TO P2P OR NOT P2P

PRIVATE EQUITY AND PUBLIC TAKEOVERS IN THE AFTERMATH OF COVID-19

ADDLESHAW GODDARD

INTRODUCTION

COVID-19 HAS PUT NORMALITY ON HOLD...

...but as the UK economy starts to come out of lockdown, the commercial drivers behind 2019's resurgence in private equity-backed public-to-private takeovers will be amplified. In the light of a likely reduction this year in auction processes for private businesses while the buyer/seller valuation expectation gap is bridged, we anticipate that, 'UK plc' will prove an attractive value proposition for private equity in the second half of 2020.

IN 2019 THERE WERE 30 ANNOUNCED PUBLIC TAKEOVER TRANSACTIONS INVOLVING PRIVATE EQUITY

ADDLESHAW GODDARD'S P2P SURVEY AND COVID-19

Addleshaw Goddard conducted a survey of leading mid-market UK private equity firms and their principal corporate finance advisers on the reasons for the 2019 resurgence of private equity-backed 'public-to-private' takeovers (P2Ps). The Covid-19 crisis derailed our publication plans - M&A dropped off the radar as the City reacted to the unprecedented crisis. Private equity funds focused on triaging their existing portfolio companies and investment banks embarked on a round of trading updates and fundraisings for existing listed clients.

Now that the initial shockwave of the Covid-19 outbreak has passed, we, alongside many others, are considering what opportunities the medium term will hold post-lockdown, and how best to prepare for the landscape that will greet us all once a degree of normality resumes. As the recovery phase begins, our survey results allow us to gauge how private equity in particular may react following the Covid-19 interruption. We are aware from our conversations with PE sponsor clients following the outbreak that, particularly given the recent drop in share prices, PE's focus will increasingly be on the listed sector for the foreseeable future, both for P2Ps and potentially also strategic private investments in public equity (PIPE) transactions.

If you would like to discuss this survey in more detail, please contact your usual AG representative.

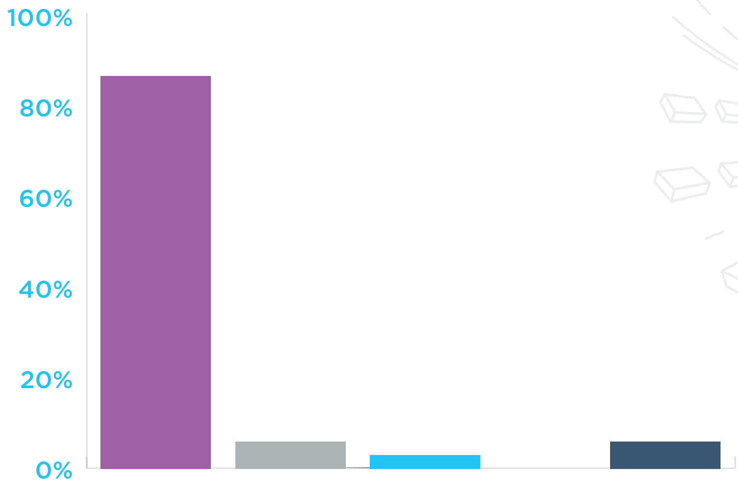
> **"...WE ANTICIPATE THAT 'UK PLC' WILL PROVE AN ATTRACTIVE VALUE PROPOSITION FOR PRIVATE EQUITY IN THE SECOND HALF OF 2020**

WHEN WAS THE LAST TIME YOU OR YOUR ORGANISATION WAS INVOLVED IN A P2P TRANSACTION?

PE HOUSES

ANSWER CHOICES	RESPONSES
Within the last year	22%
1-2 years ago	4%
3-5 years ago	7%
5+ years ago	33%
Never	33%

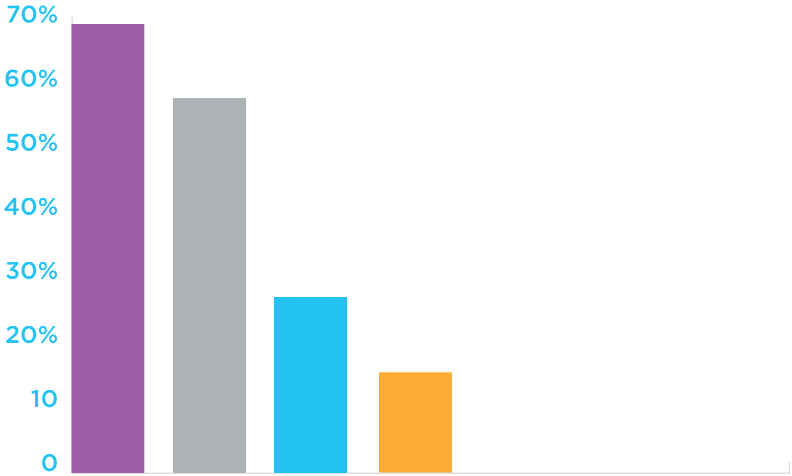
FINANCIAL ADVISERS



ANSWER CHOICES	RESPONSES
Within the last year	86%
1-2 years ago	5%
3-5 years ago	3%
5+ years ago	0%
Never	5%

