Private Equity Quarterly Index – PrEQIn

March 2012

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The Need for a Private Equity Index

Returns from private equity funds are typically measured using IRRs and multiples. These are appropriate measures of the returns from these types of long-term investments and enable direct comparisons of private equity funds to other private equity funds.

However, a different metric is needed by investors seeking to compare their private equity portfolios with their overall investment portfolios, as well as directly with their investments in other asset classes. These asset allocation tasks call for metrics that facilitate comparison between private equity returns and those of other asset classes.

In order to meet this need from investors, Preqin has created the first index for the whole of the private equity industry, PrEQIn – Private Equity Quarterly Index.

The PrEQIn Index is a money-weighted index that uses fund-level cash flow transactions and net asset values for over 3,900 private equity funds collectively worth more than $2.7 trillion. Preqin's **Performance Analyst** database also holds transparent net-to-LP performance data for over 5,800 private equity funds of all types and geographic focus. In terms of aggregate value, this represents around 70% of all capital ever raised by the industry.

For more information on **PrEQIn**, and to register to receive access to both the Index and to our free **Private Equity Performance Benchmarks** service, please visit our website at www.preqin.com/index.

Contents:

All the data in this report is available for free download on Excel.
Just click on the symbol and your download will begin automatically. You are welcome to use the data in any presentations you are preparing; please cite Preqin as the source.

Objectives and Methodology

Objectives

Investors face many challenges when constructing and maintaining an effective private equity program and a number of different metrics are needed to enable them to effectively monitor and assess their portfolios.

- **Asset Allocation:** an index is required to enable investors to directly compare private equity portfolio returns to returns from other asset classes. This allows investors to determine the optimum level of exposure to private equity in their portfolios to meet their overall investment objectives and should be revisited on a regular basis to ensure the portfolio continues to meet these needs.
- **Fund Selection:** benchmarks are required to allow investors to review how successful they have been at selecting the right funds by comparing the performance of the funds they have invested in to the median IRRs and multiples of funds of the same strategy, geographic focus and vintage year.

It is our aim at Preqin to provide tools to assist investors with both of these challenges. Our complimentary **Private Equity Performance Benchmarks** service has long provided private equity professionals with access to benchmarks, drawing on data available through our **Performance Analyst** database, which holds transparent net-to-LP performance information for over 5,800 funds.

March 2012 marks the launch of our **PrEQIn Private Equity Quarterly Index**, also available through our Private Equity Performance Benchmarks service. This, the first index covering the whole private equity industry, will allow investors to compare the returns from their private equity portfolios to those from other asset classes. In addition to an overall private equity index, we have also provided indices of particular segments of the private equity market, including buyout, venture capital and distressed private equity, allowing investors to analyze and compare different parts of their private equity portfolios.

Methodology

The PrEQIn Index is a money-weighted index that uses fund-level cash flow transactions and net asset values for over 3,900 private equity funds collectively worth more than $2.7 trillion.

The index is based on the following calculation:

Percentage change in quarter = [(NAV at end of quarter + distributions during quarter)/(NAV at start of quarter + call-ups during quarter)] – 1

“Call-ups during quarter” refers to total capital drawn by fund managers in dollars during the quarter, meaning the cumulative cash called to date as at the end of the quarter minus the cumulative cash called to date as at the start of the quarter.

“Distributions during quarter” refers to the total cash distributed to LP in dollars during the quarter, meaning the cumulative cash distributed to date as at the end of the quarter minus the cumulative cash distributed to date as at the start of the quarter.

These returns are then combined to form an index with the starting value of 100 as of 31st December 2000.

The PrEQIn Private Equity Quarterly Index is available to private equity professionals for free as part of Preqin’s **Private Equity Performance Benchmarks** service. For more information, or to gain complimentary access to this service, please visit www.preqin.com/index.

The PrEQIn Private Equity Quarterly Index draws on information taken from **Performance Analyst**, the industry’s most extensive and transparent source of net-to-LP private equity fund performance, with full metrics for over 5,800 named vehicles. In terms of aggregate value, this represents around 70% of all capital ever raised by the industry. For more information on Performance Analyst, please visit www.preqin.com/pa.

