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Skill and luck in private equity performance[☆]

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A B S T R A C T

Private equity (PE) performance is persistent, with PE firms consistently producing high (or low) net-of-fees returns. We use a new variance decomposition model to isolate three components of persistence. We find high long-term persistence: the spread in expected net-of-fee future returns between top and bottom quartile PE firms is 7 to 8 percentage points annually. This spread is estimated controlling for spurious persistence, which arises mechanically from the overlap of contemporaneous funds. Performance is noisy, however, making it difficult for investors to identify the PE funds with top quartile expected future performance and leaving little investable persistence.

JEL classification: C11 D83 G11 G14 G23 G24

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