PERDa

Price Earnings Ratio Database

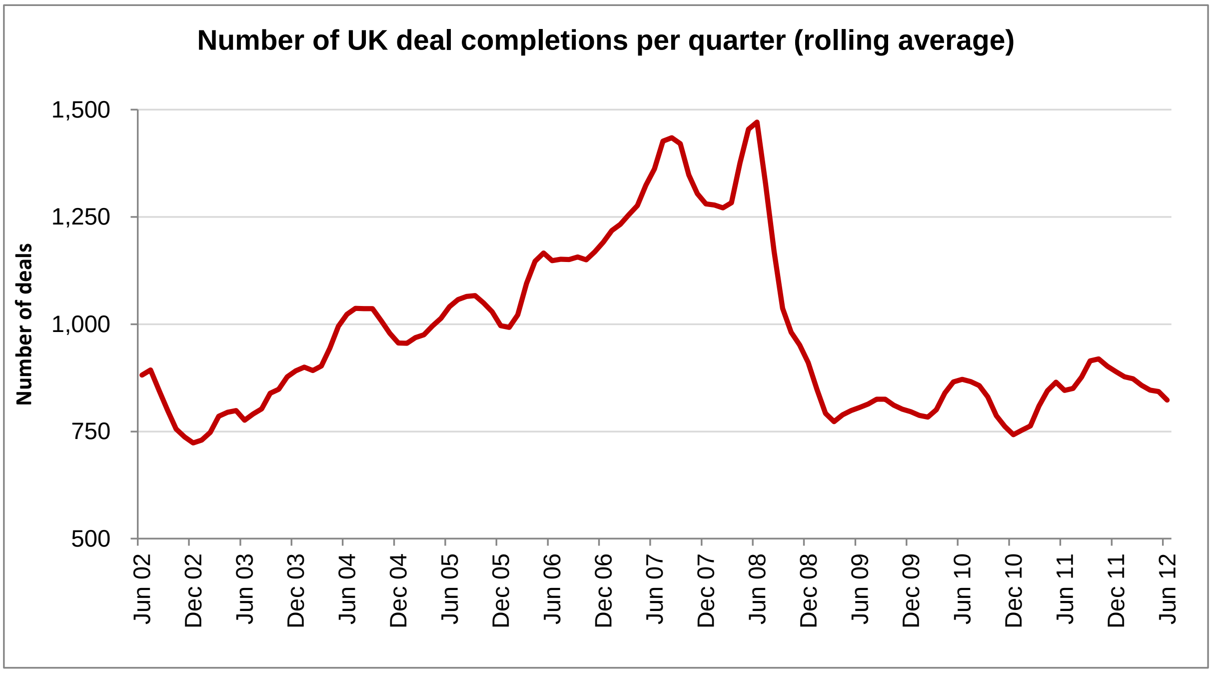
Issue 9: Summer 2012 UK Edition

INTRODUCTION

Welcome to the Summer 2012 issue of PERDa, the newsletter that summarises and provides commentary on the data contained in the private companies' Price Earnings Ratio Database. This data is used to highlight changes in the average value of private companies as shown by recent transactions, with this edition concentrating on UK companies and deals.

DEAL VOLUMES

As shown below, UK deal volumes started to recover in 2011, but this trend reversed in 2012, and volumes are now 15% below their long term average level (data from Corpfin/Experian):



This decrease matches the continued economic, financial and (global) political uncertainty, and some limitations on funding resulting in a lack of Corporate confidence. The combined effect is that many Corporates are unwilling to commit to acquisitions.

It also looks like this level of uncertainty will continue for some time. Recent surveys show that UK manufacturing activity dropped again in Q3 2012, fuelling fears that the economy is deteriorating after a brief rebound. The UK data came amid a series of dismal manufacturing surveys from around the world.

Therefore, there is unlikely to be a dramatic increase in volumes unless more fundamental solutions are found to the underlying issues. However, on the bright side, we are seeing some early indications of a small recovery in late Q3/Q4 2012.

On funding, it is welcome to see numerous completions being undertaken by the new Business Growth Fund, especially at the harder to fund, smaller end of the equity range. We are also glad to see new debt being provided either by existing players relaxing some of their rules, or from new players in the market. It will be interesting to see over the forthcoming months whether the coalition's actions to increase lending to business through initiatives such as "Funding for Lending Scheme" have the desired impact and whether any of these funds come through in financing deals.

