European PE Breakdown

1Q 2019

Contents

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Introduction

European PE deal activity saw a notable decline following the record-setting deal value in 2018. However, many GPs took advantage of lower prices in public equity markets to secure attractively priced take-privates, which are expected to close later in the year. Additionally, bolt-ons and software deals were standout areas driving buyout activity. Both accounted for record proportions of deal count in 1Q and will likely continue gaining share. Software was especially noteworthy, nearly trebling its share in five years. VCs and software executives alike now view an exit to PE firms in a more favorable light thanks to PE firms evolving their ownership strategy for software companies, likely leading to more future deals. The mounting levels of dry powder and constant competition for deals helped keep EV/EBITDA multiples elevated. These high levels of competition in addition to continued low interest rates also mean LBO multiples are likely to continue closing in double-digit territory.

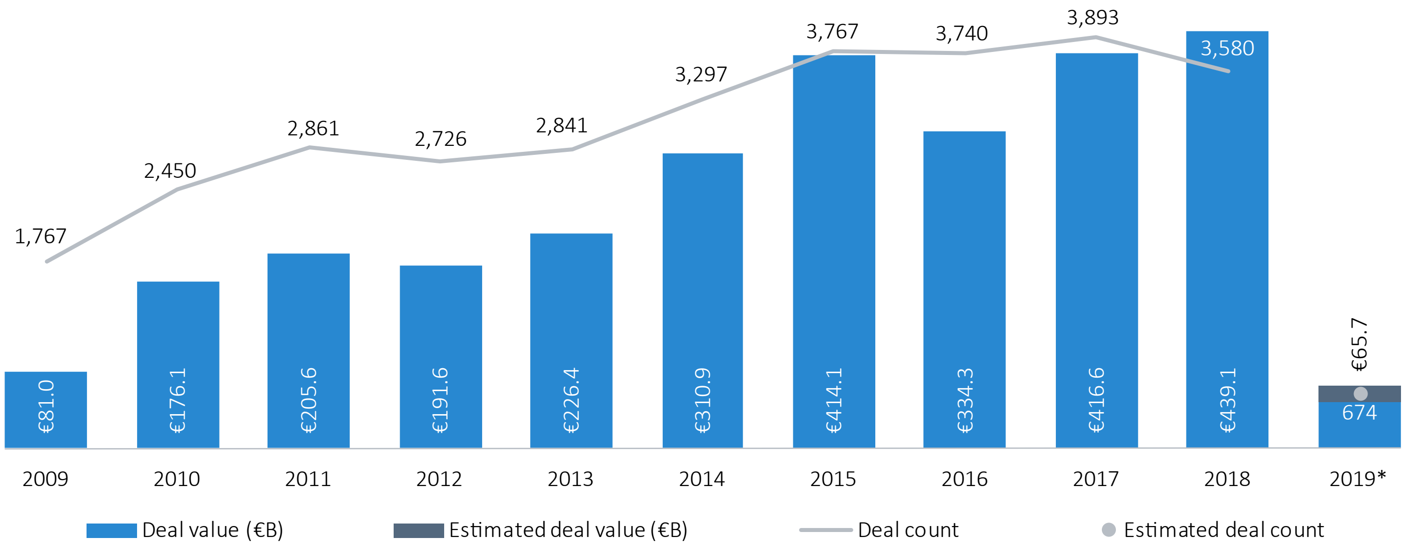
Exits experienced a similar dip, likely because GPs are waiting for public equity prices and debt markets to rebound after the declines seen at the end of 2018. Despite a recovery in public equity markets and a generally stable environment, there were no PE-backed IPOs in the quarter. Instead, GPs continued turning to secondary buyouts (SBOs), which accounted for a majority of exits in the quarter, as seen for the first time in 2018. The steadier atmosphere seen throughout 1Q should entice GPs that delayed selling, potentially pushing exit activity in later quarters above 1Q's showing.

Fundraising activity, meanwhile, was robust, driven by a flurry of middle-market-focused vehicles. This ran counter to the trend of late that saw mega-funds driving fundraising levels. The lone mega-fund to close was in France, which saw several massive funds close in 1Q. Looking forward, with multiple mega-funds (€5 billion+) currently in the market, fundraising figures look poised to continue their healthy pace throughout the year.

Wylie Fernyhough
Senior Analyst, PE

Overview

PE deal activity



Source: PitchBook | **Geography:** Europe
*As of March 31, 2019

European PE deal activity slowed in 1Q 2019 after 2018's record showing. The first quarter saw GPs close on 674 deals valued at €65.7 billion—YoY declines of 26.8% and 34.2%, respectively. The fall in deal value was attributable to the lower count as well as the downtrend in mega-deals (€1 billion+). Just three mega-deals closed in 1Q 2019, the lowest figure in three years. In 4Q 2018, pricing for leveraged loans and high-yield bonds—typically used to finance LBOs—dipped, which meant financing costs were overly burdensome during much of the quarter, and many PE firms postponed deals as a result. A similar decline in public markets, while depressing mark-to-market pricing, created take-private prospects, however. Several PE firms pounced on the opportunity in 1Q as credit markets thawed, securing deals such as the €3.0 billion take-private of satellite telecommunications company Inmarsat.

While deal count and value lagged previous quarters, bolt-on activity continued heating up. During the quarter, bolt-ons accounted for over 55% of deal count, the highest on record, though with nine months remaining in 2019, these figures could move meaningfully by year end. Although bolt-ons tend to be smaller than the median deal size, the bolt-on acquisition of payments company Concardis was the largest deal to close in 1Q. The company was acquired by competitor Nets just months after the firm was bought out by a Hellman & Friedman-led consortium, creating a payments powerhouse.

The enduring ascension of bolt-ons is a continuation of a trend that began over a decade ago. It is also likely one reason PE bids have remained competitive with strategics. In fact, GPs have been outbidding corporates in recent years.[1] Strategics can typically justify a high purchase price due to expected synergies, but research indicates that through the bolt-on strategy, PE firms can price in expected synergies and are able to capture at least some of these anticipated synergies, allowing them to bid competitively with corporates.

