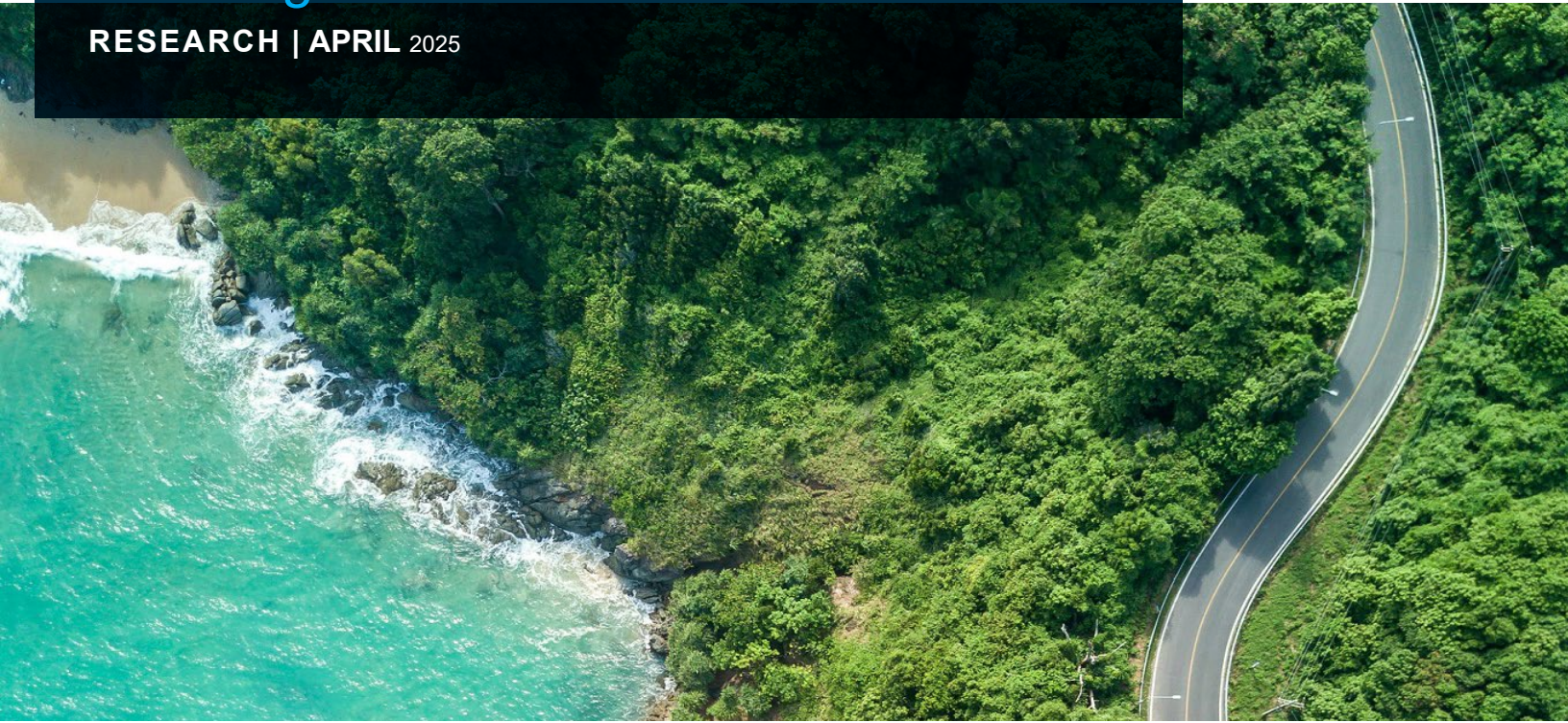


# Investing in Private Markets

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*Private market investments are increasingly playing an important role in the portfolios of today's investors. By allocating a percentage of their portfolios to private markets, investors may enhance diversification while potentially realizing higher risk-adjusted returns. To assess whether investing in private markets might be an effective way to pursue your financial goals, the first step is to learn more about this versatile asset class.*

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## What Are Private Markets?

Private market investing refers to the investment in privately owned companies versus publicly owned companies. Private market investments could be equity or debt investments in companies that are not traded on public exchanges.

