PRIVATE EQUITY SPECIALISTS: THE BDO TEAM

BDO's Private Equity group is a highly collaborative network of more than 300 experienced advisers from all disciplines across the firm including audit, tax, M&A, transaction services and corporate advisory. This practical team has a profound understanding of the Private Equity industry, particularly in the mid-market. Our people are part of the process at every level, interacting with funds, advising on deals, and working closely with portfolio companies to help them realise their goals.

BDO is the home of the entrepreneur. Over the last three years we've worked with:

>700 Private Equity backed companies

We audit **>350** Private Equity backed companies

We work with **>200** Private Equity houses

In 2016 we completed **243** deals worth **£11.7bn** **30%** of our deals involved Private Equity

Globally BDO's 2016 network revenues were **$7.6bn** generated by **68,000** people across **158** countries

The investments we've made in infrastructure, resources and talent mean that we offer a powerful combination of service, scale and expertise; and through our deep working relationship with each client we can focus on their unique needs and deliver practical individual solutions.

We've never lost our agility and personal approach. We understand the intense pressure that comes with the challenge of entrepreneurial growth, and we work strategically alongside our clients. Private Equity can offer huge rewards to businesses, but knowing how to manage it effectively makes all the difference. That's where our team comes to the fore.

WE WANT TO HEAR **FROM YOU**

The reasons for embarking on Private Equity investment may be complex, but whatever your motivation, we are searching for ambitious businesses to champion through this chapter and enhance future growth.

Contact **Julian Frost** on +44 (0)7775 705 543 for more information.
We look forward to meeting you and learning about your business.

FOR MORE INFORMATION:

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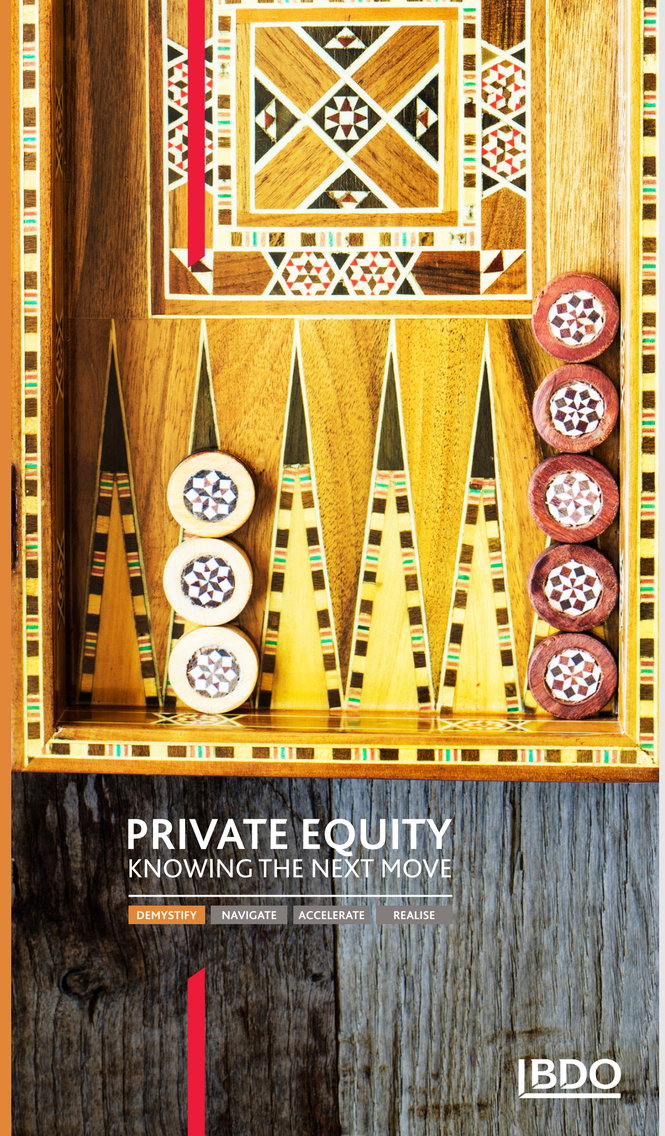


PRIVATE EQUITY
KNOWING THE NEXT MOVE

DEMYSTIFY | NAVIGATE | ACCELERATE | REALISE

BDO

BDO – DEMYSTIFY

Private Equity investment enables entrepreneurial businesses to expand at speed, and clears the way for skilled and ambitious people to step up a gear. If managed in the right way, Private Equity can be an exceptionally positive route to growth.

Using Private Equity should be a positive and exhilarating using experience especially for those doing it for the first time. It can help entrepreneurial businesses and their leaders professionalise, grow and achieve transformation in their business. In fact, taking on Private Equity can help an entrepreneur become more entrepreneurial.

