Setter

Volume Report H1 2020

First in the secondary market.

Highlights

The Setter Capital Volume Report analyzes global secondary market activity in H1 2020 and covers the following topics:

› Total Volume of Secondary Deals

› Secondary Volume H1 2020 vs. H1 2019

› Breakdown of Volume between Funds and Directs

› Breakdown of Volume by Type of Assets Purchased

› Breakdown of Volume by Geography of Assets Purchased

› Maturity of funds Purchased

› Profile of Buyers

› Number of Deals and Average Deal Size

› Payment Terms

› Execution Risk

› Buyers' Scope of Interest

› Buyers' Return Targets

› Profile of Sellers

› Percentage of Intermediated Deals

› Predicted Secondary Deal Volume for FY 2020

› Changes in the Level of Competition

› Changes in Debt Levels

› Expected Returns of Secondary Purchases

› Expected Distribution and NAV Changes in H2 2020

› General Partners' Approach to the Secondary Market

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The survey

As the secondary market continues to grow and evolve, we seek to take a comprehensive and methodical approach to quantifying the market and identifying trends. Using a survey approach, we asked principals directly the same questions that buyers, sellers, agents and secondary fund LPs often ask us. How much was completed in H1 2020? How much was completed in LBO, venture, real estate, infrastructure and hedge fund secondaries? What are the expected returns and buyer debt levels?

This report summarizes the results of our 30 question survey of the most active global buyers in the secondary market for alternative investments conducted at the end of June 2020. Volume is defined as total exposure (NAV + unfunded in USD) purchased by the respondents, including only deals where a binding agreement was entered into during H1 2020. Please note that all values throughout the report are denoted in USD.

We were pleased by the high response rate, as 96 of the 119 most active and regular buyers in the secondary market agreed to share their confidential results (see partial list of participants on page 27). Given the high response rate, and the fact that all ten of the largest buyers participated, the respondents to our survey represented 89.2% of the transaction volume, making it the most reliable and detailed study of the industry's activities.

Being mindful of response bias, we compared the list of respondents to those who had declined to respond and did not find any obvious or meaningful differences in the known and observed levels of activity between the two groups. We then estimated and charted the total volume, number of transactions, and other reported figures herein by prorating the survey results based on the proportion of small, medium and large buyers that participated.

We hope you find the results interesting and useful. We welcome any questions and would be happy to provide further insights into the results.

H1 2020 in review

After hitting a record $85.4 billion in 2019, secondary market volume dropped precipitously to $20.2 billion in H1 2020. Undoubtedly impacted by the Covid-19 crisis, this represented a 56.1% decrease from the $46.0 billion in secondary volume recorded in the **Setter Capital Volume Report H1 2019.**

Volume was down across all types of alternative investments. The private equity secondary market (funds and directs) decreased 58.5% year over year, to a total of $17.46 billion. Real estate secondaries (funds and directs) were down 53.4% to $890 million, as were hedge fund secondaries which were down 55.1% to $150 million. Private equity fund secondaries were down 60.4% ($10.11 billion in H1 2020 from $25.51 billion in H1 2019. Notably, private debt fund secondaries were down 81.8% ($380 million in H1 2020 from $2.20 billion in H1 2019) and energy fund secondaries were down 93.9% ($63 million in H1 2020 from $1.04 billion in H1 2019). Two bright spots were secondaries of agriculture and timber funds, which saw a 69.5% increase to $270 million in H1 2020, and secondaries of infrastructure funds which were down only 4.7% to $1.44 billion.

Traditional fund secondaries were down 56.0% from $28.58 billion in H1 2019 to $12.58 billion in H1 2020, while direct secondaries were also down 56.2% from $17.43 billion to $7.64 billion (private equity directs were $7.34 billion and real estate directs were $290 million).

While the breadth and number of buyers continued to increase, the most significant activity was driven by the largest buyers in the market. The eight largest buyers, defined as those that deployed more than $600 million in H1 2020, accounted for 50.0% of the market's total volume (vs. 68.6% in H1 2019), while the thirty mid-sized buyers accounted for 38.1% (vs. 24.3% in H1 2019) and the 81 smallest buyers represented 11.9% (vs. 7.1% in H1 2019).

Although 71% of respondents felt buyer competition was similar to H1 2019, 27.5% of respondents felt it was lower, as many buyers pulled back when the Covid-19 crisis broke out. As a means to stay competitive, the use of debt to improve pricing and deal returns continued to be common in the secondary market, however 52.3% of respondents felt that buyers used significantly less leverage in H1 2020 as compared to the prior year.

Agents intermediated 70.4% of deals in H1 2020, versus 75.4% in H1 2019. In terms of dollars, agents intermediated $14.23 billion in deals in H1 2020, which was 59.0% less than they did in H1 2019.

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There were a total of 543 transactions in H1 2020, with an average size of approximately $37.19 million. The number of transactions was down 39.3% from the 895 transactions completed in H1 2019 and the average deal size was down 27.7%, given the drop in large scale deals being completed.

Not surprisingly, 60% of buyers felt that more deals fell apart in H1 2020 versus the preceding six months. Buyers noted that the two main reasons that deals fell apart were that the seller decided not to sell (46%) and adverse economic issues (35%). In the latter case, buyers noted the use of Material Adverse Change (MAC) clauses, due to Covid-19, as a primary mechanism to call off a deal.

The ranks of sellers declined noticeably as many chose to take a wait-and-see approach in light of the pandemic. Managers of funds across LBO, VC, hedge funds, fund of funds and secondary funds accounted for 34.6% of all sellers, as they looked to raise money to support their portfolios or to create liquidity for their LPs. Indeed, 72.5% of the survey respondents felt that meaningfully more GPs coordinated tender offers to their LPs or attempted to liquidate or restructure older funds in H1 2020 as compared to H1 2019. Pensions were the next most active sellers accounting for 33.2%, insurance companies accounted for 4.7%, endowments and charities accounted for 3.4% and sovereign funds accounted for 6.7% of the total volume. Looking forward, most buyers again expect pensions to be the biggest sellers in FY 2020.

From a geographical perspective, North American sellers accounted for the largest proportion of volume in H1 2020 selling $12.04 billion (59.6% vs. 57.4% in H1 2019), whereas Western European sellers sold $4.71 billion (23.3% vs. 19.4% in H1 2019) and Asia-Pacific sellers accounted for about $2.26 billion (11.2% vs. 20.3% in H1 2019). Other geographies such as the Middle East accounted for 5.9% of the total volume in H1 2020, up from 2.9% in H1 2019.

Buyers estimated that NAV valuations will increase 0.1% only and the pace of distributions will decrease 0.6% in H2 2020. These forecasts are less optimistic than those in the **Setter Capital Volume Report H1 2019**, where buyers expected NAV and distributions to increase by 2.3% and 2.5% respectively in the following half year.

Looking forward, buyers expect FY 2020 volume to be $58.30 billion, which would be down 31.7% from the record $85.41 billion transacted in FY 2019.

More Insight.

In the secondary market, knowledge is power.
By providing granular custom portfolio analysis and industry-leading market research, we empower our clients to make the most informed decisions.

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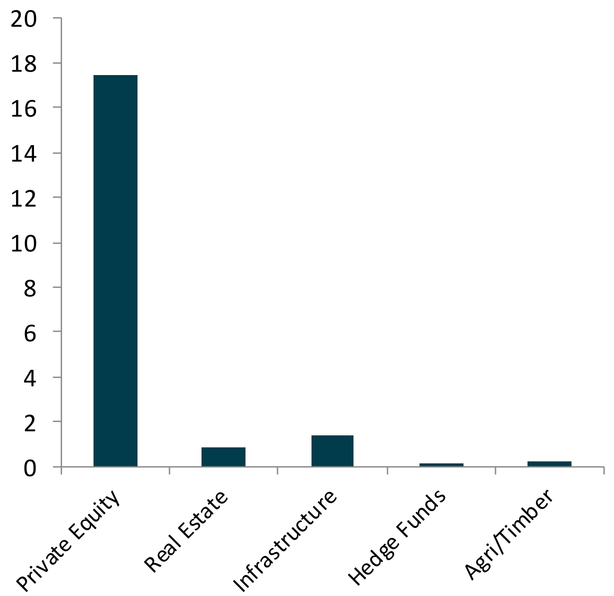
Total volume

Total secondary market volume for H1 2020 was $20.21 billion. This is the volume estimate derived from the 119 secondary buyers surveyed with dedicated secondary efforts and includes 66 secondary funds, 39 funds of funds, 8 hedge funds, 5 investment consultants, and 1 pension. We believe this estimate is reliable as the 96 survey respondents alone reported $18.03 billion of volume in their survey responses. The figure is also conservative, as **it does not include the activity of over 1000 opportunistic and non-traditional buyers,** whose combined activity may be significant. For instance, the activities of all sovereign funds (including ADIA, ADIC, GIC, Temasek, etc.) were excluded entirely, even though some have built teams dedicated to secondary purchases.