In addition to bolt-ons, buyouts in the software space have been driving European PE activity. During the quarter, software accounted for 15.4% of deals, nearly three times higher than the 5.6% seen in full-year 2014. This surge in software deals is due to myriad factors, but chief among them is performance. The pooled gross multiple of invested capital for technology buyouts between 2009 and 2015 has outperformed all sectors other than healthcare.[2] These hefty returns stemmed from high organic growth rates, which appear set to continue. Gartner predicts that in 2019, the SaaS market will grow by 16.2%[3] while worldwide IT spending will rise at just 1.1%.[4] To glean the most from these buyouts, PE firms have had to rethink the PE playbook when it comes to software, looking to growth rather than simply cost cutting. After Cvent, an enterprise software company, was acquired by Vista Equity Partners for $1.7 billion in 2016, its CEO and founder, Reggie Aggarwal,

1: "Private Equity: Tech's Best Kept Secret," Victor Basta, Financial Times, January 7, 2019
2: "Global Private Equity Report 2019," Bain & Company, 2019
3: "Gartner Forecasts Worldwide Public Cloud Revenue to Grow 17.3% in 2019," Gartner, September 12, 2018
4: "Gartner Says Global IT Spending to Grow 1.1% in 2019," Gartner, April 17, 2019

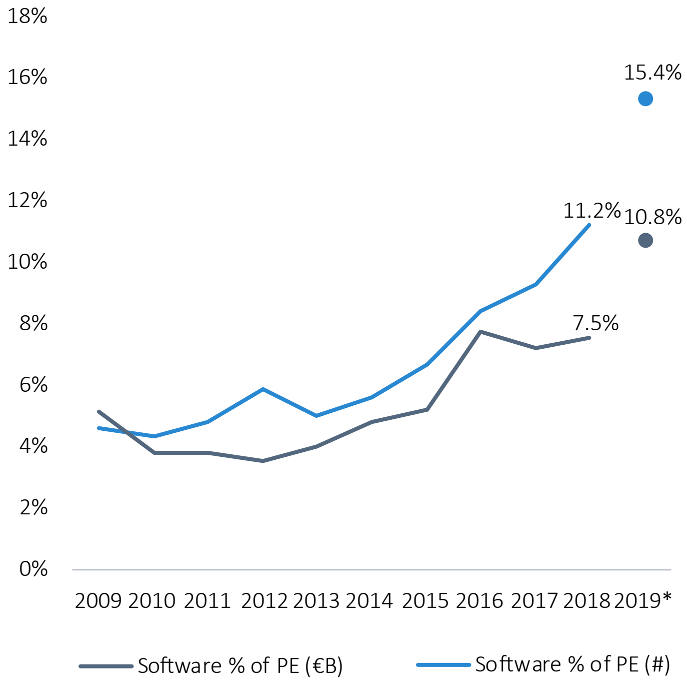
said, "You don't pay that kind of premium and then squeeze it for a profit." Rather, PE firms must continually reinvest in the company.

In light of these changes, VCs and software CEOs are coming around to the option of exiting to PE. In a post on Madrona Venture Group's website, the managing director, Matt McIlwain, wrote, "New PE owners offer a high degree of autonomy and flexibility to executives who are meeting or exceeding agreed-to milestones (admittedly with greater EBITDA emphasis over growth), as well as additional capital to take advantage of strategic opportunities."[5] In another example of the changing attitudes toward software buyouts, Jason Lemkin, a SaaS founder, described selling to PE firms as "a wonderful third option for liquidity."[6] As founders and their investors become more comfortable exiting to PE firms, this option is likely to become more frequent, further propelling software PE deal activity.

Looking to the rest of the year, software deals ought to continue gaining share in PE activity. Two of the largest announced PE deals yet to close are technology deals, including the €5.7 billion take-private of Germany-based online marketplace Scout24 and the $2.0 billion (£1.6 billion) take-private of UK-based online travel company Travelport. European regulation may also be fostering the next generation of software targets. Laws such as the recently enacted GDPR, while a hindrance to most businesses, are creating opportunities for software firms in the bourgeoning fields of data tracking, protection, and management.[7]

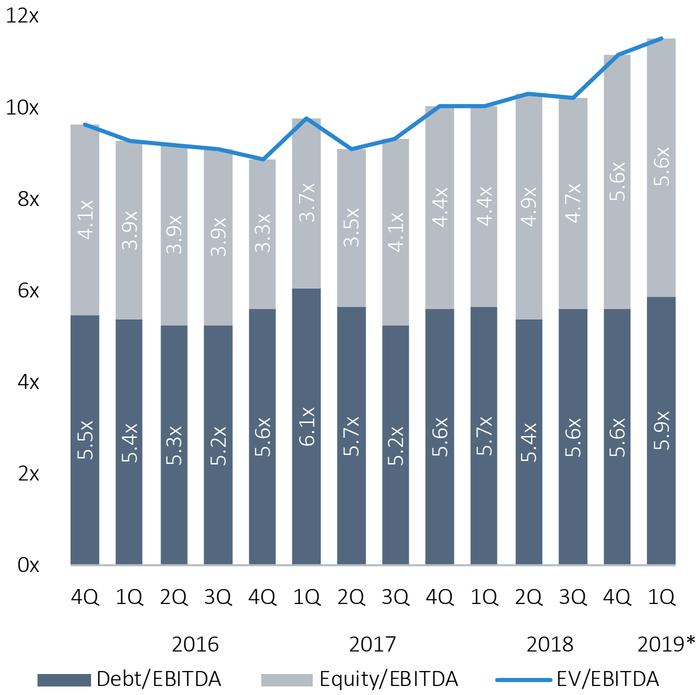
While many of the deals to close this quarter were priced in 4Q 2018—when public equities were expected to put downward pressure on pricing—multiples remained aloft during the quarter. Looking at the last four quarters, the median European buyout multiple was 11.5x, the highest figure on record. During the quarter, several deals closed above 10x, including the €200 million buyout of beverage dispensing equipment manufacturer Celli by Ardian and the company's management, which closed at 11.8x. Such elevated pricing has led to firms loading up on debt and aggressively making pro-forma adjustments to rationalize the buyouts. Jonathan Lavine, co-managing partner at Bain Capital, reportedly called attention to these trends, arguing that PE firms are accumulating too much debt in the competition to secure deals. However, the European Central Bank's prolonged low interest-rate policy, which is leading to depressed credit costs, means highly levered transactions are here to stay, at least for the time being.

