Survey of the Economic and Social Impact of Management Buyouts & Buyins in Europe
The European Private Equity and Venture Capital Association (EVCA) exists to represent the European private equity sector. With over 740 members throughout Europe, EVCA's many roles include providing information services for members, creating networking opportunities, acting as a lobbying and campaigning organisation and working to promote the asset class both within Europe and throughout the world. EVCA's activities cover the whole range of private equity, from early-stage seed capital to development capital, and buyouts and buyins to the flotation of venture-backed companies.
Survey of the Economic and Social Impact of Management Buyouts & Buyins in Europe

This paper considers the role played by venture capitalists in buyout deals. It is based on a pan-European survey conducted on behalf of EVCA by the Centre for Management Buy-out Research (CMBOR), University of Nottingham, United Kingdom. The survey was sponsored by PricewaterhouseCoopers.

January 2001

1 The Centre for Management Buy-out Research (CMBOR) was founded at Nottingham University Business School in March 1986 to monitor and analyse management buyouts in a comprehensive and analytical way. As an independent body, CMBOR has developed a wide-ranging and detailed database of almost 16,000 companies, which provides the only complete set of statistics on management buyouts and management buyins in Europe. CMBOR publishes regular reports on buyout trends and relevant issues in its Quarterly Review and annual European Management Buy-out Review.
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Foreword

In 1996 the European Private Equity and Venture Capital Association (EVCA) undertook an investigation of the economic impact of private equity (venture capital + buyout) in Europe.

The results of this survey are now well documented, and prove that venture capitalists contribute positively to the rapid growth of companies to increase sales, employment, investment, R&D expenditure and exports.

This, however, is only part of the story. Although, between 1995 and 1999, 51% of the total amount of private equity investment was invested in buyout deals, companies and policy makers have in many ways still to recognise the full potential of the buyout. Creating a broader understanding of this financing method will help companies and managers to assess the full range of possibilities when planning corporate restructurings – and to choose the option which optimises the economic and social outcome.

One of the main reasons for the lack of knowledge about buyouts has been the fact that, until now, research has not provided adequate information for useful or detailed analysis.

It was EVCA’s Buyout Committee who, in the year 2000, undertook this study to bring about greater knowledge of this type of investment. This pan-European survey, the first of its kind, was conducted on behalf of EVCA by the Centre for Management Buy-out Research (CMBOR, Nottingham University Business School, United Kingdom). The survey was sponsored by PricewaterhouseCoopers.

The survey had four main objectives:

- To improve understanding of the rationale for a buyout transaction
- To understand the social impact of a buyout on the investee company
- To understand the economic impact of a venture-backed buyout transaction
- To learn about the role played by the venture capitalist in the buyout process.

This report proves that buyouts are important mechanisms for restructuring the economy, leading to better than average performance and competitiveness, increased employment and the creation of additional value. It also proves that buyouts allow for the transfer of ownership from the founders of a business to the next layer of management and solve succession difficulties or issues of strategic fit.

EVCA strongly recommends that European Union Institutions and Member States review the existing tax and legal environment and remove the existing barriers in order to allow for the full development of venture backed buyouts.

EVCA would like to thank all the contributors to this survey for the valuable time they have given and the precious work they have achieved – in particular, all members of the EVCA Buyout Committee, who launched this survey under the chair of Mr. Lionel Anthony and concluded it under the chair of Mr. Jonathan Russell.

Ari Tolppanen  
Chairman, European Private Equity and Venture Capital Association (EVCA)

Jonathan Russell  
Chairman, EVCA Buyout Committee
Sponsor’s Note

PricewaterhouseCoopers is delighted to sponsor this important survey into the growing importance of Management Buyouts and Buyins in Europe.

As the leading advisor on European Buyouts over the last five years, PricewaterhouseCoopers has witnessed the development of the market at first hand. Our dedicated private equity team comprises 75 staff operating throughout Europe. We are seeing an increase in the funds available for investment, deals becoming larger and more innovative and private equity houses expanding their horizons right across Europe. This strength of activity has provided economies with enormous opportunity and resource to support economic growth.

