FIRMEX

M&A FEE GUIDE 22/23

EUROPEAN EDITION

Key insights on M&A advisory fees in the middle market.

Partnered with: Langcliffe International

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This Year's Highlights

1. **A majority of middle-market European merger advisors said they kept their fee levels the same in 2022 as in 2021 for deals of similar size and complexity.**

2. **About two-fifths of the firms raised success fees, work fees, or both.**

3. **More than half of the advisors said their revenue from M&A fees would be higher in 2022 than in 2021.**

4. **Most firms said they would be about as profitable in 2022 as in 2021. Of the rest, more said profitability increased than said it declined.**

5. **The number of firms that don't charge a retainer or work fee in addition to a success fee increased to 13% from 8% last year.**

6. **Three-quarters of firms said there was no change in the pressure to cut fees in 2022. Only 15% of firms said the pressure increased.**

Building off the success of last year's first regional M&A Fee Guide, we are pleased to once again offer a European edition of the guide. We have partnered with Langcliffe International to produce a comprehensive source on transaction fees in the middle market in Europe. With 155 M&A professionals who contributed to this year's data, business owners and M&A practitioners alike can expect a clear and accurate picture of what it's looked like to be on either side of a deal this year. Additionally, commentary from our partner lends expert perspective that helps us interpret the numbers and trends. We're confident this will be a useful and relevant resource as we enter the year and markets ahead.

—Mark Wright, General Manager, Firmex

Overview

IF THERE'S ONE THING we've learned conducting surveys over the last seven years, it's that middle-market merger advisors are a very plucky crew. They are optimistic by nature, and they find ways to thrive in any environment.

The last year certainly was not ideal for dealmaking. Interest rates rose sharply. There is a ground war in Eastern Europe with substantial disruption to the energy market. Public equity markets have fallen, and the prospect of a recession looms.

In our quarterly survey of deal volume, middle-market advisors say their overall volume has flattened out but is not declining. That's better than the overall merger market, which has seen volume fall significantly over 2022.

Now in our annual look at sell-side merger fees, the smaller firms say they are doing well. They said that in 2022, their merger fee income increased from 2021, and most said their profits would hold flat or increase. Many bulge bracket firms, by contrast, are suffering from declining earnings.

Many of the advisors said volume has been steady, but the nature of the transactions is changing. "Growth deals are slowing down, but distressed M&A deals are picking up," said Greg Bouille, Managing Director, Chiron Financial, Lausanne.

Anecdotally, some participants expressed concern that the market will become more difficult in 2023. So far, however, the advisors say that merger feel levels are remaining steady. About two-fifths of the advisors have raised their fee rates in 2022.

When we probed about the specific fees and terms they use, the answers were similar to those last year, with one exception. This year, it's more common to specify a single rate for success fees in a deal. Last year, the most frequent structure was a success fee that increased for larger deals.

If we created an engagement letter based on the most common answers from this year's survey, we would include these terms:

- A one-time work fee of $25,000 to $50,000 that will be deducted from any success fee.
- A success fee with a set commission rate that does not vary with the ultimate transaction value.
- The overall success fee would depend on the deal size:
  - 4%-6% for $5 million deals.
  - 2%-4% for $10 million and $20 million deals.
  - 1%-2% for $50 million and $100 million
  - Less than 1% for $150 million deals.
- The success fee is payable at closing.
- The client reimburses the cost of travel and accommodation.

Methodology

Since 2016, Firmex has monitored the world of merger advisory fees through regular surveys of middle-market investment bankers, brokers and other advisors.

This year we are conducting two parallel studies, as we did in 2021. This one covers Europe, and a separate report looks at North American fees.

The results in this report are based on an online survey that was completed by 155 European middle-market professionals in late October and early November 2022.

The respondents were spread throughout the continent. The largest contingent was in the United Kingdom (29%), followed by Germany (16%), Italy (7%) and the Netherlands (5%). Within that region, the advisors work in more than 50 different cities, most frequently London, Frankfurt and Milan. Most of them (69%) work as investment bankers or merger advisors, and another 13% call themselves business brokers. More than half of the respondents (58%) are chief executives or managing partners. Another 28% are partners, managing directors, or other senior leaders.

Two-thirds of the advisors are generalists. Of those with specialties, the most common is technology, media, and telecommunications (34%), followed by consumer and retail (21%) and healthcare (21%).

The firms serving middle-market companies are generally small. Half of those in our survey had five employees or fewer. Only one-sixth had more than 50 employees.

The 2021 survey had 107 European respondents. The 2020 survey had 106 respondents from Europe.

Contributor

Mark Eardley

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Educated at the University of Cambridge, Mark's career started at Barclays Capital.

He subsequently joined a PLC as director of corporate finance where he was involved in numerous acquisitions prior to a disposal to a larger PLC. For a number of years thereafter he ran his own CF boutique and attended to the interest of a Jersey based family office.

Following this, he headed up corporate finance at a mid-tier firm of accountants, prior to establishing Langcliffe in 2012. Langliffe has evolved from being a small UK-centric merger broker, to Europe's leading deal origination business.

About Langcliffe International

Langcliffe International has established unrivalled relationships with vendor advisors, corporates and private equity firms, across Europe and beyond. Connecting the sell-side and the buy-side, Langcliffe continuously communicates with vendor advisors and holds the acquisition criteria of 15,600+ buyers on their system, of which over 4,400 are engaged. To support this, Langcliffe now employs 16 professionals and a further five consultants. Their model encompasses a presence in each key economic area of Europe: the UK & Ireland, Benelux, DACH, the Nordics, France, Southern Europe and CEE. They continue to invest in a proprietary deal matching and management system to support their operations.

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Langcliffe International

Overall Revenue and Fee Levels

The post-pandemic surge in dealmaking in 2021 continued to keep advisors busy in 2022. Slightly more than half of them said their total revenue from merger and acquisition fees would be higher this year than last. Only 14% said their revenue declined.

The firms that enjoyed increased revenue growth said they benefited from an increase in deal size and a return on their marketing and networking investments.

The economic uncertainty and war in Ukraine affected firms differently. Some said that deal volume increased, as sellers rushed to complete transactions before conditions worsened, and buyers looked for bargains. Many, however, said the turmoil is slowing down the pace of dealmaking.

About two-fifths of the firms raised success fees, work fees, or both. But of the firms that didn't raise fees, 38% still saw their revenue increase in 2022.

"Our fee percentages for retainers and success fees are the same year on year," said a managing director of a corporate finance boutique in London. "But our revenue has grown due to increased deal activity."

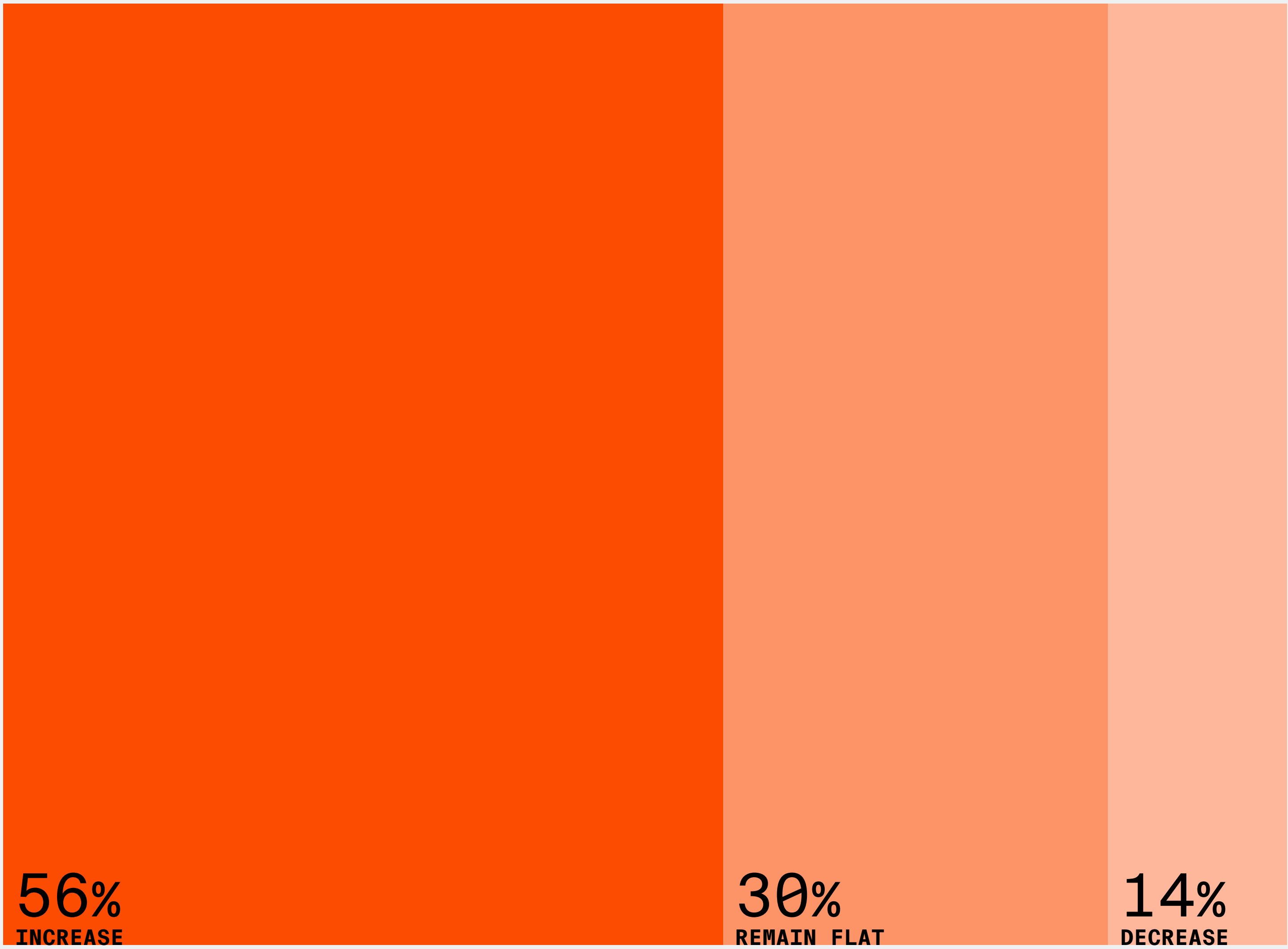
The most significant force affecting fee levels, the advisors said, was competition. Rising costs, especially for labor, was a common reason that firms said they were raising prices.

Contributor Commentary

The ongoing positivity throughout 2022 and demand for M&A services, coupled with a shortage of experienced M&A professionals, has enabled M&A advisors of all transaction sizes to be more selective of the mandates they take on, and impacted the fees they have been able to charge. In simple terms, in any market, if demand is strong and supply is constrained, prices increase. ***—Mark Eardley, Langcliffe International***

Overall Revenue and Fee Levels *CONTINUED*

How do you expect your firm's revenue from mergers and acquisition fees in 2022 to compare to 2021?



