

Footnotes

Understanding Private Equity and Its Major Role in the Economy

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In 2007, \$431 billion came out of the public stock markets and the appetite for public companies going private has never been stronger. During the year, 926 companies were removed from the New York Stock Exchange, the AMEX and the NASDAQ. Locally, First Data Corporation was acquired by KKR, a well-known player in private equity. The cost associated with government regulation, particularly Sarbanes-Oxley, has thrown gas on the fire. It's estimated that a minimum of 3% of GDP growth is driven annually by private equity. Historically, institutional investors and family offices were the only participants in this market, but private equity investing has attracted interest from the media and smaller investors.

Private equity firms focus on maximizing the value of the companies that they acquire. Strengthening management, adding or spinning off business lines, and leveraging distribution sources are strategies that these buy-out firms utilize. Private companies also do not need to focus on quarter-to-quarter earnings that are Wall Street's obsession. Companies can be long-term focused and stay away from the public spot light.

Although private companies have an element of correlation with the public markets driven by the commonalities of business economics, they are a distinct opportunity that is not represented in other investment vehicles. Warren Buffet recognizes this fact and last year added three private stocks to his Berkshire Hathaway Portfolio: Pacific Corp., Business Wire, and Applied Underwriters.

Private equity professionals are typically heavily incentivized to succeed, and investors have the potential to make sizable returns over time. However, randomly selecting "opportunities" does not ensure success. We believe that manager selection is critical. Management's judgment is crucial in selecting opportunities and in maximizing a company's value through expertise and experience.

Single-manager funds typically have life spans of five to 10 years. Management fees tend to be around 2% per year, plus usually 20% of the profits, as well. Diversification is crucial. Although a single fund usually invests in a handful of companies, its holdings are often concentrated in a particular region, stage, or sector.

While it is wise to consider multiple funds, the minimum investment level to obtain proper diversification can be significant. An alternative is to consider a multi-manager fund, which should offer exposure to a variety of sectors, geographies, and vintages. Private equity funds typically experience flat to

DID YOU KNOW...

- The Annual Golf Tournament will be held on May 16, 2008 at Riverdale Dunes in Adams County.
- CGFOA has a lending library—see page 4 for details.
- The National GFOA Conference will be held in Fort Lauderdale, Florida from June 15—18, 2008, and there will be a Colorado Delegate breakfast on Tuesday, June 17 at the Renaissance Fort Lauderdale.

Private Equity *(Continued from page 2)*

down performance in the early years called the J-Curve effect. A fund-of-funds (another name for multi-manager funds) reduces the J-Curve profile. Although fund-of-funds have an extra layer of expenses, many investors find the diversification benefits to be well worth the additional costs. A negative factor is that fund-of-fund's managers often may not have access to the top private deals, particularly when private equity investment capital is abundant.

An emerging opportunity is investing in the listed stocks of companies that invest in private equity. These publicly traded private equity companies invest in private equity in the same fashion as a limited partnership. These listed companies include well-known private equity investors such as Fortress, Blackstone, Capital Source, and KKR to name a few. Red Rocks Capital, a Colorado-based money manger, has developed a Listed Private Equity Index that includes 30 U.S. companies with direct investments in over 1000 private businesses. The Powershares Listed Private Equity Portfolio is an exchange-traded fund (etf) on the AMEX that seeks of replicate the Red Rocks index. Additionally, Red Rocks Capital, recently started actively managing, a mutual fund that invests in listed private equity companies worldwide. Listed private equity mutual funds and etfs offer not only exposure to the private equity opportunity set, but diversification, daily liquidity, low investment minimums, stringent reporting requirements, and transparency. Some investors believe the downside is the liquidity. The stocks of publicly traded private equity firms are volatile and normally trade at a 30% discount to the underlying investments' estimated net asset value.

Private equity investing is not for the faint of heart. However, for patient, long-term investors, private equity investing can offer quality diversification benefits and an interesting experience that may generate significant returns.

CML Municipal Finance Listserv CGFOA Finance Listserv

CGFOA is thrilled that the Colorado Municipal League Listserv for municipal finance officers is up and running. This list is designed to facilitate communication among municipal finance directors, managers, administrators, clerks or whomever may handle finance administration and management functions for their municipality.

Essentially, the objective of the Listserv is to create an opportunity to learn from each other and provide a forum for sharing ideas, efforts, policies and experiences. Using the Listserv is easy....any Listserv subscriber can raise a question or provide information, which then is automatically e-mailed to all the members of the group. Any and all responses from other members of the group are also e-mailed to all members. The Listserv and online sign up form are on the CML website - look for the link to the Municipal Finance Officers Listserv sign up form.

CGFOA also hosts a Finance Listserv. Registration for the CGFOA list is located in the Members Only section or you may subscribe to the Finance Officers Listserv by clicking on this link: CGFOAListserve@cgfoa.org Just type the word subscribe in the subject line and send the email. Once registered, you may send an email to everyone else on the list by simply addressing your email to: FinOff@cgfoa.org . Just like the CML Listserv, the CGFOA Listserv creates an opportunity to ask questions, learn from each other and provides a forum for sharing ideas, efforts, policies and experiences.

To be removed from the CGFOA Finance Listserv, please send an email to administrator@cgfoa.org with Unsubscribe in the subject line.

Feel free to register for both lists; if you are not a municipal finance officer you will find good value in being on the CGFOA Finance Listserv.