CanterburyConsulting

Quarterly Asset Class Report

Private Equity

canterburyconsulting.com

September 30, 2019

Role in the Portfolio

Canterbury Consulting recommends a diversified portfolio of private capital strategies. Consistently committing to private capital drives long-term asset growth, net of inflation, by taking advantage of the illiquidity premium derived from inefficient markets and superior manager selection.

— Canterbury blends strategic and opportunistic approaches to construct private capital portfolios that are diversified by sector, geography, and vintage year.

- Strategic: Using various market inputs to form a baseline, we create a recommended model portfolio allocation.
- Opportunistic: We combine top-down and bottom-up analysis to achieve excess risk-adjusted returns through market intelligence and superior manager selection.

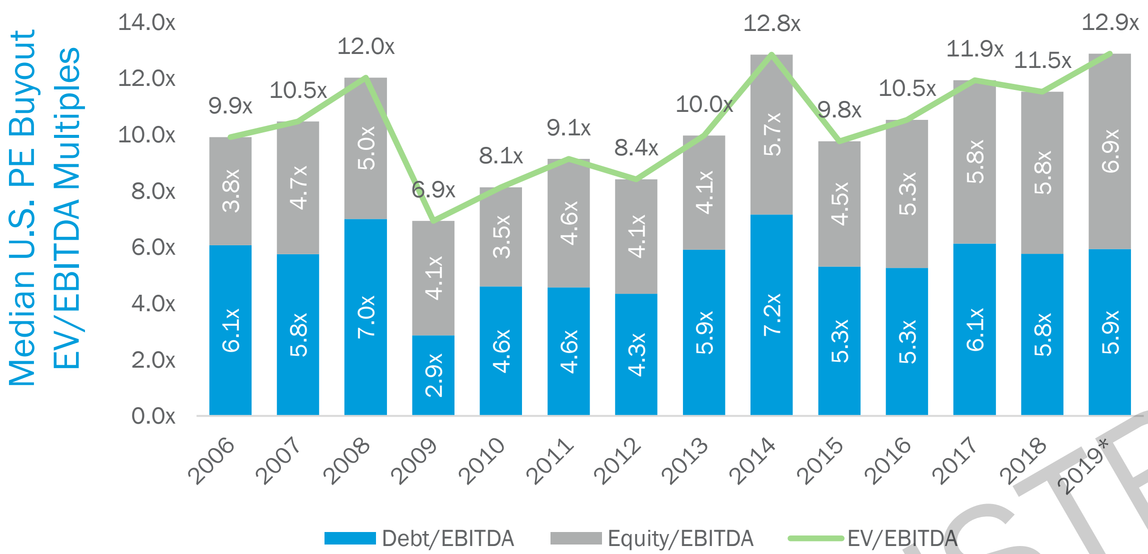
Role	Asset Categories	Risks
Growth	Public and Private Equity	Market Decline
Capital Preservation	Fixed Income, Hedge Funds	Rising Interest Rates, Highly Correlated Markets
Inflation Protection	Real Assets: Real Estate, Commodities	Deflation