Observations: M&A Revenue

Buyer appetite is increasing in an uncertain economic market. ***—CEO, Corporate Finance Boutique, Cheshire, UK***

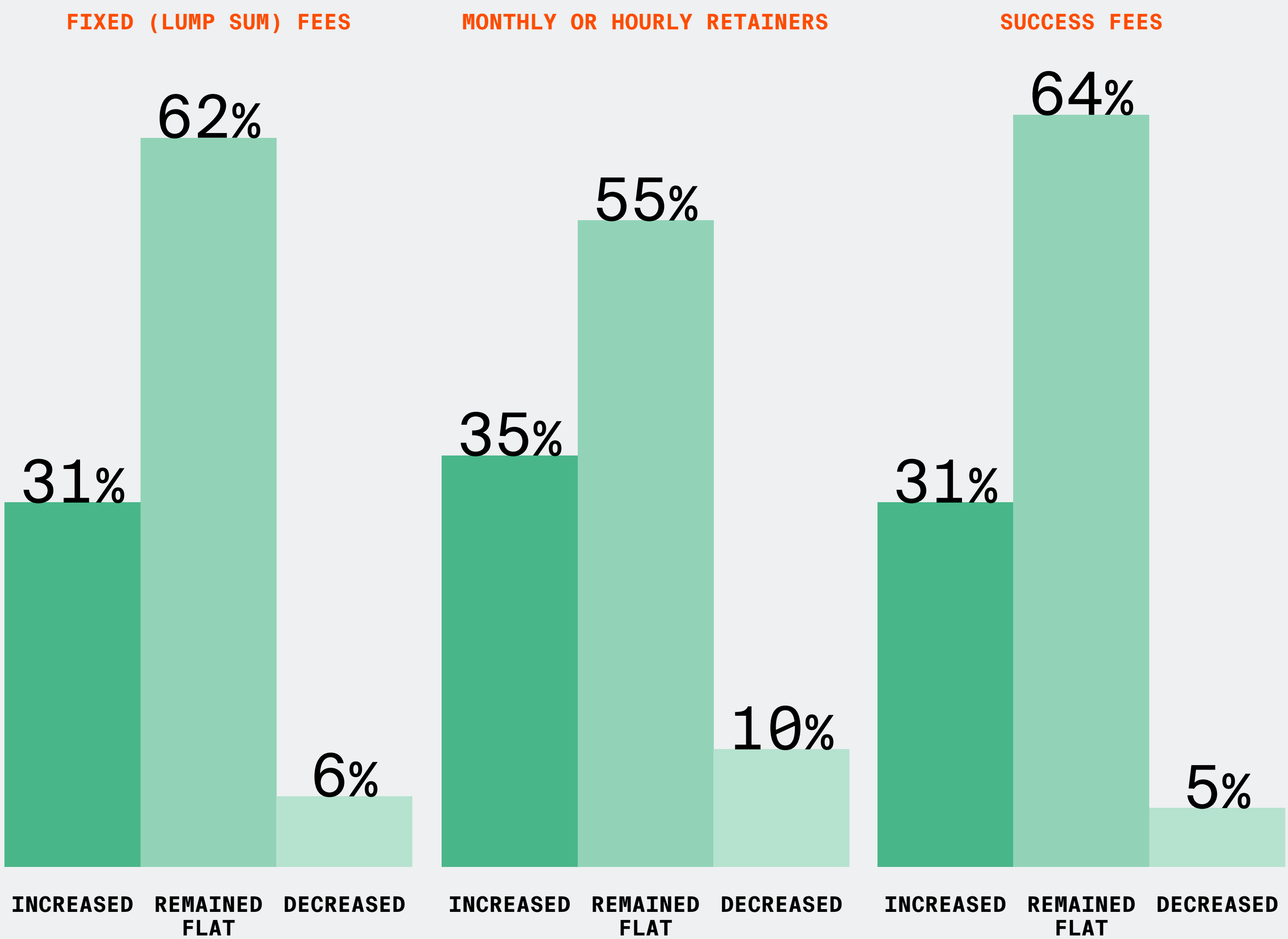
Revenues are flat because market uncertainty is increasing the time to close deals. ***—Director, Investment Bank, London***

Market uncertainty and high seller price expectations are depressing volume. ***—Colin Marson, Managing Partner, Lisergy Consulting, Rugby, UK***

Deal volume is down due to the regional economic instability generated by the Ukraine conflict and related consequences. ***—Daniel Ionescu, Managing Partner, Larive Romania IBD SRL, Bucharest***

Overall Revenue and Fee Levels *CONTINUED*

For deals of similar size and complexity, how have your fee levels changed in 2022?



Observations: Fee Levels

You can get any reasonable fee if the right target can be presented. ***—CEO, Investment Bank, Vienna***

Although the level of fees has remained broadly flat, we're finding that converting a prospect to a client is increasingly difficult. This reticence to commit, however, does not seem to be driven by the level of the fees. ***—Partner, Advisory Firm, Aberdeen, UK***

I think fees will not be affected since many companies will face hurdles accessing capital and will be willing to pay higher fees. ***—Managing Director, Corporate Finance Boutique, Varna, Bulgaria***

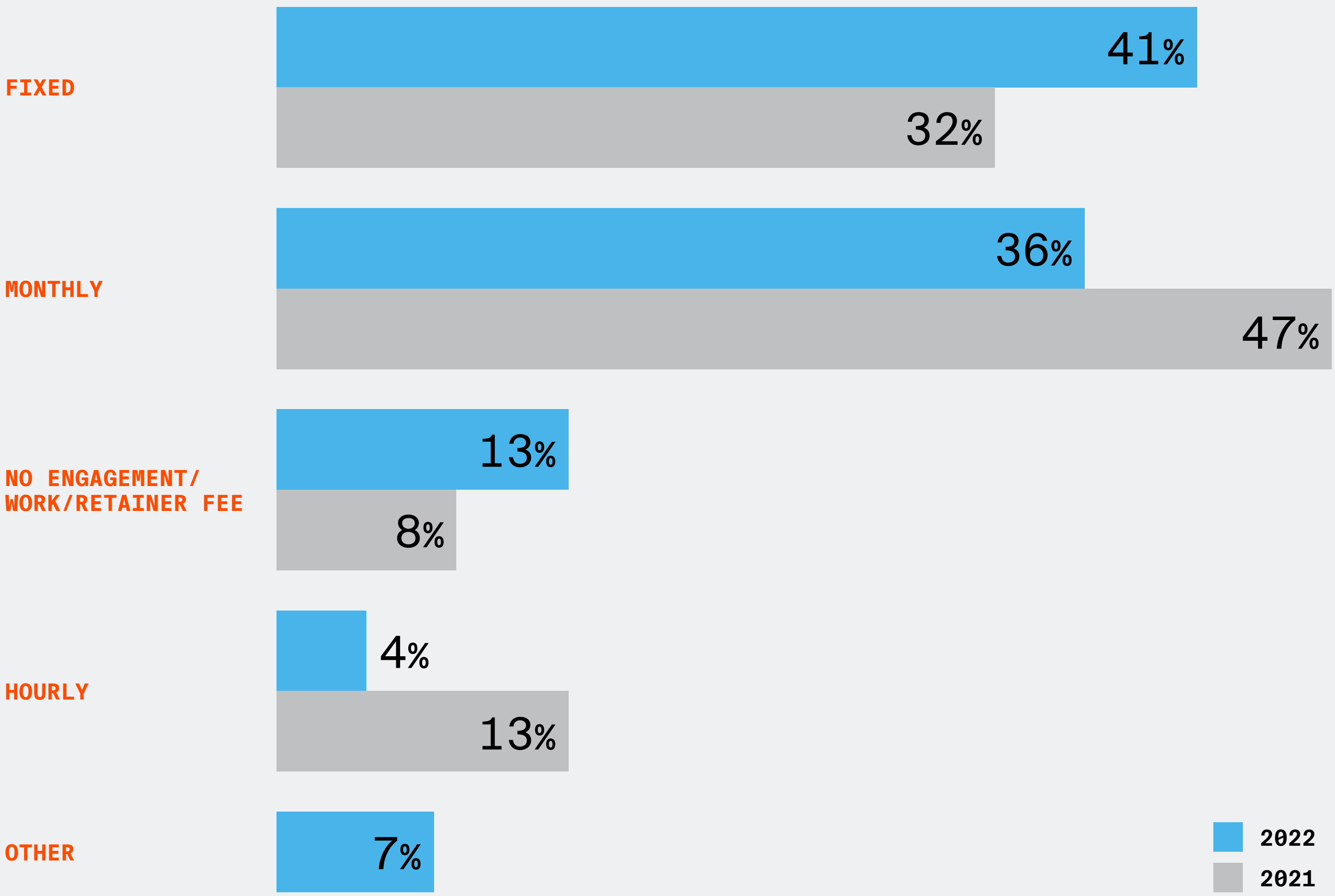
We are more selective and will reject clients who are not willing to pay reasonable fixed and success fees. ***—Director, Investment Bank, Cyprus***

Engagement Fees

In Europe, 87% of the middle-market advisors charge an engagement fee, also known as a retainer or work fee. That's slightly down from last year, when 92% of advisors said they charged engagement fees.

The most common format is a single up-front retainer, used by 41% of the advisors. Monthly fees were used by 36% and hourly fees only by 4%. A few said they used other structures, such as work fees based on milestones or periodic fees with a cap.

For sell-side transactions, do you charge an engagement/work/retainer fee, and if so, how is it most commonly structured?



Contributor Commentary

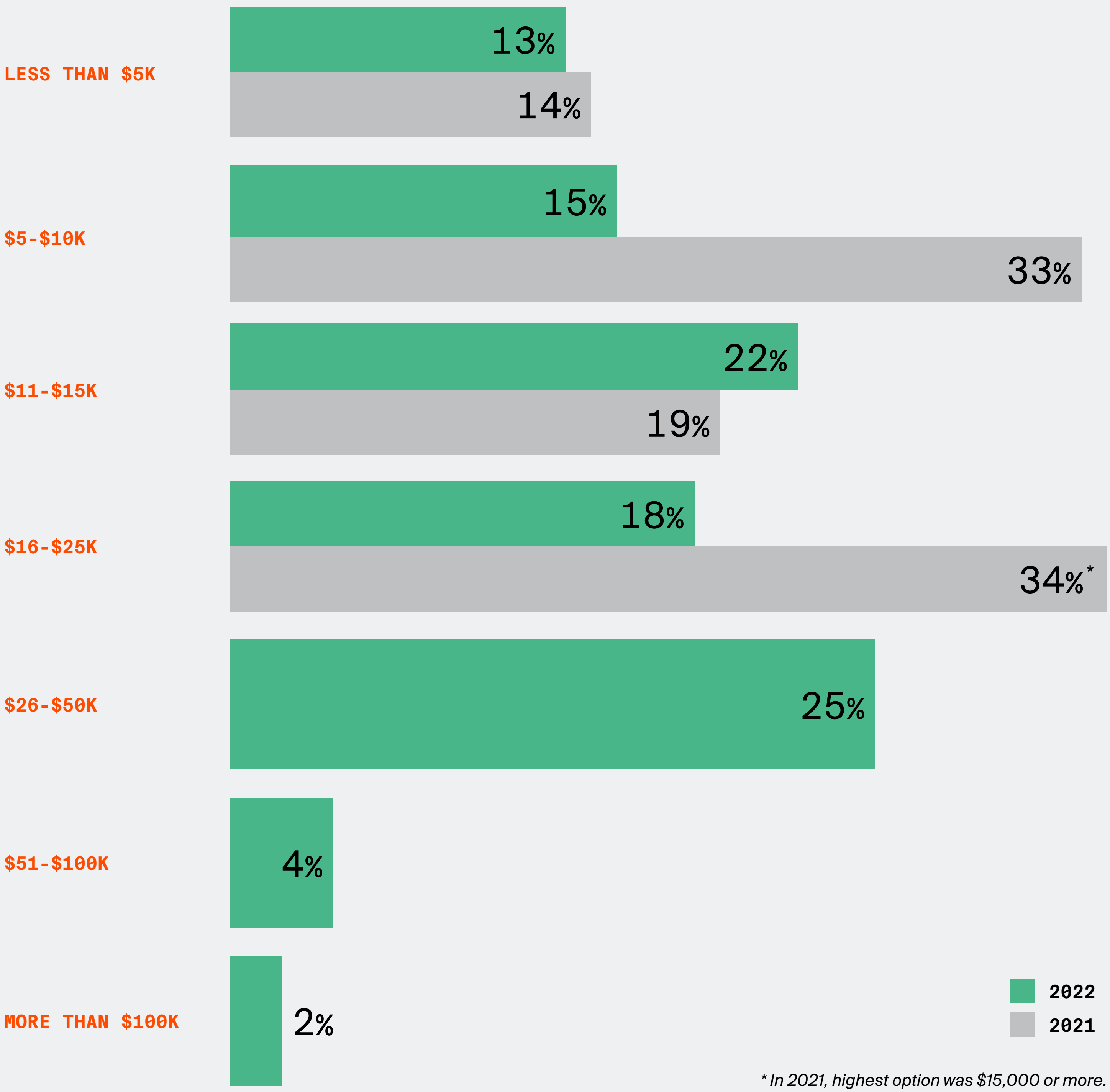
The continuing high percentage of retainer / fixed fees reflects the need for significant committed work to prepare a company for a sales process. The reduction in engagement fees reflects a slight softening of the market from Q2 2022 onwards.

