London Borough of Hillingdon Pension Fund
Adams Street Partners Update: Third Quarter 2012

Industry Update

Buyouts

Debt markets, particularly in the US, remain liquid. Sponsored loan volume for larger companies in calendar year 2012 surpassed levels experienced in all prior years but 2007. That said, nearly 60% of this activity in 2012 went toward refinancing and dividend recaps as opposed to new LBOs and/or outright acquisitions. Buyout loan volume has been most concentrated in the IT and service-oriented sectors, combining for just over 30% of the total. Earlier in the year, energy-related sectors played a much larger role in overall loan volume but the market has since become more diversified in its interests. Purchase price multiples for LBOs in general during 2012 are down modestly from 2011 levels, however there was a definite uptick during the fourth quarter. As has been the case for some time, multiples for larger deals are higher than those of smaller to medium-sized deals, although the year end increase was experienced consistently across the size categories. The equity component of these transaction prices (as opposed to the debt component) is now well below levels experienced during the financial crisis (when traditional debt financing was largely unavailable) but remain well above levels witnessed during the buildup of the credit bubble in the middle of the last decade.

Fundraising continues to be subdued relative to heights attained during the 2005-2008 vintage years. However, after bottoming in 2009 the pattern of year-to-year increases in global buyout capital raised since then continues to hold true in 2012 – despite what preliminarily appears to be fewer funds coming to market in 2012 than calendar year 2011. After several years of working through the overhang of capital raised in prior funds, large and even mega funds have begun to return to the market in the past year. While in many cases the managers have less aggressive fundraising targets than in prior, overheated, vintages, the average size of fund raised in 2012 increased. This pattern of fewer funds raising more capital was particularly the case in the US. In Europe preliminary indications are that fewer funds raised modestly less capital than they had in 2011 – a testament to the more challenging fundraising environment created by the region's macro-economic challenges.

Venture Capital

Venture capital fundraising and exit activity were also top heavy during 2012. Similar to the experience in buyout space, overall global venture capital raised during 2012 looks to have been flat to modestly up from 2011 levels, but the total was raised through fewer funds. The number of companies that had their IPO listed on US exchanges during 2012 was quite consistent with the number in 2011. Since one of those companies was Facebook however, the volume raised from the year's IPOs exceeded all prior years except for the internet bubble years of 1999 and 2000.

Through interaction with venture GPs in our portfolio as well as with our own Direct Investments team, we can see that deal flow remains solid in venture space. That said, we are cautious on price as valuations in certain areas of the technology sector (especially in enterprise SAAS, mobile, big data, and cloud computing) remain frothy. Healthcare pricing rarely appears to be an issue on the surface but, as always, a close eye must be focused on the near and long term viability of the drug, service or device being considered given the rapidly changing regulatory environment impacting the sector.

Adams Street has committed to a number of very interesting venture capital funds over the course of 2012. In the US portfolio our interests have spanned the size spectrum from smaller groups like seed investor Harrison Metal to larger diversified funds like NEA. In Europe we have recommitted to well-respected health care investor Abingworth and after an extended period of time researching the region have also made a recommitment to Israel-focused manager Pitango. In the emerging markets, contrasting with calendar year 2011 when most venture commitments were to managers in China and India, we made two commitments to interesting funds based in Brazil and one to a group focused on bridging business model arbitrage opportunities between China and Japan. Once again we are reminded that the characteristics of managers coming to market can differ quite significantly from calendar year to calendar year, and that successful private equity programs tend to be diversified across regions, sectors, managers and time.

Portfolio Statistics as of September 30, 2012

	Inception Date	Committed / Subscription	Drawn / Subscription	Drawn / Committed	Total Value / Drawn	IRR Since Inception*	Public Market	3Q12 Gross IRR
Total Hillingdon Portfolio	**02/2005**	**99%**	**78%**	**79%**	**1.17x**	**6.64%**	**2.62%**	**2.53%**
2005 Subscription	02/2005	100%	87%	87%	1.20x	6.82%	2.57%	3.15%
2006 Subscription	01/2006	100%	82%	82%	1.13x	5.87%	2.62%	2.56%
2007 Subscription	01/2007	100%	68%	68%	1.19x	9.67%	4.32%	2.38%
2009 Subscription	01/2009	76%	34%	44%	1.15x	19.47%	9.78%	2.13%
Direct Co-Investment Fund	09/2006	100%	96%	96%	1.02x	1.75%	0.16%	-1.52%
Co-Investment Fund II	01/2009	100%	39%	39%	1.45x	32.27%	9.32%	5.03%

*Gross of client's management fees paid to Adams Street Partners, LLC.

Note: The Public Market is the equivalent return achieved by applying Hillingdon's cash flows to the MSCI World Index.

Main Drivers of Performance

During the three months ended 30-September, public equity benchmarks bounced back from their negative absolute performance the prior quarter, with most markets generating returns in the mid-to-high single digits depending on location and industry concentration. Public market equity indices have exhibited a tremendous amount of quarter on quarter price volatility over the past eighteen months. Our private equity returns generally lagged the public markets' strong results during this three month period, but posted a solid 3.6% return.

Portfolio Outlook

Markets were bolstered by an increase in positive economic news flow in the US and Europe during the third quarter. In the US, an improved unemployment rate (albeit amid a reduced labor force) and growing indications of a housing market recovery outweighed continued uncertainty surrounding the November elections and potential implications of the since addressed "fiscal cliff". In Europe, news that the Central Bank is willing to support aid-seeking countries via purchases of their sovereign bonds also served to reduce some of the financial stress in global markets and encouraged more risk-seeking behavior amongst investors. This pattern of strong absolute returns continued into the final quarter of 2012, particularly outside the US.