

Fourth quarter 2010 – optimism flies in the face of a dip in M&A activity

In its regular quarterly commentary on UK private equity investment activity, Corbett Keeling gives a practitioner's view of trends in the number, value and financing of deals and finds that, even though the M&A recovery appears to have faltered, optimism is riding high.

Last time we reported on private equity activity – at the end of the third quarter of 2010 – statistics from *unquote*™ revealed increasing numbers and values of deals. The question we asked then was: would that last, or was it just a temporary phenomenon, caused by the coincidence of a handful of larger deals?

Well, judging by the statistics, it looks increasingly like the latter, with the most recent results showing a downturn in activity in the fourth quarter. Yet these statistics are in stark contrast to the prevailing optimism in the marketplace.

So let's look at the facts, as usual starting with larger UK buyouts of more than €150m enterprise value, then UK buyouts of less than €150m, and finally early-stage and expansion capital deals.

- The aggregate value of larger UK buyouts (€150m or above) in the quarter finished at just above €2bn. Indeed, there were only three larger UK buyouts – the lowest quarterly amount in 2010. So, although the year as a whole was encouraging for deal-makers – and an enormous improvement on 2009 – it appears to have been considerably harder to get deals closed in the last three months than the preceding nine.
- The picture for smaller UK buyouts (below €150m) was similar, with just 12 deals for a total of €340m – a record-breakingly weak fourth quarter on both counts. Again, though,

the picture for the whole of 2010 is much more encouraging, with aggregate deal values more than double the 2009 figure and volumes also well ahead.

- Last time we reported, there was some solace for deal-makers from the statistics for UK early-stage and expansion capital deals. This time, there is none: at just 28 deals and total funding of €320m in the fourth quarter, the result was exceedingly weak. As with buyouts, however, the year as a whole paints a more favourable picture for those hoping to get deals done, with both deal volumes and values coming in at around the average level for the preceding 11 years.

The key question is: what has caused the recent slowdown? When we at Corbett Keeling noticed that the City was eerily quiet in the run-up to Christmas, we put it down to the freezing weather and the consequent seizing up of public transport. But was it, in fact, a sign of an impending economic freeze?

Not so, say our other indicators.

First, the survey of deal-makers' expectations suggests that, despite the last quarter's result, optimism is increasing.

- The proportion of survey respondents expecting a rise in smaller deal activity is up from the already high level of 70% at the end of quarter three to 80% at the end of quarter four.

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- It is a similar picture for larger deals, with 70% of respondents now being optimists – ie thinking deal activity will increase – compared with 40% at the end of quarter three.
- At the same time, the market appears to think business valuations have bottomed out, with more survey respondents now expecting prices to rise than fall.

Secondly, the supply of debt funding appears to be freeing up. That is the implication of the declining proportion of all-equity funded buyouts to all buyouts, which was 20% for the second half of 2010, down from a peak of 45% 18 months ago. So the banks appear to be doing their bit to provide fuel for deal activity.

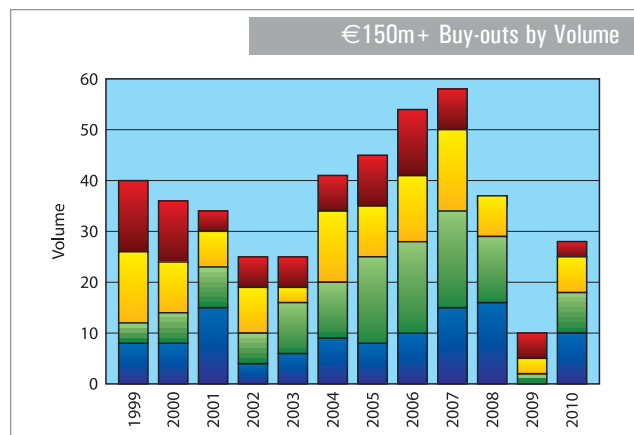
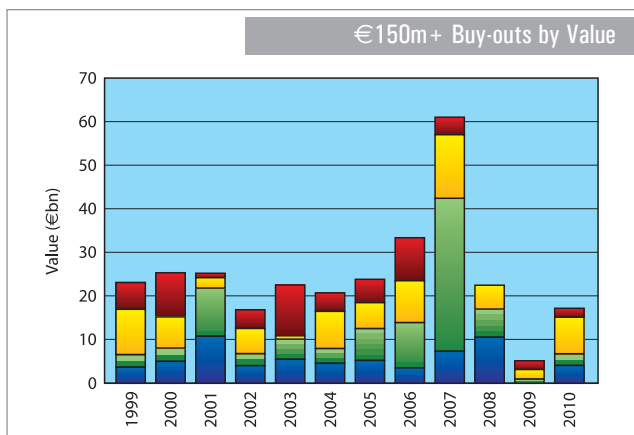
Thirdly, the chatter we hear around the market is resolutely of stronger deal pipelines. These are driven not just by economic conditions but also by the length of time that owners – be they fund managers or owner managers – have held on to assets. As time goes on, they have an increasing desire to realise value by selling to a new owner.

