



CAPITAL MARKETS UPDATE

Middle Market M&A
Q3 2021



**CAPSTONE
PARTNERS**

MARKET COMMENTARY



“Total deal volume has increased nearly 10% and is rising, while average deal value is up over 30%, signaling that we are close to peak historical valuations.”

“Party on, Wayne! Party on, Garth!”

In our last market commentary, my colleague Todd McMahon talked about the massive increases in deal volume being driven in part by increases in the capital gains tax rate. On September 13, we learned that House Democrats were targeting a 5% increase, which was much less than the 20% that was feared. They also announced that rate would be active as of that date – squashing the hopes of business owners already in the market and hoping to get a deal done by year end. However, due to stagnation and internal policy disagreements, this increase never passed creating some hope that deals getting done by year end would not be subject to the increased tax. There were some worries that this bill may pass in 2022 and be retroactive to January 1, fueling the continued M&A frenzy through Q3 and likely peaking in Q4. When you combine potential increases in capital gains with backlog from the pandemic downturn, the \$1.4 trillion of private equity dry powder, and massive amounts of cash on strategic balance sheets, you get a frantic global M&A market that saw over \$1.5 trillion in deal activity in Q3 (a ~40% increase YOY) and a new quarterly record. Private equity investments represented over 50% of this activity, representing an increase of over 130% YOY – proving that the desire to deploy capital in an irrationally exuberant market should continue to build momentum throughout the rest of the year and into 2022. In addition, total deal

volume has increased nearly 10% and is rising, while average deal value is up over 30%, signaling that we are close to peak historical valuations.

Outside of the M&A market, the U.S. economy, has also been booming. Employment rose by more than five million since January, but the labor market is still short five million jobs from normalcy. This optimism has led to a record number of job-seekers saying this is the ideal time to find a new job, fueling the Great Resignation – which contrary to some experiences of business owners feeling the pinch of worker shortages – is a good thing for the economy. With the S&P 500 up more than 25% year-to-date and less spending on consumer discretionary services over the last year, families are sitting on record savings and inflated retirement accounts.

Over the summer, with the masses largely vaccinated, optimism was at an all time high and people finally took long needed vacations, digging into some of that savings – finally! Then the Delta variant came, ending the party for a short time, until it became clear that vaccinations were working and preventing deaths, providing renewed optimism in late September. Towards the end of Q3, concerns about inflation and supply chain issues seemed to be a big topic of discussion but the hope was those issues were the inevitable growing pains of an economy continuing to restart after a global pandemic and transient in nature.

Q4 is looking very strong and will likely set every M&A record for a quarter since these statistics started being measured. However, one of the interesting facts that will drive M&A volume over the next few quarters is the fact that M&A was too frothy in Q3 and Q4. Many bankers paused on bringing deals to market because businesses were not receiving the attention they should because everyone was too busy. Starting in September, many private equity firms and strategics alike stated that they were just too busy to look at additional opportunities. A common statement was that they just didn't have the capacity for

MARKET COMMENTARY (CONTINUED)

any more deals. This was also prevalent among other M&A service providers from accounting firms performing quality of earnings work, to market study providers, to representation and warranty insurance providers. The hope is this backlog will dwindle in Q1 and Q2 of 2022.

In conclusion, as we are closing the book on a great 2021 for middle market business owners, think about those communities that may not have had the same experience this year and throughout the pandemic (approximately 40% of people throughout the U.S.). At Capstone, we ascribe to this belief and our Capstone Cares initiative has donated hundreds of thousands of dollars to organizations such as The Trevor Project, Invest in Girls, Boys & Girls Clubs, Shoes that Fit, Heart & Hand, C5 Youth Foundation, Matrix Human Services, and Toys for Tots both in our local communities and nationally. Capstone fervently supports organizations focused on education and children to help in any way we can to help give these communities an opportunity to potentially become business owners themselves one day.

Jacob Voorhees

Jacob Voorhees
Head of M&A



MIDDLE MARKET OUTLOOK

Q3 2021 TAKEAWAYS & THEMES

The M&A market is approaching historic levels with three years worth of deals packed into 12 months

- Many sale processes that were delayed last year have been initiated in 2021 while sellers that were eyeing a liquidity event in 2022 have pulled their exit timeline forward ahead of prospective tax increases.
- Elevated valuations and abundant capital levels have driven a record supply of transactions, although dealmakers continue to combat staffing challenges as pipelines reach capacity.
- The pandemic has fatigued many business owners who have emerged from COVID-19 only to encounter supply chain woes and workforce challenges – encouraging many owners to capitalize on the current M&A environment.
- A flight to quality in the market has been largely driven by capacity constraints among buyers, as PE firms and strategics are narrowing their focus and bidding on assets that align with their expertise or present a strong fit.

We expect volume to remain robust in 2022, although the drivers of M&A are likely to be different

- Transaction supply is likely to normalize but remain at healthy levels as the availability and low cost of capital provides a favorable backdrop.
- 2021 deal flow has been focused on high-quality assets, 2022 presents opportunities for deals with imperfections to close.
- Middle market M&A is largely demographic driven and the wave of baby boomers reaching retirement age with significant wealth tied up in their business creates a healthy inventory of transactions in the near term.

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Capstone Barometers

- Fully Integrated Expertise
- Firm Data
- Private Equity Preferences
- Recent Deal Closings
- Leadership Team

Q3 2021 BY THE NUMBERS

8.7% ↑

INCREASE IN DEAL VOLUME FROM Q2

M&A volume increased 8.7% from Q2 to Q3 as heightened valuations and attractive capital levels have fueled activity

4.1x ↑

AVERAGE DEBT MULTIPLE

Average debt multiples have reached elevated levels, increasing substantially to 4.1x in Q3 from 3.6x in Q2.

11.1x ↑

AVERAGE EBITDA MULTIPLE

The average middle market EBITDA multiple climbed from the prior quarter and remains above historic averages

16.4% ↓

DECREASE IN PE TRANSACTIONS

Closed deals by PE fell 16.4% in Q3 from Q2, however, PE deal count in 2021 has already surpassed full year 2020 levels

\$71.7M ↑

AVERAGE DEAL VALUE

Average transaction value has increased nearly 29% year-over-year through Q3 to a record of \$71.7 million

10.8% ⇌

DEALS BY FOREIGN BUYERS

Foreign buyers have comprised 10.8% of deals through Q3, a strong year-over-year increase but slightly below Q2 levels

\$142B ↑

PE FUNDRAISING

Private equity fundraising through Q3 has rivaled the record setting pace seen in 2019 with \$142 billion raised year-to-date

1.2% ↑

PRIVATE COMPANY ACQUISITIONS

Closed acquisitions by private companies increased 1.2% in Q3 from Q2, demonstrating a robust M&A market

\$1.4T ↑

PE DRY POWDER

Capital overhang has remained at elevated levels, providing a favorable backdrop for healthy PE deal activity

CAPSTONE'S PROPRIETARY MIDDLE MARKET INDEX

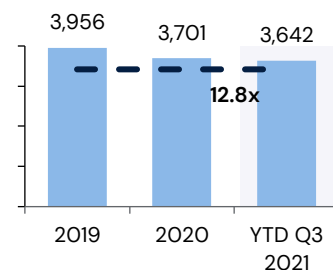
Valuation & Transaction Volume Takeaways

- Middle market M&A activity in the Technology, Media & Telecom sector has led all industries through YTD Q3.
- The Consumer sector is on pace for historic M&A volume, although the 3-year average EBITDA multiple of 10.5x has modestly trailed the middle market average of 10.6x.
- Deal volume in the Education & Training sector has already surpassed full year 2019 and 2020 totals as online learning applications have been in high demand.

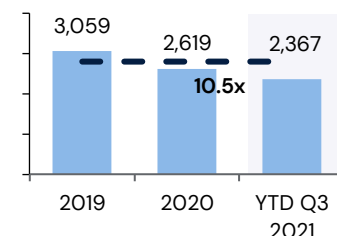
For more information on the fair value of your business, comparable transactions and public companies, [contact us](#).

--- 3-Year Average EBITDA Multiple
Transaction Volume

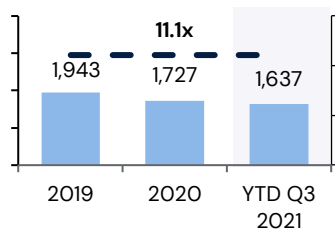
Technology, Media & Telecom



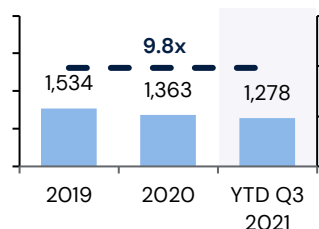
Consumer



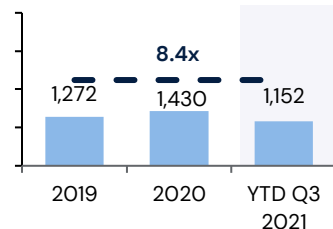
Healthcare



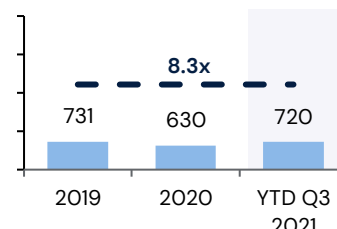
Industrials



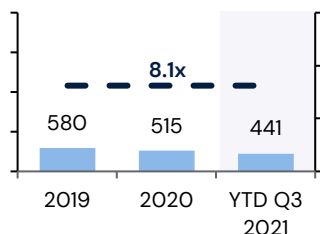
Energy, Power & Infrastructure



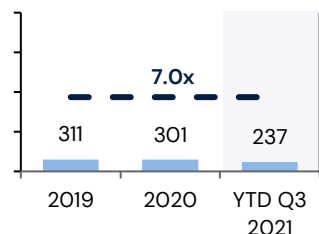
Building Products & Construction Services



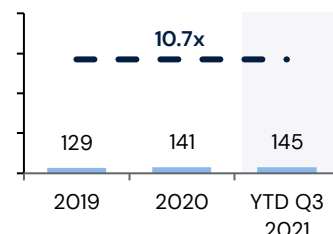
Business Services



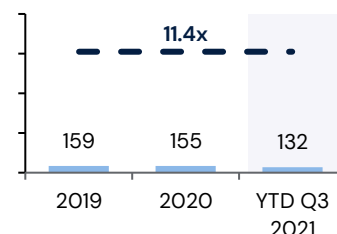
Transportation & Logistics



Education & Training



Aerospace, Defense, Government & Security



CAPITAL MARKET DASHBOARD

YTD EQUITIES

S&P 500
+26.67%



| Last | 1Y % | P/E LTM |
|---------|-------|---------|
| 4,697.9 | +33.0 | 24.4 |

Dow Jones Industrial
+18.25%



| Last | 1Y % | P/E LTM |
|----------|-------|---------|
| 35,601.9 | +23.0 | 19.5 |

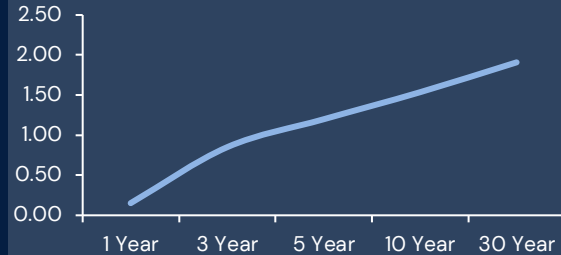
NASDAQ
+25.32%



| Last | 1Y % | P/E LTM |
|----------|-------|---------|
| 15,967.7 | +35.7 | 38.0 |