—Mark Eardley, Langcliffe International

Engagement Fees *CONTINUED*

For firms that use lump sum fees, the amounts charged are sharply higher than last year. Half of the advisors charged $16,000 or more, compared to only one-third in 2021. This year, the most common retainer amount is between $26,000 and $50,000.

What is your most common fixed (i.e., lump sum) engagement/work/retainer fee?



In 2021, highest option was $15,000 or more.

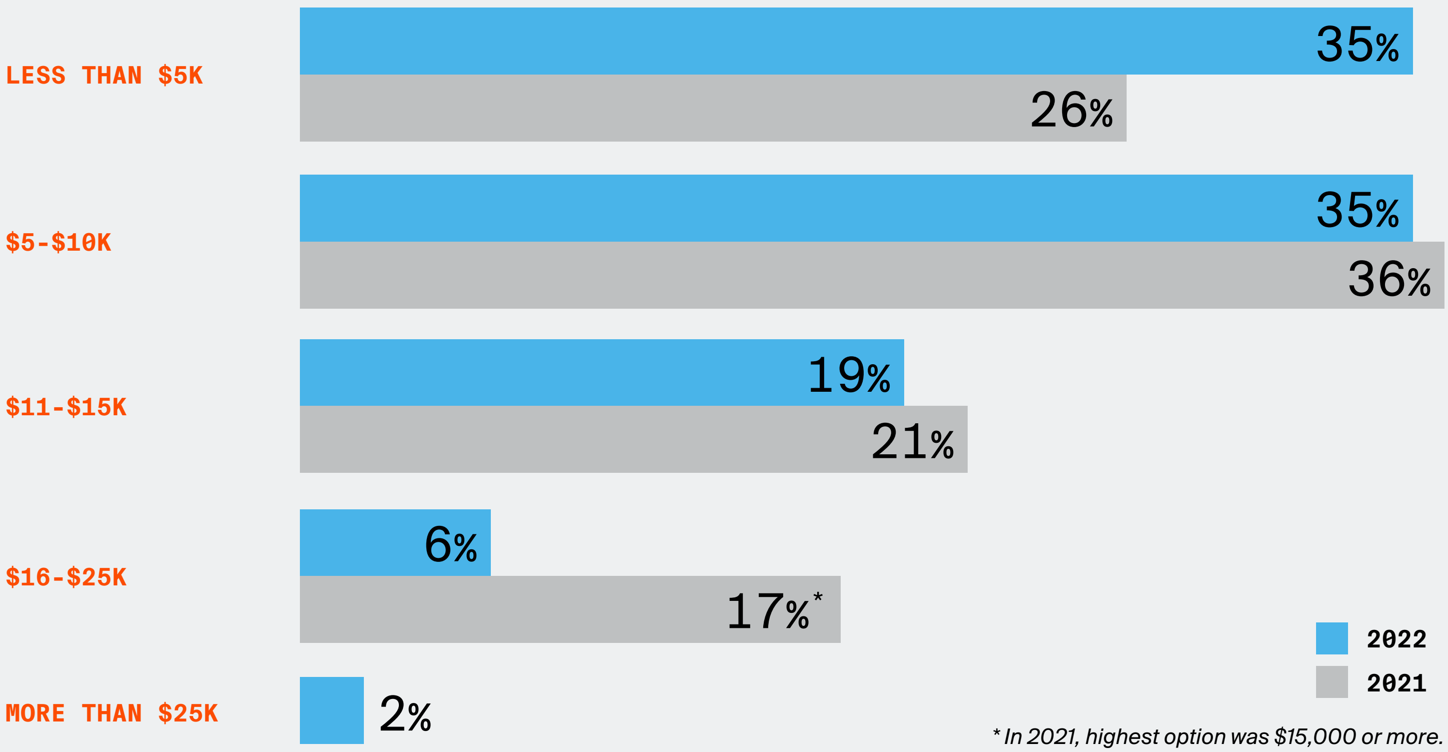
Engagement Fees *CONTINUED*

Monthly retainers, by contrast, have declined somewhat. The number of advisors charging $16,000 a month or more was 8% this year, down from 17% last year. About one-third of advisors charge $5,000 or less, and another third charge $5,000 to $10,000.

Moving forward, firms are weighing competing factors in setting their work fees. Slowing volume and increasing competition are forcing fees down. Yet, in the face of rising inflation and falling success rates, many see a need for higher retainers.

"There may be pressure from clients to reduce our fees in the future," said Jarmo Kuusivuori, CEO of Wolfcorner in Helsinki. "Now we have pressure to increase our retainers because our costs are increasing."

What is your most common monthly engagement/work/retainer fee?



** In 2021, highest option was $15,000 or more.*

Observations: Engagement Fees

We've increased our upfront fees, given the market uncertainty.
—Associate Director, Investment Bank, London

Deals are getting more difficult to complete, and we expect to increase our pre-deal charges. *—Evgeni Kanev, Managing Partner, Maconis LLC, Sofia, Bulgaria*

Fees should be increased with inflation.
—CEO, Corporate Finance Boutique, London

We prefer fixed fees over success fees. And we've been able to increase our daily rate. *—Nicolas Rädecke, Partner, Troesser & Co, Hamburg, Germany*

Success Fees

Success fees, typically a percentage of the transaction value, continue to be the bulk of revenue for merger advisors. Nearly half (45%) of advisors charge a flat-rate percentage for any deal size. About 30% use what is known as the Lehman formula, where the percentage decreases for large deals. Another 19% use an accelerator formula, which increases the rate as the deal size increases.

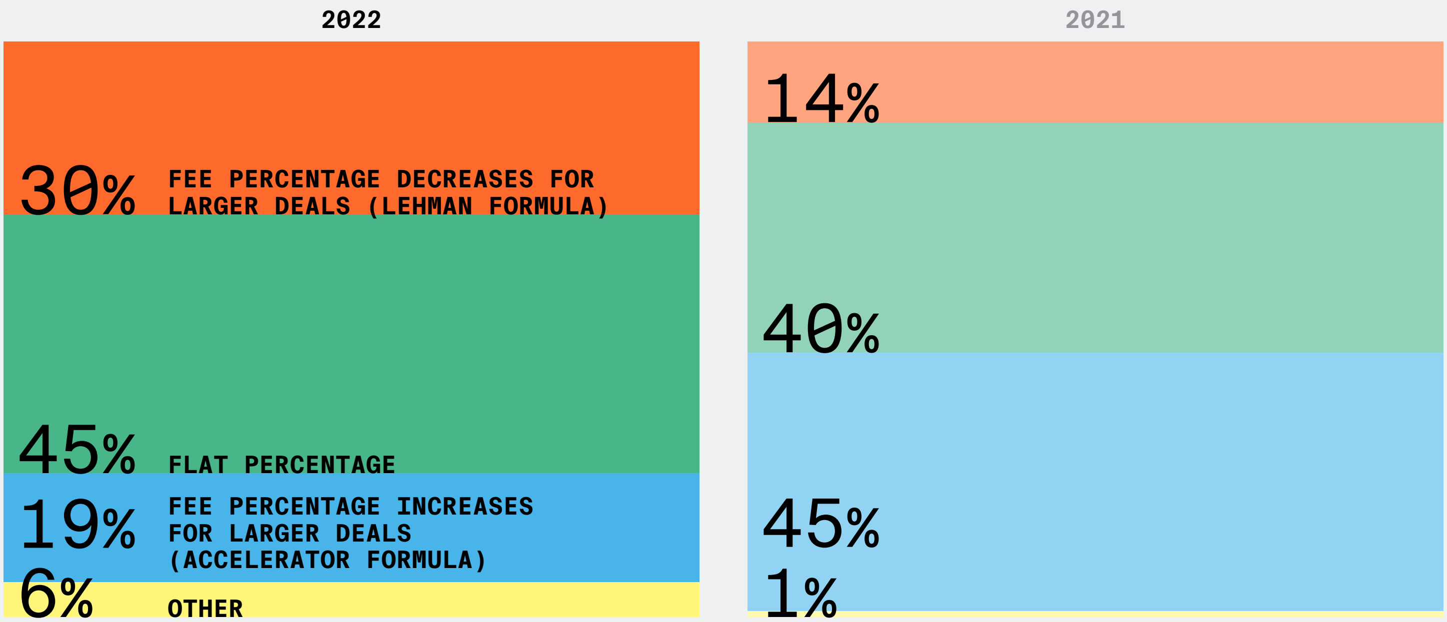
This represents a shift from last year when the most common structure was the accelerator formula followed by a flat percentage.

When we asked advisors what their typical success fee rate would be for deals of various sizes, the levels were slightly lower than last year.

The most common fee for a $5 million deal is between 4.1% and 6%. For a $150 million deal, the most common fee is less than 1%.

Of several factors that go into setting a sell-side success fee, the complexity of the transaction was the most commonly cited, followed by the engagement size.

For your sell-side success fees, what is your most common structure?

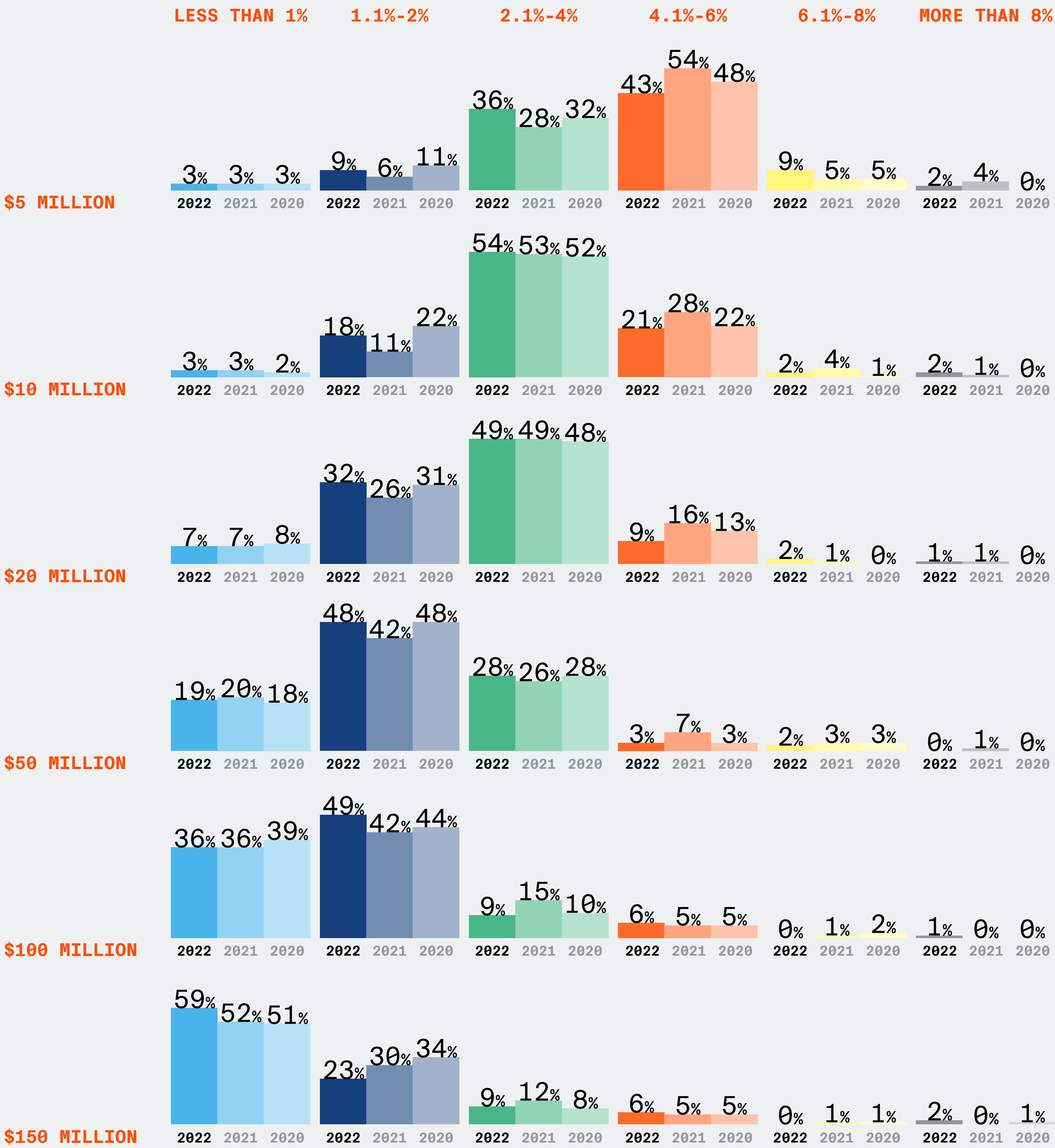


Contributor Commentary

Success fees remain the predominant source of revenue for M&A firms. In 2022, there has been market resistance to flat fee percentages and it is clear that advisers have had to charge lower percentage fees on larger deals – a trend that seems likely to continue. Fees are more susceptible to risk factors than last year, reflecting the triple whammy of Ukraine, COVID-19 and Brexit, all of which have increased transaction uncertainty. ***–Mark Eardley, Langcliffe International***

