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Alpha Generation and Value Creation Through Private Equity Analytics

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Alpha Generation and Value Creation Through Private Equity Analytics

Leveraging Specialized Private Capital Software to Take Data Collection, Investment Analysis and Performance Reporting to the Next Level

by Ganesh Iyer, iLEVEL

The credit crunch and resulting liquidity crisis have reduced the availability of leverage and diminished the role of financial engineering in generating high returns for the private equity asset class. Market dynamics and the challenging economic climate have forced private equity firms to depend on their ability to improve the operating performance of portfolio companies to exceed their investment objectives. Analytics, a key driver of alpha in other asset classes, has now emerged as an important tool for measuring value creation in private equity. Private equity analytics calls for sophisticated and innovative ways to manage and track all the financial, operational, and qualitative data associated with investments. Consequently, intelligence derived from the ability to efficiently collect and store private capital data now commands a significant premium for market participants.

In this environment, some fund managers have very clearly differentiated themselves from the rest of the GP pack by becoming data-driven portfolio activists. They are leading the way by astutely applying technology to monitor all the key performance indicators (KPIs) of investments and strengthening the reporting of the performance of funds and portfolio companies. This not only enables them to quantify alpha generation and value creation to their limited partners (LPs) but also empowers them in a number of other ways including the ability to:

- Conduct portfolio-wide analysis and optimize performance.
- Assemble, analyze and publish investment performance and cash transaction data.
- Reduce the cost and complexity of regulatory compliance.
- Streamline financial modeling and run valuations more rapidly.
- Quickly prepare fundraising materials and investor presentations.

So what has held the others back and prevented them from being able to keep up with the demanding reporting requirements in private equity?

First, collecting data from portfolio companies is often a tedious, error-prone, complicated and manual process. Portfolio companies send data in a variety of formats including spreadsheets, PDFs, PowerPoint decks, emails and paper reports. The resulting volume, variety, and velocity of data and file formats not only affects productivity and efficiency at a private firm, since the data received from portfolio companies often has to be manually re-keyed, but also has the potential to create inaccurate analysis and reporting. The lack of precise information of portfolio company positions, exposures and valuations could also result in situations where the risks related to various investments are not methodically managed and measured. The problem is exacerbated and becomes profound for those fund managers that have complex portfolios, international holdings or investments across multiple strategies.

Second, investment KPIs are invariably spread across various departments of a private equity firm. Data essentially lives in multiple places in disparate documents. Document management is not the challenge — managing the data within documents is the challenge. Financial statements, internal deal models, fee and carried interest calculations, valuation analyses, audit reports, restatements, compliance data, reporting templates, comments and narratives, portfolio reviews and investment staff analyses are not available in a central data warehouse that serves as a single source of truth.

Alpha Generation and Value Creation Through Private Equity Analytics (continued)

CFOs regularly have to go to deal team members to gather financial data on portfolio companies. Investor relations professionals every so often have to contact other teams to collect investment performance metrics. Operating partners frequently find it problematic to accurately quantify their value creation efforts. This is particularly troubling given that portfolio company performance management is now the primary source of value creation for the asset class. To add to these vexing issues, the data available to various teams may not be version-controlled.

In order to successfully overcome these two challenges fund managers require industrial strength data accuracy and standardization as well as a repeatable process for collecting and storing KPIs in a data warehouse. Purpose-built private capital software can assure this and transform the way fund managers control and communicate private capital data by:

- Replacing manual data collection processes with automated web-based processes.
- Creating a secure central repository of this data that serves as a single source of truth.
- Radically reducing the time required for data validation, auditing and verification.
- Making private capital data as transparent, timely, and actionable as public company data.

Lastly, software allows private equity firms to meet the growing demand for information and transparency from regulatory bodies, LPs and internal stakeholders by offering comprehensive web-based dashboards originating from data stored in a central data warehouse that enable consumers to:

- Carry out trend analysis and forecasting.
- Effortlessly model valuations.
- Scrutinize individual company performance.
- Aggregate data to analyze portfolio and fund-wide performance.

The result is improved communication and collaboration among various teams in a private equity firm that helps the fund manager unearth alpha, accelerate value creation and ease fundraising. LPs also benefit from software as they now have reliable and timely information and analysis on how the funds which they have committed their capital to are performing. This transparency helps enable the increased allocation of capital to alternatives by investors seeking greater returns on their investments, but who must provide the same level of reporting to their investment committees as for other asset classes.

Analytics - An Important Tool For Measuring Value Creation in Private Equity

- Private equity analytics calls for sophisticated and innovative ways to manage and track all the financial, operational, and qualitative data associated with investments.
- Fund managers are applying technology to monitor all the key performance indicators (KPIs) of investments and strengthening the reporting of the performance of funds and portfolio companies
- Purpose-built private capital software can transform the way fund managers control and communicate private capital data.

For more information on private equity analytics and private capital software, contact us at salesteam@ilevelsolutions.com.

Ganesh Iyer is the Director Product Marketing at iLEVEL.
You can reach Ganesh at 646.747.9809, giyer@ilevelsolutions.com.