

PRIVATE MARKETS DILIGENCE IN 2020



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WEBINAR TAKEAWAYS

01 What are the key oversight areas in 2020?

- The immediate focus in 1Q20 was on BCP, operational resiliency and ensuring that firms could understand the impact of the pandemic on their IT infrastructure, as well as on the functioning of key controls around the investment process. Very few managers experienced issues.
- Continued focus has been on the managers' ability to source and implement new investments, especially as the private markets fundraising has been strong.
- Focus on the cultural impact of teams working remotely has been a growing area of discussion.
- Cybersecurity controls and training is a key focus as there have been increased incidences and data breaches.
- There is also a greater focus on the understanding and diligence of 3rd service provider value chains associated with managers. There is a push to understand if the managers have the process in place to assess the operational risk of the 3rd parties at appointment as well as on an ongoing basis.

02 The pandemic forced change, but transitioning to working in the virtual world has been better than expected

- The frequency of engagement with managers has gone up, especially risk-based assessments focused on managers in sectors most affected by the pandemic.
- Technology, flexibility and open lines of communication have been critical. Zoom, Skype, virtual data rooms, and digital diligence platforms have been critical. Had the pandemic occurred 5-10 years ago, there would have been significant technological barriers to working remotely.
- With virtual diligences, there is greater scheduling flexibility and the ability to have more manager touchpoints than before. Investors and managers are having multiple calls and are following an organic Q&A based agenda as opposed to strict one-day onsite.
- While transparency has improved overall, there are pockets of managers that remain reluctant to share certain documents.
- Verification of key processes is central to all ODD frameworks, which is being addressed via virtual meetings in conjunction with partnering with local network of service providers and agents.
- IDD and ODD have the same challenges and benefits in assessing manager's interpersonal relationships virtually, and thus have collaborated more closely in 2020.

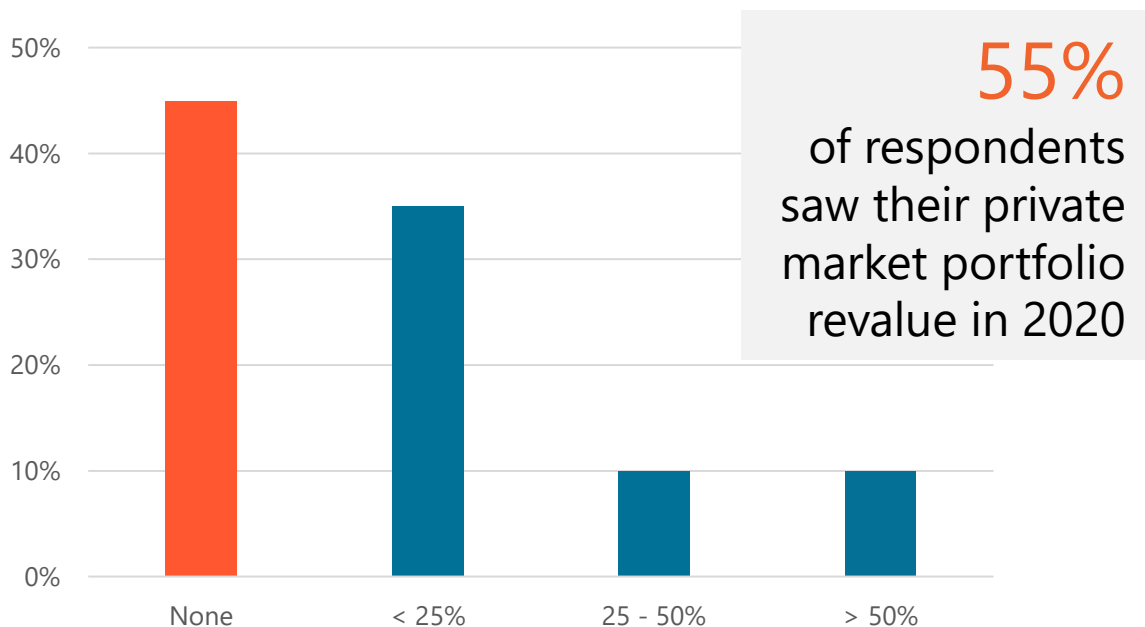
03

Business viability and asset valuations in focus

- For Real Estate funds and sectors that have been most affected, closure of assets, cash levels, loans coming to maturity required close monitoring.
- Valuation has also been challenging. The struggle to get reliable data and information because of reduced transactions in the early days of the pandemic challenged fair market value. 2Q and 3Q continued to be challenging, and the delivery of statements and reports were delayed.
- The updated valuation of assets in current environments can have impact on debt financing covenants which needs to be addressed by both the investors and managers.
- Most affected managers are including additional risk disclosures for the basis of the valuations and identifying deviations from the valuation procedures to provide transparency to their investors.
- For funds that had March 31st year end, Emphasis of Matter section was increasingly included in the audit opinions.
- Investors are forming prospective views of the fund assets based on asset performance, liquidity as a way of augmenting variability in the valuation assessments.

