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ORGANIZATIONAL INNOVATION IN PRIVATE EQUITY BACKED COMPANIES

By

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ABSTRACT

Coherently with the aims of this XXXVI Italian Congress of Regional Sciences regarding the drivers used by policies to promote the SMES' competitiveness, this study focuses on the match between the supply of non banking credit and the demand of these funds. According to my opinion, one of the most significant and, meanwhile less discussed so far, tool to promote the SMES' competitiveness has been represented by public and private investments in innovation which right now in Italy have been below the minimum fixed by Lisbon 2014 agreements.
In order to fence off this weakness, Italian policies have started to drive up the channelling of non banking credit to manufacturing sector most innovative by the promotion of different funds such as Italian fund rotating for technological innovation and fund for finance to innovative companies.
Funds of coinvestment between public and private have been also selected to stimulate private to invest in R&D spillover ting up the public supply of credit's to private equity funds which are going to invest in high tech companies.
Although this polices have been promoted, the lack of math between the supply and the demand of funds persists and can be ascribed to cultural resistance of entrepreneurs to involve private equity's managers inside the corporate governance because of difference in their views: the former has been oriented to self- financing in the medium term contrary to the latter who want to maximize the return of investments in the short term.
This research aims to draw a comparison between the private equity backed companies (PEBCs) and non private equity backed companies (non PEBCs) in order to realize if the private equity could improve the financial performance of target companies and their organization.
Furthermore, regarding the corporate governance of PEBCs it will be investigate if the cash flow rights and control ones assigned to PE's managers could be influence the decision making of the entrepreneur and could raise potential conflict of interests with him.
This study shifts the focus from the structure of private equity market to the companies which have been financed by private equity selecting the private equity as variable to discriminate innovative companies with those which are not.

KEY WORDS

Private equity backed companies, innovative firms, financial performance, corporate governance and business' organization

INTRODUCTION

This research aims to conduce a business' analysis regarding private equity backed companies distinguishing itself from the ordinary literature on private equity and venture capital which has been based on the analysis of the structure of funds such as Investment Management Company (usually IMCO), investment phases and disinvestment of private equity investors (PEs) and their comparison in different countries.
This study shifts the focus from the financial prospective regarding the supply of credit to management prospective focused on the analysis of financial performance and organization of these companies which raise money from private equity.
Private equity backed companies (PEBCs) are compared with non private equity backed companies (non PEBCs) in terms of financial performance, corporate governance and organization in order to realize if private equity could improve their financial performance and their strategy by the support of private equity's managers. Finally, it will be investigate if private equity's participation could widen the supply chain of target companies and improve their information system.
This analysis wants to be a critical thinking to the literature which considers private equity as a driver for the growth of industrial companies not bearing in mind that the longevity of relationship between private equity investors and industrial companies is short.
According to the minority of literature, the short length of the relationship between private equity investors and companies does not represent a driver for the company's growth rather a credit channel alternative to bank loans provided that strategies of private equity will be concentrated to build up value for the target companies over a short term rather than a long term perspective.
Although there is an increasing discussion on the potential managerial benefits which private equity could bring to a company such as the monitoring of operation systems and the management of resources, I think that the main reason which leads companies to raising funds is the need for capital. Furthermore, the speculative investment of short-sigh strengthens the interpretation of private equity and of venture capital as an alternative channel for capital raising rather than as a driver for the company's growth since an investment plan oriented to build up economic value requires a long time and, therefore a greater involvement of private equity. On the contrary, the investment of the private equity into industrial firms represents instead an indicator of the innovative capabilities of these latter and of the potential of their market and it can be interpreted as an indicator capable to distinguish between innovative firms and non-innovative ones.
Although there is scarce literature about the correlation between private equity and innovation, many economists have explained that it is the innovation potential inside the company to attract private equity investments rather than being the private equity a driver for innovation of the firm.
According to Engel and Keilleback (2008), the positive correlation between investment and innovation depends on the fact that institutional funds finance more frequently innovative venturing rather than companies which have low technological innovation and little potential in the future. This proves that the private equity funds are not the drivers which stimulate the ability and capacity of companies to innovate because they invest in companies that have already developed innovation before raising funds.
Furthermore, a recent Italian survey (Casellis S., 2008) carried out on 153 private equity backed companies over the period from 1995- 2004 has verified the impact of private equity investments on the progress of business. Two hypotheses were tested: 1) if innovation had already been introduced

