

## PRIVATE EQUITY OVERVIEW

The dramatic market decline in the 4<sup>th</sup> quarter has finally caught up with private equity. As can be seen in the table below, all private equity strategies show negative performance in the 4<sup>th</sup> quarter and over the one-year period, which should not be surprising, but in every case still outperformed listed indices. Somewhat more conservative write-downs from private equity managers may account for some of the “outperformance”. Given the weak market early in 2009, investors should not be surprised to see negative performance again in the 1<sup>st</sup> quarter. If there is a silver lining to the negative private equity performance, however, it is that it helps to match the value of public and private investments more closely, reducing the impact of the so-called “denominator effect”. Still, this is little consolation. The poor performance of both listed and private markets has additionally contributed to a general liquidity squeeze. Lower institutional portfolio values have made it more difficult for investors to generate cash to meet future expected capital calls, while the lack of distributions from private equity funds given the very poor exit environment has proved little help in this regard. As such, investors are rightly focused on liquidity. While it is possible that this experience could lead to more conservatism among institutional investors with respect to private investments, the long-term trend of increasing allocations to private equity and new entrants into the asset class should continue to increase on asset flows into private equity over the long-term, even if the current environment causes a temporary slowdown.

The difficult environment noted above has led to challenges in fundraising, across virtually all private equity strategies. Additionally, investment activity has slowed materially, reflecting a more difficult environment in which to invest (fewer sellers, less accommodative financing, etc.), and perhaps a somewhat more conservative attitude among GPs toward new investments in the current environment (pressure from LPs to reduce capital calls, maintaining higher reserves for follow-ons, waiting for a more certain investment environment). However, this crisis, both in the general economy and in the broader markets, will likely create interesting investment opportunities from which private equity managers will be well-positioned to take advantage. At a time of perhaps cyclically low earnings and valuations, and perhaps less competition for deals, now may be an attractive opportunity to commit to new funds, even though it may be more difficult to do so.

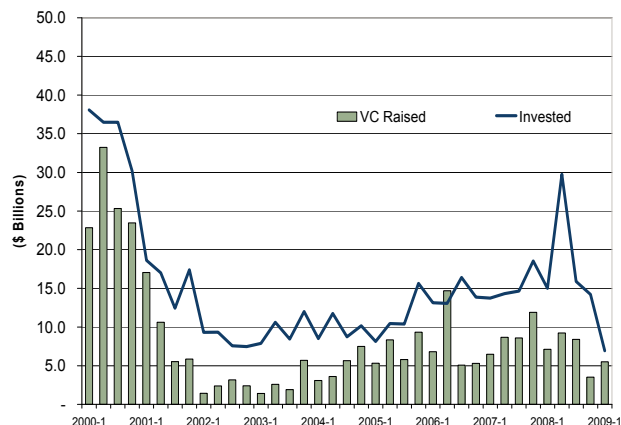
US Private Equity Performance Index (PEPI)  
Investment Horizon Performance through 12/31/2008

Fund Type	3 Mo	1 Yr	5 Yr	10 Yr	20 Yr
Early/Seed	(13.3)	(20.6)	3.7	36.0	21.8
Balanced	(19.4)	(26.9)	8.4	13.5	14.5
Later Stage	(8.0)	(6.8)	8.7	7.5	14.5
<b>All Venture</b>	<b>(14.8)</b>	<b>(20.9)</b>	<b>6.4</b>	<b>15.5</b>	<b>17.0</b>
Medium	(9.5)	(20.6)	11.3	7.9	11.3
Large	(8.9)	(9.6)	10.9	6.6	10.9
<b>All Buyouts</b>	<b>(15.9)</b>	<b>(23.9)</b>	<b>8.4</b>	<b>5.9</b>	<b>9.8</b>
<b>All P.E.</b>	<b>(15.9)</b>	<b>(23.6)</b>	<b>7.9</b>	<b>7.9</b>	<b>11.9</b>
NASDAQ	(24.4)	(40.0)	(4.0)	(2.7)	8.1
S & P 500	(21.9)	(37.0)	(2.2)	(1.4)	8.4

\*The PEPI is based on the latest quarterly statistics from Thomson Venture Economics. All returns are calculated by TVE from the underlying financial cash flows. Returns are net to investors after mgmt fees and carried interest.

