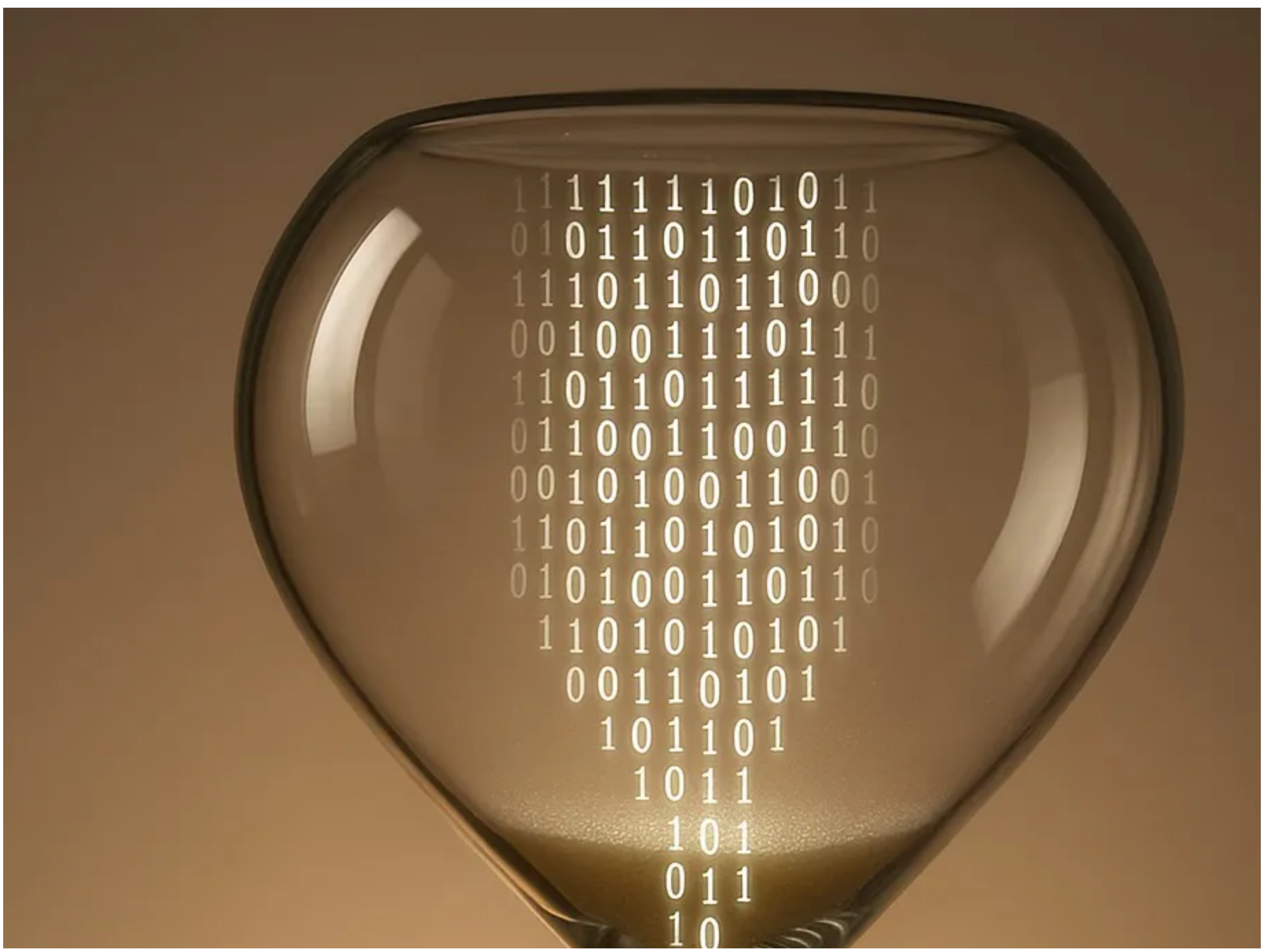
# Turning a Gaze to Funds of Funds Governanc

Primer for the week ahead: Essential concepts for navigating the AI transformatio private equity

TANYA MATANDA
SEP 28, 2025

Sha

Article voiceover
0:00 -10:5



Private equity is being reshaped by two converging forces: the rise of f
funds (FoFs) as a vehicle for diversification and access, and the rapid integration of artificial intelligence into investment decision-making. Together, they create new opportunities—and new governance risks—
investors cannot afford to ignore.

This week, we will analyze how these forces are changing private equit

shifting fee structures and performance attribution, to evolving oversi
challenges, to governance arbitrage across jurisdictions. This primer
establishes the vocabulary and frameworks that will anchor those anal

## What Are Funds of Funds?

A **fund of funds (FoF)** raises money from investors—known as limited p
(LPs)—and allocates that capital not into companies directly, but into a
portfolio of other private equity, venture capital, or hedge funds (the
underlying funds).

