

NAV and Fund Finance: Liquidity for GCC Managers

NAV facilities, subscription lines and the wider fund-finance toolkit as portfolio-level liquidity instruments, and a framework for judging when they serve limited partners

Chennakeshav (CK) Adya

Independent Researcher

July 2026

ABSTRACT

Background. Fund-level borrowing has moved from a bridging convenience to a strategic instrument. Subscription lines, net asset value (NAV) facilities, hybrid facilities, financing of the general partner (GP) and management company, preferred equity and structured secondaries now form a recognisable toolkit, yet debate about NAV finance in particular has become polarised between enthusiasm and alarm. **Objective.** This paper gives Gulf Cooperation Council (GCC) fund managers, and the family-office chief investment officers who sit on their limited partner advisory committees (LPACs), a structural framework for deciding when portfolio-level liquidity creates value for limited partners (LPs) and when it merely shifts it. **Approach.** The paper organises the toolkit as a spectrum of claims against different collateral, from undrawn commitments at one end to portfolio value at the other. It develops five propositions from agency theory, secured-lending theory, the secondaries literature and the performance-measurement literature, then applies a formal sizing and alignment framework to three fully worked cases: a mid-life buyout fund bridging an exit, a tail-end fund accelerating distributions, and a GP financing its own commitment. The base-case calibrations behind every exhibit, drawn from market convention and the author's transaction experience, are recorded in full. **Findings.** NAV finance creates LP value only when the marginal return on the financed use exceeds the all-in cost of the facility and the cheapest alternative is more expensive; distribution acceleration is at best value-neutral and primarily improves reported IRR; concentration and carry proximity raise the agency cost of fund-level debt. **Implications.** GCC managers face a distinctive alignment calculus: concentrated, relationship-driven LP bases make genuine consent easier to obtain and quiet leverage far more damaging when discovered.

Highlights

- Fund finance is a spectrum of claims, from undrawn commitments to portfolio value
- A NAV draw must beat its all-in cost; base-case breakeven is 1.15x over two years
- Accelerating distributions is IRR-cosmetic: roughly value-neutral for LPs at best
- Concentrated GCC LP bases make consent easier and non-disclosure costlier
- A five-question alignment test separates value-creating from value-shifting draws

JEL Classification: G23, G24, G32, G33, G11

Keywords: NAV facilities, fund finance, subscription lines, private equity, GCC, limited partners, fund-level leverage, secondaries

This paper is an educational and structural analysis prepared for research purposes. It is not investment advice, an offer, or a solicitation. It contains no client information.

1. INTRODUCTION

A manager in year seven of a ten-year buyout fund faces a familiar squeeze. The portfolio is performing but slow to exit. One company needs follow-on capital that the fund's undrawn commitments can no longer supply. Two anchor limited partners, both Gulf family offices, are asking, politely but repeatedly, when distributions will resume. The manager's next fundraise depends on demonstrating distributions to paid-in capital, yet selling a good asset into a soft market to manufacture liquidity would destroy exactly the value the fund was formed to capture. Into this squeeze steps a lender offering a facility secured on the net asset value of the portfolio: five to fifteen per cent of NAV, available in weeks, no asset sale required.

Whether to accept is not a financing decision in the narrow sense. It is a decision about whose money bears what risk, in what order, for whose benefit. Fund-level debt sits senior to every limited partner. Drawn to fund a follow-on investment that succeeds, it is cheap capital that avoided a dilutive alternative. Drawn to accelerate distributions that were coming anyway, it is an interest bill charged to the partnership so that the reported internal rate of return looks better in the next fundraising deck. The same instrument, the same term sheet, can be either. The difference lies entirely in the use of proceeds, the state of the portfolio, and the governance surrounding the draw.

This paper addresses that decision for a specific audience: managers of private equity, private credit and real-asset funds based in or raising from the Gulf Cooperation Council, and the family-office chief investment officers and heads of alternatives who sit on limited partner advisory committees and must evaluate a manager's request to lever the fund. The GCC setting is not incidental. Limited partner bases in the region are concentrated, relationship-driven and often anchored by a small number of sovereign or family investors; a portion of the capital is sharia-sensitive; and the regional banking market prices fund collateral differently from the specialist fund-finance desks of London and New York. These features change the alignment calculus in ways the international commentary, written for funds with hundreds of institutional LPs, does not capture.

The paper asks three research questions. **RQ1:** How should the instruments of fund finance, subscription lines, NAV facilities, hybrid facilities, GP and management-company financing, preferred equity and structured secondaries, be organised analytically, and what determines which instrument fits which situation? **RQ2:** Under what conditions does a NAV facility create value for limited partners rather than transfer it to the manager or the lender, and how can that condition be expressed as a test a manager and an LPAC can actually apply? **RQ3:** How does the GCC institutional environment, concentrated LP bases, sharia-sensitive pools and regional bank appetite, alter the answer relative to the United States and Europe?

The paper makes four contributions. **First**, it organises the fund-finance toolkit as a single spectrum of claims against different collateral, running from undrawn commitments at one end to realised portfolio value at the other, and shows that most structuring questions reduce to locating the fund correctly on that spectrum. **Second**, it develops five propositions from established finance theory, agency costs of delegated management, debt overhang, liquidation values and collateral, and the measured effect of fund-level credit on reported performance, and carries those propositions through the analysis rather than leaving them decorative. **Third**, it builds a transparent sizing and alignment framework, calibrated to market convention and recorded in full, and applies it to three worked cases that span the legitimate-to-contentious range: bridging an exit, accelerating distributions, and financing the GP itself. **Fourth**, it translates the results into separate, actionable guidance for the GCC manager contemplating a facility and for the LP or LPAC member asked to bless one, including a negotiation and disclosure checklist.

The argument, compressed: NAV finance is neither a scandal nor a free lunch. It is senior capital with a running cost, and it creates value for limited partners exactly when the marginal return on what it finances exceeds its all-in cost and the cheapest alternative source of the same liquidity is more expensive. That

condition is demanding but checkable. It fails most obviously when proceeds accelerate distributions the portfolio would have produced anyway, and it fails dangerously when a concentrated portfolio meets a manager whose carried interest is out of the money, because fund-level debt then finances an option whose downside belongs to the LPs.

The remainder of the paper proceeds as follows. Section 2 reviews four strands of literature and states the propositions. Section 3 sets out the institutional context, global and GCC-specific. Section 4 defines the sizing and alignment framework and records its base-case calibrations. Section 5 analyses the toolkit instrument by instrument. Section 6 applies the alignment test to three worked cases. Section 7 examines sensitivity and robustness, names a worst case, and states what would falsify the claims. Section 8 draws implications for managers and for LPs, with an international comparison. Section 9 acknowledges limitations and outlines future research. Section 10 concludes.

2. LITERATURE REVIEW AND PROPOSITIONS

Four strands of literature bear on the fund-finance decision. None addresses NAV facilities directly at length; each supplies a piece of the machinery. This section takes them in turn and closes each with its implication for the Gulf setting, before stating five propositions that the rest of the paper develops.

2.1 Agency Theory in Delegated Management

The foundational result of Jensen and Meckling (1976) is that separating ownership from control creates costs that contracting can reduce but not eliminate. A private equity fund is a deliberately extreme case of delegation: limited partners commit capital for a decade, surrender control over its deployment, and rely on a compensation contract, management fee plus carried interest, to align the general partner's incentives with their own. Metrick and Yasuda (2010) document how much of GP compensation is fixed rather than performance-linked, and Chung, Sensoy, Stern and Weisbach (2012) show that a large share of the true incentive comes not from the current fund's carry but from the effect of current performance on future fundraising. Gompers and Lerner (1996) show that where incentive alignment is weak, partnership agreements substitute explicit covenants, restrictions on leverage among them.

Fund-level borrowing enters this machinery in two ways. First, it changes the payoff structure: debt senior to the LPs makes the LPs' residual claim more option-like, and a GP whose carry is under water gains from volatility that the LPs would not choose, the classic risk-shifting problem. Second, it interacts with the fundraising incentive identified by Chung and co-authors and by Barber and Yasuda (2017): if fund-level credit can improve interim reported performance, and interim performance drives the next fund's size, the GP has a private benefit from borrowing that is unrelated to portfolio value. Brown, Gredil and Kaplan (2019) find that pressure on reported returns is strongest for managers currently in the market, precisely the moment at which distribution-accelerating facilities are most tempting.

Implication for the Gulf. GCC funds are typically anchored by a handful of large, repeat relationships rather than hundreds of arm's-length institutions. Reputational discipline is therefore stronger per LP, but formal covenant discipline is often weaker, because older regional LPAs were drafted before NAV finance existed and are silent on it. The agency problem does not shrink; it moves from the contract to the relationship.

2.2 Capital Structure, Collateral and Secured Lending

Three classic results organise the lender's side. Myers (1977) shows that debt overhang can cause a borrower to pass up positive net present value investments because the gains accrue partly to existing creditors; a fund whose NAV facility is near its loan-to-value covenant faces exactly this distortion when weighing a follow-on investment. Myers and Majluf (1984) establish the pecking order: when insiders know more than outsiders,

financing that is least information-sensitive is cheapest, which is why a facility secured on a diversified borrowing base can undercut a secondary sale of the same assets, the sale price of which must absorb the buyer's adverse-selection discount. Shleifer and Vishny (1992) show that the debt capacity of an asset depends on the liquidation value to the next-best user, and that this value is lowest exactly when the whole industry is distressed; a NAV lender's advance rate against a concentrated portfolio embeds this insight, which is why concentration haircuts are universal.

