



# Secondaries: A Primer

July 2021

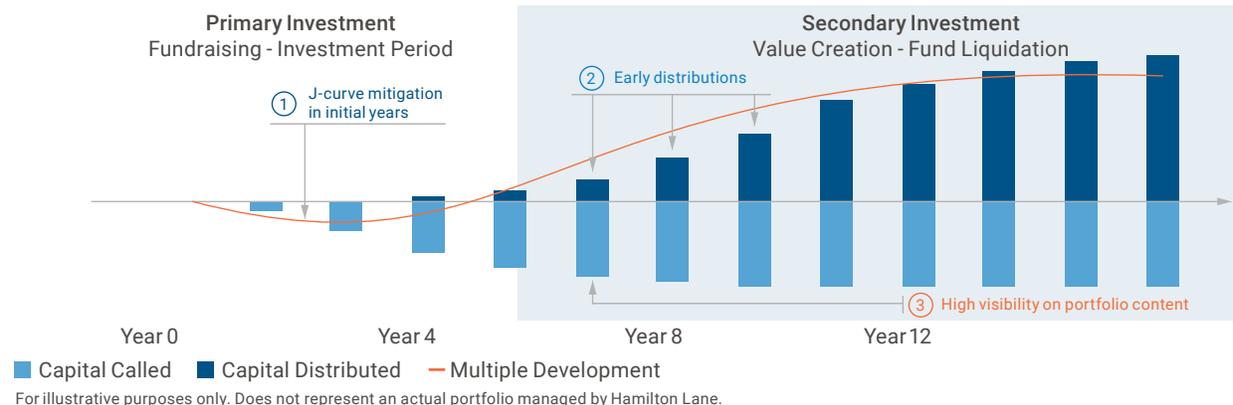
## What are Secondaries and how do they work?

A transfer of a private equity interest from one investor to another. Secondary buyers will purchase an investor's commitment to a private equity fund and become a replacement investor (limited partner, or LP).



## Primaries vs. Secondaries

Private Equity Investments	Secondaries
<ul style="list-style-type: none"> <li>• One fund with one strategy, invest in 10-30 companies over 4-5 year investment period</li> <li>• Long-term commitment</li> <li>• Illiquid by nature</li> <li>• Life of fund is typically 12+ years</li> <li>• Asset class has seen sustained growth</li> </ul>	<ul style="list-style-type: none"> <li>• Several funds of various strategies and vintages, hundreds of companies, 3-year investment period and 10-12 year fund life</li> <li>• Mechanism for liquidity for an illiquid asset class</li> <li>• Offers investors the option to sell and transfer interest in a fund/asset to another investor</li> </ul>

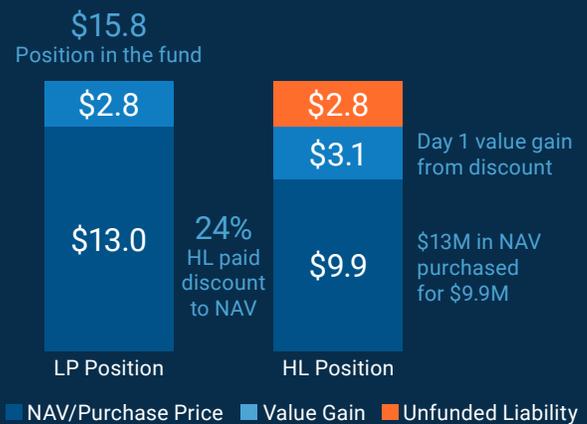


## Mechanics of a Secondary Transaction and Why LPs Sell

- Buyer will pay a price to the selling investor (limited partner).
- Pricing is expressed as a percentage of recent net asset value.
- Discounts: Secondaries are often purchased at a discount which may result in immediate attractive returns and provides downside cushion.
- Buyer will fund all future capital calls and receive future distributions.

▶ Below is an example of a transaction completed by Hamilton Lane. The aim of this case study is to illustrate the mechanics of a secondary purchase.

The LP was looking to sell a private equity fund in year seven of the fund life, with a current value of \$13 million and \$2.8 million in unfunded obligations. No information was provided and the process was restricted to secondary investors with strong primary relationships with the GP. Our competitive position - a deep familiarity with the GP, multiple advisory board seats on their funds, and limited competition for the secondary - allowed us to buy the position at a 24% discount.



For illustrative purposes only. Past performance is not an indicator of future results.

