Driving the Shakeout in Private Equity

The Role of Investors in the Industry's Renaissance

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July 2009

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In our previous White Paper on private equity, we predicted that the financial and economic crisis would trigger a major shakeout in the private-equity industry, with 20 to 40 percent of the 100 largest leveraged-buyout (LBO) private-equity firms going out of business.[1] This prognosis was based on an analysis of the interplay of four key factors, including private-equity firms' refunding schedules, long-term performance, recent deal activity, and exposure to crisis-prone industries. Ultimately, who will win and who will lose is in the hands of so-called limited partners—that is, the investors in private-equity firms, such as pension funds, funds of funds, banks, and sovereign wealth funds.

Our new research leads us to conclude that there is more available capital—also known as *dry powder*—than ever before and that limited partners will stay committed to private equity.[2] But the shakeout of the private-equity firms will continue, driven by a shift of power toward limited partners.[3]

In addition, some limited partners will not be able to fund their commitments, and if they are anchor investors, this will increase the likelihood of taking their private-equity firms down.

This paper addresses three main questions:

- Will limited partners be able to deliver the dry powder needed to sustain private-equity deal activity?
- How will the liquidity pressures on different types of limited partners affect individual private-equity firms?
- What impact will the liquidity pressure on limited partners have on the shakeout of the private-equity industry and how the industry operates?

To answer these questions, we created a proprietary database of more than 3,000 commitments by limited partners to private equity. This database draws from publicly available data on limited partners and private-equity funds, as well as from commercial databases—including Preqin's Investor Intelligence, Thomson Financial, Dow Jones's Directory of Alternative Investment Programs, and Dealogic. In addition, we conducted in-depth interviews with more than 30 limited partners and private-equity firms in the United States and Europe.

Investors Have Committed Record Levels of Dry Powder to Private Equity

Our research indicates that limited partners currently have undrawn commitments of $550 billion to LBO private-equity firms, compared with $460 billion at the end of 2007 and $380 billion at the end of 2006. But how much of this money will investors deliver when these firms make their capital calls? More critically, how will any shortfall in commitments affect these firms' ability to realize their strategy?

Few limited partners will abandon or scale down their capital commitments. In the wake of the financial and economic crisis, many limited partners have suffered a 30 to 40 percent drop in their net asset values, and, in addition, some of them now face severe liquidity constraints. "Should we

1. See *Get Ready for the Private-Equity Shakeout: Will This Be the Next Shock to the Global Economy?*, BCG and IESE White Paper, December 2008.

2. Dry powder is the capital committed by investors into private-equity funds minus both the capital invested by the firm managing the fund and the capital investors will not be able to provide: the truly undrawn commitment.

3. Throughout this paper, the phrase "private-equity firm(s)" refers exclusively to LBO private-equity firm(s).

honor our commitments to private-equity firms or walk away?" asked the managing director of a U.S. pension fund.

Our research suggests that relatively few limited partners will abandon or scale down their commitments. We estimate that, on average, limited partners will negotiate to reduce their LBO commitments by 5 to 15 percent, leaving private-equity firms as a whole with around $500 billion of dry powder. This conclusion is based on an analysis of the likelihood of limited partners' choosing one of the three main options available to them: defaulting on capital calls, selling commitments in the secondary market, and renegotiating their total commitment levels.

Few defaults on capital calls are expected. Historically, there have been very few cases of defaults on capital calls from private-equity firms, and we do not expect this situation to change. The long-term risk to an investor of defaulting on its commitments is so high that a cash-constrained limited partner would rather sell its commitments in the secondary market—even at a loss—than suffer damage to its credibility.

Many commitments of distressed limited partners are likely to change hands in the secondary market. These transactions will have no impact on the dry powder that is available to private-equity firms. "I believe that commitments will mainly be transferred among limited partners in the secondary market rather than be reduced," said the chief investment officer of a U.S. private-equity fund of funds. The fund manager of a U.S. public pension fund noted, "The secondary market will alleviate a lot of limited partners' stress." These sales present attractive opportunities for limited partners with sufficient liquidity to buy.