FIXED INCOME

U.S. Yield Curve



| 1Y | 3Y | 5Y | 10Y | 30Y |
|-------|-------|-------|-------|-------|
| 0.153 | 0.850 | 1.199 | 1.536 | 1.908 |

POLICY RATE

Federal Funds Target Rate



ECONOMIC INDICATORS

GDP, LABOR MARKET, & INFLATION

| | Last | YOY | |
|----------------------|-------|--------|--|
| GDP | 2.0% | -31.8% | |
| Consumer Confidence | 113.8 | +12.2% | |
| Unemployment | 4.6% | -2.3% | |
| Consumer Price Index | 276.7 | +6.2% | |

HOUSING MARKET

| | | | |
|--------------------|-----------|-------|--|
| Housing Starts | \$1,520.0 | +0.4% | |
| Total Construction | \$1,573.6 | +7.8% | |

PMI & NMI

| | | | |
|---------------------|-------|--------|--|
| Purchasing Managers | 60.8% | +2.0% | |
| Non-Manufacturing | 66.7% | +10.5% | |

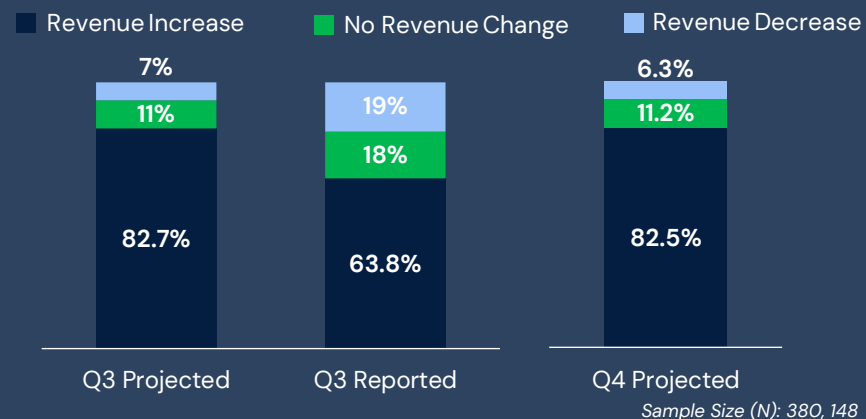
RETAIL

| | | | |
|--------------|---------|--------|--|
| Retail Sales | \$638.2 | +16.3% | |
|--------------|---------|--------|--|

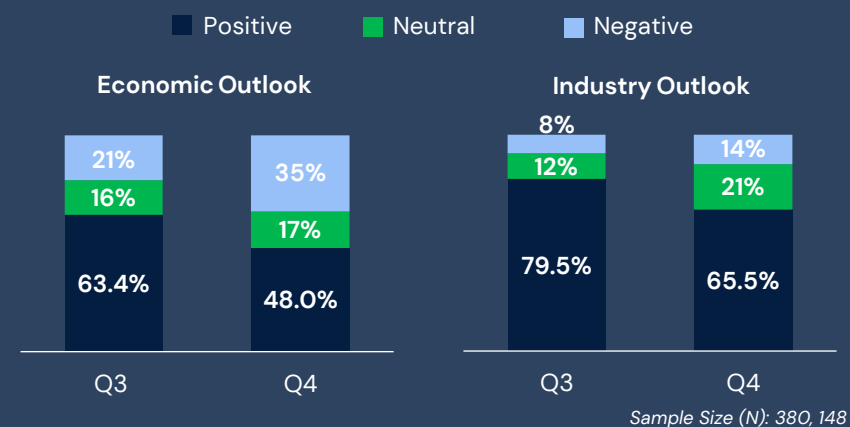
Source: FactSet as of 11/22/2021

CAPSTONE'S MIDDLE MARKET BUSINESS OWNER SURVEY

64% OF OWNERS EXPERIENCE Q3 REVENUE INCREASES

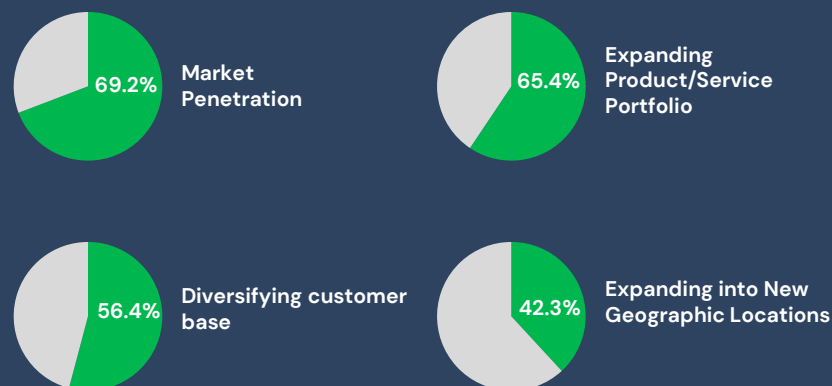


ECONOMIC & INDUSTRY CONFIDENCE DECLINE



22% OF OWNERS PLAN TO SECURE CAPITAL IN Q4

Organic Initiatives



Inorganic Initiatives



Source: [Capstone Partners' Middle Market Business Owner Survey](#),
Sample Size (N): 78

LEVERAGED FINANCE CONDITIONS



Kent Brown

Managing Director, Head of Debt Advisory Group
303-951-7127
kbrown@capstonepartners.com

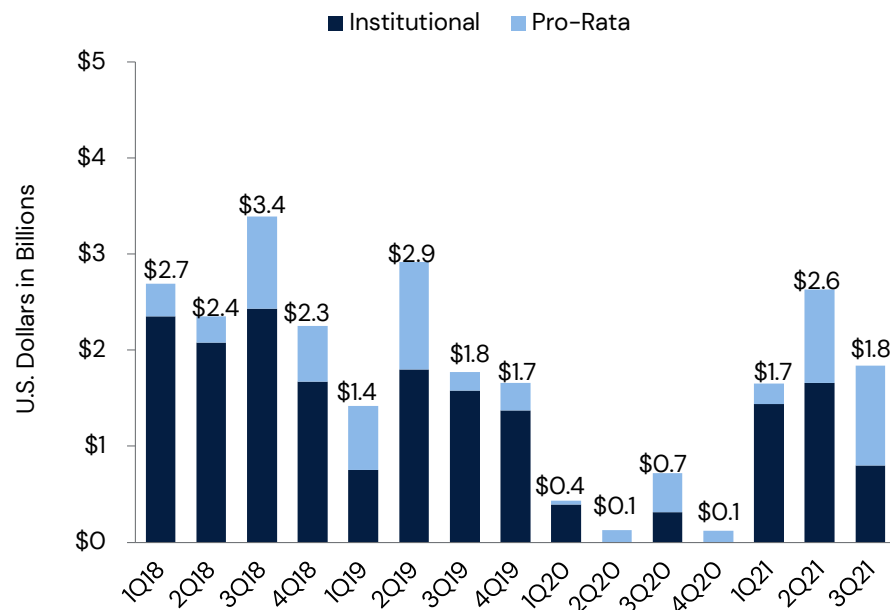
Key Market Stats

- **Strong loan volumes.** Annual middle market loan volume through the first three quarters of 2021 increased substantially, year-over-year, as the broader global economy continues to rebound from the COVID-19 pandemic. Refinancing activity (34% of total volume) continues to drive increased volume as rates are nearing historic lows and competitive processes for strong private equity sponsored transactions continue to push volume forward. Leveraged buyout (LBO) (29%) and acquisition (25%) transactions have surged as Biden's tax policy pulled 2022 merger and acquisition (M&A) deals forward into 2021. Corporate purposes and mergers (~12%) accounted for the remaining balance.
- **Leverage remains elevated.** As of December 2021, Total Debt/EBITDA multiples for larger loans remained steady at 5.7x, the highest recorded level since 2005. A robust M&A environment and a continued supply/demand imbalance for middle market transactions caused lenders to increase available leverage in order to win deals. Equity contributions of ~40% are still required in most cases; however, elevated purchase multiples and excess dry powder with lenders and sponsors have driven leverage multiples higher.
- **Pricing throughout 2021 remained stable.** Average LIBOR spreads remained near 500 basis points (bps) with all in expected yields of

~6.0% for large, marquee deals and L+575 (bps) for smaller deals. Capstone continues to expect yields to hold in this range going into 2022 as competition for deals remains robust.

- **Private credit fund dry powder sits at record highs.** Private credit funds have maintained their record investable capital and will continue deploying through multiple vehicles heading into 2022.

Leverage Loan Volume per Quarter



Source: S&P Global Market Intelligence

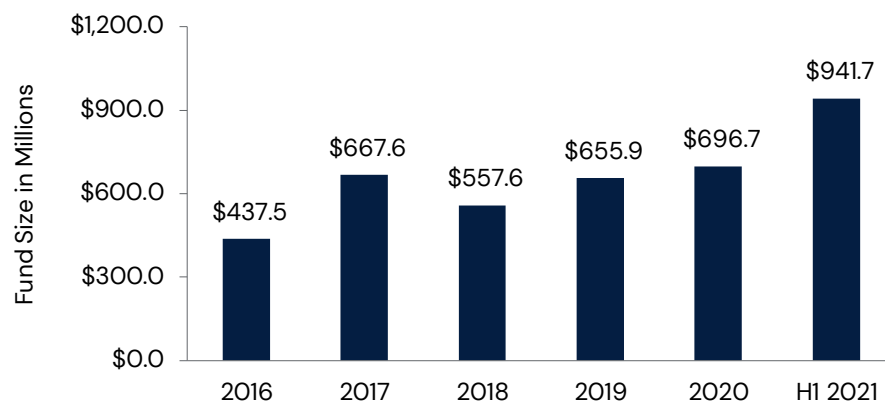
LEVERAGED FINANCE CONDITIONS (CONTINUED)

Quarterly Market Observations

- **Middle market M&A activity remains robust, driven by potential tax changes.** Supported by improving economic conditions, inexpensive debt capital, ample private equity dry powder, and the possibility of a capital gains tax hike, middle market M&A activity approached its highest levels on record in 2021. In a recent survey of M&A professionals, SRS Acquiom found that the proposed tax changes accelerated 2021 deal velocity with more than half (63%) of respondents indicating that their clients' or their own deal activities were accelerating before the close of 2021 in anticipation of proposed tax changes. As we look to 2022, just over half (52%) of respondents believe that deal activity will remain flat, with 43% of respondents anticipating a slowdown. Only a small percentage (5%) expect acceleration to continue in 2022.
- **Unitranche migrating up market.** Middle market private equity investors have long favored the unitranche structure for its flexibility and ease of use. However, over the past six years, direct lenders' average hold sizes have expanded from \$25–30 million to well over \$100 million. This growth, and the continued adoption of the unitranche structure, have given managers a competitive instrument to deploy more capital. In 2017, per Refinitiv LPC, only 28% of unitranche facilities were above \$250 million in size. Today, that number is up to 77%, reflecting a significant shift away from the broadly syndicated market.
- **ESG growing in importance to debt capital providers.** Conventional wisdom had private debt managers lagging behind their private equity counterparts in their commitment to environmental, social, and governance (ESG) investing. With new systematic approaches to ESG lending, that is no longer the case. In its recent survey of over 110

debt capital markets institutional investors, SS&C Intralinks found that 91% of respondents expect to issue more sustainable/ESG focused debt over the next year. Capstone has found that investments with an “ESG angle” attract strong lender interest, particularly from institutional investors like pension funds and insurance companies.

