

Overview of Southeast Private Equity Opportunities & Private Equity after the Global Financial Crisis

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Introduction

- CapAsia
- Changes in Private Equity after the Global Financial Crisis
- Overview of Southeast Asia
- Conclusion



How has the private equity model changed post GFC?

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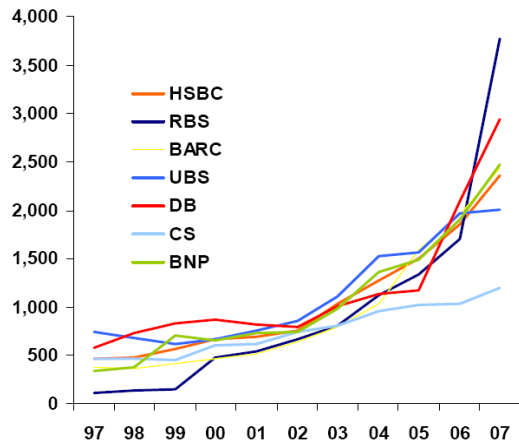
"Too Early to Tell"

Attributed to **Zhou Enlai**, the first premier of the People's Republic of China, when asked in the 1950s what he thought the impact of the 1789 French Revolution had been.

The Global Financial Crisis, the Party

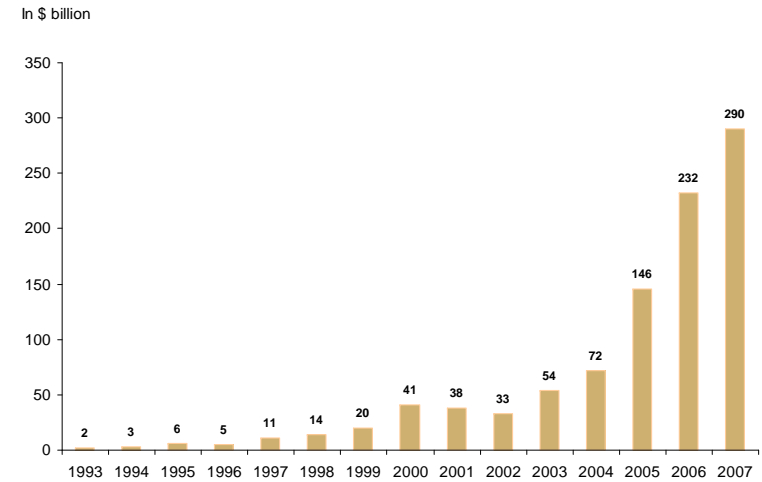
First the Feast...

European Financials' Balance Sheets
Total Assets, \$bn



Bankers' banquet

European LBO Loans (1993-2007)



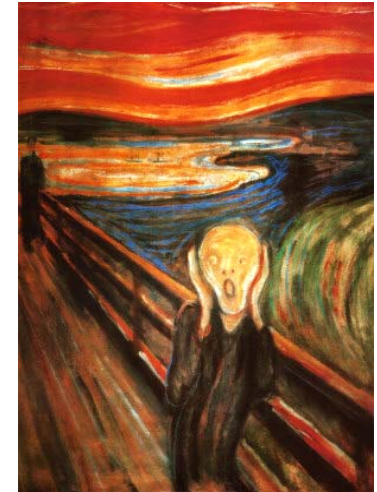
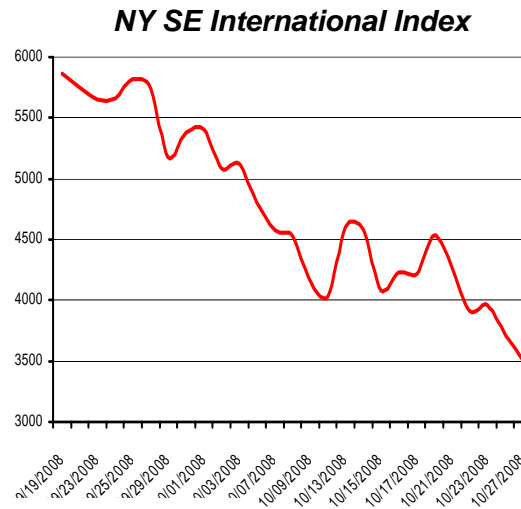
Source: Dealogic, December 2008

