

OPALESQUE

PRIVATE EQUITY STRATEGIES

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Editors Letter

Welcome to the June issue of Private Equity Strategies. This issue we will be featuring some new market sector coverage along with a few recent updates from stories we've covered before.

In a new feature - MicroCap Monitor we are looking at DelMar Pharmaceuticals, which has been making the rounds following a recent IPO. The company is gaining the attention of both private equity and alternatives investors based on recent cancer treatment trials in the US and abroad.

In our Dealmakers Q&A we speak with StoneCapital Partners to learn about community bank investing, which may be some of the cleanest assets available in the market today. An update from the Russian Direct Investment Fund features a new fund launched with the Abu Dhabi Investment Company along with new interest in infrastructure.

In Regs watch we bring new you changes in regulation that may have a significant impact for private equity firms

In Movers and Shakers Evercore Partners raises its largest fund to date for investments in Mexico. And in The Next Generation we highlight a bit of a row happening in the UK between the British Venture Capital Association and local business schools on the impact of PE investments on employment.

As always in Quick Hits we bring you the latest fund news and events. I welcome your feedback and hope you enjoy the issue and the summer season. Please send me any updates, thoughts, tips or comments.

Best,
Bailey McCann
Editor

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MicroCap Monitor: DelMar Pharmaceuticals

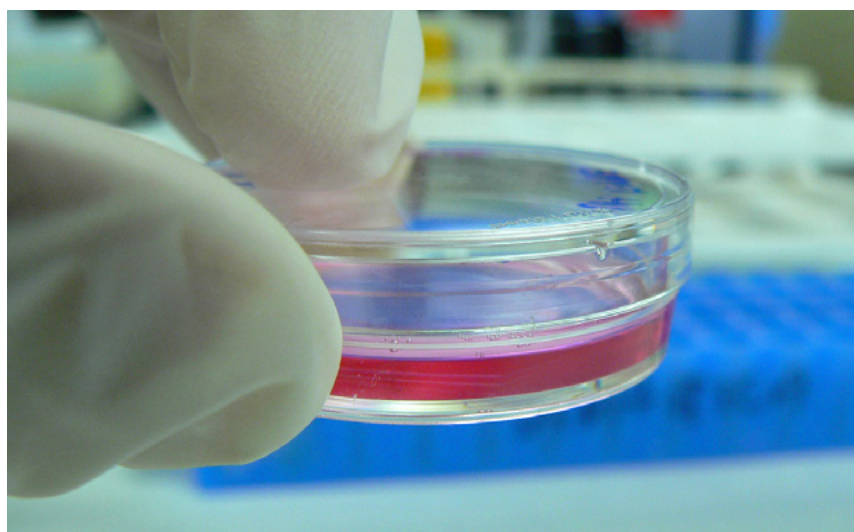
Highlights Continued Activity in Pharma at All Market Caps

Bailey McCann
Private Equity Strategies

Founded in 2010, DelMar Pharmaceuticals is focused on clinical and commercial stage development of cancer treatment drugs. The company, which recently went public, has been talking to investors highlighting their clinical successes and pipeline projects. Co-Founder and CEO Jeffery Bacha and CFO Scott Prail recently spoke with Private Equity Strategies at the Marcum MicroCap Conference.

"We took the company public through an RTO in January, and it was generally positive," explains Bacha. "Now we are focused on the trials and telling people our story."

Unlike other cancer treatment companies, DelMar focuses on patients with on patients with refractory glioblastoma multiforme (GBM), the most common type of aggressive brain cancer. Treatment of this cancer has had mixed success although some drugs are showing promise where standard treatments have failed. Through clinical work in both the US and China, the company has already been awarded an Orphan Drug Designation by US FDA & European EMA for VAL-083, one of its treatments for glioblastoma. The firm is working on clinical trials this year that look at the possibility of using higher doses of the drug in treatment for glioblastoma multiforme (GBM) and metastatic brain cancer for patients who have failed or are otherwise ineligible for currently approved treatments. This is big news for patients who are faced with a median survival of 4 ½ months from



diagnosis without treatment.

