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**To:** Undisclosed recipients;;

**Subject:** Eye on the Market: May 17, 2011

**Date:** Tue, 17 May 2011 14:37:49 +0000

**Attachments:** 05-17-11\_-\_EOTM\_-\_Lazarus\_returns\_-\_private\_equity\_after\_the\_recession.pdf

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**Eye on the Market, May 17, 2011**

**Topics: Private Equity after the Recession; update on Microsoft and Skype**

Our recent Eye on the Market notes have spent a lot of time on the US debt ceiling, the situation in Japan\*, rising oil prices and the failure of Middle Eastern growth models, the deteriorating European periphery, Asian inflation and other challenges to the robust global improvement in corporate profits. I cannot recall a period when there were quite so many macroeconomic headwinds facing a private sector recovery. Our view remains the same: while profits are likely to grow again this year (by 10%-12%), markets are unlikely to pay much for them, since P/E multiples reflect sustainability of the profits themselves. Portfolios are positioned for a single-digit return year for developed market equities.

This week, a look at private equity in the wake of the recession, with sections on the performance and the return of capital of our funds offered from 2005 to 2010; recent academic studies focusing on the performance of private equity versus public equity over extended periods; current pricing and leverage trends; the prospects for corporate carve-outs; and an update on Skype, the largest holding of one of our growth equity managers, now that Microsoft has announced its intention to buy it for \$8.5 billion.

Michael Cembalest  
Chief Investment Officer

\* There has probably been a melt-through in reactors 1, 2 and 3, unnoticed by plant managers until last week due to faulty readings of pressure differentials designed to indicate water levels. Without water to serve as a heat transfer, decay heat of the nuclear materials appears to have burned through reactor vessels. The risk of faulty pressure differential readings was discovered in the US in 1993; unclear if Japan was aware of it. More next week.

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