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TRANSACTION ADVISORY SERVICES

Review of 2015 and Observations on Middle Market M&A

There has been a lot of press in the past year about the high level of activity in the M&A world, much of which pertains to very large deals. We thought it would be helpful to give you our view from the Middle Market trenches. GBQ's Transaction Advisory Services (TAS) group works predominately in the Middle Market which we would define for our purpose as companies in the $5.0 million to $2.0 billion revenue range.

GBQ's 2015 TAS Activity

2015 turned out to be the most active year to date for our TAS practice. We worked on nearly 100 transactions in various capacities, including:

- 15 assurance and tax due diligence projects (including quality of earnings reports in some cases);
- 14 ESOP formation projects;
- 18 shareholder valuations involving transactions;
- 35 purchase price allocation projects; and
- 10 buy and sell-side advisory projects in collaboration with our alliance with Footprint Capital, LLC, managed by Josh Curtis. This included seven successful sell-side closings in 2015 and three retained buy-side projects. We also entered 2016 with a healthy list of five active projects in conjunction with Footprint and a number more in the pipeline.
- Another exciting development in 2015 was entering into a strategic relationship with Corporate Value Metrics for use of their Value Opportunity Profile (VOP) program, which is a sophisticated tool to help companies analyze readiness and attractiveness in preparation for a future liquidity transaction. We did this in response to a growing number of companies retaining us to help prepare them for a liquidity transaction. We will be providing more information on VOP in future communications. Please click **here** to view a snapshot of the process we follow to help clients prepare for liquidity transactions.

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Tremendous M&A Activity

A recent article by StreetInsider said that at least 60% of middle market companies are interested in M&A. It is a perfect storm on both the buy- and sell-side. Why?

- First, there is a huge supply of dollars looking for a place to invest…nearly $1.0 trillion by PE firms alone.
- There are over 3,300 private equity firms in the U.S., not to mention the huge number of corporations looking to do acquisitions.
- The low interest rate environment helps fuel transactions.
- On the sell-side, potential sellers know this is a good market to attract strong values and many do not want to face another potential recession, although most believe a downturn is still a number of years away.
- Buyers are looking to augment organic growth, expand geographically, enhance intellectual capacity and do it quickly.
- Many business owners are baby boomers and are now actively seeking an exit strategy that best fits their situation.

High Valuations but Very Deal Specific

Yes, valuations are high right now, but that can also be misleading. In a recent article by GF Data, they reported an average multiple of 7.1 in the third quarter of 2015 on 37 deals in the $10 million to $250 million enterprise value range. People throw around big multiples that they read about, but those usually pertain to larger companies with at least $5.0 million in EBITDA that are well positioned or have extremely attractive characteristics like certain SAAS companies. In reality, most business owners overestimate their value. It is important to know what your company is worth and know what you can do to make it more valuable. The answers often surprise business owners.

More Smaller Company Deals

We are seeing more successful deals with smaller companies which for this purpose would be companies in the $1.0 million to $5.0 million EBITDA range. We are seeing more PE firms interested in this market because they face less competition than for larger deals and the multiples are typically lower. We are even seeing activity in the sub $1.0 million EBITDA range, but these are usually bolt-on acquisitions instead of platform acquisitions. Furthermore, we have found that smaller companies are woefully unprepared to go through a transaction and the owners have no idea how much they are giving up by not being ready.

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Multiple Exit Strategies Being Used

Most business owners also do not realize that there are a number of strategies to seek liquidity that have very different advantages, characteristics and implications. While there are certain groups that promote specific strategies like ESOPs or sell-side mandates, we start with a blank sheet of paper and walk clients though all of their options to decide which strategy is in their best interest. Click **here** to see a list of your Exit Options.

More Middle Market Companies Doing Acquisitions

While only large companies (over $1.0 billion in revenues) historically have had corporate development groups, smaller companies are now interested in a formal process to perform and execute acquisitions. Why? First, it is difficult in this economic environment to get organic growth so many more companies are looking to acquisitions. The reality though, is that most middle market companies do not really know how to go about it or have the internal resources to execute it. Most companies are reactive in this regard when they really need to be proactive. The two critical mistakes we see in this area are 1) making an acquisition that does not align with the business' overall strategy, and 2) incorrectly structuring the transaction; which can include too high of a purchase price. To give you a snapshot of what we do in this area to give companies a competitive edge, click **here** to view a summary of our Corporate Acquisition Services.

More Types of Mezzanine or Subordinated Debt Type Lenders

Another noteworthy phenomenon in recent years has been the proliferation of sub-senior or mezzanine debt type lenders. These include BDCs, SBCs, life insurance companies, private equity, credit opportunity funds and family offices to name a few. To some extent, this has happened due to the tightening on banks by the Federal government. This tightening opened a whole new market for these types of lenders who are not subject to the same regulation as banks. These various lenders are also trying to seek higher yields that are difficult to find in today's environment. We have seen these alternative type lenders on even very small deals.

Finally, we would like to express our appreciation and gratitude to all of you that have allowed us to be involved in your transactions and we look forward to working with more of you in 2016. Our TAS group is a strong, integrated group of professionals that can offer a multitude of services on all aspects of transactions, including the execution of Buy and Sell-Side deals.

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