AALBORG UNIVERSITY
DENMARK

Summer 2017

4th Semester: Master's Thesis

Title: How to mitigate short-termism in business drawing inspiration from the uniqueness of private equity firm practices.

Confidential: No

Number of keystrokes of the project: 183.824 equal to ≈ 76,6 pages

Submission: 09/08/2017

Supervisor: Svetla Trifonova Marinova

Student: Thomas Olesen

Student number: 2014-2895

____

Summary:

This master's thesis sets out to discuss a relevant topic on the rise in the business community. The issue of short-termism. There is empirical evidence showing how companies are increasingly acting upon the short-term goals of the organisation at the expense of long-term objectives and thus limiting the potential future performance of the business. Furthermore, executives alter budgets to meet the quarterly financial goals, even though they are aware it hurts future performance. It is shown that the pressure on organisations to meet short-term goals have increased in recent years and comes from several sides, such as stakeholders, competitors, and economic uncertainty.

The projects revolve around coming up with ways that can mitigate this issue of short-termism in companies. This is done by drawing inspiration from an asset class that manages with a long-sighted strategy successfully and puts less thought towards short-term performance and goals. This asset class is private equity.

Private equity funds manage their portfolio companies in a widely different way than normal public equity companies do. This is due to a longer investment horizon and the understanding that long-term objectives are what grows the business. There is empirical evidence showing that long-term orientated companies revenue grew 47 percent more, spent 50 percent more on research and development, post greater shareholder returns, added more jobs compared to short-term orientated firms.

Through an analysis of two private equity portfolio companies this project attempts to dismantle how this long-term strategy is realised. While each of the companies have unique properties, there are common traits. To realize the long-term objectives several successful business actions has been utilized by the portfolio companies that even revolutionized the industries in which they operate. Moves such as cost-cutting, zero-based budgeting, business review, reinvestment, stakeholder management, human capital management etc.

The analysis of the portfolio companies combining with understanding the issue of short-termism resulted in the development of a framework that can be drawn upon for mitigating short-termism in other types of companies than portfolio companies, where through continuously performing the steps with a long-term objective in mind can reach the goal of reducing short-term focus at the sacrifice of long-term objectives.

Keywords:

Private Equity, Portfolio Companies, Public Equity, Strategy, Strategy Formulation, Performance, Investment, Investing, Shareholders, Stakeholders, Agency Theory, Business Model, Growth, Cost-Cutting, Zero-based budgeting, Short-Term, Short-Termism, Mid-Term, Long-Term.

Table of Content:

List of figures:

Chapter 1 – Introduction:

The goal of a business is to realize returns for its owners and stakeholders. Doing this in perpetuity requires a well-run business model that works both in short-, mid- and long-term.

A plethora of owners and stakeholders look only at the short-term strategy to realize fast profits. The average holding time for stocks have reduced to a mere eight months in 2016 from eight years in 1960 (Semuels, 2016). LPL Financial even starts talking about average holding times as short as 5 days (Kleintop, 2012) (LPL Financial, 2017). The picture is easy to fathom.

The dream of excessive returns on a short-term basis can however be very damaging to both the company and the economy, as the economy is dependent on companies making the right long-term business decisions. However, short-termism makes little sense when e.g. Ernst & Young (2014) and McKinsey (2017) show in empirical investigations how long-term companies outperforms other firms in the period of 2001 to 2014. Long-term firms gained 47 percent more revenue than other firms, earnings grew 36 percent more than other firms, economic profit grew 81 percent more than other firms, 50 percent higher likelihood to deliver top shareholder returns, created more jobs than other firms, spent 50 percent more on research and development than other firms, lower human capital costs, longer tenure of executives etc. (Ernst & Young, 2014) (McKinsey Global Institute, 2017). These makes for compelling arguments, why one can ask themselves why short-termism happen.

Short-termist behaviour is in short: behaviour where companies act on short term sacrificing long term performance. Neglecting long term goals because of short term goals limits the firm's future performance and has been empirically proven to give companies with a good balance between short term goals and long-term objectives a competitive edge in the long run (Ernst & Young, 2014).

Nigel Wilson the CEO of Legal & General argues that under-investment because of a focus on short-term profits is a major contributor to why emerging markets, Asian Tiger economies, and especially China is catching up to the west and might soon surpass the west (Wilson, 2015). Furthermore, an example of the damages caused by extreme short-term thinking can be seen at Wells Fargo, where the employees opened accounts with no consent from the customers. If the employees did not perform the task they were in some cases fired for underperformance (NPR, 2016) (Phillips, Heller, & Coleman-Fenn, 2016).

The necessity for long-term thinking is slowly being realized in the investment community, corporate world as well as in society. This also holds true, if the West want to uphold their position of power in the world it is increasingly more necessary to realize that long-term thinking is what makes or breaks the economy in the long run. In addition, with even broader considerations, the world we live on is one of finite resources, which should be used optimally.

Examples of scrapping short-term thinking include Legal & General, which is a big multinational company providing financial services as well as insurance, that manages over 1.1 $ billion USD (Legal & General, 2017). They have stopped giving shareholders quarterly reports on financial performance, as they reason it promotes short-term thinking. Legal & General have instead taken the approach of giving reports every 6 months. Furthermore, they try to get companies of which they invest to end quarterly reporting as well. A couple of statements from Legal & General investment management chief Mark Zinkula sums this up well. First, he argues the added benefits of this strategy, as “We think it can lead to more articulation of business strategies, market dynamics and innovation drivers, which are linked to key metrics that drive business performance and long-term shareholder value” and, secondly, he adds that companies should not worry about communication etc., as “We value the communication we have with management teams highly. Reducing the time spent on reporting, which adds little to the business, does, not, in our view lead to a deterioration in that communication (Wallace, 2015). Interestingly, Legal & General do not stand alone taking this position.

Unilever already took the position of not releasing profit figures in 2009 stating that they were a distraction and only attracted short-term investors (Dakers, 2014). The stock market was not thrilled with the announcement to say the least shaving 22 % of the Unilever’s stock price (Semuels, 2016). Furthermore, The CEO of Unilever, Paul Polman, states “Too many CEOs play the quarterly game and manage their businesses accordingly” and “Many of the world’s challenges cannot be addressed with a quarterly mindset” (Semuels, 2016).

There are also initiatives such as the ‘American Prosperity Project’ (American Prosperity Project, 2016) and ‘Focusing Capital On The Long Term’ (FCLT Global, 2017) aiming to encourage both companies and the nation into long-term thinking. Several prominent business personalities support the American Prosperity Project such as CEO Paul Polman form Unilever, CEO Chip Bergh from Levi Straus, and CEO Ian Read from Pfizer (American Prosperity Project, 2016). Several prominent companies support the idea of long-term objectives, and thus founded Focusing Capital On The Long Term. The company’s founding FCLT Global are BlackRock, Canada Pension Plan Investment Board, DOW, McKinsey & Company, and the Tata group.

Other leaders such as Damon Silvers from America’s unions have urged the government of the United States, through a detailed report, to make it easier for companies “to think in the long-term by investing in infrastructure and changing both the tax code and corporate governance laws” (Semuels, 2016).

The United Kingdom’s Financial Conduct Authority has taken a step in the right direction, after they came to realize this in the end of 2014 where they erased “the rule requiring public firms to release interim management statements, as part of the Government’s push to encourage more long-term thinking in the stock markets” (Dakers, 2014). However, there is still way to go before this is a mentality widely adapted, but there are, as shown above, examples of companies, investors, and stakeholders moving in the direction of long-term thinking. Some scholars also agree that there should be a change in this sentiment, as it is argued “that the essence of stakeholder management should be the firm’s participation in creating and sustaining moral relationships or the firm’s fulfilling its affirmative duty to stakeholders in terms of fairly distributing the harms and benefits of the firm’s actions” (Mitchell, Agle, & Wood, 1997, s. 857).

In the searching of how companies can adopt long-term thinking this project looks at an asset class that, almost exclusively, manages with a long-term sight in mind. This alternative asset class, private equity, is quite special in that regard, as it usually ignores the short-term view completely, why private equity maybe can be used to come up with plausible solution to the short-termism. Private equity is interesting because it manages their portfolio businesses like no other type of investment. Jensen (1989) argues that private equity firms apply financial, governance, and operational engineering to their portfolio companies, and, in so doing, improve firm operations and create economic value. In addition to all this, empirical evidence suggests that the investment behaviour and ways of management that the private equity industry employ creates value for both society and stakeholders (Kaplan & Strömberg, 2008) (Ljungqvist & Richardson, 2003). How the creation of economic value in a long-term sustainable way happens is what this thesis will try to decipher and afterwards give suggestions on how to apply this to both private as well as public companies.

Private Equity Introduction:

In short private equity is an asset class, that is a possible investment method for both institutional investors as well as wealthy individuals. The objective is to get excessive returns through a different method than the stock market. Generally, one can talk about three different types of investment approaches within this field, of which this project will only focus on one. These three investment approaches are Private Equity Funds, Venture Capitalists, and Angel Investors. Private Equity and Venture Capital are the two with the highest amount of similarities, as they have the same goals for profit and only invests when they can see a working business plan. However, private equity is a type of investment fund that invests in or buyout rather mature companies and then try to flip the companies within a period of 3-7 years after tinkering with them e.g. strategically, and financially. “This is distinct from venture capital (VC) firms that typically invest in young or emerging companies, and typically do not obtain majority control of the invested company” (Kaplan & Strömberg, 2008, s. 2). Another rather interesting distinction is described by Ljungqvist and Richardson (2003, s. 1), as “relative to other asset classes, private equity investments are illiquid, in the sense that there is no active secondary market for such investments, investors have little control over how the capital is invested, and the investment profile covers a long horizon” (Ljungqvist & Richardson, 2003, s. 1). Being illiquid it is also hard to evaluate how much an investment is worth in short-term, thus making it harder to evaluate short-term profits.

Private equity is a rather secretive field of business. This has the implication that there is not much info about them in the publics frame of mind and focus in the world of business and academic world. Scarce information has had the implication that not much has been done in the case of exploring private equity. The lack of knowledge has made it increasingly interesting to investigate closer but at the same time also a hindrance in investigating it copiously. There are several reasons, as to why there is not much general knowledge about the field of private equity, however, two explanations stand out. It is still a rather new phenomenon only dating back to the 1980s, where leveraged buyouts first emerged (Kaplan & Strömberg, 2008, s. 2). The other reasons being that private equity is a bit of a closed circle. Implicating that that it is both hard to get into the world of private equity, as well as get information from the private equity funds. This can also be seen further down in the literature review, where a lot of studies rely on the individual private equity funds self-reported data with no chance of confirming whether the stated data sets happen to be true or not.

However, the way private equity companies manage their portfolio companies with a long investment horizon are interesting when looking towards solving the issue of short-termism in companies, investors, and stakeholders. It could be a possible way of going about the problematic subject, and could be a breath of fresh air and furthermore to solve difficult topics it is sometimes necessary to step outside of the box.

Motivation:

There are immense motivating factors behind this project both for me personally as well as professionally. How a business efficiently can conduct practice both taking investors, stakeholders, society into consideration is interesting.

I firmly believe that there is another route other than focusing on short-term profits, which previously explained can be harmful to both society along with stakeholders. Drawing inspiration from private equity makes the perfect combination for me, as I find the subject of private equity exciting after hearing about the alternative asset form both throughout the bachelor in economics and business administration and the course on transnational business strategies in a legal and financial perspective during the master's degree.

What really interests me regarding private equity is how they contribute to the business they invest in and how they do it. They, in a lot of cases, contribute to their investments and try to add value to the portfolio businesses in different regards. How they influence and tinker with the business for long-term results could be a key contributor to solving the problem of short-termism in society, companies, and stakeholders.

Furthermore, it is revolving around the fields that interest me the most. The field of business, strategy and private equity. It is topics I could see myself take part of in my future career and with a project like this it should be possible to come to a better understanding both for strategy formulation, business execution, long-term thinking strategic wise as well as of what private equity is, how they operate, and what the tricks of the trade are.

Problem formulation:

The introduction has led to investigating the following problem formulation:

How can the unique mid- and long-term thinking of private equity businesses mitigate business short-termism?

- **Research Question 1: What is the uniqueness of business practice of private equity funds?**

- **Research Question 2: What are the specifics of the strategical, financial, and managerial management of private equity portfolio companies?**

- **Research Question 3: What are the strategical and financial tools used by private equity which can inform non-private equity firms and what are the benefits and weaknesses of the proposed tools?**

- **Research Question 4: What are the drivers of short-termism in other types of firms?**

- **Research Question 5: What can non-private equity firms learn from these practices and tools to mitigate short-termism?**

Through these research questions it should be possible to come forth to an understanding of how private equity operate on a long-term basis and maybe even come forth to an understanding that can mitigate short-term thinking in non-private equity firms making for a more sustainable future for both companies and society.

Structure of the project:

The guideline of the flow of the project is shown below:

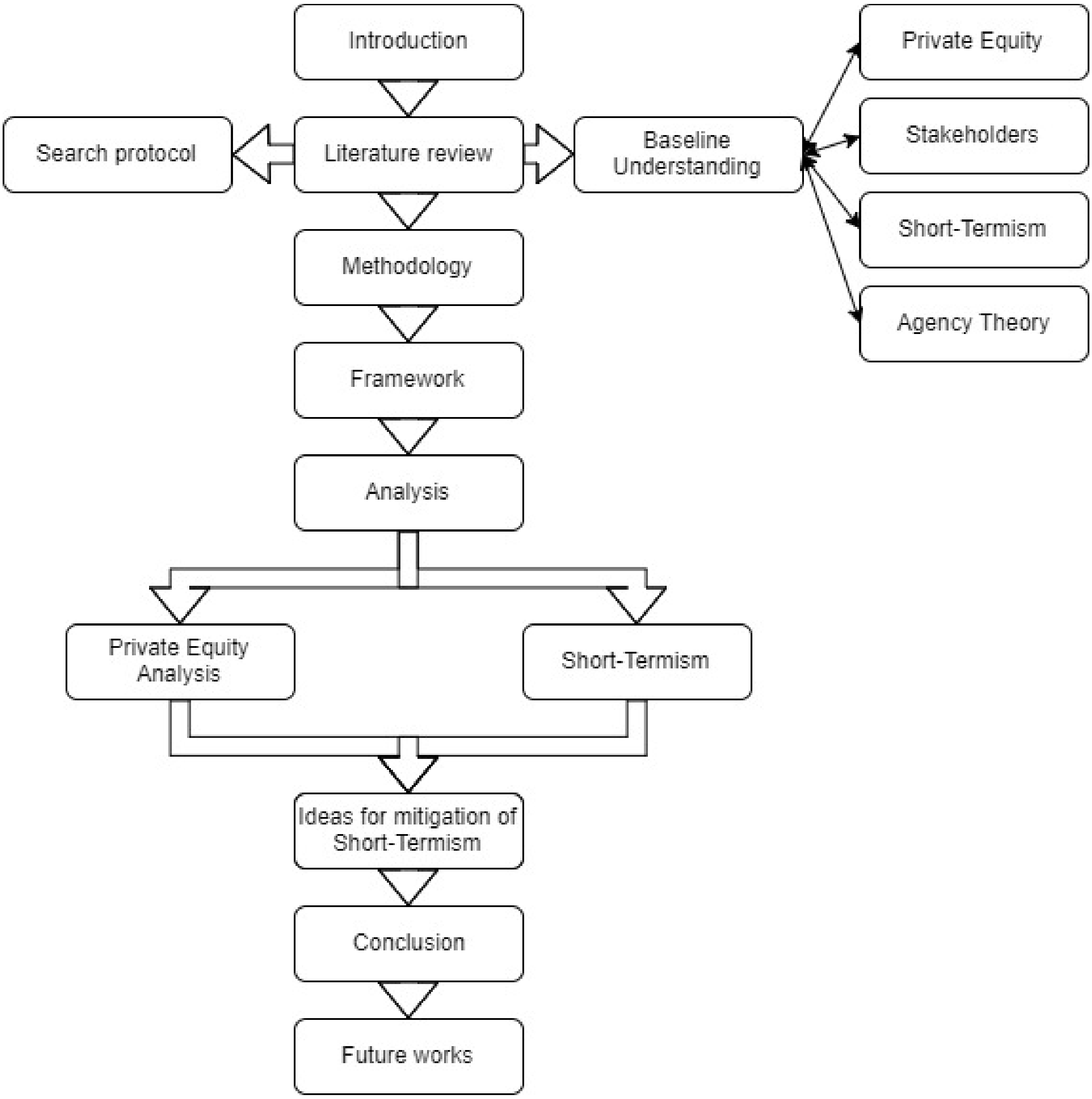

Figure 1 - Project Structure Source: Own Creation

Chapter 2 – Preunderstanding & Literature Review:

This chapter will contain the researchers' preunderstanding and what is previously known about the research topic. This includes reflections upon my preunderstanding as well as the process of a thematic literature review upon topics deemed necessary to understand before the analysis. So, preunderstanding and literature review serves as a starting point for both the author and reader to get a grasp of the preceding knowledge in the area.

Preunderstanding:

Preunderstanding is once own preconceived understanding of a subject. The importance of understanding this is because it influences ones' approach to the subject at hand. This is also supported by (Gummesson, 2000) in his book where he states preunderstanding as per "People's insights into a specific problem and social environment before they start". It derives from previous experiences of a person, both professionally as well as personally.

Prior to going through with this endeavour, I did not have much experience with the term of short-termism, which is involved of a rather big part of the corporate world and investment community. All the experience, although limited, I had originated from educational experiences and learnings, the fact I am interested in investing, and my work experiences.

Strategy has always been a big focus point both throughout the bachelor as well as the master but strategy in the courses has usually been utilizing previously known strategies and applying them to a business model. This project is new for me, as it consists of coming up with a new concept of strategy aiming at transforming businesses from a short-term focus to a more mid-term and long-term focus. Private Equity is a not a business area there has been much focus on during the education either, as we have only touched briefly upon in it finance, which makes it very interesting to investigate and learn from especially regarding strategy where they usually slide under the radar seeing how their business is run. My interest in investing certainly helps.

My relevant work experiences include a short-term search engine optimization project for an e-commerce store where I came to see how much focus were on getting immediate progress and not so much in the formulation of a strategy that would secure the business in five to ten years' time. However, this might also come down to the nature of the harsh competition between e-commerce stores around the world where 'Bigger is better' has been the mantra for quite some time.

Another relevant work experience includes my internship position during the ninth semester at an executive search firm, more acknowledged in public minds as a headhunting company, in Hong Kong. I spent close to four months with the company where I came to learn that focus was mostly the current year. The market had moved very slow for the companies they were attached to, thus making them more desperate to come up with short-term ways of contributing to the year's results. However, the problem could possibly have been mitigated with due care, which is also why the internship project evolved around developing a strategy to keep them one step ahead of their competitors and through the offering of additional value to customers would retain and get more clients in the long run.

So, all in all, both educational experiences as well as practical experiences have inspired me to confront the problem of short-termism.

Thematic literature review:

Bryman and Bell (2015) describes a literature review as a “critical examination of existing research relating to the phenomena of interest and relevant theoretical ideas” (Bryman & Bell, 2015, s. 14). In this case, the phenomena of interest have already been hinted throughout the introduction and problem formulation, which has been used to select some keywords for conducting the actual gathering of the necessary existing research to investigate the phenomena. To narrow down and make the literature manageable on the given space the way of a thematic literature review is chosen rather than the other type of literature review being systematic literature review. This is also possible, as the research area is already known to some degree where the goal of a systematic literature review is to find gaps in the existing research to build ones’ project around (Bryman & Bell, 2015) (Kuada, 2014).

Several databases were tested and utilized in the process to find an adequate number of applicable academic research journals. This included but were not limited to Google Scholar, Scopus, Research Gate, and ProQuest. However, this also means that the process of explaining the number of articles found throughout the process and how many articles have been discarded through the process is not that easy to assess. Furthermore, not only one search was conducted, as could be the case if only one specific subject were to be investigated. However, rather a plethora of searches on different databases resulted in the chosen literature. This also brings a high level of subjectivity to the selection process however, which might end up skewing the literature review. Ideally this would not be a problem, as on some subjects with scarce or limited literature it is possible to contemplate almost if not all previously existing literature.

For the investigation of the problem formulation several areas need to be addressed in the thematic literature review. One of the vital areas to investigate is private equity, how it works as a business to understand it, as a basis for the analysis and an inspiration for a possible solution to the problem formulation. Other vital areas include agency theory and short-termism. Furthermore, one of the reasons the short-term thinking exists is because of stakeholders valuing it. These areas should be able to give information on how the private equity business is unique in the way they think as well as the building blocks for strategy and stakeholders. The search terms are therefore chosen from these topics with terms that are related directly or indirectly to them.

The thematic literature review builds on papers collected through the following search strings used in various combinations on various academic databases, though ProQuest has been the primary contributor with its vast collection of papers, through e.g.: “Private Equity”, “Management”, “Governance”, “Performance”, “Strategy”, “Strategy Formulation”, “Investment”, “Investing”, “Finance”, “Business Model”, “Agency”, “Stakeholders”, “Agency Costs”, “Short-Term”, “Short-termism”, “Mid-Term”, “Long-Sighted”, and “Long-Term”.

An example of a used search string could be (“Private Equity” AND “Performance”) AND (“Performance Management” OR “Performance”) AND (“Mid-Term” OR “Midterm” OR “Long-Term” OR “Long term” OR “Long-Sighted”). The found papers were then screened based on title and abstracts. However, this also leaves a margin for error that some papers might be e.g. accidently left out or undiscovered in the search process. Though, it was still seen as the most suitable way to conduct the compilation of papers.

After conducting the searches and reading the chosen papers there were some papers using interesting sources, which after further investigation also got included in the literature review. One might call some of the collected papers in the literature review admitted through a 'snowball literature review'. Named after the data collection method 'snowball sampling'. While this might not be true to academic ways papers improving the literature review should not be left out.

To gain an overview of the chosen articles they will be analysed to get an overview which type of paper it is, when it origins, what is being researched, which theories are being applied, what major findings the paper brings forth, and which methodology is used. The table of the chosen articles can be found after the literature review of the chosen topics.

Private Equity:

The first topic that will be touched upon in the thematic literature review is that of private equity. All topics involving or necessary to understand the phenomena will be grouped here. The first section of the thematic literature review about the private equity firms will give a general understanding of what they are and how they work. This is necessary as a basis for figuring out the uniqueness of the private equity firms in the analysis.

