PitchBook

Lead sponsor Antares Capital

In partnership with ACG

# US PE Middle Market Report

2019 Annual

Lead sponsor

In partnership with

# Contents


| | |
|---|---|
| Introduction | 3 |
| Overview | 4-5 |
| Antares: Keynote and Q&A | 6-7 |
| Spotlight: VC-to-PE buyouts | 8-9 |
| ACG Q&A: The private equity opportunity in cannabis | 11-12 |
| Exits | 13-14 |
| Fundraising | 15-16 |


## Credits & contact


**PitchBook Data, Inc.**

**John Gabbert** Founder, CEO
**Adley Bowden** Vice President, Market Development & Analysis

**Content**

**Stephen-George Davis** Analyst, PE
**Zane Carmean** Senior Data Analyst

**Contact PitchBook**

**Research**
reports@pitchbook.com

Report design by Kelilah King

*Click here for PitchBook's report methodologies.*


# Introduction

**US PE middle-market (MM) dealmaking activity crossed the $500 billion threshold for the first time in 2019 after cresting $400 billion in 2018.** This activity was buoyed by several interest-rate cuts from the Federal Reserve in a climate of already low interest rates. Bracing for a potential downturn, dealmakers focused their attention on defensive, recession-resistant sectors, such as healthcare, and high-growth sectors, such as tech. PE shops have continued to use add-ons to execute buy-and-build strategies. While GPs continue to take fewer companies private, they have begun to supplement this decrease with non-control investments such as private investment in public equities (PIPE).

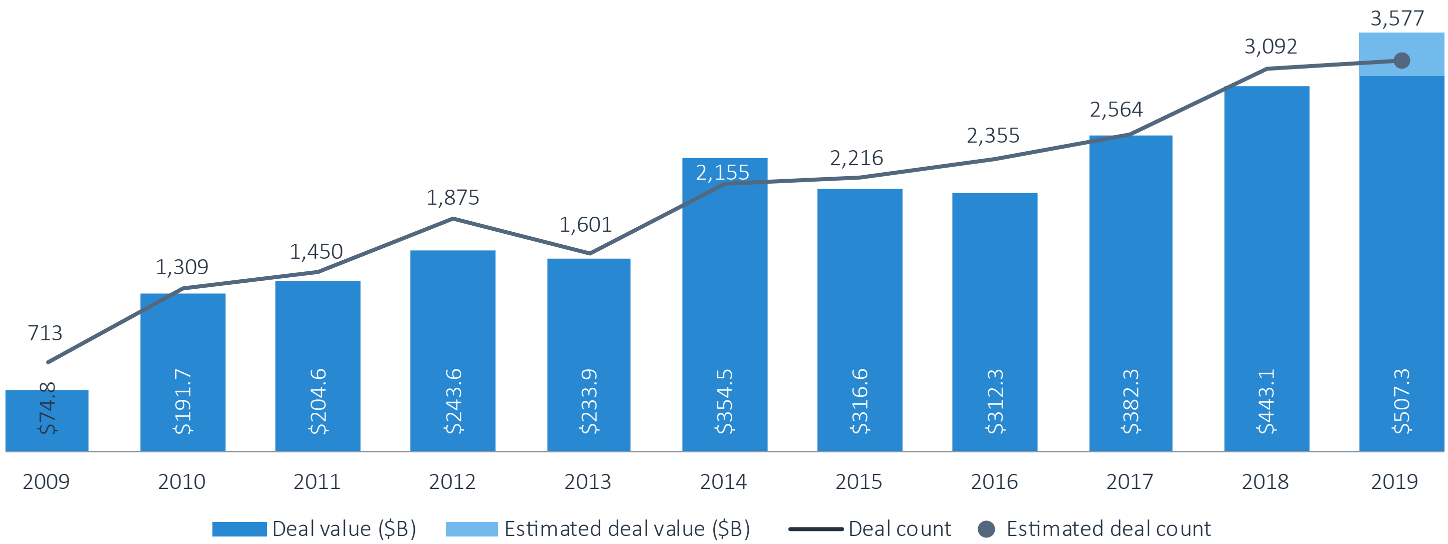
**MM exit activity in the US continued to hit multi-year lows.** 2019 notched less than $200 million in exit value, the first time this mark has been missed since 2013. While there were some bright spots, WeWork's failed IPO seemed to be the straw that broke the camel's back, leading to a downturn in IPO activity toward the latter half of the year. While corporate acquisitions were also down, with an almost 40% decrease, secondary buyouts (SBOs) picked up some of the slack with more than a 10% increase.

**Fundraising in the MM was stellar in the year, with a more than 25% increase in capital raised YoY.** 2019 marks the first time fundraising broke $130 billion and the first time that the median fund size breached half a billion. GPs continued diversifying to appease their client base—raising long hold funds, moving into new sectors and switching up their strategies by dipping into the public markets. LPs have also illustrated continued commitment to private market investment, with large university endowments, for example, doubling down on their allocations to PE.


**Stephen-George Davis**
Analyst, PE

# Overview

## MM PE deal activity

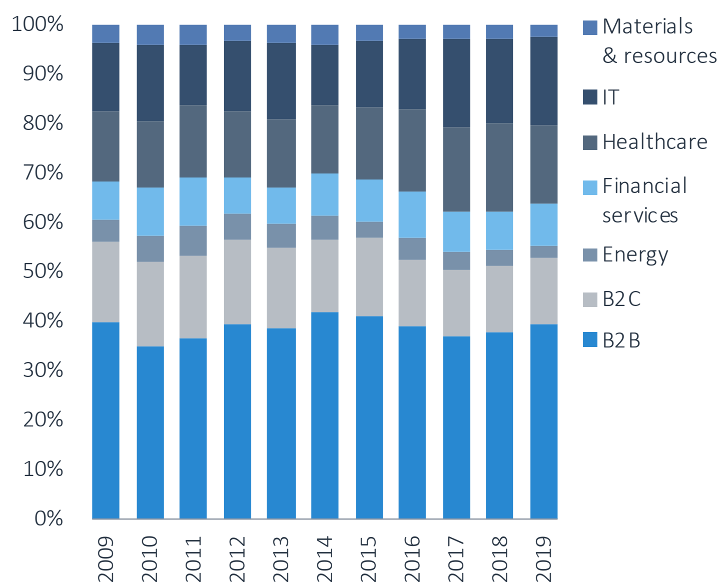



**Source:** PitchBook | **Geography:** US

MM deal activity reached new highs in both deal count and value in 2019. GPs closed 3,577 deals for $507.3 billion in value—YoY increases of 15.7% and 14.5%, respectively. MM dealmakers shook recession fears, trade tensions and geopolitical uncertainty in 2019 and continued closing deals at a record-setting clip. They also aimed to take advantage of a low-interest-rate environment prolonged by three rate cuts from the Federal Reserve. Median and average deal sizes also ticked up in the year, reaching $215.0 million and $309.7 million, respectively.

The healthcare sector has afforded investors a recession-resistant space to do deals, especially as many GPs believe we are late in the business cycle. The largest MM deal of the year was Nordic Capital's $993.0 million buyout of Michigan-based healthcare company Orchid Orthopedic Solutions. The orthopedic implant market is the beneficiary of secular tailwinds such as an increased access to orthopedic medical care and a growing elderly population, which is increasingly active. These long-running trends will not abate in an economic downturn.