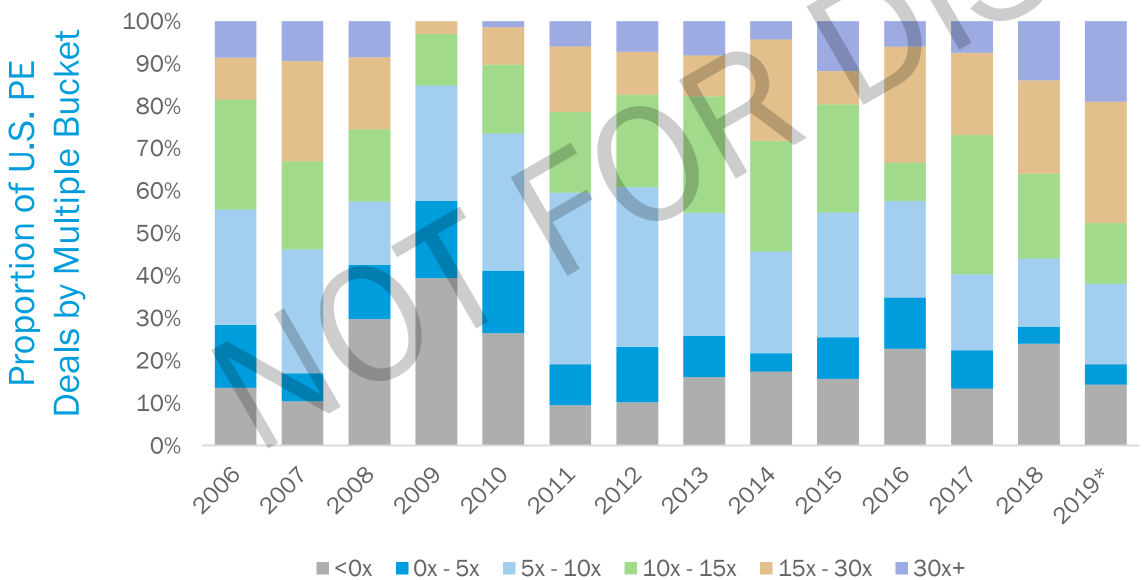
— Over a full market cycle, private equity is intentioned to generate above-market returns commensurate with risks associated with the asset class (i.e., illiquidity, time horizon, etc.).

— Given the length of the time required to deploy capital and constant evolution of the opportunity set, investors in private equity must commit consistently across cycles and avoid “market timing” in order to generate returns.

