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The European Private Equity Data Service provides monthly coverage on the European private equity market and records fund launches and closings in Europe and Israel.

## Private Equity Analyst Outlook 2002 – Conference Notes.

The Private Equity Analyst Outlook 2002 Conference, held in New York last week, was a subdued affair. The keynote speaker ventured "A New Sense of Optimism?" as the title for the event, whereas "A New Sense of Realism" would have been more appropriate. Distilled down from almost two days of panels and discussion, the following struck me as the most salient points: 1) conservative estimates on 2002 fundraising; 2) reality returning to valuations; 3) LP activism gradually picking up steam; and 4) limited bright spots for 2002.

**1) Conservative estimates on 2002 fundraising**

Asset Alternatives produced their 2001 numbers, showing overall fundraising down over 40% in the US from $175 billion in 2000 to $100 billion in 2001. Worst hit were the venture capital and fund of fund segments, with only life science and secondaries showing an increase. The prognosis for 2002, based on the views of pundits asked to make forecasts, ranged from $55 to $90 billion, averaging close to $65 billion. In the context of a 2001 European fundraising total of $55 billion I'd say this looks too low; but illustrates how expectations in the US market have been firmly reset.

**2) Reality returning to valuations**

With commendable frankness Brooks Zug at HarbourVest Valuations stated that the 1999 vintage venture funds in their portfolio look like being the worst in their history; worse even than 1982 vintage funds. With values among this group declining by 15% a quarter most will do very well to return capital. Seen from the secondary market perspective Brent Nicklas at Lexington thought that venture valuations are over half way to a full correction, and that buyout valuations have now fully corrected. December 2001 quarterly reports could provide the opportunity for GPs fully to reset expectations.

**3) LP activism gradually picking up steam**

While the majority of LPs continue to look at performance net of fees, it seemed clear from the conference that the days of 30% carry have gone. According to one participant, "if the terms are not industry standard the fund does not even get looked at". Beyond this, LP activism appears to be focusing on three main issues: right of transfer; GP commitments; and fund size. In terms of right of transfer, JP Morgan now insists on absolute, unfettered rights of transfer on all LP interests – good news for the secondary market should this become the predominant industry trend. On GP commitment (the "fund size to doe" ratio in Goldman Sachs parlance) there is a clear trend towards GPs being asked to show additional financial commitment to their own funds. On fund size, much was made of the fact that there are now over 30 "early-stage" venture capital funds in the US with funds in excess of US$ 1 billion. Notwithstanding certain imaginative attempts to justify such structures the message to GPs was loud and clear: "Go back to the fund size that made you successful".

GPs (with certain exceptions) remain defensive on these matters and resistant to change, preferring in general to be administering "tough love" (through preferential returns, ratchets and the like) than receiving it. The most critical issue in our view, standardised performance data, is a continuing source of despair among LPs. Furthermore, there is no concerted effort to improve the situation, so it's likely that every GP will be "top-quartile" for some years to come!

**4) Limited bright spots for 2002**

Other than the segments of the market which one would expect to benefit from an economic downturn (secondaries, distressed, certain specialist funds) there were possibly just two areas that some consider bright spots for 2002: healthcare services and nanotechnology. Healthcare services looks set to benefit from Congress changes to Medicare rulings in the US and as a sector is gaining increasing acceptance by the capital markets. Nanotechnology receives strong opinions on both sides, but looks interesting as an area that has the potential to spawn truly revolutionary approaches to technology. Otherwise, with many of the top GPs forecast to be absent from the market in 2002, and a huge overhang of capital, it's a year to be selective. The brightest spot of all was the healthy realignment of expectations in this market. Of the 4,000 GPs that one prominent LP has examined, only 15% had actually made 20% net cash on cash returns. Another LP stated that 15% net was a great overall return from private equity. Balanced with the consideration that exceptional returns were made coming out of both the 1980/1981 and 1990/1991 recession makes this an environment in which it will pay to be investing, selectively, in quality GPs, with an eye on good times ahead.

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## News and Developments from European Fundraisers

| Status | Fund Name | Manager | Region | Stage | Sector | Target (Em/bn) | Close (Em/bn) |
|---|---|---|---|---|---|---|---|
| FIN | Global Private Equity IV | Advent International | Europe / US | Buyout | Generalist | 2000 | 2000 |
| FIN | BioEquities Fund | MPM Capital | US / Europe | Public and Private | Biotech | 509 | 509 |
| FIN | Abingworth Bioventures III | Abingworth Management | US / Europe | Early-Stage | Life Science | 170 | 255 |
| FIN | Baring Vostok Private Equity | Baring | Russia, Ukraine, N | Expansion, Buyout | Generalist | n/a | 232 |
| FIN | Emerald Fund | Emerald | Italy | Mid-Market | Generalist | 200 | 216 |
| FIN | Walden Israel | Walden Israel | Israel | Early-Stage | Technology | 136 | 102 |
| 1st | Private Equity European LP | HSBC Private Equity | Europe | Mid-Market | Manufacturing, Service | 876 | 642 |
| 1st | Polytechnos Venture Partners | Polytechnos Venture Partners | Germany, US, Mid | Early-Stage | Technology, Life Science | n/a | 120 |
| FA | Charterhouse Development Capital | Charterhouse | UK / Europe | Buyout | Generalist | 3000 | 0 |
| FA | Conduit Ventures | Conduit Ventures | US / Europe | Early, Expansion | Fuel Cell Technology | 113 | 0 |

*Status Key: FA - Fund Announced; 1st - 1st Close; 2nd - 2nd Close; 3rd - 3rd Close; Fin - Final Close; P - Pulled*

*Target Key: na - not available; ns - not set, Includes funds with a target size over E100m*

*Source: Brain Capital. For an up to date schedule of European Private Equity fundraising activity contact James Miller on +44 (0)207 488 4401 or email james@braincapital.com*