## Why Do Limited Partners Sell in the Secondary Market?

Liquidity	Allocation Issues	Portfolio Management
<ul style="list-style-type: none"> <li>• Cash needs; often distressed</li> <li>• Desire to reduce unfunded commitment balance</li> <li>• Selling interests in older funds to reduce number of GP relationships</li> </ul>	<ul style="list-style-type: none"> <li>• “Denominator effect”: declining public market values and timing of private equity distributions result in LPs exceeding their private equity allocation target</li> <li>• Overcommitment (invested too aggressively)</li> </ul>	<ul style="list-style-type: none"> <li>• May need to sell existing interests to permit investments in new funds</li> <li>• Duplicative exposure to single fund post-merger</li> <li>• Change in private equity investment strategy</li> <li>• Selling interests in older funds to reduce number of GP relationships</li> </ul>

Achieve liquidity	Reduce unfunded commitment liability	Free up allocation for new commitments	Change in investment outlook/strategy	Monetize performing or tail-end equity exposure	Rationalize non-core GP relationships	Reduce overweight to private equity	Rebalance/optimize private equity portfolio
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← Liquidity ————— Portfolio Management →

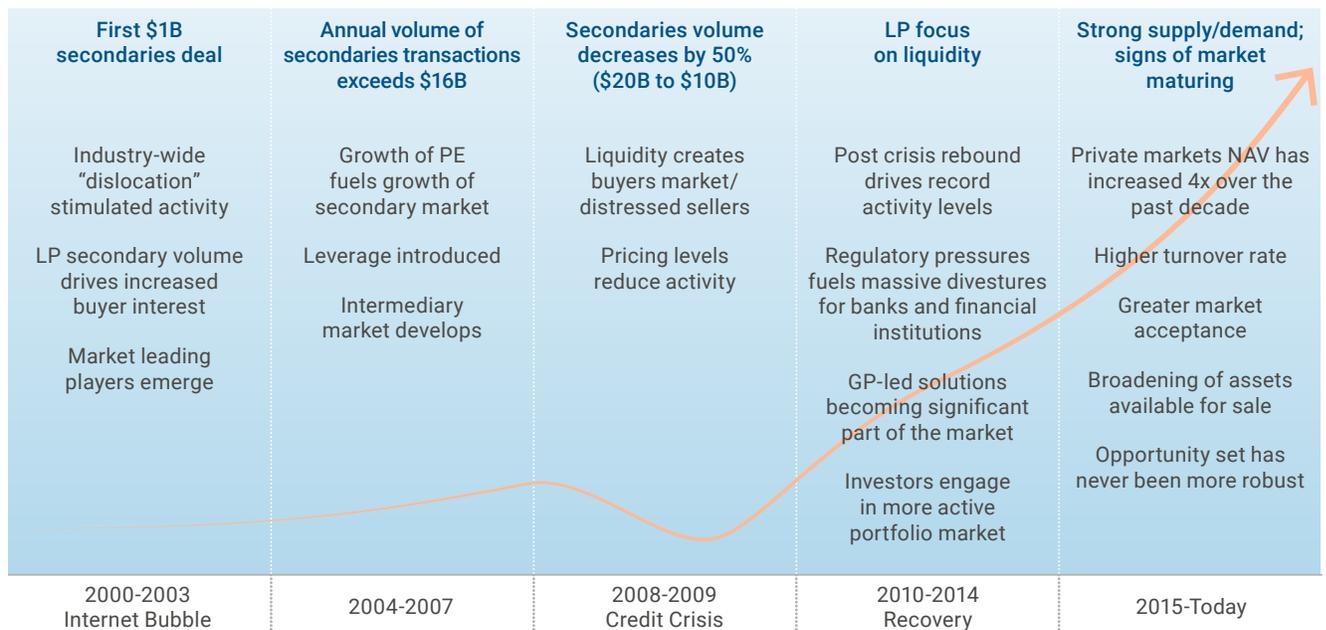
## Secondary Market Overview

### Why does the secondary market exist?

- The secondary market is the only way for individual LPs to exit early from their private equity investments.
- The secondary market has expanded to now provide alternative forms of liquidity to both LPs and GPs/ private equity managers, allowing private equity investors an opportunity to:
  - Achieve early liquidity from their private equity assets
  - Manage their portfolios more pro-actively
  - Modify their portfolios in response to strategic change
  - Lock-in returns from their private equity investments

### Secondary Market Evolution

- Initially a niche strategy, secondary investments have become mainstream.

