



# Private Equity Update

7/28/2016



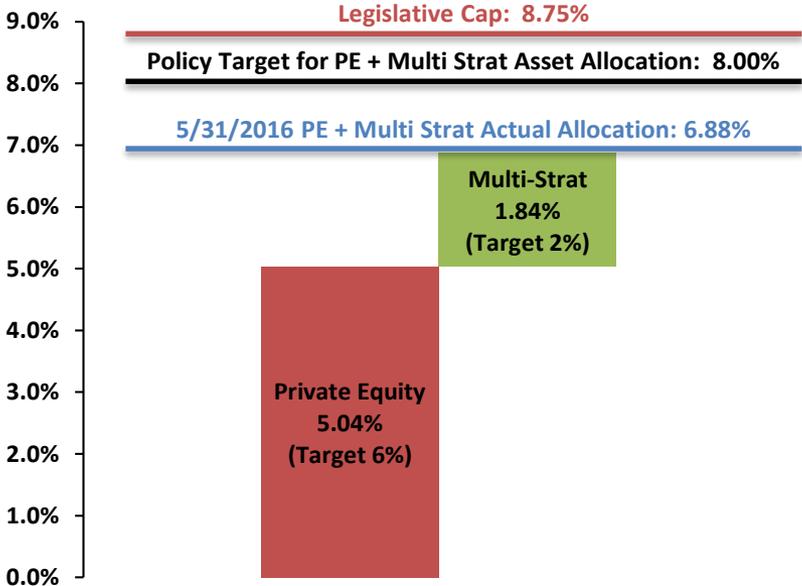
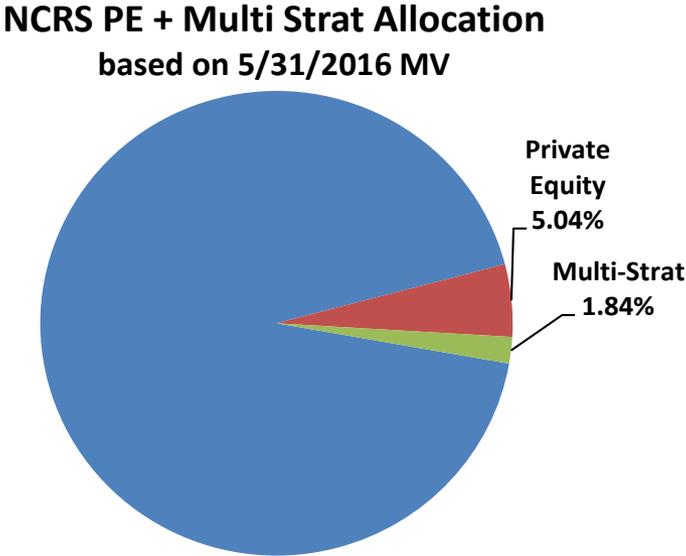
North Carolina Department of State Treasurer  
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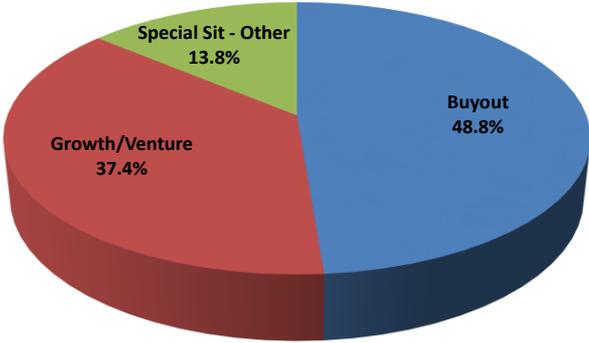
# Statutory Allocation

As of May 31, 2016

- Private Equity + Multi Strat represented 6.88% of the Total NCRS Plan
- Private Equity represented 5.04%, below the Policy Target of 6%



