PREQIN SPECIAL REPORT: PRIVATE CAPITAL COMPENSATION AND EMPLOYMENT

MARCH 2018

In association with

FPL Associates

preqin

FOREWORD

The private capital industry has seen significant growth and development in recent years; with that comes the demand for key talent to undertake specific roles to contribute to the success of this increasingly competitive industry. Assets under management are nearly at the $5tn mark globally, and capital raised has increased year on year since 2010. As the industry has grown, so has the number of firms active in the market. Preqin estimates that there are currently over 7,500 active firms in the industry (as at the end of 2017), each employing staff integral to the firm's activities and success.

Preqin and FPL Associates have partnered together to produce **The 2018 Preqin Private Capital Compensation and Employment Review**, a 218-page publication packed full of data from our latest global compensation survey. In its ninth year, the publication serves an important role in the industry to provide transparency and data in an opaque area of the market.

Over the course of 2017, we conducted an in-depth survey with 173 leading firms across the private capital industry (private equity, private debt, real estate, infrastructure and natural resources) to gain a better understanding of their compensation practices and remuneration levels. The information and data collected is used to compile meaningful statistics covering a wide range of positions at these firms, from junior-level professionals to senior executives. The publication encompasses all of the major private capital strategies, including buyout, growth, venture capital, distressed debt/special situations, mezzanine, real estate, infrastructure and natural resources. The main publication looks at a wide range of employment practices as well as actual figures for salaries by individual position.

In this Special Report, we take a look at key highlights of the survey and provide exclusive insights into the main publication.

PARTICIPATING FIRMS

We are extremely grateful to all the firms that participated in this important study.

If you would like to participate in the next survey and receive a free copy of next year's Review and an exclusive Excel document containing all the compensation data, please contact **info@preqin.com**

KEY FACTS

THE STATE OF THE PRIVATE CAPITAL INDUSTRY

$4.93tn
Private capital assets under management (as at June 2017).

7,500+
Number of firms active in the industry globally.

200,000
Estimated employment of the private capital industry.

$909bn
Amount of capital distributions in 2016, the highest on record*.

$754bn
Aggregate capital raised by private capital funds closed in 2017.

GROWING JOB MARKET AND DEMAND FOR TALENT

65%
of firms expect to increase the size of their workforce in 2017/2018.

61%
of firms added to the staff headcount in 2016.

> ***The need for good investments starts with the deal team***
>
> \- Survey respondent

WOMEN IN THE INDUSTRY

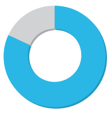
5%
Average proportion of women in Chief Executive Officer positions at participating firms.

3%
Average proportion of women in Managing Director/Partner roles in the investment (deal) team at participating firms.

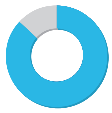
15%
of all senior employees at China-based private equity firms are women, the largest proportion among the top 10 locations**.

SHARE OF PROMOTE/CARRIED INTEREST

32.2%
Average promote/carried interest allocation to CEOs for their most recent fund(s) (as a percentage of GP's share).



82%
Average allocation of GP's share of carried interest split to partners at buyout firms.



87%
Average allocation of GP's share of carried interest allocated to investment (deal) team employees at venture capital firms.

COMPENSATION

37%
A Managing Director/Partner in the investment (deal) team in the US makes 37% more (based on median total remuneration) than the same position in Asia-Pacific.

Chief Executive Officers that work at firms primarily involved in buyout funds earn the highest total remuneration out of all private capital strategies.

*Latest full-year total available.
**By aggregate capital raised by closed-end funds over the last 10 years by firm location.

CURRENT TRENDS IN COMPENSATION PRACTICES

- Austin Morris, **FPL Associates**

Firm-Wide Changes in Base Salaries and Annual Bonuses by Organization Function and Level

	Salary		Annual Bonus	
	Percent of Firms that Increased	Average Increase	Percent of Firms that Increased	Average Increase
Function				
Investments (Deal Team)	73%	11.6%	49%	19.0%
Portfolio Operations (Operating Partners)	34%	6.8%	22%	17.5%
Investor Relations - Capital Raising	33%	7.0%	23%	16.8%
Investor Relations - Reporting/Marketing/Support	41%	6.1%	26%	16.0%
Corporate Operations (i.e., Accounting, HR, IT, Legal)	67%	7.0%	44%	20.3%
Organization Level				
Company Overall	77%	8.6%	52%	17.7%
Executive Management	33%	10.2%	34%	16.6%
Senior-Level Professionals	55%	9.6%	42%	18.3%
Mid-Level Professionals	57%	8.3%	43%	18.4%
Junior-Level Professionals	64%	10.3%	43%	15.8%

