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TECHNOLOGY REPORT 2024

THE DRAWDOWN

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LEADER *Taku Dzimwasha*

Welcome

Technology is now a cornerstone of midmarket private equity – not only as a sectorial investment thesis, or a way to unlock the full potential of portfolio companies, but as a transformative force within the industry itself.

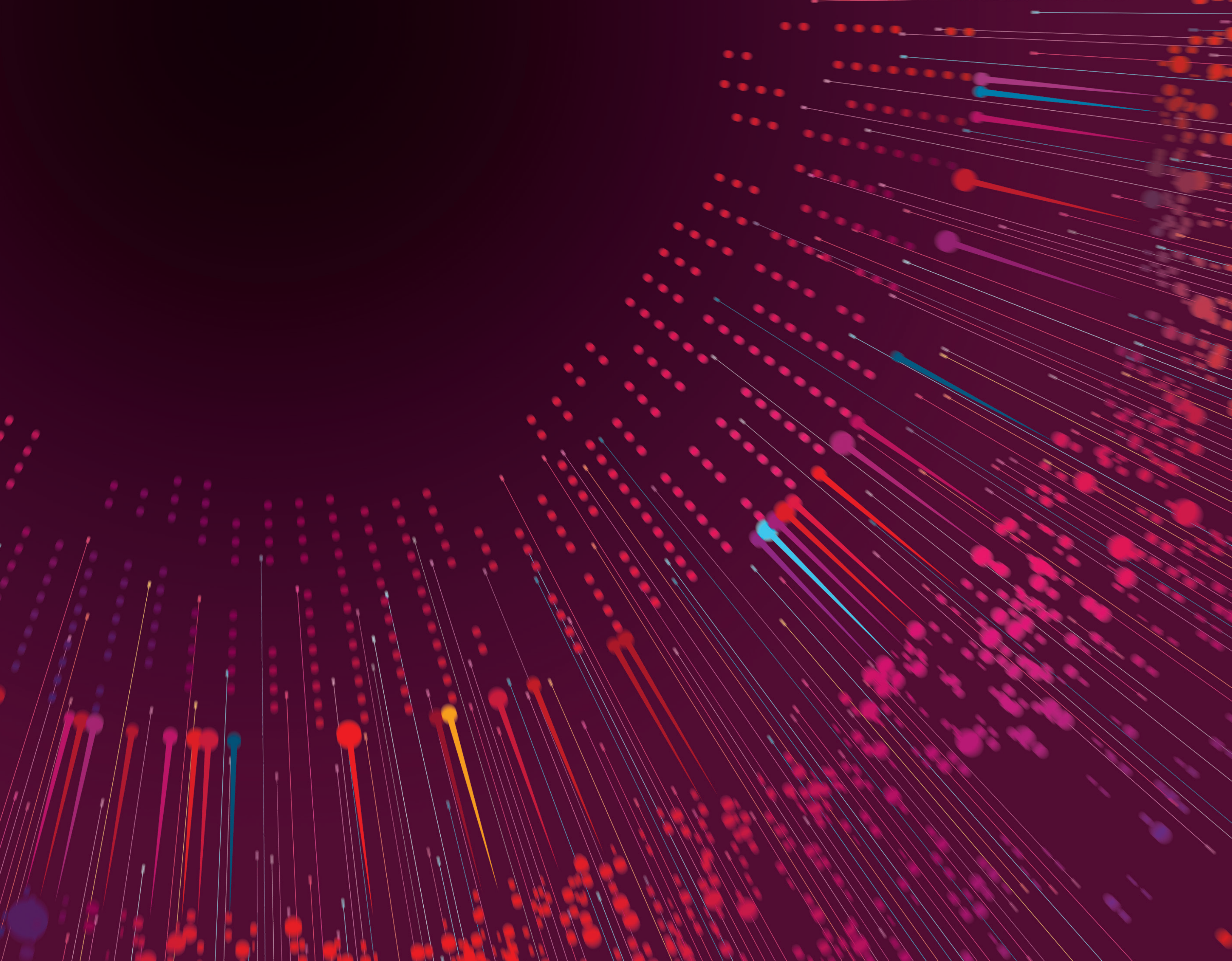
Notably, the best private equity firms are now harnessing the power of technology across their organisations to unlock deal origination opportunities well ahead of processes and turbocharge their value-creation frameworks. Especially in such a difficult M&A environment – when finding the right deal to focus time, effort and capital on is more important than ever – we thought this should be a natural starting point for our new series of *Technology Reports*.

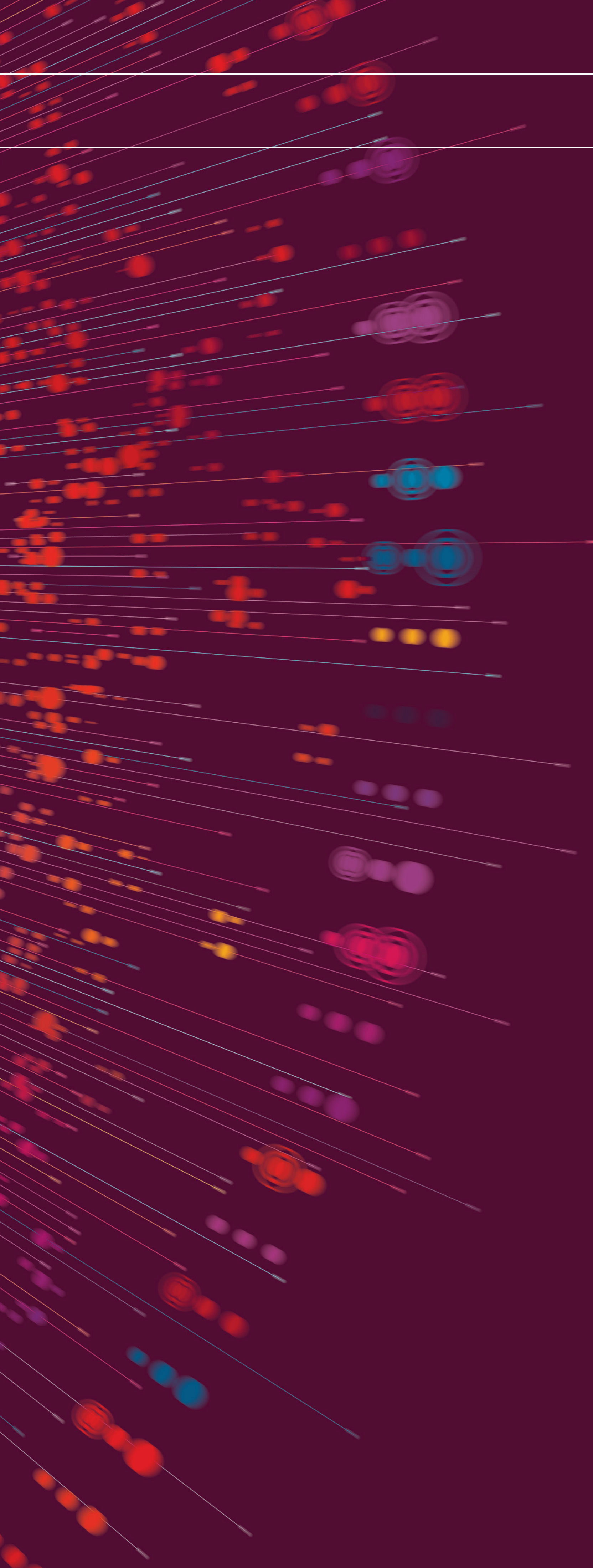
This first instalment is dedicated to giving you unparalleled insight from GPs at the cutting edge of tech adoption – from AI-driven sourcing algorithms to big data-powered portfolio synergy plays. But it also shines a light on some of the most innovative service providers, working in the background to give fund managers the tools to radically overhaul their origination and value creation playbooks.

Because while we remain convinced that private equity will always be a people business, where human touch and EQ ultimately trump cold data, one thing is now clear: the Excel spreadsheet is fast going the way of the Rolodex, and GPs can ill afford to get left behind as technology radically transforms both the industry and the businesses it supports. ●

GOING DIGITAL

Nicholas Neveling explores how GPs are harnessing big data and AI not only to boost portfolio company performance, but also to provide a competitive edge when it comes to sourcing and executing deals





Private equity is at a digital inflexion point as growing numbers of managers embrace technology to gain a competitive edge in the core business of deal sourcing and portfolio management.

When it comes to back-office functions, technology has played a crucial role in helping managers meet rising investor expectations for faster, more detailed reporting and fund accounting. But digitalising the private equity front office has been a tougher nut to crack in an industry where ‘pressing the flesh’ and the black books of savvy dealmakers have long been the primary drivers of dealmaking and value creation.

Rapid developments across deal software, artificial intelligence and data analytics, however, are reshaping how managers think about supporting core front-office functions, and are driving a surge in uptake for technology in front-office settings.

A poll of 110 private equity LPs by Coller Capital found that 75% of respondents saw artificial intelligence as a useful tool for originating dealflow, with 60% saying it could be useful as part of a deal assessment or post-transaction portfolio company engagement. In a separate survey published at the end of 2023, EY found that 74% of private equity-backed portfolio companies were already using or piloting the use of AI solutions in their transaction processes.

“Firms are incorporating digital lenses into target screening, using alternative data sources to conduct market screens, using large-scale company data to identify add-on opportunities and leveraging data from other assets in a portfolio to inform investment theses,” says Andy Roberts, an associate partner at Bain & Company. “We’ve seen, for example, firms using credit card and e-receipt data, web traffic, search traffic, blog mentions, Amazon scraping and tech reviews to spot fast-growing brands that are under the radar.”

74%

Almost three quarters of private equity-backed portfolio companies were already using or piloting the use of AI solutions in their transaction processes in 2023, according to EY

The strategic importance of GPs’ tech enablement has become especially apparent through the current macroeconomic downcycle.

GPs with the digital capability to collate data quickly and accurately, and gain early visibility of portfolio performance, sector trends and deal valuations, have been much better positioned to navigate market headwinds and keep deal pipelines flowing in flat markets.

“Looking back at 2023, global private capital dealmaking was much slower compared to the record activity in 2021 and 2022. Our analysts view this as a market correction, rather than a collapse [...] this correction has made reliance on data and insights more important than ever,” says John Gabbert, founding chief executive of private markets data and intelligence provider PitchBook.

Technology is also becoming increasingly important for GPs when articulating their investment propositions and points of difference to prospective LPs.

“Tech enablement is becoming an important differentiator for GPs, and more and more investors now demand that GPs utilise technology to enhance their operations,” says Yuriy Shterk, chief product officer of Allvue, a specialist alternative assets software developer. “Accessing data and being able to slice and dice it to understand how capital is being deployed is becoming an essential capability that LPs want to see managers evidence.”

Still early days

Progress with the implementation of front-office digital tools, however, varies significantly across the industry, with many firms still testing the waters and assessing their specific organisational requirements.

“Private equity is a young industry and managers are working out what processes can be improved and where technology can have an impact,” says Yann Magnan, chief executive and co-founder of 73 Strings, a software company focused on illiquid asset classes. “The priority for all managers is to identify the tasks that are necessary but relatively low value, and can be taken off deal teams and managed with digital tools.”

Pinpointing these workflows and selecting an appropriate technology solution, however, is not always obvious, and there is a delta emerging between private equity’s technology leaders and managers that are only just embarking on their digital transition.

At one end of the spectrum, some managers have recruited dedicated development teams to build proprietary data analytics platforms that use machine learning and algorithms to identify deal targets and scope out transactions early in the origination pipeline. At the other end, some managers that have run successfully for years using very basic technology tools are now looking to upgrade their front-office technology infrastructure.

"Across the market, dealflow is much more visible and much more competitive, and if you want to win deals you have to have all of your ducks in a row," says Matthew Hardcastle, vice-president of industry solutions for Intapp DealCloud. "All of your deal intelligence and knowledge has to be pulled together in one place. You want to be investing firm time in the right assets, rather than just reacting to what is coming in. Data and pipeline management are central to that."

Data demand

Aggregating data into one place is the starting point for building this capability. This enables firms to build deeper, more proactive visibility of key performance indicators for existing portfolios in the first instance, which can then be expanded to cover shadow portfolios and potential target companies.

"Structuring data correctly and aggregating data into a single place is the first step," Magnan says. "Collating data from across a firm into one data warehouse is mainly a mid-office function, but the process does have impact and potential for the front office. The ability to extract meaningful benchmarks from existing portfolios gives GPs a much clearer picture of the best-performing strategies and value creation levers. This intelligence feeds into the deal origination process and provides deal teams with insight into the most attractive companies and sectors to invest in."

Firms that have successfully aggregated data and built data lakes are now taking the next step, layering third-party data and AI tools over their data pools to drive further gains.

"The most successful firms have shown great discipline around how they triage and manage their deal pipelines and are now taking that further. Once processes are running well, forward-thinking managers are exploring how they can use third-party data and ChatGPT-like functionality to summarise deal intelligence and make people more efficient," Hardcastle says.

Data providers have recognised this demand and are supporting managers by developing tools that facilitate the integration of their data into the data lakes of managers.

"Our solutions are often custom-built to each client's unique requirements," says Laura Gonzalez, EMEA and customer success managing director at PitchBook.

3/4

The proportion of LPs (75%) that see artificial intelligence as a useful tool for originating dealflow, according to a survey by Coller Capital

> **The technology is there to make resources and contacts available to portfolio company teams without overwhelming them**
>
> **Lucie Mills**
>
> *NorthEdge*

"We offer direct data feeds, CRM (customer resource management) integration, and API (application programming interface) solutions that have customisable queries and robust analytical tools to digest large quantities of data within existing business systems."

Gaining an edge

Firms that have successfully embedded digital tools into front-office functions say they have been able to accelerate target identification and expedite deal conversion.

"Put simply, our time to target identification is faster, and our quality of insight and foresight stronger, which drives our target discovery to be six to 12 months or more ahead of the market, and our conversion ratios of lead-to-execution substantially ahead of peers," claims Yair Erez, a partner at midmarket buyout firm Stanley Capital. Read our interview with Erez on page 22.

Large-cap manager Permira, meanwhile, has established an advanced analytics unit within its value creation team to provide direct support to portfolio companies and explore ways to drive growth and efficiencies through the use of data analytics and AI.

"Broadly speaking, our strategy is to work with and encourage our portfolio to experiment with GenAI applications, and as part of that, leverage the portfolio as a distributed laboratory to rapidly prototype solutions and then share the learnings within the portfolio," Permira vice-president David Floyd says (turn to page 8 to read our full interview with Floyd). "There is an average of three GenAI development projects currently live in each portfolio company – over 200 in total – with new initiatives being identified continually."

In addition to its work directly at portfolio company level, Permira has also developed internal tools to support front-office work. One of these, Gaia, is an internal platform the firm developed to run AI tools securely across all of its internal data.

"The initiative started as an experiment to see if we could use generative AI effectively, and we are now in the production phase. We have seen teams across the whole organisation use it," Floyd says. "It is still early days but initial indications suggest that every individual using the platform saves between 5% and 11% of their time every week. The exploration and testing of ways to use the technology to automate more simple tasks, as well as handle autonomous workflows, is an ongoing process."

