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Private Equity for Retail Investors

How to efficiently involve Finnish retail investors in private equity

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Private equity has been the best performing asset class for institutional investors. Meanwhile, retail investors have been left out from the asset class for several reasons, such as legislation and wealth profiling. This study aims at assessing the types of private equity vehicles that could be the most appropriate for Finnish retail investors. The study solely focuses on the investment opportunities, hence it does not cover investment behaviour.

Private equity should not be a primary asset in an investor's portfolio, however private equity offers different risk and return profile than the public equities. Therefore, private equity could be a good addition for many types of investors.

Fin-tech innovations such as equity crowdfunding have enabled private equity investing for all investors. However, active management, strict selection criteria and a well allocated portfolio are things that equity crowdfunding does not offer. Therefore, crowdfunding investors are not getting the same product as private equity investors. Hence, will probably not generate the same returns on their investment.

Several interim vehicles have been created to enable private equity investing for retail investors, however most of the vehicles offer only partial exposure to private equity. Vehicles such as Listed private equity funds and feeder funds are one of the most effective vehicles for retail investors wishing to have private equity in their investment portfolio.

Keywords	Private Equity, Crowdfunding, Alternative Finance, Retail Investors

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1 Introduction

The funding of small and medium sized enterprises (SMEs) is becoming more important all the time for the European economies. The European Union describes SMEs as the backbone of the economy, is therefore trying to enhance SME growth. One important factor of the growth is access to funding for these companies (European Commission 2017). Though many of these companies are not traded publicly they do have various funding sources, and access to equity investors alike (Horton 2015).

Private equity is an asset class that has gained popularity among investors in the recent years (Leleux et.al 2015: 2). One of the reasons why private equity has attracted many investors is the higher returns that it has been able to provide over many traditional asset classes (Barber & Gold 2007). Currently, an estimated $2,7 trillion has been invested into private equity (McKinsey 2017: 8). This asset class is dominated by institutional investors. Retail investors have been left out of from this asset class (Butt 2016). One of the reasons is that there are very few options for retail investors to invest into private equity. The typical private equity funds have such large minimum investment requirements that very few retail investors can match these requirements (Greenberg 2015). In addition, the legislation plays a role in explaining why retail investors are not involved in more frequently.

The Internet is creating new, innovative opportunities all the time. This has created new innovations in SME financing too, one of these Fin-tech innovations is crowdfunding (Heitzman 2015). Crowdfunding has gained in popularity as a financing tool. Crowdfunding gives opportunity for everyone to access private company funding. Equity crowdfunding is a form of private equity investment that is accessible to the retail investors, too (Madden 2016). However, equity crowdfunding differs in many ways from traditional private equity funds. This study will explain the main differences between these two.

This thesis aims at assessing the types of private equity investment vehicles that could be appropriate for retail investors and by which such investors could be mobilised to a greater extend in Finland. Hence, we will examine why retail investors are not investing into private equity as actively as their European peers.

In addition, the thesis aim is to analyse the existing retail investor offering of private equity investment vehicles and understand how these differ from those offered to institutional investors. Finally, how these vehicles differentiate from the options that are offered for institutional investors.

Chapter 2 will go through the form of private equity. It is important to understand the world of private equity first before thinking about the Investment opportunities to the asset class. Therefore, Chapter 2 will explain how private equity is typically practiced, what is the risk and return profile of the asset class, what is the typical incentive structure of private equity, the exit process and private equity in Finland. Chapter 3 will be looking at the current investment possibilities of retail investors into private securities. It is important to look at the current options that the retail investors have, as the goal is to offer a better solution for retail investors. Chapter 3 discusses both direct and indirect access to private equity. Chapter 3 looks at global opportunities, as well as Finnish to understand the core differences between private equity and crowdfunding, Chapter 4 will discuss these from the investor’s aspect. Chapter 4 includes views of Finnish professionals of the current market trends. This provides an overall view of the market and how it works. Chapter 5 will try to provide a solution regarding how retail investors could be offered private securities in a more transparent and efficient way. Chapter 5 includes a comparative overview on existing private equity vehicles that can be used by retail investors. As well as an assessment on alternative approaches for Finnish private equity retail investors. Chapter 6 will summarise all findings.

1.1 Study Objectives

The main objective of this thesis is to answer how Finnish retail investors could be efficiently involved into private equity. Finnish legislation is considered to understand the restrictions of the legislation, which may affect retail investors’ possibilities to invest in private securities. Beyond the legislation, the thesis will study differences between investment vehicles that are offered for retail investors and institutional investors. This study will solely focus on the types of private equity vehicles that are or could be offered to retail investors. Hence this study does not cover investor behaviour which is considered *“Ceteris paribus”.*

1.2 Research Methods and Scope

The main research methods rely on secondary research in the form of core books about the topics of private equity and crowdfunding. The main book that is used to examine private equity is “Private Equity for the investor - value creation, operational improvements” by Leleux, Van Swaay and Megally. The book is used because of its both optimistic and critical view at the same time of private equity (2015: Foreword). The book covers the post-financial crises market conditions and how the industry has changed. For equity crowdfunding the book from Freedman and Nutting, “Equity Crowdfunding for Investors” is used. This book is essentially helpful as it covers crowdfunding from the investors point of view. Additionally, as the text covers equity funding possibilities for retail investors, the book offers great views as it focuses on equity crowdfunding.

The thesis is supported by the latest opinions and views of the private markets with articles and market studies relating to private equity and crowdfunding. As the text mainly focuses on the current situation in the Finnish market, The Finnish Venture Capital Association (FVCA) serves as an important source of reference as they provide studies from the Finnish private equity industry. Their main objective is to promote the Finnish private equity market and its importance. FVCA has published a recent study about the relevance of Finnish private equity market, therefore this book is used as reference. Global data is also used to provide a larger view of the overall market conditions and the current market trends. Research studies serve as great source of reference to complement the market data. Market data is useful to look at the industry size and trends. Preqin is the global leader of alternative asset studies (Preqin.com). The 2015 Preqin alternative asset performance monitor edition is used for reference in this text.

Primary research is additionally employed as qualitative research method. Finnish industry experts are interviewed to find out valuable opinions on the Finnish market conditions and to seek solution for efficient market. In total 5 different experts are interviewed. covered representatives are a business angel, two equity crowdfunding providers, the head of the Private Equity association and a relevant industry lawyer. Hence this study covers a wide range of views on the topic. The interviews were conducted in Finnish, therefore the questions, that are provided in the Appendix 1, as well as the answers that have been used in the thesis have been translated by the author.

Additionally, the Finnish Financial Supervisory Authorities (FIVA) have been interviewed. The interview is also conducted in Finnish, therefore translated by the author (see appendix 2).

2 Private Equity

Private equity is an investment that is made in companies that are privately held i.e. not publicly traded on the stock market (Collins, 2015). Private equity can be considered a relatively new asset class, as it has really boomed during just the past 2 to 3 decades (Leleux et.al 2015:2). Private equity is usually practiced through close-ended funds. These funds are mainly for institutional investors and for the high net worth individuals as the minimum investments tends to be from $1 million and upwards (Foley, 2016). The global average fund size in 2015 was $578 million, according to research house Preqin (2016). As the funds are so large it would require a lot of effort to collect small amounts from retail investors.

The legislation has a role in why private equity companies do not collect capitals from individuals. In many countries, the legislation basically does not allow retail investors to be included. In the European Union, for instance the alternative investments are mainly meant for professional investor. However, every member state can choose their policy whether these funds will be offered for retail investors (2011/61/EU: Article 43). Chapter 3 will explain different ways how retail investors can have access to private equity.

2.1 Private Equity Funds

Private equity funds have normally been divided in many separate ways. For instance, the former European Venture Capital Association (EVCA) has two main categories; venture capital and private equity. The Difference between these funds are the stage of investment. Venture capitalists typically play a role in the early years of companies, whereas private equity funds typically invest in more mature businesses. Both of these groups can be divided into many sup groups (Invest Europe: 3). However, as Leleux et.al (2015:30) explain, in the US the term private equity is typically used for the whole industry. Therefore, their book uses the term private equity for the whole industry, venture capital for the earlier stage investments and buyout for the later stage. Additionally, Pajarinen, Rouvinen and Ylhäinen (2016:5) use this categorisation, therefore the same categorisation is used in this text. Both strategies have several sub-categories as venture capitalist have normally been categorized as following; seed, start-up and venture growth. Buyouts have different strategies such as leverage buyout (LBO) and Management Buyout (MBO) (Leleux et.al 2015: 30-35). Figure 1 shows the different strategies of private equity funds.