Types of assets purchased



Private Equity (Directs[1] & Funds): $17.46 billion (58.5% decrease YoY)

Real Estate (Directs & Funds): $890 million (53.4% decrease YoY)

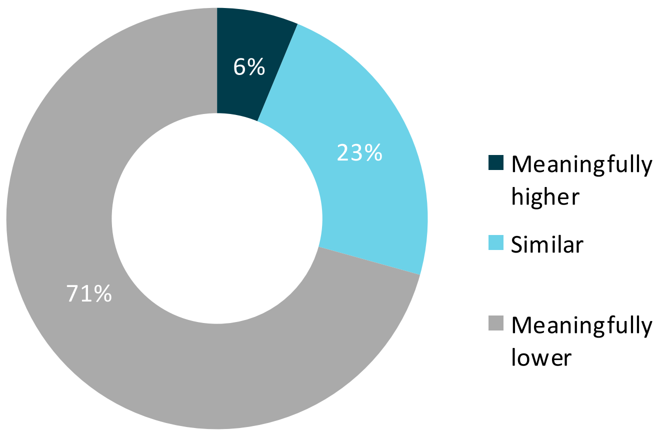
Infrastructure Funds: $1.44 billion (4.4% decrease YoY)

Hedge Funds: $150 million (55.1% decrease YoY)

Agriculture/Timber Funds: $270 million (69.5% increase YoY)

[1] Direct include fund recapitalizations and restructurings, fund liquidations, and purchase of single minority stakes and co-investments.

H1 2020 volume vs. H1 2019 volume

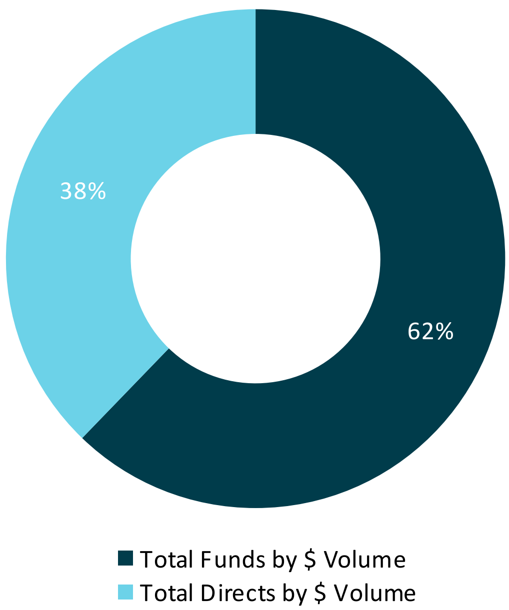


Undoubtedly a result of the Covid-19 crisis, H1 2020 volume decreased 56.1% compared to H1 2019, which was $46.01 billion.

Not surprisingly, 70.7% of survey respondents felt their volume was significantly lower while only 6.3% felt their volume was higher.

Assets purchased

Funds vs. Directs[1]



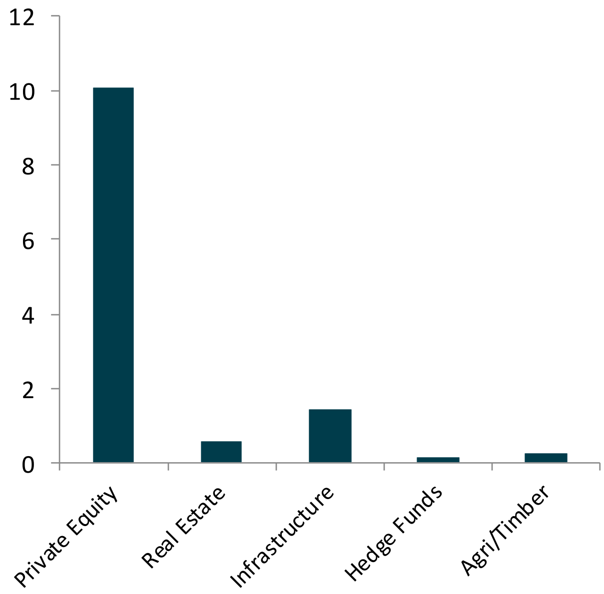
Fund secondaries decreased 56.0%, from the $28.58 billion recorded in H1 2019 to $12.58 billion in H1 2020. Direct secondaries[1] likewise decreased 56.2% from $17.43 billion in H1 2019 to $7.65 billion in H1 2020.

As a proportion of total volume, Direct secondaries went from 37.0% in H1 2019 to 38.7% in H1 2020.

Survey respondents estimated that the split between fund and direct secondaries in 3 years would be 61.3% funds and 38.7% directs.

[1] Direct secondaries include fund restructurings, tender offers, and purchases of single minority stakes and co-investments.

Breakdown of fund secondaries



Private equity fund purchases totaled $10.11 billion (60.4% decrease YoY)

Real estate fund purchases totaled $600 million (44.0% decrease YoY)

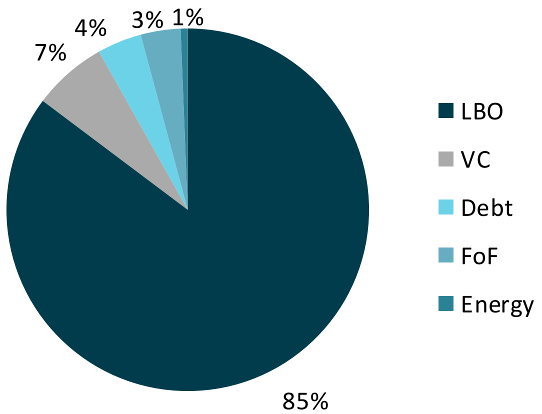
Infrastructure fund purchases totaled $1.44 billion (4.4% decrease YoY)

Hedge fund purchases totaled $150 million (55.1% decrease YoY)

Agriculture/Timber fund purchases totaled $270 million (69.5% increase YoY)

Types of funds purchased

Private equity funds



LBO – $8.62 billion
(Down 55.0% YoY from $19.18 billion)

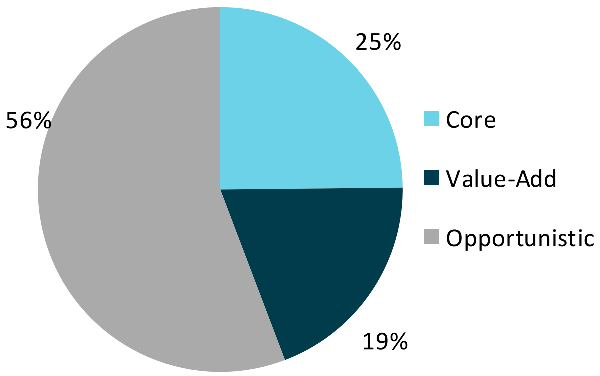
VC – $670 million
(Down 68.6% YoY from $2.12 billion)

Debt – $401 million
(Down 81.8% YoY from $2.20 billion)

Fund of Funds – $360 million
(Down 62.7% YoY from $970 million)

Energy – $63 million
(Down 93.9% YoY from $1.04 billion)

Real estate funds



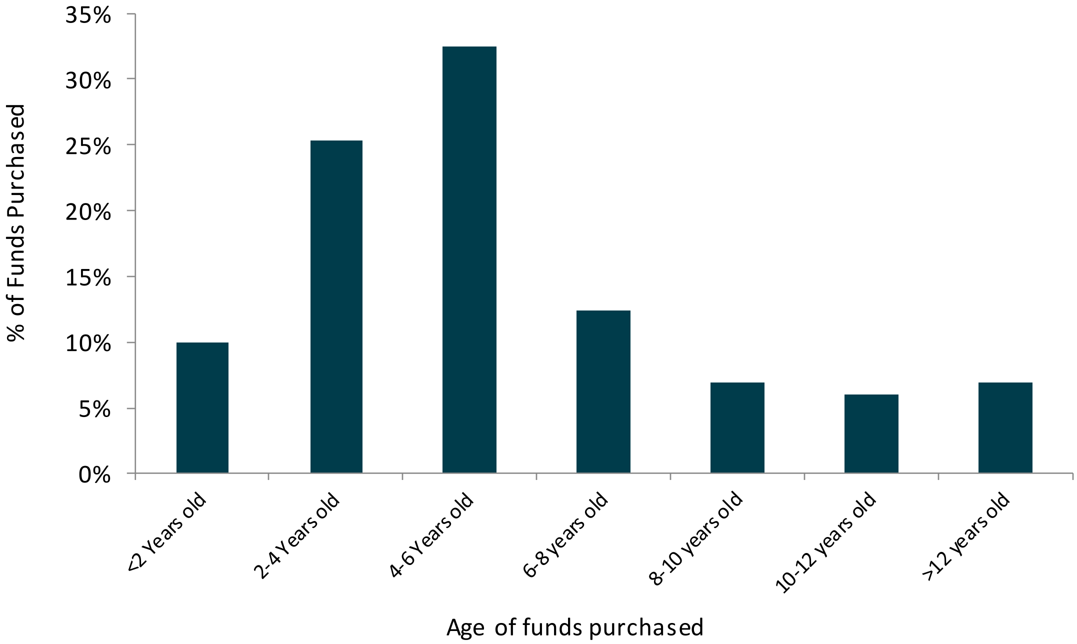
Core – $149 million
(Down 51.5% YoY from $310 million)