Private Equity - Funds:

As it has already been stated in the introduction private equity in short is an asset class, that is a possible investment method for both institutional investors as well as wealthy individuals. The objective is to get excessive returns through a different method than its counterpart, the public equity market, where the most commonly known type is the stock market.

The private equity funds are usually rather small in manpower compared to the capital and investments they make and manage. In Jensen' (1989) survey of seven large leveraged buyout partnerships, he found an average of 13 investment professionals, who tended to come from an investment banking background. Today, the large private equity firms are considerably larger, although they are still small relative to the firms in which they invest. Another change is that private equity firms now appear to employ professionals with a wider variety of skills and experience than was true 20 years ago (Jensen M. , 1989) (Kaplan & Strömberg, 2008).

From a legal standpoint, the private equity funds are organized as limited partnerships in which the general partners manage the fund and the limited partners provide most of the capital. However, there are also cases where the private equity firm is arranged as a limited liability corporation (Kaplan & Strömberg, 2008, s. 4). The typical governance structure of a private equity fund will look like the figure shown below 'Figure 1 – Depiction of a Typical Private Equity Fund's Governance Structure', where Limited Partners, the investors of the private equity fund, is shorted as LP, General Partners, shorted as GP, managers the private equity fund, and, the A-E representing the companies of which the general partners invest:

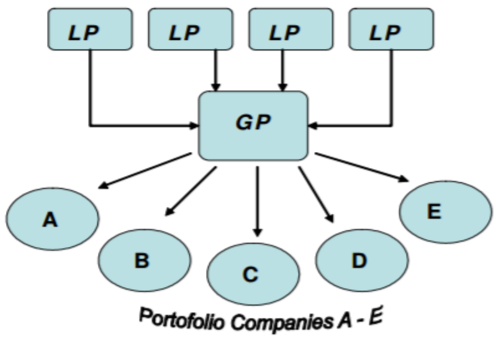

Figure 2 - Depiction of a Typical Private Equity Fund's Governance Structure (Harris, 2012)

The limited partners typically include institutional investors, such as corporate and public pension funds, endowments, and insurance companies, as well as wealthy individuals. It is a very beneficial investment form for e.g. insurance companies and pension funds, as they have very long investment horizons compared to the average investor.

The fund usually has a fixed life, usually ten years, but can be extended for up to three additional years. It takes quite some time for the committed capital to be invested. After committing their capital, the limited partners have little say in how the general partner deploys the investment funds, if the basic covenants of the fund agreement are followed. Common terms include limitations on how much fund capital can be invested in a single company, the types of securities a fund can invest in, and restrictions on debt at the fund level, where there previously has been an influx of gearing the capital committed to investing (as opposed to borrowing at the portfolio company level, which is unrestricted). Additionally, this is also a fact that sets private equity funds apart from hedge funds that typically gear on a fund level where private equity rather tailor the gearing to the individual investment level. Restrictions on gearing helps mitigate becoming insolvent also known as the bankruptcy in investing (Kaplan & Strömberg, 2008, s. 4-6) (Gilligan & Wright, 2014, s. 13-22).

Most private equity firm raises equity capital through a private equity fund. Most private equity funds are “closed-end” vehicles in which investors commit to provide a certain amount of money to pay for investments in companies as well as management fees to the private equity firm. In most cases the managers or the private equity firm also provide a small portion of the cumulative capital committed (Kaplan & Strömberg, 2008, s. 4).

Nominal dollars committed each year to U.S. private equity funds have increased exponentially since the beginning of the phenomenon. It has increased from a mere 0.2 billion $ in 1980 to over 200 billion $ in 2007. During the past 25 years (1979-2004), over $ 1 trillion has passed through the hands of private equity funds (Kaplan & Strömberg, 2008, s. 7) (Lerner, Hardymon, & Leamon, 2004).

Kaplan and Strömberg (2008) shows that the commitment is cyclical, through their figure 1, as capital commitments increase in 1980s, decline in early 1990s, increase late 1990s, decline in early 00s. By 2006 and 2007, private equity commitments appear high by historical standards, exceeding one percent of the value of the U.S. stock market. Phalippou and Gottschalg (2006) also indicate this and shows private equity as an increasingly attractive investment form throughout its short span as a concept, as more money and more funds were raised between 1994 and 2000 than between 1980 and 1993 (when their’ in-sample funds were raised). The patterns documented in private equity fundraising are mirrored in overall buyout transaction activity. There is a similar cyclicality in fundraising and transactions (Kaplan & Strömberg, 2008, s. 8).

Bratton (2008) gives an example of a typical firm that private equity funds are on the lookout for. “Assume that Buyout Firm X is looking at two firms, A and B, as potential buyout candidates. Firm A has an excellent management team and low leverage, but is a value stock—its steady but dowdy industry does not enjoy investor favour. Firm B, also with low leverage, is an underperformer in a more glamorous industry due to a substandard management team and business plan. As between the two, which is the better buyout candidate? Agency theory, read together with the EMH, signals Firm B over Firm A. If the managers are good and the stock price is right, Firm A holds out no value. Meanwhile, Firm B holds out a disciplinary arbitrage profit. In the buyout world, in contrast, Firm A is the quintessential target. Private equity firms look for value, which exists in cases of pronounced inequality between market capitalization and fundamental value. At the same time, because the control transfer comes on friendly terms and the managers take equity stakes, manifest problems with the top team make for value-reducing frictions. Finally, value enhancement does not necessarily imply basic changes in the business plan. The leverage can do the heavy lifting in generating positive returns." (Bratton, 2008, s. 520).

Private Equity – The leveraged buyout phenomenon:

Leveraged buyouts first emerged as an important phenomenon in the 1980s. In a leveraged buyout, a company is acquired by a specialized investment firm using a relatively small portion of equity and a relatively large portion of outside debt financing. In a typical leveraged buyout transaction, the private equity firm buys majority control of an existing mature firm (Kaplan & Strömberg, 2008, s. 2). The leverage is one of the primary reasons private equity came to be. "To see the importance of leverage, assume a buyout target with $1 billion enterprise value and $700 million of debt in its post-buyout capital structure. If the company is sold in five years in a $1.3 billion public offering, the annual growth of the value of the firm is 6 percent over the initial $1 billion. Any number of factors can contribute to that 6 percent value enhancement. Certainly, firm-specific management improvements will help. Even so, a $1.3 billion IPO yield could be due entirely to growth in the economy, a stock market more inclined to favour the firm's industry, or the tax advantages attending the buyout debt. Whatever the source of the gain, the value of the equity investment will have doubled— as a result of the leverage, it will show a 15 percent annual rate of return rather than a 6 percent return." (Bratton, 2008, s. 520) However, with such high leverage comes high risk and an enterprise value of $850 million at the end of the five-year period, without debt payments, implies a 50 percent loss on the private equity investment (Bratton, 2008, s. 520-521).

As leveraged buyout activity increased in the decade, Jensen (1989), as mentioned in the introduction, predicted that the leveraged buyout organizations would eventually become the dominant corporate organizational form. His argument was that the private equity firm itself combined concentrated ownership stakes in its portfolio companies, high-powered incentives for the private equity professionals, and a lean, efficient organization with minimal overhead costs. The private equity firm would then apply performance-based managerial compensation, highly leveraged capital structures, and active governance to the companies in which it invested. According to Jensen (1989), these structures were superior to those of the typical public corporation with dispersed shareholders, low leverage, and a weak corporate governance (Jensen M. , 1989) (Kaplan & Strömberg, 2008).

The typical private equity transaction completes as follows, the private equity firm agrees to buy a company. If company is public, the private equity firm typically pays a premium of 15 to 50 percent over the current stock price. The buyout is typically financed with anywhere from 60 to 90 percent debt – hence the term, leveraged buyout. The first buyout wave during the late 1980s was primarily a U.S., Canadian, and to a smaller extent a U.K., phenomenon. From 1985-89, these three countries accounted for 89 percent of the worldwide leverage buyout transactions and 93 percent of the worldwide value of these transactions. At this time, the leveraged buyout business was dominated by acquisitions of relatively large companies, in mature industries (such as manufacturing and retail), and public-to-private research deals accounted for almost half of the value of private equity transactions (Bargeron, Schlingemann, Stulz, & Zutter, 2007) (Kaplan S. N., 1989) (Kaplan & Strömberg, 2008, s. 5-10).

As the early private equity research studied the deals of the first buyout wave, these transactions helped form the perception of private equity for years to come: leveraged buyouts equal going private transactions of large firms in mature industries. However, in the following years middle market buyouts of non-publicly traded firms grew significantly and accounted for the bulk of private equity activity during the fall of the junk bond market in the late 1980s (Kaplan & Strömberg, 2008, s. 9). The leveraged buyouts were primarily happening in the United States in the beginning. Though, the buyout phenomenon also spread rapidly to continental Europe and even happened to surpass the United States in value in some years. In the 2000-2004 period, the western European private equity market (including the United Kingdom had 48.9 percent of the total value of worldwide leveraged buyout transactions, compared with 43.7 percent in the United States (Kaplan & Strömberg, 2008, s. 10).

Private Equity – Difference from others:

Private equity is an alternative asset class. The alternative asset classes, meaning other classes than public equity, that have the most in common with private equity is venture capital and angel investors. Each of these asset classes has “its own set of goals, preferences, and investment strategies, yet each providing working capital to the target firm to nurture expansion, new product development, or restructuring of the firms’ operations, management, or ownership” (PrivCo Knowledge Bank, 2017). A note that differentiates the alternative asset classes from e.g. public equity is that relative to other asset classes, private equity investments are illiquid, in the sense that there is no active secondary market for such investments, investors have little control over how the capital is invested, and the investment profile covers a long horizon (Ljungqvist & Richardson, 2003, s. 1). The way private equity funds are distinct from venture capital (VC) firms and business angels is that venture capitalists and business angels typically invest in young or emerging companies, and typically do not obtain majority control. An illustration of the alternative asset classes compared to when they invest in a company is displayed below:

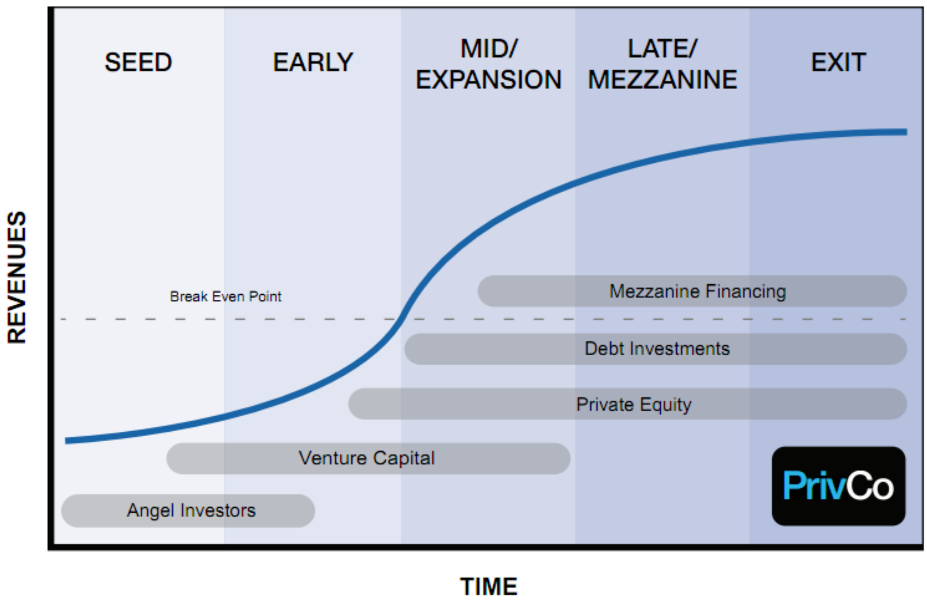

Figure 3 - The Private Company Life-Cycle (PrivCo Knowledge Bank, 2017)

As it can be seen business angels, also known as angel investors, invest early in the company, also known as the seed stage. Venture capital is primarily based on the early stage but can also be found in the seed stage as well as the mid stage. Private Equity invest primarily in the mid-stage as well as in mature companies in the late stage but can also in rare situations be found in the early stage. Debt financing is an investment form that private equity companies employ and leverage in the invested company' assets. Mezzanine finance, which this paper will not focus on, is an investment form primarily in the late stage already mature companies, that will often lead to an exit. The unique part about mezzanine financing is that they do not tend to get security in the assets but rather in stakes of equity of the company.

However, in several datasets there is no distinction between venture capital and private equity funds, which is a problem when trying to give an overview of private equity funds (Kaplan & Strömberg, 2008, s. 2). Ljungqvist and Richardson (2003, s. 7) reports that in their data, that for the entire period from 1981 to 2001, a quarter of funds, representing 14.8 % of fund capital, are venture funds. This differs quite a lot from the universe of funds tracked by Venture Economics, where venture funds account for 74.6 % of funds by number and 41.5 % by capital. Their dataset therefore suggests that their limited partners invests disproportionately in private equity (primarily buyout) funds. However, it is hard to differentiate how much is going to venture capital funds and private equity funds, even though there is a difference between these two types of funds. The data is still going to be used anyways, as it is the only viable data on the subject but it creates some uncertainty about the results of the studies on private equity.

Private Equity – Horizon:

As mentioned in the section around private equity firms is a type of investment with a long investment horizon. The private equity firm typically has up to five years to invest the capital committed to the fund into companies, and then an added five to eight years to return the committed capital to its limited partners (Kaplan & Strömberg, 2008, s. 4-5).

The private equity firms are rather keen on waiting for profitable investments to create value in one way or the other. Ljungqvist and Richardson (2003) reports that 16 % of committed capital is invested at the end of the first year, while Phalippou and Gottschalg (2006) find something similar in their data. The fee payment at the end of the first year is thus as high as 12.5 % of the amount invested. During the following years, the invested amount slowly increases where after 5 years about 80 % of the capital has been invested, thus reducing the management fees to about 2.5 % (Phalippou & Gottschalg, 2006, s. 30-31). Li, Davis, Kinniry and Wicas (2004, s. 27-34) reports that it takes approximately five to six years to for the private equity funds to invest all the committed capital. Although, Li, Davis, Kinniry and Wicas (2004, s. 27-34) do not report the exact same as (Phalippou & Gottschalg, 2006) and (Ljungqvist & Richardson, 2003) it is possible to fathom the picture.

Recently private equity firms have been willing to sell after a couple of years of ownership if the right offer came along. Historically however, accounting for secondary buyouts, Strömberg (2008) shows that the median LBO is still in private equity ownership nine years after the original buyout transaction. In comparison, Kaplan (1991) found the median leveraged buyout target remained in private ownership for 6.82 years, which is consistent with privately-owned holding periods having increased since the 1980s (Kaplan & Strömberg, 2008, s. 12).

That means the median investment horizon is anywhere between 1-5 years for the private equity firm to invest the capital and 5-9 years to realize the investment. However, there is bound to outliers in both ends where the investment can be liquidated in a short span after investment. To sum it up the investment horizon varies quite a bit depending on the individual investments (Strömberg, 2008) (Kaplan S. N., 1991).

Private Equity – Exit of Investments:

Above the motive for the private equity funds have been explain and what sets them apart from others. Additionally, it has been investigated how long they hold onto investments but there is a lack of investigation how they realize the investments.

There are several exit modes for the private equity funds. Conditional on exits, the most common route is the sale of the company to a strategic (i.e. non-financial) buyer; this occurs in 38 % of all exits. The second most common exit route is a sale to another private equity fund in a so-called “secondary leveraged buyout” (24 %); this exit route has increased considerably over time. Initial public offerings, where the company is listed on a public stock exchange (and the private equity firm can subsequently sell its shares in the public market), account for 14 % of the exits; this route has decreased significantly in relative importance over time. The low fraction of initial public offerings does not imply that the growth of private equity has been at the expense of public stock markets, however. Strömberg (2008) shows that for private equity transactions form 1970-2002 period, the fraction of firms eventually going public was 11 %, while only 6 % of these firms were public before the buyout, implying a positive net flow from private to public equity markets. Given the high debt levels involved in these transactions, one might expect a non-trivial fraction to end in bankruptcy. For the total sample, 6 % of deals have ended in bankruptcy or reorganization (Kaplan & Strömberg, 2008, s. 11). Assuming an average holding period of six years, this works out to an annual default rate of 1.2 % per year. This is lower than the average default rate of 1.6 % Moody’s reports for all U.S. corporate bond issuers from 1980-2002, thus showing there is not a higher rate of bankruptcy among companies held by private equity funds (Kaplan & Strömberg, 2008, s. 11).

Recently, private equity funds have been accused of becoming more short-term oriented, preferring to quickly “flip” their investments rather than keeping their ownership of companies to fully realize their value potential. In Kaplan & Strömberg’s (2008, s. 12) analysis, they see no evidence of “quick flips” (i.e. exits within 24 months of investment by private equity fund) becoming more common. On the contrary, holding periods of private equity funds over the 12-, 24-, and 60-month horizons have increased since the 1990s. Overall, only 12 % of deals are exited within 24 months of LBO acquisition date (Kaplan & Strömberg, 2008, s. 12).

With all of this in mind, the few fraction of IPO’s, it is odd that some researchers use the fraction of investments exited through an IPO as an indicator for fund performance, while other use the fraction of either IPO or M&A as an indicator for fund performance, even though it is shown that IPO or M&A is not the only exit mode (Phalippou & Gottschalg, 2006).

Phalippou & Gottschalg (2006) measure on a relationship between cash-flow based performance and exit success with highly statistically significance, where when exit success is shown through the previous defined methods, only IPOs, then the relationship between cash-flow based performance and exit success is much weaker. The use of IPO’s as a factor for performance is also odd, as the data gets skewed heavily towards an optimistic assessment of private equity according to

Li, Davis, Kinniry and Wicas (2004, s. 27-34). They report that through the period of 1985 until June 2002 the average instant return from venture capital IPOs was more than 300 %. It is argued that these returns happen because the companies behind the IPO knows how the stock market works and tend to file for IPOs with greater frequency during periods where the public equity performs rather well.

As, it can be seen above there is a weak link between IPO performance and fund performance in the case of (Phalippou & Gottschalg, 2006), which is why performance will be investigated further in the next section.

Private Equity – Performance:

There are generally two levels upon which the returns are calculated throughout the studies. It is either on the individual investment level or the complete fund level. Several authors have tried, with varying results, in both categories to go about calculating private equity performance, albeit it has proven hard to estimate.

Studies of performance of individual venture capital investments, such as those conducted by Hwang, Quickly and Woodward (2005); Cochrane (2005); Woodward and Hall (2003) have faced the challenge that in the majority of cases only get to watch the performance when the investments are fruitful, meaning the results are biased with less unsuccessful investments, even though those also exists, obviously.

Hwang, Quickly and Woodward (2005); Cochrane (2005); Woodward and Hall (2003) all report different returns with their datasets on individual investments. Hwang, Quigley and Woodward (2005) find gross real returns are like the return of the S&P 500 on venture capital investments. Woodward and Hall (2003) estimate a higher performance of 8.5 % per year. Cochrane (2005) finds a 5.9 % return on IPOs and annual average gross return. However, Cochrane (2005) has no estimates of companies that remain private, which accounts for close to 45 % of his data set, thus creating big uncertainties.

Another type of studies focuses on the funds, where they hereby reduce the sample bias, as both fruitful and unsuccessful investments are included. Though, there is a possibility of several funds being left out of the datasets. Fund level studies include Kaplan and Strömberg (2008); Phalippou and Gottschalg (2006); Gompers and Lerner (1997); Kaplan and Schoar (2005); Ljungqvist and Richardson (2003); Jones and Rhodes-Kropf (2003).

The analyses are not very up to date as some of the newest numbers being just before the financial crisis. However, as of September 2007, Venture Economics reports private equity returns over the previous three years of 15.3 % versus Standard and Poor's 500 stock market returns of 12.7 % (Kaplan & Strömberg, 2008, s. 21-28).

Phalippou and Gottschalg (2006) tries to focus on the overall performance of the private equity asset class, which perhaps is the first time that has been done in the way they do. They report that the average PI goes down to 0,87 after correcting for potential biases, meaning private equity funds have lost 13% of the value invested in present value terms. They show in their paper that private equity performance has been lower than the S&P 500 with up towards -3,8 % per year. However, they speculate, that future performance might differ from that observed in their dataset, as other papers indicate otherwise, such as (Kaplan & Schoar, 2005). The performance analyses are also prone to be affected by what year the data has been gathered in.

Ljungqvist and Richardson (2003) finds that private equity funds generate excess returns over the past two decades, where especially funds between 1981 and 1993 does well with reported rates of return average 19.8 percent, where at the same time the S&P 500 index 'only' reported returns of 14.1.

(Gompers & Lerner, 1997) only investigates a single fund so is therefore very likely to be biased and might not be representable for the rest of the funds, however they find, after examining risk-adjusted performance, a positive performance. Jones and Rhodes-Kropf (2003) reports a positive but not statistically significant alpha. Ljungqvist and Richardson (2003) reports a high average performance, though the results should be treated with thoughtfulness, as their sample is somewhat small and biased towards not including first-time funds and venture funds, both of which according to other scholars such as (Kaplan & Schoar, 2005) perform lower on average than second-time funds. An influence hereof is that there is a higher chance of successful first-time funds to raise a second-time fund (Ljungqvist & Richardson, 2003, s. 6).

That means in short there is still debate upon the question if private equity outperforms the public equity market where it is shown in some cases it does but in others do not. It is also shown in several of the papers that the top funds in private equity outperforms the median heavily while the lowest percentile underperforms heavily. Thus, the median, being the median, do not manage to show the complete picture.

In addition to performance, the evidence also is strong that private equity is subject to boom and bust cycles, which are driven by recent returns as well as by the level of interest rates relative to earnings and stock market values. This seems particularly true for larger public-to-private transactions. Another interesting note is that private equity fund returns tend to decline when more capital is committed to this asset class. Capital commitments to private equity tend to decline when realized returns decline. In other words, the patterns are consistent with a boom and bust cycle in private equity (Kaplan & Strömberg, 2008, s. 21-28).

Private Equity – Risk:

Private equity being different than public equity possess some other types of risks, which scholars have been discussing throughout the lifetime of private equity.

Li, Davis, Kinniry, and Wicas (2004, s. 27-34) also emphasizes that private equity investments are far riskier than public equity investments. However, they mention the fact that through investment vehicles some of these risks can be mitigated. These risks include investment horizon, rigid liquidity constraints, and high bankruptcy rates among the invested companies. Another factor, of which limited partners are not able to do much is the realizing of returns on the investments.