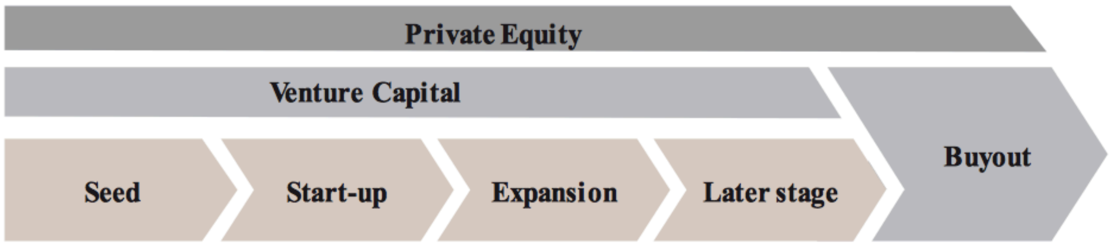

Figure 1: Private Equity Phases (Sommer 2013: 13)

2.1.1 Private Equity Structure

Private equity is typically practiced by a close-ended fund, which means that the investor's investments are locked until the closing of the fund (Sommer 2013: 14). Typical target period for a private equity fund is ten years, however the average lifetime of the funds has expanded to 13 years in 2015 (Bollen 2015). Therefore, private equity a long-term investment.

The typical fund is a limited partnership where the General Partners (GP) are the fund managers and the Limited Partners (LP) are the investors. The GPs are normally finance professionals. It is a market standard that the GPs also invest in the fund typically, 1-5% of the total fund to show commitment to the LPs (Leleux et.al 2015: 38). Typical LPs are institutional investors such as pension funds, endowments and insurance companies. The reason for this is that the typical minimum capital requirement to enter a private equity fund can be anything between one to several hundreds of million depending on the fund size (Leleux et.al 2015: 38).

The fund managers make revenues through management fees and carried interest. The funds typically charge a management fee of 2%. There are some exceptions to the market standard as the management fee might be anywhere between 1,5% and 3%. Larger funds tend to have smaller management fees, as this fee was originally intended to cover the operating expenses of the fund. The real returns for the GPs is achieved through performance and this is called carried interest. The typical carried interest is 20%, this is calculated after the LPs have been returned their original investment plus a preferred interest. The preferred interest or hurdle rate is sort of a “minimum return” to the LPs. The hurdle rate is typically 8%, meaning that the investors have a preferred return of 8% before the GP gets any success fees. After the LPs have been provided with their original investment, the external returns will be distributed in a 20/80 waterfall structure, where GPs will have 20% and LPs will have 80% of the returns (Leleux et.al 2015: 43-48).

2.2 Private Equity as an Asset Class

Private equity is considered to be an alternative asset. Alternative asset is a common name for all the other asset class beyond the traditional asset classes. Stocks, Bonds and Cash, that are considered as the traditional asset classes or so called mainstream assets. Other alternative assets are things such as real estate and hedge funds (Leleux et.al 2015: 3). Private Equity is an illiquid asset that makes it less attractive compared to the traditional ones. Although, the secondary market has started to grow for private equity, it is still relatively small. The secondary market is typically traded on heavy discounts; therefore, it is an asset that should be held for the entire period i.e. fund lifetime. This might mean holding for a long period like 10 years for instance (Leleux et.al:58-60).

2.3 Risk & Return

Private equity has several risk factors one of them being illiquidity of the asset class, as it is relatively hard to have access to the investments before exiting the investments. The secondary market of private equity is not yet fully existing, however the secondary market has evolved in the recent years (Leleux et.al 2015: 28-29). Unfavourable factor in the secondary market is that the funds are sold at significant discount before maturity (Diller & Jäckel 2015: 7-9). The asset class itself has more risk than the traditional assets as private securities tend to be more sensitive to changes in the company than the public counterparty. The investments are typically made in earlier stages companies, which include more risk than the later stage investments (Freedman & Nutting 2015:136-137). There is always the risk that the business will not take off and will be sold with a loss or even worse will go into bankruptcy.

Figure 2 demonstrates that this has been true in private equity as venture funds have been far riskier than the buyouts. What is interesting to realise is that the average return in the venture funds has been lower than in the Buyout funds, which does not seem to apply the risk/return theory. However, it is important to notice that both risk and return are measured from the average IRRs between selected vintage years. What the figure might imply is that Buyout funds tend to have less volatile performance than the venture counter parties, which makes sense as these investments are made to later stage. The theory is supported while looking at the best performing funds, that are mainly venture capital funds (Preqin 2015: 22-23). The vintage year also affects the performance differences (Preqin 2015:12-13).

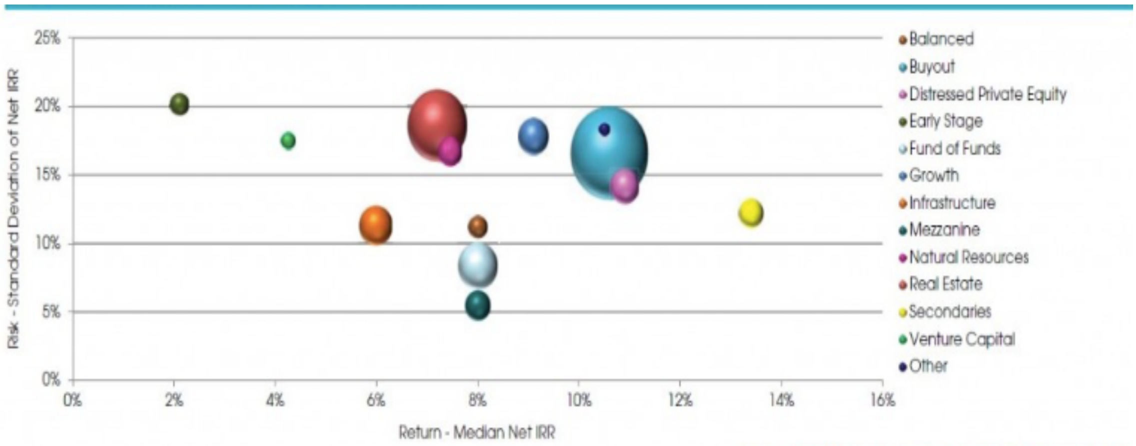

Figure 2: Private Equity Risk Return by Strategy (Preqin 2015: 11)

The superior returns that private equity has been able to provide over any other traditional asset class makes it very attractive (Greenberg, G 2016). This is, of course, logical result as riskier investments should have better returns (Foley 2016). However, it has been argued that the average private equity funds do not over or underperform the market. As some studies have showed that the average returns of the average funds are very average indeed and only the top quarter of the managers performs extremely well (Leleux et.al 2015:104-105). Appelbaum & Batt (2016:13-16) had similar findings in recent studies. They pointed out that private equity returns have been declining since 2006, as the returns over performed the market before 2006.

Figure 3 indicates that private equity has been the best performing asset class for the median public pension fund especially in the long-term (Preqin 2015: 10). Only in the 3-year period offended in December 2014 the listed equity has outperformed private equity. The average private equity annual return tends to be relatively steady at around 12%, whereas listed equities have had significant turbulence that vary a lot depending on the time frame. This might indicate that private equities are actually less volatile than listed equities.

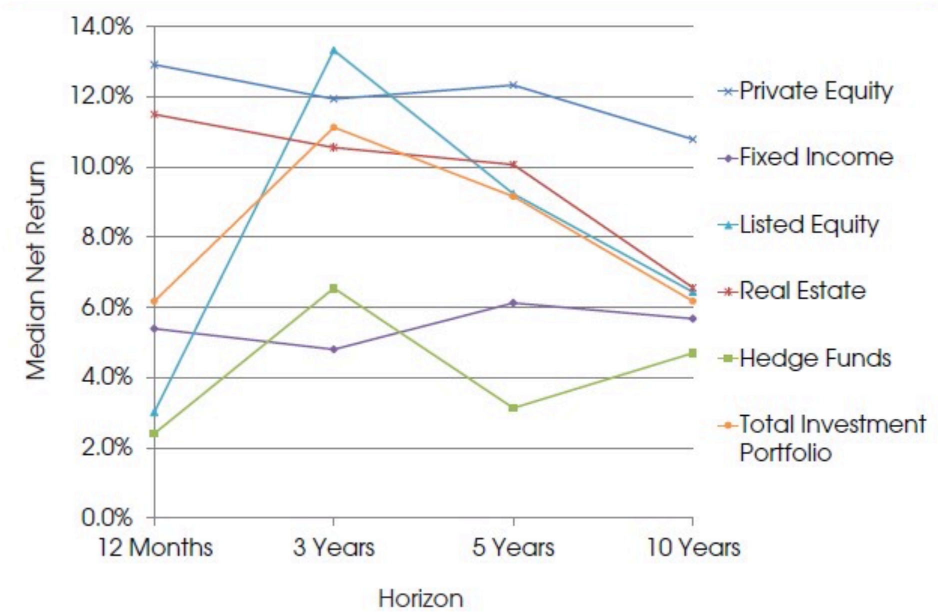

Figure 3: Median Public Pension Fund Net Returns by Asset Class (As of December 2014) (Preqin 2015:10)

Private equity returns are normally measured by Internal Rate of Return (IRR) and total value paid in capital (TVPI), where the former considers the time value of money. These models are used together as both have restrictions of their own, but together have relatively good view of the overall returns of the investment (Leleux et al. 2015: 106-107). Valuing sold investments is a straightforward process, however the unrealised investments are harder to value as the investment do not have daily-quoted value. The real returns are generated as the investment are sold (Leleux et al. 2015: 108). The selling process it is not an easy one as the investment cannot be sold in a public market, so the fund managers must look for opportunities that are in the best interest of all parties.

