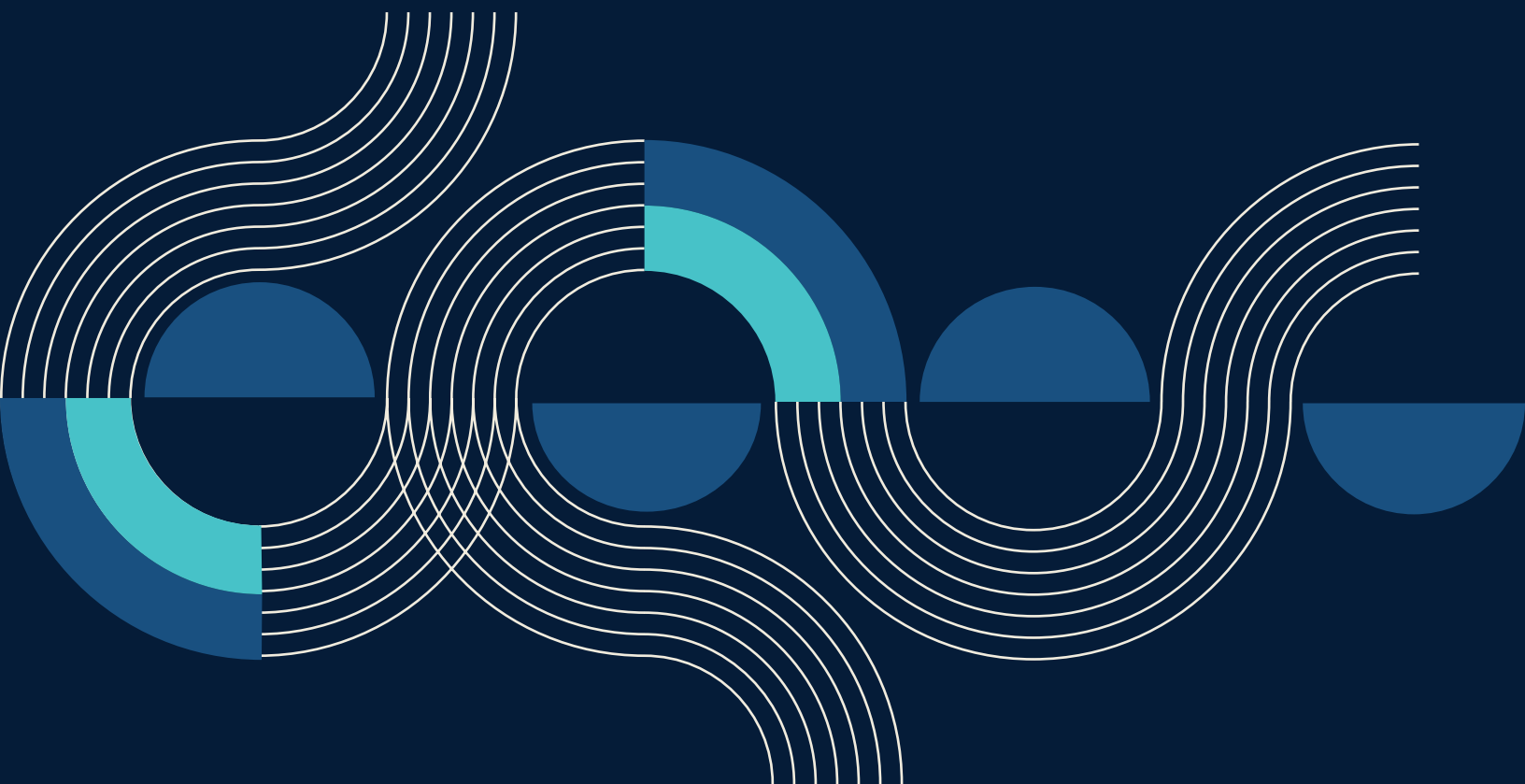


# **PitchBook guide for first-time fund managers**



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# Overview

Starting a first-time fund can be likened to opening an asset management startup. Most aspiring fund managers face an uphill battle to close their first fund, with the process taking an average of nearly two years, according to PitchBook data. Like founders, new fund managers need to find product-market fit for their investment thesis, have a compelling story, possess a deep understanding of the market and know how to differentiate themselves and stand out from their peers.

Gaining the trust and commitments of LPs is traditionally a difficult undertaking for first-time fund managers. From an LP's perspective, investing in a debut fund is likely a much riskier endeavor than allocating to more experienced managers, whose investment team has a tested and proven framework for assessing deals and sourcing winning opportunities. But that story may be changing slightly. LP interest in first-time funds has slowly started to gain momentum, with first-time fundraising occurring at a higher pace in recent years—especially in venture funds.

While it may be easier to raise a first-time fund than it was a decade ago, the landscape for first-time fund managers is still extremely competitive. There are more managers competing for the same LP and founder attention. With such fierce competition among first-time fund managers to secure capital, we compiled this guide of important considerations and tips emerging managers should take into account during their journey.

# Setting up your fund: determining portfolio construction, management fees and jurisdiction

As a first-time fund manager, it's essential to consider the structure, jurisdiction and reporting framework of your fund—and ideally optimize your limited partnership to be “LP-friendly” and tax favorable. For example, you may choose to restrict your fund to certain geographies to reduce complexity or limit your fund to US-based investors to avoid the extensive regulations associated with opening a fund to investors outside of the US.

Setting up shop before knowing who your LP is poses its own challenges. It's hard to optimize a fund for the right LPs when you don't know who they will be, but LP shopping can be more challenging without having a structure or established term sheet.

