



2019 M&A Market Update & 2020 Outlook

About Us

Calabasas Capital is a boutique investment banking firm focused on serving lower middle-market privately held companies and their business owners. We specialize in representing and advising businesses on sell-side and buy-side mergers, sales and acquisitions and we raise private equity and debt capital.

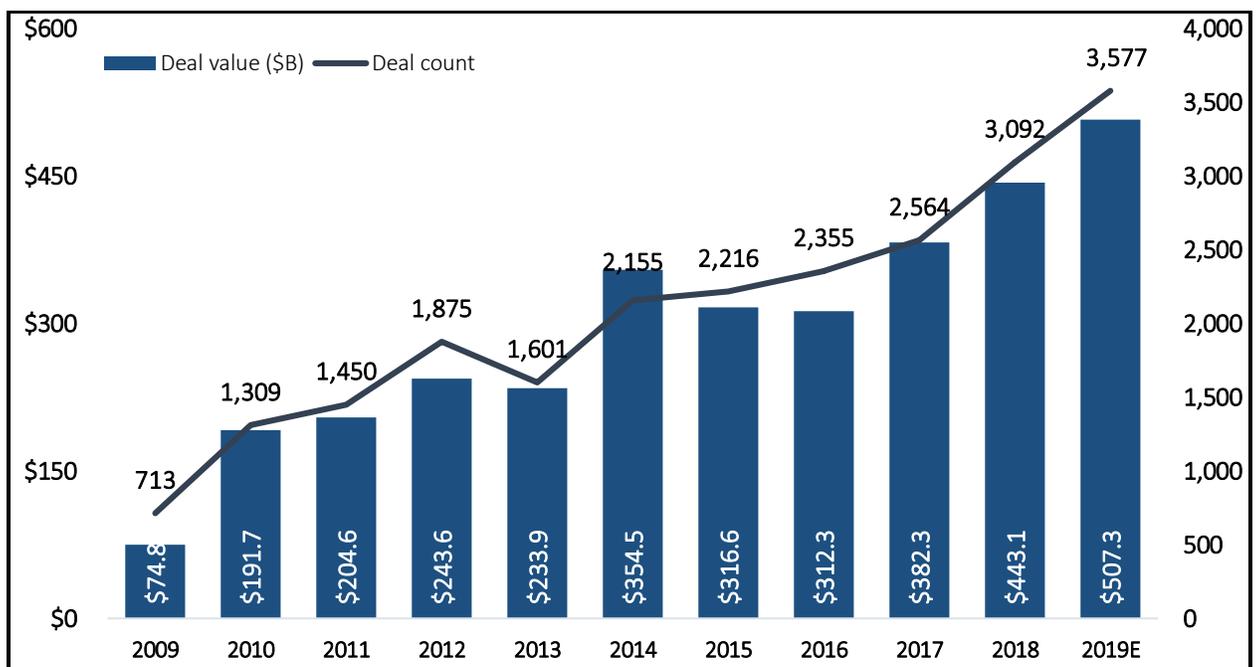
Private Equity M&A Activity Hits Record in 2019

According to PitchBook Data, U.S. private equity middle-market transaction activity (deal values of \$25 million to \$1 billion) crossed the \$500 billion threshold for the first time in 2019 increasing by 15% from \$443Bn in 2018 to \$507Bn. Total deal volume increased by 16% from 3,092 deals in 2018 to 3,577 in 2019. This activity was supported by:

- A significant amount of equity capital available to invest,
- An abundance of debt capital available to finance acquisitions,
- Low interest rates, and
- A robust market for add-on acquisitions to execute roll-up strategies.

Median and average deal sizes also ticked up in the year, reaching \$215.0 million and \$309.7 million, respectively.

U.S. Private Equity Middle Market M&A Activity (\$Bns)*



*Source: PitchBook Data 2019 U.S. Private Equity Middle Market Report.

2020 Outlook

While many deals have been postponed recently due to the impact of the corona virus pandemic, a fair number of deals have and will continue to proceed to a successful closing in the near term. Even assuming a rebound in the second half of the year, however, M&A activity will be down in 2020 over last year. How much is hard to say but the actions by the Fed and Congress should help the economy recover from the malaise sooner than later and reinvigorate business confidence enough to facilitate a return to strong deal activity later this year and into next year. In terms of private capital, there remain hundreds of billions of dollars in dry powder. Many private equity and debt capital providers are looking for new deals in the current environment.

Valuations & Leverage

At least for the time being, valuation multiples of larger private companies will likely come down in lockstep with the drop in public market valuations. According to PitchBook Data, the median leverage multiple (DEBT/EBITDA) of PE buyouts in 2019 was 5.5x while the average valuation multiple (Enterprise Value/EBITDA) overall was 12.5x. These statistics are skewed by larger deals as the universe includes deals up to \$1Bn. In the lower middle market (\$10MM to \$250MM) where we play, according to GF Data, the average leverage multiple for PE deals in 2019 was 4.0x and the average valuation multiple was 7.3x.

While valuation multiples across the board are likely to come down for the near term, we would expect a much larger impact on the larger deals than on smaller deals. Deals valued at 12x a few months ago may be valued at 9-10x today (a 20-30% decrease). Smaller deals valued at 7x a few months ago, may be valued at 6x today (a 10-15% decrease). Financial buyers, many of whom are still active today, will have to do their part also by putting in more equity to get deals done. Strategic buyers, however, who do not rely as much on leverage and who tend to dominate at the lower end, will not be impacted as much in terms of buying power.

Not all industries will be impacted to the same extent, however. Strong sectors like software, high growth direct-to-consumer branded consumer products, non-commercial aerospace & defense, government services, industrial technology and healthcare, for example, will see less of an impact, if any at all.

More Minority/Growth Equity Deals

We also anticipate an increase in growth equity and other minority equity investments for the near term as some of the companies who were previously looking to sell outright consider selling a small piece of their businesses instead.

The credit funds and other nonbank cash flow lenders are still lending as well albeit not quite as aggressively as before.

Intrinsic Value

Here's a message that may provide some solace to middle market business owners. Just because your revenue and profits decline by say 30% in 2020 over 2019, despite what opportunistic buyers may argue, this does not mean the value of your business has necessarily declined by as much as 30%.

The key will be to demonstrate that the economic fallout from the pandemic has minimal long-term impact on the business and its industry. Your astute investment bankers can then incorporate convincing and supportable addbacks in calculating adjusted EBITDA to mitigate the impact on valuation.

Calabasas Capital

Our comprehensive services include:

- Sell-Side and Buy-Side Mergers & Acquisitions Advisory
- Private Equity & Debt Capital Raising
- Acquisition Financing
- Financial Restructuring

Our industries of expertise include:

- Consumer Products & Services
- Business Services
- Aerospace & Defense
- Software & Ecommerce
- Industrial Manufacturing & Distribution

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