In fact, there is already a strong trend toward secondary market sales. Partners Group estimates that the volume of private-equity fund interests sold in the secondary market more than doubled from 2006 through 2008—from $20 billion to $50 billion.[4] There are two main reasons for this increase. Although sellers were previously driven by portfolio-management considerations, the financial and economic crisis has led to a surge of liquidity-thirsty sellers. Until the first quarter of 2009, declining values of publicly listed investments relative to the value of private-equity commitments also created an asset-allocation imbalance in limited partners' portfolios, forcing them to sell commitments to redress the balance—the so-called denominator effect. With the recent uptake of equity markets and the lagging reevaluation of private-equity investments, the denominator effect has lost its force.

Some downward renegotiation of commitments is anticipated. Some limited partners—typically the anchor investor or a group of influential investors—will renegotiate commitments downward with their private-equity firms. We have already seen this in Europe and in the United States, and it is likely to continue. This is especially true for those private-equity firms expected to invest in megadeals (historically greater than $5 billion in transaction value), which hold dry powder of approximately $150 billion to $200 billion (30 to 40 percent of total dry powder).[5] These private-equity firms may also attempt to renegotiate their terms with their limited partners in order to enable them to reallocate some of the capital to smaller deals or to other asset classes.

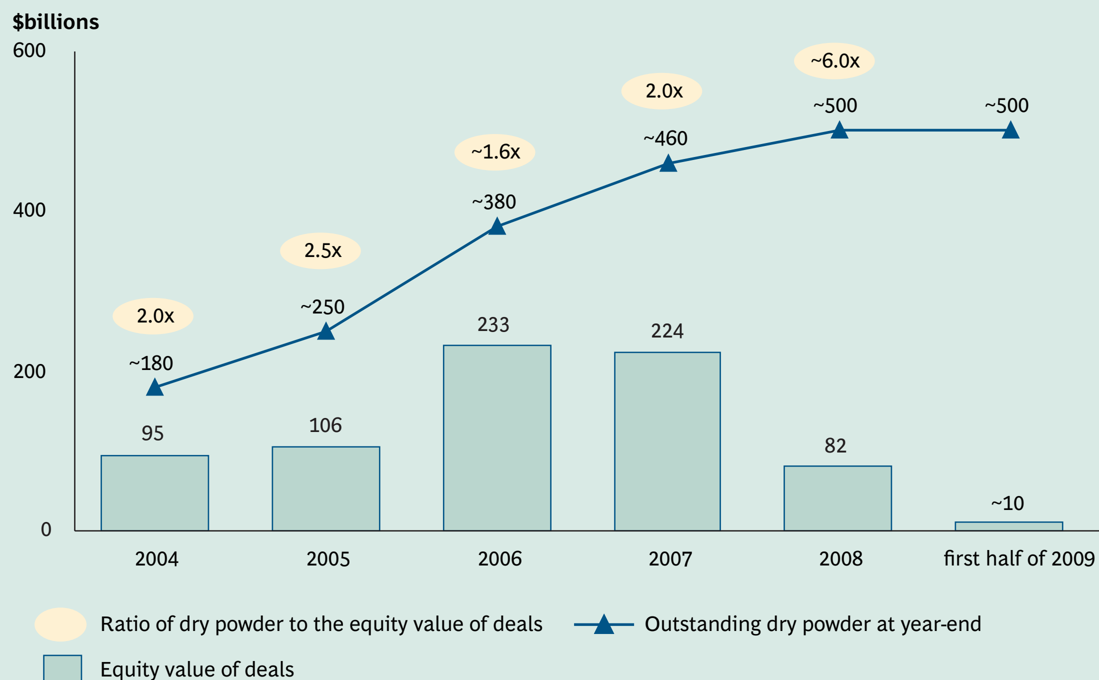
The available dry powder today is 2.5 times greater than ever before. The historic success of private equity has brought a strong and steady inflow of dry powder—with the volume of commitments exceeding the value of deals in any given year. In part, this is because dry powder is intended to be deployed over several years, and, in the past, commitments were based on the assumption that the private-equity industry would continue to grow. Before the financial and economic crisis, from 2004 through 2007, commitments were roughly twice as high as the value of transactions. (See Exhibit 1.) But in 2008 and the first half of 2009, the volume of deals plummeted. Nonetheless, dry powder continued to grow, albeit at a slower rate, to $500 billion, raising the ratio of dry powder to the equity value of transactions to a record level of six.[6] As a consequence, new fundraising activities have already been significantly reduced.

