FEATURE:
FACING UP TO THE DEMANDS OF MULTI-JURISDICTIONAL PRIVATE DEBT FUNDS

PRIVATE EQUITY:
PRIVATE EQUITY EXECUTIVES UNDER PRESSURE

REAL ESTATE
OPPORTUNITY ZONES:
TIME IS SHORT TO MAXIMISE THE OPPORTUNITIES
Welcome to the first issue of our quarterly magazine, Sensus. Our goal is to provide you with commentary on a wide range of topics and areas of interest within the alternative investment world, a world on the verge of significant change. With expert analyses and opinions presented through a series of articles, interviews and in-depth commentary, we strive to make sense of the issues that matter most to you. Each article is written by an experienced specialist in their field, bringing unique insights and a real understanding of the challenges and opportunities that the alternative investment fund industry is facing.

In this first issue, we shine a spotlight on the structuring of alternative investment funds while also examining niche areas such as Opportunity Zone Funds in the US and the rise of renminbi-denominated funds in China. The multitude of different topics we explore is a true reflection of the breadth of knowledge our people represent. Sensus is designed to be an important and relevant information source for all professionals in our industry. We very much hope you enjoy this first issue and encourage all of you to share any feedback or suggestions for future publications.
SENSUS:
IN THIS ISSUE

INVESTOR FOCUS
4
HOW TO EXCEED INVESTOR EXPECTATIONS WITH INDEPENDENT OUTSOURCING

PRIVATE EQUITY
6
PRIVATE EQUITY EXECUTIVES UNDER PRESSURE

DEBT & CAPITAL MARKETS
8
RISING INTEREST RATES AND THE IMPACT ON LENDERS
10
FACING UP TO THE DEMANDS OF MULTI-JURISDICTIONAL PRIVATE DEBT FUNDS
12
AN OUT-OF-THE-BOX SOLUTION FOR FIRST TIME CREDIT FUND MANAGERS

REAL ESTATE
14
INVESTOR REQUIREMENT TRENDS FOR PRIVATE REAL ESTATE FUNDS
16
OPPORTUNITY ZONES: TIME IS SHORT TO MAXIMISE THE OPPORTUNITIES

GLOBAL
18
SPOTLIGHT: THREE KEY QUESTIONS EVERY CFO SHOULD ASK THEMSELVES
24
OPENING UP TO OPEN-ENDED FUNDS
26
THE FINE LINE: COST VS QUALITY

PRIVATE CLIENTS
28
BRIDGING THE GAP: MEANINGFUL SOLUTIONS IN THE UNHW INVESTOR SPACE

INTERNATIONAL INSIGHTS
30
NAVIGATING ASIA’S GROWING PRIVATE CREDIT MARKETS
32
THE SUN SHINES ON MALTA’S FOREIGN INVESTMENT INDUSTRY
34
CHINA: THE RISE OF RENMINBI FUNDS
With investors demanding greater due diligence and an increase in data accessibility, credit fund managers are seeking ways to meet these growing expectations while continuing to pursue their core activities. Finding the right resources and balancing the time and expertise needed to deliver relevant information can be challenging. Timothy Ruxton looks at how outsourcing can help relieve pressure on the back office.

Today’s fast-paced digital technology is transforming nearly every aspect of investor activities. Fast answers, clear insights and accurate analysis are central expectations as investors seek increased access to real-time data. While speedy responses are essential, so is the accuracy of the information being supplied. Both credit fund managers and investors must be able to trust the integrity and security of the data and the sources providing it. Transparency and data security are at the forefront of investors’ requirements.

According to Private Debt Investor, 98 percent of US institutional investors have increased due diligence over the past three years, putting more pressure on the back office.

Against this background of a need for increased transparency, data scrutiny and accuracy, credit fund managers are turning to independent outsourcing solutions. This option offers a win-win scenario, enabling managers to focus on sourcing deals and managing their investors’ money, while clients are assured a first-class and consistent reporting service. With the reporting burden on the back office significantly reduced a more streamlined operation is established. A thorough evaluation of investor requirements allied with an analysis of the manager's team resources and workload may identify areas where independent third-party administration can provide essential support.

IT’S A QUESTION OF CONFIDENCE

By outsourcing administration and reporting functions to a third-party administrator, credit fund managers experience enhanced levels of independence, giving investors and other market participants greater confidence. It also helps to ensure more efficient financing of new credit in the market.

Managers have been utilising warehouse facilities with borrowed funds more frequently, and banks might be more willing to lend to a manager with independent outsourcing than those without. Why? Because they have greater assurance of the fund’s ability to meet compliance expectations, knowing the manager has the time to focus on sourcing deals and executing strategy.

TRUSTED SOURCES, TECHNOLOGICAL SOLUTIONS

While the benefits of outsourcing these administrative functions to a third party may seem crystal-clear, choosing the right partner is critical. Managers should look for a provider with experience administering and transacting in their specific industry; one that understands the daily processes and procedures and the operational issues before they are contracted to supply support services. With both the administrator and manager speaking the same language from the start, they are ideally placed to get the job done right first time around.

In addition to being knowledgeable, the administrator must also be capable. Technology plays a vital role in providing investors with greater access to fund-related data. Alter Domus has created a tool to meet this specific need: CorPro, an online portal that enables managers to streamline their outsourced third-party administrator relationships. Benefiting from consistent access to their data and workflow, it maximises the efficiency of interaction between investment managers and delivery teams.

“Third parties conduct operational activities for a living. Fund managers and their staff may not be experienced in all aspects of the operations and are forced to figure it out. By outsourcing these functions, greater time savings, money savings and efficiency are built into the fund’s overall strategy,” reveals Timothy Ruxton.
While administrative functions such as reporting and data collection are critical and complex activities, they create a huge compliance burden even for the most efficient fund managers. They are time-consuming activities with no room for complacency or inaccuracy. Outsourcing to a trusted third-party administrator frees up time to focus on their core business, provide investors with exactly what they seek, and set themselves apart in the highly competitive credit market.

According to Timothy Ruxton, “CorPro offers investors access to fund financial data, documents and reports, providing them with everything they expect and more. All of the fund’s activities can be segregated or aggregated in order for the strategy to be viewed as a whole. All data is independently verified for accuracy. This gives managers and investors immense peace of mind and potentially sets the fund ahead of its competitors.”
As reporting and compliance requirements on private equity firms evolve, Chief Financial Officers are finding their time under increasing pressure. The result? Many feel they are prevented from focusing on their core activities of funding and structuring deals. Ross McCann takes a look behind the scenes to examine the changing expectations of limited partners and the challenges CFOs face today.

WHY ARE LIMITED PARTNERS MORE DEMANDING?

