OPALESQUE
PRIVATE EQUITY STRATEGIES

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Happy holidays and welcome to the second issue of *Private Equity Strategies.* This month we open with a continued discussion of where private equity in the US is headed. In the last issue, we discussed the industry's search for its public identity in the wake of the US' first private equity candidate, Mitt Romney. Now we look at new survey data from global accounting firm Grant Thornton as well as a survey from global private equity firm Coller Capital both of which show stiff competition for North American private equity firms on their home turf and abroad.

A contributed article from private equity attorneys at Dechert examines new developments in acquisition finance, including notable court rulings.

Regs Watch offers updates on a full scope of new guidelines, recent court cases and 2013 outlooks that include continued discussions on dividends, tax rates and carried interest as the US and global governments dig in on implementing new revenue increases and regulations.

Movers and Shakers highlights the chemical industry as a bright spot for private equity investments in 2013. The companies represented in the diverse chemicals sector are grabbing the attention of private equity firms the world over as they seek companies well positioned for growth.

In our Dealmaker Q&A we will speak with Valiance, a British private equity firm that has recently partnered with SLC Land Co. Brazil's largest publically traded agriculture firm in a 50/50 deal to acquire several large farming operations in an effort to dramatically increase the country's agricultural output through the support of private equity.

We'll continue our exploration of Brazil and Latin America in our Data Snapshot, which provides detail on investment in the region over 2012 and looking forward into 2013.

In Tools of the Trade we talk with Stuart Keeler of eFront, a London-based company that works with GPs on reporting. Keeler is joining many GP's in calling for a unified reporting standard in private equity, similar to the SWIFT system in banking. We will also take a quick look at a new, free environmental assessment tool launched by the Environmental Defense Fund designed to help private equity firms manage their environmental impact.

Finally, we offer brief updates on recent transactions and people moves in Quick Hits. Our events calendar will look at the events happening in the remainder of this year and leading off 2013. I do hope all of you enjoy the holiday season! Please send any updates or feedback on this publication to me at mccann@opalesque.com - I'd love to hear from you.

Best,
Bailey McCann
Editor

In This Issue

North American Private Equity Firms Facing New Global Competition

Bailey McCann
Private Equity Strategies

Last month, we discussed the impact that the US Presidential election and specifically, Mitt Romney's candidacy had on the reputation of private equity in the public consciousness. Even though the votes have been cast, and the US and indeed the rest of the world is more focused on the fiscal cliff, private equity still finds itself with an image problem.

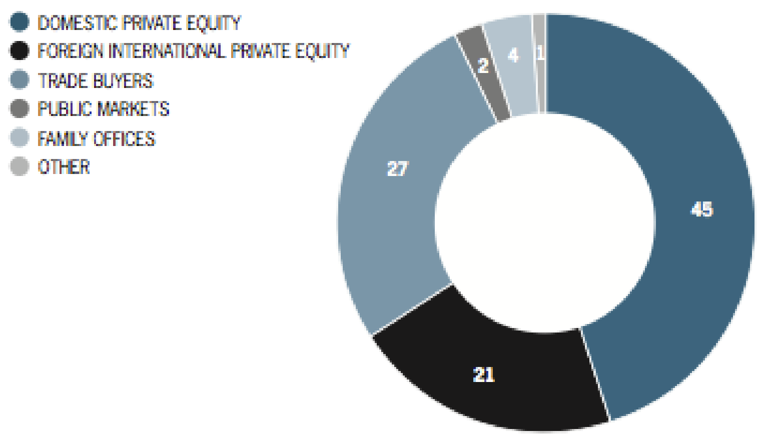
At the end of November, the industry was implicated, perhaps unfairly, as part of the problem in the collapse of poorly managed Hostess. Other articles have noted the shift happening within the structure of firms away from pure play private equity into more broad based asset management or alternative investment firms – further adding to the confusion. Now, new data shows that even while US firms work on all of these issues, international competition is snapping up key deals in the US and abroad.

Structures and products

As this publication noted in its first issue, firms that might once have been considered pure private equity are diversifying into other business lines. Some are now offering hedge funds, closed-end funds, or business development companies as a means of drawing new capital and opening up new investment opportunities. While this may be great news for general partners and their investors, it further underlines the need for improved education to investors and the public about what each of these structures mean.

Changes in regulatory requirements in the US have also forced private equity firms to register with the Securities and Exchange Commission (SEC), making it much more difficult for firms to stay off the radar. These factors, coupled with growing transaction sizes, and the trend

FIGURE 1: EXPECTED SOURCES OF COMPETITION
PERCENTAGE OF RESPONDENTS



SOURCE: Grant Thornton

toward dividend recapitalization ahead of new tax rates, make it seem like the spotlight on private equity is here to stay.

A piece in the *New York Times* quoting Richard Trumka, president of the A.F.L.-C.I.O, summed up the populist view, "what's happening with Hostess Brands is a microcosm of what's wrong with America, as Bain-style Wall Street vultures make themselves rich by making America poor."

The Hostess debacle added shelf life to an idea that emerged during the Presidential campaign – that something could be "Bained." The piece notes rightly that Ripplewood – the private equity firm involved in the Hostess collapse, neither got rich quick, or mimicked Bain in any real way. Yet, the perception is important. Attack ads during the election looked at the communities in the US that had been Bained too. What does this mean for the industry, in the new era of regulation and transparency? Why is private equity so loathe to point out the benefits it provides to the broader economy?

Perception has a way of becoming reality. As the specter of getting Bained takes over for an aging Gordon Gekko in the pantheon of finance archetypes that are simultaneously hated and glorified, it falls to the industry to offer a counterpoint. So far, not much of one is emerging. But, that may change if international private equity firms have anything to say about it. North America's global competition is rapidly becoming the new face of the industry.

