CLEARWATER INTERNATIONAL

Clearview

Q2 2020

Q2 2020 Multiples Heatmap

In-depth analysis of the acquisition multiples paid for European private equity transactions

Inside:

- Deal volume substantially impacted by COVID-19
- Multiples increased compared to the same period in 2019
- Overview of US sponsor activity in Europe
- Real estate sector focus

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European overview

This report identifies key themes driving European private equity (PE) deals' EV/EBITDA multiples on a quarterly basis. The objective is to assist PE investors in understanding drivers behind value trends across regions and sectors, leading to good investment opportunities.

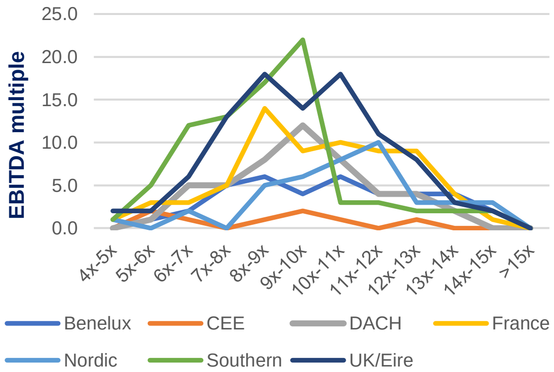
Q1 2020 suffered a slight reduction in deal volume when compared to the same quarter in 2019 as the effects of COVID-19 were not yet realised by market figures. However, with the global situation worsening throughout Q2 2020 the deals market was substantially impacted as deals in their infancy were put on hold to wait out the unfolding situation across the globe.

In Q2 2020, flight to quality and scarcity of opportunities has driven average multiples paid in PE-backed transactions throughout Europe to increase slightly when compared with the previous quarter and the same quarter in 2019. However, deal volumes were down by a third compared to the previous quarter and the lowest since Q1 2016.

For the fourth quarter in a row, the Nordic region saw the highest average multiples despite a 1% reduction versus the previous quarter and a 2% decrease against the same quarter in 2019. Despite the reductions, the average valuation for the quarter was still well in excess of 10x and reduction in deal volumes was far lower than the average drop across all European regions.

The second hottest region in Europe for the quarter was France despite experiencing the second largest drop in deal volumes at over 50%. With a 4% increase versus Q1 2020 and a 5% increase on Q2 2019 the region also revealed the second largest increases in valuations.

LTM multiples distribution by region



The third richest region in terms of valuation was the UK and Ireland with valuations remaining broadly flat and well in excess of 10x. However, the region experienced a 62% drop in deal volumes, the largest reduction of any region throughout Europe.

A similar valuation trend was experienced in the Southern region however, average valuations were sub10x for the sixth quarter in a row with deal volumes reducing by nearly a third.

Despite demonstrating a strong quarter on quarter increase in Q1 2020, the DACH region experienced a sharp 5% decline in average valuations in Q2 2020. However, the region experienced the greatest volume of transactions in the quarter, despite only placing third in Q1 2020.

Benelux saw the largest increase in valuations of any region in the quarter, up 6% against Q1 2020 and 12% against the same quarter in 2019, bringing average valuations in the region above 10x for the first time in more than six quarters. In comparison to other regions, Benelux also experienced a modest reduction in deal volume of 16%.

European overview

Despite a 28% reduction in deal volumes for the quarter, the TMT sector experienced the largest number of PE-backed transactions for the second quarter in a row. Furthermore, average multiples were richest in the sector for the third quarter in a row, despite a 1% decrease in valuations compared to the preceding quarter and 2% against the same quarter in 2019.

The second hottest sector for the quarter in terms of valuation was healthcare, with valuations remaining well in excess of 10x for the sixth quarter in a row. Despite valuations holding in the sector, volume of deals was down by nearly 50% on the previous quarter and 40% on the same quarter in 2019.

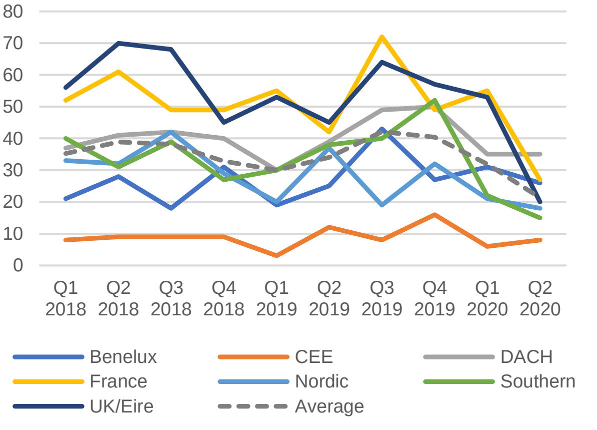
The financial services sector saw a modest reduction in deal volumes in the quarter whilst valuations remained flat versus the previous quarter, despite a 12% reduction against the same quarter in 2019. The financial services sector has often experienced the richest valuations but in recent quarters, TMT has eclipsed the sector with healthcare also continuing to challenge.

