

CONTENTS

Feature Articles

This month's focus: **Private Equity—Issues in Japan and Potential Resolutions**

Overview *Yosuke Mitsusada, CMA* 2

Articles

Private Equity Trends and Performance Measurement
..... *Takeshi Shimizu, CMA / Junichiro Akiyama* 6

Globally, the amount of assets under management invested in private equity (PE) is expected to more than double over the nine years from 2016 to 2025. In Japan, in order to promote growth and raise awareness of PE as an asset class among investors, we think it useful to measure and disclose the performance of PE assets in the country. This article thus outlines the performance measurement of PE funds and trends in Japan.

Practical Considerations for Institutional Investors Building a Private Equity Portfolio
..... *Hideya Sadanaga, CMA / Tadashi Nishizawa, CMA / Yasuhiro Ono, CMA* 17

In recent years, institutional investors have been investing in private equity on a significant scale, aiming to achieve returns higher than through the public equity markets as well as to diversify their portfolios. In Japan, too, there appears to be increased interest in private equity among the institutional investor base.

However, for institutional investors to be able to invest in private equity on a large scale there are many practical issues and challenges that must be addressed. In this article, we try to point out some of the key issues and challenges pertaining to portfolio construction, fund selection, setting up middle and back office functions, and building an appropriate internal organization.

Private Equity Investment Benchmark: Model and Test
..... *Naoshi Ikeda / Kotaro Inoue, CMA / Hiroki Ozawa* 30

We constructed a simulation model of investment return from private equity funds and calculated a benchmark return by vintage year and industry based on 274 investments by 21 private equity funds in Japan from 1998 to 2015. We confirmed the appropriateness of our simulation model assumptions based on our original survey to PE funds. Furthermore, with the cooperation of two PE funds, we analyzed sources of excess return over the benchmark by using detailed information on actual investment cases.

Comparison of Performance Measurements of Private Equity Fund Investments	<i>Shin Shiraki, CMA / Shinobu Miyata</i>	42
--	---	----

In general, measurement of the performance of private equity investments refers to ‘internal rate of return’ (IRR) so as to take into account erratic cash legs arising from investment in terms of both timing and amounts. And, ‘investment multiple’ is also referred to as a typical measurement to gauge absolute return on investment. Global Investment Performance Standards (GIPS) require the disclosure of an annualized since-inception internal rate of return (SI-IRR) and other investment multiples regarding performance of private equity funds. Recently, investors have found it difficult to compare the performance of private equity funds among peer groups of private equity funds or against public market indices due to the uniqueness of cash flows in private equity investments, hence many measurements have been created and tested. However, even now, there exists no established measurement of performance of private equity funds that is commonly used, but rather various measurements and tools are applied by each investor and GP for their own respective purposes.

By analyzing advantages and disadvantages, this article endeavors to compare the performance measurements of private equity funds which practitioners utilize for their investments. Following this comparison, the authors highlight the ‘direct alpha’ method (Gredil, Griffiths and Stucke[2014]) as being the most reasonable and reliable measurement.

Prospects

Definition and Identification of High-Frequency Traders	<i>Katsumasa Nishide</i>	53
--	--------------------------	----

Economic and Industrial Analysis

The End of History and Uncertain Times that Follow	<i>Hideaki Asahi</i>	57
---	----------------------	----

Point of View	<i>Yasuhiro Atsumi</i>	70
----------------------	------------------------	----

Article

Evolution of Size Premium in the Japanese Stock Market: An Implication for Valuation Practice	<i>Takayoshi Nakaoka / Ryosuke Osakake, CMA</i>	75
--	---	----

The aim of this paper is to examine the evolution of size premium in the Japanese stock market. We show that size premium, which is estimated by CAPM-based econometric specification, fluctuates over time and depends on the economic cycle. Moreover, even when we apply the Fama-French three factor model to this analysis, we find that size-related excess returns correlate to economic expansion periods. This result suggests the existence of ‘remaining’ size premium being overlooked so far.

Book Reviews	<i>Sadakazu Osaki, CMA / Satoshi Sakamaki, CMA / Satoshi Komiyama</i>	85
SAAJ News		96