## MM PE add-ons (#) by sector




**Source:** PitchBook | **Geography:** US

In addition, while tech isn't necessarily defensive or recession resistant, the sector is an area in which GPs can expect to see high (often organic) growth, even in a downturn. Syncsort's $700 million acquisition of Pitney Bowes' (NYSE: PBI) software solutions unit via its financial sponsors Centerbridge Partners and Clearlake Capital Group provides an example of one such MM tech deal. Pitney Bowes, whose stock has been on a steady decline for the last five years, has adjusted to appease shareholders. In 2018, the board of directors and senior management began considering options to return value to shareholders. This has manifested in paying down debt and the sale of non-core assets, including Pitney Bowes' software solutions unit. Pitney Bowes' CEO remarked that the software solutions unit was growing consistently prior to the acquisition by

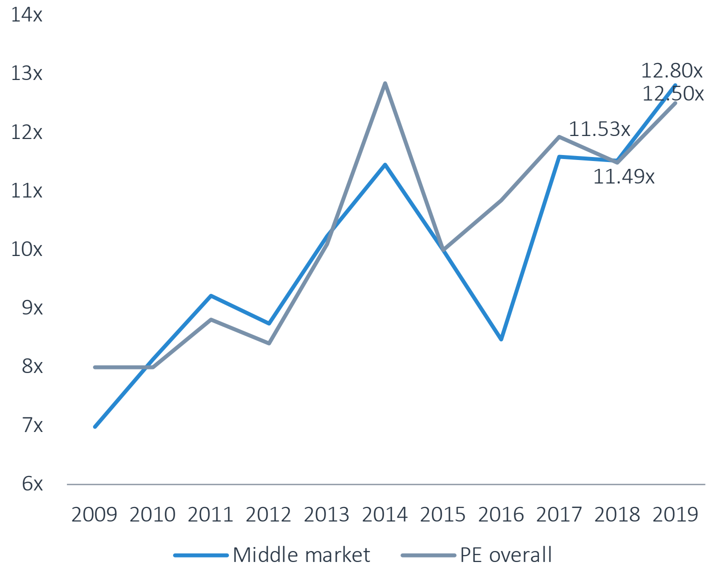
Syncsort. We believe GPs and their underlying portfolio companies will continue to acquire specific high-growth technology companies or assets they believe can weather an economic downturn in the near future.

Another way GPs have approached the technology sector is through add-on deals. In 2019, the sector reached a new high of 20.6% of all add-on deal value, second only to B2B at 32.2% (down from 36.9% in 2018). Add-ons comprised 68.6% of all PE deals in 2019, a 1.9 percentage point increase from 2018. GPs complete these types of deals as add-on's are an integral part of a buy-and-build strategy, which has become a common approach to value creation. Add-ons can also be a useful method for cultivating returns in a high-multiple environment. We expect GPs will continue to use add-on deals to boost returns by blending down acquisition multiples.

On the other hand, GPs employed fewer public-to-private (take-private) MM deals in 2019 as part of a larger downward trend we've seen since the financial crisis. Take-privates have also accounted for a decreasing percentage of total MM deal count over the same time period. We believe this can be partially attributed to the long-running reduction in the number of publicly traded stocks. However, GPs have still been investing in public firms via other methods. As traditional LBO strategies become more crowded, we anticipate increased usage of both growth equity deals and private investment in public equity (PIPE) deals by GPs to find returns from non-controlling investment techniques. Advent's minority investments in apparel manufacturer Lululemon Athletica (NAS: LULU) are a good example of this. Advent initially placed a $195 million growth equity bet on the company along with Highland Capital Partners and BPEA Private Equity. This investment paid off two years later with Lululemon's initial public offering in 2007. However, Advent evidently was not done in their dealings with the athletic apparel manufacturer. Advent completed a $845 million private investment in public equity (PIPE) deal with the entity in 2014. Advent was not alone in their strategy with Lululemon; other investment managers such as Thornburg and FIS Holdings also executed private placements with the retailer in 2015 and 2017, respectively. This investment was a nod to the prospects of the company, as its stock price has more than quadrupled since 2017 lows.

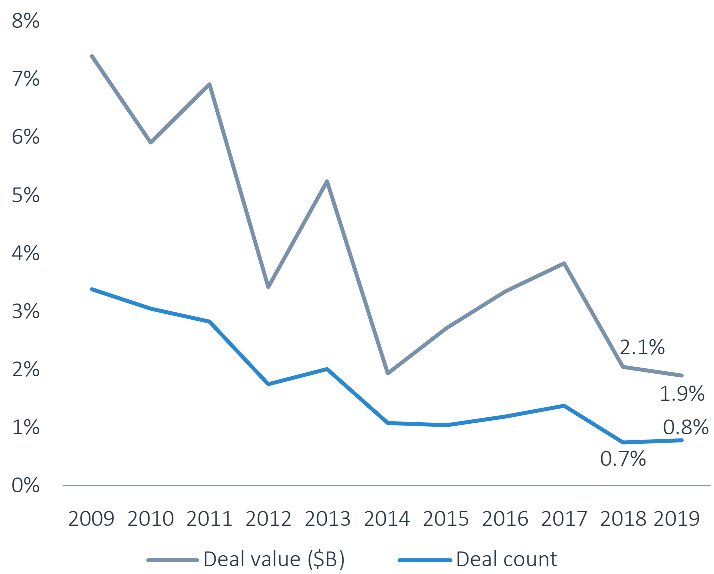
Looking forward to 2020, many GPs are already bracing for an economic downturn, though the MM may provide auspicious investment opportunities for companies in cyclical sectors, such as financial services, real estate and basic materials. It has already been predicted that certain steel companies may see drops in output due to trade

## Median MM PE buyout multiples compared to overall




**Source:** PitchBook | **Geography:** US

## Public-to-private deals as proportion of MM PE deals




**Source:** PitchBook | **Geography:** US

tariffs.[1] Furthermore, the Lincoln Middle Market Index (Lincoln MMI), which tracks changes in enterprise values of MM companies, showed EV growth of only 1.4% in Q3 2019, the slowest growth in two years.[2] Given that downturns tend to create more attractive entry pricing, we may see certain funds, particularly distressed specialists,[3] become more aggressive if valuations dip.

1: "Tools of the Trade War," Key, January 2020.
2: "Lincoln International Reports Slowing Middle Market Growth at 1.4% in Q3 2019, As Bifurcation in Performance Amongst Industries Unfolds," Cision PR Newswire, Lincoln International LLC, December 5, 2019.
3: Note that distressed debt funds are not included in the data in this report. For details, see our H2 2019 Global Private Debt Report.

# Antares: Keynote and Q&A

**Coronavirus: Markets try to catch their breath**

Our 4th Annual Antares Compass Survey of sponsors, borrowers and investors completed in January suggested resilient—albeit slightly diminished—optimism for the US economy heading into 2020, with a recession looking unlikely. However, while the coronavirus (COVID-19) was in the news at the time of the survey, it was largely confined to China's Wuhan region and the stock market was still roaring ahead. Now, as we sit here in early March in the wake of rising death counts, a recent sharp spike in the VIX and drop in the equity markets, and a surprise 50 basis point cut by the Federal Reserve, the needle has no doubt moved sharply on such sentiments.