IPO's are filed more frequently during periods where the stock market is doing well, as it is easier to realize a positive return during these periods, thus making it hard to liquidate an investment during times where the public equity market is not doing well. This also makes up for the misconception that private equity is safer, as an investment seeing it is separated from the public equity market. Therefore, Li, Davis, Kinniry, and Wicas (2004, s. 27-34) argues that private equity should not be an alternative asset class but instead as a "unique component of the overall equity market". However, one can make the counter-argument that private equity might wait realizing returns until the stock market is back on track, which helps mitigate the fact that private equity does not fare well if the public equity does not fare well.

Ljungqvist and Richardson (2003, s. 3-23) reports that private equity funds are typically not very well diversified. Their data sample shows that, on average, up towards 40 percent of the fund capital is invested in a single industry. There is not the case in the different types of private equity funds on average, as buyout funds tend to invest in far fewer companies than venture funds.

One way to mitigate risks such as conflict of interest and information risks, according to Li, Davis, Kinniry, and Wicas (2004, s. 27-34) is to properly motivate the general partners, through linking the bulk of partnership compensation to performance. However, this also creates a risk of general partners investing with greater risk than before, as they want to maximize their own returns on the partnership.

Li, Davis, Kinniry, and Wicas (2004) sums up the primary risks of private equity into a few topics:

- Bankruptcy risks
- Liquidity risks
- Reinvestment risks
- Conflict of interests in the partnership and fund
- Information risks (e.g. biased data)
- Tax risks

Private Equity – Economic Value:

One of the key questions to answer is if private equity creates economic value, meaning if they create value for society and its limited partners. The empirical evidence is strong that private equity activity creates economic value on average. Kaplan and Strömberg (2008, s. 28) suspect that the increased investment by private equity firms in operational engineering will ensure that this result continues to hold in the future. Because private equity creates economic value, Kaplan and Strömberg (2008, s. 28) believe that private equity activity has a substantial permanent component (Kaplan & Strömberg, 2008, s. 28).

Another way in which private equity creates economic value is described by Ljungqvist and Richardson (2003), where they focus on private equity as a mediator for reallocating capital to increasingly productive parts of the economy, hence boosting the economy through increased productivity and more effective liquidity allocation (Ljungqvist & Richardson, 2003).

The empirical evidence at the company level suggests that leveraged buyouts by private equity firms create value (adjusted for industry and market). This finding does not necessarily imply, however, that private equity funds earn superior returns for their limited partner investors. Summing up, because private equity firms often purchase firms in competitive auctions or by paying a premium to public shareholders, sellers likely capture a meaningful amount of value, while at the meantime the limited partners earn returns on their investments later (Kaplan & Strömberg, 2008).

However, there are also cases where the private equity companies do not manage to create value for their stakeholders and society as well as cases where they only manage to create value for its stakeholders and society.

In relation to not creating value for both society and limited partners the case of RJR Nabisco can be used. It is probably the most famous of all the leveraged buyouts. The case is about a former big American conglomerate involved in tobacco and food products. It became the biggest private equity deal of the time, as there was a huge bidding war between all private equity firms of the time. Everybody wanted in on the deal, though Kohlberg Kravis managed to secure it. Albeit, it ended up as a very poor investment, as the premium paid for RJR Nabisco, a total deal of $25 billion, ended up being too high for the RJR Nabisco's cashflow to handle when its stock plummeted in early 1990s. Kohlberg Kravis lost $730 million and the conglomerate wound up defuncting in 1999. However, the portfolio of which RJR Nabisco was part of still returned about 10 % adjusted yearly performance (Norris & International Herald Tribune, 2004).

A case where the private equity firm only managed to create value for its limited partners can be found in Bain's investment of $27 million along with other firms to acquire Dade International. Dade International had with Bain in charge burrowed $1.6 billion to make expansions. However, the debt amounted were too much to pay off and the company had to lay off 1700 people and cutting benefits for some workers. In the end, Dade International merged with a German company ultimately shutting down several of its plants in the United States. However, even though it did not fare well for Dade International Bain Capital still got a return of $421 million on its $27 million investment (Barbaro, 2011).

Private Equity – Compensation:

In the previous section the economic impact of private equity for limited partners and society were investigated, however, it was not investigated how the general partners gets compensated, which therefore will be done below.

The private equity firm or general partner is compensated in three ways. Firstly, the general partner earns an annual management fee, which is a percentage of capital committed, and, then, as investments are realized, a percentage of capital employed. Secondly, the general partner earns a share of the profits of the fund, often referred to as "carried interest", that almost always equals 20 percent. Finally, som general partners charge deal fees and monitoring fees to the companies in which they invest. The extent to which these fees are shared with the limited partners is a somewhat contentious issue in private equity fundraising negotiations. A common arrangement is that these fees end up being split 50-50 between general and limited partners (Kaplan & Strömberg, 2008).

Metrick and Yasuda (2007) describe the structure of fees in detail and provide empirical evidence on those fees. Metrick and Yasuda (2007) estimate that fees equal $19 in present value per $100 of capital under management for the median private equity fund.

A skill that is very beneficial for limited partners to have is negation skills. When making contracts about the future investment it demands expertise and experience of having been in such situations before, else the capital contributions and return distributions might end up heavily favoured for the general partners, which is also why about 20 % of the limited partners hire mediators, also frequently identified as gatekeepers. They charge about 1 % of the fund's size in addition to a 5 % to 10 % carried interest. Limited partners who do not hire gatekeepers use quite a lot of time and resources screening potential funds instead (Li, Davis, Kinniry, & Wicas, 2004, s. 27-34) (Phalippou & Gottschalg, 2006, s. 29).

As it could be seen earlier it takes up till 5-6 years before the committed fund capital is invested. Ljungqvist and Richardson (2003) reports that 16 % of committed capital is invested at the end of the first year, while Phalippou and Gottschalg (2006) find something similar in their data. The fee payment at the end of the first year is thus as high as 12.5 % of the amount invested. During the following years, the invested amount slowly increases where after 5 years about 80 % of the capital has been invested, thus reducing the management fees to about 2.5 %. Consequently, while the compensation might seem high in the beginning it evens out over the course of the years of the fund (Phalippou & Gottschalg, 2006, s. 30-31).

Private Equity – Critique of Limited Partners:

As previously mentioned the limited partners are the investors of a private equity fund. The literature is sometimes puzzled why limited partners still participate in private equity, though it is in human nature to be opportunistic when the potential for excessive returns present itself but it can also be done e.g. for tax reasons. Phalippou and Gottschalg (2006) asks the question why investors still provide capital to the private equity asset class, but they speculate that there is a form of mispricing. There are also several things that can go wrong in the performance investigation, which might be a contributing factor to the continued success of private equity. It is a relatively new asset class, where payoffs are highly skewed in relation to investors weighting successful investments higher than unsuccessful ones, which causes investors to blindly participate in some funds. Investors might have a biased view in relation to performance as only the gross-of-fees returns are provided in memorandums and prospectuses used to establish and fundraise. They mention other reasons such as limited opportunity for benchmarking as well. A speculation after investigating the literature of private equity is that the anonymity private equity enjoys possibly gives them a better reputation that than should have. Summing up, different scholars report different returns, which still leads to the an ongoing discussion whether private equity is a feasible investment opportunity or not.

Limited partner's behaviour has also caused trouble in the data sets for the papers. Ljungqvist and Richardson (2003) have trouble with their data set not being representative if the limited partners only invested in follow-on funds by professionals with a proven track record. Though, they explain there are several reasons why limited partners involve in the investment. One reason is obviously to get the highest risk-adjusted return. However, it is also to get the funds to buy the services the limited partners' corporate parents are offering, when we are talking about institutional investors. These services are even more attractive if the fund professionals do not have a proven track record, surprisingly, which helps first-time funds getting an easier start (Ljungqvist & Richardson, 2003, s. 5-7).

Private Equity – Potential biases:

Under the investigation of the literature review about private equity several flaws have been revealed in the data sets or in other regards, which will be addressed in this section. These involve biases such as it is hard to get the complete picture, the transparency of fund data, living dead investments, hidden data, accounting valuations, fund vs. individual level etc. This paper will go into depth with some of them below.

Studies of performance of individual venture capital investments, such as those conducted by Hwang, Quickly and Woodward (2005); Cochrane (2005); Woodward and Hall (2003) have faced the challenge that in the majority of cases only get to watch the performance when the investments are fruitful, meaning the results are biased with less unsuccessful investments, even though they exists. Kaplan and Strömberg (2008) reports the same, as they found one caveat in that not all cases of distress may be recorded in publicly available data sources; some of these cases may be "hidden" in the relatively large fraction of "unknown" exits (11 %).

Another type of studies focuses on the funds, where they hereby reduce the sample bias, as both fruitful and unsuccessful investments are included. Though, there is a possibility of several funds being left out of the datasets. Another problem when focusing on the funds is that it is hard to obtain the right data, in that sense that e.g. Ljungqvist and Richardson (2003) uses data from Thomson Financial's Venture Economics Service (Thomson Reuters, 2017) but even these data sets can be strongly biased, as the data are self-reported from the funds and in addition are based on both realized as well as unrealized investments (Ljungqvist & Richardson, 2003). Li, Davis, Kinniry, and Wicas (2004, s. 27-34) and Bratton (2008) also find that these data can have drawbacks, even though it is the most comprehensive collection of data available. They mention, just like Ljungqvist and Richardson (2003), that the data is self-reported, but also include drawbacks such as that reporting is optional, data do not always include the same fund universe, and historical data are continually revised, as new information emerges. It is important that the data collection report reality as close as possible but that can also make earlier research done with previously reported data obsolete.

Determining which investment is a living-dead and thus which accounting valuation is exaggerated is bound to be a subjective exercise. Phalippou and Gottschalg (2006) argues that it is most reasonable to write-off all residual values of effectively liquidated funds, however it is important to bear in mind that erasing only the most obvious ones and treating as correct the remaining ones would affect average performance only marginally as seen in Phalippou and Gottschalg (2006) data set (Phalippou & Gottschalg, 2006, s. 4).

Standard practice is to weight each fund by the total capital committed. However, the value invested differs from total capital committed as funds do not invest all capital upfront and vary in the speed at which they call capital (Ljungqvist & Richardson, 2003). If poorly performing funds invest more slowly, then capital committed-weighted performance is downward biased (and vice versa). Thus, some scholars weight performance by the present value of the stream of investments throughout the paper (Phalippou & Gottschalg, 2006, s. 4-5).

As it can be seen there are a lot of potential and actual problems in the data sets. When a paper is transparent it is possible to adjust or at least have these problems in mind but sometimes even the papers have troubles adjusting for these. However, this is bound to happen with the lack of transparency private equity funds provide.

Private Equity – Pros and Cons:

Throughout the literature review several points has been touched upon in relation to both pros and cons. In the late 1980s, Jensen (1989) described these organizations as lean, decentralized organizations with relatively few investment professionals and employees (Kaplan & Strömberg, 2008, s. 4). Additionally, Jensen (1989) argues that private equity firms apply financial, governance, and operational engineering to their portfolio companies, and, in so doing, improve firm operations and create economic value (Kaplan & Strömberg, 2008, s. 12). Private equity funds have better access to credit markets because they are repeated borrowers in the market, which enables them to build reputation with lenders. Recent papers by Ivashina and Kovner (2008) and Demiroglu and James (2007) finds that more prominent private equity funds seem to be able to obtain cheaper loans and looser covenants than other lenders. The private equity funds can pick between which project they want to invest and many projects gets discontinued before the investment is made, but that stems from increased competition and requirements (Khan, Vilanova, & Hassairi, 2011). This is only just a few of the advantages private equity has. Generally, the attractiveness of a company can be simplified to some degree in a few bullet points from (Khan, Vilanova, & Hassairi, 2011, s. 496):

- Undervaluation of the going private firms as compared their peers in market.
- Low visibility being illiquidity of their stock and hence low analyst coverage.
- High free cash flows and tax shields issues; and
- High managerial ownership.

Criticisms and scepticism come basically in two different forms. First, some argue that private equity firms take advantage of tax breaks and superior information, but do not create any operational value. Second, some argue that private equity activity is influenced by market timing (and market mispricing) between debt and equity markets (Kaplan & Strömberg, 2008, s. 12). But it can also be in relation to e.g. agency costs, boom and bust cycles (there are both more filing for IPO's and more fundraising going on during times where the economy flourishes, which one can speculate that they cannot manage to create economic value on their own). Because of these cons Li, Davis, Kinniry, and Wicas (2004, s. 27-34) suggests that private equity should be treated as but one small component of a portfolio's allocation to all equity investments, both private and public. However, other scholars report private equity creating economic value. Thus, it is still a topic of contention in academia.

Private Equity – Peculiarities Discovered:

IPO is only the case in 14 % of the exits, whereas I in actuality was led to believe this would be the most popular option e.g. from reading about private equity randomly in newspapers or hearing about it during classes.

It is rather troublesome to find quality papers in scientific journals on the subject, however there are quite a few papers work in progress - working papers reaching there and university works. Meaning, that currently bigger amount of data from more unconventional places in the academic community, however, the authors are still authorities on the subject, such as Kaplan and Strömberg. Several of the articles make cross-references to one another putting forth an improved validation of the working papers.

A problem, which has also been mentioned previously, is that often there is made no distinction between venture capital and private equity, which also have made the literature review quite hard to perform. This is also because private equity can have various definitions. The best example of how different these definitions can be being that one describes the opposite of public equity while the other describes the asset class using leveraged buyout in relatively mature companies.

There are fewer bankruptcies among private equity owned companies compared to public equity companies. Assuming an average holding period of six years, this works out to an annual default rate of 1.2 % per year. This is lower than the average default rate of 1.6 % Moody's reports for all U.S. corporate bond issuers from 1980-2002, thus showing there is not a higher rate of bankruptcy among companies held by private equity funds (Hamilton, Varma, Ou, & Cantor, 2005) (Kaplan & Strömberg, 2008, s. 11). However, these data might not have been adjusted if the company goes bankrupt after the private equity ownership, gets acquired or defunct, as the case was with e.g.

RJR Nabisco, and Dade International (Barbaro, 2011) (Norris & International Herald Tribune, 2004).

Stakeholders:

Stakeholders are an important subject when it comes to the business world. A company always should look after different stakeholder's interests and how decisions affect the different stakeholders. Stakeholders can also influence the company and how it is run with various goals in mind. It is argued that one of the reasons for e.g. short-termism is because some stakeholders in the company want a big payoff in the short run, which could be seen in the previously given Unilever example where Unilever took the position of not releasing profit figures in 2009 stating that they were a distraction and only attracted short-term investors (Dakers, 2014) (Ernst & Young, 2014) (McKinsey Global Institute, 2017). The stock market was not thrilled with the announcement to say the least shaving 22 % of the Unilever's stock price (Semuels, 2016). Therefore, it is important to define and understand the term stakeholder and furthermore figure the capabilities out for each stakeholder regarding e.g. Power, Legitimacy, and Urgency (Mitchell, Agle, & Wood, 1997).

A stakeholder can be defined in a variety of ways. Generally, the literature distinguishes between a broad or narrow view and a public affairs approach and a social responsibility approach. This paper will use the broader definition of Applegate (2008, s. 1) and Freeman (1984), where they put it as: "A stakeholder is any person, group, or organisational unit that will be influenced by (or will influence the actions you take to accomplish your goals" (Applegate, 2008, s. 1), and "A stakeholder in an organisation is (by definition) any group or individual who can affect or is affected by the achievement of an organisation's objectives" (Freeman, 1984). Albeit, there is more clarity upon what and who a stakeholder can be. "There is not much disagreement on what kind of entity can be a stakeholder. Persons, groups, neighbourhoods, organizations, organisations, institutions, societies, and even the natural environment are generally thought to qualify as actual or potential stakeholders." (Mitchell, Agle, & Wood, 1997, s. 855).

Kenny (2014) has a remark on the importance of identifying the stakeholders: "It is truly an important task, as with resources being limited an organization cannot do everything for everyone" (Kenny, 2014). The problem of giving priority to competing stakeholders claim are coined stakeholder salience. This means, that even though all stakeholders in some regard is important it is truly important to know how to categorise or rate these stakeholders in relation to factors such as e.g. urgency, importance, and power (Mitchell, Agle, & Wood, 1997). Getting to know which relationships to value etc. puts forth a goal on the horizon for a business.

It should furthermore also be considered on what level the analysis will take place, e.g. if it be local, regional, or global, and if it tackles specific topics or broader topics. This process takes place after deciding whether the paper should opt for either a reconstructive approach or analytical approach. A reconstructive approach means going from the bottom up and allows for parameters to be defined by the stakeholders themselves, which is a good way of conducting an analysis if it is possible to reach out to the applicable stakeholders. An analytical categorization means going from the top down, which means moving from the higher levels in the business and categorizing based on these views. This however means, that it is hard to get the valuable information from the bottom of organizations or stakeholders own opinions upon categorizations and parameters. In addition, it is important to note whether the stakeholders identified are external or internal (Reed, et al., 2009).

The literature proposes several ways of going about making a stakeholder analysis. Several are widely applicable, as there for e.g. were a vagueness in the early definition of what a stakeholder is. This paper will go into depth with two proposed frameworks of which one will later be applied and not so much in the definition of stakeholders, as it is deemed those already established by scholars, who are authorities about stakeholders are appropriate. The frameworks, which will be the focus points, are made by (Eden & Ackermann, 1998) and (Mitchell, Agle, & Wood, 1997).

(Eden & Ackermann, 1998) proposes a framework involving a categorisation of stakeholders in four different key groups duly named: 'Key Players', 'Context Setters', 'Subjects', and 'Crowd'.

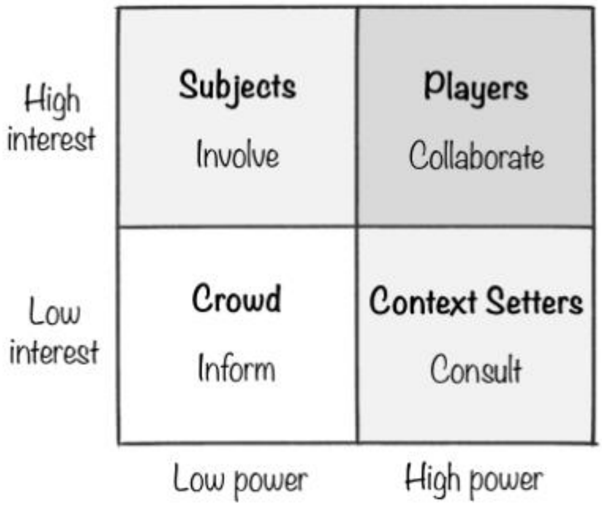

Figure 4 - Stakeholder Analysis *(Eden & Ackermann, 1998)*

Examples are giving in the parenthesises. Stakeholders, that should be actively paid attention to and groomed are key players (Owners, Customers, Employees etc.), as they have high influence and power. Context setters (Trade Unions, Government, Trade Associations etc.) lack the interest but has power, whereas they should be monitored and managed. Subjects (Interest Groups, Media etc.) has high interests but lack the influence, meaning they can be helpful but do not necessarily offer much in terms of getting to the goal but they can make alliances with other stakeholders e.g. Crowd (e.g. Academic Institutions) possesses both low interest as well as power making them not very useful. However, this framework seems quite simple when compared to (Mitchell, Agle, & Wood, 1997), as they incorporate other features into the equitation establishing a more thorough analysis.

Mitchell, Agle, & Wood (1997) has managed to come up with a framework involving supplementary factors making it more widely applicable, which is also why this paper will put more focus on (Mitchell, Agle, & Wood, 1997) paper.

The basis for the framework was the need for a theory of stakeholder identification that can reliably sort non-stakeholders from actual stakeholders. The factors they investigate closer in a theory of stakeholder identification and salience is based on stakeholders' possession of "one or more of three relationship attributes: Power, Legitimacy, and Urgency. By combining these attributes, we generate a typology of stakeholders, propositions concerning their salience to managers of the firm, and research and management implications" (Mitchell, Agle, & Wood, 1997, s. 853). When mentioning power, the stakeholder's power to influence the firm is investigated. When mentioning legitimacy, the stakeholder's relationship with the firm is looked at. When mentioning urgency, the stakeholder's claim on the firm is examined (Mitchell, Agle, & Wood, 1997).

To investigate the framework closer, it is first necessary to define what a stake in a firm is though. Savage, Nix, Whitehead, and Blair (1991) argue that a stakeholder needs to have two attributes in both a claim in the firm as well as the ability to influence the firm. Other scholars, like Brenner (1993) argue that only one of the previously stated needs must be fulfilled. However, in Mitchell, Agle, and Wood (1997) argue that their influencers could have power over the firm, whether or not they have valid claims or any claims at all and whether or not they wish to press their claims. Therefore, claimants may have legitimate claims or illegitimate ones, and they may or may not have any power to influence the firm. In addition, Mitchell, Agle, and Wood (1997) also manages to include potential relationships with stakeholders that in other theories are forgotten, as there might not be an actual relationship currently. This view makes the model more universally applicable than that of e.g. Eden and Ackermann's (1998) stakeholder analysis, as it tries to cope with all known and unknown both current as well as potential stakeholders.

Three important factors have been identified in the evaluation of stakeholders. Power, Urgency, and Legitimacy. Mitchell, Agle, and Wood (1997, s. 863) shows that they are both vital factors individually as well as in combination. These factors are also something that has been put great importance to in other topics of the literature: Agency Theory, Resource Dependence Theory, and Transaction Cost Theory. Organizational theories and population ecology theory links legitimacy of stakeholders closely to organizational survival. All these theories also involve the last factor which is urgency. Its dealt with in relation to contribution to costs and in terms of the outside and inside pressure on the firm (Mitchell, Agle, & Wood, 1997).

The three factors have evolved during the years but scholars have come with quite proper definitions, which is the following. Power is "the probability that one actor within a social relationship would be in a position to carry out his own will despite resistance" (Weber, 1947). Legitimacy is "a generalized perception or assumption that the actions of an entity are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs, and definitions" (Suchman, 1995, s. 574). Urgency is defined by Merriam-Webster Dictionary as "calling for immediate attention" or "pressing". It is about dealing with the stakeholder with regards to time sensitivity in relation to criticality; criticality could be factors such as ownership, sentiment, expectation, and exposure (Mitchell, Agle, & Wood, 1997, s. 867-868). Furthermore, Mitchell, Agle, and Wood (1997) explains that stakeholder attributes are variable and constantly shifts. Stakeholder attributes are socially constructed entities, that, just like all other socially constructed entities, are not objective. Consciousness and wilful exercises can or cannot make the stakeholders attributes change.

