NautaDutilh Belgium's Private Equity & Venture Capital Barometer Q1 2018

This is NautaDutilh Belgium's fourteenth Private Equity & Venture Capital Barometer. After our spring 2014 Interim Report, we decided to survey, on a quarterly basis, a select group of private equity and venture capital players, asking about current and expected trends in their practice. This issue shares highlighted results from the first quarter of 2018 (Q1 2018).

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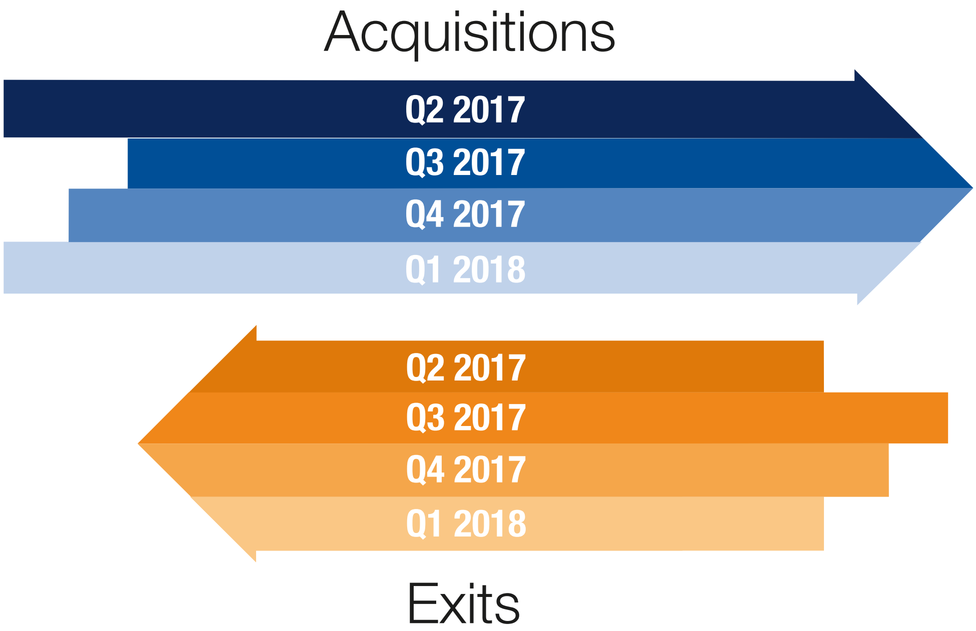
The Q1 2017 Barometer refers to NautaDutilh Belgium's tenth Private Equity & Venture Capital Barometer, available at
https://www.nautadutilh.com/siteassets/documents/brussels/barometerbelgiumq1_2017_a4.pdf
The Q2 2017 Barometer refers to NautaDutilh Belgium's eleventh Private Equity & Venture Capital Barometer, available at
https://www.nautadutilh.com/globalassets/barometerbelgiumq2_2017_a4.pdf
The Q3 2017 Barometer refers to NautaDutilh Belgium's twelfth Private Equity & Venture Capital Barometer, available at
https://www.nautadutilh.com/siteassets/documents/brussels/barometerbelgiumq3_2017_a4.pdf
The Q4 2017 Barometer refers to NautaDutilh Belgium's thirteenth Private Equity & Venture Capital Barometer, available at
https://www.nautadutilh.com/globalassets/barometerbelgiumq4_2017_a4.pdf

Exits now account for 41% of reported transactions



Until this past quarter, exits had been rising steadily, from 28% of reported transactions in Q4 2016 to 45% in Q4 2017. As these figures indicate, however, exits still lagged behind acquisitions by 5%. Indeed, according to our barometers, acquisitions have exceeded exits since Q4 2015. Somewhat surprisingly, the Q1 2018 figures revealed a drop in the number of exits to 41%, suggesting that PE players are in an acquisition phase. Furthermore, in reality, it appears that the percentage of acquisitions is even higher, as a substantial number of reported exits relate to secondary buyouts, meaning the target company is sold between private equity players.

