

Limited Partners in a New Era

The Good, the Bad, the Ugly

A poll of how LPs have reacted to the events of the financial crisis and in its aftermath



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What we do and our experience in the field of LP/GP communications

ABOUT IE CONSULTING

What does IE Consulting actually do?

“IE Consulting is a private equity research and advisory team
dedicated to helping you
see with clarity, act with
confidence and communicate with
conviction”

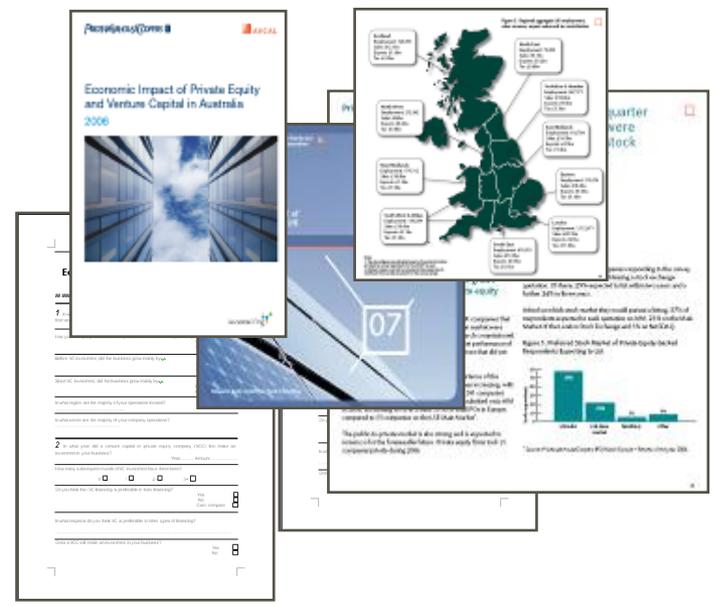
A large proportion of our work involves market research surveys and analysis conducted in the realm of LP/GP communications



promotional and lobbying work to support the industry



high value and arresting content for market communications



"An innovative, valuable and professional research business."

"I would have no hesitation using the service again."

"We are thrilled with the results and will definitely use [them] for further research projects going forward."

"Creative"

"I would go to [IE Consulting] again for any high level analysis or consulting work."

"delivered rapidly on promises."

"Good value"

"[IE Consulting] strives to provide solutions to our business challenges by continuously enhancing and tailoring its services to suit our needs."

"...good understanding of our objectives."

"...years of experience consulting the private equity industry"

"...went beyond the call of duty to deliver great service"

**"...professional and personable and adds a lot of value to projects...
...produces work to a high standard"**

"High integrity"

"... understood our business requirements instantly and delivered the necessary results on time."

"...works in partnership with us."

"...very reliable and efficient...I can focus on strategic initiatives rather than having to worry about schedule and quality."

"Expert"

"We plan to use [IE Consulting] for projects such as this for all our top-end events going forward."

"...always strives to support our business decisions."

"Personable"

"[IE Consulting] has a solid database of industry data"

"[IE Consulting's] ability to present insights logically and quantitatively is very useful."

"We continue to use [them] for all of our research needs and hope to continue working with them long into the future."

"...professional and reliable from start to finish and really made the process as seamless as possible."

"...expert on research tools and techniques."

"On time"

"...bright, incisive and analytical to the point of it being quite depressing... for others."

"...expertise in its field meant we got maximum results from this project"

"Great results"

"...delivered a number of projects for me, using good practical ideas."

"...completely understood our objectives"

"...listened, understood our needs and subsequently responded in a superb way."

"We have worked with [IE Consulting] on a number of occasions and I would be highly likely to work with [them] again in the future"

"...a pleasure to work with"

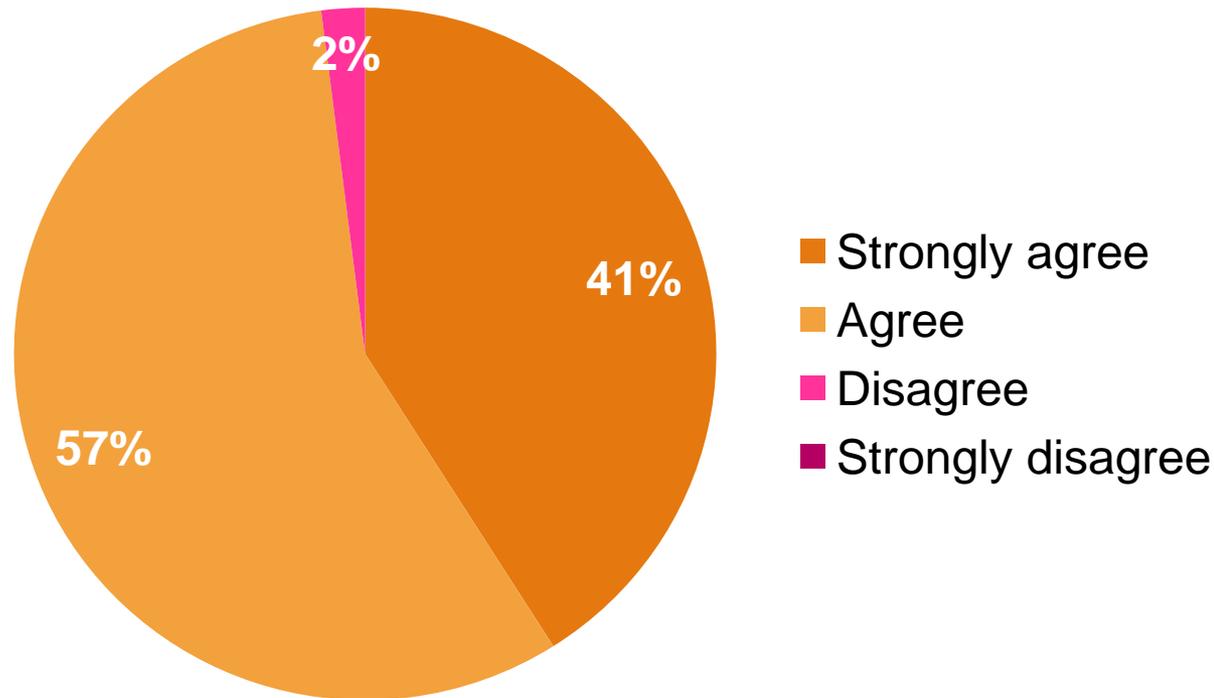
"..always conducted quickly and efficiently."

How the landscape has changed since the financial crisis

FUNDRAISING ENVIRONMENT

Institutional investors in private equity are predicting a tough road ahead for GPs looking to raise new funds in the next two years.

