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Middle Market **Pulse**

EXECUTIVE BRIEFING *Mergers, Acquisitions and Capital Resources Since 1956* June 2021

A new Q1 2021 M&A report has just been published by GF Data, a database of private mergers and acquisitions transactions, suggesting that the after-effects of the global pandemic have resulted in difficult to read current conditions. There has been a resurgence of deal activity, but at overall valuations slightly below the range that has characterized the markets since 2017. Quality premiums are still sky high; and, depending on the size of the transaction, equity contributions are nearing 56%, a five year high.

Quality Premium - Buyouts Only

By Year

	2003 –2016	2017	2018	2019	2020	YTD 2021	Total
Above Average Financials	6.4	7.8	7.8	7.6	7.8	7.6	6.8
Other Buyouts	5.9	6.4	6.3	6.3	6.1	5.7	6.0
Premium (/Discount)	109%	121%	124%	121%	128%	134%	114%
Incidence	56%	57%	59%	52%	55%	57%	56%

GF Data Resources

Figure 1

Best in class companies continue to command top dollar in the market. However, as those companies are acquired at stiff premiums (Q1 2021 saw an average 34% quality premium), portfolio managers looked to smaller deals or add-ons to a platform company to create value. In the first quarter of 2021, companies between $10 million and $25 million sold for an average of 1.9 X EBITDA less than companies in the $100 million to $250 million range. Add-on investments comprised approximately 30% of all deal activity in Q1 2021. This trend will likely continue.

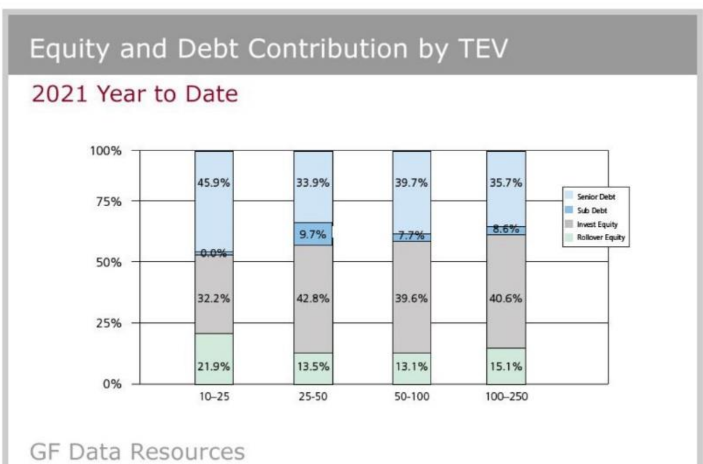

Figure 2

Use of leverage is an important component in the structure of an M&A transaction. Corporate cash flow must be sufficient to service the debt placed on the transaction. Too much debt can cause undue financial pressure on a business; yet too little debt may constrain growth potential. Leading up to 2020, average equity contributions on all size transactions neared 50%; but the size of a transaction also impacts debt placement. The average equity share on $100 million to $250 million size transactions rose to nearly 56%.

Seller financing or earn-outs are a way to bridge the valuation gap between buyer and seller. Earn outs appeared in nearly 39% of all transactions during 2018-2019. In 2020, that figure rose to 42% and, in the first quarter of 2021, it jumped again to 43%. This trend may continue as well.

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