Animal Spirits at Franklin Resources?

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New York Stock Exchange listed **Franklin Resources** is an investment management business with a long track record of evidenced success. It is more widely known by its commercial brand name as Franklin Templeton. Founded in 1947, today it is a huge global entity with over 12,000 employees and offices in 34 countries, still led with distinction by descendants of the founding Johnson family.

In February 2020, Jenny Johnson was appointed as the new CEO after working in the business for over 30 years. Within a relatively short period of time, Jenny and her executive team have completed some of the most significant acquisitions in its 74-year history, including **Legg Mason** - a formerly listed holding company for a group of respected and individually branded boutique fund management firms.

This week they announced the acquisition of **Lexington Partners**, a privately owned business. The transaction mechanics are of interest; they are paying US$1bn in cash upfront, with an additional US$750mn in cash over the next 3 years. They then also give back 25% of the acquired equity to the employees of Lexington Partners over a 5-year period, and in addition they will pay them US$338mn in cash retention awards over this same 5-year period.

This means they are paying US$2.088bn for 75%, which is US$2.784bn for 100%.

How does this stack up in terms of valuation multiples? Assuming an ungeared Lexington Partners balance sheet, this deal is being done at multiples of 10.9 times 2022 expected future sales, and 24.7 times 2022 expected future EBITDA. These types of businesses usually have negligible fixed assets and accounting depreciation, so the price to after-tax earnings multiple could be as high as 31.3 times.

Putting these numbers into context - the 120-year price to earnings multiple on the S&P 500 is around 15 times. The S&P 500 represents the best of the large, listed businesses in the world, so it can be thought of as a quality business valuation proxy.

It looks like Franklin Resources is paying a steep price for this acquisition, that will now demand nothing less than a brilliant outcome in order to deliver long-term value for its shareholders.

Our work continues...

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