



Opalesque North America PE & VC Roundtable

Opalesque Roundtable Sponsor:

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Editor's Note

Private Equity AUM as a share of US GDP was 5% in 2002 and 17% in 2018 which gives rise to many questions and concerns: Is this already too big for the economy? What about valuations? Should we invest now or wait a bit?

Participants of this Roundtable believe that the PE class will continue to grow driven by institutional investors' dilemma of how to get to a seven or eight percent actuarial assumption in a low yield environment with an expensive stock market. The answer for many institutions is to increase their target allocations to private assets.

Meanwhile, some investors already think that *certain pockets of private equity are absurdly expensive and some offerings might turn into a game of musical chairs at some point (page 8)*. Also Venture Capital is very expensive and funds are challenged to find sound investments that are not already fully priced (however, an investment can be "okay" even if fully priced as long as the business model executes – see example on page 10). Still, the industry is being forced to develop new, more specialized models and turn away from the "cocktail party" investing style (page 11) at a time where VC funds at a fraction of a SoftBank Vision Fund size are also gaining traction with investors.

"What is ODD?" 10 years behind hedge funds & tax issues coming down the pipe

Some people in the industry think that private equity is now where hedge funds used to be 10 years ago – more or less before Madoff. Sure, a number of the bigger private equity firms are using an external administrator – but does this address all potential concerns? Why is **AML risk** still a major theme in PE and VC?

Another theme that seems to resonate through out the industry is that private equity players are still quite reluctant to evaluate their specific tax risk profile. Structurings should provide for after-tax benefits for investors, but these concepts are endangered. New tax transparency concepts such as **DAC6** will be enacted latest 2020 with a retroactive three year reporting period. Furthermore the very stringent anti-avoidance tax directive will be implemented soon, too. This means there are plenty of tax issues coming down the pipe both on national and international level. In this context it should be noted that part of the German CFC/PFIC concept is now introduced in US tax legislation as well.

Data Crunching: Surprising Findings

What does "big data" say when you look at questions such as "death by committee" versus "death by a gunslinger" (quality of investment decisions), and why often with fund three "the wheels can start to fall off, and fund four then often is a disaster"? (page 27-28)?

The Opalesque 2019 North America Private Equity & Venture Capital Roundtable, sponsored by **WTS Global**, took place in New York with:

1. Anushree Mohta, **Head of Operational Due Diligence, Siguler Guff & Company**
2. Barry Seeman, **US Investor Relations and Advisor, Leaseum Partners**
3. Christopher Zook, **Chairman and Chief Investment Officer, CAZ Investments**
4. Matthew Leibowitz, **Partner, Plaza Ventures**
5. Robert Welzel, **Partner, WTS Global (sponsor)**
6. Ronen Schwartzman, **CIO, Cooper Family Office**

The group also discussed:

- Combining private credit with private equity. Where to look for low correlations to equity markets. The risks of covenant-lite lending (page 8)
- What to think of the mega buyout funds. The role of the Multiple On Investing Capital (MOIC) ratio vs. IRR. Adding true value post-acquisition (page 10)
- The attraction of small and emerging PE/VC managers / seeding (page 10, 25, 30) and how to address their business viability (page 30-31)
- Making money with 'tweener rounds'. How to minimize the J-curve return on LP capital. A new mode of raising VC capital (page 12-14)

- VC in Israel (page 15-17). VC in Canada (page 16-19). VC in New Zealand and Africa (page 7, 17-18, 33)
- **Aspects on Due Diligence on PE/VC funds: Administrators, Internal Controls, Business Risk, Governance** (page 19-23)
- Tokenization: Why family offices are cautious (page 24)
- **Key man risk / Succession: As private equity matures - literally - the industry could be facing its first major wave of retirements: Implications for investors** (page 24)
- GP Academy /Kauffman Fellowship Program. How GPS should deal with disputes inside of their partnerships (page 26-28)
- **Where are fees heading in PE/VC? Who is charging zero management fees? Co-Investing: More words than action. The history of the 2 and 20** (page 28-29)
- How to get and manage good deal flow (page 32).

Enjoy!

Matthias Knab
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Participant Profiles



(LEFT TO RIGHT):

Robert Welzel, Christopher Zook, Ronen Schwartzman, Matthias Knab
Matthew Leibowitz, Anushree Mohta, Barry Seeman

Image credit: NASA / GSFC / LaRC / JPL, SRTM / MISR Teams

Introduction

Ronen Schwartzman
Cooper Family Office

I am the CIO for the Cooper Family Office. We are a single-family office. I have a team of four investment professionals that work with me. Both private equity and venture capital are a part of the illiquid portion of our portfolio and we have grown our allocation to both PE and VC in recent years.

I am a former Special Ops Intelligence Officer in the Israeli Air Force. So, you could say I have been in the business of capital preservation for 27 years now. I have spent the last 20 years in capital markets out of which I have been allocating to managers for the last 11 years and made money both in 2008 and 2018, the only two years when the markets were down in the last decade.

Barry Seeman
Leaseum Partners

I'm Barry Seeman, founder of Bear Run Partners which is my private consulting group. I have over 30 years of experience on both the buy-side and sell-side of Wall Street and in Asset Management. A number of years ago, I was co-head of AXA's alternatives platform – the French life insurance company. After that, I formed my own company with the other co-head from AXA. We then sold that business to Natixis, one of the large French Investment Banks, and subsequently, I became head of their US operation for alternatives. So, I have a lot of alternative investments in my blood but also capital markets experience. Prior to forming Bear Run Partners, I was a head of Global Derivatives and Hedging for Aegon for six years. During this time, I put my trading hat back on and lead a highly professional team of derivatives traders and portfolio managers concentrated on risk management of the global exposures of large insurance and annuity portfolios.

Today, I am working with a wonderful team at Leaseum Partners, which is a brand new private equity real estate fund tapping into the talents of the Chetrit Organization, which is one of largest private real estate family offices in the United States.

Anushree Mohta
Siguler Guff & Company

I'm Anushree Mohta. I recently joined Siguler Guff & Company as the Head of Operational Due Diligence. To provide a bit more context, I am responsible for conducting the operational due diligence on our underlying private equity and real estate fund managers.

Prior to Siguler Guff, I was at GM Asset Management's and was responsible for conducting operational due diligence on alternative and traditional asset managers included within GMAM's pension portfolio. Prior to GMAM, I was Vice President, Operational Due Diligence at Citi Private Bank. I started my operational due diligence career right at Castle Hall Alternatives in Montreal and have also worked at Alliance Bernstein and Towers Watson. I went to McGill University for both my Bachelors and MBA and am currently a guest lecturer there.

Matthew Leibowitz
Plaza Ventures

Matthew Leibowitz from Plaza Ventures based in Toronto. Plaza Ventures started off as the family office of Plazacorp which is one of Canada's largest private real estate developers and has been around for about 40 years. Plazacorp is currently doing about 5 billion dollars in real estate development primarily in the Greater Toronto Area market which has been booming for the last 20 years or so.

I joined Plaza Ventures 7 years ago with a view to formalize a private equity venture capital practice out of the family office platform. Plaza Ventures is now one of Canada's largest and most active venture capital firms. We have a very unique model which I will be happy to talk about today.

Christopher Zook
CAZ Investments

My name is Christopher Zook. I am based in Houston, Texas where I serve as Chairman and Chief Investment Officer of a multi-family office that I started in 2001; we invest in anything, anywhere, anytime and literally cover the gamut from direct investments, co-investments, and fund investments; managed internally and externally. We have about 1.3 billion in AUM currently deployed, with about 75% of that in private equity.

We are very thematic, and our largest current theme is the growth of private equity as an asset class. Alongside our various partners, we own minority stakes in the general partners of private equity firms. Obviously, we also invest as a limited partner in funds of some of the same firms, and many other firms.

About 300 million of our assets that are currently deployed is our shareholders' capital. We are the largest investor in our vehicles, and we are always the first money in. One of the things that probably is the most unique about us is that we rarely charge management fees for what we do, we typically just work for carry.

Robert Welzel
WTS Global

My name is Robert Welzel. I am a tax partner at WTS Global in Frankfurt with a consulting focus on international tax and regulatory issues. The company was formed in 2000 by former employees from the central tax department of Siemens and has since then developed rapidly. At present, our headcount in Germany is approx. 1,000, and the international tax network of WTS Global worldwide exceeds already 3,000 consultants.

Our main focus in Germany is tax consultancy and tax compliance for large corporations, both DAX and "Mittelstand". **These clients are expanding their investments in private equity and alternatives.** Our unique business partnering model constitutes de facto the in-house tax functions of corporations. We are expanding this business model not only in Germany but also on a worldwide basis.

WTS Global serves both major private equity houses and big institutional clients to manage cross-border tax reporting needs. The WTS Global service offering may be of interest for private equity houses intending to strengthen their international investor basis, too. Seamless cross-border tax and investor reporting should support the distribution of private equity and venture capital funds. WTS Global bottom up granularity methodology approach based on capturing and analyzing the economic data of the underlying target investments of the alternative funds provides for the realizability to adapt and facilitate the e.g. partnership, CFC-alike tax compliance reporting needs of any envisaged jurisdiction in a scalable and economically reasonable approach per investor. Applying a reasonable fee estimation reflecting the complexity of the specific alternative funds would bolster the economic scalability of any global fund marketing strategy especially in the institutional investor sphere.

WTS Global will soon announce a new New York based partner firm. This new partner will enhance significantly our US tax service offering in the asset management industry.

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Christopher Zook: Well, as I referred to briefly in my introduction, our largest theme is that **the private equity class will continue to grow**. And one of the reasons for that is that it has become apparent to so many institutional investors they are going to have a really difficult time hitting their target rates of return from traditional investments.

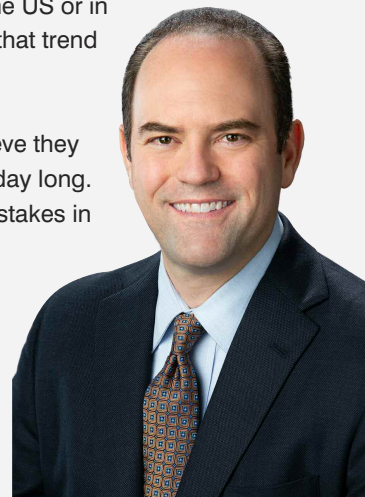
To make a long story short, I was involved with the fixing of the Houston pension system two years ago. For that, I did a significant study of almost all the national plans, including the statewide plans, big city plans, etc., because we had a seven-billion-dollar hole that we had to try to figure out how to fill. Around that time, I was at a conference here in New York where I had the opportunity to ask eight of the largest pension fund managers about the expected investment return of their portfolio over the next decade?" They thought about it for quite a bit, and after a while, the highest number I got was 4.3%, the medium was basically 3.9% and several were as low as 3.2%.

