

Content Includes:

Unrealized Assets in Tail-End Funds

Over \$190bn in unrealized assets is currently held in vintage 2005 or older buyout, growth and venture capital funds.

Secondary Market Solutions

The secondary market is increasingly providing a solution for managers and investors involved with tail-end funds.

Transactions

A notable 40% of secondary market transactions so far in 2015 have involved 2005 vintage or older funds.

Potential Sellers

Family offices and private sector pension funds are most interested in selling tail-end funds on the secondary market.

Preqin Special Report: Private Equity Unrealized Assets

A Secondary Market Solution?

September 2015





Foreword

The issue of the volume of assets that remains unrealized in mature private equity funds transcends the secondary market and is of increasing concern to LPs and GPs alike, especially as boom-year vintages approach the end of their pre-agreed 10-year lifetime. The prospect of GPs seeking extensions from their LPs is already a reality for some funds and looms for many more.

This trend of ever maturing funds unable to fully realize their assets is occurring in tandem with a growing and maturing secondary market that has seen record fundraising and transaction levels in recent years. Implicit in a bigger market is the increased participation of the limited partner universe; no longer a resort for distressed investors seeking liquidity, the secondary market now serves as a viable tool for the active management of alternative asset portfolios, an avenue for investors to realize value from these mature funds should they see fit. The nature of transactions being completed in the secondary market is becoming more diverse as the market matures; GPs are also utilizing the buoyancy of the secondary market to offer a whole fund liquidity option to their LPs in end-of-life funds.

Preqin's **Secondary Market Monitor** continues to be underpinned by a sustained research effort to unveil and update information on buyers and sellers in the institutional investor universe and the provision of updates on their plans for the secondary market. It also contains information on the investment portfolios of potential sellers and on the universe of tail-end funds. Analysis in this report uses data from Secondary Market Monitor to provide insight on the tail-end fund issue, seeking to quantify the size of the challenge faced by GPs in coming years, and in turn, the opportunity for secondary buyers. It also highlights the ways in which the secondary market is providing solutions to deal with remaining assets in maturing funds.

Contents

Unrealized Assets in Tail-End Funds	3
Secondary Market Solutions for Tail-End Funds	5
Secondary Market Transactions	6
Potential Sellers of Tail-End Funds	7

Secondary Market Monitor: In-Depth Data and Intelligence on All Aspects of the Private Equity Secondary Market

Preqin's **Secondary Market Monitor** online service provides vital intelligence on all areas of the secondary market and is constantly updated by Preqin's team of dedicated analysts through direct contact with institutional investors and fund managers from around the world.

Use **Secondary Market Monitor** to:

- Identify all the key players in the secondary market
- Find firms seeking to buy fund interests
- Find potential sellers of fund interests
- Access details of secondary transactions and all the latest secondaries news

For more information, please visit: www.preqin.com/smm

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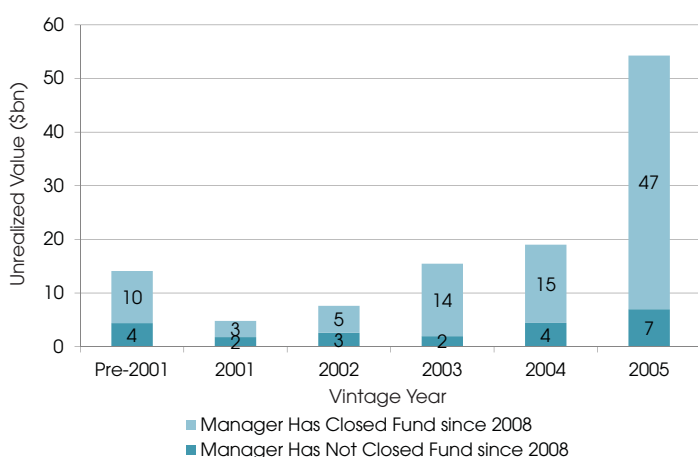
Unrealized Assets in Tail-End Funds

Distributions from private equity funds have improved greatly in recent years as managers have taken advantage of improving market conditions to realize value from remaining assets in their portfolios. This has gone some way to alleviating concerns regarding the overhang of unrealized value in ageing funds; however, the issue has not yet been fully rectified, particularly as funds raised in the boom years of 2005-2008 reach the 10-year mark. Abundant capital and heady prices in those years set the bar high to attain meaningful returns from exiting investments made in that period. The task of attaining value from remaining assets in ageing funds can be a full-time one, specifically for managers that have not succeeded in raising funds of more recent vintages, and particularly since the end of the aforementioned fundraising boom post 2008. Preqin's data indicates that there are 1,326 private equity fund managers still active that are yet to close a fund post-2008 having raised funds prior to that – victims of the selectivity and cautiousness of limited partners. The majority of these (52%) are North America-based managers, while 27% are based in Europe (Fig. 1).

