# Successful private equity-backed firms are more likely to push for acquisitions, but cut internal investments

Submitted by: BlueSky Education

Wednesday, 24 January 2024

---

New research from Vlerick Business School reveals that private equity (PE)-backed companies, that are overperforming and have large investments, prefer to push for acquisitions and reduce internal investments to boost their returns.

On the other hand, underperforming firms, that have experienced boards and larger investments, tend to focus on capital investments.

Veroniek Collewaert, Professor of Entrepreneurship, and Sophie Manigart, Professor of Entrepreneurial Finance, along with their colleagues, studied how PE investors guide their portfolio firms to pursue growth either internally (capital investments) or externally (acquisitions). Additionally, the research examines whether the company's performance, relative to the targets set by both the primary PE investors and the portfolio firms, had an impact on their growth strategies.

Analysing a sample of 51 portfolio firms over 5 years, the study found that the growth strategies pursued by PE-backed firms depended not only on their performance relative to their targets but also on the incentives and influence of their PE investors in governing their actions.

The study found that when a PE portfolio firm is not meeting expectations, its investors are more likely to push for capital investments, and against acquisitions when the PE has invested more money and has more experienced people on the board. On the other hand, when the company is doing better than expected, the researchers found that investors push for acquisitions and against capital investments when they have put in more money. In cases where the PE investor has invested relatively larger amounts, acquisitions hence became more likely to occur in the event of overperformance.

Contrary to the researchers' initial expectations, boards with more senior members were found to be more inclined towards advocating for capital investments rather than pursuing acquisitions.

In short, the study showed that underperformance correlated with increased capital investments (but fewer acquisitions) when investors are more heavily financially committed and boards are more experienced. Conversely, during overperformance, less capital investments happen with a more heavily financially committed investor, but more with more senior board members.

The likelihood of the company making acquisitions is thus linked to larger investments but less likely with experienced board members in the case of overperformance.

"Firms double down on improving existing operations when faced with significant performance shortfalls. As one of the PE investors we talked to put it – ‘if your company is in distress, the last thing you want to do is put another M&A target on top and add complexity and stress for the management team.’ Acquisitions are not a great way to buy yourself out of trouble. Yet, we found overperforming firms receiving larger PE investments pursue more acquisitions and scale back internal investments, aiming to amplify returns," explains Collewaert.

However, a PE investor's directing hand depends on involvement and influence, which varies across portfolio firms based on factors like the size of their investment and the experience of appointed board members. Firms gaining less PE attention and influence exhibited more muted reactions regardless of exceeding or missing performance milestones.

"With limited oversight from their PE investors, there's less pressure on management teams to strategically shift capital allocations between internal investments and acquisitions," notes Professor Manigart.

The study advances knowledge of how portfolio firms respond to the performance aspirations imposed by their investors. "Our findings should interest PE investors looking to optimise value creation, as well as managers hoping to accelerate growth," suggests Collewaert.

Alongside Collewaert and Manigart, undertaking the research was Jeroen Neckebrouck, Professor of Entrepreneurship at IESE Business School, Tom Vanacker, Professor of Entrepreneurial Finance at Ghent University (Belgium) and University of Exeter (UK), and Dries Bourgois at KU Leuven. The research was published in the Strategic Entrepreneurship Journal in November 2023.

To speak with the researchers, or for a copy of the academic article, please contact Alexandre Lopez at BlueSky Education at alex@bluesky-pr.com or call +44 (0)1582 797959.



Distributed via Press Release Wire (https://pressreleases.responsesource.com/) on behalf of BlueSky Education

Copyright © 1999-2024 ResponseSource, The Johnson Building, 79 Hatton Garden, London, EC1N 8AW, UK

e: info@responsesource.com t: 020 3426 4051 f: 0345 370 7776 w: https://www.responsesource.com

responsesource