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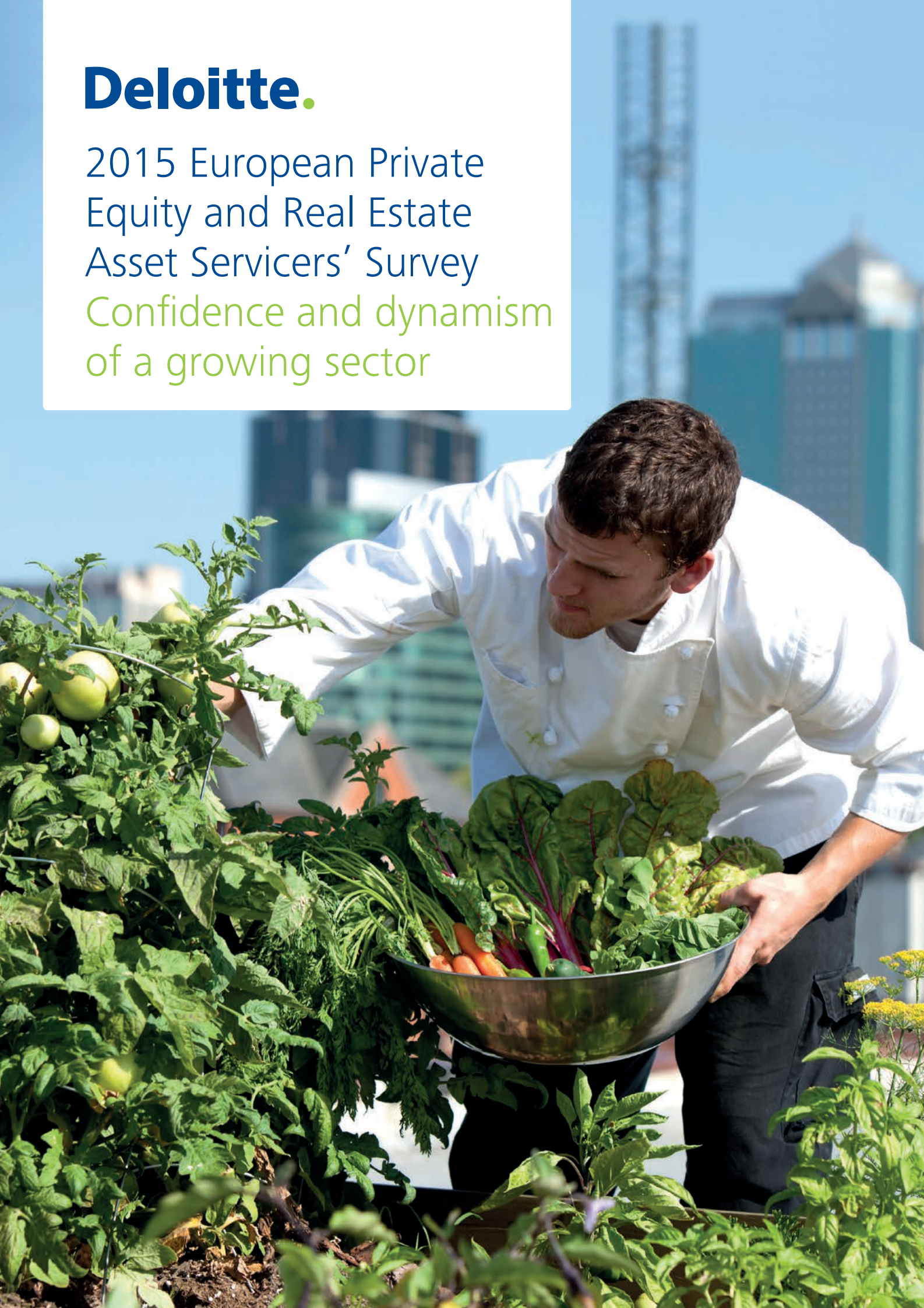
2015 European Private Equity and Real Estate Asset Servicers' Survey

Confidence and dynamism of a growing sector



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Executive summary

The Deloitte 2015 European Private Equity and Real Estate Asset Servicers' Survey highlights an industry in transformation, seeking to adapt its activities to reflect the asset management industry's increasingly global context.

In the light of their expanding client base both in terms of investor type and country of origin, asset managers have diversified into new fund domiciles and strategies. Asset servicers are reacting by adapting their offer to increase the country coverage and, in the second step, the breadth of services offered to asset managers. This will help to encompass more middle office services as well as services increasing numbers of investment structures between the fund and the targets).

Asset servicers strongly believe that their business growth will be fueled mainly by new clients, while extending their activities with existing clients only comes second. This will put pressure on costs and increase the focus on the quality of services, and lead to fierce competition between established players and newcomers.

Furthermore, regulations, market initiatives and investor pressures on asset managers are having knock-on effects for asset servicers. These include AIFMD, investor reporting standards (i.e., INREV and ILPA) and accounting standards (i.e., IFRS 9 and IASB/FASB). For asset servicers to be in a position to develop and concentrate on value-added products–the only true differentiator in the current climate–it is of paramount importance that they invest in technology, and focus on operating models and organizational transformation.

Asset servicers are very positive and confident in the growth of the PE/RE industry, while also being aware of the significant challenges ahead of them for the next 12-24 months. Some asset servicers have already initiated internal measures to turn these challenges to their competitive advantage.

Introduction

In 2014, Deloitte Luxembourg launched its first private equity survey targeting Luxembourg asset servicers. Following the positive feedback and high level of participation, Deloitte decided to expand the 2015 survey to the real estate asset class on a pan-European basis.

From an asset services standpoint, the 2015 European Private Equity and Real Estate Survey is particularly interesting as it gives insights into current market trends such as:

- Asset servicers moving toward pan-European coverage via acquisitions or by opening new offices in PE/RE centers
- Convergence of service offerings between specialized PE/RE entities entering the depositary space thanks to AIFMD and mainstream banks starting to target the non-regulated PE/RE market

Our PE/RE market survey was conducted among PE/RE asset servicers, particularly those active in the pan-European market. It was primarily designed to foster an understanding of key areas of their business, their operations and their insights into business growth and development.

The aggregate asset size of the PE/RE asset servicers participating in the survey is approximately €197 billion in assets under management and €107 billion in assets under depositary management.