So our conclusion is that, during the big freeze, deal-makers didn't stop work but instead continued to nurture deals from their homes and mobile phones, even if not from their offices. As the large proportion of optimists indicates, transaction volumes and values can be expected to increase in the year ahead. Roll on 2011!



Jim Keeling,
Joint Chairman, Corbett Keeling
www.corbettkeeling.com

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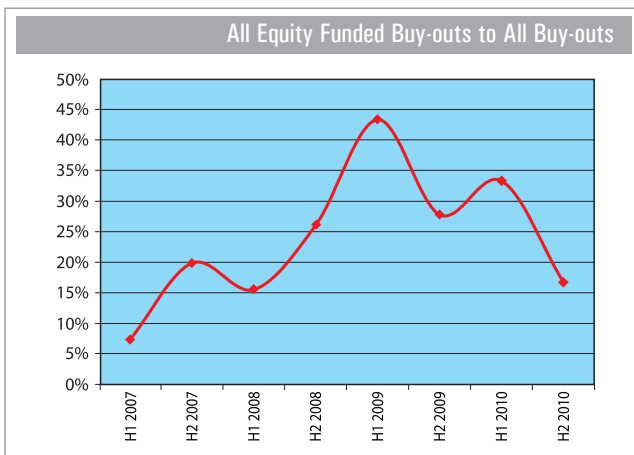
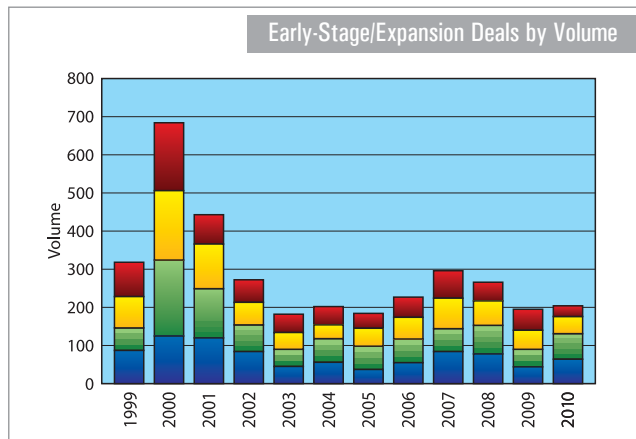
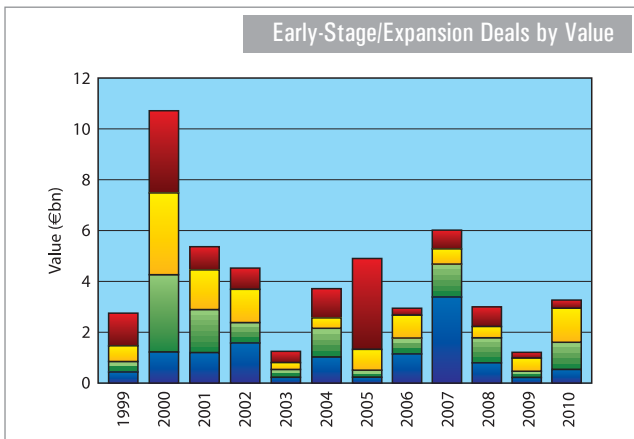
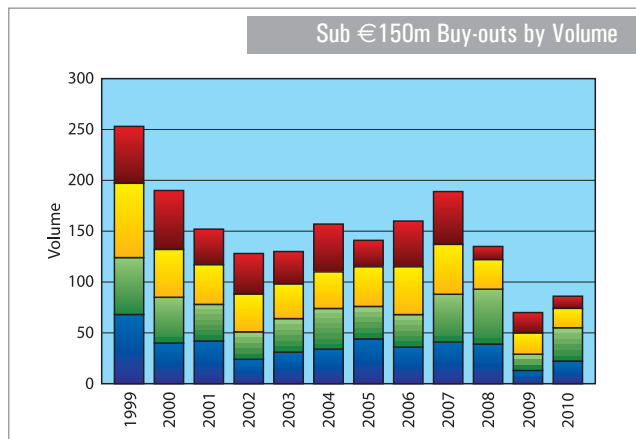
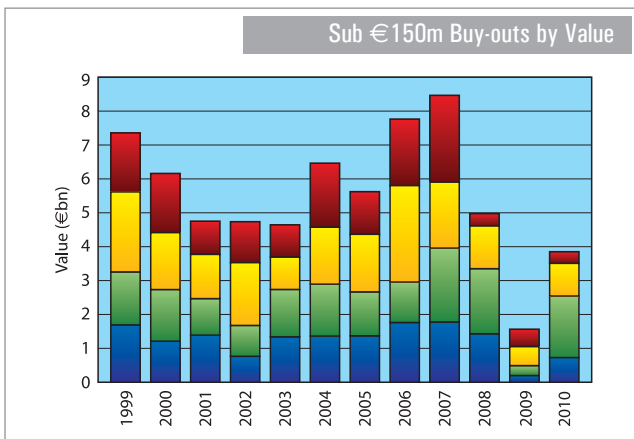


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- RAISING FUNDS FOR MANAGEMENT BUY-OUT TEAMS
- SELLING BUSINESSES

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Figures are based on all deals that were confirmed, at the time of going to press, as having an institutional private equity or mezzanine investor as a lead or syndicate partner investing in a UK-based business. Sourced from Private Equity Insight.

