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Capital Dynamics Private Equity Review & Outlook

Summary H1 2013

US buyout

In brief

- Robust exit activity of US private equity funds shaped H1 2013, with the number of private equity-backed IPOs and dividend recaps breaking records. Distributions from follow-on sales of shares from previously floated companies contributed substantially to the elevated level of liquidity to investors.

Table: US buyout market data

USD billion	H112	H113	Q212	Q113	Q213	Dy/y	Dq/q
Fundraising	89.1	**88.2**	46.2	33.1	**55.2**	(1%)	67%
Investments	36.3	**66.5**	22.7	21.8	**44.7**	83%	105%
Exits	53.1	**75.6**	22.7	21.4	**54.2**	42%	153%
Drawdowns	27.3	n/a	16.1	**6.6**	n/a	(41%)	(67%)
Distributions	40.2	n/a	25.2	**19.4**	n/a	29%	(48%)
Appreciation as % of NAV	5.4%	n/a	(0.0%)	**3.0%**	n/a	(2%)	0.2%
10 year pooled net IRR	9.0%	n/a	9.0%	**10.8%**	n/a	1.9%	0.4%

Notes: Dq/q is the comparison of Q2 2013 vs. Q1 2013 for fundraising and deals and Q1 2013 vs. Q4 2012 for cash flows and performance data. Dy/y is the comparison of H1 2013 vs. H1 2012 for fundraising and deals and Q1 2013 vs. Q1 2012 for cash flows and performance data. n/a – data not available.
Source: Thomson ONE, S&P Capital IQ, as of September 18, 2013. Cash flows, appreciation, and 10-year pooled net IRR data are as of March 31, 2013.

Fundraising

- Private equity fundraising was steady during H1 2013, powered by mid-market funds

Following a quiet start, fundraising accelerated in the second quarter. LPs committed USD 55 billion to private equity funds during the second quarter, the most since the third quarter of 2008. Fundraising through the first six months kept pace with last year, powered by mid-market buyout funds. Buyout funds with target sizes between USD 0.5 billion – 3.5 billion raised USD 30 billion during the first half of 2013; 56% more than last year. Among large and mega funds, Silver Lake's Fund IV raised USD 6.3 billion in the first half and closed at USD 10.3 billion – USD 1 billion more than the predecessor fund. Nevertheless, commitments to large and mega funds were still down 22% in the first half, to USD 20 billion, year-over-year.

Investments

- Leverage in buyouts increased; companies with stronger earnings were acquired

Investment activity was mixed. On one hand, the first half of 2013 marked the return of mega buyouts, which drove an 83% increase in completed deal values and reflected GP confidence and the strength of credit markets. On the other hand, the number of completed deals declined 13% to 750 deals from the year-ago period. Buoyant credit markets allowed GPs to finance deals with less equity: buyout funds contributed 32% during the first half, down from 39% in 2012. However, increased financial risk was to some extent mitigated by better terms and/or stronger EBITDA of acquired businesses as average interest coverage ratios increased to 3.21, up from 2.90 in 2012 and well above the 2.10 seen during 2007.

Exits

- Exits increased as IPOs and dividend recaps rose to historic highs

Exit activity intensified in the second quarter, driving a 42% increase in exit values during the first half. Bullish public markets spurred IPO exits and resulted in the most animated quarter ever for the buyout industry: 22 IPOs raised USD 11 billion. Credit markets continued providing liquidity for buyout fund investors, indicated by yet another record-breaking quarter boasting USD 19.5 billion in dividend recaps. M&A exits and deal values increased on the quarter, aided by the USD 11.6 billion sale of Bausch & Lomb by Warburg Pincus and Welsh, Carson, Anderson & Stowe to Valeant Pharmaceuticals. However, in line with overall M&A activity, private equity-backed M&A exits were muted compared with the first half of 2012, which saw 20% more exit deals.