Stakeholders make up a firm and therefore it is important to pay attention to the previously mentioned points such as who stakeholders are and their attributes. The important part to capture throughout an analysis paying attention to stakeholders is to bring forth an understanding of the attribute of what a stakeholder is part of as well as a specific type of stakeholder, who has more power than other stakeholders, which this paper will also aim to understand: "Whatever the magnitude of their stake, each stakeholder is a part of the nexus of implicit and explicit contracts that constitutes the firm. However, as a group of stakeholders who enter a contractual relationship with all other stakeholders. Managers are also the only group of stakeholders with direct control over the decision-making apparatus of the firm" (Hill & Jones, 1992, s. 134). All in all, this model and view upon stakeholders was developed to get a good long-standing relationship with stakeholder with the right management techniques aiding managers to deal with different and sometimes conflicting stakeholder interests, which is also why it were brought up in the literature review.

Short-termism and Private Equity:

The introduction manages to outline the concept of short-termism and why it is important to stakeholders, as it is argued that companies hurts future performance and society by focusing only on short-term results. In relation to stakeholders it is important to evaluate topics mentioned in the literature review such as power, urgency, and legitimacy. Examples of dealing with some of these stakeholders can be seen by Unilever where they shopped releasing profit figures stating they were only a distraction to the operation of the firm and only attracted short-term investors (Dakers, 2014). Furthermore, The CEO of Unilever, Paul Polman, states “Too many CEOs play the quarterly game and manage their businesses accordingly” and “Many of the world’s challenges cannot be addressed with a quarterly mindset” (Semuels, 2016). Another interesting point regarding short-termism is that “almost 80 percent of chief financial officers at 400 of America’s largest public companies say they would sacrifice a firm’s economic value to meet the quarter’s earnings expectations. And companies are spending more and more on purchasing their own shares to drive stock prices up, rather than investing in equipment or employees.” (Biden, 2016).

This section will go more into depth with details and try to make a comparison and differentiation between short-termism in public equity companies versus private equity companies. The best example in the corporate world of short-termism is probably the manipulation of quarterly results to meet benchmarks either/both set up by analysts and a company’s earning same quarter last year.

Unilever dealt with their problems by stopping releasing profit figures, which is a way of mitigating some of the short-term plans of the stakeholders of a company. That is a probable way for public companies to deal with it (Dakers, 2014). On the other hand, for private equity investors main aim is restructuring of their target companies. Problems is easier to fix in the case of private companies rather than public companies. Therefore, one of the main reasons for private equity investors taking a company private could be the conflict of short term goals with long terms aims and goals involving strategic ones as most of the shareholders are more interested in quarterly earnings (Khan, Vilanova, & Hassairi, 2011, s. 497). This is also a focus area for the private equity funds, as there is evidence that alterations of operations made by public equity firms in apparent response to capital market pressure appear to negatively impact future firm performance (Kim, 2011, s. 7).

In the discussion of short-termism Kim (2011) goes into depth with an analysis comparing public equity firms versus private equity firms. The most vital finding in the paper is that “public equity firms are more likely than private equity firms to opportunistically alter normal operations to improve earnings by cutting R&D spending, by pushing sales through discounts and promotions, and by lowering costs of sales through overproduction.” (Kim, 2011). One of the reasons there is a push for this kind of culture can be found in the corporate bonus packages, where e.g. CEO’s annual bonuses take a substantial reduction if the company do not manage to meet quarterly earning benchmarks set up by analysts or the earnings for the same quarter last year (Matsunaga & Park, 2001). There is however, no difference between discretionary expenses, which is nonessential expenses often seen as wants rather than needs in the corporate world (Coyne, Coyne, & Coyne Sr., 2010).

Evidence from Kim (2011) and Zang (2012) suggests that companies with an exposure to public equity markets is associated with a greater tendency to meet earnings benchmarks through accrual management- and real earnings management-alteration manipulating the company's activities. Therefore, a higher exposure to private debt such as e.g. institutional investors suggests less real earning management. However, there is evidence a higher exposure to private debt causes more earnings management regarding zero earnings benchmark the closer the debt comes to default. This is because companies that fail to meet this earning benchmark gets punished with a higher cost of capital indicating that the debtholders exert pressure like public equity investors as the debt moves closer to default (Jiang, 2008) (Kim, 2011). Although, private equity companies still alter operations it is not just to meet market expectations but rather as a long-term strategic firm decision thus is part of constructing the narrative that private equity companies think more long term than short term (Kim, 2011, s. 6).

An important find in relation to the altering of operations comparisons between private equity companies and public equity companies is found in (Kim, 2011). Kim (2011) finds evidence "that the public equity firms that just meet the short-term earnings goals while engaging in real earnings management experience more negative future performance while private firms that just meet earning benchmarks while engaging in real earning management do not. This might indicate that private equity firms' deviations from their normal operations are more likely to be driven by strategic as opposed to opportunistic considerations." (Kim, 2011, s. 6).

Summing up public equity companies are more likely to alter operations through earning management, even though it impacts future firm performance negatively. Private equity companies in some cases also alter operation, especially as debt comes closer to default, but it is more of a strategic move rather than opportunistic decision making. Thus, evidence from Kim (2011) suggest that private equity companies benefits in terms of future firm performance where public equity companies limits their future performance.

Agency Theory and Private Equity:

This literature review sets out to investigate the agency theory phenomenon, how to reduce agency costs in companies, and how it is done specifically in the private equity world. This is done to form a baseline of information and subjects, which are to be drawn upon later in the analysis.

The central problem agency theory addresses are how principals can control the behaviour of their agents to achieve their, rather than the agent's, interests. The power of agents to act in ways divergent from the interests of principals may be limited by use of incentives of monitoring (Jensen & Meckling, 1976), so that managers are expected to attend to those stakeholders having the power to reward and/or punish them. The private equity world has received praise from many corners for reducing agency costs arising between the interests of fund managers and investors (Harris, 2012, s. 259).

The private equity funds reduce agency costs in companies, however in some cases the agency costs are just transferred to the private equity funds. Though, the private equity funds still try to actively reduce agency costs in private equity companies (Kim, 2011) This is done in several ways. Both mispricing and agency-based theories imply that relatively more deals will be undertaken when debt markets are unusually favourable, which is also the case for private equity companies, but this also poses them fragile to boom and bust cycles (Kaplan & Strömberg, 2008) (Bratton, 2008).

One of the major changes a private equity company makes is to pay out higher dividends, which reduces free agency problems, and are motivated by high free cash flows. As per Jensen (1989) cash richness hypothesis agency problems related to cash tend to result in lesser growth prospects of firm where private equity funds invests the cash wiser, however this theory has later been disproven (Bratton, 2008). Albeit, the results of Khan, Vilanova, and Hassairi (2011, s. 500-501) suggest that free agency problems may be mitigated by high dividend ratios, which is also seen as a big difference between companies under control of private equity firms, as they tend to pay higher dividends.

Proponents of the buyout phenomena argues that the buyout target emerges from the control transfer with a governance structure that approaches the agency ideal. Its incumbent managers get high-powered incentives as minority shareholders. Furthermore, the structure also eliminates blockholder incentive problems and free-rider problems. “The general point is that buyouts mean monitoring and monitoring means productivity gains” (Bratton, 2008, s. 519-525). Even as buyouts pose a structural alternative to separated ownership and control, their business model exploits and depends on market liquidity, but market liquidity is the case, at least in boom cycles (Bratton, 2008, s. 511).

In corporate context scholars such as Harris (2012) and Conaway (2008, s. 814-815) proposes contractual ways of limiting major agency costs. The best example of a contractual way of trying to limit agency costs is probably to “hitch manager compensation to firm performance. Corporate firms frequently give mangers a relatively low fixed base salary, but supplement it with large equity-based compensation in the form of stock or options.” (Harris, 2012, s. 264). However, there is also evidence that in the corporate context that actors manage to undermine the incentive based contractual arrangements (Bebchuk & Fried, 2004, s. 135-136).

In the context of private equity funds, it is a bit different however. The investors have little to no influence on how the funds invests money and manages companies. There are many obstacles to reduce agency costs and equal the playing field. Regarding legal obstacles several can be mentioned such as Centralized Management with all Decision-Making Power, Limited Liability of Funds, and Fiduciary Duty of Care. Regarding contractual obstacles several can be mentioned such as: Distribution of Liquidity, Liquidation of Funds, and Manager Compensation.

Harris (2012) suggests that the classical contractual ways of limiting agency costs, like tying salary to performance, is just one of a few parameters that should be looked at. Harris (2012) proposes to include two completely different methods of reducing agency costs in relation to private equity funds, which is public enforcement and different private enforcement. The idea of public enforcement is to get stronger default rules for investor influences, where Harris (2012, s. 265) proposes a stronger right to sue for investors if misbehaviour were to happen. The idea of different private enforcement is to get increased, ongoing monitoring of fund manager conduct, instead of the current over-reliance on contract design (Harris, 2012).

These are a few ways to try and mitigate agency costs, nevertheless actors should be careful with how these possible mitigations are used, as they might increase agency costs, even if they are done with the best intensions (Harris, 2012) (Bebchuk & Fried, 2004). Therefore, it is difficult to evaluate "whether or not these shortcomings offset the benefit of such clauses" (Harris, 2012, s. 266).

Summation:

The project set out to explore how to mitigate short-termism drawing upon lessons learned from private equity businesses mid- to long-term strategic horizons, which has led to conducting the literature review on the concepts of Private Equity, Stakeholders, Short-Termism, and Agency Theory in relation to Private Equity. From this a basis has emerged for understanding the subjects involved in this project. There are several unknows though. There have not been conducted a lot of work solely focusing on private equity, as the data on private equity often has been mixed with that of venture capital. There has been done quite a lot of work on agency theory in corporate context but not that much when involving the context of private equity. Short-termism in general is a relatively new term in the world of academia and in corporate context, which is also why it has been difficult to investigate. The combination makes for an interesting combo.

Table of papers:

Figure 5 - Table of papers

Paper 1: (Kaplan & Strömberg, 2008)

Title – Authors – Date	*Type of paper*	*Research topic*	*Theories*	*Method*	*Findings*
Leveraged Buyouts and Private Equity. Kaplan, S. and Strömberg, P. (2008)	Empirical	Study of the private equity wave presently and in the past.	*n/a*	Longitudinal data study of secondary data. Quantitative analysis with a level of qualitative interpretation.	Private equity activity is very prone to happen in boom and bust cycles. There is evidence that private equity creates economic value for firms as well as private equity professionals. However, that same evidence is not present for limited partners when compared to the Standard and Poor's stock market index for a limited amount of years (2004-2007). Private equity leveraged buyouts are less likely to go bankrupt when compared to all companies. The majority of exit modes of private equity is reselling to a strategic buyer and reselling in a secondary leveraged buyout, whereas initial public offering with 14 % of the exits were the third most used exit mode.

Paper 2: (Phalippou & Gottschalg, 2006)

Title – Authors – Date	*Type of paper*	*Research topic*	*Theories*	*Method*	*Findings*
The Performance of Private Equity Funds. Phalippou, L. and Gottschalg, O. (2006)	Empirical	Study of past and recent performance of private equity.	*n/a*	Longitudinal data study of primary and secondary data. Quantitative analysis with a level of qualitative interpretation.	Previous research has been very biased towards better performing funds, which skewers the performance the private equity industry reports. Quite a few of the investments that has not been exited yet represent living dead investments that biases previous reports. When correcting for sample bias, living dead investments, accounting values etc. Phalippou and Gottschalg shows that the average fund performance is not slightly over S&P500 but albeit slightly below S&P500. However, in the end they bring forth some pros and cons on why private equity is still a popular asset class.

Paper 3: (Ljungqvist & Richardson, 2003)

Title – Authors – Date	*Type of paper*	*Research topic*	*Theories*	*Method*	*Findings*
The Cash Flow, Return and Risk Characteristics of Private Equity. Ljungqvist, A. and Richardson, M. (2003)	Empirical	Study of past and recent performance of private equity.	*n/a*	Longitudinal data study of secondary data. Quantitative analysis with a level of qualitative interpretation.	They have gathered a thorough data set with cash flow data for each fund, where other studies fall short with only having aggregate or accounting returns. Timing, returns, amount etc. is known as well. It is shown that it takes a long time to invest, where in some cases only about up towards 20 % of the committed capital to a fund is invested in the first year. However, private equity as an asset class is reportedly doing well with a per annum return of 5 to 8 percent when compared to the public equity market.

Paper 4: (Li, Davis, Kinniry, & Wicas, 2004)

Title – Authors – Date	*Type of paper*	*Research topic*	*Theories*	*Method*	*Findings*
Private Equity Performance Measurement and Its Role in a Portfolio. Zhu, L., and Davis, Joseph H., and Kinniry Jr., Francis M, and Wicas, Nelson W. (2004)	Empirical	Study of past and recent performance of private equity.	*n/a*	Longitudinal data study of primary and secondary data. Quantitative analysis with a level of qualitative interpretation.	They put a question mark at the positive view people have of private equity through data showing that private equity not necessarily provides great returns on investments. Many risks are debated and shown such as investment horizon, liquidity constraints, contract conflicts etc. Their most important point is that private equity should be but a part of a portfolio rather than a portfolio.

Paper 5: (Ivashina & Kovner, 2008)

Title – Authors – Date	*Type of paper*	*Research topic*	*Theories*	*Method*	*Findings*
The Private Equity Advantage: Leveraged Buyout Firms and Relationship Banking. Ivashina, V. and K., Anna (2011)	Empirical	Study of private equity firm loan behaviour for investing.	*n/a*	Longitudinal data study with statistical analysis.	One of the reasons private equity is successful as an asset class is it close relationship with the banks. Through tight bonds that has formed over a plethora of transactions they together can help reduce inefficiencies. They major finding is that a one standard deviation increase in relationship strength as well as cross-selling potential adds into up to a 4-percentage point increase in equity for the private equity firm.

Paper 6: (Jensen M. , 1989)

Title – Authors – Date	*Type of paper*	*Research topic*	*Theories*	*Method*	*Findings*
Eclipse of the Public Corporation. Jensen, M. C. (1989)	Conceptual	Study of why the public corporation is outlived with the invention of private equity.	*n/a*	Agency theories and conflict management.	The public corporation is ineffective. There are a lot of conflicts happening between all participating stakeholders such as owners and managers. These conflicts happen for a plethora of reasons, which can be explained through the agency theory. A way of solving or at the very least mitigating these issues is with the new organizational form of private equity that can manage resources as well as motivate people more efficiently.

Paper 7: (Eden & Ackermann, 1998)

Title – Authors – Date	*Type of paper*	*Research topic*	*Theories*	*Method*	*Findings*
Making Strategy: The Journey of Strategic Management. Eden, Colin, and Ackermann, Fran (1998)	Empirical	Strategy making appropriate for the organization and its stakeholders.	*n/a*	Singular cases of successful strategy formation used in conjunction with previously existing knowledge on the topic of strategy formulation.	Through cases Eden and Ackermann explains the process of formulating a strategy fitting for a specific companies' size, purpose, and available resources. The interesting part for this project is how they manage to incorporate stakeholder management where they come up with a figure describing stakeholders in relation to two key factors: Interest and Power.

Paper 8: (Mitchell, Agle, & Wood, 1997)

Title – Authors – Date	*Type of paper*	*Research topic*	*Theories*	*Method*	*Findings*
Toward a Theory of Stakeholder Identification and Salience: Defining the Principle of Who and What Really Counts. Mitchell, Ronald K., and Agle, Bradley R., and Wood, Donna J. (1997)	Meta paper conceptualizing previous research.	Stakeholder literature and how it can be legitimised and used.	*Stakeholder Theories.*	Meta study of stakeholder theories conceptualizing into their own framework.	After a careful analysis of previously existing literature and definitions of topics such as stakeholders and stakeholder rationales, which end up being summed up into urgency, legitimacy, and power. This is used to create a framework describing 4 levels each containing different types of stakeholder.

Paper 9: (Harris, 2012)

Title – Authors – Date	*Type of paper*	*Research topic*	*Theories*	*Method*	*Findings*
A Critical Theory of Private Equity. Harris, Lee (2012)	Conceptual	Study of the private equity world contract design and how to reduce agency costs in private equity.	*n/a*	A critical assessment and analysis of common contracts in private equity.	Harris investigates partnership agreements in the private equity world. Even though they have received praise for reducing agency costs he finds that they also create some if not done correctly or are valued to mitigate more agency costs than they do. These include but are not limited too Centralized Management, Limited Liability, and Fiduciary Duty of Care. He brings forth some claims to include in contracts to reduce agency, which is Distribution, Liquidation, and Manager Compensation. Furthermore, he argues that implicit contractual agreements are necessary to reach a common understanding with best mutual interest in mind.

Paper 10: (Khan, Vilanova, & Hassairi, 2011)

Title – Authors – Date	*Type of paper*	*Research topic*	*Theories*	*Method*	*Findings*
Effects of Private Equity Investment on the Decisions of European Companies to go Private: An Empirical study. Khan, Haroon Ur Rashid, and Vilanova, Laurent, and, Hassairi, Slim A. (2011)	Empirical	Study of how private equity investments with the goal of going private affects the companies in question.	*n/a*	Comparison between private equity and management backed deals in going private through multinomial logit regression.	A longitudinal investigation showing that private equity funds have changed role in how they manage the companies they take private and which companies they take private. Previously they partook in highly leveraged transactions sometimes with over 90 % debt financing whereas now it is closer to 70-80 % leverage. Now they look towards business with low valuation, good management, strategic advantages, strong customer base etc. Therefore, operational improvements with the right strategy is how private equity creates value compared to the normal business, which is argued to also be because of the longer time frame of investments.

Paper 11: (Kim, 2011)

Title – Authors – Date	*Type of paper*	*Research topic*	*Theories*	*Method*	*Findings*
The influence of public equity ownership on earnings management through the manipulation of operational activities. Kim, Yura (2011)	Empirical	An investigation of whether public- or private-owned companies tend to manipulate earnings more than the other.	*n/a*	Data study comparing the difference on companies with public debt whether they are privately or publicly owned.	The major finding in this paper is that public equity firms are more likely than private equity firms to opportunistically alter normal operations to meet earning benchmarks. This is done through various ways, albeit often through cutting R&D spending, by pushing sales through discounts and promotions, and by lowering costs of sales through overproduction. Furthermore, the opportunistically altering of operations is found to have a negative impact on future performance, thus finding privately owned non-altering companies to have better performance long-term even though they are overlooking short term earning benchmarks.

Paper 12: (Bratton, 2008)

Title – Authors – Date	*Type of paper*	*Research topic*	*Theories*	*Method*	*Findings*
Private Equity's Three Lessons for Agency Theory. Bratton, William W. (2008)	Empirical	An investigation of the buyout phenomenon regarding agency theory.	*n/a*	Comparisons of how private equity buyouts have evolved over time and how there has been a shift in how they work and what implications that has had.	The paper suggests there has been a chance from hostile takeovers to just takeovers in the world of private equity. This also means that topics such as control transfers and governance discipline needs to be addressed differently than done in the past, proposedly through corporation. The link between agency theory and buyout motivation is also investigated, as there has been speculation agency theory is the cause of buyouts. However, the paper suggests that buyouts are rather a product of the economics of leverage. Though, the agency costs come into play, as agency costs associated with a buyout fund eats away at the bounty that there is not much left for private equity investors. Therefore, a transfer of agency costs from the firm to the private equity firm seems probable.

Chapter 3 – Methodology:

This chapter will involve a wide range of concepts vital when investigating a research topic. The meaning of methodology in this project draws upon the definition of Burrell and Morgan (1979), where they define methodology as "the way in which one attempts to investigate and obtain knowledge about the social world" (Burrell & Morgan, 1979). The aim is to get the methods and tools to undertake the research questions (Saunders, Lewis, & Thornhill, 2009). Concluding, methodology is important to define the strategy to guide the further research.

First, considerations regarding this project philosophic standing will be taken, which will be done through the topics of ontology, epistemology, human nature, and philosophy of science. Second, deliberations concerning this project research design will be done, which will be done through the topics of data framework, theoretical framework, validity, and reliability. Thus, creating the backbone of the analysis.

Philosophy:

The projects paradigmatic constructs will be discussed in this subchapter.

Ontology:

Ontology is involving describing the nature of social entities, as Bryman and Bell (2015) states it "Social ontology is concerned with the nature of social entities" (Bryman & Bell, 2015, s. 32). Thus, ontology attempts to deal and describe the researchers' conception of reality.

There are two general approaches, which is two either take an objective approach or a subjective approach. This project takes a subjective standpoint and faces the fact that in the end all matters are subjective. The world is socially constructed through interactions between actors, which is why to understand what is happening with phenomena in the world it is necessary to conduct a plethora of interactors. With a subjective approach, there is also no one size fits all. Therefore, a subjective approach might limit how widely applicable the project is however there will still be tried to make generalizable results, which then can be researched and tried in practice to increase the applicability of the results.

The focus is on the issue of short-termism investigated through the world of private equity. This means that primarily these will be the focus point, thus limiting other subjects that potentially could benefit by reduced short-termism as well. The idea of drawing upon private equity is new though, which draws in a lot of inspiration for the subject of short-termism. There are not many theories to draw upon though, as the subject is new. Therefore, an inductive approach has been taken in other to come up with tools and methods for future academic and in corporate contexts. There are however several fields drawn into the project, which will not be taking the inductive approach, as they already have solid work put into them, such as theories on stakeholders e.g. Thus, the deductive approach is also taken into consideration when applicable. Consequently, the project applies an abductive approach alternating between the inductive approach as well as the deductive approach when applicable (Bryman & Bell, 2015, s. 27).

Summing up the projects ontology falls under the constructionist approach. With this approach, I also recognize previous experiences and knowledge is a factor in the way the project develops.

Epistemology:

"An epistemological issue concerns the question of what is (or should be) regarded as acceptable knowledge in a discipline. A particularly central issue in this context is the question of whether or not the social world can and should be studied according to the same principles, procedures, and ethos as the natural sciences." (Bryman & Bell, 2015, s. 26). In short, epistemology is about what the concept of truth is and how knowledge is regarded.

