RBC I&TS tracks trends in private equity investing

Mickael Fischer, Director of Client Coverage at RBC Investor & Treasury Services (RBC I&TS), talked to **Amélie Labbé,** Managing Director at Global Investor/ISF in an exclusive interview about how technology is reshaping private equity, investing and operations.

"We wear a double hat - one is business development and the second is relationship management," Fischer says.

His team covers the alternative investment fund manager space, and his portfolio is based on European, North American and a bit of Asian asset managers, focusing on real estate, private equity, infrastructure and private debt. Fischer has been with RBC for almost 16 years.

Could you share with our audience some of the specific areas within the tech space that private equity firms have been interested in investing in? How has this translated in terms of deal flow and deal value over the past few years?

Fischer reflects to a decade ago when some experts were predicting that software and technology would become the dominant sector. Those predictions have materialised, to some extent, with examples such as Amazon, Booking.com, Uber, Airbnb, Facebook, Netflix, even Tinder having disrupted our everyday life.

"Smartphones, online references sites and encyclopaedias did the same with our access to technology," he says. "Again, if you think about corporates today, I think it will be very difficult for somebody to go into the office and be able to work without using some of the leading software companies like Microsoft, Cisco, Salesforce, Zoom or SAP Concur."

"Without these, I don't think we would be able to spend a day efficiently at work. Technology changes the way we are, we live and work."

Moving the focus towards the investment areas, Fischer says there is no clear market when it comes to technology investment but comes up with 10 main themes. The first one is AI (artificial intelligence), the second is blockchain, followed by cloud, cybersecurity, Internet of Things, Metaverse, robotics, self-driving, software, and 3D printing.

"If we look at some of the studies published in the market, there was a very good one from Bain & Company in March 2022 which showcased that private equity-led technology deals totalled US$284 billion in 2021, corresponding to 25% of total buyout value and 31% of deal count, making it the biggest sector in the industry's overall portfolio," he says. "Technology is a key investment theme. If you deep dive into technology, out of the 10 sectors I mentioned before, the dominant one is software. Some US$256 billion out of the US$284 billion private equity-led technology investments I just mentioned was for software alone - 90% of the investments."

"If you look at it from an asset manager standpoint, I think there is growing interest - many asset managers are looking to get a technology fund," says Fischer. "If we are talking about specialised asset managers like Thoma Bravo, Vista Equity, Silver Lake, or even the multi-sector ones like Blackstone, Bain, KKR or the Rothschilds of this world, everybody has had a technology fund over the past five years."

There has been a clear push from the market to go into technology investment.

Why are those sectors of specific interest to private equity managers - what challenges or questions do they tackle in practice?

Fischer believes that private equity (PE) asset managers want to "go back to basics". He says that money and

returns are what PE asset managers are looking for.

"If they're able to find the so-called 2.5x multiples, this is an area where they will invest in. I think software investment has been good in that sense," he says. "Disruption is key here. If you are investing in a disruptive company, a company which can modify people's habits or behaviours and is widely accepted, you will have potentially great returns - again 2.5x or greater - which is why PE asset manager houses have focused on technology."

"Another example is Tesla. When Elon Musk initially entered the relationship and became a shareholder, he only put $6.5 million on the table back in 2004. The Tesla shares were introduced in June 2010, at $17, with a peak at $300 this year. Now, of course, we can say 2022 was a downturn year for the technology sector though we're facing a slowdown in the economy more generally. However, $6.5 million was on the table initially, with shares at $17 and at some point, they reached $300. It's better than my 2.5% multiple. Return is a key element."

Apart from returns, Fischer says there is a need to look at the characteristics of the technology deals, and how they match to some of the key criteria PE asset managers look for in an investment: a secure, stable and cashflow consistent investment.

During the recent pandemic, when people were stuck at home and certain business models were impacted due to supply chain or other COVID-related difficulties, software companies managed to weather the storm, because they were providing stability in a global market with little assurance.

"Software is a key theme because of the safe, stable and predictable revenue. We are often speaking about a subscription-based fee. It's recurring, it's not a one-off where you go to the shop, you buy and then don't come back. There is an annual feature, which is key for some of the PE houses, as it shows stable and consistent cashflows," says Fischer.

What you said is interesting because from a general perspective, every sector you have mentioned including software has a common thread: how they store, manage, process, and disseminate data. How do you think private equity managers are responding to increasing investor demands about timeliness of the delivery of this information and the quality of that data?

Fischer says that, as an asset servicer, they are seeing more queries come in.