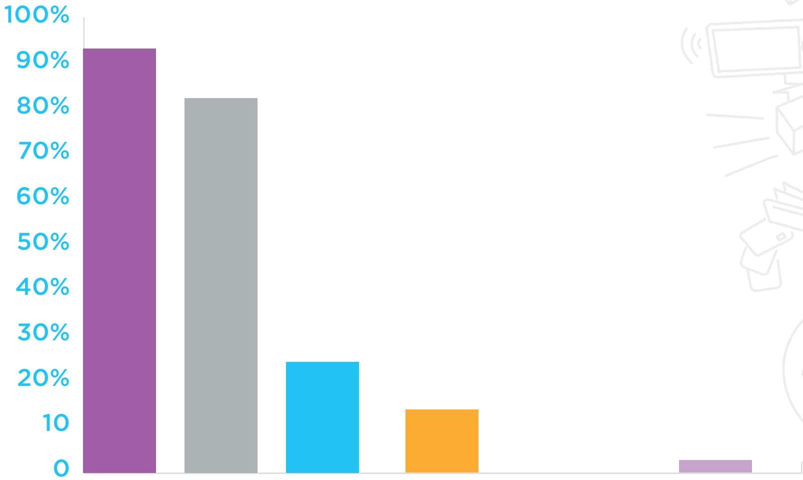
FROM WHICH JURISDICTIONS DO YOU PERCEIVE SIGNIFICANT PE BIDDER INTEREST IN UK P2P'S IS COMING FROM CURRENTLY?

PE HOUSES



ANSWER CHOICES	RESPONSES
US/ North America	67%
UK	56%
Rest of Europe	26%
Asia	15%
Africa	0%
South America	0%
Other	0%

FINANCIAL ADVISERS



ANSWER CHOICES	RESPONSES
US/ North America	92%
UK	81%
Rest of Europe	24%
Asia	14%
Africa	0%
South America	0%
Other	3%

2019'S P2P RESURGENCE

It is clear that there was a marked uptick in P2P activity in 2019. There were 30 firm offer announcements of public takeover transactions involving private equity. These deals accounted for approximately half of all such bids and compare with 14 P2P transactions in 2018 and 11 in 2017.

Our survey gives some further colour to the bare transactional numbers:

The P2P resurgence covered all sizes of deals. Historically, P2P transactions had been mainly the preserve of larger PE houses, often as part of a consortium, but our analysis shows that the **median value of an announced P2P deal in 2019 was £139m**, and 14 of 2019's P2Ps were sub £100m, with the remainder spread relatively equally through the valuation range up to £1bn+ deals.

A common narrative heard in 2019 was that 'cheap sterling' would lead to an influx of deals, predominantly led by US-domiciled, dollar-denominated PE funds, but our survey debunks that. While currency exchange rates did feature in commentary from financial advisers (50% of financial advisers mentioned it as a contributing factor for dealflow), **80% of financial advisers and 55% of PE houses noted the UK was the source of P2P interest**. In the light of the Covid-induced share price falls, currency advantage will be an even less prominent valuation factor.

THERE WAS A CLEAR RESURGENCE OF INTEREST IN P2PS

26% of PE houses surveyed were actively considering a P2P transaction, and 52% stated that they had become 'more likely' to carry one out

THIS INCREASED INTEREST IS AGAINST A BACKGROUND OF LIMITED P2P EXPERIENCE

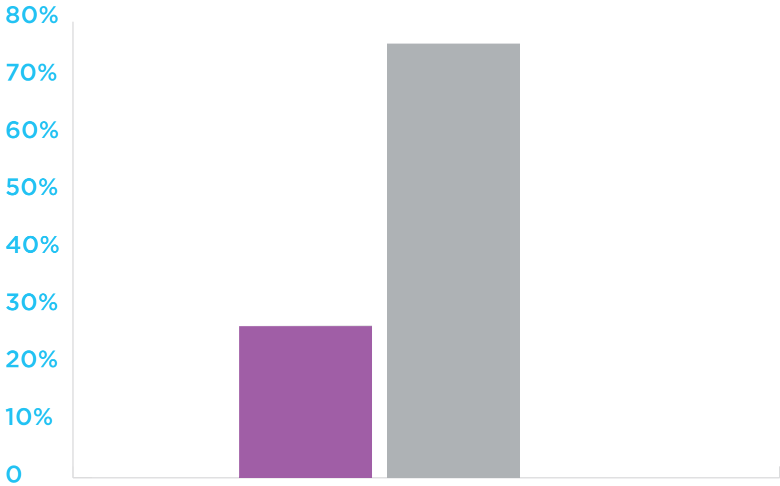
Within PE houses, approximately two-thirds of those surveyed had never carried out a P2P or only done so over 5 years ago