Here comes everybody

Private equity firms in the United States are facing increased competition from foreign and international firms for investment opportunities within the U.S. market, according to the 2012 Global Private Equity Report by Grant Thornton International. 43% of global respondents to the survey plan to open an office in North America within the next two to three years.

"North America, and the United States specifically, is a far more mature investment market than others around the world, so it's not surprising that there is increased interest from global PE firms to invest here," said Carlos Ferreira, a partner in Transaction Advisory Services of Grant Thornton LLP. "PE firms here have to realize that they're not the only ones invited to the show—they are going to have to figure out a way to thrive despite this growing competition from foreign investment firms."

Another telling statistic in the survey was this – 65% of North American respondents believe the image of their industry is deteriorating. Whereas half of respondents in the MENA region see their image as improving as private equity gains a greater foothold in that area and the firms based there make a global reputation for themselves. The majority of MENA and BRICs firms represented in the survey indicated that they are looking for global – read North American investment opportunities and plan to open offices here.

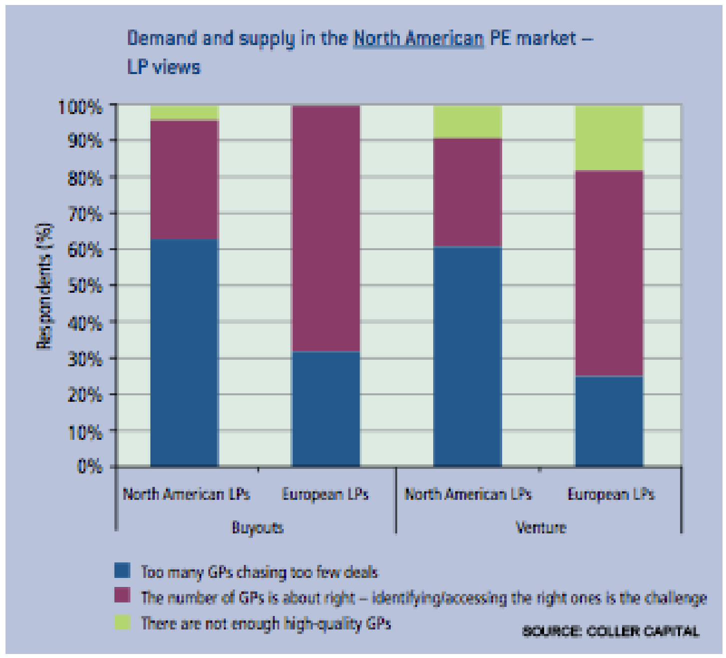
This image problem could have a material impact on the fundraising lifecycle for US private equity firms. According to the survey, in 2012 40% of respondents said that their next funds would be majority funded by first time investors. That's up from 24% in 2011. These first time investors may be less willing or able to look past questions over image. Some leading indicators like Cerebus announcing its interest in selling Freedom Group in the wake of the Newtown Massacre show an awareness of this perception problem.

North American LPs circle the wagons

Even where GP's are making these realizations internally and working to respond strategically, perception may be catching up to them in another material way. According to data in Coller Capital's Global Private Equity Barometer, almost two thirds of North American investors believe too many GPs are chasing too few deals in the region – both in buyouts and venture capital. This view is reflected in LPs' plans for their number of GP relationships: around half of North American investors plan to reduce their roster of GPs over the next two years. Coller Capital is a global investor in the secondary private equity markets.

Adding to this troubling news, another data point in the survey shows that two thirds of North American LPs believe that the weakness in IPO markets is not purely cyclical but is partly a structural phenomenon – a worrying prospect for private equity in the long term.

Still, GP's do hold some good cards. 38% of investors said they would back GPs on a deal-by-deal basis, looking beyond the traditional fund-investing model. 80% of investors in the survey also expect returns of 11+% from their private equity investments – giving private equity a fairly significant edge over other asset classes. Whether it's enough of an edge to leave the image question unanswered, remains to be seen.



Recent Developments in Acquisition Finance

by Jeffrey M. Katz and Scott M. Zimmerman,
Dechert LLP

Certain recent legal developments will likely impact acquisition finance. This article will survey some of the more notable ones.

We discussed in the last newsletter the Eleventh Circuit Court of Appeals' decision in *In re Tousa*,[1] in which the court affirmed a bankruptcy court decision ordering the return of more than $400 million that had been repaid to prior lenders of a parent company in connection with a subsequent secured financing to the parent and its subsidiaries. Among the key elements of the decision were findings that the subsequent financing was a fraudulent transfer in respect of the subsidiaries not obligated on the loan to the parent entity repaid with the proceeds of the financing, and that various of these subsidiaries were or became insolvent at the time of such financing, despite representations and opinions as to their solvency given at the time.

A recent decision of a U.S. District Court in Indiana highlights some of the risks stemming from *Tousa* in the acquisition finance context, particularly for leveraged buyout financing.

In *Mathioudakis v. Conversational Computing Corp.*,[2] the District Court refused to dismiss an action to hold an individual, who was both the controlling shareholder and chief executive officer of a corporate borrower, personally liable for a loan made to the corporation which he had not personally guaranteed, on a theory of "piercing the corporate veil." Ordinarily the lack of a personal guarantee for a corporate loan would mean a lack of personal liability for control persons and executives on the corporate loan. The court's decision to "pierce the veil" and hold the individual personally liable was based on both an intentional misrepresentation by the individual to the lender on which the lender relied, and the undercapitalization of the corporation at the time of the loan.