Private Equity funds make profits upon exiting their investments (Invest Europe: 5). The exit process is the ultimate measurement of performance. Both realised assets and unrealised are given value, however the unrealised valuations are subjective, therefore only the sold investments value can be reliably valued (Leleux et al. 2015: 108). The private equity managers receive the carried interest as the investment is sold. There are several options for exiting the investments. The most common exits for private equity buyout funds globally has been trade sale followed by sale to another private equity fund and only thirdly Initial public offering (IPO), which has been widely considered as measure of success (Leleux et al. 2015: 95-96). While looking at all private equity in Finland the most common way for exit has been capital loan re-payment followed by trade sale, sale to the management and write offs. In Europe trade sale has been the most common way of exit. The higher level off write offs in Finland might be explained by a higher level of venture capital funds, where the write offs are more typical than in Buyout Funds (Pajarinen et.al 2016: 20-22).

2.4 Private Equity in Finland

Private equity has grown extremely quickly in Finland as 2015 was a record year in terms of assets under management (AUM) for the Finnish private equity companies. The total AUM reached 6 billion euros, and private equity is now ten times larger in Finland than 10 years ago (FVCA 2016). Figure 4 shows the growth of the Finnish private equity firms in terms of assets under management. The green column represents the total AUM in millions of euros by year. It can be seen from the Figure 4 that the previous peak year was 2010 as the AUM decreased slightly after 2010. The total amount of investments to Finnish growth companies in 2015 was 1 billion euros (FVCA 2016).

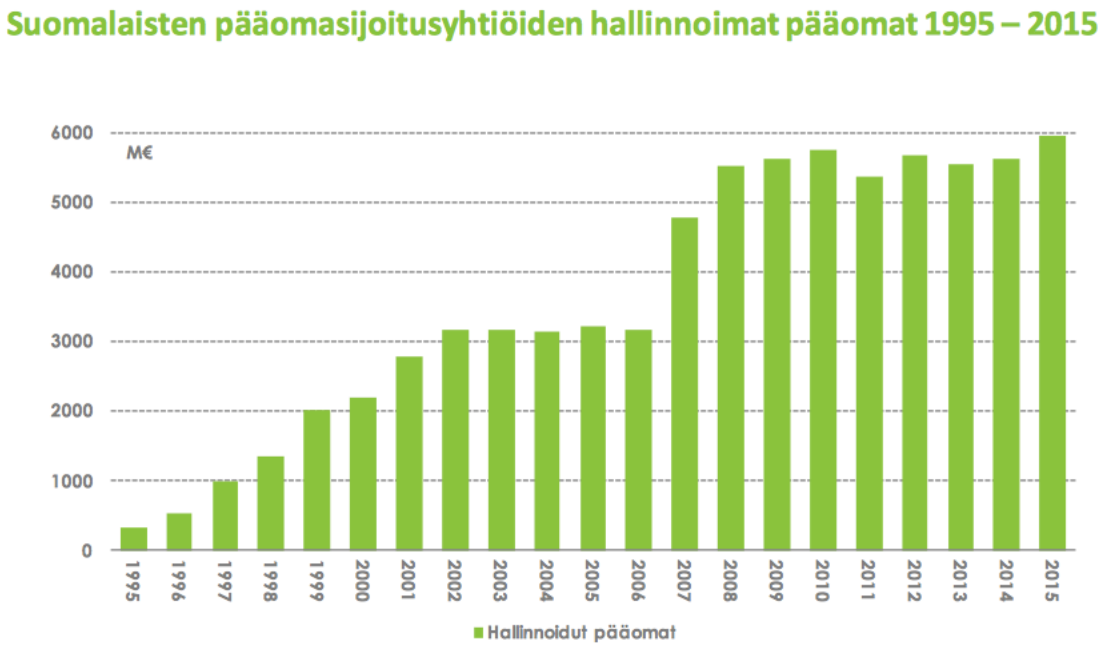

Figure 4: Finnish Private Equity companies' asset under management between 1995-2015 (FVCA 2016)

Finnish start-ups received funding of 383 Million Euros in total from different Investors in 2016 which was a record (FVCA 2017). Figure 5 demonstrates the amounts invested per investor group. Growing trend can be seen in the total amounts invested. The majority of the investments came from foreign investors that almost doubled its share from the previous year, whereas venture capital firms were the only party to invest less in Finnish companies than in the previous year. However, even though Finnish venture capital Investments in Finland decreased, the total amount of investment by the Finnish venture capital firms grew slightly, as 40 million was invested to foreign companies (FVCA 2017).

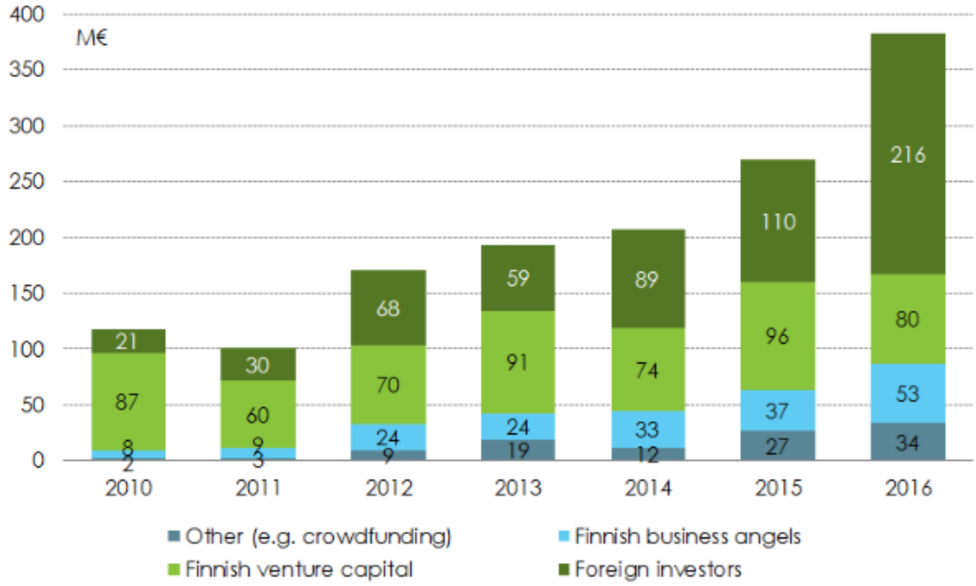

Figure 5: Investments to Finnish Start-ups by source (FVCA 2017)

Figure 6 demonstrates that only 2% of the Finnish private equity fund investors are individual investor, while the European average is 5%. This means that Finnish individual investors are less involved with private equity funds than the European peer group. Therefore, alternative models could serve these investors to have allocation in private equity. The Categories in the figure from top to bottom are; Not disclosed, others, private investors, banks, insurance companies, family offices, fund of funds, government and pension funds. The left column represents Finland and the right one represents Europe.