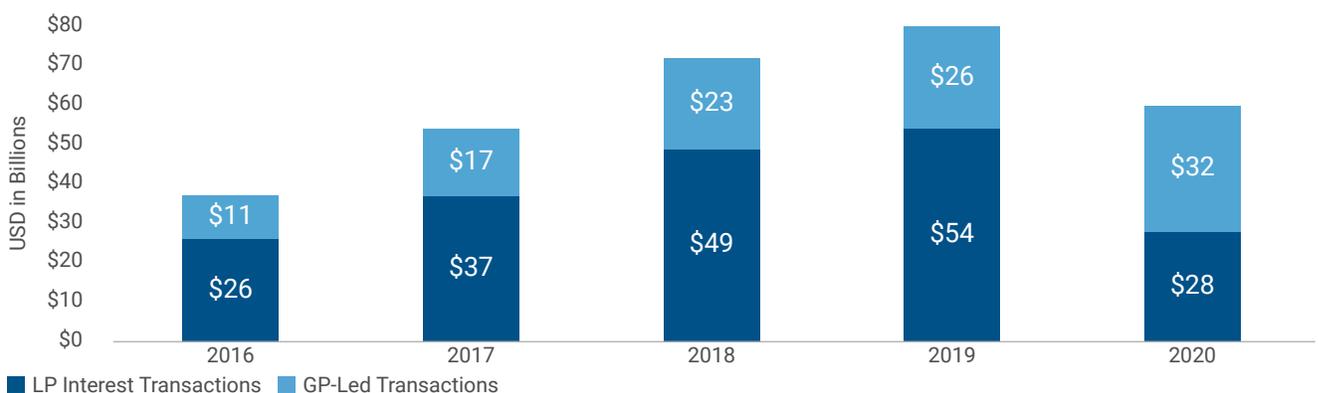


Growth Drivers	Market Themes
<ul style="list-style-type: none"> <li>• Growth of private markets / primary fundraising – driving secondary inventory and diverse opportunity set</li> <li>• Increasing turnover / portfolio management</li> <li>• Introduction of GP-led secondaries</li> </ul>	<ul style="list-style-type: none"> <li>• Higher Quality – greater market acceptance, LP's sensitive to discount willing to sell higher quality funds</li> <li>• LP deals coming back – portfolio management decisions delayed from 2020</li> <li>• Greater GP participation – using the market to create strategic relationships, directing deals to those they want in their fund(s)</li> </ul>

## Types of Secondary Transactions

	Traditional LP Transactions	Structured/GP-Led Transactions	Complex Transactions
Transactions	<ul style="list-style-type: none"> <li>• Single fund/fund manager LP</li> <li>• Portfolio’s LP</li> </ul>	<ul style="list-style-type: none"> <li>• Multi asset</li> <li>• Single asset</li> <li>• Sale of some or all of the remaining LP stakes / assets to a new investor often enabling existing investors to remain within the fund</li> </ul>	<ul style="list-style-type: none"> <li>• Secondary Direct</li> <li>• Pref/Structured</li> <li>• Sale by corporations or financial institutions of directly-held investments</li> </ul>
Current Market Dynamics	<ul style="list-style-type: none"> <li>• Projected slowdown in distributions will likely act as a catalyst on the LP side to seek liquidity for re-deployment</li> <li>• Supply of large, brokered deals remains muted</li> <li>• LPs increasingly comfortable to transact directly, looking for speed and certainty</li> <li>• High-quality funds/GPs sold more frequently than ever</li> <li>• Focus on optical discount vs current discount in a rising value environment</li> </ul>	<ul style="list-style-type: none"> <li>• Broad market acceptance by all constituents driving growth and rapid evolution</li> <li>• GPs continue to see benefits in proactively finding ways to get liquidity for their investors through secondary transactions</li> <li>• The GP-led secondary market has recently been defined by a flight to sponsor and asset quality</li> <li>• GPs are increasingly steering deals only to those groups that represent current or potential long-term primary capital providers.</li> <li>• Potential slowdown in liquidity or challenges accessing capital to support assets may act as growth catalyst</li> <li>• Value in complexity – offering investors the opportunity to achieve attractive risk-adjusted returns</li> </ul>	

Secondary Market Volume by Deal Type



Source: Evercore 2020 YE Survey Results (January 2021).