Proportion of PE deals targeting software companies



Source: PitchBook | **Geography:** Europe
*As of March 31, 2019

PE buyout EV/EBITDA multiples (four-quarter rolling median)

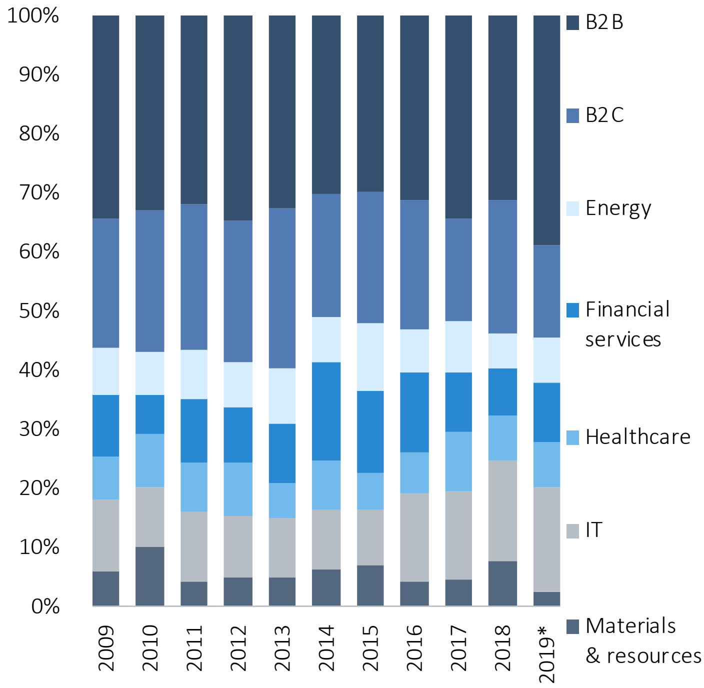


Source: PitchBook | **Geography:** Europe
*As of March 31, 2019

5: "How VC-to-PE Buyouts Can Change Market Dynamics for Later-Stage, VC-Backed Companies," Madrona Venture Group, Matt McIlwain
6: "The Rise of Private Equity in SaaS: A Gift to Founders," SaaStr, Jason Lemkin, October 4, 2017
7: "PE Firms Seeking Software," Lincoln International, William Bowmer & Scott Twibell, October 2018

Deals by sector and size

PE deals (€) by sector



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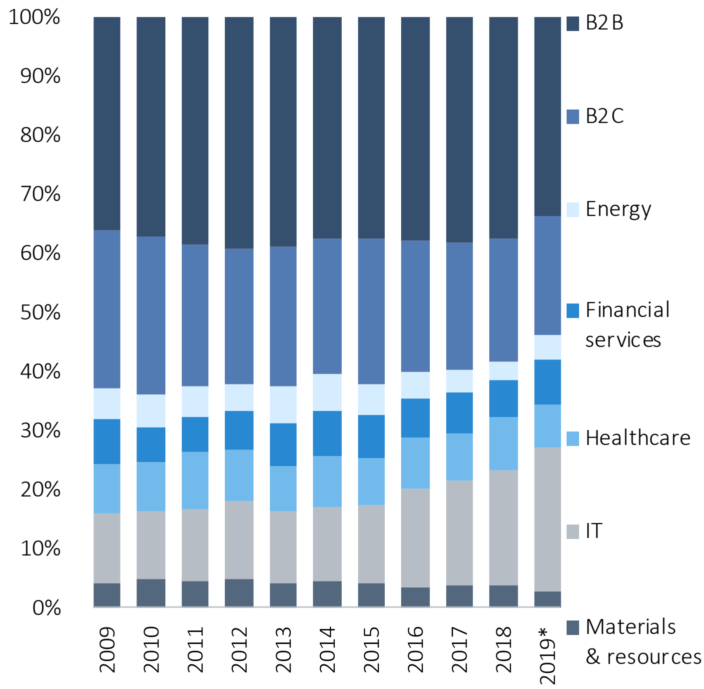
PE deals (#) by sector



Source: PitchBook | **Geography:** Europe
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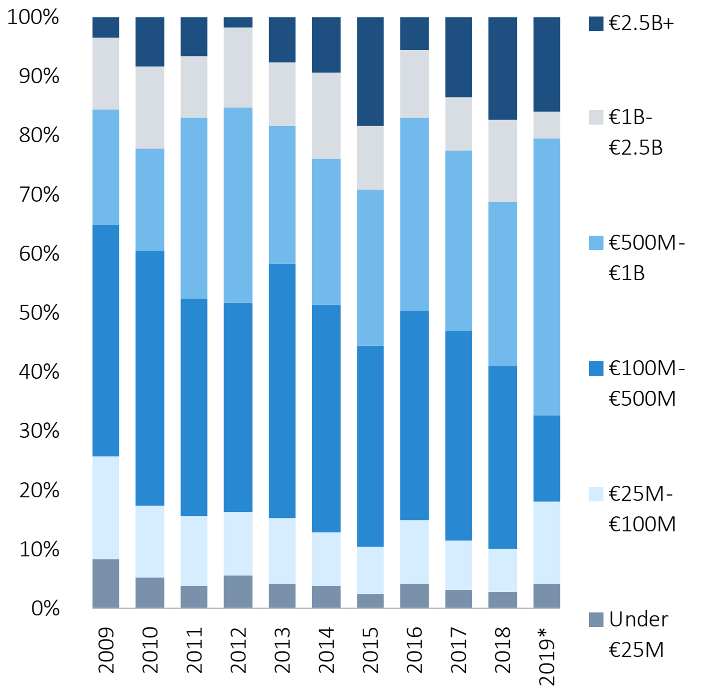
PE deals (€) by size



