



Putting the Middle Market on Top

Past, Present & Future

Introduction

The Middle Market

Middle Market company definition

Based on deal size

Upper Middle Market

\$500M to \$1B

Core Middle Market

\$100M to \$500M

Lower Middle Market

\$25M to \$100M

Select US UMM PE deals

3Q 2017

Company	Investor(s)	Deal size
 CERTARA	EQT Partners	\$850M
 ODYSSEY	Odyssey Investment Partners	\$800M
 TRC THE RITEDOSE CORPORATION	AGIC Group, China Investment Corp.	\$700M
 Xactly Inspire Performance	Vista Equity Partners	\$564M
 CAREER BUILDER	Apollo Global Management, Ontario Teachers' Pension Plan	\$500M

Most active investors

By deal count

Audax Group	18
HarbourVest Partners	16
Genstar Capital	13
AlpInvest Partners	12
Hellman & Friedman	11

Where are we now?

Middle market M&A decline continues

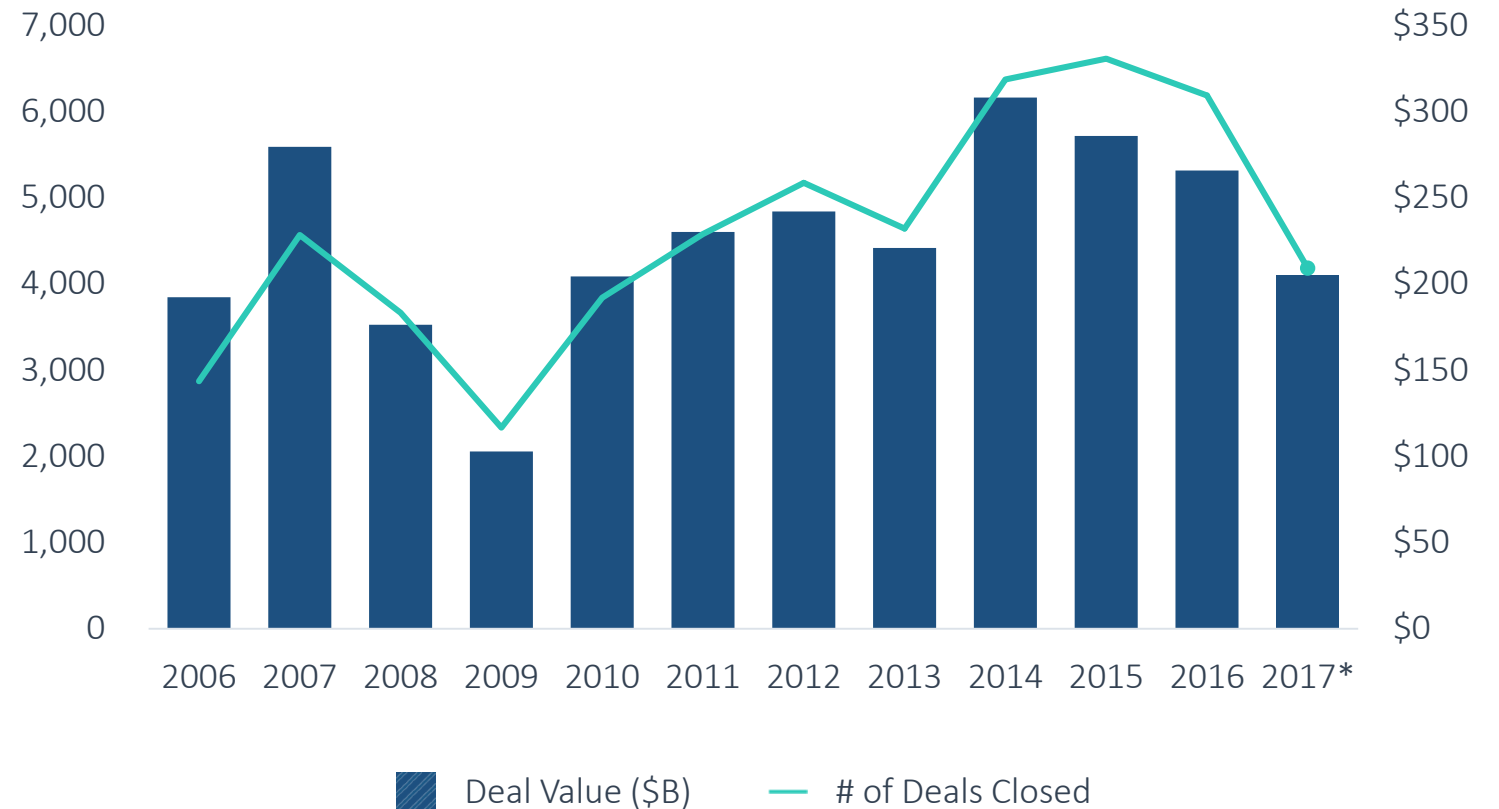
US MM M&A deal activity by year



Deal activity on track to fall for the **third straight year**

2014

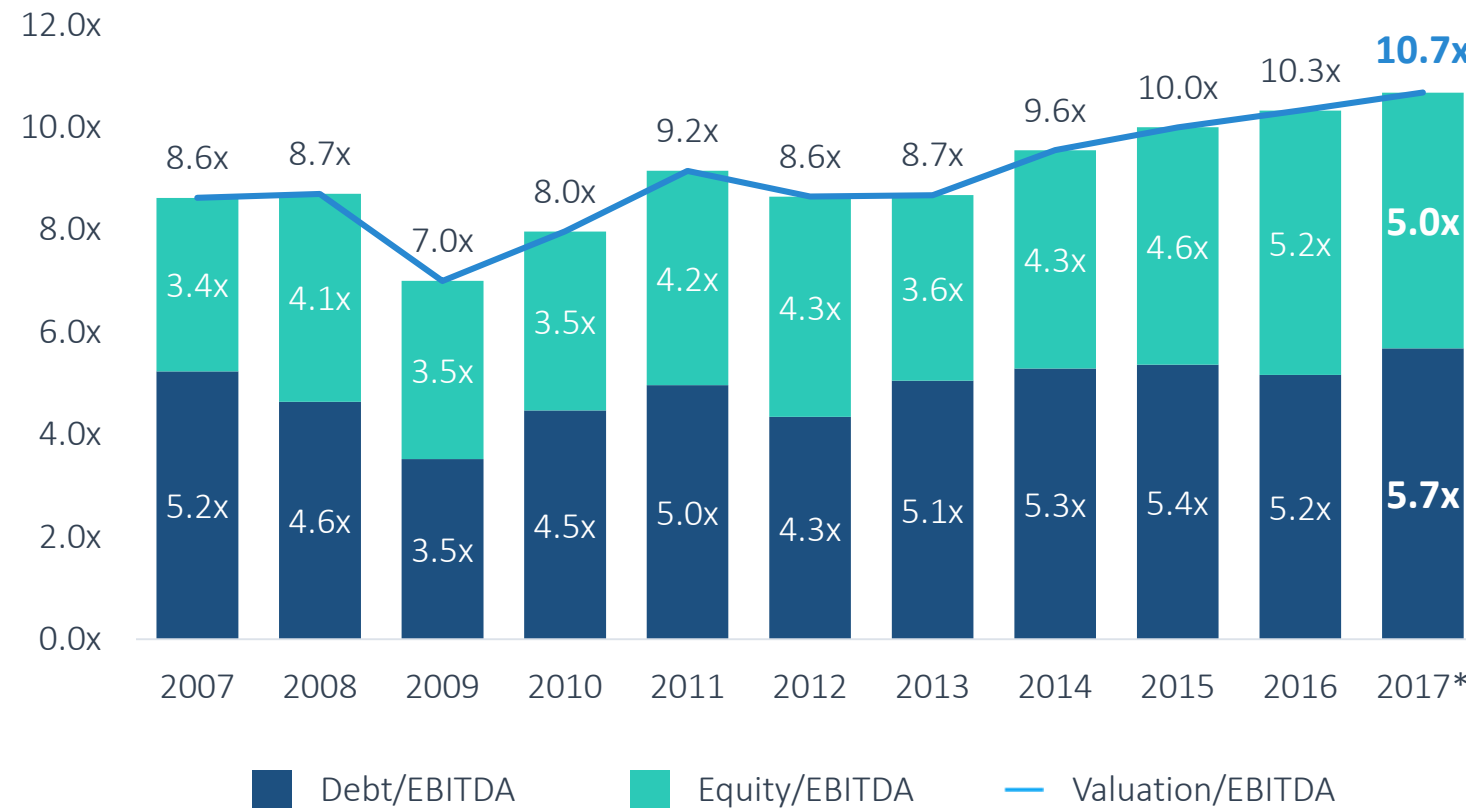
The most active year on record in the middle market



