# California Public Employees' Retirement System (CalPERS) Private Equity Program (PE Program)

## Quarterly Report
## Executive Summary

### (As of December 31, 2013)

**Presentation Date: February 18, 2014**

# Quarterly Report

*December 31, 2013*

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## 1.0 Introduction

Private equity is a long-term asset class with performance results influenced by various factors. This report concentrates on several key exposures that contribute to performance results, including strategy, geography, structure and vintage year. In addition, the broad industry trends highlighted herein may affect future performance results.

## 1.2 Highlights of Program Activity

- The PE Program underperformed the Policy Benchmark over the latest one, three, five, and ten-year periods. Despite trailing the Policy Benchmark by 160 basis points over the latest ten-year period, **the PE Program's 13.2% average annual return as of December 31, 2013 is above CalPERS' expected return for the asset class of 12.1%[1] and well above the actuarial rate of return**.

- As has been noted in previous quarterly reports, including a public market index in the PE Program Policy Benchmark continues to result in questions about comparable performance. Most private equity investors use this type of benchmark and the industry is attempting to develop an alternative that will be more readily understood and acceptable. **In the interim, generally expect private equity to underperform rising public equity markets and outperform falling ones.**

- **The PE Program has been net cash flow positive (i.e., distributions received exceeded capital contributions made) over the past three years.** Over the latest three year period ending December 31, 2013, the PE Program has received \$24.7 billion in distributions while contributing \$11.0 billion, resulting in a positive net cash flow of \$13.8 billion. The PE Program has received \$6.9 billion in net cash flows (\$9.8 billion of distributions less \$2.9 billion of contributions) over the latest one-year period ending December 31, 2013.

- The **Buyout strategy continues to be the largest proportion of the PE Program** at **62%**, and was the largest contributor to performance over the latest three-year period due to valuation increases across the strategy. The PE Program's buyout exposure posted a three-year return of 14.7% as of December 31, 2013. Strategy allocations are within target ranges.

- The **United States, representing the largest geographic exposure of the portfolio at 75%, had the most significant impact on performance** results over the latest three-year period. As of December 31, 2013, the PE Program's domestic exposure generated a 15.9% three-year return compared to an 11.7% return for the PE Program's international-developed world exposure.

- **Partnerships, representing the largest type of investment vehicle in the portfolio, had the most significant impact on performance** results over the past three years posting a 15.5% average annual return as of December 31, 2013.

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[1] Source: 2010 ALM Workshop CMA

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- An analysis of the existing unfunded commitments shows that the **PE Program's general partners have significant "dry powder"** ($11.1 billion), almost a third of which is from the 2007-2008 vintage years and a material proportion is expected to be deployed within the next several years.

- Although the PE Program is in its twenty-third year, the preponderance of value and performance are attributable to **commitments made in the last ten years**. More specifically, commitments made in the 2006-2008 vintage years currently represent approximately 74% of aggregate value.

- **The PE Program's five largest general partner relationships represent approximately 35% of total exposure**, which is defined as market value plus unfunded commitments. Amongst these five firms, capital is allocated across more than 80 investments (partnerships and direct investments), targeting multiple strategies and geographies.

### 1.3 Industry Trends

- **Fundraising activity continued to increase in 2013.** Approximately $217 billion of commitments were raised domestically in the full calendar year of 2013, with buyouts continuing to represent the largest proportion of capital raised. This exceeds the full calendar year 2012 commitment amount of $189 billion. The market continues to be bifurcated, resulting in the most attractive funds becoming over-subscribed, with the remainder continuing to struggle in an otherwise challenging environment.

- **Announced U.S. buyout deal volume exhibited an increase in Q4 2013 from the prior quarter.** Total announced U.S. buyout deal volume was $55.1 billion in Q4 2013, up from $46.5 billion in the third quarter. Activity still remains well below the pre global financial peak of $595 billion for the 2007 calendar year but, at $200.3 billion in 2013, activity last year was the highest annual level among the past six years.

- **Risk metrics in the leveraged buyout market were mixed during the fourth quarter of 2013** as purchase price multiples increased and debt multiples decreased. The average purchase price multiple in the fourth quarter of 2013, at 9.7x, increased from 8.5x in the third quarter and was well above the ten-year average of 8.5x. Debt multiples for the fourth quarter of 2013 were at 5.1x, below the 5.3x level for the entire calendar year.

- **Venture capital investment activity increased slightly in the fourth quarter of 2013** and outpaced the annual investment activity in 2012. Approximately $29.4 billion was invested across 3,995 companies in 2013 which exceeded the $27.3 billion invested across 3,858 companies in 2012. Approximately $29.7 billion was invested across 4,001 companies in 2011.

- **Exit activity for venture capital investments continued to increase in the fourth quarter of 2013.** The number of merger and acquisition (M&A) transactions increased in the fourth quarter of 2013, but the aggregate annual level was below the prior three years. The initial public offering (IPO) market also exhibited an increase in the fourth quarter of 2013 as 38 venture-backed companies went public, raising $5.4 billion. Excluding the second 2012 quarter spike due to Facebook, the fourth quarter represented the highest quarterly value generation since the second quarter of 2000.

- **The outlook for distressed debt investment strategies continues to be mixed.** Debt pricing remains near par (according to the Leveraged Loan Index produced by the Loan Syndications and Trading Association), minimizing the near-term opportunity set for trading strategies. The magnitude of debt that was “amended and extended” during the crisis, pushed out the maturity dates and subsequently reduced the perceived near-term opportunity set for debt-for-control strategies.

## 2.0 PE Program Performance Overview

### 2.1 Overall Private Equity Program Performance

The PE Program underperformed the Policy Benchmark over the latest one, three, five and ten-year periods. Despite posting a very strong 19.1% return, above long-term expectations for the asset class, the PE Program underperformed the Policy Benchmark by 5.0% over the latest year. The PE Program Policy Benchmark, which is a blend of U.S. and global public equity markets, posted a one-year return of 24.1%, well above long-term return expectations. The strong absolute three-year returns for the PE Program and the Policy Benchmark exhibit the continued recovery from the economic crisis in late 2008/early 2009, while the PE Program underperformed by 2.9%. The absolute five-year return for the PE Program now reflects performance after Q4 2008, which captured the severe write-downs and value declines that applied to holdings just after the Lehman bankruptcy and amidst material market turmoil of the fourth quarter of 2008. The Custom Young Fund Index, a benchmark utilized until July 2009, did not reflect the public market declines entering the crisis. Subsequent to the crisis, the benchmark changed to a public equity oriented benchmark as public market valuations exhibited a greater rebound despite the PE Program's holdings being marked to market. The PE Program has posted a return above the expected return for the asset class and above the actuarial rate of return over the latest ten-year period, despite trailing the Policy Benchmark by 160 basis points.

**Performance vs. Policy Benchmarks**

| | 1 Year | 3 Year | 5 Year | 10 Year |
|---|---|---|---|---|
| **CalPERS' PE Program[2]** | **19.1%** | **14.5%** | **11.4%** | **13.2%** |
| *PE Program Policy Benchmark[3]* | *24.1%* | *17.4%* | *15.9%* | *14.8%* |
| **Excess Return** *v. Policy Benchmark* | (5.0%) | (2.9%) | (4.5%) | (1.6%) |

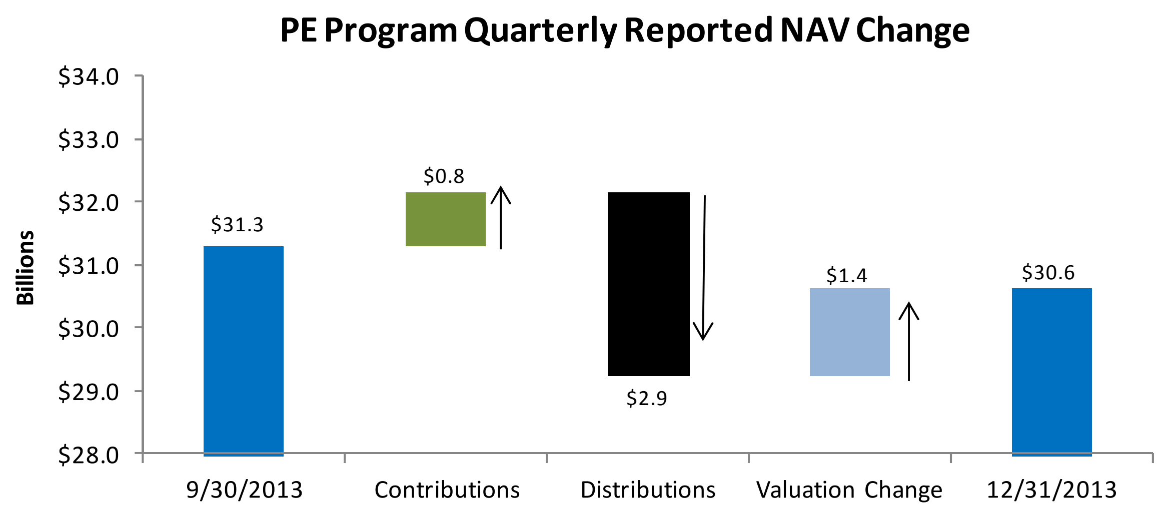
Source: Wilshire Associates

[2] The net asset value of CalPERS' PE Program portfolio is lagged one quarter with adjustments for current cash flows through the reporting period

[3] Currently equals (67% FTSE US TMI + 33% FTSE AW x-US TMI) + 3% 1-quarter lagged from and since September 2011; the Wilshire 2500 ex-tob + 3% since July 2009; previous periods for the PE Program Policy Index are linked historically to the Custom Young Fund Index, the PE Program's prior benchmark. The Custom Young Fund Index was composed of private equity holdings where write downs lagged the public markets declines in the reporting period.