Source: PitchBook | **Geography:** Europe
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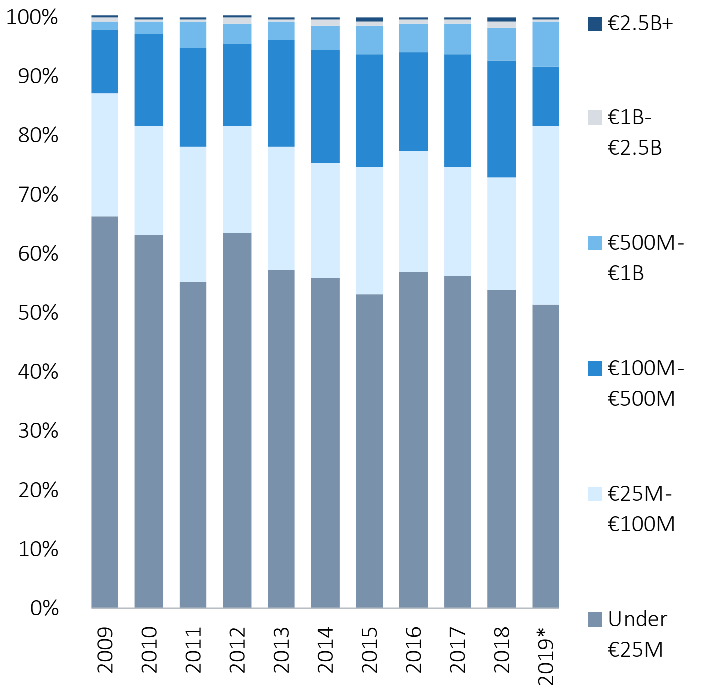
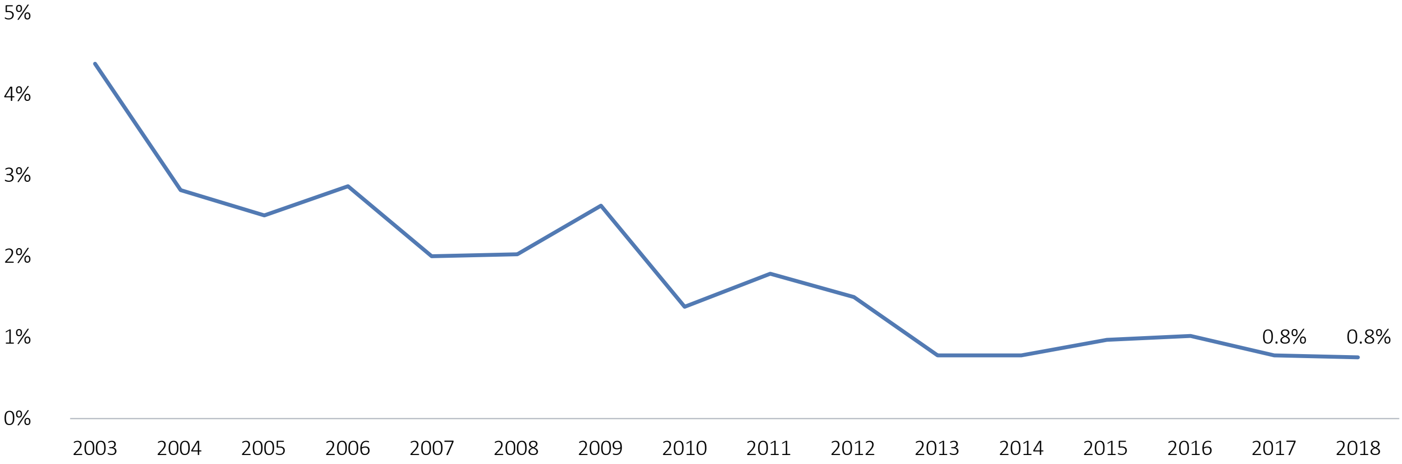
PE deals (#) by size



Source: PitchBook | **Geography:** Europe
*As of March 31, 2019

Spotlight: Take-privates

Take-privates (#) as proportion of overall PE deal activity



Source: PitchBook | **Geography:** Europe

This section was published separately as an analyst note, written by Senior PE Analyst, Wylie Fernyhough, on April 8, 2019.

Introduction

Take-private buyouts have been declining as a portion of overall deal activity for nearly two decades. In 2018, these deals accounted for 0.8% of deal flow in Europe. However, the number of take-privates has held relatively steady as the count of non-take-privates has ballooned. Interestingly, these deals now account for a higher portion of deal value than 15 years ago as the size of take-privates has dramatically outpaced non-take-privates during that time.

While the count of take-privates may be level with the figures of 15 years ago, some structural changes are underway in the PE industry that we believe will boost the number of take-privates in the coming years. Public markets in Europe offer fertile hunting ground for billion-dollar-plus buyouts that allow GPs to spend down dry powder and begin earning fees on uninvested capital. To note, PE mega-funds in North America and Europe have $328.3 billion in dry powder as of 2Q 2018 and are seeking deals sizable enough to move the needle on called capital; this is nearly double the sum of dry powder just four years prior.

Opportunities

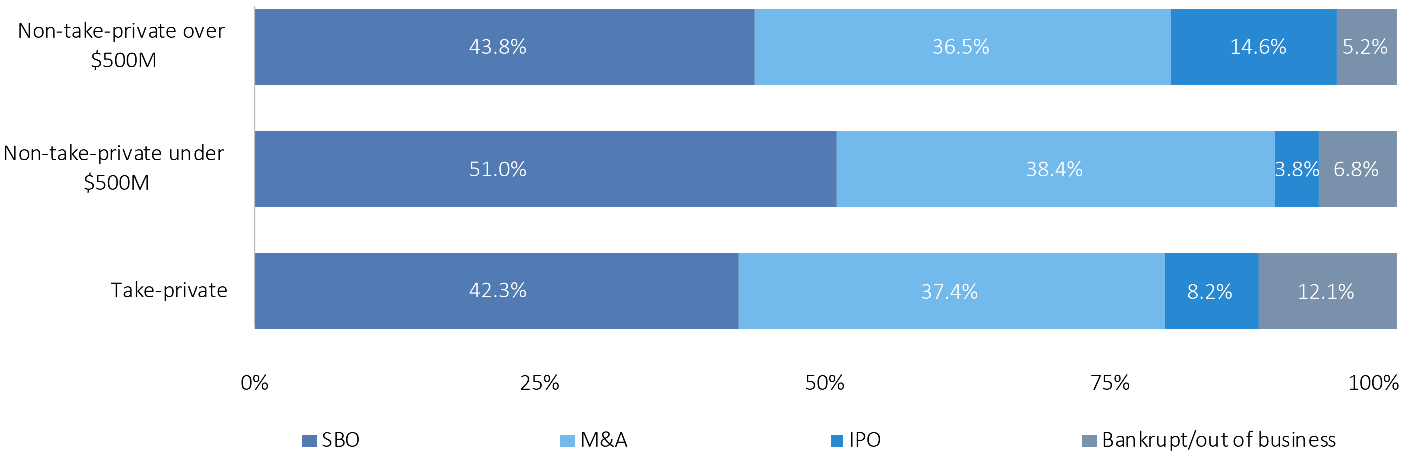
For many years, public companies traded at a premium to their private market counterparts. This was mostly due to liquidity preferences and the increased visibility into financials. Heightened competition for private assets, among other factors, has caused a paradigm shift whereby private market multiples have approximated public markets for nearly a decade. This presents PE firms with a massive opportunity. Pockets of downward volatility—similar to what we saw in 4Q 2018—can cause public companies to drop by 20% or more in a quarter. These moments of price weakness present an opening for PE firms, and many seized the opportunity.

Take-privates are also tending to focus on technology companies, evident by the recent Scout24 and Travelport buyouts. The sector accounted for 42.5% of take-private deal value between 2016 and 2018. These buyouts are happening sooner in a company's public life as well. In a recent example, cloud-based Apptio was barely public for two years before Vista Equity Partners took the company private in a $1.9 billion buyout in 2018. The median number of years since the public listing of take-private targets fell from 15.5 years in 2015 to 8.5 years in 2018. In some cases, PE firms are not waiting for companies to go public, instead acquiring them while still VC-backed or in IPO registration.

