Why SoftBank Vision Fund is one of the most complex private equity funds ever raised

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SoftBank Vision Fund isn't just the largest private equity fund ever raised, at $100 billion. It's also one of the most complicated.

How it works: All outside limited partners are promised a 7% annual coupon on their invested capital, which through June had come out to $1.6 billion. And some of that $1.6 billion has *come from those same limited partners*, in a bizarre bit of capital carousel. The result, from a practical perspective, is that SVF might not really invest $100 billion into outside tech companies.

Around $75 billion of Vision Fund comes from outside LPs like sovereign wealth funds of Saudi Arabia and Abu Dhabi. Each of those commitments is structured in two parts:

- **Common**, whereby LPs receive a percentage of any positive investment returns.
- **Preferred**, whereby LPs receive the 7% annual coupon on invested capital, plus a percentage of any positive investment returns.
    - Each outside LP has a 60/40 split between traditional and preferred, which ties the coupon to upwards of $40 billion.
    - The only LP to only have the common piece is SoftBank Group itself, which committed $25 billion.

SoftBank created the coupon as a marketing tool, knowing it would be difficult to get investors to bite on such an out-sized fund. But it also assumed that the coupon could be entirely paid for via distributions — something that hasn't yet born out.

- Of the $1.6 billion in coupon payments-to-date, only $400 million has come from distributions (Flipkart and Nvidia)
- The rest has come from capital calls.
- The result: Outside LPs are basically paying themselves, SoftBank Group is paying them even more (on a percentage basis, since it only has traditional equity), and Vision Fund isn't really investing $100 billion.

Vision Fund was around 71% invested through the end of Q2, and has given indications that it's now at between 80% and 85%. The remainder is to be used for follow-on investments and to pay the coupons.

So what happens if Vision Fund can't meet its future coupon obligations through distributions, and runs out of committed capital to be called? Does it take out a loan? Does SoftBank Group dip into its balance sheet? Does it pull from the still-theoretical Vision Fund 2? A firm spokesman declined to comment.

This may sound like a Chicken Little scenario, driven by Vision Fund's recent troubles with Uber and WeWork, but it's not impossible.

- Assuming that 85% of the fund is invested, the coupon works out to twice-yearly payments of around $1.2 billion. Over the fund's lifetime, including prior payments, it's over $11 billion.
- Add to that the 1% annual management fee — also on *invested* capital, not committed — and the fund must generate returns of at least $120 billion just to break even.
    - And that's not including a possible two-year fund life extension, which is permitted in the fund documents.

Vision Fund still views the prospect of illiquidity as laughable, particularly given how it remains comfortably in the black on companies like Slack and Guardant Health. But it could help explain why fundraising for Vision Fund 2 is stuck in the mud, Masa Son is doing mea culpas, and last week's major credit default swap price spike.

The bottom line: A 300-year vision may not be compatible with a 10-year fund.