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The technological revolution may be in full swing, but is everyone being swept along?

Containing exclusive data picked up from our latest Private Funds CFO Insights survey, this report details how C-level executives across private funds and alternative assets are responding to technological development.

Technology is of course a natural partner for all teams but with the introduction of waterfall automation, artificial intelligence, machine learning and robotic process automation capabilities, it appears that CFOs are at odds when it comes to what should be embraced and what shouldn't across the middle and back office.

This report also draws from the 2019 survey to explore how CFOs are using external third-parties to survive - and ultimately thrive - in dealing with their significant workload. It's not quite as simple as passing this work on to others of course - cost, due diligence and lack of suitability are among the common reasons as to why some choose to keep things in-house.

At the **CFOs & COOs Europe Forum**, in **London** on **12-13 October** technology will unsurprisingly be a significant theme that permeates across our two-day agenda. On the morning of day one, market experts including Marc Dumbell, CFO & COO of advisory firm Campbell Lutyens will be discussing digital transformation and the technology revolution in an exclusive plenary panel discussion. Later in the day, the forum transforms into focused stream sessions, including a technology-focused forum that will enable finance and operations professionals to hear from and engage with their peers.

Day 2 of the forum will introduce the developing debate around outsourcing versus in-house capabilities, with Neel Metha, CFO of DWS Private Equity, and Leo Scanavino, CFO of RJD Partners amongst those debating the merits and drawbacks.

The answer no doubt lies somewhere in the middle - so read on in this report and attend the forum this October to discover how you can find the right balance when it comes to outsourcing for your firm.

"I'm looking forward to taking part in the panel discussion on digital transformation and am keen to hear how others are thinking about how they can better use data and technology, particularly on investor targeting and relations."

Marc Dumbell,
CFO & COO,
Campbell Lutyens

Tech revolution still a work in progress

CFOs have yet to really see the benefits of adopting new technologies in-house, writes Victoria Robson

It's a telling example. Only a tiny minority of firms, 6 percent, use a waterfall automator to help with this fundamental and complex calculation, according to our latest Private Funds CFO Insights Survey. Many do not believe automation is necessary; others have been unable to find a system that works well or been put off by poor reviews. Some have not had time to explore automation or already outsource waterfall calculations. More than a third simply prefer to use Excel.

There is a huge amount of chatter around the potential for technology to streamline any number of functions from preparing financial reports to conducting deal due diligence. It might be surprising then, that while some GPs are reviewing their approach, only 10 percent have concrete plans to automate waterfall calculations. A significant majority of respondents have yet to even review adopting artificial intelligence,

robotic process automation or machine learning tools. A small minority are evaluating their usefulness, while only a sliver have already implemented them.

When asked about the impact of AI on back office functions generally, one compliance officer is not alone in noting, "I'm not informed enough to comment on this." Another respondent adds that he suspects AI is "being over hyped at the moment."

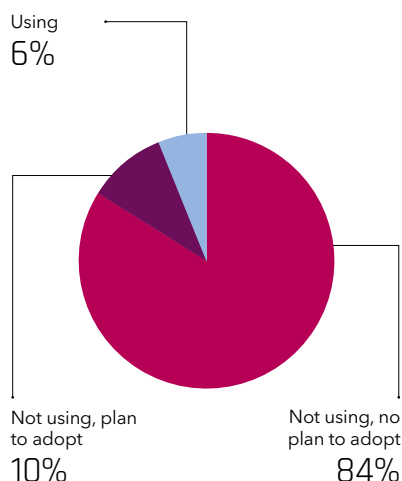
Of those firms that do use new technological tools, enthusiasm is markedly muted. Barely 3 percent believe technology has been highly effective in back office management. More than half rate the effectiveness of technology on investor relations, risk management and returns as "low". This disappointment rises to 70 percent in deal sourcing and 76 percent in due diligence. But one respondent does note that "AI might be able to help with some deal-related

decision making, for example sorting through some high-level inputs to see if a deal is worth pursuing."

