PitchBook

European PE Breakdown

Q3 2020

Contents

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Introduction

PE deal volume came roaring back in Q3 2020, as dealmakers shifted focus to offence and were selectively aggressive in certain parts of the economy. The re-opening of leveraged lending markets, elevated dry powder levels, and resilience shown in the lower end of the market contributed to the uptick in deal volume. That said, deal activity is still considerably shy of pre-pandemic figures, and we expect a multi-year recovery that will be choppy, uneven, and uncertain, with diverging trends across regions and asset classes due to COVID-19. The UK & Ireland contributed the largest jump in deal volume after a sizable fall in Q2. And finally, sponsors' insatiable appetite for technology assets continued, with IT deal volume proportions hitting a new quarterly peak.

Although exit activity in the quarter remained largely stale from Q2 2020, annual exit count is pacing towards a ten year low, as sponsors continued to be cautious about exiting positions during volatile periods. Until a sense of normalcy resumes and valuations bounce across PE portfolios, sponsors will avoid liquidity events unless assets are distressed, meaning longer hold periods, fewer distributions, and more GP-led secondaries. Sales to financial sponsors drove exit value in the quarter, while exits to strategics lagged. Following a rebound in public markets, we saw the largest IPO by market capitalization since 2013 list on the London Stock Exchange. We anticipate more exits via IPO in the coming quarters as the public equity markets continue their strong recovery.

PE fundraising activity gained considerable momentum in the third quarter, putting 2020 on pace for its second-highest capital raised total in a decade. The bifurcation in the fundraising market continues to accelerate as underlined by funds sized above €1 billion driving totals. CVC Capital Partners closed the largest European buyout fund in history in Q3 2020, raising €21.3 billion in seven months, while Nordic Capital raised €6.1 billion completely remotely—further quickening the digital transformation and adoption in the fundraising market. In a diverging fundraising market, fund count is pacing towards a new annual nadir as less established managers struggled to close funds amid the volatility. While not yet prevalent in Europe, SPACs could be making a comeback in the region with Harvester Holdings set to list on the London Stock Exchange.

Dominick Mondesir
EMEA, Private Capital Analyst

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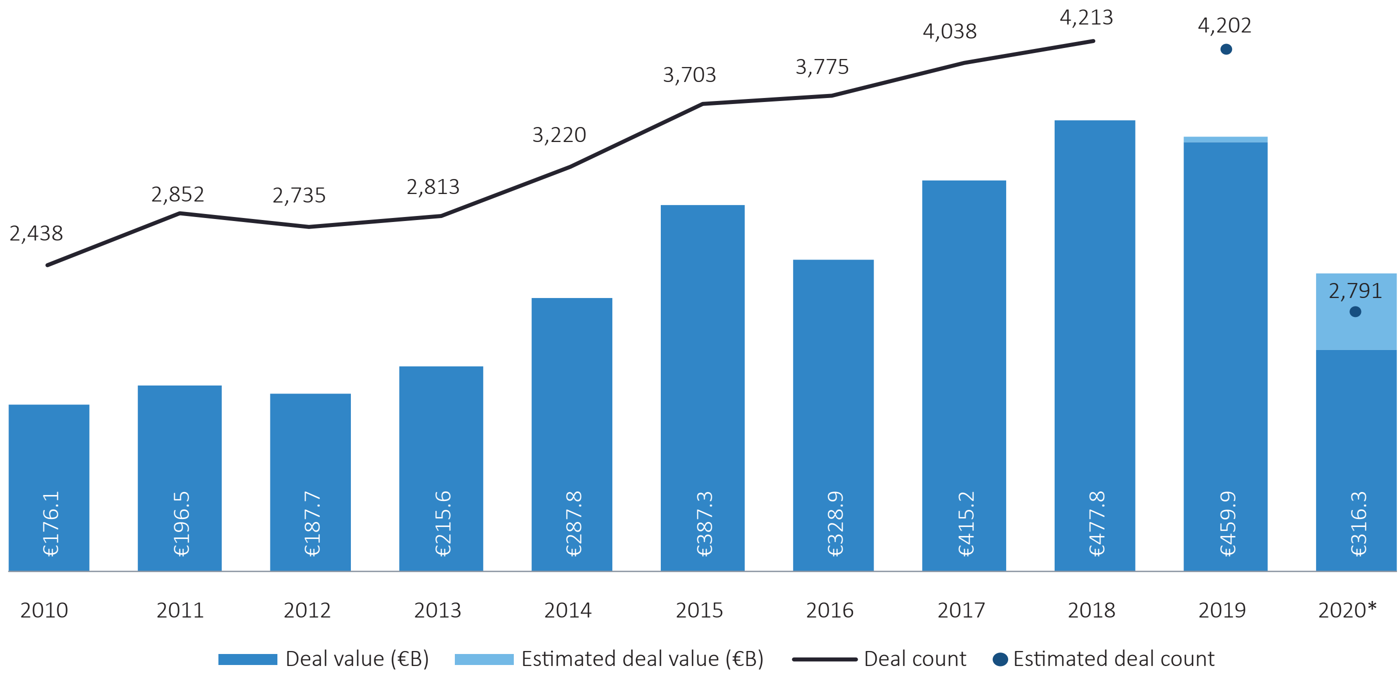
Overview

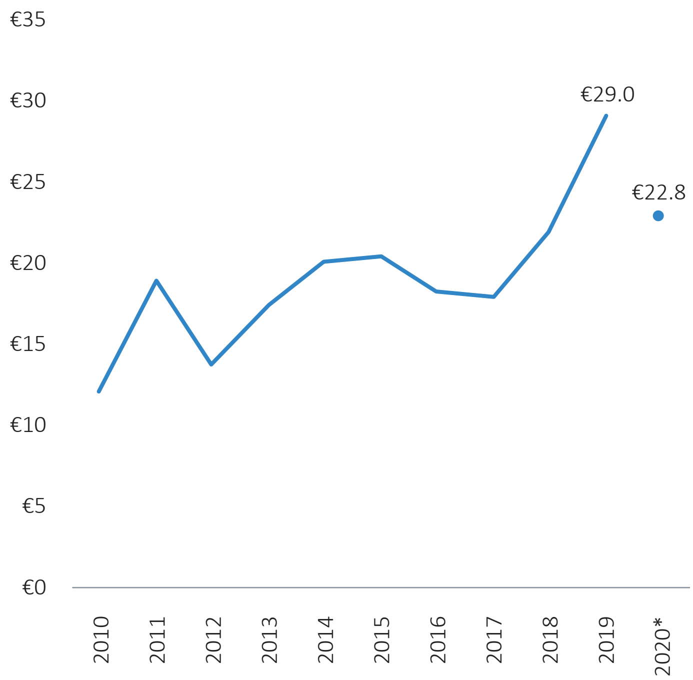
PE deal activity



Source: PitchBook | **Geography:** Europe
*As of 30 September 2020

Q3 2020 was the first full quarter in which European economies started to re-open from the "Great Lockdown" crisis, and the pickup in European PE deal volume was apparent. European dealmakers closed on 972 transactions worth €100.8 billion in the third quarter—QoQ increases of 32.9% and 2.9%, respectively. A combination of the re-opening of leveraged lending markets, a record of €224.6 billion of dry powder,[1] and GPs shifting part of their focus to sourcing and executing on new opportunities contributed to the uptick in deal volume. In a recent survey by S&P Global, 57% of European dealmakers stated their main area of focus in the coming months will be making new investments.[2] Although deal volume saw a strong recovery from the previous quarter, we are still considerably shy of pre-pandemic figures, and we expect a multi-year recovery that will be choppy, uneven, and uncertain, with diverging trends across regions and asset classes due to COVID-19. On an annual basis, the numbers paint a bleaker picture, with deal volume down 6% from Q3 2019. The fall was even steeper in terms of deal value, with numbers down one fifth YoY. This dynamic pushed the median deal size down to €22.8 million, as the bulk of GPs forewent making outsized platform bets amid the volatility and tighter financing thresholds for larger deals.