In 2005, defendant Stephen Rondel, founder and chief executive officer of Conversational Computing Corp., requested and received a loan from plaintiff Michael Mathioudakis, based on Rondel's representation that his company was about to receive a substantial wire transfer from a foreign investor and was in need only of short-term financing in order to meet upcoming payroll. Rondel represented that the wire transfer was all set, and was being held up only on account of procedural issues relating to Patriot Act requirements that would be resolved quickly. The loan was made to the company and, as noted, not guaranteed by Rondel personally.

The corporate borrower never received any of the foreign investment as Rondel had represented, defaulted in repayment of the loan to the lender, filed for bankruptcy protection, and was found by the bankruptcy court to have been undercapitalized at the time the loan was made. On the basis of Rondel's intentionally misleading the lender into believing a substantial foreign investment in the company was imminent, when nothing of the sort was the case, and the finding that the corporate borrower was undercapitalized at the time, the court refused to dismiss plaintiff lender's action for personal liability against Rondel on a theory of piercing the corporate veil, notwithstanding the absence of his personal guarantee of the loan.

Under a strict reading of the court's decision, which applied Indiana state law on veil-piercing, the court held that the undercapitalization and intentional misrepresentation alone were enough, as a matter of law, not to dismiss the action for personal liability against Rondel. Whether the executive making the misrepresentation was also the controlling shareholder seemed not directly relevant to the court's analysis, so long as the injustice or fraud perpetrated by the misrepresentation was sufficient. Indiana state law requirements for veil-piercing are easier to satisfy than the corresponding requirements of many other states, including New York, for example, where there is a strong line of authority limiting successful veil-piercing to claims against controlling shareholders. Between New York, where this and other more stringent requirements for veil-piercing apply, and Indiana, where cases have allowed such claims to go forward against non-shareholders and under somewhat looser criteria generally, lie a host of other states' laws falling at various points along the continuum of veil-piercing requirements.

In terms of the issue of solvency of the various obligors in a borrowing group in the acquisition finance context, such issue is fundamental, especially in leveraged buyout financings featuring liens granted by the target entities, where the proceeds typically are used by the acquiror to finance the acquisition, and will not be paid to or held by or for the benefit of the target entities. Under the rationale of *Tousa*, to the extent any of the relevant entities is rendered insolvent by the financing, there is a risk that the financing could be unwound as to such entity on fraudulent transfer grounds.

In this light, some financing arrangers have begun requesting that borrower groups make solvency representations for each entity in the consolidated group on a stand-alone basis. Such a representation has not yet by any means become market practice, or even common for that matter. However, if a borrower should consider making such a representation individually for one or more of the relevant subsidiaries serving as guarantors, it will need to be very cautious in doing so, especially given the rationale of a case such as *Mathioudakis*. For if a solvency representation for a particular entity within a consolidated borrower group is deemed by a court (after the fact) to have been intentionally misleading, or perhaps made even with a reckless disregard as to whether it was true, such misrepresentation and insolvency together, under the rationales of *Tousa and Mathioudakis*, may potentially give rise to assertions of personal liability against the executive who made the false representation as to solvency, at least where a lender could show reasonable reliance on it.

Insolvency and undercapitalization are not identical concepts, of course; yet they are related notions. Insolvency for fraudulent transfer purposes is most often determined on a balance-sheet basis, in terms of the fair value of assets over liabilities on the date in question, whereas undercapitalization generally refers to whether an entity has sufficient capital to run its business given its ongoing access to and sources of capital. In a case in which an entity is determined by a court to have been insolvent for fraudulent transfer purposes, it may be difficult persuading the court that the entity was not also undercapitalized, if the court is considering the issue of veil-piercing asserted by a party in interest.

Tousa is a decision of the Eleventh Circuit Court of Appeals, and *Mathioudakis* one of the U.S. District Court in Indianapolis that applied Indiana state law in its veil-piercing analysis, so there is not much in terms of direct precedential effect for cases in the second and third Federal circuits (including New York and Delaware, respectively). Still, these are potentially significant developments that could lead in certain cases to claims of personal liability that otherwise would seem wholly without merit. Such a claim might be asserted in a case featuring an eclectic mix of variables including a liberal state law on veil-piercing, solvency representations made by a principal executive in respect of an individual entity or entities found to have had little or no basis in fact, a court considering the solvency of individual entities in a consolidated group independently under a *Tousa*-type analysis, and thin capitalization and insolvency of the relevant entity or entities.

A recent decision by the Second Circuit Court of Appeals,3 in the context of an initial public offering (IPO) of a previously acquired target, provides a measure of clarity for contracting parties regarding enforceability of certain contractual rights.

Tyco International Inc. (Tyco) had acquired CIT Group Inc. (CIT) in 2001. In the following year Tyco chose to spin off CIT in an IPO, in connection with which CIT would be merged into a Tyco subsidiary that had $800 million of net operating losses (NOLs) that could be used to offset CIT's future tax liabilities. CIT agreed to pay Tyco for its use of these NOLs.

CIT filed for bankruptcy in 2009, before utilizing all the NOLs, and in the bankruptcy process rejected its prior agreement with Tyco obligating it to pay for the NOLs. Tyco accordingly asserted a claim against CIT for breach of contract, typical for contracts rejected by a debtor in a bankruptcy case. However, CIT argued that Tyco's asserted damages ultimately arose in connection with the purchase and sale of CIT equity in the IPO, and should thus be treated like equity interests and subordinated to the claims of CIT's other creditors, under Section 510(b) of the Bankruptcy Code. That section accords a claim for damages arising "from" the sale of common stock with only the priority of an interest in common stock. Tyco asserted that its claims were ordinary breach of contract claims, i.e., obligations, and not equity interests.

