

## Beyond Liquidity: Why Continuation Vehicles Have Become a Core Portfolio Management Tool

Continuation vehicles have become one of the most important strategic tools in private equity. Once viewed primarily as a liquidity solution, they are now a core portfolio management strategy that enables sponsors to balance investor liquidity while extending ownership of their highest-quality businesses.

The shift reflects more than a challenging exit environment. Private equity has entered a fundamentally different market characterized by longer hold periods, lower distributions to investors and fundraising that increasingly depends on realized performance rather than unrealized value.

Rather than serving as an alternative to a traditional exit, continuation vehicles have become a strategic option that allow sponsors to provide liquidity, retain ownership of exceptional assets and continue executing their investment strategy.

# Three Structural Forces Reshaping Private Equity

Continuation vehicles are not simply benefiting from cyclical market conditions. Rather, they are responding to structural changes reshaping private equity.

- 1 Exit activity has not kept pace with private equity growth.** Private equity assets under management have expanded dramatically over the past decade, while traditional exit channels—including sponsor-to-sponsor transactions, strategic acquisitions and IPOs—have struggled to absorb the growing inventory of private equity-backed companies.
- 2 Lower DPI has created fundraising challenges.** Limited partners (LPs) place greater emphasis on realized distributions than at any point in recent years. With realizations lagging, LP liquidity has tightened, fundraising timelines have lengthened and re-up decisions have become increasingly selective.
- 3 Longer hold periods create additional value creation opportunities.** Many private equity-backed businesses continue to have substantial upside beyond a traditional five-year investment horizon. Additional time and capital can unlock value through acquisitions, expansion, operational initiatives and technology investments.

## Continuation Vehicles as a Strategic Portfolio Management Tool

The strongest continuation vehicle candidates are often the businesses that sponsors are least eager to sell. Rather than exiting because of fund-life considerations, continuation vehicles allow sponsors to benefit from continued future growth while providing existing investors with a liquidity option.

Sponsors most commonly use continuation vehicles to fund acquisitions, extend ownership of exceptional assets and optimize exit timing when current market conditions do not fully reflect long-term value.

Increasingly, sponsors are evaluating continuation vehicles alongside traditional sale processes rather than viewing them as a fallback for an unsuccessful sale process. Considering both options early allows sponsors to pursue the strategy that best aligns with the company's long-term potential and broader fund objectives.

# What Separates Successful Continuation Vehicles?

As the continuation vehicle market has matured, investor expectations have evolved significantly. Today’s investors evaluate opportunities with rigor comparable to a traditional buyout investment, requiring comprehensive diligence, detailed operating information and a clearly articulated value creation plan.

Approximately half of continuation vehicle transactions ultimately fail to close—not for lack of investor demand but because of investor selectivity. Investors prioritize continuation vehicles that include:

| Characteristic                     | Why It Matters                                                                                                                                                       |
|------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| High-quality, market-leading asset | Businesses with sustainable competitive advantages, resilient business models and consistent operating performance are best positioned to attract investor interest. |
| Strong sponsor alignment           | Sponsor conviction in the next phase of growth remains one of the strongest indicators of investor confidence.                                                       |
| Defensible valuation               | Alignment among new investors, selling LPs and the sponsor is essential to achieving a successful outcome.                                                           |

Investors also favor businesses with durable cash flows, experienced management teams, conservative leverage profiles and multiple credible exit alternatives.

The strongest processes begin well before a transaction launches. Sponsors that prepare diligence materials early, articulate a clear investment thesis and establish realistic valuation expectations are generally better positioned to execute efficient, competitive processes.

## Three Questions Every Sponsor Should Answer Before Pursuing a Continuation Vehicle

- 1
- What strategic objective are you trying to achieve?**

Successful continuation vehicles begin with a clearly defined objective, whether improving DPI, funding growth, extending ownership of a high-performing asset or supporting future fundraising. Establishing the right strategy early helps sponsors pursue the path most likely to maximize value.

2

**Is the asset truly institutional quality?**

Not every portfolio company is an appropriate continuation vehicle candidate. Investors prioritize businesses with:

- Market leadership
- Predictable growth
- Strong margins
- Clear remaining opportunities to compound value

Asset quality remains the single greatest determinant of transaction success.

3

**Will the valuation withstand investor scrutiny?**

Successful continuation vehicles require alignment among new investors, existing LPs and the sponsor. Valuations should be supported by current market data, and sponsors should be comfortable investing into the continuation vehicle at the new entry price. Transparent pricing and disciplined execution remain essential to building investor confidence.

## When a Continuation Vehicle May Not Be the Right Solution

Continuation vehicles are not the right solution for every portfolio company. The strongest continuation vehicle transactions are those where sponsors can clearly demonstrate that continued ownership is expected to create greater long-term value than an immediate sale.

Sponsors should carefully consider alternative exit options when:

Strategic buyers are willing to pay premium valuations

Valuation expectations materially exceed current market conditions

Management succession or operational challenges create uncertainty

The business lacks a clearly identifiable next phase of growth

# Why Continuation Vehicles Are Increasingly Relevant for Lower Middle Market Sponsors

Although much of the market's attention has focused on large-cap transactions, many compelling continuation vehicle opportunities exist in the lower middle market. These businesses often offer stronger organic growth, significant opportunities for operational improvement, highly fragmented markets and multiple future exit alternatives. Because many remain earlier in their value creation journey, sponsors can continue compounding value over an extended ownership period while accessing an increasingly deep pool of continuation vehicle capital.

## Looking Ahead with Lincoln

Continuation vehicles have become a permanent feature of private equity and an increasingly important portfolio management tool.

As holding periods lengthen and fundraising remains tied to distributions, leading sponsors are evaluating continuation vehicles earlier alongside traditional strategic alternatives—not as a replacement for a sale but as a tool to selectively maximize value.

Sponsors that embed continuation vehicles into their portfolio management strategy will be better positioned to optimize liquidity, retain ownership of high-conviction assets and deepen LP relationships.

Lincoln International's integrated approach across Private Funds Advisory, Mergers and Acquisitions, Capital Advisory and Valuations Groups, together with deep sector knowledge and experience, helps sponsors holistically evaluate strategic alternatives, execute continuation vehicles and deliver tailored capital solutions that maximize value across the investment lifecycle.

Ready to discuss the opportunities ahead for you?

Connect with a senior professional at [connect@lincolninternational.com](mailto:connect@lincolninternational.com)