Private Equity Spotlight

January 2008 / Volume 4 - Issue 1

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Welcome to the latest edition of Private Equity Spotlight, the monthly newsletter from Preqin, providing insights into private equity performance, investors and fundraising. Private Equity Spotlight combines information from our online products Performance Analyst, Investor Intelligence & Funds in Market. This month's issue contains details from our latest publication, The 2008 Global Private Equity Review

Feature Article

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You Ain't Seen Nothing Yet - With the recent credit crunch and trouble in the financial markets, many commentators have (again!) called the top of the market for private equity. We explain why we believe that private equity will continue to grow – from $2 trillion today to $5 trillion over the next five to seven years.

Performance Spotlight

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In this month's Performance Spotlight we examine the relative performance of private equity in the portfolios of public pension plans on both sides of the Atlantic. Featuring data from our newest publication, The 2008 Preqin Global Private Equity Review.

Fundraising

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2007 was another excellent year for private equity fundraising. This month Spotlight examines global fundraising in 2007, with final figures by fund type and region.

No. of Funds on Road	US	Europe	ROW	Total
Venture	220	82	104	406
Buyout	162	60	41	263
Fund of Funds	96	68	14	178
Real Estate	145	93	30	268
Other	109	39	41	189
Total	732	342	230	1,304

Investor Spotlight

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With exclusive information taken from The 2008 Preqin Global Private Equity Review, this month's Investor Spotlight gives the results of our 2008 LP Survey - find out how investors feel about the current state of the private equity market.

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All the latest news on investors in private equity:

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- BlackRock Private Equity Partners has invested in New Atlantic Venture Fund III.
- SCERS selects fund of fund managers to run mandates for its maiden allocation to private equity.
- SFERS seeking advisor for alternatives as its current advisor comes into the last year of a five year contract.
- Folksam appoints new head of private equity.

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Feature Article:
You Ain't Seen Nothing Yet

The credit market crunch has been a major shock for financial markets, including private equity. Many commentators have (again!) called the top of the market for private equity. This month's Spotlight Feature Article, taken from Preqin's 2008 Global Private Equity Review, explains why they are wrong, and how private equity will continue to grow – from $2 trillion today to $5 trillion over the next five to seven years.

The global private equity industry has enjoyed spectacular growth in recent years, doubling in size from $1.0 trillion AUM in 2003 to $2.0 trillion by mid-2007. The expansion has been widespread across geographies and fund types – the mega buyout funds may have captured most of the headlines, but there has been solid growth in mid-market and smaller buyouts, in distressed debt, mezzanine, real estate, infrastructure, venture and other fund types.

And then along came the credit market crunch in mid-2007.

After years of increasingly favourable terms for the provision of debt finance, the music suddenly stopped. Deal volumes shrank in the second half of the year, and many asked the inevitable question: was this the end of the road for the buyouts boom, or just a (major) pothole along the road to further growth?

We believe that all the evidence points firmly to the latter: private equity will continue to grow strongly over the medium to long term. There are several reasons for this:

- **A profitable ownership model**: private equity has proved itself to be a very effective ownership model, delivering superior net returns to investors over an extended period, covering good times and bad. Public pension plans is just one illustration of this – PE has consistently out-performed other investments over whatever time horizon you choose to take: one, two, five or ten years. Critically, this demonstrates private equity's ability to deliver superior returns over the cycle – and not only during periods that may be distorted by unusually-favourable availability of debt finance.

- **Routes to adding value**: private equity has clearly enjoyed unusually favourable market conditions in the recent past. However, private equity adds value to acquired businesses in many ways, most importantly through being truly involved owners, and empowering management to develop the business's potential for long term value creation. This is difficult to analyze in an academically rigorous manner, but one only has to speak with a few managers at newly-acquired private equity portfolio companies to realize that these businesses are being managed in a fundamentally more involved and value-oriented manner.

