

M&A

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Accelerating UK bid activity

A classic indicator of a disconnect between short-term concerns and longer-term opportunity is when non-equity investors start to buy the assets. This is clearly happening, with 10 bids for FTSE 250 companies progressing currently. This is unsurprising given the de-rating of the FTSE 250, with the overall index -18% YTD and 80% of the members down on the year. This has driven heightened interest from overseas and private buyers. There have been 14 proposed and announced bids in the past six weeks, adding up to £21bn of equity value. This should help to replenish cash positions for hard-pressed equity investors.

Bid activity accelerating

There have been 20 announced and possible bids so far this year with an equity value of £26bn (based on M&A activity with >£100m equity value). After a slow start to the year, there has been an acceleration in the past few weeks. This reflects lower valuations, greater potential for deal completion and the scale of dry powder in private equity.

Focus on FTSE 250

The main activity has been in the FTSE 250 with 10 bids, compared to five in the FTSE SmallCap and four in the AIM. They are spread across Transport (four), Support Services and Real Estate (three each), Healthcare and Retail (two) and one each in Energy, Financials, Housebuilders, Media, Oil & Gas and Retail. There have been eight financial buyers, nine corporate, and three family. Looking at the location of the bidders, 11 are from overseas and nine are domestic.

The majority of the transactions are likely to complete, though some may fall away. For instance, FirstGroup, THG and Mediclinic have all rejected their respective bids. Countryside Properties has rejected its proposed offer, but has announced a formal sale process.

Themes to consider

The pace has clearly accelerated after a slow start. There is a clear focus on hard assets, with most of the businesses being acquired having strong market positions with clear and lasting cash flow credentials. The mix of financial and corporate buyers reflects the strength of balance sheets, access to funding, and the ability to look through a tough economic environment. Weaker sterling should also increase the appetite from overseas.

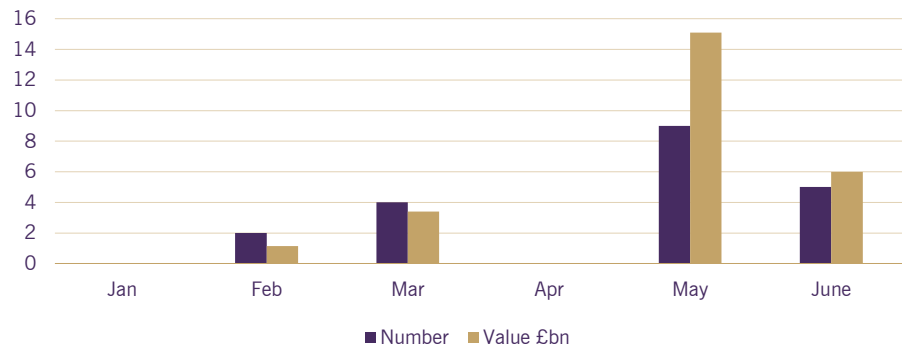
Increased cash for investors

The recent market malaise is driven by the worsening economic outlook, rapid escalation in inflation and rising interest rate expectations. This has been exacerbated by higher redemptions from equity funds, particularly those focused on the mid & small cap markets and growth orientated. Given the environment and the redemptions, fund managers have chosen/needed to hold higher cash balances, resulting in them being net sellers of the market.

The increase in M&A provides some respite from this trend, particularly as there is limited demand for funding currently, with a dearth of IPOs and few material equity raises. The following chart shows the value and number of announced and proposed offers per month.

Chart 1: Number and value per month

Source: Peel Hunt



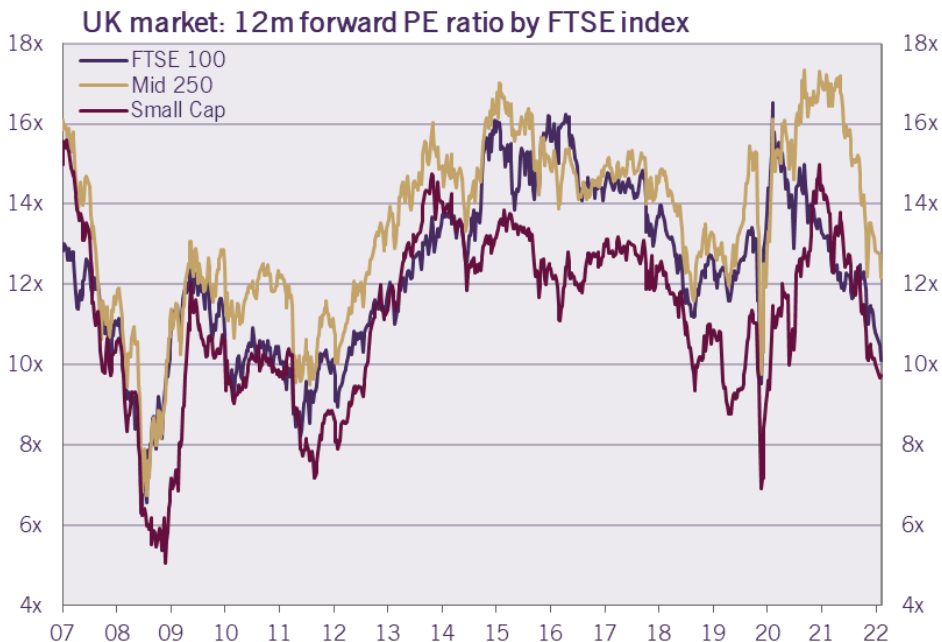
The UK mid & small cap – an undervalued market?