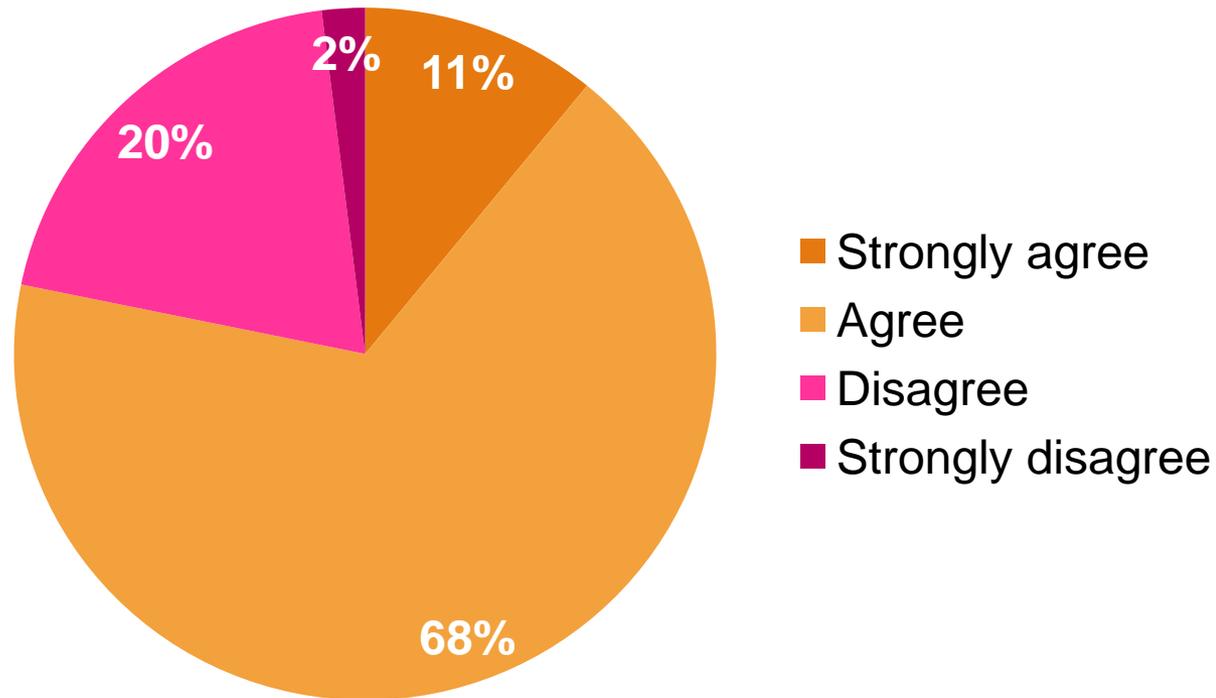
More GPs than ever will struggle to raise a new fund over the next 2 years.



The very best funds will still be able to raise money from institutional investors, but alone the amount of due diligence performed by LPs will mean that fundraising will take much longer.

The Limited Partners we contacted believe that the balance of power has shifted in their favour.

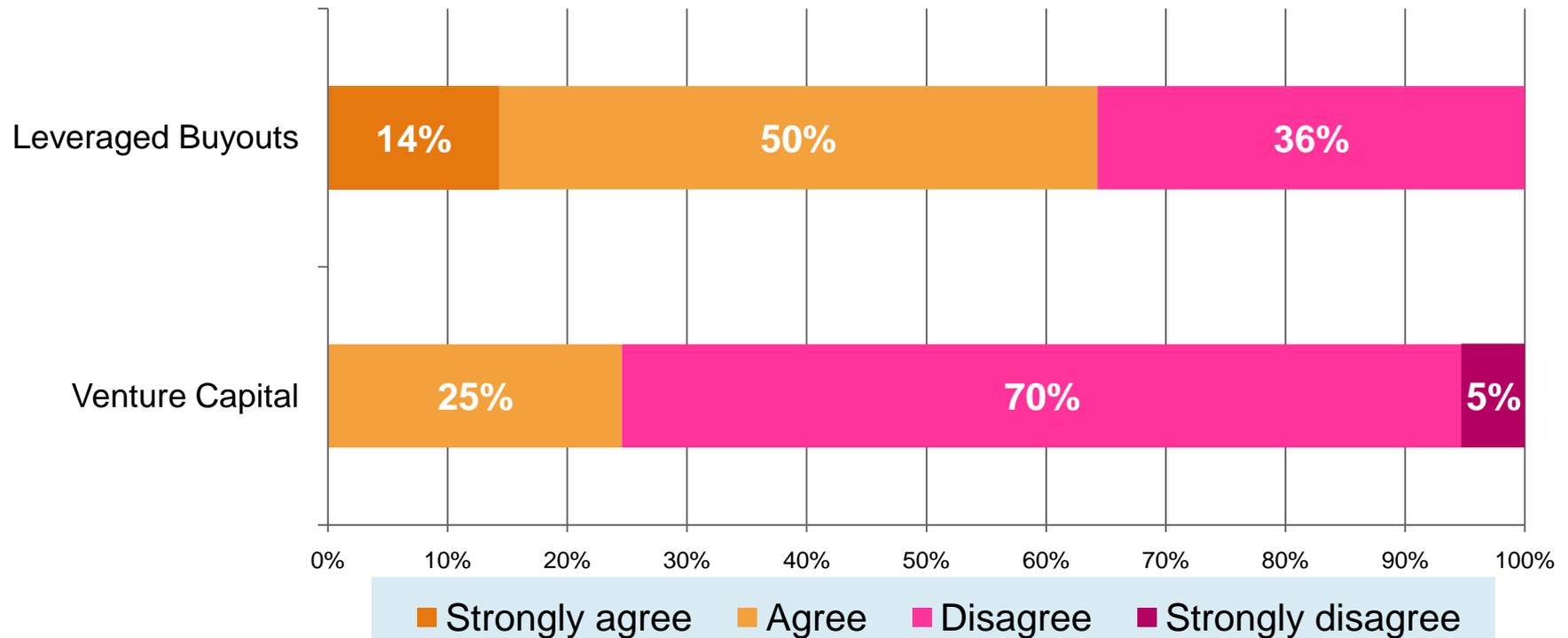
The balance of power between LPs and GPs has shifted in favour of LPs.



Fundraisers in 2010 and 2011 must prepare themselves for significant pushback from LPs on financial and non-financial terms and conditions in their funds.

Close to two-thirds of respondents had less confidence in the leveraged buyout model in the aftermath of the crisis.