4. Partners Group Research Flash, "Factors of Success for Secondary Investing in the Current Market Environment," March 20, 2009.

5. This analysis took into account all available deal information for megadeal funds. In 2007 alone, megadeals accounted for one-third of all LBOs.

6. The estimate of $500 billion of dry powder as of the first half of 2009 is based on a 5 to 15 percent reduction of the total undrawn commitments of $550 billion.

Exhibit 1. In 2008, the Ratio of Dry Powder to the Equity Value of Deals Jumped to an All-Time High



Sources: BCG-IESE database; Standard & Poor's Leveraged Commentary & Data.
Note: The equity value of deals is based on S&P data on debt-equity splits.

Investors' Ability to Meet Their Commitments Varies Across the Board

Investors in private-equity firms—their limited partners—are heterogeneous. Each category of investor faces liquidity challenges and has differing degrees of interest in the private-equity asset class (measured by the share of funds they allocate to private equity), which means that each category of limited partner has a different predisposition when it comes to honoring its commitments.

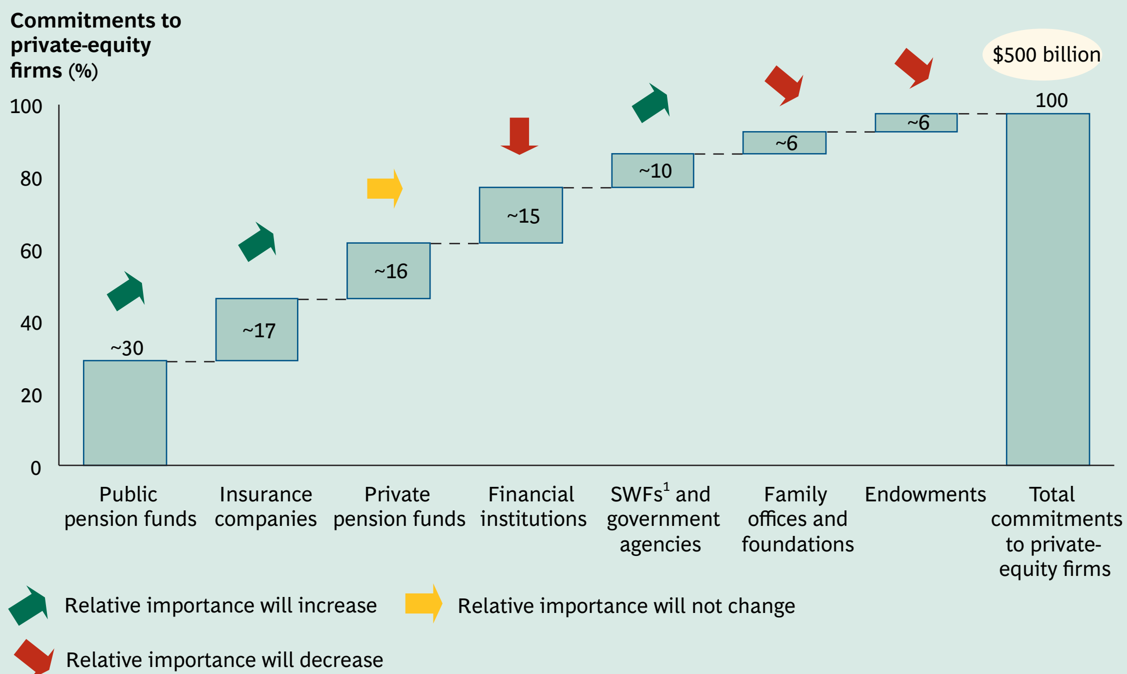
We have segmented limited partners in private-equity firms into seven main types of investors. The relative importance of these limited partners to the private-equity industry as a whole—today and in the future—is measured by their relative share of outstanding dry powder. (See Exhibit 2.) Public pension funds are the biggest players in private equity by a substantial margin, and their significance is likely to increase, as will the importance of insurance companies, sovereign wealth funds, and government agencies. Private pension funds, which currently account for the third-largest share of dry powder, are expected to sustain their significance, while financial institutions, family offices, and endowments will become less relevant to the private-equity industry. We did not include private-equity commitments by funds of funds, asset managers, and secondary funds of funds in our analysis. (For a discussion of funds of funds, please see the sidebar "A Note on the Role of Funds of Funds in Private Equity" on page 7.) Limited partners are discussed below in the order of their share of dry powder.