U.S. Private Equity Valuation Overview

Private Equity



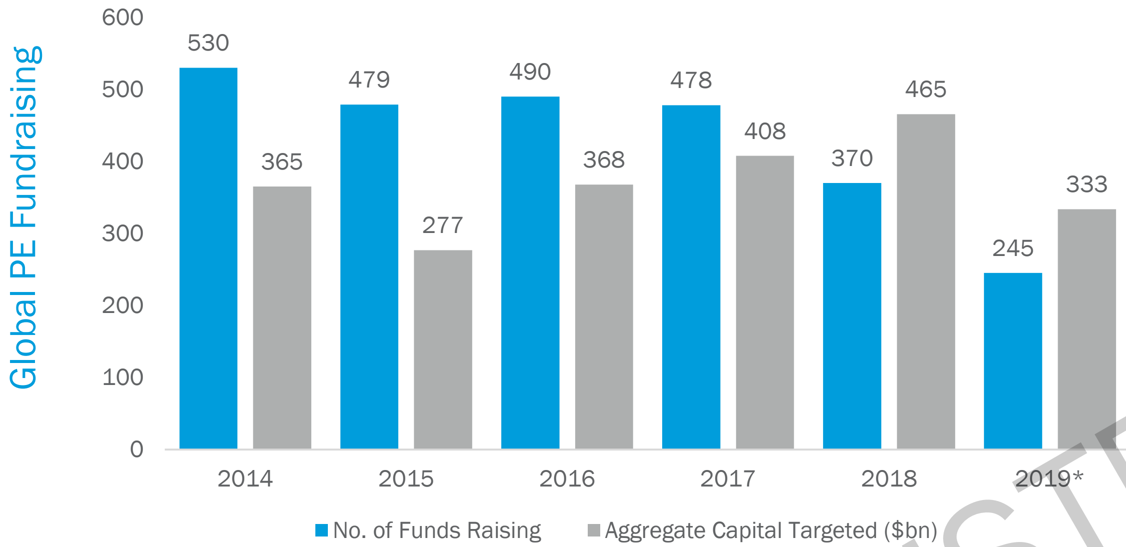


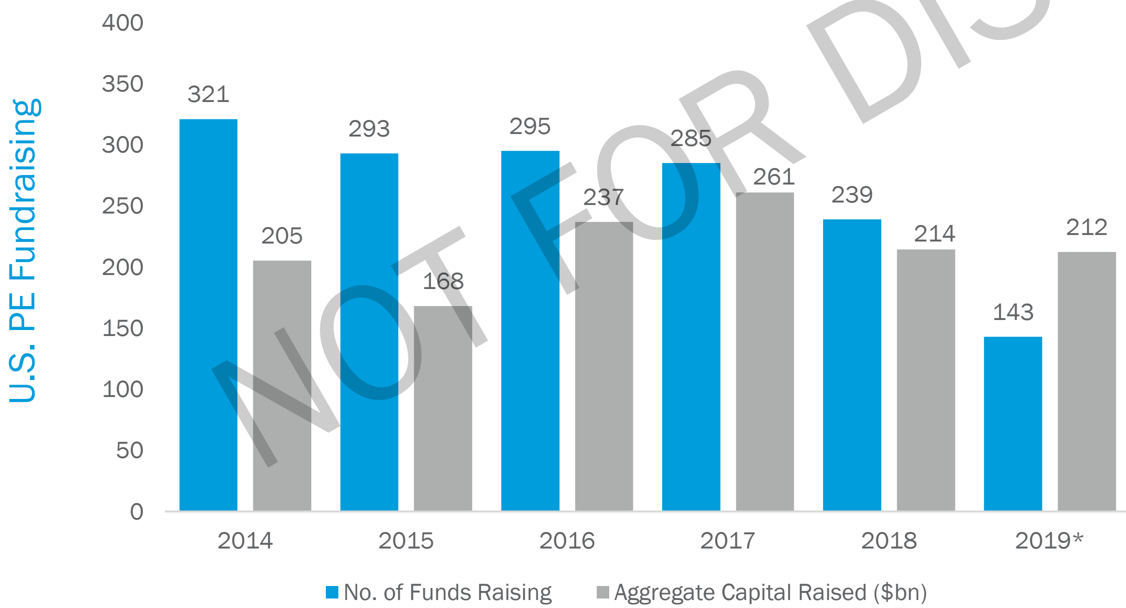
- U.S. median private equity buyout multiples have been on an upward trend since 2015, now slightly exceeding 2014 levels. The strength of public markets in 2019, as well as increased levels of private equity commitments and competition, continue to apply upward pressure on buyout multiples, leading to a higher proportion of deals priced above 15x. Additional factors that have contributed to the run-up in private equity multiples include:
  - **High levels of low-priced debt in the private equity market:** The continued attractive lending terms, as can be seen through the Fed's accommodative monetary policy, have been an instrumental part of private equity transactions. Increased equity dollars have also been important, as investors are seeking higher yielding investments and increased diversification. This has contributed to higher debt levels from prior years.
  - **Increased fundraising activity in the buyout space:** The increased dollars raised and current level of dry powder have increased the competition for assets throughout the private equity markets, propelling deal multiples upward. In Q3 alone, Blackstone and Vista Equity Partners closed on their latest flagship buyout funds, raising over $40 billion of combined commitments.
  - **Pursuit of higher growth sectors:** PE firms have been investing more capital in higher growth sectors, such as IT and healthcare, which trade at higher multiples.

Source: PitchBook Q3 2019 U.S. PE Breakdown

**2019 figures are through 09/30/2019*

Private Equity Fundraising Activity





- The number of global private equity funds raising capital has steadily decreased between 2014 and 2019 while the average fund size has increased from $689 million to $1.4 billion over this same time period. This has been partially driven by a number of large fund closings, but also the shift of large LPs, such as public pensions, to consolidate their GP relationships.
- As of the end of the quarter, venture funds comprised approximately 41% of total global private equity funds in market, followed by buyout and growth/expansion funds, which accounted for one-third of funds in market. However, buyout and growth/expansion funds accounted for almost 60% of the total capital targeted.