One possible explanation for this trend is that PE players are now seeking to invest following a number of advantageous exits in the preceding year. Indeed, in 2017, exits rose from 32% of reported transactions in Q1 to 49% in Q3. Another (partial) explanation is that a number of closed-end funds came to an end, and their investors may prefer to realise a capital gain rather than reinvest the proceeds straight away, as multiples are increasing due to high seller expectations.

In our practice, we continue to see high multiples, meaning that under current market conditions, sellers can often obtain high prices for their assets. Another interesting fact is that PE players are increasingly not disclosing in their press releases the amounts offered/received (reserving this information for shareholders).

The foregoing finding is confirmed by PitchBook's *2018 PE Crystal Ball Report*,[1] in which respondents cite high transaction multiples and deal sourcing issues/lack of quality assets as the most important challenges facing PE dealmakers in 2018. Given the substantial amounts of dry powder available and low interest rates, access to financing was considered least important.

[1] The full report is available at https://files.pitchbook.com/website/files/pdf/PitchBook_2018_PE_Crystal_Ball_Report.pdf?pdf=repromote

Sectors with the most PE/VC activity[2] - the technology and IT sector is still hot

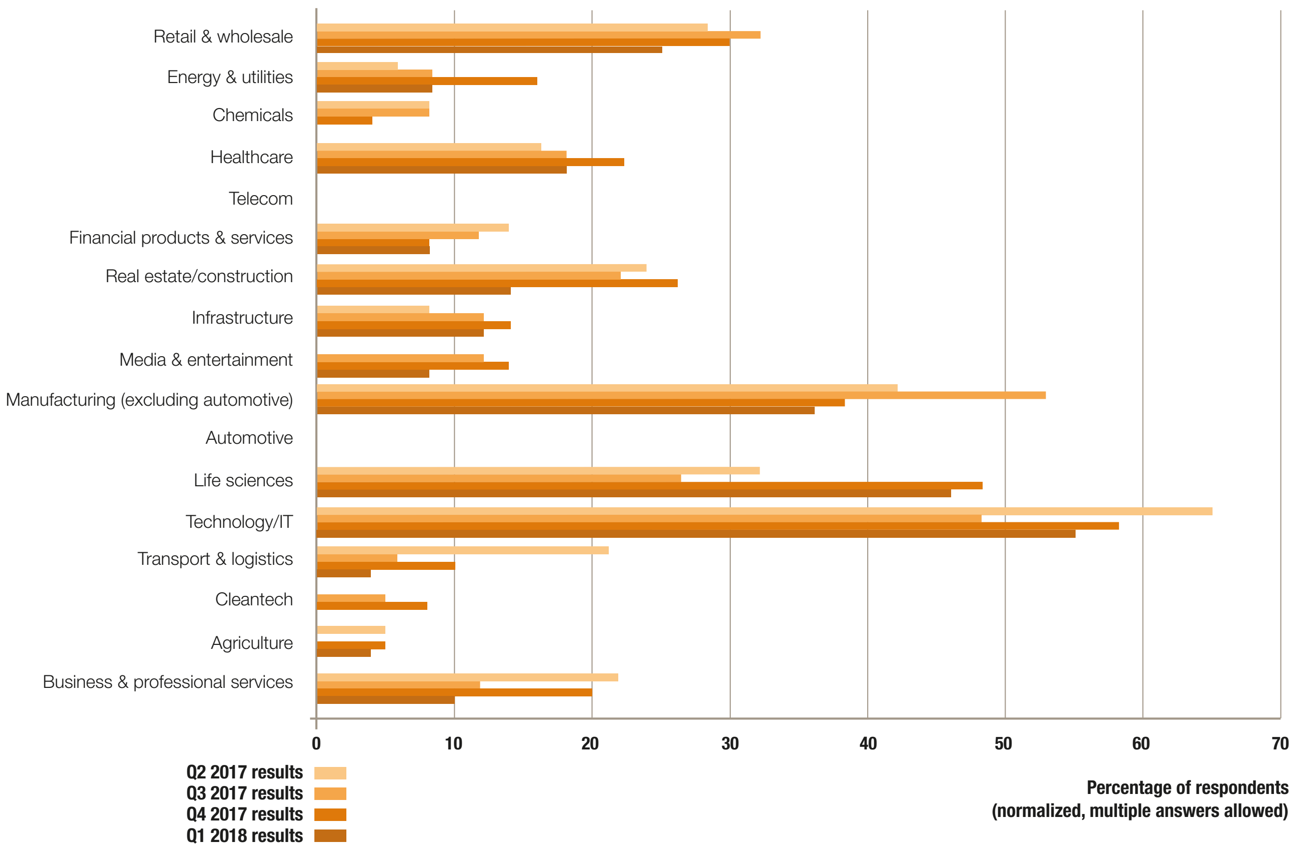
Whilst prior to Q4 2016, the sectors with the most PE/VC activity varied widely from one quarter to the next, starting in Q1 2017 our barometers revealed fewer surprises. The Q1 2018 data confirm this trend with regard to the top three spots.