The team has been here before, they previously worked at another pharmaceutical firm, NCI on oncology treatments, and brought this knowledge to DelMar. The cancer treatment market as a segment of the broader pharmaceutical market is approximately \$78bn. So far, DelMar's story tracks with other companies in terms of successful IPOs, and positive shareholder value even through turbulent economic conditions.

According to a recent study of the [global health care market for private equity](#) by Bain Capital, deal value declined slightly in 2012, even while deal volume remained consistent. This indicator may point to broader interest in microcaps like DelMar. Interest from strategics is also on the rise making it harder for large private equity firms in the US and elsewhere to find deals and deploy capital efficiently.

The report shows that top returns in the health care market will likely come from "healthcare heavy" sectors, which reward risk taking and industry-specific expertise. 70% of the buyout deals done in this space in North America last year were done by small and midsize funds with some expertise in the field. "The implication: In order to unlock top-tier deal returns, funds are going to have to work harder and more creatively in North America to find assets, price them appropriately and create value post-close," the report says.

Based on a [recent analyst report](#) of DelMar, these market factors could be a boon for the company, as they aren't necessarily focused on acquisition. "We can control our own destiny," Bacha says. "We have the capital available to us now through our IPO so we can after product revenue and we aren't dependent on being acquired."

That said, he notes that even if they sell, the team will probably

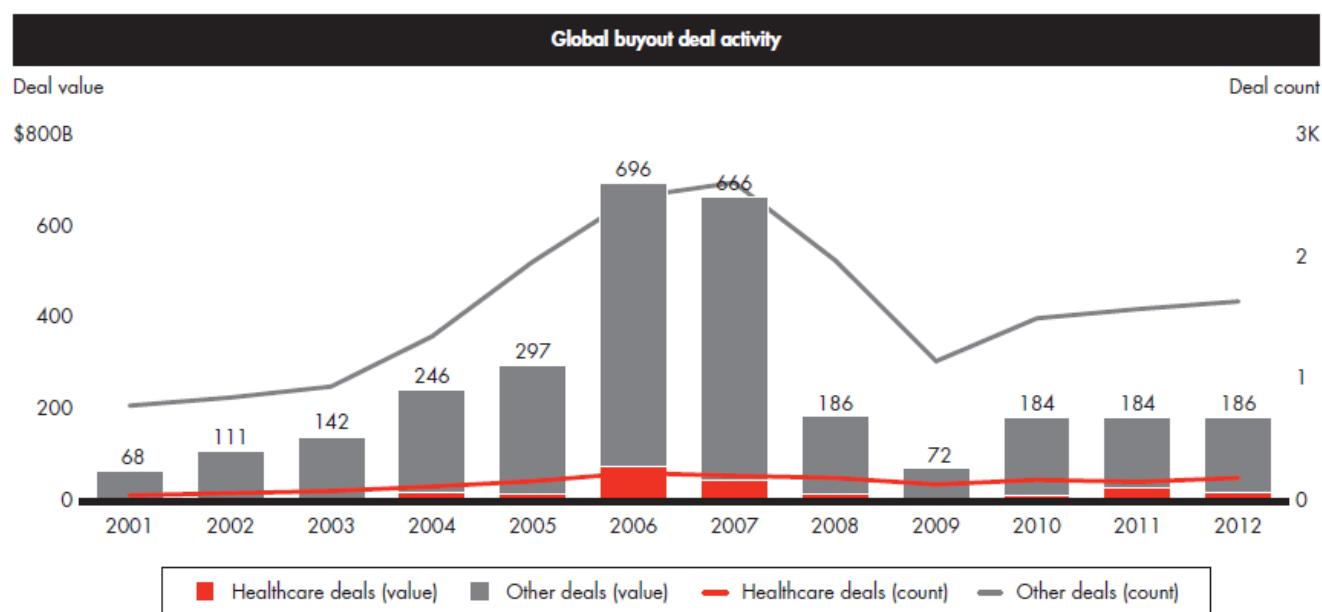
Pharma Funds:

