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WHAT IS THE DIFFERENCE BETWEEN PRIVATE EQUITY AND VENTURE CAPITAL?

The terms private equity and venture capital are often used interchangeably, but if your company is looking for investors, whether you should pursue private equity or venture capital investors can differ depending on the type of company and your long-term goals.

What is Private Equity?

Private equity refers to ownership of, or an interest in, a company that is not publicly traded or owned. Private equity investors generally seek out mature, established companies and acquire a majority, controlling interest. Private equity investors may seek out businesses in distress or businesses that are successful but that could benefit from increased efficiency or further resources. Because private equity investors usually acquire a controlling interest, they tend to be more hands on in the management of the business, seeking to spearhead changes to increase profitability, often including streamlining the business and making leadership changes. The goal for most private equity investors is to sell the business, with its improved operations, for a profit. Thus, private equity investors tend to focus on short-term value maximization to ensure a return on their investment.

What is Venture Capital?

Venture capital refers to financing invested in startups or smaller companies, generally closer to their infancy, that show significant growth potential. In this sense, venture capital is actually a subset of private equity. Venture capitalists tend to acquire less than a majority interest in the business. As such they can still lend their expertise, but have less control and may have less of a hand in the day-to-day business. Further, because venture capitalists seek out young, growing companies, they tend to be more interested in the long-term value of the company. An "angel investor" is also a specific type of venture capital investor. Typically, this term refers to an individual who invests their own money in startups, rather than through a capital company owned by a group of investors. Angel investors may invest earlier than other venture capital in a startup and may exit earlier as well, as they focus on the early-stage funding for startups.

What Are the Key Similarities and Differences?

- Because venture capital is a type of private equity, both are forms of investments in privately held companies with the goal of increasing the value of the company and making a profit.

- Private equity investors tend to invest in older, more established companies that have the potential to increase profitability with the help of investors. On the other hand, venture capitalists tend to invest in young, growing startups with unproven, yet promising, value.
- Private equity investors generally seek to acquire a controlling interest in a company, while venture capitalists generally acquire a minority share of a company.
- Private equity investors are more likely to be involved in the decision making of the company and to be more hands on. Venture capitalists, by contrast, may be more hands off, especially with day-to-day matters.
- The goal for private equity investors tends to be more focused on maximizing the value of the company in the short-term with the intent to sell the company once it has done so. On the other hand, the goal for venture capital investors tends to thinking about value in the long-term with the intent to maintain equity until the company reaches a good cash-out event such as going public. As such, venture capitalists are long-term investors who aim to get in early on company with long-term potential.
- While both types of investments are riskier than investing in established publicly traded companies, venture capital investments tend to be riskier for investors than general private equity given the volatile nature of startups. About 90% of startups fail, so venture capital investors expect that the majority of their investments may not pan out. In contrast, private equity targets more mature companies that they hope to purchase on a discount, providing for more opportunity to turn a profit.

JAH Can Help

Working with private equity or venture capital investors can be a challenging but exciting prospect. The experienced **corporate attorneys** at JAH are available to counsel you throughout the investment process, ensuring that your business is protected and its value is maximized. **Click here to contact** a member of our **Corporate Group** if you are in need of assistance.