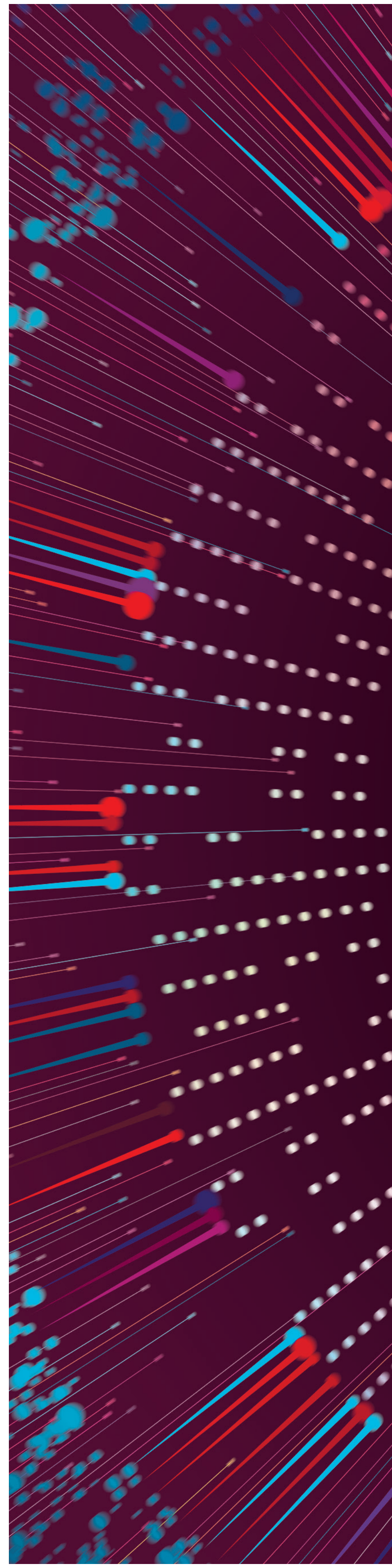
Permira has also built a second proprietary platform called Prism, which provides readouts of a target company's customer churn 'health', as well as its upselling and downselling performance.

Proprietary or in-house?

Reflecting the industry's wider approach to operational support, firms have used a mixture of proprietary and third-party technology when digitalising front-office workflows.

Permira, for example, has explored using complementary third-party technology options to support and enhance its Gaia and Prism platforms. These include AI-powered enterprise search tools such as Hebbia and Glean, as well as automated workflow tools like Dataiku.

Midmarket manager NorthEdge, meanwhile, uses Microsoft Dynamics as its CRM and third-party data visualisation tool Cobalt, but also works with AI academics at the Alliance Manchester Business School to develop bespoke AI-powered deal-filtering tools.



> Accessing data and being able to slice and dice it to understand how capital is being deployed is becoming an essential capability that LPs want to see managers evidence
>
> **Yuriy Shterk**
> *Allvue*

In addition, NorthEdge has built a proprietary portfolio support tool called Nexus, which serves as an interface between portfolio company senior management teams and the NorthEdge operating partner network.

"Nexus has been a really efficient way to bring relevant groups of people together across the portfolio to share knowledge and information and facilitate networking. The technology is there to make resources and contacts available to portfolio company teams without overwhelming them," says NorthEdge partner Lucie Mills (turn to page 14 to read our full interview with Mills). "Nexus is a ready-made content hub – covering everything from pricing strategies and recruitment to customer engagement and supply chains – that portfolio companies can draw from whenever they require it."

Dealcloud's Hardcastle says that managers will typically turn to established software providers for core areas such as CRM, portfolio monitoring and fund accounting technology, then develop in-house tools to cover more specialist, bespoke internal requirements.

Working in tandem

Whether managers are using in-house technology, off-the-shelf software, or a combination of both, the industry is still a long way from reaching a point where technology can realistically replace the value of human insight in the dealmaking process.

Critical thinking and personal relationships are paramount. The role of technology is to produce actionable data that complements the deal team's judgement and allows dealmakers to spend more time with management teams and less time on manual tasks that can be automated and streamlined.

"We are not trying to replicate everything we do, but rather harness technology to give us more insight, help us get to things quicker and support the building of relationships with potential deal targets and portfolio companies," NorthEdge's Mills says.

The ability to build networks and personal relationships with management teams and advisers is likely to remain the most central element of successful dealmaking for some time yet.

But in order to identify and reach these key stakeholders before the competition, it is becoming increasingly important for managers to overlay human insight with digital capability – something even LPs are now keeping a watchful eye on, further fuelling the digital arms race among GPs keen not to get left behind in tough fundraising times. ●

Q&A

Transforming with tech

Opportunities abound when technology is used to its full potential, according to Permira's *David Floyd*

David Floyd, vice-president at global investment firm Permira, talks to *Real Deals* about how the business is harnessing advanced analytics to drive competitive advantage in its funds' portfolio companies, and outlines how Permira is using AI tools internally to support investment teams.

RD: How is Permira using data and analytics to support value creation in the portfolio?
David Floyd: Permira established an advanced analytics team within the value creation team about five years ago, with its primary function being to identify ways to use technology to help management teams to drive value creation at the portfolio company level.

We strive to find the most impactful use cases for data and AI in portfolio companies, show companies what they can do with their data and then demonstrate proof of concept to the management team. We will get involved in some forecasting if there's a clear bottom-line opportunity, but top-line growth is the main priority.

We do not mandate that all portfolio companies use the same software or follow the same implementation blueprint. The aim is to help each company find the right tool and right process for the right situation. There are, however, recurring themes that we have observed and we regularly see advanced analytics utilised to drive improvements in pricing, customer churn and personalisation.

We also have a significant focus on knowledge sharing. If you take the example of AI, we have built a community of more than 260 senior stakeholders across our portfolio who can collaborate through various forums, roundtables and a new digital engagement platform.

This is proving a very fertile community and helps our portfolio companies stay up to date on the latest – and rapidly evolving – regulatory environment relating to AI. It also allows these companies to take part in topical training sessions, deepen partnerships with vendors and develop collaborative exercises between portfolio companies.

At the same time, the portfolio companies have been continually experimenting and sharing knowledge about various GenAI tools – such as Enterprise ChatGPT, GitHub Copilot, AWS CodeWhisperer – to find ways to improve productivity.

RD: How are you approaching the topic of AI more specifically in the portfolio?
Floyd: Broadly speaking, our strategy is to work with and encourage our portfolio to experiment with GenAI applications and, as part of that, leverage the portfolio as a distributed laboratory to rapidly prototype solutions and then share the learnings within the portfolio. As part of this, we are encouraging all companies to ring-fence teams to ensure a focused approach.

There is currently an average of three GenAI development projects currently live in each portfolio company – more than 200 in total – with new initiatives being identified continually, either by dedicated R&D teams from within business functions or through company 'hackathons'. In a tech portfolio, this average figure can be as high as 10.

RD: With regards to your work on the firm's internal technology capability, what is the focus and what are you hoping to achieve?
Floyd: During the last 12 to 18 months, one of the major areas of focus has been to work closely with our CTO to look at how Permira can drive performance advantage for the firm and the Permira funds from generative and predictive AI. We have explored everything from deal origination, due diligence and value creation through to portfolio management, financial reporting and ESG compliance.

We have built an internal platform for running AI tools securely across all of our internal data. The platform delivers similar output to what you would expect from a tool such as Microsoft Copilot, but we decided to do the build in-house so that we could learn about the technology as fast as possible, deploy it quickly and not be tied into any one vendor. Developing the platform internally has also helped us to deal with the information security challenges that come with deploying this kind of technology, which are significant for any private equity manager.

The platform is called Gaia; it is live and working. The initiative started as an experiment to see if we could use Generative AI effectively, and we are now in the production phase. We have seen teams across the whole organisation use it.

It is still early days but initial indications suggest that every individual using the platform saves between 5% and 11% of their time every week. The exploration and testing of ways to use the technology to automate more simple tasks, as well as handle autonomous workflows, is an ongoing process.

We have also developed a second tool in-house – Prism – which produces a visual and predictive readout of a company's customer churn 'health', as well as its upselling and downselling performance. Pulling together that information supports a much more informed management conversation.

> **The aim is to help each company find the right tool and right process for the right situation**

In addition to the platforms that we have developed ourselves, we have also explored a few complementary third-party technology options. Hebbia, Glean, and Dataiku are the tools we are most familiar with – Hebbia and Glean serve as AI-powered enterprise search tools, similar to Gaia and M365 CoPilot, while Dataiku operates as a broader platform for deploying AI/ML models in automated workflows.

It should also be said that as part of all of this work, we have worked closely with our legal department to ensure that all AI tools operate mindful of relevant

> **The AI finds the needle in the haystack and uses natural language processing-style analytics to pull out something structured from something unstructured**
>
> *David Floyd, Permira*

compliance frameworks and procedures.

So, if I am on a deal team and I log in to one of the tools, how can they support me through the deal process?

Tools like Gaia assist dealmakers with finding and synthesising relevant documents at speed. A piece of analysis that would have been a huge undertaking because of the time it would take to assemble the relevant documentation can now be done in a couple of hours. It might also help to compile a quantitative picture of a company or opportunity out of the mass of available commentary and qualitative data.

These are common applications for generative AI. The AI finds the needle in the haystack and uses natural language processing-style analytics to pull out something structured from something unstructured.

Tools such as Prism provide deep insights into a company's revenue flows and areas of risk or opportunity early in the diligence process, to support evaluation and to provide value to management teams.

We also have a proof of concept for using AI to not only identify top-performing companies in particular sectors, but also to recognise characteristics that may not be immediately obvious but can predict growth and outperformance.

RD: Are there any particular highlights or success stories from your team's work that stand out?

Floyd: Personalisation has been a powerful lever. Customers increasingly expect a personalised service from brands; this is especially true at the luxury end of the market. More than half the growth (and high tens of millions of euros per year in direct-to-consumer revenue) at one of our luxury goods portfolio companies, for example, has been due to the personalisation programme that we put in place.

Improving customer retention in the portfolio has been another highlight. Increasing retention by 5% can lead to a company's profits growing by anywhere between 25% and 95%. It has been interesting to observe how translatable this model is, and the success of the model is what led to the development of Prism.

Finally, pricing is an interesting area and can yield exceptional results when done well. One of our portfolio companies saw gains in the tens of millions of euros after using technology and data analytics to analyse how it was using promotions and signals at the best times to market promotions to customers.

RD: What are some of the biggest challenges you have encountered when it comes to the implementation of new technology in a company, and how can these hurdles be navigated?

Floyd: The challenge that comes up time and again is the siloing of data. What we are trying to do is to find signals in data but what we often find, particularly for early-stage companies, is that managers are focused on their own KPIs and are not really interested in what other parts of the business are doing.

Therefore, when you are trying to leverage data analytics and AI, implementing cultural change is central to the success of the project. Often you will want to change the culture of the company completely, but that is not realistic. The key is to identify the culture that exists in the company and adapt, making subtle changes to make data and AI work for the business.

A journey of discovery

Philippe Laval, chief technology officer at Jolt Capital, discusses its proprietary software platform Ninja, and reflects on the highs and lows of bringing the system to life

RD: How does your firm incorporate technology into the deal origination process? Are your systems off-the-shelf or built in-house?
Philippe Laval: We have developed our own software tools in our own system to find interesting investment opportunities for Jolt. Every day, partners use this system – which we call Ninja – to get suggestions of companies they could reach out to, or to find out more about a company that they have heard about elsewhere – for example, who its competitors are.

Ninja also indexes all our office emails, so we can share all our knowledge and insights firmwide in an easy and secure way.

While Ninja is our own system, it is like an umbrella. Every time we find a new service that could be useful – for example, the new open AI tools that are emerging – we integrate them into Ninja.

RD: When did you start implementing Ninja, and what drove you to do so?
Laval: We started developing Ninja in 2017 and had two key reasons for developing the system. Firstly, we wanted to know how deep the market in growing technology companies was in Europe, and whether it was deep enough that targeting only companies in this category could be a viable investment strategy for us; Ninja gave us a way to conduct a census.

Second, it was the way to scale our business. We felt that there were two ways to attempt to grow. One would be to hire a large amount of junior staff members, send them to a lot of commercial shows and pitch meetings, and have them report back to us. The alternative would be to use technology to give partners direct access to the markets in which they were interested in investing.

We said from the beginning that we would take the latter option because we did not want too many layers of people between a potential portfolio company and those who make investment decisions.

Cost was not a motivation initially. To create Ninja, we needed to hire a full-time chief technology officer and software developers, and buy data, so at the beginning it was a significant financial investment. Now that we have scaled the project however, cost has become a third reason for having Ninja. The system has become cheaper than having people doing an analogous job would be.

In addition, with Ninja we have built value inside Jolt and created something that we can continue to use in the future, whereas human knowledge and skills can be lost when people move on. As entrepreneurs, we wanted to build a real company, not just an investment vehicle, and Ninja has become part of that.

RD: What were the biggest challenges you faced when you first implemented Ninja, and what are your current challenges?
Laval: The first challenge at the beginning was understanding what kind of analytical system could be built. The European geographical area we were looking at is very fragmented, perhaps 20 countries speaking many different languages and each with their own different national register for companies.

Then there was the question of what makes a good investment for us. Can we identify a fixed set of characteristics for a business that Jolt should invest in? The answer is no.

Next was the challenge of adoption. Every partner was committed to using the system but it was so different to the tools that they were used to using. To be honest, at that stage Ninja was still developing but it had to be used otherwise it would never be a great system. Everyone was very supportive, so in the end it worked.

Now that the system is working better, the challenges are different. The data problem is solved. We now have access to information about almost four million companies and know how to get the information we need about them. Adoption is almost completely solved. People at the firm are so used to Ninja now that it is almost as much a part of their daily working life as email. We

The idea is to give a superpower to the investor at Jolt so they can be more efficient at doing their real job, which is to connect with an entrepreneur, understand their business model and work towards an investment

Philippe Laval, Jolt Capital

were also lucky that our managing partner said nobody should look at non-Ninja companies.

After six years of using Ninja, we have a huge corpus of companies – almost 30,000 – that have been tagged as 'interesting' or 'not interesting' by every investment partner, so we can use our deep-learning system to tell us how aligned any other company is with Jolt and our goals.

Now we have the challenge of continuing to innovate, in particular to bring something even more useful to the partners: analysis at an ecosystem level. That could mean taking the names of, say, two companies in an industry and having the system build a competition map around them. If you were looking at companies working with drones used in agricultural technology for example, the system might break this field down into subsectors, such as precision agriculture, drone construction, sustainability for drones, and so on, and then show you companies in each one. This is what we are striving for but it is difficult.

The other ongoing challenge is finding good software developers. It is not that easy to get good potential employees to work for an investment firm because they would often rather be at a technology giant like Google or a startup.

Then there is the problem of scaling what we already have. Analysing millions of companies is not the same as dealing with 200,000, and we want to keep the system fast and not too expensive. Finally, we would like to move up another level and analyse other GPs as well as companies' to find out who invests where and how much.

RD: What are some of the successes you have had since starting to use Ninja? What pain points have you been able to eliminate or mitigate?
Laval: When Ninja started and was suggesting a company to a partner, they would decline 80% of the time. Now, it is the opposite. I would say that now about two-thirds of our dealflow is generated by Ninja, and our last four investments all came from the system.

The system will suggest a company to an investor, who will then complete some pre-deal diligence, using the system as a single point of truth to share information. Months will then pass between this first suggestion and an investment, and it becomes a question of human interaction with the founding entrepreneur as we build a common investment case, so the process is the best of both worlds.

The idea is to give a superpower to the investor at Jolt so they can be more efficient at doing their real job, which is to connect with an entrepreneur, understand their business model and work towards an investment.

RD: In what ways does your use of Ninja extend to the value creation process?
Laval: We use Ninja to look for bolt-on acquisitions, and a little to assess exit potential. We also give our portfolio company executives access to the system, so that they can search for bolt-ons or competitive intelligence themselves.

RD: Do you have any highlights that stand out in that value creation area when it comes to technology?
Laval: I can think of two of our portfolio companies, both of which were suggested to us by Ninja a few years ago, that are now using Ninja to find acquisitions. One of them, a biotech company, is doing as many as two bolt-ons a year.

RD: Do you think LPs see the use of technology during origination and value creation as a differentiating factor for a private equity firm?
Laval: We have just closed a €100m extension to our fourth fund and we are already starting to raise fund five. Every meeting with an LP or potential LP included a Ninja demonstration. Most of the time they went on to ask for access, which we are happy to grant.