There are different approaches to epistemology in different types of research whether the research is of quantitative or qualitative nature. However, even though there are different types of data they have a shared starting point, which is that one starts with previous knowledge identified in relation to key topics as a basis and through the research process and as new knowledge emerges challenges previous established knowledge, as such is science structured. Thus, being critical and at the same time forward thinking is one of the ways knowledge evolves, which this project aims to contribute within the subjects of private equity and short-termism. This project aims through interactions and critical assessment of the both quantitative and qualitative data necessary to conduct the project to bring forth knowledge that in collaboration with previously known knowledge can improve the understanding of the field. Summing up, knowledge is assembled and explored from an array of sources of different nature and put together to understand and explore the social world.

Human Nature:

Human nature is the concept of unfolding assumptions about the interplay and describing the relations between individuals, the collective, and the environment from the researchers' viewpoint. "Some researchers see the social environment as being outside the individual. Other researchers hold the view that human beings and the social environment codetermine each other." (Kuada, 2014). Taking a constructionist approach and reading the epistemological deliberations it implicitly states that actors influence each other in the social world through interactions and also that, as a researcher, participating the actors are influenced by me and I by them. This also leads to the point that the project possibly will not contribute universal truths, as there is always a subjective bias present throughout all interactions.

Philosophy of Science:

"Describes the reasons underlying the choice and use of specific methods in the research process." (Kuada, 2014). The above ontological, epistemological, and assumptions regarding human nature is the basis for the approach of philosophy of science.

This project takes a structural interpretivist method. This means that there is both a focus on the individuals as well as the collective. Interpretivism puts emphasis on how individuals define situations in which they are involved and meanings derived from those experiences. Structuralism on the other hand focuses on the collective rather than the individual. Therefore, the project focuses both on the individuals and collective. One of the goals with the investigation is to tie individual experience into a collective framework more widely applicable, though one always should be wary of contextual settings. First off, the goal of the project is to simply understand and then try to explain from the understanding. Society is composed of complex system including interrelated parts, where e.g. the individual companies are individuals and the whole business community or the whole private equity business community is society. The actors within the society are ever-evolving, which is also why one can only get a snapshot of the constructed reality at the time of the analysis but it is quickly outdated as new actors emerges or actors evolve. With this focus on both individuals as well as the collective it should be possible to understand and bring forth the emersion of new knowledge (Kuada, 2014) (Bryman & Bell, 2015, s. 28).

Research design:

The projects research design will be discussed in this section. This involve subjects such as data collection and methods. Furthermore, the impact of the data framework and theoretical framework on the project will be discussed in validity and reliability.

Data and Theoretical Framework:

The data framework of a project describes how the process of collection is and which data is gathered. Generally, as a person I am very curious and have an open mind, which have also been tried to be translated into the project, meaning in relation to the data framework an inductive exploratory approach is being deployed. This shines especially through in the topic of the project, as I generally find private equity and different emerging business topics interesting, thus combining them an employing inductive method could possibly yield future progress. This also shows in the research structure where the aim is to first understand and then develop theories with an open mind. However, it also employs the deductive approach in relation to some topics such as stakeholder where existing suitable theories are present. Consequently, alternating between inductive and deductive is the overall framework, thus being abductive (Bryman & Bell, 2015, s. 27).

Different types of data are used during the investigation; however, they all have a secondary nature in common. There is an also a convenience factor over which data has been deployed. “In business research, we are rarely in a position in which we can interview, observe, or send questionnaires to all possible individuals who are appropriate to our research; equally we are unlikely to be able to read and analyse the content of all articles in all newspapers relating to an area of media content that interest us. Time and cost issues will always constrain the number of cases we can include in our research, so we almost always have to sample” (Bryman & Bell, 2015, s. 12). This has also been the case in this study. It would have been most optimal to gather primary data. However, I tried to reach out to a plethora of private equity businesses in Scandinavia as well as the United Kingdom but none were willing to use time and resources on a project that might not yield them anything. The most common answer was that they did not currently have time for a project like this and that their data are confidential as well as their tools and methods for running their business and associated businesses. Therefore, secondary data have been the data of choice along with a purposive sample, albeit out of necessity. The purposive sample has been a way to reduce the time and resources to be committed for e.g. a random sample. This creates a level of bias in the selection, which is why the results of the project should be an inspiration for increased work in the field rather than a definitive conclusion to the research problem (Bryman & Bell, 2015).

Consequently, the study employs the desk research approach. The term desk research refers to using data gathered either by another actor, such as researchers, institutions, or companies, or with another goal in mind than the one currently proposed (McCaston, 2005). McCaston (2005) suggests that it is more often a combination of the two, which will also be the case in this study. One of the objectives of the study is to form a baseline and be a helpful tool in the designing of future research projects, which desk research is a good tool for according to McCaston (2005). So even though this project is not able to use primary data future projects within the area might draw upon this project and have a higher chance of completing an investigation of the subjects through the scope of primary data.

Throughout the project both data of a qualitative and quantitative nature has been applied to mitigate the weaknesses of each of the data forms and drawing upon the strengths of both, also referred to as mixed methods research by Kuada (2014, s. 119). This has been applied to get the best data for the research purpose increasing the yield, consistency, and triangulation (Kuada, 2014) (O'Cathain, Murphy, & Nicholl, 2007) (Greene, Caracelli, & Graham, 1989).

In relation to method the project applies several, depending on what kind of research question it is. One of them being the concept of content analysis, which according to Bryman and Bell (2015) is: “Content analysis is a research technique for the objective, systematic, and quantitative description of the manifest content of communication” (Bryman & Bell, 2015, s. 298). The technique aims at coming forth with a conclusion on a topic with minimal amount of subjectivity, which e.g. has been applied in research question 2. The conclusion is reached by drawing in all available data and applying the data together. The data investigated throughout the project also helps sum up the evaluating parts of the project, because several points of view has been examined, although evaluation will always have a level of subjectivity.

The main types of secondary data include:

- Reports.
- Scholarly articles.
- Newspaper articles.
- Company information.
- Other electronic sources.

Validity:

“Validity is concerned with the integrity of the conclusions that are generated from a piece of research.” (Bryman & Bell, 2015, s. 50). The concept of internal validity is concerning if there is a match between the observations and theoretical ideas. Throughout the project this has been given thoughts. It is a hard topic to evaluate regarding internal validity, as the project attempts at using an approach from one concept and adapting it to be used in another context. However, I have attempted to create a good match throughout the investigation and the linking of topics. The logical process of the research questions is a testament to that, through the creation of a linked process leading there to be a good match between what is observed and theoretical ideas applied. The observation and theory-crafting of the project has taken place over a rather long period of time, which according to Bryman and Bell (2015) “allows the researcher to ensure a high level of congruence between concepts and observations” (Bryman & Bell, 2015, s. 400).

The concept of external validity is regarding if the findings of the project can be generalized across social settings. The very aim of the project is to try and tweak concepts to make them fit other social settings. However, the issue is that the sample size is relatively small and no work has been done in this field before, yielding it hard to evaluate whether the findings are generalizable. Using different types of companies e.g. helps though and topics such as how to cope with business challenges are universal business subjects.

Reliability:

"Reliability is concerned with the question of whether the results of a study are repeatable." (Bryman & Bell, 2015, s. 49). The external reliability of the project is high, as only available public data is employed throughout the project, meaning everybody has the same baseline of information, though seen through other eyes the data might be yielding other conclusions due to there always being a level of subjectivity present no matter. The fact that purposive sampling was used lowers reliability, as some might pick another purposive sample or another sample method. However, the data employed are all from available and different origins to gain a wider reference. Cross-analysing, reviewing, and interpreting these data increases the external reliability.

Internal reliability, better known as inter-observer consistency, is more of a problem with more researchers on the same project, as there might be different views upon reality and the data from the researchers thus giving different conclusions on the analysis of the data. Though, since there is only one research in this project it is not a matter (Bryman & Bell, 2015, s. 400).

Chapter 4 – Analysis:

This chapter will include a careful analysis of the proposed research questions done through the research design leading up to an answer for the problem formulation via a proposed framework. It should be noted, it has been hard to find tools and methods to solve the problem formulation in the existing literature, which is why subjects have been drawn in inductively and through careful analysis attempts to solve the issue of short-termism.

Research Question 1: What is the uniqueness of business practice of private equity funds?

Private equity has become an increasingly growing player on the equity market in recent years. Private equity can be considered the counterpart to public equity (PrivCo Knowledge Bank, 2017). Therefore, a private equity investment is an investment in a company that is not listed or gets delisted from the public exchange in the investment process. Private equity funds are a specific fund-type aiming at taking over the company and make it private, although there are other acquisition methods as well such as buying a business unit from a private company, buying a business unit from a public company, buying an independent private company, buying a business unit from private equity, buying business from the government. However, these are all negligible compared to buying a public company and turning it private being around 75 % of the total deal value (Barber & Goold, 2007). The goal of the private equity investments is different (Neuberger Berman, 2017):

- Buyouts: Using a combination of debt and equity a company is bought.
- Special situations: The aim is to restructure the investment target.
- Growth capital: Investment in a business' early stages to help the business grow.
- Venture capital: Similar intent as growth capital. However, often with higher risk.
- Private debt: Stable companies where returns derive from the leverage and illiquidity.

The presence of private equity backed companies has grown immensely since the concept of private equity funds emerged. Just since the year 2000 the number of private equity backed companies have grown from 1000 to over 6500 in 2015, whereas the publicly listed companies have been reduced from just over 6000 in year 2000 to around 3750 in 2015. *This only includes company's worth over 100 $ million dollars however. Still it talks to the ever-growing presence of this ownership arrangement, which can also be due to the returns private equity post publicly or in some cases lack of returns, as private equity choose to publish or not, due to the nature of their organizational form (Neuberger Berman, 2017).

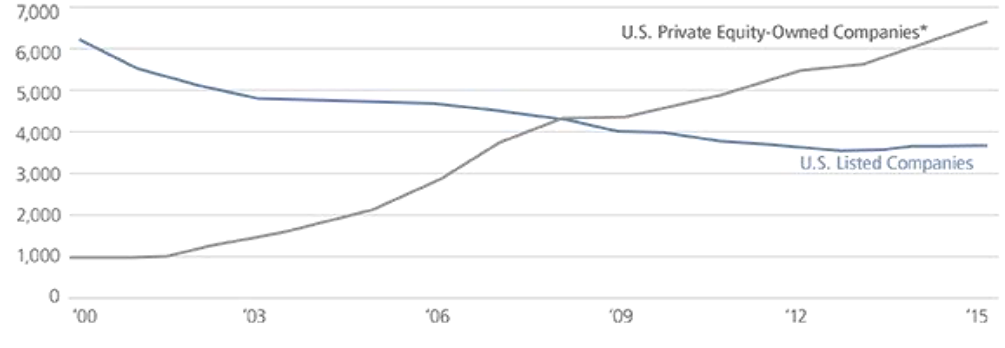

Figure 6 - Private Equity Companies Are a Growing Presence *(Neuberger Berman, 2017)*

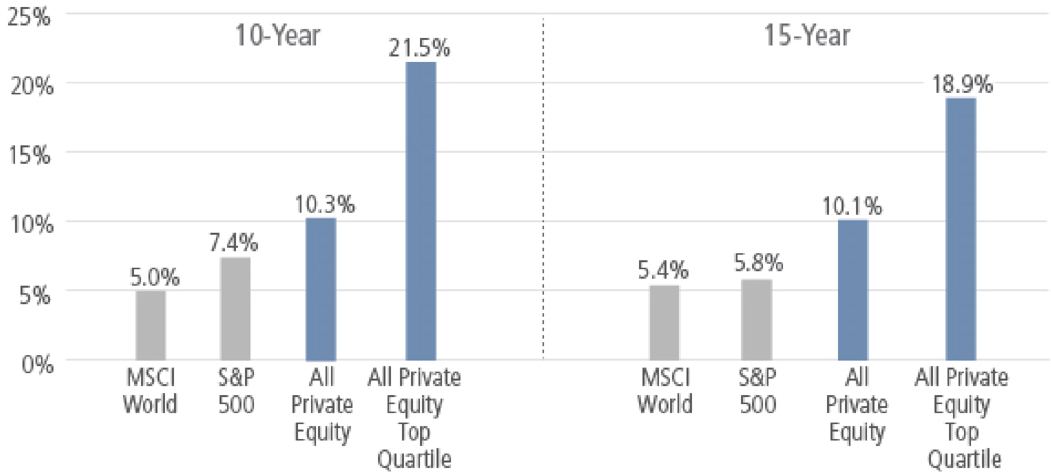

Figure 7 - Comparison of Horizon Returns - Public vs. Private (June 2016 and back)
(Neuberger Berman, 2017)

As can be seen private equity is a growing presence with higher returns. This research question aims to decipher and bringing forth an understanding of the uniqueness of private equity. Quite a lot of information has already been revealed in the literature review in relation to private equity and The Leveraged Buyout Phenomenon, The Difference from Others, Investment Horizon, Exit Strategies, Performance, Risk, Economic Value Creation, and Compensation. Therefore, this is going to be a short analysis upon the most vital uniqueness traits of the business practice of private equity funds and aims at building a point of departure for research question 2.

Uniqueness traits:

This section will involve the most vital uniqueness traits of the private equity business practice, that also provides them a competitive advantage.

Structure and Incentives:

The way private equity funds are structured is rather special, as can be seen in the literature review on private equity funds, why this paragraph will also just be a quick sum-up. They are most of the times structured as general partnerships with a general partner controlling the fund both in relation to management and investments. This also has the implication the investors, also known as limited partners, have little to no say in the investment and only has an impact on the initial contract arrangements, thus giving the private equity fund a lot of manoeuvrability compared to their public equity counterparts, as public equity companies must adapt to public company regulations. The way this partnership work is through high-powered incentives for both the portfolio managers and the managers of the invested businesses ultimately mitigating e.g. agency costs (Neuberger Berman, 2017) (Barber & Goold, 2007).

Tax:

One of the primary ways private equity funds create returns is because of the way they work around the tax system. Companies under the management of private equity often very aggressively use debt to gain advantages in the market. The use of debt provides both financing and tax advantages for the companies and the owners. However, one should remember these methods are also available to public companies (Barber & Goold, 2007).

In the case of the United states “Private equity funds, organised as private partnerships, pay no corporate tax on capital gains from sales of businesses, public companies are taxed on such gains at the normal corporate rate. This corporate tax difference is not offset by lower personal taxes for public company investors.” (Barber & Goold, 2007). However, lately there has been some debate about the area, as some of the private equity funds are publicly traded, whether they should be treated as private partnerships or in the same line as public companies in relation to tax. Also, the case of profits of selling a business should be treated as personal income or capital gains for the general partners, seeing there is quite a difference in relation to the amount of taxes paid (Barber & Goold, 2007).

Tinkering:

One of the primary factors that sets private equity funds aside from other investors are their ability to impact the investment. When they perform a buyout on a company there is a strategic plan to be followed for a long time. This plan usually involves a stringent emphasis on the management of cash flow and the product-, sales, etc.-margins of the business. In the beginning the focus is on swift performance improvements (Barber & Goold, 2007). This is a fast-paced business plan set to succeed in a relatively short amount of years. However, at the same time there is a long leeway in the sense that it does not matter if quarterly earnings take a hit if the strategy requires several years to complete. An important note is that private equity companies do look towards synergies in the sense of shared costs, shared capabilities, or shared customers among their portfolio businesses and only focus on what they can change within the company. Consequently, the fast-paced way private equity funds manage the portfolio companies gives them quick knowledge of the business and with the focused, lean management creates immense long-term value. The advantage for private equity funds is the experience level by having done this a plethora of times where public companies do not share the same experience level (Barber & Goold, 2007).

Targets:

During the early days of private equity funds, they focused more on noncore business units of big public companies, as they had usually been neglected under previous ownership. The neglect often involved constraints in relation to being part of the corporations, poor management, or unfitting performance targets. However, sometimes even with a good incumbent management these businesses could still perform poorly, why private equity tried to find targets that has been neglected in the corporation and at the same time were hard to value due to e.g. being integrated with other units. After 2004, however, this type of buyout were no longer the most common and new targets were on the scope. Public companies are now the target of choice, as the appetite for returns grows, because there still are benefits of being private rather than public, and the term ‘conglomerate’ is being phased out in the corporate world (Barber & Goold, 2007).

Summing up:

These structure-, tax-, tinkering-, target-traits are contributing to the returns that private equity companies pose and this forms a baseline of understanding for the investigation of what private equity contribute to the portfolio companies. In the next research question the portfolio companies will be investigated in specifics with a greater focus on what private equity funds do to improve the private equity owned companies.

Research Question 2: What are the specifics of the strategical, financial, and managerial management of private equity portfolio companies?

The focus in this research question will be on one of the previously mentioned uniqueness traits, as the goal of the research project is to find moves that other companies can make use of, of private equity: Tinkering. This means that the specifics of the strategical, financial, and managerial moves that private equity makes in portfolio companies will be investigated. This is done through selected private equity portfolio companies, that is investigated closer in order to get a perspective upon the specifics.

Portfolio companies:

This section will involve examples of specific portfolio companies and what has been done from the side of private equity in the deals and investment periods. The number will be limited to a few to go into depth with the changes the corporations has undergone. It is a choice of going into detail with a few rather than a superficial analysis of a plethora of portfolio companies. Furthermore, one fund has been chosen as inspiration, as they have recently been the whiz kid on the market only with long-term strategic intentions in mind.

The private equity firm 3G capital has been a very prominent on the private equity scene lately and as cases I will use some of their biggest investments. Burger King (2010), which later were part of the creation: Restaurant Brands International. H.J. Heinz Company, which later merged into Kraft Heinz Company (2015).

3G Capital:

3G Capital is interesting for several reasons. The corporate philosophy of the 3G private equity firm is described as like running a marathon: "You're running, you're always close to a limit, you're working very hard and being evaluated all the time" (Roberts, 2013). "3G Capital focuses is on long-term value on long-term value, with a particular emphasis on maximizing the potential of brands and businesses" (3G Capital, 2017). They aim to work in close partnerships with management teams at portfolio companies and puts increased emphasis on the importance of recruiting, developing, and retaining top-tier talent. 3G Capital has good connections, which is also showing when Warren Buffett time and time again help them finance (3G Capital, 2017).

Their strategy revolves around identifying and investing "in opportunities that are well-positioned for profitable, long-term growth, and success across a variety of different sectors and regions. Leveraging prior investment experience, industry expertise, and an extensive global network" (3G Capital, 2017) provides the reference point for the strategy. Through cautious analysis and a philosophy of "factoring in the downside of an investment is equally as important as the upside potential" (3G Capital, 2017) 3G capital has been able to pose results even though the global economic cycles has not always been beneficial. Another trait of 3G Capital that is recurring in a lot of private equity firms is the concept of partnership with the companies, making use of meritocracy, awarding adequate compensation, thus creating an "alignment of interests among 3G Capital's Principals & Partners and relevant management teams." (3G Capital, 2017).

Burger King:

A steadily growing category of business is fast food chains. Private equity has in recent years been very interested in these types of businesses, at least so in the United States. I will use Burger King as a case, but there are quite a few examples of private equity takeovers in the last couple of years. Examples include Wendy's receiving interest in a potential deal, Arbys receiving interest in a potential deal, Carl's Jr. parent CKE Restaurants were sold, On the Border Mexican Grill & Cantina were brought from the parent Brinker International, California Pizza Kitchen Inc is looking for buyers, Benihana Inc is looking for buyers (Baertlein, 2010).

Restaurant Brands International has been chosen, as a case because they have a very interesting history and recently, in 2010, were sold to a private equity fund, 3G Capital. The history of Burger King starts with its creation in 1953. Already in 1967 it was purchased by a corporation, Pillsbury. However, Pillsbury had no clue how to run restaurants, probably due to Burger King being unrelated to their other business areas. In 1988 the British company, Grand Metropolitan (later part of the merger with Guinness turning into the world's largest liquor distributor, Diageo), acquired Burger King through a hostile takeover. Burger King had been neglected in both ownerships with corporations that did not focus on improving the Burger King brand. Thus, here is a case of a business unit in a corporation that has been neglected throughout several ownerships, even though there once were potential for Burger King to be as big or bigger than McDonalds (Nocera, 2012).

In 2002 private equity found an interest in Burger King. Three private equity firms teamed up, Goldman Sachs' private equity arm, Texas Pacific Group, and Bain Capital, and bought Burger King. The takeover was on the base of $210 million of provided money and $1.29 billion burrowed money. The numbers do not lie and they managed to make $511 million while still retaining a 76 % stake (Ip & Sender, 2006). In 2010 Goldman Sachs, Texas Pacific Group, and Bain Capital choose to cash out and sell Burger King to another private equity company, 3G, for $3.3 billion. The deal in total is in the ballpark of $4 billion, with around $2.8 billion financed with debt. 3G already has experience with fast food restaurants after having invested in Wendy's, which will come to show as a big advantage. Analysts were baffled by the deal's valuation due to Burger Kings bad fundamentals at the time, but the deal still made it into top 10 business deals of the year (evaluated by TIME (Gandel, 2010)) (Dealbook, 2010) (Baertlein, 2010).

The first trio of private equity firms nursed Burger King back to health and stabilized the brand and the franchisees, whom in many cases were in worse shape than Burger King itself. In the first couple of years 3G seemingly had done nothing but to lay off a large amount of the staff in the Burger King headquarters. However, after going through with 3G's long term strategy, e.g. increased internationalisation, Burger King and bringing in a few other investors to expand or acquire other businesses 3G's stake (51 percent) is now worth $6.7 billion, as of May 2017, where Restaurant Brands (the new parent organisation) has a market capitalisation of $13.1 billion (Forbes, 2017). It should be noted that Restaurant Brands is not completely private, as the stock market can purchase about 29.4 percent of the shares. However, majority stake and operations are still in the hands of the private equity firm 3G. Burger King together with capital from other investors along with 3G acquired Canadian fast food chain Tim Hortons in 2014 forming Restaurant Brands International.

Restaurant Brands International Specifics:

This section will involve specifics in relation to what the private equity firms has transformed and changed in Burger King and later Restaurant Brands. There were plenty of room left for improvements when 3G took over Burger King in 2010. To name a few: improve operations, expand internationally, diversify revenues (Burger King had 2/3 of their revenue in the United States and Canada, while McDonald's had 35 percent of their revenue in the United States (Gandel, 2010)), refocus on their loyal customer group.

