Hamilton Lane

The Secondary Market Opportunity

July 2022

The Current Secondary Market Backdrop

While we continue to see a tremendous amount of deal flow in the secondary market, the deal completion rate slowed in Q2 2022 as the market paused to digest volatility and lower pricing. Deal flow is expected to remain strong, as seeking liquidity and capital via the secondary market will continue to be priority for both LPs and GPs in the current environment.

For LPs in particular, the challenge will be determining what pricing they are willing to accept in order to solve their increasing over-allocation issues. What was an opportunistic exercise in recent years is set to become more tactical and need-based.

Supply/Demand

With broad market acceptance continuing to drive secondary supply growth, the secondary market has never been more undercapitalized than it is today. Currently, there is only around $100-$125 billion[1] of dry powder, which is less than 2021 transaction volume and still just a small fraction of the $6+ trillion of NAV in the private markets. There is a tremendous amount of potential secondary opportunity relative to the capital available to execute on those opportunities. This dynamic is creating an attractive opportunity from a buying perspective.

LP Interest Pricing

Pricing has declined across the board since the beginning of the year, with most deals still pricing off of year-end NAVs (or March 2022 NAVs, which were broadly similar to year-end). The quick decline in pricing, along with increasing buyer caution, has caused LP deal activity in the secondary market to temporarily slow down. However, there is a strong backlog of motivated LPs bringing portfolios to market in the second half of 2022 and we anticipate volumes increasing as buyers and sellers gain visibility into second quarter valuations and performance. To the extent June valuations come down to account for the current environment, optical discounts could be palatable, further supporting deal activity in the second half.

Transaction Landscape – Macro Impacts

	Supply Impact	Opportunity Outlook
LP Interest	• LPs are overallocated to private equity, driven by the decline across many asset classes aside from private equity, which did not move materially in Q1. • This dynamic should support LP interest deal flow in the next several quarters as LPs rebalance their portfolios and maintain their private markets commitment pacing.	• Targeted sales of higher-quality portfolio subsets may be the most efficient path for motivated, price-sensitive sellers, as buyers focus on funds they know best and the market shifts from macro to micro. • Motivated sellers will increasingly transact directly with secondary buyers that can offer certainty in an uncertain environment.
GP-Led/ Complex	• GP-led/complex transactions still comprised the majority of deal flow through the first half of 2022, and supply from general partners is showing no signs of slowing. • The benefits to GPs (providing liquidity to LPs, holding onto their best/most resilient assets, developing and strengthening strategically important relationships) are all magnified in the current market environment.	• There will continue to be a shortage of capital for GP-led transactions, as average deal sizes remain high and buyers become more cautious on valuation. As a result, we expect this to be a buyer's market for some period of time. • While continuation vehicles should continue to represent the majority of this market segment, macroeconomic and valuation uncertainty should present more opportunities to pursue structured and complex transactions. GPs will prioritize both existing relationship status and secondary expertise in identifying preferred counterparties to partner with directly in these transactions.

ENDNOTES

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[1] Source: Evercore 2021 YE Survey Results

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