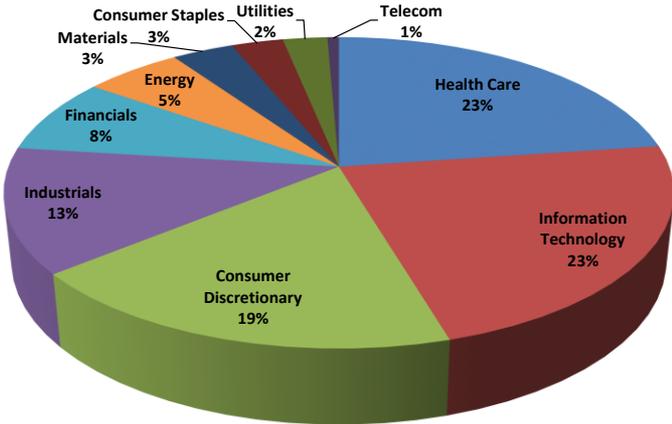
# Private Equity Allocation



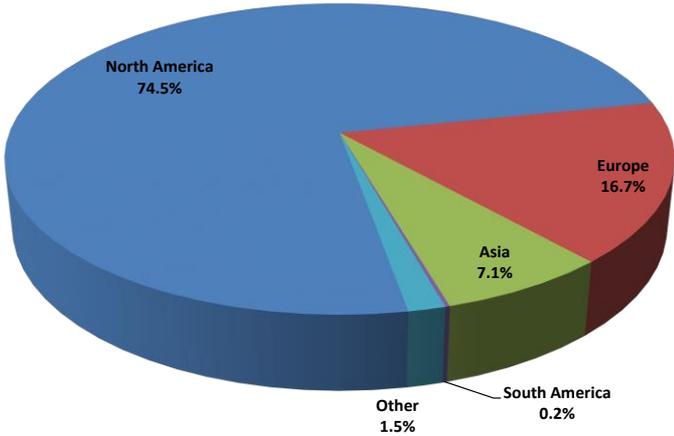
Policy Relative to Actual Portfolio Weights						
Strategy	Policy Range			Actual* (12/31/2015)	Estimated* (6/30/2016)	Unfunded* (6/30/2016)
	MIN	TARGET	MAX	(FMV)	(Adj. Value)	
Buyout	35%	50%	65%	48.8%	48.7%	48.4%
Growth/Venture	10%	20%	30%	37.4%	36.5%	26.9%
Special Situations	15%	30%	45%	13.8%	14.8%	24.7%
<b>TOTAL</b>				<b>100%</b>	<b>100%</b>	<b>100%</b>

➤ Based on forward pipeline through 2017 (as of 6/30/2016), targeted commitments to: Buyout – 62.8%, Growth/Venture – 14.2%, and Special Situations – 22.7%

## GICS Industry Allocation\*



## Geographic Allocation\*

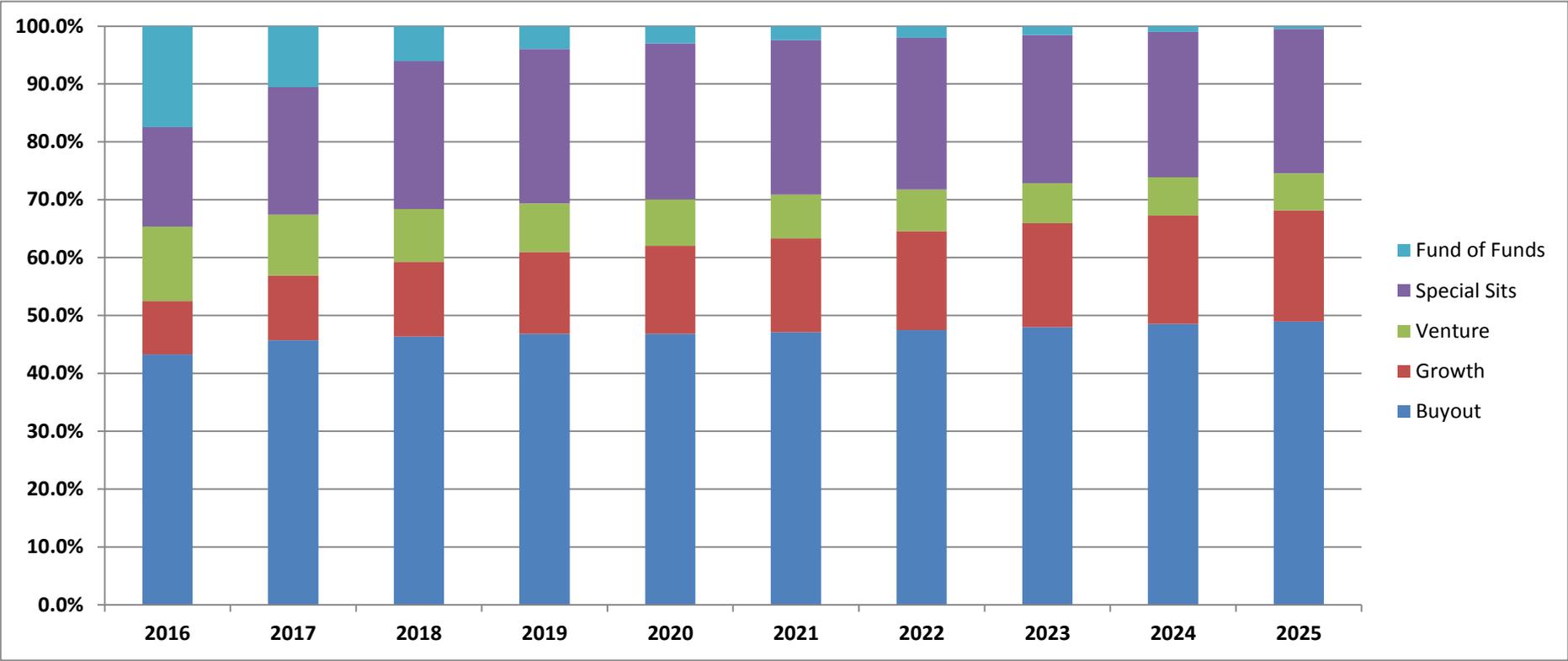


\*Data includes Fund of Funds' underlying exposure (as of 12/31/15 or most recent)