in the venture before the arrival of private equity funds 2) if the funds, once arrived, were used in the development of innovation or if they just exploited it. After collecting data, the results confirm that private equity investors are looking for companies which have already been exploring innovation and have high growth perspectives. Moreover, the results show that private equity exploits the innovation rather than being involved in the development of new innovative projects.
As a logical consequence, it can be affirmed that private equity backed companies represent innovative business while non- private equity backed companies are less innovative.
Once the distinction between innovative businesses and non- innovative ones has been drawn, these two categories will be compared in order to realize if the private equity could improve the financial performance of target companies and their organization.
Furthermore, regarding the corporate governance of PEBCs it will be investigate if the cash flow rights and control ones assigned to PE's managers could be influence the decision making of the entrepreneur and could raise potential conflict of interests with him.

1 FINANCIAL PERFORMANCE OF PEBCs IN THE ITALIAN SCENARIO

In this part, it will be discussed if the involvement of private equity inside companies improves their financial and income performance respect to those companies which do not raise money from private equity, bearing in mind that the financial structure of Italian SMEs over the period from 2008- 2014 has experienced high levels of undercapitalization, due to bank-loan dependency, high financial charges and an important investments' decrease.
The problem to verify seems to be that PEBCs had a better performance than non private equity backed companies.
This analysis has been hold on the sample built from the PEM 2013 (private equity monitor 2013) which includes 261 PEBCs and 456 non PEBCs. In order to avoid some of the limits regarding the criteria to sample the companies, PEM chose 2 non private equity backed companies per each private equity backed company which operated in the same sector over the period 2006- 2010.
The business dimension is tested through active and net assets, the income performance is registered by revenues, Ebitda, Ebt, profit, Roe, Roa and Rosf and finally the financial solidity is proved by net debt, capital turnover, liquidity ratio , solvency ratio and debt out of equity ratio.
As indicated by the table (Table 1), the amount of business is greater in the PEBCs than in non PEBCs in terms of active and net assets. This is coherent with the role that private equity plays inside target industrial companies provided that injections of capital are used by board of directors to invest into new intangible and tangible assets. Furthermore, the private equity backed companies are going to be involved in new networks which allow them to negotiate with different suppliers and distributors. This boosts PEBCs' assets. As far as the book value is concerned, this results to be higher in PEBCs rather than non PEBCs because of share capital increase and extraordinary reserves.

Table 1 – Financial comparison between PEBCs and not PEBCs

Il campione include 261 imprese oggetto di private equity nel periodo 2006/2010 e 495 imprese non oggetto di private equity. Le definizioni delle variabili e le fonti sono presenti in appendice (tabella A.1). I dati finanziari sono in unità di Euro. Valori mediani tra parentesi. Test della T di *Student* sull'eguaglianza delle medie. * Significativo al 10%. ** Significativo al 5%. *** Significativo all'1%.

	Campione PE	**Campione NPE**	**Test T**
Attivo	130.154.594	7.555.880	(<0,00001)***
	(42.800.128)	(789.974)	
Patrimonio netto	39.254.902	2.460.232	(<0,00001)***
	(9.395.903)	(88.853)	
Ricavi	67.734.638	6.337.824	(<0,00001)***
	(26.798.764)	(642.785)	
Ebitda	6.854.615	519.866	(<0,00001)***
	(1.888.992)	(37.025)	
Risultato ante imposte	-9,99	32,81	(<0,00001)***
	(0,34)	(3,83)	
Risultato di esercizio	-5.651.556	221.388	(0,00938)***
	(-105.808)	(2.652)	
Roe	-10,04	4,20	(<0,00001)***
	(-1,14)	(3,12)	
Rosf	-5,74	42,81	(0,00003)***
	(1,91)	(8,52)	
Roa	-0,73	0,25	(0,53802)
	(1,42)	(2,85)	
Posizione finanziaria netta	44.572.384	1.863.929	(<0,00001)***
	(10.567.451)	(35.353)	
Rotazione del capitale	0,73	0,99	(<0,00001)***
	(0,63)	(0,87)	
Liquidity ratio	0,62	7,20	(0,0078)***
	(0,47)	(0,88)	
Solvency ratio	29,18	34,87	(0,13219)
	(26,02)	(16,4)	
Debt/equity ratio	2,73	1,71	(0,35047)
	(1,20)	(0,26)	

Source: PEM, 2013

As to the income performance, the results are ambiguous if we consider that revenues are higher in PEBCs, while Ebt (earnings before taxes), ROE and ROA are higher in non PEBCs.

