FT FINANCIAL TIMES

Private equity groups step up pursuit of white-collar partnerships

Accounting firms, consultancies and other professional services take outside cash to fund growth

Grant Thornton agreed to sell a majority stake to New Mountain Capital last week, the latest deal between private equity and an accounting firm © Artur Widak/dpa/picture alliance/NurPhoto

Antonie Gara and **Stephen Foley** in New York, March 18, 2023

Private equity is accelerating its pursuit of consultancies, talent agencies and accounting firms, as it targets professional partnerships in one of the buyout industry's last unconquered territories.

Two of the top-10 largest US accounting firms — Grant Thornton and Baker Tilly — have agreed to sell majority stakes to private equity in the past six weeks, and bankers and executives expect more deals to come.

With debt expensive and public market valuations high, some private equity players say acquisitions of partnerships could have more upside than other deals, and they point to lucrative exits on older buyouts in professional services as evidence for the investment thesis.

“We are in a new era of realising that these partnerships have attractive alternatives,” said Peter Munzig, a partner at TPG, one of the most active dealmakers in professional services.

TPG has invested in partnerships such as talent agency Creative Artists Agency and registered investment adviser LPL Financial in recent years, and last year it made an unsuccessful pitch to buy into in EY’s global consulting business. Now it says it is targeting other large deals.

Hellman & Friedman, THL and Madison Dearborn are among other private equity groups with a similar thesis, according to people familiar with their thinking.

One sector in particular has become a hot new hunting ground: accountancy firms. A burst of dealmaking in 2022, when three of the top-25 US accounting firms took private equity cash, has reignited this year. Last week, Chicago-based Grant Thornton agreed to sell a majority stake to New Mountain Capital in the sector’s largest deal. Baker Tilly secured a $1bn investment led by H&F in February.

Private equity has been attracted to accounting firms by the combination of steady income from tax and audit work and the opportunity to expand into new services such as consulting. “People recognised that these are generally stable businesses and ripe for consolidation outside of the Big Four,” Munzig said.

Private equity dealmakers have cast a wide net across white-collar professional partnerships in recent years. PwC, KPMG and Grant Thornton are among the large accounting firms to have sold parts of their advisory businesses to private equity. A wave of insurance brokerages including Hub Group and Integrity Marketing Group have taken private equity cash. Buyout groups are betting they can grow these businesses through acquisitions and turn many into companies large enough to eventually be listed on public markets.

In the past year, TPG and Madison Dearborn have sold partnerships they acquired for multibillion-dollar windfalls, validating the investment thesis and inviting copycats. TPG sold a controlling stake in the talent agency CAA to Artémis, the holding company of the Pinault family, at a $7bn valuation.

In contrast to some M&A, there can be room for both sides to think they are getting a marvellous deal. Because partnerships typically distribute all their income to partners each year, they do not have a traditional earnings record, allowing acquirers to negotiate a relatively low valuation.

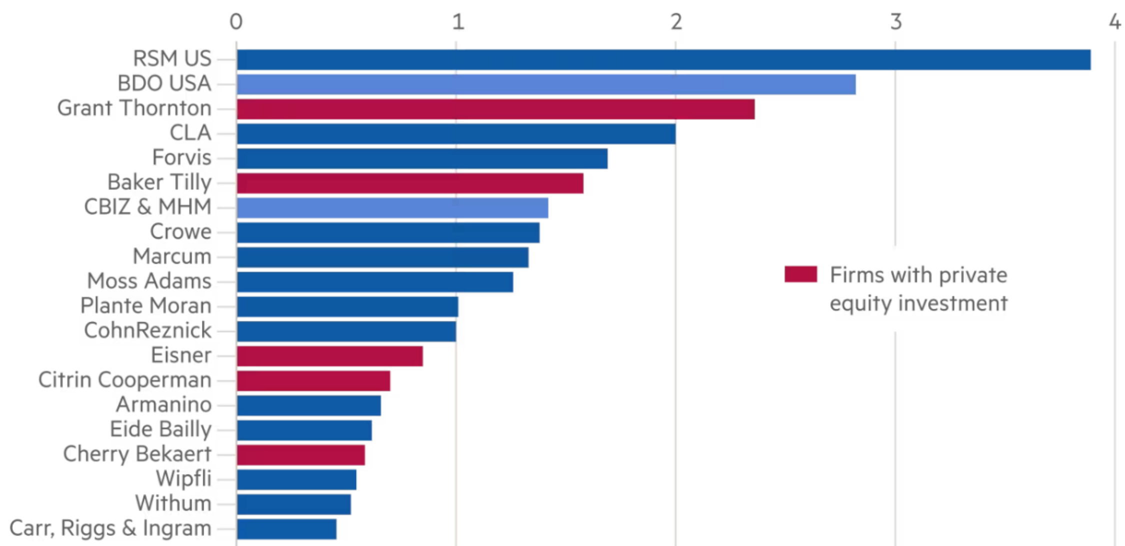
For partners, a minority equity stake that grows in value over time can be more attractive than a promise to be paid out of their partnership interest on retirement. “Younger talent doesn’t want to take one job and work for 40 years and get a measly buyout when they’re done,” said Allan Koltin, M&A consultant to accounting firms.

Koltin has advised on several deals that have shaken up the sector since 2021, and expects more.

“Firms desperately need capital to transform the business,” he said. “Tax and audit work is being replaced by technology and the lowest price is winning, hence the transformation to consulting and advisory services. To make acquisitions in those industries you have to pay real money.”

Private equity courts accountancies

Largest US accounting firms, excluding Big Four, by annual revenue ($bn)



Grant Thornton and Baker Tilly deals are expected to close in the second quarter. BDO converted from a partnership to an employee share ownership plan, funded by private debt. CBIZ is publicly traded
Source: Accounting Today
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Accounting firms that have taken private equity investments have indeed sped up their expansion.

A case in point: Moore Global, a global network of more than 200 mid-size accounting firms with annual revenue that rose 15 per cent last year to $4.5bn, said more than half its revenue growth in 2023 came from the three firms in its network that had taken private equity money. The trio — Moore Kingston Smith in the UK and Moore Belgium, both backed by Waterland, and New Mountain Capital-backed Citrin Cooperman in the US — posted revenue growth more than double that of Moore Global overall.

“Private equity backing is a clear growth accelerator and investment opens opportunities for acquisition, funding technology and other innovations,” said Anton Colella, Moore Global chief executive.

Blake Kleinman, partner at H&F, said after doing the Baker Tilly deal that his firm liked to be “the first capital” coming into a partnership to shake up the ownership model.

“The transaction itself can be a real catalyst,” he said. “It creates an equity culture so that partners are focused on how to grow the equity value of the business and not just their own individual book of business.”

Private equity buyers see an opportunity that has sometimes played out inside their own firms.

Over the past 16 years, big buyout groups such as Blackstone, KKR, Apollo and TPG have transformed from clubby partnerships into publicly traded corporations with large public market valuations.

David Trujillo, another partner at TPG, summed up the pitch to accountants and others they are trying to lure away from the partnership model.

"Instead of taking an extra dollar of compensation this year, why not be a shareholder and create an extra dollar of earnings that gets a market multiple?"