Outlook

- Market conditions continue to favor exits, which could outpace investments

Exits and distributions are expected to continue increasing, and at a faster pace, supported by strong public equity and capital markets. The investment pace of platform acquisitions will likely be constrained by the lack of opportunities, as overall M&A activity remains subdued. In such an environment, private equity firms will continue to enhance portfolios through add-on acquisitions and/or the optimization of capital structures.

US venture capital

In brief

- Fewer and smaller funds were raised in H1 2013
- Cautious VC investment activity continued, while valuations climbed
- An open IPO window spurred VC exits; biotechnology IPOs shined

Table: US venture capital market data

USD billion	H112	H113	Q212	Q113	Q213	Dy/y	Dq/q
Fundraising	11.1	**7.4**	6.3	4.3	**3.1**	(33%)	(28%)
Investments	15.9	**14.6**	8.7	7.4	**7.2**	(8%)	(2%)
Exits	32.5	**16.3**	20.6	6.2	**10.0**	(50%)	61%
Drawdowns	2.5	n/a	1.1	**0.7**	n/a	(50%)	(22%)
Distributions	3.8	n/a	1.6	**1.4**	n/a	(33%)	(50%)
Appreciation as % of NAV	5.4%	n/a	0.4%	**1.0%**	n/a	(1%)	0.9%
10 year pooled net IRR	3.9%	n/a	3.9%	**5.7%**	n/a	2.4%	0.4%

Notes: Dq/q is the comparison of Q2 2013 vs. Q1 2013 for fundraising and deals and Q1 2013 vs. Q4 2012 for cash flows and performance data. Dy/y is the comparison of H1 2013 vs. H1 2012 for fundraising and deals and Q1 2013 vs. Q1 2012 for cash flows and performance data. n/a – data not available.
Source: Thomson ONE, Dow Jones VentureSource, as of September 18, 2013. Cash flows, appreciation, and 10-year pooled net IRR data are as of March 31, 2013.

Fundraising

- Q2 fundraising was the slowest since Q3 2011

Venture fundraising slowed significantly in the second quarter. As a result, the total amount of capital raised during the first half of 2013 was down by a third and the number of funds declined 17% to 92 from the first half of 2012. The decline reflected the absence of any billion-dollar fund closings compared to the three that took place in the first half of last year. Battery Ventures raised USD 650 million and Matrix Partners raised USD 450 million in the second quarter; the largest funds to close during the first half of 2013. Overall, the drop in venture fundraising was attributable primarily to the smaller target sizes of funds seeking commitments during the first half of 2013 rather than to any change in LP sentiment toward venture capital.

Investments

- VC investments in IT companies dipped; the healthcare industry regained attractiveness

Venture deal flow has trended downward over the past four quarters. There were 1,606 venture financings during the first half of 2013, 11% less than the prior year. Invested capital was down 8% during the same period. IT deals, the largest industry target for US venture, cooled in the first half of 2013, following four strong quarters in 2012. Amounts invested in IT companies decreased 19% to USD 4.1 billion across 514 deals. In contrast, investments in healthcare companies gained traction during the period. During the first half of 2013, healthcare companies received 14% more capital from venture capital firms as compared with the first half of 2012.

Exits

- M&A exit values and IPOs increased in 2Q 2013, but trailed last year's benchmarks

Large corporations stepped up their acquisitions of venture-backed companies in the second quarter: several high-profile billion-dollar exits were announced, including the acquisition of Waze by Google, Pearl Therapeutics by AstraZeneca and Tumblr by Yahoo! for a combined value of USD 3.6 billion. Despite these high-profile successes, overall M&A exits remained sluggish compared with the first half of 2012. IPO activity soared during the second quarter, with 24 IPOs (twice as many as in the first quarter) raising USD 2.4 billion in initial proceeds. Biotech companies accounted for almost half of all IPOs during the first six months of 2013. Their positive post-IPO performance contributed toward the 27% gain to the NASDAQ Biotechnology index. In addition, many venture firms took advantage of a strong stock market during the first half of the year (the NASDAQ Composite Index gained 13%) to realize liquidity on companies that had completed IPOs in the prior two years.