On one side indeed, PEBCs' revenues result to be higher than non PEBCs' ones because of new relationships built up between target industrial companies and new clients and distributors. On the other side, private equity does not seem to improve the income performance as the table shows. Indeed, when private equity purchases shares in the target company, it increases the book value of the company itself and, as a consequence, the value of ROE goes down.

Furthermore, ROA is lower because revenues are not able to repay the amount of active which results to be significant because of external injections.

As far as the financial solidity is concerned, the PEBCs result to be less solid than the non PEBCs because they register a higher net debt and debt out of equity ratio. Indeed, the capital of debt in the PEBCs is higher than non PEBCs because of higher grade of dependence from external stakeholders.

It seems that it is not possible to confirm the starting hypothesis for which private equity improves the performance of companies because PE increases the dimension of target business, but it does not improves the income performance.

2 CONFLICTS IN THE CORPORATE GOVERNANCE OF PRIVATE EQUITY BACKED FIRMS

This paragraph aims to verify if the presence of private equity inside a company can improve its decision making regarding business strategy and investment plan in the long term. Considering that the business target is represented by SMEs and that they mostly are family business structure, the problem is to investigate what happens when the PE underwrites company's shares, looking at how PE's managers advise entrepreneurs and at which potential conflicts could arise between them. Then, it is necessary to understand if the private equity's involvement in the corporate governance can improve the quality of decision making or if it can degenerate in conflicts between the parties involved.

Indeed, the allocation of cash flow rights and control rights assigned to the private equity may improve the quality of decision making and reduce the conflicts between entrepreneurs and private equity managers. In order to verify it, the research of Cumming Douglas and Sofia Atiquah Binti Johan (Douglas and Atiquah Binti Johan, 2007) conducted on 74 European SMEs including Italy will be discussed. Furthermore, it will be possible to test if the quality of the legal system, where the target company is located, could improve or not the relationship between PEs and entrepreneurs. Finally, I will test other governance mechanisms, such as entrepreneur's experience, business risk ranking, the firm's stage of development and project innovativeness, to see if they can improve the time spent by PEs with entrepreneurs in business strategy and in monitoring the operational system and if they can reduce the potential conflict between them.

2.1. LEGAL AND CONTRACTUAL INSTRUMENTS TO ADVISE THE COMPANY AND TO REDUCE CONFLICT BETWEEN PEs AND ENTREPRENEUR

Cumming Douglas and Sofia Atiquah Binti Johan (Douglas and Atiquah Binti Johan, 2007) have conducted a research on 74 European SMEs targeted by private equity to verify if the allocation of cash flow rights, control rights and the quality of the legal system where the target business is located can improve the advice by the private equity to the entrepreneur on the business strategy and reduce potential conflicts between the parties. Indeed, while the entrepreneur wants to build up value in the long term, the private equity wants to maximize the profit in the short times since it will be exiting after few years. Because of this incompatibility of goals, each party sets up his own strategy which sometimes does not match with the other one, bringing their relationship into a conflict. Focusing on the legal and contractual instruments to advise the company, three principal problems could raise. The first concerns the allocation of cash flow rights, according the one prior research has established that efficient effort is elicited from PEs where PEs have convertible securities (convertible debt in equity) (Casamatta 2003; Schmidt 2003). The thesis is as follows. Consider non-convertible debt relative to convertible securities. If PEs used non-convertible debt, PEs could not obtain any ownership interest in the entrepreneurial firm and therefore could not typically have a financial incentive to provide effort. On the contrary, whenever PEs used convertible securities, they will obtain ownership interest into the company and will benefit from the positive income results. Therefore, PEs provide more effort and advice to entrepreneurial firms financed with convertible securities (instead of common debt).

