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White Paper No. 40: Private Equity Investing

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Once an investor decides to allocate capital to private equity, the first question is "How should I go about it?" Properly structured, private equity can be the most rewarding sector of an investment portfolio. Unfortunately, most investors in private equity don't earn returns anywhere near what they need to compensate for the risks they have taken. The purpose of this paper is to summarize the private equity opportunity, identify the key risks, and outline a strategy for investing in private equity sensibly and profitably. This paper is designed to be useful to investors who are looking to put less than about $50 million into a diversified private equity portfolio.

An Introduction to Private Equity

❖ The Asset Class

Private equity investing is the business of investing in privately-held companies or those that are taken private in the process. For most individual investors this is a prohibitively difficult and risky business. A more sensible channel is to invest in private equity funds (that is, limited partnerships) alongside a seasoned private equity investment firm. The present day private equity market emerged in the 1970s when private equity firms formed partnerships to provide private financing to start-up companies. These partnerships are raised by private equity firms who act as the *general partner* (GP). Investors who provide the capital are known as *limited partners* (LP). The date of the first investment into a company is known as the *vintage* year. Companies into which the fund invests will be in various phases of their own lives, giving rise to styles of investing. Private equity funds generally concentrate on a particular style of investing defined by the stage of development of the companies into which they invest.

The *stage* of company development represents a range from start-ups to large, mature companies. A private equity fund will generally focus its investing in a particular segment along this range of maturity. Start-up companies are generally seeded by individual angel investors or venture capital firms. Once a firm has developed its business plan, product or service, but is pre-revenue, it is considered to be *early-stage* by venture capital firms. As these companies mature, produce revenues and develop a customer base, they are considered *growth equity* or *late stage* venture capital candidates. More mature, often profitable and larger companies become the playground of the buyout funds. Buyout funds leverage their acquisitions of private companies with debt based on the cash flow characteristics of the underlying operating companies. Buyout firms will generally concentrate either on small, middle or large capitalization companies, sometimes a combination of two. A private equity firm's commitment to a stage will be based on the skill sets, history and experience of the

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individuals in the firm. In addition to stage investing, there are "other" styles, including mezzanine debt investing, distressed investing, secondary investing, etc.

Lastly, private equity is a global asset class. Key drivers of opportunities in private equity in Europe, Asia and the US differ as we will discuss later but diversification into non-US markets is every bit as important as stage and vintage year diversification.

Venture and buyout investing represent a riskier means of gaining exposure to equities than the public markets. The high leverage in buyout transactions and the early-stage nature of venture investing create greater risk and the investor has the right to expect materially higher investment returns as a result. A private equity firm's goal is to invest in a private company and then sell its interest for a profit. This realization of the investment is known as the "exit" and generally occurs as the result of a sale, public floating of the stock or merger with another firm. The correlation of returns to the public markets varies with the stages of investment but is fairly high given the importance of IPOs as exit channels and the public market impact on corporate valuations in merger and acquisition activity. Overall, historic private equity returns represent a compelling opportunity for investors, and argue for an allocation to this asset class in a well-diversified investment program. As we will see, the aggregate returns of the asset class over a long period of time are in excess of the public markets. However, they carry considerable volatility along with issues associated with illiquidity, cyclicality and a dispersion of the returns. In the next few paragraphs of this paper we examine these return characteristics, their disparity and persistence amongst various fund investors, and, various other important considerations to investing in private equity.

❖ The Investment

Once an investor decides to allocate to private equity, the next question is "How?" There are several important challenges associated with realizing the historic high returns of the private equity asset class given the corresponding high volatility, illiquidity, and the sometimes very confusing range of implementation alternatives available. Important considerations include cyclicality, the disparity of returns amongst upper, median and lower quartile performing private equity firms, stages and vintage years, the importance of identifying and gaining access to top-tier managers, terms and conditions, conflicts of interest and the difficulty of sorting through all of this as a relatively small investor. A successful program will be long-term in nature, diversified across geography, stages and vintage years, and have access to the best managers in the business. For other than the largest institutional investors, this turns out to be a rather tall order.

Access to the top-tier funds has always been difficult. In the venture capital and small to mid-cap buyout market it is extremely difficult, globally. In the US the equivalent of 'irrational exuberance' in

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late 1990's venture capital created an overhang of capital that took several years to absorb. The consequence was that the better funds downsized, coming back to the market less frequently making access all the more difficult. A similar situation unfolded in the buyout market as abundant liquidity facilitated massive fund raising and transaction activity in 2004-6. The collapse of the credit markets in 2007 brought activity to a near standstill, leaving a worrisome overhang of unused capital and problem credits associated with deals, particularly in the large cap market. Two consequences are returns in that sector will be badly damaged for some time to come, and, there now exists additional pressure to put money to work at a time when credit is in lesser supply. Investors are aggressively seeking out the more experienced small and mid-cap managers, making the individual investor's job very difficult.