Industry guidelines that were initially embraced only by a small number of larger limited partners are now gaining traction with a wider spectrum of investors. It is easy to understand why - large portions of their portfolios are dedicated to private equity. Disappointment at lower returns in other asset classes, coupled with the opportunities offered by private equity investments, are key factors in driving increased private equity holdings.

If a large institutional limited partner has invested in 50 different funds, they want standardised information to help manage their portfolio efficiently. And, as these investments now account for a significant proportion of overall assets under management, better information on performance and risk management is essential. It is a proactive approach that requires private equity executives to respond with reliable data and accurate analysis.

WHAT KIND OF INFORMATION ARE LIMITED PARTNERS REQUESTING?

They want a breakdown of all distributions by source of value creation, such as whether it was a capital gain, for example. They also want a more granular view of the characteristics of the underlying investments in order to establish their overall exposure in different countries, industry sectors and other key criteria.

CYBERSECURITY IS UNDER THE SPOTLIGHT - DOES OUTSOURCING RAISE CONCERNS?

We are seeing increased scrutiny of the cybersecurity systems of registered financial providers with particular focus on the safe sharing of data. Data security should always be at the forefront of the service provider’s focus and throughout its internal and external processes.

Strong risk management systems must be in place. One basic step would be to implement controls to restrict staff from sending any client information outside of the company network.

WILL EUROPEAN CLIENTS CONTINUE TO OUTSOURCE MORE SERVICES?

Yes, we believe they will, and that a growing number of managers will initiate outsourcing. Some 70 percent of private equity firms are already outsourcing a significant portion of their back-office work to third-party administrators. We don’t see this trend as restricted to the back office. We are increasingly hearing from private equity houses seeking to outsource parts of the middle office, such as treasury management and some investor relations processes. What is clear is that it is critical to the success of the manager that the CFO has sufficient time and energy to devote to the specialised tasks that really matter. Traditionally the CFO was someone who pulled together the numbers, but today the role has become increasingly strategic.
CFOs add value through activities including sourcing financing in efficient ways, structuring deals and progressing the lifecycle of investments. But as back-office workloads increase, firms that have not yet outsourced this function are finding that largely low-value-added matters are being handled by senior individuals whose expert skills would be better used elsewhere. This in turn leads to a significant drop in time available for their core functions. Today, back-office work accounts for some 50 percent of the CFO’s and their staff’s time.
Credit conditions in the US for both commercial and industrial firms have remained accommodative, with the banking community willing to extend funding to corporate borrowers. However, many years of easy credit have led to increasingly high debt levels among non-financial corporations.

According to Reuters, global non-financial corporate debt has reached an all-time high. Some analysts have begun to fear the impact of this debt mountain in the event of an economic downturn. John Budyak, Director, analyses the current and future state of the commercial and industrial loan market in the US.

The overall spread between short-term and long-term interest rates has been narrowing since 2010. Between December 2017 and December 2018, the spread fell from 1.08 percent to 0.45 percent. This narrowing spread is due, in large part, to the Fed’s increase in short-term rates. It is still unclear whether the interest rate spread trend will continue, but historically, a declining yield spread moving toward a negative spread often suggests that a recession is on its way.

In general, we’re hearing more concern about continued increases in interest rates and their ultimate effect on borrower cash flow. Adding to that concern, many believe that an economic slowdown is getting closer, but are just not sure when and how severe it will be. Overall, I would say our clients’ risk tolerance remains flat, but has begun to decline modestly.
A rise in interest rates can have crippling effects as consumer disposable income declines and a higher proportion of credit payments for cars, credit cards and mortgages go to paying interest, reducing overall purchasing power. From a corporate standpoint, the increase can also mean lower profit, lower dividends and ultimately lower stock prices. Long- and short-term investing may be affected as investors move money to higher-yield short-term and long-term bonds and other debt instruments and possibly away from equity markets.

During an economic slowdown, and especially in the case of a recession - which may also be compounded by higher interest rates - there will undoubtedly be more distress in the credit markets with more loans going to non-performing or underperforming status. At Alter Domus, we have seen this scenario play out in the past. During the last recession, our Special Asset Management group was involved in the management, restructuring and litigation of more than $800 million in defaulted loans.

Many of our lender and regulator clients chose to outsource their non-performing loans to seasoned asset managers within our credit services team for multiple reasons. In some cases, they came to realise that they lacked the necessary in-house expertise. In others, the volume of loans that became distressed was simply too large for them to manage internally.

In the case of an economic slowdown, we expect to see much of the same as in the past, where our lender clients, especially relationship lenders, see their loans move to a distressed state and understand that they’re in the tricky position of trying to collect on a defaulted loan. Third-party special asset servicers often have much more experience with moving that non-performing loan efficiently through the workout process. The outcome is often faster and more economic, with less disruption to the lender client’s base. It’s important for lenders to understand that if and when the markets do take a dip, there are options available to them that will help ease the shock.

Third-party special asset servicers often have much more experience with moving that non-performing loan efficiently through the workout process.
In a trend that first emerged in 2008 and is still gathering pace today, analysts estimate that assets under management in private debt funds will double from their 2017 level of US$667 billion by 2023. With private debt funds still a relatively new asset class, a number of opportunities are opening up with multi-jurisdictional private debt funds among the more promising. Two key factors are helping to drive real investor appetite – investment return and counter-cyclical performance. According to an alternative assets report published by Preqin, 46 percent of investors believe they can achieve an annual absolute return of 8 to 12 percent. Some 74 percent of investors expect their portfolios to perform the same or better year-over-year, despite the threat of rising interest rates. Some multi-jurisdictional private debt funds may offer counter-cyclical opportunities, either through currency or geographical diversification, in the event of a market downturn. Of the investors who think this is a possibility, 43 percent believe that special situation funds will present opportunities with 36 percent looking to distressed debt to balance their portfolios.

RESHAPING RELATIONSHIPS AND RESOURCES

For private fund investors, this asset class is an increasingly important aspect of their portfolios and is set to reshape their relationships with fund managers. For instance, just 23 percent plan to work solely with their current fund manager while some 40 percent plan to develop relationships with new managers alongside their existing managers. With around 20 percent of investors relying mostly on new fund managers, the risk of losing business and the opportunity to gain new business are both very real. To maintain existing relationships, fund managers must be well-equipped to handle investors’ demands that include tax-efficient investments, competitive returns and diversification, access to global funds and comprehensive data and transparency.
In order to build multi-jurisdictional private debt fund structures, fund managers must address a broad range of operational considerations that are specific to this asset class. These include:

- Access to experts who understand the rapidly-changing global private debt fund landscape advising them on how trade, political change, and regulatory requirements will affect their fund.

- Substance. The days when jurisdictions allowed fly-ins and fly-outs with no need to set up shop in multiple places are over. Today, if you manage a fund in Luxembourg, you must have a Board of Directors with two members who live there and a commitment to comply with laws and requirements.

