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unquote ”

Leading the way

LDC's Darryl Eales talks to unquote's Emanuel Eftimiu about the challenges of investing in a disrupted market

The UK private equity industry has had to adjust to a new market reality over the past 18 months. In a market characterised by limited availability of debt and falling multiples, it is not surprising that investment activity has plummeted. Industry players have reacted differently to the challenging environment, adapting to the new reality at different rates, and for some the market disruption is representing an opportunity. "Of course we're dealing with a more complex market, but our regional stance, which provides excellent local visibility, and our focus on backing outstanding management teams hasn't changed," states LDC CEO Darryl Eales. "For us it's business as usual and we're set to keep investing through the cycle."

In fact, a look at the statistics shows LDC to be by far today's most active player, with seven investments in the first half of 2009. Such activity may make some "wait-and-see" players shudder, though others long for capital to deploy in what many deem the best vintage year for some time. "There is a general lack of confidence to invest in the current climate with many firms preferring to wait until recovery signs are more evident before committing sizeable sums of money. That said there are definitely opportunities in the mid market at the current time and money available to support the right proposition. Selection and assessment remain key," Eales explains.

What is more, the drive to make the most of the current market is not restricted to primary investments. "We are encouraging portfolio companies to make strategic investments as this is the time for transformational acquisitions," insists Eales. Indeed, though overall deal activity has been subdued, add-on acquisitions have seen an uptick as portfolio management has moved to the top of the agenda for most

private equity houses and financing has become more readily available.

Additionally, the challenging macro-economic environment has generated increased opportunities for bolt-ons as ailing corporates rely on non-core disposals to raise cash and even private equity firms look to offload troubled assets. Consequently, the much cited gap in price expectations between vendors and buyers has started to narrow, with Eales expecting it to effectively close soon, leading to increasing activity at the end of 2009. Of course there is still the issue of funding constraints, as financial institutions look to bolster their balance sheets before committing to new lending, but vendor financing has already proved to be a good way to bridge the difference in price expectation and unlock the stalemate.

The impact of the liquidity crunch has obviously been felt across all UK regions with all sectors experiencing difficulties to a lesser or greater extent depending upon their reliance upon not only consumer markets but also business supply chains. "Analysing the dire situation is not enough," notes Eales, "one also has to come up with a plan going forward." In his view, private equity has a major part to play in revitalising, supporting and growing UK businesses. Judging by the first six months of this year, LDC is leading the way.



regional mid-market barometer

Methodology



- All data published in the *unquote*™ regional barometer is extracted from Private Equity Insight, the proprietary data system of Europe's leading private equity information specialist. Although every effort is made to ensure that the statistics contained within are as comprehensive as possible, the figures published in this edition are effectively a snapshot of the data held as at 31 July 2009. For this reason the statistics are likely to change over time as information on further deals comes to light.
- All details have been confirmed, where possible, with the private equity investors involved in the transactions. In some cases deal values have either been provided confidentially or have been estimated and these will not be shown in the text.
- Four regional groupings are analysed as part of this barometer. Each of these is made up of more than one of the discrete regions as defined by the BVCA. The groupings are as follows:
 - North:** North-West & Merseyside, Northern Ireland, Scotland, North-East and Yorkshire & The Humber;
 - London:** London and Eastern;
 - Midlands:** West Midlands and East Midlands;
 - South:** South-East, South-West and Wales.
- For more information on the regional barometer, please contact: Emanuel Eftimiu, European research manager. Tel: +44 (0)20 7004 7464.
- For more information on Private Equity Insight, please contact: Nicola Tillin, commercial director. Tel: +44 (0)20 7484 9884

League tables

UNITED KINGDOM	
Name	Volume
LDC (Lloyds TSB Development Capital)	7
Accel Partners	3
Foresight Group (Foresight Venture Partners)	3
Index Ventures	3
3i	2
Advent Venture Partners	2
Barclays Private Equity	2
Scottish Enterprise	2
Sovereign Capital	2
Aberdeen Asset Managers Private Equity	1

