IPEM 22, 23, 24 JANUARY 2019
PALAIS DES FESTIVALS - CANNES - FRANCE

London, 3 December 2018

Private equity: the continuous reinvention of a value proposition

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The current context of abundant liquidity is pushing private equity to unremittingly explore new sources of value creation. As the first step toward transforming a system based on publicly held, intermediated capital into one of private capital, this continuous fracking of a previously off-market investment universe sets the stage for a reshuffling of players in the sector, who are under pressure to explore hybrid models and new ways of interacting with each other.

Bridges between businesses, hybridization of models, reversals of power relationships... The value chain of unlisted securities has experience radical change in recent years. While the marketing of funds still revolves around selling a certain notion of consistency and unity of assurances, reality paints quite a different picture. Let's take a quick look at the situation. Traditionally, investors (LPs) entrust funds to management companies (GPs), which pool them to invest in companies, using their influence to capture an increase in shareholder value by accelerating portfolio companies' transformation (strategic repositioning, optimisation of operational efficiency, geographical deployment, etc.).

While this blueprint clearly remains valid, it is no longer the only game in town. Let's start with the GPs themselves. Coming primarily from a background in buyouts, these investment management companies are gradually transforming their business models to become platforms for providing protean solutions to meet a wide range of financing and investment needs, in some cases including private debt and infrastructure financing. By placing the private equity asset class on a new playing field, this one-stop-shop strategy pushes industry players to aggressively pursue a critical mass that keeps increasing, calling into question the viability of certain niche models that are now too restrictive.

A continuous process of 'fracking' that is turning private markets into a quasi-liquid asset class

Meanwhile, a growing number of LPs are bypassing GPs and investing directly in both the debt and capital of companies. For management companies, this means redefining and asserting a value proposition threatened by this new competition from their own clients. Those pioneering investors who have decided to take matters into their own hands must focus on building in-house teams of seasoned professionals. As for companies, they are themselves increasingly inclined to finance the development of other—generally less mature—firms, using corporate ventures as outposts for detecting the seeds of the disruption within their own industries. Finally, traditional asset managers are setting up dedicated teams, following in the footsteps of certain hedge funds, prompting a semantic shift from the traditional notion of 'unlisted securities' to the more ambivalent notion of 'real assets'.

Among the many drivers of this hybridization, there is one that accounts for the lion's share of this change: the vast reservoirs of liquidity to be invested throughout the world in a context of declining yields, ultra-sophisticated methods, saturation of deal flow and excess recourse to the capital markets, now too restrictive in the current 'hunt for yield' context. This produces runoff throughout the economy that is transforming mere stress fractures into value creation opportunities, almost into asset classes. Combined with a boom in marketplaces and the increased fluidity of secondary transactions, this kind of continuous 'fracking', which leads players in the sector to constantly explore new investment opportunities, facilitates access to previously off-market assets to an unprecedented extent. The result: increasingly illiquid assets that are more and more... liquid!

A pioneering sector in the ongoing transformation of capitalism

Implications for the industry are considerable. From a clear and vertical chain model, its organisation is gradually moving towards the model of a more organic ecosystem, where every member can be simultaneously partner, customer and competitor to others. Rich in opportunities, this change nonetheless brings many challenges. More than ever, the stakeholders in this constantly changing ecosystem must interact with each other, build bridges, join new types of networks and test new combinations, at the risk of being pushed out of the deal flow. To do this, private equity must doubtless rely on vertical associative networks, but must also develop around open exchange platforms that are conducive to informal interactions and creativity.

The ongoing reflection on how the industry should best be structured, like the need for dialogue within it, are all the more crucial as they go beyond the sole interest of its actors. The shift more broadly indicates a transformation from "public" and intermediated capitalism to a "private" capitalism, whose transformative power it illustrates. No less than the transformation of capitalism is at stake here.

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