In Q1 2018, the four sectors with the most PE/VC were (i) technology and IT, (ii) life sciences, (iii) manufacturing and (iv) food production and processing. In Q4 2017, the four sectors with the most PE/VC were (i) technology and IT, (ii) life sciences, (iii) manufacturing and (iv) business and professional services.

The major difference in 2018 compared to 2017 is the inclusion of the food production and processing sector in the top four for the first time.

Respondents continue to report substantial PE/VC activity in the ***technology and IT*** sector (48% in Q3 2017, 58% in Q4 2017, and 55% in Q1 2018). However, although mentioned by many respondents, few deals in the sector received press coverage. The most important deals covered by MergerMarket and the press included:

- GIMV's sale of ActivePath Solutions, a tech company offering baking solutions;
- Capricorn Venture Partners & PMV's acquisition of a EUR 7 million stake in Lindacare, makers of remote monitoring software for chronic desease management;
- GIMV's sale of the German company Mackevision Medien which produced the special effects for «Game of Thrones»;
- Cobepa and others' announcement of the sale of French IT group Exclusive to Permira for EUR 1.3 billion (completed in April 2018).



[2] This information is based on press coverage or obtained from www.mergermarket.com. Please note that unless expressly stated otherwise, acquisition/sale means the acquisition/sale of a stake in/all shares of the target company.

The technology and IT sector also witnessed a large number of capital increases which were covered by the press:

- Vectis' EUR 1 million capital increase in Trustbuilder, a world leader in identity and access management;
- Volta Ventures and Pamica [3] EUR 1.2 million capital increase in Yields.io, an AI platform for model risk management;
- Volta Ventures and SRIW's series A EUR 3 million fundraising round for a capital increase in Qualifio, an online platform to engage digital audiences and collect data by creating and publishing viral interactions;
- US-based Insight Venture Partners' EUR 25 million capital increase in Showpad, a sales enablement platform to make content easy to find, present, share and measure;
- PMV, LRM and Korys's[4] EUR 4.3 million capital increase in Ontofoce, a search engine for the pharmaceutical industry;
- the EUR 4 million capital increase by Oncoradiomics, a specialist in medical artificial intelligence;
- the EUR 1 million capital increase by Helpper, a start-up platform for personal assistance and carers.

The ***life sciences*** sector is still in second place. For the past two years, this sector has been in the top four. Noteworthy deals in Q1 2018 included:

- Mentha Capital's acquisition of Ardena, a Belgian pharmaceutical company active in clinical supplies;
- GIMV's acquisition of the Irish company Foundry Innovation & Research, a digital healthcare developer of therapeutic devices, for EUR 7 million;
- Quest for Growth's acquisition of a stake in HalioDx, a French oncology diagnostics company, for EUR 19 million.

