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Executive summary

Balance is returning to private equity. Exits are starting to gain traction, fund-raising conditions are improving, and developed and emerging markets activity levels are poised to both rebound and even out.

Last year marked the start of a rebalancing as economic conditions improved in developed markets while the rapid growth rates in many emerging markets slowed. PE investments reached a steady state in 2013 and are expected to rise moderately over the coming year. At the same time, increased availability of debt on very attractive terms, coupled with an increase in dry powder, might suggest a return to pre-crisis days. Nevertheless, concerns around valuations, greater competition for assets and a relatively low level (supply) of targets will likely keep the market in check.

The most compelling story for 2013 was the return of the IPO market for PE-backed companies. Seeking out strong opportunities in the US and Europe, public markets investors have welcomed PE-backed companies with open arms. PE has opportunistically taken advantage of receptive market conditions and is finally now able to exit some of its largest portfolio companies, many of which date back to pre-crisis times. This is beginning to restore balance to PE portfolios, offering relief to aging investments.

The development of new exit routes in emerging markets is another key feature of 2013. While IPOs had been the mainstay of markets such as Asia-Pacific until recently, the options are broadening out as trade sales increase and a proportion of exits and secondary buyouts become more common. In Africa, meanwhile, the predominance of sales to corporates has lessened over the last year, while private sales and secondary buyouts are on the rise as a proportion of exits. Overall, PE firms in emerging markets are managing to balance exits across the main available routes rather than relying too heavily on a single type of realization.

Stability is also returning to the fund-raising markets. Developed market totals are up, while emerging markets funds are now focused on deploying the high amounts of capital they’ve raised. After a period of strong growth in emerging market fund-raising, LPs are now seeking to build a broad geographic spread of commitments across developed and emerging markets. This is restoring some balance to the outlook for fund-raising.

There likely will still be volatility in the markets. Concerns about the sustainability of the economic recovery prevail, and the effect of tapering off quantitative easing in the US remains uncertain. Nevertheless, PE enters 2014 with increased confidence and a sense of optimism about investment opportunities and the ability to exit and raise new capital, having proven it can react and thrive in difficult market conditions.

Jeffrey Bunder
Global PE Sector Leader
EY
PE investments rebalance
Equilibrium across markets

Last year saw a gradual rebuilding of confidence in developed markets. Sustained good news in the US and an improving outlook for a number of European countries began the process of rebalancing investor portfolios at a global level. The US Federal Reserve’s announcement during the year of a potential tapering of quantitative easing, together with a slowdown in growth rate in countries such as China and Brazil, caused many to question whether emerging markets could sustain the levels of comparative high growth seen in recent years. As a result, investors in many asset classes began shifting focus toward developed markets. While there is no doubt that long-term demographic trends will create renewed growth in the emerging markets, investments have been migrating toward the developed markets as investors favor a more balanced approach.

Private equity has not been immune to this shift, and many buyout houses have turned their attention to the US and Europe, where improved economic outlooks and, in particular, a stabilized Eurozone, are providing a new impetus to invest.

Nevertheless, this rebalancing of investment flows will not come entirely at the expense of emerging markets – countries such as Brazil, Mexico, India, Southeast Asia and China remain attractive destinations for PE capital over the long term. However, PE is taking a more cautious approach to investing as growth moderates in some countries and funds come under pressure to increase their exit pace from their existing emerging market portfolios.

This trend is reflected in the investment totals for 2013. Globally, PE investment volume was down by 9.4% on 2012 figures to 2,013, while value increased by 25% to US$249.5b. Europe and the US saw some reduction in PE deal numbers, but both saw increases in value, with Europe showing a particularly strong Q3. This contrasts with the experience in Asia-Pacific and Latin America, which dragged on the global totals. In Asia-Pacific, deal values fell from US$28.5b in 2012 to US$27.2b in 2013, but volume increased slightly, from 330 to 340. Of the emerging markets, only Sub-Saharan Africa showed an increase in PE investment totals, albeit from a comparatively low base.

Looking ahead, the effects of the geographic rebalancing seems set to persist. European and US PE investment markets are climbing, with Europe in particular showing a strong start to the year. At the beginning of 2014, there were 12 megadeals valued at €14b in the European pipeline. Increasing confidence in the US economy is also starting to attract more PE investment. Global funds will likely invest more capital in developed markets in contrast to recent years as they seek to deploy capital in the larger transactions available in these countries. At the same time, PE activity in emerging markets will be sustained by the fact that many firms have spent the last few years building capital and talent to take advantage of opportunities in these markets.
Overview of emerging markets

China

Slowing economic growth, closed IPO markets and regulatory uncertainty weighed heavily on buyout activity in China in 2013. PE firms announced 161 separate transactions with an aggregate value of US$10.8b in 2013, an 18% decline from the US$13.1b announced in 2012. Take-private transactions have been a powerful trend in recent years, and 2013 was no exception. The year saw the largest take-private ever of a US-listed company by a Chinese company, when Smithfield Foods received a US$7.1b offer from Shuanghui International Holdings. Shuanghui is backed by CDH China Holdings Management, Temasek Investments, New Horizon Capital and Goldman Sachs.

