Up in the air!?

– Evolution of main terms and economics in European PE deals

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The Panel

Panelists

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Head of the Chiomenti London Office, Luca assists clients with corporate-M&A matters, and in particular with extraordinary transactions and matters relating to company law and business contracts, with a focus on deals involving strategic-industrial investors and private equity funds, and also in relation to listed companies operating in supervised or regulated sectors.

Luca has, in particular, developed a solid experience in crossborder corporate and M&A transactions, both inbound and outbound on the Italian market, which require an integrated and multidisciplinary expertise, assisting mainly foreign clients or Italian groups with a multinational dimension.

Panelists

Nicholas Page
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Nicholas is a partner in Macfarlanes LLP’s corporate M&A practice, advising on a range of domestic and international transactions, including strategic M&A (particularly in the financial services sector), private equity, joint ventures and restructurings.

He acts for clients across a variety of industries, and has a particular focus on GP and asset manager M&A. Much of his work has a cross-border element and in 2018 he spent a year as a visiting attorney at a leading firm in New York.

Panelists

Mark D. Pflug
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Mark Pflug is a Partner in Simpson Thacher & Bartlett's mergers & acquisitions practices, where he represents both corporate and private equity clients. Mark advises on a wide variety of M&A transactions, including strategic business combinations, leveraged buyouts and other private equity sponsor-led transactions, minority investments in public and private companies, joint ventures, spin-offs and split-offs and divestitures for clients across a range of industries.

Mark has been a resident partner in the firm's New York, London and Hong Kong offices.

Mark received his J.D. from Columbia Law School in 1995, where he was a Harlan Fiske Stone Scholar. He received his B.S., high honors, from Rochester Institute of Technology in 1992.

Panelists

Lieke van der Velden
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Lieke is one of the managing partners of NautaDutilh. She combines her management tasks with her Corporate M&A practice in which she focuses on the financial sector. She advises banks, insurers and other players and investors in the financial sector on a wide variety of corporate transactions, including M&A, buyouts, portfolio transfers and minority and majority investments.

Lieke graduated from Utrecht University in 1995 and joined NautaDutilh in the same year. She became partner in 2005. Before becoming one of the firm’s managing partners in 2022, Lieke headed our global corporate/M&A team between 2017 and 2022.

Moderator

Isabella Ramsay
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Isabella Ramsay is a partner of Mannheimer Swartling, Chair of the Mergers and Acquisitions practice group in Stockholm and a member of the firm's Private Equity practice group. She serves as Vice Chair of the IBA Private Equity Subcommittee.

She works primarily with the acquisition and sale of non-listed companies for both private equity and strategic players.

Isabella graduated from University of Helsinki in 1999 and has been with Mannheimer Swartling since then. She obtained an LL.M. degree in corporate law from NYU Law School in 2003.

Topics for discussion

Up in the air!?
– Evolution of main terms and economics in European PE deals

- **General market update on PE M&A-activity and deal trends** *introduced by Mark D. Pflug and Lieke van der Velden*
- **Bridging the valuation gap and dealing with financing constraints** *introduced by Nicholas Page and Luca Frignani*
- **General Partner (GP) consolidation** *introduced by Mark D. Pflug and Nicholas Page*
- **Developments in management packages** *introduced by Lieke van der Velden and Luca Frignani*

General market update and deal trends

European PE Market Update – 2023 Review

- Deal value down significantly (over 25%) but deal count held steady to slightly up (low single digit %)
  - Resilience despite macro headwinds
  - Strength / importance of middle market

- Significant share of deals were add-on deals (approx. 55% by count), highest in recent years
  - In challenging environments, PE focus on portfolio management

- IT/Tech, Financial Services and Healthcare sectors continue to grow in deal activity
  - Continuing boom in Tech-centric transactions continues unabated
  - Consolidation in Financial Services spurred by Silicon Valley Bank and Credit Suisse crises, while Asset Management (including in the PE sector) consolidation is burgeoning trend
  - Healthcare sector continues to attract capital across the capital structure from mega Pharma deals to provider/services/healthcare tech deals, to growth/venture capital investments to innovative collaboration structures
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- Regionally:
  - UK/Ireland continues to lead (30% by value), followed by
  - France/Benelux (23%)
  - Germany/Austria/Switzerland (12%)

