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# The Preqin Quarterly

Private Equity - Insight on the quarter from the leading provider of alternative assets data

Q2 2011 JULY 2011

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## Private Equity Secondary Market Is Heating Up

Recent large transactions suggest that predictions for an upturn in the market were right.

## Meeting LP Demand

We examine what LPs are currently demanding from their private equity investments.

## Latest Fundraising Figures

For the second consecutive quarter, we have seen some improvement in private equity fundraising.

## Private Equity-Backed Deals

Deal flow reached a post-Lehman high this quarter.

Q2 Special Guest Contributor: David Chamberlain, Capstone Partners

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# Editor's Note

For the second consecutive quarter, we have seen some improvement in private equity fundraising and there is evidence to suggest the start of a gradual recovery in capital raising for new vehicles. Increased exit flow and, by extension, distributions have led many institutional investors to pick up the pace at which they make new commitments to funds and this is gradually being reflected in fundraising levels. In addition to the 201 funds that reached a final close in the second quarter, raising a combined $66.9bn, a further 115 funds held interim closes, having secured $24.1bn so far.

Delving deeper into the fundraising statistics reveals that the picture is more mixed than it appears on first glance. Venture funds had a difficult quarter, with closed funds raising just $5.8bn, 42% less than the $10bn secured the previous quarter. Buyout funds raised $15.3bn this quarter, a small increase on the $13.9bn secured in Q1 2011. Real estate funds had a strong quarter, with 19 closed funds raising an aggregate $11.9bn, which includes $5.5bn raised for Lone State Real Estate Fund II. More on fundraising this quarter can be found on pages 10 to 14.

While overall fundraising levels are set to increase, conditions will remain extremely challenging for GPs on the road. Investors may be starting to pick up the pace of their commitments, but they are expecting more from their investments: in December 2007, just 17% of LPs we interviewed expected their private equity investments to outperform public markets by more than 4%, but in June 2011, this has risen to 69% of respondents. Furthermore, LPs can afford to be highly selective in their investments. 1,665 funds are on the road at present competing for LP commitments, just slightly below the peak number of funds in market of 1,673 seen in Q2 2009. We examine what LPs are currently demanding from their private equity investments on page 8.

This year has seen an improvement in secondary market deal flow and a number of high-profile deals have been finalized in recent months, including AXA Private Equity's purchase of a $1.7bn portfolio from Citigroup. Secondaries fundraising was also bolstered this quarter by the final close of Lexington's seventh fund on $7bn, making it the largest fund to close in Q2 2011. Please see page 6 for more information.

We are also thrilled to have a guest article from David Chamberlain at leading placement agent Capstone Partners, which provides further perspectives on the key trends affecting the industry.

Behind each of the data-points you see in the Preqin Quarterly exists a wealth of information on our industry-leading online products and publications, with extensive profiles for firms, funds, investors, consultants, law firms, placement agents and more. Our approach to being the most accurate source of intelligence is simple: we maintain offices around the world filled with dedicated analysts directly contacting industry professionals on a regular basis, over 5,000 of whom are Preqin subscribers.

We hope that you find this report to be interesting and informative and as ever we welcome any feedback that you may have. If you would like more information on any of our products and services, please feel free to contact us at our New York, London or Singapore offices.

Helen Kenyon, Editor

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# David Chamberlain, Capstone Partners

Interview with David Chamberlain
Conducted by Claire Wilson, June 2011.

How has the fundraising market changed over the past 12 months?

As a firm we believe there has been a clear, positive change in the market, both in terms of activity and investor sentiment. However, this may not yet be reflected in the fundraising statistics. The 2010 and early 2011 numbers do not look good. Somewhere in the region of $225bn of capital was raised in 2010, which was the lowest yearly amount since 2004. The reason for this is that many funds that had planned to return to market in 2009/2010 held back to wait for a better environment. This was particularly true of large buyout funds, which tend to skew the stats. We're faced with the same statistical anomaly in Q1 2011, particularly in Europe, with capital raised representing just 15% of global capital. It's probably driven by the way the stats are recorded - only the final closes are counted and it doesn't reflect the number of funds in market or include the funds that have held a first close.

Is it fair to say that the short-term outlook for the market is fairly positive?

Despite this grim statistical news, we, as a global placement firm, continue to see a positive change to investment sentiment and ambition. Our discussions with GPs and LPs around the world clearly indicate a significant upturn in activity and confirm the conclusions of recently released reports.

On the demand side, many investors will be coming back to invest in funds with either unchanged or increased allocations to the asset class. Maybe the only exception will be funds of funds that themselves have had difficulties raising capital over the last 2-3 years and will therefore suffer from a knock-on effect in their capacity to invest in 2011/12.

On the supply side, we already know many GPs have delayed fundraising into late 2011/2012, not just due to the reluctance of investors to deploy capital, but also due to a general lag in their own investment activity in 2009/2010. Many GPs have yet to reach their 75% threshold and so are not technically in a position to raise a new fund. Furthermore, they need to generate performance in order for people to support them in their next fundraise. Clearly, the return of the mega funds will boost the statistics.

What type of activity do you expect to see in the fundraising market over the next 12 months?

It's becoming clear that 2011/12 will be seen as years of re-ups, with intense activity amongst investors and GPs alike.

The number of funds coming to market is substantial and it'll be interesting to see how the investor community is going to digest it all. There will certainly be a decline in the number of re-ups, driven by disappointing performance, team changes, investment overlap with other GPs, generational issues and relationship fatigue. Performance will ultimately be the measuring stick and investors will certainly have their work cut out over the next 18-24 months as they try to bench-mark and evaluate the relative performance and true value creation of GPs.

This great wave of returning GPs looking for re-ups will make it tough for new private equity firms. Normally, coming out of an economic shake-up, you would expect to see a number of new firms emerging with new ideas, and ambitious, young, talented people with a hunger for success. Unfortunately, few have made the breakthrough in 2008-10 due to the reluctance of investors to invest. The great wave of returning funds in 2011-12 will provide a different sort of barrier to entry as investors focus much of their attention on cleaning up their existing GP relationships.

To what extent has the market recovered at this juncture?

"Recovery" may not be the best description of what's happening in the market. The macro position of the markets, in the sense of what should be driving investor activity, hasn't

improved, and so it's difficult to claim a recovery. Western economies remain sluggish; the public equity markets show continued signs of weakness and volatility, bond markets have not recovered; there are deep concerns surrounding the political and economic stability of countries in Europe, which in turn has upset the currency markets. Add to this the issues and possible consequences of the planned solvency and banking regulations which will surely affect private equity.

Nevertheless, the market has reached the point where it needs to move on, so if there is a "recovery", it is being driven more by the underlying structure of private equity; funds get raised every four or five years, and once the current funds have been invested, like it or not, GPs need to return to market to raise new capital. So it is the structure of private equity that is driving the so-called "recovery".

It is interesting to note that deal activity has been particularly strong in the mid market. Prices are returning to pre-crisis levels and there has been a recovery in the debt markets, as banks are more willing to lend. Again, the "recovery" in investment activity may in part be driven more by the underlying structure of private equity funds and the need to deploy capital rather than a pipeline of really good investment opportunities.

There has been another contributor to the "recovery": the increased role of the secondaries market. Secondary firms have improved liquidity options for investors, enabling certain institutional investors to clean their portfolios and build new GP relationships. We see this as a healthy contribution to the market.

How have you adapted your business in these changing times?

From the outset we tried to build an entrepreneurially led business. Ownership is well spread, rather than being amongst just one or two people. As a result, we have highly motivated professionals who really share in the responsibility of making our business a success. This has led to remarkable stability within the team despite the prolonged turmoil in the fundraising market.

In response to the changing needs and growing sophistication of investors, we have made significant investments in people and infrastructure. We have continued to recruit senior professionals to both our North American and European offices. I'm pleased to say that we have succeeded in building an active placement presence in the Middle East, a region which will continue to grow as an important source of capital. We have also established a fully fledged operation in Asia to originate new fundraising mandates as well as to place funds with new, local investors. We opened our office in Shanghai in early 2009, at the height of the financial crisis, with the clear aim of providing a global platform for our GP clients and to become an active player in the emerging private equity industry in Asia.

Do you think we will ever see a return to fundraising levels seen in 2007?

This is a complicated issue. In many respects, the amount of capital allocated to private equity has not significantly changed since 2007. Some institutional investors have cut their allocations; others have stopped investing altogether. But others, as recent reports show, will maintain their programs or even increase their allocation to the asset class. So the amount of money at work in private equity is possibly still at 2007 levels.

What has changed is the availability of capital to be invested in new relationships. If we look back at 2004-07, many investors were still in the process of building out their investment portfolios. There was therefore a much higher propensity to invest into new funds. In addition, at the height of the boom, investors were inflating their portfolios with leverage, either in the form of over-commitment strategies or with debt. Obviously, this has now disappeared from the market.

In today's new environment, the combination of more mature investment portfolios and no leverage will reduce significantly the appetite and capacity of investors to commit to new GP relationships. This will change over time as a result of the on-going clean-up of investment portfolios and by new capital entering the asset class.

To conclude on an optimistic note, we all hope that private equity will remain an attractive asset class for investors. Its ability to come through the crisis of the last few years and continue to outperform the public markets should attract new capital and increased allocations.

