



The AUSTRALIAN
PRIVATE EQUITY &
VENTURE CAPITAL
ASSOCIATION Limited

2009 Yearbook

Australian Private Equity and Venture Capital Activity Report

- EXECUTIVE SUMMARY

In association with



Foreword

As Australian business regroups after the global financial crisis, venture capital (VC) and private equity (PE) will play an increasingly important role in providing alternative funding sources within Australia's financial eco-system. To support sustainable economic growth, Australia needs a robust domestic VC and PE industry – able to step up at a time when other sources of capital are unavailable.

As this executive summary reveals, over 500 Australian companies, many of them household names, are currently backed by VC or PE funding. Given the wide reach of their activities, it is important to have reliable statistics on the size and activities of this vital driver of economic growth.

To deliver on the increasing need for data, in 2009 AVCAL launched its new Australian Private Equity Research Exchange Platform (PEREP_Analytics), based on the PEREP_Analytics data collection platform used in Europe. For the first time, this gives our local VC and PE industry a centralised proprietary database of its own, providing a richer data resource from which we can produce evidencebased research.

This document offers a snapshot of the industry's activity in FY2009, based on the first year of data collection from the new platform. Given the vast differences between the nature and fortunes of VC and PE, following a general overview, the summary breaks down its report by asset class.

We hope it furthers a broader understanding of PE's importance to the Australian economy and acts as a wake-up call to the risk of near-extinction of our VC sector.

I would like to thank AVCAL members (and non-members) who contributed their data voluntarily or their support and shared vision.

I would also like to thank Ernst & Young for partnering with AVCAL to support the PEREP_Analytics implementation and their valuable input into this document.

KATHERINE WOODTHORPE Chief Executive, AVCAL

November 2009

Overview

Like most asset classes, VC and PE were severely affected by the global financial crisis in FY2009. In Australia, total funds raised fell to \$1,540 million, on par with FY2004 levels. This sharp decline mirrored that seen in other major markets, such as the US.

However overall investment levels in Australia remained relatively stable at \$1,740 million, with a large proportion of this capital provided to existing investees for follow-on investments and capital restructures.

Figure 1: VC and PE funds raised in Australia by fiscal year (in AUD millions)

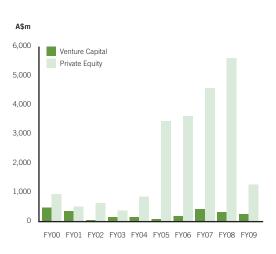
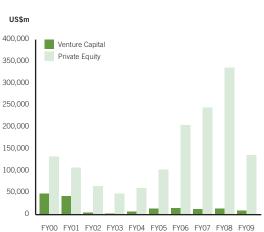


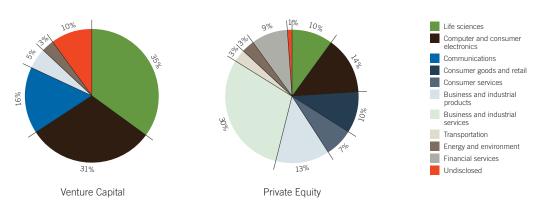
Figure 2: VC and PE funds raised in the US by (Australian) fiscal year (in USD millions)
Source: Thomson Reuters



Investment by industry

The industry continued to fund companies across a broad range of sizes and sectors. The top three sectors receiving VC investments in FY2009 were life sciences (35%), computer and consumer electronics (31%) and communications (16%). By contrast, PE investment went largely to business and industrial services (30%), computer and consumer electronics (14%), and business and industrial products (13%). In terms of total investment from VC and PE, business and industrial services received 27%, computer and consumer electronics 18% and life sciences 13%.

Figure 3: Sectoral distribution in FY2009, by investment amountNote: Sectors with fewer than 3 companies receiving investments have been aggregated into "Other/Undisclosed".



Investment by geography

As expected, Australian-domiciled companies accounted for the lion's share (84%) of the total amount invested. US-domiciled companies came second: a large proportion of these companies are VC investees building on Australian-grown technologies that have since relocated to the US.