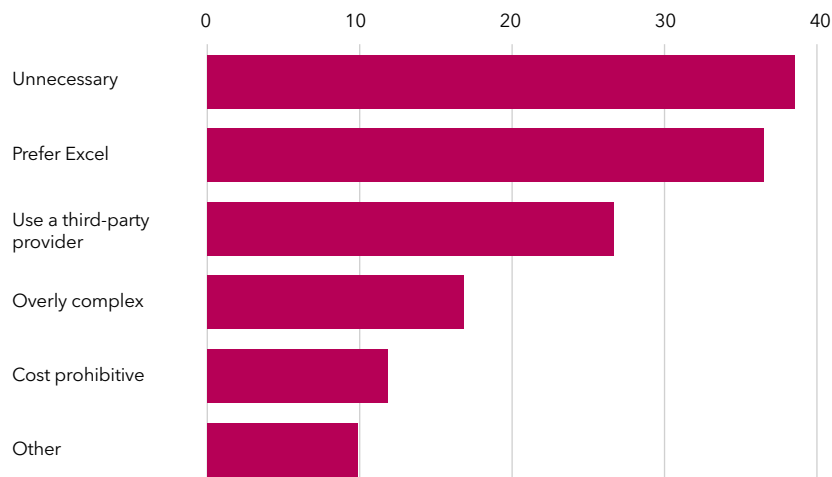
Most managers believe the impact of AI will be felt some time away (five years = 53 percent; 10 years = 43 percent). John Otterson, partner at Jackson Square Ventures, points out that "AI/ML has been evolving for decades and still has a way to go to find truly compelling business applications, let alone singularity. There is certainly an opportunity for further automation in the back office, but it is difficult to predict how/when/where that will happen - perhaps further data aggregation ... is the near term play."

Another CFO adds: "I do not believe [AI] will have a significant impact in the short term or medium term on investment management firms, with two notable exceptions: one, large-scale players (ie, bulge bracket firms) can invest [in new technology] and ultimately

Firms using a waterfall automator



Reasons for not using a waterfall automator (%)*



see some benefit over time, and two, I believe that outsource service providers, in particular third-party administrators, should invest and will benefit from AI so long as they have a practical plan and throw enough internal resources to make it a reality."

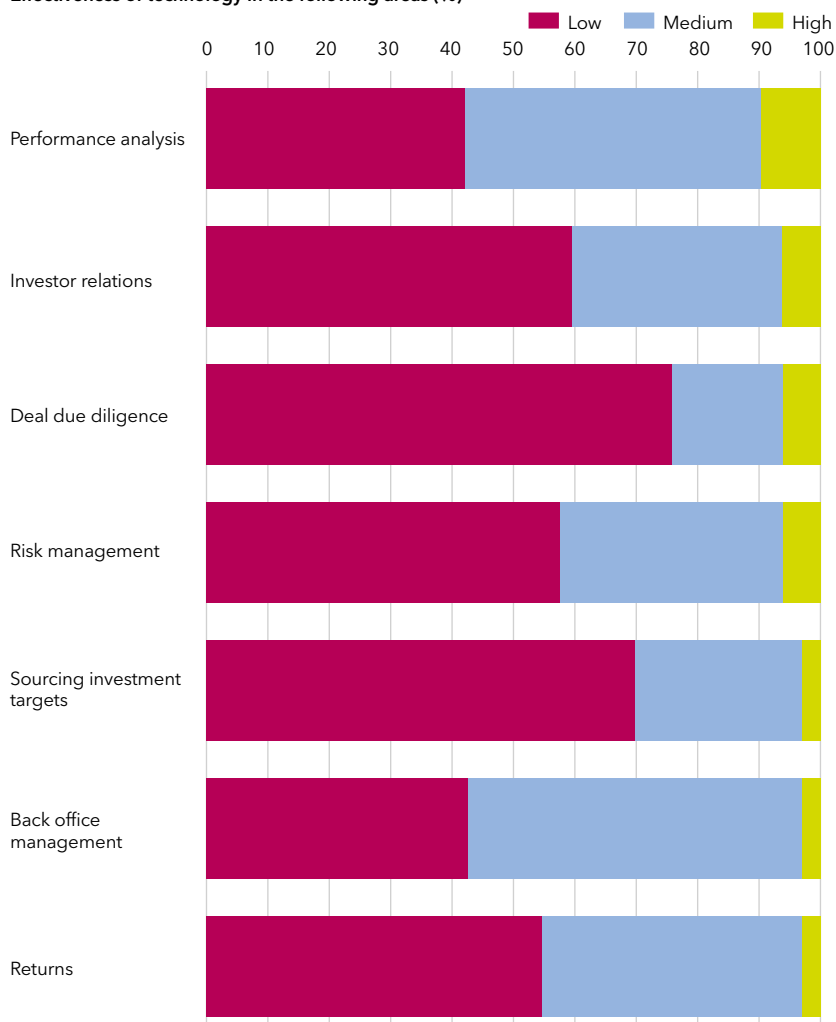
GP reliance on external service providers to meet their technology needs has already shifted the burden to keep abreast of innovation onto those with specific functional expertise. "GP expectations are forcing fund administrators to be more tech-savvy," says Fred Steinberg, SANNE's managing director for North America.

