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Taking a More Direct Approach

W Capital's oversubscribed new fund demonstrates the growing interest in direct secondary investments.

Everyone agrees that the secondary market for interests in private equity has been growing rapidly, and that most of the activity has been directed toward the purchase of limited partnership stakes in buyout and venture funds. But interest in purchasing portfolios of direct private equity and venture investments is gaining ground.

One indication of that interest came this week, when New York City-based W Capital Partners announced that the firm had raised \$172 million so far for its new fund, W Capital Partners LP. It is expected that the fund will soon reach \$250 million, significantly more than the firm's original target of \$150 million. That's in addition to \$50 million it had raised in 2002 and 2003.

"Our business is highly specialized," says David Wachter, managing director of W Capital Partners. "We buy portfolios of direct investments, actively manage the underlying companies, and selectively support them with follow-on capital." That makes W Capital one of the very few funds that focus exclusively on buying directs. So far, W Capital has bought six private equity portfolios and is continuing to look for opportunities across venture, growth equity and buyout.

According to Wachter, much of the deal flow in the directs business has come from corporations and financial institutions looking to exit or reduce their direct private equity exposure. He also expects more deal flow to be driven by the mutual decision on the part of general and limited partners to liquidate funds. "We provide GPs the ability to generate immediate liquidity for the entire portfolio by selling it directly into the secondary market, then distribute the money to their investors and be able to close the fund."

In Wachter's view, directs are becoming a more important part of the secondary market; indeed, over the long term it may approach the secondary LP business in market share. "Unlike the LP business, you can't buy and hold," he notes. "In the direct business you've got to be willing to work with every portfolio company and put up the necessary follow-on capital. It's very labor-intensive, so you've really got to want to be in it."