

PRIVATE EQUITY OVERVIEW

The nearly unprecedented events of September, including the failure of Lehman Brothers, the acquisition of Merrill Lynch, the conversion of Goldman Sachs and Morgan Stanley to bank-holding company status, and the policy responses that came out of these events will have long-term implications for private equity which are yet to be fully defined. Despite these transformative events, we do not believe that private equity will go away, as have the large investment banks; private equity will evolve along with the new financial order. Some private equity firms may disappear over time, but given the long-term nature of private equity, it is not likely to follow the path of the hedge fund industry, which is expected to see considerable shrinkage.

While venture-backed companies will struggle in a deteriorating economy, and venture firms may cull their existing portfolios, their ability to invest is largely unhindered, although investment activity will still likely slow. The credit crunch has a much less direct impact in this space given the lack of leverage at portfolio companies. On the buyout side, existing portfolios will be adversely impacted as portfolio companies must deal with the combined effects of the credit crunch, making it difficult if not virtually impossible to refinance debt, and the economic weakness, hurting profits at many companies. Even investments in operationally sound companies may struggle if they are unable to economically refinance existing debt. With the financing market all but dried up, the pace of deal activity has materially slowed; private equity firms will have to evolve by putting more equity into deals with the hope of refinancing later, or find other creative ways to put capital to work. Given the dramatic recent drop in stock prices, and the values at which bonds are trading of some private equity-backed companies, LPs should be prepared for lower valuations on private equity fund investments. Looking ahead, the prospects for investment are better, given the valuations at which new investments can be made. However, the ability to deploy capital is still difficult, meaning that traditional buyout firms will have to be more creative about doing so, at least in the near term.

Other strategies, including secondary and distressed funds, are likely to find greater opportunities in this environment. Secondary funds should find opportunity among distressed entities, particularly financial firms and other entities that need to raise capital by selling non-core private equity assets and LPs overallocated to private equity given falling markets. Distressed funds should find plenty of opportunity among those entities that are expected to experience both operating and financial distress.

US Private Equity Performance Index (PEPI)
Investment Horizon Performance through 6/30/2008

Fund Type	1 Yr	3 Yr	5 Yr	10 Yr	20 Yr
Early/Seed	2.1	4.9	5.0	32.9	21.4
Later Stage	15.3	12.4	11.1	8.5	14.5
All Venture	5.1	8.5	8.8	16.6	16.9
Medium	15.1	11.6	12.8	7.4	11.8
Large	27.4	8.3	13.5	6.7	12.0
All Buyouts	0.4	10.5	13.9	7.4	11.6
All P.E.	1.6	10.6	12.3	9.5	13.3
NASDAQ	(11.2)	4.5	7.9	2.5	10.0
S & P 500	(13.1)	4.4	7.6	2.9	10.5

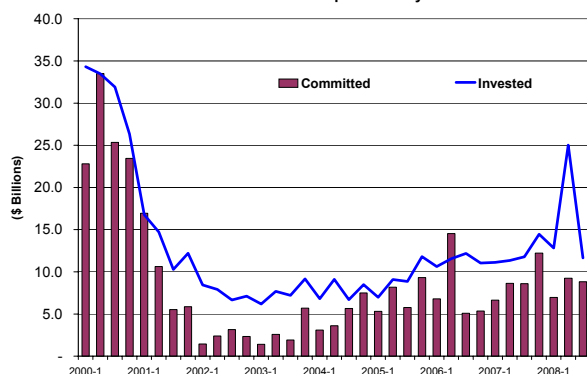
*The PEPI is based on the latest quarterly statistics from Thomson Venture Economics. All returns are calculated by TVE from the underlying financial cash flows. Returns are net to investors after mgmt fees and carried interest.