FINANCIAL ADVISERS BACKED THESE FINDINGS UP

86% of those surveyed actively advised on a P2P mandate in 2019 and 83% reported an increase in P2P activity

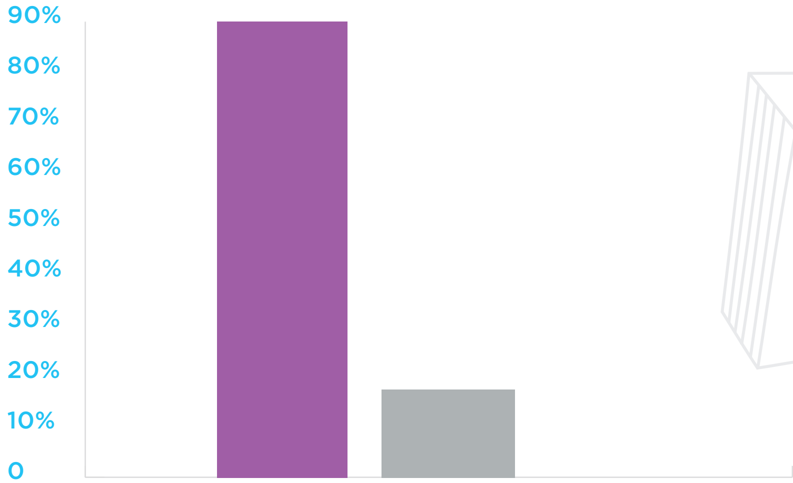
IS YOUR ORGANISATION CURRENTLY INVOLVED IN A POTENTIAL P2P TRANSACTION OR DO YOU THINK YOU WOULD BE LIKELY TO BE INVOLVED IN ONE IN THE NEAR FUTURE?

PE HOUSES



ANSWER CHOICES	RESPONSES
Yes	26%
No	74%

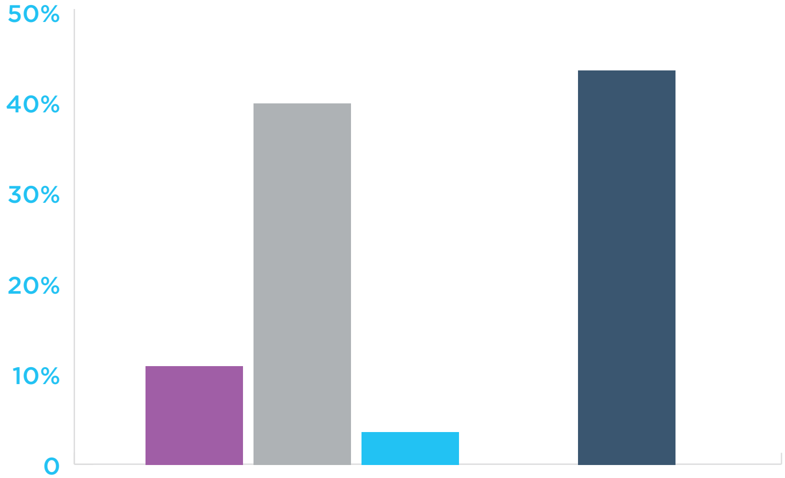
FINANCIAL ADVISERS



ANSWER CHOICES	RESPONSES
Yes	84%
No	16%

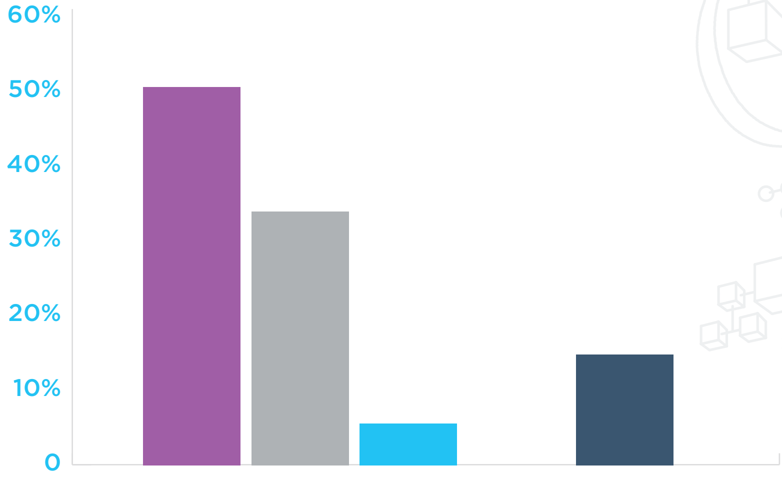
HAVE YOU OR YOUR PE CLIENTS BECOME MORE OR LESS AMENABLE TO CARRYING OUT A P2P TRANSACTION IN THE LAST 1-2 YEARS?