The Global Financial Crisis the Morning After

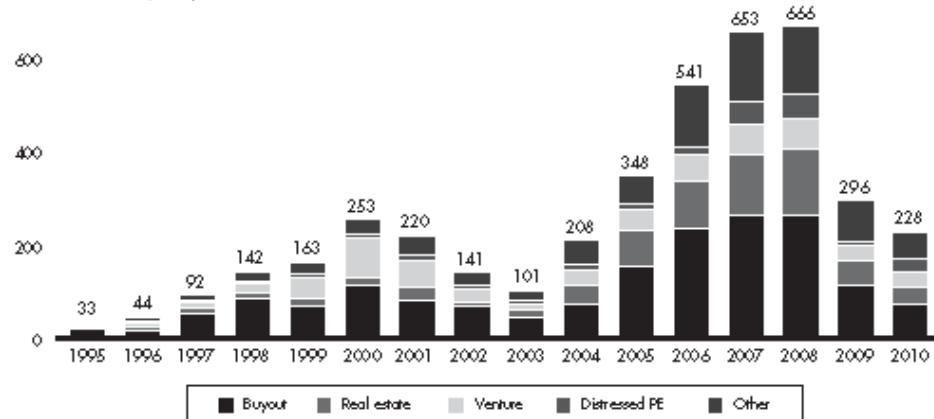
... then the Famine



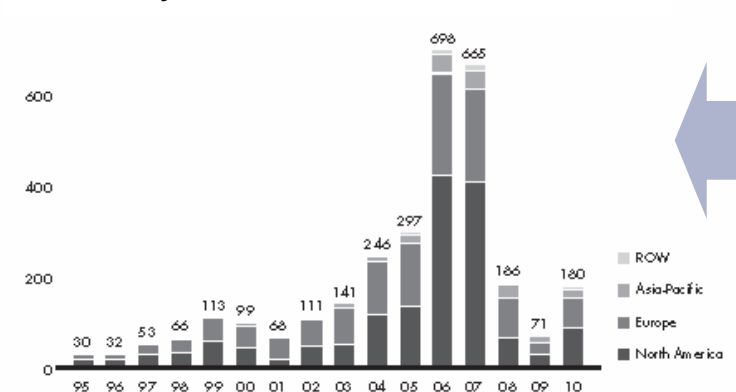
Market mauls bull



Private Equity Funds Raised 1995 - 2010



Global Buy-out Deal Value 1995 - 2010



The PE World Post-GFC

GPs will have to work harder for the money they plan to earn ...

- Fund Raising Environment Shaken Up
- LP – GP Relationship Rebalanced
- Fund Management Industry Regrouping
- The End of Leverage as Return Driver
- Portfolio Management Capabilities More Prominent

Changed Fund Raising Environment

- Most LPs Got a Bloody Nose Some Virtually Disappeared as an Investor Category
 - Basel III
 - Solvency II
 - Volcker Rule
- Fund Raising More Heavily Regulated
 - Cf AIFM Directive
 - Increased Compliance Requirements and Administrative Costs
- Fund Raising More Challenging
 - Institutional Investors More Discriminating
 - Strengthened Review and Decision Making Processes
 - Target Fund Sizes Reduced – The End of Mega Funds?
- IFIs and DFIs Got a New Lease on Life
 - More Important Role as Seed Investor and Catalyst
- Listed Fund Model Discredited