- **LP appetite**: LP allocations to private equity have been growing steadily for many years, both as a result of more new LPs entering the asset class, and existing investors raising their target allocations. Preqin regularly surveys the intentions of LPs, and our most recent survey, conducted in December 2007 after the impact of the credit crunch, confirms that the trend is continuing: 52% of LPs surveyed intend to increase their allocations, 48% intend to maintain them at their current levels, and 0% plan to reduce them. These LPs recognize private equity's ability to deliver superior returns, and are increasingly making it a core part of their long term plans.

- **Availability of deals**: deal volumes clearly fell off severely in the second half of 2007, but this was primarily at the top end of the market. Deal volumes have continued in the mid-market, and new opportunities are opening up for mezzanine and distressed investments. The evidence over a long period from the rate of call-up of private equity funds confirms that fund managers have had no difficulty in finding adequate opportunities to invest the ever-larger funds that have been

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raised. On the contrary, the recent fund vintages have been called up more quickly than ever before. Looked at in a broader context, the availability of potential investments for private equity is quite staggering: in the EC alone, there are approximately 130,000 privately owned companies with 250 employees or more. Many of these are now (under-) managed by ageing family boards with significant succession issues. Add to this a further body of divisions of publicly-held companies that may be better candidates for private ownership, medium and larger public companies that may be suitable for take-privates, and secondary buyouts, and the scope for potential private equity deals is truly vast.

- **Availability of debt finance**: an important point to remember about the credit market crunch is that it came as no surprise. Private equity practicioners had been saying for some time that the prevailing terms for debt finance, while hugely favourable and welcome, were probably unsustainable. Many had cautioned their LPs not to expect the uniquely favourable conditions of 2006 and early 2007 to last. Now, few would have guessed precisely when or how things were going to re-adjust, but an eventual re-assertion of reality was widely expected. At the time of writing, the mid-market is open for business, but the top end of the market is still frozen. Will this continue? Absolutely not. Keep two facts in mind: first, there is simply a huge amount of yield-hungry money in the world looking for investment opportunities; and second, private equity has a very good record of delivering returns for these investors – indeed, there are some major private equity firms who have never lost a lender any money. Think about that. The debt markets will clearly come back – not to the sublime conditions of early 2007, but come back they will. And private equity will be ready.

- **A burgeoning supply side**: the wonderful thing about private equity is that it is perhaps the ultimate expression of Adam Smith's invisible hand at work. The huge talent pool within the private equity industry – around 77,000 skilled people worldwide – are constantly looking for new investment opportunities, in good times and bad. An illustration of this is the current stock of new funds on the road worldwide – nearly 1,300 of them according to Preqin's records, seeking over $600 billion of funding between them.

- **Private equity is still small**: yes, that's right, small. Achieving global AUM of $2.0 trillion may be a major achievement, but it begins to look like a rounding error when viewed in the context of public markets. According to the World Federation of Exchanges, global stock market capitalization reached an all time record of $59.7 trillion in September 2007. In other words, private equity equates to just over 3% of the capitalization of global stock markets. The scope for further growth is huge.

In conclusion, we believe all the evidence points to continued growth for private equity over the medium to longer term: it is simply a great ownership model for businesses, and a great investment opportunity for institutions. How big can it grow? That remains to be seen, but Preqin certainly believes that $5 trillion of AUM within 5 to 7 years is perfectly possible and likely.

Wishing you all success for 2008 and beyond.

This month's Spotlight Feature Article is drawn from Preqin's 2008 Global Private Equity Review, available 31st January.

For further details please see ***www.preqin.com/pereview*** www.preqin.com/pereview

2008 Preqin Global Private Equity Review

The 2008 Preqin Global Private Equity Review is the most comprehensive review of the private equity industry ever undertaken, and is a must have for anyone involved in private equity, or looking to learn more about this growing asset class.

