How Firms Approach and View the Use of Subscription Lines

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The concept of subscription (sub) lines has been around for decades. However, longer dated sub lines are all the craze right now because they can have a material impact on net IRR in the early years of the fund's life and with rates at historic lows.

Longer dated sub lines allow general partners (GPs) to call capital from (limited partners) LPs once a deal has already appreciated in value (6-12 months after the initial investment). The overall impact to IRR of an aggressively managed subscription line amounts to somewhere between 250 and 1500 basis points. But manual processes present significant challenges to realizing this value. On longer dated sub lines, each draw on the line to fund a deal has its own maturity date and as the fund gets deployed and uncalled capital is reduced, that can reduce the capacity of the sub line and trigger loan covenants. If this process isn't proactively monitored, you could find yourself short on cash when a deal is closing. The current banking portals are limited – all they show, at best, is the outstanding loan balance and the available capacity. This is not enough information to accurately forecast future cashflows. Firms struggle to gather the right information to tell a complete story about the health of their organization, from a liquidity standpoint. Ask yourself one question, are you aggressively managing your subscriptions lines?

The introduction of subscription lines gave firms the ability to smooth out their cashflows and help with liquidity management, but that is only one piece of the puzzle. Sub lines provide a short term "cushion" to help manage liquidity, but the more complex the firm, the harder it is to manage. Today, 85% of private equity organizations monitor their liquidity on **multiple** excel spreadsheets.

Does the below sound like your firm?

1. Manually gather bank balances and populate cash excel spreadsheet.
2. Manage drawdowns, paydowns and maturity dates via another spreadsheet.
3. Manually consolidate future projections and add to cash excel spreadsheet.
4. Manually log into multiple banks to facilitate daily cash movements and record in excel.
5. Somehow tie all this information together to predict the future.

Thus, why the treasury department was born. The burden of navigating through the complexity of liquidity and disparate systems forced firms to hire a dedicated treasurer to manage liquidity and help with the organization's transparency, both in and outside the organization. Many firms are using this new department concept to market to new LPs by highlighting the strength of their liquidity management, which could directly affect the funds investors. Ask yourself one question, do you manage your liquidity in the best way possible?

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Mike joined Hazeltree in 2019 and is responsible for sales and presales for all U.S.-based clients. Prior to joining Hazeltree, Mike held a senior position at an early-stage treasury management startup and helped expand their business, globally. He has a BS in Finance and an executive MBA (EMBA) from the University of Notre Dame.