*Through 9/30/2017

Debt usage rises as valuations get frothy

US MM M&A multiples by year



*Through 9/30/2017

2017 US MM M&A
Multiples

10.7x

Valuation/EBITDA

5.0x

Equity/EBITDA

5.7x

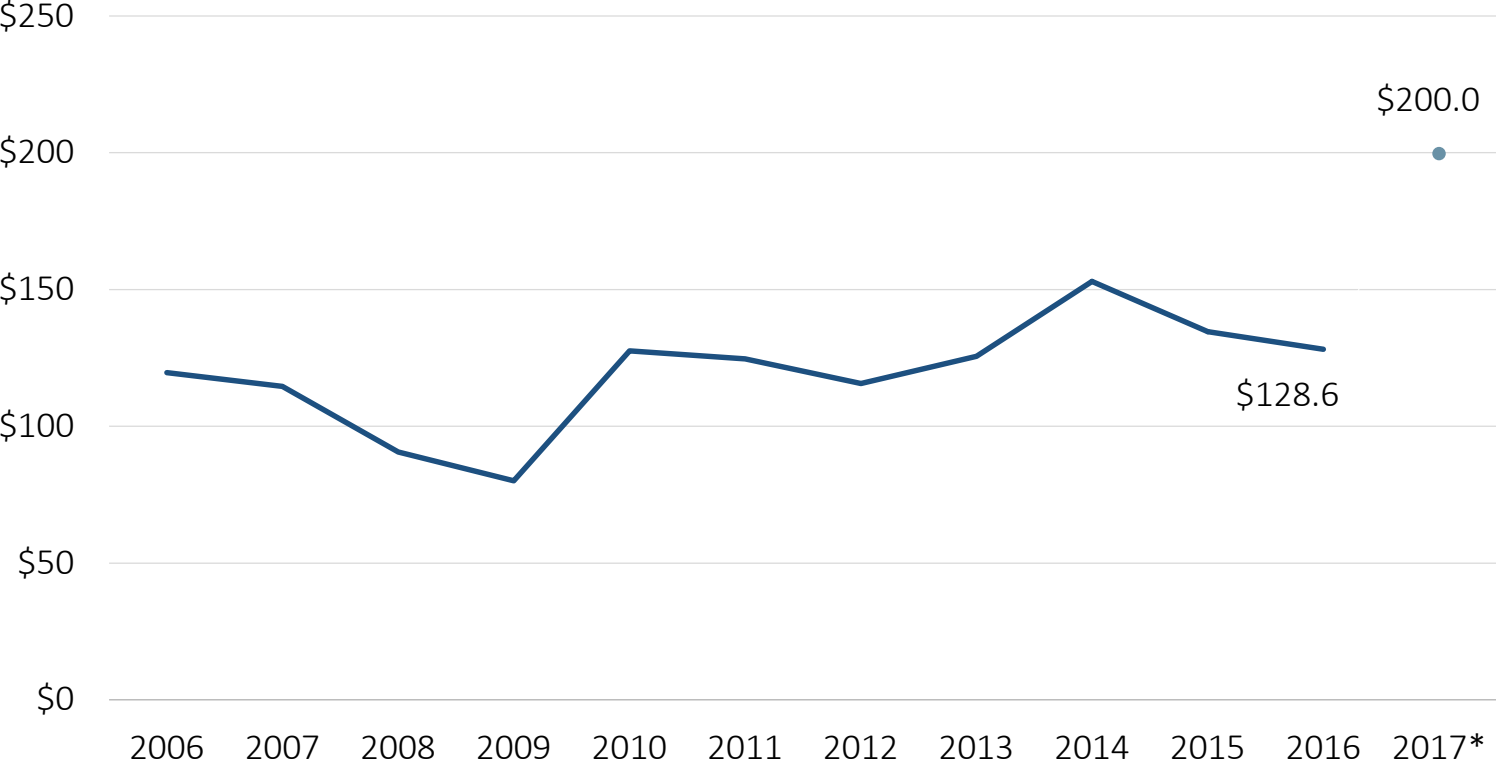
Debt/EBITDA

In your opinion, what is the most important factor driving mid-market M&A valuations today?

- A. Leverage levels
