

Secondaries

Private markets education

Karim Cherif, Head of CIO Alternatives, UBS Switzerland AG; Antoinette Zuidweg, Alternative Investment Strategist, UBS Switzerland AG; Laetitia Friedemann, CFA, Alternative Investment Strategist, UBS AG Singapore Branch; Daniel J. Scansaroli, Head of Portfolio Strategy & UBS Wealth Way Solutions, CIO Americas, UBS Financial Services Inc. (UBS FS); Jennifer Liu, Private Markets Strategist, UBS Financial Services Inc. (UBS FS).

This primer provides an overview of private market secondaries and covers the strategy basics, market dynamics, performance, and benefits in an investor’s portfolio.



Secondary funds currently have over USD 465 billion in assets under management (AUM), representing 3% of private markets AUM.



Secondary funds acquire an existing fund interest or asset from primary investors, offering an opportunity for liquidity in private markets.



Secondary funds offer diversification benefits and defensive characteristics valuable to building private markets portfolios.

Summary

- Private market secondaries refers to transactions whereby a secondary investor buys an existing fund interest or asset from primary investors, also called limited partners (LPs).
- In traditional LP secondaries, a secondary buyer acquires primary investors’ commitments into funds, usually at a discount.
- In GP-led secondaries, the general partner (GP) of a fund proactively engages a secondary buyer to generate liquidity for its investors, while aiming to hold onto assets for longer.
- Transaction volumes reached USD 112 billion in 2023, Private equity strategies, including buyouts and venture capital, represented the majority of transactions, as did North American funds.
- Secondary funds delivered a median 14.2% internal rate of return (IRR) and 1.6x total value to paid-in (TVPI) multiple over the 1999–2019 vintages.
- Secondary funds tend to exhibit higher IRRs but lower TVPI multiples than primary private equity funds owing to faster cash distributions and more mature holdings, respectively.
- Secondaries tend to exhibit a lower return dispersion, loss rates, and return volatility than primary buyout funds, which is why they are viewed as a more conservative way to build initial exposure to private markets. Secondaries typically also offer access to more mature assets than primary buyouts.
- Economic stress typically enhances investment deal flow in secondaries and creates an opportunity to acquire assets at greater discounts.
- Secondary funds offer diversification benefits and defensive characteristics that are valuable to building private markets portfolios, including accelerated exposure, reduced blind pool risk, early liquidity, and J-curve mitigation.

This report is part of a series of short primers on specific private market strategies. For a deeper understanding of private markets, please read our [Introduction to Private Markets](#). Find more information on the client portal or contact your advisor for assistance.



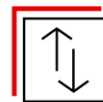
465bn
Secondaries assets under management (AUM) in USD in 2023



3.5x
AUM growth 2013 – 2023



1.6x
Median Secondaries TVPI 1999 – 2019



14.2%
Median Secondaries pooled IRR 1999 – 2019



85%
Average 2023 LP portfolio pricing as a % of NAV



\$112bn
Secondary transaction volume 2023

Source: Jefferies, Cambridge Associates, Preqin, UBS October 2024.

What are private market secondaries?

Private market secondaries refer to transactions whereby a secondary buyer acquires an existing fund interest or asset from primary investors, creating liquidity in private markets

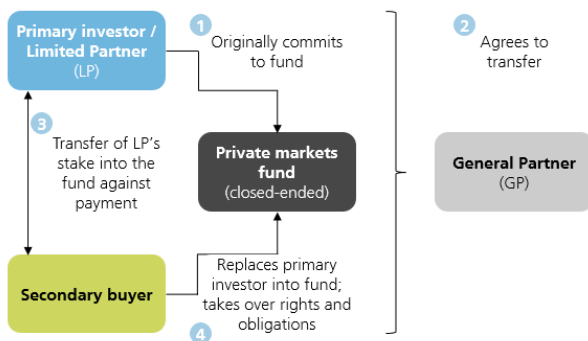
Definition and transaction types

- Private market secondaries refers to transactions whereby a secondary investor buys an existing fund interest or asset from primary investors, also called limited partners (LPs).
- In traditional LP secondaries, a secondary buyer acquires primary investors' commitments into funds (Fig. 1), usually at a discount. LPs typically initiate these transactions out of a need to generate liquidity or to rebalance their portfolio.
- LPs can decide to sell one or multiple fund interests at the same time, and the underlying funds can vary in maturity. Early stage secondaries involve funds that are still investing, while mature and tail-end secondaries involve funds that are in their harvest and extension periods, respectively.
- In GP-led secondaries, the general partner (GP) of a fund proactively engages a secondary buyer to generate liquidity for its investors. In a majority of cases, GPs aim to continue holding onto assets for longer, while giving their LPs the option to either cash out or remain invested. Transactions offer limited discounts compared to traditional LP deals, but incentives to secondary buyers can include deferrals, earnouts, or preferred equity.
- GP-led transactions take a variety of forms, including single or multi-asset continuation vehicles, strip sales, tender offers, fund restructurings, and stapled secondary transactions.