Exits were also particularly challenging as the IPO route was closed and buyers paused for breath. While IPOs have long been the preferred exit route for PE investors in the region, the lack of a functioning IPO market posed a question to investors: wait until the IPO markets reopen, or seek out alternatives among strategic buyers and secondary PE investors? Many chose the latter. According to data provider Dealogic, between 2012 and 2013, PE exits by M&A more than doubled, to US$5.4b in volume.

Nevertheless, 2014 looks set to be a better year for China’s economy and its PE industry. The Government’s 12th Five-Year Plan, announced in late 2013, offers some clarity around future policy as the economy transitions from export-driven to one characterized by consumption. This shift will take some time to play out. China’s growing middle class should create high demand for consumer goods, which in turn should drive PE investment opportunities as companies seek capital and expertise to help them meet this demand. Unsurprisingly, therefore, 90% of general partners (GPs) in China expect investment activity in the country to increase slightly or significantly over the coming months.

Exit activity also looks set to resume, in particular as the IPO market has reopened. With an estimated 750 companies waiting to list in China, it may take time for some of the PE-backed IPOs to come through, but it seems likely that 2014 exit numbers will rise. Quality data and transparency will be key to getting this market back on a positive trajectory.

Figure 3: Value of China PE acquisitions 2012-2013 (US$b)

Source: Thomson One, Dealogic

The year saw the largest take-private ever of a US-listed company by a Chinese company, when Smithfield Foods received a US$7.1b offer from Shuanghui International Holdings.
India

India’s difficult economic and political conditions have created challenges for the country’s PE investors. In a year when the rupee fell to historic lows, eroding the value of portfolio investments and stalling exit plans, economic growth continued to shrink and IPO listings dropped.

Unsurprisingly, Indian buyout figures declined in 2013. Last year, there were 66 buyouts in India, worth US$2.3b. That figure was down from the 86 completed in 2012, totaling US$3.8b, and significantly lower than 2011 figures: 94 buyouts, worth US$5.2b. The market continues to be dominated by small deals, largely completed by domestic firms: the average deal size between 2010 and H1 2013 was just US$41m.

While the depreciated currency may provide some opportunity for investors, GPs are significantly less optimistic about the market than those in China. Just 47% expect PE activity to increase slightly over the coming months. Nevertheless, India jointly ranked at the top with Brazil as a destination for investment in EY’s latest Private Equity Capital Confidence Barometer, with 78% of respondents expecting to increase acquisition activity over the next 12 months.

Similar to China, the consumer sector is poised to be most active, with 87% of market participants saying this sector would see the most investment, followed by technology, media and telecommunications (TMT), with 80%.

Fund-raising figures were muted for India. Last year, just US$3.1b was raised by PE, down from US$3.9b in 2012 and 2011 and significantly down from the 2010 tally of US$6.8b.
Africa

While other emerging markets appear to be less attractive, Africa’s growth continues unabated. And this is reflected in PE figures. Sub-Saharan Africa was the only region to see an increase in fund-raising figures for 2013. In fact, figures for the whole continent show a 136% increase in fund-raising on 2012 totals to US$3.3b – the highest amount recorded since 2007. Africa’s fund-raising total even surpassed India’s for the first time in 2013. The coming year is expected to continue the region’s good run: many limited partners (LPs) now see Sub-Saharan Africa as the most attractive emerging market, according to the Emerging Markets Private Equity Association (EMPEA), and GPs are actively expanding into the region.

While the majority of the market is dominated by regional and local firms, there is increasing interest from bigger players. Investment figures increased significantly last year. PE invested US$3.3b in 2013, up from US$1.6b in 2012, although a handful of large deals boosted the overall figures. Africa now accounts for 8% of all emerging PE activity, up from just 2% in 2010, according to EMPEA figures.

Meanwhile, exits were more muted last year, possibly the result of slowdowns in growth rate in India and China, two of Africa’s key trading partners. However, the routes to exit have broadened out, with corporate acquisitions declining as a percentage of overall exits, and private sales with exits to PE increasing in importance.

Figure 5: Annual PE investment in Africa (US$b)

Source: EMPEA (2010-12 data), AVCA (2013 data). Investment totals reflect total equity amounts for transactions in which financial details have been disclosed.

While other emerging markets appear to be pausing for breath, Africa’s growth continues unabated.
Latin America

Like other emerging markets, the operating environment in Latin America has become increasingly challenging for PE firms seeking to invest in the region. Growth has slowed from the peak levels of just a few years ago, and private consumption in many countries and industries has decelerated, challenging companies to find new ways of growing their businesses.

As a result, transaction activity declined across Latin America in 2013. PE firms announced 93 deals valued at US$2.9b during the year. While this represented a decrease from the US$4.5b announced in 2012, it was up nearly 38% from the US$2.1b for 2011. The fourth quarter of the year was the most active, with 27 announced deals and a combined value of US$1.1b.

