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IS INITIAL PUBLIC OFFERING (IPO) BETTER THAN PRIVATE PLACEMENT FOR NEW FIRMS? A LITERATURE REVIEW.

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ABSTRACT

One of the most important decisions for new firms is the choice between an Initial Public Offering (IPO) and a private placement for the issuance of equity. While both methods allow for the raising of equity capital, there are significant differences in terms of issuance costs, ownership and control, disclosure requirements and other regulatory matters, investor base, market liquidity and long-term strategic consequences. This qualitative review synthesizes twenty core studies of empirical and theoretical work on the two methods, supplemented by a number of methodological and background references including Jensen and Meckling (1976), Kamal (2025), and Wood and Wright (2009). The evidence does not support a clear ranking of IPOs over private placements or vice versa in terms of superiority. Rather, the choice between the two methods depends on a number of factors including the firm's life-cycle stage, information asymmetry, required amount of capital, objectives of investors, market liquidity, and a number of other institutional factors and governance structures. Private placements are particularly suited for young, high uncertainty information-intensive firms that require the support of strategic investors. Older firms that are in need of larger amounts of capital that value liquidity and can sustain the reporting and other requirements of public markets are more likely to opt for an IPO. The review also identifies some of the key accounting and governance implications of the two methods. While IPOs increase the formal financial reporting and disclosure requirements of firms, private placements shift the information search of potential investors to negotiated situations with selected investors.

Keywords: *Initial Public Offering; Private Placement; Equity Financing; Cost of Capital; New Firms*

1.0 INTRODUCTION

In a global market, an increasing number of firms find themselves struggling to achieve their goals and survive in the early years of their development. Access to external financing is a major factor that affects a firm's survival, innovation and long-term success. New firms face severe financial constraints (Lafayette, 2003) . These include the limited history of their operations, uncertainty in their future cash flows and the lack of adequate collateral to secure loans. More critically, there is a severe information asymmetry problem between the firm's insiders and external investors (Lafayette, 2003; Martos-vila, 2011). This means that the firm faces severe financing constraints. For firms at the early stages of their development, the process of selecting the optimal financing mechanism is critical.

By definition, when a company seeks to raise external equity capital, it has two basic options to consider: issuing stocks and bonds as a publicly traded corporation (issuing initial public offerings or "IPOs") or issuing stocks and bonds as a privately held corporation (issuing a private placement of stocks and/or bonds) (Bharath & Dittmar, 2010; Martos-vila, 2011). While both types of issues represent means by which a company can raise funds on the basis of issuing equity (i.e., stocks) and/or debt (i.e., bonds) obligations, each has a number of distinct characteristics. Thus, there are some very fundamental differences that distinguish the management of a growing entrepreneurial company must consider when determining which of the two forms of issues are most appropriate for financing a company's growth (Fischer, 2000; Martos-vila, 2011; Wood & Wright, 2009).

The issuance of stock through an Initial Public Offering (IPO) is frequently considered a significant milestone in a company's growth and development (Ragozzino & Reuer, 2007). The ability of a company to go public and raise permanent capital on the public markets, pursue additional growth opportunities, gain exposure and a higher market rating are all perceived benefits (Lowry, Michaely, & Volkova, 2017). While there are several reasons that a company may choose to go public (Brau & Fawcett, 2006), the most frequently cited reasons include: 1) to raise capital to fund an acquisition; 2) to raise capital to improve future financing opportunities; 3) to utilise the public markets to receive a higher rating on the exchanges; and 4) to spread risk to a large number of investors while retaining control of the company. Finally, the cost of an IPO to the issuing company cannot be ignored (IPO underpricing). The direct and indirect costs of going public include underwriter's fees and other fees paid to participants in the issuance, as well as

accounting, legal and other advisor fees. Disclosure required of issuers of public companies can also be quite expensive. And, there is always the risk that the issuing company's stock will decline drastically in price after the company goes public.