Source: Thomson Venture Economics/NVCA, Stylus

US Venture Capital Activity



Source: Venture Economics

## VENTURE CAPITAL

- The 1<sup>st</sup> quarter of 2009 again proved difficult for venture capitalists, in a continuation of the weak environment from the latter part of 2008. Only forty-six venture firms raised funds in the quarter, essentially flat with the forty-seven that closed funds in the prior quarter, but down from the seventy-one in the prior year's 1<sup>st</sup> quarter. However, \$5.5 billion was raised in 1Q09, up from \$3.5 billion in the 4<sup>th</sup> quarter of 2008. While the last two quarters were among the weakest in terms of fundraising since the 2002-03 bursting of the tech bubble, venture fundraising is still meaningfully higher than was the case during that downturn, which was much more directly related to the technology and venture capital industries.
- Venture investment activity was much more directly impacted by the market weakness; \$6.9 billion was invested during the 1<sup>st</sup> quarter, down materially from the \$14.2 billion invested in the prior quarter. This is the lowest total invested in a quarter since the 1<sup>st</sup> quarter of 1998.
- The exit market remained essentially closed, and has been largely limited to M&A activity over the past several quarters. In fact, for the past six months, and in three of the past four quarters, there have been no venture-backed IPOs. There has been only one such IPO in the past year. The weakness is unprecedented as there are no recorded periods in which there were two quarters with no venture-backed IPO activity. In addition, the pipelines of IPO candidates has been deteriorating as there are only twenty-six venture-backed companies in registration with the SEC, while six companies recently withdrew from registration.
- Venture-backed M&A activity was also quite weak. Only fifty-nine venture-backed companies were acquired in the quarter with a disclosed deal value of \$645 million, down from the sixty-one in the prior quarter and down from the

## BUYOUTS

- Fundraising for buyout and mezzanine funds remained essentially flat relative to the prior quarter. \$17.8 billion was raised in the 1<sup>st</sup> quarter of 2009, up only marginally from the \$17.0 billion raised in the prior quarter, but down materially from the \$76.7 billion closed in the 1<sup>st</sup> quarter of 2008. Thirty-seven funds closed in the quarter, down from the forty-two and eighty that closed in the prior quarter and the 1<sup>st</sup> quarter of last year, respectively.
- New investment activity continues to be slow, particularly due to the less favorable financing markets. In addition, in some cases, LPs are pressuring GPs to not call capital in the near-term, so as to not exacerbate liquidity issues among LPs. Even secondary funds, which have generated much interest lately, are generally investing relatively slowly, as the spread between buyer and seller expectations remains wide. This phenomenon likely plays a meaningful role in the slow investment activity more broadly as well.
- On a related note, many buyout firms may be more concerned about the viability of, rather than the exit of, their portfolio investments over the near-term. With financing still challenging, and many buyouts completed near the height of the market with high debt loads, many firms may be focused on working with portfolio companies, at the expense of new investment activity, which may also be good for cash-strapped LPs.
- Exit market activity was weak during the quarter, similar to the environment for venture capital. There were no buyout-backed IPOs in the first quarter, and there were only four over the past twelve months. This is down dramatically from the sixty-six and forty buyout-backed IPOs in 2006 and 2007, respectively.
- M&A exit activity was weak as well. There were only fifteen acquisitions of buyout-backed companies in the 1<sup>st</sup> quarter, down from thirty-three in the prior quarter and down from forty in the first quarter of 2008. While deal value rose dramatically, to \$29.5 billion, up from \$2.2 billion in the prior quarter, this is due to the acquisition of Alltel by Verizon, which was announced in June of 2008, and accounted for \$28.1 billion of value. Excluding that single deal, M&A deal value was the lowest total since the 3<sup>rd</sup> quarter of 2003.