- A solution for investors’ demands for data and transparency, including access to a dedicated data system.

**TAILORED TECHNOLOGY, UNIQUE ACCESS**

The globalisation of the market has undoubtedly created new opportunities for fund managers. But without necessary systems to provide investors with the real data and transparency multi-jurisdiction private debt funds require, these opportunities can be hard to exploit. While outsourcing administrative functions such as investor reporting, allocations, and financial reporting helps streamline operations, an administrator can also act as an agent for credit and allocate funds between multiple fund loan administrative products. With this solid support, managers are free to build their next fund. At Alter Domus, we quickly realised that suitable software solutions dedicated to this asset class are limited. Our customised software, together with our proprietary web portal investor interface, give managers and investors the ability to instantly access data and create dynamic reports, charts, and graphs at the click of a button.

Additionally, and unique to Alter Domus, we offer managers use of trade closers for the trade settlement process, eliminating the need to hire specialised resources for activities that ebb and flow dramatically. With the consistency and integrity a third party administrator can provide, managers are free to focus on their core activity of scaling their business.

“We only consider ourselves successful when our fund managers reach their highest potential. Working with us gives them the ability to access the global stage of investors and investments by engaging in experience-based strategic conversations. By evaluating various fund structures and their tax implications, receiving on-the-ground expertise in jurisdictions targeted by their fund, and leveraging industry leading data systems, fund managers can take advantage of the opportunities that today’s private debt market presents.”

**Stuart Wood,**
**Director**
AN OUT-OF-THE-BOX SOLUTION FOR FIRST TIME CREDIT FUND MANAGERS
In the aftermath of the global financial crisis and the subsequent changes in financial regulations, banks have found themselves having to curtail lending. As a result, private credit lending platforms have been steadily gaining traction. However, lending to middle market companies creates its own unique set of complexities for even the most seasoned asset managers. Greg Myers, Director, looks at some of the implications and solutions.

Banks have pulled back lending, investors are demanding more liquid returns and distributions and private credit investments remain a sellers’ market. What this all points to is continued growth in the private credit sphere with Private Debt Investor expecting the market to reach US$1.4 trillion by 2023. Such an increase would see private credit replace real estate as the third-largest alternative investment class, just behind hedge funds and private equity. While many of the funds launching these platforms have historically been private equity firms, others include mutual funds and traditional broadly syndicated bank loan managers.

NEW PARTICIPANTS, NEW CHALLENGES

Many of the new managers seeking to take advantage of the rising capital flows associated with private credit come from outside the credit world where things operate differently. Typically, private equity firms have lean back office operations. But the loan market presents a very different landscape with its own back office challenges - challenges that do not fit easily within existing private equity infrastructure. Not only do private credit lending platforms demand a different style of accounting, they require credit monitoring, financial reporting, tracking spreads, accrued interest and much more. While hiring experienced staff to fill the necessary roles in a private credit lending platform is certainly an option, it is likely to be the most complex and expensive option available. Building a specialist team with an in-depth knowledge of the credit market can be an enormous drain on time and resources.

“At Alter Domus, administering credit platforms is not something we’re learning on the go, it’s one of our core activities,” explains Greg Myers. “We help managers venture effectively into the loan market by giving them a practical out-of-the-box solution so they can hit the ground running. From loan agency and administration to borrowing base support, loan trade settlement and full fund administration, our vertically integrated solution means that we’ve got everything set up for those managers looking to embark on a private credit platform.”

It is clear that for some companies launching private credit facilities, they can face significant challenges to their infrastructure, reporting processes and operating models. Rather than bearing the overhead costs involved with hiring the back office team and deploying credit-specific asset and portfolio reporting platforms, asset managers are seeking a streamlined, one stop solution from a proven third-party provider. Managers gain time-savings, cost-savings and peace of mind. Why? Because asset managers who partner with third-party administrators are able to maintain control of their operations and focus on closing deals. Choosing an administrator with deep experience in the credit world is a key component in successfully tapping into the opportunities the private credit market offers.
Q&As: WHAT’S TRENDING IN PRIVATE REAL ESTATE FUNDS?

With an increasing need to maintain a competitive edge, private real estate fund managers are wise to take note of the expectations placed on them by investors. By working to meet these expectations, managers help to make their funds more attractive while differentiating themselves in this highly competitive market. Greg Myers, Director, is asked how investors in private real estate funds have changed their expectations, particularly when it comes to communication and reporting.

Q WHAT’S THE CURRENT STATE OF THE MARKET IN PRIVATE REAL ESTATE? ARE INVESTORS STILL HUNGRY?

A Private real estate funds certainly continue to garner a significant inflow of institutional capital. As positive returns and market stability remain, I expect the market will continue to be attractive to investors. For now, investors have an appetite for private real estate funds, but there’s clear capital concentration in the market where we’re seeing fewer funds raising more capital. This is driven, predominately, by investors choosing to allocate their capital to larger funds amid concerns over high valuations and the possibility of market uncertainty.

Not only are investors becoming more selective in the funds in which they choose to invest, their requirements and expectations of fund managers have also begun to shift.

Q IN WHICH WAYS ARE INVESTORS’ REQUIREMENTS CHANGING?

A It goes without saying that fund managers should consider the varying return profiles, risk tolerances and resulting fund structures that investors seek when marketing their funds. But what’s equally important is the fund managers’ ability to cater to investors’ changing requirements. Now, reporting, transparency and data security have come to the forefront of investor concerns. Investors are no longer demanding simple statements and financials with return metrics; they’re seeking robust datasets of not only their allocated income and expense-related items, but also broader datasets. They want information on underlying assets, analytics on asset-level performance and analyses on local area markets, comparable properties, and peer properties. Investors are hungry for data and transparency, and fund managers who cannot promise this will likely miss out.
Q HOW CAN MANAGERS POSITION THEIR FIRMS TO FACE THESE NEW CHALLENGES?

A It’s imperative that managers have access to the technologies necessary to help collect, store and report on all facets of their portfolios— not only the accounting information found in their financial statements and their partners’ capital statements. This can be done in many ways, such as deploying new technology solutions internally, outsourcing the tech aspects completely, or working with a service provider who is already equipped with the technology necessary to meet or exceed investor expectations.

While the task of positioning their firm to face these challenges may seem daunting, it’s certainly possible when the right systems, technology and service providers are in place. With certain infrastructure considerations, it’s possible to give investors exactly what they seek.

Q WHAT KINDS OF INFRASTRUCTURE CONSIDERATIONS SHOULD BE MADE?

