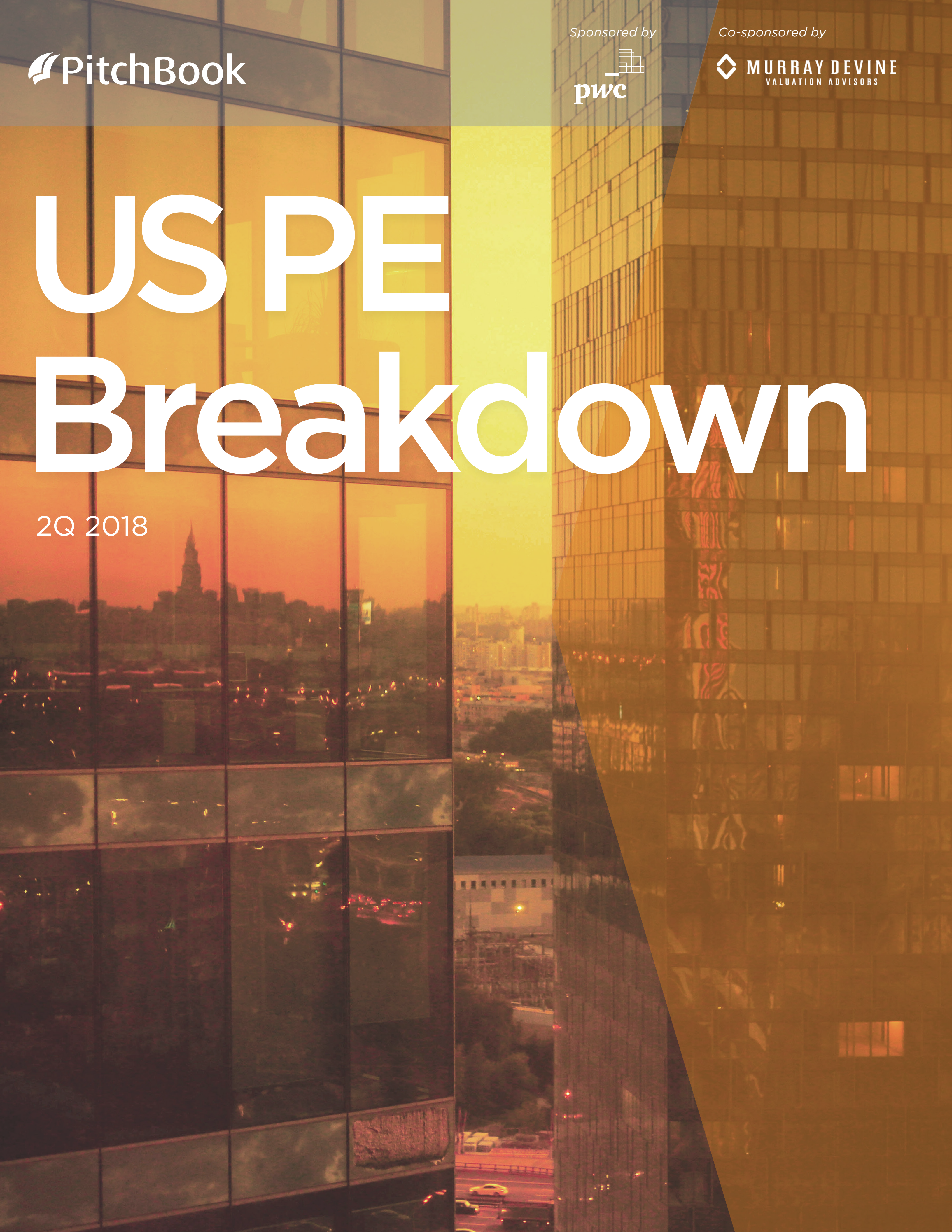


PitchBook

Sponsored by

pwc

Co-sponsored by

MURRAY DEVINE
VALUATION ADVISORS

US PE Breakdown

2Q 2018

The fuel to maximize opportunity

At PwC, we provide deep industry knowledge, seamless engagement service delivery and a unique perspective so you can move at the pace of opportunity. Our seasoned professionals provide integrated solutions to help position you for growth at every stage of the private equity lifecycle, from deal strategy through value capture.

For more information or to sign up to receive the latest news from our PE practice, go to pwc.com/privateequity

Sponsored by pwc

Co-sponsored by MURRAY DEVINE VALUATION ADVISORS

PitchBook

Contents

Credits & Contact

PitchBook Data, Inc.

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

Content

Dylan Cox Senior Analyst, PE
Wylie Fernyhough Analyst, PE
Darren Klees Data Analyst

Contact PitchBook

Research
reports@pitchbook.com

Editorial
editorial@pitchbook.com

Sales
sales@pitchbook.com

Cover design by Caroline Suttie

Click here for PitchBook's report methodologies.

Key takeaways from the analysts

The first half of 2018 proved to be a hotbed for PE activity; 2,247 deals were completed totaling $263.9 billion in value—representing a 2% increase in volume and a 6% decrease in value compared to the first half of 2017. Activity continues to be driven by easy access to credit and sustained strength in fundraising that has resulted in a buildup of dry powder.

The proportion of PE targets that were publicly traded at the time of acquisition has been cut in half, from a recent high of 2.9% in 2011 to just 1.4% through the first half of 2018. Concurrently, PE firms are now more likely to source deals from companies with VC backing (3.7% of deals in 1H 2018), coinciding with PE's growing interest in software businesses.

PE fundraising in the first half of 2018 is off to a slow start in comparison to the prolific numbers achieved in 2017, though still strong by historic standards. A combined 51 funds raised $32.5 billion in 2Q.

