# Investment Summary

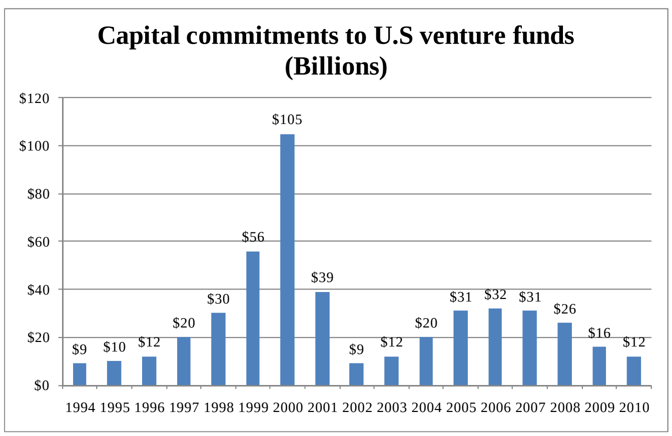
Venture Capital

**Overview:**

In 2006 Aureus wrote to clients explaining why private equity and venture capital were asset classes to be avoided. While many factors contributed to our view, fundamentally we felt excessive asset flows combined with a weak exit environment combined to create a poor return dynamic. Today, we believe venture capital in particular is an attractive asset class for clients with the appropriate profile.

**Venture:**

The end of the .com bubble in 2000 marked the beginning of a challenging decade for venture capital. From 2000 through 2010, venture investors were lucky to have their capital returned, let alone see meaningful performance. A byproduct of poor returns has been a steady exodus by investors. From a peak of $100 billion raised in 2000, annual asset flows to venture dropped to an average of $25 billion between 2001 and 2008. Those inflows dropped even further in reaction to the financial crisis to $16 billion and $12 billion in 2009 and 2010, respectively. Sentiment toward venture capital is unquestionably negative, which we believe is a positive indicator.




Against this backdrop, innovation in several areas including cloud computing, data storage, mobile computing, second generation internet applications (e.g. social networking), green/clean technology, and biotech to name a few has evolved to a point where demand for products and services in these areas is creating compelling and scalable business opportunities.

Furthermore, we believe the environment for exits from venture-backed companies looks much better over the next ten years than it did for the previous ten. Corporations have the highest level of cash on their collective balance sheets than at any time in history. Some of that cash has been accumulated by pushing off spending on innovation. Aureus believes venture-backed companies will help satisfy pent up demand for innovation over the next five to ten years, as many companies look for growth catalysts.

Another positive is an improving IPO environment, which has been quiet for years. While we recognize headwinds from The Sarbanes Oxley Act (increased reporting/expense burden), we do believe investor appetite for high growth stories is returning, making public market exits for venture-backed companies an increasingly viable option.

**Key Investment Considerations:**
Aureus believes the following are key considerations when allocating assets to venture capital:

- Venture is a "hits" business, meaning that access to the best deals drives returns
- Successful entrepreneurs are drawn to either dominant venture capital firms or newer firms where key partners have demonstrated success
- Studies suggest smaller fund size positively influences higher returns
- Diversification across managers and vintage years increases the odds of exposure to the hits that drive outsized returns
- Access to dominant/larger firms is limited and minimum investment hurdles (greater than five million dollars in many cases) significantly impacts the absolute dollars required to create a portfolio of these funds
- Understanding the potential for smaller firms is driven by many factors, not the least of which is deal experience of key partners. High investment hurdles apply for these firms as well

**Implementation:**
Aureus has thoroughly reviewed implementation options and concluded that a funds-of-funds structure best addresses the considerations outlined above. After an in-depth review of the venture funds-of-fund universe, we have determined that a group of four firms stands out. We are recommending clients with the appropriate profile allocate a portion of their portfolio to a combination of these firms over a period of several years.

Our diligence involved in depth reviews with each group, reference checks with their investors, reference checks with managers in their portfolios, and conversations with venture capitalists known well to us. We believe we have identified exceptional firms which have impressed us with their commitment to, and passion for, venture capital, understanding of the industry, access to the very best venture managers, attention to portfolio construction, and investment monitoring/administration capabilities.

The firms we have identified have meaningful (large allocations) access to established and emerging venture capital firms. The following are representative managers/funds represented across the portfolios of these firms.

**Aureus Selected Funds-of-Funds**
**Representative Portfolio Managers[1]**

| Established | Emerging |
|---|---|
| Accel Partners | .406 Ventures |
| August Capital | Andreessen Horowitz |
| Battery Ventures | Fairhaven Capital |
| Benchmark Capital | Felicis Ventures |
| Charles River Ventures | First Round Capital |
| General Catalyst | Flybridge Captial Partners |
| Greylock Partners | Foundry Group |
| Kleiner Perkins | Spark Capital |
| Redpoint Ventures | True Ventures |
| Sequoia Capital | Union Square Ventures |

Aureus believes that an investment with one or more of the funds-of-funds we have identified is an attractive opportunity and source of portfolio diversification for clients with the appropriate profile. Key profile factors to consider are investment horizon, risk tolerance, liquidity needs, and income requirements. Aureus is currently working with clients to include one or more of these managers in their asset allocation. We are happy to share details for each of these firms with clients interested in learning more.

1. Representative managers across four funds-of-funds firms. There can be no guarantee that these will be managers in specific funds invested in by Aureus clients. For illustration purposes only.