Outlook

- Venture performance is expected to improve, driven by IPOs and higher public prices

Venture performance is expected to keep posting improvements as long as public markets remain robust. Venture IPO exit activity is on track to be the most successful since the dotcom era. Venture investment activity however, while expected to remain fairly stable overall, may vary significantly across sectors.

European buyout

In brief

- Large and mid-market buyout deals recovered as confidence and debt markets gradually improve
- Secondary exits and robust public markets provided liquidity for private equity funds
- Fundraising continued to rebound, and is on track to reach a five-year high

Table: European buyout market data

EUR billion	H112	H113	Q212	Q113	Q213	Dy/y	Dq/q
Fundraising	17.9	**26.1**	6.3	10.9	**15.2**	46%	**40%**
Investments	31.5	**33.5**	16.9	8.9	**24.5**	6%	**174%**
Exits	38.9	**34.5**	26.1	8.8	**25.6**	(11%)	**190%**

Notes: Dq/q is the comparison of Q2 2013 vs. Q1 2013. Dy/y is the comparison of H1 2013 vs. H1 2012.
Source: Thomson ONE, unquote data, as of September 18, 2013. European private equity cash flow and performance data for 2013 has not yet been published by Thomson ONE.

Fundraising

- Fundraising volume and the number of funds raised increased 46%

The first half of 2013 saw a turnaround in European fundraising, with buyout and other private equity funds raising EUR 15.2 billion in the second quarter, the most since the fourth quarter of 2008. The turnaround was broad-based: the number of funds holding a close increased 46% to 57 during the first half year-over-year. Apax Partners raised EUR 2.4 billion of its EUR 5.7 billion fund in the first half of 2013. This was also the largest buyout fund closed during the first half of 2013. Mid-cap buyout managers continued to receive investor support: HgCapital raised EUR 2.3 billion, the largest fund raised during the first half of 2013 by GPs focused on mid-market buyout deals.

Investments

- Average buyout deal sizes expanded in H1 2013, while deal numbers declined

Following a quiet first quarter, buyout deal values bounced back strongly in the second, driven by large-cap deals. There were 12 deals exceeding EUR 500 million compared with just one during the first quarter. Germany was home to a number of large deals including BC Partners' EUR 3.3 billion acquisition of Springer Science from EQT Partners. Mid-market buyout deal values were up 10% quarter-over-quarter and 3% year-over-year during the first half. However, overall deal flow declined 20% from the prior year, mainly due to a slowdown in small-cap buyouts. Mid-market deal flow was resilient, accounting for 70% of all deals, up from 60% a year ago. While acquisitions of private and family-owned businesses faded, secondary buyouts accelerated.

Exits

- In H1 2013, large exit deals were either secondary exits or public offerings

Exit deal values also reflected the surge in secondary acquisitions, which nearly tripled from the first quarter. In the first half, six of the top 10 largest exits were secondary exits. The other four largest exits were IPOs such as the offering of Belgium bpost by CVC Capital Partners and follow-on sales of public holdings. Overall, despite the boost robust stock markets gave to IPO exits, total exit deal value declined 11% during the first half versus the same period a year ago. However, activity measured by the number of exits gained pace, indicating an improved exit environment.

Outlook

- Improving confidence should drive a recovery in buyout deals in H2 2013

Attractive mid-market buyout opportunities continue to arise, though fundraising remains highly competitive as many managers return to market. Fundraising among just a few of the industry's largest players could drive overall amounts raised to a five-year high, based on current trends. Deal flow is improving as macroeconomic risks continue to abate, although volatility persists. Slower than expected trade-buyer activity will likely curtail exits. However, improving capital markets and the acceleration in buyout firm investing will continue to drive exit opportunities and liquidity.