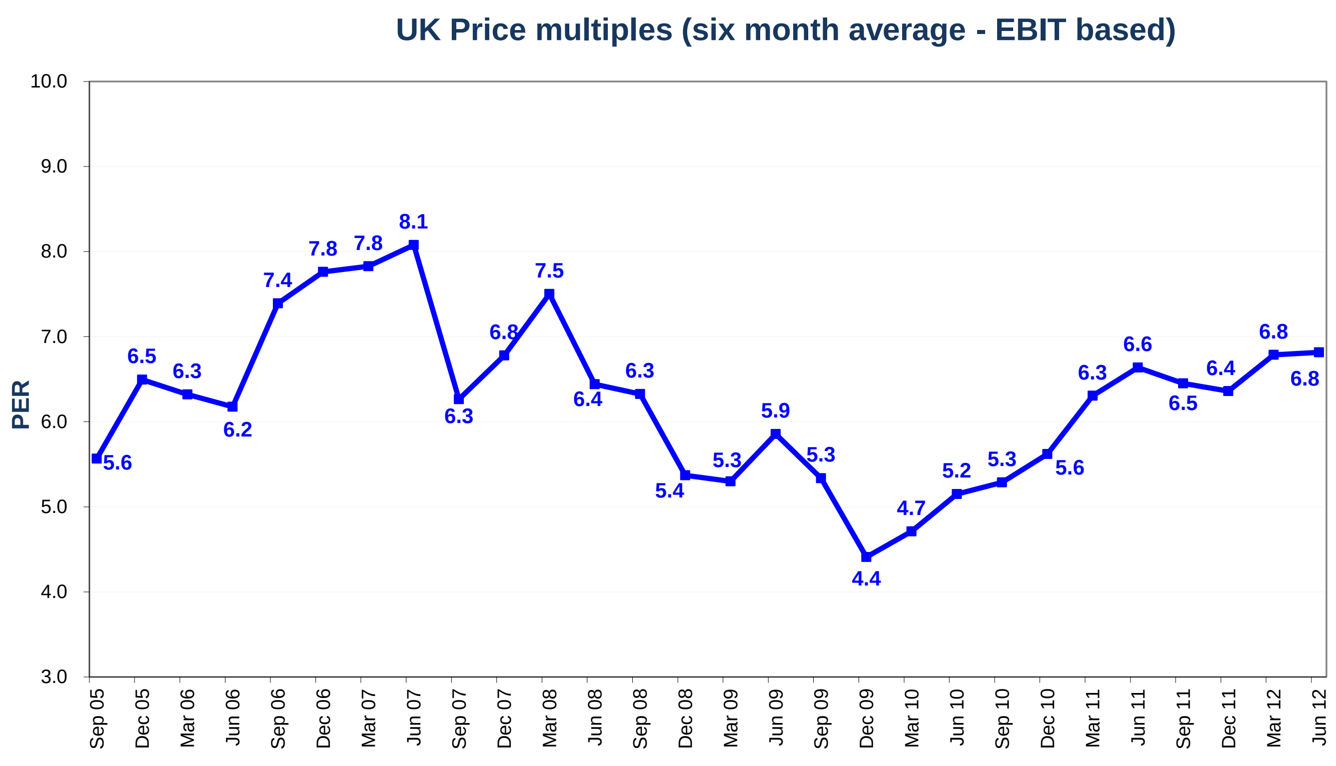
Our only note of caution is that most of these debt and equity funds continue (albeit understandably) to focus on the best, and often larger, deals.

The other defining characteristic of deal volumes is the continued high level of aborted transactions. This is shown both by anecdotal feedback on small and mid size deals, but also 2011 and 2012 studies on larger international deals.

We have also seen a significant increase in the scope of all of our due diligence work, with either acquirers or funders requiring additional support, and not being afraid to call off deals where this cannot be achieved. Creativity remains a key requirement to complete deals.

PRICE EARNINGS RATIO

Below is a summary of the latest UK data from PERDa, showing the movements in the average Price Earnings Ratio ("PER"). This ratio measures the relationship between the consideration (price paid) for private companies and their profits on an adjusted Earnings Before Interest and Tax ("EBIT") basis.