Value-Add – $116 million
(Down 56.1% YoY from $260 million)

Opportunistic – $334 million
(Down 32.9% YoY from $500 million)

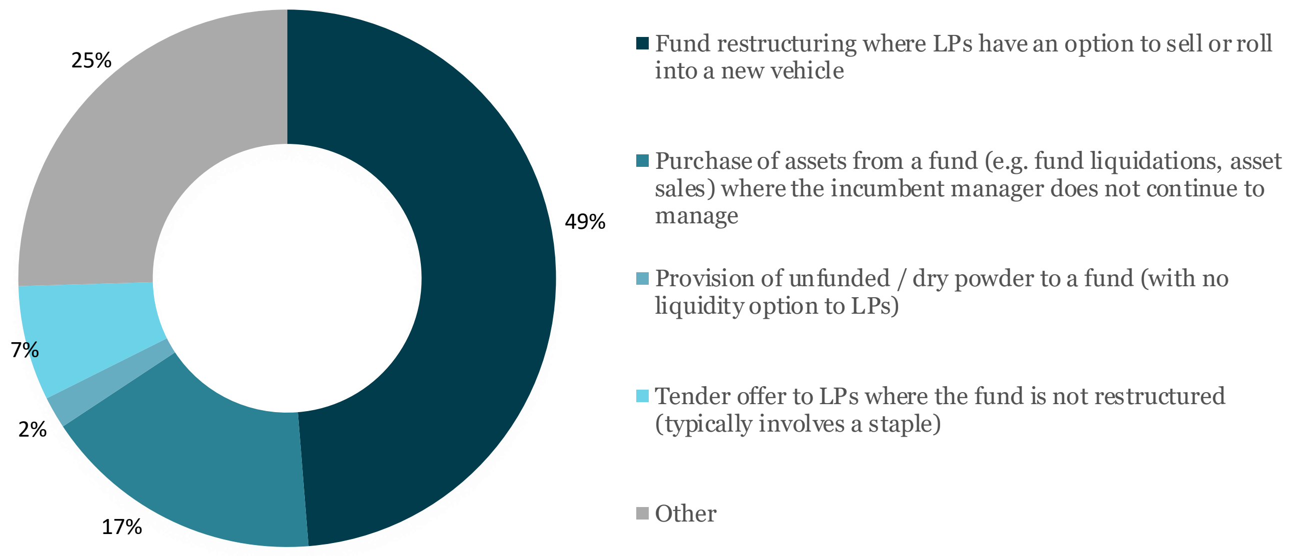
Maturity of funds purchased

As illustrated below, buyers bought funds across various vintages, whether as a portfolio or on a single line basis. The average fund purchased was 5.52 years old.

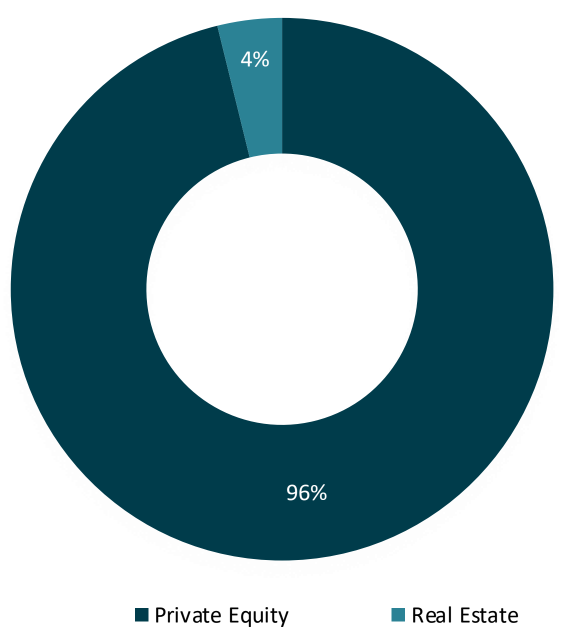


Types of direct secondaries

Types of direct deals completed by buyers

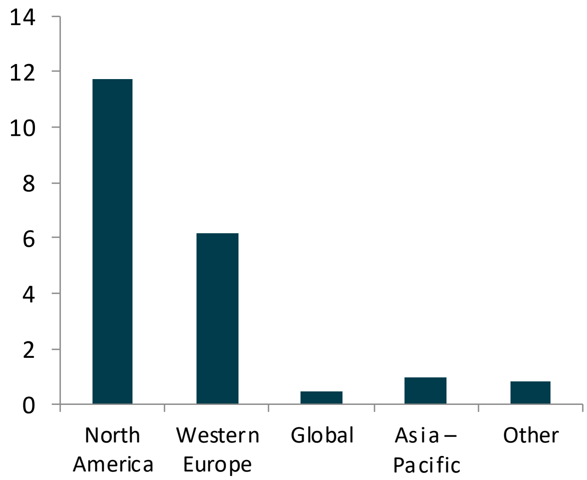


Private equity directs vs. real estate directs



Private equity directs and real estate directs accounted for 96.2% and 3.8% respectively of the total directs volume.

Geography of assets purchased



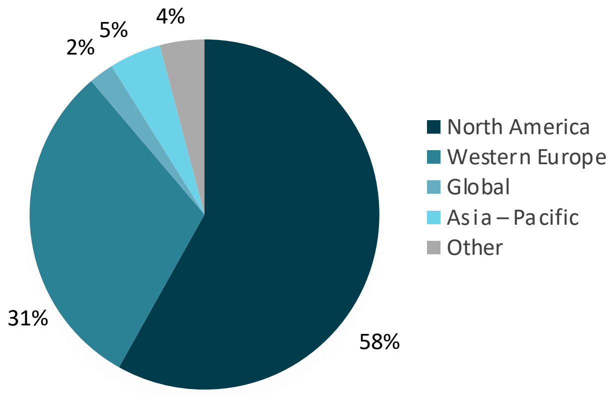
North American and Western European focused funds/directs accounted for the vast majority of assets purchased in H1 2020:

North America – $11.75 billion
(Down 61.6% YoY from $30.58 billion)

Western Europe - $6.20 billion
(Down 35.6% YoY from $9.63 billion)

Global – $460 million
(Down 79.4% YoY from $2.26 billion)

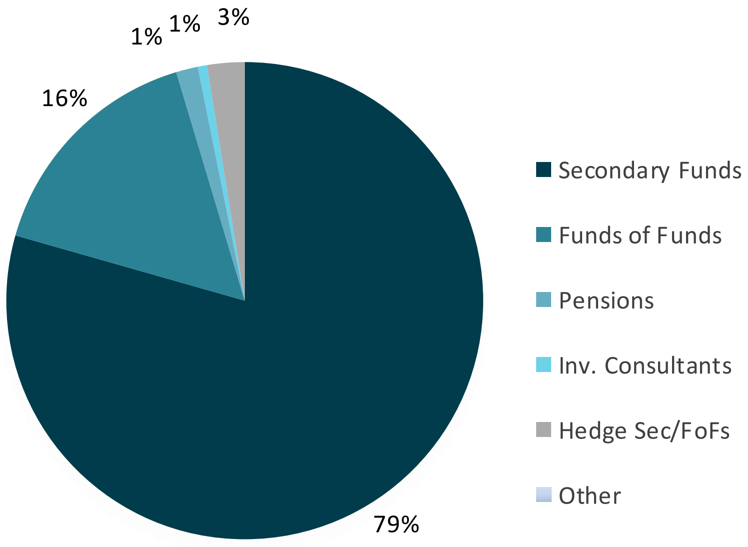
Asia-Pacific – $970 million
(Down 68.5% YoY from $3.07 billion)



In terms of percentage, North America focused funds and directs accounted for 58.1% of total volume, Western European funds and directs accounted for 30.7 % and Asia-focused funds and directs accounted for 4.8% of sales.

