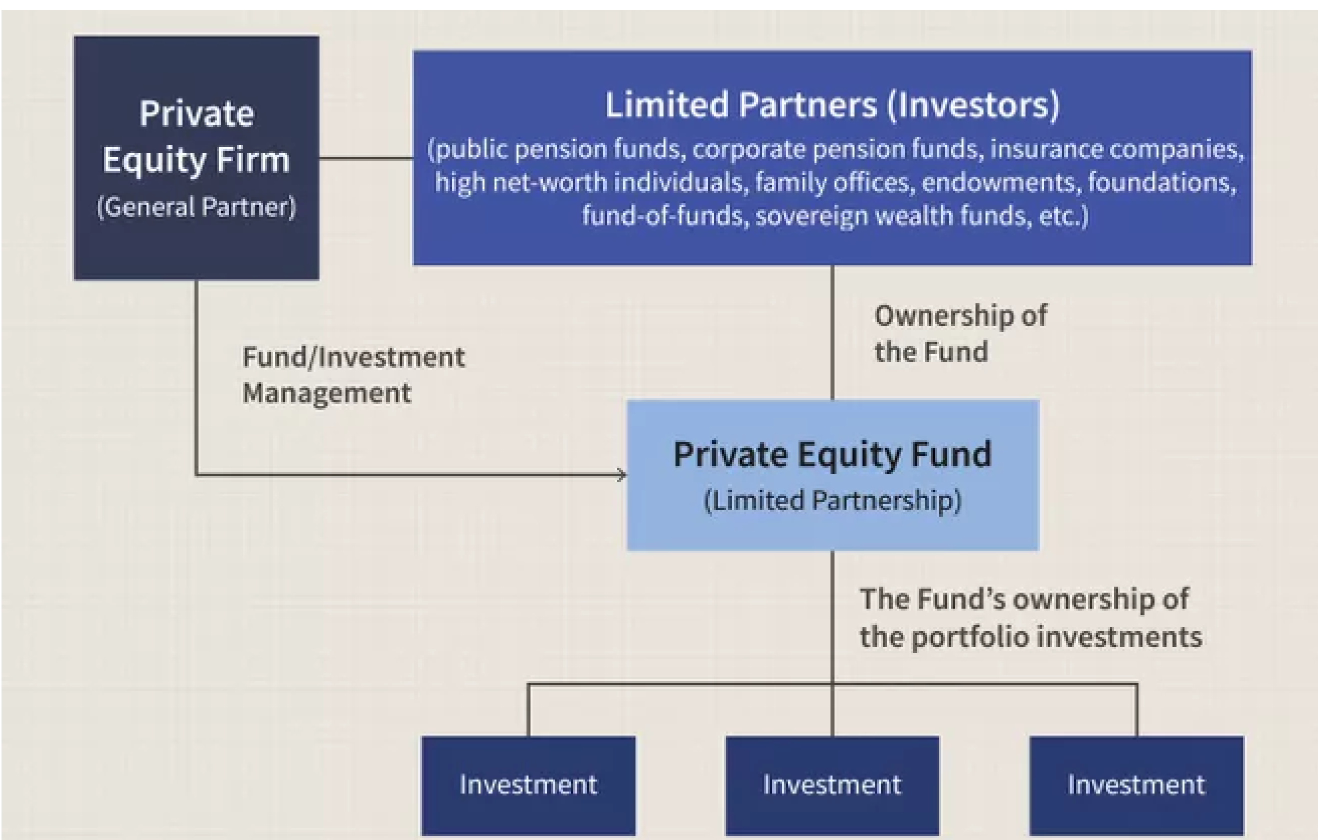
Private Equity:

- Private equity is an alternative form of private financing, away from public markets, in which funds and investors directly invest in companies or engage in buyouts of such companies.
- Private equity firms make money by charging management and performance fees from investors in a fund.
- Among the advantages of private equity are easy access to alternate forms of capital for entrepreneurs and company founders and less stress of quarterly performance. Those advantages are offset by the fact that private equity valuations are not set by market forces.
- Private equity can take on various forms, from complex leveraged buyouts to venture capital.

Understanding Private Equity

Private equity investment comes primarily from institutional investors and accredited investors, who can dedicate substantial sums of money for extended time periods. In most cases, considerably long holding periods are often required for private equity investments in order to ensure a turnaround for distressed companies or to enable liquidity events such as an initial public offering (IPO) or a sale to a public company.