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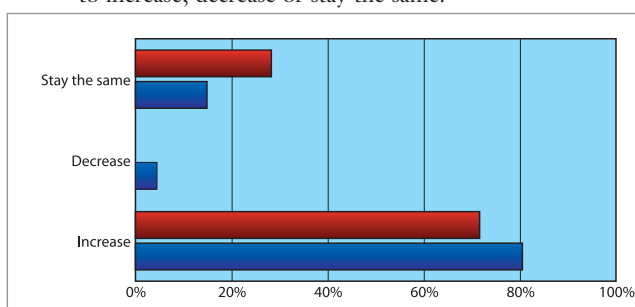
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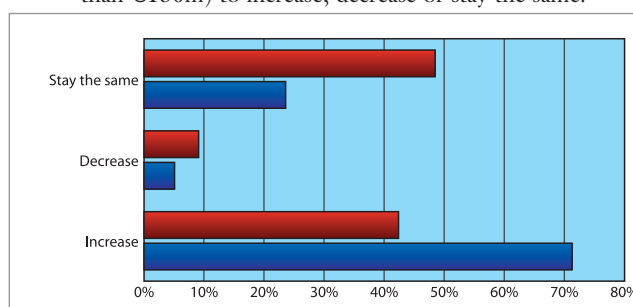
In order to produce these statistics, more than 500 key players in the UK private equity and venture capital markets were surveyed.

■ Q3 2010 predictions
■ Q4 2010 predictions

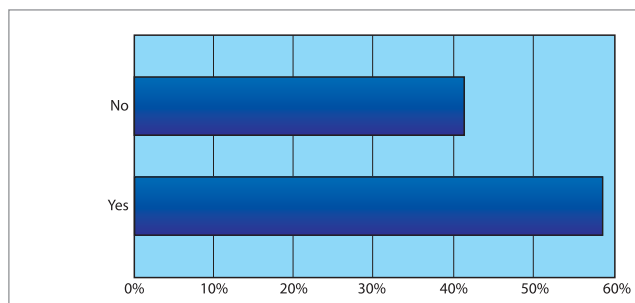
1 Over the next six months do you expect activity levels in the lower mid-market buyout segment (less than €150m) to increase, decrease or stay the same?



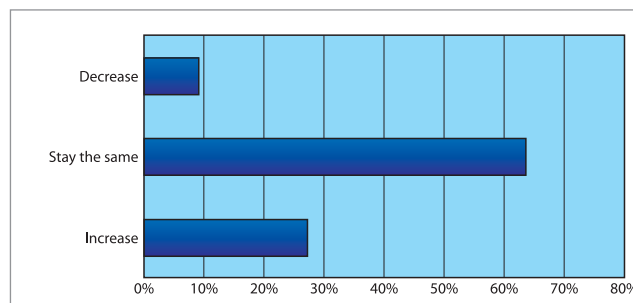
2 Over the next six months do you expect activity levels in the upper mid-market and larger buyout segment (more than €150m) to increase, decrease or stay the same?



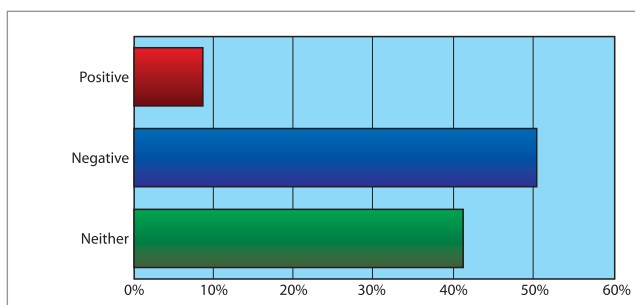
3 Is there sufficient leverage to support primary transactions at the lower end of the market?



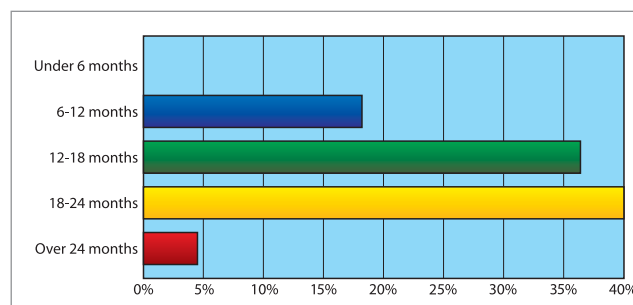
4 Do you expect overall pricing levels in 2011 to decrease, increase or stay the same?



5 What impact will government spending cuts have on private equity portfolio companies?



6 How long should GPs assume it takes to raise a new fund after the official launch?



Corbett Keeling

CORBETT KEELING 13 ST SWITHIN'S LANE LONDON EC4N 8AL UNITED KINGDOM

T: +44(0)20 7626 6266 F: +44(0)20 7626 7005 WWW.CORBETTKEELING.COM

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