# Future Portfolio Weighting

## Strategy Allocation including Fund-of-Funds



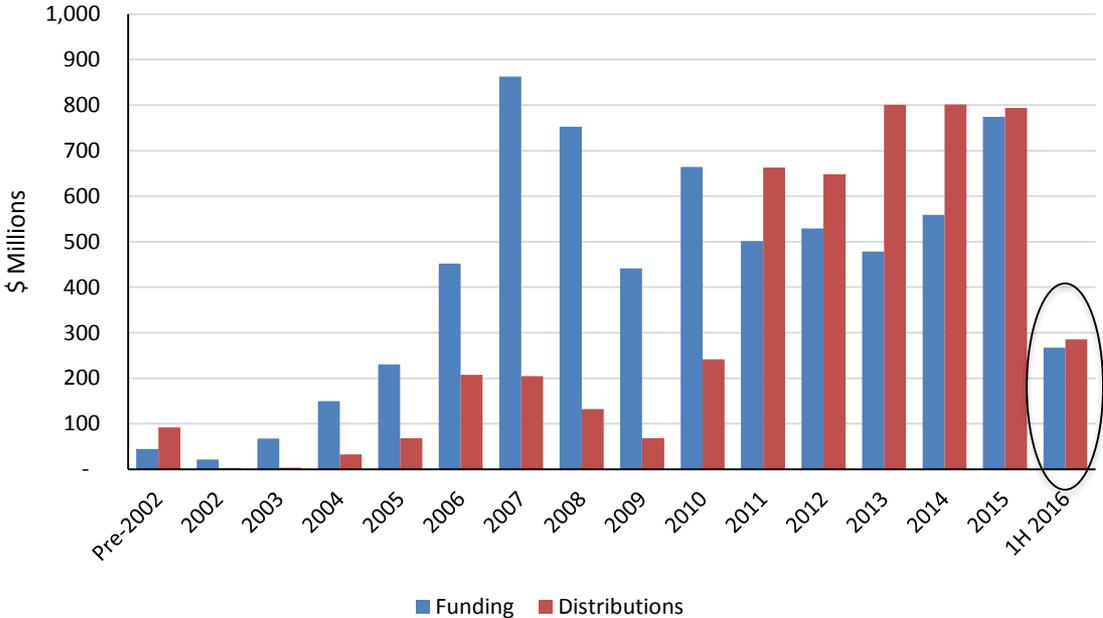
Note: Fund of Funds is comprised of: Buyout – 33.5%, Growth/Venture – 59.1%, and Special Situations – 7.4% (as of 12/31/15 or most recent)



