PitchBook

In partnership with

ACG

Association for Corporate Growth

European PE Breakdown

2018 Annual

PitchBook

In partnership with ACG Association for Corporate Growth

Contents

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Introduction

In 2018, European PE saw:

•€396.3 billion total deal value across 3,208 deals (YoY decreases of 4.5% and 12.8%, respectively)

•€216.2 billion total exit value across 969 exits (YoY decreases of 22.9% and 24.5%, respectively)

•€66.0 billion total capital raised across 67 funds (YoY decreases of 9.0% and 36.2%, respectively)

European PE deal value was down slightly in 2018 while count saw a steeper decline. Access to financing remained inexpensive, and a rise in overall leverage helped dealmakers bid up for deals, pushing up the average deal size. These factors, coupled with increased competition, meant that EV/EBITDA multiples rose as well, with the median hitting a record high, despite the decline seen in public market indices across the region, which typically depresses multiples due to mark-to-market practices. The pressure from poor equity markets performance allowed activists to effectively agitate for change, sparking deals across the region.

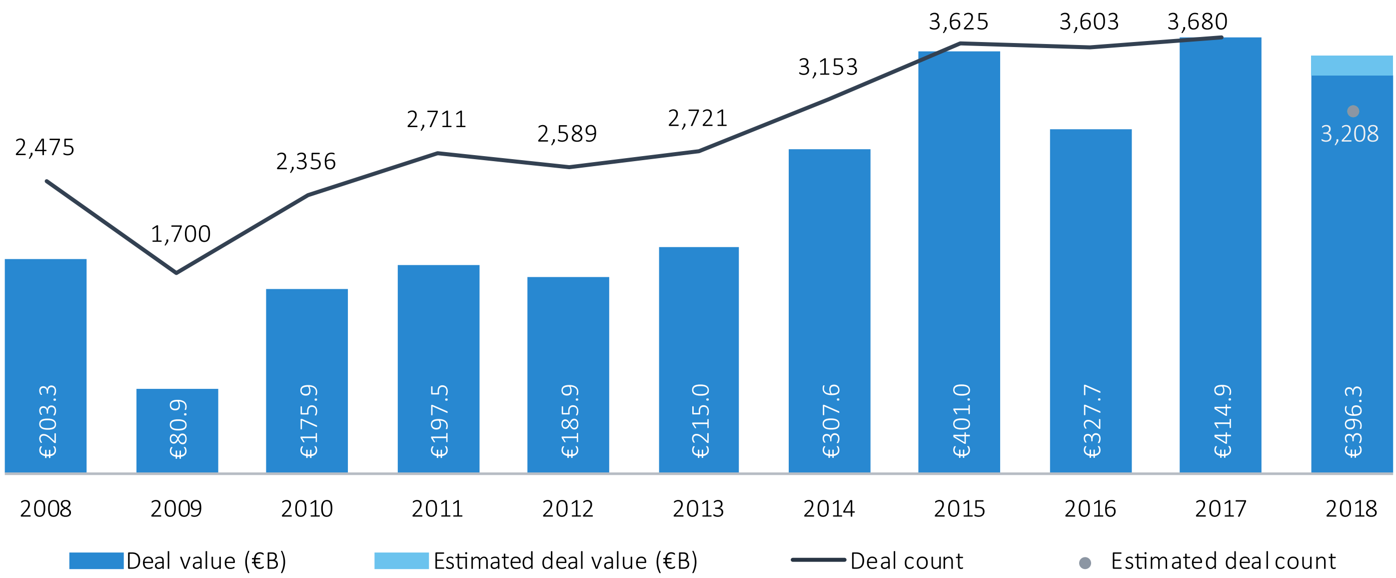
While the decline in deals was marginal, the drop in exit activity was more substantial. This is not a new development, however. Exit activity has been trending downward since peaking in 2015. Secondary buyouts (SBOs) further lifted their share of exit count in 2018, accounting for over half of all exits for the first time on record. IPOs—common among larger exits—saw little action on the year due to broad-based weakness in public market indices throughout the region.

Fundraising saw declines in count and value as well. Particularly noteworthy was the steep decline in the number of vehicles raised. European PE firms raised the fewest funds in over a decade, yet the total capital raised was the second-highest amount raised post-financial crisis. As a result, the average buyout fund hit a record, eclipsing €1 billion for the first time.

Wylie Fernyhough
Analyst, PE

Overview

European PE deal activity



Source: PitchBook

After a record-setting 2017, deal activity in 2018 softened, totaling €396.3 billion across 3,208 deals—YoY declines of 4.5% and 12.8%, respectively. Deal value was relatively steady despite waning deal count due to the median deal size rising 22.5% to €24.6 million. Interestingly, despite the lower overall deal value, 2018 saw more mega-deals (€1 billion+) close than 2017—45 compared to 40—though only one deal valued above €10 billion closed. A Carlyle-led consortium bought out the specialty chemicals division of AkzoNobel for €10.1 billion and subsequently renamed the division Nouryon. The carveout came after fellow specialty coatings manufacturer, PPG Industries, made an unsolicited takeover offer and after activist investment firm Elliott Management pressured the company.

A €6.4 billion debt package was secured to finance the buyout, pushing the debt portion to just over 6x the previous year's EBITDA.[1] The debt package was also notable because of the market demand for buying up the loans and bonds. During much of the year, a seemingly insatiable appetite for fixed-income products helped dealmakers secure cheap acquisition financing. The underwriting banks received more than $20 billion of orders for the $6.5 billion in loans and $1.2 billion in bonds, allowing borrowers to secure lower interest payments on certain tranches as well as keep several covenant-light clauses. The mixture of loans and bonds also speaks to the general shift PE is undergoing, tending to favor loans to bonds.

Loans are now the preferred option for financing. The end of 2018 saw a jarring drop in market appetite and pricing for debt packages used to secure previous LBOs fell substantially. In December, the US loan market saw its largest monthly loss since 2011.[2]

In another example of American PE firms closing mega-deals in Europe, KKR's €5.6 billion acquisition of Unilever's spreads business was the second-largest buyout of the year. After Kraft Heinz made an unsolicited—and ultimately unsuccessful—offer to buy Unilever, the company reexamined assets and decided to focus on growth businesses. The slower-growing, cash-flowing business was sold off. This buyout also utilized loans for the bulk of financing needs, with €4.6 billion in loans and just under €1 billion in bonds. The loan and broader fixed-income markets bear watching in 2019 due to their knock-on effects on deal pricing.

