Coller Capital

Global Private Equity Barometer

WINTER 2013-14

A UNIQUE PERSPECTIVE ON THE ISSUES AND OPPORTUNITIES
FACING INVESTORS IN PRIVATE EQUITY WORLDWIDE

Coller Capital's *Global Private Equity Barometer*

Coller Capital's *Global Private Equity Barometer* is a unique snapshot of worldwide trends in private equity – a twice-yearly overview of the plans and opinions of institutional investors in private equity (Limited Partners, or LPs, as they are known) based in North America, Europe and Asia-Pacific (including the Middle East).

This 19th edition of the *Global Private Equity Barometer* captured the views of 113 private equity investors from round the world. The Barometer's findings are globally representative of the LP population by:

- Investor location
- Type of investing organisation
- Total assets under management
- Length of experience of private equity investing

Contents

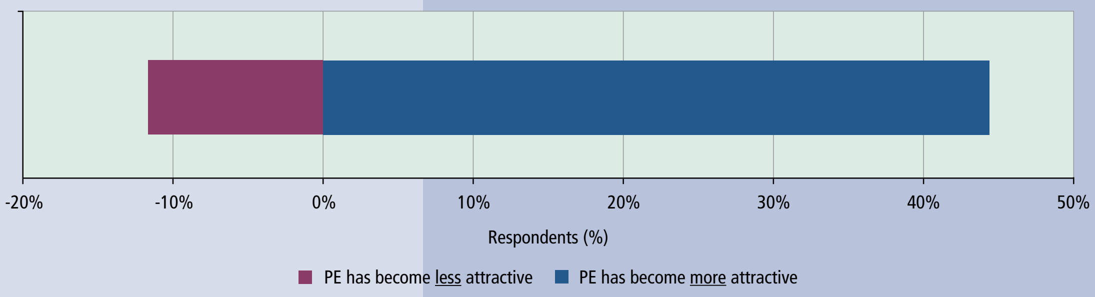
Topics in this edition of the Barometer include investors' views and plans regarding:

- PE as an asset class after the financial crisis
- Return expectations & appetite for PE
- The risk of private vs public equity
- The appropriate level of hurdle rates
- The LP workplace
- Expectations for capital calls & distributions
- Direct investments & co-investing by LPs
- The secondaries market
- Regional PE markets
- Venture capital & innovation
- The debt markets

PE more attractive to many investors since the GFC

Economic volatility has increased since the global financial crisis (GFC) began. 44% of LPs believe this increased volatility has made the PE asset class more attractive. Only 12% of investors think private equity has become less attractive.

LPs' views of PE since the financial crisis

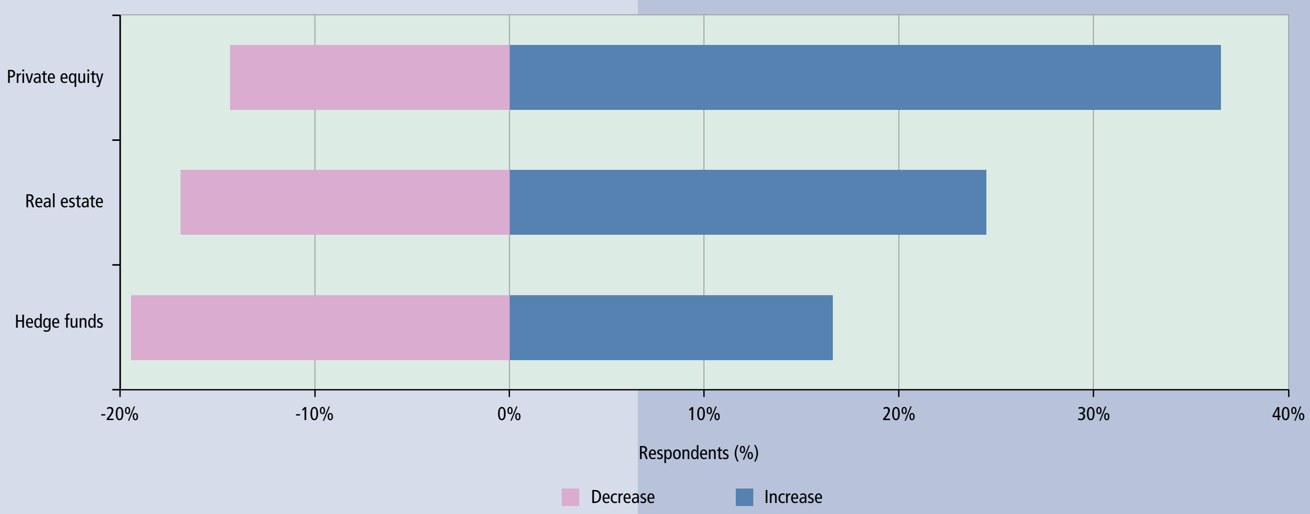


(Figure 1)