When being offered to investors, private market investments are generally structured in the form of limited partnerships that usually consist of 10 to 20 investments in individual private companies. The managers of these limited partnerships are referred to as general partners and investors are referred to as limited partners.

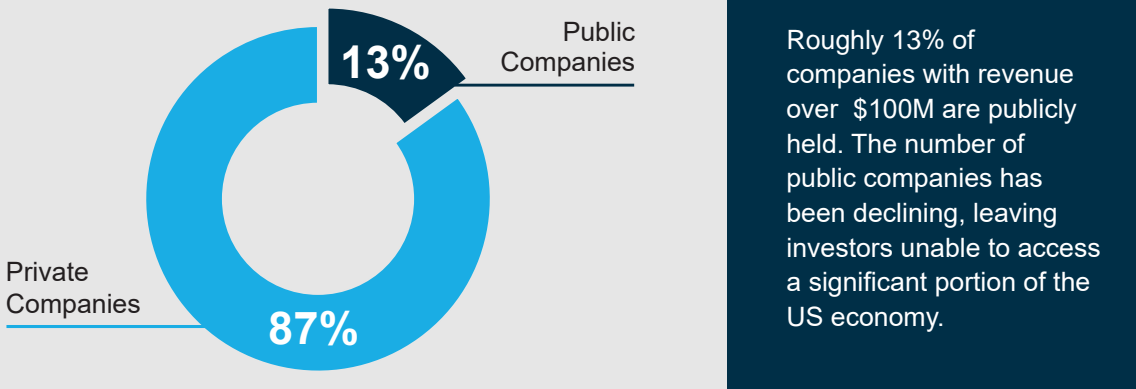
Private markets do not have regulated exchanges, and these investments are not registered with the Securities and Exchange Commission (SEC). Instead, transactions are conducted directly between interested parties.

## What's Driving Investment in Private Markets?

Investing in private markets creates new opportunities for investors. That's because there's a larger universe of available investment opportunities in private markets than in public markets. There are more than 19,000 private companies in the US with annual revenues over \$100 million.<sup>1</sup>

Meanwhile, the number of public companies in the US has fallen by nearly half since the late 1990s. After peaking at more than 8,000 companies in 1996, the number of domestically publicly traded companies available on the major US stock exchanges has declined to less than 4,000.<sup>1</sup>

<sup>1</sup> Source: S&P Capital IQ and Statista; data as of Q1 2023, [NYSE and Nasdaq: listed companies comparison Q1 2023](#) | [Statista](#)



Roughly 13% of companies with revenue over \$100M are publicly held. The number of public companies has been declining, leaving investors unable to access a significant portion of the US economy.

**FIGURE 1**  
**Percentage of US Private and Public Companies**

Source: S&P Capital IQ data as of December 2022; Statistics of US businesses; Bain & Company, Global Private Equity Report, February 27, 2023.

What's driving the decline? Mergers and acquisitions between public companies have contributed, as well as a wave of bankruptcies. But more telling are these additional reasons:

- A decrease in the number of Initial Public Offerings ("IPOs") since 2000,<sup>2</sup>
- An increase in the number of public-to-private transactions;<sup>3</sup> and
- More and more companies are simply choosing to remain private.

<sup>2</sup> Source: Stock Analysis, [IPO Statistics and Charts - Stock Analysis](#)

<sup>3</sup> Source: Dealogic, [Private equity deal-making hits 10-year high](#) | [Dealogic Insights](#)

## Why More Companies Are Choosing to Remain Private

The challenges (versus the reward) of becoming a public company today have tilted the scales in favor of staying private.

Additional governance requirements and the associated higher costs are one significant reason. The Sarbanes-Oxley regulation, enacted in the wake of a series of corporate scandals in the early 2000s, resulted in increased regulation of public companies. This and other new rules and regulations, including heightened accounting and auditing requirements, pile on greater administrative burdens and increase costs. The average recurring annual costs of operating as a public company now exceed \$1 million a year, according to PricewaterhouseCoopers.<sup>4</sup>

Meanwhile, business owners have increasingly valued the inherent benefits of staying private. They can focus on long-term strategic objectives to pursue company value without being distracted by quarter-to-quarter performance results. Remaining private gives executives greater control and flexibility over their decisions and business development as they grow and compete.





