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Quick Sales Yielding Secondary Gains

In a departure from their usual strategies, some secondary-market buyers are trying to flip their investments for quick profits.

The play involves limited partnership interests that managers of secondary-market funds and funds of funds picked up from distressed sellers last year on the cheap — often for prices around 40% of net asset value. The thinking now is that with market conditions looking better, they can unload those same positions for double that price or more.

There's no word on who is involved in the transactions. The sellers have been keeping their activities under tight wraps, in part to shield their identities from fund managers who typically frown on active trading strategies.

Such trades aren't usually in the repertoires of secondary-market buyers either. But for some, rising values are temporarily creating impossible-to-resist opportunities to boost their short-term returns. That's especially the case for firms that are preparing to raise fresh capital or that want to roll the proceeds into long-term plays — along with those that got into investments that were outside their usual strategies simply because prices were too good to pass up.

Take a fund stake purchased at 40 cents on the dollar at the midpoint of 2009. Today, that position might be worth 80 cents, which works out to a gross annualized return of 147%. What if the buyer took the more common strategy of holding the interest to maturity? Assuming the underlying assets could be sold at par in, say, mid-2011, the annual return would be a much lower 58%.

New York secondary-market consultant **Azla Advisors** has helped buyers and sellers carry out some such deals. Azla chief **David Waxman** said intermediaries have come into play as the principals in the sales try to remain anonymous, at least until the managers have to sign off on the transfers. However, there are times when the managers whose fund shares are being traded might also want to replace secondary buyers with limited partners that have the capacity for new-fund commitments. "We have been working with several secondary funds



that were bold enough . . . to be very active buyers in the bottom of the market during the first half of 2009," Waxman said. "It's a very short-lived phenomenon in the secondary-market world."

Another source reported seeing a fund of funds in Europe sell a position it bought last year, something the seller wasn't planning to do when it got into the deal. "It's quite unusual for a fund to be on the secondary market and to sell after only a year or so," he said. ❖