On the other hand, the private placement of equity financing has become an extremely popular means of financing for entrepreneurs especially startup companies (Lafayette, 2003; Ning & Abdul Jalil, 2023). Until recently, there has been a perception that private placements of equity were primarily used by established firms to obtain funds at lower cost of capital than that available from public debt markets (Chinchwadkar & Seth, 2018). However, in recent years the private placement of equity has become an extremely popular means of financing for start-up companies (Fonseka, Colombage &Tian, 2014). Private placements offer a wide array of advantages over IPOs, including the ability to raise funds in a timely manner and to structure a financing to best meet the needs of a particular firm (Wang & Xu, 2014). In addition, according to Normazia, Ariff and Shamsher (2013), private placements present a wide array of advantages to small, unseasoned firms. Private placements of equity allow firms to raise capital without having to go through the time consuming and expensive process of completing an IPO (Janney & Folta , 2006). In a private placement, a firm issues stock to a small, select group of investors. These investors are usually very knowledgeable and experienced with the operations of firms similar to the one in which they are considering an investment (Barclay et al., 2006; Lafayette, 2003). Because the information required to be disclosed in a private placement is so minimal, private placements are able to avoid many of the informational asymmetry problems that are so prevalent in the IPO market Lafayette (2003). In private placements, firms are able to establish strategic relationships with experienced investors (Ning & Abdul Jalil ,2023). These relationships can provide a firm with access to a variety of resources, including financial, commercial, and technological (Brau & Fawcett, 2006; Lafayette, 2003). As noted by Lafayette (2003), private placements can have long term strategic benefits for a firm. Janney and Folta, (2006) note that firms with reputable private investors can receive certification benefits that increase the perception of the firm in the eyes of others. This perception is particularly important for young, unseasoned firms (Lafayette, 2003). Such firms benefit from any activities that increase the perception of the firm in the eyes of others, as they have limited resources to handle the costs of information asymmetry (Lafayette, 2003).

Although a great deal of research has been conducted into the IPO and the private placement market, considerable ambiguity exists with regard to the merits of each form of equity finance (Bharath & Dittmar, 2010; Fischer, 2000; Martos-vila, 2011; Wood & Wright, 2009) Many studies of IPOs note their benefits of greater liquidity, greater reputation, and growth opportunities (See for instance, Katti & Phani, 2016; Lowry et al., 2017; Ragozzino & Reuer, 2007; Ritter, 2011), while a host of others present evidence and arguments which demonstrate the advantages to a firm of financing through a private placement, including low cost of finance, reduced disclosure requirements, information asymmetry, lower financing frictions and a host of strategic advantages deriving from the financing relationship with a private place (Barclay et al., 2006; Brau & Fawcett, 2006; Chinchwadkar & Seth, 2018; Chuang, 2019; Fonseka et al., 2014; Janney & Folta, 2006; Lafayette, 2003; Ning & Abdul Jalil, 2023; Normazia et al., 2013; Wang & Xu, 2014). All in all, studies of the different types of equity finance have revealed that there are a number of factors which must be taken into account in an evaluation of a firm's finance decisions, including the objectives of finance, the environment in which a firm is doing business, the ownership structure of the firm, and the development stage through which the firm is currently passing (Fischer, 2000; Martos-vila, 2011; Wood & Wright, 2009) .

These various changes in the global capital markets environment have recently received increasing attention in the finance literature. A large body of evidence has documented the decline in IPO activity over the last several years (e.g., Lowry et al., 2017).Some of the studies of IPO activity (e.g., Brau & Fawcett, 2006; Hertzel et al., 2002; Li et al., 2015); identify a host of negative features associated with going public, including high underwriting spreads, heavy underwriting conflicts of interest, a complex and burdensome regulatory environment, and negative effects on corporate governance and on managerial incentives and behavior. These features suggest that, for many firms, remaining a private (or unlisted) company for a longer period of time may be the superior financing strategy (Barclay et al., 2006; Brau & Fawcett, 2006; Chinchwadkar & Seth, 2018; Chuang, 2019; Fonseka et al., 2014; Janney & Folta, 2006; Lafayette, 2003; Ning & Abdul Jalil, 2023; Normazia et al., 2013; Wang & Xu, 2014).

The central problem of this review is to find an answer to the question whether the Initial Public Offering (IPO) is a better financing strategy for young and newly established firms than a private placement of equity. There is a lot of empirical evidence from studies from all over the world that has been undertaken by researchers from various disciplines. However, the results have not been conclusive yet, in part, due to differences in countries, industries, as well as methodological approaches. Thus, the time is now right for a comprehensive review of the evidence.

