Overview of Private Equity Markets

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Agenda

- Private Equity Overview
- Investment Strategies
- Terms and Fees
- Implementation/Keys to Success
Private Equity – BIG Deal?

“Private Equity Continues Positive Annualized Returns for Long-Term Investors”

“Private equity basks in ‘golden age’ of returns”

- $3.4 trillion in Assets Under Management
- Over 65,000 PE-backed companies
- Over 15 million employed by PE-backed companies
- In 2018:
  - 24,444 transactions worldwide
  - $563 billion invested globally
  - $416 billion in M&A exit value

SOURCE: Mergermarket, Preqin, and Pitchbook.
Private Equity Is...

- Investments in privately held companies in various stages of development, within a variety of strategies, including venture capital, growth equity, and buyouts.

<table>
<thead>
<tr>
<th>PUBLIC EQUITY</th>
<th>PRIVATE EQUITY</th>
</tr>
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<tbody>
<tr>
<td>- Liquid investments</td>
<td>- Illiquid investments</td>
</tr>
<tr>
<td>- Purchased through exchanges</td>
<td>- Privately negotiated transactions</td>
</tr>
<tr>
<td>- Dispersed ownership</td>
<td>- Significant ownership</td>
</tr>
<tr>
<td>- Passive strategy</td>
<td>- Active strategy</td>
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Private Company Opportunities—Access to Expanded Opportunity Set

**PRIVATE COMPANY OPPORTUNITY SET**

Number of U.S. Companies
Revenues of $10 million and Above

- **U.S. Private Companies**
  - 97% (178,821)
- **U.S. Public Companies**
  - 3% (4,611)

**BUYOUT-BACKED COMPANY GROWTH**

Number of U.S. Companies
Public vs. Buyout-Backed

- Since 2000, the number of PE-backed companies has grown, whereas the number of public companies has declined.

Source: Capital IQ Database, May 16, 2018.

Source: World Bank, Pitchbook.

As of September 30, 2018.
Private Equity: Opportunity for Strong Returns

- Greater resources = higher costs than public equity strategies.
- However, private equity has outperformed public benchmarks by certain measures, net of fees and expenses.¹

¹. See slide 7.
Private Equity Has Generated Strong Long-Term Relative Returns

20-YEAR RETURN

<table>
<thead>
<tr>
<th>Index</th>
<th>IRR</th>
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<tbody>
<tr>
<td>PE-Composite World&lt;sup&gt;a&lt;/sup&gt;</td>
<td>11.9</td>
</tr>
<tr>
<td>MSCI Emerging Markets&lt;sup&gt;b&lt;/sup&gt;</td>
<td>8.8</td>
</tr>
<tr>
<td>NASDAQ&lt;sup&gt;b&lt;/sup&gt;</td>
<td>6.7</td>
</tr>
<tr>
<td>S&amp;P 500&lt;sup&gt;b&lt;/sup&gt;</td>
<td>5.6</td>
</tr>
<tr>
<td>MSCI World&lt;sup&gt;b&lt;/sup&gt;</td>
<td>5.0</td>
</tr>
</tbody>
</table>

<sup>a</sup>Represents global all private equity dollar-weighted horizon returns from 6,520 funds tracked by Burgiss Private iQ in the strategy categories of venture capital, corporate finance, generalist, and energy and calculated using Burgiss data available as of December 31, 2018.

<sup>b</sup>Public index returns are obtained from Bloomberg and are time-weighted for the period indicated.

NOTE: As of December 31, 2018.
Private Equity Has Not Only Created Value but Has Also Generated Significant Cash

- U.S. PE funds distributed $480 billion to limited partners in 2018.

U.S. PRIVATE EQUITY DISTRIBUTIONS

<table>
<thead>
<tr>
<th>Year</th>
<th>Distribution ($)</th>
</tr>
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<tbody>
<tr>
<td>2010</td>
<td>106</td>
</tr>
<tr>
<td>2011</td>
<td>237</td>
</tr>
<tr>
<td>2012</td>
<td>313</td>
</tr>
<tr>
<td>2013</td>
<td>406</td>
</tr>
<tr>
<td>2014</td>
<td>458</td>
</tr>
<tr>
<td>2015</td>
<td>465</td>
</tr>
<tr>
<td>2016</td>
<td>368</td>
</tr>
<tr>
<td>2017</td>
<td>530</td>
</tr>
<tr>
<td>2018</td>
<td>480</td>
</tr>
</tbody>
</table>

Source: Burgiss Private iQ, as of December 31, 2018, as produced using Burgiss data.
Private Equity Has Delivered Attractive Returns, But What About the Risks?
Private Equity Has Delivered Attractive Returns, But What About the Risks?