Now, the 10-year treasury at that time was about two, so, it was a bit of a different world than where we are today, but we are not that far away. **The point of course, is how do you get to a seven or eight percent actuarial assumption in a low yield environment, with an expensive stock market? The answer for many institutions is to increase their target allocations to private assets.** Therefore, if institutions are going to continue to allocate more capital to the private market because they don't have any other realistic choice, that is going to drive assets under management growth for the entire industry. It is going to go to private equity, private real estate, private credit, etc., and *we want to own the firms that are going to benefit from that systematic growth.*

The theme is reinforced by the ongoing decline of the number of publicly traded companies. So many listed companies have gone private or consolidated and there are less that want to go public because of the burden of being a public company. That percentage of private companies as a percentage of GDP will, therefore, continue to go up. That also supports the logic for institutions to also increase their allocations to private assets.

I was in New Zealand recently, doing research on nearly every private equity firm in the country. One statistic that I found fascinating is that roughly 70% of the New Zealand GDP is controlled by private companies and only about 30% by public companies, despite the fact that they have a robust stock exchange. While I don't think that in the US or in Europe we will grow to become that large a percentage but, barring major regulatory changes, that trend of more of GDP being in the private hands is going to continue.

Valuations in many pockets of the world are definitely higher than is ideal, but If institutions believe they can make even 12%, and feel like they have a pretty high certainty of that, they will take that all day long. That will drive more and more capital to private equity. One of the main reasons we like owning stakes in the asset management firms themselves is that, whether or not the LP's hit their expected return targets, the GP's are providing their investors with a better chance to achieve their objectives. When they do that, as the owners, we get to share in all of the economics of the company, including the management fees, carried interest, and profits from investing the balance sheet, etc.



Ronen Schwartzman: *I completely agree with you with about the challenge of getting those seven or eight percent returns and that private equity is, of course, a place people look for that. But we also have a concern around that. It's now already a decade where everything has been working, but there will come a year when it's not going to work and then what? Secondly, as we all know there is a J-curve where you first invest and then there's this time gap until you get returns. The way we thought about it is by not only invest in private equity but also have allocations to private credit that generates yield as we are waiting for the PE funds to generate performance.*

On the private credit side, the common theme for investors like us is to find areas that have a **low correlation to equity markets**. This can include things like solar projects that also tax advantage from the depreciation of the assets.



We also looked at life settlements in the past which we think is an asset class that is completely uncorrelated to the equity and debt markets.

But we agree, if you want kind of the type of upside returns we talked about, other than just owning an S&P 500 ETF which has been great the last decade, then private equity is a place that we are and should be active in.

Matthias Knab

So what will happen to valuations if this wall of money is just continuing to flow into PE? As investors, what are your investment, your selection and risk parameters?

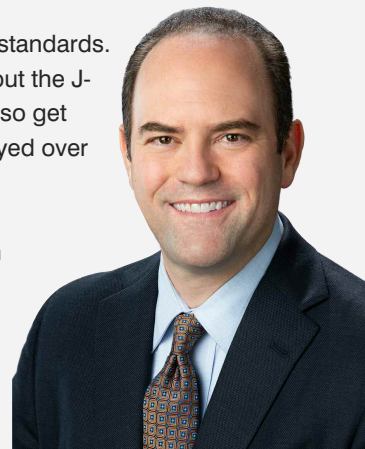
Christopher Zook: *From the standpoint of valuations, there are pockets of private equity right now that are certainly expensive, absurdly expensive. We would not, as a limited partner, invest in a buyout fund that is buying companies at 12 times EBITDA and putting six turns of leverage on it. That is just a game of musical chairs, somebody's not going to have a chair when the music stops.*

However, there are still lots of parts of private equity that are not ridiculously expensive. They might be a little bit expensive but they are still cheaper than the public market comparable.

*The biggest concern we have for the asset class as a whole is the amount of the **covenant-lite lending** that's being done. That is actually a good thing for the private equity sponsors because they will not have their feet held to the fire when the economy turns down, but it's really not good for those that are on the other side of that credit situation.*

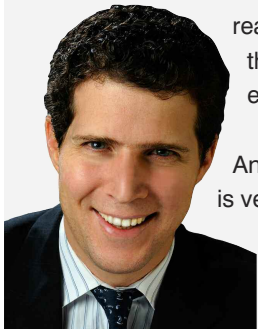
So, we are very cautious about who is being diligent and who is sticking with their underwriting standards. But ultimately, as the owner of the private equity firm itself, going back that what Ronen said about the J-curve, we get paid management fees while potentially the downturn comes. Then, capital can also get deployed at better prices, because yes, there is this huge war-chest of money that will be deployed over the next three to five years. We actually like that.

Let's say the recession comes sometime, who knows, in 2021. This means there are likely much better valuations, and the firms will be allocating capital at those much more attractive levels. In the meantime, we get an extremely attractive yield from the cash flows from the management fees, because being on the general partner side of the table, we all know is a preferred



economic situation versus being on a limited partner side of the table. And this, again, is why we are really comfortable with the asset class as a whole. But, as a limited partner where we spend a tremendous amount of time, I agree that it's tough to find things that are inexpensive. We want to make sure that we are not chasing managers that are being unwise with how they are deploying capital. There are a lot of landmines out there that people need to avoid.

Ronen Schwartzman: I agree with you, we all know that we are in the seventh or eighth inning of this rally in the market which might continue another year or two or three, nobody knows, right? We may have thought that maybe the fourth quarter of 2018 was the beginning of the end, but now, very few people think like that. We had great GDP numbers in the first quarter and also corporate earnings in Q1 were stronger than expected. We have election coming up next year, and at the same time, we have a president and an administration that pay a lot of attention to the stock market. We also have a Fed that is very accommodative as they switched completely in January and so we don't expect them to raise rates any time soon. Therefore, this bull market can continue for a while.



Because we are LPs and not GPs, we are extremely cautious with what we are investing in today. You really have to be something special and unique for us in order to write that check to be an LP and to take that duration risk. For example, it could be an artificial intelligence focused venture capital fund, this is an example of something that I would think is unique.

And to Christopher's point about how new funds are raising capital today but also how rapidly they deploy it is very important. Because maybe today they are buying something at X but it could be that in 18 months, it will be worth only 0.8x. So, you need to be very careful and pay attention to that as well.

Barry Seeman: I would ask Christopher and Ronen since you are managing allocations to this asset class, how are you looking to split your time between VC, buyout firms or funds, and some of the private products that are out there?

There has been a tremendous amount of capital raised over the last two years by all of the large firms from Blackstone, Carlyle, Cerberus – are there still ample opportunities for them to get the money to work in a way that will satisfy your target returns?



Christopher Zook: I'll answer the second question first. **We think the mega funds are going to have a tougher time hitting our target returns.**

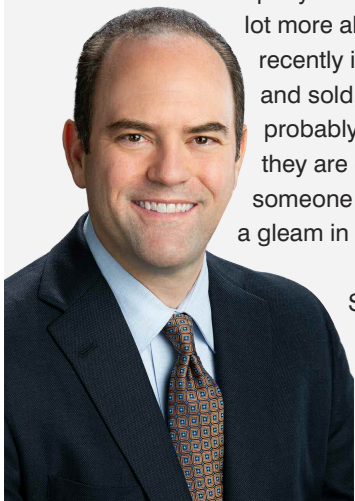
*Our target returns tend to be higher than a lot of others. We want a 2X **multiple on investing capital, MOIC**, and a 15% IRR. People come and present us a 1.4X with an 18% IRR and that's just not very attractive to us personally, because we can't eat IRR but we can eat MOIC. So, I believe that it's going to be very hard for those mega funds to reach our target returns but they are meeting the target returns of the big institutions to be happy with 12 to 14%. Those allocators also feel confident that they are not going to get fired because their committee knows XYZ mega firm and feels comfortable with them. So, we as an LP, would not be allocating much to that segment.*

To the first part of your question, we tend not to actually invest much in buyout as a general rule. We are not big fans of just financial engineering creating alpha. We like buyout firms that do something unique, going back to Ronen's point, where a company comes in and actually adds value, that they can grow the portfolio company faster or they can strip out the inefficiencies. Full disclosure, we are partners with HIG which is or one of our favorite firms in this space. HIG buys what many people will not buy but then they are masterful at creating incredible rates of return through coming and fixing those situations. Platinum is another great example of **true value post-acquisition**. That for us is worth looking at, but there aren't a lot of firms of the caliber of HIG and Platinum out there.

Ronen also brought up the lack of correlation, which we believe is important as well. This could be through things like medical royalties or other asset classes that just don't correlate, we do like those.

But Barry's question was specifically between venture capital, private equity, and private credit. For us, private credit as an LP is not very attractive because it doesn't meet our target rates of return, most of the time. We just don't have to invest in that space, unlike some professional buyers who have a portfolio with strict allocation mandates.

Venture capital is very interesting for us, but it's one of those areas right now that is very expensive, so it's hard for the underlying funds to find things and investments that are not already fully priced. **It's okay if something is fully priced as long as the business model executes.** We invested in Lyft several years ago, we knew it was fully priced then based on where the company was. Now, today, one could argue whether \$60 is fair market value or \$88, we don't know. We care a lot more about what it is when our lockup comes off, that's what matters to us. We made an investment recently in Opendoor, which is a company that is completely changing the way that homes are bought and sold, along with a few other players. But if they execute on their business model, even though it was probably fairly valued at the time we made the investment, based on the magnitude of the change that they are creating, we will still make a phenomenal rate of return on our money. That is a lot different than someone else that is going into a series A paying a billion-dollar valuation for a company that is just kind of a gleam in somebody's eye.

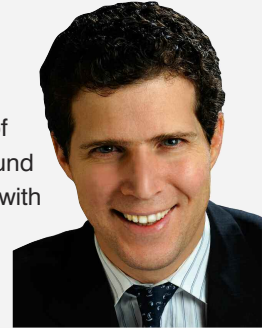


So, we are spending time on those asset classes. It is just very idiosyncratic. From our perspective, besides the growth of private equity as an asset class and then also the ride-sharing revolution as our second biggest theme, it is hard to find compelling risk/reward situations.