On the intermediation side, Diamond (1984) explains why a monitoring lender can hold claims that dispersed investors cannot: the bank economises on duplicated monitoring. Holmstrom and Tirole (1997) add that borrower net worth, here the equity cushion below the facility, determines access to intermediated finance, and that shocks to intermediary capital tighten lending exactly when borrowers most need it. Hart and Moore (1994) ground the whole structure: because the manager's human capital is inalienable, lenders lend against what can be seized, which in a fund is the right to intercept distributions rather than the assets themselves. This is why NAV facilities are overwhelmingly structured as security over distribution accounts and equity interests in holding vehicles, not as mortgages over operating companies.

Implication for the Gulf. Regional banks have deep experience lending against real assets and trade flows but thinner experience underwriting diversified fund portfolios; the Diamond monitoring advantage sits mostly with international fund-finance desks. GCC managers should therefore expect the local bid for NAV risk to be narrower, more collateral-literal and more relationship-priced, and should expect sharia-compliant structures (commodity murabaha funding legs, for example) to add documentation time and a modest cost premium.

2.3 Liquidity Management in Private-Markets Portfolios and the Secondaries Literature

The alternative to borrowing against a portfolio is selling part of it. Nadauld, Sensoy, Vorkink and Weisbach (2019) document that secondary-market sales of fund interests transact at meaningful discounts to reported NAV and that the discount widens when sellers need liquidity quickly; the secondary market is a real but expensive liquidity channel. Sorensen, Wang and Yang (2014) show that the certainty-equivalent value of an illiquid private equity position to a constrained investor is well below its reported NAV, which explains why LPs themselves sometimes prefer the fund to raise liquidity centrally rather than each LP selling its interest at a discount individually. Ang, Chen, Goetzmann and Phalippou (2018) show how much apparent smoothness in private-market returns is an artefact of appraisal-based NAVs, a warning that the borrowing base of a NAV facility is an estimate, not a price.

This strand frames the manager's true choice set. Portfolio-level liquidity can come from four places: asset exits, a secondary sale of a strip of assets, LP-level solutions such as tender offers, or fund-level credit. Each has a cost: exits sacrifice timing, strip sales pay the adverse-selection discount of Myers and Majluf (1984) plus the empirical secondary discount, and credit pays a running spread and subordinates the LPs. The right comparison for a NAV facility is never credit versus nothing; it is credit versus the cheapest of these alternatives.

Implication for the Gulf. The institutional secondary bid for GCC-managed portfolios is thinner and slower than for pan-European or US portfolios, so the realistic alternative cost against which a facility is judged is higher in the Gulf. This widens the range of situations in which NAV finance is the value-maximising channel, and it is the honest core of the case for the instrument regionally.

2.4 Fund-Level Leverage and Performance Measurement

The measurement literature explains why fund-level credit is controversial even when economically benign. Kaplan and Schoar (2005) and Harris, Jenkinson and Kaplan (2014) established the modern benchmarks for

fund performance, IRR, multiples and public market equivalents, and Phalippou and Gottschalg (2009) and Phalippou (2014) document how sensitive headline performance is to methodological choices. Subscription credit lines interact directly with this apparatus: by delaying capital calls, they shorten the measured duration of LP cash flows and mechanically raise IRR without changing the multiple of money. Axelson, Stromberg and Weisbach (2009) provide the deeper structural point: the fund form itself, ex-ante committed capital deployed deal by deal, exists to control agency problems, and leverage decisions inside that form alter the option value of the GP's compensation, a theme extended empirically by Axelson, Jenkinson, Stromberg and Weisbach (2013), who show that buyout leverage responds to credit conditions rather than to firm characteristics, evidence that cheap available credit gets used because it is available. Robinson and Sensoy (2013) show that fee and ownership structures, not just gross returns, determine what LPs actually keep, which is precisely the net-of-costs lens this paper applies to facility economics.

Implication for the Gulf. GCC LPs comparing managers on IRR across funds with different financing practices are comparing unlike with unlike. Family offices with small investment teams are more exposed to this than large institutions with performance-analytics staff, so disclosure of levered versus unlevered performance matters more, not less, in the Gulf.

2.5 Propositions

The four strands combine into five propositions carried through Sections 5 to 8.

Proposition 1 (Spectrum). Fund-finance instruments are ordered by the collateral they claim: undrawn commitments (subscription lines) at one end, portfolio value (NAV facilities, preferred equity) at the other, with hybrids between. The efficient instrument matches the fund's life stage to the collateral that is most valuable and least information-sensitive at that stage; mismatch, such as portfolio-secured borrowing by a young fund, signals either constraint or opportunism.

Proposition 2 (Value test). A NAV draw creates LP value if and only if the marginal net return on the financed use exceeds the all-in cost of the facility over its life, and no alternative channel (exit, strip sale, tender) delivers the same liquidity more cheaply. Where proceeds fund distributions the portfolio would have generated anyway, the draw is at best value-neutral for LPs and improves only reported IRR.

Proposition 3 (Risk-shifting). The agency cost of fund-level debt rises with portfolio concentration and with the distance of the GP's carried interest from its hurdle. A concentrated portfolio plus out-of-the-money carry is the configuration in which NAV borrowing is most likely to destroy LP value, because the GP holds a levered option on assets the LPs own.

Proposition 4 (Governance substitution). Where LPAs are silent, governance quality, meaning explicit LPAC consent, full disclosure of terms and reporting of levered and unlevered performance, substitutes for contractual discipline. In concentrated, relationship-driven LP bases, obtaining genuine consent is easier and the reputational penalty for undisclosed leverage is larger; both effects are stronger in the GCC than in dispersed institutional markets.

Proposition 5 (Regional form). Sharia-sensitivity of part of the capital base and regional bank collateral practice push GCC fund finance toward asset-literal and hybrid structures, murabaha-based funding legs, and preferred-equity substitutes for conventional NAV debt, at a modest cost premium and longer documentation timelines.

3. INSTITUTIONAL AND MARKET CONTEXT

3.1 The Rise of Fund Finance Globally

Fund finance began as a housekeeping product. Subscription credit lines, revolving facilities secured on the unfunded commitments of investors, emerged decades ago so that managers could close deals in days and call capital in orderly quarterly batches. The product was uncontroversial for as long as it bridged capital calls for a few weeks. Over the past fifteen years three things changed. First, tenors lengthened: bridging weeks became bridging quarters, and the measured-IRR effect described in Section 2.4 turned an administrative tool into a performance-optics tool, prompting institutional guidance; ILPA, the institutional limited partners' association, has published recommendations on both subscription lines and, more recently, NAV-based facilities, and the direction of that guidance is consistently toward disclosure, LP consent and reporting of performance with and without the effect of fund-level credit. Second, the lender base broadened from a handful of subscription-line banks to a market that includes insurers, private credit funds and specialist NAV lenders, which pushed products up the fund's life cycle: if the early years belong to the subscription line, the later years now have a dedicated instrument in the NAV facility. Third, the exit drought that followed the 2022 rate reset left many funds long assets and short distributions simultaneously, and NAV finance moved from niche to headline, attracting both genuine demand and genuine criticism.

The criticism deserves to be stated fairly, because this paper's framework must answer it. Critics argue that NAV facilities let managers avoid the discipline of selling, that they subordinate LPs without fresh consent under LPAs drafted before the product existed, that proceeds have in prominent cases funded distributions rather than investments, and that borrowing against appraisal-based NAVs during a valuation standoff is borrowing against a number nobody would pay. Defenders reply that the facilities are small relative to portfolio value, cheaper than secondary sales, and often the only way to fund value-accretive follow-ons late in a fund's life. Both descriptions are accurate for different transactions. That is precisely why a use-of-proceeds framework, rather than a verdict on the instrument, is the right unit of analysis.

3.2 GCC Specifics

Three features distinguish the Gulf setting, and each reshapes the alignment calculus.

Concentrated, relationship-driven LP bases. A typical GCC-managed fund is anchored by a small number of sovereign-linked investors, family offices and merchant families, often with the anchor holding a stake large enough that its individual consent is decisive. This concentration cuts both ways. Consent is genuinely obtainable: a manager can convene the three investors who matter within a week, which no pan-European fund can do. But the same concentration means an anchor LP discovering undisclosed fund-level leverage is not one disappointed institution among two hundred; it is the relationship on which the franchise rests. Proposition 4 formalises this: governance substitutes for contract, and both the ease of consent and the cost of concealment are amplified.

Sharia-sensitive pools. A material share of regional capital operates under sharia constraints that prohibit conventional interest-bearing debt at the entity level or restrict the purposes for which financing may be raised. In practice this does not remove fund finance from the toolkit; it reshapes it. Facilities are structured with commodity murabaha or wakala funding legs, screening applies to the use of proceeds, and some LP sleeves require that their capital not be commingled with conventional leverage at all, which drives parallel-vehicle structures. The economic substance of the alignment test in Section 4 is unchanged, but documentation is longer, the lender universe is narrower, and preferred-equity structures, which sit more comfortably within some sharia frameworks than debt, gain relative attractiveness. This is Proposition 5.