Quantifying Tail-End Fund Assets

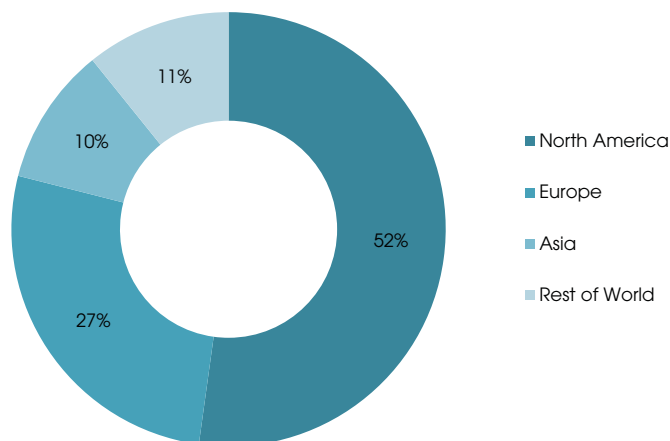
What is the size of the task that lies ahead for managers for their older vintage funds? Fig. 2 illustrates the aggregate remaining value in funds with a 2005 vintage and older, i.e. those that are very close to, or past, their original agreed lifetime, with private equity funds typically having a 10-year term. For buyout & growth capital funds, there remains around \$115bn in these older vintages (as of December 2014), with a notable amount (\$54bn) in 2005 vintage funds. Only 19% of the aggregate unrealized value in 2005 vintage funds and older is managed by firms that have not closed a vehicle since 2008. The total unrealized value in funds of a 2005 vintage and older is less in venture capital funds at \$78bn (Fig. 3); however, a larger proportion of assets (40%) are managed by firms with no recent fundraising success.

Fig. 2: Buyout & Growth Funds: Unrealized Value in Vintage 2005 and Older Funds (As of December 2014)



Source: Preqin Secondary Market Monitor

Fig. 1: Breakdown of Private Equity Fund Managers that Have Not Closed a Fund since 2008 by Location



Source: Preqin Secondary Market Monitor

Unrealized Assets in Tail-End Funds by Geography

As might be expected given the size of the industry, the majority of unrealized assets in buyout, growth & venture capital funds with a 2005 vintage or older is in North America-focused funds; these funds have \$129bn in unrealized assets, as shown in Fig. 4, accounting for 67% of the global total. In these funds, \$37bn in unrealized assets is being managed by firms that have not raised a vehicle since 2008. For Europe-focused buyout, growth & venture capital tail-end funds, \$44bn is currently unrealized, with a smaller proportion (20%) managed by firms with no recent vintages, compared with 29% for North America-focused funds. Fewer unrealized assets are held by Asia- and Rest of World-focused funds of these vintages, with an aggregate unrealized value of \$13bn and \$7bn respectively. These figures reflect the pattern of historical fundraising, with North-America focused funds having raised the most capital in the primary market, followed by Europe.

Fig. 3: Venture Capital Funds: Unrealized Value in Vintage 2005 and Older Funds (As of December 2014)



