

Newsletter

General Market Review August 2005

The soaring costs of crude oil, gasoline and other energy products appear to have had a smaller overall impact on two key economic variables in the two months preceding hurricane Katrina's landfall than analysts had expected. The U.S. trade deficit narrowed by 2.6%, to \$57.9 billion, as imports of consumer and capital goods fell and exports of industrial supplies and materials and capital goods rose. Economists had been expecting the trade deficit to widen to \$59.8 billion. The producer price index, which measures what producers receive for their goods and services, rose 0.6% in August. Excluding the volatile energy and food prices, the core index was unchanged. Economists were expecting an overall increase of 0.7% and the core rate to rise by 0.1%.

Hurricane Katrina's aftermath largely overshadowed the results of other economic news during August. Consumer confidence for August reached 105.6, higher than July's 103.6 and ahead of the market's expectation of 101.0. Unemployment reached a four-year low of 4.9%, while a Labour Department report showed 169,000 jobs created in August, fewer than the 190,000 predicted. Making sense of these two seemingly disparate pieces of economic data is complicated by the post-Katrina situation. Many fear the hurricane's aftermath will exacerbate a slowdown already perceived as beginning to emerge in the economy and persuade the Federal Reserve to halt its string of interest-rate hikes.

Sources: AP, The New York Times

Absolute Private Equity Ltd.

Portfolio Description

Absolute Private Equity focuses its investment strategy mainly on the private equity market. Absolute Private Equity commits its money to private equity funds, which pursue investment strategies differing by industry, geographic region and stage of financing. The asset class of private equity is characterized by a long investment horizon. From the time of capital commitment, through the investment cycle and up to the realization period, between three to seven years elapse. In order to maximize the returns on capital invested for its shareholders, Absolute Private Equity employs a cash management strategy through a portfolio of absolute return strategies, which targets investments in non-traditional funds that can generate immediate returns. The capital within the absolute return part will be allocated to the private equity portion, as soon as the underlying private equity funds call committed capital for investments.

Investment Performance as of August 31, 2005

		Performance August 2005	Performance year to date	Performance since Inception
Absolute Private Equity NAV (USD)	USD 66.19	2.02%	11.28%	24.42%
Share price (USD)	USD 58.15	-1.44%	35.23%	2.88%
Premium (Discount)	-12.15%			
Morgan Stanley World Equity	1'194.81	0.53%	2.18%	-8.46%
JP Morgan Global Government Bond Index	359.576	0.89%	3.95%	30.93%

Past performance is no guarantee of future results. Performance numbers are estimated net of management and performance fees and are subject to change

Private Equity Review

Even as private equity firms continue to lobby against new accounting rules slated to take effect in 2006 - especially those requiring expensing of stock options - their portfolio companies are quietly preparing for the impact of those rules. The biggest changes that these companies should be bracing for under the new rules known as FAS 123(R) are changes to equity compensation methods. Many publicly traded companies have already adopted the rules, and all indications are that private companies will have to start complying with them on January 1, 2006.

The new rules, which determine how compensation and equity awards are treated for accounting purposes, will have a significant impact on the companies' balance sheets, potentially affecting the sale price a private equity firm can command when it looks to exit. Accounting treatments can also have an impact on private equity-backed companies that are contemplating an initial public offering ("IPO"), or companies trying to arrange for bank debt. The accounting technique known as "the fair value approach" that will generally be adopted under the new rules requires companies to value options over the entire vesting period, rather than at the time of the grant, generating a higher value for the options. This is expected to greatly increase compensation expense for companies, compared to the method previously popular with companies, the intrinsic value method. Under that method, companies were required to use the difference between the market price of the stock and the strike price. Companies can still use that method, but going forward, companies would need to recalculate the difference between the market price and the strike price every quarter until the options are exercised. Doing so would result in greater balance sheet volatility, making it problematic especially for companies that are preparing for an IPO.