Ronen Schwartzman: Barry, just to frame this correctly, in our family office we always focus on **small and emerging managers**. We prefer the smaller funds where in general it's easier to generate alpha and where the founders have most net worth-invested along with us.

Buyouts were never something that personally I liked so much because of similar reasons to those that Christopher mentioned. But we do like venture capital. We have also invested in real estate but I have to say we were more active in it a few years back when we thought the opportunity set was more compelling. But even here, we chose to focus on more niche opportunities like senior living housing, light industrials or self-storage, that we found to be more attractive. These days, we are seeing many deals that are priced at 8% return valued at three cap. We think there is very limited upside when you are buying real estate at these valuations and therefore, we are extremely selective when we do things in real estate.

Back to VC where it's about the innovation and the growth. We absolutely pay attention to the valuations of the companies we invest in and will not invest at any price. We typically invest anywhere from the seed round to the A round, so we like to be early. We have strong relationships with other families we like to co-invest with as well as with accelerators.



Matthias Knab

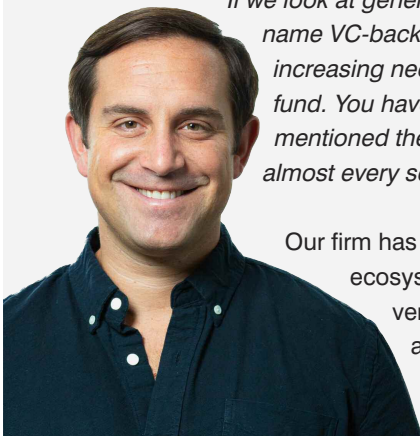
Matthew, you are a VC manager, please share with us what you see from your perspective.

Matthew Leibowitz: *Honestly, there are a lot of expensive and over-valued companies. We correctly pointed out that a lot of firms have raised big funds recently. And those managers are under pressure to put that capital to work. This trend pressures VCs to take riskier bets and move quickly on deals when they should do a little bit more due diligence or pass on the opportunity.*

Canada is different in some ways. We do have some of the largest private equity firms on the planet which are typically the pension funds, CPPIB, OMERS, et cetera. These funds are active here in New York and all of the world, but have limited presence in venture, which is very unique. We do hear some rumblings though that they are starting to get more into VC and we have been talking to some folks over there, but mostly they have been a laggard. The VC industry in Canada has really been either led by the government or by independent firms like us.

If we look at general trends in the industry, first there seems to be an insatiable appetite for any sort for brand name VC-backed companies to go public right now. The second trend, which you also touched on, is an increasing need for VCs to become more specialized. It has gotten harder for a VC to be a generalist fund. You have to focus either on a specific area or the VC model itself has to be different. – Ronen mentioned the AI-focused VC fund, which is also very general because AI can now be deployed in almost every sector and every company.

Our firm has employed a very different kind of VC model which is resonating well with the tech ecosystem. That to me is really the future of venture capital – either you specialize in an industry vertical, and/or you adapt your structure to make it more unique or bespoke in the ecosystem as well.



Matthew Leibowitz: Sure. Actually, we don't believe in big funds either, so we have no interest in raising one. I personally have no interest specifically because I don't think the economics work.

See, the typical venture capital model is that you raise a hundred million dollars, just for argument sake, you invest in 30 companies, 20 of which are write-offs the day after you invest, 5 are okay, three are good and two are your unicorns, your fund-makers. And it's a 10-year black box fund. The GP charges two percent per year and management fees plus some operating expenses. This means that by the time you back out all of the fees and expenses over the 10-year fund, depending on capital calls and how it is structured, you are basically left with between 72 to 78 cents on a dollar to net invest into a company. And you need about a 3.3, 3.4 X and on that 75 cents in order to return all the capital, start getting past your hurdle rates and get into some carry, which is the reason why VCs should be getting into it in the first place.

I looked at that model and just found that it doesn't make sense for me structurally. I'll use a real estate analogy here, **imagine building a 30-story building and relying on the penthouse in order to make money.** You probably wouldn't want to build that building, that's my guess. What we do instead is we raise a relatively small fund every year when we have the immediate deal flow to support it. We put it in about a third of the capital ourselves to seed each fund and we don't charge any management fees. Thus far, our investors are exclusively ultra-high net worth individuals and family-offices.

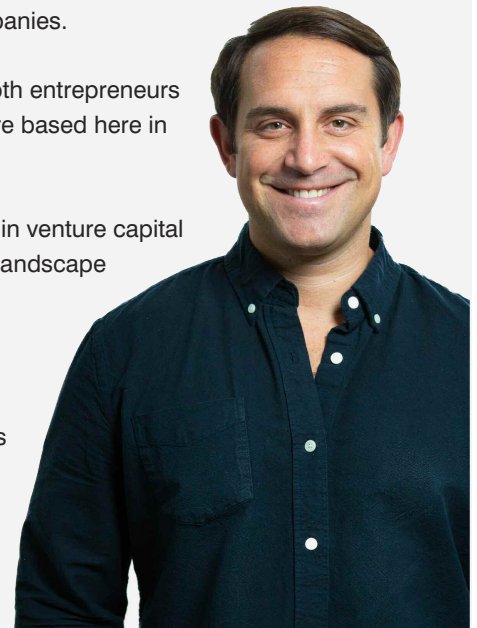
We have three strategies that we employ. First is a series A/series B fund which is really for more growth-orientated companies. And even within that fund, we specialize in something that I call **'tweener rounds'** or extension rounds. A tweener is a term that you would relate to a kid who's not really a kid and not quite a teenager. So, I am applying this term to our investment thesis relating to a company that has raised series A and is just a little bit premature for that large series B. Often times, such a firm is just looking for a little bit more runway and wants to raise another 1 million to 4 million in order to hit some more milestones to be able to raise its next round at a higher valuation and higher multiples. That is really our specialization.

And then over the last summer, we launched Canada's first ever direct secondary fund, where we're buying out shares from either early angel investors or early employees in pre-IPO, pre-M&A tech companies. Thirdly, we just launched Canada's first ever venture capital fund to invest in Israeli technologies companies.

For that, we were able to bring on two phenomenal Israeli women partners who are both entrepreneurs turned angel investors turned VCs, who have joined us to launch this VC fund. They are based here in New York and in Israel.

So, coming back to the big picture, we believe in specialization which is really the key in venture capital going forward. We are seeing other folks like us who also have a different take on the landscape being successful with that, and hopefully, that will yield much better returns.

Ronen, you brought up the J-curve earlier, and indeed, our reason why we started the fund and platform was to **minimize that dip in the J-curve return on LP capital.** We have been able to demonstrate that we can return LP capital in 18 to 36 months versus the typical VC fund or private equity fund terms that is more like 7, 8 years.



Ronen Schwartzman: And how exactly do you do that?

Matthew Leibowitz: The tweener rounds allow us to realize quicker returns. Typically the companies raise their next round after our investment in 6 to 18 months, which gives us an opportunity to liquidate out investment. Probably 90 plus percent of the VCs don't sell at that point and this differentiates us from typical VCs.

Ronen Schwartzman: And you said no management fees. How do you sustain a business without management fee?

Matthew Leibowitz: We are bearing some of the overhead cost ourselves, for example, we are housed inside of the Plazacorp family office. We also have a capped expense budget that we publish to our LPs in advance. In terms of net invested dollars, we come in at about 92, 93 cents on the dollar to invest in companies, so compared to the other figures I mentioned before, we are following a more efficient model.

Ronen Schwartzman: How large are your funds then?

Matthew Leibowitz: Each fund is about \$25 million every year. We are structured like a multi-hundred-million-dollar venture capital fund, but we only raise the fund when we have the immediate deal flow to support. This allows us to have higher transparency in expenses and in capital allocation.

Ronen Schwartzman: So you are raising every year in a new vehicle, do you find this also puts pressure on you to deploy the capital?



Matthew Leibowitz: Sure, I understand that this is the situation many VCs are in, but we will only raise the fund when we have the immediate deal flow to support it.

This means that when we start speaking to prospective LPs, they know from day one where 40% to 60% of the capital is going. We are always working on deal flow, so I can clearly demonstrate to investors where their money would be going tomorrow. If you look at our track record, we are now on our seventh fund in five and a half years. The longest we've taken to invest entire funds has been seven months.

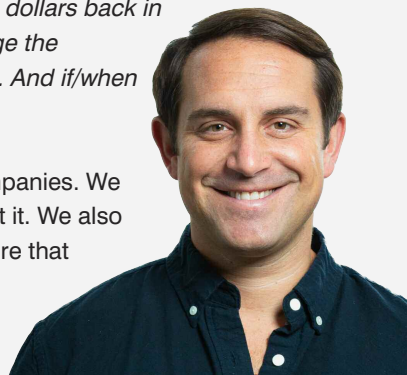
Ronen Schwartzman: And how many investments are in a fund?

Matthew Leibowitz: We started off doing two or three in a fund, now we're in about eight, nine per fund.

Ronen Schwartzman: And then you also don't do any follow-ups. You just invest the first round and you sell -

Matthew Leibowitz: Correct, we don't reserve any capital in our funds. This is another point of differentiation. We don't believe in reserving capital because we think that it creates bad decision-making. **Many VC managers end up putting good money after bad, to protect their positions.** *If a company is going down, you see VCs often piling dollars back in to support their ownership. Our view is different. We believe that management should change the business model, or right size, or do something to recalibrate the economics of the business. And if/when that works out, we will be able to re-invest.*

However, typically, about half of the future funds will be invested in prior funds' portfolio companies. We are very upfront to management teams about our philosophy and structure and they respect it. We also have an LP advisory committee and investment committee that help us adjudicate and ensure that there are no conflicts of interest.



Ronen Schwartzman: These questions are very interesting to look at when doing operational due diligence.

Matthew Leibowitz: You are right. Of course, we have been dealing with such ODD for four or five years and never had issues. If you look at our track record, we have passed on a few "interim or down rounds", but when a company is raising their next round of financing and it's a good deal to do, we have followed on. And so, we've made numerous follow-on investments to continue supporting our portfolio companies.

Christopher Zook: Do you offer rights of first refusal to those in a previous fund, if that's a follow-on to the existing position?