European PE Market Update – 2024 Outlook

- Deal activity expected to pick up, potentially substantially and increasingly as the year moves forward
  - Pros: Interest rate stability; inflation calming; massive PE dry powder (over USD 1 trillion); challenging fundraising broadly speaking fueling need for both exits and new deals; refinancing risk leading to exits and other solutions
  - Cons: Geopolitical issues (Ukraine, Gaza, Middle East); high energy costs; US election uncertainty

- Return of large deals
  - Large, blue chip PE funds raised the vast majority of new funds (54% of capital raised by 5 PE funds)
  - Increasing need to deploy capital (i.e., the “sideline effect”)
  - Valuation gap finally narrowing

- Continued P2P activity
  - 2023 saw significant P2P activity (especially in the UK, which accounted for approx. 50%), which is likely to continue as public company valuations continue to be compressed

- Debt financing markets strengthen
  - Bank financing (syndicated lending) to rebound
  - Private credit markets to expand

European PE Market Update – Deal trends

- Buyers increasingly selective / less risk appetite
  - business plan quality assurance
  - affecting risk appetite: stress testing
  - avoidance of auctions or deals with significant strategic interest

- Deal failures
  - significant number of busted auctions / broken deals / early terminations, largely caused by lower risk appetite and valuation gap
  - this trend may slow or abate in 2024, depending on factors previously discussed

- Sell-side considerations
  - Sponsors focusing on boosting EBITDA of portfolio companies to achieve better exit prices
  - Organic: old-fashioned operational improvements
  - Inorganic: add-on deals

- Secondary PE transactions
  - GP led transactions vs traditional LP stakes
  - Continuation funds

- Bridging valuation gaps
  - earn outs / earn ins
  - rollover equity investments
  - vendor loans

Bridging the gaps

Dealing with valuation gaps and financing constraints

- Usual suspects
  - earn-outs
  - vendor financing/deferred consideration
- Sponsor rollovers increasingly common
  - same fund
  - fund-to-fund
  - continuation funds
- Minority sales also prevalent
- Fewer auctions and more bilateral processes

General Partner consolidation

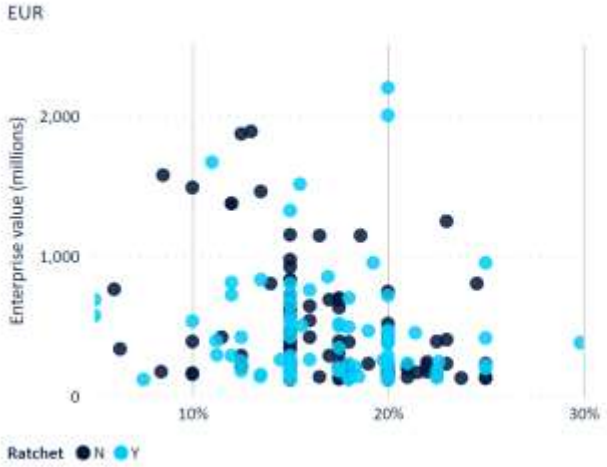
GP consolidation

- Types of transaction
- Drivers
- Trends in deal structuring

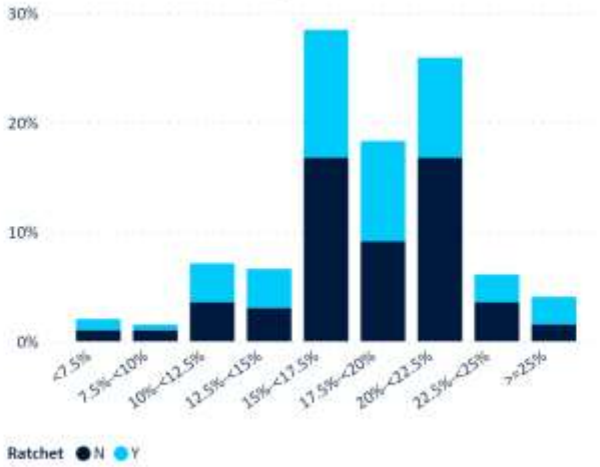
Developments in MIP packages

Illustrative benchmarking data (€100m to €2bn enterprise value)