## 2.2 Net Asset Value Change

At the end of 2013, the PE Program value declined slightly from the prior quarter of $31.3 billion as distributions materially exceeded contributions over the quarter. Approximately $0.8 billion of capital was contributed to underlying partnerships during the quarter while $2.9 billion was distributed (representing over 9% of quarter-end market value). The PE Program holdings exhibited unrealized appreciation of approximately $1.4 billion resulting in an aggregate valuation of $30.6 billion as of December 31, 2013.



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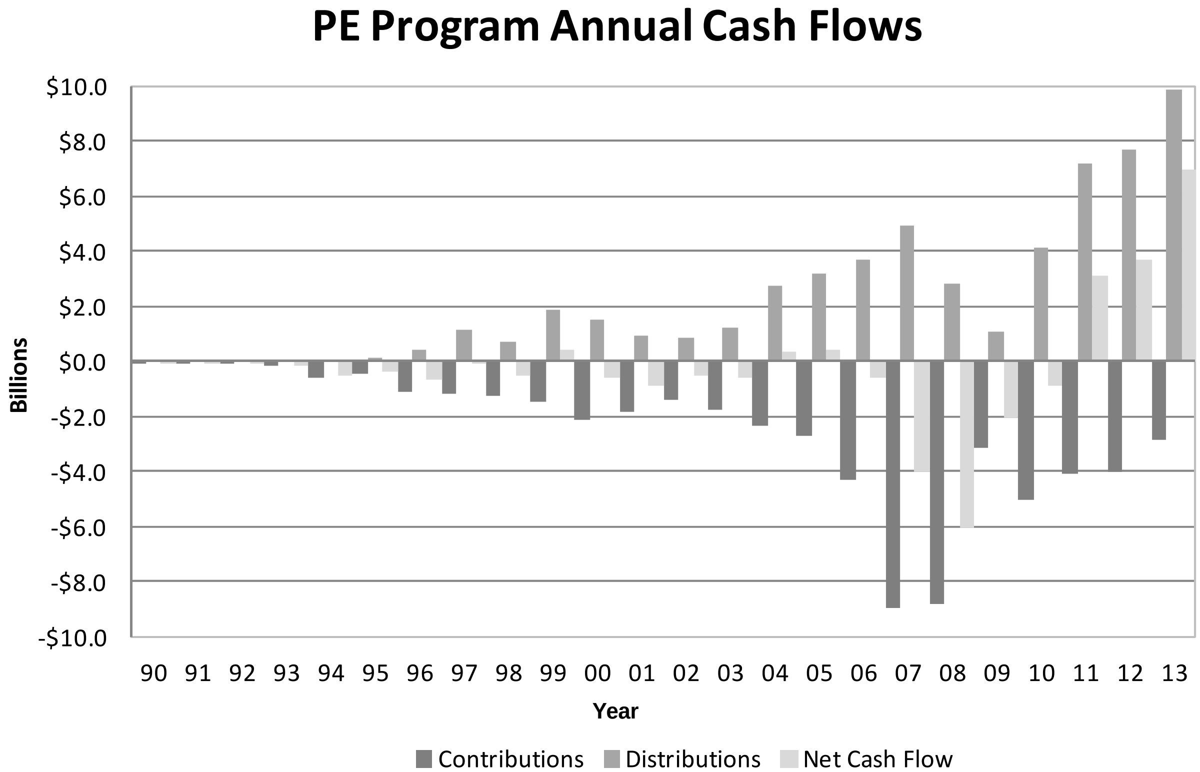
### 2.3 Portfolio Cash Flows

**The PE Program's net cash flow was positive (i.e., distributions exceeded capital contributions)** during 2013 as well as 2012 and 2011. Over the last three years, the PE Program has received $24.7 billion in distributions while contributing $11.0 billion, resulting in a positive net cash flow of $13.7 billion. Distribution activity has been high due to more friendly credit markets, material utilization of the dividend recap, and greater use of the IPO market. In addition, the PE Program's sales of holdings on the secondary market during the 2012 calendar year and proceeds received when investments in Apollo Global Management and The Carlyle Group were monetized in 2013, generated distribution activity and contributed to the positive net cash flows.




Source: Private Edge, PCA

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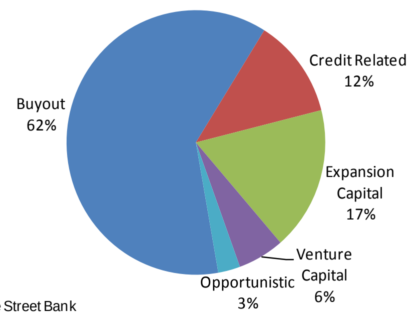
## 2.4 Portfolio Strategy Composition and Performance

Strategy distribution reflects the markets that the PE Program has determined will enable it to produce the expected return imbedded in the Investment Committee's asset allocation. The following charts portray exposure by net asset value (NAV). The **Buyout strategy continues to be the largest proportion** of the PE Program at 62%, up from 61% the prior quarter. **Strategy allocations are within target ranges.**

**PE Program NAV by Strategy: $30.6 B**



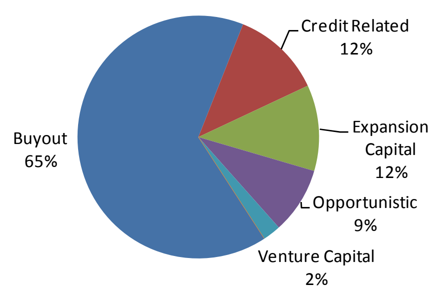

Source: State Street Bank

**Target Strategy Allocations**

| Strategy | Target | Range | Actual |
|---|---|---|---|
| Buyouts | 60% | 50%-70% | 62% |
| Credit Related | 15% | 10%-25% | 12% |
| Venture Capital | 1% | 0%-7% | 6% |
| Growth/Expansion | 15% | 5%-20% | 17% |
| Opportunistic | 10% | 0%-15% | 3% |

Strategy-wise, Buyouts represent the greatest proportion of the PE Program's unfunded commitments and will therefore continue to be its largest exposure prospectively.

**PE Program Unfunded Commitments by Strategy: $11.1 B**




Source: State Street Bank, Private Edge, PCA

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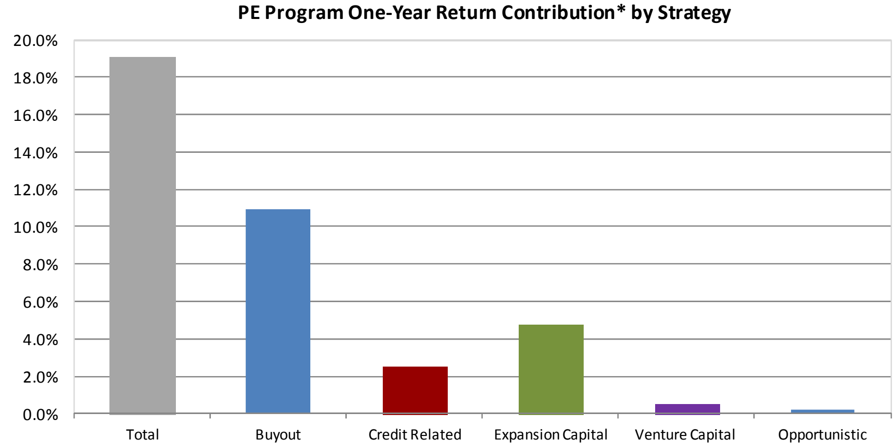
All major strategies of the PE Program contributed positive results over the last twelve months. **Buyouts were the largest contributor to performance** as the strategy continued to experience valuation increases. Expansion Capital, representing 17% of the Program, was the second largest contributor to results for the year followed by Credit Related.