Average Size of Private Debt Funds



Source: The Lead Left

DEBT ADVISORY GROUP

Capstone's Debt Advisory Group helps privately-owned and sponsor-backed companies secure debt capital for organic growth, acquisitions, dividend recapitalizations and refinancings. The team works closely with clients to optimize their debt structures and secure the best long-term institutional partners for their business.

FINANCIAL ADVISORY SERVICES



John Koskiewicz

Managing Director, Financial Advisory Services
214-886-7845
jkoskiewicz@capstonepartners.com



Jeremy Putka

Associate, Financial Advisory Services
720-234-7121
jputka@capstonepartners.com

The Value of the Interim Executive

Private equity, venture capital, and investment management firms have often used interim executives to support portfolio companies when retaining a full-time operating partner or replacing a highly compensated executive does not properly serve the business in its short-term goals.

As former executive officers, consultants, and investment bankers, interim management professionals provide the operational and transactional experience to oversee boots-on-the-ground accounting, finance, performance improvement, sales, marketing, and cash management functions, while also affording companies with valuable M&A, investment evaluation, and capital-raising knowledge. Interim executives augment the capabilities of a well-trained technical manager with the skills of a strategic investor.

Contractor vs. Interim Executive

For business owners, it is likely that they have engaged a contractor to complete a project or perform a set of prearranged tasks. So, what is the difference between an interim executive and a contractor? The answer is linked to the services being provided.

Simply put, a contractor (e.g., outside accounting firm, social media/marketing consultant, IT administrator, product strategist, etc.) should be used when a specific objective can be performed, and that objective is independent of the strategic development of the business. For instance, contract accountants are an effective resource for logging accounting entries, performing month-end closings, paying bills, issuing invoices, and reconciling bank accounts. However, they are not typically the ideal resource for developing financial projections, forecasting inventory, planning cash flows, or managing lender and investor relationships. These strategic tasks benefit from the guidance of an experienced leader who is not only technically savvy in finance and accounting but who also has broad experience with and knowledge of the operational and sales functions of the business. In order to properly advise on financial projections, this executive must be able to understand and scrutinize the assumptions and parameters driving the company's forecasts, contribution margins, inventory lead times, borrowing capacity, and distribution tactics.

Ultimately, if a business needs help performing a well-defined set of tasks, contractors are a cost-effective way to address that need. They can do the work and train full-time employees to take over the responsibilities going forward. But, if the business would benefit from a strategic leader, who can analyze the cross-functional needs of the business and manage the implementation of a holistic process, this often exceeds the scope and skills of a contractor and is more successfully filled by an interim management professional.

FINANCIAL ADVISORY SERVICES (CONTINUED)

Responsibilities of an Interim Executive

The experience of a company's management team and the objective at hand will determine the type of interim executive that will provide the most value:

- **Interim Chief Financial Officer:** An interim CFO has extensive experience as a corporate consultant, company CFO, or investment banker. These executives are experts at analyzing investment opportunities, developing and maintaining forecasts and financial budgets, raising capital, communicating with lenders and investors, systematizing accounting processes, integrating enterprise resource planning systems, and supporting activities around mergers and acquisitions, such as sell-side preparations or merger integrations.
- **Interim Chief Operating Officer:** An interim COO also has a strong background in finance while providing a deeper understanding of product development, sales and marketing, supply chain management, and corporate administration (such as projects related to human resources and information technology). Operationally-focused interim managers support CEO and CFO teams with the implementation of new strategies across the company. This might include procurement and distribution enhancements, logistics planning, cost cutting initiatives, quality improvements, or process and policy developments.
- **Interim Chief Executive Officer:** Less common among middle market companies, but extremely beneficial in certain circumstances, an interim CEO is an experienced executive who can parachute into a business and immediately represent the brand. In cases where an interim CEO is engaged, the company may have lost its chief executive, and in order to quickly stabilize the business, an interim CEO is hired to lead employees, communicate with lenders and investors, and make swift decisions.

Interim Management in Practice

Interim managers are engaged in a variety of scenarios, but they are typically hired under one of the following circumstances:

1. **Business Growth:** A growing business may lack the resources or management expertise to prepare for a transaction, manage increasing financial obligations, analyze investment opportunities, or construct robust financial plans that support business strategies.
2. **Unexpected Departure:** A business that experiences the unexpected departure of a senior leader needs an executive manager who can start immediately, organize and prioritize functional projects, and support a team of technical contributors.
3. **Crisis Management:** A business in crisis is usually on poor terms with its financial stakeholders, and in the event these stakeholders have not already required the use of an interim executive, a company can proactively seek support from an interim manager to alleviate tensions between the company and external parties.

Taking Action

Hiring an interim executive provides a quick and strategic solution for companies experiencing difficult organizational changes. When facing the unexpected, time is of the essence – acting quickly before issues worsen and options disappear will give your interim executive and your business a stronger chance of achieving a successful outcome. If you have questions regarding interim management or are interested in engaging an interim executive, Capstone's [Financial Advisory Services](#) team specializes in working with middle market companies and financial stakeholders to stabilize, rehabilitate, and grow companies. Please [contact us](#) to discuss your specific challenges and how we can help you resolve them.

INDUSTRY SPOTLIGHT



Brian Boyle

Managing Director

312-287-9812

bboyle@capstonepartners.com

Food Distribution Industry Update

M&A activity in the Food Distribution sector has been on a torrid pace through the first three quarters of 2021 with a total of 62 transactions having been announced so far, with expectations that the full year number will exceed 80 transactions. This number greatly exceeds the five-year average of 58 transactions per year.

We have identified five key themes that have fueled this acceleration in M&A activity:

Recovery in the Food Service sector: After dismal 2020 results, the Food Service sector has rebounded sharply. The belief by both strategic and financial buyers that the COVID-19 pandemic is coming to an end (or at least will be manageable) has instilled confidence to aggressively pursue M&A activity in the Food Service sector.

A Difficult Operating Environment: Inflation is creating a more difficult operating environment for food distribution companies. Although revenues have generally increased for well positioned companies, margins have eroded. Rising fuel and transportation costs, rising warehousing costs, increased wages due to labor shortages, and supply chain disruptions have all contributed to the challenging environment. This phenomenon has helped some middle market operators come to the realization that continuing alone may not be the best strategy to maximize shareholder value.

Rising Transaction Multiples: Despite the difficult operating environment, transaction multiples have remained high and actually increased during this period to a mean EBITDA multiple of over 15x. The fact that transaction multiples have increased during this difficult period may seem counter-intuitive, but expectations from many buyers is that these inflationary pressures will moderate. Meanwhile, sellers are willing to transact to capture these higher multiples and offset their lower earnings.

Vertical Integration: As the process of delivering from point A to point B has become increasingly less profitable, food distribution companies are focused on moving up the value curve. Broadline distributors have been focused on acquiring specialty food distribution businesses with value-added food processing capabilities. Specialty food distribution companies have been focused on enhancing their offerings by investing in further processing capabilities and automation.

Channel Crossover & Scale: During the height of the pandemic, food distributors that had traditionally focused on the food service channel started, or increased, selling into the grocery, club, and specialty retail channels. These strategic decisions were fueled out of necessity given the Restaurant sector's sharp decline, but this channel crossover continued even as the food service channel recovered. Additionally, companies continue to focus on gaining scale to improve operating leverage and efficiencies.

Heading into 2022, we expect these five trends to continue, but we do look for some relief in supply chain disruptions. While we anticipate some moderation in inflationary pressures, we expect costs to remain elevated well above pre-pandemic levels. Labor shortages will be on the forefront of every CEO's list of concerns, adding fuel for continued consolidation in the industry.



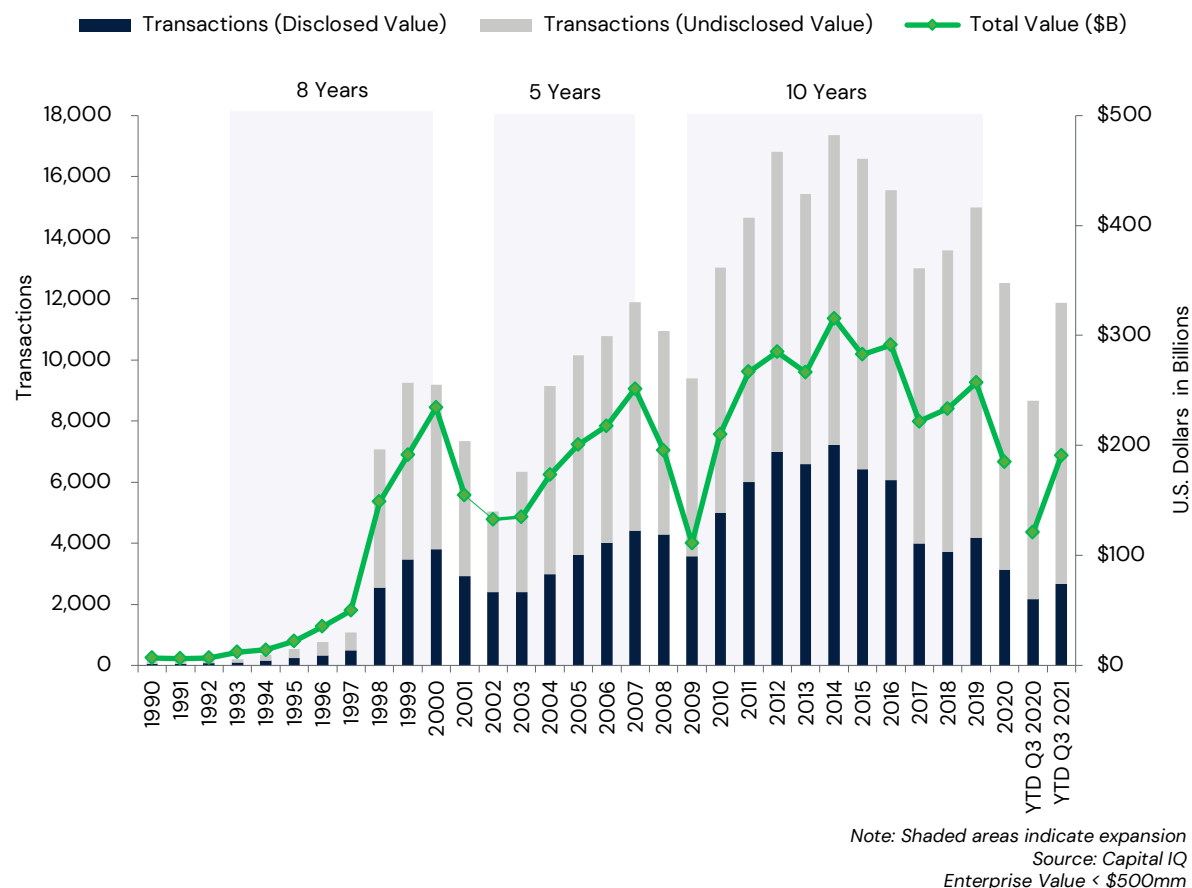
MIDDLE MARKET M&A ACTIVITY

M&A AMID ECONOMIC CYCLES

MIDDLE MARKET M&A ON PACE FOR HISTORIC YEAR

- Total closed transactions through Q3 2021 have surged 37.2% over the prior year period. Middle market M&A volume is on pace for a historic year, following lackluster deal activity through much of 2020 which saw volume fall 16.4% from 2019.
- Competition in deal processes has encouraged aggressive bidding behavior, evidenced by the average transaction value through Q3 rising to a record of \$71.7 million, increasing nearly 29% year-over-year.
- Bandwidth constraints and delays for transaction related services continue to challenge dealmakers, although volume is expected to remain at elevated levels through the final quarter.

