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CAMBRIDGE ASSOCIATES LLC

Cambridge Associates LLC Private Equity and Venture Capital Market Commentary for Quarter Ending December 31, 2009

Overview

Private equity and venture capital funds ended 2009 on the upswing as indicated by the Cambridge Associates LLC benchmark indices of the two alternative asset classes. For the third consecutive quarter, both asset classes earned positive returns. The private equity index kept pace with the public markets in the fourth quarter and outperformed the venture capital index for the third quarter in a row. Both asset classes, however, trailed public equities for the year while continuing to outperform over the long term.

The quarter ending December 31st was one of the best since 2007 for both the **Cambridge Associates LLC U.S. Private Equity Index®** and **Cambridge Associates LLC U.S. Venture Capital Index®**. As the public markets rebounded in 2009 both indices trended upward due largely to increased valuations for private companies. Leverage started to become more available at the end of 2009 but exit opportunities remained far below historical averages.

The Cambridge Associates LLC U.S. Private Equity Index® is derived from performance data compiled for funds that represent the majority of the institutional capital raised by private equity partnerships between 1986 and 2009. Based on that data, private equity's returns versus indices tracking large- and small-capitalization public equities – the Dow Jones Industrial Average, the Russell 2000 Composite, and the S&P 500 – are shown below:

U.S. Private Equity Index Returns (%) for the Periods ending December 31, 2009

For the periods ending	Qtr.	1 Year	3 Years	5 Years	10 Years	15 Years	20 Years
December 31, 2009	5.9	13.8	1.1	9.7	7.8	11.8	12.0
Other indices at December 31, 2009							
DJIA	8.1	22.7	-3.1	1.9	1.3	9.3	9.5
Russell 2000 Composite	3.9	27.2	-6.1	0.5	3.5	7.7	8.3
S&P 500	6.0	26.5	-5.6	0.4	-0.9	8.0	8.2

Sources: Cambridge Associates LLC, Dow Jones & Company, Inc., Frank Russell Company, Standard and Poor's, and Thomson Datastream.

The Cambridge Associates LLC U.S. Venture Capital Index® is derived from performance data compiled for funds that represent the majority of the institutional capital raised by venture capital partnerships between 1981 and 2009. Based on that data, venture capital's returns versus indices tracking large- and small-capitalization public equities – the NASDAQ Composite, the Russell 2000 Composite, and the S&P 500 – are shown below:

U.S. Venture Capital Index Returns (%) for the Periods ending December 31, 2009

For the periods ending	Qtr.	1 Year	3 Years	5 Years	10 Years	15 Years	20 Years
December 31, 2009	3.3	3.0	-0.3	4.3	-0.9	37.8	23.4
Other indices at December 31, 2009							
NASDAQ Composite	6.9	43.9	-2.1	0.8	-5.7	7.6	8.4
Russell 2000 Composite	3.9	27.2	-6.1	0.5	3.5	7.7	8.3
S&P 500	6.0	26.5	-5.6	0.4	-0.9	8.0	8.2

Sources: Cambridge Associates LLC, Dow Jones & Company, Inc., Frank Russell Company, Standard and Poor's, and Thomson Datastream.

Note: Because the U.S. Private Equity and Venture Capital indices are capital weighted, the largest vintage years mainly drive the indices' performance.

In the sections below we provide details regarding the indices' performance. Highlights of the fourth quarter are:

- Private equity returns virtually equaled those of the public markets in the fourth quarter while venture continued to trail them in last three years. Both asset classes outpaced the public markets over the long term.
- Over the ten-years ending December 31, 2009, private equity outperformed venture capital due mostly to the collapse of the technology sector at the beginning of the decade.
- Private equity and venture funds both called more capital in the fourth quarter than they had in any of the previous three quarters.
- Private equity and venture funds both distributed more capital in the fourth quarter than they had in the previous three quarters combined.
- For the third consecutive quarter, the private equity funds raised in 2007 earned the best return among the five vintage years that represented at least 10% of the index. The only vintage year to outpace 2007 was 2001, which represented only a little more than 3% of the index.
- All industries that represented at least 5% of the private equity index produced positive results for the quarter; the large components produced about the same results as their public market counterparts.
- Energy and consumer-related businesses were again the leading recipients of capital from the fund managers in the private equity index.
- Funds raised in recent years, including 2007 and 2008, had higher returns in the fourth quarter than the more mature funds from vintage years 1998 through 2006. Only two vintage years beginning with 1998 had negative quarters, 2002 and 2009, neither of which represented a significant portion of the index's value.
- As of December 31, 2009, the ten-year return for the venture capital index was negative for the first time in its history. Because the ten years ending December 31 start on January 1, 2000, the fourth quarter of 1999, the index's best quarter ever, was no longer

part of the ten-year performance. (The return during the fourth quarter of 1999 was nearly 85% and it was replaced with the fourth quarter of 2009's return of about 3%.)