Source: The 2018 Preqin Private Capital Compensation and Employment Review

Consistent with the past several years, compensation levels continue to rise year-over-year. In this section, we have highlighted some of those key changes. Additionally, we have summarized and expanded on relevant hot topics related to incentive plan design (compensation structure). While the amount of compensation remains a pressing issue, delivering the 'right' currency is playing an increasing role in compensation discussions. Specifically, firms are focusing in on delivering the most effective currency for attracting, motivating and retaining key talent. In some cases, this requires more line-of-sight between pay and performance by clearly delineating performance metrics, and in other cases, it means creating long-term incentive plans to serve as an alternative (or additive) to carried interest.

BASE SALARIES

For the last several years, the vast majority of participants have increased salaries. This year's survey was no exception, with 77% of firms increasing base salaries by an average of 8.6% (see table). These increases are more commonly going to professionals on the investments team and corporate functions. Functions like portfolio management, investor relations (reporting/marketing/support) and capital raising did not see the same frequency or amount of increase in base salaries (on average 36% of firms increased salaries for these functions and by an average of 6.7%). Investments, junior professionals and executive management saw the most dramatic increase in salaries (all above 10%). Not surprisingly, junior-level investment professionals remain the most in-demand functions.

BONUS TARGETS

Actual bonus awards remain strong. While the average aggregate bonus pool as a percentage of pre-bonus profits was slightly down from last year (34% from 40%); over half (52%) of participating firms reported bonus increases (up from 47%), with the average individual increase holding steady at just under 18%.

Bonus practices continue to evolve to be more balanced (not completely discretionary or overly formulaic). Nearly 60% of participating firms use an annual bonus target. Bonus targets are commonly communicated at the beginning of the year and most often accompanied by specific performance goals/initiatives for the year. Actual awards are driven based upon the achievement of those goals and fall above or below target. Most commonly, awards fall between 50-200% of target (in some cases up to 300%). Goals almost always include some form of company-level performance as well as individual performance and the weighting of these two dimensions (company and individual) is oftentimes driven by level and function within the organization.

Finally, while not a majority practice, 16% of firms force a deferral of annual bonuses. These deferrals generally range between 15-50% of the award size and cover a three-year window. In general, these types of deferrals are more common at institutional firms (versus independent firms). Bonus deferrals serve as a retention strategy, especially for employees who are not yet eligible for a long-term incentive award like carried interest.

NON-CARRY LONG-TERM INCENTIVES

Last year was the first year in which this survey reported out on non-carried interest long-term incentive (LTI) plans. This year's results continue to indicate that many of the participants of this survey use this as a third or fourth currency for their professionals (40% of participating firms offer non-carried interest vehicles). Many types of LTI awards are prevalent, including enterprise awards and cash-based awards.

Firms oftentimes use this currency to achieve one or more initiatives, including: offsetting more modest cash compensation, offsetting modest carried interest allocations, offering a long-term incentive award to employees who would not otherwise be eligible to participate in the carried interest, and/or developing an incentive that ties employees to platform performance versus investment returns.

CARRIED INTEREST PLANS

The amount of carried interest shared with key members of management remains a key aspect of any private equity firm's compensation program. While carried interest eligibility expanded at nearly a quarter of participating firms, it remains fairly restrictive, allocated largely to senior professionals and select mid-level investment professionals. Actual allocations are influenced by several key factors and key among them is ownership. Allocations to management teams that are captive to larger firms range between 30-60% of the amount of carry received by the GP. Actual allocations are dependent on the type of investment, management's track record, how much support is being received by the 'parent', cash compensation practices and eligibility. For independent firms with active partners, allocations to non-partners tend to fall between 15-30%. This perceived 'lower' allocation is typically due to the fact that the active partners within these independent firms have a substantial role as members of the management team, so the traditional approach of analyzing the split between 'house' and 'management' can be misleading.