LONDON	
Name	Volume
Accel Partners	3
Barclays Private Equity	2
Index Ventures	2
3i	2
Sovereign Capital	2

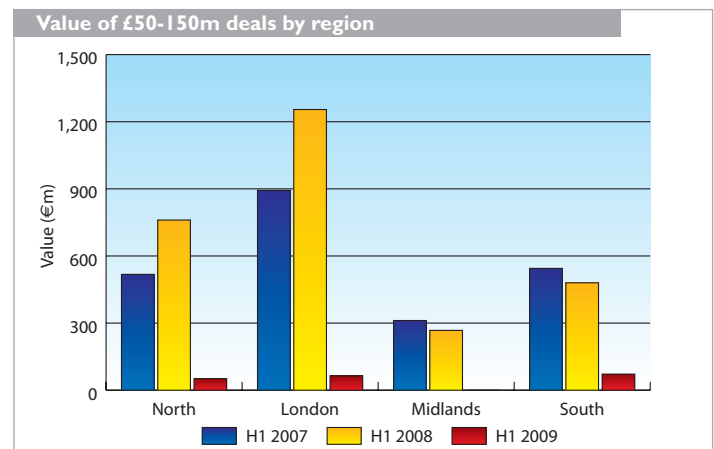
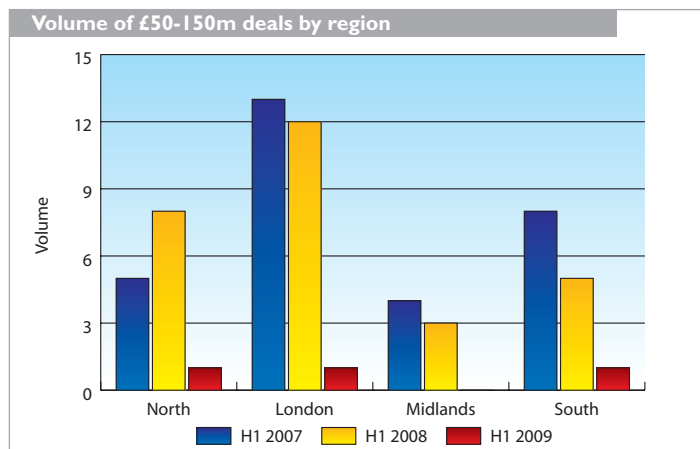
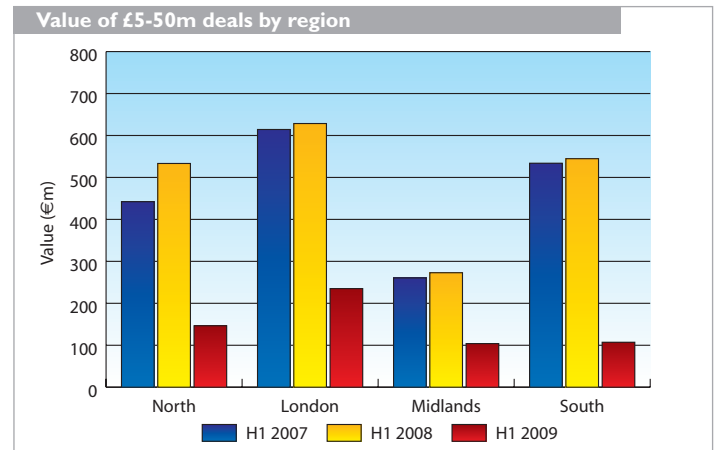
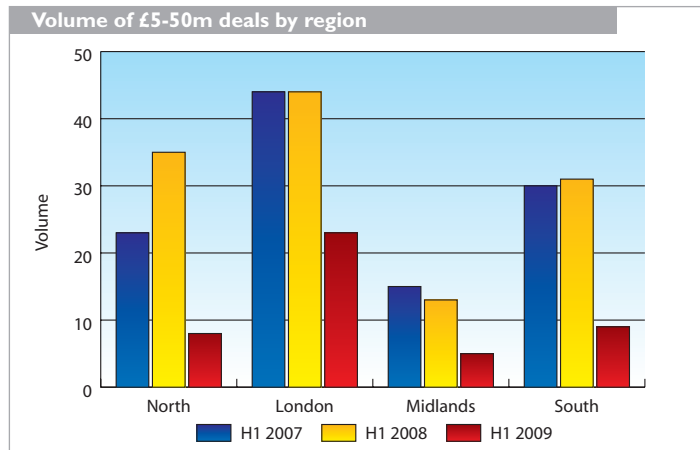
NORTH	
Name	Volume
LDC (Lloyds TSB Development Capital)	3
Scottish Enterprise	2
Capzantine	1
MBO Partenaires	1
Close Growth Capital	1

