PUBLIC VALUE:
A PRIMER ON PRIVATE EQUITY

2007

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INTRODUCTION

You can hardly open a newspaper today without learning of a major new corporate transaction involving private equity (PE). As private equity has become more prominent, as private equity funds and the size of the transactions they finance have grown larger and as the names of the companies they acquire have become more familiar, reasonable questions are being asked: What is private equity all about? How does it work? What does it mean for the American economy, for American workers and for American competitiveness? This paper is intended to address these and other relevant questions—and to ensure that any public policy debate about private equity is balanced and rooted in facts, not fears or provocative rhetoric.

Though few know it, private equity is an integral part of the everyday lives of millions of Americans. When you buy coffee in the morning at Dunkin' Donuts, you're interacting with private equity; when you see a movie produced by MGM Studios and buy a pizza at Domino's afterwards, you're interacting with private equity. When you shop at Toys R Us for the hottest new video game or the latest "must have" doll or when you buy a new outfit at J. Crew, you're touching private equity. When you purchase pet food and supplies for your dog or cat at Petco, that's private equity, too. And when you make online plane and hotel reservations for your vacation, you may be relying on private equity. Many of us work in office buildings owned by private equity companies, and drive cars and fly in airplanes that rely on parts and equipment made by private equity-owned firms. Even the power that lights our homes in some parts of the country is delivered by private equity-owned companies.

In short, private equity is an important and positive part of the American economy and, more importantly, plays a critical role in driving its growth. Private equity, directly or indirectly, makes a major contribution to the quality of life of tens of millions of Americans. (Exhibit 1) Consider:

- Over the last five years, businesses backed by private equity increased employment an average of nine percent per year, compared to one to two percent for public companies, according to a study by the British Venture Capital Association. A separate study by the European Venture Capital Association found that between 2000 and 2004, employment in private equity-backed companies rose by 5.4 percent, almost eight times higher than the European Union average of 0.7 percent. When the Financial Times studied the 30 largest European private equity transactions in 2003 – 04, it reported that "overall, jobs were more likely to have been gained than lost as a result of private equity-backed buys."

While similar data have not yet been developed in the United States, there is no reason to doubt that performance here mirrors that of PE companies in other developed countries.

- During the 25 years from 1980 to 2005, the top-quartile private equity firms generated annualized returns to investors of 39.1 percent (net of all fees and expenses). By contrast, the S&P 500 returned 12.3 percent a year during the same period. This suggests that $1,000 continuously invested in the top-quartile PE firms during this 25-year period would have created $3.8 million in value. The same amount invested in the public markets would have increased to $18,200. (Exhibit 2)

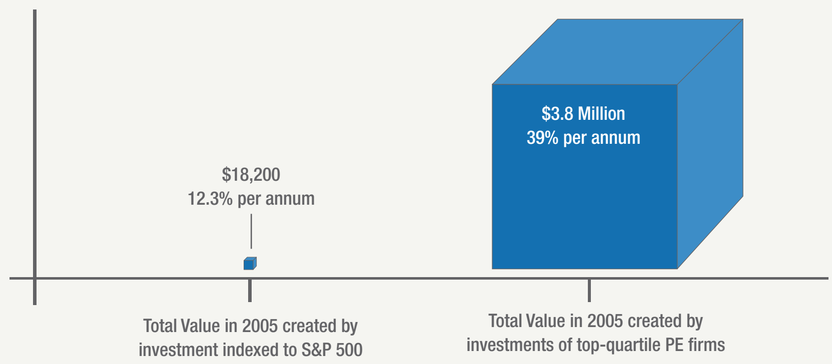
- Here is what these returns mean: Private Equity Intelligence reports that by 2006, the total net profits distributed to investors by private equity funds raised between 1991 and 2003 was $430 billion.