The bankruptcy court, affirmed by the Second Circuit, agreed with Tyco and held that Tyco's claims not be treated as equity merely because they had some connection to the purchase and sale of equity in CIT's IPO. The Bankruptcy Code's subordination of claims arising from breach of a contract for the sale or purchase of equity is based on the notion that a party to such a contract with a debtor has the expectations of a shareholder rather than a creditor, and should thus not be allowed to receive a higher priority on account of the breach of an agreement to become a shareholder of the company. Tyco's claim, however, related to its transfer of NOLs to CIT, not to the purchase or sale of equity in CIT. Accordingly, the court allowed Tyco to pursue an unsubordinated debt claim against CIT. The Second Circuit upheld the decision of the bankruptcy court utilizing the same rationale.

This decision is noteworthy because a contrary ruling by the Second Circuit would have created uncertainty for contracting parties in such instances, where their agreement with a debtor is not for the purchase or sale of equity, but consummated within the context of an equity transaction by the debtor. If a tangential connection to an equity transaction would effectively subordinate a party's contractual claim against the entity in question to claims of its other creditors, the same might become an additional hindrance to transacting business with a stressed or distressed entity. The Second Circuit avoided this result with its ruling.

A recent District of Arizona bankruptcy court decision4 may tip the scales to some degree in favor of a debtor trying to stave off a secured creditor pursuing a loan-to-own strategy in a chapter 11 case.

In this case, the court refused to disqualify a creditor's vote approving a debtor's proposed chapter 11 plan of reorganization, where the debtor and creditor seemingly had cooperated, first, in impairing the creditor's claim in a minor fashion, and then classifying that claim separately, for the apparent purpose of meeting the chapter 11 condition that at least one impaired class approve the plan of reorganization. The plan thus would be confirmable over the objections of other classes of creditors, by having satisfied that condition under the Bankruptcy Code for confirming a plan over such objections.

BATAA/Kierland, the debtor, in the period leading up to its chapter 11 filing, financed its purchase of certain computer equipment and, after the filing, agreed with the lender that the interest rate on the loan would be reduced to 5% from 8%. The loan was classified separately by the debtor and also classified by the debtor as impaired in its reorganization plan, and the equipment lender then proceeded to approve the plan. A disapproving creditor challenged the separate classification, claiming that the debtor had colluded with the lender in bad faith to artificially create an impaired creditor class that would vote to approve its plan of reorganization. The challenging creditor claimed that the equipment lender's vote in favor of the plan was not made in good faith and should be disqualified (or "designated"), asserting that the equipment lender's approval was given merely to increase its prospects for future business with the debtor on its emergence from chapter 11.

The court was unwilling to consider possible ulterior motives of the debtor or the equipment lender, and found that the lender's voting for plan approval to enhance its prospects for future business with the debtor was in fact a legitimate objective of the equipment lender, because it had acted in its own enlightened self-interest and as a creditor. The court found no indication of fraud or attempt by the lender to obtain more than it otherwise was entitled to under the Bankruptcy Code.

The court also held that it was not improper for the debtor to have created, in contemplation of its bankruptcy filing, a new creditor class that it believed would be receptive to its reorganization plan, and that it would not inquire into the debtor's motives for classifying and treating different claims as it did nor consider alternate classification and treatment alternatives the debtor might have employed. The court cited the decision of the Second Circuit Court of Appeals in *In re DBSD North America, Inc.*[5] in support of its decision, a case we had discussed in an earlier newsletter.

The case supports a debtor's ability, at least in some measure, to creatively classify its claims in coordination with certain favored creditor constituencies in order to enhance prospects of confirming its proposed plan of reorganization, and to begin laying the ground for this ahead of its bankruptcy filing. This could potentially frustrate the objectives of other creditors, which otherwise may be well-situated to control the case and have their own plan of reorganization approved. For example, a secured creditor whose claim is impaired and holds what appears to be the fulcrum security in the case, potentially could be thwarted or delayed by a plan of reorganization proposed by the debtor that is approved by another impaired creditor class creatively classified by the debtor and structured in coordination with it. This potentially could occur in a case in which a bankruptcy judge can find the technical criteria for plan confirmation over creditor objections satisfied, and where the objecting creditor pursues a type of distressed or other investment strategy that the judge in question does not admire.

A final note follows up on an item previously reported, and concerns new Treasury Regulations that apply to debt instruments issued on or after November 13, 2012, expanding the definition of when a debt instrument is considered to be "publicly traded" for purposes of determining its issue price. The determination of the issue price of a debt instrument can have a significant impact both on the borrower and on the holder of the instrument. It is particularly important in the case of a debt-for-debt exchange, including when an amendment of debt causes a "significant modification" for U.S. federal income tax purposes (treated as a taxable exchange of hypothetical "old" debt for hypothetical "new" or amended debt). In such circumstances, the amount of the issue price of the "new" or amended debt instrument is of great importance because

1. the amount of original-issue discount associated with the "new" or amended debt instrument is determined based on the difference between the instrument's issue price and its stated redemption price at maturity,
2. the issue price is used to determine whether the borrower has (and the amount, if any, of) cancellation-of-debt income taxable to the borrower resulting from the exchange, and
3. the determination of the holder's gain or loss from the exchange depends on whether the holder's basis in the "old" debt instrument is greater or less than the issue price of the "new" debt instrument.

The new regulations could be relevant, for example, in the case of a portfolio company amending its loan agreement for covenant relief, in exchange for fees or increased loan pricing. The new regulations increase the likelihood that a loan amendment could result in substantial cancellation-of-debt income for the borrower, depending on the amount of discount (if any) at which its debt was trading and other factors. A borrower considering an amendment to its loan documentation should therefore carefully consider possible tax implications and the possible impact of these new regulations.

We look forward to updating you on additional developments in the next issue. The current full issue of Dechert's Private Equity Update is available here.

Footnotes

1 *In re Tousa, Inc.*, 680 F.3d 1298 (11th Cir. 2012).