This sector (once again) saw a fair number of capital increases:

- the EUR 25 million capital increase by Miracor Holding, a biotech start-up specialising in cardiology;
- Boehringer Ingelheim & Merck's EUR 15 million capital increase in Rewind Therapeutics, a KUL spin-off engaged in MS research;
- the EUR 3.2 million capital increase by Mitral Technologies, a specialist in medical technologies and interventional cardiology which recently transferred its headquarters from the US to Liège;
- the EUR 23.5 million capital increase in US-based Cyteir Therapeutics by Droia, a developer of combination therapies to fight cancer;
- the EUR 23.4 million capital increase through a private placement by Kiadis, a developer of life-saving therapies for blood cancer;
- the EUR 1.5 million participation in the capital increase of Ectosense by Saffelberg, a specialist in sleep apnoea diagnostics.

The largest Belgian biotech deal in Q1 2018 was the take-over of biotech company Ablynx by global biopharmaceutical company Sanofi (listed on Euronext and NYSE). NautaDutilh, together with Weil, Gotshal & Manges, assisted Sanofi. The latter acquired all outstanding ordinary shares, including American depositary shares (ADS), warrants and convertible bonds of Ablynx at a cash price of EUR 45 per share which represented an aggregate equity value of approximately EUR 3.9 billion. This was Sanofi's second big deal in January 2018, after acquiring Bioverativ, and comes after Ablynx rejected a EUR 2.6 billion offer from Denmark's Novo Nordisk.

The ***manufacturing sector*** (which held the top place in Q3 2017) came in third, with deals mentioned by 36% of respondents. Important deals covered by MergerMarket and the press included:

- Ergon Capital Partners' sale of Nicotra IT, a manufacturer of ventilation applications, for EUR 125 million;

[3] Michel Akkermans's investment vehicle.
[4] The Colruyt family's investment vehicle.

- Bencis Capital Partners sale of Winsol International, a manufacturer of roller blinds & doors, to the Moortgat family;
- Creafund's acquisition of Diresco, a Belgian producer of composite stone;
- GIMV's acquisition of Stiplastics, a French maker of plastic solutions;
- BNP Paribas Fortis PE and KeBeK PE's acquisition of Sign & Façade, a Belgian specialist in illuminated signboard.

Finally, according to market research and the press, the ***food production & processing*** sector was in fourth place. Noteworthy deals in this sector included:

- BNP Paribas Fortis PE's acquisition of Food Associates, a Belgian maker of organic bread;
- BNP Paribas Fortis PE's acquisition of Stoffels Tomaten, a Belgian tomato grower and distributor;
- Korys' sale to Kerry Group of a stake in Ojah, a pioneer in the latest generation of textured meat alternatives using proprietary high moisture extrusion (HME) technology, for EUR 20 million;
- Cobepa's EUR 10.5 million capital increase in Le Pain Quotidien.

Family owned companies continue to attract PE players

In previous barometers, we noted the importance of family owned businesses in Belgium. Many owners/managers of such companies will reach retirement age in the coming years and are therefore actively examining exit strategies. While preference is usually given to other family members, private equity funds in search of interesting targets are another option.

NautaDutilh recently signed a Prime Foundation Partnership Agreement with the Centre for Mergers, Acquisitions & Buyouts of the Vlerick Business & Management School.[5] Further to this agreement, **Elke Janssens** (M&A and Private Equity Partner with NautaDutilh) participates in the Vlerick Exit Academy (designed for entrepreneurs that wish to sell their business or transfer it to the next generation) and was invited to give two presentations, on 3 and 22 May 2018, on the transaction process and negotiations.

The importance of family owned businesses is further confirmed by the deals that received press coverage in Q1 2018. However, it is important to note that family owned businesses are not always the target of the transaction. Such businesses are increasingly on the buying side, for example the Moortgat family, which acquired Winsol from Bencis, and the Colruyt family, through its investment vehicle Korys. NautaDutilh's M&A and Private Equity Teams have extensive experience assisting both sellers and private equity funds that wish to acquire a family business and family offices seeking to acquire assets.

