Blueprints for enduring value:

The case for private equity

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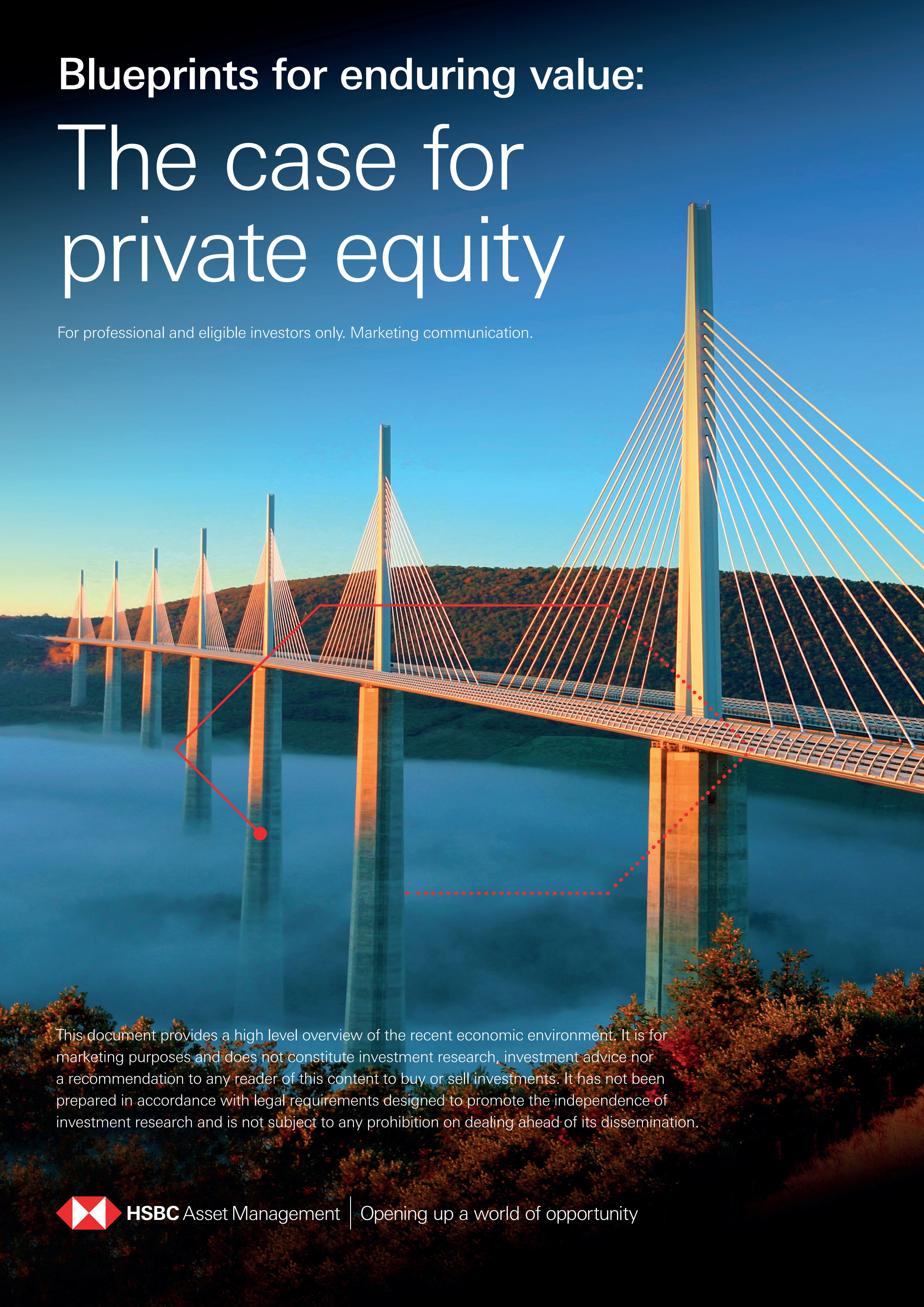

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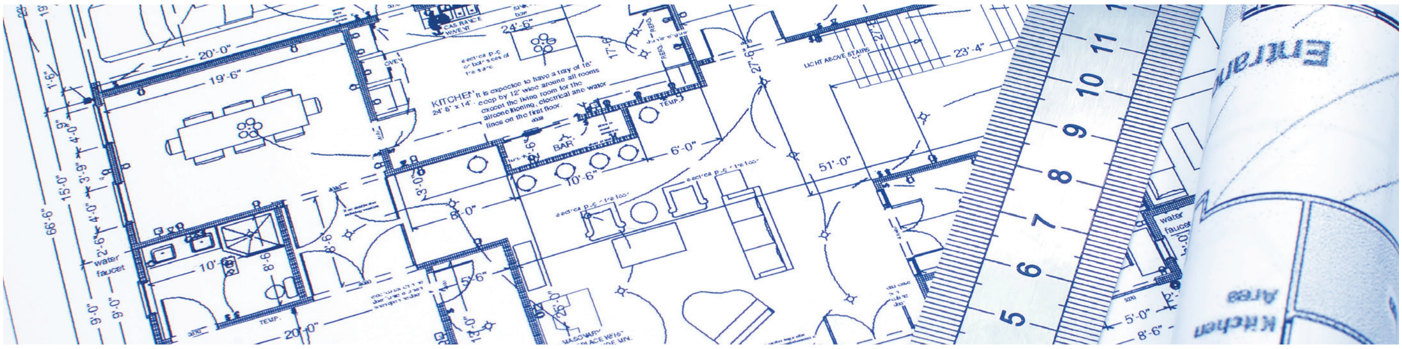
Today's global investment landscape has rarely been more complex and changeable. Geopolitical realignment, trade tensions, and other policy shocks, are combining with AI, the energy transition, and other disruptive forces to create a volatile investment environment.

In these conditions, the benefits of patient capital are clear. Rather than passively react to volatility, investors need a blueprint for growing and future-proofing their portfolio. Private equity allows investors to achieve long-term resilience through active ownership, disciplined governance, and the ability to create enduring businesses across market cycles.

