

A COMPREHENSIVE ANALYSIS FOR LIMITED PARTNERS

PRIVATE EQUITY:

Two Models and Structural Implications

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Introduction: What Private Equity Does

Private equity firms raise capital from institutional investors—pension funds, endowments, insurance companies, and sovereign wealth funds—and use that capital, typically combined with substantial debt, to acquire controlling stakes in operating companies. The academic literature has long recognized that private equity fund managers respond to high-powered incentives and seek to maximize shareholder value through a variety of channels. Yet beneath this simple description lies a profound divergence in how value is actually created — or destroyed.

The textbook private equity model is built on three pillars: leverage (using debt to amplify returns), multiple expansion (selling at a higher valuation than the purchase multiple), and operational improvement. In practice, however, the industry has fractured into two fundamentally different operating models with sharply divergent outcomes for stakeholders and the aggregate economy. The first model treats companies as assets to be extracted. The second treats them as enterprises to be built. The structural implications of these two approaches could not be more different.

Who This Paper Is For

This paper is addressed to Limited Partners — the pension funds, endowments, and institutional investors who provide the capital that fuels the private equity industry. As the principals in the principal-agent relationship, LPs bear the ultimate risk and reap the ultimate rewards. Yet LPs have allowed General Partners to exploit the principal-agent problem, optimizing for their own rent-seeking behavior at the expense of long-term capital appreciation and broader economic productivity. The structural reforms proposed in this paper are designed to correct these market failures and realign the industry with its stated purpose: the creation of genuine, sustainable economic value.

Two Models of Private Equity

Private equity is not a monolith. Across manufacturing, technology, real estate and utilities, two structurally distinct operating models have emerged — with sharply divergent consequences for workers, consumers, innovation and, ultimately, for the Limited Partners who supply the capital.

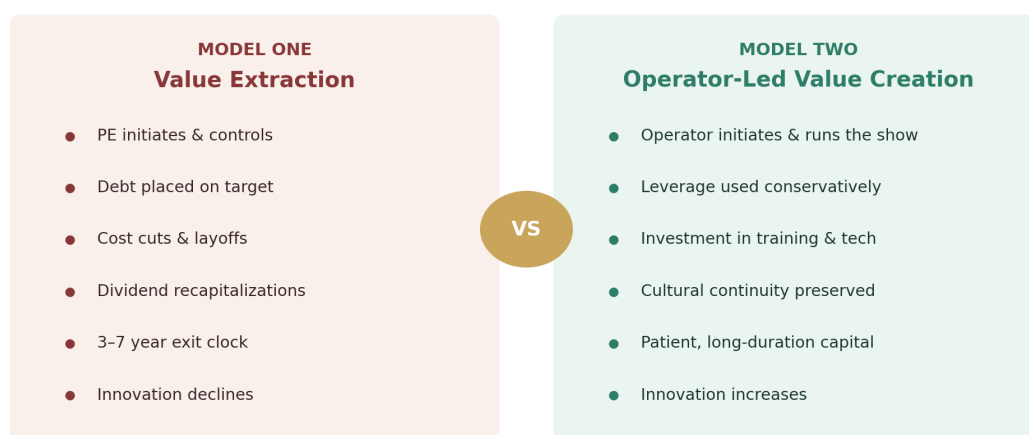


Figure 1. The two dominant operating models in private equity today.

Model One: The Value Extraction Model

The value extraction model — sometimes called the "financial engineering" or "turnaround" model — acquires companies and prioritizes short-term financial returns over long-term enterprise health. The playbook is consistent across sectors:

- **Leverage:** the acquisition itself is debt-financed, and that debt is placed directly onto the target company's balance sheet, converting the business into a cash-sweep machine that must service interest payments before anything else.
- **Cost reduction:** operating costs are reduced, most commonly through redundancies and layoffs.
- **Further extraction:** additional debt is loaded onto the company post-acquisition and valuable components are sold or partitioned. Dividend recapitalizations — forcing the company to borrow more to pay dividends to the PE firm — are a standard tool.
- **Short-term horizon:** the fund lifecycle (typically 3–7 years) dictates strategy, subordinating long-term investment in R&D, workforce development and capital infrastructure to the exit timeline.

