AVCAL

Australian Private Equity &
Venture Capital Association Limited

The economic contribution of private equity in Australia: report summary

MARCH 2013

In 2012, AVCAL commissioned Deloitte Access Economics (DAE) to conduct a study of the economic contribution of private equity in Australia.

This report presents the key findings on the role of private equity in the Australian economy in terms of revenue and jobs growth, and how the private equity model impacts the businesses invested in.

It presents evidence that private equity investment makes a significant economic contribution in Australia through total value added and the provision of jobs. The modelling finds that, if private equity investee firms were an industry in their own right, their revenue would exceed that of either the coal mining or the general insurance industry. They would also directly employ more people than either the automotive or the banking industries.

A summary of the report's main findings is set out below. The full report is available from the AVCAL website.

SUMMARY OF KEY FINDINGS:

- Australian companies backed by private equity employ **262,000 workers**, making this group a larger employer than either the automotive or banking industries.

- They also indirectly support an estimated **251,000 additional jobs** through flow-on effects to other businesses. All in all, private equity backed companies in Australia support an estimated **half a million jobs**.

- Private equity backed firms contribute total value added of **$58.8 billion per annum** to Australia's GDP.

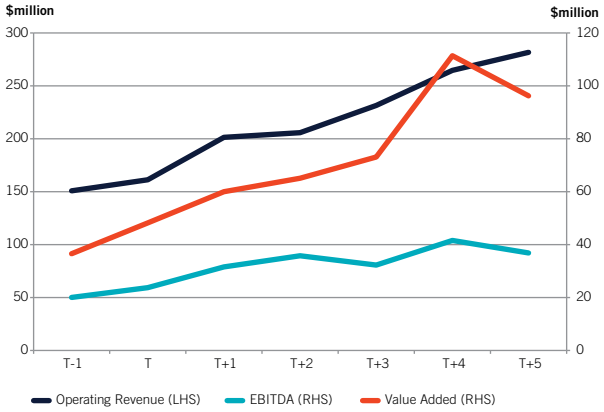
- Private equity backed firms **generate more revenue** than either the coal mining or the general insurance industries in Australia.

THE IMPACT OF PRIVATE EQUITY ON BUSINESSES

- This analysis is based on survey data for 106 Australian investee companies for private equity investments made since FY2000, for which at least three years of data is available. This data was provided by 18 private equity firms that account for around 70% of total private equity funds under management in Australia.
- **Length of ownership.** The average length of ownership of the investee firms for those that have been disposed of was 48 months. For the firms which were still held by the private equity investors as at 30 June 2012, the average length of ownership was slightly longer at 51 months. The fact that private equity owners maintain their exposure to the investee firms for four years on average suggests a substantial commitment to adding value to the firm.
- **Impact on business operations.** The private equity business model brings a high degree of agility to running firms and an alignment of owner/manager interest that may not be possible under other ownership structures. While this can provide advantages for investors in private equity funds, more flexible businesses can also be good for the broader economy, building resilience and enabling innovation in the face of change. This report finds that private equity investment has a significant impact on the operational and management structures of investee firms, and adds capital and expertise to help the firm grow. It also brings a new focus and a greater sense of urgency to the task by changing operational practices and management. The extent of this influence can be found in the range of management improvements introduced by private equity, as shown below:
  - 90% of private equity managers introduced new operational practices in their investee companies;
  - 85% introduced new managers to help drive and support the growth strategy; and
  - 70% injected additional capital into the company.

  Additional case studies support the findings that private equity-owned firms bring strong people management and operational management practices. This legacy is likely to remain even after private equity investors exit from the firms.
- **Impact on financial performance.** The proof of the benefits of the private equity model lies in the performance of the firms acquired and transformed by private equity management. In the majority of cases, the report finds improved performance across a range of industries. During a typical five-year period of private equity investment:
  - Revenue grew at a compound annual growth rate (CAGR) of 11.0%;
  - The average EBITDA grew from $20 million to $37 million after five years, at a CAGR of 10.7%; and
  - The average value added (the sum of EBITDA and wages) was $37 million per company prior to acquisition, rising to $96 million after five years at a CAGR of 17.5%.