Ninja also features a lot in our LP marketing in other ways. Every week we publish data, a business map, or something else potentially useful to our LP network that we have drawn directly from the system.

Building a tech Nexus

NorthEdge's *Lucie Mills* and *James Hales* discuss how the mid-cap GP is using technology to support deal origination, identify potential deal targets and enrich various interactions

RD: How is NorthEdge incorporating technology into the front- and middle-office functions of deal origination, deal execution, portfolio management and value creation?

James Hales: Deal origination in the midmarket is incredibly competitive and everyone is always chasing the same ball. Every manager is working to find assets off-market or go into adviser-led processes with some kind of advantage. Several managers are now using software to help deal teams to identify potential deal targets by sector and size.

We have worked on developing our own AI and machine learning tool for about seven years now. We first worked with Peak, an AI consultancy in Manchester, to get the platform off the ground, and now we are working with Alliance Manchester Business School to develop the technology further. We work closely with Richard Allmendinger, a professor of applied AI.

Fundamentally, we are trying to develop a tool that uses a variety of financial metrics and selection criteria to catch businesses with high potential early, in a more sophisticated way, so that we can build relationships with relevant businesses that we may invest in.

Lucie Mills: We have also built a platform for our portfolio community called Nexus. It is a proprietary product that we built ourselves, exclusively for our portfolio company management teams. Portfolio company chief executives, chief financial officers, sales leaders, marketing leaders and technology leaders all use it, and it also interfaces with our operating partners network.

Nexus has been a really efficient way to bring relevant groups of people together across the portfolio to share knowledge and information and facilitate networking. The technology is there to make resources and contacts available to portfolio company teams without overwhelming them. Nexus is a ready-made content hub – covering everything from pricing strategies and recruitment to customer engagement and supply chains – that portfolio companies can draw from whenever they require it.

As James highlighted, a general point of principle for us when using technology is that it is there to complement the relationship-focused part of our work.

We are not trying to replicate everything we do, but rather harness technology to give us more insight, help us get to things quicker and support the building of relationships with potential deal targets and portfolio companies.

James Hales: When speaking to a management team, a tool like Nexus provides a clear demonstration of how we can add value. Lots of managers talk about value creation but don't have anything tangible to evidence that. With a platform like Nexus, we do. It is a massive unique selling point.

One area where Nexus has been especially helpful is around ESG. Management teams have been far more challenging around ESG, so the ability to be able to showcase Nexus to them, where they've got access to all our ESG reports as specific examples of how we help companies to add value using ESG is very powerful.

The reality is that there are many suitors out there for management teams to choose from, so being able to point to specific examples of what we can offer is a key point of differentiation.

RD: As you have developed your own proprietary technology, what have you learned with respect to making sure the technology is doing what it is supposed to?

Lucie Mills: Let me answer that in terms of how we use technology to support portfolio management across the firm.

We are not trying to replicate everything we do, but rather harness technology to give us more insight

Lucie Mills, NorthEdge

The key principle is to keep things as simple as possible. We have made a conscious decision that we want to keep everything on one platform. There are so many excellent technologies and tools available, and it would be great to be able to use them all, but it is important to keep the technology interface with our portfolio companies clear and simple.

When capturing data and financials from portfolio companies, we don't ask for more data than we need, and we are totally clear on why we are asking for information and what we do with the information they share with us.

We have one system that all the information flows into. It is a repository for all the ESG, financial and value creation metrics. We use portfolio management software from Cobalt to facilitate that.

RD: Why has holding data in one place been such a priority?

Mills: There has been a focus across the firm on achieving real data integrity. Bear in mind that we have invested in 44 companies over an 11-year period from four funds. Making sure that we are on top of all that data, and focusing on data integrity, is the only way that we can then leverage technology.

We could have started leveraging technology two or three years ago but we wanted to make sure that we're not just using technology for the sake of it, but rather drawing insights from the technology. That all comes down to data quality, which has been a massive focus for us.

Data visualisation and data automation will be the next big priority areas for us, with those capabilities layering over our CRM – we use Microsoft Dynamics – and Cobalt systems to make the technology really dynamic. These programmes do have data visualisation capability but we are working towards the formation of a single lens that sits across all of the systems.

As a dealmaker or business leader, I don't want to have to go into four systems to source my information. I want to go to one place and see it all. So that's why we want to spend more time on that visualisation piece and put everything in one place, making it easier to look at and easier to compare and contrast.

The end goal is to put information about our business into the fingertips of everybody in the business. That can help an investment team when they're looking at a track record in a sector or a geography or a deal. It can help when we are going fundraising and speaking to investors. It can help when we're just answering general queries or looking at deployment rates.

Rather than someone having to run around and gather up figures from various sources, everyone will have access to all of the data and will be able to self-serve. That is very exciting.

There are many suitors out there for management teams to choose from, so being able to point to specific examples of what we can offer is a key point of differentiation

James Hales, NorthEdge

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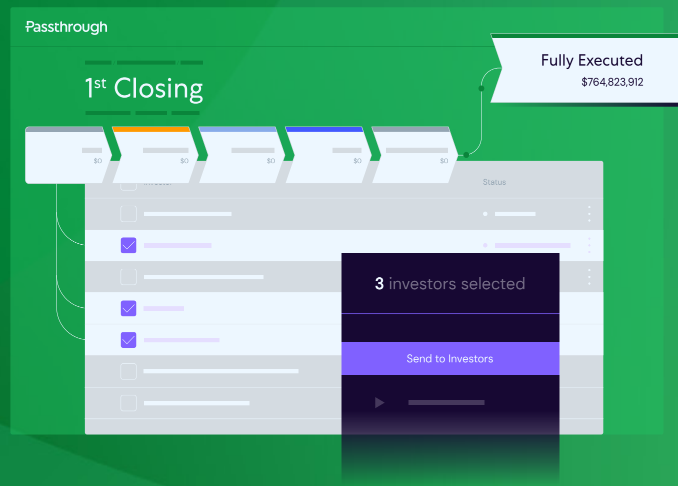

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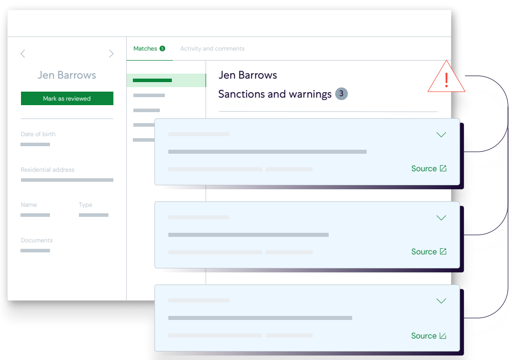

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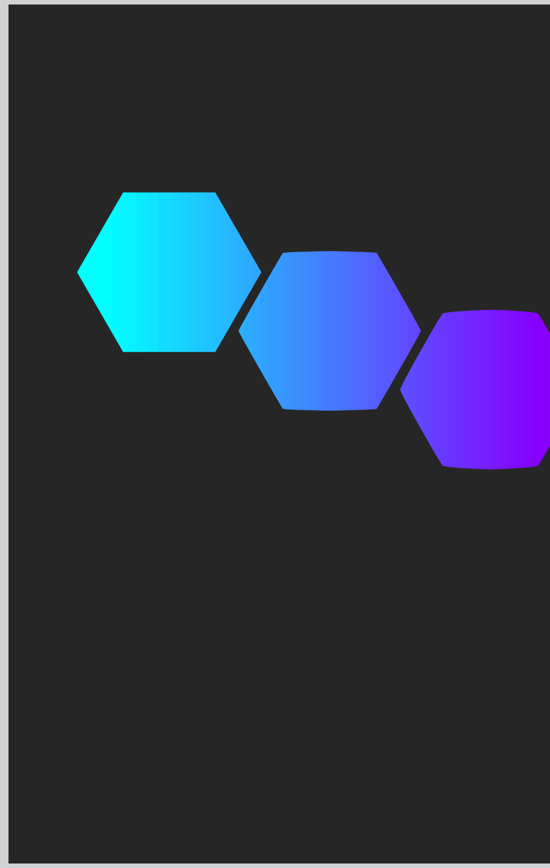
Entering a transformative era

AI-based deal-sourcing tools can automate market mapping and company research, giving firms the time they need for higher-value activities. *Ruth Eagle* is head of origination at CBPE, a client of deal-sourcing platform Sourcescrub



RD: To what extent are private equity firms embracing technology when it comes to deal origination today?
Ruth Eagle: I have been working in private equity for seven years and the adoption of technology within that timeframe has increased significantly.

When I first started out in the market, the industry had access to a handful of data sources but origination was largely a manual process. Origination teams would trawl the internet looking for potential targets, stitching together maps in a long-winded and not particularly sophisticated manner.

Fast forward to today, I think most midmarket firms have recognised that they need to be a lot more tech-forward when approaching origination. At the same time, platforms like Sourcescrub have emerged, allowing sponsors to be more sophisticated in the way that they identify investment opportunities. For us, engaging with Sourcescrub has helped to dramatically cut down on the time spent mapping markets, automating away many of the most laborious and manual tasks.

As a result, many private equity firms today are now embracing technology in the origination function and elsewhere within the organisation. Adoption has also been driven by an increasingly competitive market – and technology can be a great differentiator.

RD: Do you view true artificial intelligence as a game changer when it comes to deal sourcing?
Eagle: There has been a lot of talk about artificial intelligence in recent years but very often, when people have used the terms AI or machine learning, they have actually been referring to something less sophisticated. It has only really been in the past 18 months to two years that we have witnessed a significant jump forward.

Private equity firms are now able to use AI and machine learning models in a genuinely transformative way.

For example, we are currently using AI platforms to help us screen and profile businesses more efficiently. Instead of manually pulling together information to triage businesses, we are now using a generative AI programme to do the same job in half the time. Additionally, we have employed machine learning to map markets by identifying companies based on specific inputs.

Machine learning and AI will be a game-changer during the next couple of years and I expect to see more tools emerging that can be applied to deal origination. This is a journey, and the industry is still very much at the start.

RD: What are the first steps that any private equity firm thinking about embarking on this journey needs to be thinking about?
Eagle: Our strategy was to start by ensuring that all our underlying data was high quality and well structured. If you point AI or machine learning models at inaccurate data you will get inaccurate results, which will not improve over time. Once you have ensured the accuracy and quality of your data, only then will you be in a position to realise AI gains.

There are also some quick wins that can be achieved by using tools such as ChatGPT or Microsoft Copilot, which can make swift work of cutting out unnecessary manual tasks.

Sourcescrub has implemented a secure GPT model in the platform

Once you have ensured the accuracy and quality of your data, only then will you be in a position to realise AI gains

Ruth Eagle, CBPE

This is a journey, and as an industry we are just setting off

that acts as a co-pilot for sourcing activities. There are also firms that are using machine-learning algorithms to help predict which businesses may be of most interest. For certain investment strategies these can be a quick and efficient way to get up the AI curve.

RD: As the number of potential technology partners continues to proliferate, how should private equity firms decide who to work with? What questions should they be asking?
Eagle: As mentioned just now, data accuracy is the most important factor for us; how is that data generated and where does it come from? If you delve into the core data model and discover that the data they are using is not accurate in the first place, then applying machine learning or artificial intelligence onto those data models is only going to produce the wrong outputs.

This is one of the reasons we have chosen to work with Sourcescrub, and recently made the decision to use its data as a core part of our data warehouse initiative.

Focusing on the foundations – where the data comes from and how it is joined together – is absolutely critical.

You also need to think about how technology partners fit into your work processes. What gap are they filling and how will they improve your workflow? One of the reasons we chose to work with SourceScrub is that its solution was a great fit for some of the processes that we were performing manually and integrated easily with our CRM to help us join the dots.

RD: In addition to ensuring that the underlying data is sound, what other potential risks are involved in employing artificial intelligence in the origination function and how can these best be mitigated?
Eagle: One of the challenges that we have encountered stems from the fact that our investment strategy is broad. There are predictive models in the market that are designed to surface the most interesting targets for a given fund. We are considering carefully how to apply such models in a way that fits our broad investment strategy.

It is important to ensure that any technological tool and partner you are engaging with is a good fit for your strategy. Do not make the mistake of thinking that just because it involves artificial intelligence or machine learning that it is automatically going to solve all your origination problems.

RD: How do you see the use of artificial intelligence in deal sourcing evolving going forward and what other functions within private equity do you see as ripe for transformation?
Eagle: I think that AI and machine learning models are going to become a lot more accessible and a lot easier to implement, particularly as tech giants such as Microsoft continue to introduce AI into their software.

In terms of other parts of the business that can be enhanced with the use of artificial intelligence and machine learning, our portfolio team is seeing great results when it comes to improving the way that our businesses are managing and using their own data. There are significant gains to be made and that is something that we are also actively investigating.

RD: Where would you say we are currently in the AI 'hype cycle': peak hype, trough of disillusion, or slope of enlightenment?
Eagle: I think the industry is only at the start of the adoption curve. We are now starting to see tools emerging that are genuinely useful and that are actually producing positive results.

During the past three to four years, there has been a lot of talk about AI, but practical implementation and use on a day-to-day basis have been far more limited. Now, however, we are on the cusp of seeing what AI can really do when it comes to improving our efficiency and enhancing origination functions.

There is still a long way to go. We are still discovering which tools are the right fit for which strategies and what will ultimately enable us to reduce the time spent on manual tasks, but I believe that these tools could be transformational.

It is important to note that we are not talking about automating away the origination team. It is about giving us back time that can then be spent on higher value activities such as forging relationships with businesses, conducting diligence or developing off-market deals.

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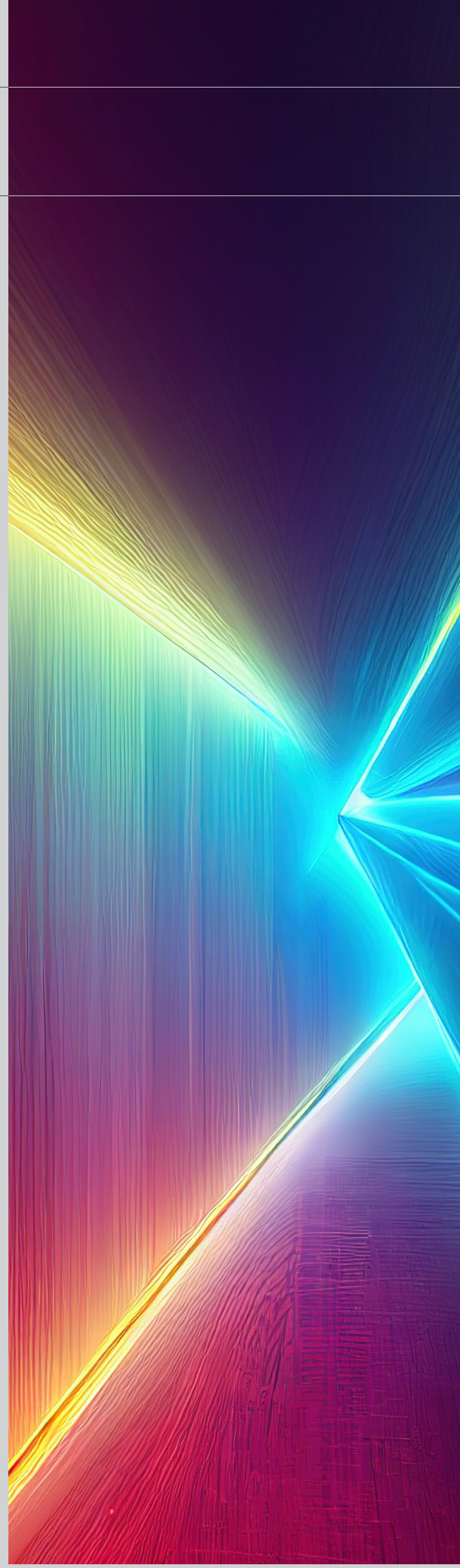
Navigating AI in private equity

Frister Haveman from Gain.pro discusses the role GenAI has in the private equity market and why it should be embraced, not feared



In 2023, ChatGPT marked the biggest release in technology since Google. Since then, GenAI has seeped its way into industries across the globe, compelling businesses to think innovatively about their product offering as well as their internal operations. The same goes for the private equity market.