Structural Consequences

The academic literature identifies a consistent pattern of outcomes under this model: innovation declines or becomes more narrowly focused; consumers face higher prices and reduced availability of products; low-skilled workers are hurt by automation and job cuts; and in regulated industries, the high-powered incentives of private equity magnify distortions already present in the regulatory framework.

Model Two: The Operator-Led Value Creation Model

The operator-led model inverts the relationship between capital and management. In this model, the operator initiates and runs the show; private equity is passive capital in the background.

The Operator-Led Sequence



Figure 2. The structurally distinct sequence of the operator-led model.

This model is sometimes called the "vertical rollup" or "operator-led platform" model. It consolidates fragmented businesses within a single industry into something larger and more capable. The operator is typically a seasoned executive who has run a business at scale before, and who can hold the trust of a workforce while making necessary changes.

Structural Consequences

Under this model: innovation increases, as the operator maintains R&D investment and long-term product vision; consumers benefit from greater variety and broader geographic availability of products; high-skilled workers benefit from increased IT investment and upskilling; and strategy crystallizes around the operator's vision rather than shifting with each fund cycle.

The Critical Distinction

The critical distinction is one of initiation and control. When the operator initiates, the business remains operator-centered. When private equity initiates, the business becomes extraction-centered.

The Five Structural Factors

Across both models, five factors determine the ultimate outcome for the enterprise and its stakeholders.

Factor	Value Extraction Model	Operator-Led Model
1. Crystallization of Strategy	Dictated by fund lifecycle; each portfolio company treated as an island, little continuity.	Strategic continuity, because the operator — not the PE firm — sets the direction.
2. Economic Stressors (Debt Burden)	Companies loaded with debt; converted into cash-sweep machines vulnerable to downturns.	Leverage used conservatively, as a tool for growth rather than extraction.

Factor	Value Extraction Model	Operator-Led Model
3. Cost of Doing Business (Financialization)	Sale-leasebacks, dividend recaps and complex structures multiply administrative burdens.	Financial distortions minimized; capital structure kept simple.
4. Productivity (Genuine vs. Statistical)	"Gains" are often statistical illusions from layoffs, not real productivity improvement.	Genuine productivity growth from training, technology and process investment.
5. Worker Uncertainty & Social Bonding	Labor treated as a variable cost; layoffs and loss of institutional memory are standard.	Worker dignity preserved; investment in training sustains the social fabric.

Case Studies

Manufacturing — The Pyrex Plant in Charleroi

The Pyrex glass plant in Charleroi, Pennsylvania, has anchored its river town for generations. Under private equity ownership since 2017, the plant became a textbook case of the extraction model.

In 2023, private equity-owned Anchor Hocking acquired the bankrupt plant through a complex web of shell companies, compelling strategic bankruptcies, and backroom negotiations — all designed to gobble up competition at the best possible price. The deal relied on multiple name changes, lender shifts, and shell companies to dodge FTC approval, saving tens of millions of dollars while taking full control.

The result: the planned closure of the plant, the loss of roughly 300 jobs, and the devastation of a community that had depended on the factory for generations. A federal judge temporarily halted the closure, citing the community devastation, and Senator Bob Casey called for further investigation into an acquisition that represented a merger of direct manufacturing competitors that escaped government oversight.

The Pyrex story is not anomalous. Across the nation, private equity firms have extracted value from manufacturing plants, hollowing out once-thriving enterprises through leveraged buyouts, sale-leasebacks, and talent stripping. American manufacturing has, in this telling, been transformed from a long-term enterprise into a disposable commodity.

Technology — Thoma Bravo and Medallia

The technology sector provides the most dramatic illustration of the extraction model's structural unsoundness. Between 2019 and 2021, private equity firms entered software buyouts at inflated multiples, using cheap debt financing. The collapse that followed was, in hindsight, structurally inevitable.

Medallia is the defining case. Thoma Bravo took the customer-experience software firm private in a \$6.4 billion deal in 2021. Five years later, \$5.1 billion of that value had been destroyed — the second-largest private equity loss on record. Thoma Bravo wrote down its investment to practically zero, and control of the company transferred to its lenders — Blackstone, Apollo, and FS KKR Capital — in a loan-to-own restructuring.