**CONSULTANT ESTIMATES OF STANDARD DEVIATION**

- Private Equity: 24.7%
- Domestic Public Equity: 16.5%

**ACTUAL STANDARD DEVIATION**

- 10-Year:
  - Private Equity: 5.6%
  - Domestic Public Equity: 14.2%
- 20-Year:
  - Private Equity: 12.9%
  - Domestic Public Equity: 15.9%

**NOTE:** Based on the average 10-year expected standard deviation taken from six market consultants, as of December 31, 2018. Private equity estimates range from 21.1% to 29.3%; domestic public equity estimates range from 13.8% to 18.0%.

*aBased on the standard deviation of quarterly returns of the Burgiss Private iQ global all private equity benchmark, as produced using Burgiss data.*

*bBased on the standard deviation of quarterly returns of the S&P 500 index.*
Who Invests in Private Equity

BREAKDOWN OF AGGREGATE CAPITAL CURRENTLY INVESTED IN PE BY INVESTOR TYPE

- Public Pension Fund: 30%
- Financial Institutions: 14%
- Foundations & Endowments: 12%
- Sovereign Wealth Fund: 17%
- Private Sector Pension Fund: 15%
- Other: 12%

% OF INVESTORS SEEKING TO INCREASE EXPOSURE OVER NEXT YEAR

- Increase/Maintain Exposure: 88%
- Decrease Exposure: 12%

Private Equity Targets Companies in All Stages

**Strategies:**
- Venture Capital
- Growth Equity
- Buyouts
- Distressed Debt/ Turnaround

**Companies:**

NOTE: Examples are included for illustrative purposes only.
Buyouts Explained

**PURCHASE**
- Stable & cash-generative companies
- Combination of equity and debt

**IMPROVE**
- Strengthen and de-risk
- Enhance management
- Operational improvements
- Expand market

**DEBT PAYDOWN**
- Reduce debt using company profits

**SELL**
- Take public or sell to strategic or financial buyer
Buyout Market

BUYOUT PARTNERSHIPS SIZE/REGION MAP

NOTE: Examples are included for illustrative purposes only.
Public Market vs. Private Market EV/EBITDA Multiples

- The EV/EBITDA multiple for the public market has increased by 67% since 2008, compared with a 5% increase in the private market multiple.
- Public market valuations have been considerably more volatile than private market valuations over the past 10 years.
Venture Capital Explained

- **SEED STAGE**
  - Idea generation
  - Limited revenue

- **EARLY STAGE**
  - Initial product marketing

- **EXPANSION STAGE**
  - Product traction
  - Revenue growth

- **LATER STAGE**
  - Revenue growth
  - Improving margins

**Exit**
- IPO
- M&A

NOTE: Examples are included for illustrative purposes only.
Venture Capital Market

VENTURE PARTNERSHIPS STRATEGY/SECTOR MAP

NOTE: Examples are included for illustrative purposes only.
Venture Capital Market Continues to Evolve

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>2012</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S. Venture Fundraising&lt;sup&gt;a&lt;/sup&gt;</td>
<td>$100 billion</td>
<td>$23 billion</td>
<td>$42 billion</td>
</tr>
<tr>
<td>Number of New Unicorns&lt;sup&gt;b&lt;/sup&gt;</td>
<td>NA</td>
<td>7</td>
<td>52</td>
</tr>
<tr>
<td>Median Sales at IPO&lt;sup&gt;c&lt;/sup&gt;</td>
<td>$12 million</td>
<td>$108 million</td>
<td>$174 million</td>
</tr>
<tr>
<td>Number of Tech IPOs&lt;sup&gt;c&lt;/sup&gt;</td>
<td>260</td>
<td>39</td>
<td>38</td>
</tr>
<tr>
<td>Median Age at IPO (Years)&lt;sup&gt;c&lt;/sup&gt;</td>
<td>5</td>
<td>9</td>
<td>12</td>
</tr>
</tbody>
</table>

**NOTES:** Data provided for informational purposes only. NA=Not available.<sup>a</sup>Source: Thomson Reuters and Pathway Capital Management. Fundraising amounts are based on net amounts raised, which are adjusted for fund-size reductions. <sup>b</sup>Source: PwC and CB Insights’ MoneyTree Report™. <sup>c</sup>Source: Dr. Jay R. Ritter, University of Florida.