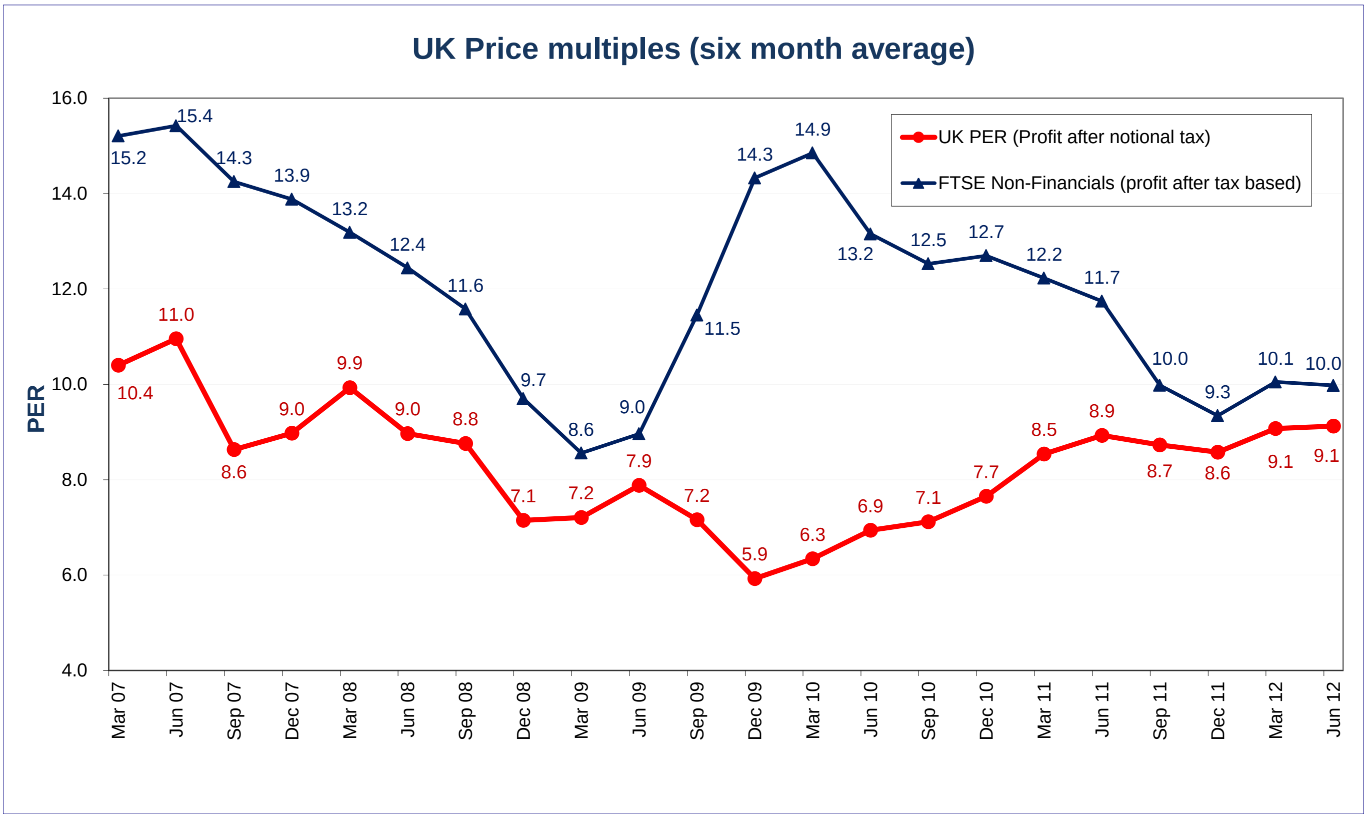
Note: The above private company PER trend is for UK deals only and differs from the European PER data shown at www.perda.org

In contrast to volumes, average PERs increased in 2012. Set against the decreasing volume data above, this implies a lower quantity of higher PER deals, again emphasising quality over quantity. Average UK PERs are now slightly above their long term average, and we are seeing some premiums being made for the best companies, particularly in certain markets/sectors (see below).

However, it is also true that much more of the consideration for deals is being not only deferred but linked to future performance. It seems that these arrangements now feature in a majority of deals, and the negotiations from the vendors focus on minimising the risks from deferrals/earn outs rather than eliminating them.

LISTED VERSUS PRIVATE COMPARISON

Our analysis of post-tax PERs from PERDA against the average Non-Financial FTSE PERs (first shown in our last newsletter) proved quite popular, so is repeated and updated below.



Again, this shows the different driving forces of pricing for private and public companies, as well as highlighting the problem with basing valuations for private companies from data derived from FTSE or other public based data series.

LISTED VERSUS PRIVATE COMPARISON

Looking at other data from PERDa since 2005:

1) The average PERs for MBOs are some 15% less than those of trade sales, although this discount has shrunk since 2008, reflecting the less frothy pricing of trade deals since that date;
2) Food, hotels and health sectors continue to be premium priced (i.e. average PERs in these sectors are between 10% and 50% higher than overall average PERs). However health and recycling sectors PERs show the most variability; and
3) UK PERs have tended to be lower than those in Germany and Sweden, but higher than those in Norway and the Netherlands.

MORE INFORMATION

Should you wish to discuss the details of this newsletter, or obtain a current market valuation report for your company using the data in PERDa, please contact your local LEA member at www.leadingedgealliance.com.

DATA COMPILATION

The database contains data submitted by members of the Leading Edge Alliance ("LEA"). The LEA is an international professional association of major, independently-owned accounting and consulting firms.

Financial data recorded for each deal is adjusted by the submitter to reflect the underlying basis of the deal. Graphs in this newsletter are based on the contents of the database at the time of compilation. The database is being constantly updated as deals complete and members submit new deal data. Over the period the database has been operating, we have received a number of late submissions that have been excluded from the derived average. Starting from the Summer 2011 update, we have included these late submissions, which has altered some of the historic averages from previous newsletters, although not to a material extent.

The PERDa data represents companies from across Europe, with an average Enterprise Value of £10.3m and average EBIT profit of some £1.5m. The UK transactions used in this newsletter have an average Enterprise Value of £14.6m and average EBIT profit of some £2.2m.

We would highlight that the PERDa data is primarily based on profits before tax and interest, whilst other PERs such as those quoted in the Financial Times are based on post tax profits.

The information in this newsletter is based on averages derived from the PERDa database and is not intended to be an absolute guide to private company valuations as there are significant other factors involved. Due to the nature of the data, the subjective nature of the adjustments made and the constant process of updating, no responsibility is accepted by the LEA or any of its members for the use of the data in the PERDa database or this publication.