Regional bank appetite. GCC banks are well capitalised and liquid, but their collateral culture is built on real estate, trade finance and name lending. Underwriting a diversified borrowing base of unlisted equity stakes is a different discipline, one concentrated in international fund-finance desks that may treat the region as a marketing destination rather than a booking centre. The practical consequence for a GCC manager is a barbell: relationship-priced facilities from regional banks for simple, asset-literal structures, and international pricing for genuine NAV risk, with a thinner middle than managers in London would expect. Sizing expectations should be set accordingly.

3.3 Why the Question Is Live Now

The regional fund ecosystem is young. Many GCC managers are on fund one or fund two, exactly the vintages where distributions to paid-in capital determine whether fund three exists. Meanwhile regional LPs, having absorbed the international debate, are beginning to ask fund-finance questions in due diligence: whether the LPA permits NAV borrowing, what the manager's policy is, and how performance will be reported. A manager without considered answers is now at a fundraising disadvantage regardless of whether a facility is ever drawn. The framework that follows is intended to be that considered answer.

4. DATA AND METHODOLOGY

4.1 Nature of the Framework

The framework developed here is structural. It makes the economics of a fund-level facility explicit, comparable to alternatives, and inseparable from the governance surrounding the draw. The calibrations that drive the exhibits reflect prevailing convention in the fund-finance market and the author's transaction experience in the region, and they are recorded in full in Appendix A so that a reader can re-run the arithmetic on the parameters of a live situation in minutes. The framework's boundaries are stated in Section 4.5.

4.2 The Sizing Framework

The sizing framework maps a fund's portfolio to a facility size in four steps, mirroring standard lender practice qualitatively.

Step 1: Gross NAV. The reported net asset value of the portfolio, acknowledged to be an appraisal-based estimate (Section 2.3).

Step 2: Eligible NAV (the borrowing base). Gross NAV reduced by exclusions and haircuts: assets below minimum diversification thresholds, assets in restricted jurisdictions, and concentration caps that limit the contribution of any single asset, with no single asset counted beyond 20 per cent of the borrowing base being a common formulation, alongside aggregate caps on the largest few positions.

Step 3: Advance rate. A loan-to-value (LTV) ratio applied to eligible NAV. NAV facilities on diversified buyout portfolios typically carry LTV limits of 5 to 15 per cent of gross NAV, and 10 per cent is the base case used throughout; advance rates rise towards 25 per cent for highly diversified or credit portfolios and fall towards 5 per cent for concentrated tail-end pools.

Step 4: The cost stack. All-in cost equals a reference rate plus a margin, plus non-margin items amortised over the expected life of the draw: arrangement fee, commitment fee on undrawn amounts, legal and agency costs. The base case uses a reference rate of 4.0 per cent, a margin of 3.0 per cent, an arrangement fee of 1.0 per cent flat and a commitment fee of 0.5 per cent per annum on undrawn amounts, consistent with mid-market terms for diversified portfolios.

4.3 The Alignment Test

The alignment test asks five questions of any proposed draw. It operationalises Propositions 2 to 4.

Q1: Use. What, precisely, do the proceeds fund, and would the fund pursue that use if it had uncalled capital available?

Q2: Marginal return versus all-in cost. Let the draw be D , the expected gross multiple on the financed use over horizon T be m , and the all-in cost of the facility over T (interest plus amortised fees) be C . The draw passes the value test if the expected net gain $G = D(m \text{ minus } 1) \text{ minus } C$ is positive with a margin of safety, and fails if G is negative under the manager's own base case.

Q3: Cheapest alternative. Is there a channel (asset exit, strip sale, LP tender, delayed action) that delivers the same liquidity at lower cost than C , after honest accounting for discounts and forgone upside?

Q4: Risk configuration. How concentrated is the portfolio, and where does the GP's carry sit relative to its hurdle? A draw that passes Q2 on expected values can still fail alignment if it is, in substance, a volatility purchase by an out-of-the-money GP (Proposition 3).

Q5: Governance. Does the LPA authorise the borrowing at fund level, at what limit, and has the LPAC been asked in a form that permits genuine refusal, with terms, security, use of proceeds and both levered and unlevered performance reporting disclosed?

A draw that passes all five questions is treated as value-creating for LPs; a draw that fails Q2 or Q3 is value-shifting; a draw that passes Q2 and Q3 but fails Q4 or Q5 is value-at-risk, economically defensible but structurally unsafe.

4.4 Base-Case Calibrations

The analysis runs on three vehicles. **Fund A** is a mid-life buyout fund: committed capital USD 500 million, gross NAV USD 400 million in year seven of a ten-year term, ten portfolio companies, largest position 18 per cent of NAV and top three positions 45 per cent. **Fund B** is a tail-end fund: gross NAV USD 150 million in year eleven of an extended term, four remaining assets, largest position 40 per cent of NAV. **GP Co** is the management company of Fund A's manager, with a GP commitment to Fund A of USD 10 million, 2 per cent of commitments. Facility parameters, return calibrations for financed uses, the secondary-sale discount and the LP reinvestment rate are listed in Appendix A, and every number appearing in Sections 5 to 7 traces to that table.

4.5 What the Framework Does and Does Not Do

The framework does three things: it makes the cost of fund-level credit explicit and comparable to alternatives; it separates the effect of a draw on LP value from its effect on reported IRR; and it forces the governance question into the same analysis as the economics. It does not do four things. It does not price facilities, since pricing is a market outcome. It does not model the lender's behaviour in default beyond stylised covenant mechanics. It does not resolve valuation uncertainty in the borrowing base; it inherits whatever error the NAV contains. And it does not substitute for legal review of any actual LPA, side letter or facility agreement. It is an economic screen, deliberately upstream of documentation.

5. THE FUND-FINANCE TOOLKIT

5.1 The Spectrum

Proposition 1 holds that the toolkit is best understood as a single spectrum ordered by collateral. At one end sits the subscription line, a claim on money that has not yet entered the fund: the undrawn commitments of investors, enforceable through the right to call capital. At the other end sit NAV facilities and preferred equity, claims on money that is already at work: the value of the portfolio itself, enforceable through security over distribution flows and holding-vehicle equity. Between them sit hybrid facilities, which look to both pools, and alongside the fund sit GP and management-company financings, which claim the manager's own economics rather than the LPs' capital. Figure 1 arranges the instruments on two axes: the life stage of the fund at which each is naturally used, and the collateral against which each is secured.

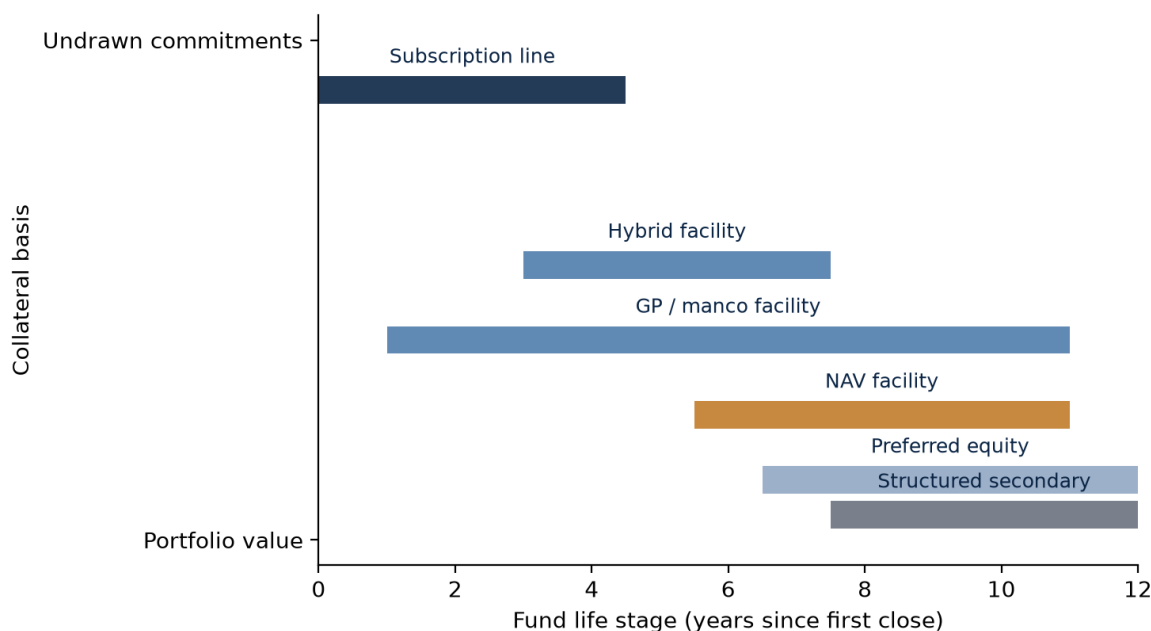


Figure 1. The fund-finance spectrum: instruments by fund life stage and collateral basis.

Source: author's analysis.