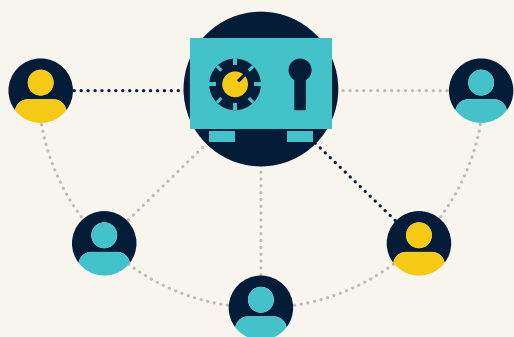
In the limited partnership agreement, you'll also want to define a clear capital allocation strategy and portfolio construction, determining factors like the ticket size of your investments, target ownership percentages and your fund size. You should also be able to articulate your expected fund performance, detailing the assumptions behind your model based on industry benchmarks or performance criteria on similar funds. Here we explore some of key considerations when setting up a first-time fund.

## Choosing whether to raise your fund publicly or not

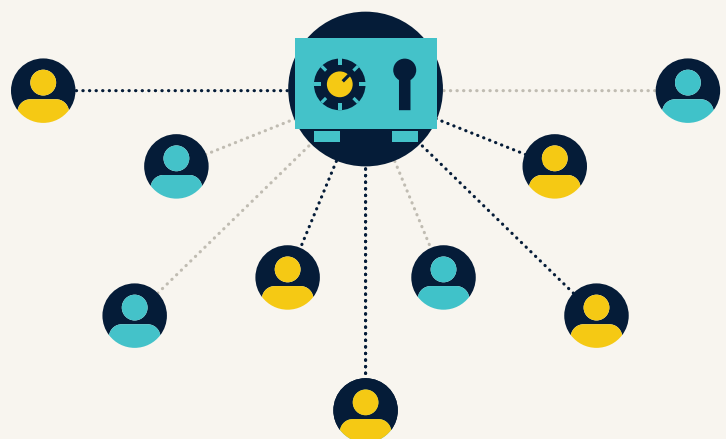
There are two routes for raising an emerging fund: Managers can choose to raise through a 506b, in which they can't publicly declare they are raising a fund, or through a 506c, in which they can publicly recruit investors.

Raising your fund privately essentially locks you into fundraising from your personal network, which can be a challenging route for aspiring managers who do not come from a wealthy background or network of friends and family who can write checks in the hundreds of thousands of dollars. In general, it's better for most emerging managers to raise their fund publicly so that you can leverage a wider toolkit to source investors.

**Raising through a private network**



**Raising through a public network**

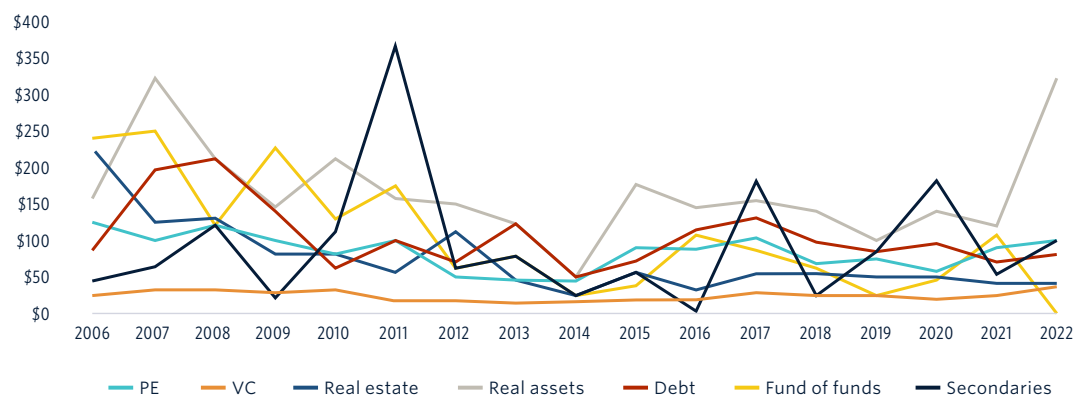


## Determining portfolio construction

### Fund size

Choosing the right fund size is another important consideration for emerging managers. Raising a \$100 million fund is going to require different LPs than raising a \$50 million fund. Therefore, fund size plays a significant role in the types of LPs you can and should target. Some new managers choose to raise larger funds, targeting big institutions who can accommodate loftier check sizes. However, large LPs like pension funds and endowments tend to be some of the most reluctant LPs to commit to first-time funds. Additionally, in certain scenarios, raising a larger fund can make it more difficult to close. Usually, fund managers must secure from 10-20% of the fund for a first close; it is significantly more challenging to close 20% of a \$100 million fund than one that is sub-\$50 million. Most commonly, first-time fund managers choose to raise smaller funds. However, competition among smaller funds is high. For example, 40% of VC funds are under \$50 million—generally targeting the same VC companies.

### MEDIAN FIRST-TIME FUND SIZE (\$M) BY FUND CLASS



\*According to PitchBook data from January 2006- June 2022

### Fund life

Another important element of the fund terms is the fund life, which is the sum of the investment and liquidation period. In general, the standard private market fund life is 10 years with possible extensions to accommodate extra-long holding periods. However, this time will largely depend on your strategy, as different approaches and asset classes have different market standards. Different LPs have varying liquidity preferences—some are after shorter liquidation periods while others are willing to forego liquidity in search of long-term, boosted returns. Approaching LPs during the fundraising process whose preferences align with your fund terms can help you better target your efforts.

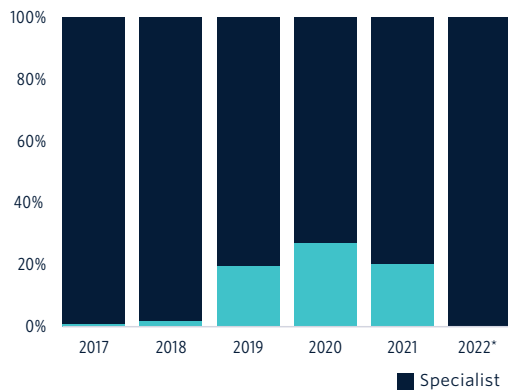
### The largest proportion of the fund's capital that one deal may receive

One bad deal can be extremely detrimental to a fund's performance. As a first-time manager, it's equally important to know when to abandon a portfolio company as it to identify investments in one. Setting a limit on the amount of capital that can be poured into a single portfolio company provides some disciplinary infrastructure in the LPA can limit the temptation to throw capital into a bad investment.