Public pensions funds will continue to honor most of their commitments.[7] Public pension funds have committed about $150 billion in dry powder (about 30 percent of the total) to private-equity firms.

Because public pension funds have a statutory obligation to honor their liabilities to members, these funds typically pursue relatively safe and stable sources of income. To provide a stable income from their investments, such funds allocate amounts of capital to different asset classes.

7. Our analysis is based on the BCG-IESE proprietary database sample of 601 public pension funds worldwide, representing more than $5.4 trillion of funds under management.

Exhibit 2. Seven Types of Investors Have Committed a Total $500 Billion in Dry Powder to Private-Equity Firms



Source: BCG-IESE database.
Note: The relative importance of commitments from each type of limited partner is measured against the anticipated commitments of the other types of limited partners.
[1]SWFs are sovereign wealth funds.

There are good reasons to believe that public pension funds will continue to honor most of their commitments and become more important in the limited-partner universe. Many of the large U.S. public pension funds have a long track record in private equity, stretching back more than 20 years in some cases, and they recognize that short-term downturns are inevitable. Most funds also have relatively liquid portfolios, aided by stable inflows from state and member contributions, limiting the need for secondary market sales and defaults. In addition, the denominator effect has eased as stock markets have rebounded, and private-equity valuations have also been written down.

Most of the largest U.S. public pension funds that invest in private equity are backed by state governments, which help the pension funds honor their commitments in order to avoid damage to the reputations of their pension systems. "I do not believe public pension funds are endangered because they are large, have unleveraged alternative investments, and are state-owned," said a senior managing director of a U.S. public pension fund. Despite the current budget crisis, we believe public pension funds will remain stable because of a strong annual inflow of cash—in 2008, for example, contributions to the California Public Employees' Retirement System (CalPERS), one of the world's largest public pension funds, were about $11.8 billion, with distributions of about $11.7 billion—and the very low likelihood that a state agency rated Aaa by Moody's would default.

In fact, there is evidence that public pension funds, which, on average, allocate about 6 percent of their capital to private equity, are stepping up their commitments. CalPERS, for instance, has raised its private-equity asset-allocation target from 10 percent to 14 percent, while the California State Teachers' Retirement System (CalSTRS) has raised its private-equity asset-allocation target from 9 percent to 11 percent.[8] This change was mainly triggered by the denominator effect, but it also indicates that these investors have continuing confidence in the attractiveness of the private-equity asset class.

8. CalPERS press release, "CalPERS Alters Asset Allocation—Raises Private Equity, Cash Allocation Targets," June 15, 2009.

Insurance companies will increase their commitments.[9] Insurance companies have committed about $90 billion in dry powder (about 17 percent of the total) to private-equity firms.

The insurance industry has been hit hard by the financial and economic crisis. During 2008, the sector wrote down approximately $150 billion of assets worldwide—one write-down alone accounted for more than $50 billion. Despite these setbacks and additional losses looming on the horizon, confidence in the sector's long-term future remains relatively strong, reflected in credit agencies' ratings: Moody's, for example, has downgraded only two of the ten largest insurance sector investors in private-equity funds since January 2008.

Insurance companies have both the resources and the long-term investment strategy to sustain or even increase their commitments to private equity. In addition, many aspects of their business model—for instance, life and property insurance—have reliable cash inflows and outflows that are not directly affected by the difficulties in the financial markets. The insurance companies' commitment is reflected in the fact that they were some of the first limited partners to participate in the latest round of private-equity fundraising.

Private pension funds are unlikely to default on their commitments.[10] Private pension funds have committed about $80 billion in dry powder (about 16 percent of the total) to private-equity firms.

The stability of private pension funds is intertwined with the health of the corporations backing them. Using credit ratings as a proxy for the health of these corporations—and, by implication, for the financial stability of private pension funds—the picture is mixed. There is evidence that the financial stress on some of these corporations has increased. For example, four of the ten corporations backing the largest private pension funds that have commitments to private-equity firms have suffered ratings downgrades since January 2008. Three of these corporations are now rated below investment grade, and another has gone into administration.