MIDLANDS	
Name	Volume
LDC (Lloyds TSB Development Capital)	3
Valco Capital Partners	1
Rcapital	1

SOUTH	
Name	Volume
Foresight Group (Foresight Venture Partners)	2
Advent Venture Partners	1
LDC (Lloyds TSB Development Capital)	1
MML Capital Partners	1
Abingworth Management	1

National overview

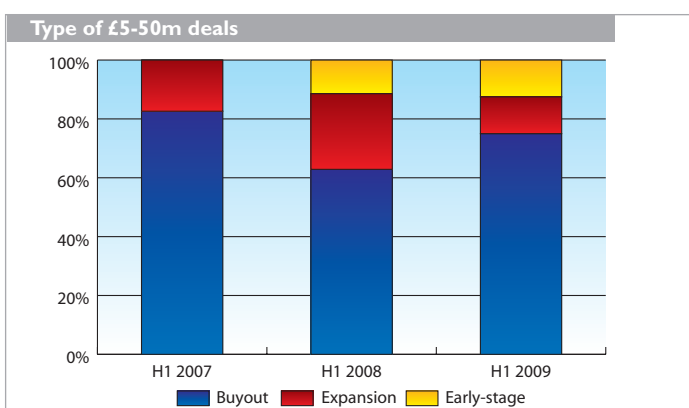
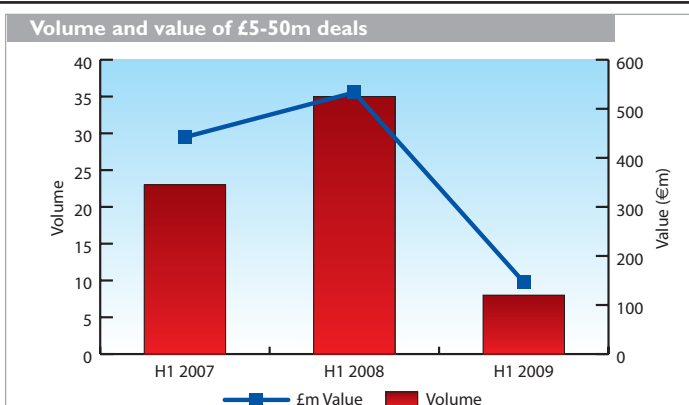
- On the back of already subdued deal activity at the end of 2008, the first half of 2009 saw a further slowdown in the UK private equity market in terms of both volume and value. Indeed, while H1 2008 figures compared well against the same period in 2007, not least due to a rush to complete deals before changes to the capital gains tax came into effect in April 2008, statistics for the first six months of 2009 paint a rather bleak picture.
- The prevailing fragile market sentiment, as well as vendor price expectations that are in general still perceived to be too high, has resulted in a drastic fall in deal activity in the £5-50m range. In the first six months only 45 deals were registered in this lower bracket, a drop of 63% from the 123 transactions completed during the same time last year. This decline was reflected across all of the UK regions, with the Midlands seeing deal completions shrink to five while London remained by far the most active area with 23 deals. Additionally, after years of steady increases activity in the North dropped in the first six months to eight transactions, a 77% decline from the 35 deals completed in the first six months of 2008.
- Perhaps unsurprisingly, the value of £5-50m deals in the UK fell by a slightly higher margin than deal volumes, with H1 2009 transactions amounting to only £593m – a 70% drop from the £2bn total recorded the previous year. In line with activity levels, the Midlands represented the lowest value with a total of just above £100m, while London dropped from £629m in 2008 to £235m for the first half of 2009.
- Given the continuing lack of financing available to support more sizeable transactions, activity in the £50-150m bracket collapsed by 89% from 28 in the first half of 2008 to a mere three deals this year. Among the UK regions, the Midlands did not record a single transaction in this size bracket, while deal activity in London, historically the busiest region, also came to a standstill.
- In line with the drop in volume, value totals for the £50-150m range in the first half of 2008 also plummeted from £2.7bn to £188m – a staggering 93% drop. Again, London saw the biggest fall in total value from £1.25bn registered over the same period in 2008. No deal in this bracket breached the £100m level.