$263.9B
total over 2,247 deals in 2Q 2018

1.4%
the proportion of PE targets that are publicly traded

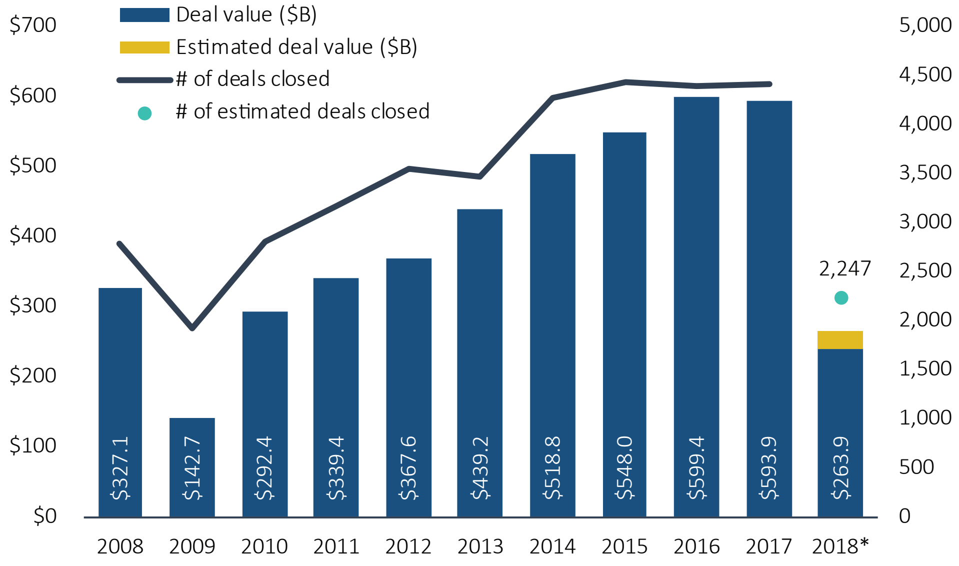
$32.5B
total raised over 51 funds in 2Q 2018

Overview

The first half of 2018 proved to be a hotbed for PE activity; 2,247 deals were completed totaling $263.9 billion in value—representing a 2% increase in volume and a 6% decrease in value compared to the first half of 2017. Activity continues to be driven by easy access to credit and sustained strength in fundraising that has resulted in a buildup of dry powder. Notable deals that were announced or closed this quarter include Silver Lake's $3.5 billion take-private of Blackhawk Network Holdings and KKR's $8.3 billion secondary buyout (SBO) of BMC Software from Bain and Golden Gate Capital, both of which represent PE's growing interest in IT. We expect deal flow to be continually strong in the second half of 2018, due primarily to the aforementioned dry powder and easy access to debt financing.

Deal flow on pace for another strong year

US PE deal flow



Source: PitchBook
*As of June 30, 2018

PitchBook

Sponsored by pwc

Co-sponsored by MURRAY DEVINE VALUATION ADVISORS

OVERVIEW

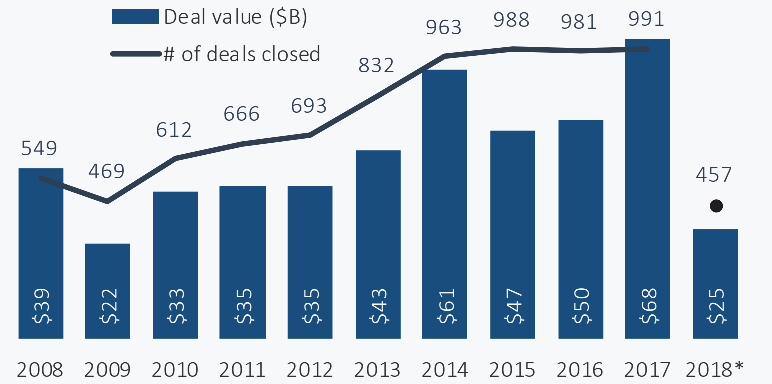
Typically viewed as a hybrid approach between buyouts and VC, growth equity is an often-overlooked portion of the PE market. Through the first half of the year, growth equity transactions accounted for 23% of all PE deals, on pace with its 10-year trailing average of 22%. Non-tech companies in the expansion phase are often those that need growth capital most. For example, emergent consumer brands MOD Pizza and Chobani raised growth equity rounds in 1H 2018.

As the rate of PE deals has increased in recent years, the deal sizes have also tended to be much larger. The median deal size increased to $197.1 million in 1H 2018, representing a 31% increase over 2017's full-year figure. However, we expect the most recent figure to be revised downward since small deal values generally take longer to collect; nonetheless, the trend is clear. Higher purchase-price multiples are one factor driving deal sizes above historic norms. Another catalyst is the sizable step-up in fund sizes, which have required managers to pursue larger deals to deploy capital efficiently. As a result, deals under $25 million accounted for just 40% of deal flow in the first half of 2018—the lowest figure since 2007.

As deal sizes have been shifting, so has the composition of PE target companies. The proportion of PE targets that were publicly traded at the time of acquisition has been cut in half, from a recent high of 2.9% in 2011 to just 1.4% through the first half of 2018. Concurrently, PE firms are now more likely to source deals from companies with VC backing (3.7% of deals in 1H 2018), coinciding with PE's growing interest in software businesses.