Advantages of Private Equity

- Private equity offers several advantages to companies and startups.
- It is favored by companies because it allows them access to liquidity as an alternative to conventional financial mechanisms, such as high interest bank loans or listing on public markets.
- Certain forms of private equity, such as venture capital, also finance ideas and early stage companies.
- In the case of companies that are de-listed, private equity financing can help such companies attempt unorthodox growth strategies away from the glare of public markets.
- Otherwise, the pressure of quarterly earnings dramatically reduces the time frame available to senior management to turn a company around or experiment with new ways to cut losses or make money.

Disadvantages of Private Equity

- Private equity has unique challenges. First, it can be difficult to liquidate holdings in private equity because, unlike public markets, a ready-made order book that matches buyers with sellers is not available.
- A firm has to undertake a search for a buyer in order to make a sale of its investment or company.
- Second, pricing of shares for a company in private equity is determined through negotiations between buyers and sellers and not by market forces, as is generally the case for publicly-listed companies.
- Third, the rights of private equity shareholders are generally decided on a case-by-case basis through negotiations instead of a broad governance framework that typically dictates rights for their counterparts in public markets.

Hedge Funds:

- Hedge funds are actively managed alternative investments that typically use non-traditional and risky investment strategies or asset classes.
- Hedge funds charge much higher fees than conventional investment funds and require high minimum deposits.
- The number of hedge funds has been growing by approximately 2.5% over the past five years but they remain controversial.
- Hedge funds were celebrated for their market-beating performances in the 1990s and early 2000s, but many have underperformed since the financial crisis of 2007-2008, especially after fees and taxes are factored in.
- For example, the manager of a fund that focuses on a cyclical sector that does well in a booming economy, such as travel, may devote a portion of the assets to stocks in a non-cyclical sector, like food or power companies. If the economy tanks, the returns of the non-cyclical stocks should offset the losses in cyclical stocks.
- In modern times, hedge fund managers have taken that concept to an extreme. In fact, their funds have little to do with hedging, except for a few who stick to the original concept of the hedge fund, known as the classic long/short equities model.

How Hedge Funds Are Categorized

- Each hedge fund is designed to take advantage of specific market opportunities. They can be categorized into a number of broad hedge fund strategies such as event-driven investing and fixed-income arbitrage. They are often classified according to the investment style of the fund's manager.
- Legally, hedge funds are often set up as private investment limited partnerships that are open only to a limited number of accredited investors and require a large initial minimum investment.
- Investments in hedge funds are illiquid as they often require investors to keep their money in the fund for at least one year, a time known as the lock-up period. Withdrawals may also only happen at certain intervals such as quarterly or bi-annually.

Liability:

- A liability (generally speaking) is something that is owed to somebody else.
- Liability can also mean a legal or regulatory risk or obligation.
- In accounting, companies book liabilities in opposition to assets.
- Current liabilities are a company's short-term financial obligations that are due within one year or a normal operating cycle (e.g. accounts payable).
- Long-term (non-current) liabilities are obligations listed on the balance sheet not due for more than a year.
- Liabilities are a vital aspect of a company because they are used to finance operations and pay for large expansions.
- They can also make transactions between businesses more efficient.
- For example, in most cases, if a wine supplier sells a case of wine to a restaurant, it does not demand payment when it delivers the goods. Rather, it invoices the restaurant for the purchase to streamline the drop-off and make paying easier for the restaurant.
- The outstanding money that the restaurant owes to its wine supplier is considered a liability. In contrast, the wine supplier considers the money it is owed to be an asset.

Current Liabilities

Ideally, analysts want to see that a company can pay current liabilities, which are due within a year, with cash. Some examples of short-term liabilities include payroll expenses and accounts payable, which include money owed to vendors, monthly utilities, and similar expenses.

Non-Current Liabilities

Considering the name, it’s quite obvious that any liability that is not current falls under non-current liabilities expected to be paid in 12 months or more.

Asset:

- An asset is a resource with economic value that an individual, corporation, or country owns or controls with the expectation that it will provide a future benefit.
- Assets are reported on a company's balance sheet and are bought or created to increase a firm's value or benefit the firm's operations.
- An asset can be thought of as something that, in the future, can generate cash flow, reduce expenses or improve sales, regardless of whether it's manufacturing equipment or a patent.
- A right or other access is legally enforceable, which means economic resources can be used at a company's discretion, and their use can be precluded or limited by an owner.
- For an asset to be present, a company must possess a right to it as of the date of the financial statements.
- An economic resource is something that is scarce and has the ability to produce economic benefit by generating cash inflows or decreasing cash outflows.

