

Woman and Minority-Owned Private Equity Firms

A market update and review of woman and minority-owned private equity firms actively raising capital in 2016 based on data collected by Fairview Capital

February 2017

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Fairview Capital Partners, Inc. ▪ West Hartford, CT ▪ San Francisco, CA ▪ (860) 674-8066
www.fairviewcapital.com

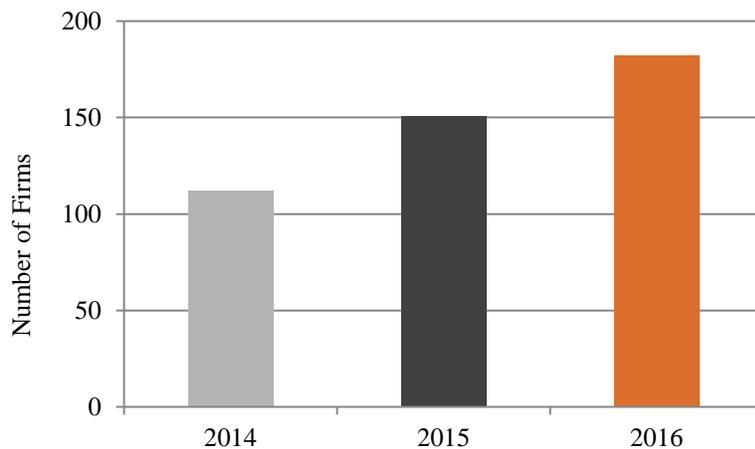
Fairview Capital’s Market Review of Woman and Minority-Owned Private Equity Firms

The criteria for classifying a private equity firm as woman and/or minority-owned often varies. In this market review, we only consider institutional quality private equity firms that are majority owned (>50%) by women and/or ethnic minorities¹. The firms must be based in, and primarily investing in, the United States.

The universe of woman and minority-owned private equity firms continued to grow and evolve in 2016. The number of woman and minority-owned private equity firms had risen to over 180 at the end of the year, up from just over 150 at the end of 2015. Fairview observed 66 of these firms actively raising capital in the market in 2016, in line with 2015 when 65 firms were in the market. In aggregate, these firms represented just 7% of all private equity firms in the market during the year.² While still underrepresented, these managers cover a wider range of strategies, industries and geographies than ever before.

A significant trend has been the high rate of new firm formation as experienced women and minorities have been launching their own new firms at a swift pace over the past few years. At the same time, there are more established woman and minority-owned firms than ever before. These managers are highly competitive with the broader private equity industry. In fact, many of the woman and minority-owned firms in the market feature strong track records, compelling strategies, truly differentiated approaches, and meaningful competitive advantages.

Exhibit 1: Universe of Woman and Minority-Owned Private Equity Firms



Data: Fairview Capital Proprietary Database of Woman and Minority-Owned Firms as of December 31, 2016

Many sophisticated institutional investors have recognized the opportunity and continue to undertake efforts to be more inclusive of diverse managers in their private equity portfolios through various means. This includes numerous public pensions plans with active or pending mandates that target woman and minority-owned firms.

Fairview was the first private equity investment management firm to broadly articulate the investment opportunity with diverse managers and remains one

of the most active firms investing with diverse managers today. Currently, Fairview manages several mandates that include a focus on woman and minority-owned firms for public pension plans across the country. The goal of all of these programs is to leverage Fairview’s experience

¹ Defined by the U.S. Census Bureau as American Indian or Alaska Native, Asian American, Black or African American, Hispanic or Latino, and Native Hawaiian or Other Pacific Islander

² Fairview Capital data and Preqin Q3 2016 Quarterly Private Equity Update (North American private equity)

and relationships to invest with select managers and achieve outperformance relative to the larger private equity universe.

