

Europe's mid-sized companies offer great potential for Private Equity

Munich, April 2006 – A study of 33 leading European Mid-Market Buy-Out Funds produced by the Private Equity Consultants FHP (Fleischhauer, Hoyer & Partner) and sponsored by Access Capital Partners (European Private Equity Funds of Funds) shows increased maturity in the sector, strong deal flow and lower risks going forward compared to the large buy-out market. The study concentrated on funds targeting the majority acquisition of companies valued below the 250 million Euro threshold.

There are almost 200,000 small and mid-sized companies with more than 25 million Euro revenues in Europe. The increasing acceptance of private equity as a source of capital and liquidity among entrepreneurs, family owners and large industrial groups creates a huge potential market for European mid-market Buy-out funds. In 2005 close to 500 family owned businesses have been sold to Private Equity Funds, a 22% increase compared to 2004 (figures according to recent study of CMBOR 2005). Overall a third of all companies sold are now prior family owned businesses and represent the most important source of deal flow for Private Equity Funds in Europe.

Mature Group of Experienced Fund Managers with domestic focus

With an average of 13 years investing experience and generally investing their 3rd generation fund, the leading European mid-market fund managers surveyed are a mature group with a high level of discipline in sticking to their investment strategy as domestic buy-out generalists. About 80% of the funds surveyed have an exclusively domestic portfolio.

Relationship Driven Deal Origination

Screening on average about 160 pertinent deals p.a., over 90% of the fund managers surveyed believe that building an intensive relationship with the management and the vendors is a key differentiating factor. As a consequence, formal auctions are not as common in the mid-market segment as they are for large deals. Just 20% of the fund managers surveyed participate regularly in auctions. "The mid-market is certainly characterized by a lower level of intermediation" says Uwe Fleischhauer, Managing Partner at FHP Private Equity Consultants in Munich who also emphasises that "generation changes in family businesses will be one of the key investment drivers for the future, creating a need for close relationships with local vendors to avoid competitive bidding situations".

Value Creation

Value creation skills will continue to be the predominant driver for returns as financial engineering is becoming more and more a commodity. Mid-market funds generally take a strong majority shareholding (equity stake of 70% on average) in order to drive the transformation of under-managed companies with a focus on restoring margins and selectively pursuing external growth.

Investment opportunities

Increasing investment activity is expected for 2006 (three new deals per fund on average). Besides traditional sectors like manufacturing, there will be an increased focus on promising sectors like healthcare, services, and consumer goods. Particularly

attractive countries for mid-market deals will be Spain, Germany, and France in the next few years.

Sustainable market

Although entry valuations are generally believed to increase slightly due to increased competition, the European market potential appears deep enough to fuel a sustainable market expansion according to the respondents. Trade sales will remain the most common and preferred exit channel while secondary buy-outs should continue their progression thanks to the record fund-raising which have taken place in 2005. IPOs will remain a marginal exit channel.

Window of opportunity for investors – access becoming an issue

The next fundraising efforts of the 33 fund managers that participated in the study will be taking place mainly in 2006 and 2007 – 22 funds out of 33. They aim at maintaining relatively stable fund sizes, to avoid investment style drift: The expected fund size targeted for the next generation is on average of about € 340 million, a 20% size increase compared to the previous generation. Access to the best performing funds will therefore become an issue for limited partners as the appetite for the sector has grown exponentially among institutions. Pension funds and fund of funds (named as preferred source) are expected to be future key sources of capital for European mid-market buy-out funds.

Background information

The new study, conducted by FHP Private Equity Consultants, Munich in cooperation with Access Capital Partners is based on an empirical research with 33 European mid-market Buy-out fund managers. For the purpose of this study the mid-market segment was defined as being transactions of up to 250 million Euro of enterprise value. In terms of fund size, managers were considered whose most recent funds were of less than 1 billion Euro in commitments.

Further information, graphics and slides will be provided on request.

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