LP – GP Relationship Rebalanced

- **Terms and Conditions Revisited**
 - Management fee
 - Hurdle rate
 - No more "add-on" fees
 - Investment restrictions to investment strategy, leverage policy
- **Better Alignment of Interests**
 - General sharing of returns/income
 - Carry split
 - Team with meaningful skin in the game
 - More rigid key executive clauses
 - Captives acceptable only in specific situations / circumstances
- **Face Value No More: Track Record Required**
 - More difficult for start up/first-time funds – in contrast, GPs with a track record AND survived the GFC found it easier to raise funds
 - Team at the core
 - Possible exception: green funds (clean energy; renewables; energy efficiency)
- **No Tolerance for Strategy Drift**
 - Well-articulated and focused investment strategy enforced through investment restrictions
 - Execution capacity
- **Strengthened Focus on Money Multiple**
 - More emphasis on MM at given minimum IRR
 - Longer hold periods

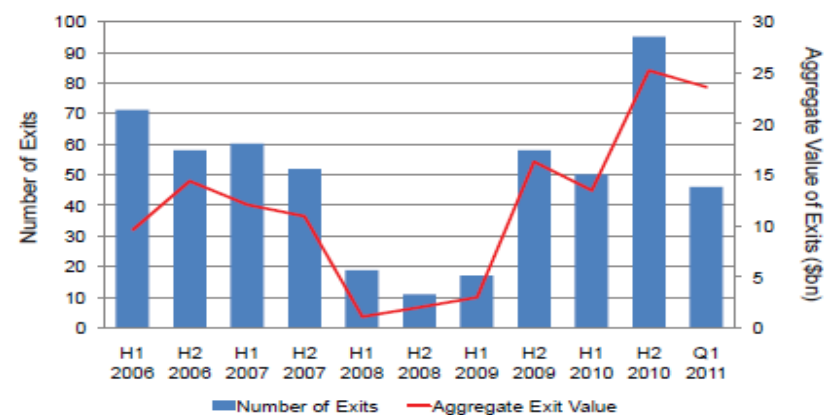
Fund Management Industry Regrouping

- The Men Separated from the Boys
 - "When the tide goes down, you get to know who is swimming without his trunks on" - Warren Buffett
 - Exposed the weakness of certain investment strategies, lack of execution capability and absence of portfolio management capacity
 - Shrewd fund managers saw opportunities in buying up discounted debt in their portfolio companies while others saw their equity drown
- Barrier To Entrance (First Time Funds or Fund Managers) Raised Higher
- Banks Spinning off Captive GPs as a Result of Basel III
- Portfolio Asset Management Capacity no Longer an Afterthought
- More Emphasis on Down-Side Risk Management Capability
 - Control strategies favoured
 - Certain sectors no-go zones
 - Infrastructure has emerged as an increasingly attractive asset class

Portfolio Management and Exit Strategy More Prominent

- GP added value capability has become more important
- Track record in downside risk management and protecting value throughout the crisis of key significance
- Controlling interests in portfolio companies matter more
- Exits more demanding:
 - The end of parcel passing: LPs selling to themselves (secondaries and tertiaries)
 - More emphasis on market timing strategies:
 - IPO markets virtually disappeared until Q3/Q4 2009

PE-Backed IPOs (2006-1Q2011)



Source: Preqin

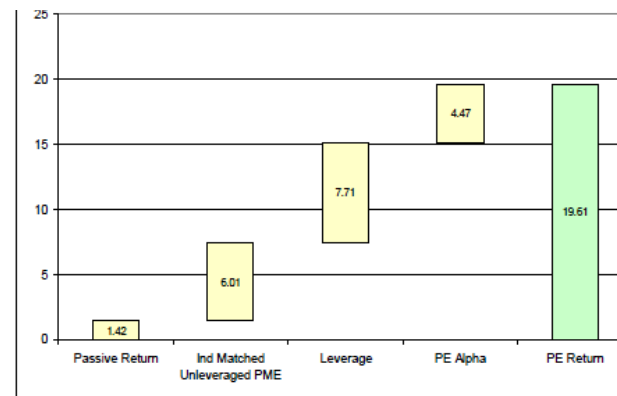
The End of Leverage as Main Return Driver