- B. Dry powder
- C. Public equity valuations
- D. Potential tax policy changes
- E. Other

Middle market PE deal size ballooned this year

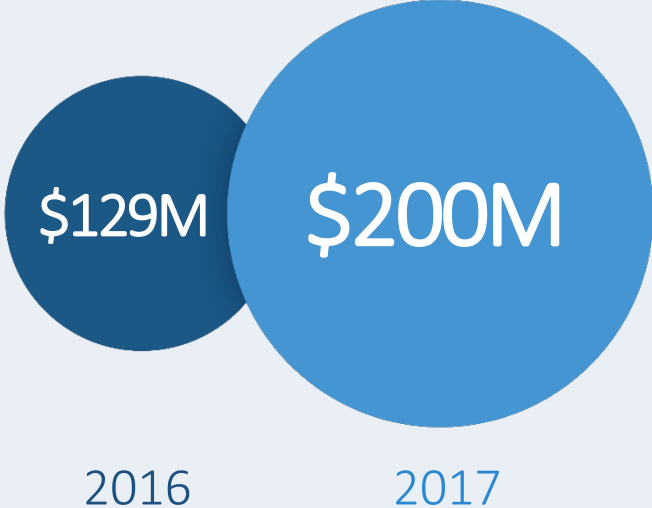
Median US MM PE deal size (\$M) by year



*Through 9/30/2017

+56%

2016-2017 increase in median US MM PE deal size



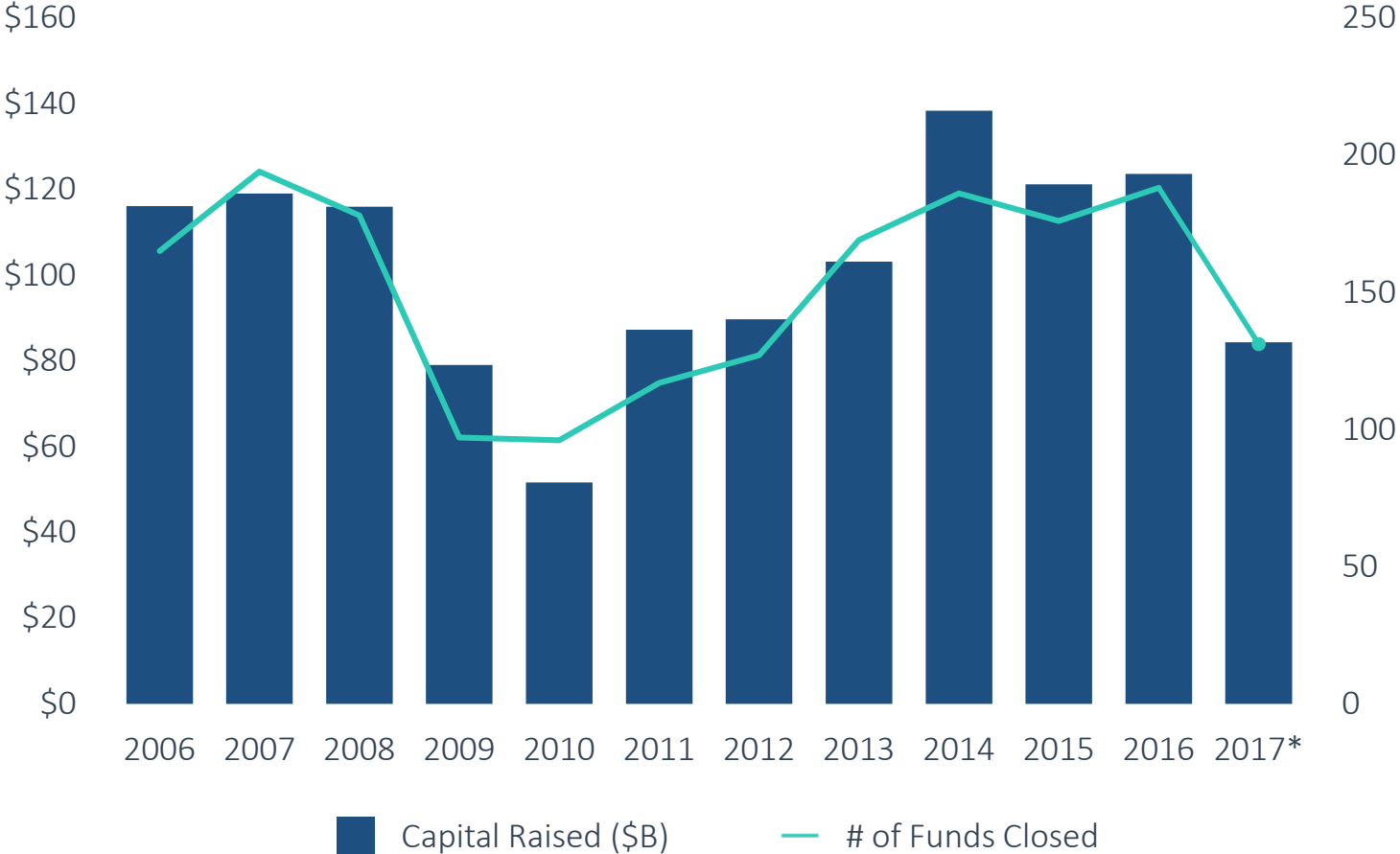
How did we get here?