Source: Thomson Venture Economics/NVCA, Stylus

VENTURE CAPITAL

- In the 3rd quarter of 2008, fifty-eight venture funds raised a total of \$8.8 billion, versus the seventy-six funds that raised \$9.2 billion in the prior quarter; in the prior year's 3rd quarter, seventy-eight funds raised \$8.6 billion. The larger average fund size is expected to be invested in more capital-intensive sectors such as clean technology.
- After an unusually strong 2nd quarter, venture investment activity fell back to more typical levels in the 3rd quarter, to \$11.6 billion, which was down from \$25 billion in the prior quarter. This was more in-line with the 3rd quarter of 2007, when \$11.8 billion was invested in venture deals.
- Exit activity remained very weak, which is not surprising given the difficulties of the 3rd quarter. There was only one venture-backed IPO in the U.S. which raised \$188 million; this was up from the zero IPOs in the prior quarter. The IPO window for the first three quarters of 2008 is as closed as it has been since 1977; there have been only six venture-backed IPOs during the year. Notably, thirty-eight venture-backed companies are "in registration" for an IPO, down from forty-two in the prior quarter; twenty-eight companies have withdrawn from registration in 2008.
- On the M&A front, the news is somewhat better, as seventy-six firms were acquired for \$3.7 billion. While this remains at the low end of the range of activity since 2002, M&A activity has not fallen off the proverbial cliff as has the IPO market.
- With markets volatile and many corporations struggling with deteriorating business fundamentals, the prospects for exit activity do not appear good in the near-term. However, unlike the prior market downturn in 2001-2003, the venture capital space has remained relatively more disciplined from a fundraising standpoint this time around, which should lead to a more stable industry as the markets recover.

US Venture Capital Activity



Source: Venture Economics

BUYOUTS

- Buyout funds raised \$47.1 billion in the 3rd quarter, up from \$41.5 billion in the prior quarter, and essentially flat with the \$47.7 billion in the 3rd quarter of 2007. While this represents a material drop from the \$73.9 billion record raised in the 1st quarter of 2008, it is still an impressive total considering the difficulties in the market. Notably, this data include mezzanine fundraising totals. While fundraising for traditional buyouts is more challenging given the difficult financing and investment environment, and with reports of some struggling past deals, other segments of private equity may pick up some of the slack over time, including distressed debt, mezzanine and secondary funds, discussed below.
- Performance among the various buyout segments has meaningfully diverged over the past few quarters, as small and mega buyouts have generated negative performance over the last year, while medium and large buyouts have been solidly positive over the same period. The weakness in mega buyouts is not surprising, as a number of such deals have openly struggled (TPG's investment in Washington Mutual, for example).
- Investment activity has slowed materially since the height of the buyout bubble, and will likely remain slow until the credit markets open up. In the meantime, in order to deploy existing funds, private equity firms will need to invest more equity into deals, and to consider other alternatives for investment, including PIPEs and other non-traditional investments.
- In a continuation of last quarter, the exit market for buyouts was weak. There was only one buyout-backed IPO in the 3rd quarter, down from two in the prior quarter and down from fourteen in the 3rd quarter of last year. 2008 is shaping up to be a particularly weak year for buyout-backed IPOs, with only five having been completed through the 3rd quarter.
- The exit market for buyout-backed M&A was relatively weak as well. Twenty-seven companies were acquired for \$3.0 billion, versus the twenty-eight acquired for \$1.8 billion in the prior quarter. However, this was down materially from the forty-five acquisitions for \$11.1 billion in the 3rd quarter of 2007.