Private Equity is Woven into Our Everyday Lives

Exhibit 1

Leading Private Equity Firms Outperform Public Markets by a Wide Margin

Returned on $1,000 investment in 1980



Source: Venture Economics; Bloomberg

Exhibit 2

Top 20 US Public Pension Plans by Assets Under Management

Investor Name	No. of Members	AUM ($Millions)	PE allocation ($Millions)	PE allocation (%)	PE target allocation ($Millions)
California Public Employees' Retirement System (CalPERS)	1,500,000	230,300	21,625	9.4	13,818
California State Teachers' Retirement System*	795,000	158,000	10,371	6.5	18,960
New York State Common Retirement Fund	995,000	130,000	8,190	6.3	11,700
Florida State Board of Administration	240,000	123,000	3,379	3.0	6,150
New York City Retirement System	200,000	114,598	2,177	1.9	5,730
Teacher Retirement System of Texas	1,000,000	109,000	3,564	3.3	4,360
New York City Teachers' Retirement System	150,000	87,353	2,446	2.8	4,368
New York State Teachers' Retirement System	385,000	85,000	2,800	3.3	4,250
State of Wisconsin Investment Board	527,000	81,570	2,447	3.0	4,079
New Jersey State Investment Council	600,000	79,000	2,370	3.0	4,345
Washington State Investment Board	443,699	76,300	10,682	14.0	12,971
Regents of the University of California	n/a	71,000	3,550	5.0	8,875
Ohio Public Employees' Retirement System	670,000	67,582	607	0.9	2,703
Oregon State Treasury*	315,000	67,000	10,050	15.0	10,050
State Teachers' Retirement System of Ohio	446,500	65,500	3,657	5.6	1,965
Oregon Public Employees' Retirement Fund	300,000	60,000	5,400	9.0	7,200
Pennsylvania Public School Employees' Retirement System	410,000	57,168	5,431	9.5	6,300
Michigan Department of Treasury*	576,163	55,000	6,600	12.0	7,500
Virginia Retirement System	500,000	48,500	2,570	5.3	3,395
Minnesota State Board of Investment*	498,000	45,000	3,375	7.5	4,500
TOTAL	10.5 Million	$1.8 Trillion	$111 Billion	5.8 (average)	

*Membership numbers from fund website
Source: Private Equity Intelligence; 2007 LP Universe Survey

Exhibit 3

Who benefits from these returns? The big winners are public pension funds, university endowments, and leading foundations. Together, these funds represent the single largest group of investors in PE and collectively accounted for one-third of all capital allocated to private equity in 2006. In fact, the 20 largest public pension funds for which data is available (including the California Public Employees Retirement System, the California State Teachers Retirement System, the New York State Common Retirement Fund, and the Florida State Board of Administration) have some $111 billion invested in private equity, delivering strong investment returns to their 10.5 million beneficiaries. Add in corporate and some union pension plans and it becomes clear that private equity has gone to work on behalf of tens of millions of Americans. Of course, the private equity industry's executives also benefit from the returns generated by these investments. However, the perception that private equity is mainly about a handful of New York financiers doing very well at everyone else's expense is demonstrably misleading. (Exhibits 3 & 4)

Some suggest that private equity delivers its substantial returns mainly as a result of financial engineering and does little to create real-world value. In its early years, private equity firms could simply change a firm's capital structure and make considerable profits. But that is no longer the case. Winning private equity strategies must

Top 20 US Corporate Pension Plans* by Assets Under Management

Investor Name	No. of Members**	AUM ($Millions)	PE allocation ($Millions)	PE allocation (%)	PE target allocation ($Millions)
TIAA-CREF	3,000,000	406,000	7,000	1.72	n/a
AT&T Pension Fund		96,343	7,291	7.57	n/a
IBM Retirement Fund (USA)		73,885	5,098	6.9	n/a
General Electric Pension Trust	508,000	50,600	3,500	7.0	3,500
Boeing Company Pension Fund		43,484	2,175	5.0	2,175
Lucent Technologies Pension Fund		33,184	2,489	7.5	2,489
SBC Communications Pension Plan		28,100	3,542	12.6	n/a
Lockheed Martin Pension Plan		27,744	750	3.0	n/a
United Technologies Pension Fund		25,904	1,295	5.0	n/a
BellSouth Corporate Pension	60,000	24,972	2,997	12.0	n/a
Raytheon Company Pension Plan		24,381	213	1.0	n/a
Citigroup Pension Fund		21,956	966	4.4	n/a
DaimlerChrysler Master Retirement Trust	100,000	20,054	1,304	6.5	1,404
GTE Pension Plan		17,140	2,571	15.0	2,571
Hewlett Packard Company Pension Fund		13,500	945	7.0	n/a
Wells Fargo and Company Pension Plan		13,240	132	1.0	n/a
Bank of America Pension Fund	130,000	13,097	236	1.8	n/a
Northeast Utilities Pension Fund		12,569	58	3.0	156
World Bank Group Staff Retirement Plan	18,000	12,000	850	7.08	1,200
Alcoa Corporate Pension		11,927	441	3.7	n/a
TOTAL	3.8 Million	$970 Billion	$44 Billion	5.9 (average)	