PE HOUSES



ANSWER CHOICES	RESPONSES
Much more	11%
Slightly more	41%
Slightly less	4%
Much less	0%
No difference	44%

FINANCIAL ADVISERS



ANSWER CHOICES	RESPONSES
Much more	49%
Slightly more	32%
Slightly less	5%
Much less	0%
No difference	14%

PRIVATE EQUITY MARKET FUNDAMENTALS: REACTION

It is vital to understand the reasons for 2019's increased interest in P2Ps in order to understand how the market may react following the easing and gradual release of the Covid-19 lockdown measures.

Three key factors were identified in our survey driving 2019's resurgence - all of these factors are interlinked and have been exacerbated by the Covid-19 crisis:

- **Increased competition** for private assets sold in auction processes: a factor for 59% of our private equity respondents in their focus on P2P transactions
- **Lack of opportunity** to acquire privately held businesses: mentioned as a reason by 26% of private equity respondents
- **Better value proposition** provided by listed targets: 44% mentioned this as a key factor. One commentator noted that it was not that PLC targets were necessarily undervalued but that good companies being sold in private auction processes were very fully priced

As a degree of normality slowly returns to the transactional arena in 2020, these three key drivers highlighted by UK PE funds will only become more relevant.

We anticipate auctions of quality private assets to be delayed by sellers to allow pricing to recover, and for auction processes to be well prepared and streamlined when they are finally launched. This scarcity of assets will increase competition and pricing for those auctions that are held.

Against this background the recent falls in 'UK plc' share prices make listed companies appear a better value proposition.

Financial advisers' views on the drivers for the 2019 P2P resurgence were similar, indicating these trends are firmly embedded: 56% noted increased competition for private assets, 32% noted a lack of opportunity to acquire privately held businesses and a significant 75% noted that listed companies appeared to offer a better value proposition. Financial advisers also highlighted some other underlying trends that support the conclusion that 2019's resurgence of P2P transactions will be resumed post-lockdown:

- Development of a 'herd mentality' among PE houses once a few successful P2P transactions had been completed. This was also mentioned as a transactional driver by 26% of private equity respondents. No doubt competitors demonstrating a capability to transact on P2Ps may persuade some investors to feel that it is more important they too create a track record, in order to maximize their opportunities for future fundraisings.
- Covid-19 will have disrupted the run-rate of the deployment of reserves of 'dry powder' held by PE funds, and with many finding their cash reserves already underdeployed pre-Covid-19, this too seems a likely further spur for PE houses to consider the public markets for acquisition targets this year.