Industrials and chemicals and business services both experienced large drops in deal volumes in the quarter, 39% and 41% respectively. However, valuations remained flat in industrials and chemicals whilst business services experienced a 3% increase, both with average multiples in excess of 10x. This was the third quarter in a row that business services endured an increase in average multiples paid in PE-backed transactions.

Averages over last twelve months

Start	01/04/18	01/07/18	01/10/18	01/01/19	01/04/19	01/07/19
End	01/04/19	01/07/19	01/10/19	01/01/20	01/04/20	01/07/20
	Q1 2019	**Q2 2019**	**Q3 2019**	**Q4 2019**	**Q1 2020**	**Q2 2020**
Benelux	9.6	9.3	9.4	9.9	9.8	10.4
CEE	9.8	9.0	9.0	8.5	8.3	8.6
DACH	10.2	9.9	9.9	10.5	10.8	10.2
France	10.5	10.3	10.3	10.6	10.4	10.9
Nordic	11.5	11.2	11.0	11.5	11.2	11.0
Southern	9.3	9.4	9.6	9.5	9.5	9.4
UK/Eire	10.9	10.9	10.8	10.7	10.8	10.8
Europe	10.4	10.2	10.2	10.3	10.3	10.5

Deal volumes by region



Last quarter, the consumer sector saw the lowest valuations in six quarters, dropping below 10x for the first time since Q1 2019. This trend continued in Q2 2020 with a further 2% reduction. Deal volumes also dropped 24% in the quarter and 38% versus the same quarter in 2019.

In terms of deal size, and in line with most quarters historically, the largest volume of deals was in the sub €50m category despite a 32% reduction in deal volumes for the quarter. Conversely, the smallest volume of deals was experienced in the >€1bn range.

For the fourth quarter in a row, the richest valuations were seen in transactions >€1bn, despite being down 3% on the previous quarter and for the fifth quarter in a row, transactions between €500m-€1bn endured the second hottest valuations, being over 6% up on the previous quarter.

Deals in the €250m-€500m range showed decreasing valuations of 6% and 9% when compared with the previous quarter and same quarter in 2019 respectively whilst also being the only deal range to experience an increase in deal volumes with more than a 100% increase.

Valuations remained broadly flat in the €50m-€250m deal range despite a reduction in deal volumes of nearly 40%.

In this quarter, the Multiples Heatmap focuses on trends seen in US sponsor activity in Europe and the real estate sector now the effects of COVID-19 have come to fruition.

This publication reports averages of multiples in the last 12 months for each quarter per region, sector and deal size.

US sponsor activity

In spite of the economic volatility brought about by the coronavirus pandemic, United States (US) sponsors are continuing to view Europe as a solid market for investments, says Brett Donelan, a Managing Director in the Financial Sponsors Group of KeyBanc Capital Markets.

US sponsors completed 27 buyout deals in Europe in H1 2020 totalling circa €13.59bn ($16bn), according to Unquote Data. Although this is a drop from the 40 buyouts completed in first half of 2019 with an aggregate value of circa €20.3bn ($23.8bn), US sponsors were still involved in some of the largest deals recorded in the European market in the challenging environment brought about by the coronavirus pandemic. Such deals included Insight Venture Partners' circa €4.5bn ($5bn) buyout of Swiss software business Veeam, as well as KKR's circa €4.7bn (£4.2bn) carve-out of UK-based Viridor Waste Management.

Targeted fundraising in the US is evidence of the enthusiasm of US sponsors for the European market, Donelan notes. KKR closed its fifth European Fund in November 2019 on €5.8bn, while Carlyle held a final close for its fourth Carlyle Europe Technology Partners fund in January 2019 on €1.35bn and for Carlyle Europe Partners V in October 2019 on €6.4bn. Such fundraises are also testament to the desire of such sponsors' LPs to reap rewards from European investments.

The European M&A field has also traditionally seen lower valuations than the US market, which naturally makes for appealing investment prospects. Donelan adds: "On average, in recent years US PE deals have generally traded at one multiple higher than European ones."