- Companies are waiting longer to IPO, potentially shifting a greater portion of a company’s growth and value creation to private investors.
Private Credit: A Complement to Traditional Fixed Income

**CHARACTERISTICS OF PRIVATE CREDIT INVESTMENTS**

- Contractual interest payments (fixed/variable, cash/PIK)
- Governed by loan agreements or indenture
- Typically backed by collateral
- Enhanced yields compared with public alternatives
- More illiquid than fixed income
- Generally non-marketable

NOTE: There can be no assurance that any private credit investments will ultimately have these characteristics.
Infrastructure Investment…

- Infrastructure is a broad sector consisting of a wide array of assets that provide necessary services to society.

Characteristics of Infrastructure Assets

- Essential Services
- Monopolistic/High Barriers to Entry
- Stable, Long-Term Cash Flows
- Inflation-Correlated Revenues

Note: There can be no assurance that any infrastructure investments will ultimately have these characteristics.
Private Equity Model

**LIMITED PARTNER INVESTORS (LP)**
- Oversight Role
- Majority of Capital
- Limited Liability

**PRIVATE EQUITY FUND MANAGER (GP)**
- Responsible for Investment Decisions
- Unlimited Liability
- Contributes Personal Capital
- Participation in Profits

**PRIVATE EQUITY FUND (LIMITED PARTNERSHIP)**

Company A  Company B  Company C  Company D  Company E
Life Cycle of a Primary Fund

- **Capital Call Period**: Manager ‘calls’ cash from investors
- **Deployment of Capital**: Manager puts cash to work
- **Harvest of Returns**: Investments are realized, cash is returned to investors
What is a Co-investment?
What is a Secondary?

BUYER
New Investor

PRIVATE EQUITY PARTNERSHIP

Company A

Company B

Company C

Company D

Company E

SELLER
Current Investor

Purchase Price ($)

Transfer of Remaining Commitment and Current Assets
Fund Structure and Terms

- The Limited Partnership Agreement (LPA) is negotiated between the LP and GP and defines the terms of the fund and the legal foundation for the partnership.

**IMPORTANT CATEGORIES OF KEY TERMS**

- Economics
- Safety Triggers and Remedies
- Investment Restrictions
- Conflicts of Interest
- Indemnification
- Reporting
Carried Interest

- Carried interest rewards the fund manager for strong performance.
  - Managers receive compensation for gains generated over a certain preferred return.
  - Paid from investment distributions.
  - High carried interest = Strong returns!

**DISTRIBUTION WATERFALL**

- Return of Capital: 100%
- Preferred Return: 8%
- Catch-up: 20%
- Carried Interest: 80%

NOTE: For illustrative purposes only. Not all distribution waterfalls resemble the one presented.
Investing in private equity is more complicated than investing in the public markets.
Characteristics of Successful Private Equity Programs

- Consistent Investment
- Robust Resources
- Access to High-Quality Opportunities
- Disciplined Manager Selection
- Rigorous Due Diligence
- Durable Portfolio
Common Mistakes in Private Equity Fund Investing

PERFORMANCE SPREAD BETWEEN UQ AND LQ MANAGERS

NOTE: IRRs are ranked by quartile. The graph shows the IRR spread between the first and fourth quartiles (i.e., the 25th and 75th percentiles), as measured in basis points. Managers may have more than one fund in the sample set, and funds from the same manager may have different quartile rankings.

\[ \text{NOTE: Based on Burgiss Private iQ U.S. all private equity returns, as of December 31, 2018, as produced using Burgiss data.} \]

\[ \text{\textsuperscript{a}Represents horizon returns from 2,001 funds tracked by Burgiss Private iQ.} \]

\[ \text{\textsuperscript{b}Represents horizon returns from 4,028 funds tracked by Burgiss Private iQ.} \]

\[ \text{\textsuperscript{c}Represents horizon returns from 2,998 funds tracked by Burgiss Private iQ.} \]
Looking Forward

- The private equity asset class offers the potential for an expanded universe of investment opportunities and for high return.

- Private equity is not without risks and can be complicated and challenging for investors to access.

- A focus on manager selection and a long-term, consistent approach are key tenets of many successful private equity programs.
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