Profiles of buyers

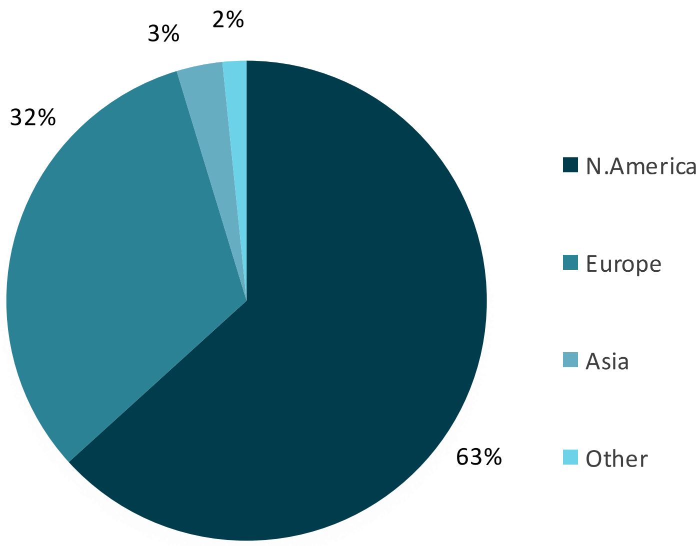
Type of buyers



Secondary funds were again the most active buyers in H1 2020, accounting for 79.4% ($16.05 billion) of total purchases while funds of funds accounted for 16.0% ($3.23 billion).

Please note: over 1,000 non-traditional buyers were not included in our survey and the resulting estimates.

Location of buyers[1]



North American buyers transacted the most (63.3% of total volume) in H1 2020, up as a percentage from 58.3% total volume in H1 2019.

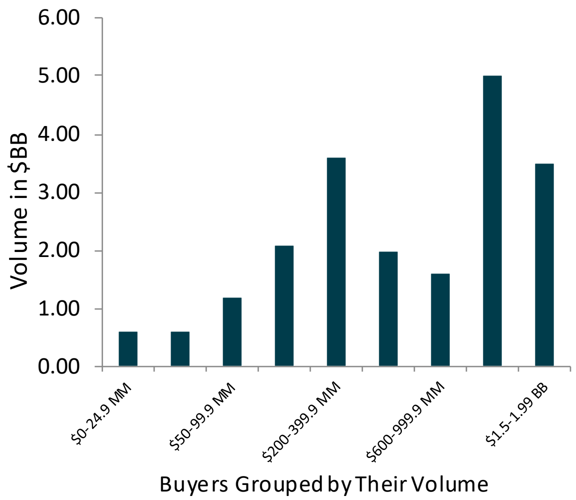
European buyers accounted for 32.0% of total volume in H1 2020, which was lower than H1 2019 (39.7%).

[1]Location is based on head office location.

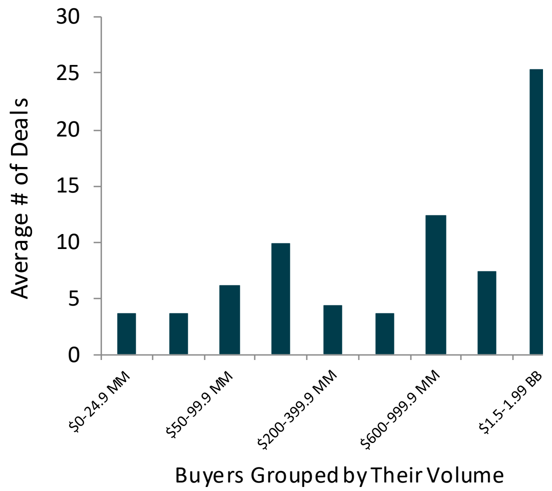
Activity levels of small, medium and large buyers

Applying the survey respondents' dollar volume and transaction numbers, while taking into consideration the proportion of small, medium and large buyers that did not participate, we estimated the market share of small, medium and large buyers as follows:

Volume distribution by size of buyer



Avg. number of deals by size of buyer



8 large buyers (defined as those that deployed $600 million or more in H1 2020) purchased $10.1 billion, representing approximately 50.0% of total volume across 92 transactions with an average deal size of $109.94 million. This was a meaningful decrease from H1 2019, where large buyers accounted for 68.6%.

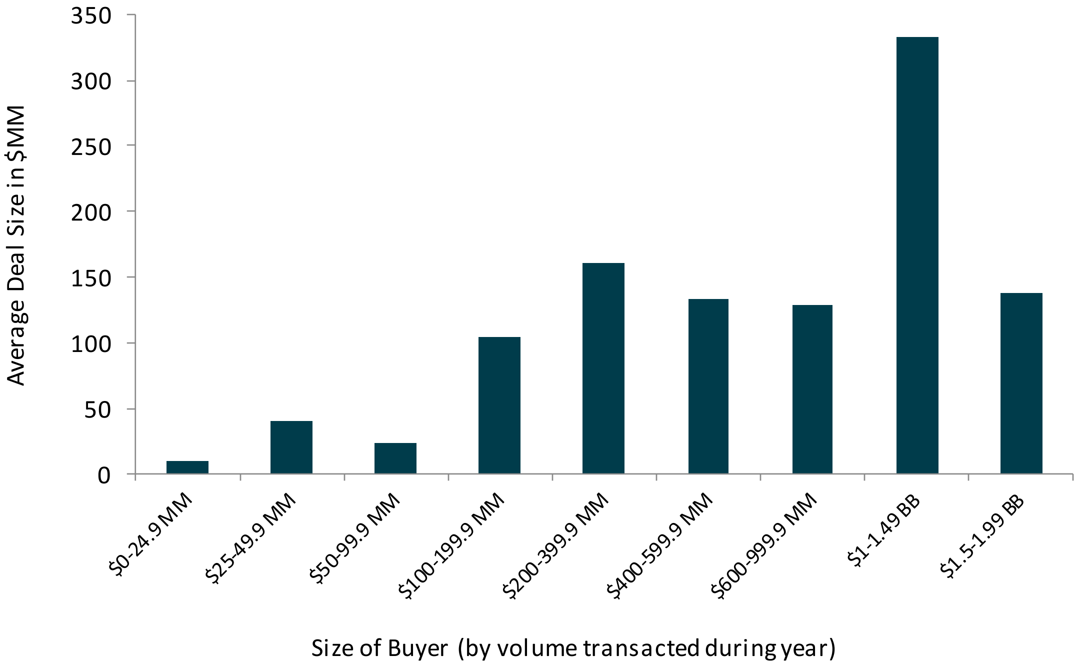
30 medium-sized buyers (defined as those that deployed $100 million to $600 million in H1 2020) purchased $7.7 billion, representing approximately 38.1% of total volume across 169 transactions with an average deal size of $45.42 million. This was a large increase from H1 2019, where they accounted for 24.3%.

81 small buyers (defined as those that deployed less than $100 million in H1 2020) purchased $2.41 billion, representing approximately 11.9% of total volume across 282 transactions with an average deal size of $8.55 million. This was an increase from H1 2019, where they accounted for 7.1%.