- **Some Facts**
 - Since the GFC there has been a 70% reduction in primary leveraged loan market liquidity
 - Leverage: First Six Became the new Five and then Four Became the New Six
 - Post-GFC EV/EBITDA Multiples in Europe contracted from 8 – 12 x to 5 – 9 x
 - In developed markets leverage accounted for over 40% of the IRRs of buy-out funds
- **GPs will have to do the heavy lifting – debt capital markets muss less so**
 - Style change to buy-and-build strategies
- **Certain Classes of Subordinated Debt Virtually Disappeared**
 - PIK only; Second Lien; etc.
- **Tightening of the availability and terms of debt at investee company level**

Understanding Leverage



Components of Buyout Fund Returns



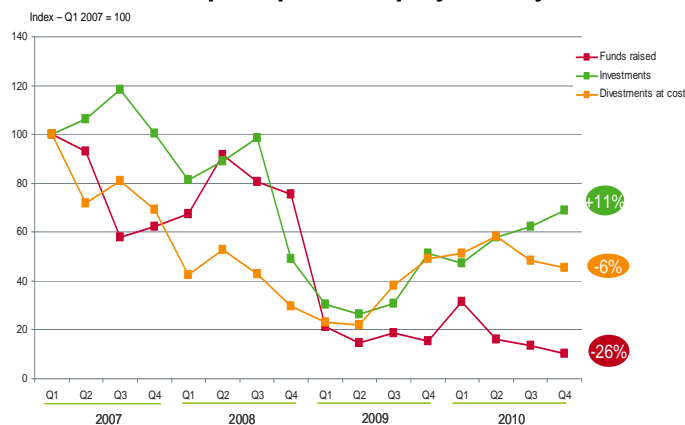
Source: LBS. HED, "Private Equity Fund Level Return Attributions", June 2010

Too Early to Tell

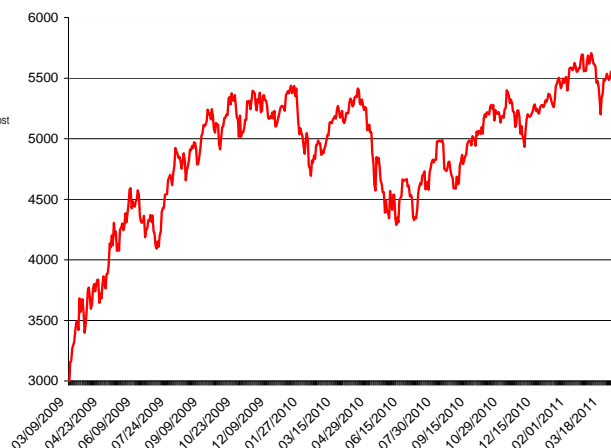
...how permanent are these changes going to be?

- Not likely that the "new" private equity model or paradigm will hold up for the long term
- In the advanced markets, 2009/2010 marked the trough of private equity
- Investor amnesia will return (it always does)—first signs already visible
 - Debt again available for LBOs
 - Investor enthusiasm for selected markets rapidly growing
- Full circle around? Excess liquidity building up and looking for deployment
 - QE
 - High oil prices
 - Growing forced savings contributions

Trends in European private equity activity flows



NYSE International Index March 2009 - April 2011



Quantitative Easing



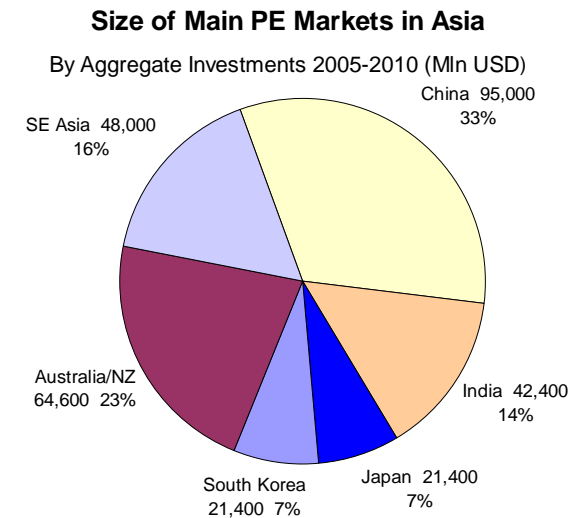
Meanwhile in Asia and Southeast Asia ...

