

PRE-EXIT · STRATEGY · GOVERNANCE

# THE AVOIDABLE DISCOUNT WEAK GOVERNANCE BRINGS TO A PE EXIT

Owen Vallis · 5 June 2026

BlackRock now wants a fifth of the standard institutional portfolio in private markets.

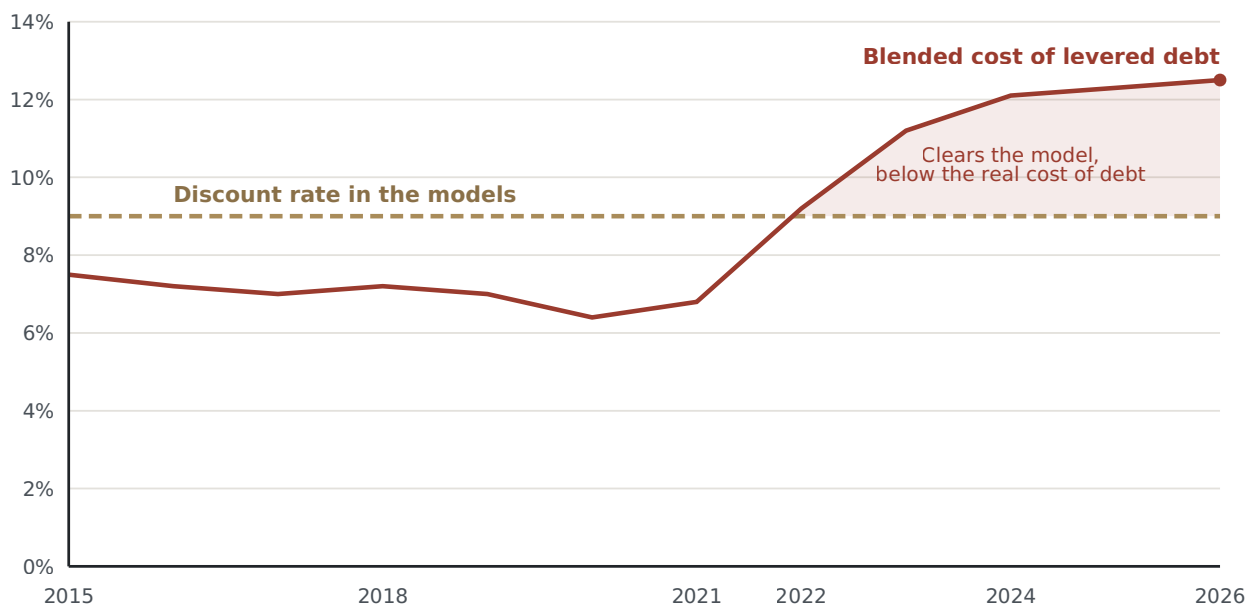
That is the headline of Larry Fink's 50-30-20 model, an allocation call for the limited partners who fund private equity. The force behind it lands one level down, in the operating companies those funds are preparing to sell. Their cost of debt has re-based and capital rationing has returned. Have their boards reset how they approve capex, service their debt and price their bolt-ons for what money now costs, or are they still running the rules they wrote when it was cheap?

That question rarely appears on an exit readiness checklist. It should. A buyer asks it under deal pressure, once a stale answer has already become a reason to pay less.

## The cost of capital has re-based, but the governance still reflects the cheap-money era.

Every capital decision a portfolio company's board makes runs off an assumption about the cost of capital. Most of those assumptions were set when money was close to free, and they still drive decisions today. Three of them now sit exposed.

The investment models still assume cheap money. Boards expect capex and bolt-on acquisitions to clear the sponsor's underwriting hurdle, typically 15 to 20%, but the models that justify them still discount cash flows at a rate set in the zero-rate era. With the blended cost of levered debt now past 12%, a project that shows a healthy return on the old spreadsheet destroys value from the day the capital is drawn.



Model discount rate vs blended cost of levered debt

The discount rate baked into management's project models has barely moved, while the blended cost of levered debt has repriced above 12% since 2022. Once the real cost of capital exceeds the rate in the model, a project that looks healthy on the spreadsheet destroys value from the day it draws down.

The figures are illustrative of a typical leveraged mid-market business.

Debt and hedging exposures are uncovered. Loose board oversight of treasury was survivable when money was free. The interest-rate swaps and caps written in the zero-rate era are now expiring, floating-rate debt is repricing higher, and debt-service coverage tightens just as the exit window opens. A treasury function still set up for cheap money leaves that cash flow exposed, and unhedged currency does the same to any company with international operations.

