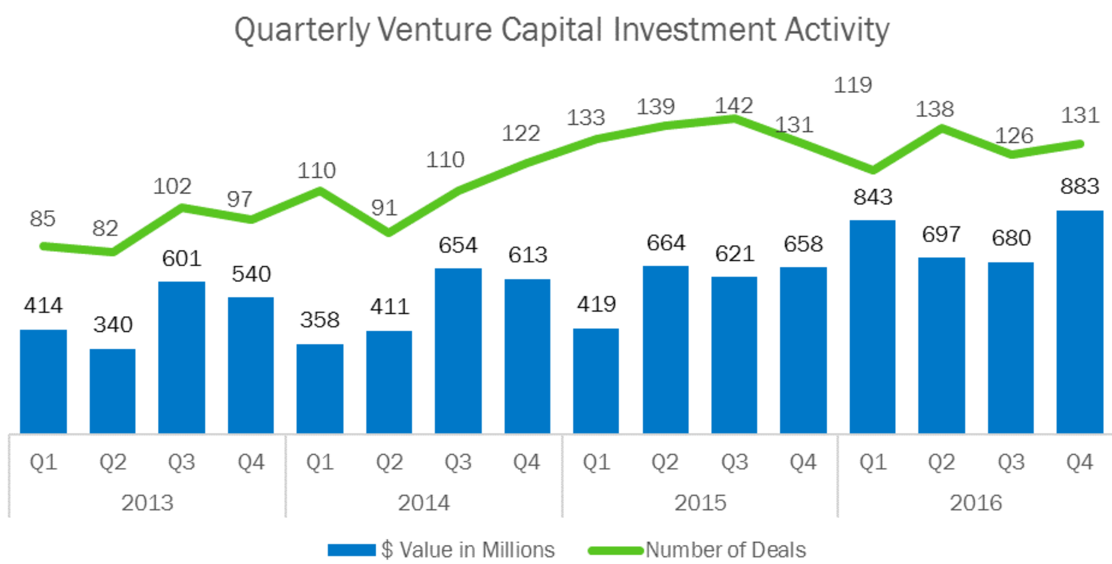
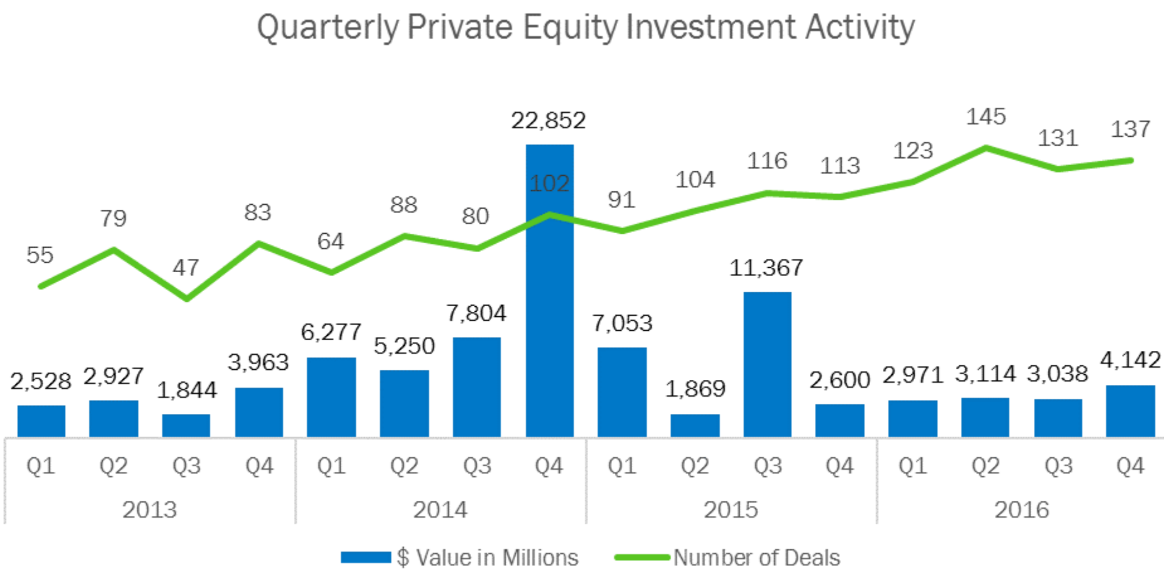
Valitas Insights: The Middle Market – The Deal Engine for Canadian Private Equity in 2016