European venture capital

In brief

- Venture capital investments continued to recover
- Exits were boosted by large corporate M&A activity
- Small funds dominated fundraising and select brand-name managers attracted top LP money

Table: European venture capital market data

EUR billion	H112	H113	Q212	Q113	Q213	Dy/y	Dq/q
Fundraising	1.8	**1.3**	1.0	0.8	**0.5**	(26%)	(44%)
Investments	2.4	**2.4**	1.4	1.1	**1.3**	0%	24%
Exits	3.0	**3.7**	2.0	2.0	**1.8**	23%	(11%)

Notes: Notes: Dq/q is the comparison of Q2 2013 vs. Q1 2013. Dy/y is the comparison of H1 2013 vs. H1 2012.
Source: Thomson ONE, Dow Jones VentureSource, as of September18, 2013. European VC cash flow and performance data for 2013 has not yet been published by Thomson ONE.

Fundraising

- Fundraising was sluggish in Q2 2013

Halfway through 2013, fundraising levels trailed those of the prior year significantly. During the second quarter, the dearth of large fund closings dragged the amount of raised capital down to the lowest point in seven quarters. The largest fund, Switzerland-based BB Entrepreneur Europe Fund, received EUR 100 million from investors during the second quarter. In contrast, the previous quarter included a EUR 368 million close of the Accel London IV Fund, which closed after a very short (eight-week) due diligence process. European fundraising remained difficult for first-time funds: only three such funds out of 25 raised capital during the first half of the year. A lack of late-stage venture funds was also another distinctive feature of the fundraising landscape.

Investments

- VC investments in healthcare companies surged

The first half of the year saw a solid rise in deal flow, which balanced a decline in the average size of financing rounds. In particular, venture investments accelerated during the second quarter, with the number of deals and invested capital increasing 16% and 24% respectively from the previous quarter. A 14% increase in healthcare deal flow was the largest contributor. The consumer services industry retained its position as the industry attracting the most venture money. During the first half, consumer services companies received EUR 689 million or nearly 30% of all venture financing and accounted for 25% of overall deal flow. The largest venture investment of the second quarter was in consumer services as well, with Summit Partners contributing a EUR 100 million financing round to KupiShoes LLC, an online retailer servicing the Russian market. Indeed, Russia is becoming a market of increasing focus for venture and growth investors.

Exits

- M&A exits rose; IPO exits were rare

Exit levels continued to improve in the second quarter, supported by M&A activity of large corporations. There were 36 M&A exit deals, up from 31 during the first quarter, several of which were notable in size: GlaxoSmithKline acquired Italian biotech company Okairos from Versant Ventures for EUR 250 million, and Cisco Systems paid EUR 235 million for the UK-based IT company Ubiquisys to a consortium including Accel Partners, Advent Venture Partners and Atlas Venture. The IPO exit route continued to play a minor role in European venture. There were four IPO exits in the first half of 2013 compared with nine last year.

Outlook

- Ongoing improvement in the macro environment is expected to support VC activity

The recovery in European venture deal activity is expected to stabilize. A slowly improving macroeconomic environment, including both the Eurozone and the European Union's recent returns to growth, should support European venture activity in the upcoming quarters.

Asia-Pacific private equity

In brief

- Regional fundraising tapered down as Chinese fundraising levels stabilized
- The pace of growth capital investment was subdued, but held steady for buyouts
- M&A exits advanced, while regulation in China impacted private equity-backed IPOs

Table: Asia-Pacific private equity market data

USD billion	H112	H113	Q212	Q113	Q213	Dy/y	Dq/q
Buyout fundraising	5.6	**3.2**	4.9	2.2	**1.0**	(43%)	(55%)
Growth fundraising	20.4	**18.6**	8.9	14.5	**4.1**	(9%)	(72%)
Buyout investments	13.6	**14.6**	8.5	6.6	**7.9**	7%	19%
Growth investments	20.6	**16.6**	10.7	6.1	**10.5**	(19%)	72%
M&A exit values	16.3	**23.2**	9.8	15.0	**8.2**	42%	(45%)
IPO exit values	12.1	**4.1**	9.2	1.0	**3.2**	(66%)	218%

Notes: Investment & exit values are enterprise values. IPO exit values are total proceeds raised by all shareholders including non-PE investors.
Source: Asian Venture Capital Journal database, as of September 18, 2013. Dq/q is the comparison of Q2 2013 vs. Q1 2013. Dy/y is the comparison of H1 2013 vs. H1 2012.

