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Side Letter

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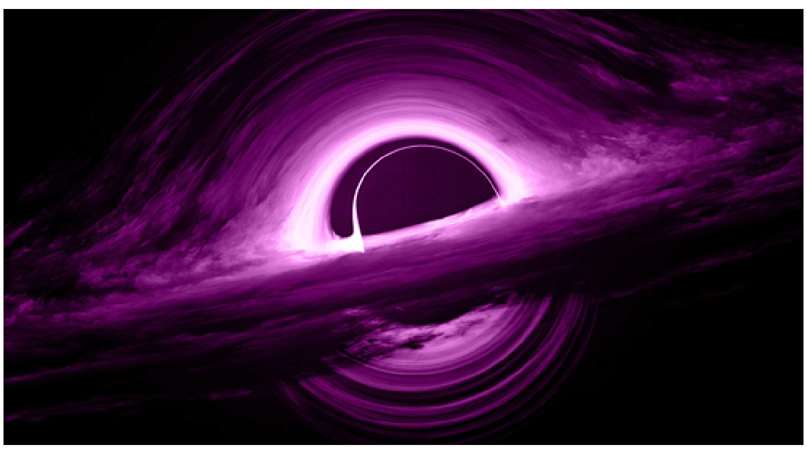
LPs without the technical capacity or appetite for secondaries could find themselves with a trophy asset blind spot. Plus: San Bernardino reckons emerging managers could prove key to unlocking exit opportunities. Here's today's brief, for our valued subscribers only.

Fresh insights



GP-leds: a black hole for LPs without secondaries exposure

Source: Getty

Black hole fund

As a growing number of managers look to roll their best assets out of traditional funds and into CVs, LPs not investing in secondaries or continuation funds may end up with a blind spot in their private equity portfolios. That's according to our colleagues at *Secondaries Investor*, who cite Pantheon principal Morten Lundin (registration required). Those without secondaries exposure "more or less have a black hole" in their portfolio as trophy assets get traded into CVs, Lundin explained at the British Private Equity & Venture Capital Association's secondaries conference last month.

The impact of missing these opportunities could prove significant for returns. Debevoise & Plimpton partner Gavin Anderson said at the conference that for many funds, returns tend to come from "a small amount of investments doing really well". LPs should be better equipped to elect for roll options because of the benefits these transactions can bring, added Lexington Partners managing director Jacob Rawel, noting that this is easier said than done since internal constraints limit some LPs' capabilities.

Indeed, some institutions are still devising ways to deal with the often resource intensive and highly time sensitive process of deciding whether to roll into or back a third-party continuation fund. Research from Lazard has previously found that LPs choose to sell rather than roll their exposure approximately 90 percent of the time.

This dynamic is particularly pronounced within Asia-Pacific. "We've seen a lot more investors in Europe and the US increase their allocations towards secondaries and also adopt policies as to how to respond to GP-led secondaries transactions and how they adopt solutions to look into election forms," Alex Chauvin, a London-based partner at White & Case, tells *Side Letter.*

"They have now increasingly taken an approach to standardise the process… In Asia, we're starting to see the same thing, probably not to the same extent as Europe and US, but I think it's more of a matter of timing."

National Pension Service of Korea – a behemoth of an institution and a trend-setter among East Asian LPs – was awarded Limited Partner of the Year in Asia-Pacific for the PEI Awards 2024 thanks to its somewhat pioneering decision to launch a dedicated continuation fund team.

It is, of course, worth noting that Lundin and Rawel have secondaries products to sell and, as such, are predictably bullish on such opportunities. Still, the evidence suggests their arguments have merit: research from Upwelling Capital Group shows LPs that systematically avoid rolling over their exposure to continuation funds are incurring a tangible opportunity cost of around 8 percent per vintage year. A study by Evercore in partnership with Paris's HEC School of Management found that single-asset CVs have lower return dispersion than buyout funds, indicating lower return variability.

As these vehicles proliferate, so too will the administrative burden on LPs. Those with the means to make an informed decision about these opportunities will be best placed to capture any potential upside associated with these trophy assets and illuminate an otherwise expanding 'black hole' in their portfolios.

Essentials

Emerging interest

San Bernardino County Employees' Retirement Association staff are pushing for more involvement with emerging managers to gain entry points to funds presenting exit opportunities outside of ideal market conditions, our colleagues at *Buyouts* report (registration required). Even as LPs gravitate to larger funds, there's attractive returns to be found – without the same level of competition – in small buyout strategies, Thomas Kim, senior investment officer at SBCERA, recently told the board. There are also more stable exit routes than the larger end of the market, he said.

The pension presented plans for a $200 million fund dedicated to PE-focused emerging managers at its most recent board meeting. It would represent 1.25 percent of the $15 billion portfolio, which has 20 percent exposure to PE. The board has been exploring options for emerging manager exposure since last June. "It's not an enormous bet," said Kim. "But it's one we do expect to help the portfolio."

A wider spread of exit options in the mid-market has caught the eye of many a large institution in recent years, prompting some to shift focus towards smaller managers.

Making rain in Spain

Spanish mid-market firm Corpfin Capital is set to hold a €300 million final close on its sixth flagship fund by the end of the month, hitting its target and hard-cap, according to a statement. The firm began raising Corpfin Capital VI at the end of 2024 and garnered €400 million of interest. Once the fund is wrapped up, the vehicle will be about €20 million larger than its 2019-vintage predecessor.

Fund VI received "strong support" from existing LPs, most of whom "significantly" increased their commitments, the firm said. The LP base is mainly based in Europe, similar to prior vintages, per a spokesperson.

Fund VI will invest €15 million-€40 million in up to 15 companies in Iberia. Private capital investment in Spain last year reached €6.54 billion across 725 investments, down slightly from 2023's €6.7 billion, according to preliminary estimates obtained by industry association SpainCap. PE investments made up nearly 90 percent of that total investment volume, or €5.6 billion across 150 investments.

Today's letter was prepared by Alex Lynn with Carmela Mendoza, Katrina Lau and Silas Sloan.