- Celtic Pharma
- ESP Equity
- Advent International
- APAX
- Carlyle Group

look to repeat the process again around other products they already have in the pipeline. "The orphan disease market is more profitable than people think," he says. "It takes skill, but there are a variety of opportunities for investors and companies here."

*Figure Source: Bain Capital

Figure 1: Capital deployed in healthcare declines as overall private equity investment plateaus



Notes: Excludes add-ons, loan-to-own transactions and acquisitions of bankrupt assets; based on announcement date; includes announced deals that are completed or pending, with data subject to change; deal value does not account for deals with undisclosed values
Sources: Dealogic; Bain analysis

Figure 2: Top 10 healthcare private equity buyout deals announced in 2012

Target	Acquirer(s)	Sector	Country	Deal size
Par Pharmaceutical	TPG	Biopharma and related services	US	\$2.2B
BSN medical	EQT Partners	Medtech and related services	Germany	\$1.6B
Mediq	Advent International	Provider and services	Netherlands	\$1.4B
Four Seasons Health Care	Terra Firma	Provider and services	UK	\$1.3B
Heartland Dental Care	Teachers' Private Capital	Provider and services	US	\$1.3B
Thomson Reuters healthcare business	Veritas Capital	Provider and services	US	\$1.3B
M*Modal	One Equity Partners	Provider and services	US	\$1.1B
CHG Healthcare Services	Leonard Green & Partners, Ares Management	Provider and services	US	~\$1.0B
Mercury Pharma	Cinven	Biopharma and related services	UK	\$0.7B
Aenova Group	BC Partners	Biopharma and related services	Germany	\$0.7B
Total				~\$12.6B

Dealmakers Q&A: StoneCastle Partners Eye Community Banks

By: Bailey McCann
Private Equity Strategies

After 2008, the last place many investors would consider investing are banks. However, according to StoneCastle Partners, a New York-based asset management firm, the community banks that made it through the crisis, may well represent some of the cleanest assets in the market today.

“As a pet project in the late 1990s, I put together a white paper looking at community bank failures. According to that data, community banks failed less than anyone believed but there is a cognitive bias. The worst year in history for community bank failures was 2010, when the rate was 2%, so I thought either I was crazy or there was an opportunity here,” explains Joshua Siegel, managing principal of StoneCastle Partners, in an interview with Private Equity Strategies.

Siegel took his data to ratings agencies like Fitch and had them verify his findings. Once they did, he started looking more into investments in community banks and founded StoneCastle in 2003. The firm currently manages approximately \$5.1bn in assets.

“Community banks on average are about \$300m in size and only make about \$3m in profits off that. So there is barely a middle market. The investment community at large really doesn’t understand this space, and thinks they are very high risk, which is great for me and a few others that do invest in them,” he says.

Community banks overall have seen a bit of consolidation, there were approximately 14,000 community banks in the US in the 1970s. That number dropped to 9,000 by the 1990s and now sits just over 6,000. Of that 6,000+ only about 500 are publically traded and the remainder are privately held. Some observers attribute that to acquisition by large banks and bank failures, but one of the key drivers is age.

“The average senior staff of a community bank is 60 or older, the average age of the board of directors is 70 plus. Not many people are running back to Kansas to run the bank, so if they don’t have a succession plan in place, they are going to want to sell out,” Siegel says. “A lot of that is that its just not as much fun to run a bank, you used to be a leader in the community. Now there are regulatory costs, in the US and internationally, Basel III, for example may have implications for community banks too. The Consumer Financial Protection Bearu is making it very hard to lend to consumers, and capital raising within the community is much harder.”

