DEALMARKET

DIGEST 35

SEE WHAT'S NEW AND NOTEWORTHY IN PRIVATE EQUITY THIS WEEK /// ISSUE 35

January 26, 2012

PE-BACKED CORDILLERA ENERGY TO MERGE WITH APACHE CORPORATION IN $2.85 BN DEAL

The deal of the week looks to be a trade sale for investors in Cordillera Energy Partners III LLC, which is merging with Apache Corp. in a USD 2.85 billion transaction. According to a news release from Cordillera, the sellers, including private equity investor EnCap Investments and other institutional investors, along with Cordillera management, will receive approximately USD 600 million in Apache common stock subject to customary lock-up provisions. The balance of the consideration will be paid in cash to be funded with debt.

DEALMARKET DIGEST ASKS:
WHY SHOULD PE INVESTORS MORE RAPIDLY ADOPT INFORMATION TECHNOLOGY?

Private equity investors should adopt information technologies rapidly for at least three reasons. The first and probably the most pressing reason is: regulations. European (AIFMD, Solvency II Directive…), American (FATCA, « Volcker rule », Dodd-Franck Act…) and international regulations (Basel III Agreements, Pension funds regulations, and insurance regulations) have introduced new obligations to private equity fund managers. They can be summed up as follows: timelier (insurance groups expect quarterly reports within 45 to 60 days, for example), more comprehensive and more objective reporting (AIFMD, CalPERS vs. San Jose Mercury News). Adopting a state-of-the-art IT system (for example connected to the limited partners systems and transmitting easily reusable data) saves time and helps to fulfill these obligations.

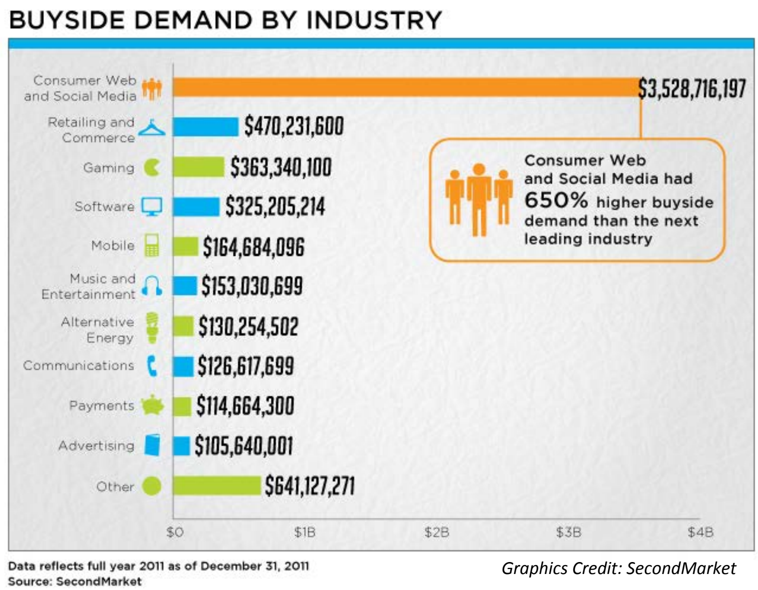
The second reason is: communication. The increased number of limited partners new to the asset class, the need of large amounts of data for due diligences, as well as the scarcity of information in private equity are a significant driver to document the business of general partners on-going. This approach helps to provide detailed information, to avoid significant extra work when preparing a fundraising – notably because general partners are more or less on a “permanent fund raising”. The 2007-2009 crisis presses for more extensive due diligences by limited partners and hence the need of information.

The third reason is: operational risk management. As private equity fund managers will institutionalize, due to regulations and their transformation into “asset management houses*, there will be an increased need to manage the risk of conflicts of interests (for example by unruly communication between LBO / PIPE / real estate / distressed debt teams) or avoid insider trading accusations. To be able to so, general partners will have to set up processes and rules, enforced technically and also supporting investigation in case of legal proceedings.