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# Private Equity Secondary Market Heating Up

With reports of a considerable number of secondary market deals completing during the first half of 2011, expectations of an increase in secondary market deal flow over the course of the year seem likely to be met. Recent large transactions, including AXA Private Equity's purchase of a $1.7bn private equity portfolio from Citigroup and Pantheon International Participations' recent purchase of a $40mn portion of a $500mn portfolio of private equity fund stakes, are all contributing to the increase in secondary market deal volume in 2011 compared to previous years.

Improving cash flow in investors' private equity portfolios has seen fewer distressed sellers being forced to offload interests in funds on the secondary market. However, we are still seeing a good supply of fund stakes being offered up for sale by LPs seeking to manage their portfolios. 17% of investors spoken to by Preqin over the past year have indicated some degree of interest in making a secondary market sale within the following 24 months.

One notable investor that recently decided to place a portfolio up for sale is New Jersey State Investment Council. The $74.7bn public pension fund is looking to sell off a large portion of its portfolio in order to make room for new private equity investments and establish relationships with other managers, a strategy that has been employed by several investors in recent months.

Investors bringing portfolios to the secondary market in the coming months are unlikely to be short of offers for their portfolios as there is still a considerable amount of capital available to be deployed into the market. While secondaries fundraising was slow in 2010, secondary fund of funds managers are still sitting on a significant amount of dry powder; from the start of 2009 to the end of H1 2011, $43.5bn was raised by dedicated secondaries funds and, with secondary market deal flow remaining at low levels in 2010, managers will be looking to put a considerable amount of this capital to work in the coming months.

One manager that will be actively seeking to purchase portfolios of secondary interests in the coming months is Lexington Partners. It closed its latest vehicle, Lexington Capital Partners VII, in June 2011 after collecting $7bn from investors, making it the biggest secondaries fund ever raised. This was $1bn over its initial target, suggesting continued investor appetite for the market.

Fig. 1: Top 5 Secondary Transactions in H1 2011

| Seller | Buyer | Price (mn) |
|---|---|---|
| Citigroup | AXA Private Equity | $1,700 |
| Alberta Investment Management Corporation | Goldman Sachs Private Equity Group | $800 |
| California Public Employees' Retirement System (CalPERS) | AlpInvest Partners, Other Unidentified Buyers | $800 |
| Lloyds Banking Group | Lexington Partners | £470 |
| Barclays Bank | AXA Private Equity | $740 |

Fig. 2: Top 5 Secondaries Funds Currently Raising

| Fund | Target Size (mn) | GP Location |
|---|---|---|
| Coller International Partners VI | $5,000 | UK |
| AXA Secondary Fund V | $3,500 | France |
| CS Strategic Partners V | $2,500 | US |
| Pinebridge Secondary Partners III | $1,300 | US |
| Greenpark International Investors IV | $1,200 | UK |

## Global private equity fundraising

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# Meeting LP Demand

The private equity market has suffered in the years following the financial crisis. Diminished LP confidence, teamed with the denominator effect, led to a significant reduction in the number, and value, of fund commitments being made. However the pace of new commitments is gradually increasing and conversations with investors over the course of 2011 have indicated that the majority of LPs are keen make new commitments to funds.

Although LPs are picking up the pace of their commitments, they are a lot more discerning when choosing funds to commit to than in the years prior to the financial crisis, and with so many funds on the road to choose from, LPs are well positioned to be selective. Competition between fund managers remains high and, to secure a commitment, managers need to know exactly which LPs to target and how best to approach them.

In June we interviewed 100 LPs to find out their attitudes to the current market, how their portfolios are performing and their plans for future investments.

### LPs' Returns Expectations

A fund's performance potential is a crucial factor that LPs consider when selecting funds to invest in – 69% of investors we spoke to in June expect their overall private equity portfolio to generate returns in excess of 400 basis points over the public market benchmark (see Fig. 3). To attract LPs, fund managers need to prove that they can generate strong returns from their investments at all points during the market cycle. We spoke to a German LP earlier in the year who noted that "GPs need to show they have managed the crisis well. Their portfolios need to be in good shape and they need to show they can do good deals going forward."

A number of investors we spoke to feel that private equity has not yet fully recovered from the financial crisis, and remain realistic about the returns the asset class can achieve. Along with 68% of investors (see Fig. 4), one Helsinki-based asset manager feels its private equity returns have met its expectations telling us: "Our private equity investments were exceeding expectations before the collapse of Lehman Brothers and the financial crisis, but now our investments are only meeting our expectations."

Another LP, based in the Netherlands, stated: "We would expect our private equity returns to be between 2.1% and 4% above the public market; this is a risk-adjusted premium and we believe this return to be achievable."

In the current market, investors need to regain confidence in the asset class, and with so many funds to choose from, they are able to take the time to ensure they feel confident they are allocating their capital to the best teams that have proven consistent returns. When asked what it takes for a GP to secure a commitment from them, one US insurance company told us: "Proven performance is the number one thing that GPs need to have."

Fig. 3: Investors' Returns Expectations for Their Private Equity Portfolios

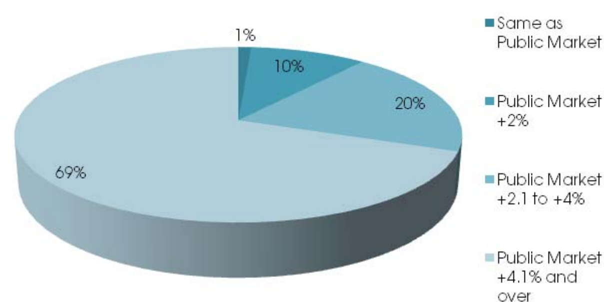
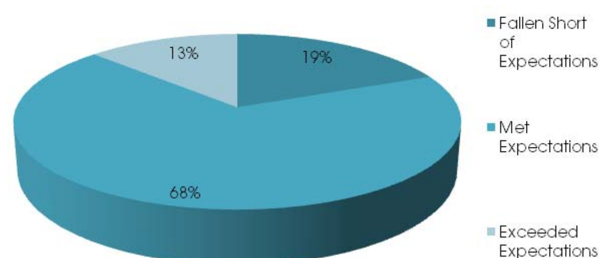



Fig. 4: Proportion of Investors That Feel Their Private Equity Fund Investments Have Lived Up to Expectations



### Importance of Fund Terms and Conditions

As GPs compete for commitments, LPs are increasingly having more say when negotiating terms and conditions for funds. In recent months we have seen a number of fund managers accommodating LP demands. California Public Employees' Retirement System (CalPERS) recently negotiated reduced fees with its longstanding manager Apollo Management, and the fund manager also agreed to forgo the use of placement agents when seeking capital from the pension fund.

The terms and conditions of funds can and have deterred investors from making commitments to otherwise attractive opportunities. In May Preqin interviewed 50 prominent LPs from around the world to discuss their opinions on fund terms and conditions and found that a significant 55% of investors have previously chosen not to invest in a fund because of the proposed terms and conditions. One US endowment, a well established investor in private equity, told us: "[We] constantly choose to not invest in appealing funds because of terms, it happens every day."

In this competitive fundraising market, LPs are in a strong position to negotiate on terms, and to stand the best chance of securing commitments, GPs need to be open to negotiations and willing to adapt their terms to meet LP requirements.

### How Long Do LPs Expect the Shift to Last?

Over the last few years the balance of power has certainly shifted more towards the LP when it comes to negotiating on issues such as fund terms and conditions with managers. However, will the balance of power revert back to GPs once the market fully recovers? While some investors feel that the changes in prevailing terms will be temporary, GPs should be aware that a significant 50% of investors expect the shift in prevailing terms to persist in the longer term (Fig. 5).

### Investors' Plans for 2011 and Beyond

A sizeable 64% of investors have made new commitments to funds so far in 2011 and, as Fig. 6 shows, an encouraging 57% of LPs expect to make additional fund commitments before the end of the year. It is also important to note that 16% of LPs will invest if they see attractive opportunities arise; therefore fund managers need to make sure they know how to target these potential LPs so that they really stand out from the crowd.

To secure capital from these investors GPs need to ensure that they are targeting the right investors, and in the right way. One Norwegian insurance company told us: "If GPs do not have the same investment philosophy as we do, then it is pointless approaching us as they will not receive our business."