Performance

While they can be compellingly priced, take-privates present certain unique risks of which GPs need to be aware and for which they are (hopefully) compensated. Looking at exits of take-privates over the past three full years, we see these buyouts are more than twice as likely (12.1% versus 5.2%) to go bankrupt or out of business when compared to similarly sized non-take-privates. In addition to the deleterious impact bankruptcies can have on fund performance and stakeholders, bankruptcies reflect negatively upon

Take-privates and non-take-privates (#) by exit type (2016-2018)

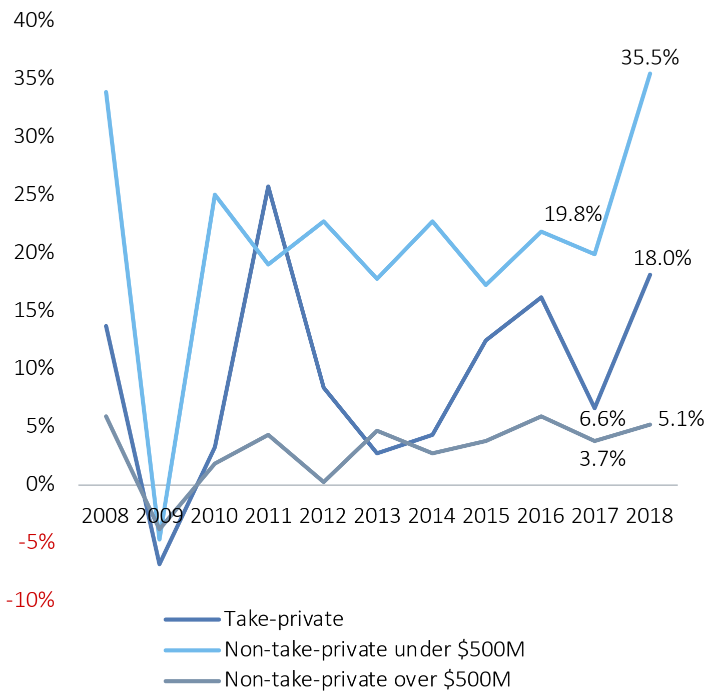


Source: PitchBook | **Geography:** North America & Europe

the GP, potentially causing reputational damage and making future fundraising efforts more challenging. One explanation for the higher rate of bankruptcy in take-private deals is that to afford these massive buyouts, PE firms employ greater amounts of leverage. Lenders are often willing to boost leverage given the lower levels of perceived risk and added levels of financial insight that can be gleaned from years of public filings. However, given the higher bankruptcy rates, this line of thinking appears flawed.

The most important question as it pertains to performance, however, is if GPs are being compensated for this additional downside risk through higher returns. Overall, we find the answer to be that performance—as measured by the annualized change in EV over the holding period—shows a discernible benefit for take-privates compared with non-take-privates of a similar size (over $500 million). One reason for this could be that GPs are able to act when price dislocation occurs, securing buyouts at more attractive prices than would be available in private markets. These findings may also give credence to the belief that public companies are overly focused on short-term thinking and become inefficient, allowing an actor with a longer-term focus to step in and realize untapped value.

Median annualized change in EV for take-privates and non-take-privates by exit year



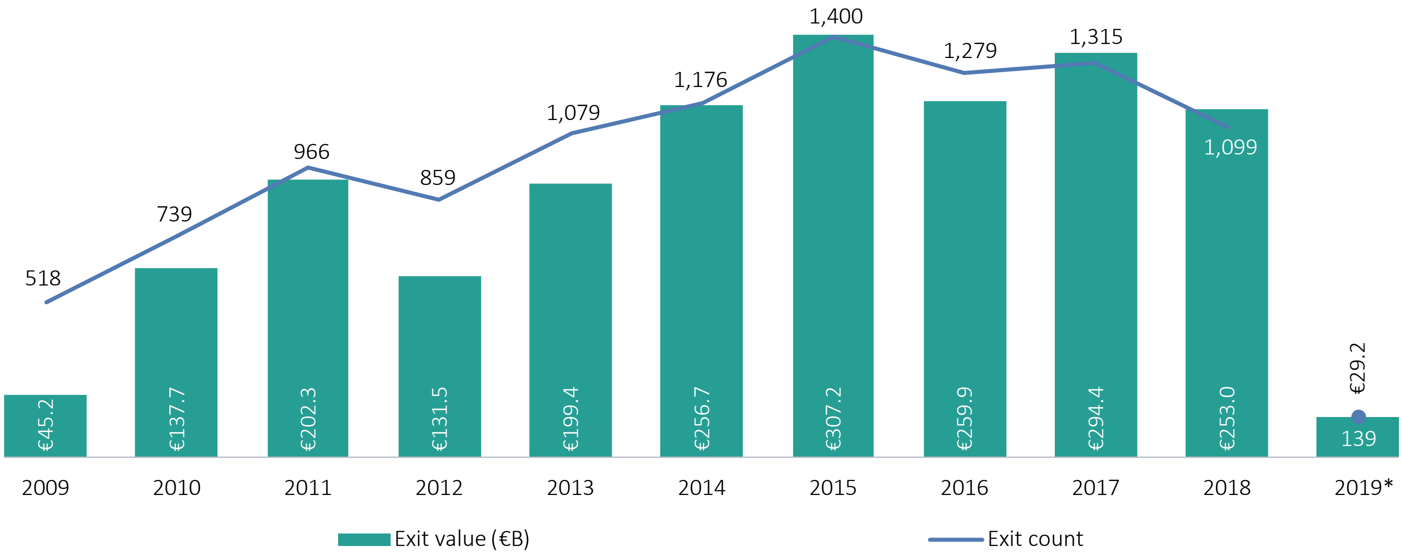
Source: PitchBook | **Geography:** North America & Europe

Conclusion

In summary, take-privates suffer a higher level of bankruptcy or going out of business but show measurable upside, as compared to similarly sized non-take-privates, to justify this risk. When looking at take-privates as a source of deal flow, GPs ought to have a clear value-creation plan laid out. Additionally, GPs may consider altering the mix of financing— favoring equity—to derisk the acquisition and hopefully avoid bankruptcy. Since take-privates present opportunities to spend down heaps of dry powder at reasonable valuations, we believe the coming years will see a rise in take-private activity. We will have to watch performance closely as the recent flood of high-profile technology take-privates are exited and see how returns stack up.