Also worth watching in 2019 is the rise to prominence of non-PE firms buying out companies, especially Elliott Management. The firm, known for its relentlessness, has undertaken multiple activist campaigns throughout Europe and recently asked investors for another $2 billion to target buyouts. In December, the company—along with Siris Capital—agreed to buy UK-based travel services company Travelport for €3.9 billion ($4.4 billion). Other hedge funds will be watching this deal and looking to follow Elliott's lead if returns bear out.

1: "Wall Street Wins Its High Stakes Bet on Akzo Nobel Buyout," Bloomberg, Lisa Lee & Laura Benitez, September 21, 2018
2: "Leveraged Loans Suffered Biggest Monthly Decline in Seven Years," Bloomberg, Lisa Lee, January 2, 2018

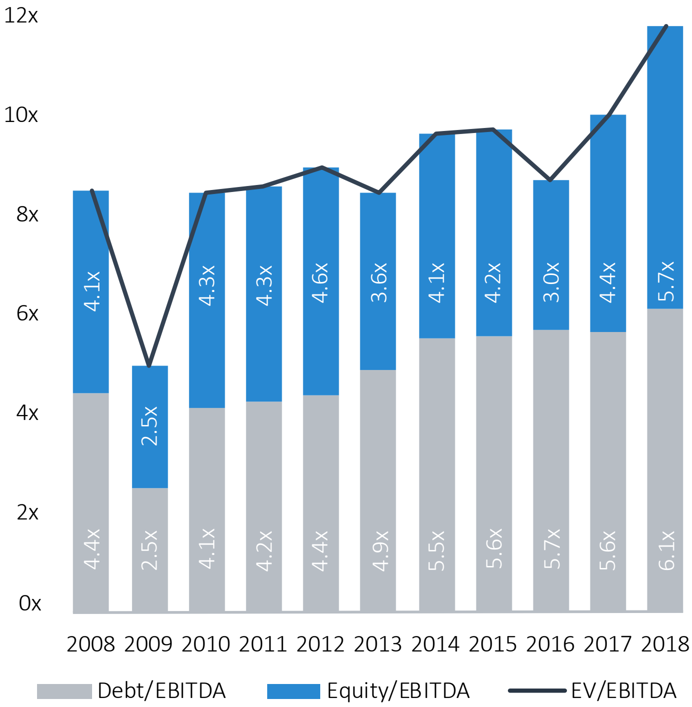
Overview

The easy financing available for most of 2018 allowed dealmakers to pay up for deals. The median buyout multiple vaulted to the highest level on record, surpassing the 11.6x pinnacle set in 2007. Deal multiples often went well into the double-digits, such as JAB Holdings' €1.7 billion (£1.5 billion) buyout of Pret a Manger—which priced the company at an EV/EBITDA multiple of 17.0x. The largest jump was to the equity portion paid, rising more than a full turn to 5.7x from 4.4x. Reasons for this could be a desire to more quickly spend down dry powder and/or plan ahead with an additional equity cushion in case of future economic hardship. While debt levels were certainly elevated in 2018, they did not reach the levels seen prior to the global financial crisis. Though 2018 saw debt/EBITDA eclipse 6x (6.1x), 2007 hit 7x. Today's lower interest rates and larger equity proportion ought to allow PE firms additional flexibility if an economic slowdown were to occur. The EU's GDP growth is slowing, Brexit seems to be taking a measured toll on the UK, and Germany and France are at risk of entering a recession.

As prices return to pre-crisis levels, the composition of deals has shifted. IT has ballooned as a proportion of deal count and value. In 2007, IT accounted for 10.7% of European PE deals and 8.6% of total value. By 2018, the sector had roughly doubled to 19.9% of deals and 17.2% of total value. 2018 saw myriad high-profile IT deals, including the buyout of Danish payments company Nets for €2.5 billion (DKK 33.1 billion) by a consortium led by Hellman & Friedman. The sustained push into IT—thanks to solid growth profiles and relatively stable cash flows—has changed the PE industry and spawned dozens of tech-focused PE firms. IT's record year was offset by a decline in financial services, which saw its proportion of overall deal count (6.1%) and value (7.2%) hit the lowest levels since 2007.

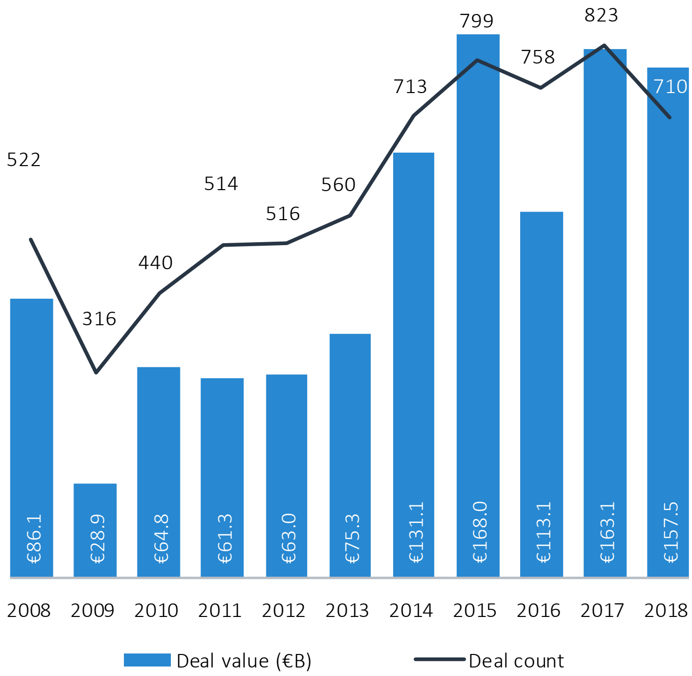
Another change occurring within the European PE landscape is taking place in the investor base—namely that more non-European investors are leading deals or are part of a consortium. Each of the 10 largest European PE deals in 2018 involved at least one non-European buyer, with nine out of 10 involving a North American investor. During the year, non-European investors participated in 710 European deals worth €157.5 billion. Though the count and value of these deals declined YoY—mirroring European PE in general—the percentage of deals involving non-European investors rose to 23.2%, the highest figure in over a decade. The trend has generally been rising since the financial crisis and ought to continue going forward.