But given that private equity is traditionally a less technology-driven space, Frister Haveman, co-founder and co-CEO of Gain.pro, explores the impact AI has had on the market thus far. Haveman, along with co-founder Nicola Ebmeyer, built the private market intelligence platform by combining the best of AI technology with expert analysts.

Haveman shares insights drawn from his own experience in private equity and consulting, as well as interactions with clients who are actively implementing GenAI in their operations.

RD: Do you think we are in an AI bubble?
Frister Haveman: I have been working in private equity for seven years and the adoption of technology within that timeframe has increased significantly.

I think we are certainly in an AI investment bubble, but I am also bullish on AI. I am comparing it to the beginning of the 2000s when we had a dotcom bubble and then the dotcom crash. Back then, people wrongly thought the internet hype was over; I think the same is going on with AI.

While there is a lot of hype and likely overinvestment, I think there is significant future potential with AI. The technological breakthrough is real and the magnitude of its impact is huge. Specifically as an investor, you need to be cautious – widely investing in a bubble market can be a risky endeavour. But overall, I think we are going to see genuine innovation from AI of the kind that we have not seen in decades.

RD: How do you think AI will impact private equity in the next few years?
Haveman: It is important to separate between the internal operations of a private equity firm and its investment opportunities and portfolio. I see a few distinctions on the investment side.

Private equity investors are already diligent in checking the impact of the operations of the companies they invest in. They are thoroughly scanning such companies for any risks and opportunities. With AI, this will only accelerate. As the impact of AI becomes bigger on the general economy, it will touch on all the investment opportunities that present themselves. On the one hand, investors will want to invest into this trend but on the other, they will be keen to avoid companies that will be negatively impacted or disrupted by it.

When it comes to the internal operations of a private equity firm, I personally do not feel we are about to see major disruption of the core of investing. I just do not think that the key function of private equity as a capital allocator and an active owner of private assets will be dramatically changed.

However, the impact on the 'engine room' of doing deals is likely quite major and transformational. Throughout the stages of fundraising, sourcing, transaction execution, portfolio work and exits, there are efficiency-gaining improvements to be made. Like any professional service, there are several opportunities to streamline processes and improve efficiency by simply leveraging the technology that is out there. While we may not be on the cusp of being disrupted by AI, you can certainly use it to develop a competitive edge.

RD: How has PE deal sourcing changed over the years and how will it change further with AI?
Haveman: If you look back 30 years, people found companies by leveraging their network or literally driving through an industrial area and writing down the names of the companies they wanted to reach out to. That process has progressed as markets have professionalised and early technology, such as structured databases, has been introduced.

Now we are at the stage where, with AI, intelligence platforms can offer a holistic view of the market. What the best private equity firms are doing is combining this technology with a strong understanding of their sweetspot to prioritise opportunities that are exactly right for them. This way, they streamline their deal-sourcing process and, as a result, source better deals faster than ever before.

But as the markets get increasingly transparent with this technology, they also become more competitive.

RD: How do firms differentiate themselves in today's transparent market?
Haveman: If finding a company is no longer differentiating, your differentiation must come from what you bring to the table. To stand out, it is important to allocate as many resources as possible into differentiation. You can do this by freeing up your teams through automating manual work.

Perhaps paradoxically, in the age of AI, the right strategic response may be to double down on the distinctly human parts of the deal work such as building trusted relationships. However, this can only be done with

“To stand out, it is important to allocate as many resources as possible into differentiation

“GenAI is useful for research and analysis in our space, but in no way threatens the core of human creativity in the construction of deals

Frister Haveman, Gain.pro

significant automation of other processes.

RD: On the portfolio operations side, what are some best practices you recommend investors take when communicating with their management teams about implementing AI?

Haveman: I think that depends on what role you take as an investor. Do you see yourself driving change and educating your portfolio companies, or as the party that looks at financing the balance sheet and having a constructive board dialogue, taking a hands-off approach with operations?

If you are looking to be more hands on, you need to upskill technically within your own firm first before helping your portfolio companies navigate a digital transformation, whether that is about AI or otherwise. If you do not understand GenAI, how are you going to help your portfolio companies?

RD: What role do humans play alongside AI in private equity operations and should we fear AI?

Haveman: GenAI is useful for research and analysis in our space, but it in no way threatens the core of human creativity in the construction of deals. I see it more as an augmentation tool more than anything else. Humans also play an important role in validating the output of technology. Not everything produced by AI can be fully trusted just yet.

Ultimately, you can automate certain jobs, which allows humans to focus on more value-adding tasks – those that AI cannot do.

RD: What are some unique ways you’ve seen PE firms leverage AI?

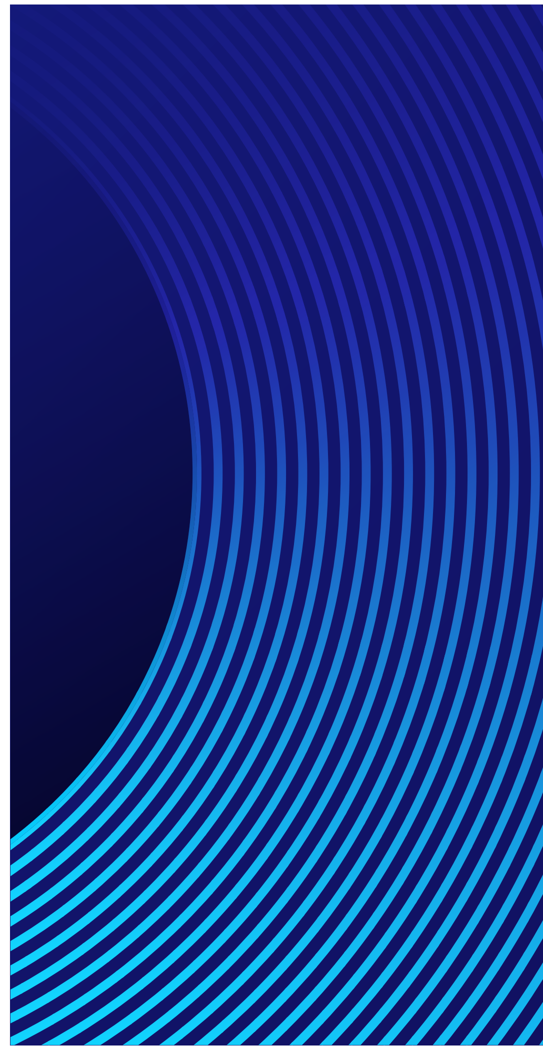
Haveman: I think AI is still at a quite early stage. There are firms out there that have built their own platforms or advanced integrations of third-party data into their own systems, but I have yet to see a firm holistically apply this throughout their entire processes.

I believe some large firms are paying quite a bit of learning money from wanting to be a first mover. Taking the ‘buy’ route in build-or-buy can certainly be a valid strategy still. The best firms are leveraging third-party platforms to absorb data on the outside world and then focusing their efforts on integrating that with the unique and proprietary data they sit on.

There are some very strong examples of that, both on the investment side and with advisers. In general, you also see that VCs are ahead of the game relative to private equity. There is a lot to be learned from them that private equity firms can smartly apply now. ●

A model idea

A bespoke solution was key for ECI's deal origination process according to *Suzanne Pike*, partner and head of origination at the firm



RD: How does your firm incorporate technology into the deal origination process?
Suzanne Pike: We use Amplifind, which is a proprietary AI platform for lead sourcing and prioritisation. At the heart of Amplifind is a machine learning tool that takes and processes data that we have entered into Salesforce about the many thousands of businesses with which we are, or have been, in contact with as potential investee companies.

It looks at areas including company financials, ownership information and keyword metrics, and then produces a prioritised list of opportunities. Each month, one of my team reviews the shortlist on the Amplifind platform and we have a meeting to review each that has been positively selected. This process then flags new lead opportunities in Salesforce for us.

The other way that it helps us is through the automated profiling of companies in which we are interested. We used to have to ask the analysts in our team to produce these profiles, using data from Companies House, LinkedIn, business websites, Google searches and other sources. Now all of that can be done with the click of a button.

Amplifind uses AI to generate rich descriptions of what a company does and how it is currently performing. This means that our analysts are freed up for more in-depth research because Amplifind has taken care of the simpler tasks.

So while it started out as a lead-sourcing tool, it has grown in terms of remit and has effectively become the backbone of our origination research process.

RD: Was Amplifind bought off the shelf or built in-house?
Pike: Amplifind was created completely in-house and is bespoke to us, as the ML models are trained on proprietary data and the UI is designed with our specific business processes in mind, but we did get some help. We used a firm of data analysts and engineers to productionise our prototype in Microsoft Azure and we have intentionally used standardised code in the UI to make the product relatively low risk and flexible from a technological perspective.

We did not want to use an expensive third-party platform that would not actually give us any edge over the competition. In that case we would be making our business fit the technology, rather than making the technology fit our business.

RD: When did you start implementing Amplifind, and what drove you to do so?
Pike: We created the first Amplifind models in 2020 and then embedded the prioritisiation tool in our core processes from 2021.

One driver was that there is so much data out there now that it is not physically possible for humans to get through it all. Using a system like Amplifind ensures that our human skills are deployed to the right business. Another related driver was that, in a competitive market, we were finding we needed to identify leads and meet management teams of target companies earlier and earlier.

That meant that although we had gradually moved up in deal size, the potential universe of relevant growth businesses to trawl through had significantly increased. On average, we engage with a business for five and a half years before investing, and sometimes as much as a decade.

RD: What were the biggest challenges you faced when you first implemented Amplifind, and what are your current challenges?
Pike: We are in the process of exploring a possible partnership with a university applied AI department to look at how we might best leverage our proprietary language-based data. An area that has been harder to crack, however, is the availability of third-party language-based data and good quality keywords.

We have a subsector-driven approach to origination so the better the keyword data we can extract, the better indication we will have of whether a business is a good fit for us.

However, the nature of the challenges has changed radically in just the last few months. Our business goals regarding technology are still the same; to use technology to enhance the origination work we do as humans and to support value

Everybody has been talking about ChatGPT since its launch but, even since then, the growth in the number of new technologies providing quick wins for a business like ours has been phenomenal

Suzanne Pike, ECI Partners

> **There is so much data out there now that it is not physically possible for humans to get through it all**

creation in our existing portfolio companies. What has changed is that the barriers to accessing data are falling away. There are more and more off-the-shelf AI tools available too.

Everybody has been talking about ChatGPT since its launch but, even since then, the growth in the number of new technologies providing quick wins for a business like ours has been phenomenal. The main challenge now is not getting carried away with the technology and staying focused on what we are trying to achieve. The danger is that technology just creates a lot of extra complication in our business processes, which is not what we want.

RD: What are some of the successes you have had since starting to use Amplifind? What pain points have you been able to eliminate or mitigate?
Pike: Ideally, we would be able to point to all the deals we have completed that came to us through Amplifind. But in reality there will always be multiple touch points along the way to an investment. Our goal is to talk to a potential portfolio company before anyone else, but we understand that advisers will get involved later and the process of originating and winning a deal will be multifaceted.

However, I can say that we have reduced the time spent reviewing potential leads by more than 80% and we have seen an eight-fold improvement in terms of converting companies reviewed into leads on Salesforce, when compared with our previous traditional Companies House searches. This is because with Amplifind we can now look at a wider range of businesses in less time.

More than 40% of our pipeline is now sourced from the Amplifind platform. That ratio will increase because we have had Amplifind in place now for almost three years but we typically identify and meet target businesses more than five years ahead of a deal.

RD: In what ways does your use of Amplifind extend to the value creation process?
Pike: We use Amplifind to assess potential bolt-ons and portfolio companies' M&A strategy in general.

Going further, we would like to give the management teams at our portfolio companies direct access to Amplifind so that they can use it to monitor potential targets as well.

RD: Do you have any highlights that stand out in the value creation area when it comes to technology?
Pike: We have found that people are using Amplifind in interesting and unexpected ways.

If we are working hard on a potential deal and we know who our competition is, then we always want to check how investments they have previously made in the industry are performing. Before Amplifind, doing so was hard and would involve a lot of digging around in company accounts. But now we have the ability to automatically profile any business in the UK with one click of a button in Amplifind, this information is available instantly. It is just a marginal gain but, once added to the many other marginal and major gains we get from Amplifind, the effect is powerful.

RD: Do you think LPs see the use of technology during origination and value creation as a differentiating factor for a private equity firm?
Pike: We ran a number of demonstrations of Amplifind for LPs during our last fundraise and had very positive responses.

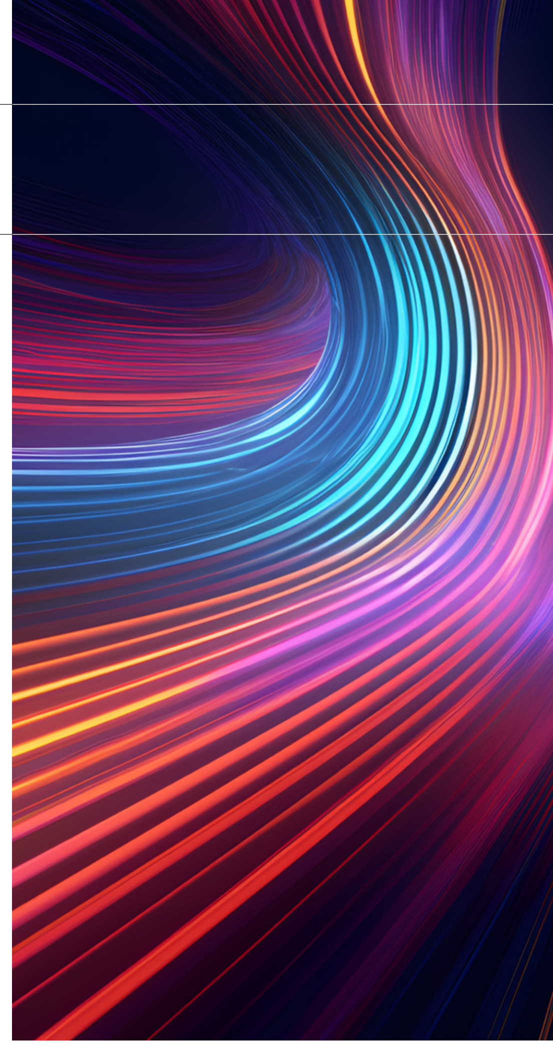
Investors want a track record – nothing trumps that. They also look forward, however, wanting to know that a private equity firm is not just a group of individual deal-doers but a business with a coherent, repeatable model. Effective technology really helps to show that you have good central management and robust processes.

We are going to continue to invest in technology such as Amplifind because we feel that technology will be an even bigger topic next time we fundraise.

Q&A

The digital edge

Yair Erez and *David Poole*, partners at Stanley Capital, discuss how the firm is using a combination of proprietary and third-party technology to accelerate target identification and expedite deal conversion



RD: How does your firm incorporate technology into the deal origination process?
Yair Erez: Essentially, we aim to be a digital business, rather than a private equity firm applying digital. We think that this needs to be a cultural design element, not an accident, so we want digital to be at the heart of everything we do – and that includes permeating throughout our origination process.

Most importantly, we have defined digital as the technology we deploy to help enable our portfolio companies. This includes five ecosystems of automation and two main AI technologies (as opposed to an undefined concept).

