

Staying Private: The New Path for Liquidity

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The shift toward secondary share sales, as opposed to traditional initial public offerings (IPOs), is a reflection of several interconnected factors shaping modern financing. This trend raises important questions about the evolving dynamics of capital markets, particularly for high-growth technology companies. These factors include market volatility, regulatory pressures, and the desire for founders and employees to maintain operational and cultural autonomy while still accessing liquidity.

Staying Private: The New Path for Liquidity

The data presented in the graphic below demonstrates how secondary share sales from just seven private companies — including major players like Stripe, Canva, and Databricks — have collectively raised more funds than all tech IPOs combined in the past two years. This underscores the declining reliance on public markets as a source of capital for private tech companies. Instead, companies are leveraging secondary markets to provide liquidity for founders, early employees, and even some existing investors, bypassing the traditional IPO route.

This phenomenon is emblematic of a broader shift in the capital-raising landscape. In the past, going public was seen as the ultimate milestone for a company, providing access to a broader investor base and enabling large-scale capital infusion. However, the volatility of public markets in recent years, coupled with rising interest rates and the complex regulatory burdens associated with being a public company, has made IPOs less attractive.

Advantages of Secondary Market Liquidity

Avoiding Public Market Volatility:

Companies like Stripe and Canva are staying private to shield themselves from the unpredictability of public market dynamics. Public markets, especially for tech companies, have been subjected to dramatic valuation swings driven by macroeconomic factors like inflation, geopolitical uncertainty, and tightening monetary policies. In such a climate, secondary share sales offer a safer, more controlled way to secure liquidity without exposing the company to external pressures.

Maintaining Operational Focus:

Public companies face intense scrutiny from shareholders, analysts, and regulators, often leading to a short-term focus on quarterly earnings at the expense of long-term innovation. By staying private, companies can focus on product development, market expansion, and other strategic priorities without the distraction of appeasing external stakeholders.

Empowering Founders and Employees:

Secondary share sales allow founders and early employees to realize some of the financial benefits of their equity without being forced to wait for a liquidity event like an IPO. This approach not only rewards early contributors but also helps companies retain top talent by offering a tangible financial benefit that rivals the compensation packages of public companies.

Private Funding Remains Robust:

The influx of capital into private markets from venture capital firms, private equity funds, and institutional investors has created a favorable environment for secondary transactions. These investors, flush with cash and seeking high-growth opportunities,

are willing to fund late-stage companies in exchange for equity, even if the company remains private for longer.

The Role of Investor Demand

The demand for secondary market transactions is not just a company-driven phenomenon; it is also fueled by investors seeking access to high-growth companies before they go public. Many institutional investors and venture capital firms see secondary share sales as an opportunity to invest in companies at valuations lower than what might be achieved in a future IPO. This dynamic creates a win-win situation: companies gain liquidity without going public, and investors gain access to promising companies earlier in their lifecycle.

The Broader Implications for Capital Markets

The rise of secondary share sales and the corresponding decline in IPO activity suggest a fundamental transformation in how companies approach funding. While this trend offers several advantages, it also has broader implications for the ecosystem.

Reduced Public Market Participation:

When companies delay or forgo IPOs, retail investors lose out on opportunities to invest in high-growth companies during their formative years. Historically, public markets have served as a democratizing force, allowing individuals to invest in companies like Apple or Amazon at relatively early stages. The shift to private markets and liquidity risks limiting these opportunities to institutional investors and wealthy individuals.

Valuation Transparency:

Public companies are required to disclose financial information regularly, which provides transparency to investors and fosters market efficiency. Private companies, on the other hand, operate with less oversight, making it harder to assess their true financial health and valuation. The reliance on secondary markets, where valuations are negotiated in private transactions, exacerbates this lack of transparency.

Potential for Overvaluation:

In a competitive private funding environment, where investors are eager to participate in high-profile companies, there is a risk of inflated valuations. While this benefits companies in the short term, it can create challenges during future funding rounds and an eventual IPO, as public markets may not be willing to support these lofty valuations.

Concentration of Wealth:

The growing importance of secondary share sales in private markets may exacerbate wealth concentration among institutional investors and early insiders. As companies stay private longer, the majority of wealth creation occurs within a relatively small circle of stakeholders, further excluding retail investors.

A Symptom of Unpredictable Markets or a Permanent Shift?

The question remains whether this trend is a temporary response to current market conditions or a more permanent shift in tech financing. While the macroeconomic environment has undoubtedly influenced the rise of secondary share sales, there are structural advantages to this approach that may persist beyond the current cycle: flexibility, control, and reduced regulatory burden associated with staying private. These are compelling reasons for companies to continue leveraging secondary markets in the years to come.

However, it is unlikely that IPOs will disappear altogether. Going public still offers unique benefits, such as access to a larger pool of capital, increased brand visibility, and the ability to use publicly traded stock as currency for acquisitions. As market conditions stabilize, we may see a resurgence of IPO activity, albeit at a pace and scale that reflect the lessons learned during this period of secondary market dominance.

Conclusion

The image encapsulates a profound shift in the way high-growth technology companies approach capital raising. Secondary share sales have emerged as a viable alternative to traditional IPOs, offering liquidity and flexibility while insulating companies from the challenges of public markets. This trend represents both an adaptation to current economic realities and a strategic rethinking of long-term financing models. While it offers numerous advantages, it also raises important questions about transparency, equity, and the future of public market participation. As the landscape continues to evolve, stakeholders will need to balance the benefits of private market innovation with the broader societal role of public markets in wealth creation and economic growth.