Fundraising

- Regional fundraising declined 16% y/y; China remained the largest contributor despite a slowdown

Subdued fundraising continued into the first half of 2013. Commitments to Asia-Pacific funds declined 19% to USD 21.8 billion from the prior year. Japan was a bright spot, the only regional market to experience gains in fundraising, driven by corporate venture and private equity distressed debt funds. Chinese funds raised USD 15.7 billion, 19% less than a year ago, pushed down by a sharp decline in RMB fundraising. Nevertheless, China continued to dominate the regional fundraising landscape, attracting 70% of all capital raised. A number of highly sought managers closed large funds this year, such as Affinity Asia (USD 2.5 billion) and CDH China (USD 2 billion). The third quarter opened with KKR closing the largest-ever Asia-Pacific private equity fund at USD 6 billion, and MBK Partners is expected to hold a final close at USD 2.6 billion.

Investments

- Investments faltered on sluggish growth capital activity; buyout deals held steady

A slowdown in growth capital deal flow pushed investment levels down during the first half from the prior-year period. Deal making was cautious on ongoing concerns over short-term economic growth prospects in China and the country's stalled IPO environment. However, other large markets such as India posted a 27% gain in growth-capital deal values year-over-year. In contrast, buyout deal flow remained steady and deal values expanded year-over-year. Large buyout deals in Australia and South Korea contributed to a 7% increase in deal values during the first half. Of note, South Korean private equity investments expanded rapidly since the second half of last year. Deal values, which included the USD 958 million buyout of clothing company NEPA by MBK Partners, soared 56% in the first half to USD 4.4 billion.

Exits

- M&A exits advanced throughout the region; IPO exits retreated to 2001 levels

Exits through IPOs fell to a new low with just 33 offerings completed during the first half of 2013, a level not seen since 2001. However, the surge in stock market prices outside of China supported the USD 1.6 billion follow-on offering of Japanese Aozora Bank by Cerberus Capital Management and the USD 1.3 billion partial sale of Indonesian Matahari Department Store shares by CVC Asia Pacific to public investors. In contrast, M&A exits rose in the first half of 2013, with all sub-regions demonstrating robust growth. In China, GPs shifted their focus to M&A exits as IPOs remain on hold due to government regulation. In the first half, 78 exits through M&A took place in China, 16% more than a year ago and outpacing IPO exits for the first time ever.

Outlook

- Asia-Pacific continues to present attractive fund and portfolio investment opportunities

The highly competitive fundraising environment will continue to offer attractive fund investments for LPs. Volatility in capital markets and the current uncertain economic growth outlook is likely to drag down investment activity in the second half of the year, yet also present sound investment opportunities.

Emerging Markets (Ex. Emerging Asia)

In brief

- Investments trended down during H1 2013. However, Q2 showed clear signs of improvement q/q, with investments increasing in most key emerging markets
- Fundraising in emerging markets improved significantly in Q2 but has not yet reached 2012 levels
- Private equity continued to be a key growth driver for emerging markets. We expect this expansion of private equity to persist throughout the remainder of 2013, despite the apparent political and social issues across many of the key geographies