It is important to note that the current September 2011 data is preliminary and subject to change, as we constantly gather and update the returns information on private equity vehicles. Furthermore, it should also be noted that we are in the final stages of gathering returns information for June 2011 and we expect our final run of June data will happen over the next couple of months. As such, we anticipate the index returns may change somewhat for this dataset. Our September 2011 figures are still in the preliminary stages of the data collection process and so will be subject to more significant change.

PrEQIn Index: All Strategies

Fig. 1 shows the PrEQIn Private Equity Quarterly Index calculated for the private equity industry as a whole, as well as for the main strategies within the private equity asset class. This includes buyout, venture, real estate, fund of funds and distressed private equity. Each of these strategies has a different risk-return profile and it is important for investors to consider risk-adjusted performance in order to tailor their exposure to the private equity asset class to meet their requirements.

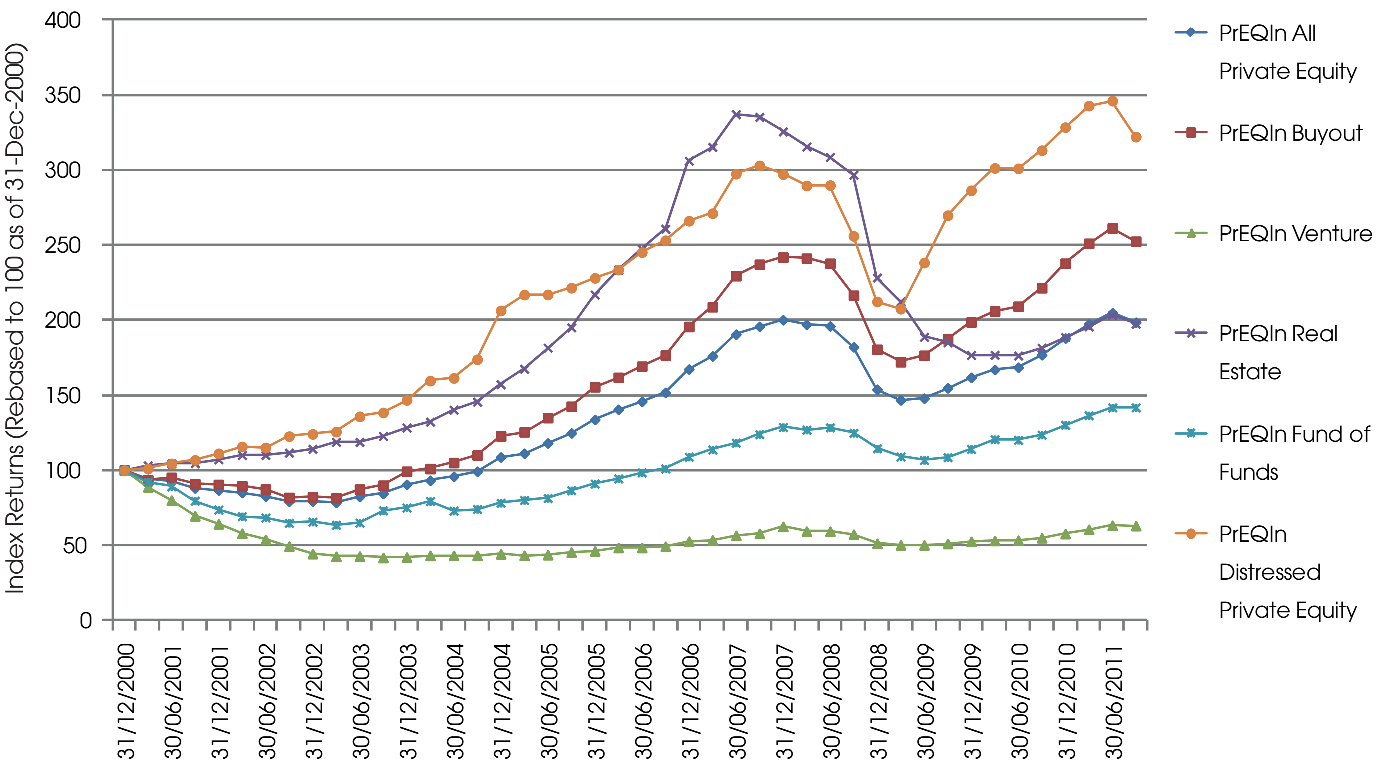
An examination of these indices gives an insight into the performance of the main private equity fund types in comparison to each other and to the asset class as a whole. The PrEQIn All Private Equity Index shows an initial decline after the dot-com crash in the early 2000s. Following this, the performance of the asset class steadily improved from Q2 2003 to Q4 2007, reaching 200.1 in December 2007. After that point returns across the asset class declined in response to not only the global financial crisis but also the introduction of mark-to-market valuations, which came into effect in December 2008. After the market bottomed out in Q1 2009, the index shows a quarter-on-quarter increase until the third quarter of 2011, when falling confidence surrounding the sustainability of the sovereign debt levels of some European countries caused instability in the financial markets. It should be noted that the latest two quarters are subject to change, with the former being in the advanced stages and the latter in the early stages of the data collection process.