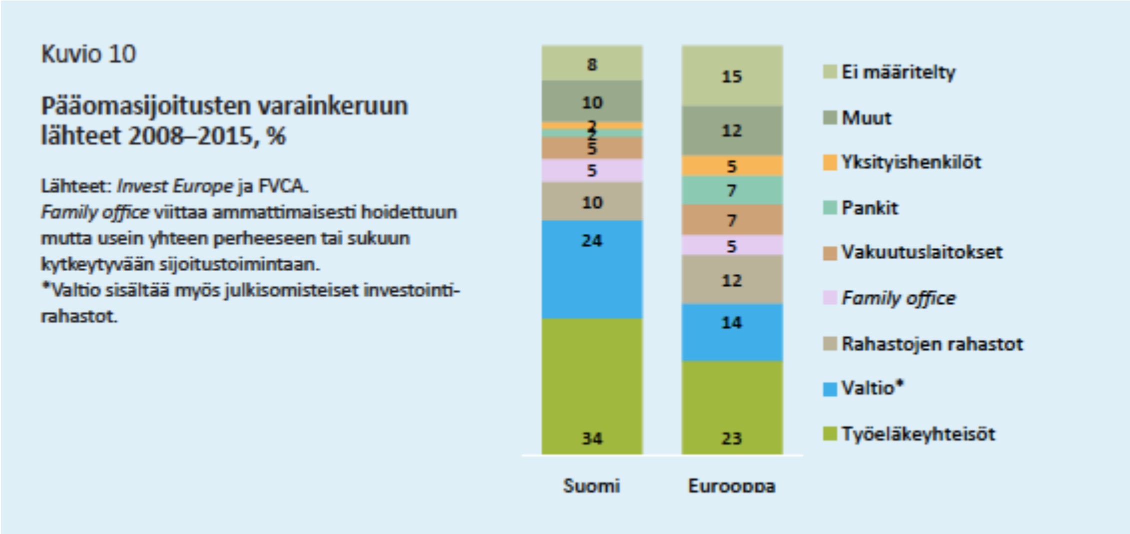

Figure 6: Private Equity Fund raising sources 2008-2015 (Pajarinen et al: 21)

Between 2012 and 2015 3 billion euros were invested to Finnish private companies. In absolute terms this is not much in the European contexts, while in proportion of the GDP it was clearly above the European average (Pajarinen et.al 2016: 16).

3 Investment Vehicles for Retail Investors

The existing possibilities for retail investors to invest in private equity should be looked at in order to provide a better solution. Investors are normally categorised as either institutional investors or retail investors. A retail investor is a person who buys shares for their own use, whereas institutional investors, such as pension funds and life insurance companies, buy these for firms or organisations (Investopedia, 2003). Retail investors are often referred to as small investors or individual investors, their individual wealth tends to be much less than institutional investors for obvious reasons. In the U.S., the Securities and Exchange Commission (SEC) has a categorisation that divides accredited investors and non-accredited investors (Freedman & Nutting 2015: 26). These are separated by their individual wealth, which means that an accredited investor might be a retail investor. These are the wealthy individuals, whom are both retail and accredited investors. In the U.S., the wealthy retail investors with accredited investor status have had better opportunities to invest in private securities than the non-accredited investors. In the U.S., the private equity managers have been starting to provide funds for accredited investors. One example of this is the AMG Pantheon Fund, which has a minimum investment of $25 000, which can be considered relatively small when compared to the typical private equity investments. This is believed to lead into a situation where the private equity market will be one day open for all retail investors. Currently the legislation denies this possibility, but it is expected to change, with these vehicles being the first step (Butt 2016).

The Finnish professionals are interviewed to seek views on the current market conditions, the legal limitations dealing with investment to retail investors, the views on how the market could be shaped to a more efficient model, what the professionals believe will happen in the future, why these models exist, what value each model bring to the economy, what are the risks in the asset class, how a retail investors should build their investment portfolio, and their thoughts on Crowdfunding.

3.1 Legislation

The legislation restrictions are one of the main reasons why private equity funds are not offered to everyone. As legislation is different in every country, it is almost impossible to offer the same solution to all investors. The main point of the legislation like The Alternative Investment Fund Managers Directive (AIFMD) of the European Union is said to be to protect the investors (Blackrock.com 2011). This might be common benefit at some level as private equity is a difficult asset class from its nature, however everyone should have the possibility to invest to the asset class. This thesis will focus on Europe and mainly in Finland for the things that are possible to do and what might be in the future legislation wise.

3.1.1 U.S.

The modern day private equity started in the United States after the World War 2 (Leleux et.al 2015: 6). Therefore, the U.S., legislation plays an important role in how private equity has been shaped. In the U.S., the SEC has the Regulation D. This regulation has a restriction on deals made to private securities. Every deal is limited to have maximum of 35 non-accredited investors, whereas there is no limitation on the number of accredited investors and no capital limitations either. Accredited investors are categorized as an individual that has net worth over 1 million dollars (excluding the residence where one lives) or has a yearly income of $200 000 (or $300 000 for married couple together) (Freedman & Nutting 2015: 26). These investors are wealthy enough to invest in crowdfunding platforms that operate under the regulation D, but still most may not have the minimum capital that private equity funds require. The first online equity crowdfunding platforms in the U.S started to arise after 2011. These platforms operated under the Regulation D of the Securities Act of 1933, however these platforms opened the gate only to the wealthiest investors. The real change happened in 2012 when the Jumpstart Our Business Startups (JOBS) act was passed as the Tittle III of this act allows all investors to invest in private equities. The Act limits investors yearly investments by their wealth, the investors cannot invest more than $2 000 or 5% of their annual income into private securities (Freedman & Nutting 2015: 29).

3.1.2 Europe

In the European Union, all the Alternative investment fund managers are regulated by the Alternative Investment Fund Managers Directive (2011/61/EU). Private equity is categorised as an alternative investment, therefore the directive applies to it. According to Article 31 of the directive, fund managers should mainly market to professional investors. However, Article 43 (1) of the act is an exemption clause as the member state may allow marketing to the retail investors (Directive 2011/61/EU). Therefore, the directive does not fully restrict the possibility to market the funds to retail investors, and the decision power has been left to the member states.

3.1.3 Finland

As Finland is the case study area of this thesis, the legislation in Finland has to be studied. Finland being an EU member country, the AIFMD applies to Finland. As explained in the previous section, each member state may decide to allow marketing to the retail investors. The main legislation considering the alternative management in Finland is the act 162/2014 *“Laki vaihtoehtorahastojen hoitajista”.* For crowdfunding the main legislation is the act of 734/2016 *“joukkorahoituslaki”.* FIVA is the party that gives the licences and supervises the financial sector in Finland. Two employees from FIVA have been interviewed for this thesis. The questions for which answers were sought were; what information should be disclosed to the investors, how much capital can be collected from the unprofessional investors if any and what other requirements exists, if unprofessional investors are involved (see appendix 2)? The legislation considering alternative management in Finland states that these funds are mainly for professional investors (162/2014). Professional investors have been categorised in the Investment Services act 747/2012 *“sijoittuspalvelulaki”.* The Act categorises professional investors in a similar way as the Institutional investors are categorised. Chapter 13 of act 162/2014 applies rules for marketing alternative funds to the non-professional investors.

Finland has two different kinds of processes that an alternative asset manager may follow. An alternative asset manager is either required to have a licence or registration, the former being stricter (FIVA 2017). The act of 162/2014 on alternative asset manager states that managers that are licenced are allowed to market the fund for retail investors. The asset managers that are registered can only do so with a special acceptance from FIVA (162/2014). The majority of the Finnish alternative asset managers are registered and do not have a licence (FIVA 2017). In Finland, the requirements for alternative asset management licences tend to require lot of resources, which might be the reason why the majority of fund managers are registered instead of licenced (Santavirta 2017). The requirements for the special permissions are set in the directive of Minister of Finance 226/2014 “Valtionvarainministeriön asetus”. The act states that a fund manager can only market the fund to unprofessional investors who have 1) net worth of at least $500 000 and 2) invest at least $50 000 to the fund. These are clear reasons why the small investors cannot be offered a private equity fund if the asset manager does not have a licence.

3.2 Crowdfunding

Crowdfunding is an innovative Fin-tech solution that enables retail investors to fund unlisted companies (Airaksinen 2013). The success of crowdfunding platforms such as Kickstarter has drawn attention to crowdfunding (Freedman & Nutting 2015: 19). Crowdfunding is normally done through an online platform. Crowdfunding is not a new phenomenon, even though people may think so. There are many different types of crowdfunding platforms, such as reward based crowdfunding, loan based crowdfunding, and equity based crowdfunding (Freedman & Nutting 2015: 1). The thesis will solely focus on the equity crowdfunding process as the purpose of this study is to offer a way for retail investors to be involved efficiently in private equity. It is important to separate the reasons why people invest in crowdfunding platforms as people invest to companies via crowdfunding for other reasons than economical (Williams 2016). Therefore, it is important to notice that this study is looking at equity crowdfunding solely as an investment opportunity, and thus looking for the profits that crowdfunding can provide for the investors.

3.2.1 Equity Crowdfunding

Equity crowdfunding is a model for small investors to have ownership in a privately held company. Otherwise, the access is very limited for small investors to invest in private equity. The first equity crowdfunding platforms that emerged in the U.S., were only available to the wealthiest 7% of the population for legislative reasons. The real change in the U.S., happened in 2012 when congress passed the JOBS act which meant that companies can seek money from all investors via online based crowdfunding platforms. This has helped the growth of equity crowdfunding (Freedman & Nutting 2015: 29).