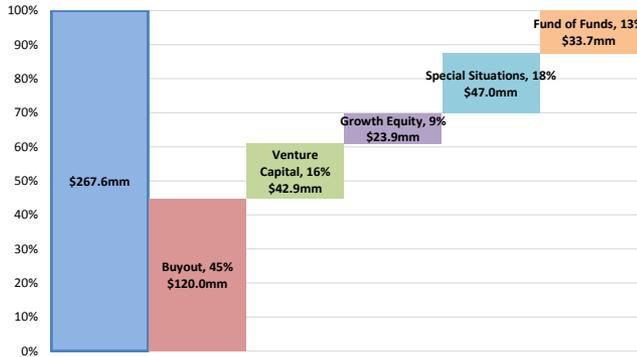
# Private Equity Cash Flow Detail

➤ From 2011 through 1H 2016 Distributions have exceeded Funding

**Private Equity Cashflows  
by Calendar Year**



**1H 2016 Funding  
by Strategy**

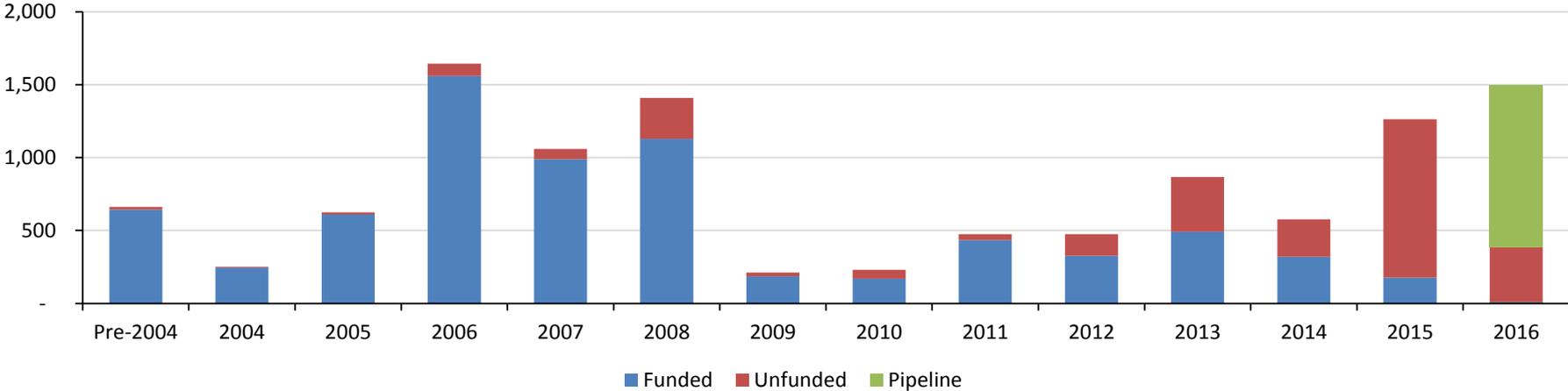


**1H 2016 Distributions  
by Strategy**



# Private Equity Commitments

Private Equity Commitments by Vintage Year



Note: Data as of 6/30/2016

<i>\$ in Millions</i>	2016					2017		
	<u>Closed</u>	<u>Pending</u>	<u>Identified</u>	<u>2016 Total</u>		<u>Identified</u>	<u>Potential</u>	<u>2017 Total</u>
Buyout	250	500	100	850		650	200	850
Growth/Venture	135	210	-	345		125	-	125
Special Situations	-	-	300	300		225	-	225
<b>TOTAL</b>	<b>385</b>	<b>710</b>	<b>400</b>	<b>1,495</b>		<b>1,000</b>	<b>200</b>	<b>1,200</b>



# Performance Attribution

## IRR by Vintage Year (%)

Year Ended	Vintage Year												
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	Total*
2015	7.59	4.99	3.00	9.67	10.10	13.65	20.04	10.97	15.84	9.67	11.91	0.04	7.76
2014	8.35	5.34	3.23	9.59	10.96	14.23	20.34	8.09	18.07	4.03	-25.13	N/A	7.74
2013	7.51	5.69	3.62	7.52	10.25	11.45	19.43	8.54	2.99	-15.45	N/A	N/A	7.36

Note: Data as of 12/31/2015

\*Total includes pre-2004 vintage year performance

## Performance by Vintage Year

Vintage Years	# of Funds	IRR
Inception - 2015	133	7.76%
1988 - 2009	98	7.30%
2010 - 2014	26	13.67%

## Performance by Strategy (2010 - 2014 Vintages)

Strategy	# of Funds	IRR
Buyout	14	13.97%
Venture Capital	3	10.81%
Growth Equity	2	11.13%
Special Situations	5	6.69%
Fund of Funds	2	19.86%

## Private Equity Portfolio

as of December 31, 2015

USD in Millions

Vintage Year	<b>2010 - 2014</b>
Funds	26
Called Capital	\$1,540.0
Realized Value	\$282.4
Residual Value	\$1,600.0
Total Value	\$1,882.4
Gain/Loss	\$342.4
TVPI	1.22x
DPI	0.18x
IRR	13.67%
K&S Public Market Equivalent*	1.08x

\*PME is run against S&P 500

7



# Private Equity - Market Activity

## Slow Start to 2016

1Q16 sequential quarterly decline

- Invested down 8.5%
- Transactions down 23.3%

1Q16 Y-O-Y quarterly decline

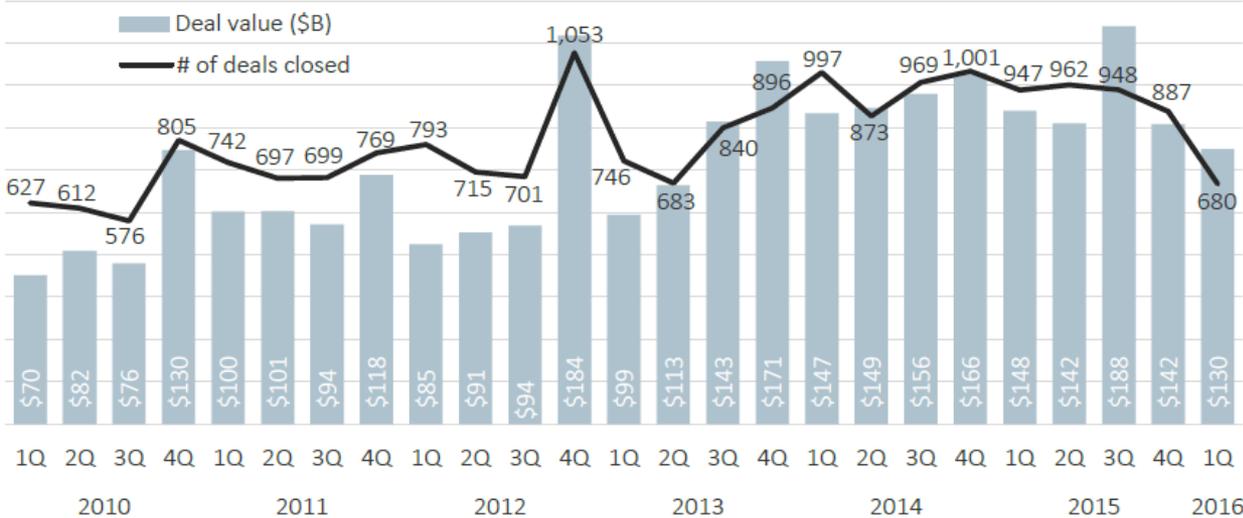
- Invested down 11.6%
- Transactions down 28.2%