And as business executives look to the private markets for financing to expand their businesses rather than undertake IPOs, they find themselves supported by private equity firms that have a vested interest in helping their companies grow and succeed.

The businesses in today's private markets are often established and profitable, rich in assets, with a solid track record of providing core products and services. They typically reflect the real, broader economy, and in many cases, are the more solid and promising companies in which to invest. Private investment markets, in turn, have become long-term oriented, focused on financing strong and proven companies.

<sup>4</sup> Source: Pricewaterhouse Coopers, Nov. 2017. Considering an IPO to Fuel Your Company's future? [Considering an IPO to fuel your company's future? \(pwc.com\)](https://www.pwc.com/considering-an-ipo-to-fuel-your-company's-future)

## Private Market Asset Classes

The four primary asset classes in private markets include:

 <p><b>Private Equity</b></p> <p>These are direct equity investments in non-publicly traded companies. These range from large buyouts of established firms to venture capital deals supporting innovative start-up companies and small businesses.</p>	 <p><b>Private Credit</b></p> <p>These investments provide capital to privately owned companies in the form of direct lending and other types of private debt. These loans can help earn incremental yield away from traditional fixed-income investments and are typically backed by senior claims on company cash flows or assets, helping to give the lender more security.</p>	 <p><b>Private Infrastructure</b></p> <p>These are equity and debt investments in private infrastructure assets, such as roads, railways, airports, utilities, satellites, cell towers and data centers. Infrastructure assets provide essential services that underpin the structure of an economy or society. As an asset class, it provides investors with stable, often inflation-protected returns.</p>	 <p><b>Private Real Estate</b></p> <p>These are private investments in real estate, such as commercial and residential buildings. Bricks-and-mortar assets, such as commercial and residential buildings, have a long lifespan and may provide inflation protection through rental increases.</p>
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## The Potential Benefits of Private Market Investments

Investors allocate a percentage of their portfolios to private market investments with the objective of enhancing return and lower risk through diversification. Private market investments can help investors:

### Capture Higher Potential Returns

Private market investments may provide access to innovative, high-potential private companies in their early stages of growth, providing opportunities for higher long-term returns. And private markets typically provide a return premium for their lack of liquidity.

### Increase Diversification

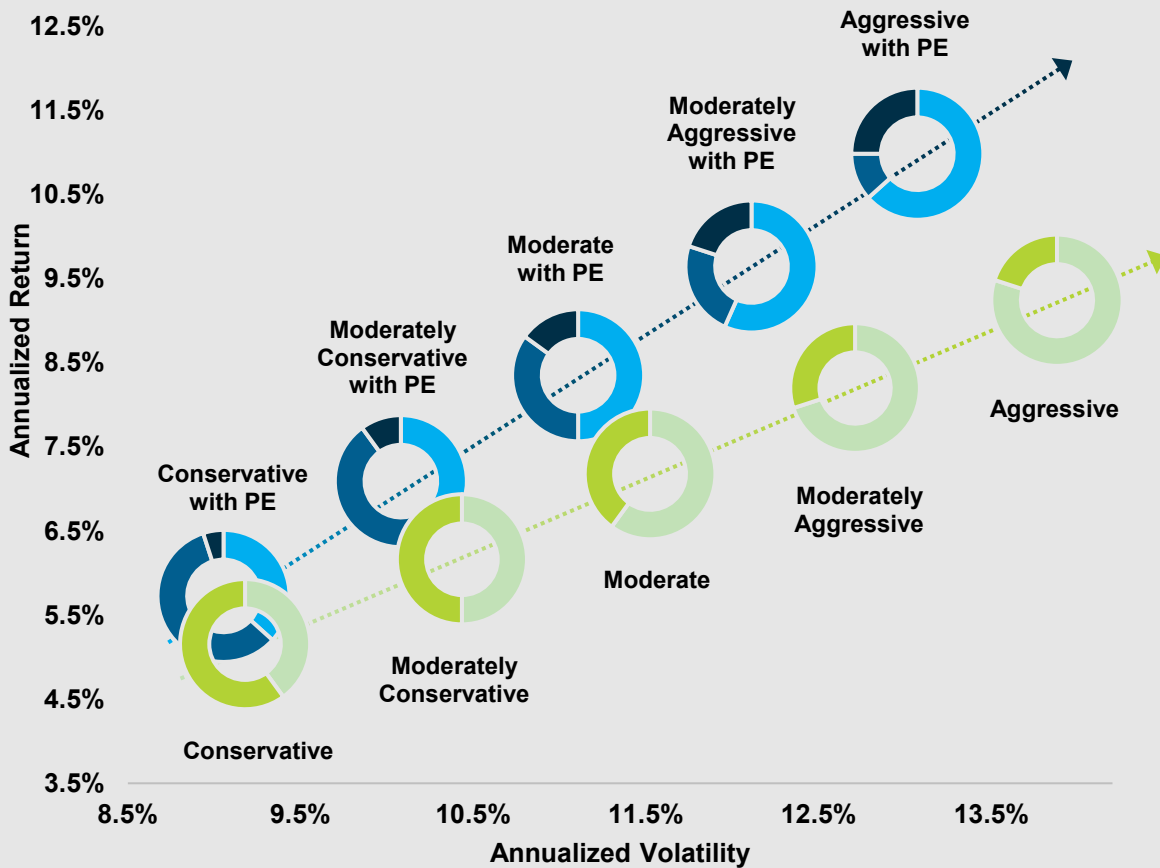
Spreading investments over a wide variety of investment options – including those that represent the broader economy – may be healthier for a portfolio. As mentioned earlier, the majority of the U.S. economy is made up of private companies. Only a small percentage of companies are publicly held. Private investing provides access to different segments of the markets not available through public investments.