Exits

PE exit activity

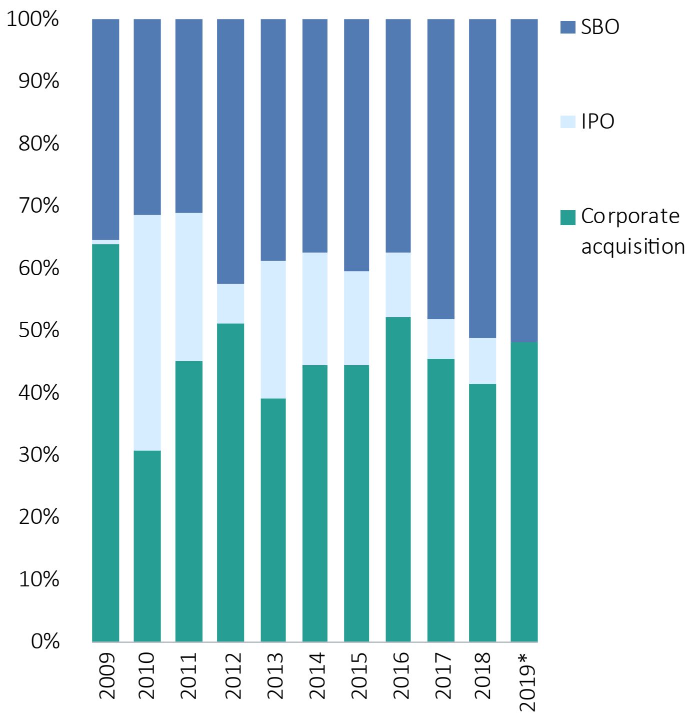


Source: PitchBook | **Geography:** Europe
*As of March 31, 2019

In 1Q 2019, PE exit activity decreased significantly, totaling €29.2 billion across 139 transactions—declines of 50.1% and 52.7% YoY. While first-quarter declines in exit activity can be seen across all deal types, SBOs continue to account for the majority of exits. Since 2009, SBOs have consistently increased their proportion of exits, lifting their share in all but three years. By contrast, the number of exits via corporate acquisition has fallen for the last three years and seems on track to continue its current downswing. In a similar vein, there were zero PE-backed IPOs in the first quarter, as GPs waited for year-end volatility to subside before listing portfolio companies.

In addition to broader public market volatility, the lack of 1Q IPOs can be attributed to multiple factors, including but not limited to geopolitical concerns, trade issues and potential economic headwinds in Europe. It was not only PE-backed companies that delayed IPOs in the quarter. Volkswagen postponed the IPO of its truck unit, Traton SE, which was anticipated to be Europe's largest IPO of 2019, citing "weak market conditions." 2019 has given way to Europe's slowest IPO market since 2009, the height of the financial crisis. However, the rest of the year has some hopeful prospects, with expected offerings from other large PE-backed companies, such as Moscow-based Sibur Holding and London-based Global Switch Holdings, which gives the rest of the year a more sanguine outlook.

PE exits (€) by type



Source: PitchBook | **Geography:** Europe
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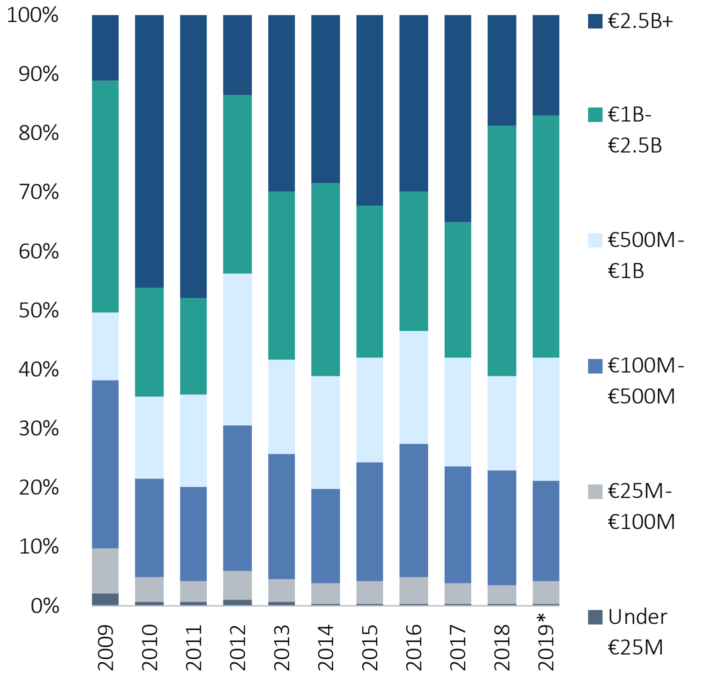
Exits

The drop in exit value can also be credited to a lack of larger exits, continuing a trend from 2018. 1Q 2019 recorded only one exit in the €2.5 billion+ bucket, the sale of Spain-based sports management and marketing company, Dorna Sports, which is most recognized for owning the commercial and television rights for the motorcycle racing world championship Grand Prix (MotoGP). The company's story is indicative of PE firms wanting to "hold onto their winners." Bridgepoint Advisers purchased Dorna in a €345.0 million SBO from CVC Capital Partners in 2006, after which Bridgepoint sold a 39% stake to the Canada Pension Plan Investment Board (CPPIB) for $518.0 million in 2012. After a growth round in 2013, and several dividend recapitalizations along the way, Bridgepoint sold the company to itself, transferring ownership to one of its newer flagship funds. It should also be noted that various PE firms were interested in the asset, some of which even submitted preliminary bids after Lazard bankers were appointed to explore a sale. Bridgepoint used these bids to calculate a "fair" sale price. We anticipate these types of GP "self-sales," especially of portfolio companies with relatively strong performance, to continue in the near term as GPs attempt to hold onto coveted assets beyond the typical PE fund lifespan as a means to navigate anticipated uncertainty.

IT has seen a spike in exit count from 12.6% in 2018 to 18.7% in 1Q, which is not wholly unexpected given the increases in deal activity within the sector in the past few years, specifically in software. One of the more notable IT exits in 1Q was of Denmark-based KMD by Advent International. KMD, which offers software services to local and central governments as well as the private sector, was initially purchased from Local Government Denmark, an association of the 98 municipalities in Denmark, in an LBO by an EQT-led consortium in 2009 for $335.2 million (DKK 2.0 billion and €267.8 million). Three years later, in 2012, the company was again exited via SBO by another consortium for an undisclosed amount. In 1Q 2019, KMD was sold to NEC Corporation for €1.2 billion to help expand NEC's business from northern Europe into the majority of European countries. This is one example of why software and IT companies have come to comprise a larger portion of deals and exits in the last few years, as they are scalable assets which often appreciate rapidly. We expect to see more exits in this vein moving forward.