Private Equity houses are often tarnished by the headlines of a rogue few, making it difficult for some entrepreneurs to distinguish fact from fiction. However, there are very few real predators out there looking for an opportunity to take advantage.

We believe there is a more balanced truth out there for those with a clear purpose, an ambition to embark on the next phase of growth and the stamina for this transformational change over a relative short period of time.

Deciding that Private Equity is the right choice and finding the right partner for our clients is very important to BDO. Our knowledge and understanding of this market is deep rooted in the heritage of our business. Through our relationships with and understanding of Private Equity, we help businesses assess the opportunity, avoid conflict and find the right solution for maximum effect.

As the home of the entrepreneur, we are founded on helping entrepreneurially-spirited clients along the whole life journey of their businesses and often a part of that is spent in the Private Equity world. We have years of relevant experience.

We help to dispel the big misconceptions and broaden knowledge of how Private Equity works so that decisions can be taken on an informed basis. Nothing is more important to us than our clients' success. We bring people together from across our business and our network to help our clients achieve their long term goals that goes beyond their immediate Private Equity ambitions.

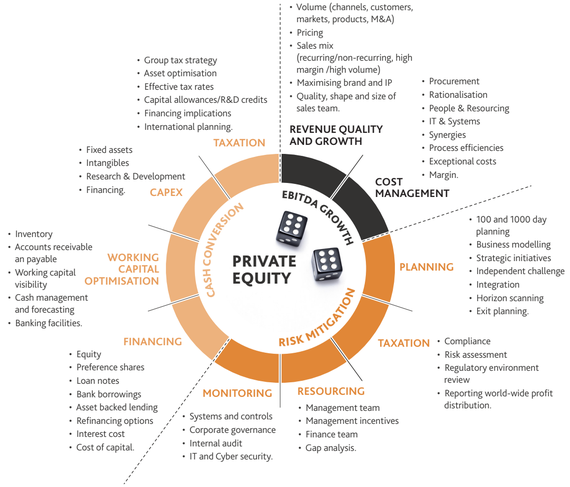
WHAT INVESTORS LOOK FOR

Private Equity houses actively manage businesses to improve efficiencies and drive value. This intense effort concludes in sale within an accelerated timeframe, when the gains are realised. As such, investors are looking to work with companies and their management teams with the greatest potential to increase the value of their equity. Businesses of particular interest may have the following characteristics:

- 01 RECURRING REVENUES
- 02 CONTRACTED REVENUES
- 03 DISRUPTORS
- 04 INTELLECTUAL PROPERTY
- 05 GROWTH
- 06 CASH GENERATIVE
- 07 STRONG MANAGEMENT TEAMS
- 08 SCALABILITY
- 09 SOMETHING THAT NEEDS FIXING

PRIVATE EQUITY
THE DRIVERS OF VALUE

In our experience, there are three areas which should be focused on in order to drive value and maximise your value. Some considerations in each of these areas are set out below:



91%

OF PEOPLE WHO HAVE BEEN PRIVATE EQUITY INVESTED WOULD RECOMMEND IT.

87%

SAW THEIR COMPANIES GROW UNDER PRIVATE EQUITY OWNERSHIP.

OVER THE PAST 10 YEARS

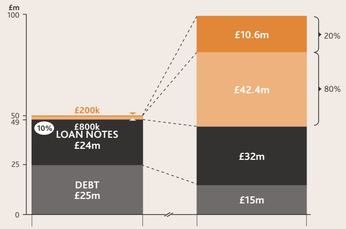
PRIVATE EQUITY BACKED BUSINESS HAVE RETURNED FOUR TIMES THE RETURN THE PUBLIC MARKETS WOULD HAVE RETURNED.

HOW PRIVATE EQUITY WORKS

PRIVATE EQUITY: THE ANATOMY OF A DEAL

Private Equity is the term used to describe various types of investments; management buy-outs, institutional buy-outs, leveraged buy-outs, venture capital and growth or development capital, provided in return for an equity stake in a potentially high growth business. The ultimate goal of Private Equity is to drive transformational growth during a relatively short period, typically 3-5 years, resulting in significant returns. To put a number on it, the normal PE rule of thumb metric is 'double your money in 3 years', although that metric is under pressure in current markets.