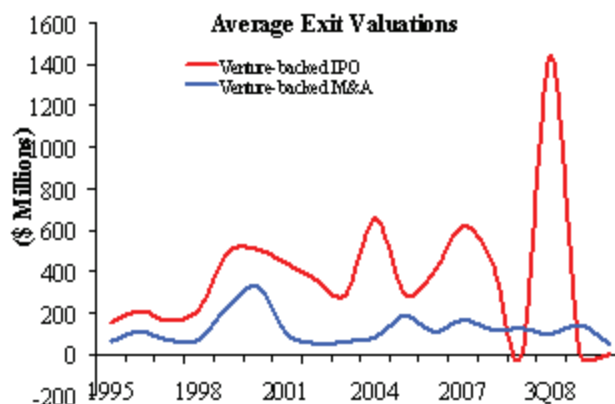
## OTHER

- While fundraising has been challenging across the board, certain strategies have had a better reception in the current market environment; secondaries, distressed and mezzanine in particular are anecdotally among the currently most popular investment strategies. These strategies attempt to take advantage of distress among holders of private equity assets, distress among companies, and distress in the financing markets, respectively.

### Venture Exit Analysis:

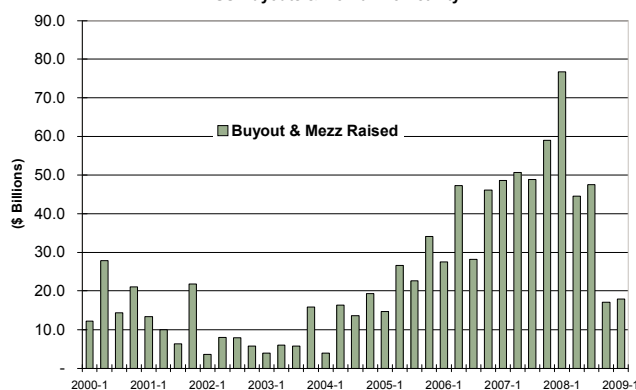
	# of Venture-Backed IPO's	Offer Amt (\$MM)	# of Venture-Backed M&A	Deal Value (\$MM)
2004	94	11,378	350	16,066
2005	57	4,485	371	35,640
2006	56	5,075	387	17,603
2007	86	10,326	372	29,092
2008	6	470	339	13,303
2Q08	0	0	84	3,293
3Q08	1	188	88	3,080
4Q08	0	0	61	2,386
1Q09	0	0	59	64.5

Source: Venture Economics



Source: Venture Economics

### US Buyouts & Mezzanine Activity



Source: Venture Economics

### Buyout Exit Analysis:

	# of Buyout-Backed IPO's	Offer Amt (\$MM)	# of Buyout-Backed M&A	Deal Value (\$MM)
2004	57	11,293	42	9,257
2005	67	15,764	97	22,672
2006	66	17,451	146	32,947
2007	40	9,627	178	46,955
2008	6	1,250	151	14,002
2Q08	2	357	41	2,324
3Q08	1	500	37	4,793
4Q08	1	126	33	2,247
1Q09	0	0	15	29,480

