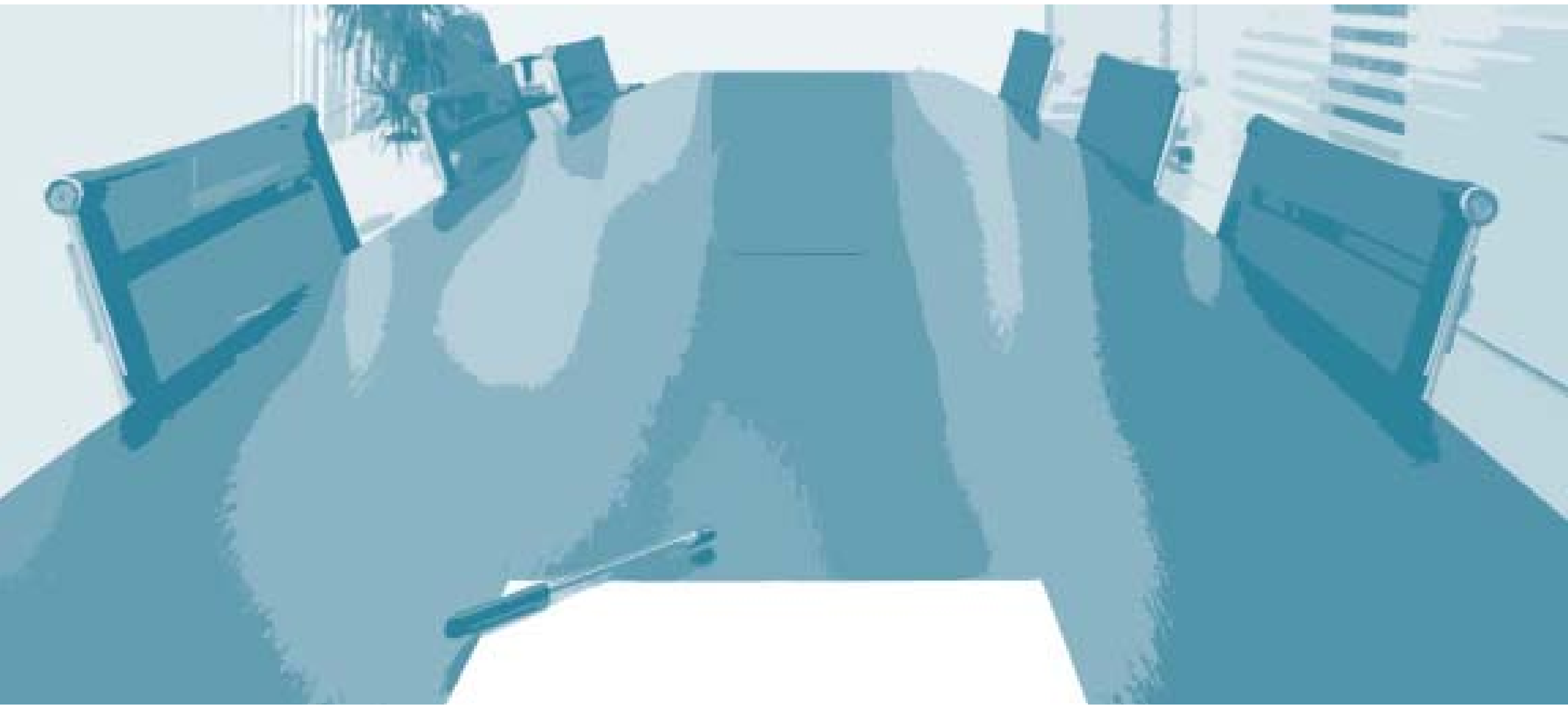
Private Equity Investor Survey

Preqin Research Report

October 2010



alternative assets. intelligent data.

Private Equity Investor Survey

The financial crisis has clearly had a significant impact on private equity fundraising over the past 18 months. Private equity funds that reached a final close during 2009 secured $286 billion in capital commitments, a far cry from the $653 billion secured by the funds that closed the year before. Investor confidence in private equity also suffered as fund valuations fell during 2009 and the lack of deal flow in the industry left many investors over-committed to the asset class with a shortage of capital for new investments.

Despite increasing fund valuations and evidence of improving investor appetite for private equity seen towards the end of 2009, fundraising in early 2010 still fell below levels seen the previous year: in H1 2010, 242 funds closed having raised $116 billion, compared to the 336 funds which closed in H1 2009 having raised $171 billion. Furthermore, our December 2009 LP survey showed that the proportion of investors seeking to reduce their private equity allocations over the coming year had reached a considerable 13%, though perhaps this was a reflection of the fact that many LPs found themselves over-allocated to the asset class at this time. But how are LPs viewing the asset class now?