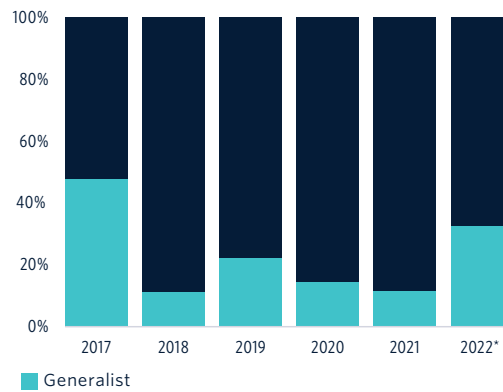
## The sectors and industries that will be invested in and in what proportions

How many companies will your portfolio invest in and what will the ticket size of those investments be? Will you employ a specialist strategy, zeroing in on specific industries or take a generalist approach? This should be determined in a logical way to reflect the size and experience of the investment team, how many deals each person can take on and manage to exit and any calculations a manager has done regarding their returns. Does the team plan to have only a small number of deals drive most of the fund's returns, or will each investment pull its own weight? The former, more popular in VC, may require a larger portfolio of companies to ensure that no single investment sinks the fund—while the latter, more popular in PE may be able to prioritize a handful of investments, since there is less expectation of big wins or losses.

### FIRST-TIME PE FUNDS BY STRATEGY: GENERALIST VS. SPECIALIST



### FIRST-TIME VC FUNDS BY STRATEGY: GENERALIST VS. SPECIALIST



\*According to PitchBook data from Jan 2017- October 18, 2022

## Management fees

Management fees are used to fund operations, including salaries, office space and travel. Typically, management fees charged annually to LPs are between 2%-3% per year depending on fund size and number of vintages. So if, for example, it will cost \$1 million to operate your fund, then a \$50 million fund will need to be raised. As a first-time fund manager, you can use management fee discounts to attract LPs to your fund, a topic discussed later in this guide.

## Fund expenses

Running a fund is a business, and managers must consider the money that will need to be allocated towards banking, audits, taxes, insurance, fund administration and other expenses. Typically, funds may allocate anywhere from \$500 thousand to \$1 million towards fund expenses. Fund administrators like Carta and AngelList can be great resources for fund managers looking to allocate administrative and back-office tasks to open their time to focus solely on sourcing portfolio company investments and securing LP commitments.

# Identifying the right LPs for your fund

Maybe the most important consideration for first-time fund managers is identifying the best LP prospects for their fund. When you're starting out, it's tempting to cast a large net or take every meeting and hope for a check. This isn't a very strategic approach and tends to result in unnecessarily wasted time and resources. What's the point of pitching to a pension fund that's never committed to a first-time fund, doesn't write checks in your target size or doesn't invest in your sector?

Aspiring GPs need to be intentional about creating their LP network and audience. LPs take on a broad spectrum, ranging from family offices to big institutions with AUMs in the high billions. Different LPs have varying investment ethos, risk tolerances, strategies and goals. Setting yourself up for success in the fundraising process means taking the time to diligence LP prospects and identify suitable targets for your fund. Not every investor will be a good fit—and that's okay.

Gather as much information on potential LPs as possible. Who have they worked with in the past? Have they committed to a first-time fund before? Benchmark the returns of that fund—was it successful? If it has a strong IRR, maybe they'd be willing to invest in a first-time fund again. What stages, sectors, geographies and check sizes do they prefer? Commitment sizes are a biggie. Many LPs want to write larger checks, and most first-time fund managers can only take on smaller commitments.

In short, gather as much information as possible before making a pitch. The goal is to construct a targeted list of LPs that align with your brand as a fund, so it's easy to advocate for your strategy and its unique attributes because you know your pitching LPs who are aligned with what you have to offer.

## A look at some active limited partners to first-time funds

### Archean Capital Partners

[Archean Capital](#) is a private equity firm that primarily operates as a fund of funds. The firm is solely focused on anchoring new private equity firms and is primarily focused on buyout, growth equity, and turnaround strategies.

### Recast Capital

Founded in 2020, [Recast Capital](#) is a female-founded venture capital fund of funds that seeks to support emerging managers in the venture ecosystem.

## Active limited partners to first-time funds continued

### **Gatewood Capital Partners**

[Gatewood](#) is a private equity firm with a dedicated fund that seeks to make seed and sponsorship-level investments in highly qualified investment managers pursuing a wide range of private equity and other alternative investments strategies.

The firm targets small to medium-sized North American-based alternative asset managers, pursuing a range of investment strategies, including buyout, growth equity, private credit, distressed, real estate and other strategies.

### **HarbourVest Partners**

[Harbour Vest](#) is one of the most prominent funds of funds that backs first-time fund managers. The firm has worked with emerging managers for more than 10 years and offers an emerging manager program dedicated to identifying promising new fund managers.

### **Teacher Retirement System of Texas (TRS)**

[Teacher Retirement System of Texas](#) (TRS of Texas) is a public pension fund based in Austin, Texas. They offer an emerging manager program that is designed to identify and grow the next generation of exceptional, high performing managers, with the goal of potential graduation to a Trust level commitment. As of 2021, the TRS has committed \$5.9 billion in capital to 204 emerging managers across 342 investments.

### **Stable Asset Management**

[Stable](#) is a sponsor that backs emerging managers across all asset classes. Stable invests across the fund lifecycle with a focus on early and growth stages, doing seed, acceleration and strategic capital deals.