Median PE deal size (€M)



Source: PitchBook | **Geography:** Europe
*As of 30 September 2020

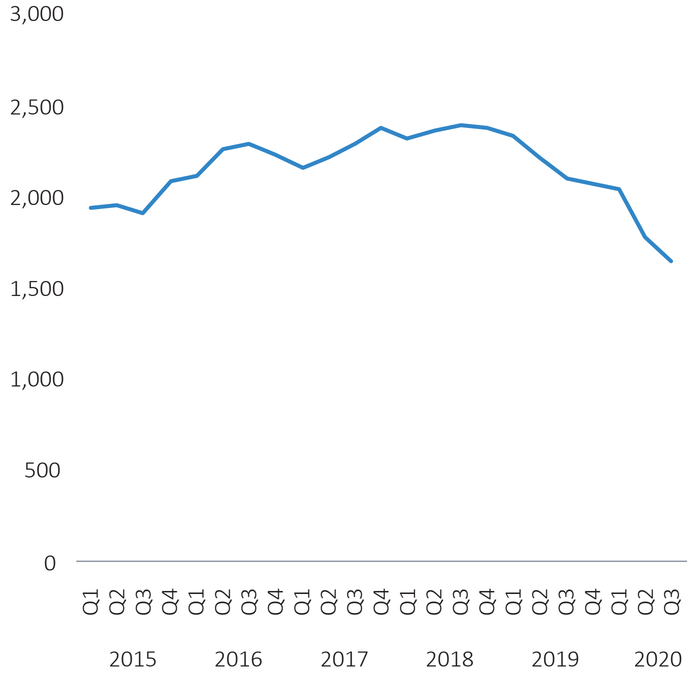
1: As of 31 December 2019.
2: "The Impact of the COVID-19 Pandemic on the Private Equity Market," S&P Global Market Intelligence, Ewa Skornas and Larisa Whitmore, 14 September 2020.

More broadly, while we saw a rebound in European GDP growth in Q3 2020, buoyed by the EU's signing of the landmark €750.0 billion recovery fund, the revival in European deal activity is far from complete. Although dealmaking remains substantially above the lowest points of the global financial crisis (GFC), dealmakers are being cautious and prudent on the real economy and are expecting the unexpected for a few reasons. First, the European Commission recently forecast a Eurozone GDP contraction of 8% in 2020, which will weigh negatively on PE-backed assets that tend to be GDP linked and therefore somewhat cyclical in nature. Second, rising COVID-19 infections and a stronger euro, which has appreciated around 10% against the US dollar since March,[3] will make European assets less attractive for non-euro denominated buyers. Third, economies reinforcing restrictive social distancing measures will substantially weigh on businesses' cash flow profiles and will further widen the disconnect between valuations and fundamentals. And lastly, the potential of second national lockdowns, a hard Brexit, and the winding down of critical fiscal support programmes pose substantial risks to the economic outlook in Europe in the short-medium term.

Although large headwinds persist in the European PE deal environment, sponsors with the firepower and staying power to ride out the crisis were being selectively aggressive in certain areas of the economy, as they tried to capture mispriced risk and heighten portfolio resilience. In the largest transaction of Q3 2020, KKR (NYSE: KKR) carved out UK-headquartered Viridor Waste Management, a division of FTSE 250 company Pennon Group, for €4.7 billion. The recurring and long-lasting nature of Viridor's revenue generation activities makes the company resilient during volatile periods, as it benefits from contracts with local authorities that last as long as 25 years. In the coming quarters, we may see more carveouts of UK assets from domestic and foreign entities as companies look to de-risk operations due to the looming possibility of a hard Brexit.

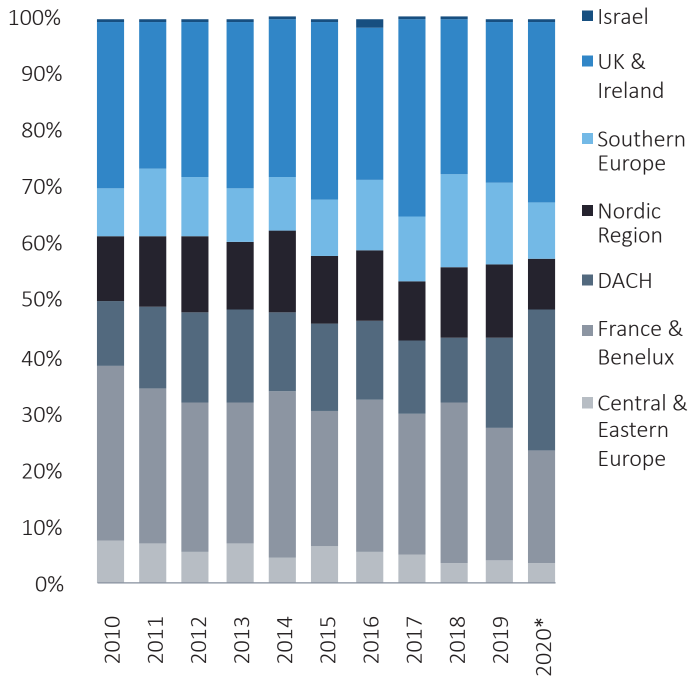
The rise in PE deal volume from Q2 2020 can largely be attributed to resilience shown in the lower end of the market. In Q3 2020, the volume of deals that closed under €25 million grew nearly one fifth from the previous quarter. The development of the European private credit space, which has €58.8 billion of dry powder,[4] smaller valuation disconnects, and reduced equity cheque sizes, has made financing for smaller transactions easier to obtain and may explain why we have seen an uptick in deal count for

PE deals under €25 million (#), rolling 4 quarter



Source: PitchBook | **Geography:** Europe
*As of 30 September 2020

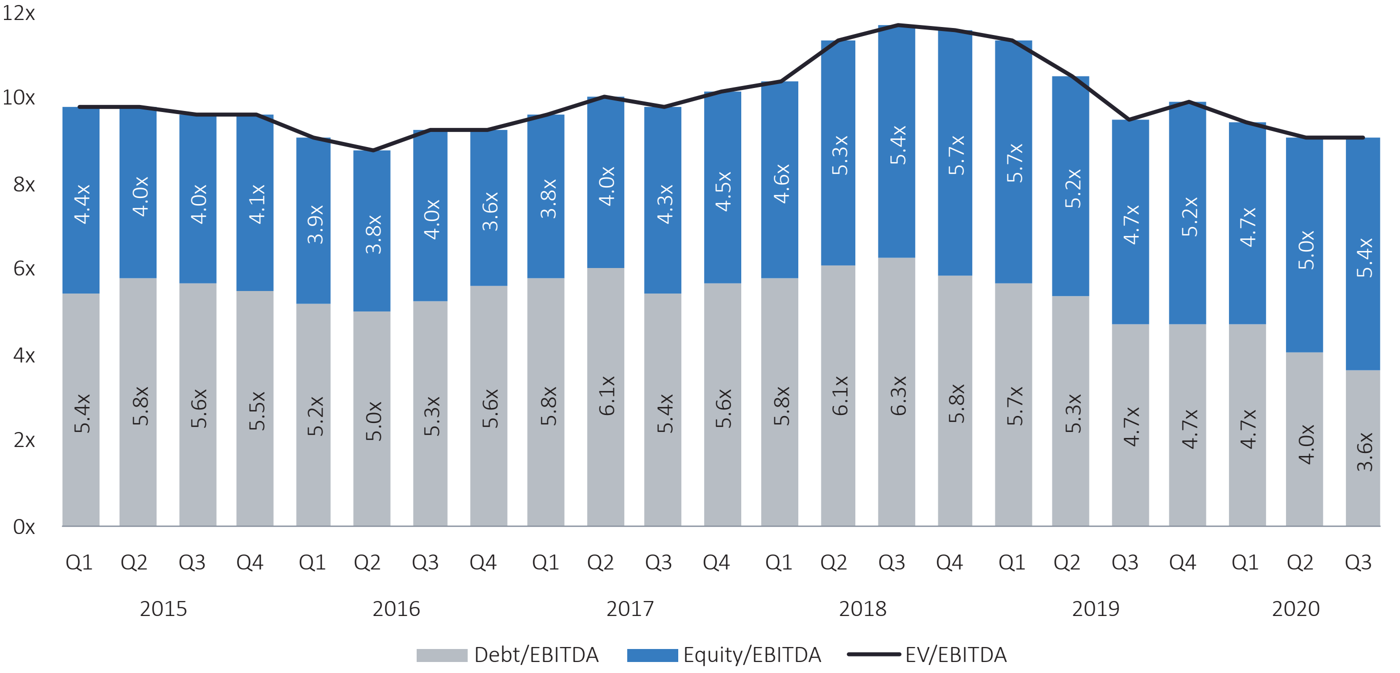
PE deals by region (€)



Source: PitchBook | **Geography:** Europe
*As of 30 September 2020

3: "ECB to Monitor Rise of Euro After Keeping Rates on Hold, " Financial Times, Martin Arnold, 10 September 2020.
4: As of 31 December 2019.