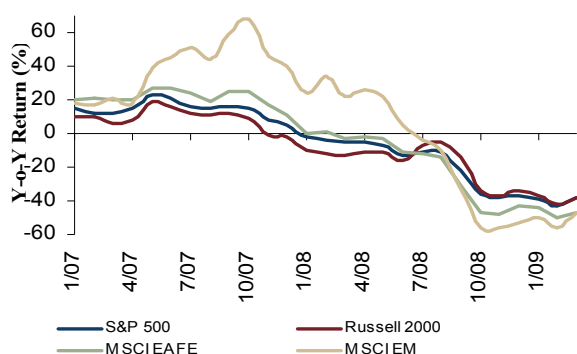
Source: Venture Economics

**HEDGE FUND OVERVIEW**

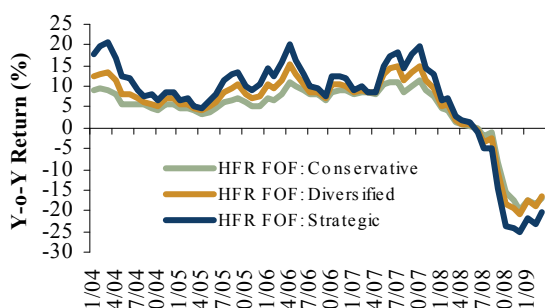
In the first two months of the first quarter equity and credit struggled but rebounded in March to help partially offset the losses. At the end of March 2009 the S&P 500 was down 11.01%, the MSCI EAFE (\$) was down 13.94%, and the MSCI Emerging Market Index was up 1.02%. For hedge funds the story was quite different, producing a positive return for the quarter after a year where hedge funds did not protect capital as well as investors would have thought. The HFR Weighted Composite Index was up 0.53% during the first quarter, with convertible arbitrage strategies leading the way after a dismal 2008. Convertible arbitrage was profitable due to increased activity in the secondary market and a surge in convertible buybacks, which helped bolster prices. In contrast, the weakest performing strategy during the quarter was macro, which had been the only positive performing strategy in 2008. Throughout the quarter many managers continued to raise cash for redemptions or in some cases margin calls, but it seems that the worst transpired back in the fourth quarter.

Hedge Funds of Funds also had a positive quarter, with the HFR FOF Diversified Index, the collection of broadly diversified funds of funds, up 1.06%. Funds included in the HFR FOF Conservative Index were up 0.40% for the quarter, while the more aggressive mixture of funds, those that typically emphasize equity long/short strategies and are included in the HFR FOF Strategic Index, were down 0.12% for the quarter. The differential in performance of various hedge fund of funds largely relates to how much exposure managers have to relative value and macro type strategies.

