



Secondary Market: Overview and Outlook

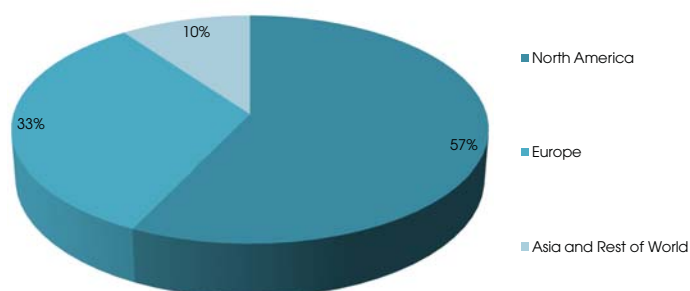
With secondary market activity continuing to rise, [Jessica Duong](#) and [Patrick Adefuye](#) explore the latest trends in the market, as well as those likely to sell and buy interests on the market in the future.

Secondary market activity in 2012 has continued to increase following record levels of transaction activity achieved in 2011. The \$25bn worth of transactions completed last year is expected to be surpassed this year, given reports of a considerable number of deals taking place, including several large transactions. Some of the largest transactions to be completed in 2012 so far include Coller Capital's purchase of a portfolio of funds from UK-based bank Lloyds Banking Group in a transaction worth approximately \$1.7bn; the New York City retirement systems' (New York City Employees' Retirement System, New York City Fire Department Pension Fund, New York City Police Pension Fund and New York City Teachers' Retirement System) sale of \$976mn worth of private equity fund interests on the secondary market, reducing the number of its managers by nine in the process; and OMERS' sale of \$850mn worth of fund investments to AXA Private Equity as part of a continued push towards direct investing.

Fig. 1 shows that the overwhelming majority of transactions to date have involved buyout and venture capital fund interests changing hands, according to Preqin's Secondary Market Monitor historical transactions data. Other fund interests sold include real estate, growth capital, fund of funds and mezzanine interests. Fig. 2 reveals that the majority of traded interests have been in North America-focused vehicles, which is unsurprising given that much more capital has been raised for these vehicles compared to Europe and Asia and Rest of World-focused vehicles. The growth in capital raised in the primary market for Asia and Rest of World vehicles will likely translate to a larger volume of secondary transactions of fund interests targeting this region in the future.

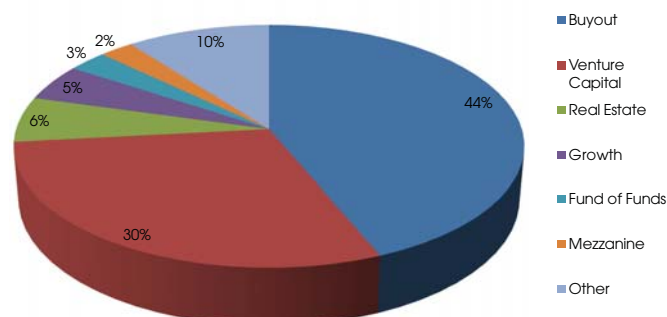
The supply of fund stakes to the secondary market has come mainly from public pension funds, as well as banks and investment banks,

Fig. 2: Breakdown of Funds Traded on the Secondary Market by Primary Geographic Focus



Source: Preqin Secondary Market Monitor

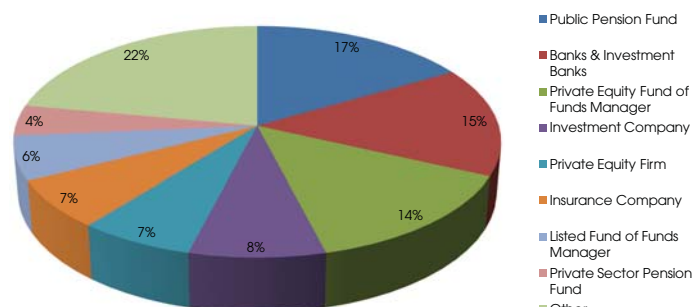
Fig. 1: Breakdown of Funds Traded on the Secondary Market by Type



Source: Preqin Secondary Market Monitor

as shown in Fig. 3. Additionally, the active portfolio management strategies of fund of funds managers and the disposal of legacy fund interests by private equity firms have supplied interests to the market. Listed private equity funds of funds have also been contributors, particularly in the last couple of years, when assets consistently trading below NAV put pressure on the boards and managers of listed vehicles, as shareholders demanded the liquidation of underlying fund interests to regain capital. Listed private equity fund of funds Conversus Capital is one such example; pressure from shareholders over the discount to which shares in the vehicle were trading relative to NAV led the fund of funds to adopt a harvesting strategy and review options to maximize shareholder value, which eventually culminated in a secondary sale. In July 2012, Conversus Capital sold all of its private equity fund interests to HarbourVest Partners in a transaction worth \$1.4bn.