So now what? Will this prove to be just another "buy the dip" opportunity as central banks come to the rescue? Or is this a global pandemic that will roil markets and economies for many months to come? Or something in between?

On the optimistic side, global health crises over the past few decades such as SARS, Zika, Ebola, MERS and others have not had long-lasting detrimental impacts on markets. As Cliffwater LLC has noted in a recent analysis piece on the topic: "Looking at the 13 past global health crises, in all but one instance equity markets were positive from the three months leading up to the declaration of the global health crisis through the six months after."

However, some (Bill Gates) fear this could be a "once-in-a-century pathogen." Although the coronavirus appears to be much less lethal than, say, SARS back in 2003, it has already spread much more widely. It has also already taken a significant toll on China, which comprises a much bigger share of the global economy and is more integrated into global supply chains than was the case during the SARS epidemic. Fortunately, central banks around the world are on guard to cushion the blow and help in preserving business and consumer confidence (and perhaps helping a bit on the debt servicing cost side too). However, cutting already low rates can only go so far. Rate cuts won't solve supply side/supply chain issues, nor are they likely to sway a consumer's behavior around going to a local restaurant, catching a football game or traveling if they fear getting sick.

**Dave Brackett**

*Chief Executive Officer*
*Antares Capital*

*Dave is a member of Antares' Investment Committee as well as Antares' Board of Directors. Previously, Dave served as president and CEO for GE Antares. He was a founding partner when Antares was formed in 1996. Prior to starting Antares, Dave was a senior executive with Heller Financial.*

**Credit discipline is like good hygiene**

One of the most effective and simple defenses against pestilence is to be disciplined about washing hands thoroughly and frequently. Staying fit and avoiding high-risk travel and close proximity to sick people is also advised.

As a lender, credit discipline is not unlike good hygiene. Not everyone has good habits and takes precautions… but those that do are much less likely to get sick.

**Q&A with Dave Brackett**

**What do you expect the impact of the coronavirus to be on deal activity and related financing options in the year ahead?**

It's obviously a fluid and volatile situation. Heading into 2020, there was optimism that M&A activity might rise as indicated in our Compass Survey in January; however, as we sit here in early March, the prospects look more uncertain. Our pipeline had been building nicely through February, but it's unclear if that trend will continue if refinancing activity dries up in the wake of rising virus spreads. M&A activity, which has been pretty tepid to begin with, may slow further from new platform LBOs, though opportunistic add-on activity will likely continue.[4]

Looking forward, on the syndicated side, the latest feedback from our capital markets team suggests that while retail loan mutual fund outflows have soared of late, many long-term institutional investors view the current market as an opportunity, albeit with selective bias toward higher-quality credits.

4: Refinitiv LPC reported a 2% drop in syndicated sponsored M&A volume as of March 4, 2020 against relatively weak year-ago comparisons.

On the direct lending side, we had already seen a surge in unitranche volume, which rose to 23% of total US sponsored middle-market volume in 2019 versus 14% in 2017-2018, according to Refinitiv LPC. While some of these gains have likely been secular, some are likely cyclical following the stock market swoon seen in late 2018. Unitranche may continue to make inroads in 2020 following the latest surge in market volatility as speed and surety of execution become increasingly critical attributes compared to other considerations. We at Antares pride ourselves in offering our sponsors best-in-class execution across all options, be it syndicated, club or unitranche. However, lenders need be particularly diligent and selective in view of unitranche's higher attachment points. We have already seen a rise in non-accrual activity among the BDCs in Q4 2019.

**How is your portfolio of PE backed borrowers performing? Do you expect much impact on the credit side in terms of portfolio performance?**

Our portfolio continues to perform well with default rates low and specific loan losses low/below our forecast in 2019; however, we have seen a pickup in our early warning watchlist. Our analysis suggests most of the migration of names to our watchlist over the past year reflects challenges our borrowers flagged in our Compass survey. About half of the migration drivers relate to revenue shortfalls and half correspond to rising labor and raw material costs. Interestingly, only a very low percentage of our watchlist migration appears to be explicitly tied to EBITDA add-back misses.

On the coronavirus front, the impact on our portfolio is still to be determined, and we are monitoring the situation closely. About 15% of our portfolio names appear to have exposure to China-dependent supply chains, with a few names in the travel or transportation areas. Very little of our portfolio has direct sales to China. On the supply chain side, many companies have built up inventory ahead of the Chinese New Year (providing near-term cushion) and/or have alternative supply options. Ironically, some of these supply chain alternatives were developed in reaction to trade war-related tariffs—the impact of which we were already monitoring closely. In the case of tariffs, the credit concern had been mostly around the ability to pass along the tariff costs (that other competitors often faced). However, in the case of the effects of the coronavirus, the main risk relates more to an outright curtailment of supply that if prolonged could be more material and cause lost revenue. Of course, the broader potential impact of the coronavirus's spread on confidence, hiring, economic growth and more remains unknown. While rough waters may lie ahead, we expect sponsors will support their investments as needed given good prospects for an eventual v-shaped recovery as medical/containment solutions take hold. In the meantime, our highly senior-focused portfolio remains well-diversified with low concentrations across companies, industries and hold sizes.

**There have been some press articles and opinion pieces of late warning that private debt markets are looking bubbly. Do you view private debt as still an attractive asset class given recent developments?**

We believe there is good, sound reason for the strong secular growth we've seen and expect to continue to see for private debt as an asset class. However, that's not to say the credit cycle is dead. Various metrics are looking stretched late in cycle, and it's no time to be complacent as a lender. Understanding a borrower's cash flows and enterprise value through the cycle is critical. While being senior in the capital structure is a source of comfort, not all senior is created equal. A first lien loan at 4x to 5x is not the same as a 7x unitranche with questionable EBITDA add-backs. Chasing yield and/or deploying dry powder under pressure can lead to bad credit decisions.

Managing risk well requires selectivity, credit discipline, dedicated workout capabilities, portfolio diversification and deep experience and relationships working with our sponsors through multiple cycles. While we believe private debt will prove itself to be an attractive asset class through the cycle, performance may vary significantly among lenders.

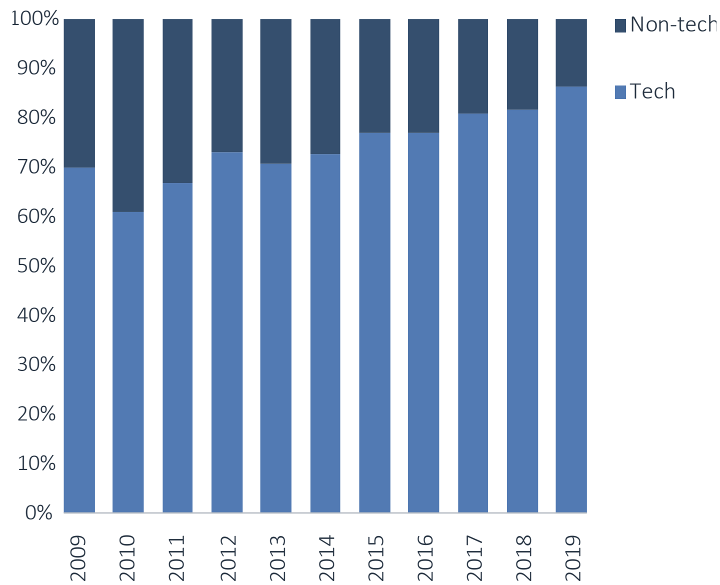
# Spotlight: VC-to-PE buyouts

The proliferation of PE buyouts of VC-backed companies (referred to here as VC-to-PE buyouts) stems from PE firms seeking earlier exposure to tech companies that are often staying private for longer. While PE firms may not be specifically pursuing investment in VC-backed companies, the growing overlap between buyout barons and tech entrepreneurs appears here to stay. VC-to-PE buyouts not only account for a rising percentage of PE deals, but also of VC exits. Between 2000 and 2019, the number of VC-to-PE buyouts has grown at a CAGR of 18.1%, compared to overall buyouts at 9.5%. During that time, PE buyouts went from accounting for 2.4% of VC exits to 19.2%. While a variety of different types of companies can be (and have been) VC-backed, the bulk (86.3%) are tech companies.