In turn, outsourcing to the more tech-aware is allowing back office teams to alter the way they work. "The role of the back office has become less routine-based and more project-based (routine work is usually outsourced)," says Dimitri Korvyakov, CFO at Sandton Capital Partners.

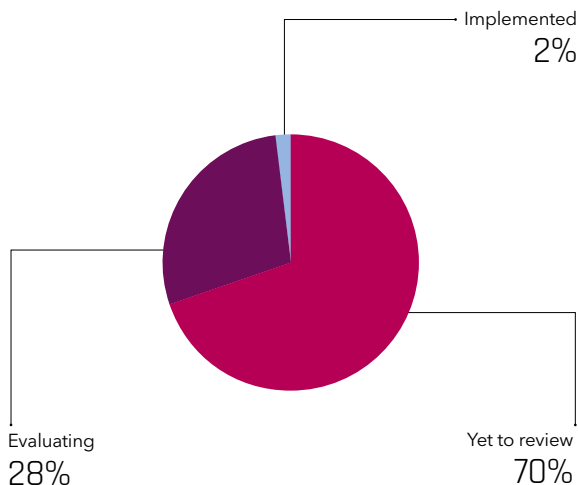
eFront chief executive Tarek Chouman sees a continuation of this swing. "In the future, we believe, GP back office staff will shift focus and work increasingly on the analytical side of the business and less on producing reports or sending emails or generating financial statements."

Whether or not they use technology directly, it seems certain that AI will play a significant role in determining the size and shape of back office teams. In a tech-dominated world, says Chouman, "employees will be more client-facing and involved in decision-making tasks." ■

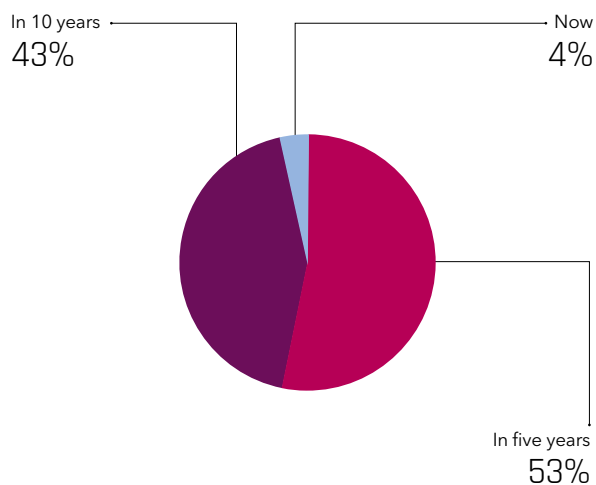
Effectiveness of technology in the following areas (%)



Adopting artificial intelligence



Greatest impact of artificial intelligence on PE firms (%)



The rise of outsourcing

Victoria Robson explores how CFOs are using external providers to cope with an increased workload

The 2019 Private Funds CFO Insights Survey reveals an unexpected pattern. Although the demands loaded onto the back office are growing (due to LP reporting, soaring fund sizes and regulatory scrutiny, among other factors), the rate of back office hiring appears to be slowing. Only just more than a quarter of respondents plan to increase their team by more than one person, compared with more than a third last year.