Fund-raising also saw a marked decline, the result of macroeconomic deceleration and a current surplus of dry powder. After raising nearly US$18b in 2011, and an additional US$8.1b in 2012, PE firms raised just US$5.2b in 2013, a decline of nearly 36% from the prior 12 months. Among the most significant drivers for the decline was the lack of fund-raising by the large Brazilian funds. In 2011 and 2012, large funds were raised by a number of the region’s most venerated houses, including Gávea Investimentos, Victoria Capital Partners, Pátria Investimentos and Vinci Capital Partners. Last year saw relatively few such large funds raise capital. Instead, the emphasis was on smaller funds, many focused on the emerging markets of Mexico, Central America and, in particular, the Andean region.

However, PE firms in Latin America have several tailwinds. The industry is flush with capital after several years of successful fund-raising. Entrepreneurs and family owners are becoming increasingly familiar with PE and the benefits that the model can provide. Regulators are growing increasingly comfortable with PE investment and cognizant of the important role it can play in the region’s economies. Perhaps most importantly, valuations could trend lower as equity prices fall. As 2014 unfolds, Latin America remains a region with substantial opportunity for PE firms and their investors.

Figure 6: PE deal value in Latin America, 2010-2013 (US$b)

Source: Thomson One

Growth has slowed from the high levels registered a few years ago, and private consumption in many countries and industries has decelerated, challenging companies to find new ways of growing their businesses.
Good market conditions return

PE’s confidence is supported by much improved debt markets. Financing is available for a wide range of deal types, from refinancings and dividend recaps to new acquisitions. In the US, sponsored leveraged loan issuance broke a new record in 2013, totaling US$322.2b. Meanwhile in Europe last year, leveraged buyout loans saw their most active year since 2008, with €36.2b in new loans issued. High-yield bond issuance also reached record levels. These robust markets have so far continued into 2014. A tapering of quantitative easing in the US may, however, impact new issuance and increased borrower costs.

The improved availability of debt for PE acquisitions on good terms is complemented by an increasing amount of capital that funds have to deploy. For the first time in several years, dry powder increased in 2013. With US$399.8b available for investment, the world’s buyout houses have significant firepower to fund new deals. In addition, there is US$100b of dry powder set to expire in 2014, nearly a quarter of the overall total.

Figure 7: US leveraged loan and high yield by value (in US$b)

Figure 8: European senior sponsored loans by value (in €b)
Heated PE deal markets held in check

Greater confidence, record-breaking debt markets and high amounts of capital to invest are ingredients for heated deal markets. However, there are several factors that will keep buyout investments levels on an even keel.

With distributions starting to flow back to limited partners over the last 12 to 18 months and their other asset classes increasing in value, PE fund investors are attempting to maintain their PE allocations. Most LPs are therefore keen to extend investment periods that are set to expire. This removes the threat of GPs needing to hand back committed capital that has not yet been invested and relieves the pressure to deploy capital quickly. This is helping to keep the market in balance.

In addition, PE faces a number challenges to getting deals done, and these will temper the new acquisitions market.

The first is the M&A markets. Last year saw a fall in global volumes from 43,385 M&A deals in 2012 to 37,003 in 2013. However, there are signs that corporate dealmaking may pick up over 2014. As many as 70% of executives expected deal volumes to improve over the next 12 months, according to the October 2013-April 2014 EY Global Capital Confidence Barometer, with many citing rising confidence in the global economy as a reason for their increased confidence. Over one-third expected their company to make acquisitions, up from one-quarter a year earlier. While a return to M&A may improve potential deal and exit opportunities, the high level of cash currently held by corporations globally means that trade buyers now have a significant war chest at their disposal if they decide to press ahead with acquisition strategies.

Figure 9: GPs expect M&A valuations to increase over the coming year, except in Western Europe

Do you expect your company to pursue acquisitions in the next 12 months?

What do you expect the price/valuation of M&A assets to do over the next 12 months?

In addition, PE funds are facing intense competition from other sources. In particular, the last couple of years have seen players such as the Canadian pension funds, which have been focusing on direct investing and, consequently, have expanded their teams to target this aspect of the market. In particular, 2013 saw a number of large high-profile deals in Europe, the US and Asia-Pacific involving direct investment from pension or sovereign wealth funds.

A number of sovereign wealth funds have also signaled that they have similar ambitions, adding additional capital and competition to the market.

These factors, together with improving stock markets, translate into company valuations that are high and rising. In all markets except Western Europe, PE expects valuations to continue upward for the foreseeable future, with well over half of respondents to EY’s latest Private Equity Capital Confidence Barometer in emerging markets and North America saying they will increase in the next 12 months.

While this offers good exit opportunities, on the buyside, PE will need to be circumspect about making new acquisitions. Average global purchase price multiples crept above 8x globally in 2013 and, with the prospect of developed markets’ stimulus policies changing in the near to medium term, PE globally looks set to maintain a cautious stance and invest highly selectively.