Given the increasingly unique ownership structures (multiple partners, strategic partners and captive structures), there are many approaches to analyzing how much carry should be allocated to the management team. To that end, firms are evaluating market practices in aggregate, by individual, based on capital contribution (co-investment) and ownership, among others. We are increasingly working with firms to evaluate carry allocations based on peer/competitor landscape, but also the company-specific factors that influence carry allocations.

Many firms continue to use a reserve when allocating carried interest. On average, firms carve out 12% of the carried interest allocated for management into a reserve to be used for future awards such as new hires and promotions. As mentioned last year, we are continuing to see more and more firms tie the final vesting event to liquidation of the fund. As it relates to termination provisions, a best practice provides the company the ability to buy out vested interests for departed employees upon termination. When provided the option, this allows companies to differentiate how carry is treated based upon the employee-specific situation.

CO-INVESTMENT

While not considered compensation, co-investment continues to be a common requirement and/or option at many firms. Many firms tie co-investment requirements to individual promote allocations. Firms can offset the co-investment requirement by the use of a promote-to-co-investment ratio (i.e. for every three points of promote a participant receives, they are required to co-invest 1% of the GP's co-investment requirement, or 3:1) and/or a loan. Ratios and/or loan terms vary based upon other compensation program-specific aspects. For example, firms with generous cash compensation arrangements and generous carried interest allocations may require a more robust co-investment requirement from the team. The key to a balanced co-investment program is that it is aligned with carried interest, ownership and/or cash-compensation, and takes into account the other aspects of the overall compensation program.

FPL ASSOCIATES

FPL Associates, a member of the FPL Advisory Group family of companies, provides a range of specialized compensation and management consulting solutions to the real estate and related financial services industries. FPL actively represents a number of leading private equity firms in which, as part of our compensation services, we assist such firms in the assessment, design, and implementation of compensation programs. We specialize in compensation benchmarking, program design with respect to crafting performance management and reward systems that align management interests with the achievement of strategic business objectives, employment agreement structuring and negotiation, customized compensation surveys, IPO-related compensation assistance, and integrating compensation plans resulting from mergers/acquisitions.

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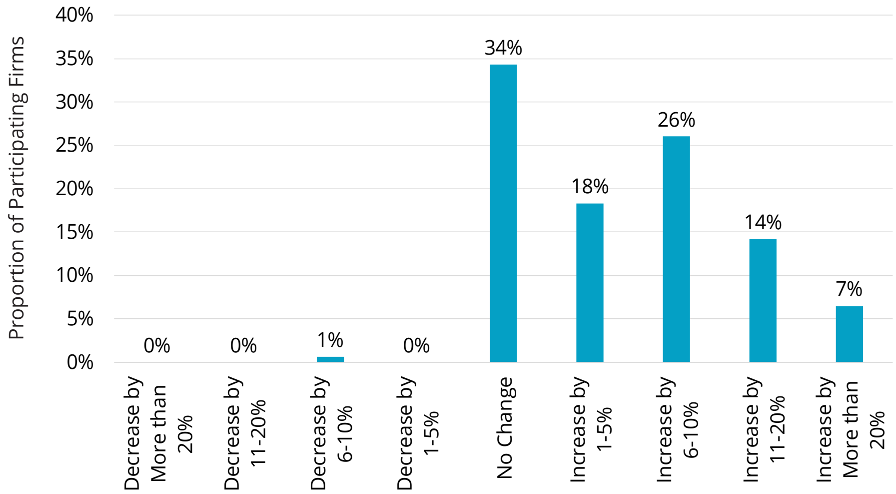
GROWING JOB MARKET AND DEMAND FOR TALENT

EMPLOYMENT LEVELS

Participating firms were asked about changes to their staff headcount over 2016 (Fig. 2). The majority (61%) of firms reported that they added to the staff headcount within their company, while the smallest proportion (8%) made reductions during the year.