When 3G Capital acquired Burger King in 2010 one of the first moves they made were to hire one of their own partners as CFO. Interestingly, the CFO, Daniel Schwartz, did not have any experience with running a restaurant chain. However, he was determined to figure out how Burger Kings competitors like, Chipotle, enjoyed double digit growth while Burger Kings growth stalled. To gain that experience Daniel Schwartz worked in restaurants in positions ranging from working the kitchen to fixing scrubbing the toilets. The experience he gained there became the basis for a lot of the major changes he later did to improve the future iteration of Burger King. Daniel Schwartz later became CEO in 2014. However, at the first couple of years 3G Capital worked closely with the CEO to go through with their strategy. What 3G Capital has done with Burger King speaks for itself, as Burger Kings earnings before interest, taxes, depreciation, and amortisation (EBITDA) minus capital expenditures increased 60 % in the first year. "Burger King operating profit margins expanded from 13 per cent in 2010 to 54 per cent in 2015." (Munshi & Daneshkhu, 2015). Later their 1.2$ billion-dollar investment idea have turned into a corporate behemoth, Restaurant Brands International, valued up to $22 billion (Peterson, 2017).

The first principle 3G Capital applied to Burger King were cost cutting. "Costs are like fingernails; they always need to be cut" (Munshi & Daneshkhu, 2015) is the moto of one of the founders of 3G capital. 413 people total with 261 at corporate headquarters, which is quite a lot considering 500-700 executives worked at headquarters, were cut after the takeover. Thus, 3G aimed at people higher up in the hierarchy, who had high salaries, paid vacations, and prestige. 3G managed to improve operations and efficiency, even though they trimmed some of the higher ranked employees (Devaney & Stein, 2010). General spending and administrative spending were in general cut to the bone at the same time. Burger King managed to reduce overhead costs per restaurant by almost two-thirds (Maze, 2016). 3G capital are very aggressive in their cost-cutting, through the application of zero-based budgeting. When Tim Hortons were acquired and thus forming Restaurant Brands there were still a sharp focus on cost-cutting. Tim Hortons's general and administrative expenses fell 32 % in a year. "Zero-based budgeting puts pressure on managers to scrutinize every line item of costs every year. Everything is under the microscope" (Strauss, 2015). However, they at the same time encourage development in the franchises.

In relation to cost-cutting Daniel Schwartz also looked at basic financial expenses in Burger King. There are quite a few examples of cost-cutting that made the value of the business increase. A lot of the corporate perks given to executives were axed out. The corporate jet was sold, as he argued with Burger King headquarters location next to an airport made them able to fly commercial. An annual party in Italy with a spending of $1 million annually was put to an end. Offices was no longer made in mahogany and other expensive materials. He found three years' worth of office supplies stuffed in closets. Headcount reduced from over 38000 to 1200 with initiatives such as refranchising (Went from 1300 Burger King run restaurants to 71, which is the same thing 3G Capital did with Wendy's as part of "System Optimization" (Maze, 2016)). Split costs between operators and Burger King for remodels of the franchisees. Made the menu more lean and easier to understand through "a more measured approach" (Peterson, 2017). The same principles were applied to Tim Hortons's as well. The first quarter 3G capital took ownership they laid off 350 people (around 15 percent of the staff) at headquarters, and regional offices. They also put up their corporate jet and cut spending by quite a margin (Devaney & Stein, 2010). This is simply the result of e.g. applying the 5-whys and lean concepts. This resulted in an industry leading profit margin, as can be seen below where they have attained 45 percent profit margin, which is much more than any of its competitors:

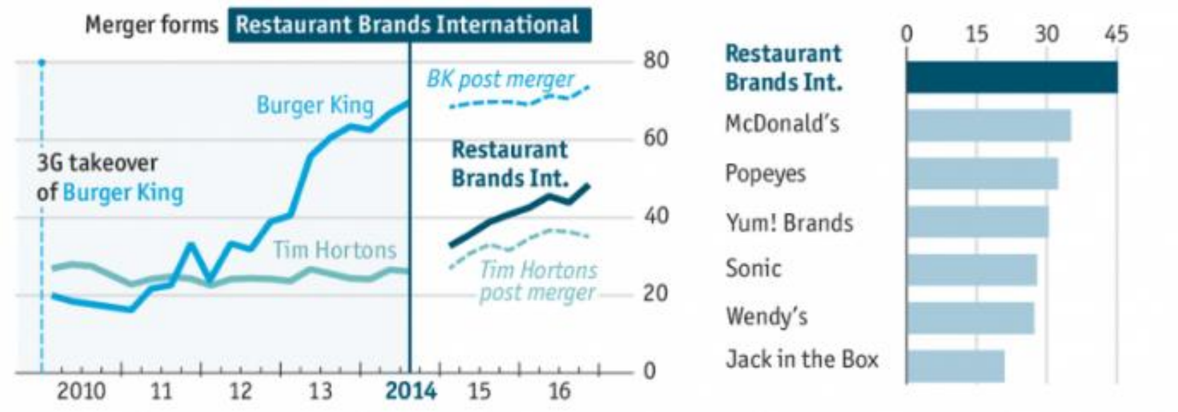

Figure 8 - Tasty Profits *(The Data Team, 2017)*

The management philosophy changed quite a bit under the new leadership at Burger King. Daniel Schwartz believes in management by walking around, which is why he spends a lot of time connecting with stakeholders such as franchise partners. Being better connected with franchise partners and their employees gives the knowledge of what should be changed to benefit the business in the long run. Furthermore, Restaurant Brands International also implemented individual goals and compensation for everyone, which creates a culture that creates results.

The results of the transformation are easy to see. “When 3G acquired Burger King they had $14 billion dollar in annual sales and was growing by about 150 new restaurants a year. 2016, the company’s total sales had grown to $18.2 billion and it opened 735 new Burger King restaurants worldwide” and “Burger King’s sales per unit have grown from $1.1 million to $1.3 million in 3 years (Peterson, 2017). This is even with the highly increased profit margins. The same recipe was applied at Tim Hortons’s which enjoyed growth for “11 percent from 2015 to 2016 when adjusted for the dollar’s value” (Strauss, The Globe and Mail, 2015). In the long term, there are plans for aggressive international expansion for Tim Hortons’s brand, even though it has failed in the past. However, one of the main reasons Burger King has expanded successfully internationally has been because of 3G Capitals wide range of contacts and all-round knowledge, which also could be successfully used at Tom Hortons (Strauss, 2015).

There are several lessons to be taken away from how 3G Capital has run Burger King and Restaurant Brands International:

- Cost-cutting and zero-based budgeting.
- Refranchised restaurants to operators and connect refranchise deals with remodel requirements.
- Adequate individual compensation.
- Developing aggressively in international markets with high growth potential, and thus diversifying the revenue area.
- Focus on both organic growth and mergers & acquisitions in areas where they have knowledge.

- Big focus on advertising and marketing.
- Rethink strategic partnerships and pricing models with stakeholders such as clients and suppliers.

Kraft Heinz Company:

Another example of a classic target and case for a private equity company is Heinz. A stable business in a market with steady growth rates. In 2013 Heinz were acquired by 3G capital in a transaction valued at $28 billion. Later in 2015 3G Capital arranged a merger between H.J. Heinz and Kraft Foods Group creating Kraft Heinz Company, which would come to create the fifth-largest food and beverage company in the world and the third-largest in North America. The transaction was valued at $62 billion (Daneshku, Whipp, & Fontanella-Khan, 2017). 3G Capital argued that there are endless opportunities for synergies, which can be realised through marketing and innovation. There were also talks of a merger between Kraft Heinz Company and Unilever, though so far nothing has come of it after Unilever and Theresa May spoke negatively of the deal (Davies, 2017) (3G Capital, 2017).

The history of Heinz and Kraft are much simpler than that of Burger King. In this case it is not because of a corporate business unit has been neglected but rather public companies, which has much to improve in relation to strategy and efficiency.

H.J. Heinz was a stable business with some of the highest recognizable brand-value in the food industry. The ketchup business is basically dominated by Heinz with around 26 percent share of the global market and 59 percent share of the United States market. However, there are room for improvements in the sense that the largest portion of Heinz's sales are from Europe, even though their most profitable consumer market is the North American. The Asian Pacific market looks strong in the future and grew 11 percent just in 2012, mainly due to increased demand from China. This provides good fundamentals, which also caused the deal to involve a 19 percent premium added to the stock's all-time high to shareholders (Berkowitz & Geller, 2013).

Kraft Foods were before the merger in major troubles. Their earnings fell 62 % in 2014, which in part were because of change of consumer behaviour. Local, fresh foods are what an increasing number of consumers desire and not the processed brands Kraft Foods offer. February 2014 the CFO stepped down, along with a couple of high-ranking executives when Kraft Foods reported a loss of $398 million in fourth quarter of 2014 (Timmons, 2015). Thus, there is talk of a public company, which has some major obstacles set out for them in the next couple of years from the buyout, such as change in consumer behaviour and economic uncertainty.

The result of the merger, Kraft Heinz Company, has created a powerhouse in the food and beverage business to be reckoned with.

Kraft Heinz Specifics:

This section will involve the specifics of how 3G Capital has transformed the businesses they have ownership over through the previously mentioned mergers and acquisition process. Heinz were a stable company with decent growth numbers before the acquisition while Kraft Foods were posting poor performance leading up to the merger.

When 3G Capital took over Heinz they changed quite a bit in terms of management. The old CEO of Burger King, Bernardo Hees, were brought in due to him being wildly successful in the turnaround with the brand. The cost-cutting strategy which has been described thoroughly above has also been applied in the case of Heinz. Just two months after the business were acquired an announcement were made to 1350 jobs on top of 600 corporate layoffs announced just after the takeover. The reasons behind the cuts were to cut the corporate fat and consolidate North American manufacturing. On the bright side, the consolidations also created 470 positions to be filled. The quest for efficiency were endless. With growth rates of just 6 % before the takeover and industry level profit margins drastic action were necessary to get ahead of competitors (Gasparro, 2013). Through the measures applied by 3G the profit margins increased by 58 percent to 28 percent within just two years, which previously had been thought impossible in the food industry, as the average profit margin in the food industry is 16 percent (Daneshku, Whipp, & Fontanella-Khan, 2017).

Since the creation of the Kraft Heinz Company it has been the same story. A trim of the corporate fat on the back of zero-based budgeting. “Since 2013, more than 10000 people – one-fifth of the workforce – have been laid off from Kraft and Heinz, with seven plants shut, highlighting the human cost and upheaval involved in producing the highest profit margins in the food industry.” (Daneshku, Whipp, & Fontanella-Khan, 2017). There has been a sharp focus on marketing and product development, however Kraft Heinz has posted less successful sales growth numbers for existing products than anticipated, though profits and money reinvested were increased (Daneshku, Whipp, & Fontanella-Khan, 2017). The profit margins have been increased hard and Kraft Heinz Company is the industry leader, as can be seen in the figure below:

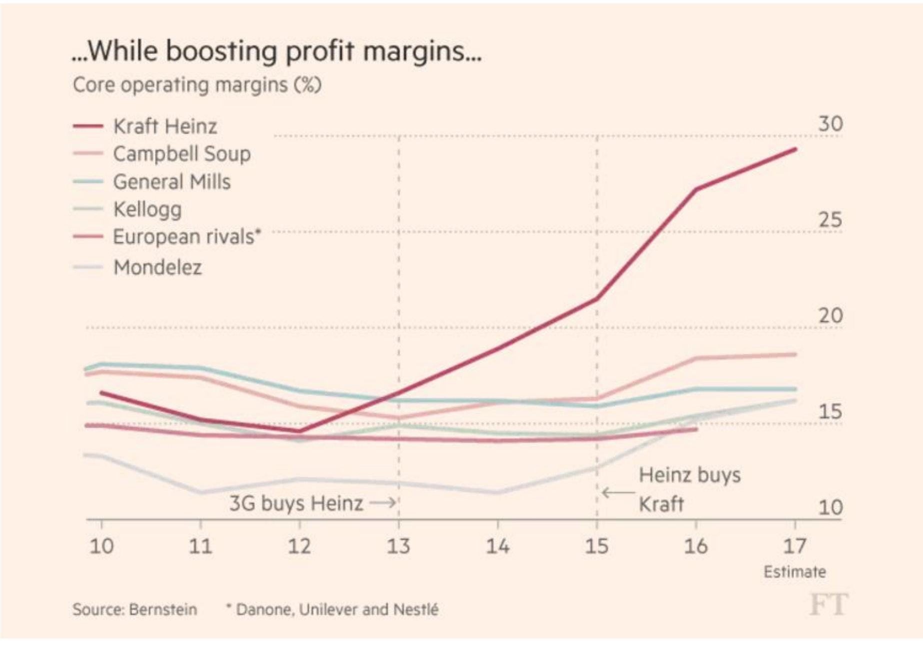

Figure 9 - ...While boosting profit margins... *(Daneshku, Whipp, & Fontanella-Khan, 2017)*

The overall retail sales in the United States have grown 12 percent from 2014 to 2014, which is on the back of the reinvestment program in product innovation and extensive marketing (Daneshku, Whipp, & Fontanella-Khan, 2017).

Overall, a few lessons can be taken away from the strategy that resulted in the fifth-largest food and beverage company:

- Build the brand.
- Reinvest in product innovation.

- Expand internationally.
- Both chasing organic and mergers and acquisition growth.
- Cost-cutting and zero-based budgeting
- Adequate individual compensation.

Summing up:

The approach and growth that has been taken in Restaurant Brands International and Kraft Heinz Company has been on the back a sound long-term strategy with a focus both on how the companies can deliver better cash flow on the short-sight to improve operations in the future. On the back of 3G Capital and their connections the targeted companies have had more money than ever to deliver value to shareholders and to grow both organically and through mergers and acquisitions. This would appear to be a signature method from the private equity firm, that has been pioneered in the building of the world's largest brewer of beer, Anheuser-Busch InBev SA/NV, where the 3G Capital founders invested their money before starting the private equity fund.

Another takeaway is a lesson for other private equity firms; Stay in long-term. In the case of Burger King the original private equity trio cashed out before they could gain the big profits. It is the same in the case of "Domino's Pizza, which has tripled in value since Bain Capital sold its last share." (Gara, 2017). It appears private equity funds can sometimes be too quick to exit when an investment shows profits, which shows the importance of staying in long-term and developing the business over a long investment horizon.

Research Question 3: What are the strategical and financial tools used by private equity which can inform non-private equity firms and what are the benefits and weaknesses of the proposed tools?

There are several takeaways from research question 2, which will be attempted to be summed up and divided into a few general points here in research question 3: Cost-side, Market side, and Cultural side. Summing up the biggest change that has happened in the portfolio companies has been:

- Cost-side:
  - Cost-cutting.
  - Zero-based budgeting.
- Market side:
  - Revaluation of strategic partnerships and pricing models with stakeholders such as clients and suppliers.
  - An efficient look at the business model.
  - Focus on both organic growth and growth through mergers & acquisitions in areas like the business they operate.
  - An openminded look towards which markets to focus on.
  - Increased focus on advertising and marketing.
  - Focus on increasing the brand value.
  - Reinvest into research and innovation.
- Culture side:
  - Meritocracy where the best is hired or the best is kept.
  - Adequate individual compensation.

- Nurse young talent and hire the best.

Cost side:

As has been described in research question 2 3G Capital has had a very rigorous approach to cost with nothing being off limits in the portfolio companies. This has improved operations by quite a huge margin resulting in an industry leading profit margin wherever they act. Big cuts such as corporate jets have been cut but also small costs-cuts like printing in black and white or printing on both sides of the paper. Corporate perks are another area to have taken a hit. The fresh eyes coming from the outside can objectively evaluate what is necessary and what is not (Peterson, 2017) (Devaney & Stein, 2010). This method is loathed by employees but is necessary for the business to thrive with manoeuvrability in the short term and success in the long term. A tool that has been applied in the portfolio companies is zero-based budgeting, which will be described below.

Zero based budgeting (ZBB):

The cause of 3G Capital's success are by many perceived to be because of zero-based budgeting. Before the successful implementation of ZBB by private equity the tool had a tarnished reputation among seasoned executives in companies. It is argued by Anderson and Schmitt (2016) that both large corporations and small companies alike. Before the success of investors implementing the tool, it was seen by corporate executives as: difficult, time-consuming, potential for negative impact on growth, and seen to be placing a burden on Managers whom has run successful budgets and resources throughout the years. However, if implemented correctly it can make operations much more efficiently (Anderson & Schmitt, 2016) (Pennsylvania CPA Journal, 2016).

The way ZBB works is to reset the budget each year and let managers account for what they need of resources to do all activities throughout the year. It requires planning and time but causes managers to rethink each expenditure that is required for the business to run successful, as they must defend the budgets to their superiors. This process causes managers to be vary of what each of their employees need and causes them to be in contact with all facets of the business. The strength and weaknesses of ZBB according to Anderson and Schmitt (2016) is:

Strengths	Weaknesses
Overall helps eliminating unnecessary costs. Helps to decide the most appropriate way of performing an activity. Can be applied to discretionary costs and support activity. Can be used for those activities where there is no clear relationship between input and output. Helps to curtail activities by creating questioning attitude. Helps confront conventional thinking and resource allocation by challenging every line item and assumption.	Time consuming and therefore expensive to implement. May create undue tension amongst managers. Cutting costs deemed non-core to a company's operations that are in fact core to its customers' experience could harm the brand and decrease value.

Figure 10 - Strength and Weaknesses of Zero-based Budgeting *(Anderson & Schmitt, 2016)*

As seen above there are both strength and weaknesses of the proposed method but the strengths outweigh the weaknesses in many cases. With thoughtful implementation, there is a lot to gain in organisations using the ZBB approach. Organisations should according to Anderson and Schmitt (2016) pay attention to identifying the decision makers correctly, construct the baselines correctly, and easy to understand.

Market side:

In the portfolio companies, several market side changes have happened. This has largely been on the back of a new pair of eyes combined with a philosophy to turn every single stone, meaning no expenditures, partnerships, pricing models etc. should be taken for granted.

This efficient look at the business has caused the portfolio companies to become more efficient and come in closer contact to markets. The focus has been on both organic as well as growth through mergers & acquisitions, which has netted the companies touched by 3G Capital to grow immensely fast with increasingly bigger industry leading profit margins. There is a big focus on growing in other markets and diversify where the income comes from to make the companies less sensitive to individual markets. On all markets, there has been an increased focus on the marketing and advertising to keep up / get ahead of competitors. To get ahead there has been increased efforts in relation to investing in research and development, creating new products, which in the long run grows the business. The focus on business improvements on all levels has led to what one of 3G Capital's focus points are; Focus on increasing brand value. This is all made possible by the immense focus on the cost-side, which frees up a lot of capital to focus on improving the business as well as the return for shareholders. The benefit of this strategy is a thriving business with attention to all details but it requires time and great execution to be wary of all these elements at once. It takes flair to run a business like this in the long run with day-to-day disruptions such as mergers and acquisitions always on the table.

Culture side:

3G Capital has changed quite a few number of things on the culture side in their portfolio companies. They swear by running the company on the principles of meritocracy, where everyone is evaluated upon their suitability for the position and nothing else. This causes the companies to hire the best talent. It is also increasingly important for them to nurse the talent arising in the organisations, whom they are not afraid to promote if results are provided in ample time. At the same time, they are rewarding all stakeholders adequately to their value, which means e.g. individual compensation and goals for employees. This creates a high pressure to perform culture, which can both be a pro and con from the standpoint of employees. The executives and employees laid off certainly do not see this culture as a plus, however, it creates a more efficient organisation with factors that motivate everyone (Roberts, 2013).

Research Question 4: What are the drivers of short-termism in other types of firms?

This research question will investigate what the drivers of short-termism is, using public companies as an example, as short-termist behaviour lately has become apparent there.

Short-termism:

Short-termist behaviour is in short: behaviour where companies act on short term sacrificing long term performance. Neglecting long term goals because of short term goals limits the firm's future performance and has been empirically proven to give companies with a good balance between short term goals and long-term objectives a competitive edge in the long run (Ernst & Young, 2014). This happens even though the arguments for a good balance and increased long term objectives are solid. According to McKinsey (2017) in an investigation from 2001 to 2014 they are:

- The revenue of long-term firms grew on average 47 percent more than the revenue of other firms, and with less volatility.
- Earnings of long-term firms grew 36 percent more than the revenue of other firms.
- Economic profit grew by 81 percent more than other firms.
- Long-term companies spent 50 % more on research and development than other firms, and even during the financial crisis they increased spending by 8.5 percent per year compared to 3.7 percent for other companies.
- Long term companies experienced stronger financial performance over time, also with a higher likelihood, 50 percent, to deliver top 25 % shareholder returns.
- For society, long-term companies created more than 12,000 more jobs, which would result in, if everybody took that approach, to five million more jobs and $1 trillion of increased gross domestic product, just in the case of United States. (McKinsey Global Institute, 2017).

Both the arguments and empirical evidence points towards the benefits of a better balance between short-term goals and long-term objectives. Therefore, this research question aims to dismantle the concept to come forth with recommendations in research question 5. When dealing with short-termist behaviour it is important to understand the mechanisms behind it. According to Ernst & Young (2014) the pressure on investors that gets channelled further to managers comes from several general factors, which can be seen below.

Figure 11 - Sources of pressure exerted on managers by investors. (Ernst & Young, 2014)

McKinsey (2017) has asked executives if they have faced pressure from stakeholders recently, which 87 percent has in the recent two years, according to their figure below.

Figure 12 - Surveys show that executives are feeling pressure from short-termism *(McKinsey Global Institute, 2017)*

Furthermore, a survey from FCLT Global (Focusing Capital On The Long Term) conducted by Barton, Bailey, and Zoffer (2016) shows that the short-term pressures come from several areas.

