Press Release **London, Nice, Singapore, January 17, 2011**

Ground-breaking research shows that large private equity firms underperform small firms

Newly-released research by Florencio Lopez-de-Silanes of EDHEC Business School with co-authors Ludovic Phalippou and Oliver Gottschalg, entitled "**Giants at the Gate: On the Cross-Section of Private Equity Investment Returns**," examines the determinants of private equity (PE) returns using a newly constructed database of 7,500 investments worldwide over forty years. The dataset is, to the best of the authors' knowledge, the largest panel of worldwide PE (buyout) investment performance.

Among the many key and previously undocumented findings of the study:

* **The scale of private equity firms is a significant and consistent driver of returns.** Diseconomies of scale are linked to firm structure: independent firms, less hierarchical firms, and those with managers of similar professional backgrounds exhibit smaller diseconomies of scale. More globally, **small investments outperform large ones**.
* The evidence is consistent with the view that PE performance suffers from structural features of the firm that curtail information flows and reduce the value-added capacity of management in more hierarchical firms and those in which communication is more difficult. In short, **as the PE firm scales up, its larger communication costs outweigh the benefits of its higher knowledge utilisation rate**.
* **Investments held at times of a high number of simultaneous investments underperform substantially.** The number of simultaneous investments over the life of the deal is a better predictor of negative returns than are other proxies.
* The authors are the first to document **substantial underperformance of investments in emerging countries**, which is of interest given their recent spectacular growth. Investments in developing countries exhibit poorer performance across all measures, with the exception of bankruptcy rate.
* The data also shows for the first time that **most PE investments around the world are small equity-wise**. The median equity investment is a mere $10 million. The multi-billion-dollar deals covered in the press are in fact a small minority: only 10% of the investments in the sample involve more than $100 million of equity.
* The median investment IRR (internal rate of return) is 21%, gross of fees. One in ten investments goes bankrupt, whereas one in four has an IRR above 50%.
* There is a **strong negative association between performance and duration**. A large proportion of high-return deals are quick flips (investments held less than two years) and quick flips are cyclical. Accounting for 12% of all PE investments, quick flips have median IRR of 85%, whereas investments held more than 6 years, which account for nearly 18% of all PE investments, have a median IRR of only 8%.
* IPO-exited investments have higher returns than the rest. Yet investments exited through a sale (a trade sale or secondary buyout) or recapitalisation, refinancing, or other methods also perform well.
* The notion that PE focuses heavily on cash-rich industries is not borne out by the data.

Contact:

For further information or to receive a copy of the study, please contact **Séverine Anjubault**:

Tel.: **+33 (0)4 93 18 78 63** – E-mail: **severine.anjubault@edhec-risk.com**

About EDHEC-Risk Institute

EDHEC-Risk Institute is part of EDHEC Business School, one of Europe's leading business schools and a member of the select group of academic institutions worldwide to have earned the triple crown of international accreditations (AACSB, EQUIS, Association of MBAs). Established in 2001, EDHEC-Risk Institute has become the premier European centre for financial research and its applications to the industry. In partnership with large financial institutions, its team of 56 permanent professors, engineers and support staff implements six research programmes and eleven research chairs focusing on asset allocation and risk management in the traditional and alternative investment universes. The results of the research programmes and chairs are disseminated through the three EDHEC-Risk Institute locations in London, Nice and Singapore.

EDHEC-Risk Institute validates the academic quality of its output through publications in leading scholarly journals, implements a multifaceted communications policy to inform investors and asset managers on state-of-the-art concepts and techniques, and forms business partnerships to launch innovative products. Its executive education arm helps professionals to upgrade their skills with advanced risk and investment management seminars and degree courses, including the EDHEC-Risk Institute PhD in Finance.

www.edhec-risk.com