Where is the corporate road heading?

Brian Pound,
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AS the retired founder of CVS, I have watched with interest the recent comments in the veterinary press about changes to the market and predictions for the future. When I started the company, reactions to corporate practices were all doom and gloom, both for the future of the profession itself and of incorporation.

The more recent concerns about the viability of the sector were triggered in 2017 by Medivet taking a break in acquisitions, followed by Pets at Home and its subsidiary Vets4Pets announcing some consolidation and practice closures, and then, most recently, CVS reporting a slowing of profit growth, and thus a review of their acquisition strategy.

None of this should come as a surprise. The market is maturing and the rapid growth in corporate ownership of practices over the past 20 years will inevitably slow because the number of independents wishing to sell will start to dry up. The boards of every corporate should be putting plans in place to manage their businesses when acquisitions do not represent the biggest element of their business growth.

The venture capitalists (VCs) who fund most of the current corporate groups all have an exit plan; IVC, one of the largest corporates operating in the UK and northern Europe, has already seen numerous changes in ownership over the past eight years. Each time they've sold the company they've achieved huge multiples of EBITDA (Earnings before Interest, Tax, Depreciation and Amortisation) – some reported to be as high as 18. Compare that with the historic cost of acquiring a practice at less than 10 times EBITDA and these financiers have made a huge killing.

Now that practice owners have realised that they can get a lot more for their business, they too have been pressing for higher multiples, with current transactions reported to be peaking at 15 times EBITDA.

Although the market is slowing, for the time being the VC-funded corporate will still make a clear profit when it sells. However, with the larger groups getting bigger, there will start to be fewer buyers willing to invest such large sums of money, particularly when they realise that the current growth rate cannot be sustained.

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Investors might also become more cautious because the maths is starting to look scary. The cost of acquisition in the early days of CVS could easily be repaid within four to five years. The current high multiples being paid will take over 11 years to repay; this is regarded by most investors as being far too long.

The announcement from Simon Innes, chief executive of CVS, that the company is reconsidering its policy on the multiples it is willing to pay was unavoidable. As a listed publicly owned company, investors expect to see a timely return on their investments and a prudent level of borrowing by the business.

So where does this leave the market? The future of corporate ownership is set to change. Mars, already a huge owner of veterinary clinics in the USA, has now entered the European market and may make changes to the businesses that they buy. Indeed, the first company they acquired in the UK, Linnaeus Group, has already seen some changes in management, so there could be more.

Future mergers may also become tricky. The Competition and Markets Authority (CMA) – a regulator designed to preserve competition and prevent a monopoly – will certainly take a close look if the larger groups plan to merge as it is likely that they will hit the trigger point for intervention (ie, if the CMA believes a merger is against public interest and limits competition, it will stop the merger or insist that the company divests some of its businesses to enable it to merge). Even growth by simple practice acquisitions could put the largest groups at risk of CMA intervention if it believes these acquisitions damage competition.

In the meantime, although the independent sector has shrunk over the past 20 years, it is still alive and local groupings between practices (such as that seen with XLVets) will potentially secure their independence for many years to come.

Watch this space.

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