We surveyed a representative sample of over 100 institutional investors of a wide variety of types, including insurance companies, sovereign wealth funds, public and private sector pension funds and family offices, located across the globe in order to obtain an insight into their current views on the asset class, their appetite for different areas of the private equity market at present and their plans for the future.

Allocations to Private Equity

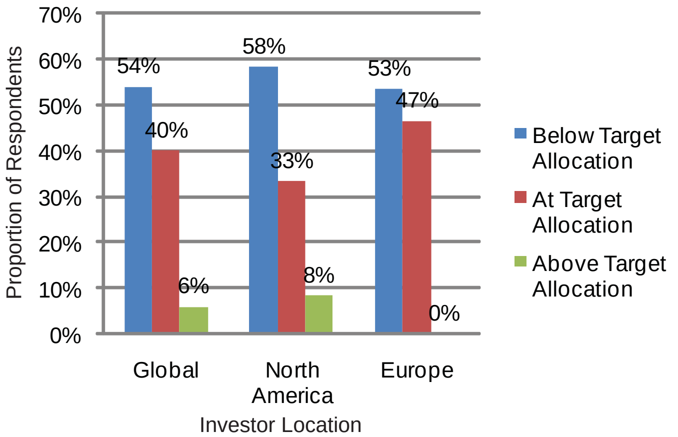
The financial crisis left many investors over-allocated to private equity as a result of falling public equities valuations and delays in revaluing private equity holdings. Many LPs were consequently prevented from making new commitments to private equity funds. 21% of respondents to a survey of institutional investors carried out in December 2008 were exceeding their target allocations to private equity.

We asked respondents to our June 2010 survey whether they were at, below or above their targeted level of exposure to the asset class. As shown in Fig. 1, a considerable 54% of respondents informed us that they were below their target allocations. Just 6% of respondents were exceeding their long-term target allocations to private equity.

Return Expectations

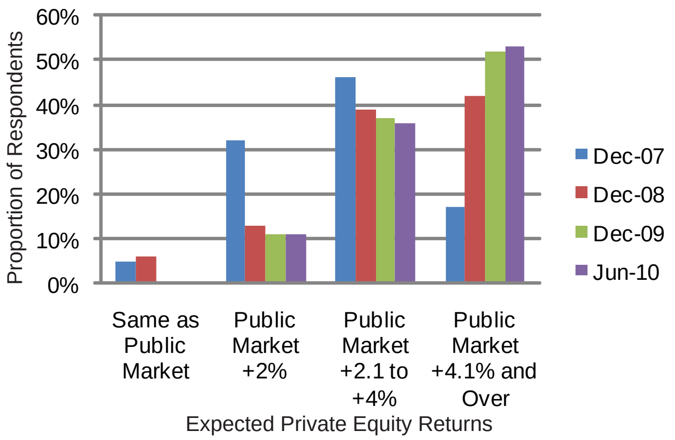
The amount by which investors expect their private equity portfolios to outperform public market investments has on average increased over the past couple of years, as shown in Fig. 2. In December 2007, when LPs were asked how they expected their private equity investments to perform, 17% thought they should provide returns of more than four percentage points over public markets. In December 2008, this had risen to 42% of LPs, and in December 2009, 52% expected returns of in excess of four percentage points over public markets. Little has changed in the past six months: in June 2010, 53% of survey participants expected their portfolios to outperform public markets by more than four percentage points.

Fig. 1: Proportion of Investors Currently At, Above or Below Their Target Allocations to Private Equity