Asia's Private Equity Markets

- Emerging Asia
 - China
 - India
 - Southeast Asia
 - The Rest (Pakistan; Bangladesh; Central Asia; other)
- Industrialised Asia
 - Japan
 - Taiwan, South Korea
 - Australia, New Zealand



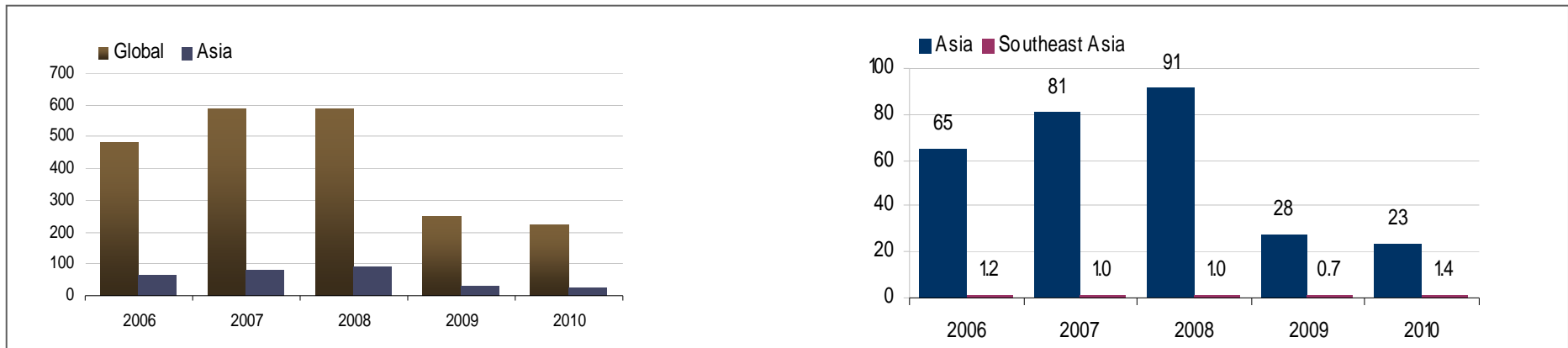
- Emerging Asia: 55% of Asia
- China single largest market
 - One third of total Asia
 - Well over 50% of Emerging Asia
- India 2nd largest Emerging Asia market
- SE Asia: around 8% (excl. Singapore)



Source: AVJC; Recof M&A; McKinsey

PE in Asia and Southeast Asia before and after the GFC

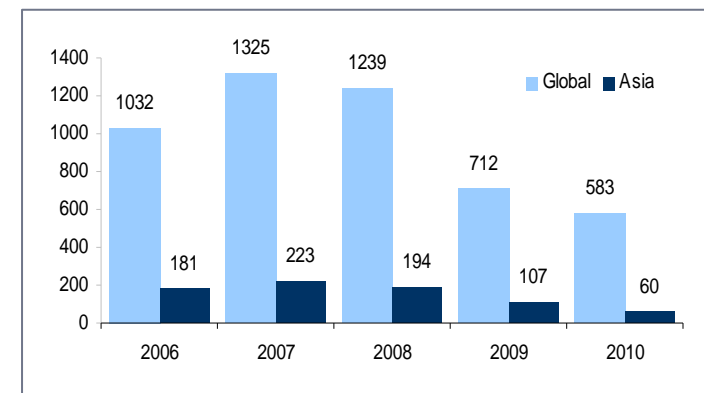
Aggregate Amount of PE Capital Raised 2006-2010, Global, Asia and Southeast Asia (US\$bn)



Sources: Preqin; EMPEA, PE Round up 2010

- Global PE fund raising continued to deteriorate in 2010 but is expected to pick-up again in 2011
- Between 2008 and 2010 Asia fund raising contracted at roughly the same rate as global fund raising both in terms of amounts and number of funds
- By contrast, Southeast Asia fund raising remained level throughout boom & crisis and increased in 2010