The second variable correlated with the efforts of private equity on corporate governance regards the allocation of control rights. Indeed, theoretical work in PE finance has indicated that control rights also matter for PE's effort on the corporate governance. Control rights come from the ownership on the company acquiring by the shares. Indeed, more shares are assigned to PE and more right controls PE is going to obtain. More control rights improve PE's effort exertion.

Therefore, because of control rights, PEs are able to substitute the original manager or founding entrepreneur once that manager turns out to be inadequate as the firm progresses or develops. As a logical consequence, when PEs exercise control rights to replace the founding entrepreneur or existing manager with a new manager, conflicts are also more likely to arise between them. In addition to internal risk regarding the founding entrepreneur's skill, there is also risk regarding the feasibility of the project and the likelihood of market adoption.

Where the entrepreneur disagrees with the control rights exercised by the PE, there is also greater scope for potential conflict between the parties. These theories imply that PEs provide more effort and advice for entrepreneurial firms for which they have been allocated greater control rights and, meanwhile conflicts between them are more likely among investee firms for which the PE has been allocated greater control rights

Finally, the quality of the legal system has been selected to evaluate how this influences the quality of corporate governance of firms which have been based in.

Countries differ in terms of the strength of legal protections afforded to investors and entrepreneurs alike, including the efficiency of the judicial system, the rule of law, corruption, risk of expropriation, risk of contract repudiation, and shareholder rights. La Porta et al. (1997, 1998) have developed indices that account for the strength of each of these legal factors across countries and Berkowitz et al. (2003) have developed a " legality index", which is a weighted sum. These indices derived from La Porta et al. (1997, 1998).

There are at least three primary reasons to believe that "legality" matters in the context of managing PE—entrepreneur relationships (Leleux and Surlemont 2003). All else being equal, a higher " legality index" in a country is associated with more certain enforcement of contract terms and a clearer delineation of the rights and responsibilities of the PE and the owner-entrepreneur. Better legal systems mitigate information asymmetries associated with decision making pursuant to rights granted via contracts (con- sistent with La Porta et al. 1997, 1998; however, see also Drobetz 2002, and Bührer et al. 2005). Moreover, better legal systems provide a clearer interpretation of incomplete contracts. Contracts are by their nature incomplete, as not all contingencies and eventualities can be anticipated at the time of investment and incorporated into a written contract. Terms, items, and eventualities not considered and incorporated into contracts are interpreted by the legal system of the country of domicile of the entrepreneurial firm. Matters that govern relationships between firms and their investors depend on the quality of the legal system. Therefore, it is possible to expect that legality or legal system will mitigate the scope of PE–entrepreneur conflicts and facilitate the provision of PE advice.

2.2 FINDINGS ON DATASET ON SEVEN EUROPEAN COUNTRIES

The data were obtained by a survey conducted by Cumming Douglas and Sofia Atiquah Binti Johan (2007) following up interviews of PE fund members of the European private equity association (EPEA). In total, there is data on 121 investment rounds in 74 entrepreneurial firms from 14 PE funds in 7 continental European countries: Belgium, Denmark, Germany, Hungary, Italy, Portugal, and Netherlands (Cumming and Sofia Atiquah Binti Johan, 2007).

Table 2 (Panels A, B) depicts the data by different numbers of hours worked by the PE manager. The first column in Table 2 presents the data for all the entrepreneurial firms in the sample. The next columns break the information down by the number of hours per month spent with the entrepreneurial firm by the respondent PE, including the managing partners and their associates.

Table 2 - Summary of the data by monthly hours spent with the entrepreneurial firm. This table presents a summary of the data in terms of the average number of hours per month spent with the entrepreneurial firm by the respondent PE

