More nuance around first-time funds

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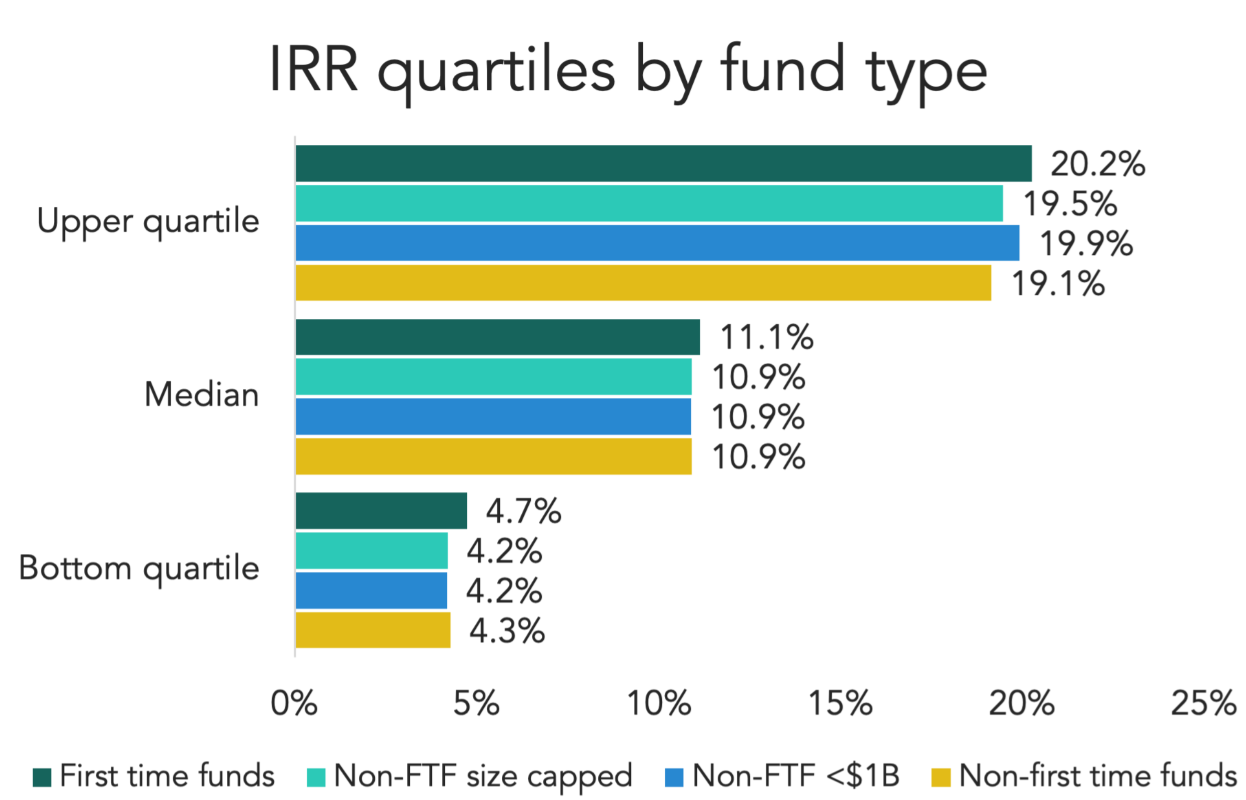

Download PitchBook's Report here.

Past PitchBook research has found statistical outperformance for first-time PE funds compared to follow-on funds. That note was one among many studies that arrived at the same conclusion: first-time funds tend to do relatively well, for a variety of reasons. PitchBook just released a follow-on note (so to speak) which adds more nuance to the discussion.

Most importantly, our data suggests that first-time outperformance levels are minimal in aggregate and sporadic in terms of timing. Their outperformance is about 100 bps or less compared to more established funds, a pattern that holds for upper quartile, median and bottom quartile metrics. First-timers have just over a 25% chance of returning 5% or less in IRR, which is marginally lower than more established funds. They do, however, deliver IRRs above 25% more frequently than the rest, 18.3% of the time. The old narrative of "hungry newcomers" holds true, but the results don't show up across the board. LPs, as they always do, have to select wisely in promising managers, which is one of the primary motivators of investing in first-time funds—getting in early and developing a strong relationship with new GPs. Our research shows, however, that IRRs are a mixed bag for most first-time funds. They may take longer to exit portfolio companies, or they might not be as adept at dividend recaps or capital call facilities compared to established managers.

Few first-time funds were raised last year, as expected. Fund closes shrank from 47 in 2019 to only 25 in 2020. LPs were more focused on re-upping commitments with familiar GPs, especially at the high end of the market. How well the 2020 vintage does, only time will tell. PitchBook, meanwhile, will continue researching the dynamics of first-time fundraises. Future notes will look at attrition rates, style drift, step-up sizes, and whether second, third, and later funds deliver the outperformance LPs are looking for.

(Past performance is no guarantee of future results.)