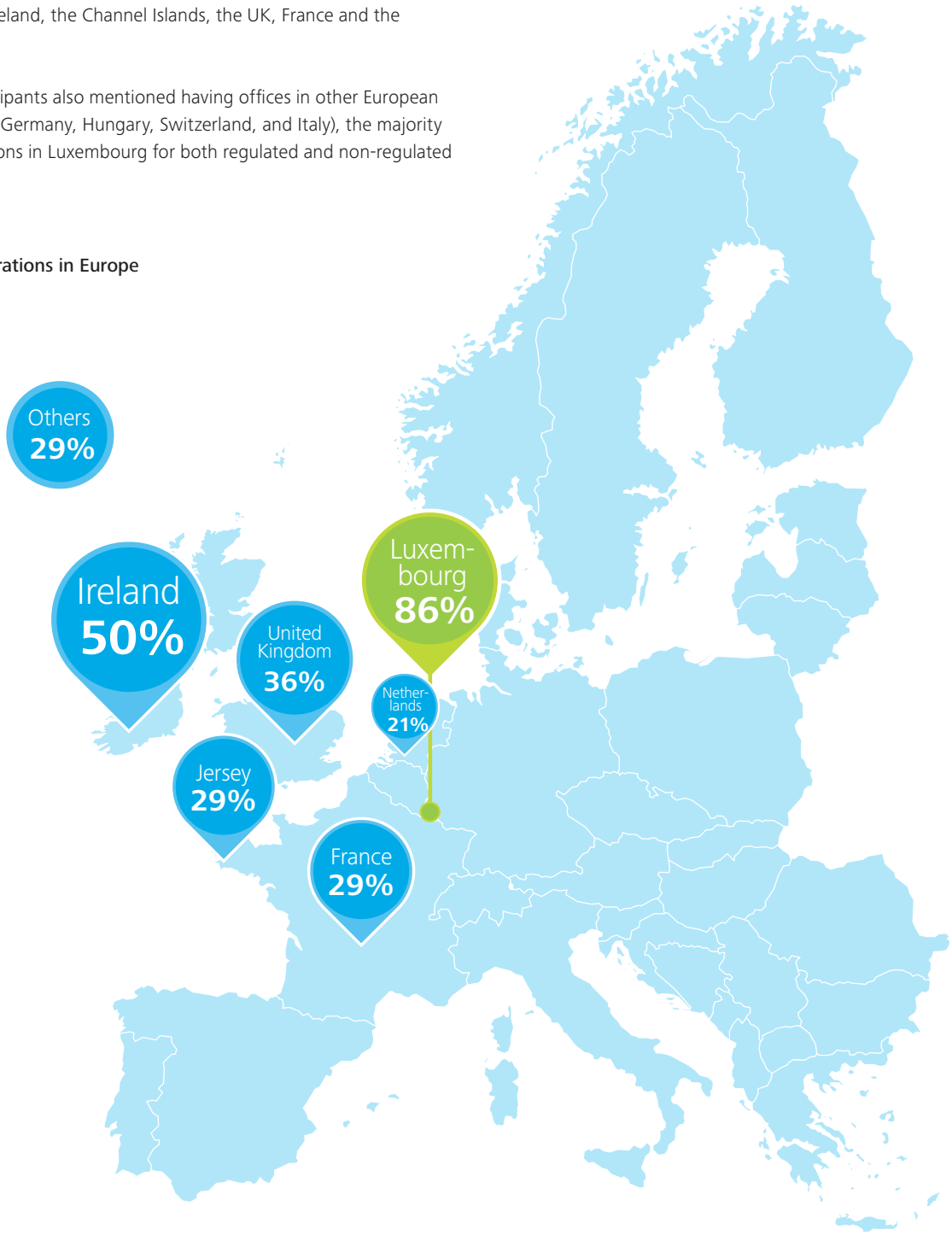
The survey respondents were a mix of mainstream banks and specialized service providers in the alternative asset classes. Where relevant, we have contrasted last year's results on the Luxembourg PE asset servicing industry with some of the responses received this year for the PE market.

General overview

Luxembourg is recognized as the main hub for pure pan-European PE and RE asset servicing activities thanks to its historical positioning for regulated private equity and real estate funds, as well as its non-regulated business. It is followed by Ireland, the Channel Islands, the UK, France and the Netherlands.

While some participants also mentioned having offices in other European countries (namely Germany, Hungary, Switzerland, and Italy), the majority base their operations in Luxembourg for both regulated and non-regulated funds.

Countries of operations in Europe

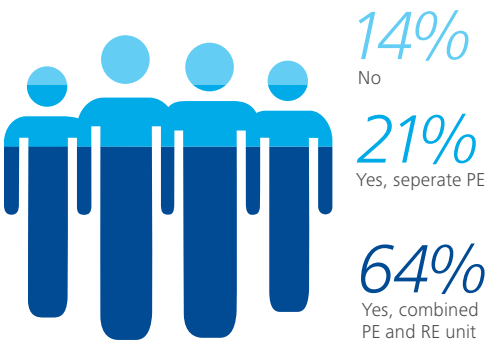


Overview of PE/RE organization and services

Most PE/RE asset servicers (over 80 percent of respondents) indicate that they have specialized PE and RE units within their organization. This proportion includes both separate PE and RE units and combined PE/RE units. Although 14 percent of survey respondents for PE and 17 percent for RE have no specialized units, they have an operating model with specialized PE and RE staff or teams, but only in some departments/functions rather than a desk centralizing all services. 52 percent of survey respondents for PE and 44 percent for RE maintain between 1 and 10 specialized FTEs per asset class.

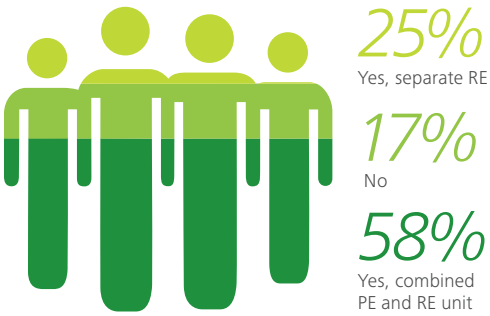
52 percent of the survey respondents for PE and 44 percent for RE maintain about 1 to 10 dedicated FTEs per asset class

Specialized Private Equity unit

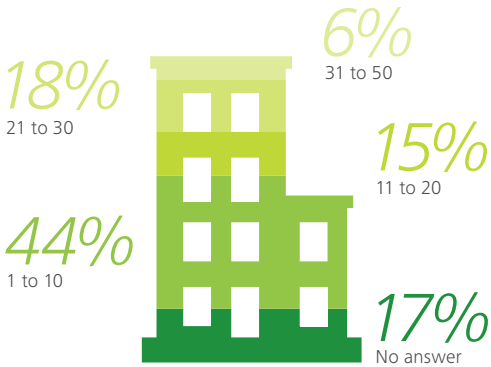


Size of Private Equity unit (in FTE)

Specialized Real Estate unit



Size of Real Estate unit (in FTE)



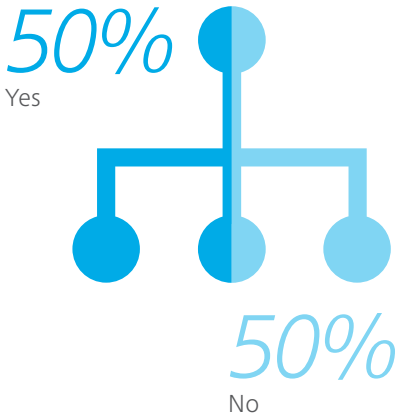
Outsourced services

The survey shows that 50 percent of PE asset servicers and 42 percent of RE asset servicers (wholly or partially) outsource their activities, mostly within their group. Mainstream banks generally outsource such services to other entities within their group, to global/regional hubs or to centers of excellence.