The conclusions reached in the survey are consistent with our extensive experience of European buyouts in recent years. Private equity is now a credible purchaser of family owned and large corporate businesses across Europe and is creating new wealth and economic opportunities.

More than finance

Buyouts are not just about financial engineering, but about adding long term value through the implementation of a strategic vision, with sharper and more focussed operational and financial controls. This means that organisations considering an MBO or MBI are likely to need not only appropriate funding, but also strategic advice, which allows the best use and delivery of capital funds, so as to achieve real value. Specialist sector knowledge, and the ability of advisors and private equity houses to add value through industry focus is becoming increasingly important.

Regulatory changes

Regulatory changes can also add to the enormous potential. In Germany for example, market conditions and the anticipated tax changes are likely to create a large number of buyout opportunities. The funds available and the number of private equity houses active in the buyout market have never been higher.

There is a growing acceptance that new forms of investment capital particularly private equity will continue to provide the European economy with further opportunities for growth. We are confident that European private equity will continue to strengthen its position within the overall mergers and acquisitions market.

Peter J. Jacobs
Partner, PricewaterhouseCoopers Corporate Finance
Executive Summary

Since 1990 the acquisition of companies by teams of managers has become a significant feature of the European private equity market.

During the 5-year period covered by this study, investments in buyouts grew by over 150%, rising from 39.8% of the €4.7 billion total private equity investment in 1992, to 50.1% of the €9.7 billion total in 1997. In the following two years, this figure rose by a further 174%, and in 1999 buyouts represented over half (53%) of the total private equity investment of €25.1 billion (source: EVCA).

Management buyouts (MBOs)\(^2\) and management buyins (MBIs)\(^3\) are popular across all sectors of industry because:

- They allow managers to gain considerable personal reward from taking ownership and addressing pre-existing problems
- They provide an opportunity for investors to become involved in enterprises that are likely to generate excellent returns

But although buyouts are known to be successful mechanisms for revitalising companies and generating high levels of investment return, little is understood about the economic and social impact they have on the target company.

This study was designed to investigate some of the reasons for the success of this type of restructuring. Its purpose was to find out more about three aspects of buyouts:

- **Background characteristics** – the nature and sizes of companies undergoing buyouts, the reasons for the buyout and types of transaction involved
- **Operation of the buyout** – the internal organisation and strategies adopted by buyout companies
- **Post-buyout performance** – indicators showing post-buyout achievement in a number of areas

Between April and September 2000, questionnaires were sent out to a sample of companies across Europe which had undergone a venture-backed buyout between 1992 and 1997. This report analyses the 300 representative responses we received from these buyout companies.

Possibly the most significant finding of this study is the fact that: 84% of responding companies stated that, without the buyout, they would either have ceased to exist or have grown less strongly. Of almost equal importance is the generally held view that the contribution of the venture capitalist – in both financial and non-financial aspects of company operations – has been crucial to post-buyout success.

The economic and social impact of the buyout on investee companies can be seen in virtually every one of a wide variety of indicators – from increased sales and profits, higher levels of employment and employee earnings through to a larger percentage of exports, better marketing and improved customer service.

Two thirds of respondents reported that they had outperformed their competitors over the five years from 1992 to 1997.

\(^2\) A management buyout (MBO) is the acquisition of a company by its own managers. In most cases, the management team seeks the support of PE investors to buy the shares of the company.

\(^3\) A management buyin (MBI) occurs when there are insufficient internal management skills to conduct a buyout. A management team from outside the company acquires a controlling interest – again with the support of private equity investors.

Note that, unless specifically stated otherwise, the term ‘buyout’ in this report includes management buyouts, management buyins and other forms of buyout (e.g. investor-led buyouts, management-employee buyouts).
Post-buyout performance

The responses of the buyout companies support the global perception that the contribution of the venture capitalist has been crucial to the feasibility and success of the buyout. 84% of companies said that, without the venture-backed buyout, the organisation would either have failed to survive or would have had limited growth prospects.

The survey shows that the buyout companies implement a range of growth strategies in the post-buyout period, and that these strategies generally lead to significant increases in turnover and pre-tax earnings.

Moreover, two thirds of respondent companies considered that post-buyout improvements in competitive position and financial performance had been significantly greater than those achieved by their competitors. The improvement in competitive position is gained through increased market share brought about by a relatively higher growth of turnover than competitors.

