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Mid-cap valuations still stuck on pre-crisis levels

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22 Feb 2012, Gregoire Gille, unquote

The median EBITDA multiple paid in European mid-cap private equity buyouts – here defined as businesses in the €15-150m range – stood at 7.5x in the second half of 2011, according to the recently released Argos Mid-Market Index. This is virtually identical to the 7.6x recorded in the much busier first half of last year, and still in line with multiples paid by GPs prior to Lehman's collapse.

The steady rise in valuations from early 2010 to mid-2011 was largely blamed on the race to invest significant amounts of dry powder quickly – one could have thought that a much tougher lending market would curb this trend. But actually the rocky environment seems to have further sparked competition and encouraged buyers to keep paying big bucks for the handful of assets available.

"We witnessed a very active first half of the year, with rather high valuations. The second semester was different, with dealflow slowing down significantly – but the market remains heavily bifurcated," explains Argos Soditic partner Karel Kroupa. "On the one hand you get complex transactions that don't attract much attention and are harder to finance – these could have driven prices down, but they simply struggle to close. On the other hand, the best assets still generate a strong appetite from buyers and lenders; these are the ones that GPs focus their efforts on and prices have therefore remained steady."

That said, PE houses are not the only buyers affected by the proverbial "flight-to-quality" syndrome. Increased activity in late-2010 and early-2011 led to LBO players paying higher multiples than trade buyers for the first time in years, according to Argos's index – the trend reverted in the second half of

2011 as multiples paid by corporates kept rising to a 7.6x median. "Trade buyers show the same selective appetite for M&A, although they tend to look for businesses that best fit their strategy and not necessarily the best performers. Given that corporates still have large amounts of cash available, they are less constrained by financing issues and are therefore willing to pay relatively high multiples for such businesses," notes Kroupa.

It remains to be seen whether multiples for mid-cap LBOs will keep hovering around pre-crisis levels in the coming months. But as far as activity levels are concerned, Kroupa echoes the currently popular view that dealflow might remain lacklustre for quite some time: "Financing is still available, but with lower leverage multiples and less friendly terms; the macroeconomic environment is not likely to improve much in 2012; and many vendors are not under intense pressure to sell. All these factors are currently converging, and make the LBO landscape hard to navigate."

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