Private Equity Returns

Private equity returns run in cycles and are strongly influenced by market conditions, credit markets, company valuations, liquidity for exits, merger and acquisition activity, and other factors, including the amount of money looking for exposure to the asset class. Private equity investing should be undertaken only with the long term in mind, i.e., investors should commit to a long-term plan of continuous investment in order to bridge the inevitable bad return years.

In a mere 12 year period through 2010, we have been witness to the unpredictability of events affecting not only activity and returns, but investor psychology. In the late 1990s, investor enthusiasm for venture investing in emerging technologies led to the now famous bubble, which burst dramatically in 2000. This left a significant overhang of excess capital and well remembered losses. It also gave rise to an active secondary market in relieving illiquid investors of unwanted commitments. Returns stagnated for years as the industry retrenched. Events of 2001 depressed the equity markets further, placing additional pressures on exits and therefore returns. As the markets languished there was continued investing by smaller buyout firms. What was unclear at the time was these investments in 2003-5 would prove to be extremely successful later in the decade. As liquidity built in the economies of 2005-7 the large cap buyout market became extremely active and for a short period returns were spectacular. Of course when the credit markets collapsed in 2007 this party came to a quick end, leaving much downsizing to be done. Meanwhile, the secondary and distressed sectors took full flight. Venture continued to downsize late in the decade producing minimal returns. However, it finished 2010 with considerable strength and renewed optimism. So, how do you see all of this coming? You don't. Investing in this asset class requires great discipline and commitment. Realizing consistent returns over a long time frame requires patience and restraint, investing deliberately with top tier firms that have a history of success.

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Asia and Europe were not immune to events that took place in the US as most of the calamities became global. Europe is mainly a buyout market and experienced similar swings as the US. Asia is dominantly a growth equity market, and while public equity markets had an effect on activity and returns, the credit markets were much less of an issue. In reality, Asia snapped back from the 2007 meltdown much faster than the rest of the world.

❖ Return Characteristics

Returns vary amongst the stages of private equity. Historically, early stage venture capital returns are higher than later stage venture capital. Buyout returns are lower than those of venture capital, brought down by large and mega-cap fund performance, while small- and mid-cap returns are among the highest in the asset class. This can be explained by the difference in risk undertaken between the stages of investing. Early stage companies are pre-revenue and the winners can provide huge payoffs. On the other hand, failures are plentiful, so patience, granularity and access are a must. In the buyout arena, firms are more mature, cash flow positive and they have accepted business models. While the volatility is less, historic returns are lower.

Fund Stage	3 Years	5 Years	10 Years	20 Years
All Venture Capital	**-0.85**	**3.87**	**-2.41**	**19.23**
All Buyouts	**-0.54**	**4.35**	**4.07**	**8.86**
Small Buyouts	-1.25	1.58	2.7	12.14
Medium Buyouts	3.1	7.06	3.5	11.58
Large Buyouts	3.26	6.29	3.29	11.9
Mega Buyouts	-1.34	3.91	4.45	7.2
Mezzanine	1.12	2.94	2.75	6.95
All Private Equity	**0.14**	**4.8**	**2.55**	**11.47**
NASDAQ	-2.1	2.64	-	-
S&P 500	-6.0	0.7	0.1	8.2

All data is as of 9/30/2010.
Source: Thomson Reuters

As the chart suggests, longer term returns follow the expected patterns, but short and even intermediate term returns are unpredictable. Note, for example, that the recent performance of buyouts funds reverses the longer term performance. As we will discuss shortly, there is great disparity between upper quartile, median and mean average returns. Being the average for all

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reporting funds, this chart understates the possibility for returns if the investor has access to the top tier performers.

❖ The Persistence of Returns

When we talk about the importance of "access," we refer to the disparity of returns of upper-quartile performers versus those at the median and those in the bottom quartile. There is a persistence of investment returns with individual private equity partnerships. In MIT's detailed research paper, "Private Equity Performance: Returns, Persistence and Capital," Steve Kaplan and Antionette Schoar quantitatively chronicle the relative success of firms that have raised several successful funds over those that have raised fewer:

> Returns persist strongly across funds raised by individual private equity partnerships. The returns also improve with partnership experience. Better performing funds are more likely to raise follow-on funds and raise larger funds than funds that perform poorly. Funds started in boom times are less likely to raise follow-on funds, suggesting that these funds subsequently perform worse. Aggregate industry returns are lower following a boom, but most of this effect is driven by the poor performance of new entrants, while the returns of established funds are much less affected by these industry cycles.[1]

It is these firms that are the most difficult to access.