Capital deployment habits were formed in a different market. The cheap-debt playbook of aggressive, debt-funded bolt-ons without integration discipline has become a liability. Buyers now reward organic growth, balance-sheet deleveraging and working-capital efficiency, and a diligence team reads the old playbook straight off the numbers.

This is the environment an acquirer's diligence team works in. The gap between it and the assumptions most portfolio companies still run on is wide enough to set out in a single table.

DILIGENCE VECTOR	ZERO-RATE-ERA BLIND SPOT (2015 TO 2022)	2026 HIGH-RATE REALITY
<b>Investment models</b>	Cash flows discounted at a zero-rate-era cost of capital	Blended cost of levered debt past 12%, so model returns are overstated
<b>Debt and rate hedging</b>	Unhedged floating debt or short-dated rate caps	Expiring swaps and caps tighten debt-service coverage, demanding active treasury oversight
<b>Strategic capital deployment</b>	Aggressive, cheap-debt bolt-ons without integration audits	Organic growth, deleveraging and tight working-capital discipline
<b>Regulatory exposure</b>	Compliance run as a back-office tick-box	Cross-border data, supply-chain and ESG rules (DORA, CSDDD) carry late-stage deal risk

The table sets out the gap between the assumptions most portfolio companies still run on and the 2026 cost-of-capital reality.

The cost-of-capital figures are illustrative of a typical leveraged mid-market business.

## The three questions an acquirer will ask

How a company runs its capex, debt and deals falls inside the scope of both financial and governance due diligence at a sophisticated buyer. The questions are specific, and they are answerable. Most boards have simply never been asked them under deal conditions.

The first is validation. Can the board independently audit the financial inputs management uses to justify capital deployment? Major decisions reach the board, but directors are structurally dependent on management's own modelling, which rarely meets independent, adversarial challenge.

The second is stress-testing. When did the board last audit its treasury policy against today's re-based debt pricing and stress-test its debt-service coverage for a higher-rate world? Has it confirmed that the models behind its coming bolt-ons use the company's true marginal cost of debt today?

The third is challenge. Does an independent voice interrogate these models before capital is committed, or does the first hard challenge come from the buyer's team in diligence?

These are the same questions our [Pre-Mortem Diagnostic](#) asks. The difference is timing and cost. An acquirer asks them once, under deal pressure, when a gap has already become a negotiating lever. A pre-mortem asks them at the point where the answer can still be fixed quietly.

## Why the exit window makes this urgent

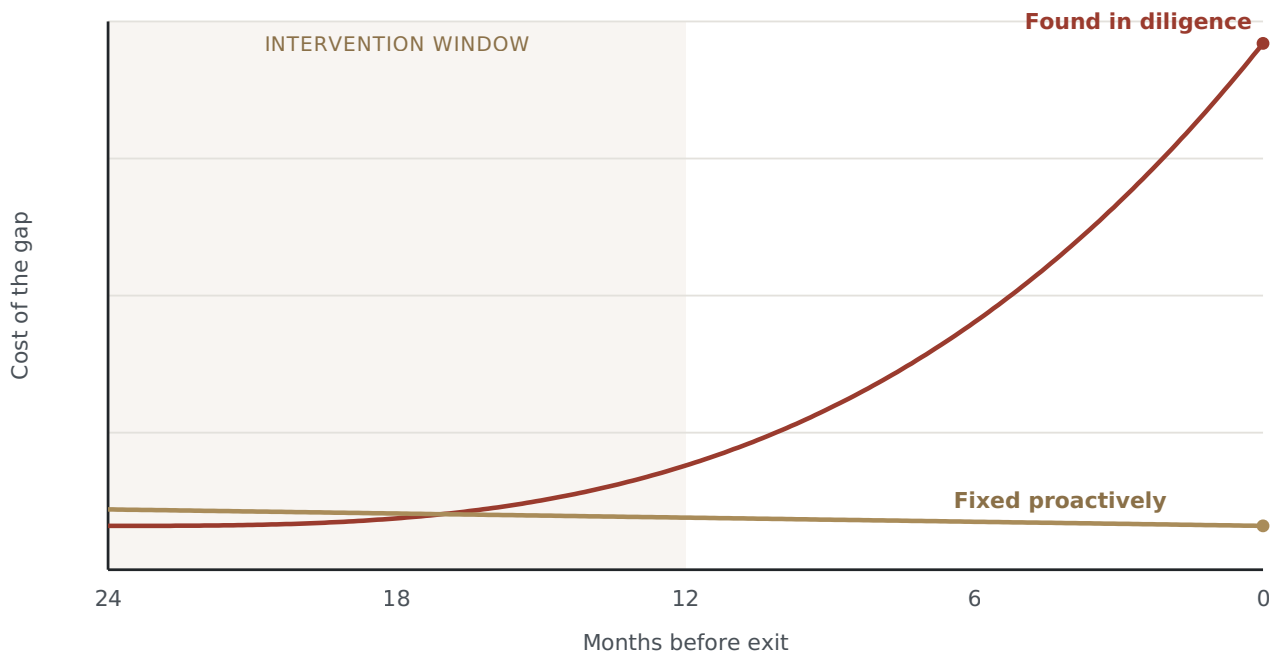
The exit environment is the most congested on record, and the buyers who now dominate it are precisely the ones most likely to examine this gap.