Intended for use as both a vital source of information about the current market, and also as an information-packed reference guide, this year's edition includes:

- Interviews and articles from the most important people in the industry today, including GPs, investors, placement agents and more.
- Detailed analysis on every aspect of the industry with a review of 2007, and predictions for the coming year.
- Comprehensive source of stats on private equity - including fundraising, performance, deals, GPs, investors, placement agents, advisors, law firms...
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- Results of questionnaires with different groups on the state of the industry - what do LPs really think about private equity? What effect has the credit crunch had? What is going to happen to the industry in coming years?
- Plus much more...

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Performance Spotlight:

Private Equity: Delivering Superior Returns for Pension Funds

Pension plans are amongst the most important investors in private equity worldwide – Preqin's Investor Intelligence database of LP profiles lists over 950 pension plans with over $500 billion committed to private equity. Preqin's latest research shows just how well private equity has performed for these LPs.

The average pension fund has an allocation of approximately 4.3% of its total AUM to private equity, in itself a significant proportion, but even this understates the importance of private equity to these pension funds: the 20 largest public pension plan investors in private equity have a total investment in private equity of approximately $173 billion, equivalent to 8.8% of their combined AUM.

So, how well has private equity performed for these pension funds?

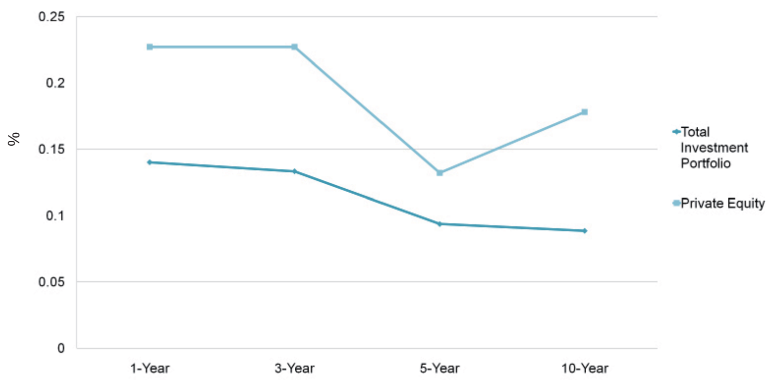
Taken on the level of individual private equity funds, the evidence shows that private equity has performed well relative to listed equities, but how does this result translate to the actual portfolio returns experienced by pension funds? Will the good performance also show through for the private equity portfolio as a whole, or could there be reasons (e.g. adverse fund selection) for the aggregate net performance for pension funds being less attractive?

Preqin reviewed the annual report and accounts for 108 separate public pension funds spread across the US, Canada, UK and Europe to compare the returns from their private equity investments with those of the rest of their portfolios. These pension plans had combined AUM of $3.9 trillion, and are amongst the most important investors in private equity. Given the long-term and illiquid nature of private equity investments, we compared net returns for their private equity investments with the rest of their portfolios over a range of time horizons – 1, 2, 5 and 10 years.

The results are shown in the chart below, which demonstrates that these public pension plans have enjoyed significantly higher returns from their investments in private equity than they have across the rest of their investment portfolios – with a margin of between 4% and 9% p.a. over all time horizons surveyed, between one and 10 years.

These results are an impressive demonstration that private equity has delivered superior returns for these pension funds, but the skeptic might argue that private equity should be delivering superior returns, given its "high risk-high return" investment role in the pension fund's portfolio. In order to address this we looked also at consistency of private equity's outperformance. The second chart below shows the results: private equity out-performed these pension plan's other investments in no fewer than 82% of cases, taken across the full range of time horizons between one and 10 years. In other words, private equity has