A Fund managers should either invest in technology or partner with a service provider who is able to consolidate data from disparate datasets, including accounting information, property level data, as well as local and national demographics. This will inevitably place them in a position to make a ‘build versus buy’ decision. They need to be able to evaluate exactly what kind of staffing model the implementation would require if done internally, and compare that to an outsourced provider who is able to provide the same capacity.

When vetting either in-house technological solutions or an outsourced provider, they should also pay very close attention to the solutions’ data availability and security. Is the investor portal easy to access and navigate? Is proprietary data and investor information appropriately safeguarded?

Is the appropriate infrastructure in place to avoid cyber-attacks? And last but certainly not least, does the tool provide the robust reporting investors seek?

We’ve increasingly seen private real estate managers turn to us to provide them with outsourced solutions to their problems. This frees up time for them to focus on their core business of deploying capital, rather than spending time setting up and staffing an in-house technology solution that may or may not fit their target investors’ expectations.
With 2019 the end date for investing in Qualified Opportunity Zones (QOZs), time is short for investors wishing to take full advantage of the benefits they offer. Fund managers are rushing to get in on the programme before the year ends while investors are showing a keen interest in their advantages. The market is primed and the pressure is on.

While investors have always sought ways to reinvest or defer capital gains, Qualified Opportunity Zones (QOZs) offer unprecedented means to reduce, delay and exempt tax liabilities. Currently, there are about 8,700 QOZs in the U.S., which are low-income census tracts certified by the U.S. Department of the Treasury. The requirement that a minimum of 90 percent of a fund’s assets must be invested in new real estate development or substantial rehabilitation projects in these communities can be daunting for fund managers with limited real estate experience. Additionally, as the U.S. Treasury continues to issue complex regulations surrounding these funds, the need for specialist administrative support is clear.

While most of the new regulations center around offering guidance to investors about how to set up business arrangements within the QOZs, there are some key takeaways for managers. For example, the proposed regulations eliminate the need for funds to take assets into account unless those assets have been in the fund for at least six months. And once a fund sells an asset, it has up to a year to reinvest the proceeds. The new regulations also allow people to invest in a fund directly or to purchase an interest in a fund from an existing investor.

“Although the most recent regulations somewhat clarify the reporting requirements with the working capital safe harbor amendment, further clarifications are expected. Fund managers can benefit from working with administrators who stay on top of the reporting guidelines.”

Stephanie Golden, Managing Director

A SPEEDY SERVICE SOLUTION

The advantages of establishing QOZs include offering investors a temporary deferral of capital gains, a potential step-up basis from five to 15 percent, tax exclusion if the fund is held for at least ten years and the ability to use gains from various asset classes. According to Preqin, 51 percent of investors are considering investing in Opportunity Zone Funds within the next 12 months with a further 12 percent interested in investing after this timeframe. Such figures underline the interest this nascent investment strategy is generating.

Yet time is of the essence as the year-end deadline for investors to receive the full 15 percent step-up basis looms. Managers should be aware that the tax will be triggered at year end 2026 and only those acting this year will hold the investment for the full seven years and thus qualify for the 15 percent increase in tax basis.

It is not too late to get the ball rolling if the right administrative support is in place. By outsourcing the administration, managers do not have to try to put together an in-house team and get them up to speed before the end of the year. Maximilien Dambax, Head of Fund Services North America, says many fund managers use Alter Domus to help navigate the evolving QOZ landscape because they recognise that outsourcing fund administration allows them more time to grow their business. Alter Domus helps fund managers establish funds across jurisdictions, find service providers in every market where we operate, establish systems and processes, and help launch the fund on time and budget.
“Our extensive experience in setting up and administering all types of investment vehicles for real estate managers and navigating the regulations associated with them makes us an ideal partner for managers who intend to become active in this rapidly-evolving QOZ marketplace.”

Maximilien Dambax
Head of Fund Services, North America
In this SPOTLIGHT series we focus on the role of Chief Financial Officer. It is a position that must continuously evolve as the firm’s business cycle progresses, the core business develops, and new strategies unfold. CFOs face unending challenges and a high-pressure environment as they seek to provide real strategic value in a wide range of financial and operational areas. We ask three critical questions and examine the qualities needed for today’s CFOs.

DO I UNDERSTAND MY FIRM’S KEY STAKEHOLDERS AND THE INFORMATION THEY NEED?

A great CFO recognises that all stakeholders are not created equal and must therefore identify those internal and external relationships that are critical to the firm - typically these include investors, managing partners (Key Persons), minority interest holders and at times, regulators. Generally, the CFO directs the firm’s limited resources to focus on the financial and operational needs of these top priority stakeholders. Effectively identifying and managing the information needs of key relationships helps provide a path for demonstrating clear, strategic value to the firm. While less-experienced CFOs may attempt to satisfy every request regardless of stakeholder status, a more accomplished CFO will communicate realistic turnaround times to lower priority stakeholders.

Meeting investor reporting requirements may seem mundane and at times uninspiring, but a deeper review can uncover a number of issues that an established CFO will evaluate and consider strategically. These issues may be related to accounting, reporting and structural complexity, specific jurisdictions requiring local expertise, technology shortfalls, internal or external resource insufficiencies, incomplete, inaccurate and/or delayed information, volume demands, presentation complications and compliance considerations. An experienced CFO recognises that many key internal stakeholder information requirements can offer a real opportunity to demonstrate strategic value through supporting or influencing the decision-making process of the managing partners.

CFOs can display a real depth of understanding of the business and financial operations that goes beyond interpreting the numbers by communicating the effects of various business decisions on the income statement, the firm’s liabilities, and at all times, cash. Senior management want to hear about ROI, IRR, distributable economics, growth forecasts, LP relations, governance, and future fundraising. It is important that the CFO can talk their language as well as accounting speak. A disciplined focus on the goals of the managing partners and senior leadership is an important asset. One technical tool CFOs can incorporate into their communication is to translate their understanding of the business into a concise forecasting/budgeting model. Such a tool allows CFOs to react and respond more quickly to various economic scenarios and provide valuable quantitative facts to senior management.

While other relationships, such as professional service providers, may not take priority in terms of a fundamental impact to the success of the firm, they still require effective relationship management as they can play both an important supporting role and an integral role in the firm meeting the demands of key stakeholders. A strategically focused CFO can evaluate these relationships with professional service providers beyond pricing. Areas to examine include ability to grow with the private equity firm’s complex future, global resource capabilities, technological perspective and experience. In order to meet the increasing demands of key stakeholders, service providers must meet these critical criteria.
CFOs can display a real depth of understanding of the business and financial operations that goes beyond interpreting the numbers by communicating the effects of various business decisions on the income statement, the firm’s liabilities, and at all times, cash.
In the second part of our SPOTLIGHT series we look at self-awareness where one question in particular gives rise to so many more: ‘Do I know what I don’t know?’ An honest answer to this question is essential in any risk management role and a proactive CFO can quickly identify where third-party expertise may be needed, or where a greater allocation of their time may be required. Are you ready to ask the question?