Source: Preqin

Fig. 2: Investors' Return Expectations for Their Private Equity Portfolios

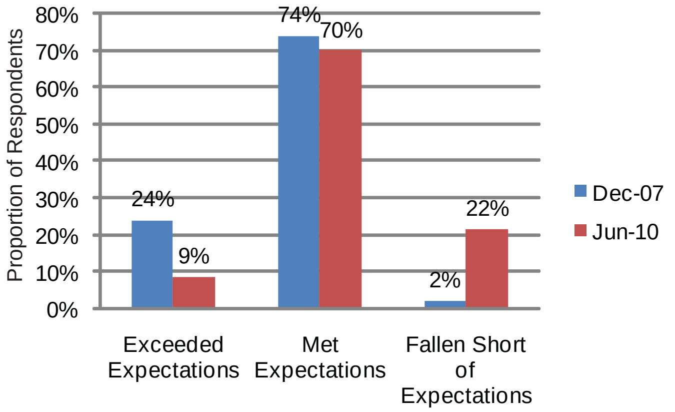


Source: Preqin

Private Equity Investor Survey

The private equity industry entered a more challenging period with the onset of the financial crisis, with fund valuations falling and a difficult exit environment leading to a drop in distributions from funds. Although some recovery has been seen in the performance of private equity funds, investors' views of the asset class were affected. Whereas in December 2007 just 2% of LPs were dissatisfied with the returns they received from their private equity investments, in June 2010, 21% felt that their private equity investments had fallen short of their expectations, though as we have seen, their return expectations have increased in comparison to public markets during this period. The majority of LPs, however, feel that the returns they are receiving from their private equity investments have met their expectations. A well-known Asian investor told us, "Overall, our private equity investments have met our expectations; since the financial crisis, our funds have under-performed but before the crisis they out-performed so overall it has been alright."

Fig. 3: Have Investors' Private Equity Fund Investments Lived up to Expectations?



Source: Preqin

Secondary Market and Direct Investments

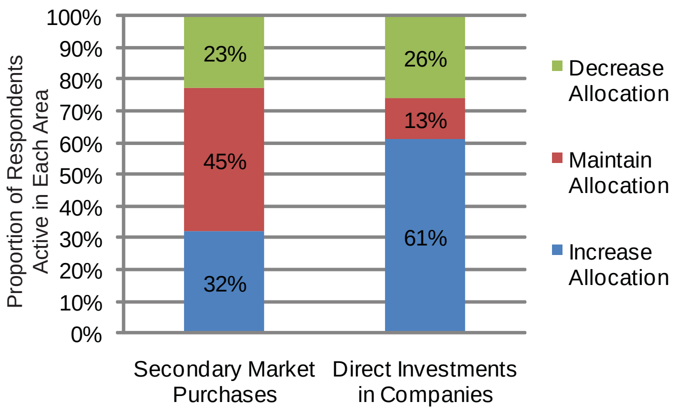
Some of the more experienced private equity investors, and/or those with greater resources at their disposal, have started to divert an increasing proportion of capital that previously would have been used for fund commitments to direct investments in private companies instead. Our recent survey found that 38% of investors set aside a proportion of their private equity portfolios for direct investments, either on a proprietary basis or as co-investments alongside GPs in their portfolios in select transactions.

Of these LPs, 61%, or 23% of those polled overall, invest directly in private companies on a proprietary basis. For some of these investors, such investments have always formed part of their strategies; however, for others, direct investments are becoming a core part of their overall private equity investment strategies. Alberta Investment Management Corporation (AIMCo), for example, has decided to make more direct and co-investments going forwards but will still seek to make fund investments in sectors and regions in which it does not make direct investments, such as vehicles targeting distressed opportunities or Asia.

Of the LPs that invest directly, 76% (or 29% of all LPs polled in the survey) seek to make co-investments alongside GPs. Saplings Alternative Advisors, a hybrid fund of funds manager, engages in co-investments to enhance returns, produce earlier liquidity and to mitigate the double layer of fees faced by its clients.

Such investments are on the rise: a considerable 61% of survey participants that have an allocation to direct private equity

Fig. 4: Investors' Expectations of the Level of Both Secondary Market and Direct Investment Activity in 2011 Compared to 2010



Source: Preqin

investments intend to increase the level of their activity in direct investments during 2011 compared to 2010, as shown in Fig. 4. (This chart shows only the intentions of investors that are active in the secondary market and/or invest directly in companies.) Just over a quarter (26%) of investors that make direct investments in companies, however, are looking to decrease their activity in this area in 2011 in comparison to 2010.