Median rolling four quarters PE buyout EV/EBITDA multiples

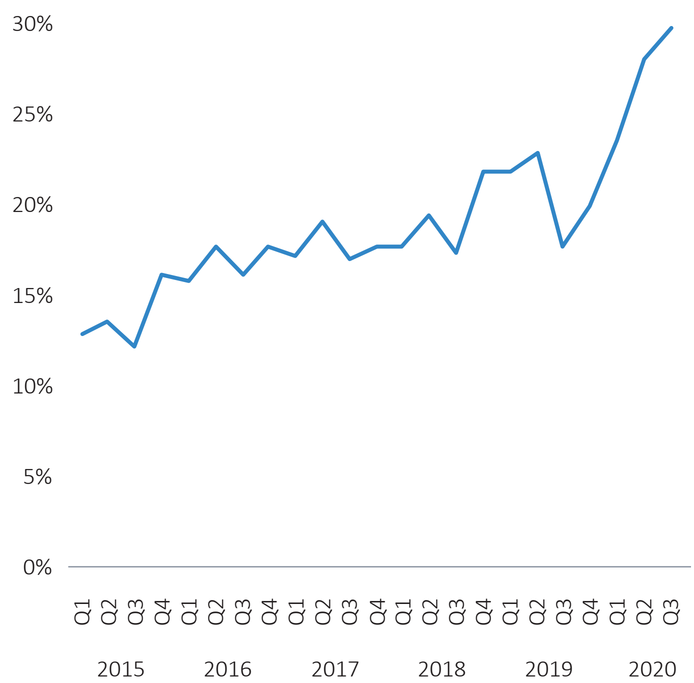


Source: PitchBook | **Geography:** Europe
*As of 30 September 2020

this transaction size bucket. Moreover, the majority of closed transactions sized under €25 million had no institutional backing, meaning founders and management teams were arguably more receptive to a sale or an injection of equity to either stabilize operations during the dislocation or to quicken growth by taking advantage of opportunities the pandemic presented. For example, Summit Partners injected €22.6 million of growth equity into Belgium-based CluePoints, a software provider that monitors risks and general data quality oversight of clinical trials for pharmaceutical companies. This transaction underlines sponsors' continued appetite for healthtech assets, as discussed in our Q2 2020 European M&A breakdown.

Dissecting regional activity by deal count shows the UK & Ireland contributed a near one-quarter jump from Q2 2020—the largest of any European region. Interestingly, the region also accounted for the largest fall in deal volume in the previous quarter, at just over 54%, as discussed in our Q2 2020 European PE breakdown. The sharp rise in activity perhaps signals the beginning of a recovery in the region after GDP contracted by a record 19.8% in Q2 2020,[5] falling twice as fast as the US and Germany. While many economists are forecasting UK GDP to rise by a sizable 14% in Q3 2020,6[6] significant headwinds still

IT deal volume proportions (#)



Source: PitchBook | **Geography:** Europe
*As of 30 September 2020

5: "BoE Economist Warns Against Pessimism After Record Drop in GDP, " Financial Times, Chris Giles and Valentina Romei, 30 September 2020.

plague the UK economy—and therefore, dealmaker confidence. The winding down of the government's furlough scheme; the introduction of a new three-tier lockdown system, which has seen certain UK regions go back into a near full lockdown; and the real possibility of a hard Brexit will weigh negatively on the UK. In addition, consumers are curtailing spending and increasing savings considerably amid rising unemployment and the potential of a second national lockdown due to rising COVID-19 cases.[7] The aforementioned factors, coupled with the region's excessive reliance on consumer services, indicate GDP output will track lower than other jurisdictions in the coming quarters and could slow PE deal momentum.

That being said, the region saw some interesting deals close in the quarter, including a €422.2 million growth investment in UK-based Ki Insurance by The Blackstone Group (NYS: BX) and BRIT insurance. The digital platform will replace work traditionally done by underwriters by evaluating policies and offering automatic quotes in the first fully digital algorithm syndicate to be approved by Lloyds of London. The platform will launch in Q4 2020 and has the potential to revolutionize the insurance industry. The need for digital adoption in the insurance industry has been accelerated by the pandemic as the underwriting process was forced to switch from exchange floors to online.

Sponsors' appetite for technology's six Cs of cashless, cybersecurity, e-commerce, collaboration, cloud, and content creation, which are growing drastically faster than the broader economy, continued in the third quarter, with IT deal volume proportions hitting a new quarterly peak of 29.7%. The sector has proven resistant to the pandemic, and with the majority of transactions in the space being bolt-ons, which are also pacing towards a new annual high, we anticipate these two strong secular trends will bring additional capital inflows into the IT space. GPs will play offense via IT-enabled bolt-ons across their portfolios, no matter the underlying sector of the asset, as platform companies seek to augment their digital adoption, transformation, and resilience. However, competition for such assets will remain fierce due to elevated dry powder levels, meaning valuations will sustain if not increase for IT businesses.

Valuations remained muted in the third quarter, and we do not expect any material falls in the short term. The median rolling four-quarter PE buyout EV/EBITDA multiple came in unchanged from Q2 2020 at 9.0x. Although valuations are unlikely to fall precipitously from current levels as the bulk of current PE dealmaking is occurring in sectors benefitting from the pandemic, such as technology, mission-critical B2B, and healthcare, it should be noted private equity is not monolithic, and valuations are extremely sector dependent. Assets in the aforementioned sectors have generally attracted full valuations, as they have taken cues from the public market's rapid recovery, which saw a plethora of corporate PE portfolios marked up. On the other hand, negatively affected pandemic sectors such as energy, hospitality, and travel will see multiples quickly fall should they come to market as significant challenges in valuing businesses arise. The difficulty here is trying to forecast when consumption or revenues will bounce to pre-pandemic levels. For some assets in these sectors the damage will be permanent, while for others it will be a short-term blip.

Incidentally, when the pandemic first hit, our COVID-19's Influence on the European PE Market analyst note addressed the potential of more lender-friendly structures coming to market via GPs putting more equity into transactions, lenders requiring tighter covenants, and exercising greater scrutiny of EBITDA add-backs. This dynamic played out in the third quarter with debt/EBITDA proportions falling to 3.6x, while sponsors' equity/EBITDA percentages increased to 5.4x. While the data suggests more lender-friendly structures are coming to market, we would hesitate to say it's widespread just yet, but it will be interesting to see how things play out in the coming quarters.

6: ''UK Set for Record-Breaking Economic Growth in Third Quarter, '' Financial Times, Chris Giles, 24 August 2020.
7: ''BoE Economist Warns Against Pessimism After Record Drop in GDP, '' Financial Times, Chris Giles and Valentina Romei, 30 September 2020.