Source: Preqin Secondary Market Monitor



Future Tail-End Funds

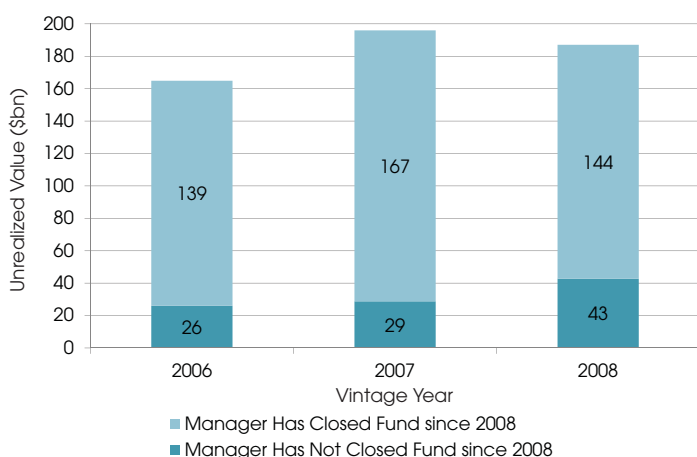
Looking ahead, to funds with a 2006-2008 vintage as they approach the end of their lives, illustrates the task that lies ahead for private equity managers. In total, for buyout & growth funds of these vintages, there is \$548bn in unrealized value (as of December 2014), as can be seen in Fig. 5. Eighteen percent of these assets are managed by firms that have not raised a fund since 2008. For 2007 vintage funds, \$196bn is still held, the most of any of the three vintages. As shown in Fig. 6, \$133bn in unrealized assets is held in venture capital funds of these vintages, of which 32% is managed by managers with no funds of more recent vintages. Even with the distributions pace maintained at current levels, it is likely that funds of these vintages will carry significant unrealized value past the 10-year mark, and could lead to requests for fund extensions for some of them, with LPs having to make a choice between holding on patiently for value to be realized, or seeking alternative options for immediate liquidity.

Fig. 4: Buyout, Growth & Venture Capital Funds: Unrealized Value in Vintage 2005 and Older Funds by Geographic Focus (As of December 2014)



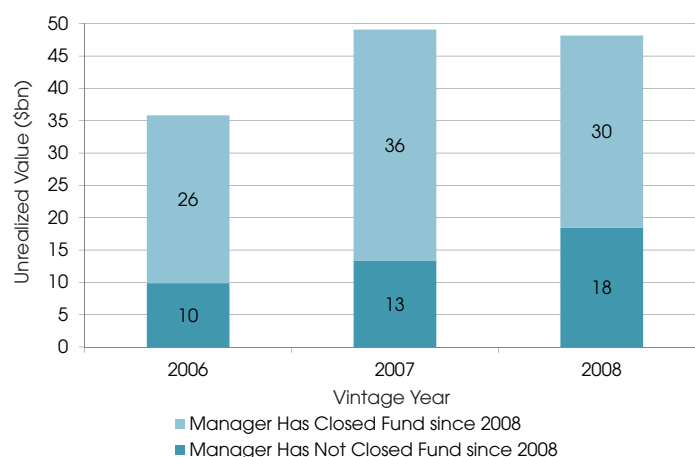
Source: Preqin Secondary Market Monitor

Fig. 5: Buyout & Growth Funds: Unrealized Value in Vintage 2006-2008 Funds (As of December 2014)



Source: Preqin Secondary Market Monitor

Fig. 6: Venture Capital Funds: Unrealized Value in Vintage 2006-2008 Funds (As of December 2014)



Source: Preqin Secondary Market Monitor

New to Secondary Market Monitor: Search for Tail-End Funds

Preqin's **Secondary Market Monitor** now features the option to search for tail-end funds, and can be used to:

- Navigate through mature funds managed by fund managers with no recent vintages (that have not raised a new fund in at least the last seven years)
- Filter tail-end funds by industry, stage, geographic focus, size, or a combination of all of these
- Find out the NAV, performance (IRR) and the quartile ranking of tail-end funds
- Search for potential sellers of interests in these funds specifically by fund name

For more information, please visit:

www.preqin.com/smm



Secondary Market Solutions for Tail-End Funds

An inability to raise recent funds is, perhaps unsurprisingly, related to past performance. Looking again at 2008 vintage funds and older, those funds managed by firms without a successful subsequent fundraise have fared worse, with an average IRR of 0.79% compared with 13.71% for managers that have raised more recent vintages. Returns of these funds are likely below those targeted and managers are unlikely to earn carry, which may motivate them to hold on to the assets in hope of improved performance.

Fundraising struggles also flag another possible issue related to the incentive to realize investments, as the ageing funds are the firm's sole source of income through management fees. However, so called 'GP-led fund restructurings' – where secondary buyers buy into these older vintage funds, offering existing LPs the option to cash in on their investment or retain their interest in the fund with capital typically made available for follow-on investments – are forecasted to grow. In February 2015, Preqin asked over 50 managers of secondaries funds about what types of transactions they completed in 2014; as shown in Fig. 7, a third of respondents indicated that they had completed GP-led restructuring deals. Of these, 77% anticipated completing a similar level of these deals in 2015 as in 2014, while 19% anticipated doing more in 2015.