Median European PE buyout multiples



Source: PitchBook

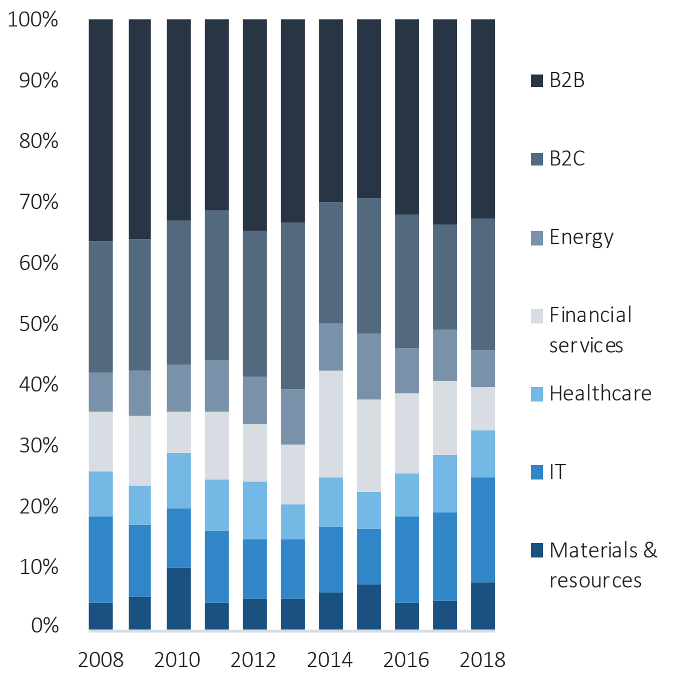
European PE deal activity with non-European investor participation