	Total	Hours < 10	10 ≤ hours < 20	20 ≤ hours < 30	30 ≥ hours
Panel A					
Respondent VC hours	74	31	17	9	17
Contractual terms and legal conditions					
Number of common equity and/or warrant investments	38	18	9	3	8
Number of convertible preferred equity and/or conv. debt investments	28	12	6	2	8
Number of debt and/or preferred equity investments	8	1	2	4	1
Average VC ownership	0.29	0.31	0.26	0.22	0.32
Average VC board seats/total board seats	0.25	0.23	0.22	0.30	0.31
Number of investments with partial or no veto control	27	13	11	2	1
Number of investments with full veto control	47	18	6	7	16
Average legality index in entrepreneur's country	19.53	20.06	19.29	17.89	17.68
Project and environment related risk					
Average overall risk ranking	4.46	4.42	4.03	3.69	4.37
average ENT experience ranked on scale 1–10	6.57	6.65	6.35	6.58	6.76
Number of early (seed/start-up / expansion) Stage Investment	53	21	11	7	13
Number of late (late / buyout / turnaround) stage Inv.	21	10	6	1	4
Number of investments in high-tech industry	38	14	9	9	6
Number of investments in non-tech industry	36	17	8	0	11
Number of foreign VC investments	14	8	1	0	5
Number of domestic VC investments	60	23	16	9	12
Investment characteristics and performance					
Average number of financing rounds	1.64	1.35	1.76	1.56	2.06
Syndicated VC hours	74	46	12	4	12
Average book value ('000)	5,570	3,255	11,939	2,616	4,987
Average investment duration (months)	30.73	33.93	33.88	25.11	24.70
Number of actual IPOs	5	1	0	2	2
Number of expected IPOs	7	4	2	0	1
Number of actual acquisitions	11	2	6	0	3
Number of expected acquisitions	22	4	7	6	5

Table 2 - continued

VC Characteristics					
Number of limited partnership VCs	38	16	10	4	8
Number of bank affiliated VCs	36	15	7	5	9
Average capital under management ('000) per VC manager	17,888	21,922	18,290	24,422	23,217
VC portfolio size per# VC managers	2.15	2.97	1.06	1.72	2.00
Panel B					
Average VC advice ranked on scale 1–10					
Strategic advice	3.99	3.10	3.94	5.22	5.00
Marketing advice	1.91	1.29	1.65	4.00	2.18
Financial advice	4.64	4.65	3.35	6.11	5.12
R&D advice	0.80	0.84	0.18	1.11	1.18
Product development advice	0.88	0.84	0.41	0.56	1.59
Human resource advice	1.91	1.29	1.53	2.78	2.94
Exit strategy advice	3.04	2.74	3.53	1.56	3.88
Interpersonal support	1.66	0.94	1.76	1.67	2.88
Help in networking	2.73	1.94	1.76	3.89	4.53
Average overall advice ranking	2.39	1.96	2.01	2.99	3.25
Number of disagreements with management team					
Strategy	21	4	6	2	9
Marketing	8	1	1	3	3
Financial	11	3	1	0	7
R&D	3	1	0	1	1
Product development	8	1	1	1	5
Human resources	7	1	1	1	4
Other	1	1	0	0	0
VC has replaced founder as CEO	7	1	0	0	6
Total number of disagreements	66	13	10	8	35

Panel A presents the characteristics of the respondent VCs (type of VC, capital under management), entrepreneurial firm characteristics (legality index of the country of location, foreign versus domestic investments, stage of development, industry), transaction specific (number of hours syndicated partners, type of securities used, board composition, allocation of veto and ownership rights, number of rounds, and book value) and performance characteristics (investment duration, and the actual and expected IPOs and acquisitions). Panel B shows the average advice ranking for nine different advising fields, the number of disagreements in eight possible matters including appointing a new CEO, the number of conflicts related to exit with founder and other parties, the average risk ranking of investments for 13 different risk factors, and the average rank of the entrepreneurs' experience. Some important variables are typed bold

Source: Cumming and Sofia Atiquah Binti Johan, 2007

The first group of numbers in Table 2, Panel A, describes the most important contracting features employed in the investments in the sample. Most of the transactions are financed by convertible securities (28) or straight equity (38), but also by small number of debt investments (8). The use of convertible securities does not seem to enhance the number of hours PEs spend with entrepreneurs considering that there are only 8 companies financed by convertible securities in which PEs spend more than 30 hours, while there is a significant group of companies - nearly 18 - in which PEs spend less than 10 hours. As a logical consequence, it is possible to affirm that the use of convertible securities does not enhance advice of PEs towards entrepreneurs because there are few companies in which PEs spend more than 30 hours per month.

Board representation and the allocation of veto rights reveal however that investors are more involved in firms in which they have more extensive control. In particular, average PE board seats

out of total board seats increase when PEs spends more time with entrepreneurs. This confirms that the investors are more involved (in term of hours spent with entrepreneurs) when they have more control (in terms of PE board seats out of total board seats).

