CMBOR
EQUISTONE

CENTRE FOR MANAGEMENT BUY-OUT RESEARCH
NEWSLETTER // WINTER 2019

Continental buy-outs stay strong

Europe is not without challenges but buy-out investors continue to find it an attractive destination.

European buy-out investors have capital to deploy and, in the three and a half years since the June 2016 'Brexit' vote, have become increasingly confident as to how this change to the Euro landscape might impact their investment risk. Life was breathed back into the buy-out market in 2015 as quantitative easing programmes fuelled money supply, boosted capital markets' liquidity and ultimately enabled firms to source attractively priced debt for transactions. This in turn was followed by a huge jump in buy-out fundraisings, which left firms with greater capital to deploy. Consequently, aside from a drop to €65.1bn in 2016 (from €95.4bn in 2015), largely attributed to the uncertainty surrounding Brexit, buy-out investment has continued its upward trajectory.

CORE TRENDS

Germany and France have both remained consistent performers in terms of the value of their buy-out markets during the past decade. The UK market wobbled in 2016; thanks to the Brexit vote its buy-out market was worth just €14.9bn that year. That put the UK almost level with France, which saw €13.8bn invested in buy-outs in 2016. Overall, in the past decade the combined value of French and German buy-outs is roughly on a par with UK buy-outs over the period.

This is not the case for the Netherlands, however, which emerged as an ever-stronger market as the decade progressed. In total, Dutch buy-outs in the period 2010-2019 were valued at €66.5bn, putting the country fourth place in Europe. Admittedly, this figure includes the €10.1bn buy-out of Akzo Nobel Speciality Chemicals in October 2018 and the €6.8bn buy-out of Unilever's spreads division in July 2018.

2019 continued this trend and was also a strong buy-out year for The Netherlands, with €12.4bn invested. This was boosted by: the €2.6bn sale of United Group by KKR to BC Partners; the €2.2bn sale of IFCO Systems to Triton and ADIA (Abu Dhabi Investment Authority); the €1.7bn buy-out of CRH European Distribution by Blackstone; and the €1.5bn buy-out of Exact Software by KKR from Apax Partners.

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However, this still leaves €4.4bn of value coming from mid-market buy-outs. This demonstrates the growing interest and activity in the Dutch buy-out market. In 2018, by comparison, only €2.4bn of the €23.7bn buy-out activity fell into the mid-market with €21.3bn being generated by buy-outs worth €1bn-plus.

MEGA DEALS

In 2019 there were 23 European buy-outs with a combined value of €56.6bn. To put it another way, 50.5% of European buy-outs total value (€106.3bn) came from mega deals. Of the 22, nine resulted from trade sales, the largest of these being the €9.4bn spin off of Nestlé's Skin Health business acquired by EQT Partners and ADIA in October. After trade sales, which were worth a combined €25.4bn, five public-to-private buy-outs accounted for the next biggest segment at €17.1bn. Four were of UK-headquartered companies (Merlin Entertainments, Travelport Worldwide, Inmarsat and BCA Marketplace) and the fifth (Ahlsell) was Swedish. A further six deals were secondary buy-outs; the largest of these being the transfer of Eastern European cable and pay-TV operator United Group from KKR to BC Partners for €2.6bn.

SECTOR PREFERENCES

European financial services deals fell back both in numbers (to 29 from 39 in 2018) to €2.8bn in 2019 (down from €12.6bn in 2018.) Manufacturing buy-outs also tailed off in 2019 (as they did in 2016); with 194 buy-outs worth €17.6bn. This compares to 240 buy-outs worth €17.6bn in 2018. Both manufacturing and financial services sectors across Europe are expected to face difficulties as the UK withdraws from the EU. This could explain why both sectors also saw a drop off in investment activity in 2016, when the UK first voted to leave the EU, and in 2019 when concerns about a hard Brexit were at their height.

In contrast, the healthcare, leisure and TMT sectors had bumper years in 2019. Healthcare saw 67 buy-outs (up from 48 in 2018) worth €16.9bn in 2019 (up from €14bn in 2018). Although deal numbers were up, value in 2019 was driven by the spin out of Nestlé's Skin Health business for €9.4bn in October.

