Private Equity Analyst

Secondary Bids Improve But Deal Volume Still Down

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Secondary investors may have predicted a record year for deal volume in 2009, but so far their ship has yet to arrive.

Secondary deal volume for fund interests is down by nearly half for the first five and half months of this year, compared to the same period last year, despite the fact that prices increased modestly since the first quarter, according to a report from secondary intermediary NYPPEX LLC.

"Although prices improved in the second quarter, they are still too low for many LPs," said Managing Member Laurence Allen. ""We see many LPs sitting on the sidelines waiting for prices to improve another 30% into the 60s on average (as a percentage of NAV) before selling."

The median secondary bid across all sectors increased to 43% of net asset value as of June 1, up from 36% of NAV as of March 31, and roughly in line with overall median bid as of Dec. 31, according to the report from the Greenwich, Conn., firm.

The second quarter pricing data was based on $2.1 billion in bids and surveys of more than 50 secondary buyers between April 1 and June 1.

Venture capital funds continue to command the highest median bids at a little more than 55% of NAV as of June 1, according to the report. Median bids for buyout funds were a little less than 43% of NAV, while median bids for fund of funds ranked last at just over 35% of NAV.

However, improved pricing wasn't enough to drive more deal flow. Through June 1, estimated global secondary volume hit $4.1 billion, a 51% drop from the $8.3 billion estimated global secondary volume over the same period in 2008, according to the report.

A significant percentage of what closed in the second quarter appeared to consist of non-core assets, such as Asian venture capital funds, real estate funds, direct investments, fund of funds and loan participations, the report stated.

During the second quarter, the firm also saw more GPs sell interests that they seized from defaulting LPs, a shift from the approach they took during 2000 to 2003, when capital call defaults last peaked. At that time, firms typically financed the capital calls, wrote them off or assigned the interests to other LPs on a pro-rata basis. The firm predicts that interests with outstanding capital calls held by institutions will reach 9% in the second half of this year, compared to 6.4% as of June 1, 2009, the report said.

That said, NYPPEX expects deal flow to increase significantly during the second half of this year, as the volume of capital calls pick up, putting investors under greater liquidity pressure and prompting more to become active sellers. The firm predicts that secondary volume for limited partnership interests could increase to $27 billion by year-end, compared to $20 billion in 2008, according to the report.

"Prospective sellers should consider making available portfolios to advisors, who can opportunistically offer and sell interests at attractive prices over time," Allen said.

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