PRIVATE EQUITY COUNCIL

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# Executive Summary

*The Credit Performance of*
*Private Equity-Backed Companies*
*in the 'Great Recession' of 2008–2009*

A PEC Study - March 2010

The paper addresses the important policy and business question of whether companies acquired through leveraged buyouts and similar transactions are more likely to default on their obligations than other non-investment grade firms. This topic has understandably and appropriately received renewed attention in recent years due to the increase in private equity transaction volume and related debt issuance from 2005 to 2007.

Key conclusions of the study are:

- Analyzing a dataset of more than 3,200 private equity-backed companies acquired in a buyout or similar transaction between 2000 and 2009 and held through 2008-2009, the paper finds that during the "Great Recession" of 2008-2009 private equity-backed businesses defaulted at less than one-half the rate of comparable companies:  2.84 percent versus 6.17 percent.
- This finding is at odds with the suggestions of critics who argue that "overleveraged" portfolio companies have or will default at rates that are several times higher than those of similar businesses.
- Both Moody's Investors Service and Standard and Poor's (S&P) produced studies that inflated private equity default rates by developing new and expansive definitions of what constitutes a default or by artificially broadening the universe of firms deemed to qualify as private equity-owned.
- A widely-cited 2008 paper by Boston Consulting Group (BCG) forecasting that nearly half of the world's private equity-backed companies would default appears to have significantly overstated the problem. Data show that cumulative defaults are running at a rate that is approximately 30 percentage points below that predicted by BCG.

While additional defaults are likely to occur and refinancing challenges will remain, the data to date support the contention that the changes introduced by private equity investors reduce the incidence of default.  Claims to the contrary either rely on misleading data, or involve speculation about future default rates without historical basis.