Public Pension Plan Median Returns - PE vs. Total Investment Portfolio

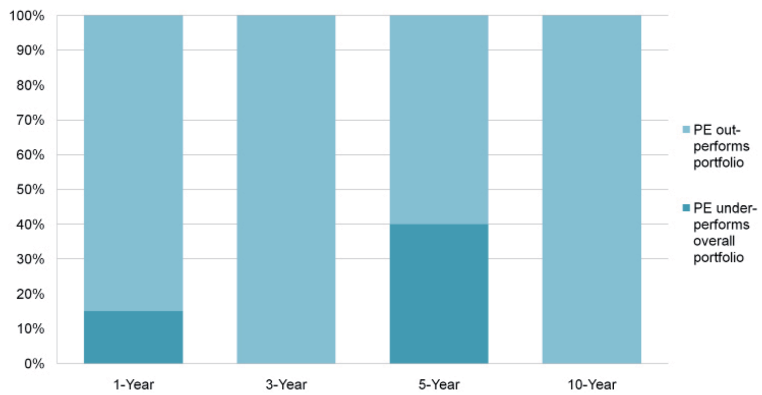


Performance Spotlight:
Private Equity: Delivering Superior Returns for Pension Funds

proved to be a consistent and ultimately low risk investment for these pension funds.

The conclusions appear to be fairly clear and robust: private equity has delivered superior returns for public pension funds on a very consistent basis. Small wonder that the overwhelming trend is for pension plans to increase their allocations to the asset class.

Consistency of Private Equity's Out-Performance vs. Other Investments



This article is taken from the 2008 Preqin Global Private Equity Review, which is packed full of the latest information, trends and expert opinion on the state of the private equity LP universe, along with countless other information packed sections.

At only $195 / £95 / €135 The 2008 Preqin Global Private Equity Review is an absolute must-buy for anyone involved in the private equity industry. This year's edition examines every aspect of the global private equity market and is available to order now. For more details including sample pages and information on ordering your copy, please visit:

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Fundraising Spotlight:
Overview of Fundraising in 2007

Since 2004 the private equity industry has experienced a boom in fundraising unparalleled by any other period during the lifetime of the asset class. After reaching a low ebb in 2003, private equity fundraising has grown every year, with 2006 figures marking the first time that the industry exceeded $500bn raised in one year.

Our latest figures indicate that 2007 is going to be another record-breaking year for the industry, with an aggregate $502bn being raised by a total of 726 funds achieving final closes over the course of the year. Although this falls just short of 2006's total of $516bn, we are confident that as additional information continues to trickle in, the total for 2007 will rise enough to ensure another record year.

Fundraising by type

Buyout funds again accounted for the largest slice of capital in the private equity industry, with 209 funds achieving a final close over the course of the year raising an aggregate $209bn. This represents a slight drop in terms of aggregate capital from last year's figures, when $232bn was raised by 200 vehicles. The credit crunch certainly seems to have affected fundraising for buyout funds, with a significant 62% of all capital being raised in 2007 coming in the first half of the year, and only 38% in the latter half. More details on buyout fundraising, plus details for each individual fund type can be found in the 2008 Preqin Global Private Equity Review.

Real estate funds raised the second largest amount of capital overall, with 126 funds raising an aggregate $79bn over the course of the year. Venture funds were the most prevalent in terms of the number of funds closed, with 218 vehicles raising an aggregate $56bn, $4bn up on last year's figures.

Fund of funds remain a popular fund type with 90 vehicles achieving final closes raising an aggregate $36bn. This does however represent a slight decrease from 2006, when an aggregate $43bn was raised.

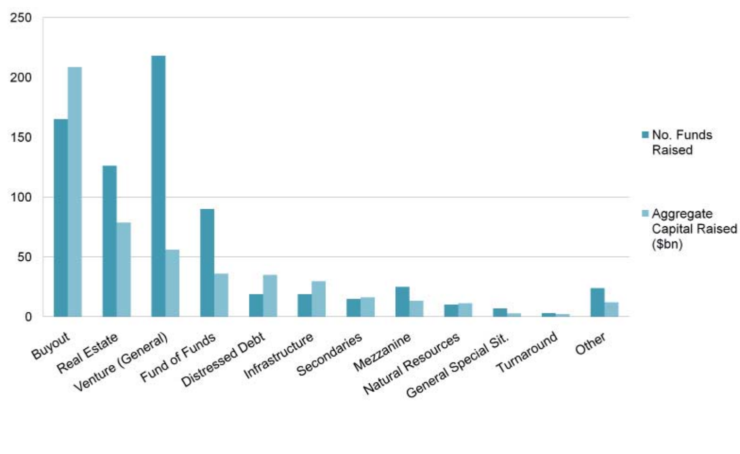
The number of distressed debt funds has continued to grow in 2007, and a total of $35bn was raised by 19 funds achieving a final close over the course of the year, almost three times as much capital as was raised in 2006.

