Hedge and private equity funds

WHAT ARE HEDGE AND PRIVATE EQUITY FUNDS?

Hedge and private equity funds are privately-owned investment funds that offer high returns – and high risks. A large proportion of their money comes from pension funds.

WHAT IS THE PROBLEM?

There are three big problems with hedge and private equity funds:

- They are a menace to healthy companies and to workers rights. These funds are often involved in 'leveraged buy-outs': a company is bought with borrowed money, the company is then saddled with the debt and interest payments, and workers are laid off and assets sold off in a hunt for fatter profits. The once profitable and healthy company is milked for short-term profit, and working conditions suffer.

- They are a threat to financial stability because they rely on huge accumulated debts and a lack of transparency - a potentially fatal combination. The funds are not subject to the same rules of disclosure as public companies (because they are privately-owned). This means it is very hard to find out where they are investing, what they own and who is responsible for what debt. This is alarming because our pension funds invest heavily in these funds.

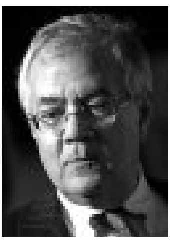
- They pay very little tax. This mattered less years ago when these funds were much smaller and mainly invested in innovative and start-up companies. Now they are very big players but contribute much less revenue to our societies than other companies. One fund manager admitted he paid less tax than his cleaning lady!

"There cannot be a serious argument for hedge and private equity funds to be exempt from the disclosure, transparency and taxation rules that apply to everyone else in the financial market"

Poul Nyrup Rasmussen,
President of the
Party of European Socialists

"It gets close to outright foolishness, if every little penny bank is under daily supervision of the authorities, whereas private financial institutions, which are a hundred times more powerful, can act without the least restraint"

Helmut Schmidt,
Former Chancellor of Germany



"When a small number of individuals benefit from a particular deal in the tens and sometimes hundreds of millions of dollars, and concurrently workers are laid off, we have a situation which it seems to me (is) wrong"`

Barney Frank,
Chairman of the US Congress Financial Services Committee

"Some financial investors don't waste a single thought on the people, whose jobs they destroy - they stay anonymous, they don't have a face, they invade companies like swarms of locusts, devour everything and then move on. It is this form of capitalism that we are fighting against"

Franz Müntefering,
Former Vice Chancellor of Germany

"The real winners are the private equity and hedge fund managers – while investors and workers employed by companies targeted for leveraged buy-outs, have no such guarantees. The retirement incomes of millions of workers are at stake"

Guy Ryder,
General Secretary of the International Trade Union Confederation

FUND FACTS

The biggest five private equity deals involved more money than the annual budgets of Russia and India.

Two thirds of all new debt is generated by hedge and private equity funds. The American sub-prime mortgage crisis was triggered by bad debts, but hedge and private equity funds are responsible for a huge increase in debt.

The British 'Automobile Association' was bought by private equity in 2004. It was making £75 million profit and providing an expanding service with 10,000 staff. Since been taken over, profits have gone up to £190 million, while some 6,000 workers were laid off, and both prices and waiting times for customers have increased.

"The union's experience with private equity firms in the past hasn't been positive as they tend to borrow money, invest, take over an existing company, cut and slash and then sell the operation for a quick profit"

President of the Canadian Auto Workers

In 2001 a private equity firm bought Cognis, a German chemical company. Cognis made a pre-tax profit of €109 million the previous year. Following the takeover it was so burdened with interest payments that despite rising sales it registered a loss of €136 million in 2006. The private equity firm and bank that lent the takeover money have taken €850 million out of the company!

Danish telecommunications company TDC was taken over by a group of private equity firms in 2005. 80% of the purchase was financed by borrowing. The result was that the company's ratio of asset to debt leaped from 18% to over 90%. To pay off the debt the company's reserves for long-term development were used.

Satellite operator PamAmSat was bought by private equity firms for $4.1 billion. The firms put in $550 million and borrowed the rest. PamAmSat were saddled with debt while the private equity firms paid themselves a $250 million dividend.

"Hedge funds need added transparency"

Investment News

THE CHALLENGE

Financial markets have a vital role to play. For long-term investment we need stable and effective financial markets. Transparency and accountability is an absolute necessity. The rules of the game must apply to all players. "*The European Union should decide on all appropriate measures to establish full transparency, disclosure and accountability – particularly in relation to hedge and private equity funds – in the financial markets*".
Party of European Socialists, adopted at PES Leaders Conference 21 June 2007

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