2 *Mathioudakis v. Conversational Computing Corp.*, 1:12-cv-00558, 2012 WL 4052316 (S.D. Ind. Sept. 13, 2012).

3 *In re CIT Group Inc.*, 479 F.App'x 393 (2d Cir. 2012).

4 *In re BATAA/Kierland, LLC,* 476 B.R. 558 (Bankr. D. Ariz. 2012).

5 *In re DBSD North America, Inc.*, 634 F.3d 79 (2d Cir. 2011).

Regs Watch: Brief Updates on Changes in Regulation for Private Equity

A a journalists like me and lawyers have written ad nauseum, new and ever more regulations are in the pipeline for private equity and alternatives as a whole. Here we will hit on some of the cases of note and provide links to new guidance over the past month.

Bribery is Still Bad:

The US Department of Justice (DOJ) and the Securities and Exchange Commission (SEC) have released updated guidance on the Foreign Corrupt Practices Act. Basically, bribery is still a bad idea, but now there's a fact sheet for easy cross referencing, if someone offers you a bribe.

National Gas Fuel Company Withdraws its Own Suit:

National Fuel Gas Company, has withdrawn its own lawsuit after a shareholder proposal submitted by the Harvard Shareholder Rights Project, on behalf of a public pension benefit trust, sought declassification of the company's board of directors. The company withdrew citing procedural issues surrounding the proposal.

Court Sides With Private Equity on ERISA Liability:

The Federal District Court of Massachusetts sided with Sun Capital Partners over withdrawl liability in the case involving the New England Teamsters & Trucking Industry Pension Fund. "Specifically, the court found that the PBGC had incorrectly applied the law of agency by attributing activities of a private equity fund's general partner (which had provided certain management and advisory services to the fund's portfolio companies for a fee) to the fund itself," explain attorneys with Hunton & Williams.

New Tax Rules in Luxembourg Focus Specifically on Private Equity:

The Luxembourg Parliament has approved the bill 6497 modifying the Luxembourg Income Tax Act. The changes will impact private equity firms, including increases to the alternative minimum tax for Luxcos. The alternative minimum tax rules will apply now even if the income is exempt under international law. Detailed guidance is offered here by attorneys with Bonn Steichen & Partners.

German AIFMD Tax Regime Implementation Hits Private Equity:

From a tax law perspective, UCITS funds and a limited range of tax privileged AIFs will be granted the favorable existing fund tax law regime. However, the draft legislation would bring about - prohibitive - product regulation, first via regulatory law and second via tax law, for a large number of AIF like many hedge funds and private equity funds. According to the latest InfoLetter from WTS Steuerberatungsgesellschaft mbH, in Germany, private equity funds operating there are likely facing new scrutiny and higher tax bills.

SEC Settles First-of-its-Kind Asset Valuation Case

The SEC has opted to settle with KCAP Financial, Inc., f/k/a/ Kohlberg Capital Corporation, over misstatements of exit prices and fair value. The number of these such cases are on the rise, two others closed this month.

Private Equity and Venture Capital Valuation Guidelines IPEV Board Releases Updated Private Equity and Venture Capital Valuation Guidelines:

Notably, these Guidelines take into account amendments to Fair Value accounting standards promulgated by the Financial Accounting Standards Board (FASB) in the United States and the issuance of Fair Value accounting standards by the International Accounting Standards Board (IASB). Full guidelines available here.

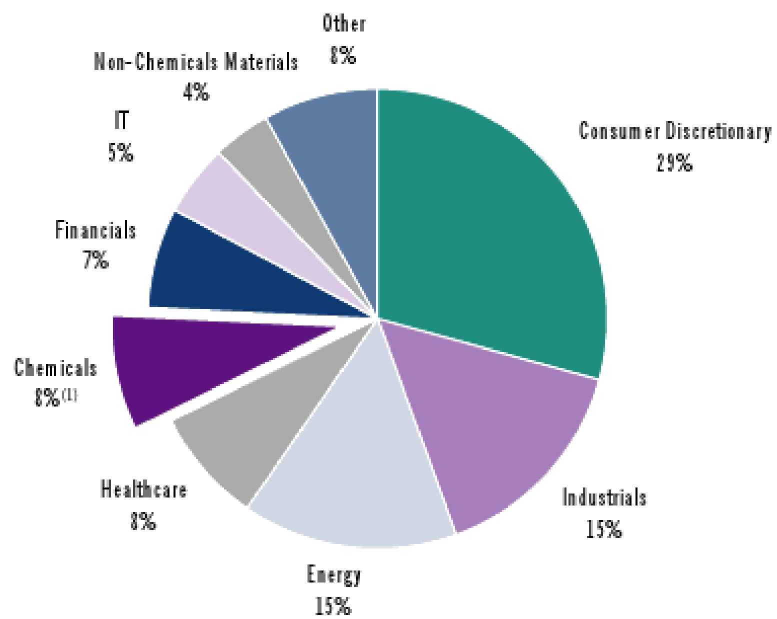
Dodd-Frank Progress:

Movers and Shakers: New Research Shows Big PE Play in the Chemicals Industry

Bailey McCann
Private Equity Strategies

Chemicals companies are becoming a hot item for private equity. The US chemicals sector is represented by 80-100 sub-sectors and has approximately $1tln in revenues. Of that, private equity firms control $64bn. Globally, chemicals account for $2.5tln in revenues. Private equity has had a varied role in this space in terms buying companies, and also securing discounts for strategic buyers which has supported consistent activity in chemicals M&A.

