GROUP

Capital Performance

Winter 2022

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MANAGING DIRECTOR
FINNCAP CAPITAL MARKETS
Stuart Andrews

Introduction

George Soros once said "markets are constantly in a state of uncertainty and flux and money is made by discounting the obvious and betting on the unexpected". If it is the case that there is always uncertainty, then it is also true that sometimes that uncertainty can seem more quantifiable than at others.

Whilst it might not feel like it, at the time of writing the VIX is at 21, compared to a level of circa 66 in March 2020 and circa 29 in November 2021, which reflects a degree of stability in comparison to the volatility we have seen in the markets since the first lockdown of March 2020. Whilst it seems as if there is a lot to be fearful about, the global fear index seems somewhat complacent at present.

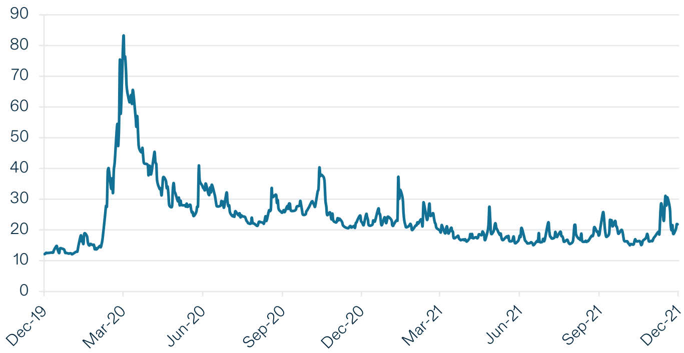
Before tackling where we are going and some bets on the unexpected, it is worthwhile looking back at 2021. In some ways we are back to the start with a return to home working, mask wearing and the need for more vaccines. Yet the year has seen a continued market recovery and a market that for the most part has been highly receptive to IPO's and secondaries, seen a resurgence of private equity buyers taking companies off market and has seen a large amount of private M&A activity. In many ways this was a continuation of the trends seen in the second half of 2020 with the only obvious sea change being the departure of the retail investor as people returned to work in May and June.

Continued page 2.

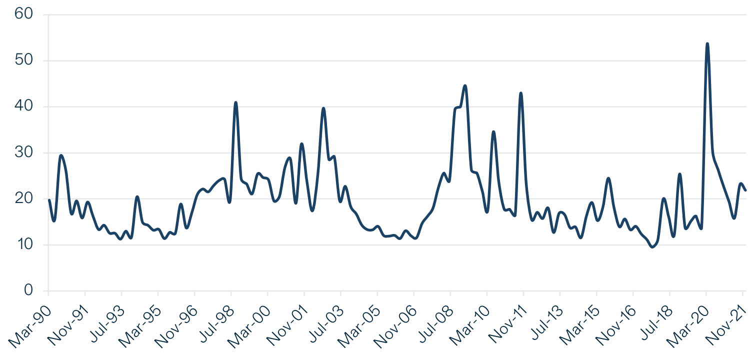
The information in this document is correct at the time of writing in December 2021.

Introduction Cont.

2 year VIX Index



All time VIX Index



Whilst markets have generally remained at or near a peak post Summer, the issuance market began to dry up in September as, predictably, the sheer volume of IPO's and secondaries ran into each other and concerns started to be aired over the continued robustness of the markets. Those concerns, that led to the increase in volatility in November, remain with us and act as the unresolved questions as we enter 2022.

The concerns centre on two opposing forces although both are a product of the establishments' response to Covid 19. On the one hand there are the inflationary effects of the considerable liquidity being provided by central banks and on the other the supply side shocks from a world economy awakening from its slumbers combined with labour shortages in core areas of the economy. With the former, the concern is whether the central banks response to inflation will be the correct one and with the latter there are the practical business implications that can cause erosion of equity value as businesses struggle with wage bills, transport costs, stock holding costs and how to effectively pass these rising costs on. It is a difficult area to manage and, just as these forces were being digested by the market, we now also have a new Covid variant to compound matters. The resolution of these issues will dominate the early months of 2022.

FTSE 250 Index

Introduction Cont.