Private equity managers are like skilled architects who plan strategically, construct systematically, and build to endure. This paper explores why the time-tested traditional closed-ended model of private equity can potentially deliver robust value creation for investors.



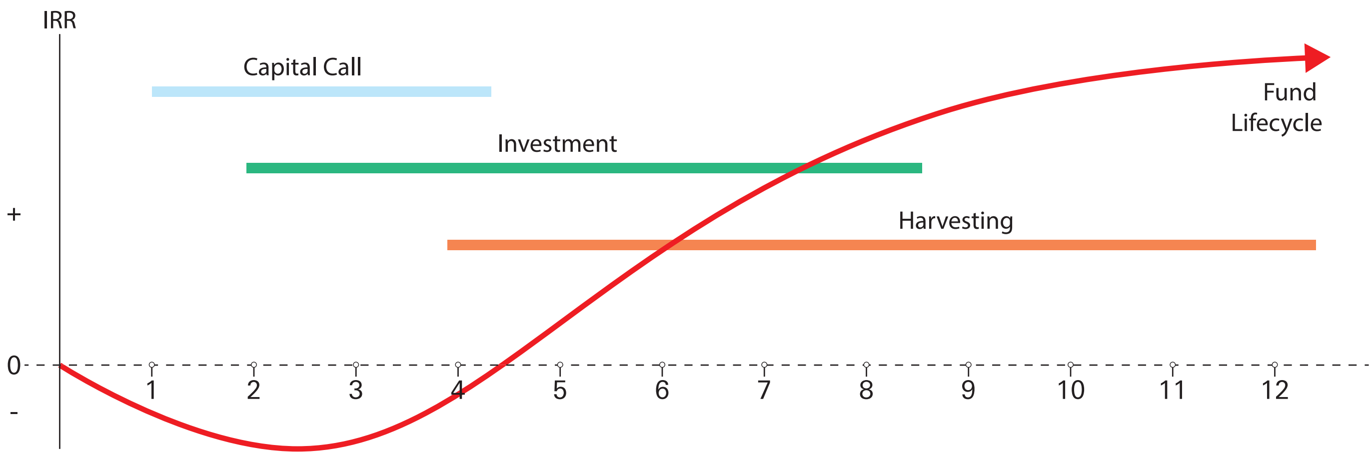
Back to basics

Understanding the traditional private equity model

A traditional closed-ended drawdown fund has a fixed lifetime of around 10-12 years. Investors (limited partners, or LPs) commit capital at the outset, which is then 'drawn down' periodically as the private equity manager (general partner, or GP) identifies attractive investment opportunities. The GP works closely with acquired portfolio companies to enhance performance.
Over time, the expectation is that these improvements translate into more durable cashflows and higher valuations.

As the portfolio matures, the GP seeks to realise investments, commonly through trade sales, M&As, IPOs, or secondary buyouts. The proceeds from such sales are distributed back to LPs and the expectation is that LPs recycle some or all distributions into new fund vintages. Early outflows and delayed inflows create the familiar J-curve pattern of returns as negative cashflows in the early years are offset by rising distributions and as investments mature.

Figure 1: Private equity J-curve pattern of returns



Source: HSBC Asset Management (2025)

This model explicitly separates long-term value creation from market volatility and rewards patience, discipline, and active ownership. These are the hallmarks of private equity's enduring performance advantage.

How do private equity managers generate value?

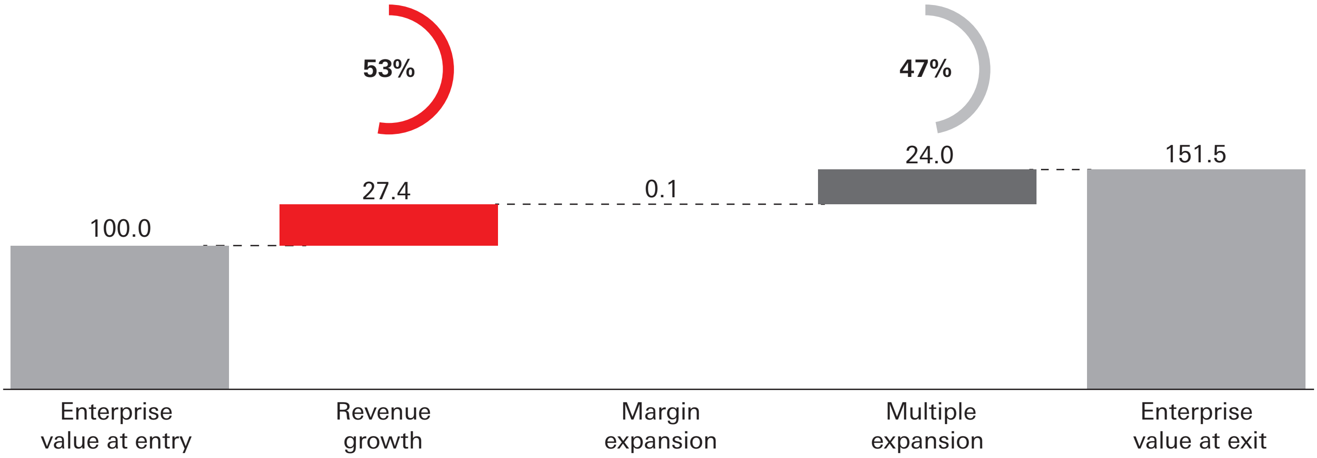
Private equity managers have a variety of ways to create value among their portfolio companies.

- **Revenue growth:** GPs have different levers to grow revenues, including fund a company's expansion, restructuring management, improving operations, and pursuing strategic growth initiatives, like entering new markets or making acquisitions.
- **Multiple expansion:** GPs can sell a company at a higher valuation multiple than they bought it for. This is possible if the GP can increase margins and revenue, professionalise operations, acquire attractive companies, or exit investments under favourable conditions.
- **Margin expansion:** GPs can boost earnings EBITDA through improving operational efficiency, cost reduction, and increasing productivity by automating processes with AI, for instance. Margin expansion can also be achieved through enhancing revenues via strategic pricing, sales performance management, improving procurement, and acquiring companies to create synergies.

