Briac Houtteville on Private Equity Secondary

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Briac Houtteville is the European Head of Secondaries at Portfolio Advisors, bringing 15 years of experience in the private equity secondary industry. Before his current role, Briac served as Managing Director & Co-Head of European Capital Advisory at Greenhill & Co for over six years. He also held positions as a Vice-President and Principal at Greenhill Cogent. Houtteville is a graduate of ESSEC Business School, where he earned his Master's degree, and Grenoble INP - ENSIEG, where he earned a Master of Science degree.

Portfolio Advisors is a global private asset management firm that manages approximately $40.8 billion in assets. The firm offers a diverse range of investment programs that encompass private equity, private credit, and private real estate investment strategies, with a particular focus on the mid-market. Established in 1994, Portfolio Advisors has a team of over 140 highly skilled professionals who operate out of offices in Darien (CT), Dallas, Zurich, London, Singapore and Hong Kong.

There are two main segments of the private equity secondary market: (1) the traditional sale of limited partnership ("LP") interests ("LP-led" market); and (2) general partners of private equity funds ("GPs") that use the secondary market to move one or more existing assets under their ownership into a continuation vehicle ("GP-led" market).

Wikram Chowdhury: To begin, could you provide a brief introduction of yourself and share what drew you to the secondary market 15 years ago?

Briac Houtteville: I am the Head of European Private Equity Secondary at Portfolio Advisors, currently based in London. I began my career advising financial sponsors during the strong growth period of the private equity market between 2006-2008, primarily in a corporate finance and transaction services capacity. As the private equity market became a major component of limited partners' and institutional investors' portfolios, the need for liquidity grew, particularly after the global financial crisis. That was when I was given the opportunity to join Cogent Partners, one of the first advisors in the private equity secondary market. At the time, the secondary market was much smaller, around USD $10 billion, but I could see its growth potential. I initially started working on a lot of portfolios then on GP-led transactions and eventually transitioned to investing in both GP- and LP-led secondary transactions at Portfolio Advisors.

Wikram Chowdhury: Moving to Portfolio Advisors, I would be interested in hearing your perspective on what sets Portfolio Advisors apart from its competitors and what motivates Portfolio Advisors to focus on mid-market transactions?

Briac Houtteville: We were established in the mid-90s as a platform for private markets and today, with more than 29 years of experience, we are widely regarded as the mid-market specialists in this area due to our broad offering and strong track record. Our private equity offerings encompass primary, secondary, and co-investment transactions, in addition to dedicated teams for private credit and private real estate. We aim to provide a comprehensive 360-degree solution for mid-market general partners, whether they require capital for a new fund, seek liquidity, co-investment opportunities, or financing through our private credit team.

My belief is that the mid-market offers a compelling opportunity, given the significant number of managers and companies operating at this level worldwide. Additionally, mid-market companies typically have lower leverage and valuations compared to other benchmarks, which can result in superior performance compared to larger companies. This is the core focus at Portfolio Advisors, which as of Dec-22 manages nearly $40.8 billion, with the majority invested in private equity, and we deploy almost $4 billion every year in private markets.

Wikram Chowdhury: Now, let us shift our focus to your area of expertise. To start off, could you share your thoughts on the key differences between the secondary private equity markets in the EU and the US?

Briac Houtteville: Firstly, it is important to note that the secondary market is inherently global, with US investors holding European funds and vice versa. Secondly, the size of the secondary market is closely linked to that of the primary market, and this relationship is reflected in global AUM. The US is the largest market accounting for approximately 60% -

65% of secondary market investments followed by Europe, which accounts for ~30%. The rest of the world, primarily Asia, accounts for 5% - 10%. Regarding megatrends, pricing, and deal types, we see notable similarities between the US and Europe. However, differences arise in the historic use of secondary transactions, the pace of deals, and their size/volume. Historically, US investors utilized the secondary market as a tool for portfolio management before other regions. Due to the size of the market, transactions in the US also tend to be larger on average compared to those in Europe. Furthermore, the US also tends to see greater deal flow velocity, resulting in larger transaction volume than elsewhere.