Middle Market Transactions

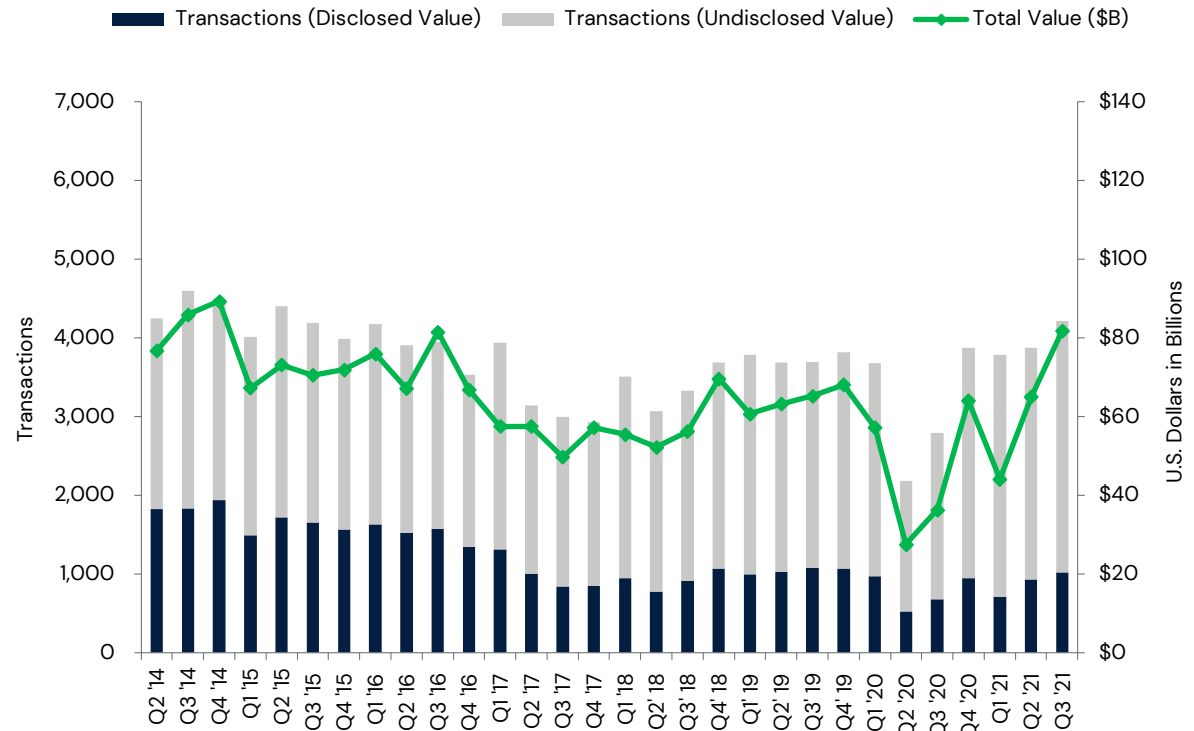


QUARTERLY M&A VOLUME

Q3 DEAL VOLUME SURPASSES PRIOR QUARTER

- Transaction volume in Q3 increased 8.7% from Q2 and reached the highest level of quarterly transactions since Q2 2015. Deal volume has increased in each of the last two quarters, setting the stage for a potentially historic Q4.
- Average middle market transaction enterprise value increased 14.4% from the prior quarter to a record of \$80 million in Q3.
- Prospective tax increases fueled a race to the market for many business owners. The vast pipeline of deals approaching or in the closing process is expected to contribute to robust levels of transaction activity in Q4.

Quarterly Middle Market Transactions



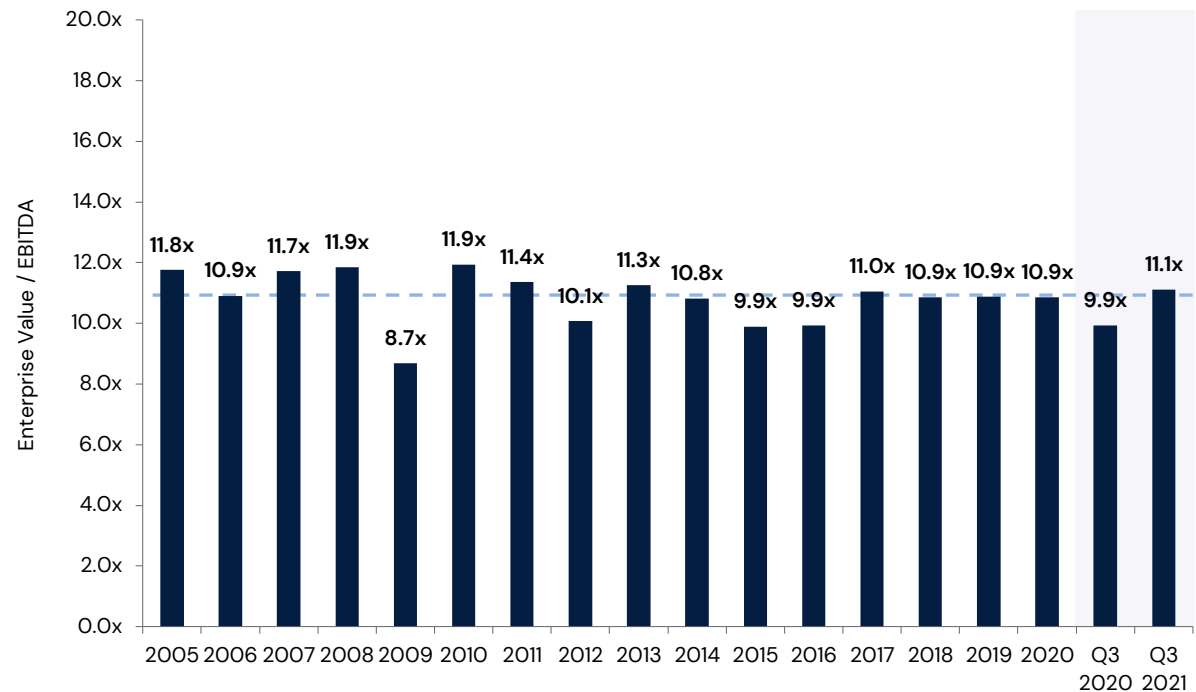
Source: Capital IQ
Enterprise Value < \$500mm

PRICING TRENDS

EBITDA TRANSACTION MULTIPLES INCREASE IN Q3

- Valuations remained elevated in Q3, with the average EBITDA multiple amounting to 11.1x, a strong increase from year-over-year levels and slightly above historic averages.
- Strategic buyers, leveraging improved balance sheets, have paid premium multiples for accretive targets. Private equity firms have also demonstrated a willingness to pay elevated multiples for attractive businesses that complement their investment thesis.
- Attractive privately-owned businesses continue to fetch elevated valuations amid a buyer frenzy for high quality assets with strong growth prospects and healthy margins.

Middle Market Average EBITDA Multiple



Dotted line indicates 2005 to 2020 average of 8.8x

Source: Capital IQ

Includes multiples 3x-30x

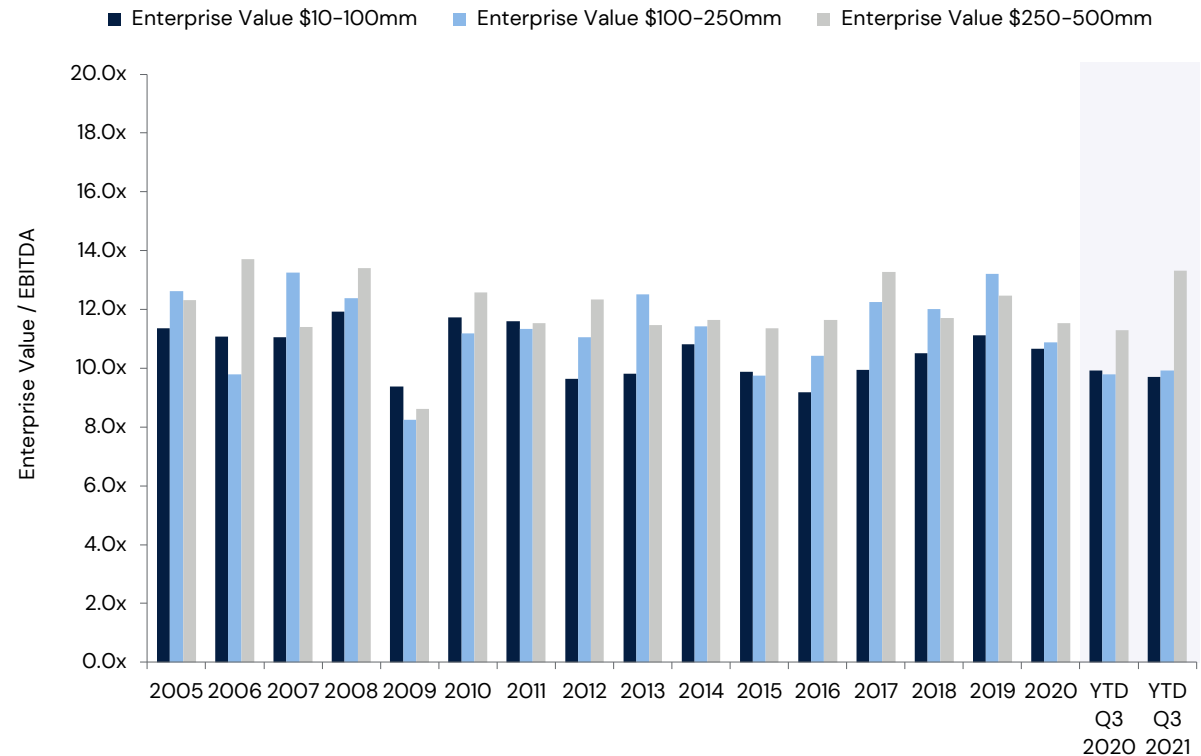
Enterprise Value < \$500mm

BREAKING IT DOWN BY SIZE

CORE MIDDLE MARKET VALUATIONS RISE

- Average EBITDA multiples in the core middle market, enterprise values between \$100 and \$250 million, increased to 9.9x through Q3 from 8.8x through Q2. Average valuations are modestly higher compared to the prior year's average of 9.8x.
- Upper middle market valuations, characterized by enterprise values between \$250 and \$500 million, increased substantially year-over-year through Q3 to 13.3x and have mirrored valuations recorded through Q2.
- Story deals have struggled to attract buyer attention while deals with strong growth, limited COVID impacts, and high-quality financial reporting are garnering premium valuations.