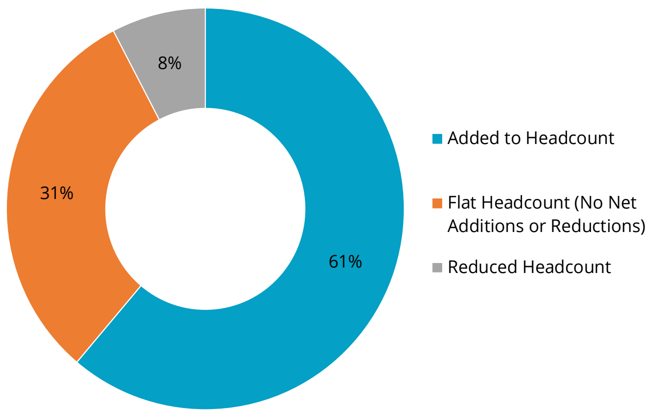
Firms in the study were asked about the level or function that is most in demand from a hiring and retention standpoint, the results of which are shown in Fig. 3. The large majority (72%) of firms stated that the hiring and retention of their investment team (deal team) was the most in demand, with one respondent explaining that "this is the hardest area to gain experience and therefore [to] find experienced individuals".

Fig. 1: Expected Proportional Change in Size of Workforce in 2017/2018 at Participating Firms



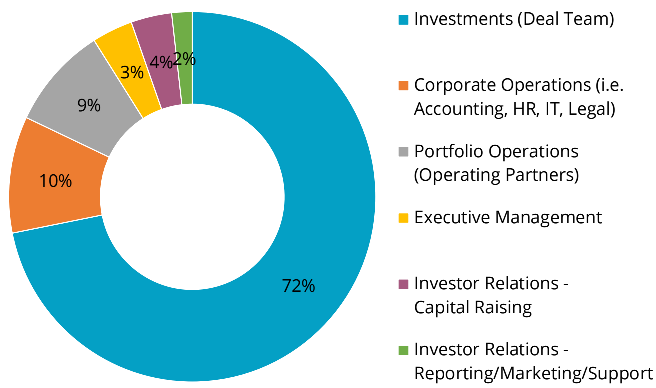
Source: The 2018 Preqin Private Capital Compensation and Employment Review

Fig. 2: Changes to Company Staff Numbers in 2016 by Headcount



Source: The 2018 Preqin Private Capital Compensation and Employment Review

Fig. 3: Level or Function that Is in the Greatest Demand from a Hiring/Retention Standpoint at Participating Firms



Source: The 2018 Preqin Private Capital Compensation and Employment Review

Fig. 4: Sample Reasons Why Each Level/Function Is in Greatest Demand*

Level/Function	Participant Response
Investments (Deal Team)	"The need for good investments starts with the deal team."
	"Critical to the success of the business."
Corporate Operations (i.e. Accounting, HR, IT, Legal)	"Candidates are receiving multiple offers when they are interviewing with the firm."
Portfolio Operations (Operating Partners)	"Lots of competition for qualified candidates."
Executive Management	"Very senior, experienced operations professionals are typically very entrenched in their current position and loyal to their firm."
	"Need highest quality of talent to lead the organization."
Investor Relations - Capital Raising	"Raising capital continues to be the greatest challenge in our sector."

Source: The 2018 Preqin Private Capital Compensation and Employment Review

**Some quotes have been edited for clarity or to protect the respondent's anonymity.*

INDUSTRY COMPENSATION PRACTICES

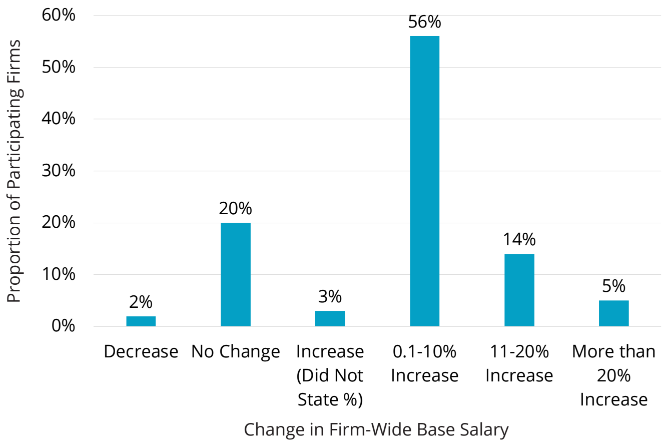
BASE SALARIES AND BONUSES

Fig. 5 shows that the largest proportion (78%) of firms that participated in the most recent compensation and employment survey saw an increase in the firm-wide base salary over the past year. This is indicative of the wider health of the industry, as fundraising continues to gain momentum and more firms enter the marketplace, presenting more employment opportunities for private capital professionals. Notably, 5% of firms saw a rise of more than 20% in the firm-wide base salary.