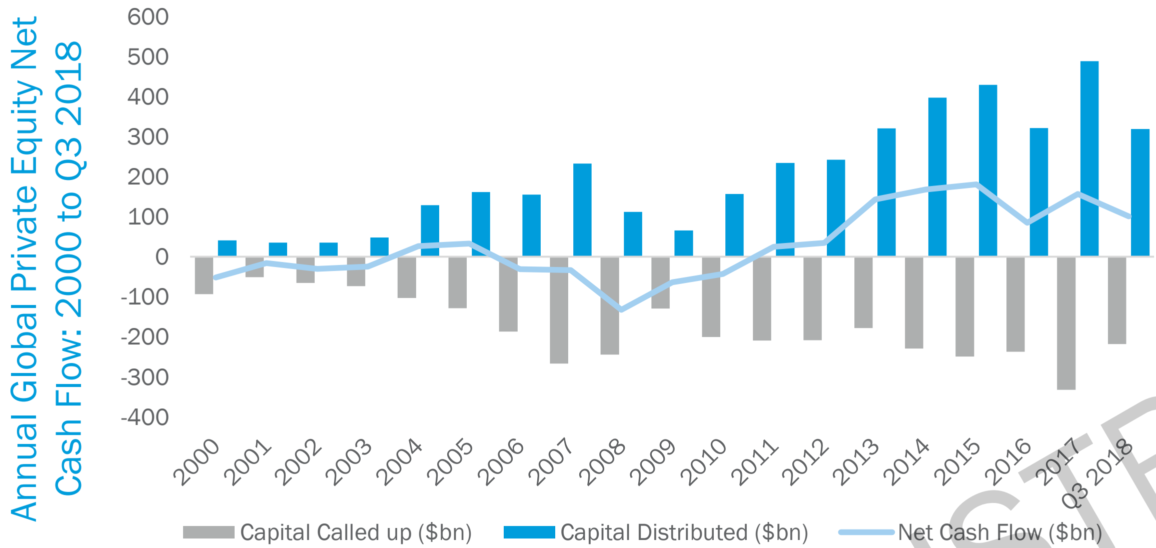
Source: PitchBook

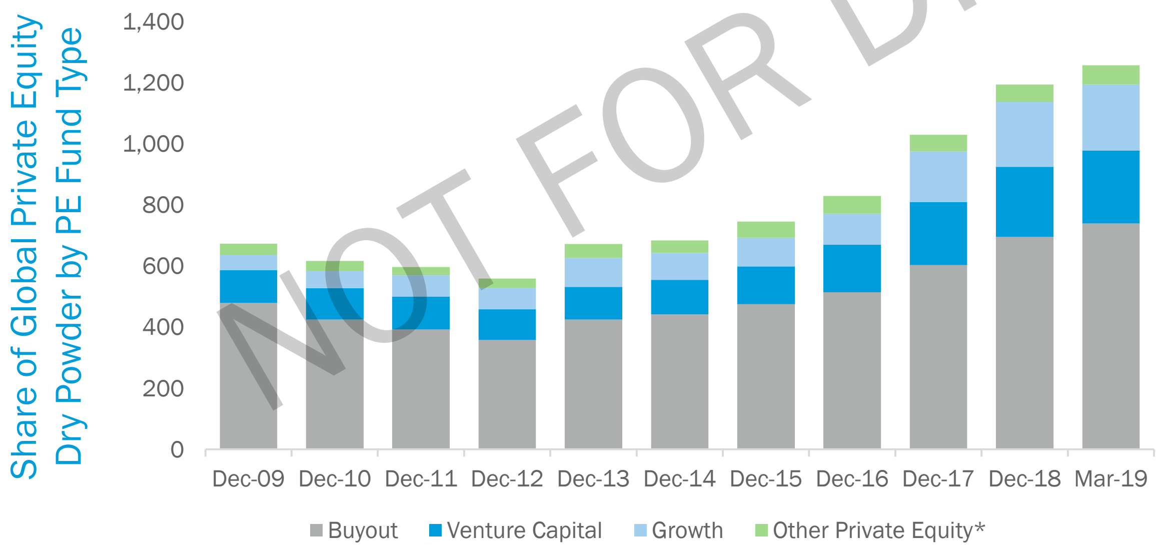
Private equity funds include: buyout, growth/expansion, diversified private equity, mezzanine, secondaries, co-investment, restructuring/turnaround, venture capital, private debt, energy, real estate, and fund of funds