Infrastructure fundraising was strong, with an aggregate $30bn raised - double the amount garnered in 2006.

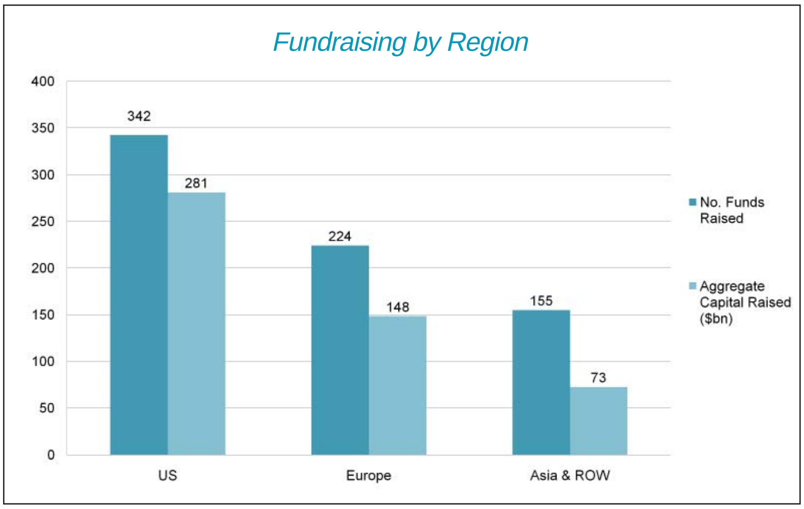
A total of 15 secondaries funds achieved a final close in 2007, raising an aggregate $16bn, up on the $11bn that was raised by the secondaries sector in 2006.

Mezzanine fundraising has declined from levels seen in 2006, with a total of $13bn raised in 2007 compared with an aggregate $22bn raised in 2006.

Fundraising by Fund Type



Fundraising Spotlight:
Overview of Fundraising in 2007



Total fundraising for the natural resources sector is also down on 2006 figures, but the aggregate $11bn raised by this emerging sector still represents a successful fundraising year.

Fundraising by region

The US continues to dominate the global fundraising market, with a total of 342 funds focusing on this region raising an aggregate $281bn over the course of 2007. This represents 56% of the global market, a very slight drop of 2% from the 58% market share held in 2006.

European funds raised $148bn from a total of 224 funds, leading to a market share of 29%, up on the 28% market share of 2006. A total of 155 Asia and Rest of World focused funds achieved a final close raising an aggregate $73bn. The global market share of these funds was 15%, 1% up on 2006 when the share for funds focusing on Asia and Rest of World was 14%.

This report is just a sample of the many different analyses on fundraising undertaken for this year's 2008 Preqin Global Private Equity Review, with further data being available for fundraising by GP country, average size of funds, final close as % of target, time spent on the road, plus detailed analysis for each individual fund type and a look at the current state of the fundraising market, including predictions on fundraising in 2008. We also gained the opinions of leading professionals working within the industry on conditions in 2008, including Mounir Guen, founder of leading placement agent MVision.

Investor Spotlight:
LP Survey Results

Private Equity Intelligence's Investor Intelligence database is the industry's leading source of information on institutional investors in private equity, with over 3,800 LPs listed as of January 2008. More LPs are added every day, and plans for existing LPs are being constantly updated by a team of more than 12 dedicated analysts. Using this database we identified some of the most important institutions actively investing in private equity today, and asked them a series of questions relating to the current state of the industry. Respondents are from around the world, and are of varying type. Where possible we have identified trends amongst different groups of investors as well as on an overall basis.

