

University of Zurich

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Bachelor Thesis

New regulation: costs and benefits for Swiss private equity industry

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Executive Summary

This essay provides an analysis of the current regulatory changes in the private equity markets and studies its effects on the Swiss private equity industry, in particular its costs and benefits.

In the first place, I analyze the current financial markets situation. The recent financial crisis was an example of a global system collapse where all financial markets and investors suffered. To prevent any other potential crisis of this scope, the systemic risk has to be decreased and the lack of transparency eliminated. Therefore, new requirements for investment providers, including private equity investment providers, are being introduced. In this essay, I provide an overview of the four most discussed regulations that have recently been introduced and cover the private equity industry, namely the Dodd Frank Wall Street Reform, the Foreign Account Tax Compliance Act, the Alternative Investment Fund Managers Directive and the revision of the Swiss Collective Investment Schemes Act.

Afterwards, I analyze all cost types related to the implementation of new regulations and continue with a cost-benefit analysis. Unfortunately, the largest part of the analyzed costs and benefits cannot be quantified. Therefore, I analyze in detail the quantifiable part, the compliance costs. I project the potential compliance costs in a simplified example of a Swiss private equity fund manager and estimate its effect.

The compliance costs represent a substantial part of the fund managers' expenses and, as other overhead fund costs, will most probably be borne by the investors. Such higher costs will cause the decrease in the net investors' return. Due to that, the risk that some existing investors will no longer subscribe to private equity fund investments increases. Other potential effects of the new regulation are, inter alia, the risk of regulatory capture and the distortion of the competitive environment.

It is not easy to estimate the effects of the regulation from the present point of view. The largest part of the costs and risks is not quantifiable, as well as the potential benefits. In addition to that, the final costs for each private equity fund manager depend on the size of the manager's funds and on the efficiency of the compliance process. Nevertheless, this is a challenge for me to analyze the cost issue again in a few years retrospectively after fund managers will have already applied the new regulatory requirements and it is clear which of the potential effects that I analyze in this essay will have occurred.