An overabundance of capital in private markets and low interest rates have allowed private companies to readily access funding and borrow at historically low rates. This has led to a new crop of VC-backed acquisition targets that are more mature—in terms of revenues, headcount and valuations—than in past decades. Indeed, the median VC-backed company acquired in a buyout is about a decade old, compared to around seven and a half years old pre-financial crisis. Therefore, while it was previously more common for PE firms to source technology investments from public markets, they can now go straight to the source. Most VC-backed companies skip the public offering altogether. VC-to-PE buyouts comprise over 4% of all buyouts, whereas PE take-privates (formerly VC-backed and otherwise) account for 0.97%, a reversal from the past. We expect to see a continuation of this trend going forward.

GPs can also quickly drive top-line growth by integrating addon companies and cross-selling and/or boosting the company's offerings. Often, PE firms will streamline operations and properly incentivize sales teams. While this is a key part of the broader PE playbook, PE firms can more swiftly make changes with tech companies due to the unique scalability of software. While some methods of value creation are industry-agnostic, there are some levers PE firms frequently pull that are specific to software. Experienced PE investors in software often improve operations through cloud/SaaS integration, sales and pricing initiatives, sophisticated software engineering

## Proportion of VC-to-PE buyouts in the tech sector




**Source:** PitchBook | **Geography:** US

and productization.[5] Top-line growth is of paramount importance because markets generally value software companies on revenue multiples.

Myriad factors underlie the VC-to-PE buyout trend. An influx of capital has pushed prices higher in PE's traditional, lower-growth industries, making outperformance more difficult in the process. This has lured many GPs into the tech space, where the (often organic) high growth and promise of outsized returns can offset generally elevated buyout valuations. In this typically low-growth environment, investors are willing to pay up for tech companies with these types of robust return profiles.

Compared to corporate ownership, selling to PE has certain advantages. Although PE firms are often the highest bidder—the primary consideration for most VCs—selling to a financial sponsor may be a more attractive exit route even if the headline acquisition price is not the highest. PE firms can appeal to founders and management with a "best of both worlds" solution: partial liquidity while maintaining some upside.

5: "Cracking the Code in Private Equity Software Deals," BCG, Michael Brigl, et. al., May 16, 2017

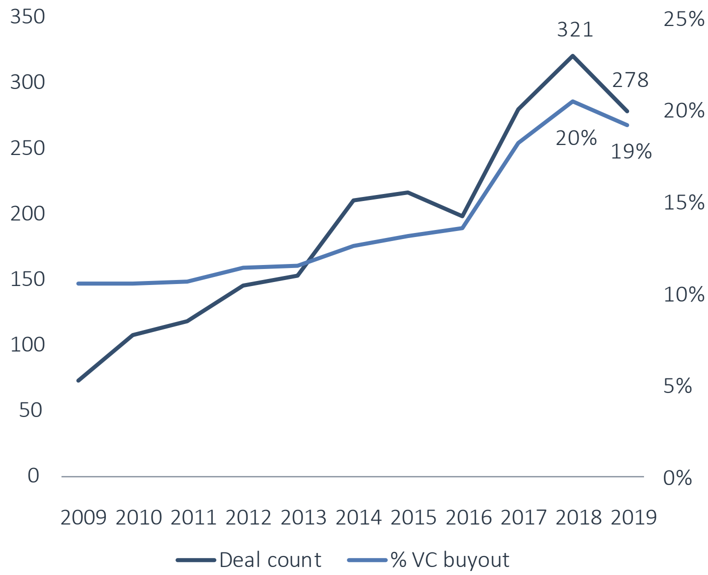
Spotlight: VC-to-PE buyouts

In the pursuit of quickly growing VC-backed companies, PE firms have developed several key advantages to outbid strategic acquirers and appear more attractive than an IPO. Today, every serious PE firm has developed an operations shop (op-shop) focused on boosting top-line growth. This contrasts with prior PE strategies that relied more heavily on cost cutting and financial engineering. The most prominent tech-focused buyout firms, Vista Equity Partners, Thoma Bravo and Silver Lake Partners, all have in-house operations teams that explicitly focus on building technology companies. Vista takes this a step further; executives across their portfolio companies will meet regularly in order to trade tips on strategy and share best practices, allowing them to reap the rewards from economies of scale. To be a serious competitor in the space, sector specific op-shops are a requirement.

VC-backed companies are highly sought after because of their potential for growth. To PE firms, buyouts of VC-backed companies represent a way to maintain mid-double-digit returns, while for VC-backed companies and founders, they can be a lucrative exit option with additional upside potential. We expect these deals to continue proliferating as tech-focused PE funds multiply and spend down dry powder. Further, many later-stage VC funds will seek nontraditional liquidity options amid public market pushback on unicorn valuations.

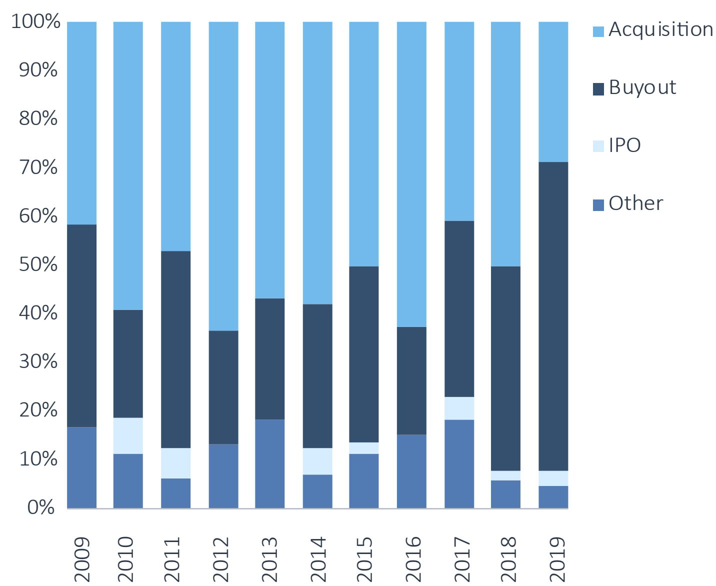
*This section appeared originally in the Q1 2020 PItchBook Analyst Note: VC-to-PE Buyouts: Adapting the PE Playbook, written by PE Analyst Stephen-George Davis on February 20, 2020.*

## Buyouts (#) as a proportion of all VC exits




**Source:** PitchBook | **Geography:** US

## PE exits (#) of formerly VC-backed companies by type




**Source:** PitchBook | **Geography:** US


ACG has the top global network for middle-market businesses, hands down.
SEE THE POWER THAT MEMBERSHIP BRINGS.
JOIN TODAY
THE POWER OF
ACG®
Association for Corporate Growth
© 2020 Association for Corporate Growth. All Rights Reserved.

