



2011

# PCPIQ4

Private Company Price Index

## ► CAPACITY FOR M&A ACTIVITY EXISTS BUT CONFIDENCE APPEARS STIFLED

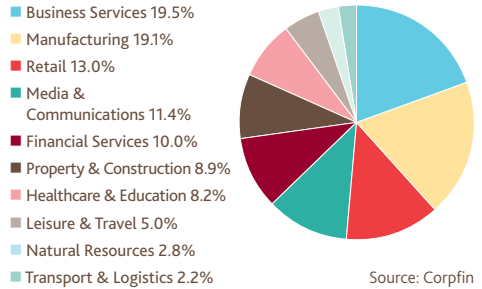
In total 2,071 deals were completed in 2011, of which 83% were trade deals and 17% were private equity deals. This represents a 7% increase on the 1,928 completed deals in 2010; however the relative split between trade and private equity deals has remained comparable.

The Private Companies Price Index (PCPI), which tracks the price/earnings (p/e) multiples paid by trade buyers for private companies fell from an average multiple of 11.7 times in 2010 to 10.6 times in 2011. This fall in pricing appears to have helped deal volumes with lower pricing making acquisitions more attractive in the private market.

The Private Equity Price Index (PEPI), which shows comparable multiples on sales to private equity rose from an average in 2010 of 11.7 times to 12.8 times in 2011. The BDO Private Equity survey found that 82% of PE managers are prepared to pay a scarcity premium for good quality businesses as evidenced by the sale in December 2011 of Wiggle. The overhang of private equity funds raised during previous years appears to have driven pricing with the incentive to invest resulting in higher multiples being paid to secure deals.

During 2011, business services, manufacturing, retail and media & communications deals accounted for over 60% of all transactions completed, with business services making up the largest number of deals due to the breadth of the sector. The relative mix of deals by sector remained fairly consistent with 2010, however retail experienced the largest increase but this was largely constituted by higher levels of distressed M&A activity being seen in this sector. PE managers do not expect this trend in retail to continue over the next 12 months with many predicting it to be the least active sector

### Total completed deals for 2011 by sector

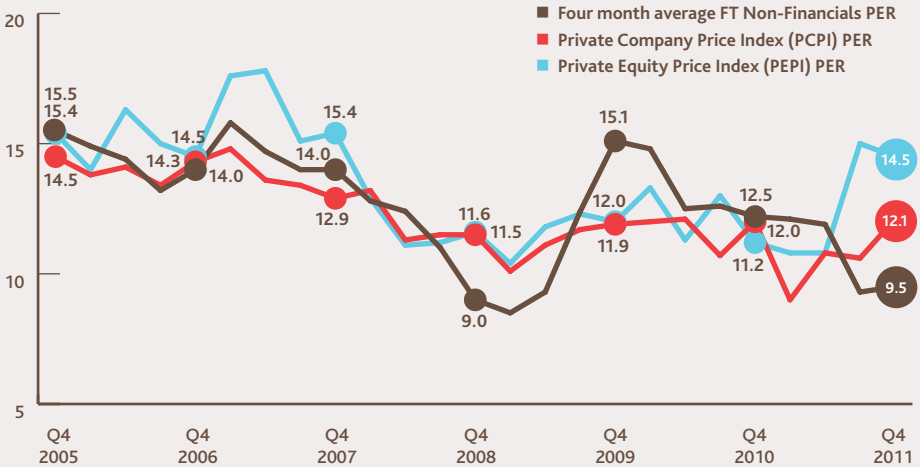


distressed deals aside. This is in contrast with the technology sector which PE managers predict to experience an increase in activity.