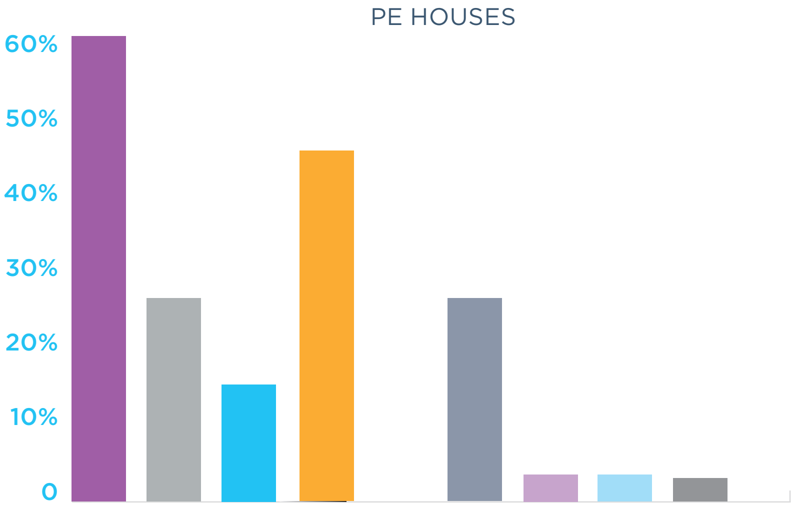
THREE KEY DRIVERS

- INCREASED COMPETITION
- LACK OF OPPORTUNITY
- BETTER VALUE PROPOSITION

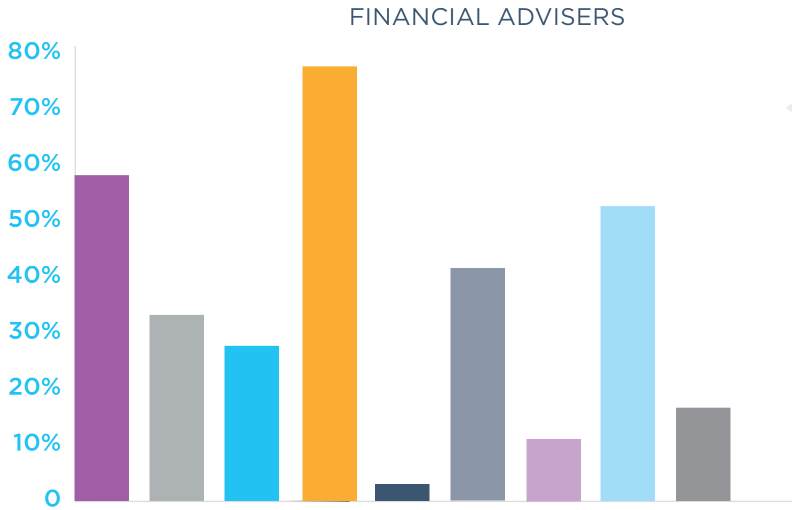
"

THE THREE KEY FACTORS DRIVING 2019'S P2P RESURGENCE HAVE BEEN EXACERBATED BY THE COVID 19 CRISIS

IF YOU OR YOUR PE CLIENTS HAVE BECOME MORE AMENABLE TO CARRYING OUT A P2P TRANSACTION, WHAT FACTORS DO YOU THINK HAVE CONTRIBUTED TO THIS?



ANSWER CHOICES	RESPONSES
Competition for assets in the private market	59%
Lack of quality assets coming to the private market	26%
Seeing similar organisations carrying out a P2P, or considering one	15%
Public assets perceived as being undervalued	44%
Public assets perceived as being better quality	0%
Public assets neglected, creating operational improvement opportunities	26%
Pressure from investors to avoid secondary buy-out transactions	4%
Favourable currency exchange for paying in UK sterling	4%
Attitudes to the UK/ Brexit	4%



ANSWER CHOICES	RESPONSES
Competition for assets in the private market	57%
Lack of quality assets coming to the private market	32%
Seeing similar organisations carrying out a P2P, or considering one	27%
Public assets perceived as being undervalued	76%
Public assets perceived as being better quality	3%
Public assets neglected, creating operational improvement opportunities	41%
Pressure from investors to avoid secondary buy-out transactions	11%
Favourable currency exchange for paying in UK sterling	51%
Attitudes to the UK/ Brexit	16%

DETERRENTS TO P2P PROCESSES

Our survey indicated that the three main deterrents to UK PE firms considering a P2P transaction were:

LACK OF CERTAINTY OF OUTCOME:
interloper risk on a P2P was a concern for 44% of respondents

COMPLEXITY AND COST OF A P2P PROCESS:
raised by 55% of respondents as an issue

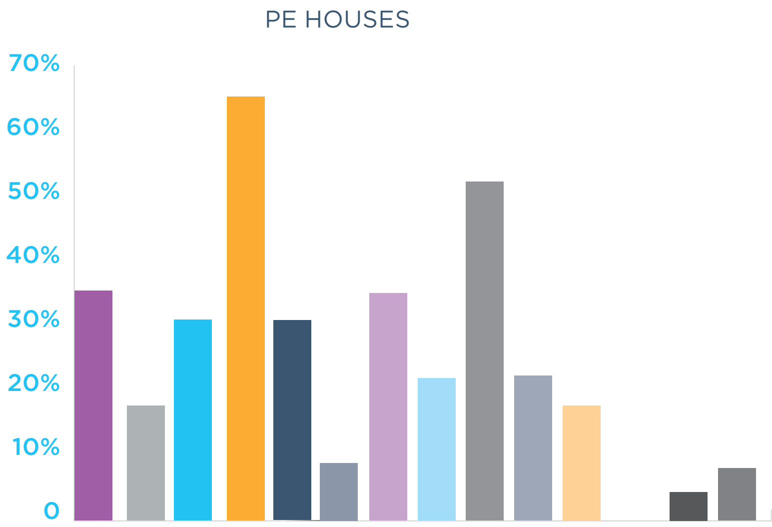
SKILLS GAP WITHIN PE HOUSES:
30% of replies noted a lack of familiarity with implementing these transactions

These deterrents will remain after the easing of lockdown measures, but all remain readily addressable for a PE house keen to explore a P2P process. Increasingly, private auction processes have little certainty of outcome for PE participants, and can involve significant aborts of time and cost. By comparison, there are relatively few interlopers in public bids. Our analysis of P2P transactions announced in 2017-2019 show that out of 55 P2P transactions, only 1 interloper made a competing firm offer announcement and 4 potential competing offers were identified (but did not proceed to a firm bid).