Source: PitchBook

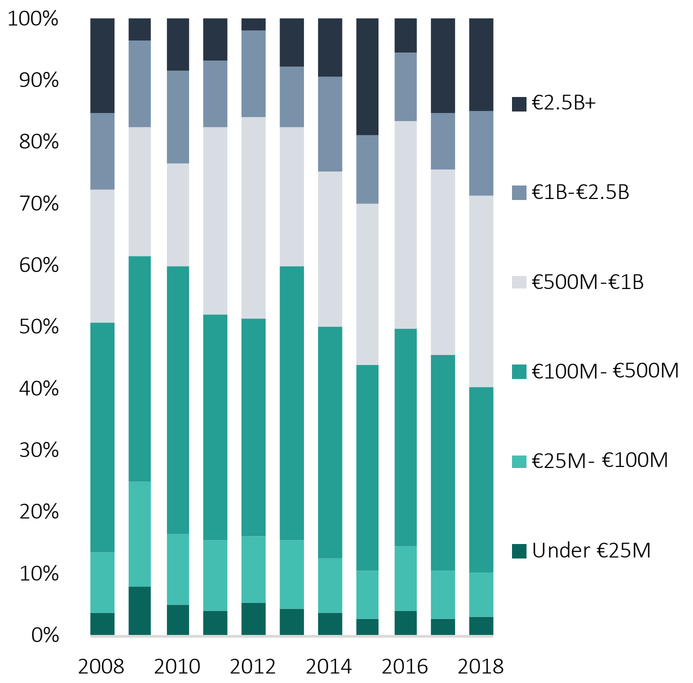
Deals

European PE deals (€) by sector



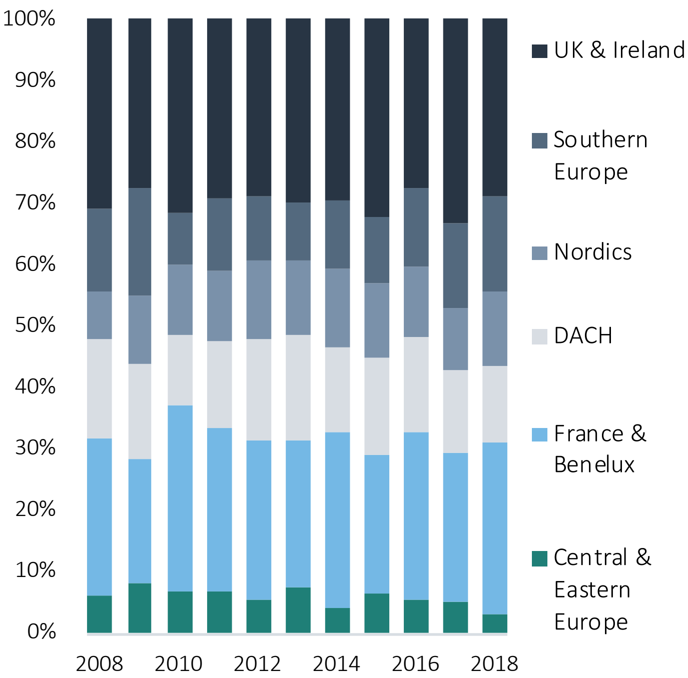
Source: PitchBook

European PE deals (€) by size



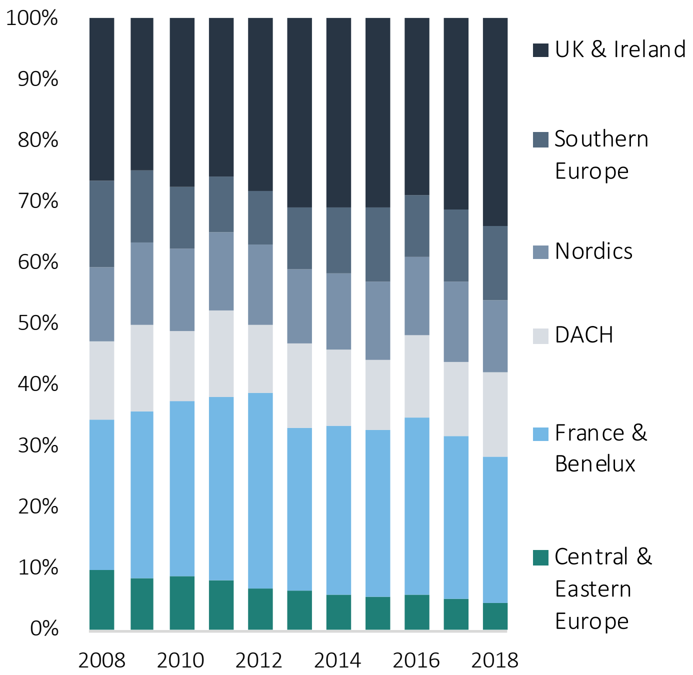
Source: PitchBook

European PE deals (€) by region



Source: PitchBook

European PE deals (#) by region



Source: PitchBook

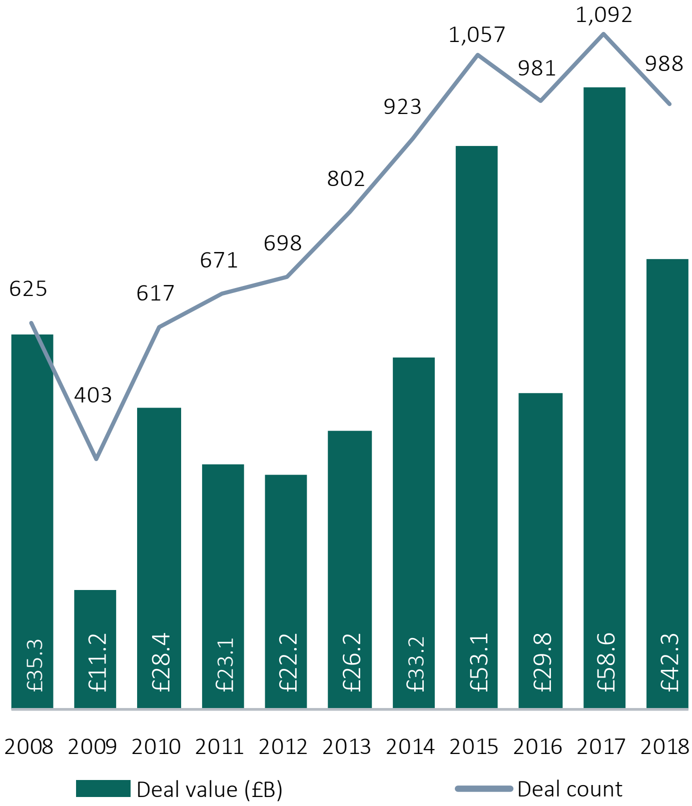
Regional spotlight: UK

With Brexit present in headlines on a daily basis, we thought it appropriate to look at UK data. With weekly announcements about financial services companies moving workers—or even regional headquarters—out of London, there can be no question that Brexit is having some effect on the UK economy. In just the past few weeks, Cboe Global markets announced it will move most European equities trading to Amsterdam if Brexit occurs, and CME Group will transfer its foreign-exchange forwards & swaps venue to Amsterdam as well. Many others are already moving staff and operations outside the UK in anticipation of the March 29 cutoff date.

The data for PE, though, is a mixed bag. In 2016, the year the Brexit referendum passed, deal value experienced a marked downturn. However, most of the slowdown in that year occurred in the first and second quarters, prior to the referendum. Furthermore, deals take several weeks, if not months, to close, meaning much of the weak data was bound to occur whether Brexit did or not. 2017 then went on to post the highest deal count and value on record for UK PE. 2018, though, seems to be the year in which Brexit really began to bite. Deal value was down 27.7%, compared with 5.9% for broader Europe ex-UK. Overall, the UK remains the preeminent financial hub in Europe, driving a plurality of deal value. The shift away from the UK will be gradual, but it seems it is already underway unless the Brexit process is reversed or the EU grants the UK a sweetheart deal, which seems unlikely.

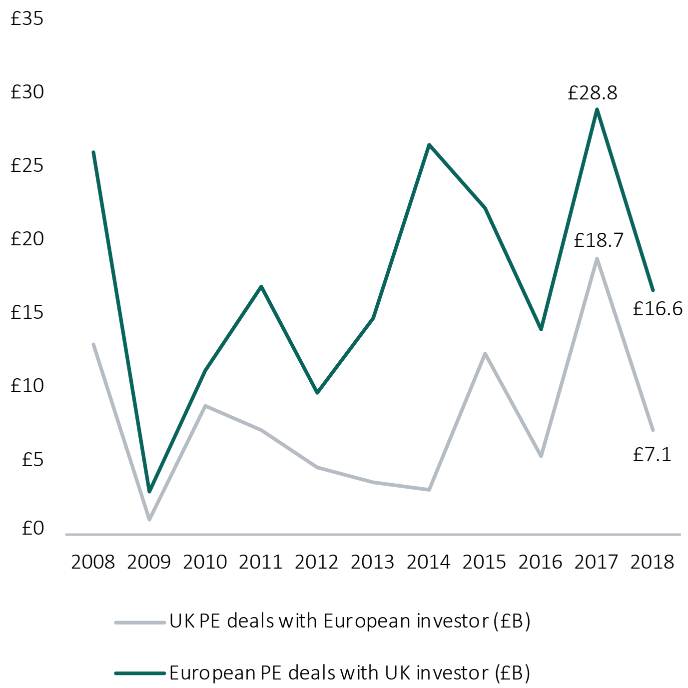
In total, Brexit seems to be a lose-lose situation, at least from a financial markets perspective. Many finance jobs are flooding outside out of London, yet many believe the even larger risk is the potential jobs that would have been created in the UK but will now be created elsewhere. Any ramifications are likely to have spillover effects in continental Europe, because more capital flows from the UK to the rest of Europe than the other way around. In fact, Europe has a $90 billion annual trade deficit with the UK. Moreover, UK investors invested in £16.6 billion (€18.8 billion) worth of PE deals in Europe in 2018 against the £7.1 billion (€8.0 billion) that European investors closed in the UK. With many of the major European economies looking fragile, including Germany, a hard Brexit may be enough to throw the whole region into recession. We will have to watch the data and Brexit process closely in 2019 and beyond.

UK PE deal activity



Source: PitchBook

European (non-UK) and UK PE deals (£) with outside investor participation



Source: PitchBook

ACG: European PE's resolve is as strong as ever

According to PitchBook's 3Q report, 2018 was on pace to be one of the best performing years for European deal activity in the last decade. Do you expect 2019 to mirror 2018, or has the golden age of PE ended?

Titus Schurink: The large amount of PE dry powder will ensure investments continue. However, global factors make M&A activity predictions difficult. Will the American trade conflict with China resolve itself or worsen? What impact will Brexit have, if at all? How large of an impact will the US government shutdown have on economic performance? Even with so much uncertainty, I expect we won't see a big decline in deal activity compared with last year.

Stewart Licudi: PE has backed a lot of high-quality businesses, which tends to be a big driver for M&A. If you look at the maturity of UK companies, you likely won't see the next wave of exits until 2020. We might see a slight drop in volume, but I don't expect activity to shift dramatically unless something significant happens in the global economy.

TS: The end of a PE golden age is not near. If anything, PE is becoming more mature and sophisticated. Maybe there will be less fundraising, but that's cyclical, too. For instance, in 2009-2010, HPE raised €155 million for our first fund with a first-time team.