Target allocations to PE increase vs RE and hedge funds

37% of LPs plan to increase their target allocation to private equity over the next 12 months, compared with 14% who plan to reduce it. LPs' appetite for real estate and hedge funds remains mixed, with fairly equal proportions of investors planning to increase and decrease their target allocations.

LPs' planned changes to their alternative assets allocations over the next year



(Figure 2)

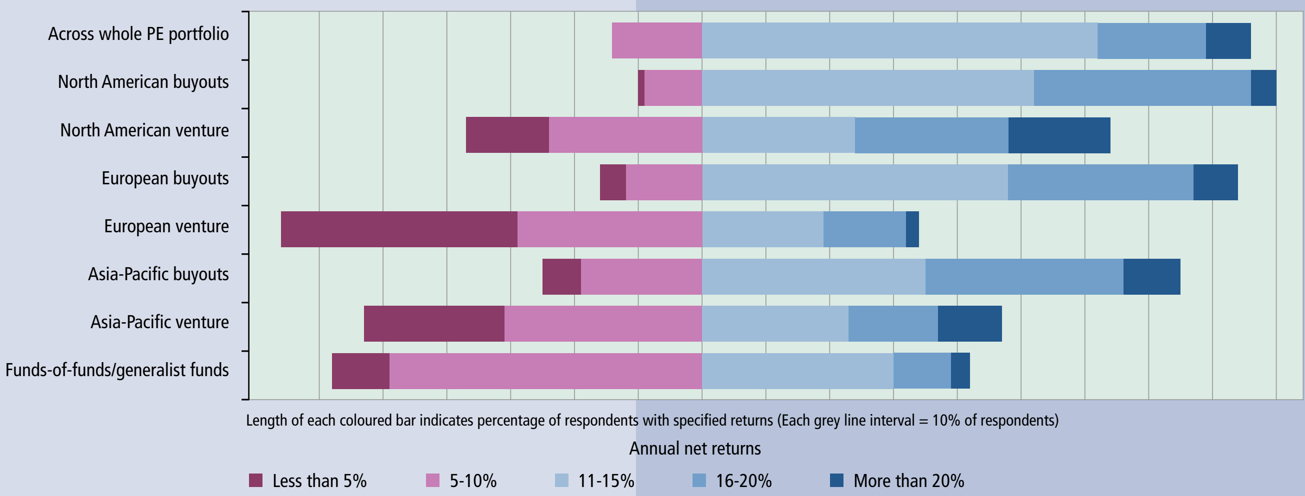
Almost all LPs are forecasting net PE returns of 11%+

Looking across their PE portfolios, 86% of LPs anticipate annual net returns of 11%+ over the next 3-5 years – and a quarter of LPs expect net returns of 16%+.

Buyouts in all regions of the world are regarded as the safest bet – around four in five LPs expect net PE returns of 11%+.

LPs' views of venture are more mixed – two thirds expect North American venture to deliver 11%+ over the next 3-5 years (and 40% expect returns of 16%+). This compares with half of LPs expecting 11%+ returns for Asia-Pacific venture, and one third of LPs for European venture.

LPs' annual net return expectations from their PE portfolios over the next 3-5 years



(Figure 3)

The 'typical' LP expects a 5% risk premium from PE over public equities

The 'typical' (median) PE investor expects a 5% risk premium from private equity relative to public/quoted equities. Institutional expectations vary by investor type – more than a third of asset managers expect a risk premium of 6% or more from private equity over public equity. This compares with one quarter of insurance companies and 15% of pension funds.