The reviews primarily the empirical and theoretical studies published in academic and professional journals on the subject of IPOs and private placements as forms of equity finance for newly founded companies. The main

characteristics of both forms of equity finance are identified and analysed within a logical framework and their respective advantages and disadvantages are compared. The main studies on the subject are reviewed and the results presented to provide a comparative analysis of the two forms of finance. Consensus and conflict in the findings of the reviewed studies are highlighted and a conclusion reached as to whether or not new companies are better to list on a stock exchange by means of an IPO or to raise equity by means of private placements. The paper is presented within an accounting and governance-reporting conference and therefore special reference is made to the issues of financial reporting, disclosure, regulatory requirements and corporate governance-reporting for both forms of equity finance.

1.1 Research Questions

The following research questions were raised for the purpose of the study:

What distinguishes Initial Public Offerings from private placements as sources of equity financing?

Which theoretical perspectives best explain firms' financing decisions?

What does existing empirical evidence reveal regarding the relative advantages of IPOs and private placements?

Under what conditions does either financing mechanism become more advantageous for new firms?

2.0 METHODOLOGY

This study employed qualitative literature review. The review was based on existing empirical and theoretical studies on IPOs and private placements as new firms' equity financing options. The studies were analysed using thematic analysis and comparative analysis in order to highlight similarities and dissimilarities as well as conditions under which IPOs or private placements were more advantageous.

2.1 Evidence Base and Source Classification

The empirical evidence and theoretical work were obtained from twenty core sources, including the research on IPOs and private placements as well as their respective advantages and relative advantages, on information asymmetry, cost of capital, the speed of financing, ownership and control as well as on corporate governance, post-issue liquidity and growth of new firms, that is, Barclay et al. (2006), Bharath and Dittmar (2010), Brau and Fawcett (2006), Chinchwadkar and Seth (2018), Chuang (2019), Fischer (2000), Fonseka et al. (2014), Hertzel et al. (2002), Janney and Folta (2006), Jensen and Meckling (1976), Katti and Phani (2016), Lafayette (2003), Li et al. (2015), Lowry et al. (2017), Martos-Vila (2011), Ning and Abdul Jalil (2023), Normazia et al. (2013), Ragozzino and Reuer (2007), Ritter (2011), and Wang and Xu (2014). Jensen and Meckling (1976) are included in the twenty sources cited above because the two authors introduced the seminal work on agency problems as a function of ownership. The methodological supplementary source is Kamal (2025) and the background supplementary sources are Wood and Wright (2009).

2.2 Search and Selection Protocol

The reviewed literature in this study comprises studies from developed, emerging markets worldwide and consists of substantial empirical evidence from year 2000 onwards. The above-stated substantive inclusion criteria for potential studies were research on IPOs and private placements, equity financing, information asymmetry, cost of capital, speed of financing, among others, including the aspects of ownership, control, corporate governance, liquidity, growth of firms, and their strategic financing and subsequent life-cycle consequences.

The searches were conducted on some academic databases which also serve as scholarly repositories which are ScienceDirect, Google Scholar, SSRN, Wiley Online Library and ProQuest). The literature on management, corporate governance, finance, accounting, business and economics was retrieved from Google Scholar, SSRN and ProQuest, which in addition to providing access to high-impact and foundational finance and strategy journals, also enabled the backward and forward citation searches of seminal articles (Rock 1986; Jensen 1986; Wruck 1989). A range of search terms were employed, including combinations of terms denoting private placements and initial public offerings (IPOs) (private placement, private equity placement, private investment in public equity, IPO and initial public offering) together with terms denoting outcomes and explanations (underpricing, market discount, long-run performance, ownership concentration, and corporate life cycle). A second set of searches were also conducted to identify information asymmetry and governance related literature (investor identity, monitoring hypothesis, managerial entrenchment, tunneling, and family control), trading mechanisms and market friction literature (wall-

crossing, short interest, lending fee, resale restriction, financial flexibility, and illiquidity discount), and the mechanisms of and underwriting in IPOs (bookbuilding, gross spread, underwriter syndicate, lockup expiration, quiet period, and venture capital backing). In terms of the types of issue examined by the studies included in the review, all common types of common-stock offerings (including primary and secondary issues) were covered, namely private placement issues of standalone equity, private placement issues of private convertible debt and standalone IPOs, as well as issues of common-stock to non-public market institutional and strategic investors. Issues by financial institutions (banks, insurers, etc.), utilities, closed-end funds, unit trusts, royalty trusts, limited liability partnerships and other corporates in suspension were excluded from the review, as were market-switching issues without new capital, and issues affected by material confounding events within specified event windows (rights issues, debt restructurings, dividend announcements and mergers and acquisitions, for example).