General partners whose funds outperform the industry in one fund are likely to outperform the industry in the next. This is far different from other asset classes, e.g., large-cap equity, where the persistence of performance is evident mainly on the downside. Much of the persistence in private equity returns can be explained by the reputation of the individuals in the firms and their ability to attract the very best entrepreneurs and opportunities. These firms have a rich history of making companies successful. The resulting record of success helps to establish proprietary deal flow. As the MIT paper suggests:

> …better funds may see and be able to invest in better investments. Second, private equity investors typically provide management or advisory inputs along with capital. If high-quality general partners are a scarce commodity, differences in returns between funds could persist.

Most well known private equity firms are all but impossible for the individual to gain access to. "Smaller" investors obtain access to these managers through established funds of funds.

[1] Steven N. Kaplan, Antoinette Schoar, "Private Equity Performance: Returns, Persistence, and Capital Flows," The Journal of Finance 60 (4), 1791–1823 (2005).

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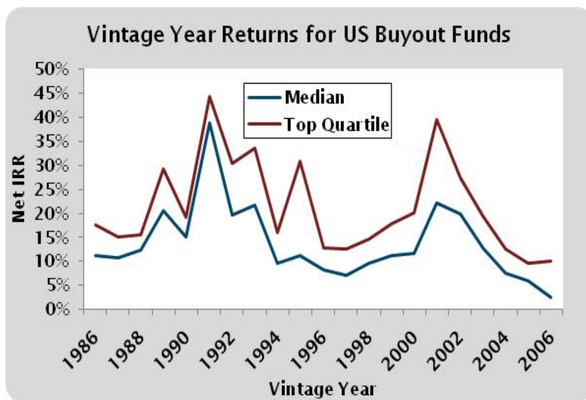
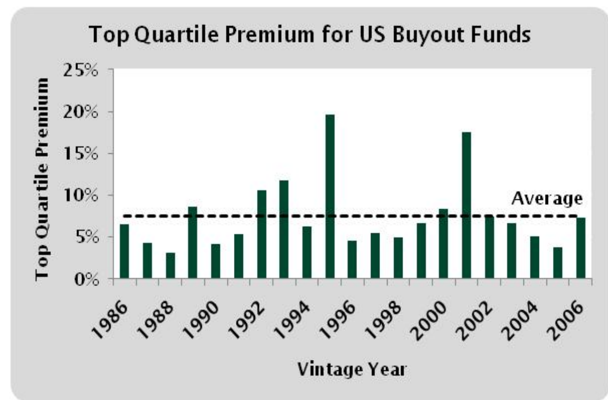
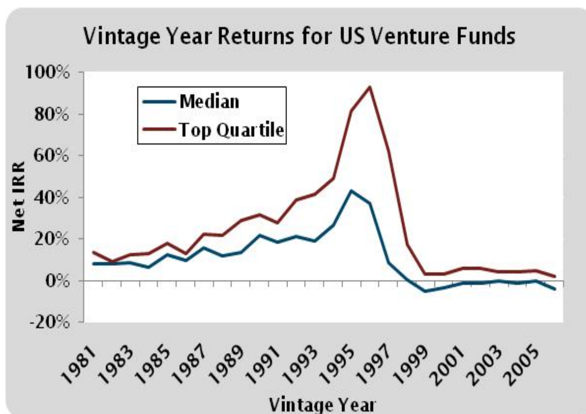
❖ Return Differentials Among Private Equity Firms

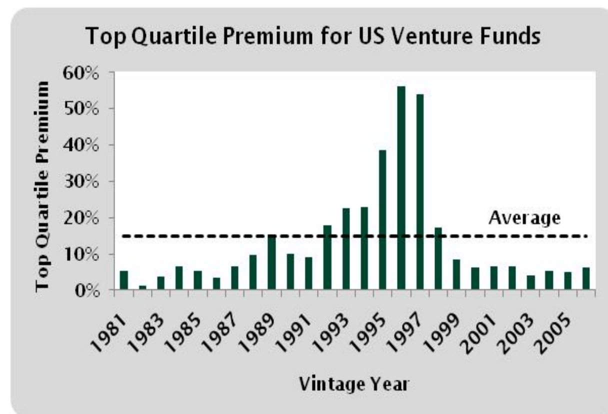
The disparity of returns between the upper quartile performers, the median and the bottom quartile performers is dramatic, underscoring the importance of gaining access to the top performers. Note that this disparity, large as it is, is understated by "survivor bias," i.e., it does not include the performance of funds that have failed or are no longer in business. Their inclusion would make the results even more compelling. In the case of performance against the median, buyout's top quartile performers have out- performed by a factor of 8X, whereas venture capital's top quartile has bested the median by 15X. In the investment world, outperformance on this scale is eye-popping, indeed.