"PE asset managers may have been too kind with their limited partners [LPs] and have agreed to provide a lot of tailormade reporting which can turn out to be very time-consuming and complicated. I think asset managers have realised that too personalised and specific reporting is not only time-consuming but it's also difficult to produce as you need to identify, extract, clean, analyse the data, build the reporting and send it within the agreed timeline. All these tasks come with a price tag. However, if you're spending too much time to get there, you're losing money. That's why more and more PE asset managers are turning to their asset servicers to see how they can assist," he tells Global Investor/ISF.

"I'm also seeing a clear trend towards the development of investor portals: you let the LP take care of sourcing the reporting and play with the data. For example, in your LPA (limited partnership agreement), if your quarterly reporting needs to be done 15 days after quarter end, you will put everything into your investor portal, where each investor will then get access to the reporting. You can even add a lot of reports for them to search, for any specific information they need, maybe provide some data analytics tools for them to play with the data, do the work themselves because they know what they want. Only in case a LP is not able to find the appropriate data, it will come back to the asset manager for further information and support."

This plays into the theme of the investor being savvier, not only on the data side, but more generally. How are managers adapting their own infrastructure, network systems to this growing savviness, or sophistication within their investors?

Fischer believes it's one of the paradoxes of the subject being discussed.

"While there is a push really from PE asset managers to do tech investments on behalf of the fund they are managing, some of them are still operating with pretty outdated technology," he says. "It's pretty funny because they're investing heavily in technology for their LPs. But are they doing that for themselves? Not sure."

"I think we all see endless manual input in spreadsheets, databases on different systems that can lead to an experience for firms that is far from optimal. I think the leaders within the PE house are really focusing on their internal solutions to help their staff be quicker, more efficient towards the LP. Again, PE houses are competing against each other. Blackrock is competing with KKR, which is competing with Rothschild & Co."

"You need to give your staff the modern experience and the tools to be able to deliver what you promise to your LPs. Again, within RBC or even within some of my clients' companies, I've also seen the development of mobile applications for the staff, so not only for the LP. Some may argue that this makes you work a bit more, but mobile ready applications, strong analytics, reporting and communication tools are key. We have all been working under COVID so we know Microsoft Teams, Zoom and WebEx by heart."

He points out that staff should be

provided with the means to achieve the goals towards the LP.

"It's not only the investment you're doing on behalf of the funds, it's the investment in your staff and within your company."

A less discussed topic - distributed ledger, Blockchain - has seen some initiatives, but they are still small scale. What needs to be done specifically for those areas to become more attractive investment opportunities?

Fischer refocuses on the unstoppable growth that the tech industry has enjoyed over the past five to 10 years. He fast forwards to 2022, where the global economy slowed down. Tech companies of all magnitudes laid off staff due to inflation, rising interest rates and lower sales which added pressure on the financial outlook and on their capabilities.

"When the market is going down, you need to go back to basics: what is the most important item? Trust. I think the difficulty for new, 'emerging technologies' like crypto, digital assets and, as you mentioned, DLT, has been a lack of trust."

"I was reading a study from Ernst & Young from March 2022. It showed that only 3% of larger managers are investing in crypto-related or digital assets. So, very limited penetration. I think the managers were a little uneasy because of the volatility of the asset class alongside the absence of corporate regulation and price fundamentals."

"If you take a step back and look at what happened recently with the spectacular collapse of FTX, that won't necessarily improve the feeling of some asset managers because that big cryptocurrency action platform wiped out millions of people's investments and dealt a massive blow to trust in cryptocurrency. Trust will take time to be rebuild and make private equity investors and asset managers go back into the asset class."

"For the ones that are already investing there, I think we should not throw the baby out with the bath water. I think FTX was an issue, and the market managed the issue by itself. But I think distributed ledger technology (DLT) can still help. I'm far from being a DLT specialist but the way I'm seeing that and what I've been told by some of my colleagues either within RBC or by peers in the market, is that these solutions can offer greater transparency, easier auditability, more speed and efficiencies, cost reductions and automation. Why should we not give it a try?"

"If we want a solution that can help us do business faster and with more accuracy, we should jump into it. This is also why PE houses may come back. For the ones that are currently suffering, they may come back and keep on investing in a technology that is not super mature. Cryptocurrency and DLT: how long have we been speaking about that? Not that much: 10 or 15 years which is not that much from a macro perspective and compared to the generic investment themes." ■

Amelie Labbe, Global Investor, Mickael Fischer, Director of Client Coverage at RBC Investor & Treasury Services (RBC I&TS). Video also available by following the link to the digital magazine at www.globalinvestorgroup.com