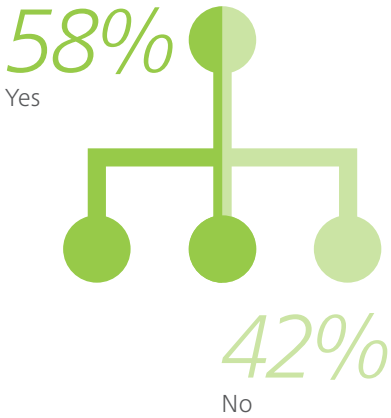
On the other hand, specialized service providers in alternative asset classes prefer to have dedicated units locally. The activities outsourced within the group are mainly those linked to high volumes or repetitive transactions or activities, which when centralized provide increased efficiency and cost savings.

Outsourced services (in percent)

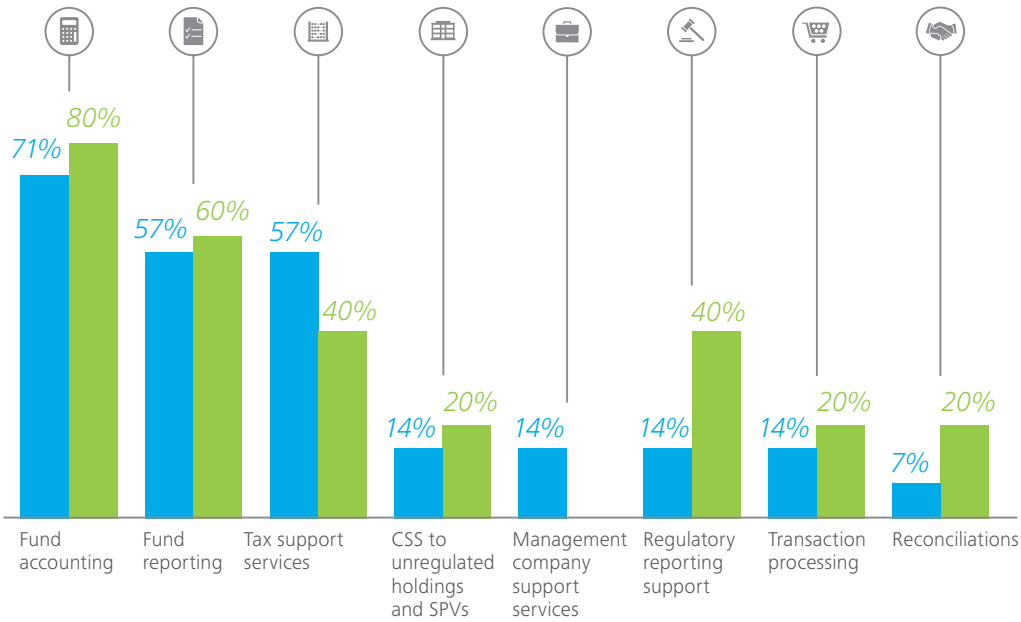
Private Equity



Real Estate



Type of services outsourced (in percent)

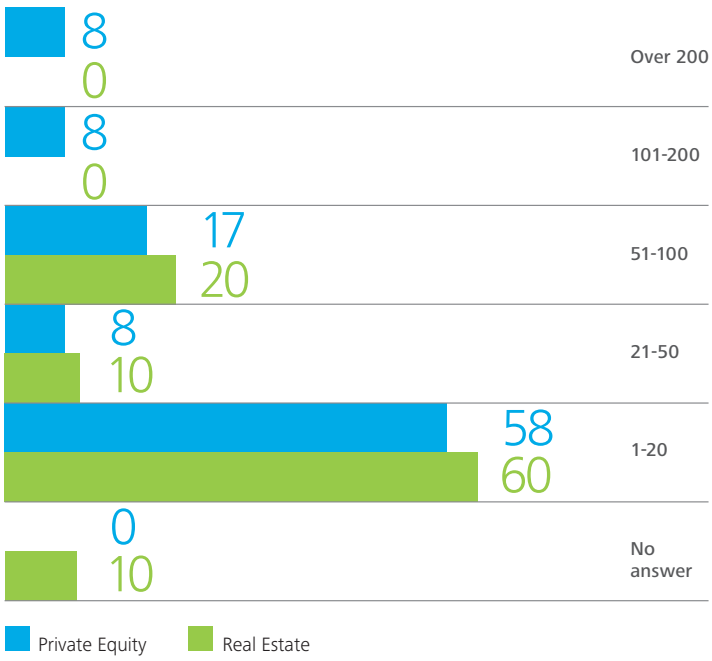


Private Equity Real Estate

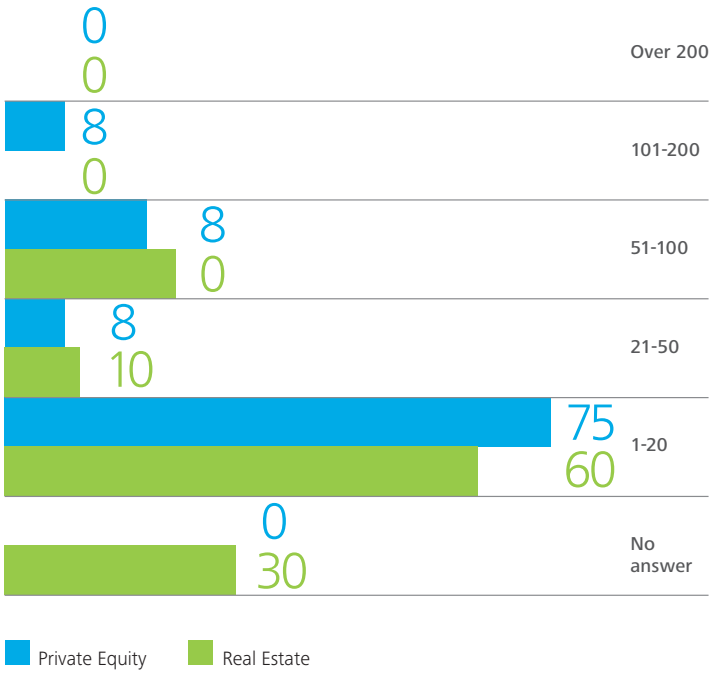
PE and RE asset servicers mostly have fewer than 20 sub-funds investing in underlying assets

The majority of respondents have limited numbers of sub-funds (1-20) in their portfolio; this is even more apparent for Fund of Funds (FoFs) concerning PE asset servicers. Compared to the PE world, RE shows a large concentration at the lower end of the scale.

