WHITE PAPER

EVERGREEN FUNDS

Simplifying Access To Specialized Private Market Opportunities

VISTA

AUTHOR
Dan Parant
Global Head of Private Wealth

Introduction

As investors continue their search for differentiated opportunities to diversify portfolios and achieve financial goals, private investments – historically reserved for institutional investors – are gaining traction among a wider audience. While enthusiasm for private asset classes grows, hurdles remain for broader adoption. These challenges include educational gaps – such as understanding the illiquid nature of private investments – as well as operational complexities like managing cash flows to meet capital calls and navigating high investment minimums.

Evergreen funds are an attractive structure for certain investors as they address some of the pain points that have historically made access to alternative investments more difficult. Beyond solving operational issues, evergreen funds can allow for consistent compounding over the life of the investment and can serve as tools for asset allocation and portfolio diversification.

Furthermore, specialist evergreen funds offer focused exposure to high-performing sectors where deep expertise can more effectively create value.

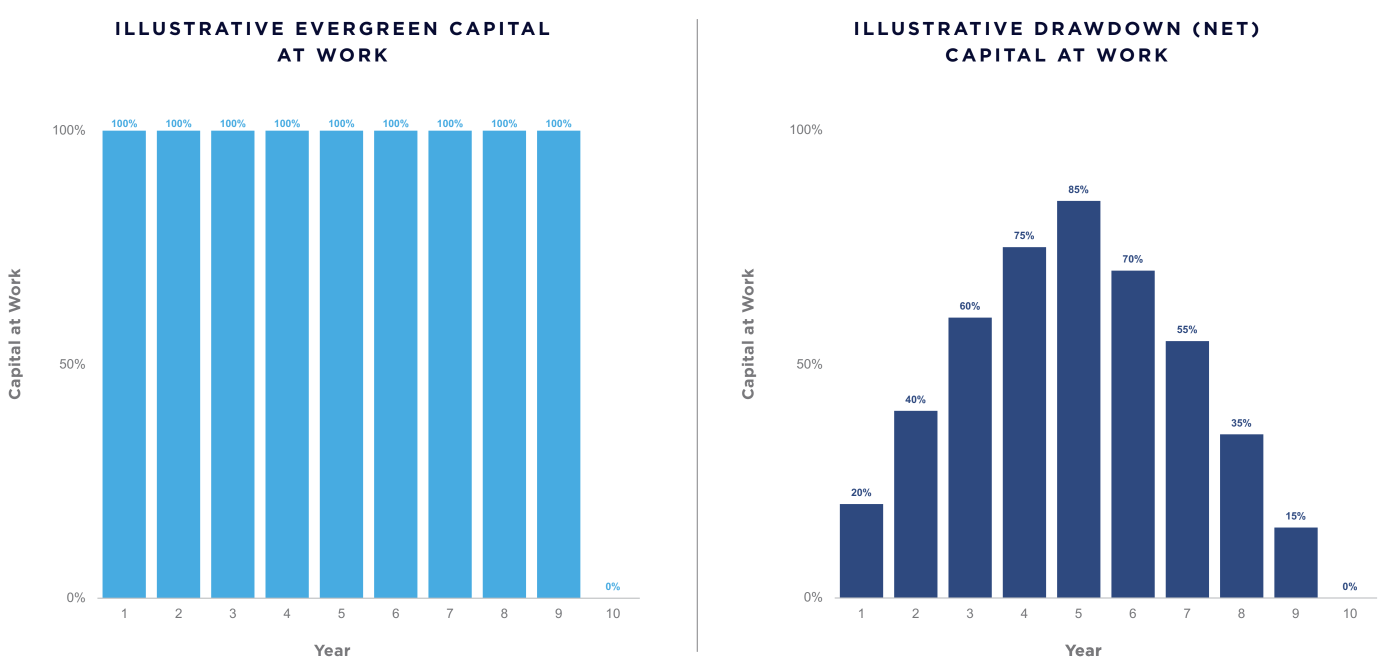
In this article, we explore the essential features that can make evergreen funds, especially those with specialized strategies, an attractive option for investors seeking long-term growth and diversification.