Fig. 5: Changes in Prevailing Terms in the Last Year: LPs' Perceptions of How Permanent the Changes Are

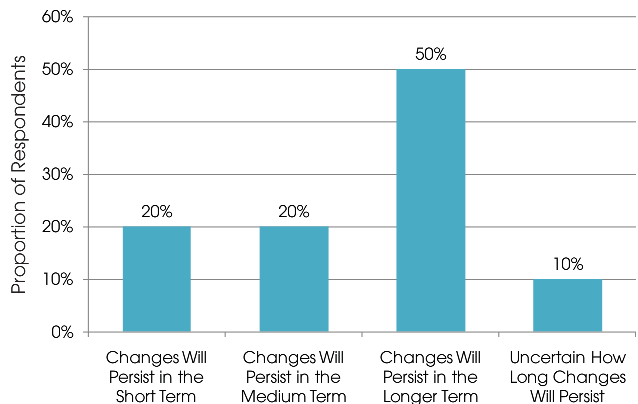
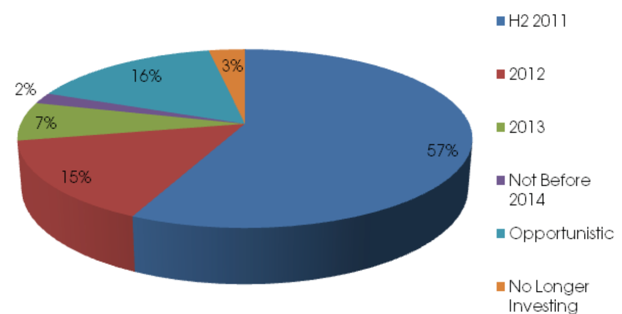



Fig. 6: Time Frame for Next Intended Commitments to Private Equity Funds




Maintaining good relationships is essential, and fund managers need to be mindful of their investors' needs. A Finnish LP told us that to secure a commitment "GPs need to have stability, a good record; they need to be service orientated, and not have a bad attitude. We increasingly have fewer good relationships with GPs." A notable sovereign wealth fund emphasized this point, commenting: "GPs need to remember that they are in partnership with LPs and need to treat them with respect."

### Outlook

As the shake-up of the private equity industry following the market slump is beginning to settle, investors are picking up the pace of their investments. In the years following the crisis, investors have become far more prudent about the investments they make. LPs have higher expectations of their fund managers, and with so many funds competing to secure their capital, LPs are able to pick and choose funds to commit to. GPs should take the time to look after the requirements of LPs in their funds, as well as new investors, in order to build and maintain lasting and successful relationships.

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# Fundraising Overview

During Q2 2011, 120 private equity funds held final closes worldwide, raising an aggregate $66.9bn, as shown in Fig. 7. This is the second consecutive quarter-on-quarter increase in private equity fundraising; however, the market remains depressed compared with the levels of commitments that were garnered in the pre-global financial crisis era. These figures would suggest that fundraising market conditions still present difficulties to fund managers seeking investor capital commitments, even with some very successful fundraising efforts during the quarter, such as the EIG Energy Fund XV, which surpassed its target of $2.5bn with total commitments of $4.1bn.

Fig. 8 displays the length of time that funds which closed in Q2 2011 spent on the road, and illustrates a continued positive trend in the fundraising market. Just over a quarter (28%) of funds that reached a final close in Q2 2011 had been in the market for less than six months. A further 18% of funds took in between seven and 12 months to raise, meaning that almost half of funds closed in the second quarter of 2011 managed to conclude their fundraising in under a year. This is up from the previous quarter, during which 41% of funds completed a final close within a year. Furthermore, all funds that closed during Q2 2011 did so in less than 36 months, while 6% of those that closed during Q1 2011 took more than three years to reach a final close. Additionally, 112 funds in market held an interim close during Q2 2011, and collected more than $24bn in capital towards their overall targets.

Buyout funds raised the most capital in Q2 2011; $15.3bn was collected by 21 such funds, as shown in Fig. 9. This figure is a slight improvement on the amount raised in Q1 2011, during which buyout funds raised the lowest amount of capital since Q4 2004 ($13.9bn in Q1 2011 compared with $11.8bn in Q4 2004). Buyout funds were also the most abundant fund type in terms of the number of funds to close, with 21 vehicles closing in the quarter, followed by 20 venture capital vehicles. The second-largest amount of capital raised in the period was accounted for by real estate funds, which raised an aggregate $11.9bn. Fig. 10 shows details of the 10 largest funds to close during Q2 2011.

Fig. 7: All Private Equity Fundraising by Quarter, Q1 2004 - Q2 2011

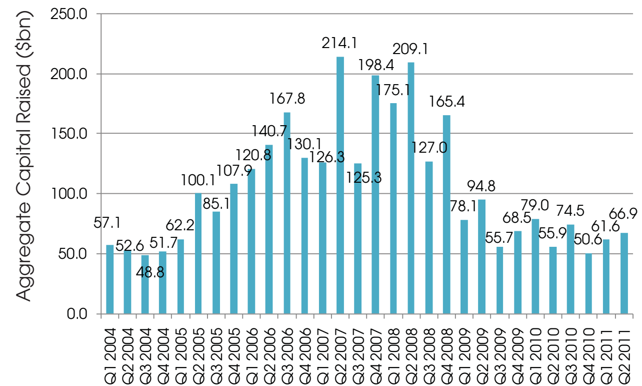


Fig. 8: Time Spent on the Road for Funds Closed in Q2 2011

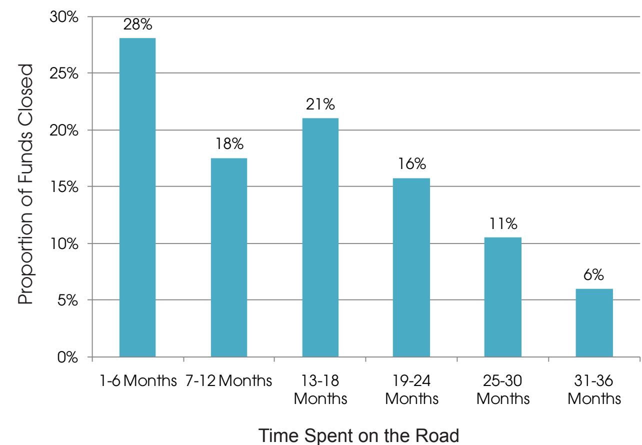


Fig. 9: Private Equity Fundraising by Type, Q2 2011

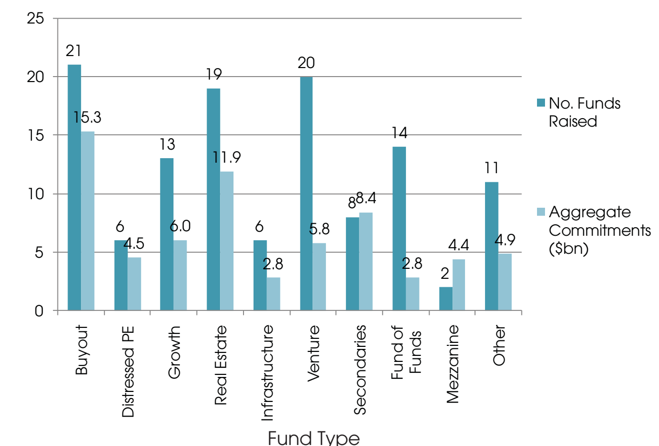




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Fig. 10: Top 10 Funds Closed during Q2 2011 by Final Close Size

| Fund | Fund Manager | Type | Final Close Size (mn) | Manager Location | Fund Focus |
|---|---|---|---|---|---|
| Lexington Capital Partners VII | Lexington Partners | Secondaries | 7,000 USD | US | US |
| Lone Star Real Estate Fund II | Lone Star Funds | Real Estate | 5,500 USD | US | US |
| EIG Energy Fund XV | EIG Global Energy Partners | Mezzanine | 4,120 USD | US | US |
| Montagu IV | Montagu Private Equity | Buyout | 2,500 EUR | UK | Europe |
| OCM Opportunities Fund VIIIB | Oaktree Capital Management | Distressed Debt | 2,600 USD | US | US |
| KSL Capital Partners III | KSL Capital Partners | Buyout | 2,000 USD | US | US |
| Gávea Investment Fund IV | Gávea Investimentos | Hybrid | 1,800 USD | Brazil | ROW |
| BTG Pactual Brazil Investment I | BTG Pactual | Buyout | 1,600 USD | Brazil | ROW |
| Bessemer Venture Partners VIII | Bessemer Venture Partners | Venture | 1,600 USD | US | US |
| Vinci Partners I | Vinci Partners | Growth | 1,400 USD | Brazil | ROW |

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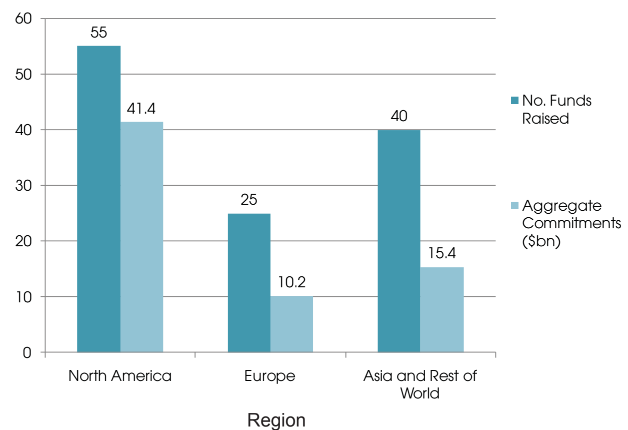
# Regional Fundraising

Out of the 120 funds that reached a final close in Q2 2011, 46% are primarily focused on making investments in North America. These funds account for 62% of the aggregate capital raised in the second quarter of 2011. This is four percentage points more than the proportion of total capital that was raised by funds with a North American investment focus in the previous quarter. Asia and Rest of World-focused funds raised the second-largest amount of capital in Q2 2011, which makes two successive quarters that Asia and Rest of World-focused funds have raised more capital than their European counterparts.