### **MIT Investment Management Company**

[MIT Investment Management Company](#) is the investment firm that provides stewardship of the MIT Corporation's financial resources and offers one of the most robust emerging manager programs in the endowment ecosystem.

### **New York State Common Retirement Fund**

[The New York State Common Retirement Fund](#) (NYSCRF) is a public pension fund based in New York. They have a dedicated emerging manager program that provides capital to newer, smaller and diverse investment management firms. The Fund is one of a few public pension plans to establish an emerging manager program and has committed \$9 billion into the program.



## Exploring the pros and cons of different LPs that back first-time funds

### Family offices

Family offices have historically been an important LP category for emerging managers, representing one of the most active and willing investors in first-time funds. In general, family offices have different incentives from larger, institutional LPs in that they have more tolerance for risk taking in exchange for long-term, higher returns. Family offices have the flexibility and benefit of indefinite fund lives and long-term or even no investment horizons and are therefore able to provide patient, evergreen capital. Additionally, they are not subject to the same extensive diligence processes of other LPs and don't have formal investment committees or mandates, resulting in more agile flexible investment decision making that can be favorable to emerging managers.

However, family offices do have certain drawbacks as an LP. For one, they are more prone to consistent management changes, meaning exits can occur when the family's objectives or goals change. Successions, management changes and fluctuations in capital requirements are some issues that can prompt unexpected changes in previously secure capital courses, posing distinct considerations for GPs. Additionally, of all the LPs that fund managers can pitch, family offices tend to be more opaque, and it can be challenging to identify those that are actively allocating capital.

### High-net-worth individuals

Like family offices, high-net-worth individuals (HNWIs) have also been a traditionally active supporter of first-time funds, as they are usually more patient and willing to see their investments build value over longer time horizons. And like family offices, they are not looking to make quick a quick buck and are more willing than other LPs to trade liquidity for higher returns in the long run.

Both HNWIs and family offices tend to have specific interests regarding the sectors in which they allocate capital. For example, if a HNWI made their money from building a company in media, they may be more likely or apt to invest in that sector, as it's where they built their career and have specific knowledge sets.

### Funds of funds

Funds of funds are typically ready and willing LPs, making them another popular option for first-time fund managers. They will often write checks faster than other LPs—however, funds of funds are unique in that they too are raising their own funds, which can make timing an issue.

### Institutions

Endowments, pension funds and other large institutions have typically been the hardest LP group to get on board with first-time funds. Institutions tend to want to write larger checks, and their investing methods are more traditional—requiring extensive due diligence. But institutions can anchor funds, and they are increasingly attracted to the favorable economics and co-investment rights that can be associated with first-time funds. Additionally, some larger institutions, like pension funds, have dedicated emerging manager programs.

Choosing the right LP for you will ultimately depend on a variety of factors, such as your background, fund size, strategy and network.

# Tips for crafting a winning pitch to LPs

Once you've identified target LPs for your fund, it's time to sell them on your vision. Pitching to LPs is a lot like pitching a pre-seed startup—there's a limited track record to go off, so the pitch needs to tell a strong story and showcase the value of the team. Differentiation is key— aspiring managers need to demonstrate what makes them special. What's your story, edge and investment thesis, and how are they different from the competition?



## Cover the nuts and bolts

Summarize the framework of the fund. Provide investors with your estimated fund size, what stage, geography and sector you'll focus on and preferred timeline to close. Your track record and history will be top of mind for LPs. Show your success as an investor in the past, discussing experiences and deals in your chosen market and niche that have shaped your investment approach.

If you have a team, be sure to articulate your collective experience and history working together and why you are best positioned to buy, manage and sell assets for positive fund outcomes. One area LPs tend to have concerns is with partners—they want to feel confident that you'll work well together. How will your team successfully convince portfolio companies that you will provide a better result than other sources of capital?



## Showcase your investment thesis

You need to pitch a well-defined investment thesis to LPs. This should cover anything from your broader view on market opportunities and approach to investing to specific underlying principles and frameworks that will guide how you assess prospects. Detail the type of opportunities and companies you will focus on; discuss the verticals, business models and market space you want to target and explain why you are uniquely fit to do so. If you are focusing on a particular market, show LPs why now is the right time to commit capital to that opportunity and demonstrate the credibility you have in these chosen markets to attract portfolio companies seeking capital. Not every sector or market is always ripe for outsized investment returns, and GPs should have knowledge of their spaces and current prospects.



## Differentiate yourself from the crowd

As a first-time fund manager, there's a high bar to get LPs to invest—and you'll need to stand out more than your veteran peers. With no shortage of other options for capital commitments, differentiating your fund to LPs is key. PE managers selling just another middle market buyout strategy or VC managers pitching SaaS roundups in Silicon Valley won't have LPs sitting on the edge of their seat with their checkbooks in hand. Do you take a geographical focus, investing in companies near you, becoming more of an operational partner rather than financially engineering their success? Will you seek orphaned assets, companies ready for a next phase of growth, products seeking international distribution or something else? Think about your edge in the investment value chain. What is your "special sauce" when it comes to identifying, supporting and ultimately winning investments? Demonstrating how you personally resonate with your investment ethos will go a long way in a crowded market. Do you only invest in portfolio companies of a certain size and scope? Find what makes you special and own it.



## Include your terms and any special fund economics

Lastly, you'll want to outline your fee structure and any deal sweeteners or preferential economics you're willing to offer to LPs. Using selling points like co-investment rights, warehousing options, seed structures or anchor carry fees and discounts is an effective way to create a sense of urgency in your fundraising and speed up the process. Later in this guide, we dive into preferential economics, exploring some key advantages and disadvantages associated with various deals and structures.



### REPORT

## PitchBook's guide to your pitch: a former LP's advice for emerging managers preparing to fundraise

Former LP and PitchBook Analyst Hilary Wiek provides a comprehensive overview of to tips for winning your pitch.