- Of the top three industries by size in the venture index, healthcare, IT, and software, IT earned the best return.
- Based on market values at December 31, 2009, public companies accounted for slightly more than 12% of the private equity index and companies based outside of the U.S. represented nearly 20%. For the venture capital index, public companies made up about 9% of the market value and ex-U.S. companies 8%.

Private Equity Performance Insights

During the fourth quarter, there were signs of an improving economy, and returns for public equity indices were positive, albeit tempered in comparison with the prior two quarters. The quarter's return for the Cambridge Associates LLC U.S. Private Equity Index, 5.9%, brought the index's performance for 2009 to 13.8%, a more than 36% jump from 2008. For the second quarter in a row, valuations for assets held by funds raised in vintage years 2000 to 2007 increased by just under $1.0 billion or more per vintage. Private company values grew most in the retail, healthcare, and manufacturing sectors, due in part to a small increase in consumer spending, likely as a result of the holiday season.

As always, the index's performance was driven by its top vintage years by size, in this case, 2006, 2005, 2004, 2007, and 2000, which together represented 76% of the index's value. Fourth quarter returns for the top five vintages ranged from the 2005 funds' gain of 4.7% to the 2007 funds' increase of 7.3%. Write-ups of $500 million or more in five sectors, retail, healthcare, manufacturing, financial services, and media, led the largest vintage year, 2006, to a quarterly return of 6.5%. The 2005 funds' gain of 4.7% was due mostly to rising values for consumer and healthcare companies. The 2004 funds were up 5.3%, and higher valuations for their retail investments contributed most to the return. Much like the 2006 vintage, gains for the 2007 funds were spread across many industries, with software leading the way. The 2000 funds, now the smallest of the top five vintages, benefited most from realizations and growth in the value of their healthcare investments.

All Eight Prominent Sectors in the PE Index Earned Positive Returns for the Quarter

Each of the eight sectors that together represented 90% of the index's value earned positive returns in the fourth quarter. The top three industries by size—consumer, energy, and healthcare—rose between 3.3% and 8.8%; retail performed the best and energy the worst. Combined the top three sectors accounted for a little more than half of the benchmark's value. Healthcare, financial services, and consumer companies collectively contributed more than half of the index's return. Out of the meaningfully sized sectors, manufacturing gained the most and information technology performed the worst.

Capital Calls and Distributions Increased Over the Prior Quarter

In the fourth quarter, private equity managers called roughly $14 billion from investors and returned a little more than $10 billion– the most contributions and distributions in over a year. Contributions increased by about $4 billion, or 43%, the biggest quarter-over-quarter increase in more than three years, and distributions rose by nearly $6 billion, or 124%, the largest quarterly increase in about 18 years. Investors in funds raised from 2006 through 2008 contributed 78% of the total capital called – the 2006 and 2007 vintages called roughly $4 billion each. Conversely, five vintage years, 1999 through 2001, 2003 and 2006 each distributed over $1 billion or 57% of the total for the quarter. After a slow first half of the year, the private equity investment pace continued to gain momentum in the fourth quarter with the bulk of the capital going into energy, retail, software, information technology, and manufacturing companies.

Gap between Contributions and Distributions Narrowed

While distributions continued to trail contributions in the fourth quarter, the difference between the two was lower than it was since the beginning of the recession, a promising sign for private equity funds and investors. Macroeconomic factors, such as unemployment and rising energy prices, continued to make consumers reticent to spend, but public market performance helped lift company valuations. Signals that the credit markets were starting to loosen were a welcome development, especially for middle-market investors.

Another Quarter of Positive Impact from the Public Market Valuation Methodology

As public equities continued to rally during the fourth quarter, the private equity index again benefited from the "mark-to-market" valuation methodology. This quarter though, the variation in returns between the public markets and the private equity index was negligible. For example, two subsectors, discount retail and semiconductors, saw some of the largest write-ups mirroring the trend in the public markets. A weakened U.S. dollar and strong performance in markets outside of the U.S. combined to boost valuations for the underlying companies in the index's private equity funds that invest outside of the U.S.

Cambridge Associates derives its U.S private equity benchmark from the financial information contained in its proprietary database of private equity funds. As of December 31, 2009, the database comprised 814 U.S. buyouts, private equity energy, growth equity, and mezzanine funds formed from 1986 to 2009, with a value of roughly $363 billion. Ten years ago, as of December 31, 1999, the index included 330 funds whose value was nearly $104 billion.

Venture Capital Performance Insights

As 2009 progressed, the amounts of capital being called and distributed slowly increased, and during the fourth quarter, distributions increased significantly over the prior three quarters. There was one more initial public offering (IPOs) in the fourth quarter than in the third, but there was less capital raised by the fourth quarter's IPOs, mostly because the third quarter's offerings included the largest venture-backed IPO exit in more than two years. The 12 IPOs in 2009 were double the number in 2008. Exits through mergers and acquisitions (M&A) increased by only four in the fourth quarter, but based on deals with disclosed values, the average transaction size leapt from about $61 million in the third quarter to approximately $223 million in the fourth.

