

Private Equity Involves Public Market Risk

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The community of traders and investors focused on publicly-traded securities, from stocks to bonds to options, are now having to pay considerable attention to what is happening in private equity and private credit. This is not a new concept, given that the largest US companies make up only small part of the total economy, and that many large companies are increasingly opting not to go public and remain private. What has super-charged the role of private equity and credit as a potential driver of what happens with publicly-traded securities has been the revolution in artificial intelligence (AI) which has linked sectors of the economy in ways that were not as relevant in the past. As a result, the intersection of private and public markets has some very important risk management considerations both for short-term stock and options traders as well as longer-term asset managers of pension and endowment portfolios that often combine both private and public investments. Even if your portfolio or trading activity does not involve private equity, you now need to assess contagion risk.

Decline of publicly-traded companies in the US

By way of background, the number of US companies with a publicly-traded stock has been declining from the mid-1990s based on data compiled by the National Bureau of Economic Research (NBER, "The Shrinking Universe of Public Firms: Facts, Causes, and Consequences", by René M. Stulz, 2018). Back in the 1970s there were approximately 5000 US firms listed on stock exchanges. The peak in the mid-1990s was about 8000 firms. By 2016, the number of listed stocks was down to 3600 and declining. Research by Torsten Sløk at Apollo Global Management puts this development in perspective relative to the size of the US economy. If you are thinking about jobs, S&P500 firms contribute less than 20% of the employment in the US. These are big companies, so they still make up about half of the economy's corporate profits. It is no wonder why stock market indexes are not very good at forecasting the ups and downs in the economy as a whole. And it is also easy to see how risks in private equity could cascade into publicly-traded markets.

Enter the AI Revolution

The AI revolution is accelerating the influence of private companies on how securities trade in public markets. Every company is now a tech company whether they like it or not. Fear of missing out (FOMO) is a concern with many firms. Some firms had moved headlong into AI adoption, appreciating the possible advantages of being an early mover. Some early movers, though, have spent considerable funds and, so far, have seen minimal productivity and profitability improvements. It is a very fast-moving environment with winners and losers.

One key focus is the large data centers required by AI intensive tasks. Billions of investment dollars are flowing into the development of data centers. The risks with the development of data centers are only now being fully understood. The air conditioning (AC) failure at a CyrusOne data center in Aurora, Illinois shut down many global futures and options markets on Friday, November 28, 2025. This data center failure highlighted the risks involved with the tremendous electric power and AC infrastructure requirements of data centers. The data center outage also caused Goldman Sachs to delay a mortgage bond issue for CyrusOne. CyrusOne is privately held and is a top tier firm in data center world. But it also has financing needs partly involving public markets.

Other AI companies are highlighting different sets of risks for public markets. For example, several large publicly-traded companies are intimately involved with OpenAI, a highly-valued private equity owned company. The competition among AI platforms is heating up, and probably about to get a lot hotter. Alphabet (Google) knows that its dominance in search means it has no choice but to develop advanced AI tools. The Chinese have shown with DeepSeek that they can compete with lower development costs for large language models (LLMs). While OpenAI can certainly be credited with helping to ignite the AI revolution when it introduced ChatGPT back in November 2022, OpenAI now faces fierce competition from public companies with strong cash flow and deep pockets (Alphabet), as well as low cost Chinese competition, not to mention hundreds of start-ups developing specialized AI tools, such as Perplexity and Anthropic, just to name two of the many.

What does all this mean for public markets? As the AI narrative has shifted from “the AI rising tide lifts all boats in the sector” to “the promise of large profits and game-changer technology generates intense competition”, it can matter how AI-technology companies will see their stocks and options trade. Companies in OpenAI’s ecosystem, including some high-profile names such as Microsoft, Oracle, CoreWeave, have seen their stock price underperform others in the sector as the narrative shift occurred this past November. This underperformance is probably temporary, but it highlights the importance of appreciating the linkages between public and private companies.

Chip makers are seeing fortunes rise and fall, too, as competition comes to challenge the early leaders. Nvidia was the initial beneficiary of making AI-advanced chips. Now that Alphabet has announced its tensor chips, the competition is getting real. Alphabet's ecosystem includes companies such as Broadcom, Lumentum, and Celestica, not as well known, but still benefitting from Alphabet entering the chip and the AI tools competition.

And then there is the infrastructure element. Affordability is a political narrative, but electricity prices are critical to consumers (i.e., voters). To avoid depending on public utilities, Microsoft is partnering with NextEra to restart a nuclear plant to power a new (off-the-grid) data center. And back to the data center risk factors, Schneider Electric (SE) is a leader in data center air conditioning (FYI, SE was not part of the CyrusOne AC failure in November), and its stock has done very well in the AI revolution.

Private Equity: Lessons for Publicly-Traded Equity Risk Management

Appreciating the intersection of private and public markets is critical for the risk management of publicly-traded stock and options portfolios. What the digital and AI revolution has done is to tightly link the two sectors. A new product development by a public company can impact a private company, which can impact the public companies intertwined with it. We do not get timely or quality information about the profitability and cash flows of private companies. So, news stories, product announcements, and unfortunately challenges such as the data center episode, all can work to cause sharp movements in stock and options prices. Following the narratives and the changes in the narratives has become a critical element of the potential risk contagion between public and private entities.

And since the private equity market is relatively opaque, one may wish to use the fortunes of the companies that specialize in private equity as potential guideposts. That is, the stock performance of, say, Blackstone (BX) and KKR, which are publicly-traded may speak volumes for the health of the private equity business and help one understand if the risks from private equity to public stocks are rising or waning.

We also note that some of the large privately-held companies are issuing public-market debt. Debt can conceptually be considered a short put option on the assets of the issuing company. That is, the buyer of the debt receives a premium in the form of regular interest payments. But if the asset value declines and the company cannot pay the interest (i.e., options premium) then the company can go bankrupt and "put" the assets to the lender or buyer of the bond. We recommend monitoring the public debt of the larger private companies in the AI sector as a leading indicator should any problems develop.

The AI revolution is fast-paced and developing in unforeseen ways. For risk managers this increases the probability of sharp, abrupt price moves, as well as correlation shifts as the alignment of companies change with the shifting narratives.