The spectrum has an economic logic, not merely a chronological one. Early in a fund's life, undrawn commitments from creditworthy investors are the least information-sensitive asset the fund possesses: a lender needs to underwrite the LPs, not the portfolio, and pricing is correspondingly tight. Late in a fund's life the position inverts. Undrawn commitments are exhausted, and the portfolio, however hard to value, is the only collateral there is. Following Myers and Majluf (1984), each instrument is cheapest when it is secured on the asset about which the least private information exists at that moment. A young fund reaching for portfolio-secured debt, or an old fund straining to lever residual commitments, is working against the grain of the spectrum, and the pricing and the covenants will say so. Table 1 compares the instruments.

Table 1. The fund-finance toolkit compared.

Instrument	Collateral	Typical stage	Advance / size	Pricing order	Primary LP risk
Subscription line	Undrawn commitments	Years 0 to 4	15 to 25% of undrawn	Reference + 150 to 250 bps	IRR distortion; call risk at maturity
NAV facility	Portfolio value	Years 5 to 11	5 to 15% of NAV	Reference + 250 to 450 bps	Subordination; covenant-driven

					sweeps
Hybrid facility	Both pools	Years 3 to 7	Blended base	Between the two	Complexity; creeping reliance
GP / manco facility	Fee stream, carry	Any	0.5 to 1.5x annual fees	Reference + 400 bps and up	Manager distraction; key-person stress
Preferred equity	Portfolio value (junior)	Years 6 to 12	10 to 25% of NAV	12 to 16% expected return	Expensive capital; waterfall dilution
Structured secondary	Assets sold or stapled	Years 7 to 12	Priced per asset	Discount to NAV	Adverse selection on what is sold

Source: author's analysis.

5.2 Subscription Lines

The subscription line is the workhorse and needs the least introduction. Secured on the right to call undrawn commitments, supported by investor letters or by the LPA's acknowledgement of the lender's step-in rights, it bridges capital calls so that deals close on the manager's timetable and LPs receive orderly, batched drawdowns. Facilities typically advance against a borrowing base of eligible, investment-grade-equivalent commitments, with concentration limits by investor, and run at margins in the range of 150 to 250 basis points over the reference rate, the tightest pricing in the toolkit because the collateral is the strongest.

Two disciplines keep the instrument benign. The first is tenor: a line that cleans down within two or three quarters is an administrative tool; a line that stays drawn for years is synthetic leverage that shortens the measured duration of LP cash flows and flatters IRR, the effect documented in the performance-measurement literature reviewed in Section 2.4. The second is disclosure: reporting performance both with and without the effect of the line, which ILPA guidance has pushed towards standard practice, removes the optics motive entirely. A GCC-specific note: because regional LP bases are concentrated, a single anchor investor's credit standing can dominate the borrowing base, so the practical debt capacity of a GCC fund's subscription line is often set by one or two names, and a downgrade or a side-letter transfer restriction on that name reprices the whole facility.

5.3 NAV Facilities

The NAV facility is the instrument this paper exists to examine. Structurally, the lender advances against the value of the portfolio, secured not on the operating companies themselves but on the chain through which value reaches the fund: pledges over the equity of aggregator or holding vehicles, security over the bank accounts into which disposal proceeds and dividends flow, and covenants that intercept those flows if performance deteriorates. Following Hart and Moore (1994), the lender takes what can be seized, and what can be seized in a fund is the distribution waterfall.

The defining mechanics are four. **The borrowing base** applies eligibility criteria and concentration caps to gross NAV, as set out in Section 4.2. **The LTV covenant** is the heart of the document: the facility might be advanced at 10 per cent LTV with a cash-sweep trigger at 15 per cent and an event of default at 20 to 25 per cent, so that a fall in NAV tightens the structure progressively rather than abruptly. **The cash sweep** redirects some or all distributions to prepayment once a trigger is hit, which is precisely when LPs most want liquidity, a feature LPs should price before consenting. **The cure and valuation machinery** governs who values the portfolio, how often, and what happens when manager and lender disagree; quarterly manager valuations with a lender right to commission an independent valuation on trigger events is the standard compromise.

Table 2 sizes the base-case facility for Fund A and assembles its cost stack.

Table 2. Sizing and cost stack for a NAV facility on Fund A.

Item	Value
Gross NAV	USD 400 million
Eligible NAV after haircuts (80% of gross)	USD 320 million
Advance at 12.5% of eligible (10% of gross NAV)	USD 40 million
Running cost: reference 4.0% + margin 3.0%	7.0% per annum
Arrangement fee at 1.0% flat	USD 0.4 million
Interest over a two-year draw	USD 5.6 million
All-in two-year cost	USD 6.0 million
Breakeven multiple on financed use over two years	1.15x

Source: author's analysis. Two-year cost assumes the facility is fully drawn at close.

The final row of Table 2 is the single most useful number in the paper. A USD 40 million draw costing USD 6.0 million over two years must finance something that returns at least 1.15 times, roughly 7.3 per cent per annum, before it adds a dollar of LP value. Everything in Section 6 is an application of that row.

5.4 Hybrid Facilities

Hybrid facilities take security over both undrawn commitments and portfolio value, and they exist because the middle years of a fund embarrass both pure instruments: undrawn commitments are no longer large enough to support the subscription line the manager wants, and the portfolio is not yet seasoned enough for a NAV lender's full confidence. The blended borrowing base lets the facility amortise its reliance from one pool to the other as the fund matures. Pricing sits between the two pure instruments. The structural risk is subtler than either parent product: because the facility can survive the exhaustion of undrawn commitments, it can become a permanent fixture rather than a bridge, and a fund that rolls a hybrid into its NAV years without a fresh alignment analysis has acquired portfolio leverage without ever deciding to. For GCC managers, the hybrid has a particular attraction under Proposition 5: regional banks that hesitate to underwrite pure portfolio risk will often lend against a base that retains a claim on sovereign-linked undrawn commitments, so the hybrid is frequently the most local-bankable structure on the spectrum.

5.5 GP and Management-Company Financing

Not all fund finance is fund-level. The manager itself borrows: against the management-fee stream, against the value of accrued carried interest, or against its balance sheet, to fund GP commitments to new vehicles, to finance succession and equity transfers among partners, or to seed operations while a first fund's fees ramp. The critical structural distinction is that the collateral is the manager's own economics. A management-company facility of USD 6 million against Fund A's fee stream, at a margin reflecting the concentration and cancellability of that stream, puts no claim on LP capital whatsoever; it is the manager borrowing against its own future income, and LPs should be broadly indifferent to it, provided key-person and change-of-control provisions in the LPA are respected and the manager's service capacity is not impaired.

The alignment problem arises when the boundary is crossed: when fund-level borrowing, secured on LP assets, funds obligations that belong to the GP, most obviously the GP commitment itself. Section 6.3 works this case. The rule that falls out is simple and worth stating early: the collateral should belong to the party whose obligation is being financed.

5.6 Preferred Equity and Structured Secondaries

When debt does not fit, because covenants would be breached, because the portfolio is too concentrated, or because part of the capital base cannot sit above conventional interest-bearing leverage, the toolkit continues past the end of the debt spectrum. Preferred equity injects capital into the fund or a holding vehicle in

exchange for a priority claim on distributions up to a fixed return, typically in the 12 to 16 per cent range, with the common equity retaining all upside beyond it. There is no covenant, no sweep, no event of default: if distributions are slow, the preferred return simply accretes. That patience is what the higher cost buys, and for concentrated tail-end pools it is often the only portfolio-level liquidity a prudent provider will offer. Under Proposition 5, preferred structures also travel better across sharia screens than conventional debt, which matters for GCC vehicles with mixed capital bases.

Structured secondaries complete the spectrum by exchanging assets rather than claims: strip sales of a portfolio slice, tender offers that give LPs individual liquidity, and continuation vehicles that move an asset to a new fund with new capital and reset economics. These are sale transactions, priced at whatever discount or premium the market sets, and they carry the adverse-selection burden identified in Section 2.3: the market assumes the manager sells what the manager least wants to keep. The relevance here is as the benchmark: every NAV facility should be priced against the honest cost of the secondary alternative, and Section 6.1 does exactly that. Where the secondary bid is thin, as it is for many GCC portfolios, the facility wins the comparison more often, which is the regionally distinctive core of the case for NAV finance.

6. THE ALIGNMENT TEST APPLIED

This section applies the five-question test of Section 4.3 to three cases that span the legitimate-to-contentious range. The arithmetic is deliberately simple enough to check by hand.

6.1 Case A: A Mid-Life Buyout Fund Bridging an Exit and Funding a Follow-On

Consider Fund A as calibrated in Section 4.4: USD 400 million of NAV in year seven, undrawn commitments exhausted, one portfolio company requiring USD 40 million of follow-on capital to complete a bolt-on acquisition ahead of a sale process expected to conclude within two years. The manager's base case is that the financed use returns 1.5 times gross over those two years. The choice set has three branches: draw a NAV facility, sell a strip of the portfolio in the secondary market at a 12 per cent discount to NAV, or decline the follow-on.

The facility. From Table 2, USD 40 million drawn for two years costs USD 6.0 million all-in. At the 1.5x base case the financed use returns USD 60 million, a net gain to the partnership of USD 14.0 million after repaying principal and costs. The breakeven is a 1.15x multiple; the manager's base case clears it with a wide margin of safety.