[Read the report](#)

# How first-time fund managers use PitchBook: Spotlight on Embedded Ventures

**EMBEDDED**  
VENTURES



**Jenna Bryant,**  
Cofounder &  
General Partner



**Jordan Noone,**  
Cofounder &  
General Partner

## Embedded Ventures

Launched in 2020, Embedded Ventures is a next generation venture capital firm investing in dual-use space startups beyond launch. Best described as “the skunkworks of Venture Capital” due to their unique investment approach and backgrounds, Embedded has a first-of-its-kind partnership with the United States Space Force, investing in pre-seed and seed-stage startups focused in space operations, digital engineering and advanced manufacturing. To date, Embedded Ventures has announced investments in KittyCAD, Inversion, Slingshot Aerospace, Skyrise, Chromatic 3D Materials and Akash Systems.

Year founded:	Total investments:	Median round amount:	Co-investors:
2020	7	\$10 million	64

Embedded Ventures Cofounders Jenna Bryant and Jordan Noone discuss how they leverage PitchBook to identify the best LPs and accelerate their fundraising process.

### **Q: What made you choose PitchBook as your data provider and what benefits do you see from having PitchBook during the early stages of your fund?**

**A:** When starting Embedded Ventures in 2020, we rapidly expanded our network of LPs. Using data from PitchBook, we were able to focus deeper with Limited Partners interested in the early-stage deep tech investing we do, especially those open to us as emerging managers.

### **Q: What challenges were you trying to solve with PitchBook?**

**A:** When our network of LPs grew quickly, we used PitchBook data to take a deeper look at those interested in investing in dual-use space startups beyond launch. The amount of data at our fingertips and ease of use helped us make informed decisions as we continued to expand our network of LPs.

### **Q: How has your fundraising process improved since joining PitchBook?**

**A:** The resources and data available to us through PitchBook allowed us to easily target LPs who have similar investment theses and who were open to emerging managers. The ability to target certain people on such an individual level helped drive our growth trajectory.

### **Q: How has PitchBook helped you win?**

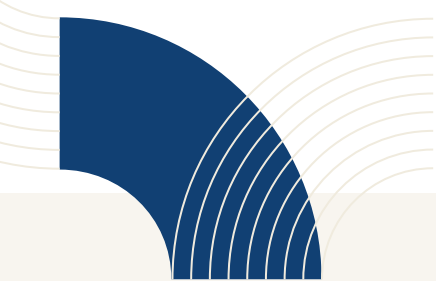
**A:** Since we’ve started using PitchBook we’ve grown our pipeline of new Limited Partners significantly. The data and advanced search tools allowed us to target LPs who are looking for early-stage, deep tech and are willing to work with emerging managers.

# How to accelerate the fundraising process—exploring preferential economics

Fundraising is undoubtedly the biggest hurdle faced by first-time fund managers. One outlet aspiring fund managers can pursue to accelerate the fundraising process is offering preferential economics to LPs. These “deal sweeteners” typically offer fee and carry discounts or some permanent or long-term percentage of gross revenue in exchange for a significant upfront commitment and play a notable role in attracting LP interest to first-time funds.

Seed deals, anchor commitments, deal warehousing and co-investing rights are a few of the most common preferential economics first-time fund managers can explore in the fundraising process. These deals can have a significant influence on a fund managers ability to raise capital, and in some cases create a catalytic domino effect on their ability to fundraise successfully from other investors. However, the decision to engage in any of these deals will be unique to each manager and aspiring first-time fund managers need to weigh the potential benefits against the economics they will be giving up over an extended time horizon.

Here we explore how first-time fund managers can different kinds of preferential economics to accelerate their fundraising process along with key considerations they should consider with these deals.



## Anchor commitments

Anchor commitments are commitments made by LPs (typically to first-time funds) that make up a significant percentage of the target fund size—typically as much as 20% to 30%. Anchors are usually pursued during a fund’s first or second close and can be helpful to aspiring GPs in accelerating their fundraising process. Once one reputable LP makes a large commitment to a fund, it can help to establish the credibility of the fund manager, reducing the friction in attracting additional commitments from additional LPs. In exchange for an LP taking on the risk of making a large commitment to a new manager, they typically receive a hefty fee discount. For example, an LP making an anchor commitment could have a fee and carry ratio as low as 1 and 10 compared to the standard 2 and 20.

## Seed deals

Seed deals were first developed in the hedge fund landscape and heavily favored LPs. However, seeding has become a popular option for managers across private market asset classes, with GPs demanding more favorable terms. Today, there is no market standard seed structure, with the terms of these deals heavily dependent on the players involved, their negotiating power and how much they bring to the table. Seed deals typically involve a substantial commitment to the fund with some scenarios also including additional “operating” capital to help the manager get up and running. Situations in which an LP makes only a fund commitment is typically associated with a temporary revenue or profit share while those in which an LP makes a fund commitment alongside providing working capital are usually accompanied with an equity stake in the firm.

Like anchor commitments, seed deals are structured to help a first-time or emerging manager get off the ground beyond the first fundraising while providing long-term economic benefits to the seeder. In return for making a large fund commitment—comparable to an anchor—and providing operating capital, the seeder receives either an equity stake in the GP, the management company or both. Typically, this takes place in the form of an equity stake or revenue share, which both sunset over time once an AUM or performance hurdle has been achieved. Since investors in these arrangements are receiving an equity stake or revenue share, they usually pay full fee and carry for their fund commitments.



### Revenue and profit shares

One form of seed structuring, revenue or profit shares provide LPs with preferred fund economics without the complexity of owning an equity stake in a GP or management company that could include exposure to additional expenses such as partner and staff bonuses. In general, revenue shares are more popular than profit shares, as profit margins in a first-time fund can be slim early on.

Revenue shares involve a percentage—usually 20% of revenue from management fees and carry—that are paid to the seeder until a specific triggering event occurs, such as a third fund, the payback of a certain multiple of the original investment or any number of other milestones.