**Figures are through 09/30/2019, unless otherwise noted*

Global Private Equity: Performance and Dry Powder

Private Equity



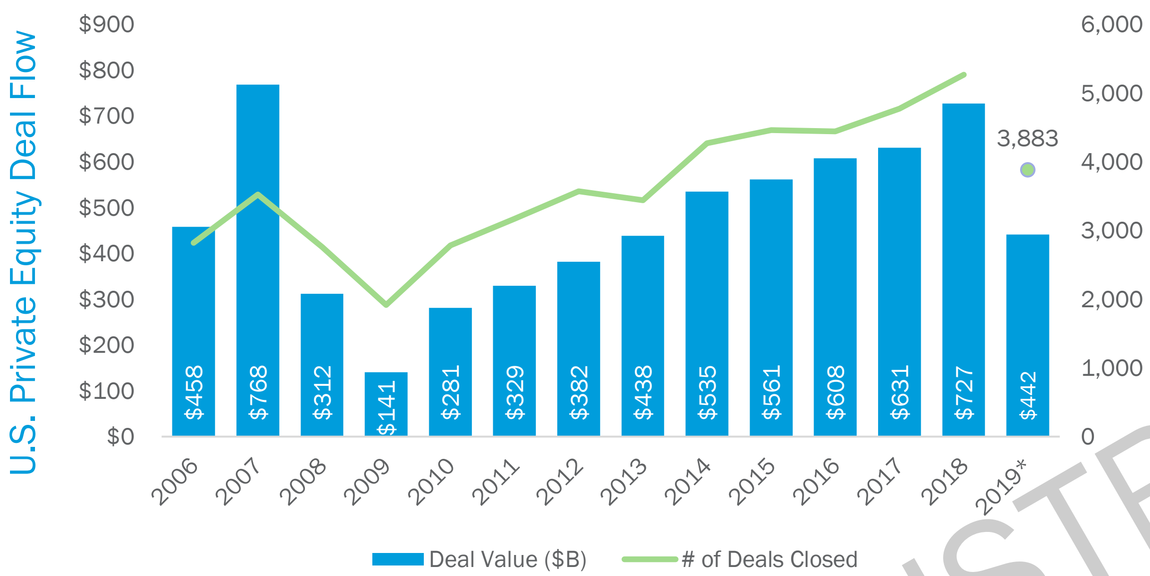


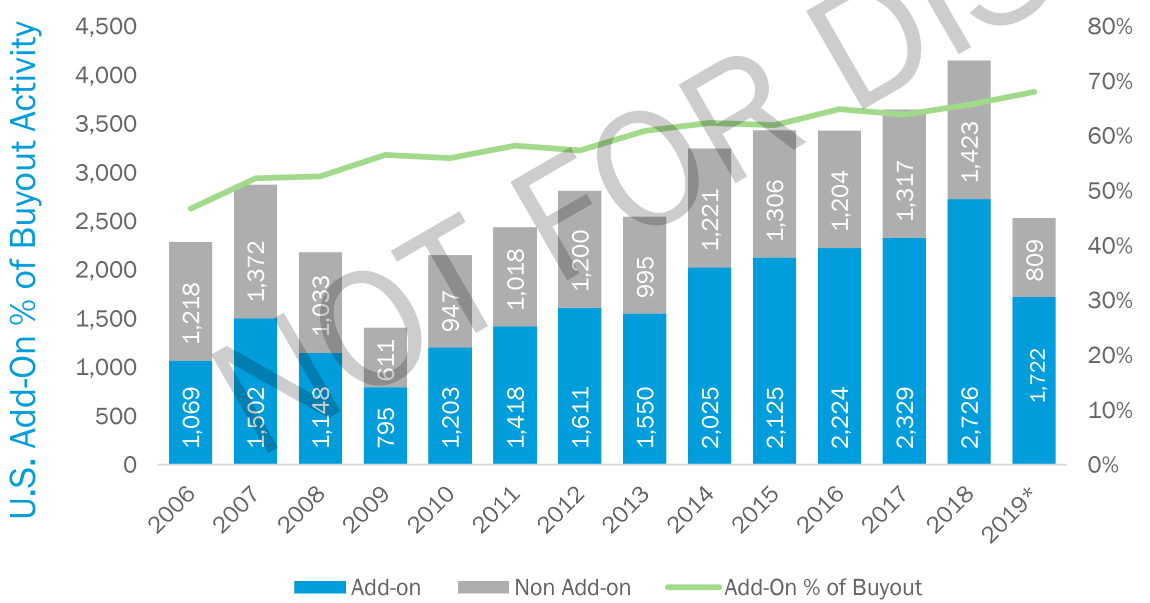
- LPs have experienced positive net cash flow for the eighth consecutive year, which is indicative of the strong exit activity among private equity funds late in their fund life. More recent fund vintages are seeing opportunities to exit out of their positions earlier than expected.
- Despite the continued trend of positive net cash flow to LPs, contributions will likely increase commensurate with the levels of dry powder and the increasing number of mega funds either closing or coming to market.
- As of the end of Q1 2019, private equity dry powder is approaching the $1.3 trillion mark.
- 59% of total dry powder is currently allocated to buyout funds, followed by venture (19%) and growth (17%) funds.