*Sector return weighted by proportion of NAV.
Source: State Street Bank, PCA

Over the most recent three-year period, the PE Program posted a 14.5% average annual return. The Buyout strategy (with a 14.6% return) was a large factor in generating returns over the last three years due to its significant allocation in the PE Program. The Credit Related and Expansion Capital strategies were also large contributors, posting strong returns of 18.8% and 13.9%, respectively, over the same time period. The five-year results improved dramatically this quarter as this time period now spans from valuation lows at the depth of the economic crisis through the continued recovery. The Buyout strategy has generated attractive results over the longer ten-year period, posting an average annual return of 17.7%.

**Performance Summary: by strategy**

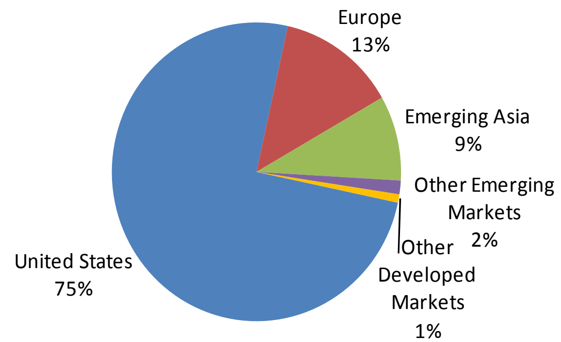
| | 1 Year | 3 Year | 5 Year | 10 Year |
|---|---|---|---|---|
| **PE Program** | **19.1%** | **14.5%** | **11.4%** | **13.2%** |
| *Buyout* | *17.9%* | *14.6%* | *10.4%* | 17.7% |
| *Credit Related* | *20.9%* | *18.8%* | *17.7%* | *15.6%* |
| *Expansion Capital* | *27.4%* | *13.9%* | *12.7%* | *8.8%* |
| *Venture Capital* | *8.4%* | *8.0%* | *2.8%* | *5.0%* |
| *Opportunistic* | *7.0%* | *9.5%* | *8.8%* | *6.1%* |

Source: State Street Bank

### 2.5 Portfolio Geographic Composition and Performance

The PE Program, like CalPERS' other asset classes, invests globally. Approximately **75% of the PE Program's NAV is inside of the United States** (based on the location of the investment firm) with 14% invested in developed markets (primarily Europe at 13%) and 11% in emerging markets (primarily Asia at 9%).

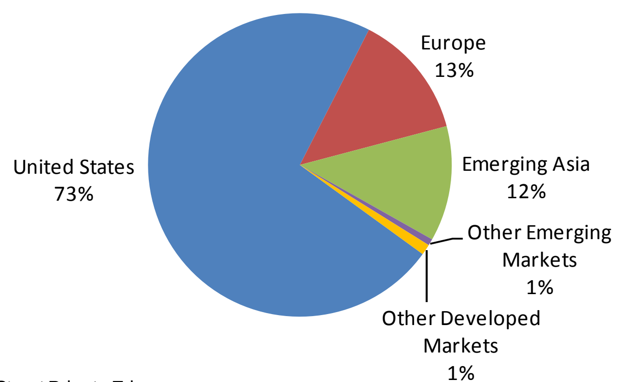
**PE Program NAV by Geography: $30.6 B**




Source: State Street Bank, PCA

The United States is expected to receive 73% of remaining unfunded commitments, followed by Europe at 13% and emerging Asia at 12%.

**PE Program Unfunded Commitments by Geography: $11.1 B**




Source: State Street Private Edge

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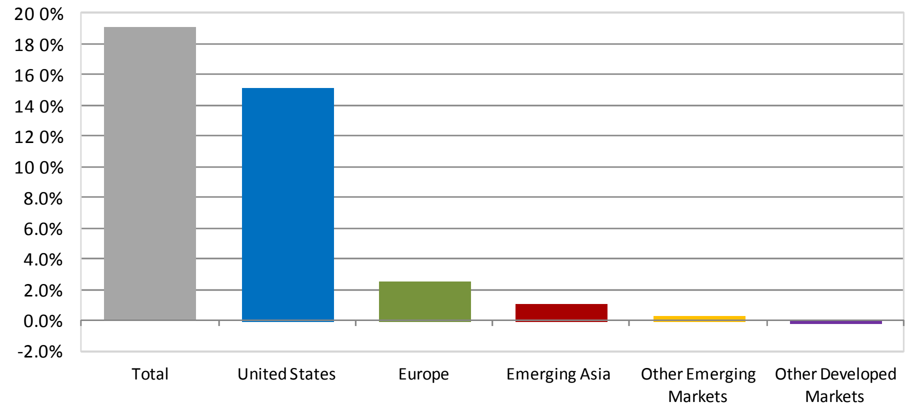
Performance results were positive across the major geographic sectors except for Other Developed Markets (primarily Developed Asia). The **United States, representing the largest exposure of the portfolio, had the most significant positive impact on performance** results over the past year. Europe, the second largest exposure, generated positive results over the latest year but had a much smaller contribution to performance than the domestic holdings and was followed by Emerging Asia.

**PE Program One-Year Return Contribution* by Geography**




* Geographic return weighted by proportion of NAV.
Source: State Street Bank, PCA

Over the most recent three-year period, the PE Program's United States exposure was the largest contributor to performance as the overall Program posted a 14.5% return. The PE Program's U.S. exposure posted an average annual return of 15.9% over the past three-year period. The PE Program's international developed markets exposure posted an 11.7% average annual return over this period while emerging markets returned 9.6%. The U.S. has historically represented the largest geographic component of the Program but its prominence has decreased over recent years with the globalization of the portfolio. The U.S. exposure posted average annual returns of 12.8% and 12.9% over the latest five-year and ten-year periods, respectively.

**Performance Summary: by geography**[4]

| | 1 Year | 3 Year | 5 Year | 10 Year |
|---|---|---|---|---|
| **PE Program** | **19.1%** | **14.5%** | **11.4%** | **13.2%** |
| *United States* | *20.3%* | *15.9%* | *12.8%* | 12.9% |
| *International- Developed World* | *17.5%* | *11.7%* | *4.2%* | *16.3%* |
| *International- Emerging Markets* | *12.3%* | *9.6%* | *10.4%* | *13.9%* |

Source: State Street Bank

[4] Currency exposure for the non–U.S.-dollar denominated portion of the PE Program is managed by CalPERS' fixed income group.

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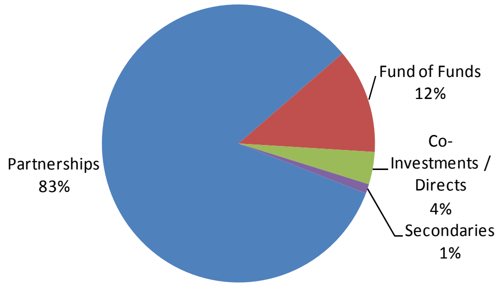
## 2.6 Portfolio Structure Composition and Performance

The PE Program has been constructed using multiple investment structures. Approximately **83% of the PE Program's NAV is invested in Partnership structures,** with Fund of Funds representing an additional 12%, followed by Co-Investments / Directs at 4% and secondaries at 1%.

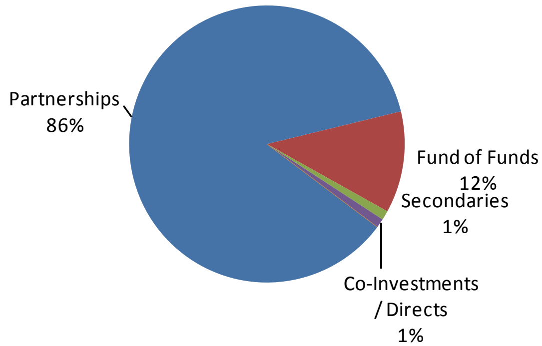
**PE Program NAV by Structure: $30.6 B**




Source: State Street Bank

Partnerships are expected to receive the vast majority of unfunded commitments at 86%.