My level of confidence in the following has decreased since the crisis:



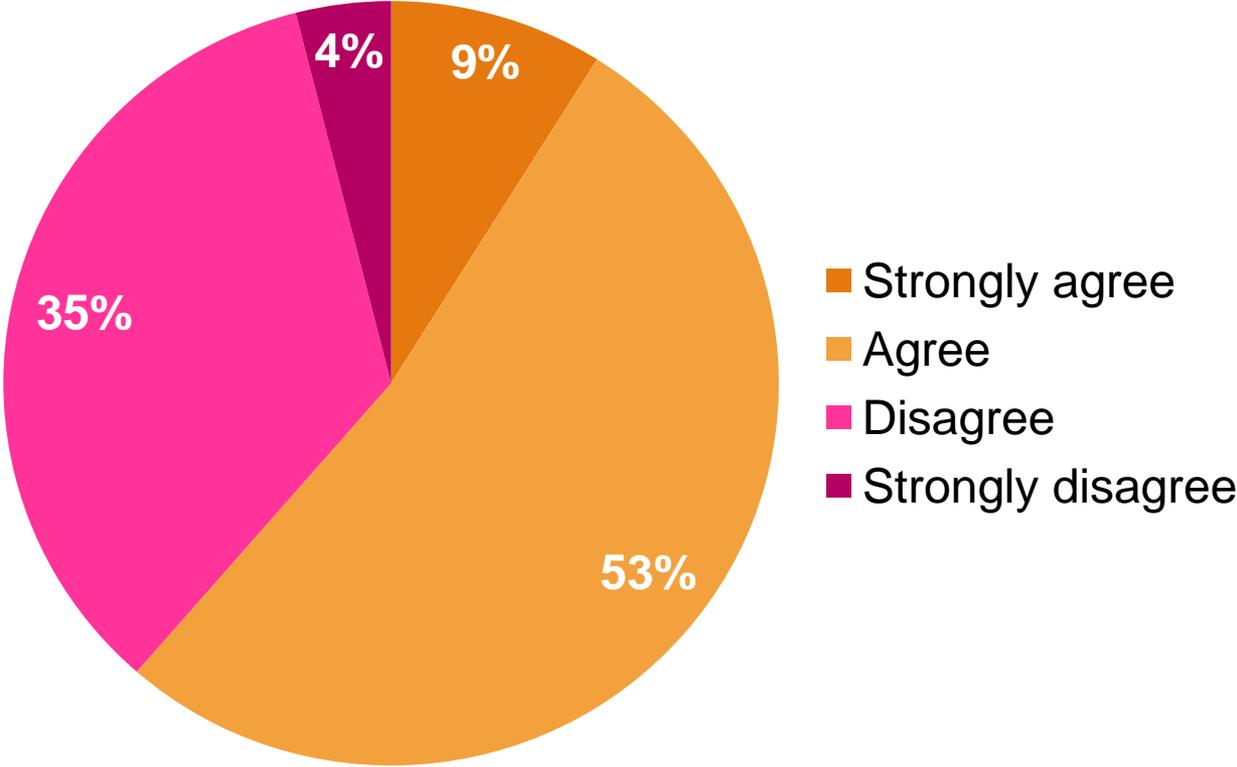
Those that had not experienced a similar mental shift with regards to venture capital investments might, of course, simply have a low level of confidence in VC to start with.

How General Partners communicate with their investors

LP/GP COMMUNICATIONS

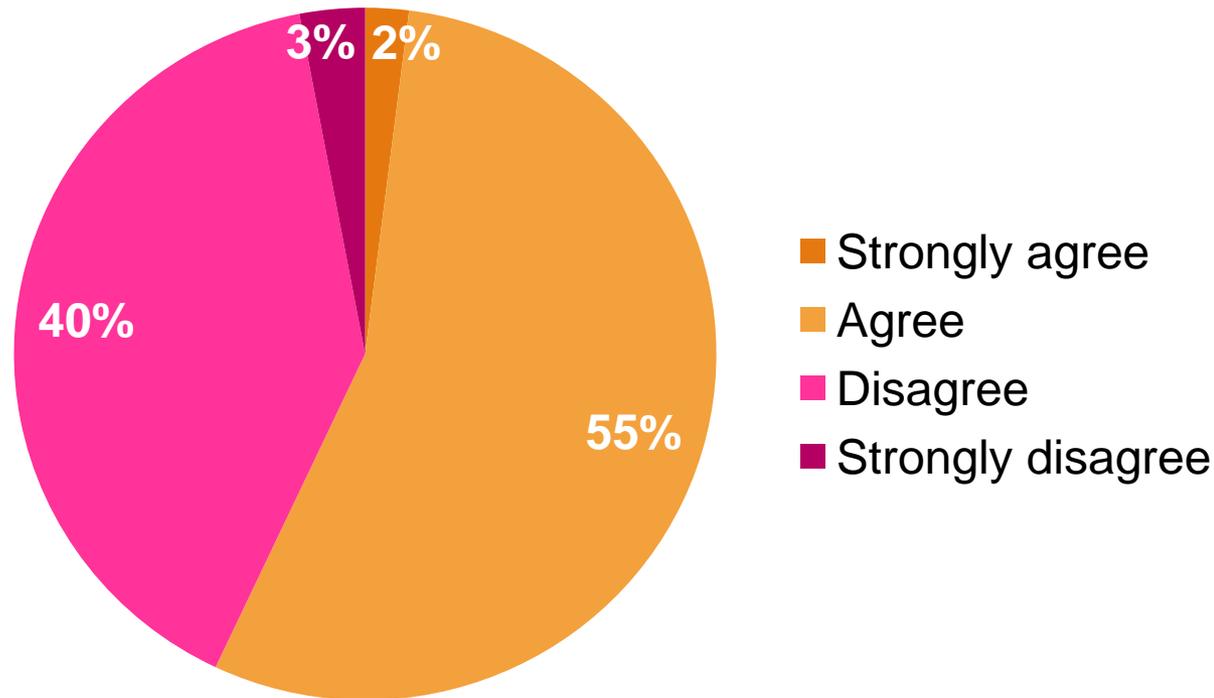
Poor communications and GP opacity is now a genuine reason for LPs to pass on commitments to a new generation fund.

I will (or have already) decline(d) to invest in new fund vehicles launched by certain managers I have previously invested with **as a direct result of poor communications or a lack of transparency during the crisis.**



Many General Partners need to do more to match the communications expectations of their investors.