The McKinsey Global Private Markets Report 2026 counts roughly 16,000 companies in the global exit backlog with hold periods over four years. That is 52% of total buyout-backed inventory, the highest share recorded, and the average hold period now stands at 6.6 years. A company held that long has traded through the entire cost-of-capital shift set out above. The financial assumptions and debt structure set in year one are being tested by conditions that arrived long after they were approved.

Secondary buyouts and GP-led continuation vehicles, meanwhile, have become primary exit routes alongside the strategic trade sale. The buyers running them are institutional, governance-literate, and put a target through exhaustive operational due diligence. They have seen this gap before, and they know which companies carry it.

## The intervention point

Proactive governance uplift in the 12 to 18 months before an exit costs less than reactive remediation under an acquirer's scrutiny. The work is governance audit and challenge. It rebuilds the project models on today's cost of capital, tests the hedging and covenant position, hardens the bolt-on approval discipline, and closes the regulatory gaps a buyer's diligence team would find. The [Pre-Mortem Diagnostic](#) applied to the company's capital decisions asks one question. What in this company's capital deployment would a buyer use to justify a faster fade and a lower price? In a high-rate regime, the honest answer is usually a longer list than the board expects.



The curve is illustrative. A governance gap is cheap to settle while there is still runway before a sale, and expensive once an acquirer finds it in diligence and turns it into a price chip at the close.

This is the core of our [Pre-Exit SGaaS engagement](#), and the case for it is defensive. The fade rate a buyer underwrites is set in the operations, beyond the reach of governance. What governance can reach is the buyer's pretext to assume that fade comes faster. A diligence team that finds project models still discounting at zero-rate-era assumptions, floating-rate debt left unhedged, thin covenant headroom, or an undisciplined bolt-on record has exactly that pretext, and uses it to mark the price down during exclusivity, when the seller has least leverage. Pre-Exit SGaaS finds and closes those gaps in the 12 to 18 months before the process starts, hardens the treasury, hedging and capital-discipline position against a buyer's quality-of-earnings and due diligence work, and leaves the board with a documented assurance position to meet that diligence from. It protects the headline price the operating business has already earned.

## What to do next

Ask your CFO one question this week. Has the board rebuilt its project models and treasury policy for the cost of debt the business now carries, or are they still the ones set when money was cheap?

The timing gives the question weight. Global M&A reached \$5.1 trillion in 2025, up 49% on the year and the highest since 2021, with sponsors under mounting pressure to return capital after holding periods stretched to six and seven years (J.P. Morgan, 2026). The exit window is open, and the buyers moving through it read the governance section of vendor due diligence closely.

Governance quality is the cheapest form of price protection a seller can buy. On a £200 million business, a single 3% chip at exclusivity is £6 million of lost value, and a project model still run on cheap-money assumptions, or an unhedged facility, is exactly the kind of gap that earns one. Closing it ahead of the process is a few months of focused work set against a valuation measured in millions, and it

pays for itself the moment one chip is avoided. That is what [Pre-Exit SGaaS](#) is built to do, in the 12 to 18 months before a sale. Check out the full evidence in our [white paper](#), and [book an introductory call](#).

FROM THE SGaaS WHITE PAPER

## Governance as a defence of the exit price

The white paper develops the full evidence base behind continuous, adversarial governance and the four-tier SGaaS delivery architecture, including the Pre-Exit tier built for the 12 to 18 months before a liquidity event.

[Download the paper →](#)

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*Owen Vallis is the founder of Marentis Labs, the firm that originated Strategic Governance as a Service. He spent ten years as UK Head of Fiduciary Risk Management at Credit Suisse and served as Group Chief Risk Officer at SICO Bank. Pre-exit capital discipline is a core component of [Pre-Exit SGaaS](#) engagements. [Schedule a confidential discussion](#).*