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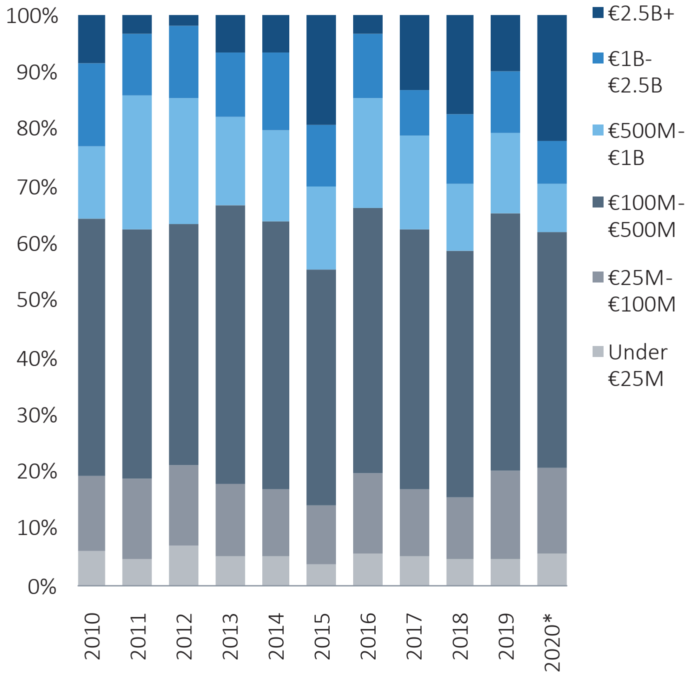
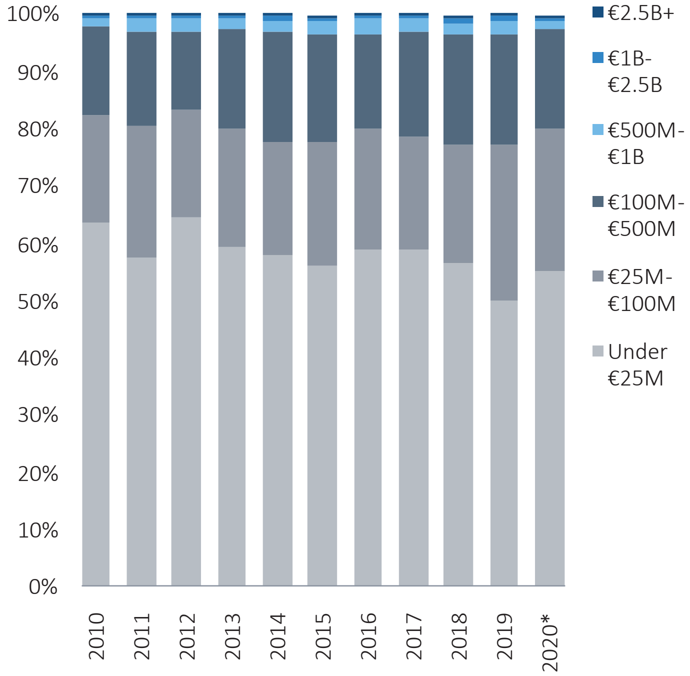
Deals by size and sector

PE deals (€) by size



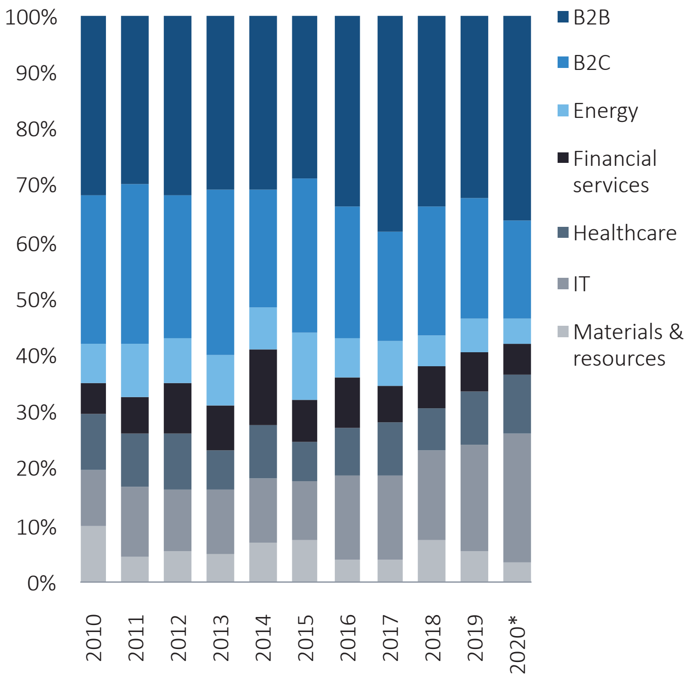
Source: PitchBook | **Geography:** Europe
*As of 30 September 2020

PE deals (#) by size



Source: PitchBook | **Geography:** Europe
*As of 30 September 2020

PE deals (€) by sector



Source: PitchBook | **Geography:** Europe
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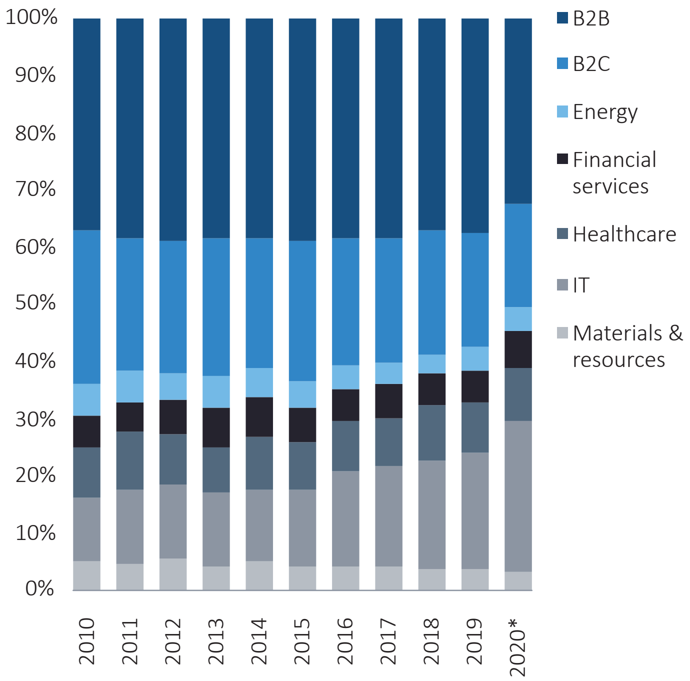
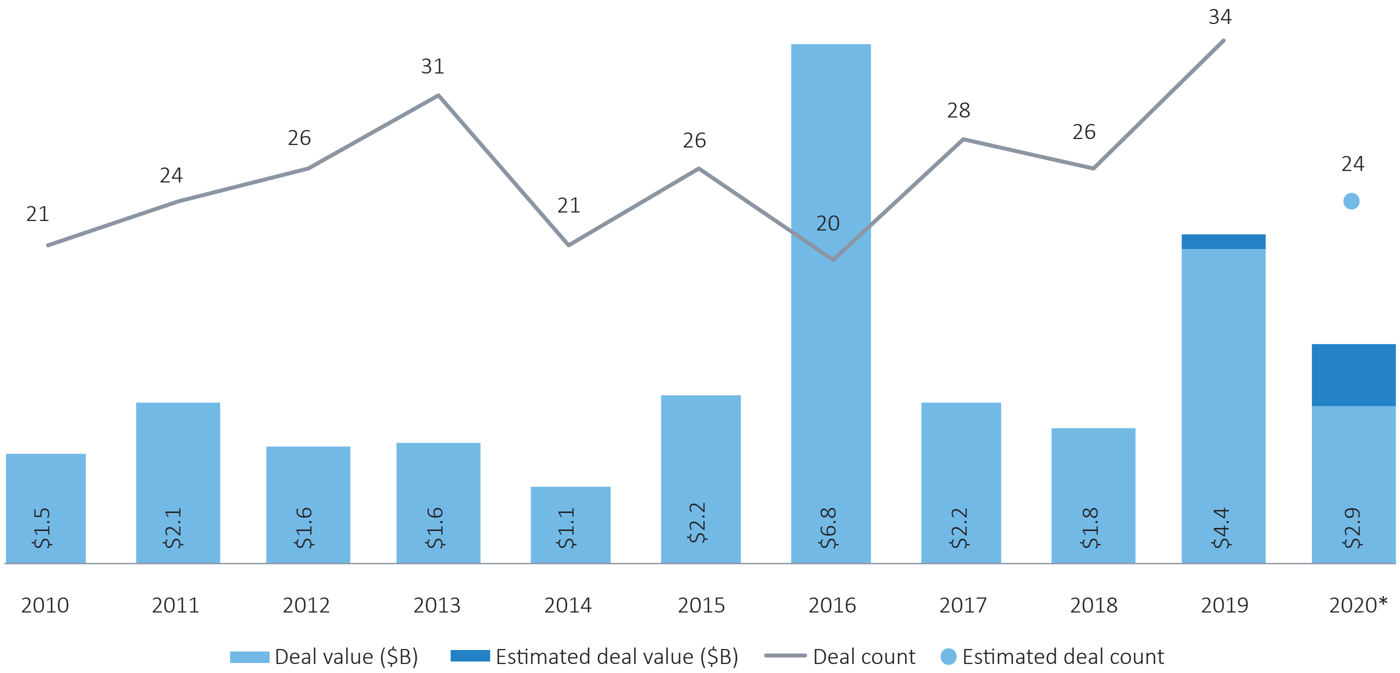
PE deals (#) by sector



