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Mid-cap valuations dragged down by trade buyers

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20 Nov 2012, Gregoire Gille, unquote

It could have been worse. Despite an alarming 47% decline volume- and value-wise for mid-cap LBO activity in Q3, the median multiple paid by buyout houses operating in the €15-150m segment remained stable at 6.6x EBITDA, the latest Argos Mid-Market Index shows. However, Argos Soditic president Gilles Mougenot warns that, given the historically small sample in the past quarter, strong disparities might be hiding behind the headline figure.

Despite the stability witnessed in Q3, the median multiple paid by LBO players took a noticeable hit in 2012. It fell by 10.8% between Q1 and Q2 – and the 6.6x EBITDA figure is similar to the one witnessed in June 2010, before mid-cap LBO valuations settled around the 7.5x mark for most of 2011.

But businesses taken over by corporates were even more affected by declining multiples in the past quarter: trade players paid a median 6.3x EBITDA according to the Index, significantly down from the 7.5x recorded in Q2.

As a result, the overall index – taking both LBO and trade players into account – fell by 18% year-on-year and now sits close to the 6.2x EBITDA median witnessed in the second half of 2009. "A number of businesses – healthy as they may be – are failing to attract the attention of strategic buyers," comments Mougenot. "For those companies that do not have a strong strategic angle to woo trade players, I wouldn't be surprised to see entry multiples drop even further in the coming months."

Mougenot also highlights the fact that mid-cap valuations are in sync with the current state of the European private equity market: "Witnessing lower valuations is not surprising given the current environment. The factors that drove rising multiples in the boom years (namely readily accessible debt and intense competition among PE houses) are largely absent in the current cycle, hence the reversal of the trend."

The silver lining here is that those investors willing to hunt long and hard for the right business might be in for a bargain. "The idea of returning to the multiples seen in the early days of the industry in continental Europe, when funds were paying 6-7 X net profit, is not ludicrous. We are currently starting to look at assets valued around the 4x EBIT mark, even though they are profitable," notes Mougenot. "Now would be the time for PE houses to go shopping, albeit cautiously and selectively."

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