Looking into the crystal ball, an immediate rate rise to tackle inflation looks much less likely (although still possible) as the implications of the economic impact of the response to Omicron are digested. Until we move from a position of ignorance to one of knowledge about the mutation, it is also unlikely there will be any resolution to the supply side issues either with government policy possibly exacerbating these issues. The obvious bets for an investor are therefore to steer clear of pubs and bars, hospitality, travel and the like and to hold the Covid cures, delivery companies and the previous lockdown winners. This was the playbook from March 2020 and is repeating now. However Mr. Soros instructed us to ignore the obvious and go for the unexpected.

So what is the market not expecting? In brief, an end to Covid as an issue in relatively short order. The risks of Omicron being highly disruptive is fully priced in alongside a lack of resolution to the supply side issues that confront the UK economy. The risk is therefore on the upside that Omicron does not cause severe issues and at the same time government measures introduced do not choke off the economy to any great degree. If this is the case then the supply side issues will work their way through accompanied by a modest increase in rates in the New Year. This is currently the unexpected, but on balance, possibly the most likely and therefore being long of the market and exposed to some Covid losers is perhaps no bad thing.

If this is the outcome then we can expect more settled conditions in UK markets next year with a return to a more normalised level of issuance which is likely to be skewed to environmental solutions, fast growing disruptive consumer stocks, tech enabled life sciences and artificial intelligence as this is where the growth is. If this is where issuance is then potentially the UK market can start the transition to something more forward looking and less reliant on old fashioned and, even in the FTSE 100, domestic companies. However to do this, all market participants need to educate themselves about the business of tomorrow before we discover that the UK market is a global backwater.

Capital Markets

CO-HEAD OF CORPORATE FINANCE
FINNCAP CAPITAL MARKETS

Christopher Raggett

In our last report we detailed the renaissance of the public markets as the venue of choice for ambitious companies seeking support or growth capital. The pandemic had proved that institutional investors were willing to act quickly to help management teams to ride out the crisis and subsequently to help fuel growth for companies new to the market. The upshot was a more fertile IPO market than we have seen for many a year but we wondered whether an oversupply of companies seeking capital would lead to fund managers exercising more caution over capital allocation for new issuances.

The last six months has certainly seen a lot of supply from companies keen to ride this wave of capital access and there have been 172 secondary issuances on the London Stock Exchange since 30 June raising an aggregate of £3.6bn. In addition, we have seen 60 IPOs raising over £6bn during the same period. These numbers alone would suggest that the capital markets remain open for business despite supply-chain and inflationary concerns covered elsewhere in this review. Yet there is a more cautious feel to the last six months as proved by a net selling of small cap funds in October, the first time this had happened in 15 months.

As ever, the statistics only tell half the story and we must rely on anecdotal evidence to get the full picture. While reports of the deals that have concluded seem to indicate that capital raises are still possible and investors are allocating funds to new businesses in their portfolio, the numbers don't show the transactions that don't get away. However, the business pages were rife in September and October with reports of pulled IPOs and struggling fundraises. In London, roofing specialist Marley and aviation stalwart Virgin Atlantic both pulled or postponed their planned public debuts while Eurowag and Marks Electrical both listed at the bottom end of their valuation ranges having raised less capital than they sought. We could list many others. In each case the companies and their advisers cited the "choppy" nature of the capital markets.

In truth, while there have been some modest fund redemptions and investors have sounded more cautious, the performance of the capital markets over the last six months do not point to "choppiness" but rather a fairly steady rate of growth. Since 30 June, the FTSE 100 and 250 have grown by 2.97 and 0.74 per cent. respectively.

Market sentiment or fundamental weakness is therefore not to blame. Rather it is fairly simple supply side economics – investors have had a wealth of choice over the last six months and have therefore been able to apply a gold-standard to their investment choices or drive prices down. We heard reports during November of over 20 IPOs marketing at the same time – not all of them could get away.

Some common themes do however emerge from the transactions that did conclude. There is a particular ESG-flavour to many of the completed IPOs of the last six months. At the end of November, finnCap acted as sole broker to two such issuances – Eneraqua and Gelion – both seeking to bring positive change to traditional industries. It is clear that the focus on investing for "good" is no longer marginalised or transient. Investors expect all of their portfolio companies to report on their environmental and social impact and are clearly favouring those that perform well on those metrics. We expect this trend to continue as public sentiment drives more responsible behaviours.