**PE Program Unfunded Commitments by Structure: $11.1 B**




Source: State Street Bank, Private Edge, PCA

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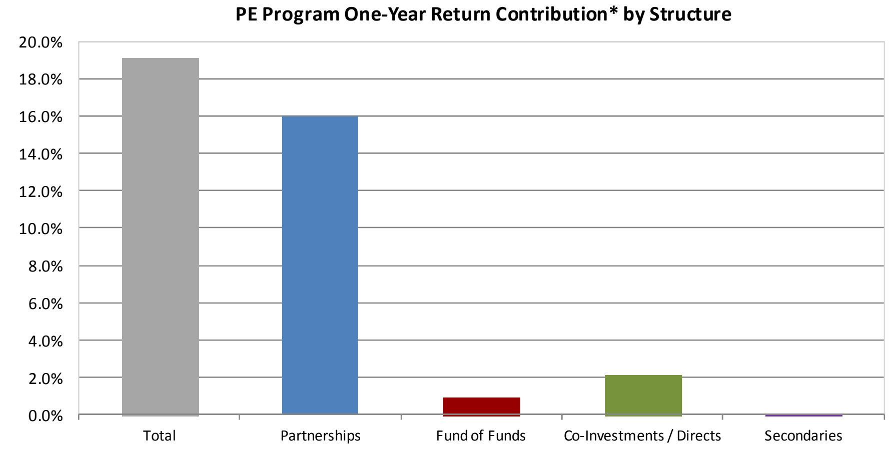
Performance results are net positive across all structures over the latest year. **Partnerships, representing the largest structure of the portfolio, had the most significant impact on performance** results. The PE Program's Co-Investments / Directs, despite representing only 4% of the Program, provided the second largest positive contribution over the latest year.




*Sector return weighted by proportion of NAV.
Source: State Street Bank, PCA

Over the most recent three-year period, the PE Program's Partnership investments were the largest contributors to performance as the overall Program posted a 14.5% return. The PE Program's Partnership investments, with the largest exposure, posted an average annual return of 15.5% over the past three-year period. Partnership investments have historically represented the largest component of the Program and have posted average annual returns of 12.1% and 13.8% over the latest five-year and ten-year periods, respectively. Co-Investments / Directs, while representing a small proportion of the overall portfolio and underperforming over the latest five-year period, posted a strong 21.1% average annual return over the latest ten-year period while Fund of Funds were a drag on performance with a 6.8% average annual return.

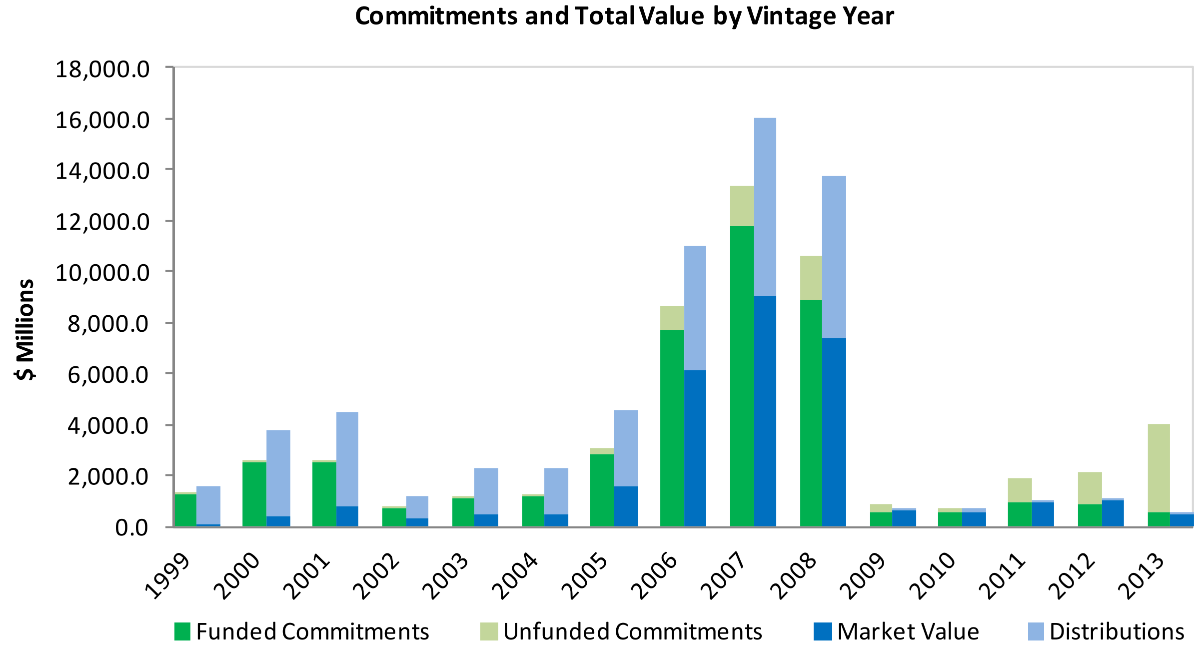
**Performance Summary: by structure**

| | 1 Year | 3 Year | 5 Year | 10 Year |
|---|---|---|---|---|
| **PE Program** | **19.1%** | **14.5%** | **11.4%** | **13.2%** |
| *Partnerships* | *19.4%* | *15.5%* | *12.1%* | 13.8% |
| *Fund of Funds* | *7.8%* | *9.2%* | *3.5%* | *6.8%* |
| *Co-Investment / Directs* | *58.2%* | *14.8%* | *20.1%* | *21.1%* |
| *Secondaries* | *8.0%* | *10.2%* | *6.7%* | *12.6%* |

Source: State Street Bank

## 2.7 Portfolio Vintage Year Composition and Performance

The PE Program currently has $56.6 billion in active commitments[5], $11.1 billion of unfunded commitments, and $30.6 billion in market value. PE Program new annual commitments were $900 million in 2009, $800 million in 2010, $1.9 billion in 2011, and $2.0 billion in 2012. In 2013, approximately $4.0 billion was committed reflecting a recovery in the private equity market space. The majority of active commitments and market value are currently represented by the 2006 to 2008 vintage years at $33.0 billion and $23.2 billion, respectively.




Source: Private Edge

[5] Active commitments only include commitments that have drawn down capital as of the reporting date.

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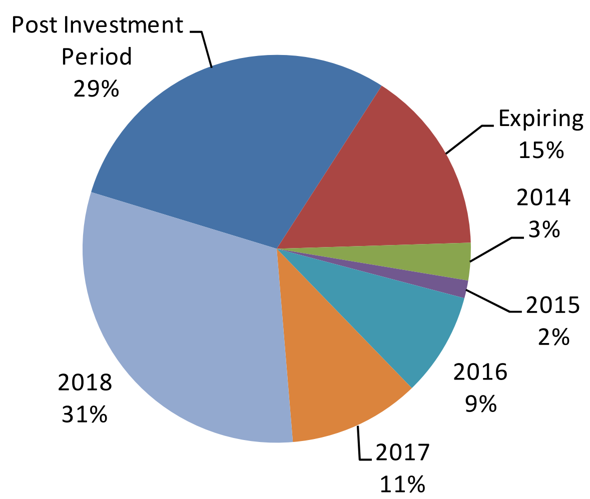
The **majority of unfunded commitments are expected to be deployed within the next several years** (utilizing the assumption that investment periods commonly terminate after five years and only follow-on investment activity would occur post investment period). However, the pace at which capital is drawn is primarily at the discretion of each general partner and may be called at any time, subject to any restrictions contained in the respective limited partnership agreements. In addition, a material amount of the unfunded commitments are relatively dated and are therefore past their investment period with much of this capital being utilized to fund management fees/expenses and follow-on transactions. The material exposure in the Post Investment Period category is due to the significant commitments ($22.0 billion) made in 2006 and 2007 vintage years.