The strip sale. Raising USD 40 million at a 12 per cent discount requires selling assets carried at USD 45.5 million. Terminal wealth comparison makes the cost concrete. With portfolio growth of 10 per cent per annum, the debt route ends the two years with the retained portfolio grown to USD 484 million plus USD 60 million of follow-on proceeds less USD 46.0 million of principal and costs: USD 498.0 million. The strip route ends with the reduced portfolio of USD 354.5 million grown to USD 428.9 million plus the same USD 60 million: USD 488.9 million. The facility beats the strip sale by USD 9.1 million, because the strip surrenders both the discount and two years of appreciation on the assets sold.

Declining. Doing nothing ends at USD 484 million, and in practice below it, since a portfolio company that cannot fund a value-accretive bolt-on ahead of exit typically sells for less.

Case A therefore passes Q1 (the use is investment the fund would make with uncalled capital), Q2 (expected gain USD 14.0 million against a USD 6.0 million cost), and Q3 (the cheapest alternative is USD 9.1 million worse). Q4 requires a check rather than a waiver: Fund A's largest position is 18 per cent of NAV and the carry is near the money, so the draw is not a volatility purchase. Q5 then does the remaining work: LPA authority

confirmed, LPAC consent sought with full terms, levered and unlevered performance reported thereafter. This is NAV finance doing what its defenders claim.

6.2 Case B: A Tail-End Fund Accelerating Distributions

Now consider Fund B: USD 150 million of NAV in year eleven, four assets, the largest 40 per cent of the pool, exits realistically eighteen months away. The manager, in the market with a successor fund, proposes a USD 15 million facility at 10 per cent LTV, margin 3.5 per cent reflecting the concentration, to fund an immediate distribution. Nothing new is being financed; cash that would arrive in eighteen months is being moved forward.

The arithmetic is short and damning in its neutrality. Interest at 7.5 per cent on USD 15 million for eighteen months is USD 1.69 million; the 1.0 per cent arrangement fee adds USD 0.15 million; all-in cost USD 1.84 million. The benefit to LPs is the time value of receiving USD 15 million early. At an LP reinvestment rate of 8 per cent per annum, eighteen months of reinvestment earns USD 1.84 million. The net effect on LP wealth, to the nearest ten thousand dollars, is zero. The fund has paid a bank a spread to do something LPs could not do for themselves only if their own reinvestment rate exceeds the facility's all-in cost, and for most LPs it does not: whenever the reinvestment rate is below roughly 8.2 per cent per annum, the trade destroys value outright.

What the draw unambiguously improves is the reported IRR of Fund B, because accelerating late distributions shortens measured duration, and it improves the distributions-to-paid-in optics of a manager mid-fundraise. Those are benefits to the GP's franchise, paid for from the LPs' waterfall, which is the precise configuration Proposition 2 labels value-shifting and the fundraising-incentive literature of Section 2.1 predicts. The draw also fails Q4: a 40 per cent single-asset concentration means an impairment of the largest asset moves LTV rapidly, and the cash sweep would then trap the very distributions the facility was raised to accelerate. An LPAC asked to bless Case B should decline it, or should reprice it as what it is: a franchise benefit to the manager, for which the manager, not the fund, should pay.

6.3 Case C: A GP Financing Its Own Commitment

Finally, GP Co owes USD 10 million into Fund A's successor as its GP commitment and lacks the liquidity to fund it. Two routes present themselves. The aligned route is a management-company facility: USD 6 million borrowed against GP Co's fee stream at a margin reflecting its concentration, topped up with partner capital. The collateral is the manager's own income; LP capital is untouched; the alignment purpose of the GP commitment, that the manager should have real money at risk beside its investors, is preserved, and arguably sharpened, since the manager now has debt service riding on its own performance.

The misaligned route is to draw on a fund-level NAV facility, directly or through distributions engineered by one, so that LP collateral ultimately funds the GP's stake. This fails Q1 immediately: the use of proceeds is not an investment of the fund. It fails Q4 structurally: the GP acquires its carry-bearing stake with money borrowed against the LPs' assets, converting the commitment from skin in the game into a levered option written by the LPs. No pricing makes this pass; it is a category error, not a term-sheet negotiation. The rule from Section 5.5 resolves every variant: the collateral must belong to the party whose obligation is being financed.

6.4 Reading Across the Cases

Figure 2 shows the net-to-LP outcome of Case A across realisation scenarios, and Table 3 generalises the three cases into a use-of-proceeds map.

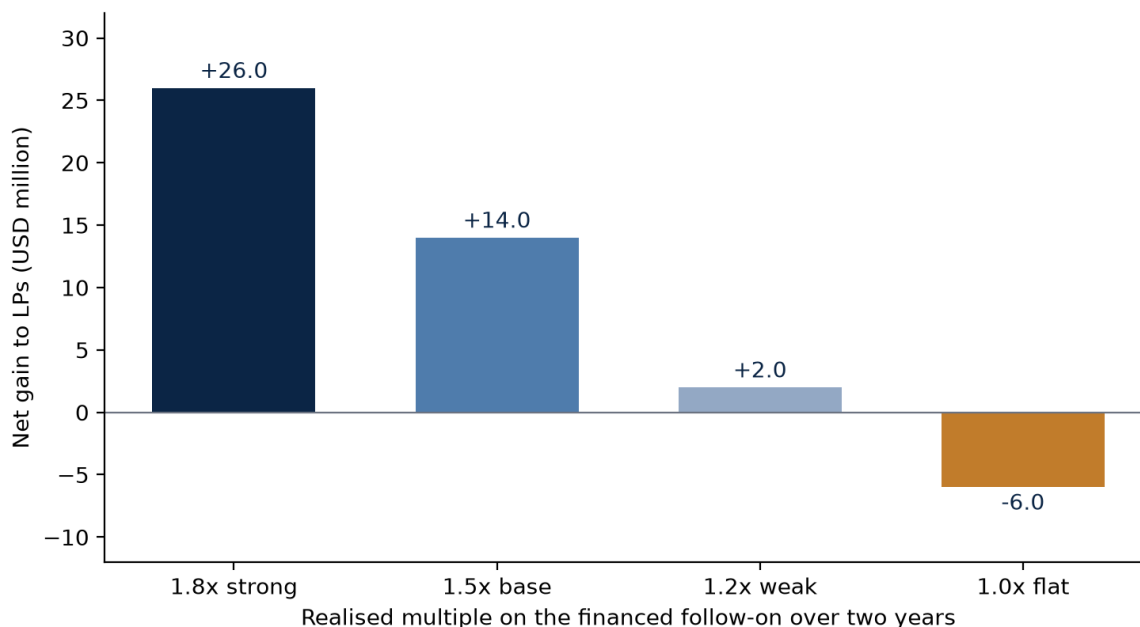


Figure 2. Net gain to LPs from the Case A facility across realisation scenarios, USD million.

Source: author's analysis. Net of principal, interest and fees on a two-year draw.

Table 3. Use of proceeds and the alignment verdict.

Use of proceeds	Principal beneficiary	Clears the Q2 test?	Verdict	Governance minimum
Follow-on into a performing asset	LPs	Yes, above 1.15x breakeven	Value-creating	LPAC notice with terms
Bridging a signed but unclosed exit	LPs	Yes, if bridge is short	Value-creating	LPAC notice with terms
Defensive capital to protect an asset	LPs, if triage is honest	Case by case	Conditional	LPAC consent
Accelerating distributions	GP franchise	No, at most a wash	Value-shifting	LPAC consent after full arithmetic
New platform deals late in fund life	GP fee base	Rarely	Value-shifting	Should generally not proceed
Funding the GP commitment or manco	GP	Not applicable	Misaligned	Move to manco facility

Source: author's analysis. Q references are to the five-question test in Section 4.3.

6.5 Failure Modes and Protections

Three failure modes recur. **The concentration spiral:** a large asset is impaired, LTV jumps, the sweep captures all distributions, and LPs discover that the facility has first claim on the only liquidity the fund will produce for years. **The rolling bridge:** a facility raised for a specific short use is extended, repurposed and refinanced until it is permanent leverage that no one ever approved as such. **The quiet draw:** a facility executed within the letter of a silent LPA, disclosed in a footnote, discovered by an anchor LP from a third party; in a concentrated GCC LP base, this is a franchise-ending event under Proposition 4. Table 4 lists the protections that a well-advised manager should offer before being asked, and that an LPAC should require.

Table 4. Covenants and protections: the negotiation map.

Protection	What it does	Manager position	LPAC position
------------	--------------	------------------	---------------

LTV cap with trigger ladder	Caps leverage; graduates response	Accept cap near 15%	Insist; sweep before default
Use-of-proceeds covenant	Locks the draw to stated purpose	Offer proactively	Require per-draw certification
Sweep carve-outs	Preserves partial distributions in stress	Negotiate hard	Support; protects LP liquidity
Tenor and extension limits	Prevents the rolling bridge	Accept 3 years, one extension	Require LPAC consent to extend
Dual performance reporting	Shows results with and without credit	Adopt as policy	Make it a condition of consent
Valuation machinery	Governs who marks the base in dispute	Retain quarterly marks	Independent valuation on triggers
Recourse limitation	Confines security to the collateral chain	Non-negotiable	Confirm no recourse to LPs

Source: author's analysis.

7. SENSITIVITY AND ROBUSTNESS

The conclusions of Section 6 rest on a small number of parameters. This section moves each and reports what survives.