### Equity stakes

Seeders can also choose to structure deals to acquire a minority equity stake in the GP or management company. Equity stakes deals are more likely when the seeder provides a fund commitment alongside operating capital and the way equity stakes are structured largely depend on whether the working capital is expected to be repaid. If the GP plans to repay the working capital, the deals are typically structured as preferred equity or mezzanine.

For example, in addition to a fund commitment, a GP receives \$10 million in working capital, in which they make payments to the seeder at a 10% interest rate along with providing a 5% stake in the management company. Alternatively, choosing to not repay working capital may involve a permanent equity stake for the seeder alongside a sunset clause where management buys back the stake once specific milestones are hit.

## Warehousing

As a first-time fund manager, it can be beneficial to “warehouse” a set of portfolio deals or essentially put them in storage to use when you launch your fund. Deal warehousing is another route GPs can take to get off the ground, and it has the benefit that it doesn't involve seeder-style economics. In general, there are two kinds of warehouse deals: those in which the fund manager personally has equity in as an angel investor or advisor, or those in which the fund manager plans to invest in when they launch their fund, given the portfolio company has agreed to hold an allocation for them.

In a typical arrangement, an LP will finance the first one to three deals a GP makes and place them into a special-purpose vehicle. Once the GP closes on fund commitments, they call capital from the new LPs and put these companies to their new fund—typically leaving 50% with the warehousing entity. Deal warehousing is beneficial in that it can de-risk the fund by allowing LPs to participate in marked up deals at lower valuations. Additionally, having warehoused deals in your back pocket can be a positive signal to LPs of the caliber of your deal flow, serving as a proof of concept in the fundraising process.

## Co-investing rights





LPs' continued interest in direct investing has made co-investing rights a popular strategy for GPs looking to retain LPs interest in their funds. While this trend is not exclusive to emerging managers, it is another path they can explore to differentiate themselves and attract LP interest by providing preferential terms. Co-investment rights allow LPs to invest directly alongside GPs as co-investors and unlike commitments, which are associated with carry and management fees, co-investments most commonly charge no or highly reduced management or carry fees, resulting in a significant difference in the overall profitability of the co-investment. LPs are also attracted to co-investing rights due to the additional control over portfolio exposure it provides compared to blind pool investing, in which they are typically required to participate in every underlying investment of a fund.

# Deciding whether to pursue preferential economics in your fundraising process




Attracting LPs and their capital through preferential economics can be an effective tool first-time fund managers can leverage to close their initial fund. However, while these deals can accelerate the fundraising process, each pose their own advantages and disadvantages that are important to consider.

Of all the potential deals a first-time fund manager can explore, the choice to take seed or anchor capital has the most economic considerations that should be weighted over the long-term. Some key advantages and disadvantages associated with seed and anchor deals include:

## Advantages

-  Seed and anchor deals can provide meaningful upfront capital that can significantly reduce the length of the fundraising process. This can be especially advantageous to fund managers who have been operating as fundless sponsors, do not have an extensive network, do not come from a wealthy background, have less prestigious resumes or cannot forego income for a two-year fundraising period.
-  Seed and anchor deals can provide credibility to a first-time fund manager and help to attract subsequent LPs. Often, when investors see another reputable LP committed to a fund, they “piggyback” off that commitment—if the anchor or seed LP did extensive diligence on the manager.
-  LPs providing seed or anchor capital can provide support and mentorship in marketing, risk management and other areas of business development that can be valued by certain aspiring managers.
-  Seed deals that are accompanied by operating capital can help first-time fund managers finance and handle their back-office operations.

## Disadvantages

-  Seed and anchor deals can cause lower initial revenue as the investor either gets discounts on fees and carry or gets a share of the GP or management company’s revenue and in some scenarios, this reduced revenue can continue over an extended timeframe, leading to less long-term benefits for the GP. Managers who have long track records at big-name firms, are experienced fundraisers or are well networked may not benefit from seed or anchor economics as they tend to have easier fundraising processes.
-  Revenue shares or equity stake agreements that are too complex may serve as a deterrent to other LPs in committing to the fund.
-  Having an anchor or seed investor in your fund can lead to less freedom as they may expect to have more of a say on how a fund is managed and operated along with its investments than a typical LP. Having a dominant anchor or seed investor on board can add risk in that it leads to a primary point of failure and ultimately, having a diversified group of LPs is a more ideal and healthier for the fund.

These are a couple of key advantages and disadvantages of seed and anchor deals and how they can affect different stakeholders. Each GP's situation is unique and will determine the deals and economics best for their circumstances. We have heard cautionary tales of seeded managers later regretting their arrangement; We have also heard seeded managers enthuse about the support they received and their ease in subsequent fundraises. Ultimately, first-time fund managers must balance their immediate short-term needs with the long-term viability and incentives for their firm.

Co-investing rights and deal warehousing come with their own considerations, too. While offering co-investing rights can improve the chance of a successful fundraise, it can also slow the dealmaking process, come with additional costs and negatively impact relationships with other LPs who may want access to the same co-investing rights offered to other investors in your fund. Similarly, while having a stockroom of potential investments can make it much easier to raise a fund, deal warehousing has its own risks that should be considered—namely, if you are unable to close your fund, someone will be left holding your warehoused investment.



## **Checklist of questions to answer when choosing if preferential economics is right for you**

- How robust is your personal network of potential investors?
- How much time can you dedicate to the fundraising process?
- Do you have a strong investment resume from past deals?
- Could you benefit from the credibility associated with securing a first LP?
- Are you looking for mentorship in your LP relationships?
- Are you willing to sacrifice some degree of freedom to accelerate your fundraising process?
- Do you need capital to support your fund operations?