Research reveals that over the last decade, private equity buyout funds, on average, have largely ignored margin growth as a driver of value and have focused on multiple expansion [1].

1 Private Equity Outlook 2024: Industry Trends', Bain & Company (2024) Private Equity Outlook 2024: Industry Trends | Bain & Company

Figure 2: Median indexed value creation drivers for global buyouts (Deal entry years 2013 – 2023)



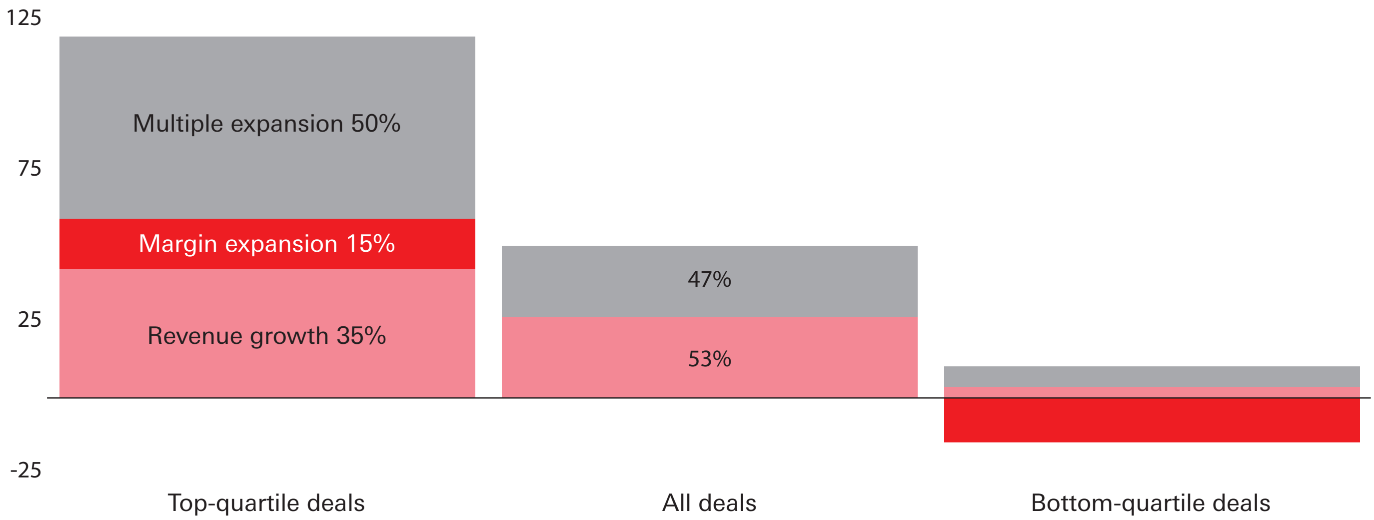
Notes: Indexed to enterprise value at entry; includes fully and partially realised global buyout deals by year of entry; includes deals with invested equity capital of $50 million or more; excludes real estate; all figures US dollars.
Sources: DealEdge powered by CEPRES data. Bain analysis.

Source: Bain Capital (2025)

As the chart above shows, for global buyout funds in the decade to 2023, revenue growth contributed to 53% of value creation, multiple expansion contributed 47%, and margin expansion the very small remainder.

However, when focusing on the top-quartile buyout deals, we see a different mix. While multiple expansion represents half the upward movement in the enterprise value of their portfolio companies, margin improvement plays a significantly larger role than it does for the average fund.

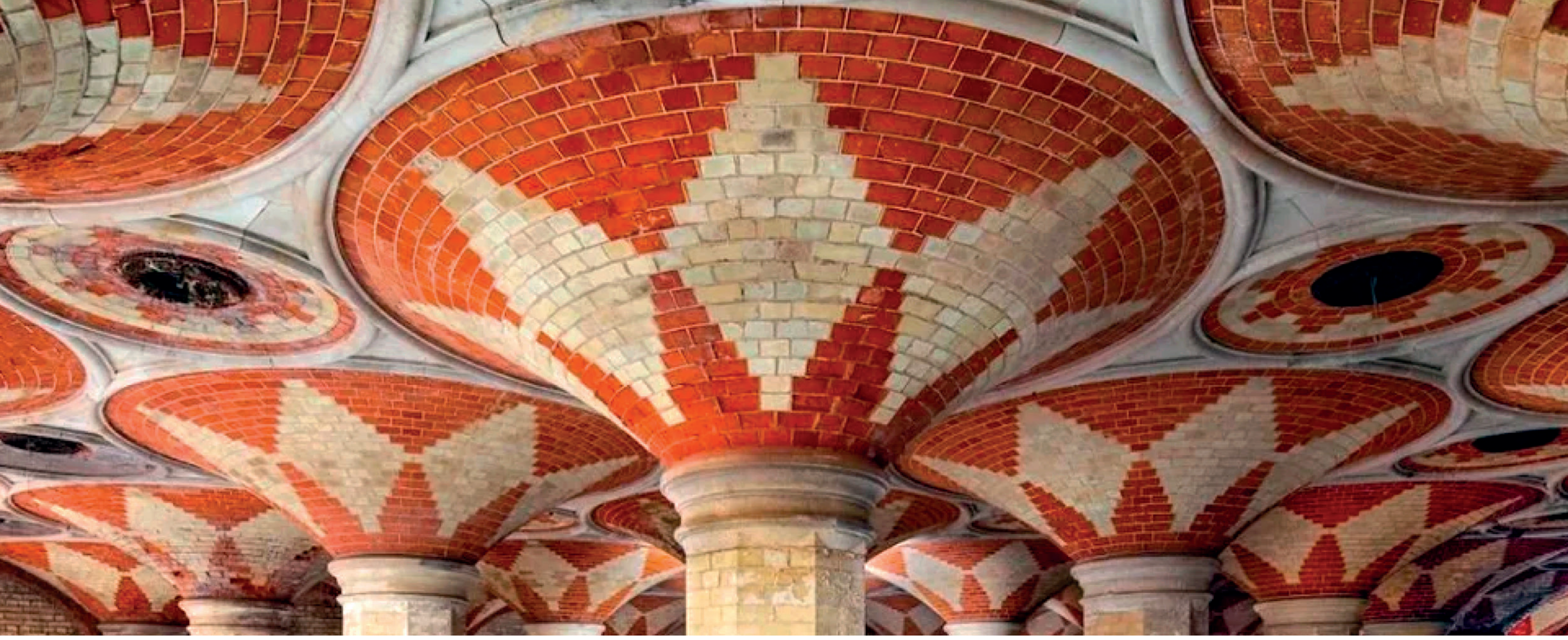
Figure 3: Median indexed value creation drivers for global buyouts, by quartile performance (Deal entry years 2013 – 2023)