3.2.2 Reward Model for Crowdfunding Platforms Example Case MicroVenture

MicroVenture is one of the first equity based crowdfunding platforms in the U.S. MicroVenture offers their service mostly to accredited investors only, as it operates under the regulation D. Microventures have a $5 000 minimum investment, which can be considered relatively low. MicroVentrues take 10% of all successful deals, half is taken from the investors and other half from the target company. MicroVentures has a carried interest of 10% in case of a sale or IPO (Freedman & Nutting 2015: 33). This model is very close to a private equity model, however the initial 10% “broker fee” is relatively large. MicroVenture’s CEO has made a statement that in the long rung the goal is to eliminate the carried interest which means that incentive will not be aligned at any level with the investor (Freedman & Nutting 2015: 33- 34).

3.3 Interval Funds

The traditional way for retail investors to invest in private equity in the U.S., has been through a fund of funds. The investment requirements tend to be fractions, if compared to the direct funds. These funds divide the investments between dozens of private equity funds. These funds might offer also a larger allocation to private equity even global, however there are two layers of fees. These funds are typically offered by wealth managers (Foley 2015). In 2012 CPG Carlyle Private Equity Fund LLC was founded, which is an Interval Fund. The fund’s purpose is to invest its assets in other private equity funds. Additionally, the fund can invest directly in private equities between 0-20% of the total assets. The interval fund is distinct from the traditional private equity funds in that it offers redemption possibilities. The fund managers predict to offer a 5% liquidity on a quarterly basis. In other terms the fund gives the investors the possibility to withdraw 5% of the total assets (Papagiannis 2013). Other large private equity houses like KKR aim to offer similar interval funds. They are offering direct access in private equity with a small minimum investment like $10 000 (Foley 2015). These funds invest around 70% in private equity as well as offering periodic liquidity (Weiss 2014; Benjamin 2016).

3.4 Listed Private Equity options

Few listed options exist through which retail investors may have access to private equity through stock market. For instance, an investor may invest in a company such as KKR, Apollo or Blackstone. These are publicly held private equity firms (Leleux et al. 2015: 60-61). This gives the investors some sort of exposure to private equity returns. However, it has been argued that it is not the same thing as investing into a private equity fund. By investing to the managing company the investors have only access to the returns that the managing company makes. By buying listed private equity companies the investor do not get access to the deals, but rather to the earnings streams of the managers (Greenberg, G 2015; Seekingalpha.com 2016). Additionally several private equity Exchange Traded Funds (ETF) exist. These ETFs tend to invest in listed private equity firms, therefore by investing in these ETFs, investors have a wider network of listed private equity companies (Seekingalpha.com 2016). The problem with these ETFs are the same as the problem with the listed firms. The returns that these ETFs generated compared to the returns of the private equity indices have not been appealing. This is because the private equity companies tend to have intense incentive programs for the managers. Part of the profits will be paid to the management team as a reward (Seekingalpha.com 2016). Therefore, investing into the listed management company is a different thing than investing directly to a fund, where the returns can be accessed directly.

The alternative more direct way to access private equity through the stock market is to invest in a listed private equity fund (Leleux et al. 2015: 60-61). These funds offer the most direct access to private equity. These funds invest directly in private companies, therefore the owner of the stock has direct access to the private equity companies in a similar way to the LPs do (Lpeq.com). The Problem with listed funds is that after 2008 the funds tend to trade on significant discounts to their net asset value (NAV) (Williams 2016). The short-term discount is not necessarily bad, but the problem is that in long term the discount may create pressure from the investors side and the investor may start to withdraw their investments (Louch 2016). However, the discount is also a possibility for the investors as it means that the funds trades under its “real” value. The listed private equity funds started to trade at a discount because of lack of trust for the asset valuation (LPEq 2011: 7-9). More accurate methods for valuation has been implemented after the credit crises which should create more trust to the industry (LPEq 2011: 7-9). However, as explained in Chapter 2, unsold investments are hard to value. Therefore, it is normal that the listed private equity funds trade at discount, as the typical limited partner funds do so too before maturity (LPEq 2011:4; See page 7). Figure 7 provides key differences between limited partner private equity funds and listed private equity funds.

Limited Partnership Fund Characteristics	Listed Private Equity Characteristics
· Illiquid – limited and costly secondary market. · Generally 10 year fixed life with five-six year investment period. · Large commitment size typically £5m or more. · Tend to be focused. · Manager selection critical to performance · Initial investment at NAV. · Fees generally 1.5-2.0% with additional carry of around 20%, once hurdle rate achieved. · Investor rights generally limited to power to change manager. · Investors have access to detailed information on portfolio investments. · Investors must manage complicated cash-flows – drawdowns and distributions.	· Liquid – shares can be freely bought and sold on public market. · Usually unlimited life. · No minimum commitment. · Broad range of available strategies, diversified to focused. · Diversified fund of funds offers broad manager exposure. · Funds may be at a discount to NAV, though discount variable. · LPE fees are typically lower, but investment returns carry the underlying manager cost. · Usually full voting and shareholder rights and strong corporate governance. · Report & accounts meet minimum standards but portfolio information is variable. · Cash-flows are managed by the LPE manager.
Summary	**Summary**
Direct access to managers and detailed information on underlying companies, for large, sophisticated investors that are comfortable with illiquidity and can manage sometimes complicated cash-flows.	Liquid, diversified access to asset class with low minimum investment requirement and potential to boost returns by acquiring shares at discount to NAV.

Figure 7: Listed Private Equity and Limited Partnership Fund characteristics (LPEq 2011:12)

3.5 Vehicles for the Finnish Retail Investors

The thesis looks at the current opportunities that the Finnish investors have for investing in private companies. The public options are similar for Finnish retail investor than for others. Finland has few publicly held investment companies such as, Norvestia Oyj, Panostaja Oyj and Sievi Capital Oyj which invest directly from their balance sheet part of their assets to private companies. Capman Oyj is a listed Finnish private equity company (Fvca.fi). Norvestia Oyj was recently sold to Capman Oyj via share swop (Cns.omxgroup.com 2016). The study will look further at opportunities that Finnish retail investors have through two case examples.

3.5.1 Interval fund Elite Capman Collection

Elite group has a "fund of funds" that discloses its strategy as investing mainly to Capman's private equity funds. The minimum investment for the fund is €5 000. Additionally the fund invests in publicly traded private equity houses, and other asset classes like for stock and bonds to provide liquidity (Elitevarainhoito a). The fund is marketed as a private equity fund of funds, however while looking at their annual statement of 2016 it can be recognised that around 30 % is invested in the Capman's private equity funds (Elitevarainhoito b). The Fund has sizeable fees as, for investments under €100 000, investors are charged a management fee of 2,5%. In addition to the management fee, the fund charges a subscription fee of 3% and this is topped with a redemption fee of 1-5% depending on the length of the investment period (Elitevarainhoito a). The fund being a fund of funds means that there exists additional layer of fees, as the underlying funds have management fees, too. The fund structure seems similar to the interval funds discussed in the thesis (see page 16). The fund only offers a partial coverage to private equity as only 30% is invested into private equity funds. The fund has an additional 11,78% in private equity ETFs, 9% in Publicly Traded private equity companies and 9% in DNB Private Equity, which is according to Morningstar a Sub-fund, that invests in different Private Equity options, like companies, ETF and others. Therefore the fund has around 30% directly in private equity and 30% indirectly, while the rest is mainly in bonds (Elitevarainhoito b; Morningstar.fi). The Investors could invest in all the other assets directly besides the investment to the private equity funds, therefore the investors are paying aggressive management fees from the 30% of the assets.

3.5.2 Equity Crowdfunding in Finland

Several Equity crowdfunding platforms operate in Finland. Invesdor is one of the leading equity based crowdfunding platform in the Nordics (Invesdor). Invesdor has been able to provide nearly 30 Million euros for 78 companies (Invesdor.com). Invesdor had average investment round of €118 000 with a Pre-Money valuation of 1,5 million euros in 2015 (Invesdor). Invesdor's CEO Lasse Mäkelä has been interviewed for this thesis. Invesdor currently charges an initial €6 000 to start the due diligence process. Then 7% is charged as a success fee and an additional €1 500 as a legal closing fee is charged to conclude the share issue (Mäkelä 2017). The CEO of Kansalaisrahoitus Toni Lahti has been interviewed for this study. Kansalaisrahoitus is looked at as their model differ from the Invesdor's model. Kansalaisrahoitus does not currently have online platform, but is considering to develop one (Lahti 2017). One of the main differences in Kansalaisrahoitus's business model is the incentive model, which includes carried interest. Kansalaisrahoitus gets a fee from the successful deal as well part of the fee comes as a target company stock option (Lahti 2017).