Moreover, the average number of hours spent is proportionately less when the PEs have partial or no veto controls as opposed to full veto controls. Indeed, when PE spends more than 30 hours with entrepreneurs, there are 16 companies financed by PEs with full veto controls and just one financed by PEs with partial veto controls. This means that full veto controls incentive PEs to spend more time with entrepreneurs and, therefore, to increase their advice. These observations indicate univariate support for the assumption that control rights increase the involvement of PEs in their entrepreneurial firms.

The average legality index in the entrepreneur's country is lower when PE managers spend more hours. This because worsen legal systems require PEs to spend more time with the entrepreneur. There is more contractual uncertainty. Therefore, the hypothesis according to the one a better legal system implies more trust between the parts and less relational conflicts has been confirmed. Regarding the entrepreneur's experience, the chart shows that when the entrepreneur's experience increases, PEs spend more time with the entrepreneur, proving that PEs are available to spend longer time with him when he has more skills because can create value for the company easier than less skilled entrepreneurs.

It can be observed that there are more early stage investments (53) than late stage investments (21). Furthermore, hours to support early stage investments are more than those to support late stage investments. In fact, there are 14 companies in the early stage which receive 30 hours of counselling from PEs, while just 4 in the late stage receive the same number of hours.

About half of the firms in the sample were in high-tech industries (biotech, electronics, or the Internet). There do not appear to be any differences in the involvement of PEs by industry type.

Table 2, Panel B, provides information pertaining to advice and conflict measures. A number of rankings of PE's advice is provided in the first group of indicators including strategic, marketing, financial, R&D, product development, human resources, exit strategy, interpersonal support, and help in networking. The table indicates that for most support activities, PEs report higher advice rankings if they spend a higher number of hours with the firm.

The second group of numbers in Table 2, Panel B, reports various types of disagreement between the PEs and the entrepreneur (including situations in which the PE has replaced the founder with another professional manager as entrepreneur). Most disagreements regard strategy and financial resources.

3 PE IMPROVES THE ORGANIZATION OF INDUSTRIAL TARGET COMPANIES

This paragraph tests the impact of PE on the internal and external organization of private equity backed companies according to the research conducted by Ehrlich B. S. and De Noble A. F. (2013) on a sample of SMEs which received financing from PEs.

These results are compared with non PEBCs which instead receive organizational support by PIs meaning personal investors which are not formalized as well as private equity.

Over 80% of these consisted of high tech and medium tech companies whose entrepreneurs averaged 13,4 years of experience in their respective industries and raised revenues from 1 to 5 million every year.

Ehrlich B.S. and De Noble A.F. delivered a questionnaire to entrepreneurs of PEBCs and non PEBCs in order to realize how they perceive respectively the level of participation of PEs in the first case and PIs in the latter and how they feel participation of their investors could change their business in the future. Below the results of this research are reported and these include the support by investors to entrepreneurs regarding the internal organization such as developing a professional support group, formulating business strategy, developing production and service, formulating and testing marketing plans, monitoring financial and operating performance, improving control system and formalizing the relationships with personnel. Furthermore, the table shows variables regarding the external organization as well as soliciting consumers and distributors and selecting vendors.

A one way analysis of variance (ANOVA) was utilized by Ehrlich B.S. and De Noble A.F. to locate significant differences between entrepreneurs’ perceptions about: 1) level of participation of PE in the PEBCs and of PIs (private investor) in the non PEBCs and 2) desired change of investors’ participation in various managerial activities.