SL: I've been in PE since 1996, and even then, I heard the demise of PE was near. What does "golden age" mean? Some PE professionals would argue it is a golden time for sellers but not buyers, so it is tough to define what that actually means! PE and M&A are healthy.

It's been written that the right deal happened because two people were in the right place at the right time. Has technology made personal meetings and acquaintances obsolete in the dealmaking process?

TS: When people meet face-to-face and like each other, the deal closes much easier. You can't undervalue the importance of knowing and trusting someone with whom you are working. That relationship doesn't end when the deal closes.

SL: Technology advances have streamlined processes and improved communication, but it's no substitute for meeting people face-to-face. With so many factors of uncertainty, from the micro environment to the global economy, the best way to navigate those challenges and figure out what's really happening in the market is to spend time with a group of people in the same business as you. Even if you don't walk away with a deal, you leave with knowledge to help you be more thoughtful and productive in your M&A work.

Titus Schurink

Titus Schurink is the chief financial officer of Amsterdam-based PE firm HPE Growth Capital. Since 2008, he has managed HPE's back-office activities, portfolio and fund controlling, compliance and reporting. He also supports the CFOs at HPE's portfolio companies. Schurink leads the Association of Corporate Growth's European Task Force, served as the 2015 chairman of EuroGrowth, ACG's annual dealmaking meeting in Europe, is an active board member for ACG's Holland chapter, and a former global board of directors member.

Stewart Licudi

Stewart Licudi is a managing director and head of European financial sponsors coverage for William Blair based in the firm's London office. An investment banker with the firm since 2006, Licudi works on a variety of assignments involving M&A, private placements and public offerings. William Blair's focus in Europe is on cross-border, sell-side transactions. Licudi has worked on deals in more than 20 countries. He is the former chairman of EuroGrowth and the ACG UK chapter.

The UK is scheduled to leave the EU on March 29. What impact do you expect Brexit will have on M&A?

SL: I don't think anyone, including the government, can tell you what will happen. Uncertainty is never great for the market. However, PE is great at anticipating situations and being proactive. Brexit is not a surprise move. If you talk to UK PE firms, they've been working with their portfolio companies and LPs since talk of Brexit began.

TS: I expect Brexit will affect European PE briefly. Then, as always, M&A and PE communities will move on, identify opportunities and continue to invest. PE is prepared and resilient.

As large European economies face threats—Brexit in the UK, a potential recession for Italy, slowing growth in Germany—where are the safe havens for investors?

TS: Europe in general is a safe haven, and the US will always be as well. Compared to emerging markets, Northern Europe-- specifically the Nordics--is a safe haven. Outside of slowing growth in Germany and a recession in Italy, plenty of good businesses to target for investment remain.

SL: PE has become much better at not investing in volatile industries and unstable regions. A PE investor won't tell me that Spain is safe and the UK is not. Instead an investor looks at the cycle of an industry sector, its resiliency—specifically its ability to weather an inevitable downturn.

Investors projected growth areas for green companies in 2019, including socially conscious and sustainable companies. Do you agree?

SL: Nobody wants to buy a business damaging the environment or using sweatshop labor. Impact investment funds remain small but important, and it is great to see people paying attention. PE, like other responsible companies, is already considering social consciousness and sustainability carefully when they make investment decisions.

TS: We read a lot about environmentally and socially conscious investing, but it remains a small part of the market and new for investors. It's easy to discuss but less easy to implement, because like other parts of operation, these practices require an investment of revenue.

Chinese buyers have shown an increased interest in the European market. To what extent is this affecting competition and pricing?

TS: The influx of Chinese buyers continues to have an impact on competition and pricing, although that doesn't mean they're willing to outbid other buyers every time. Meanwhile, Chinese investors and acquirers can purchase European concerns easier than the reverse. Entering China remains difficult, and many European investors believe barriers put them at a disadvantage relative to their Chinese counterparts.

SL: Dealing with Chinese buyers is not straightforward, and they're not interested in every segment. Some still struggle with the M&A process, although many are now better equipped to participate. There is still a question about some buyers' ability to get money out of the country. You might have the deal, but if you can't pay for it, it's not going to happen. China is a great place to look for buyers, and we see them competing for and winning more and more deals.

New European financial regulations implemented last year were expected to affect PE deal flow, along with firms' back-office operations. How significant were they?

TS: Regulations such as MiFID II and GDPR have affected middle-market firms, though they they've had a greater impact on larger organizations. As firms grow, so do layers of financial regulations that apply to them. As our firm approaches €500 million in AUM, HPE faces additional compliance regulations, including those tied to the Alternative Investment Fund Management Directive from the EU, which applies to funds of HPE's size and larger. We must now comply with stricter regulations related to capital and liquidity requirements, risk management and more.

SL: For William Blair, more rules mean enhanced compliance, and we've hired more people to ensure we're meeting and exceeding new requirements. M&A in Europe continues to evolve, and you want to believe that the regulations will improve things. So, you do the right thing.

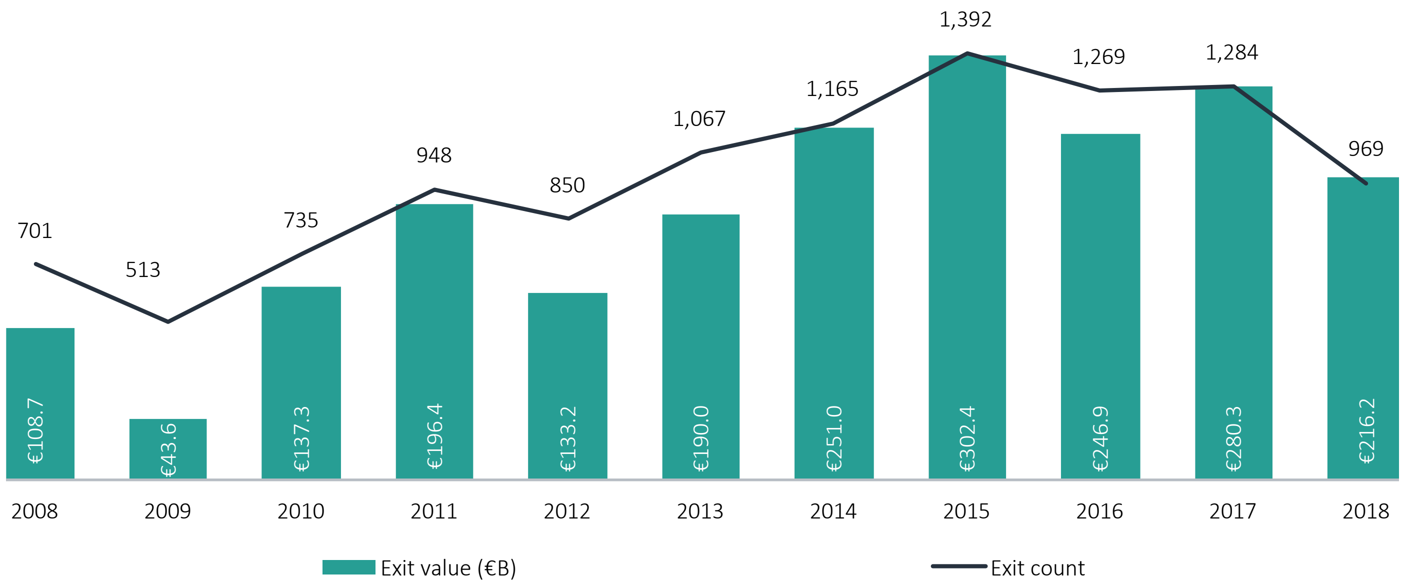
Any parting words?