Number of deals and average deal size

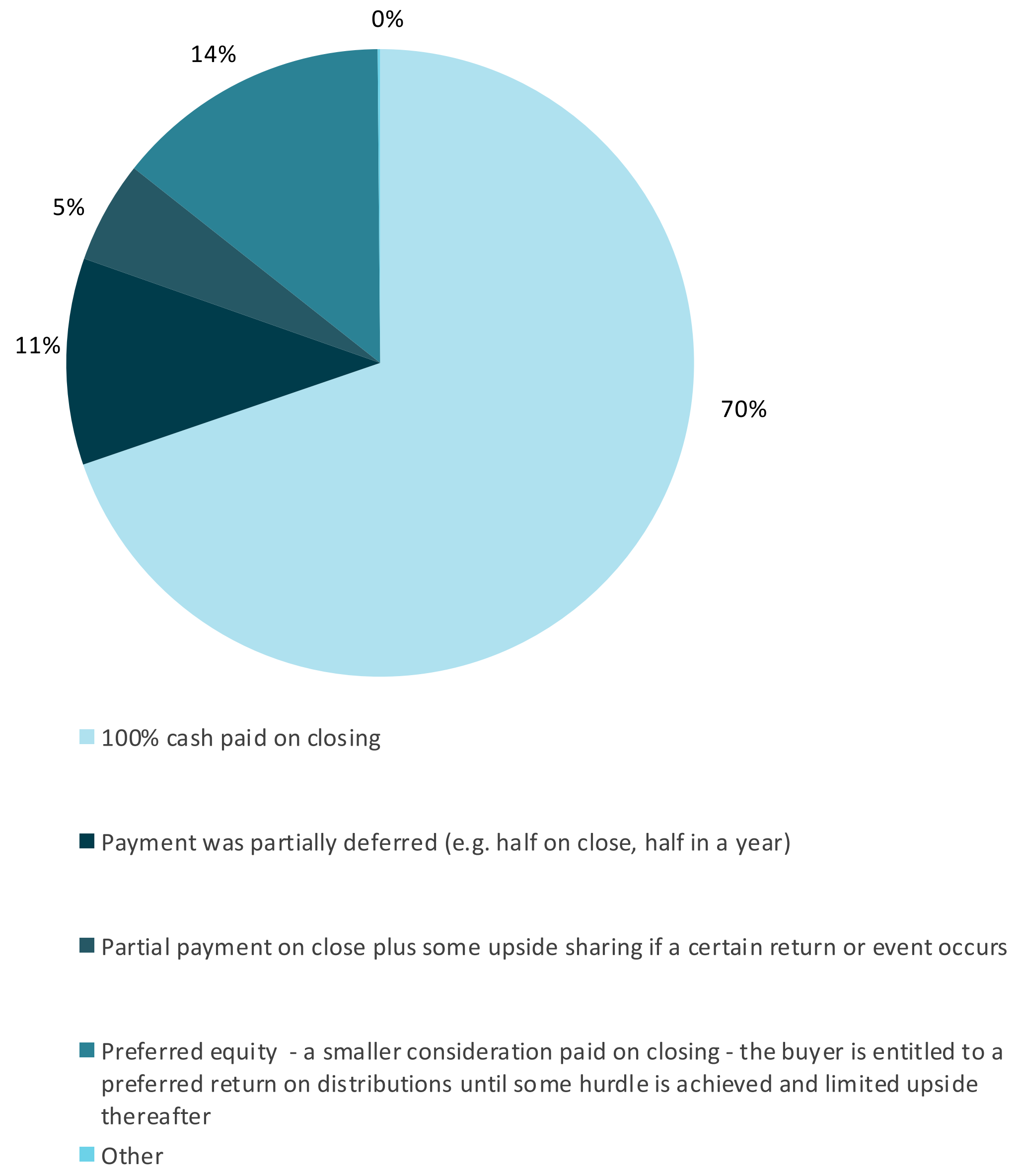
Buyers completed 543 transactions in H1 2020 across the entire secondary market for alternative assets, with an average size of approximately $37.19 million. The number of transactions decreased 39.3% from 895 transactions in H1 2019, while the average deal size likewise decreased 27.7% from $51.40 million in H1 2019.

Average deal size by size of buyer



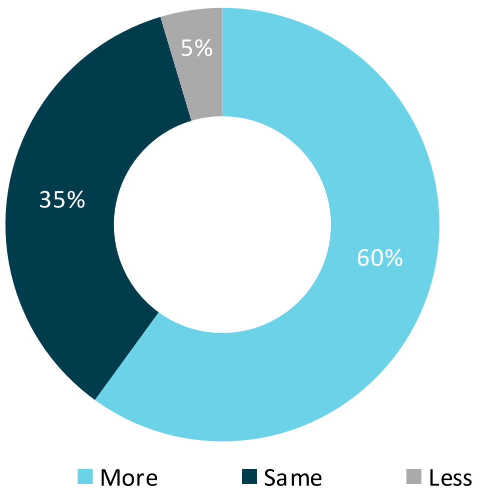
Payment terms

Although for 69.7% of their deals, buyers paid 100% cash on closing, 30.3% of deals involved other payment terms or structuring as outlined below.



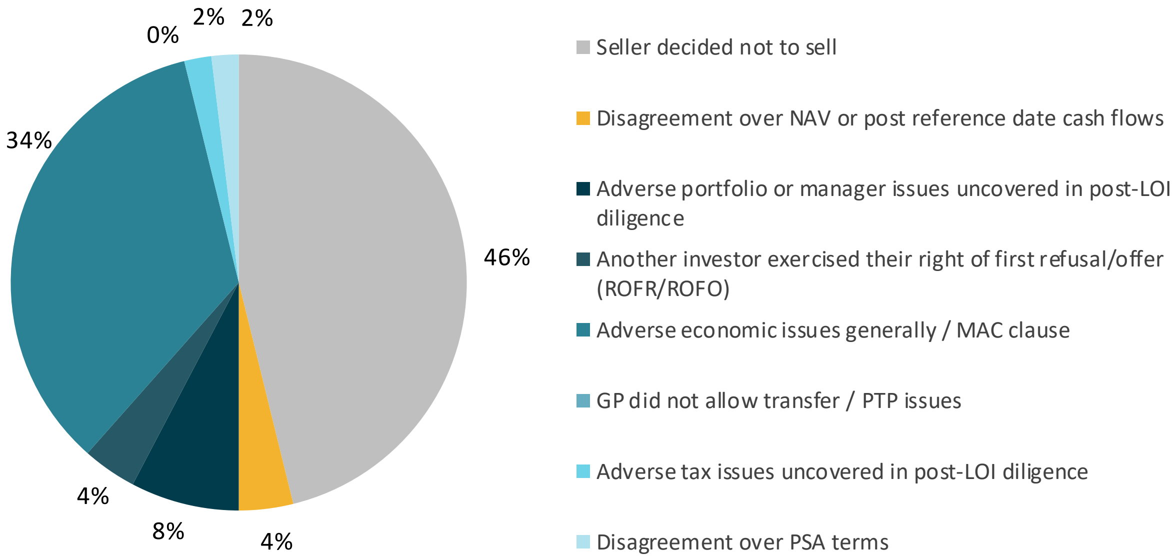
Execution risk

Percentage of deals that fell apart in H1 2020 versus H2 2019



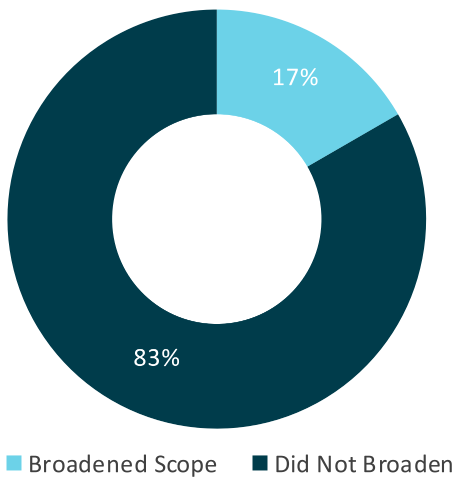
60% of respondents had a higher proportion of their deals fall through in H1 2020, versus the prior 6 month period.

As illustrated below, the two main reasons that deals fell apart were that the seller decided not to sell (46%) and adverse economic issues (35%). In the latter case, buyers noted the use of Material Adverse Change (MAC) clauses, due to Covid-19, as a primary mechanism to call off a deal.



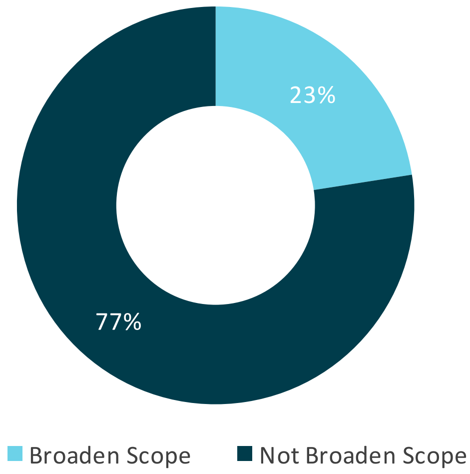
Buyers' scope of interest

Buyers that broadened their focus in H1 2020



16.7% of participants broadened their secondaries focus in H1 2020 to include buying other alternative investment types (e.g. infrastructure, real estate, direct secondaries, etc.).