Europe has long been an appealing market for US sponsors, with the UK and Ireland a particularly favoured region. "The UK is culturally similar to the US, with a common language, relatively low corporate tax rates, good transport infrastructure and a stable legal environment," Donelan says. He adds that Ireland is also positively viewed by US investors. "Ireland is the most western point of Europe, so there are a number of data centres there, which is also good for sponsors looking to invest. A lot of US companies with European headquarters agree that Ireland is a good place to be, such as Google and Microsoft. So, it will continue to be a good place for US private equity to spend time."

"Brexit uncertainty has led to headwinds when it comes to deal activity in the UK, but I would expect there will be an uptick when sponsors can move forward with transactions that have been delayed," says Donelan.

The DACH region, and Germany in particular, is also a market that has traditionally sparked interest from US investors, exemplified by deals including the acquisition of Stada by Bain's European arm, alongside Cinven, in 2017. "English is widely spoken in Germany and it's viewed as a robust and stable economy," says Donelan. "Its business culture is known for precision and efficiency, which US investors like."

Donelan explains that some US-based GPs have already looked to Europe for more complex deals as the M&A and debt markets have fluctuated. "When the pandemic presented itself, most PE firms were initially focused on the liquidity of their portfolio companies; we saw many companies drawing on their revolvers, even just for precautionary reasons. The next step was focusing on company projections and whether they had the appropriate cost-cutting measures in place. Many sponsors then decided that they would get active in this environment – for example, in buying up secondary debt or in making structured investments such as PIPEs."

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US sponsor activity

While there has been less plain vanilla buyout activity from US sponsors in recent months, there will be opportunities for such investors as the market stabilises, Donelan suggests. “The equity and debt markets are currently trading up. There will be less opportunity to buy things at a discount, but there is more regular M&A dialogue. TMT and healthcare are certainly where we are seeing an uptick, as well as in business services.”

Beyond platform investments, US GPs have historically looked to the European market to find add-ons for their US-headquartered portfolio companies, a strategy which presents both opportunities and challenges. “I would say the two main advantages that US sponsors and their portfolio companies have when seeking European acquisitions are ready access to US financing markets, and the multiple arbitrage generally observed between the US and European deal markets,” says Donelan. “The obvious disadvantages can include cultural and language differences, and challenges caused by distance, such as operating in different time zones and the difficulty of meeting in-person, especially nowadays.”

COVID-resilient businesses have nonetheless been looking to expand in recent months, Donelan notes, reflecting the trend seen in platform deals. “Much of the add-on activity I have seen has been in the area of business services, especially those services less impacted by COVID.”

“US sponsors are always seeking to grow their portfolio companies, and one of the ways to do that will be to continue to pursue European add-ons,” says Donelan. US-based portfolio companies made 41 add-on acquisitions in Europe in the first half of 2020, according to Mergermarket, compared with 20 such deals in the same period in 2019, showing that add-ons have remained desirable in spite of the pandemic. Nevertheless, it remains to be seen whether appetite will hold up in the second half of 2020 as the pandemic uncertainty continues. “I do think the current COVID environment may delay that effort somewhat,” says Donelan.

Although the pandemic might also slow the pace of new office openings for US sponsors in Europe, this does not mean that appetite for deal-doing is diminishing, says Donelan. “COVID has made international travel less desirable. PE firms globally have also accelerated their adoption of digital technology – Zoom can often be more efficient than jumping on a plane. Face to face meetings are not going away, but COVID might have changed how they are viewed.”

“US large-cap sponsors generally have the advantage of having more resources in dollars, offices and personnel,” says Donelan, noting that US sponsors are well-known for their role in high-end deals. “Without feet on the ground in Europe, it might be harder for US mid-market firms to generate deals there. But with the increased use of digital technology since COVID, you might see mid-market sponsors getting creative in terms of how they source deals in Europe. In the long term, you will see more US sponsors in Europe.”

“TMT and healthcare are certainly where we are seeing an uptick, as well as in business services.”

Brett Donelan
Managing Director,
Financial Sponsors Group,
KeyBanc Capital Markets

Harriet Matthews
Reporter, Unquote

Real estate insights

The real estate market has been deeply affected by the COVID-19 pandemic, which has rapidly changed consumers' habits and behaviour, with a direct impact on several asset classes and strong repercussions on investors' allocation and strategies.