Highlights of NautaDutilh's private equity seminar of 28 February 2018

On 28 February 2018, NautaDutilh's Private Equity Team presented the results of our Q4 2017 survey and discussed the trends and developments revealed by our barometers in the past year. On this occasion, we welcomed as keynote speaker Professor **Sophie Manigart** from Vlerick Business School, who shared her thoughts on the correlation between financial covenants and interest rates in buyout deals with an audience of 60 people. NautaDutilh provided an update on recent legal developments in Belgium and the Netherlands relevant to acquisition finance. We are pleased to present below selected highlights from the seminar.

Buyout deals and bank financing: why your network is crucial to determining interest rates and covenants

Professor Manigart and Vlerick have conducted substantial research in this field and polled the PE

[05] For more information about the Centre, please visit https://www.vlerick.com/en/research-and-faculty/research-in-action/accounting-finance/centre-for-mergers-acquisitions-and-buyouts/partners.partners.

players present in order to gather information about which factors play a role in loan pricing in the context of buyout deals.

When entering into a buyout debt agreement, the most commonly negotiated terms are the amount of the loan, the cost (spread), collateral, maturity and covenants. Buyout debt terms are always interconnected, and characteristics of the target, the PE players involved and the bank can also influence the deal terms. The first question posed immediately gave rise to an interesting finding: while in 95% of deals there is a previous relationship between the PE sponsor and the lead bank, there is a previous relationship between the target and the lead bank in only 45% of deals. During the presentation, the following terms were discussed.

Average debt/EBITDA ratio. The debt/EBITDA ratio (with debt including only bank loans) is on average 3.5 (in the United States, the ratio is 4.09). Both target and bank characteristics determine the ratio, while the prior relationship with the bank and the type of PE player (new, long established, foreign or domestic) do not play an important role. More central banks provide higher debt/EBITDA ratios, hence bank centrality plays a crucial role. Therefore, working with a bank with well-established connections, instead of smaller or unknown financial players, increases the amount of debt available to finance a buyout transaction.

Average (weighted) loan spread (i.e.% above Libor). The average loan spread is only 2.5% (in the United States, the spread is 3.84%). Based on these figures, we can conclude that loans from Belgian banks are quite cheap (please note that these findings do not apply to mezzanine loans). Important factors that lead to cheaper loans are the size of the company and the centrality of the bank. A very interesting finding here is that the better the relationship of a PE investor with the bank, the lower the interest rate charged. Other deal terms also impact the spread. If a longer maturity period is negotiated, the spread increases, while pledging collateral decreases the spread. Interestingly, these terms do not impact other deal characteristics.

Loan maturity. While the average maturity (in years) of debt (excluding revolving credit lines) is 6 to 8 years, 30% of those surveyed indicated a term of 4 to 6 years. In general, maturity periods in Belgium appear slightly longer than in the United State (where the average maturity is 5.69 years). Again, bank centrality is important, as it leads to a shorter maturity period. Further, more profitable companies contract longer loan maturities, while larger companies and transactions in which the PE sponsor has a prior relationship with the bank are associated with shorter maturities.

Probability of pledging collateral. 82% of those surveyed reported that collateral was pledged (in the US, collateral is pledged in only 49% of loan tranches). An interesting (but strange) finding is that the older and more established the PE player, the greater the probability that collateral will be pledged. More central banks typically require less collateral.

In general, the survey showed that one's network is crucial to determining the interest rates and covenants, in a twofold manner: *first*, the PE player's previous relationship with the bank has a significant influence (as it decreases the spread and shorters the maturity period), while the relationship of the target with the bank does not and, *second*, the centrality of the bank (or its position on the debt syndication market) plays an important role, creating a highly positive impact on all deal terms (spread, amount of the loan, etc.). Therefore, over the past 25 years, the bank syndication network on the US leveraged buyout market has become much more interconnected and centralised.

What the new Company Code and Insolvency Code mean for distressed M&A

In our practice, we deal with three types of distressed M&A cases: (i) deals intended to maintain the value of a business, including for shareholders (takeover by the former owners); (ii) out-of-court restructuring; and (iii) court-supervised restructuring in the framework of a judicial reorganisation or post-bankruptcy. For our clients, both the Insolvency Code and the new Company Code will have significant consequences.