Manager Motivation

These restructurings significantly tend to be GP-led, with the GP typically engaging intermediaries to proactively find buyers for their fund interests. It is perhaps no coincidence that these processes tend to be pursued in tandem, with a manager's plans to raise capital for a new vehicle driving the desire to find a solution for LPs in the older vintage fund. For the secondary buyer, assessment of the potential of underlying assets is a key part of its decision making, as is the ability to set new fund terms that re-incentivize the manager (such as management fees and hurdle rates). Follow-

on investments to reinvigorate the companies can also take the form of preferred security providing an additional layer of security.

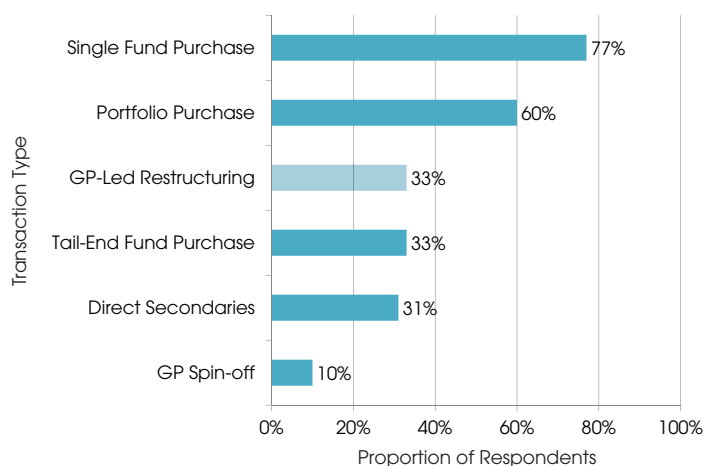
Direct Secondaries

Restructurings are not the only means by which secondary buyers offer solutions to tail-end funds. Direct secondaries involving the purchase of a portfolio of interests of companies in these funds also play a part. Fig. 7 shows that 31% of surveyed managers of secondaries funds completed direct secondary transactions, showing that some secondary buyers are capable of such investments. However, there are also a number of private equity firms that pursue a direct secondaries strategy, utilizing their experience in managing portfolio companies.

Traditional Secondaries

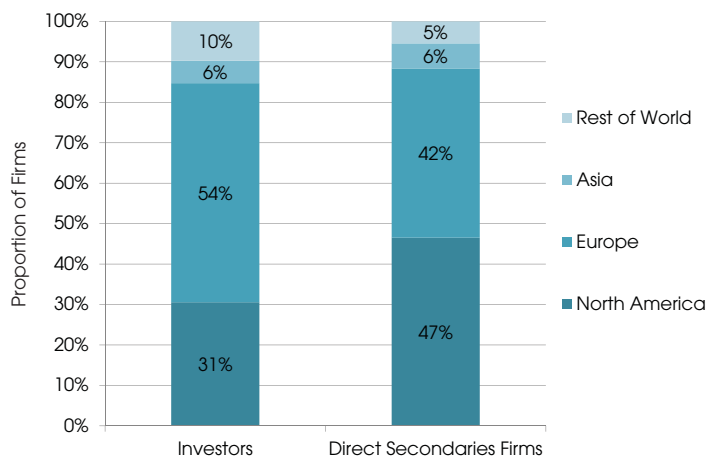
The traditional fund interest purchase also plays a part in providing liquidity for tail-end funds; the LP has the option of being patient with its manager, or deciding to cash in their interest – albeit often at a discount to NAV. However, NAVs are high now, with strong stock market performance feeding through. Even with the better performing managers (that are likely to command secondary prices close to NAV), an LP might decide to sell because it wants to reduce its administrative burden or to alleviate the risk associated with the manager not realizing investments soon. A healthy secondary market affords the LP these options. For the secondary buyer, the price effect (purchasing at a discount to NAV) and distributions effect (capital returned quickly) make such investments particularly attractive. Preqin profiles 85 investors that have stated an interest in purchasing tail-end funds, either through the traditional fund stake purchase route, or by participating in restructurings. Furthermore, there are 113 direct secondaries firms that seek opportunities to buy up portfolio companies in tail-end funds. Fig. 8 shows where these firms are based.