North

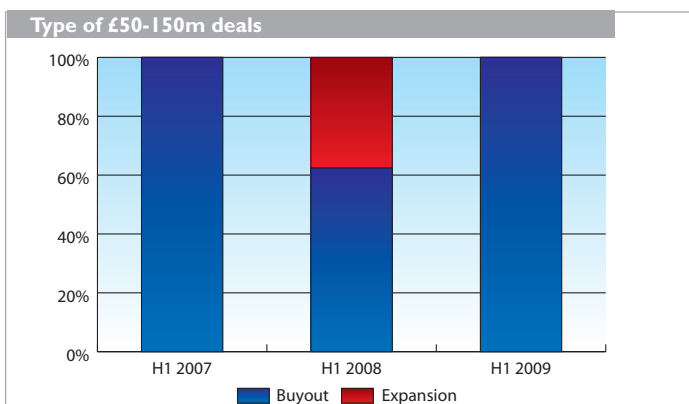
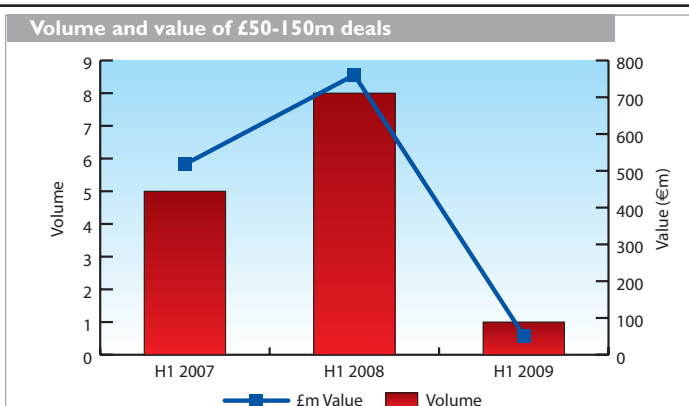
Deal activity in the £5-50m size range

- Following steady growth in dealflow in the first half of 2007 and 2008, activity levels for £5-50m transactions in the North have plummeted in the first six months of 2009. A total of eight deals were completed in this range, a drop of 77% from 35 transactions recorded over the same period in 2008 and the lowest half-year total on record.
- Not surprisingly, overall value of £5-50m deals in the North fell in line with the drop in volume. The eight deals completed were worth £147m, down 72% from £533m the previous year. That said the average value of deals in the size range was up by 20% compared to 2008, rising from around £15m to more than £18m, though this remains lower than the figure of £19m recorded in 2007.
- The increase in average deal size is mainly due to a proportional increase in the number of buyout transactions, which accounted for six deals in the region, while early-stage and expansion deals represented just one transaction each. What is more, in contrast to developments in the other regions, in the North it is in particular the expansion segment that has seen the largest drop in activity, having fallen from nine transactions completed in the first six months of 2008.