According to the National Venture Capital Association (NVCA) and Thomson Reuters, there were 4 IPOs and 73 M&A in the fourth quarter; the IPOs were split evenly between information technology and healthcare companies and 48 of the M&A involved information technology companies. The fourth quarter's 40 deals with announced values were worth $8.9 billion, more than six times the value of the 23 deals in the quarter before, which, as reported to the public, were worth $1.4 billion.

VC Index Has Best Quarter in Two Years; Funds Raised in 1999 Performed Best among the Top Six Vintage Years

Venture capital performance gradually improved during 2009. The fourth quarter return of 3.3% for the Cambridge Associates LLC U.S. Venture Capital Index was its highest in three years and it lifted the index's 2009 return to 3.0%, a more than 19% increase over the 2008 results. Six vintage years, 1999 through 2001, and 2004 through 2006, accounted for about 77% of the index; all had positive returns in the fourth quarter with the funds raised in 1999 performing best, 5.5%, and the 2006 funds the worst, 1.8%. Higher values for technology, software, and financial services companies buoyed the 1999 vintage's return; information technology accounted for more than half of the write-ups in the 2006 funds' companies. The largest vintage year in the index, 2000, earned 2.0% for the quarter, resulting from meaningful write-ups for technology companies, and slightly lower values for electronics and energy businesses. The funds from the remaining top six vintage years, 2004, 2005, and 2001, returned 2.4%, 4.2%, and 2.8%, respectively. Increased valuations for technology companies were by far the largest positive contributor to the performance of both the 2004 and 2001 vintage years. Better values for healthcare, technology, and software companies were the main drivers of return for the 2005 vintage year funds.

Healthcare, information technology, and software remained the largest sectors in the venture capital index, representing nearly 73% of the index's value. All three sectors earned positive returns during the fourth quarter; information technology led all industries, not just the top three, with a return of 10.7%. Healthcare's return of 2.3% lagged both technology and software. Electronics and communications were the only other sectors that represented more than 5% of the index's value. Among the meaningfully sized industries, energy (the only one to produce a negative return) performed the worst. Overall the index's companies produced a return of 5.4%; when excluding healthcare, the company-level return rose to nearly 7.0%.

Distributions Reached Level Not Seen in Seven Quarters; Distributions and Contributions Were Nearly Equal for the First Time in Three Years

In the fourth quarter, the index's venture capital fund managers called more than $3 billion from investors, a 12% increase over the prior quarter. Distributions from the venture funds also equaled slightly more than $3 billion, marking a 181% increase over last quarter and the most since the first quarter of 2008. As a group, the funds from vintage years 2005 through 2008 were responsible for about 79% of the quarter's capital calls. The funds raised in 2000 and 1999 distributed just shy of $2 billion, or 61% of the quarter's total.

Venture-Backed Company Valuations Increased Again in the Fourth Quarter, but there Remained a Shortage of Profitable Exit Opportunities

Valuations for venture-backed companies rose more in the fourth quarter than they did in either of the previous two. Given that technology companies dominated both IPOs and M&A transactions, it is not surprising that values for companies in that sector increased the most. The number of deals with disclosed values nearly doubled compared with the previous quarter, average deal values increased nearly four-fold, and fewer companies were sold for less than the amount of capital invested. The bad news for the industry was that exits were still not plentiful and that the ten-year return dropped into negative territory for the first time, a problem also faced by some large public equity indices, such as the S&P 500. It is unclear how long this trend will last.

Cambridge Associates derives its U.S. venture capital benchmark from the financial information contained in its proprietary database of venture capital funds. As of December 31, 2009, the database comprised 1,291 venture funds formed from 1981 through 2009 with a value of nearly $98 billion. Ten years ago, as of December 31, 1999, the index included 700 funds whose collective value was slightly more than $118 billion.

About Cambridge Associates and the Indices

Founded in 1973, Cambridge Associates delivers investment consulting, independent research, and performance monitoring services to more than 800 institutional investors and private clients worldwide.

Cambridge Associates LLC's proprietary databases provide independent statistics to the institutional investment industry and the National Venture Capital Association (NVCA). The Cambridge Associates LLC U.S. Venture Capital Index® is based on performance data compiled for funds that represent the majority of the institutional capital raised by venture capital partnerships from 1981 through 2009. Similarly, the Cambridge Associates LLC U.S. Private Equity Index® is based on returns data compiled for leveraged buyouts, subordinated debt, and special situations funds that represent the majority of institutional capital raised by private equity partnerships formed from 1986 through 2009. The pooled means represent the net end-to-end rates of return calculated on the aggregate of all cash flows and market values as reported to Cambridge Associates by the funds' general partners in their quarterly and annual audited financial reports. These returns are net of management fees, expenses, and performance fees that take the form of a carried interest.

Both the Cambridge Associates LLC U.S. Venture Capital Index® and the Cambridge Associates LLC U.S. Private Equity Index® are reported each week in *Barron's* Market Laboratory section. In addition, complete historical data can be found on Standard & Poor's Micropal products and on our website, www.cambridgeassociates.com.

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