Merger accounting is also getting tricky for small banks. Siegel explains that through purchase accounting, banks now have to price at fair market value, which can have an effect on how banks look before and after a merger even if they are healthy.

There is also the possibility that the largest banks dump credit, and offer high savings rates to get community banks out of the market and then go back to business as usual. “It would take very little effort for the top five or ten money center banks to do this, and there’s nothing legally to stop them, it’s more of an ethical question. There would be a huge uproar if they did it and it should be watched. Thankfully Congress and regulators are very aware of this risk and are making efforts to support community banks.”

Even with those headwinds, Siegel says, community banks will always have a place in large part because they make the bulk of US small business loans and other loans the economy needs to function.

"With the regulations as they are, big banks like Bank of America, simply can't afford to make small farm loans anymore. Since 1980 the dollar has increased 2.8 times, while the largest banks have grown 20 times. There's only so much more growth they can get and it's not going to be in small ticket loans."

He notes that the technology consumers have come to expect from big banks like remote deposits, branchless banking, and slick online portals is also coming down in cost to deploy. Community banks are likely to embrace that technology as a value add instead of a trade off for personal service the way big banks have.

"We support strong banks that want to acquire the tired. That's how the community bank sector is going to grow and take market share. They can afford to do it, and there is no replacement for the services they offer. When we approach banks, management, market, balance sheet have to be in place - in that order. Management matters most. We look at whether they are invested in their community, do they have good credit, if they are involved in local organizations. It's really a local disgrace issue, if they head of the bank is involved in the community he's not going to want to go to church and explain how he lost money in derivatives."

Geography is also a factor. "You can have a fortress balance sheet, but if the community risk is too high, say everyone is employed at the one plant in town that's a red flag. I might still be interested depending on capital, liquidity, and emerging factors in that economy," he says.

Siegel believes the US may see more consolidation of community banks over the next 3-10 years driven by the factors outlined above and that the opportunity set is nationwide. StoneCastle has made investments in 49 states so far. "We still have three banks that have been around since the war of 1812. Many banks are over 70 years old. They're boring, sure, but 59% of the loans to small businesses and local economies come from community banks they build businesses. That's what keeps me coming back to work every day."

Who Said That?

"I never would have guessed that private equity a critical role in meeting the aspirations of the two billion people still in poverty today," - Jim Yong Kim President of the World Bank Group at a recent EMPEA conference .

The comment, and a note that Kim had changed his opinion overall on private equity was first reported in Finance Asia.

Update: The Russian Direct Investment Fund Launches New Fund

By: Bailey McCann,
Private Equity Strategies

In February we spoke with Sean Glodek, Director, Russian Direct Investment Fund (RDIF) on the success of the MICEX IPO. Which created Moscow's first publically traded exchange. Now is out with more news and a new fund launch.

RDIF and Mubadala Development Company (Mubadala), the Abu Dhabi-based investment and development company are joining on a \$2bn co-investment fund to pursue opportunities in Russia. The agreement was announced at the St. Petersburg International Economic Forum 2013 by CEO of RDIF Kirill Dmitriev and CEO of Mubadala Khaldoon Al Mubarak.

The fund will predominantly focus on long-term investment opportunities across a range of industry sectors, acting as a catalyst for direct investment in Russia. The announcement is aligned with Mubadala's plans to establish a strong presence in key international markets.

Mubadala and RDIF are each committing \$1bn. The majority of Mubadala's commitment will be deployed in opportunities that will be evaluated on a deal-by-deal basis while some of the capital will be invested as an automatic co-investment into RDIF deals.

