KEYNOTE INTERVIEW

# Remaining constant in a changing market

*The secondaries market has grown rapidly over recent years, but the principles of successful investing are the same as they have always been, says Michael Granoff of Pomona Capital*

With exit activity remaining slow, an estimated $3.2 trillion of capital is stuck in buyout portfolios alone, according to Bain & Co figures. That presents a significant opportunity for secondaries funds as LPs and GPs seek ways to unlock liquidity to fund capital calls, make investments and raise new funds. It's hardly surprising that the bets are on for a record year for secondaries deal volume.

We spoke to secondaries veteran Michael Granoff, CEO of Pomona Capital, to get his perspective on what's happening in the market, including the impact of capital inflow from retail investors on secondaries transactions.

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Here's what he had to say.

**Q With many predicting that secondaries are set for a record year by volume, what's your take on activity in 2024?**

It's clear that this year has been quite busy. We've already reviewed nearly $100 billion in dealflow, and the final quarter is expected to be even busier, potentially bringing the market total to $140 billion in 2024. This isn't surprising as the supply of secondary deals stems from two key factors: the amount of capital flowing into private equity and the turnover rate. Private equity funds now manage trillions instead of billions, and turnover rates have increased due to both cyclical pressures for liquidity and a broader acceptance of the secondaries market. Today, there are two sources of supply: when I started in 1994, it was solely limited partners, but now we also see general partners involved.

The demand side is just as crucial. As a buyer, we are rigorous on the quality of assets we pursue and the prices we are prepared to pay. We are not interested in buying the generic market.

**Q What will be the biggest motivating factors for sellers in 2025, and will they be any different from what we've seen over the past year?**

The world can be messy and noisy at any time, but it feels particularly so right now. GPs and LPs have been affected by a material lack of liquidity for a while now and we've seen some smart responses to generating liquidity and some that are perhaps less prudent, such as adding more leverage.

Liquidity is beginning to improve, with ours increasing by about 20 percent so far this year compared to 2023, and we expect it to continue to ease over time. Estimates suggest there is a backlog of around 28,000 companies in private equity portfolios that are waiting to be sold. The longer the squeeze lasts, the more it will push GPs and LPs to sell as funds reach the end of their lives and as LPs face capital calls they are struggling to meet. This may mean the turnover rate increases further, especially as investors who have not been sellers before start to access the market, joining the growing number of serial sellers.

**Q Would you say it's a good time to buy?**

Timing the market is often a misguided effort – we don't have a better crystal ball than anyone else. We are investing our funds over several years, not just a few quarters. Currently, there are various factors at play, including a moderation in private equity valuations relative to public markets, which suggests we're in a less overheated market than we were two years ago. Additionally, IPOs are being priced lower than private market valuations, creating opportunities to purchase companies at a discount. This makes it a great time for smart decisions, but not for reckless ones. It's essential to navigate the market with caution and avoid making generic bets.

For Pomona, that means being disciplined and pacing our investments. We've committed around $1 billion this year, or 1 percent of our deal volume – consistent with our historical execution rate. We believe that our strategy and mid-size position enables us to make informed choices and maintain consistent buying.

One thing many people are not focused on right now is that dispersion of returns will increase over the coming period. The better companies can get liquidity, but the not-so-great businesses will have a harder time and they'll be left standing in a game of musical chairs. We see this in our own portfolio – there is a difference even between the very best companies and those that are just high-quality.

> *"The era of the investment boutique has passed, as our market has become much larger and more complex"*

**Q How do you see the growth of retail investors in private equity?**

The retail opportunity represents a more revolutionary shift than an evolutionary one. It mirrors the changes in the institutional space 30 years ago when regulatory reforms allowed pension funds to invest in private equity, fuelling the growth of the asset class. While there may not be a single catalyst for the growth in retail, the influx of capital will be substantial for a few reasons. First, most retail investors currently have little to no exposure to private equity. Additionally, they are beginning to recognise, much like institutions did, that alternatives are no longer just alternatives; they are essential components of core portfolios. Together, these factors will drive momentum in the growth of the retail sector.