The rest of the year reveals more good news for staff at such firms: 68% of survey participants projected an increase in the firm-wide base salary for the period 2017-2018 (Fig. 6). While the largest proportion (54%) of firms predicted an increase of 0.1-10%, a small proportion (3%) were looking to increase the firm-wide base salary by more than 20% during the period. This suggests that firms are more inclined to increase the base salary in smaller increments than in huge raises.

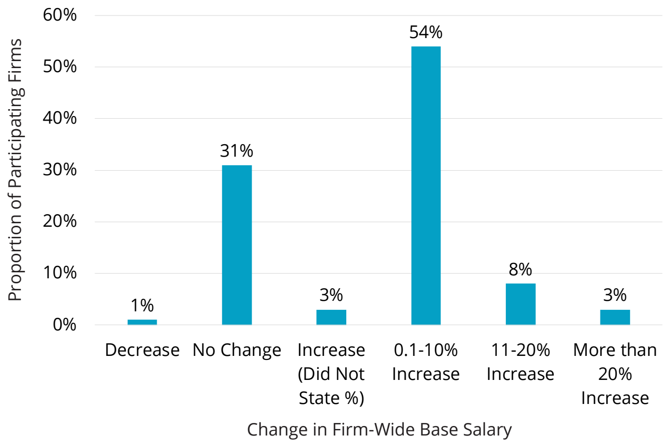
Twenty percent of firms reported that between 2016 and 2017 there was no change in the base salary of their employees firm wide, while only 2% decreased the firm-wide base salary over the same period (Fig. 5). In the projected timeframe defined in Fig. 6, only 1% of firms will look to decrease the firm-wide base salary, while 31% anticipate that it will not change. While many other companies have seen increases in the base salary of their employees or will look to increase it, this is certainly not the case for all survey participants.

Fig. 5: Firm-Wide Changes in Base Salary at Participating Firms between 2016 and 2017



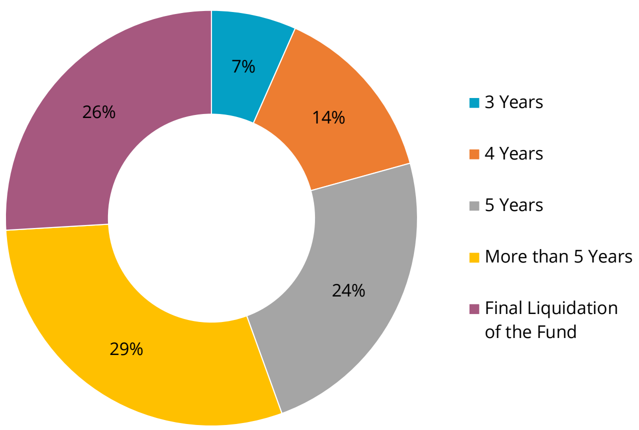
Source: The 2018 Preqin Private Capital Compensation and Employment Review

Fig. 6: Projected Firm-Wide Changes in Base Salary at Participating Firms between 2017 and 2018



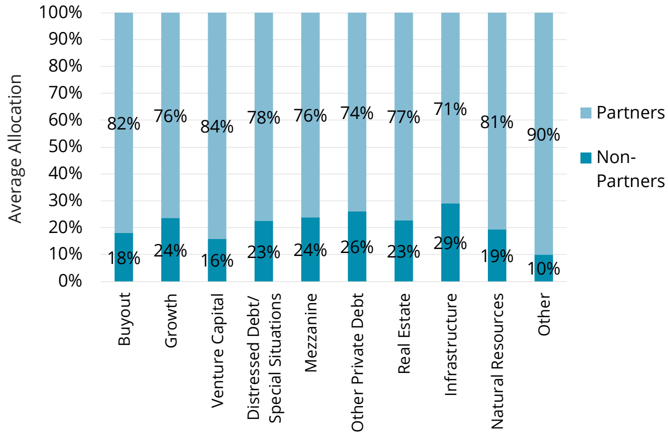
Source: The 2018 Preqin Private Capital Compensation and Employment Review

Fig. 7: Total Number of Years Required to Be Fully Vested



Source: The 2018 Preqin Private Capital Compensation and Employment Review

Fig. 8: Average GP's Share of Carried Interest Split among Partners and Non-Partners for Independent Companies Owned Entirely or Mostly by Members of Management



Source: The 2018 Preqin Private Capital Compensation and Employment Review

PROMOTE/CARRIED INTEREST AWARDS

Promote/carried interest awards are an important feature of compensation at private capital firms.

