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# INVESTORS' APPETITE FOR PRIVATE EQUITY – GOOD OR GREAT?

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***Retail Investors Reap Unintended Consequences as Companies Shift from Public to Private and Private Equity Gains Momentum***

In 2015, I joined Triton Pacific, a Los Angeles based Private Equity firm as a partner, with a singular mission – provide access to private equity to everyone! Over the last five years, we have refined the messaging and feel we have made successful steps in helping democratize private equity to the mass affluent with various offerings in fast food restaurants, health care, specialty finance and consumer goods. Why? Because it should be so, the current market trend is unlike anything we have experienced before.

***Political Spotlight on Private Equity***

While some companies may be choosing a private business model instead of the public alternative, many investors do not have the luxury of options when it comes to where they can invest their money. Until recently, the antiquated and outdated qualification standards only enabled institutions or ultra-high-net-worth individuals to access the most promising private market opportunities. Because of its net worth standards, it limits retail investors to only a few investment products outside of traditional stocks and bonds. This lack of opportunity for investors to diversify one's portfolio has put many at risk of over-allocating into a single asset class.

Regulation of the private equity industry has become a heated political issue over the past few years. The demand for increased regulation of private equity hinges on the idea that the private equity model "feeds" on the economy for the benefit of only a few wealthy individuals.

Our attention should not be on restricting the efficiency of the model, but on granting access to more individual investors in a manner that provides insight and guidance as to the nature of the investment and the private equity sector an investor is contemplating. The ability to brush politics aside and introduce private equity investments to the masses is vital to changing the industry. The time to maximize the opportunities for all individuals, rather than for a select few has come. This access will become increasingly important as the dynamics of the global markets shift from public to private.

***The Corporate Shift from Public to Private Impacts Investors***

In increasing numbers, markets are shifting from public to private, which decreases access to worthwhile investments for retail investors. Over the past twenty years, private equity has significantly outperformed public equity[1].

For example, the average private equity investment made on December 31st, 2001 would have returned 288% by 2018, while a comparable investment in the S&P 500 Index fund would have returned only 155%[2]. This performance is likely one of many reasons why more and more capital is flowing into private equity products as institutions and wealthy individuals search for yield.

This flood of private capital is illustrated by a nearly 50 percent decrease in public companies over the past 20 years, and by the fact that IPOs are less than half of what they were during the 1990s[3]. Uber is an example of this trend, where highly successful companies chose to remain private for a long duration, and when they finally did go public, they posted some of the highest valued IPOs in history.
Uber grew rapidly for ten years prior to going public and was valued at $82 billion at the time of its IPO. However, like other post-IPO stocks, Uber has not been able to garnish the same returns as it did pre-IPO.

Private equity is also transforming the restaurant industry as it enters new market segments that have traditionally been owned by smaller owners/operators. The quick serve restaurant ("QSR") industry is one example, that represents a $500 billion industry and accounts for over 50% of restaurant sales nation-wide[4].

QSR restaurants with nationally recognized brands have traditionally been owned and operated as a single entity via a franchise agreement. As these individual locations are sold to private equity firms, the locations are consolidated into a large operating platform, creating economies of scale across the portfolio of QSR locations. The capital and operating efficiencies that are created often lead to increased profitability across the portfolio.

The Uber and QSR examples demonstrate how retail investors have been excluded from some of the most profitable investment opportunities. Today, retail investors only have the option to earn approximately half of what those with access to private equity do[5]. Because of this, we are further expanding the great wealth divide in this nation. It's time that we modernize our investment regulations so we can begin to close the gap between the ultra-wealthy and retail investors.

As a result of the recent public market trends, retirement accounts may be insufficient when investors need them the most. Private markets are expected to continue outperforming public markets for the foreseeable future[6].

Is it that inconceivable that investors saving for retirement can no longer rely on stock market investments to generate the sufficient returns needed for retirement? Not really.

In a modern digital era, the research opportunities are boundless. It's time that we work together to determine how we can give retail investors the opportunities and the tools needed to make informed investment decisions. And given that the latest financial trends leaning more favorably towards private equity, investment reform needs to start here.

It is now time to grant the public access to private equity markets. The net worth requirement should be reduced or eliminated to enable retail investors access to this historically well-performing investment segment and our technology today can help mitigate many of the historical concerns that contributed to the stricter suitability requirements for private equity. However, past performance is not indicative of future results.

### *Moving Beyond the Illiquidity Concern*

One of the main concerns with the introduction of illiquid credit and real estate products was whether retail investors would understand the complex investment structures involved. The idea that retail investors may not have the resources or savings in place to weather a financial burden is concerning to regulators. In addition, the concern that investors may not understand that investments in illiquid investments are in fact that—illiquid.

According to the 2019 Global Alternative Fund Survey conducted by Ernst & Young, 91% of current private equity investors are planning to maintain or increase their allocation to the asset class. This study indicates a growing demand for these types of alternative investments in the retail markets, despite their illiquidity.

Investment professionals can and will most likely play a crucial role here, as they can help to explain the trade-offs of alternative investment products and help to get clients comfortable with illiquidity in a private equity investment.

Sources


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