- Currency swings
- Volatile public markets
- U.S. Treasury inflows
- China
- Valuations
- Election
- Brexit
- Energy



Result: Underwriting becomes more difficult given macro unknowns.

U.S. PE activity by quarter



Source: PitchBook as of 3/31/16



# BREXIT: Portfolio Impact

- **Certainty** that we are in another period of volatility, funds are guarded but looking for new opportunities.
- **Uncertainty** around renegotiation of trade agreements and timing of an actual exit from the EU.
- Private Equity currently has an allocation of 16.7% to Europe\*, however the majority of our exposure is to Western Europe.
- No covenant, liquidity, or maturity issues as managers completed acquisition financings and refinancing ahead of vote.
- Weaker GBP could make acquisitions cheaper for foreign buyers.
- This will be complex and benefit those managers who can take advantage of volatility.
- Opportunities to recapitalize and or acquire European distressed opportunities.

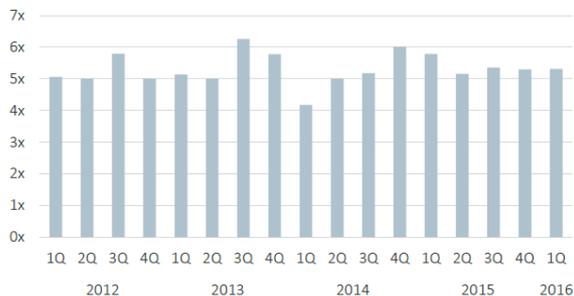
\*As of 12/31/15



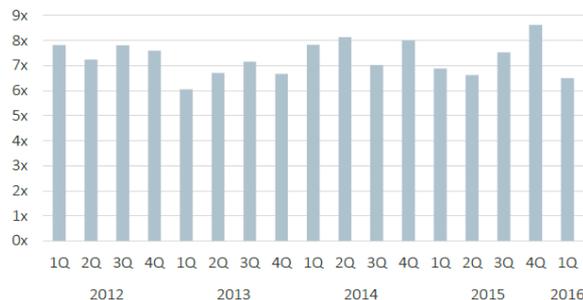
# Private Equity - Valuations

## Multiples Decline in 1Q16

Median EV/EBITDA buyout multiples by EV under \$25M



Median EV/EBITDA buyout multiples by EV from \$25M to \$250M



Median EV/EBITDA buyout multiples by EV above \$250M



- Buyers weighing the environment and factoring in more conservative assumptions → Lower Valuations
- Sellers holding out for higher valuations if not forced to sell → Lower Volumes
- In 1Q16, smaller transactions are making up the bulk of deals
  - Deals sized below EV \$100 MM approaching 75% of transactions, similar to 2008 and 2009
  - 2010-2015, typically 65-70%

Source: PitchBook as of 3/31/16

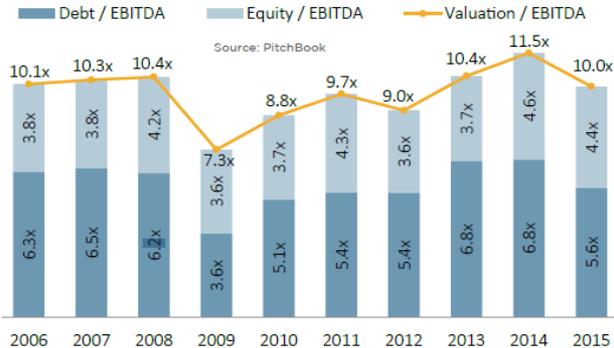
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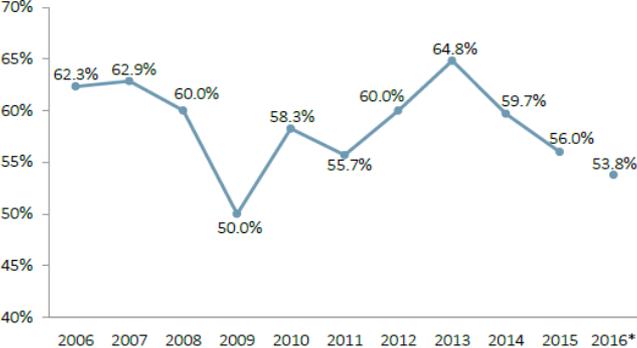
# Private Equity - Leverage