Matthew Leibowitz: No, *we treat each follow-on investment as though it's a net new investment opportunity because it's a new fund, we have new LPs, etcetera.*

When we speak to new LPs, we need to justify and clearly explain that this is the best deal we can do right now. We are also already on the board of these companies and have clarity into the business to make a real-time decision to follow on or not.



Ronen Schwartzman: And has been any situation where you sold a stake from fund one into one of your later funds?

Matthew Leibowitz: Absolutely not, and we are very clear about that. As I said, we have a limited partner advisory committee and investment committee. We only do add-on investments.

Our transparency and investment model have resonated well with our LPs' interest. A few years ago, we had zero investors aside from the Plazacorp family, and now we have about a hundred ultra-high net worth individuals and single and/or multi-family offices that are investors in our funds.

Christopher Zook:

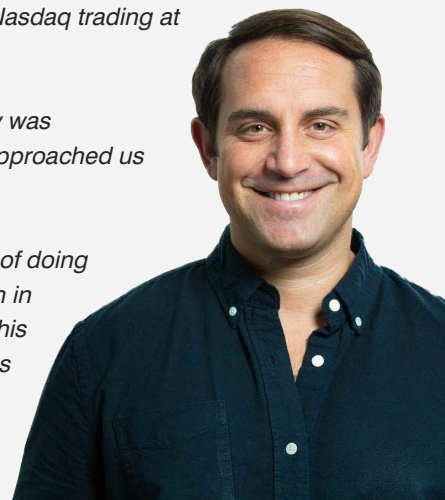
Matthew, coming back to your Israeli investments, we invested in Israeli healthcare via two separate funds. Israeli healthcare seemed to be less developed than the Israeli technology world, which we felt could generate opportunity. With that backdrop, I am curious as to your thoughts whether the technology space there is overcrowded these days?

Matthew Leibowitz: *Even though the country is number two on the planet for start-ups after the United States, there's way more capital in Israel than there are returns and/or companies. There is no shortage of capital to invest in Israeli tech companies and they don't need new check writers from that perspective.*

We are not unaware of that situation or immune to the fact that we are going to be a new player, and so the question is why do we think we have a "competitive advantage?" It's because of the two partners that we just brought on. One is one of the early team members of a company called, "Wix" which is now publicly traded on Nasdaq trading at about a \$6.5 billion market cap.

The other woman started with her husband a company acquired by IBM. Their company was bootstrapped, and they did extraordinarily well. The couple were LPs in our funds and approached us with the Israeli fund strategy.

The two partners are both Israeli, as I mentioned, and they wanted to bring our concept of doing extension rounds and fund structure to the Israeli tech ecosystem which we haven't seen in other Israeli, American or Chinese VCs. In our view, the Israeli VC ecosystem is ripe for this sort of extension round investing opportunity. Also, we can be a value-add for companies that are looking to move into the North American market by providing them the platform to do that.



Christopher Zook:

Will you be following the same kind of concept for the Israeli VC fund of doing just very small funds as needed or will you be taking more of a traditional approach for that one?

Matthew Leibowitz:

Yes, effectively replicating exactly what we have been doing in our core series A, series B fund in Canada with extensions and applying that to the Israeli tech ecosystem with the support of these two partners.

Anushree Mohta:

Do you offer co-investments on the side as well?

Matthew Leibowitz:

Absolutely. We offer co-investments to our LPs, and there were many instances where our LPs have co-invested along with the fund. We create a Special Purpose Vehicle on a deal-to deal basis.

Ronen Schwartzman:

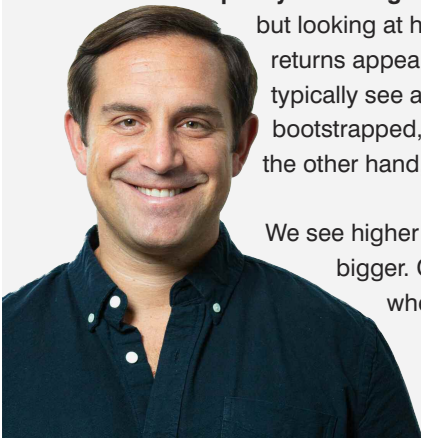
And how do you think about valuations in your space?

Matthew Leibowitz:

In Canada or in Israel?

Ronen Schwartzman:

Anywhere where you invest.



Matthew Leibowitz: Let's start with Israel. There, we see valuations in line with Silicon Valley or New York. I will say **the quality of management and IP is extraordinary in Israel.** However, this fact does not justify any valuations but looking at how business plans and business models can be implemented there, the potential for returns appears attractive. In Canada, not that I'm here to denigrate the Canadian tech industry either, we typically see a different profile of companies. Canadian companies that we typically see are mostly bootstrapped, looking to raise 5, 10 million dollars and then work towards a liquidity event. In Israel, on the other hand, it's more like a let's 'swing for the fences', if you will.

We see higher valuations in Israeli tech companies compared to Canadian ones, and the bets are also bigger. Our LPs are very aware of this and goes in with eyes wide open to the rules of engagement when investing in Israeli tech.

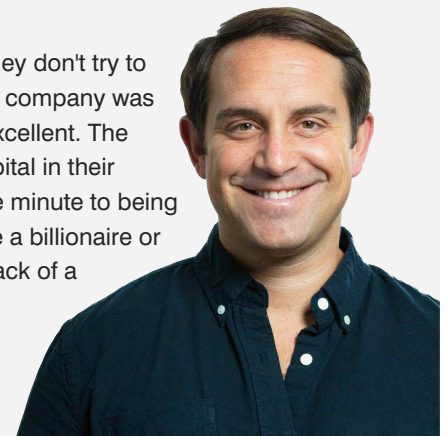
Christopher Zook:

I'm curious, is there a certain niche that the Canadian companies are trying to serve? What is it that differentiates them as opportunities compared to Israel or the U.S, etc.?

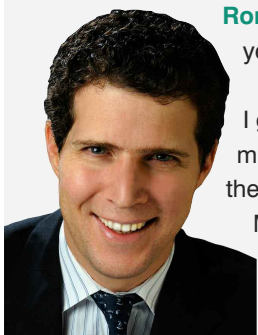
Matthew Leibowitz: I wouldn't say there's a specific niche per se but allow me to elaborate a bit on the general landscape. Canada, particularly Toronto over the last couple years has really become known as one of the global AI hubs for various reasons, some justified and others unjustified. But nevertheless, there are six world-class universities within an hour's drive of downtown Toronto. The tax base is capital-deficient for tech companies. Toronto just became the third largest city in North America to surpass Chicago with seven and a half million people living in the city, where 51% of the population was born outside of Canada, so you have immigrants from four corners of the globe bringing their culture and striving for a better life. They are motivated entrepreneurs.

What we don't see though, are big returns and marquee exits, which is somewhat ironic given that we have all the ingredients to build world-class international companies. I wrote a blog about this conundrum about a year and a half ago. My view of it is in America, you have the American dream. Well that's actually been supplanted in Canada by the 'Canadian dream', in which you have this objective of buying a house with the white picket fence, you send your kids to private school, you buy a cottage and you sell your company and put 5 to 10 million dollars in your pocket. In Israel or New York or Silicon Valley, that dream may be considered a failure. However, in Canada, that's a massive home run. While it's not that the dollar goes further in Canada per se because the tax base is high, but, as a Canadian, that's a huge win and more money than most people who come to Canada even dreamed of.

What this means, is that **I believe a lot of Canadian companies sell prematurely** and they don't try to swing for the fences. We just had an exit three weeks ago, and it was a fabulous exit. The company was acquired for \$100 million. We were only invested for 19, 20 months, and our MOIC was excellent. The management of the firm, a few guys in their mid-30s, each put a significant amount of capital in their pockets and it changed their lives materially as they went from being non-millionaires one minute to being multi-millionaires the next. However, they became multi-millionaires instead of trying to be a billionaire or aiming to build a billion-dollar company. And I think that's something very Canadian, for lack of a better term.



In my humble opinion, as a Canadian-born and bred, this mindset is unique to Canada. However, there is also a younger generation of entrepreneurs that read TechCrunch, have watched Silicon Valley grow and now aspire to build billion-dollar companies. They are adopting the "get out of my way, I'm building a billion-dollar company" mentality.

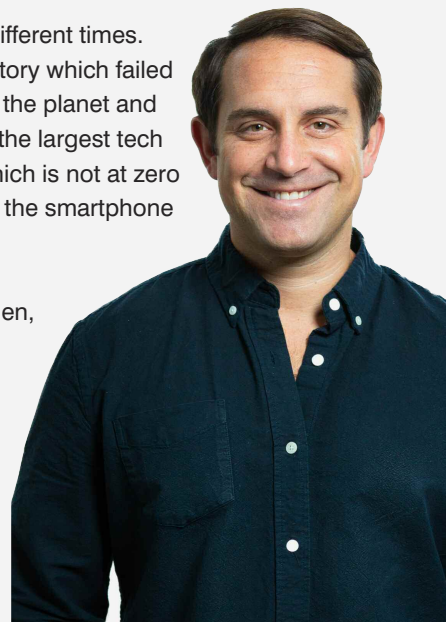


Ronen Schwartzman: Interestingly, what you are describing is also true in Israel when we go back 15 or 20 years.

I guess the first generation of newborn entrepreneurs that built a company and sold it for 25, 50 or 80 million dollars, when they come back to their new startup company or new big idea then they want to grow the company into a few hundred millions of dollars before they are going to sell because of many reasons. Maybe that will happen in Canada as well at some point.

Matthew Leibowitz: Right, we are all evolving, and ecosystems and cultures evolve at different times. Admittedly, there have been some phenomenally successful Canadian companies in history which failed or lost massive market share. Nortel, at one point one of the biggest tech companies on the planet and now, it's zero. At a time, Corel was the biggest software company in Canada and one of the largest tech companies on the planet. And lastly, of course, one of the most famous is BlackBerry which is not at zero as it's trying to resuscitate itself. But, at one time it was unequivocally the world leader in the smartphone space.

