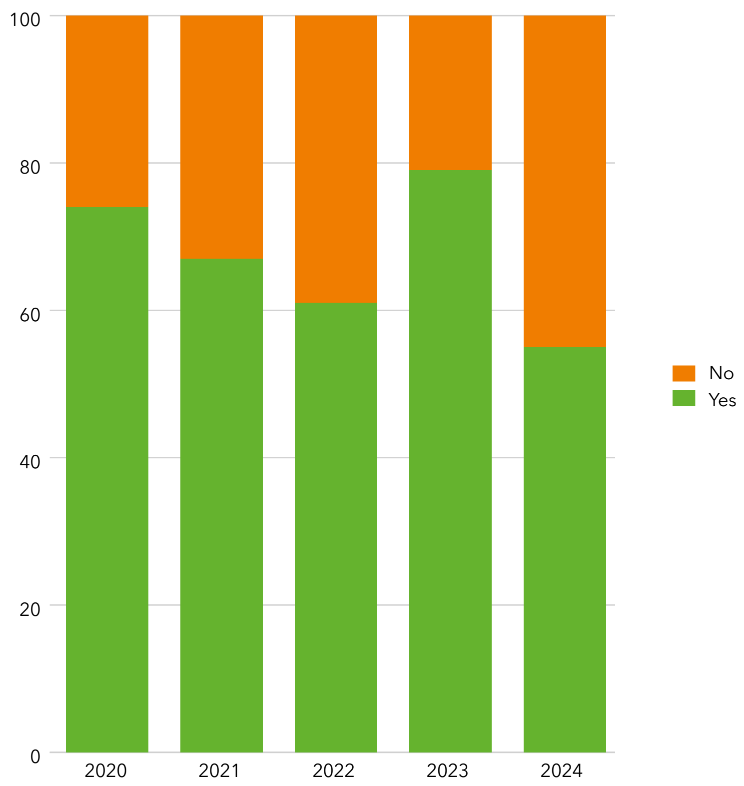
Though the market is hard to crack, there are LPs ready to back emerging managers that demonstrate patience and the rigor to make their case

For several years now, emerging managers have struggled to raise capital, and in many ways 2024 is the natural result of several years of LP hesitancy. According to PEI Group data, emerging GPs raised a record low amount in the first three quarters of 2024, with no one expecting a fourth-quarter comeback. And according to the *Buyouts Emerging Manager Survey*, conducted in partnership with Gen II Fund Services, there was a steep drop in groups actively fundraising this year.

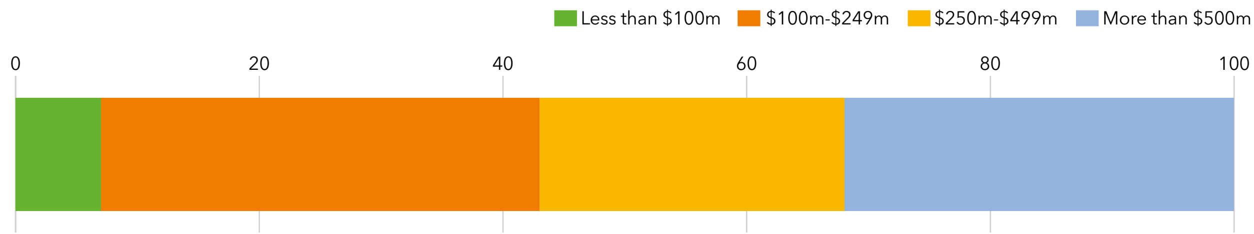
So, fundraising might not be for the faint of heart right now, but by drilling even deeper into the state of play, a resilient status quo can be found. Managers' sentiment remains positive about their own prospects, and there's a sense 2025 might see a rebound in actual commitments.

Some elements of fundraising and manager activity have been remarkably steady. Emerging GPs might

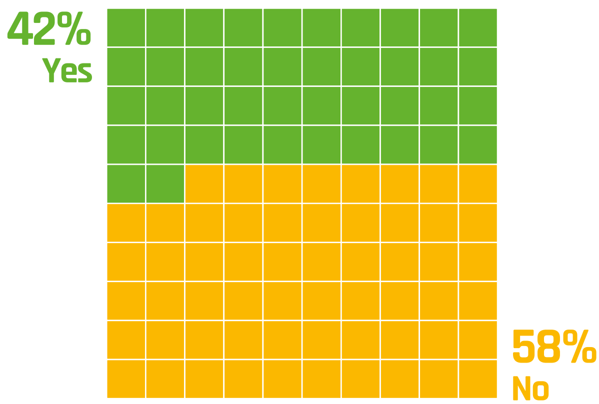
Are you currently fundraising? (%)



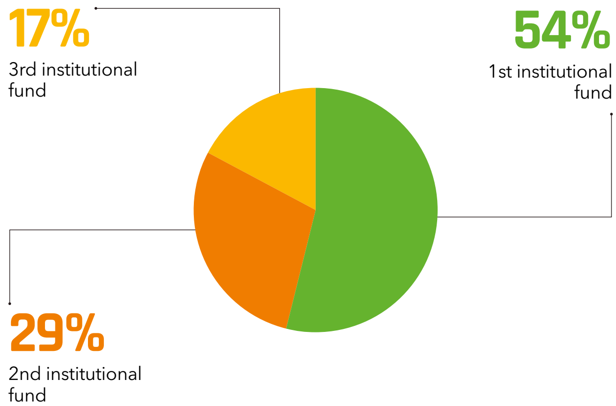
What is the target of the fund you are currently raising, or of your most recent fund? (%)



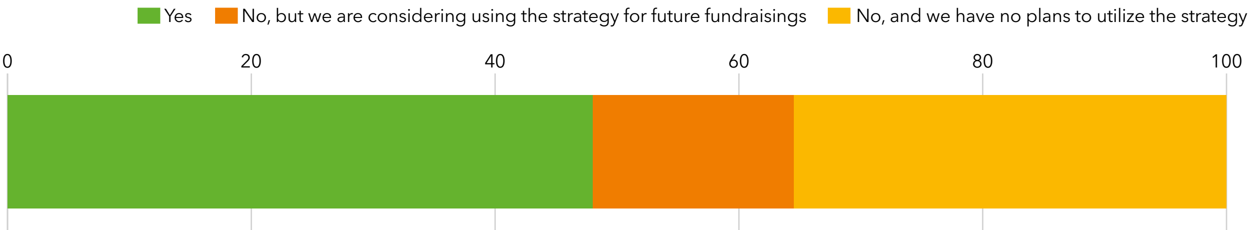
Did you use, or are you currently using, a placement agent?



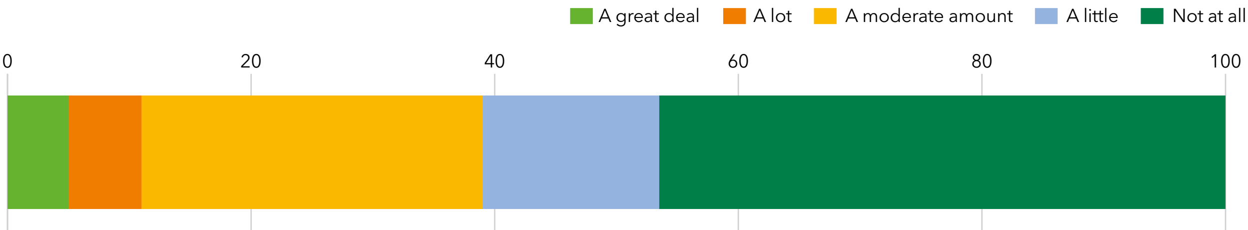
Is your current, or most recent fund, your 1st, 2nd or 3rd institutional fund?



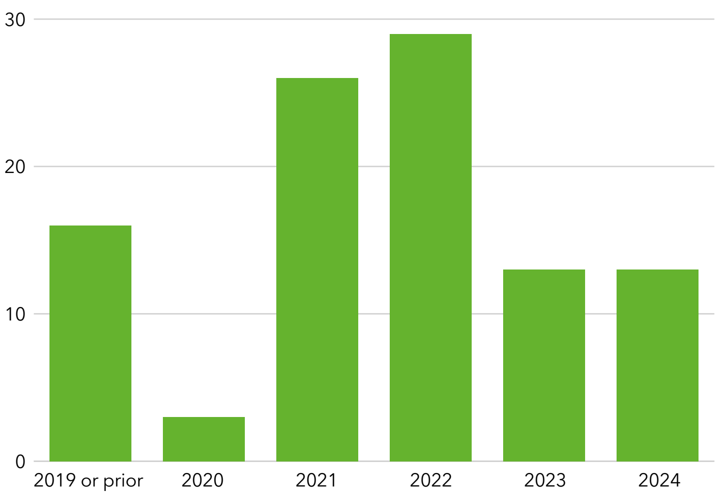
Are you utilizing, or have you utilized, a seeded portfolio strategy to attract investors? (%)



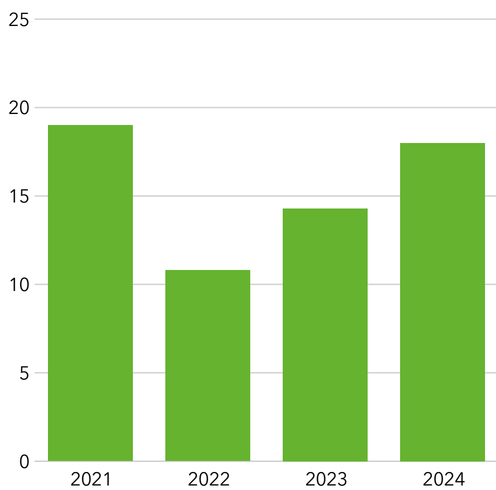
To what extent have recent SEC regulatory changes influenced how you are fundraising, or how you plan to fundraise? (%)



When did you launch marketing for the fund? (%)

