Pradip Somaia: Regent Assay

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Pradip Somaia, partner at Regent Assay, 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

European TMT M&A activity increased by 46% in terms of the total number of deals announced. There were 5,240 deals announced in 2021, which is a new record high, compared with 3,584 in 2020. The number of European TMT companies making an IPO was erratic during the year, but overall the total number of IPOs reached a peak of 422 in 2021, up from 135 in 2020.

The ICT channel is 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 Assay, 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.

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