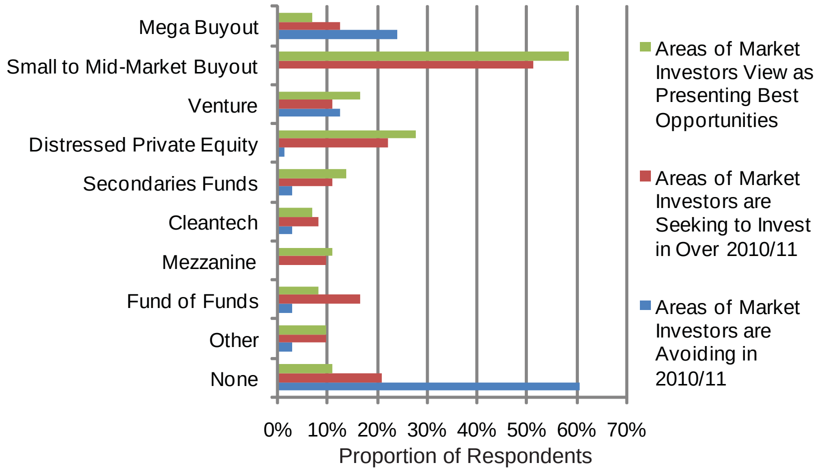
The private equity secondary market is also continuing to attract a significant degree of attention from investors that are seeking to purchase stakes in funds. As Fig. 4 shows, almost a third of institutional investors (32%) that are active as purchasers of fund interests on the secondary market are intending to increase their activity in this area in 2011 in comparison to 2010, and a further 45% intend to maintain the level of their activity.

Private Equity Investor Survey

Investor Appetite for Different Fund Types and Geographies

The financial downturn led many investors to reassess their private equity portfolios, reviewing not only what proportion of their overall investment portfolio they would set aside for investments in the asset class, but also reassessing the private equity market and the fund types that best take advantage of the opportunities currently available. LPs were asked which types of funds they felt were most attractive at present and which areas they would invest in or not over the next 18 months. Respondents to the survey were not prompted with any fund types and were able to provide multiple responses to each question, and therefore their responses, displayed in Fig. 5, illustrate those fund types that investors are particularly interested in or are avoiding at present.

Fig. 5: Investor Attitudes to Different Fund Types at Present



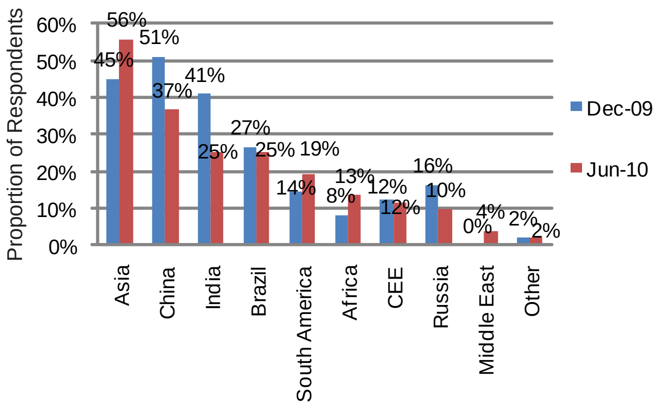
Source: Preqin

Small to mid-market buyout funds were cited by 58% of respondents as a fund type presenting good investment opportunities in the current climate. Just over half of respondents (51%) informed us they were intending to invest in these funds during 2010 and 2011. Distressed private equity funds were viewed by 28% of respondents as being particularly attractive at present and 22% intend to invest in these vehicles. Investor appetite for mega buyout funds also shows signs of gradual improvement. 9% of respondents to our December 2009 survey were intending to invest in mega buyout funds during 2010/11 compared to 13% six months later.

Over the past year, emerging markets have continued to attract the interest of a significant proportion of the LP universe. Two-thirds (67%) of respondents to our December 2009 survey were either currently, or would consider, investing in emerging markets. In June 2010, this had risen to 72%.

Survey participants were asked which regions or countries within emerging markets are presenting the most attractive opportunities. Again, investors were not asked about their attitudes to individual regions and countries and were instead invited to name the locations they felt offered the best opportunities without prompting. As Fig. 6 shows, a considerable 56% of respondents named Asia as an especially attractive region, the most frequently cited location. China, India and Brazil are also seen by significant proportions of investors as particularly attractive at the present time, with 37%, 25% and 25% of respondents naming each location respectively. However, it is interesting to note that 51% of respondents to

Fig. 6: Regions and Countries within Emerging Markets That Are Viewed as Presenting the Best Opportunities in the Current Financial Climate



Source: Preqin

the December 2009 LP survey viewed China as particularly attractive and 41% named India. The proportion of LPs naming Africa as an attractive area for private equity investment rose from 8% in December 2009 to 13% in June 2010. Another location attracting a growing amount of LP interest is South America, with the proportion of LPs naming this region rising five percentage points from 14% to 19%.