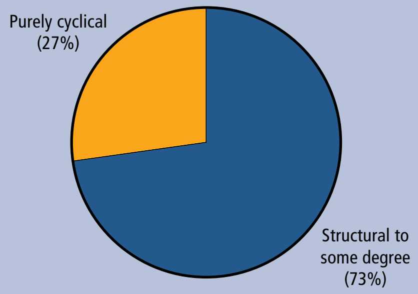
Risk premium expected from PE over public/quoted equities – by LP type

(Figure 4)

Lower PE returns since the GFC are a structural issue

Three quarters (73%) of LPs believe the reduction in PE returns since the onset of the global financial crisis is partly structural, rather than a purely cyclical phenomenon.

Factors behind the reduction in PE returns since the financial crisis

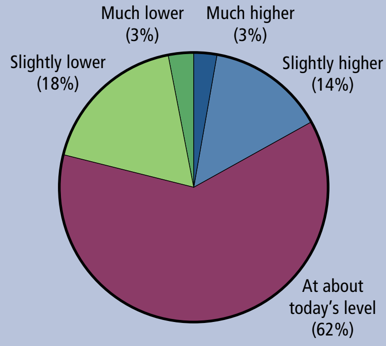


(Figure 5)

Hurdle rates should remain at around today's level, LPs think

Hurdle rates were first agreed during a different economic era. However, two thirds (62%) of LPs believe they remain fit for purpose and that rates should be maintained at around current levels for the next 5-10 years.

The ideal level of hurdle rates over the next 5-10 years compared with current levels – LP views

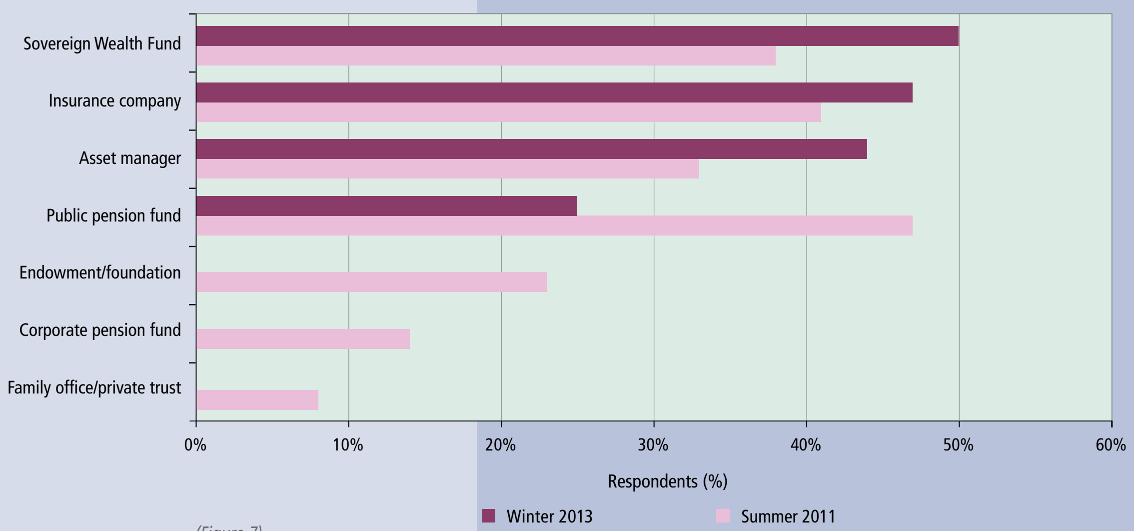


(Figure 6)

Many of the world's largest investors plan to grow their PE teams

Half of sovereign wealth funds, 47% of insurance companies and 44% of asset managers plan to increase the size of their PE teams over the next 12-18 months. One quarter of public pension funds plan to do the same. All endowments/foundations, corporate pension funds and family office/private trusts plan to maintain the size of their PE teams.