Fig. 3: Breakdown of Past Secondary Market Sellers by Firm Type



Source: Preqin Secondary Market Monitor

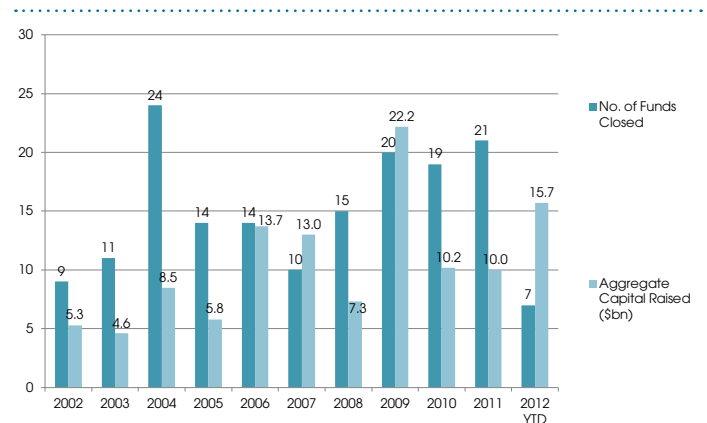


On the buying side, the record levels of capital raised in 2009 have clearly filtered into secondary market transaction volume, given the growth in this area over the past three years. As the investment periods of those vehicles come to an end, managers are likely to seek to raise fresh capital in the coming years. Indeed, 2012 has seen some of the prominent secondary fund of funds managers successfully return to the fundraising market, seeking to raise larger vehicles. The record amount ever raised for a secondaries vehicle was broken this year when AXA Private Equity raised \$7.1bn for AXA Secondary Fund V, surpassing the \$7bn raised by Lexington Partners for Lexington Capital Partners VII in 2010.

Coller Capital and CS Strategic Partners both also raised large vehicles this year, closing on \$5.5bn and \$2.4bn for Coller International Partners VI and CS Strategic Partners V respectively. Although just seven secondaries vehicles completed fundraising in January to September 2012, the aggregate \$15.7bn raised surpasses every historical yearly total, with the exception of the record of 2009 (Fig. 4). Additionally, there are currently 32 secondaries vehicles in the market seeking an aggregate \$27bn in capital commitments.

Fig. 5 shows the top 10 secondaries fund managers by their amount of estimated dry powder. The largest two are Coller Capital and AXA Private Equity, buoyed by their recent fundraising efforts.

Fig. 4: Annual Secondaries Fundraising, 2002-2012 YTD



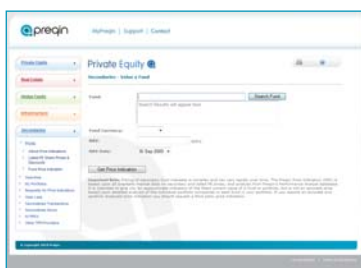
Source: Preqin Secondary Market Monitor

Lexington Partners also still has substantial dry powder available to deploy, while further secondary capital is still available to a number of primary fund of funds managers, such as Pantheon and Adams Street Partners.

The amount of capital to be invested in secondary market opportunities will be augmented by non-traditional LPs investing in the secondary market, meaning those that are not managers of secondaries vehicles. These investors continue to see the

Preqin's Secondary Market Monitor

The private equity secondary market is a rapidly evolving and non-transparent market. Preqin's Secondary Market Monitor provides vital intelligence to aid the execution of a successful investment strategy.



- **Pricing information:** view historical and current trends in share price and trading discounts / premia for listed private equity funds, an excellent proxy for secondary market pricing.
- **Profiles:** view detailed profiles for the investment preferences of over 680 potential buyers and over 300 potential sellers of fund interests, plus profiles for over 60 intermediaries, identified through interviews conducted by our dedicated research teams.
- **Secondaries news:** view the latest news in the secondary market, including recent transactions and fund closes.
- **Transaction history:** view an archive of past secondary market transaction details in tabular form. This information can be viewed by individual transaction or by fund interests sold.