Table 3 - One- way ANOVA Comparing of Amount of Participation by Investor Type

	Panel A- Level of Participation (a)				Panel b- Change in Participation (b)			
Area of Participation	**PE**	**PI**	**DF**	**F**	**PE**	**PI**	**DF**	**F**
Search of Management team	2,38	2,05	1,41	0,75	3,00	3,21	1,40	0,80
Interview/ select management team	2,46	2,00	1,41	1,52	3,04	2,95	1,40	0,18
Negotiate employment term	1,75	1,79	1,41	0,01	2,78	3,05	1,40	2,36
Interference with investor group	2,80	2,74	1,39	2,85	3,36	3,37	1,39	0,20
Develop professional support group	3,80	1,37	1,41	4,2**	3,24	3,42**	1,38	0,88
Obtain alternative debt financing	2,14	2,63	1,38	1,12	3,70**	3,74***	1,37	0,02
Obtain alternative equity financing	3,30	2,16	1,40	7,54**	3,52**	3,84***	1,38	0,88
Formulate business strategy	3,40	2,26	1,41	7,20	3,05	3,16	1,39	0,23
Develop actual product/ service	1,42	1,37	1,41	0,03	2,86	2,95	1,39	0,18
Develop production/ service	1,04	1,16	1,40	0,99	2,95	3,05	1,38	0,24
Select vendors/ equipment	4,30	1,16	1,41	8,8**	2,82	2,95	1,39	0,65
Formulate marketing plans	1,96	1,79	1,41	0,17	2,95	3,16	1,39	0,76
Test/ evaluate market plans	1,46	1,37	1,41	0,17	3,09	3,26	1,39	0,76
Solicit customers/ distributors	4,50	1,53	2,38	7,8**	3,14	3,47*	1,39	2,12
Monitor financial performance	3,13	2,67	1,40	2,13	2,82	3,28*	1,38	8,94**
Monitor operating performance	3,40	2,21	1,41	0,00	2,91	3,21	1,39	3,29
Serve as sounding board	3,42	2,58	1,41	1,87	3,24	3,79**	1,38	4,27**
Motivate personnel	1,75	1,83	1,40	1,50	3,14	3,26	1,38	0,23
Replace management personnel	1,59	1,39	1,38	0,49	2,75	3,11	1,36	3,86
Manage crises and problems	4,23	1,79	1,41	6,7**	2,90	3,32**	1,38	3,37
Improving control systems	4,30	1,80	1,40	5,8**	2,70	3,30**	1,32	3,26
Formalize relationships with personnel	4,10	1,30	2,30	5,2**	2,40	1,20	1,12	0,58

(a) Five-point scale: 1=no participation at all by investor(s) vs 5= all by the investor(s)
(b) Five-point scale: 1=much less vs 5=much more desired investor involvement
*p < .05
**< .01
***< .001

Source: Ehrlich B. S., De Noble A. F., 2013

Regarding the level of participation perceived by entrepreneurs of PEs inside the PEBCs and of PIs inside the non PEBCs, PEs have been assigned higher scores than PIs regarding the selecting vendors, soliciting consumers and distributors and the introduction of new control systems. The most significant differences between PEs and PIs regard the supply chain management, the involvement of control system and the formalization of relationship with personnel. This confirms the hypothesis according to which PEs should widen the links with new partners and increase internal efficiency better than PIs. It has been confirmed indeed that PEs allow to the industrial

target companies to be included in their networks and negotiate with new partners as well as distributors, suppliers and clients. Furthermore, the entrance of an institutionalised external stakeholder inside the share capital formalizes the relationships with personnel shifting from an informal business structure as well as Italian business families to more impersonal one.

For what concerns the expected change in participation, the entrepreneurs expect from PIs to improve the development of the professional support group, obtaining alternative financing to debt, soliciting customers and distributors, monitoring financial performance and increasing system controls. On the other hand, the entrepreneurs do not expect significant change of involvement from PEs. This means that they are satisfied of the PEs' performance while they expect more from PIs.

The research conducted by Ehrlich B. S. and De Noble A. F. showed that PEs are able to improve the supply chain of target business, its system controls and formalization of relationships inside the company better than PIs and therefore, the PEBCs should result to be more organized than non PEBCs.

This represents a stimulus for the entrepreneur to apply for a private equity's partnership as that may lead to benefit from the financing and the from organizational perspective. Indeed, control systems and the formalization of relationships with personnel improve the efficiency and cut down costs. Furthermore, the new partnerships with distributors and costumers allow companies to increase their revenues.

4 CONCLUSIONS

In Italy the public and private investments in innovation in term of growth domestic product account nearly the 0,5% below the minimum target fixed by Lisbona 2014 which has been fixed to 2%. Italian investments in innovation are such a lot lower than USA and EU average as well. Although this leaded structural reforms inside our country aim to facilitate the supply of credit by financial operators non banking such as private equity and venture capitalist, the mismatch between supply of funds and their demand persists. According to the most significant literature on the financing entrepreneurship which I agree, the problem of the deficiency of investments in innovation could be ascribed not to absence of funds but to a cultural resistance of entrepreneurs to get private equity's managers involved inside their business strategy. Coherently what I said, 4/8 funds are foreign proving that the deficiency of investments in innovation could be not ascribed to the supply of funds but cultural and managerial problems on the side of demand.

