Private Equity Partners | market update

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The Year Ahead in Private Equity Fundraising

Earlier this month, the NVCA released its 2006 private equity fundraising statistics. Not surprisingly, 2006 was a record year for private equity (venture and buyout) fundraising. Venture funds raised $28.6 billion, the largest amount raised since 2001, while buyout funds raised a record $102.9 billion in 2006. However, fundraising slowed considerably in the fourth quarter for both venture and buyout funds.

Will this slowdown continue into 2007?

Not likely. Instead, we believe investors were catching their collective breath before setting out to again deploy near-record amounts of capital in 2007.

Last year was a banner year for public equity markets. The Dow was up 16.3%, the S&P rose 13.6% and the Nasdaq gained 9.5%, while the MSCI World Capital Markets Index (excluding the US) climbed 18.8%. This strong performance substantially enlarged investors' asset bases, which should allow them to commit additional large amounts of capital to private equity firms in 2007. Moreover, venture and buyout industry dynamics continue to point to a big year of fundraising:

- The vast size and quantity of offerings by top buyout firms in 2006 commandeered institutional investors' 2006 private equity allocations, largely at the expense of venture capital firms. We believe many investors will be looking to catch up on missed/deferred commitments to venture firms and to re-deploy their recent gains as they rebalance their portfolios in 2007. Many good firms are already lining up to raise funds this year.
- The amount of capital raised recently by buyout funds was record-setting and so was their investment. Demand for paper in the high yield market continues to exceed supply allowing LBO firms to raise debt cheaply and with fee restrictive covenants. As a result, buyout firms are readily able to finance transactions and are very effectively competing against strategic acquirers. This is helping to maintain the current investment pace for buyout firms. According to Dealogic, there were $370 billion of buyout transactions in 2006. Assuming 30% of the transactions was in the form of equity, buyout firms spent approximately $111 billion in 2006 (compared to $102 billion raised). Buyout funds will need to replenish their coffers in 2007 in order to maintain their torrid pace, fueling another strong year of buyout fundraising.

Implications

- Venture: Whereas the size of many buyout funds has doubled or tripled from one fund to the next, most VC firms have remembered the excesses of the bubble and have kept fund sizes the same or smaller, despite being two and three times oversubscribed in many cases. As investors move back into venture capital in the first half of the year, demand for top-tier venture firms will grow substantially, making access to top-tier venture firms even more difficult to obtain for new entrants and non-value added investors.
- Buyout: Readily available financing has fueled escalating purchase price multiples and increasing competition, as seen through high profile bidding wars for coveted properties including Harrah's Entertainment and Equity Office Properties. While we believe the top-tier firms will be able to generate outsized returns by offering portfolio companies more than just financing (i.e., contacts, industry expertise, group purchasing organizations, etc.), many other buyout firms' returns will be compressed in this competitive environment.

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Conclusion

We expect 2007 to be another banner fundraising year. However, the limited fund size of the top-tier VC funds and the overabundance of capital on the buyout side will create access and selectivity issues for many investors. That said, we believe those able to gain access to the top-tier VC and LBO firms will continue to enjoy outsized returns in 2007.

Mark Austin Joins Private Capital Team

Mark Austin recently rejoined Piper Jaffray to manage our institutional sales efforts and new account development. He has over 15 years of institutional sales experience from his tenures at both Piper's and U.S. Bancorp's asset management divisions. Immediately prior to rejoining Piper Jaffray, he was a managing director at FAF Advisors, Inc., an affiliate of U.S. Bancorp, in Minneapolis.

We had collaborated with Mark on our four prior funds over the last seven years. He brings a tremendous amount of investment and sales experience to our team. We look forward to continued growth in our business through his well-established institutional relationships. For more information on Mark, please see our team biographies on the Web.

CleanTech Ventures Exceeds Expectations

We have closed the **CleanTech Ventures** fund at $60 million dollars in investor commitments. This exceeded both our original target of $25 million and our revised target of $50 million. We are extremely pleased with the quality and quantity of investment opportunities in the CleanTech sector and our position as a fund of funds in this rapidly developing industry. The vast majority of our commitments to underlying fund managers has been completed, and we anticipate finalizing the remaining few fund commitments in the coming weeks.

Piper Jaffray was established in 1895 and has grown to become a nationally and internationally recognized firm serving growth companies and growth company investors. We have a significant commitment to alternative assets through our series of fund of funds.