London Borough of Hillingdon Pension Fund
Adams Street Partners Update: First Quarter 2013

Market Update

While equity markets overall continued their strong run into 2013, with the MSCI World Equity Index up nearly 8% during the first three months of the year, returns by market have begun to bifurcate quite meaningfully. Japan's Nikkei 225 had an incredible start to the year, up 20% for the first quarter on the back of a concerted monetary easing effort focused on containing deflationary pressure. US equities also performed well, up over 10% as evidence of a housing recovery, labor market improvement, consumer spending increases and solid corporate earnings combined to create positive momentum that attracted significant investor flows back into the market. European markets were generally higher, but less so than Japan and the US, as recessionary pressures evidenced by cuts in economic growth expectations, reduced ratings on sovereign debt and continued political pressure on governments to maintain public spending levels continued to weigh on investors' minds. Public equities in emerging markets struggled in the first quarter, generating negative absolute returns as the slowdown in Europe spread to its trading partners in other parts of the world.

Our private equity returns exhibited similar regional differences during the first quarter, with returns from US investments generally outperforming those in the developed and emerging markets. The pattern of less volatile quarterly valuation moves in private equity markets relative to those of public equities, which was discussed in last quarter's letter, appears to have continued with first quarter 2013 results.

Portfolio Statistics as of March 31, 2013

	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%**	**82%**	**82%**	**1.20x**	**7.04%**	**4.21%**	**2.47%**
2005 Subscription	02/2005	100%	89%	89%	1.22x	7.03%	3.95%	2.04%
2006 Subscription	01/2006	100%	85%	85%	1.16x	6.29%	4.26%	2.62%
2007 Subscription	01/2007	100%	76%	76%	1.21x	9.80%	6.26%	2.09%
2009 Subscription	01/2009	85%	43%	50%	1.15x	17.79%	12.78%	1.58%
Direct Co-Investment Fund	09/2006	100%	96%	96%	1.09x	2.97%	1.77%	4.01%
Co-Investment Fund II	01/2009	100%	49%	49%	1.45x	30.61%	12.00%	4.75%

*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

While we believe that economic growth and the availability of debt financing in certain parts of the world will continue to be modest over the next few years, there are attractive private equity investment opportunities in each of our target markets. Around the world we are finding managers with the ability to invest in companies with substantial growth opportunities, irrespective of the economic cycle, due to their ability to add value to their investments by providing managerial and operational support. Historically, private equity returns have been generated by growth, debt pay down, multiple expansion, and knowledge arbitrage (i.e., leveraging industry and/or market expertise). However, in a slower growth world, it is more difficult to expect broad-based growth across all sectors of the economy, ever-increasing valuations, or robust debt markets to consistently generate attractive returns.

Portfolio Outlook

We recognize that economic and market cycles have a significant impact on **buyout** returns. As a result, Adams Street focuses on buyout strategies that are less dependent on the macroeconomic environment or financial/credit markets to be successful. We invest with general partners that can identify growth and add value to their portfolio companies beyond applying leverage to balance sheets. Typically this value is more easily applied to middle market companies (less than USD500 million in revenue) where management teams can be augmented with successful professionals that are a part of the general partner's network. These management teams and the private equity owners are then able to work together to implement operational and/or strategic improvements to create value. Additionally, the company level investment opportunity set at the middle market segment tends to be more plentiful, with less efficient pricing, resulting in increased potential for reasonable valuations at time of purchase. Our experience points to the fact that small to mid-sized buyout transactions have generated more attractive realized multiples than large and mega-sized deals over numerous economic and market cycles. Across the PE opportunity set, we are attracted to strategies that inherently have multiple exit paths for their portfolio companies. Businesses that have a large pool of potential acquirers tend to be realized more quickly and at higher prices than others, so we want to invest in strategies that produce a healthy mix of M&A and IPO candidates.

When **co-investing** into portfolio companies alongside buyout and growth managers we know well, we simultaneously look to take advantage of robust deal flow while remaining cautious on our revenue assumptions. Although most general partners that Adams Street backs continue to see their funds oversubscribed, the more difficult fundraising environment for the industry overall creates a need for equity co-investors like us. We continue to lever Adams Street's relationships with general partners to position us as a "first call" for co-investment opportunities, thereby allowing us to selectively choose those portfolio companies where pricing allows for meaningful upside potential given reasonable growth assumptions.

In **venture capital**, we invest in managers that have demonstrated the skill and ability to leverage industry and geographic market expertise. While there are pockets of secular change in all market segments driving the growth of markets or changing the composition of spending, the largest changes are driven by technological innovation, business model innovation, and/or execution-oriented growth, which scales proven business models. Venture-backed firms should be able to generate attractive returns with more capital efficient business models and diminished start-up costs. Our 3 to 4 year forecasts include investments in managers that have access to top entrepreneurs and target enterprise infrastructure, internet applications and enterprise software companies.

When **investing directly** into venture capital and growth equity backed portfolio companies, our strategy in technology focuses on more price-rational, less traveled markets. We do not rule out stretching for what we view to be outstanding investment opportunities, but recognize that the market is still frothy in certain areas like mobile, software as a service, cloud and big data. The life science market is full of its own challenges, but we believe it's a good time to be identifying and backing winners in the space. We seek to do so by targeting companies with a high probability of clinical success or by focusing on healthcare service opportunities where success is driven by non-clinical factors.