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The Impact of Leverage Buy-Out (LBO) Operations on Value Creation in Target Companies: An Empirical Study of the French Market

L'impact des opérations de Leverage Buy-Out (LBO) sur la création de valeur dans les entreprises cibles : une étude empirique du marché français

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Abstract

In an economic context shaped by the rapid evolution of financial markets, Leverage Buy-Out (LBO) transactions have become a key strategic tool for corporate restructuring and ownership transfer. This study aims to examine the impact of LBO operations on the performance and value creation of target companies. Using a sample of 183 French firms acquired through LBOs between 2013 and 2023.We adopted a longitudinal study design over a five-year horizon (two years before the LBO, the year of the transaction, and two years after). we compare their financial performance to that of similar non-LBO firms. The analysis is based on three indicators: ROA, ROE, and EVA. The results indicate that despite some performance decline post-LBO, the LBO-backed firms tend to outperform their peers, especially in the industrial sector.

Keywords : Private equity – Leveraged buyout – Debt-financed acquisitions – Leverage – Value creation – Performance

Résumé

Dans un contexte économique marqué par l'évolution rapide des marchés financiers, les opérations de Leverage Buy-Out (LBO) se sont imposées comme un instrument stratégique de restructuration et de transfert de propriété. Cette étude examine l'impact des LBO sur la performance et la création de valeur des entreprises cibles. À partir d'un échantillon de 183 entreprises françaises acquises via LBO entre 2013 et 2023, nous adoptons un design longitudinal sur cinq ans (deux années avant l'opération, l'année de la transaction et deux années après) et comparons leurs performances à celles d'entreprises similaires n'ayant pas fait l'objet d'un LBO. L'analyse mobilise trois indicateurs (ROA, ROE et EVA). Les résultats mettent en évidence une baisse de certains indicateurs après l'opération, tout en montrant que les entreprises soutenues par des LBO tendent à surperformer leurs homologues, notamment dans le secteur industriel.

Mots clés : Capital-investissement – Leverage buyout – Acquisition financée par la dette – Effet de levier – Création de valeur – Performance

Introduction

The globalization of the economy has led to significant changes in international financial activity, as well as the emergence of new technologies that have greatly increased the sophistication of various financial products. In response to this complex new economic and financial environment, companies are increasingly faced with difficult decision-making processes in their search for the most appropriate solutions.

Since its emergence, private equity (PE) has earned a reputation for delivering particularly attractive returns. Moreover, an increasing number of investors are choosing to allocate part of their capital to this asset class. It is also noteworthy that private equity activity and performance are becoming increasingly concentrated in late-stage investments involving major restructurings, such as Leveraged Buyouts (LBOs). According to the French Private Equity Association (AFIC): « A Leveraged Buyout can be defined as the acquisition of a company, partially financed through debt, within a specific legal structure optimized for tax purposes, where management teams are partnered with specialized professional investors.»

The basic principle behind LBO operations is the creation of a holding company (a company whose sole purpose is to hold financial assets), often referred to as the NewCo (New Company), which takes on debt to acquire a target company, also known as the OpCo. The holding company gains control of the target company while minimizing equity contributions. Its financial structure is typically characterized by high leverage and the use of sometimes highly complex financial instruments.

LBO operations allow their initiators (companies, financial institutions, executives, etc.) to gain control of a company while minimizing their equity contributions. They are intended to create a positive shift in the organizational structure and in the contractual relationships between managers and capital providers.

The objective of an investor when entering into an LBO structure is to achieve a high return within 3 to 5 years by selling their shares to another fund, through a secondary or tertiary LBO, or by taking the company public. Their role during the operation is therefore to help the company improve its performance (Kaplan and Stromberg, 2009).

This study enhances our understanding of the critical role played by LBOs in the performance and value creation of target companies. In the remainder of this article, we present the literature review and develop the research hypotheses (Section 2), followed by the research

methodology, including the results and their discussion (Section 3), and conclude the study (Section 4).

2- Literature Review and Hypothesis Development

Research on Leveraged Buyouts (LBOs) has evolved through three main generations, with increasing methodological rigor and geographic diversification.

The first generation of studies (1989–1995) laid the empirical foundation, primarily examining the effects of Management Buyouts (MBOs) on firm performance. Kaplan (1989), studying 48 large, listed U.S. firms undergoing MBOs between 1980 and 1986, found significant improvements in performance measured by EBITDA, investment levels, and net cash flows—up to +24% after three years. However, as in the works of Phan and Hill (1995) and Zahra (1995), these performance indicators were not benchmarked against industry peers. In contrast, Wright et al. (1996), focusing on the U.K., compared MBO and non-MBO firms over a five-year horizon and found that MBO firms outperformed their peers. Smith (1990) linked post-buyout earnings gains to asset divestitures, while Chanter (1990) emphasized the role of improved cash flow and governance. Jensen (1990) observed improved financial ratios in MBO firms relative to a control group. Opler (1992), in a sample of 44 MBOs, found higher operating profit-to-sales ratios and productivity per employee, with no significant impact on R&D. Phan and Hill (1995), based on 214 LBOs, argued that value creation stems more from increased managerial ownership than from financial leverage.