Are investors intending to increase, decrease or keep their private equity allocations the same in the coming year?

As the graph below shows, investors are universally either planning to maintain their current levels of exposure, or are intending to increase their allocations to private equity. 52% of investors plan to maintain their current levels of exposure, while 48% are intending to increase their allocations. Of those investors we surveyed, not a single respondent was planning to decrease their allocation to private equity in the coming twelve months.

The most positive group of respondents were banks, insurance companies and corporate investors, with 59% of investors in this group intending to increase their allocations over the coming year.

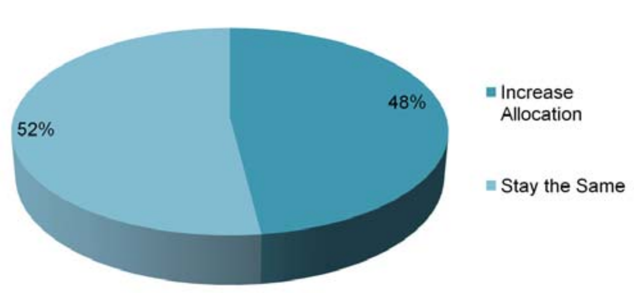
Have investors' private equity plans changed in light of the credit crunch?

Much has been said over recent months about the credit crunch potentially affecting the returns for managers within various sectors of the private equity industry, with the end of readily available cheap credit potentially affecting firms' ability to carry out the same deals that they have until recently been able to undertake.

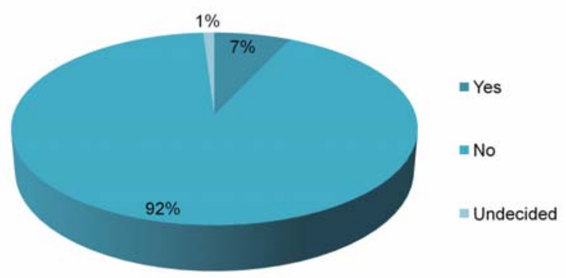
Have such arguments affected LP attitudes to private equity? We asked investors whether the credit crunch had affected their private equity plans, whether their strategy was to remain the same, or whether they were still unsure about how the credit crunch might affect their strategy.

As the chart below shows, the overwhelming majority of investors have not altered their strategy as a result of the credit crunch, with 92% of investors polled keeping their strategies the same. 7% of respondents have altered their plans, while the remaining 1% are still unsure as to what effect the credit crunch will have.

Future Private Equity Allocation Intentions



Has the credit crunch affected private equity plans?



Investor Spotlight:
LP Survey Results

These results are encouraging, but it is the individual responses themselves that are most telling. Amongst those that reported no change to their strategy, there were a number that stated that they would be exercising more caution when selecting funds. A prominent UK-based bank stated that ‘although we are not going to change our strategy towards private equity, new funds will be approached with caution’, and a European bank stated that current market conditions had led to them being ‘more reluctant and careful’ when investing.

Amongst those investors that were intending to change their strategies, there was one consistent theme: mega funds. A US based public pension plan with a significant private equity allocation will be ‘more conservative towards mega-buyout funds’, although the institution is still positive towards the asset class generally, and is planning to increase its allocation. A US endowment plan is going even further, stating that they will be ‘staying away from the mega buyout funds and generally being more selective’.

Although those investors that are changing their allocations as a result of the credit crunch are in the minority, the results do indicate that investors are starting to view mega-buyout funds less favourably than has been the case in recent years, and certainly that investors are being more cautious than they might have been before the credit crunch when selecting new investments. This more cautious approach has manifested itself in the build up of funds on the road to new record levels, as this more cautious approach taken by investors has lengthened the fundraising process for managers beyond initial projections.