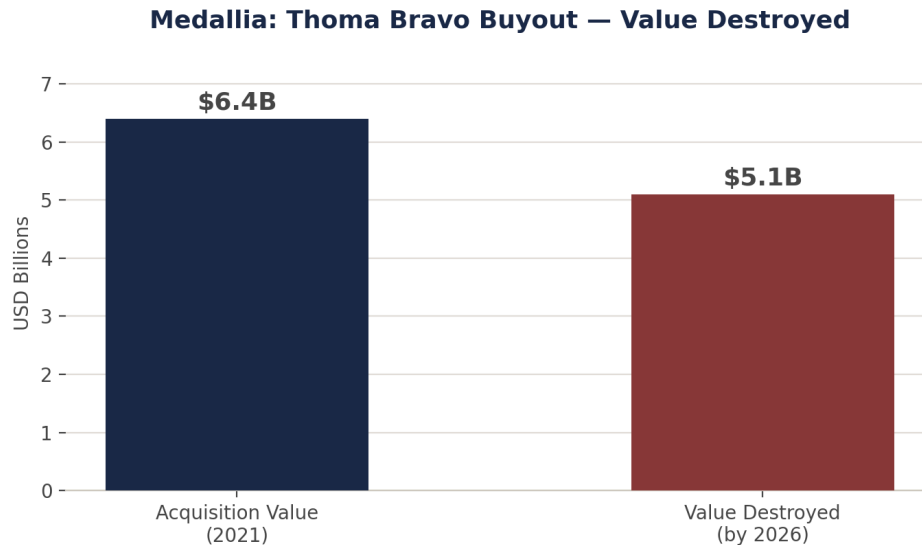


Figure 3. Medallia deal value versus value destroyed by 2026.

The factors behind the collapse were structural, not incidental: a rising cost of debt over five years, the retreat of private equity buyers who had previously been ready to make follow-on investments, and a broader slowdown in the software industry's growth.

Orlando Bravo, Thoma Bravo's founder, has publicly acknowledged that his firm overpaid. The deeper lesson, in the words of one technology-industry marketing executive, is the distinction between software built to be flipped and software built to last.

The collapse was not an isolated failure. Private credit faces its most severe stress test since the sector's rapid expansion, with business development companies trading at their deepest discounts to net asset value in more than 5.5 years. As of February 2026, distressed software loans across the private credit market totaled \$46.9 billion.

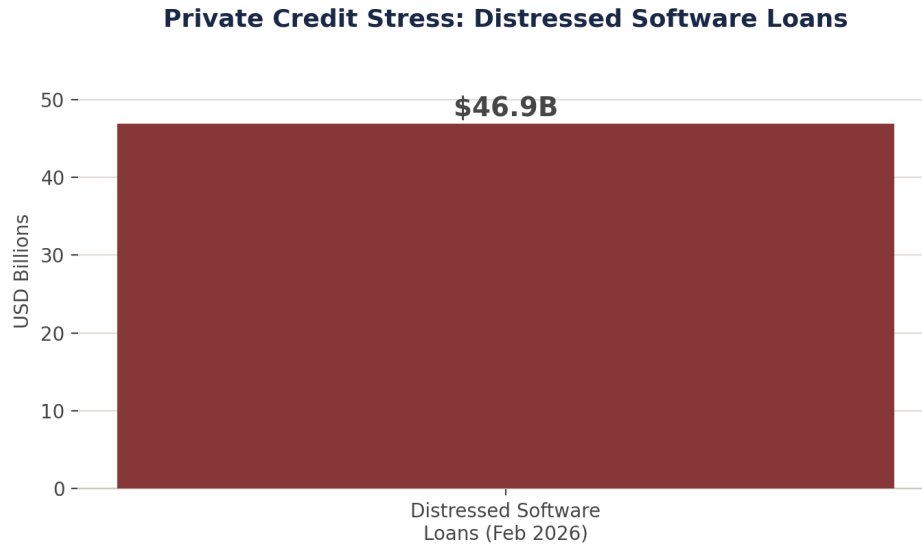


Figure 4. Distressed software loan volume, private credit market, February 2026.

The extraction model in technology destroys the very assets it claims to optimize: engineering talent, R&D capacity, and customer relationships. When the flipping stops, the value evaporates.

