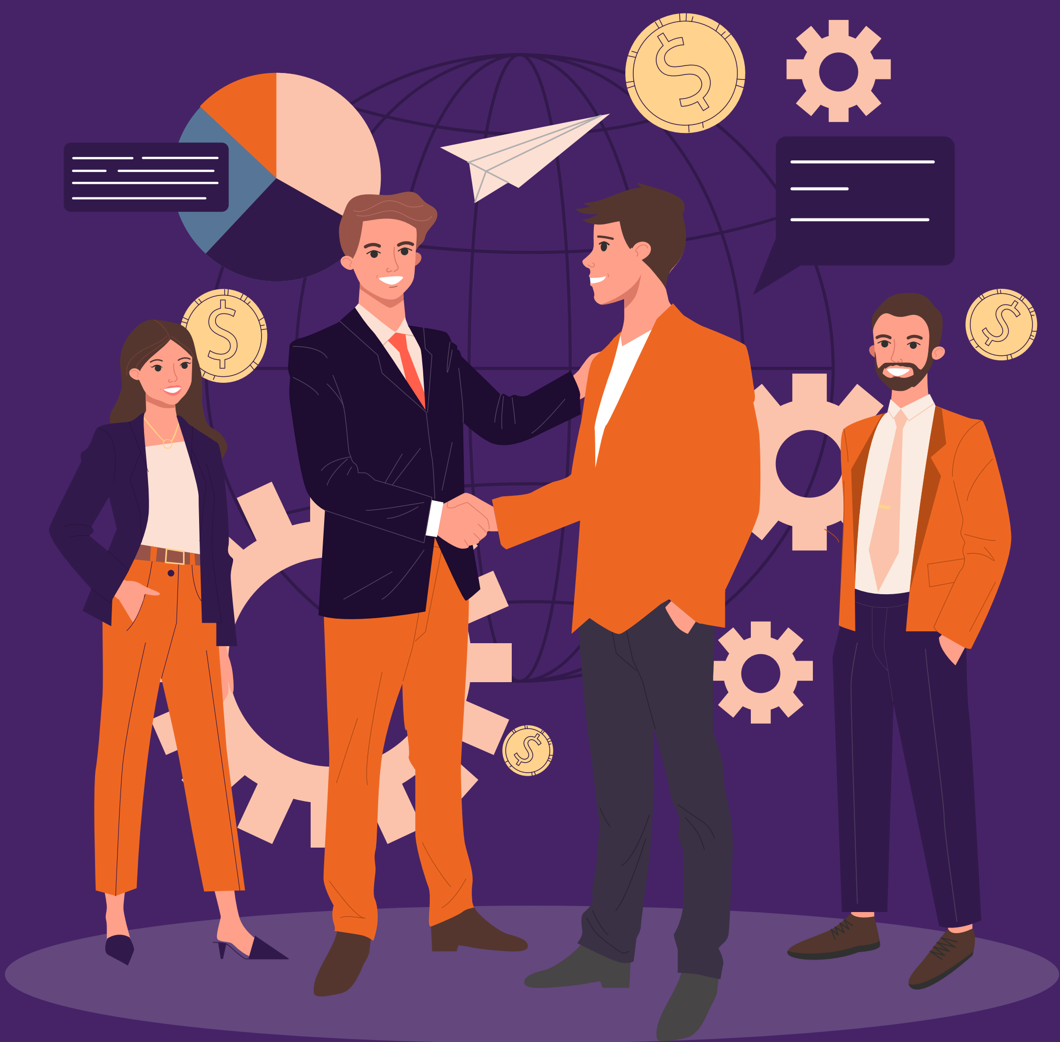
WHAT IS PRIVATE EQUITY?

White paper



There are lots of people who are interested in pursuing private equity, and some people are wondering what this actually means. Many of the goods and services that people use are from companies that are backed by a private equity firm or organization. For example, whether someone is purchasing food from a local restaurant or visiting the veterinarian for their pet's health needs, there is a chance that this could be back by a private equity firm.

So, what does private equity entail? How is this different from other companies? There are a few important points that everyone should keep in mind.