Companies in Victoria received the most VC and PE funding in FY2009, accounting for nearly half of all funds invested in Australia. The state received over 60% more in capital invested than the next most popular Australian investment destination, New South Wales, followed by Queensland, Western Australia and South Australia.

Table 1: Investment amounts by company location in FY2009 (in AUD millions)

Note: Locations with fewer than 3 companies receiving investments have been aggregated into "Other".

	AMOUNT (AUD millions)	% OF TOTAL
Australia	1,466.00	84%
Victoria	690.30	47%
New South Wales	424.09	29%
Queensland	146.78	10%
Western Australia	58.60	4%
South Australia	9.15	1%
Unknown	137.08	9%
US	144.00	8%
New Zealand	119.82	7%
Other	10.39	1%
TOTAL INVESTMENTS	1,740.21	100%

Private Equity

While the financial crisis has limited PE activity, the flexibility of the PE business model has allowed the industry to adapt quickly to the new conditions. PE firms have responded to the crisis by intensifying their focus on improving operating efficiencies and driving growth in existing portfolio companies.

In FY2009, funds raised by PE firms totalled \$1,277 million, bringing total funds raised in the five years between FY2005 and FY2009 to \$18,541 million. The decline in funds raised in FY2009 reflects both the impact of the global financial crisis and the lower number of new funds established over the past two years, following intensified fundraising activity to capitalise on the end of the economic boom.

However, while fund raising slowed significantly, PE investment levels remained steady at \$1,560 million - slightly higher than FY2008. Given liquidity issues and trading and covenant pressures, PE deployed most of this as follow-on investment into portfolio companies to help them weather the downturn. As a result, 108 companies received the benefit of this investment: one-third of the total number of PE portfolio companies.

This active stewardship will position PE well to reap the rewards of the upturn. The industry goes into FY2010 with many healthy assets ready for exit, alongside a large pool of funds ready to be invested.

The activity documented in FY2009 dispels the myth that PE was only prospering on a wave of cheap credit. The industry has proved its ability to weather current economic conditions and is poised to become a key long-term player in Australia's economic future.

Table 2: Private equity investments in FY2009

	AMOUNT (AUD millions)	NO. OF INVESTMENTS	NO. OF COMPANIES	
Total investments in FY2009	1,559.96	108	89	
No. of companies in PE portfolios as of 30 June 2009	326			

Figure 4: Investments by Australian PE funds by fiscal year (in AUD millions)

A\$m

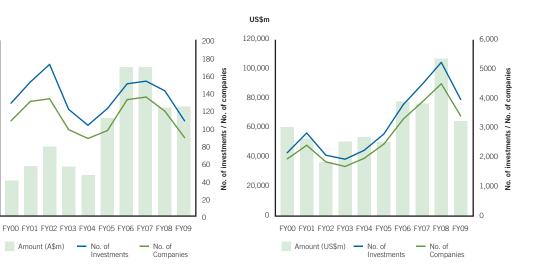
2.500

2,000

1,500

1,000

Figure 5: Investments by US PE funds by (Australian) fiscal year (in USD millions)



Source: Thomson Reuters

Venture Capital

At a tenth the size of the PE industry, VC was hit hard by the global financial crisis. In FY2009, funds raised by venture firms fell by 19% from the previous year to \$263 million, recording two consecutive quarters of declines in the first half of 2009 (-89% q-o-q in 1Q 2009 and -32% q-o-q in 2Q 2009), reflecting the difficult fundraising environment faced by the sector. None of the new VC commitments in FY2009 was for seed investments, indicating a gap at this stage of the innovation pipeline.

Table 3: Funds raised by investment stage focus - amount raised in FY2009 (in AUD millions)

INVESTMENT STAGES	AMOUNT (AUD millions)	NO. OF FUNDS RAISING CAPITAL		
Seed Stage	-	0		
Early Stage VC	44.10	3		
Later Stage VC	-	0		
Balanced VC	219.29	4		
TOTAL VENTURE	263.39	7		

Like PE, VC sustained its investment levels in FY2009, putting \$180 million into 103 companies: 26% more entities than in FY2008. Of the total investment in these companies, 67% of funds went to support start-up and early stage activity, with only 7% allocated to seed funding.