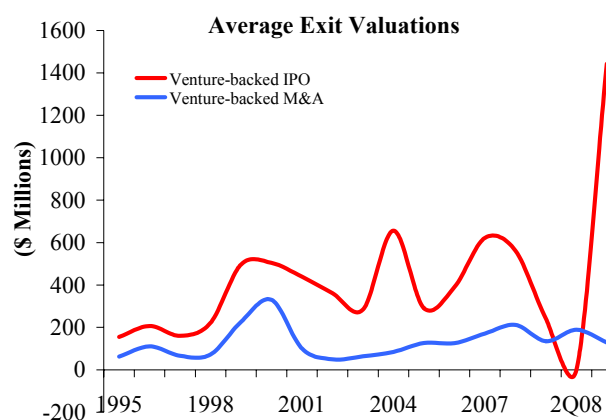
OTHER

- As noted above, other private equity-related strategies have gained some prominence in the market recently, as the traditional buyout market has become very difficult; these include mezzanine, distressed debt, and secondary funds. Each of these strategies could potentially benefit from the difficult market environment. In the 3rd quarter, mezzanine, distressed debt and secondary funds raised \$820 million, \$5.4 billion, and \$2.3 billion, respectively. Particularly for mezzanine and distressed debt, these totals are down materially from earlier in 2008, when mezzanine funds raised \$18.1 billion in the 1st quarter, and distressed debt funds raised \$14.8 billion in the 2nd quarter. Given the relatively smaller pool of managers in these segments, a small number of large funds can materially skew the data.

Venture Exit Analysis:

	# of Venture-Backed IPO's	Offer Amt (\$MM)	# of Venture-Backed M&A	Deal Value (\$MM)
2003	29	2,023	299	7,535
2004	94	11,378	351	15,942
2005	57	4,485	371	22,179
2006	57	5,117	387	19,316
2007	86	10,326	361	28,457
4Q07	31	3,044	88	9,084
1Q08	5	283	71	3,908
2Q08	0	0	72	4,154
3Q08	1	188	76	3,741

Source: Venture Economics

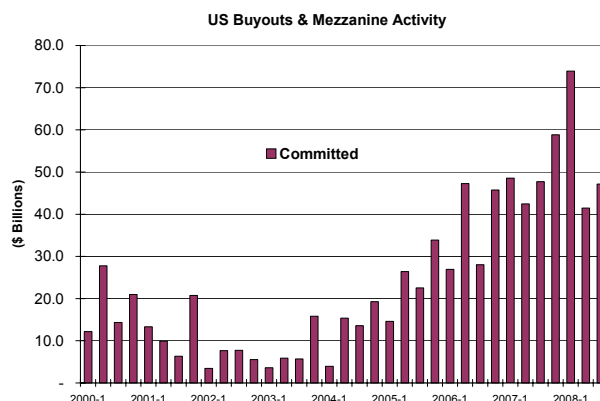


Source: Venture Economics

Buyout Exit Analysis:

	# of Buyout-Backed IPO's	Offer Amt (\$MM)	# of Buyout-Backed M&A	Deal Value (\$MM)
2003	22	5,038	39	8,572
2004	57	11,293	39	9,251
2005	67	15,764	97	22,672
2006	55	17,451	142	26,222
2007	40	9,627	166	43,215
4Q07	10	2,593	39	7,800
1Q08	2	267	26	3,690
2Q08	2	357	28	1,773
3Q08	1	500	27	2,995