Bill Tomai, CFO at Centre Partners, believes that “hiring will continue above trend as more funds are created.” But, he adds, “after a long period of above trend growth, a slow down makes sense.” Looking to the future, he expects the automation of the routine elements of reporting will eventually dampen hiring growth.

Today, not everyone notices a change in pace. “Back office [recruitment] is not slowing for us, but it is also not picking up: [it’s] flat,” says one CFO. “I don’t see this changing any time in the near future.”

“We are not seeing that [slow down in pace], we are spending more time on internal and external reporting,” says another CFO. The divergence of opinion seems to reflect the state of private markets today: a wide variety of firms at different levels of maturity investing across different strategies in numerous locations, each with their unique back office staffing needs.

A third CFO comments that he doesn’t know if a slowdown in the rate of hiring is a trend because “I outsource most back office functions.” His response highlights a key determinant of team size: how much work a CFO

deems appropriate to delegate to external service providers.

“Our internal back office headcount has been stable over the last three years, but if you include all outsourced work, the number of people involved in supporting the back office function has increased,” notes Dimitri Korvyakov, CFO at Sandton Capital Partners. “So while hiring directly by investment advisors may have slowed down, I would expect the slack was picked up by the companies supporting the back office, like fund administrators, compliance consultants, etc.”

In the face of increased investor scrutiny, CFOs need the additional support. “I would always consider [outsourcing back office functions], and there is usually at least one workstream in each function where you can leverage a third-party’s technology, scale and human resources,” another CFO points out.

One-third of respondents have seen a hike in LP interest in back office functions over the past three years. But LPs still expect a strong CFO to oversee the back office and external providers. An overwhelming majority of respondents, 73 percent, report that a permanent CFO is “to a great extent” an LP “must have.”

One area where LPs insist that firms invest in support is cybersecurity. “One area where we’ve seen a significant

uptick in due diligence by prospective investors and relates to cybersecurity infrastructure,” says Fred Steinberg, SANNE’s managing director for North America. “Over the past few years, it has become a hugely sensitive area.”

Compliance is a top priority for investors (around half of respondents report that LPs ask detailed questions on this topic), which is an area that GPs prefer to keep in-house. Only a third outsource these services. “We already outsource tax, accounting and IT,” says one CFO. “We’ve no plans to outsource compliance. However, we are required to appoint a regulated fund administrator and to appoint a compliance officer for the fund/manager. This is in addition to our in-house compliance function.”

One chief compliance office notes that while he is open to outsourcing tax, accounting, technology and compliance, the latter “still needs someone in-house to oversee/own it.”

Similarly, 88 percent of respondents conduct investor relations from within the fold, and only 11 percent – the lowest proportion across functions – plan to increase the amount they outsource.

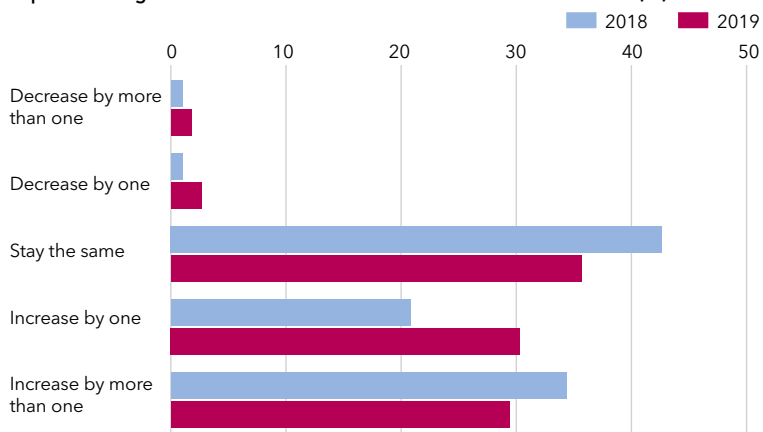
Unsurprisingly, tax and technology – areas that require cutting-edge expertise – are the two most commonly outsourced functions at 88 and 73 percent, respectively. Of all functions, the biggest proportion of respondents – around one-third – plan to increase outsourcing of fund accounting, which is already high at 69 percent.