Our digital edge in origination starts with our research process. We rely on highly intensive research-led origination, starting with deep dives into sectors and the publication of comprehensive research before we invest. Without technology, this would be sub-economic. Through application of a range of technologies, including proprietary products, we have created faster and more repeatable discovery, synthesis and publication.

Put simply, our time to target identification is faster, and our quality of insight and foresight stronger, which drives our target discovery to be six to 12 months or more ahead of the market and our conversion ratios of lead-to-execution substantially ahead of peers.

RD: What systems specifically are you using? Are these off-the-shelf or built in-house?
David Poole: We have a confidential digital development product plan, using typical off-the-shelf private equity products together with our own bespoke enterprise architecture and tools.

As an example, we have built a powerful in-house origination and value creation engine, Insight, which helps in originating potential investment targets, identifying relative value opportunities and providing a repeatable approach to value creation.

Insight applies the BERT and PaLM family of LLM models, which creates M&A landscapes, from proprietary and published sources, almost instantaneously. The results include clustering of targets, statistical KPI-led differences between clusters of companies in that landscape. This allows us to drill down quickly into sectors, subsectors and identify relevant investment targets.

Our digital-first approach post-origination is in effect a large systems integration and business architecture team that uses RPA, low code/no code, process mining, IDP, business process management, conversational and generative AI to re-engineer business processes. We use best-in-class third-party software in all of these technologies and implement that to facilitate revenue growth, margin expansion and competitive edge into our portfolio companies. This implementation is bespoke to the business and its operational needs.

RD: When did you start implementing these systems, and what drove this internally?
Erez: We have invested in digital products since inception in 2019. We think you cannot be a strong healthcare or resource efficiency GP without understanding how digital can make healthcare more efficient while also maintaining or improving patient care. A strong resource efficiency investor must have a clear idea of how digital can be deployed to save energy and the earth's resources.

Our founding partners have led the strategy to date and initial execution of the digital-first strategy. This has been written into the partnership agreement and now I, as head of transformation, along with David Poole, the head of SCP Digital, are leading the further development of Stanley's IP and helping to standardise this approach.

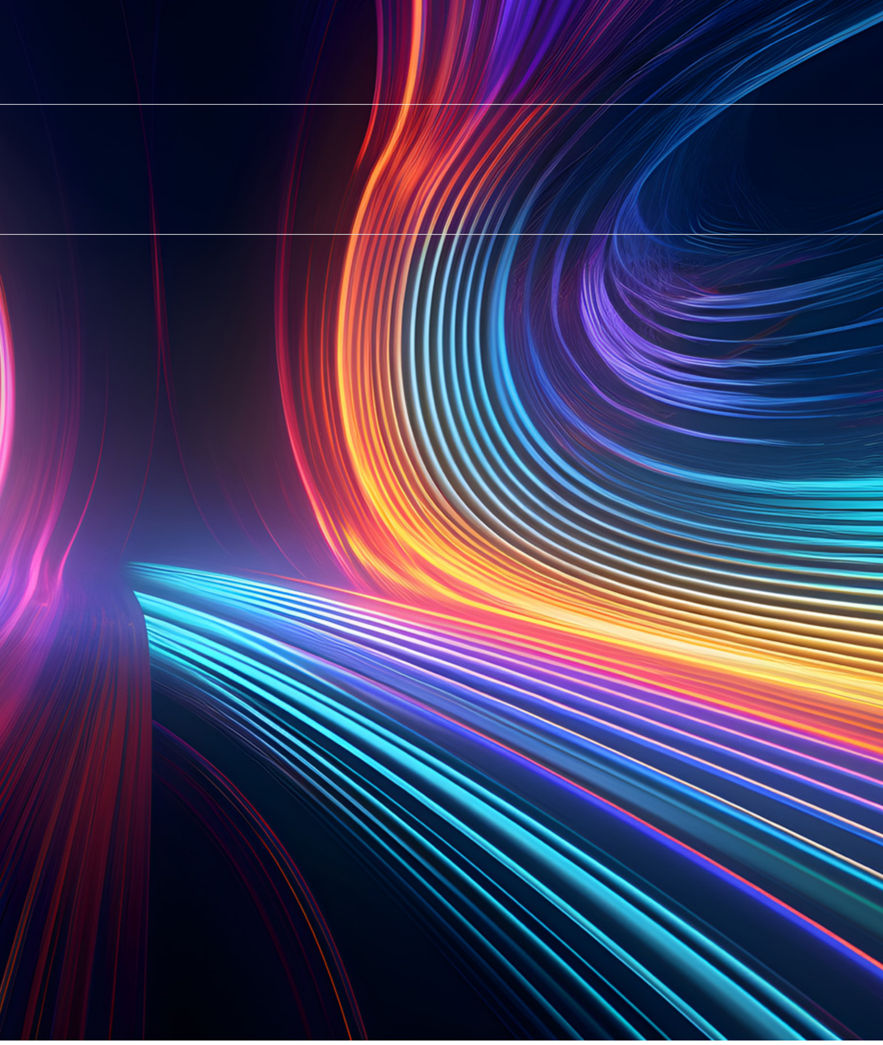
The key steps have included the foundational partnership with UK-based software company Mathlabs to build Insight, through to today's complete portfolio digital transformation capability built around our own SCP Digital platform that has a 120-person team doing hyper-automation, generative and conversational AI, and enterprise digital transformation projects, combined with our partnerships with technology vendors.

RD: What was the biggest challenge you faced when it came to the original implementation, and what are some of your ongoing challenges in managing that technology on a daily basis?
Poole: Our original digital strategy for portfolio transformation was focused on product partnerships led by a small digital team in-house. This model did not have enough connectivity to the market, which was moving faster than a PE-firm's in-house team could track and relied on external implementation skills in a market with a real talent gap that led to inconsistent delivery and time-to-value of projects.

The formation of SCP Digital addressed this design weakness, giving us access to consistent and repeatable transformation SCP processes that de-risk and increase the return and time-to-value of projects. The connectivity to the market is solved by SCP Digital

The continual challenge will be to stay at or ahead of the overall market

David Poole, Stanley Capital



serving third parties as well as the SCP portfolio to drive wider applied learnings and market connectivity to innovation.

This is an emerging area and we will continue to enhance our proposition – across our overall architecture, products and services.

The continual challenge will be to stay at or ahead of the overall market, judging ourselves against the leading applications of technology, not our peers in private equity and their adoption.

RD: What are some of the highlights in terms of success you have had since adopting this approach?
Poole: Qinecsa, an SCP portfolio company in pharmacovigilance technology and services, leveraged our insight and other products to identify and execute five bolt-on acquisitions in less than 18 months.

Key to this execution was the use of Insight, which enabled us to identify each investment ahead of making the initial platform investment. This meant a well planned and seamlessly executed buy-and-build programme was possible. All of the initial conversations for the bolt-ons, bar the last one, were actioned during the first three months of the first platform investment being completed.

Across our platform, through application of a digital mindset, our performance KPIs across pace of origination, conversion of leads to deals, portfolio value acceleration and deployment rate of capital for a small team have all been substantially ahead of peer benchmarks.

RD: What pain points have you been able to eliminate or mitigate?
Poole: Our use of technology has mitigated multiple typical pain points in the deal origination process.

For a start, our digital origination and transformation capabilities look totally differentiated to our competitors, immediately creating a competitive advantage intended to give us an edge when it comes to communication with sellers and management teams in processes. We undertake subsector landscape research promptly, recognising opportunities in minutes as opposed to months, which provides maximum visibility on the target market, and we review higher quality and more relevant opportunities. This sharpens SCP's focus from an early stage onto only the investments that we want and have a right to win, and avoids wasting time on businesses outside our investment strategy.

All of this leads to a higher conversion rate on opportunities, which is a key differentiator for us.

> **We aim to be a digital business, rather than a private equity firm applying digital**
>
> *Yair Erez, Stanley Capital*

RD: Does your use of technology extend to the value creation process? What systems do you use for that?
Erez: SCP Digital leads the digital diligence and value creation plan creation and execution of targets.

We bring SCP Digital with us from the first meetings with a target. With this in-house capability we can underwrite a value creation plan during diligence and immediately execute post-acquisition using our stack or repeatable templates and processes. We do not have to wait for augmentation of CTO or digital teams, target design or vendor selection processes that could take 12 to 24 months.

The first step is to understand how a business works and then map out its business processes. We can do that with our innovative process-mining software. Once mapped, we use the data to understand which technologies would be appropriate to redesign or improve the associated business processes.

Examples of the template tools include productivity and process mining, digital assistants, data structuring, intelligent decisioning, workflow orchestration and robotic process automation, which have been successfully implemented at our existing portfolio companies.

RD: Likewise, do you have any highlights and challenges that stand out in that value creation area when it comes to technology?
Erez: At Qinecsa for example, SCP Digital has identified and is leading implementation of value creation opportunities through automation savings that could increase Ebitda by almost 100% in an already high-margin business.

We implemented process-mining software in the business for six months to fully understand how parts of the business functioned. This identified large cost-saving initiatives through implantation of automation software such as email orchestration and using generative AI to allow touchless processing of adverse events in Qinecsa's end sector of pharmacovigilance.

RD: Do you think LPs look at the use of technology during the value creation process as a differentiating factor for a PE firm?
Erez: While most GPs claim that they use technology to deliver value creation, we believe LPs look for genuine differentiators when assessing GPs.

SCP has a proven capability to drive actual earnings improvement, and therefore tangible value, through highly replicable digital, AI and automation solutions. This is a real digital track record.

Evolving retail trends

Technology has an integral role to play as private markets adapt to the needs and expectations of retail investors and HNWIs, according to *Yann Magnan*, CEO and co-founder of 73 Strings, a global fintech shaping the future of how illiquid assets are analysed, valued and monitored; and *Jonathan Balkin*, co-founder and executive director of Lionpoint, a global operational transformation consulting firm

RD: How must private markets evolve and adapt to address the requirements of retail investors and HNWIs?
Jonathan Balkin: Private markets have historically catered to large, institutional investors, so the industry will need to evolve to address the needs of retail and HNWI investors.

Enabling accessibility for such investors will require lower investment minimums, simplified processes and user-friendly platforms, which have been a challenge historically. Technology can assist by providing intuitive online platforms that allow investors to research, analyse and invest in private market opportunities with ease. From an operational perspective, firms need technology solutions and operating models that can scale from supporting hundreds to thousands, or perhaps tens of thousands, of investors.

The digitalisation of a GP's valuation capabilities will also be an important area to solve. Existing private market investors are used to receiving information much less frequently than the retail and HNWI profile, therefore a monumental shift in the pace of deriving valuations is imminent. The future reporting requirements of new investor classes will not be sustainable without utilising technology.

Yann Magnan: When GPs start addressing retail investors and HNWIs themselves, there will be multiple consequences in terms of distribution, but also in terms of processes. The common understanding is that this new source of capital for the alternatives industry will be reluctant to invest *en masse*, unless they have more visibility as to if and when they can redeem their investments.

Open-ended, evergreen funds are quite often referred to. That will also have multiple consequences in terms of reporting towards this new category of investors, including more frequent valuations, from quarterly to monthly, or even different valuation methodologies. These valuations will also change in nature, from mostly a reporting topic to a topic that will have direct cash/performance impact. I believe that only a great collaboration between best-in-class technology and valuation consultants will be able to scale to address this significant increase in demand.

RD: To what extent will information and transparency be a requirement to attract retail investors and HNWIs into private markets investing?
Magnan: The higher the transparency, the higher the likelihood of attracting retail investors and HNWIs towards alternatives. It is a question of trust, in the same way that public markets have been thriving on higher transparency and more in-depth reporting.

Balkin: Retail investors and HNWIs will require more transparency and information from GPs to be effective investors in private markets. This is a shift from the way things have been done before, as larger institutional LPs often have the ability to interact with investment professionals at the GP, which will become increasingly difficult with a higher volume of investors.

Retail and HNWIs will rely on comprehensive information to make informed investment decisions. They need access to data regarding investment opportunities, potential risks, expected returns and the underlying fundamentals of private companies or assets. Without sufficient information, investors may be hesitant to commit capital to illiquid and opaque investments typical of the private markets.

RD: How has technology improved transparency in the investment landscape and how will it continue to do so?
Magnan: Technology will be instrumental in helping collect data efficiently and in high volumes. Until reporting for private companies is standardised – which may or may not happen – there will be a need to create consistency across data and a portfolio. This is where technology, and in particular AI, will help significantly by providing better and faster analysis to encourage prompt investment decisions.

Balkin: Technology has been a

I am a firm believer that AI has transformational potential in the alternative investments industry

Yann Magnan, 73 Strings

Retail investors and HNWIs are more likely to engage with investment opportunities when they perceive transparency

Jonathan Balkin, Lionpoint, an Alpha Group Company

critical foundation for GPs to improve transparency in the investment landscape. It has allowed firms to establish the 'facts' of the business via valid sources that can be reported to current and prospective LPs, regulatory agencies, investment teams and firm leadership. For GPs continuing their innovation journey, the ability to automate business processes that have historically been manual and performed 'offline' has been an important trend we have witnessed.

We're seeing technology-driven data analytics and artificial intelligence tools as a key area of exploration for the purposes of analysing large datasets to identify trends, patterns and anomalies, and to continue automating inefficient business processes. These tools can help investors assess the quality of financial information, detect outliers and make more informed investment decisions. AI-powered algorithms can also automate the analysis of banker investment memos, credit agreements, regulatory filings or market research reports, providing investors with valuable insights and enhancing transparency.

RD: What real-time data, market analysis and performance metrics should be accessible to retail investors and HNWIs?

Magnan: I believe that besides getting valuations for their investments, retail investors and HNWIs will need to be informed of how the business and financial instruments they have invested in are performing, both on their own and compared to their peers.

That means that GPs addressing retail investors' and HNWIs' interests must consistently collect and structure as many data points as possible to address these demands. This is something that 73 Strings have been focusing on for some time, and where we are seeing significant traction and growth.

Balkin: We have seen this become a focus area for GPs, as large institutional investors have become more sophisticated and the need for real-time data has expanded. Instead of a quarterly report that represents the previous state of the portfolio, that information is increasingly required to be up to date and readily available.

Whether it is the company financials, economic indicators, risk and exposure factors or benchmarking data showing peer funds' performance, the shift to establishing this as a mature capability will be required.

RD: How will technology streamline the investment process and how can semi-automated platforms, such as 73 Strings, assist GPs with portfolio management and valuation?

Magnan: Digital transformation is going to be a priority for most alternative asset managers. For example, at 73 Strings, our technology streamlines the entire valuation process of an alternative asset, equipping the GP with a technology that delivers valuations more efficiently and with greater consistency.

With largely automated auditing and reviewing capabilities, the third-party valuation providers and auditors who remain key to the process can derive their conclusions for GPs faster. The automated data collection technology that 73 Strings has developed is also a significant enabler in running an efficient process as it aids the collection, structuring and tracking of the relevant data points and their data sources.

Balkin: We see technology streamlining the investment process at all stages of its lifecycle, from the initial onboarding of investors and evaluation of investment opportunities to tracking dealflow in a pipeline management solution, to collecting financial data from portfolio companies and automating valuations. We have deployed 73 Strings' technology to GPs and the resulting efficiency gains around portfolio monitoring activities and valuations have been significant.

RD: How do advancements in emerging technologies shape the future of alternative investing?

Magnan: I am a firm believer that AI has transformational potential in the alternative industry. AI can help – and is already helping – to automate routine tasks, reporting and the structuring of data.

It is also worth considering that the alternative investment industry is technical and the development and training of relevant algorithms will require specific resources and specific competencies. Additionally, the security of data, how it is used and its availability must be managed with care.

Balkin: Alternative and private fund managers have historically employed largely manual and inefficient business processes that could suffice for a small investor base and relatively low volume of assets and transactions.

However, as volumes and competition increase, the opportunities to leverage technological innovations, such as AI, have become increasingly attractive.