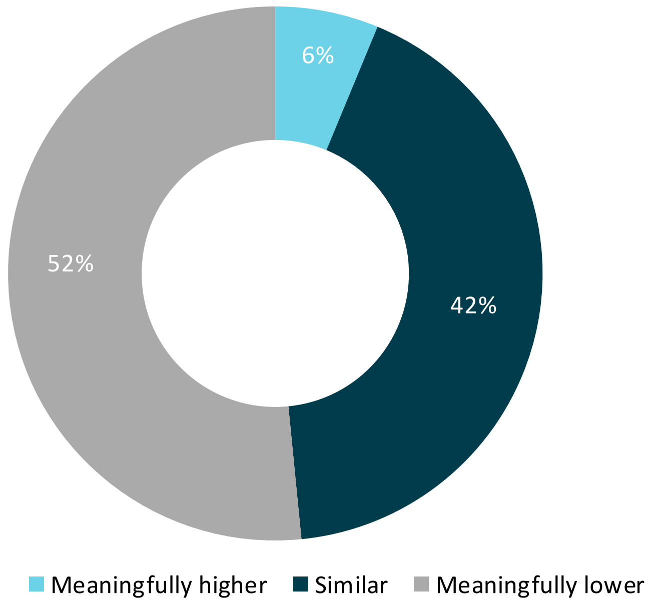
Buyers that intend to broaden their focus in H2 2020



22.5% of participants plan to broaden their secondaries focus in H2 2020 include buying other alternative investment types.

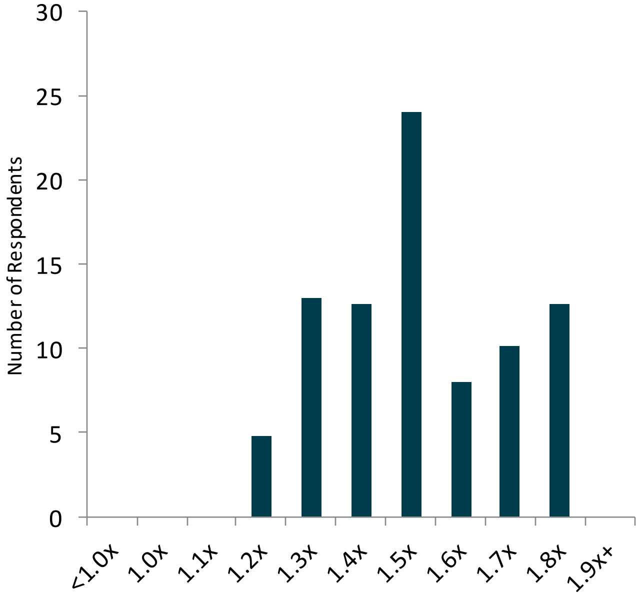
Leverage and returns

Level of debt used by buyers in H1 2020 vs. H1 2019



52.3% of respondents believed the level of debt used by buyers had decreased significantly in H1 2020. 41.5% felt it was the same and 6.2% felt it was more.

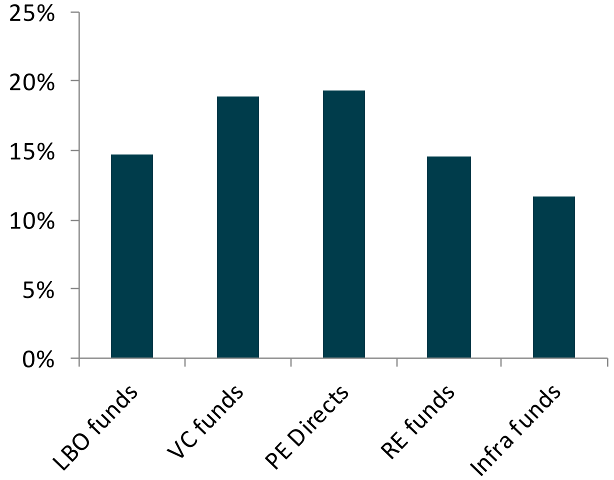
Expected multiple for secondary deals completed in H1 2020



Respondents predicted that the average gross multiple for secondary deals completed in H1 2020 would be 1.49x, which was higher than the 1.42x multiple buyers expected from deals completed in H1 2019.

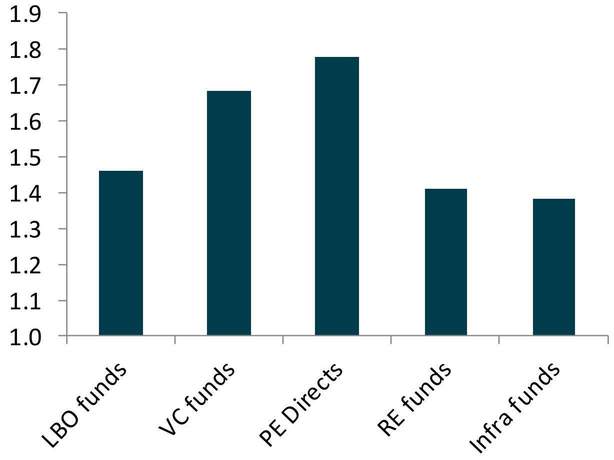
Buyers' return targets

Targeted IRRs on secondary purchases



When underwriting new purchases, buyers estimated their peers' average targeted IRR to be 14.7% for LBO funds, 19.0% for VC funds, 19.3% for PE directs, 14.5% for real estate funds and 11.7% for infrastructure funds.

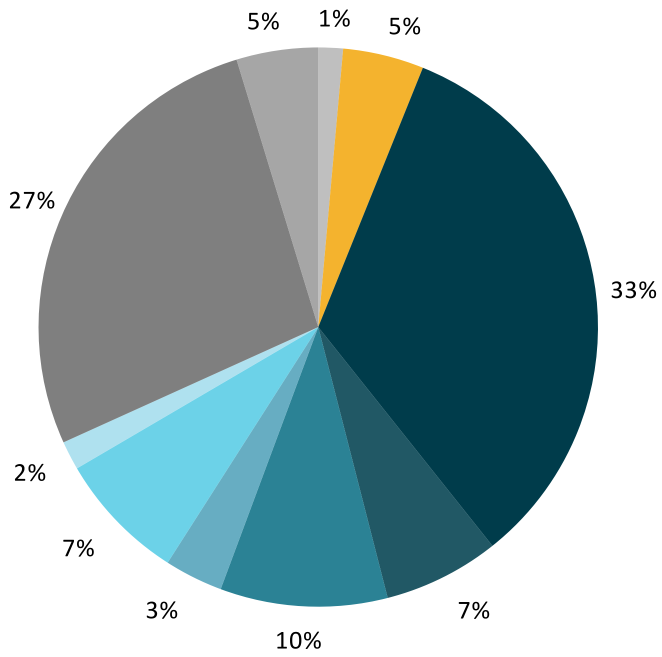
Targeted multiples on secondary purchases



On average, buyers estimated their peers' targeted multiples to be 1.46x for LBO funds, 1.68x for VC funds, 1.78x for PE directs, 1.41x for real estate funds and 1.38x for infrastructure funds.

