Key Factors for a Successful Private Equity Fund: People, Strategy, Market, Product

April, 2005
Zurich
3 Major Success Factors

PEOPLE

"Keep up the good work, whatever it is, wherever you are."

"No, the computers are up. We're down."
## Right mix and evolution of skills

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<th>First Fund</th>
<th>Second Fund</th>
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<td>Big Four Alumni</td>
<td>I-Banking Skills</td>
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<td>I-Banking Skills</td>
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Right mix of levels in the organization

IB/Consulting Structures

PE organizational charts

- Partners / Senior Professionals
- Investment Officers / Junior Professionals
- Interns

“Say! When did I start reporting to my computer terminal?”
Right motivation

PE compensation approach

- Cash Compensations
  Higher than Big 4 but can’t compete with IB Sector

- Bonuses
  Less dependent on year end result

- Carried Interest
  Carry early on as Russia use to be a short term planning country
Right cultural mix

Russian and International experience is a core sales message

- Russian Language and Experience
  
  Russian speaking PE team as a must, Russian business experience for expats as a plus

- International Exposure
  
  International experienced team with proven contacts and success stories is a part of Fund’s success

“We are all of the same opinion, Ms. Beckett. What’s more, we look like America.”
Capital nature and team skills are major strategy drivers

Expansion Capital Teams:
- entrepreneur driven
- Russian/Western know-how as well as networking opportunities
- Mostly sponsored by International Private and Institutional Investors
- Lower risk expectations/higher entry multiples

Venture Capital Teams:
- venture/entrepreneur driver
- Russian/Western know-how
- Capitalize on exits to Western VC markets/western strategists to step into Russian market
- Extremely high risks and rewards expectations

Turnarounds Teams:
- Industry specialization and know how as a must
- Merge and consolidation play
- Mostly sponsored by Russian Private Investors
- Lowest entry multiples/average risk returns assuming local know how in place
Adding value is a key

Your strategy in Private Equity depends on your view of the Value Creation Process

Corbett:
“No, Hoskins, you’re not going to do it just because I’m telling you to do it. You’re going to do it because you believe in it.”
Changing sources of return

% of total return

100%


Sales/margin growth

Multiple expansion

Financial leverage

• Future development?
• PE investors role?

Source: General Partner Survey, Asset Alternatives
Non-monetary contribution

Deal sourcing in our part of the market is to a large extent dependent on the ability to present the non-monetary part of PE to entrepreneurs who are relatively new to the concept of PE.

To be convincing an entrepreneur may involve:

- General coaching
- Corporate transformation
- Networking
- Decision making process

- An investor base with relevant & accessible skills
- Hands-on experience in building and managing businesses in Russia
- References among peers. Happy entrepreneurs in the portfolio who can vouch for you.
Russian market analysis – another strategy driver

**Deal Size Analysis**
- Lots of small projects (<5 Mio USD)
- Enough mid-sized deals (5-15 Mio USD)
- Lack of large transactions (>20 Mio USD)

**Deal Type Analysis**
- Lots of Pre IPO deal: but expensive and difficult to get in
- Many mid-sized deals: but needs proprietary deal flow and balanced portfolio approach
- Cheap distressed assets: most of them targeted by private Russian capital
- Post privatization buy-outs: not attractive until substantial leverage available
- LBO/LBI: interesting but lack of teams and little leverage available

- **Best Strategy mainly based on your team’s core skills and fund’s capital nature**

“Where do you want us to start, Chief? Our expansion plans or our bankruptcy plans?”
New products to emerge in a bigger scale

Expansion Capital

Turnarounds/Consolidation

Venture Capital

LBO/MBO

Western Money

Russian Money

> 40% IRR

> 60% IRR
Hedge schemes are welcomed

Hedge your downside and be open for upside as much as possible

- Ratchet Mechanisms
- Convertible structures
- English law and investor’s protection rights
Although the major success factor....

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