Source: PitchBook | **Geography:** Europe
*As of 30 September 2020

Spotlight: Israel

PE deal activity



Source: PitchBook | **Geography:** Israel
*As of 30 June 2020

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Although PE deal activity in Israel is skewed towards micro, small, and mid-sized transactions that tend to come with a unique set of cultural challenges for non-Israeli investors, PE deal activity remained extremely resilient in H1 2020, posting its best H1 deal value and volume figures in over a decade. 24 transactions closed worth $2.9 billion in H1 2020—YoY increases of 48.3% and 16.2%, respectively. If dealmakers maintain this pace by year end, the region will have recorded its highest PE deal count and second-best deal value in over a decade.

Top five PE investor countries in the Israel region since 2015

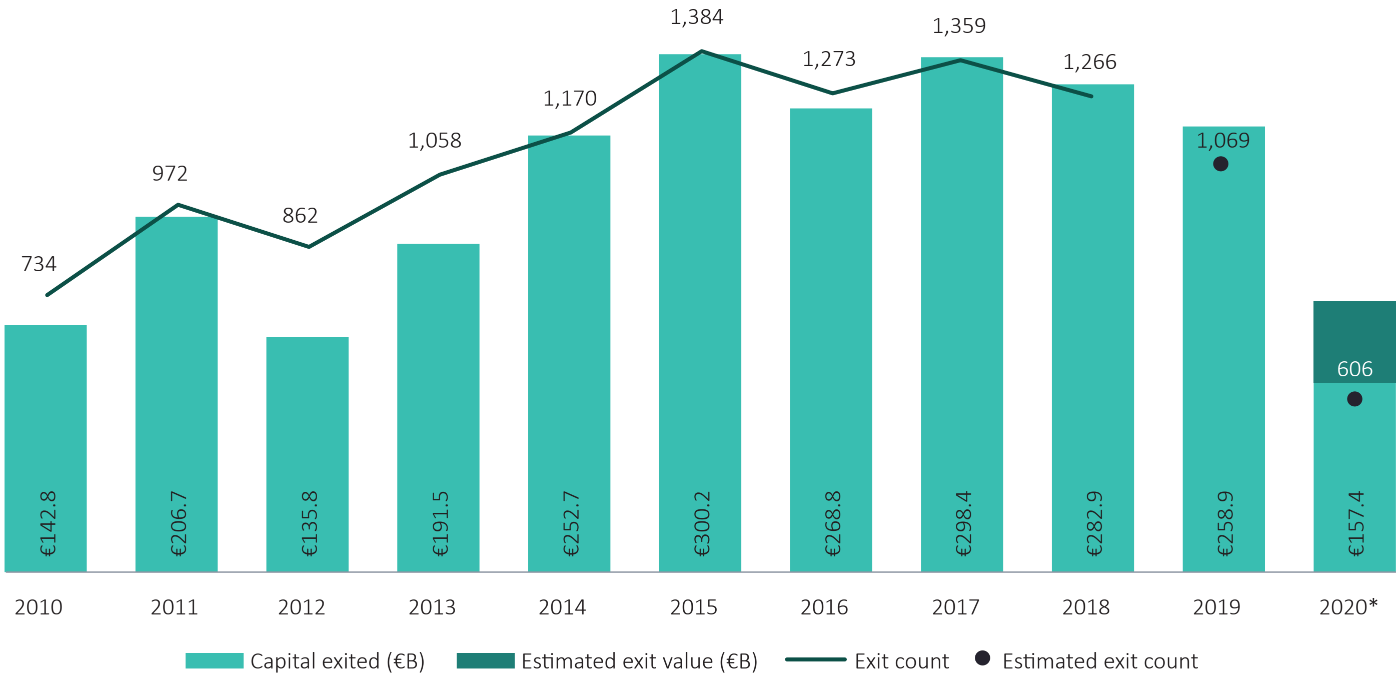
Investor country	Deals closed
United States	85
United Kingdom	20
China	16
Germany	7
France	6

Source: PitchBook
*As of 30 June 2020
Note: This table excludes Israel as an investor country.

While many deals that closed in H1 were negotiated pre-pandemic, the PE ecosystem in Israel is growing due to many factors. First, the region has benefitted from greater brand recognition in recent years, due in part to global players such as Barings Private Equity Asia, KKR, and Warburg Pincus executing high-profile transactions in the region. Investors based outside of Israel, especially those in the US, have participated in a larger share of deals closed in the country in the past few years. Many Israel-based companies focus on generating revenues overseas, and more often than not, the US is the first economy they look to penetrate, which has helped spur US investor interest. In addition, foreign GPs, such as those from the US are typically willing to write bigger cheques than domestic GPs for local assets, due in part to record dry powder levels and significant scale across their PE platforms. Second, Israel's domestic PE scene, which includes groups such as FIMI Opportunity Funds and Fortissimo Capital—both of which have approximately north of $1.0 billion in AUM—has also contributed to its emerging PE ecosystem. Company founders, management teams, and boards in the region are increasingly comfortable and receptive to PE's value proposition. And third, international LPs are becoming more comfortable allocating capital to hard-to-reach regions such as Israel, due to the no-interest-rate environment and the diversification benefits funds in the region bring. High cultural and geographic barriers to entry make penetrating the Israel market difficult for those foreign GPs without a robust PE infrastructure or established network.

