

CONDUCTING REFERENCE CALLS



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Many limited partners and advisors use reference calls as an essential element of their due diligence on investment managers. These calls can verify a manager's official statements used in their marketing materials and also be used to gather additional information and specific examples of the manager's processes, reputation, and relative strengths and weaknesses. Over time, Pavilion Alternatives Group® ("Pavilion") has developed an effective strategy for conducting reference calls and have a number of tips and tricks to improve their usefulness.

Choosing References

The first step of conducting reference calls is identifying who to contact. Categories of potential contacts include portfolio company management teams (past and present), limited partners, co-investors, competitors, ex-employees, and other industry participants. Managers will often provide a list of contacts that have agreed to serve as references. It is important to keep in mind that these references have been thoroughly vetted by the manager and are likely to have primarily positive things to say. If they don't, you should question why the manager could not find a better reference. Despite their potential bias, these references can still serve as knowledgeable sources of information and offer examples of the manager's culture, investment strategy, and relative team strengths. In order to gain a more complete view of a manager, Pavilion also typically speaks with "off-list" references, which represent other industry contacts that know the manager but were not provided as an official reference and have not been prepped for a reference call.

Preparing for Reference Calls

Reference calls are usually short, often only 15 or 20 minutes. Because time is limited, it is advisable to prepare

beforehand to get the most out of the call. A starting point is to research both the reference and their company. It is helpful to have already completed some due diligence on the manager to provide a general understanding of the manager and how they interacted with the reference. By knowing something about the reference as well as the manager, you can develop a set of relevant questions and determine the specific objectives of the call. We have found that focused questions rather than generalized ones are more likely to produce useful information.

Asking Questions

Reference calls can have a variety of purposes, and the questions should be customized accordingly. When calling an executive from a company that the manager invested in, goals may include verifying the sourcing process (was it really a proprietary transaction?), determining how the manager has added value, understanding the manager's strengths and weaknesses, assessing which professionals have been the most helpful and the most responsible for the manager's returns (and checking if those professionals still work for the manager!), and asking why the company chose to partner with the manager. Former employees can be called to verify their reasons for leaving and to confirm that there are not any systemic issues around the manager. Other limited partners can confirm the manager's statements and discuss any concerns they may have. Bankers can be asked how the manager compares to other investors with which they have worked. Co-investors can discuss their experience working with the manager. Finally, competitors can provide insight into how the manager is viewed in the marketplace.

It is helpful to have a pre-determined list of questions that you can ask, but you should avoid blindly following the list. The conversation should flow naturally and you

should be ready to press for more information and ask follow-up questions when appropriate. Finishing with an open-ended question (e.g., “Is there anything else you wish to share?”) also allows the reference to talk about any other issues that they want to discuss but have not been directly addressed by your previous questions. Another good final question is to ask the reference if they know anyone else who could provide especially good insight into the manager.

It is best to avoid asking yes or no questions and instead opt for questions where the reference can elaborate on items that he or she feels are important. If something is mentioned in passing, or a reference provides a brief or vague answer, ask for additional details.

Etiquette

An effective approach is to treat each reference call as an opportunity to build a relationship. Start by sending an email to introduce yourself, explain what you are looking for, and ask to schedule a call. It is important to always be respectful of the reference’s time. Since you are using some of their valuable time, it is good form to offer to be helpful to them in the future, such as by providing a reference on another manager. Finally, after the call is over, you may wish to send the reference an email to thank them for their time and for the insight they have provided on the manager.

Reference calls come in all shapes and sizes, with some proving to be extremely helpful and others being less informative. With practice and focus, reference calls can become an effective and integral part of your due diligence process and help you develop a deeper understanding of the strengths and weaknesses of the manager.

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