Real Estate — The Financialization of Shelter

The extraction model applied to real estate produces a distinct pattern of harm: treating shelter as a financial asset rather than a human necessity.

Leslie's Poolmart offers a window into the playbook. Over several decades, the pool-supply company has been passed between different investment groups as a case study in financial engineering. Despite \$1.25 billion in sales and \$440 million in gross profit, the company carried \$750 million in long-term debt. Its share price plummeted from a peak of almost \$33 in 2021 to less than a dollar in February 2026 — a decline industry observers have compared to the atmosphere at Lehman Brothers in its final days.

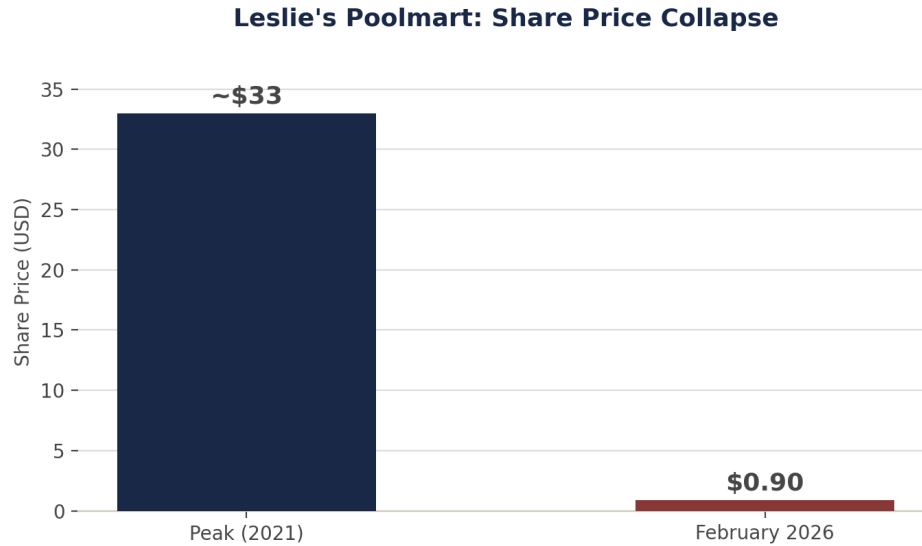


Figure 5. Leslie's Poolmart share price, 2021 peak versus February 2026.

The real estate investment trust model has proven equally fragile. S2 Capital's multifamily REIT, which owned over 9,000 units in Texas and Arizona, saw common equity lose 90% of its value by the end of 2025. The feeder fund that brought investors to the REIT warned that equity investors should expect a full loss of capital. Interest rates remained elevated much longer than industry experts predicted, allowing distress to creep into the portfolio; the same month S2 raised \$343 million for its second value-add fund, the firm lost a property to foreclosure.

The structural pattern across real estate is consistent: buy with leverage, extract through fees and dividends, and leave behind deteriorated assets, foreclosed properties, and devastated communities.

Utilities — The Emerging Frontier

The utilities sector represents the newest frontier for private equity extraction — and potentially the most dangerous, because utilities are essential services with captive ratepayers.

In 2026, a private equity-led consortium agreed to take AES Corp. private in a \$33.4 billion deal, shifting one of the largest U.S.-listed power companies into private ownership. KKR made a \$9 billion bid for UGI Corp., targeting surging AI data-center power demand. Blackstone acquired a 19.9 percent ownership stake in NIPSCO's parent company, NiSource, in 2024.