The leisure sector was boosted by the €5.6bn take-private of Merlin Entertainment in November. Overall 32 leisure buy-outs accounted for €13.5bn of investment in 2019. TMT buy-outs had their best year in a decade with 137 transactions worth a combined €21.8bn. Mega deals had a part to play here too and TMT buy-outs were spread across Europe. In March German open-source enterprise software business SUSE was bought in a trade sale by EQT Partners for €2.2bn. Also in March, Dutch cable and pay-TV operator United Group was the subject of a secondary buy-out worth €2.6bn.

In May, UK-headquartered travel technology company, Travelport Worldwide, was taken private in a €3.9bn transaction led by Siris Capital & Evergreen Coast Capital Corp. In July, Norwegian robotics company AutoStore was the subject of a €1.6bn secondary buy-out when EQT Partners sold out to Thomas H Lee Partners. In November, BCA Marketplace, which trades as 'webuyanycar.com', was taken private in a €2.2bn buy-out led by TDR Capital.

CENTRAL AND EASTERN EUROPE

Lithuania's Luminor Bank was sold by Nordea Bank and DNB Bank to Blackstone for €1bn in September 2019. This was the sixth largest buy-out exceeding €1bn in the Central & Eastern Europe (CEE) region in the past five years. And it is one of only 11 to exceed €1bn in the past decade. The Luminor buy-out placed Lithuania at the top of CEE buy-outs by value in 2019. Lithuania was followed by the Czech Republic, which had five buy-outs worth €276m, and Poland with seven buy-outs worth €234m. The CEE region is still in relative infancy; of the €29.1bn invested across 2010-2019, mega €1bn+ buy-outs account for €14.4bn. This leaves €14.7bn mid-sized buy-outs over the period, with the Czech Republic, Poland, Romania and Turkey being the most active markets.

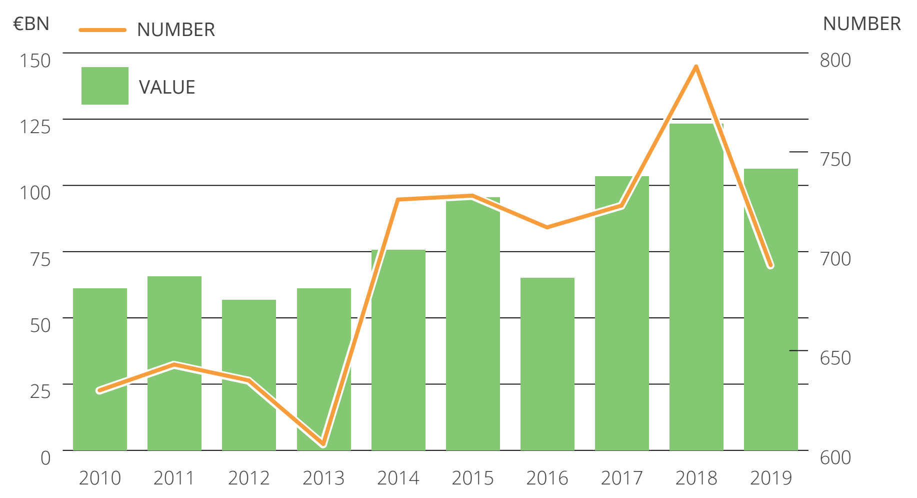
UK EFFECT

Despite the talk of the effect Brexit will have, or is having, on the UK deal market, it is not easy to discern a pattern from the overall figures. In 2019, UK buy-outs at €30.8bn accounted for 29% by value of all European buy-out activity (€106.3bn).

UK buy-out numbers and combined value were down in 2019, compared to 2018. However, the UK's share of the European buy-out market was actually lower at 20.9% in 2018. In 2018 UK buy-outs were worth €25.7bn whereas the total European market was worth €123.2bn that year.

Mega buyouts have an important part to play. In 2019 there were 23 mega buy-outs with combined value of €56.6bn and in 2018 there were 29 such buy-outs with a combined value of €62bn. However, seven of the mega buy-outs in 2019 were from the UK and had a combined value of €20.4bn; equivalent to 36% of the €56.6bn invested in 23 buy-outs. Given that the UK's share of 2018's mega buy-outs accounted for just €7.5bn (across its five mega buy-outs), equivalent to 12% of the €62bn raised, it is clear why the UK share of the European buy-out market was just 20.9% in 2018.