LPs planning larger private equity teams over the next 12-18 months

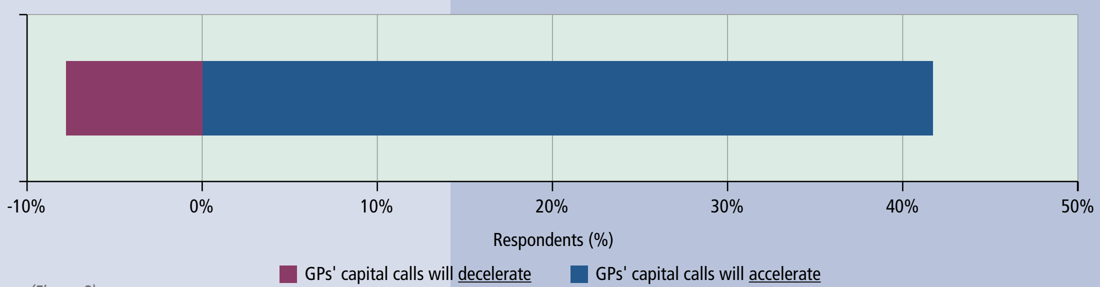


(Figure 7)

LPs expect capital calls and distributions to accelerate

On balance, LPs expect the rate of GPs' capital calls and distributions to accelerate over the next 12-18 months. 42% of LPs expect the rate of GPs' capital calls to accelerate, compared with 8% of LPs who expect the rate to decelerate.

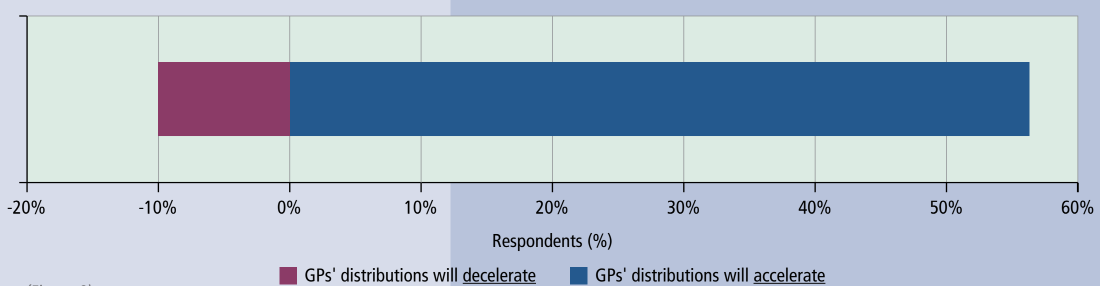
Likely changes to the rate of GPs' *capital calls* over the next 12-18 months – LP views



(Figure 8)

56% of PE investors expect the rate of GP distributions to accelerate over the next 12-18 months, compared with only 10% who expect the rate to decelerate. European LPs are most confident about distributions – two thirds expect the pace to accelerate, compared with just under half of North American LPs.

Likely changes to the rate of GPs' *distributions* over the next 12-18 months – LP views

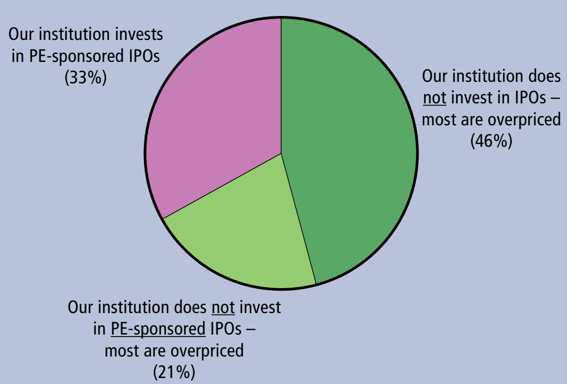


(Figure 9)

Only one third of LPs invest in PE-sponsored IPOs

Two thirds of LP institutions avoid investing in PE-sponsored IPOs. 21% of investors believe GP-sponsored IPOs are too aggressively priced, and a further 46% of investors believe *all* IPOs are overpriced. This feeling is strongest in North America, where three quarters of LPs avoid IPOs.