7.1 Cost and LTV

The Case A verdict is robust to pricing within the realistic band. Figure 3 plots the net gain to LPs against the realised multiple for all-in running costs of 6, 7 and 9 per cent per annum. The breakeven multiple moves only from 1.13x to 1.19x across that range: pricing matters at the margin, but no plausible margin turns a 1.5x follow-on into a losing trade, and none rescues a 1.0x one. LTV scales the stakes rather than the verdict: at 15 per cent LTV the base-case gain rises proportionally, but so does the flat-scenario loss, and, more importantly, the distance to the sweep trigger halves. The binding constraint on size is not the lender's advance rate but the fund's tolerance for covenant proximity.

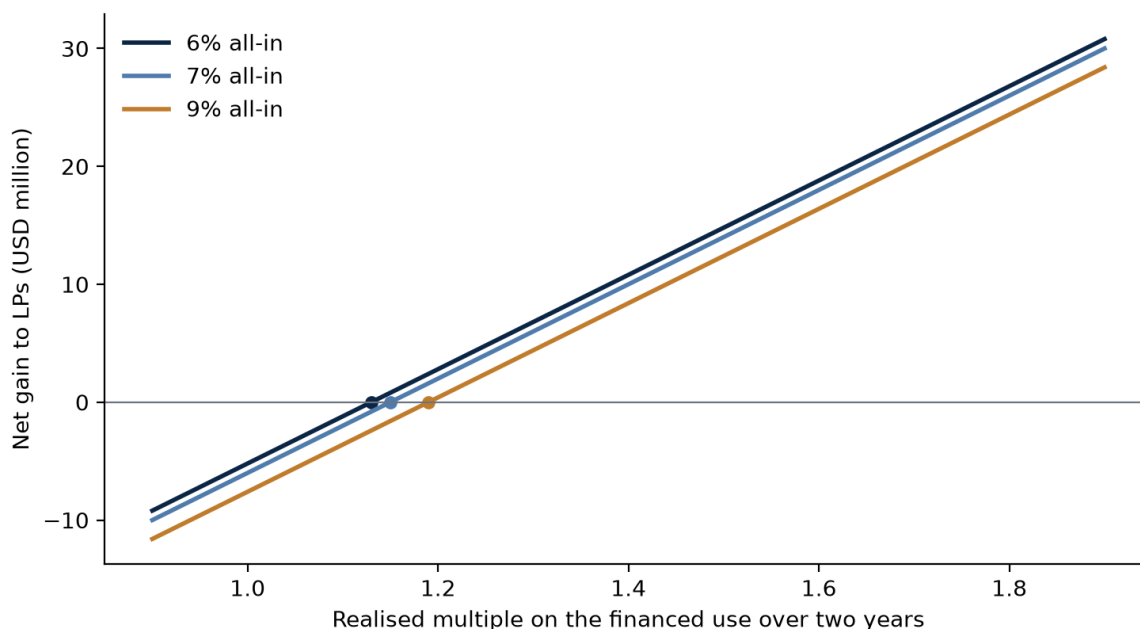


Figure 3. Net gain to LPs against realised multiple at three all-in running costs, Case A.

Source: author's analysis. Two-year draw of USD 40 million including a 1.0 per cent arrangement fee.

The Case B verdict is even sturdier. The acceleration trade is a race between the LP reinvestment rate and the facility's all-in cost, and since NAV margins price above high-grade reinvestment rates in every normal market, the race is lost before it starts. Only an LP whose alternative use of cash returns more than roughly 8.2 per cent per annum with certainty gains from the base-case acceleration, and an LP with such an alternative has better uses for consent.

7.2 Portfolio Correlation and Concentration

The expected-value arithmetic treats NAV as one number; risk lives in its composition. Ten positions with modest cross-holdings justify treating a 10 per cent LTV as remote from its 15 per cent trigger. Four positions dominated by one asset do not: in Fund B, a 40 per cent write-down of the largest asset alone cuts NAV by 16 per cent and lifts LTV by a fifth. High correlation across portfolio companies, common in GCC portfolios tilted toward regional consumption, real assets and government-linked demand, compresses the effective diversification well below the position count, following the logic of Shleifer and Vishny (1992): the collateral is weakest exactly when all of it is weak together. The practical rule: judge covenant distance on the stressed NAV of the correlated cluster, not the position count.

7.3 Exit Timing

Case A ran on a two-year horizon. If the exit slips to three years, the all-in cost rises from USD 6.0 million to USD 8.8 million and the breakeven multiple to 1.22x; the base case still clears, but the weak scenario goes negative. Timing slippage is the quiet killer of facility economics because it raises cost and delays the numerator simultaneously. Case B inverts: if the tail-end exits slip, the acceleration facility stays drawn longer, cost accrues past the reinvestment benefit, and the sweep eventually captures the delayed proceeds. Every month of slippage moves Case B from a wash to a loss.

7.4 A Named Worst Case

Call it the concentrated tail-end spiral. Fund B draws USD 15 million and distributes it. Six months later its largest asset, 40 per cent of NAV, is written down by half: NAV falls to USD 120 million and LTV rises from 10.0 to 12.5 per cent. The sale process for the second asset slips a year. A further market-wide markdown of 20 per cent takes NAV to USD 96 million and LTV to 15.6 per cent, through the sweep trigger. All distributions now prepay the lender; the manager, blocked from distributing and mid-fundraise, requests an extension, which prices at a wider margin and a fresh fee; the LPAC, which approved a distribution, finds it has approved a structure in which the bank stands between the LPs and their own portfolio for the remaining life of the fund. Every step in the chain is ordinary; only the combination is ruinous, and the combination is exactly what correlation plus concentration plus a mid-fundraise GP makes likely under Proposition 3.

7.5 What Would Falsify the Claims

Three observations would overturn the paper's conclusions. First, if realised secondary-market discounts for GCC portfolio strips were persistently narrower than all-in NAV facility costs, Q3 would flip and strip sales would dominate facilities regionally, weakening the core case in Section 2.3. Second, if funds that borrowed to accelerate distributions systematically raised successor funds on better terms and LPs knowingly shared that gain, Case B's welfare arithmetic would be incomplete: the franchise benefit would be partly an LP benefit, and Proposition 2 would need a fundraising-externality term. Third, if levered and unlevered performance disclosure became universal and LP allocation decisions proved insensitive to the difference, the optics motive at the centre of Sections 2.4 and 6.2 would be shown to be self-correcting rather than structural. None of these is currently observable in the region; all three are testable as the market matures, and Section 9 returns to them.

8. DISCUSSION

8.1 Implications for the GCC Manager

Seven operating conclusions follow for a manager. **First, write the policy before the need.** A fund-finance policy adopted mid-crisis convinces no one. Managers raising successor funds should codify borrowing authority, LTV limits, permitted uses and disclosure commitments in the LPA now, when the conversation is unpressured, and treat the codification as a fundraising asset: regional LPs are beginning to ask, and the manager with a considered answer differentiates itself.

Second, size to covenant distance, not lender appetite. Section 7.1 showed that the binding constraint is proximity to the sweep trigger under stressed NAV, judged on the correlated cluster rather than the position count. A facility a lender will write at 15 per cent LTV is not thereby safe for a portfolio whose top three positions move together.

Third, run the five-question test and show the working. The strongest position a manager can occupy in front of an LPAC is to present the arithmetic of Section 6 for its own transaction: use, breakeven, cheapest alternative, risk configuration, governance. A manager who presents the Case B arithmetic honestly, and prices the franchise benefit to itself accordingly, will keep the relationship even when the answer is no.

Fourth, respect the boundary of Section 5.5. Fund-level collateral funds fund-level uses; the GP funds itself at the management company. No exception survives scrutiny.

Fifth, plan sharia structuring early. Murabaha funding legs, screened uses and parallel-vehicle carve-outs add weeks to documentation. A manager who discovers this after signing a term sheet pays for the discovery in extension fees.

Sixth, adopt dual performance reporting unilaterally. Reporting returns with and without the effect of fund-level credit costs little, pre-empts the strongest criticism of the instrument, and converts a governance vulnerability into a credibility signal.

Seventh, choose lenders for workout behaviour. In a thin regional market, the question is not who offers the finest margin but who extends constructively when the exit slips, because Section 7.3 shows the exit will sometimes slip.

8.2 Implications for the LP and LPAC Member

For the family-office CIO or head of alternatives evaluating a manager's request, the framework compresses to a sequence. Ask the five questions of Section 4.3 in order, and require written answers. Require the protections of Table 4, particularly the trigger ladder, the use-of-proceeds certification, tenor limits and dual reporting, as conditions of consent rather than requests. Demand the Case B arithmetic whenever the stated use is distributions: the manager should show the all-in cost against the reinvestment benefit and defend the difference. Watch for the three failure modes of Section 6.5, and treat the rolling bridge with particular suspicion, since it never announces itself.

Concentrated LP bases also confer power that GCC allocators have not yet fully used. In a dispersed institutional market, no single LP can move practice; in the Gulf, an anchor investor that makes dual reporting, LPA borrowing limits and LPAC consent standard conditions in its side letters will find those terms propagating across every manager that wants its capital. Regional market standards are, at this stage of the ecosystem's development, set by a dozen allocators. That is an opportunity to build the disciplined market ex ante that older markets are retrofitting ex post.