The responses regarding complexity and cost are best addressed in the context of the third concern that there is a skills gap. This lack of familiarity with the mechanics of a public bid was evident in the answers to the question concerning takeover regulation: 85% of financial advisers felt that the application of the Takeover Code was ‘about right’, whereas 30% of PE responses felt that the UK regime was overly restrictive, and 33% offered no view.

We put this concern down to the lack of familiarity that many UK PE houses have with P2P transactions – but this needs to be overcome if private equity’s interest in the public markets is to be satisfied. In our view, this makes it critical for a PE house considering a P2P to select advisers who are experienced market practitioners in both private equity and public takeovers.

WHAT FACTORS MIGHT CONTRIBUTE TO DISSUADING YOU OR YOUR PE CLIENTS FROM CARRYING OUT A P2P TRANSACTION?



ANSWER CHOICES	RESPONSES
Lack of familiarity with or experience of these transactions within their organisation	30%
Lack of time / resource within their organisation	15%
Requirement to pay a premium increases the risk of overpaying for assets	26%
Complexity	56%
Adviser's fees	26%
Prohibition on break fee arrangements	7%
Prohibition on exclusivity arrangements	30%
Lack of availability of wide-spread warranty cover	19%
Increased interloper risk	44%
Publicity requirements resulting from a public transaction	19%
Better opportunities elsewhere	15%
Less favourable currency exchange for paying in UK £	0%
Attitudes to the UK/ Brexit	4%
Other factors not listed above	8%

ANSWER CHOICES	RESPONSES
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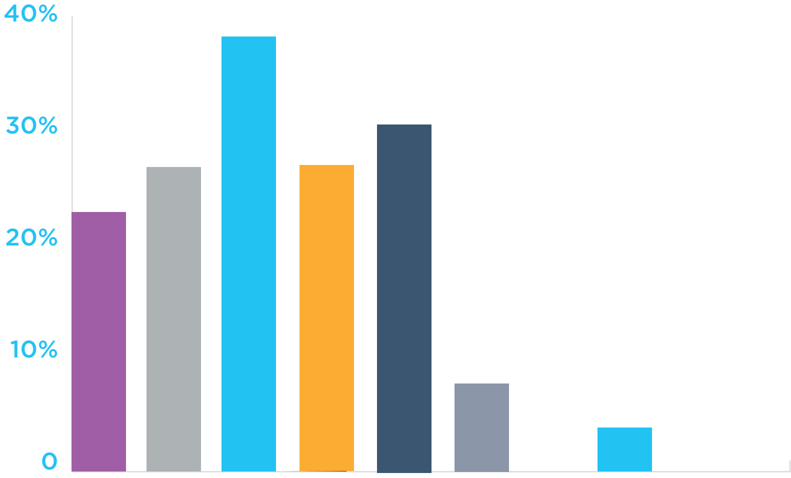
Increased interloper risk	27%
Publicity requirements resulting from a public transaction	43%
Better opportunities elsewhere	16%
Less favourable currency exchange for paying in UK £	3%
Attitudes to the UK/ Brexit	46%
Other factors not listed above	8%

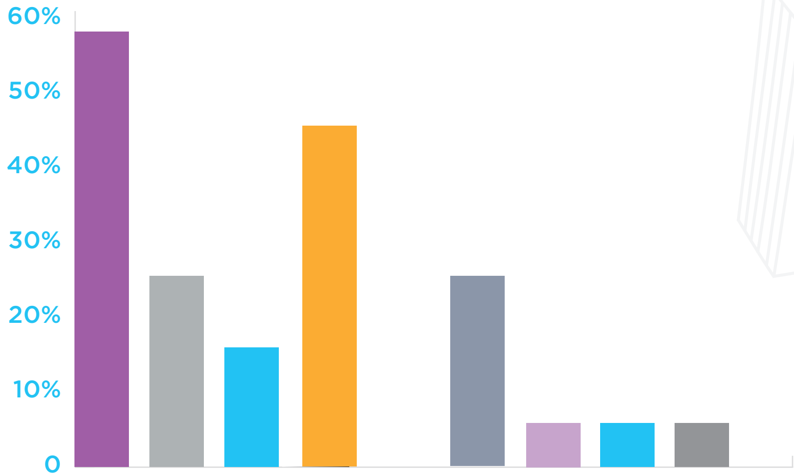
IF YOU OR YOUR PE CLIENTS ARE NOT CONSIDERING A P2P TRANSACTION, WHAT MIGHT MAKE THEM MORE AMENABLE TO CARRYING ONE OUT?