Notes: Top and bottom quartile deals by internal rate of return; top and bottom quartiles include only deals with IRR data available; includes fully and partially realised global buyout deals by year of entry; includes deals with invested equity capital of $50 million or more; excludes real estate; all figures US dollars. Sources: DealEdge powered by CEPRES data. Bain analysis.

Source: Bain Capital (2025)

The implication is that to drive future performance, GPs may need value-creation strategies that both boost revenue and margins. LPs that align with GPs that can generate on operational improvements amid a challenging macroeconomic and geopolitical environment will be rewarded. This is particularly important if interest rates remain elevated as the multiple expansion that has fuelled buyout returns over the past decade will be more challenged.



Why invest in private equity?

The traditional closed-ended drawdown model offers several unique benefits for investors.

Long-term discipline

Just as a well-built structure is built over months or years, a differentiated and diversified private equity portfolio takes time to construct. Architects have a clear blueprint, source materials carefully, ensure foundations are robust, and test each stage of construction meticulously. Similarly, private equity managers have a clear plan for value creation, conducting careful due diligence and market research to methodically deploy capital in high-conviction opportunities over a fixed timeline. This leads to the construction of a portfolio of robust value-generative assets that can usually be exited in 10-12 years.

The advantage of a long-term disciplined approach is that there is no redemption pressure. GPs have the time and freedom to improve businesses away from persistent short-term market scrutiny. GPs can thus ride the cycle and sell into strength, supporting sustainable value creation and returns, as measured by IRR [2], and TVPI [3] or MOIC [4].

This is important when markets are challenged when public market investors can be forced sellers. For example, amid tariff-related volatility in 2025, GPs were able to focus on long-term operational value creation and positioning companies for growth.

2 IRR (Internal Rate of Return) is a money-weighted rate of return that captures the impact of the GP’s active decisions regarding the timing of capital calls, exits, and distributions over multiple years.

3 TVPI (Total Value to Paid-In) is the ratio of the total value of the investment or fund to the total capital paid in.

4 MOIC (Multiple on Invested Capital) is the ratio of the total value of the investment or fund to the initial capital invested.

Governance and control

Just as a structure is built to last using sound engineering and robust foundations, in private equity, strong governance is instrumental to building company resilience.

Unlike investment in public companies which confer only minority shareholder rights, closed-ended funds usually have direct control over key decisions, such as guiding strategy, selecting management teams, and rationalising costs. These governance rights underpin the GP's ability to make bold decisions and are the mechanisms through which company transformation can occur.

Strong governance is also key to understanding, monitoring, and managing risks. For example, the way a GP structures covenants will impact a company's leverage and debt sustainability, helping to support equity valuations.

In 2025, many GPs implemented value creation programmes to rebuild margins through digital transformation and capital allocation decisions. This was enabled by GPs having strong governance and direct control over company strategy.

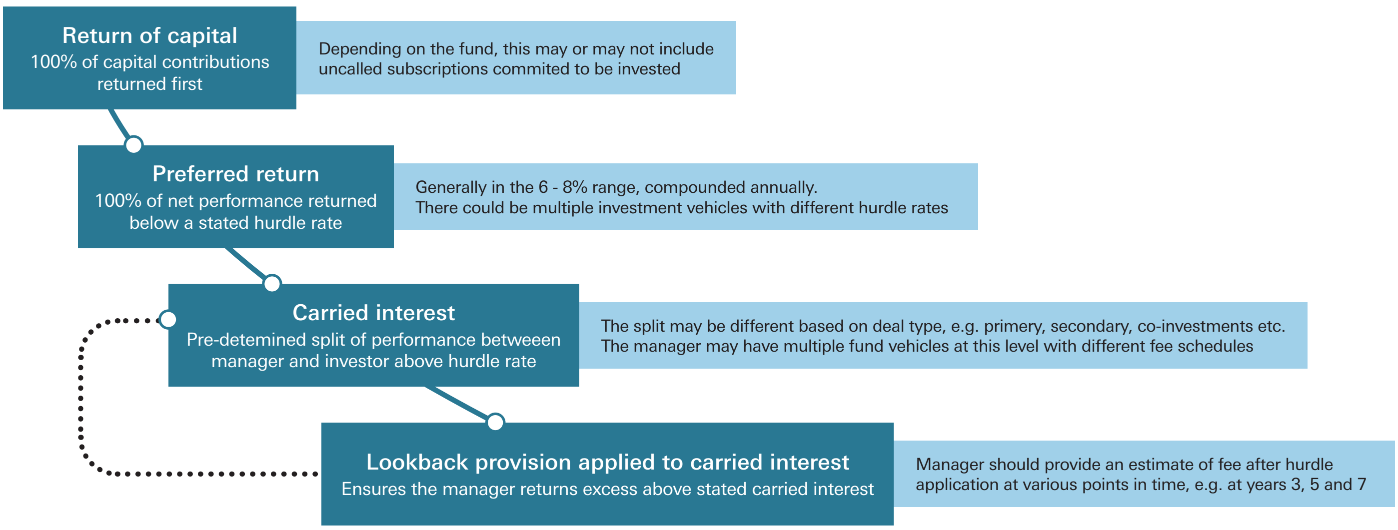
Close alignment of interests

The fee structure of a traditional private equity fund consists of a management fee (typically 1%-2.5% of committed capital or NAV) and a performance fee, also known as carried interest. Just as an architect is often paid in instalments as phases of a building are completed, GPs are paid carried interest based on surpassing certain milestones.