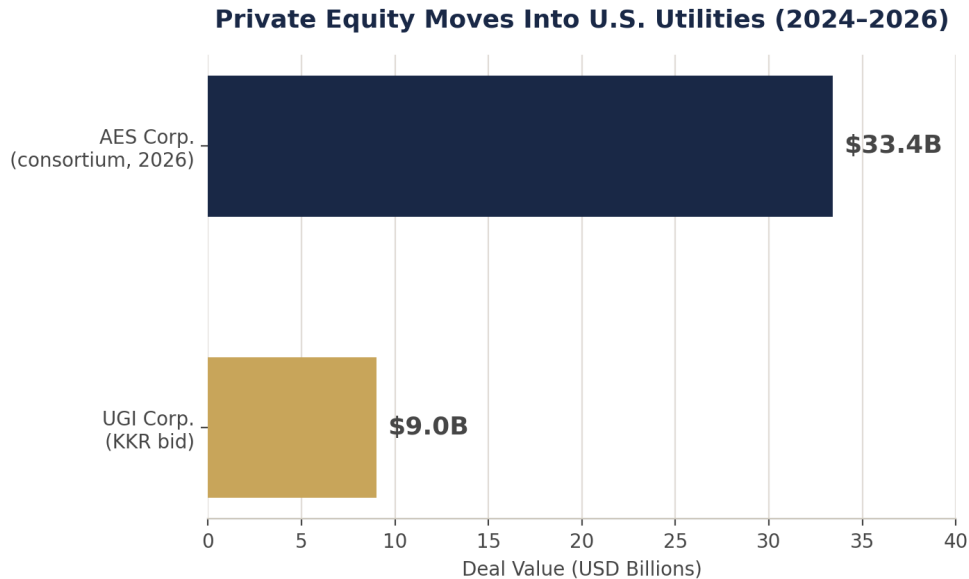


Figure 6. Selected private equity moves into U.S. utilities, 2024–2026.

The structural concern is evident: distortion in incentives created by the regulatory framework tends to be magnified when combined with the high-powered incentives of private equity. Utilities have captive ratepayers who cannot choose their provider. When private equity applies the extraction model to utilities, the costs are passed directly to consumers while the returns flow to investors.

The evidence from other regulated industries is instructive. In healthcare, for-profit education, and insurance, private equity's high-powered incentives have produced documented harm. The utilities sector, with its combination of essential services, regulatory capture, and captive customers, may prove even more vulnerable.

A Structural Reform Agenda for Limited Partners

The failures documented in the case studies above are not merely the result of bad market timing or cyclical downturns. They are the predictable outcome of misaligned incentives and structural market failures embedded in the limited partnership model itself. As Principals, Limited Partners have allowed General Partners to exploit the principal-agent problem, optimizing for their own rent-seeking behavior at the expense of long-term capital appreciation and broader economic productivity.

To correct these market failures, LPs must implement three structural reforms that realign incentives, extend time horizons, and tie compensation to realized value.

Reform One: Realigning Principal-Agent Incentives

Eliminating AUM Rents and Extending Time Horizons

The Problem

The traditional "2 and 20" fee structure creates a fundamental misalignment of incentives. By charging a fixed annual management fee based on Assets Under Management (AUM), GPs are rewarded for asset accumulation and leverage, regardless of actual performance — encouraging rent-seeking and myopic short-termism.

Between 2019 and 2021, GPs deployed capital at inflated multiples because the fee structure rewarded deployment, not returns. The larger the fund, the larger the management fee; the more leverage employed, the larger the potential carry — without regard to the downside risk borne by the underlying enterprise. This is a classic moral hazard: GPs capture the upside while LPs bear the downside. More perniciously still, the current structure permits GPs to collect carried interest on unrealized, mark-to-market valuations that are often artificially inflated through additional debt issuance, including dividend recapitalizations — meaning the GP extracts wealth before any actual cash is returned to the LP.

The Reform

- Abolish fixed management fees — transition to a pure profit-sharing model. GPs receive a percentage of realized profits only (typically 20–25% of the upside), with no fixed compensation for deployed capital that underperforms, eliminating the incentive to grow AUM for its own sake.
- Mandate 15-year fund lifespans, with the option for two 3-year extensions, so GPs internalize the long-term consequences of operational decisions. Research suggests genuine operational value creation requires a minimum of 7–10 years, particularly in sectors requiring R&D investment, workforce development, and customer relationship building.
- Segregate capital by duration and strategy — short-duration capital (3–5 years) allocated to credit, distressed debt, or rapid turnaround strategies where the risk/return profile matches the timeline; long-duration capital (e.g., pension liabilities) reserved for operator-led, strategic value creation.

Reform Two: Optimizing for Leading Indicators of Productive Capacity

Shifting the Optimization Function

The Problem

The financial engineering model treats financial returns (IRR, MOIC) as the primary target, treating the underlying business merely as a mechanism to achieve them. This is a categorical error: financial returns are lagging indicators — the historical output of a business — while the actual drivers of sustainable cash flow (human capital, R&D, customer retention, operational continuity) are leading indicators.