2.3 Thematic and Comparative Analysis Procedure

The analysis of each core source was operationalised by summarising the objectives of the study, the theoretical underpinnings, the geographical setting, methodology, sample (or analysis units) and the main results of the study. The results were then coded into a number of recurring themes (e.g. cost of capital and pricing, information asymmetry and certification requirements, ownership and control, etc.). The themes across the studies were then compared within each category to determine whether there was agreement or disagreement as to which form of issue would be more advantageous under given circumstances. The synthesis was then organised within a contingency framework which analysed the results in respect of seven different criteria: life-cycle stage of the firm, information environment, required financing, characteristics of investors, and institutional environment.

2.4 Scope and Limitation of the Review

This is a qualitative review which does not undertake any meta-analysis or other form of pooled statistical estimation. Inevitable differences between studies (for example, in design, institutions, samples, outcomes) therefore preclude any direct numerical comparison. The absence of a copy of the database-searches conducted for the source-includes also limits the potential for reproduction of the source-selection process. That said, neither IPOs nor private placement appear to be universally superior.

3.0 DISCUSSION

3.1 Comparative Analysis of IPOs and Private Placements

Although the immediate cost of capital of an IPO and of a private placement of new shares can be compared easily, the two alternatives create a package of financial, ownership, information, governance, market liquidity and strategic consequences for the issuing company. The relative advantage of one alternative over the others is affected by the development stage of the company, its financial requirements, the information environment, the objective of existing owners and a number of other market-related factors. This paper compares the two main alternatives for new companies for five related aspects: the cost of capital and the stock price, ownership and control, information disclosure and protection of investors, speed, flexibility and market liquidity, and growth and reputation of the issuing company.

3.1.1 Cost of Capital and Pricing

One should note that when comparing the total financing costs of IPOs and private placements, one has to look beyond the cost of the initial transaction. In addition to the underwriting costs and other issuer and intermediary costs of IPOs, there are also disclosure and other compliance costs, as well as the value of any underwriting. There are also some issuance and disclosure costs of private placements that are reduced by having a negotiated transaction, however these costs are also transferred to the investors in the form of negotiated discounts and other valuation effects. The evidence on pricing effects and other aspects of financing value in announcements of private placements indicates that the value of financing in such transactions cannot be determined from a series of transaction costs. All of the costs and values of financing in IPOs and private placements has to be taking into consideration. Total economic cost and value of financing includes all of the transaction costs, pricing effects, issuer disclosure requirements, liquidity and other governance factors. As an example, Chuang (2019) examines the issuance and valuation effects of private placements and finds that several factors, including pricing and discounts, affect the financing value of such

transactions. In their study of emerging markets, Normazia et al. (2013) reported that there were very positive announcement-period share-price reactions, of about 2% to 3% in total, for private placements, indicating that much of the value of such financing is indeed reflected in the market price in the transaction's announcement period.

3.1.2 Ownership Dilution and Control

There are many major ownership and governance considerations involved in a company's decision to go public or to remain private. Founders of growth companies want to retain control of their company when they finance with venture capitalists and other investors. The founders desire to retain control is one of the main considerations that influence their financing decisions (Brau and Fawcett, 2006). However, when there is highly concentrated ownership by a small group of individuals and they are not externally monitored, then there is the potential for abuse. The addition of public shareholders in a going public transaction can dilute the ownership of a company's founders but they can still retain a large amount of voting power after an IPO (Fischer, 2000). Substantially all of the new shares that are issued in an IPO are distributed to the public and founders can retain a large percentage of their pre-issue shares. In addition, the founders can determine how the new shares that they issue will be allocated. Private placements can be used to raise capital on terms similar to those found in a going public transaction and founders can retain highly concentrated ownership by structuring a private placement with passive investors (e.g., institutions) and others (Barclay et al., 2006). However, there is also the potential for misuse by management in a private placement with passive investors.