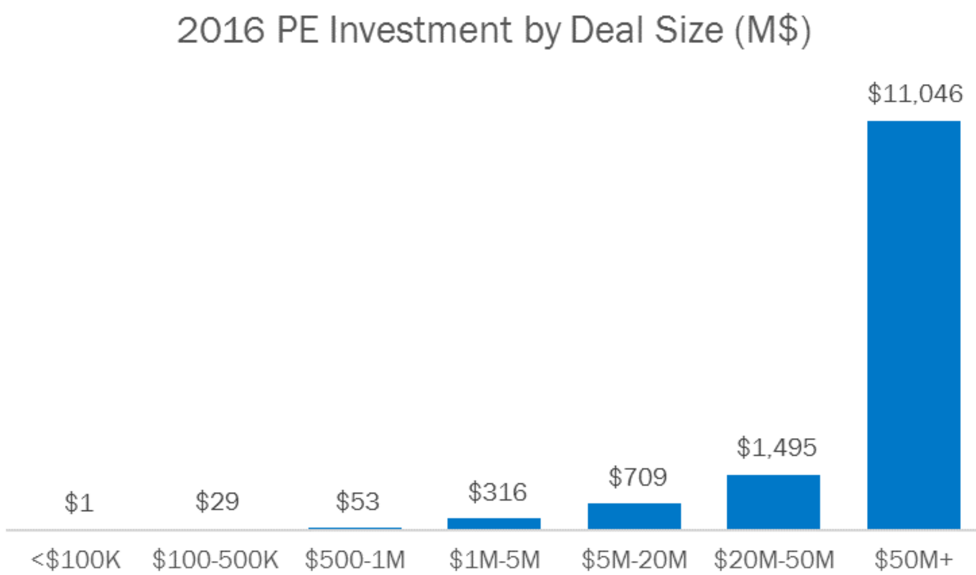
The past year ended on an interesting note for Canadian Private Equity (PE). When we last reported on Canadian VC and PE activity (Q3, 2016), there was a divergence in trends: VC surged ahead, while PE deal value plummeted. But the recently released Canadian Venture Capital and Private Equity Association's 2016 VC & PE Year in Review paints a different PE picture.

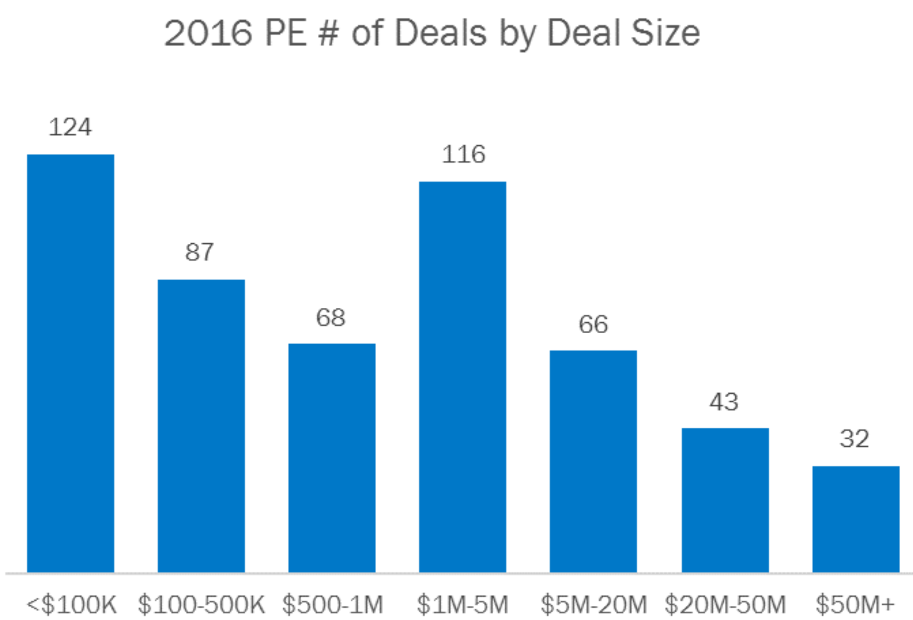
VC activity sustained its positive momentum in Q4, driving Canadian investment to $3.2 billion for 2016, a 41% increase over 2015. PE activity, on the other hand, experienced a dramatic shift in direction, recovering from its previous nosedive and rebounding for a nice Q4 recovery. Private equity investment was $4.1 billion across 137 deals in Q4, an increase of 36% over the $3 billion invested in Q3.





For the full year, total PE investment was $13.7 billion, a decline of 40% from 2015. Deal volume increased, however, with 536 deals completed versus 424 deals in 2015. The smaller average deal size is, of course, reflective of a decline in oil and gas sector activity with its associated mega deals; investment in oil and gas companies was $4.4 billion in 2016, a 49% year over year decrease. Cleantech and Information and Communications Technologies (ICT) were the sector beneficiaries of this decline, with investment increases of 200% and 352% respectively. In addition, investors are looking to mid-market companies in a range of sectors to pick up the slack. Investment in mid-market ($20-50M) deals increased to $1.5 billion in 2016, reflecting a 41% increase over 2015.





"[Private Equity] activity continues to climb in mid-market deals..." Mike Woollatt, CEO, CVCA

We've written previously about current challenges for PE investors, including rising valuations and a shrinking pool of quality investments. The Canadian environment reflects the broader North American trend in this regard, as strategic buyers continue to compete with PE investors for acquisitions. In this context, the middle market offers lower valuations relative to its large company peers, providing a more attractive value proposition for PE investors, particularly in the case of add-on acquisitions. And with increased investment promoting a healthy Canadian middle market across multiple sectors, there is the added benefit of building a healthy buffer to the ups and downs of oil prices.