This shifts the focus from the analysis of private equity market to the companies which received their support in order to realize if private equity improves their financial performance and their organization.

Regarding the financial performance of private equity backed companies, it has been verified from the sample of Italian firms based on PEM that PEBCs grow up more than non PEBCs because they have a bigger active and book value meanwhile they result to be less solid than the latter because they register a higher net debt and debt out of equity ratio.

Regarding the stability of the corporate governance of private equity backed companies, the analysis based on the research of Cumming Douglas and Johan Sofia showed that:

- The control rights assigned to PEs, by writing of the share capital of PEBCs, improve their advice on the entrepreneurs' business strategy and reduce the disagreement with them.

Indeed, PE's managers, by attending of the board of directors, line up their goals with the entrepreneur's ones and therefore, the conflict of interest between them will decrease

- bad legal system worsens the relationships between the PE and the entrepreneur because it is not able to guarantee transparency on contract clauses

Regarding the organizational support which PEs could lead to target companies, it has been emerged from the research conducted by Ehrlich B. S. and De Noble A. F. (2013) on a sample of 70 SMEs which received financing from PEs and personal investors that:

- PEs introduce the PEBCs in new networks with new partners. On one side new suppliers represent for the PEBCs a better quality of the production and new supplying time while new distributors and new clients indicate more revenues. Therefore, the productive structure and supply chain change adopting leaner approach.
- PEs can improve the efficiency of PEBCs and cut down their costs because of better system controls
- PEs formalized the relationships with personnel and this improves the relationship inside the company between the functions

This research introduces future analysis on corporate governance and organization of PEBCs.

Regarding the stability of corporate governance of PEBCs, some limits emerged from the research conducted by Douglas Cumming and Sofia Atiquah Binti Johan (2007) on a sample of 74 businesses and 24 investment funds. Indeed, it has been showed that PEs which finance the companies by writing off shares and by acquiring convertible securities are more than the ones which support the industrial companies by financing capital of debt. Therefore, PEs increase their decision making inside the board of directors and it has been expected that they are going to dedicate much more time to the business strategy than PEs could do in the case of capital of debt. Contrary to this expectation, the data have demonstrated that PEs which have targeted industrial companies with convertible securities and shares dedicate short time to their entrepreneurs. Future researches could widen the existing sample including more PEBCs in Europe in order to verify these contradictions and to test if cash flow rights assigned to PEs increased the time spent together with the entrepreneur reducing potential conflicts with him.

In addition, it seems useful that future researches analyzed the conflict of interest between entrepreneurs and investors using different approaches from legal and contractual instruments such as perceived of unethical behaviors, bearing in mind that the objective is to enhance the relationship between them in order to create value for business in the long term.

Regarding the organization of PEBCs, it is important that future studies can be carried on in order to confirm the results obtained by Ehrlich and De Noble's research on a sample of 70 SMEs which received financing from PEs and PIs. Secondly, future researches may be worthwhile in order to realize how the organization changed after the PE had disinvested and if the entrepreneur could be able to maintain the relationships with new partners. Furthermore, these studies could investigate which strategies the entrepreneurs could have to set in order to maintain the organizational benefits acquired by PEs. Indeed, while the existing literature had studied if private equity improves the internal and external organization of target company once private equity joins the share, next researches could investigate what happened in term of supply chain management and internal organization once private equity disinvests.

The originality of this analysis is also represented by the limits of PEs rather than illustrate only their strengths which are commonly more acknowledged and discussed from current literature. The limits of PEs seems be the following:

- PEBCs result to be less solid than the non PEBCs because they register a higher net debt and debt out of equity ratio. Indeed, the capital of debt in the PEBCs is higher than non PEBCs because of higher grade of dependence from external stakeholders
- The stability of corporate governance of the PEBCs has correlated to many variables such as entrepreneur's experience, riskiness of project and phase of investment contrary to non PEBCs where corporate governance is more independent and autonomous

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