LPs' policies towards PE-sponsored IPOs



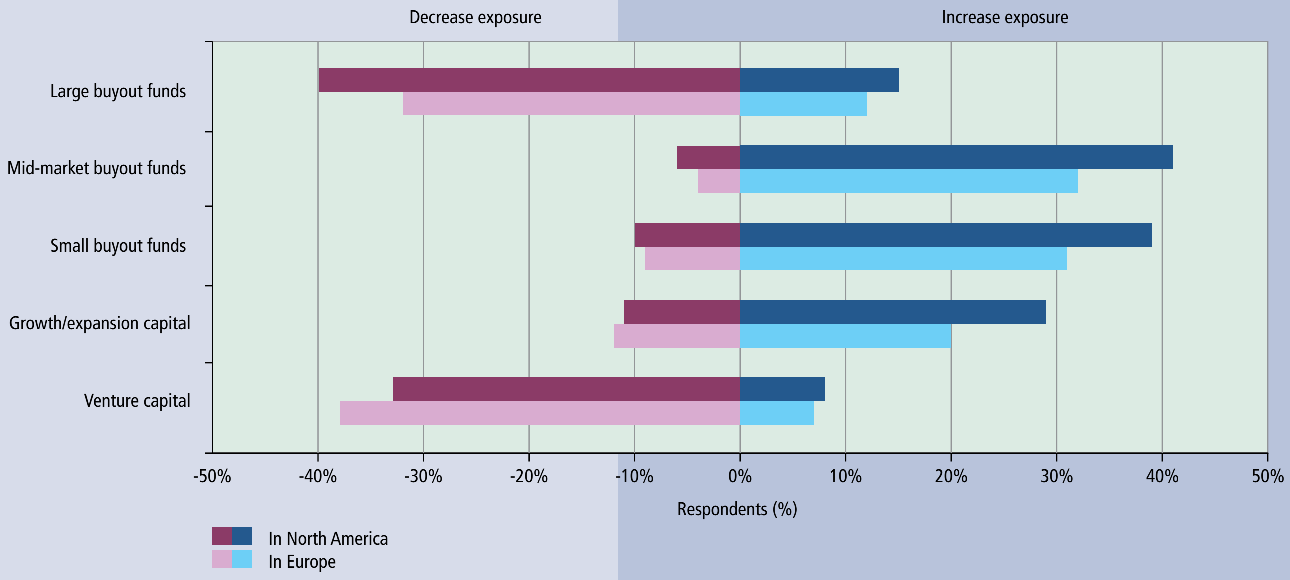
(Figure10)

LPs still increasing investment in small and mid-sized buyouts in Europe/North America

Investor sentiment by investment stage has changed little in the last couple of years. LPs believe small and mid-market buyout transactions in Europe and North America will offer the best PE opportunities in the next 2-3 years – 30-40% of LPs plan to increase their exposure to this kind of PE.

Investors are continuing to scale back their exposure to venture capital and large buyouts investments – areas they see as more risky in today's climate. 30-40% of LPs plan to reduce their new commitments to these areas over the next 2-3 years.

LPs' plans for European and North American fund commitments in the next 2-3 years – by fund type

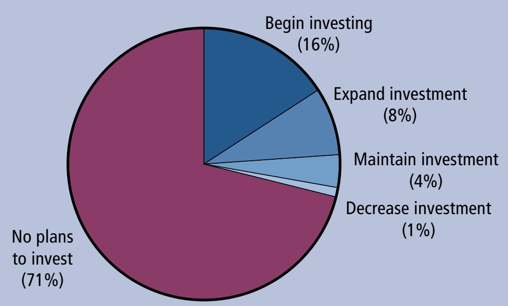


(Figure 11)

A quarter of global LPs plan increased exposure to African PE

One quarter (24%) of global investors expect to begin investing, or expand their investment, in African private equity over the next 2-3 years.

LPs' plans for African PE exposure in the next 2-3 years

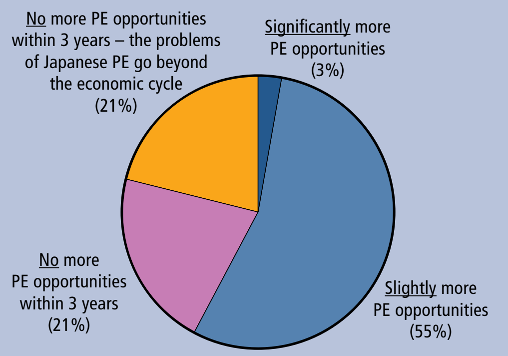


(Figure 12)

LPs expect a slight improvement in Japanese PE

Although a majority (58%) of investors believe recent economic improvements in Japan will create more PE opportunities in the country, most LPs believe the effect will be slight.