Carried interest, is usually charged only if the fund returns all capital contributions and then achieves a certain preferred return, or hurdle rate. The hurdle rate is commonly around 6-8% compounded annually. Some funds will also have a look-back or clawback provision, which ensures that the GP does not receive more than its agreed percentage of carried interest over the life of the fund.

The visual below highlights a typical private equity fund fee structure.

Figure 4: Private equity waterfall return of profits



Source: FineMark (2025)

The presence of carried interest ensures close alignment of interests between GPs and LPs because it incentivises GPs to focus on value maximisation.

A further way a GP can signal strong alignment of incentives is to invest significant amounts of their own assets into their funds alongside their LPs. A typical investment is 1-5% of the total fund's assets.

Cashflow predictability

As we saw earlier, traditional drawdown fund returns typically follow a J-curve pattern, with initial negative returns as capital is called turning positive as value is created, and companies are exited over time.

The Limited Partner Agreement [5] (LPA) between the LP and GP sets out key terms, including the expected life of the fund, and a schedule of capital calls, exits, and distributions.
This provides LPs with transparency and predictability of cashflows. The drawdown process ensures capital is only called when needed to invest in attractive deals, helping to minimise cash drag, thus supporting IRR.

Enabling close matching of cash flows to deal flow is particularly important when deal flow is inconsistent, as happened in 2025 in the wake of US tariffs. This contrasts with evergreen private equity strategies, where managers must maintain a steady flow of deals to deploy cash. If evergreen managers struggle to find and execute on deals, then the fund's liquidity sleeves can increase and become a cash drag [6].

The predictability of exits and distributions is another feature of the drawdown model. After a period since the COVID pandemic, which saw a bottleneck in private equity exits and holding periods being extended, traditional exit routes are steadily opening. Strategic purchases, trade sales, M&A, and IPO markets are picking up, as macroeconomic and geopolitical uncertainty wanes and interest rates are cut.

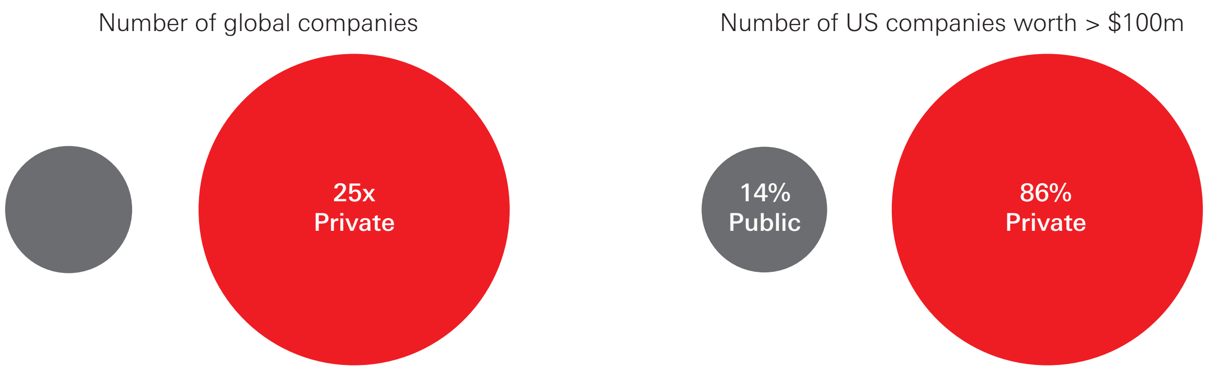
The rapid growth and evolution of the secondaries market, particularly GP-led continuation vehicles are also helping to provide an important exit route. In a secondary fund, the buyer acquires existing ownership stakes in private companies or private equity funds. Secondaries can provide sellers with earlier liquidity and quicker exits as the assets are more mature.

In summary, the cashflow profile of private equity is integral to the ability of managers to create long-term value, while also managing risk and liquidity.

Access to the huge private market opportunity set

The investable private company universe is vast. Globally, there are approximately 25 times more privately held companies than publicly listed ones [7], providing a more diverse set of opportunities across industries, geographies, and growth stages. In the US, over 86% of companies with over $100m in annual revenues are private, with the remaining 14% public companies [8].

Figure 5: Privately vs publicly owned companies



Source: HarbourVest (2025) and Blue Owl (2025)

5 The LPA is a key legal document that governs the relationship between the GP and the LPs, detailing the fund's structure, investment strategy, and terms, including capital commitments, distributions, management fees, and carried interest. The LPA also defines the rights, responsibilities, and liabilities of both the GP and LPs.

6 'Morgan Stanley tilts back to drawdown funds', Citywire (2025) Au-Yeung: Morgan Stanley tilts back to drawdown funds

7 'How does the size of private markets compare to public markets?', HarbourVest (2025) How Does the Size of Private Markets Compare to Public Markets? - HarbourVest

8 'The growing opportunity in private markets', Blue Owl (2025)

Many of today's most innovative and capital-efficient companies remain private for longer, preferring strategic partners who can help them build, rather than simply finance growth. Other companies avoid going public because of the additional investor scrutiny and burden of regulatory reporting requirements that accompany a public listing.

