



# SAN MATEO COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

## Private Equity Review

December 15, 2015

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# SAN MATEO COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

As of June 30, 2015

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## MARKET COMMENTARY

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As of June 30, 2015

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### Debt-Related:

- **New issuance slowing down.** First half 2015 high yield issuance of \$185 billion is down 1% from the same period last year and leveraged loan volume of \$229.0 billion<sup>1</sup> is down 29.4% versus the same period last year.
- **Spreads have increased.** BB-, B+ and B index widened by 33 bps, 22 bps and 61 bps respectively, a 9.6%<sup>1</sup>, 5.8%<sup>1</sup> and 14.8%<sup>1</sup> increase versus same period last year while HY Credit Index widened by 71 bps or 24.2%<sup>1</sup> versus last year.
- **Despite weakness, LBO debt terms have loosened further.** Total leverage for the first half of 2015 at 5.6x<sup>2</sup> EBITDA is up 15.09% from the first half of 2014. Similarly, Interest coverage (EBITDA / Cash Interest) for the first half of 2015 at 2.55x<sup>2</sup> is down 24.8% from the first half of 2014.

### Buyouts & PE:

- **Capital overhang continues to persist.** PE dry powder at \$835 billion<sup>3</sup>, up 9.7% from same period last year. Total buyout dry power at \$475 billion<sup>3</sup>, up 7.9% from prior year.
  - **Fundraising is weakening.** During the first half of 2015, PE firms raised \$198.3 billion<sup>4</sup>, down 10.7% from prior year. Buyout firms across all buyout strategies raised \$45.5 billion<sup>4</sup>, down 47.91% from prior year.
  - **Investment activity is also slowing down.** PE firms invested \$216 billion<sup>5</sup>, down 21.7% from prior year and closed 1,509 deals<sup>5</sup>, down 13.9% from prior year.
- **LBO price multiples continue record highs.** US LBO purchase price multiples now at 10.1x<sup>2</sup> EBITDA, a 9.2% increase from prior year. The previous peak was 9.7x<sup>2</sup> EBITDA which was reached in 2007 and 2014.
- **Exit activity increased significantly.** PE firms exited 1,026 companies<sup>6</sup>, representing \$326.8 billion<sup>6</sup> in total transaction value. This represents a 0.6% decrease in # of exits but a 21.8% increase in total transaction value compared to prior year.

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VC:

- **Capital overhang evident in VC.** VC dry powder at \$143.5 billion<sup>3</sup>, up 14% from the same period last year.
  - **VC fundraising continues 2014 upswing.** VC firms raised \$21.7 billion<sup>4</sup> in the first half of 2015, a 7% increase from the same period last year. Similarly, 129 funds<sup>4</sup> closed in the first half of 2015, a 30.3% increase from the same period last year.
  - **Investment activity strengthened.** US VC firms deployed \$38.5 billion<sup>7</sup> in capital for the first half of 2015, a 17.30% increase from prior year. Growth was driven by a substantial increase in average investment per deal which grew to \$10.8 million<sup>7</sup>, a 44.0% increase from prior years. The increase in average deal size was driven by US managers preferring later stage investments over early stage investments. Later stage companies generally require larger check sizes versus earlier stage companies.
- **US entry valuations are up.** In the US, while the average valuation of a Seed Stage investment was down 1.46% versus last year at \$6.07 million<sup>7</sup>, the average valuation of a Series A valuation was up 24.26% at \$15.06 million<sup>7</sup>, a Series B valuation was up 1.0% at \$41.4 million<sup>7</sup>, a Series C valuation was up 2.60% at \$82.5 million<sup>7</sup> and a Series D+ valuation was up 12.2% at \$184.0 million<sup>7</sup>.
- **Weak exit activity troubling.** While fundraising and investments are up, VC exits are down significantly. VC firms exited just 383 companies<sup>8</sup> in the first half of 2015, down 70.8% from the same period last year. Similarly, VC firm exits represented \$23.7 billion<sup>8</sup> transaction value down 49.2% from the same period last year.