Source: Cambridge Associates





Source: Cambridge Associates

As was pointed out in the discussion of persistence of returns, firms that have raised more than one fund tend to outperform those that have raised a lesser number. (Hardly surprising – it's a lot easier to raise that second fund if the first one went well.)

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Gaining Exposure to Private Equity

Most sophisticated asset allocation programs will include exposure to private equity. The challenge is to create a durable program, gain access to managers that have a history of out-performance, and structure a portfolio that is well diversified across vintage years, geography, and the various stages of company maturity. There is also the challenge of reaching one's target allocation to the asset class given the nature of the investment pattern (see Ramping up to Your Target Allocation, below).

Constraints imposed by the size of an individual's allocation to this asset class are a further complication. A normal allocation for the long-term investor is probably 10-20% of the total portfolio. Let's take the case of a $100 million investment portfolio. How would an investor develop a well diversified portfolio that spans geography, time and style with "only" $10 to $20 million to invest, given the difficulty of getting access to the best managers and their generally high minimums of $5 million and up?

In order to achieve this vintage year and style diversification, patience and persistence are needed. It means making annual commitments of, say, $5 to $10 million in order to reach the $10-20 million target. Since this money will be drawn down over a 4 to 7 year period, reaching the target allocation requires discipline and some luck, given the uncertainty of the draws, the unpredictable return of cash, and the changing size of the total portfolio over time.

We recommend structuring a program with one or more "fund of funds" (FOFs) and committing to investing with them over a period of years to get the targeted diversification. This allows the investor access to multiple underlying funds whose minimum investments are far greater than the individual's annual commitment would otherwise permit.

❖ The Emergence of Funds of Funds

Private equity funds of funds are a relatively new phenomenon. They have been around since the 1970s but proliferated in the 1990s as individuals and smaller institutions began to demand access to the asset class but were too small to gain direct access to the better individual funds. Funds of funds (FOFs) represent an efficient way to quickly build a diversified private equity program. There is a wide array of FOFs, sponsored by a variety of firms, including banks, off-shoots of diversified asset managers and independent firms. Most of the best individual private equity funds have fairly high minimum investment requirements and are all but closed to new investors. For the investor who will commit, say, $5 million annually, committing to a FOF in that amount permits access to multiple funds, vintage years and styles…at each commitment. This represents an effective alternative to building a direct private equity program. It is a way of delegating portfolio construction and monitoring to a firm with the resources to do it and the access to top performers that is so

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important. In selecting FOFs for our clients it is important to consider the investor's needs, the nature of the FOF offerings, and their distinctive characteristics. Amongst these important characteristics is their longevity, access to top-tier managers, proven relationships with these managers, fund size, the ability to identify tomorrow's top-tier performers, reputation and reasonable fees and terms. It is decidedly an art, not a science, but one that is very attainable.

Most FOFs have been raised since 1995. Given the disparity of private equity returns across upper quartile managers versus the mean and/or lower quartile managers, it is crucial that the FOF have access to the best managers, and be selective when structuring a portfolio of underlying funds. FOFs that seek size (for the sake of fees) tend to be forced into investing in too many funds, including those without an adequate track record. A friend of ours likens this to the old hot dog analogy…the best have no "fillers or extenders," where taste gives way to mass. We want our clients to be exposed to the best, or "tastiest," with a limit on "bets," or "fillers." Fund size discipline is important. A $200 million FOF is in a position to be selective, investing in 15 to 20 underlying funds over, say, a 2-year period, and therefore not forced to make sub-top-tier investments. A $400 million FOF will probably commit to 30-40 underlying funds over a 3-to-4 year period. In every event, the FOF needs to be patient, waiting for the best managers to return to the market, and not pressing to put money to work.

The investment experience of the FOF management is critical. The GPs of the FOF should have years of market experience, a vested interest in the fund, interests aligned with the LPs, demonstrated manager selection capabilities, and proven relationships with and access to the top-tier managers.