An Overview of **Private Equity**

Private equity is usually shortened to PE. This is a specific type of financing. These organizations are responsible for investing capital, in the form of money, into a company. Usually, people who work for these firms target mature, traditional industries, providing money that can be used for inventory management, research and development, or to hire new employees. Then, in exchange for this funding, the private equity firm takes a stake in the company. The size of the stake is usually negotiated when the money is given.

Importantly, PE is very different from investing in traditional stocks and bonds, which are traded publicly. Private equity is similar to real estate investing and venture capital investments. These are less traditional equity Investments, meaning that it is not as liquid as some stocks, bonds, and mutual funds.

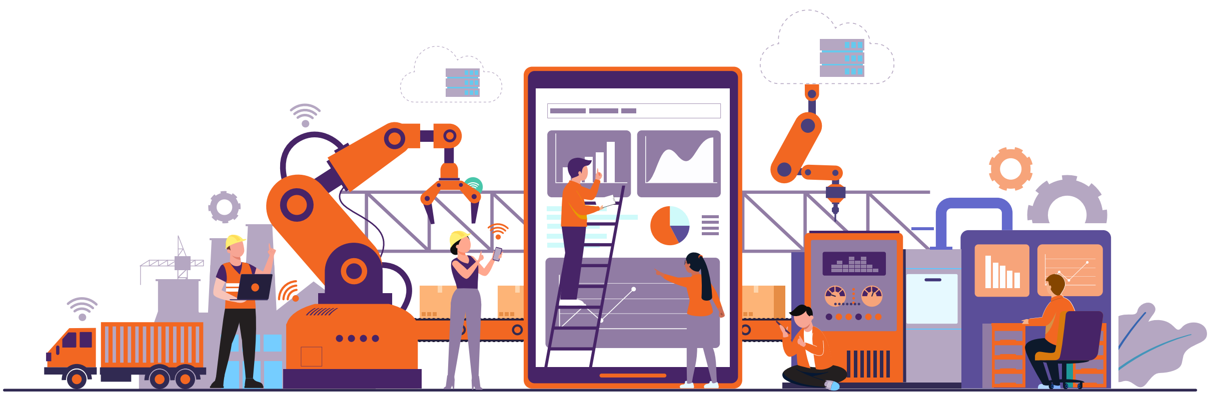
What Does a Private **Equity Firm Do?**

Individuals who work at a private equity firm are usually professional investors. They have a strong background in the business world. The goal of people who work for a PE firm is to invest their money in businesses that are going to grow significantly in the future. A lot of these investments have horizons that are several years or more.

Typically, private equity firms raise the capital to use to invest in companies from limited partners. Then, they promised these partners a significant return on their investment by choosing companies wisely.

When a PE firm invests in private companies, they usually try to take a controlling stake. This means they try to purchase 50 percent are more at the business when they hand over their capital.
A lot of private equity firms have dozens of companies in their portfolios. Even though some private equity firms specialize in a specific industry, many private equity firms target multiple industries as a way to diversify their investments.

Even though they may still allow the original members of the company to make decisions, private equity firms purchase a controlling stake to direct the company's future and maximize the return on their investments.



How Do People Who Work in PE Make Money?

In general, there are three ways that a private equity firm might make money. These include management fees, performance fees and the profit from the sale of companies or assets acquired through acquisition and sold for a profit. The vast majority of private equity funds follow something called the two and 20 rule.

What this means is that private equity firms charge management fees as a percentage of total assets, which is usually two percent. These are used to cover daily expenses and overhead costs that arise regularly.

Then, private equity firms usually charge a performance fee. In this case, private equity firms take 20 percent of the profits they make from investing. This is usually done to incentivize the people who work for the private equity firm to maximize their returns. Then, bonuses are paid out to employees in order to reward their success.

Finally, if one of the companies is sold for a profit, the private equity firm will earn a share of the profit from the sale of the company, or the assets acquired through acquisition and sold for a profit.

Is a PE Firm the **Same as a Hedge Fund?**

These investment models are similar; however, there are some differences. The biggest difference is that a hedge fund usually operates in the public market. This means that they are trading companies that are publicly available on the stock exchange.

In contrast, a private equity firm usually targets companies that are still private. This means that the average investor cannot buy shares in that company. As a result, hedge funds and private equity firms have different areas of expertise in the finance world. Both private equity firms and hedge funds seek to invest money in strong companies as a way to maximize the return on their investments.