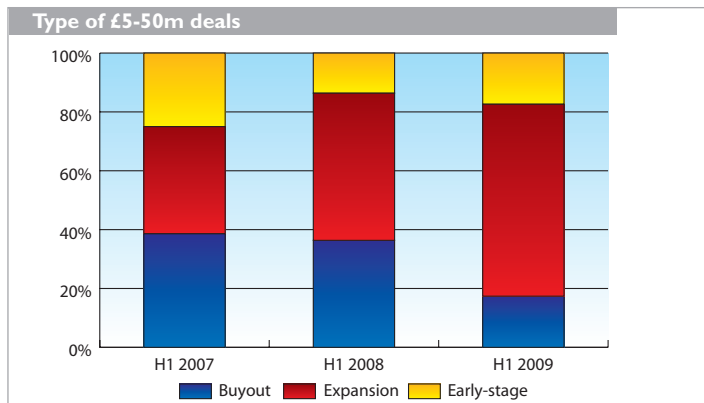
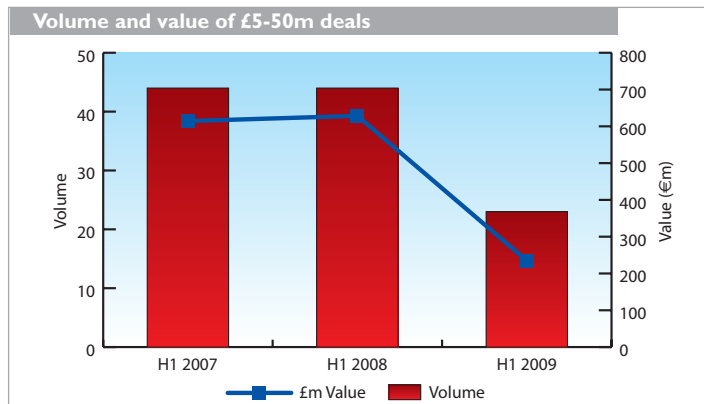
Deal activity in the £50-150m size range

- There was only one recorded transaction in the larger size bracket in the first six months of 2009, as debt financing for larger deals remained hard to come by. Interestingly this represents a significant drop from the eight deals completed over the same period in 2008, and further highlights the frail macro economic environment and state of the debt markets. It remains to be seen whether market sentiment can improve sufficiently in the second half of the year to kick-start activity in this size range once again.
- Unsurprisingly, the value of £50-150m transactions in the North has plummeted from £760m over the first half of 2008, to a record low of less than £100m in 2009. Indeed, the single deal seen in the first six months of the year was valued at just half of the average deal value seen in previous years – further testament to the limited availability of financing for larger transactions.
- While 2008 saw a larger than usual number of substantial expansion deals in the North, with private equity players adjusting their focus towards existing portfolio companies, this trend has so far not continued in 2009, reflecting a steep decline in the number of sizable acquisition finance transactions.



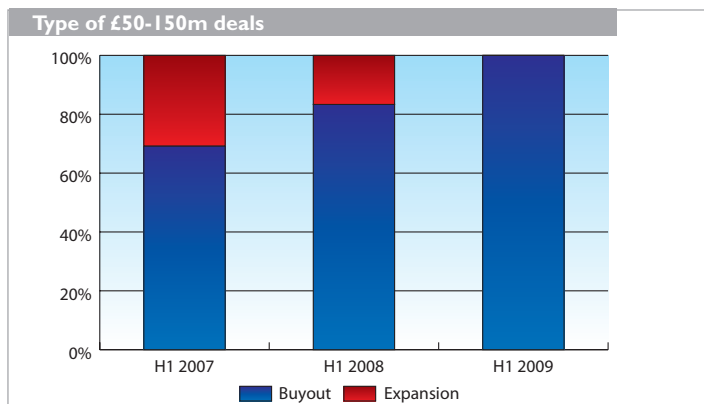
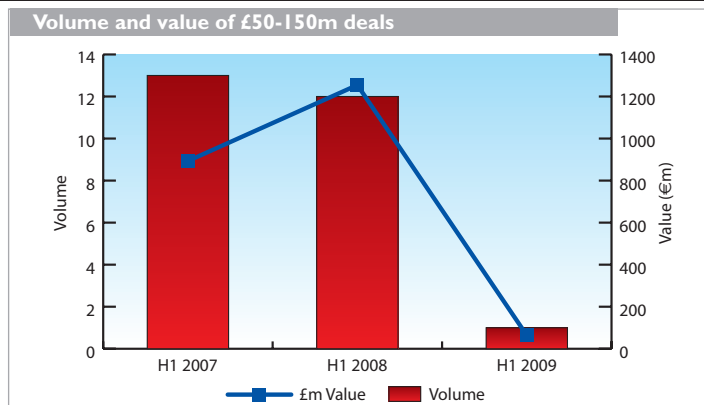
Deal activity in the £5-50m size range