Source: Venture Economics



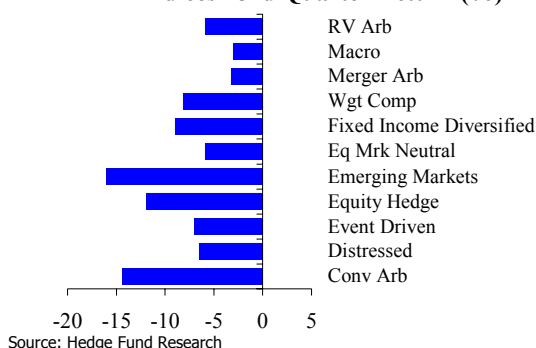
Source: Venture Economics

HEDGE FUND OVERVIEW

Equity markets plummeted and credit markets eroded in September producing third quarter hedge fund losses that will likely go down in the history books as some of the worst on record. The HFR Weighted Composite Index slid 8.14% during the quarter, and is down 8.4% on the year. Difficulties for managers really took hold in September when credit seized up following Lehman Brothers' bankruptcy and lending was materially curtailed, even on an interbank basis. This lack of credit, combined with massive redemptions from mutual funds and hedge funds, forced portfolio managers to liquidate securities in order to raise cash regardless of underlying fundamentals. The hedge fund managers that suffered the most were employing strategies that were highly levered, such as various arbitrage strategies, or highly concentrated. To make matters even worse, in the middle of September rumors about new short-sale restrictions and the bailout led to a dramatic short covering of positions, causing some of the worst stocks, on fundamental basis, to outperform. A large part of this deleveraging has been caused by hedge funds experiencing a relatively high level of redemptions, which in the long run will reduce the number of hedge funds operating in the market place.

Hedge Funds of Funds were also pounded in the third quarter, with the HFR FOF Diversified Index, the collection of broadly diversified funds of funds, down 8.79%. More conservative funds included in the HFR FOF Conservative Index were down 6.78%, while the more aggressive mixture of funds, those that typically emphasize equity long/short strategies and are included in the HFR FOF Strategic Index, took the biggest hit, down 10.70%. The differential in performance of hedge fund of funds relates to how much exposure managers have to relative value and macro type strategies.

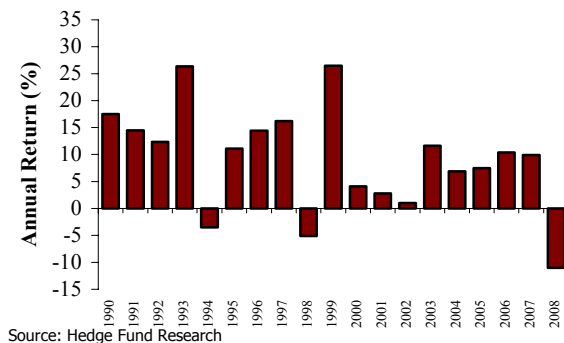
HFR Indices - 3rd Quarter Return (%)