❖ The Varying Characteristics of Funds of Funds

Funds of funds come with differing ownership. Some fund GPs are completely independent, some are sponsored by banks, and some are associated with diversified investment companies. We strongly favor the independent firms and selectively recommend some FOFs sponsored by diversified investment firms. Our concerns are mainly access to top-tier managers, the GPs' alignment of interest with the LPs, terms and conditions, and conflicts of interest.

Funds of funds also differ in their approach to diversification, both as to styles and vintage year commitments. Some concentrate on one stage, e.g., early or late-stage venture capital, large-cap buyout, small to mid-cap buyout, etc. Others are diversified across these and other asset classes. In addition to the US there are very high quality independent Asian, European and Israeli FOFs. For the initial investor, we will recommend starting a program to gain access to this range of styles, geographic and vintage year exposure. Many of the better FOFs will also have access to the same

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underlying managers. To avoid manager overlap it is important to consider the right mix of FOFs for the individual investor.

Fund of funds vary in their approach to fundraising. The variation is in the frequency with which they are in the market and the number of underlying funds to which each of their offerings will commit. Typically, the more often a FOF is in the market, the fewer underlying funds it will commit to and its vintage year coverage will be shorter. For those that raise funds less frequently, they will typically commit to a larger number of underlying funds over a greater number of vintage years. In either case, it is important to re-invest with the selected FOF as it comes back to the market in order to achieve the goals associated with diversification and access to top-tier managers as those managers return to the market.

As the private equity portfolio matures, we will recommend opportunistic commitments to more narrowly focused fund of funds to complement the diversification. Such commitments might focus on early stage venture capital, secondary investment offerings or small to mid-cap buyout, both in the US and elsewhere as a few examples. These extensions into the sub-sectors can provide exposure to areas that have historically provided higher returns than the norm without creating undue concentration.

The number of investor-friendly FOFs is extremely limited, particularly those that truly have access to the better private equity funds and who have the infrastructure to adequately perform due diligence and monitor and report performance. Many of these funds were typically started by groups of individuals that had had extensive experience working with individual funds either at banks, family offices or investing institutions, providing them with continuing access to, and knowledge about, the better and more established firms as well as promising emerging firms.

❖ Asia, Europe and Israel

With the maturation of private equity outside the United States and the weathering of a few cycles and several global dislocations, quality FOFs have emerged. Many years ago the smaller investor relied on their US fund of funds for access to non-US funds and several of them did and do a good job. However, there are now several Asia, Europe and Israel specific FOFs that are in position to extend access to top performing country specific funds that are very hard to discover and otherwise access.

Europe's economy is the largest in the world measured by GDP. Private equity opportunities are mainly in buyout and mainly resulting from the consequence of EEC integration generating a high level of cross-border merger and acquisition activity. Private equity firms also add value to smaller companies that wish to expand geographically, overcoming a variety of barriers such as language,

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legal and regulatory. Unlike the US where the 80/20 rule applies to large v. smaller buyout, in Europe it is much closer to 50/50. The market is still emerging. Europe's private equity investment activity 2004-2006 as a percent of its GDP was about half that of the US. As is the case in the US, returns are the highest with small and mid-cap funds, which are the most difficult to access.

Asia contains some of the fastest growing economies and rapidly emerging middle classes, offering a wide range of opportunities in private equity. As the first decade of the 2000s drew to a close Asia had emerged as a significant source of private capital for investment. From beginning to end, Asia had increased funds raised four-fold to levels competitive with the US and Europe. Moreover, it weathered the 1997 meltdown, 2000 bubble-burst, and the 2007 credit crisis in many ways better than other parts of the world. China is the engine of Asia but the private equity industry throughout the area is now well defined and mature. Broadly speaking, Asian private equity is not as dependent on debt as it is elsewhere. Opportunities vary from country to country. Buyout is most prevalent in Korea, Japan and Australia. Venture capital, or growth equity, dominates the opportunity in China and other parts of Asia (as it does in India). In nearly all cases there has been a rapid emergence of smaller independent quality funds that are generating the highest returns, and predictably, are the hardest to access. In the last decade several high quality, independent, but hard to access FOFs have emerged.

Israel private equity was traditionally a venture capital market and remains so today but with an emerging later stage/buyout component. Key drivers in private equity in Israel include outsized national expenditures on research and development and one of the most highly educated populations in the world. Again, access to smaller emerging funds is very difficult.