GP Relationships

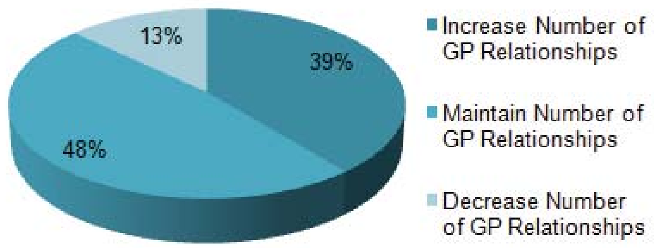
LPs have increasingly scrutinized the relationships they maintain with GPs over the past year. Many have seen the more challenging fundraising environment being faced by fund

Private Equity Investor Survey

managers as the ideal opportunity to push for concessions from the managers they maintain relationships with, perhaps seeking to negotiate discounts on fees. Many have also taken the opportunity to assess the GP relationships they maintain.

Survey participants were asked whether they were likely to increase, maintain or reduce the number of relationships they maintain with GPs over the next couple of years. Excluding survey participants that did not anticipate making any new commitments to private equity funds over the next two years, a considerable 87% intend to increase or maintain the number of relationships with GPs they have, leaving just 13% that intend to decrease the number of GPs they invest with in the future. In fact, as Fig. 7 shows, 39% of investors responding to the survey plan to add additional managers to their roster in the next couple of years.

Fig. 7: Likely Changes to Number of GP Relationships Maintained by Investors in Next Two Years

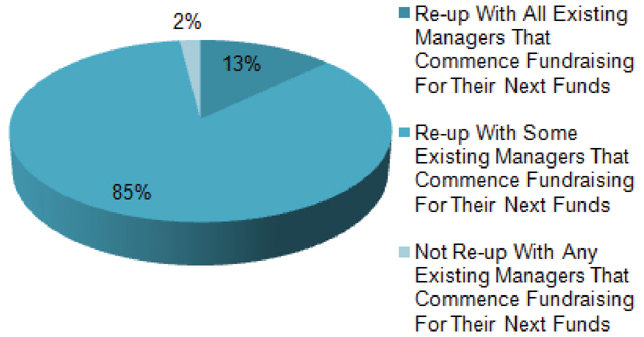


Source: Preqin

In order to examine investors' plans relating to the number of manager relationships they maintain, we asked LPs how they expected to respond to existing fund managers in their portfolios that approached them with new vehicles in 2010/11. As shown in Fig. 8 (which excludes those LPs that are not planning to make new private equity investments in this time frame), the majority (85%) intend to invest further capital with some of the existing managers in their portfolios, but anticipate declining some reinvestment requests. 13% of respondents expect to make commitments to new vehicles being raised by all GPs they have prior relationships with that commence fundraising for new vehicles in 2010 and 2011. Just 2% do not intend to re-up with any of the current managers in their portfolios, though they do anticipate making new commitments to private equity funds during this period.

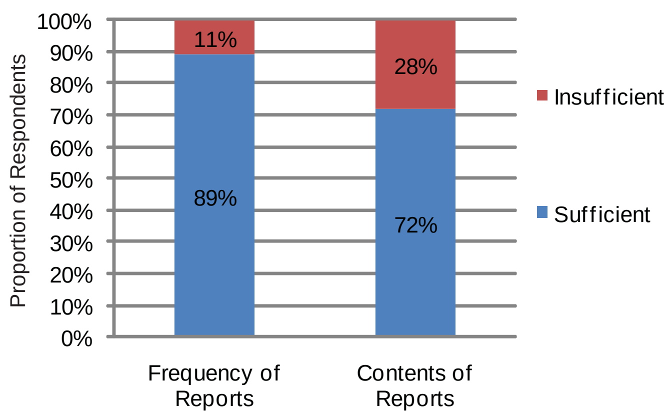
When questioned further about their responses to this question, 14% of respondents informed us that this plan differed from that employed in previous years. One of these respondents, a sovereign wealth fund, told us, "It was difficult to gauge the performance of fund managers before the crisis, but since the difficult times it has become clearer to judge their performance and what they are like." Consequently, the sovereign wealth fund has become more selective. Another respondent, a US endowment, told us it would only re-up with some existing managers because it "now has more GP relationships than in prior years" and is consequently going through the process of selecting which relationships to maintain and which to discontinue. A Middle Eastern investment company said it "will consider re-upping with some managers on a case-by-case basis; some move away from their strategy for new funds, but they should stick to their niche."

