Private Equity: Strategies for Improving Performance

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Abstract:
Evidence from the literature suggests the median private equity manager does not create excess returns over public markets net of fees. The major issues are the fees and the managers’ ability to lag valuations (referred to as stale pricing). In this paper, we first confirm findings from literature using a more robust factor model that allows for leverage, illiquidity and volatility clustering. Our factor model explains 70 to 90 percent of the variation in returns. Second, based on the high explanatory power, we suggest two methods of applying these factor models to improve performance. We test the robustness of the methods using historical and simulated data. The findings from our paper can alter the views institutions currently hold on private equity in terms of asset allocation.

Presenter: Ron Bird