Key Features of Evergreen Funds

INVESTMENT BENEFITS

In evergreen fund structures, 100% of an investor's capital is deployed into a portfolio with existing assets on day one.[1] As a result, investors in evergreen funds can efficiently mitigate the opportunity cost of holding cash for capital calls by immediately putting it to work in productive investments.

CASH DEPLOYMENT COMPARISON[2]

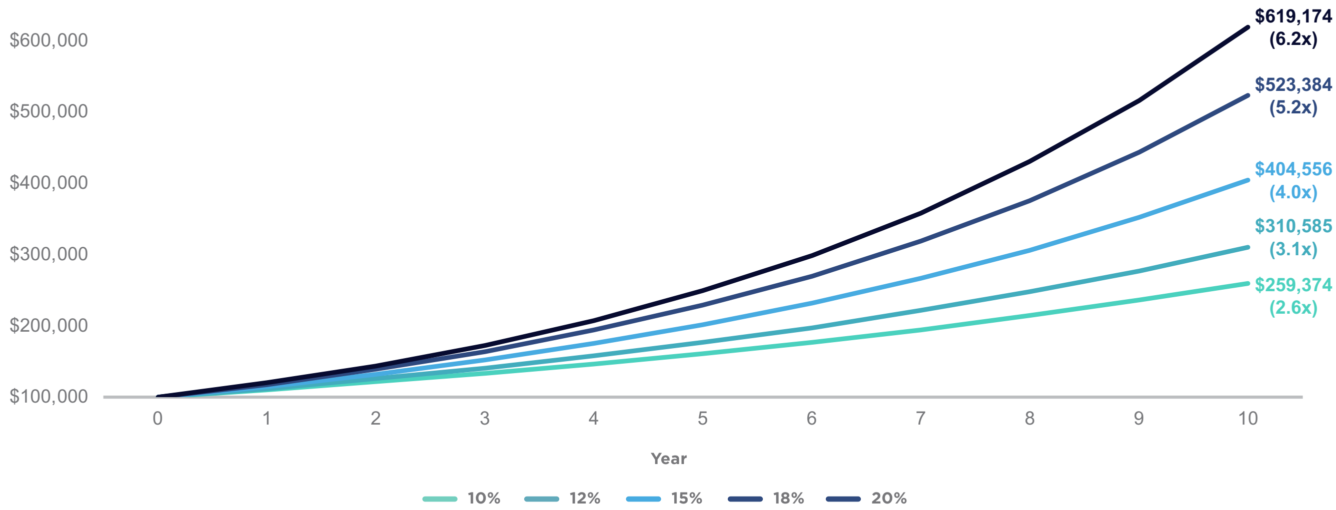


[1] Most funds tend to have a liquidity sleeve of 15-20% to help with cash management (deployment, redemptions, etc.) that is required from the elimination of capital calls.
[2] Vista Equity Partners, 11/2024. For illustrative purposes only.

Evergreen funds can also deliver a higher multiple on invested capital (MOIC), even if their annualized returns are lower, depending on the investment horizon and deployment speed. For example, an evergreen vehicle may achieve the same MOIC of 3.1x over 10 years with a net annualized total return of 12%, whereas a drawdown fund might need to generate an 18.5% net internal rate of return (IRR) to reach the same result.[3] This compounding effect can make evergreen structures particularly attractive for long-term investors.

ILLUSTRATIVE COMPOUNDING POWER OF EVERGREEN FUNDS

HYPOTHETICAL GROWTH OF $100K FOR VARIOUS ANNUAL RETURN RATES[4]



PORTFOLIO CONSTRUCTION BENEFITS

Evergreen funds address potential portfolio construction challenges for investors by providing immediate and consistent exposure to underlying investments. Investors can align capital allocations with strategic targets more effectively since the capital is fully deployed without delays or fragmented capital calls. This structure minimizes gaps between intended and actual allocations and can deliver more precise portfolio management and reduce cash drag.