### Potentially Reduce Volatility

Private market investments can help build more resilient portfolios designed to provide protection during market turmoil. While public market investments are valued daily, private assets are typically valued on a quarterly basis, potentially smoothing out overall performance. Private investments provide the potential to gain diversified exposure to strategies and managers that reflect lower correlation to traditional asset classes; that is, private market investments may not be as closely tied to the ups and downs of public markets.

# The Impact of Private Equity on Portfolio Optimizations

Investors allocate to private equity investments with the objective to enhance returns and/or lower risk through diversification.



## Portfolio Weight Mixes

	Conservative	Moderately Conservative	Moderate	Moderately Aggressive	Aggressive
<b>Equity</b>	37%	43%	50%	57%	63%
<b>Bonds</b>	58%	47%	35%	23%	12%
<b>PE</b>	5%	10%	15%	20%	25%
<b>Equity</b>	40%	50%	60%	70%	80%
<b>Bonds</b>	60%	50%	40%	30%	20%

## The Potential Risks of Private Market Investments

Before investing, it's always important to understand the risks of any investment decision, and private market investing is no exception. Some of the risks of private market investing to consider include:

### Illiquidity

Unlike securities in the public market that are easily bought and sold on a daily basis, private market funds, usually structured as limited partnerships, lack daily liquidity. These investments should be considered long-term investments, with time horizons of 10 to 15 years. To address this risk, investors can seek to invest through vehicles like internal funds, which typically provide some measure of liquidity on an interval basis, typically quarterly.

### Long-term Commitments

Along with the illiquidity inherent in private investments, investors need to plan for a lack of immediate return of capital and longer timeframes to recoup an initial investment. Small private companies can take years to produce returns, and investors must honor the capital commitment to fund the investment through the terms of the limited partnership agreement.

### Business and Economic Risks

As with public investments, there is no guarantee of success with private market investments. Private market funds may use speculative investment techniques, concentrated portfolios, high amounts of leverage, and illiquid investments.

## Effective Implementation Can Enhance Portfolio Outcomes

Investors and their advisors have become more open to allocations to private investments in recent years as they seek improved risk-adjusted returns and diversification benefits. By thoughtfully constructing a portfolio to include private investments, investors can increase diversification, possibly lower volatility, and potentially tap into the growth potential nonpublic investments offer. Yet private market investments can be complex and include a diverse range of investment structures to consider. Determining how to fund an allocation to private market investments effectively requires a thoughtful and systematic approach. Partnering with an experienced investment firm can help investors navigate the decision process successfully.

## Risks and Disclosures

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Private market investments are complex, speculative investment vehicles and are not suitable for all investors. An investment in a private market investment entails a high degree of risk and no assurance can be given that any private market investment objectives will be achieved or that investors will receive a return of their capital.

Investing involves risk, including loss of principal.

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