KEYNOTE INTERVIEW

Split secondaries

Increasing specialisation in the GP-led secondaries market is bringing evolving opportunities for investors, say Pantheon's Amyn Hassanally and Charlotte Morris

Q How are you seeing the GP-led secondaries market evolve and specialise?

Charlotte Morris: GP-led deals have evolved significantly over recent years, going from being a way to deal with so-called 'zombie' funds, to more sophisticated restructurings and tail-end portfolio solutions, through to today's market, where they are an increasingly mainstream strategy within secondaries focusing on high-quality assets, including through the emergence of single-asset deals. As the definition of a GP-led deal has expanded, we are also seeing investors specialising in specific sub-segments.

Amyn Hassanally: There are a number of ways we are seeing investors specialise, including those that focus exclusively on single- or multi-asset deals, tail-end fund specialists, or those that differentiate according to investment size, including managers concentrating on the large and mega end of the market, while others, like Pantheon, have a dedicated focus on the mid-market. There is also differentiation among investors that operate primarily as lead investors and those that mainly do syndicated deals, as well as based on the different financing structures employed, ranging from NAV loans and preferred equity to plain vanilla equity.

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Q Among the various specialisms, are there different requirements in capability and skill of the investor?

CM: Let's take lead versus syndicate as an example. There are very few investors that have the capabilities to lead on these often-complex deals, while there is a larger group of investors that are offered deals on a negotiated, take-it or leave-it basis. As a lead investor, you can shape the transaction, ensure you have strong alignment, and you have the opportunity to protect the bite size you want. You need strong credentials here, as well as the capability to do asset-level due diligence and a deep understanding of deal structuring. We are able to target these lead situations and can leverage our extensive network of primary fund manager relationships globally.

AH: You also need to be of a certain size to lead these deals, which can be very time- and resource-intensive. It is much harder for smaller groups to lead and so they often need to take a smaller piece of a bigger deal as it stands. I think we will start to see some dispersion of returns over time between lead and syndicated positions.

As Charlotte alluded to, we also see a difference between pure-play secondaries players and those with primary investing platforms. At Pantheon, we are able to leverage our primary platform in a number of ways. We have insight into GPs and can assess them more thoroughly because we may have information that isn't provided as part of the deal, which can be very helpful when bidding in competitive situations. Our existing relationships with GPs can also offer an advantage when the GP is selecting the lead buyer – relationships built through primary platforms tend to be deep and long-term, compared with those between GPs and secondaries funds, which I would say are generally more transactional.

Q What about large versus mid-market deals?

CM: Some of the large-cap deals are extremely large and this is where concentration limits can come into play, so lead investors can often only take a small position. Returns also tend to be driven to a certain extent by leverage, while exits are often more focused on IPOs.

We prefer the mid-market space because this is where the relationships from your primary investments can be a differentiator; you benefit from both access and information. The mid-market also tends to be more nimble and higher growth, with returns able to be driven to a greater extent by operating performance. There is more flexibility on exits than in large deals, since the asset may be of interest to strategic buyers, other financial sponsors ready to take the business to the next level, or it may be suitable for an IPO.

Q Do single-asset or multi-asset deals offer the most opportunity?

AH: The growth of single-asset deals has been one of the big stories over the past two years. There are a number of secondaries groups that do both single-asset and multi-asset deals, but we tend to focus more on the single-asset side within our GP-led strategy. Here, the risk-return characteristics are different from traditional secondaries in that the investments are more concentrated and don't mitigate the J-curve in the same way. On the other hand, we feel they can offer better alignment with the sponsoring GP than traditional secondaries and multi-asset deals.

> *"The growth of single-asset deals has been one of the big stories over the past two years"*
>
> **AMYN HASSANALLY**

CM: With single-asset transactions you can also select the most compelling individual companies in which to invest, while with multi-assets there will always be some kind of quality ranking of companies, with those lower down the order potentially diluting top-performers' returns. As Amyn mentioned, you do have to keep an eye on concentration risk; you need to be cognisant of how the asset fits with your wider portfolio and ensure that you are building adequate diversification.

Q How are LPs allocating to this space to achieve their objectives?

AH: We are seeing a mix of approaches. Some LPs have one broad secondaries bucket and are interested in GP-led deals as an interesting source of alpha within that. Other LPs are looking at these deals through a primary buyout or co-investment lens; the returns are comparable even though the duration is shorter – and you can achieve better alignment. You are also investing in a known asset, so you are reducing the risks associated with a blind investment. Then there are opportunistic investors, who are seeking to benefit from the current environment, which, due to demand for liquidity from both GPs and LPs, is generating attractive dealflow and favourable pricing.

Q How do you see the market innovating and developing over the next few years?

CM: GP-led deals will continue to grow – and in the short term this will be driven by that need for liquidity among GPs and LPs that Amyn referenced. But we will also see further innovation, including with specialisations for GP-led deals around sectors and geographies as this area matures. We are also starting to see the development of other forms of capital emerge to support the liquidity needs of GPs and their portfolios, including structured capital and NAV lending.

AH: I see a place for liquidity solutions for the feeder funds that have attracted record amounts of private wealth capital over the past two years or so; that could be an interesting area. I also think we will see best practice evolve in the GP-led market – it is still quite young, after all. In addition to regulatory mechanisms, we are seeing this develop organically across the market through feedback between stakeholders and initiatives such as the Institutional Limited Partners Association's guidance on GP-led deals. ■

Amyn Hassanally is global head of private equity secondaries at Pantheon and Charlotte Morris is a partner on the firm's global secondaries team

Important disclosure

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