Market dynamics and opportunity

- Private equity secondaries have grown more than threefold over the past decade, accumulating USD 465 billion in assets under management (AUM) in 2023 (Fig. 2).
- Meanwhile, transaction volumes reached USD 112 billion in 2023 based on data by Jefferies (Fig. 3), 54% of which being traditional LP secondaries and 46% GP-led deals.
- Based on the same dataset, private equity strategies continue to dominate transactions, with buyout funds representing 72% of total volume and venture capital 12%. Private debt and real estate made up 5% and 2% of the overall volume, respectively.
- In terms of geographies, North American funds represented 68% of volumes, followed by Europe with 25%, and Asia and the rest of the world making up the remainder—roughly in line with the composition of private markets AUM.
- The main LPs that are selling fund stakes are institutional investors—such as endowment, pension, and sovereign wealth funds, as well as fund-of-funds and financial institutions—while family offices and high net worth individuals have increased their participation over the years.
- Secondary volumes should continue to gain momentum, as LPs remain unsatisfied with the distribution levels and undergo regular portfolio management exercises, GP-led secondaries become mainstream, and secondaries as a strategy continue to attract capital.

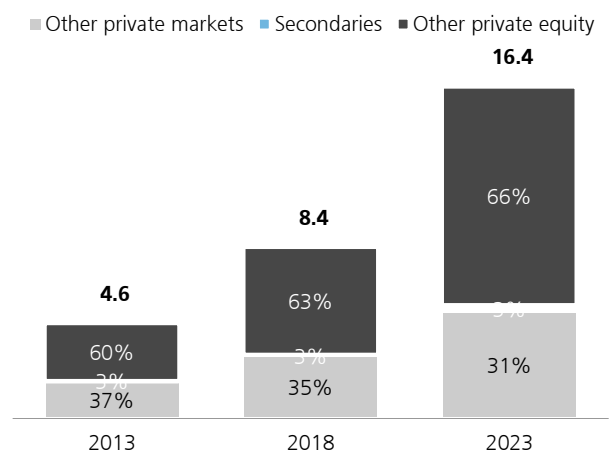
Fig. 1: Illustration of traditional LP secondary transactions



Source: UBS

Fig. 2: Secondaries have grown 3.5x in the last decade

With over USD 465 billion in AUM, secondaries represent 3% of total private markets



Source: Preqin, UBS October 2024.

Performance analysis

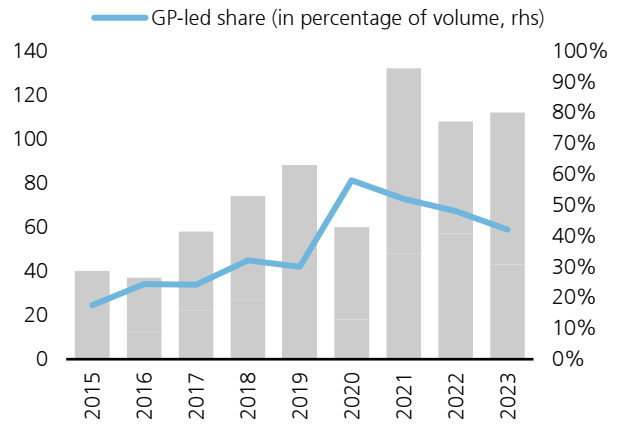
- Secondaries have generated attractive returns for investors with higher IRRs (internal rate of return) but lower TVPI (total value to paid in) multiples versus primary private equity funds (Fig. 4).
- Higher IRRs are the result of secondaries' faster cash distribution, which mitigates the usual drag on performance in the early life of a fund.
- Lower TVPIs—i.e., the multiple earned on cash invested—reflect the more mature nature of the holdings. This also explains why secondaries may not have the same upside potential than primary buyout funds.
- Secondary funds exhibit a lower return dispersion, loss rates and return volatility than primary buyout funds. As such, secondaries are often viewed as a more conservative way to build initial exposure to private markets.
- Secondaries can also be good complements to concentrated primary portfolios that would benefit from extra diversification, return stability, and early distributions.