**World Equity Markets**

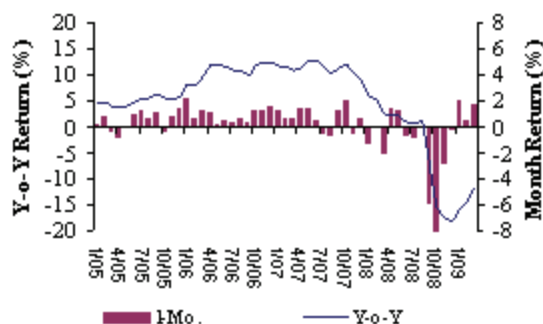


**Hedge Fund of Funds Indices**



Source: Hedge Fund Research, CSFB Tremont

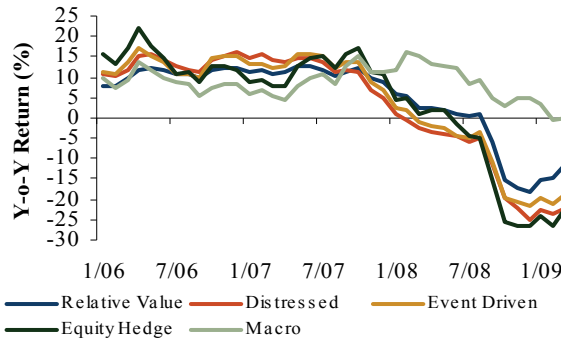
**HFR Relative Value Arbitrage**



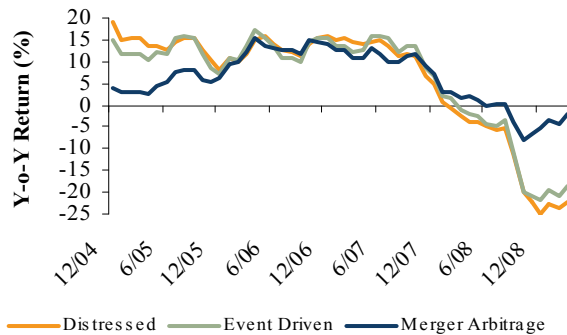
**NON-DIRECTIONAL STRATEGIES**

- The HFR Equity Market Neutral Index was down for the quarter, dropping 0.35%, but remains a top performing strategy year-over-year with a -6.09% return. Market neutral managers continued to be affected by risk aversion and high volatility but found some safe haven in long trades in the healthcare sector and short positions in financials, consumer and industrials. These sectors suffered from increased concerns over the deepening recession.
- Convertible arbitrage, as represented by the HFR Convertible Arbitrage Index, was the best performing strategy for the quarter (+12.45%) but is still down on a year-over-year basis (-20.50%). The strategy benefited from a rally in the convertible bond market as both investment grade and non-investment grade bonds rose above their lows reached in November 2008. There has been continued buying interest from companies repurchasing issues in the secondary market which has caused spreads to tighten. Profits were also largely attributed to bargain hunting causing an uptick in the values of secondary convertible issues. On the negative side, new issuance was thin during the quarter with many potential issuers concerned about issuing convertibles with depressed stock valuations. At this juncture, convertibles are viewed by some as cheap based on volatility and credit conditions.
- The HFR Relative Value Arbitrage Index was up 4.41% for the quarter and is down 11.46% for the one-year period. Over the quarter managers benefited from higher levels of volatility in the credit markets and generated gains through security selection.
- The HFR Fixed Income Index was up 4.39% for the quarter and is down 13.27% for the one-year period. The quarter's performance stemmed from a solid January (+2.02%) and March (+1.37%), as credit spreads tightened and signs of increased activity in high yield new issuance appeared. U.S. High Yield, as measured by the Merrill Lynch High Yield Master II Index, was up 5.02% for the quarter. Meanwhile, investment grade corporate credits were down during the quarter, with the Barclays Capital Corporate Index down 1.93%. High quality corporates suffered from the bleak economic outlook, and from investors moving into high yield and bank loans seeking higher yields.

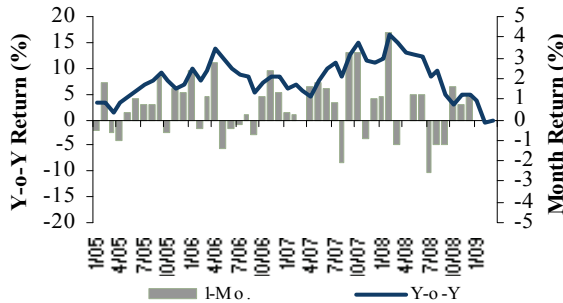
**HFR Strategy Returns**



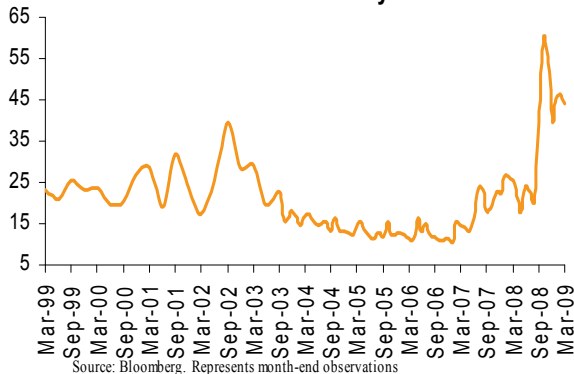
**HFR Event Strategy Returns**



**HFR Macro**



**VIX - CBOE SPX Volatility Index**



**EVENT DRIVEN STRATEGIES**

- The HFR Event Driven Index was up 0.51% for the quarter and is down 18.56% for the one-year period. Due to a lack of M&A activity and unattractive deal spreads, managers are getting their exposure on the credit side through bank loans, distressed corporate debt and mortgage-backed securities, which were profitable in the first quarter.
- The HFR Distressed Index was down slightly (-0.17%) during the quarter, and is down 22.30% for the year-over-year period after a horrible 2008. February was the main negative driver for the quarter as credit markets deteriorated with spreads widening and defaults increasing to 5.2%. Distressed managers have had trouble posting in positive performance, as they typically perform better after defaults have peaked. Moody's is forecasting default rates to peak at 14.8% by the end of the year. In addition, managers in this space continue to be plagued by illiquidity, which has forced them to mark down their portfolios. Trades of note include GMAC, the financial services group with close ties to General Motors, which rallied earlier in the quarter after renegotiating with their bondholders. However, gains in this trade were tempered because of the uncertainty over GMAC's loan value and business viability. During the next couple of quarters/years, it is expected that volatility will increase due to downgrades and higher default rates.
- The HFR Merger Arbitrage Index was up 1.65% in the first quarter, and was down 2.08% for the year-over-year period. The index remains one of the top performers over the one-year period, despite the continued trend of slowing global M&A activity. Deal spreads have tightened from their extreme levels with M&A not expected to pick up for some time. The most attractive opportunities managers are seeing are in announced deals by well financed strategic buyers, which are less prone to break. During the quarter there have been notable deals in the healthcare sector with Merck's announced \$41 billion acquisition of Schering-Plough and the completed acquisition of Genentech by Roche.