It is, therefore, not surprising that more than 60% of respondents declared an increase in the total number of employees since the buyout.

The survey also showed that the total number of employees per company increased on average by 47%, and that this growth in employee numbers has been accompanied by a simultaneous increase in employee remuneration.
Operation of the buyout

One key finding is that there was broad agreement that the injection of funds and initiative provided by the buyout has enabled crucial long-term development and investment to take place.

Indeed, the sampled companies reported that the involvement of the venture capitalist is not simply restricted to financial contributions, but often includes a non-financial input. For example, the considerable roles of many venture capitalists extend to acting as a sounding board for management ideas and monitoring operational performance.

The companies surveyed use buyout investment to increase funding for long term, value-adding developments such as research and development, marketing, capital expenditure and employee training.

It is clear that respondents recognise that employee involvement and motivation play a vital role in the achievement of business success. Buyout companies deploy a variety of strategies to gain and improve the commitment of their employees. These include various activities aimed at increasing communication and decreasing the perceived gap between management and employees.

Expenditure in four areas as a percentage of sales before and after the buyout (source: CBOR/EVCA)

Note: ‘Last year’ means either 1999 if the venture capitalist’s investment is still maintained in the buyout company, or the last year before exit if the venture capitalist has exited.
**Background characteristics**

The buyout is an important mechanism for company restructuring and transfer of ownership.

The survey tells us that buyouts are used by home country or foreign country parent companies, family owners or receivers to solve issues of lack of strategic fit, succession difficulties (retirement of the owner) or poor company performance.

Buyout restructuring is used by companies of all sizes, in all sectors of industry (including high tech), although in the survey sample, manufacturing and services predominate.
1. Background characteristics

1.1. Although buyouts occur across a wide range of company sizes, most responding companies have fewer than 250 employees.

- The number of employees in the companies surveyed ranged from 5 to 12,000, with the median size of workforce being 170.
- About a third (36.4%) of the sample had 100 or fewer employees at the time of the survey, of which almost a sixth (16.5%) had 50 or fewer employees.
- Over a quarter (26.6%) had between 101–250 staff, while a sixth (16.2%) had 251–500 employees.
- One fifth of buyouts (20.9%) involved larger companies with more than 500 employees.

1.2. Buyouts take place in all sectors, including high tech companies, although manufacturing and industrial products/services predominate in this sample.

- The companies surveyed fall mainly into the manufacturing (22.6%) and industrial products/services (13.8%) sectors.
- High technology sectors (including biotechnology, computer hardware, software, services and semiconductors, electronics, telecommunications hardware, medical instruments and pharmaceutical activities) account for almost a tenth (9.7%) of the sample.
1.3 Buyouts are an important mechanism for company restructuring and transfer of ownership. The most commonly reported motive for the buyout was lack of strategic fit with the parent organisation, with other significant reasons being retirement of private/family owners and poor performance. In some cases, the only alternative to the buyout would have been receivership.

- 39% of the vendors in the sample were homecountry parent companies. The next largest group of vendors was private/family owners, which accounted for 34% of the survey. Sales by foreigncountry parent companies constituted 10% of the sample. A significant proportion (2.4%) of buyouts were from receivers.

- The principal reason given for the sale of the business and the consequent restructuring was lack of strategic fit with the vendor (44.6%).

- More than a quarter of respondents (26.2%) gave financial difficulties and adverse performance as a reason for the buyout. Indeed, significant reasons were lack of profitability (10.4%), cash flow considerations/difficulties (9.1%), poor growth prospects (4%) and liquidation/failure (2.7%).

- In just over one fifth of cases (22.8%) the reason for the sale was the retirement of the owner(s).

Note: the total exceeds 100% because respondents were able to select more than one option.

1.4. Management buyout appears to be by far the most common type of buyout/buyin transaction.

The change of ownership in 72% of responding companies was a management buyout, with the balance being split between management buyins and other types of buyout operation (e.g. investor-led buyouts, management-employee buyouts).
2. Operation of the buyout

2.1. Our survey suggests that venture capitalists view buyouts as medium to long-term investments.

- In over a quarter of the sample, at the time of the buyout, investors anticipated that they would maintain their investment for more than 5 years.
- In three-fifths of the sample (62.2%), investors envisaged a time-scale to exit at the time of the buyout of four years or more.
- A fifth (21.3%) reported that no specific time-scale to exit was planned at the time of the buyout.