Buyout funds hold the largest proportion of capital in the industry and this, coupled with using a money-weighted index, makes it no surprise that the trend exhibited by the PrEQIn All Private Equity Index is mirrored by the PrEQIn Buyout Index. After a period of growth from 2003 onwards, the index declined in 2008 and reached its lowest point in Q1 2009. Since then returns have increased each quarter, peaking in Q2 2011 at 261.3, before declining over the most recent quarter shown. Furthermore, it can be seen that the buyout index has been outperforming the PrEQIn All Private Equity Index since Q1 2001.

The PrEQIn Real Estate Index tracks the performance of real estate funds and from Q4 2000 it can be seen that the index increased steadily, reaching its highest point of 337.0 in Q2 2007 having outperformed all of the main strategies within the private equity asset class. However, real estate funds then suffered large write-downs in portfolio values, beginning with the sub-prime mortgage crisis in 2007, before the market bottomed out in the latter half of 2010. For the most recent quarters, the PrEQIn Real Estate Index is at a similar level to the PrEQIn All Private Equity Index and currently stands at 198.5 as of Q3 2011.

Distressed private equity is a more niche strategy within the private equity industry, and such funds aim to invest in companies that are bankrupt, or are facing bankruptcy or reorganization. The strategy

Fig. 1: PrEQIn Index: All Strategies



Source: Preqin

therefore carries a higher risk but can potentially provide greater returns for the investor. The PrEQIn Distressed Private Equity Index shows that this fund type has consistently outperformed the private equity asset class as a whole and has been one of the best performing strategies within the industry. The index shows a steady quarterly increase from Q4 2000 until Q3 2007 when distressed private equity began to be affected by the period of financial dislocation. From Q3 2009, the index increased sharply, and is currently the best performing private equity fund type, as managers have sought to take advantage of the relative abundance of distressed investment opportunities caused by the economic downturn.

The PrEQIn Venture Index shows that the performance of venture funds saw a steady decline from Q4 2000 until Q4 2003 caused by the technology crash in early 2000 resulting in large write-downs of portfolio valuations. Since this time, the index has remained relatively flat, reaching a peak of 63.2 in Q2 2011.

The PrEQIn Fund of Funds Index experienced a relatively steep quarter-by-quarter decrease during the early 2000s as many such vehicles had higher allocations to venture funds during this time. The decline experienced by the fund of funds index as a result of the financial crisis is less pronounced than for the other private equity strategies. It should be noted that fund of funds returns typically lag a quarter due to the reporting schedules of the underlying vehicles and as such the index reaches its lowest point Q2 2009; this is in contrast to the All Private Equity, Buyout, Venture and Distressed Private Equity Indices, all of which reached their lowest points in Q1 2009.