However, oversight remains a CFO concern. “I do not think that we should outsource 100 percent of [any] function, as we need to retain some control,” says Korvyakov. ■

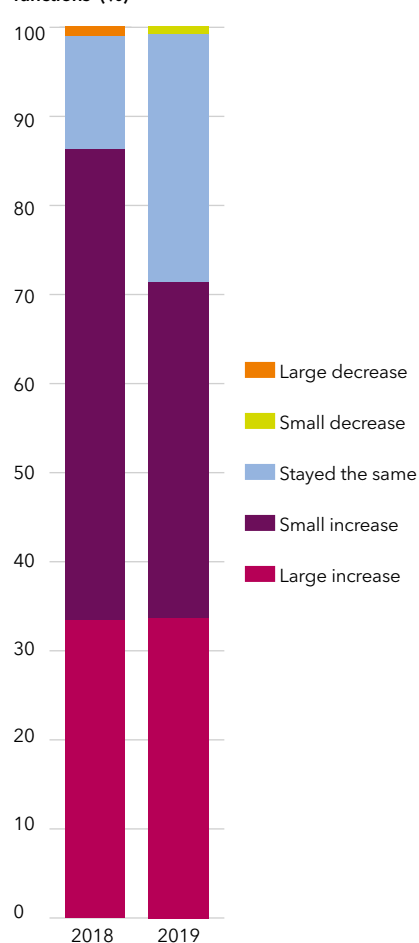
31%

Firms planning to increase outsourcing of technology

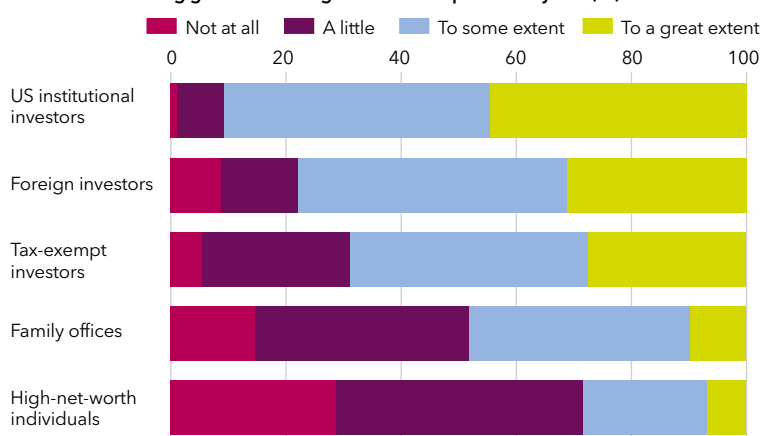
Expected change to the size of the back office team in the next 12 months (%)