Fig. 7: Breakdown of Transaction Types Completed by Managers of Secondaries Funds in 2014



Source: Preqin Secondary Market Monitor

Fig. 8: Breakdown of Investors and Direct Secondaries Firms Interested in Purchasing Tail-End Funds



Source: Preqin Secondary Market Monitor



Secondary Market Transactions

Secondary buyers remain very well capitalized given the fundraising success experienced in 2012-2014 that saw an aggregate \$69bn raised by private equity secondaries funds. Fig. 9 shows the largest 10 managers by secondaries fund dry powder, estimated by uncalled capital in their secondaries funds. These 10 firms have \$45bn available in dry powder.

Tail-End Fund Transactions in 2015

These amounts are somewhat dwarfed by the total size of assets in mature funds mentioned earlier in the report, illustrating the potential for further growth in the secondary market, especially as evidence shows that LPs and GPs alike have tapped into secondaries liquidity as an avenue to realizing value in their more mature funds. Secondaries transactions involving tail-end funds (funds that are at or close to the end of their life span – 10 years or older in age) are a driver of overall secondaries transaction activity. Estimates by intermediaries of their contribution to secondary activity in H1 2015 range from 30-43%, made up of GP-led deals, direct secondaries deals and traditional fund sales.

Fig. 10, which shows funds involved in secondaries transactions in 2015 YTD by vintage year, corroborates this; 40% of funds involved in secondaries transactions were of a 2005 vintage or older,

Fig. 9: Top 10 Managers of Secondaries Funds by Estimated Dry Powder (Uncalled Capital)

Firm	Headquarters	Uncalled Capital (\$bn)
Lexington Partners	US	11.6
Ardian	France	9.5
Collier Capital	UK	5.9
Goldman Sachs AIMS Private Equity	US	4.2
Strategic Partners Fund Solutions	US	3.7
Landmark Partners	US	3.6
DB Private Equity	UK	1.8
Pantheon	UK	1.6
HarbourVest Partners	US	1.6
Partners Group	Switzerland	1.4

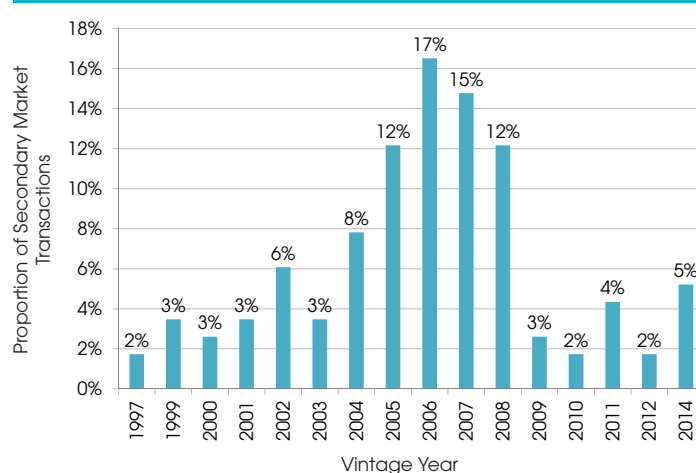
Source: Preqin Secondary Market Monitor

emphasizing their importance to secondaries activity. The chart also shows the contribution of boom-year funds to secondaries activity, with 43% of funds involved in transactions in 2015 of 2006-2008 vintages.

GP Tender Offer

Fig. 11 shows examples of transactions completed in 2015 involving funds of 2005 vintage and older, illustrating the various ways in which the secondary market is providing liquidity for these funds. The typical GP-led deals have tended to take the form of complex restructurings that could involve the creation of new vehicles to acquire existing assets. More recently, a less complex form of transaction has emerged – the ‘GP tender offer’ – where the LPs are simply offered the choice to sell to a GP-elected secondary buyer or remain in the fund. An example of this is KRG Capital Partners: the \$1.5bn private equity firm is offering existing investors in its 2008 vintage buyout fund, KRG Capital Fund IV, the option of selling their fund stakes to an undisclosed buyer. Credit Suisse Private Fund Group is acting as intermediary in the secondaries transaction wherein the unnamed buyer will also be injecting fresh capital into KRG Capital Partners’ latest buyout fund. KRG Capital Fund V is currently in market seeking \$500mn in investor capital.

