Brexit and Valuations in Private Equity: How are Fund Managers Leveraging Technology to Overcome Rising Challenges?

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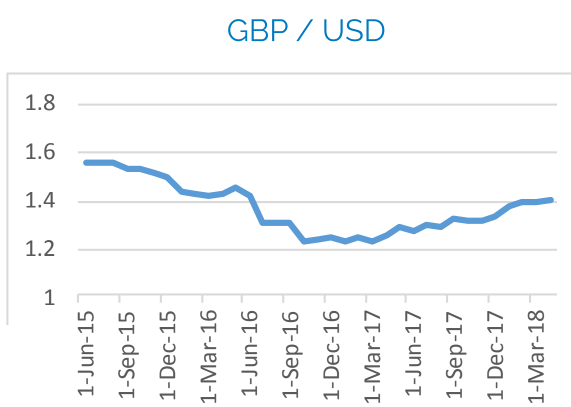
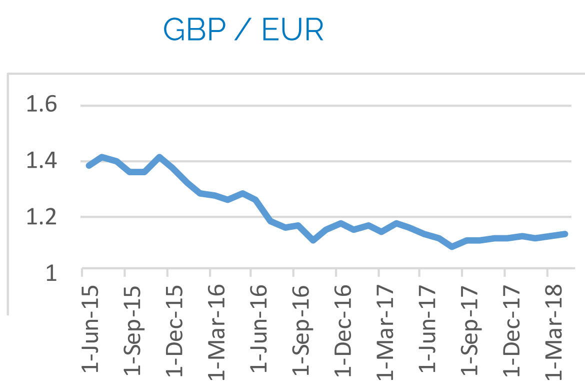
After the post-referendum results, fund managers face new challenges. The fluctuation and depreciation of the sterling pound, the uncertainty of a trade deal between the UK and the EU, and the impact of these factors on the market capitalisation of publicly listed firms create multiple scenarios where fund managers will find it increasingly difficult to value their existing and prospective investments.

In this article we will explore these factors and examine how technology can help overcome these difficulties.

The devaluation of the pound against the euro and the dollar can be seen as a double-edged sword for UK businesses in terms of their performance and, ultimately, their respective valuations. For example, both exchange rates are currently 13-15% below the rates posted on 23rd June, 2016. For businesses that primarily sell outside the UK, the devaluation of the pound is likely to lead to a surge in sales, while those firms that rely on importing goods, services, and raw materials from abroad will see their costs spike. Therefore, fund managers who are currently using a discounted cash flow (DCF) approach or a company multiple method need to understand how these changes in the exchange rates can affect the performance of their portfolio companies.





(Source: UKForex Limited: 2018)

A second challenge that fund managers face is determining how the market capitalisation of publicly listed companies, particularly those listed in the FTSE, have appreciated. In a post-Brexit environment, fund managers need to be able to assess the potential impact that increased exposure to the UK market may have on privately owned, mid-tier companies in their portfolios.

At the same time, it is increasingly problematic to assess the risk using company comparables, since domestic and privately-owned firms are unlikely to perform similarly to publicly listed and export orientated firms.

For valuations using a DCF approach, the impact of Brexit may be easier to model in the cash flows, but there is still some subjectivity involved in determining how the current economic circumstances will develop and how Brexit negotiations may impact business confidence. For example, fund managers need to evaluate how Brexit could potentially affect discount and risk rates when applying a DCF model in valuations.

How Can Technology Help Fund Managers Overcome the Challenge?

Given the factors mentioned above, many fund managers are exerting a greater level of scrutiny over their portfolios. This, in turn, is creating a need for more sophisticated calculations, and many of our clients are using iVAL to evaluate the different valuation methodologies and composites in a sophisticated and intuitive tool.

> "When you systematize the valuation process with a product like iVAL, you don't have to worry about simple math errors or accidentally overriding a number that breaks your "
>
> Andy Cisneros, Ipreo PCM Associate Director, Product Development

One of the main benefits of using this technology is that it ensures that all the data associated with valuations are centrally stored in a single source, whether these are cash flow transactions, company financial metrics, currency exchange rates, or company comparables. This enables different team members within a private equity firm, along with auditors and advisors, to share access to the data during a valuations review.

Ipreo also offers a thoughtful solution for valuations that enables users to standardise and scale their valuations process and toolset using a series of step-by-step wizards that generate audit-ready valuation reports with all the necessary supporting documentation.

In addition, our platform has an integrated feed-in from Capital IQ that enables clients to extract live and historical company comparables directly from the source.

Brexit brings a new set of challenges to the task of valuation. Fund managers are trusted by their LPs to have the knowledge and practise in these unpredictable environments to create and maintain value of portfolios. Technologies that bring greater consistency, rigour, and sophistication to their process can help them to navigate the challenges with greater confidence.

To see the valuation model that is helping fund managers conduct valuations amid the uncertainty of Brexit, please schedule a live demonstration with us.

For more information contact Ipreo Private Capital Markets at PCM-info@ipreo.com