8.3 International Comparison

GCC practice will not simply replicate the US and European fund-finance market with a lag; the structural differences push it down a distinct path. In the US and Europe, discipline operates through dispersed-market institutions: standardised disclosure norms shaped by ILPA guidance, specialist lender competition across dozens of active providers, secondary markets deep enough to make Q3 a live comparison on every trade, and, at the margin, litigation and press scrutiny. Consent is procedural because genuine assembly of hundreds of LPs is impossible. In the Gulf, discipline operates through relationships: consent is genuinely obtainable because the LPs who matter fit in one room, but the institutions that substitute for relationships, standard disclosure templates, deep lender panels, active secondary bids, are thinner.

Three predictions follow. First, GCC managers will adopt preferred equity and hybrid structures ahead of pure NAV debt, because the first travels across sharia screens and the second travels across regional bank credit committees (Proposition 5). Second, LPA codification of fund-finance authority will arrive in the region compressed into one fundraising cycle, imported by family offices from the terms they see as LPs in US and European funds, rather than evolving gradually as it did elsewhere. Third, the disclosure norm will bind faster in the GCC than it did internationally, because the reputational mechanism of Proposition 4 is stronger: in a market where every anchor knows every manager, the quiet draw is not a governance lapse but a career event. Managers should plan on the assumption that regional practice will be at the disciplined end of the global range within a few years, and position accordingly.

9. LIMITATIONS AND FUTURE RESEARCH

Five limitations bound the claims. First, the analysis is structural, not empirical: the framework is calibrated from market convention and transaction experience rather than estimated from a dataset, and its numerical outputs are only as good as the parameters a user supplies. Second, the borrowing base inherits the appraisal problem: NAV is an estimate, returns computed from it are smoothed, and the framework prices claims against a number that no transaction has verified, a limitation the literature of Section 2.3 quantifies in other settings but this paper does not. Third, the analysis takes a single-fund lens; it does not model leverage cascading across layers, as when a levered fund-of-funds holds a levered fund holding levered companies, where modest ratios at each layer compound into substantial look-through leverage. Fourth, legal enforceability of security over distribution chains varies across GCC jurisdictions and free zones, and no economic framework substitutes for jurisdiction-specific legal analysis. Fifth, LPs are treated as homogeneous, with a single reinvestment rate, whereas real LP bases mix investors for whom acceleration has genuinely different values, so a draw that is a wash on average can redistribute among LPs.

Each limitation is a research agenda. A hand-collected sample of borrowing clauses from GCC fund LPAs would establish how much authority already exists on paper and how it is changing across vintages. A survey of LPAC consent practice in the region would test Proposition 4 directly. Pricing comparisons between murabaha-based and conventional facility legs would quantify the sharia structuring premium asserted qualitatively in Proposition 5. The falsification tests of Section 7.5, secondary discounts against facility costs, fundraising outcomes of accelerating funds, and allocation sensitivity to dual reporting, are each executable as the regional market generates observations. This paper's framework is intended to be the null hypothesis those studies confront.

10. CONCLUSION

This paper set out to replace a polarised argument with a decision framework. The fund-finance toolkit, subscription lines, NAV facilities, hybrids, GP and management-company financing, preferred equity and

structured secondaries, is best understood as a single spectrum of claims ordered by collateral, from undrawn commitments at one end to portfolio value at the other, with each instrument cheapest at the fund life stage where its collateral is least information-sensitive. Locating a fund correctly on that spectrum answers most structuring questions before a term sheet is drafted.

On the question that generates the controversy, the paper's answer is deliberately unexciting. NAV finance is neither a scandal nor a free lunch; it is senior capital with a running cost, and it creates value for limited partners exactly when the marginal return on the financed use clears the all-in cost of the facility, roughly a 1.15x two-year breakeven in the base case, and no cheaper channel delivers the same liquidity. A mid-life fund funding a value-accretive follow-on clears the test with room to spare and beats the secondary-sale alternative by a wide margin. A tail-end fund accelerating distributions does not: the trade is at best a wash for LPs and reliably improves only the reported IRR and the fundraising optics of the manager, which is why it should be priced, and usually declined, as a franchise benefit to the GP. A GP funding its own commitment from fund-level collateral fails categorically; the manager borrows against its own economics or not at all. Around the economics stands the risk configuration: concentration plus out-of-the-money carry converts fund-level debt into a volatility purchase at LP expense, and the worst case named in Section 7.4 shows how ordinary steps compound into a spiral.

For the GCC, the alignment calculus is distinctive rather than merely delayed. Concentrated, relationship-driven LP bases make genuine consent unusually feasible and undisclosed leverage unusually destructive; sharia-sensitive capital and regional bank credit culture will pull the market toward hybrids and preferred equity; and a small number of anchor allocators currently hold the power to set regional standards, disclosure, borrowing limits, consent mechanics, before bad practice rather than after it. The managers who will raise their next funds most easily are those who treat that discipline not as a constraint imposed by LPs but as the product they sell them.

DECLARATIONS

Funding. The author received no external funding for this research.

Conflicts of interest. The author is the managing partner of an independent capital advisory firm that advises managers and allocators on transactions of the type discussed in this paper. No client information has been used, and no live mandate is referenced.

Data availability. The paper uses no proprietary dataset. The base-case calibrations used in the exhibits are recorded in Section 4 and Appendix A.

Disclaimer. This paper is an educational and structural analysis. It is not investment advice, an offer, or a solicitation of any kind.

REFERENCES

- [1] Ang, A., Chen, B., Goetzmann, W. N. and Phalippou, L. (2018) 'Estimating private equity returns from limited partner cash flows', *Journal of Finance*, 73(4), pp. 1751-1783.
- [2] Axelson, U., Jenkinson, T., Stromberg, P. and Weisbach, M. S. (2013) 'Borrow cheap, buy high? The determinants of leverage and pricing in buyouts', *Journal of Finance*, 68(6), pp. 2223-2267.
- [3] Axelson, U., Stromberg, P. and Weisbach, M. S. (2009) 'Why are buyouts levered? The financial structure of private equity funds', *Journal of Finance*, 64(4), pp. 1549-1582.
- [4] Barber, B. M. and Yasuda, A. (2017) 'Interim fund performance and fundraising in private equity', *Journal of Financial Economics*, 124(1), pp. 172-194.

- [5] Brown, G. W., Gredil, O. R. and Kaplan, S. N. (2019) 'Do private equity funds manipulate reported returns?', *Journal of Financial Economics*, 132(2), pp. 267-297.
- [6] Chung, J.-W., Sensoy, B. A., Stern, L. and Weisbach, M. S. (2012) 'Pay for performance from future fund flows: the case of private equity', *Review of Financial Studies*, 25(11), pp. 3259-3304.
- [7] Diamond, D. W. (1984) 'Financial intermediation and delegated monitoring', *Review of Economic Studies*, 51(3), pp. 393-414.
- [8] Gompers, P. and Lerner, J. (1996) 'The use of covenants: an empirical analysis of venture partnership agreements', *Journal of Law and Economics*, 39(2), pp. 463-498.
- [9] Harris, R. S., Jenkinson, T. and Kaplan, S. N. (2014) 'Private equity performance: what do we know?', *Journal of Finance*, 69(5), pp. 1851-1882.
- [10] Hart, O. and Moore, J. (1994) 'A theory of debt based on the inalienability of human capital', *Quarterly Journal of Economics*, 109(4), pp. 841-879.
- [11] Holmstrom, B. and Tirole, J. (1997) 'Financial intermediation, loanable funds, and the real sector', *Quarterly Journal of Economics*, 112(3), pp. 663-691.
- [12] Jensen, M. C. and Meckling, W. H. (1976) 'Theory of the firm: managerial behavior, agency costs and ownership structure', *Journal of Financial Economics*, 3(4), pp. 305-360.
- [13] Kaplan, S. N. and Schoar, A. (2005) 'Private equity performance: returns, persistence, and capital flows', *Journal of Finance*, 60(4), pp. 1791-1823.
- [14] Metrick, A. and Yasuda, A. (2010) 'The economics of private equity funds', *Review of Financial Studies*, 23(6), pp. 2303-2341.
- [15] Myers, S. C. (1977) 'Determinants of corporate borrowing', *Journal of Financial Economics*, 5(2), pp. 147-175.
- [16] Myers, S. C. and Majluf, N. S. (1984) 'Corporate financing and investment decisions when firms have information that investors do not have', *Journal of Financial Economics*, 13(2), pp. 187-221.
- [17] Nadauld, T. D., Sensoy, B. A., Vorkink, K. and Weisbach, M. S. (2019) 'The liquidity cost of private equity investments: evidence from secondary market transactions', *Journal of Financial Economics*, 132(3), pp. 158-181.
- [18] Phalippou, L. (2014) 'Performance of buyout funds revisited?', *Review of Finance*, 18(1), pp. 189-218.
- [19] Phalippou, L. and Gottschalg, O. (2009) 'The performance of private equity funds', *Review of Financial Studies*, 22(4), pp. 1747-1776.
- [20] Robinson, D. T. and Sensoy, B. A. (2013) 'Do private equity fund managers earn their fees? Compensation, ownership, and cash flow performance', *Review of Financial Studies*, 26(11), pp. 2760-2797.
- [21] Shleifer, A. and Vishny, R. W. (1992) 'Liquidation values and debt capacity: a market equilibrium approach', *Journal of Finance*, 47(4), pp. 1343-1366.
- [22] Sorensen, M., Wang, N. and Yang, J. (2014) 'Valuing private equity', *Review of Financial Studies*, 27(7), pp. 1977-2021.