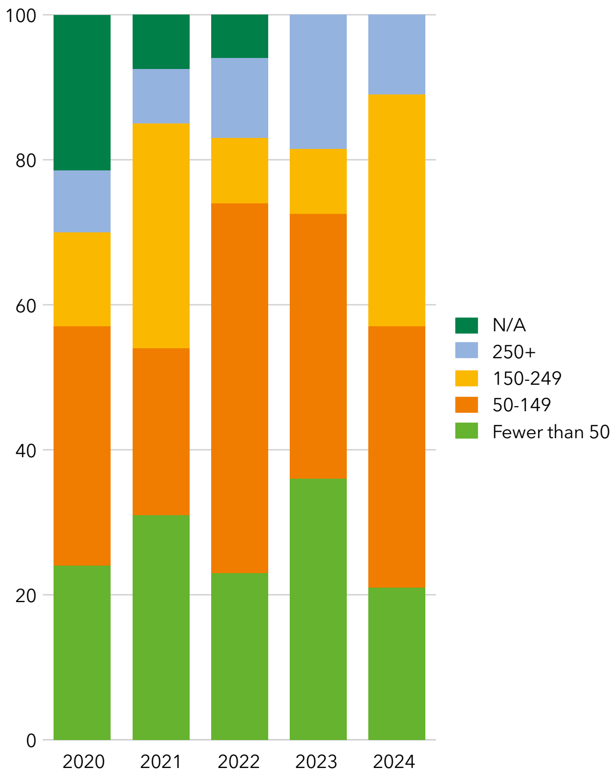


What was the length of time between first and final closing? (Average months)

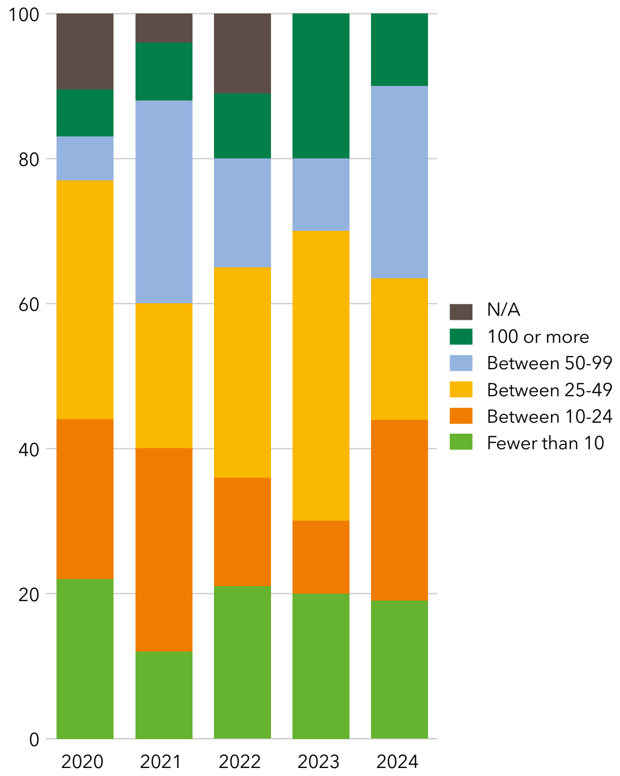


Source for all data: Buyouts Emerging Manager Survey 2024

How many prospective investors did you meet with? (%)



How many limited partners do you have in your most recent fund? (%)



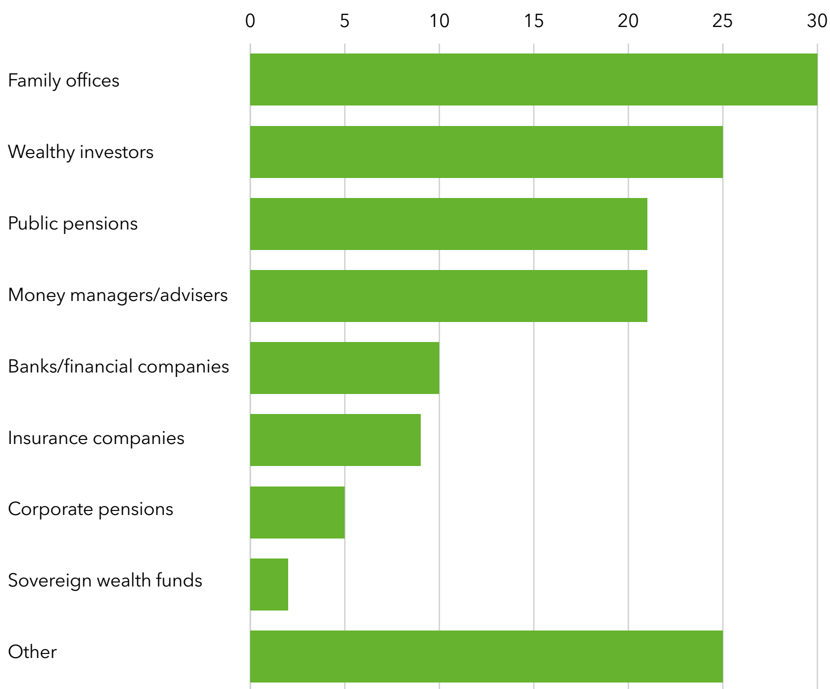
be downbeat in their assessment of their end of the market, but they are not trimming their sails just yet. This year's targets fall mostly between the traditional $100 million-$500 million range, but 32 percent are targeting a close above that.

Proposed Securities and Exchange Commission reforms have had a negligible impact on managers' behavior – 47 percent of respondents say regulatory issues have no impact at all, and only 5 percent report they matter a great deal.

The number of active portfolio companies has also been remarkably consistent, with respondents this year expecting the same number of new investments in the coming year, supporting the sentiment that while emerging managers are struggling to close funds, they remain confident of closing deals.

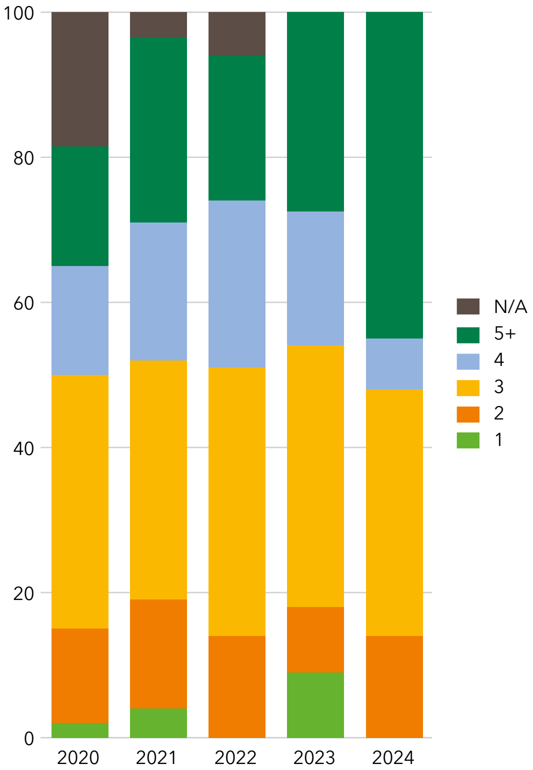
"We've seen clients do one or more fundless sponsor deals, which allows

What percentage of capital came from the following sources? (%)

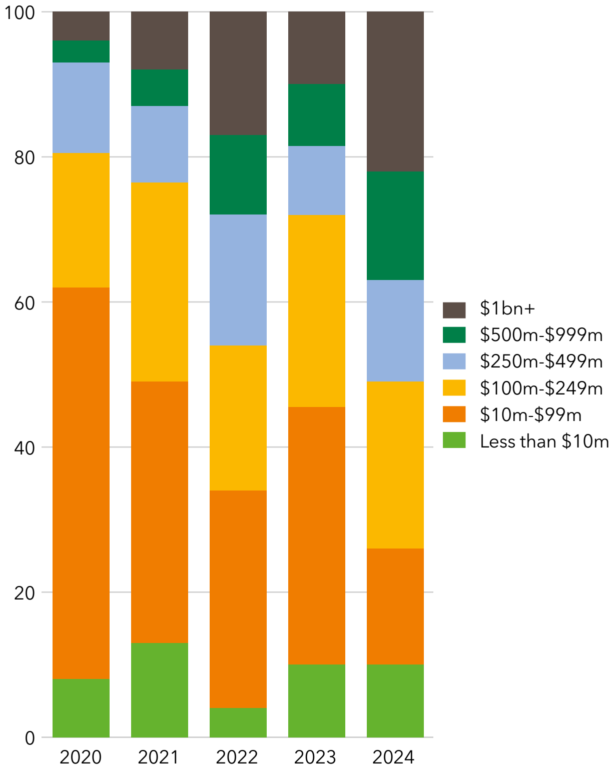


Source for all data: Buyouts Emerging Manager Survey 2024

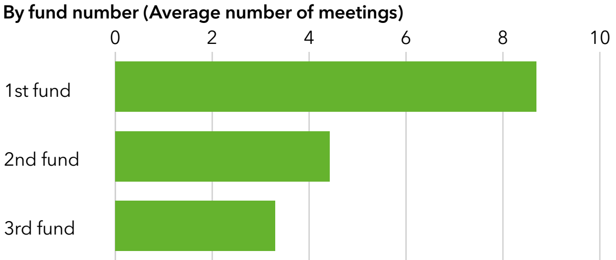
For investors that ultimately committed, how many meetings (including conference calls) did you have with them on average? (%)



What is the total committed capital to all your active funds? (%)



By fund number (Average number of meetings)



> *"Testing the waters with a half-baked strategy is not a winning method"*
>
> **ARTHUR ANDERSEN**
> **Ropes & Gray**

them to demonstrate what a group with its current team and strategy can actually accomplish," says Matthew Chase, an investment funds partner at law firm Latham & Watkins. "And that's been useful in eventually earning a close on that debut fund."