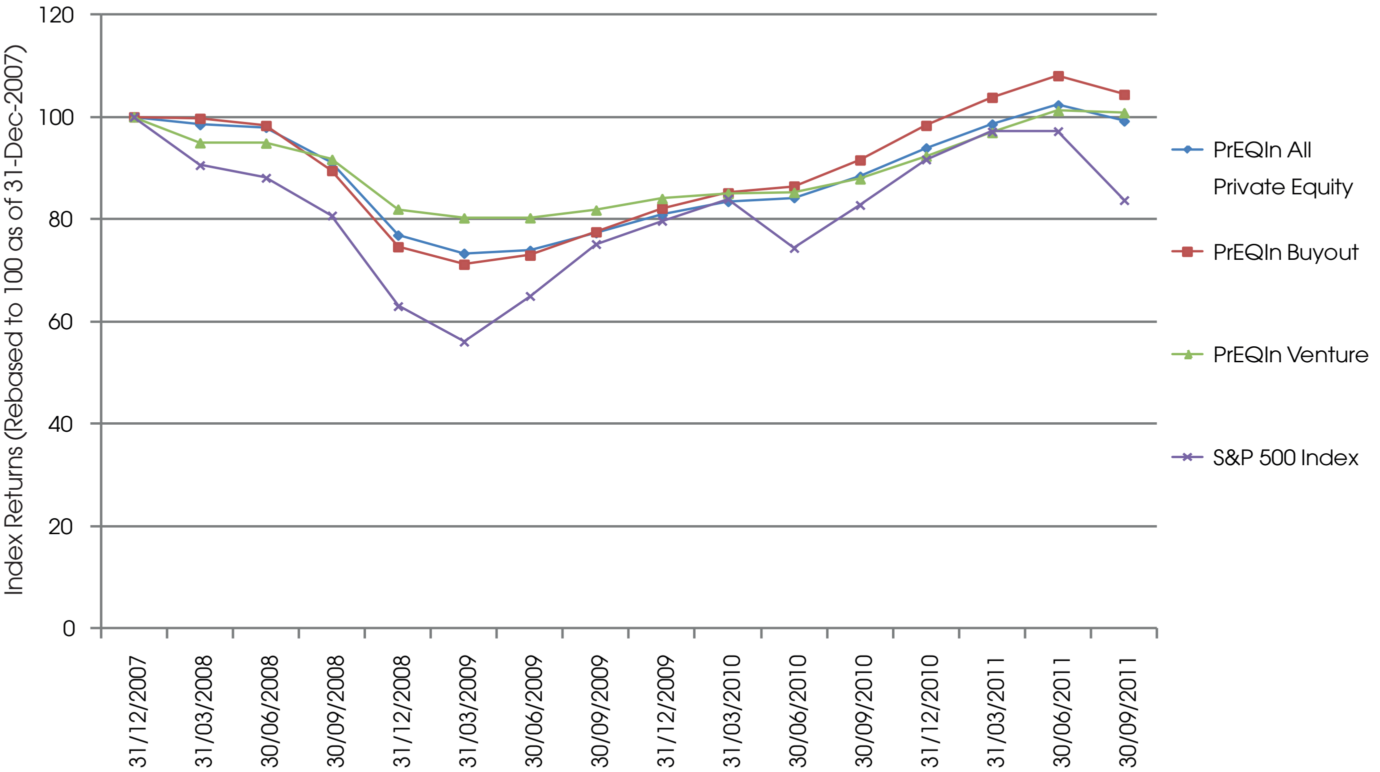
PrEQIn All Private Equity, Buyout and Venture Indices vs. S&P 500

Fig. 2 shows the PrEQIn All Private Equity, Buyout and Venture Indices compared to the quarterly S&P 500 Index rebased to 100 as of 31st December 2007, demonstrating the decline and subsequent recovery of these private equity strategies due to the financial crisis of 2008. By comparing their performance to the S&P 500 Index, we can gain an insight into how the private equity industry performed during this period compared to the listed markets. The graph shows that all of the indices reached their lowest points in Q1 2009, with the S&P 500 Index showing a greater initial decline in comparison to the PrEQIn Indices; however by Q1 2010 all the indices shown had recovered to a similar level. From Q1 2010, the private equity indices continue to recover at a steady rate whereas the S&P 500 Index is more variable, declining further between Q1 2010 and Q2 2010 before recovering. In the most recent quarter, all the indices in the graph have shown a quarterly drop as a result of the European sovereign debt crisis. It should be noted that Q3 2011 figures are based on preliminary results and could subsequently change.