# ACG Q&A: The private equity opportunity in cannabis

Entourage Effect Capital is a private equity firm focused on the cannabis industry. Founded in 2014, the firm has deployed close to $150 million in over 40 companies out of its two dedicated funds and coinvestment vehicles. Based in Fort Lauderdale, FL, EEC invests across the value chain, including distressed opportunities. Managing Director Codie Sanchez will speak on April 21 for a virtual panel "How To Capitalize On The Budding Cannabis Industry" that was originally scheduled at InterGrowth, which was canceled due to COVID-19.

**Codie Sanchez**

*Managing Director, Entourage Effect Capital*

*Sanchez previously lead First Trust's Latin America Investment business and held positions at Goldman Sachs, State Street and Vanguard. Sanchez's columns on investing, cannabis and startups have appeared Forbes, Fast Company, Entrepreneur, and People en Español.*

**What makes a cannabis business an attractive investment target for Entourage Effect Capital?**

We've evolved along with the cannabis industry as it has become a more developed market, although it's still far from maturation. We invest across the value chain, and these days we look to invest in companies in the growth equity phase, typically with $10 million to $75 million in revenue. In the current environment, we're searching for turnaround or distressed opportunities, and investments where we can set beneficial terms because of the current liquidity crunch in cannabis.

**How has your investing strategy changed over the years?**

When we first started investing in 2014, we invested in cultivators, multistate operators and some real estate. Those all made sense early on. Our second fund had a much different profile, with almost no cultivation whatsoever. There were more retail brands and still some multistate operators, but we looked for companies with a path to profitability or with plenty of cash on their balance sheets. Our second fund also included biotechnology, technology and ancillary services businesses, in tandem with strong operators who are in execution and moving to the profitability phase.

Today, we're focused on intelligent retail and companies we think are going to circle the market on retail, especially those with the ability to handle delivery. We're concentrated on brands with a unique path to distribution. We're increasingly looking at emerging technologies such as biosynthesis, which could upset the industry. Recently, we invested in a company that focuses on consumer behavior data and analytics within the cannabis industry. We announced our third fund in October with a target of $150 million, which will focus heavily on distressed opportunities.

**How have you seen the competitive landscape for cannabis deals evolve?**

The number of PE firms in the industry has certainly increased. In 2014, there were only two or three PE investors in the space, but today, there are seven to 12 real funds that have significant assets behind them. Still, that's not enough to support the liquidity needs of the industry overall. For investors that have the capital, the cannabis industry provides a unique opportunity because it's capital starved.

Most traditional PE firms investing in other industries will tell you that good deals are currently hard to find, and valuations are too high. Cannabis is completely different. There has been an 80% decline in public market stocks, which has trickled down to private companies. The industry's biggest issue is that it needs to raise more capital, because there are many deals to be had. Companies cannot use leverage, loans or revolving lines of credit. They've had to rely on equity, which is expensive for companies but good for investors.

**How has capital been allocated within the cannabis industry?**

There has been a massive diffusion of capital. I've never seen this before in my career. Everyone is putting cannabis companies in one basket instead of differentiating who will be the real winners and losers.

ACG Q&A

This diffusion means investors are not allocating capital to create kings of each sector. Take California for example, which has a $3 billion cannabis market. We bought a company that is the number one distributor of pre-rolled joints and one of the top edible distributors in the state. In any other market, you'd probably expect that company to have annual revenue around $75 million to $100 million, but the cannabis industry is different. This company is doing $12 million of revenue. It just reflects that every category of cannabis consists of a slew of small providers. We aim to change that by creating an ecosystem of investors and companies that can be kingmakers.

The companies that are going to succeed in this space are the ones that are big enough for large consumer packaged goods, pharma, tobacco or alcohol companies to come in and buy them. Right now, a large entrant to the space would say: "This company has $10 million in revenue? I'm going to build that myself. Why would I buy that at a high multiple?" That's the difference in this space.

**Are PE funds starting to show an interest in cannabis now that many states have legalized medicinal or recreational use?**

We've certainly seen some firms come into ancillary services or hemp and CBD-based brands, now that those are federally legal, but most are still waiting on the sidelines to buy individual companies and do what we're doing. Many can't get over vice clause issues within their own funds, or prohibitions in their bylaws that don't allow them to invest in cannabis as a fund.

Where we have seen PE investors get involved is as LPs in funds like ours, using our fund investments as their learning curve. Partners do it to learn quickly, and I anticipate that learning curve will ramp up and they will start investing directly in companies going forward.

**What's your outlook for federal legalization?**

It's the million-dollar question, right? As an investor, I want prohibition to stay around for a while because once legalization happens, it removes the moat around these business—companies that are capital starved and don't have access to public markets aren't attractive to a KKR or Blackstone. All of that changes the second the plant gets legalized. That's when we'll have a massive uptick in prices and multiple expansion.

We're probably three to four years out from broad cannabis legalization. I don't anticipate it becoming federally legal this year—in part because of the presidential election—but the following year could be interesting.

I'm in favor of legalization for decriminalization and access for consumers who want to buy cannabis. However, for investors, it's okay if we have a few more years of federal prohibition, because it gives companies longer to incubate before large conglomerates come in to buy them and compete.

This window that we're in right now is not going to last forever. Our ability to set terms and do turnarounds and distressed deals will eventually be eclipsed when these companies have differentiated funding sources. That is why the limited capital that exists today, along with incredibly depreciated valuations, mean the time is right to jump on the cannabis PE opportunity.

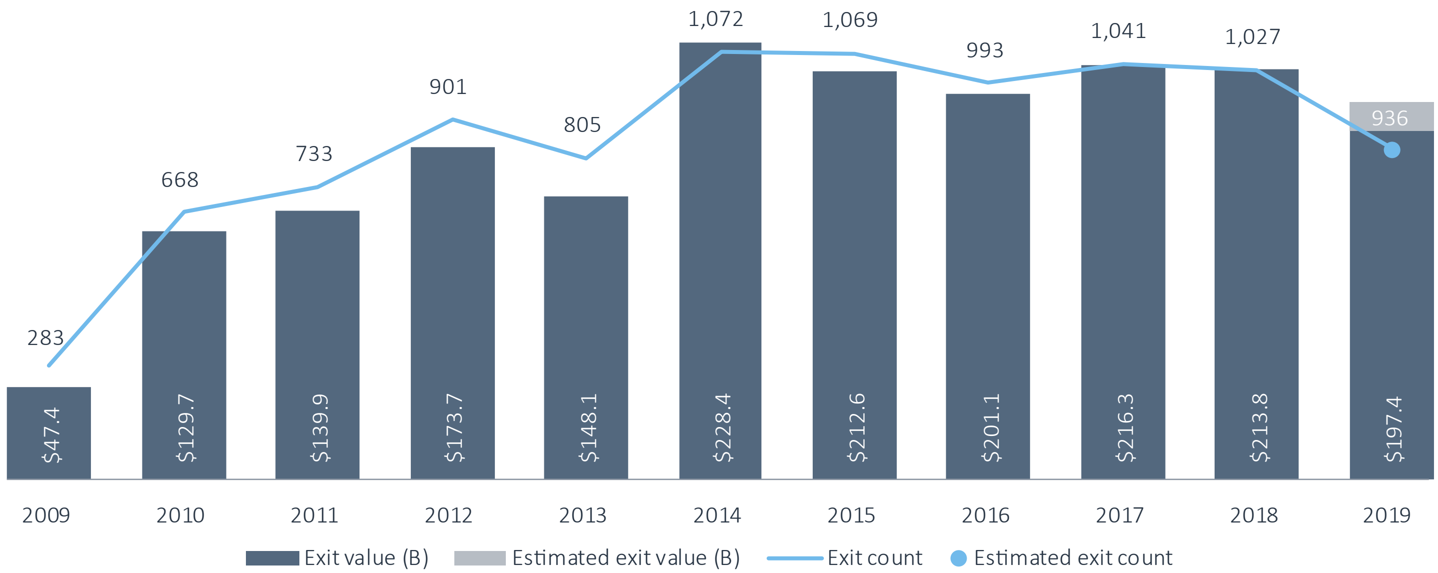
**Are there other legal or regulatory issues you're watching?**