Mid-market PE fundraising continually strong

US MM PE fundraising activity by year

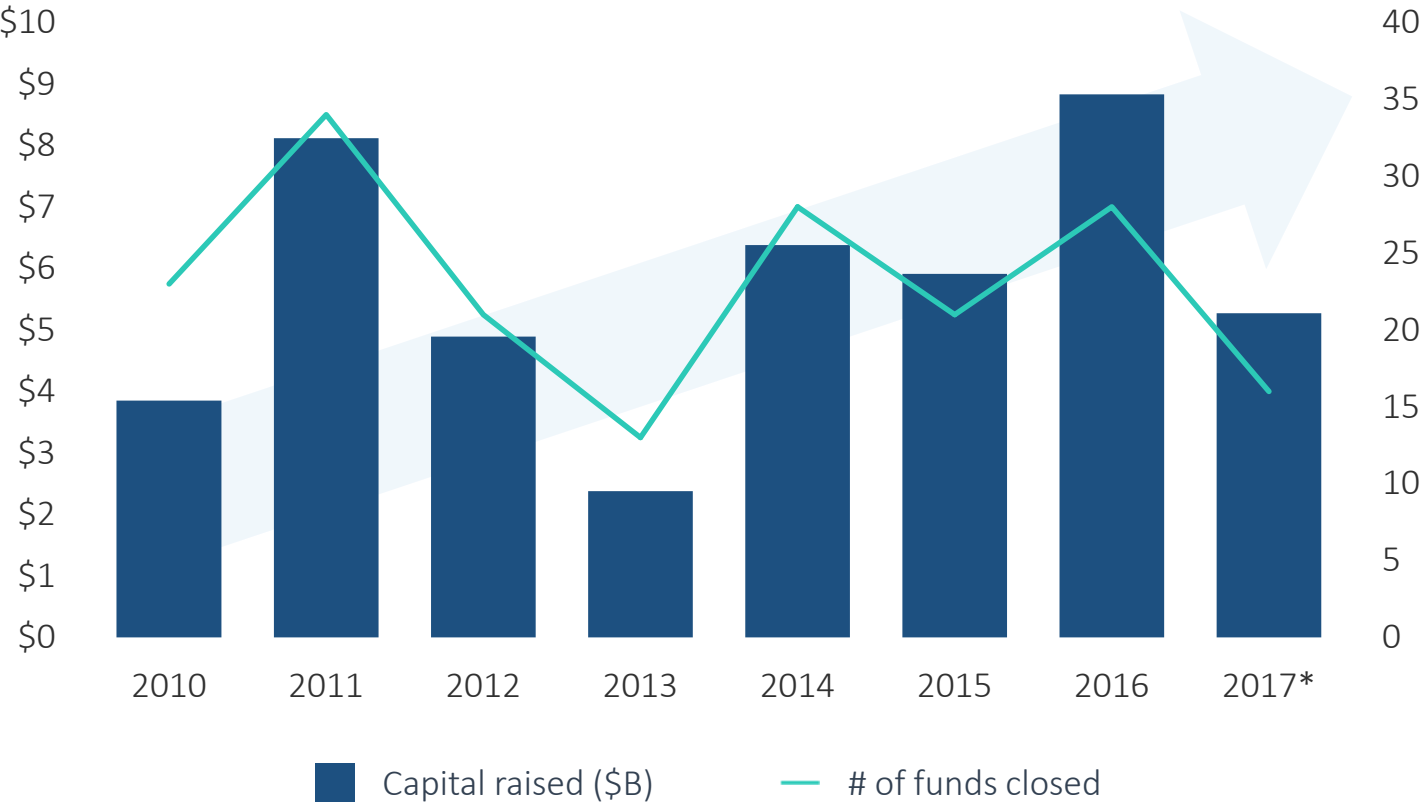
Select MM funds raised in 2017

- Crescent Mezzanine Partners VII**
Mezzanine – \$4.6B
- Genstar Capital Partners VIII**
Buyout – \$4.0B
- Veritas Capital Fund VI**
Buyout – \$3.55B
- Oak Hill Capital Partners IV**
Buyout – \$2.65B