The FTSE 250 is currently trading on a PE of 12.5x, which compares to 16x for the S&P, 11x for the Russell 2000 (ex loss makers) and 12x for the Euro Stoxx 600. So the index looks cheap vs the S&P, but is broadly in line with the Russell 2000 and Stoxx 600. However, it is important to remember that the UK market has a very global make up with >50% of sales generated ex-UK. It is no wonder that UK businesses are attractive to a broad number of acquirors, with the FTSE 250 a particular focus given the greater dynamism among the constituents, as well as being a manageable size.

The following chart shows the drop in rating of the FTSE 250 from a peak of c.17x, and that it is now trading at close to a 10-year low.

Chart 2: PE ratios by index

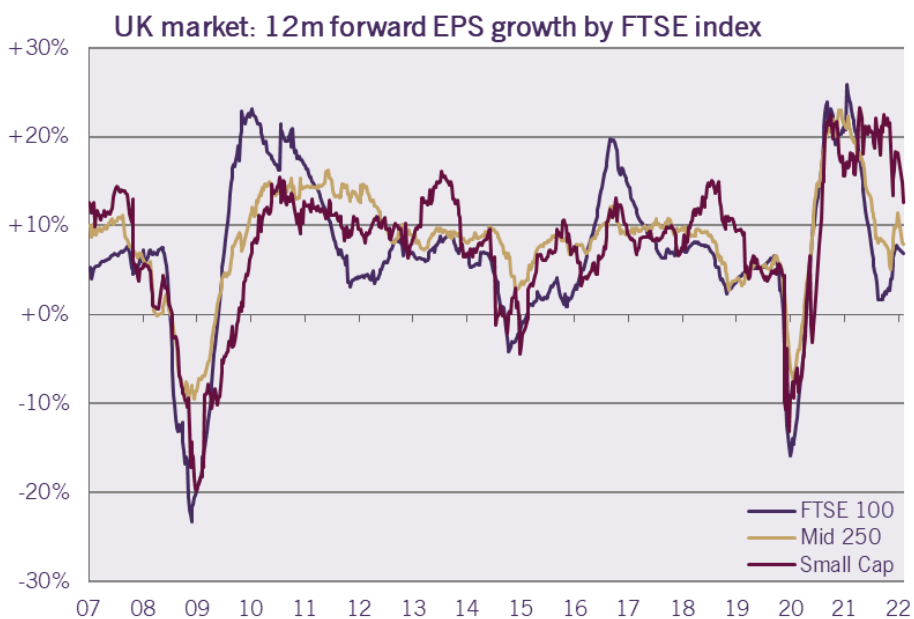
Source: Refinitiv Datastream



It seems inevitable that bids among the FTSE SmallCap will also increase given that the PE rating has now dropped to sub-10x. The following chart shows the forecast EPS growth per index, which has started to tail off as the economic outlook has worsened.

Chart 3: EPS growth per index

Source: Refinitiv Datastream



Clearly forecasts will continue to be pulled back, so some of the rating decline is reflecting that expectation. Nonetheless, the markets must now be tempting for a long-term investor.

Current M&A transactions

The following table shows the proposed and announced transactions during 2022 valued at over £100m.

Table 1: Current M&A transactions

Source: Peel Hunt

Company	Offeror	Index	Sector	Equity value £bn	Payment	Announced
McKay Securities	Workspace	FTSE SmallCap	Real Estate	0.3	Cash & shares	03-Feb
Clipper Logistics	GXO Logistics	FTSE 250	Transport	0.9	Cash	28-Feb
CareTech	Sheikh Holdings	AIM	Healthcare	0.8	Cash	07-Mar
Stagecoach	DWS	FTSE SmallCap	Transport	0.6	Cash	09-Mar
Brewin Dolphin	RBC	FTSE 250	Financials	1.5	Cash	31-Mar
John Menzies# (Restricted)	Agility Public Warehouses	FTSE SmallCap	Support Services	0.5	Cash	30-Mar
Shaftesbury (Restricted)	Capco# (Restricted)	FTSE 250	Real Estate	2.3	Shares	05-May
Ideagen	HG Capital	AIM	Technology	1.0	Cash	09-May
Secure Income REIT (Restricted)	LXI REIT# (Restricted)	AIM	Real Estate	1.5	Shares	11-May
ContourGlobal	KKR	FTSE 250	Energy	1.7	Cash	16-May
Countryside Partnership	Inclusive Capital	FTSE 250	Builders	1.4	Cash	17-May
HomeServe	Brookfield Asset Management	FTSE 250	Support Services	3.9	Cash	19-May
THG	Belerion / Candy Ventures	N/A	Retail	2.0	Cash	19-May
M&C Saatchi	Next 15	AIM	Media	0.3	Cash & shares	20-May
FirstGroup	I Squared	FTSE 250	Transport	1.0	Cash	26-May
Capricorn Energy (Restricted)	Tullow Oil (Restricted)	FTSE 250	Oil & Gas	0.7	Shares	01-Jun
Ted Baker	Unnamed	FTSE SmallCap	Retail	0.2	n/a	07-Jun
Biffa	Energy Capital Partners	FTSE 250	Support Services	1.3	Cash	07-Jun
Mediclinic	Remgro & SAS	FTSE 250	Healthcare	3.2	Cash	09-Jun
Go Ahead# (Restricted)	Kinetic & Globalvia	FTSE SmallCap	Transport	0.6	Cash	13-Jun
Total				25.7		

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