2.2. Following the change in ownership, the buyout companies surveyed implemented a wide range of key strategic actions to grow their businesses.

- 69.6% increased their product range
- 62.5% expanded into new markets
- 53.7% invested in new sites or locations
- 52% developed existing sites.

Note: the total exceeds 100% because respondents were able to select more than one option.

2.3. Sampled companies identified improved financial control, better customer service and higher levels of business efficiency as the most important ways of adding value.

We asked the surveyed buyout companies to consider how they planned to add value by ranking a number of factors on a scale between 1 (very low importance) to 5 (very high importance). The respondents considered the three most important factors for creating value to be:

- Improving business efficiency (4.2 on the 1–5 scale)
- Improving customer service (4.2 on the 1–5 scale), and
- Improving cash flow/financial controls (4.2 on the 1–5 scale)

They also assigned a high importance (3.5 to 3.9 on the 1–5 scale) to seven other factors.
2.4. The companies surveyed used buyout investment to increase funding for long-term strategic developments such as research and development, marketing, capital expenditure and training.

Our survey suggests that the injection of capital following a buyout enables previously constrained businesses to expand longer-term development. For each of four key strategic areas, expenditure (as a percentage of sales) in the year before the buyout was compared with that for the last complete financial year\(^4\). We found that in all four areas average expenditure increased during the period.

- Research and development – 66% increase
- Capital expenditure – 62% increase
- Marketing – 59% increase
- Training – 54% increase.

2.5. Respondents recognise that employee involvement and motivation play a vital role in the achievement of business success. After the buyout, companies deployed a variety of strategies to gain and improve the commitment of their employees.

We asked buyout companies to consider a number of factors describing how their approach to managing employees had altered since the buyout. They were asked to rank these factors by assigning each one a score on a scale of 1 (has become much less important) to 5 (has become much more important).

The factor reported to have changed most significantly after the buyout (4.1 on the 1–5 scale) was the importance attached to making employees feel that they are an integral part of the company. However, it is significant that none of the involvement-promoting factors we identified achieved a score of less than 3.1 on the 1–5 scale.

\(^4\)‘Last year’ means either 1999 if the venture capitalist’s investment is still maintained in the buyout company, or the last year before exit if the venture capitalist has exited.
2.6. Most venture capitalists adopt a hands-on strategy in their working relationships with buyout companies.

Of the 275 buyout companies responding to this question, the majority (68%) have contact with their venture capitalist on a weekly or monthly basis, while only 32% have contact less than once a month.

![Figure 2.6: Frequency of contact between venture capitalists and buyout companies (source: CMBOR/EVCA)](image)

2.7. Venture capitalists are involved in non-financial (as well, of course as financial) aspects of the reporting companies' operations.

We would naturally expect venture capitalists to focus on monitoring financial performance and giving financial advice. But their input into buyout companies often extends beyond these areas.

Two questions in the survey focused on this aspect of the investor/company relationship.

- In the first question dealing with this area, the sampled buyout companies were asked to identify the level of input of the venture capitalist in a number of company activities. For each activity, they were asked to estimate the percentage of venture capitalist involvement, ranging from 0% (venture capitalist has no involvement) to 100% (venture capitalist has sole responsibility).

Not surprisingly, the venture capitalist's contribution is relatively high in monitoring financial performance. However the venture capitalist's involvement also covers non-financial areas. These include acting as a sounding board for management ideas, monitoring operating performance, strategy formulation and challenging the status quo.

- The second question asked buyout companies what they valued as the single most important contribution of the venture capitalist, other than the provision of funding. Financial advice and contacts was the most common reported response, with acting as a sounding board for management ideas and providing strategic advice also featuring prominently.