Fig. 7 shows the total number of years that are required for awards to be fully vested – the largest proportion (29%) of firms in the survey stated that to be fully vested required a time period greater than five years. The second largest proportion (26%) required that the award be fully vested at the final liquidation of the fund. Further analysis reveals that 55% of firms reported that the frequency of vesting used was pro-rata vesting (equal vesting during the period).

Fig. 8 shows how the GP's share of the carried interest is distributed among partners and non-partners at private capital firms for independent companies that are owned entirely or mostly by members of management. Infrastructure firms in this study have the largest average allocation (29%) of carried interest distributed to non-partners of all firm types. Venture capital firms have the highest average allocation to partners, at an average of 84% of the carried interest split.

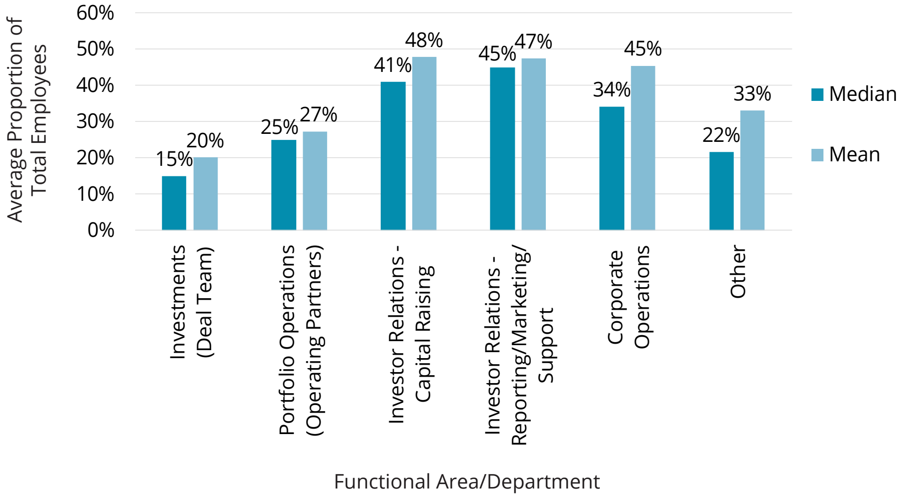
WOMEN AT PRIVATE CAPITAL FIRMS

When looking at the representation of women working within different functions at participating firms, data shows that women make up a notable proportion in the investor relations (reporting/marketing/support) department, accounting for a median of 45% of employees in this function area (Fig. 9). For those firms in which women worked in 'Other' functions across the firm (median proportion of 22%), these were named to be primarily secretarial, administrative or personal assistant roles.

Fig. 10 shows the representation of women working in private capital firms across various regions. Asia-Pacific has the highest median representation (46%) of female employees as a proportion of total staff at firms based in the region.

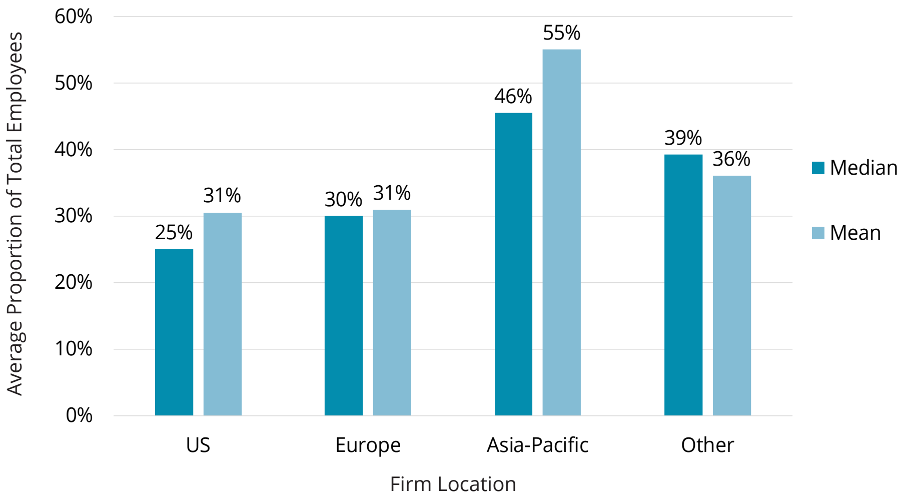
The main publication features information about individual positions at private capital firms, including the average split by gender. For a Managing Director/Partner in the investment (deal) team, the position is far more likely to be held by a man, as men make up an average 97% of this position across participating firms (Fig. 11). In contrast, an administrative assistant is more likely to be a woman, with women making up an average of 97% of this position across participating firms.