Fig. 11 shows that 55 funds with a primary regional focus on North America completed their fundraising campaigns in Q2 2011. This is a noticeable decrease from the number of funds that reached a final close in the previous quarter, down from 67 funds, but a substantial increase in the aggregate capital raised, up from $35.5bn last quarter to $41.4bn. The number of Europe-focused funds that reached a final close during Q2 2011 also decreased, with 25 funds completing the fundraising process in Q2 2011 compared to the 38 that closed in the previous quarter. These funds raised slightly more capital than in Q1 2011, but accounted for the same proportion of total capital raised across all regions, $10.2bn, representing 15% of the global total was raised this quarter compared to $9.4bn, also representing 15% of the total, raised in the previous quarter.

The number of Asia and Rest of World-focused funds reaching a final close increased by one this quarter, but the capital raised by such funds decreased along with their proportion of total capital raised globally. 39 funds with a primary investment focus in Asia and Rest of World closed in Q1 2011, raising an aggregate $16.7bn, which equated to 27% of capital raised in the quarter. In Q2 2011, $15.4bn was collected by 40 funds and accounted for 23% of total global capital raised.

Fig. 11: Private Equity Fundraising by Primary Geographic Focus, Q2 2011



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# Buyout and Venture Fundraising

An aggregate $15.3bn was raised by 21 buyout funds that closed in Q2 2011, as shown in Fig. 12. In comparison to Q1 2011, these figures represent an increase in capital of $1.4bn, or 10%, and a decrease of 9% in the number of funds closed.

The largest buyout vehicle to close in Q2 2011 was Montagu IV. The fund, which focuses on investment in consumer products and services, healthcare and manufacturing in Europe, closed above its €2bn target on €2.5bn. Another fund to hold a final close during the quarter exceeding its target was KSL Capital Partners III, the second-largest buyout vehicle to close in the quarter. This vehicle, managed by KSL Capital Partners, focuses on making operational improvements in real estate companies in North America. This fund targeted $1.5bn but surpassed this to raise $2bn when it held its final close in June 2011.

The number of venture capital vehicles reaching a final close in Q2 2011 stood at just under two-thirds of the number that closed in Q1 2011, 20 such funds closing in Q2 2011 compared to 32 in Q1 2011. Venture funds clsoing in Q2 2011 garnered $5.8bn in aggregate capital, representing a 42% fall from the $10bn in capital commitments in Q1 2011.

Bessemer Venture Partners VIII was the largest venture fund to reach a final close in Q2 2011. The fund, managed by Bessemer Venture Partners, focuses on investments in high-growth companies across multiple industries and geographies. It invests out of US, Israel and India offices, with a quarter of the fund's capital targeting investment in Indian companies. The second-largest venture vehicle to close in Q2 2011 was IDG-Accel China Capital Fund II. It held a final close in April 2011, raising $750mn in the space of three months.

Fig. 12: Private Equity Buyout Fundraising by Quarter, Q1 2008 - Q2 2011

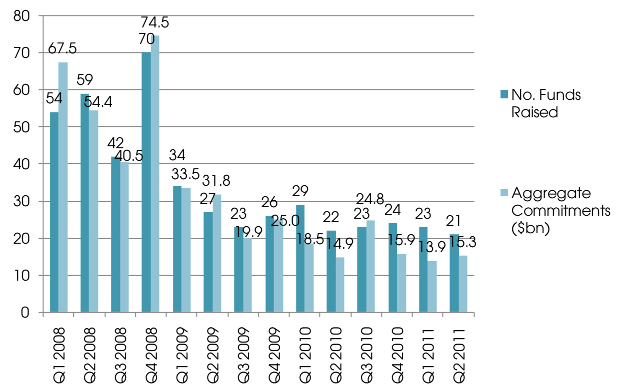


Fig. 13: Private Equity Venture Fundraising by Quarter, Q1 2008 - Q2 2011

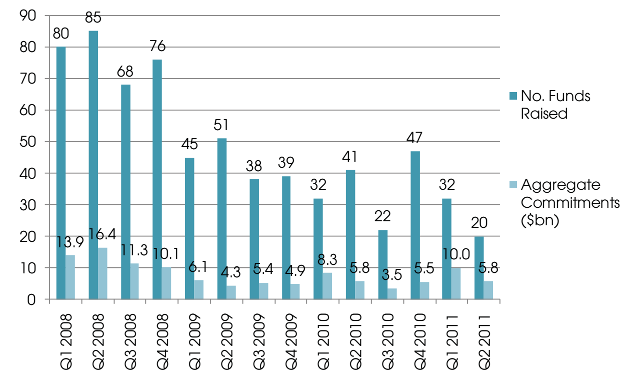


Fig. 14: Five Largest Buyout Funds Closed in Q2 2011

| Fund | Fund Manager | Size (mn) |
|---|---|---|
| Montagu IV | Montagu Private Equity | 2,500 EUR |
| KSL Capital Partners III | KSL Capital Partners | 2,000 USD |
| BTG Pactual Brazil Investment I | BTG Pactual | 1,600 USD |
| Chequers Capital XVI | Chequers Capital | 850 EUR |
| Oaktree Power Opportunities Fund III | Oaktree Capital Management | 1,040 USD |

Fig. 15: Five Largest Venture Funds Closed in Q2 2011

| Fund | Fund Manager | Size (mn) |
|---|---|---|
| Bessemer Venture Partners VIII | Bessemer Venture Partners | 1,600 USD |
| IDG-Accel China Capital Fund II | IDG Capital Partners | 750 USD |
| IDG-Accel China Growth Fund III | IDG Capital Partners | 550 USD |
| Accel XI | Accel Partners | 475 USD |
| Qiming Venture Partners III | Qiming Venture Partners | 450 USD |

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# Private Equity Fundraising: Other Types

Just over two-thirds of private equity capital raised in Q2 2011 was committed to fund types other than buyout and venture. Of these vehicles, real estate and secondaries raised the most capital.

As shown in Fig. 16, eight secondaries funds raised a combined total of $8.4bn in Q2 2011. Just two secondaries vehicles closed in Q1 2011, raising an aggregate $250mn and accounting for just 0.4% of the total global private equity capital raised, while those closed in Q2 2011 account for 15% of aggregate global fundraising. The $8.4bn raised in Q2 2011 was largely due to the final close of Lexington Capital Partners VII, the biggest fund to close in the quarter. This global vehicle finished fundraising in June 2011 on $7bn, exceeding its $6bn target.

19 real estate funds reached a final close in the quarter garnering an aggregate $11.9bn. Although fewer funds closed in Q2 2011 than in Q1 2011, 19 compared to 30, the aggregate capital raised increased by $3bn to $11.9bn in Q2 2011. Lone Star Real Estate Fund II was the largest real estate fund to close in Q2 2011, surpassing its $4bn target to reach a final size of $5.5bn. The fund features in Fig. 17, which shows the 10 largest funds to close in Q2 2011, excluding buyout and venture funds.

Following Lexington Capital Partners VII and Lone Star Real Estate Fund II, EIG Energy Fund XV was the next largest non-buyout or venture fund to close in Q2 2011. It reached a final close on $4.12bn and is one of two mezzanine funds to feature in Fig. 17.

OCM Opportunities Fund VIIIB is the larger of the two distressed debt funds to feature in Fig. 17. Oaktree Capital Management manages the fund and the firm has a global focus, specializing exclusively in alternative and inefficient investment markets.

Fig. 16: Private Equity Fundraising (Excluding Buyout and Venture Funds) by Fund Type, Q2 2011

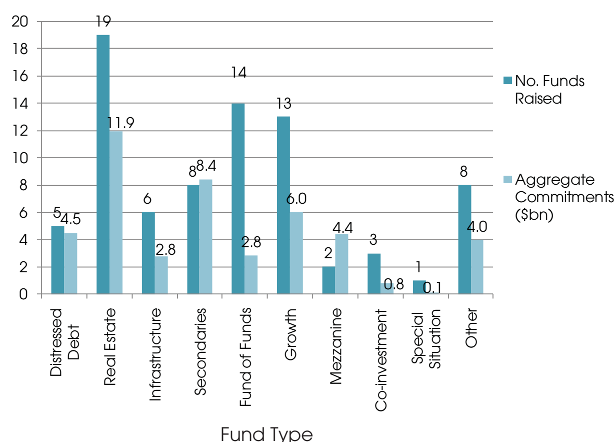


Fig. 17: 10 Largest Funds (Excluding Buyout and Venture Funds) Closed in Q2 2011

| Fund | Fund Manager | Fund Type | Size (mn) |
|---|---|---|---|
| Lexington Capital Partners VII | Lexington Partners | Secondaries | 7,000 USD |
| Lone Star Real Estate Fund II | Lone Star Funds | Real Estate | 5,500 USD |
| EIG Energy Fund XV | EIG Global Energy Partners | Mezzanine | 4,120 USD |
| OCM Opportunities Fund VIIIB | Oaktree Capital Management | Distressed Debt | 2,600 USD |
| Gávea Investment Fund IV | Gávea Investimentos | Hybrid | 1,800 USD |
| First Reserve Energy Infrastructure Fund | First Reserve Corporation | Infrastructure | 1,228 USD |
| Energy Spectrum Partners VI | Energy Spectrum Capital | Infrastructure | 999 USD |
| CVI Credit Value Fund | CarVal Investors | Distressed Debt | 854 USD |
| Mesirow Financial Private Equity Partnership Fund V | Mesirow Financial Private Equity | Fund of Funds | 841 USD |
| Och-Ziff Real Estate Fund II | Och-Ziff Real Estate Advisors | Real Estate | 840 USD |



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# Funds on the Road Overview

The start of 2011 saw the most private equity funds on the road for over a year and a half, coupled with the highest aggregate capital targeted by funds in market for over half a year. Going into Q3 2011, both the level of capital sought by private equity firms and the number of funds in market have increased, with 1,665 funds on the road collectively targeting $673bn. This represents an increase of almost 12% in aggregate targeted capital since the start of the year and an increase of almost 2% since the second quarter of the year. Q3 2011 marks the fourth quarter-on-quarter increase in both the number of funds and aggregate targeted capital.