*For which PE allocation data is available
**Where available
Source: Private Equity Intelligence; 2007 LP Universe Survey

Exhibit 4

differentiate themselves on the basis of *fundamental business improvements that often are more difficult to achieve by current managers working under the constraints of public ownership*. Because the managers of publicly-owned companies are forced to keep a close eye on quarterly earnings to maintain their company's stock price, they sometimes are hesitant to make the often substantial investments in new processes, personnel or equipment required to drive strong, long-term growth. Private equity firms, on the other hand, can take a longer-term view. Ultimately, the mangers of private equity firms understand that they must improve the underlying value of the companies they own over time to generate the returns their investors demand and to attract the capital they will want to raise for future funds. By better aligning the interests of owners and managers and by instituting a nimbler operating style that fosters greater innovation and long-term investment, private equity owners are leaders in spurring improved productivity and competitiveness.

And their impact goes beyond the firms they own and operate. Increasingly, public companies are adopting the techniques of private equity to increase shareholder value and build more competitive companies, suggesting that the private equity industry's impact on the future strength of the American economy is deeper than most imagine.

PRIVATE EQUITY'S MODEL OF CORPORATE GOVERNANCE

For over a century, *public equity*—stocks listed and traded on public stock exchanges—has been the single most important way to raise large amounts of capital and control the ownership and performance of large companies in capitalist economies. Early in this era, owners' interests were represented on the board by company founders who still owned large blocks of shares or by the financiers who raised the company's debt and equity.

Over time, however, the voice of the owner weakened. Important legislation to protect fund investors and pensioners scattered ownership more widely. For example, commercial banks were forbidden from using depositors' money to invest in risky stocks in 1933 (for understandable reasons). Similarly, investment funds in 1940 and pension funds in 1974 were required to spread their investments over many stocks. Owners with small percentage holdings in many stocks may have spread their risks—but they also had little incentive to participate on the boards of corporations to influence management and operating decisions. Mostly, they wanted the stock price to rise so they could attract more investors. Filling the vacuum, corporate CEOs assumed the role of representing both management and owners. Academics call this the era of managerial capitalism. Others, less charitable, think of it as the rule of Emperor CEOs. This disconnect between CEOs and shareholders sowed the seeds for the emergence of private equity as a business model based on aligning the interests of shareholders and management.

WHAT IS PRIVATE EQUITY?

Private equity may involve the acquisition of a private company with the intent of providing its founders the capital necessary to take its performance to the next level. It may involve the acquisition of a division of a large company, with the purpose of offering the newly-independent business the management focus and resources needed to achieve a new mission. Or it may involve "privatizing" a public company in an effort to undertake improvements that would be difficult to achieve given the short-term earnings focus of the public markets.

Most recently, public-to-private transactions have gained the most attention. These transactions offer a way of increasing the value of businesses by temporarily transferring ownership from millions of public shareholders to a much smaller number of private owners. Without the pressures from outside shareholders looking for short-term gains, owners and managers can focus in a laser-like way on what is required to improve the medium to long-term performance of the company. This structure makes it far easier to align the interests of owners with those of managers, who also have a direct stake in the success of the company.