Growth equity has seen substantial growth in the last decade

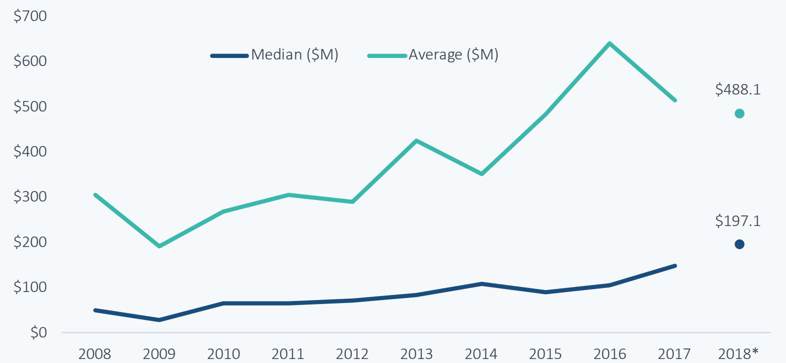
PE growth deal flow



Source: PitchBook
*As of June 30, 2018

Buyout sizes continue to balloon

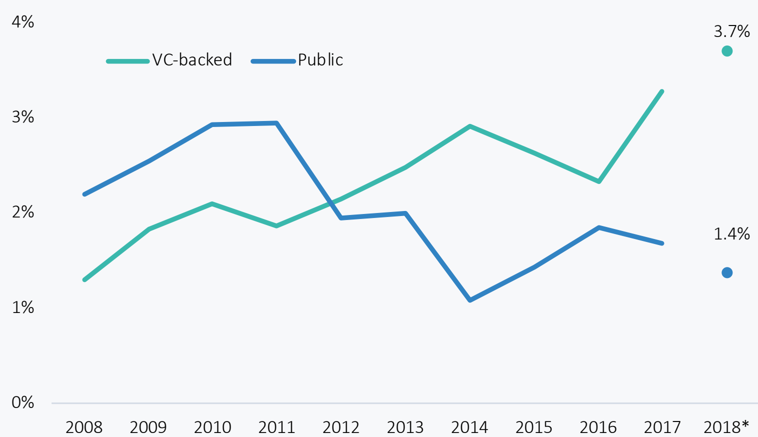
Median and average buyout size by year



Source: PitchBook
*As of June 30, 2018

PE more likely to source from VC than public markets

Proportion of PE deal count by target backing status

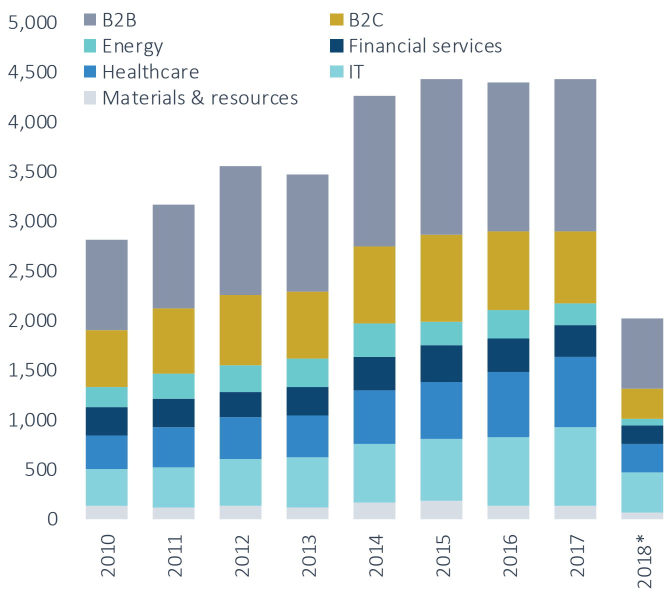


Source: PitchBook
*As of June 30, 2018

Deals by sector & size

Dealmaking picks up in IT and financial services

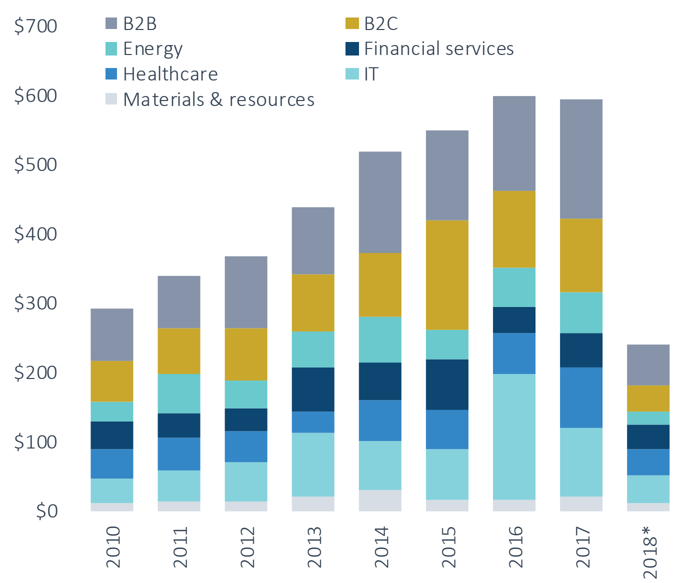
US PE activity (#) by sector



Source: PitchBook
*As of June 30, 2018

Deal value nearly on pace with prior year

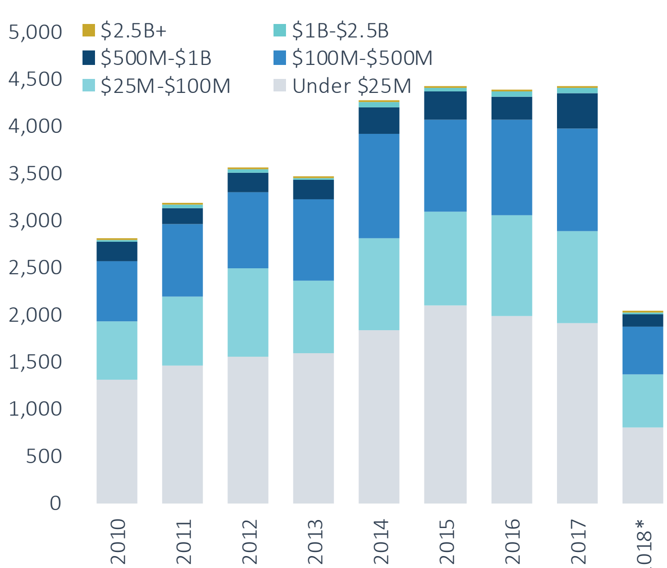
US PE activity ($B) by sector



Source: PitchBook
*As of June 30, 2018

Despite announcements, few mega-deals closing in 2018

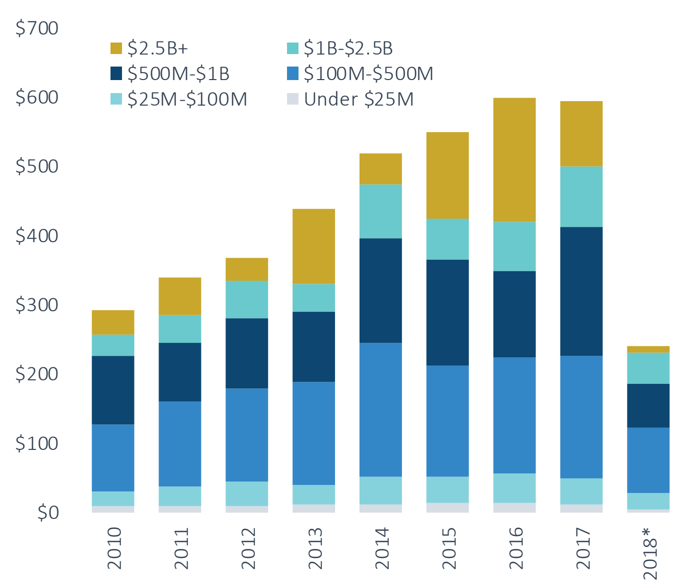
US PE activity (#) by size



Source: PitchBook
*As of June 30, 2018

Dearth of mega-deals weighs on capital invested

US PE activity ($B) by size



Source: PitchBook
*As of June 30, 2018

Q&A: Andrew Cristinzio & Dean Bekas

Perspectives on the PE market and middle market companies

Andrew R. Cristinzio

US Private Equity Leader

Andrew is PwC's US Private Equity leader. In his role, he oversees the national practice, delivering PE clients a single point of access to assist them at every level of their business: managing funds, portfolio company performance, and transaction diligence.

With more than 15 years of experience working with PE clients, Andrew has led multinational teams in the evaluation of transactions in North America, South America, Europe and Asia. His industry expertise includes: aerospace and defense, retail and consumer products, telecom and media, industrial products, and technology. Andrew received an M.S. in the Management of Technology from the University of Pennsylvania, an M.B.A. from Drexel University, and a B.S. in Business Administration from Millersville University. He is a Chartered Financial Analyst and Certified Public Accountant.

Dean C. Bekas

Partner, Private Company Services

Dean Bekas has served domestic and global clients working in multiple sectors and has deep expertise in advising clients on equity and debt financings, mergers and acquisitions and complex transactions. He has extensive experience serving both family held businesses and portfolio companies of private equity sponsors and has collaborated with numerous of their advisors when solving business issues.

He is a graduate of Indiana University, is a member of the American Institute of Certified Public Accountants (AICPA) and Illinois CPA Society.

What is your take on the US private equity (PE) dealmaking landscape as we head into the back half of 2018?