Over the last few years, PE has increasingly focused on value creation in its portfolio to ensure it can meet return expectations. This remains as important now as it has been at any time since the crisis. In a high-valuation environment, those that have built up strong teams with genuine operational experience and capacity will have the edge in deal negotiations and in implementing company performance improvement measures. Add-on deals have been a powerful trend over the last several years, and 2013 was no exception. According to research firm Pitchbook, add-on transactions as a percentage of total global buyout deals reached a record 46% in 2013, up from 42% the year before, and up from just 31% in 2004. The shift toward more add-on activity is reflective of an increased focus by PE firms to optimally structure existing portfolio companies for continued growth, and preparing them ahead of a sale to a strategic or secondary buyer or an IPO.

Last year, we highlighted the trend of large buyout houses migrating toward a multi-asset manager model. These firms have continued to diversify their platform into new areas, such as credit and distressed opportunities, hedge funds and real estate. This strategy works well at a time of increased company valuations and intense competition: these houses have greater flexibility about where to deploy their capital, allowing them to be more opportunistic.

**Figure 10: Top direct investments made by sovereign wealth funds and pension funds in 2013**

<table>
<thead>
<tr>
<th>Announcement date</th>
<th>Target</th>
<th>Deal value (US$b)</th>
<th>Acquirer</th>
</tr>
</thead>
<tbody>
<tr>
<td>9-Sep-13</td>
<td>Neiman Marcus Group Inc.</td>
<td>$6.0</td>
<td>Canada Pension Plan Investment Board, Ares Management LLC</td>
</tr>
<tr>
<td>4-Apr-13</td>
<td>Printemps Holdings France SAS</td>
<td>$2.1</td>
<td>Qatar Holding LLC</td>
</tr>
<tr>
<td>28-Mar-13</td>
<td>NET4GAS sro</td>
<td>$2.1</td>
<td>Ontario Municipal Employees Retirement System – (OMERS) (50%/50%), Allianz Capital Partners GmbH</td>
</tr>
<tr>
<td>22-Feb-13</td>
<td>MSR Resort Golf Course LLC</td>
<td>$1.5</td>
<td>Government of Singapore Investment Corp Pte Ltd. – GIC</td>
</tr>
<tr>
<td>19-Aug-13</td>
<td>CPG International Inc.</td>
<td>$1.5</td>
<td>Ares Management LLC, Ontario Teachers’ Pension Plan</td>
</tr>
</tbody>
</table>

Source: Dealogic
Last year saw the return of the consumer sector. An improvement in economic confidence in the US and Europe, moves by China toward a consumption-led economy, and the continued rise of the middle class in other emerging markets creating investment opportunity all led to the consumer sector attracting more PE attention globally.

In Asia-Pacific, the energy, mining and minerals sector has been knocked off the top spot for attracting PE investor interest over 2014; it had held this position for two years. Nearly three-quarters of Asia-Pacific PE market participants expect the consumer sector to be the most popular area for PE investment, versus just 53% citing energy, mining and minerals.

Technology was the other big story in 2013 (the Dell deal is excluded from the results and the chart below, given its size). Low interest rates, wide availability of credit and opportunities in the financial technology, cloud, big data, and software and services spaces (including companies weakened by disruptive technologies) were among the key drivers fueling activity. Moreover, the opportunity for roll-ups in the tech space is growing, as corporations become more active acquirers.

Meanwhile, health care took more of a back seat, in part because of uncertainties in the US around the Affordable Health Care Act.
PE exits start to level out portfolio investments
IPOs rectify portfolio imbalance

True to form, PE has taken advantage of good exit opportunities as they have emerged around the globe. This is helping to rebalance PE portfolios, which have aged steadily since the onset of the crisis. PE needs to increase the pace of exits still further if it is to work through its current overhang – there are now more than 12,000 portfolio companies owned by PE globally, according to Pitchbook. However, public market appetite for new issues was the big story for 2013 and continues to be strong into 2014. This should provide further opportunity for PE to release more of the capital tied up in some of its biggest deals that date back to the boom era.

In 2013, PE-backed IPOs had their strongest year on record, raising a total of US$58.5b, more than twice the amount raised in 2012. By the end of the year, 187 PE-backed IPOs had priced, compared with 110 in 2012. Overall, IPOs accounted for nearly one-fifth of all companies that went public globally (versus 10% in 2007 and just 6% in 2008) and 35% of the total proceeds.