From a regulatory standpoint, we could see the SAFE Banking Act passed. I'm not sure that will happen this year—next year is more likely.

This year, I think it's possible that California gets more reasonable with its cannabis taxation and regulation policies. The legal cannabis market in California is $3 billion; the black market is worth $9 billion. If California lawmakers decrease its regulations, the market could easily quadruple within several years. California represents 10% of the global cannabis market, yet its onerous taxes result in some companies being effectively taxed at a rate of 75%-80%. These companies have double- or triple-digit growth levels, even as they compete with the black market.

# Exits

## MM PE exit activity

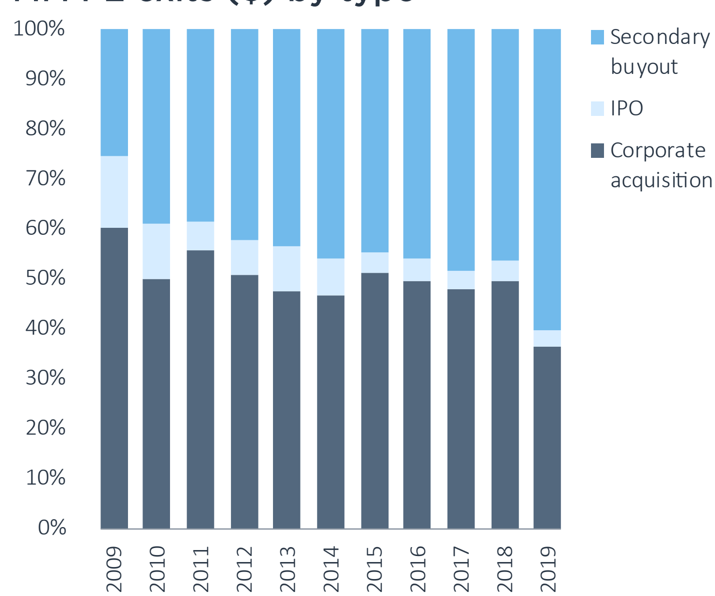



**Source:** PitchBook | **Geography:** US

As MM dealmaking expanded, exit count and value contracted in 2019. MM PE firms exited 936 companies for a combined value of $197.4 billion, YoY declines of 8.8% and 7.7%, respectively. While these numbers represent six-year lows for exit value and count, exit activity fell just short of the 1,000 deals and $200 billion mark that has been the norm since 2014. We believe an increase in add-on deals contributed to this downward trend. MM companies are frequently bought then combined into a larger entity, leading to a divergence in number of companies bought compared to exited. An example of this is the exit of Anvil International by One Equity Partners. Anvil added on 5 companies to itself between the time they were purchased by One Equity and the 2019 exit. The year began slowly due to the government shutdown, which led to several firms pushing back their IPOs to Q2 and Q3. Further, WeWork's failed IPO plans, which began in August of Q3, led to a level of skepticism of private market valuations from public market investors and subsequently a poor showing in Q4 2019 for IPO activity. With that said, there were still several notable exits in 2019.

One prominent exit, which we touched on in the Q3 2019 edition of this report, was cybersecurity company Ping Identity's IPO. While Vista Equity Partners generally prefers sales to corporates or financial sponsors, in October 2019, Vista took Ping Identity public at $1.2 billion after not receiving satisfactory

## MM PE exits ($) by type

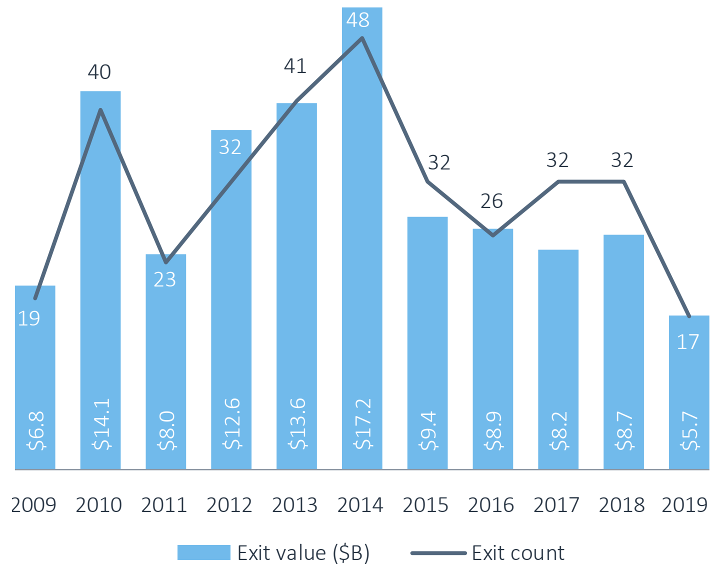



**Source:** PitchBook | **Geography:** US

bids from financial sponsors and strategics. By the end of December, Ping had a market cap of $1.9 billion, nearly matching the valuation Vista was pursuing for the company. This exit is a good example of GPs using public markets to make bets on promising portfolio companies, especially when they feel they are not receiving high enough bids from the private markets. Furthermore, GPs make an implicit bet on any portfolio company taken public given lock-up periods. Ping was a bright spot for the dismal PE-backed IPO market in 2019.