Andrew Cristinzio, PwC's US PE Leader, and Dean Bekas, PwC Partner, Private Company Services, acknowledged this is one of the best fundraising environments in history. Mega, top-tier and middle-market firms with strong track records continue to raise funds with favorable terms, due in part to large increased interest by LPs in PE. For the largest funds, there is a mounting interest in investing across borders to focus on more sizable and complex opportunities, particularly by those funds that have the capacity, global expertise and resources to do this effectively. On the other hand, best-in-class funds that don't have the same global reach are implementing a thematic strategy and/or sector focus to try and stand out in the current competitive landscape. All these factors are helping to contribute to deal volume, attracting new entrants and non-traditional investors. Dean agreed with Andrew and added that these new entrants and non-traditional PE investors—including high-net-worth individuals, family offices, and others—are active in the lower middle market. There has been a lot of added focus on the middle market given it is a source for add-on opportunities, which allow valuation optionality due to potential cost-savings. Further, high valuations have placed added focus on the necessity to have a value creation framework during the evaluation phase that can be fully vetted during due diligence and form the basis for the underlying investment thesis. In addition to the operational levers that can be utilized to drive value, Dean suggested there has been a significant increase in the number of buyouts in the mid-cap private company space. These types of companies are attractive candidates for the inorganic growth levers within the value creation framework.

What primary drivers do you see emerging from this current environment that will shape the back half of 2018 specifically? Do you see the prior trends shifting or accelerating?

With so much capital to deploy, Andrew noted, PE firms are paying close heed to their deal sourcing strategies as they look to innovate in order to thrive in the current environment. Take the lower middle market for example; many US-based entities are looking to expand overseas, so for those PE firms targeting such companies, demonstrating operational expertise and standing leveraging relationships is critical. PE firms continue to opt for add-ons—which often can be completed for a more attractive entry price—that they can acquire quickly to drive operational improvements and expand operational footprints of their current portfolio companies. For example, suppliers typically need to demonstrate capabilities across more than one geographic location to effectively serve their customers, and thus will look for targets to maintain and grow those capabilities.

Depending on the situation, Dean stated, funds can also offer different forms of liquidity to owners of small to medium-sized enterprises. Some owners may not wish to sell right away, but rather obtain some infusion of liquidity and still remain involved with their businesses to some extent.