## Quantifying the Benefits of Secondaries

### Portfolio Benefits

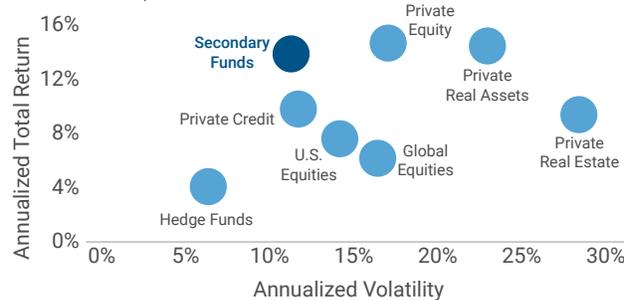
- ▶ From the private equity investor’s perspective, secondaries can offer a number of diversification and return benefits relative to primary fund investments.

J-Curve Mitigation	Portfolio/Vintage Diversification	Risk Reduction From Knowledge of Underlying Assets
<ul style="list-style-type: none"> <li>• Investments are purchased farther along in their life cycle, with the potential to reduce the negative impact of management fees and accelerating the pace and timing of distributions</li> </ul>	<ul style="list-style-type: none"> <li>• Secondaries may provide investors with the ability to quickly diversify a portfolio by vintage year, investment strategy, industry sector and fund manager</li> </ul>	<ul style="list-style-type: none"> <li>• When evaluating a secondary transaction, the portfolio companies can be carefully analyzed, reducing the “blind pool” risk associated with primary investments</li> </ul>

### Secondary Resilience & Risk-Adjusted Returns

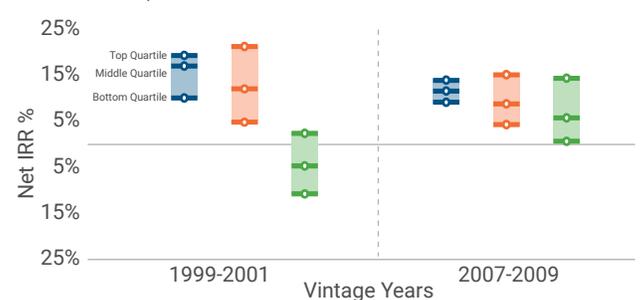
- ▶ Secondaries have proven to be a lower risk strategy and have historically performed well through cycles. They have the ability to benefit from growth while capitalizing on wider discounts in volatile or distressed markets.

15-Year Asset Class Risk-Adjusted Returns  
As of June 30, 2019



Source: Hamilton Lane Data via Cobalt (January 2021)

Dispersion of Returns During Market Downturns  
As of June 30, 2019

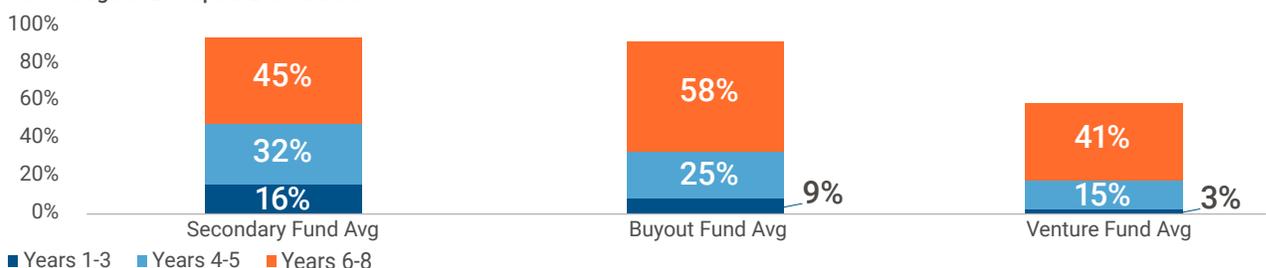


Source: Hamilton Lane Data via Cobalt (January 2021)

### Increased Pace of Capital Deployment

- ▶ Investments are typically at or near their investment periods when purchased and because a secondary fund’s underlying investments are already seasoned, secondary funds may send back distributions to investors early in a fund’s life.