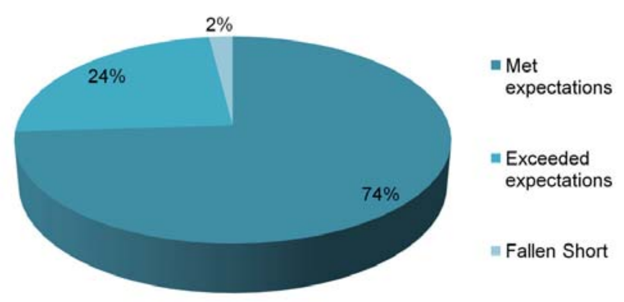
The evidence would suggest that managers currently raising new vehicles should take extra care in emphasising how they intend to deal with credit conditions when marketing funds to a more apprehensive investor community.

Have investors’ private equity fund investments lived up to expectations?

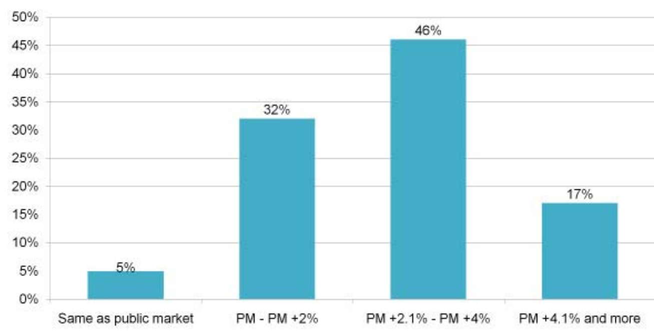
Perhaps unsurprisingly when the future private equity allocation results are considered, the majority of investors have been satisfied with the returns from their private equity portfolios. As the chart below shows, 74% of investors polled are satisfied with the returns from their private equity portfolios, with 24% going further than this, stating that results had actually exceeded their expectations. Only 2% of investors felt that their investments had fallen short of expectations.

Public pension plans, private pension plans, and asset managers were most satisfied with their private equity portfolio returns, with 33% stating that returns had exceeded expectations. The least enthusiastic group of investors were family offices, endowments and foundations, with only 12% of these investors having found

Have investors’ private equity fund investments lived up to expectations?



What returns do investors expect from their private equity portfolios?



Investor Spotlight: LP Survey Results

that returns exceeded expectations. This is possibly due to the higher expectations that investors of these types have of their portfolio when compared to other more conservative investor types.

What returns do investors expect from their private equity portfolios?

It is immediately obvious from the graph opposite that investors expect private equity to exceed the public markets, with only 5% of investors expecting returns to match public markets, and no investors expecting their private equity portfolio to underperform this benchmark.

A significant 32% of investors expect returns in the range of up to 2% above public markets, and 46% of all investors expect returns to exceed the public markets by between 2.1% and 4%. A total of 17% of investors fall into the most ambitious category of expecting returns to exceed 4.1%.

In terms of average expectations, the results indicate that the average institutional investor expects returns of 3.3% above public markets. Family offices, endowments and foundations collectively were most ambitious, with average expectations of public markets +3.7%, followed by public pension plans, private pension plans and asset managers, which collectively had an average returns expectation of public markets + 3.5%. A group comprising banks, insurance companies and corporate investors were most conservative with their expectations from their private equity portfolio, expecting returns at just 2.2% over public markets.

Where will investors be looking to expand in the future?

During the LP survey, respondents were asked where future areas of interest lay, both geographically and in terms of fund type. A wide variety of responses were given, but one trend that is easily identifiable is that investors are planning to widen their portfolio geographically. Of those investors polled, 59% intended to invest in Asia and other emerging markets, or on a global basis. China and India were especially prevalent amongst responses relating to future ambitions.

In terms of fund types, most LPs intended to continue with the established fund types such as buyout, venture, mezzanine and fund of funds. Some LPs did state that they would be focusing more on identifying opportunities in smaller buyout funds, and in growth funds as opposed to the larger mega buyout vehicles. Other popular responses included infrastructure, special situations and distressed debt- all fund types that have experienced growth over recent years. On this evidence it appears that this growth is sustainable, with investors still keen to gain exposure to these emerging fund types.