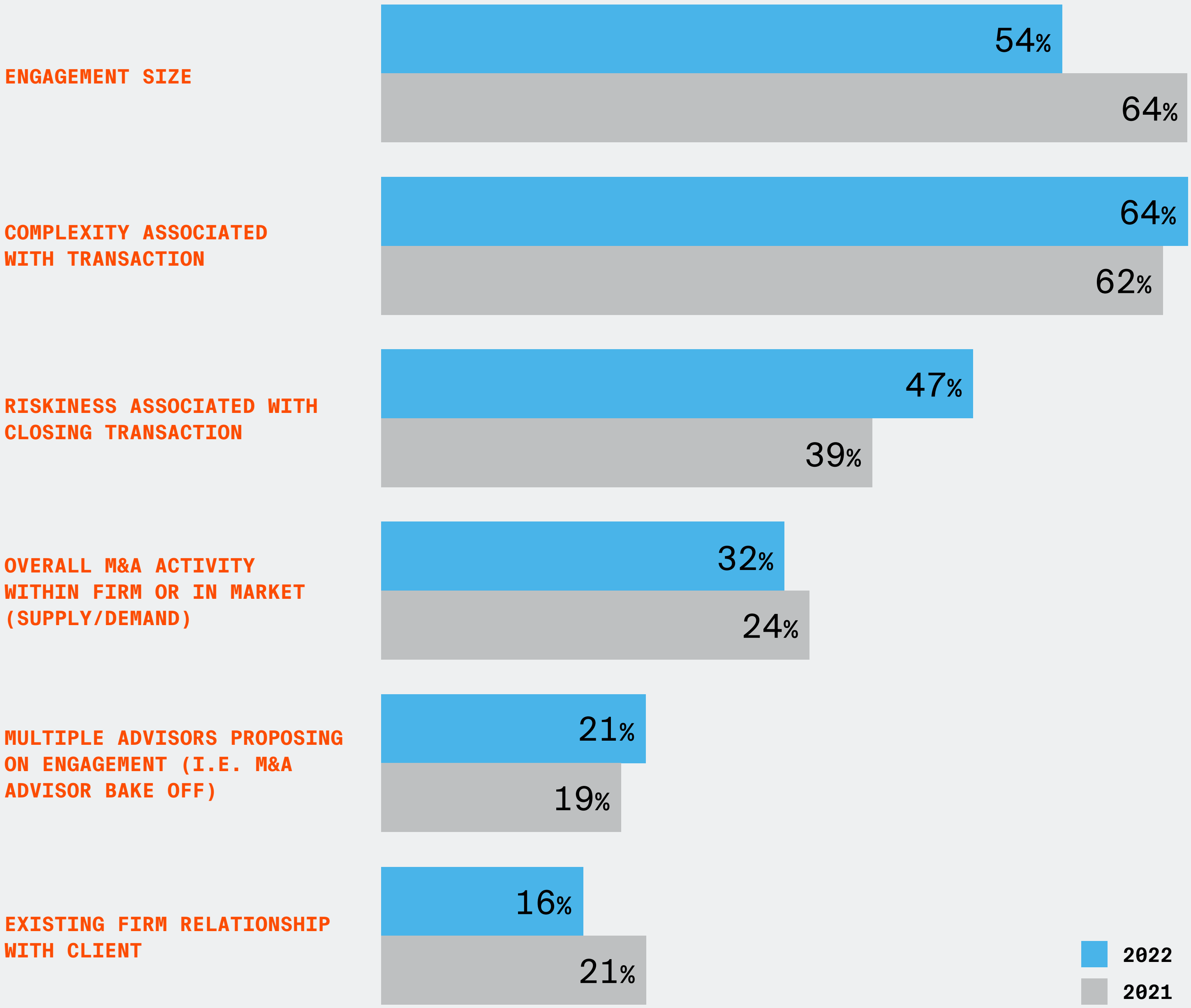
Success Fees *CONTINUED*

What would your success fee be on a deal of the following sizes?



Success Fees *CONTINUED*

What factors are taken into consideration when proposing a success fee percentage for a sell-side engagement?



Observations: Success Fees

We have managed to sustain the levels of our success fees overall.

—Nedko Kolev, Partner, Nextoria, London

On selected sell-side mandates, we're partially exchanging retainers for increased success fees, while we do not give up the exclusivity.

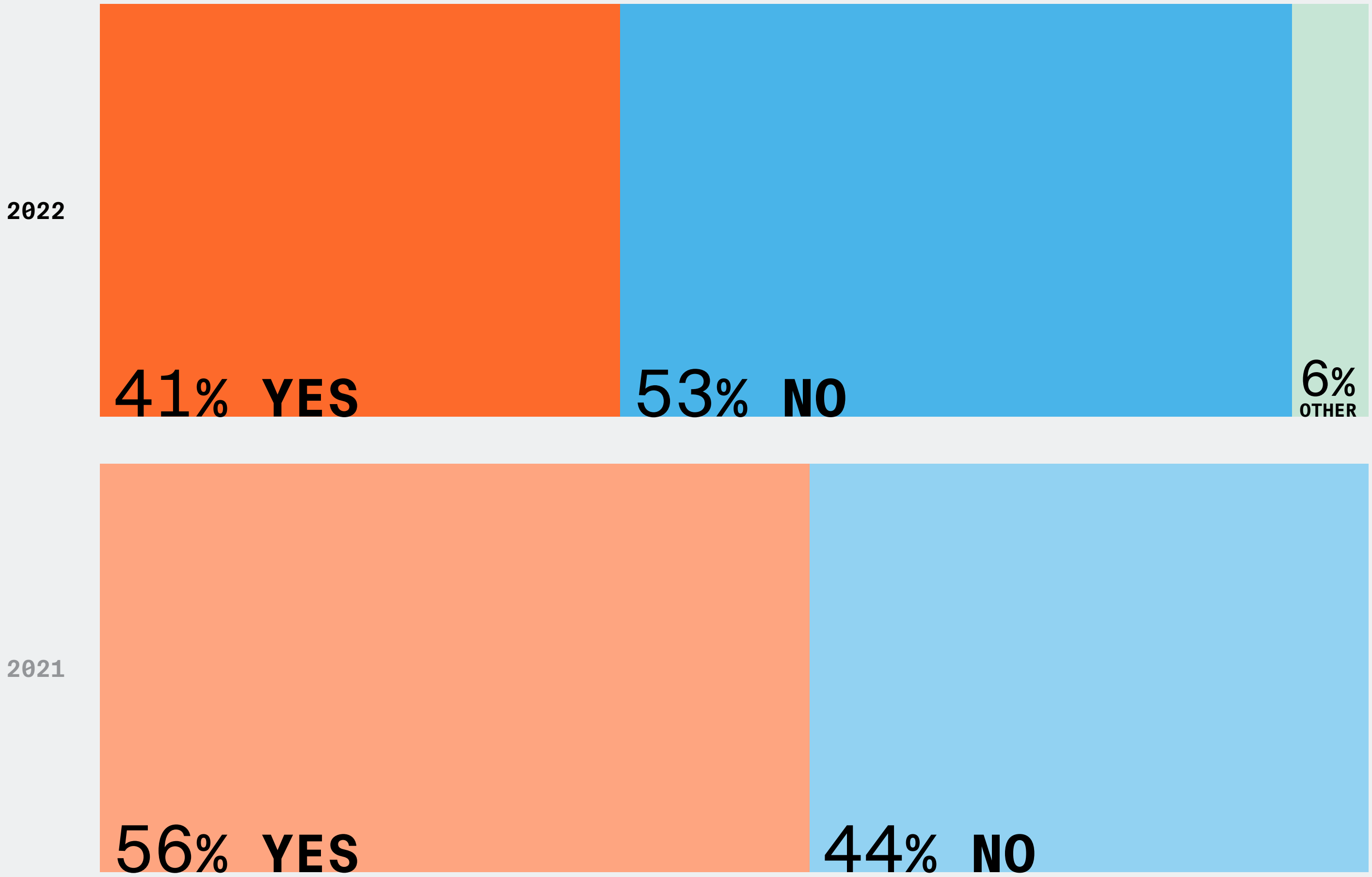
—Guidalberto Gagliardi, CEO, Equity Factory Srl, Milan

Additional Terms

Beyond the fee levels, the additional terms associated with the engagement can have a significant effect on the overall revenue from a deal. Two-fifths of the advisors charge break fees that are payable when a client rejects a bona fide offer, slightly more than last year. More firms (72%) now have minimum success fees, up from 58% last year.

The practice of deducting engagement fees from success fees is less common this year. In 2022, only 41% of firms net their success fees against engagement fees, down from 56% last year. Some advisors said they only agree to this structure when responding to pressure to cut fees.

Do you most commonly deduct collected engagement/work/retainer fees from success fees earned?



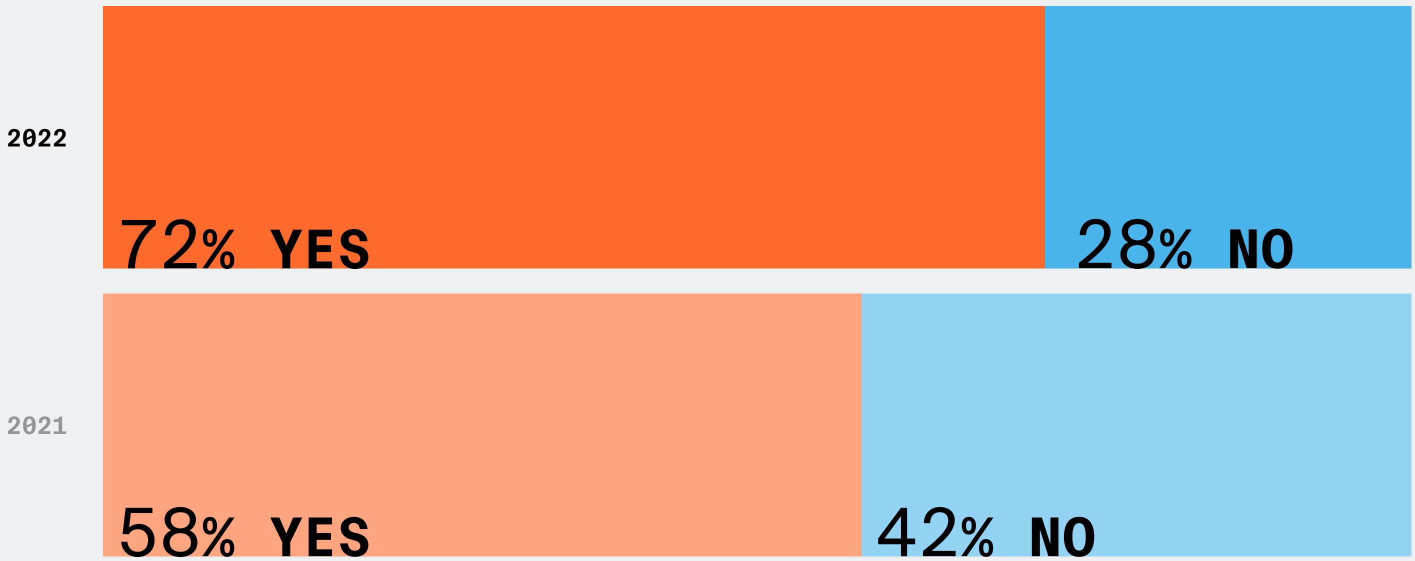
Contributor Commentary

The increase in minimum success fees is, perhaps, a reflection of the uncertain trading outcomes for clients and a desire for advisors to protect themselves against these. *—Mark Eardley, Langcliffe International*

