# Pradip Somaia – Regent Evolution

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Pradip Somaia, partner at Regent Evolution, outlines the current trends in EMEA merger and acquisition (M&A) activity for the technology, media and telecoms sector (TMT).

## M&A in EMEA channels: drivers, valuations and trends

The European TMT landscape for Mergers and Acquisitions has seen much turbulence in the last four years.

As the world emerged from lockdown, the market responded with a record numbers of deals announced in Q4 2020. 2021 saw the number of IPO's more than double. A contributory factor was the rise of the SPAC – Special Purpose Acquisition Vehicles – that saw financial investment firms roll up businesses and launch them on the public markets.

But what comes up must come down and the declining number of IPOs was most painfully felt in 2023 when there were only 12 IPOs announced in the European TMT sector.

External factors, mainly the war in Ukraine, rising inflation and energy costs, depressed transaction volumes in 2022 but the TMT sector fared better than other industries, recording only a 7% drop in transactions. The UK TMT sector continues to battle wider macroeconomic pressures and this negative sentiment was reflected in deal volumes during 2023.

2024 has seen a recovery with total deal value in the first three months of 2024 recording the highest since the second quarter of 2022, according to S&P Global Market Intelligence 451 Research.

M&A activity in the TMT sector this year is being driven by strategic buyers and continues to weather the storms of economic volatility. Various factors are driving strategic buyers back to the deal table, including improving equity values, including the regulatory environment and the ongoing demand for digital transformation and technological advancement.

Whilst the sector is sensitive to volatility in bank rates, which has resulted in a 'valuation gap' between buyers and sellers, the need to deploy capital in order to pursue strategic acquisitions is expected to result in an increase in transaction volumes and in deal values during 2024.

The ICT channel continues to adapt to the growing demand from consumers for new technology. This started with the move from desktop to laptop computers, progressed further with the move from basic mobile phones to smart phones and the introduction of tablets. The latest trend has been the surge in consumer demand for wearable technology in the form of smart watches and health monitors.

While these new and evolving markets create huge opportunities, they are not without risk. A sudden change in fashion that can beset distributors who need to be able to provide the latest technology but run the risk of losing a significant revenue stream. Potentially being left with unwanted stock if a new product range emerges or a manufacturer withdraws from a market or is acquired.

The emergence of new technologies emphasises the need for value added services and technology skills in the channel. Thus, enabling the distributors to help the manufactures enter the market and to help the retailers or resellers to maximise the sales potential. The demand for value added services and new product lines is therefore becoming an important driver in M&A in the channel to increase the economies of scale, improve profit margins and rapidly build expertise.

## Valuation

The valuation of any business depends on many factors but the primary one is usually the underlying profit of the business. In particular the earnings before interest, tax, depreciation and amortisation (EBITDA) is a frequently used measure. Most businesses are valued in the region of 6 to 10 times EBITDA although the spread can be wider depending on the sub sector. The actual multiple within this range depends on other factors such as size, growth and reputation or brand awareness.

A secondary valuation measure is the multiple of price to sales (PS) which can act as a guide to what would be a reasonable earnings multiple. For example, a 5% EBITDA margin implies a PS in the range of 0.25 to 0.4 which is typical of a low margin distributor. However, for EBITDA margins of 20%, the implied PS range would be in the region of 1 to 1.6 which is more typical of value added resellers or system integrators. Selective M&A provides a means to increase the underlying profitability and also improve the profit margin by acquiring scale and higher margin business such as value added services.

Regent Evolution, with over 30 years' experience advising clients in Growth Sectors, particularly TMT, Healthcare, Industrial and Support Services and Renewables, has completed many deals in this space. The company presents its latest views and analysis on M&A deals at numerous events.

Pradip Somaia, Partner

Regent Assay (www.regentevolution.com)

Email: psomaia@regentevolution.com

Mob: +44 (0) 7785 316 584