London Borough of Hillingdon Pension Fund
Adams Street Partners Update: Third Quarter 2009

Industry Update

Despite returning investment optimism, the venture business is in the process of right-sizing due to scarce LP capital and poor 10-year returns. We are hearing plenty of stories about GPs who are unable to raise funds, who raise smaller funds than targeted, and who have initiated personnel restructurings. Capital is hard to come by, fewer new companies are being started, and money is increasingly finding its way into companies demonstrating rapid growth. While painful for those that do not attract adequate funding, we view this as a positive for the health of the business long-term and are optimistic about the prospects for future attractive returns.

Bank lending remains tight, but new deals are getting financed, albeit with less leverage and with more lenders needed to accomplish the financings. When more parties are involved it can cause deals to progress more slowly. This has created a new set of lenders (including the buyout managers themselves), replacing those lenders that were badly burned in the peak of the cycle, namely CLOs, large institutional investors, and hedge funds that purchased the senior and secured loans sold down by the banks. Whereas many in the buyout business believed that the days of covenant light financing were a thing of the past (ourselves included), we have heard anecdotes of those terms returning to the market today. Creative financing is required, particularly where larger amounts of leverage are concerned.

Portfolio Statistics

	Committed / Subscription	Drawn / Subscription	Drawn / Committed	Total Value / Drawn	IRR Since Inception*	Inception Date
Total Hillingdon Portfolio	94%	56%	60%	0.86x	4.12%	02/2005
U.S. Partnership Program	95%	55%	58%	0.88x	-2.79%	02/2005
Direct Subscription	100%	74%	74%	0.75x	-8.04%	01/2006
Non-U.S. Developed Partnership Program	92%	57%	62%	0.92x	-1.06%	03/2005
Non-U.S. Emerging Partnership Program	12%	2%	16%	0.61x	-8.53%	03/2009
2005 Subscription	100%	67%	67%	0.91x	-1.10%	02/2005
2006 Subscription	100%	58%	58%	0.83x	-5.86%	01/2006
2007 Subscription	85%	37%	44%	0.90x	-1.18%	01/2007
2009 Subscription	20%	4%	18%	0.92x	14.39%	01/2009
Direct Co-Investment Fund	100%	89%	89%	0.68x	-17.37%	09/2006
Co-Investment Fund II	100%	9%	9%	0.98x	1.11%	01/2009

*Gross of client's management fees paid to Adams Street Partners, LLC. Internal rates of return are not calculated for fund less than one year old; instead the return is the change in value over amount invested.

Main Drivers of Performance

Unlike January in Chicago, the private equity market has begun to thaw out with some increase in deal activity and selective exits for companies that have made it through these challenging economic times. Not surprisingly, Adams Street's portfolio has seen three consecutive positive quarters of valuation write-ups as the public markets have leapt off their March 2009 lows. The third and fourth quarter saw a number of successful exits in the broad Adams Street private equity portfolio that ultimately drove some of the recent distributions that many of our investors have received. The exits came from a diverse set of industries and geographies. These exits are significant and commendable under normal market conditions, but given the uncertainty and headwinds in today's financial markets, they are quite extraordinary. While it is premature to begin packing away the hats and sweaters and donning swimsuits, we are encouraged by the activity and warming mood displayed by our General Partners and portfolio companies.

M&A activity picked up as large tech companies seek accretive growth through acquisition. Amazon's $930M purchase of Zappos was the largest deal of the third quarter and VMWare's $420M purchase of SpringSource (in ASP's portfolio) was the second largest. While tech stocks outperformed the market in the first nine months of 2009 (NASDAQ up 35%; S&P 500 up 19%), the third quarter was a dead heat with both indices up about 15%. The NASDAQ's strength, coupled with an improving M&A climate and an open but selective IPO window, is causing fear to slowly dissipate.

Portfolio Outlook

The buyout activity can be characterized as a move from playing defense to playing offense. Problem assets from the last few years have been written off in the worst cases or in better situations, restructured by extending the debt maturities, allowing companies the time to get back on their feet. General Partners, with most of the fires under control, are looking at attractive entry multiples for new deals and relatively inexpensive debt. On top of that, economic data is showing improved health which provides optimism for future growth.

Underpinning the activity is the low interest rate environment that many developed economies have maintained for fear of hindering their recoveries or worse, risking a retreat back into recession. Almost 800 stimulative policy initiatives have been announced around the world, providing temporary support for businesses. The stimulus has undeniably helped create a warming trend, however many are left to wonder if the winter frost will return once governments return to less accommodating fiscal policy.