Fig. 9: Average Proportion of Total Employees at Participating Firms that Are Female by Functional Area/Department



Source: The 2018 Preqin Private Capital Compensation and Employment Review

Fig. 10: Average Proportion of Total Employees at Participating Firms that Are Female by Firm Location



Source: The 2018 Preqin Private Capital Compensation and Employment Review

Fig. 11: Gender Split between Managing Director/Partner in Investments (Deal Team) and Administrative Assistant in Corporate Operations

Function	Position	Average Male	Average Female
Investments (Deal Team)	Managing Director/Partner	97%	3%
Corporate Operations	Administrative Assistant	3%	97%

Source: The 2018 Preqin Private Capital Compensation and Employment Review

INDIVIDUAL COMPENSATION BY POSITION - EXECUTIVE MANAGEMENT (SAMPLE TABLE)*

**The tables below provide an example of the compensation data included in the full 218-page publication for each of the 83 individual positions analyzed.*

CHIEF EXECUTIVE OFFICER	Typical Years of Experience	Typically Report to	Alternative Title(s)	Typical Education
	20+	Board(s)	Chairman, Managing General Partner	Advanced

Responsible for directing the overall business activities of the company. Establishes short- and long-term company objectives and policies and leads new business development initiatives. Focuses on profitability of the firm and defines organizational framework used to operate the business in order to ensure resources are available to execute the business strategy.

May also be the/a founder of the company.

		Responses	Base Salary				Total Annual Cash Compensation			
		No. of Companies	25th Percentile	Median	Average	75th Percentile	25th Percentile	Median	Average	75th Percentile
	Aggregate									
Assets under Management	Under $150 Million									
	$150 Million - $399.9 Million									
	$400 Million - $1 Billion									
	Over $1 Billion									
Geographic Market	Asia/Pacific									
	Africa/Middle East									
	Europe									
	United States									
	Other									
Type of Fund	Leverage Buyout (LBO)									
	Growth Capital/Equity									
	Venture Capital									
	Distressed & Special Situations									
	Mezzanine									
	Other Private Debt									
	Real Estate									
	Infrastructure									
	Natural Resources									

Job Description Degree of Match	Average	Target Annual Incentive (% of Base Salary) - Calendar/Fiscal Year 2017	25th Percentile	Median	Average	75th Percentile

		Responses	Long-Term Incentive Award + Promote/Carried Interest Award				Total Remuneration			
		No. of Equity Receivers	25th Percentile	Median	Average	75th Percentile	25th Percentile	Median	Average	75th Percentile
	Aggregate									
Assets under Management	Under $150 Million									
	$150 Million - $399.9 Million									
	$400 Million - $1 Billion									
	Over $1 Billion									
Geographic Market	Asia/Pacific									
	Africa/Middle East									
	Europe									
	United States									
	Other									
Type of Fund	Leverage Buyout (LBO)									
	Growth Capital/Equity									
	Venture Capital									
	Distressed & Special Situations									
	Mezzanine									
	Other Private Debt									
	Real Estate									
	Infrastructure									
	Natural Resources									

Number of Direct Reports	Average	Gender	Average Male	Average Female	Number of Funds Currently Participating In	Average	Average Promote Allocation - Most Recent Fund(s)	% of GP's Share

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PREQIN

More than 60,000 alternative assets professionals rely on our global data, tools, insights and intelligence to achieve their objectives:

- **Investors:** asset allocation, manager selection and portfolio management
- **Fund managers:** fundraising, portfolio monitoring and investor relations
- **Service providers and advisors:** business development and in-depth market knowledge
- **The wider alternative assets industry:** insight, understanding and information

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