Some early indications of what the new fund may look at were also offered at the event. Dmitriev, who is also Chairman of the B20 Taskforce on Investment and Infrastructure, finalized recommendations on infrastructure investments in the country and had this to say on those opportunities - "the key objective of our recommendations is to create the optimal conditions for global economic growth by promoting investment, especially in infrastructure. Approximately \$60 trillion of global investments into infrastructure will be required in the run up to 2030. This represents more than the value of all the existing infrastructure today. The introduction of international best practices in infrastructure development would save up to \$1 trillion per year, enabling world GDP to grow by at least 3% if these savings were re-invested."

Those recommendations are focused on improving the quality and return of infrastructure investments as well as making it easier to invest in infrastructure. The B20 will be included in broader discussions of global infrastructure investment at the G20 meetings.

RFID made two additional announcements today of memoranda of understanding with General Electric (GE) and OJSC Russian Grids to expand electrical and power grid capabilities within the country. RFID hopes to work with OJSC Russian Grids to attract investment into the Russian power industry and will work with GE on providing cogeneration power to the commercial sectors of Russia's economy.

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

A s 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.

Congress May Agree That PE Doesn't Pose Systemic Risk

An editorial in [The Hill](#) suggests that Congress may not view private equity as a systemic risk to the broader economy in the same way that it does banks.

10 Ways PE Changed Post Recession

A new podcast from the Carlyle Group discusses how private equity and regulation has changed the industry since 2008. A written excerpt of the podcast is available [here](#).

Africa's Second Largest Law Firm ENS Publishes Private Equity Review

Attorneys [offer a brief run down](#) of the landscape of private equity on the continent along with new legal changes.

Reverse Mortgage Private Equity Faces New Scrutiny From States

State legislatures are taking [a harder look](#) at reverse mortgages and private equity firms involved in the space amid concerns that consumers may not fully understand what a reverse mortgage is when they agree. States are also concerned about new activity in the space overall and are looking to get a better handle on what firms are involved.

Sun Life-Guggenheim Deal Held Up on State Led Risk Probe

New York State is [taking a closer look](#) at the Sun Life-Guggenheim Deal to make sure that the investment isn't too risky and short term.

PE, Audit Bills Make It Through The House

The House Financial Services Committee has [approved two bills](#) that look at private equity and auditing. They now move on to the Senate.

PEGCC Snags Emerson from TIAA-CREF

Private Equity Growth Capital Council has hired Langston Emerson as vice president of government affairs. He comes to the job from TIAA-CREF, where he was senior director of federal government relations.

Asian Pensions Take A Closer Look at PE

More Asian pension funds are [eying private equity investments](#) or are looking to increase allocations despite tight controls on their activity.

US May Double Leverage Standards For Largest Banks

The US [may double capital requirements](#) for the nation's largest banks. The move would likely force them to halt dividend payment to investors and tighten lending practices even more. If the measure goes forward, PE firms may find new opportunities in private lending.

Massachusetts Sees Another PE Candidate

Former Advent International executive Gabriel Gomez is running for an open Massachusetts Senate seat against Democrat and incumbent Senator Ed Markey who is the favorite to win. This represents the second PE candidate Massachusetts has put on the ballot and BloombergBusinessweek notes that Gomez is doing all he can to avoid the specter of Mitt Romney.

Other PE candidates currently on ballots include: ormer GTCR Chairman Bruce Rauner is running for governor of Illinois, and former Gores Group senior executive Scott Honour for governor of Minnesota. The article notes that so far, all have been compared to Romney. Read our previous discussion of his impact on PE [here](#).

NZ Superannuation Fund Gets Out of Nukes, Back Into Cluster Munitions

New Zealand Superannuation Fund has excluded seven companies with operations in nuclear bases from its portfolio. And is allowing four back in that had previously been excluded for working on cluster bombs. The excluded companies are Babcock & Wilcox, Bechtel Group, Fluor Corp, Huntington Ingalls Industries, Jacobs Engineering Group, Serco Group and URS Corp. The Fund has an overall portfolio of \$NZ22bn. General Dynamics, L-3 Communications, Raytheon and Goodrich Group were all allowed back in after they stopped making cluster bombs.