3.1.3 Disclosure, Regulation and Investor Confidence

This aspect of financing is concerned with the disclosure and other regulatory requirements of accounting and governance. In terms of formal reporting, listing companies are required to produce on-going financial information. Furthermore, their activities are subject to a considerable amount of investor scrutiny, corporate governance and other rules and regulations. For newly formed companies, in particular, the costs of certain aspects of the accounting and reporting imposed on listed companies can be considerable and be a burden to management in terms of time to prepare reports etc. However, it is also important for young growing companies to provide assurance to investors in terms of transparency etc. that they are growing satisfactorily. Private placements result in less disclosure than a public offer and so less immediate reporting burden. However, it is normal for investors in a private placement to require considerable information on a company on a confidential basis and it will be for the management of the company to negotiate this information with each potential investor (Janney & Folta, 2006). Such information would not normally be made public and thus there is less transparency and less public price information than with a public offer of finance. Thus, public finance increases formal reporting and a number of other corporate governance issues. Private finance, on the other hand, shifts the information process to negotiated disclosure with investors.

3.1.4 Speed, Flexibility and Liquidity

A main constraint on private placement is that investors have less liquidity than they would in an IPO. While an IPO requires its authors more preparation and more formal procedures, a private placement can be negotiated and closed faster than an IPO (Martos-Vila, 2011). The relative value of public markets and private markets for a firm varies over the firm's life cycle (Bharath and Dittmar, 2010). While firms with immediate financing needs and higher information asymmetry value the speed and flexibility of a private placement, firms that need to constantly raise capital and issue securities on the market are better off with an IPO.

3.1.5. Growth, Reputation and Strategic Opportunities

Going public by listing a company on the stock exchange can support growth by increasing visibility and providing liquidity. By listing shares of a company that has already grown, they can be used for subsequent corporate development. Brau and Fawcett (2006) note that for example the reason for going public for many companies is acquisition financing and future financing opportunities. The characteristics of the IPO and the subsequent opportunities for acquisition for entrepreneurial firms have been studied by Ragozzino and Reuer (2007). In contrast, private placements can create even deeper relationships with individual investors. These investors may bring not only financial resources but also commercial, technological and management expertise (Janney & Folta, 2006; Lafayette, 2003). This type of relationship with investors in the capital market has its own characteristics that differ from those of public market relationships. There is a trade-off between the breadth and liquidity of public-market relationships, the depth and strategic-sensitivity of relationships with individual private investors.

3.1.6 Accounting, Financial Reporting and Governance Implications

These decisions also have significant implications for a young firm's accounting and governance practices. First, an IPO would expose a young firm to more formal financial reporting and disclosure requirements as well as investor relations and even governance reporting. Although these may impose additional costs and administrative burdens on young firms, they could enhance transparency, credibility, and external monitoring for the firm. In contrast, private placements would require less public disclosure, allowing for more negotiated information flow with investors. The extent of governance practices by private investors, however, would vary significantly between those who actively monitor and intervene in a firm and those who are mere passive holders, as has been highlighted by research including that of Barclay et al. (2006). Thus, a firm's decision with respect to financing must also consider its capacity to generate and report reliable financial information and to comply with appropriate disclosure requirements and sustain appropriate governance reporting over time.

Table 4.1 below provide the decision criterion and the relative advantages between IPO and Private Placement for new firms.

Table 4.1: The decision criterion and the relative advantages between IPO and Private Placement for new firms.

ion criterion	**te Placement**	**ive advantage for new fi**
al scale	tially large public investo limited investor pool	where very large expa l is required.
saction flexibility	r flexibility; formal proce r negotiated flexibility	e placement.
ıg risk	pricing and market-timin iated discounts/valuation	er universally superior.
dity	ly tradable shares	ly less liquid
ımation asymmetry	ed through disclosure e reduced through private cation but costly nce	placement for l tain firms.
der control	dilute control, but dilutio reserve concentration uctured	private placement, subj ıchment risk.
rnance	scrutiny and market discor-specific governance	xt dependent.
egic investors	investor base; pot elect investors with res sition currency lationships	e placement for stra ce needs.
tation	listing can enhance visib able private investors / quality	through different channel
-term financing	tial repeated public- nted private rounds possibl ;	fter sufficient scale/readin
ıp suitability	ive; strongest when m for early, unc nation-intensive firms	e placement at early stage
growth firm suitability	when scale and liq ility dominate	when strategic capita ds on growth stage.

