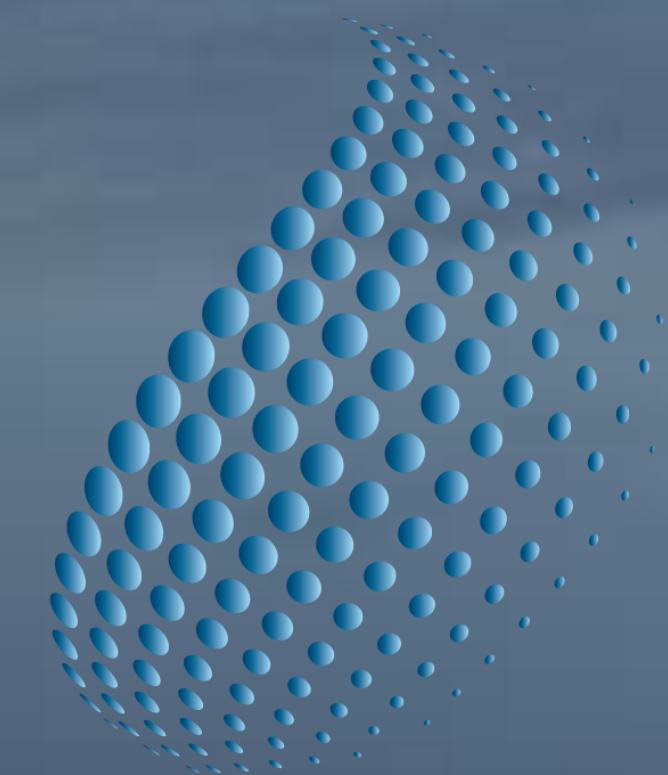


# Capturing private market opportunities

By Oddbjørn Dybvad



**REQ CAPITAL**

INVESTING WITH INSIGHT

**Our investment philosophy is to own companies that have a persistently high return on capital, and a long runway of growth prospects.**

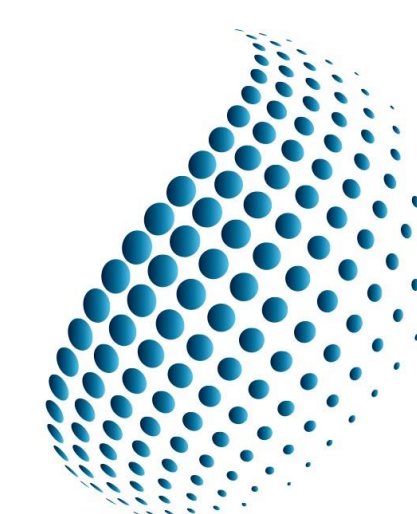
**Many publicly listed serial acquirers share these characteristics. We believe that the "duration" aspect of many of our investments is underestimated by the market, because the opportunity pool of future acquisitions is so large. We believe the right serial acquirers are attractive investments as they reinvest a high proportion of their free cash flow in a disciplined manner (high ROCE acquisitions) over time, and keep acquiring new companies over and over again.**

**The publicly traded serial acquirers we invest in benefit from several advantageous features of the private SME market (Small and Medium sized Enterprises). These companies are not constrained by the size of an end-market or by a particular sector or geography when looking for new acquisitions. For most of our companies, the global SME market is their target.**