For those that closed a fund this year, it took them roughly the same time as it did in previous years, but there is a selection bias since these were all groups that did manage to reach their target.

However, there was a slight uptick in the amount of committed capital, with a seven-point increase in the percentage of funds with between $500 million and $1 billion of committed capital, and a 12-point rise in those with $1 billion or more, although this may be due to those 'unicorns' that wooed LPs easily. Of this capital, a greater proportion is coming from pension funds, constituting 21 percent of the capital raised among emerging managers, up from just 5 percent last year.

Above all, patience

Market participants agree that while fortunes can vary wildly among emerging GPs, fundraising is taking longer and getting more expensive. "Fundraising periods have been getting longer," says Chase. "And it's requiring more handholding with investors during due diligence, so they can truly understand the track record, team and strategy of a new manager."

One of the frequent blind spots lawyers and placement agents cite among new managers is how long fundraising takes now. "One of my colleagues mapped the process to securing commitments and it became 50 Steps to a Sale, knowing that in some cases it can take even longer," says Sarah Sandstrom, a partner at placement agent Campbell Lutyens.

Sandstrom also notes that a good meeting with a potential LP is only a very early step to landing a commitment. "There's a long way to go from

What was the most challenging aspect of the fundraise?

- Worst fundraising market (2022-24) since 2009
- Demonstrating institutional crediblity with a highly innovative investment strategy in a non-core market
- Limited track record to market
- Denominator effect
- Time away from doing deals
- Capital-constrained environment in an era where liquidity was prioritized and allocation to alternatives was slashed
- LPs demonstrating interest then pulling back for internal reasons; lots of false starts
- Requires lots of meetings/ Zoom calls
- Staffing the fundraise while fulfilling existing portfolio management duties
- Going solo without a placement agent or pre-existing investor relationship during covid-19
- Gaining traction as a first-time manager
- Covid
- LP liquidity issues

Source for all data: Buyouts Emerging Manager Survey 2024

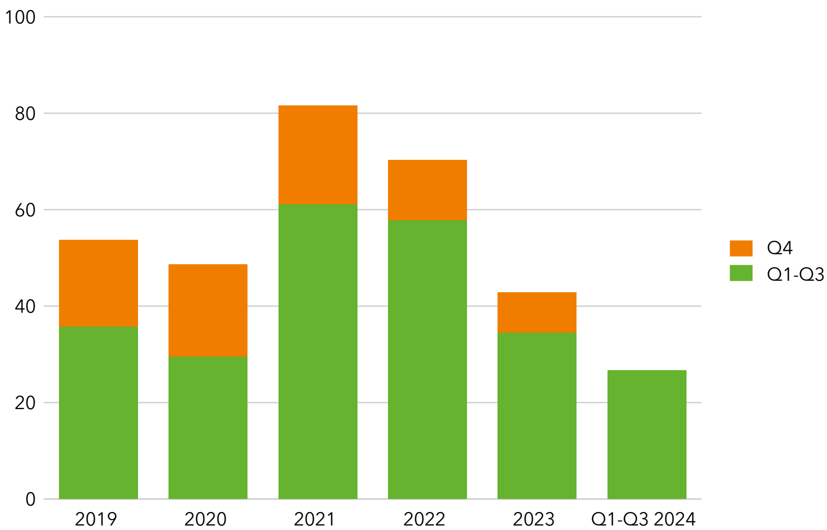
that 'good meeting' to the signing of documents."

Unfortunately for managers, this kind of placement agent expertise isn't getting any cheaper.

"Placement agents used to charge a monthly retainer of around $5,000, but now those rates for large placement agents being engaged by small and medium-sized managers can hover around $25,000-$40,000 a month," says Joseph Suh, a partner at law firm Reed Smith. "And most striking is that these retainers usually offset dollar for dollar when the placement was successful, but now larger agents no longer offer such offsets at all, at least as a starting point."

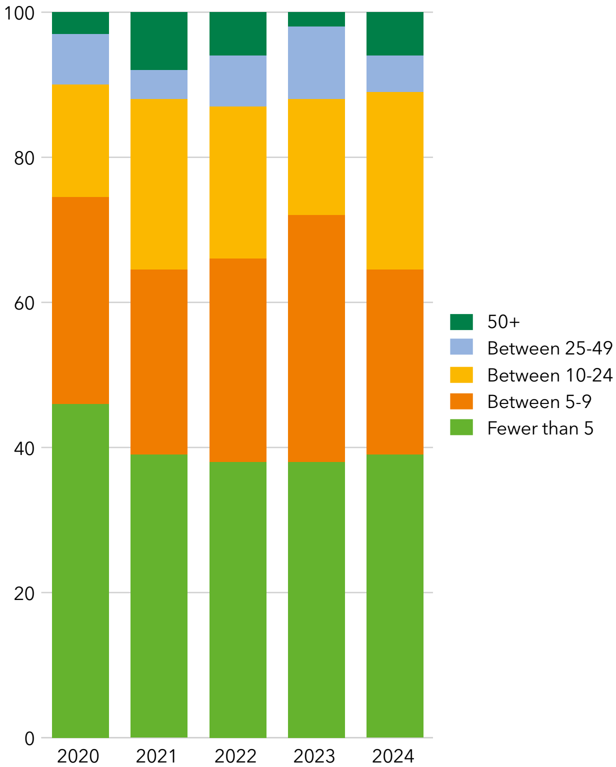
Further, managers are often

Private equity first-time funds capital raised by close year ($bn)

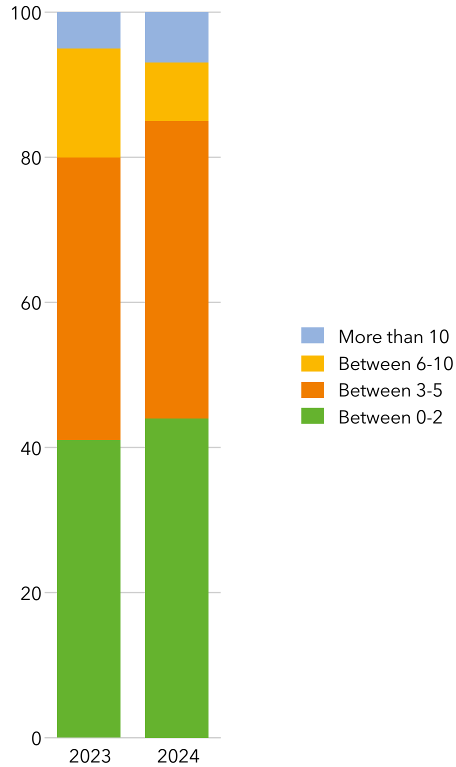


Source: Buyouts

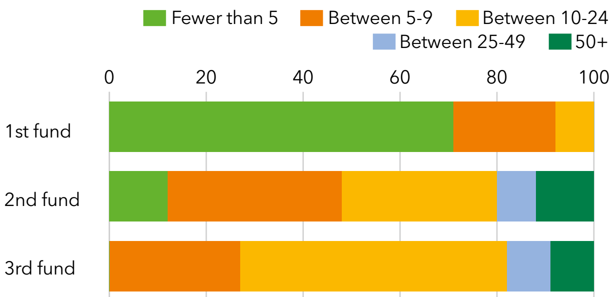
How many active portfolio companies do you have? (%)



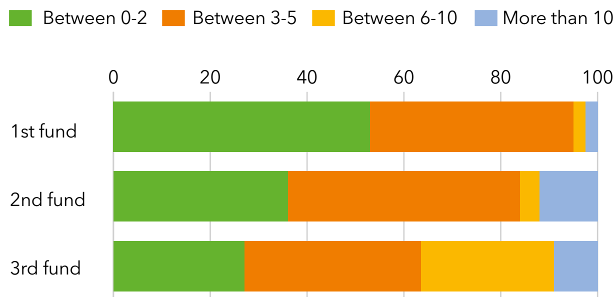
How many new investments do you anticipate making over the next year? (%)



By fund number (%)



By fund number (%)



Source for all data: Buyouts Emerging Manager Survey 2024

encouraged to tap placement agents earlier and earlier. "If emerging managers are going to work with an intermediary, they should get them engaged soon enough to help them craft a truly compelling narrative around their value proposition," says Arthur Andersen, a partner at law firm Ropes & Gray. However, 58 percent of survey respondents did not use a placement agent.

With or without an agent, a compelling story is a necessity. "Emerging managers can pivot with LP feedback, but they need a business plan and strategy with internal processes in development or being put in place," says Andersen. "Testing the waters with a half-baked strategy is not a winning method for new managers right now."

SBA-driven silver linings

There are some recent developments that might help fundraising tallies, beyond a broader rebound. Last August, the US Small Business Administration (SBA) announced a set of reforms to increase the access of private equity emerging managers, among other groups.

"They're essentially now in the business of providing matching capital to lower mid-market equity strategies," says Sheryl Mejia, a managing partner at Steward Asset Management. "Traditionally, it's been debt with a little bit of equity attached, but it's full-out equity or debt strategies now. And their licensing volume has more than doubled."

It may not fuel a boom, but it is another sign that the broader world sees the value of emerging managers.