Private equity firms seek out companies in which they believe they can unlock significant value—by changing the business strategy, investing new capital or injecting new managerial talent. Any one of these steps, when taken by a publicly-traded company, could cause earnings to dip and trigger shareholder dissatisfaction, stock sell-offs and a drop in enterprise value. The private equity ownership structure eliminates these concerns and fosters a climate in which companies can do what is necessary to promote increased growth and profitability over the long run. Regardless of whether the company acquired is public or not, the ability to align the interests of owners and managers has proven to be an extremely effective governance model, which results in building strong businesses over the long term.

One study offers compelling evidence that private equity ownership creates stronger, more competitive, healthier businesses. Professor Josh Lerner of the Harvard Business School and Professor Jerry Cao of Boston University reported that—based on analysis of 496 acquisitions between 1980 and 2002—companies that went public again *after* being acquired by private equity firms and operated by them for more than a year consistently outperformed the market and other IPOs.

Private equity often is confused with hedge funds. But the two forms of investment differ in some key ways. Private equity funds invest in companies with the intent of owning and operating them for several years or more. Private equity firms typically create value by improving the operations, governance, capital structure, and strategic position of the companies in which they invest. The goal is to grow them, turn them around, and otherwise strengthen their performance. By contrast, hedge funds are a loosely-defined category of investment pools that, like a retail mutual fund, principally invest in publicly-traded securities, currencies or commodities. While most mutual funds typically own "long" positions in securities, that is, they actually own the security with the hope it will rise in value, a hedge fund may take "short" positions (betting on a company's stock price to fall), and engage in many more complex trading strategies, including futures trading, swaps and sophisticated derivative contracts.

A recent example illustrates how private equity works in the real world. When Bain Capital, Thomas H. Lee Partners and the Carlyle Group bought Dunkin' Brands (Dunkin' Donuts and Baskin-Robbins ice cream shops) in 2006, they didn't just take control of a popular breakfast and dessert business. By buying this company from a larger and more diversified parent, they brought performance focus and attention to a relatively neglected asset in a larger family of companies. Many private equity acquisitions involve carve-outs of this sort, aimed at maximizing the value of an overlooked asset. The PE firms' strategy, now being executed, is to pour talent and capital into the business to expand Dunkin' Donuts west of the Mississippi and to relocate many Baskin-Robbins stores to areas that are more likely to be visited by customers who want to buy ice cream. This change in strategy requires significant expenditures that reduce short-term earnings.

If the company were still part of a publicly-traded entity, a decline in quarterly earnings would likely have hurt the stock price and, therefore, investors. But under private equity ownership, investing in long-term growth is an attractive option. The private equity investment gives management a reprieve from quarterly earnings pressure, enabling it to do the right thing for the business. It also provides the resources to ensure success. Over time, Dunkin' Brands expects to create 250,000 new jobs—jobs with good career paths in restaurant management as new stores are opened across the western United States and sales at the company's ice cream shops rise. Its success also is creating a new class of small business entrepreneurs who find owning multiple Dunkin' Donut franchises a way to achieve personal financial security and success.

Jon Luther, CEO of Dunkin' Brands recently told the U.S. House of Representatives Financial Services Committee, "The benefits of our new ownership to our company have been enormous. Their financial expertise led to a ground-breaking securitization deal that resulted in very favorable financing at favorable interest rates. This has enabled us to make significant investments in our infrastructure and our growth initiatives…They have opened the door to opportunities that were previously beyond our reach."

HOW DOES PRIVATE EQUITY WORK?