2012 YTD US Private Equity by Sector



Source: Capital IQ and Valence Group
1. Excluding the Carlyle/DuPont Coatings $5.1bn transaction, 2012 YTD private equity chemicals M&A would represent 3.0% of total industry M&A activity

As a group, chemicals companies have a lot to offer private equity firms. The industry is global, and much of the new activity grows with other sector spikes. The companies themselves also offer decent scale, relatively limited competition in their sub-sector, and high barriers to entry.

Secondary chemical deals have also seen new momentum this year – a trend that is likely to continue into 2013. Big names like Riverside Co. have recently announced secondary deals like their sale of chemical maker DuBois Holding Co. to Aurora Capital Group.

"Private equity, as it relates to the chemical industry, has been a consistent participant in M&A year after year," explains Telly Zachariades, partner in The Valence Group, a boutique M&A advisory investment bank specializing in the chemical industry. Private equity investment in chemical industry M&A accounted for 8% of private equity transactions in 2012 alone.

Since 2000, private equity has accounted for 17% of the chemicals industry total M&A Value, with 2007 marking the peak year at 20%. Historical data shows that relative to strategic buyers, chemicals transactions offer private equity a 7.2x multiple on average, making the space appealing for firms of all sizes.

"The financing markets for good chemicals properties are in good shape and relatively cheap," Zachariades says. Despite this, in order to invest, GPs have to come with greater technical understanding of the industry than they might otherwise. This makes for limited competition among firms but also stiffer competition overall.

The role of private equity in the industry has also changed, Zachariades notes. Early on, private equity may have been more focused on fixing, IPOing, or selling the business, but now much of that has changed.

"Private equity sometimes gets a bad rap, particularly in Europe, but that attitude is very old. There was a time long ago when private equity had a reputation as an asset stripper and cost cutter, but the attitude of private equity today is what can we do with this company to improve and grow it," he says.

Now private equity firms are more focused on growing their businesses rather than going to the IPO market. Some of that has to do with cost. According to Zachariades, companies need to be sizable, with an EBITDA north of $100m to justify an IPO. This reality means that companies and GPs alike are redefining what it means to add value, and grow in the space. Today, fixing broken businesses or consolidating niche areas are finding more favor.

Geographies can also provide opportunity – Asia is a rapidly growing region for chemicals M&A, and is on pace to continue attracting firms as those economies grow. "One third of the M&A activity now is coming out of Asia, in about five years I expect it will be half," Zachariades said.

Dealmaker Q&A: Valiance Advisors Partners With SLC Agricola for Major Brazilian Agriculture Effort

Bailey McCann
Private Equity Strategies

One of the core initiatives of the Brazilian government, and indeed Brazilian landholders is to make the country the new agricultural hub for the world. Brazil currently ranks #1 in exports of beef, chicken, and coffee, and is on pace to overtake the US in soybean production if not corn very soon. Despite this leadership role, the government and many new investors have been active in pushing the boundaries of yield and potential farmland in an effort to ramp up production.

SLC Agricola is one of these leaders. The company is Brazil's agriculture benchmark and one of the largest listed farmland operators globally – it went public in 2007. Current market cap for SLC Agricola stands at approximately $1bn. SLC Agricola was started in 1977 by SLC Land Co, which has been operating in agribusiness for 67 years, including a 20-year joint venture with John Deere.

The amount of land SLC Agricola owns and operates is 308,500 hectares, which is a land area 20% larger than the country of Luxembourg. Given this dossier, Valiance Advisors keyed in on SLC and Brazil when he began looking for agriculture opportunities. Valiance, founded in 2007 is a London-based asset manager focused on real asset and special opportunity investing.

"We have been focused on agriculture since 2008, and looking at the opportunities landscape, Brazil is a big standout to buy and operate farms in," Mark McLorrnan, Head of Agribusiness for Valiance, says in an interview with Private Equity Strategies. Agriculture accounts for nearly half of the Brazilian economy and almost 40% of its jobs. The country's corn exports recently provided a critical backstop against the lasting drought in the US Great Plains region, a reality which only added to the sense of urgency Brazil's agribusiness leaders feel to keep production high.

Under the terms of the over $400m partnership, SLC Agricola will have 50.6% and will be responsible for much of the operational heavy lifting. Valiance will have 49.4% drawing revenue on the land. McLornan is quick to point out that the partnership is all about action, both firms have already made significant moves this year and will continue into 2013.

"To date our partnership is capitalized at $300m, with $180m more to be invested over the course of 2013. We currently own three large farms and are in the process of acquiring three more," he says.

The process involved around taking these acquisitions from raw land to a functioning farm will take approximately three years. That includes all the logistics of permitting, making the land ready for farming, and planting – the real work in agribusiness. However, the returns on this work are notable – over the last ten years Brazilian farmland has an appreciation of approximately 12%.

More than just purchasing more land, the key differentiator for Valiance was SLC's focus on sustainable farming models. McLornan explains that in addition to adding acreage, SLC uses new agriculture technology to improve yield and reduce environmental footprint. Brazil has been the source of international scrutiny over how it balances the demands of its agribusiness economy against fragile local ecosystems like the rainforest. McLornan points out that Brazil has some of the strictest enforcement on land use and environmental impact, in large part because the world is watching. Brazil requires 30% of any land purchased to remain in its original state.

"In 8 years, the world will need 100m more acres to meet agriculture demands, in European terms that's 3x the size of England. Brazil has to increase its own productivity to meet that demand," he says, noting that what often gets lost in the conversation around large agricultural operations is the realities of global population and their food needs.

"The collapse in current grain stocks is missing from the conversation. People aren't realizing that these yearly population booms are already having a significant effect on grain stocks, that will only continue," McLornan says. "People talk a lot now about peak oil. They should be talking about peak food."

Latin America: A New Hotspot for IPOs:

According to a survey released by J.P. Morgan's Depositary Receipts (DR) business, 70% of institutional investors in North America and Europe who responded recommend that a Latin American company pursue an initial public offering in today's capital markets.