Exits

PE exit activity

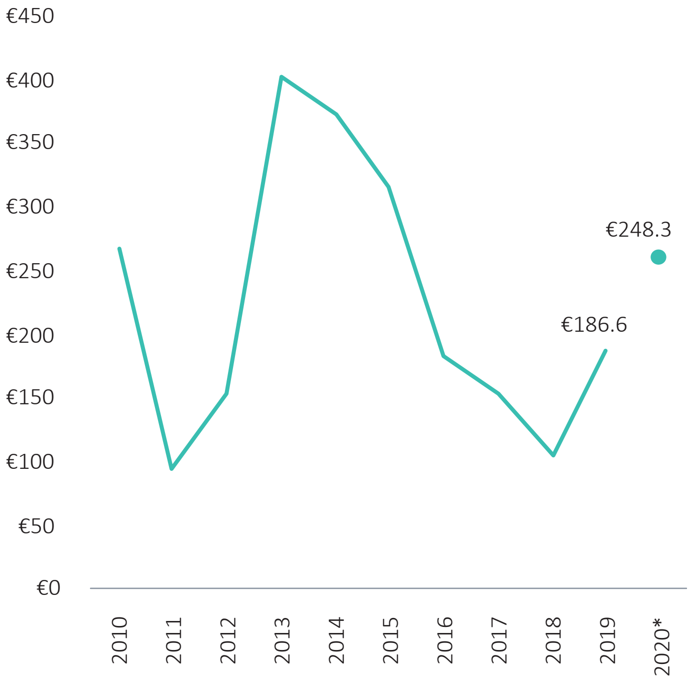


Source: PitchBook | **Geography:** Europe
*As of 30 September 2020

Contrary to what we observed in deals, exit activity in Q3 2020 remained largely stale from the previous quarter. The third quarter saw 181 liquidity events worth €58.1 billion close—QoQ increases of 6.9% and 1.9%, respectively. However, on an annual basis exit count is pacing towards a ten year low, and the severe declines in exit value and volume were palpable—accounting for YoY decreases of 35.0% and 36.5%, respectively. We expect realization activity to be slow through the remainder of 2020 because sellers are likely to be extremely cautious about exiting positions during such volatile periods, as buyers tend to mark to market a lot quicker than sellers during market gyrations. Until a sense of normalcy resumes, and valuations bounce across PE portfolios, sponsors will avoid liquidity events unless assets are distressed, meaning longer hold periods, more GP-led secondaries, and fewer distributions. For example, on its most recent earnings call, EQT stated exits will be delayed until valuations across its PE portfolio reach 1.7x -1.8x gross multiple on invested capital (MOIC). This dynamic in the exit market will lower carry income for GPs in 2020 while considerably boosting AUM.

The booming public equity markets, which have whole-heartedly embraced central bank and government stimuli, have enhanced sponsors'

Median IPO exit size (€M)

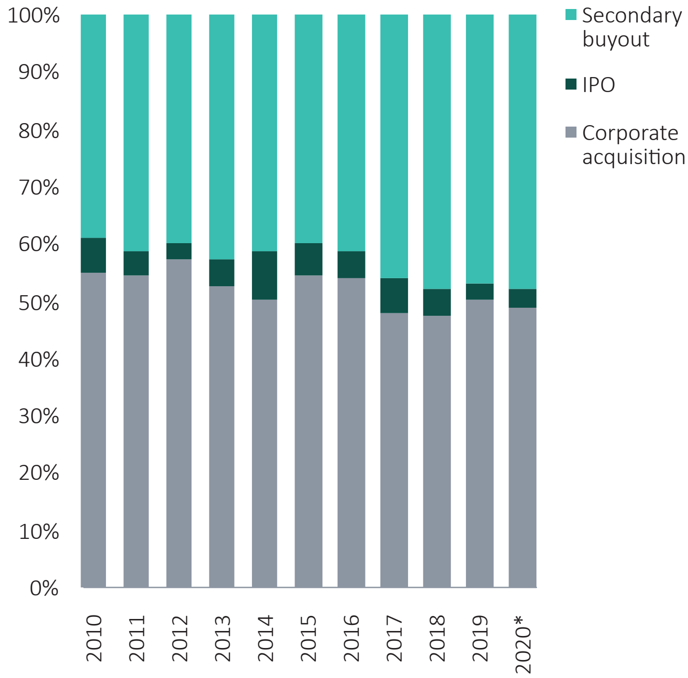


Source: PitchBook | **Geography:** Europe
*As of 30 September 2020

desire to exit portfolio companies through a listing. Fourteen European IPOs worth €22.0 billion (pre-money valuation) closed YTD, already surpassing 2019's full-year exit value total with less than half its IPO count. In the largest exit of Q3 2020, UK-based e-commerce company The Hut Group (LON: THG) raised €2.1 billion on the London Stock Exchange at a pre-money valuation of €5.0 billion. This was the LSE's largest listing by market capitalization since Royal Mail's debut in 2013. KKR has taken advantage of the buoyant public markets by exiting its entire stake. The group's shares increased 30% in its first day of trading, as institutional investors' insatiable appetite for technology assets continues. BlackRock (BLK: NYSE), Janus Henderson (JHG: NYSE), and the Qatar Investment Authority were among the first three cornerstone investors. Despite the group's indicated market value making it eligible to join the FTSE 100 as a premium listing, the company will not be included in the blue-chip index for a few reasons, including red flags in terms of corporate governance, supermajority voting power via dual share classes, and dual chairperson and CEO roles. Founder friendly terms have become the norm with many startups, as founders tend to play a critical role in the organization's story. Many analysts don't expect this to be much of a concern with the Hut Group, as the founder was a crucial part of the company's rise to the public markets.

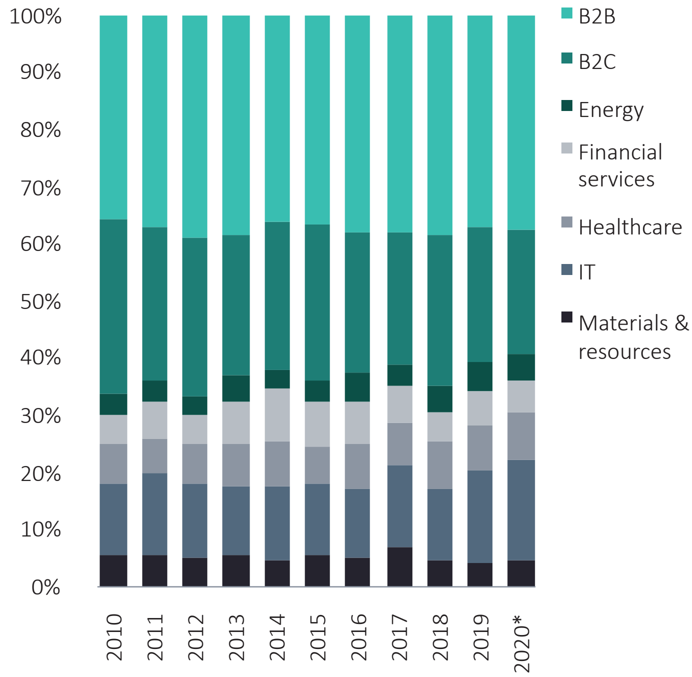
SBOs drove much of the exit value and volume in the quarter. With record dry powder levels in the market and many ageing PE portfolios after ten years of strong dealmaking, sponsors are finding value in offloading assets to competitors. Contrary to popular belief, the data suggests PE-owned assets still have room for further value creation even after being owned by a PE group for several years. In a normal 3- to 5-year holding period, sponsors typically deploy one or two value creation strategies, which allows room for the next acquirer to add further value. In the largest SBO of the quarter, France-based Galileo Global Education was acquired by a consortium of investors including Montagu and CPPIB for €2.5 billion. The acquiring consortium will work to expand Galileo's higher education presence in new markets, as well as enhance subjects and specializations they offer to higher education students globally.