Interview person:
Cyril Demaria is also a Professor at HEIG-VD, EDHEC and EADA and author of an Introduction to Private Equity , Coll. « The Wiley Finance Series », Wiley

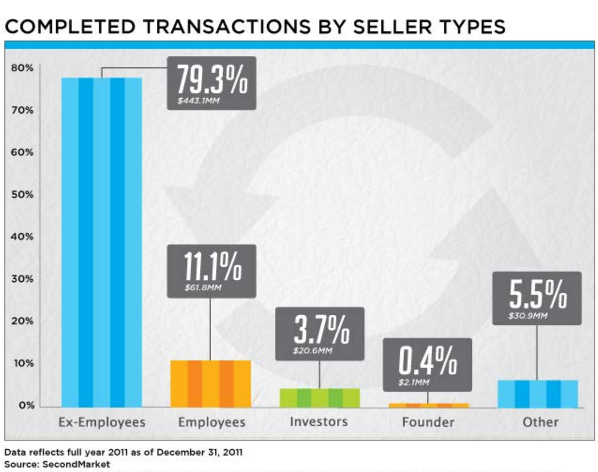
SECOND MARKET'S ALTERNATIVE TRADING PLATFORM GROWS BY 55% IN 2011

SecondMarket, an electronic platform for buying and selling alternative investments and shares in private companies, released some news about activity on its platform in 2011 in a report published on its website. It processed USD 558 million in transactions which it said is a 55% increase over the previous year. Investor interest in using SecondMarket is largely driven by the hope of getting in on winning companies pre-IPO, according to industry observers, such as Forbes and The Street. In particular, the consumer Internet and social media dominate transactions completed in 2011, as the chart below makes clear.



Graphics Credit: SecondMarket

The chart below shows the seller types that sold private stock on SecondMarket in 2011 were mainly former employees and current employees selling shares granted as part of a compensation package.



One of the most used features on SecondMarket, the company claims, is a "watch" feature that lets users track private companies as well as related news stories and updates. The chart below shows the most popular VC-backed companies in 2011.

LEGENDARY FOUNDERS EXIT TWO TECH GIANTS

It is time for a changing of the old guard it seems. A new era in mobile and consumer Internet is taking its toll on the founders responsible for Blackberry and Yahoo!, two of the most well-known brands from two of the leading companies of the last decade, namely Research in Motion (RIM) and Yahoo. Both tech giants saw the departure of their founding executives in the past two weeks. The driver of the management changes is battered share prices and investors that want a change.

Jerry Yang, who co-founded Yahoo in the mid-nineties, announced that he was stepping down from the board and severing ties with the company. The move is seen as “smoothing the way for a major infusion of cash from private equity” or a deal to sell off Yahoo’s stake in China's Alibaba, unlocking value for shareholders, Reuters reports.

In Canada, RIM's co-CEOs Mike Lazaridis and Jim Balsillie, the men who founded RIM were replaced by an internal executive, according to Reuters. The move is seen as preparing the way for a turnaround of the company, or a trade sale. RIM still has a loyal following, particularly among business users due to the security and stability of its email services. It recently introduced a tablet device that benefits from that market position, with high-profile business users, such as Aviva and Royal Bank of Scotland using the new RIM tablet as a replacement for insurance forms and questionnaires that used to be on paper, reports ZDNet in an article entitled Why this $90 Billion British Insurer is High on BlackBerry PlayBooks.

HOW FAMILY OFFICES HANDLE ECONOMIC WOES

A new survey from Cambridge Associates says that family offices made few strategic changes in response to the 2008 meltdown and subsequent volatility. The firms that oversee assets for ultra-high net worth revealed that few families made “tactical adjustments” but few strategic changes in recent years, which reflects the underlying families long-term horizon and satisfaction with current management practices, according to the report.

The median asset size of the family offices in the survey was USD 534 million, and participants represented a mix of Cambridge Associates clients and other family offices that work independently or with other advisors.

Tactical Steps Undertaken

- 62% increased liquidity and cash reserves. (Cash positions rose to 9.6% from 7.5% pre-2008.)
- 49% rebalanced portfolios.
- 43% actively reduced portfolio risk.
- 41% conducted more projections of cash flow and capital calls.

With greater liquidity and cash reserves, family offices will likely take advantage of future market opportunities, such as European distressed debt. “When it comes down to it, the most common response to questions about changes to family office oversight and management policies in the post-2008 period was that none was made,” said Douglas Macauley, managing director at Cambridge Associates. He added that it interesting to see the long-term horizon, and he confirmed that UHNW families appeared to have the resources to “ride out difficult market environments” and, for the most part, did not initiate changes in their investment policies in reaction to the crisis.

IS A STARTUP’S SUCCESS DETERMINED BY ANGELS?

Josh Lerner and a team of researchers are studying the impact on startups by early-stage financiers. One of their most recent papers is available by SuperReturn 2012. We read the report and found that delves deeply into the dealflow, portfolio, and long term results of two US-based angel groups. The data, although limited, was examined in detail and Lerner’s team came to some intriguing conclusions, which we summarized below.