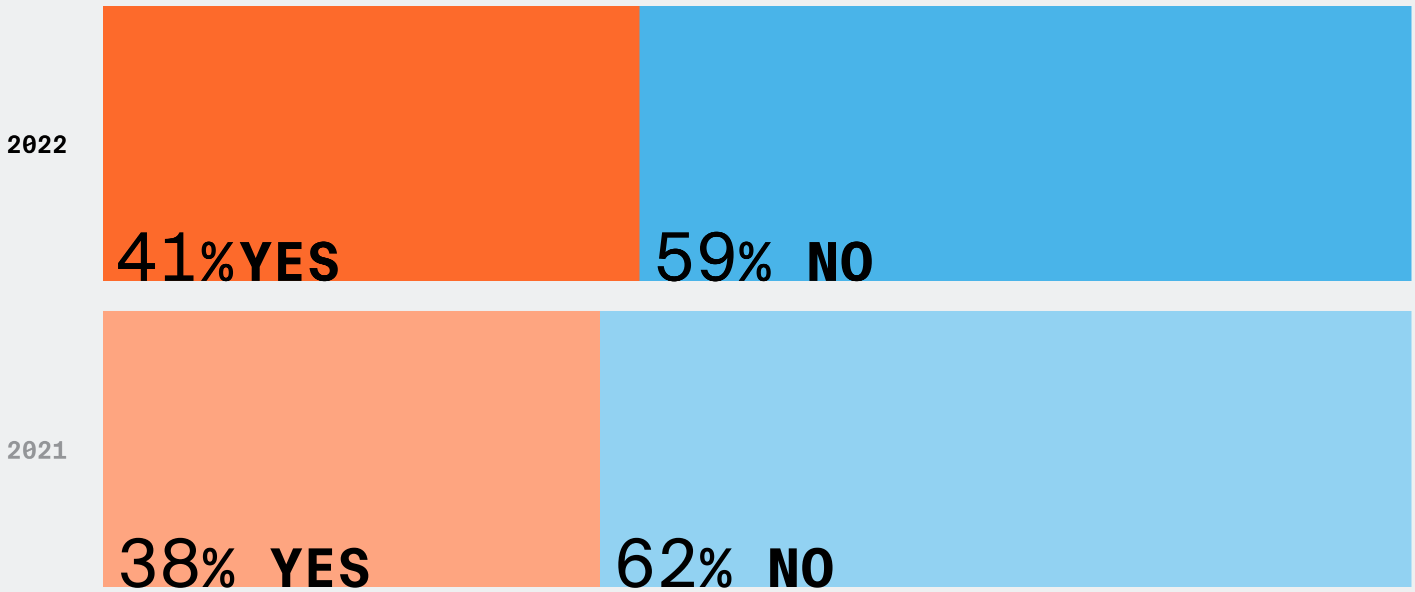
Additional Terms *CONTINUED*

The timing of success fee payments is becoming more of an issue as a larger number of deals use an earn-out structure, where part of the sale price is delayed and contingent on the performance of the acquired company. In such cases, slightly more than half of the advisors (56%) said they expected payment for the full transaction amount at the time of closing. The rest said they would accept their success fee over time as the seller is paid. Collecting the fee at closing, of course, requires some negotiation.

Do you most commonly charge a minimum success fee?

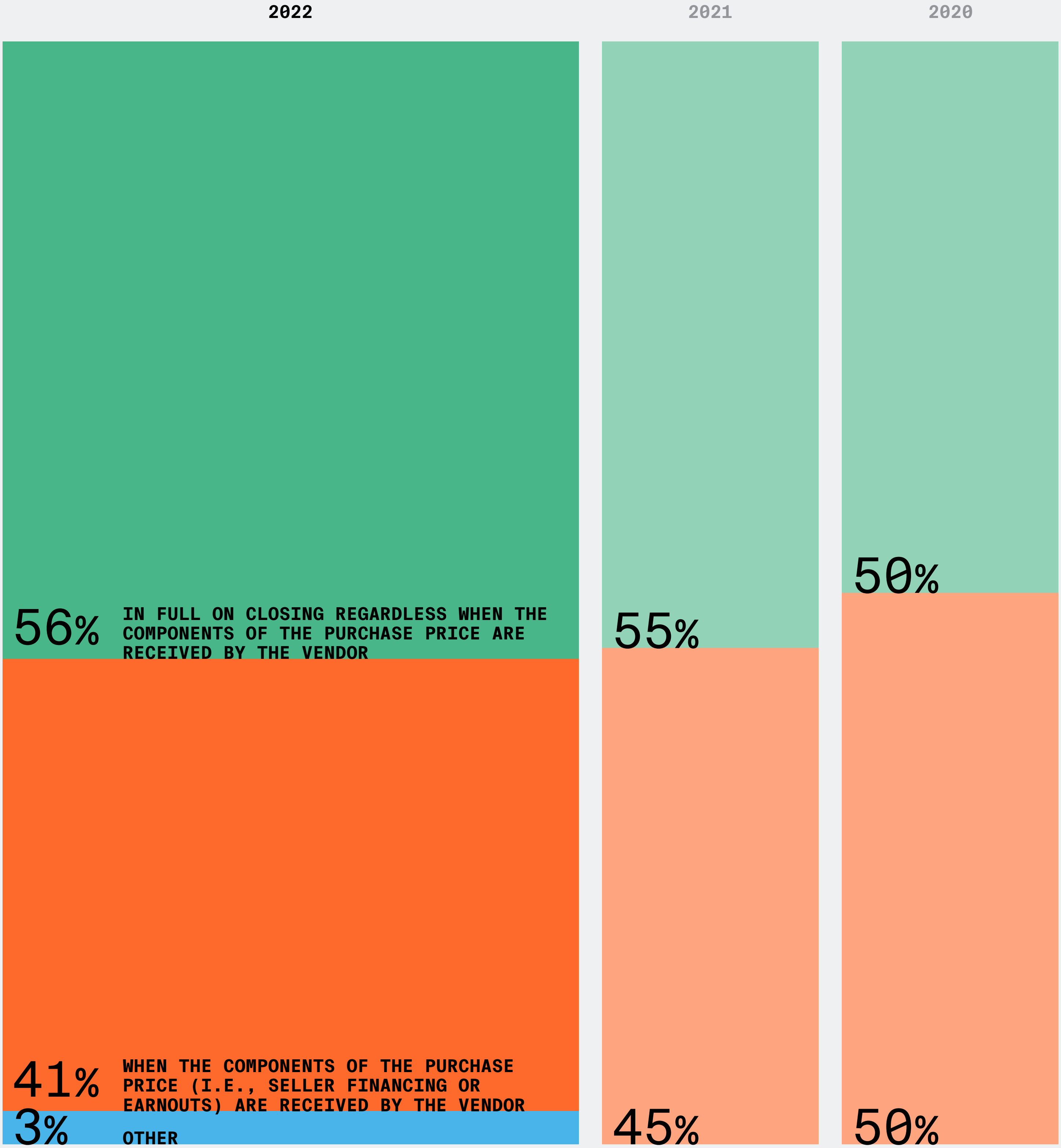


Do you commonly charge a break fee when a client rejects a bona fide offer?



Additional Terms *CONTINUED*

If a success fee is earned, when is it most commonly paid?

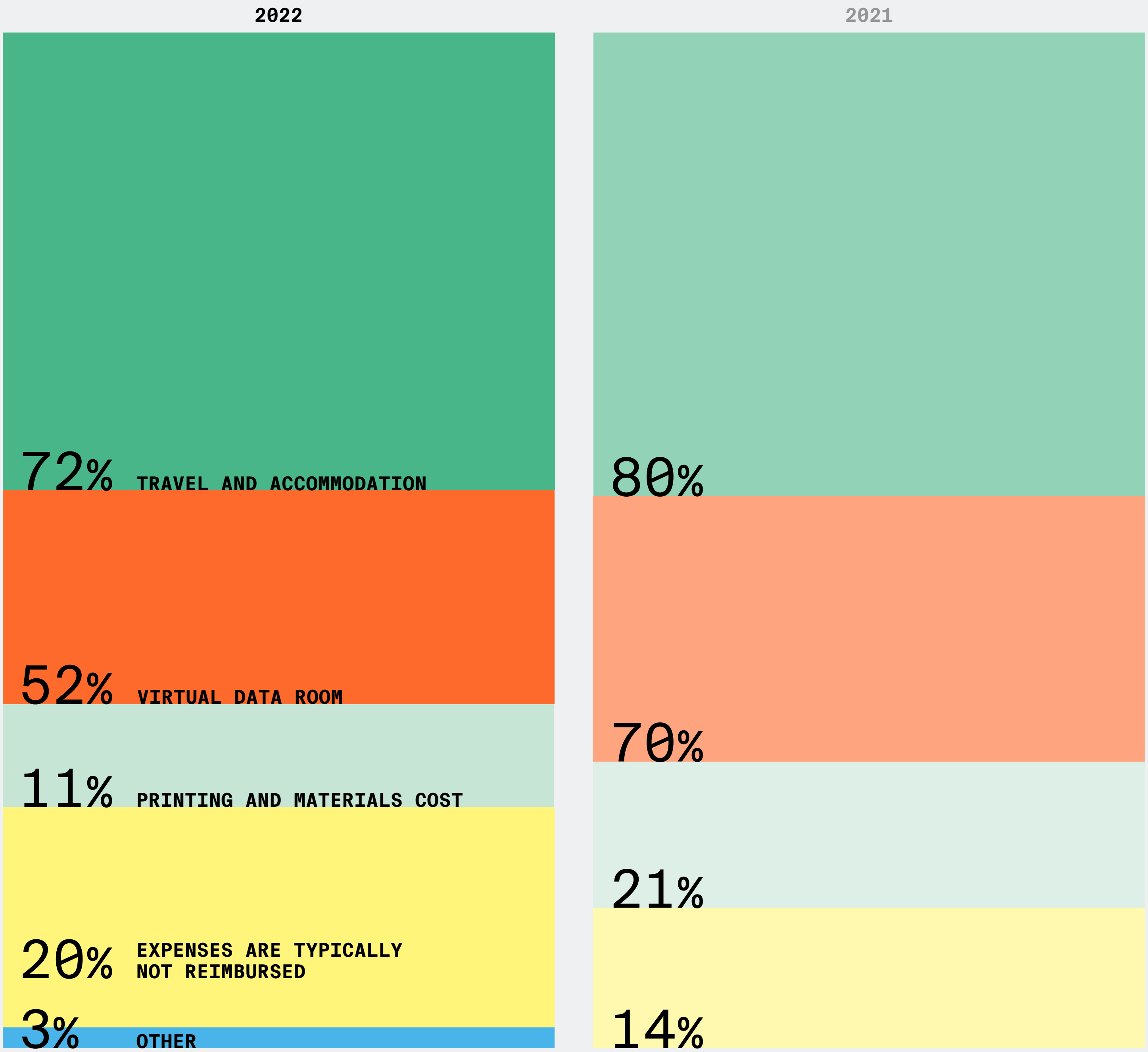


Additional Terms *CONTINUED*

“We agree on the likely earn-out amount and calculate the success fee based on the total enterprise value,” explained a director of a corporate finance boutique in West Sussex, UK.

