How profitable is private equity?

What is the purpose of this article?
This article enables a discussion regarding the profitability of PE (Private Equity) funds. The focus is on traditional PE funds with a fixed liquidation date. Much, but not all, of the data is about buyout PE funds.

The audience for this article includes: LPs (Limited Partners), GPs (General Partners i.e., PE fund managers) and PE fund portfolio company leaders.

This article does not provide tax, legal or financial advice.
You must do your own research and fact-based analysis using current and relevant information.

What are the critical learnings in this article?
1) The traditional PE equity value creation model appears broken. For 40 years the approach has been financial leverage and increasing the price to EBITDA multiple. This approach now often appears to fail.
2) The future is impossible to predict. The future is uncertain. The future cannot be predicted by extrapolating historical trends.
3) Successful GPs and LPs will be those who have the desire and ability to transform themselves.

What types of companies get PE investments?
1) The company is well established and mature. There is a long operational and financial history. The company revenue is often in the $100’s of millions.

How many years does a PE fund exist before it is liquidated, all of its investments sold, and cash distributions to LPs completed?
1) I’ve often read that a PE fund lasts for 10 years. But what are the facts?
2) At the end of 2024, the average age at liquidation was about 15 years. [1]

Some recently launched PE funds have target lifetimes of 15 to 20 years or no fixed end date.

How profitable have PE funds been?
#1 If you had the talent to assess GPs and could predict managers would be successful, you could have had excellent returns. But many LPs did poorly or lost money.

#2 PE has outperformed the S&P Small Cap 600 and Russell 2000 by about 6% per year in the past 5 and 10 years. It’s been about 3% per year outperformance in the past 15 years. [2] Many PE portfolio companies are comparable in size the companies in the S&P Small 600 600 and Russell 2000.

#3 What have been the IRR returns for PE funds?
What were the IRR results for fund launched from 2000 to 2007, based on Q4 2024 data. [3]
LPs lost money or had poor returns in bottom decile funds. Top quartile funds did well.
1) The yearly IRR for the combined assets of all PE funds ranged from 7.81% to 22.56%
2) The yearly median fund IRRs ranged from 8.00% to 16.20%
3) The yearly bottom quartile fund IRRs ranged from 3.29% to 8.54%
4) The yearly bottom decile funds IRRs ranged from -2.68 to +2.00%
5) The yearly top quartile fund IRRs ranged from 13.93% to 22.60%

#4 What were the IRR results for North Americans PE funds launched from 2010 to 2015, based on Q4 2024 data.
I have not included the published IRR results. Why not? Many of these funds have not yet liquidated. Thus, the IRR numbers often include both actual cash returns to LPs plus hoped for future returns.

#5 How many North American PE funds have lost money for LPs?
LPs lost money, and never recovered all of their investments, in over 10% of the North American funds launched from 2000 to 2007.[4]

What have been the massive changes in the public vs private equity markets?
1) Over the past 10 years private equity has spent $900 billion taking public companies private. [5]
2) From 2000 to 2024 the number of US public companies declined from about 7,000 to 4,500. The number of PE backed companies grew from about 2,000 to 11,600. [6]
3) 61% of the stock value creation occurs prior to the IPO, leaving less value creation potential for the average investor. 85% of US unicorns that went public were unprofitable in 2023. [7]

4) 44% of the Russell 2000 companies are unprofitable. [8]
5) The conventional thinking that smaller companies outperform larger companies is not supported by facts. The Russell 2000 has been underperforming the S&P 500 and Nasdaq composite by increasing amounts over the past 20 years. E.g. over 20 years: -5.6% per year, over 10 years: -9.2% per year, over 5 years: -10.7% per year. [9]

What are the current GPs face in providing cash returns to LPs?

1) The traditional PE equity value creation model appears broken. For 40 years the approach has been financial leverage and increasing the price to EBITDA multiple. [10] This approach now often appears to fail.
2) The total PE assets appear to be greater than the capacity and demand from IPOs and operating companies.
3) There is a backlog of portfolio companies waiting for exits The assets under management have tripled since 2014 while the value of exits has remained flat, resulting in a build up of unsold assets. [11] Late 2024, global buyout funds were holding about $3.6 trillion of unrealized value in about 29,000 unsold companies. [12]
4) To provide capital returns, GPs: are borrowing money to give to LPs or selling some assets to the GP 's continuation fund. [13] (the cash from LPs investing in the continuation fund can be given to LPs in the original fund.) Most existing investors in a PE fund decline the option to roll over their investment in a continuation fund run by the same GP. [14]
5) There different points of view regarding portfolio companies sold to a continuation fund. Some believe these portfolio companies have major profit growth potential and they should be retained. Others believe these portfolio companies have few or no buyers and thus are being sold to avoid a write-down.
6) LPs are getting return on capital by selling their interest in a fund to a third party. This is a secondary investment. Online marketplaces are emerging to enable LPs to sell their PE fund investments.

What will the future look like?

1) The future is uncertain and impossible to predict. The future cannot be predicted by extrapolating historical trends.
2) The future will be turbulent, with unforeseen major crisis.
3) The future will be even faster changing: technology, what customers perceive as urgent needs and problems, global political environment.
4) Competition will become even more fierce. Competitors will grow even faster, fuelled by unlimited capital.
5) Historical knowledge, skills, experience, and facts will become obsolete even faster.