First-time fundraising begins to rebound

All US PE first-time fundraising activity by year



*Through 9/30/2017

First-time managers

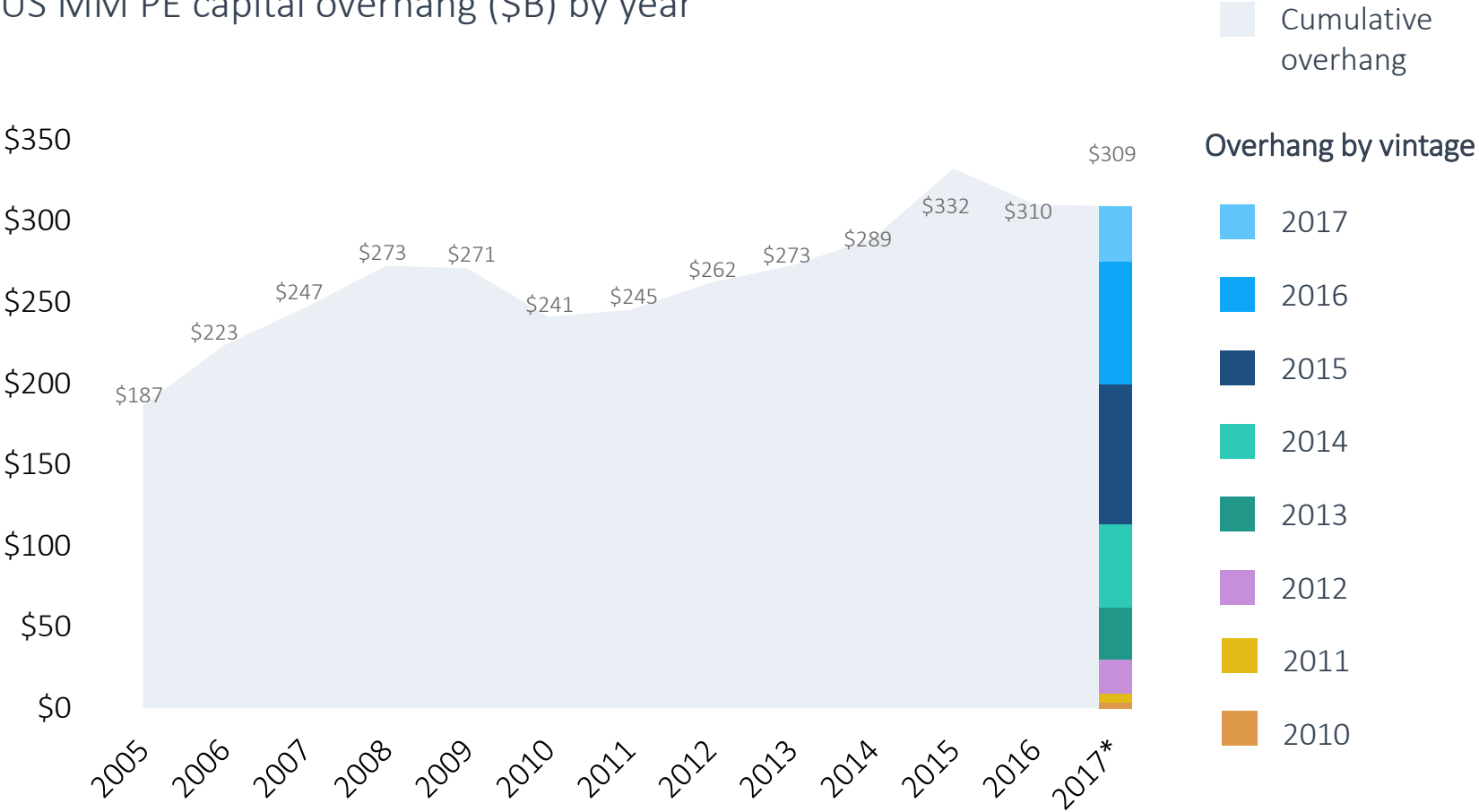
encouraged by success in the broader fundraising market