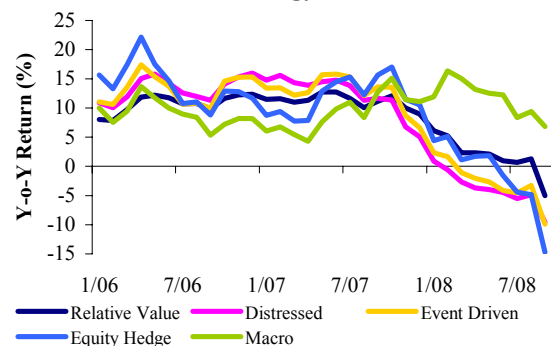
NON-DIRECTIONAL STRATEGIES

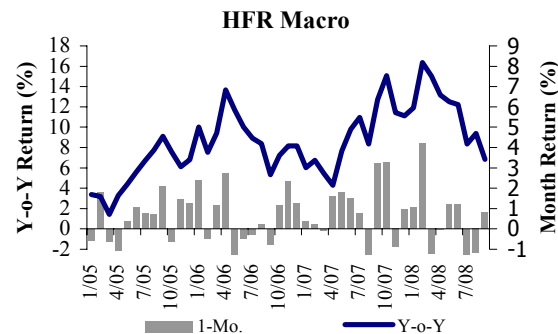
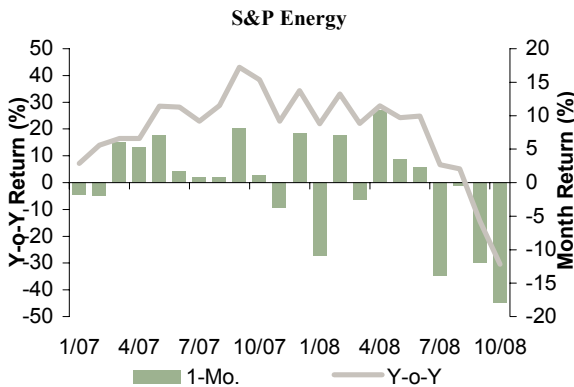
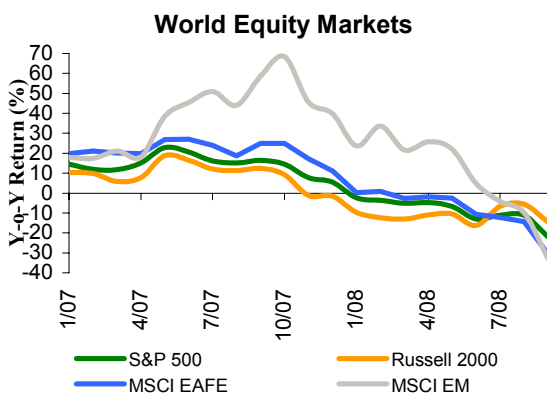
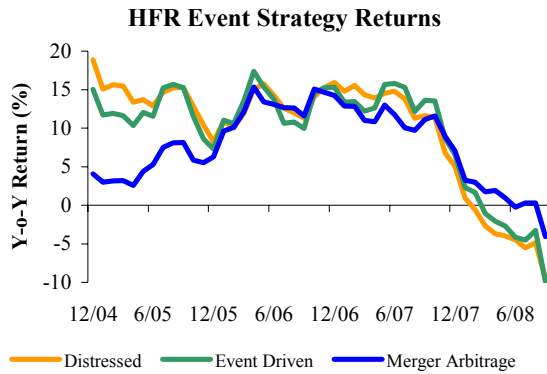
- The HFR Equity Market Neutral Index sustained its largest loss since its inception, dropping 5.95% for the quarter. However, market neutral remains the top performing segment over the one-year period, suffering just a 2.64% decline. As with most hedge funds strategies, market neutral managers were affected by the accelerated unwinding of positions by hedge funds and other investors, as well as the implementation of the short-sale ban in September.
- Convertible arbitrage, as represented by the HFR Convertible Arbitrage Index (-14.46%), was among the worst performing strategies for the quarter, and is now the worst performing strategy over the one-year period with a 19.64% decline. A dramatic implosion of converts occurred in September as the index dropped 11.97% partly due to the short-sale ban instituted by the government following the bankruptcy of Lehman Brothers. Since most convertible bonds issued are from financial based companies, hedge funds could not offset their long exposure to financials because some of those companies were on the restricted list. After the losses sustained during the third quarter, convertible arbitrage strategies are the worst performers on a year-over-year basis with many dedicated managers in this space having to suspend redemptions. The strategy remains attractive as strong issuance and elevated levels of continued volatility benefit convertible arbitrage.
- The HFR Relative Value Arbitrage Index was down 5.86% for the quarter due to the increasing cost of leverage.
- The HFR Fixed Income Index finished dramatically down for the quarter with a loss of 8.98%. This was due to forced selling caused by deleveraging and the effects of the short-sale restrictions. These actions were required as a result of unprecedented moves in credit spreads on a global basis. U.S. High Yield, as measured by the Merrill Lynch High Yield Cash Pay Index, fell 8.3% for the month of September, and finished the quarter off 9.45%. Additionally, investment grade corporate credits were down just as much, with the LB Long Credit Index down 8.78% during the quarter. A dramatic steepening of the yield curve also proved problematic for many managers, as the short end of the Treasury curve was pounded lower on flight to quality demand.