Are there additional methods of value creation for PE firms to adopt in the current landscape, especially given how pricey transaction multiples can be nowadays?

Coming out of the financial crisis, many PE firms were unprepared to retool or reimagine their portfolio companies, as few had experienced such a shift in the business cycle. Now, however, that has entirely changed. The firms that will be able to successfully harvest current investments in the future tend to compose a valuation creation thesis at the outset of deal sourcing that remains executable through the changes in the current environment. In the course of PwC's PE practice now, Andrew said, we spend a significant amount of time helping our PE clients design valuation theses. There is little reliance on multiple expansion in the market now; value creation will be key.

What types of competitive edges are PE firms looking for in deal sourcing and the landscape as a whole? What types of transactions are they looking to engage in more frequently, given the current environment?

Andrew contended that PE firms will increasingly look to invest in corporate carveouts. The environment is favorable for divestitures, especially given the AT&T-Time Warner ruling, which could be seminal for mega-deals and, in turn, accelerate the carveout trend. Proactive corporate governance will lead managers to analyze their portfolios streamline operations, potentially resulting in preemptive shedding of assets. On the other hand, if anti-trust concerns emerge, there will be involuntary shedding of assets during mega-mergers.

Andrew also observed an uptick in traditional buyout shops entering the minority stake, growth investing space. Some financial sponsors are increasingly looking for portfolio exposure in areas of fast growth, while some owners of software and technology companies are looking to take on a value-add financial partner and obtain capital to ramp up growth even further.

Are there other factors you see impacting PE or affecting even longer-term outlooks?

Data privacy and protection will continue to be a primary concern for PE sponsors and their portfolio companies, Andrew noted. Such concerns are an accelerating global corporate phenomenon. On the macroeconomic side, more generally, activity looks set to be robust over the next 18 to 24 months. However, as there is a greater chance of a recession in the next 36 months, the investment cycle could eventually slacken in tandem with any economic slowdown, albeit on a lagging basis. That said, PE investors could also benefit from a deflation in valuations across financial markets. Management teams analyze their models in order to see how they may need to adapt. In addition, businesses are analyzing their overall supply chains and relationships with their customers in light of those changes.

We would be amiss if we did not mention tax reform as another factor that will impact PE. Tax reform will no doubt have a substantial impact on PE funds and their portfolio companies. Market participants will have to continually evaluate the tradeoff between the benefit of a reduced corporate and individual rate and increased limitations on the ability to claim certain deductions like interest.

About PwC

At PwC, our purpose is to build trust in society and solve important problems. We're a network of firms in 158 countries with more than 236,000 people who are committed to delivering quality in assurance, advisory and tax services.

PwC private equity professionals help minimize risk and fuel opportunity at every level - from management and operations, to portfolio and fund strategy, and throughout the deal lifecycle. With an unrelenting focus on value creation, our teams bring together unparalleled experience and cross-functional integration to tackle every new challenge.

Accelerate your business and connect with us on LinkedIn, Twitter, pwc.com/privateequity, Facebook, Instagram or YouTube.

Spotlight: Long-dated funds

The lifespan of PE funds is often perceived to be between eight and 10 years but, in reality, most funds take much longer to wind down. On average, it takes between 11 and 14 years for funds to reach a residual value to paid-in (RVPI) of less than .05x. Despite this reality, most limited partnership (LP) agreements reflect the traditional eight to 10 year timeline, which has led to fund extensions—typically in one-year increments upon LP approval—becoming the norm. For example, our data shows that 53% of 2004-vintage buyout funds are still active.[1]

Some PE firms have begun to adjust their fund offerings to meet the reality of longer timelines. Industry giants CVC Capital Partners, Blackstone and The Carlyle Group have all recently completed fundraising for vehicles with stated durations of at least 15 years. Vista Equity Partners is reportedly targeting $3 billion for an evergreen vehicle of its own, while BlackRock is said to be targeting at least $10 billion for a similar fund.

Long-dated funds afford managers flexibility in timing the entrance and exit of investments, as well as greater latitude to enact long-term operational improvements. From the LP perspective, long-dated funds generally have lower management fees, less reinvestment risk and fewer taxable events; the tradeoff, however, is greater illiquidity and key-person risk.

Select long-dated funds

Currently fundraising or officially announced by fund manager (including vehicles that have held final close)

Fund name	Status	Vintage	Fund size
Blackstone Core Equity Partners	Open	N/A	$5.0 billion (target)
CVC Strategic Opportunities II	Upcoming	N/A	$4.7 billion (target)
CVC Strategic Opportunities I	Closed	2016	$4.4 billion
Carlyle Global Partners	Closed	2016	$3.6 billion
Apollo Hybrid Value Fund	Open	N/A	$3.0 billion (target)
Core Equity Holdings I	Closed	2017	$1.3 billion
Cove Hill Partners Fund I	Closed	2017	$1.0 billion
Altas Partners Holdings	Closed	2016	$1.0 billion

Source: PitchBook
*As of June 30, 2018

Critics will argue the recent expansion of fund offerings, including long-dated ones, is simply a way for managers to increase assets under management (AUM) and lock in long-term fee income without offering real differentiation or superior returns. But proponents maintain that the broad range of hold periods, fee structures and strategies (including PE, debt, real estate, hedge funds, etc.) allows LPs to choose a fund—or terms within that fund—that meet their individual preferences.

In a recent deal, Carlyle transferred its stakes in asset manager TCW Group from its financial services and flagship buyout funds to its long-dated vehicle. Similar deals are likely to continue occurring but will invite investor scrutiny due to their intra-firm nature. For more on long-dated funds, see our recent analyst note on the subject.