Survey participants believe that despite significant macroeconomic headwinds in Europe and China, Latin America is a region with steadfast domestic markets and attractively-valued companies that demonstrate significant growth potential.

Key Findings:

Government intervention and trading liquidity are the two greatest challenges Latin American companies face with respect to maintaining a fair market valuation, according to 38% and 28% of survey participants, respectively.

55% believe that an ADR program can help a Latin American issuer maintain a fair market valuation, citing the benefits of improved trading liquidity and free float as well as increased exposure to a greater number of potential new investors.

35% of investors surveyed recommend that Latin American companies that do not adhere to international reporting standards do so, as a means to maintain fair market valuation.

Data Snapshot: Brazilian Agriculture in Focus

Bailey McCann
Private Equity Strategies

Even though it now leads the worlds in many key agricultural areas, Brazil is still considered an emerging market in agriculture. Deal sizes remain relatively small and deals in the country are still somewhat new. The data we compiled with Preqin, the global leader in private equity data, examines some of these trends:

Largest Brazil-Focused Agriculture Funds Closed 2006 - December 2012 by Final Size

Fund	Type	Final Size (Mn)	Manager
Brookfield Brazil AgriLand Fund	Natural Resources	601 USD	Brookfield Asset Management
Brasil Agronegocio	Natural Resources	840 BRL	BRZ Investimentos
Pampa Capital Fund	Growth	365 USD	Pampa Capital
AMERRA Agri Opportunity Fund	Hybrid	277 USD	AMERRA

Notable PE-backed Buyout Food & Agriculture Deals in Brazil: 2006 - 2012 YTD (as at 17th December 2012)

Firm	Investment Type	Deal Date	Deal Size	Buyers
LeitBom	Buyout	Apr-08	260.60 USD	GP Investments, Laep Investments
BGK	Buyout	Apr-11	300.00 BRL	BR Partners
Globalbev	Growth Capital	Oct-11	50.00 BRL	Endurance Capital Partners
Frigorifico Mercosul	Growth Capital	Sep-06	21.50 USD	PineBridge Investments
Dall	Buyout	Sep-12	35.00 BRL	Darby Overseas Investments

Tools of the Trade: Service Providers Push For Communications and Reporting Standard in Private Equity

Bailey McCann
Private Equity Strategies

The way information, reporting and communications are exchanged throughout the alternatives investment landscape is outmoded and often cumbersome. This is especially true in private equity, where general partners are often making bespoke reports to give to their largest limited partners. The ILPA standards have had limited success in moving standardization forward, so far.

On the GP side there is support across firms and their vendors for movement to a unified standard. While there are communications guidelines, there is no active, enforceable or verifiable standard for GPs and LPs to follow today. All players including invested entities, administrators, co-investors and fund of funds would benefit from standardization, says Stuart Keeler, of eFront, one of the service providers working in this space.

He explains in an interview with Private Equity Strategies, that while progress has been made with the likes of ILPA and IPEV, the industry now needs to facilitate their implementation, and extend their scope. That requires the technology community to look for a way to make these guidelines and standardization best practice; otherwise, they risk remaining purely academic concepts.

“If you look back three or four years ago there was a lot of chatter about GPs increasing transparency, some of that happened but we need true standards,” Keeler says. “Most of the other areas of the financial industry are regulated and have viable information transfer not just recommendations but in practice.”

He advocates for a solution like the SWIFT system used in banking as a means of providing clear-cut communications and reporting between entities. Movement to a standard like SWIFT would allow GPs to comply with all of their LPs in the same way, saving the additional cost and time of individualized reporting on a per-LP basis.

“GPs are faced with doing ILPA reporting for some investors and customized reporting for others. It’s not that the industry isn’t trying, but investors need to come together and present a unified voice on what they expect,” he says.

Keeler says that when it comes to technology vendors like eFront, not only are they trying to be responsive, but also they have to stay ahead of new regulations in addition to creating bespoke solutions. As the basic compliance burden grows, firms can be distracted from their core mission or find themselves with significant and not entirely necessary cost outlays driven by being reactive instead of proactive.

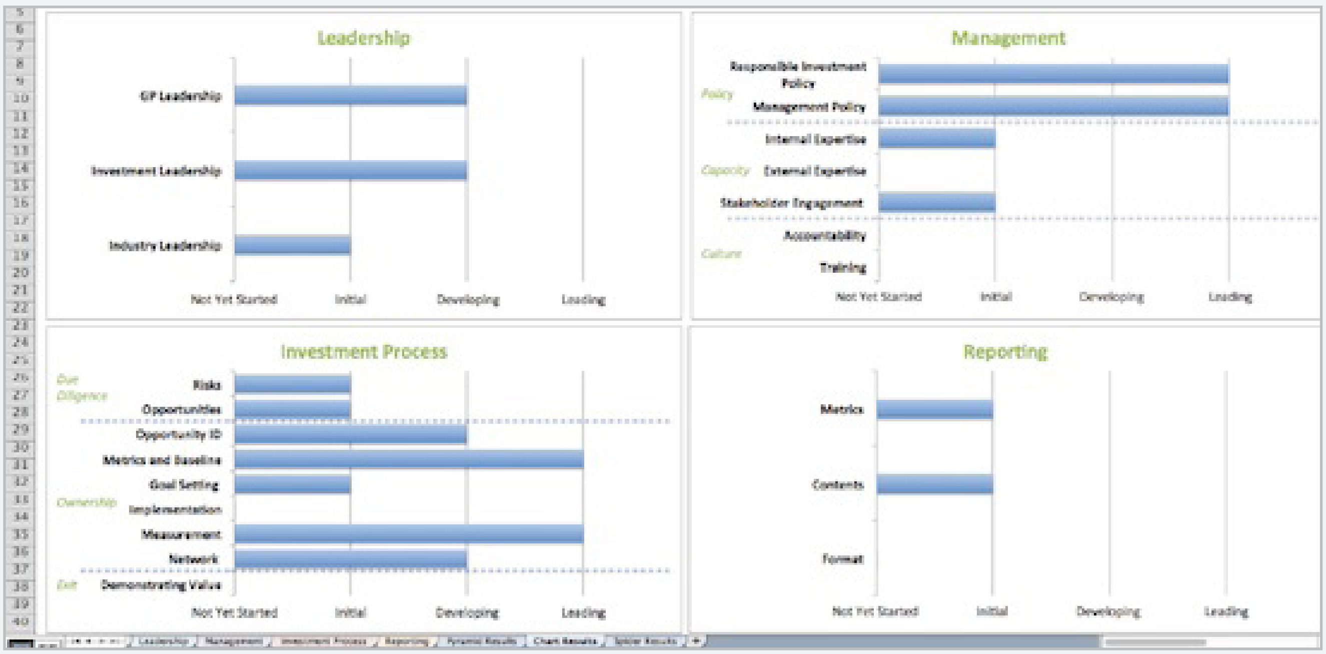
“The process is being controlled by large investors and they should outline how they want to get to the next level of efficiency. We saw this in securities trading with the shift from paper based trading to electronic trading.”