Negotiating for performance

Even in a market this competitive, investors are aiming for terms that will not hinder any manager's ability to deliver returns

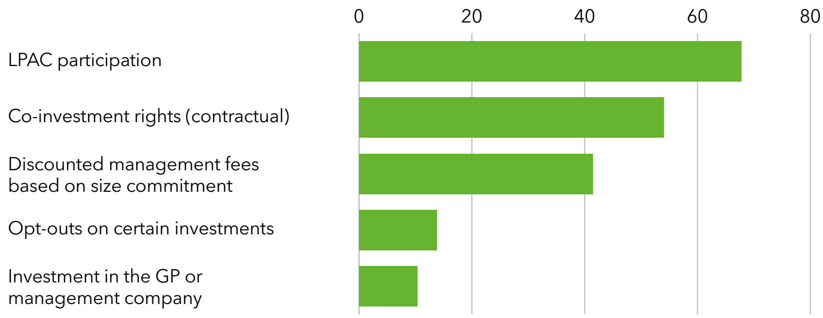
Given the story around emerging GP fundraising, it seems safe to assume LPs are demanding all kinds of discounts and carve-outs. However, in reality, investors know they need to set up new managers to succeed, and steep cuts to management fees or owning a stake in the management company can hinder that. LPs do of course have their own preferences, especially around co-investments, but they are negotiating to find the best balance between those and any firm's ability to perform.

For example, according to the *Buyouts Emerging Manager Survey*, conducted in partnership with Gen II Fund Services, 41 percent of respondents offered discounted management fees based on the size of commitment, down from 48 percent in last year's survey, and 54 percent back in 2020. Further, only 3 percent of respondents report receiving a great deal of pressure to lower fees, and 40 percent say they received no pressure at all.

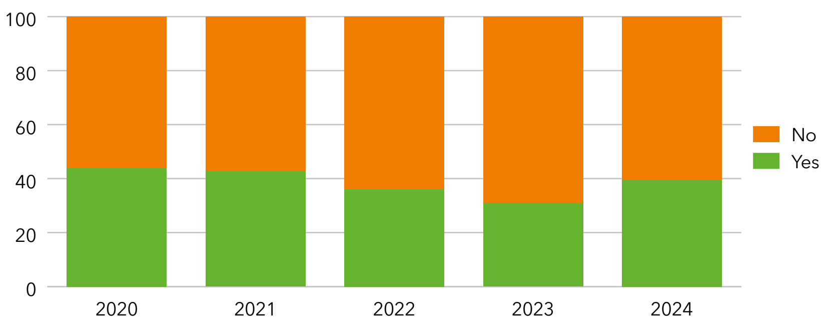
"LPs are pressuring more established managers on fees because LPs understand that emerging managers need those fees to launch their firm," says Sarah Sandstrom, a partner with the placement agent Campbell Lutyens.

Yet, when it comes to anchor investors, discounted fees are by far the

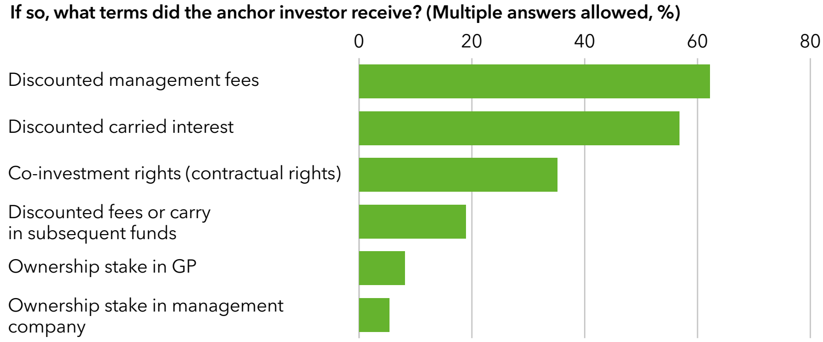
Which of the following terms did you offer/provide to investors? (Multiple answers allowed, %)



Did you have an anchor investor with more favorable economic terms? (%)

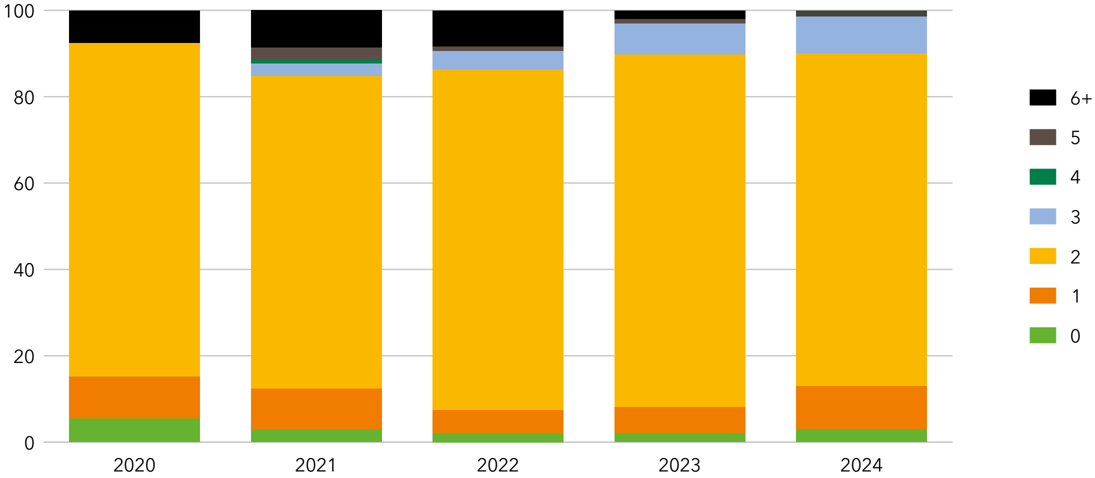


If so, what terms did the anchor investor receive? (Multiple answers allowed, %)

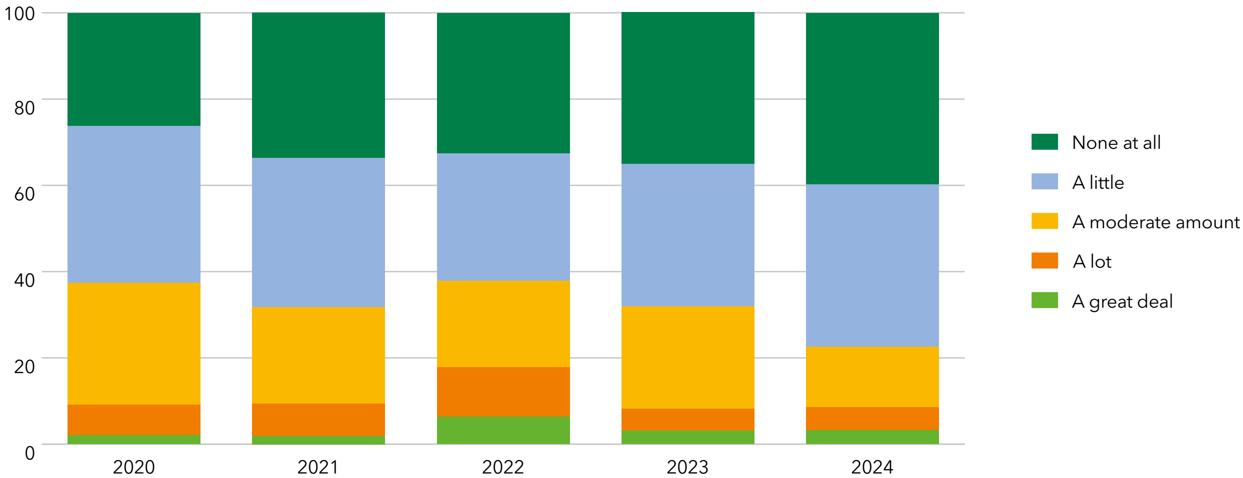


Source for all data: Buyouts Emerging Manager Survey 2024

What management fee as a percentage have you asked for in your fund? (%)



Do you receive pressure from investors regarding fees? (%)



most popular perk, with 62 percent of manager respondents offering anchors a lower rate.

However, anchor investors are no longer snagging stakes in the management company or GP – only 5 percent took a piece of the management company, down from 18 percent in 2020; and 8 percent won a stake in the GP, down from 33 percent in 2020.

Perhaps the most fascinating result is that a clear majority of managers are not giving any favorable terms to their anchor investors, with 61 percent reporting that their anchors have no more favorable terms than any other LP, which is surprising given the difficulty in launching these days.

Market participants stress that LPs know that emerging managers are in a different category to more established peers. "[Our anchor investor] had a partnership-oriented viewpoint," says Beau Thomas, managing partner at Agellus Capital. "Their support also allowed us to be selective with our LP base, as our investor agreed that we're building our fund to execute our investment strategy, not the other way around."

A similar rationale appears in a lack of interest in management company stakes. "Some LPs are evolving to say that they're seeding a manager to launch them, and don't require a stake in the management company," says Eric Requenez, a partner at law firm Ropes & Gray. "Because they're betting on that manager, but will also restrict the manager's ability to sell that stake down the line."

However, LPs are still laser-focused on co-investment rights – one manager admitted to turning away several investors that wanted a first look on opportunities and other perks around co-investments, which would have hindered its ability to welcome other LPs. Investors are also increasingly sensitive to fellow LPs having better terms than their own.

Managers are finding ways to sweeten the offer. "We've placed a 10 percent preferred return in our fund docs," says Andrew Albert, co-founder of Channel Equity Partners. "We want to put our money where our mouth is."

Perhaps that is a term that LPs will always appreciate.

Q&A

New Catalyst Strategic Partners offers seed and growth capital to help launch and scale emerging managers. Founder and managing partner, Jason Howard, shares his view of the current market

Q How's the market for emerging managers today?

A Let me start with how we define emerging managers. They are groups on their first, second or third fund with fund sizes under $2 billion in AUM. If you look at this portion of the market, LPs continue to see performance and alpha in emerging managers, and see the industrial logic of managers wanting to launch their own firms, either due to succession, governance or economic issues, or the manager seeking to establish a different culture compared to their current firms.

There's a recurring theme of managers wanting to return their focus to investment performance rather than asset gathering. That's driving new entrants into the emerging managers space. This means LPs have more choices than ever, which is good, but can be challenging to manage and sift through. This dynamic often results in LPs deferring commitment decisions. While these challenges exist, I believe this is an ideal time for exceptional managers to launch.

Q And what do those exceptional managers need to do to launch?

