



<u>Committee and date</u> Pensions Committee	<u>Item / Paper</u>
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PRIVATE EQUITY

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Summary

The report provides Members with the current position on the actual level of investment in Private Equity compared with our target level of investment. It explains why it is necessary to commitment to a third cycle of investment in the asset class in order to reach our target level of investment of 5% of the Fund and achieve diversification across time periods. The report highlights that HarbourVest continue to be "A" rated by Mercer and the HarbourVest proposal to commit \$22.2 million to the HIPEP VI Partnership Fund.

Recommendations

Members are asked to:-

- A. Note the recommendation of HarbourVest to commit \$22.2 million to the HIPEP VI Partnership Fund.

REPORT

Background

1. In 2002 HarbourVest Partners were appointed as fund of funds manager for the Funds allocation to private equity. A 3% strategic allocation was made to private equity and \$30 million (£18.2 million) was committed at this stage as part of the first cycle of investment. The HarbourVest fund of funds are denominated in either US dollars (\$) or Euros (E) and the Fund makes its commitments in these currencies.
2. Members will be aware that when an Investment Manager is appointed funds will be provided on the inception date for the Investment Manager to invest. Private equity is different to any other asset class in that the Fund makes a commitment to invest in the asset class and the Investment Manager only draws down funds for investment when opportunities are identified.

3. Private equity commitments can take a number of years to be drawn down. So whilst the Fund had committed \$30 million in 2002, by 2005 it was finding that its actual investment was significantly below this level. In 2005 the Pensions Committee made the decision to over commit to private equity up to a maximum of 2.5 times the strategic allocation so as to increase the actual level of investment towards the strategic allocation of 3%. The Fund at this time committed a further \$70 million (£42.4 million) to a second cycle of investment in the HarbourVest fund of funds.
4. The second cycle of commitment in 2005 increased both the frequency and size of private equity drawdowns and the actual level of investment has increased to 3.5% of the total Fund. In March 2009, the Pensions Committee made the decision to increase the strategic allocation to private equity to 5%. This is to be funded by a reduction to the allocation to UK equities.
5. In order to reach the target 5% strategic allocation to private equity it is necessary to commit to a third cycle of investment.

Cash Flow Characteristics

6. The commitments made to private equity in the first cycle of investment in 2002 have largely been drawdown and invested. The Fund has also received some significant income from distributions when the underlying private equity investment are realised, by for example, a takeover or flotation. The Fund has received distributions of \$13.7 million (£8.3 million) from its first cycle investments. The first cycle of investments has delivered good returns with the HIPEP IV Partnership Fund, for example, delivering annualised returns of over 15% since inception to the end of June 2009. HarbourVest will be attending Pensions Committee as part of the routine cycle of meetings and will explain the performance of existing investments.

	Commitment	Drawdown	Distributions (Investment Income to SCPF)
Cycle 1 (2002)			
HIPEP IV - Partnership	\$15 million	\$13.4 million	\$12.2 million
HVP VII – Venture	\$6 million	\$4.5 million	\$0.2 million
HVP VII- Buyout	\$9 million	\$6.4 million	\$1.3 million
	\$30 million	\$24.3 million	\$13.7 million
Cycle 2 (2005)			
HIPEP V – Partnership	E 25.1 million	E13.6 million	E 0 million
HIPEP V – Direct	E 6.3 million	E 5.0 million	E 0.3 million
	E 31.4 million	E18.6 million	E 0.3 million
HVP VIII - Venture	\$12.0 million	\$5.0 million	\$0 million
HVP VIII - Buyout	\$23.0 million	\$7.8 million	\$0 million
	\$35.0 million	\$12.8 million	\$0 million

Note – All figures as at June 2009

7. The second cycle of investments is still at the investing stage and the distributions to date are minimal.

- 8. HarbourVest have modelled the forecast drawdown and distributions associated with the current commitment levels. The Fund is not expected to reach its 5% strategic allocation with its current commitment levels (Appendix A). After 2010 it is expected the actual level of investment as a proportion of the total Fund will fall as private equity investments are realised and the proceeds distributed.

Proposed New Commitments

- 9. HarbourVest Partners recommend that the Shropshire Fund commits to a third cycle of investment so as to reach its target level of investment of 5% of the total Fund.
- 10. It is important that the Fund's private equity investments are diversified across time periods because different stages of the economic cycle provide differing opportunities for private equity investment. HarbourVest believe that investing in a third cycle will also provide diversification across time periods.
- 11. HarbourVest recommend that the Fund commits \$22.2 million to HIPEP VI Partnership Fund. This is a diversified fund of funds offering exposure to investments to European company buyouts as well as buyout and venture capital opportunities in Asia Pacific and Emerging Markets. This Fund is the successor to HIPEP V in which the Fund currently invests.
- 12. HarbourVest will be offering US private equity fund of funds (HVP IX Venture & Buyout) in 2010. HarbourVest recommend that commitments to this HVP IX are considered by Pensions Committee in 2010.

	Recommended Commitment
Cycle 3	
HIPEP VI – Partnership	\$22.2 million
HVP IX – Venture	} to be made
HVP IX- Buyout	} in 2010.

- 13. HarbourVest will attend Committee to present their recommendation for a new commitment to the HIPEP VI Partnership Fund.

Mercer Opinion

- 14. The Fund takes advice from Mercer Investment Consulting regarding its private equity investments. Officers have consulted with Mercer who have confirmed that HarbourVest continue to be “A” rated (Mercers highest rating). Attached at Appendix B is the latest Mercer research note on HarbourVest.

List of Background Papers (This MUST be completed for all reports, but does not include items containing exempt or confidential information)

Pensions Committee, 25 November 2005, Item 10, Paper C – Private Equity

Human Rights Act Appraisal

The recommendations contained in this report are compatible with the provisions of the Human Rights Act 1998

Environmental Appraisal

Not applicable

Risk Management Appraisal

Regular monitoring of investment managers and their performance will ensure regulatory compliance and give early warning of areas of difficulty and potential loss.

Community / Consultations Appraisal

N/A

Cabinet Member

N/A

Local Member

N/A

Appendices

A – Private Equity – Cashflow Model

B – Mercer rating on HarbourVest Partners