For more information on Secondary Market Monitor please visit:
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Fig. 5: Top 10 Secondary Fund of Funds Managers by Estimated Dry Powder

Firm	Firm Location	Estimated Dry Powder (\$mn)
Coller Capital	UK	6,517
AXA Private Equity	France	6,369
Lexington Partners	US	3,511
Goldman Sachs Private Equity Group	US	3,061
CS Strategic Partners	US	2,622
Pantheon	UK	2,338
AlpInvest Partners	Netherlands	1,149
Landmark Partners	US	998
Adams Street Partners	US	933
Newbury Partners	US	722

Source: Preqin Secondary Market Monitor

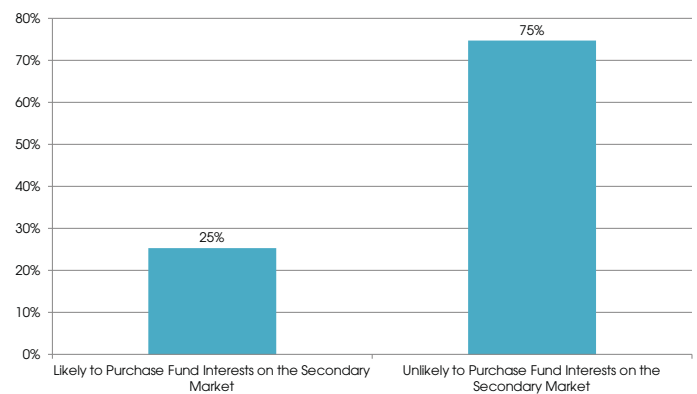
benefits of purchasing secondary market positions, which include the mitigation of the J-Curve and the ability to purchase assets at discounts to NAV. Preqin's Secondary Market Monitor database, which profiles limited partners and gauges their interest in buying funds on the secondary market, shows that over the next 24 months 25% of non-traditional buyers indicate that they are likely to purchase fund interests on the secondary market, as shown in Fig. 6. Within this 25% of non-traditional buyers likely to purchase fund interests, 61% see adding secondary market stakes to their private equity portfolio as a possibility, while 30% view secondary market purchases purely as an opportunistic investment strategy and 9% state that they are highly likely to buy a fund interest on the secondary market.

Fig. 7 shows the wide range of types of investor that have an interest in buying on the secondary market. Public pension funds and private sector pension funds represent a significant 25% and 13% respectively of these institutional investors. Montgomery County Employees' Retirement System is an example of a public pension fund that is an entirely opportunistic investor in the private equity secondary market, considering purchasing stakes in most fund types, geographies and fund vintages.

The supply of fund interests to the secondary market in the coming years is generally expected to be provided by financial institutions, as well as public pension funds. Financial institutions are expected to continue to bring further interests to market in the future, with regulatory restrictions looming closer, such as Basel III and Solvency II. Public pension funds in the post-financial crisis environment now adopt a more proactive approach to portfolio management, using the secondary market to remove underperforming managers and rid themselves of the administrative burden and negative impact on performance of lingering 'tail-end' vehicles that are struggling to liquidate.

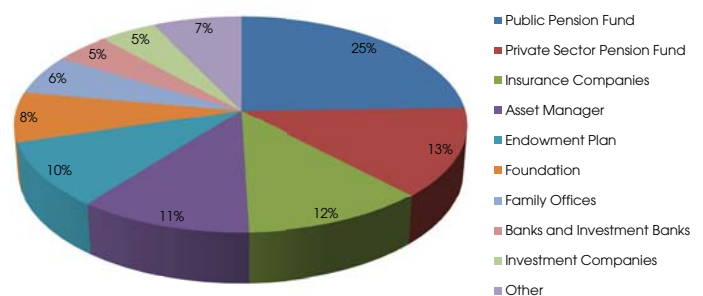
Fig. 8 illustrates the make-up of institutional investors that have indicated an interest in selling fund interests on the secondary market over the next 24 months. A noteworthy trend can be seen in the geographic location of these potential sellers. Fig. 9 shows that, of the financial institutions that have indicated an interest in selling, the overwhelming majority are based in Europe. In comparison, US-based financial institutions make up a much smaller proportion

Fig. 6: Institutional Investor Likelihood of Purchasing Fund Interests on the Secondary Market over the Next 24 Months



Source: Preqin Secondary Market Monitor

Fig. 7: Breakdown of Institutional Investors Purchasing Fund Interests on the Secondary Market Over the Next 24 Months by Type