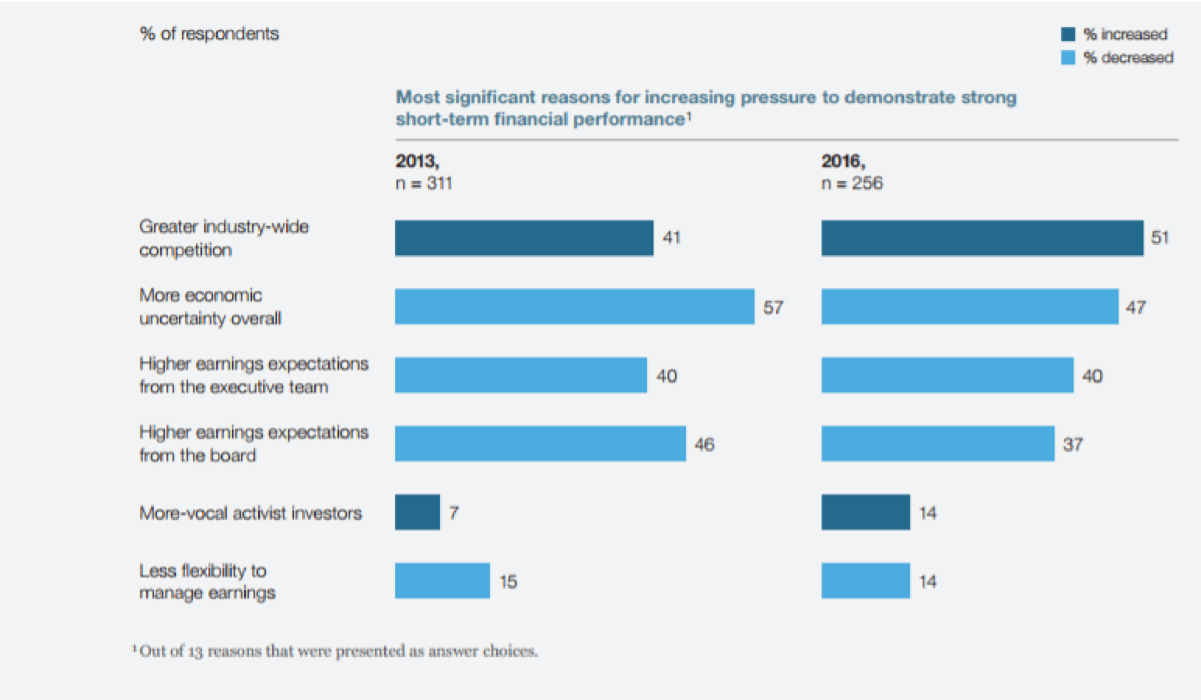

Figure 13 - Sources of short-term pressure have evolved over time *(Barton, Bailey, & Zoffer, 2016)*

Ultimately, summing up shows that investors face pressure, which makes public companies more likely to face short-termism, as executives of the companies has also faced increased pressure for short-termism over the last years. An explanation for the origins of the short-term pressure areas are given and their evolvement over a three-year period. This project focuses on two of the main drivers, as most of the points brought forth by Ernst & Young (2014), McKinsey (2017), and (Barton, Bailey, & Zoffer, 2016), which can be summed down to pressures by stakeholders and agency costs. An argument is also that, due to this project speaking about generalities of short-termism it is hard to dig down in industry wide competition e.g. but human nature does not change between companies. However, the other factors will still be drawn in as possible merits in the evaluation of how to mitigate short-termism. Stakeholders and agency costs will be investigated below.

Stakeholders and Agency Costs:

Investors face a lot of challenges nowadays that simply was not a reality several decades ago. The world moves faster than ever with increased technological development, higher market volatility, increased media coverage, reduced trading times / costs etc. This has caused the stakeholder class to focus more on the short term in an erratic way, thus creating increased pressure in organisations that simply was not a case or to lesser extent case decades ago. An example of this is the pressure on investors to get short-term returns on the assets they manage, as they miss out on short-term value creation, which is highly valued in an investment environment. However, in the process fundamentals are forgotten (Ernst & Young, 2014).

There are a lot of stakeholders in a business all of which have different levels of interaction, interplay, and leverage power in the organisation. This makes it hard to align everyone's interests, as different stakeholders have different goals with the organisation. Investors want short-term goals realised, while e.g. suppliers and employees have long term objectives in mind. A framework for categorising the stakeholders has been developed by Mitchell, Agle, and Wood (1997, s. 872). They focus on the legitimacy, urgency, and power of the stakeholders dividing the stakeholders to be focused on in different groups.

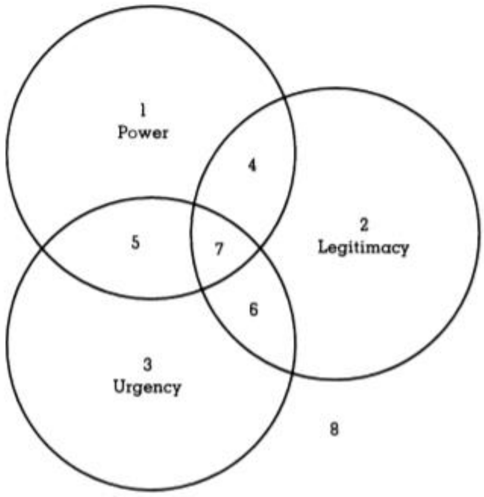

Figure 14 - Qualitative Classes of Stakeholders *(Mitchell, Agle, & Wood, 1997, s. 872)*

The numbers in the figure above represents a different kind of stakeholder, thus each number has different capabilities. There are plenty of stakeholders always interacting with or following an organisation, such as: owners, customers, employees, management, financial community, suppliers, media, government etc.

These all have different perspectives and demands, which an organisation should pay attention to. In the case of short-termism there an environment has been created that encourage it. In public companies, it has been widely recognized the owners are the one of the biggest drivers for short-termism along with higher ranking executives pressuring the rest of the organisation increasing agency costs. This is due to these stakeholder classes wanting short-term results that benefits themselves, as if they do not get short-term results they miss out on potential returns.

The fact also is that through the identification framework of Mitchell, Agle, and Wood (1997, s. 872), these stakeholders hold all three identification values. The urgency involved in getting short-term results. The power to do something about their wants. The legitimacy of being an owner or employee in the company, thus giving them a way to act on their desires. The result is stakeholders handling on their own behalf rather than the organisation causing short-termism to blossom and increasing agency costs. Examples can be budget manipulation, the increased transparency as results of being a public company, shareholders executing on their pressure by shorting / selling stocks, cutting short on research and development spending, short-term limiting training of staff to improve budgets, or influencing a faster shift in executives etc. Summed up these factors can be put in categories as shortened executive employments, neglected investments, and human capital sacrifices (Ernst & Young, 2014). An outline of the pressure put on organisations by investors and the nature of CEOs reaction in response to the short-term focused environment can be seen below.

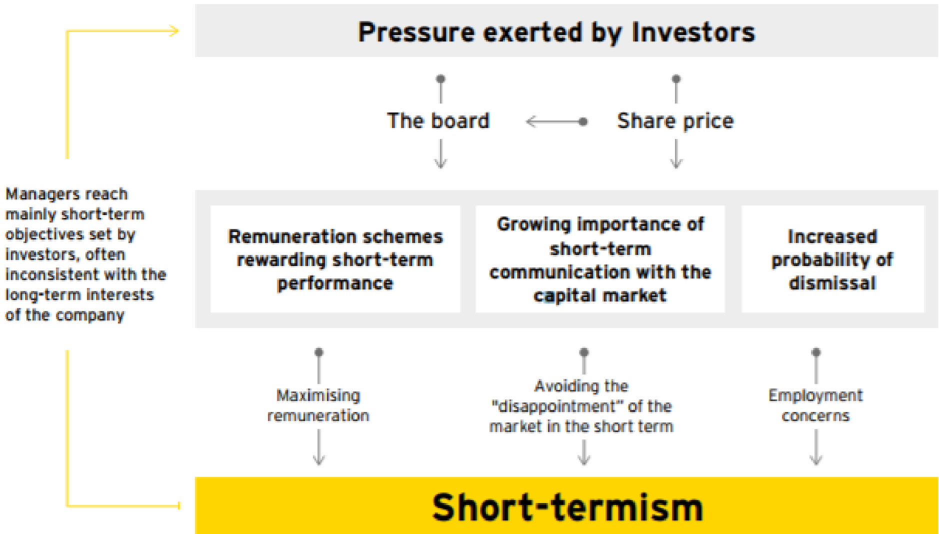

***Figure 15 - The reactions of CEOs to the pressure on short-term profits exerted by investors** (Ernst & Young, 2014)*

As it can be seen the company do not have a lot of choices regarding handling with a long-term objective to the pressures of the owners.

The consequences of short-termism are as explained in this project widespread: from limited company performance to society lacking behind. Drivers has been explained above where there has been a focus on owners and agency costs arising from the situation resulting in limited future performance. Below, possible mitigations for these trends will be investigated.

Research Question 5: What can non-private equity firms learn from these practices and tools to mitigate short-termism?

The aim of this research question is to tie the project together in the sense that the lessons learned from the private equity portfolio companies will be used to bring forth practices and tools, which can possible mitigate short-termism in public equity companies. The arguments for learning from private equity are plenty. Kim (2011) and Zang (2012) shows in a study that "public equity firms are more likely than private equity firms to opportunistically alter normal operations to improve earnings by cutting research and development spending, by pushing sales through discounts and promotions, and by lowering costs of sales through overproduction." (Kim, 2011). Thus, the pressures and need to perform in public companies makes them more prone to short-termism hindering future performance. While there are cases of private equity portfolio companies altering operations, it is a part of a long-term strategic decision according to Kim (2011, s. 6). Summing up public equity companies are more likely to alter operations through earning management, even though it impacts future firm performance negatively. Private equity companies in some cases also alter operation, especially as debt comes closer to default, but it is more of a strategic move rather than opportunistic decision making. Thus, evidence from Kim (2011) suggest that private equity companies benefits in terms of future firm performance where public equity companies limits their future performance. Therefore, this research question sets out on a pursuit to mitigate short-termism in non-private equity firms drawing inspiration from private equity firms ending in a framework that companies can draw upon in the encounter of short-termism.

A couple of scholars, Barber and Goold (2007), have already tried to dismantle the secrets of the returns that private equity hides through a study of how the industry of private equity work. They came forth with two lessons from their paper for other types of companies.

- Adopt a buy-to-sell model.
- Adopt a flexible approach to the ownership of businesses.

The argument is that it is necessary with a flexible approach to business units and acquisitions. "willingness to hold on to an acquisition for the long term is balanced by a commitment to sell as soon as corporate management feels that it can no longer add further value." (Barber & Goold, 2007). While the approach makes public companies more agile and able to react to market changes there is also the risk that management feels the pressure of this kind of strategy and sells to soon, which might contribute to short-termism. Long-term objectives are empirically shown earlier in the project to be more productive than short-term goals. Therefore, this approach is dismissed because the focus on long-term objectives has been shown to be one of the primary sources for private equity portfolio companies success. However, there are also a few points from their study and this project agrees on. The portfolio companies "remain in the spotlight and under constant pressure to perform" (Barber & Goold, 2007), which increases the company's likelihood to succeed compared to public companies that might neglect part of their businesses. The management of both the private equity firm and the portfolio company has been made lean and focused, which "avoids the waste of time and money" (Barber & Goold, 2007). Barber and Gold (2007) argues that quick acquisitions and disposals are the way to go, while this project looks towards a long-term horizon.

Practices, Tools and Conceptualization:

Throughout the project well-resonated arguments have been made for managing with long-term objectives in mind but how should the companies go about it?

The techniques from learned in this project that other companies can learn from private equity portfolio companies will be explained below. It should be mentioned that bringing strategy to an equilibrium and balance between short-, mid-, and long-term thinking requires continued effort by the organization and first then will the benefits show.

One of the primary motivators for the short-termism are the companies' stakeholders. Public equity companies face huge pressure to perform on the short field especially from the investors, owners, board members etc., which drives the motivation to e.g. manipulate budgets quarterly. Drawing inspiration from the cases and the knowledge of Unilever leads to show that a way of getting around this pressure is to make the stakeholders that are involved in the business face that long term objectives are the focus point rather than short-term goals. In the case of private equity there is no reason to release quarterly statements, which makes quarterly budget manipulation much less likely to happen than in public companies, though it happens, however, it has been proven to part of a strategic move rather than short-term thinking (Kim, 2011). It would not be the first-time companies deal with short-term thinking stakeholders this way. As examples can be given Legal & General and Unilever. Both has stopped releasing quarterly reports on financial performance, as they believe it promotes short term thinking only attracting short-term investors. The point is to focus on things that adds value to business rather than reporting, which adds little to no value to the business. Legal & General instead releases reports every 6 months and furthermore try to get companies they invest in to stop releasing quarterly reports as well. Unilever release whenever deemed necessary. However, a stand like this costs value in the short term and in the case of Unilever it removed 22 percent of their stock price (Semuels, 2016) (Dakers, 2014) (Wallace, 2015).

A lesson taken away from how 3G Capital manages their portfolio businesses is to create a different culture than the one, which existed in the companies they bought out, unless the one being there is already efficient. An increasingly efficient culture that focuses on results were utilized. Methods utilized were the concept of meritocracy where the best is used for the position, which means the company has the available talent to grow and be better than their competitors. A way of always having the best accessible talent is through extensive training of their talents in the organisation, thus if an employee performs they will not be overlooked. One of the ways private equity portfolio stays ahead of other types of firms is the utilization of adequate individual compensation attached to relevant aspects that the individual has an influence on. However, it has been shown that in corporate context there is room for improvements in relation compensation by scholars such as Harris (2012) and Conaway (2008, s. 814-815), as the incentives tend to get undermined (Bebchuk & Fried, 2004, s. 135-136), where that is less so the case in private equity portfolio companies.

On the market side of a business there are also several takeaways from the private equity portfolio companies, which can mitigate short-termism. As explained earlier setting long-term objectives will help focus both the organisation as well as investors on the matter of fact that long-term objectives are what makes or break the company compared to competition in the long run. What 3G Capital did in their portfolio companies always depended on their situation. However, there were always one goal: to maximise future potential. With that goal in mind the portfolio companies have revaluated their strategic partnership, pricing models, business model, growth strategy, marketing, and increased research and development. These parts are all vital for the businesses long-term success and a strategy to grow puts the focus away from what actors can do in the short run to make the business look pretty.

All of this is made possible on the back of a rigorous attention to running the business efficiently. On the cost-side of the business there are one important lesson to learn from the portfolio companies: Cost-cutting and zero-based budgeting. The fresh look from outside the organisation that portfolio companies get is part of transformation process. It is hard to imagine corporate executives cutting their own perks as much as required for running the business efficiently. The way zero-based budgeting can help mitigate short-termism is to make managers less focused on previous year compared to next year. The argument is that there is no pressure to decrease budgets every year resulting in managers that can focus on what matters. It is important for the businesses implementing this kind of budgeting to define the scope of the effort as well as use technology to simplify and facilitate the process (Anderson & Schmitt, 2016). Efficiency is a quest that creates economic value both for the firm as well as society in the long run, as business icon Warren Buffet (2016) puts it: "I (Warren Buffet) believe enormously in efficiency. It's the only way living improves is to get more output per unit of input. If we did everything like we did in 1790 we would be living like in 1790." (Buffett, 2016).

Concluding in a couple of focus points companies should pay attention to and improve to get closer to the industry-leading performance some private equity portfolio companies has obtained in recent years:

- Better stakeholder communication, salience, and transparency.
- Less obsession of quarterly reports.
- Performance culture with long-term incentives as well.
- Motivate executives and employees.
- Continuous business model review.
- Organic and mergers and acquisitions growth focus.
- Reinvest in e.g. research and development.
- Zero-based budgeting along with efficient cost-cutting.

In addition to the lessons learn from private equity portfolio companies, there are now thinktanks that try to come up with ways of mitigating short-termism as well. Key points to take away from FCLT Global (2017) propositions are: Clear statements about the company's business model and how long-term value is created, specify what is competitive advantages to stakeholders, highlight how strategic goals create value long-term, tie medium- and long-term performance to bonuses (Barton, Bailey, & Zoffer, 2016).

The analysis has resulted in developing the following framework, which sets out to mitigate short-termism and promote long-term growth. It should be a continuous effort long-term committed and determined to take a stand against short-termism, as the circle shows.

The circle explains the process to companies on how to mitigate short-termism with the company in the mist of it all making ends meet. It is about being open in relation to communication to stakeholders (especially does with power, legitimacy, and urgency. Otherwise known as players), implement cash-flow creating activities (cost-cutting and zero-based budgeting), motivate employees (adequate individual compensation in a performance culture, thus reducing agency costs), reinvest (increase e.g. research and development spending), continuous business review (stay updated on the smartest path for the business both short-, mid- and long-term), and finally remembering to strike a balance between short-, mid- and long-term strategies, which again should be explained to stakeholders through communication and transparency. The framework is visible below.

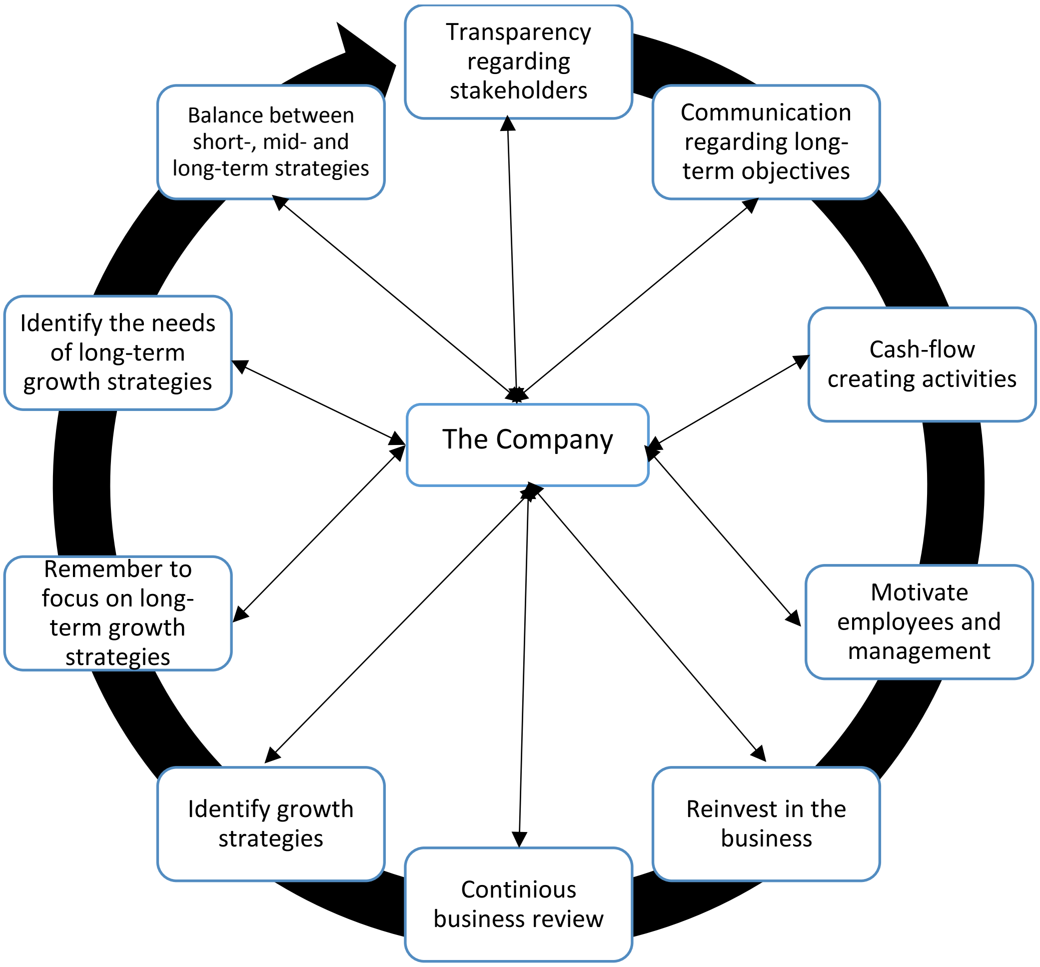

Figure 16 - Framework for mitigating short-termism Source: Own Creation

Chapter 5 – Conclusion:

The idea of the project took starting point in the subject of short-termism. Shortly, after a thought process, the subject of short-termism was connected to private equity long-term objectives forming the basis of the research problem.

Firstly, a baseline understanding of the subjects is presented. It is important to understand how private equity works to analyse and draw lessons upon their portfolio companies. The same goes for the subjects of short-termism, stakeholders, and agency costs.

The projects analysis is divided into several steps: Understanding the business practice of private equity, what private equity applied in some of their portfolio companies, what other companies can apply, understanding the subject of short-termism, and applying the analysed tools to mitigate short-termism.

The presence of private equity has been ever-growing since its inception. Lately, the number of private equity owned companies surpassed the public equity companies (worth $100 million and above). It is evaluated there are several reasons for the emergence of private equity over public equity companies, as private equity is evaluated to have some advantages regarding structure, incentives, tax, business evolvement, and the targets they select. Especially, the ability to select the ideal business and to change the business financially, strategically, and managerially is found interesting.

Two private equity portfolio companies were selected for the investigation: 'Restaurant Brands International' (Initially: Burger King) and 'Kraft Heinz Company' (Initially H.J. Heinz Company). They were both purchased by the same private equity firm, 3G Capital, that lately has been the whiz kid of the private equity world. The targets were selected carefully, even though analysts were puzzled by the Burger King deal. 3G Capital applied several practices and tools in the portfolio companies, such as tough cost-cutting, less auditing (no quarterly reports to shareholders), utilize zero-based budgeting, give adequate compensation, make a strategy for long-term growth, increase research and development, meritocracy, and revaluate business / pricing models. These tools, through good execution, caused the businesses to flourish and be industry leaders in several measures. Most notably revolutionizing the profit margin for each industry they touched, which freed up cash to pursue the portfolio companies' strategic long-term objectives.

The issue of short-termism in other types of firms is investigated afterwards to understand and how to mitigate it. Public equity companies are found by scholars to be more likely to alter operations in a way that affects future performance negatively than private equity companies, where it is often a strategic move. 87 percent of executives even say they have faced pressure to present strong financial performance within 2 years or less, and that the pressure has only increased in the last five years (2011-2016). The pressure comes from several stakeholders, increased competition, and uncertainty. However, in some cases it is also just agents acting on their own behalf.

Ultimately, utilizing a few of the strategies that has been implemented at the private equity portfolio companies might help mitigate short-termism in other types of firms. Short-term thinking is not an easy subject to take a stand against. However, here are a few ideas based on the analysis and knowledge gathered:

- Stakeholder management and communication in relation to statements and organisational direction.
- Cost-cutting with a long-term purpose in mind frees up capital to focus on factors that adds value to the business.
- Utilize the concept of zero-based budgeting, thus streamlining the costs of the organisation.
- Make everyone understand how the long-term objectives benefits the business.
- Performance culture with adequate compensation tied to relevant objectives (a proposition could be tying compensation to long-term performance) makes the business perform short-, mid-, and long-term.
- Continuously review the future strategy of the company in relation to e.g. strategy, organic versus acquisition growth, marketing.