Consumer and technology businesses continue to thrive accounting for seven and 16 issuances on AIM respectively raising a total of over £900 million in aggregate. However, there is again evidence that investors are applying higher standards to their investments even in these high-growth areas –the tide turned against The Hut Group in H2 as its governance structure was deemed toxic as its returns slowed.

In summary though, the capital markets remain supportive for high-growth and positive-impact companies. But in a time when competition for capital is fierce, structure and timing will be key to success.

Plc Advisory

HEAD OF PLC STRATEGIC ADVISORY

FINNCAP CAPITAL MARKETS

Henrik Persson

It is a comfort, in a long period of variants and uncertainty, that at least one of my predictions as we entered 2021 – that of a high level of public takeovers and shareholder activism – has borne out to be true. Perhaps it was not the bravest call compared to 2020, but fascinating themes have emerged nonetheless.

To set the scene, at the time of writing in late December 2021, there had been 51 firm offers announced for LSE-listed companies, which is in line with the general long-term trend over the last decade. By comparison, there were 66 firm offers in 2019, a particularly busy year, but a limited fall to 40 offers during the exceptional year of 2020. We are proud to have been trusted to act on six of these transactions, of all shapes and sizes, in 2021 and four in 2020.

At the very least, given the number of transactions, it is clear therefore that the UK public markets host fundamentally attractive takeover targets but there are deeper observations:

- the proportion of firm offers with a value of greater than £1 billion (19 in 2021, approximately 40%) has risen markedly to be at least double the proportion in recent years, unusually also matching the number of smaller offers with a value less than £250m;
- private equity and financial sponsors were involved in almost two-thirds of these offers;
- approximately two-thirds of offers were by overseas bidders, a pattern consistent since at least the Brexit referendum, including a number of US private equity and/or in larger deals, and roughly half of the overall value of offers made were by North Americans;
- there was an exceptional number of public auctions and competitive situations, most famously that for Morrisons, where two different private equity firm consortia competed publicly over a “blockbuster” £7bn takeover.

The long-awaited increase in financial sponsor-led public-to-private transactions appears finally to be bearing out. The willingness of financial sponsors to put aside historical concerns around the risks and cost of public market transactions, and to do so on big ticket transactions, and sometimes in public competition with each other, highlights both that they are more comfortable with these concerns, but also that there are relative bargains or relatively gentler competition for these assets as compared to private or overseas markets.

It is perhaps understandable that private equity would target larger, more established, or otherwise derisked and/or potentially more readily geared targets at a time when financial firepower is readily available. One expects that midmarket financial sponsors will also increase their interest in public company transactions, having seen the offers launched by their larger or braver peers.

It has frequently been noted that whilst UK public markets are at near pre-pandemic levels and institutional shareholders remain supportive, broadly valuations lag overseas peers.

Equally, there has been a marked emboldening of investor activism after an understandable pause for much of 2020. Heightened ESG concerns and executive remuneration have increased as reasons for campaigning for change though, as ever, the classic thesis remains that superior value could be released by agitating for break-ups and management change. There has also been a number of situations where major shareholders have threatened or launched takeover offers.

Looking into the new year, there are very good grounds for expecting these patterns to continue: equity firepower and debt financing for transactions remains readily available; private equity remain hungry for deals; and opportunities will arise from the hangover from the tapering of financial stimulus and other state support. The currency advantage for overseas bidders continues, but in this respect, the extent and impact of newly-implemented national security legislation and increasing state intervention in foreign takeovers remains to be seen.

M&A activity

Against what perhaps the textbooks would have described should happen in a global pandemic, we have found ourselves in an M&A market achieving all-time records, surpassing $5 trillion in total global transactions. To put that into some perspective, the previous full year record sat at $4.2 trillion in 2015. The market still has the month of December to go, and early estimates point to a very active closing month of the year!

It is fair to say this has been a year like no other, and closer to home, the UK has been the third most active territory, behind the US and China, as highlighted in the chart below.