In France, Desbrières and Schatt (2002) studied 132 LBOs between 1989 and 1994 and observed a decline in financial performance post-buyout, both in absolute terms and relative to industry peers. Le Nadant (2000), analyzing French LBOs from 1992 to 1995, found that post-buyout cash flow performance was lower than both pre-buyout levels and those of comparable firms. Other operational indicators also failed to show any performance enhancement.

However, Le Nadant (1998) noted that former subsidiaries performed better than independent targets, particularly in terms of adjusted return on equity and employee productivity and compensation.

Lichtenberg and Siegel (1990), using U.S. industrial data from 1972–1988, found that LBO and MBO targets had 14% higher productivity growth over five years, largely due to more efficient resource use rather than reductions in R&D, labor, or investment. The most notable

change was a decline in non-productive staff, suggesting a shift toward performance-sensitive compensation for skilled labor.

The second generation (2007–2017) brought more diverse methodologies and nuanced findings. Mikael and Jonsson (2007), analyzing 69 LBOs from 1993–2006, found operational gains without job destruction or negative debt effects. They observed no significant differences between pre- and post-2000 LBO waves. Harford, Klasa, and Walcott (2009) showed that LBO targets are structured to reach optimal leverage levels. Achleitner, Braun, and Engel (2011), in a global study of 1,980 LBOs, identified entry/exit timing and EBITDA multiples as key drivers of IRR, with debt playing a central role. Robinson and Sensoy (2011) highlighted the correlation between public and private equity performance. In contrast, Cohn, Mills, and Towery (2013) reported only moderate performance gains and minimal leverage-driven value creation.

Ilg (2015) showed that returns diminish with longer holding periods, especially in carve-outs, and that large deals rely more on debt to address agency issues. Ayasha and Schütt (2016) pointed to accounting-driven performance inflation without substantive improvement. Hung and Tsai (2017) examined LBOs in emerging markets, revealing specific strategic behaviors and implications for institutional development.

Gaspar (2008), analyzing 158 French LBOs between 1995 and 2005, found marked improvements in economic performance compared to peer firms. Sales growth reached 13.91% in the first post-buyout year (vs. 6.04% for peers), and the gap widened to 9.5 percentage points by year two. Most striking was the EBITDA differential: a median gap of 22.3 points in year one and 25.66 in year two. Boucly et al. (2008), using a large sample of 400 French LBOs (1994–2004), confirmed significant gains in economic profitability and growth post-buyout.

The third generation (2019–2024) expanded the analytical focus to governance, investment horizons, institutional ownership, and geographic differences. Gao (2019), using a bilateral matching model, showed that value creation is more closely tied to investor involvement (7.8% of market cap) than to leverage. Mittoo and Suman (2020) reported significant financial improvements in Indian LBOs. Manigart (2020), through a meta-analysis, confirmed medium and long term performance gains but no employment effects. Ang and Xu (2021) linked LBOs to increased earnings management.

Chemmanur, He, and Hu (2022) found that longer investment horizons enhance sustainable performance. Berezinets et al. and Borell, Crespi, and Moreno (2022) emphasized the positive impact of private equity on growth and profitability. He and Lu (2023) underscored the importance of institutional ownership, while Gokkaya (2023) explored the effects of financial constraints and governance structures. De La Bruslerie and Crapsky (2023) discussed capital structure adjustments and the role of higher leverage. In China, Feng and Hu (2023) highlighted the positive effect of institutional ownership on investment efficiency.

Finally, in 2024, consulting firms Simon-Kucher and McKinsey reported a structural shift in the value creation mechanisms of LBOs. Their findings indicate that operational improvements particularly organic revenue growth and margin expansion have surpassed financial leverage as the primary driver of returns in modern buyout strategies. In light of the previous research, we propose the following hypotheses:

H1: In terms of evolution, the level of value creation of firms improves after a LBO operation.

H2: From a comparative perspective, firms involved in a LBO exhibit a significantly higher level of value creation than comparable firms.

3- Research Methodology

3-1- Selection of Companies

In this section, we examine the impact of LBO operations on the evolution of value creation among French target companies (H1) over a five-year horizon (two years before the LBO transaction, the year of the transaction, and two years after). We will also test the hypothesis that companies acquired through leveraged buyouts experience higher value creation compared to a control sample of companies from the same industry that did not undergo an LBO (H2).