**PE Program Unfunded Commitments by Maturity**




Source: State Street Bank, Private Edge, PCA

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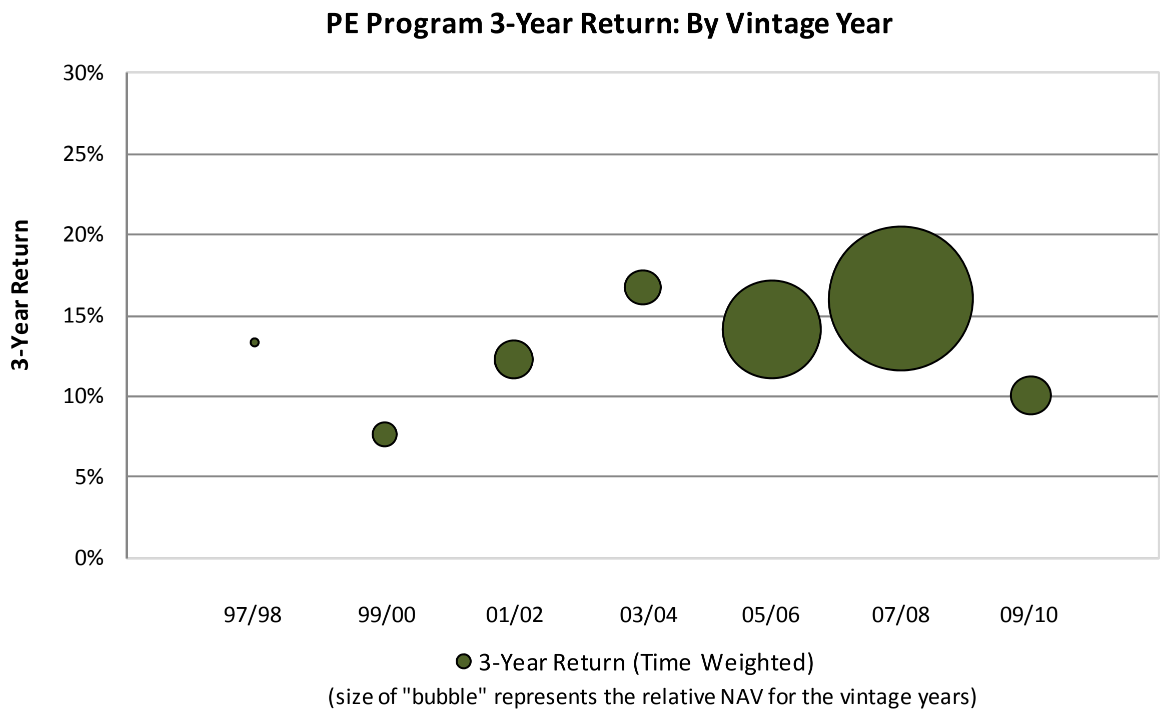
The following chart depicts the distribution of returns and net asset values by vintage years for the PE Program. Although the Program is in its twenty-third year, the preponderance of value (represented by the size of the "bubbles" below) and **performance results are being driven by commitments made in the last ten years**.




Source: State Street Bank, PCA

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## 2.8 Annual Commitment Activity and Manager Concentration

The PE Program committed $5.2 billion across 17 opportunities through year-end categorized as a 2013 vintage. All but two commitments in the 2013 calendar year to date represent existing relationships.

**PE Program Commitment Activity in 2013**

| Partnership/Firm | Commitment ($M) | Sector | Relationship |
|---|---|---|---|
| TowerBrook Investors IV | $380.0 | Buyout | Existing |
| Carlyle Partners VI | 547.0 | Buyout | Existing |
| GSO Capital Solutions II | 500.0 | Credit Related | Existing |
| KKR Asian Fund II | 575.0 | Buyout | Existing |
| Silver Lake Partners IV | 400.0 | Buyout | Existing |
| Triton Fund IV | 97.5 | Buyout | New |
| Six Co-Investments | 442.0 | Co-investment | Existing |
| Apollo Investment Fund VIII | 500.0 | Buyout | Existing |
| CVC Capital Partners VI | 649.9 | Buyout | Existing |
| Blackstone Tactical Opportunities Fund | 300.0 | Opportunistic | Existing |
| Cerberus CP Partners | 600.0 | Opportunistic | Existing |
| Trident VI | 250.0 | Buyout | New |

Source: CalPERS, PCA

The PE Program's five largest relationships, based on total exposure (defined as market value plus unfunded commitments) are listed below and represent approximately 35% of total exposure. Amongst these five firms, capital is allocated across more than 80 investments (partnerships and direct investments) and targets multiple strategies and geographies.

**Largest PE Program Relationships by Total Exposure**

| Firm | Investments | Total Exposure ($M) | % of Program |
|---|---|---|---|
| The Carlyle Group | 31 | $4,081 | 10% |
| Apollo Investment Management | 14 | 3,720 | 9% |
| Blackstone Group | 13 | 2,517 | 6% |
| TPG Capital | 16 | 2,434 | 6% |
| KKR and Company | 8 | 1,764 | 4% |

Source: State Street Bank, Private Edge, PCA

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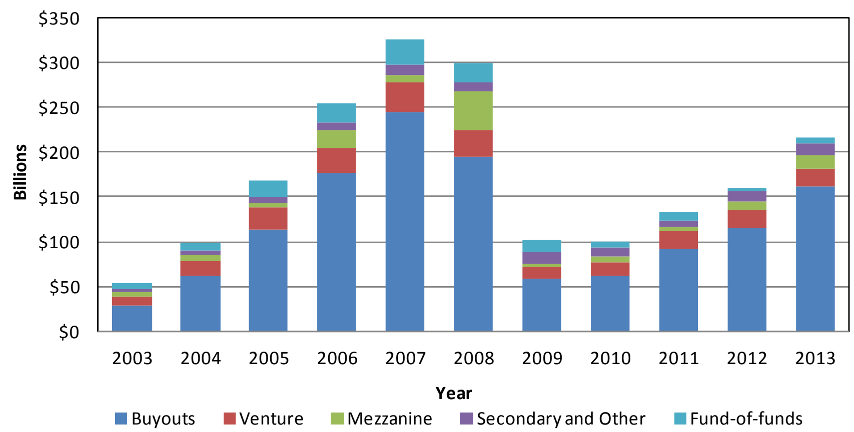
## 3.0 Private Equity Market Environment

### Fund Raising Trends

- During 2013, approximately $217 billion of commitments were raised. Commitments raised in 2013 exceeded the $189 million raised in the full calendar year of 2012.
- Buyouts led fundraising activities in 2013 raising $162 billion of commitments, followed by venture capital at $20 billion, mezzanine at $15 billion, secondary and "other" at $13 billion, and fund of funds at $8 billion.

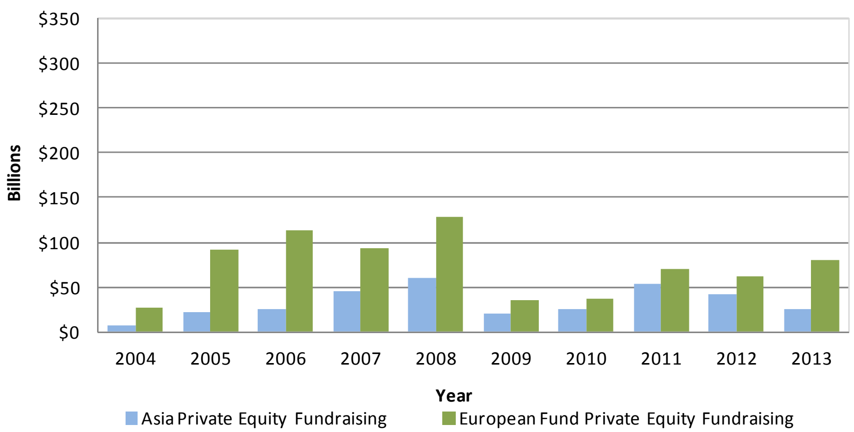
**Commitments to U.S. Private Equity Partnerships**




Source: *Private Equity Analyst* through December 2013

- Commitments to private equity partnerships outside of the U.S. have exhibited similar trends in fund raising activity over the past several years.
- Commitments to European funds have historically outpaced those to Asian private equity funds. This continued to be true in 2013 as commitments to Europe significantly outpaced those to Asia.

**Commitments to Non-U.S. Private Equity**




Source: Thomson Reuters

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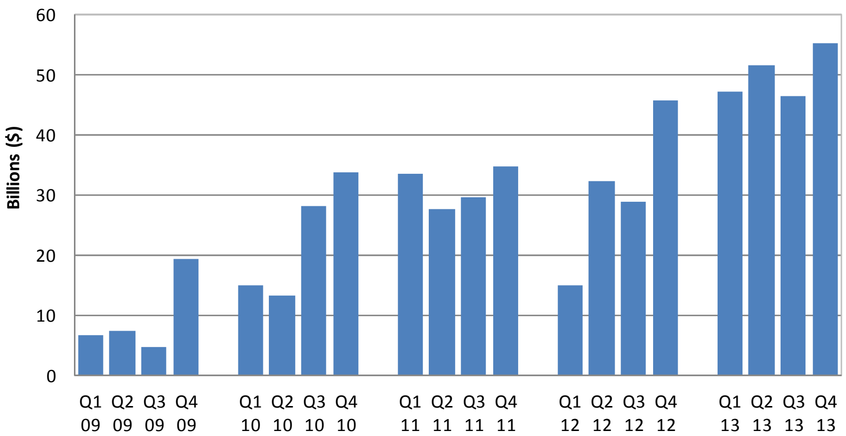
## U.S. Buyout Market Trends

- Total announced U.S. buyout deal volume was $55.1 billion in Q4 2013, up slightly from $46.5 billion in the third quarter. 2013 activity, at $200.3 billion, exhibited the highest annual deal volume since 2007.
- Q4 2013 saw standalone buyouts representing the largest proportion of transactions followed by add-on acquisitions and platform investments.
- Industrials exhibited the most transaction activity over the latest quarter, followed by the high technology industry, consumer products and services, and healthcare.

