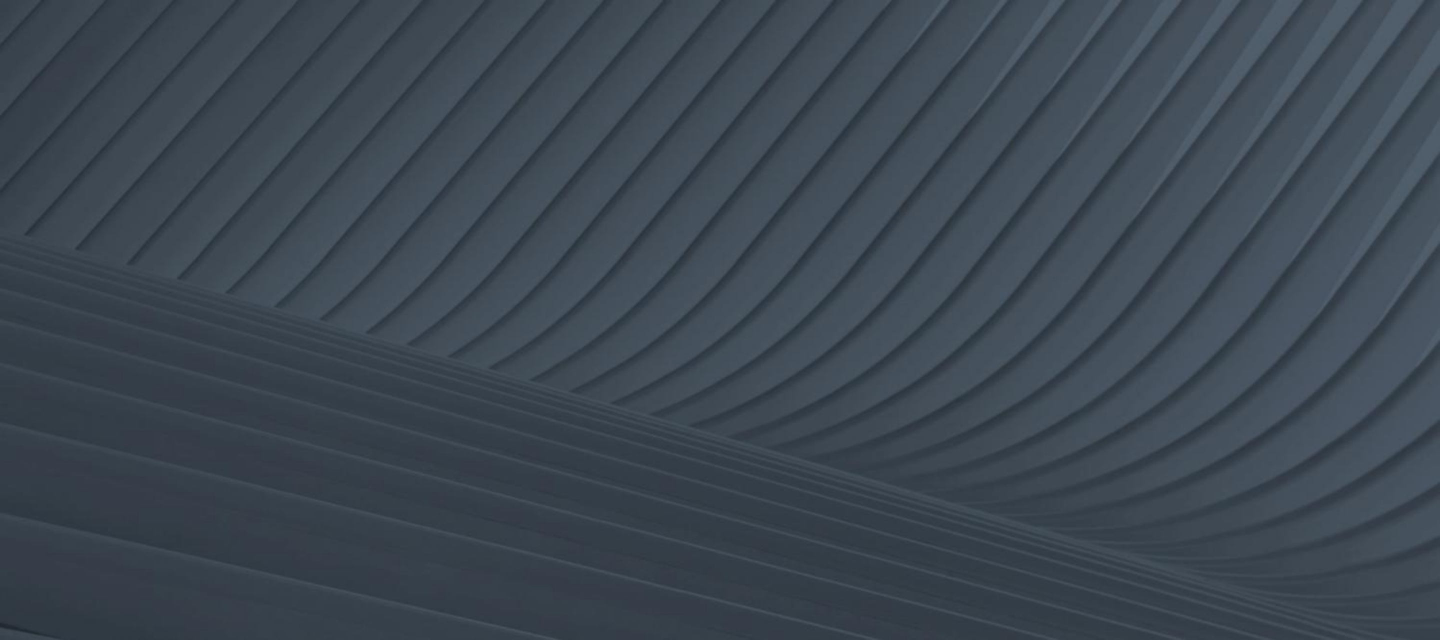
Missing: $52 Billion in Distributions

Analyzing the slowdown in secondary fund distributions since 2021

Please see disclaimer for calculation of “Missing Distributions.”



The past two years have been challenging for private equity. Inflation, interest rate hikes, war and a banking crisis have all impacted both valuations and realizations.

In this paper, we focus on the pace of distributions since 2021 across private equity, with a specific emphasis on secondary funds. While it is widely known that there has been a slowdown in exits, we wanted to examine the cash flows coming from secondary funds compared to other private equity strategies.

Historically, one of the main purposes of secondary funds has been their ability to accelerate distributions for investors. How have they performed in this regard, particularly over the last two years?

Private Equity Distributions have Slowed

In 2021, we saw unprecedented exit activity across private equity, particularly from technology funds. In contrast, the last two years have been characterized by a dramatic slowdown in market activity.