## Debt Percentages Declining

Median EBITDA multiples of U.S. buyouts



Median debt percentages for U.S. buyouts



➤ Borrowing Cost

Today		
1st lien	3-3.5X EBITDA	L + 500-550
2nd lien		L + 900-950

1Q16		
1st lien	3X EBITDA	L + 450
2nd lien		L + 1000

Mid 2015		
1st lien	3.5-4X EBITDA	L + 400
2nd lien		L + 750-900

- Opportunity – Direct lending strategies could take advantage of the void of traditional capital
- Higher volume of smaller deals – don’t require as much if any debt
  - Tuck in acquisitions

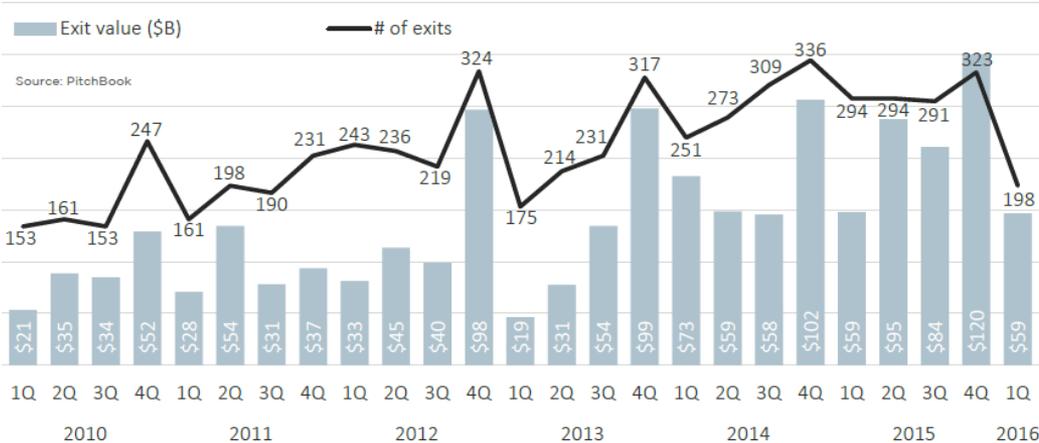
Graphs - Source: PitchBook as of 3/31/16  
 \* Figures are preliminary and are likely to adjust as more data is collected



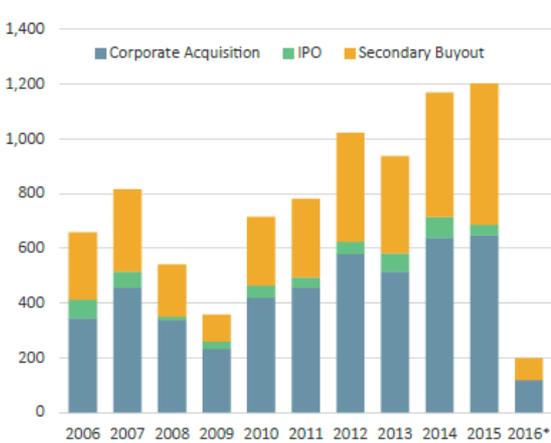
# U.S. Private Equity – Exit Environment

## PE-Backed Sales Plunge

U.S. PE-backed exit activity



U.S. PE-backed exits (#) by type



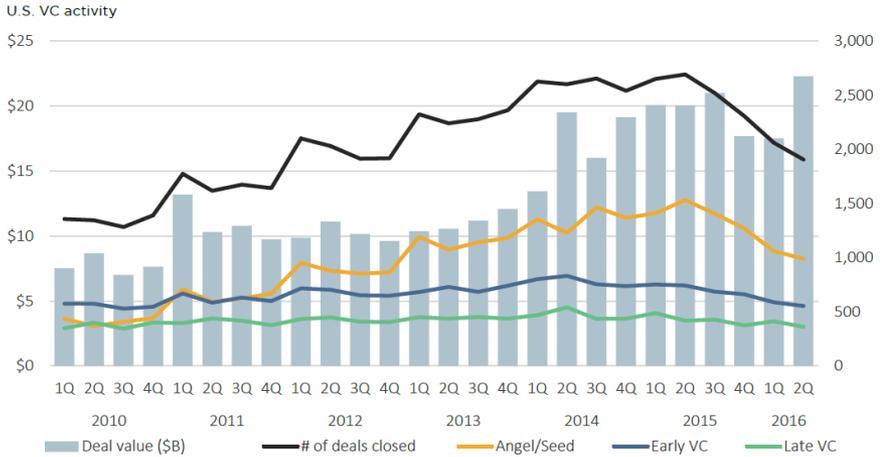
- 1Q16 PE backed exits decline sequentially → 39% on a transaction basis; 51% on a dollar basis
  - However, 1Q is typically a slower period
- Exits were down across the board – Corporate Acquisitions / IPOs / Secondary Buyout (other sponsors)
  - Noteworthy – Zero PE-backed IPOs → Market Uncertainties / Volatility

