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Mid-cap valuations pick up in Q4 2012

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26 Feb 2013, Gregoire Gille, unquote

Following a sustained drop for most of 2012, pricing improved slightly in the fourth quarter for lower mid-cap private equity-backed transactions, defined in Argos Soditic's Mid-Market Index as deals valued in the €15-150m range: buyout houses paid a median entry multiple of 7.1x EBITDA. This is up from 6.6x in Q2 and Q3 – the lowest multiple seen since Q2 2010.

This uptick – no doubt a welcome sight for GPs in exit mode – came on the back of a comparatively strong fourth quarter in terms of European M&A activity, both from private equity and trade players. But Argos Soditic partner Karel Kroupa warns that this remains a small consolation prize after a particularly lacklustre 2012: "Although Q4 marked a noticeable improvement compared to the previous quarter, both lower mid-cap activity levels and valuations remain historically low when looking at the whole of 2012. A large part of the transactions completed in Q4 had been on the market for a long time and several processes dragged on, on the back of disappointing preliminary results and (in the case of France) fiscal uncertainty."

Argos president Gilles Mougenot (*pictured*) also explains that most private equity deals that made it through to the finish line involved highly sought-after assets: "The flight to quality that was apparent in the second and third quarters – with sale processes for the less attractive assets halted altogether – should continue well into 2013." He adds: "Only the best businesses will change hands, and we are notably expecting to see a strong bifurcation between assets depending on which international markets they are addressing."

Trade players are comparatively less selective, which might explain why the median entry multiple paid by such buyers remained stable at 6.3x EBITDA in Q4. Businesses bought by GPs display a 16.9% median EBITDA margin and 7.5% median turnover growth in the index, compared to 11.7% and 3% respectively for companies acquired by trade players.

Bargain hunting

But Mougenot warns that despite their apparent unwillingness to spend as much as their private equity counterparts, it remains key for GPs in exit mode to include corporate buyers in auction processes: "Trying to sell a business that isn't particularly attractive to at least several corporate buyers is tough for vendors hoping to maximise their returns. Potential private equity buyers will be less prone to put in higher bids and this will mechanically have an impact on valuations, which more often than not will not come with the premium expected by the vendor in the first place."

Mougenot remains confident in terms of private equity dealflow going forward, but is still cautious as to whether valuations will pick up significantly: "A few assets were taken off the market altogether from September onwards, when these uncertainties became too much of an obstacle," he says. "We are expecting several processes to restart in the coming weeks but this will be a challenge for vendors: it is very hard to achieve the sort of valuation multiples expected the first time around, as private equity players tend to be very sceptical towards these assets when they come back to the market the second time."

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