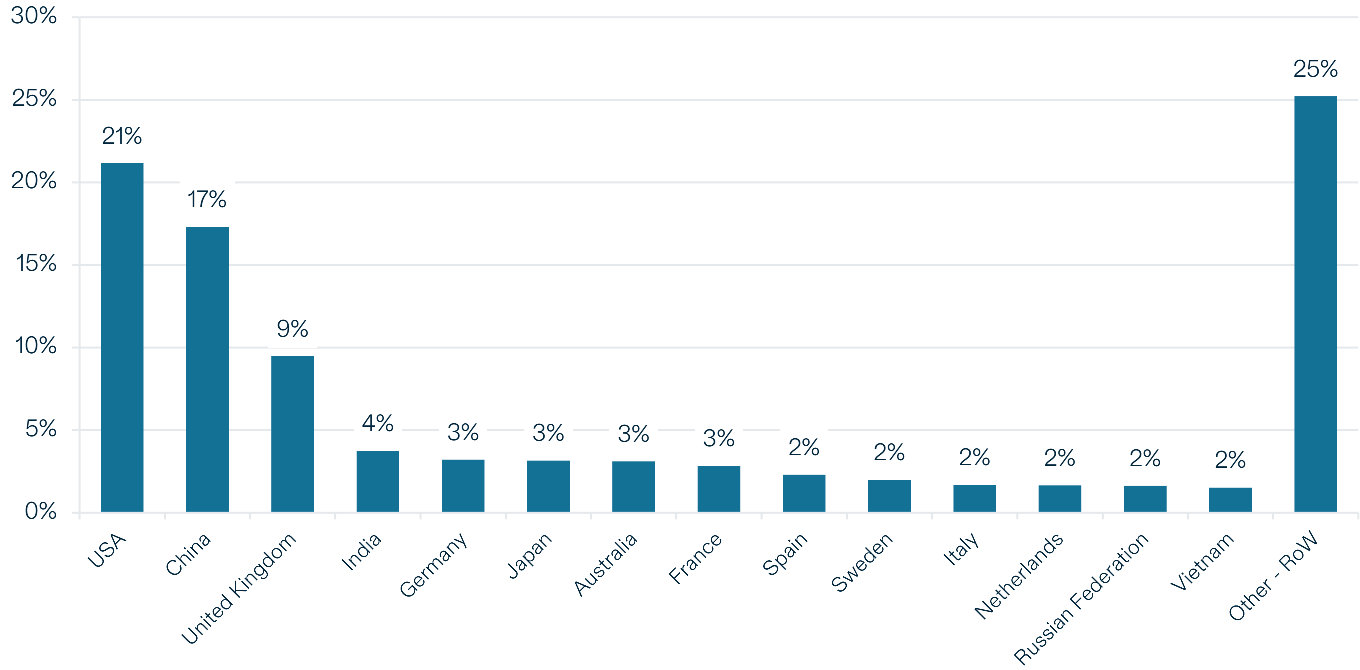
Looking ahead to 2022, the third year of the Covid-19 pandemic, the debate within the UK deal community is what transaction activity will look like. Despite the pandemic wearing on, the ingredients of capital availability, improving market conditions and financial market enthusiasm, coupled with dealmaking appetite (whether stable or distressed) look set to contribute to a continuation of the deal frenzy.

MANAGING PARTNER

FINNCAP CAVENDISH

John Farrugia

2021 M&A Deal Activity - by Country



Source: Zephyr 2021

M&A activity Cont.

UK M&A trends to look for in 2022:

1. Private Equity Activity

   The supply of private equity capital sits at an all-time high, with many funds still behind their 'target deployment' rate, due to early investment reservations and uncertainty at the beginning stages of Covid-19. 2022 will see private equity continuing to contribute to a significant proportion of deal volume, with strategies supporting both new target investments and buy and build.

2. Environmental, Social and Governance ("ESG") Measurement

   2021 saw more of a focus on ESG criteria within a transaction than ever before, and this will certainly continue into 2022 and beyond. Measuring ESG criteria will become the 'new normal' within investment considerations, and deal activity is expected to see increased due diligence being carved out specifically for this area.