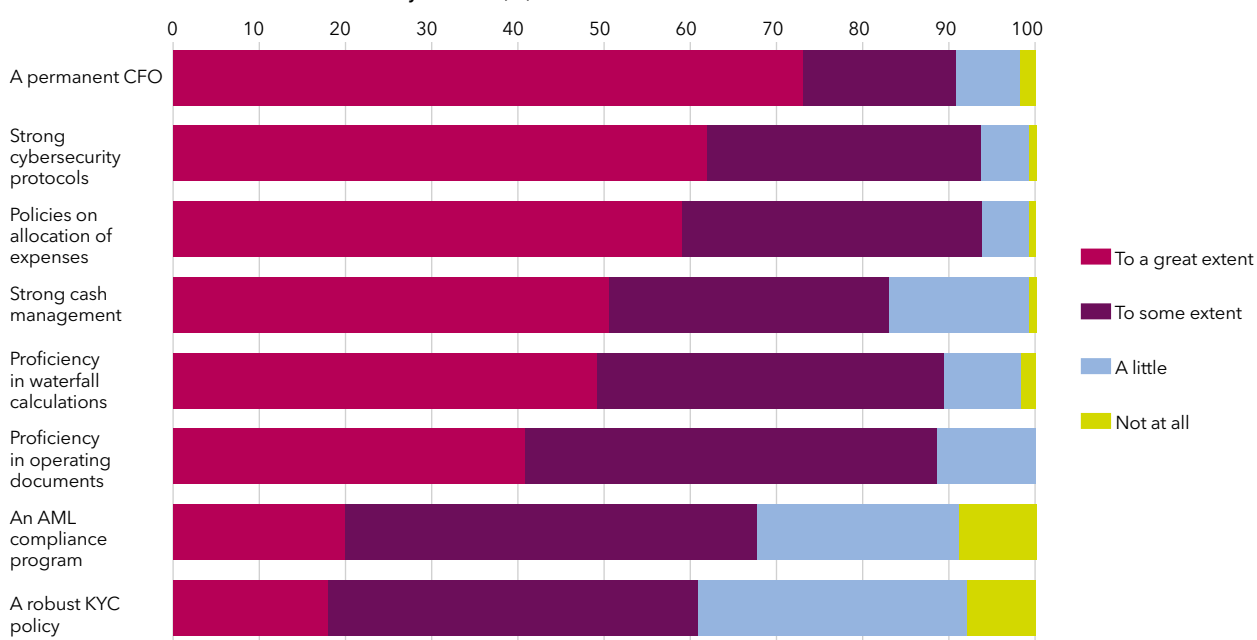
Change in LP interest in back office functions (%)



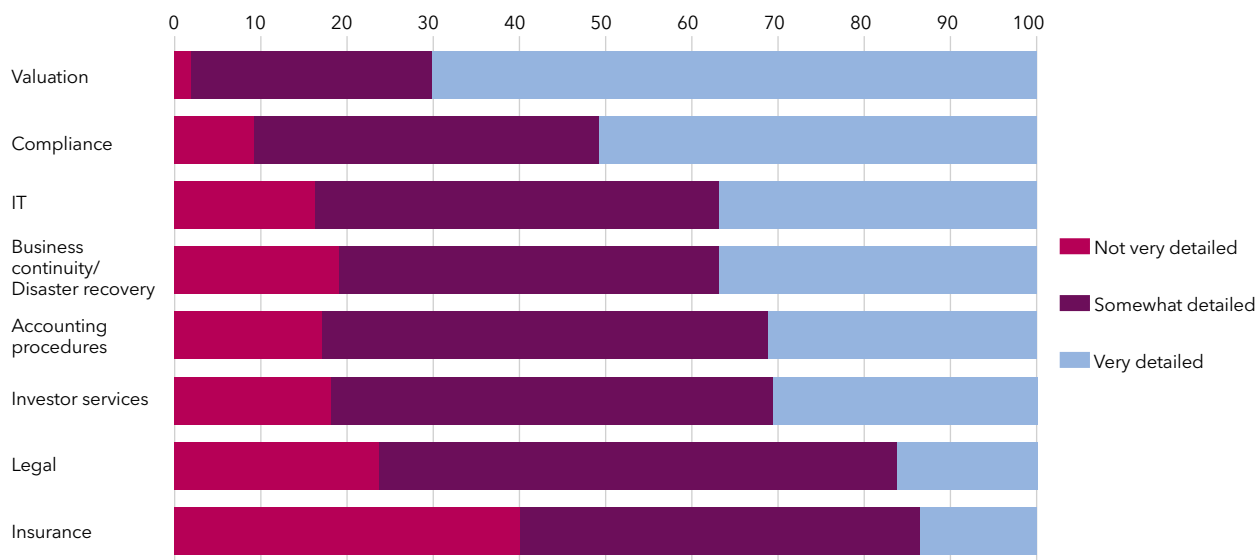
Investors conducting greater due diligence over the past three years (%)