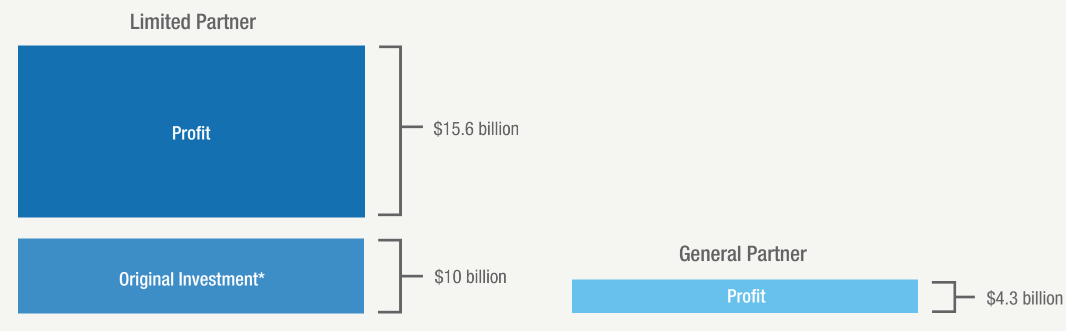
At its core, private equity is simple: PE firms establish funds that raise capital (the year in which the money is raised is called the vintage year of the fund) from investors—who are referred to as limited partners, or LPs. The private equity firms—known as general partners, or GPs—invest this capital on behalf of their investors, along with funds borrowed from banks and other lenders. The general partners buy companies that they believe could achieve significantly greater growth and profitability with the right infusion of talent and capital. Their approach is to put in place strategies and management teams to improve the company's performance.

Private equity GPs typically hold companies for three to five years, and then sell them, hoping to realize a gain on the sale as a result of the increased value they have created during their period of ownership. The size of the capital gain directly relates to the increase in value the PE firm has created. The concept is comparable to buying a house that needs repairs, an extra bedroom, a garage or updated kitchen, making the improvements and then selling the house for more than the original price plus the cost of the investment. There always is a risk that the real estate market will go sour, or that construction will be more costly than anticipated. Of course, transforming companies is considerably more complex: new products have to be developed and launched, new markets have to be entered and new capabilities have to be built. Often the business plan of the acquired company looks nothing like the business plan of the pre-acquisition entity. But the goal is the same in a private equity fund or a home renovation: increase the value of the underlying asset for the investors and sell for a capital gain.

Most PE firms are private partnerships. They typically charge an annual management fee to the limited partners that ranges from one to two percent of the assets investors commit to a fund. The management fee finances the day to day operations of the PE firm, including employee salaries and office rent. The typical management fee has been falling from two to 1.4 percent recently, as fund sizes have grown and as PE has become more competitive. Appropriately, investors want PE firms to be more dependent on generating returns than on fees.

When private equity funds sell investments for a profit, limited partner investors reap the overwhelming majority of the gains. The PE firm cannot take any profit until it first

Returns to Investors from Private Equity



Returns from $10 billion fund assuming return at 20% per year over a 6 year period

*Including GP investment

Exhibit 5

returns to investors the capital they invested offset by the losses on any bad investments—plus the first eight to nine percent (a contractually agreed-to "hurdle" rate) on the total invested capital, along with any fees paid by the investor. If any proceeds remain after the hurdle is cleared, they are split so that the investors usually receive 80 percent and the general partner receives 20 percent of net overall fund profits. (GPs and LPs can and do sometimes agree to splits other than this 80/20 standard in negotiating partnership agreements but the 80/20 split is typical.)

The 20 percent is referred to as the general partner's "carried interest" or "carry." It is subject to a "clawback" provision that requires the PE firm to return distributions to the extent of any subsequent losses in other investments of the fund, so that the GP never ends up with more than 20 percent of all value created and fees paid. If the PE firm generates losses on some investments, it shares in the downside because its carry from other successful investments is offset by the deals gone sour. If enough deals in a fund do poorly, the GP could be left with no carry at all, making carried interest both a risk-sharing mechanism and an incentive mechanism to deliver returns for investors. The 20 percent carry, then, is the PE firm's main reward for finding the right company, becoming its "sole proprietor," fixing it and reselling it, and for doing all these things well. The other 80 percent goes to the fund's limited partners investors. (Exhibit 5)

Capital Commitments to Private Equity by Source

Percent of capital invested in PE by LP type

	2005*	2006**
Public Pension Funds	22	26.6
Corporate Pension Funds	10	12.3
Union Pension Funds	1	1.4
Banks & Financial Services	6	9.8
Insurance Cos.	12	7.5
Endowments/Foundations	10	7.7
Family Offices	11	6.8
Wealthy Individuals	10	10.1
Funds of Funds	13	13.9
Other	5	3.9
Total	100	100