A GPs often need $5 million-$10 million of working capital to launch a fund. That's driven by a few factors. GPs need to show up to LPs ready and in business, with a strong investment team, robust deal pipeline and operational infrastructure. They need to be prepared to fund 1-2 percent GP commitments. GPs also need to have spent time with a sufficient number of potential LPs that are likely to find their strategies compelling. This takes time and working capital, often costing several hundred thousand dollars a month to launch and run a private equity firm. As fundraising periods stretch to 24 months, those costs add up.

> *"GPs need to show up to LPs ready and in business"*

Q Are there common blind spots that even the best emerging managers can miss?

A I'll frame a couple of key blind spots we see in the market as the difference between deal execution and fund management. Sometimes emerging managers don't implement strategies from the outset to manage the gross-to-net performance spread on their funds. I've seen many emerging GPs generate attractive gross performance, but suboptimal net performance as a result.

Portfolio construction is another area. At times, GPs over allocate to specific deals, beyond what's prudent in the portfolio. I've also seen very concentrated portfolios, which makes sense, given a GP's desire to focus on a few companies, but they also need to consider risk mitigation in case assets underperform.

But overall, these GPs are the equivalent of world-class surgeons that have simply decided to move from a physician group of a hundred, to practice their craft with a group of five. And that's what makes these groups so attractive to us, and to many LPs. ■

The lynchpin principle

While still taking advantage of outsourcing options, emerging mangers are frequently hiring internal talent to manage third-party operational support

How many months in advance of the first closing did you engage with, or do you anticipate engaging with, the following professional services firms?

Source for all data: Buyouts Emerging Manager Survey 2024

LPs want to ensure that any dealmaking is complemented by professional-grade support around investor relations, human resources, fund administration and legal issues, making it harder for new managers to rely on the Silicon Valley recipe of a garage and a giant tub of cheese puffs. So, first-timers have addressed this demand by tapping service providers to fill the roles they cannot afford to have in-house – and these outsourced solutions have only improved with time.

The *Buyouts Emerging Manager Survey*, conducted in partnership with Gen II Fund Services, reveals a trend among emerging managers to engage key service providers earlier than before. In 2020, placement agents were typically hired about six months before the first close; in the latest survey, that timeline has extended to nearly eight months. The same is true for fund administrators and compliance consultants.

They are selecting those providers according to experience and expertise in similar funds (62 percent of respondents), and by referrals from trusted sources (54 percent). Notably, the number of respondents that listed these two factors as incredibly important nearly doubled in 2023 and has remained consistent since then.

Multiple GPs have at least one member of the team dedicated to managing outsourced functions, in most cases by first close for the fund. Although GPs make it a priority to bulk up their IR staffing to better manage those crucial relationships, "if you're leveraging a fund administrator for investor communications, that conversation may feel too transactional for LPs," says Jordan Bastable, co-founder and managing partner of LongWater Opportunities.

"We established an investor relations team dedicated to fostering deeper, more personalized partnerships with our investor partners, where we can provide value beyond the IRR."

One common theme among emerging managers is just how much operations matter. "Performance and our operations are what won us our anchor investor," says Senofer Mendoza, founder of Mendoza Ventures. "We always aspired to be an institutional firm, and we did that by taking a very hands-on approach from the very beginning to everything we outsourced, even conducting our own audits alongside our providers."

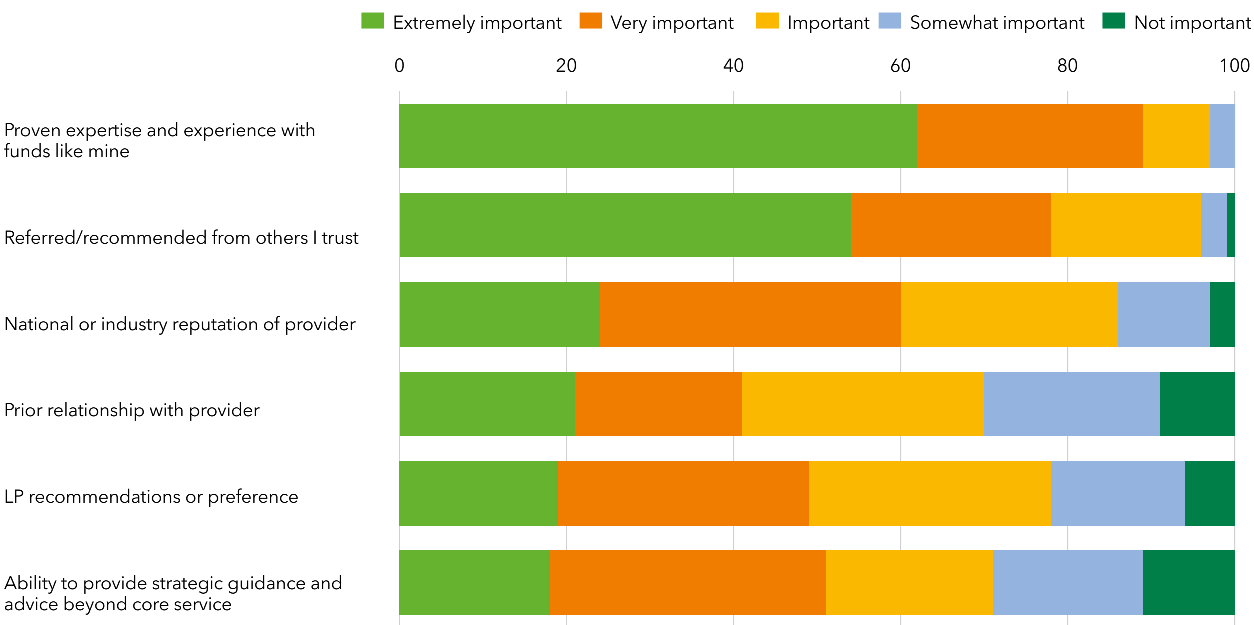
While no one is making commitments due to operations (yet), GPs are making it a priority to assure their investors these tasks are handled.

AI is capturing emerging managers' attention

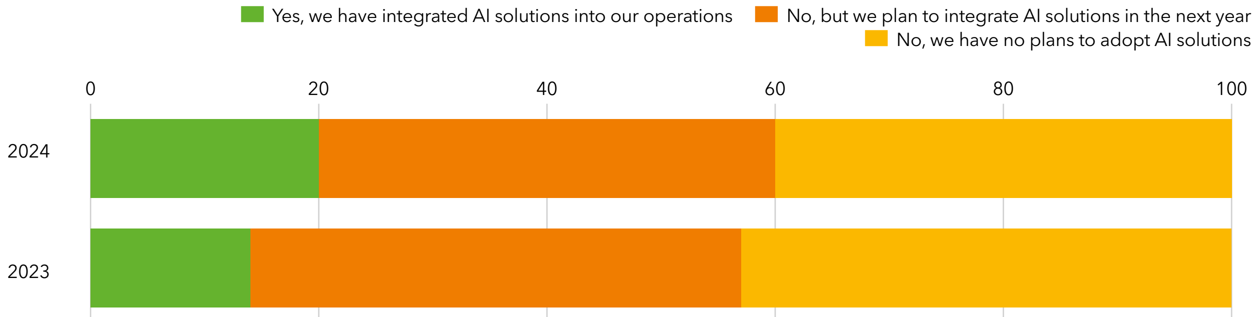
The adoption of AI solutions signals a shift in how emerging managers approach challenges

Twenty percent of respondents report having already integrated artificial intelligence solutions into their operations – up from 14 percent in the 2023 survey – and 41 percent are planning to integrate such solutions within the year. However, the consensus among market participants is that these AI projects are being pursued by providers and not internal staff. Blackstone can afford an entire data science team, but that is out of reach for a firm with a staff of 10.

How important are the following factors in choosing service providers? (%)



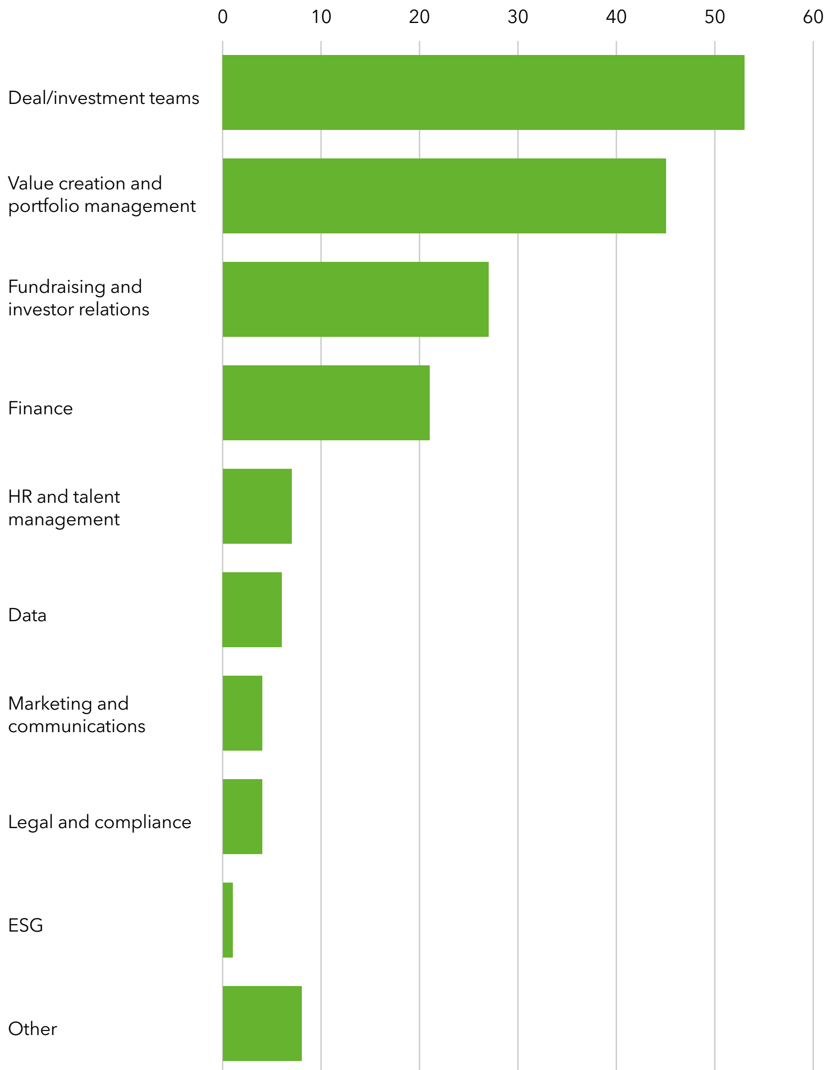
Have you integrated any AI-based solutions into your operations? (%)



Building the bench

Emerging managers are still hunting down investment and value-creation skills, all while actively building their own talent pipelines

In which three areas is it most difficult to hire talent currently?