- True to its status as the most active UK region, deal volume over the first six months of 2009 was highest in London. That said, the difficult macro economic environment took its toll on deal activity in the London region as well, with the volume of £5-50m transactions falling by almost 50% to 23 transactions. As deal figures for the first half of 2008 were positively affected by the rush to complete deals before the changes in capital gains tax took effect, it remains to be seen whether full year deal totals for 2009 will show a more moderate fall.
- The value of £5-50m deals in the London region fell more sharply in the first half of the year, down 63% to £235m from £630m over the same period in 2008. The drop in value is mainly due to a fall in the number of buyouts, with only four such transactions recorded in the smaller deal bracket compared to 16 in H1 2008.
- With private equity firms putting portfolio management at the top of their agenda, expansion deals saw a significant proportional increase. The total number of growth capital deals showed some degree of resilience, dropping to 15 from 22 over the same period last year and making up 65% of all transactions in the London region in the first six months of 2009.



Deal activity in the £50-150m size range

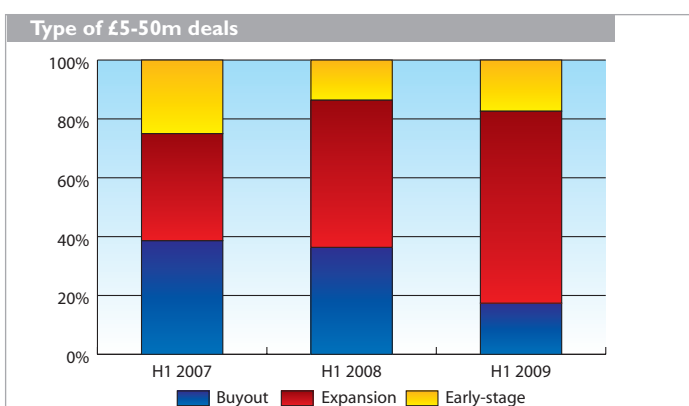
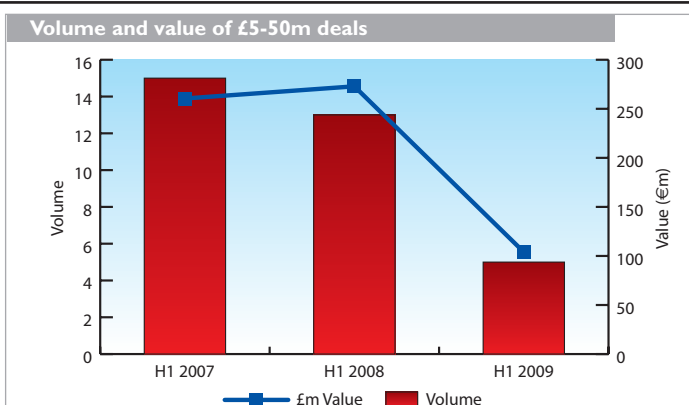
- Similar to other UK regions, transactions in the larger deal bracket remained conspicuous by their absence in the London area. Having been historically the most prominent region for deal activity in the £50-150m range, London recorded only a single deal in the first six months of 2008. Just as in other regions, the lack of leverage to support such transactions as well as limited trading visibility affecting enterprise valuation levels, have impacted negatively on deal volumes.
- With activity down from 12 deals over the same period in 2008, the total value of larger deals consequently also took a significant hit, dropping substantially from £1.3bn in H1 2008. The only transaction completed in this range was Barclays Private Equity's £64m acquisition of Bounty Group. Similar to other regions, the trend of add-on acquisitions in the larger deal range has so far not continued in 2009.