Fig. 18 displays the change in the number of funds on the road and aggregate capital targeted at the start of each quarter since Q1 2009. Since the start of Q3 2010, the number of funds in market has been growing steadily, increasing by over 9% over the period. In line with an increasing number of funds on the road and aggregate capital being sought each quarter, there has also been an increase in the average target size of funds on the road compared to the start of the year. At the start of Q1 2011, there were 1,594 funds in market seeking aggregate capital of $602bn, equating to an average target size of $378mn. Going into Q3 2011, the average target size stands at $404mn, representing a 7% increase.

The largest proportion of funds in market will primarily focus their investments on North America with 738 such vehicles primarily targeting an aggregate $313bn as shown in Fig. 19. These funds account for 44% of the number of funds on the road and almost half of the global aggregate target capital.

Europe-focused funds are targeting the second-largest amount of capital, with 389 vehicles seeking $183bn in investor capital, accounting for 24% of the number of funds in market and 27% of the aggregate targeted capital. Funds that primarily focus on Europe have the largest average fund size of all funds in market, with an average fund target of $470mn, compared to $424mn for North America-focused funds and $329mn for Asia and Rest of World-focused funds. There are currently 538 Asia and Rest of World-focused funds on the road targeting an aggregate $177bn in capital commitments. These funds account for 32% of the number of funds on the road and 26% of the global targeted capital.

The two largest funds currently in market are Apax Europe VIII and Blackstone Real Estate Partners VII. Apax Europe VIII is targeting capital commitments of €9bn for buyout investments in Europe across a range of industries. Blackstone Real Estate Partners VII is a global opportunistic real estate fund targeting $10bn in investor capital.

Fig. 18: Funds in Market by Quarter, Q1 2009 - Q3 2011

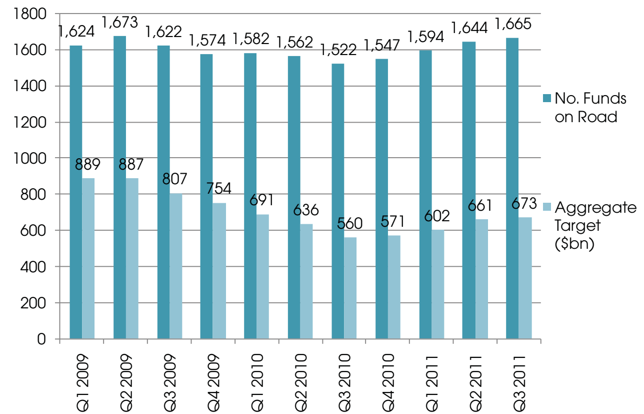
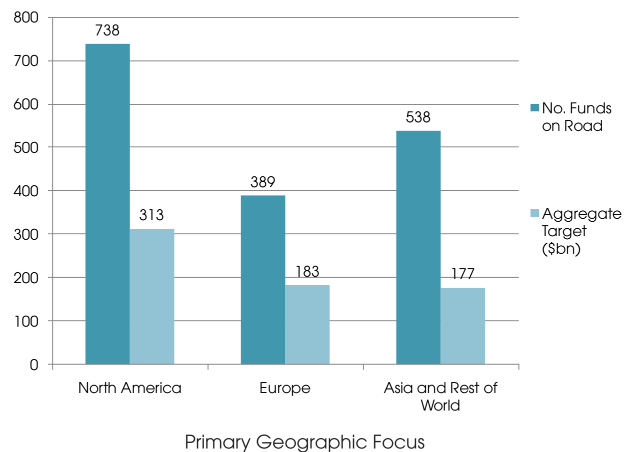



Fig. 19: Composition of Funds in Market by Primary Geographic Focus

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# Funds on the Road by Type

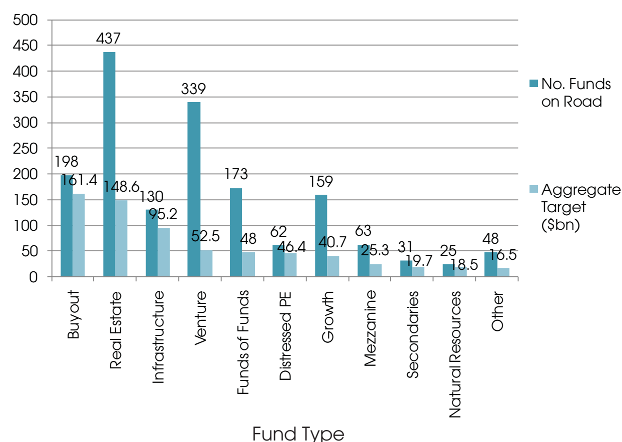
Buyout funds are targeting the largest amount of capital of all funds on the road, accounting for 24% of all commitments currently being sought by private equity funds in market, as shown in Fig. 20. Going into Q3 2011, there are 198 buyout vehicles on the road targeting $161bn in capital commitments.

Private equity real estate and infrastructure funds have the second and third-largest aggregate targets respectively, with 437 real estate funds aiming to raise $149bn and 130 infrastructure funds seeking $95bn in capital commitments. The two fund types account for 22% and 14% respectively of the aggregate target of all funds on the road.

Private equity real estate funds are the most numerous type of fund on the road followed by venture capital funds, with 339 such vehicles are in market, accounting for 20% of the total number of funds currently fundraising. Venture capital funds are targeting the fourth-largest amount of capital, with an aggregate target of $53bn. Khosla Ventures IV is the largest venture capital fund currently on the road, seeking $1.05bn in commitments. The fund targets early and late stage investments predominantly in the clean technology and information technology industries.

Funds of funds, distressed private equity funds, and growth funds all account for significant proportions of the private equity funds on the road. Fund of funds vehicles are the third most numerous fund type with 173 such funds currently in market targeting $48bn in commitments. Distressed private equity funds account for 7% of the total targeted capital, with 62 funds in market seeking $46bn. Growth funds account for 6% of all capital targeted, with 159 such funds looking to raise $41bn. Buyout funds alone have the largest average target size of all funds in market, $815mn.

Fig. 20: Composition of Funds in Market by Type




Preqin's Funds in Market database contains details of over 1,600 private equity funds on the road seeking capital, plus information on every vehicle that has closed since 2009. For more information about this product and how it can assist you, please visit:
www.preqin.com/fim



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# Fundraising Future Predictions

Private equity fundraising has been extremely challenging over the past couple of years. A record low was reached in Q4 2010, when funds that closed in the quarter raised just $50.4bn. Since then, fundraising has shown some small improvement, with closed funds securing $61.6bn in commitments in Q1 and $66.9bn in Q2.

So have we now passed the lowest point in the private equity fundraising cycle and are conditions set to get better?

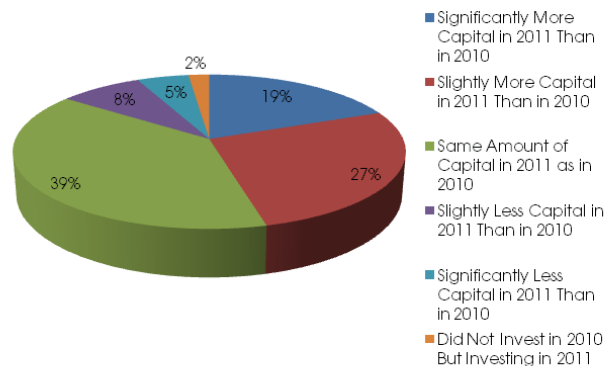
Improvements in fundraising rely upon two factors – a supply of good quality funds, and LPs with an appetite for private equity and capital available to put to work in the asset class. The supply of new opportunities has not been an issue over the past couple of years and 2011 has seen a number of big-name firms return to the market with new vehicles. At present, 1,665 funds are on the road actively being marketed to potential investors. In the 12-month period from July 2010 to June 2011, 585 funds closed, meaning that nearly three years' supply of funds is currently in market.

An abundance of new vehicles are also being launched: during Q2 2011, 120 funds reached a final close and left the market and 116 funds were launched. A considerable number of managers are also expected to begin fundraising for new vehicles in 2011-2012 as their existing funds wind up their investment periods.

The demand for private equity investments is still there and investor sentiment has remained resilient in spite of changing market conditions. 81% of LPs spoken to by Preqin in June 2011 felt their private equity investments had met or exceeded their expectations. The appetite of institutional investors for private equity over the longer term is also encouraging, with 21% intending to increase their exposure to the asset class over the longer term and 70% planning to maintain their current level of exposure.