We accessed the Thomson One Bankers database to identify companies that underwent LBO transactions in France between 2013 and 2023. To obtain the accounting data for our sample, we used the Diane database, which also enabled us to construct the control sample. Each LBO firm in our sample was matched with a non-listed company that did not undergo an LBO during the study period.

The matching was based on two criteria:

Industry criterion: To avoid potential sector-specific biases, each company in the control group operates in the same industry as its corresponding LBO company.

Size criterion: Based on the book value of assets before the transaction.

The selection of these two criteria is grounded in the assumption that operating performance varies according to industry and firm size. Fama and French (1995) demonstrated that smaller firms tend to have lower returns on equity (relative to book value) than larger firms. Similarly, Anglo-American studies on operating performance (Kaplan, 1989) have used size as a key criterion when constructing control samples.

The following table provides details on the types of activities of the companies in the sample. It can be observed that the majority of firms acquired through LBOs during the 20013–20023 period operate in the services and industrial sectors.

Table 1: Distribution of Sample Companies by Industry Sector

Sector	LBO
Industry	76
Real Estate, Leasing, and Business Services	46
Construction	15
Commerce	30
Transport and Communication	6
Others	10
Total	183

We opted for a longitudinal study over a 5-year horizon (two years before the LBO operation, the year of the operation, and two years after). We followed the methodology developed by Barber and Lyon (1996) in their study on detecting abnormal operating performance of firms involved in a specific event. The indicators in this study are calculated over a 5-year window, from (t–2) to (t+2), with t representing the calendar year of the LBO. We propose to carry out two sets of tests.

The first set aims to determine, over the four years surrounding the operation, to what extent firms involved in an LBO differ in characteristics from those in the same industry sector.

The second set focuses on the variations in the performance indicators in order to assess the evolution of the target firms' performance.

Firm performance will be measured using three indicators: Return on Assets (ROA), Return on Equity (ROE), and Economic Value Added (EVA).

3-2- Results and Discussion

Table 2: Panel A – Return on Assets (ROA)

	T-2	T-1	T+1	T+2	-2, +1	-2, +2	-1, +1	-1, +2
Average of the LBO sample	0.0830	0.0841	0.0776	0.0751				
Average of the control sample	0.0281	0.0394	0.0380	0.0346				
T/Z-test value	1.943*/ 2.039**	1.997**/ 2.309**	1.761*/ 1.782*	1.708*/ 2.166**				
Average change (Δ)					-0.0054	-0.0079	-0.0065	-0.009
T/Z-test value					-0.247/ -0.606	-0.057/ -0.075	-0.218/ -0.179	-0.583/ -1.504
Industry-adjusted average change					0.0540	0.0646	0.0214	0.0342
T/Z-test value					2.683***/ 2.265**	2.344**/ 2.327**	2.613**/ 2.653***	1.876*/ 1.547

****, **, and * indicate significance at the 1%, 5%, and 10% levels, respectively.*

Table 3: Panel B – Return on Equity(ROE)

	T-2	T-1	T+1	T+2	-2, +1	-2, +2	-1, +1	-1, +2
Average of the LBO sample	0.2350	0.2456	0.2343	0.2295				
Average of the control sample	0.1158	0.1698	0.1553	0.1600				
T/Z-test value	3.365***/ 2.964***	1.965*/ 2.327**	3.803***/ 3.517***	2.036**/ 2.798*				
Average change (Δ)					-0.0007	-0.0055	-0.0113	-0.0161
T/Z-test value					-2.109**/ -1.925*	-0.210/ -0.438	-1.884*/ -0.536	-0.433/ -0.229
Industry-adjusted average change					0.09188	0.0926	0.09868	0.10395
T/Z-test value					2.260**/ 1.916***	1.995**/ 2.118**	2.678***/ 2.223**	2.795***/ 2.737***

****, **, and * indicate significance at the 1%, 5%, and 10% levels, respectively.*

Table 4: Panel C – Economic Value Added (EVA)

	T-2	T-1	T+1	T+2	-2, +1	-2, +2	-1, +1	-1, +2
Average of the LBO sample	1814039	751540	140994	542845				
Average of the control sample	-2273188	-5340236	28279	251602				
T/Z-test value	1.838*/ 5.645***	1.092/ 6.588***	0.354/ 4.855***	0.165/ 3.699***				
Average change (Δ)					-1673045	-1271194	-610546	-208695
T/Z-test value					-0.2186/- 1.677*	-0.559/- 0.732	0.127/- 1.297*	-0.002/- 1.724*
Industry-adjusted average change					1615095	1954520	167208	2011473
T/Z-test value					1.797*/ 4.220***	1.336*/ 2.351**	1.519/ 2.050**	1.174*/ 0.797

****, **, and * indicate significance at the 1%, 5%, and 10% levels,respectively .*

Table 2 shows that the average value of economic profitability tends to decline in the years following the LBO operation (t-1, t+1) and (t-1, t+2). This value decreases from 0.0841 to 0.0776, then to 0.0775 in the second year after the operation. The change in the average economic performance measure is negative over the entire period (t-2, t+1) and (t-2, t+2), reinforcing the observation of a decline.