**Announced and Disclosed U.S. Quarterly LBO Deal Value***




* Total deal size (both equity and debt).
Source: *Thomson Reuters Buyouts*

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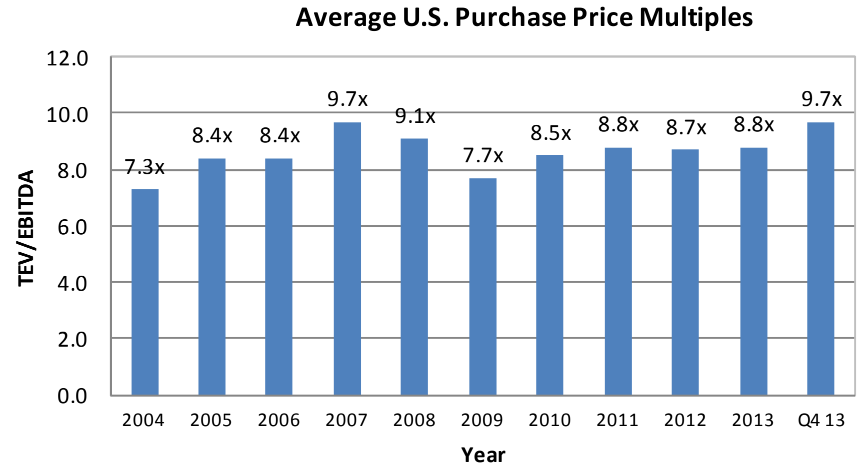
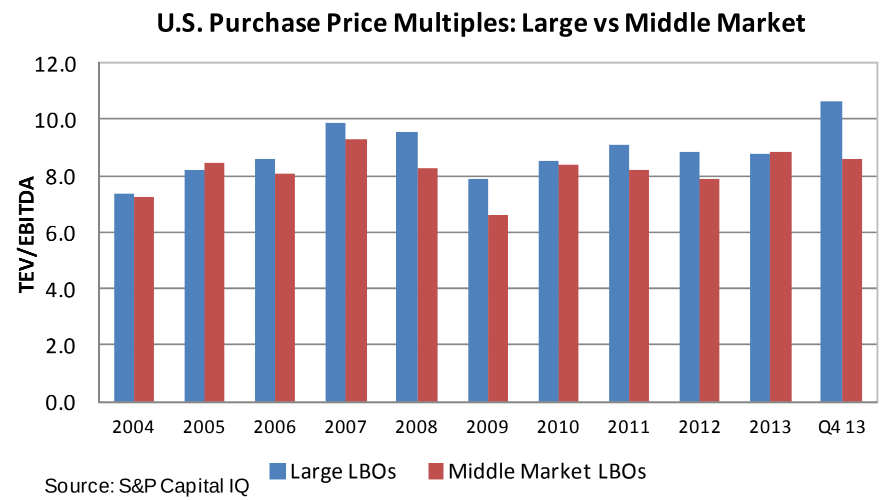
## U.S. Purchase Price Multiples

- Purchase price multiples (as represented by total enterprise value divided by earnings before interest, taxes, depreciation and amortization or EBITDA) have stabilized over the past three years after a recent low in 2009.
- The average purchase price multiple for 2013, at 8.8x, is above the ten-year average of 8.5x and well above the longer-term average purchase price multiple (dating back to 1997) at 7.9x.
- However, transactions in the fourth quarter of 2013 exhibited a significant increase in purchase price multiple. Continued monitoring is warranted to determine if this was due to year-end activity or the start of a longer trend.




Source: S&P Capital IQ

- Purchase price multiples for larger transactions (EBITDAs >$50 million and represented by the blue bars) have historically been higher than the purchase price multiples exhibited in the smaller and middle market (EBITDAs <$50 million and represented by the red bars).
- Post crisis focus shifted towards commitments to smaller/middle market opportunities, suggesting additional competition for deals that could influence the purchase price multiple in the smaller end of the market. In 2013, purchase price multiples for small/middle-market transactions slightly exceeded those for larger transactions.
- Given the rise in middle-market pricing, the average 2013 EBITDA multiple of 8.8x is above the ten-year average of 8.1x and materially above the longer-term average of 7.6x.




Source: S&P Capital IQ

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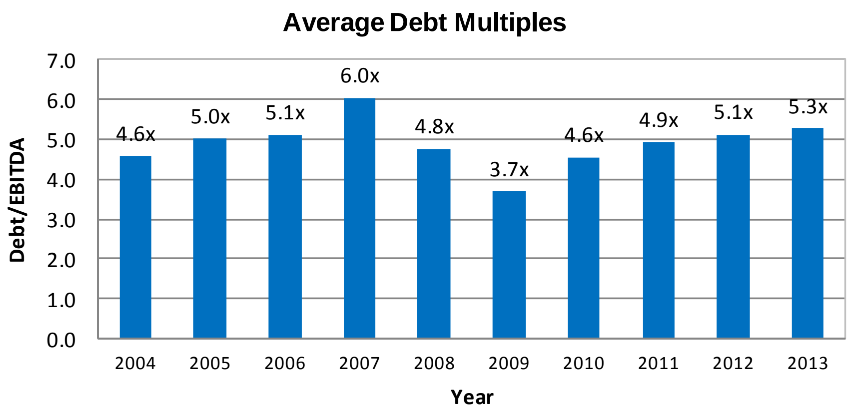
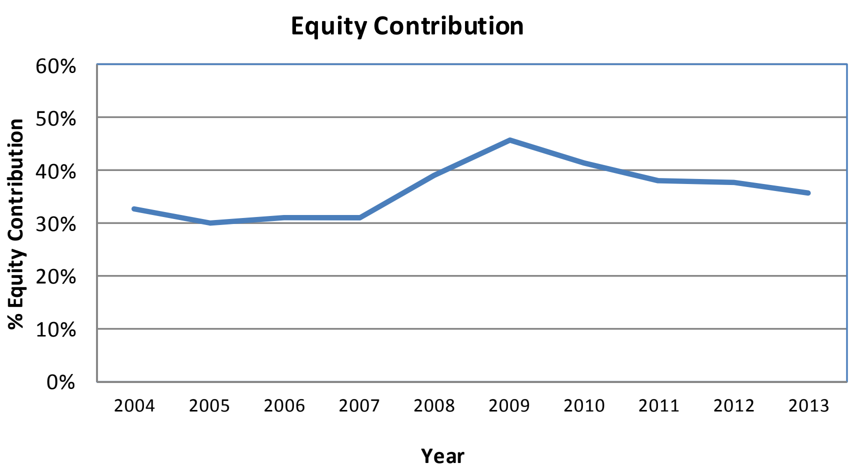
## Debt Multiples

- 2013 exhibited a slight increase in the average debt multiple to 5.3x.
- The average debt multiple increased from a low of 3.7x in 2009 as risk appeared to be increasing in buyout transactions.




Source: S&P Capital IQ

- The average equity contribution has declined from a high of 46% in 2009 and was at 36% in 2013.
- Lower equity contributions result in less conservative capital structures for transactions. The long-term impact on performance results remains uncertain.