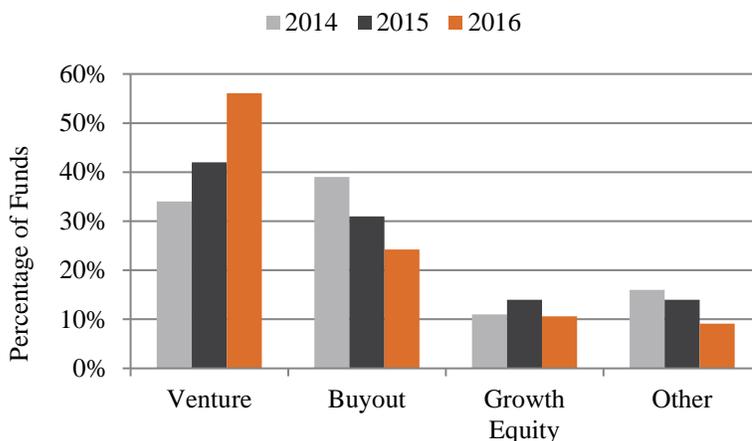
More broadly, efforts continue across the industry to increase opportunities for women and minority fund managers. The National Association of Investment Companies (NAIC), of which Fairview has been a longtime supporter, remains very active as the largest network of diverse-owned private equity firms. In June, the NAIC and the American Investment Council (AIC) partnered to form the Private Equity Women's Initiative. The Initiative has the goal of increasing the number of women entering and advancing in the private equity industry and will be led by a Working Committee of which Fairview's JoAnn Price is an initial member. The National Venture Capital Association's Diversity Task Force continued to engage in initiatives aimed at developing opportunities for women and underrepresented minorities across the venture capital ecosystem. The National Association of Securities Professionals (NASP) continued its work in supporting and advocating for the minority professionals within the securities and investments industry. At the state level, in Illinois, the Illinois Public Fund Collective Program along with NASP and other public pension plans continued to push for diversity and inclusion in financial services. In California, efforts also continue to address diversity. In October, the State Assembly Committee on Jobs, Economic Development, and the Economy held a roundtable discussion on Venture Capital, Diversity, & Economic Development in which Fairview was a participant.

As progress continues to be made, Fairview continues to believe real opportunities to foster diversity in the industry exist for institutional investors. Building programs that include funds managed by women and minorities have been proven to be impactful without compromising results and in fact have the potential for outperformance.

Given the firm's level of activity and involvement in the space, Fairview maintains one of the most robust databases on woman and minority-owned firms in the industry. The 66 woman and minority-owned firms Fairview observed actively raising capital in 2016 are a strong representative cross-section of the state of the market for woman and minority-owned firms. The following report is a summary of the characteristics of the universe today based on data from this set of funds.

In terms of strategy, 56% of woman and minority-owned funds in the market in 2016 were pursuing venture capital investments. This figure is up from 42% in 2015 and comports with a continuing trend in venture capital – a high rate of new firm formation, particularly by diverse managers. Venture funds are typically smaller in size (most seed and early stage strategies can be executed with funds smaller than \$150 million), which makes them less daunting to raise for

Exhibit 2: Fund Strategy



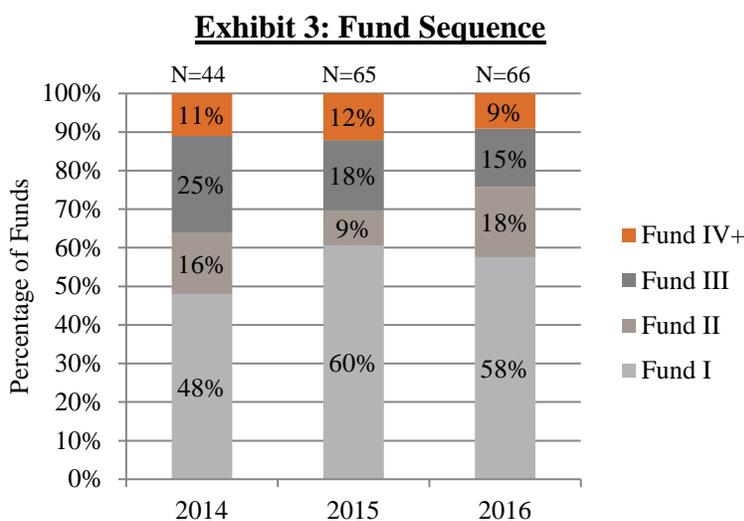
Data: Fairview Capital Proprietary Database of Woman and Minority-Owned Firms as of December 31, 2016

newer firms. In many cases, these new firms are formed through spinouts or team-ups of managers from more tenured venture capital firms. Many of the new firms are “millennial-friendly” and are more reflective of, and relatable to, the entrepreneurs and markets in which they invest. The rise in woman and minority-owned firms in venture capital has also occurred against the backdrop of continued advocacy for increased gender and ethnic diversity in venture capital as well as in the technology industry broadly.

While progress continues to be made, there remains ample opportunity for further change and inclusion. Venture capital firm Social Capital conducted a breakdown of diversity in leadership roles at the top venture capital firms in 2016 and found that progress in terms of diversity has been limited – only 11% of venture capital investment professionals were female and only one quarter of investment professionals were minorities.³ Newer venture capital firms tend to be significantly more diverse and, in turn, are much more likely to back diverse entrepreneurs. In 2016 Fairview conducted a review of the portfolios of woman and minority-owned venture capital firms recently committed to and found that between 60% and 65% of investments were with companies featuring women and/or ethnic minority founders or co-founders. It is clear that one way in which institutional investors can support diversity in the technology sector is supporting woman and minority-owned venture capital firms.