Number of sub-funds **directly** investing in underlying assets (direct funds)



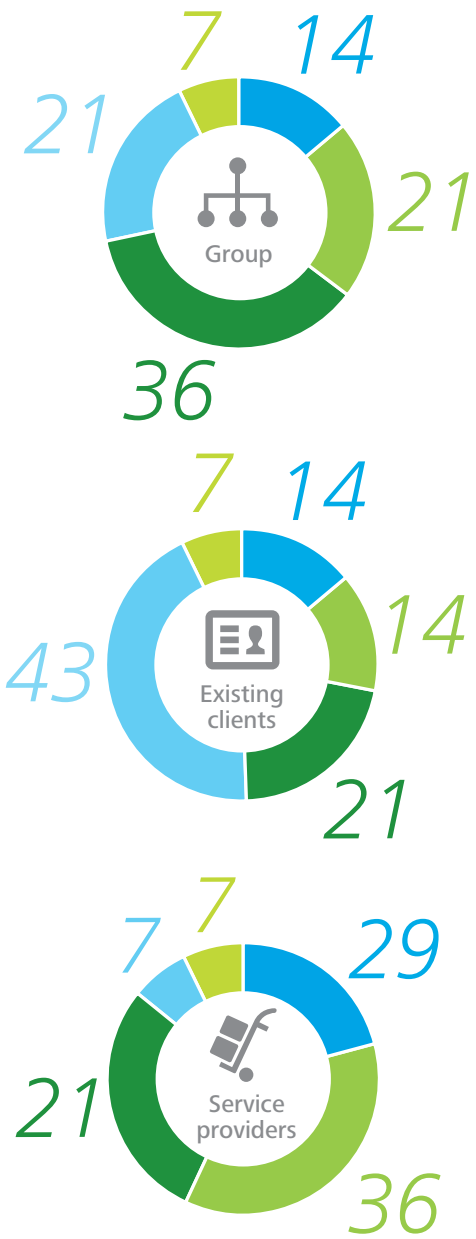
Number of sub-funds **indirectly** investing in underlying assets (FoFs)



Main business feeders and client acceptance

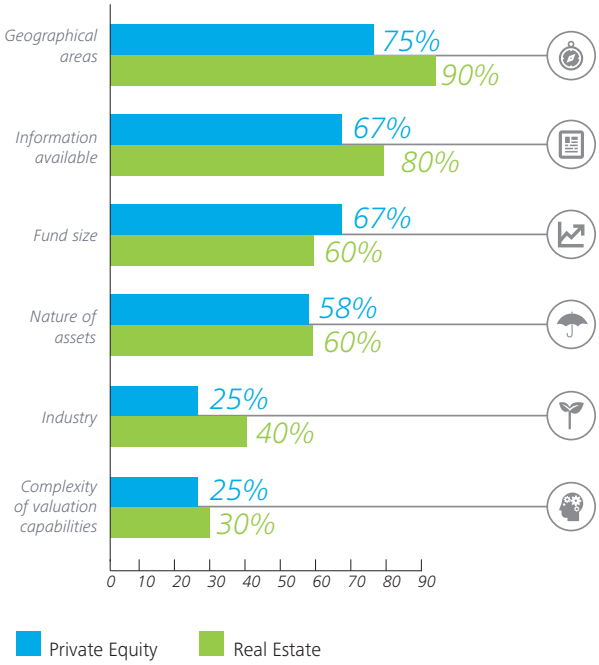
PE asset servicers, like their RE counterparts, name existing clients and the group as their main business feeders.

Main business feeders and their weight in business development (in percent)



- NO ANSWER
- LOW (0-19%)
- MEDIUM (20-39%)
- HIGH (40-59%)
- VERY HIGH (>60%)

Restrictions on some investment types when accepting a client or project



The restrictions when accepting a client or project cited by most PE and RE asset servicers are geographical areas (75 percent and 90 percent of survey respondents respectively), closely followed by the availability of information (67 percent and 80 percent). The nature of assets and fund size are equally important for RE asset servicers, as indicated by 60 percent of respondents.

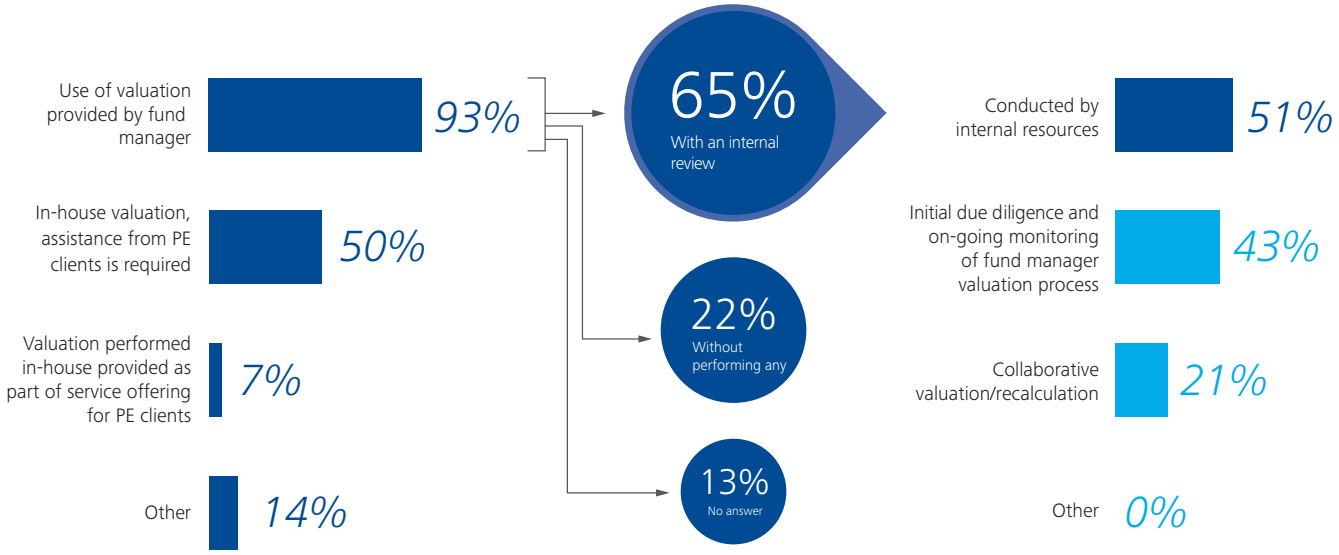
For 67 percent of PE asset servicers, fund size is more important than the nature of assets, which was quoted as the fourth most important type of restriction when considering new client acceptance. We observe a clear shift in the perception of the PE/RE asset class among market players, especially those from the banking sector, who are now more familiar with the specificities of these assets and are increasingly willing to service this type of clients. The industry and complexity of valuation and valuation capabilities are the least cited restriction types for both groups of asset servicers.