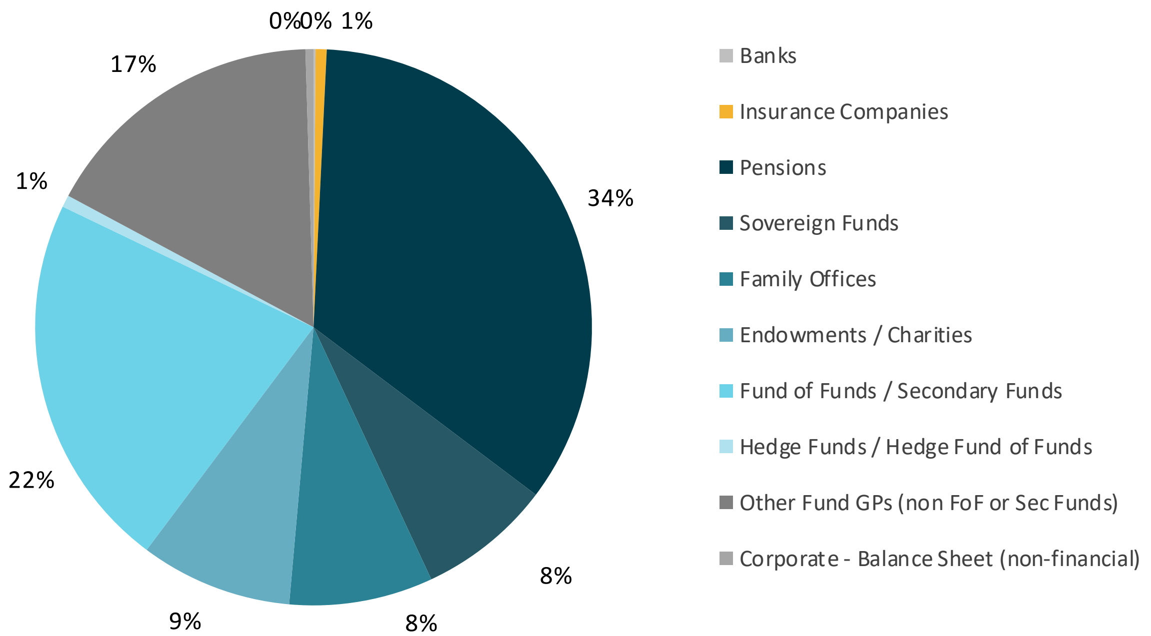
Seller profiles

Types of sellers in H1 2020



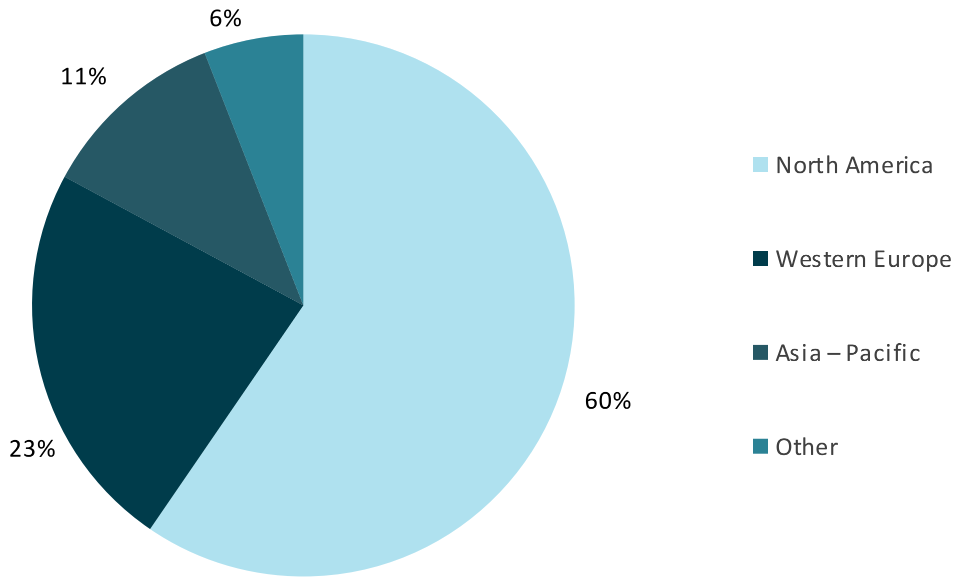
Pensions and GPs (that are not fund of funds or secondary funds), were the most active sellers in H1 2020 making up 33.2% and 27.0% of the H1 2020 volume, respectively. Most buyers expect Pensions to be the biggest sellers again in H2 2020 (34.5% of total transaction volume).

Expected sellers in FY 2020

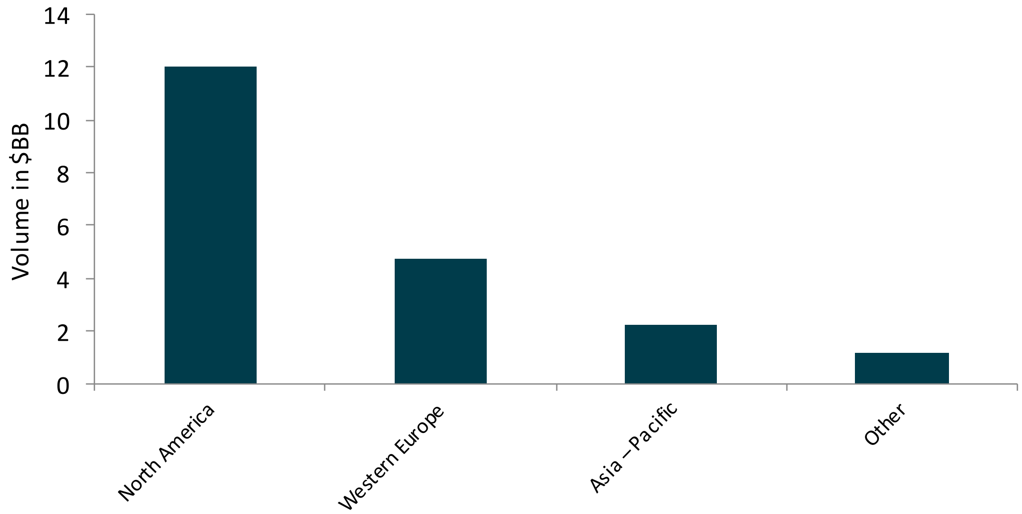


Seller location

Geography of sellers

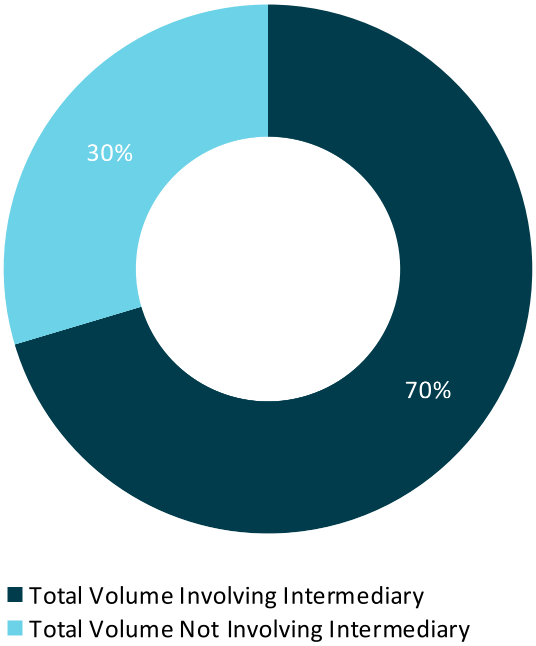


In terms of the location of sellers, North America accounted for the majority of volume in H1 2020. North American sellers sold $12.04 billion (59.6% vs. 57.4% H1 2019), whereas Asia-Pacific sellers sold $2.26 billion (11.2% vs. 20.3% in H1 2019). Western European sellers accounted for 23.3% of the total volume up from 19.4% in H1 2019. Other geographies, such as the Middle East accounted for 5.9% of the total volume in H1 2020, up from 2.9% in H1 2019.



Intermediation and level of competition

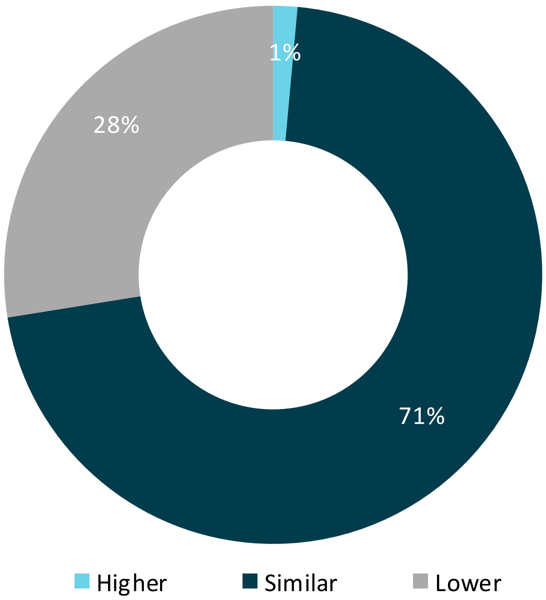
Volume of intermediated transactions



Approximately $14.23 billion (70.4%) of total secondary volume involved an intermediary, on either the buy or sell-side, which was notably lower than H1 2019 where it was $34.71 billion (75.4%).

In terms of volume, agents intermediated $20.48 billion less in deals as compared to H1 2019, representing a marked decrease of 59.0%.

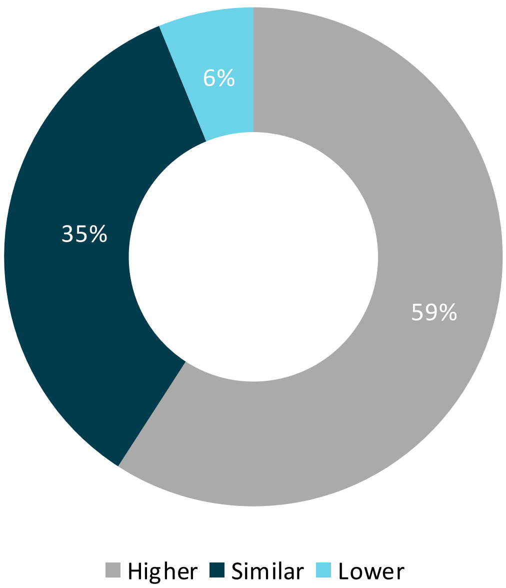
Buyer competition for deals in H1 2020 vs. H1 2019



71.0% of respondents felt buyer competition in H1 2020 was similar to H1 2019, while only 1.4% felt buyer competition was significantly higher. On the other hand, 27.5% of survey respondents felt buyer competition was lower in H1 2020.