Despite the downgrades of some corporations, there is a relatively low probability that corporations overall will default on their payments to private pension funds—in large part because they want to prevent damage to their reputations. As a result, we expect the commitment of private pension funds to private equity to remain steady overall. We anticipate this to be the case especially for large, healthy corporations. Less stable, smaller companies may run into financial difficulties, which, in turn, will put stress on their pension funds' ability to meet private-equity capital calls.

Financial institutions are the most likely to reduce commitments.[11] Financial institutions have committed about $75 billion in dry powder (about 15 percent of the total) to private-equity firms.

The banking sector has been at the very core of the financial crisis. By the end of 2008, write-downs of toxic assets amounted to $1 trillion worldwide.[12] The perception of risk has also increased. Since 2008, Moody's has downgraded seven of the ten largest banks investing in private equity, and many large financial institutions only maintain above-investment-grade ratings because of the high likelihood of systemic support from governments.

Financial institutions are the most likely group of investors to reduce commitments to private-equity firms. In light of substantial loan losses—which are likely to increase as the recession bites more deeply—financial institutions need cash to calm concerns. Financial institutions will, for the foreseeable future, steer away from illiquid assets that require cash calls and are unlikely to deliver cash returns for several years. Many financial institutions also face pressure from the public, their stakeholders, and regulatory authorities to reduce the risk on their balance sheets—and private equity is often viewed by the public as high risk. Consequently, we anticipate that financial institutions will lobby strongly to reduce their

9. Our analysis is based on the BCG-IESE proprietary database sample of 274 insurance companies worldwide.

10. Our analysis is based on the BCG-IESE proprietary database sample of 615 private pension funds worldwide, representing more than $4.5 trillion of funds under management.

11. Our analysis is based on the BCG-IESE proprietary database sample of 438 financial institutions worldwide.

12. Standard & Poor's Banking Industry Survey, December 11, 2008.

private-equity commitments and may, in certain cases, default. It is safe to say that financial institutions will commit less to private equity in the near future, and their relevance within the limited-partner universe will diminish. “So far, we have seen two large financial institutions winding down their LBO units,” said the CEO of a European private-equity fund of funds. “It feels like this list may get longer.”

Sovereign wealth funds and government agencies are expected to increase their commitments.[13] Sovereign wealth funds and government agencies have committed about $50 billion in dry powder (about 10 percent of the total) to private-equity firms.

The financial and economic crisis has eroded the net asset value of sovereign wealth funds’ direct investments and reduced their main source of revenue—sales of commodities such as oil and gas. Although energy prices have recently picked up, most commodities still trade below their 2008 historic highs. And more than half of these sovereign wealth funds’ estimated $3 trillion of assets are generated from energy-exporting states in the Gulf. Noncommodity sovereign wealth funds, such as foreign-exchange funds in China and Singapore, have also been negatively affected by currency volatility and other macroeconomic developments during the crisis.

Sovereign wealth funds are relative newcomers to private equity, but we expect them to become increasingly important, not least because many sovereign wealth funds have little private-equity exposure at all and may perceive market entry in 2009 and 2010 as good vintage years. According to previous BCG estimates, the assets of sovereign wealth funds will increase by 19 percent per annum to $12 trillion by 2015.[14] At the same time, sovereign wealth funds will step up their low levels of capital allocation to private equity in order to diversify their asset bases and pursue higher long-term returns. “Sovereign wealth funds are currently undercommitted compared with public pension funds and endowments,” said a senior executive of a European sovereign wealth fund.

Family offices and foundations are likely to scale down their commitments.[15] Family offices and foundations have committed about $30 billion in dry powder (about 6 percent of the total) to private-equity firms.

Family offices, which manage the fortunes of very wealthy families, have been hit hard by the financial and economic crisis owing to their high reliance on equities. According to recent studies by the Wharton School and IESE, family offices in the Americas (where many of the largest are found) invested up to 44 percent of their assets in equities before the crisis.[16] These investments took a direct hit from the plunge of the stock markets.

Family offices have one of the highest private-equity allocations, averaging more than 11 percent of total funds—with some as high as 20 percent. Given present-day economic conditions and the likelihood of diminished returns from current private-equity investments, family offices will probably scale down and reallocate some of their capital earmarked for private equity to other asset classes. “I believe that some family offices are overcommitted and may want to reduce their exposure,” said a sovereign wealth fund alternatives investment manager.