<table>
<thead>
<tr>
<th>Month</th>
<th>Issuer name</th>
<th>Issuer country</th>
<th>Sector</th>
<th>Exchange</th>
<th>Value (in US$b)</th>
</tr>
</thead>
<tbody>
<tr>
<td>15-Oct-13</td>
<td>Plains GP Holdings LP</td>
<td>United States</td>
<td>Oil and gas</td>
<td>New York</td>
<td>$2.9b</td>
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<tr>
<td>11-Dec-13</td>
<td>Hilton Worldwide Holdings Inc.</td>
<td>United States</td>
<td>Dining and lodging</td>
<td>New York</td>
<td>$2.7b</td>
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<td>9-Oct-13</td>
<td>Antero Resources Corp.</td>
<td>United States</td>
<td>Oil and gas</td>
<td>New York</td>
<td>$1.8b</td>
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<td>8-Nov-13</td>
<td>Merlin Entertainments PLC</td>
<td>United Kingdom</td>
<td>Leisure and recreation</td>
<td>London</td>
<td>$1.7b</td>
</tr>
<tr>
<td>2-Feb-13</td>
<td>Asiacell Telecommunication Co. Ltd.</td>
<td>Iraq</td>
<td>Telecommunications</td>
<td>Iraq Stock Exchange</td>
<td>$1.3b</td>
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<td>20-Jun-13</td>
<td>bPost SA/NV</td>
<td>Belgium</td>
<td>Transportation</td>
<td>Brussels</td>
<td>$1.2b</td>
</tr>
<tr>
<td>12-Jun-13</td>
<td>Coty Inc.</td>
<td>United States</td>
<td>Consumer products</td>
<td>New York</td>
<td>$1.1b</td>
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<tr>
<td>13-Aug-13</td>
<td>Envision Healthcare Holdings Inc.</td>
<td>United States</td>
<td>Health care</td>
<td>New York</td>
<td>$1.1b</td>
</tr>
<tr>
<td>26-Jun-13</td>
<td>HD Supply Holdings Inc.</td>
<td>United States</td>
<td>Construction/building</td>
<td>Nasdaq</td>
<td>$1.1b</td>
</tr>
<tr>
<td>8-May-13</td>
<td>Quintiles Transnational Holdings Inc.</td>
<td>United States</td>
<td>Health care</td>
<td>New York</td>
<td>$1b</td>
</tr>
</tbody>
</table>

Source: Dealogic
The IPO resurgence in EMEA was particularly striking. In 2013, PE firms raised US$17.8b across 35 separate IPOs, compared with just 6 raising US$2.3b in 2012.

In addition, global PE-backed IPO performance has been strong, showing a strong 25.1% rise through mid-February 2014. As hold periods have lengthened, PE has intensified its focus on making operational improvements in the businesses it backs. This hands-on approach is starting to bear fruit as public markets investors respond with strong demand for PE-backed assets.

As we go into 2014, PE is filing for IPOs at an accelerated pace. At the beginning of the year, there were nearly 60 PE-backed companies in the IPO pipeline, with the potential to raise more than US$14b in total. Further IPOs have been announced since then.

Secondary buyout appetite remains strong in Europe and is growing in emerging markets. Many of the companies exited via this route in Europe dated back to post-crisis vintage years: 3 of the top 10 deals in the region were secondary buyout sales of deals completed post-2008. Those PE firms that were able to continue investing through the downturn are now starting to reap the rewards as their peers seek new deal opportunities at a time when acquisitions are proving challenging to source.

**Hold periods set to stabilize**

Overall, exit proceeds continue to outstrip new investment values (US$268.5b versus US$249.5b, respectively, in 2013). This attests to PE’s increased focus on realizing investments and working through the overhang. As this process continues, and as some of the post-crisis deals start coming onto the market, average hold periods may stabilize rather than continue to lengthen, as they have over the last five years.

GP are also making headway with returning capital to LPs through recapitalizations. The total value of PE-backed refinancings and recapitalizations were close to all-time highs in Europe ─— higher than debt totals for new deals in the first three quarters of the year ─ and very strong in the US. PE is seizing the opportunity of demand in debt markets to refinance companies on attractive terms, in some instances, and making distributions through dividend payments.

**Figure 15: PE exits by M&A and IPO (in US$b)**

![Figure 15](image_url)

Source: Dealogic
M&A exits still to come through

The missing ingredient for exit market equilibrium in the US and Europe has been M&A. Last year was slow for PE exits to trade buyers, and both values and volumes were down from 2012 figures, causing a drag on overall exit numbers. By value, exits via M&A declined by 2.3% last year from 2012 figures.

However, as we noted in the investments section, there is increased confidence about M&A. While few may be expecting a dramatic upturn, corporations are becoming more optimistic about making acquisitions. If corporations really do reactivate their M&A plans in 2014, PE exit activity will increase, allowing firms to work further through the exit overhang and balance out portfolios.

Maturing emerging markets see more balance in exit routes

Emerging markets have followed a rather different path for PE exits over the last year. In Asia-Pacific, for example, IPOs have become a less favored option, in part because of the regulators’ decision in China to close the IPO market, but also because economic deceleration in some areas of the region affected public market appetite.

While the reopening of the IPO market in China looks set to rectify this to some degree, there has been a noticeable shift in PE investors’ views on exit routes. Trade sales are now seen as an attractive option as corporates look to improve their strategic position in the region and local trade buyers emerge. Indeed, there was a sharp increase in sales to corporates last year. These accounted for 166 deals in 2013, totaling US$31.5b, up from 116 the prior year, totaling US$17.4b.

And as the markets mature, secondary buyouts are becoming a more realistic exit route: 54% of respondents to EY’s Asia-Pacific PE outlook for 2014 said they expected secondary buyouts to comprise the bulk of deal activity in the region, second only to distressed debt acquisition.

In Africa, where trade sales have long been the most important PE exit route, there has been a similar broadening of sale type. Sales to corporations reduced significantly as a proportion of exits last year (to 30%, down from 49% in 2012 and 59% in 2011). Private sales, meanwhile, increased to 30% in 2013 from 20% a year earlier. Interestingly, sales via secondary buyout increased to levels not previously seen in the region, accounting for 22% of exits in 2013 (versus a historical average of 14%).

