# Mirror, mirror

*As more capital flows in to the region, Asian private equity firms are rapidly coming up the learning curve in fund administration, but finding experienced administrators is a challenge.* Wanching Leong *reports.*

In private equity, fund administration may seem tedious next to the glamour of deal-making. But the function, which includes portfolio accounting, tracking, reporting and servicing, is crucial: investors see the back office as a mirror of the firm's investment process and, ultimately, the viability of the fund.

"Fund administration and reporting is probably one of the critical concerns and focuses of investors doing due diligence," says Mounir Guen, chief executive officer of private equity advisory firm MVision in London, who advises clients around the world. "It's the ultimate sign of institutionalisation in the sense that a GP has a clear valuation policy, governance and reporting guidelines and is able to execute them."

As the industry increasingly looks to Asia for new investments, what is the state of fund administration at private equity firms in the region? Common is the start-up fund that relies on just one partner to handle the function internally. So is the spin-out team that outsources the back office to a service provider. Less common is the fund with all systems and processes in place, and which handles fund administration in-house.

"On the whole, fund administration in the region is probably five years behind Europe or the US," finds James Hutter, business executive and COO of JPMorgan Private Equity Fund Services in New York. Hutter has observed that many firms are using Excel to monitor and track their investments. However, he expects fund administration to evolve rapidly in Asia.

*Vora: better control to administer funds in-house*

> *"Discussions with investors, in terms of what they want to see, help us improve our reporting and incorporate the latest international best practices in our processes."*

But there are wide differences in the sophistication of fund administration at private equity firms across Asia. Firms in Australia, Hong Kong and Singapore are typically advanced, as are GPs in Japan and South Korea. Groups based in China and India are for the most part still catching up.

Some LPs say they have been "pleasantly surprised" at the quality of reporting at those Asian funds they have chosen to back. But they also find new funds to be "innocent" and lacking in fund administration know-how. As more local groups emerge, LPs are keen to help new funds structure the back office in order to provide the kind of reporting they expect and want to see. It's potentially a win-win situation for both GPs and LPs in Asia, but not without some patience, education and good people.

## ALL OVER THE MAP

The local start-up that works off the lowly Excel spreadsheet should not fear: LPs say it doesn't matter what tools and whose software they use, as long as they have good processes, internal governance, a defined valuation policy and, importantly, the ability to deliver good returns. Asian operations of international private equity firms may have the benefit of a global network and established fund administration practices and processes, but local firms have the advantage of local expertise.

Here are examples of fund administration at three local private equity firms in Asia – East West Capital, Mekong Capital and IDFC Private Equity, whose realities and challenges mirror those of many funds in the region, as well as elsewhere.

**The start-up:** Sanjay Sehgal, the managing partner and chief executive officer of Singapore's East West Capital was previously a partner at Schroder Capital Partners (Asia). Like his former employer, Sehgal has appointed an external administrator for East West's healthcare fund. He chose Bermuda and

Guernsey-based Schroder Administrative Services. London-based SV Life Sciences, with whom East West Capital has a strategic relationship, also uses a third-party administrator. "This has worked well for all of us," he notes.

The 11-hour time difference between the firm and its fund administrator, however, presents a challenge. "Having a third-party administrator introduces some delays in execution and responsiveness," admits Sehgal. "But we feel these costs are well worth the comfort that it gives investors that their money is administered by a credible third-party administrator."

East West Capital says it adheres to International Private Equity and Venture Capital Association (IVCA) guidelines for valuation and International Financial Reporting Standards (IFRS) for accounting. The fund reports semi-annually, and Sehgal claims "we have extensive social, environmental, corporate governance and compliance policies in place."

**Growing pains:** Truong Dieu Le, manager of corporate and shareholder services at Vietnam's Mekong Capital says the firm is scaling up its fund administration activities. Truong, a former investment manager, was asked to take over the responsibility from founder and managing director Chris Freund in August 2006. Freund had handled virtually all administrative tasks single-handedly since the firm's inception in 2001 and throughout its first two funds.

"Being a fund administrator demands of you an ability to look at an investment from many different angles in order to have a feel of the 'big picture' before you can produce meaningful reports that meet the requirements of the shareholders," says Truong.

According to her, Mekong Capital has developed a clear and detailed fund administration management process and defined strict corporate governance requirements for portfolio companies. The firm adheres to IFRS accounting standards and IVCA guidelines are applied for subsequent measurement.