Secondaries and the business cycle

- Economic stress typically enhances investment deal flow in secondaries and creates an opportunity to acquire assets at greater discounts.
- LPs may be more inclined to sell their stakes into private market funds when they are overallocated to the asset class, either as a result of the “numerator effect”—when private market portfolios significantly outperform publicly listed portfolios, as was the case in 2021—or due to the opposite “denominator effect,” following a significant decline in public valuations, as observed in 2022.
- A lack of distributions—owing to a difficult exit environment—or limited capital availability for new commitments may also offer incentives to LPs to seek liquidity on the secondary market.
- Discounts tend to widen during market dislocations, as LPs' urgent need to sell favors GPs, and the muted outlook raises fear around inflated valuations.
- Conversely, discounts narrow as competition among secondary buyers intensifies, and the quality of the underlying assets improves.

Fig. 3: Secondary transactions have accelerated

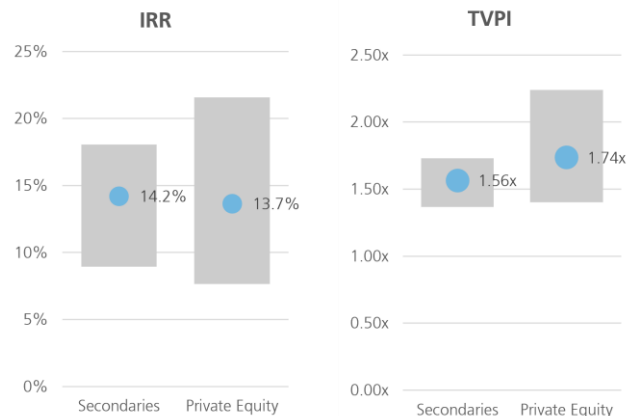
Global secondary transaction volumes, in USD billion



Source: Jefferies H1 2024 Global Secondary Market Review and earlier versions, UBS.

Fig. 4: Compelling IRRs and Multiples

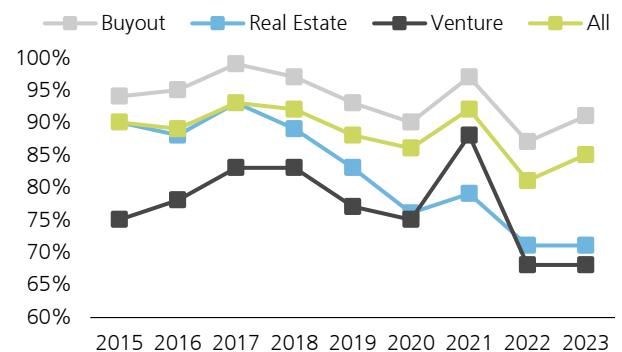
Secondary PE funds vs primary PE funds (1999-2019 vintages)



Source: Cambridge Associates, UBS November 2024

Fig. 5: Narrowing discounts are driven by record levels of available capital and strong public markets

LP portfolio pricing, as % of NAV



Source: Jefferies H1 2024 Global Secondary Market Review and earlier versions, UBS.

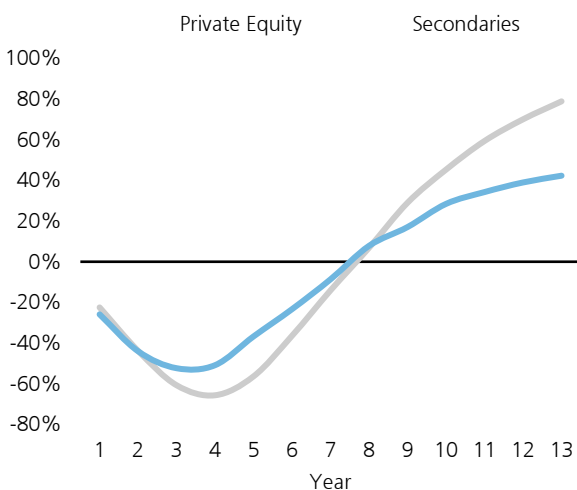
Secondaries in your portfolio

Secondary funds offer diversification benefits and defensive characteristics that are valuable to building private markets portfolios.