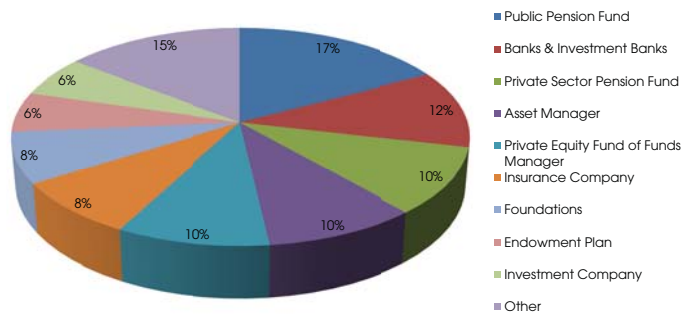


Source: Preqin Secondary Market Monitor

of financial institutions seeking to sell. One example of a financial institution likely to sell interests on the secondary market is Sweden-based Länsförsäkringar. The insurance company brought a portfolio of 36 private equity fund interests, worth up to €1.5bn, to the secondary market earlier this year and it is believed to be in the final stages of completing a sale.



Fig. 8: Breakdown of Possible Sellers of Fund Interests on the Secondary Market over the Next 24 Months by Type

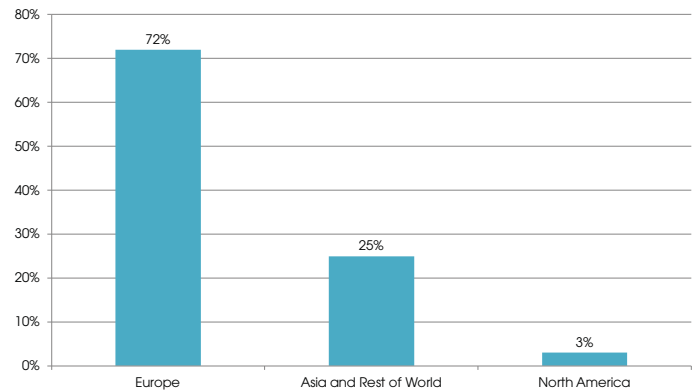


Source: Preqin Secondary Market Monitor

The supply of fund interests on the secondary market from North America-based institutions will most likely come from public pension funds. Fig. 10 shows that the majority of public pension funds with an interest in selling in the next 24 months are based in North America. Likely public pension fund sellers include California Public Employees' Retirement System (CalPERS). The public pension fund completed two secondary market transactions in 2011, selling portfolios at a premium, and is believed to be currently in the market with another portfolio of interests worth \$200mn, consisting mainly of mature venture capital fund investments with late 1990s vintages.

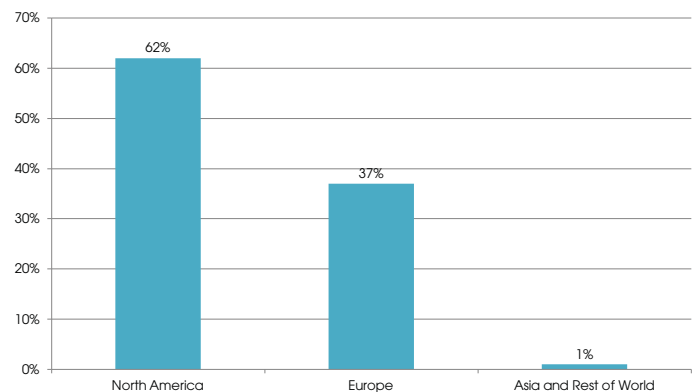
In what looks set to be a record year for the secondary market, capital has been put to work in a number of large transactions. There is also still ample capital available for investment in the secondary market. This capital comes from secondary fund managers, some of whom have returned to the fundraising market to raise mega vehicles, as well as from the more experienced and sophisticated institutional investors looking to take advantage of the benefits of the secondary market. The supply line of interests is likely to continue to come from financial institutions (particularly Europe-based ones), in the immediate future, as they need to sell to conform to new regulations. Pension funds may also contribute,

Fig. 9: Breakdown of Financial Institutions Considering Selling Fund Interests on the Secondary Market over the Next 24 Months by Location



Source: Preqin Secondary Market Monitor

Fig. 10: Breakdown of Public Pension Funds Considering Selling Fund Interests on the Secondary Market Over the Next 24 Months by Location



Source: Preqin Secondary Market Monitor

though the extent of this will depend heavily on pricing as they are under less pressure to sell.

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