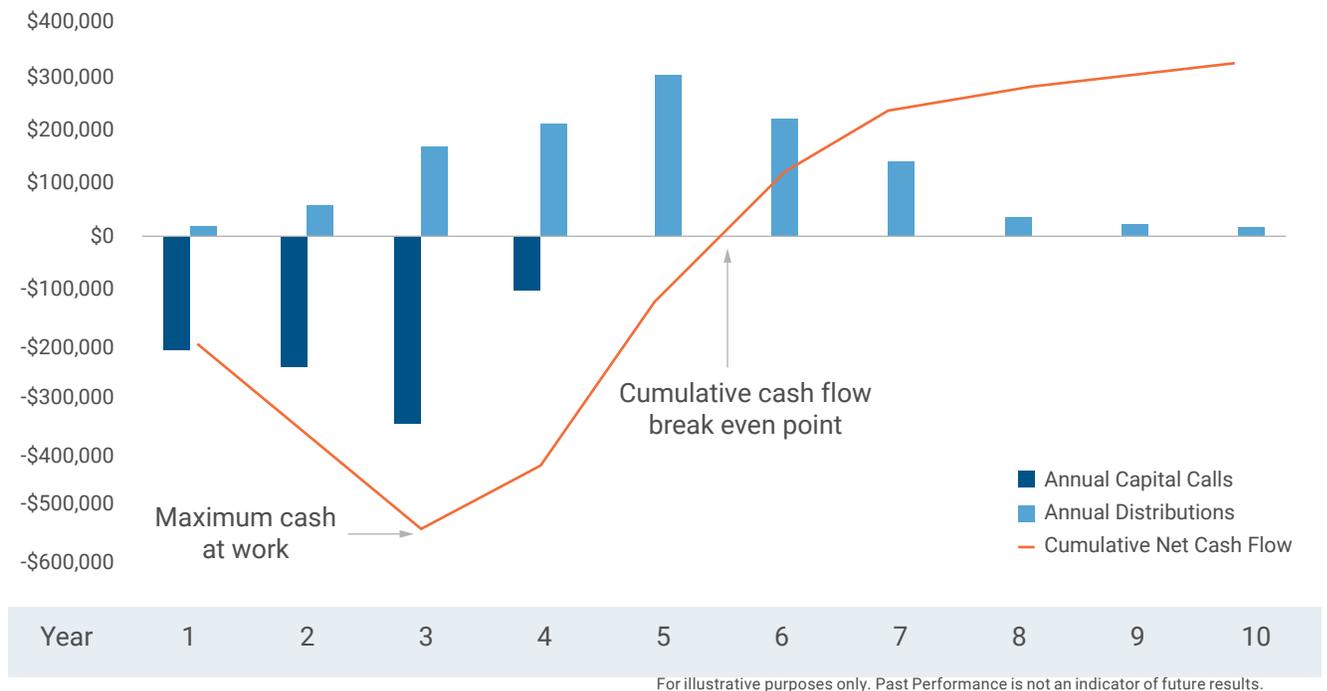
Percentage of LP Capital Distributed



## Investor Cash Flow Experience

### HL Secondary Fund Investor Experience – 2008 Secondary Fund

- ▶ The following scenario illustrates a \$1M commitment to Hamilton Lane’s 2008 vintage Secondary Fund (HLSF II). Prior to and throughout the GFC, Hamilton Lane remained highly selective and patient in deploying capital out of HLSF II.



### Expected Cash Experience for Investors:

- Hamilton Lane may deploy capital over the fund’s three-year commitment period
- Investors’ capital may be called down periodically during the investment period and should expect to have 80-90% of their commitment invested by years 3-4
- The value of investors’ capital should grow over time and that value will be sent back to investors in the form of distributions, also known as realizations

## Hamilton Lane Secondary Platform

History of Investing  
in Secondaries

21

Years experience

Secondary AUM<sup>1</sup>

\$10B+

Secondary Transactions  
Completed

215+

Experience & Credibility<sup>2</sup>

32

Secondary  
team members

Secondary Investment  
Committee

25+

Average years  
investment experience

Capital Invested in 2020

\$1.3B

### Who We Are

- ▶ Long-standing, successful secondary platform benefiting from Hamilton Lane's leading position in the private markets
- ▶ Large, tenured team with broad skillsets that have ability and experience to cover the entire secondary market landscape
- ▶ Disciplined investors with proven investment strategy. Targeting high-quality, highly-funded, and attractively-priced secondaries

### Why HL Secondaries?

- ▶ Competitively well positioned in an evolving market
- ▶ Strategic capital provider in a market with increasing GP influence and where relationships matter
- ▶ Access & information provide deal flow and due diligence advantages
- ▶ Highly selective portfolio with attractive risk/return characteristics
- ▶ Well-positioned secondary platform in a growing and evolving secondary industry that is increasingly driven by GPs and high-quality investment opportunities

As of March 31, 2021.

<sup>1</sup> AUM equals assets under management for active accounts. AUM is equal to market value, unfunded, plus ANI. ANI is defined as the amount of money remaining that has been authorized to Hamilton Lane but not invested. ANI is only attributable to the Hamilton Lane Secondary Fund I, II, III, and IV.

<sup>2</sup> Includes Secondary Committee members

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As of July 20, 2021