When GPs optimize solely for lagging financial metrics, they inevitably destroy the leading indicators to artificially inflate short-term margins:

- Firing skilled labor to reduce costs
- Cutting R&D to boost current cash flow

- Degrading product quality to increase margins
- Deferring maintenance to preserve liquidity

The Reform

- Mandate quarterly reporting on leading indicators: human capital (retention, training investment, wage growth), innovation pipeline (R&D spend, patent filings, new-product revenue share), customer health (NPS, retention, share of wallet), and operational continuity (capex/depreciation ratio, deferred-maintenance backlog, supply-chain diversification).
- Tie carry to leading-indicator performance — a portion of carried interest (e.g., 25–30%) contingent on preserving workforce stability and R&D capacity, forfeited if destroyed to achieve short-term returns.
- Internalize stakeholder externalities by requiring GPs to demonstrate, in fund governing documents, how they are preserving and enhancing human capital, customer relationships, and long-term competitive position.

Reform Three: Resolving Duration Mismatches and Liquidity Illusions

Tying Compensation to Realized Value

The Problem

The industry suffers from a severe duration mismatch: LPs deploy long-duration capital (e.g., pension liabilities) into short-duration strategies (3-to-5-year flip models), creating structural fragility. The current fee structure allows GPs to extract wealth based on unrealized "paper" valuations that are often artificially inflated by loading the target company with debt.

Dividend recapitalizations are the purest expression of this dysfunction. The GP forces the portfolio company to borrow additional funds — often at higher interest rates — to pay a dividend to the PE firm, extracting cash before the exit while the enterprise deteriorates. The LP receives a paper mark while the enterprise takes on additional debt; when that debt becomes unsustainable, the enterprise collapses, and the GP has already taken its profit.

The Reform

- Tie compensation to realized liquidity — GPs participate in profits only when actual cash is distributed to LPs; dividend recapitalizations no longer generate carry, only actual exits do.
- Prohibit dividend recapitalizations — any debt issuance must be tied to genuine capital investment in the enterprise, not extraction.
- Mandate realized-return metrics — shift the evaluation framework from unrealized IRR (which can be manipulated through valuation assumptions and leverage) to realized DPI (Distributed to Paid-In Capital), the only metric that cannot be manipulated.

The Structural Case for Reform

Market Failure	Reform	Outcome
Principal-agent misalignment	Abolish fixed fees; tie carry to realized returns	GP incentives align with LP interests
Short-termism (horizon problem)	Mandate 15-year fund lifespans; segregate capital by duration	Enterprise can invest for the long term
Extraction through leverage	Prohibit dividend recaps; tie carry to realized liquidity	Genuine value creation, not financial engineering
Pseudo-productivity	Optimize for leading indicators	Sustainable cash flows, not statistical illusions

Conclusion: Two Models, Two Futures

Private equity is not a monolith. It is a structure that can be deployed in two fundamentally different ways.

In the value extraction model, private equity initiates, controls, and extracts. The operator is subordinate to the financial engineer. Strategy shifts with each fund cycle. Debt burdens the enterprise. Financialization raises costs. Productivity gains are statistical illusions created by layoffs. Workers are treated as disposable costs. Communities are strip-mined. Innovation declines. Value is destroyed.

In the operator-led model, the operator initiates and runs the show. Private equity provides patient capital and governance oversight, nothing more. Strategy crystallizes around the operator's vision. Leverage is used conservatively. Financialization is minimized. Productivity gains come from genuine investment in people and processes. Workers are treated as assets. Communities are sustained. Innovation flourishes. Value is created.

Bottom Line

The evidence across manufacturing, technology, real estate, and utilities is consistent. When private equity stays in the background, it can be a constructive force. When it steps forward as the frontrunner, it becomes what critics have called a virus — extracting value, destroying enterprises, and leaving behind hollowed-out industries and devastated communities.

Recommendation

The Investment Committee should:

- Adopt these reforms as the baseline standard for all new private equity commitments.
- Require existing GP relationships to adopt these reforms as a condition of continued investment.

- Collaborate with other major LPs (CalPERS, Ontario Teachers', Norges Bank) to establish these reforms as industry standards.