Source: S&P Capital IQ

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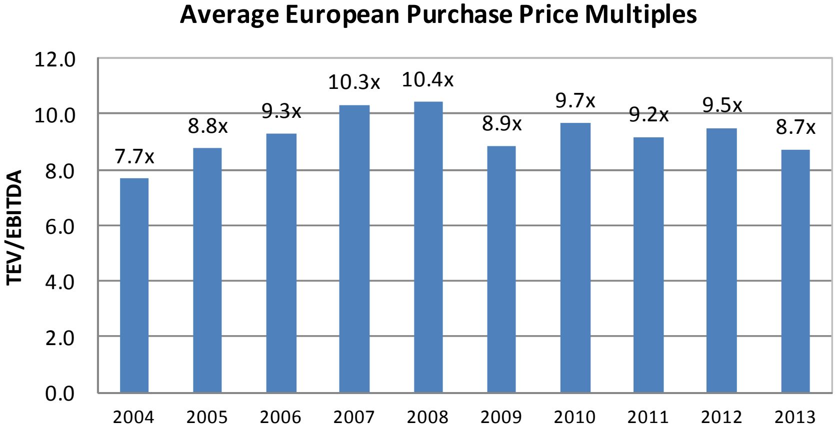
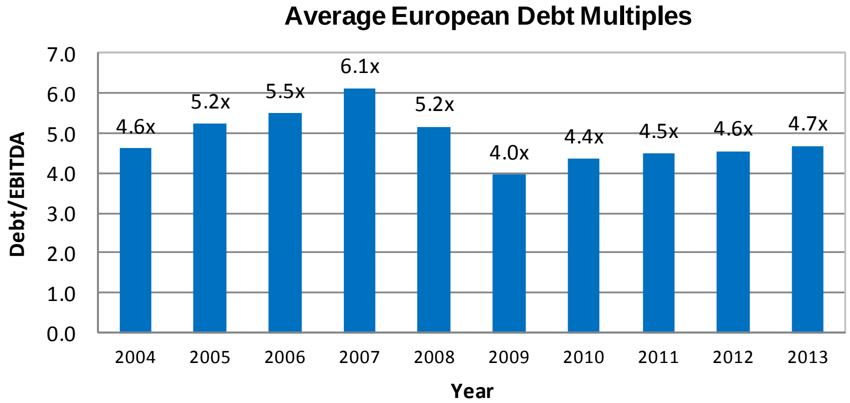
## European Purchase Price and Debt Multiples

- European purchase price multiples initially declined from their 2007/2008 peak to a near-term low in 2009, but rebounded quickly to 9.7x in 2010.
- The average purchase price multiple for 2013, at 8.7x, is below the ten-year average of 9.2x.




*Transaction size of €500M or more
Source: S&P Capital IQ

- As with the U.S. credit markets, 2007 reached a peak in average debt multiples. The dynamics of 2009 and 2010 resulted in more conservative capital structures for transactions completed.
- The average debt multiple for European LBO transactions increased from a low in 2009 of 4.0x, up to 4.7x 2013.




Source: S&P Capital IQ

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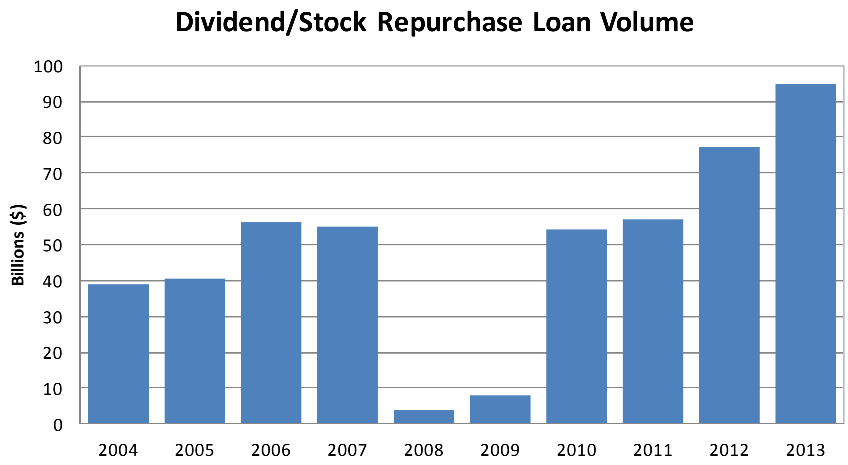
## Recaps and Stock Repurchases

- Dividend recaps result in increasing leverage, and ultimately risk, at the portfolio company level. The effect on future performance results by increasing leverage/risk remains uncertain.
- The private equity market saw a re-emergence of dividend recaps and stock repurchase activity in 2010, which had virtually disappeared post credit bubble.
- $94.9 billion in dividend recaps/stock repurchases occurred in 2013, exceeding the $77.3 billion that occurred in 2012. Much of this activity is believed to be recapitalizing transactions that occurred in the crisis with more conservative capital structures.




Source: S&P Capital IQ LCD, Bank of America Merrill Lynch

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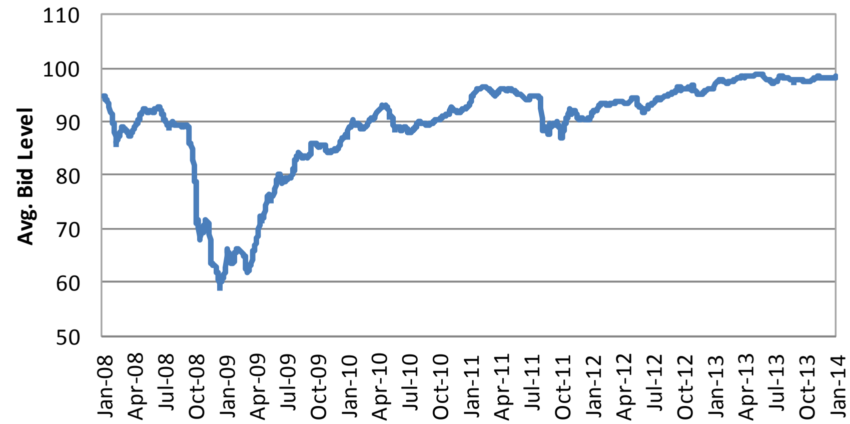
## Distressed Debt

- Interest in the leveraged loan market pushed the price of leveraged loans back towards par after lows seen in 2009, easing the opportunity set for trading strategies.
- Prices have continued a steady climb towards par since late 2011, limiting opportunities.

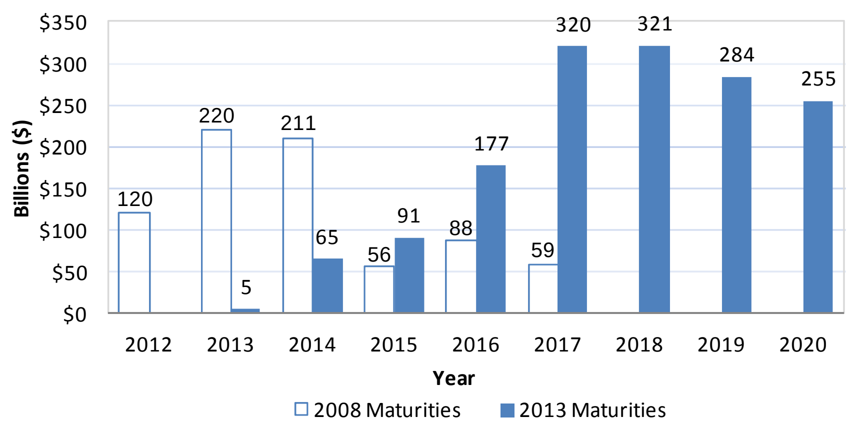
**Leveraged Loan Index**




Source: Loan Syndications and Trading Association (LSTA)

- The opportunity set for debt-for-control strategies remains unclear. There appears to be an attractive pending opportunity set over the longer-term. With the magnitude of debt that was "amended and extended" during the crisis, a significant volume of debt issues are now maturing several years out.

**Bond and Loan Maturities: 2008 vs 2013**




Source: LCD, Standard & Poors, Ares Management

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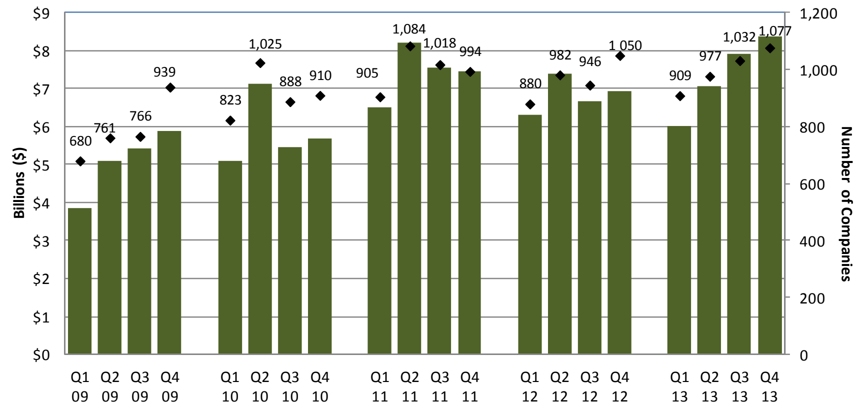
## U.S. Venture Capital Trends

- In the fourth quarter of 2013, 1,077 companies received approximately $8.4 billion of capital up from the third quarter of 2013 where 1,032 companies received $7.9 billion of capital.

- After year over year increases in venture capital investment activity from 2009 through 2011, 2012 exhibited a slight decrease of investment activity. Approximately $29.4 billion was invested across 3,995 transactions in 2013, up from 2012 levels and just slightly below 2011 activity.