3. Due Diligence Environment

   As well as increases in ESG specific due diligence, traditional due diligence activity will challenge the aftermath of COVID-19 more than ever. As more time passes from the beginning of the pandemic, more data points become available for comparison. These datapoints will drive calculations as to what levels of profitability is 'sustainable' going forward and highlight what was or wasn't exceptional profit or loss due to Covid-19.

4. Continued Technology Highlights

   Covid-19 turbo charged a reliance on digital consumption and the importance of connectivity. This was reflected in deal activity, with one in five investments in 2021 falling within the technology sector. Technology touch points will continue to connect deal activity across varying sectors in 2022 and beyond, with premium valuations, driven by competition, set to continue for established market leaders.

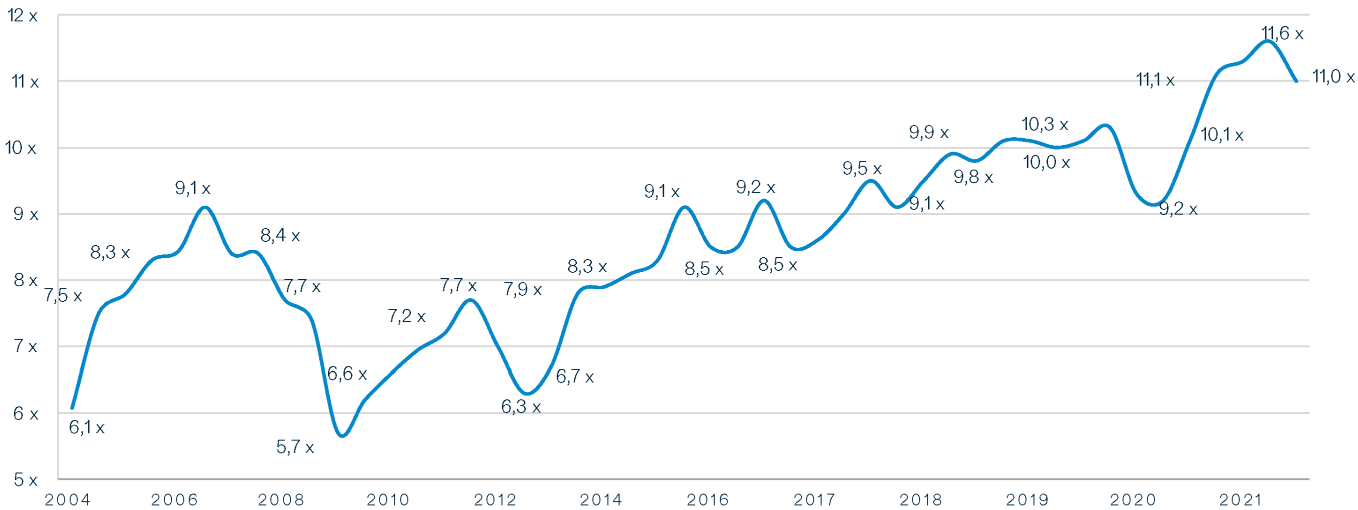
The year ahead will continue to be an uncertain and perhaps unprecedented one, yet the key ingredients are there for another flurry of significant M&A activity.

Global M&A

Global M&A activity is on track for a record year. In the first three quarters of 2021, a total of 18,736 deals were agreed with an aggregate value of almost US$4.3 trillion, increases of 47% and 122% respectively on the same period in 2020. This is a phenomenal performance when one considers the dark days at the height of the COVID-19 crisis in Q2 2020, with much of the world in lockdown. The strong activity levels have fed into deal pricing with the average multiples which acquirers are prepared (or being forced by market conditions) to pay at record levels. The chart below shows deal pricing trends in the European market, but this is indicative of global trends.

PARTNER
FINNCAP CAVENDISH
Peter Gray

Argos index® mid-market
Median EV/EBITDA multiple on a six-month rolling basis



Source : Argos Index® mid-market / Epsilon Research

Looking forward to 2022, the big question is whether the stellar performance of the market is sustainable. In that regard, there are considerable grounds for optimism.

Most of the current drivers of the M&A market are not going away any time soon. On some estimates, there is some $7trillion of private equity dry powder looking to be deployed globally. In addition, corporate acquirers have strong balance sheets and are under pressure to deploy cash piles from shareholders in a low interest rate environment.