SL: European PE market is in good health and remains an exciting, vibrant place to work. PE continues to become more sophisticated, from the types of companies' firms target to what they do after the deal closes. The days of buying a company, paying off some of its debt and hoping someone will one day pay more for it are gone.

TS: The dry powder is there, so investments will be made. The M&A market is in good shape and coping with new regulations. Inevitably, a downturn will come and affect prices and deal count. But in the long run, PE in Europe will continue to mature and remain resilient.

Exits

European PE exit activity

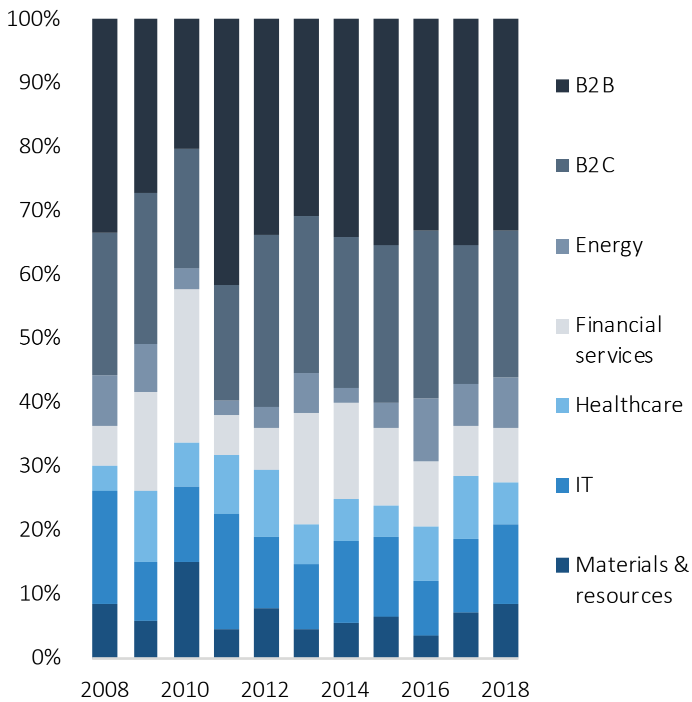


Source: PitchBook

European PE exit activity continued its downward slide in 2018. Overall, PE firms exited €216.2 billion across 969 transactions—YoY declines of 22.9% and 24.5%, respectively. This is the lowest exit value in five years. Although exit activity was down, the median exit size rose to €153.5 million, cresting €150 million for the first time. Much of this jump can be attributed to the largest source of exits, SBOs, which jumped to €216.2 million (compared with €178.8 million in 2017); the median size of corporate acquisitions rose more slowly to €113.7 million (compared with €108.7 million in 2017). PE exits may experience further pressure in 2019 as the European economy appears to be slowing, which often deflates pricing. PE firms may extend holding periods and forego sales to wait for a more stable economic environment.

Exit activity was especially subdued in the IT sector, despite unabated growth on the deal side. 2018 saw the sector record six exits above €1 billion. However, the sector accounted for just 12.5% of overall exit value, down from the 17.4% the sector achieved in 2008. One reason is that many IT companies are sourced by non-tech firms as bolt-on transactions meant to, for instance, improve operational efficiencies. In 2018, 26.3% of all IT bolt-ons were completed by non-IT companies. As IT continues to account for a rising portion of deals, the exit data ought to eventually reflect this, rising in the coming years.

European PE exits (€) by sector



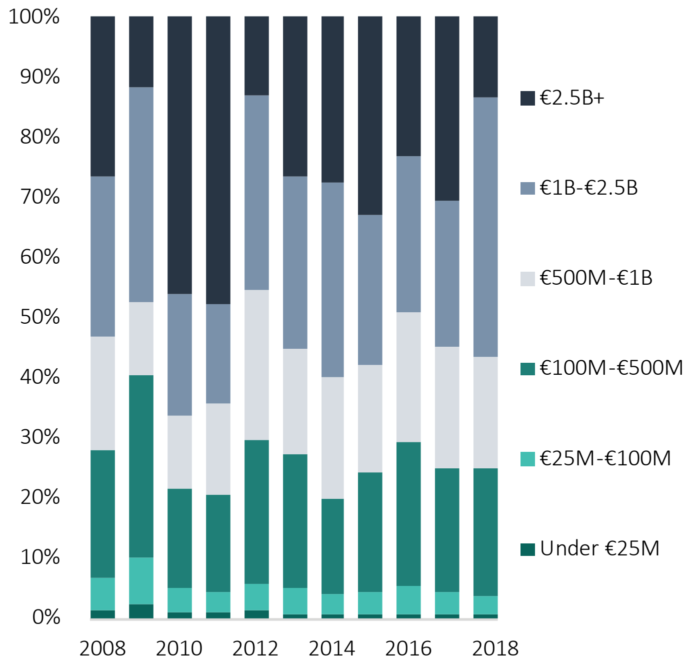
Source: PitchBook

Much of the decline in exit value can be attributed to the lack of exits above €2.5 billion. This size bucket accounted for just 13.3% of exit value on the year, a steep decline from the 30.4% in 2017. Indeed, there were just five exits above €2.5 billion in 2018. This was less than half of the 11 seen in 2017 and the lowest figure since there were just three exits of this size in 2012. Nonetheless, there were several substantial exits in the year. Perhaps the most noteworthy was the IPO of Aston Martin—the brand behind so many infamous James Bond cars. The company—which had been backed by multiple investors, including Kuwait-based ADEEM Investment and Wealth Management Company and Tejara Capital—went public in the fourth quarter at a €3.8 billion (£3.3 billion) valuation and raised €1.3 billion (£1.1 billion). The Aston Martin IPO also represents the only IPO with a valuation over €2.5 billion.