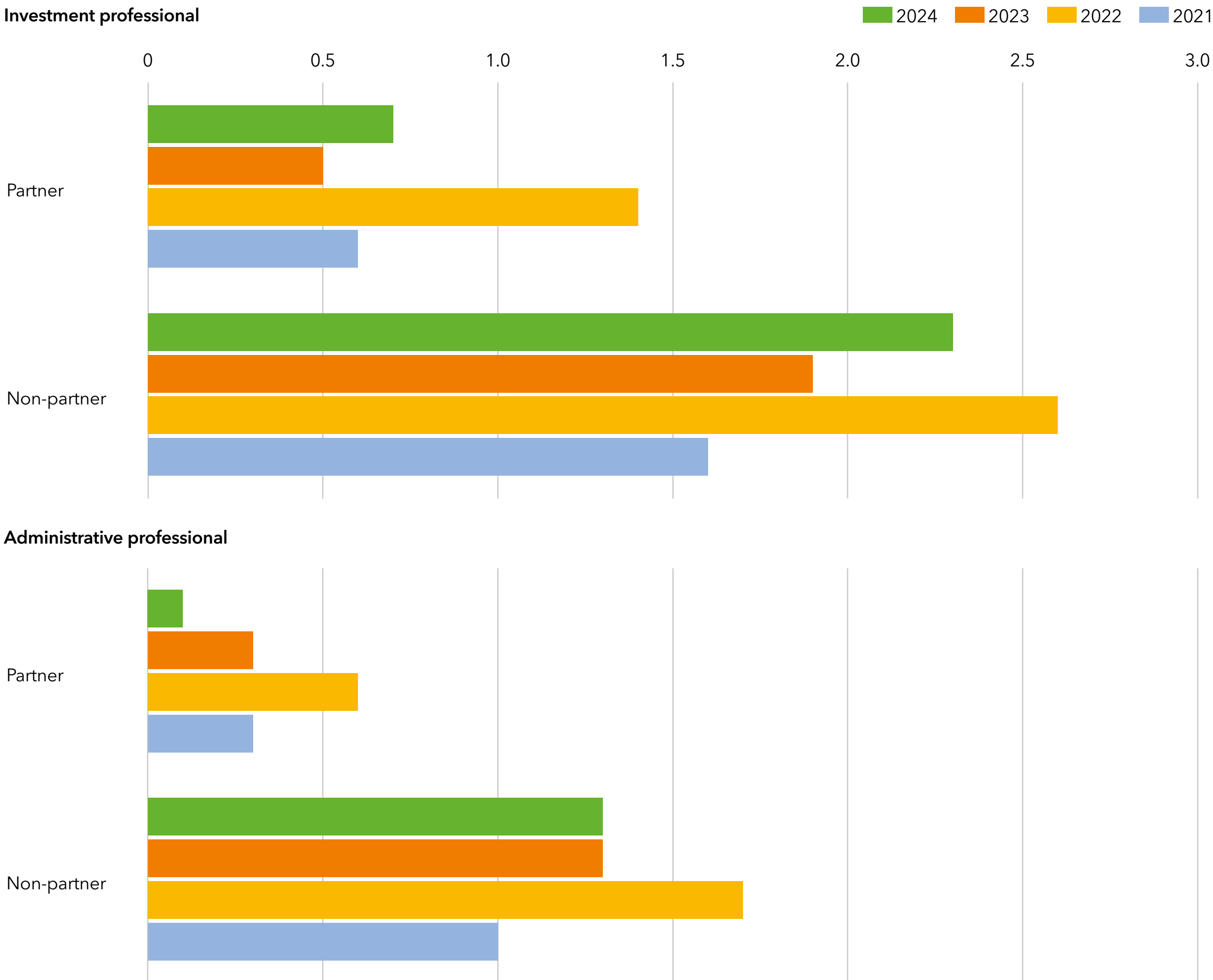
Source for all data: Buyouts Emerging Manager Survey 2024

Emerging managers are not just competing with their larger, more established peers for capital, they are also vying for talent. That whiz kid with the Ivy League pedigree can have their pick of those top-tier funds, so why would they cast their lot with a GP that's only raised a small fund? Nowadays, emerging managers are finding new answers to that question.

The *Buyouts Emerging Manager Survey*, conducted in partnership with Gen II Fund Services, finds that emerging managers are having an easier time sourcing talent, and this year they've been bulking up on investment professionals: 29 percent report having 11 or more investment staff in their team, up from 14 percent last year. But the biggest growth has been among non-partner investment professionals.

This is unsurprising given that most new funds launch with a core group of veterans, so the first new deal hires naturally will be more junior, which has the virtue of being less costly too. That doesn't mean these managers are never in the market for senior dealmaking acumen and value creation experts, whether they be operating partners or ex-CEOs that are on call, but these are

How many staff do you plan to add at the following levels and roles over the next year?



the areas proving hardest to fill, according to the survey data.

"The traditional mid-level, or entry-level deal team role has gotten easier to find, as lots of professionals are not happy with the trajectory of many up-market funds," says Ryan Anthony, co-founder of Longshore Capital Partners. "That's loosened the hiring market a bit, but it's still very competitive for more experienced operating team professionals or company executives."

As a result, many managers are upgrading their talent development processes to nurture the skills of the next generation in-house. Senofer Mendoza, founder of Mendoza Ventures, developed a fellowship program where underrepresented MBAs learn the business for a semester or two.

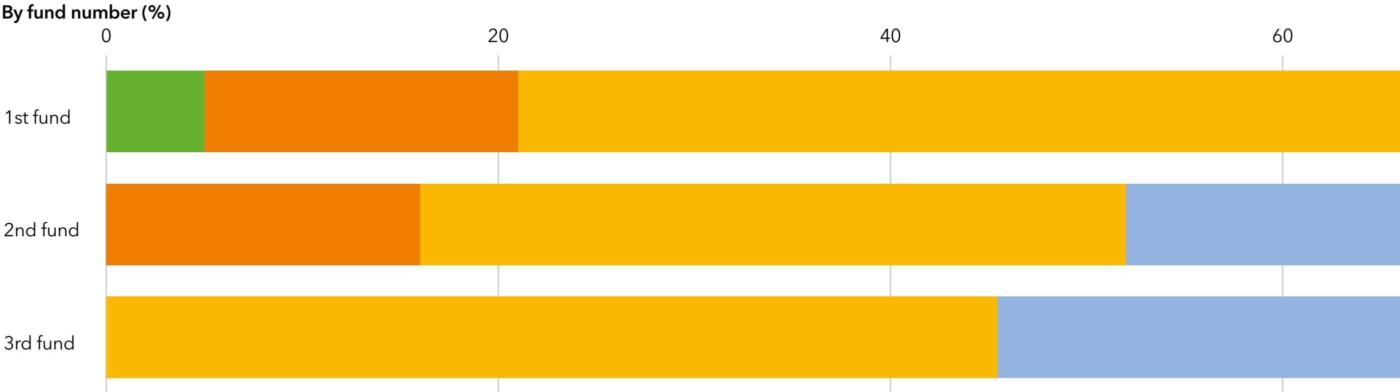
"We have them sit in on investment committees and they help us oversee our inbound pipeline of opportunities, often getting pitched by countless start-ups," says Mendoza. "Unlike other traditional internships, they're able to direct their learning experience into actual work, and they develop a real pattern recognition in fundraising or deploying capital." Mendoza Ventures has also prioritized transparency in all its operations, which has proven to be a major asset in retaining talent.

Some emerging managers are shaking up their associate programs as well. "We don't position our associate role as a two-year program," says Brooke Coburn, founder of Capital Meridian Partners. "This is an apprenticeship business, so we invest to give them a world-class development experience and if they show promise, there is a path to partner. For high-potential individuals willing to bet on themselves, that's a compelling career opportunity."