Fig. 8: Investors' Plans for Re-up Investments in 2010/11



Source: Preqin

Fig. 9: Proportion of LPs Satisfied with Level of Communications and Reporting from Existing Funds in Their Portfolio



Source: Preqin

Private Equity Investor Survey

We asked LPs how satisfied they were with the level of communications and reporting received from existing funds in their portfolios. As shown in Fig. 9, 89% of LPs are satisfied with the frequency of the reports they received, though some felt reports could be provided more frequently: a US family office told us that "reporting is getting better and the level of information is improving, but it is still only on a quarterly basis," and that it would like more frequent updates from its GPs.

A greater proportion of LPs expressed dissatisfaction with the content of the reports they receive. 28% of respondents to the survey felt that the content was insufficient and this proportion rose to 37% when the responses of European LPs were analyzed separately. Many LPs expressed frustration with the lack of transparency of information provided by some GPs and said that the quality varied significantly from manager to manager. An Austrian LP that was particularly dissatisfied with the reports it receives from its GPs said, "They could tell the truth more!"

Although the majority of LPs were relatively satisfied with the reports they receive from GPs, many still think improvements could be made and that there are large variations between those providing the best reports and those providing the worst. A large Middle Eastern LP told us, "Reporting has improved but is still not satisfactory. The frequency of reporting is ok, once a quarter, and they provide information when it is requested, but the content could still be improved." With many LPs considering discontinuing relationships with managers, GPs must be aware of LPs' expectations for more transparent information to be provided on their investments. Supplying the right level of information to, and improving communications with, LPs can help managers to forge a stronger relationship with their LPs.

In addition to choosing to maintain or discontinue relationships with existing managers in their portfolios, many investors are seeking to forge new relationships with managers in the coming year. Excluding survey respondents that do not intend to make any new commitments to funds in the next 12 months, a considerable 77% plan to establish some new relationships with GPs compared to just 23% that are intending to only invest with managers they have prior relationships with.

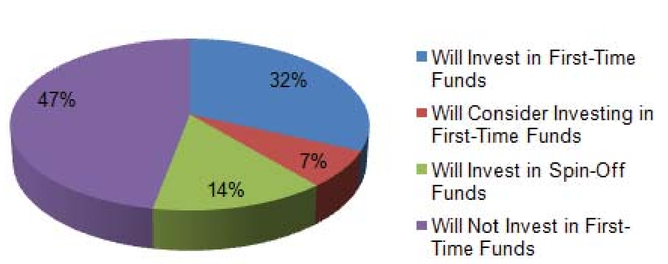
For emerging managers seeking to raise their first funds, the results of the survey are also relatively positive. As shown in Fig. 10, of those investors seeking to make new commitments to funds in the next 12 months, 39% will consider investing in first-time funds. A further 14% will invest in spin-off funds, but not a first-time fund being managed by a first-time team. However, this does mean that almost half (47%) of respondents would not consider investing in first-time or spin-off funds in the coming 12 months.

Investor Appetite in 2010/11

Despite the slow start to fundraising in 2010, the results of our survey show continuing improvement in investor attitudes towards private equity, with 54% of respondents already having made at least one commitment during the first half of the year.

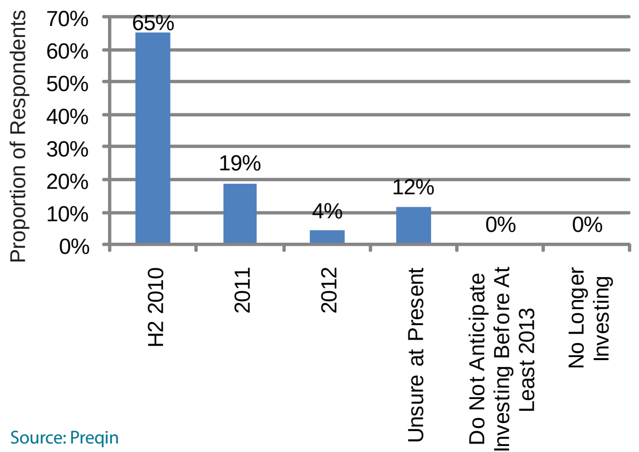
Almost two-thirds (65%) of respondents told us they intend to make their next commitment to a private equity fund during the second half of 2010, as shown in Fig. 11. A further 19% anticipate doing so in 2011. In December 2009, a quarter of investors were uncertain when they would next be active in the asset class, but just 12% of respondents in June 2010 had yet to decide on the timing of their next commitment.