The majority of the survey respondents, more than 90 percent, use valuation provided by the fund manager, which is a common practice observed in the PE/RE industry. In-house valuation assistance is commonly provided only for funds of PE funds or for funds of RE funds.

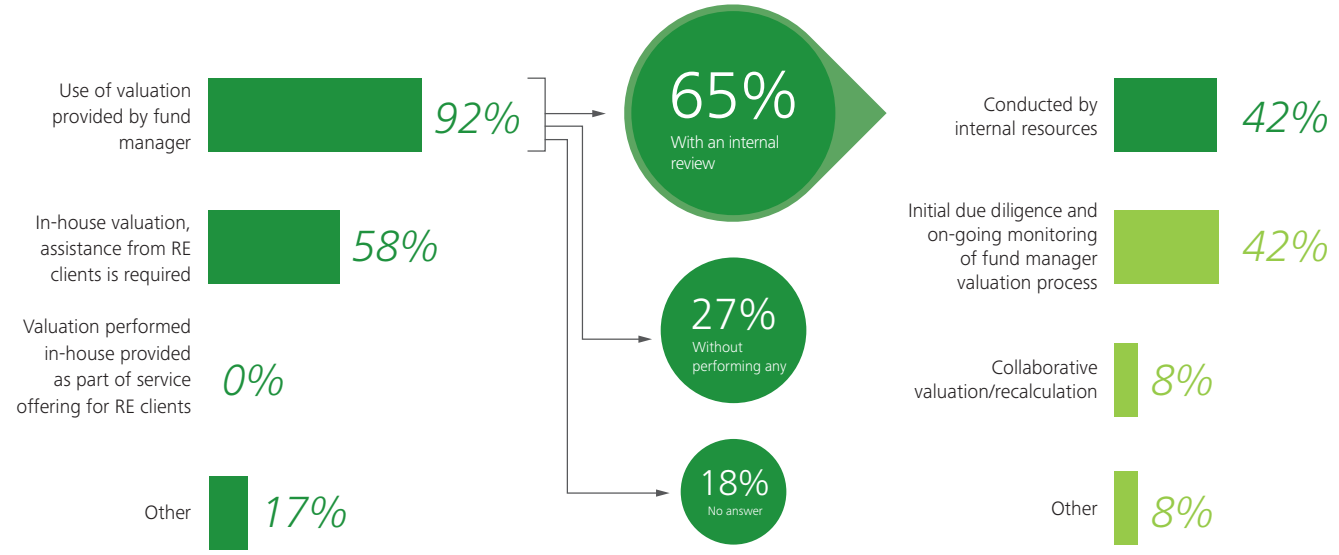
Among the majority of respondents who use valuation provided by the fund manager, 65 percent for PE and 55 percent for RE review this valuation internally. This review is generally conducted by internal resources or via an initial due diligence and on-going monitoring of the fund valuation process. As the valuation is often performed by 3rd party valuation agents who have more technical expertise to conduct the work, the RE asset servicers only ensure that such valuations are done by independent and reputable entities or focus more on the controls around the valuation and approval process by the client.

The nature of assets and fund size are equally important for RE asset servicers, as indicated by 60 percent of respondents

Valuation of PE investments obtained or performed by the organization



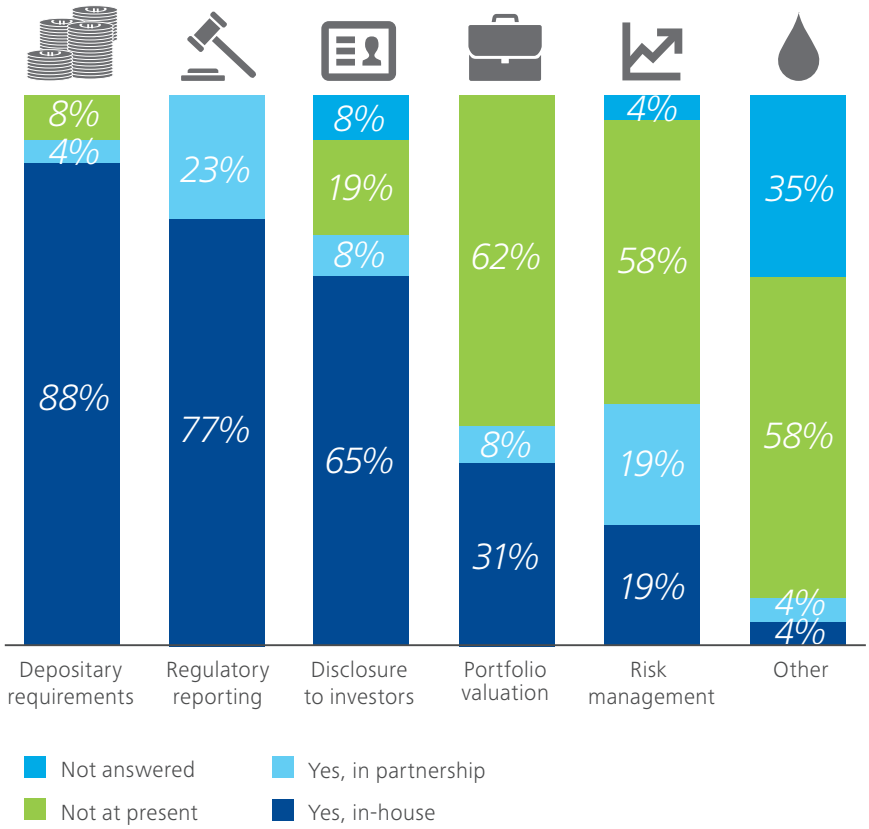
Valuation of RE investments obtained or performed by the organization