DO I UNDERSTAND THE RISK AREAS OF THE FIRM AND THE FINANCE AND OPERATIONS FUNCTION?

Regulation alone has been the single most important driver to the evolution of the CFO’s role, whether the CFO also serves as the compliance officer or not. For the CFOs that serve as CCO, risk management and documentation exercises have required an enormous time commitment from even the most organised CFOs. Where firms have a dedicated compliance officer or third-party compliance consultants, the CFO cannot dismiss themselves from regulatory responsibility but understand how their role dovetails with the compliance function across a wide range of activities. Crossovers include identifying regulatory risk watch areas such as conflicts of interest, proper marketing material notations, operating partner structures, origin and allocation of ancillary fee revenue and other fee and economic arrangements. The list is extensive and includes expense allocations, co-investment opportunities, governance procedures and an executed and fully complete inventory of firm-wide documentation, financial reports and audits.

Most CFOs instinctively run through ‘if/then’ scenarios in their mind. To take this exercise one step further, CFOs can tailor this approach in areas where poor execution would lead to risks in areas such as negotiating leverage facilities, investor communications, investor reporting, internal reporting, fundraising support, allocation and coding of expenses, valuation, cybersecurity, technology, disaster recovery, privacy, waterfalls, the investment process and deal closings. This approach, in conjunction with clear communication with your fund counsel and other deal advisors, is an efficient way to identify both vulnerable points and new opportunities to add strategic value over time.

Advising senior management on risk management matters during business planning meetings for the CFO who already has a seat at the table can become second nature. But for less experienced CFOs it can be risky until they have an answer to the ‘do I know what I don’t know’ question. A CFO can invest time in this area, utilising outside resources and aiming to incorporate risk management factors into their forecasting and budgeting models.

KEY RISK CONSIDERATIONS:

• reputational risk,
• key staff turnover or extended absences,
• loss of invaluable institutional knowledge,
• loss of personnel trained in the firm’s systems,
• lack of ability to scale quickly,
• operational inefficiencies,
• performance uncertainty of additional hires,
• automation opportunities,
• increased regulation and reporting requirements,
• increased investor reporting demands,
• future outsourcing requirements by institutional investors, and market trends
SPOTLIGHT part three examines how CFOs can build a resource model that reflects the dynamic nature of private equity firms by comparing the financials of insourcing and outsourcing and offering a clear, time-weighted view of each resource category. A trend is emerging where criteria used to select auditors, tax advisors and legal counsel is now applied to fund administrators as increasingly CFOs need them to act as an extension of their internal resources. Are you following this trend?

“Without healthy communication and mutual respect at all levels of the relationship, service provider partnerships can deteriorate over time. Understanding the less measurable criteria is an often-overlooked area of resource allocation – a relationship breakdown can be costly, time-consuming and undermine the CFO’s ability to meet stakeholder requirements.”

Sean Reilly, Director

DO I UNDERSTAND THE RESOURCES AVAILABLE TO ME NOW AND IN THE FUTURE?

Private equity CFOs can estimate the trajectory of resources required by marrying the key stakeholder and risk results over senior management’s near, intermediate and long-term strategic goals. While cumbersome, it does project the firm’s resource needs as demands on the finance and operations team grow. Applying their analysis to each type of resource category constructs a calculated, time-weighted picture for anticipated resource requirements. These categories may cover single or multi-jurisdictional areas and include tax, compliance, technology, accounting systems, valuation and portfolio company monitoring, accounting and reporting. Discussing the results of their assessment together with its implications and qualitative considerations demonstrates strategic value in an unambiguous and unbiased way.

A good financial model can reasonably compare insourcing to outsourcing and quantify the financial impact of items such as compensation, employer taxes, employee benefits, overhead, cash flow available for hiring alternatives, technology investments, additional cash flow for expansion, fund partnership expenses, and net IRR and PREF. With a strategic decision to ‘right-size’ the middle and back office through the addition of or transition to external resources, a CFO will ensure the selected third-party providers are the right long-term partners for the firm, avoiding biased input by maintaining an active ‘pre-outsourcing dialogue’ with a select network of services providers. CFOs will be looking beyond the firm’s structure today and focusing on providers that can scale and execute quickly on unforeseen operational and reporting challenges that may lie ahead. Today, CFOs need fund administrators to perform and function as an extension of the CFO’s internal resources. Knowing that the fund administration model is evolving rapidly, due diligence should focus on the fund administrator’s business, service, and technology models. Comparing fund administrators would include a review of:

- history
- product offering
- growth trajectory and forecasts
- expansion strategies
- management and ownership structure
- local and global footprint
- number of employees
- key employee credentials
- policies related to attracting and retaining talent
- track records
- client base
- key differentiators
- cybersecurity and disaster recovery policies

Technology models have become one of the most important determining factors during the fund administrator selection process as their current and future blueprint for technological progress is a key indicator of long-term viability. Future technological advancements will allow fund administrators to provide their clients with a service model experience that truly feels as if their engagement teams are sitting in the next room. But achieving this goal requires a strong commitment to internal and external resources in terms of dollars, talent, and time. In order to help identify the ‘right fit,’ a CFO will challenge these points with a view to the strength of the fund administrator’s technology model.
Our SPOTLIGHT series ends with an examination of the core qualities needed for today’s successful CFOs. While allocating time to think, read, research and network may seem like a luxury to most private equity CFOs, time spent away from a steady focus on the daily operational issues allows CFOs to consider more strategic planning and value-creation opportunities. The CFO as a strategic thinker can bring an invaluable mix of skills, experience and attitude.

Experienced CFOs think about the company’s current performance, where it must be improved, and uncover strategies to influence efforts for improvement. While there are numerous areas to reflect upon, which may vary depending on the CFO’s tenure at the firm and the maturation stage of the firm, here’s a checklist of some important qualities.

• Prioritising the most important areas of focus for senior management, which include those with direct implications on the firm’s current strategy, and offering solutions.

• Anticipating the next phase of the firm’s evolution and identifying the operational changes required to support future growth.

• Communication strategies with senior management; understanding their styles, personalities, and what drives them.

• Identifying and developing important relationships that contribute to the success of the firm’s strategy.

• Maintaining knowledge on current market trends in fundraising, investor due diligence, regulation, compliance, accounting policy, areas of auditor focus, valuation, structuring, tax and technology.

• Analysing the finance function’s capabilities for advancing data analytics and new financial models to support senior management’s decision-making process.

• Devising solutions for obstacles inhibiting efficiency, such as internal resources issues and talent levels, historical complacency, lack of process or discipline, and underperforming third-party provider relationships.