*Sample size: over global 75 funds with total capital of over $32 billion
**Sample size: over global 110 funds with total capital of over $44 billion
Source: The PE Analyst 2006 Sources of Capital Survey presented in *PE Analyst*, April 2007

Exhibit 6

Who invests in private equity funds? Companies investing employee retirement savings in private equity include such household names as General Motors, General Electric and Boeing. Public and private universities, ranging from the University of California to Rice University, do the same. Public pension funds—the Washington State Investment Board and the Los Angeles County Employees Retirement Association are two—also are pursuing private equity investment opportunities. Ever since legendary investor David Swensen, who manages Yale University's endowment, made outsized returns for his alma mater by investing significantly in private equity, other institutions have followed suit. (Exhibit 6)

According to the Russell Survey on Alternative Investing, on average, public pensions commit seven to eight percent of their assets under management to private equity investments, corporate pensions commit six to seven percent and university endowments commit nine to ten percent. This does not include for-profit asset managers, whose allocations to private equity also have been growing rapidly.

PRIVATE EQUITY PERFORMANCE: SUPERIOR RETURNS

Why have thoughtful and serious investors charged with assuring the long-term well-being of millions of pensioners and preserving the destiny of the nation's leading cultural and academic institutions chosen to allocate a portion of their assets to private equity? In a word, the answer is "returns." Data from Venture Economics and Bloomberg show that between 1980 and 2005, top-quartile private equity firms, on average, delivered 39.1 percent annualized returns, significantly beating the S&P 500 and other public market indices. Those superior returns helped strengthen several major public pension funds and defined benefit programs. Importantly, these are net returns, *after* all fees, expenses and the GP's carry.

Although the industry is evolving rapidly, the group of high-performing firms that makes up the top-quartile is relatively stable and very well-known. At the same time, the spread between the top performers and the rest is much wider for private equity than for other asset classes. For this reason, capital has continued to flow into these firms and the best ones have been able to raise larger funds, which, in turn, enable them to acquire larger companies than in the past. Five years ago, a $6 billion fund would have been among the largest around. Today, the top firms routinely raise more than that. These firms include Apax Partners, Apollo Management, Bain Capital, the Blackstone Group, the Carlyle Group, Hellman & Friedman, Kohlberg Kravis Roberts (KKR), Providence Equity Partners, Silver Lake Partners, Thomas H. Lee Partners and TPG Capital (formerly known as Texas Pacific Group). Together these 11 firms, and a handful of others, rapidly are emerging as the industry's winners, delivering superior returns while deploying half or more of all private equity capital invested in the last five to seven years.

PRIVATE EQUITY VALUE CREATION

One common misperception about private equity firms is that they increase value through financial engineering rather than by rolling up their sleeves to improve the operations of the businesses they acquire as "active owners." Perhaps 20 years ago, simple "financial engineering" (borrowing heavily against a company's stable income) may have been sufficient to generate adequate private equity returns. But it is no longer enough. Recent data from SDC, Factiva and Auction Block show that there are, on average, more than four bidders for each transaction valued between $1.5 and $2.5 billion and more than five bidders for larger ones. These "auctions" between multiple buyers are now the way in which 80 percent of all companies valued at more than $500 million are bought and sold. In this new and intensely competitive environment, the use of efficient capital structures is still important. However, whatever upside there may be in financial engineering is fully known and fully priced into every player's initial bid. In other words, a strategy of simply adding more debt to an "underleveraged" balance sheet—which once might have allowed PE firms to realize substantial gains from a company with only modest performance improvements—no longer works. This is analogous to the value of a good school district being well-known and already priced into the home values in a neighborhood.

To succeed today, a PE firm needs to bring much more to the table than financial creativity. It must be an active owner. The PE firm must add new capabilities to the company it buys (by adding new products), increase competitiveness (by reducing waste and improving operations) and grow revenues (by entering new markets or finding new customers) to make any money for itself or its investors. And it needs to develop, implement and successfully execute a compelling business strategy.