Another sizable exit was Cinven's €2.6 billion sale of CeramTec to a consortium led by BC Partners. The buyout is the third leveraged buyout (LBO) in CeramTec's history. The sale inks a jump in EV of over €1 billion since its €1.5 billion buyout in 2013, though some of the increase may be thanks to the 2015 bolt-on acquisition of US-based competitor DAI Ceramics. The exit is also another example of a non-European PE firm participating in a large European PE deal. Despite proportional exit value above €2.5 billion dropping in 2018, the proportion of exit value above €1 billion grew in 2018—accounting for 56.6% of exit value compared with 55.0% the year prior.

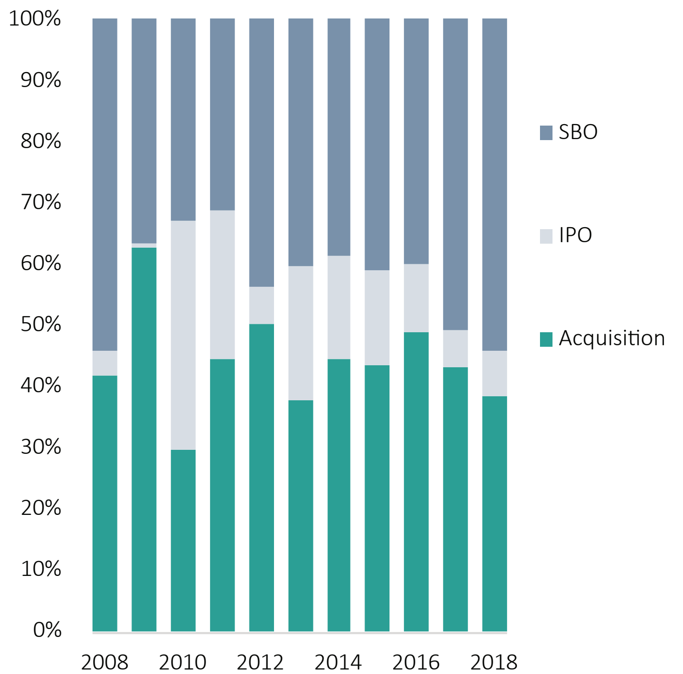
While large exits are occurring with increased frequency, PE firms are relying on IPOs less and less to exit companies. 2018 saw just 44 companies go public at a total exit value of €16.0 billion, the lowest figures since 2012. The drop off, however, is understandable given the poor performance of public equity indices in 2018. Major indices, including the STOXX 600, DAX, and CAC were negative on the year, reflecting more pessimistic economic sentiment. SBOs have stepped up to offset the activity decline seen in IPOs. In 2018, SBOs accounted for over half (51.8%) of European PE exit count, marking the first time SBOs comprised the majority. Interestingly, the same thing happened for the first time in the US market in 2018 as well. One major difference, though, is that SBOs also accounted for the majority of exit value in Europe, whereas corporate acquisition took the majority in the US market. This is one area we will be watching closely throughout 2019, because a rise in financing costs—and a continued weak showing in public equity markets—may constrain the largest sources of exits.

European PE exits (€) by size



Source: PitchBook

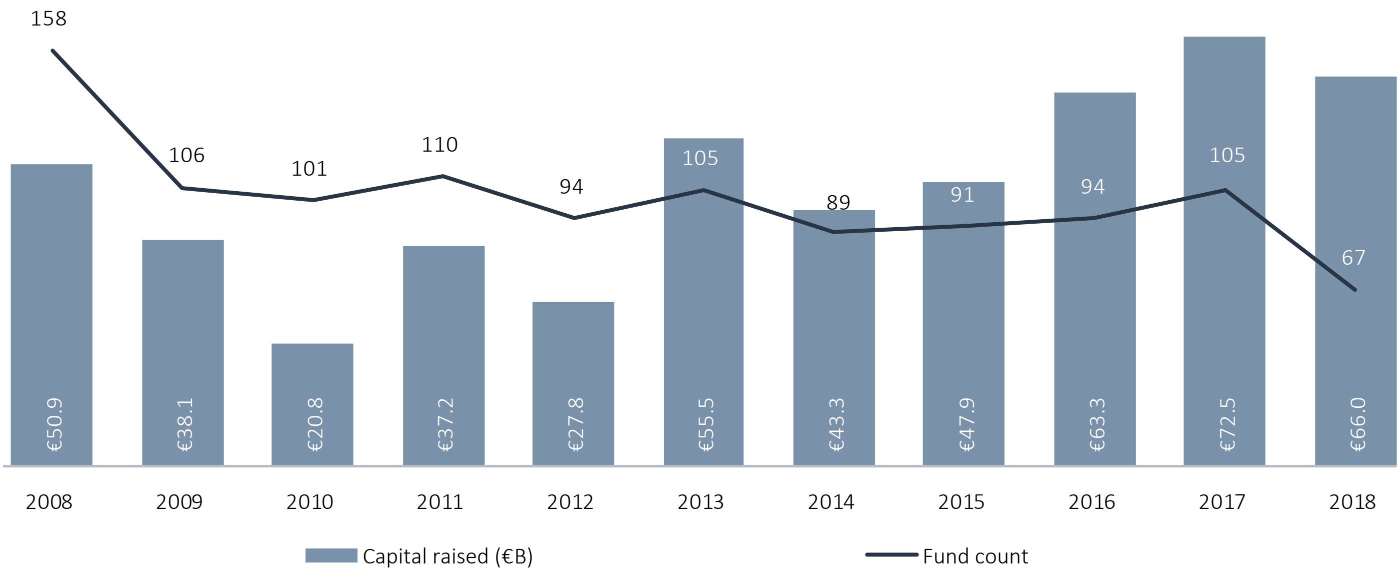
European PE exits (€) by type



Source: PitchBook

Fundraising

European PE fundraising activity



Source: PitchBook

Fundraising activity was varied in 2018. Overall, European PE raised €66.0 billion across 67 funds—YoY decreases of 9.0% and 36.2% respectively. Despite the massive decline in the number of funds raised, the drop in total capital raised was far less severe thanks to an enormous jump in average fund size. In 2018, the average buyout fund rose 35.5% to €1.1 billion. This also marks the first year in which the average buyout size eclipsed €1 billion. There were also far fewer small funds that closed in 2018, with 43 funds under €500 million closing compared with 70 the year prior. On the upper end, 2018 recorded four closed mega-funds (€5 billion+), more than any other year, though much of the activity was front-loaded, with three of the four closing in the first quarter.