![Figure 2.7a: Contribution made by venture capitalist in various aspects of buyout company operation (source: CMBOR/EVCA)](image)

![Figure 2.7b: Single most important contribution (funding excluded) by the venture capitalist (source: CMBOR/EVCA)](image)
3. Post-buyout performance

3.1. The post-buyout period is characterised by a significant increase in turnover.

This factor is of key importance to buyout stakeholders, as it provides evidence that existing, competent management teams can translate their expertise into improved financial performance when they are given the freedom to do so. Our data shows that not only is there a significant increase in growth in the year following the buyout (9.1% to 12.5%), but also that this high level is sustained in following years.

The percentage difference in turnover was calculated for each buyout. An average (mean) was then calculated for the annual increase in turnover of all companies that supplied data. Figure 3.1 shows that the average annual growth rate of buyout companies rose from 9.1% in the year before buyout to 16.7% in the third year after buyout – an increase of 84%.

3.2. Respondents reported significant increases in EBIT (Earnings before Interest and Tax) as percentage of turnover. A rapid growth follows the buyout, and earnings then stabilise at a high level.

This is again of vital importance to buyout stakeholders. As with turnover, we calculated the average change in earnings for the companies reporting EBIT data. Figure 3.2 shows that:

- In the year in which the buyout occurred, average EBIT rose from 4.2% to 6.4% – an increase of 52%
- The biggest increase occurred in year 1 after the buyout, with average EBIT rising to 7.5%
- In subsequent years there was a slight fall-off, with average buyout EBIT stabilising at 7% in year 3.
3.3. Most of the responding companies reported an improved competitive position and significantly better financial performance than competitors.

These impressive improvements in turnover and earnings should, of course, be viewed within the context of overall changes in general market conditions. In order to give an indication of the performance of the buyout, respondents were asked to compare the buyout’s performance with that of its competitors. The data here is more subjective, but:

- Almost two-thirds of respondents (65%) reported that their turnover grew faster than that of their competitors since the buyout.
- Approximately the same proportion (67.3%) reported that earnings grew faster than those of their competitors since the buyout.

3.4. There is some evidence that buyout companies become more involved in exporting.

Although the figures here are not as dramatic as those for turnover and EBIT, this increase may be further evidence of a more entrepreneurial culture following the buyout. Of the 234 companies providing such information, the number engaged in exporting rose from 72.6% in the year before the buyout to 83.8% in the last year\(^5\) – an increase of 15%.

For those buyouts engaged in exporting, the share of their output exported rose from 24.7% in the year before the buyout to 28.3% in the last year\(^5\) – an increase of 14.7%.

\(^5\) ‘Last year’ means either 1999 if the venture capitalist’s investment is still maintained in the buyout company, or the last year before exit if the venture capitalist has exited.
3.5. Over 60% of sampled companies reported an increase in the number of employees after the buyout.

Three-fifths of the 298 responding companies (61.4%) reported that the total number of employees increased since the buyout, while in 13.1% of cases the number of employees remained constant.

The average change in the total number of employees following the buyout is an increase of 46.9%.

![Fig. 3.5: Change in the total number of employees after buyout](source: CMBOR/EVCA)

3.6. Not only managers, but employees at all other levels achieved higher levels of both earnings and other forms of remuneration following the buyout.

In 70% of responding buyout companies, total remuneration (including fixed and variable earnings and equity packages) rose for top management since the buyout. For middle management, remuneration rose in over 70% of companies and for other employees in more than 60% of companies.

Forms of additional remuneration such as equity participation and variable (performance-related) pay are becoming increasingly popular as management motivation tools. 28% of responding companies made greater use of these types of remuneration following the buyout.

The number of employees of sampled companies who participated in share option schemes rose fivefold from 2.1% in the year before the buyout to 10.7% in the last year.

The number of employees receiving performance-related pay more than doubled from 16% in the year before buyout to 37.7% in the last year.

![Fig. 3.6: Post buyout changes in management and employee remuneration](source: CMBOR/EVCA)

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6 'Last year' means either 1999 if the venture capitalist’s investment is still maintained in the buyout company, or the last year before exit if the venture capitalist has exited.
3.7. The perception of responding buyout companies is that the contribution of the venture capitalist has been crucial to the feasibility and success of the buyout.