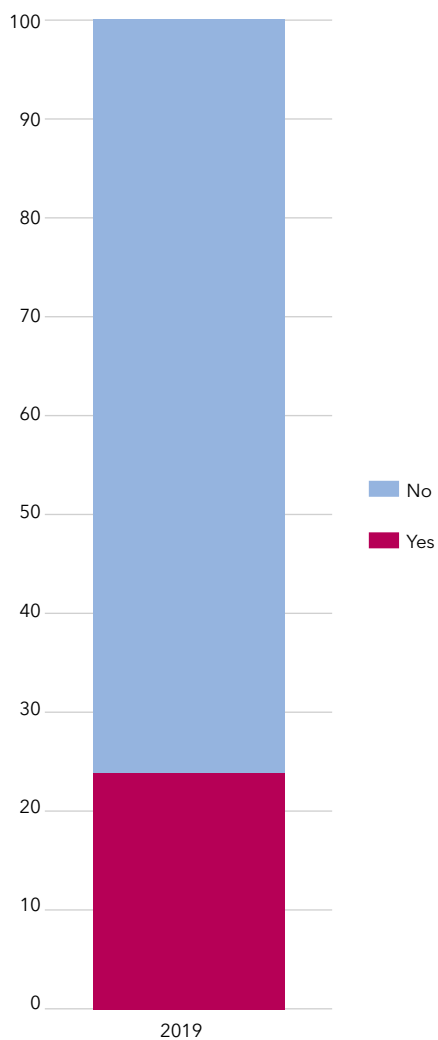
Back office functions considered 'must-haves' by investors (%)



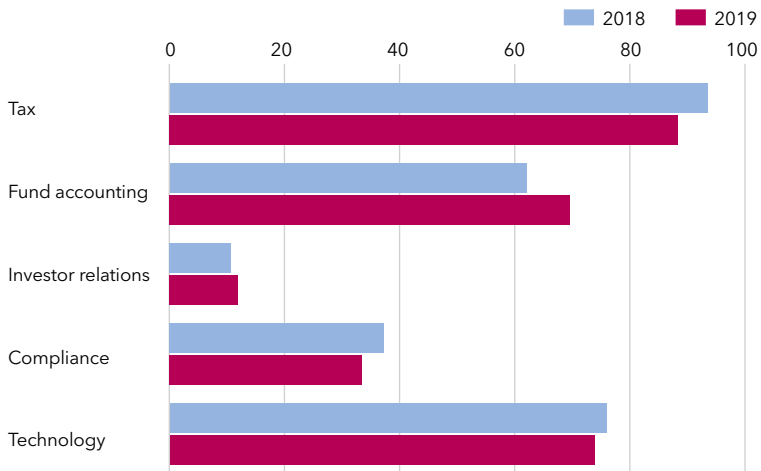
LPs' questions on back office functions during due diligence (%)



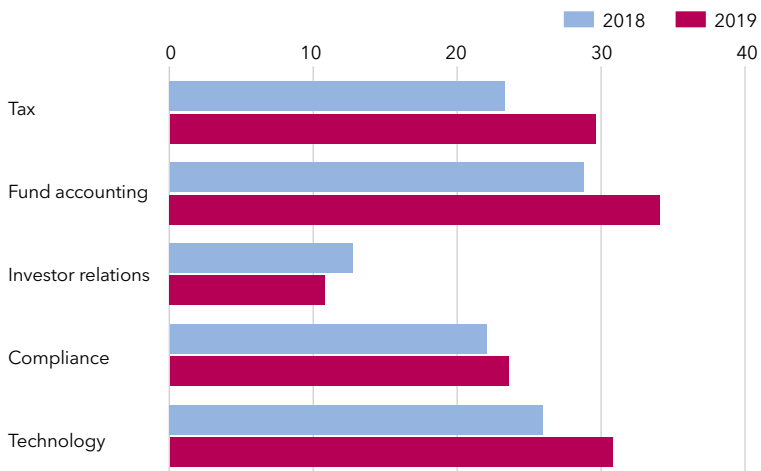
Firms outsourcing AIFM (%)



Firms currently outsourcing (%)



Firms planning to increase outsourcing (%)





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