Newsletter (20) - Democratization of Private Equity

(1) Introduction

In today's newsletter we look at the democratization of private equity, which is the process of making private markets more accessible to a wider range of non-institutional investors. Family offices, endowments, pension funds, insurers, and sovereign wealth funds are examples of institutional capital that have historically dominated the private equity market. These investors, due to their structure, have accepted the lengthy holding periods, a lack of transparency, and structural illiquidity associated with private equity investments. However, as retail demand grows in the sector, private equity is being democratized. New platforms and fund structures have made private equity easier to access, but higher fee layers, liquidity constraints, and continued institutional perks like co-investment rights and priority deal access suggest that broader participation doesn't fully level the playing field or guarantee the same risk-return profile.

(2) Lowering the Barriers: New Investment Structures

Several new vehicles are making private equity more accessible. This section outlines the main instruments and the challenges each is designed to address.

Evergreen and semi-liquid funds are a core innovation. They are open-ended and often offer periodic liquidity, as managers can keep recycling capital from exits into new deals, investors
get a smoother return path. Most importantly, they can reduce the early J-curve, which in classic closed-end funds often leads to negative returns in the first 3–5 years due to management fees and investment costs. This, along with lower minimum investment requirements and the elimination of capital calls, makes evergreen funds key enablers for retail access to private equity. The trade-off is that these funds usually need cash buffers and liquidity management, so the portfolio is not always fully invested, and cash drag can reduce returns.

Regulated retail wrappers such as ELTIFs (European Long-Term Investment Funds) and interval funds also widen access. They are built for non-institutional investors and allow limited flexibility through redemption windows and liquidity gates, even though the underlying assets remain illiquid. This structure helps balance investor access with fund stability, while preventing forced asset sales during periods of market stress.

Another route enabling retail access to private equity investments is listed private equity, where investors buy public shares of listed PE managers or listed PE funds. This gives easier entry and daily pricing. However, returns are influenced by public-market volatility and may diverge from the NAV-based returns typically experienced by institutional private equity investors.

Finally, distribution platforms such as Trade Republic are partnering with managers like EQT and Apollo to make these products easier to buy in small amounts, sometimes even fractionally, often using evergreen ELTIFs and internal secondary mechanisms to support liquidity. Overall, these structures broaden access to private equity, but do so by managing, rather than eliminating the asset class's inherent illiquidity and complexity.

(3) Secondaries as a Gateway to Private Equity

Alongside the emergence of more flexible fund structures, the rapid expansion of the private equity secondaries market has become a critical enabler of broader investor participation. By allowing investors to acquire existing fund interests or portfolio assets rather than committing capital at inception, secondaries materially lower several structural barriers that have historically limited access to private equity.

For new and retail-oriented investors in particular, secondaries address one of the most persistent challenges of traditional private equity: the J-curve. Secondary investors typically gain exposure to portfolios that are already partially or fully invested. This accelerates time to cash flows, reduces blind pool risk, and improves visibility into asset quality, valuation, and manager execution.

LP-led secondaries, which are transactions where existing limited partners sell their private equity fund interests to secondary buyers to gain liquidity before the fund matures, play a central role in this evolution. These transactions provide access to seasoned portfolios with established operating histories, offering greater transparency into underlying assets, cash flow dynamics, and GP behavior. Within semi-liquid or retail-access vehicles, LP-led secondaries also serve an important portfolio construction and liquidity management function, enabling exposure to mature assets while preserving flexibility at the fund level.

GP-led continuation funds represent a further development in the secondaries ecosystem. In these structures, general partners transfer one or more portfolio companies into a newly formed vehicle, giving existing investors the option to exit or roll over their exposure. For new investors, continuation funds provide access to high-conviction assets later in the value-creation cycle, often after significant operational and strategic initiatives have already been implemented. As a result, these transactions can shorten duration, improve cash flow visibility, and partially mitigate J-curve effects.

The growing prominence of secondaries reflects broader structural shifts within private markets. Longer holding periods, reduced IPO activity, and constrained traditional exit channels have increased demand for alternative liquidity solutions, pushing secondaries from a niche strategy into a core component of private market infrastructure. In this context, secondaries have emerged as one of the most scalable and investable entry points for democratization initiatives in private equity. That being said, secondaries do not fundamentally democratize private equity ownership. While they improve investability and accessibility at the product level, information asymmetry remains significant, asset-level ticket sizes remain large, and pricing power continues to favor institutional investors and experienced secondary managers. Consequently, secondaries primarily expand access through intermediated structures, enhancing exposure and liquidity without meaningfully broadening control, governance, or direct ownership across the investor base.

(4) Trade-Offs: Liquidity, Returns, and Risk

Democratization brings access to attractive growth opportunities as private equity has performed strongly over the last years. Gompers and Kaplan found that between 1995 and 2021, PE funds outperformed the S&P 500 by about 5% annually. However, expanding access to private markets also introduces structural trade-offs that investors must clearly understand.

One of the biggest challenges is balancing liquidity expectations with the illiquid nature of underlying assets. Even in semi-liquid or interval-style funds, redemption terms are conditional and restricted. During periods of market stress, funds may have to resort to liquidity gates, extended notice periods, or forced secondary sales to control outflows, often at unfavorable valuations. As a result, perceived liquidity may diverge materially from realized liquidity when it is most needed.

Another area of concern is fee layering and complexity. Many democratized private equity products gain exposure indirectly, investing on top of traditional private equity funds or secondary strategies, thereby introducing multiple layers of management and performance fees. Although this does not impact the underlying investment thesis, it can meaningfully affect net returns, especially in smaller allocations where fee drag is proportionally more pronounced.

A further issue is the potential dilution of returns. In order to facilitate periodic liquidity and diversification needs, some retail-focused strategies may choose more prudent investment rhythms, higher cash allocations, or more diversified structures. These strategy choices may mitigate risk exposure to the most illiquid and highest-upside parts of the PE universe.

Lastly, there is the matter of investor understanding and misalignment. Stanford studies have indicated that a lack of proper safeguards in the democratization of private equity may increase systemic risks. As indicated in a Stanford GSB commentary, a poorly constructed democratization process may transform private equity into a “systemic risk machine” instead of a portfolio stabilizer.

Crucially, lower minimum investment thresholds do not reduce the fundamental risks of private equity. Operational risk, leverage, valuation subjectivity, and exit dependence remain defining characteristics of the asset class. Democratization alters the access point, but not the underlying risk profile, making investor education and structural design critical to sustainable participation.

(5) Conclusion

In conclusion, while recent trends have increased accessibility to private equity, they do not yet amount to a full democratization of the asset class. New fund vehicles, secondaries, regulatory solutions, and distribution channels have decreased the barriers to entry and transformed the way investors access private markets.

But the essence of private equity has not changed. Creating value through operational enhancements, capital management, and exit strategies remains the same. Information asymmetry, governance concentration, and episodic liquidity continue to favor institutional investors. As a result, current trends are better understood as a repackaging of private equity exposure, rather than a redistribution of ownership or control. Whether these developments ultimately benefit retail investors will depend less on access itself and more on expectation management, transparency, and alignment between investors and managers.