Source: PitchBook as of 3/31/16



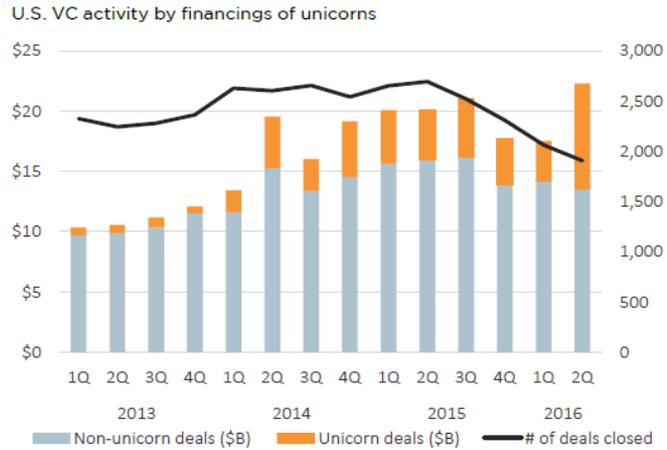
# Venture Capital – Market Activity

Activity is Mixed



- Deal volume has declined at every stage over the past year
- Capital invested has remained relatively robust

- Since 2014, “unicorns” have been responsible for much of the surge in VC invested
- VCs backing what they see as clear winners



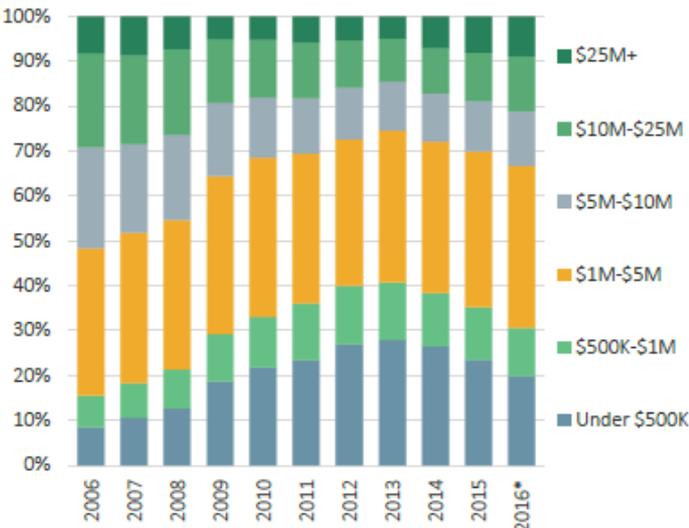
Source: PitchBook as of 6/30/16



# Venture Capital – Financing

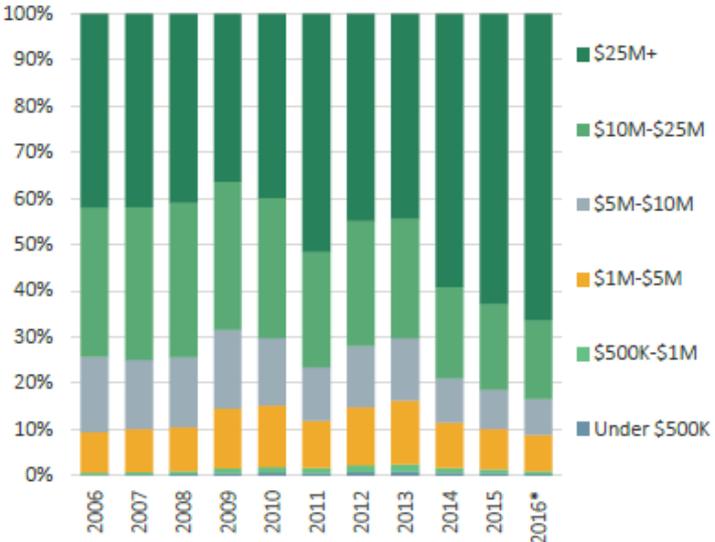
## Risk Aversion

U.S. VC activity (#) by round size



➤ A flight to quality continues to boost the proportion of large financings

U.S. VC activity (\$B) by round size



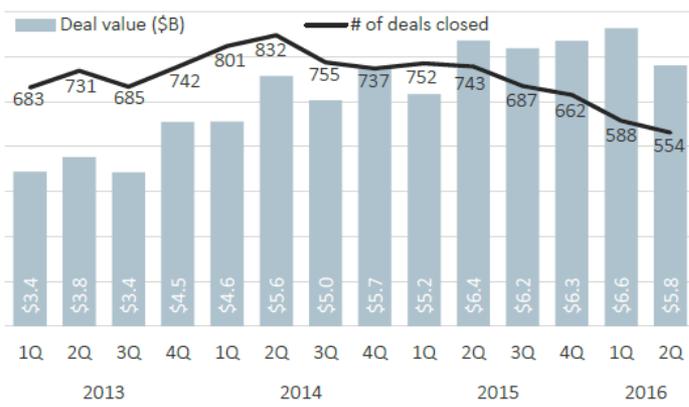
➤ A focus on more mature companies  
 ➔ \$25M+ financings accounting for over 2/3 of all VC \$ invested in 1H16