EXITS HAVE SLOWED DRAMATICALLY SINCE 2021

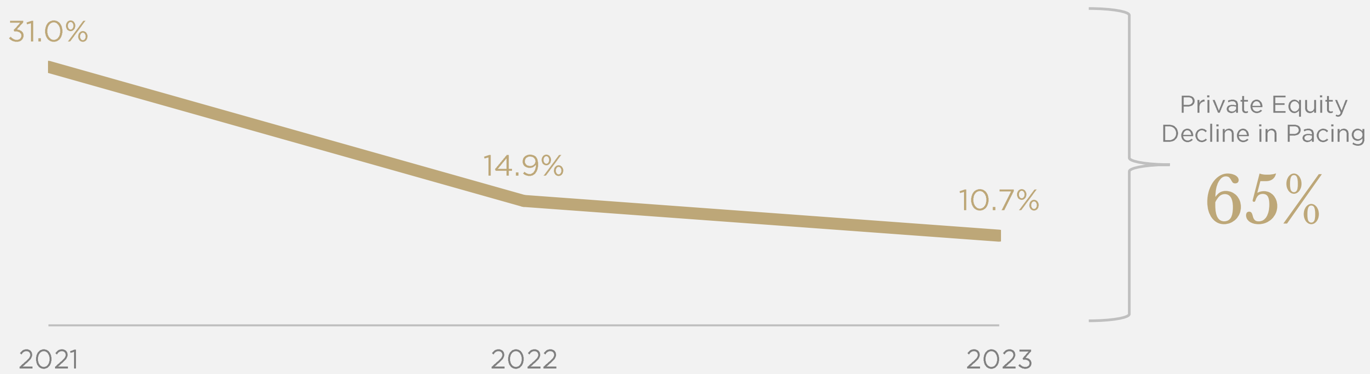
M&A[1]	IPOs[2]
▼47%	▼73%

Consequently, the rate of distributions across private equity funds fell considerably as well.

Average distributions across private equity dropped from around 31% of NAV in 2021 to 11% of NAV in 2023, representing a 65% decline.[3]

Private Equity Distributions

As a % of Beginning NAV[3]



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[1]White & Case. Change in global M&A activity by value between 2021-2023. [2]EY Global IPO Trends, Q1 2024. Change in global IPO activity by proceeds since 2021. [3]Overbay analysis of Pitchbook Data. 2021 and 2022 distribution figures based on FY figures. 2023 distributions figure based on TTM Q3 2023.

Secondary Fund Distributions have Really Slowed

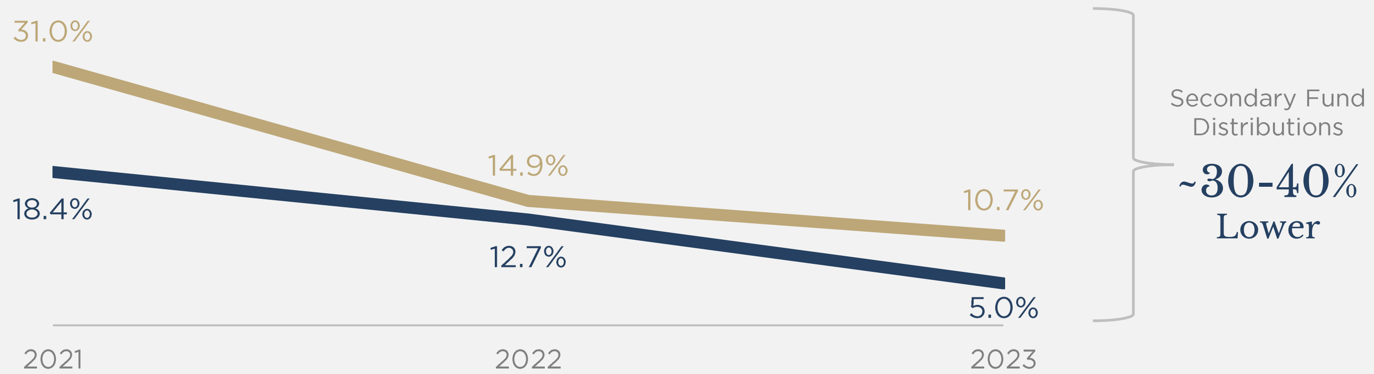
The slowdown in exits over the past two years has impacted all private equity strategies—and secondary funds are certainly not immune to these forces. However, and perhaps surprisingly, secondary funds have distributed significantly less than other private equity strategies on average.

From 2021 to 2023, while private equity distribution pacing dropped by 65%, secondary fund distribution pacing dropped by over 70%. Even focusing solely on post-investment period secondary funds (pre-2019 vintage) yields a remarkably similar conclusion.[1]

Overall, secondary fund distributions were almost 40% lower than the average private equity fund over this period.

Private Equity vs. Secondary Fund Distributions

As a % of Beginning NAV[1]