ABOUT THE AUTHOR

Chennakeshav (CK) Adya is an independent researcher and corporate-finance practitioner with more than twenty-five years of experience as both an operator and an investor across capital markets, private capital and cross-border transactions. His research focuses on capital structure, private markets, fund formation and the financing of high-growth ecosystems in the Gulf and beyond. He writes to make the mechanics of private capital legible to managers and allocators alike, combining a practitioner's view of how funds are actually raised and structured with the discipline of a structured, evidence-aware framework.

APPENDIX A. BASE-CASE CALIBRATIONS

The table below records the base-case calibrations used in the exhibits, drawn from market convention and the author's transaction experience in the region. Readers applying the framework to a live situation should substitute the parameters of that situation; the arithmetic of Sections 4 to 7 carries over unchanged.

Table A1. Base-case calibrations.

Parameter	Value	Used in
Fund A committed capital	USD 500 million	Sections 4.4, 6.1
Fund A gross NAV, year 7 of 10	USD 400 million	Sections 4.4, 5.3, 6.1
Fund A positions; largest; top three	10; 18%; 45%	Sections 4.4, 6.1, 7.2
Fund A portfolio growth	10% per annum	Section 6.1
Fund B gross NAV, year 11	USD 150 million	Sections 4.4, 6.2, 7.4
Fund B positions; largest	4; 40%	Sections 4.4, 6.2, 7.2
GP commitment to successor fund	USD 10 million (2%)	Sections 4.4, 6.3
Management-company facility	USD 6 million	Sections 5.5, 6.3
Eligible NAV haircut	80% of gross NAV	Sections 4.2, 5.3
Advance rate on eligible NAV	12.5% (10% of gross)	Sections 4.2, 5.3
Reference rate	4.0%	Sections 4.2, 5.3
Margin, Fund A facility	3.0% (7.0% all-in)	Sections 5.3, 6.1
Margin, Fund B facility	3.5% (7.5% all-in)	Section 6.2
Arrangement fee	1.0% flat	Sections 4.2, 6.1, 6.2
Commitment fee on undrawn	0.5% per annum	Section 4.2
Sweep trigger; default LTV	15%; 20 to 25%	Sections 5.3, 7.2, 7.4
Facility tenor	3 years, one extension	Sections 5.3, 6.5
Fund A draw; horizon	USD 40 million; 2 years	Sections 5.3, 6.1
Two-year all-in cost at 7%	USD 6.0 million	Sections 5.3, 6.1, 7.1
All-in cost at 6%; 9%; 3-year at 7%	USD 5.2m; 7.6m; 8.8m	Sections 7.1, 7.3
Breakeven multiples	1.13x; 1.15x; 1.19x; 1.22x	Sections 5.3, 7.1, 7.3
Follow-on multiple scenarios	1.0x; 1.2x; 1.5x; 1.8x	Sections 6.1, 6.4
Net LP gain by scenario	-6.0; +2.0; +14.0; +26.0 USD m	Sections 6.1, 6.4
Secondary strip discount	12% of NAV	Sections 6.1, 7.5
Strip sold to raise USD 40m	USD 45.5 million	Section 6.1
Terminal wealth: facility; strip; decline	USD 498.0m; 488.9m; 484m	Section 6.1
Fund B draw; horizon	USD 15 million; 18 months	Sections 6.2, 7.4
Fund B all-in cost; LP reinvestment gain	USD 1.84m; USD 1.84m at 8%	Section 6.2
LP reinvestment rate	8% per annum	Sections 6.2, 7.1
Worst case: largest asset write-down	50% (NAV to USD 120m)	Section 7.4
Worst case: further markdown; peak LTV	20%; 15.6%	Section 7.4
Subscription line advance; margin	15 to 25% of undrawn; 150 to 250 bps	Sections 5.1, 5.2
NAV facility margin band	250 to 450 bps	Section 5.1
Preferred equity expected return	12 to 16%	Sections 5.1, 5.6

Source: author's analysis.

APPENDIX B. NAV FACILITY TERM CHECKLIST

The checklist below pairs the terms a manager should negotiate with the questions an LPAC should ask before consenting. It extends Table 4 into the sequence in which the points actually arise in a transaction.

For the manager to negotiate:

- Borrowing base definition: eligibility criteria, concentration caps and the treatment of new investments and realisations, so that the base breathes with the portfolio rather than ratcheting against it.
- LTV ladder: advance level, sweep trigger and default threshold set with visible distance between each step, tested against a stressed valuation of the correlated cluster, not the headline position count.
- Sweep carve-outs: minimum distribution allowances, management-fee funding and expense carve-outs that survive a trigger, so that a covenant event does not immediately defund the manager or freeze the waterfall entirely.
- Valuation machinery: retention of quarterly manager marks as the default, with independent valuation rights confined to defined trigger events and a named appointment mechanism.
- Cure rights: a realistic cure period, the right to cure by partial prepayment or collateral addition, and no cross-default to unrelated vehicles.
- Tenor and extension economics: extension pricing agreed at signing rather than negotiated in distress.
- Recourse limitation: security confined to the defined collateral chain, with no recourse to LP commitments or to LPs directly.
- Sharia structuring where required: murabaha or wakala funding legs, use-of-proceeds screening and parallel-vehicle mechanics agreed before the term sheet is signed.

For the LPAC to ask:

- What, precisely, do the proceeds fund, and would the fund pursue this use with uncalled capital?
- What is the all-in cost over the expected life of the draw, and what is the breakeven return on the financed use?
- What is the cheapest alternative channel, and what does it cost after discounts and forgone upside?
- What does the facility do to the distribution waterfall on a trigger event, and what carve-outs survive?
- Where does the GP's carry stand relative to its hurdle, and how concentrated is the portfolio the facility is secured on?
- Does the LPA authorise this borrowing, at what limit, and is this request within it?
- Will performance be reported with and without the effect of the facility, in every subsequent report?
- Who bears the costs of the facility if the stated use changes, and what re-consent does a change of use require?

APPENDIX C. GLOSSARY OF KEY TERMS

Borrowing base. The subset of a fund's assets or commitments against which a lender will advance, after applying eligibility criteria, exclusions and concentration caps. The borrowing base, not gross NAV, determines actual debt capacity.

Advance rate. The percentage of the borrowing base a lender will lend, the fund-finance equivalent of a loan-to-value ratio applied to eligible collateral.

Loan-to-value (LTV). Facility outstandings divided by portfolio value. NAV facility documentation typically sets an advance LTV, a higher cash-sweep trigger and a still higher default threshold.

Cash sweep. A covenant that redirects some or all fund distributions to prepay the facility once a trigger, usually an LTV level, is breached, standing between LPs and their liquidity until leverage is restored.

Subscription line. A revolving credit facility secured on the undrawn commitments of a fund's investors, used to bridge capital calls and smooth drawdowns, priced off the credit quality of the LP base.

NAV facility. A loan secured on the value of a fund's investment portfolio, typically through pledges over holding-vehicle equity and distribution accounts, used for portfolio-level liquidity in the second half of a fund's life.

Hybrid facility. A facility secured on both undrawn commitments and portfolio value, with a blended borrowing base that migrates from one pool to the other as the fund matures.

GP commitment. The capital the general partner invests in its own fund alongside the LPs, conventionally in the low single digits of commitments, existing to align the manager's incentives with investors.

Management-company facility. Borrowing by the manager itself, secured on management fees or carried interest, which places no claim on LP capital.

Preferred equity. Capital injected into a fund or holding vehicle in exchange for a priority claim on distributions up to a fixed return, with no covenants or default mechanics; a patient, more expensive alternative to NAV debt.

Continuation vehicle. A new fund formed to acquire one or more assets from an existing fund managed by the same GP, giving existing LPs the choice to roll or exit and resetting the manager's economics.

Strip sale. The sale of a defined slice of a portfolio, rather than whole positions, to a secondary buyer, typically at a discount to carried NAV.

Tender offer. A process in which a secondary buyer offers to purchase fund interests from any LP wishing to sell, providing investor-level liquidity without leveraging the fund.

LPAC. The limited partner advisory committee, a small committee of the fund's investors that consents to conflicts, valuation matters and other reserved items under the LPA.

DPI. Distributions to paid-in capital: cumulative amounts returned to LPs divided by amounts contributed, the measure of realised performance that dominates fundraising diligence.

IRR. Internal rate of return, the discount rate equating a fund's cash flows to zero; sensitive to the timing of flows and therefore to fund-level credit that delays calls or accelerates distributions.

MOIC. Multiple of invested capital: total value divided by invested capital, insensitive to timing and therefore the natural cross-check on IRR wherever fund-level credit is present.

Murabaha. A sharia-compliant cost-plus financing structure, commonly used as the funding leg of facilities for funds whose investors cannot contract conventional interest-bearing debt.