Average Enterprise Value to EBITDA Multiple



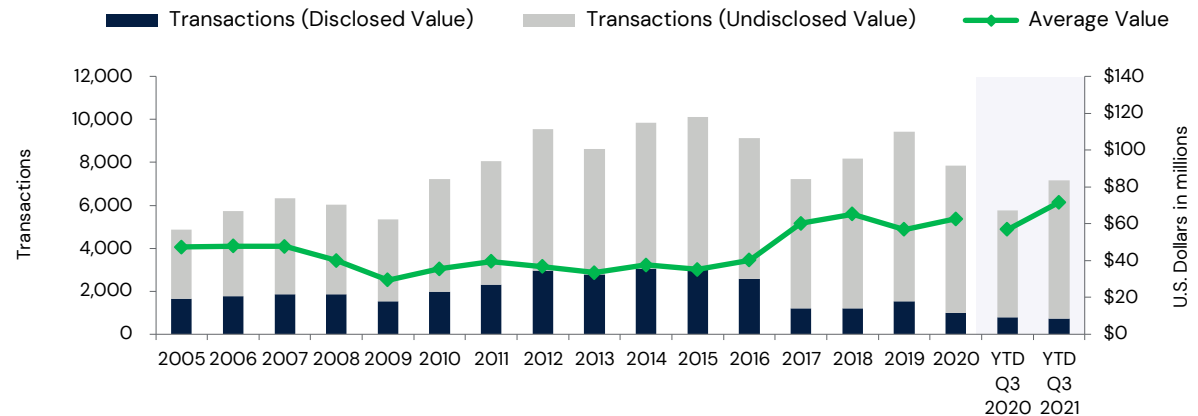
Source: Capital IQ
Includes multiples 3x-30x
Enterprise Value < \$500mm

STRATEGIC ACQUIRERS

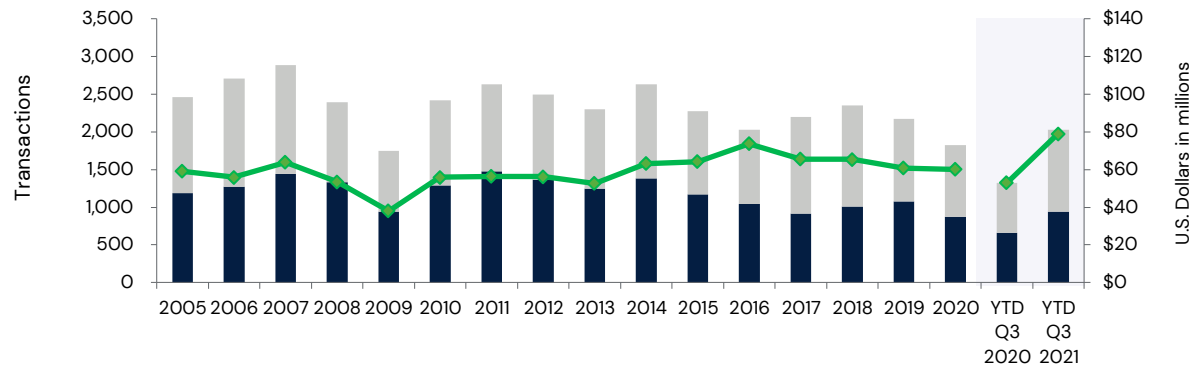
AVERAGE DEAL VALUE RISES FOR STRATEGIC BUYERS

- Strategic buyers are paying elevated prices to close deals, as average deal value for acquisitions by private and public buyers has reached record levels through Q3 at \$71.6 million and \$79 million, respectively.
- The number of closed deals by private companies increased 1.2% from Q2 and rose 24.4% when compared to the prior year period.
- Total public company closed acquisitions in Q3 nearly mirrored Q2, modestly increasing 0.7%. Closed deals through Q3 have substantially outpaced year-over-year levels, rising 52.8%.

Acquisitions by Private Companies



Acquisitions by Public Companies



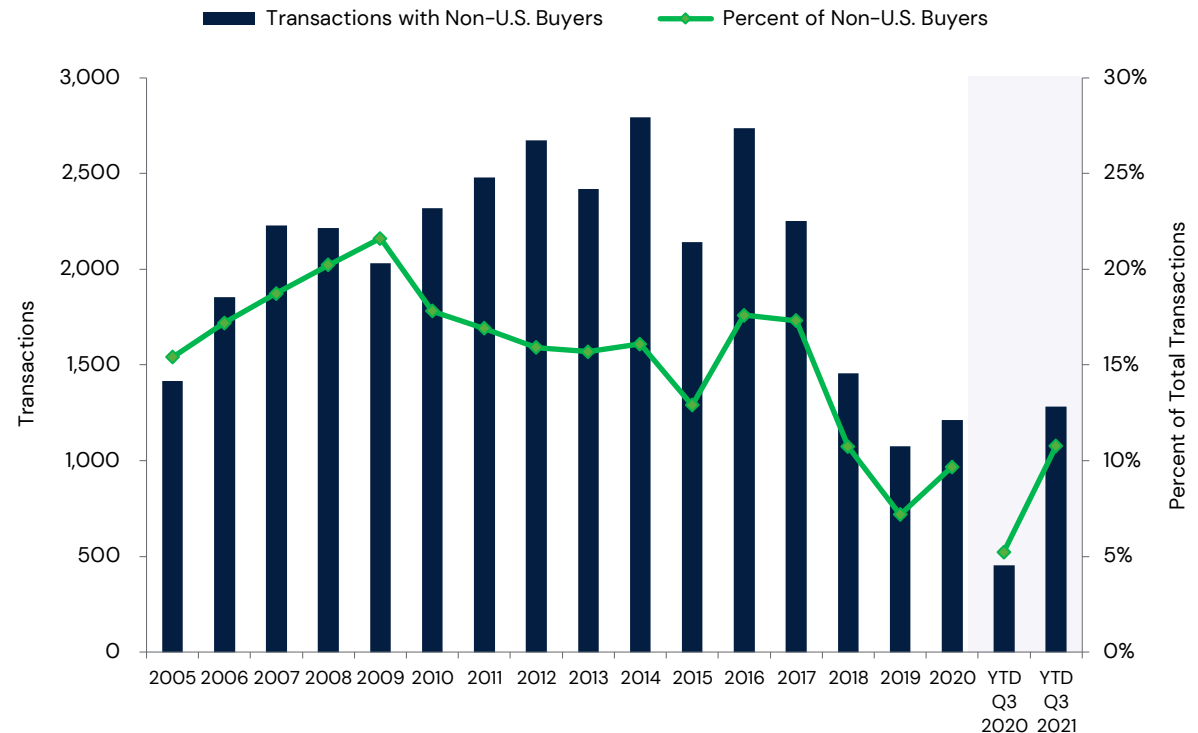
Source: Capital IQ
Enterprise Value < \$500mm

FOREIGN ACQUIRERS

CROSS-BORDER DEAL ACTIVITY REMAINS HEALTHY

- Non-U.S. buyers accounted for 10.8% of middle market transactions, a strong uptick year-over-year but slightly below Q2 levels. On average, foreign buyers have paid 10.9x EBITDA for companies based in the U.S. and Canada.
- The United Kingdom has continued to lead foreign buyer activity. Application software targets remain the most highly sought-after domestic assets.
- Foreign relations and the regulatory environment will remain key factors in cross-border transactions throughout 2021 and into the new year.

Non-U.S. Buyers



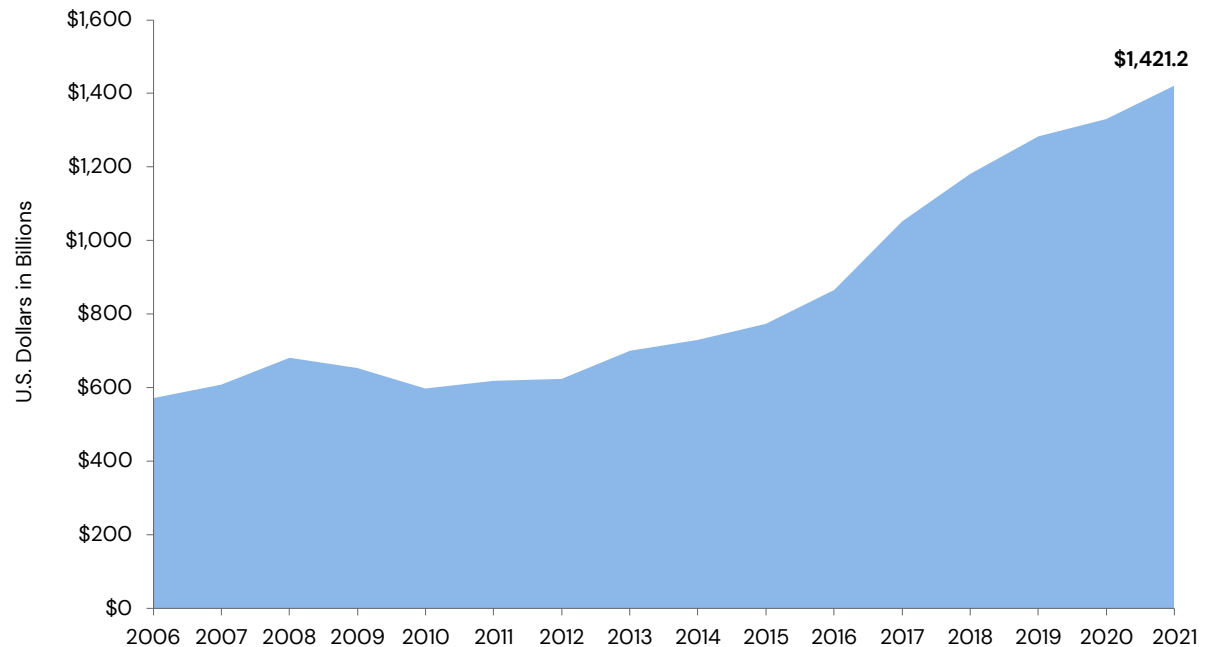
Source: Capital IQ
Enterprise Value < \$500mm

PRIVATE EQUITY DRY POWDER

DRY POWDER LEVELS REMAIN FAVORABLE FOR PE DEALS

- Private equity firms have actively deployed capital to high growth sectors, leveraging expansive levels of dry powder which has amounted to over \$1.4 trillion in 2021.
- Many sponsors have increasingly focused on building sector or situational specialization, seeking differentiation in the market amid elevated competition in M&A sale processes.
- Deal flow has continued at a historic pace with private equity firms being increasingly selective in bidding efforts amid capacity constraints and the frenzy of activity – pursuing areas in which they hold expertise or a track record of success.