PE exits (€) by size



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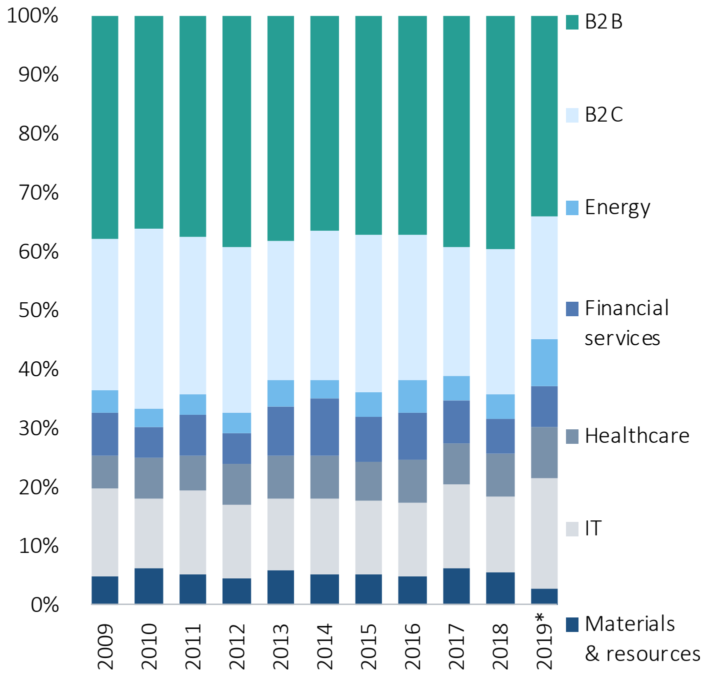
PE exits (#) by sector



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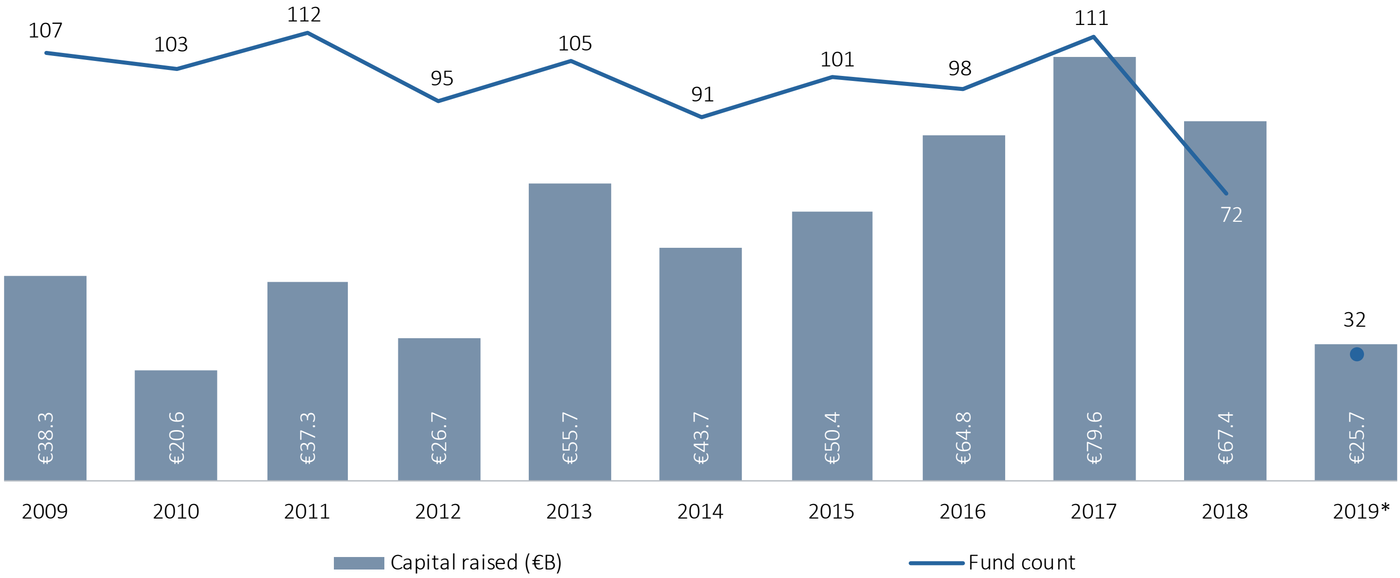
Fundraising

PE fundraising activity



Source: PitchBook | **Geography:** Europe
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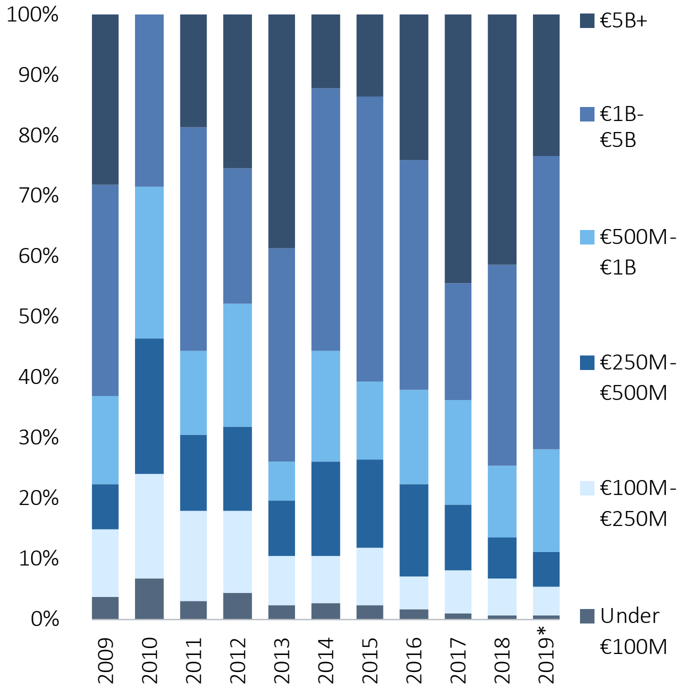
Fundraising in 1Q 2019 came in strong with €25.7 billion raised across 32 funds. This increase was largely due to healthy fundraising activity for larger France-based funds, namely in the €1 billion to €5 billion bucket. Additionally three €1 billion-plus growth funds closed in the quarter, buoying fundraising gains. These substantial increases are significant, considering they take place concurrently with vast reductions in fundraising in the UK due to uncertainty around Brexit. That said, there is at least one $10 billion fund based in the UK likely to close this year, which would alter fundraising figures drastically.

While GPs have been raising ever larger funds (noted by the sizable increase in median fund size in 1Q), only one mega-fund closed in this quarter, a €6 billion buyout fund from Paris-based Ardian. However, there are multiple European mega-funds currently open and expected to close sometime during the year, indicating that the trend toward a swelling number of mega-funds remains intact. Two such examples are Apax X, a $10 billion buyout fund based in London,[8] as well as Permira VII, a €10 billion buyout fund based in Frankfurt. Vehicles in the €1 billion-€5 billion bucket comprised nearly half of total capital raised at 48.6%, putting 2019 on pace to have the highest proportion of capital raised in this range since 2008. Interestingly, four of the seven funds raised in this size bucket were growth funds.