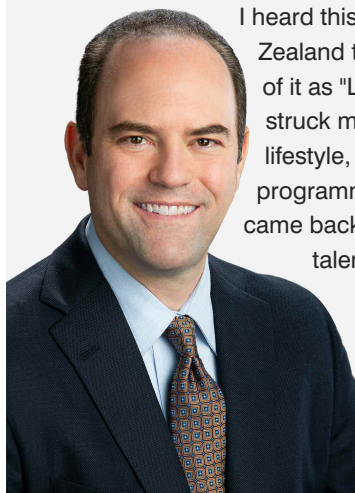
So, some Canadian companies came out of nowhere and became global players, but then, they went in the other direction. As a result, the current generation of Canadian entrepreneurs as well as the ecosystem at large that supports those entrepreneurs are very cognizant of that history. But, this mindset is changing. Having said that, our exits, with our fund structure, do not require billion dollar exits to make money. In fact, we can do phenomenally well these \$100m-ish exits or even smaller, from a MOIC, ROIC and IRR perspective.



Christopher Zook: This is interesting to learn about Canada's setup. I mentioned earlier how I was recently in New Zealand, where I had many meetings in a short period of time. When you ask a whole lot of different people the same question and you start hearing the same answer over, and over, and over again, it means that, either everybody is doing the same thing and it would make sense to be a contrarian. Or, number two, there's potentially a compelling theme developing. In this particular case, what is clear about New Zealand is that there are tons of angel investment capital, and there is a lot of late-stage technology investment capital but very little in the middle. I heard that from the people that were trying to take advantage of this from all different angles. Clearly, there is a gap and a need that people are trying to fill.

Using the industry terminology, there's a ton of seed and a little bit of Series A and then plenty of Series D, E, and pre-IPO, but

really nothing in between. New Zealand is generally too small for the big Australian funds to come over and get involved, because the check size is just not big enough, and certainly, Silicon Valley is not going to come over and do it. Yet the quality of the technology teams there is very solid. So, the isolated location of New Zealand may potentially provide an interesting opportunity to profit from filling that gap.



I heard this concept over and over, which is why I asked the question as to what the real value of New Zealand technology is. I would not have thought of New Zealand as a technology hotbed but rather think of it as "Lord of the Rings" and gorgeous, and it is, for those who have not been there. But what also struck me is that there are a lot of people that are very skilled that choose to live there because of the lifestyle, the safety, the cleanliness, the quality of life, all the activities, etc. But they are great coders, great programmers, and they are really, really good at what they do. So, they are either natives or those that came back, or they chose to move there for the lifestyle. Therefore, much of the VC community is taking this talent, with strong skills, and effectively exporting it to the rest of the world.

So, I was wondering about the lay of the land in Canada. Do you have a lot of angel and you have a lot of late and not much in the middle, or do you have a lot in the middle and not much angel?

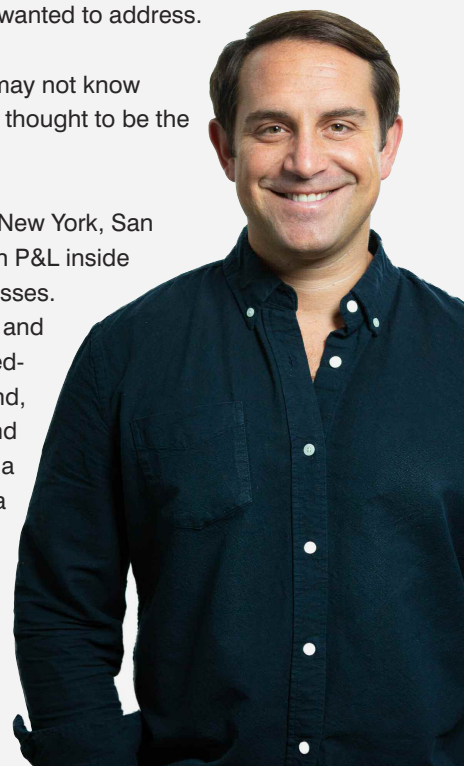
Matthew Leibowitz: I can give you a few different answers to that. Part of my initial investment thesis was that Canada has the large institutional investors, early-stage VCs, and angels, and nobody in the middle market, and so this is why we have been doing this sort of extension and series B rounds.

That has changed a little in recent times. When we launched the fund structure five and a half years ago, we were pretty much the only game in town for doing Series A and Series B, give or take. And now, there are a few others, which I think is great, and we collaborate with them. But it's still nowhere where it needs to be. *The Canadian Venture Capital Association, where I am a Board member, published the data that there's still a dearth of CA\$1.5bn-2bn of VC money in Canada per annum.* That's a lot of money. So, there is still a huge gap and opportunity, and that was really what I wanted to address.

But on the angel side, part of the problem is that they don't have access to deals and may not know where to start. I was on a conference panel in Montreal and someone asked me what I thought to be the big problems in Canadian venture and in the Canadian tech ecosystem?

To me, there are two things that come to mind. First, we don't have a lot of people like New York, San Francisco or Houston, where you have an individual who has built or who has run \$2bn P&L inside of an Oracle, Dell or any of the big tech companies where they have established processes. Those types of people are missing, we don't have many executives that could come in and help Canadian tech companies scale from say 5 - 30 million in revenue to multi-hundred-million-dollar revenue. But there are also a lot of expat Canadians, and like New Zealand, we are trying to sell them on moving back to Canada as a great place to live for you and your family. And so, the Canadian government and VCs – people like me – have spent a lot of time focusing on these type of initiatives to help move that talent either to Canada and/or back to Canada.

The other Achilles heel is angel money. It's not as though there aren't a lot of wealthy people in Toronto or Canada, quite the opposite. Toronto is one of the wealthiest cities on the planet. There are 20 to 30 billionaires living in the city alone. However, most of



those billionaires derived their wealth from the resource-based economy, which is a large part of our economy. Many have made their money by either making buildings, or digging holes in the ground in Alberta, or pipelines and there hasn't been accessible to VC or the tech ecosystem. Part of our role is to try to inform these people on how to re-orientate some of their wealth into the innovation sector.

It's not that they are not interested per se, but more that it is not obvious how to access the Canada tech ecosystem or VC world. Of course, the sector is small, so they just don't know where to go. We don't have a Sequoia or HIG in Canada.

I think access is the Achilles heel, but the good news in Canada is that the VC ecosystem has matured, even in the last four to five years. It's totally different now compared to six years ago. I'm excited about the Canadian VC sector as a member of the CVCA, where I wave the Canadian flag, but also as someone who likes to co-invest with like-minded individuals and smart people in support of the Canadian tech ecosystem. Of course, as an industry, there is room to grow. To give you some context, last year the VCs in New York City alone invested more dollars than all of Canada combined.

Matthias Knab

Anushree, you are working as Head of Operational Due Diligence, I wonder if you can share some insights you are seeing from your perspective?

Anushree Mohta:

Based on my career dealing with various asset classes, particularly during my time in private banking I would agree that there has been an increase in the investor demand for private equity type products. Given the high growth multiples in emerging markets, this has been an attractive area for private equity investments. I expect this trend to continue in the coming years.

Christopher Zook:

Having worked in operational due diligence on hedge funds and now moving over private equity, what's the biggest challenge that you see, or the things that you have the most trouble getting comfortable within private equity compared to maybe hedge funds?

Anushree Mohta:

Based on my career dealing with various asset classes, particularly during my time in private banking I would agree that there has been an increase in the investor demand for private equity type products. Given the high growth multiples in emerging markets, this has been an attractive area for private equity investments. I expect this trend to continue in the coming years.

Ronen Schwartzman:

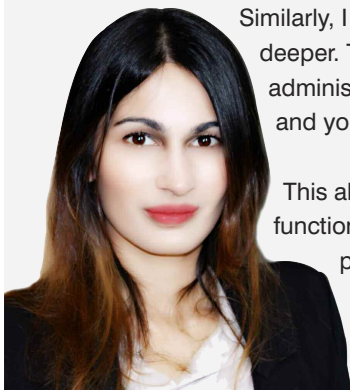
Just waiting for a fraud to happen.

Matthias Knab

Some people in the industry think that private equity is now where hedge funds used to be 10 years ago, kind of around the time of Madoff or just post Madoff.

Anushree Mohta: Exactly.

I've had to experiences of sending a PE fund an ODD request and they came back to me "What is ODD?", which would never happen with a hedge fund in this day and age. But in general, they have come a long way. *Some of the bigger private equity firms are getting an external administrator, but the vast majority do not have administrators, which I personally – and let me make the point again that I don't talk on behalf of Siguler Guff or any institution – don't consider a big risk as long as they have adequate internal controls.*



Similarly, I am also not as concerned about **evaluations**, but when it comes to AML risk, I do look a little bit deeper. To address **AML risk** is the one benefit of having a transfer agent or this type of service administrator. But a lot of PE funds don't have those types of functions and view them as a major benefit, and you need to spend a lot of time educating them on the various risks of not having an AML function.

This also applies to venture cap which may not be required to be registered or have a compliance function at all from a regulatory perspective, but they could definitely still get dinged from a lot of perspectives. So, right, Christopher, I do spend a lot more time educating the smaller private equity firms on those risks than I had to do with hedge funds.

Christopher Zook:

Do you see a particular threshold of AUM where you really see the professionalism and the depth of a PE firm ratcheting up, like from \$200m or \$500m?

Anushree Mohta: Unfortunately, not. I think it's more of a mindset. Certain firms stick to legacy processes and procedures because it's the 'way it's always been done'. And you will find small start-up shops adopt best practice controls whenever they are economically viable.

I think a lot of change is also investor driven, so a firm marketing to more institutional investors will be forced to adopt certain controls as opposed to one with more high net worth investors.



Ronen Schwartzman:

What about cash movement policies?

Anushree Mohta:

Cash control policy is an area I spend a large amount of time on. Understanding the signatory and approval process is critical to private equity due diligence. Unfortunately, in this day and age we need to trust but verify, so checking that the manager's policies are actually implemented and binding with the banks and custodians through independent verifications is also an important step.

Ronen Schwartzman:

Like dual signatures and things like that?

Anushree Mohta: Ideally, dual signatory, yes. However, if the manager is a start-up with two or three employees, this can be tough to implement. In those instances, managers may allow small expense payments with a single signatory and establish a threshold after which dual signatories are mandatory.

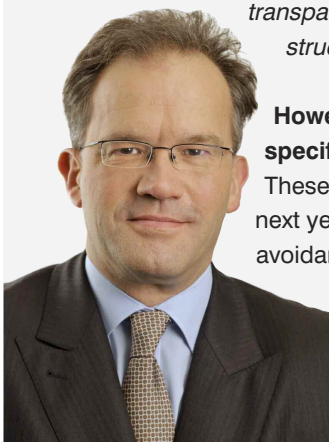
Christopher Zook: And also, an administrator doesn't necessarily stop that from happening, no?