Investor Spotlight: News

The sale of a portfolio of private equity fund interests on the secondary market by **California Public Employees' Retirement System (CalPERS)** appears to nearly be at an end. Several potential buyers are rumoured to be taking substantial portions of the offering, including HarbourVest Partners, Lexington Partners, Coller Capital, Pantheon Ventures and Oak Hill Investment Management. Up to 20 further bidders are competing for smaller pieces of the portfolio.

BlackRock Private Equity Partners has invested in New Atlantic Venture Fund III, which has held a first close with USD 75 million in commitments. This latest fund commitment follows the UK-based fund of funds manager's announcement in Q4 2007 that it will be looking to commit up to USD 750 million to the private equity asset class over the next 12 months. New Atlantic Venture Fund III will give investors exposure to US firms in the IT, technology and Internet sectors. Other investors in the fund include Adveq Group.

Sacramento County Employees' Retirement Association (SCERS) has chosen three fund of funds managers to run mandates for its maiden allocation to private equity. It has selected **Abbott Capital Management**, **Goldman Sachs Asset Management** and **HarbourVest Partners** to handle its maiden 5% allocation to the asset class. The pension fund is planning to allocate USD 75 million each to the latest fund of fund vehicles from Abbott Capital Management and Goldman Sachs Asset Management, and a total of USD 50 million to the combination of a domestic and international focused fund of funds from HarbourVest Partners. The pension fund's decision to opt for fund of funds for its private equity investment strategy was motivated mainly by a desire for a diversified portfolio along with concerns over limited staffing.

European Investment Fund (EIF), in conjunction with Technology Foundation of Turkey, SME Development Organisation of Turkey and Development Bank of Turkey launched Istanbul Venture Capital Initiative to serve as a catalyst for the private equity industry in Turkey. EIF is expected to invite blue chip Turkish and international institutions to partake in the vehicle, which is targeting EUR 200 million and held a first on close on EUR 150 million in November 2007.

Folksam, which has SEK 175 billion in assets under management, appointed Johan Held as its head of private equity. He will be responsible for kick starting the private equity investment activity of Folksam. It previously invested on a small scale but has not maintained an allocation for several years. It is likely that the investor will shortly set a new target allocation to the asset class but it has already started to make some new fund investments. It anticipates making fund of funds the main focus of investment for its private equity activity.

Vital Forsikring and **Oslo Pensjonsforsikring** have announced that they are to increase their allocation to private equity. The government of Norway has announced that it is to increase the allowance to alternative assets from 5% to 7% of total assets under management. This new figure is significantly lower than the expected allocation of up to 20%, but following the recent hedge fund scandal where four municipalities suffered significant losses from housing loan investments, the government have decided to act with caution. Vital Forsikring is to increase its 2% allocation to private equity and Oslo Pensjonsforsikring (OPF) is also expected to follow suit and increase its allocation to the asset class.

San Francisco City and County Employees' Retirement System (SFERS), which has a 12% target allocation of its total assets for its private equity investments, is seeking for advisors for its alternative investments because its current advisor Portfolio Advisors is in the last year of a five year contract as SFERS' alternative investment consultant and private equity advisor. The renewal of Portfolio Advisors' contract will still be an option for SFERS and as part of its efforts for renewal the advisor has outlined a series of strategies for investment, one of which includes a proposed larger allocation for secondary market opportunities.

VCM has opened a new office in Paris in order to expand its investor base abroad. The office will be led by managing director Pascal Feucher who will be in charge of client relationships in France and Italy and will be co-managing VCM's portfolio of mezzanine funds.

Each month Spotlight provides a selection of the recent news on institutional investors in private equity.
More news and updates are available online for Investor Intelligence subscribers.
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2008 Preqin Hedge Institutional Investor Directory: Order Form

The 450 page 2008 Preqin Hedge Institutional Investor Directory is the leading source of information on institutional investors in hedge funds, and is an essential purchase for all hedge fund managers and marketing professionals.

- Detailed analysis on the make up of the investor universe, plus latest investor trends, including the full results of our 2008 investor survey.
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