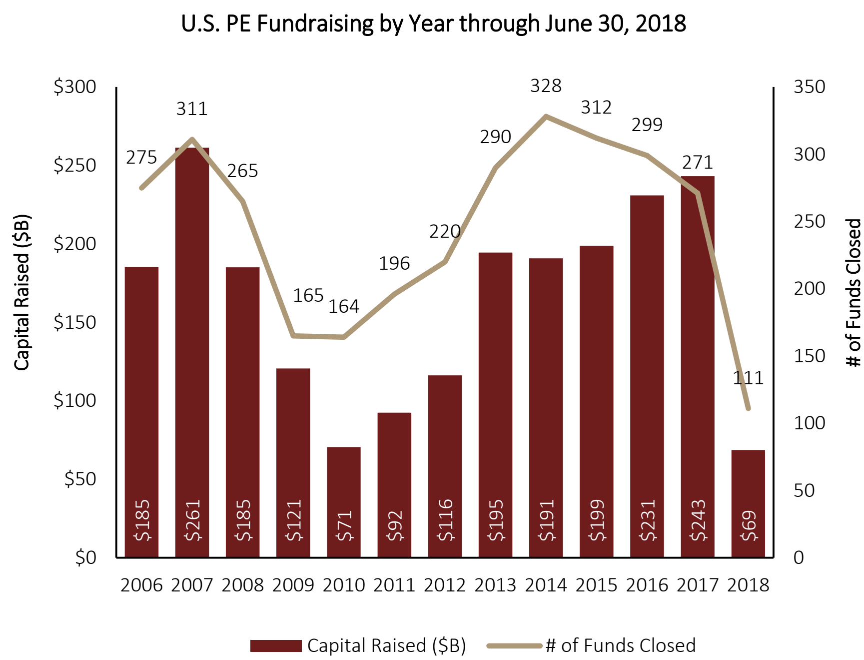
The first half of 2018 presented a contrast between strong economic and corporate earnings growth, and lackluster and increasingly volatile public market trading. Political uncertainty in the U.S., specifically regarding the impact of potential trade tariffs, was one culprit, although the future impact of the Fed's continued tightening of monetary policy and resulting rise in interest rates also concerned investors. At the same time, M&A and stock buyback activity was robust, likely a result of the tax law changes that went into effect in January 2018. In fact, current M&A volume is on a record-breaking pace, fueled largely by mega-sized corporate transactions. From a venture capital and private equity perspective, general market conditions discussed in past market reviews have persisted; limited partner demand for venture capital and private equity funds remained strong, while elevated valuation levels were observed across nearly all private markets.

Private Equity

Private equity fundraising in 1H 2018, while strong by historical standards, was down in comparison to record-breaking 2017 levels. According to Pitchbook, 111 U.S. private equity funds raised $69 billion during the first half of the year, compared with 204 funds that raised $181 billion during 1H 2017. In spite of this year-over-year decline, many limited partners have continued to increase private equity allocations and are still committing capital at historic levels given expectations for future long-term outperformance versus the public markets and other alternative asset classes. Abbott, on behalf of its clients, has committed nearly $500 million to 10 primary buyout and special situations funds through August 2018. Approximately 32% of those commitments were to four small buyout funds, 47% to three North American buyout funds, and 21% to two European buyout funds. Commitment activity during the second half of the year is likely to drop slightly due to the timing of several attractive investment opportunities in the first half of the year.



Source: Pitchbook

Private equity-led transaction activity remained strong during 1H 2018 driven by record amounts of dry powder and easily accessible debt financing, and is expected to continue to be robust in the second half of the year for the same reasons. According to Pitchbook, median deal size for 1H 2018 increased 31% over full-year 2017 primarily due to growing fund sizes and higher purchase price multiples. This interest in larger deals is driving an increase in take-private transactions as well as corporate carve-outs. It is also driving an increase in buy-and-build strategies as M&A enables managers to deploy larger amounts of capital into both new and existing investments. M&A, specifically platform add-ons, has the added benefit of enabling a sponsor to average down what are historically high entry multiples. High purchase price multiples are influenced by available liquidity in the market, but also by the industry's increasing interest in higher growth technology investments, software in particular. With multiple expansion potential muted in a high-price environment, a focus on multiple levers of growth are key drivers of returns. Fortunately, these same traits should also help to mitigate the impact of a potential downturn on a sponsor's portfolio when the cycle turns.