First-time funds

have outperformed follow-on competitors in recent vintages

Middle market PE dry powder remains robust

US MM PE capital overhang (\$B) by year



*Through 9/30/2017

\$309B

Dry powder ready to be deployed

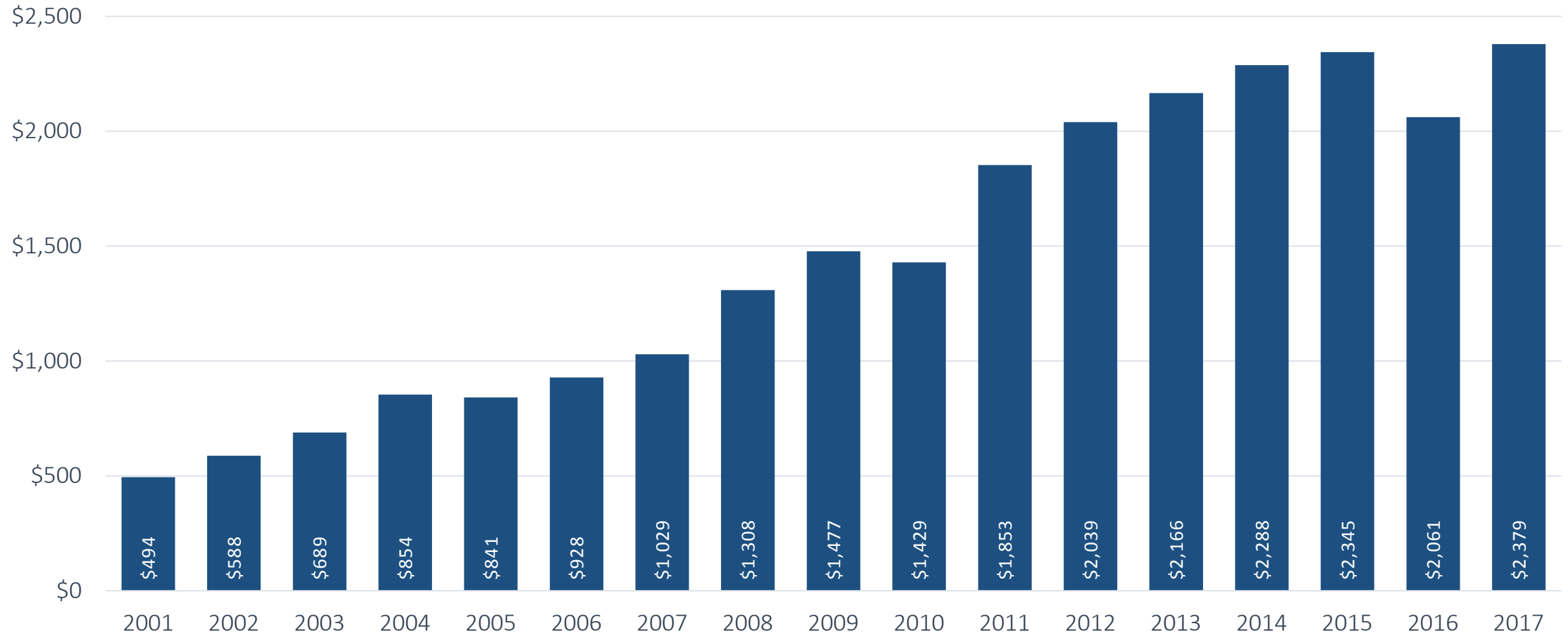
4.1 yrs

If invested at 2016 rate

Corporate cash growth has slowed

Cash on hand (\$B)

(NASDAQ, NYSE, NYSE American)



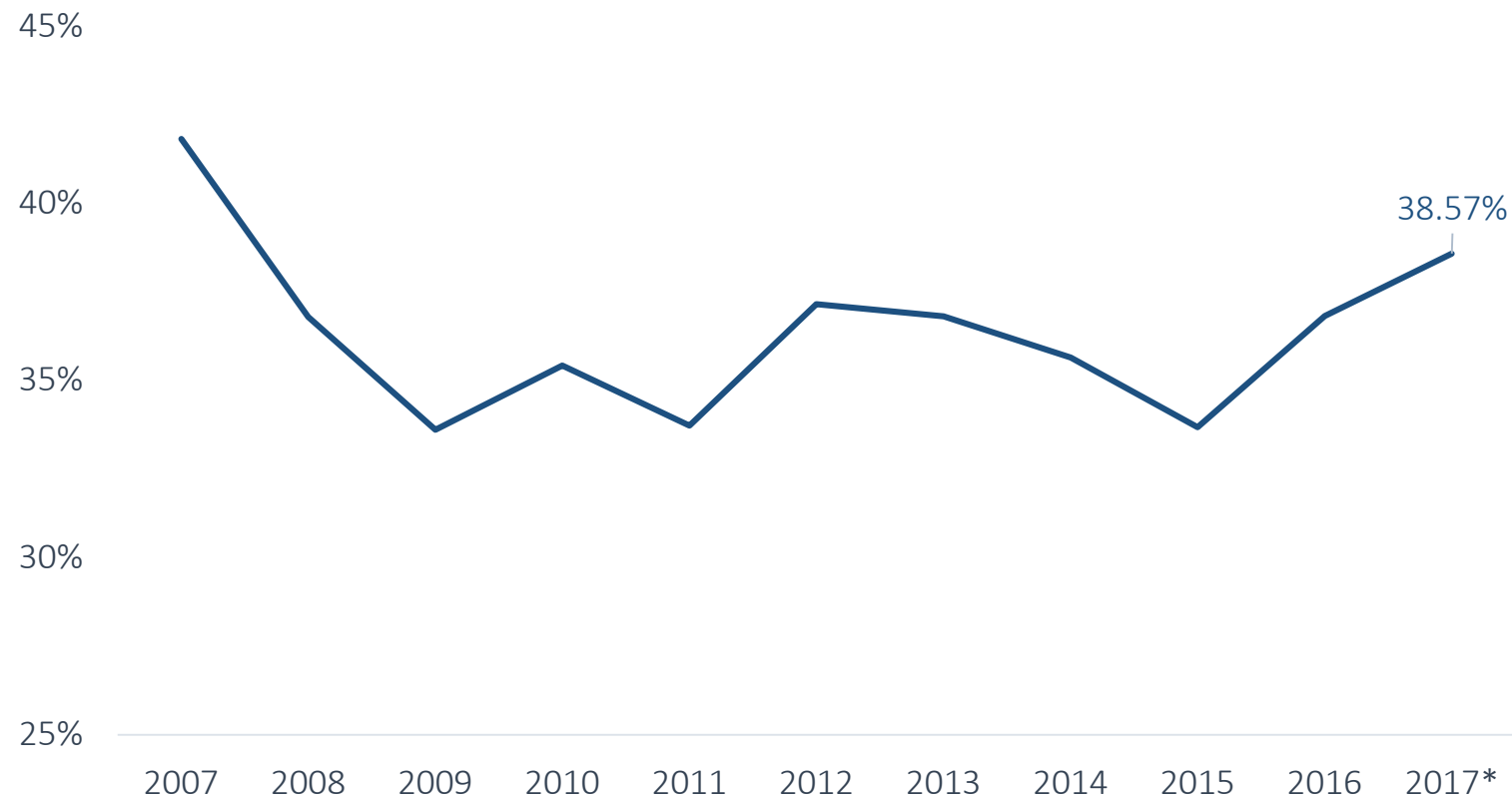
*Source: PitchBook Data –through Q3 each year

From whom do you currently see the most competition for mid-market deals?