Using this graph, we can also examine the effect of the financial crisis on the buyout and venture sectors in comparison to the wider private equity asset class. The PrEQIn Buyout Index shows a similar trend to the PrEQIn All Private Equity Index, both reaching their lowest points in Q1 2009 and subsequently recovering. From Q2 2010, the gap between the Buyout Index and the All Private Equity Index begins to widen, with the Buyout Index reaching its peak of 108.0 in Q2 2011 compared to a peak of 102.3 for the All Private Equity Index.

The PrEQIn Venture Index shows that the financial crisis had a relatively smaller effect on the performance of the venture index compared to the buyout index and private equity as a whole. The level of decline experienced by the venture index is less steep compared to buyout and all private equity. However the subsequent rate of increase is correspondingly smaller.

Fig. 2: PrEQIn Index: All Private Equity, Buyout and Venture vs. S&P 500



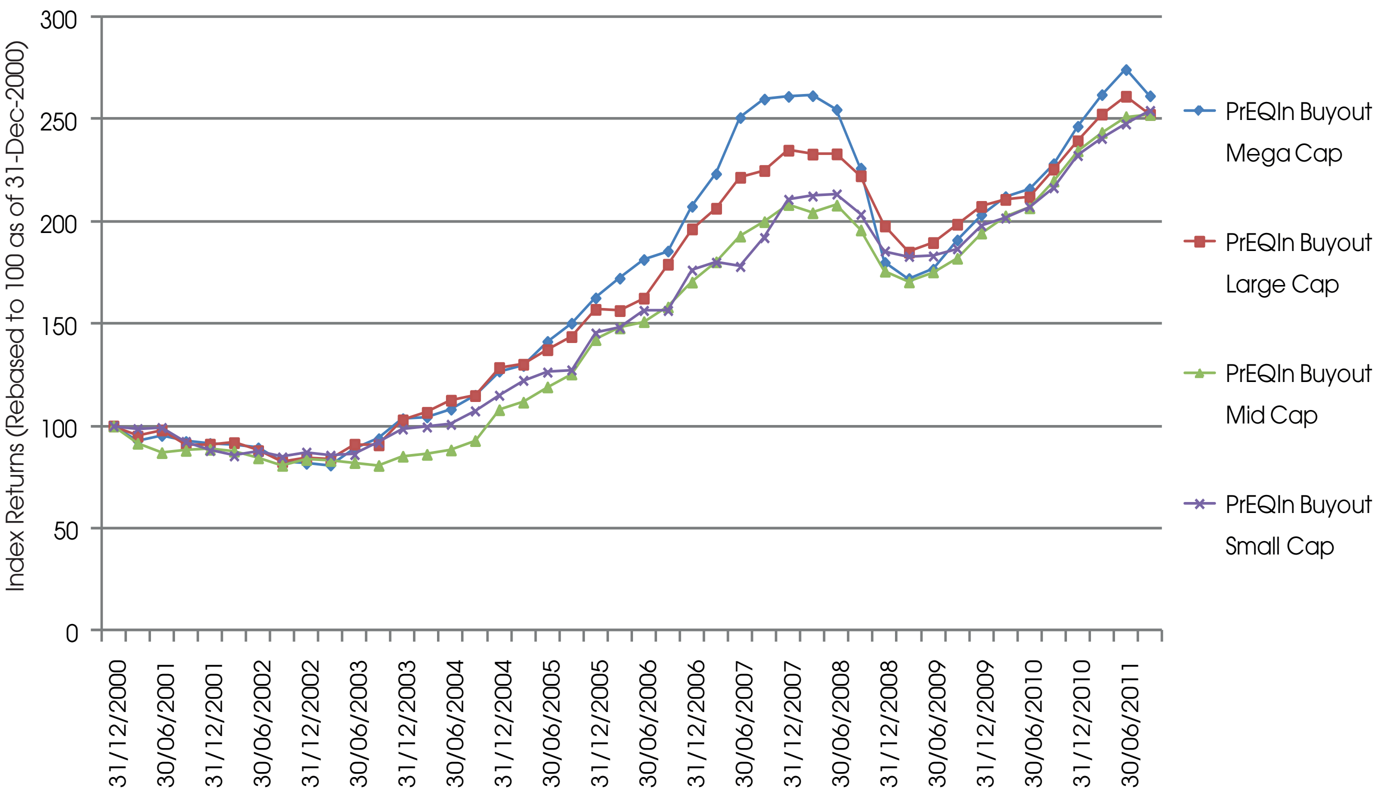
Source: Preqin

PrEQIn Index: Buyout by Fund Size

By classifying buyout funds into their respective size groups, it allows us to examine the trends within the buyout sector. Fig. 3 shows the relative performance within this sector by fund size by plotting the PrEQIn Buyout Mega Cap, Large Cap, Mid Cap and Small Cap Indices, all rebased at 100 as of 31st December 2000. The graph shows that initially, all four Indices maintain similar levels, declining gradually until Q1 2003. From Q3 2003, the Indices of all fund sizes begin to show quarterly increases, with Mega and Large Cap increasing at a faster rate than Mid and Small Cap. During 2007 and early 2008, the gap between the Mega and Large Cap Indices is at its widest, and the financial crisis then causes steep declines in all indices from Q2 2008. The Mega Cap Index shows the steepest decline, falling from 261.5 in Q1 2008 to 172.1 in Q1 2009 and dropping below both the Large Cap and Small Cap Indices. From Q1 2009 onwards, all Indices begin to show quarterly increases at similar rates, with the Mega Cap Index becoming the best performer again in Q2 2011.

The latest quarter has seen the Mega and Large Cap Indices both decrease, while the Mid and Small Cap Indices both show a quarterly increase; however, as Q3 2011 figures are preliminary results, this could subsequently change.