Reporting

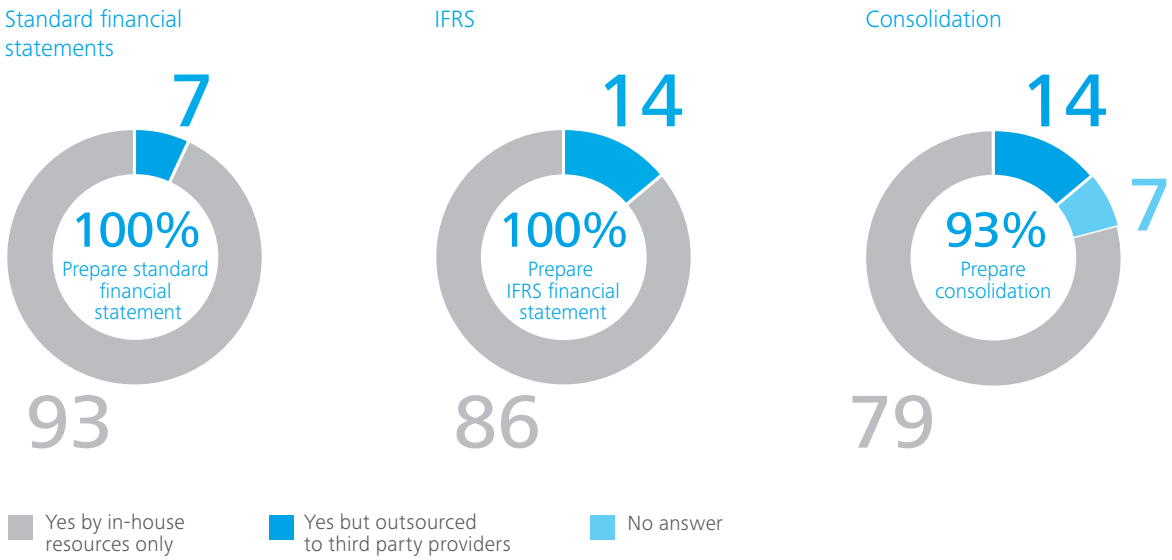
Regulatory reporting is the only service offered by all PE and RE survey respondents. PE and RE asset servicers have fully recognized the operational challenges faced by fund managers due to AIFMD. Reporting requirements constitute one of the greatest challenges and PE and RE asset servicers clearly intend to seize the opportunity by developing and providing various regulatory reporting services to their clients, either using their own resources or in partnership with other service providers. The rate of respondents providing this service is 88 percent for the PE industry and 92 percent for the RE industry. Most survey respondents wish to differentiate themselves from their peers by developing in-house services related to depositary requirements, regulatory reporting and disclosure to investors.

Services proposed to clients following AIFMD implementation

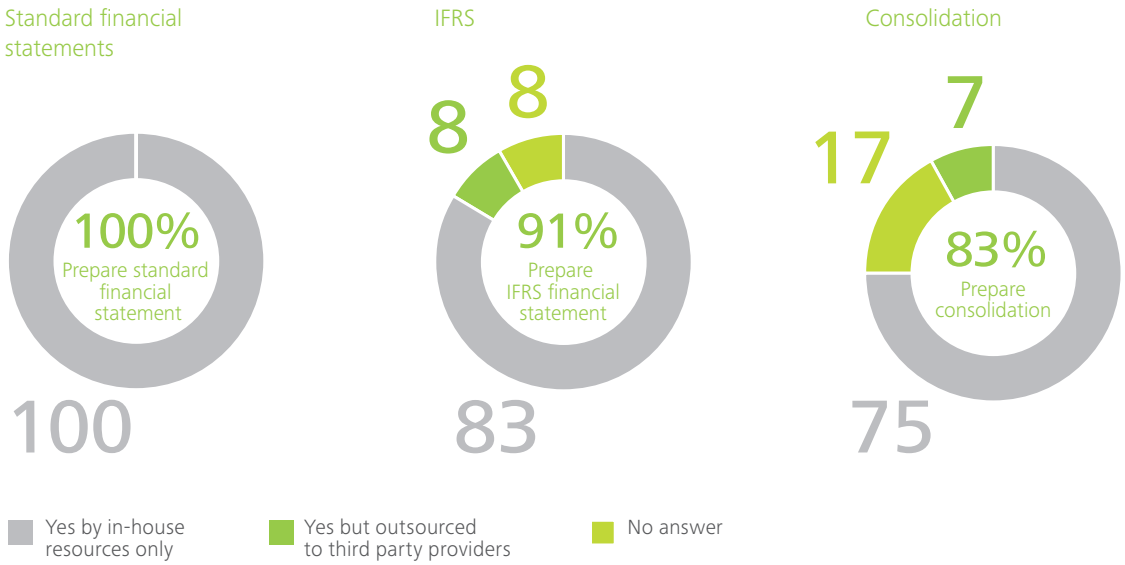


Almost all PE and RE asset servicers provide a comprehensive range of financial statement services. 79 percent of PE asset servicers and 75 percent of RE asset servicers have a dedicated team preparing financial statements or dedicated PE reports team. Standard financial statements, IFRS financial statements and consolidation services are offered by the majority of PE and RE asset servicers. Only a minority of survey respondents do not provide financial statements with in-house resources but are instead using third-party providers to complement their range of services (usually the 'Big Four' accounting firms).

PE financial statements preparation



RE financial statements preparation



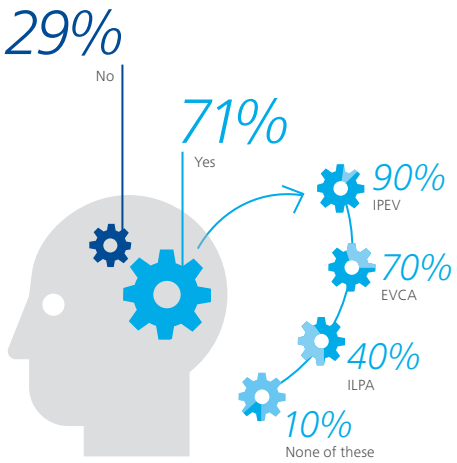
From the reporting solution standpoint, the survey highlights the fact that a significant majority of service providers offer reporting solutions to Limited Partners. IPEV is the most commonly used reporting standard among PE industry representatives, while INREV is the most common standard for the RE industry.

However, 45 percent of PE survey respondents who either use IPEV, EVCA, ILPA or other standards feel that these standards still need to be improved. On the other hand, there is an equivalent number of respondents who believe these standards are appropriate and adequate as they stand. Only a minority (around 10 percent for both the PE and RE industries) believe that the cost of implementation is expensive or burdensome.

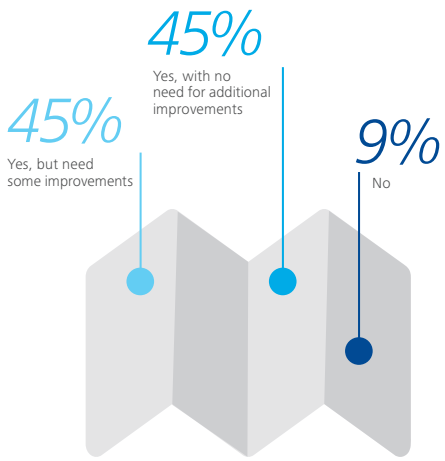
The asset servicers from the RE sphere expressed similar views, with 50 percent stating that there is a need for some improvements vs. 40 percent who view the standard guidelines as appropriate in their current form.

