Brexit and the European Private Capital Markets: The Deal Makers' Playground

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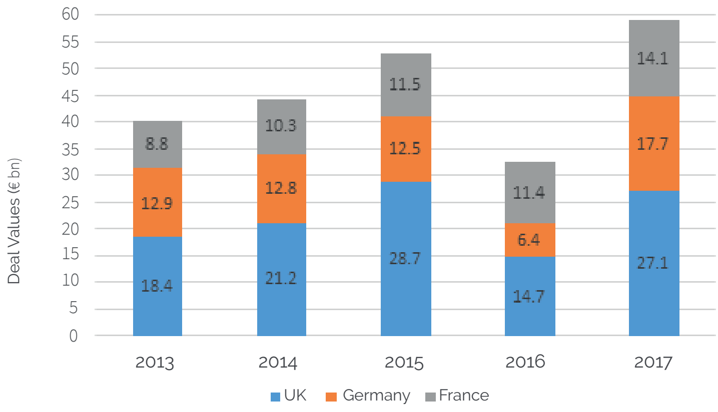
Uncertainty or opportunity? That is the question. When setting strategy and converting capital commitments into deal activity, private capital market participants seek both, regardless of geopolitical events such as Brexit. As such, depending on strategy, Brexit could be seen either way.

After the 2016 Brexit vote, uncertainty appeared to persuade deal makers to keep capital in hand within the UK and in other core European markets, such as Germany. For example, buyouts and buy-ins in the UK decreased from €28.7bn in 2015 to €14.7bn in 2016. Similarly, deal activity in Germany decreased from €12.5bn in 2015 to €6.4bn in 2016. French PE-backed buyouts and buy-ins, on the other hand, proved more resilient and remained stable after the Brexit referendum according to figures from Private Equity international [1].

Early 2017 saw deal makers who had dry powder on hand in YE 2016 seizing the opportunity created by this uncertainty. Deal activity in the UK reached a record £5.3bn in Q1 2017, which was the largest value recorded since Q1 2015 and a 15% increase over the full 2H 2017 value of £4.6bn according to the Centre for Management Buy-out in Private Equity Research [2].

A trend appears to be surfacing in continental Europe, where PE-backed buyout and buy-in activity is showing a greater recovery. Germany and France, for example, increased deal activity by €11.3bn and €2.7bn, respectively. UK private equity spending also experienced an increase of €12.4bn; however, this was still slightly below the level reached in 2015.

PE-Backed Buyout and Buy-In Activity



Source: CMBOR/Equistone Partners Europe/Investec Bank

This is perhaps illustrated best by a statement made by Shaun Mullin of Investec Growth & Acquisition Finance:

> *"The bigger firms have been more active across Europe and have done more in France and the Mediterranean, markets which have maybe been a little less loved in recent years."*

In addition, a trend seems to be in the making with fund managers investing in European markets that could split future deal activity across geographies. At the SuperInvestor Conference in Amsterdam, Neil MacDougall of Silverfleet Capital, a London-based private equity fund manager, said that during their current fundraise, investors were asking, “You won’t invest more than 30 percent of the fund in the UK, will you?”

He continued, “Most people feel that they don’t want to be overly UK exposed. There will be some companies that do better out of this, but, equally, others clearly won’t.”

Others at the conference were quoted in a Financial Times article expressing caution about deals in the UK in light of Brexit. Some noted that they are exploring other markets, such as France, for deal activity. Others noted that this cautious attitude was due to trading environments, the flight of European nationals from the UK, and a slowdown in the number who are coming into the country, all of which is putting a strain on portfolio companies.

Cash is king, and dry powder may be keeping deal activity strong. As discussed in the previous blog post, from 2014 to 2016, record levels of capital were raised in Europe and the UK as well as with global investment managers. The uncertainty of Brexit has not hampered deal activity in the UK given the current access to dry powder. However the geographic limitation placed on fund managers by investors may hinder the future deployment of capital investments into the UK.

Will this result in opportunity for other European countries, such as France and Germany, to become the top tier investment destination for Europe?

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This is the second of a series of articles in which the Private Capital Market (PCM) team in Ipreo’s London office reports on the potential impact of Brexit, both the uncertainty and the opportunities. Future articles will examine the strategies of fund managers and investors, valuations in the face of uncertainty, pipeline and risk management, and the direct impact on venture capital in Europe.

Sources:

1. Private Equity International, “UK Private Equity Spends Big After Brexit Slump,” December 20, 2017.
2. Financial Times, Private Equity Faces Pressure to cap UK Deals over Brexit, November 27, 2017.
3. Real Deals, “UK Private Equity Activity in Q1 Higher Than the Whole Second Half of 2016,” April 3, 2017.
4. Latham & Watkins, “French Employment and Tax Reforms Set to Boost Private Equity Buyouts,” December 7, 2017.