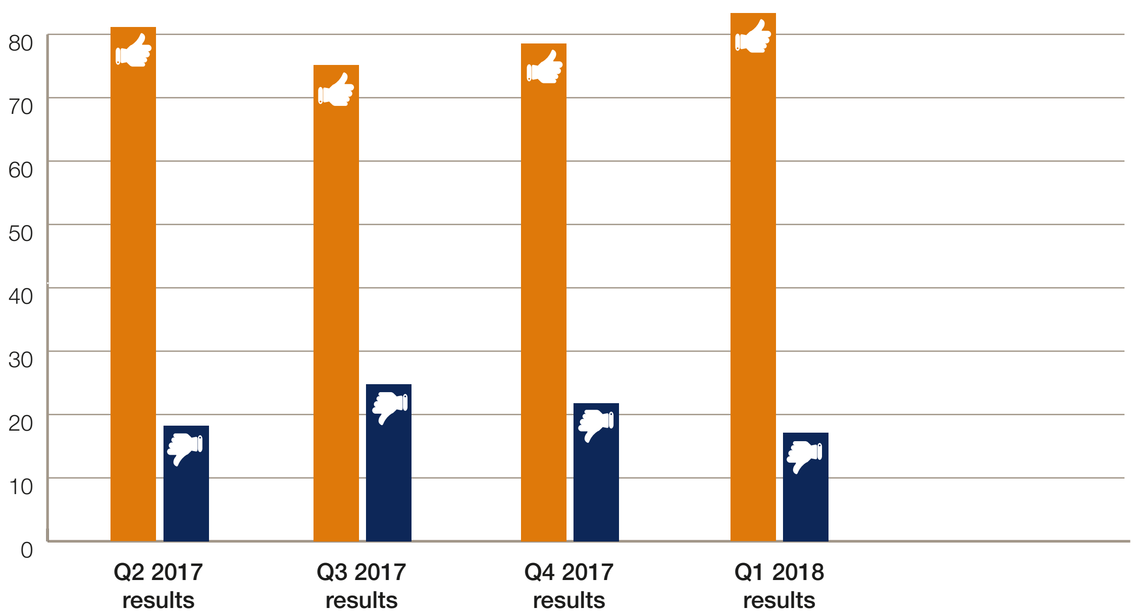
First, the Insolvency Code creates greater awareness of director's liability (and shareholder liability) especially in the two following situations: (i) serious misconduct or gross negligence which contributes to the bankruptcy (Art. XX.225 Insolvency Code), by past or present directors, managers, etc., as well as any other persons with de facto managerial responsibility for the undertaking's activities and (ii) wrongful trading, i.e. when a person knew or should have known that there was no reasonable chance for the company to continue its activities and avoid bankruptcy. In general, greater emphasis is placed on maintaining the value of the business through court-supervised restructuring.

Second, the new Company Code will modify the rules on director's liability. In this respect, members of a corporate organ will be jointly liable (rather than jointly and severally liable), and individual managers will only be jointly liable in the event of a violation of the law or the company's articles. *Last but not least*, it is expected that director's liability will be capped, based on the size of the company, with a maximum of EUR 12 million, but discussions are still underway on this point.

Update on stock options/warrants

Stock options and warrants are widely used as a compensation optimisation tool and incentive in the PE/VC context. The Act of 26 March 1999 provides for (lump-sum) taxation upon grant. According to **Ken Lioen** (Tax Partner with NautaDutilh Brussels), three important developments in 2017 should be borne in mind.

Is Belgian ruling practice a factor when considering potential deals?



First, based on Circular 2017/C/21 of 13 April 2017, stock options or warrants granted by a company to individuals working through a management company do not qualify for the lower valuation system.

Second, in Decisions 2017.715 and 2017.934 of 16 January 2018, the Ruling Commission provided clarification on the maximum amount of options/ warrants that can be granted. Where no statutory guidelines exist on the maximum grant, 20% of the recipient's total annual remuneration package should be used as a guideline.