Table: Emerging Markets (ex. Emerging Asia) private equity market data

USD million		H112	H113	Q212	Q113	Q213	Dy/y	Dq/q
MENA	Fundraising	96	**219**	13	104	**115**	128%	11%
	Investments	437	**168**	0	54	**114**	(62%)	111%
	Number of deals	17	**17**	6	9	**8**	0%	(11%)
SSA	Fundraising	489	**100**	196	38	**62**	(80%)	63%
	Investments	605	**850**	163	100	**751**	40%	654%
	Number of deals	28	**36**	13	15	**21**	29%	40%
CEE & CIS	Fundraising	2,592	**553**	531	365	**188**	(79%)	(49%)
	Investments	973	**218**	863	99	**119**	(78%)	20%
	Number of deals	53	**35**	31	18	**17**	(34%)	(6%)
Russia	Fundraising	82	**126**	82	126	0	54%	(100%)
	Investments	639	**65**	589	58	**7**	(90%)	(88%)
	Number of deals	20	**14**	15	8	**6**	(30%)	(25%)
Latin America & Caribbean	Fundraising	1,651	**2,491**	626	558	**1,933**	51%	246%
	Investments	1,408	**1,218**	649	242	**976**	(13%)	303%
	Number of deals	48	**48**	21	22	**26**	0%	18%
Brazil	Fundraising	675	**758**	550	161	**597**	12%	270%
	Investments	1,271	**689**	589	120	**569**	(46%)	374%
	Number of deals	29	**30**	13	11	**19**	3%	73%
Emerging Markets (Ex. Em. Asia)	**Fundraising**	4,828	**3,363**	1,366	1,065	**2,298**	(30%)	116%
	Investments	3,423	**2,454**	1,675	495	**1,959**	(28%)	296%
	Number of deals	146	**136**	71	64	**72**	(7%)	13%

Notes: Data for Russia and Brazil is also included in CEE &CIS and Latin America & Caribbean, respectively.
Source: Emerging Markets Private Equity Association, as of August 31, 2013. Dq/q is the comparison of Q2 2013 vs. Q1 2013. Dy/y is the comparison of H1 2013 vs. H1 2012.

Brazil

- In Q2 2013, Brazil's economy and private equity environment showed signs of stabilization and improvement

Fundraising in Brazil was strong during the second quarter (USD 597 million), resulting in nearly three times the amounts raised in the first quarter. Overall, the first six months of 2013 started well, with USD 758 million raised, surpassing the USD 675 million raised in the same period of 2012. BTG Pactual's successful fundraising for its second infrastructure fund was responsible for Brazil's strong fundraising performance: In the first six months of 2013, the manager secured USD 554 million in commitments, far ahead of the second-largest closing of a Brazil-dedicated fund, which was Aqua Capital Partners' with USD 56 million.

Increasing investment volumes further underpinned the solid fundraising environment in Brazil. Second-quarter investment figures jumped 374% to USD 569 million from USD 120 million in the first quarter. The most significant contributors to the higher investment volume were General Atlantic (USD 198 million) and Denham Capital Management (USD 125 million). Additionally, Brazil's recovering economy as well as the effects of post-monetary and fiscal stimulus measures supported the overall private equity environment. In the short-to-medium term, however, some uncertainties remain.

Middle East North Africa (MENA)

- Private equity struggled as political turbulence affected investor sentiment and economic development

Despite some signs of stabilization, private equity still has limited traction in the MENA region. Uncertainty related to the Arab Spring continued to weigh on sentiment in the private equity community. Fundraising was up 11% to USD 115 million in the second quarter compared to USD 104 million in the first. Investment volume, however, was still significantly below 2012 levels – USD 168 million in the first half compared to USD 437 million in the year-ago period.

Seventeen deals were closed in the MENA region during the first six months of this year. While the number of investments was the same in the first half of 2012, the average deal size was significantly lower, dropping to USD 9.8 million from USD 25.7 million. Most of the deals closed in the United Arab Emirates, translating into USD 2 million. Interestingly, most equity was directed to Egypt. The crisis-shaken country attracted USD 112 million in three transactions. Actis, with its USD 102 million investment in Edita Food Industries, was the primary contributor of investment activity in Eqypt.