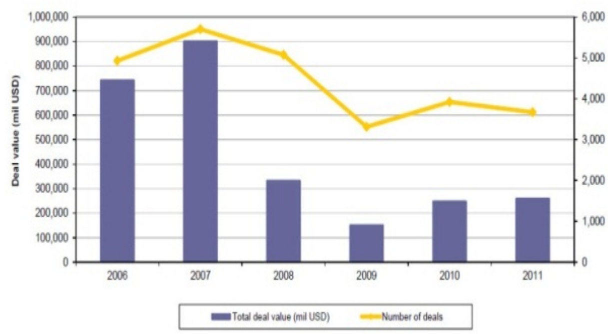
- Ventures that are funded by the two successful angel groups experience superior outcomes to those that were rejected
- They have improved survival, exits, employment levels, patenting, web traffic, and financing.
- Angel financing has a positive effect on most operations of the venture, with qualitative support for a higher likelihood of successful exits.
- There is no difference in access to additional financing, which might suggest that financing is not a central input of angel groups.
- Results suggest that some of the softer features about angel investment, such as their mentoring or business contacts, may help new ventures the most.

You can access the complete study here.

BUYOUTS INCREASED IN 2011 BY FIVE PERCENT

The value of global private equity investment in 2011 rose 5 per cent year-on-year to USD 260 billion, reports Zephyr. Although there was a gain, the increase in value was not nearly as impressive as the previous year’s, when transactions featuring private equity almost doubled to USD 248,028 million from USD 151,004 million in 2009. The FY2011 number of deals actually fell by 6 per cent over the same period.

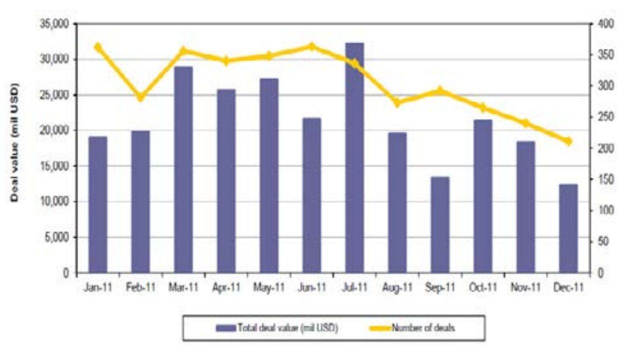
Deals by volume and value 2006 - 2011



Overall, dealmaking levels are still well below 2007 when USD 900.7 billion was invested.

The largest deal of 2011 was the USD 9 billion institutional buy-out of Centro Properties Group's US assets and platform by BRE Retail Holdings. North American targets accounted for the five highest value transactions during the year.

Deals by volume and value in 2011



FAST FUNDRAISING FOR HONY'S LATEST FUND SHOWS CHINA'S ALLURE

Hony Capital is a China focused fund that recently completed a rather quick new fundraising where it amassed USD4 billion from investors in just a few short months.

Hony Capital's John Zhao, chief executive officer, discussed his strategy this week with Bloomberg Television's "Asia Edge". He described construction and consumer trends, such as fast food restaurants, and spoke of economic restructuring as providing a lot of opportunity. Hony Capital is a sister company of Lenovo, both are backed by Legend Holdings Ltd.

QUOTE OF THE WEEK

"The fight over the right to have a glimpse the future of economics was easily the WEF's most controversial moment so far."

Who said it: Francesco Guerrera, WSJ reporter

In Context: Outside the doors of a panel discussion at this week's WEF Forum, a WSJ journalist observed a heated battle. The controversy was not about economics, rather access to the room that hosted the panel discussion. A group of want-to-be attendees were being denied entry to the "The Future of Economics" discussion because the room was fully occupied.
On the panel were eight economists and top business executives, such as Robert J.Shiller, the Yale professor best known for his work on the housing market, and Columbia University's Joseph E. Stiglitz, a well-known economics author and economist, as well as Josef Ackermann of Deutsche Bank. At least two of the panelists were Nobel prize winners.
The journalist said a small crowd gathered at the door and became irritated when they were refused access to the room. A "visibly angry" female executive accused the WEF organizers of moving the interesting panel to a smaller room than previously advertised, even though the official program listed the right room. And there was even a private equity executive who, ever the dealmaker, tried to strike a deal by suggesting the group outside the door be allowed in to at least see whether there was any space.

Where we found it: WSJ Blogs

The Dealmarket Digest empowers members of Dealmarket by providing up-to-date and high-quality content. Each week our in-house editor sifts through scores of industry and academic sources to find the most noteworthy news items, scoping trends and currents events in the global private equity sector. The links to the sources are provided, as well as an editorialized abstract that discusses the significance of the articles selected. It is a free service that embodies the values of the Dealmarket platform delivers: Professional, Accessible, Transparent, Simple, Efficient, Effective, and Global.

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DealMarket

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