Finally, the Ruling Commission published its 2016 annual report on 21 June 2017, a highlight of which is its position on re-invoicing (to another group entity) of capital losses realized in relation to a stock option plan. According to the Ruling Commission, under these circumstances, there is no tax-deductible expense as the nature of a capital loss on shares is maintained

Impact of recent legislative reforms on security interests in Belgium

Thibaut Willems (Banking & Finance Partner with NautaDutilh Brussels) and **Nathalie Van Landuyt** (Banking & Finance Senior Associate with NautaDutilh Brussels) discussed the importance of the new act on in rem security interests in movable assets which dates back to 11 July 2013 but only entered into force on 1 January 2018. The main takeaways from the act are:

- Dispossession is no longer required to create a valid pledge of movable assets. Moreover, the pledge can also include future assets.
- The act provides for a new way to perfect a pledge (in addition to perfection through dispossession which remains possible): perfection of the pledge by registration in the National Pledge Register, a publicly accessible national electronic database. Registration is in principle valid for 10 years.
- With respect to tangible movable assets, the pledgor not only has the right to make reasonable use and dispose of the pledged assets in the ordinary course of business, but (unless agreed otherwise) is also allowed to process and co-mingle the pledged assets. For a pledge of a business *(pand handelszaak/gage sur fonds de commerce)*, 100% of the inventory can be pledged. Please note that transitional rules apply to pledges granted before 1 January 2018, which must be recorded in the National Pledge Register before 31 December 2018 in order to preserve the security interest and ranking.
- With respect to intangible movable assets, a pledge of receivables can still not be perfected through registration in the National Pledge Register (the existing rules are maintained), while a pledge of intellectual property rights can be perfected through registration (without prejudice to the requirements and formalities provided for by other legislation).
- Pledges of financial collateral (such as financial instruments and bank accounts) are still governed by the Financial Collateral Act, which was recently amended. Further to the latest amendments, there is no longer a dispossession requirement for pledges of financial instruments and future shares can be pledged. For pledges of bank accounts, the collateral must be «in the possession or under the control» of the collateral taker.

Finally, the SME Financing Act of 21 December 2013 (as amended by the Act of 21 December 2017) was discussed. Based on an assessment of the SME Financing Act, certain aspects should be modified, such as determination of the most suitable type of credit, the pre-contractual information and documentation obligation, the justification for a refusal to extend credit, and the provisions on early repayment and break costs. As of 8 January 2018, the break costs for loans of less than EUR 2 million are limited to six months' interest. Moreover, in certain circumstances, partial release of the security interest will become possible.

Acquisition finance in the Netherlands

Niels Hagelstein (Finance Senior Associate with NautaDutilh Amsterdam) provided insight into the most important points for attention in an acquisition finance transaction under Dutch law: (i) the *ultra vires and financial assistance rules*, (ii) the notarial pledge of shares, (iii) the pledge of receivables, (iv) the pledge of movable assets and IP rights, and (v) the mortgage on real property. In general, security interests can be created in all types of assets. All types of assets, aside from those that can only be pledged or mortgaged by a civil law notary, can be combined in a private deed, which makes acquiring security in such assets easy and cost-efficient. No registration fees are due.

The ultra vires and financial assistance rules. The granting of security or guarantees can in general be limited by statute or the company's articles of association. The most important restrictions in the Netherlands are the *ultra vires* and *financial assistance* rules. Pursuant to the *ultra vires* rule, any transaction entered into by a legal entity may be invalidated by the legal entity itself or its trustee in bankruptcy if the transaction violates the entity's corporate purpose and the other party to the transaction knew or should have been aware of this fact without independent investigation (all relevant circumstances must be taken into account, in particular whether the transaction served the interests of the legal entity).

Final assistance rules may apply to a public limited-liability company *(naamloze vennootschap)* in the event of a subscription to or acquisition of its shares by third parties.