- Accelerated exposure: Because they target more mature fund stakes and assets, secondary managers deploy capital quicker than a typical primary fund and thereby provide accelerated exposure to private assets.
- Diversification: Acquired fund interests are typically highly diversified across geographies, strategies, and vintage years, which typically help reduce the variability of returns.
- Reduced blind pool risk: As managers buy mature fund stakes, they can analyze underlying investments more precisely before making an investment decision, therefore reducing so-called blind pool risk.
- Early liquidity and J-curve mitigation: Secondary funds acquire stakes in existing funds or portfolio companies that are close to or are already generating cash flows. As such, secondary funds start distributing capital faster than primary fund investments, and can help mitigate the J-curve effects in a portfolio. Using Pitchbook cash flow data, secondaries recover their cost basis about a year earlier than private equity funds (Fig. 6)

Fig. 6: Secondary funds return capital to investors faster

Net cumulative cash flows as % of commitment



Source: Pitchbook as of November 2022, UBS November 2024.

Risks

While secondaries are more diversified than primary investments, they do entail risks.

- Leverage: Secondaries may use leverage at either the fund or deal level to partially finance secondary transactions.
- Management resources: Funds including multiple LP stakes can have less direct access to asset-level information or the ability to due diligence assets than primary buyout or co-investment funds.
- Limited control: Managers that buy existing LP stakes in a portfolio have a lack of control over exit timing of underlying assets.
- Valuation risk: Deal dynamics in pricing define the success of a transaction. Portfolios are assessed on a quarterly basis, and pricing to NAV can turn out differently between the last quarterly valuation and closing date. Higher discounts to NAV may also indicate distress at asset level.
- Single-asset risk: Funds focused on single-assets like GP-led continuation funds require a more sophisticated skillset to navigate conflicts of interest and the negotiation process between GPs, existing and selling LPs and the new buyer.
- The secondary strategy also remains exposed to other private market risks, including illiquidity, fees, limited control over investment decisions and limited disclosure on underlying assets. Some, but not all of these risks, can be mitigated by partnering with experienced and disciplined secondary managers who can effectively underwrite assets.

Appendix: Select definitions

- **Blind pool:** money collected from several people which is put into a fund and invested for their profit. It is left unspecified which properties are to be acquired.
- **Cash flows:** cash flow is the net amount of cash and cash-equivalents being transferred into and out of a fund.
- **Control provisions:** designed to provide a level of influence over significant operational and business matters.
- **Correlation:** the degree to which the fluctuations of one variable are similar to those of another.
- **Dry powder:** refers to cash reserves kept on hand by a private markets firm to cover future obligations, purchase assets or make acquisitions.
- **Exit:** the time period in which an investor can convert holdings into cash to be liquidated over a designated period of time.
- **Illiquidity premia:** the premium that an investor can demand depending on how difficult it is to convert the underlying security can be converted to cash.
- **Idiosyncratic risk:** risk associated with a narrow set of factors pertaining to a particular company. Risk that has little association with overall market risk.
- **IPO:** the first sale of stock by a private company to the public. Also referred to as an "initial public offering."
- **IRR:** a return method used to evaluate private market investments and reflects the discount rate at which the present value of an investment's future cash flow equals the cost of the investment.
- **J-curve:** illustrates a period of initial negative cash flows (contributions) towards positive cash flows (distributions back to the investor) over a period of time.
- **Junior debt:** loan that ranks below other loans with regard to claims on assets or earnings. In the case of borrower default, creditors who own subordinated debt won't be paid out until after senior debt holders are paid in full.
- **Leverage:** the use of borrowed capital or instruments to increase the potential return (but also potential losses) of an investment, a simple example is a mortgage used in real estate transactions.
- **Leveraged buyout funds:** a private equity strategy using borrowed capital to gain control of a company.
- **Minority stake:** reflects a non-controlling interest that is less than 50% of a particular entity.
- **Multiple expansion:** describes the way a particular valuation metric increases to reflect a higher value assigned to an underlying investment.
- **M&A:** mergers and acquisitions is a general term that refers to the consolidation of companies or assets through various types of financial transactions. M&A can include a number of different transactions, such as mergers, acquisitions, consolidations, tender offers, purchase of assets and management acquisitions.
- **Multiples:** a term that measures some aspect of a company's financial well-being, determined by dividing one metric by another metric. The metric in the numerator is typically larger than the one in the denominator, because the top metric is usually supposed to be many times larger than the bottom metric.
- **Public Market Equivalent (PME):** a method that converts public market returns to a benchmark that can be compared to private market returns.
- **Redemption rights:** gives investors the right to force a company to repurchase their shares after a period of time.
- **Secondary buyout:** describes a sale between private market firms
- **Senior debt:** loans or debt securities that have claim prior to junior obligations and equity on a corporation's assets in the event of liquidation.
- **Spin off:** describes the separation of an independent company from a larger parent.
- **Sponsor:** the general partner in a limited partnership who organizes and signs up investors.
- **Standard deviation:** a measure of the degree to which individual values vary from the distribution mean. The higher the number, the greater the risk.
- **Tag-along provisions:** provides a minority shareholder the right to join in on a sale of a company that is initiated by a majority shareholder.
- **Trade sale/strategic sale:** describes a sale of a business to another business operating in a similar industry.
- **TVPI (Total Value to Paid In):** a return metric that describes the total capital distributed back to the investor + residual value left in the fund divided by invested capital.
- **Unit economics:** a measure of direct revenues and costs on a unit basis for a particular business model.
- **Value add:** describes the operational, business, or structural improvements private market managers seek through underlying portfolio investments.
- **Vintage year:** is the year in which the first influx of investment capital is delivered to a project or company. This marks when capital is contributed by venture capital, a private equity fund or a partnership drawing down from its investors.