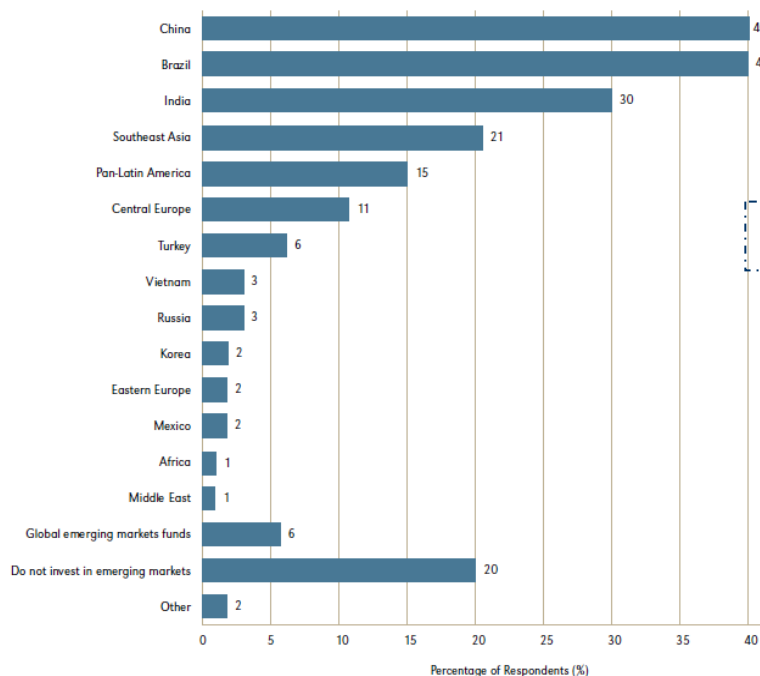
Number of Funds Raised 2006 - 2010



Southeast Asian Market Increasingly Attractive to Investors

Most Attractive Emerging Markets

“I find the most attractive emerging markets to be: (Choose no more than two).”

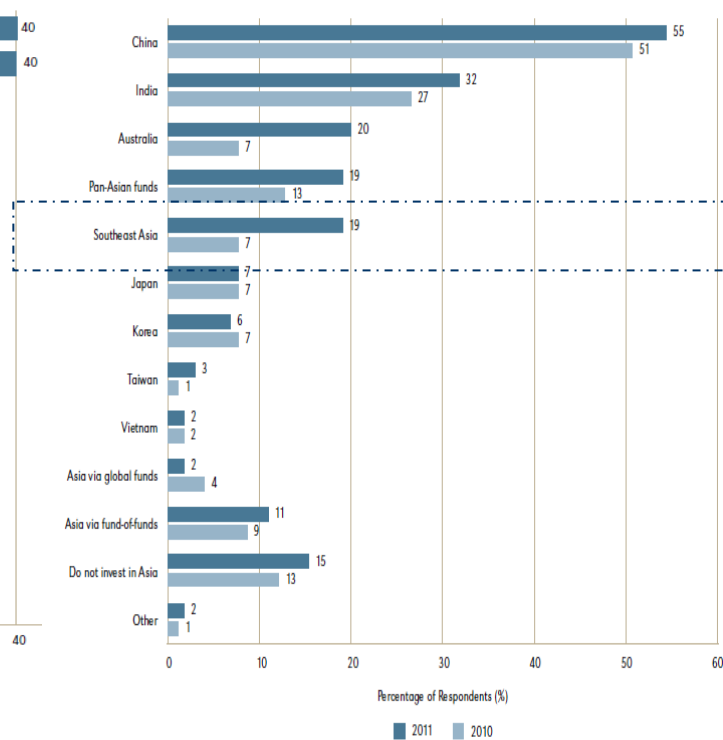


Southeast Asia seen as one of the four most attractive emerging markets

Respondents who rate Southeast Asia as an attractive Asian market increased by 12%--the largest increase among Asian markets