Pledge of shares. This is the most important type of security interest, as the lender can, through the exercise of voting rights, acquire (direct or indirect) control over the company. The general rule is that shares in a private limited-liability company *(besloten vennootschap)* may be pledged (by way of a notarial instrument), unless its articles of association provide otherwise. When the shares of a private limited-liability company are validly pledged, the pledgor retains the voting rights relating to the pledged shares, unless the pledgor and the pledgee agree otherwise.

Pledge of receivables. This type of security interest can take the form of a disclosed pledge (notified to the debtor) or an undisclosed pledge (registered with the tax authorities). The register is not publicly accessible. Future receivables, i.e. those which do not exist at the time of creation of the pledge, can only form the object of an undisclosed pledge. Receivables arising from a legal relationship not yet concluded at the time of the pledge must be pledged separately at the time they come into existence. This requirement has led to the practice of requiring the pledgor to periodically submit «supplementary pledge agreements» .The Dutch Supreme Court has ruled that a lender/security agent is entitled to pledge to itself all receivables of a borrower by registering an unspecified collective pledge agreement on a regular basis (e.g. weekly or daily), provided (i) a master pledge agreement between the lender and the borrower and (ii) an irrevocable power of attorney from the borrower to the lender have been previously registered.

Pledge of movable assets and IP rights. Under Dutch law, a pledge of movable assets may be possessory or non-possessory. A non-possessory pledge is created by means of a pledge agreement registered with the tax authorities. Registration provides conclusive evidence of the date of creation of the pledge. A pledge of intellectual property rights is commonly created using a pledge agreement and recorded in the relevant public registers for various intellectual property rights.

Mortgage. This type of security interest can be created on all real property and is effected by way of a deed executed before a civil law notary and recorded in the appropriate land registry.

Privatisation as a PE deal driver

In Belgium, the largest privatisation wave took place in the '90s. At that time, privatisation mainly related to three types of entities: (i) credit and financial institutions, (ii) investment funds and (iii) industrial companies. Today, there is still a substantial window for opportunity. State-owned shareholdings are mainly structured through three government agencies:

- the Federal Holding and Investment Company (for the Belgian federal government);
- the Flanders Participation Company or PMV (for the Flemish Region); and
- the Walloon Investment Company, Société wallonne de gestion et de participations or SOGEPA (for the Walloon Region).

The Brussels-Capital Region has a similar agency.

In Q1 2018, certain members of the federal Parliament advocated floating at least some of the government's stake in the Federal Holding and Investment Company, although no express announcement was made to this end. In Wallonia, a proposal has been made to merge SOGEPA and SOWALFIN (the Walloon agency for the encouragement and coordination of SME financing). The combined group would be able to exert considerable influence over the economy in Wallonia (approximately EUR 4 billion). While (full or partial) privatisation is not currently being discussed and will probably only be tabled after the 2019 elections, it could have a positive impact on the budget of the Walloon Region.

Deal speed

After having declined sharply from 19 to 14 (Q4 2015), the number of weeks needed to sign/close a deal (from receipt of the information memorandum) dropped further to 11 in Q1 2016 but rose to 17 in Q2 2016 and 21 in Q3 2017. Our latest barometer revealed an average deal time of 24 weeks. The reason for this could be that bidders are placing higher initial offers on the table and then trying to negotiate the price down, for reasons that come to light during the due diligence process.

Post-closing issues

A more worrisome trend (noted for the first time in our Q3 2015 barometer and confirmed by subsequent surveys) is that an increasing number of respondents report post-closing issues, while previously they stated that, in principle, they do not experience claims under the representations and warranties. Our Q2 2017 survey revealed the highest number of respondents reporting post-closing issues (86%), while in Q1 2018 only 78% mentioned such issues (a drop of nearly 10%).

While we do not have detailed information about the underlying reasons for this trend, there are several possible explanations. *First*, parties are paying more attention to precisely formulated representations and warranties. *Second*, more clients and private equity players are requesting limited due diligence, which means potential issues may not be spotted. *Last but not least*, the markets in which certain companies operate (including the retail & wholesale and technology & IT sectors) are increasingly complex.

Post-closing issues