

The Digital Revolution in Fund Operations

How new technologies are streamlining fund operations, helping asset managers focus on what they do best – investing.

The private equity (PE) and venture capital (VC) markets have responded very differently to the cooling economic climate.

For venture funds, capital has been flowing at a blistering pace this year. In the first six months of 2022 alone, Pitchbook estimates that more than \$137 billion has been deployed into new VC funds - putting 2022 on a pace to eclipse the 2021 record by close to 100%¹.

A starkly different story is at play in private equity. Only ~\$250 billion in new PE funds have been raised so far in 2022, a major decline relative to the \$1 trillion raised in 2021².

Still, regardless of recent fundraising trends, the average private markets firm is much larger today than it was just a few years ago. As fund operations grow increasingly complex, firms are turning to technology providers to drive efficiency and performance gains in today's economy.

Larger Funds Are Looking for Leverage

One key similarity across both VC and PE markets is that more money is flowing into larger, more established funds.

Private markets players have scaled considerably: McKinsey notes the average firm today is over 60 percent larger than it was in 2016³, and firms at the top end are larger than ever before.

¹ Pitchbook: "VC fundraising is set to surpass 2021 record"

² Preqin: "Three fundraising challenges for private equity fund managers and how to overcome them"

³ McKinsey & Company: "McKinsey Private Markets Annual Review 2021"

60%

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Such explosive growth in total assets under management (AUM) has led to a corresponding lift in operational complexity and limited partner (LP) expectations. Unfortunately, most firms have not been able to capture any of the benefits that often come with greater scale. Per McKinsey:

“In private markets investing, however, operating leverage has been elusive. Increased operational complexity...has mitigated the extent to which large GPs benefit from scale economies.”

In response, firms are increasingly focused on upscaling their operations, and more frequently rely on third parties to do the heavy lifting for them. Best-in-class VC and PE firms leverage digital tooling and dedicated service providers to improve operational efficiency and increase bandwidth for their investors to focus on their primary responsibility – investing.

The Benefits of Digital Tooling for Fund Operations

Digital and analytics solutions can help private markets firms maintain efficiency as they scale, create differentiated insight, and improve investment performance.

Still, despite the clear benefits, digital tooling is in the early stages of market penetration. McKinsey notes that:

“While the private markets overall are still in the early stages of digital maturity, leading participants are increasingly investing in digital and analytical solutions to combat such scale inefficiencies.”

Per McKinsey, fund managers with greater than \$10 billion in AUM typically spend \$1 million to \$5 million per year on third-party solutions, with that figure rising to over \$10 million per year when the internal spend by fund operations teams is factored into the equation.

Benefits of adopting software-based tooling are also prevalent for mid-sized managers with AUMs between \$2.5 and \$10 billion. EY research shows that⁴:

“A significant number of firms (39%), particularly mid-size managers consider enhancing back-office processes and technology to be a strategic priority.”

The table below outlines key areas of fund operations that are starting to realize the benefits of digitization through dedicated technology.

Operational Area	Impact of Software Tools
Data rooms	Streamlined access to due diligence materials for LPs
LP subscriptions	Simplified document management, signature collection, and AML / KYC
Asset screening	Analytical tools that screen market / company information efficiently
PortCo analysis	Allow PortCos to self-report, reducing communication overhead
Data warehousing	Single source of truth on fund data for GPs, LPs, and service providers
LP communications	Workflows for ongoing actions, such as capital calls or data requests

⁴ EY: “Are you exploring the future or just vising?”