- Despite lower investment activity, several dynamics in the industry suggest potential for attractive long-term results going forward, including: reduced institutional investor commitments to venture capital resulting in decreased competition for deals and less “me too” companies; ability for entrepreneurs to create new companies at a lower cost due to ongoing technological enhancements; embedded value within existing venture capital portfolios that have yet to be realized.

**Quarterly U.S. Venture Capital Deal Volume***




* Only includes equity portion of deal value.
Source: Thomson Reuters

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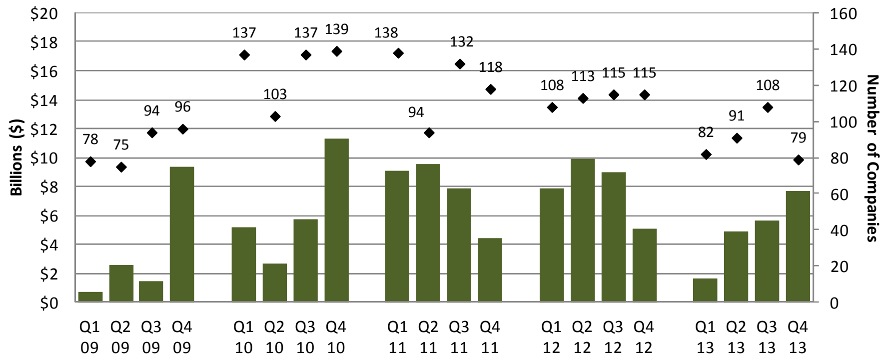
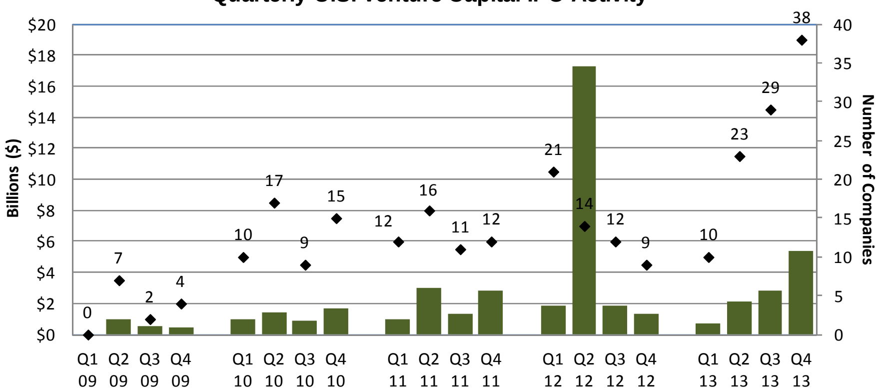
## Venture Capital Exit Environment

- M&A value for venture-backed companies increased in the fourth quarter of 2013, as 79 transactions were completed representing $7.7 billion of value.
- Exit opportunities for venture-backed companies had leveled off over the prior two years. In 2011, 482 venture-backed M&A transactions representing $30.9 billion in value were completed, slightly trailing the $31.8 billion in value transacted across 451 companies in 2012.
- In 2013, M&A levels were well below the prior two years as $19.8 billion was transacted across 360 companies. This decline could be reflective of increased IPO activity as venture capital firms may be holding on to their best IPO candidates rather than exiting via M&A.




Source: Thomson Reuters

- The fourth quarter of 2013 continued to exhibit an upward trend in IPO activity as 38 venture-backed companies went public, raising $5.4 billion after 29 companies went public in the third quarter raising $2.8 billion.
- Removing the Q2 2012 spike in IPO activity due to Facebook, the fourth quarter of 2013 represented the largest amount of capital raised since the second quarter of 2000.




Source: Thomson Reuters

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## Appendix 1: PE Program Relationships by Total Exposure (Market Value Plus Unfunded Commitments)

| Firm | Total Exposure ($M) | % of Program |
|---|---|---|
| CARLYLE GROUP | 4,081 | 10% |
| APOLLO MANAGEMENT | 3,720 | 9% |
| BLACKSTONE GROUP | 2,517 | 6% |
| TPG CAPITAL | 2,434 | 6% |
| KKR AND CO. | 1,764 | 4% |
| ADVENT INTERNATIONAL | 1,315 | 3% |
| SILVER LAKE | 1,293 | 3% |
| CERBERUS | 1,082 | 3% |
| CALIFORNIA EMERGING VENTURES | 1,042 | 3% |
| CVC CAPITAL PARTNERS | 1,024 | 2% |
| CREDIT SUISSE FUND INVESTMENT GR | 945 | 2% |
| 57 STARS | 914 | 2% |
| OAK HILL CAPITAL PARTNERS | 906 | 2% |
| THE YUCAIPA COMPANIES | 903 | 2% |
| TOWERBROOK CAPITAL PARTNERS | 861 | 2% |
| HELLMAN AND FRIEDMAN CAPITAL PAR | 825 | 2% |
| FIRST RESERVE | 734 | 2% |
| HEALTH EVOLUTION PARTNERS | 628 | 2% |
| BRIDGEPOINT CAPITAL | 578 | 1% |
| STANDARD LIFE | 569 | 1% |
| KMCP | 559 | 1% |
| ARES MANAGEMENT LLC | 553 | 1% |
| MHR | 500 | 1% |
| NEW MOUNTAIN CAPITAL LLC | 483 | 1% |
| RIVERSTONE LLC | 459 | 1% |
| GREEN EQUITY INVESTORS | 459 | 1% |
| ASIA ALTERNATIVE ASSETS | 438 | 1% |
| HAMILTON LANE | 426 | 1% |
| RIVERSTONE GLOBAL ENERGY | 414 | 1% |
| WLR RECOVERY | 410 | 1% |
| PROVIDENCE EQUITY PARTNERS | 372 | 1% |
| KHOSLA VENTURES | 340 | 1% |
| MADISON DEARBORN PARTNERS | 331 | 1% |
| COLLER CAPITAL | 315 | 1% |
| AVENUE CAPITAL PARTNERS | 315 | 1% |
| CAPITAL DYNAMICS | 297 | 1% |
| WELSH AND CARSON AND ANDERSON | 296 | 1% |

| Firm (continued) | Total Exposure ($M) | % of Program |
|---|---|---|
| PERMIRA | 289 | 1% |
| THL EQUITY ADVISORS | 288 | 1% |
| FRANCISCO PARTNERS | 260 | 1% |
| WAYZATA OPPORTUNITIES FUND | 253 | 1% |
| SAIF PARTNERS | 249 | 1% |
| ARCLIGHT | 246 | 1% |
| BIRCH HILL EQUITY PARTNERS | 243 | 1% |
| OAKTREE CAPITAL MANAGEMENT | 225 | 1% |
| THE RESOLUTE FUND | 220 | 1% |
| PALLADIUM | 204 | <1% |
| KPS | 194 | <1% |
| RIVERWOOD CAPITAL LLC | 187 | <1% |
| AFFINITY EQUITY PARTNERS | 182 | <1% |
| AUDAX GROUP | 165 | <1% |
| AISLING CAPITAL | 159 | <1% |
| LEVINE LEICHTMAN CAPITAL PARTNER | 157 | <1% |
| INSIGHT CAPITAL | 156 | <1% |
| CLESSIDRA CAPITAL | 154 | <1% |
| LIME ROCK | 151 | <1% |
| LION CAPITAL | 149 | <1% |
| POLISH ENTERPRISE | 147 | <1% |
| WELLSPRING CAPITAL MANAGEMENT | 135 | <1% |
| CLEARWATER CAPITAL | 134 | <1% |
| HUNTSMAN GAY CAPITAL | 132 | <1% |
| ESSEX WOODLANDS HEALTH VENTUR | 123 | <1% |
| TRITON PARTNERS | 102 | <1% |
| PAGASI | 101 | <1% |
| EM ALTERNATIVES | 100 | <1% |
| CLARUS VENTURES | 97 | <1% |
| GRANITE GLOBAL VENTURES | 96 | <1% |
| VANTAGEPOINT VENTURE PARTNERS | 90 | <1% |
| W CAPITAL PARTNERS | 87 | <1% |
| BARING | 87 | <1% |
| MAGNUM CAPITAL | 86 | <1% |
| SAGEVIEW CAPITAL LLC | 79 | <1% |
| RHONE PARTNERS | 75 | <1% |
| KLINE HAWKES CALIFORNIA | 67 | <1% |
| OTHER | 586 | 1% |



Source: State Street Bank, Private Edge, PCA

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