This pattern of a broadening of exit routes is taking root across emerging markets, providing a healthy balance between the three key means of realizing portfolio companies: IPOs, secondary buyouts and M&A.

Last year was slow for PE exits to trade buyers, and both values and volumes were down from 2012 figures, causing a drag on overall exit numbers.
PE year in review 2013

Key stats at a glance (in US$b)

<table>
<thead>
<tr>
<th>Year</th>
<th>PE funds closed</th>
<th>Fund-raising</th>
<th>Announced PE deals</th>
<th>Announced PE deal value</th>
<th>Average PE deal equity component</th>
<th>PE-backed M&amp;A exits</th>
<th>PE-backed IPOs</th>
</tr>
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<tbody>
<tr>
<td>2007</td>
<td>1,111</td>
<td>$615.5</td>
<td>3,387</td>
<td>$734.1</td>
<td>30.87%</td>
<td>$301.9</td>
<td>$57.7</td>
</tr>
<tr>
<td>2008</td>
<td>1,060</td>
<td>$634.2</td>
<td>2,737</td>
<td>$219.7</td>
<td>38.85%</td>
<td>$140.6</td>
<td>$9.9</td>
</tr>
<tr>
<td>2009</td>
<td>680</td>
<td>$292.3</td>
<td>1,888</td>
<td>$138.6</td>
<td>45.51%</td>
<td>$65.3</td>
<td>$16.8</td>
</tr>
<tr>
<td>2010</td>
<td>697</td>
<td>$267.4</td>
<td>2,068</td>
<td>$229.6</td>
<td>41.37%</td>
<td>$221.5</td>
<td>$35.5</td>
</tr>
<tr>
<td>2011</td>
<td>750</td>
<td>$289.8</td>
<td>2,094</td>
<td>$215.8</td>
<td>37.95%</td>
<td>$232.6</td>
<td>$38.8</td>
</tr>
<tr>
<td>2012</td>
<td>758</td>
<td>$341.7</td>
<td>2,222</td>
<td>$200.3</td>
<td>37.74%</td>
<td>$214.8</td>
<td>$22.0</td>
</tr>
<tr>
<td>2013</td>
<td>644</td>
<td>$401.1</td>
<td>2,013</td>
<td>$249.5</td>
<td>35.63%</td>
<td>$210.0</td>
<td>$58.5</td>
</tr>
</tbody>
</table>

Fund-raising

2013 was the best year for PE fund-raising since 2008.

Global PE fund-raising

PE dry powder by region (in US$b)

Firms raised a collective US$401b in new commitments across 644 funds.
Acquisitions
PE acquisitions closed out the year up 25% by value and down 9% by volume.

Firms announced 2,013 PE deals in 2013 with a combined value of US$249.5b.

2,013 deals
US$249.5b combined value

Exits
The strength of the IPO market was one of the most important stories for PE in 2013.

- **187** companies went public
- Raising **US$58.5b**
- Up **70%** by volume
- Up **166%** by value

IPOs
Global IPO activity rebounded in 2013, following two years of decline.

IPOs by proceeds, 2013

<table>
<thead>
<tr>
<th>Industry</th>
<th>Americas</th>
<th>Asia-Pac</th>
<th>EMEA</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financials</td>
<td>10%</td>
<td>0%</td>
<td>0%</td>
<td>10%</td>
</tr>
<tr>
<td>Consumer goods</td>
<td>7%</td>
<td>0%</td>
<td>3%</td>
<td>10%</td>
</tr>
<tr>
<td>Materials</td>
<td>3%</td>
<td>1%</td>
<td>3%</td>
<td>7%</td>
</tr>
<tr>
<td>Oil and gas</td>
<td>12%</td>
<td>0%</td>
<td>5%</td>
<td>17%</td>
</tr>
<tr>
<td>Health care</td>
<td>8%</td>
<td>1%</td>
<td>1%</td>
<td>10%</td>
</tr>
<tr>
<td>Industrials</td>
<td>3%</td>
<td>1%</td>
<td>0%</td>
<td>4%</td>
</tr>
<tr>
<td>Telecom</td>
<td>2%</td>
<td>1%</td>
<td>4%</td>
<td>7%</td>
</tr>
<tr>
<td>Technology</td>
<td>2%</td>
<td>0%</td>
<td>0%</td>
<td>2%</td>
</tr>
<tr>
<td>Retail</td>
<td>8%</td>
<td>3%</td>
<td>10%</td>
<td>21%</td>
</tr>
<tr>
<td>Consumer services</td>
<td>5%</td>
<td>1%</td>
<td>1%</td>
<td>7%</td>
</tr>
<tr>
<td>Utilities</td>
<td>1%</td>
<td>1%</td>
<td>3%</td>
<td>5%</td>
</tr>
<tr>
<td><strong>Grand total</strong></td>
<td>61%</td>
<td>9%</td>
<td>30%</td>
<td>100%</td>
</tr>
</tbody>
</table>
Regaining equilibrium: Global private equity watch 2014

A new lens on insurance market growth

For most of the past decade, focusing on the BRICs seemed a simple strategy for insurance companies seeking to expand their business in RGMs.