Endowments will cut back on their commitments.[17] Endowments have committed about $25 billion in dry powder (about 6 percent of the total) to private-equity firms.

Endowments generate cash inflows from donations, tuition, license fees, patents, and investment income. While these cash sources are to a large degree unpredictable, it is reasonable to assume that the ongoing

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13. Our analysis is based on the BCG-IESE proprietary database sample of 171 sovereign wealth funds and government agencies worldwide. We have included government agencies in our sovereign wealth fund category because, in many ways, these agencies operate in similar fashion to sovereign wealth funds. Where they differ, however, is that government agencies should be less affected by commodity swings but hindered by short-term government restraints that could influence private-equity investments.

14. See *Conquering the Crisis: Global Asset Management 2009,* BCG report, July 2009.

15. Our analysis is based on the BCG-IESE proprietary database sample of 606 family offices and foundations worldwide.

16. The Wharton Global Family Alliance and IESE, *Single Family Offices: Private Wealth Management in the Family Context,* 2008.

17. Our analysis is based on the BCG-IESE proprietary database sample of 434 endowments worldwide, representing more than $523 billion of funds under management.

A Note on the Role of Funds of Funds in Private Equity

Funds of funds play an important role as distributors of about 10 to 15 percent of limited partners' commitments to private-equity firms. We have not included them in our universe of limited partners because they are intermediaries, not original sources of capital—as is the case with asset managers and secondary funds of funds.

There are two types of funds of funds: private, nonlisted funds of funds, which raise capital mostly from institutional investors, and listed funds of funds, which raise capital on the public market.

How have these funds of funds been affected by the financial and economic crisis? Most private funds of funds are, and will remain, stable investors owing to their strong, long-term relationships with limited partners and low levels of overcommitment. But publicly traded funds tend to commit more capital than they have available, bridging the gap with leverage or betting on timely distribution from existing investments. Given the limited availability of debt and the current lack of distribution, several listed funds have already gone out of business or have had to scale down commitments. That difficult situation for overcommitted funds will get worse, once the investment activity and the call down for capital picks up.

financial and economic crisis will decrease the likelihood of donations and push investment income below expectations. Further, there is evidence of cost cutting and scaling back on expansion projects.

Historically, endowments have invested strongly in private equity, allocating about 12 percent of their capital to this asset class. "Endowments have invested in private equity quite strongly in the past," said the CEO of a European fund of funds. "As distributions dry out, they may have a problem." Markdowns in the values of their investment portfolios will add to this pressure, as will liquidity constraints: several high-profile university endowments have already tapped the bond markets for more than $1 billion, and some endowments have started to sell their commitments in the secondary market. It is likely that university endowments will have to cut back on their private-equity investments.

Relative Exposure to Certain Types of Limited Partners Is an Additional Driver of the Shakeout