The expected impact of Japan's recent economic improvements on Japanese PE

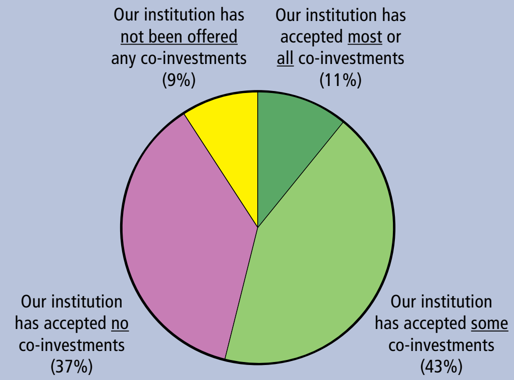


(Figure 13)

Over half of LPs have co-invested with GPs in the last two years

Just over half of LPs (54%) have co-invested with their GPs in the last two years. Only one in ten LPs had not been offered any co-investment opportunities in this period.

Proportion of GP-offered co-investments accepted by LPs in the last 1-2 years



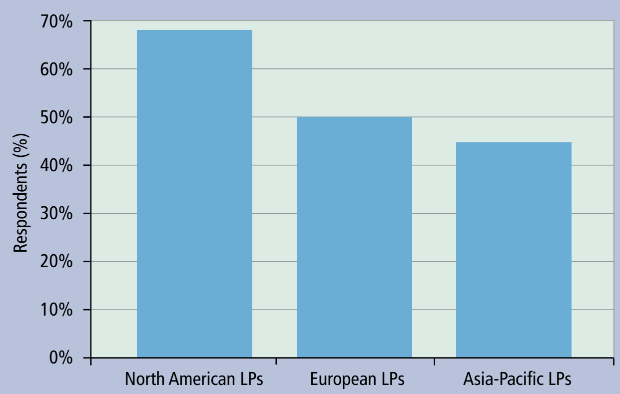
(Figure 14)

Typical LP now has a tenth of PE commitments in directs

The 'typical' (median) LP currently invests 10% of its total PE commitments directly into private companies (on a stand-alone basis and/or via co-investment with GPs). Within the next 3-5 years, this proportion is expected to increase to 15%.

Two thirds of North American LPs and half of European LPs say they would like to be offered more co-investments.

Proportion of investors desiring an increased number of co-investments – by location of LP

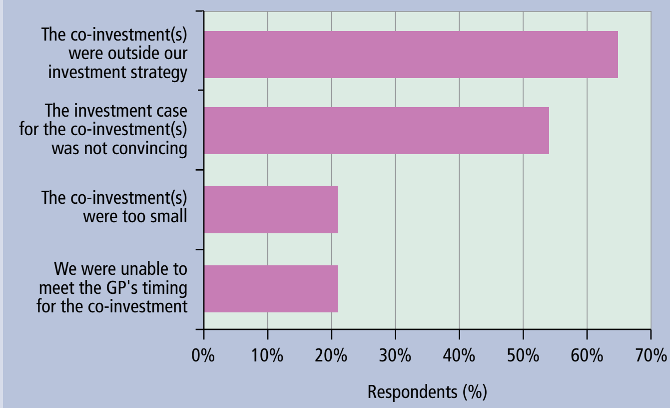


(Figure 15)

Investment fit and investment case prompt most co-investment refusals

Two thirds of LPs declined one or more co-investment opportunities because they fell outside their investment strategy (eg, by deal size, geography, sector) in the last two years. 54% of LPs refused a co-investment because they considered the investment case made by the GP to be unconvincing.

LPs' reasons for declining co-investment opportunities in the past 1-2 years



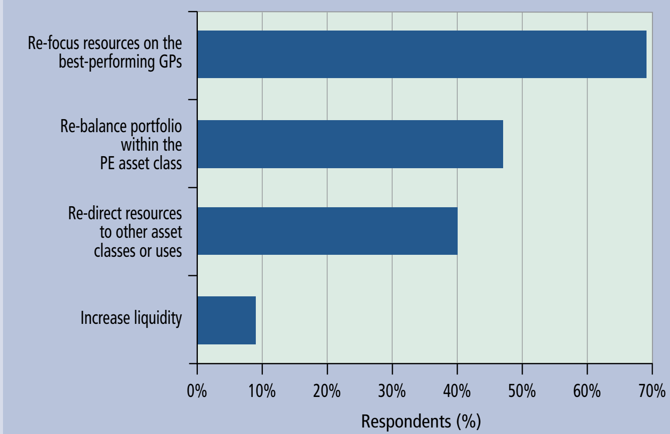
(Figure 16)

LPs continue to change overall composition of their portfolios

42% of LPs plan to sell assets in the secondaries market in the next two years. Investors continue to see the secondaries market as an important tool for changing the overall composition of their portfolios.