4 Main Differences between Crowdfunding and Private Equity

To answer how retail investors could be efficiently involved in private equity, the differences between crowdfunding and private equity should be studied. In the authors opinion crowdfunding has proven its value when it comes to reward based crowdfunding platforms or donations based platforms. The reward based crowdfunding is an innovative way for companies to access funding. One of the best-known reward based crowdfunding companies is Kickstarter. Companies seek money through the platform and in return the company provides the investors a reward. The reward might be anything, but normally it is a product. The platform providers like Kickstarter earn their compensation in case the company will be able to collect the minimum they were looking for (Freedman & Nutting 2015: 5-7). The model seems fair as the crowd decides whether they are willing to “invest” money for the reward that is promised and then the platform charges a commission from the successful deals. This is an effective model where the rules are clear between all parties and the “crowd” is sophisticated enough to decide which companies should have the money for the reward. The investors have all the information needed for the decision-making process.

There are not large differences between the revenue models for different kinds of crowdfunding platforms, although the equity based crowdfunding revenue model has some variations. Crowdfunding has several similarities with private equity, as both typically provide funding to unlisted companies. The crowdfunding cases are closer to venture capital side of private equity as the investment are typically made to early stage companies (Greenberg, J 2015). Crowdfunding poses several core similarities with private equity from the investor’s point of view, such as illiquidity of the asset class. However, there exist several differences, too. One difference is that in crowdfunding, an investor can decide where to invest while in private equity the fund manager makes the decision. The fund managers however are professionals as the crowd can be anyone. Existing fear is that the crowd investors do not understand the risk that the asset class has and therefore will not have similar allocations as venture funds (Greenberg, J 2015). This chapter will cover the other differences between these models and how the process of professional private equity managers and the crowd investors differs. Things such as due diligence, the profit realisation and the incentive structure will be discussed in more detail.

4.1 Due Diligence Process

Due diligence should be looked at, as it is important aspect of an effective investment process. Freedman and Nutting (2015:205) characterise due diligence as a research and investigation that the investor should do before investing in any securities. The crowdfunding platforms are required to present fair information from the companies, however this is very different from the due diligence process. Due diligence is typically divided into three different sections; business, legal and financial. These are fundamental for every successful deal (Freedman & Nutting 2015:206-209).

Private equity investors are careful investors, who invest in only a fraction of the companies. Therefore, private equity firms do very extensive due diligence process. Due diligence process has been seen as one of the value creators in private equity (Leleux et.al 2015: 53). Santavirta (2017) sees that one of the main reasons, why she thinks that crowdfunding has more risk, as compared to similar phase venture capital firms, is that venture capital funds have a stricter selection criteria. The level of the due diligence process in crowdfunding is in every service providers' hands. Kansalaisrahoitus states that their process follows the standards of a private equity fund's due diligence (Lahti, 2017). In general, the due diligence process is stricter in private equity funds than in crowdfunding as private equity managers returns depend directly on it (Santavirta 2017). Vasconcelos (2014) also picks due diligence process to be one of the most important criteria to look at when choosing crowdfunding platforms, as the individual investors cannot have similar resources to spend on the due diligence process that the private equity funds have.

4.2 Profit Realisation

The process of profit realisation should be studied to offer an effective investment possibility for the retail investors. As explained in Chapter 2 the private securities are an illiquid asset, which means that opposite to the stock market the asset has poor secondary market (see page 6). Therefore, it is hard to access the profits before the exit process. The profits can be only realised by the form of dividends or by selling the investment. The investors should be aware that getting money out from the company might be hard and if eventually it is possible to sell the ownership to a third party, it might have to be done with a significant discount (Mäkelä 2017). This applies to private equity funds, too, as investors who wish to sell the commitments before the maturity are often forced to do so at a discount to the value (see page 7).

The exit process might be challenging for crowdfunding investors, however there are investment opportunities where crowdfunding can offer interesting opportunities. One of these is when the company's strategy is to return the investment to the shareholders via dividends. According to Asikainen (2017) these types of investments do not tend to interest private equity funds or business angels. Another phase where crowdfunding has been seen to be effective is the before listing round, as when a company wants to be listed it needs at least 300 shareholders, for this crowdfunding offers effective solution to restructure the owner base (Asikainen 2017; Mäkelä 2017). In these pre-IPO cases, the exit is at sight and the company is collecting funding for it. Mäkelä (2017) gave an example of Finnish company Heeros. Heeros raised capital through Invesdor in 2015 and was listed on the First North market place in 2016. It gave the investors some 15% return in less than a year (Mäkelä 2017). Lahti (2017) had similar example as a Kansalaisrahoitus success story. Cleantech Invest raised funding through Kansalaisrahoitus in 2013 and has had around 500% increase in value in 4 years (Lahti, 2017).

4.2.1 Voting Rights

One concern in crowdfunding platforms is that these do not always include voting rights (Kauppalehti.fi 2016). The investor with small stake even with voting rights has very little possibilities to affect the company's strategy through the board of directors of the company (Tähtinen 2017). Therefore, the investors should make sure that there is common strategical view between the shareholders. The company strategy should be in the shareholder's agreement as to protect the investors (Lahti, 2017). Crowdfunding could offer a solution, if all the investors would be pooled together and would have a representative in the board of directors to look out for their best interest. Although this might be hard as several of the investors may have different expectations. One way this could be assured is, for instance, if a venture capital firm acts as a lead investor. This is also seen to lower the risk (Airaksinen 2013). The crowd investor should be familiar with the investment process before investing, as this may affect their ownership later (Santavirta 2017). Some crowdfunding platforms offer pre-emption rights which is a way for the investors to be protected from dilution of the share in the possible follow-up investments, however the investor should always check whether the platform offers this (Vasconcelos 2014).

4.2.2 Incentive Model

Crowdfunding is practiced through different models. While the thesis is looking at the two common models, the basic difference of the models is that one of the models includes carried interest and the other one does not. Both models tend to have a success fee that is charged from the company (see page 20). This seems fair and effective to the company as the fees are paid based on success of the investment round (Lahti 2017). However, from the investor's point of view the success should be measured in return on the investment. As the return is uncertain until the investment is paid back to the investors, it should be argued that the model does not work in the investor's best interest. However, the investor should be familiar with the risks of the asset class (Santavirta 2017). There is always the risk that the investor might even lose the entire capital (Lahti 2017). One of the possible problems with the models that does have carried interest is that it may not work in an investor's favour as the models that have incentive towards returns tend to have better companies (Greenberg, J 2015). However, Mäkelä (2017) points out that Invesdor for instance, wish just to stay as a platform. This way he sees that the interest is biased. He does not believe that a platform model with a carried interest is better, as his opinion is that the roles would be mixed this way. By mixing organisers and investors roles, there is more risk that conflict of interest will arise. Additionally FIVA is looking at the roles of the provider according to Mäkelä (2017). Other crowdfunding providers on the market sees this very differently and wish to align their interests with the investors. Lahti (2017) states that the idea of Kansalaisrahoitus has been from the beginning to align the interest with the investors, this way they have interest towards the returns and will provide better cases.

Private equity fund managers have an incentive to exit their investments as this way the managers earn the carried interest. This model drives the exits of the private equity funds, which means returns for the investor. Private equity firms make certain plans that they will execute in the company (Leleux et.al 2015: 54). The Active management is one of the very core value creators in private equity (Santavirta 2017; Leleux et.al 2015: 54). Even if the platforms owners align their interest with the investors, they will not be actively managing the company. Therefore, even with aligned interest the platforms are not truly comparable to private equity. However, the investors could get an active owner if a private equity fund invests into the same company with same terms (See page 22). Mäkelä (2017) gave an example of this as company called Transfluent is currently raising money through Invesdor. Lahti (2017) also said that Kansalaisrahoitus has had several cases where there is a private equity fund has been a co-investor.

Start-up investing is a very risky business, were the odds seems to be against the investors. Even though the venture capitalist and angel investors have been able to make millions, we should be aware that they have wide portfolio of start-ups and they are very aware of the risks that most will fail. This raises the concern that individuals who will only invest in few early stage companies will get hurt, it has been even compared to lottery (Greenberg, J 2015). This suggests that the investors who would like to invest in this risky asset class would have their investments better covered with a professional manager that allocates the investments correctly (Santavirta 2017; Tähtinen 2017).