Source: PitchBook 2019 Global Fund Performance Report; bottom chart reflects data as of 03/31/19

**Other Private Equity includes balanced, co-investment, co-investment multi-manager, direct secondaries, and turnaround funds*

U.S. Private Equity Deal Activity



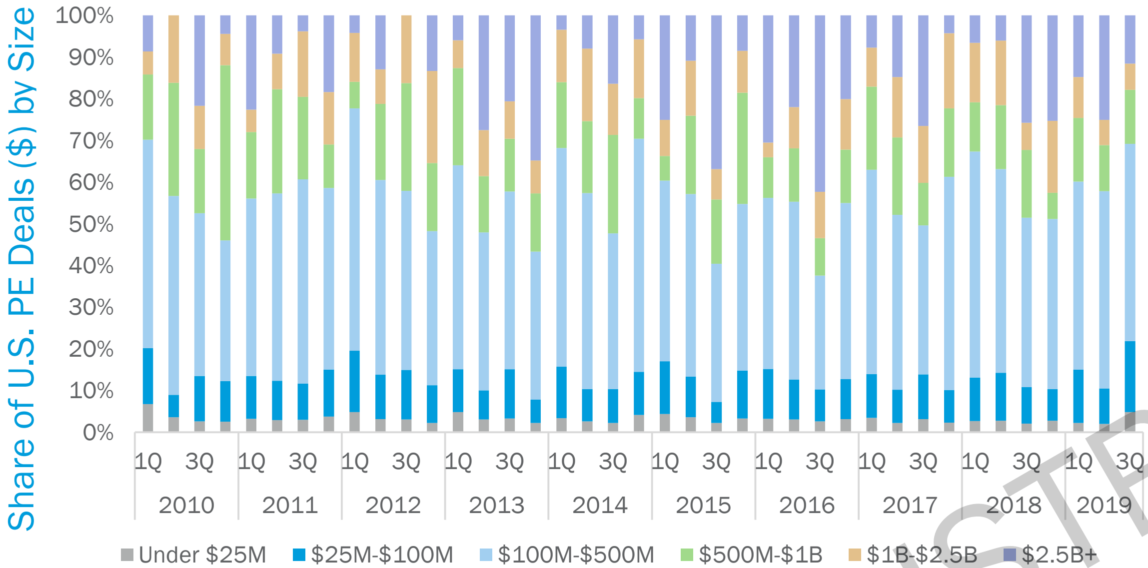


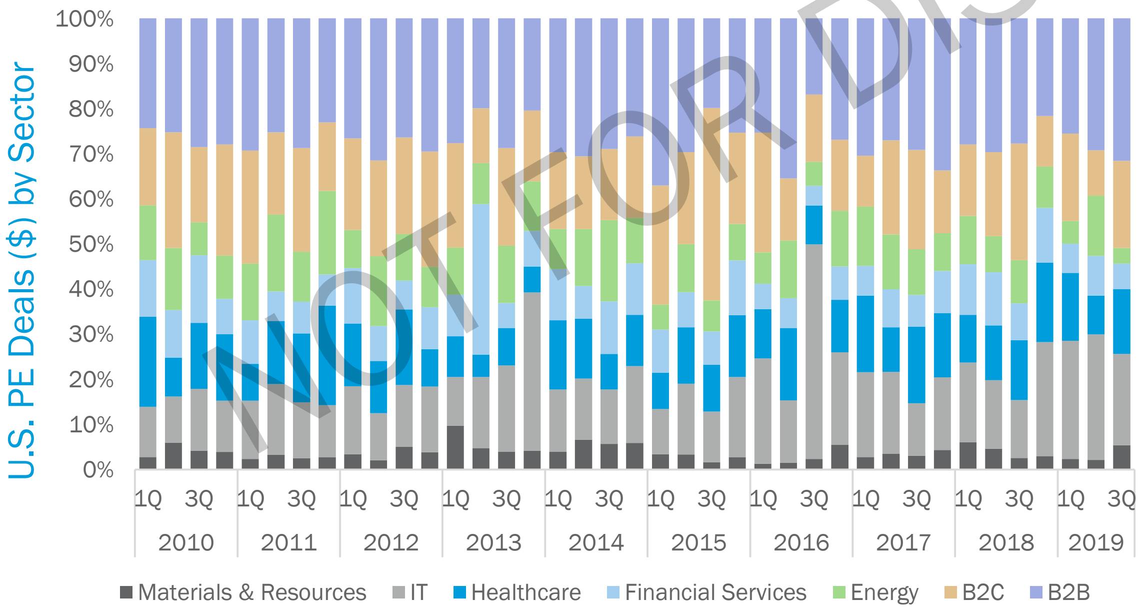
- Throughout Q3, the number of private equity deals closed kept pace with 2018 levels. Private equity deal flow should be expected to continue at this pace given the current fundraising environment.
- Increased levels of dry powder, coupled with elevated multiples, have prompted GPs to focus on downside protection and distinct value-add capabilities when sourcing prospective deals.
- Add-ons continue to account for over two-thirds of all buyout activity as of Q3, with PE firms focusing on the lower middle market as a source of add-on opportunities. Add-on acquisitions typically have more attractive entry prices and are often acquired to drive operational improvements, as well as blend down the total purchase multiple.
- In connection with high buyout entry multiples, GPs have continued to emphasize operational improvements rather than financial engineering or multiple expansion as a means of driving performance.

Source: PitchBook Q3 2019 U.S. PE Breakdown
**2019 figures are through 06/30/2019*