PE HOUSES



ANSWER CHOICES	RESPONSES
Having a greater understanding of applicable rules	22%
Seeing other P2Ps being carried out by similar organisations	26%
Lack of other, better opportunities elsewhere	37%
Continued or increased perception of public assets being undervalued	26%
De-regulation of takeovers or more flexible regulation	30%
Pressure from investors to avoid secondary buy-out transactions	7%
Favourable currency exchange for paying in UK sterling	0%
Attitudes to the UK/ Brexit	4%
Other factors not listed above	0%

FINANCIAL ADVISERS



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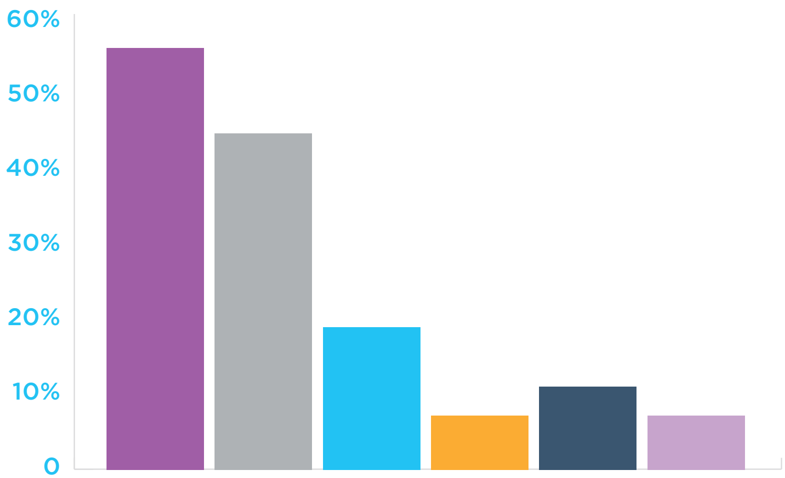
Lack of other, better opportunities elsewhere	15%
Continued or increased perception of public assets being undervalued	44%
De-regulation of takeovers or more flexible regulation	0%
Pressure from investors to avoid secondary buy-out transactions	26%
Favourable currency exchange for paying in UK sterling	4%
Attitudes to the UK/ Brexit	4%
Other factors not listed above	4%

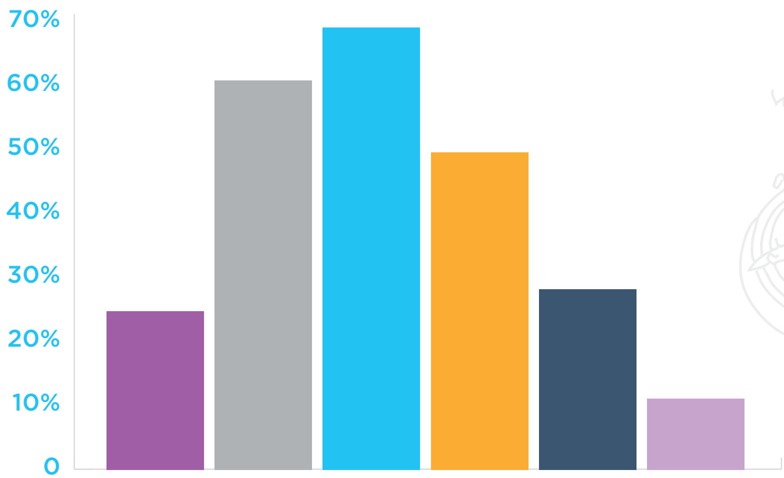
IF YOU OR YOUR PE CLIENTS ARE CONSIDERING ONE OR MORE P2P TRANSACTIONS, WHAT ENTERPRISE VALUE BRACKET DO THOSE DEALS FALL INTO?

PE HOUSES



ANSWER CHOICES	RESPONSES
less than £50 million	56%
£50 million to £100 million	44%
£100 million to £250 million	19%
£250 million to £500 million	7%
£500 million to £1 billion	11%
£1 billion +	7%

FINANCIAL ADVISERS



ANSWER CHOICES	RESPONSES
less than £50 million	24%
£50 million to £100 million	59%
£100 million to £250 million	68%
£250 million to £500 million	49%
£500 million to £1 billion	27%
£1 billion +	11%

THE FUTURE

Our survey indicates that PE interest in P2P transactions during 2019 was not a passing fad, but rather a reaction to the practical and commercial issues faced by every PE house in acquiring attractive businesses at acceptable multiples – it is a long-term systemic issue. Following the Covid-19 outbreak, the factors driving PE houses to look at public targets have been exacerbated, so we anticipate renewed interest as lockdown measures are eased. There still, however, remain Covid-19-related challenges in implementing these transactions:

FUNDING

Banks and debt funds have been focusing on their own customers and existing loans: the timeline for when they will open up and start lending on M&A opportunities, and the extent to which terms shift more towards lenders to reflect market conditions, will determine both the timing and volume of transactions.

VALUATIONS

Those businesses whose long-term cash flow has been interrupted by Covid-19 may prove difficult to value. This uncertainty, plus the expectation gap caused by listed companies having recently had much higher share price valuations, may result in it being a harder process to obtain a fulsome target board recommendation. That said, institutional shareholders in a listed company may turn out to be more willing sellers at an acceptable premium to current valuations than the founders and private equity owners of private businesses who are still hanging on to their pre-crisis value expectations.