Ex US:

- **Capital overhang is more evident outside the US.** PE dry powder outside the US grew 11.2% to \$578.3 billion<sup>9</sup> for 2014 compared to 2013. Currently, dry powder outside the US is greater than dry powder in the US by 8.4%.
  - **Ex US fundraising down.** Reflective of the current market dislocation in Europe and Asia, fundraising was down 32.0% to \$67.9 billion<sup>10</sup> compared to prior year. Asian funds raised \$15.9 billion<sup>10</sup> in capital, down 39.4% from prior year and European funds raised \$43.6 billion<sup>10</sup> in capital, down 35.0% from prior year.
  - **Ex US investment activity slightly down.** For the first half of 2015, Ex-US PE firms deployed \$75.2 billion<sup>11</sup> of capital, down 1.2% from prior year. The largest decline in deployment was in Asia where firms only deployed \$9.2 billion<sup>11</sup> in capital, a 52.5% decrease from prior years. This was offset by an increase in deployment in Europe of \$52.8 billion<sup>11</sup> (+10% from prior year) and the rest of the world of \$13.2 billion<sup>11</sup> (+49.5% from prior year).

As of June 30, 2015

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- **Ex US entry valuations declined.** Median EV/EBITDA multiples was up at 6.9x<sup>12</sup> EBITDA globally, a 3.6% increase from prior year. However, this was largely driven by a 9.2%<sup>2</sup> increase in purchase multiples in the US. Ex US purchase multiples declined overall.
- **Leverage multiples in Europe have declined.** European LBO leverage multiples have averaged 4.9x<sup>13</sup> EBITDA through the first half of 2015, a decrease of 4.0% from prior year. Similarly, total LBO financing at \$39.4 billion<sup>14</sup> is down 12.9% versus prior year.
- **Ex US exit activity is weak.** In contrast to the US which recorded \$185 billion<sup>15</sup> in exits for the first half of 2015, an increase of 81.8% from prior year, exits outside the US only amounted to \$142.0 billion<sup>15</sup>, a 14.8% decrease from prior year.

### Outlook:

- **PE allocations likely to increase.** A recent survey of institutional investors indicated that 52%<sup>16</sup> were below their target allocation for private equity. This is an increase of 13% from year end 2014.
- **Institutional investors most satisfied with US and like small- to mid-market buyout.** Institutional investors are most satisfied with their US private equity commitments with 92%<sup>16</sup> claiming that such managers met or exceeded expectations. This compares favorably versus Europe (81%<sup>16</sup>) and Asia (86%<sup>16</sup>). In the same survey, 50%<sup>16</sup> of institutional investors also cited the small to mid-market buyout strategy as presenting the best opportunities for 2015. Venture capital was mentioned next with 23%<sup>16</sup> of institutional investors believing it presented the best opportunities for 2015.

As of June 30, 2015

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Footnotes:

- (1) UBS' US Leveraged Capital Markets Weekly Update – July 2, 201
- (2) LCD's Leveraged Buyout Review – 2Q15
- (3) Preqin Quarterly Update – Q2 2015
- (4) Preqin Q2 2015 Private Equity Fundraising
- (5) PitchBook's Private Equity Breakdown Data Sheet (Q2 2015)
- (6) PitchBook's 1H 2015 Global PE Exits & Company Inventory Report
- (7) PitchBook's Venture Capital Valuations + Trends Data Sheet (2H 2015)
- (8) PitchBook's Venture Capital Liquidity Data Sheet (2H 2015)
- (9) To estimate Ex US capital overhang, SIS took annual global private equity dry powder from Preqin Quarterly Update – Q2 2015 and subtracted it from U.S. PE Capital Overhang from PitchBook's Fundraising & Capital Overhang Report Data Sheet (2H 2015). Year-end data was used as PitchBook did not have bi-annual data available.
- (10) Preqin Q2 2015 Private Equity Fundraising
- (11) Preqin Q2 2015 Private Equity-Backed Buyout Deals and Exits Factsheet - July 2015
- (12) PitchBook 3Q 2015 Global PE Deal Multiples & Trends Report
- (13) LCD European Leveraged Buyout Review (1H 2015)
- (14) LCD European Leveraged Lending Review (1H 2015)
- (15) PitchBook's 1H 2015 Global PE Exits & Company Inventory Report
- (16) Preqin Investor Outlook: Alternative Assets, H2 2015 Data Pack