PE Capital Overhang by Year



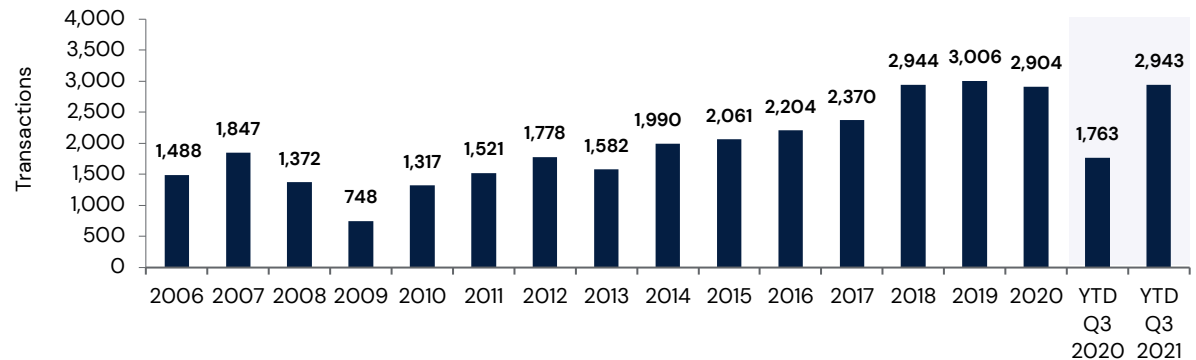
2021 dry powder figure as of March 31, 2021
Source: PitchBook

PRIVATE EQUITY ACTIVITY

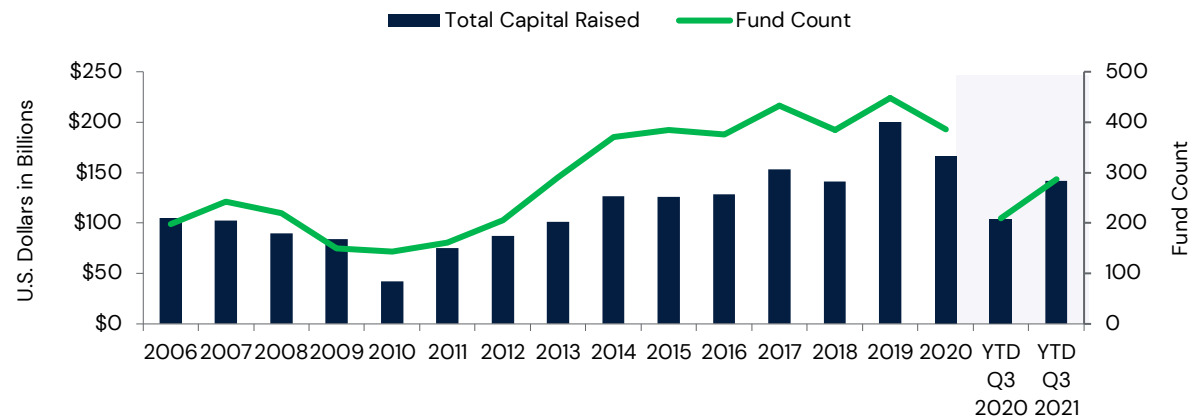
PE CLOSED TRANSACTIONS SURPASS FULL YEAR 2020

- PE transaction volume through Q3 has already eclipsed full year 2020 levels, however volume has moderated in the past two quarters, with total closed deals falling 16.4% in Q3 from elevated levels in Q2.
- Middle market PE fundraising has swelled to over \$142 billion through Q3, nearing the record setting pace experienced in 2019. As many sponsors have expedited holding times to capitalize on high valuations, GPs have sought to raise and deploy capital faster.
- ESG factors continue to gain traction in private equity investment screening and diligence efforts.

Middle Market Transactions Closed by Private Equity Firms



Middle Market Fundraising by Private Equity Firms



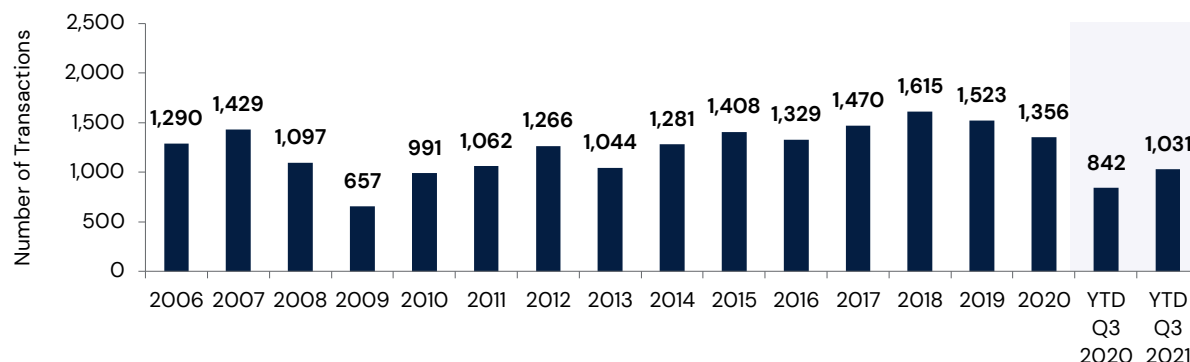
Source: PitchBook
Note: EV; \$25-\$500mm, Fund size < \$5B

PRIVATE EQUITY TRANSACTION TYPES

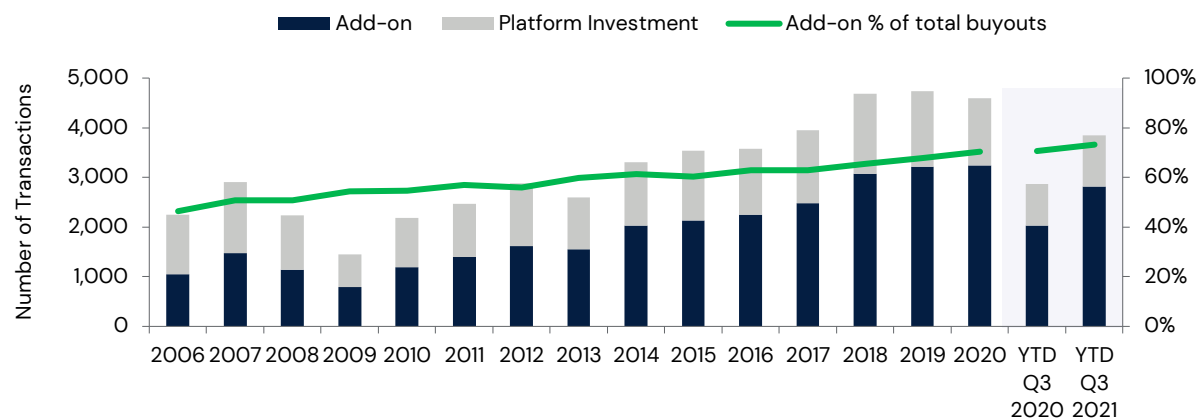
SPONSORS INCREASINGLY UTILIZE ADD-ONS

- PE platform investments declined 19% in Q3 compared to Q2, although remain 22% higher year-over-year through Q3.
- Cheap access to capital has provided a favorable backdrop for robust buyout activity. With the Federal Reserve beginning to taper bond purchases, many suspect multiple rate increases in 2022.
- Add-on acquisitions continue to comprise a large percentage of total buyouts, accounting for nearly 75% through Q3. The prevalence of bolt-on deals bodes well for smaller middle market companies that can serve as valuable additions to bolster a sponsor's portfolio holding company.

PE Platform Investments



PE Add-On Acquisitions



Source: PitchBook

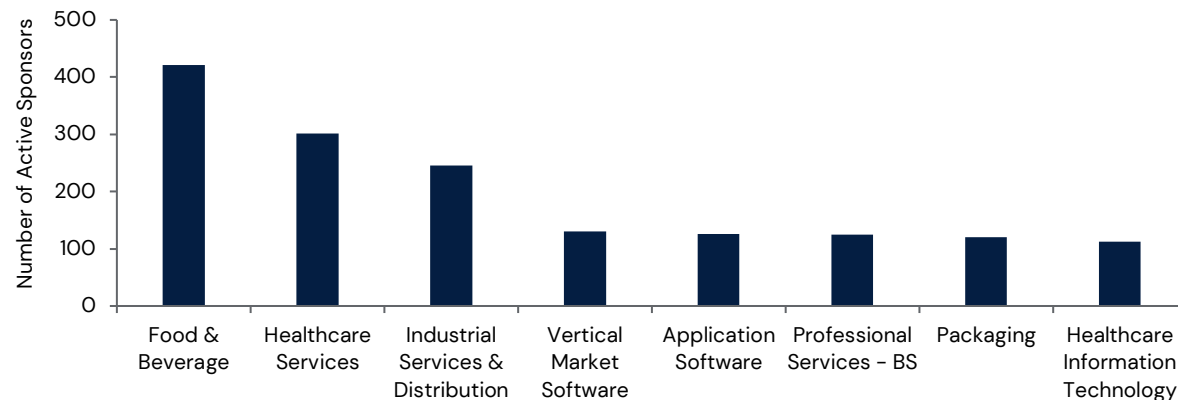
Note: Includes all U.S. PE transactions

CAPSTONE'S PRIVATE EQUITY NETWORK PREFERENCES

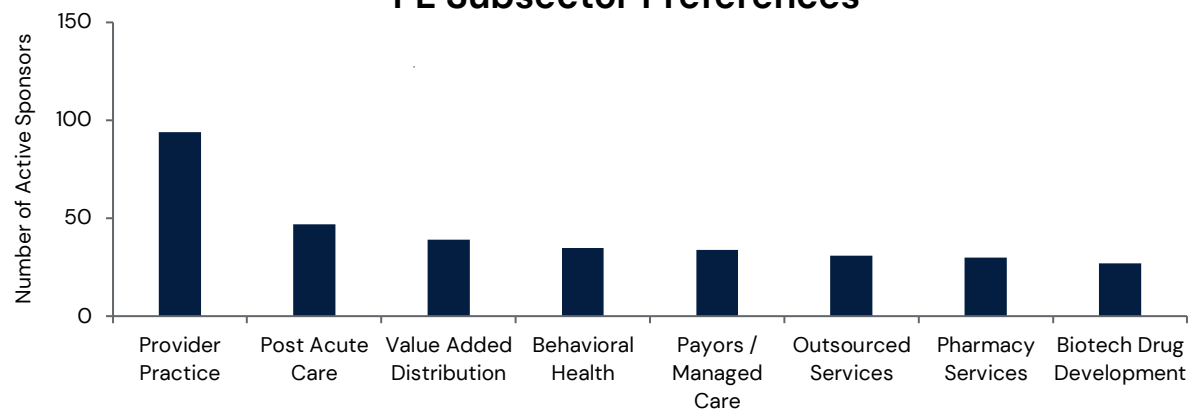
FOOD & BEVERAGE, HEALTHCARE IN DEMAND

- Many sponsors have been working at near full capacity to close deals prior to year end while continuing to eye attractive opportunities in high growth sectors, especially when they have existing investments in the space.
- Capstone's network of PE firms have identified Food & Beverage and Healthcare Services as their most preferred sectors to deploy capital, followed by Industrial Services & Distribution.
- PE firms have been hesitant to take on deals with imperfections or those that need additional positioning, however these deals are likely to experience more demand as supply normalizes in 2022.