5 How to Efficiently Involve the Finnish Retail Investors in Private Equity

To answer the study how the retail investor could invest in private equity, the study looks at why they should invest. There is an ongoing debate about the problems of including unprofessional investors into risky private securities (Greenberg, G 2015). As we can see from Appendix1 of this study, this question has been asked from the professionals. Everyone answered that there is no reason why private equity should not be offered to retail investors. However, the GPs should have always the right to choose their customers (Asikainen, 2017). According to Asikainen (2017) collecting funds from many investors rather than from one institutional investor might not be a preferred choice of any GP as these additional investors do not really bring any value.

To offer retail investors private equity or private securities in general, we should first look how the investor should invest. Private securities are not the first asset class to allocate individual savings (Santavirta 2017). The investor should only allocate from 5-15%, depending on one's risk profile, this should be divided further into at least a dozen different companies (Freedman & Nutting 2015: 142; Tähtinen 2017). Mäkelä (2017) pointed out that unlisted securities are not necessarily riskier than the listed, but the question is rather about the maturity of the company that determines the risk level.

One of the risks in the asset class is that the investor might lose the investment capital (Lahti 2017). The question that one might ask is why would any retail investor be interested investing into such a risky asset class. The possibility to earn far greater returns than the other asset class is what draws the attention to private securities (Freedman & Nutting 2015:136-137). Another factor to notice is that alternative assets do not tend to correlate strongly with the public market, therefore the asset class offers diversification from the public market this then would special good for the portfolio (Freedman & Nutting 2015:138-141).

The retail investors would not even need to invest all their money to private equity, but rather to have opportunity to have a similar exposure to the asset class than the institutional investors have. In terms of diversification, it might be good to invest 10-15% of the total assets to private equity (Tähtinen 2017). The legislation has its point for protecting the retail investors on some level, that they do not lose all savings. Therefore, the rules that SEC has created for the JOBS act protect small investors as they are only allowed to invest 5% of their annual income to crowdfunding companies (Greenberg, J 2015). This an effective way to protect investors from losing too much for something as complicated as private securities. As average pension fund has asset allocation of 10% in private equity while individual investors currently have only 1-1.5%, therefore there is potential to involve retail investors more to the asset class (Butt 2016). Figure 3 shows that private equity has been the best source of revenue for the average public pension fund in the long run (See page 8). The reason why retail investors have been left out might be because the asset class has not been open to everyone (Lahti 2017; Santavirta 2017; Mäkelä 2017). There are several solutions how retail investors could be involved in private equity efficiently. This chapter will go through the findings and possibilities.

5.1 Common Vehicles

The possibilities that the retail investor have should be looked at to seek a better solution. Crowdfunding has several upsides compared to the traditional private equity, things such as easy access and small investment tickets are some core benefits of crowdfunding. However, as Santavirta (2017) points out, the retail investor might have difficulties in selecting the best investments. One of the problems has been that crowdfunding is missing the professional investors that public share market has (Asikainen 2017). Invesdor's investors are highly educated base on a study that has been made from their investors (Mäkelä 2017). However, a product that needs lot of knowledge to make the investment decision may not suitable for majority of the retail investors. Crowdfunding companies do not seem to get the best companies involved, which creates challenges (Asikainen, 2017). However, it is true that crowdfunding is still in its first steps, and therefore is hard to make yet any kind of judgement. Time will show us how crowdfunding companies will perform (Lahti 2017). A model that includes carried interest for the provider might be efficient for investors. However, Mäkelä (2017) makes a valid point, that this might confuse the roles. This is because a model that is purely a platform is more like stock picking, as the investor makes the decision. This might be effective, if the investor is capable to find the best investment cases.

The Elite's Interval fund Capman Collection, theoretically gives the investor exposure in private equity, with just a minimum ticket of €5 000. The downside of this fund are the relatively high fees of the fund and the underlying fees as the fund invests to other funds (See page 19). The Fund is affected by some of the positive outcomes that private equity offers, however as the fund only invest 30% directly to private equity funds, it is not the most effective for the retail investors and the fees might eat most of the returns in the long run.

The listed private equity companies are not really the same thing as the private equity fund as explained in chapter 3 (see page 17). The Public shares or the ETFs do not really cover private equity investments, therefore are not included in this chapter.

5.2 Primary Vehicles

In Finland licenced alternative asset managers could offer private equity funds to the retail investors (see page 14). However, the current form of private equity funds with its commitments is challenging for retail investors. This creates a situation where it is hard to involve retail Investors directly to the funds. A middle vehicle would be needed to collect all capital at once (Santavirta 2017; Tähtinen 2017). Another thing that would be good to consider is the liquidity and how this could be provided for the retail investors (Viitanen 2017).

5.2.1 Feeder Fund

Taaleritehdas has a real estate fund called *"Taaleri Afrikka Rahasto II"*. It is a limited partnership, with investment period of 10 years. The structure of the fund is similar with private equity funds. The fund offers the opportunity to the retail investors to invest in it. The minimum investment is €5 000, the investments are done through a "carried loan" (Taaleritehdas). How the carried loan works is that it pools the investment and then invest it to the underlying fund. The returns of the carried loan depend on the returns of the underlying fund. Therefore, the risk profile is similar as the underlying fund. The fund charges a commitment fee of 2%, then investors who commit under €50 000 are charged a management fee of 3%, the fund has a carried interest of 25% on the net returns (from investments below €50 000) and there is an additional fee of 0,2% (Taaleritehdas). This type of vehicle could be offered by private equity funds as the Taaleritehdas is licenced in the alternative asset manager list, which FIVA provides (Finanssivalvonta.fi). The manager would need a licence as it is marketed to retail investors. The benefits would be that it would be direct access to private equity, as the underlying fund would be a private equity fund. This way the investors would have access to the same product that the institutional investors have. The fees are in line with private equity fees, just slightly above as the management fee is 3% and the carried interest is 25%. However the 2/25 structure might be typical for real estate funds. The underlying fund charges the fees directly, thus there is only one layer of fees. The negative side of this kind of feeder fund where the capital is collected at once is that it affects strongly to the IRR. This is because the typical private equity fund collects capital when needed. Collecting all capital at once would mean that part of the money would just be waiting without generating revenue. However, this would still be the most direct access to private equity and it would generate the same revenues if measured in TVPI (see page 8). The investors would have an active manager that manages their money. This model lacks liquidity, so this means that the investors would need long-term commitment.

5.2.2 Listed Private Equity Fund

While Finnish investors can already invest into the foreign listed private equity funds, there are also few Finnish listed private equity vehicles (see page 18). If an investor wishes to promote the growth of Finnish growth companies, the foreign option will not serve. Investors should always look whether it is a listed fund or a listed private equity company as the former invests directly to the companies and the latter is only the managing company (see page 16-17).

Listed private equity have some absolute benefits like liquidity. However, as the share price tends to trade below the value NAV the funds do not seem to appeal investors. One reason for this might be that the investors do not understand the funds (Pritchard 2016). However, as a long-term investment the listed private equity could pay strong dividends when the assets (i.e. investments) are sold. The other key differences are that the listed funds do not have an end date (see figure 7). There are both positives and negatives to this. First, the fund can take longer positions in the companies and can earn the returns by dividends in the long-term. Another key benefit is that the fund is not forced to sell at a bad time, and the fund always looks at the best interest of the shareholders (Alpsredrocks.com). The negatives are that the fund managers can control the cash flows to the investors, whereas traditional limited partnerships have strict rules on profit distribution (see figure 7; see page 5). Another key difference is that the fees are more transparent in the traditional limited partnership model. Listed private equity managers are paid by the performance of the underlying company (Alpsredrocks.com). The performance of the fund might be subjective as it is very hard to measure unsold investments (see page 8-9). The investor should always check the investment policy of the company, additionally it would be good to check how the returns are expected to be paid in.

Several models have been provided in this thesis, and every model has unique characteristics. Figure 8 shows a comparison of the models and their benefits. Figure 8 indicates that active management comes with a cost. The more managers there are between the investors and the companies, the more fees. In terms of cost efficiency, an investor, who believes they are capable of building an effective portfolio could invest directly through crowdfunding. However, only the top managers in private equity perform extremely well (see page 8). The possibility that an unprofessional investor with less resources would be able to do so seems very unlikely.