We have seen an initial focus on the investment diligence process as investment professionals are often reviewing a high volume of investment opportunities, with data, reports and documents requiring time-intensive analysis.

AI has been able to accelerate that analysis through identification of key data from presentations and reports while correlating findings with market research data. Additionally, as a key challenge for GPs is collecting, organising and analysing financial data from portfolio companies, AI has been able to step in and automate the way in which data is ingested into platforms such as we've seen with 73 Strings. ●

Gilles Daguet tells *Real Deals* about the ambitions for Brienne IV

Tikehau Capital's newest vintage targets the growing digital security space

By *Silvia Iacovcich*

Gilles Daguet, head of private equity cybersecurity strategy at Tikehau Capital, recently spoke to *Real Deals* about the firm's Brienne IV fund, which held its first close on €200m in October 2023.

The final close is expected by the close of 2024 and, according to the GP, Brienne IV is set to be one of the largest vehicles dedicated to digital security in Europe. The firm has strong ambitions for the flagship fund, as it aims to double the size of its previous vintage – Brienne III – which closed on €175m.

Brienne IV has already made its first two investments. "The first is ChapsVision, a French company offering sovereign solutions dedicated to cyber intelligence and cybersecurity for the defence, intelligence and security markets," Daguet explains. The second is a €15m fundraising round for cybersecurity software company ProvenRun, which was led by Tikehau's new vintage of Brienne and unveiled in December 2023.

The vehicle has been supported by a diverse range of institutional and private investors, including corporate and family officers. "Fund IV has also partnered with the French Ministry of Defence and the National Cybersecurity Agency of France," adds Daguet.

"Our investors are interested in cybersecurity because it is becoming more common to read about cyberattacks in the news. Additionally, we bring to our strategic LPs a view on the dealflow of new technologies and new items in cybersecurity," Daguet explains.

Tikehau will be looking to attract interest from new international investors during the second phase, including family offices, corporations and institutions based in the Middle East and Canada.

Brienne IV focuses on European opportunities with a significant B2B and B2G scalability potential, investing in cybersecurity and digital trust as a broader sector. It is also open to potential reinvestments in companies committed to improving the cybersecurity landscape.

€200m

The vehicle's first close

€10-50m

Ticket size of new fund

€3-5m

ARR revenues of firms that the fund will target

The GP invests in firms that have revenues between €3m and €5m of ARR, as it does not want to be exposed to the technical risks with pre-seed or seed capital, Daguet explained. Its ticket size ranges from €10m to €50m.

The fund focuses on opportunities in Benelux, Switzerland, Germany, Italy, Spain and the UK, while also exploring deals in the US, Canada and Israel, Daguet confirmed.

"Europe is full of firms funded by engineers that are bringing new solutions within the cybersecurity space," he says. "In Europe, we now need to give companies the resources they need to become European cybersecurity champions."

Growing size

According to Dauget, launching a fund that was bigger than its predecessor Brienne III was a critical factor for the launch of Brienne IV.

The increased size means the fund can facilitate M&A strategies and accelerate growth, according to Daguet.

"We thought we needed a larger size, as we looked at series A and series B from the first investment in cybersecurity that we made in October 2019. Four years after the initial fundraising, the numbers were completely different: the series A four years ago was roughly €5m, and today it is between €15m and €20m," he says.

Cybersecurity evolution

The launch of this vintage reinforces the GP's commitment to investing in pioneering technology and fortifying digital security across the European business landscape, which is particularly vulnerable to the recent wave of cyber threats that are impacting companies across all sectors.

Cybersecurity represents a strong investment opportunity for Tikehau, with the sector maturing since the launch of its private equity cybersecurity strategy in 2019. Dauget explains that cybersecurity is a sector of interest due to its resilience and the growth of the markets.

"We launched the first fund dedicated to cybersecurity four years ago, as the sector represented a real opportunity in terms of investments, as well as being a top priority for our firm and investors," he says.

"In 2019, we wanted to dedicate a fund entirely to cybersecurity as the idea was new in Europe. [Cybersecurity] has already been explored in the US and Israel where there are currently the largest funds," he continues.

Within three years, Brienne III invested in 15 companies: 10 in France, two in Germany, one in the Netherlands, one in Belgium and one in Portugal.

"The fundraising was taken care of by our expert sales teams and then by following the usual process with the investment teams. There were no external players involved in this round," Daguet confirms. ●

> Our investors are interested in cybersecurity because it is becoming more common to read about cyberattacks in the news
>
> **Gilles Daguet**
> *Tikehau Capital*

The power of cyber risk intelligence in private equity

Proactive cyber risk management is essential to preserving value across the investment lifecycle, says chief executive and founder of KYND, *Andy Thomas*

RD: What does KYND do, and what value do you bring to private equity firms?
Andy Thomas: Firstly, it is important to note that we are not a cybersecurity business. We are cyber risk management experts. We do this on a non-penetration basis, essentially outward-looking in, so gaining cyber risk insights from KYND is simple and quick.

We began our journey by focusing on the insurance market back in 2018. Insurance companies at that time were starting to suffer significant losses associated with increased ransomware attacks, and we were able to help better inform their decision making around who they were willing to insure.

We see the risk of cyber losses concentrating in numerous industries and will continue to expand our industry footprint. Recently, we have been drawn into the private equity world, as private equity firms have begun facing the same issues as insurance companies five years ago. As cyberattacks continue to rise in frequency and sophistication, they want to understand the cyber risk profile of portfolio companies and target companies, as what was once a peripheral concern has become mainstream.

Cybersecurity is a very complex area and we see it as our role to ease that complexity for a non-specialist audience, enabling people to prioritise those risks directly connected to attacks, rather than worrying about every potential risk that exists.

RD: What role does cyber risk management play in the due diligence phase, in particular?
Thomas: There can be a significant degree of tech due diligence carried out on investments; firms that are really looking to get under the bonnet to see how things are done. A necessary component of that involves insight into cybersecurity governance within the business. Instant, easy-to-understand exposure visibility such as KYND's enables private equity firms to easily confirm external cyber risk profiles and internal cyber risk processes in a light-touch manner, as opposed to an expensive consultant-led due diligence exercise.

We provide tailored, focused reports that highlight priority issues that have been identified within the tech infrastructure of a business. We also explore the target company's internal processes and cyber maturity using a simple questionnaire that helps private equity firms quickly get to the nub of the matter. Again, thanks to the close cooperation with our insurance clients, we've learned a lot in terms of how they evaluate a company's internal and external cyber posture.

RD: How should private equity firms then integrate cyber risk management into the asset management or value creation phase?
Thomas: I recently had a conversation with a private equity firm that suffered a cyber incident almost immediately post-transaction, and it is important to be aware that this is one of the highest-risk periods in any investment. If a portfolio company suffers a disruptive cyberattack, it leads to increased expense, reputational damage and lost focus on meeting business objectives. The business is distracted by the acquisition process and so its exposure, post-deal, may be significant.

During due diligence, it's important for firms to prioritise actions for those early days after the deal is completed and then continually monitor the portfolio company thereafter to ensure they stay ahead of the dynamic cyber threat landscape. We enable both by allowing the private equity firm to quickly gain instant insight into the risk profile and risk maturity of each business, as well as help portfolio organisations to address existing and new vulnerabilities before cybercriminals exploit them.

This cooperation has proven successful as private equity firms do not want to become the IT department of their portfolio companies. Rather, they want to be able to monitor, support and nudge firms that appear in need of improvement because cyber incidents are undoubtedly a real disruption to any business.

In 2023, one of our global asset management clients published a whitepaper that revealed that cyber incidents have a material and lasting impact on opex, capex and SG&A costs. Being burdened with those increased costs for an extended period of time can have a significant impact on value. These are the tangible impacts of an incident, and don't even count the brand or reputational risk to impacted firms.

RD: How can you gauge the cybersecurity culture of a business and why is that so important?
Thomas: It matters because the more mature a company's cybersecurity culture is, the better positioned it will be to respond to any incident, and the more likely it will be to put everything in place to ensure that everyone connected to the business understands cyber risk exposure.

This could include having the right cyber training in place to ensure cyber risk is front of mind for everyone in the business, such as simulated phishing exercises and sensitivity to data security and confidentiality. That culture has to permeate the entire company and safe behaviour has to be infused into corporate culture. It is no longer sufficient for only senior management to be aware of the risks.

We find that one of the best indicators of a company's cyber culture can be seen in how they respond when we tell them that they are exposed to a critical vulnerability in their infrastructure. If a company recognises the benefits of having more good-guy-eyes on the business in order to spot vulnerabilities that the bad guys could exploit, that is generally a good sign. Conversely, if an organisation cannot be contacted, or is resistant to what we have to tell them, that is typically a sign of a poor cybersecurity culture and a lack of cyber maturity.

In addition, with an ever-changing attack surface, new

While the cyber risk profile of a company may not directly and immediately impact its value, it will certainly impact the ease of sale

Andy Thomas, KYND

vulnerabilities arise constantly; therefore continuous risk monitoring of portfolio companies has now become integral for private equity portfolio management processes.

Obtaining ongoing visibility into organisations' risk profiles not only enables them to proactively oversee digital risk across portfolios but also fosters engagement with the organisations, as witnessed by our clients.

RD: How can private equity firms support their portfolio companies when it comes to accessing cyber insurance?
Thomas: In a digital-first and interconnected era, cyber insurance is no longer a luxury, but a vital component of an effective cyber risk management programme for businesses of all types and sizes. But obtaining and keeping this much-needed coverage is not that simple.

With our background, we understand what insurers are looking to focus on, and therefore the cybersecurity standards that private equity firms have to ensure are in place within their portfolio companies for them to be insurable. We are able to assist with that process, helping businesses ensure they can access the right insurance at the right cost.

RD: How important is cyber risk management to the exit process?
Thomas: While the cyber risk profile of a company may not directly and immediately impact its value, it will certainly impact the ease of sale. The cyber risk landscape is ever-evolving, and organisations must continually adapt to it to avoid reputational, financial, or legal repercussions.

When we are monitoring portfolio companies on a continual basis, we produce a set of reports that are designed for the board of that business, which show how the risk profile of an organisation has evolved over time and how it compares to its peers.

When it comes to preparing a company for exit, these same reports can be used to demonstrate the cyber resilience of the business to prospective buyers, complementing their due diligence efforts. Maintaining a close eye on cyber readiness can also help to resolve any major issues that could threaten to undermine the exit process. If a company suffers an incident the week before closing a deal, that could derail the transaction. Heightened risk awareness during these key periods can be extremely valuable.

RD: How is the regulatory environment evolving when it comes to cybersecurity and how do firms need to respond?
Thomas: The Digital Operational Resilience Act, or DORA, in the EU, will have implications for private equity firms. It is not entirely clear what form that impact will take as of yet, but the consensus is that private equity firms will need to evidence that they have active oversight of the cybersecurity and risk posture of the businesses they invest in, and that they are doing everything they can be reasonably expected to do in order to protect their investors' money.

It certainly seems as though this will be the minimum required from this regulation, and having active cyber risk governance and monitoring of portfolio companies in place would therefore be a major plus.

RD: How should firms approach resourcing their cyber risk management function as a firm, and within portfolio companies, including through partnerships with experts?
Thomas: No private equity firm wants to step in and take over the cybersecurity function from a portfolio company's own IT team. They simply do not have the bandwidth. I would also add that none of the private equity clients that we speak with would be willing to instruct their portfolio companies to install software within their networks.

Instead, the ethos seems to be 'trust but verify'. You must trust your portfolio companies to do what is right and what they say they will do, but then monitor to make sure that that is the case.

Equally, portfolio companies are likely to have their own existing relationships with experts and it is neither the job of the private equity firm, or us at KYND, to replace those relationships. Instead, we are here to provide guidance and monitoring, helping those businesses prioritise and aiding them in using the resources and expertise that they already have at their disposal wisely.

We do not identify issues and then offer to fix them. That is not our business model. We provide insights that IT departments and their services providers can use to quickly identify issues that we have flagged, enabling them to ultimately fix them themselves and become more resilient.

Data wave

Demanding LPs and AI advancements have moved the dial on data. But what does a data strategy during a holding period look like? *Xhulio Ismalaj* reports

With a challenging exit environment, GPs are having to hold onto portfolio companies for longer. As such, there is even greater tenacity needed to squeeze value out of investments.

The role of data is central to all of this, with many GPs deploying data workstreams as part of their value creation toolbox. Further, with advancements in LLMs and more broadly with AI, there is an increasing focus on data quality.

Accurate data at a granular level helps GPs report to their LPs, getting beyond the portco's P&L statement and finance team. Vera Huang, UK sales director of data services at fund administrator IQ-EQ, says: "LPs are increasingly coming to GPs with more ad hoc requests, becoming more and more demanding, in a good way, for better transparency, to find out how GPs are creating value, how portfolio companies are doing and have been performing over time."

While financial and commercial metrics are usually the place to begin for tracking value creation, many are now looking at non-financial metrics.

"A couple of such metrics that have gained popularity over the years would be net promoter score to track how likely your clients are going to recommend your product, or annual contract values, which is more prominent in the SaaS industry," says Huang.

Of course, with a growing emphasis on ESG and the energy transition, GPs are increasingly asking for ESG metrics to be tracked too.

Business transformation

The first step in a portco's data journey starts with a high-level value creation plan, says Marco Ferrara, operating partner at Limerston Capital, a UK investor targeting businesses valued between £20m and £200m.

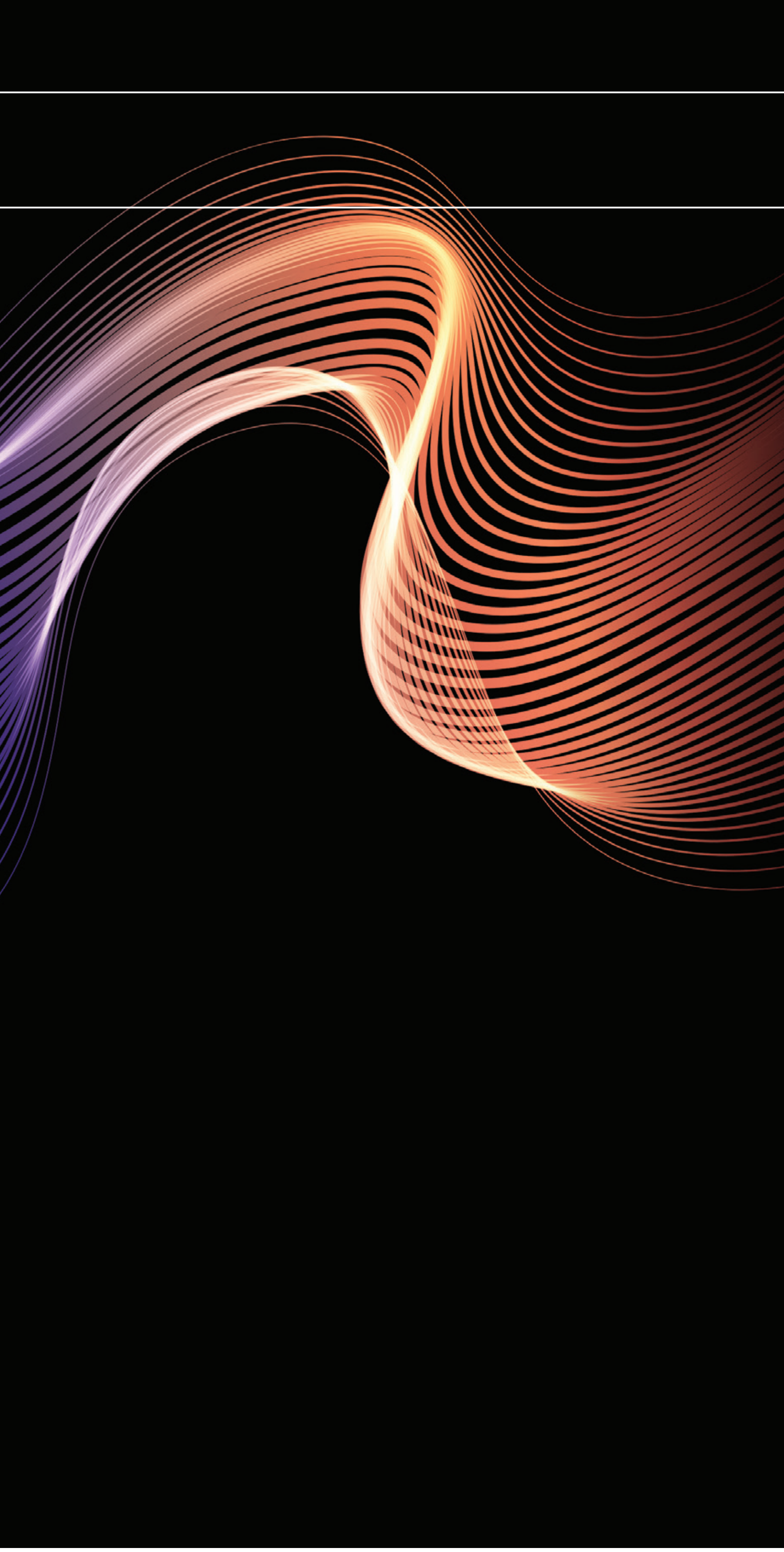
Then it's about identifying the KPIs throughout the different layers of the business needed to hit the high-level value creation objectives, and translating them into data points. Limerston's Ferrera likes using the objectives and key results framework to cascade the business's key priorities throughout the organisation.