Midlands

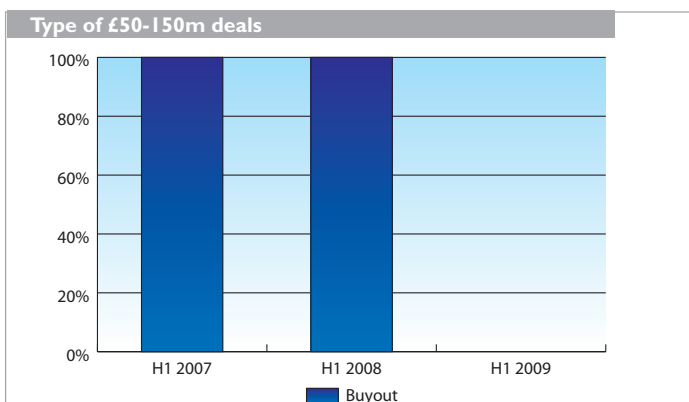
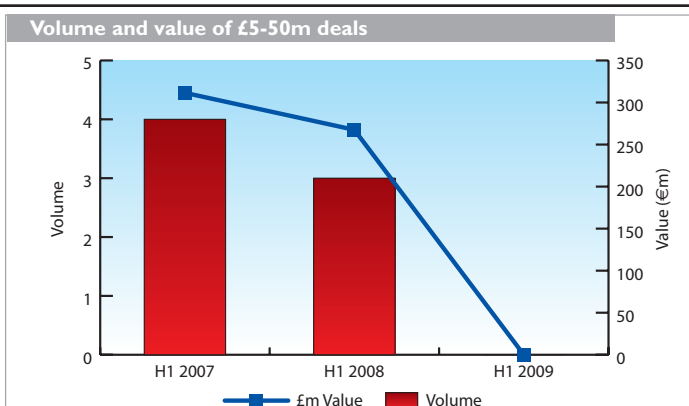
Deal activity in the £5-50m size range

- The negative trend in deal activity in the smaller £5-50m bracket could also be observed in the Midlands. In line with other regions the number of deal completions fell to five in the first half of 2009, compared to 13 over the same period in 2008 – a drop of 62%. That said, the Midlands has historically seen the least deal activity compared with other regions and it is also worthy of note that the downturn in this area was less than that seen in both the South and the North.
- The trend as far as value is concerned follows in line with volume, dropping by more than half to £104m in H1 2009 from £273m in the previous year. Nevertheless, although volume and value is down, the average size for deals completed in the Midlands is the highest among the four regions with almost £21m – almost matching the previous year's average. LDC has been by far the most active in this region completing three deals so far this year, notably Orion Media and Nuclear Engineering Services Limited.
- As the number of buyouts has fallen more significantly from 11 in H1 2008 to just three so far in 2009, expansion deals inevitably make up a higher proportion in the overall total. Noticeably, the Midlands saw no early-stage investments in the first half of the year.