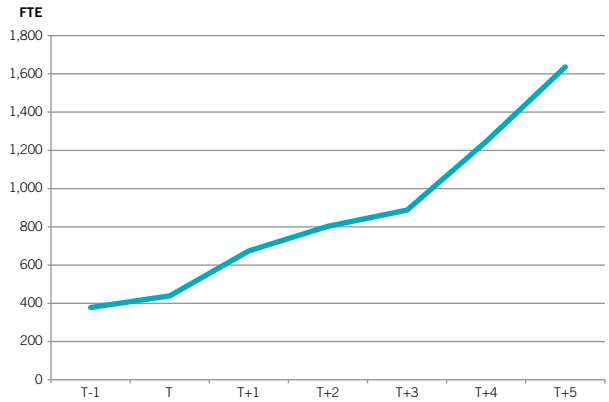
Chart 1: Impact of private equity on selected financial measures



Sources: DAE, AVCAL

- **Impact on employment.** Private equity investment is a significant job creator. Over a five-year period from the year of initial investment:
  - Investee firms expanded their workforces at a CAGR of 27.6%; and
  - The average workforce per company grew from 378 to 1,636 full-time equivalent (FTE) jobs.

Chart 2: Impact of private equity on employment



Sources: DAE, AVCAL

THE CONTRIBUTION OF PRIVATE EQUITY TO THE AUSTRALIAN ECONOMY

The economic contribution analysis was based on a representative sample of 49 investee companies for which financial and employment data was available throughout the sub-period of FY2007 to FY2011.

The economic contribution of private equity is measured in terms of:

- **value added**, which is the contribution to GDP; it includes wages paid to employees and the gross operating surplus generated including taxes less subsidies; and
- **employment generated**, measured in full-time equivalent jobs.

Contributes total value added of $58.8 billion per annum to GDP

The annual direct contribution of private equity to the Australian economy is estimated to be $25 billion. This is a substantial figure by itself. But private equity investee firms also contribute indirectly to the economy by acquiring goods and services from other firms. This is the indirect contribution made by investee firms to the economy, obtained by subtracting EBITDA and wages from revenue. This needs to be taken into account when estimating the flow-on effects. The indirect contribution of private equity investee firms is estimated to be $33.8 billion in value added. This brings the total economic contribution of investee firms to an estimated $58.8 billion.

Employs more jobs than the automotive or banking industries

Private equity investee firms employ an estimated 262,000 full-time equivalent jobs. To put it in context: the average number of jobs employed by private equity-owned firms over FY2007-11 exceeds both the banking and automotive industries in Australia (which employed an average of 196,000 and 260,000 people respectively over the same period).

Investee firms also indirectly support an additional 251,000 full-time equivalent workers. All in all, companies backed by private equity provide employment for 513,000 full-time equivalent workers.

Generates more revenue than coal mining or general insurance

The total revenue of private equity investee firms is estimated to be around $63.5 billion. This exceeds the coal mining (black and brown coal) and the general insurance industries, which had average turnover of $55 billion and $54 billion during FY2007-11, respectively.

CONCLUSION

This research breaks new ground by providing, for the first time, a detailed analysis of the economic contribution of private equity in Australia.

The findings show that private equity investee firms make a noteworthy contribution to the domestic economy. Private equity ownership generally results in growth in revenue and employment. The total impact on the economy – including flow-on effects to other businesses – is even greater.

The data demonstrates that private equity ownership has profound, positive effects on investee firms. In most cases, this has resulted in improvements to the management team and operating practices, and injections of new capital. Shedding more light on these aspects of private equity's input is likely to provide more insights into its contribution to the economy.

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