An analysis of more than 60 transactions from primary data collected from 11 PE firms in the U.S. and Europe showed that overall fund performance is disproportionately driven by the very best and the very worst transactions in each fund. For these outlier transactions, company performance is the main factor driving returns. In the very best transactions (with annualized returns greater than 60 percent), 70 percent of the value created came from improving company performance. In the transactions that did not produce significant returns, the failure was caused by the general partner's inability to make fundamental improvements to the company's operations.

The best private equity firms today bring much more to the table than just capital. They deliver deep expertise in the sector in which the investment is being made; a performance culture that rewards entrepreneurialism and results; managerial and functional capabilities (IT, for example); and an ownership structure that allows even the toughest decisions to be made quickly. A few anecdotes illustrate the "active ownership" model increasingly common in leading private equity firms:

- **Deep expertise:** The best public equity firms spend years developing powerful networks of experts that they can draw on to complement the management teams of the companies they acquire. These experts are typically former CEOs or CFOs, consultants, or deep subject matter experts (experts on new manufacturing techniques, for example). Often they come from inside the acquired company's industry and may include some of the most noteworthy names in the business. Lou Gerstner, the legendary CEO of IBM, for example, is now Chairman of the Carlyle Group, and John Bond, former Chairman of global banking giant, HSBC, now advises KKR. Leonard Schaffer, former CEO of the leading health insurer WellPoint, is committed to helping TPG identify and assess new healthcare opportunities.

- **Performance culture that rewards entrepreneurialism:** When Bain Capital, KKR and others acquired the troubled toy retailer Toys R Us, they hired former Target Vice Chairman Gerald Storch as CEO, along with former executives from Sears, Best Buy, Mervyn's and Atari. The management team and its advisors decided that the best way to aggressively grow sales was to make Toys R Us much more "mom-friendly." Similarly, the private equity acquisition of SunGard, a major software development and vendor, relieved near-term earnings pressure and allowed the company to dramatically increase its R&D investment, according to SunGard CEO Cristobal Conde. The company plans to complete 53 new research projects in 2007 (up from about 10 annually pre-PE acquisition). Conde says the company's common services architecture program is thriving under new ownership: it covers 60 SunGard products (compared to four before the private equity acquisition). In addition, the company now trains about 800 programmers a year, up from 50 prior to the buyout. The program aims to streamline software development and distribution and, according to Mary Knox of research firm Gartner Inc., could reduce the cost of rolling out products and make it easier to integrate SunGard software with other vendors' products.

- **Managerial and functional capabilities:** Bain Capital drew on its Domino's Pizza management team's expertise in the quick-service restaurant segment to help evaluate and later manage the investment it made in Burger King. Leading PE firms increasingly have standing relationships with experts who are deeply versed in topics that range from information technology systems to human resources. They call on these experts to drive everything from implementing complex equipment upgrades that enhance efficiency to designing compensation packages that align incentives and maximize collaborative performance.
- **Nimble ownership structure:** The PE firm and the company CEO form a tightly-knit group that can agree quickly and move decisively. Control is far more dispersed in public companies, and the ability of a diverse group of shareholders to monitor management is far weaker than in a private setting.

Private equity firms tie a far greater share of senior manager compensation to company performance than public companies. Often, the top team in a private equity-controlled company will own two to eight percent of the company, creating real incentive alignment and a passionate commitment to performance.

At the same time, patience for under-performing managers is limited. PE firms often replace members of top management to ensure the right mix of skills and a high level of performance. Surveys of recent deals show that some or all of the senior management team is changed in around 70 percent of all PE transactions, a higher number than many realize. PE ownership can be lucrative for management, but only if that management team creates value for the owners of the business.

CONCLUSION

Private equity has proven itself to be a powerful engine for creating economic value for investors, for retirees, for many workers, and for institutional investors—including universities and foundations that are better able to meet their educational and charitable objectives as a result of their private equity investments. Moreover, the role PE firms play in improving performance of companies of all kinds in all sectors increases productivity and competitiveness.

Finally, private equity represents an important governance innovation that is value-added in its own right and—because it offers public capital markets real competition for the first time—may improve performance even in companies in which it is not an owner.

Private equity is not to be feared. It does need to be better understood. We hope this paper advances this important objective.

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