PE reporting solutions

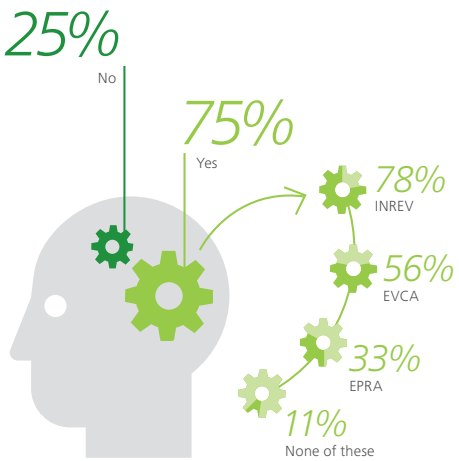
Reporting solutions provided to Limited Partners

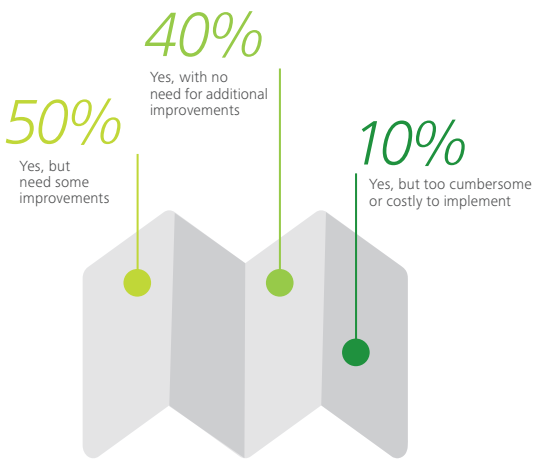


These guidelines constitute an appropriate standard for the activity



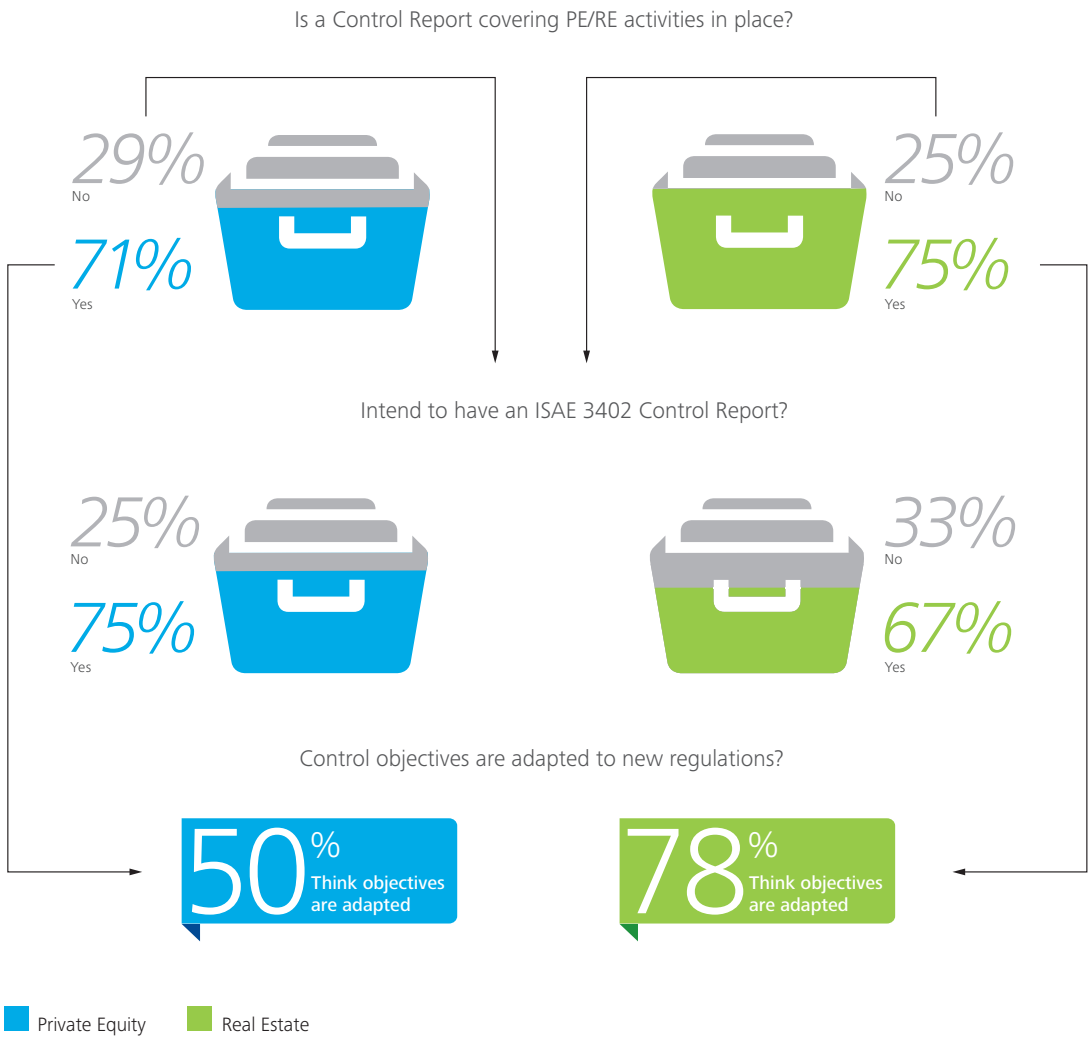
RE reporting solutions





The ISAE 3402 Control Report is another issue underlined by the survey from which emerges that 71 percent of PE asset servicers and 75 percent of RE asset servicers have an ISAE 3402 Control Report covering their respective activities. Of those survey respondents who have Control Reports covering their PE and RE activities, only half believe that their control objectives are adapted to PE asset class. The RE controls seem to be more in line with the new regulations, as 78 percent of the respondents have expressed their confidence in the objectives of their ISAE 3402.

