

Secondary Market for Alternative Assets: A Seller's Market

A Secondary Buyer's Perspective

- Michael Hacker, Managing Director, AlInvest



How has your level of activity changed in the past 12 months compared to the 12 months prior to that?

AlInvest has deployed capital in the secondary market at a very consistent pace over the past five years and continues to target an annual deployment of \$1.0bn to \$1.5bn in secondaries. While we have seen the volume of secondary opportunities actually continue to increase steadily in 2013 and again in 2014, the composition of the deal flow has been more variable.

What proportion of deals you are involved in are intermediated?

We find that intermediaries can play an important role working with sellers in the secondary market. Since the first intermediaries were formed about 10 years ago, the number of these players has grown substantially to the point where we believe that over half of all secondary volume is intermediated in some way. Today, our experience shows that many LPs choose to hire an advisor, particularly to organize an auction process for the sale of a large portfolio of fund interests, and AlInvest has sourced a significant number of investment opportunities through these intermediated processes. However, an important component of AlInvest's strategy is to identify opportunities that are not broadly available to all secondary buyers. These transactions tend to be negotiated directly with the seller, and an intermediary (if any) serves primarily an advisory or confirmatory function.

Are you seeing more competition from non-traditional LPs in auctions?

For several years we have seen institutional LPs trying to increase their level of direct activity in the secondary market, and we continue to see LPs of all stripes participating in the market, albeit at the margins. We have regularly seen LPs participate in secondary auctions; however, we find it is far less common to see these investors successfully navigate an auction process and prevail against dedicated secondary investors. In our experience the average LP approaches the secondary market opportunistically and we believe these LPs do not have the resources necessary to source, conduct due diligence and execute secondary transactions on a meaningful scale. Although a small number of large LPs have formed dedicated teams to pursue secondaries, we believe most LPs pursue secondaries on an indirect basis through an existing investor in the market.

What impact is this having on pricing of the various fund types?

We believe that demand in the secondary market has increased as a result of an increased amount of dedicated capital raised

by new and existing secondary investors as well as capital from non-traditional buyers, including LPs. Since mid-2013, despite the increased supply of assets in the secondary market, we have seen increased competition for assets and higher prices. The focus of traditional LPs in the secondary market has often been on LP interests in US buyout funds managed by brand-name managers. Competition can be particularly noticeable in intermediated auctions for small to medium sized portfolios of these LP interests. However, these traditional LPs have not been a significant factor in large or complex transactions, where AlInvest has historically been most active.

What types of institutions are you seeing selling fund interests?

The seller universe in the private equity secondary market has been broad for some time. We believe that an increasing proportion of investment managers view the secondary market as an important portfolio management tool and that most sizeable institutional investors have at least contemplated a secondary transaction at some point. Financial institutions have been a very steady source of deal flow for AlInvest for many years, as well as public pensions, endowments and funds of funds.

Do you expect the current level of activity in the market to be sustained?

Because the volume in the secondary market has continued to set new records each year, it is always difficult to predict whether this trend of sustained growth can continue. However, our expectation for 2014 is that volume will once again increase year-over-year. We believe that the increased base of private equity assets outstanding, combined with an increasingly broad acceptance of the secondary market as a tool for portfolio management purposes, may point toward a sustained high level of volume for the foreseeable future.

AlInvest Partners

AlInvest is a global private equity investor with \$52bn of assets under management as of March 31, 2014. AlInvest's activities cover a broad range of private equity investing, including primary fund commitments, secondary purchases and co-investments. The firm's investments span the full spectrum of private equity, including buyouts, venture capital, growth capital, mezzanine, and distressed.

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