- A. Corporate acquirers
- B. Private equity firms
- C. Fund-less sponsors (e.g. family offices, SWFs, etc.)

PE as a % of MM M&A highest since 2007

US MM PE deals as a % of M&A activity by year



*Through 9/30/2017



Structure of PE fund timelines means they will **continue deploying capital** even in times of higher prices

Add-ons dominate middle market activity

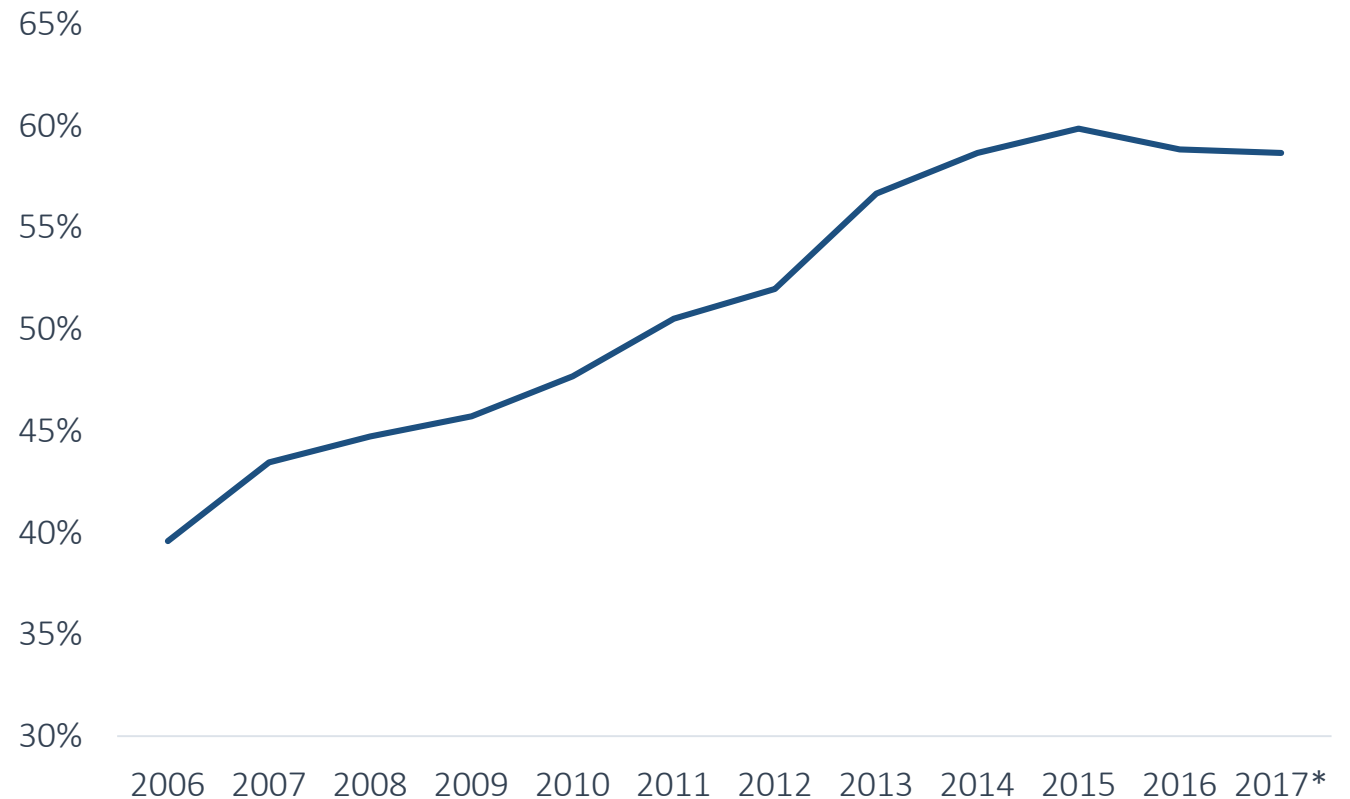
Add-ons as a % of US MM PE buyouts by year

Since
2006

add-ons have transacted at a **median valuation/EBITDA of 8.4x**, compared to 9.0x for non add-ons