We cannot change the past. But we can change the future of our capital — and the enterprises it is meant to build.

Appendix: Economic Definitions for Committee Reference

Principal-Agent Problem

A conflict of interest where an agent (GP) is motivated to act in their own best interests rather than those of the principal (LP). In private equity, this manifests when GPs prioritize fee generation and asset accumulation over risk-adjusted returns to LPs.

Rent-Seeking

The practice of obtaining economic gain through manipulation of the economic environment rather than through value creation. In private equity, rent-seeking includes extracting fees based on AUM rather than performance, and using dividend recapitalizations to extract cash before value is realized.

Moral Hazard

The tendency to take on excessive risk when the negative consequences of that risk are borne by another party. In private equity, GPs take on excessive leverage because the downside risk is borne by the portfolio company and its stakeholders, while the upside accrues to the GP through carried interest.

Duration Mismatch

The misalignment between the time horizon of capital and the time horizon of the investment strategy. LPs deploying long-duration capital (e.g., pension liabilities) into short-duration strategies (3-to-5-year flip models) create structural fragility for both the enterprise and the LP.

DPI (Distributed to Paid-In Capital)

A measure of realized returns, calculated as total distributions to LPs divided by total capital paid in. DPI is the only metric that reflects actual cash returned to LPs and cannot be manipulated through valuation assumptions.

IRR (Internal Rate of Return)

A measure of investment performance that can be manipulated through timing assumptions and valuations. Unrealized IRR is particularly susceptible to manipulation through additional leverage and optimistic valuation marks.

Leading vs. Lagging Indicators

Leading indicators predict future performance (e.g., employee retention, R&D investment, customer satisfaction). Lagging indicators report past performance (e.g., quarterly earnings, EBITDA). Optimizing for lagging indicators while destroying leading indicators produces ephemeral returns and long-term value destruction.

Carried Interest

The share of profits GPs receive as compensation, typically 20–25% of fund profits above a specified hurdle rate. In current practice, carried interest is often calculated on unrealized valuations, creating an incentive to inflate paper marks rather than build sustainable enterprises.

Dividend Recapitalization

A transaction in which a portfolio company takes on additional debt for the purpose of paying a dividend to its PE owner. This transfers wealth from the enterprise to the GP while increasing the enterprise's economic stressors, making it more vulnerable to economic downturns.

Sale-Leaseback

A transaction in which a portfolio company sells its owned real estate or equipment to a third party and then leases it back. This converts a fixed asset into a rental expense, increasing the cost of doing business while providing a one-time cash infusion to the PE owner.

References

This report synthesizes findings from academic literature on private equity ownership and reporting on individual transactions during 2023–2026. Key sources referenced in this analysis include:

- Academic literature on private equity incentive structures and shareholder value maximization channels, and on the magnification of regulatory distortions by high-powered incentives in regulated industries.
- Reporting on the Anchor Hocking / Pyrex plant closure in Charleroi, Pennsylvania, including federal court proceedings and statements from Senator Bob Casey regarding the acquisition's evasion of FTC merger review.
- Reporting on Thoma Bravo's 2021 acquisition of Medallia and its subsequent write-down and loan-to-own restructuring involving Blackstone, Apollo, and FS KKR Capital, including public statements by Orlando Bravo and industry commentary from Zycus.
- Reporting on private credit market stress, business development company valuations, and distressed software loan volumes as of February 2026.
- Reporting on Leslie's Poolmart's financial performance, capital structure, and share price history, and on S2 Capital's multifamily REIT performance and related feeder-fund disclosures.
- Reporting on the 2026 take-private of AES Corp., KKR's bid for UGI Corp., and Blackstone's stake in NiSource, in the context of AI-driven data-center power demand.
- Industry and regulatory commentary on private equity's role in healthcare, for-profit education, and insurance as comparative evidence for the utilities sector.

Full source citations, transaction documentation, and underlying data are available upon request from Genie Capital Ltd.

About Genie Capital Ltd

Genie Capital Ltd is an IP origination and stewardship company based in Buea, Cameroon. In addition to its core mission of IP origination and stewardship, we use our unique frameworks to diagnose structural fragilities, market trajectories, and related dynamics — and make them freely available on our website.

We are not an investment fund, advisory firm, or a lobbyist.

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