What are the implications of the future upon GPs?

1) Increasing equity value by financial leverage and multiple increase will have limited applicability.
2) The knowledge, skills, experience, facts, and software of many GPs has become obsolete.
3) One of the critical GP skills will be helping portfolio leaders understand customers and provide what customers perceive as a competitively differentiated value proposition.
4) Future successful GPs will be different from those who succeeded in the past.
5) GPs will have to transform themselves.

What are the implications of the future upon LPs?

1) The knowledge, skills, experience, facts, and software of many LPs have become obsolete.
2) LPs will have to be able to assess which GPs will be able to transform themselves and transform their portfolio companies.
3) LPs will have to be able to assess which GPs have the talent needed to succeed in the future.
4) LPs will have to transform themselves.

Why will most GP and LP leadership transformations fail?

1) The main reasons for failure are psychological and cognitive.
2) Leaders succeeded due to the success of their past mental models. In a very different future, those mental models are no longer valid. It is often impossible for leaders to consciously recognize this.
3) Leaders, like most people, keep repeating what they know how to do and what has proven to work in the past.
4) The leader is trapped by their own expertise.
5) Leaders often like to be perceived as decisive and correct. Their ego makes it difficult to admit mistakes, to say "I don't know". Many leaders will continue to make decisions without listening, learning, and unlearning.
6) Transformation is inhibited by cognitive biases such as: status quo bias (preference for no change), loss aversion (failures are more emotionally acute than successes), over confidence in their own judgement and abilities.
7) Many leaders are afraid to fail. It takes courage to do new things with no certainty of success.

What are your next steps – as an LP?

1) Define the words/concepts you're using, in a glossary. I've seen major confusion when the same words mean different things to different people. Different data sources will have different definitions.
2) Document your future cash flow requirements, with scenarios.
3) State your overall investment thesis.
4) Define your asset allocation mix and criteria for changing the mix.
5) State your private equity investment thesis.
6) Describe future scenarios.
7) Determine the required GP talent, skills and tools needed to be successful.
8) Assess GPs against talent requirements.
9) To do fact-based analysis you may have to: pay for access to databases, interview GPs and their portfolio company leaders, analyze the GPs data room, and utilize AI tools.
10) When looking at IRR – determine the IRR of cash to LP, excluding hoped for returns.
11) When looking at NAV, four possible additional metrics about portfolios are cash received if the company was: IPOed, sold to an operating company, sold to a secondary buyer, or sold to the GPs continuation fund.

Footnotes

[1] "Private Equity in 2025: The outlook for fundraising, deals, and performance" , Preqin, January 05, 2025
https://www.preqin.com/news/private-equity-in-2025-the-outlook-for-fundraising-deals-and-performance

[2] "Private Equity Can Add Diversification to Your Public Index Holdings", page 6, iCapital, 2025 July 16
https://icapital.com/category/insights/private-equity/

[3] " Private Equity PitchBook Benchmarks Q4 2024", Page 19,PitchBook
https://pitchbook.com/news/reports/q3-2024-pitchbook-benchmarks-with-preliminary-q4-2024-data
[4] ibid., Page 23

[5] "Private Equity Can Add Diversification to Your Public Index Holdings", page 5, iCapital, 2025 July 16
https://icapital.com/category/insights/private-equity/
[6] ibid., Page 5
[7] ibid., Page 5
[8] ibid., Page 5
[9] ibid., Page 6

[10] "Bridging Private Equity's Value Creation Gap", page 2, McKinsey, 2024 April 12
https://www.mckinsey.com/industries/private-capital/our-insights/bridging-private-equitys-value-creation-gap

[11] 2025 Global Private Equity Report – Bain, Page 4,6
https://www.bain.com/insights/topics/global-private-equity-report/
[12] ibid., Page 17

[13] What is a continuation fund? A GP creates a new fund, managed by the GP. Some assets are sold to the new fund. LPs have the option to receive cash or roll over their investments into the new fund.

[14] Kobi Kastiel, Yaron Nili "The rise of private equity continuation funds", Chicago Booth Stigler Center January 2024 page 1
https://www.chicagobooth.edu/research/stigler/research/-/media/5d46328c68e0466b9787f42d98275f3b.ashx

What further reading should you do?

How profitable is angel investing? Koor and Associates
https://koorandassociates.org/selling-a-company-or-raising-capital/how-profitable-is-angel-investing/
How profitable are search funds? Koor and Associates
https://koorandassociates.org/selling-a-company-or-raising-capital/how-profitable-are-search-funds/
How profitable is venture capital? Koor and Associates
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Your company will fail? Koor and Associates
https://koorandassociates.org/avoiding-business-failure/your-company-will-fail-v1/
What are the core components of talent? Koor and Associates
https://koorandassociates.org/creating-business-value/core-components-of-talent/

LP (Limited Partner) assessment of a fund. Koor and Associates
https://koorandassociates.org/selling-a-company-or-raising-capital/lp-limited-partner-assessment-of-a-fund/