PRIVATE EQUITY INVOLVEMENT AND PERFORMANCE OF BUY-OUT FIRMS: ENTREPRENEURIAL GROWTH VERSUS EFFICIENCY (SUMMARY)

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SUMMARY

PRIVATE EQUITY INVOLVEMENT AND PERFORMANCE OF BUY-OUT FIRMS:
ENTREPRENEURIAL GROWTH VERSUS EFFICIENCY

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Principal Topic

There is a vast academic literature that shows that company performance and value improves after a buy-out (BO). This is explained by the use of significant leverage, lower agency problems and tighter governance of private equity (PE) investors enhancing efficiency. Further, a renewed entrepreneurial climate spurs growth and innovation. This paper analyses the sources of value creation after the BO transaction and distinguishes between non-PE backed BOs, PE-backed BOs and investor-led BOs. We hypothesize that value creation is higher in PE-backed BOs compared to non-PE backed BOs, thanks to their tight governance and lower financial constraints. Tight governance leads to increased efficiency (leading to higher margins and more efficient use of assets), while lower financial constraints lead to higher growth in revenues.

Method

We identified 180 buy-outs in Belgium that took place between 1996 and 2003 using secondary data sources as Zephyr, CMBOR, press releases and press clippings. To the best of our knowledge, the sample is close to the population of Belgian buy-outs in that period. 50% of the BOs in the sample are PE-backed. Post-BO financial and employee variables were taken from the yearly annual accounts provided by the Belgian National Bank. Independent variables, including private equity firm characteristics, source of the BO and macro-economic variables, were gathered from the Zephyr database and from EVCA. Data were analysed using multivariate panel regression techniques.

Results and Implications

Consistent with results in other countries, we see that post-BO performance increases thanks to growth and efficiency increases. We find little differences between non-PE backed and PE-backed BOs, however. The major difference is that PE-backed BOs have lower growth in return on assets, due to lower growth in margins, than non-PE backed BOs. The impact of PE investors in BOs is hence limited.

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