GPs are raising larger funds to compete in a market where everything seems to be growing from year to year. Not only are buyouts growing in size—necessitating larger funds to appropriately allocate capital—but traditional GPs are competing for deals with nontraditional GPs, including sovereign wealth funds and family offices. In addition to acting as LPs and investing in PE funds, these nontraditional entities are growing increasingly sophisticated, sourcing and completing direct deals on their own. Moreover, hedge funds are looking to enter the PE space, which may further complicate the fundraising picture. If these entities become adept enough at executing direct deals or co-investing on larger deals, fundraising may be more difficult in future years for traditional PE firms.

Average European PE fund sizes (€M)

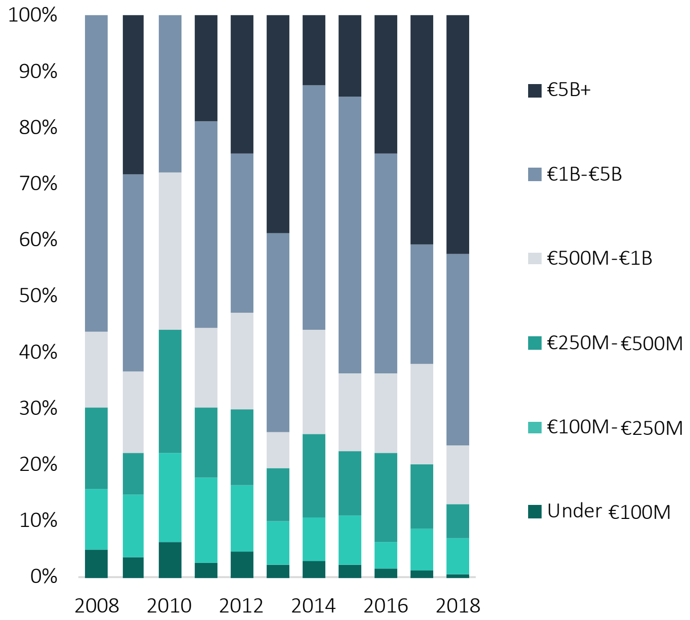
Source: PitchBook

The proportion of capital raised by mega-funds set a record in 2018, accounting for 42.2%—surpassing the 40.7% achieved in 2017. The largest vehicle raised was EQT's eighth flagship fund, the €10.8 billion EQT VIII. The Swedish investor is no stranger to mega-funds, having closed three prior funds above the €5 billion mark. However, the €3 billion increase over the previous flagship fund was noteworthy as the last three funds were incremental jumps of €1 billion. Three other PE managers—BC Partners, PAI Partners, and Triton—raised mega-funds during the year as well. PAI Partners' Fund VI, which closed at €5.1 billion, marks the firm's first true fund over €5 billion. After closing a vehicle in 2008 at €5.4 billion, the firm decided to reduce the commitments by half and ultimately closed it at €2.7 billion. With the continued surge upward in fund sizes, we expect European mega-fund closes to become more common going forward.

All these mega-funds share a common strategy: buyouts. This underscores a broader shift favoring buyouts above all other strategies within the European PE market. In 2018, buyout funds accounted for 76.1% of funds raised. At the beginning of the decade, in 2010, buyouts accounted for just 58.4% of funds raised with growth and mezzanine making up the remainder. This shift away from growth has been particularly interesting because US PE showed an opposite tendency, with this strategy making up a higher proportion of fundraising capital in recent years.

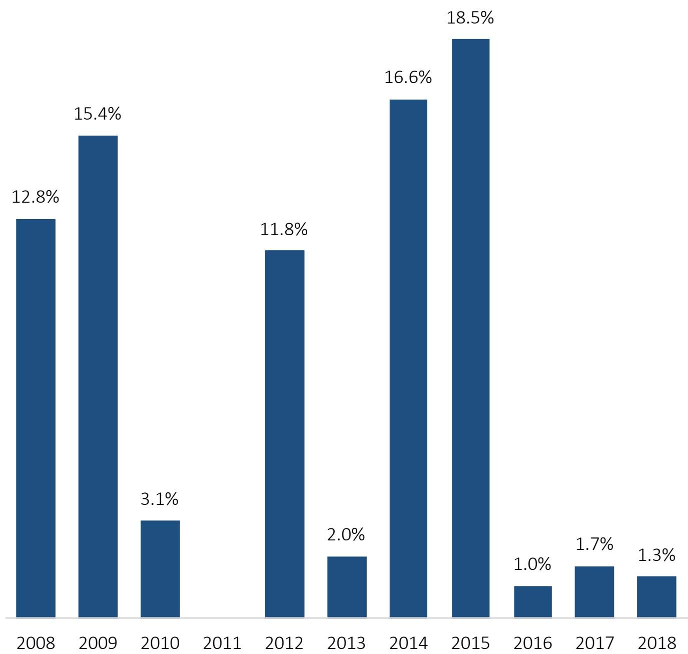
Another trend we have been watching is the lumpiness of non-European PE firms raising European PE funds. The largest managers, such as Bain and KKR, have been active in Europe for over a decade, raising multiple Europe-focused funds. In 2014 and 2015—which saw Bain, KKR, and Carlyle raise multi-billion-dollar funds focused on Europe—foreign GPs raised over 15% of the total capital secured for the region. Going the other way, TPG—one of the first major US PE firms in the region—seems to be restricting buyout activity in Europe, though they are still growing other strategies in the region.[3] However, Europe seems to present opportunities for bulge bracket, North American PE firms attempting to expand offerings and satiate LP demand. EU GDP is roughly the same as the US, yet dry powder in Europe is sitting at less than half that of the US. In the years ahead, as additional PE firms ascend into the upper echelon of GPs, we expect to see the more firms look to Europe as an area for additional fundraising so long as performance is commensurate with other geographies.

European PE fundraising (€) by size



Source: PitchBook

Proportion of European PE fundraising (€) by GPs headquartered outside of Europe



Source: PitchBook

3: "TPG hits lull in Europe after deals sour," Financial Times, Javier Espinoza, October 31, 2018