MIP EQUITY % TO ENTERPRISE VALUE



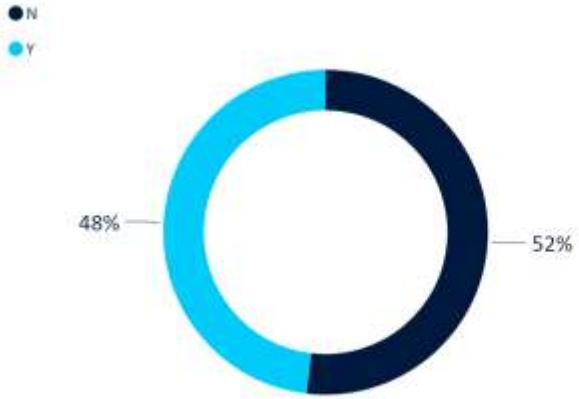
DISTRIBUTION OF MIP EQUITY %



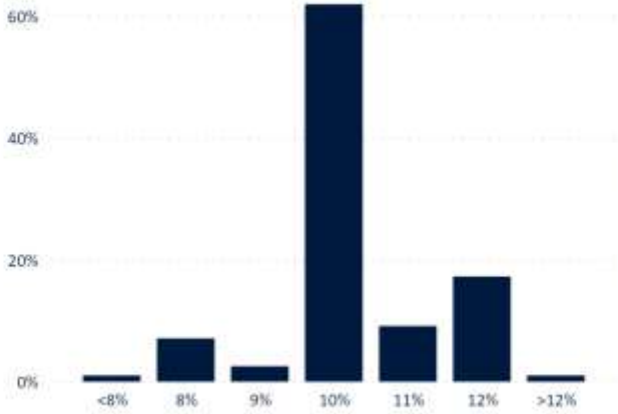
MIP EQUITY % METRICS

5.0% Minimum	**15.0%** Lower quartile	**17.5%** Median
17.2% Average	**20.0%** Upper quartile	**29.8%** Maximum

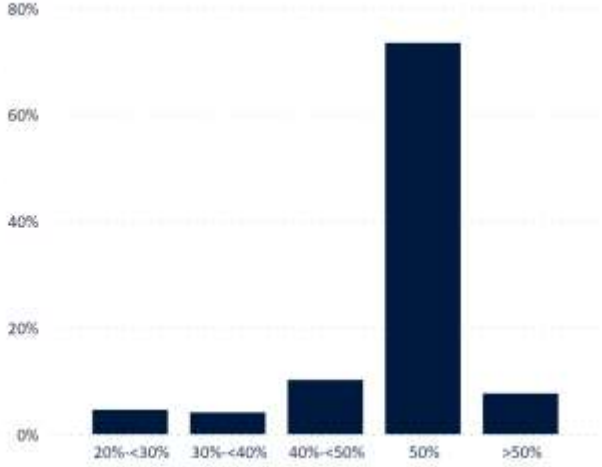
RATCHET vs. NO RATCHET



DISTRIBUTION OF YIELD %



DISTRIBUTION OF ROLLOVER %



***Note**: The dataset primarily includes ratchets that supplement MIP equity*

Source: LCF deals between 2018-2024

Common terms and recent trends

- Need to have “Skin in the Game”
- Typical Capital Structure of BidCo
- Mgmt Rollover (Inst’l Strip)
- Sweet equity (MIP)
- Allocation of MIP
- Follow-On Funding (Anti-dilution)
- Leaver Provisions
- Transfer Restrictions
- Fund-to-Fund Deals (incl. Continuation Vehicles)
- Restrictive covenants
- Mgmt Warranties
- Service Contracts