Anushree Mohta: That's true, I have seen in hedge world that the administrator is authorized to release, but they do not take any liability for fraudulent transactions.

Christopher Zook: Exactly.

Anushree Mohta: So how liable are they? They are there as part of the process, but if they are not actually verifying anything prior to just releasing a cash transfer, if it's just say a junior person at the administrator just clicking a button, what comfort are you getting from that?

Robert Welzel: Allow me to add a few comments related to tax risks. *In Europe, the fiscal authorities are implementing transparency regulations and quite strict anti-avoidance tax legislations in order to capture the tax structuring taking place in the private equity sphere.*



However, it is my impression that the private equity industry is still quite reluctant to evaluate its specific tax risk profile. The current structuring should provide for after-tax benefits for the investors. These concepts are endangered. New tax transparency concepts such as DAC6, will be enacted latest next year even with a retroactively three year reporting period. Furthermore the very stringent anti-avoidance tax directive will be implemented soon, too.

This affects all European investments and European investors. Addressing adequately the inherent tax structuring risks in Europe may be an issue for many firms in the global PE industry.

Christopher Zook: Plenty of tax issues coming down the pipe?

Robert Welzel: Yes, both on national and international level. E.g. it is an noteworthy remark that part of the German CFC/PFIC concept is now introduced in US tax legislation, too.

Matthias Knab Anushree, you already mentioned a few relevant aspects regarding operational due diligence in PE, what else is important?

Anushree Mohta: I personally structure my PE due diligence starting off with something that's common across all asset classes, so by looking at **business risk**. The risk of the organization, HR, succession planning, and then spending the bulk of my time on operational controls, wire transfers, related party payments, any different types of servicing companies that might be providing fee-based services to the funds.

Disclosures in the private equity world and regulatory risk have gotten better. It is less common to see related parties charging fees that are not disclosed within the financial statements or within the operating documents, but it still needs a little bit of digging into.

Obviously, valuation risk needs to be looked at, also from a regulatory perspective. Cybersecurity is always a hot topic as well as compliance and regulatory demands, so a firm's ability more than anything else to respond to the regulatory demands, because most of the private equity funds I personally see do not have a dedicated Chief Compliance Officer or even dedicated Compliance personnel in general.

So, those are some of the topics that I focus on. Let me also add that due diligence is then also very dependent on the particular risks that you might identify. For that, I would spend a good one or two weeks just going through the documentation and figuring out what the risks would be.



Barry Seeman: I mentioned Leaseum Partners in my introduction, a new commercial real estate fund, which is going to be tapping the talents of Michael Chetrit of the Chetrit organization, a large family office in the United States that specializes in commercial real estate assets.

So, similar to Matthew with Plazacorp, we are tapping the talent of the family office. You might wonder, *"Why would a family office want to open itself up to third-party asset management?"* So, as this is a new foray into a new area of management and fiduciary responsibility for them, you immediately get into **governance issues such as of conflict of interest**, as in, will there be some cherry picking being done by the family office versus the fund, and so forth.

In our case, as we sat down and we started putting together the structure, we began to immediately tackle those issues, starting with the assembly of a very strong team that includes the former head of alternatives and real estate from Aviva, David Dahan, who is our Chief Investment Officer and helping to implement the institutional oversight onto the whole investment process.

Leaseum has put in place a substantial amount of checks and balances, on everything from money transfers through compliance.

David Dahan is overseeing the investment committee, so no investment or divestiture is happening as a consequence of just one person's decision that could impact the fund. Investments and controls will be implemented by the team, so there are checks and balances throughout the process.

But the fascinating thing is, as much as the marketplace is attracted to this asset class, we consistently see similar same questions in a set up like ours, such as, "Am I really getting access to the family? Can I do side-by-side investing? Are all of these things possible?" And the answer is, yes, under the right circumstances and with the right structure, you can make that happen, but it's precarious as—



Christopher Zook:

Can I ask you a question? There are parts of the country where valuations are very, very tight. Are there areas of the country that you see as more attractive or more reasonable in terms of real estate?

Barry Seeman: You are asking a great question because, of course, we are investing in one of those tight markets. The fund will be investing in New York City and mainly, what I would call, core-plus, with very little value added, focused upon office space, with some multi-family, but mostly office space.

Leaseum believes it can achieve target returns in this tight market because the Chetrit family, like many of the other real-estate families, are often shown off-market transactions which might not necessarily get to the large asset managers of the world. Many institutional investors are comfortable with the return profiles of these large managers because they believe they can give up some carry in return for a brand name and significant investment infrastructure. Leaseum believes that the incremental returns come from the sort of upside trades that a unique family office can realize, and which are going being made possible through this fund.

Coming back to the valuation question, for example, a large property that's going to be looked at by all the top real estate funds won't be that attractive as an investment for Leaseum. You will probably not be able to achieve the cap rate targets that you are really looking for. But, the off-market types of deals that we are looking at today are very attractive.



Ronen Schwartzman:

Is that true still even after Amazon was told goodbye from New York?

Barry Seeman: Absolutely! In fact, the number of deals became more attractive because of the exit of Amazon, as things were getting bid up right in front of that announcement and the market became very tight.

Not connected to the Amazon departure but also a good example in the public domain is that Michael Chetrit spearheaded the purchase of 850 3rd Avenue from a Chinese conglomerate, HNA Group. And this is the type of deal that makes sense in today's market, although not exactly for the fund, because that was a \$450m transaction whereas the fund is probably going to target more \$25m to \$100m transactions.



Christopher Zook:

Equity check or transactions?

Barry Seeman:

Transactions, with probably a 60 to 70 LTV.

Barry Seeman: Right, let's look at the FinTech aspect. The partners of Leaseum originally wanted their offering to be a **security token**, which I would argue was doable in 2017, but today, it's more of a question mark. A tremendous number of FinTechs are chasing and promoting blockchain technology and digital securities. As far as I am concerned, it's often a solution looking for a problem, but it has the potential to be truly revolutionary.

The security token space is still finding its footing at this time. I even would not call it a security token but a digital share at the end of the day. And how it creates value is also evolving in the marketplace. *There has been so much talk of adding liquidity to another-wise illiquid market such as real estate, but the reality is that so far the marketplace for trading the tokens has not developed the way that many expected or wanted. As more investors adopt this form of asset allocation, the market dynamics will dramatically improve.*



Ronen Schwartzman: I think the whole tokenization frenzy and deals kind of disappeared, and maybe rightfully so. Possibly Bitcoin will survive and maybe starting to make a comeback.

But for us as investors, to invest in a token of a private real estate company? What kind of liquidity you are going to get? What's the exit? I really don't know who would have invested in something like this?

So, Barry, I think you are probably doing the right thing of postponing it for now.



Barry Seeman:

We are not necessarily postponing, but rather offering flexibility that should be attractive to both traditional investors and those embracing the digital security space. Investors will have feeders that can handle either form of investment.

Robert Welzel: *Blockchain Technology (DLT or Distributed Ledger Technology) is destined to revolutionize the financial services industry. Nowhere is this transformation more apparent than within the asset management sector. Blockchain technology will also be shaping the tax servicing and compliance in the future.*

WTS is currently piloting new Blockchain-based tax services to accelerate our clients' efforts to advance to such services infrastructure. Given the pioneering work, **WTS is ready to embed tax compliance functions within smart contracts** and to adopt its business propositions within the emergent Blockchain driven ecosystems. WTS uses smart contracts to automate, simplify and streamline core tax servicing processes at reduced cost.





Barry Seeman: Anushree, going back to **succession planning**, which you said you are also looking at when doing operational due diligence on a firm.

I was wondering, how much of that done by the research team and what is done by the operational due diligence team?

And, looking at succession plans, while of course, every firm is different, but as a whole, do you see firms getting better in how they address succession or is this still too often ignored?

Anushree Mohta:

It's more often than not a combination of the research team with the operational due diligence team, so looking at succession at an asset manager is one of the topics where we actually work together. It is important to understand the depth of the team below the founders and the principals. *What are the key-person provisions within the documents? Is the investment period halted or suspended until they find someone to replace a key person?* These are definitely very pertinent questions both for the research and the diligence teamwork.

Christopher Zook:

Do most of the firms give you visibility to the actual splits with those junior partners and the related economics? Like, how are they actually building and handcuffing those folks to keep a team together?

Anushree Mohta:

Absolutely, I delve into the economics, because that is exactly the biggest alignment for the junior personnel to actually take those leadership roles. In some instances, I would look at the partnership agreement as well to understand buy out mechanisms, sunset clauses etc.

Christopher Zook:

Christopher Zook: As long as you write a big enough check, they'll let you look at it...

[laughter]

Ronen Schwartzman:

On the other hand, this is also a sort of argument to look at some smaller, new funds because the risks of somebody retiring in the middle of the investment period is somewhat lower because they are still trying to build up and expand.

Barry Seeman: Out of curiosity, if you come across a platform that has robust succession planning, do you see that impacting in one form or another the decision making as well?

Oftentimes, we are looking at companies where one founder is sort of the brainchild behind everything. With a robust, formulated succession plan in place, do you see the decision-making process potentially shifting from that person to a committee as a consequence?



Anushree Mohta:

Not particularly, but also goes back to what you were saying in terms of decision-making structures and committee-based decision-making structures at your own firm as opposed to a single person. So, absolutely, these are aspects to consider.



Barry Seeman: From the perspective of the end investor in any discretionary asset management business, we sometimes have this debate about "**death by committee**" versus "**death by a gunslinger**", and the question of whether or not, performance is more persistent if you have one strong decision-maker, as opposed to getting watered down by lots of different folks in a committee.

Are most of the firms that you and/or your peers from the professional investor side chose to invest in reveal a preference for either committee or the solo structure, or where does the line fall?

Anushree Mohta:

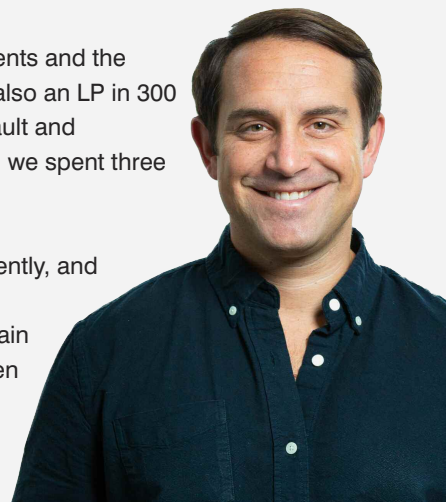
I can't really talk for our investment teams and their preferences, but I do agree with you that there is a fine line and a question of balances that you need to understand. Funds could be giving excellent returns, but then, their structure might not be sustainable. So, we need to marry the two to obtain an attractive and stable investment in the long run.