Nearly 25% of woman and minority-owned firms in the market in 2016 targeted buyout investments, the largest segment of the broader private equity universe in terms of number of firms and dollars invested. Buyout investing can benefit as much from transactional experience as relationships. This can make the transition to private equity for new diverse managers with relevant backgrounds, such as investment banking, more appealing. The vast majority of woman and minority-owned buyout funds are targeting small and middle-market opportunities. As was the case in 2015, there was again a notable increase in woman-owned buyout firms raising funds in 2016. In fact, woman-owned buyout firms represented nearly half of the woman and minority-owned buyout firm opportunity set. Similarly to what we have seen on the venture side, larger, more established buyout firms have been slow to increase diversity amongst their leaderships ranks

and as a result we find a much greater proportion of new buyout firms to be led by women and minorities.



Data: Fairview Capital Proprietary Database of Woman and Minority-Owned Firms as of December 31, 2016

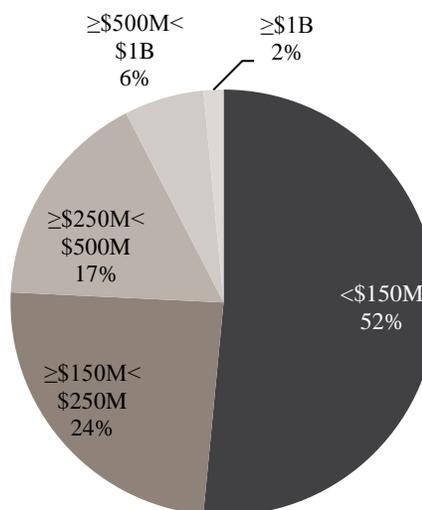
Growth in the woman and minority-owned firm market is directly correlated to new firm formation. In recent years, we have experienced a particularly high rate of new firm formation. The majority of the opportunity set in the past two years has been comprised of first-time funds being raised by new firms. In 2016, 58% of woman and

³ Social Capital and The Information, “The Future List,” December 2016

minority-owned firms in the market, 37 firms, were raising first-time funds, roughly in line with 2015. This high rate of new firm formation is a positive sign for the industry as it indicates confidence on the part of women and minorities in their ability to attract institutional capital. Managers have been encouraged and motivated to form new firms amid what has been a relatively strong fundraising environment that has featured more receptivity towards new firms and funds. Diversity in the industry has been building for some time and many women and minority investment professionals have now advanced their careers to the point they are comfortable striking out on their own. The vast majority of new firms in the market feature experienced investors with track records developed at larger, more well established firms. In addition, there are more tenured firms in existence than ever before. In 2016 there was a comparable proportion of tenured woman and minority-owned firms in the market relative to 2015.

In general, expected fund sizes for most woman and minority-owned funds are correlated to fund sequence and strategy, reflective of observations in the broader private equity market. The average expected fund size for woman and minority-owned funds in the market in 2016 was \$191 million. In aggregate, these funds were targeting \$12.6 billion in capital. The broader private equity industry featured nearly 900 funds in the market in 2016, targeting a total of \$215 billion in capital – an average of \$240 million per fund.⁴ Part of the disparity in average fund size can be explained by the fact that the majority of woman and minority-owned firms are raising first-time funds which are typically smaller than average. Also, within the buyout segment, there are very few managers leading large and mega buyout firms – whose funds drive up the overall industry average.

Exhibit 4: Fund Size



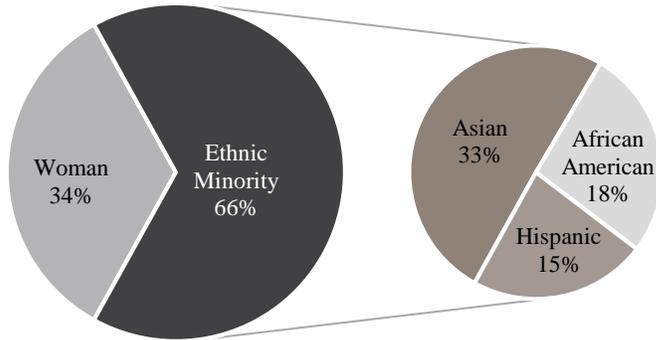
Data: Fairview Capital Proprietary Database of Woman and Minority-Owned Firms as of December 31, 2016

The ethnic and gender diversity mix within the set of woman and minority-owned firms has been constantly changing over the past few years. One notable trend has been the rise in woman-owned firms. In 2014, woman-owned firms comprised just 18% of all woman and minority-owned firms in the market. In 2016, that figure had jumped to 34%. Of the 23 woman-owned firms in the market in 2016, roughly half were pursuing venture capital strategies with the other half primarily pursuing buyout strategies. Nearly two-thirds of woman-owned firms in the market in 2016 were raising first-time funds.