Types of Assets

Current Assets: Current assets are short-term economic resources that are expected to be converted into cash within one year. Current assets include cash and cash equivalents, accounts receivable, inventory, and various prepaid expenses.

Fixed Assets: Fixed assets are long-term resources, such as plants, equipment, and buildings. An adjustment for the aging of fixed assets is made based on periodic charges called depreciation, which may or may not reflect the loss of earning powers for a fixed asset.

Financial Assets: Financial assets represent investments in the assets and securities of other institutions. Financial assets include stocks, sovereign and corporate bonds, preferred equity, and other hybrid securities. Financial assets are valued depending on how the investment is categorized and the motive behind it.

Intangible Assets: Intangible assets are economic resources that have no physical presence. They include patents, trademarks, copyrights, and goodwill. Accounting for intangible assets differs depending on the type of asset, and they can be either amortized or tested for impairment each year.

Mezzanine financing:

- Mezzanine financing is a way for companies to raise funds for specific projects or to aid with an acquisition through a hybrid of debt and equity financing.
- Mezzanine lending is also used in mezzanine funds which are pooled investments, similar to mutual funds, that offer mezzanine financial to highly qualified businesses.
- This type of financing can provide more generous returns to investors compared to typical corporate debt, often paying between 12% and 20% a year.
- Mezzanine loans are most commonly utilized in the expansion of established companies rather than as start-up or early-phase financing.
- Both mezzanine financing and preferred equity are subject to being called in and replaced by lower interest financing if the market interest rate drops significantly.
- Mezzanine financing can be considered as very expensive debt or cheaper equity, because mezzanine financing carries a higher interest rate than the senior debt that companies would otherwise obtain through their banks but is substantially less expensive than equity in terms of the overall cost of capital.
- It is also less diluting of the company's share value. In the end, mezzanine financing permits a business to more more capital and increase its returns on equity.

Characteristics are common in the structuring of mezzanine loans, including:

- Mezzanine loans are subordinate to senior debt but have priority over both preferred and common stock.
- They carry higher yields than ordinary debt.
- They are often unsecured debts.
- There is no amortization of loan principal.
- They may be structured with partially fixed and partially variable interest rates.

PROS

- Long-term "patient" debt
- Cheaper than raising equity
- Structural flexibility
- No dilutive effect on company's equity
- Lenders tend to b long-term

CONS

- High interest rates
- Debt is subordinated
- Can be hard and slow to arrange
- May include restrictions on further credit
- Owner must relinquish some control

In general, mezzanine loan financing and preferred equity are useful in various situations. Among these are:

- Recapitalization of an existing business
- Leveraged buyouts to provide financing to the purchasers
- Management buyouts, to allow the company's current management to buy out the current owners of the company
- Growth capital for significant capital expenditures or construction of facilities.
- Financing acquisitions
- Shareholder buyers, especially attractive to family-owned businesses trying to regain control of shares that may have fallen out of the family's hands to maintain or increase family control of the business.
- Refinancing of existing debt to pay it off or replace it.
- Balance sheet restructurings, especially by allowing time for mandatory repayments or no mandatory repayment at all.

Income:

- The term “income” generally refers to the amount of money, property, and other transfers of value received over a set period of time by individuals or entities as compensation for services, payment for products, returns on investments, pension distributions, gifts, and myriad other transfers of value.
- There is no single, standard definition of income; income is defined, and its amount determined, according to the context in which the concept is used.
- Taxable income is the result of determining the annual total or gross income of an individual or entity and reducing that amount by the exclusions, exemptions, and deductions allowed under the tax law.
- Financial regulators, businesses, and investors focus on businesses’ annual financial statements, which are prepared in accordance with generally accepted accounting principles (GAAP), and start by determining all revenue and then adjusting that amount by expenses and losses to determine a net income figure.

What is taxable income?

Taxable income is the total of all income from all sources and in any form—e.g., money and property, derived, adjusted to exclude tax-exempt amounts, and reduced by allowable deductions. It is the amount that is subject to income taxation.

Capital Gain: Gain and loss realized on the disposition of capital assets are treated as capital gain or loss. The tax rates on net capital gains realized with respect to assets held more than one year are 0%, 15%, and 20%. Capital assets include personal residences and investments such as real estate, stock, bonds, and other financial instruments.

Tax-exempt Income: Interest paid on certain bonds issued by governmental entities is treated as tax-exempt income. Interest paid on federal bonds and Treasury securities is exempt from state and local taxation.