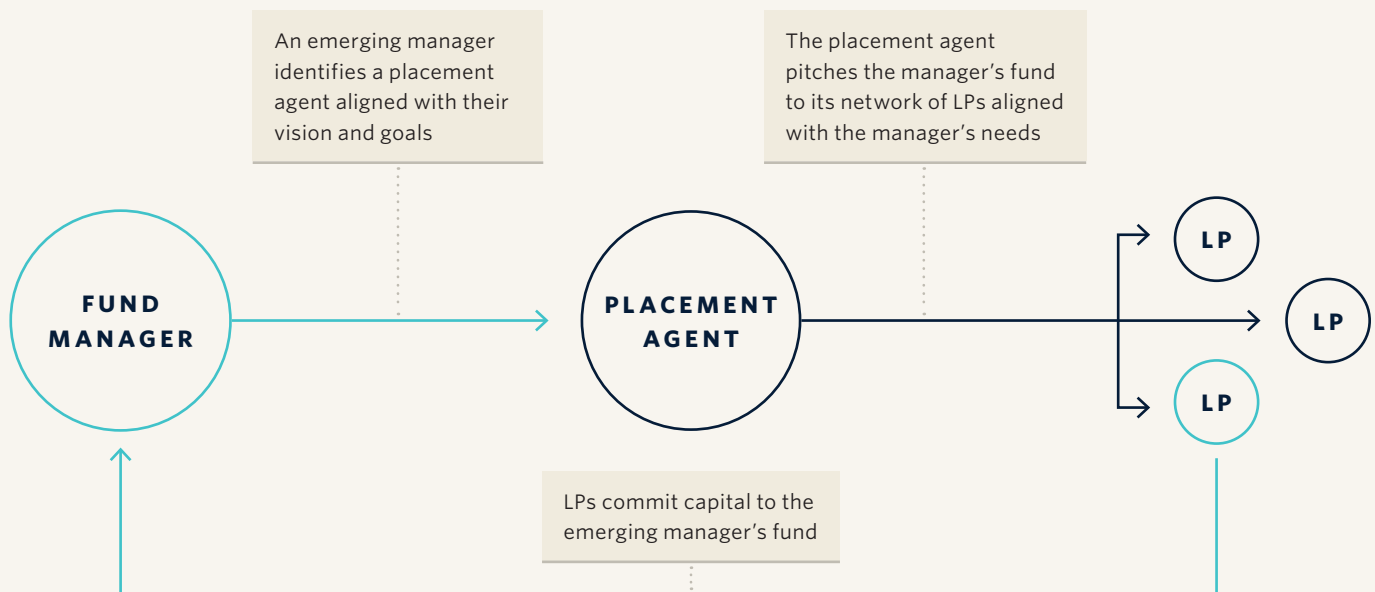
# Determining whether to use a placement agent

When raising a first-time fund, one of the first questions considered by GPs is, “Should I use a placement agent?” And the answer—well, it depends. Do you or one of your partners have extensive fundraising experience and a robust network to leverage? Do you have the time and resources to focus on pitching and following up with LPs and the relationship building necessary to secure commitments? Are you confident that your investor base provides you with the best chance for long-term success? Do you have a long, established track record at a big-name firm? These are some questions you should consider.

## What are placement agents?

Placement agents are intermediaries—normally brokers dealers—that raise capital for investment funds quickly and efficiently by connecting fund managers to qualified investors. Placement agents assist in all aspects of fundraising and fund development, including marketing and LP communications. In exchange, they usually take a 2-3% fee on capital “placed” and in some cases, a small retainer. This placement fee is often paid over several quarters after the fund’s closing.

Determining whether to use a placement agent is typically top of mind for emerging fund managers as they can be a great resource for creating marketing materials, providing valuable insights on market conditions, evaluating an investment thesis and pitch and shedding light on the current interest from LPs in emerging managers. They can also handle logistical tasks, like scheduling meetings and follow up with LP prospects—freeing up time for GPs to prioritize sourcing investments. The best placement agents act as a true partner behind the scenes to refine messaging and differentiation. However, not all placement agents are created equal, and while they can open the doors to certain opportunities, there are also some issues that can arise when selecting and working with them.



## Key things to consider when determining whether a placement agent is right for you



### Do your diligence

Just as it's important to perform due diligence prospective LPs to ensure that you're optimally targeting your efforts, the same holds true for placement agents. If you are going to use a placement agent, it's important to ensure they have a clear alignment toward your investment thesis and vision along with a deep understanding of the industries, deals and strategies you're targeting and a successful track record of placing capital in similar scenarios. Many agents can present an impressive network of potential investors. However, a history of successfully persuading those investors to write checks is what you're looking for.

Make sure the placement agent has trusted relationships with LPs who would be a good fit for your product—if you're a first-time manager in VC, you wouldn't want to hire a placement agent with a hedge fund or PE background. Do your diligence by talking with similar managers with comparable strategies who have used a prospective placement agent in the past or ask for referrals from any attorneys, accountants or peers in your network.



### Consider the economics of the deal

Most placement agents charge a fee of 2% on capital placed. However, this fee can range between 1-3%. Before signing an agreement, it's essential to know if you will be charged on any capital placed from LPs that you both know along with the fee repayment period. It's important for managers to weigh the costs of a placement agent and how and if the terms of their fund's governing agreement could accommodate the payment of such fees and costs along with the personal benefits and value a placement agent could provide. Some first-time fund managers are better positioned than others, and the potential value a placement agent could provide could justify the economics in certain scenarios over others. It is important to note that certain banks will finance placement fees, which can be helpful to emerging managers who feel an agent would be helpful but don't have the resources to pay for one.



### The typical minimum AUM for a placement agent is \$100M

Placement agents, too, are particular in the managers they will take on with preference towards those managing larger funds in which the economics are more attractive. In short, they don't make a lot of money on emerging managers since the fund sizes involved are relatively small, and it is difficult and rare to find a placement agent to take on sub-\$50 million dollar fund— with the typical fund minimum for a placement agent being \$100 million. This can make it difficult for first-time fund managers to find an agent who will accommodate their fund size. It can be strategic to seek out boutique placement agents that will back emerging managers.