African American, Asian American and Hispanic managers together tend to comprise the majority of funds being raised by ethnic minority-owned firms. This year we have observed a significant

⁴ Fairview Capital data and Preqin Q3 2016 Quarterly Private Equity Update (North American private equity)

Exhibit 5: Ethnic and Gender Diversity



Data: Fairview Capital Proprietary Database of Woman and Minority-Owned Firms as of December 31, 2016

amongst partners. The reverse is also true – African American, Hispanic and Asian-owned firms often feature women partners on the team.

Geographically, as with the broader private equity universe, woman and minority-owned private equity firms tend to be headquartered in the nation’s financial hubs. In recent years, there has been a significant increase in the number of woman and minority-owned firms being formed in the San Francisco Bay Area. The vast majority of these firms are pursuing venture capital investments. In the Northeast, New York is home to a large proportion woman and minority-owned firms – not a surprise given the diversity of the city itself, as well as the resources, mentorship and accessibility to financial firms available to woman and minority-owned firms. New York-based firms tend to be diverse in terms of strategy, featuring a strong mix of buyout, venture, growth and debt focused firms. Boston and Washington, D.C. typically come in behind New York in terms of the number of women and minority-owned firms.

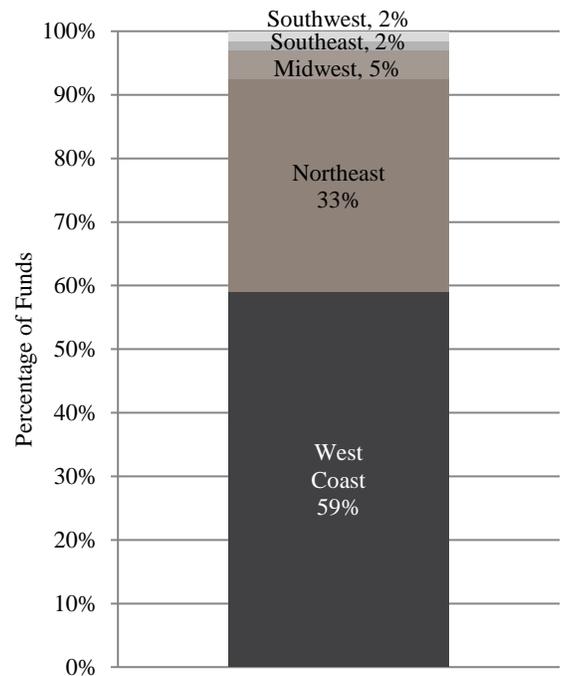
In the Midwest, woman and minority-owned firms in the tend to be based in Chicago and most focus on buyout and buyout-related investments – in line with the competitive advantages afforded by Chicago’s financial ecosystem.

The woman and minority-owned segment of the private equity industry continued to expand at a disproportionately higher rate relative to the overall private equity market in 2016. The universe is likely to continue to expand in the coming years as woman and minority managers find themselves in leadership positions at legacy firms and continue to launch their own firms.

increase in the proportion of Asian American-owned firms in the market. There has also been a moderate increase observed in the proportion of African American-owned firms in the market in 2016.

Fairview’s data reflects the primary diversity characteristic of each firm and fund. Recognizing gender and ethnic diversity are not mutually exclusive, additional analysis shows that at least one-third of woman-owned firms feature additional ethnic diversity

Exhibit 6: Firm Geography



Data: Fairview Capital Proprietary Database of Woman and Minority-Owned Firms as of December 31, 2016

Despite the continued expansion of the universe and efforts on the part of some institutional investors to be more inclusive of woman and minority managers, these firms continue to face significant challenges in raising capital and building their organizations. Too often, these managers are not on the radar of larger institutional investors and their consultants, or are associated with higher levels of risk. As has been indicated in this report, these managers certainly do not lack experience.

From a performance perspective, Fairview has ample experience building programs in the space that have outperformed the broader private equity programs of large institutional investors. These programs have helped larger institutional investors efficiently access the opportunity set, which, in addition to being overlooked, tends to feature smaller funds that are more challenging for these larger institutions to deploy capital into. Given its own history and the experiences of its team, Fairview is confident that opportunities to invest with high-quality woman and minority managers will continue to be plentiful and rewarding. We remain optimistic that these opportunities will continue to be recognized more broadly and that institutional investors will find ways to participate in this dynamic and promising segment of the private equity market.

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