

For immediate release
Dec. 6, 2012

Pepperdine study finds businesses backed by private-equity and venture-capital funding have significantly stronger sales and job growth

CASSOPOLIS, Mich. — Both private equity and venture capital financing dramatically accelerate sales and job growth of small and medium-sized U.S. businesses, according to a new study being released by the Institute for Exceptional Growth Companies (IEGC) and Pepperdine University.

John Paglia and Agus Harjoto, associate professors of finance at Pepperdine's Graziadio School of Business and Management, studied the performance of 8,669 establishments (individual workplaces) with fewer than 500 employees that received private capital financing between 1995 and 2009. During the five years following a financing event, the 6,815 establishments that received private equity:

- Generated a revenue increase that was \$7 million higher (129 percent more) than a control group of non-backed establishments of similar size and characteristics. This translated into an 11.6 percent compound annual growth rate versus 5.7 percent.
- Created 36 more new jobs (257 percent higher) than the control group — a 5.6 percent compound annual growth rate versus a 1.8 percent rate for the control group.

The results were even more dramatic for the 1,854 recipients of venture capital. During the five years after their financing event, these establishments:

- Generated an increase in revenue that was \$24.7 million higher (846 percent more) than non-backed counterparts. This translated into a 36.4 percent compound annual growth rate versus a 6.9 percent rate for non-funded establishments.
- Created 127 more new jobs (608 percent higher) than non-backed establishments — a 22.4 percent compound annual growth rate versus a 4.5 percent rate for the control group.

The researchers also determined that the impact on growth was more immediate for recipients of venture capital than private equity, although growth wasn't as significant in two to three following years unless more venture capital investment was added.

"The magnitude of revenue and job growth for private-capital backed companies was surprising," says Paglia. "We expected it to be positive, especially at the lower end of the marketplace, but we didn't realize how large it would be. The results suggest two things: 1) private capital is a powerful stimulant for small- and mid-sized companies, and 2) when capital is deployed in this segment, it's focused on value creation rather than financial engineering, which is often seen in larger buyout transactions."

One explanation for private capital's significant impact on smaller establishments may be an inherent gap in skill sets in these businesses, Harjoto observes: "Private capital fund managers bring more to the table than just

money. They also bring expertise to help owners address various growth challenges and can help establish the kind of networks and relationships that allow these companies to move forward.”

In addition to performance, Paglia and Harjoto also examined various demographic traits for the 8,669 establishments that received private capital. Among their findings:

Ownership — Minority-owned businesses were 12.6 percent less likely to receive private equity and 34.7 percent less likely to receive venture capital. Women-owned businesses were 3.6 percent less likely to receive private equity and 22.5 percent less likely to obtain venture capital. Foreign-owned businesses were 39 percent less likely to receive private equity and 45.6 percent less likely to obtain venture capital. This confirms previous research for minority- and women-owned businesses, but was a new finding for foreign-owned.

Size — Establishments with more employees tend to attract private equity. Of those establishments studied, the 6,815 recipients of private equity averaged 155 employees compared to an average of 59 employees for the 1,854 venture-capital recipients.

Geography — Small and mid-sized establishments most likely to attract private equity were located in California, New York, Texas and Florida. The top five states most likely to attract venture-capital recipients were California, Massachusetts, Washington, Texas and New York.

Industry clusters — Private-equity recipients tend to be in retail, transportation and machinery production whereas establishments in business services, computers, chips and medical equipment tend to attract venture capital. In addition, establishments with government contracts were more likely to attract both types of private capital.

Paglia and Harjoto are among researchers that IEGC has selected to study high-growth companies and tap its unique data sets, which merge National Establishment Time-Series (NETS) with PitchBook data on private-equity portfolio companies and venture-capital backed firms. “IEGC’s data was extremely beneficial,” says Paglia. “The matched NETS and PitchBook data allowed us to look at the establishment perspective and examine the impact of private capital at a very granular level.”

Doug Tatum, chairman of IEGC’s advisory committee, says that the Pepperdine study not only highlights the important role of private capital in the U.S. economy, but also expands the industry’s knowledge base. “This is especially true for job creation,” Tatum explains. “Until now, most of the research on private capital has focused on European companies, larger U.S. companies or aspects unrelated to job creation, such as venture capitalists’ role as an intermediary or the governance, ownership structure, operations and value of private-capital backed companies.”

“John and Agus’ study clearly shows that companies with private capital funding demonstrate higher growth than those without,” observes Gary Kunkle, IEGC research fellow. “This should encourage government agencies to promote the role of private equity and venture capital financing in the economy. In addition, if governments wish to increase social equity and spread the benefits of growth across a larger population, more effort should be made to extend private equity and venture capital financing into minority and women-owned firms.”

###

About Institute for Exceptional Growth Companies (IEGC): The Institute for Exceptional Growth Companies was created by the Edward Lowe Foundation through a three-year grant from the NASDAQ Educational Foundation. IEGC is creating new datasets and using existing data in innovative ways to track and better understand exceptional growth companies, their impact on community and economic development, and their relationship with equity-funding sources. More information at: <http://youreconomy.org/pages/iegc.lasso>

About Pepperdine University's Graziadio School of Business and Management:

Founded on the core values of integrity, stewardship, courage, and compassion, Pepperdine University's Graziadio School of Business and Management has been developing values-centered leaders who advance responsible business practice since 1969. Student-focused, experience-driven and globally oriented, the Graziadio School offers fully accredited MBA, Masters of Science, bachelor's completion and non-degree executive business programs for business professionals, entrepreneurs, managers and senior executives at all stages of their professional and personal development. More information: <http://bschool.pepperdine.edu/newsroom>

Media contacts:

T.J. Becker at 269-445-4257 or tjbecker@lowe.org

Douglass Gore at 310-568-5580 or fgore@pepperdine.edu