HFR Funds of Funds



HFR Strategy Returns





EVENT DRIVEN STRATEGIES

- The HFR Event Driven Index delivered its worst quarterly loss (-7.00%) since inception of the index in 1990. In July (-1.27%) and August (-0.42%) the index suffered modest to minimal losses before collapsing (-5.41%) in September.
- The HFR Distressed Index lost 6.57% during the quarter, the strategy's worst loss since inception since 1990. Many managers continue to agree that there are increasing opportunities for distressed trades, and now with a massive sell off in the third quarter, the sentiment is that it has become even more attractive. For example, corporate credit markets were at the epicenter of the quarter's deleveraging activity, and good credits were sold along with the bad. Certain bank loans that mature within a few years and are high in the capital structure are trading at 70-75 cents on the dollar or lower. Other odd relationships exist in which more senior bonds of certain companies have sometimes traded at higher yields than less senior bonds. This anomaly is occurring as highly leveraged managers are forced to unwind positions without regard to underlying value.
- The HFR Merger Arbitrage Index declined 3.29% in the third quarter, and is down 4.08% on a year-over-year basis. In the funds of funds space we are not seeing managers actively allocating to dedicated merger arbitrage, instead getting exposure through multi-strategy funds that can rotate capital opportunistically. Over the past couple of quarters merger spreads have remained wide as investors have remained concerned about deals getting done following equity market declines and tight lending markets. Recent mergers have been primarily of the strategic variety, and although these deals typically are considered less risky than heavily financed LBO transactions, the current spreads in some of these deals suggests a material probability that many of them will fail. Alternatively, the spreads may also be a reflection that event driven hedge funds have been liquidating their portfolios to raise cash, in turn forcing substantial short-term pressure on deal spreads, even those that have a high likelihood of being completed.

DIRECTIONAL STRATEGIES

- The HFR Macro Index posted a 3.03% loss for the quarter, but remains the best performing hedge fund strategy and is the only positive category over the past year with a +6.83% return. Performance in the third quarter was hampered by losses in emerging market debt and commodity positions, particularly energy. However, profitable trades were long positions in short-dated fixed income, such as government bonds and short positions in global stock indices.
- Equity long/short managers were beaten up in the third quarter as global markets plummeted and government intervention (i.e. ban on short selling) roiled markets and sharply increased volatility. The HFR Equity Hedge index was down 11.97%, considerably more than the S&P 500 (-8.37%) but less than the MSCI EAFE (\$) Index (-20.56%) or the MSCI Emerging Markets (\$) Index (-26.86%). Managers aggressively raised cash during the quarter in anticipation of elevated redemption requests for year-end.

REAL ASSET OVERVIEW

The contagion in the capital markets is starting to reach the commercial real estate (“CRE”) industry; the outlook for the sector dampened during the quarter with the near collapse of the global financial system and further weakening of the overall economy. CRE is experiencing collateral damage from the capital markets as fundamentals still have not deteriorated much in aggregate, although signs of weakening are apparent. The paralysis of the credit markets may profoundly impact some property owners with short-term debt originated over the past few quarters that will need refinancing; Macklowe’s inability to refinance several properties in New York earlier in the year is perhaps the most high-profile example of this, but there are likely to be other investors who run into similar difficulties. There is no doubt that property values are under pressure with rising vacancy rates and weakening net operating income. Price-discovery remains difficult though, as the lack of transactions and dislocation between buyers and sellers (wide bid/ask spreads) continues; however, prices are expected to fall putting upward pressure on cap rates. Overall, the state of CRE space fundamentals during this cycle may provide some resiliency to survive a down-cycle, as although demand is slowing, the overall lack of supply growth over the past few years has kept fundamentals essentially at equilibrium levels. Despite the uninspiring outlook for commercial real estate, this market environment may provide interesting opportunities for good real estate managers who can create value at the property level or take advantage of some of the dislocations in the market.

While the economic downturn has also cut into the timberland industry with demand for lumber declining sharply and prices reaching 30-year lows, given the relatively low leverage of timberland investments, the credit crisis is likely to have a less direct impact on this space. Capital flows may be a more important driver of deal activity and valuations. However, the poor outlook for residential real estate does not bode particularly well for any near-term recovery in the lumber markets.