"The pandemic has accelerated some trends already evident, exercising a noticeable influence on the view that investors have on retail and particularly on shopping centres," says Laurent Camilli, Head of Real Estate at Clearwater International. "Before the coronavirus outbreak, global consumption was already moving towards digital shopping and investors were showing uncertainty and even some mistrust towards investing in large shopping centres. This trend has accelerated due to the pandemic, which has had a critical impact on the entire retail segment. To have an idea of how deep the impact has been, we can take a look at how valuations of listed companies operating in this sector have plummeted. Shopping centres company Unibail, for example, was trading at €215 per share before the pandemic, and is currently valued by the stock market at €40 per share[1].

The pandemic has affected working habits, encouraging remote working and putting under scrutiny the ongoing trend for densification of the workplace. "The impact of the crisis on the office market has been deep and is already tangible," says Camilli. "The spread of remote working has changed the view of what the needs of office buildings really are. This is especially true for large central business districts, such as Region Ile-de-France in Paris and the City of London. Around 10% of these areas could become vacant in the next three to five years. This concern has caused uncertainty and distrust among investors towards this asset class, considering that the rental value will probably decrease in the coming months, but the cap rate will remain the same, around 3.5-4.75% depending on the location."

The hotels and leisure real estate segment has also been heavily impacted by the pandemic, with numerous deals delayed or put on hold. Camilli says: "The sector will probably fully recover only in 2022, while investments will remain very scarce in the upcoming 18 months. There might still be investors' appetite for some strategic assets, but buyers will take into account in their valuations that the next two years will be quite challenging."

1. Accurate as of 21/08/2020

Richard O'Donnell, a Partner at Clearwater International, adds: "We expect to see a number of transactions in the coming months where operating businesses with freehold assets partner with real estate funds to step-change the scale of their business. This will only apply to those operating businesses that did not have stretched balance sheets pre-COVID, but the opportunity to accelerate growth through partnering with a real estate fund will be attractive. From the perspective of real estate funds, the ability to acquire a number of freehold assets with a strong operating partner ready to trade can aid capital deployment rates and provide attractive long-term returns given underlying tenant strength."

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Real estate insights

Interesting opportunities are also available across the healthcare real estate segment, which comprises the most economically resilient property type in the industry. “Healthcare real estate, which includes both retirement homes and private clinics, has shown its resilience among the pandemic” says Camilli. “After the March 16 all the stocks of all the big listed real estate companies dropped down, except for one company, Edifica, a Belgium company which focuses on healthcare real estate assets and which has been traded with a premium on its net asset value.”

“There is no lack of liquidity in the market,” says Joe Dyke, a Partner and Head of Clearwater International Real Estate Finance in the UK. “Most of the funds operating across the real estate industry have committed capital and minimum return rates to hit and need to deploy capital into good assets.”

He adds: “Some of the largest investors which at the beginning of the pandemic had pulled out of transactions have started to come back to the market, while numerous alternative and special situations funds have been looking to deploy their capital. On the operator side we have seen well capitalised groups interested in partnering with providers of equity and debt to take advantage of attracting buying opportunities. In the next 12-24 months we expect to see a wide range of deals and interesting transactions, especially for those investors that have the right amount of liquidity available.”

Camilli says: “For many private equity firms this will be the perfect moment to raise money via real estate assets. This can be a very flexible and successful strategy, allowing them to refinance their LBOs at cheaper prices while gaining time, which is currently a major issue given the concerning outlook for the rest of 2020.”

Laurent Camilli
International Head of Real Estate

Joe Dyke
Head of Real Estate Finance, UK

Richard O’Donnell
Partner, UK

Alessia Argentieri
Senior Reporter, Unquote

Selected Clearwater International private equity transactions

MML sold Learning Curve Group to Agilitas	Singlepoint sold to Version 1	Consortium of investors acquired Bridge Farm Group from Sundial	Panhard sold a minority stake to Andera Partners
Sell-side Undisclosed	Sell-side Undisclosed	Buy-side €74m	Sell-side Undisclosed
Waterland raised unitranche debt funding to support the merger and acquisition of direktgruppe, binary, Beck et al.	Waterland raised debt finance from LGT Capital Partners to support the acquisition of imc group	Trendhim sold to Priveq	Cofigeo raised new equity finance from Crédit Agricole, Société Générale, LCL, CIC, Banque Populaire, Artemid
Acquisition finance Undisclosed	Sell-side Undisclosed	Sell-side Undisclosed	Sell-side Undisclosed

To discuss any of these topics or investment opportunities, please contact:

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