**The appeal lies in three factors:**

- **Diversification:** Spreading capital across multiple managers, secto
  geographies reduces concentration risk.
- **Access:** Many elite funds are closed to new investors or require hig
  minimum commitments. FoFs provide an entry point.
- **Expertise:** Professional FoF managers select, monitor, and realloca
  among funds, offering due diligence that individual LPs may lack.

Yet FoFs introduce an extra layer of governance. LPs must evaluate not
the FoF manager's decisions but also the governance quality of the unc
funds themselves. Weakness at either level can amplify risks. In an AI-
era, this "double-layered governance" becomes even more consequent

## The Paradigm Shift in Private Equity

For decades, private equity rested on relationships, judgment, and exp
Today, algorithms are shifting from supporting human decision-makin

shaping it outright.

For example, several firms now reallocate capital mid-quarter based o models that continuously track portfolio metrics and market signals— something human committees rarely attempted. These adjustments ca improve returns but also raise questions: who is accountable when an algorithm rebalances prematurely or chases spurious correlations?

The evolution introduces new categories of risk, new sources of alpha, new demands for oversight—ones that traditional governance framew were never designed to address.

## The New Vocabulary of AI in PE

To analyze these changes, four distinctions are critical:

- **Algorithmic vs. Assisted Decision-Making**
  Where does human control end and algorithmic dominance begin often advertise "AI-assisted," yet many are in practice becoming "A driven." If an LP committee rubber-stamps AI outputs without cha accountability blurs.
- **Model Governance vs. Investment Governance**
  Strong investment committees mean little if the algorithms benea go untested. Oversight of models and oversight of investments are same. Assuming one covers the other is a dangerous blind spot.
- **Attributable Alpha vs. Correlated Performance**
  Did AI genuinely drive performance, or did it ride a rising market? Consider a fund claiming AI alpha during a tech rally—without attr

analysis, correlation masquerades as causation.

- **Governance Arbitrage vs. Regulatory Arbitrage**
  Firms exploit regulatory differences across jurisdictions, but some exploit governance gaps between what regulators require and wha actually creates durable value. For LPs, the latter may determine w they capture alpha or absorb hidden risks.

## The Structural Shifts Emerging in the Data

**Evidence suggests three fundamental shifts are underway:**

1. **From Scarce Information to Information Overflow**
   Competitive advantage no longer lies in privileged access, but in processing vast datasets.
   - *Governance implication:* Boards must now scrutinize how data pipelines are validated, not just who provides them.
2. **From Episodic Oversight to Continuous Optimization**
   Algorithms make micro-adjustments daily, even hourly.
   - *Governance implication:* Quarterly oversight cycles are misalig compliance must evolve toward real-time monitoring.
3. **From Individual Manager Risk to Systematic Risk**
   As more firms use similar AI models or data providers, diversificati across managers may not protect portfolios.
   - *Governance implication:* LPs should evaluate systemic exposur cut across funds, not just fund-level risks.

## Why This Matters Now

The stakes are rising. Early adopters with strong AI governance are alr pulling ahead, while firms with weak structures lag not only behind pe even behind traditional approaches. Performance dispersion is wideni window for implementing proper AI governance is narrowing as early adopters cement their advantages.

Meanwhile, regulation is crystallizing. Funds that build governance frameworks early will adapt smoothly; those that retrofit will face high and reputational risks.

And fee structures remain misaligned. Many LPs are paying premiums enabled" funds without evidence of attributable alpha. Yet innovative r that tie fees to measurable AI performance are beginning to appear—c opportunities for informed investors and traps for the rest.

## The Meta-Framework for Analysis

To navigate this landscape, investors and board members need a struc approach. Every AI-enhanced private equity opportunity should be ass across three layers:

These lenses should be reinforced by decision hierarchies (irreversible reversible vs. operational) and attribution matrices (measured vs. clain sustainable vs. temporary performance). Together, they allow investors separate signal from noise.

## Setting the Stage

This primer establishes the vocabulary and frameworks we will use throughout the week. In the coming articles, we will analyze:

- How fees and performance attribution are shifting in AI-enhanced of funds,
- The evolving oversight challenge facing boards,
- The interplay of governance and regulatory arbitrage, and
- What data reveal about firms that govern AI effectively versus thos do not.

Technology can be copied. Data can be bought. Algorithms can be repl But governance quality—the systems that oversee, align, and hold AI accountable—remains a sustainable source of competitive advantage.

Readers who master these frameworks will be positioned to identify governance quality that others miss—and capture the alpha that flows that advantage.

*This article explores ideas from “Shaping the Decade: Governance, Sustainability, and AI 2026–2036,”* a comprehensive guide for boards navigating the intersection of governance, technology, and stakeholde capitalism. For those ready to learn more about AI, this book offers pra strategies and insights.
Explore it here

## *Research Supported by AI Systems*

## *Audio Supported by AI Systems*

← Previous

## Discussion about this post

Comments Restacks

Write a comment...