PE exits (#) by type



Source: PitchBook | **Geography:** Europe
*As of 30 September 2020

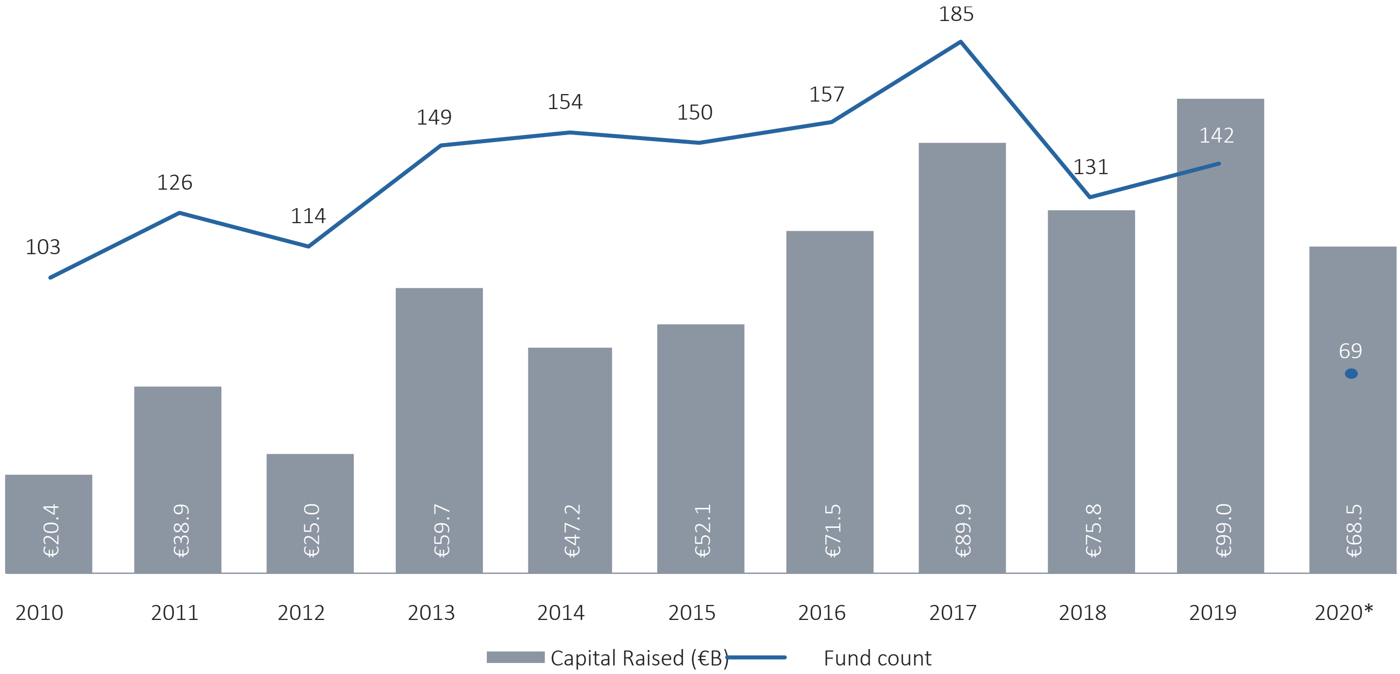
PE exits (#) by sector



Source: PitchBook | **Geography:** Europe
*As of 30 September 2020

Fundraising

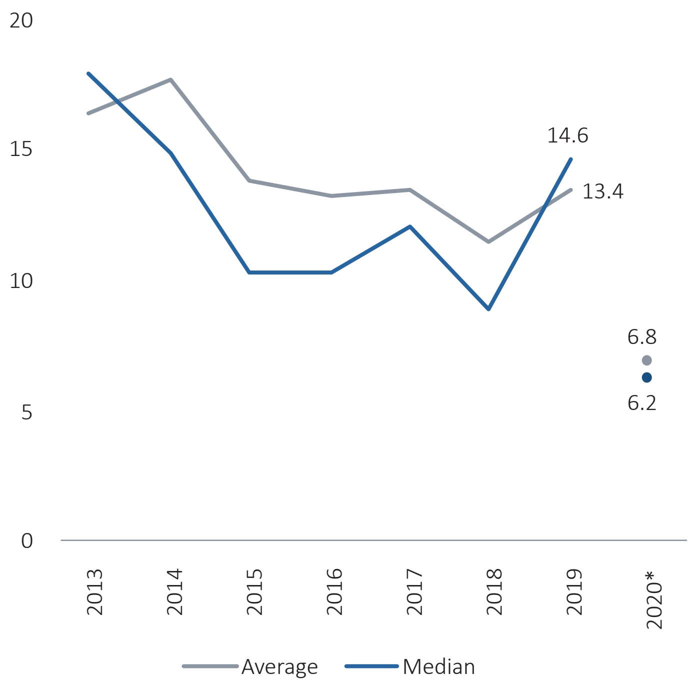
PE fundraising activity



Source: PitchBook | **Geography:** Europe
*As of 30 September 2020

PE fundraising activity came roaring back in the third quarter, posting healthy figures and further accelerating the bifurcation in the market. 69 funds held a final close worth a combined €68.5 billion, putting 2020 on pace to surpass €90 billion in fundraising—its second highest total in a decade. Despite challenges posed by the pandemic to business travel, and therefore onsite due diligence, LPs continue to consolidate GP relationships and commit more capital virtually to their most trusted, well-resourced, and experienced managers. The largest and most established managers have attracted considerable sums through the downturn at breakneck pace, with approximately 80% of all capital raised in 2020 coming from funds sized above €1 billion. For example, CVC Capital Partners closed on €21.3 billion for CVC Capital Partners Fund VIII, the largest-ever European buyout fund. CVC started fundraising in January 2020 and closed the fund in seven months, as LPs persist in trading liquidity for higher yields in this no-interest environment, which has boosted demand for riskier assets. Additionally, we saw Nordic Capital raise €6.1 billion for Nordic Capital Fund X in six months, surpassing its initial €5 billion target. The fund was launched in April 2020, and was raised entirely remotely through the pandemic, without face-to-face-meetings. We feel the PE fundraising process for experienced managers will remain predominately remote even when the pandemic abates, as LPs and GPs realize digital fundraising works.

Median and average closing times for funds sized above €1B



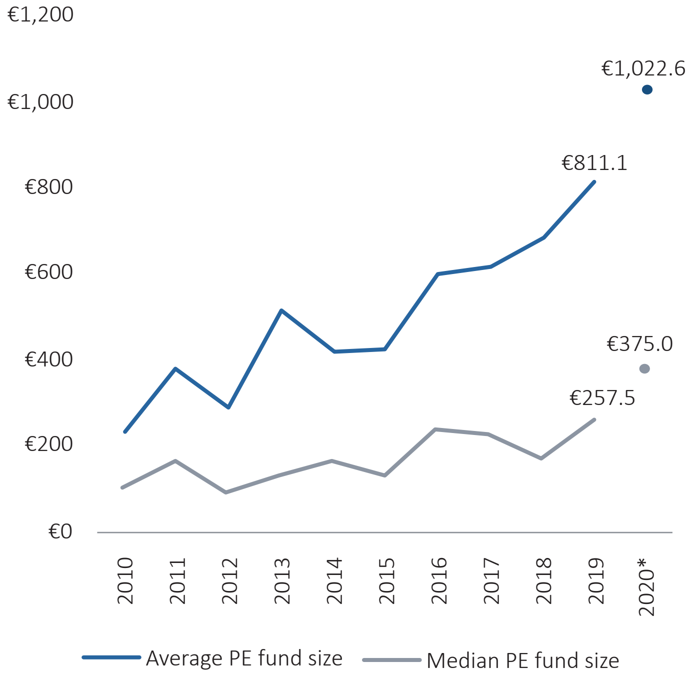
Source: PitchBook | **Geography:** Europe
*As of 30 September 2020
**Some years have low data counts.

Despite the lofty capital-raised numbers, fund count is pacing towards a new annual nadir in 2020. The less-established GPs are finding the transition to online difficult because LPs rarely make commitments to riskier emerging managers without onsite due diligence and/or face-to-face meetings. In addition, the pandemic has made LP underwriting standards more conservative, which makes allocations to less-experienced GPs harder to secure. Funds sized under €100 million have only accounted for 16.4% of fund count in 2020, pacing noticeably lower than funds sized between €1 billion and €5 billion, which have contributed 22.4%. If this pace is maintained through the remainder of 2020, it will be the first time in over a decade such a difference between the counts of the two fund sizes has occurred.

However, PE always has room for new injections of energy, ideas, and strategies, which bodes well for first-time funds and less-experienced managers. There has never been a more favorable environment for disruptive strategies that are ideally positioned to benefit from the pandemic to come to market. LP euros will always flow to market opportunities, whether offline or online, and we saw this with Kester Capital II, which closed €99.4 million over a nine-month fundraising period. The fund was oversubscribed and benefited from the use of a placement agent. This is Kester's second fund, and it will invest in UK small- and medium-sized enterprises (SMEs) that require institutional capital for the first time and are in the TMT, healthcare, and financial services sectors. There remains considerable upside potential to investing in SMEs during the COVID-19 crisis, as entities here don't have access to the large government and central bank stimuli, and liquidity bridges put in place since March likely won't last long enough, and this is where private capital steps in. Kester Capital II will focus on entities that need injections of equity to either quicken growth to take advantage of the dislocation or to build defensive capital for fundamentally strong businesses to ride out the volatility.