DRIVING VALUE INTO ORDINARY SHARES



	YEAR 0	YEAR 3
EBITDA	£5m	£10m
MULTIPLE	10x	10x
EV	£50m	£100m

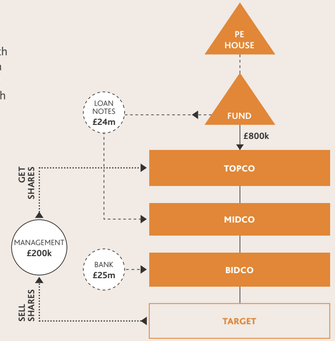
HOW PRIVATE EQUITY INVESTS

Buy-outs are largely funded by way of loans from the PE house and bank. The cash generated by the company is used to service and pay down these loans over time. The growth in value accrues to the ordinary shares of which management will typically hold a minority, say 10% to 20%. Management will have paid much less than 10% to 20% of the overall funding of the transaction (hence this is known as 'sweet equity').

Private Equity houses advise funds which provide finance for buy-out transactions. Additional funding is provided by third party banks and debt funds. Typically, a majority of funding is in the form of interest-bearing shareholder loans or preferred equity. The interest usually 'rolls up' into the principal and the whole lot has liquidation preference to (i.e. gets paid out before) the ordinary equity. The buy-out almost always involves the creation of a number of new holding companies.

As time progresses and the business and EBITDA grows, bank debt is paid off or amortised and enterprise value increases, driving value into the ordinary shares, provided that the value growth outstrips the cost of debt.

TYPICAL STRUCTURE



ALIGNMENT

Most entrepreneurial management teams are well aware of the importance of agenda alignment amongst the leaders of the business. This comes into sharp focus when a Private Equity investor joins the board. The investor agenda is likely to be simply to drive value. Altruistic objectives of management may not be shared by investors.

Real success in a relationship with Private Equity comes where there is significant alignment, and non-aligned factors can be clearly de-prioritised.

In our experience it is important to have absolute clarity about your own objectives and those of your team. Questions you might find it useful to pose include:

- What is your definition of success for yourself over the medium & long term?
- What is your definition of success for your business over the same period?
- What are you looking for from Private Equity? How much do you really know?
- What alternatives are there?
- What are your 'non-negotiables'?
- How could your business (safely) grow faster?
- Could you cope with sharing control of your business?
- Who will you eventually hand the business over to?

We typically help business owners to identify and prioritise their objectives and understand how they can be aligned with those of the Private Equity investor.

WHERE WE HELP

We bring value in two areas. Firstly, we have a vast wealth of experience to bring to bear for our clients considering Private Equity. Secondly, we care that our clients have a positive experience with Private Equity.

In our experience:

- Most scenarios can be modelled
- Most legal constructions have been seen before
- Most tax issues and structures have been encountered elsewhere already
- Most behaviours can be predicted.

Therefore, taking on Private Equity is, in some ways, a process. It is a particularly complex and intricate process, but a process nonetheless. In other words, it is a 'tame problem'.

GLOSSARY

Auction	A process in which an investment bank or other corporate finance adviser invites several Private Equity houses to look at a particular company that is for sale and to offer a bid to buy it.
BIMBO	Buy-in-management-buyout. A combination of a management buy-in (MBI) and a management buy-out (MBO).
Capital Markets	A marketplace in which long-term capital is raised by industry and commerce, the government and local authorities. Stock exchanges are part of capital markets.
Carried Interest	An entitlement accruing to an investment fund's management company or individual members of the fund management team. Carried interest becomes payable once the investors have achieved repayment of their original investment in the fund plus a defined hurdle rate.
Conditions precedent	Certain conditions that a Private Equity firm may insist are satisfied before a deal is complete.
Covenants	An agreement by a company to perform or to abstain from certain activities during a certain time period. Covenants usually remain in force for the full duration of the time a Private Equity investor holds a stated amount of securities and may terminate on the occurrence of a certain event such as public offering. Affirming covenants define acts which a company must perform and may include payment of taxes, insurance, maintenance of corporate existence etc. Negative covenants define acts which the company must not perform and can include the prohibition of mergers, sale or purchase of assets, issuing of securities etc.
LBO (Leveraged buy-out)	A buy-out in which the Newco's capital structure incorporates a level of debt, much of which is normally secured against the company's assets.
Management buy-in (MBI)	A buy-out in which external managers take over the company. Financing is provided to enable a manager or group of managers from outside the target company to buy into the company with the support of Private Equity investors. Where many of the non-managerial employees are included in the buy-out group it is called a management/employee buy-out (MEBO).
Management buy-out	A buy-out in which the target's management team acquires an existing product line or business from the vendor with the support of Private Equity investors.
Sweet Equity	An instrument in the form of options, performance rights, or rights to further shares that increase the value of management equity relative to other shareholders. Often issued at a lower price to motivate management with the incentive of a higher upside when objectives are achieved.
Institutional Buy-out	A buy-out initiated by institutional investors, such as Private Equity houses, where they take a controlling interest in the business.
Secondary Buy-out	A buy-out in which a Private Equity house sells control of a portfolio company to another Private Equity house.