Fig. 3: PrEQIn Index: Buyout by Fund Size*



Source: Preqin

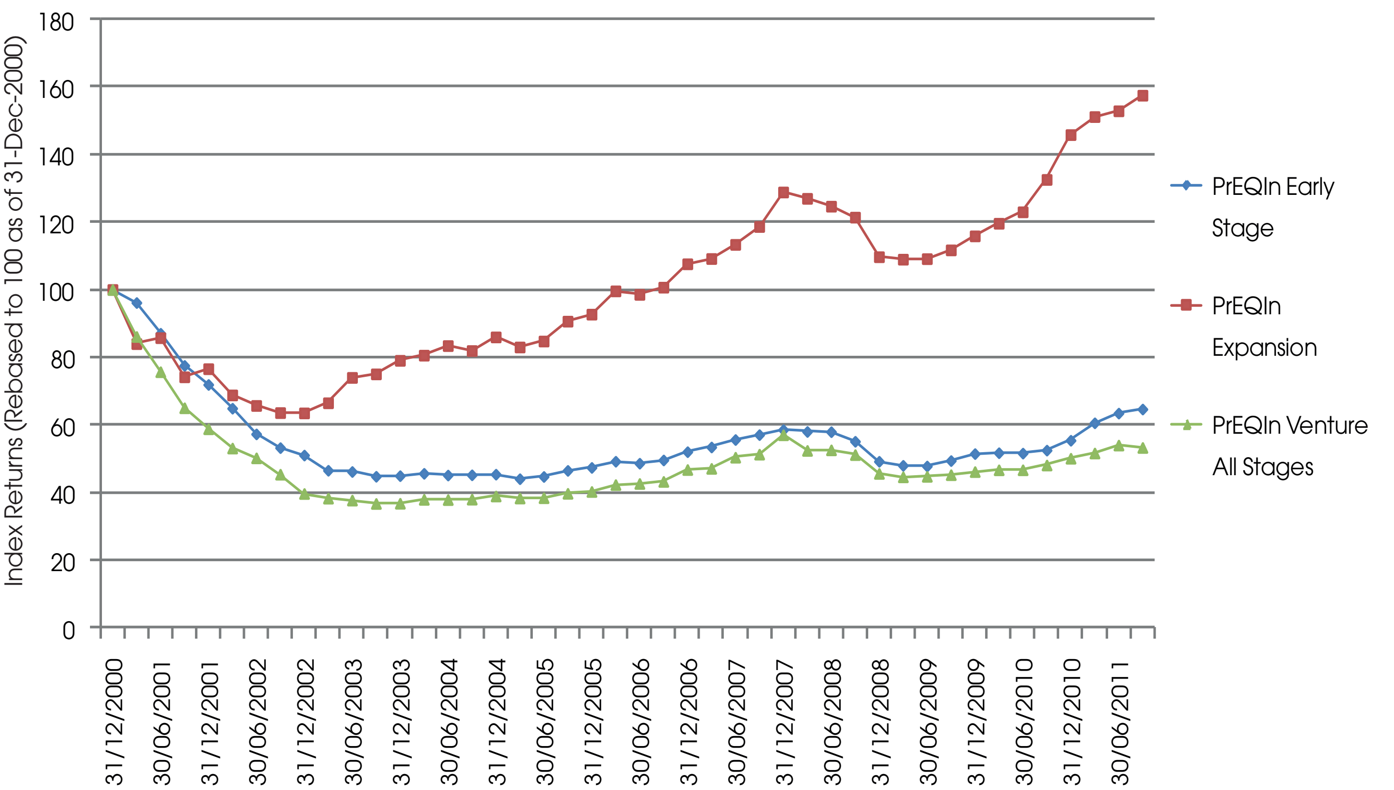
*Size ranges:
Vintage 1992-1996: Small Buyout ≤ $200mn, Mid Buyout $201mn-$500mn, Large Buyout > $500mn
Vintage 1997-2004: Small Buyout ≤ $300mn, Mid Buyout $301mn-$750mn, Large Buyout $751mn-$2bn, Mega Buyout > $2bn
Vintage 2005-2010: Small Buyout ≤ $500mn, Mid Buyout $501mn-$1.5bn, Large Buyout $1.51bn-$4.5bn, Mega Buyout > $4.5bn

PrEQIn Index: Venture by Investment Stage

Fig. 4 shows the PrEQIn Venture Index split out by venture investment stage focus. This allows us to gain an insight into the relative performance of early stage and expansion funds in comparison to venture funds that have no specific investment stage focus. The graph shows that the PrEQIn Early Stage Index follows a similar trend to the PrEQIn Venture All Stages index, declining initially until Q3 2003 and then gradually recovering until Q4 2007, when a further decline was experienced due to the financial crisis.

In contrast to the relatively flat performance of the Early Stage and Venture All Stages Indices, the PrEQIn Expansion Index shows more variability. After an initial decline, the Expansion Index then recovers, increasing to over 100 in Q3 2006. After the subsequent decline following the 2008 financial crisis, the Expansion Index shows quarterly increases, reaching 157.5 in Q3 2011.