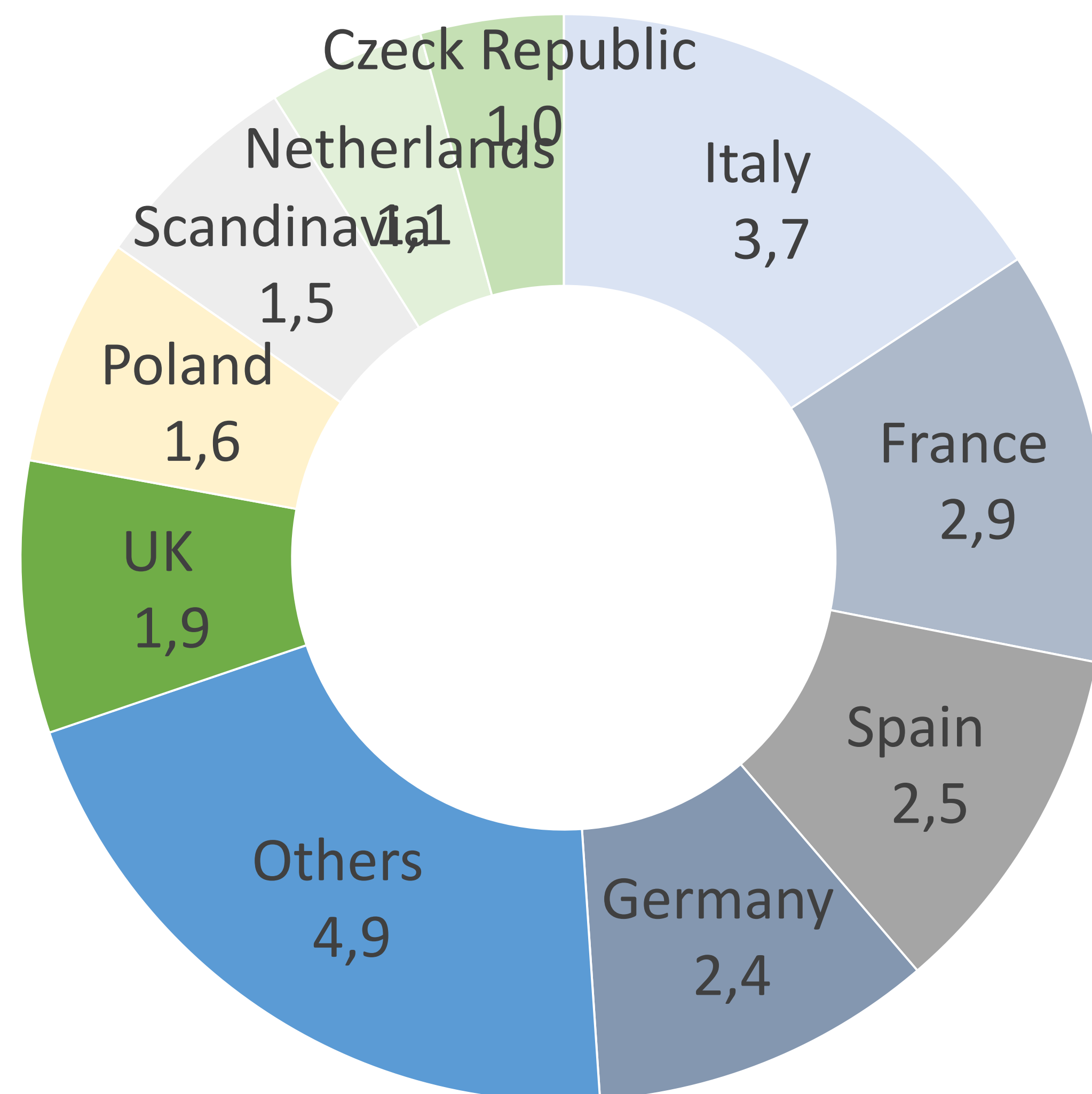
#### **The backbone of the economy**

**Small private businesses are the backbone of the economy. In Europe, 99.8% of all companies<sup>1</sup> are small and medium-sized enterprises with fewer than 250 employees. This group of companies comprises a total of 23.5 million companies.**

**94% of these companies are "independent", meaning not controlled by large corporations. These companies are owned by families and founders. In Europe, about 15,000 companies are sold each year<sup>2</sup>. Some are acquired by large corporations or strategic buyers, some by private equity firms, and some by serial acquirers. The country distribution of SMEs in Europe is as follows (in millions of companies):**



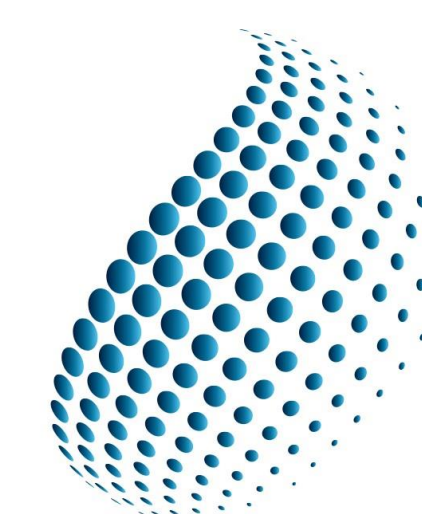
## Distribution of European small private companies



### Italy

Italy is one of the largest manufacturing countries in Europe. Many family businesses were established in the 1950s and 1960s<sup>4</sup> when Italy experienced a major economic boom. Many of Italy's regulations favor small businesses. The transition from one generation of entrepreneurs to the next brings both challenges and opportunities. Family goals may differ from business rationale and threaten a company's competitiveness, which can lead to a transaction. Given the cultural importance of close personal business relationships, it is important for acquirers to have a local presence in Italy.

