

Notes from the frontline

Frozen debt markets, volatile public markets and government-backed banks increase the need for growth investors, writes John Bernstein.

Posted - 12 Nov 2008 09:10 GMT

The terms “growth” and “recession” don’t normally go hand-in-hand, but even in severe downturns, such as the one that most people believe we are now entering, companies with rapidly growing revenues and profits do exist and will continue to attract capital for their growth.

These are not just the debt collectors and insolvency practitioners that most people associate with counter-cyclical revenues. They include:

- Companies with breakthrough technologies that help customers increase revenues, manage costs or drive efficiency. Examples of this might include those focused on monetising online opportunities such as AKQA, a digital marketing media company or software-as-a-service companies;
- Offshoring and out-sourcing companies which help companies in mature markets restructure their businesses in times of hardship to reduce cost and improve services; a key trend which takes on even greater importance in weaker economic environments. Xchanging, a UK-based leading provider of outsourced based services is growing well and continues to expand globally;
- Healthcare companies that have long-term growth drivers and government or non-discretionary spend: Wagne Stibbe, a lab-testing healthcare company based in Germany is showing strong organic revenue growth;
- Processing or trading platforms that depend on volume rather than upwards or downwards movements in prices such as Saxo Bank, an online foreign exchange trading company.

Capital provided by growth equity investors becomes increasingly important for growth companies when other forms of financing – such as debt or public equity – are no longer available. Debt markets are currently frozen and government ownership of banks is unlikely to lead to a quick return to the cheap and easy lending environment of the mid 2000s. And with public markets both volatile and battered, it is unlikely that many IPOs or rights issues will be successful in the short term at least.

Both private and also public firms will look to growth equity investors to raise capital to fund their operations. Moreover, some of the best companies will also see this downturn as an opportunity to build scale by completing acquisitions, consolidating competitors or building geographic or product extensions at a time when asset prices are more attractive. The growth equity segment of the PE industry will be an attractive source of this strategically oriented funding.

Equity capital is the lifeblood of growth companies whether public or private, and the demand is as strong as it has ever been. Whereas in previous recessions the pool of private growth capital available to fund the best growth companies was relatively small, this pool is now dramatically larger, and all-equity investments of €50 million to €500million (for each investment) are available from a number of investment firms. In the recession of the early 1990s, the entire funds of most venture capital/private equity firms were less than €50 million to €500m.

In addition to capital, these growth investors provide industry specific expertise, global networks and other resources to assist companies with their growth strategies. Growth capital investors may therefore play a more important role than at any time historically in backing the best companies even in dark economic times, and by doing so should help make the clouds a touch lighter.

John Bernstein is a London-based managing director for General Atlantic and head of its European operations.



John Bernstein