**Q What advice would you offer to retail investors new to this space?**

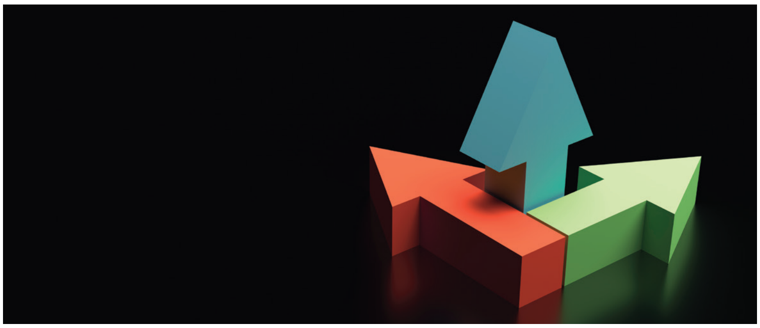
As retail investors move into private equity, we believe their investment criteria should be similar to those of institutional investors: they should own a diverse portfolio of high-quality assets with a healthy risk-return balance that is likely to generate good returns over time, and not expose them to inordinate risk. We believe that a differentiated secondaries strategy can be a prudent, attractive opportunity for individual investors.

It is not so easy to create and manage private equity structures for individual investors. We thought our model and approach to private equity investing had the potential to uniquely solve for common issues facing individual investors and their investment goals. In 2015, Pomona launched Pomona Investment, the first diversified secondaries-focused registered investment fund that now has nearly $2 billion of assets under management.

**Q Given their differing characteristics, how do you approach building a portfolio that includes both LP-led and GP-led deals?**
We are agnostic about the type of deal. However, we are guided by the principle that LPs invest with us to access a diversified portfolio of high-quality assets, acquired at a significant discount, with enhanced liquidity and a lower risk profile. When we identify such opportunities, we pursue them aggressively, which often means focusing on LP-led deals.

It can be argued that most GP-led deals do not meet this criterion because they often offer minimal discounts, vary in quality, lack diversification, and have liquidity that is far out. When GP-led deals first emerged, they mostly involved troubled funds and assets and were not appealing transactions to us. Today, where there are some high-quality GP-led deals, they can be an exception to our rule.

Unlike with LP-led deals, most performance data for GP-leds is currently based on unrealised portfolios. An investor needs to understand how aligned the GP is with you as a buyer, dig into the asset or assets deeply, and understand the GP's motivations. If interests are aligned, it is likely you will have a greater chance of achieving good results in private equity; without alignment, however, things can unravel quickly.



*"It's essential to navigate the market with caution and avoid making generic bets"*

**Q What effect is the increase in capital from retail investors having on the secondaries market?**
The secondaries market is already competitive, and most firms offering retail products are not new players. What we've seen so far is that retail capital is depressing quality as opposed to discounts – these structures need discounts for quarterly returns.

A risk for the retail funds is that the need to report returns quarterly can lead them into the mutual fund trap. If they chase short-term returns and make short-term decisions, that runs counter to the long-term nature of private equity.

**Q As you celebrate your firm's 30-year anniversary, what are the most important lessons you have learned, and how do these position the organisation for the future?**
Maintaining success over the long term is challenging, and survival sometimes is underappreciated. Over a 30-year span, you must make numerous decisions and ensure that more of them are correct than incorrect. This demands a values system that people believe in and that remains stable. However, since change is constant, those values must enable the organisation to adapt to its environment.

Today, there's a lot of excitement around technology and data structures, but the truth is that no one possesses truly proprietary tools. We all share a similar toolbox; the key differentiator lies in how we utilise it.

I believe the era of the investment boutique has passed, as our market has become much larger and more complex. Our business must adopt a more corporate structure while continuously building the right blend of systems and agency.

Systems help us navigate complexity and execute effectively, while agency empowers individuals to make decisions and drive progress. We need to marry both for success. ■