**DIRECTIONAL STRATEGIES**

- The HFR Macro Index posted a 0.91% loss for the quarter, but remains the best performing strategy over the one-year period (-0.18%). Losses in March (-0.66%) hampered the performance for the quarter. Short US Treasury positions suffered as prices increased from the Fed's announcement that they would buy US Government bonds. Gains in the strategy were achieved through short dollar positions and long trades in commodities, which managers remain bullish on as demand is expected to increase due to the Chinese stimulus plan.
- Despite a slightly negative return (-0.17%) equity long/short managers, as represented by the HFR Equity Hedge Index, performed well during the quarter relative to the global equity markets. Managers' gross and net exposures remained at record lows throughout the quarter. The equity rally in March helped save the quarter's performance with positions in the technology sector contributing the most. In addition, during the quarter volatility, as represented by the VIX index, continued to decline off of its peak in October to 44.14.

**REAL ASSET OVERVIEW**

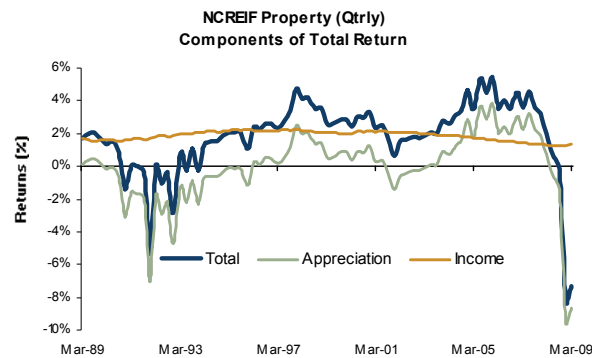
Coming off its worst quarterly performance ever (-8.3%) in the 4<sup>th</sup> quarter, the commercial real estate (“CRE”) market as represented by the NCREIF Property Index (“NPI”) experienced another steep decline, falling 7.3% during the first quarter of 2009. The dual impacts of market deleveraging and weakening property fundamentals are fully aligned in the CRE market, with asset values falling rapidly and demand for space and net operating incomes declining. Debt for CRE continues to be scarce and/or expensive, and rising unemployment and reduced consumer spending continues to negatively impact fundamentals. Distress is anticipated to rise among property owners with the inability to refinance maturing debt and/or among those holding poorly performing assets. Transaction activity remains slow with private capital sitting on the sidelines waiting for further price declines or distressed opportunities. Notably, according to Preqin, 44% of the private capital raised during the first quarter will target opportunistic investments, many of which will be distressed opportunities, while 40% will target real estate debt (the remaining is focused on value-added transactions).

With credit markets still challenged and the CMBS market a shadow of its former self, the government continues to introduce solutions to support the debt market and assist financial institutions in clearing their balance sheets in order to improve liquidity. Initially, the Term Asset-Backed Securities Loan Facility (“TALF”) was designed to provide cheap government financing to eligible U.S. entities for the purchase of new issue triple-A rated ABS securities; it was then expanded to include CMBS. Most recently, the Public-Private Investment Program (“PPIP”) was introduced with the intent of purchasing existing securities to improve liquidity. Under PPIP, private investors, including mutual funds, private-equity firms and pension funds, will partner with the Treasury on an equal-dollar basis and then employ leverage with nonrecourse debt provided by the FDIC, Treasury or Federal Reserve (depending on the program) to buy impaired loans or securities. Both programs are a work in progress but appear to be heading in the right direction toward facilitating the recovery and stability of the real estate market.