04

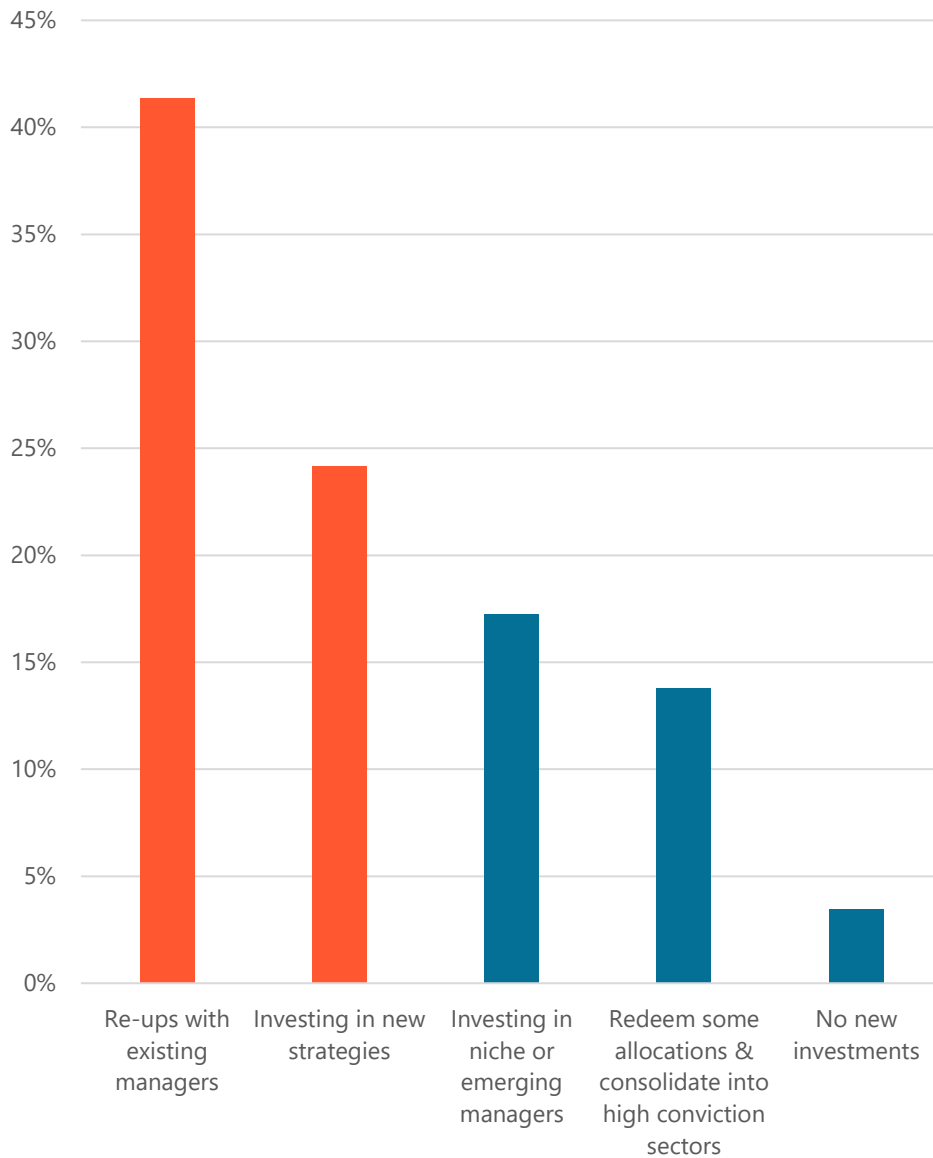
Poll: What % of your assets have needed revaluation in 2020?



What is the future outlook? How are managers reacting?

- **Virtual diligences:** Technology platforms will continue to be instrumental in executing IDD and ODD assessments including potential replacement for in-person meetings, system demos, sharing policy documents, and more.
- **Emerging managers:** New managers will benefit less from virtual meetings as they seek to build strategic relationships with their investors.
- **Background checks:** Background and reference checking will continue to play an increased role, as the risk factors shift in this remote environment.
- **Local experts:** There will be increased willingness to leverage local service providers to perform verifications.
- **Manager sourcing:** Sourcing new managers with networking breakouts at niche conferences has been useful. With limited travels, people are more accessible, and speaking to other LPs has been a key source.
- **IDD – ODD collaboration:** IDD and ODD teams have seen non-linear collaboration as they work together to react to rapidly changing environments. Whereas the teams had overlapping areas but less contact, there has been a move to reduce redundant questions to reduce the burden on managers. Additionally, the focus on active risk and more frequent touchpoints, make conversations between ODD and IDD teams more necessary.
- **Tech adoption:** Managers are increasingly open to adopting standardized technologies that they had historically resisted.
- **Disclosure and transparency:** Managers have been flexible to adapt to investor requirements on disclosure and transparency. This trend is expected to continue as managers build competitive advantage by being investor friendly.
- **Regulatory oversight:** FCA issued “Dear CEO” letters to some of the private markets managers on their handling of governance and social aspects of portfolio companies. This is expected to be a continued focus area in current environment.
- **Operational bench:** Managers are accelerating to strengthen their operational bench with more middle market managers choosing to add COOs.
- **Compliance hotspots:** Investors expect to see increased regulatory focus on compliance policies and use of company approved communications in the remote environment.

Poll: What's been your dominant investment trend in 2020?



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