Fig. 4: PrEQIn Index: Venture by Investment Stage



Source: Preqin

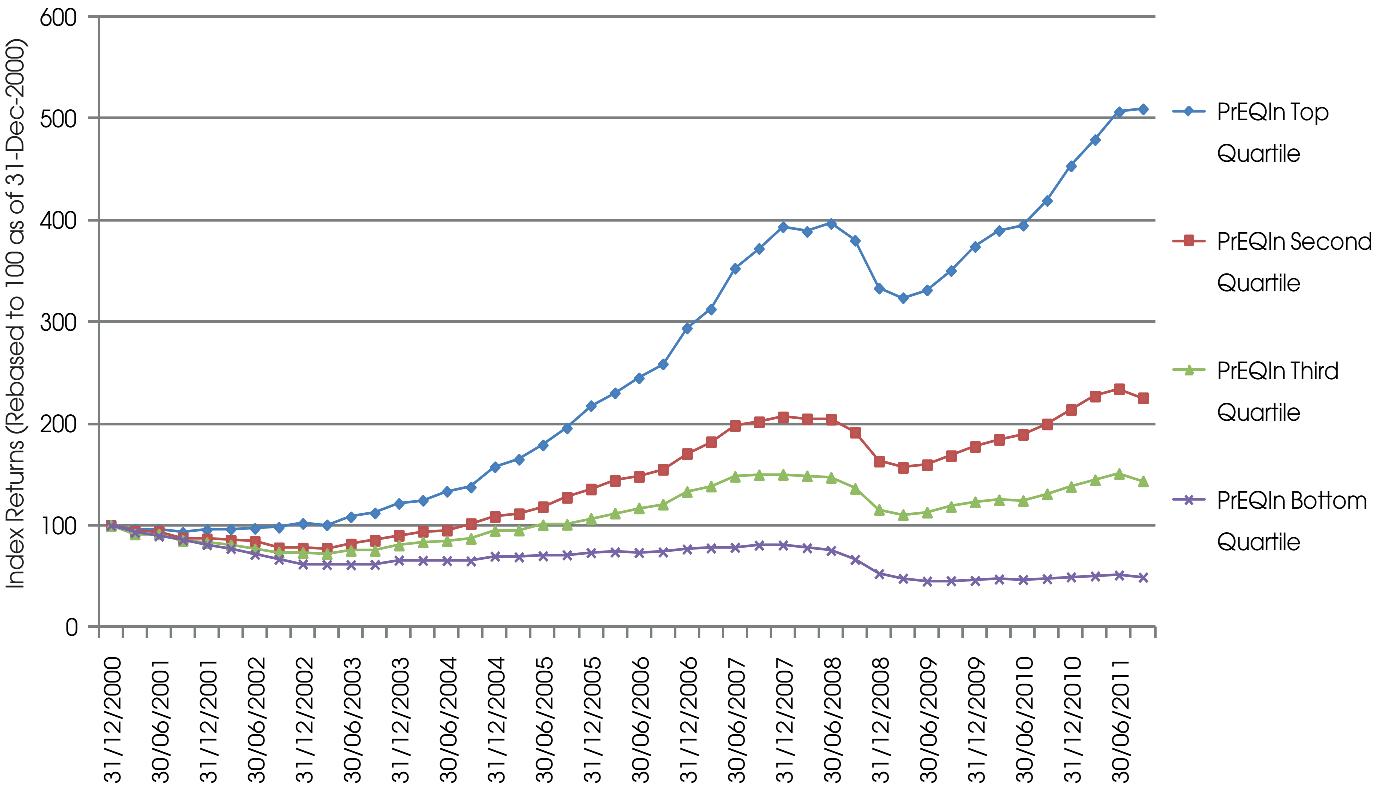
PrEQIn Index: Fund Quartile Indices

Preqin assigns quartile rankings to funds of the same vintage year, and where possible, funds which adopt similar strategies and a similar geographic focus. By calculating the PrEQIn Private Equity Quarterly Index rebased at 100 from 31st December 2000 for funds within each performance quartile ranking, we can shed light on the relative performance of each quartile. This is the focus of Fig. 5.

While the Indices of all four quartiles show quarterly declines initially, the Top Quartile Index increases back above 100 in Q4 2002, and the Second and Third Quartile Indices move back above 100 in Q3 2004 and Q2 2005 respectively. The Top Quartile Index continues to show steep quarterly increases, reaching 396.8 in Q2 2008, before declining due to the financial crisis. After several quarters of decline, the Top Quartile Index then begins to recover, passing 400 in Q3 2010, and stands at 509.5 as of Q3 2011.

The Second and Third Quartile Indices show similar trends through the periods shown and even with the effect of the financial crisis both indices remain above 100. The Bottom Quartile Index shows much flatter performance during the period. After reaching a peak of 80.7 in Q4 2007, the financial crisis caused subsequent quarterly decreases and the Index has remained relatively flat since this time, standing at 49.1 as of Q3 2011.

Fig. 5: PrEQIn Index: Fund Quartile



Source: Preqin

About Preqin

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

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