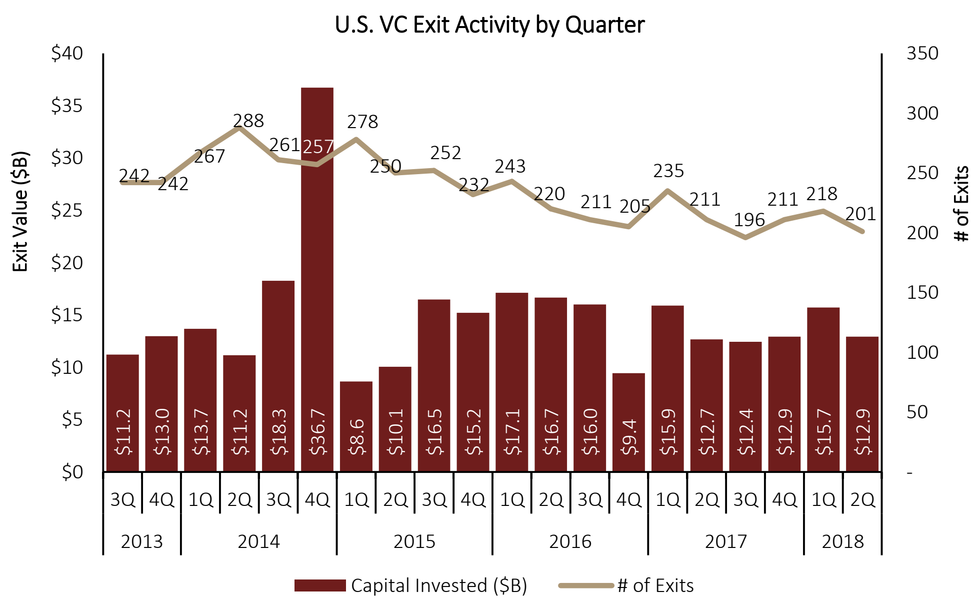
In spite of increasing deal sizes, the number of private equity exits in 1H 2018 was down slightly year-over-year. In general, exit markets remain strong with secondary buyouts, IPOs, and corporate acquisitions presenting clear paths to liquidity for private equity sponsors. We expect these trends to continue into 2H 2018 absent a material change to the economic or financial markets.

Venture Capital and Growth Equity

Although venture capital and growth equity fundraising got off to a slow start in 2018, a sharp increase during the second quarter put year-to-date capital raised on a similar pace to that of 2017. According to the NVCA, 157 venture capital funds raised $20.2 billion during the first six months of 2018, slightly exceeding 2017 levels when 119 venture capital funds raised $19.1 billion. Thus far, micro trends during 1H 2018 appear to be in line with 2017; such trends include strong first-time fundraising activity and a decrease in the number of mega-funds (funds greater than $1 billion in size) raised. As of June 30, 2018, first-time funds are on track to exceed 2017 first-time fundraising activity, with 26 funds raising $1.8 billion compared to $1.5 billion raised across 15 funds during the same period last year. The number of mega-funds raised in 2018 is on par with the number raised during 1H 2017, however, we expect fundraising in this segment to increase throughout 2H 2018 as seven mega-funds are projected to raise capital. Through August 2018, Abbott has committed roughly $180 million to seven venture capital and growth equity managers.

Sustained fundraising momentum and companies opting to remain private longer have continued to fuel a robust investment environment. 2018 is on pace for yet another record year with more capital invested in a six-month timeframe than seen in any other six-month timeframe in the last decade. According to the NVCA, venture capital and growth equity investors deployed $57.5 billion in 3,997 deals including $11.8 billion into 42 "unicorns," or private companies with post-money valuations over $1 billion; investments in "unicorns" have accounted for 20% of total dollars invested since 2015. However, in a break from previous years, it is not only unicorns that are driving investment activity, as companies at every stage are, on average, raising larger financing rounds. Angel and seed deal sizes are at a decade-high level, with a median size of $830,000 and $2.1 million, respectively. Similarly, early-stage investing rose for the seventh straight quarter, reaching $10.5 billion in Q2 2018, compared to $6.8 billion during Q2 2017.

According to NVCA, exit activity is on pace to match 2017 levels; 419 venture-backed companies were exited for a total deal value of $28.7 billion. What we believe to be the most impactful news for venture investors is that the IPO market showed signs of awakening for venture-backed companies, with eight of the 10 IPOs in the second quarter being "unicorns." While pharma & biotech companies have comprised the majority of IPOs recently, information technology companies, in particular enterprise software companies, have been the largest IPOs in 2018. Two of the largest IPOs of the quarter included DocuSign ($466 million) and PluralSight ($311 million), both of which are trading above their IPO price. At the same time, the M&A market for venture-backed companies during the first half of the year remained relatively flat year-over-year, with 297 exits with a total value of $20.4 billion exited during the first half of 2018 compared to 337 exits with a total value of $18.5 billion in 1H 2017.