LP appetite for private equity has remained strong but what about the level of LPs' planned activity over the next few months? Fundraising levels are a testament to the difficulty GPs have faced in securing commitments from investors in the recent past. A more cautious approach to investments and uncertainty in the market played a part, but we also saw many investors prevented from making new investments by a lack of capital available for new investments, frequently as a result of low levels of distributions caused by two years of poor exit conditions.

Fig. 21: Amount of Capital Investors Plan to Commit to Private Equity Funds in 2011 Compared to 2010




The rate of distributions from private equity funds is now picking up considerably, with exits of private equity-backed companies reaching record levels post-Lehman. In Q2 2011, there were 309 PE-backed exits valued at an aggregate $120.1bn, outstripping the previous record quarter of $81.5bn in Q4 2010 by a considerable margin. This has left investors with a significant pool of capital to recommit to new vehicles in order to maintain allocations.

Our recent conversations with LPs also indicate many intend to increase the pace of new commitments during 2011. 48% of respondents to our June 2011 LP survey plan to commit more capital in 2011 in comparison to 2010 and a further 39% intend to commit the same amount.

Further evidence for improved fundraising conditions can be seen in the length of time it is taking managers to raise new vehicles. During 2010, it took an average of 20.4 months from a GP starting to actively market its fund to it holding a final close. Funds closed in Q2 2011, however, took an average of 15 months to raise. It is also worth noting that 28% of funds closed in Q2 2011 took six months or less to raise, compared to just 10% over the course of 2010.

Overall, there is strong evidence to support our expectations that fundraising will continue to steadily pick up over the course of 2011. LPs are still keen to invest in private equity and now have increasing volumes of capital free to inject into new opportunities. Improvements in exit levels over the past few quarters should lead to increased LP activity which will be reflected in fundraising levels later this year. However, with so many funds still on the road, conditions are set to remain extremely competitive.

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# Deals and Exits Overview

Deal flow reached a post-Lehman high in Q2 2011; 674 PE buyout deals were announced globally with an aggregate value of $75.6bn, a 33% increase from the previous quarter and 37% higher than the same quarter last year. This is partially attributed to an increase in larger deals; 21 deals valued at over $1bn were announced during Q2 2011, accounting for 8% of total number and 49% of value, compared to 13 deals valued at over $1bn completed in Q1 2011. Deal volume has also increased to an average of 664 deals per quarter in 2011 compared to 634 in 2010. As buyout dry powder stands at around $390bn, it is likely that deal flow will continue at, or above, current levels during the second half of 2011.

$39.9bn of North American deals were completed in Q2 2011, accounting for 52% of aggregate deal value, a significant 63% increase from the $24.1bn in deals in the region in Q1. Aggregate deal value in Europe also increased, and reached $30bn, 37% higher than Q1 2011. Buyout activity in Asia and Rest of World fell however; in Q1, a post-crisis high of $10.6bn was invested, but the figure fell to $6.3bn in Q2. This was a result of the lack of mega buyout activity rather than a decline in completed deals; just three deals valued at over $500mn were completed during Q2 2011.

A record 309 PE-backed exits worth $120.1bn were announced in the quarter, a 50% increase on Q1 2011 deal value, and surpassing the previous high of $81.5bn set in Q4 2010. Market conditions are relatively robust in comparison to 2009, and as buyout houses exit investments made during the boom era of 2005-2007, the surge in exit activity is likely to continue in the coming months.

Notable exits during the quarter include the €9.6bn trade sale of Nycomed by Nordic Capital, DLJ Merchant Banking Partners and Avista Capital Partners to Takeda Pharmaceuticals. Nordic Capital acquired Nycomed in a secondary buyout from a consortium of private equity firms which included AlpInvest Partners, Blackstone Group and DLJ Merchant Banking Partners, with some investors keeping a minority stake in Nycomed during this secondary buyout in 2005.

Fig. 22: Number and Aggregate Value of Deals Globally, Q1 2006 - Q2 2011

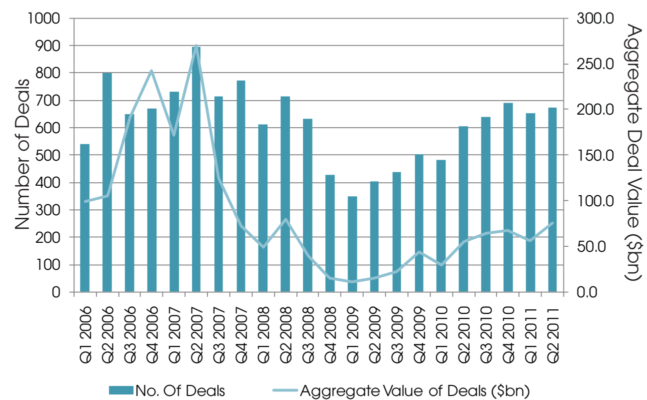



Fig. 23: Aggregate Value of PE-Backed Deals by Region, Q1 2008 - Q2 2011

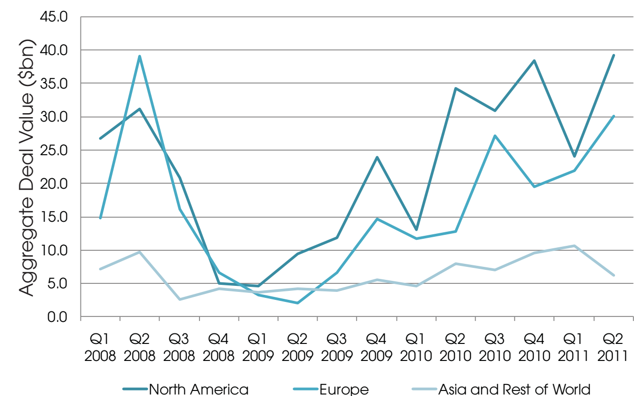
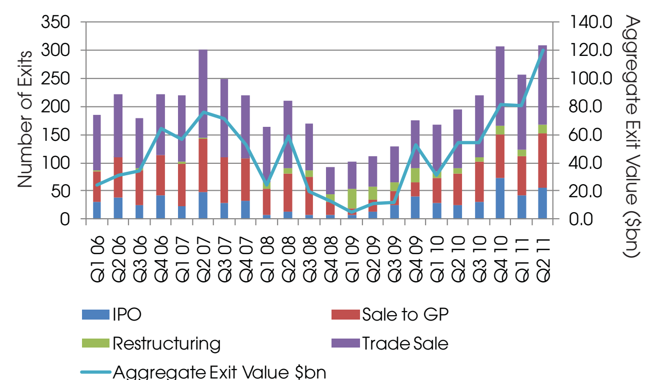



Fig. 24: Number of PE-Backed Exits by Type and Aggregate Exit Value, Q1 2007 - Q2 2011



# Deals by Type, Value and Industry

Leveraged buyouts accounted for approximately 60% of all PE-backed buyout deals in Q2 2011, a similar figure to Q1 2011. A breakdown of buyouts by type is shown in Fig. 25. Growth capital represented 12% and 4% of the number and aggregate value of deals announced for this quarter respectively, a 56% drop in number and 130% fall in value compared to Q1 2011.

As in Q1 2011, the industrial sector accounted for the highest number and value of buyout deals in Q2 2011; the proportion of deals remained at 26%, but the proportion of aggregate value rose from 18% to 25%. The most notable contrast between Q1 and Q2 2011 is in the fall in deal value in the telecoms and media industry, which accounted for 17% of the total value in Q1 2011, but just 3% in Q2 2011.

The resurgence in secondary buyouts which began in 2010 has continued in 2011, with 165 secondary buyouts valued at $35.9bn announced in 2011 to date. 96 of these, valued at $24.4bn,were completed in Q2. These transactions are expected to continue apace and are likely to surpass 2010 levels. Notable secondary buyouts announced in Q2 2011 include the SEK 21bn ($3.3bn) acquisition of Securitas Direct by Hellman & Friedman and Bain Capital from EQT Partners in June 2011, and AXA Private Equity, Clayton Dubilier & Rice and Caisse de depot et placement du Quebec's announced acquisition of Spie for €2.1bn from PAI Partners.