Non-Traditional Assets

Non-traditional asset classes are alternative investments that include hedge funds, private equity, real estate, and managed futures (collectively, alternative investments). Interests of alternative investment funds are sold only to qualified investors, and only by means of offering documents that include information about the risks, performance and expenses of alternative investment funds, and which clients are urged to read carefully before subscribing and retain. An investment in an alternative investment fund is speculative and involves significant risks. Specifically, these investments (1) are not mutual funds and are not subject to the same regulatory requirements as mutual funds; (2) may have performance that is volatile, and investors may lose all or a substantial amount of their investment; (3) may engage in leverage and other speculative investment practices that may increase the risk of investment loss; (4) are long-term, illiquid investments, there is generally no secondary market for the interests of a fund, and none is expected to develop; (5) interests of alternative investment funds typically will be illiquid and subject to restrictions on transfer; (6) may not be required to provide periodic pricing or valuation information to investors; (7) generally involve complex tax strategies and there may be delays in distributing tax information to investors; (8) are subject to high fees, including management fees and other fees and expenses, all of which will reduce profits.

Interests in alternative investment funds are not deposits or obligations of, or guaranteed or endorsed by, any bank or other insured depository institution, and are not federally insured by the Federal Deposit Insurance Corporation, the Federal Reserve Board, or any other governmental agency. Prospective investors should understand these risks and have the financial ability and willingness to accept them for an extended period of time before making an investment in an alternative investment fund and should consider an alternative investment fund as a supplement to an overall investment program.

In addition to the risks that apply to alternative investments generally, the following are additional risks related to an investment in these strategies:

- **Hedge Fund Risk:** There are risks specifically associated with investing in hedge funds, which may include risks associated with investing in short sales, options, small-cap stocks, "junk bonds," derivatives, distressed securities, non-U.S. securities and illiquid investments.
- **Managed Futures:** There are risks specifically associated with investing in managed futures programs. For example, not all managers focus on all strategies at all times, and managed futures strategies may have material directional elements.
- **Real Estate:** There are risks specifically associated with investing in real estate products and real estate investment trusts. They involve risks associated with debt, adverse changes in general economic or local market conditions, changes in governmental, tax, real estate and zoning laws or regulations, risks associated with capital calls and, for some real estate products, the risks associated with the ability to qualify for favorable treatment under the federal tax laws.
- **Private Equity:** There are risks specifically associated with investing in private equity. Capital calls can be made on short notice, and the failure to meet capital calls can result in significant adverse consequences including, but not limited to, a total loss of investment.
- **Foreign Exchange/Currency Risk:** Investors in securities of issuers located outside of the United States should be aware that even for securities denominated in U.S. dollars, changes in the exchange rate between the U.S. dollar and the issuer's "home" currency can have unexpected effects on the market value and liquidity of those securities. Those securities may also be affected by other risks (such as political, economic or regulatory changes) that may not be readily known to a U.S. investor.

Appendix

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