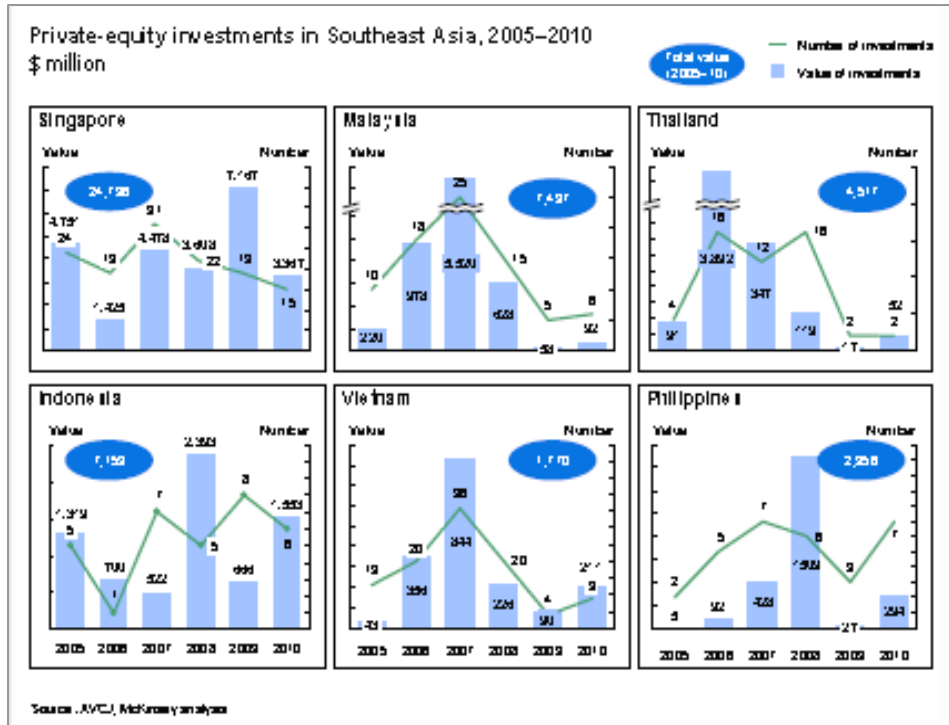
LP asset allocation to PE/VC will increase or stay the same.

“Which Asian market do you find most attractive at the moment?” (Choose no more than three)



Source: Probitas Partners Private Equity Institutional Investor Trend Survey for 2011

Private Equity in Southeast Asia



- Until recently submerged in "Asia" basket
- In overall scheme of PE investments and fund raising in Asia still relatively small
- Half of PE investments by value over 2005-2010 period in Singapore and 28% by number
- Emerging SE Asia
 - Growth & Expansion in terms of # deals most important
 - Buyouts by volume largest
- As in China and India, PE Penetration in SE Asia relatively low: 0.3% of nominal GDP
- Perceived investment opportunities in sectors that leverage on economic growth and attractive demographics: fast moving consumer goods; branded goods; retail; health care and education

Growing Investor Interest in Southeast Asia

- SE Asia benefiting from investors' interest shifting to Asia as a whole
- SE Asia increasingly seen as a region *suis generis* and a complement—if not alternative—to China and India as investment destination
- After many false dawns ASEAN integration given benefit of the doubt
 - ASEAN promise of incremental economic if not integration then at least synchronisation
 - The EU Accession process has shown that the journey is more important than the destination
 - Measures taken to facilitate the movement of goods and capital perhaps even labour within ASEAN may lead to stronger growth and somewhat more efficient economies
- SE Asia story driven by economic growth especially in Indonesia and (to a lesser extent) Vietnam and, more recently, Thailand



Indonesia the next "I" in BRIIC?