### Working with a placement agent adds an extra degree of separation

One argument that can be made against placement agents is that they add an extra degree of separation that can be sometimes less attractive to LPs and create delays in communication, contributing to lost opportunities. Some LPs take the stance that the highest quality managers should have unlimited demand and therefore, view pitches from placement agents with caution. Additionally, many LPs outsource their investment management processes to consultants, creating an extra line of communication: The placement agent must communicate with the consultant, who in turn must get to the LP. This additional lag in communication creates opacity and can sometimes cause friction in attracting and ultimately securing capital.



### **Placement agents are more common (and respected) in private equity than venture capital**

An additional consideration with placement agents is that they are more common and reputable in the private equity ecosystem than in venture capital. In fact, in the VC world, using a placement agent can often be viewed as a negative signal by investors. While it is common for PE fund managers to use placement agents in buyouts, it is rarer to see in VC deals. Many LPs in venture are skeptical towards the use of a placement agent, questioning how managers who cannot tell a compelling story on their own can win and source deals, with many believing the fundraising process to be an integral part of how managers refine their strategy and narrative.



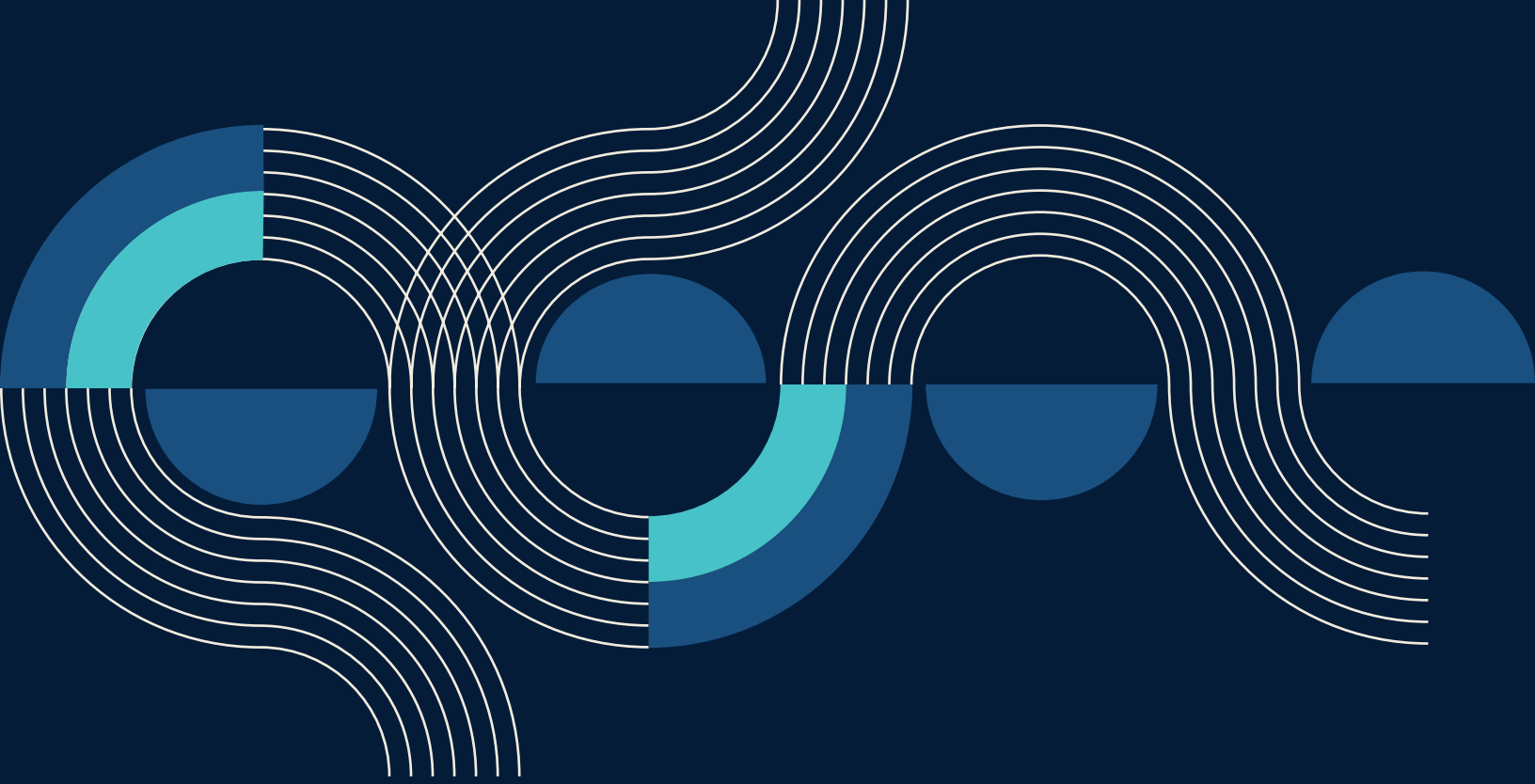
### **Your fund is just one option on the menu**

Ultimately, placement agents are in the business of pitching fund managers and must offer LPs a range of fund options to support themselves. It could be argued that your fund is just one option on the menu. And the question arises: Are you being pitched as the main course? When working with a placement agent, it can be hard to gauge if your fund is their top priority.

# Conclusion

In conclusion, the overarching advice to aspiring managers is to do your diligence across the board. From doing the groundwork to identify LPs and articulate your fund strategy to determining whether to take an anchor or seed deal and use a placement agent, successfully closing a fund requires a high degree of thought and planning. While this guide seeks to provide a comprehensive list of factors that first-time fund managers should consider—there is no one, right universal answer to these topics that applies to all emerging managers.

And although the landscape for emerging managers is competitive, commitments continue to pour into private market funds—and first-time fund managers who provide a thoughtful and cohesive explanation of their approach can find success.



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