Pradip Somaia: Regent Partners

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Pradip Somaia, partner at Regent Partners, outlines the current trends in APAC merger and acquisition (M&A) activity for the technology, media and telecoms sector (TMT).

M&A in APAC channels: drivers, valuations and trends

APAC merger and acquisition (M&A) activity in the technology, media and telecoms sector (TMT) remained strong in 2016 with 1,827 deals announced, up 6% on the 1,723 deals announced in 2015. The total value of deals increased by 22% year-on-year from $190 billion in 2015 to $231 billion in 2016. M&A activity has remained strong during the first three quarters of 2017, but at a lower level than the same period last year, with 1,275 deals worth $108 billion announced compared with 1,366 deals worth $169 billion.

The ICT channel continues to adapt to the changing technological and economic challenges as it has done for decades. The challenges depend to a large extent on the size and maturity of the local market. In large, mature markets, there has already been a lot of consolidation as distributors and resellers acquired competitors to gain market share or technical skills and services and benefit from economies of scale as margins come under pressure.

In general, a clear distinction has evolved between distributors and resellers. In the larger markets, the M&A focus is now on acquisition of technology skills and the provision of value added services. In smaller, less developed markets, there are still some hybrid distribution companies that also offer resale services in addition to pure-play distributors and resellers. In these less developed markets, consolidation will be a driving consideration both within the local market and into neighbouring regions.

The acquisition of technology skills and services will also be a feature here. The overriding consideration for channel players is to either grow to benefit from economies of scale and maintain or improve profit margins, or to build specialist technology or sector expertise and services, or, if neither of these two options are possible, sell the business before it becomes too small to be of interest to anyone.

Valuation

The valuation of any business depends on many factors but the primary one is usually the underlying profit of the business. In particular, the earnings before interest, tax, depreciation and amortisation (EBITDA) is a frequently used measure. Most businesses are valued in the region of 5 to 8 times EBITDA although the spread can be wider. The actual multiple within this range depends on other factors such as size, growth and reputation or brand awareness.

A secondary valuation measure is the multiple of price to sales (PS) which can act as a guide to what would be a reasonable earnings multiple. For example, a 5% EBITDA margin implies a PS in the range of 0.25 to 0.4 which is typical of a low margin distributor. However, for EBITDA margins of 20%, the implied PS range would be in the region of 1 to 1.6 which is more typical of value added resellers or system integrators. Selective M&A provides a means to increase the underlying profitability and also improve the profit margin by acquiring scale and higher margin business such as value added services.

Regent Partners, founded 30 years ago, specialises in TMT M&A and has completed many deals in this space. Regent Partners will present its latest views and analysis on M&A deals during a dedicated workshop session at Canalys APAC 2017.