Moreover, evergreen funds provide built-in vintage-year diversification since new investments are continuously added over time. These portfolios typically hold more diversified positions, with evergreen vehicles often having a greater number of underlying portfolio companies compared to traditional drawdown funds.

Evergreen funds are flexible and can serve as substitutes for existing drawdown allocations or as complements to public equity investments for portfolios that don't yet have a private markets allocation. The ability to upsize or redeem allocations can also allow investors to rebalance portfolios more effectively, particularly across multiple clients, ensuring consistency for consultants or advisors.

Additionally, evergreen funds typically feature lower investment minimums, making them accessible to a broader range of investors who might otherwise face high entry barriers in traditional drawdown structures.

OPERATIONAL BENEFITS

Evergreen funds can ease some operational burdens by simplifying cash management and reducing the administrative workload associated with capital calls. With no capital calls to manage, investors do not need to keep cash on hand in anticipation of commitments. Instead, the fund manager assumes responsibility for cash management, with distributions automatically reinvested into the portfolio.

Another operational advantage lies in the elimination of the need to ladder multiple fund investments across vintage years. In drawdown structures, maintaining diversification requires underwriting multiple managers for each vintage. By continuously recycling capital into new investments, evergreen funds provide automatic exposure to different vintages, streamlining the investment process.

Evergreen funds can also offer potential liquidity options, allowing investors to redeem portions of their investment throughout a fund's life. While private equity can typically perform best as a long-term investment, the evergreen structure facilitates periodic liquidity on a typically quarterly basis, with redemptions generally capped at a set percentage of the fund's assets. These established liquidity parameters can protect both investors and managers, offering some flexibility while seeking to preserve the fund's stability and returns.

[3] Vista Equity Partners, 11/2024. For illustrative purposes only.
[4] Vista Equity Partners, 11/2024. For illustrative purposes only.

Diversifying Alternatives Exposure Through Enterprise Software

THE EVOLUTION OF EVERGREEN FUNDS

Until 2024, there were few direct private equity-focused evergreen funds. Financial advisors were astute to include diversified fund of funds (FoFs) as portfolio building blocks, absent the ability to invest in direct private equity-focused evergreen funds. These FoF vehicles can often hold several hundred or thousands of underlying company investments and offer broad diversification within a single fund. This helps to mitigate risks by spreading exposure across many holdings and sectors while also delivering index-like returns. Today, investors can invest in direct private equity-focused evergreen funds which can serve as a complement to more diversified evergreen funds. This portfolio construction approach replicates the way many investors think about their public equity allocations.

DIFFERENTIATED EXPOSURE

For investors already embracing evergreen fund structures, introducing exposure to more specialized evergreen funds – such as those focused on enterprise software or other sectors – can offer differentiated return drivers and more effectively complement existing allocations.

WHY ENTERPRISE SOFTWARE STANDS OUT

1. Mission Criticality:
Enterprise software systems are deeply embedded into business operations, often delivering essential functions with high recurring revenue and customer retention. Like infrastructure, software is often the last expense businesses turn off, even during downturns, reinforcing its resilience and reliability.

2. End-Market Diversification:
Software extends across all sectors, from healthcare and finance to logistics and education, providing exposure to multiple industries and mitigating concentration risk. This allows investors to benefit from varied economic drivers.