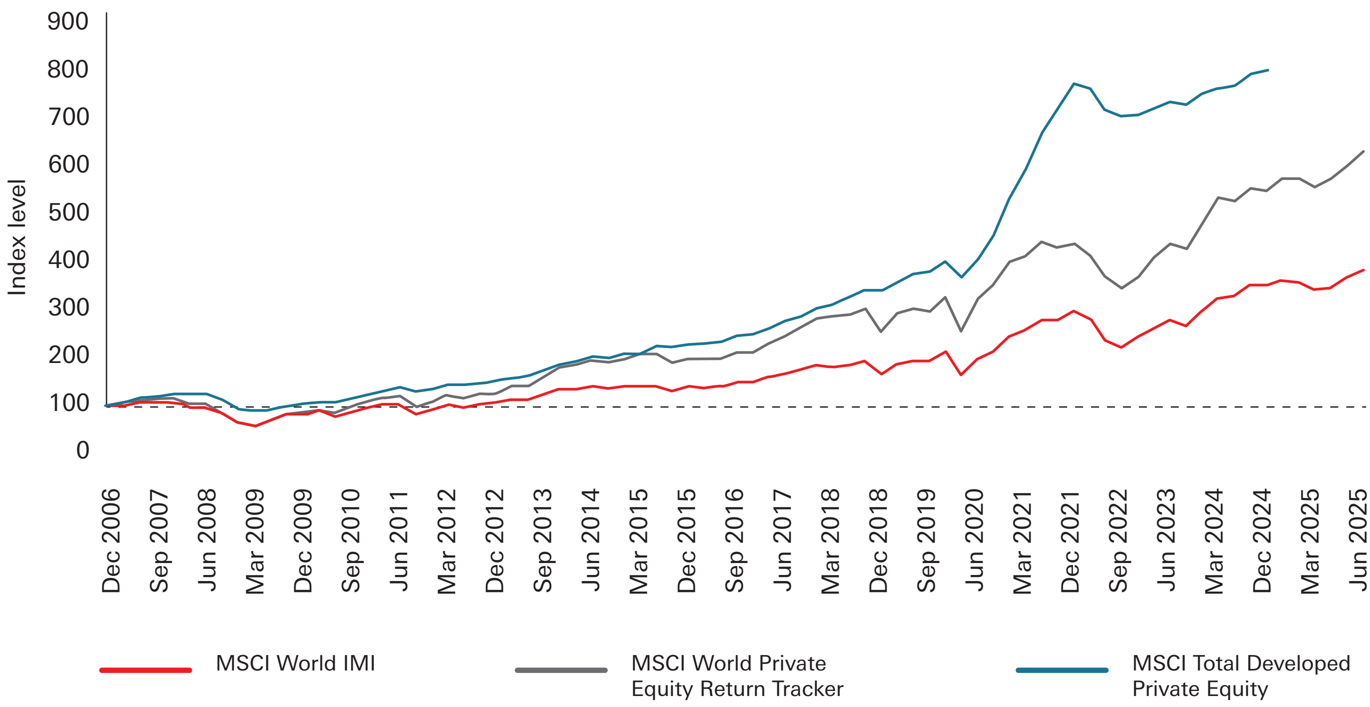
For private equity investors, this means access to the structural layers of the economy often absent from public market indices, including sector specialists, mid-market service providers, and upcoming technology platforms. The informational inefficiency within private markets provides opportunities for skilled managers to identify underappreciated and undervalued companies and transform them over the long term.

Historical track record and the illiquidity premium

Just as a well-constructed building will withstands floods and extreme weather, a differentiated and diversified private equity programme should demonstrate structural resilience to market shocks.

Recent research from MSCI finds that global private equity has outperformed public equity by about 450 basis points (bps) per year over the past two decades, with less than 100 bps due to higher leverage or market beta [9].

Figure 6: Fundamental characteristics explain a large share of private equity's outperformance



Source: MSCI (2025). The performance of the return tracker index has been intermediate to the global private and public equity markets. Index levels reflect the return in USD

Another study shows the performance of private equity funds through five previous 'crises' – the Dot-com Crash, Global Financial Crisis (GFC), Eurozone Crisis, COVID-19 Outbreak and the Return of Inflation [10]. During each of these major disruptions, global private equity outperformed the MSCI ACWI Gross Index with an average annualised excess return of 8% and outperformed the S&P 500 Total Return Index by an average of 4%. Importantly, private equity portfolios also experienced less return volatility than equities.

9 'Tracking Private Equity: Closing the Performance Gap', MSCI (2025) Tracking Private Equity: Closing the Performance Gap | MSCI

10 'Private Equity's Resilience During Major Crises: a 25-Year Analysis', Schroders Capital (2025) Private Equity's Resilience During Major Crises: a 25-Year Analysis | Institutional Investor

In two major crises – the Dot-com crash and the Global Financial Crisis, private equity generated some of its best performing vintages [11]. During the dot-com crash, private equity showed resilience, with a less significant downturn and a quicker recovery period compared to public markets. Managers capitalised on discounted valuations to yield significant long-term returns. Indeed, these were some of the strongest vintages in over two decades. Average total value to paid-in capital (TVPI) was 2.11x calculated seven years into the lifecycle of the fund.

In the wake of the global financial crisis, private equity-backed companies recovered faster and increased capital expenditure more during the crisis compared to comparable non-private equity-backed competitors. Because of this, they captured more market share and experienced higher asset growth, according to a study of almost 500 private equity-backed companies in the UK. TVPI was 1.51x again calculated seven years into the lifecycle of the fund.

Other outcomes of the GFC included enhanced governance and transparency with increasingly disciplined underwriting, for example, investors' scrutiny on valuation policy and processes. Weaker managers with poor underwriting standards failed or restructured their businesses, creating opportunities for the better managers who could withstand market cycles and distressed periods to maintain deployment discipline.