When it comes to investors, the frameworks used for portfolio management of LP stake transactions or GP-led deals are similar between the US and Europe. Additionally, most secondary firms, including ours, operate on a global scale, contributing to the truly global nature of the market.

Wikram Chowdhury: That brings me perfectly to my next question. How do you see the present macroeconomic climate, particularly regarding inflation and rising interest rates, impacting the LP secondary market? Do you anticipate this causing extended holding periods?

Briac Houtteville: My journey in secondaries began in January 2009, coinciding with a surge in volume due to the financial crisis and the emergence of distressed investors. Subsequently, events such as Brexit in 2016 and the COVID-19 pandemic in 2020 also led to a significant increase in volume in the secondary market.

To put it simply, the occurrence of significant and unforeseen macroeconomic events usually triggers limited partners to become more active in the secondary market, resulting in a significant increase in volume. This is because they may have experienced public market declines, causing overallocation to private equity and a need for liquidity. Additionally, with fewer distributions due to a weak M&A and IPO environment, longer holding periods are expected. The rise of GP-led transactions also provides a new way for GPs to keep their top-performing assets. All these factors contribute to the steady growth of the secondary market over the past 15 years and will likely continue to do so for the foreseeable future. Despite this, the secondary market still remains a relatively small percentage of the primary market.

Wikram Chowdhury: You have already touched upon a part of my next question, so let me delve a bit deeper into the topic to challenge you (laughs). How is the current change in valuation within technology affecting GP-led deals?

Briac Houtteville: There is certainly pressure on valuations in the technology sector. The impact of such a downward trend is not limited to GP-led transactions. In the venture market, particularly at the early stage, we have observed higher discounts on the secondary market, which can discourage investors from selling and seeking liquidity. Similarly, for GP-led transactions, pricing needs to be close to or above par. As a result, we have seen a slowdown in volume for venture and growth secondary transactions. This is partly due to significant supply from investors who wish to sell, while buyers are waiting for NAVs to adjust, potentially after the next financing round. This could result in a change in valuations compared to 2021. As a result, this segment of the market has been slower to respond to market shifts.

Wikram Chowdhury: According to a very recent Evercore report, GP-led deals accounted for $48 billion of transaction volume in 2022, representing approximately 46% of the overall secondary market. Do you anticipate any changes in the distribution of GP-led and LP-led transactions in 2023?

Briac Houtteville: I believe that a 50/50 split is a reasonable estimate for the current state of the market. On the one hand, we have the LP-led market, which consists of portfolios of LP stakes that have been steadily growing over time. This can be considered the historical part of the market, as more LPs have begun to use the secondary market as a tool for portfolio management. In addition, new LPs are constantly entering the market.

On the other hand, we have the GP-led market, which has seen a more recent uptick in activity in terms of volume, starting in 2017/2018. While GP-led transactions have existed for a long time, it is mainly the larger GPs and those with trophy assets that have been driving growth in this market over the past four to five years. This growth has been driven by liquidity needs, with GPs initiating these transactions as a means of managing their portfolios. These transactions tend to be more concentrated, and therefore the growth of the GP-led market will largely depend on the amount of dry powder specifically dedicated to these types of transactions going forward.

There will always be a significant supply of GP-led opportunities, as GPs are keen to identify their winners and take them through the next phase of growth, given their familiarity with the management team. However, the amount of dedicated dry powder raised from secondary funds will ultimately determine the extent to which this market continues to grow. At present, a 50-50 split between LP-led and GP-led transactions seems appropriate, but this will change depending on how much capital is raised specifically for GP-led transactions going forward.

Wikram Chowdhury: From your experience, do you observe a common denominator that contributes to the success of GP-led secondary transactions in which you invest?

Briac Houtteville: I am finding that the questions are becoming more challenging as we proceed (laughs).

In our approach to GP-led transactions, we prioritize a framework of key characteristics. Our top priority is to partner with the best GPs and ensure they can lead the next phase of growth for the asset. This involves assessing whether the GP is not only of high quality but also the right fit for the asset and its future plans, particularly in the mid-market. Portfolio Advisors' platform is distinguished by our proactive engagement with top GPs from the very beginning of their fund's inception, facilitated by our primary team.