Other Issues

❖ Illiquidity and the Dreaded "J-Curve" Effect

Investors in private equity should have a relatively long investment horizon as returns on commitments do not materialize for several years and the penalty for abandoning a commitment is severe. Most fund partnerships have a twelve year life with the possibility of one to two year extensions thereafter – it's a long time to have your capital tied up if you've changed your mind about PE exposure.

Another reality of investing in private equity is that returns in the early years are almost always negative as money flows out to meet capital calls before returns materialize. This phenomenon is referred to as the "J-Curve" and can be illustrated graphically.

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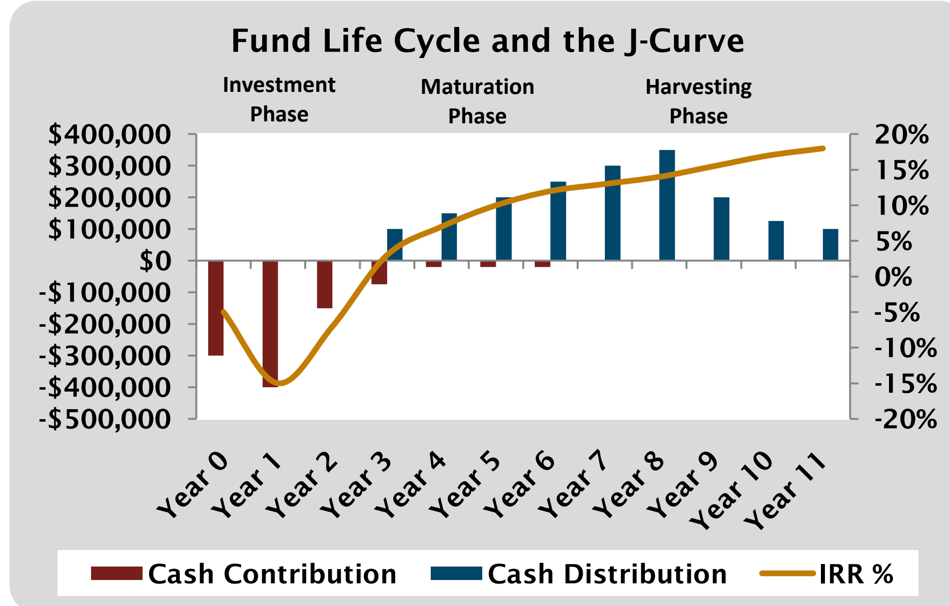

Note: Assumes $1MM commitment. Actual fund performance is not represented by this graph. For illustrative purposes only, as all numbers are hypothetical.

Investors who are new to private equity are often horrified by the sudden drop in value of their investment, but more experienced investors recognize that the J-Curve is almost inevitable. The J-Curve occurs for a number of reasons but the primary ones are these:

- Organizational expenses of private equity partnerships are deducted immediately, so no sooner does an investor meet the first capital call then his or her return immediately turns negative.[2]
- Smart general partners will identify bad investments quickly and write them down or off, while good investments will take time to pay off.
- Most of the better PE firms follow very conservative policies when writing investments up or down: bad developments cause immediate write-downs, while happy developments don't result in write-ups until some event occurs confirming the higher valuation.

[2] Another unhappy effect of the J-Curve is that fees, including startup fees, are applied against a smaller asset base, making already-high PE fees look even more outrageous. This situation will, however, correct itself in time.