Travel and accommodation are the expenses most typically reimbursed by clients. One-fifth of advisors say that their expenses are not reimbursed, a significant increase from last year.

What expenses incurred by your firm on sell-side engagements are most commonly reimbursed by your clients?



Profitability and Pressure to Cut Fees

Very few advisors (15%) said they are seeing increased pressure from clients to cut their fees. That's down sharply from last year when 29% said fee pressure was increasing.

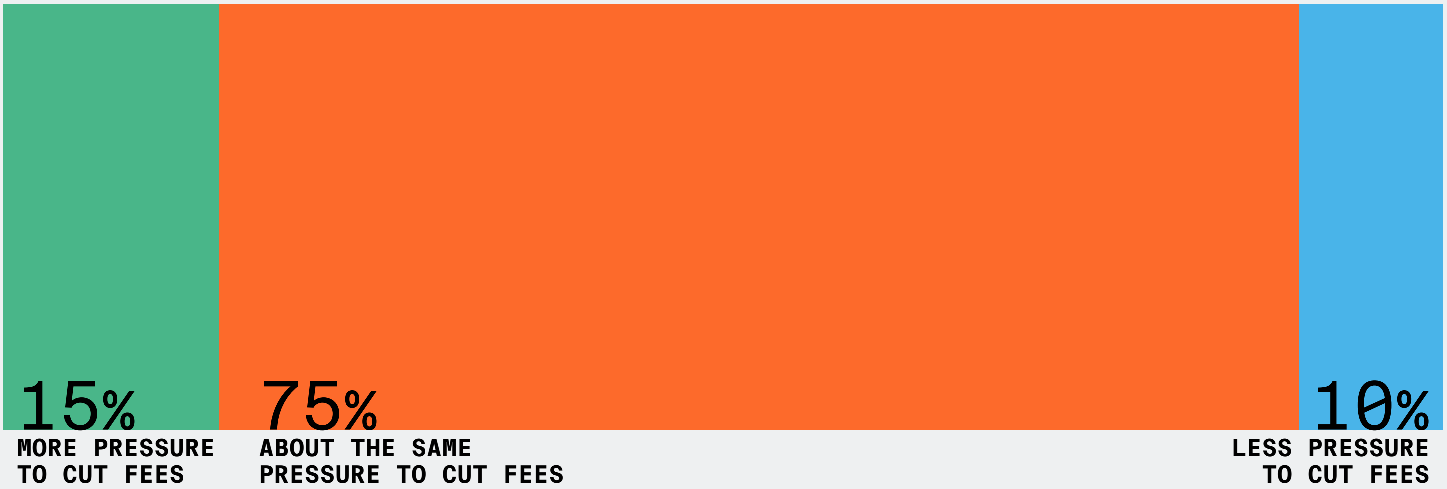
When we probed further, some advisors did say they have done some fee cutting or have alternative structures they propose to clients that balk at their standard rates.

"If there is pressure on fixed fees, we may increase success fees. And vice versa, but up to a limit," said the director of an investment bank in Nicosia, Cyprus.

Contributor Commentary

Notwithstanding the improved position of 2022, resulting in increases in fee level and profitability, the many headwinds (with an inevitable loss) will impact both these measures in 2023. *—Mark Eardley, Langcliffe International*

Compared to last year, how has the pressure from clients to cut fees changed?



Observations: Pressure to Cut Fees

For deals with earn-outs, we offer a timing "discount" with different percentages for each fraction of the payout. *—CEO, Corporate Finance Boutique, Budapest*

We've reduced fees by about 5% because reluctant buyers are slowing the progress on deals. Overall activity is also very slack. *—Founder & CEO, Business Broker, Amsterdam*

We sometimes agree to deduct the engagement fee from the success fee. Or we have a lower success fee if the price is over £5 million. *—Managing Director, Business Broker, Cheshire, UK*

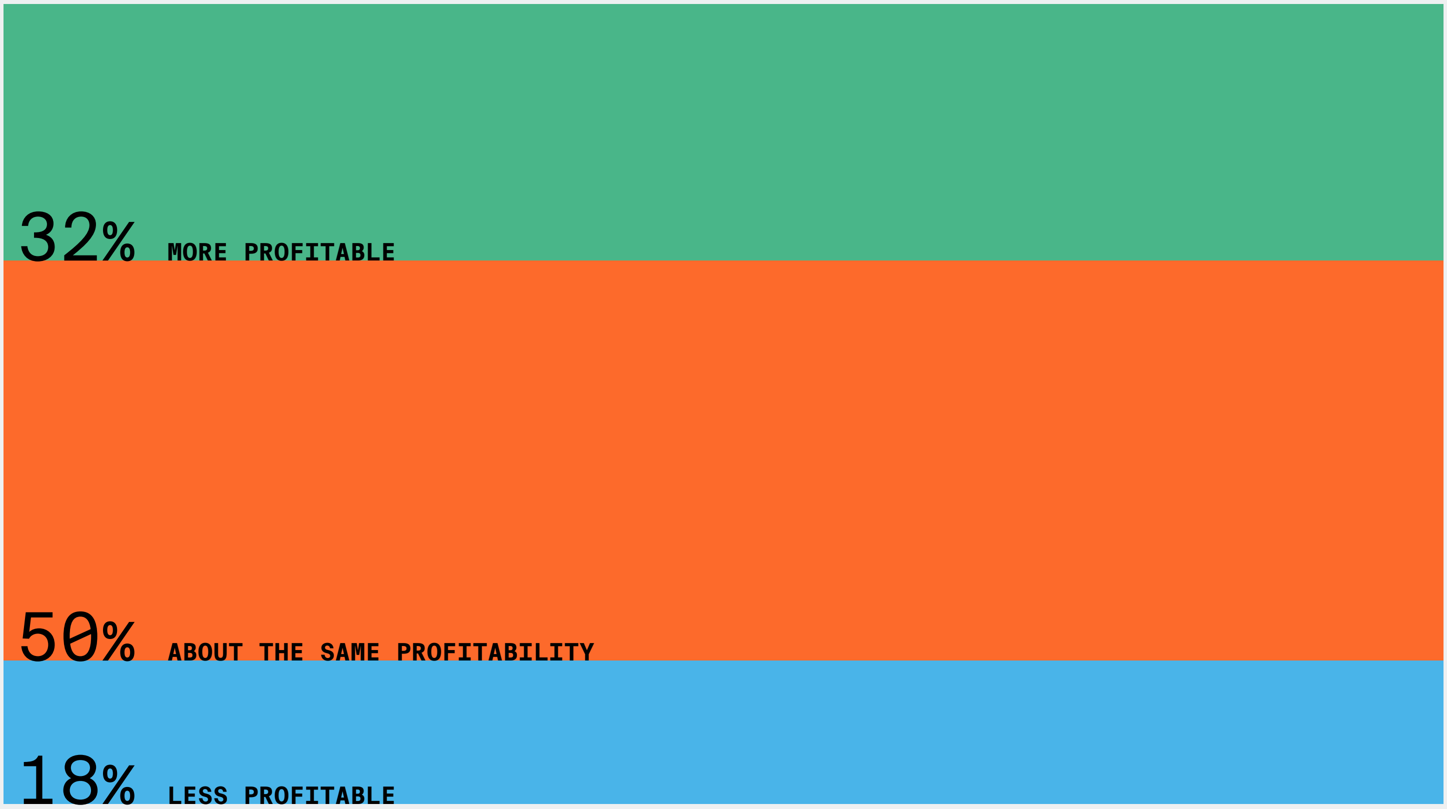
We are seeing pressure to deduct stock from the fee calculations and to reduce our success fee for any sale below their target price. *—Managing Director, Investment Bank, London*

Profitability and Pressure to Cut Fees *CONTINUED*

Putting all these factors together, most advisors were quite profitable in 2022. Half said their profitability was the same as it was in 2021, while 32% said their profitability increased. Only 18% said their firm was less profitable this year, and just 1% said they didn't make a profit.

The advisors at firms with increased profitability said they were actively managing their costs while devoting more energy to marketing. Those with more profit pressure cited rising expenses from staff and consultants.

Considering both fees and expenses, how has the profitability of your M&A business changed in 2022?



Observations: Factors That Affect Profitability

It's taking more time to close deals with the uncertainty of the pandemic and the political situation in Europe.
—Berislav Cizmek, Founder & CEO, CBBS, Zagreb

The Ukraine war has had a negative impact on the business environment. ***—Evgeni Kanev, Managing Partner, Maconis LLC, Sofia***

Profitability comes down to deal timing. Our back office expenses don't necessarily coincide with when we receive deal completion fees, for example.
—Justin Levine, Managing Director, TheNonExec Limited, Poole, UK

Outlook and Conclusions

Middle-market advisors, as we've said, are optimistic and determined, but they aren't oblivious to reality.

When we asked about their expectations for next year, most of them predicted a challenging year.

While volume may slow and margins may be squeezed, most of the advisors said they would be able to maintain their fee structures because of the value of the service they deliver.

Observations: 2023

Unlike in the large and mid-cap segments, we do not (yet) observe decreasing M&A activities in the small-cap healthcare segment. Appetite from both financial sponsors and strategic investors is still high.

—Tim Sachs, Managing Partner, Tim Sachs Consulting, Munich

I expect that interest in M&A in 2023 will increase. But I don't think fees will go higher. ***—Berislav Cizmek, Founder & CEO, CBBS, Zagreb***

Next year will undoubtedly be more challenging as the macroeconomic climate within the UK becomes tougher. ***—Principal, Business Broker, London***

Concluding Comment

Given our central position in the European M&A lower to middle market, Langcliffe has exceptional visibility of the market and lead indicators.

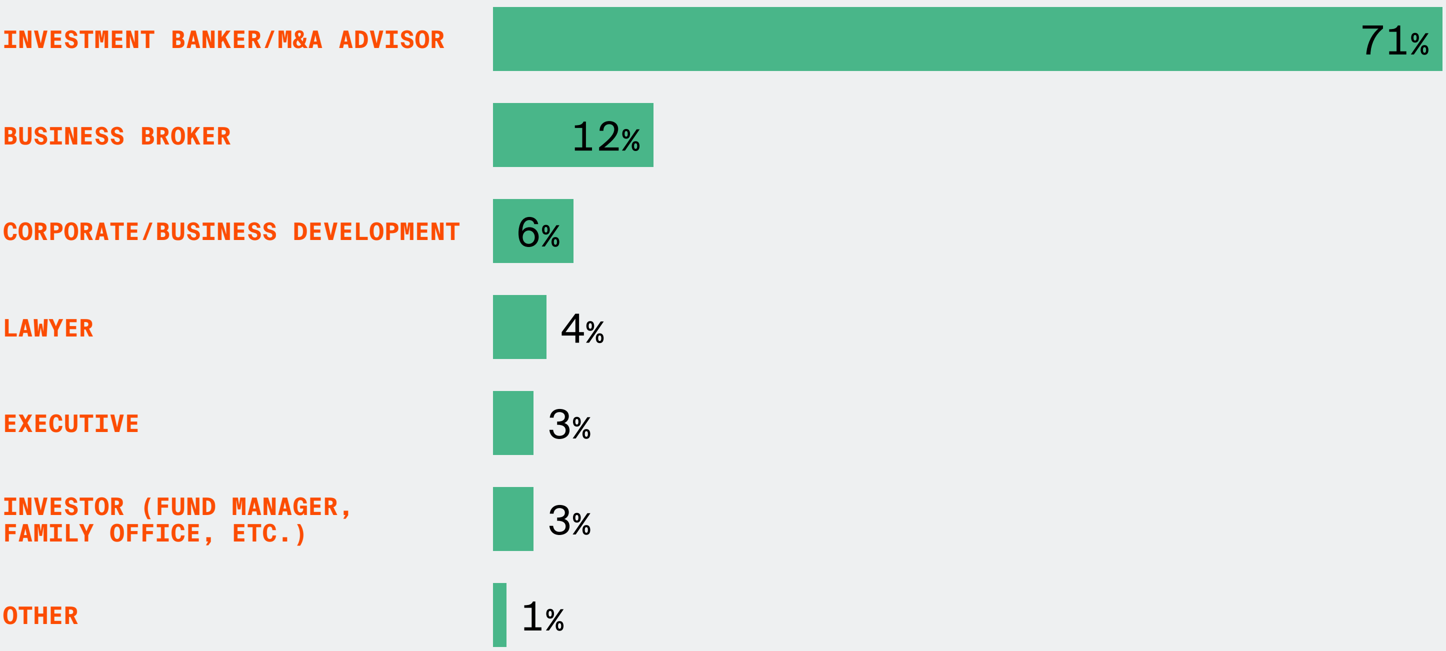
There are clearly time lags in the M&A market. Whilst completions held up very well to Q3 2002, other KPIs in our business have started to suggest a softer market ahead. In particular, statistics relating to deal closing time have increased, whilst the conversion ratio from heads to completion has decreased. Similarly, there has been a reduction in the number and quality of new mandates coming to the market.