Matthew Leibowitz: I can add a bit to this discussion.

In November 2018, I graduated from the **GP Academy** in partnership with the **Kauffman Fellowship Program**, founded originally in Kansas by Ewing Kauffman who donated a lot of money to create the Kauffman Institute, which has now become arguably the world's foremost think tank on venture capital. Already 20-something years ago, they created this Kauffman Fellowship Program for GPs of venture capital firms. It's a year and a half program with various modules scattered throughout North America where they bring in industry leaders. Each module is about three or four days every few months and is led by impressive industry titans.

I want to share the findings of one professor who analyzed all the shareholders' agreements and the cash-on-cash returns for one of the largest banks in the United States. The professor is also an LP in 300 venture capital funds. This professor spent years of his career basically going into the vault and analyzing all the shareholders' agreements, including the voting structure. In our course, we spent three days just on voting structures.

And the one way that I could surmise the findings for you, is that every firm does it differently, and there's no right answer. You could have five firms with that key person, and they have done great, and then you can have another five firms with a similar structure of one captain at the helm, and they have all done terribly. And then, you have other firms that have been voting by committee, everyone gets a vote, and you'll see the same thing there.



Ronen Schwartzman: Of course! And this is why investing is also art and not just science. But you want to know where you're getting yourself in, this is why we have to understand these questions.

Matthew Leibowitz: Correct. And, to Barry's question, the only right answer is that each firm needs to develop a system that makes sense for them. For a VC geek like me, this was a fascinating study.

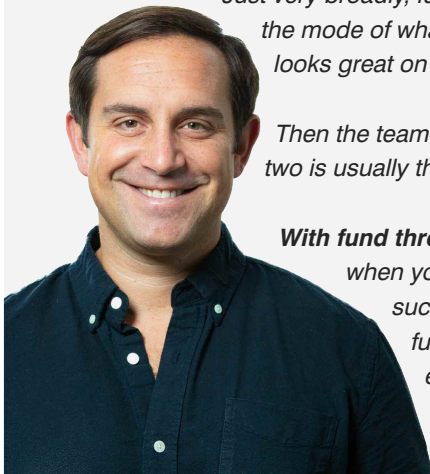
Ronen Schwartzman: Was there any data about the size of funds?

Matthew Leibowitz: Absolutely. They had all of that data.

Just very broadly, fund one of a firm tends to be okay or typically pretty good. At that time, the team is still in the mode of what I call selling the dream versus selling reality. So, all investments are still unrealized, it looks great on paper, everyone is excited, and the team is working well together.

Then the team goes out and raises fund two, that is typically a substantially bigger fund, and that fund two is usually the winner.

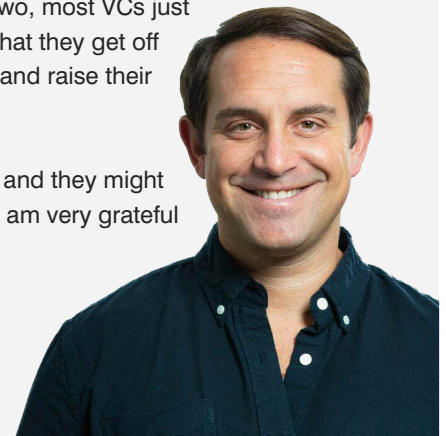
With fund three, the wheels can start to fall off, and fund four then often is a disaster. Fund four is when you can see partners starting to fight and then retire and leave, and that's where the succession question becomes really important. You may actually also see some of that by fund three, according to the data that he analyzed from the typical venture capital private equity structures.



Barry Seeman: I wonder if consultants are telling their clients that.

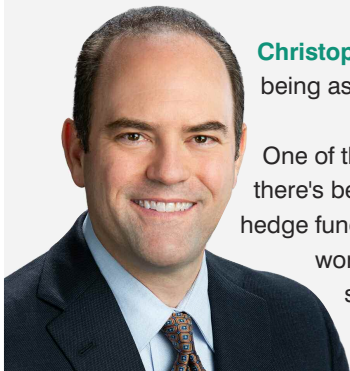
Matthew Leibowitz: In fact, there was a whole lecture where they brought in this woman – I forgot her name now, she's a professor at Harvard and, on the side, she has a consulting firm where she consults to partners on how to basically deal with their disputes inside of their partnerships. To cut it short, when it comes to fund one and two, most VCs just want to get out of the gate quickly, so they may just work a bit on the standardized docs that they get off the shelf from their lawyers but usually don't put too much thought into it, and just go out and raise their fund.

But then, by fund three, things can start to go a bit awry. Several questions can come up, and they might start thinking on how to iterate things on the fund structure. It was really fascinating, and I am very grateful that I participated in that program because it provided me with a lot of insights.



Ronen Schwartzman: I think it's time to talk about fees in our industry.

Matthew Leibowitz: Don't look at me... we don't charge fees.



Christopher Zook: Same here, we don't charge them either. Of course, we charge Carry, but we like being as aligned as possible with our partners.

One of the things that I'd be curious about to hear about from the rest of the folks around the table is that there's been this talk for the last 5 to 10 years about the fee compression that has been happening in the hedge fund world, which has been real, was going to drift over into the private equity world/venture capital world. Are people seeing that? Are people seeing fees coming down anywhere? Everybody's shaking their head, so no.

Anushree Mohta: No.

Ronen Schwartzman: Not directly, so we don't see a decline in fees in PE/VC – except for Matthew telling us he charges zero management fee. It still accounts for 2% management or even 2.5% management fee, which I think is outrageous. But the way we see a bit of discount is through co-investing opportunities. So, you can bring extra capital and you do not get charged. That's a compromise or one step into the right direction.

Maybe the real pressure on fees in PE should come from the big consultants or the big pension funds. But then, they don't pay 2% but have their side letter or separate arrangement they might have with a fund, while for everybody else sees fees of 2 and 20.



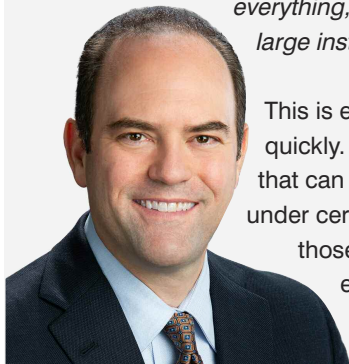
Christopher Zook: Here is an interesting story. I cannot tell you the identity of the firm, just because they would not want me to, but as an example, one of the firms that we are very involved in has been raising a mega fund. So that it doesn't identify which firm it is, let's just assume it's a \$15bn fund. The thing is that they have \$40bn of demand. **When you have \$40bn demand for a \$15bn fund, you do not cut fees.**

You are not going to gouge people because that's not good for your business, but you're also not going to give a lot. But I agree with Ronen that fee reductions are happening on the co-investment side.

The industry has pretty much gone away entirely from not offsetting fees with revenue from other sources. Board seats, the advisory fees, transaction fees, etc. those are all now pretty much being reimbursed against management fees. That change occurred over the last 15 years. So, that part has been done. I do think that preferred returns are potentially going to have some pressure on them, and I have seen a lot more nines and tens lately than I have historically. This may be a way to emphasize that the firm won't cut the fee necessarily, but it will incentivize them to perform better.

The interesting thing about the **co-invest side** is that everybody says they want co-invests, but when you talk to the sponsors, they'll say, *"Sure, they say they want to co-invest, but they really don't want to co-invest, or, they can't co-invest. In many cases, they just can't move fast enough. They can't get their arms around it, or they don't have any in-house expertise."*

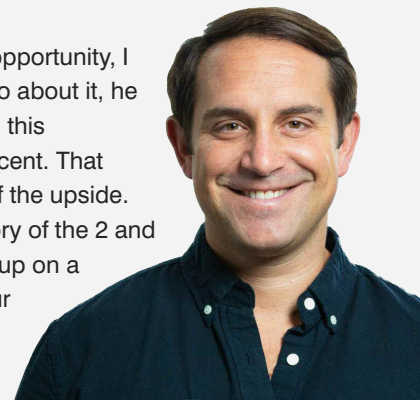
I was on a conference panel with an entire group of co-investors, and we just asked around the room how people did their co-investments? And one of the most interesting things was that most people have done it in one or two ways. *Either, they did everything, so they took each investment just as a way to reduce fees, which is a great strategy for a very large institution. Or they did it very tactically, but they had the team in-house to be able to do the analysis.*



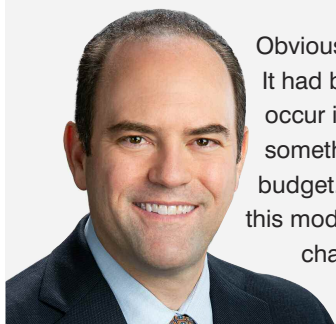
This is exactly what we believe is a huge edge for us and others that can write a big check and do it very quickly. We did a \$60mm co-invest in nine days. There are virtually only a handful of institutional investors that can get something like that done in nine days. It's not something we would always be able to do but under certain circumstances, we could do that. That is something that I think is going to be an edge for those that have that infrastructure in place to be able to take advantage of it, to drive down their own economic costs and ultimately, increase their returns as well.

Matthew Leibowitz: Does anyone know **the history of the 2 and 20?** There's this incredible documentary called, "Something Ventured", you may be able to watch it on Netflix or YouTube. It's the history of venture capital where they also interviewed someone called Arthur Rock who in around 1962 or '63 created the first venture capital fund or invented the first pool of capital to invest in a spinout of Hewlett Packard in Silicon Valley.

Arthur Rock was an investment banker in Manhattan, and when he pooled capital for this opportunity, I think it was a few million, which at the time was a lot of money. So, as he thought how to go about it, he said to himself, "Well, I've got an office here and I've been doing all of this work and I found this company. But I've got to pay the rent here in New York, so, I think, I should charge two percent. That sounds about right, and, I'm doing all this work here, so maybe I should also get a piece of the upside. Well, I'm going to charge 20 percent of the upside and take the profits." So, this is the history of the 2 and 20 fee model in venture capital – it's not based on anything except for Arthur Rock waking up on a Tuesday morning in the 1960s and coming up with it, according to this documentary. Arthur Rock later named his firm Venrock.