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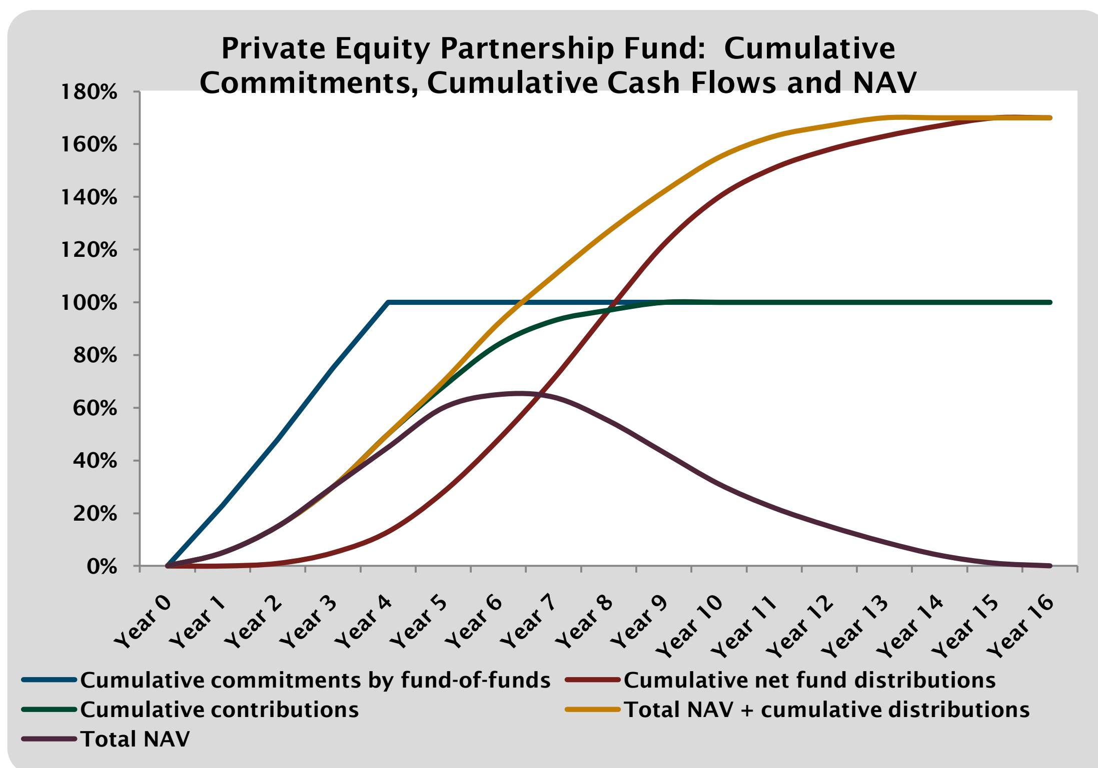
❖ Ramping Up to Your Target Allocation

Once again, we return to the art department. In private equity investing, and investing through FOFs, there is a considerable lag between commitments and actual investment of capital. Funds of funds commit to underlying private equity partnerships over a two-to- four year period. In turn, the underlying funds generally invest in operating companies over a three-to-seven year period. As a result, the investor in a fund of funds can expect that cash exposure to the asset class will rise rather slowly. Compounding this, realizations will start as early as the third year and accelerate in years 4-7. As a result and in most cases, less than 70% of a commitment will ever be outstanding. For this reason, we recommend carefully over-committing to the asset class and reinvesting over time. The graph below is a hypothetical view of cash flows and valuations of a blended fund of funds. It serves to show what might happen, based on the historic pattern of commitments, capital calls and returns with a well-diversified fund of funds:



Waterfall analysis is a quantitative approach to thinking about the requirements of repeated commitments to fund of funds in order to reach the target allocation and sustaining it. The likely pattern of cash flows to and from various funds of funds will help to determine how much and how frequently commitments should be made to achieve a target allocation and how long it will take to

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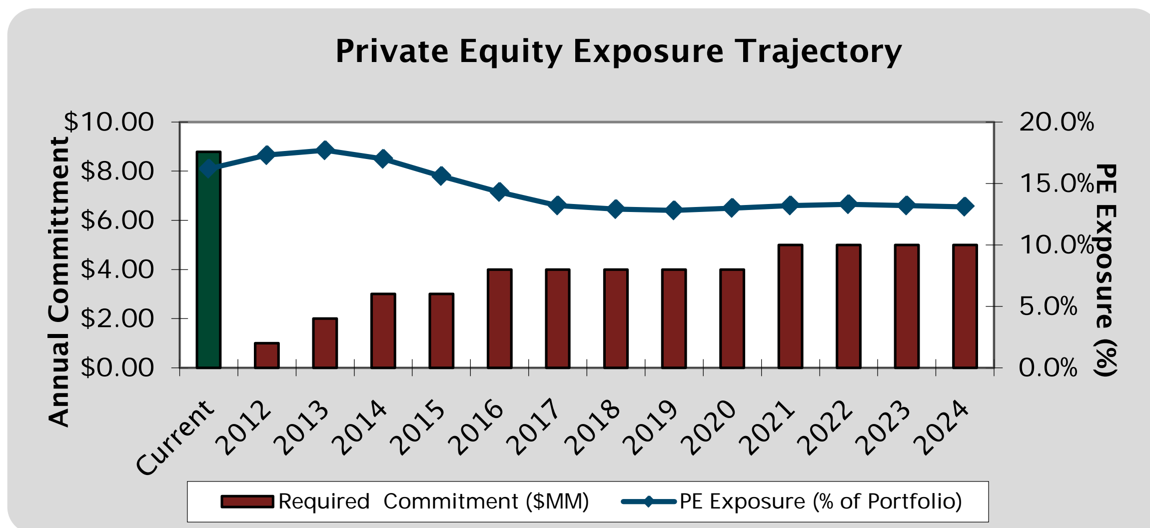
get to that target. Taking into consideration various commitment sizes also allows us to project the out of pocket exposure over time.