PE fund-raising recovers
Developed markets see totals rise

After several tough years, the PE fund-raising market is normalizing. Through 2013, conditions for raising capital gradually improved so that by the close of the year, the total committed to PE funds had increased by 17% on 2012 numbers, to US$401.1b from US$341.7b. Indeed, 2013 was the best year for fund-raising since the peak of 2008.

While the 2013 total is some way off the US$634b raised in 2008, there is increasing confidence among GPs about the future of fund-raising. Two-thirds of GPs are now optimistic about the fund-raising environment, according to our latest Private Equity Capital Confidence Barometer, a significant improvement on the 41% reported a year ago. With 71% of PE firms targeting fund sizes that are the same or smaller than their current funds, it seems unlikely that the amounts raised during the boom years will be reached any time soon. However, given the rise in dry powder over the last year and the moderate level of new investment activity, this suggests the market is reaching a state of equilibrium.

GP optimism is supported by LPs' sentiment toward PE. LPs are increasingly looking to alternative assets as they seek to achieve superior returns. PE looks set to be a main beneficiary as it continues to deliver returns that outpace the public markets over the long term. Additionally, rising PE value increases require additional alternative allocations to allow relationships to keep pace.

Two-thirds of GPs are now optimistic about the fund-raising environment, according to our latest Private Equity Capital Confidence Barometer, a significant improvement on the 41% reported a year ago.
Emerging markets fund-raising levels off

The rebalancing of investor portfolios is, however, evident in emerging markets’ fund-raising trends. In 2013, emerging markets saw a decline in fund-raising figures. While emerging markets fund-raising accounted for 20% of global PE totals in 2012, this proportion fell to 12% in 2013. Nevertheless, the decline follows a decade of strong growth. To put this into context, 10 years ago emerging markets represented just 3% of total PE assets available for investment; now, they account for 14%. LPs are now undergoing a process of honing their investment strategies to achieve a good spread across both developed and emerging markets.

Capital shifts toward larger funds

Buyout funds, particularly the large funds, are now gaining traction in the market. There were some strong, large fund-raisings in 2013 and into early 2014. Apollo Global Management attracted US$18.4b for its latest buyout fund – the largest fund raised since 2008. CVC Capital Partners raised US$13.5b for its sixth European fund, and Carlyle Partners achieved a US$13b final close on its Carlyle Partners VI fund.

Figure 18: Top PE funds raised in 2013

<table>
<thead>
<tr>
<th>Fund</th>
<th>Size (US$b)</th>
<th>Target (US$b)</th>
<th>Raised (US$b)</th>
</tr>
</thead>
<tbody>
<tr>
<td>CVC European Equity Partners VI</td>
<td>Buyout</td>
<td>$11.5</td>
<td>$13.5</td>
</tr>
<tr>
<td>Carlyle Partners VI</td>
<td>Buyout</td>
<td>$10</td>
<td>$13</td>
</tr>
<tr>
<td>Warburg Pincus Private Equity XI</td>
<td>Balanced</td>
<td>$12</td>
<td>$11.2</td>
</tr>
<tr>
<td>Silver Lake Partners IV</td>
<td>Buyout</td>
<td>$7.5</td>
<td>$10.3</td>
</tr>
<tr>
<td>Apax VIII</td>
<td>Buyout</td>
<td>$7.4</td>
<td>$7.7</td>
</tr>
<tr>
<td>Riverstone Global Energy and Power Fund V</td>
<td>Natural resources</td>
<td>$6</td>
<td>$7.7</td>
</tr>
<tr>
<td>Cinven V</td>
<td>Buyout</td>
<td>$6.1</td>
<td>$7.1</td>
</tr>
<tr>
<td>Lone Star Real Estate Fund III</td>
<td>Real estate</td>
<td>$6</td>
<td>$7</td>
</tr>
<tr>
<td>Brookfield Infrastructure Fund II</td>
<td>Infrastructure</td>
<td>$5</td>
<td>$7</td>
</tr>
<tr>
<td>KKR Asia Fund II</td>
<td>Buyout</td>
<td>$6</td>
<td>$6</td>
</tr>
</tbody>
</table>

Source: Preqin
The shift of capital toward larger funds accelerated in 2013, and the fund-raising market was driven by the largest funds. In 2013, average fund sizes increased to the highest level seen since 2008, to US$1.23b, up from just US$740m in 2012, according to Preqin. Indeed, mega-buyout funds alone raised US$85b of the year’s total in 2013.

LPs are increasingly focused on developing larger relationships with fewer managers to drive efficiencies in due diligence, monitoring and oversight and to reduce fees paid to GPs. The multi-asset managers now have the edge in fund-raising as LPs look to one-stop shops for the majority of their alternative exposure.