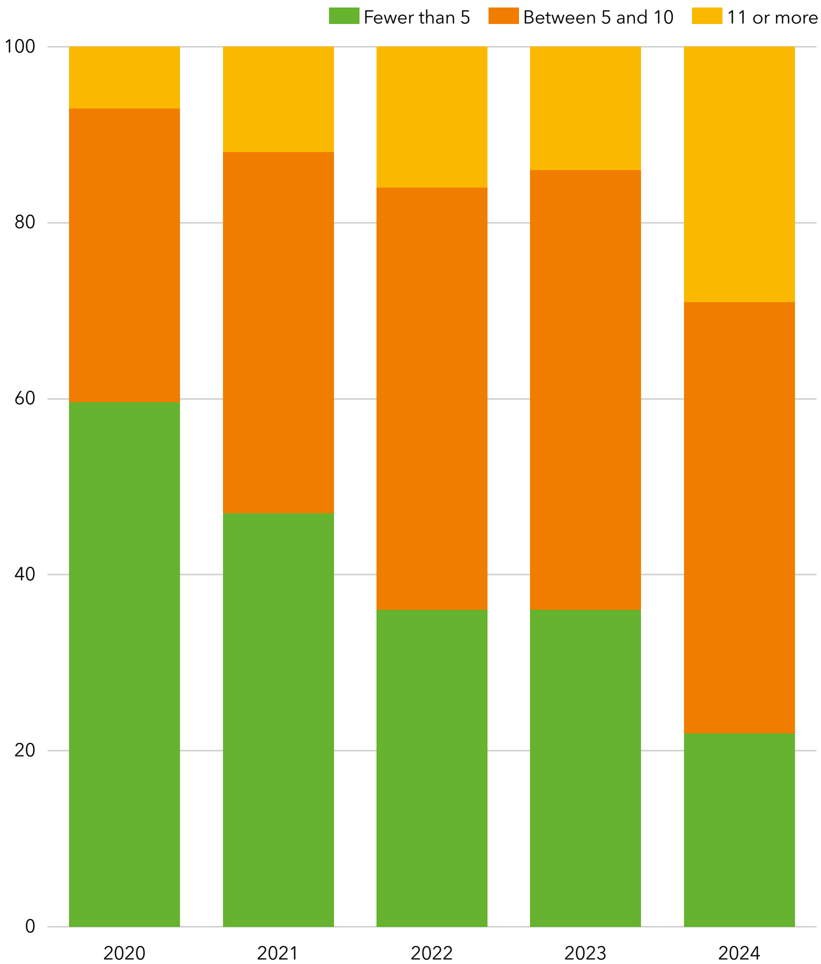
The talent war may not be as intense as it once was, but there is a sense that emerging managers are still systemically disadvantaged, so they are doing all they can to develop their own star system. ■

Over the past 12 months, has it become more difficult to attract and hire talent? (%)

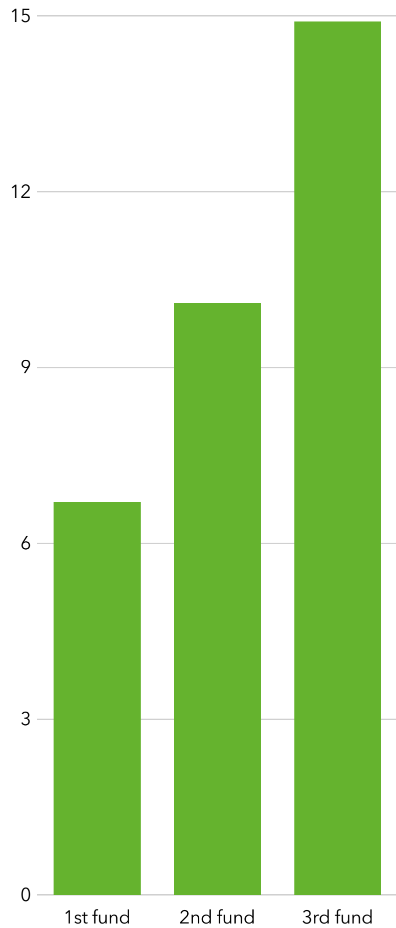
By fund number (%)



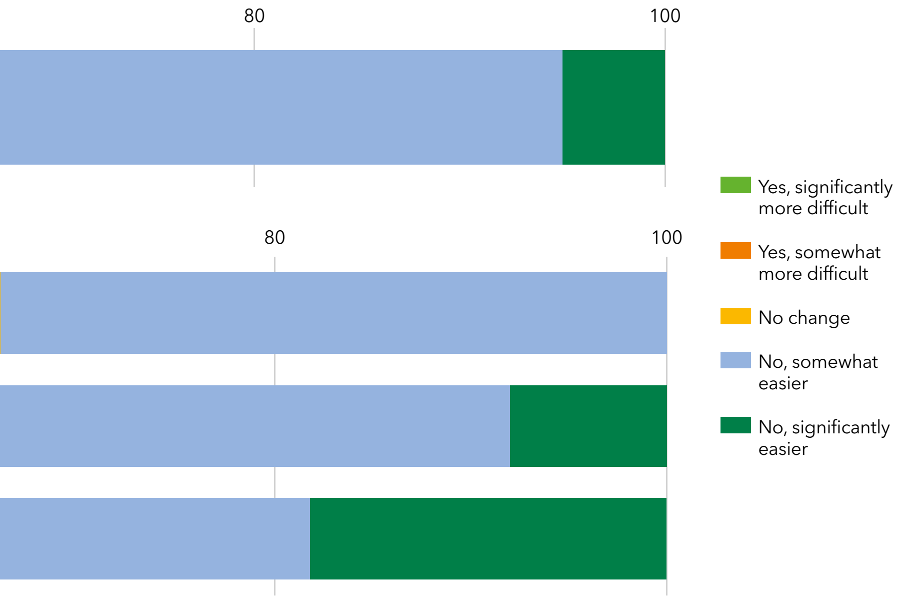
How many investment professionals work for your firm? (%)



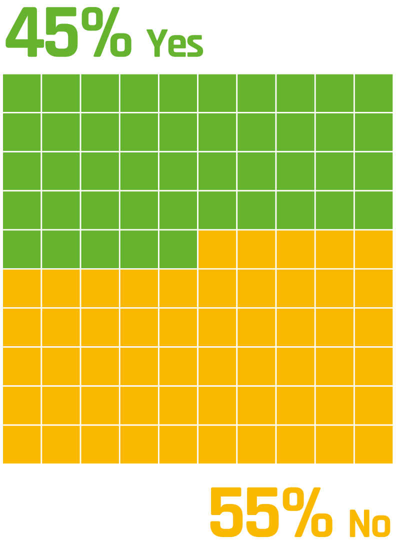
Average number of investment professionals, by fund number



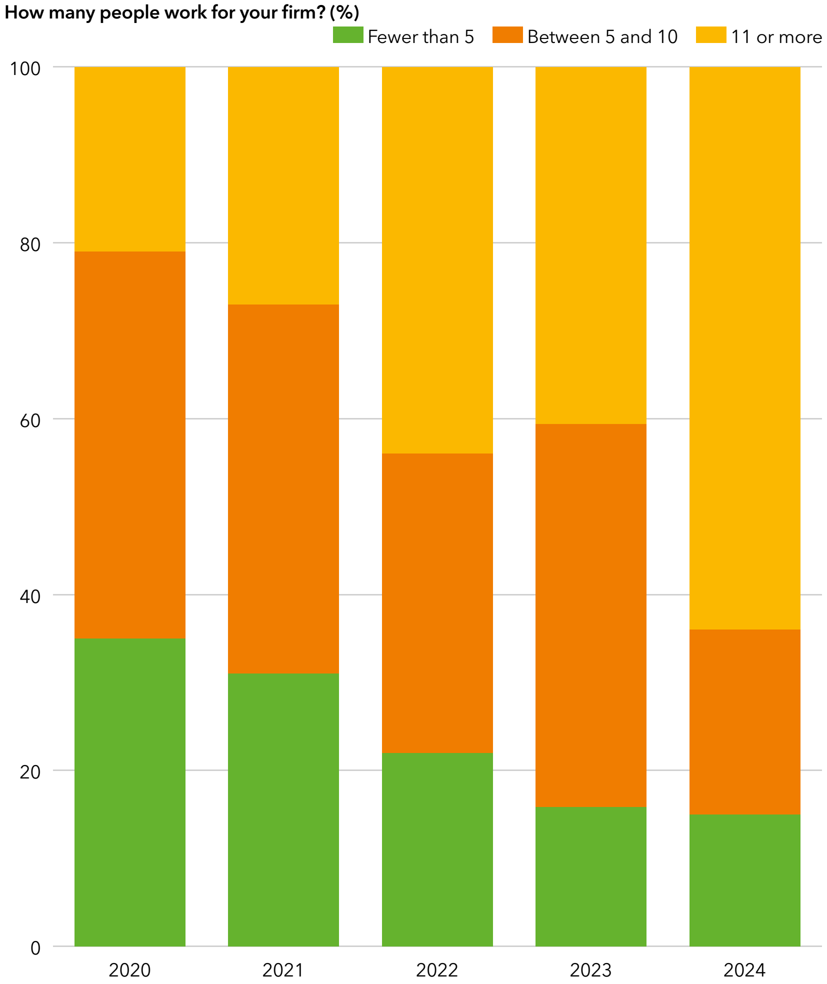
Source for all data: Buyouts Emerging Manager Survey 2024



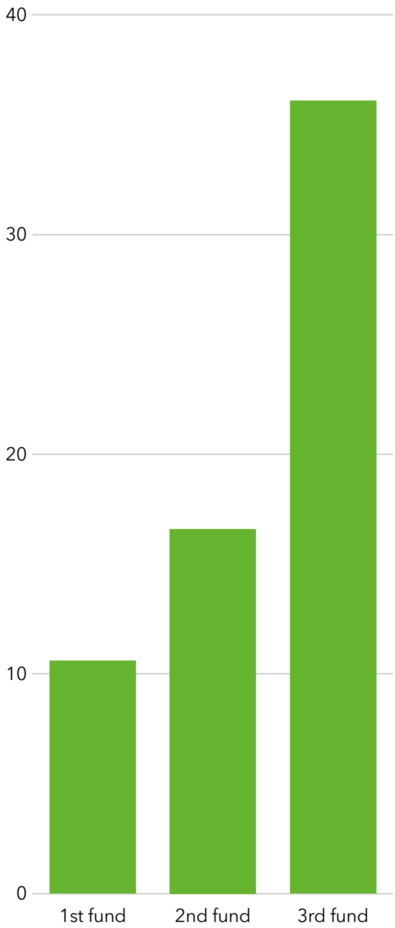
Do you have a succession plan in place? (%)



How many people work for your firm? (%)



