We use cookies to ensure that we deliver the best user experience of our website. If you would like to, you can change your cookie settings at any time. Continue

Private Equity Buyouts Lead to Job Losses but Increased Efficiency

Posted on Wednesday 7th November 2007

Even though significant job losses can occur straight after Private Equity buyouts, the companies then become stronger, more efficient and start to recruit again within five years, according to research carried out at Birmingham Business School.

Private Equity firms raise funds from sources outside the firm and then identify companies they believe have potential for growth with the objective of buying them, raising their efficiency and then selling them on at a profit.

A great deal of criticism has been levelled at the Private Equity industry lately as it is seen by many as an asset-stripping exercise which leads to huge job losses. Private Equity firms have also come under scrutiny for paying too little tax and using debt to finance buyouts thereby increasing the financial risk of their targets.

The researchers - Professor Robert Cressy, along with colleagues at the University of Bologna - have found that up to a quarter of jobs over a 4 year period are typically cut as a result of a private equity buyout. Loss-making departments are axed, redundant layers of management cut and excess labour jettisoned, thus increasing the company's operating profits and efficiency.

In the longer term this new efficiency is likely to be passed on to the customer in the form of more competitive pricing. This in turn generates increased sales. As the demand for the product rises more workers are required so the company can begin to recruit once more.

Professor Robert Cressy, lead investigator from Birmingham Business School, says, 'Our research has significant implications for the debate between the Private Equity industry and the unions as to what happens to companies after a private equity-led buyout. It does this by offering precise quantification of the effects of buyouts on jobs and efficiency in the short and longer term.

'Both parties to the debate have an element of truth in what they say. Private equity firms are probably right that after 5 years their buyouts will generate jobs; the unions are certainly right that in the short term there is job pain from sackings.

'However, both are also to some extent wrong: private equity firms are wrong in playing down the short term job cuts and the unions are wrong to oppose the increased efficiency and higher profits that eventually result in more staff being recruited and greater long term viability.'

Ends

Notes to Editors

1. In this study, job losses over a five year period after a buyout are recorded as follows:

a. Within one year after a buyout 7% of jobs have been cut

b. After 4 years 23% of jobs have been lost

c. After 5 years this figure falls to 21%

2. This is the only study so far to use a 'control sample' of companies, in other words a set of companies identical to those involved in buyouts were not bought out. Using this method, the researchers were able, with some precision, to ascertain the effects of a change of ownership and financing in a buyout on jobs and profitability.

For further information

Kate Chapple, Press Officer, University of Birmingham, tel 0121 414 2772 or 07789 921164.

© University of Birmingham 2014