Fig. 10: Proportion of Secondary Market Transactions Completed in 2015 YTD by Vintage Year



Source: Preqin Secondary Market Monitor

Fig. 11: Examples of Secondary Market Transactions in 2015 YTD Involving 2005 and Older Vintage Funds

Fund(s)	Seller(s)	Buyer(s)	Intermediary	Transaction Type
Perseus Capital; Perseus Market Opportunity Fund; Perseus 2000 Expansion Fund; Perseus 2000	Undisclosed	Centre Lane Partners	Greenhill Cogent	Direct Secondaries
3i Eurofund IV; Carlyle Europe Partners II; Apax Europe VI	National Industries Group	Strategic Partners Fund Solutions	-	Fund Portfolio Sale
Bridgepoint Europe III; Apax Europe VI	Church Pension Group	Pomona Capital	-	Fund Portfolio Sale
EQT IV; IK 2004 Fund ; IK 1997 Fund	Polux Investments	Pictet Alternative Advisors	-	Fund Portfolio Sale
IK 2004 Fund; ECI 8; CBPE Capital Fund VII	Suomi Mutual Life Assurance Company	Mandatum Life Insurance Company	-	Fund Portfolio Sale

Source: Preqin Secondary Market Monitor

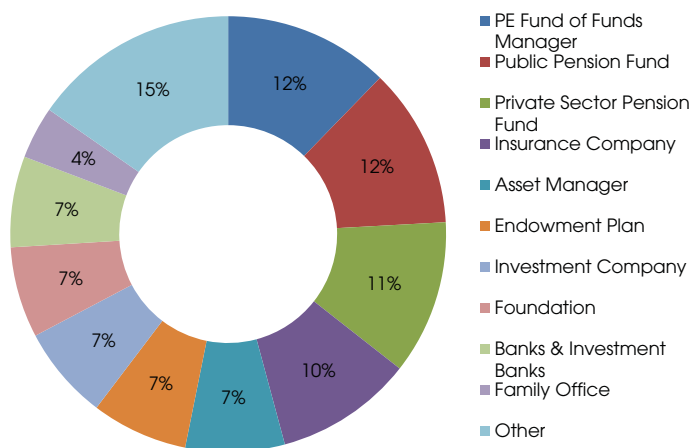


Potential Sellers of Tail-End Funds

Preqin is in regular contact with limited partners around the world in order to identify and update information on potential sellers of private equity fund interests. Preqin currently profiles 488 investors that have indicated an interest in selling private equity fund positions on the secondary market. Fig. 12 shows that a wide variety of firms are interested in using the secondary market to sell fund interests. The largest proportion (43%) of firms interested in selling are based in Europe, while 40% are located in North America (Fig. 13).

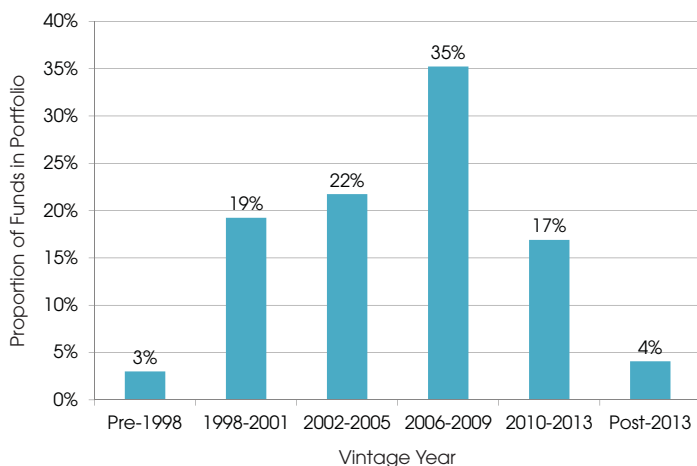
Motivations for selling vary, although portfolio management is a prime reason for most, as well as a desire to attain an attractive price for positions. Investors are also often faced with making a decision on tail-end fund positions, with LPs having to choose between selling or holding onto positions in these funds.