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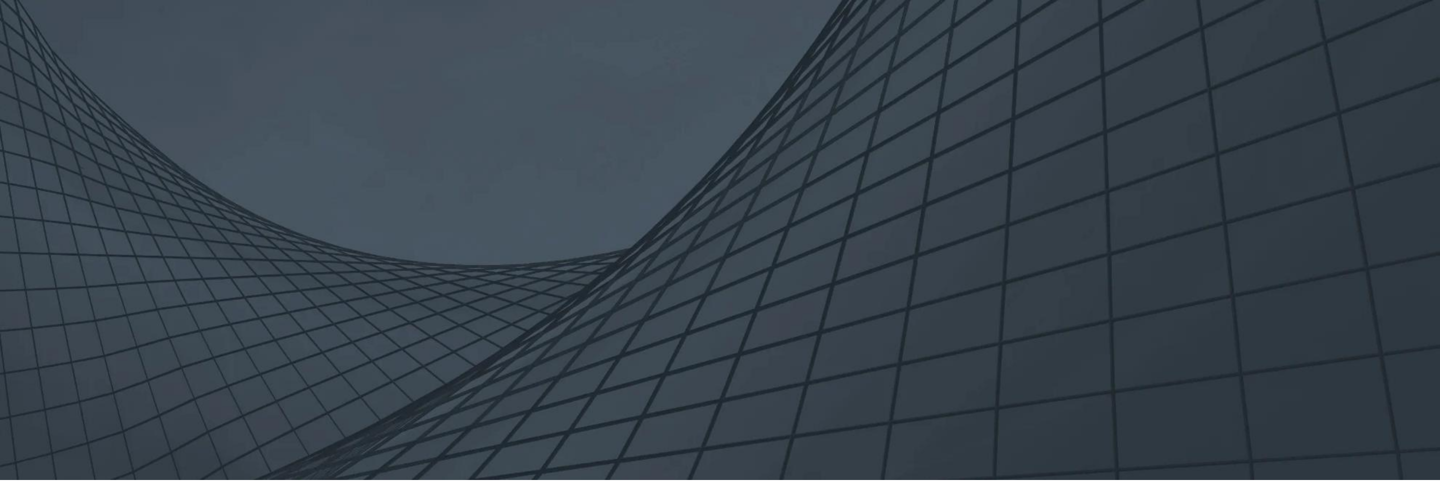
[1]Secondary Fund data based on Pitchbook Data, as of Q4 2023. Private Equity data based on Overbay analysis of Pitchbook Data. 2021 and 2022 distribution figures based on FY figures. 2023 distributions figure based on TTM Q3 2023.



The Gap Between Expectations and Reality

Intuitively, one would expect distributions from secondary funds to be higher than those from broader private equity for several reasons, including:

1. The assets being purchased are generally mature and in their "harvest period," when managers are attempting to monetize their portfolios.

2. Secondary funds typically purchase assets at discounts (averaging 15%, over the last five years[1]). Therefore, mathematically, their distributions should be proportionately higher.

2023 Secondary Fund Distribution Pace

Expected Secondary Fund Distributions[1,2,3]		Actual Secondary Fund Distributions[2]
11.4%	VS.	5.0%

However, in reality, distribution pacing for secondary funds in 2023 was less than half of the expected rate—approximately 5.0% of NAV for all secondary funds and around 6.6% of NAV for pre-2019 vintage secondary funds.[2]

To put this in context, if secondary funds distributed capital in line with expectations, they would have produced ~$52 billion more in distributions from 2021-2023.[4]

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[1]Jefferies Global Secondary Market Review, 2024. [2]Pitchbook Data, as of Q4 2024. [3](Annual Private Equity Distribution % / Average Secondary Price) – Median Management Fees: (10.7%/85%)-1.25%. [4]See Disclaimer.

Secondary Funds Have Evolved

While secondary funds were originally marketed as a way for investors to accelerate cash flows and mitigate J-curve effects, their objectives and strategies have evolved significantly over the past twenty years. Secondary funds are increasingly utilizing tools that can maximize returns at the cost of delaying distributions:

Leverage

- Secondary managers may use various forms of leverage, including fund facilities, asset-backed loans and purchase price deferrals to enhance returns.
- Instead of calling capital from investors, secondary funds often use distributions from their assets to pay down debt.

Recycling

- During the investment period, many secondary funds reinvest or ‘recycle’ early distributions from their initial investments into new secondary transactions.
- Recycling can significantly delay distributions to investors in the first few years of a secondary fund’s life.

GP-Leds

- Over the past decade, a growing proportion of secondary fund capital (~46% in 2023[1]) has been invested in GP-led transactions (“GP-leds”). These deals involve providing fund managers with additional time and capital to continue working with promising companies in their portfolios.
- By their nature, GP-leds are medium-to-long term bets, meaning that they are generally not expected to result in realizations in their first few years.

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[1]Jefferies Global Secondary Market Review, 2024.

Cash Flow vs. Long-Term Growth

Secondary funds have distributed significantly less than broader private equity since 2021. The dramatic drop in distributions highlights the significant changes in secondary fund strategies over the years. Once touted as a way to accelerate cash flows and mitigate J-curve effects, secondary funds are now focused on maximizing long-term growth.

While investors may ultimately benefit from higher returns, they should understand that their short to medium-term distributions are likely to be lower than those of other private equity strategies.

Discover Overbay's unique approach to secondaries. Our goal is to deliver the strongest distributions and the best risk-adjusted returns in private equity.

Speak with our team

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Missing Distributions Calculation = Global Secondary Fund NAV[1] * (Expected Secondary Fund Distributions – Actual Secondary Fund Distributions).
Expected Secondary Fund Distributions = (Annual Private Equity Distribution % / Average Secondary Price[2]) – Median Management Fees.

2021: 172.23*(32.4%-18.4%) = ~24B
2022: 249.89*(17.1%-12.7%) = ~11B
2023: 263.09*(11.4%-5.0%) = ~17B
Sum: ~52B

[1]Pitchbook Data, as of Q4 2024. [2]Jefferies Global Secondary Market Review, 2024.