Preqin's Deals Analyst database contains in-depth data for over 22,000 buyout deals across the globe. For more information about this product and how it can assist you, please visit: www.preqin.com/deals

Fig. 25: Proportion of Number and Aggregate Value of Deals by Type, Q2 2011

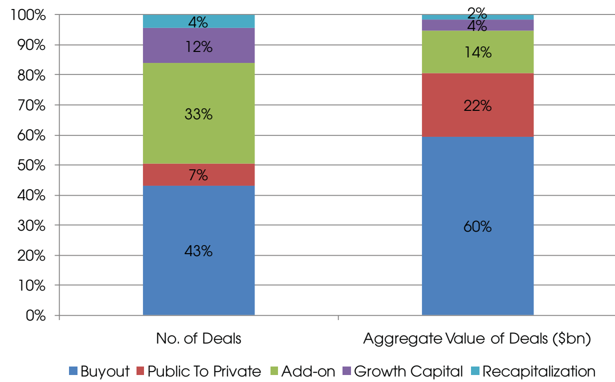



Fig. 26: Proportion of Number and Aggregate Value of Deals by Value Band, Q2 2011

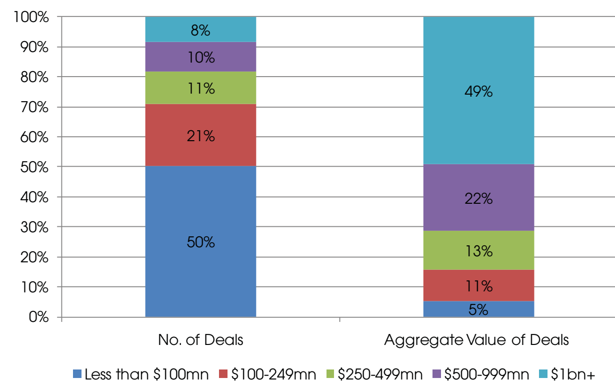
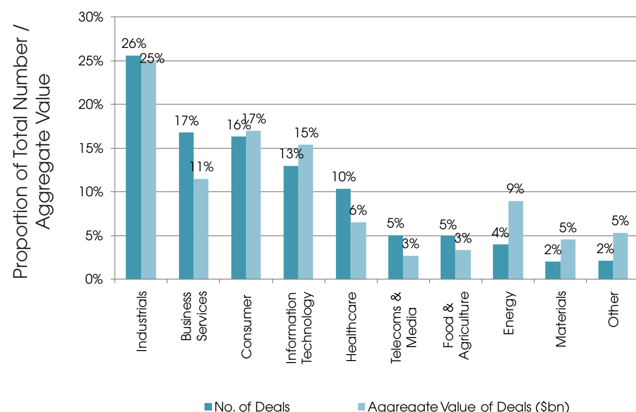



Fig. 27: Breakdown of Number and Value of PE-Backed Deals by Industry, Q2 2011

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# Largest Deals & Notable Exits

Fig. 28: 10 Largest Buyout PE-Backed Deals Globally, Q2 2011

| Name | Date | Type | Deal Size (mn) | Buyers | Sellers | Industry | Location |
|---|---|---|---|---|---|---|---|
| Frac Tech Holdings | Apr-11 | Buyout | 3,500 USD | Chesapeake Energy Corporation, CPP Investment Board, RRJ Management, Temasek Holdings | - | Oil & Gas | US |
| Securitas Direct | Jun-11 | Buyout | 21,000 SEK | Bain Capital, Hellman & Friedman | EQT Partners | Technology | Sweden |
| Spie | May-11 | Buyout | 2,100 EUR | AXA Private Equity, Caisse de depot et placement du Quebec, Clayton Dubilier & Rice | PAI Partners | Industrial | France |
| BJ's Wholesale Club, Inc. | Jun-11 | Public To Private | 2,800 USD | CVC Capital Partners, Leonard Green & Partners | - | Retail | US |
| Capsugel | Apr-11 | Buyout | 2,375 USD | Kohlberg Kravis Roberts | Pfizer | Pharmaceuticals | US |
| Husky Injection Molding Systems | May-11 | Buyout | 2,100 USD | Berkshire Partners, OMERS Private Equity | Onex Corporation | Industrial | Canada |
| Lawson Software | Apr-11 | Add-on | 2,000 USD | Golden Gate Capital, Infor Global Solutions | - | IT | US |
| SRA International Inc. | Apr-11 | Public To Private | 1,998 USD | Providence Equity Partners | - | Business Services | US |
| Gruppo Coin | May-11 | Public To Private | 1,300 EUR | BC Partners | PAI Partners | Retail | Italy |
| RAC | Jun-11 | Buyout | 1,000 GBP | Carlyle Group | Aviva plc | Industrial | UK |

Fig. 29: Five Notable Exits, Q2 2011

| Firm | Investment Date | Investors (Entry) | Deal Size (mn) | Exit Type | Exit Date | Acquiror (Exit) | Exit Value (mn) | Primary Industry | Location |
|---|---|---|---|---|---|---|---|---|---|
| Nycomed | Mar-05 | Nordic Capital | - | Trade Sale | May-11 | Takeda | 9,600 EUR | Pharmaceuticals | Switzerland |
| Glencore International AG* | Dec-09 | BlackRock, First Reserve Corporation, Government of Singapore Investment Corporation (GIC) | 1,000 USD | IPO | May-11 | - | 6,800 GBP | Industrial | Switzerland |
| Skype | Sep-09 | Andreessen Horowitz, CPP Investment Board, Index Ventures, Silver Lake | 1,900 USD | Trade Sale | May-11 | Microsoft | 8,560 USD | Technology | Luxembourg |
| Graham Packaging | Feb-98 | Blackstone Group | 2,308 USD | Trade Sale | Jun-11 | Reynolds Packaging Group | 4,500 USD | Manufacturing | US |
| Diversey, Inc. | Nov-09 | Clayton Dubilier & Rice | 477 USD | Trade Sale | Jun-11 | Sealed Air | 4,300 USD | Consumer Products | US |

* Denotes a partial exit



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# Dry Powder

The entire private equity industry has seen a decline in the amount of dry powder available since the onset of the financial crisis in 2008. In Q2 2011 a mixture of slow fundraising and a slight increase in deal activity saw dry powder levels decrease by 0.2% from Q1 2011.

The amount of dry powder available across the private equity industry is shown in Fig. 30. The latest results show that the level of dry powder has decreased every year since December 2008. The most significant decrease in the level of uncalled capital, between December 2008 and June 2011, has been for buyout funds, which have seen a decrease of 24%. Over the same period the dry powder reserves for real estate and mezzanine funds have decreased by 10% and 5% respectively. The dry powder available to venture funds has only decreased slightly in the period, having fallen in the year to December 2009 and since increased again.

Fig. 31 displays the split of the dry powder available by primary geographic focus. The uncalled capital available to funds with a primary focus on North America decreased by 14.7% between December 2008 and June 2011 by 14.4% for funds with a primary focus on Europe and by 3.4% for funds investing in Asia and Rest of World.

Fig. 32 illustrates the amount of capital invested and dry powder remaining for buyout funds of vintages 2005-2010. The median investment period for buyout funds is five years, which implies that vintage 2007 and 2008 buyout funds will be nearing the end of their investment periods over the next few years. Buyout funds with a vintage of 2007 should be approaching the end of their investment periods in 2012, and these funds currently have $87bn in dry powder to deploy. Vintage 2008 funds have $107bn in their dry powder reserves. Over the next two to three years, fund managers will be keen to use this available capital. This can already be seen in the continued increase in deal activity over the recent quarters.

Preqin's Fund Manager Profiles product shows current and historic dry powder levels across the global private equity industry, including in-depth analysis by region, fund type and fund size.For more information about this product and how it can assist you, please visit: www.preqin.com/fmp

Fig. 30: Dry Powder by Fund Type, 2003 - 2011, as of June 2011

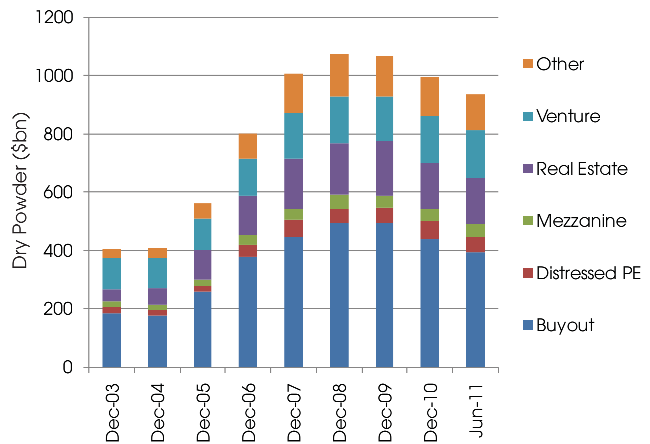



Fig. 31: Dry Powder by Primary Region Focus, 2003 - 2011, as of June 2011

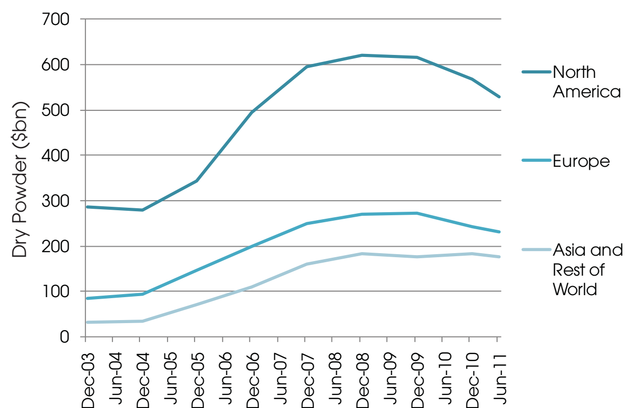
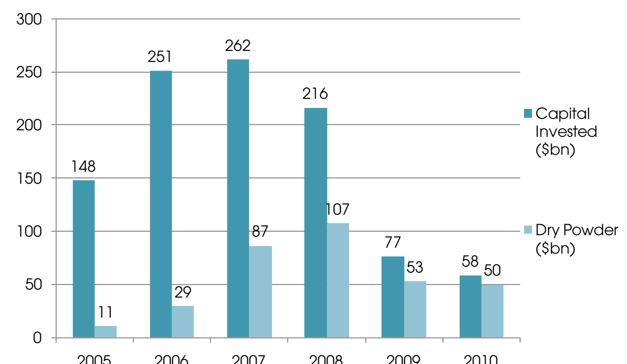