Fig. 10: Proportion of Investors That Will Consider Investing in First-Time Funds in the Next 12 Months



Source: Preqin

Fig. 11: Time Frame for Next Intended Commitment to a Private Equity Fund



Source: Preqin

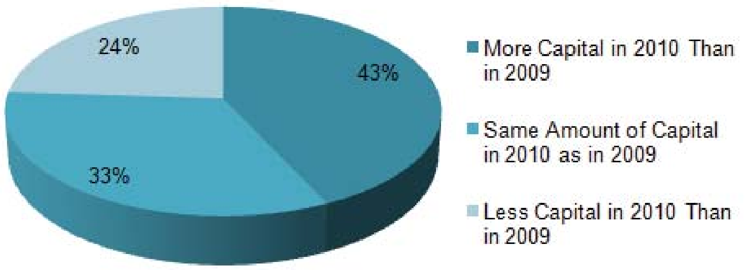
Private Equity Investor Survey

For many investors, the amount of capital they will set aside for new commitments in 2010 will be greater than the amount they pledged to vehicles in 2009. As shown in Fig. 12, 43% of investors intend to use more capital for new commitments in 2010 than they did in 2009 and a further third intend to commit the same amount. An investment company in the Middle East declared that it will "definitely invest more in 2010; 2009 was a 'wait and watch' year." Other LPs cited the increased number of funds in the market and the improvement in the quality of opportunities available in 2010 in comparison to the previous year as reasons for their increased activity in 2010.

It is worth noting, however, that in June 2010, almost a quarter (24%) of respondents anticipated committing less capital in 2010 than in 2009, compared to just 8% that anticipated such a decrease in December 2009, showing that LPs have perhaps been less active in the asset class this year than they had initially planned.

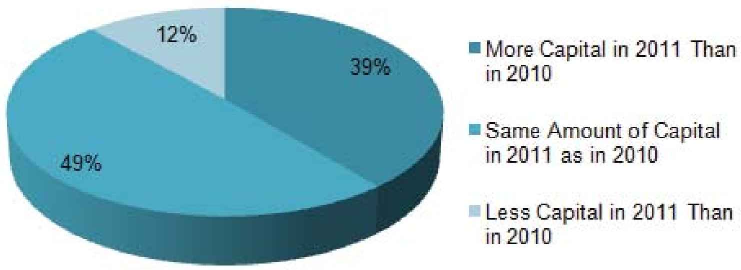
The vast majority (88%) of LPs plan to either increase the amount of capital set aside for new commitments in 2011 compared to 2010 or invest capital at the same rate, as illustrated in Fig. 13. During 2011, just under half (49%) of investors expect to commit the same level of capital as in 2010 and a significant 39% of respondents intend to increase the amount of capital set aside for new commitments. The remaining a 12% intend to reduce the amount of capital they commit that year. One of these LPs, a Belgian investment company, told us it is investing less in 2011 because it needs "to see recycling coming in too." However, others, like one Saudi Arabia-based LP, felt unable to predict the level of their activity in 2011 "because the market is changing too rapidly."

Fig. 12: Amount of Capital Investors Plan to Commit to Private Equity Funds in 2010 Compared to 2009



Source: Preqin

Fig. 13: Amount of Capital Investors Plan to Commit to Private Equity Funds in 2011 Compared to 2010



Source: Preqin

Longer-Term Outlook for Private Equity Fundraising

The results of our survey indicate that there is likely to be a gradual increase in the amount of capital available for fresh private equity commitments during the next 18 months. This is encouraging news for GPs set to enter the market with their latest fund offerings. Despite the increase in the amount of capital investors are setting aside for new commitments, however, it will still fall far short of the amounts seen prior to the financial downturn. Fundraising is consequently set to remain challenging over 2010 and into 2011, although some improvement in the overall amount of capital secured by funds is likely to occur.