2010 – 2019 // EUROPEAN BUY-OUTS



SOURCE: CMBOR / EQUISTONE PARTNERS EUROPE / INVESTEC SPECIALIST BANK

Exit slowdown

Exits from European buy-outs fell to their lowest level in seven years; recording a combined value of €70.1bn as the decade drew to a close. The UK achieved just €8.3bn through exits in 2019. Had it achieved closer to an average of its previous five years (€42bn p.a.), exits of European buy-outs would have again exceeded €100bn.

IPO markets were receptive to buy-out exits in Europe in 2019, suggesting the ongoing uncertainty over Brexit could be a cause of falling exits. Exits from UK buy-outs suffered in 2016 (when the Referendum on UK membership of the EU took place) dropping to €28.9bn down from €66.1bn in 2015 before recovering in 2017 when it became apparent that any exit from the EU was not imminent. However, political inertia around the withdrawal agreement, and the UK parliamentary stalemate throughout 2018 and into late 2019, saw some investors adopt a wait-and-see approach.

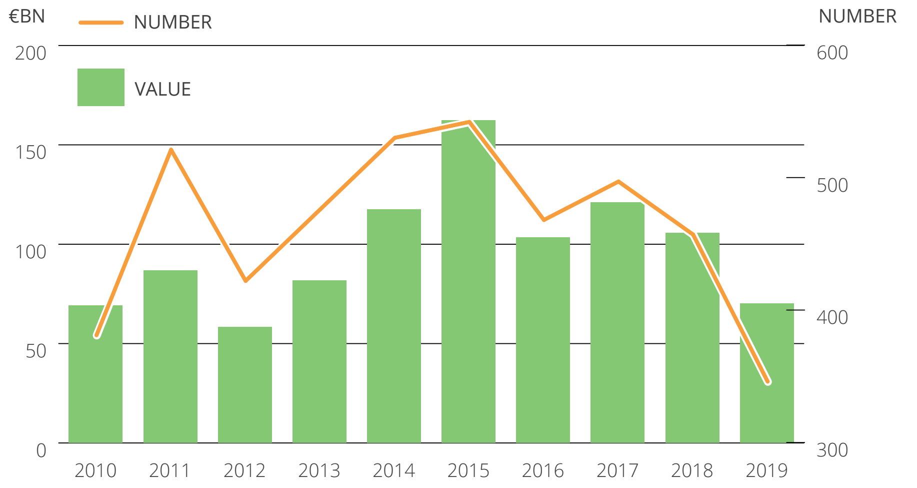
Where the UK failed to deliver, France and Germany continued apace. By the end of the decade the combined French and German exit markets equalled that of the UK for the full decade; both achieving €298bn.

There were eight IPOs in 2019 worth a combined €16.5bn. They include the two largest buy-out exits of 2019: TeamViewer, the remote connectivity specialist, listed on the Frankfurt Stock Exchange by Permira in September for €5.25bn; and Nexi Group, the electronic payments for credit card operator CartaSi, listed on the Milan Stock Exchange by Bain Capital in April for €4.7bn.

Verallia, the French glass bottle maker, was listed on Euronext by Apollo Management in October. Verallia was valued at €3.2bn. Austrian bank Addiko Bank was listed on the Vienna stock exchange in July by Advent International at a valuation of €312m. The remaining three IPOs were London Stock Exchange listings of UK companies: Watches of Switzerland raised £738m in May, Loungers raised £215m in April and The Pebble Group raised £206m in December.

IPOs made a significant contribution to European exits values in 2019; reaching almost a quarter of the overall value. IPOs accounted for 8.5% in 2018; 13.8% in 2017; and 18.5% in 2016.

2010 – 2019 // EUROPEAN BUY-OUT EXITS



SOURCE: CMBOR / EQUISTONE PARTNERS EUROPE / INVESTEC SPECIALIST BANK

Funding structures

Buy-out funding structures have been relatively stable across all buy-out sizes in the past five years. Debt across all buy-outs has moved between 44.1% and 50.6% for structures over €100m. This reflects a largely stable macroeconomic outlook over the period and a readily available debt supply thanks to the European Central Banks' quantitative easing programme, which began in March 2015.