Private equity can thrive during challenging market periods for several reasons:

- GPs with adequate dry powder can take advantage of disruption to purchase cheap distressed assets and ride the cycle.
- Highly active involvement in portfolio companies helps them navigate crises more effectively than public companies.
- GPs are not forced sellers of assets in down markets, as they can continue to hold and utilise secondaries which supports valuations.
- Private equity usually invests in less cyclical, cash-generating, recurring revenue businesses (including in business services, technology, and healthcare) that are more resilient to macro shocks like the tariffs.

> "In the long-term, private equity has outperformed public equity and has thrived during challenging market periods"

11 'The secret behind private equity's strength during the dot-com crash and the great recession', Moonfare (2022) Private equity during the dot-com crash and the great recession

A private equity construction plan

Given the multiple benefits of an allocation to private equity, how can investors build a resilient private equity portfolio? Below are key considerations for investors wanting to construct a durable, diversified programme for long-term value creation.

The power of vintage diversification [12]

Committing capital across successive fund years (or vintages) reduces the risk of entering the asset class at the wrong time. This smooths the J-curve effect and creates a pattern in which distributions from prior vintages help finance new commitments. Allocating over 4-6-year periods can help avoid market timing risk, providing diversification across interest rate cycles, valuations, and exit windows, thus smoothing returns.

Secondaries can play a key role in accelerating distributions and flattening the J-curve. With secondaries, LPs can gain exposure to mature, proven assets that have a track record, helping to avoid the blind pool risk associated with primary investments. Acquiring multiple secondary stakes across sectors and geographies also allows for greater diversification than single primary investments.

An effective vintage diversification approach can turn a sequence of discrete funds into a robust self-funding programme that maintains private equity exposure over time and achieves attractive risk-adjusted returns through market cycles.

Manager selection and dispersion

The dispersion of returns between the top- and bottom-performing private equity managers can be significant and larger than that of public equity managers. It pays for investors to align with managers with stable teams that have a strong track record of disciplined underwriting, an edge in sourcing deals, and those that can realise exits effectively.

A 2025 review by McKinsey shows a 15% median IRR gap between top- and bottom-quartile private equity funds from 2012-2021 [13]. Another study finds economically meaningful performance persistence among buyout fund managers [14].

Sector allocation

Investors can benefit from allocating to sectors with clear structural tailwinds that will grow irrespective of short-term cycles and noise. Research shows that sector allocation plays a key role in private equity performance. In the MSCI study cited earlier of private equity outperformance relative to public equities, sector tilts and fundamentals explained around 200bps of the 450bps of outperformance. Aligning with a GP that chooses the right sectors is therefore as critical as manager selection.

Perhaps the most talked about sector is technology, encompassing artificial intelligence (AI), which is transforming how virtually every business operates. AI is defining the future, from automating healthcare and logistics, to powering the energy transition and financial technology.

12 Diversification does not ensure a profit or protect against loss
13 'Braced for shifting weather', McKinsey (2025) global-private-markets-report-2025-braced-for-shifting-weather.pdf
14 'Has persistence persisted in private equity? Evidence from buyout and venture capital funds', Harris et al (2025) Has persistence persisted in private equity? Evidence from buyout and venture capital funds - ScienceDirect

Private equity investing allows access to the companies building the future, not just the large-cap giants, but also the mid-size firms developing software, data platforms, and digital tools that are making whole industries far more efficient. Long-term ownership of private companies that are at the forefront of this technological progress can anchor portfolios in the growth engines of the economy.

Mid-market focus

While all areas of private equity offer attractive investment opportunities, the mid-market (usually classed as deals in the $1-$3bn range) has key advantages:

- The mid-market contains a large and diverse opportunity set of companies that drive growth and innovation in the economy, with a favourable balance of growth potential and risk. Companies of this size have potential for significant growth from levers including operational improvements, geographic expansion, and product innovation.
- Operational improvements are easier and quicker for GPs to make in mid-cap companies than larger, more complex companies due to greater control.
- Sector depth and specialisation is much easier in a mid-market approach because of the focus on smaller companies, the ability of managers to have more control, and the potential for scalability.
- The mid-market is traditionally less competitive than the large cap end due to fewer bidders and less intermediation as deals are sourced through local or proprietary connections. Entry multiples have been found by various studies to be lower than large-cap peers, allowing for greater multiple expansion [15].
- There is greater exit optionality with mid-market companies compared to larger companies, where IPOs and M&A are more likely. This is beneficial in the recent environment of subdued exits.
- Mid-market investments offer a degree of diversification for investors with large-cap public equity exposure.

All these benefits can translate into strong historical performance [16]. The most recent data shows mid-market managers achieving robust returns (9.3%) in the year to Q4 2024 [17], despite macro and policy uncertainty. Another study shows that lower mid-market and mid-market buyout funds tend to generate higher liquidity (DPI) than large cap funds in times of stability and market uncertainty alike [18].

Investors can benefit from a targeted approach focused on leading specialised mid-cap managers. Often these GPs are hard-to-access so it can be beneficial to align with an investment partner that has a wide network and strong relationships with mid-market GPs.

There are strong reasons to suggest mid-market managers will benefit significantly in coming months as tariff uncertainty recedes, interest rates fall, and market conditions improve, supporting returns and distributions.

15 ‘The mid-market: How private equity’s ‘engine room’ can drive alpha’, Pantheon (2024)

16 Past performance does not predict future returns.

17 ‘Q2 2025 US PE Middle Market Report’, Pitchbook (2025)

18 ‘Unlocking Liquidity: The Distribution Edge of Lower Mid-market Private Equity’, PGIM (2025) Unlocking Liquidity: The Distribution Edge of Lower Mid-market Private Equity

However, investors should be aware that there is potentially greater dispersion of returns and less liquidity in smaller fund sizes.

Liquidity planning

Private equity is an illiquid investment, so liquidity needs should be anticipated and proactively addressed. This is especially true in the recent environment of subdued exits.

Investors can combine different approaches:

- Map commitments to expected distributions and review pacing periodically using cashflow tools, improving cashflow resilience. This analysis can be conducted for both base case and stress scenarios.
- Implement a cash or short duration sleeve to meet calls during distribution shortfalls.
- Allocate to more mature secondary investments to accelerate cashflows.