SPACS have also been a considerable driver of M&A activity. As at the end of October, in the US alone, over 450 SPACS had listed raising some £140bn to target acquisitions, eclipsing the comparable figures for 2020 (Source: Statista2021). SPACS now appear to represent a permanent feature of the market rather than a passing fad with the UK, admittedly somewhat late to the party, having recently seen the announcement of its first SPAC, sponsored by Hambro Perks. The appetite of banks and debt funds to support PE and corporate acquirers in their pursuit of M&A targets remains extremely strong.

Global M&A Cont.

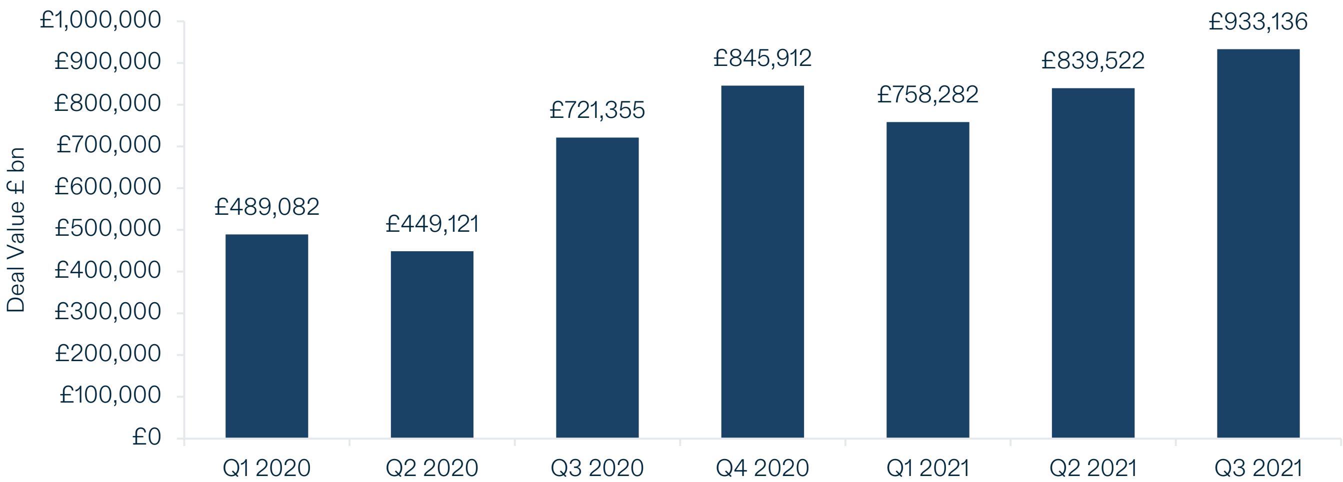
Finally, predictions for growth of the global economy in 2022 remain robust, the recent emergence of the Omicron notwithstanding. The OECD's current prediction is for economic growth of 4.5% for 2022 compared to a predicted 5.6% this year.

As ever, the market is not risk free. With Central Banks now waking up to inflationary pressures around the world (in large measure reflecting persistent supply chain issues), the direction of travel for interest rates is up albeit as yet not sufficiently so to put a major dent in activity levels.

The COVID-19 pandemic is far from over and notwithstanding the success of vaccines in reducing perceived risks, it is impossible to discount the possibility of even more deadly strains emerging. Political risks persist in terms of the uncertainties surrounding the US/China political axis and the Soviet Union's expansionary agenda.

Nonetheless, the M&A boom shows no sign of running out of steam and looks set for another bumper year in 2022.

Global Deal Value Quarterly 2020-2021



Source: Zephyr 2021

Oaklins: finnCap's access to the global M&A market

finnCap Cavendish is proud to be a member of Oaklins, the global investment bank with offices in some 45 countries around the world.

In a year when all global M&A records are set to be broken, it is little surprise that Oaklins looks set to smash all records in terms of both the value and volume of deals on which Oaklins has advised in the last 12 months. Oaklins will comfortably top the 400 M&A deal mark this year (compared to c368 deals in 2020) of which around 25% have been cross border transactions. Total deal value will be in excess of US$5bn and includes the US$1.84bn tender offer for Italian financial services firm Cerved Group where our Italian colleagues acted for a consortium of investors from Ireland, Singapore and elsewhere.