PE Sector Preferences



PE Subsector Preferences



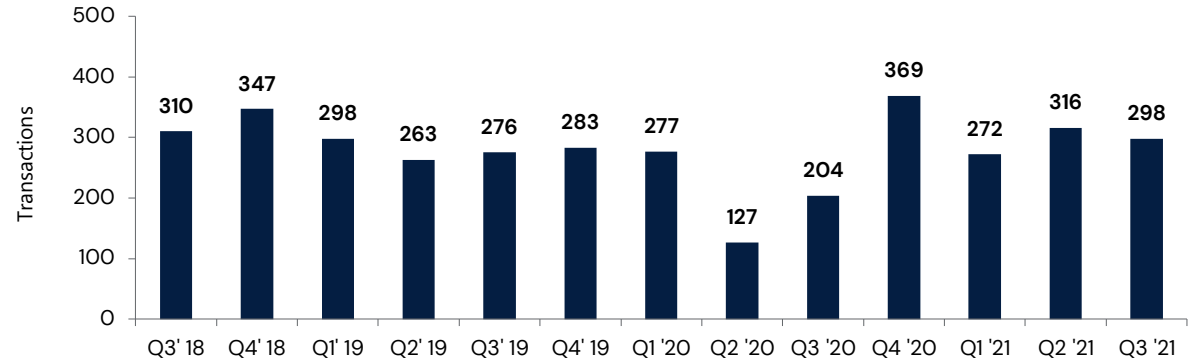
Source: Capstone proprietary data

PRIVATE EQUITY ACTIVITY

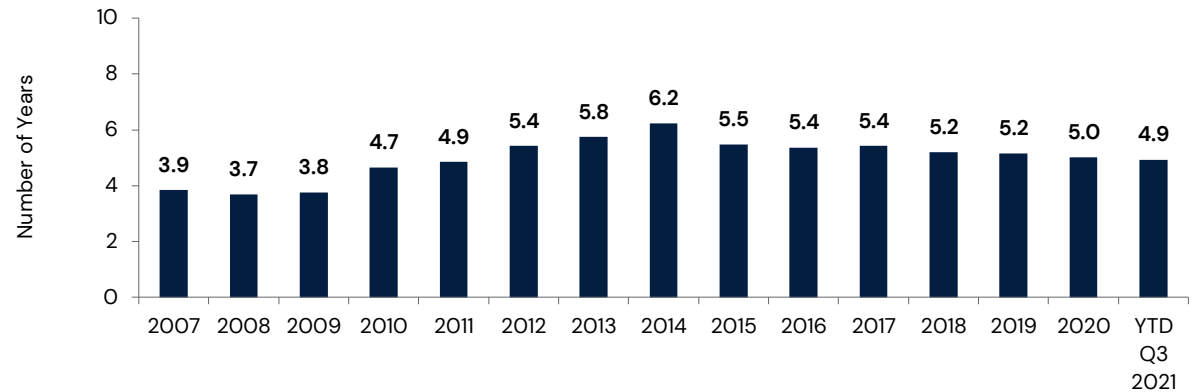
EXITS REMAIN HEALTHY, HOLDING TIMES FALL SLIGHTLY

- Private equity exit activity continues to recover from its 2020 lows, with Q3 exits surpassing historic levels despite declining modestly from Q2.
- The median holding time among sponsors fell modestly through year-to-date Q3, likely driven by sponsors exiting investments earlier than anticipated due to elevated valuations and robust buyer interest.
- Private equity firms are expected to continue to build sector-focused portfolios, with heightened competition for high-quality businesses.

Private Equity Exit Activity



Median Private Equity Holding Period



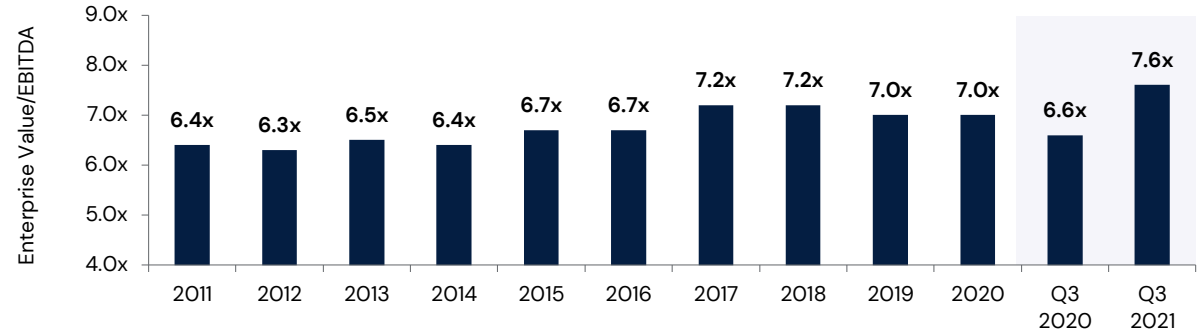
Note: Exit activity inclusive of all enterprise value ranges
Source: PitchBook

PRIVATE EQUITY VALUATIONS

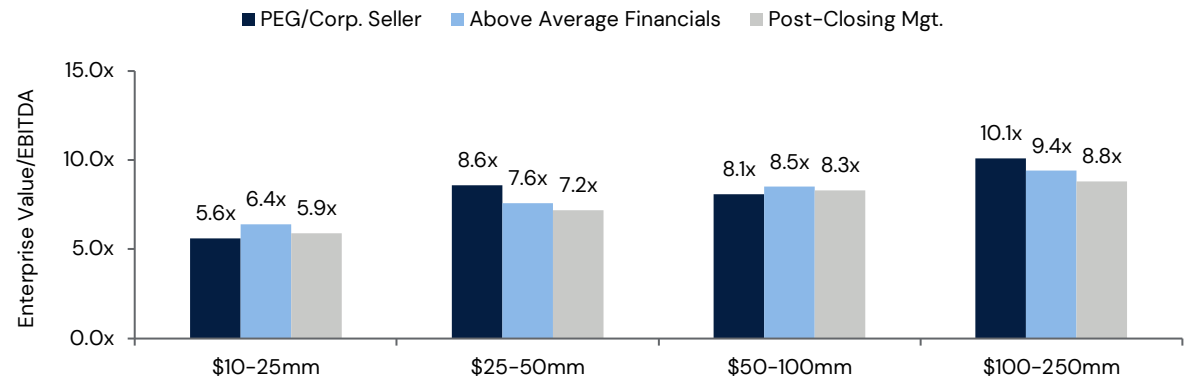
EBITDA MULTIPLES PAID BY PRIVATE EQUITY SURGES IN Q3

- The average transaction multiple paid by private equity firms has reached historic levels, amounting to 7.6x EBITDA in Q3, a strong increase from 7.2x in Q2.
- Sponsors are encountering increased competition in deal processes, with few discounts available in today's market, contributing to market clearing bids that have driven the elevated pricing environment.
- Private equity or institutional backing, above average financials, and a post-closing management solution continue to be key drivers of premium multiples in middle market M&A sale processes.

Average EBITDA Multiple Paid By Financial Buyers



Key Transaction Valuation Drivers



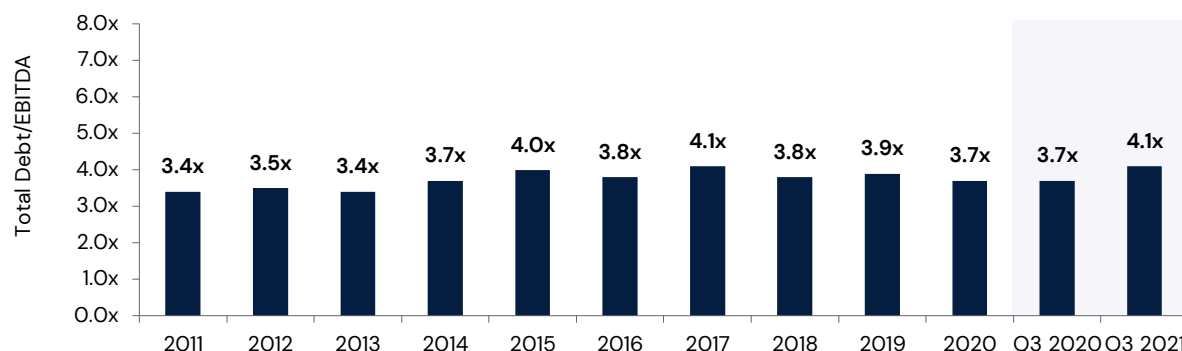
Source: GF Data®
GF Data® defines Above Average Financial Performers as businesses with TTM EBITDA margins and revenue growth above 10%, or one above 12% and the other metric at least 8%
Includes multiples 3x-15x; Enterprise Value \$10mm-\$250mm

PRIVATE EQUITY VALUATIONS

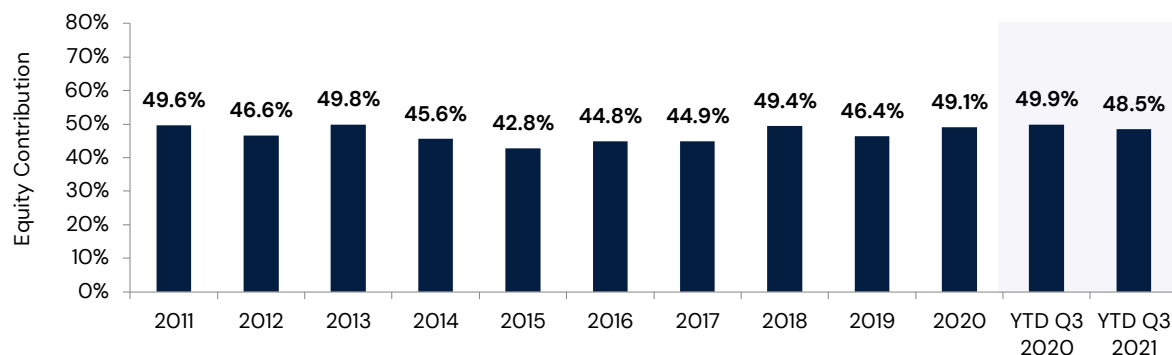
DEBT MULTIPLES RISE SUBSTANTIALLY IN Q3

- Total debt multiples have increased on both a year-over-year and quarterly basis, with the average multiple reaching 4.1x in Q3 – seemingly moving in tandem with heightened M&A transaction multiples.
- Equity contributions through Q3 have declined slightly compared to the prior year period, amounting to an average of 48.5%.
- A robust M&A environment has caused lenders to increase leverage to win deals. Equity contributions of ~40% are still required in most cases, however, elevated purchase multiples and excess dry powder have driven leverage multiples higher.

Average Debt Multiples of Middle Market LBO Transactions



Average Middle Market LBO Equity Contribution



Source: GF Data®
Includes multiples 3x-15x; Enterprise Value \$10mm-\$250mm



CAPSTONE BAROMETERS

CAPSTONE PARTNERS' FULLY INTEGRATED EXPERTISE

We have developed a service delivery model that can address the needs of any client situation, supported by vast internal resources. These capabilities are delivered together with deep domain expertise across 12 dedicated industry groups with an established, real-time access to the private equity community.