In almost half the cases, investment (48.8%) and employment (45.8%) were considered to be higher than they would have been without private equity investment in the company.

In almost a third of cases (33.2%), R&D expenditure was thought to be higher because of the venture capitalist’s involvement, while just over a quarter (26.8%) of respondents saw a positive impact of the venture capitalist on export levels.

3.8. 84% of responding companies said, that without the venture-backed buyout, the company would either have failed to survive or have had limited growth prospects.

Almost two-fifths of responding companies (38.6%) said that they would no longer exist without the buyout, whilst almost half (45%) stated that the company would have developed slower without the buyout. In only 2% of cases did management consider that in the absence of the buyout the company would have developed faster.
Two broad messages emerge from this report. Firstly, buyouts are important mechanisms for restructuring the economy, leading to better than average performance and competitiveness, increased employment, increased employee involvement and the creation of additional value. In many cases, the buyout has been seen as the only way forward for organisations previously suffering from investment constraints or poor performance.

Secondly, the contribution of the venture capitalist is crucial to the success of the buyout – both in terms of enabling it to happen and in terms of the contribution made in the post-buyout period. 84% of respondent companies said that they would not exist or would have developed more slowly without the venture-backed buyout. The venture capitalist’s primary input in the buyout is not restricted to investment funds. Many venture capitalists also take an active role in supporting both financial and non-financial aspects of the company’s operation.
Appendices

Appendix 1: Survey methodology

This survey was carried out between April and September 2000.

The sample was derived from the Centre for Management Buy-out Research (CMBOR) database which contains details of over 15,000 venture-backed and non venture-backed management buyouts (Centre for Management Buy-out Research, Nottingham University Business School, Jubilee Campus, Wollaton Road, Nottingham NG8 1BB, UK).

Our sample included all venture-backed buyouts completed in the EU between 1992 and 1997. We did not collect data on buyouts which took place after 1997 because we wanted to allow a sufficiently long post-transaction period for changes in performance to be identified.

It is important to note that 1992–1997 is not the period for which companies were asked to supply data, but the qualifying period for inclusion in the sample. The period each company was asked to consider was from the year before buyout to:

- either 1999, if venture capital still forms part of the company’s equity, or
- if venture capital no longer forms part of the equity, the last year in which venture capitalists held a stake in the company.

Piloting

Before we carried out the main survey, we piloted the questionnaire in March 2000.

The pilot group consisted of 20 management buyouts, distributed by country as follows:

- UK (6)
- Netherlands (4)
- Spain (3)
- France (2)
- Italy (2)
- Denmark (1)
- Germany (1)
- Sweden (1)

The pilot enabled us to check the questionnaire for consistency, relevance and clarity.

Response to the survey

After minor modifications, the questionnaire was translated into French, German, Italian and Spanish and mailed to the selected buyout companies.

We received a total of 300 responses from the 2,359 questionnaires sent out, representing a return rate of 12.7%.

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Table A1: Responses by year of buyout
(source: CMBOR/EVCA)
Appendix 2: Analysis of responses by country

Figure A2 below compares the proportion of questionnaires returned from individual countries with the total number of venture capital backed buyouts that took place in those countries between 1992 and 1997.

The proportion of questionnaires returned from each country reflects the relative size of the buyout market in that country, with the exception of France (6% response out of 12% total). No responses were received from Denmark, Norway and Portugal. However, these countries account for only 1.5% of the total number of European deals made during the survey period.

UK companies returned 195 questionnaires, or 65% of the total number received. This figure almost exactly matches the UK’s 66.1% share of the European buyout market during the years covered by this study. The higher number reflects the maturity of the UK buyout market.

In order to find out whether or not this predominance of UK statistics skewed the overall findings of the survey, we conducted a separate analysis which excluded the UK figures. This made little difference to the overall outcomes, and showed that the survey results from other countries are very much in line with those from the UK.

Appendix 3: Analysis of responses by business sector

Figure A3 compares the proportion of questionnaires returned by each industry sector surveyed with the proportion of venture-backed buyouts recorded as occurring in that sector between 1992 and 1997 in the CMBOR Database.

On the whole, the proportion of questionnaires returned reflects the relative size of the buyout market in the various sectors surveyed.
Contributors

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