"It aligns everyone in the company on what the key results that the business needs to deliver are," he says. "If management makes those critical KPIs that you need to hit as a business clear to everyone, and there's a clear understanding of how each layer in the organisation will contribute to delivering those KPIs, then every employee knows what they need to do to deliver success."

To give the investor a sense of the quality and robustness of a company's data pre-acquisition, Limerston identifies whether there is a single source of truth that exists for any given data point in the organisation.

Ferrera elaborates: "Some of the key things we'll test in DD are whether responses to queries that we'd expect to come from a single system come back in

> Often, things like one-off pricing or discounts might not be held in your finance system; they might be added manually or held in a separate piece of code
>
> **Marco Ferrara**
> *Limerston Capital*



> Automation means that sponsors and the portfolio companies can then focus their time on value-creating tasks rather than populating Excel templates
>
> **Vera Huang**
> *IQ-EQ*

a timely fashion and are consistently formatted across multiple data requests. We ask for the same datasets to be sliced in different ways, and we run checks for inconsistencies across datasets that should reconcile."

Of course, there is potential for conflicting information in different systems. "We test this in DD by looking at customer-level pricing and cost data. Often, things like one-off pricing or discounts might not be held in your finance system; they might be added manually or held in a separate piece of code," the Limerston operating partner notes.

"That then helps us understand that you've got issues with either the processes through which you're capturing your data, or in the integrations between the different systems as the information isn't being effectively sent from one to the other. Sometimes you might have both issues, so you might have people keying information in two different systems or capturing information in two different systems, and then there isn't an immediate reconciliation mechanism to make sure that you're cleaning that data at the outset."

Automation enabler

Many sound, profitable midmarket businesses do not have a data infrastructure, let alone dashboards. Some, even, still use paper, while many use spreadsheets, which can be labour-intensive and subject to mistakes.

Excel is still being used to collect data, despite being one of the least mature ways of doing so. For example, a GP would request its portfolio companies to submit data in a predefined Excel template to be sent over email or a portal, before manipulating it further or keying it into another system.

However, as GPs launch more funds and invest in more companies, Excel becomes an ineffective way of gathering information, as it is difficult for all that data to be taken from Excel and put into a more centralised place so that GPs can provide reporting, both for management and their LPs.

IQ-EQ's Huang says: "Nowadays, for a PE sponsor to be able to look at how much value a company has created over time, they need to have some sort of technology that allows the portfolio companies to track those metrics. We do see that more and more sponsors are looking at using tools and portals to interface directly with a portfolio company, or working with service providers to help them with that."

For instance, a GP will set up a data request in the portfolio, for which a portco's CFO logs onto the portal every quarter to submit the data. The use of technologies to streamline the data collection process is, naturally, considered a more mature way to operate.

"The less manual intervention, the better. The more automated, the better," says Huang.

"Because it means that the sponsors and the portfolio companies can then focus their time on value-creating tasks rather than populating Excel templates. They don't want to be doing the very mundane and boring tasks of collecting data; they want to be doing data analysis, instead of collecting data, so the more we can automate that away, the better," she adds.

Consistent approach

On tools, Limerston chose the Microsoft path and standardised it across all its portfolio companies.

"We use the same infrastructure approach and productivity tools as much as we can, and the same data capture and then data representation in terms of management information tools across all of our portfolio companies, which helps us get a consistent view of what's happening across companies in different sectors and of different sizes," says Ferrera.

Altogether, when considering business value, it is important that PE players start with the 'what' first instead of running to the 'how'. For example, what is the value of a GP giving a portco a dashboard, system or ML model?

Can it give more flexibility on pricing? Can it give opportunities to understand the best performance across sales teams in different jurisdictions to assess the organisational structure? If the answer is yes, how much money can they make from it, or lose from not having it?

Data platforms, it seems, should not be built for their own sake but rather with an understanding of the business context. ●

A customised approach

Kim Carter from LKCM Headwater and Passthrough's *Ben Doran* explain how collaboration is key for a successful partnership

Since its first partnership more than two decades ago, the team at Texas-based private equity firm LKCM Headwater has understood that businesses do not make businesses better, people do.

Fast forward to 2024, the firm has raised six partnerships plus co-investment partnerships totaling $2.6bn of capital commitments. LKCM Headwater's core philosophy is to add value through the expertise of its ecosystem of hands-on, strategic investors to transform businesses to be more sustainable, higher cashflowing, and more resilient over the long term. To do so, building strong relationships with their investors is critical.

"Our focus is alignment and partnering with portfolio company management teams to provide relationships, resources and capital to scale and build businesses that best serve our customers," says Kim Carter, partner and CFO at LKCM Headwater. "Our limited partners are very engaged in our efforts. They source new opportunities, sit on boards, serve as operating partners, and bring expertise from having operated and built their own business. I can pick up the phone and call our limited partners with relevant domain expertise to work with our team to help unlock value across our businesses."

Customised approach

Introduced by a limited partner, Passthrough provided a customised approach to LKCM Headwater that allowed the firm to scale the fundraising process for its lean team and simplify it for the LPs. Carter wanted a solution that meant she could expand the firm's fundraising efforts without relying on more people doing more manual work.

"What Passthrough unlocked for us in digitalising our onboarding process parallels what we do with our operating companies," says Carter. "We look for businesses where we believe we have a competitive edge and can create more value. Bryan King, the founding LKCM Headwater partner, believes in an operational, roll-up-your-sleeves approach that often requires an investment in technology, software and systems. This creates a J-curve to get operating leverage to create a step-change to a more profitable, scalable business."

Continuing to tailor the onboarding process through individualised messaging and customised ways of sharing information was key for LKCM Headwater to maintain and build connections with investors. The Passthrough team had the same collaborative approach and was quick to test and implement changes that allowed LKCM Headwater to best serve its clients.

Carter attributes a significant part of the ease and success of their raise to the Passthrough team.

KEY FACTS

As of early 2024, LKCM Headwater Investments has $26.3bn AUM, a team of 99 including 66 investment and other professionals, 27 CFAs, eight CPAs, four CFPs and 35 employees with MBAs, and is independently owned and operated by its employees.

It has over $2.6bn invested in more than 40 platform companies and has generated 5.7x MOIC from its exited investments since 2000.

What Passthrough unlocked for us in digitalising our onboarding process parallels what we do with our operating companies

Kim Carter, LKCM Headwater

"We always want to understand how customers are using the platform in order to make it even more useful for them

Ben Doran, Passthrough

"There was always a response back from the team saying, 'Yes, we can do this,' or 'We've seen this before. While you are suggesting this, I would also recommend you consider options A, B and C.'"

Constantly improving

Ben Doran, co-founder and COO at Passthrough, says feedback from customers such as LKCM is a crucial part of constantly improving the product. "We always want to understand how customers are using the platform in order to make it even more useful for them," he says. "By getting a real-time look into how Kim and her team wanted to work with their investors, we know exactly what we needed to build to get them there, which means the next customer gets that benefit too."

Security was also a critical factor during the diligence process led by Sarah Topham and the IT team at LKCM. "We needed to give our limited partners the confidence their data is protected," Carter says. "Passthrough provides a way to log in with a secure link without having to maintain passwords that could be hacked. This was one of the benefits that our IT and security teams identified when they did their diligence, and one that our limited partners really appreciated. We collect and store very sensitive data, so having confidence that Passthrough took security and privacy seriously was imperative."

Ultimately, the success of implementing any investor-facing solution comes down to what the LKCM Headwater limited partners think of it.

"Our limited partners were impressed," says Carter. "Passthrough simplified and made the process easier for them. The ability to start and stop filling their sub-documents as they needed, having all their information saved and sharing their documents with additional family members, CPAs or additional users on a single platform was something most of them had not seen before. It put control in their hands in a way that even those who were less tech savvy could easily benefit."

IN ASSOCIATION WITH

Passthrough

COMMENT

Technology's sustainability challenge

It is time to embrace the opportunities that come with the technology industry's shortcomings, according to *Bettina Denis*, head of sustainability at Revaia

The technology industry during the past decade has been a key factor in reshaping both the society and economy of Europe. The sector has created nine million tech jobs and generated $800bn (€740bn), revolutionising sectors such as education and healthcare.

Projections suggest demand for an additional 11 million tech specialists by 2030. The industry is rapidly innovating and has the potential to lead the charge towards sustainability. By embracing sustainable principles, it can demonstrate the intertwined nature of sustainability and financial performance.

Despite these expectations, there are issues that need addressing. Notably, the diversity of the technology industry requires attention and, on the environmental front, its carbon emissions could triple by 2050 without intervention.

Facing challenges

In the tech world, carbon footprint assessment is the most prioritised sustainable initiative, with 59% of seed to series-D and beyond having completed a carbon footprint analysis – a positive step. Equally positive is that the further down the maturity scale we look, where the larger companies with higher carbon emissions sit, the higher this%age rises, reaching 87% in series-D+ companies.

However, all is not rosy, as tech companies seem to overlook significant Scope 3 emissions, one of the highest contributors to carbon footprint. Scope 3 emissions account for all indirect emissions in a company's value chain, including both upstream and downstream activities, and notably procurement. Currently, just over a third (36%) of companies have implemented a responsible procurement charter.

Diversity is an area of concern – especially female representation. As it stands, just 26% of the tech workforce is female. As companies mature, there is also a risk of losing focus on ESG actions from previous financing rounds. Between seed and series-D, female representation at the board level has been shown to decrease from 37% to 27%.

Diversity charters often sit below environmental desires, but it is vitally important that we consider both to the same significance.

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Bettina Denis, Revaia

Turning the dial

However, there are reasons for optimism. Tech companies are beginning to understand their ESG responsibilities, and investors are beginning to take sustainability seriously. In 2021, $18.2bn was invested in European startups pursuing environmentally aligned business models.

VC firms are beginning to see that sustainability has to be ingrained in everything they do, and all investments must adhere to ESG rules, or they quickly see investors putting money elsewhere. In a challenging fundraising environment, this is the last thing that GPs need.

We are seeing an increasing trend of VCs, in the due diligence phase of investment, ensuring that companies have defined measurable social and environmental indicators, which can be followed in the long term. These KPIs can relate to business practices such as transparency, employee retention and work policies, as well as the company's business model such as education, partnerships and employment.

This, alongside the appointment of an ESG leader, which has proven to help increase diversity from 38% to 46% according to our latest ESG Benchmark Survey, means that companies can have a clear roadmap and in-house toolbox, improving sustainability performance and ensuring that the tech industry becomes the driving force towards a more sustainable future.

Note: All data referenced is from Revaia's 2023 Tech ESG Benchmark Survey

ESG considerations are here to stay

Dasseti's *Billy Cotter* and *Evan Crowley* discuss the most talked-about acronym in the private equity industry

ESG is one of the most talked-about three letter acronyms in private equity. Putting its status as the industry's buzzword aside, ESG due diligence has been born out of risk management and should be considered along with other operational, liquidity or capital risks.

Here, due diligence software provider Dasseti explores the key reasons why ESG should always be front of mind for investors and managers alike.

A GP STORY

Evan Crowley outlines how one GP in the US is using technology to address ESG data collection and reporting challenges.

"We have been working with a GP that is a leader in sustainable investment within the energy sector. Around 18 months ago, the GP was facing the dual challenges of manual ESG data collection and stringent regulatory demands, and embarked on a journey to transform its ESG reporting and data management processes.

"We offered a solution that streamlined data collection through customisable questionnaires but also enhanced the user experience for portfolio companies – driving up response rates and subsequently improving the data quality."

Takeaway: Since most GPs are starting from different places in their ESG data journey, operate across different sectors and have completely different reporting requirements, flexibility is the number one priority when looking for solutions to support GPs' ESG data collection and management efforts.

ESG metrics are routinely requested

LPs and GPs are taking ESG factors seriously in 2024. ESG metrics are not just something that concerns SFDR Article 8 or 9 funds – almost every GP is now being asked to provide metrics not only around their own operations but for portfolio companies too.

Dasseti has recorded a 10 times increase in the number of ESG-related questionnaires being distributed from its global LP base in the past 18 months.

There has also been increased demand from LPs for a solution that can see right through the GP, to the funds and entities or portfolio companies beyond.

What is driving demand for ESG data?

The factors driving the demand for ESG data vary, with many LPs integrating sustainability into their investment approach to manage both risks and drive value.

Dasseti's head of ESG, Billy Cotter, says: "Even as ESG regulations are nascent in some regions, anticipated regulatory pressures feature highly. Many LPs and fund-of-funds want to get ahead of the curve and start collecting baseline data that they can use when the regulatory need arises. This is then passed along to the GPs, who need to collect the data from their portcos."

How does technology stack up?

There has been a significant increase in the number of managed and consultancy services in the ESG and sustainability space in the past few years. ESG and sustainability research firm Verdantix forecasts that the ESG consultancy market will reach $48bn (€44bn) worldwide by 2028.

However, the manual data collection burden involved in providing ESG consultancy services can be significant, often resulting in overinflated price points for less than optimal service levels.

Technology is at the intersection of private equity and ESG and can be transformational for the whole sector, including ESG managed service and consultancy firms.