• Leading the finance and operations team on a path to provide greater strategic, value-added contributions to the firm.

• Recruiting, advancing, mentoring, and retaining top talent.

• Understanding the firm’s technology platforms and assessing any operational inefficiencies that could be remedied with new technology tools.

• Performing strategic hypothetical “what-if” scenarios and processing audits to ensure the CFO stays ahead of unforeseen events or damaging situations around the corner.
These are but a few possible areas of concern for the private equity CFO. Dedicating the time to think clearly about them helps a CFO visualise solutions and shape a disciplined, yet flexible approach to decision-making. Some form of financial analysis to support their ideas, hypotheses, recommendations, and strategies with quantitative facts will help them communicate their ideas effectively to other members of senior management. An experienced CFO knows that demonstrating the financial impact, or return on investing in a strategy shift—even at the operational level—will create sponsorship for moving their initiatives forward.

There are many ways CFOs can help strengthen their strategy credentials and joining industry groups that also hold events, round-table discussions, and seminars is an easy way to further cultivate peer relationships. Given the private equity CFO typically operates on an island, a network of similar professionals provides a convenient option for quick input or simply a resource to bounce ideas around with. For many CFOs networking is seen as part of their responsibility and finding the time to spend on activities beyond the numbers is an important feature. While every CFO is defined by varying experiences and challenges, a successful CFO works at developing disciplined strategies to obtain and maintain a seat at the senior leadership table.
The complex nature of the system’s setup involves moving allocations of investor accounts. Most managers are not set up to support this high frequency activity, and often benefit from outsourcing these types of administrative tasks to third-parties. Fund administrators have the systems, infrastructure and staff to manage these complexities, preventing the fund manager from having to build this costly middle and back-office ecosystem themselves.

When choosing a pooled investment fund, investors are faced with many options. Regional or global? Passive or active? Bonds or equities? An often-overlooked choice is the one between open- and closed-ended fund structures, but the distinction between the two should not be taken lightly. We examine the differences, the benefits and the risks.

When choosing a pooled investment fund, investors are faced with many options. Regional or global? Passive or active? Bonds or equities? An often-overlooked choice is the one between open- and closed-ended fund structures, but the distinction between the two should not be taken lightly. We examine the differences, the benefits and the risks.

The complex nature of the system’s setup involves moving allocations of investor accounts. Most managers are not set up to support this high frequency activity, and often benefit from outsourcing these types of administrative tasks to third-parties. Fund administrators have the systems, infrastructure and staff to manage these complexities, preventing the fund manager from having to build this costly middle and back-office ecosystem themselves.

WHAT ARE THE KEY DIFFERENCES BETWEEN CLOSED-ENDED AND OPEN-ENDED FUNDS?

Many asset managers, keen to appeal to a larger pool of institutional investors, have begun to adapt their strategies to attractive broader investment pools. They have done so by shifting from traditionally closed-ended fund strategies to establishing open-ended funds. Closed-ended funds, by definition, have fixed terms of life and often prohibit the launch of subsequent funds until certain hurdles are met on the current fund. The size of the committed capital is fixed at the final close and invested capital is often distributed at the end of the fund’s life. Existing investors who want to exit must sell on the open market to another investor who wants to put money in and requires general partner approval.

Open-ended funds, in contrast, are always open to investors with capital accounts being marked more frequently and commitments being offered on a pro rata basis to new entrants. Investors enjoy greater flexibility with more frequent NAV pricing and liquidity options for their interests in the fund, due to the assets’ higher liquidity combined with the fund’s perpetual offerings.

WHY ARE MANAGERS MAKING THIS SHIFT?

The ongoing nature of open-ended funds is a supreme advantage to fund managers. They benefit from the ability to perpetually market to investors. They can capture management fees on an uninterrupted basis and welcome additional investment from investors as their allocation requirements change, without the need to wait for their next fund.

Managing a single fund for specific strategies- rather than a new fund every few years- creates greater marketing simplicity. No sunset provisions apply as they often do with most closed-ended funds, making the management of open-ended fund structures more straightforward.

There are also favourable conditions for institutional and pension plan investors investing in open-ended funds. The ease of entry and exit provides a convenient investment vehicle for those looking to invest cash, yet retain their liquidity. They also benefit from readily available historical data about the fund’s performance over various market cycles, which helps them to make well-informed decisions. And unlike their closed-ended counterparts, open-ended funds do not require large, risky, lump sum investments at the time of the fund’s launch on the part of the manager and investors.
WHAT RISKS SHOULD BE CONSIDERED?

While the open-ended structure provides undeniable benefits to both investor and manager, they don’t come without risk. The advantage of having highly liquid investments also creates risk for the fund manager and other investors of the fund.

Although redemptions are pegged to each investor’s risk appetite, the threat of high-volume redemptions presents an undesirable scenario. Investors who maintain their capital in the fund risk losing value. However, most deals cap the redemption threshold at 5 percent to help mitigate this risk.

WHAT ARE THE OPERATIONAL DIFFERENCES TO KEEP IN MIND?

When managing an open-ended fund, there are several operational discrepancies for managers to be aware of. Open-ended funds require either internal infrastructure or an outsourced provider in order to manage the NAV-per-unit calculations and various reporting requirements that are synonymous with these fund structures.
With a possible economic downturn looming, credit fund managers are challenged to find the balance between cost and quality in their middle and back offices. First-class talent and smart technology are critical components in successfully steering an organisation through choppy waters. We talk to Timothy Ruxton, Director, about achieving balance.

TOP-NOTCH TALENT

It has become paramount for fund managers to have access to top-notch talent pools to help mitigate risk. So, what constitutes top-notch talent? Ruxton explains, “Our teams consist of CFAs, CPAs and MBAs around the world, but that’s not the only thing that gives our clients the most value. The real differentiator is experience.”

Ruxton believes that the only way to truly learn about the reality of the credit markets is to get your hands dirty and gain invaluable, first-hand experience. While certain economic scenarios or case studies can provide a strong academic understanding of the field, the in-depth intricacies of the credit markets are not typically covered in university textbooks. Alter Domus teams offer real world experience and can be an asset to credit clients as the threat of a market downturn amplifies.
INTEGRATED TECHNOLOGY SYSTEMS

Most technology systems do not stand on their own; they must be integrated with complementary systems in order to maximise results. This can be challenging to a manager with limited choices based on their strategies. However, as Ruxton points out Alter Domus has developed internally some of the best and most effective technology around. Their approach is to look at what is already available on the market. In the absence of any suitable solutions to meet clients’ exact needs, Alter Domus builds it themselves. It is this proactive approach that has seen the company launch a number of smart technology solutions.

Ruxton says, “Our internally-developed CoPro tool, for example, gives clients access to the different lines of business their Alter Domus teams are doing at any given moment. They’re able to search and assemble data in ways most appropriate to their needs.”