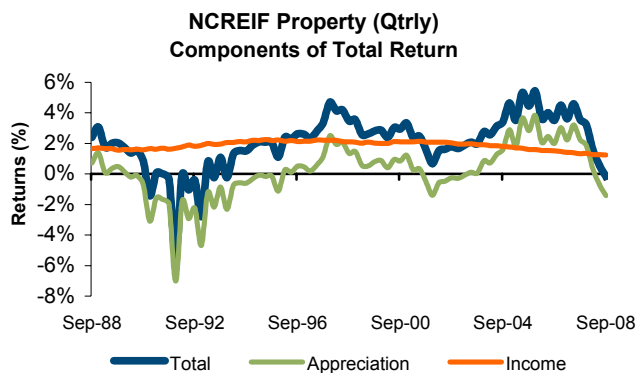
Asset Class Performance (% Annualized Returns)

As of 9/30/08	1 Year	3 Years	5 Years	10 Years
NAREIT (US)	(11.1)	5.6	13.5	12.5
EPRA/NAREIT (Global)	(30.6)	2.3	12.8	NA
NCREIF Property	5.3	13.2	14.2	11.8
NCREIF Timberland	16.6	17.1	14.6	8.9

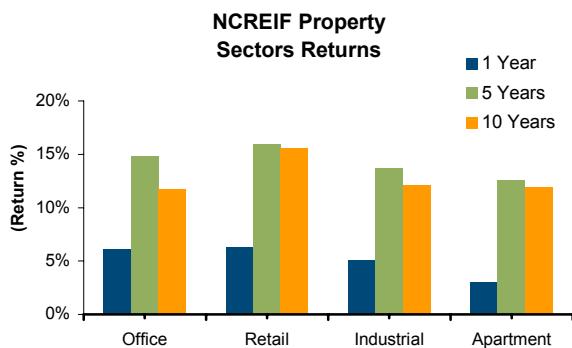
Source: NCREIF, NAREIT (Equity Only), Bloomberg

PRIVATE REAL ESTATE

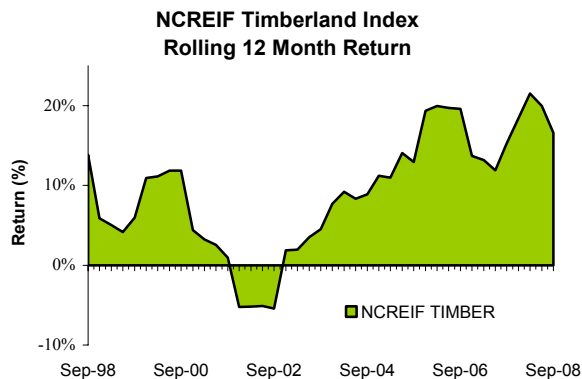
- Private real estate, as represented by the NCREIF Property Index (“NPI”), weakened in the third quarter as appreciation continued to be negative for the second straight quarter. The -1.42% appreciation return in the third quarter caused the total return to fall to -0.17%; this was the first negative quarterly total return in 15 years.
- Office fundamentals are weakening due to the deteriorating economy, especially in areas exposed to financial institutions. Vacancy rates have increased slightly and are expected to continue to rise. As a result, landlords have less leverage, meaning weaker rental growth than was projected even a year ago; rental growth is expected to be negative in many markets. For the quarter, office properties produced a negative 0.31% total return; over the trailing one-year period, office still generated a 6.10% return, however.
- Although the retail sector generated a positive total return for the quarter (+0.18%), it is likely to be materially impacted by the weakening economy as consumer confidence continues to dwindle; the bankruptcy of Linens ‘n Things may be indicative of the struggles of other retailers. With consumer spending expected to remain weak, an increase in vacancies and a decrease in rents are anticipated. Notably, on a relative basis, retail has been the best performing sector of the NPI over the past decade, although this pattern may not continue looking ahead.
- Although the industrial sector has historically been a relatively steady performer, it is expected to experience near-term volatility due to the global nature of the weakening economy. For the quarter, industrial properties were effectively flat (-0.01%) but are up 5.10% over the trailing one-year period.
- While the apartment sector was the weakest performer during the economic expansion compared to other property types, it may prove to outperform them going forward. The impact from the housing bubble and favorable demographics bode well for this sector looking ahead. During the third quarter, apartments generated a -0.36% total return.