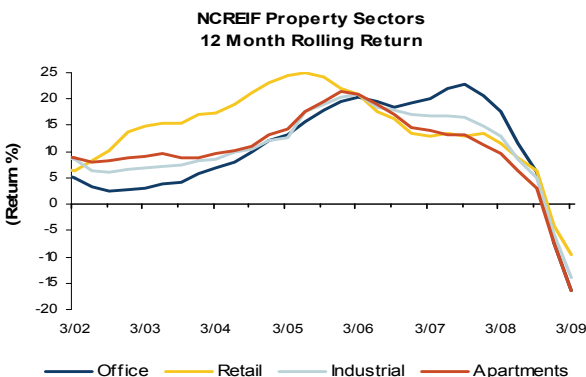
**Asset Class Performance (% Annualized Returns)**

As of 3/31/09	1 Year	3 Years	5 Years	10 Years
NAREIT (US)	(58.2)	(25.1)	(8.6)	3.9
EPRA/NAREIT (Global)	(56.8)	(22.1)	(5.4)	NA
NCREIF Property	(14.7)	4.2	9.4	9.4
NCREIF Timberland	5.6	13.2	14.1	8.9

Source: NCREIF, NAREIT (Equity Only), Bloomberg



Source: NCREIF

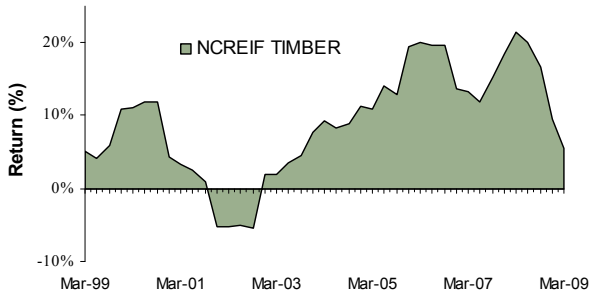


Source: NCREIF

**PRIVATE REAL ESTATE**

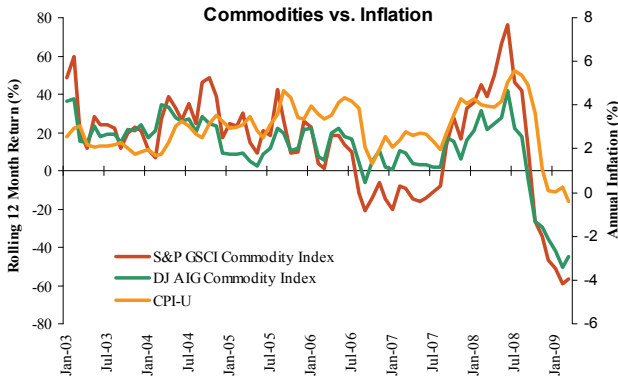
- As mentioned above, the NPI produced a total return of -7.3% during the first quarter of which -8.7% was depreciation, indicating an almost 20% drop in core institutional property valuations in the past six months (fourth quarter depreciation was 9.5%). Market fundamentals also deteriorated rapidly during the quarter with vacancies up and rents down virtually across the entire CRE market.
- The national office vacancy rate climbed to 15.2% in the quarter, up 240 bps over the trailing 12 months. Also, rents have been falling in many markets; however, some property owners may have some downside protection as older, existing leases may still be below even reduced current market rents. During the quarter the office segment was down -8.0% (and down -16.3% over the trailing one year period).
- Vacancies have risen in the multi-family sector to 7.6% according to CB Richard Ellis and Property & Portfolio Research, as the labor market continues to falter. 2008 was the first ever year of negative net annual absorption, which continued into the 1<sup>st</sup> quarter. The sector declined 8.7% over the 1<sup>st</sup> quarter, and was down 16.4% for the year. Still, financing has been most favorable in the multi-family sector, with the exception of new developments.
- With production and consumption in decline, the industrial sector, particularly warehouse, experienced its highest level of vacancies on record. Supply is more controlled in this sector relative to others however, which may help to mitigate downward pressure to some extent. For the quarter, the industrial sector declined 7.5% and is down 14.1% over the one-year period.
- The retail sector continued its positive relative performance and was the only major sector to beat the broader Index during the quarter, but was still down (-4.3%). Weak consumer spending continues to put pressure on retailers, as bankruptcies and store closings continue into 2009.