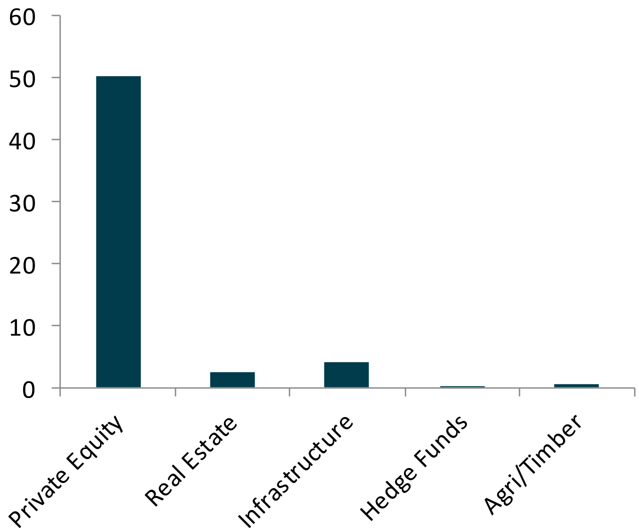
Projected volume for FY 2020

How H2 2020 volume will compare to H1 2020



59.1% of respondents felt that their H2 2020 volume will be meaningfully higher than H1 2020, 6.2% felt it would be meaningfully lower, while 34.7% of the respondents felt that it will be similar.

Predicted volume for FY 2020

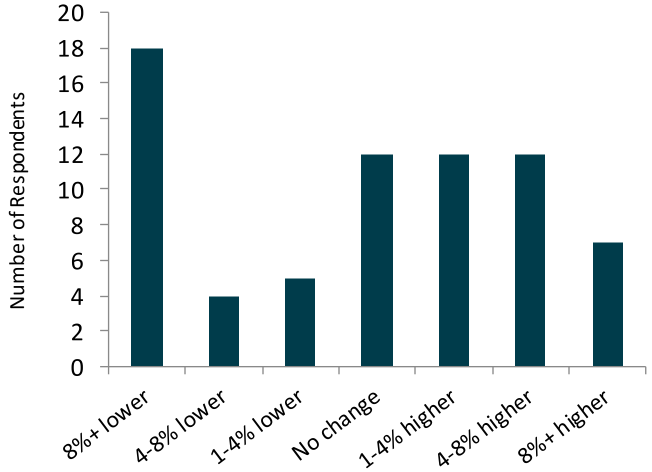


Respondents predicted total volume for FY 2020 to be $58.30 billion, which would represent a 31.7% decrease from the $85.41 billion transacted in FY 2019.

Assuming proportions do not change in FY 2020, this suggests private equity volume will be $50.26 billion in FY 2020, real estate will be $2.57 billion, infrastructure will be $4.15 billion, hedge funds will be $70 million, and agriculture & timber will be $430 million.

Expected distribution and NAV changes in FY 2020

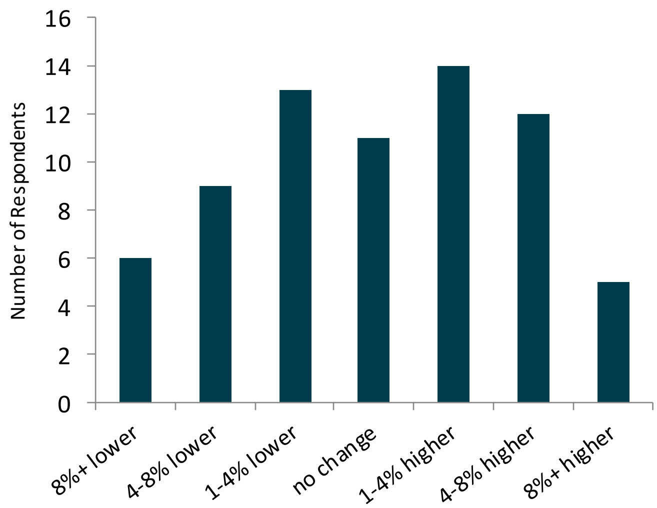
Distribution pace in H2 2020 vs. H1 2020



Respondents expect the pace of distributions in H2 2020 to be lower than H1 2020 as the average response suggests an expected decrease of 0.6%.

Respondents are less optimistic than they were in H1 2019, when they expected the pace of distributions to be up 2.5%.

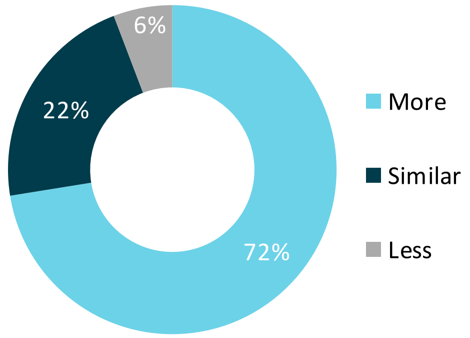
Change in NAV in H2 2020 vs. H1 2020



On average, respondents expect NAV valuations to increase marginally by 0.1% in H2 2020 compared to H1 2020. This is noticeably lower than H1 2019 when respondents expected NAVs to increase by 2.3% in the upcoming year.

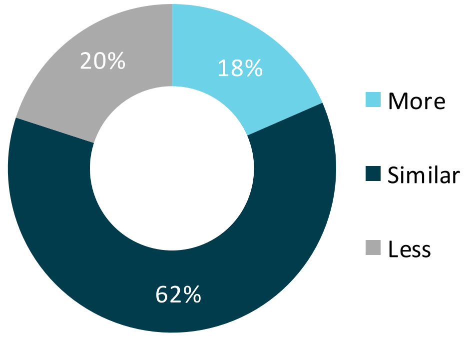
General partners' approach to the secondary market

Liquidations and restructurings in H1 2020 vs. H1 2019



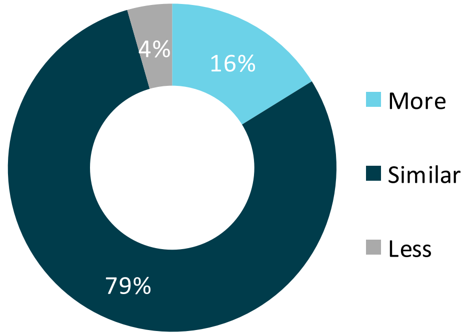
72.5% of respondents felt that meaningfully more GPs attempted to liquidate or restructure older funds in H1 2020 compared to H1 2019.

Staples sought by GPs in H1 2020 vs. H1 2019



62% of respondents felt that a similar number of GPs sought staples in H1 2020 as compared to H1 2019.

GP restrictiveness on transfers in H1 2020 vs. H1 2019



Most respondents felt that GPs' restrictiveness on transfers did not change in H1 2020 compared to H1 2019.

Select respondents

50 South Capital
Aberdeen Standard Investments
Access Capital
Adams Street Partners
Alpinvest Partners
Altamar Capital
Ant Capital Partners
Arcano Capital
Argentum
Bex Capital
Blackrock Private Equity Advisors
Capital Dynamics
Central Park Group
Cipio Partners
Coller Capital
Commonfund Capital
Corbin Capital Partners
Flexstone Partners
FlowStone Partners
Fort Washington
Glendower Capital
Glouston Capital Partners
Golding Capital Partners
Grosvenor Capital Management
Hamilton Lane
HarbourVest Partners
Headlands Capital
Hollyport Capital
HQ Capital
Idinvest Partners
Industry Ventures
Intermediate Capital Group
Israel Secondary Fund
Jasper Ridge
Jeneration Capital
Kline Hill Partners
Knightsbridge Advisers
Landmark Partners
LGT Capital Partners
Mantra Investment
Mercer Investment Management
Mercury Partners
Metropolitan Realty
Morgan Stanley
Neuberger Berman
Newbury Partners
NewQuest Capital Partners
North Sky Capital
Northleaf Capital
Oddo BHF Private Equity
Optimize Capital Partners
Pantheon Ventures
Partners Group
Pathway Capital
PineBridge Investments
Pomona Capital
Portfolio Advisors
Private Advisors
RCP Advisors
Roc Partners
Schroder Adveq
Stafford Capital
StepStone Group
Strategic Partners
Sturbridge Capital
Sweetwater Capital
Top Tier Capital Partners
TR Capital
Tyrus Capital
UBS Asset Management
Unigestion Ltd.
Vintage Ventures
W Capital
Warana Capital
Whitehorse Liquidity Partners
Willowridge Partners

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The Setter Liquidity Rating™ A unique rating system that allows buyers, sellers and creditors to assess the relative liquidity of over 7000 different fund families.

The Setter Volume Report™ and the Setter Price Report™
Two semi-annual reports that provide the most comprehensive and accurate assessments of the secondary market. Data is based on pricing of over 2000 funds and a survey of over two thirds of the most active secondary buyers globally.

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