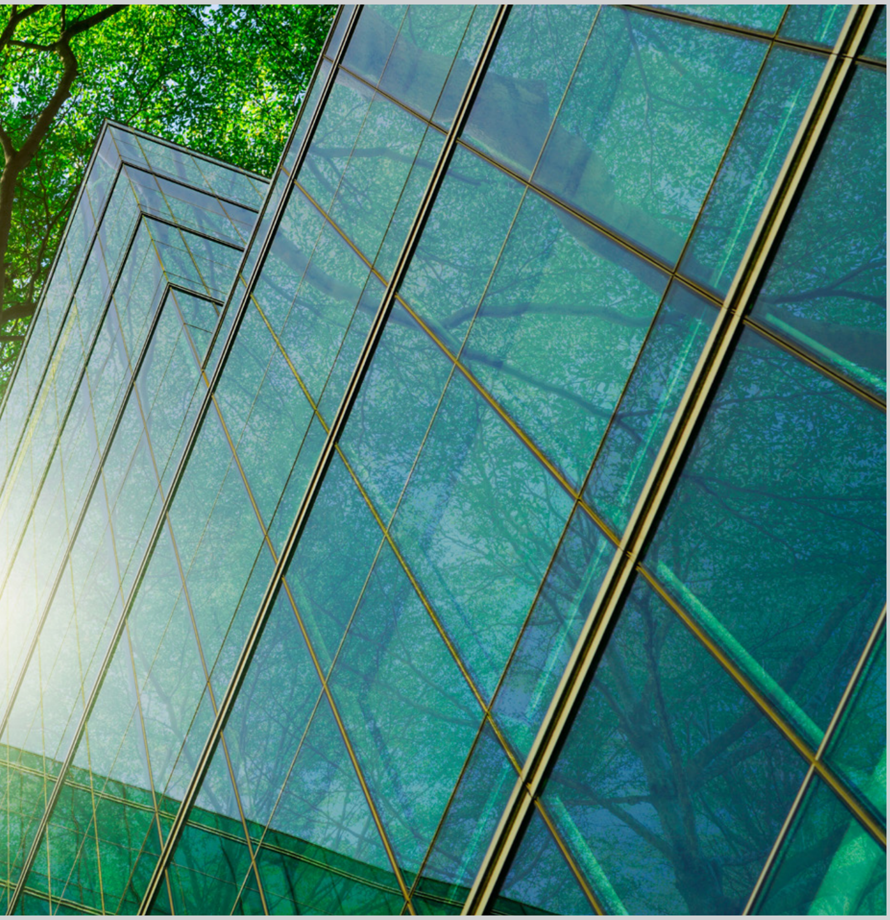
There is a wide range of tools and systems that can enhance the collection, aggregation, management and reporting of ESG data and metrics, often at a manageable cost. When assessing the technology platforms required, firms across the private equity sector should look for the following capabilities:

1. Data collection and aggregation

By automating the collection of ESG metrics, firms can minimise manual entry errors and enhance accuracy. Centralised data platforms often allow the aggregation of data from diverse sources and provide a holistic view of ESG metrics across portfolios.

"Even as ESG regulations are nascent in some regions, anticipated regulatory pressures feature highly

Billy Cotter, Dasseti



2. Data quality and standardisation
In-built data validation tools can improve the accuracy and completeness of ESG data.

By standardising incoming data to align with increasingly popular industry specific reporting frameworks such as the ESG Data Convergence Initiative or Sustainable Finance Disclosure Regulation, it becomes much easier to benchmark performance and comply with regulatory requirements.

However, collecting and aggregating first-party data directly from the source means firms are future-proofed if reporting frameworks or regulations change, or if stakeholders start to coalesce around a different pillar of metrics.

Evan Crowley, senior product specialist at Dasseti, says: "We have seen this happen with climate-related disclosures, which are now pretty much standard for the industry, but also more recently have started to see moves to collect more supply chain data. It is important to have the flexibility in a tech solution to be able to respond to those changing requirements quickly and easily."

3. Data analysis and reporting
In its 2023 global market size and forecast report, Verdantix projected that financial services firms will significantly increase spend on ESG reporting and data management software, growing at a CAGR of 32% to reach $470m in 2027.

Advanced analytics capabilities provided by some ESG platforms allow for deep insights, identifying trends and assessing the impact of investments. Reporting that meets the specific needs of stakeholders, including regulatory bodies and investors, is in hot demand.

4. Benchmarking and performance tracking
For many LPs and fund-of-funds, tracking impact over time is a core driver for collecting and analysing ESG metrics. Software tools that provide benchmarking to compare performance against industry peers or indices, or time series data to allow continuous monitoring of ESG goals, are crucial.

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It is important to have the flexibility in a tech solution to be able to respond to changing requirements quickly and easily

Evan Crowley, Dasseti

A PE FUND-OF-FUNDS STORY

Dasetti's Billy Cotter discusses the challenges facing a large private equity fund of funds business in Europe.

"This firm's ESG team was looking for a solution to manage its ESG data collection and reporting challenges. It operates funds that are regulated under the SFDR, with a requirement to report on fund-level indicators, including Mandatory Principal Adverse Impacts (PAIs) and Optional Key Sustainability Indicators (KSIs), deriving data from their portfolio companies and funds.

"They also need to gather sector-specific impact KPIs from companies within their Article 9 funds for internal sustainability reporting. All data must be fed into their internal platform via API in a standardised format, requiring multiple testing phases for final approval. Additionally, fund-of-funds must now collect asset-level data from external GPs to validate fund-level data, which is an industry-wide requirement.

"The teams were grappling with varying fund-level metrics and needed a customised approach to data collection. There is no one-size-fits-all questionnaire, and data must be tailored to the specific fund holding the issuer. The firm found that some issuers were not providing data at all, largely due to the lack of direct engagement and overly broad questionnaires.

"Dasseti presented a tech-enabled solution that would garner better engagement and direct data collection, which capitalised on strong existing relationships with issuers. The proactive engagement with issuers and customised approach to data collection have been well received."

Takeaway: Fund-of-funds and LPs have similar challenges in meeting reported KPIs and managing significant amounts of data, which can quickly become complex and cumbersome. A solution that can extract and aggregate data at multiple levels has proven to be invaluable when scalability and granularity are high on the requirements list.

Transforming portfolio monitoring and ops with tech

Establishing a centralised point of contact and a single source of truth is critical for portfolio monitoring and reporting, says *Pratap Narayan Singh*, senior director and head of private markets at Acuity Knowledge Partners

RD: What is your view of the current portfolio monitoring and reporting landscape across the private markets industry?
Pratap Narayan Singh: In our latest private markets study, we discovered that private equity and venture capital firms are spending about one-fifth of their time on portfolio monitoring. Portfolio monitoring is an essential component of overall fund operations, driven largely by demanding investors.

The level of tech sophistication employed by private equity firms varies significantly. About a quarter of firms are using third-party tools, while another 25% have developed tools in-house. The remainder continue to rely on Excel spreadsheets.

Many not-so-tech-savvy firms are devoting an increasing amount of time to portfolio monitoring and reporting instead of their core competencies – deal origination, due diligence and value creation. There is, therefore, a clear need for technology to promote efficiency. But technology adoption in this space is a work in progress.

There are a multitude of challenges tied to data, as well as reluctance on the part of internal stakeholders. In addition, PE and VC firms face increasing complexity in the deployment of tools. To illustrate this, more than 75% of respondents to our 2024 private markets study, spread across regions and designations, stated they use multiple tools and systems in their operations. More than 70% would welcome a one-system tool to streamline operations, as complex and disjointed systems, in their view, brought inefficiency.

RD: What is likely to drive greater tech adoption going forward?
Singh: There is increased pressure from investors and regulators when it comes to portfolio monitoring. The new private fund adviser rules adopted by the SEC in August 2023 mandate greater transparency with respect to audit and reporting. There is a clear understanding that as private markets continue to grow exponentially, there will be greater scrutiny and expectations on accounting practices.

Technology has an important role to play in helping private market firms remain compliant with regulations, particularly as their operations become more complex. Firms are increasingly dealing with multiple assets, spanning private equity, growth capital, private credit, real estate and infrastructure. A firm investing in hundreds of companies across several investment strategies will likely find it extremely challenging to manually monitor everything. The spreadsheet-based model will fall short of expectations of all stakeholders across fund reporting and monitoring.

RD: What are the bottlenecks or challenges that private equity firms face when it comes to embracing technology?
Singh: One of the biggest challenges preventing private market firms from embracing tech solutions is diverse preferences of teams and individuals, making it difficult from a change management perspective.

Everyone prefers their own systems, which can lead to a lack of cohesion across an organisation. In our survey, 86% respondents stated that their organisation uses multiple software or tools. In addition to the challenge surrounding the deployment of different data management methods by diverse teams, there may be reluctance, in general, to adopt new technologies.

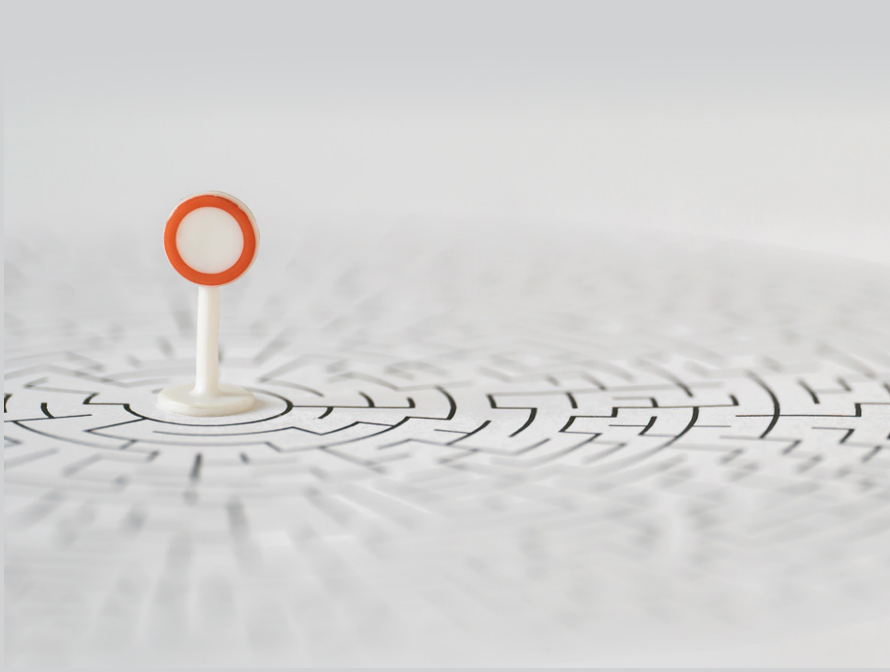
Furthermore, investment teams may be rigid in their choice of data management techniques, involving bespoke spreadsheets, making it hard to convince them about a better alternative.

There is also a lack of not only collaboration among leadership but also consensus on technology initiatives. Often the IT department pushes for investments in technology, suggesting the purchase of a third-party tool or the development of an in-house tool. But there is not necessarily enough focus on ensuring that the tool works for those who will use it across asset classes.

Finally, choosing the right technology or product can be a big challenge, given that the market is flooded with portfolio monitoring products that claim to do it all. However, many third-party technology platforms are off-the-shelf solutions, while every private equity firm is unique. It is critical to ensure the best requirements-to-product fit, because if you make the wrong choice, you may spend two to three years on implementation and maintenance before realising that you need to pivot to new software.

Moreover, constant data updates and validation for accuracy can be critical to the success of the technology/software implemented. In the past, firms have made material and long-term investments in multi-asset-class systems that they abandoned later, primarily because they failed to update data regularly. Given the challenges inherent in multiple systems, it is no surprise that 70% of respondents are open to adopting an integrated one-system tool.

One of the biggest challenges that private equity firms face is integrating multiple tools such as CRM, accounting, monitoring, reporting and ESG tools. How can managers integrate different data points to provide a single window of truth for both LPs and GPs?



It comes back to the practice whereby teams within private equity firms – such as accounting and administration, and portfolio monitoring – have historically followed their individual preferences driven by asset classes. You can find four to five data systems being used by different teams, which of course means there is no single source of truth. As a result, the lack of data management and coordination are the primary reasons for dissonance on existing systems as per half the respondents in the survey, followed by the preference for manual efforts, which multiply with multiple processes, compounding the challenges.

Data needs to be consistent, starting with CRM systems, and then linked to investment systems, portfolio monitoring, accounting and reporting, including external reporting tools being used. But this is rarely the case. To get there, you need to either develop a single centralised system or create a bespoke system, connecting the systems with APIs or other technologies, while ensuring a single, centralised point of contact.

We serve as that centralised point of contact for private equity firms implementing new portfolio monitoring technologies. We can either collaborate with third parties (such as iLevel) or deploy our in-house product – FolioSure. Our technology team then works with the accounting and administration teams to install APIs so that all reporting originates from a central source, not a myriad of systems.

We term such initiatives as 'data transformation projects' – a process that many private equity firms are going through. Some have already made great strides on this journey. Others continue to struggle to create a centralised, single source of truth for the entire firm that can form the basis of both internal and external reporting.

RD: What is your opinion on generative AI adoption in private markets and what areas are particularly ripe for disruption?
Singh: Private equity firms are starting to cautiously adopt generative AI solutions. Most are using them to explore ways to improve efficiency in portfolio companies, while a few seek to drive value across the investment lifecycle. However, GenAI comes with a set of challenges that need to be addressed by experienced technology and information security professionals to successfully embrace and unlock the potential of this technology.

In portfolio monitoring, the first step involves the collection of validation data, which is then fed into a portfolio monitoring system. Extracting this data from board packs, reports and Excel-based models is time-consuming and complex, but AI can deliver significant efficiencies. Once the data is in place, analytics can be applied to support portfolio performance benchmarking, enabling firms to generate insights based on AI that they can incorporate into their decision-making.

RD: There is a perception that technology adoption takes time to deliver real benefits. What is a realistic timeline when it comes to successful implementations that deliver positive outcomes?
Singh: Innovation, whether it involves AI or other types of technology, will realistically take two to three years to reap rewards. Consider a global private markets asset manager looking to customise existing technology, which it uses in one asset class, for a different asset class. First, the firm will need to work with internal teams to decide how to access the fund and portfolio company data needed to glean the desired insights. Then, it will take at least a year to bed in the product, adapting it to meet individual preferences.

It is important to remember that technology adoption is a journey; it is not something that is ever complete, given the constant emergence of new disruptive technologies and the need for regular software upgrades. For example, generative AI has gained significant traction during the past 18 months but there is no clear path to implementation – it is a work in progress.

Investing in technology and engaging with strategic partners is key to managing the increasing expectations of investors and regulators

Pratap Narayan Singh, Acuity Knowledge Partners

Thus, it is important to stay updated with the latest technology available and keep exploring data transformation projects while continually keeping a tab on the quality of data and expected output. Constant tweaks and course corrections are required to reach a level of consistency and efficiency that can eventually have a tangible impact on your bottom line.

RD: What is the latest trend in portfolio monitoring and the technology that supports it?
Singh: Increasingly, portfolio monitoring will also factor in the incorporation of ESG metrics. As per the survey mentioned above, only one-third of respondents suggested that they had mature ESG policies. The incidence of portfolio tracking is rising – three years ago, companies were in kick-off mode to track the ESG parameters of their portfolio companies.

About 7% and 10% of firms were tracking 10-20% and 21-30% of their portfolio, respectively, in 2023. The share has now moved northwards to 16% and 13%, respectively. Considerable work needs to be done in this area around data collection; but in a very short time, the ability to sell assets and the ability to raise funds will be contingent on getting this right.

To meet all the requirements surrounding LP scrutiny and new levels of regulatory oversight, it is critical that private equity firms establish a centralised point of contact and a single source of truth across teams and investment strategies.

It is paramount to do so now because the stakes have never been higher. Firms are already being hit with multimillion-dollar fines for failure to comply with regulations, which are only becoming more stringent. The professionals in the sector are very well aware of this – in all three editions of our survey, more than 90% of respondents believed regulations would become more stringent.

We believe investing in technology and engaging with strategic partners is key to managing the increasing expectations of investors and regulators. ●

TUNE IN

Tick Tock: Time to tokenise?

Tune into the latest podcast from *The Drawdown* to find out more about how technology can be used in private markets

CLICK ON THE QR CODE BELOW TO LISTEN

Real Deals' sister title *The Drawdown* was recently joined by a panel of tokenisation experts to discuss how the technology can be used in private markets.

The experts were: Jack Chong, an entrepreneur in residence at White Star Capital; Steven Lightstone, a regulatory partner in the investment management team at Morgan Lewis; and Myles Milston from Globacap, a fintech company he co-founded in 2017.

Tune in to the *Private Equity Talks* podcast to find out more about what tokenisation is and how it can be used in the field of private markets.

In this exclusive podcast, *The Drawdown* tackles the regulatory and operational barriers, and shares tips on how to overcome them. ●

The *Private Equity Talks* series is available on Apple and Spotify

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