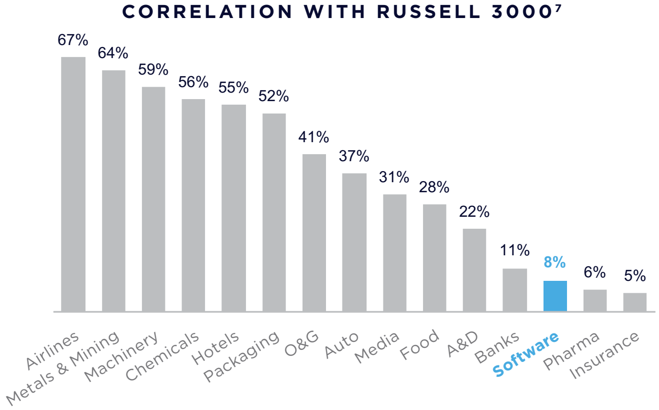
3. Low Correlation With Public Markets:
Enterprise software investments exhibit low correlation to the Russell 3000 Index and even to other individual software companies, offering unique diversification benefits.[5] These characteristics make enterprise software investments attractive as risk-adjusted positions in broader portfolios.

4. Avoids Public Market Concentration Risks:
Public markets have become increasingly concentrated, as demonstrated by the outsized influence of the "Magnificent Seven," the seven largest tech companies in the U.S. stock market. In 2023, these companies drove more than half the S&P 500 Index's gains, trading at high valuations and making up roughly 31% of the index. Because more than 96% of enterprise software companies are privately held,[6] most investors miss out on this critical segment unless they allocate capital to private markets.

5. Generative AI Innovation:
Enterprise software companies are well positioned to benefit from and integrate generative artificial intelligence (Gen AI) capabilities into their platforms. Their ability to leverage proprietary data, robust infrastructure and existing user bases may enable them to develop and deploy advanced Gen AI-driven products and features that can drive efficiency, enhance end-customer return on investment (ROI) and create new revenue streams. Enterprise software can offer investors exposure to the transformative benefits of Gen AI without relying solely on public market investments.

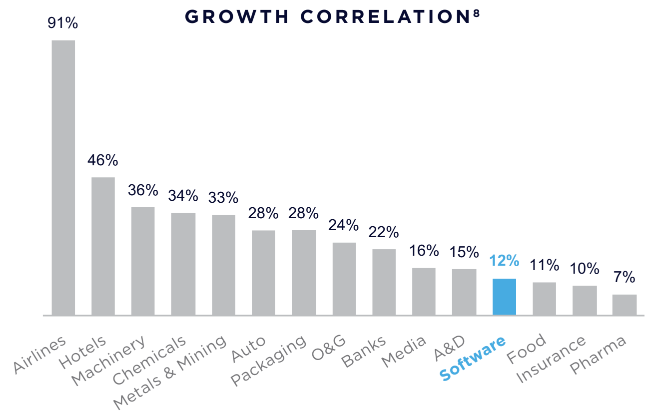
SOFTWARE EXHIBITS LOW CORRELATION TO THE BROADER MARKET AND OTHER SOFTWARE COMPANIES

INDUSTRY MEDIAN YOY REVENUE GROWTH CORRELATION WITH RUSSELL 3000[7]



Software Revenue Growth Is Non-Cyclical and Driven by Secular Forces

AVERAGE INTERNAL YOY REVENUE GROWTH CORRELATION[8]



Varied Product Sets and End Markets Drive Industry Diversity Within Software

[5] Bloomberg, as of 12/31/2022. For each sector in the Russell 3000, historical correlation between quarterly YoY revenue performance between companies in that sector and the entire index (correlation with index).
[6] Vista proprietary research in collaboration with third party independent consult, as of 09/2024.
[7] Bloomberg, as of 12/31/2022. For each sector in the Russell 3000, historical correlation between quarterly YoY revenue performance between companies in that sector and the entire index (correlation with index).
[8] Bloomberg, as of 12/31/2022. For each sector in the Russell 3000, historical correlation between quarterly YoY revenue performance between companies in that sector and one another (average internal correlation).

Evaluating Evergreen Fund Managers

VALUE CREATION

Unlike traditional private equity models, which rely on specific "vintages," evergreen funds require steady returns over time. The ability to generate consistent returns across various market environments is paramount, and managers of evergreen funds should have a systematic approach to value creation. While each company is unique, many underlying business models share similar fundamentals, making a repeatable approach a solid starting point for driving value.

