PE’s Optimistic Outlook And What It Means For Attys

By Benjamin Horney

Law360, New York (August 19, 2016, 5:00 PM ET) -- Despite grappling with uncertainty in numerous forms during the first half of 2016, the private equity industry is confident that investor appetite and deals are on the upswing, and experts say attorneys must help their clients set realistic goals while not dampening their enthusiasm.

Private equity has faced its share of challenges in 2016, from unease over the upcoming administration change in the U.S. and the U.K.’s vote to withdraw from the European Union, to global market volatility and an overall deal-making slump in the first quarter contributing to an uncertain marketplace.

Although uncertainty can be poisonous to the world of deals at large, private equity fund managers are overwhelmingly confident that the next 12 months will see an increase in investor appetite and in portfolio company acquisitions and exits, according to a report released this month by research firm Preqin. Of the 187 private equity fund managers polled by Preqin, 65 percent expect overall private equity industry assets to grow over the next year, and 62 percent intend to put more capital to work.

Howard Berkower, a partner in McCarter & English LLP’s corporate practice, said the bullishness displayed by private equity fund managers comes as no surprise as they tend to have a few common traits.

“[They] are generally very optimistic and upbeat,” he told Law360. “And they are supremely confident.”

Andrew Ahern, a partner at Debevoise & Plimpton LLP, put it bluntly: “I expect my clients to be confident.”

“Most business people are by nature confident and optimistic. There is nothing wrong with that,” he said. “I expect our sponsors to believe in themselves. After all, if they are not confident in themselves, it will be difficult to convince investors to believe in them.”

The self-assuredness of private equity players can be appealing, but it’s important for lawyers to not get too caught in the spell of a confident client. Clients can be as optimistic as they want, but it’s the lawyer’s job to take a more measured approach, something that can be difficult for attorneys, especially when they are working with a private equity fund manager that exudes an aura of fearlessness, according to Berkower.

“They do have this infectious, upbeat optimism that eggs people on, creates a lot of buzz around them,”
Berkower said.

Luckily, many lawyers have a built-in sense of caution, Berkower said, although they have to walk the line between being realistic and discouraging.

“Unlike executives and PE managers, who are very optimistic, lawyers by their very nature are cautious,” Berkower said. “For the most part, you want to be careful as a lawyer not to dampen their interest in doing deals.”

Working for a client who knows what they want and is confident they can go get it has its benefits, including that agreements can often be struck with less concern over the price a client winds up paying, according to Michael Fieweger, head of Baker & McKenzie LLP’s global private equity practice.

“It’s easier to get deals done when you have clients that feel confident bidding higher numbers,” Fieweger told Law360.

However, there is such a thing as too much confidence, and attorneys have to make sure clients only lock in a deal once they completely understand its potential risks. Risk management is the job of the lawyer, and it’s important for attorneys to be able to communicate risk properly and thoughtfully, Fieweger said.

“It’s a matter of having open conversation and dialogue with your clients and making sure everyone knows what their roles are on a transaction,” he said. “They understand they are paying you to service those risks.

“No matter how confident they are, a good client will listen to their counsel on what those issues are,” he said.

Attorneys and private equity fund managers tend to view business and risk differently, and it’s important to understand the contrast, Fieweger said.

Lawyers typically look at issues and determine whether something is or is not a problem, legal or illegal, he said, while private equity players approach things from a probability standpoint. The fund manager looks at the magnitude of risk as set out by their counsel and tries to break down the likelihood that a given decision will wind up being a net positive or negative.

“They want lawyers who can help them work those issues through,” Fieweger said. “That’s the fine line you have to dance as a lawyer.”

It’s important not to forget that your role as the attorney is to advise on the legal and commercial risks that may pop up during a deal-making or fundraising process and to work with clients to “develop a strategy that manages those risks and has the best chance of achieving their objectives,” Ahern said.

“To the extent their optimism leads them to take more risks, that is their prerogative,” he said. “My goal is to ensure they are well-prepared for those risks if they in fact materialize.”

With a private equity community that is ready to get busy, attorneys can try to take advantage by deepening relationships with clients and securing more work, including by assisting private equity managers in finding opportunities and using that experience to learn what attributes they consider
desirable versus what issues they consider to be serious risks, Berkower said.

“One way we can be proactive is touching base with clients regularly and seeing what issues exist,” he said.

--Editing by Christine Chun and Brian Baresch.