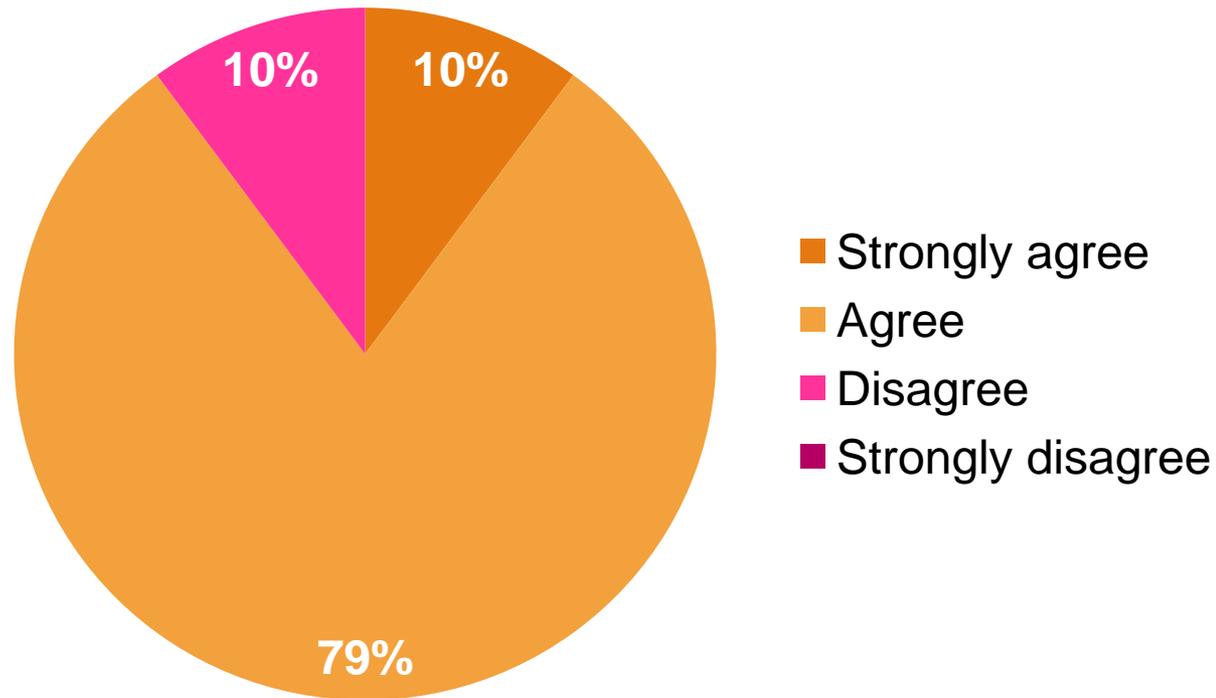
All of the fund managers I invest with understand the importance of transparency and good communication with their investors.



Communication expectations from LPs now go well beyond semi-annual reporting and an annual investor meeting. And they want to feel that GPs are taking this seriously.

When prompted, General Partners tend not to have an issue with providing detailed data on their investment and operations.

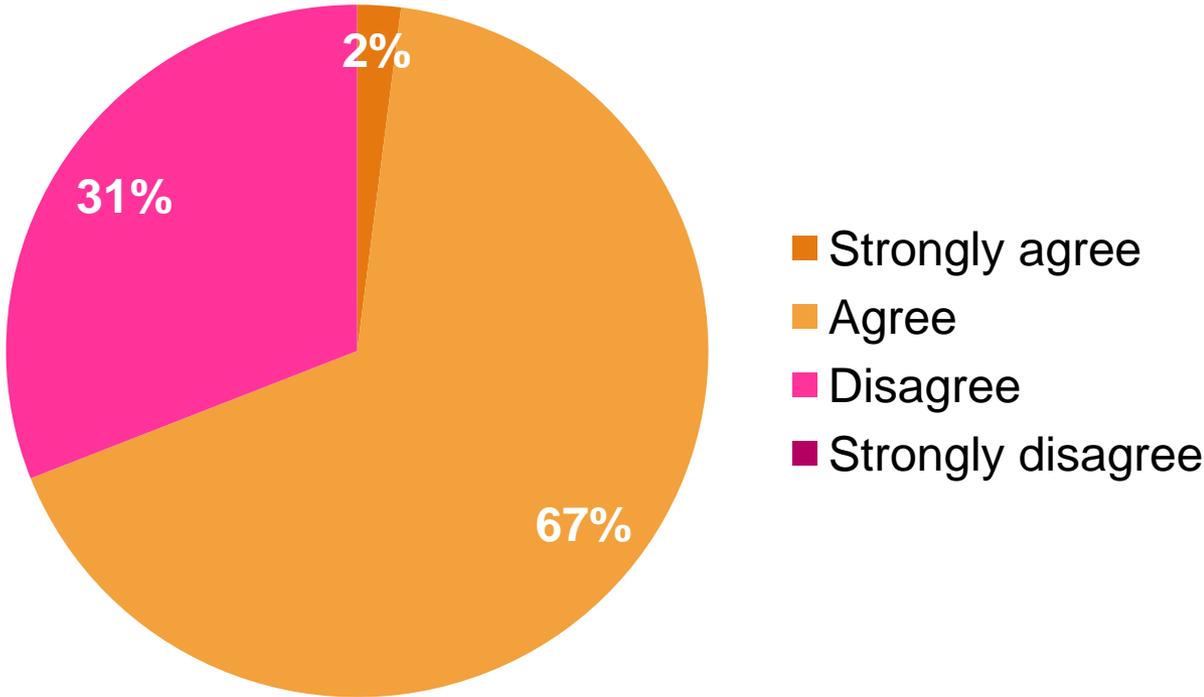
Most of the VC/PE funds I am invested in have been happy to provide any additional information I have requested.



Although GPs are comfortable with increased LP information requirements, will this continue to be the case if and when performance improves and fundraising becomes easier again?

Almost one in three Limited Partners is dissatisfied with the way they have been informed about underperforming investments.

I am happy with the way the venture capital / private equity funds I am invested in have communicated problems with portfolio companies.



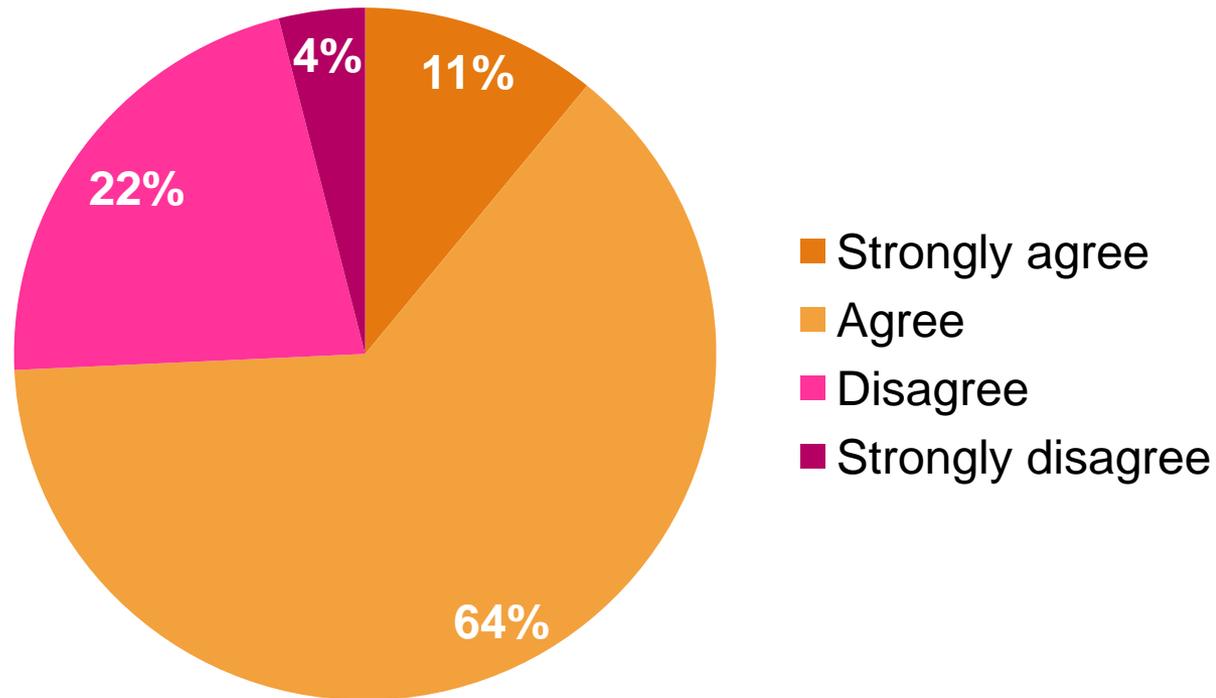
With LP scrutiny at a such a high level, private equity fund managers must promptly provide realistic valuations, as well as any other relevant information on their investments.