Average number of employees, by fund number



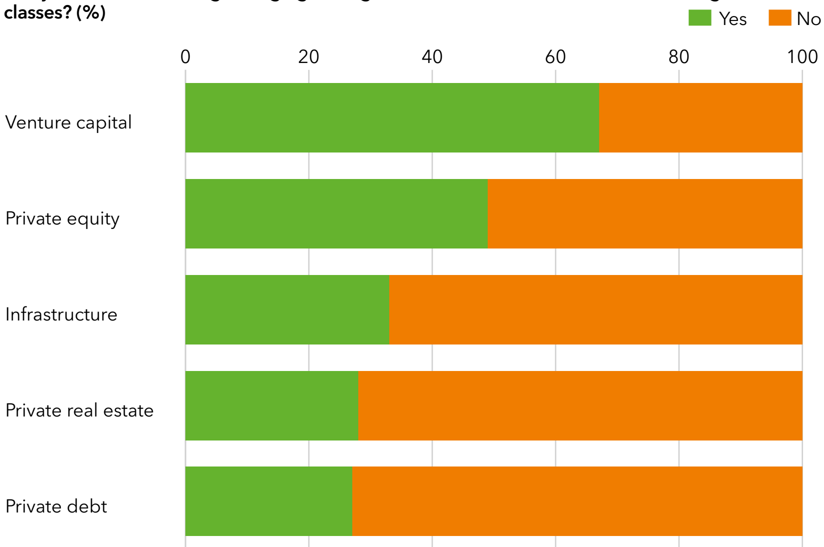
LP views

Attracting investor backing remains a tough task for emerging managers

Affiliate title *Private Equity International's LP Perspectives 2025 Study* captures the sentiments of global private markets investors across all the main asset classes for the year ahead.

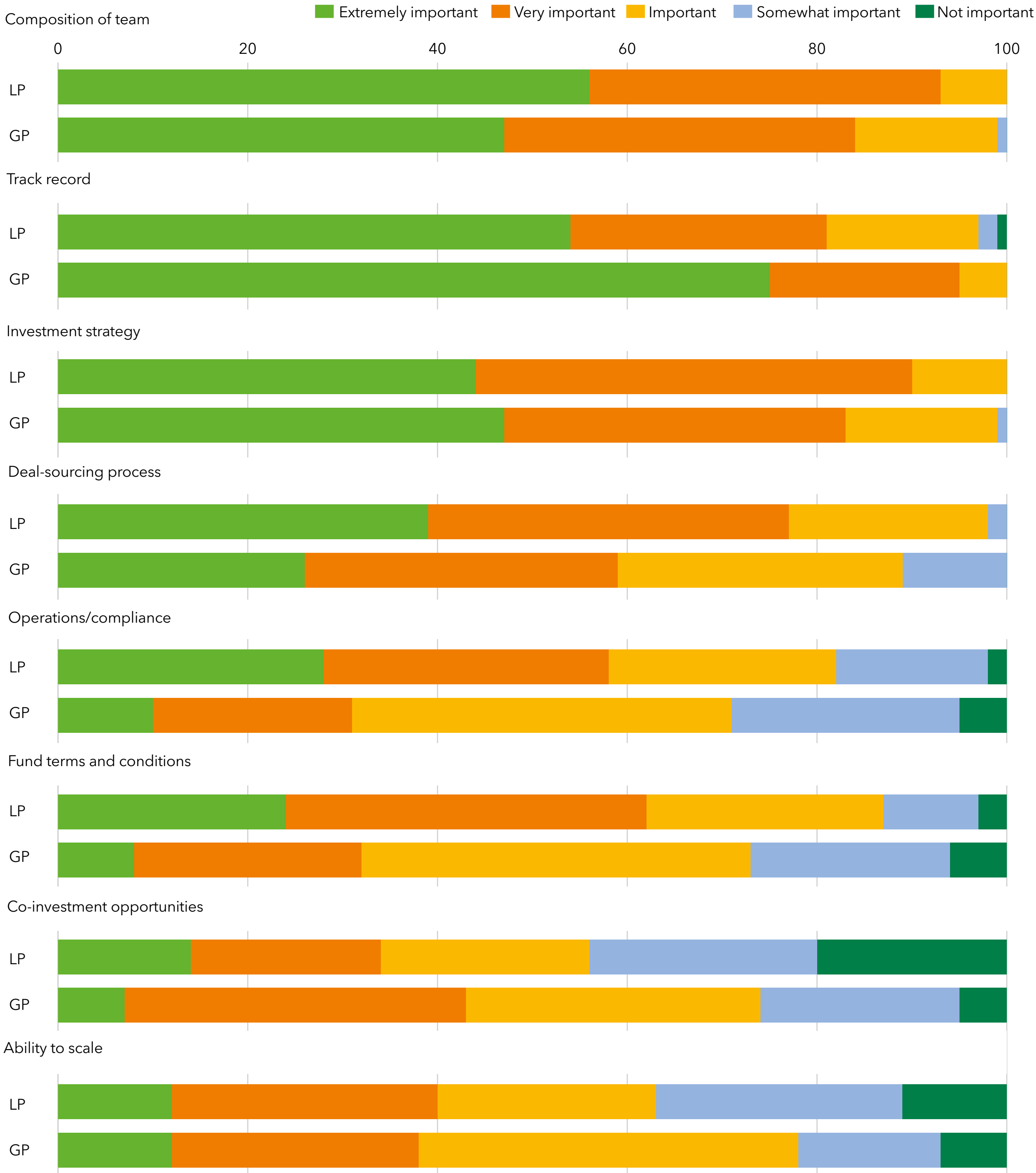
A total of 107 LPs answered 65 questions on a broad spectrum of topics from preferred allocation, regional strategies and performance expectations to macroeconomic and geopolitical concerns, ESG progress and fund due diligence. Field work was carried out between September 5 and October 7, 2024.

Will you consider backing emerging managers in the next 12 months in the following asset classes? (%)



How do you perceive market sentiment around emerging managers right now? (%)

How important are the following factors when evaluating an emerging manager fund? (%)



Source for all data: Private Equity International's LP Perspectives 2025 Study/Buyouts Emerging Manager Study

This year, LP respondents were also asked to reveal their attitude toward emerging managers. The results are presented in the charts here. Where relevant, LP views from the *Perspectives* study are compared with GP responses to the same questions posed in the *Emerging Managers* survey.

Findings indicate that GPs and LPs agree that established managers attract the bulk of capital and that emerging managers led by private equity executives with previous experience at a top-tier firm can more easily raise capital in the current market. In terms of asset class, LPs are most likely to consider allocating capital to emerging managers in the venture capital space. ■

Company Overview

Gen II is a leading independent fund administration provider for private capital asset managers and investors. Distinguished by its bespoke service offerings and robust technological infrastructure, the company has grown to become one of the largest independent private capital fund administrators since its inception in 2009, and now oversees more than $1 trillion of private fund capital.

Gen II's transatlantic operational reach is redefining excellence in the fund administration sector enabling it to provide unparalleled service capabilities to fund managers and investors globally. The company helps GPs to navigate complex international markets and regulations whilst effectively managing their operational infrastructure, financial reporting, and investor communications.

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Founded 2009

Gen II Emerging Managers Services

Gen II is the largest private equity fund administrator in the United States.

source: Convergence

Administering
$1T+
Private Fund Capital

Client Retention
99%

Helped Launch
100+
Emerging Managers & Spin-out Groups

#1
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Source: Preqin

Reporting to
50,000+
Investors for Our Clients

Servicing
8,000+
Fund Entities

Gen II

Q&A

Unity Partners' secret to success as an emerging manager may be found in its relentlessly consistent approach to its strategy and values, says its CEO, John Block

Q What is Unity Partners' strategy?

A Three words: building better together. Building world-class platforms with ambitious leaders. Our 'Propel' team brings this to life by focusing on value acceleration alongside the leaders of our portfolio companies. We want constant improvement, operationally, structurally, financially and most importantly, culturally. A focus on ownership culture, delivered through employee ownership programs, which better align employees and enterprises. 'Together' because we want a sense of partnership with all our stakeholders, creating platforms that can flourish as one, rather than as a group of disparate units slapped together and sold in a rush.

So, partnering with ambitious leaders, partnering through M&A to accelerate growth, and partnering people with technology to solve recurring and essential needs. And then propelling organic growth and platform integration through investments in people, processes, and systems.

"We want a sense of partnership with all our stakeholders, creating platforms that can flourish as one"

Q How have your deals reflected that approach?

A We partnered with an ambitious team in the tax and accounting advisory space. We liked that market, and the business focused on high-net-worth and ultra-high-net-worth tax planning. We quickly got to work helping them implement a new technology system. Eighteen months in, we've completed five acquisitions. Our second investment is a pool services business in Texas, a recurring services business, with weekly service work. We've done 25 plus small acquisitions and established a platform throughout Texas. We're really excited about it because we're driving organic growth as they have invested in technology and scalable infrastructure.

Another investment is in a commercial property and casualty insurance brokerage platform, another recurring services business, where we share a vision with the CEO, CFO and CTO to acquire small insurance agencies and build an integrated platform with a technology-first mindset. All of these share the characteristics of industries with high degrees of recurring revenue in essential services.

Q What's your approach to staffing and resources from the front to back office?

A We have an awesome team of 12 folks. By next summer, we might be up to 16. The leadership group includes Bryan Adams, chairman of Unity, Jim Sharpe, leading the value acceleration team, Propel, and Peter Cozzi, who has led many of our early investments.

Recently, we've started building the firm's infrastructure by hiring Nate Arnold as a VP of finance. We've got a third-party administrator for accounting and compliance, with a PEO (Professional Employer Orgianization) tackling HR, but we fully expect to build out our operations from there. Honestly, we're excited to see how we grow by sticking to our 'building better together' mantra, which is the foundation for how resilient our approach can be in any kind of market. ■