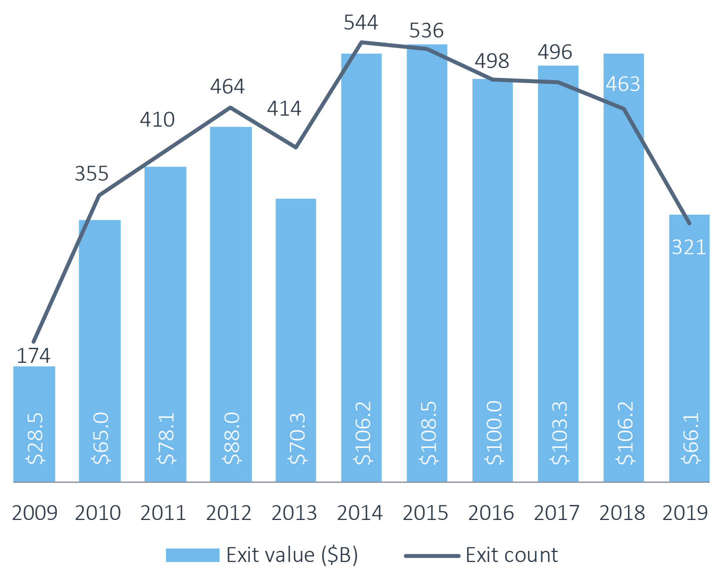
MM SBOs had a fair showing in 2019, with gains of 11.0% YoY. These increases were partially due to PE firms often being the highest bidders for MM companies. One of the largest exits was the $930 million SBO of SaaS company Global Tranz by the Jordan Company to Providence Equity Partners. Interestingly, the Jordan Company initially bought Global Tranz in a $400 million LBO from a consortium which included Providence Equity Partners. The increase in SBOs has been able to temper the decline in corporate acquisitions. Corporate acquisition exit value has not surpassed its 2015 highs, though 2019's YoY drop of 37.7% was one of the largest on record. We believe part of the reason for the dearth of corporate acquisitions can be attributed to a decline in CEO confidence, which dropped to a decade low in 2019 and led to risk averse CEO's refraining from engaging in M&A.[6] We find this interesting given the fact that shareholders have been rewarding corporations for M&A activity.[7] While it seems as though corporations across the board have largely gotten cold feet in terms of completing transactions—at least those sourced from PE portfolios—MM PE firms seem to be moving in the opposite direction.

## MM PE IPO activity




**Source:** PitchBook | **Geography:** US

## MM PE corporate acquisition activity

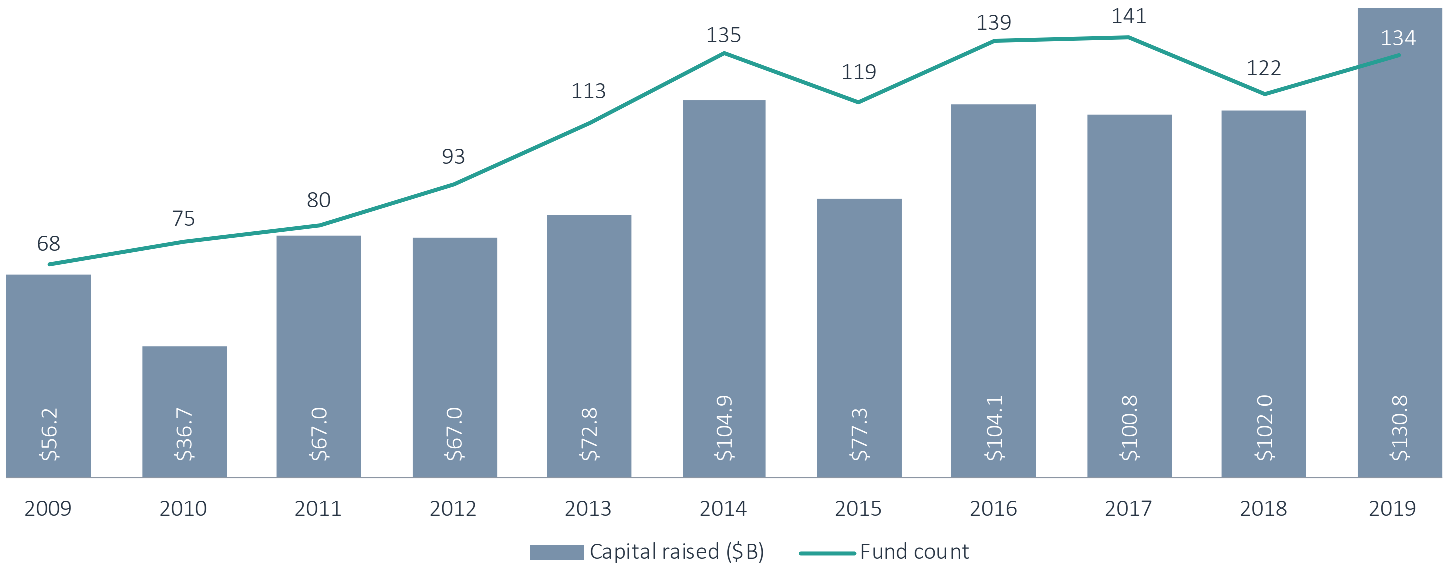



**Source:** PitchBook | **Geography:** US

6: The Conference Board Measure of CEO Confidence, January 7, 2020.
7: "Forget Buybacks and Dividends. Investors Just Want Corporate M&A," Barron's, Alexandra Scaggs, October 18, 2019.

# Fundraising

## MM PE fundraising activity

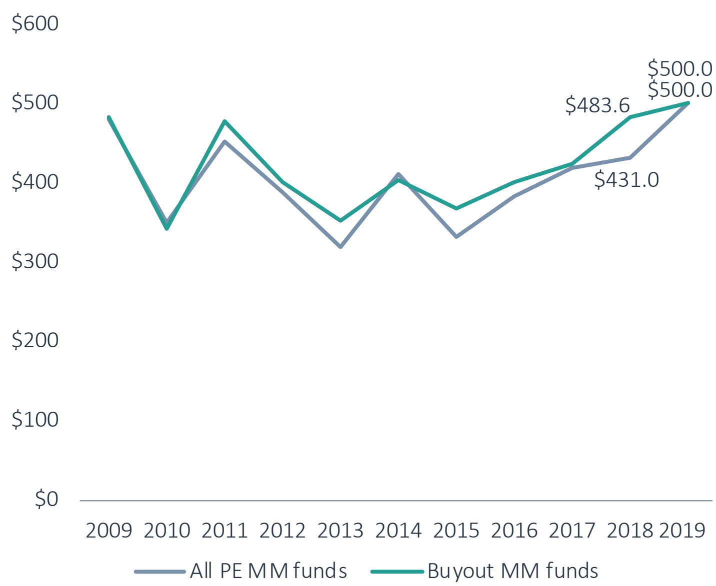



**Source:** PitchBook | **Geography:** US

MM fundraising reached new highs in 2019 as total capital raised eclipsed past years. In total, $130.8 billion was raised over 134 funds—YoY increases of 28.3% and 9.8%, respectively. Furthermore, the median fund size for both mezzanine funds and buyout funds has touched $500 million, another record. Despite these gains, MM fundraising as a percentage of total PE fundraising decreased by ten percentage points YoY to 47.3%. We view this decrease not as a sign of weakness in the MM, but as a testament to the proliferation of PE mega-funds ($5 billion+). In order to satiate client demand, we have noticed that some GPs are raising MM funds and flagship mega-funds. Some GPs are even closing their MM offerings in tandem with their flagship funds. A few of these dual-raised funds even have the same close dates. One example of this is Leonard Green, which closed a $12.0 billion buyout fund from their flagship fund family on the same date they closed a $2.75 billion MM buyout fund.

