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Slumping IPO Market Bodes Poorly for Private Equity Firms Seeking to Cash Out

By Eric Guo, J.D. Candidate 2018 | October 20, 2015

The recent slowdown of the initial public offering market has made private equity firms suffer. Private equity produce profits through two main channels: management fees based on assets, and commissions generated from the profits of the private equity funds. The latter method is their dominant moneymaking strategy. Bringing the companies in their portfolios to initial public offerings is one of the main ways that funds generate profits. As a result, a slowdown of the IPO market means that private equity firms are losing their potential profit.

The sharp fluctuations in the stock market in recent months have chilled the market overall and produced more risk-averse investing behaviors. The capital raised from U.S. offerings so far this year is less than half of the amount raised by the same time last year. These market trends have left companies that want to list their stock feeling justifiably converned. For example, supermarket chain Albertsons Companies, Inc. delayed its IPO last week because of negative market expectations. Similarly, luxury retailer Neiman Marcus Group, Inc. delayed its I.P.O until next year because of unfavorable market conditions.

Many of the companies that have delayed their IPOs, including Albertsons and Neiman Marcus, are private equity-backed. Albertsons is owned by Cerberus Capital Management. The supermarket chain originally planned a nearly 2-billion-dollar public offering. As a result, Cerberus's expected profits from the I.P.O are on indefinite hold. Neiman Marcus is jointly owned by the private equity firm Ares Management and Canadian Pension Plan Investment Board. As the company delayed its I.P.O, the two funds will have to wait until at least next year to collect the profit on their investment. Moreover, one of the largest private equity firms, Blackstone, has posted a loss due to overwhelming market volatility. The firm disclosed that it suffered a loss of 416 million dollars, compared to 758 million dollars in profit last year, indicated by the economic net income.

There are still companies successfully completing their offerings. First Data, a payment process company, raised 2.6 billion dollars in its IPO. However, the company's expected price was at 18 dollars to 20 dollars per share, while the price after the IPO was actually 16 dollars per share. The company's owner, private equity firm KKR, did not sell any stock in the offering.