**NCREIF Timberland Index**  
Rolling 12 Month Return

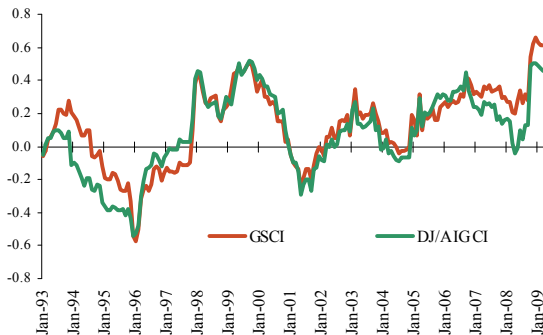


Source: NCREIF

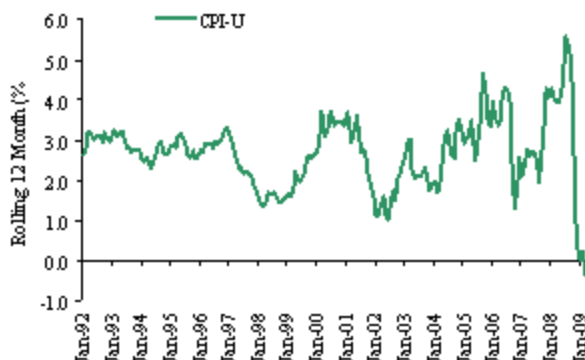
**Commodities vs. Inflation**



**2-Year Rolling Correlation With CPI-U**



**INFLATION (CPIU)**



**TIMBER**

- During the first quarter, the NCREIF Timberland Property Index returned 0.7% and was up 5.6% for the trailing one-year period ending March 31, 2009. The quarter continues to be characterized by pricing pressure for timber (although not for timberland), in a continuation from the trend in 2008.
- Southeastern timber prices struggled during the quarter across type and product with pulpwood (paper products) and sawtimber (wood products) declining in tandem. Furthermore, while prices for Northeast hardwood remained mostly flat during the quarter, Pacific Northwest timber experienced significant declines, off more than 20% from levels seen a year ago. Pricing pressure has resulted in reduced mill capacity, which should help to buffer pricing over time.
- While the value of private U.S. timberland increased over the course of 2008, according to Hancock Timber Resource Group, the absolute operating cash from timberland has decreased relative to prior years, due to both lower timber prices and less harvesting by owners due largely to lower timber prices. As a consequence, yields on timberland have moved lower.
- Given the dramatic asset repricing in the public markets (Plum Creek, a timber REIT, was down 15.1% and 24.4% over the quarter and one-year periods, respectively), private timberland returns may moderate looking ahead, outside of a near-term market recovery.

**OTHER**

- As of February 2009, there were 86 unlisted infrastructure funds in the market seeking an aggregate of \$92.3 billion (according to Preqin), which is up 98% from last year's level of \$46.7 billion.

**COMMODITIES**

- During the quarter, commodities were a poor performing asset and continue to be the worst performers over the year-over-year period. The Dow Jones-AIG Commodity Index was down 6.41% and the S&P GSCI declined 10.64% during the quarter. On a year-over-year basis, the Dow Jones-AIG was down 45.00% and the S&P GSCI was down 56.50%. The performance differential among the indices is caused by their relative allocations to oil and energy. The S&P GSCI has a high exposure to oil and energy, at 54.6% and 73.9%, respectively while the Dow Jones-AIG is more balanced with 12.1% and 30.9% allocated to oil and energy. During the quarter, oil prices increased 11.35% and gold prices were up 4.21%. The reason the Dow Jones-AIG Commodity Index outperformed the S&P GSCI Index for the quarter was because metals and copper prices surged on speculation over China's increased appetite for these products.
- Inflation, as measured by the Consumer Price Index (CPI-U) dropped significantly over the past two quarters. Inflation peaked in July 2008 at a 5.60% annual rate, fell to 0.10% in December 2008 and declined further to a -0.38% annual rate at the end of March 2009.

Data Sources: Hedge Fund Research, CSFB Tremont, Venture Economics, NCREIF, NAREIT, Citigroup, DJ-AIG, Bloomberg

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