In addition to these dual-raised funds, GPs are diversifying in other ways to meet client demands for additional product offerings. Many GPs are also raising funds with longer holding times. For example, CVC Capital Partners, The Carlyle Group and others have raised long-dated funds, with expected fund lives of at least 15 years. GPs are raising these funds for the flexibility in timing entrance and exit of investments and to allow investments to mature. Many companies require more than the typical three to five years to realize their full value creation plan, meaning solid

## MM PE median fund size ($M)



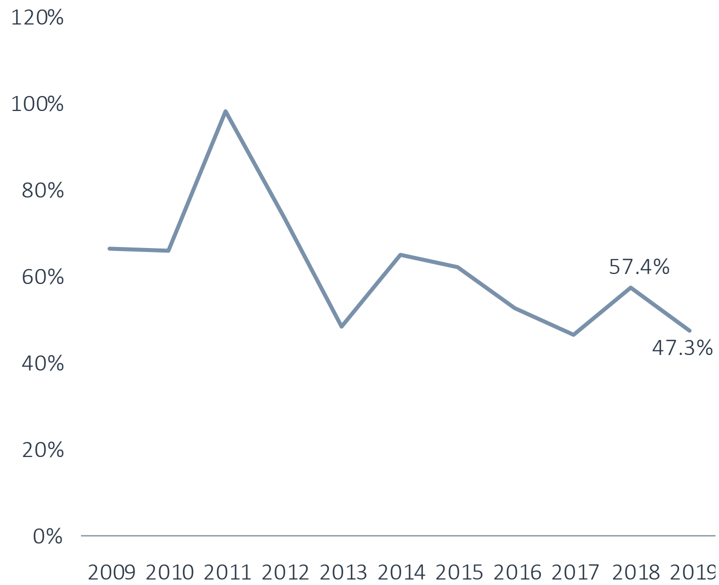

**Source:** PitchBook | **Geography:** US

investments sometimes don't fit neatly into the 10-year fund life. This is a major reason for the proliferation of GP-led secondaries. The low-growth environment has led to GPs "holding onto their winners" in an effort to get the most value out of certain portfolio companies. PE shops have also expanded into different sectors. For instance, we have seen healthcare funds raised by prominent GPs, such as KKR's strategic growth fund, Bain Capital's Life Sciences fund and Blackstone's recent acquisition of biotech specialist Clarus.

While PE shops are moving into different sectors to meet client demand, they are also moving into public markets for the same reason. For instance, Bain is currently looking to raise up to $7 billion for a new equities fund—the top end of which would push them out of the MM—whereas Advent has had a long only shop in Sunley House. Not only are PE managers diving into the public domain, but hedge funds that typically play there are jumping into the private sphere. Two Sigma, the world's largest quant hedge fund, raised $1.2 billion for a PE division, Sightway Capital. Sightway reached the final close of its inaugural fund, Sightway Capital I, in November. Two Sigma is not alone by any means. Paul Singer of Elliot Management has had a PE arm for a while and this outfit even bought out Barnes & Noble last summer. Going forward, we expect more public-private overlaps to occur, as both PE shops and hedge funds expand to curry favor from clients across the board.

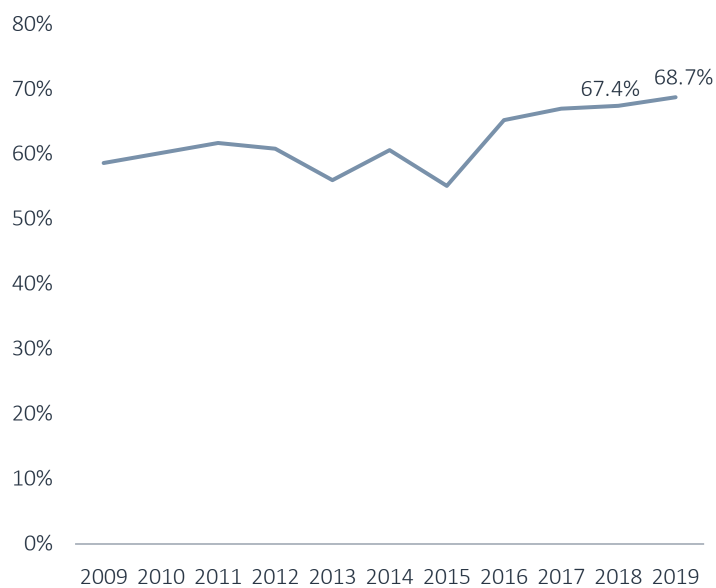
Pivoting to LPs, we also anticipate continued private market allocation from large university endowments such as Harvard and Yale, the latter of which created the endowment investing model under the stewardship of David Swensen. While Yale was instrumental in adding illiquid private market investments to the endowment playbook in the 1980s, universities have not stopped allocating. In fact, last October, Harvard Management CEO NP "Narv" Narvekar wrote that [the fund's] "allocation to buyouts, growth and venture capital continues to be low relative to what likely makes sense for Harvard." Given that Harvard already has around two-thirds of their portfolio invested in alternatives, we believe we will continue to see a concerted effort from the university, and many large endowments alike, to allocate more toward private market investments.

## MM PE funds ($) as proportion of all PE funds




**Source:** PitchBook | **Geography:** US

## MM PE funds (#) as proportion of all PE funds




**Source:** PitchBook | **Geography:** US

PitchBook

# 2019 US PE MM lending league tables

## Overall

| | | |
|---|---|---|
| 1 | Antares Capital | 166 |
| 2 | Ares | 105 |
| 3 | Churchill | 83 |
| 4 | Barings | 79 |
| 5 | Crescent Capital Group | 77 |
| 6 | The Carlyle Group | 62 |
| 7 | BMO Financial Group | 59 |
| 7 | Madison Capital Funding | 59 |
| 9 | NXT Capital | 58 |
| 10 | PNC | 56 |
| 11 | MidCap Financial | 55 |
| 11 | Twin Brook Capital Partners | 55 |
| 13 | Golub Capital | 52 |
| 14 | The Goldman Sachs Group | 50 |
| 15 | Bank of Ireland | 45 |
| 16 | Citizens Bank | 44 |
| 17 | Varagon Capital Partners | 42 |
| 18 | Monroe Capital | 37 |
| 19 | Capital One | 34 |
| 20 | Audax Group | 33 |
| 21 | SunTrust Banks | 31 |
| 22 | Jefferies Group | 29 |
| 23 | Credit Suisse | 25 |
| 23 | Bain Capital | 25 |

Source: PitchBook

## Select roles*

| | | |
|---|---|---|
| 1 | Antares Capital | 137 |
| 2 | Ares | 57 |
| 3 | Crescent Capital Group | 52 |
| 3 | Twin Brook Capital Partners | 52 |
| 5 | Madison Capital Funding | 44 |
| 6 | Churchill | 43 |
| 7 | MidCap Financial | 39 |
| 8 | Citizens Bank | 35 |
| 9 | Varagon Capital Partners | 30 |
| 9 | NXT Capital | 30 |
| 11 | BMO Financial Group | 27 |
| 12 | The Carlyle Group | 26 |
| 13 | Golub Capital | 25 |
| 14 | Barings | 24 |
| 15 | Capital One | 23 |
| 16 | Bank of Ireland | 20 |
| 17 | Jefferies Group | 19 |
| 18 | Bank of America | 17 |
| 18 | Fifth Third Bank | 17 |
| 18 | Monroe Capital | 17 |
| 21 | SunTrust Banks | 16 |
| 22 | Owl Rock Capital Corporation | 15 |
| 22 | PNC | 15 |
| 22 | The Goldman Sachs Group | 15 |

Source: PitchBook. *Select roles are comprised of bookrunners, lead arrangers, mandated lead arrangers and administrative agents only.