How the Pandemic Accelerated the Future of the Private Funds Industry

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*Prior to the 2020 pandemic and subsequent economic disruptions, assets invested in private markets (including private equity, venture capital, hedge funds, and credit funds) had tripled from $2.5 trillion to $7.7 trillion since the previous Global Financial Crisis. According to T**he Future of Alternatives 2025** research by **Preqin** – a leading provider of data, analytics, and insights to the alternative assets community – this trend is expected to accelerate with AUM growth in these alternative assets to average 9.8% per year to 2025. Their study incorporates the impact of the 2020 pandemic into their forecast data. In fact, it turns out to be providing catalysts for growth and opportunities for private markets managers to invest in areas that have been affected by the pandemic and market disruptions.*

Bill Hortz

This forecast of growth is expected to be driven in part by persistently low interest rates, high valuations and volatility of public markets, diversification expansion needs and the search for yield and lower correlations. But the pandemic also accelerated changes in fund administration technology, service levels, and strategic partnering capabilities that is enabling a level of business agility and resilience that can drive the industry to new opportunities.

Per Preqin: "The fact the industry and its service providers have managed to pivot so quickly in highly unusual times is clearly encouraging. The relationship between funds and their service providers may well evolve and be closer. Times like these that you find out who your valued and trusted partners and counterparties are and benefit over the long term. Working on issues such as increased transparency, fundraising efficiency, stakeholder (GP-LP) relationships." (Preqin Investor Survey, April 2020)

*To get a better understanding as to the nature of the changes happening in the private markets, the Institute reached out to **Evan Audette** EVP, Chief Operating Officer and **Krista McCoy** EVP, Chief Business Development Officer of Ultimus LeverPoint – one of the largest independent private fund administrators in the country.*

Hortz: What did you see as the biggest challenges private funds faced through this time frame?

McCoy: The biggest challenge for private fund managers was the need for management and operations teams to be extremely agile in responding to a disruptive environment. They suddenly needed increased and immediate access to a whole slew of data and analysis on issues such as cashflow forecasts, capital calls, liquidity positions, fundraising status, quarterly reporting, auditor sign-off and the list goes on.

Initially, many fund managers moved quickly to coordinate draw downs on lines of credit and/or issue capital calls to ensure liquidity to support fund and portfolio company operations as needed.

Hortz: Which areas of support were most requested by fund managers?

Audette: Due to an increase in inquiries and concerns from Limited Partners (LPs), many managers requested that reporting packages from administrators be issued ahead of their normal deadlines, requests for ILPA-compliant reporting intensified, and access to "real-time" reporting capabilities via portals became a priority.

Also, many previously scheduled initial fund closes were delayed due to so many uncertainties surrounding COVID and its economic impact. However, within 2 to 3 months of the initial lockdowns in March, many managers realized the opportunities available in the market, and needed to quickly move forward with initial closes. This required administrators to deploy additional resources for impacted clients to ensure that the execution of subscription documents, capital call notices, and lines of credit were completed as quickly as possible.

For some managers, the pandemic exposed certain risks, such as lack of adequate staffing internally and disruptions due to the remote working environment. This led to many managers who already outsource their fund administration functions looking to their administrators to provide additional services, such as management company servicing and accounting, tax preparation and filing services, and enhanced AML/KYC services.

Evan Audette
EVP, Chief Operating Officer, Ultimus LeverPoint

Krista McCoy
EVP, Chief Business Development Officer, Ultimus LeverPoint

Hortz: How did fund administrators respond to these challenges?

McCoy: As a fund administrator, we spent a good amount of time, money and effort working to solve these problems for our clients including a push for straight-through processing such as electronic submission of subscription docs and other documents via DocuSign.

In another area, we definitely noticed as the lockdowns started and then continued on, our clients relied on us to assist with communication efforts and the coordination of connecting firms to schedule closing activities.

Audette: With many fund launches initially delayed and other fund managers holding off on making decisions such as outsourcing fund administration, current year forecasts for staffing plans were suddenly thrown into question for many administrators. Those administrators with well-defined forecasting processes were able to quickly and effectively re-forecast staffing requirements and adjust plans as needed, to avoid reactionary layoffs.

Fund administrators, such as Ultimus LeverPoint, stayed “ahead of the game” by maintaining built-in staffing capacity, employee recruiting initiatives, and strong marketing and business development teams. We were able to take on new business without sacrificing quality or scrambling to hire new staff. As the circumstances unfolded, we were well prepared to face the challenges and opportunities presented in subsequent months as fund launch activity resumed in earnest.

Hortz: Has the fact that administrators had to pivot so quickly with expanded services been changing the traditional functional nature of fund administration and private fund managers?

Audette: While we expected an ongoing evolutionary relationship between fund managers and administrators, COVID yet again earned its moniker as the “Great Accelerator” of change. Luckily, we had been preparing for this heightened working relationship with expanded strategic service offerings and technology support. We saw the need to better integrate technology and higher level of business partnering into our client’s processes and find solutions for gaps they may have in their operations and business practices.

Hortz: How do these expanded services and higher level of administrative partnership impact the private funds marketplace going forward?

McCoy: There was an interesting opportunity for General Partners (GPs) through this all. There's been an increasing market demand for greater transparency, and it requires a commitment and capability on the part of GPs to provide greater informational services to LPs to meet their needs. This new openness and sharing can create great opportunities for improved relationships between GPs and LPs.

Another point of interest and of special benefit, some GPs are starting to understand the value of their own data. The new agility on data management from administrators required by the pandemic provides GPs the ability to see the positives that analytical LPs find in their data.

Hortz: What trends are you seeing developing in the private funds market that advisors should be aware of?

Audette: Some trends we see currently include a renewed interest in private credit strategies within more traditional PE buyout firms; a growing need for middle office services to service these credit strategies; real estate funds in distressed markets are reinventing themselves looking at structures such as 3c5c; continuing hybrid vehicle creation of open ended fund structures with private equity style investments; and a growing need for fund managers to outsource, especially around data collection, data management and performance reporting.

Hortz: Any additional thoughts you can offer from your experience?

McCoy: Looking back at these times, I think we will recognize that certain niche strategies came about in the wake of the pandemic environment and that this was the point when technology-enhanced services, fundraising activity, increased transparency, and GP/LP relationships changed the dynamics in the industry. We are already seeing many fund managers adjusting rapidly to this new operating reality.

Above all, due to the many issues presented by the COVID epidemic, many self-administered fund managers are realizing the strategic benefits of both outsourcing and co-sourcing fund administration. There is an imperative to seriously upgrade technology and for partnering with their administrators to upgrade service levels, respond to disruptions, and take advantage of new opportunities as they present themselves in the marketplace.