Movers and Shakers: Evercore Partners Raises Second and Largest Ever Fund

By: Bailey McCann
Private Equity Strategies

Evercore Mexico Capital Partners, private equity investor in Mexico and the Mexican private equity business of investment banking firm Evercore Partners, has completed fundraising for Evercore Mexico Capital Partners III (EMCP III), raising \$201m, its largest fund ever. EMCP III, which was oversubscribed, will focus on making minority investments in high-growth, family-owned and privately held Mexican companies and working with these companies' management teams to generate additional value.

EMCP III plans to invest \$15m - \$30m per investment opportunity, taking minority stakes of 16-20% in portfolio companies although sources familiar with the fund say they are open to majority positions. The fund includes a wide variety of institutional investors and family offices, many of which are located in Mexico but also include investors in the US and EU. Approximately 40% of EMCP III is composed of limited partners that invested in Evercore Mexico Capital Partners II.

Evercore's portfolio previously included investments in Volaris, the second largest airline in Mexico; Lipu, the largest school and employee transportation company in Mexico; More Pharma, a Mexican specialty pharma company; Grupo Axo a brand management company and Servicios Corporativos Javer, the largest private housing developer in Mexico.

The EMCP III Fund has already made new investments in three more companies - Intellego, Diavaz DEP and Grupo Casanueva Pérez. Sources familiar with the fund say that companies targeted by the firm have in general an EBIDTA of \$16bn, and that the fund is interested in portfolio companies across all sectors of the Mexican economy, including those that have not previously had private equity investment.

"EMCP III aims to capitalize on a highly attractive and stable Mexican macroeconomic environment," said Alfredo Castellanos, EMCP Managing Director and EMCP Investment Committee Member. "The growing demand for products and services of a rapidly growing middle class coupled with Mexican companies in the process of modernization should present attractive investment opportunities."



The Next Generation: Academic Study Shows Lack of Transparency by GPs Harms Performance

By: Bailey McCann
Private Equity Strategies

In our Next Generation series we focus on new academic work and programs focused on private equity around the world. A new study released by Geoffrey Wood, of Warwick Business School, Marc Goergen, of Cardiff University, and Noel O'Sullivan, of Loughborough University, have discovered that private equity buyouts may be harming the overall performance of the companies included in the transaction.

According to the data, when they compared 105 publicly-listed firms that went through a buy-out between 1997 and 2006 to a control group of their industry rivals they fell further behind after the takeover. The study found that four years after the buy-out the performance gap between the two groups had tripled, from GBP29,000 - as measured by turnover per employee - to GBP89,000.

This was coupled with 59% of the private equity IBO firms reducing the size of their workforce in the first year compared to 32% in the control group.

The British Venture Capital Association has responded to the report, saying that its focus exclusively on the employment consequences of institutional buyouts (IBOs), makes the conclusions partial and oversimplified. "Rather than ensuring that the report overcomes the difficulties of recognizing the heterogeneity of private equity investment and providing "greater empirical clarity" to the issue, this simply means that the report is a partial and unrepresentative look at private equity. The study concerns itself with a very small subsection of private equity deals and therefore any claims that this represents the private equity industry as a whole are erroneous," the association wrote in a statement.

They went on to say, "it appears that the authors have begged the question - they have started with the hypothesis that private equity is damaging to employment, wages and productivity, and sought to examine only those deals which they believe are most likely to prove this hypothesis."

The association also takes issue with the time frame of examination which is four years, as most private equity investments last five to seven years. However, that note by the association may have the unintended effect of supporting the assertions of the paper, by implying that private equity investment requires at a minimum four years of growing pains before improvements can be seen.