There are currently 1,300 PE funds at various stages of the fund-raising process seeking over US$440b in aggregate commitments, around half of which is for buyout funds. Not all these funds will be successful as LPs continue to be highly selective about the funds they back. At 18.2 months, the average time taken for a PE firm to raise a fund last year was the longest on record, showing that fund-raising still takes time. And while the widely predicted mass shakeout of the PE industry has not happened, there is an increasingly obvious divide between those able to raise a fund successfully and those that struggle to do so. Instead, we’re seeing a gradual unwinding of less successful firms that have been unable to generate solid returns to investors. This will continue into the medium term.
Outlook: balance is being restored to PE
PE has started 2014 with a renewed sense of confidence via an improvement in fund-raising conditions, an increase in exit pace and options, and a slow but steady range of available investment opportunities supported by strong debt markets. All of these are trends from 2013 that have followed buyout houses into the new year.

This confidence mirrors the gradual improvement in economic outlook in some of PE’s key markets, such as the US and parts of Europe. And while the World Bank recently cut its GDP projections for key emerging markets, such as some of the BRICs, growth prospects remain strong on a relative basis in most countries, with developing markets expected to generate 5.3% of GDP growth in 2014. This will create investment opportunities across all markets. As a result, we would expect a moderate rise in investment values and volumes globally over the coming year.

With increased funds available for PE investment following a steady year for fund-raising and a strong appetite for lending to new deals among banks and investors, we are also starting to see the return of corporations to the M&A market. This has been the missing ingredient for equilibrium in the PE market as corporations have held back on disposals and acquisitions as a result of the uncertainty that has prevailed over the last few years. January saw the strongest start to the year for M&A since 2000, according to S&P Capital IQ. Worldwide values exceeded US$355b, more than double the value recorded for January 2012. The recovery is being led by larger deals, but we’d expect confidence to filter through to smaller deals, too.

An increase in corporate activity will add to the number of investment opportunities available to PE as well as improve exit prospects. Yet, as we’ve suggested in the report, the return of corporations is a double-edged sword in terms of competition for deals, particularly given the large cash sums on company balance sheets. This, together with the intensified competition coming from LPs pursuing direct investment strategies, may cause valuations to rise further. PE will need to remain circumspect about the investments it makes and continue to drive through value-enhancing measures in the companies it backs to generate the kind of solid returns it has historically achieved.

One trend that may emerge as a result of this is an increased partnership between PE and corporates. Some buyout funds are already exploring this option, such as General Atlantic and Warburg Pincus acquiring 50% in a holding company that will integrate Santander’s European and Latin American asset management businesses. We may see further collaboration through joint ventures and similar partnership-style deals as a means of unlocking investment opportunity to capitalize on the strategic expertise of corporations and the financial know-how of PE.

While we have seen an improvement in exit market conditions, with IPOs continuing apace, PE will need to step up its efforts further to realize on its portfolio investments. If the expected pickup in M&A materializes and the IPO markets remain attractive, there should be plenty of opportunity for it to do so. However, the fact remains that portfolios have aged considerably over the last five years, with the average holding period for recent IPOs nearing 5.2 years, and more than 5.6 years for sales to strategics.

With some sense of balance restored to the LP-GP relationship and LPs seeking higher returns to meet their obligations, the fund-raising market looks set to remain healthy over the medium term. However, LPs will continue to be highly discerning in the funds they back as well as increasingly strategic about where they commit capital. The multi-asset managers that can offer investors a range of investment options, the more specialist funds that can help investors fine-tune their investment strategies and the funds that have consistently provided outsized returns will all have a significant advantage over the rest of the market.

An increase in corporate activity will add to the number of investment opportunities available to PE as well as improve exit prospects.
The current bifurcation in the market between the “haves” and the “have-nots” will persist. There is unlikely to be any significant shakeout of the less successful funds, particularly as LPs are reluctant to wind up PE houses, but over the longer term the zombie funds that have little prospect of raising a new fund will gradually be weeded out of the market.

The trend toward co-investments and separate accounts will continue as GPs seek to pacify LP concerns over fee drag. Yet further out, we may start to see innovations in the fund-raising market as GPs attempt to attract new investors and diversify their funding sources. We’ve already seen larger funds tap the public markets to raise permanent capital. However, we may also see the development of new structures that would enable investors, such as defined contribution pension funds, to access PE fund investments. Making PE more mainstream will put less pressure on future fund-raising rounds.

As a geographic rebalancing of portfolios continues among LPs and GPs, a move that may be hastened by further tapering of quantitative easing in the US, the pendulum swing that characterized the post-crisis period of investment flowing toward emerging markets and away from developed ones has started to move in the opposite direction. The shift of the last six years has enabled PE and its investors to get comfortable with, and establish presence in, new markets. And while capital has started flowing back to more traditional PE markets, the swing has left a legacy of experienced teams and has established track records that will continue into the future. The rush into emerging markets may have subsided, but PE is now and will continue to remain truly global.

All these trends mean that the stage is now set for a more stable PE market, with the prospect of good returns, driven by value-creating strategies.

PE enters 2014 with increased confidence and a sense of optimism in terms of investment opportunities, exit alternatives and attracting follow-on capital.
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