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3PL 'super-powers' fuel the trend for PE deals

Today's financial pages are buzzing with reports on private equity deals. PE is growing, increasing in deal size, total annual investment and target sectors with records being broken each year.

Major blue chips, public companies and well-known household brands are all prey to PE deals. This growth is facilitated by ease of financing and the new appetite for highly leveraged deal-making against a backdrop of a sound euro economy and low interest rates.

According to the latest figures from the European Private Equity Venture Capital Association, a record €1bn was invested in over 7,500 European companies in 2006, up 51.2% on 2005. Such exponential growth and the high rates of return (averaging 10.8% since inception, with buyouts and venture capital returning 14.4% and 5.5% respectively, and some top-quarter buyout funds returning as much as 31%) has increased the pool of PE firms getting in on the act with a seemingly unquenchable thirst for new deals.

So where are the new opportunities? Sectors such as technology, pharmaceuticals, consumer goods and services industries have traditionally been popular. Increasingly, business and support services are being targeted, which raises interest in our sector, notwithstanding its relatively low margin yields.

There are two key drivers for interest in logistics and mechanical handling equipment (MHE). Firstly, the global economy is supported by logistics service providers, from smaller enterprises up to PLCs, and the volume of goods movement is fast increasing.

Secondly, manufacturers and suppliers are focusing on core competence, increasingly outsourcing non-core logistics activities.

Highly leveraged PE deals need security. Logistics scores again, often with asset-rich balance sheets on one hand, and secure constant cash flows on the other, each providing collateral for PE borrowings. The nuts and bolts of our

As private equity knocks at our industry's door, Jeremy Clarke advises would-be candidates and warns of potential pitfalls

sector - warehouses, tractor units, trailers, MHE, containers and ship assets, combined with long-term contractual service commitments - are commonplace. Even where the target's asset base is weak, the non-asset based performance of skilled management teams generating regular positive cash flows can provide a solid foundation for funding.

These considerations undoubtedly drove the recent acquisition of three UK port companies, ABP, P&O and PD Ports, as well as many other shipping, airport and air freight companies worldwide.

Globalisation and consolidation within supply chain operators has created 3PL "superpowers". These have inevitably become PE targets in their own right, fuelling the trend for third-party investment in the sector.

Niche 3PL operators or suppliers offer strategically-focused targets and lower risk.

Take specialised supply chain services for growth industries like construction, or home delivery services, where demand is supported by increasing numbers of on-line shoppers.

The buy-out of Nightfreight is a good example. Originally targeted by Barclays Private Equity in 2001 in a public-to-private MBO, by 2004 it was the subject of a secondary PE-backed MBO with funds provided by RBS Debt Ventures and Barclays Private Equity.

The emerging markets of India and China offer even greater growth potential for logistics investment. These economies are built on booming low-cost manufacture, necessitating state-of-the-art supply chains to move their products in and out of the country.

While the sector struggles to come to terms with government "environmentally friendly" policies, such initiatives fuel more investment opportunities. Increasingly, retailers and PLC manufacturers will look to work with "green" 3PLs. Those that can't change won't be on the tender list. So for some, investment now in carbon-friendly facilities, vehicles and technology will help secure the green-minded customers and their contracts for tomorrow.

PE is knocking at the industry's door. 3PL and innovative IT and MHE providers should gear-up to become targets and find investors. Solid asset bases, sound business plans, consistent cash flows, proven collaborative expertise all form the right platform for ownermanagers to fast-track their businesses' growth on the back of the substantial investments available from PE by improving facilities or investing in infrastructure and technology.

A word of warning: PE investors are hard taskmasters. Salary and incentive packages may be generous, but PE demands results, and quickly, exiting within three to five years and requiring an average annual ROI of between 17% and 30%.

But while the PE market has a reputation for demanding above-average returns, there is a huge variance between top and average performing PE funds. Only a few make exceptional returns, and those that do well, tend to do so consistently. So work with advisors who know the PE investor and can verify previous performance.

Will the bubble burst? PE deals are debtbased, so rises in interest rates aren't helpful.

But interest rate rises are more likely to slow growth than stop it. PE is, and remains, an opportunistic beast - ever seeking out a great business opportunity. And those opportunities keep being delivered. . .

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