Private Equity

Private equity is an alternative investment that invests money in privately held companies or focuses on taking public companies private via a buyout strategy. Private Equity firms have bought out many public technology companies due to their struggles in the public markets. For example, Thoma Bravo has spent over $15 billion this year purchasing technology companies to further their presence in the space.

Private equity firms typically earn their money through fees charged to the investors or institutional clients invested in the firm. The fees for these firms tend to be higher due to the ability to invest in non-public companies, which could have more potential for gains in the future. Most companies that the Private Equity firms focus on have a “liquidity event” in the future. This means that the company will either be acquired by a large company that sees synergy between the two businesses, or the company will go to the public market via an IPO, where public investors can buy shares on the open market. These liquidity events typically help early investors exit their positions as certain companies (like Private Equity firms) may not want to hold publicly-traded companies in their portfolio and wish to move their capital to other names with higher potential.

To directly invest capital into Private Equity firms, investors must be accredited by the SEC and satisfy specific requirements to invest in these types of investments. An accredited investor must have over $200,000 ($300,000 joint) in average annual income, have a net worth of over $1 million (individually or jointly), or be registered as a financial broker or adviser. These guidelines protect investors from some inherent risks that come with private equity firms and private companies. Although some private companies could turn out to be the “next big thing,” many businesses fail and do not return any capital to shareholders.

Many private equity firms also require investors to invest a minimum amount for their capital to be accepted and used. If an investor is not able or willing to put up the minimum amount, the private equity company will not use its money as part of its assets under management. Investors must be willing to keep their funds tied up for an extended period for some companies held to reach their liquidity events. Remember that the companies owned are not public, and their share prices will not update every second of the day. Because of this, risk tolerance and patience are two key traits required for private equity investing.