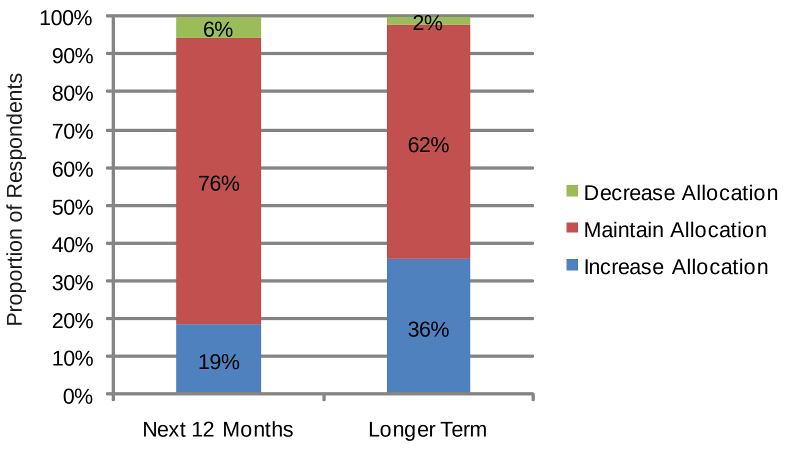
Fund managers can also be encouraged by the longer-term plans of LPs, as illustrated by Fig. 14. Few intend to cut back their allocations and in fact many foresee the size of their allocations rising over the next few years. In our December 2009 survey, 11% of respondents told us they anticipated reducing their allocations to private equity over the next three to five years. In June 2010, however, just 2% of respondents expected to reduce their allocations over the following three to

Private Equity Investor Survey

five years and a considerable 36% intended to increase their allocations. Investors' plans in the short term have also improved: 6% of respondents intended to reduce their exposure to private equity over the following 12 months compared to 13% in December 2009.

What this means for fundraising is that, since the vast majority of LPs intend to increase or maintain their allocations to private equity over the longer term, any capital freed up as distributions from private equity funds pick up will be re-injected into the asset class in new commitments to funds. Although confidence in private equity took a hit as a result of the financial downturn, more than three-quarters of investors are still relatively satisfied with how their private equity investments have weathered the crisis. Investors are seeing good opportunities in the current market and many are planning to set aside additional capital in 2011 to take advantage of this.

Fig. 14: Investors' Intentions for Their Private Equity Allocations



Source: Preqin

Data Source:

The 2010 Preqin Limited Partner Universe

With information on more than 2,700 investors worldwide, plus over 100 pages of vital analysis, the 2010 Preqin Limited Partner Universe is the most comprehensive printed guide to institutional investors in private equity ever produced.

www.preqin.com/lpu

2010 Preqin
Limited Partner Universe:
Order Form

With information on more than 2,700 investors worldwide, plus over 100 pages of vital analysis, the 2010 Preqin Limited Partner Universe is the most comprehensive printed guide to institutional investors in private equity ever produced.

Key features of this publication include:

- Profiles for over 2,700 institutional investors in private equity.
- Includes institutions from over 72 countries worldwide.
- All investor types are profiled, including public and private sector pension plans, fund of funds, insurance companies, asset managers, family offices, endowments, sovereign wealth funds and more…
- Includes direct contact information for key personnel; key financial information; sample investments; fund preferences by type size, geography and experience; future plans.
- Over 100 pages of vital analysis including detailed look at the overall universe, make up of investors in closed funds, individual analysis sections for all major countries and regions worldwide, league tables showing biggest investors, key investors to watch.

www.preqin.com/lpu

2010 Preqin Limited Partner Universe Order Form - Please complete and return via fax, email or post

I would like to purchase the 2010 Preqin Limited Partner Universe

☐ £795 + £10 Shipping ☐ $1,345 + $40 Shipping ☐ €955 + €25 Shipping

Additional Copies

☐ £110 + £5 Shipping ☐ $180 + $20 Shipping ☐ €115 + €12 Shipping

(Shipping costs will not exceed a maximum of £15 / $60 / €37 per order when all shipped to same address. If shipped to multiple addresses then full postage rates apply for additional copies)

I would like to purchase the 2010 Preqin Limited Partner Universe Graphs & Charts Data Pack in MS Excel Format:

☐ $300 / £175 / €185 *(contains all underlying data for charts and graphs contained in the publication. Only available alongside purchase of the publication).*

Name:

Firm: Job Title:

Address:

City: Post / Zip Code: Country:

Telephone: Email:

Payment Options:

☐ Cheque enclosed (please make cheque payable to 'Preqin')

☐ Credit Card ☐ Visa ☐ Mastercard ☐ Amex

☐ Please invoice me

Card Number:

Expiration Date: Security Code*:

Name on Card:

*Security Code:

Visa / Mastercard: the last 3 digits printed on the back of the card.

American Express: the 4 digit code is printed on the front of the card.

Preqin - Scotia House, 33 Finsbury Square, London, EC2A 1BB
Preqin - 230 Park Avenue, 10th floor, New York, NY 10169
w: www.preqin.com / e: info@preqin.com / t: +44 (0)20 7065 5100 / f: +44 (0)87 0330 5892 or +1 440 445 9595