Alter Domus’s Agency System, another internally-developed tech solution, was launched seven years ago and has been continuously developed and improved upon based on evolving client needs and dynamic market changes. By bringing a tool to market that previously did not exist, Alter Domus has become the leading non-bank agent in the United States – a strong position in a competitive field.

DOWNTURN OR NOT?

Whether a downturn is on the horizon or the market is flourishing, top-notch talent pools and technology are absolutely critical to credit funds, due to the complicated, hands-on nature of their asset class. Experience working out issues and leveraging integrated, transparent technology is one of the top ways credit fund managers can help to insulate themselves as the economic tides shift.
For as long as ultra-high-net-worth (UHNW) investors have existed, they have struggled to find comprehensive solutions to meet GAAP accounting standards and report on their investments. With complex portfolios, asset diversification, and partnership/co-invest structures, traditional tools fail to meet all of their needs. Here we review how the needs and expectations of this investor class have evolved.

A CHANGING LANDSCAPE, A NEW VISION

Since the 1980s, institutional investors have relied on software to meet their portfolio reporting needs, which continues to be the most common approach today. Whether it is through all-in-one software, best in breed combinations, or QuickBooks and Excel, the investor relies on technology and staff to deliver their reporting. However, the UHNW investor portfolio has changed considerably over the last 20 years. Initially this was simply a diversification from equity and bonds into currency and foreign investments. Subsequently it moved into alternatives such as hedge funds, fund of funds, and private equity. Currently, portfolios may now include more co-invest vehicles, direct assets and real estate. The future will likely hold more credit/debt structures and cryptocurrency.

Some fifteen years ago, alternative assets made up a very small percentage of the typical family office—many firms were still using a more traditional 60/40 asset mix between equities and bonds. Today, however a typical family office portfolio has almost 50 percent of assets in alternatives. Of these investments, private equity and real estate are the most common as interest in hedge funds has decreased.
“Alter Domus has invested in becoming the leader in the private client space by building the right internal teams, technology infrastructure, and providing a global long-term solution to the market. We believe in a hybrid of technology and service bridging the problems UHNW investors face. As a true extension of your firm, we handle the daily data aggregation, accounting, and processing.”

Jonathan North,
Head of Private Clients North America

In 2000, UHNW investors filled their in-house teams with knowledgeable staff experienced in the equity and other marketable security market and with some hedge fund knowledge. By 2019, however, they needed their teams to be well-versed in private equity and real estate. Not only has the required knowledge of in-house staff evolved, but UHNW investors’ approach to reporting has changed as well. UHNW investors fall into two categories – Institutional Investors and family offices – each taking their own approach to reporting over the years.

Institutional investors, such as foundations and endowments, have traditionally relied on private banks and custodian relationships for their primary reporting. With the move into alternative and direct investments, they have supplemented this information with Excel and in-house staff.

Family offices have also relied on in-house staff and software for their solutions, with their staff remaining with the family long term. At the same time, software conversions are costly and time-consuming and, as such, are extremely rare.

When firms rely solely on in-house staff and technology, they create long-term challenges that may not be apparent on day one. Different offices move into investment trends at different times and with different allocations. Over time, firms face two major drawbacks as their investment landscape changes: staff are not experienced in current investment strategies and technology becomes outdated.

TODAY’S SOLUTION FOR TOMORROW’S WORLD

Many family offices have misaligned or inflated staff relying on insufficient or inept technology tools to support current market trends and a global outlook. The result? Data lag, manual errors, and ineffective insights.

Where custodians may lack knowledge, institutions have added new staff to handle the rise in alternative assets such as real estate. Their teams are manually integrating the custodial data with their internal data for what they hope to be a complete picture. Meanwhile investors’ historic focus on accounting and tax reporting—rather than shorter-term performance metrics—has resulted in a lack of daily deliverables, daily performance, and real-time data access. To address these shortfalls, offices have started to supplement their core systems with new investor-focused ones. It is not uncommon for firms to run three separate systems heavily supplemented by Excel just to provide results to their CIO, family members, or board of directors.

Alter Domus has more than 2,200 people across 20 countries and brings both the expertise and the capacity to meet the changing needs of UHNW investors. Our technology offers complete transparency into each and every transaction. With nonstop access to dashboards, reports, and credit/debt transaction details, in addition to scalable staff and solutions, we provide the tools to capture opportunities.”
As Asia-focused hedge funds underperform and SME funding disappoints, alternative investors are turning to the debt markets. However, with this increasing interest in private credit, it is important to understand that it takes time to build up capability in new markets. Johnson Har, Head of Hong Kong at Alter Domus, and Jayesh Peswani, Director of Relationship Management for Asia-Pacific, review the dynamics of this growing trend.

The private credit market has recently captured the attention of the financial sector, with the number of institutions investing in private debt climbing significantly in recent years. Although most private credit investors are based in North America and Europe, recent research has found that Asian-based investors make up an increasing proportion of the sector—nearly doubling from just 6 percent of active investors at the beginning of 2016 to 11 percent in 2018. The growth within major Asian economies is equally impressive, with private debt investment growing by 36 percent in South Korea, 52 percent in China and a stunning 110 percent in India during the 12 months to March 2018.

Why the sudden increase in interest?

The profile of private credit is very high in Asia as astute investors look to increase their allocations in this alternative asset class. The private credit market has seen strong growth in the US and EU in recent years, and this trend has carried over to limited partners and investors in Asia. Asia-focused hedge funds are delivering underwhelming performance, with Bloomberg revealing that nearly 72 percent of funds that posted double-digit gains in 2017 went into the red in 2018. Operating against the backdrop of a sluggish, low interest rate environment with a lack of SME funding, a number of fund managers are targeting alternative investments, diversifying beyond direct equity by entering the debt markets.

Faced with many of the same challenges, asset owners such as insurance companies and pension funds are also looking to diversify their
holdings into safer places that still offer attractive upside potential.

In addition, given the volatility seen in the global economy — investors are seeking more liquid investments, even in alternatives. Therefore, traditional private equity-type vehicles with lives of up to 10 years are seen as less enticing than debt structures geared to shorter-term loans, or those that possess certain open-ended elements.

**WHAT’S THE UPSIDE POTENTIAL?**

Because it offers steady returns with comparatively lower risk over shorter periods, private debt is emerging as an important component of a strategically diversified investment portfolio. In Asia, where the market is relatively underdeveloped and underserved, many fund managers are trying to enter the market for the first time – but are finding it difficult, as few have these capabilities in-house. As a result, many are looking for third parties, including administrators, to support their private credit investments in the region. Alter Domus is one of the few players with the experience and capability to handle the entire spectrum of private credit investments post loan origination, from loan agency and syndication to ongoing administration.