“We’re on the verge of the industry going to the next level,” Keeler says, noting that lessons may be drawn from the implementation of new OTC clearing standards or other successful standards like IFRS. “Large investors hold the key to transforming the existing approach for sharing information within this industry.”

Environmental Defense Fund Launches New Free Tool For Private Equity

The Environmental Defense Fund (EDF), in response to growing feedback from both private equity firms and institutional investors has launched a new free-to-download tool that will allow users to understand environmental impact and governance issues. According to the EDF, the tool is designed to define the building blocks of a successful ESG management program and provides private equity firms of all size is a framework to assess, analyze and improve their ESG performance.

The tool produces three outputs that can be used to evaluate a private equity firm's current ESG management practices and make plans for future improvements. In less than an hour, users can assess current performance across 22 best practices for ESG management from options including; not yet started, initial, developing and leading.



Quick Hits

Monroe Capital Launches National ESOP Lending Practice and Opens Atlanta Office, Monroe Capital LLC, focused on investments in middle market and lower-middle market companies, today announced Ty Dealy has joined the firm as a Managing Director to establish an Atlanta office and lead the firm's national ESOP lending effort.

SRS puts out an M&A Holiday Game, Structured as a fun and interactive game, SRS' 2012 holiday card lets itsrecipients try their hand at guessing the correct M&A deals involving VC/PEbacked companies that have been executed by various serial acquirers like Dell, Google, IBM, Microsoft and Oracle, among others. The goal is to guide each AcqMan avatar, which represent different strategic buyers, in collecting the startups that the acquirer actually bought and avoid buying the companies it did not.

Fortress Announces Successful Close of Fortress Japan Opportunity Fund II, Fortress Investment Group LLC announced the successful close of Fortress Japan Opportunity Fund II, at its cap of ¥130bn, or approximately $1.65 bn. FJOF II is a successor fund to the Fortress Japan Opportunity Domestic Fund, which closed in June 2010 at its cap of approximately $800m. actually bought and avoid buying the companies it did not.

Cortland Chosen to Administer Procida's 100 Mile Fund, Cortland will provide enhanced investor servicing and other back office support and services for the Englewood Cliffs, NJ based Real Estate Fund.

Cambridge Associates to Develop Asia Pacific Real Estate Performance Data in Collaboration With The Asia Pacific Real Estate Association (APREA), As part of the strategic partnership, APREA will give its members access to aggregate private real estate fund benchmark data and statistics based on the performance of managers in the Asia Pacific region.

OFS Energy pools ~$50m for buyout, Based on recent SEC filings, Texasbased OFS Energy Fund II has formed a holding company - RDT Holdco LLC in connection with buying 80% of a Texas drilling company - Rotary Drilling Tools LLC.

Delta House Project Approved; ArcLight to Provide Financing, LLOG Exploration Company, L.L.C., along with its Gulf of Mexico joint venture partner, Blackstone Energy Partners, and its coowners, Ridgewood Energy, ILX, Red Willow Offshore, LLC, Calypso Exploration, LLC, Deep Gulf Energy II, LLC, and Houston Energy have approved the Delta House Project. Private Equity Strategies reported on this transaction in the last issue, this approval represents the next phase in what will be a $2bn project that will include a floating production system an oil export line, a gas export line and a number of subsea systems, in the Gulf of Mexico region.

LR Global Expands South Asia Frontier Markets Operations, Names New President,
Reaz Islam, CEO of LR Global Bangladesh, in addition to his regional role, has been appointed as President of LR Global Lanka Asset Management Company (Pvt). LR Global also secured a $10m commitment from the IFC to launch the first private equity fund dedicated exclusively to invest in Sri Lanka.

Events

Private Equity Investing In Middle- Market Manufacturing Companies

February 28, 2012 - New York, NY
Hosted By: Capital Roundtable

Beyond Farming & Land -- Finding Profits Near the Table Private Equity Investing In Agribusiness Companies

January 10, 2012 - New York, NY
Hosted By: Capital Roundtable

Chaired By: Sebastian Popik,
Managing Partner
Aqua Capital

Best Practices for Launching & Managing a BDC

January 31, 2012 - New York, NY
Hosted By: Capital Roundtable

Chaired By: Robert Hamwee,
Managing Director
New Mountain Capital LLC

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