Mantras change but the fundamentals

Veteran financier Jon Moulton has been involved in buyouts, turnarounds and venture capital since 1979 with firms such as CVC, Permira, Apax, Alchemy and, most recently, Better Capital, where he has been the chair since 2009

Over the decades you can see that some things have not changed much. Many pundits, somehow, get away with great repetition.

One leading character at a major UK firm was a steady source of expensive drinks for me at conferences. The bet I offered, often to members of his own panel, was that he would mention his time at Boston Consulting and at Oxford within 10 minutes of the start of a panel session. He never let me down. Profit can be made from spotting repetition.

He has sadly moved on, but his CV still shows the same picture.

Many panel sessions at PE conferences are indistinguishable from each other in content. Some of the mantras never seem to lose their attractiveness to speakers.

"It is not just about being in the asset class, it is about being with the right manager within the class". A regular deep insight – a similar analysis applies to horse racing.

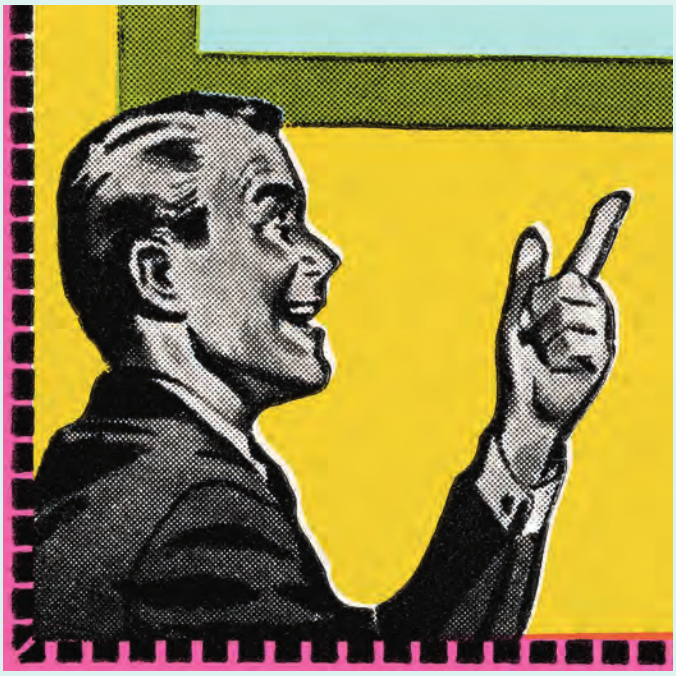
"We are passionate about (insert latest investor fad to taste)". There is much room for doubt on this mantras sincerity.

A lot of ESG declarations fall into the dodgy box. I remember a luminary of the US buyout world at a conference in Munich explaining what we should all be doing to make the planet fit for our grandchildren. (He has had three marriages, so he may be long on grandchildren!) He had, of course, flown over from the US in a monster private jet.

"For the first time in years/decade/generation entry price and valuations are the most essential thing for returns". Hardly ever true! Market movements, strategy optimisation and lots of other things count more. Reality in private equity is much more complex and variable than the consultant industry would like you to believe.

"Timing is everything". Nearly true – the problem is it is only, sometimes a long time, after you have exited the deal can you assess this. One investment of my firm was sold at a four-times multiple in three years – great. A year later we would have had 32-times and three years later it was bust. Oh, for better timing!

"We play in mid-market deals because we can make more of a difference". No one has ever put a convincing case to me on the merits of this assertion. Small, and big, companies can generally change too. Some companies clearly have difficulties in change – high street retailers with an expensive and declining network of shops are a good example.



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There's been a lot of bragging about venture returns in recent years – a lot of it now looks overconfident

"We create a lot of value in our fund due diligence". Sometimes this seems true, but the data is far from compelling. Managers in most periods have poor return correlation between consecutive funds and no amount of due diligence can forecast future changes in team, market dynamics and the like.

Much bragging has been seen in recent years about the strength of venture returns. Good sport could be had by asking the venture lords "What percentage of your returns are realised?" With luck, Youtube will have captured the overconfident questioner put-downs that resulted.

"The credit markets are open, liquid and constructive – buyouts should prosper over the coming years." Normally an excess of debt predicts failure and lousy returns – doesn't it?

Our industry is very good at generating reasons for investors to give it more money whatever the economic background. Distress is an opportunity not a prediction of failure. Fast rising prices or very high pricing allows predictions of great returns to come. Low availability of debt creates better pricing for new deals. Strong economies and weak economies both generate opportunity. And so on!

Generally, you can look at the macros and reliably estimate the sales pitch the industry will be using. It would be good to see more creativity.

For decades the industry has claimed its need for fees of about 1.5% to 2.0% and a 20% carry as essential to get, and keep, a good team together. However, firms that have sold, for example, 30% of the GP company from partners who may well now be long forgotten, seem neither to lack staff or have different returns from funds who are not part sold. Markets are not always perfect.

But new stuff mercifully keeps the industry interested. Who could have imagined crypto-venture funds?

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