Hollyport Capital LLP
75 Davies Street • London • W1K 5HT
T: +44 (0)20 7016 3370 • F: +44 (0)20 7499 3758
www.hollyportcapital.com

HOLLYPORT CAPITAL

Newsletter Summer 2008

Hollyport Capital acquires a £10 million Portfolio of mature private equity fund interests

Hollyport Capital has purchased a portfolio of 36 interests in mature private equity funds from a major European investor.

As a result of a desire to focus on its more recent and higher value private equity fund investments, the vendor wished to realise this portfolio of legacy interests. Through increased commitments to larger funds, the vendor's legacy assets had fallen to a very small proportion of its overall private equity commitment, but continuined to be a disproportionately high administrative burden.

The Portfolio comprised investments made predominantly in the 1990's in funds covering buyout, growth capital and technology in Europe, the USA and Far East.

Hollyport Capital undertook a full evaluation of all the fund interests in a short time in order to meet the vendors' requirement for a rapid response. Hollyport Capital also offered the facility to manage the transfer of all the fund interests, thereby providing a clean solution for the vendors.

This acquisition is the first investment to be made by CSP Secondary Opportunities II Unit Trust, the most recent specialist secondary fund raised by Hollyport Capital. Investors include Graphite Enterprise Investment Trust plc, others institutional investors, family offices and high net worth individuals. Fund II will acquire investments across a range of legacy private equity assets including both fund interests and direct investments. Hollyport Capital specifically seeks legacy assets which have become non-core for their owners.

John Beatty, commenting on the acquisition said, "The Partners of Hollyport Capital have undertaken a wide variety of roles in private equity over many years. Through our direct investment skills, advisory experience and fund investing knowledge, we are able to find creative solutions to the problems that often arise when funds reach the end of their intended life. We are pleased that all our investors from our first fund have supported us in Fund II and also welcome our new investors."

If you would like to discuss our activities in more detail, please contact John Carter at Hollyport Capital.

Hollyport Capital provides feeder fund for TA Associates latest fund

Hollyport Capital has formed a feeder fund to allow high net worth individuals to access TA A&P VI, the latest fund launched by Boston based TA Associates

TA Associates started investing in private equity in the 1970's, and over nearly 40 years it has acquired an outstanding reputation for consistently delivering top quartile investment returns.

TA Associates closed its latest fund, TA A&P VI, last November with commitments of $1.75bn. Due to the firm's outstanding investment record, the fund was heavily oversubscribed, with existing investors being given priority.

As a result of its investments in previous TA funds, Hollyport Capital was able to secure an allocation to TA A&P VI, which it offered to its clients. Twenty five of Hollyport Capital's investors participated in this fund, which offered them unique access to one of the world's leading private equity managers.

If you would like to discuss opportunities to access funds managed by the leading global private equity firms, please contact John Beatty at Hollyport Capital.

Hollyport Capital offers feeder fund for CVC European Equity Partners V €11bn Fund

Following the success of its TA feeder fund, Hollyport Capital has formed a feeder fund for the latest European fund being raised by CVC.

CVC has an enviable record of producing excellent returns for its investors in all of its funds through many economic cycles. The latest fund will follow CVC's proven business model, and is positioned to take advantage of the anticipated highly favourable pricing environment over its investment period.

The Hollyport Capital feeder fund is open to Hollyport Capital clients wishing to access CVC V, but who are unable to meet CVC's minimum commitment level of €20m.

If you would like to discuss participating in this fund, please contact John Beatty at Hollyport Capital.

Market Commentary

The start of 2008 has seen a steady flow of bad economic and financial news, with continuing uncertainty in credit markets and signs that there are increasing downside risks to the global economy. These trends are likely to increase pressure on private equity backed businesses. In this environment, how should the experienced private equity investor respond?

There are now tentative signs that the fall out in capital markets at the turn of the year may now have stabilised, and some commentators are starting to talk about the worst being over. However, the real risk now is the extent to which the ongoing shortage of credit feeds through to the real economy. Leveraged buyout debt continues to trade at a significant discount to par, anticipating a substantial rise in default rates. If default rates do increase, this has significant implications for highly leveraged private equity backed companies and the funds which hold equity in them.

The key question for private equity managers and investors is: how bad will the fallout be? Will we see leveraged buyout funds suffering a similar fate to venture funds following the collapse of NASDAQ in 2001? The driver of losses on those investments was the collapse in enterprise values (remember the 90% club?). No one is now forecasting similar declines in company valuations. But, where businesses have been bought on historically high earnings multiples funded by record levels of debt, it only requires a relatively modest decline in enterprise values to have a substantial impact on the value of the equity.

The immediate threat to leveraged companies is a decline in operating profit sufficient to breach covenants, causing debt defaults. While in some more recent transactions the use of ‘covenant lite’ structures may defer the day of reckoning, it will not change the basic arithmetic. In such circumstances, the equity holders will be fighting a rearguard action to avoid write-offs. Private equity managers will have to commit substantial resources when attempting to recover value from such investments.

The challenging environment of the next few years has the potential to result in significant change amongst private equity managers. Some will be badly hit by their fund’s underperformance impacting their business model. Others might see substantial turnover in personnel driven by diminishing prospects of carry - experienced partners may retire and aspiring lower ranking executives seek better opportunities elsewhere. Some private equity mangers are likely to emerge from this with reputations enhanced; others will struggle to raise their next fund.

How should the long term investor in private equity respond to this changed environment? Distributions from existing funds are likely to fall substantially as exits dry up. Portfolio losses are likely to rise, eroding the excellent returns that have been achieved in the past few years. At the same time, new investments written in the current environment are likely to benefit from lower entry pricing driven by the reduced availability of leverage, lower profit expectations and lower vendor price expectations given falls in comparable quoted businesses. If history is repeated, 2008 vintage funds could deliver excellent returns.

Bolder private equity investors will see this as a time to take stock of their current fund positions, and look to rebalance their exposure. The development of the secondary market has enabled investors to sell a wide variety of portfolios of private equity investments at competitive prices (to an extent that was not available in the Tech downturn of 2001-2003). Indeed, the record amounts raised by secondary funds in 2007 means there is no shortage of buyers. An example of such an approach is the recent sale by CalPERS of a portfolio of over 50 legacy fund interests with a reported value of $3bn. Investors who take a particularly negative view of the immediate outlook could sell a portion of their existing portfolio in the secondary market to effectively hedge the returns of the last few years and provide additional investment capacity for current vintage funds.

The message to private equity investors is to recognise that the benign conditions that led to the exceptional returns enjoyed recently have changed. The new environment will present significant challenges for some business models, but create substantial opportunities for others. In such circumstances investors should hold their nerve, but be rigorous in their selection of managers to back. Those that are bold in their review of current relationships, and incisive in their selection of new relationships with the potential to outperform at this stage in the cycle, are likely to reap the greater rewards.