The number of VC financing rounds also increased in FY2009, largely due to additional capital being injected into existing investees, but at smaller round amounts than previously. This led to a 44% decline in the average VC investment round size from almost \$2 million in FY2008 to \$1 million in FY2009.

Figure 6: Investments by Australian VC funds by fiscal year (in AUD millions)

Figure 7: Investments by US VC funds by (Australian) fiscal year (in USD millions) Source: Thomson Reuters US\$m 100,000

No. of

Investments

9,000

8,000

7.000

6,000

5,000

3,000

2.000

1.000

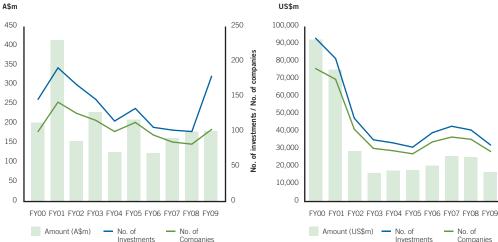


Table 4: Venture Capital investments in FY2009

	AMOUNT (AUD millions)	NO. OF INVESTMENTS	NO. OF COMPANIES	
Total investments in FY2009	180.25	179	103	
No. of companies in VC portfolios as of 30 June 2009	178			

Table 5: Distribution of VC investments in FY2009 (by stage of investee company)

STAGE OF INVESTEE COMPANY	AMOUNT (AUD millions)	% OF TOTAL	NO. OF INVESTMENTS	% OF TOTAL	NO. OF COMPANIES	% OF TOTAL
Seed	12.65	7%	34	19%	14	14%
Start-up & early stage	120.93	67%	111	62%	66	64%
Later stage venture & expansion/growth	46.68	26%	34	19%	23	22%
TOTAL VC INVESTMENT	180.25	100%	179	100%	103	100%

Conclusion

As well as offering important alternate sources of funding, Australia's PE and VC investors instil their portfolio companies with a number of cultural practices and traits that keep them growing over the long-term: an appreciation of the importance of continuous R&D, the habit of setting and reaching milestones, and the incentive structures for management to plan for long-term growth. These tenets drive companies during their formative years and remain integral parts of their DNA long after often enabling them to outperform their competitors.

Australia should therefore be concerned that the fortunes of its VC and PE sectors are markedly divergent. While at first glance the activity recorded appears parallel, with falling fund raising and sustained investment levels in both sectors, the underlying strength of these two asset classes could not be more different.

The last few years have seen Australia's PE market catch up with Europe and the US, with large amounts of funds raised and substantial investment driving economic growth. In FY2009, the PE model continued to prove robust and highly flexible, with private ownership allowing investee firms to adjust their business strategies quickly and expediently as market conditions changed.

Over the next two years, the volume of investee exits is likely to increase as markets and debt capacity free up, continuing the recent IPO activity.

With substantial capital available for deployment at a time when other sources of finance may be limited, PE appears set to continue to be an important force in shaping Australian business for years to come.

By contrast, the outlook for Australia's VC sector remains uncertain: while VC fundraising has declined sharply around the world, the Australian industry's relatively small size compounds the problem. Every month, the gap between the availability of seed capital and the demand for it grows wider - and the pipeline of start-ups grows weaker.

As the economy moves towards an upturn, this will leave Australia at a critical disadvantage. Without a healthy VC industry, Australian companies will not make the leap from new ideas to viable and sustainable economic entities. VC is a vital link in the innovation chain. Venture capitalists are the only investors willing to take entrepreneurial risks alongside company founders. No other asset class has the wherewithal or the appetite for this type of critical high-risk investment in promising ideas.

We need our PE and VC industry to continue to seek out and make the most of promising business opportunities and to fund ground-breaking ideas. This is vital to Australia's growth and innovation agenda: a necessary enabler of Australia's future economic security and our competitiveness as a nation.