1: “Active” is defined as having an RVPI of greater than 0.05x, and “vintage” is defined as the year in which the fund held its final close.

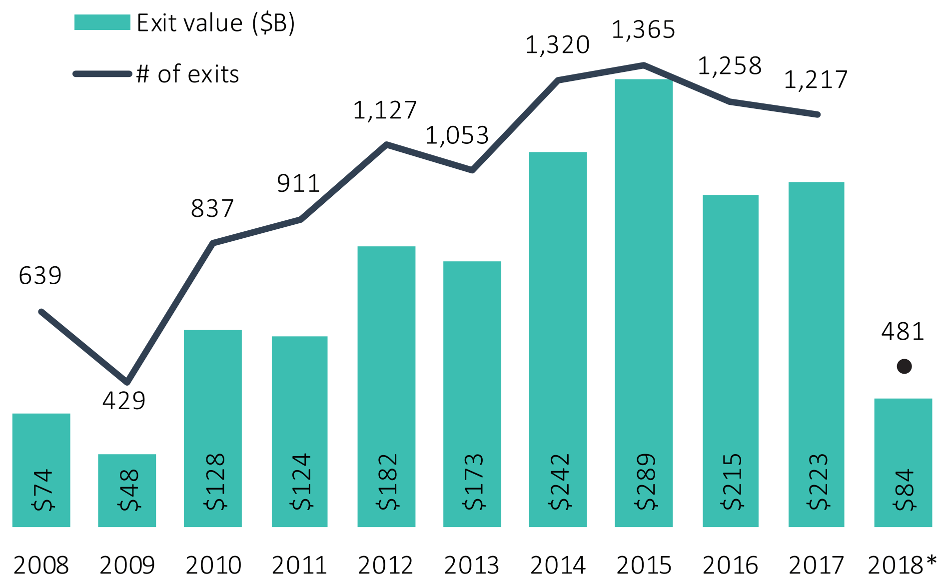
Exits

Through the first half of 2018, the number of PE exits is on pace to fall for the third straight year. Total capital exited has come in lower as well, though it experienced less of a decrease due to larger exit sizes. US CEOs' US economic outlook remains at near-record levels,[2] while credit is still cheap and competition remains stiff, pushing median transaction values to new heights. In fact, through the first half of the year, the median PE exit value reached $231 million, a 15.5% increase over the prior year.

As exit sizes have trended higher, PE firms have been active buyers. On the exit front, this has translated to record levels of portfolio companies exiting through a secondary buyout (SBO) to another PE firm. This appetite for SBOs has been whetted by strong fundraising, especially by funds raising over $1 billion, which has pushed PE firms to seek out larger deals to put dry powder to work. Deals like the $2.4 billion SBO of Hearthside Food Solutions by Charlesbank Capital Partners and Partners Group have become staples in today's exit landscape as PE firms refine their operational skillset, lending credence to their value propositions even when sourcing from another fund's portfolio. To note, the first six months of 2018 have seen SBOs account for over half of all exits, the highest figure on record.

Exit activity slows through the first half of 2018

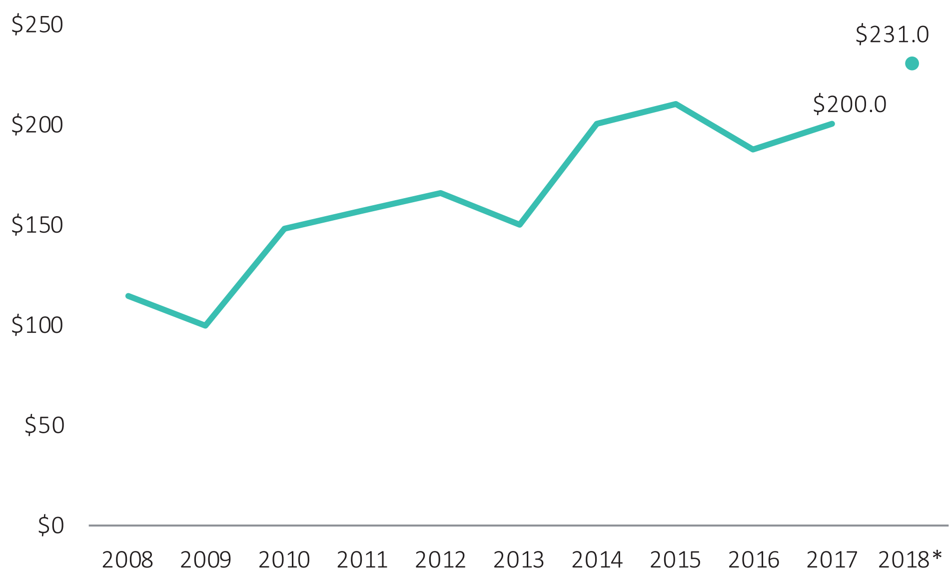
US PE-backed exits



Source: PitchBook
*As of June 30, 2018

Despite lower volume, another all-time high for exit sizes

Median US PE-backed exit size ($M)