Christopher Zook: I've heard something similar to that, it really comes down to some arbitrary decisions. Your fee model, Matthew, reminds me of what I call the Citadel model, where Ken Griffin and the folks at Citadel historically didn't charge a traditional fee, but rather passed through expenses, based on their operational budget, which they made transparent to their partners. Investors knew that they were not paying a management fee, but they were still covering the overhead from operations and the people.



Obviously, there are pros and cons to that, and in some cases, this might be less transparent than others. It had been rumored in the industry for the last 15 years or so that a similar development would potentially occur in private equity. I haven't seen your firm before today, but I do know a couple of other firms that do something very similar where they have the budget that's approved and that the LPAC approves the budget. We are investing with a firm here in New York that does it that way. It will be interesting to see if this model becomes more popular. That said, as long as the private equity firms aren't forced to make changes by their investors, there is less likelihood that we will see an industry-wide shift.

Ronen Schwartzman:

Barry, you mentioned hedge funds, just because a fund may charge zero management fee, it doesn't mean it's cheaper.

Barry Seeman:

Correct.

Ronen Schwartzman: *There are certain large multi-manager funds that do not charge management fees but will charge a pass-through fee instead. These can get up to 8% per year – I mean, that's insane. You will be better off paying two and 20 than 8% of pass-throughs. But people say "Oh, zero management, I love it." But they don't really know what they are getting into.*

The other way to try to save on fees is by **seeding a manager**. If as a seeder you help the manager to start his business than you should be compensated for taking this risk. This can come in the form of paying lower fees and get a revenue share from the performance of the fund so your interests are aligned with the manager.



Anushree Mohta: With the fee pressures and tough capital raising environments for smaller managers, **business viability** then is becoming a huge concern, given that they may not be able to charge the fees to raise the capital.

At the same time, we would have to assess that they could actually sustain their operations within the next three to five years. *Personally, I would rather pay the fees and ensure that the business is going to be viable over the long-term than having to deal with the outlook of a potentially good manager not making it over the longer term.*

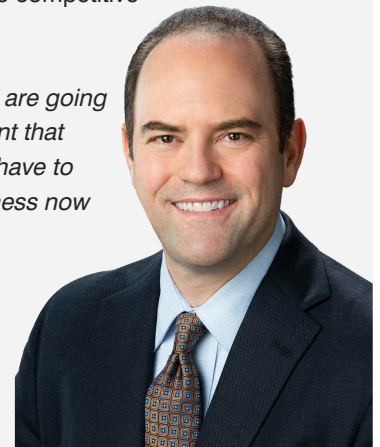


Christopher Zook: One of the things that several folks in Texas had been very vocal about, and TRS in particular, is the 2 or 20 as opposed to the 2 and 20. But, 2 or 20, or whatever that right numbers are – one and a half and 15 or whatever – against the specific benchmark.

That is something that we saw a lot of momentum on and a lot of the startup and smaller managers adapted it because they know they need to have enough fee income to pay their people, but they wanted to have a more competitive fee to offer investors.

All firms need to have is some visibility to how they are going to pay their team. Otherwise, they are going to have so much stress and they will never be successful, or they will not be able to get the talent that they need. At the same time, they also recognize, especially in the hedge fund world, that they have to outperform otherwise, they will just get replaced by an index fund. So, they are going into business now more with that mindset of the 1.5 or 20 over the benchmark as a way to do that.

Regardless of how it is structured it still has the overall effect of fee compression. This is definitely happening, especially with the newer managers, and something we will likely see more of.



Ronen Schwartzman: I agree with you. Albourne promoted the model of either 1 or 30, whatever the highest one, or the founders' share class, which can cover 1 and 10, or 1.5 and 15, whatever it is.



But sometimes, we are taking a bigger risk in seeding a manager when he is just starting, and then we should be compensated by paying lower fees. There are also **tiered fees**, so you'll come in the early days of the fund when assets are still low and will pay a management fee of two percent, but as the managers grow the AUM of the fund, the fees will come down, so this is another way to structure it. There are definitely changes going on in the industry, but a lot of that is also dictated by how challenged a manager is to raise assets, because, as Christopher pointed out, if you have a \$15bn fund and \$40bn demand then, you're not lowering your fees.

Matthias Knab

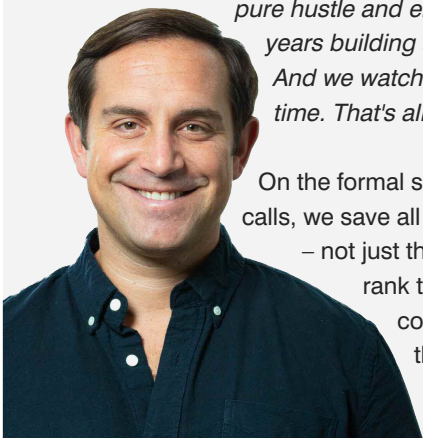
Let's look at deal flow and manager selection. How do you go about that?

Ronen Schwartzman: We are a single-family office, and deal flow comes from several places. One, of course, is our network of other family single-family offices, so we get together and talk to each other basically all the time. A few years ago, I also started a small informal group of eight of us that meet every two to three months and share our knowledge. I went to the Wharton Business School for my MBA and we have a Wharton Hedge Fund Network group that meets 3-4 times a year and has also been a good place to find ideas and talented managers.

Quality conferences and industry events are other sources, together with the usual industry chatter of like who is leaving the industry, who is spinning out from where to launch on their own, and some quality media.



Matthew Leibowitz: Deal flow is where I like to spend most of my time, and in my work, I get this question all the time from people. And my guttural response is always the same: it's a lot of breakfasts, coffees, lunches, coffees, dinners, and drinks. It's pure hustle and elbow grease – that's exclusively how you get deal flow in the VC world. We typically spend years building a relationship with a CEO, or a management team before we write a check into a company. And we watch them perform and how they manage to navigate their business over extended periods of time. That's all part of the work we do on the "informal side" of it.

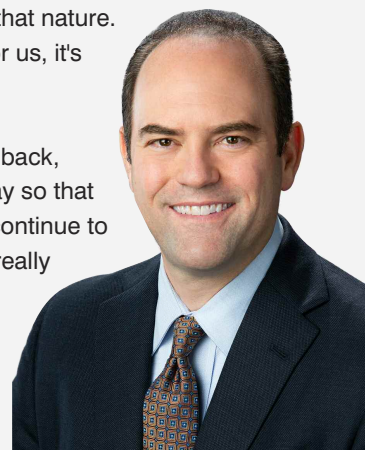


On the formal side, we've built a database, a comprehensive CRM that is managed daily. We track all our calls, we save all of the data, we built a data science model to analyze all of the companies that we monitor – not just those we invest in, but all the companies that send us their information, and we score and rank them. We built that over the last few years and think it's pretty cool. We have about 18,000 companies in this CRM where we track all our calls. That's on the more formal side of it, and then as I mentioned we as well keep in touch with them on a real personal basis.

Christopher Zook: There's no substitute for hustle, you got to work, and you need to be willing to turn over rocks. *I'm sure you'd agree with me that deal flow itself is actually not the problem, the issue is more like trying to figure out which of the deals we are going to spend time on. It's about the narrowing of the funnel.*

For us, the first step is always keeping in mind what we are as an organization, which is how we are very thematic. Last year, we looked at 650 potential investments. We were able to eliminate a whole host of them, just because they were not really investable, they were not viable to us. Then you can eliminate a whole host of them because they were completely contrary to what we wanted to look at that particular time – such as a crowded, expensive space, things of that nature. And then, as I mentioned, we will overlay our themes. When something doesn't meet a theme for us, it's going to be very difficult for us to get comfortable enough to actually make an investment.

We will invest when the wind is in our face, but we really prefer to invest when the wind is at our back, just because we'd like to have more margin for error. There is more room for things to go our way so that even if we didn't make the exact right decision, we could still do well. Those themes help us to continue to narrow that funnel down to allow us then to spend a lot more quality time on the things that we really believe are potential investments that we will make. And from there, it's just a matter of rolling your sleeves up and doing the homework and making sure you get comfortable with the investments themselves. So, our thematic overlay really helps us minimize a lot of wasted time.



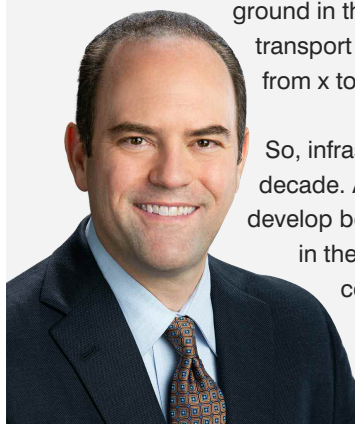
Ronen Schwartzman:

Could you maybe mention again which themes you guys are focused on, where you find the tailwind?

Christopher Zook: So, the biggest theme for us is the growth of private equity as an asset class. The second is the transportation revolution – you can call it ride-sharing, but for us, the theme goes much beyond that. We have participated primarily through Lyft and Didi, which is China's ride-sharing company. Many investors don't realize that Didi owns stakes in many other ride-sharing enterprises. They own a big piece of Uber and Lyft, but they also own stakes in providers in Europe, Egypt, and India, as well as Grab in Southeast Asia and 99 in Brazil – they basically, have the entire globe covered, and thus you kind of get the entire ecosystem with one investment. We also made a direct investment in Grab because we like what they are doing in Southeast Asia.

Beyond that, we are still very invested in the mid-stream space around shale basins. Being in Houston, we know most of the major players in the energy world. And what I can tell you is that there is still a big mismatch of what's coming out of the ground in these various locations compared to the infrastructure around those places to gather, process, and transport it. I'm not talking about long haul pipelines like MLPs but about, for instance, taking the viscosity from x to y so that it can actually go through the pipeline. That has to be done close to the wellhead.

So, infrastructure opportunities very close to the wellhead have been very good to us for more than a decade. And then lastly, we are also looking at the interplay or the massive gaps that are beginning to develop between emerging markets, international valuations, and the more developed markets, particularly in the US. That's one of the reasons why I spent time in New Zealand and plan to be on the African continent as well, just trying to find out where assets are less expensive. We believe there will be a time when other regions will be a much better place to invest. So far, we haven't done a lot there, but we're doing our homework.





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