For example, the following graph shows the yearly required commitments for an investor with $160 million in assets to achieve a chosen allocation to private equity (15%.) The goal is to maintain a 15% exposure over time, despite unpredictable returns, varying capital call and distribution schedules, and a broader non-private equity portfolio that compounds over time.



Waterfall analysis is a useful tool that can pave the way for more detailed planning, such as potential ways to accomplish diversification by strategy, geography and vintage year. However, it is important to remember that a waterfall analysis is only an estimate. Therefore, a private equity program should be re-evaluated regularly throughout the forecast period as the actual investments materialize and market conditions change.

❖ Secondary Offerings

Secondary investing is the business of buying limited partnership interests from investors in funds prior to their maturity. There are several motivating interests for a limited partner to opt out of its commitment during the life of the fund. In some cases the investor's strategy or target allocation might change. The investor might become unable or unwilling to meet its commitment. Whatever the cause, the most likely solution is a sale to a third party, e.g., a secondary buyer. In most cases the general partner will control the sale. In the case of very large sales, an auction may take place among

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larger secondary funds. At this writing there are numerous multi-billion dollar secondary funds pursuing this strategy. We think that the auction process tends to drive up prices, thus diluting return potential. But there are a handful of smaller, focused, exclusively secondary funds that deal one-on-one with general partners for smaller interests that have produced high, counter-cyclical returns by raising and disbursing small funds aimed at "bite-sized" investments. The typical approach is to carefully evaluate each partnership interest based on the underlying company valuations, thereby lessening risk and accelerating returns. The advantage of these funds is that the money goes out faster, there is little or no "J-Curve" effect and returns occur earlier. Secondary investing, opportunistically, is an excellent enhancement to a diversified program. It can also serve to accelerate attaining an investor's target allocation to the asset class.

❖ Terms and Conditions

An investor's interest in a fund of funds is governed by a partnership agreement. While the list of important terms and conditions is lengthy and interrelated, there are several issues that rise to the top. First, is the fee structure fair? Management fees range from 50 to 100 basis points per annum. Often, there is a scaling down in the latter years of the life of the fund, recognizing the declining work load of the general partner. Second, is the general partner's interest aligned with that of the limited partners? This is generally reflected in the profit sharing structure between the two parties. Profit sharing, or the so-called "carry," is an important indicator of alignment of interests. While the carried interest will impact returns, it serves as an incentive for management to produce higher returns and has less of an impact on overall returns than the management fee. While it is true that funds of funds represent another layer of fees to the investor, we consider these fees to be more than offset by access to the top performers that the best funds of funds provide. Lastly, are there any potential conflicts of interest and are there remedies to control them?

❖ A Word about Conflicts of Interest

The best independent FOFs carefully avoid most conflicts of interest and provide access to the best underlying partnerships. At the other end of the spectrum are often FOFs sponsored by banks, where the offering memorandums normally articulate in elaborate detail the potential for conflicts of interest. These include the relationship that bank affiliates, such as investment banking arms, maintain with large buyout firms that they will be investing with, where they have fee relationships. The banks may have a lending or underwriting relationship with the operating companies in the banks' funds. Other affiliate funds of the bank may compete with the bank's FOF for investments in underlying funds and/or companies. The banks might be working with firms that will be bought from, or sold to, their own fund. Also, in the event that there is the potential for secondary

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investing, investors have to be concerned with these conflicts as they relate to affiliated advisors to the transaction and the potential that the seller is a related party. Further, since FOFs and secondary offerings are "blind pools", it is uncertain whether they will be dealing with their own offerings and/or clients. Finally, and perhaps of most concern, the general partner of the sponsored FOF is usually the ultimate parent firm whose interest lies with all of its subsidiaries, including competing funds, investment bankers, underwriters, asset managers, and the like. There is little or no protection for the limited partners in the partnership agreements.

Conclusion

Private equity investing is not without its challenges. However, long-term historic returns argue strongly for exposure to this asset class for most significant investors. The most important considerations are structure of the investment program (that is, vintage year, geography and stage diversification), access to top-tier performers, and knowledge about emerging private equity firms.

This paper was written by David R. Lovejoy, Managing Director of Greycourt & Co., Inc. Mr. Lovejoy can be reached by phone at 412.361.0100 or by email at dlovejoy@greycourt.com.

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