There are some striking regional differences among secondaries sellers. Almost all North American would-be sellers (96%) plan to re-focus resources on their best-performing GPs, compared with just one quarter (27%) of European LPs. Half of North American LPs plan to sell in the secondaries market as a way to rebalance their portfolios – either within PE, or between PE and other asset classes. Around one third of European LPs plan to sell for these reasons.

Reasons for selling in the secondaries market in the next 2 years – LP views

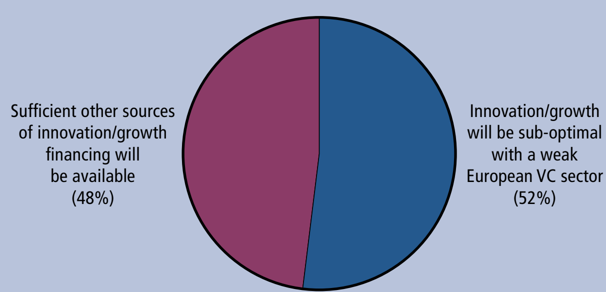


(Figure 17)

Half of LPs think Europe's weak VC sector will impact growth

Half (52%) of global LPs think the weakness of European venture capital is a significant problem that will impact the growth of the European economy.

The impact of a weak European venture capital industry on the region's economy – LP views

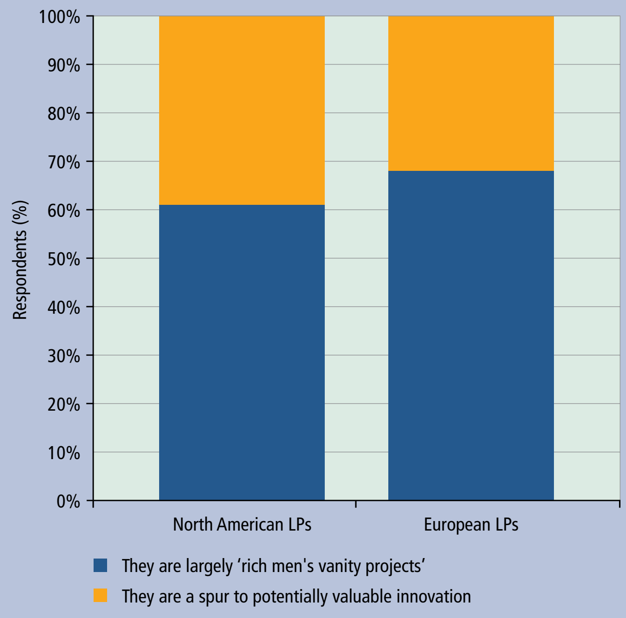


(Figure 18)

Billionaires' futuristic tech-based ventures are 'rich men's vanity projects', say LPs

The majority of North American and European LPs believe the financing of futuristic technology ventures (such as asteroid mining and the LA-San Francisco Hyperloop) by billionaires are largely 'rich men's vanity projects'.

LPs' views of billionaires funding futuristic tech-based projects

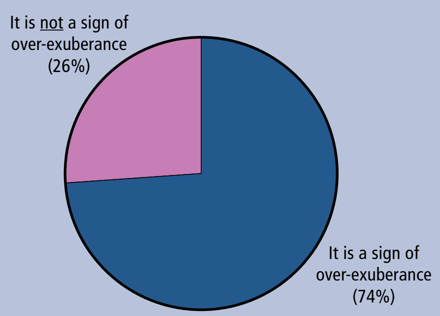


(Figure 19)

PIK debt issuance is a sign of a frothy credit market, LPs think

Three quarters (74%) of LPs think the current level of payment-in-kind (PIK) debt issuance is a sign of over-exuberance in the credit markets.

