

Unlocking value: The benefits and challenges of private equity secondaries in Canada

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As large institutional investors seek additional tools to manage their portfolios, the Canadian private equity secondaries market has continued to mature. Secondaries offer private equity investors (once dominated by pension funds and other institutional investors), a unique opportunity to access better liquidity, enhance portfolio diversification, and increase potential for higher returns. Furthermore, the rise of private equity access funds - which are directed at high-net-worth investors - has created a new investor base that wishes to access private investments via the secondary market. With secondaries poised to play a more significant role in the private equity investment landscape, we are highlighting the benefits and challenges of these opportunities for Canadian investors.

What are private equity secondaries?

Private equity secondaries transactions involve buying and selling existing private equity investments, either directly or through the buying and selling of interests, typically in the form of limited partner (LP) interests, in the funds that hold those investments. These transactions can take many forms, including the sale of entire fund stakes, of individual assets and/or the restructuring of fund portfolios that would allow existing investors to continue to hold some or all of their interest.

Historically, secondary market transactions were used to unlock some liquidity for investors in funds that were no longer actively managed or invested in new opportunities, but still held assets with no short-term prospects of sale (zombie funds), **though such sales were typically at a discount.** However, the secondary market has evolved and is being used to allow new investors access to, and to provide liquidity (at a premium) for investors in, mature blue chip PE funds.

Typically, private equity funds have relatively long investment horizons (e.g., five-to-ten years), meaning that investors are not able to dispose of their interests or cash out of their positions prior to the end of the term of a fund. With the growth of the secondaries market, we see an opportunity for existing investors to unlock liquidity. Secondaries also bring a unique value proposition for new investors, allowing them access to established private equity portfolios without the long lock-up periods and risk profile typically associated with private equity.

Private equity secondaries have been growing globally in recent years. Total global secondary transaction volume grew from US\$37 billion in 2016 and reached a record high of [US\\$162 billion in 2024](#).

The Canadian private equity landscape and private equity secondaries

Canada has become an attractive destination for private equity investments. Despite the recent challenges posed by global and domestic macroeconomic conditions, particularly U.S. tariffs and the threat of a recessionary market environment, Canada has seen steady private equity market activities.

Additionally, the country's diverse range of industries, from natural resources to technology, offer various opportunities for private equity investors.

As the private equity market develops in Canada, so too have secondary transactions.

Several key players contribute to the dynamic Canadian landscape: institutional investors, such as pension funds, endowments, and insurance companies engage in secondary transactions to manage their portfolios actively and optimize their asset allocations. Specialized secondary market funds, both domestic and international, also play a crucial role as buyers acquire portfolios or individual stakes from sellers seeking liquidity or portfolio adjustments.

Structure of private equity secondary transactions

Secondaries can either be led by an LP or by the general partner (GP) of the fund.

In an LP-led transaction, the LP takes the initiative to sell its stake in a private equity fund. This may be driven by factors such as the need for liquidity, portfolio rebalancing, **or changes in the LP's investment strategy**. **The LP typically controls the sale process**, including the selection of a secondary buyer and negotiation of terms. However, private equity funds have restrictions on the transfer of LP interests, and the GP typically has the final say as to whether to approve an LP-led sale.

Conversely, a GP-led transaction involves the GP actively managing a secondary sale process of LP interests or driving the restructuring of an existing fund (for example, through continuation funds, preferred equity options, etc.). Motivations for a GP-led transaction can include accommodating investor demands for unlocking liquidity, **optimizing the fund's portfolio by extending its life, providing an exit for specific assets, or adjusting the fund's strategy**. This approach allows the GP to take a more proactive role in shaping the fund's future and aligning it with the interests of existing and new investors.

The variety of available transactions highlights the adaptability of the secondary market, allowing participants to tailor their strategies to meet diverse objectives.

Benefits of private equity secondary transactions

Investors may find private equity secondaries particularly attractive for the following reasons:

- **Liquidity for existing investors.** Traditional private equity investments involve extended holding periods, often spanning a decade or longer, restricting investors' access to their capital. Secondaries offer an avenue for early liquidity, enabling investors to unlock value and redeploy funds according to their evolving financial needs or market opportunities. This liquidity aspect becomes especially crucial during economic downturns or when investors seek to capitalize on emerging trends and avoid risks.
- **Portfolio optimization.** Buyers can strategically select specific funds or assets that align with their investment goals and risk appetites. They can divest from underperforming assets or sectors, reallocate capital to align with shifting market dynamics, and enhance overall portfolio diversification.
- **Discounted valuations for buyers.** Secondary transactions may involve assets priced at a discount to their intrinsic value, presenting opportunities for buyers to acquire assets on favorable terms, thereby enhancing future returns. However, depending on the nature of the secondary, assets may be priced at a premium in a secondary sale, for various reasons.
- **Access to established funds and steady income stream.** Buyers may be able to access established portfolios with existing assets, potentially reducing the time it takes to deploy capital compared to primary investments. Additionally, investors may be able to gain exposure to mature income-generating assets, offering a more stable cash flow profile compared to early-stage investments.
- **Risk mitigation and operational visibility.** Secondary market transactions may allow investors to mitigate risks associated with blind pool commitments, as they can evaluate the historical performance of existing portfolios and gain better insight into the operational performance of underlying portfolio companies, compared to investing in blind pools.

Challenges and additional considerations for private equity secondaries

Despite the benefits of private equity secondaries, investors should be aware of some of the associated challenges, which include:

Valuation. Unlike publicly traded companies with readily accessible market prices, private equity investments are often less transparent, have sparse financial disclosure, and lack direct market comparables.

Liquidity. The illiquid nature of private equity investments means there is no readily available market for these assets, requiring subjective assessments and reliance on various valuation methodologies.

Pricing. The reliance on future cash flows, uncertainties in exit strategies, and the variability of individual deal structures contribute to pricing complexity, as do an uncertain interest rate environment and other macroeconomic factors that may make valuation and pricing particularly challenging.

Other. Due diligence requirements and fund manager relationships are additional challenges that merit attention. In a GP-led sale process, there are transparency factors to consider. We are also seeing increased regulatory scrutiny of these types of transactions (for example, effective March 2025, the United States Securities & Exchange Commission introduced mandatory fairness opinions for applicable adviser-led private equity secondary transactions) and this heightened regulatory attention should be carefully evaluated.

Overall, notwithstanding these challenges, private equity secondaries offer investors a unique opportunity for existing investors to obtain better liquidity and an opportunity for new investors to access PE investments, enhance their portfolio diversification and increase their potential for higher returns. As the market matures, secondaries are poised to play a more significant role in the private equity investment landscape in Canada and abroad.

For more information on private equity secondaries, or to discuss any of the topics referenced in this article, please reach out to any of our authors or key contacts below.

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