- Like Vietnam in 2006-2007, Indonesia increasingly seen as a key emerging market in Asia
- Like Brazil before the 2000s, forever the most promising young kid on the block

Buyout funds see Indonesia as next Asia stop for deals



REUTERS Thu, Feb 11 2010

JAKARTA/HONG KONG (Reuters) - Indonesia, Southeast Asia's biggest and fastest-growing economy, is becoming a new focus for a growing number of global buyout funds, drawn by improving stability and strong commodity prices. As deal valuations no longer look so attractive in Asia's most popular destinations for foreign investment, China and India, dealmakers are trying to find alternatives in Asia, the fastest-growing continent, private equity executives say.



Indonesia's GDP beats forecasts

Indonesia announced better than expected figures for 2010 growth in gross domestic product, making it one of the fastest growing economies in the G20 group of nations.



Indonesia?

"Berlin, a city condemned forever to becoming and never to being"

Karl Scheffler, 1910

Southeast Asia PE Fund Raising

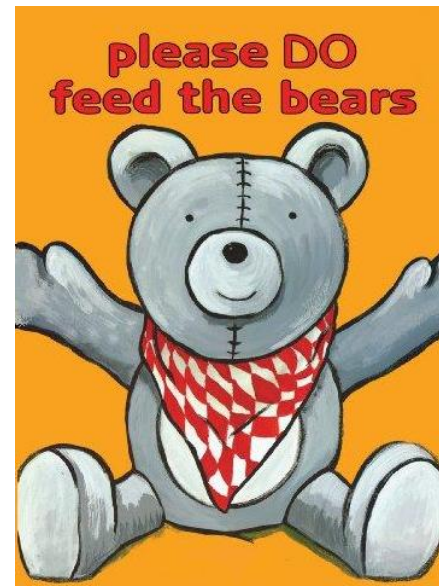
- Of PE funds active in SE Asia, in terms of volume of investments, only 20% managed by dedicated Southeast Asia GPs
- Over the past three years, the focus of existing fund managers has largely been on salvaging portfolio companies
 - Problems much less severe than in Europe as (SE) Asia never really had a crisis
 - As elsewhere, the bullet has been bitten and most losses have been taken
- During GFC only few GPs could afford to raise new funds
 - Previous fund >75% invested
 - Track record
 - Not distracted by portfolio management problems
- Who will be on the road?
 - Trend towards regionally focused funds
 - Only tested and tried fund managers with a track record of investing, successfully managing a portfolio and surviving the GFC can expect to be successful with fund raising
 - Large fund managers in US and Europe focused on steadying the ship at home and (partly) missed the boat in (SE) Asia and may look to GP acquisitions here
 - Most new funds that will be raised can expected to be traditional private equity style, closed-end funds
- Necessity to adopt and give substance to an active ownership approach
 - Operational capacity
 - Active ownership tool kit

Investment Style and Private Equity Strategy in Southeast Asia

- As a result of the crisis—as elsewhere—in Southeast Asia strategies more focused in terms of investment theme, sectors and geographies
- Relatively high-cost proposition to be fund manager in Southeast Asia with regional coverage
 - Varied geography (different economic, political and cultural environments to work in)
 - Deal size smaller
 - Deal flow smaller
 - Overall: higher USD cost/USD investment ratio
- Expansion (main PE investment style as opposed to buy-outs, Ventura Capital and mezzanine)
- To a limited extent buy-outs with mid-market focused buy and build strategies
- Infrastructure emerging as a theme but, in parallel, globally is developing into a distinct asset class
- Private equity industry relatively young and, as such, now well known to vendors. Deals tend to take longer and are more difficult to close than in more advanced private equity markets
- Role of Local (SE Asia) GPs:
 - Between 2007 and 2010, the role of local GPs declined in terms of deal volume (US\$)
 - More focused on small and mid-sized deals
 - Competition increasing as Pan-Asia funds are now looking with more interest to Southeast Asia

Conclusions

- The Future of Private Equity in Asia in general and in Southeast Asia in particular looks promising but is vulnerable to macro-economic and political events
- GP environment will become more competitive
- GPs will have to raise their game
- Beware of the Return of the Stampeding Herd: Keep the Bears Well-fed





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