How we conducted the research

WHAT LPs LEARNED FROM THE CRISIS – THE GOOD

Although returns from 2006/7 deals are unlikely to please many LPs, the current environment looks brighter.

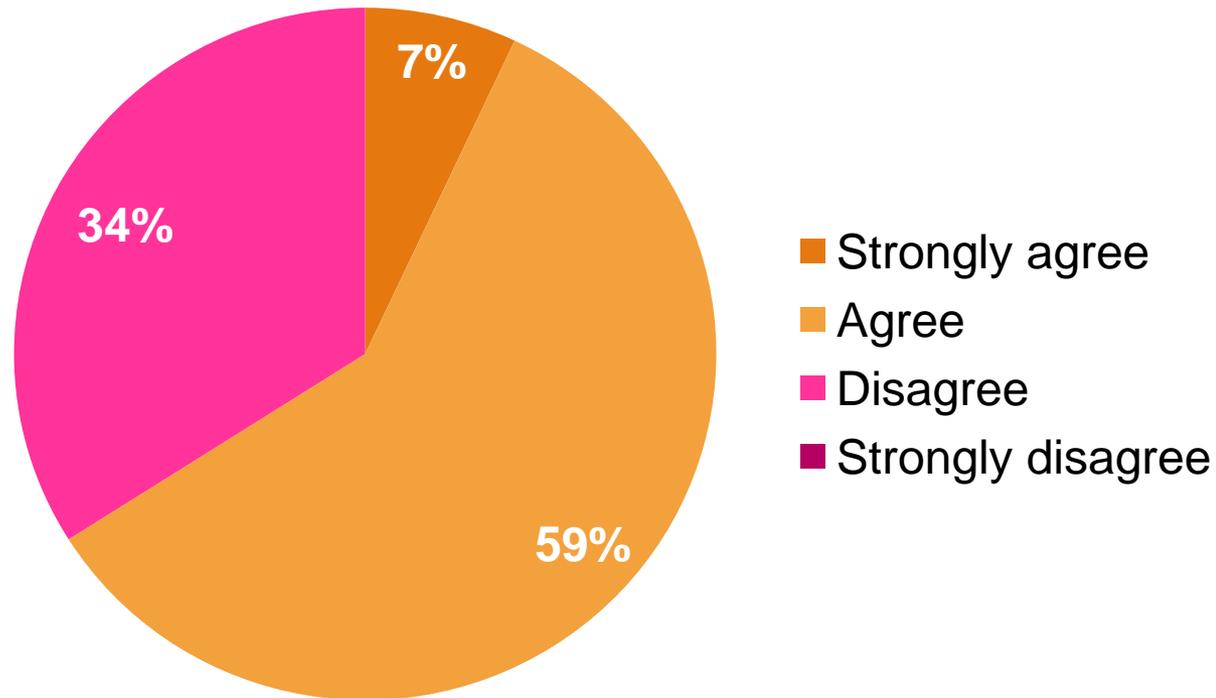
Deals done in the next 12-18 months will provide premium returns.



The question many Limited Partners are asking now, is: "If current deals are at such a premium, why isn't anyone closing anything?"

Although one-third of LPs disagreed, most were relatively confident that the long-term result of the crisis would be positive.

The fallout from the financial crisis will result in a more robust PE industry.



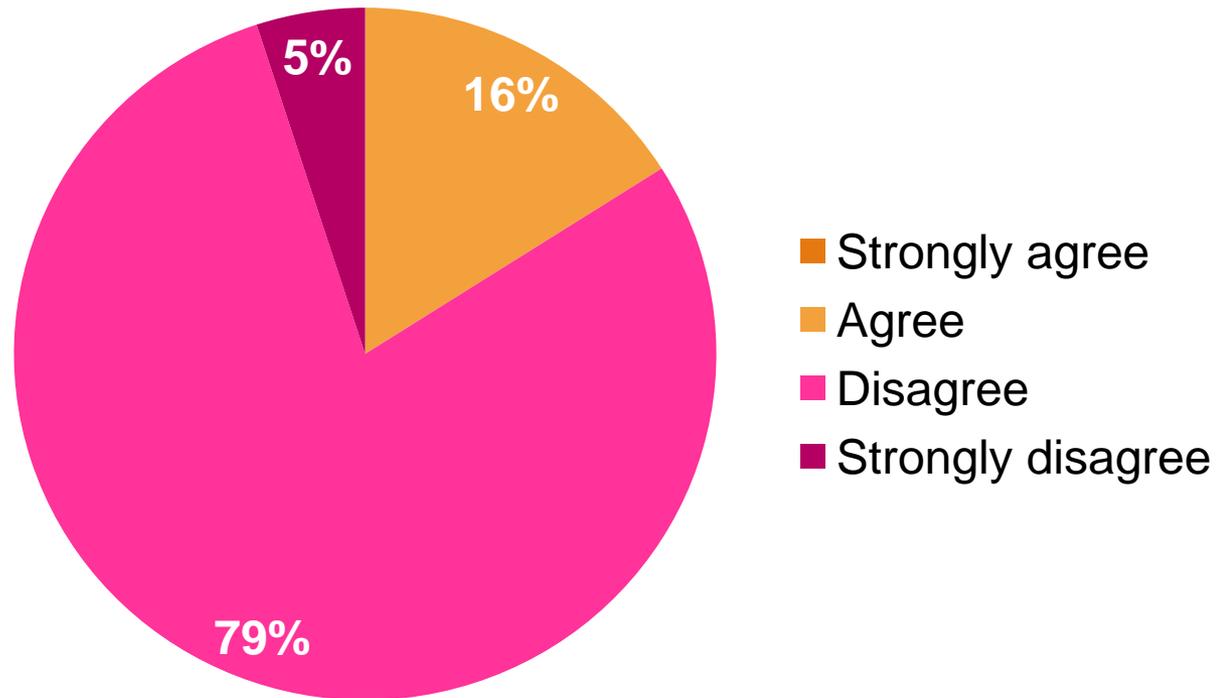
Of course, irrespective of how things turn out for the industry once the dust has settled, many LPs' investment programmes will take years to recover from the damage.

