ACCESS CAPITAL PARTNERS

PRIVATE ASSETS IN EUROPE

MARKET TRENDS

IN THE EUROPEAN

SMALL & MID-MARKET

BUY-OUT

THIRD QUARTER 2017

1. Overview

Overviewing the latest forecasts, the European economy appears to be on an improving trend. GDP figures show an average growth rate of 2.3% (up from 1.9% in spring), marking a fifth year of recovery (source: European Commission). Economic sentiment rose to the highest level in a decade in September, while the unemployment rate stood at a multi-year low and industrial production soared. Operating against a backdrop of Brexit negotiations for the remainder of 2017 and throughout 2018, the economy in the UK is however expected to soften. Uncertainty as well as a weaker currency and the consequent imported inflation are projected to undermine investment.

Despite an overheated market, the buy-out activity remains dynamic and 2017 is expected to be another strong year for the European buy-out space. With limited partners recycling gains into the asset class, fundraising continued unabated. Low interest rates, creating a receptive borrowing environment, combined to the amount of available equity and increased competition contributed to soar prices at record high levels. Latest data show the European average multiple exceeding pre-crisis levels (around 10.2x for the overall buy-out market). Closing promising deals at prices that will generate satisfactory returns remain the main challenge for managers.

2. Investment activity

Despite losing some steam, the European buy-out market had a robust quarter. The UK has proved so far resistant to the uncertainty brought on by the Brexit process, dispelling the alarming forecasts. The UK saw a return to pre-Brexit form with aggregate deal value jumping to €13.7m from €6.4m marking Q3 2017 as the strongest since the financial crisis. Recent forecasts assuming that household spending is projected to ease, as real wage growth is suffering from a higher inflation and a weaker labor market, may impact the buy-out investment activity in the medium term. Valuations of portfolio companies, notably in the consumer-related sector, are expected to be negatively impacted throughout 2018.

The DACH region performed well standing just behind the UK with €9.6m of aggregate deal value while France, Benelux and the Nordics countries witnessed a sharp fall. Small buy-outs (Enterprise Value < €100m) accounting for about 87% of market volumes, continue to drive investment volumes.

In that context, Access' GPs have demonstrated a sustained capital deployment pace which remained at a healthy level with 17 deals completed over Q3 2017 vs. 15 compared to Q2 2017. This amounted to 2.5 deals per active GP. Third quarter deals were completed at an average Enterprise Value (EV) of €80m. In line with Access' focus, the average EV/EBITDA multiple at which companies were acquired stands at 7.7x for an average debt multiple of 2.7x Ebitda. This compares favourably with the small segment market average (Enterprise value <€250m) of 8.8x Ebitda. Abundant liquidity and capital overhang fuel competition between buyers and contributes to the increase in the price of private companies. Despite rising valuations at entry, the conservative entry metrics displayed by Access' new portfolio companies demonstrate the defensive investment choice of Access. The smaller buy-out segment, highlighted for several years as the area delivering strong returns and showing overperformance, has been driven by the high number of investment opportunities with significant operational improvement and profitable growth opportunities. Companies in Access' portfolios exhibit sound financial and economic health, significantly outperforming the European economy.

The deal making activity was boosted by the UK and the DACH region which accounted for c.55% of the investment volumes vs c.45% for the combined pool of France, the Nordic region and Benelux. Italy came last with one investment. This deal making breakdown reflects the Access portfolio diversification.

3. Exit activity

In the midst of a buoyant debt market, and on the back of increasing levels of cash for both corporate and financial buyers, Q3 2017 was another strong quarter for liquidity in the Access portfolio. Should market conditions remain favourable it is likely that the fervent exit activity will continue until the end of the year. Exit activity in Q3 2017 has increased vs. Q2 2017. Access' portfolios benefited from the strong performances of the 23 exits recorded in Q3 2017 which generated an average gross cost multiple of 3.4x, comparing favourably to the 16 Q2 exits displaying an average gross cost multiple of 2.7x. Overall, companies tend to be sold above their latest reported fair market value, reflecting the difficulty for fund managers to estimate valuation multiples in line with the current market conditions.

Appetite from corporate buyers leads trade sale to be the preferred exit route in H1 2017 in Europe. However, for the second consecutive quarter, Access recorded c. 50% of exits completed via secondary buy-outs whereby companies are acquired by larger private equity funds. The increasing proportion of financial buyers signals an overheating environment, particularly in the upper mid-market and large buy-out segment.

In terms of geography, the UK, DACH region and France represent c. 70% of the exits completed over the period whilst the Nordic region, Benelux and Southern countries account for the remaining c.30%.

4. Secondary activity

As secondary market volume is expected to reach $40bn in 2017, Access has seen a marked increase in relevant secondary deal flow, with significantly more European portfolios of small and mid-market buyout funds coming to market than in the previous years. However, as fundraising for secondary funds continues to be strong, with c.$30bn raised in 2017 YTD globally - bringing the amount of dry powder chasing deals at nearly $100bn -, the market remains very competitive across all strategies (sources Preqin, Greenhill Cogent). In 2017, the top pricing for mid-market buy-out funds was on average a 4% discount to net asset value, up from a 6% discount in 2016 (source Triago).

Fund of funds managers and other discretionary vendors have continued to take advantage of the high pricing environment to actively manage their portfolios, either to de-risk and accelerate liquidity or to dispose of tail-end or non-core assets. In addition, this activity has been supplemented by a number of GP-led opportunities.

Access continues to take a disciplined approach to investment and has focused on secondary direct opportunities. In 2017, Access actively sourced and analysed 3 transactions and deployed €238m across 6 secondary transactions, 3 of which were direct deals, at an average pricing of 1% premium on record date net asset value.

ABOUT ACCESS CAPITAL PARTNERS

Established in December 1998, Access Capital Partners (“Access”) is an independent private assets manager investing in the key economies of Western Europe, active in European private equity, private debt and infrastructure, with offices in six European countries and assets under management of €7.7 billion from a diversified base of international institutional investors. The firm’s products and services encompass primary fund investments and secondary transactions as well as direct co-investments.

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