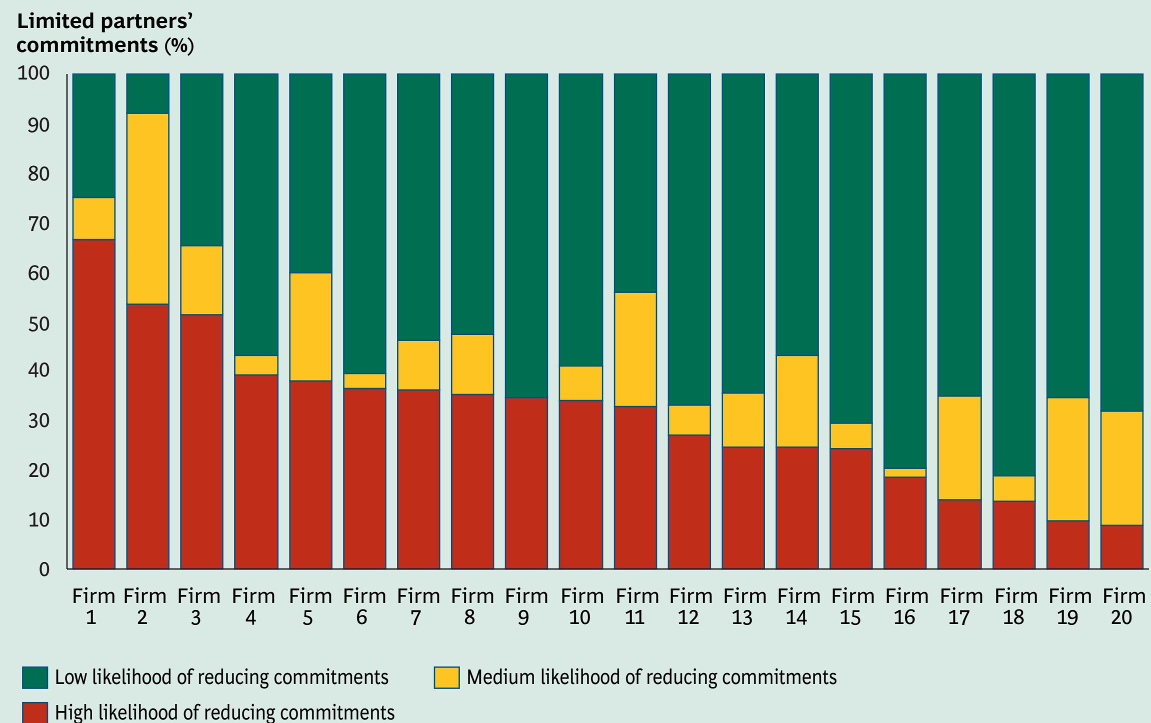
Overall, the expected reductions in commitments by limited partners do not pose a systemic threat to the private-equity industry. But the ability of individual private-equity firms to draw down limited partners' commitments will be affected to varying degrees—depending on the composition of their limited-partner universe. In short, although there is more dry powder than ever before, there will be winners and losers among individual private-equity firms.

We looked at 20 of the largest private-equity firms, ranked on the basis of outstanding dry powder, to assess their risk in terms of the likelihood of commitment reduction by their limited partners. (See Exhibit 3.) For those firms on the left-hand side of the exhibit, the likelihood that a limited partner will reduce its commitments is significantly higher than for those firms on the right-hand side of the exhibit.

As we discussed in our previous White Paper, private-equity firms are in the middle of a perfect storm: the financial and economic crisis that reduced the earnings of their portfolio companies, and, because of lower multiples in equity markets, the difficulty of selling off portfolio companies without realizing an immediate loss. The liquidity pressures on some limited partners will add strength to this storm, affecting individual private-equity firms to different extents.

Private-equity firms with a favorable mix of limited partners will not get into trouble. Those that have a large percentage of limited partners predisposed to reduce commitments may face cuts in capital that threaten the success of their investment strategy and their long-term viability. But the distinction between winners and losers is not simply a matter of which firms have the highest percentage of distressed limited partners. Even if a significant portion of a firm's commitments come from distressed limited partners, the firm could still be secure if its anchor investor is financially sound. A detailed analysis of a private-equity

Exhibit 3. A Snapshot of 20 of the Largest Private-Equity Firms Shows the Risk of Investors' Reducing their Commitments



Sources: BCG-IESE analysis; Limited Partners' disclosures.

firm's limited partners, including its anchor limited partner, is required in order to assess its long-term viability.

In the Private-Equity-Industry Shakeout, Investors Will Gain Power and Call for Major Change

The balance of power has shifted toward limited partners, and we expect that limited partners will exercise this power and guide major changes in how the private-equity industry operates. The topics already under discussion between limited partners and their private-equity firms are transparency, fees, the use of dry powder for bailouts, and the implementation of true active ownership.

More intense due diligence and higher transparency are expected. In the past, limited partners were, for the most part, as one limited partner said, "not bothered about reading the legal ramifications of commitment default." Today, investors are paying much closer attention not only to default penalties but also to the stability of their coinvestors in the fund. "If a coinvestor defaults, the problem is not just with the general partner but with the other limited partners who will have to compensate for the loss in commitments," said a leading European fund of funds manager.

Our research suggests that there will be much more intense due diligence in the future: Limited partners will probe more deeply into one another's financial positions and possible stresses. "We want to know who else is sitting around the table," said one investor. "This is not common practice yet, but it will be soon."