Source: PitchBook as of 6/30/16



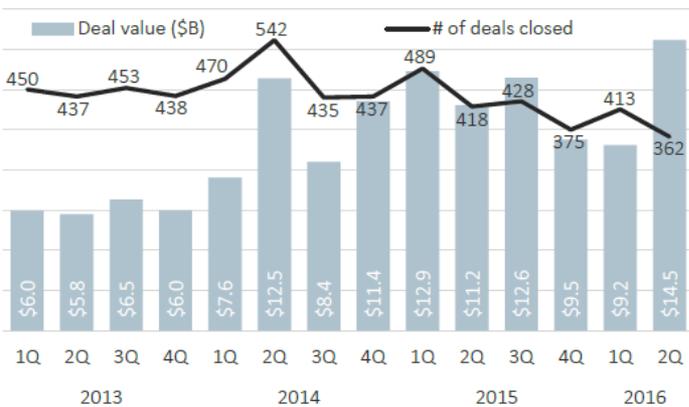
# Venture Capital – Financing

U.S. early-stage VC activity



- Earlier in the investment lifecycle, fewer companies are getting funded
- Those that can demonstrate healthy metrics are receiving larger rounds

U.S. late-stage VC activity



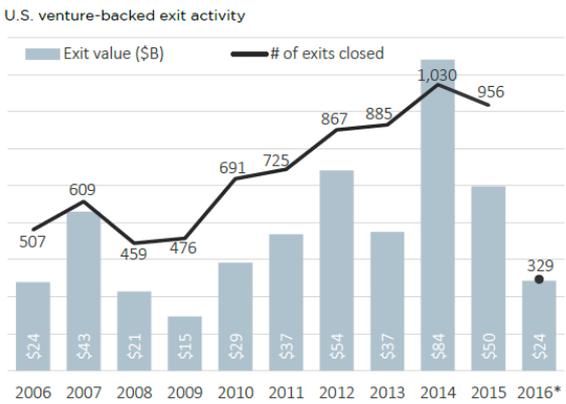
- At the late stage, highly successful companies continue to rake in large financing rounds

Source: PitchBook as of 6/30/16

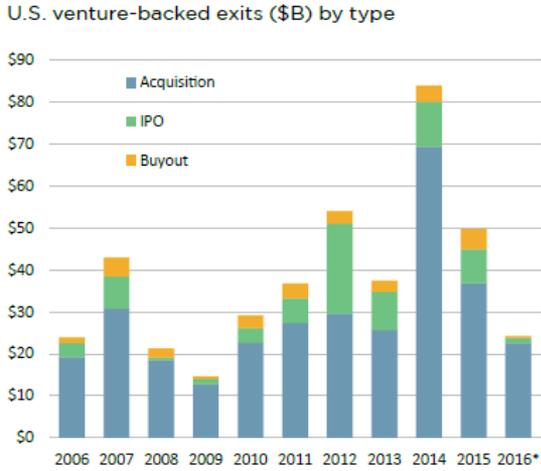


# Venture Capital – Exit Environment

Realizations Down / Exit Valuations Strong



- On pace to record the fewest exits since 2010
- Those that can demonstrate healthy metrics are receiving larger rounds



- Corporate M&A is rebounding somewhat
- The IPO backdrop is expected to remain weak given the macro unknowns

Source: PitchBook as of 6/30/16



# Current Initiatives

## ➤ Anticipated Commitments

- 2016: approximately \$1.5B of commitments
  - Year of Re-Ups
  - New Platforms
    - Co-Investment Platform
    - Secondary Platform
- 2017: approximately \$1.2B of commitments, and thereafter, pending actual flows/NAV

## ➤ Rationalization Analysis

- “Tail” Review
- Fund-of-Funds – restructure / decrease fees
- Non-Core relationships

## ➤ Special Programs

- Venture Capital Multiplier Fund – Escheat Fund



# Current Initiatives

<i>\$ in Millions</i>	2016				2017		
<b>Strategy</b>	<b>Closed</b>	<b>Pending</b>	<b>Identified</b>	<b>2016 Total</b>	<b>Identified</b>	<b>Potential</b>	<b>2017 Total</b>
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## “Core Strategy” Buyout Fund

- Focus on high quality, low volatility, established companies
  - Stable, predictable free cash flow generation
  - Companies looking for long-term business partners
  
- Investor friendly economics
  - Mitigated J-Curve
  - Co-Investment potential
  
- Longer-term hold periods
  - Returns insulated from economic and credit cycles





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