Mergers & Acquisitions

- Sell-side Advisory
- Buy-side Advisory
- Recapitalizations
- Mergers & Joint Ventures

Capital Advisory

- Equity Advisory
- Debt Advisory
- Infrastructure Finance

Financial Advisory

- Transaction Advisory
- Interim Management
- Performance Improvement
- Valuation Advisory
- Litigation Support

Special Situations & Restructuring

- Special Situations
- Turnaround
- Restructuring
- Bankruptcy
- Insolvency

Industry Groups



Aerospace, Defense,
Government & Security



Building Products &
Construction Services



Business Services



Consumer



Education &
Training



Energy, Power, &
Infrastructure



FinTech & Services



Healthcare



Industrials



Industrial
Technology



Technology,
Media, & Telecom



Transportation
& Logistics

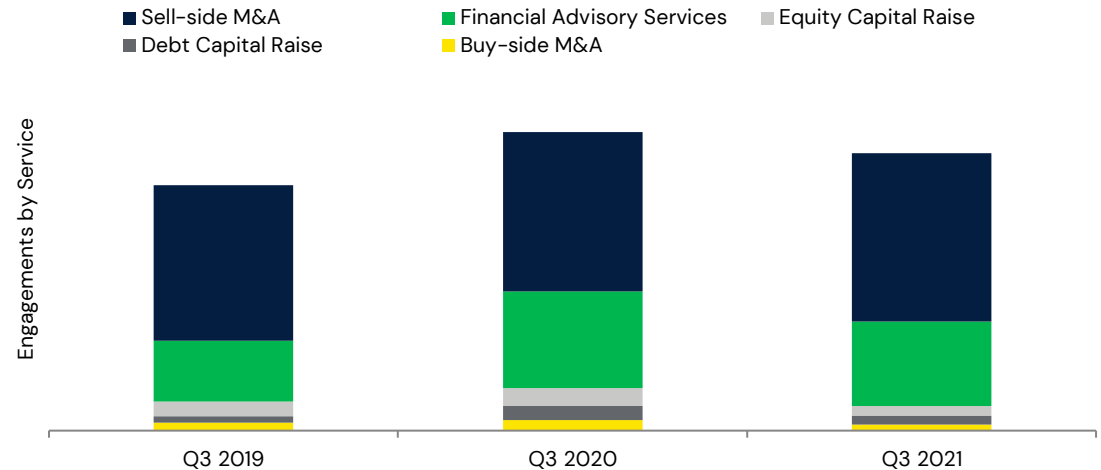
Sponsor Coverage Group

FIRM DATA

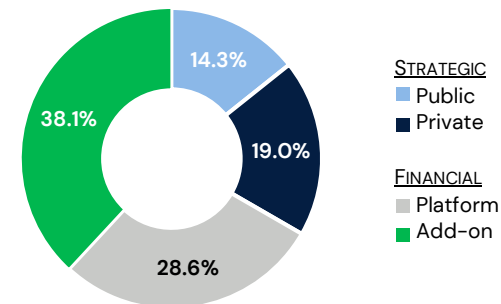
SELL-SIDE M&A VOLUME SHOWS NO SIGNS OF SLOWING

- Sell-side M&A volume has continued at elevated levels through Q3 with dealmakers and financial and strategic buyers near full capacity evaluating and closing transactions before the end of the year.
- Moving into 2022, buyers may gain additional capacity to evaluate more deals, which could bode well for companies that require additional posing due to COVID impacts or unusual operating events.
- Private equity firms continue to utilize buy and build strategies to scale their holdings, with sponsor add-ons accounting for 38.1% of Capstone closed deals.

Capstone Engagements By Service



Capstone TTM Buyer Breakdown



Source: Capstone propriety data based on live engagements and closed sell-side engagements

RECENT DEAL CLOSINGS

Capstone is an active leader in middle market M&A advisory and closed a record number of deals in 2021, serving clients and their needs despite the unprecedented disruptions to the economy. Select the deal tombstones below to read the full press release.

| | | | | | | |
|---|---|--|---|--|---|---|
|  <p>HAS BEEN ACQUIRED BY</p>  |  <p>HAS BEEN ACQUIRED BY</p>  |  <p>HAS BEEN ACQUIRED BY</p>  <p>A SUBSIDIARY COMPANY OF</p>  | <p>INDUSTRIAL METALS RECYCLING OPERATION</p> <p>FINANCIAL ADVISORY & INTERIM MANAGEMENT</p> |  <p>HAS BEEN ACQUIRED BY</p>  |  <p>FIXED COST REDUCTION</p> <p>HAS BEEN ACQUIRED BY</p>  |  <p>HAS BEEN ACQUIRED BY</p>  |
|  <p>HAS BEEN ACQUIRED BY</p> <p>AN UNDISCLOSED STRATEGIC BUYER</p> |  <p>HAS BEEN ACQUIRED BY</p>  <p>A PORTFOLIO COMPANY OF</p>  |  <p>HAS BEEN ACQUIRED BY</p>  |  <p>HAS BEEN ACQUIRED BY</p>  |  <p>HAS SOLD ITS FIRE ALARM DIVISION TO</p>  |  <p>HAS RECAPITALIZED WITH</p>  |  <p>TRANSACTION ADVISORY SERVICES</p> |
|  <p>HAS BEEN ACQUIRED BY</p> <p>AN UNDISCLOSED BUYER</p> | <p>OGLE SCHOOL HAIR • SKIN • NAILS</p> <p>A PORTFOLIO COMPANY OF</p>  <p>GREY ROCK CAPITAL GROUP</p> <p>HAS BEEN ACQUIRED BY</p>  |  <p>HAS RECAPITALIZED WITH</p>  |  <p>\$ 363 SALE ADVISORY</p>  |  <p>HAS BEEN ACQUIRED BY</p>  |  <p>HAS RECAPITALIZED WITH</p>  |  <p>HAS RECAPITALIZED WITH</p>  |

LEADERSHIP TEAM



JOHN FERRARA, FOUNDER AND CEO

jferrara@capstonepartners.com | 617-619-3325

John has dedicated 30+ years to serving as a trusted advisor to privately held businesses. Representative of over 200 engagements, he has acted as investment banker, management consultant, interim executive, investor, founder and board member. John has been recognized as one of the Top 50 M&A advisors in the U.S. and honored as an M&A Advisor Hall of Fame inductee. Under his leadership, Capstone has expanded to 19 offices in the U.S., U.K., and Brazil with an international platform that spans over 450 professionals in 40 countries worldwide. John graduated from Wesleyan University with an MBA from UCLA and The London School of Economics.



PAUL JANSON, COO

pjanson@capstonepartners.com | 303-887-0174

With 25 years of executive experience, Paul manages all administrative, legal and compliance matters for the firm and serves on Chairman of the Investment Banking Committee. On the M&A Advisory side, he is active in telecommunications services, manufacturing and infrastructure. Previously, Paul served as President & CEO of Camiant, a Packet Cable Multimedia broadband company. Paul was also CEO of Worldbridge Broadband Services Inc, a broadband and telecommunications company that was later acquired by C-Cor. Paul then became President of C-Cor's Global Services Division. He earned a BA-Business from Saint Anselm College.



JACOB VOORHEES, HEAD OF M&A

jvoorhees@capstonepartners.com | 617-216-1543

Jacob brings over 15 years of experience to the Capstone Partners investment banking team. As one of the founding members of Capstone Partners, he helped build Capstone's brand over the past decade until the merger with Headwaters MB in late 2017. Today, Jacob serves as the Head of Global M&A and is responsible for spearheading our international capabilities and coverage. Jacob received an MBA from the Sloan School of Management at Massachusetts Institute of Technology (MIT) and a BS from Cornell University.



TODD MCMAHON, HEAD OF INVESTMENT BANKING

tmcmahon@capstonepartners.com | 617-619-3334

Todd McMahon possesses over 20 years of transaction, financial services and corporate executive experience. Prior to Capstone Partners, Todd was President of Array Financial Services, a Boston based boutique M&A advisory firm he founded in 2002. He began his career at Putnam Investments, later moving to Bank Boston's investment banking group. He earned his MBA from Boston University and his BA from the University of Massachusetts.



DANIEL MCBROOM, HEAD OF PRIVATE CAPITAL MARKETS

dmcmbroom@capstonepartners.com | 303-951-7128

Daniel has 15 years of private and investment banking experience and is responsible for sourcing and analyzing hundreds of companies a year introduced by the firm's institutional clients and partners. Select companies are engaged and his team will stay involved until the transaction is closed. Before his financial career, Daniel spent seven years as a pilot in the United States Air Force. He earned an MBA from the University of Notre Dame and a BS from the United States Air Force Academy.

LEADERSHIP TEAM (CONTINUED)



BRENDAN BURKE, HEAD OF SPONSOR COVERAGE

bburke@capstonepartners.com | 303-531-4603

Brendan has 16 years in investment banking experience. He oversees the firm's outreach to private equity sponsors and recruitment of senior investment bankers. Since joining Headwaters MB (now Capstone) in 2004, he has held roles in transaction execution, business development, recruiting and marketing. In 2012, he was awarded 40 UNDER 40 by the M&A Advisor. He received a BA in Politics, Philosophy, Economics from Pomona College.



PETER ASIAF, HEAD OF BUSINESS DEVELOPMENT

pasiaf@capstonepartners.com | 617-619-3368

Peter has more than 20 years of experience as a senior business development executive across the professional and financial services industries. He has been a growth-oriented leader in early-stage, middle-market and Fortune 500 enterprises, helping them to design and execute strategic expansion plans, optimize brand positioning and strengthen key market relationships. Peter is a Certified Exit Planning Advisor (CEPA) designated by the Exit Planning Institute.



BRIAN DAVIES, MANAGING PARTNER, FINANCIAL ADVISORY SERVICES GROUP

bdavies@capstonepartners.com | 617-619-3328

Brian has 20+ years of experience working in the fields of corporate recovery, business reorganization and interim management services. He has provided financial advisory services to lenders, debtors, creditors' committees, trustees and equity holders in bankruptcy matters and out-of-court restructurings. Brian has provided assistance to under-performing businesses, acquirers of distressed companies. He has worked with companies to develop cost containment and asset rationalization plans, improve liquidity, re-engineer financial and other back-office functions. He received a MS from Bentley University and MSF from The McCallum School, Bentley University.



JIM CALANDRA, HEAD OF FINANCIAL ADVISORY SERVICES GROUP

jcalandra@capstonepartners.com | 617-619-3395

Jim has more than 25 years of experience in turnaround management consulting, interim management, fraud and forensic accounting, mergers and acquisitions, and recapitalizations. He has advised more than 50 companies through significant strategic transitions involving both public and private middle market companies with varying situations. Jim received a BS in Accountancy from Bentley University and an MS in Accountancy from The McCallum Graduate School of Business, Bentley University.



SARAH DOHERTY, DIRECTOR OF RESEARCH

sdoherty@capstonepartners.com | 617-619-3310

Sarah has nearly 10 years of professional research, writing, and data visualization experience and leads the strategic coverage and development of Capstone's middle market insights. She manages the firm's Research Team, which produces 150+ reports, articles, white papers, surveys, and capital markets updates each year. Her team's award-winning M&A commentary and analysis has been featured in more than 50 of the nation's top news outlets. Sarah earned a BA from Biola University and was recognized in 2021 with the "Emerging Leader Award" by the M&A Advisor.



Capstone Partners is one of the largest independently owned investment banking firms in the United States. For over 20 years, the firm has been a trusted advisor to leading middle market companies, offering a fully integrated range of expert investment banking and financial advisory services uniquely tailored to help owners, investors, and creditors through each stage of the company's lifecycle. Capstone's services include M&A advisory, debt and equity placement, corporate restructuring, special situations, valuation and fairness opinions and financial advisory services. Headquartered in Boston, the firm has 175+ professionals across the U.S. and an international presence including over 450 professionals in 40 countries. With 12 dedicated industry groups, Capstone delivers sector-specific expertise through large, cross functional teams on a global basis. For more information, visit www.capstonepartners.com.

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Research Team Report Contributors

Sarah Doherty, Director of Research
sdoherty@capstonepartners.com | 617-619-3310

Connor McLeod, Research Manager
cmcleod@capstonepartners.com | 617-619-3319

Max Morrissey, Research Associate
mmorrissey@capstonepartners.com | 617-619-3336

Luke LaCroce, Research Analyst
llacroce@capstonepartners.com | 617-619-3331

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