This suggests that the M&A market in 2023 will be weaker, although high quality assets will continue to be in demand. The impact on M&A revenues and profitability is likely to be negative. Hopefully, it will be short lived.

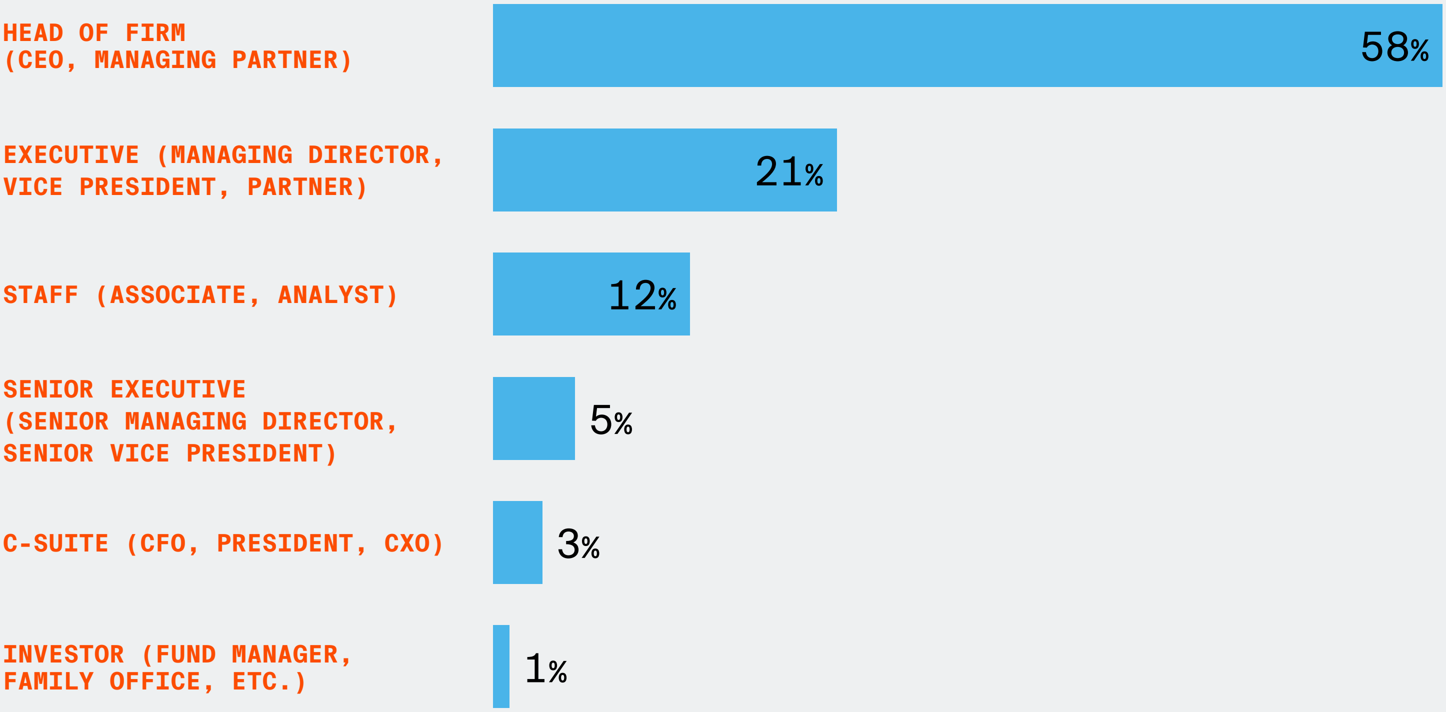
—Mark Eardley, Langcliffe International

Appendix: Respondent Demographics

Which of the following best describes your current occupation?

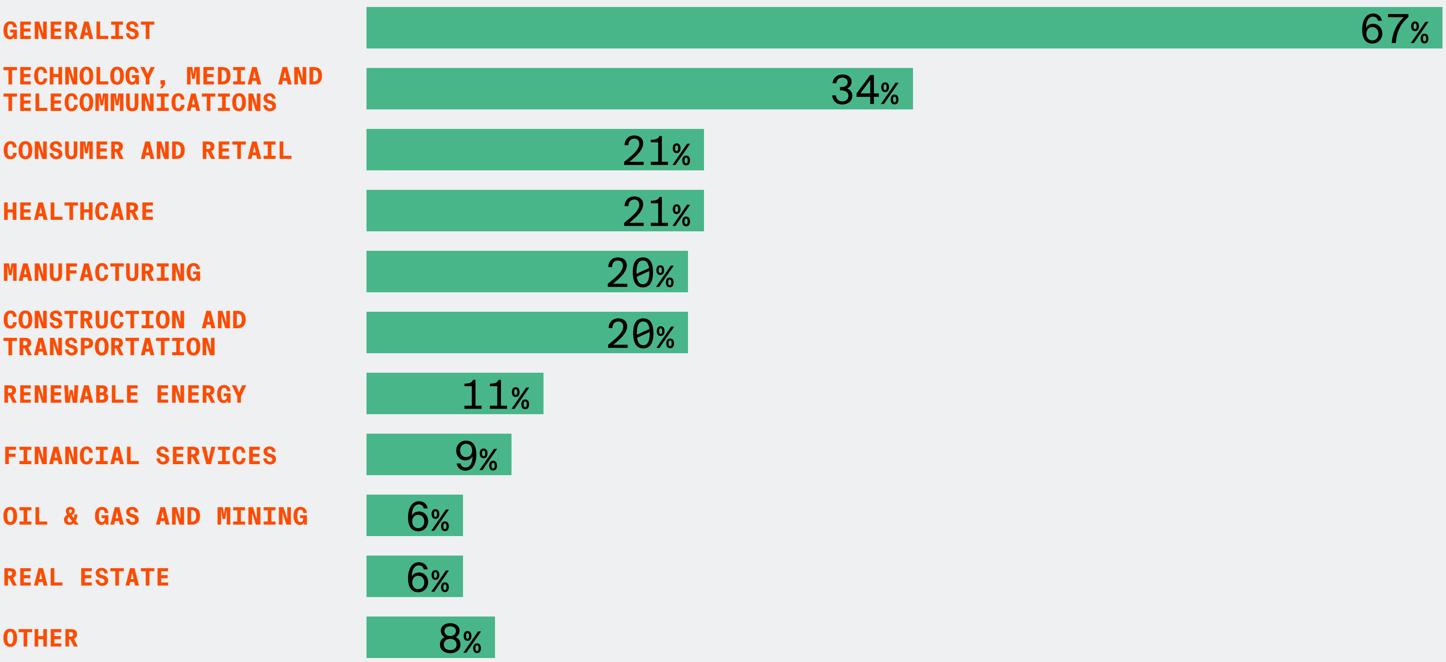


What is your job title?

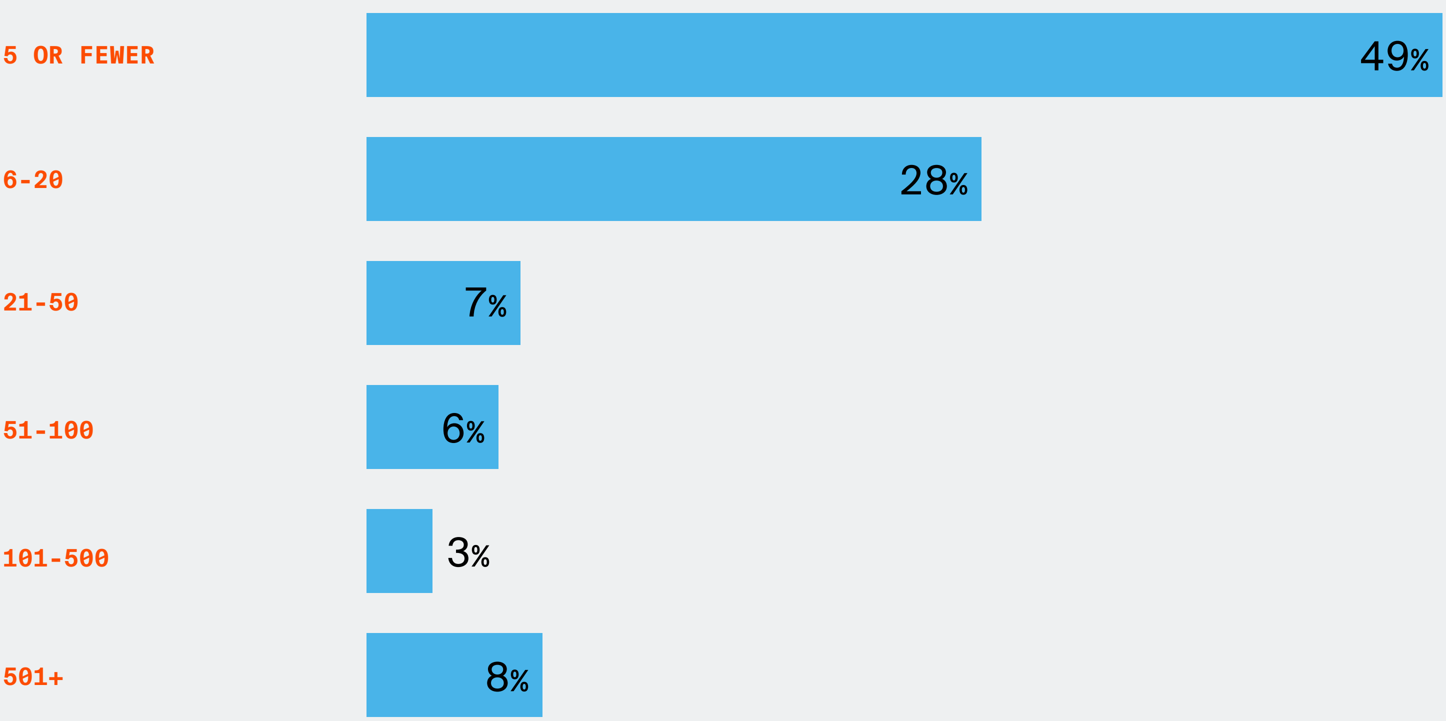


Appendix: Respondent Demographics *CONTINUED*

Do you specialize in any of the following industries?