One of the advantages of GP-led transactions is that they carry no new deal risk, which is an attractive proposition.

We also prioritize strong alignment between the GP and the asset. To achieve this, we look for a substantial GP commitment, such as reinvesting most of the carry from the sale of the asset back into the deal. We also seek strong management teams who are willing to reinvest heavily, and we note that in an increasing number of GP-led transactions, the GP's new fund also invests. When these elements are present, we see a stronger alignment between the GP and the asset, particularly because the GP is often the most knowledgeable about the asset, having worked with it for an extended period.

In terms of asset characteristics, we look for resiliency and predictability in non-cyclical sectors such as business services, software, industrials and healthcare. We also prioritize strong cash flow profiles and low levels of leverage.

Team due diligence is an additional element. We spend time with the management team, like in an M&A process, to understand its vision and plan for the asset. This is critical in our assessment of the potential for a successful GP-led transaction. When all these elements are combined, we believe we have a promising GP-led opportunity.

Wikram Chowdhury: Perhaps the shared rationale for GP-led secondary transactions in the buyout space is the belief among GPs that they can extract more value from the companies they place in the GP-led secondary transactions rather than sell it through an exit today, which may be attractive to competitors or strategic buyers. Would you agree that this is a typical motivation behind such transactions?

Briac Houtteville: That is the plot we like. Our preferred rationale involves identifying assets that possess strong market potential and can be sold at an attractive price in the near future. However, we acknowledge that each GP may have its own unique reasoning when it comes to identifying investment opportunities. It is important to note that we rarely come across identical continuation vehicle candidates, and we strive to identify and work on those that align with our preferred rationale.

Wikram Chowdhury: Do you think the current fundraising challenges of traditional primary funds will also impact the fundraising for secondary funds?

Briac Houtteville: The market for fundraising is currently facing a number of challenges, including lower liquidity, decreased levels of distributions, and the denominator effect. While these factors have led to an abundance of supply in the secondary market, they may also indirectly impact fundraising. However, the secondary market has grown to such a size that it now offers a unique risk-return profile within the private equity space, with highly attractive returns on a risk-adjusted basis and regular liquidity. As a result, institutional investors are increasingly allocating a portion of their portfolios to secondary investments. At Portfolio Advisors, we view this market as a compelling opportunity, with significant interest and dry powder continuing to grow in line with market expansion. In addition, we observe a trend of more retail investors entering the private equity market in various ways, and we believe this will become a significant component of the investor community going forward. The diversification and liquidity profile of secondary funds makes them an attractive option for these types of investors.

Wikram Chowdhury: Given our audience's interest in private equity careers, what guidance would you offer to students? Specifically, what skillsets should students aim to cultivate in order to excel as investors and reach their full potential?

Briac Houtteville: Developing a strong fundamental understanding of financials is crucial for anyone looking to start a career in private equity. During my time at EY, I focused on transaction services and worked closely with the M&A team that served financial sponsors. This gave me valuable exposure to buyouts and how GPs and sponsors analyze companies in detail. Additionally, I interacted with consultancy firms that handled management and commercial due diligence, which helped me gain a broader understanding of different sectors and transaction dynamics. Investment banks, such as during my time at Greenhill Cogent, will also provide you with additional and detailed knowledge of transaction processes and modelling in addition to financials.

To succeed in this industry, one needs to go through this process of learning and gaining a detailed understanding of the market. It is important to be curious and go the extra mile to gain a deeper understanding of the industry, beyond just the fundamentals. Once you have a general overview of the market, you can make a differentiated move, which is crucial in private equity.

Differentiation was key for me and led me to focus on the secondary market, which was relatively unknown at the time. It was a risk, but I believed in the decision and had the confidence to make that call because of the fundamental skills I had developed earlier in my career. When you are in a nascent market, there are not many reference points, so having that foundational knowledge and the confidence to make decisions is critical.

Ultimately, to build a successful career in private equity, one needs to be passionate, curious, and willing to put in the effort to build a strong foundation. That foundation, along with a deep understanding of the market and the ability to make differentiated moves, will help you succeed in this growing industry.