Fees, terms, and alignment

Alignment of interests between GPs and LPs was cited earlier as a key benefit of private equity. LPs should ensure alignment through agreement with managers on reasonable fees and carry, meaningful GP commitment, and transparent GP valuation and reporting.

The Institutional Limited Partners Association (ILPA) Private Equity Principles emphasise alignment, governance, and transparency and its templates standardise performance and cashflow reporting enabling LPs to compare GPs on a like-for-like basis [19].

To ensure alignment, investors should scrutinise GPs on their practices carefully. Two examples are understanding use-of-proceeds for GP NAV facilities to generate liquidity and agreeing fee terms for co-investments.

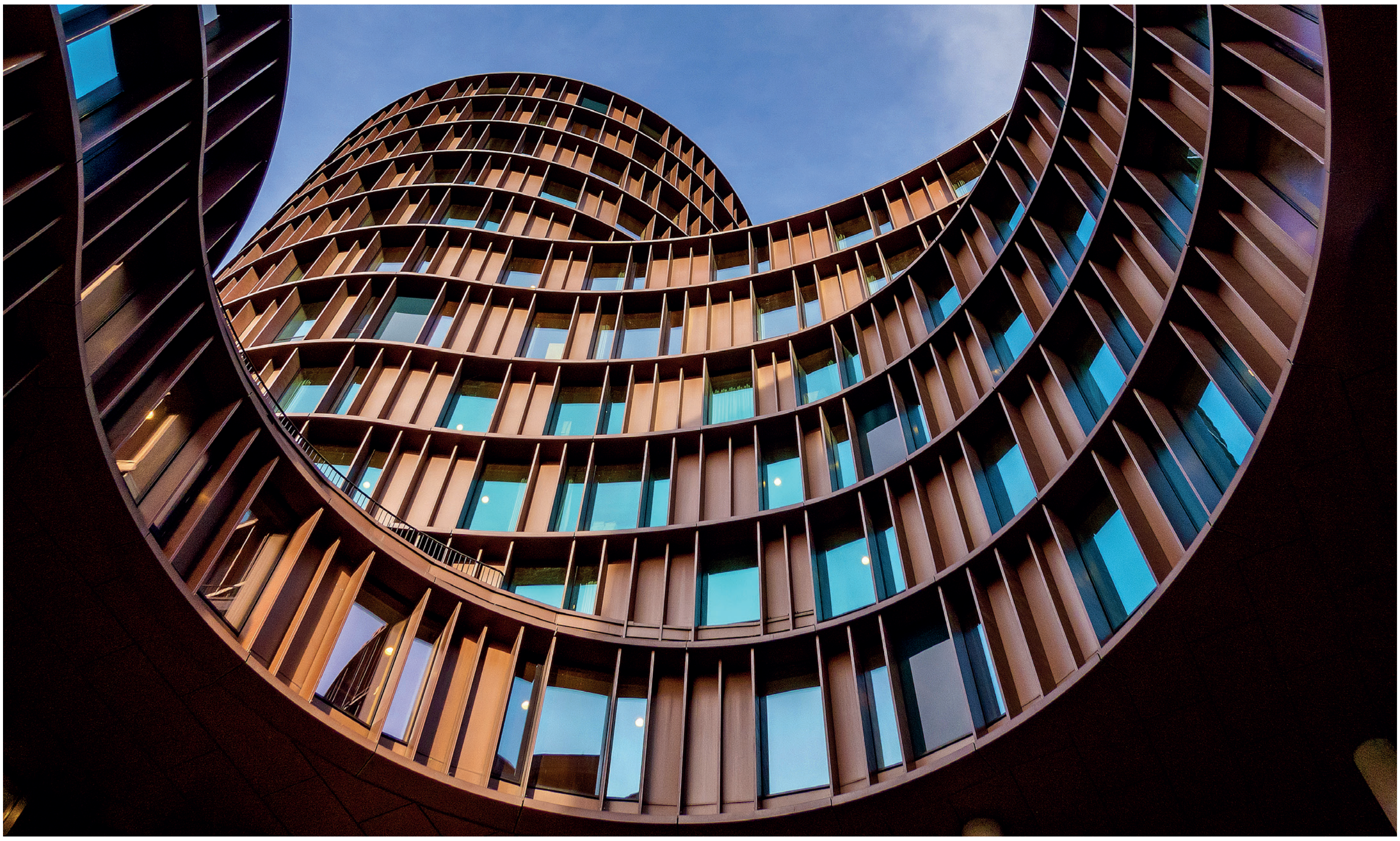
19 'Overview of ILPA's Private Equity Principles', ILPA (2025)

Co-investments

In co-investments, the LP takes a minority stake in a company alongside the GP. This allows the investor to gain direct exposure to growing companies with greater transparency and typically lower risk and lower fees (sometimes no fees) compared to a traditional fund investment. The LP can use co-investments to tilt their portfolio towards a particular sector and/or geography, while leveraging the GPs control and governance framework.

While co-investments have multiple benefits, LPs should ensure they are not concentrating risk exposure excessively and that the GP is enforcing the same due diligence standards as the GP's main funds. Service Level Agreement terms should be clear in terms of decision making and how and why such co-investment deals are allocated among LPs.

As co-investments become increasingly popular among LPs, there has been a trend for GPs to seek LPs that are 'solution providers', rather than just capital providers. These are LPs with execution capabilities and the required internal infrastructure that can co-underwrite, take syndication, and more actively partner with the GP. LPs that can play this role are more likely to access attractive co-investment deals.



Conclusion

The traditional closed-ended private equity model has endured for decades because it aligns long-term capital with active ownership and strong governance. Private equity managers can not only withstand market volatility, but also leverage it at challenging times, to generate sustainable value. For investors seeking portfolio resilience and attractive long-term returns, private equity remains a time-tested structure in modern investing.

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