Sources: Brau and Fawcett (2006); Fischer (2000); Janney and Folta (2006); Bharath and Dittmar (2010); Martos-Vila (2011); Normazia et al. (2013); Chuang (2019); Ragozzino and Reuer (2007); Barclay et al. (2006); Lafayette (2003).

3.2 Synthesis of Literature

The body of evidence on the use of initial public offerings (IPOs) and of private placements for the new equity of new firms comprises a diverse set of interrelated studies. In combination, these studies describe a complex of conditional relationships between information asymmetry, characteristics of investors and characteristics of new firms' owners; between the ownership structure, governance of new firms and market structure, between market structure, financial other regulatory institutions, and between these sets of variables and the development stage and financing objectives of new firms. Instead of providing a simple ranking of IPOs against private equity placements of new firms' equity, with the former always preferred to the latter, the twenty studies on this topic here synthesised need to be analysed for convergence as well as for divergence, for emerging structure as well as for unanswered questions. What do the studies taken together tell us about the use of IPOs as opposed to private placements by newly founded firms for their new equity? Where do they not agree? What are the unanswered questions that prevent a definitive ranking of these two forms of new equity financing?

3.2.1 Areas of Agreement About the use of IPO as Opposed to Private Placement

Many of the studies come to related but distinct conclusions regarding equity financing. First, there is the problem of information asymmetry. The study conducted by Lafayette (2003), note information problems, as do Janney and Folta (2006), Martos-Vila (2011), Katti and Phani (2016), and Ragozzino and Reuer (2007). The identity of investors affects corporate performance, Janney and Folta (2006) noted that experienced investors can bring value to firms while investor passivity affects corporate governance, as found by Barclay et al. (2006). The identity of the private equity investor can also affect subsequent exit strategies of firms, as Chinchwadkar and Seth (2018) found. Liquidity affects value of being a public company.

The two main modes of equity financing have related but distinct problems, with valuations of issues that are underpriced (as is well known with IPOs) frequently being overpriced. In the case of private placements, issues can be sold at discounts and then reverse later. The extent to which issues are under- or overpriced and the relation between initial equity market reactions and subsequent value creation by an issue are analysed in a number of studies including Katti and Phani (2016), Ritter (2011), Hertzel et al. (2002), and Chuang (2019). Their studies reach the same basic conclusion: an initial positive or negative reaction in the equity market of an issue is a very poor barometer of the issue's subsequent long-term value creation.

3.2.2 Areas of Disagreement

These results contrast with others which report negative long-run performance following the announcement of positive private placement activity. While Hertzel et al. (2002) reported positive announcements followed by poor long-run performance, Chuang (2019) found short-run gains followed by poor long-run performance for growth-oriented firms. However, other research has reported positive long-run performance following private placement activity by firms, including studies of emerging market firms, such as Normazia et al. (2013). Further, research on the announcement period stock price performance of certain regulatory filings has also reported mixed results, e.g. Fonseka et al. (2014) found that not all announcements have significant stock price effects.

There is also uncertainty with respect to the governance implications of private placements and IPOs. For instance, while information asymmetry is alleviated with sophisticated investors in private placements, there is the risk of management entrenchment (Barclay et al., 2006). On the other hand, IPOs are associated with ownership dilution; however, controlling shareholders can continue to exert considerable influence over the firm post-listing (Fischer, 2000). When viewed from the perspective of ownership structure and the respective classes of investors, apparent contradictions are resolved.

Similar trade-offs between costs and benefits have been noted for IPOs. While the costs of underpricing a stock and the fees paid to intermediaries in an IPO are well documented (Ritter, 2011), there are also a number of benefits that an acquisition seeking company can expect to derive from a going public process (Brau and Fawcett, 2006; Ragozzino and Reuer, 2007) that will make economic sense even if the issue process itself is expensive for the company.

3.2.3 Emerging Patterns

One of the emerging patterns is that companies with uncertainty about their future and companies with specialized assets tend to issue securities on a private placement basis. On the other hand, larger, more established companies with very large scale, growth, and investment needs are more likely to go public via an IPO (Janney and Folta 2006; Fischer 2000; Bharath and Dittmar 2010; Lowry et al. 2017).

Institutional dependence is a third pattern that is examined, including the impact of restrictions on the trading of listed companies, of capital market crises, and of other determinants of private placement activity in China and other emerging markets. The objective is to understand how the relative attractiveness of IPOs to private placement by companies depends on the quality of the capital market infrastructure in a country rather than on universal financial laws.