How we conducted the research

WHAT LPs LEARNED FROM THE CRISIS – THE BAD

According to Limited Partners, the financial crisis has been every bit as bad as the press has communicated.

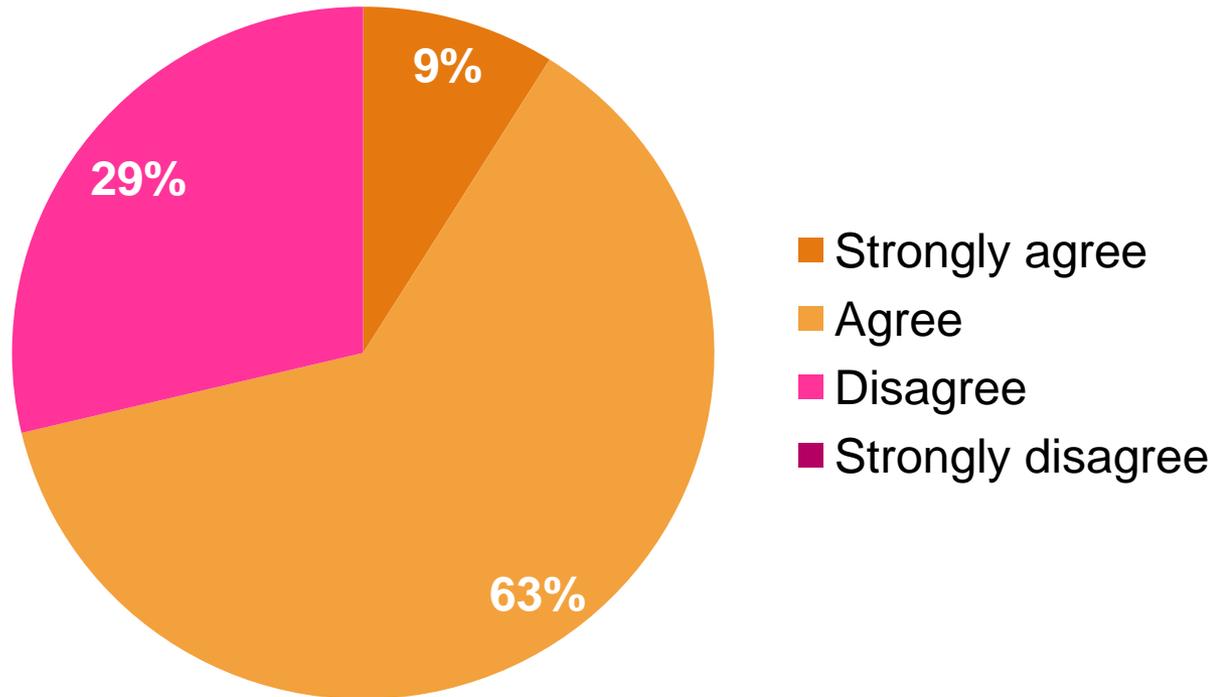
The press exaggerated the significance of the financial crisis.



Although, only 16% of survey respondents agreed that the press had exaggerated the crisis, this was the case for 25% of pension funds.

Worryingly, the majority of limited partners that responded to the survey did not expect the industry to learn from its mistakes.

It won't be long before the mistakes of the past are forgotten and made again.



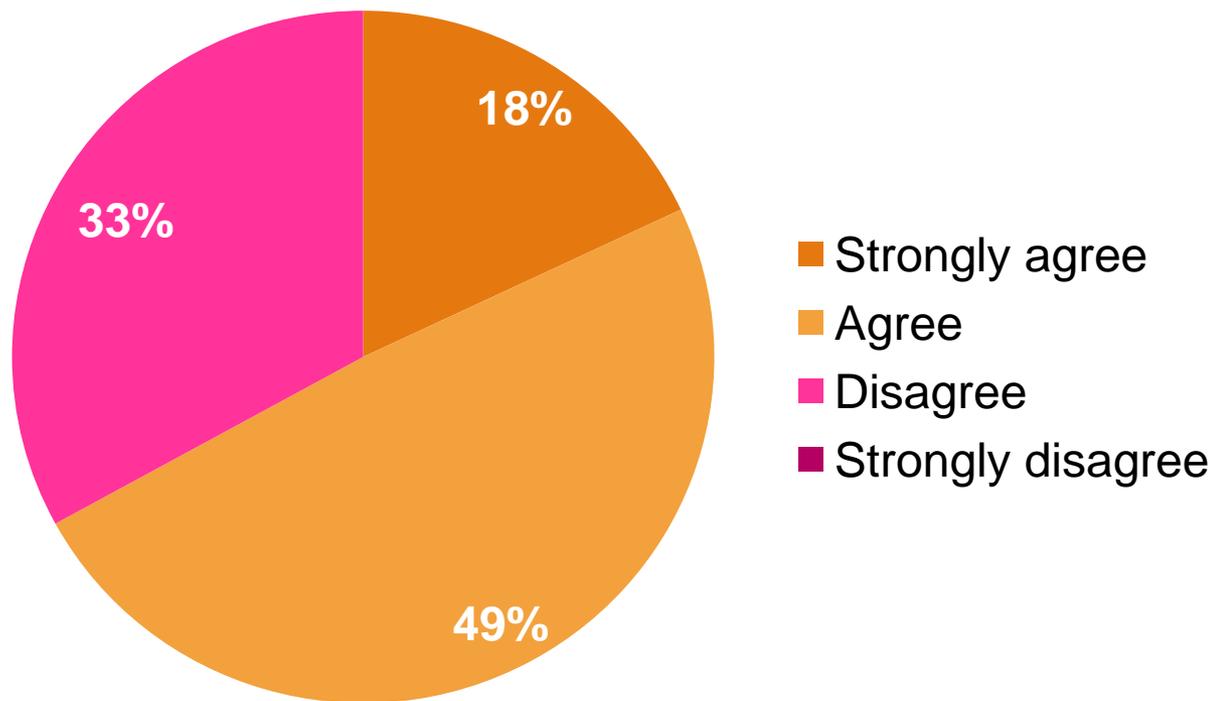
Perhaps unsurprisingly, having been at the centre of the crisis, banks were the least likely (only 50%) of the limited partners to agree that the mistakes of the past would be repeated.

How we conducted the research

WHAT LPs LEARNED FROM THE CRISIS – THE UGLY

Two-thirds of limited partners had found the crisis to have shown certain fund managers to be acting at odds to the LP's interests.