Concluding, several practices and tools has been presented that in the future strike a better balance between short-term goals and long-term objectives. Though, these are just a few utilized in different companies in different ways, why it is necessary to evaluate a company's situation and act on the back of their issues. As an example, can be given the case of Unilever that stopped releasing quarterly reports on their performance, which initially costs the stock value but made them able to focus on long-term growth. Defining the scope of the effort and carefully explaining how it is implemented appears to be key factors but I believe there is more left to explore in other investigations with a bigger sample size, as other portfolio companies backed by different private equity funds with different philosophies might show other results. Therefore, this result should be inspiration and encouragement for businesses and not conclusive results on how to mitigate short-termism, as more research is needed in the area.

Chapter 6 – Future Works:

Hopefully, this project is an inspiration. There is a lot of room to grow in the areas of investigation. Both in the way private equity portfolio companies is managed resulting in higher performance than their peers and how to mitigate short-termism. The topic could also be viewed from other angles, such as e.g. other company iterations, difference in industries, difference in markets etc. More studies should investigate how the outside pressure on companies make them alter operations, even though it hurts future firm performance. Why is there such a disconnect between what stakeholders want on the short term and the long term? Why is it not a focus point to get the best future performance? There is little talk about this between investors, even though the empirical evidence proves that a focus on long-term objectives outperforms short-term focused companies, as e.g. short-term focused companies are more likely to alter operations negatively impacting future performance in order to meet quarterly results (Kim, 2011) (Ernst & Young, 2014) (McKinsey Global Institute, 2017). It could be interesting to apply frameworks in companies that focuses long-term rather than short-term an integrate part of running businesses, such as e.g. the Corporate Horizon Index Methodology developed by McKinsey that aims to evaluate where a company is placed regarding short-, mid-, and long-term focus in relation to its peers (McKinsey Global Institute, 2017, s. 3).

There has also been evidence short-termism is a problem in society, where investments in several areas, such as infrastructure and research and development, suffers because of budget restrictions / cuts. Areas such as infrastructure and research and development are vital for societies ability to compete (American Prosperity Project, 2017).

Chapter 7 – Limitations and critique of literature:

This chapter will focus on a few of the limitations of the project and a critique of the literature applied.

Limitations:

First off, the projects two major areas of investigation might be too much to uncover in one project, as a lot of space is utilized describing the concepts. However, the mix of different areas of business requires an approach like this, although there possibly is a more appropriate way.

The focus on private equity limits the scope of the project, where there could have been other focus points investigated as well in relation to finding tools to mitigate short-termism and additionally a different purposive sample or sample method could have been selected. Topics and inspiration for other projects could include but are not limited to: management buyouts (inspiration can be drawn from (Khan, Vilanova, & Hassairi, 2011)), reverse leveraged buyouts (take a private equity private portfolio company public, as these buyouts also shows good track records and represents 11 percent of the discarded private equity portfolio companies (Bratton, 2008, s. 526) (Phalippou & Gottschalg, 2006)), fund of funds, secondary funds, co-investment (Neuberger Berman, 2017), other private equity firms etc.

Another limitation is that there is not a lot of information available on short-termism in other types of firms than public companies. It could have been interesting to differentiate and possibly see if different strategies were needed in different types of companies.

Critique of literature:

During the literature review papers of different academic quality has been applied, as a necessity to get the necessary information. Working papers has been used in a couple of instances and a report in another, even though they have not been through the same rigorous checking process peer-reviewed journal articles go through. However, if the authors are authorities on the subject, such as Kaplan and Strömberg (2008), the information has been applied. Also, it has been investigated that the bureau publishing a paper, e.g. National Bureau of Economic Research, has no strings or has not received funding from private equity, which shows little to no bias in the research.

However, a problem in the papers has been the ability to distinguish between venture capital and private equity, which in some cases are mixed and not even distinguished. Some of the papers also follow private equity funds that focuses more on typical venture capital investments. Though, that comes down to the individual private equity firms' philosophy. Probably the biggest issue with the data is the fact that private equity firms are not obliged to report anything, making it voluntary, why some do not report anything, some report numbers that might not report reality etc. However, Thomson Reuters database (2017) is still the most complete (Thomson Reuters, 2017).

In the investigation, all available data has been applied but that has been limited. Private equity firms tend to be quite silent regarding how they run companies thus the information has been scrapped together from several interviews, reports, and newspaper articles. This however gives the opportunity for journalists to push a narrative, forget to report important points etc. Though, the most applicable data has been applied in the situations and via content analysis the project has tried to mitigate this.

Bibliography:

3G Capital. (2017, August 05). *3G Capital*. Retrieved from http://www.3g-capital.com/about.html

American Prosperity Project. (2016). *A Nonpartisan Framework for Long-Term Investment.* Aspen Institute.

American Prosperity Project. (2017, August 8). *The Aspen Institute*. Retrieved from The American Prosperity Project: https://www.aspeninstitute.org/programs/business-and-society-program/american-prosperity-project/

Anderson, R., & Schmitt, R. (2016). *Zero-Based Budgeting 2.0.* Huron Consulting Group.

Applegate, L. M. (2008, 05 14). *Harvard Business School*. Retrieved from Stakeholder Analysis Tool: https://services.hbsp.harvard.edu/services/proxy/content/20331266/20417624/228933ffcd7a490ad593b938d1bc61d1

Baertlein, L. (2010, September 2). *Reuters Global Markets*. Retrieved from Burger King agrees to $3.3 billion sale to 3G Capital: http://www.reuters.com/article/us-burgerking-idUSTRE6801CB20100902

Barbaro, M. (2011, November 12). *The New York Times*. Retrieved from After a Romney Deal, Profits and Then Layoffs: http://www.nytimes.com/2011/11/13/us/politics/after-mitt-romney-deal-company-showed-profits-and-then-layoffs.html?mcubz=1

Barber, F., & Goold, M. (2007, September). The Strategic Secret of Private Equity. *Harvard Business Review*.

Bargeron, L., Schlingemann, F., Stulz, R. M., & Zutter, C. (2007, April). WHY DO PRIVATE ACQUIRERS PAY SO LITTLE COMPARED TO PUBLIC ACQUIRERS? *National Bureau of Economic Research*, pp. 1-41.

Barton, D., Bailey, J., & Zoffer, J. (2016). *Rising to the challenge of short-termism.* FCLT Global.

Bebchuk, L., & Fried, J. (2004). *Pay Without Performance: The Unfulfilled Promise of Executive Compensation.*

Berkowitz, B., & Geller, M. (2013, February 14). *Reuters #Global Markets*. Retrieved from Buffett, Brazil's 3G team up for $23 billion Heinz buyout: http://www.reuters.com/article/us-berkshire-heinz-idUSBRE91D0PY20130214

Biden, J. (2016, September 27). *The Wall Street Journal*. Retrieved from https://www.wsj.com/articles/how-short-termism-saps-the-economy-1475018087: https://www.wsj.com/articles/how-short-termism-saps-the-economy-1475018087

Bratton, W. W. (2008). Private Equity's Three Lessons for Agency Theory. *European Business Organization Law Review*(9), pp. 509-533.

Brenner, S. N. (1993). The stakeholder theory of the firm and organizational decision making: Some propositions and a model. *J. Pasquero & D. Collins (Eds.) - Proceedings of the Fourth Annual Meeting of the International Association for Business and Society*, 205-210.

Bryman, A., & Bell, E. (2015). *Business Research Methods.* United Kingdom: Oxford.

Buffett, W. (2016, February 29). *YouTube*. Retrieved from How Berkshire Differs From 3G: Warren Buffett. CNBC: https://www.youtube.com/watch?v=5T-kAaIjSlE

Burrell, G., & Morgan, G. (1979). *Sociological Paradigm and Organisational Analysis.* Ashgate Publishing.

Cochrane, J. (2005). The Risk and Return of Venture Capital. *Journal of Financial Economics*, pp. 3-52.

Conaway, A. E. (2008). Lessons to be learned: How the policy of freedom to contract in Delaware's alternative entity law might inform Delaware's general corporation law. *Delaware Journal of Corporate Law*, pp. 789-818.

Coyne, K., Coyne, S. T., & Coyne Sr., E. J. (2010, May). When You've Got to Cut Costs - Now. *Harvard Business Review*.

Dakers, M. (2014, November 15). *The Telegraph*. Retrieved from Quarterly report quietly comes to an end: http://www.telegraph.co.uk/finance/good-news/11231685/Quarterly-reporting-quietly-comes-to-an-end.html

Daneshku, S., Whipp, L., & Fontanella-Khan, J. (2017, May 7). *Financial Times*. Retrieved from The lean and mean approach of 3G Capital: https://www.ft.com/content/268f73e6-31a3-11e7-9555-23ef563ecf9a

Davies, R. (2017, February 20). *TheGuardian*. Retrieved from How Unilever foiled Kraft Heinz's £115bn takeover bid: https://www.theguardian.com/business/2017/feb/20/how-unilever-foiled-kraft-heinzs-115m-takeover-bid-warren-buffett

Dealbook. (2010, September 2). *The New York Times - Dealbook*. Retrieved from Burger King to Sell Itself to 3G for $4 Billion: https://dealbook.nytimes.com/2010/09/02/burger-king-to-sell-itself-to-3g-for-4-billion/

Demiroglu, C., & James, C. (2007). Lender Control and the Role of Private Equity Group Reputation in Buyout Financing. *Working Paper, University of Florida*.

Devaney, T., & Stein, T. (2010). *All Business*. Retrieved from Burger King Cuts Fat in Massive Layoff: https://www.allbusiness.com/burger-king-cuts-fat-in-massive-layoff-15354235-1.html

Eden, C., & Ackermann, F. (1998). *Making Strategy: The Journey of Strategic Management.* Sage.

Ernst & Young. (2014). *Short-termism in business: causes, mechanisms and consequences.*

FCLT Global. (2017, August 07). *Focusing Capital on the long term*. Retrieved from http://www.fcltglobal.org/?lipi=urn%3Ali%3Apage%3Ad_flagship3_company%3BNzrxf4WKRp%2BlAy0UpLhvUw%3D%3D

Forbes. (2017, May). *Forbes - The World's Biggest Public Companies*. Retrieved from https://www.forbes.com/companies/restaurant-brands-international/

Freeman, R. E. (1984). Strategic Management: A Stakeholder Approach. *Boston: Pitman*.

Gandel, S. (2010, December 9). *TIME*. Retrieved from Top 10 Biz Deals - Private Equity Firm 3G Buys Burger King: http://content.time.com/time/specials/packages/article/0,28804,2035319_2035005_2035025,00.html

Gara, A. (2017, February 21). *Forbes - Investing*. Retrieved from The Rebirth of Burger King Has Made 3G Capital, Bill Ackman And Warren Buffett Over $14 Billion: https://www.forbes.com/sites/antoinegara/2017/02/21/the-rebirth-of-burger-king-has-made-3g-capital-bill-ackman-and-warren-buffett-14-billion/#1af5ed1f6566

Gasparro, A. (2013, November 14). *The Wall Street Journal*. Retrieved from Heinz, Under New Owners, to Trim Factories, Jobs: https://www.wsj.com/articles/heinz-under-new-owners-to-trim-factories-jobs-1384473385?tesla=y

Gilligan, J., & Wright, M. (2014). *Private equity demystified - An explanartory guide.* ICAEW Corporate Finance Faculty.

Gompers, P., & Lerner, J. (1997). Risk and Reward in Private Equity Investments: The Challenge of Performance Assesment. *Journal of Private Equity*, pp. 5-12.

Greene, J. C., Caracelli, V. J., & Graham, W. F. (1989). Towards a conceptual framework for mixed-method evaluation design. *Educational Evaluation and Policy Analysis*, pp. 255-274.

Gummesson, E. (2000). *Qualitative Methods in Management Research.* Sage.

Hamilton, D., Varma, P., Ou, S., & Cantor, R. (2005). *Default and recovery rates of corporate bond issuers; Technical Report.* Moody's Investor's Services.

Harris, L. (2012, February). A Critical Theory of Private Equity. *Delaware Journal of Corporate Law*, pp. 259-293.

Hill, C. W., & Jones, T. M. (1992). Stakeholder-agency theory. *Journal of Management Studies*, pp. 131-154.

Hwang, M., Quigley, J., & Woodward, S. E. (2005). An index for venture capital 1987-2003. *Contributions to Economic Analysis and Policy 4, article 13*.

Ip, G., & Sender, H. (2006, July 25). *The Wall Street Journal*. Retrieved from In Today's Buyouts, Payday For Firms Is Never Far Away: https://www.wsj.com/articles/SB115379347758516154

Ivashina, V., & Kovner, A. (2008). The Private Equity Advantage: Leveraged Buyout Firms and Relationship Banking. *Working Paper, Harvard Business School*.

Jensen, M. (1989). Eclipse of the Public Corporation. *Harvard Business Review*, pp. 61-74.

Jensen, M. C., & Meckling, W. H. (1976). Theory of the firm: Managerial behavior: Managerial behavior, agency costs, and ownership structure. *Journal of Financial Economics*, pp. 305-360.

Jiang, J. (2008, March). Beating Earnings Benchmarks and the Cost of Debt. *The Accounting Review*, pp. 377-416.

Jones, C., & Rhodes-Kropf, M. (2003). The Price of Diversifiable Risk in Venture Capital and Private Equity. *Working Paper, Columbia University*.

Kaplan, S. N. (1989). The Effects of Management Buyouts on Operating Performance and Value. *Journal of Financial Economics*, pp. 217-254.

Kaplan, S. N. (1991). The staying power of leveraged buyouts. *Journal of Financial Economics*, pp. 287-313.

Kaplan, S. N., & Schoar, A. (2005). Private Equity performance: Returns, Persistence, and Capital Flows. *Journal of Finance*, pp. 1791-1823.

Kaplan, S. N., & Strömberg, P. (2008, July). Leveraged Buyouts and Private Equity. *National Bureau of Economic Research*, pp. 1-35.

Kenny, G. (2014, 03 06). *Harvard Business Review*. Retrieved from Five Questions to Identify Key Stakeholders: https://hbr.org/2014/03/five-questions-to-identify-key-stakeholders

Khan, H. U., Vilanova, L., & Hassairi, S. A. (2011, June). Effects of Private Equity Investment on the Decisions of European Companies to go Private: An Empirical study. *International Journal of Management*, pp. 493-508.

Kim, Y. (2011). *The influence of public equity ownership on earnings management through the manipulation of operational activities.* UMI - Dissertation Publishing.

Kleintop, J. (2012). *Weekly Market Commentary - LPL Financial Research.* LPL Financial.

Kuada, J. (2014). *Research Methodology - A Project Guide for University Students.* Samfundslitteratur.

Legal & General. (2017, 05 22). *Legal & General Investment Management*. Retrieved from http://www.legalandgeneralgroup.com/investors/lgim.html

Lerner, J. F., Hardymon, F., & Leamon, A. (2004). *Venture capital and private equity: A casebook.* John Wiley & Sons.

Li, Z., Davis, J. H., Kinniry, J. F., & Wicas, N. W. (2004, Summer). Private Equity Performance Measurement and Its Role in a Portfolio. *The Journal of Wealth Management*, pp. 27-34.

Ljungqvist, A., & Richardson, M. (2003). The Cash Flow, Return, and Risk Characteristics of Private Equity. *NBER working paper #9495*.

LPL Financial. (2017, May 22). *LPL Financial*. Retrieved from https://lplfinancial.lpl.com/

Matsunaga, S. R., & Park, W. C. (2001, July). The Effect of Missing Quarterly Earnings Benchmark on the CEO's Annual Bonus. *The Accounting Review*(3), pp. 313-332.

Maze, J. (2016, November 17). *Nation's Restaurant News*. Retrieved from How Burger King and 3G Capital are putting pressure on competitors: http://www.nrn.com/blog/how-burger-king-and-3g-capital-are-putting-pressure-competitors

McCaston, M. K. (2005). *Tips for Collecting, Reviewing, and Analyzing Secondary Data.*

McKinsey Global Institute. (2017). *Measuring the economic impact of short-termism.*

Metrick, A., & Yasuda, A. (2007). Economics of Private Equity Funds. *Working Paper, Wharton Business School*.

Mitchell, R. K., Agle, B. R., & Wood, D. J. (1997, 10). Toward a Theory of Stakeholder Identification and Salience: Defining the Principle of Who and What Really Counts. *Academy of Management*, pp. 853-886.

Munshi, N., & Daneshkhu, S. (2015, March 26). *Financial TImes*. Retrieved from 3G cost-cutters struggle over food sales: https://www.ft.com/content/abd94220-d3d6-11e4-a9d3-00144feab7de

Neuberger Berman. (2017). *IQ.* Retrieved from http://www.nb.com/documents/public/en-us/neuberger_berman_investment_quarterly_spring_2017.pdf

Nocera, J. (2012, June 22). *The New York Times*. Retrieved from Burger King, the Cash Cow: http://www.nytimes.com/2012/06/23/opinion/nocera-burger-king-the-cash-cow.html

Norris, F., & International Herald Tribune. (2004, July 9). *The New York Times*. Retrieved from Fund books loss on RJR after 15 years: A long chapter ends for Kohlberg Kravis: http://www.nytimes.com/2004/07/09/business/worldbusiness/fund-books-loss-on-rjr-after-15-years-a-long-chapter.html?mcubz=1&_r=0

NPR. (2016, October 7). *Planet Money - The Economy Explained*. Retrieved from Investigating the Wells Fargo Scandal: http://www.npr.org/sections/money/2016/10/07/497084491/episode-728-the-wells-fargo-hustle

O'Cathain, A., Murphy, E., & Nicholl, J. (2007). Integration and publications as indicators of 'yield' from mixed methods research. *Journal of Mixed Methods Research*(1), pp. 147-163.

Pennsylvania CPA Journal. (2016, November 28). *Pennsylvania Institute of Certified Public Accountants*. Retrieved from Zero-Based Budgeting: Building for Sucess Again, and Again, and Again: https://www.picpa.org/articles/picpa-news/2016/11/28/zero-based-budgeting-building-for-success-again-and-again-and-again

Peterson, H. (2017, June 12). *Business Insider Nordic*. Retrieved from How a 36-year-old Wall Street prodigy saved Burger King: http://nordic.businessinsider.com/how-wall-street-prodigy-daniel-schwartz-saved-burger-king-2017-6?r=US&IR=T

Phalippou, L., & Gottschalg, O. (2006, September). The Performance of Private Equity Funds. *Univeristy of Amsterdam, Faculty of Economics and Econometrics, Finance Group*, pp. 1-58.

Phillips, G., Heller, J., & Coleman-Fenn, C. (2016). *Short-Termism and its Potent Influence on Corporate Culture at Financial Firms - The Octopus in the Room.* PF2.

PrivCo Knowledge Bank. (2017, May 24). *PrivCo*. Retrieved from Private Equity and Venture Capital: http://www.privco.com/knowledge-bank/private-equity-and-venture-capital

Reed, M. S., Graves, A., Dandy, N., Posthumus, H., Hubacek, K., Morris, J., . . . Stringer, L. C. (2009). Who's in and why? A typology of stakeholder analysis methods for natural resource management. *Journal of Environmental Management*, pp. 1933-1949.

Roberts, D. (2013, August 15). *Fortune - Careers*. Retrieved from Carlos Brito: (Brew)master of the universe: http://fortune.com/2013/08/15/carlos-brito-brewmaster-of-the-universe/

Saunders, M., Lewis, P., & Thornhill, A. (2009). *Research Methods for Business Students.* Pearson Education.

Savage, G. T., Nix, T. H., Whitehead, C. J., & Blair, J. D. (1991). Strategies for assesing and managing organizational stakeholders. *Academy of Management Executive*, pp. 61-75.

Semuels, A. (2016, December 30). *The Atlantic*. Retrieved from How to Stop Short-Term Thinking at America's Companies: https://www.theatlantic.com/business/archive/2016/12/short-term-thinking/511874/

Strauss, M. (2015, April 27). *The Globe and Mail*. Retrieved from Cost-cutting strategy a boost for Tim Hortons, improves operations: https://beta.theglobeandmail.com/report-on-business/combined-tim-hortons-burger-king-results-miss-analyst-estimates/article24135140/?ref=http://www.theglobeandmail.com&

Strauss, M. (2015, March 26). *The Globe and Mail*. Retrieved from Tim Hortons borrows Burger King's global expansion plan: https://beta.theglobeandmail.com/report-on-business/international-business/tim-hortons-borrows-burger-kings-global-marketing-plan/article23649354/

Strömberg, P. (2008). The New Demography of Private Equity. *Working Paper, Swedish Institute for Financial Research*.

Suchman, M. C. (1995). Managing legitimacy: Strategic and institutional approaches. *Academy of Management Review*, pp. 571-610.

The Data Team. (2017, February 21). *The Economist*. Retrieved from 3G's purchases and their profit margins: https://www.economist.com/blogs/graphicdetail/2017/02/daily-chart-17

Thomson Reuters. (2017, 05 03). *Venture Capital and Private Equity*. Retrieved from https://www.thomsonreuters.com/en/products-services/financial/venture-capital-and-private-equity.html

Timmons, H. (2015, March 24). *Quartz*. Retrieved from Kraft Foods is said to be near a $40 billion takeover by a Brazilian private equity firm: https://qz.com/369462/kraft-foods-is-said-to-be-near-a-40-billion-takeover-by-a-brazilian-private-equity-firm/

Wallace, T. (2015, December 11). *The Teleraph*. Retrieved from Legal and General scraps quarterly reporting: http://www.telegraph.co.uk/finance/newsbysector/epic/lgen/12045164/Legal-and-General-scraps-quarterly-reporting.html

Weber, M. (1947). *The theory of social and economic organization.* New York: Free Pass.

Wilson, N. (2015, August 29). *The Telegraph*. Retrieved from The West is paying the price for decades of underinvestment: http://www.telegraph.co.uk/finance/economics/11832689/The-West-is-paying-the-price-for-decades-of-underinvestment.html

Woodward, S. E., & Hall, R. E. (2003). Benchmarking the returns to venture capital. *NBER working paper #10202*.

Zang, A. Y. (2012, March). Evidence on the Trade-Off between Real Activities Manipulation and Accrual-Based Earnings Management. *The Accounting Review*, pp. 675-703.