REDUCTION IN LISTED PLCS

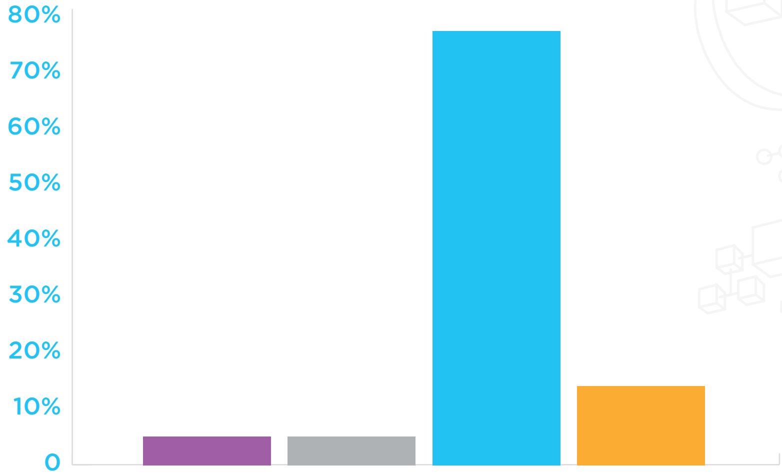
A reduction in the number of listed target companies: the pool of listed companies has been growing shallower as many more companies exit the public markets, either by takeover or by delisting, for insolvency or other reasons, than are being replaced by IPOs. One by-product of the Covid-19 outbreak is that the public markets have proved their invaluable ability to be a source of cash for listed companies, with fundraisings being completed at short notice, often within a matter of days. We hope that this will encourage more companies to reappraise the benefits of being listed, and lead to an increase in IPO dealflow in the longer term, replenishing the stocks of listed companies.

IN YOUR OPINION, IS THE REGULATION OF P2PS TOO RESTRICTIVE?

PE HOUSES

ANSWER CHOICES	RESPONSES
Too restrictive	30%
Not restrictive enough	4%
About right	33%
No firm view	33%

FINANCIAL ADVISERS



ANSWER CHOICES	RESPONSES
Too restrictive	5%
Not restrictive enough	5%
About right	76%
No firm view	14%

2019 AG PRIVATE EQUITY HIGHLIGHTS

>40

ADVISOR TO MORE THAN 40 INVESTORS ACROSS THE FULL RANGE OF MIDMARKET TRANSACTIONS

80%

REPEAT ADVISORS TO 8 OF THE TOP 10 UK MIDCAP PRIVATE EQUITY INVESTORS

OVER £7BN AGGREGATE DEAL VALUE

UK PRIVATE EQUITY ADVISOR OF THE YEAR 2019 (REAL DEALS) – OUR 3RD WIN IN 4 YEARS

100+

ADVISED ON OVER 100 BUYOUTS, INVESTMENTS, FOLLOW-ON ACQUISITIONS AND EXITS

TIER 1

LEGAL 500 RANKED TIER 1 FOR MID-MARKET PRIVATE EQUITY

#1

LEGAL ADVISOR TO LEAD INVESTOR ON SUB - £500M PRIVATE EQUITY TRANSACTIONS BY VOLUME

20+

ADVISED ON DEALS ACROSS MORE THAN 20 JURISDICTIONS

2019 AG PUBLIC TAKEOVER HIGHLIGHTS

13

NUMBER OF ANNOUNCED TAKEOVER SITUATIONS ADVISED ON

OUR TEAM INCLUDES 3 EX-TAKEOVER PANEL SECONDEES, GIVING US UNRIVALLED INSIGHT INTO TAKEOVER MARKET PRACTICE

£365M

WAS THE AVERAGE OFFER VALUE FOR TAKEOVERS WE ADVISED ON

#1

ADVISED ON THE LARGEST AIM COMPANY TAKEOVER

KCOM

ADVISED KCOM ON RARE CODE AUCTION PROCEDURE TO RESOLVE £627M CONTESTED TAKEOVER

US$889M

ADVISED SAFECHARGE ON RECOMMENDED TAKEOVER BY NUVEI CORP

TIER 1

RANKED IN TIER 1 FOR MIDCAP EQUITY CAPITAL MARKETS (LEGAL 500 UK)

£415M

ADVISED A&J MUCKLOW ON LONDON METRIC'S CASH AND SHARE OFFER

PROBLEMS. POSSIBILITIES.
COMPLEXITY. CLARITY.
OBSTACLES. OPPORTUNITIES.
THE DIFFERENCE IS IMAGINATION.
THE DIFFERENCE IS AG.

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