# PRIVATE EQUITY PORTFOLIO

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## SAN MATEO COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

## PE Portfolio Overview

As of June 30, 2015

Investment Type	Policy Target	Policy Range	Market Value %	Market Value \$(000)	Unfunded Commitment \$(000)	Market Value + Unfunded \$(000)
<b>SamCERA - Total Plan</b>			<b>100.0%</b>	<b>3,438,626</b>		
Buyout (60% +/- 20%)	4.2%	3.2%-6.4%	3.3%	113,396	96,454	209,850
Venture Capital (20%, 0%-30%)	1.4%	0.0%-2.4%	1.3%	45,994	23,642	69,636
Debt-Related/Special Situations (20% +/- 10%)	1.4%	0.8%-2.4%	1.0%	34,753	35,798	70,551
<b>Total Private Equity</b>	<b>7.0%</b>	<b>6%-10%</b>	<b>5.6%</b>	<b>194,142</b>	<b>155,894</b>	<b>350,036</b>

### Portfolio Summary

- As of June 30, 2015 the Private Equity Portfolio had a total market value of \$194.1 million, with \$113.4 million in Buyout, \$46.0 million in Venture Capital, and \$34.8 million in Debt-Related/Special Situations. Total market value is the current reported value of investments, excluding the remaining amount of unfunded commitments.
- All sub-asset classes are below policy target as commitments continue to be made to new managers.

### Portfolio Activity

- From January 1, 2015 through June 30, 2015, SamCERA committed \$8.0 million to Emergence Capital Partners IV and \$15.0 million to JLL Partners Fund VII.



# PRIVATE EQUITY PORTFOLIO PERFORMANCE

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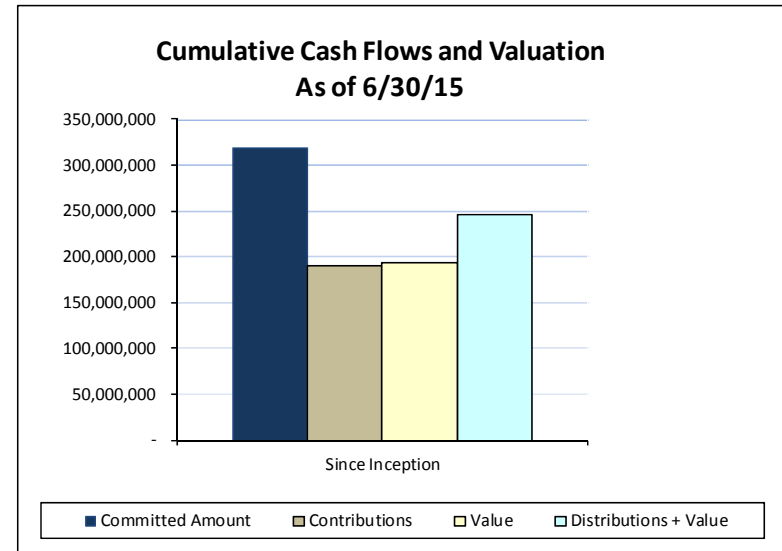
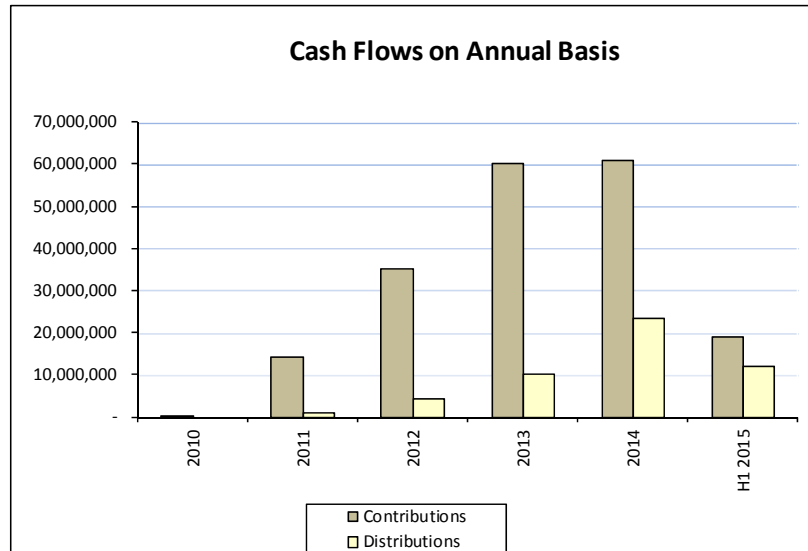
# SAN MATEO COUNTY EMPLOYEES' RETIREMENT ASSOCIATION

