Understanding Private Equity Secondaries Funds: A Cheat Sheet

Imagine buying a concert ticket—but your plans have changed, and now you can't go. Would you just throw away the ticket? Probably not. Instead, you might try to sell it to someone else.

Similarly, when an investor needs to sell their limited partnership interest in a private equity (PE) fund, they can sell it to another investor. This is called a PE secondary. Typically, the purchaser of this interest is a PE fund manager specializing in secondaries, whose portfolio consists of these secondaries interests.

What is a PE secondary?

The secondary market in private equity refers to the buying and selling of PE fund interests (also called limited partnership interests) after the original investment was made. Unlike the primary market, where investors directly invest in the PE fund or in a company, the secondary market allows investors to sell their stakes to others, usually at a discount. This gives investors liquidity, which isn't typically available in PE investments, since they are usually long-term commitments.

Are there risks to investing in PE secondaries?

Like all investments, PE secondaries come with risks. When considering an investment in a PE secondaries fund, there are several important factors to evaluate, including the manager's track record, investment strategy, access to underlying fund quality, due diligence program and risk mitigation.

What are the potential benefits of investing in a PE secondaries fund compared with primary PE?

1. **Quicker returns than primary PE:** Secondary transactions usually happen midway through a fund's lifecycle, skipping the early investment period—when expenses incur and growth may be limited—and potentially offering shorter investment periods and accelerated returns.

2. **Enhanced transparency:** When investing in a new primary private equity fund, investors may not know the future holdings. However, secondary funds consist of existing assets of the underlying fund, generally providing better visibility into holdings and potentially mitigating downside risk. During the seven worst public market drawdowns in the past 20 years, secondary PE declined 3.7% while primary PE fell 10.4% and public equities lost 24.9%, on average.[1]

3. **Discount opportunities:** Secondary sales are often driven by an investor's need for liquidity. Typically, the existing fund owner sells the interest at a discount to net asset value. The average market discount over the last five years was 9%,[2] potentially presenting attractive opportunities for investors.

[1] As of 12/31/23. Source: Voya IM, Cambridge Associates, FactSet. Secondary PE represented by the Cambridge Secondary Index. Primary PE represented by the Cambridge U.S. Private Equity Index. Public equities represented by the S&P 500 Index.

[2] Source: Jefferies Global Secondary Market Review (Jan 2024) and Evercore H1 2024 Secondary Market Survey Review (July 2024).

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Why should I consider investing in a PE 40 Act fund rather than a traditional PE fund?

Feature	PE 40 Act fund	Traditional PE fund
Investment minimum	Often starts at $25,000	Usually starts at $1 million
Tax filing	Form 1099	Schedule K-1
Liquidity	Quarterly redemptions limited to a percentage of either the fund's NAV (tender offer fund) or the investor's position (interval fund)	Available only through secondary markets, fund distributions or at the end of the fund's life
Diversification	May be diversified across sectors, geographies, investment types, vintage years and asset size	Frequently focuses on a defined subset of sectors, with concentrated holdings
Capital deployment	Capital put to work immediately	Capital invested over several years and called as needed
Availability to investors	IRA-friendly means potential for tax-deferred growth	Often not qualified for IRA investment

For illustrative purposes only. Actual features may vary depending on the specific investment product.

A note about risk

Past performance is no guarantee of future results.

Private equity may not be suitable for every investor, may involve a high degree of risk, and may be appropriate investments only for sophisticated investors who are capable of understanding and assuming the risks involved.

Private equity investments are subject to various risks. These risks are generally related to: (i) the ability of the manager to select and manage successful investment opportunities; (ii) the quality of the management of each company in which a private equity fund invests; (iii) the ability of a private equity fund to liquidate its investments; and (iv) general economic conditions. Private equity funds that focus on buyouts have generally been dependent on the availability of debt or equity financing to fund the acquisitions of their investments. Depending on market conditions, however, the availability of such financing may be reduced dramatically, limiting the ability of such private equity funds to obtain the required financing or reducing their expected rate of return.

Private equity funds as well as securities that invest in such funds and companies in which such funds or securities may invest tend to lack the liquidity associated with the securities of publicly traded companies and as a result are inherently more speculative.

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