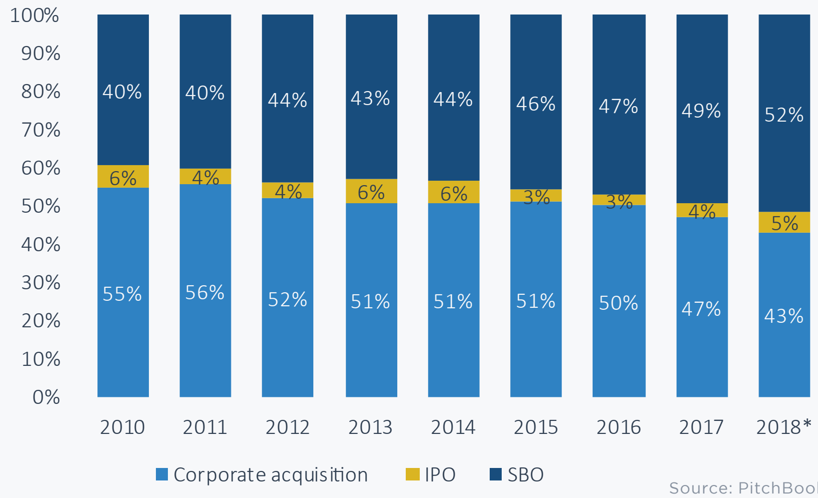
Source: PitchBook
*As of June 30, 2018

2: "Business Roundtable CEO Economic Outlook Index Eases, Remains Near Historic High," Business Roundtable, 2018

The longer-term growth of SBOs as a proportion of exits has been accompanied by a gradual uptick in IPOs as a proportion of exits over the past few years. This activity has come at the expense of corporate acquisitions, whose proportion of exits has fallen or stayed even in every year since 2011. Corporate acquirers, with strong profits and a windfall from recent US tax legislation, have been active in the M&A space; however, their acquisitions have been unable to keep up with the appetite of PE firms buying via SBO. We think corporations will continue to be active buyers of PE-backed companies, and with increased activity from SBOs and IPOs, PE firms currently have attractive exit options across the board.

SBOs account for over 50% of exits through the first half of 2018, the highest rate on record

US PE-backed exits (#) by type



Source: PitchBook
*As of June 30, 2018
Note: Some years may not add up to 100% due to rounding.

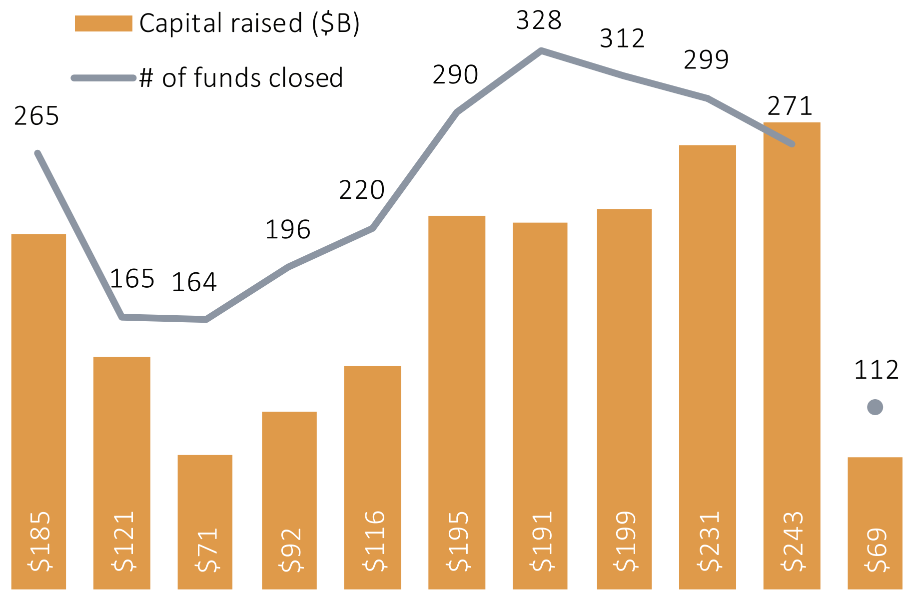
Fundraising

PE fundraising in the first half of 2018 is off to a slow start in comparison to the prolific numbers achieved in 2017, though still strong by historical standards. A combined 51 funds raised $32.5 billion in 2Q. While fundraising by $5 billion+ mega-funds has slowed year-to-date, funds between $1 billion and $5 billion have accounted for 56% of capital raised, more than any full year since 2011.

Billion-plus-dollar funds continue to take in most of the total capital raised as LPs continue to consolidate general partner (GP) relationships, making fewer but larger bets on managers. Additionally, LPs of all types continue to increase their target PE allocations with the assumption that PE will continue to deliver its historic outperformance against other asset