	Private Equity	Listed Private Equity	Feeder	Interval Fund	Crowdfunding
Active Management	Yes	Yes	Yes, in the target fund	Yes, typically both; direct manager and the underlying fund managers	No
Decision making power	Fully at the General Partners hands	Fully in the managers hands	Fully in the target fund managers hands	Fully at the managers hands	Investor has full power
Diversified Portfolio	Yes, as one fund typically invests in several companies	Yes, as the investments are allocated typically in several companies	Yes, as the underlying fund typically invest in several companies	Yes, as the fund typically invest in several funds, that invest in several companies	No Diversification , however the investor has the possibility to create diversified portfolio
Cash management	Effective as capitals are called, when needed and distributed when received	The fund recycles the profits. Fund manager has the power to pay dividends for the share holders	Capitals are typically collected at once, however profits are often distributed when received	Possibilities to invest couple of times a year, as well as withdraws	Effective as Capital is invested directly to the company and distribution will be received directly
Fee Structure	Typically a 2% management fee and a 20% carried interest	Not transparent as Manager often receives performance fees, that reflects the development of the NAV	The target fund collects fee's directly, typically a 2/20 structure	Typically 2 layers of fees as the fund collect fees as well as the underlying funds	Depends on the model, however often no direct fees to the investors as the fees are charged form the company
Liquidity	Illiquid as secondary market is relatively small still	Liquid as the shares can be sold in stock exchange, however often trade at a significant discount to the NAV	Illiquid, no data on the secondary market	Some sort of liquidity as the fund typically allows withdraws on quarterly basis	Illiquid, secondary market still very undeveloped
Ownership Structure	Typically owned through limited partnership structure	Typically owns the shares of the fund, that owns the company shares	Typically practiced through carried loan structure, therefore have rights to part of the distributions	Owns a stake of the Fund that owns different assets (typically different funds and stocks)	Most models include direct ownership structure, however depends on the platform provider
Finnish Retail Access /Possibilities	Currently no or limited access, the structure is very complicated to retail investors	Few vehicles in Finland. Several foreign possibilities exists.	Currently none in Finland, however very possible to make if a licensed Private Equity manager wish to do so	At least one fund in Finland with a minimum investment of 5000€	Several possibilities as several platforms operate in Finland

Figure 8: Comparing Private Security Vehicles

6 Conclusions

Private equity is a challenging, but rewarding asset class with its unique characteristics. The asset class is dominated by large institutional investors and these investors will continue to be the majority in the asset class. However, this does not mean that the retail investors should be left out completely. Private securities offer diversification that differentiates from the public equities. It should be remembered that private equity is a very risky asset class, therefore it needs proper asset class allocation to work. While looking at the institutional investor's portfolio the typical allocation is between 10-20% in private equity. The retail Investors should use this as rule of thumb, although this also depends on each individual's risk profile.

As the thesis indicates, Finnish retail investors are less exposed to private equity investments than their European peers. This is caused by several external factors, such as restrictive regulation discouraging service providers from offering such investment opportunities. In addition, private equity fund managers tend to favour institutional investors, as raising funds from retail investors is time consuming due low average investment amounts. Traditional private equity investment vehicles, such as private equity funds (both listed and unlisted) and specialised funds (interval funds) lack transparency and are considered to be complicated and expensive by retail investors as well as industry experts.

As the Finnish market has evolved and new opportunities have emerged with the birth of several crowdfunds, retail investors are becoming more exposed to the private equity asset class. Crowdfunding is a very innovative tool offering private equity investing to everyone, now everyone can be a venture capitalist. Namely, as crowdfunding implies that investors have to invest directly into companies it is risky by nature and requires in-depth understanding. Hence, the biggest differences between crowdfunding and private equity funds are active management that private equity funds have and the funds themselves are diversified with several underlying investments. Therefore, crowdfunding cannot offer similar benefits as private equity funds do. Considering the pros and cons of various private equity investment vehicles, several effective possible options exist on how retail investors could be involved in private equity. Such vehicles would include; 1) Listed private equity company investing directly into companies (via its own balance sheet), 2) Feeder fund i.e. carried loan.

The Finnish legislation makes private equity technically possible for everyone. The private equity manager who wishes to target the retail investors is required to have a licence. The licenced managers need more resources and capital than the registered ones. This has led to a situation in which registration is far more common amongst Finnish private equity managers (FIVA 2017).

As to policy implications this study suggests that the regulation for private equity could be lighter, as this could lead to a situation where Finnish private equity firms and funds would have more capital from retail investors. This would then contribute to the whole economy as well as to the investors. However, the risks of private securities should be recognised.

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Interview questions for the Industry Experts

Private Equity in general:

1. What affects Private Equity has for the Finnish economy?
   - Negatives and Positives
   - The pros and cons for retail investors
2. How important is Private Equity for the Finnish economy?
3. How do you think that Fin-tech will affect the future of Private Equity?

Retail Investors:

4. Retail investors current opportunities to invest in private securities?
   - How does the individual wealth affect this?
   - Discuss differences for Crowdfunding, Direct investing and Private Equity
5. Should the retail investors in have opportunities to invest in unlisted securities and why?
   - Is there some investment format(s), that should be only offered to institutional investors?
   - What has led to situation that private investors are not investing to unlisted companies (as the global average is 1-2 % while institutional investors invest 10-20% of their portfolio)?
   - How the retail investor should diversify the investments for private companies (include the total allocation for investors portfolio)?
6. What are the key aspects that a retail investor should consider when investing in private securities?
7. What do you consider to be the best way for retail investor to invest in unlisted companies (i.e. the channel)?
   - Are there key differences between experienced and unexperienced investor?
8. How the retail investors can be sure that the board of directors will drive for their best interest?
   - Or the strategy of the company i.e. Exit, evergreen or a ”just for fun” investment
9. As in the United States Private Equity funds exist, where the minimum investment is $10 000 (for accredited investors only)

- Do you believe that in Finland or Europe this will happen in the future?

Equity Crowdfunding:

10. Do you think that crowdfunding is needed?
    - Discuss from investors and companies' perspective
11. What challenges and opportunities do you see in Crowdfunding?
    - Discuss from investors' and companies' perspective
    - What are risks in crowdfunding?
    - Does "over marketed" cases exist?
12. Do you think that crowdfunding has more/ less risk than Private Equity, why?
    - If more why do you think it is possible to market crowdfunding to retail investors and the registered Private Equity funds managers can't (expect for wealthy individuals)?
13. Is the Crowdfunding platform fee model effective?
    - What kind of model your platform uses? (only asked from crowdfunding providers)
    - How the model could be improved?
    - Would the model be more effective if it would include carried interest, why?
14. Do you think that companies which seek money through crowdfunding get a certain reputation?
15. Do you think, that the "Crowd" is enough sophisticated to make the investment decisions (or to choose the best possible investments)?
16. Do you known an example of a crowdfunding success for investor, exit wise?
17. Your opinion on; what kind of companies seek funding through crowdfunding portal?
    - What are the different motives to seek funding?
    - How are the companies chosen to the portal?
    - What kind of companies should seek funding rather through crowdfunding than from Venture Capitalist or Angel investors
    - What benefits does crowdfunding bring for; investors, companies and platforms?
    - Does crowdfunding portal target companies' valuations differ from comparable Venture or Angel portfolio companies' valuations? If yes what could/should be done to this?

- How Crowdfunding portals could attract even better target companies?

18. What are the responsibilities of; crowdfunding portals and target companies, for example in a bankruptcy situation?

Legislation

19. How Private Equity is regulated?
    - How does it differ from crowdfunding regulations or other such as direct investment regulation?
20. Why Private Equity is so heavily regulated?
21. Does the Regulation protect individual investors?
22. Do you think that the regulation is too strict?

Interview Questions for the Finnish Financial Supervisory Authorities

Private Equity:

1. How it is ensured, that individual investors understand the risk, which private securities have?
2. How Private Equity is regulated and how does it differentiate from other investment forms?
3. Why Private Equity is regulated stricter than other investment forms?
4. What are the core differences between registered and licenced alternative asset managers?
5. Why Private Equity is primarily only indented for professional investors?
6. What is meant by Financial Supervisory authority's exemption clause on possibility to market alternative funds for non-professional investors?
7. Is it possible to establish a Private Equity fund that would be marketed to non-professional investors?

Equity Crowdfunding:

8. Why retail investors can invest to Crowdfunding, but not for instance to Private Equity funds?
   - Does Crowdfunding have less risk than Private Equity funds?
   - Is Crowdfunding categorised differently than Private Equity (not as alternative investment)?
9. How is the fund raising regulated in Crowdfunding?
   - Is the Fee structure regulated?
   - Should the fee structure be regulated?
10. Crowdfunding responsibilities (in a bankruptcy situation for instance)?
11. How it is ensured, that individual investors understand the risks relating to Crowdfunding?
12. How it is ensured that the investors get all the necessary information from the target company?
13. Is it possible to establish a Crowdfunding fund (or a Fund that invest through a certain Crowdfunding portal)?

Special Investment Funds:

14. How one could to have a licence for a special investment fund that invest its assets to Private Equity?

- Can the fund be closed fund?
- Is there a maximum percentage that this type of fund could invest in Private Equity?
- How should the liquidity to investors be arranged?

15. Is it possible to market Fund of Funds to retail investors?