On the other hand, we note that LBO companies consistently maintain a significantly higher economic profitability compared to the control sample. We also observe that the difference in average economic profitability between the two samples remains significant at the 5% and 10% levels.

The calculation of the average variation in economic profitability adjusted for the industrial sector shows that the variation is always positive and significant at the 1%, 5%, and 10% levels, indicating a sector effect. This explains the dominance of the industrial sector in investors' choices.

Table 3 shows that the average financial profitability decreases after the buyout operation. This value moves from 0.235 (t-2) and 0.2456 (t-1) to 0.2343 (t+1) and 0.2295 (t+2), confirming the decline in firm performance following an LBO.

We also observe that companies under LBO maintain a financial profitability significantly higher than that of comparable companies. The difference in average financial profitability between the two samples is significant at the 1%, 5%, and 10% levels.

By calculating the average variation of ROE adjusted for the industrial sector, we found that the variation is always positive and significant at the 1%, 5%, and 10% levels, indicating the presence of a sector effect.

Table 4 shows that the average EVA tends to decline over the period (t-2, t+2). This value decreases from 1,814,039 to 542,845. However, the average EVA of comparable companies increases during the same period, rising from -2,273,188 (t-2) to 251,602 (t+2).

During the study period, companies acquired through LBO have a significantly higher economic value added than comparable companies. This difference is significant at the 1% and 20% levels.

By calculating the average variation of EVA adjusted for the industrial sector, we found that the variation is always positive and significant at the 1%, 5%, and 10% levels, indicating the presence of a sector effect.

Using EVA as a measure of value creation, we can observe that the decline in the performance of target companies is more pronounced. This can be explained by the fact that EVA allows for the identification of a more concrete annual value created compared to economic and financial profitability rates. Over the past few years, EVA has established itself

as the most analytically rich and representative method of measuring value. EVA is thus defined as a generalized economic profit, different from accounting net income. More precisely, it corresponds to the surplus generated after compensating the providers of capital, represented by shareholders and debt-financing creditors.

Whatever the measure of value creation chosen (ROA, ROE, EVA), we can conclude that companies under LBO outperform comparable firms and that there is a positive sectoral effect of the industrial sector on the value creation process within target companies. This explains the dominance of the industrial sector in investors' choices (76 companies in the sample belong to the industrial sector). The results found are consistent with many previous studies such as those by Nadant (1998), Desbrières and Schatt (2002), and Jonathan B. Cohn, Lillian F. Mills, and Erin M. Towery (2014).

Desbrières and Schatt (2002) explain the decline in the performance of target companies by two characteristics specific to the French market. First, the financial leverage levels used in LBO operations in France tend to be lower than those employed in the United Kingdom and the United States, which negatively impacts the incentive effect associated with the disciplinary nature of debt.

Second, in France, a significant percentage of LBOs are conducted on family-owned businesses. As the authors suggest, performance gains following a leveraged buyout are likely to be greater in companies previously controlled by groups than in family businesses. In non-family companies, the manager is more likely to increase entrepreneurial orientation and equity participation, which can reduce conflicts of interest with shareholders. On the other hand, LBO operations carried out on family businesses often coincide with succession events, which can pose risks related to limited access to key information and the execution challenges faced by a new manager.

Conclusion

LBO refers to a specific form of private equity that helps solve the problem of transferring a company when the founding manager cannot find a buyer. The equity investor must primarily act, in close cooperation with the management of the acquired company, on the main value creation levers. This approach enables the investor to achieve the goal of generating a capital gain on the funds invested in the transaction.

Two series of tests were conducted on three measures of value creation (ROA, ROE, and EVA). The first compares the level of value creation of companies acquired through LBOs with that of comparable companies. The second series analyzes changes in value creation over a period surrounding the transaction, assessing the evolution of these indicators two years before and two years after the LBO.

The results are consistent with the findings of Le Nadant (1998), Desbrières and Schatt (2002), and Lillian F. Mills and Erin M. Towery (2014). We demonstrated that the level of value creation in French companies declines following the LBO operation but remains significantly higher than that of companies in the same industry sector. For a sample adjusted to the industrial sector, we observed an increase in the performance of companies in our sample in the years following the LBO.

Leveraged buyout transactions implement a combination of value creation levers. The mechanisms underlying each of these levers are relatively simple. However, the complexity of this type of operation arises from the multiplicity of possible combinations at various levels. The main value creation levers within companies under LBO are: the financial lever, the legal lever, the tax lever, and the managerial lever.

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