## PE Performance

As of June 30, 2015

### Performance

- The Private Equity portfolio is in the early stages of its investment period, but with a capital weighted average investment age of 1.76 years, performance results as measured by net IRR at 17.45%, are more meaningful.
- The portfolio is currently valued at \$194.1 million. Together with \$51.0 million in realized distributions, the Total Value at \$245.1 million is approximately \$55.7 million above \$189.4 million total capital contributions, resulting in a total value multiple of 1.29x and a distribution multiple of 0.27x.
  - Buyouts up \$39.8 million / +38.1% versus cost (Sycamore, ABRY VII, and Warburg Pincus XI leading), with 29.7% of Total Value of portfolio distributed;
  - Venture Capital up \$16.8 million / +55.1% versus cost (General Catalyst VI, Third Rock III, and NEA 14 leading), with 4% of Total Value of portfolio distributed; and
  - Debt-related/Special Situations down \$0.9 million / -1.7% versus cost (negatively impacted by Sheridan II-B; however ABRY Advanced Securities II & III, and Regiment Capital Special Situation V are up \$7.9 million in aggregate / 22.9% versus cost), with 34.4% of Total Value of portfolio distributed.
- Within Private Equity, the current allocation of invested capital is 58.4% to Buyout, 23.7% to Venture Capital, and 17.9% to Debt-Related/Special Situations.