Fundraising activity slows with fewer funds in the market

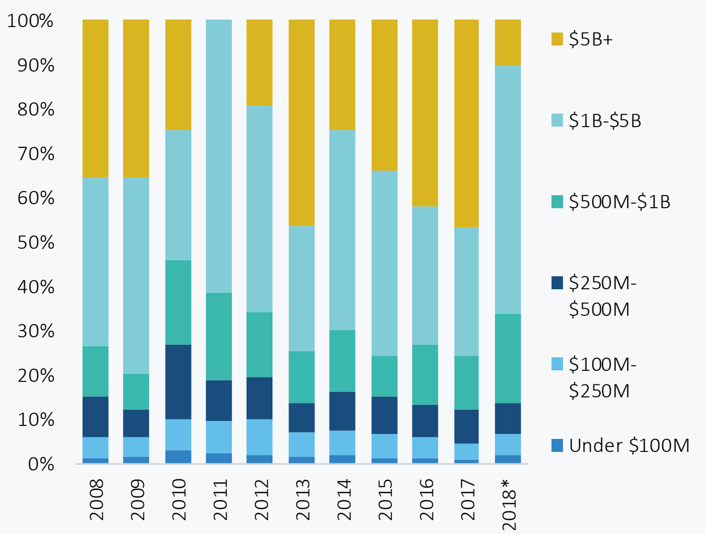
US PE fundraising



Source: PitchBook
*As of June 30, 2018

Mega-funds see a pullback through 2Q

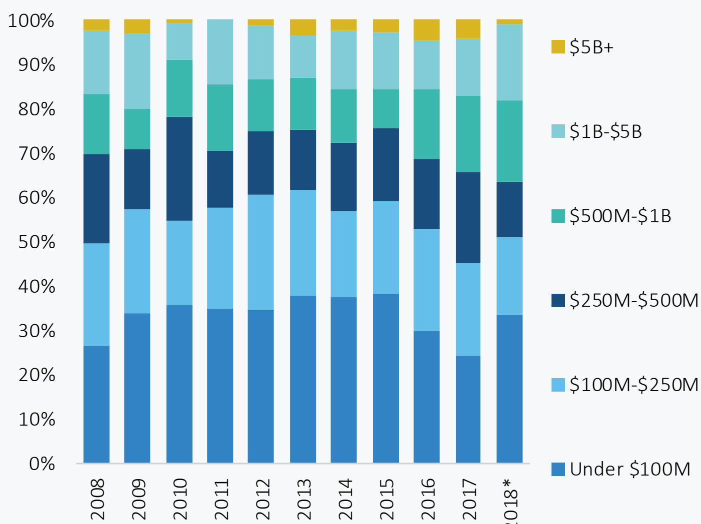
US PE fundraising ($) by size



Source: PitchBook
*As of June 30, 2018

Small funds show relatively strong activity

US PE fundraising (#) by size



Source: PitchBook
*As of June 30, 2018

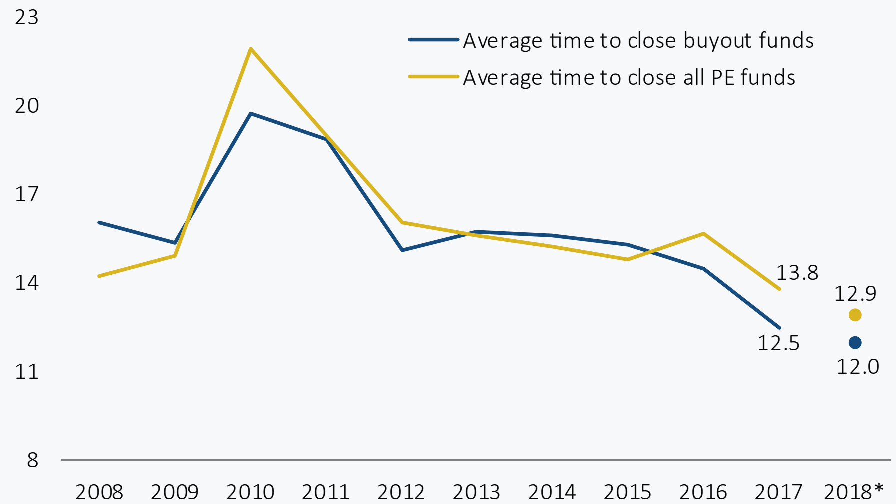
classes. In a recent investment committee meeting, Ted Eliopoulos, CalPERS's outgoing CIO, said that PE is the only asset class expected to outperform CalPERS's blended 7% expected rate of return over the next 10 years.[3]

In an attempt to reduce fees and bring more responsibility in-house, many of the larger institutional investors have been increasing their direct and co-investment allocation. In this light, co-investments fundraising is at some of its strongest levels to date, accounting for 5% of capital raised. As large and sophisticated LPs continue increasing allocations to co-investments, we expect other LPs to follow behind, but the additional resources and expertise required for co-investing can be a challenge for many smaller investors. Importantly, co-investment rights are frequently negotiated outside the typical fund structure, so there is even more capital earmarked for the strategy than fundraising numbers suggest.

As competition among LPs has heated up to get access to the top-performing funds, GPs have been closing funds at the quickest pace in a decade. While the fundraising timelines for all PE funds have been decreasing since 2010, the average time to final close was just over 12 months through the first six months of 2018. One reason GPs are taking less time to close funds is that there are fewer vehicles in the market while LPs are committing capital at near-record levels and continue to increase their target allocations.

Average PE funds holding final closes in record time

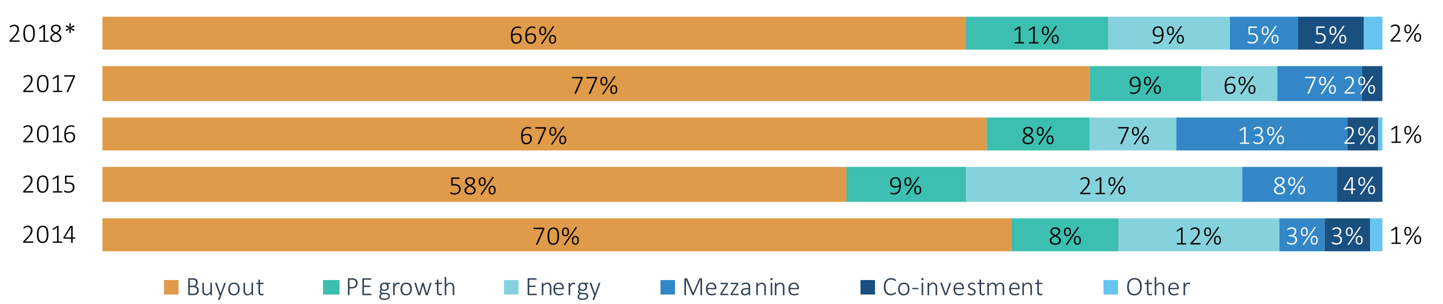
US PE fundraising time to close (months)



Source: PitchBook
*As of June 30, 2018

Co-investment funds gain share

US PE fundraising ($) by type



Source: PitchBook
*As of June 30, 2018

3: "CalPERS gears up for private equity portfolio changes," Pensions & Investments, Arleen Jacobius, June 19, 2018