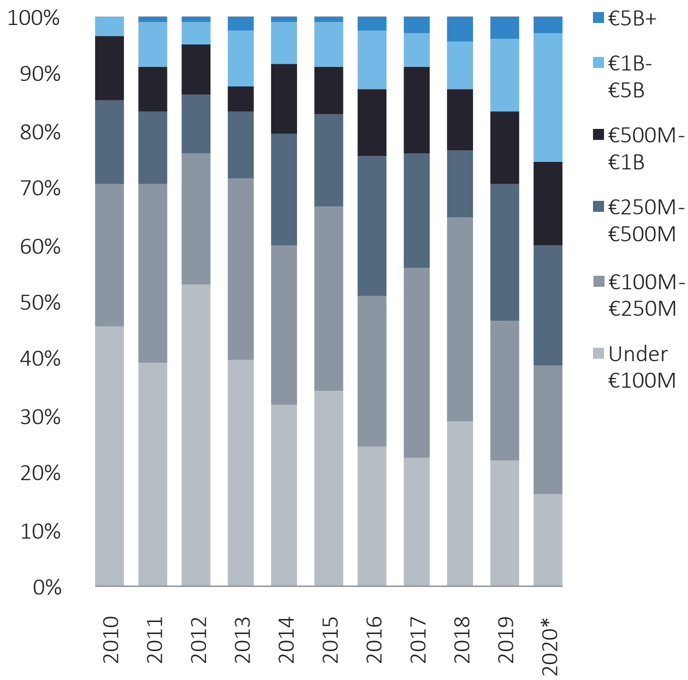
In the US, special purpose acquisition companies (SPACs, or blank-check companies) have become an attractive option to both exit portfolio companies and raise capital beyond the traditional closed-end commingled PE funds, as noted in our 2020 SPAC Frenzy analyst note; however, they have not caught on in Europe yet. Some key structural differences in the markets make SPACs less favourable in Europe. Primarily, shareholders have greater influence over any deal in the US because they are able to vote on an acquisition target and have the option to redeem shares should they not approve. In the UK, shareholders are prohibited from these actions, which heightens certainty of execution for sponsors but makes fundraising challenging as allocators prefer to have a

Average and median PE fund sizes (€M)



Source: PitchBook | **Geography:** Europe
*As of 30 September 2020

Funds by size (#)

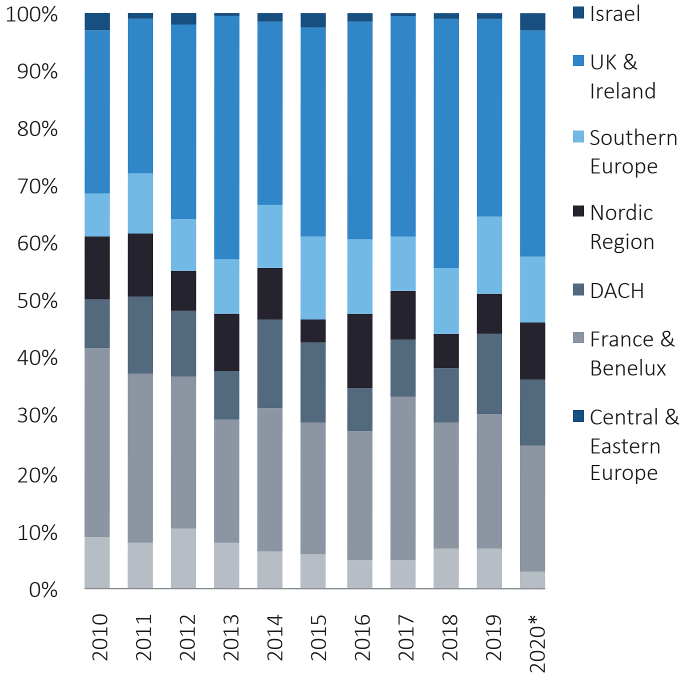


Source: PitchBook | **Geography:** Europe
*As of 30 September 2020

say in the acquisition target and the ability to walk away should they not like the deal. In theory, investors in a UK SPAC could be tied indefinitely into a transaction they do not support. In addition, the US has a deeper and wider pool of capital, with a proven model in which investors believe, and this makes fundraising for SPACs more attainable. That being said, an experienced and high-profile European team with a compelling pipeline of targets could buck this trend. For example, experienced SPAC sponsor Martin Franklin is planning to raise €750.0 million to list a SPAC known as Harvester Holdings on the London Stock Exchange. The SPAC will focus on acquiring an entity that makes the bulk of its revenues in North America. Martin actually prefers the UK structure as investors cannot redeem shares once committed to the vehicle. This provides advantages when competing for targets, as assurances around financing the deal without risk can confidently be made.

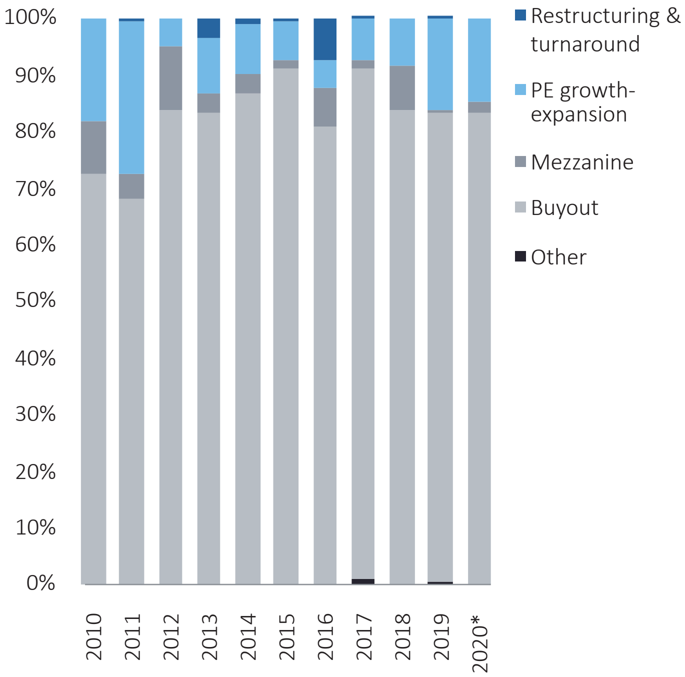
Breaking down activity via region shows the UK & Ireland continued to account for the lion's share of capital raised and fund count proportions, accounting for 66.6% and 39.1%, respectively, with London dominating fund locations. Buyout funds contributed close to 80% of fund closings while growth funds accounted for the remaining percentage. A large headwind for the fundraising landscape in the region is the looming hard Brexit cloud. Potentially rife consequences for UK-domiciled funds, IR teams, and placement agents without an EU presence linger, as outlined in our Post-Brexit Domiciling of European PE Funds analyst note. It will be interesting to see how fundraising proportions play out in the region post the 31 December transition period. Nonetheless, we still did see several impressive buyout funds close in the region, including Hg Capital's €4.4 billion close for Hg Genesis 9. The fund will target European mid-market software and technology companies with enterprise values between €500.0 million and €1.5 billion. Hg also closed its third lower-mid-market fund Mercury 3 this year at €1.3 billion. Furthermore, Hg is in the market with its second large-cap fund, Hg Saturn 2, which is targeted at €4.4 billion and is expected to close by year end. The closing of Hg Saturn 2 would mark a record €10.1 billion raised in 2020 for the group and once again underscores the healthy fundraising trail brand-name European managers are experiencing.

Funds by region (#)



Source: PitchBook | **Geography:** Europe
*As of 30 September 2020

PE fundraising (€) by type



Source: PitchBook | **Geography:** Europe
*As of 30 September 2020