Interest on bonds issued by state and local governments generally is not subject to federal taxation; municipal private activity bonds are not subject to the regular federal income tax, but they are subject to the federal alternative minimum tax. Some states and local governments also exempt interest on state and local bonds from taxation.

Expense:

- An expense is the cost of operations that a company incurs to generate revenue.
- Businesses can write off tax-deductible expenses on their income tax returns, provided that they meet the Internal Revenue Service (IRS) guidelines.
- Accountants record expenses through one of two accounting methods: cash basis or accrual basis.
- There are two main categories of business expenses in accounting: operating expenses and non-operating expenses.
- The Internal Revenue Service (IRS) has strict rules on which expenses businesses are allowed to claim as a deduction.
- One of the main goals of company management teams is to maximize profits.
- This is achieved by boosting revenues while keeping expenses in check. Slashing costs can help companies to make even more money from sales.
- However, if expenses are cut too much it could also have a detrimental effect. For example, paying less on advertising reduces costs but also lowers the company's visibility and ability to reach out to potential customers.

Two Types of Business Expenses

There are two main categories of business expenses in accounting:

- Operating expenses: Expenses related to the company's main activities, such as the cost of goods sold, administrative fees, and rent.
- Non-operating expenses: Expenses not directly related to the business' core operations. Common examples include interest charges and other costs associated with borrowing money.

Capital Expenses

Capital expenditures, commonly known as CapEx, are funds used by a company to acquire, upgrade, and maintain physical assets such as property, buildings, an industrial plant, technology, or equipment.

Forward Contracts vs. Futures Contracts:

- Forward and futures contracts involve the agreement between two parties to buy and sell an asset at a specified price by a certain date.
- A forward contract is an arrangement that is made over-the-counter (OTC) and settles just once at the end of the contract. Both parties involved in the agreement negotiate the exact terms of the contract. It is privately negotiated and comes with a degree of default risk since the counterparty is responsible for remitting payment.
- Futures contracts, on the other hand, are standardized contracts that trade on stock exchanges. As such, they are settled on a daily basis. These arrangements come with fixed maturity dates and uniform terms. There is very little risk with futures, as they guarantee payment on the agreed-upon date.
- There is no oversight with respect to forward contracts while futures are regulated by the Commodity Futures Trading Commission.
- There is more counterparty risk associated with forwards as opposed to futures, which are less risky as there is almost no chance for default.

What Advantages Do Futures Contracts Have Over Forward Contracts?

Details of futures contracts are made public because they are traded on exchanges, unlike forwards, which are negotiated privately between counterparties. Because futures are regulated, they come with less counterparty risk that forward contracts. These contracts are also standardized, which means, they come with a set terms and expiry date. Forwards, on the other hand, are customized to the needs of the parties involved.

What Are the Main Disadvantages of a Forward Contract?

There are several key disadvantages of a forward contract. For instance, their details are not made public as they are negotiated privately between the two parties involved and because they trade over-the-counter. As such, these derivatives aren't regulated and come with a greater degree of risk. Settlement isn't guaranteed until the contract's maturity date.

Bonds:

- Bonds are debt securities issued by corporations, governments, or other organizations and sold to investors.
- Backing for bonds is typically the payment ability of the issuer to generate revenue, although physical assets may also be used as collateral.
- Because corporate bonds are typically seen as riskier than government bonds, they usually have higher interest rates.
- Bonds have different features than stocks and their prices tend to be less correlated, making bonds a good diversifier for investment portfolios.
- Bonds also tend to pay regular and stable interest, making them well-suited for those on a fixed-income.
- For investors, the biggest risks are credit risk and interest rate risk. Since bonds are debts, if the issuer fails to pay back their debt, the bond can default.
- As a result, the riskier the issuer, the higher the interest rate will be demanded on the bond (and the greater the cost to the borrower).
- Also, since bonds vary in price opposite interest rates, if rates rise bond values fall.

Issuers of Bonds

There are four primary categories of bond issuers in the markets. However, you may also see foreign bonds issued by corporations and governments on some platforms.

- **Corporate bonds** are issued by companies. Companies issue bonds—rather than seek bank loans for debt financing in many cases—because bond markets offer more favorable terms and lower interest rates.
- **Municipal bonds** are issued by states and municipalities. Some municipal bonds offer tax-free coupon income for investors.
- **Government (sovereign) bonds** such as those issued by the U.S. Treasury. Bonds (T-bonds) issued by the Treasury with a year or less to maturity are called “Bills”; bonds issued with 1 to 10 years to maturity are called “notes”; and bonds issued with more than 10 years to maturity are called “bonds”. The entire category of bonds issued by a government treasury is often collectively referred to as "treasuries." Government bonds issued by national governments may be referred to as sovereign debt. Governments may also offer inflation-protected bonds (e.g. TIPS) as well as small denomination savings bonds for ordinary investors,
- **Agency bonds** are those issued by government-affiliated organizations such as Fannie Mae or Freddie Mac.