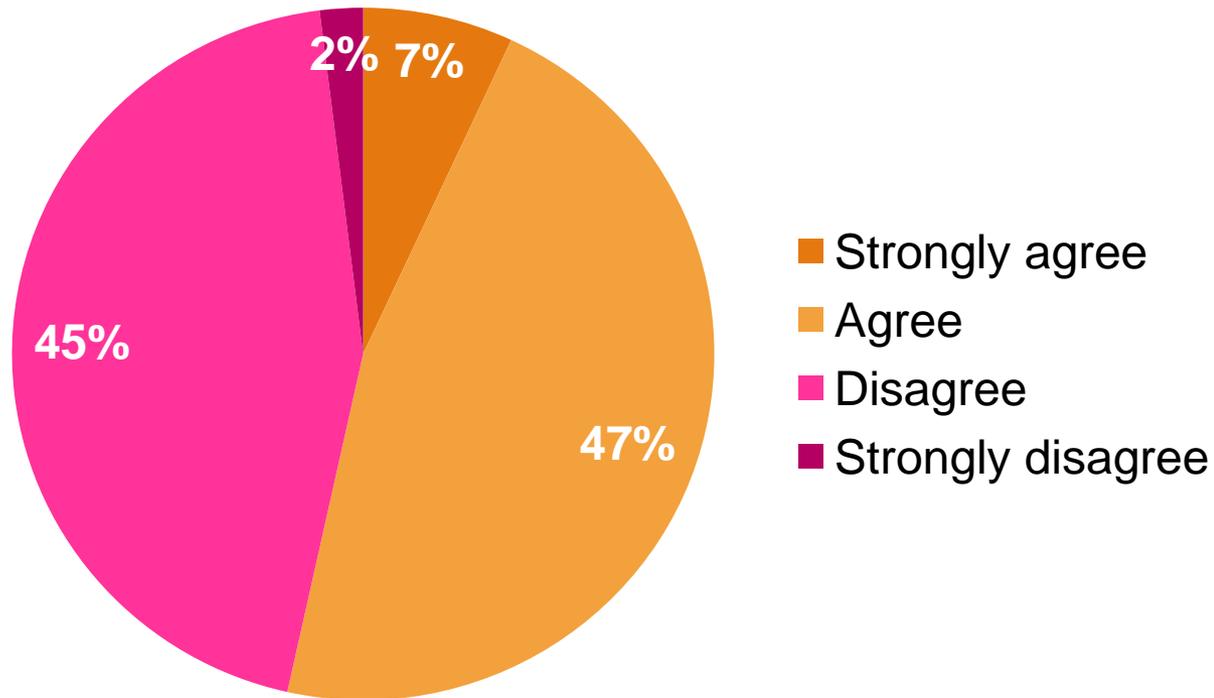
Misalignments of interests with the funds I have been invested in have become more apparent during the crisis.



When returns are good, it is natural for LPs to be less concerned with the activities of their LPs, *hoping* that GPs are acting in the LP's best interests.

More than half of the respondents to the survey felt that some of their GPs had blamed their own mistakes on the economic crisis.

Some VC/PE funds I am invested in have used the financial crisis as an excuse for poor investment decisions.



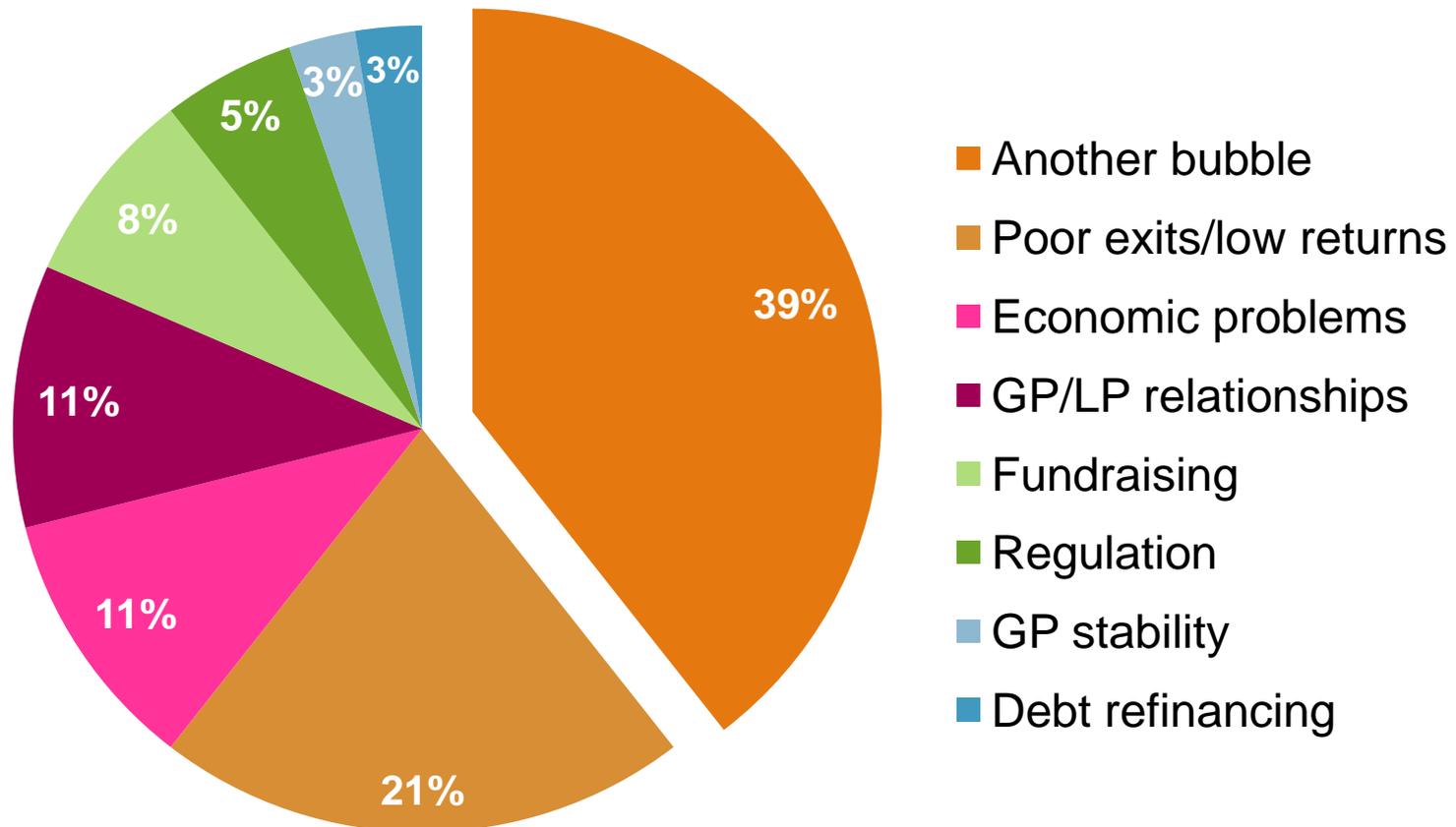
Limited partners will quickly lose respect for investment managers that are not willing to own up to the mistakes they have made.