LPs' views on the current level of payment-in-kind (PIK) debt issuance in the credit markets

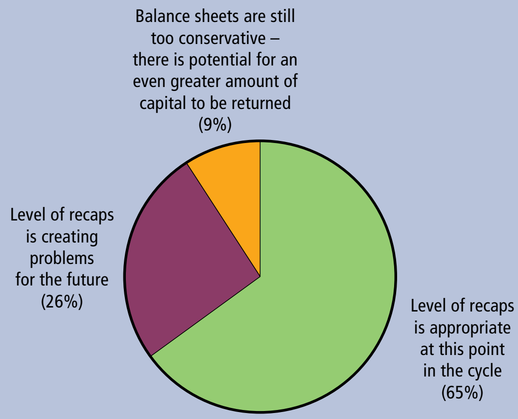


(Figure 20)

Most LPs are comfortable with the current level of dividend recaps

Two thirds of LPs think today's level of dividend recaps is appropriate at this point in the PE cycle.

LPs' views on today's volume of dividend recaps



(Figure 21)

Coller Capital's *Global Private Equity Barometer*

Respondent breakdown – Winter 2013-14

The *Barometer* researched the plans and opinions of 113 investors in private equity funds. These investors, based in North America, Europe and Asia-Pacific (including Middle East), form a representative sample of the LP population worldwide.

About Coller Capital

Coller Capital, the creator of the *Barometer*, is the leading global investor in private equity secondaries – the purchase of original investors' stakes in private equity funds and portfolios of direct investments in companies.

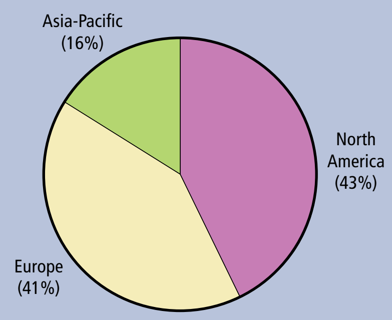
Research methodology

Fieldwork for the *Barometer* was undertaken for Coller Capital in September-October 2013 by Arbor Square Associates, a specialist alternative assets research team with over 50 years' collective experience in the PE arena.

Notes:

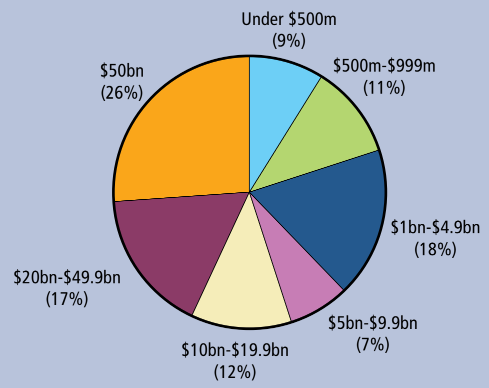
- Limited Partners (or LPs) are investors in private equity funds
- General Partners (or GPs) are private equity fund managers
- In this *Barometer* report, the term private equity (PE) is a generic term covering venture capital, buyout and mezzanine investments

Respondents by region



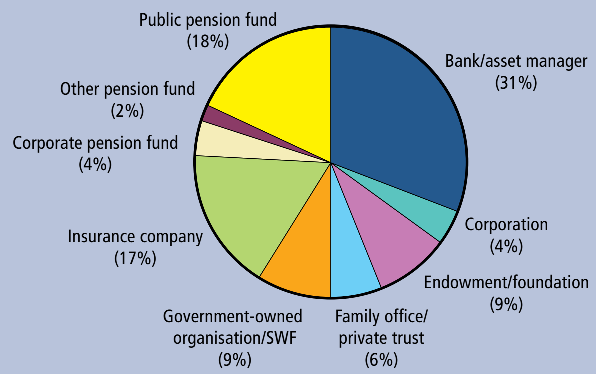
(Figure 22)

Respondents by total assets under management



(Figure 23)

Respondents by type of organisation



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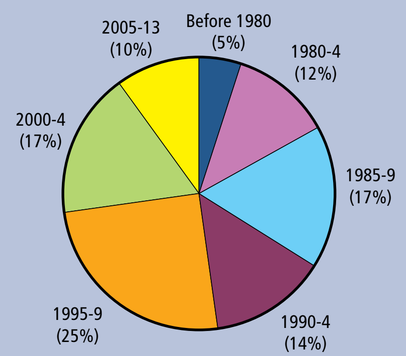
Respondents by year in which they started to invest in private equity



(Figure 25)

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