It has not just been M&A transactions in which Oaklins has had a buoyant year. It has also been boom times for ECM with Oaklins offices around the world. Oaklins Debt Advisory and fundraising teams have also had a stellar year.

Other Oaklins highlights this year include the more than doubling of the size of Oaklins Italian office and the strengthening of Oaklins presence in the Brazilian market.

Here in the UK, we have closed 12 cross border deals, a number of which have involved transactions where the ultimate buyer has been introduced to us by other Oaklins offices.

Debt Advisory

PARTNER, DEBT ADVISORY

FINNCAP GROUP

Graham Cooke

As we look back over the past twelve months, we should not overlook the general economic recovery during 2021 where the UK economy recorded its second consecutive quarter of growth in Q3. Brexit and Covid related issues continue to impact businesses with importers and exporters hit hardest. Supply chain challenges, rising raw material costs and labour availability top the list of key issues businesses are facing right now. That said, traditional indicators for businesses have started to stabilise and they have generally returned to trading more normally compared to twelve months ago.

Therefore demand for emergency liquidity support has been more subdued compared to 2020, when lenders were extending the government backed loan schemes. With government backed loans offering capital repayment holidays for the first twelve months, 2021 has now seen businesses starting to meet their repayment obligations. Utilisation of the schemes has been substantially reduced and therefore businesses have started to once again look at strategic growth investment. Pleasingly this has seen an increase in 2021 for the debt financing of specific M&A transactions and general liquidity for future buy and build strategies. Whilst admittedly this has been a cautious return to more forward looking investment with economic uncertainty and headwinds still prevalent, postponing strategic investment decisions has become less common.

We have seen the evidence of these trends in our own activity within finnCap Debt Advisory in a busy 2021. For example, we supported two public clients in expanding their existing bank facilities with Ideagen shifting from a £50m bilateral facility to a £75m two bank club and iomart refinancing an existing £80m bilateral facility into a new £100m four bank club. Both companies have clear growth agendas and enlarged debt facilities form a key part of delivering these strategies. Similarly, we have seen increased appetite from private equity after a prior year focussed primarily on existing portfolio companies and COVID's impact on their underlying business models. A positive development for the PE market has been the appetite amongst all lenders to support their activity and interesting to note how some lenders are adapting their core offering to provide more flexible options to PE borrowers. During the year, we worked with EPIC Investment Partners as they acquired Rayware with the support of Tosca Debt Capital who provided a second lien facility (outside of their core unitranche product) alongside senior debt from Clydesdale Bank. We anticipate continued strong appetite from lenders to support acquisitive businesses, whether they are UK domiciled or overseas businesses looking to expand into the UK. For example, we worked alongside US investor Cortland on its acquisition of property management company Qdime, as the Group looks to expand its global footprint and they were delighted by the strong appetite of UK banks and funds to support the acquisition.

We have been to delighted to help these and our other clients along with their respective management teams and investors. Going forward, whilst the continued economic recovery will not be straight forward, our discussions with lenders of all types indicates appetite overall remains positive and therefore capital should be available for businesses to continue to balance their own recovery with future strategic growth investment.

Two other thoughts to end. First of all, the tremendous amount of work undertaken last year by clients, lenders and lawyers combined, to execute the smooth transition away from LIBOR by 31st December as the main interest rate benchmark, to alternative risk free reference rates. This will hopefully be time well spent for existing borrowers and one easier job to come for new borrowers. Secondly and consistent with a wider context, I am sure we will only see the increased prominence of ESG in the debt markets this year. Sustainable finance continues to be of rapidly growing importance given increasing demand from regulators and investors alike. In our recent discussions with lenders, it is clear that lending decisions and strategies going forward will have even more emphasis placed in this high profile area.

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Delivering your business ambition

finnCap Group provides strategic advisory and capital raising services to companies.

We are mid-market specialists dedicated to providing the highest quality service to our clients both private and public.

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Our specialist sector knowledge and entrepreneurial approach helps companies to achieve their ambition.

IN THE BUSINESS OF TOMORROW

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