Private equity firms and their portfolio companies may well emulate public companies to cut down on the balance sheet hit the new rules will bring, issuing fewer stock options and increasing their use of restricted stock. Attorneys expect many companies to make a wave of options grants before the new rules become effective in 2006. Companies may also accelerate their timetables for making these awards. There will also be some advantages to the new methods. One is more flexibility in granting performance-based awards. The new rules on performance-based vesting no longer require companies to set a fixed vesting date. Under the old rules, a grant could sometimes vest at its fixed date even if performance goals were not met. Also on the plus side, private companies that need to re-price their options - for example if the stock price goes down - can get a fixed accounting treatment calculated using a new formula, which will result in a lower charge for the companies. Previously, the companies had to use a variable accounting method, which resulted in a greater expense for the companies.

Source: Private Equity Interactive

Overall Allocation Overview as of August 31, 2005

	Asset Value (USD)	In % of Total Assets
Private Equity Investments	491'106'256	65.15%
Absolute Return Strategies	136'279'661	18.08%
Cash	126'440'737	16.77%
Total Net Assets		
Absolute Private Equity	753'826'654	100.00 %

Private Equity Investments as of August 31, 2005

Private Equity Funds	Investment Focus	Commitments USD	Market Value of Investments USD	% of Commitments	% of Absolute Private Equity Assets
Clarity Partners	Software & technology companies in telecom, media and internet	10'000'000	4'491'489	44.91%	0.60%
Bay Partners	Early stage investment in US technology companies	8'000'000	3'052'107	38.15%	0.41%
GRP II	Start-up and venture capital in the US and EU	15'000'000	8'975'269	59.84%	1.19%
AC Private Equity Invest	Private Equity with focus on Southern Europe	10'000'000	8'011'590	80.12%	1.06%
Warburg Pincus International Partners, LP and affiliates	Venture capital, buyouts and recapitalizations in a broad range of industries world wide	200'000'000	166'549'131	83.27%	22.11%
Warburg Pincus Private Equity VIII	Venture & growth capital and buyouts in a broad range of industries	25'000'000	19'376'334	77.51%	2.57%
PAI III Europe	Focus on buyouts, lesser extent growth capital, in Western Europe	24'450'558	19'588'425	80.11%	2.60%
CSFB Fund VII Investor, LP	Venture & growth capital and buyouts in a broad range of industries	140'000'000	95'974'784	68.55%	12.74%
CSFB Middle Market Value Investor, LP	Focus on middle market buyouts in the US	74'925'000	50'892'480	67.92%	6.75%
DLJ Merchant Banking Partners III	Buyout in a broad range of industries mainly in the US	15'000'000	10'112'586	67.42%	1.34%
Matlin Patterson Global Opportunities Partners "	Investments into distressed companies world-wide	50'000'000	40'502'078	81.00%	5.38%
Terra Firma Capital Partners	Heavy-asset based and out-of-favour European companies with a potential for active value creation	90'967'454	43'400'584	47.71%	5.76%
DLJ Venture Partners II	Venture & growth capital in a broad range of industries world-wide	7'111'396	4'865'748	68.42%	0.65%
ADM Maculus Fund, L.P.	Distressed assets and undervalued situations in Asia	15'000'000	15'313'652	102.09%	2.03%
Total		685'454'408	491'106'257	71.65%	65.18%

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Private Equity Investments Review

The total commitments as of August 31, 2005 stand at USD 685.5 million, of which USD 491.1 million have been invested. This represents 71.65% of committed capital and 65.18% of total net assets. During August 25.3 million were called for new investments. Unrealized gains of USD 5.9 million were attributable to GRP II, WPIP, WPIP LLC, WP Private Equity VIII. Bay Partners and ADM Maculus show an unrealized loss of USD 367'657. Distributions of total USD 11.4 million came from GRPII, PAI Europe III, Matlin Patterson GOP, DLJ VP II, WPIP and WPIP LLC. Recallable ROC of USD 6 million was attributable to CSFB MMV, Matlin Patterson GOP and CSFB Fund VII.

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