Fig. 12: Breakdown of Potential Secondary Market Sellers of Private Equity Funds by Type



Source: Preqin Secondary Market Monitor

Fig. 14: Breakdown of Potential Secondary Market Sellers of Private Equity Funds by Vintage Year of Funds in Portfolio

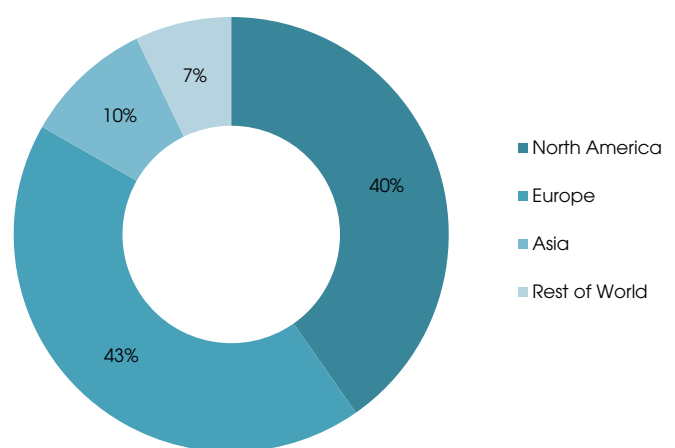


Source: Preqin Secondary Market Monitor

Fig. 14 shows that 44% of existing holdings in closed, unliquidated investments (by number of known commitments) of potential sellers are in funds of a 2005 vintage or older, indicating many investors may seek to sell off tail-end funds in their portfolio. A further 35% of funds held by potential sellers are in funds with 2006-2009 vintages.

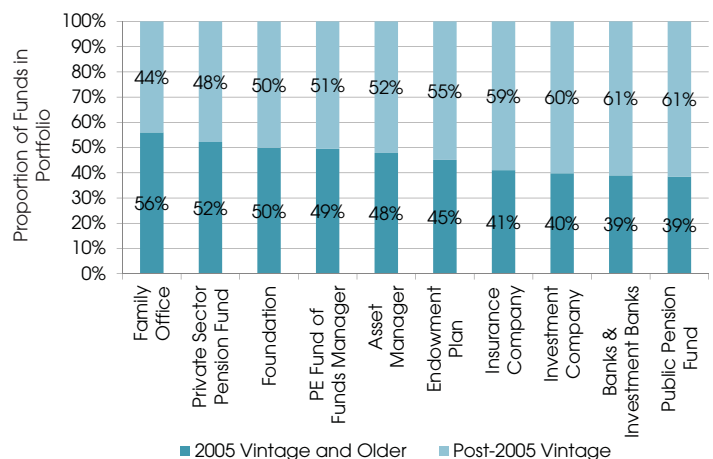
Family offices and private sector pension funds that are interested in selling fund interests are particularly exposed to older vintages; on average, over 50% of the funds in these investors' portfolios are of a 2005 vintage or older (Fig. 15).

Fig. 13: Breakdown of Potential Secondary Market Sellers of Private Equity Funds by Location



Source: Preqin Secondary Market Monitor

Fig. 15: Average Breakdown of Potential Secondary Market Sellers of Private Equity Funds by Type and Vintage Year of Funds in Portfolio



Source: Preqin Secondary Market Monitor

Preqin Special Report: Unrealized Assets

September 2015

Preqin: Global Data and Intelligence

Source potential sellers of fund interests

Find out which investors are looking to sell fund interests on the secondary market. Search for LPs by type, details of the fund interests they are looking to sell, and more.

Combine with Preqin's Investor Intelligence, Real Estate Online, Infrastructure Online and Private Debt Online services to find additional sellers, including LPs no longer investing or that have put their investments on hold, as well as those over-allocated to private equity or real estate.

Find out which LPs are looking to invest in secondaries

Source potential new investors for your latest secondaries vehicle among LPs with an appetite for secondaries funds. Analyze which types of LPs are looking to buy fund interests on the secondary market in the near future. View detailed investment plans for secondary buyers.

Analyze the latest secondaries fundraising activity

See which secondaries funds are in market and which have recently closed. Examine secondaries fundraising over time by target and final close size, strategy and location.

View private equity secondary market transactions and recent news

Explore our archive of previous secondary market transactions to find out which funds have been traded, which LPs have sold fund interests and the buyers of these interests on the secondary market.

Identify key secondary intermediaries

Identify intermediaries involved in the secondary market that match your requirements based on transaction type, intermediary location and client location, as well as size of transactions and types of client represented. View league tables to find out the key players in the market.

Arrange a demonstration today and find out how Preqin's Secondary Market Monitor can help you:

www.preqin.com/smm

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