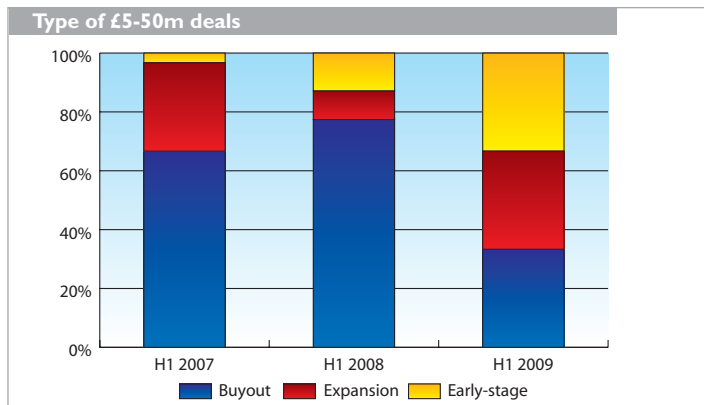
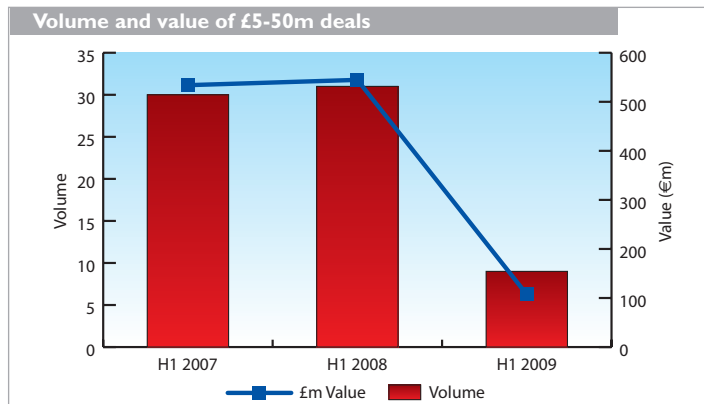
Deal activity in the £50-150m size range

- Dealflow for larger transactions completely collapsed in the Midlands region with no transactions completing above the £50m level in the first half of 2009. Although the £50-150m bracket has historically seen limited activity in the region, with four and three deals completed in the first halves of 2007 and 2008 respectively, the poor economic conditions has brought deal activity in this range to a complete standstill.
- One reason for this deal drought may lie in the fact that in the past the size range has been populated by buyouts, which are still difficult to fund. What is more, the average deal value was at £89m in H1 2008 and that would certainly require a sizeable debt package, which judging by the statistics so far in 2009 has not been readily available.



Deal activity in the £5-50m size range

- Deal volume in the smaller segment in the South collapsed by two thirds in the first half of 2009. Overall just nine deals were completed compared to 31 over the same period in 2008, a decrease that marks the end of what has been remarkably robust dealflow in the region.
- There was an even bigger drop in value terms with the nine deals totalling £107m, an 80% decrease from the £545m recorded in H1 2008. Average deal values contracted to just £12m, having remained steadily above £17m in previous years – a good indication of the new market reality characterised by falling multiples and tighter financing terms. Not surprisingly the number of buyouts completed saw a dramatic drop from 24 in H1 2008 to just three so far this year. On the other hand the number of early-stage and growth capital transactions remained steady at three deals each, resulting in deals being evenly distributed among all three deal types.
- The largest disclosed deals in the £5-50m size bracket were MML Capital Partners' £31m buyout of Vanguard Healthcare Solutions in the South West and, in the South East, the £15m financing round of Chroma Therapeutics by a consortium including Abingworth Management and Gilde Investment Management.



Deal activity in the £50-150m size range

- In line with the other regions in the study, the market for larger mid-market transactions came virtually to a standstill in the South in the first half of 2009. The region recorded only one transaction in the 50-150m range – the £72m buyout of Snell & Wilcox in the South East by LDC and Advent Venture Partners – representing a significant fall in deal activity compared to five transactions in H1 2008 and eight deals in H1 2007. Not surprisingly total value plunged considerably by 85% from £480m over the same period in 2008, while average deal value is down from £96m.
- There is also little change in the pattern of deals by type over the sample period as the larger deal bracket rarely records early-stage or even expansion deals. Indeed, though the single buyout so far this year represents a significant drop from the four seen in the first half of 2008, this compares favourably to the decline to nought seen in terms of growth-capital transactions.