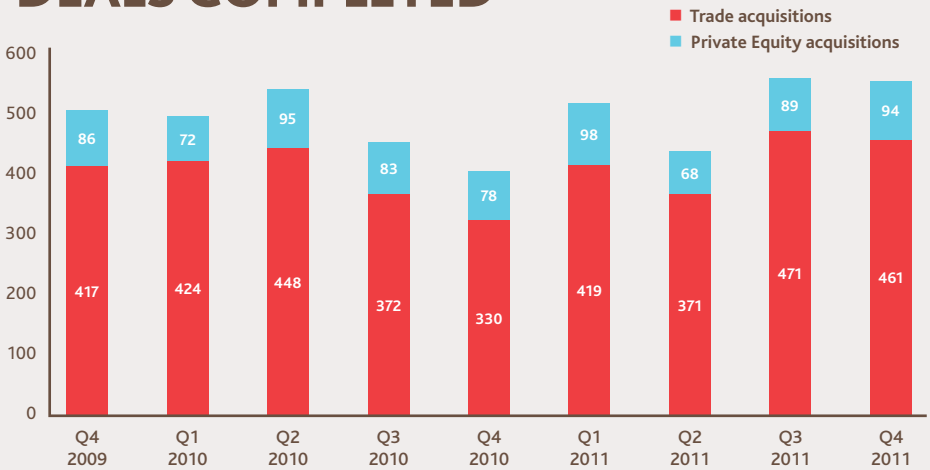
The state of the Eurozone economy remains a concern for M&A volumes generally with the impact of austerity measures in this region being likely to bring difficult challenges for the UK economy. During the Autumn Statement, the OBR forecasted negative GDP growth for the last quarter of 2011 and revised growth forecasts for 2012 to a modest 0.7%. More positively, inflation has started to fall helping consumers who have seen their living standards impacted as falling wage increases and rising inflation have taken their toll.

Despite macroeconomic challenges during the past year, falling price expectations for trade deals and the continuing pressure of private equity to invest have driven transaction volumes higher. Private equity continues to have an overhang of funds to invest and many corporates are holding relatively high levels of cash on their balance sheets. These two factors should continue to support deal volumes going into 2012.

# PCPI v PRIVATE EQUITY Q4 2005 – Q4 2011



# Q4 2009 TO Q4 2011 VOLUME OF DEALS COMPLETED





Christopher Clark,  
M&A Partner commented

“M&A volumes experienced a gradual recovery in 2011, with both deal volume and prices paid by private equity experiencing an improvement. However, macroeconomic factors including the Eurozone crisis, austerity measures and the likelihood of anaemic growth are likely to put downward pressure on deal volumes.

The private equity industry still has a large amount of funds to invest and is prepared to pay a premium for good businesses while many corporates have relatively high levels of cash to invest. These two factors should help to underpin both deal volumes and pricing going into 2012.”

## ▶ MAKING THE MOST OF THE PCPI/PEPI

The PCPI/PEPI tracks the relationship between the current four month rolling average FTSE Non-Financials price/earnings ratio (p/e) and the p/es currently being paid on the sale of private companies to trade and private equity buyers. The FTSE Non-Financials p/e is calculated from the p/es published in the FT. The private company p/e is calculated from publicly available financial information on deals that complete in the quarter. At the moment, the PCPI indicates that, on average, private companies are being sold for 12.1 times their historic after tax profits. The PEPI indicates that, on average, private companies are being sold to private equity buyers for 14.5 times their historic after tax profits.

As private companies are generally owner-managed, reported or disclosed profits tend to be suppressed by various expenses that may be non-recurring under a new owner. This will have been factored into the price the purchaser paid, but may not be reflected in the profits declared to the public. The effect of this is that the p/e paid as calculated from the publicly available information may be over stated.

The PCPI/PEPI tracks the discount between how public and private companies are being valued. This discount enables us to use valuation techniques which are only relevant to public companies and apply them to private companies in the same sector.

The PCPI/PEPI is calculated as the arithmetic mean of the p/es for deals where sufficient information has been disclosed. Over the last six years, the included deals for the PCPI have had a mean deal size of some £13m and a median deal size of some £12m. And the included deals for the PEPI have a mean deal size of £37m and median deal size of £20m. Therefore, if a company is smaller than this, then a further discount should be applied.

The PCPI/PEPI is an average measure and guide, not an absolute measure of value, as there are many other factors that can have an impact on value.

If you would like to know more about how to use the PCPI/PEPI to value your company, please contact your local BDO representative.

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