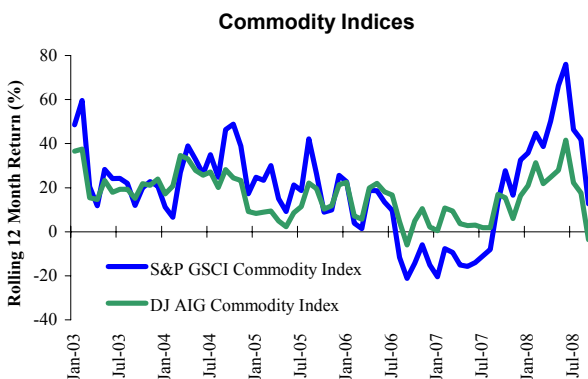
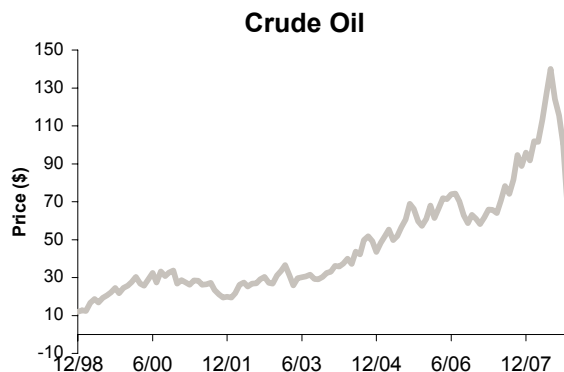
Source: NCREIF (Data as of 9/30/08)



Source: NCREIF (Data as of 9/30/08)



Source: NCREIF (Data as of 9/30/08)



TIMBER

- The NCREIF Timberland Property Index returned 0.99% during the third quarter, and is up 16.59% for the trailing one-year period ending September 30, 2008. With the summer months seasonally slow, and the continued slump of the housing market lumber prices have been depressed during the quarter.
- However, transaction activity in the timberland market has been solid on a year-to-date basis, including several large-scale deals which exhibited healthy market prices. Valuations in this sector have strengthened over the past several years largely due to the inflow of capital into the space. However, it remains to be seen how the current credit situation will impact transaction valuations going forward.

OTHER

- Private infrastructure investment has grown materially over the past few years with the recognition of significant capital needs in both developed and emerging economies for infrastructure projects. According to Preqin, an industry data source, there are currently 71 infrastructure funds seeking to raise \$90.8 billion, a dramatic increase from as recently as 2005, when only four funds were seeking to raise \$1.8 billion.

COMMODITIES

- During the 2nd quarter, commodities were the best performing asset class, but they gave back everything and more in the third quarter with the Dow Jones-AIG Commodity Index down 27.70% and the S&P GSCI plummeting 28.61% during the quarter. On a year-over-year basis, the Dow Jones-AIG Commodity Index is down 3.66% while the S&P GSCI remains up 12.72%. The differential between the two is a reflection of the higher energy allocation in the S&P GSCI. With continued rapid deterioration in oil prices into October, the sharp downward trend of the indices is expected to continue for the near term. Investors have been unloading commodity positions as clarity on the severity of the global slow down starts to develop.
- The wild swings of crude oil experienced this year have been unprecedented. With such a sharp contraction in oil prices, producers that were aggressive in locking in future supply at levels above current market prices will likely be impacted as demand evaporates.
- Inflation, as measured by the Consumer Price Index (CPI-U) peaked in August at a 5.97% annual rate, the highest reported increase in prices since January 1991, before retreating to 5.68% in September. Declining commodity prices during the quarter were perhaps the only thing that was working in favor of consumers during the quarter. With financial markets in turmoil, lower commodity prices erased concerns about inflationary pressures, thus freeing up nations around the world to combat slower economic growth through monetary stimulus measures.

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

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