PE fundraising (€) by size



Source: PitchBook | **Geography:** Europe
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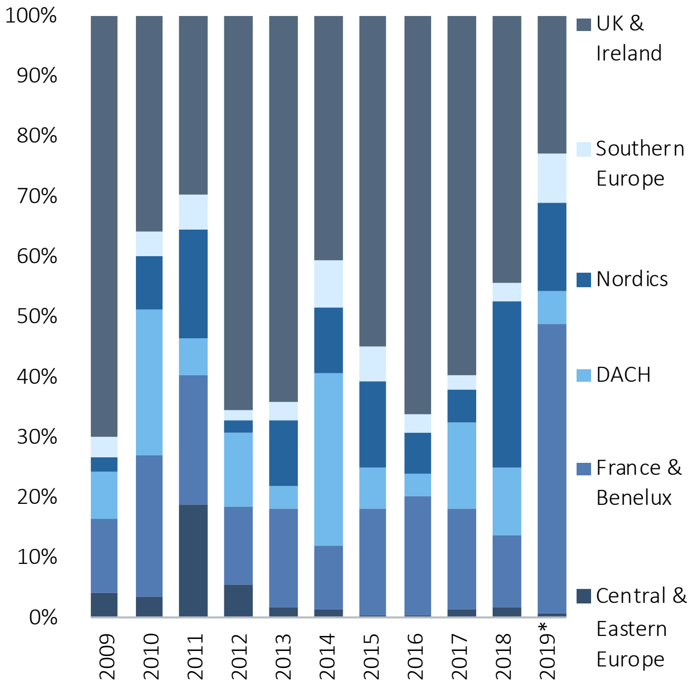
Growth funds have become more prevalent in Europe, encompassing 23.1% of fundraising value in 1Q, higher than any full-year figure since 2011. Furthermore, growth funds have been consistently accounting for a swelling portion of the funds raised in Europe. We believe that this trend is driven by two primary factors: a meteoric rise in software investments and a demand for earlier stage companies after a decade of slow growth in the region. We believe the mounting interest in growth investments will continue so long as market conditions in Europe remain stable.

8: Although Apax is based in London, its funds are denominated in USD.

PE fundraising (€) by region



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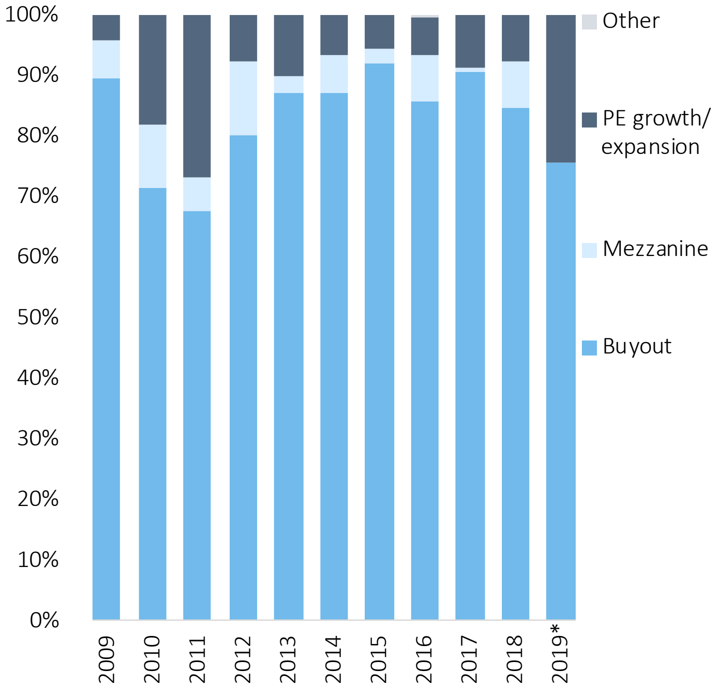
PE fundraising (€) by type



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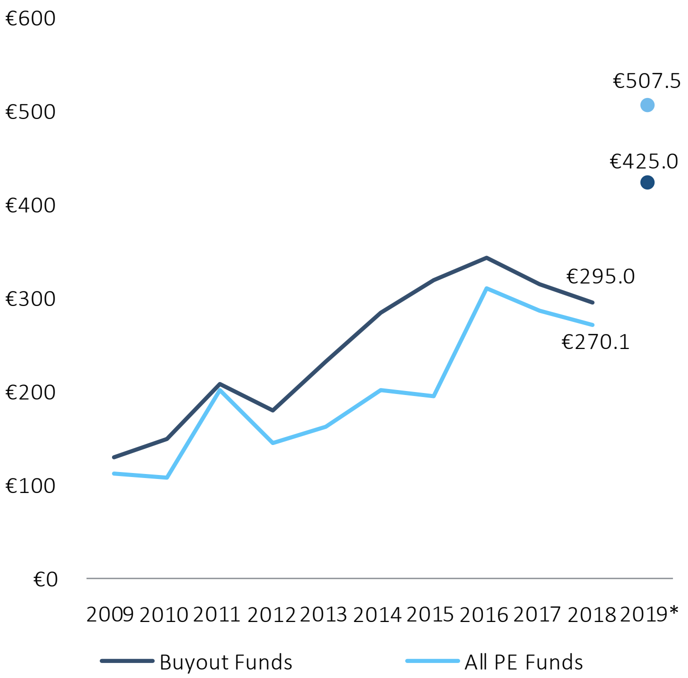
Counterintuitively, the average time to close a buyout fund has been decreasing since 2017 while the average time to close all PE funds has risen over the same time period. This may be due to LP apprehension over investing in a relatively newer strategy, growth funds, juxtaposed with the familiarity of investing in a buyout fund with a laudable track record. Of the 11 growth funds raised in the quarter, the UK raised four of them, which is notable given the region's diminished role in fundraising in the last few years.

In 1Q, the France & Benelux region accounted for 48.3% of total capital raised across Europe. Fundraising in France was especially strong with the aforementioned Ardian LBO Fund VII as well as Astorg Partners' Astorg VII, both based in Paris. The Astorg VII fund, which closed in January at €4 billion, represented a near 100% step-up from its €2.1 billion buyout fund closed in 2016. The firm tends to invest in global B2B niche market leaders with an EV range of €200 million to €1 billion. Astorg focuses on a limited number of portfolio companies in a single fund to maximize gains from its investment. However, this hyper-concentrated method of holding companies can lead to varied returns. For instance, Astorg's 2007 fund Astorg IV is a top-quartile performing fund, but its subsequent fund, 2011 Astorg V, is a bottom-quartile performing fund. Given that Brexit has been delayed another six months, the coming quarters will help inform us which regions address the gaps in fundraising stemming from the UK's likely decline in commitment figures.

Median PE fund sizes (€M)



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