U.S. Private Equity Deal Activity

Private Equity

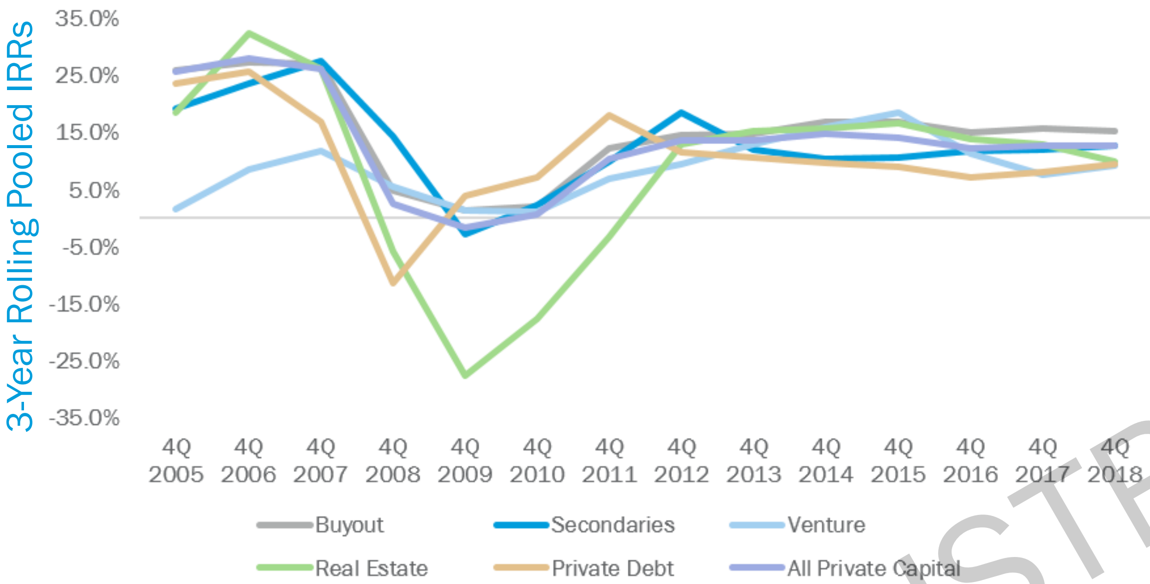


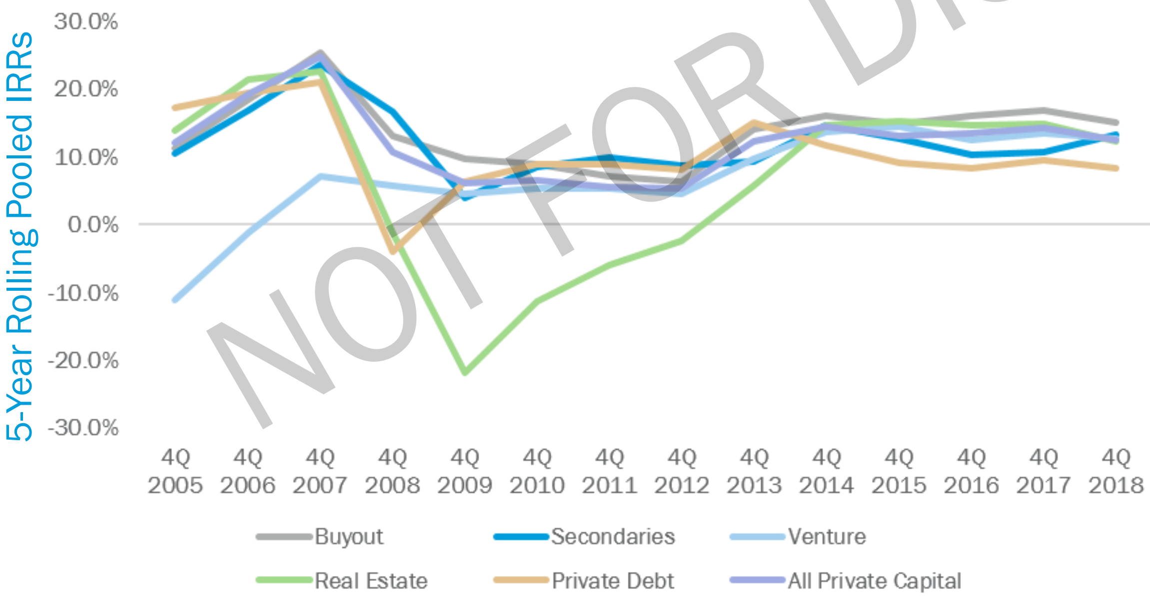


- As of Q3, nearly half of private equity deal activity in the U.S. comprised deals valued at $100 million to $500 million. Despite the lower-than-usual proportion of deal flow in excess of $1 billion during the quarter (only 18% versus 33% a year ago), we should expect deal volume in this size range to increase over the next few quarters, especially given the closes of Blackstone and Vista's flagship buyout funds this quarter. One mega-deal that is expected to close next quarter is the $8.4 billion take-private deal of Genesee & Wyoming.
- The B2B and B2C sectors continue to be attractive sectors to invest in among PE firms, accounting for over half of total deal value (in dollar terms). This is well above the 39% share experienced in the previous quarter.
- A growing sector for private equity deal activity has been financial services. What makes this sector appealing, from both a debt and equity perspective, has been the recurring revenue and high free cash flow characteristics inherent in these companies' business models.

Source: PitchBook Q3 2019 U.S. PE Breakdown
2019 figures are through 09/30/2019

Horizon Performance





- Since Q4 2010, the volatility in private equity markets have stabilized compared to what took place leading up to and during the Global Financial Crisis (GFC). Buyout funds have remained the top performer over three- and five-year time horizons. The current private equity market favors buyout funds whose portfolio investments have benefited from value-add operational improvements.
- Private real estate fund performance struggled as a result of the GFC and remained a significant underperformer until the latter part of 2013 on a trailing basis. Since then, performance has improved in large part due to a continued low-rate environment and low levels of defaults.

Source: PitchBook; data as of 12/31/2018