Derivative:
- Derivatives are financial contracts, set between two or more parties, that derive their value from an underlying asset, group of assets, or benchmark.
- A derivative can trade on an exchange or over-the-counter.
- Prices for derivatives derive from fluctuations in the underlying asset.
- Derivatives are usually leveraged instruments, which increases their potential risks and rewards.
- Common derivatives include futures contracts, forwards, options, and swaps.
- Traders use derivatives to access specific markets and trade different assets.
- The most common underlying assets for derivatives are stocks, bonds, commodities, currencies, interest rates, and market indexes.
- Contract values depend on changes in the prices of the underlying asset.
- Common examples of derivatives include futures contracts, options contracts, and credit default swaps.
- Beyond these, there is a vast quantity of derivative contracts tailored to meet the needs of a diverse range of counterparties.
- In fact, since many derivatives are traded over the counter (OTC), they can in principle be infinitely customized.

Pros
- Lock in prices
- Hedge against risk
- Can be leveraged
- Diversify portfolio

Cons
- Hard to value
- Subject to counterparty default (if OTC)
- Complex to understand
- Sensitive to supply and demand factors

Options:
- An options contract is similar to a futures contract in that it is an agreement between two parties to buy or sell an asset at a predetermined future date for a specific price.
- The key difference between options and futures is that with an option, the buyer is not obliged to exercise their agreement to buy or sell. It is an opportunity only, not an obligation, as futures are.
- As with futures, options may be used to hedge or speculate on the price of the underlying asset.

Dividend:

- A dividend is the distribution of corporate profits to eligible shareholders.
- Dividend payments and amounts are determined by a company's board of directors.
- Dividends are payments made by publicly listed companies to reward investors for putting their money into the venture.
- Announcements of dividend payouts are generally accompanied by a proportional increase or decrease in a company's stock price.
- Many companies do not pay dividends and instead retain earnings to be invested back into the company.
- The board of directors can choose to issue dividends over various time frames and with different payout rates.
- Dividends can be paid at a scheduled frequency, such as monthly, quarterly, or annually.
- For example, Walmart Inc. and Unilever make regular quarterly dividend payments.

Important Dividend Dates

Dividend payments follow a chronological order of events, and the associated dates are important to determining which shareholders qualify to receive the dividend payment.

- **Announcement date:** Dividends are announced by company management on the announcement date (or declaration date) and must be approved by the shareholders before they can be paid.
- **Ex-dividend date:** The date on which the dividend eligibility expires is called the ex-dividend date or simply the ex-date.
- **Record date:** The record date is the cutoff date, established by the company in order to determine which shareholders are eligible to receive a dividend or distribution.
- **Payment date:** The company issues the payment of the dividend on the payment date, which is when the money gets credited to investors' accounts.

Impact of Dividends on Share Price:

Because dividends are irreversible, their payments typically lead to money going out of the company’s books and business accounts forever. Therefore, dividend payments impact share price, which may rise on the announcement approximately by the amount of the dividend declared and then decline by a similar amount at the opening session of the ex-dividend date.

Why Are Dividends Important?
Though dividends can signal that a company has stable cash flow and is good at generating profits, they can also provide investors with recurring revenue. Dividend payouts may also help provide insight into a company's intrinsic value. Many countries also offer preferential tax treatment to dividends, where they are treated as tax-free income. In contrast, when investors sell stocks at a profit, they realize capital gains taxes, which may be as high as 20%.

Cash Dividend:
- A cash dividend is a payment made by a company to its stockholders in the form of periodic distributions of cash (as opposed to stock or any other form)
- Cash dividends are often paid on a regular basis, such as monthly or quarterly, but are sometimes one-time-only payouts, such as after a settlement.
- Most brokers offer a choice to accept or reinvest cash dividends.
- Dividend-paying companies are typically established, with stable cash flow, and beyond the growth stage.

Stock Dividend:
- A stock dividend is a dividend paid to shareholders in the form of additional shares in the company, rather than as cash.
- Stock dividends are not taxed until the shares granted are sold by their owner.
- Like stock splits, stock dividends dilute the share price, but as with cash dividends, they also do not affect the value of the company.