ISAE 3402 Control Report covering PE/RE activities

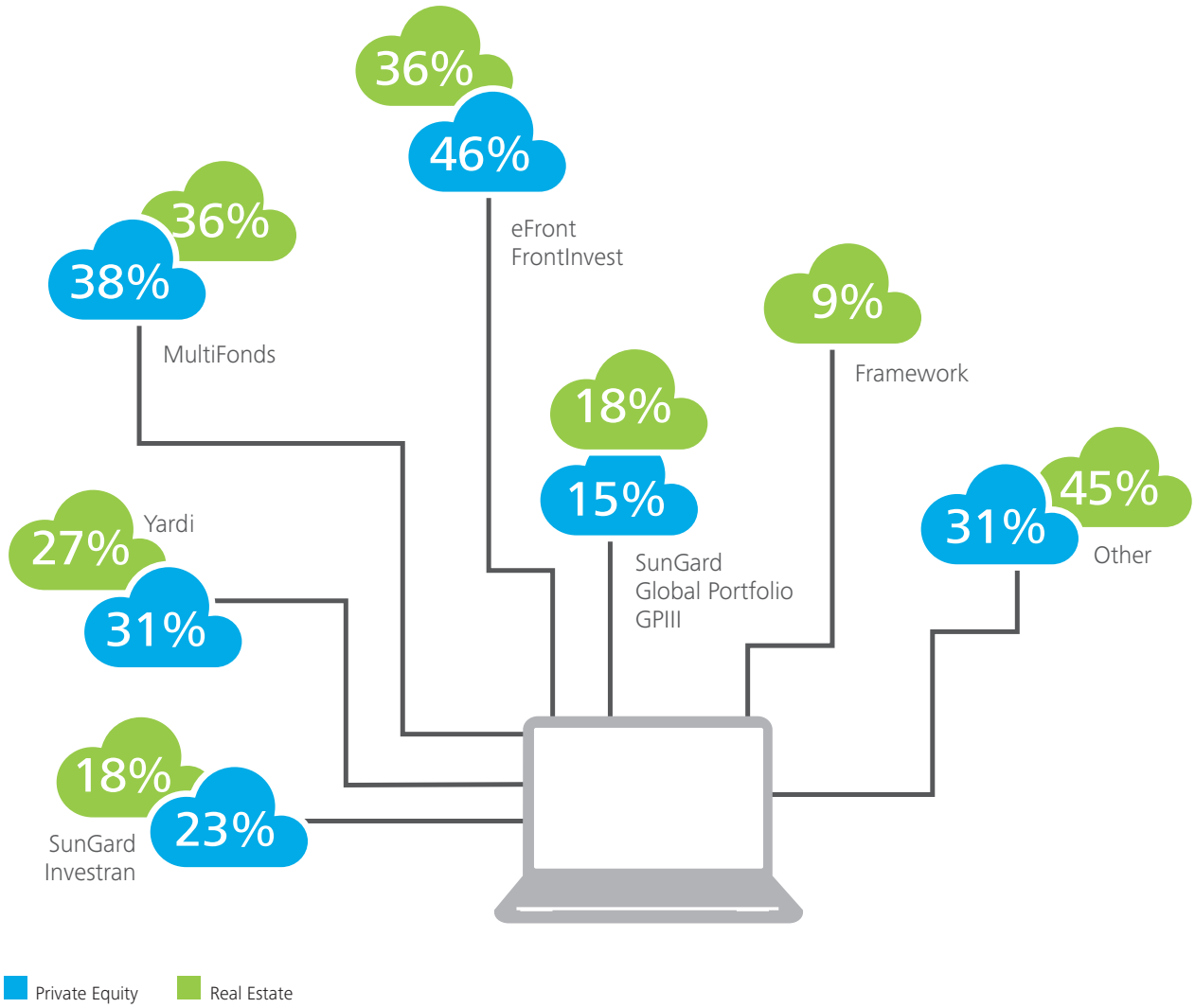


Operational aspects

The survey results show that the most common IT systems used by PE/RE asset servicers are e-Front Frontinvest and MultiFonds. The first is used by 46 percent of PE asset servicers while the latter is used by 36 percent of RE asset servicers.

More than 50 percent of survey respondents use more than one system for their activities as they often face diverse and various requirements such as investor and portfolio asset keeping, transaction processing, accounting and financial reporting, regulatory reporting, cash position keeping, etc. While there is a minority of respondents who are unsatisfied with their current system, 14 percent and 8 percent in the PE and RE industry respectively, there is a clear trend to upgrade versions in the next couple of years (86 percent on PE side and 75 percent for RE).

System used



Growth and outlook

Reinforcing staff and investing in technology, these are the top priorities for PE and RE asset servicers as it emerges from the 2015 European Private Equity and Real Estate Asset Servicers' Survey. Due to the anticipated growth of industry, PE and RE asset servicers are already directing their efforts toward recruiting the right profiles and creating learning and development opportunities for existing staff, as expressed by 38 percent of PE asset servicers and 54 percent of RE asset servicers.

Considering the technological aspects and as highlighted in the previous section, a strong will to at least upgrade the current system version within the next 12 to 24 months has been indicated by the asset servicers.

Both PE and RE asset servicers share common sentiments that their business growth will be fuelled mainly by new clients followed by increase in volume from existing clients. Value-added services for existing clients are also perceived as growth opportunities and in order to take full advantage of these possibilities a primary importance should be given to the technology aspects and the enhancement of operating models and/or new organizational transformation.

Asset servicers share an optimistic outlook for client growth trends in the next two to five years. Half of PE respondents anticipate growth in the next two years to be in the region of 11-20 percent. Expectations for the next five years are similar, with 29 percent of the respondents predicting growth of 11-20 percent.

However, 21 percent of PE respondents were more optimistic about growth i.e., predicting an increase of 21-30 percent or over 30 percent. On the RE side, asset servicers are more bullish, over both the two-year and five-year horizons. Indeed, 58 percent of respondents anticipate an increase for their client base by 11-20 percent in the near future, whereas 42 percent of respondents forecast five year growth to be in the region of 21-30 percent.

Future investments

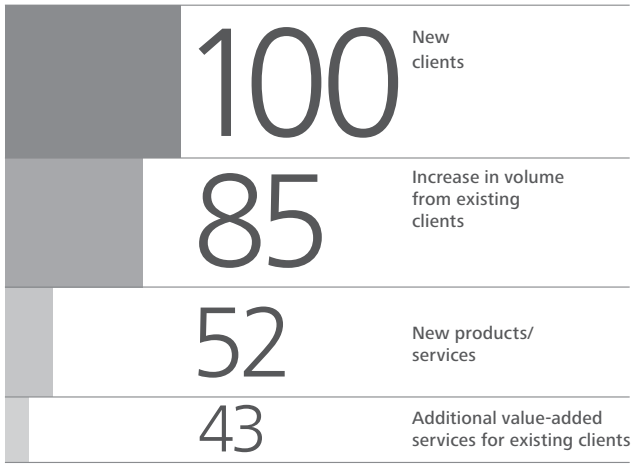
Staff development and recruitment
(PR 38%; RE 54%)

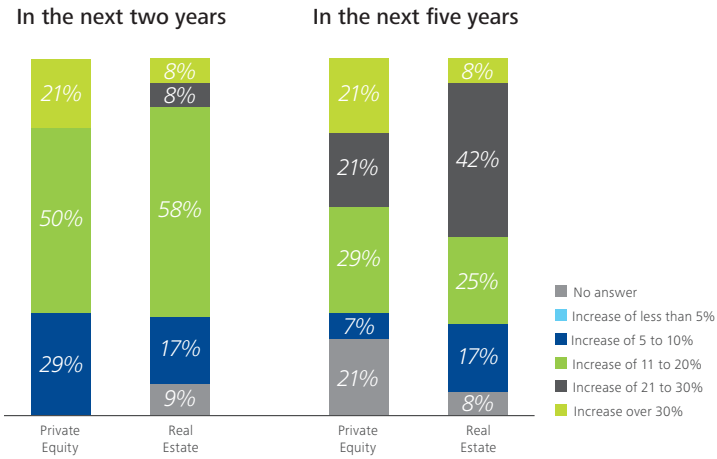
Technology
(PE: 38%; RE: 27%)

Marketing and business development
(PE: 16%; RE: 11%)

Operating model and organizational transformation
(PE: 8%; RE: 8%)

Expected sources of business growth (in percent)





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