Fig. 32: Buyout Funds - Capital Invested and Dry Powder Remaining by Vintage Year as of 30 June 2011

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# Performance Update

Preqin has analyzed the returns generated by private equity partnerships as of 31 December 2010 by using the data from Performance Analyst to provide an independent and unbiased assessment of the industry's performance. Preqin currently holds transparent net-to-LP performance data for more than 5,600 private equity vehicles of all types and geographic foci. In terms of aggregate value, this represents around 70% of all capital raised by the industry. For more information on Performance Analyst, the private equity industry's leading source of fund performance data, please visit: www.preqin.com/pa

Fig. 33, showing the quarterly change in all private equity net asset value (NAV) for all four quarters in 2010, illustrates that the NAVs have increased every quarter for the period shown in the graph. The largest change in NAV occurs in the last quarter, when the average increase is 5.8% in the non-weighted metric and 7.0% in the weighted metric. The weighted metric takes into consideration the sizes of the funds and suggests that the larger funds have experienced a greater increase in NAV than the smaller funds. This trend can be seen in all quarters in 2010 except for the second quarter. It is important to remember that the larger funds were previously more affected by the financial crisis than smaller funds.

The one-year weighted change in NAV by fund type as at each quarter end from March 2010 to December 2010 is displayed in Fig. 34. All the different private equity strategies show an increase in NAVs, except for real estate funds in the year to March 2010. The average NAV in the year to December 2010 increased for all fund types: buyout fund NAV increased by 15.1%, venture by 9.2%, fund of funds by 7.9% and real estate by 14.8%.

Fig. 35 analyzes the horizon IRR of all private equity over the one-, three- and five-year periods and the returns achieved by three public indices across the same timeframe through 31 December 2010. The overall private equity horizon IRR for the one-year period stands at 18.8%, at 0.8% for the three-year period and at 11.0% for the five-year period. Over the three periods the returns for MSCI Emerging Markets and all private equity are broadly similar, and they both outperform the S&P 500 and MSCI Europe.

Comparing private equity with listed equities should be viewed with caution as private equity is an illiquid asset class, and investors will be committed over a long period of time.

Fig. 33: All Private Equity Change in NAV by Quarter

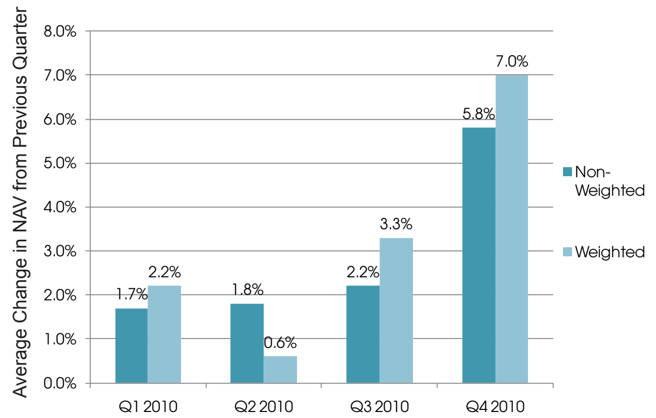



Fig. 34: Weighted Average Change in NAVs by Fund Type

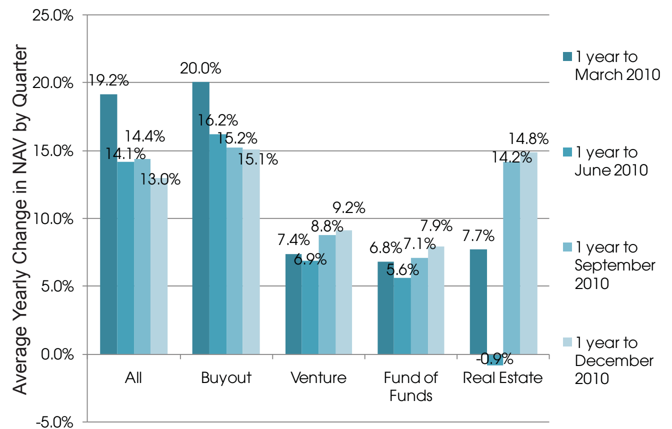
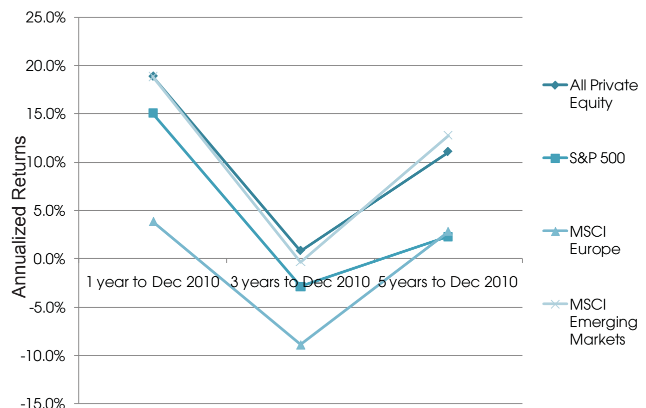



Fig. 35: Private Equity Horizon IRR Vs. Public Indices, As of 31 Dec 2010



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# Fund Terms and Conditions

In the years since the start of the financial crisis, the slow fundraising environment has led to a shift in the balance of power between GPs and LPs when negotiating fund terms and conditions. LPs have been more cautious in committing to funds and have been pushing for concessions on various fund terms prior to investing. In the depressed fundraising environment, it has been imperative for fund managers to position their vehicle in the best possible way, and an important part of this is in the competitiveness of the terms and conditions offered to LPs.

Fig. 36 shows the split of management fees charged during the investment period by buyout funds with a 2010 or 2011 vintage, or those still raising capital as of Q2 2011. Over three-quarters of these funds have a management fee in the 2.00-2.24% range, with most funds in this group actually having a management fee of exactly 2.00%. 12% of recent buyout funds have a management fee of 1.50-1.74%. Larger funds tend to have lower management fees than smaller funds; recent buyout funds under $200mn in size have a mean management fee of 2.03%. Funds in the $500-999mn size range have a mean management fee of 1.88%, and funds of $2.5bn or more in size have a mean fee of 1.58%.

Another area that is important to LPs is the level of a GP's commitment to its own fund. LPs see the GP's commitment as a key driver of the alignment of interests between investors and the fund manager. Fig. 37 shows the mean and median GP commitments (as a percentage of overall fund size) for a range of private equity fund types. Buyout funds have the highest median GP commitment of the fund types shown, at 2.50%, and real estate funds have the highest mean (4.49%). Mezzanine funds have the lowest benchmark figures, with a mean of 2.36% and a median of 1.00%. All other fund types shown have a median GP commitment level of 2.00%.

Fig. 36: Buyout Funds - Management Fee during Investment Period (Funds Raising & Vintage 2010/2011 Funds Closed)

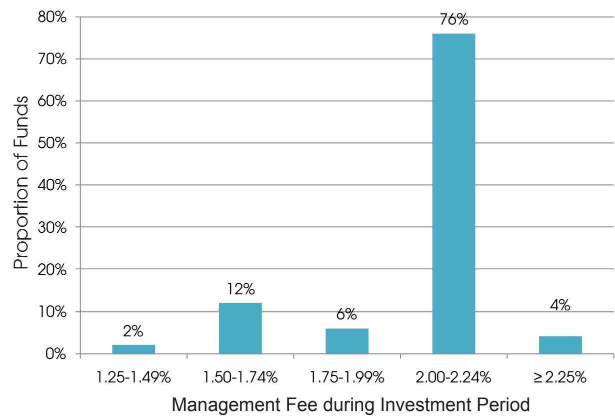
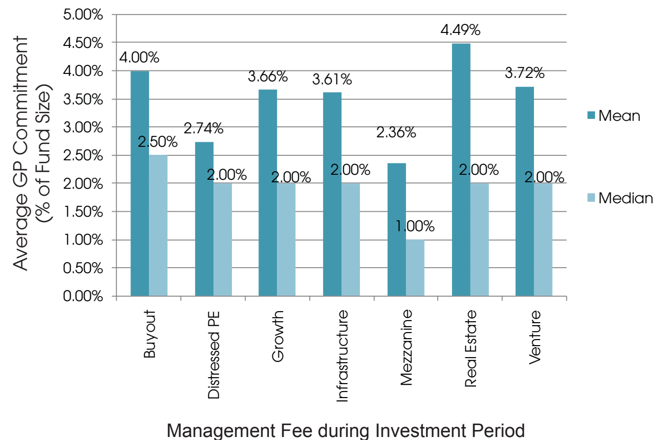



Fig. 37: Average GP Commitments as a Percentage of Fund Size by Fund Type (Funds Raising & Vintage 2010/2011 Funds Closed)



# About Preqin

Preqin private equity provides information products and services to private equity and venture capital firms, fund of funds, investors, placement agents, law firms, investment banks and advisors across the following main areas:

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- Fundraising
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