Sub-Saharan Africa (SSA)

- SSA continued as a “two-speed” region in terms of economic development and private equity

The two-speed theme continued with middle-income countries such as South Africa offering relative stability, and low-income yet resource-rich economies continuing to be dynamic and outpacing their middle-income peers in terms of economic growth. Overall fundraising in Sub-Saharan Africa in the first half of the year was down significantly from the year-ago period, to USD 100 million from USD 489 million. After the skewed fundraising environment in 2012 (Ethos Private Equity raised USD 800 million), this year’s driver of capital collection was Adenia Partners with USD 57 million.

In contrast to fundraising, the investment pace in SSA increased markedly in 2013. While the year-ago period saw USD 605 million in investments, USD 850 million was invested in the first half of this year, translating into a growth rate of 40%. In line with the two-speed regional theme, Kenya, a relatively low-income country, attracted the most capital (USD 612 million across seven deals). South Africa attracted USD 43 million across six deals. Other SSA markets, such as Nigeria (USD 34 million), Ghana (USD 30 million) and Senegal (USD 21 million), played less significant roles in first-half fundraising.

Turkey and Russia/CEE/CIS

- Fundraising was weak in H1 2013 compared to 2012, which featured several sizeable final closes

Economic stabilization and development continued to be the driving forces in the region. Fundraising in Poland was indicative of its developed market, while Turkey dropped behind as its unresolved societal conflicts continued to hamper the country’s economic expansion. After a weak start in the first quarter, with USD 365 million raised, the situation deteriorated further in the second, with USD 188 million raised. Key regional contributors were CapMan with USD 126 million, Abris Capital Partners with USD 108 million and Unicorn Capital Partners with USD 100 million.

Regional investment activity developed in a similar fashion. Whereas USD 973 million was invested in CEE/CIS and Russia in the first half of last year, the same period in 2013 only saw USD 218 million of new investment capital. Russia in particular experienced a significant drop – nearly 90% – in investment activity. The number of deals in the region, however, decreased to a lesser extent (34%). In the first half last year, 53 deals closed compared to 35 the same period this year. Most equity was targeted toward Poland (USD 146 million across seven deals) and Russia (USD 65 million across 14 deals).

Private equity secondary

- The absence of large portfolio deals cut secondary deal volume in half

Secondary market transactions in the first half of 2013 amounted to USD 7 billion, representing approximately 50% of the volume seen during the first half of both 2011 and 2012. In our experience, such a drop in deal volume is a reflection of the slowdown in the large end of the market as the supply of big portfolio deals from public pension funds and financial institutions diminished in the first six months of the year. In contrast, the smaller end of the market, which represents a more diverse seller's base, continued to produce steady deal flow.

- Secondary deal pricing rose, primarily on expected portfolio write-ups of traded LP interests

Overall, we saw decreasing discounts as sellers priced in projected higher private equity valuations that typically move in the same direction as public equities. Thus, the rise in overall pricing, as indicated by some industry reports, is not surprising given a widespread run-up in public equity prices, including a 13% gain in the S&P 500 during the first half of the year. The Cogent Secondary Pricing Trends and Analysis Report indicates that average first-round bids increased to 84% of NAV in the first half from 80% of NAV at the end of the 2012 period. While the average bid increase may not appear initially significant, the same report indicates that 10% of buyout fund secondary deals were priced at par or at premium this year, versus only 1% in 2012. However, as reiterated by research conducted by HEC Paris, pricing is just one of the factors that drives secondary fund performance. Ultimately, the quality of the assets and funds purchased is the most important factor for realized secondary fund performance.

- We expect increased deal flow at the lower end of the market

Looking forward, we expect a higher supply of deal flow at the lower end of the market. In contrast, we believe there will be a reduced supply of deal flow at the larger end of the market because of the diminishing liquidity needs of larger LPs due to improved distributions, and a relative under-allocation to private equity due to strong public equity performance.

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