Professor Geoffrey Wood responded: "The drop in our sample is a reflection of the secretiveness of the private equity industry and the difficulty of tracing target firms after their acquisition. We have made a colossal effort to trace firms after their acquisition, but in some cases a lack of disclosure, often combined with a move of the target firm's headquarters to tax havens such as Nassau or Luxembourg, has prevented us from obtaining data post-acquisition. The cynic would state that some private equity houses make a huge effort to hide their target firms within a chain of shell companies. We encourage the BVCA to improve disclosure by the industry so that studies such as ours can be more representative.

"We do not claim that our study is representative of the whole private equity industry; the focus of our study is on institutional buy-outs (IBOs). IBOs are acquisitions by private equity houses of publicly quoted UK companies. Hence, contrary to some of the existing studies we do not include relatively small, unquoted private companies. Some of the companies covered by our study include Debenhams, Pizza Express and United Biscuits."

The professor also noted that the study is specifically focused on institutional buyouts and specifically sought to avoid inclusion of other types of buyouts, such as management buyouts rather than confuse the data set. He also said that the drop in unemployment took into account the fact that companies targeted for a buyout were likely already underperforming thus accounting for any employment drop.

Update: Drones In The Portfolio:

Last issue we included a video and interview with artist, writer and futurist James Bridle about his work Drone Shadows. Previously Drone Shadows were only available to interested viewers outside of the US, now a Drone Shadow is present in the nation's capital, along with an exhibition at DC's Corcoran Gallery of Art. The shadow is outside the museum, just one block from the White House. Bridle has also created [Dronestagram](#), an Instagram feed of pictures of drone strikes.



Quick Hits

Apax Partners has raised \$7.5bn in a new fund focused on European buy-outs. The fund is called Apax VIII. The fund told investors just ten months ago it was halfway to its goal making for a quick fundraising cycle.

According to a Reuters report, Warburg Pincus is buying minority stakes in several European banks in an effort to get them to let the firm invest more in the sector.

Rockwood Holdings Inc has canceled a combined auction of its titanium dioxide and performance additives units due to a lack of offers for the units.

Accel-KKR a technology-focused private equity investment firm, has made a growth equity investment in Zinc Ahead, the world's leading provider of marketing compliance solutions for the life sciences industry. Terms of the investment were not disclosed.

CVC Capital Partners Ltd. finished gaining Eur7 billion after only six months of gathering investors, beating rivals including Apax Partners.

KKR-owned healthcare business, Genesis Care, has launched a refinancing and is seeking US\$245m through a first-lien, senior secured Term Loan B issue, and another 30m Australian dollars (US\$27.8m) through a revolving credit facility.

Monroe Capital, has provided a \$35 million unitranche credit facility to Accutest Laboratories in connection with supporting its growth by Bolder Capital LLC.

Michael Forman, Chief Executive Officer of Franklin Square Capital Partners Advisor, was awarded regional winner of the Ernst & Young Entrepreneur of the Year® 2013 Award in Greater Philadelphia. Private Equity Strategies previously spoke with Forman to learn about Franklin Square Capital and BDCs for our [April issue](#).

About the Editor: Bailey McCann is a reporter and analyst based in the US, with experience covering government, policy and regulatory issues in addition to her coverage of alternative investments. Prior to her work with Opalesque, she provided research and media intelligence for members of Congressional and White House offices, government contractors, and Fortune 500 companies. She has also reported on, and done policy analysis of state and local government issues. She may be reached directly at mccann@opalesque.com

Events

Private Equity Investing In Middle-Market Restaurant Companies Chaired By Stephen C. Sherrill, Bruckmann Rosser Sherrill & Co. LLC

June 27, 2013 New York, NY
Hosted By: Capital Roundtable

Private Equity Investing In Defense, Government Services, & Aviation Companies -- More & More Acquisition Opportunities In a Dynamic Growing Marketplace

July 18, 2013 New York, NY
Hosted By: Capital Roundtable

Private Equity Investing In For-Profit Education Companies

July 25, 2013- New York, NY
Hosted By: Capital Roundtable



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