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# Defending Private Equity From a Flawed Picture

By STEVE KLINSKY

DealBook recently published a column by the Deal Professor saying that venture capital and private equity are two very different and clashing worlds and citing venture capital's better public image. "Venture capital is viewed as a creative industry, while the world considers private equity as finance, money men who do not create," Steven M. Davidoff wrote.

Venture capital, when properly and successfully executed, does in fact deserve full praise. But the same praise is deserved for successfully executed private equity investments that benefit society just as much and generally apply in even larger dollar amounts across a broader range of industries.

Today, there are more than 1,800 American-based private equity firms that vary in size, geography and expertise, operate in all parts of the country and employ six million workers. To the extent that general conclusions can be drawn, the research has been very positive.

In December, Ernst & Young released an analysis of 158 buyouts done in 2008 and 2009 and found that "private equity investors created lasting value that outperformed public company benchmarks across comparable sectors and geographies."

Similarly, a study led by Josh Lerner of Harvard Business School found that in the first two years of private equity ownership, portfolio companies increased the rate of job growth at new American facilities to 6 percent above the industry average, and that the benefits of the improved performance are passed on to employees in the form of higher wages, competitive benefits, greater job security and stability.

My private equity firm, New Mountain Capital, publishes its own social responsibility dashboard each year. Over all, New Mountain has added or created over 8,600 jobs at the companies it has owned, net of all job losses, and most of these jobs have been created organically through business growth. New Mountain companies have spent more than $997 million on research and development, software development and capital expenditures during New Mountain's ownership. No New Mountain private equity portfolio company has ever gone bankrupt or missed a debt payment.

Other private equity firms emphasize social responsibility and business building in their own ways as well, like the path-breaking alliance between Kohlberg Kravis Roberts, the Carlyle Group, Providence Equity Partners and others and the Environmental Defense Fund.

And, of course, one crucial social benefit of high-quality private equity is the many billions of dollars of gains paid out to the pension funds and endowments that comprise our industry's main investors. The returns delivered by private equity firms over the last decade far exceed the rate of return from the Standard & Poor's 500-stock index over the same period and are critically important to help pension plans and endowments achieve their own benefit goals.

The activities of private equity firms and venture capital firms are often essentially indistinguishable. For example, New Mountain and other private equity firms have started a number of companies from scratch, like Validus Re, now a major reinsurance company listed on the New York Stock Exchange. We have built companies across technology and growth sectors like software, data and medical devices, and we have invested side by side with venture capital investors in companies like Ikaria, where the fundamental research behind the company won the Nobel Prize for medicine in 1998.

Financial engineering has also become less important to private equity firms in past years. For example, New Mountain used no debt at all in the original acquisition structures of a majority of our platform companies, and more than 20 of our 50 investment professionals were formerly chief executives, senior level operating executives or management consultants. A 2008 study by the Boston Consulting Group found that operational improvement as a source of value creation by private equity firms as a whole increased twofold from the 1980s to today, reflecting a long-term historical shift away from leverage.

I grew up in a family business in Michigan and, to me, high-quality private equity is this same family business mentality brought to a larger and more modern scale: highly involved and knowledgeable shareholders, working directly and closely with their management partners in a private setting to improve the companies they own.

Private equity, when properly executed, is a proven asset class that can deliver superior returns to its investors and can provide capital, create jobs and drive positive economic activity at a time when our economy badly needs such support. It is important to avoid false stereotypes about the private equity industry or any industry in order to prevent flawed public policy.

*Steve Klinsky is founder and chief executive of New Mountain Capital and chairman of the Growth Capital Committee within his industry's Private Equity Growth Capital Council.*