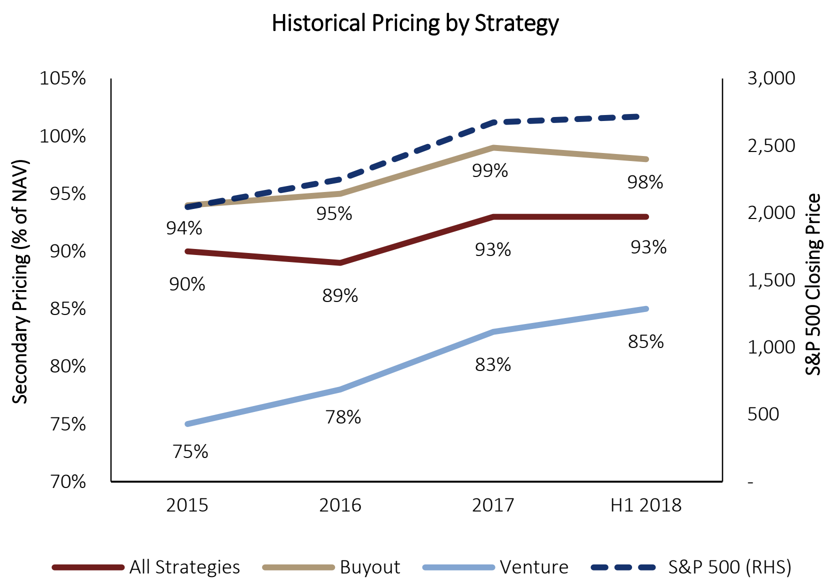
Source: Pitchbook

Secondaries

Driven by strong buyer demand and repeat seller activity, the secondary market continued its trend towards higher transaction volumes at continuously high pricing levels during 1H 2018. According to secondary advisory firm Greenhill, secondary transaction volume in the first half of 2018 was $27 billion, a 23% increase over the $22 billion recorded in 1H

2017. Abbott expects 2018 to be another year of record volume, likely surpassing the 2017 total transaction volume of $58 billion.

Preference for buyout and more recent vintage year fund sales/purchases have contributed to the elevated price environment, as both types of transactions typically trade closer to par than older or venture capital transactions. Funds with vintage years of 2012 or later are often priced significantly higher than more mature vintages, indicating buyers' focus on underlying assets with upside as opposed to relying on discounts of mature portfolios to generate returns. According to industry data collected by Greenhill, a remarkable 34% of funds with vintage years of 2012 or later received premium pricing compared to only 9% of funds 2009 or older. Average pricing for buyout transactions as a percentage of NAV remained relatively stable at 98%, compared with 99% at the end of 2017.



Source: Greenhill Cogent

Secondary dry powder remains high at $121 billion, driven by a robust fundraising environment, particularly at the larger end of the market. During 1H 2018, 12 secondary funds held final closings that amounted to a total of $12.1 billion and an average fund size of approximately $1 billion. Moreover, the average fund size is likely to increase significantly as the two largest secondary funds in history were both launched during the second quarter, each targeting $12 billion in commitments. These larger funds are competing for sizeable transactions and are driving overall market volume upwards. According to Greenhill, 11 transactions, each over $500 million, accounted for 40% of the overall $27 billion transaction volume during 1H 2018; seven of these deals were over $1 billion in NAV.

The trend towards general partner-led transactions ($7 billion in transaction volume in 1H 2018) is also expected to continue, and these deals are likely to account for 25%-30% of the overall market volume for the year. These transactions are often less diversified compared to larger fund portfolio deals and often support significantly less or no secondary deal-level leverage. To be successful in this part of the secondary market, firms need to be able to manage complexity, follow a rigorous underwriting approach to the assets, and source transactions from existing general partner relationships. In addition, the secondary market in 2018 will likely continue its broad bifurcation into (i) a segment that provides levered beta exposure to the overall PE market, where large and diversified portfolios are purchased with leverage, and (ii) a segment that is focused on alpha generation by working through complex opportunities, requiring deep asset-level diligence and strong deal sourcing and structuring capabilities.

Summary & Outlook

Political uncertainty contributed to an increase in financial sector volatility despite accelerating corporate profits to what has now been nearly a decade of uninterrupted economic growth in the U.S. Early Q3 public market trading performance has steadied somewhat after a choppier Q2, although many variables, both in the U.S. and abroad, could impact macroeconomic and financial market conditions during the second half of the year. Regarding the private markets, valuations across both the venture capital and more mature private equity segments remain elevated with several practitioners continuing to espouse the need for discipline when transacting in this type of market environment. Fundraising in both asset classes has also continued at a robust pace, and Abbott expects limited partner demand for venture capital and private equity funds to remain strong through the remainder of the year.

IMPORTANT INFORMATION

The views expressed are Abbott's as of 6/30/2018 and are in part based on market themes noted by Abbott while researching potential investments for clients. The information and charts presented in this document were generally sourced from the following materials:
Pitchbook 2Q 2018 US PE Breakdown
2Q 2018 Pitchbook-NVCA Venture Monitor
2Q 2017 Pitchbook-NVCA Venture Monitor
https://nvca.org/pressreleases/total-investment-venture-backed-companies-reached-57-billion-first-half-2018/
Preqin Secondary Market Update Q2 2018
Preqin Secondary Market Update Q1 2018
Secondary Market Overview: Greenhill & Co. (presentation to Abbott Capital dated 6/12/2018)
Greenhill – Secondary Market Trends Outlook – July 2018
Greenhill – Secondary Market Trends Outlook – January 2018

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