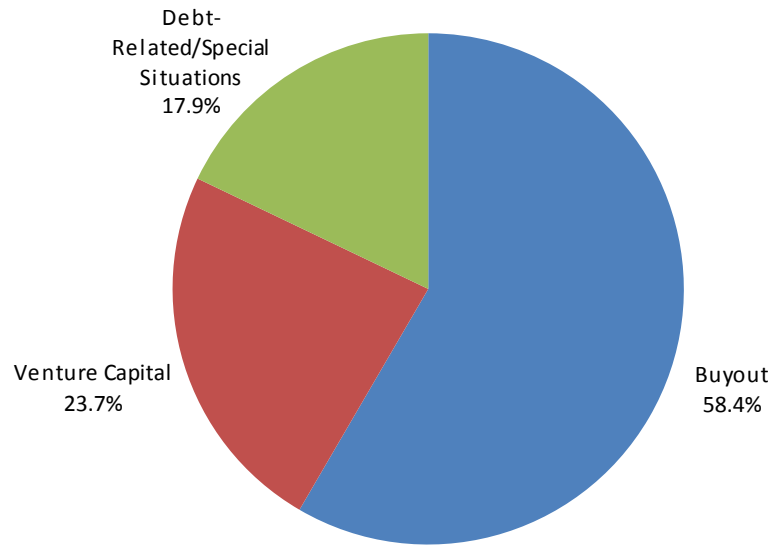


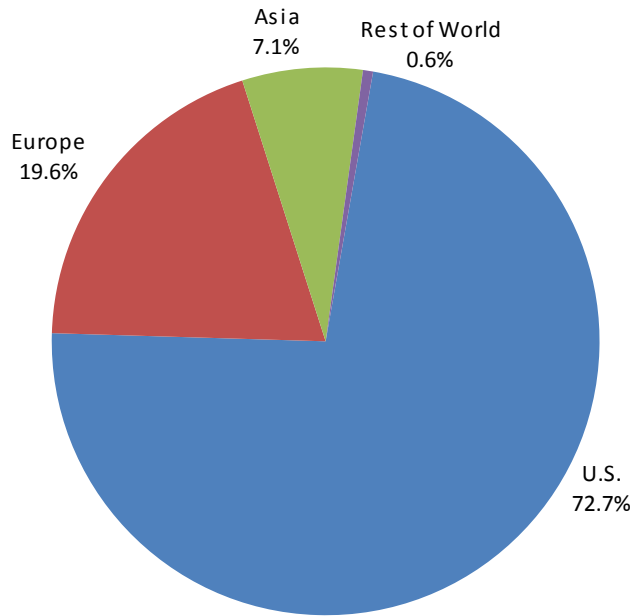


# PRIVATE EQUITY PORTFOLIO DIVERSIFICATION

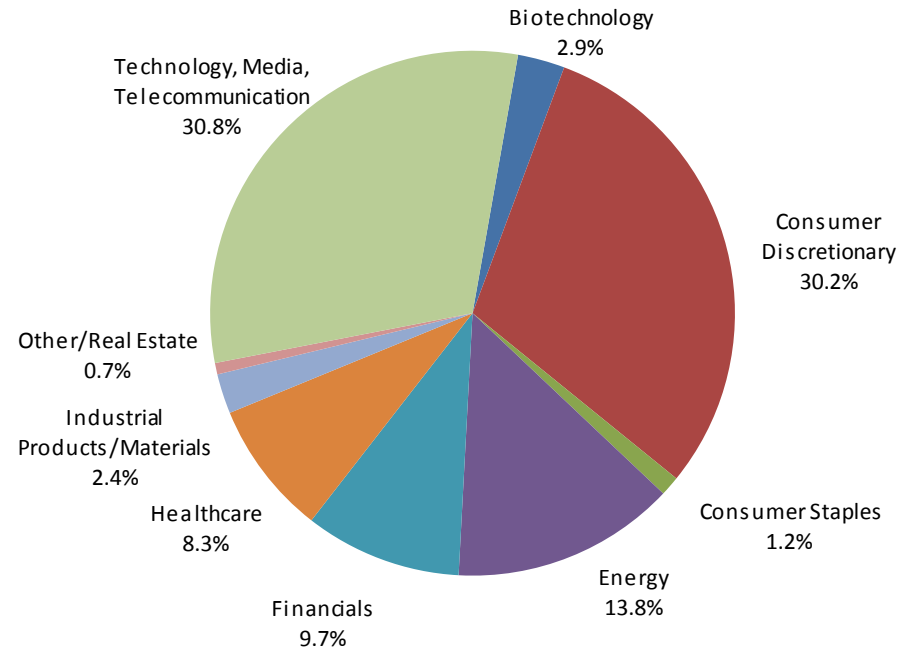
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**Private Equity Portfolio: Current Exposure**





Based on the value of portfolio companies As of June 30, 2015 if provided by the partnerships. Differences between reported value and the total portfolio valuation is due to temporary cash funds, fees, other expenses, and holdings with undisclosed geography breakdown.



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