This strategic choice of financing a company has economic and strategic consequences that go far beyond the simple financial metrics of the transaction. The structure of financing a company in terms of partnerships and certification in a private placement versus the promise of liquidity, acquisition finance and market visibility in an IPO is one that needs to be examined in some detail.

3.2.4 Knowledge Gaps and Unresolved Debates

By far the gap in the literature is that, there are very few studies on IPOs compared to private placements of new young firms. Much of the evidence in the literatures refers to already established public firms are issuing private

placements. Some of the studies refer to listed firms choosing between an IPO and a private placement as an exit route for founders of firms. There is considerable review of the two separate literatures on IPOs and private-equity but little that allows direct comparison of the two methods of financing for start-up firms.

A major knowledge gap in the currently available research concerns the full measurement of the financing costs of companies. While in the finance literature the announcement returns and the underpricing of IPOs, as well as the level of discounts in issue of private placements are often used as indicators for the respective types of financing, these do not reflect the full spectrum of disclosure costs, the time of management, investor relations, impact on the corporate governance, the future financing needs, etc. of a company. Also, the many alternative opportunities of a company, such as the acquisition of other companies, are not reflected by these indicators.

Fourth, a major gap in existing research pertains to the financing needs of a firm at different stages of the firm's life cycle. Even though research (Chinchwadkar and Seth, 2018), (Bharath and Dittmar, 2010) and the IPO literature (Lowry et al., 2017) reviewed in this study discuss the financing status of a firm at start-up, growth and mature stages of the firm's life cycle, a comprehensive integrated model that would help in determining at what stage of the firm's life cycle it is advantageous for a firm to switch over from private financing to public equity financing is missing.

Future research should explore the goals of the founder(s) of a company as well as the characteristics of the investors (outside investors vs. founders of the company, strategic investors vs. public investors, etc.). Financing decisions are multi-objective decisions for founders of companies, investors and the company as a whole and thus cannot be reduced to a simple cost-minimization problem of the company's financing.

4.0 CONCLUSION

The literature does not provide an affirmative answer to the question whether IPOs or private placements are better for new firms. The study therefore provides a conditional answer. Private placements have several advantages for young, information-intensive and resource-constrained firms that need to involve patient and/or strategically connected investors. As is documented for a sample of young technology and biotechnology firms, experienced private investors can, for example, mitigate information hazards, certify the company, provide for additional resources and services that the founder of a start-up company needs. There are, however, also several disadvantages for founders of start-up companies of private placements of equity: illiquidity, stock being traded at a low price and the risk of entrenchment by investors.

An IPO is more advantageous for larger and more established companies who have adequate and credible information about their business to go public, need to raise a large amount of capital to fund growth, need to provide liquidity to the stockholders of the company, can benefit from increased exposure that being a public company can bring, or are looking to be acquired by another public company. The CFO motivations for going public, technology and biotechnology companies going public, the number of entrepreneurial firms that are acquired by public companies and the liquidity provided by public markets are examples that support this conclusion.

In conclusion, based on the conditions outlined above, financing superiority is not fixed and can be affected by various factors including the firm's life cycle, information asymmetry, capital required, desired investors, market liquidity, institutional environment and the firm's governance structure. New, highly uncertain firms are best raised for private placement first, because of the greater amount of information exchange involved and the strategic quality of investors. Subsequently, the endowed firm can go public through an IPO, to raise capital from a much larger pool of public market investors at higher values, and enjoy a host of other benefits, including those associated with public market status that can be utilized for subsequent acquisitions. Thus, there is no inherent reason why an IPO would be better than private placement for start-up companies; both can be used.

However, value can also be transferred through the pricing of a financing, and there are also governance implications of both IPOs and private placements that are not captured by the amount of value transferred to the firm through the financing. Therefore, rather than studying for example the value created by underwritten IPOs which achieve higher first-day returns than uncalled placements, the researcher should be studying the full economic value of a financing over the life cycle of new firms. Unfortunately, there is currently a lack of good quality research on this topic.

Reference classification for the main evidence base: Twenty references are used as the main evidence base for this review. The methodological reference, Kamal (2025), and the background reference, Wood and Wright (2009), are supplementary to the core evidence base.

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