What Limited Partners are worried about

GREATEST CONCERNS

Limited partners were most concerned that the weight of capital chasing opportunities might lead to another bubble

As an investor in PE/VC funds, what is your single greatest concern for the next 2 years?



The next slides contain some examples of the verbatim comments given by respondents

Concerns that another bubble may be on its way

Enormous size of outstanding commitments/invested capital in PE/VC

That fundraising quickly returns to pre-crisis levels

How the excess liquidity accumulated in the system will affect the PE/VC industry

Too much capital being raised for the PE mid-market

New "bubbles" like investments in energy or emerging markets

2007-2008 vintages return

Funds paying excessive prices due to overhang of dry capital

Level of dry-powder in the developed market

That we get the same old "Happy days are here again"

greed takes over and we get right back into a bubble

Money (both equity and debt) flooding back into the space and overfunding/driving up prices of illiquid assets again . . .

Concerns with regards to exits and returns were the second-most popular cited by survey respondents

Concerns that exits will be weak and/or returns insufficient

Exit delay

It is difficult for the funds to realize exits and return some money to their investors

Purchase prices have not declined as much as anticipated given the declines in economic activity and the dearth of leverage. Purchase prices appear to be full relative to growth prospects.

Exit environment

We are focused on venture [and] my greatest concerns are liquidity events and aggregate fundraising: We need to see the nascent exit market maintain momentum and grow.

Returns that don't keep up with and exceed the public markets

Real returns with low risk

We are not investors in new funds, so wish to maximise exits over the next two years

Numerous institutional investors into private equity remain concerned about the economic environment

Problems with the economic environment

A follow-on crisis as a result of events in Europe.

The economy will take longer to gain sustainable strength

A “double-dip” scenario

Sovereign defaults and resulting currency crises

Financial system confidence

The relationships between Limited Partners and GPs

Relationship between GP and LP

Misalignment of interests between GPs and LPs is not corrected significantly and that bad funds with bad terms still get funded

Transparency and speed of information

Although some LPs were concerned that *too much* cash had been raised for investment, others took a contrarian view

Problems with raising funds for investment

Capital overhang in certain types of funds, i.e. secondaries, dry up of others, i.e. venture; even good GPs struggle to raise funds.

Lack of capital to invest.

Due to the inability of certain sponsors to raise new funds: 1. talent will leave and the "left behinds" will be the less skilled
2. "the walking dead" funds: the GP will fire the staff and then slow exits to maximize personal gain from management fees.

The effects of regulation on the industry

Biggest concern is over-reaching new regulation unintentionally strangling the PE industry.

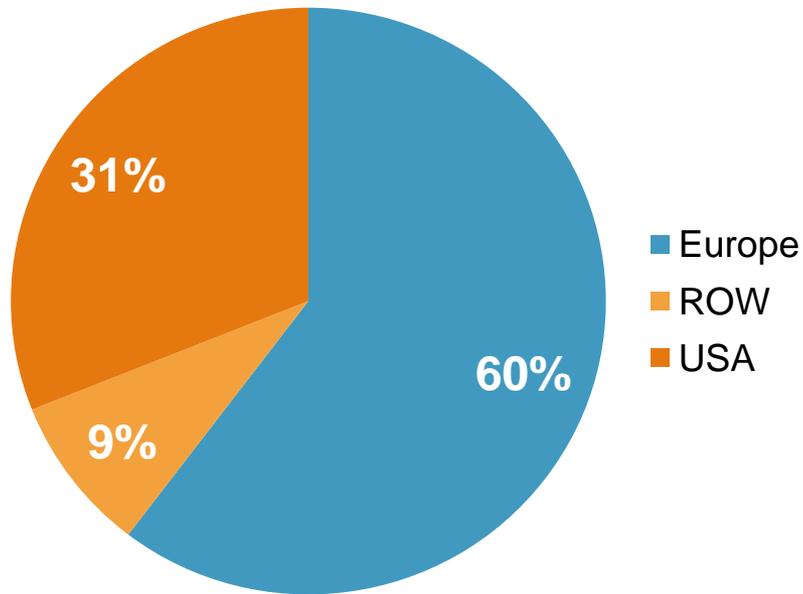
Increased regulation

How we conducted the research

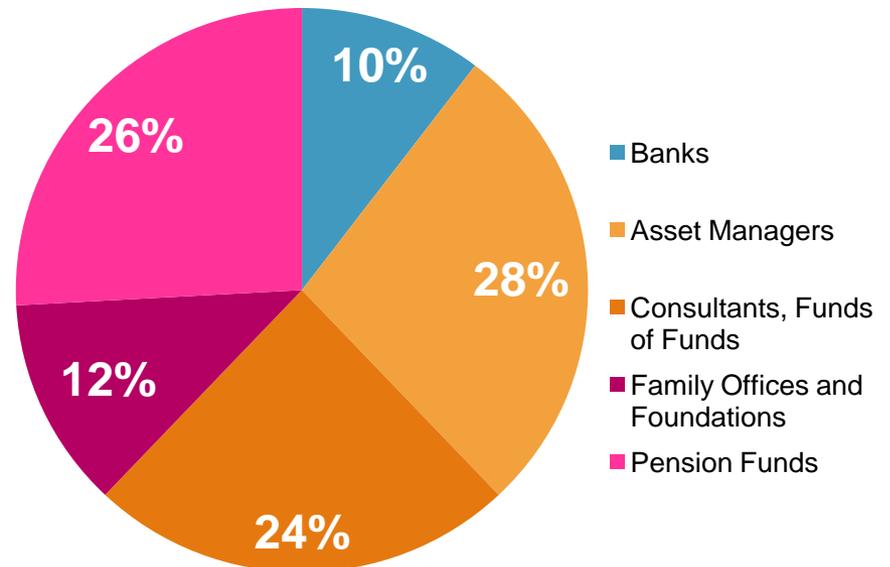
METHODOLOGY

We asked LPs from across the globe how they had coped during the difficult financial environment of the past few years.

Geographical distribution of respondents to the survey



Institutional category of study participants



The 58 respondents to the survey included the largest institutional investors into private equity in both Europe and the US. The survey was undertaken 23rd-30th April, 2010.

We would love

CONTACT DETAILS

We welcome feedback, suggestions, collaboration...

matthew.craig-greene@ieconsulting.co.uk



Tel: +44 (0)20 7004 7461

Mob: +44 (0)7917 178 321

Haymarket House
28-29 Haymarket
London
SW1Y 4RX

engage-iec.com