Private-equity firms also will be expected to make the basis of their valuations of their portfolio companies more transparent. "I see some companies' debt trading at 60 cents to the dollar, but many private-equity firms are still reporting pretty high equity values," said a U.S. limited partner. "I'm asking myself: 'Are these guys being honest with me?'" Because of the diverse techniques that private-equity firms still

use to value their portfolios, they will need to explain how they arrived at their valuations in order to achieve true transparency.

Fees will be challenged. Fees are, and will continue to be, on the radar screen in the ongoing dialogue between limited partners and their private-equity firms. There is a widespread discussion in the limited partners' community that the typical 20/2 fee model—the fees paid by limited partners (20 percent for performance or "carry" and 2 percent for management)—will be challenged when it comes to future funds. Currently, however, there is no indication that limited partners will use their collective market power to change investment terms in their favor: "My impression is that the large U.S. limited partners do not see a great urgency in changing the 20/2 standard. That's a pity, because if ever there is a chance to change something, it is now," said the head of a European leading investor. Nevertheless, some (less successful) private-equity firms have come under pressure to reduce their fees for future funds. We believe that a likely result of the shakeout will be a more differentiated fee structure.

Several limited partners also have demanded, sometimes successfully, that the discussion of fees include reconsideration of fees that private-equity firms currently charge their portfolio companies (for example, transaction fees, restructuring charges, and financing fees). These limited partners argue that fees for these services are captured in the management fee and should not be extracted from the portfolio companies in addition.

Dry powder is expected to be used for bailouts. Limited partners are asking how much dry powder is needed for existing portfolio companies that are in trouble. "There will be massive restructuring ahead when debt matures or portfolio companies hit the wall," said the chief investment officer of a U.S. private-equity fund of funds. In our previous White Paper on private equity, we estimated that more than 50 percent of all private-equity portfolio companies will breach covenants. A recent Moody's study revealed that 12 of the 30 companies most likely to default are backed by private equity.[18] Moreover, maturing LBO and high-yield debt levels are rising sharply, with refinancing needs expected to reach nearly $400 billion by 2014.[19] To deal with these challenges, private-equity firms may use some of their dry powder to bail out their current portfolio companies rather than engage in new buyouts. Limited partners' consent may be required, depending on specific contractual obligations.

It is in the interest of the portfolio companies, and of the private-equity industry as a whole, that restructuring happen as quickly as possible, even if debt is not maturing and covenants are not breached. "I want to sit at the table with stakeholders who can earn a positive return on investments made today, not with those who have lost all or most of their past investments and who are questioning how much and when they should write them off," said a CEO of a private-equity firm's portfolio company.

True active ownership will become a table stake. The clearest driver of success for private-equity firms is the capability to create operational value (true active ownership).[20] Limited partners, therefore, seek a deeper understanding of that capability by focusing on team track records and internal organization and processes (the governance model). That approach goes far beyond a quantitative analysis of the main sources of past value creation—multiple expansion and leverage. Limited partners will base their future commitment decisions heavily on that capability dimension—therefore it becomes a table stake for private-equity firms to survive.

The private-equity shakeout and the shift of power toward limited partners will turn the private-equity industry into a mature, stable sector that is able to respond positively to shocks and move forward efficiently.

18. Moody's, "U.S. Bottom Rung—First Quarter 2009."

19. Standard & Poor's Leveraged Commentary & Data.

20. See *Get Ready for the Private-Equity Shakeout: Will This Be the Next Shock to the Global Economy?*, BCG and IESE White Paper, December 2008.

When LBO private equity first started gathering pace about 30 years ago, with the relaxation of certain regulations (such as the "prudent man" rule), firms focused on multiples—buying low and selling high.[21] Later, the industry became more sophisticated and relied more on leverage as a key tool. Until now, because of ever-increasing commitments from limited partners, the LBO private-equity industry has never witnessed a serious weeding out of weaker players. The financial and economic crisis will propel the industry, through the shakeout, into the next stage of its development—creating an environment in which empowered limited partners will only engage with private-equity firms that are able to leverage the active-ownership model.

21. The "prudent man" rule prohibited pension funds in the United States from allocating significant amounts of capital to high-risk assets (until 1979).

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The authors would like to thank the following members of BCG's writing, editorial, and production team: Barry Adler, Katherine Andrews, Gary Callahan, Keith Conlon, Kim Friedman, Pamela Gilfond, and Sara Strassenreiter.

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