The picture five years earlier, at the start of the past decade, was quite different. Global markets were still recalibrating in the aftermath of the 2007/08 financial crisis. In 2010 the equity component of all buy-out funding structures stood at 69.3% with debt making up 27.3%. In funding structures over €100m the situation was only slightly different with equity accounting for 59.3% and debt 37.5%. Buy-out investors struggled to secure competitively priced debt from the 2007/08 crash through to the end of 2012.

Looking ahead, liquidity remains good. However, US presidential elections in November 2020, the potential for the US-China trade war to reignite and the Brexit transition period (December 2020) could all pose challenges with the potential to upset debt market liquidity.

2015 – 2019 // FINANCING STRUCTURES ON EURO BUY-OUTS (%)

	2015		2016		2017		2018		2019	
	All	>€100m	All	>€100m	All	>€100m	All	>€100m	All	>€100m
Equity	49.9	43.4	54.2	46.7	48.3	44.9	50.5	45.8	47.9	42.8
Mezzanine	1.1	1	0.2	0.2	0.9	1.2	0.6	0.5	1.1	–
Debt	47.5	55.4	44.1	52.3	49.7	53.9	47.6	53.4	50.6	57.2
Loan note	0.4	0.2	1.2	0.8	0.8	–	0.9	0.3	–	–
Other finance	1.1	–	0.2	–	0.3	–	0.4	–	0.3	–
Total financing (€m)	**60,482**	**58,641**	**38,370**	**35,987**	**59,272**	**56,602**	**83,182**	**81,106**	**39,892**	**39,075**
Vendor contribution	0.1	–	0.8	–	1.1	–	1.3	0.9	0.1	0.1
Management contribution	0.3	0.4	0.3	–	0.1	–	1.3	0.9	0.1	0.1
Management share of equity	28.2	19.4	28.1	19.9	26.5	22.5	27.7	21.3	27.4	21.7

SOURCE: CMBOR / EQUISTONE PARTNERS EUROPE / INVESTEC SPECIALIST BANK

Note: Sample buy-out structures.

IN MEMORIAM:

Mike Wright

In November 2019 Professor Mike Wright, the founder of CMBOR, died after a short period of illness. Mike was born in Stockport in 1952 and grew up in Derbyshire and loved to walk in its Peak District throughout his life. He is survived by his wife, son and daughter and a young grandson.

Mike spent much of his career working out of the University of Nottingham's Business School, which became CMBOR's home in 1986, before transferring to Imperial College in 2011. His decision, as a young academic, to study management buy-outs was driven by a belief that these were an important development with the potential to contribute to economic renewal. He has said of his decision to establish CMBOR: "My soon-to-be head of department didn't exactly agree, telling me, as a very junior academic at the time, that I was wasting my academic career on such a peripheral and esoteric topic that would disappear as soon as the recession was over."

To the good fortune of the private equity industry, Mike ignored this attempt to pour cold water on his entrepreneurial venture. He secured sponsorship from Barclays Private Equity and Deloitte, which allowed him to hire administrative and research staff and CMBOR came into being. (Barclays Private Equity undertook its own management buy-out in 2011, becoming Equistone, and remains a sponsor of CMBOR to this day.)

Over time, those 'peripheral and esoteric' management buy-outs were now a mainstream feature of the corporate landscape. This year alone, European management buy-outs will exceed a dizzying €100bn.

Evidently, Mike has long been vindicated in following his entrepreneurial hunch. But Mike did so much more for the private equity market than collect buy-outs data. He articulated the market, he explained what a management buy-out actually was, defined its economic importance, and in so doing, he demystified them and dispelled unhelpful myths as a growing buy-out industry navigated tax and regulatory landscapes. Mike gave management buy-outs fair representation.

It was again to the good fortune of the private equity industry that it was an academic of Mike's personal standing conveying this information: he was ranked first globally for publications in the field of academic entrepreneurship and, among many other business and academic pursuits, he sat on the advisory board of the British Venture Capital Association.

Mike and his wife had begun to live part-time in her native rural France. Mike was well known for his love of all things French, Manchester United and a life-long passion for Bob Dylan's music. He was a keen cyclist and did a 600km cycle from central France to the Pyrenees to mark his 60th birthday celebration.

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