Jon Moulton's Diary

Premiums on exits have taken a knock recently, so much so that valuations need a more sceptical eye

Veteran financier Jon Moulton has been involved in buyouts, turnarounds and venture capital since 1979 with firms such as CVC, Permira, Apax, Alchemy and, most recently, Better Capital, where he has been the chair since 2009

Hard numbers show a worrying trend. In 2020 (depending on which data-set you use) exits on average were done at prices 35% to 51% above the last reported valuations.

The 2025 numbers are now coming in. Data shows results from no premium to a discount of 5%.

These are much the worst industry results — ever. As I cover below, all kinds of reasons to justify this loss of premium are put forward.

The link of this premium/discount to actual returns is messy to analyse — the pre-exit values could be weeks or several years old.

Managers may have raised values too early to push reported returns up to help fundraising, and reality only surfaces as exit finally arrives.

Continuation vehicles are nearly always set up at or very close to the last reported value. Obviously, this may be driven by the private equity firm seeking fees that stretch into the distance and, potentially, hard luck for non-participating investors.

Sales processes have undoubtedly stretched out – this gives a greater chance of the carrying value being adjusted to a price based on the less theoretical price information coming from the sales process.

But simple reluctance to write assets down is a clear factor – illustrated by the 2% PE industry write down in 2022 when stock markets fell 22%. This is obviously a big factor. Probably the biggest.

Exit pressure

Then there is simple pressure from investors pushing very hard for exits from ageing funds, which might cause sales in non-optimal circumstances – back to continuation funds!

A less attractive possibility is the use of relatively ephemeral valuation measures that are far away from actual cash flows.

As these techniques — for example, recurring revenue multiples, or heavily adjusted earnings before interest, taxes, depreciation, and amortisation — drop out of favour, a decline in portfolio values is generated.

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It is also postulated that the high level of debt refinancings (including net asset loans and portfolio level debt) bring more "robust" valuers to the table in assessing their credit risk. This may result in the banks taking a less cheerful approach to values. But I cannot imagine GPs writing to investors saying that they had been told by their bank to drop values!

Many investors clearly are sceptical of valuations – discounts on listed private equity vehicles are very variable – and there have been discounts of single digit percentages to 50% plus in recent days.

A more pessimistic view is that competition for deals and low economic growth both tend to reduce returns and in an effort to keep the story going valuations are raised early, with weak grounds for doing so.

The arrival of almost conglomerate permanent capital funds, of course, means that this subset of private equity does not need to worry about exit values much at all.

I rather fear that the scale of PE is now too large. There is more competition for deals. Juicy targets with lots of low hanging fruit are not common any more. Returns may be in slow decline and will continue to be weak until supply and demand are more in line. If so, then perhaps the loss of premiums on exits is simply part of a lower return environment.

Positive feedback

My article last month on the downsides of government private equity clearly had some support. I got a few friendly calls. A rarity! And no feedback from the government side. These friendly calls broadly said that they shared the concerns, but they could not speak out for simple economic reasons.

The disjuncture between reported valuations and exit values could be a harbinger of a long period of lower returns

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