In private credit, the focus is on protection of rights, of periodic cash flows, and of principals. While not as flashy as direct equity deals, the predictability provided by steady monthly and quarterly cash flows, soundly reinvested, offers its own quality of return potential. As a result, the due diligence process is very different. Unlike direct equity investments, private debt investors are usually unwilling to take risk on the principal. Therefore, much of the groundwork must be done upfront, from due diligence to structuring and negotiation of terms and protection clauses to ensure the underlying investments will generate the desired return profile – higher income/yield, with principal protection.

**WHAT SHOULD MANAGERS KEEP IN MIND?**

Managers investing in the Asia-Pacific region need to take into account country and regional risk, being mindful of the nuances of each market. Although they may be familiar with the law, there can be shifts in its application. Lenders and investors need a level of certainty that their rights will be protected – which is why many deals still use vehicles established in common law jurisdictions. An additional layer of monitoring and administration work is required, including keeping track of covenants and payments. In the case of syndicated deals, an experienced fund administrator will help ensure that everyone is getting their fair share. ✶
THE SUN SHINES ON MALTA’S FOREIGN INVESTMENT INDUSTRY

Foreign investment structures are on the rise in Malta, with many foreign investors finding the ideal jurisdiction for domiciling their funds. The island nation appeals to those seeking the benefit of working with a flexible regulator amid an English-speaking Anglo-Saxon culture. We take a look at the figures.

Przemyslaw Koger, Head of Relationship Management in Malta, says: “Malta is hungry for new names and new funds, so they’re often keen to work with smaller funds and smaller managers. This is very different from other European countries where smaller funds fail to gain much traction.”

Investment business is coming to Malta from around the world; in particular, Polish investors are targeting the jurisdiction in pursuit of investment opportunities. In November 2018 Poland’s Foreign Minister Jasek Czaputowicz stated that Polish investors showing an interest in Malta are growing in numbers every year.

Many foreign investors use Malta’s Notified Alternative Investment Fund (NAIF) structure to take advantage of its speed to market. NAIFs do not require licensing, authorisation or approval, simply that the regulator be notified of their existence. In short, these are unregulated funds that have a regulated manager. According to Przemyslaw, Malta is the ideal location to set up such structures. “In Malta, a NAIF is the absolute quickest way to get an AIF in operation in the market, requiring only 10 business days between the date of filing and the first date of operation.”

“When the NAIF structure was first rolled out in 2016, we saw initial interest from those familiar with Malta that already had a presence there or past experience using Malta as a domicile. But over time, we expect to see a more diverse range of clients, as the NAIF structure becomes available to third-country AIFMs when their country of establishment is granted passporting rights under the AIFMD. The range of opportunities will undoubtedly continue to grow, and we look forward to assisting clients in taking full advantage.”

PRZEMYSŁAW KOGER, HEAD OF RELATIONSHIP MANAGEMENT IN MALTA

“The MFSA has successfully struck the difficult balance between effective oversight and ease of doing business with the NAIF regime,” Przemyslaw argues. “It’s quicker, more straightforward and more cost-effective than other European domiciles, yet still remains fully compliant with European Union law.”

RANGE OF STRUCTURING OPTIONS

NAIFs offer a range of benefits, but one of the most commonly overlooked is the sheer number of asset strategies that can be followed using these vehicles, with investments ranging from traditional to alternative. The fund can be open- or closed-ended and can be established as any of the many legal forms permitted under Maltese law, including SICAVs and limited partnerships.

While NAIFs are unregulated, they do require certain safeguards, including having an AIFMD-compliant depositary to perform oversight duties, as well as cash monitoring and safekeeping. All other AIFMD obligations must also be met, for example due diligence on the members of the governing body of the fund. According to Przemyslaw, these are all services that Alter Domus is increasingly providing to clients taking advantage of this flexible investment vehicle.
Although still relatively new, Malta’s Notified Alternative Investment Funds are secure, flexible fund structures created to appeal to the changing needs of investors and fund managers from around the world. Przemyslaw and his team at Alter Domus Malta are excited to assist clients as they exploit the opportunities NAIFs offer.
Until 2007, renminbi-denominated vehicles accounted for only 12 percent of the funds in the Chinese market; US dollar-denominated funds dominated fundraising. Today the situation has been reversed and renminbi funds account for 80 percent of all funds raised in China. Why such a dramatic shift?

In the past, both foreign and domestic GPs in China were primarily raising funds in dollars as a means to attract foreign investors and facilitate overseas listings in jurisdictions such as the US and Hong Kong. But as the Chinese government took note of the success in China of offshore dollar-investing entities, they also took measures to increase the appeal of funds denominated in their own currency. This, coupled with foreign firms’ growing interest in China’s attractive private equity market, fostered the breakthrough of renminbi funds.

RMB-denominated funds provide several benefits. There are no restrictions on where GPs can make investments, and by eliminating the laborious process of seeking government approval to convert currency, deals are often closed more quickly and with greater profitability. Ming Bi, Head of China, Alter Domus, believes that the face of the RMB fund market is changing: “The market is maturing much quicker than anyone expected. Increasing regulation and evolving investor demand are creating a massive shift.”

**SETTING NEW STANDARDS**

In addition to the role of domestic fund managers in the RMB market, foreign GPs are having their own impact with many international clients, already holding USD funds, now stepping into the RMB world for the first time. These investors arrive with certain expectations, such as the high reporting standards that they’re accustomed to. They are pushing the standard level of reporting for RMB funds much higher which is an excellent and powerful driver for an industry in greater demand.

As further regulations are established, private equity investments through RMB-denominated funds continue to increase in appeal to both domestic and foreign institutions. The Asset Management Association of China is leading the way by requiring all RMB GPs to be registered and has established guidelines regarding compliance, manager education and experience levels, all steps that further legitimise investments in the market.

Alexander Traub, Regional Executive for Asia-Pacific, says Alter Domus is ensuring clients maximise the potential offered by the changing RMB landscape: “We’re constantly expanding our presence to help clients take advantage of these rapidly-evolving markets. We now have more than 300 employees in the APAC region, including four offices in China. Our local teams are administering RMB funds for seasoned domestic GPs and look forward to assisting foreign GP clients with fundraising in RMB for the very first time. We see this as an ongoing trend and expect the market to continue on its upward trajectory, while doing everything we can to make sure our clients take full advantage.”

**CHINA: THE RISE OF RENMINBI FUNDS**
“In the past, Chinese GPs were very traditional in the sense that they kept all of their back office work in-house and private, but that is no longer the case. We’ve observed increasing numbers of RMB fund investors conducting greater due diligence on their fund managers. As a result, there is an identifiable outsourcing trend as Chinese GPs calm LPs’ apprehensions about the governance and compliance of their funds.”