In the era of near-zero interest rates, the asset management industry often relied heavily on multiple expansion – boosting valuations without significant operational improvements. However, today, that tailwind has faded. Now, general partners who excel at operational improvements – such as increasing efficiency, managing costs and improving profitability – are better positioned to produce consistent results.

DEAL SOURCING

Robust deal sourcing plays a key role in sustaining returns, as ideally, evergreen funds continually find and invest in new opportunities across market cycles. Scale and experience are also crucial, as larger platforms often have access to broader networks and resources that enhance deal flow. A longstanding track record of identifying investments and sustaining performance throughout market cycles can ensure a manager can recycle capital effectively while supporting growth.

PORTFOLIO CONCENTRATION AND STRATEGY FOCUS

Many evergreen strategies have hundreds of investments which results in diversified funds with exposure to private markets. With a more focused approach, specialized managers who select tens of investments instead of hundreds can prioritize value creation through targeted operational improvements while still maintaining the flexibility to recycle capital and capture long-term growth opportunities.

FEE STRUCTURE

Investors should carefully evaluate fee structures, as they can vary widely across evergreen private equity funds. Like traditional private equity funds, evergreen funds typically charge a management fee, calculated as a percentage of assets under management. Additionally, many evergreen funds often charge performance or incentive fees based on the returns they generate. In some cases, a hurdle rate is applied, where performance fees are only charged if the fund achieves a minimum rate of return, which can help align the interests of the fund managers and investors.

APPROACH TO LIQUIDITY MANAGEMENT

Given the illiquid nature of the underlying investments, understanding a manager's approach to liquidity is important for investors considering evergreen funds. The effectiveness of these strategies depends on how well a manager balances the need for cash reserves to meet redemptions without adversely impacting the fund's portfolio. Investors should closely evaluate whether the manager has a well-defined strategy to avoid asset sales during potential periods of high redemption activity. Additionally, typical industry practices, such as capping quarterly repurchases at 5% of the fund's net asset value, can provide insight into how managers align liquidity with long-term investment goals.

Situations Where Drawdown Funds May Be Preferable

Drawdown structures can be advantageous for investors with the resources and flexibility to actively manage their private equity exposure. For large institutions with dedicated portfolio management teams, drawdown funds allow for the customization of a series of commitments across multiple vintages, creating a diversified exposure over time. This structure is also well-suited for investors who prefer to handpick multiple managers across specific strategies, geographies and sectors. Additionally, for those with strong views on particular vintage years, drawdown funds offer the ability to concentrate investments during favorable periods. Investors who prefer to control liquidity on their own terms may also find drawdown structures appealing.

Final Thoughts

Evergreen funds present an efficient solution for investors seeking diversification and operational efficiency. By deploying capital immediately, evergreen funds enable the compounding effect and reduce the friction associated with capital calls. This structure not only aligns investments with natural growth cycles but can also provide flexibility to unlock long-term value.

By incorporating differentiated, specialized strategies, investors can access opportunities in private, high-growth sectors that may otherwise be missed. In today's market environment, where operational excellence is critical for success, selecting the right evergreen fund manager becomes even more essential.

Key Benefits of Evergreen Funds for Private Market Investors

1 **LOWER BARRIERS TO ENTRY**

Evergreen funds have lower investment minimums than traditional drawdown funds.

2 **NO CAPITAL CALLS**

Avoid the administrative burden and cash drag associated with capital calls.

3 **LONG-TERM COMPOUNDING**

Immediate capital deployment enables steady compounding over time.

4 **GREATER LIQUIDITY**

While still a long-term investment, evergreen funds offer periodic redemption opportunities.

5 **DIVERSIFICATION**

Evergreen funds provide vintage-year diversification and usually hold a larger number of portfolio companies than drawdown funds.

6 **HIGH-GROWTH SECTORS**

Specialized evergreen funds can offer targeted exposure to high-growth sectors.

For more information, visit:

vistaequitypartners.com/strategies/private-wealth-solutions |

VISTA

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