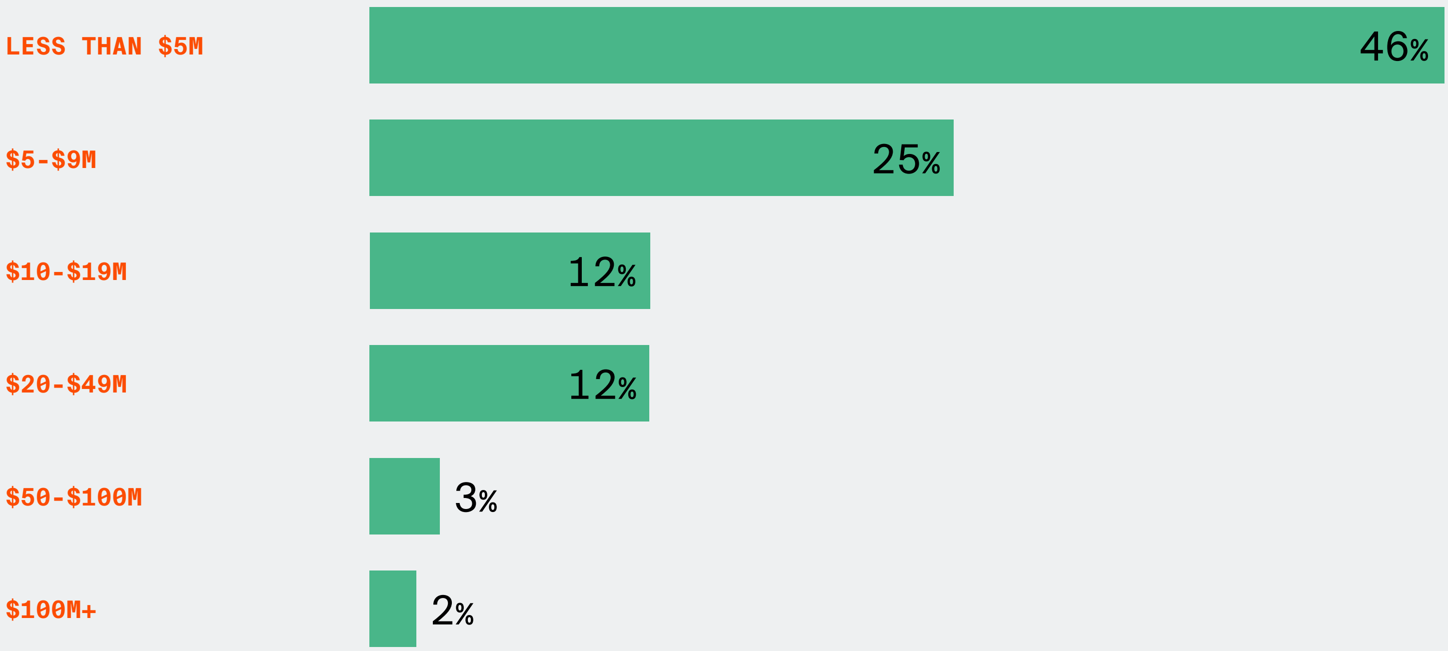


How many total employees does your firm have?

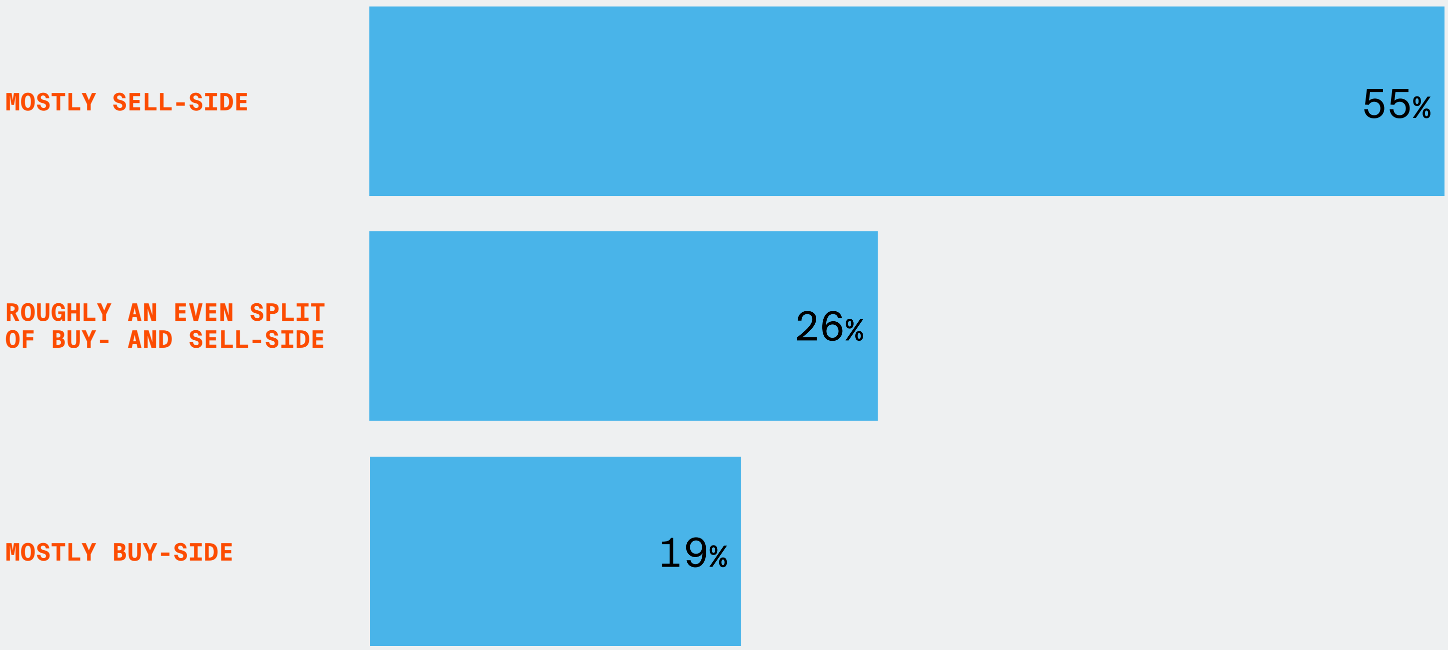


Appendix: Respondent Demographics *CONTINUED*

What is your minimum transaction value?

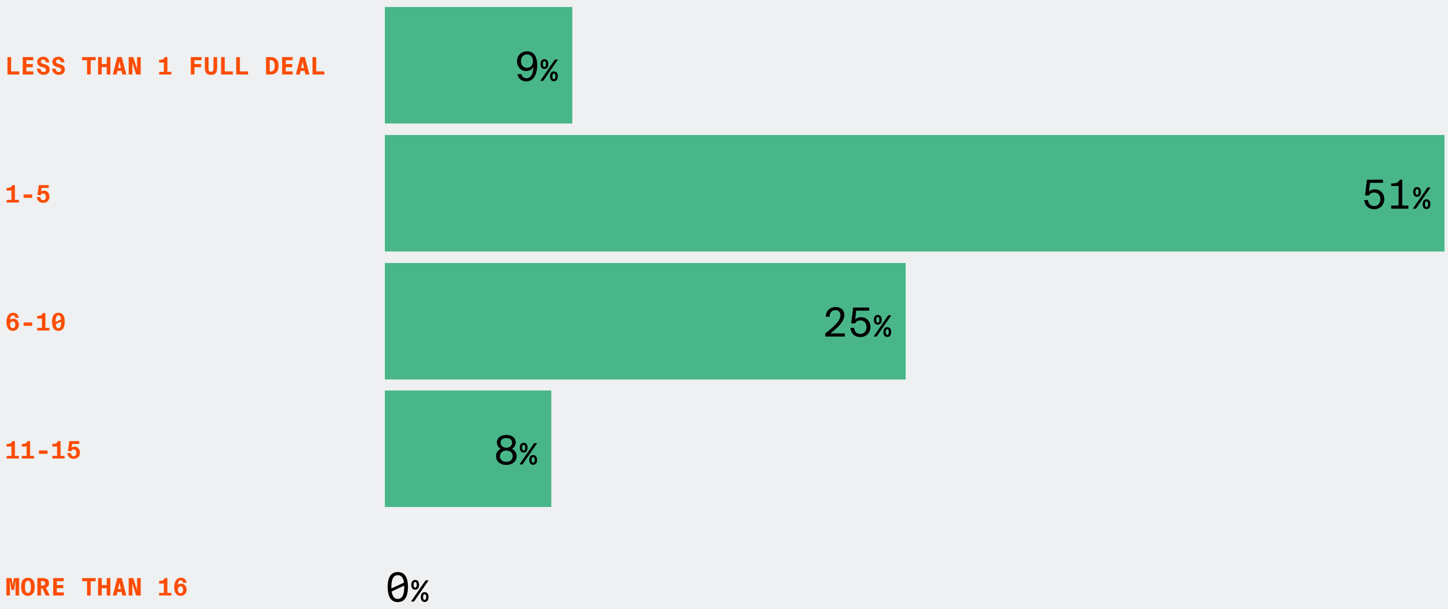


Are your clients:

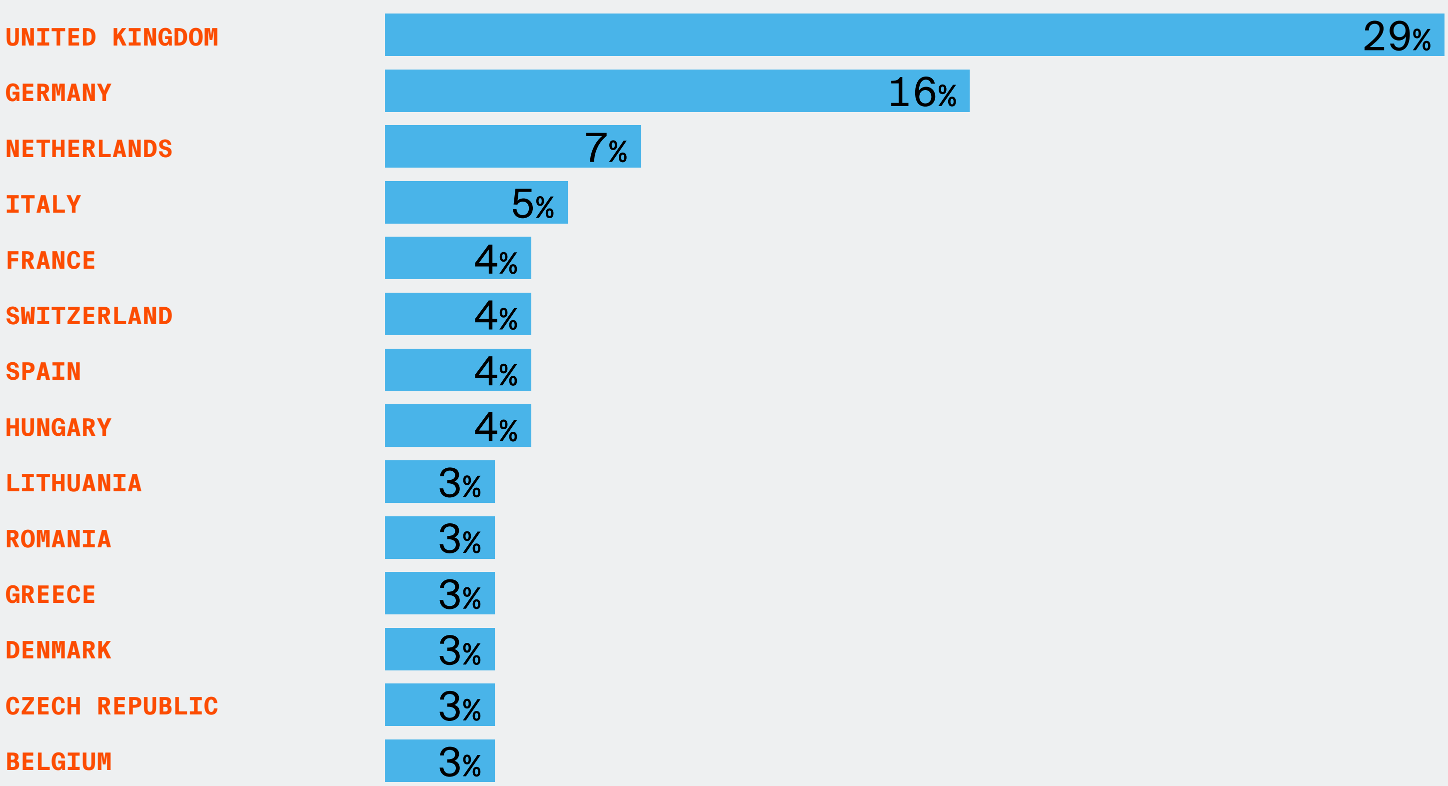


Appendix: Respondent Demographics *CONTINUED*

How many sell-side engagements does your firm work on in an average year?



What country do you primarily work in?



About Firmex

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