Read more in our
3Q 2017 PE Analyst Note
Exploring Buyout Multiples



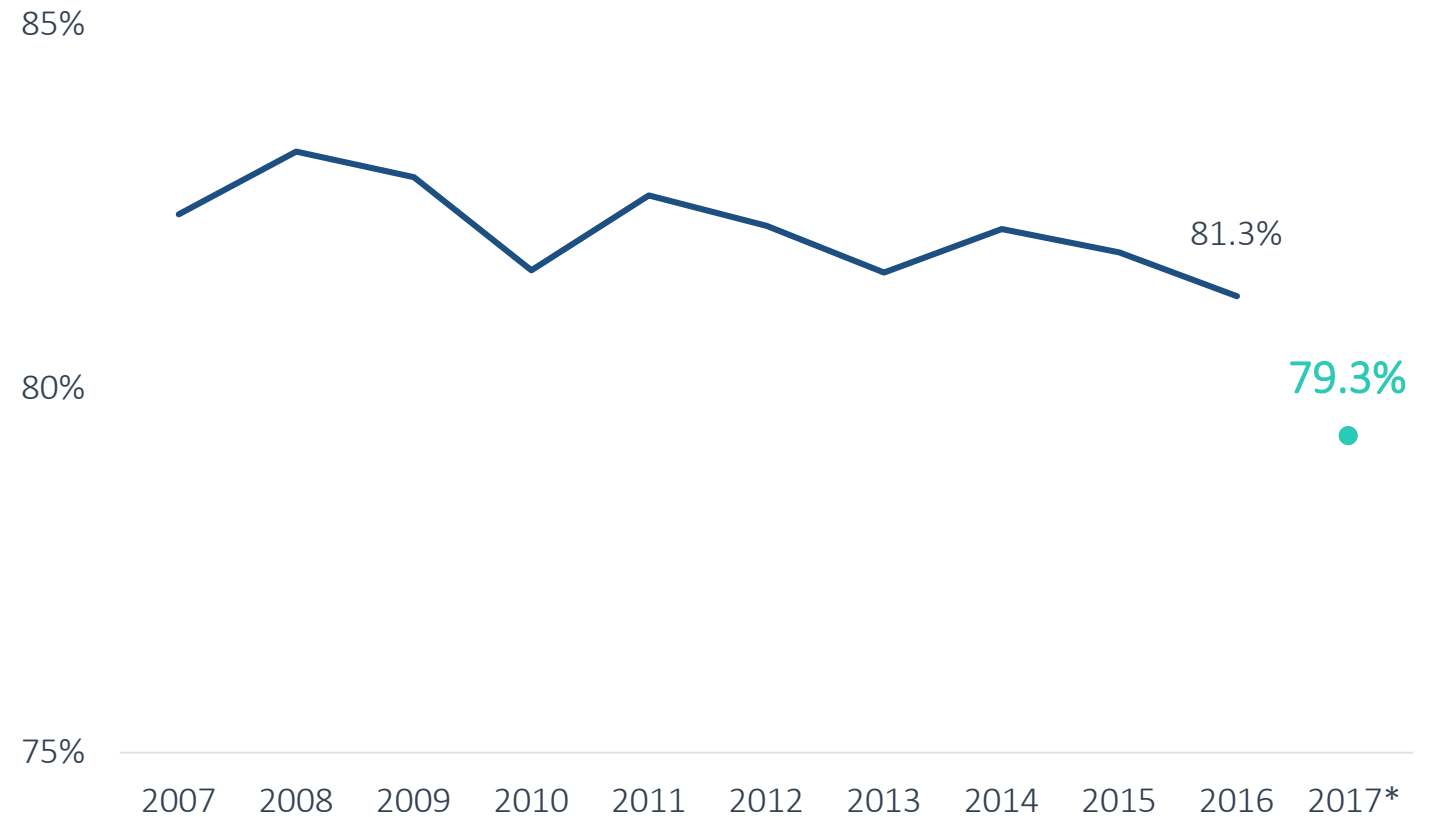
*Through 9/30/2017

Targets are increasingly institutionally-backed

% of MM targets without backing

Prevalence of secondary buyouts contributes to **higher proportion of institutionally-backed targets**

Growing PE-backed company inventory means that a **larger percentage of available targets already have institutional backing**



*Through 9/30/2017

What lies ahead

What will be the most important driver of deal flow in 2018?

- A. Pricing
- B. Sourcing/Quality of Targets
- C. Tax reform/Regulation
- D. Access to financing/Interest Rates
- E. Macro environment

Additional PitchBook reports

PitchBook

Exploring Buyout Multiples: Part II

Analysis of opportunities via add-ons and sector sourcing

PitchBook is now a Morningstar company. Comprehensive, accurate and hard-to-find data for professionals doing business in the private markets.

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Key takeaways

- Add-ons are an effective way to find buyout acquisitions at lower multiples. Often smaller and less institutionalized than platform buyouts, add-ons have transacted at a median valuation/EBITDA multiple of 8.4x globally since 2006, compared to 9.0x for platform buyouts.
- The financial services and healthcare sectors are currently the most expensive for buyout investors, given public comps trading at 51% and 23% premiums to their 10-year averages, respectively. Both have experienced a wave of consolidation after the global financial crisis, causing multiples to increase substantially.
- Public comparables in the B2C and materials & resources sectors are currently the most affordable, trading at just 13% and 14% premiums to their 10-year averages, respectively. Their relative affordability can be partly attributed to e-commerce disruptions and a prolonged downturn in commodity prices.

Introduction

In the first installment of Exploring Buyout Multiples, we discussed the relationship between multiple expansion and private equity returns. To help PE investors find opportunities for attractive entry pricing, which is paramount to achieving multiple expansion (and thus higher returns), we identified and examined three main sources of lower buyout multiples: smaller enterprise values, early stages of an economic expansion and emerging markets. In this edition, we examine two more:

1. Add-on strategies
2. Sector selection

1. Reflects premium above 10-year average. 2. Mkt Val/EbitDA

3Q 2017 PE Analyst Note Exploring Buyout Multiple

PitchBook

US PE Middle Market Report

In partnership with **ACG** Sponsored by **MADISON CAPITAL FUNDING**

2017 3Q

3Q 2017 US PE Middle Market Report

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M&A Report

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3Q 2017 M&A Report



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