Her challenges in doing her job are threefold. First is the lack of timely external resources: communication with one of the firm's fund administrators, located 12-hours behind, is largely limited to email. Second is managing the different requirements of different administrators. Third is meeting different statutory and fiduciary deadlines for the firm's funds that are incorporated in different jurisdictions.

*Truong: differentiates through quality of reporting*

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The firm clearly understands the importance of fund administration: Freund was formerly a vice president and portfolio manager at Templeton Asset Management. Truong says, "The comprehensiveness and insightfulness of our reporting is one area that Mekong Capital strives to differentiate ourselves from the fund management firms in Vietnam."

Truong, a former KPMG tax consultant, will soon manage a team of four. She plans for her staff, each with legal or finance experience, to be responsible for one of the firm's three funds.

**The sophisticate:** Established in 2002, India's IDFC Private Equity has all the elements in place – including a pre-disbursement review. According to its auditor KPMG, IDFC the only fund worldwide among its clients that conducts this review.

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"We thought it's better to have an independent accounting firm review the investment process to give comfort to investors that there is a consistent and transparent process. This also gives us additional comfort on the level of corporate governance and that things are in order," says Rupa Vora, IDFC's chief financial officer.

The infrastructure specialist attributes its sophistication to an experienced team of professionals, which has more than 100 years of private equity experience across the firm. Vora herself has worked for a subsidiary of Belgium's KBC Bank and at Credit Lyonnais.

Also important to the development of fund administration are the firm's investors. "In our second fund, about 75 percent of the capital commitments are received from foreign institutional investors. Discussions with investors, in terms of what they want to see, help us improve our reporting and incorporate the latest international best practices in our processes," says Vora.

One area in which the firm has worked with its LPs is the use of EVCA guidelines, which the investors, including Credit Suisse, Government Investment Corporation of Singapore and Japanese institutions, wanted the fund to adopt. "The only problem I see is getting comparables, because in infrastructure in India, comparables may not be easily available in the public domain," she adds.

Vora and her two staff handle all fund administration in-house. She sees outsourcing as a duplication; besides, there aren't many service providers in India. "Ultimately it's better control to do it ourselves," she says.

**PEOPLE MATTER**

Firms hoping to attract international investors can't afford *not* to set up good processes and systems. For firms that lack expertise, there is plenty of help at their disposal. LPs say they are happy to help with best practices, aside from already asking for what they want to see in reports.

Service providers are setting up operations in Asia. They are coming with the proposition of servicing firms in local time zones and with local expertise, backed by a global network and international standards. JPMorgan, for example, is sizing opportunities in the region from Sydney, while Citi is gunning for market share from Hong Kong.

But private equity firms looking to outsource beware: LPs have complained that there may be delays, and information can be less accurate than firms that handle fund administration in-house.

William LaFayette, chief financial officer of fund of funds Asia Alternatives in Hong Kong, has had a good experience with Asian private equity firms. "I thought that we would do a lot more explaining of US GAAP. What I've seen is most of these groups are running reports either through their firms in the US or big four auditors," he says, although adding that there is some learning to be done in dealing with US tax issues. He is also a fan of hosted websites from which he can download reports.

But there are three major issues in private equity fund administration in Asia: finding people, valuation and "parallel" processes. Truong's difficulty in finding experienced fund administrators in Vietnam is not unique – Citi managing director Glenn Kennedy admits that outside Hong Kong, recruiting and retaining people is one of the firm's biggest challenges, globally.

Valuation methods in Asia are not uniform. In India, where private equity is not regulated, IDFC's adoption of EVCA guidelines was prompted by the fund's LPs. A standard valuation method across the region has not been developed, nor has there been much discussion of such methods.

According to Guen, Asian private equity firms operating in countries such as Australia, India and Japan have the added challenge of different regulations for local and international investors. "Local country funds have been able to structure them to be able to have in parallel both types of investors. It means different PPMs, different diligence materials, different processes and different reporting. That's where the big complexity comes in," he says.

Wherever private equity firms may be in their fund administration, one thing's for sure – only about 10 percent of global capital was raised in Asia last year, and much more is expected in the future as the region continues to lure GPs and LPs. And for GPs that want to succeed, better fund administration will result. ■