Given the size of the private business landscape in Italy, it is therefore not surprising that one of our portfolio companies, Lifco of Sweden, made five of its 20 acquisitions in Italy in 2021. The most recent, in May of this year, was Trevi Benne S.p.A. - a manufacturer of excavator tools and attachments for demolition, scrap handling, earthmoving and forestry. Founded in 1992, Trevi Benne employs 105 people and has chosen Lifco as its permanent home.



## Germany

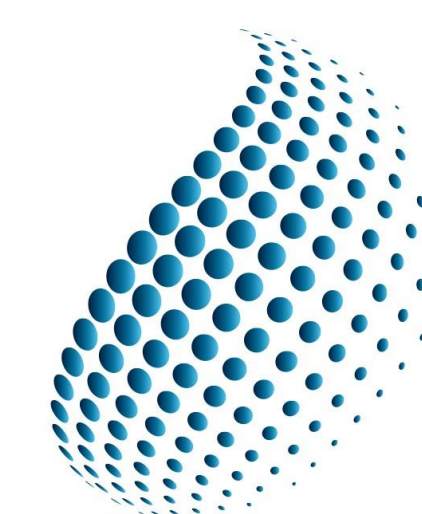
There are 2.4 million small and medium-sized enterprises in Germany. There is a strong family influence both for larger listed companies and for SMEs. A study by the "Institut für Mittelstandsforschung"<sup>5</sup> shows that around 95% of all companies in Germany are family-owned. The shareholder structure is often more broadly distributed among family members than in other countries, such as the United Kingdom. This characteristic represents both a challenge and an opportunity for potential serial acquirers.

Since January 1st of this year, our portfolio companies have acquired eight German companies. On March 31st, Addtech acquired 90% of Fey Elektronik GmbH, a German battery manufacturer. Fey has 160 employees, and the CEO remains a minority shareholder with 10% of the shares.

## UK

The UK is one of the most active M&A markets in Europe. Private equity buyers continue to be the driving force behind deal activity, but the UK is also becoming an increasingly attractive market for serial acquirers. Despite economic and political challenges, the UK mergers and acquisitions market remains exceptionally active. The smaller company segment, defined as transactions of up to £10 million, grew by 21%<sup>6</sup> last year.

We are seeing an increasing number of private acquisitions by our businesses in the UK. In June alone, four transactions were completed by our companies in the UK. The Canadian company Constellation Software was particularly active, acquiring two software companies, including Alemba with 109 employees. On 25th of July Swedish Lagercrantz acquired Door and Joinery, a UK supplier of customized fire doors with sales of GBP 4.5 million.



## In summary

Serial acquirers take advantage of the highly attractive features of the SME market. With local representatives in each market, our companies find, negotiate and close attractive acquisitions.

In summary, investing in companies with long-term growth opportunities and high returns on capital is necessary to achieve high long-term stock returns. An extensive pool of acquisition opportunities is a very good starting point for our acquisition-oriented compounders. We observe that our companies remain disciplined in finding and closing attractive acquisitions at attractive multiples, which keeps returns on capital high. As long-term shareholders, we enjoy the strong value creation in this process.

### Sources:

1)[https://ec.europa.eu/growth/smes\\_en](https://ec.europa.eu/growth/smes_en)

2)“Statistics on small and medium-sized enterprises” by George Papadopoulos, Samuli Rikama, Pekka Alajääskö, Ziade Salah-Eddine (Eurostat, Structural business statistics), Aarno Airaksinen, Henri Luomaranta (Statistics Finland)

3)Thomson Reuters, based on three-year average for 2019-2021

4)“Made in Italy” How culture and history has shaped modern Italian business environment, political landscape and professional organizations. (Susan Global and Kayla Gibson)

5)“The Environment for Business in Germany” (CVJ Simpson Associates)

6)<https://www.cbw.co.uk/2022/01/ma-activity-in-the-uk-sets-new-records-in-2021/>