

Valitas Insights: Platform or Add-on: How is US buyout activity shaping up for 2016?

What trends are surfacing in an environment characterized by lofty valuations, slow organic earnings growth and ample corporate cash balances and investor “dry powder”?

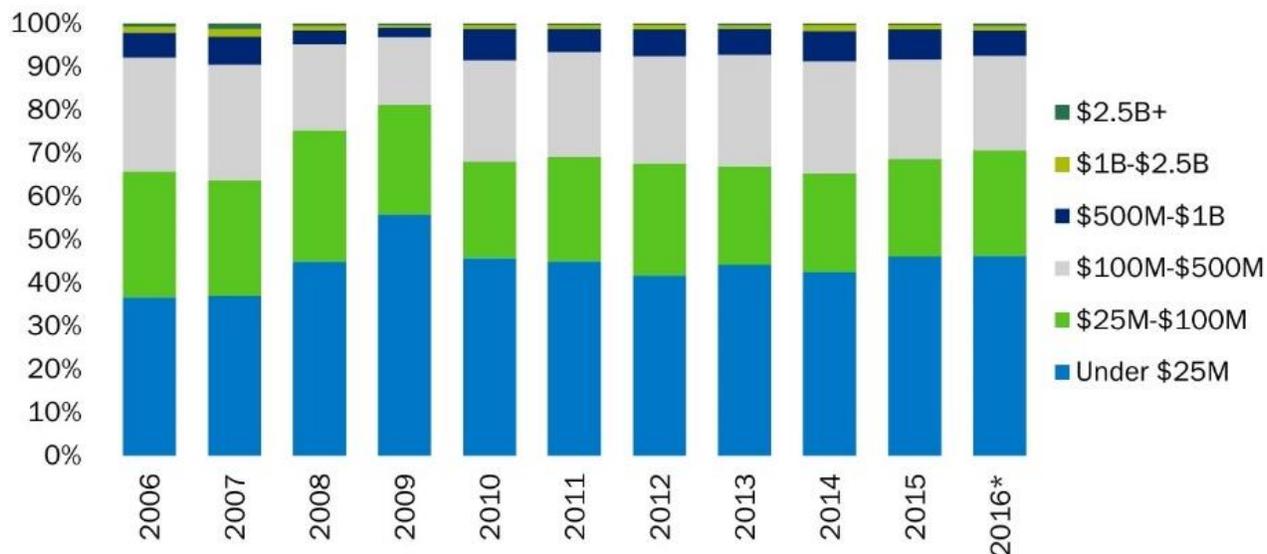
Pitchbook’s recent report, [US PE Breakdown 3Q 2016](#) reveals 2016 YTD results that do not surprise. Investors are reaching down-market, targeting smaller, less expensive add-ons to mitigate the inflated valuations of larger, platform acquisitions. Add-ons represented a whopping 64% of buyout activity for the first 9 months of 2016, the highest level recorded in a decade.



*to Sept 30, 2016

In addition, 46% of deals done in the first nine months of the year were less than \$25 million, the highest level seen since 2009.

U.S. PE Deal Volume by Deal Size

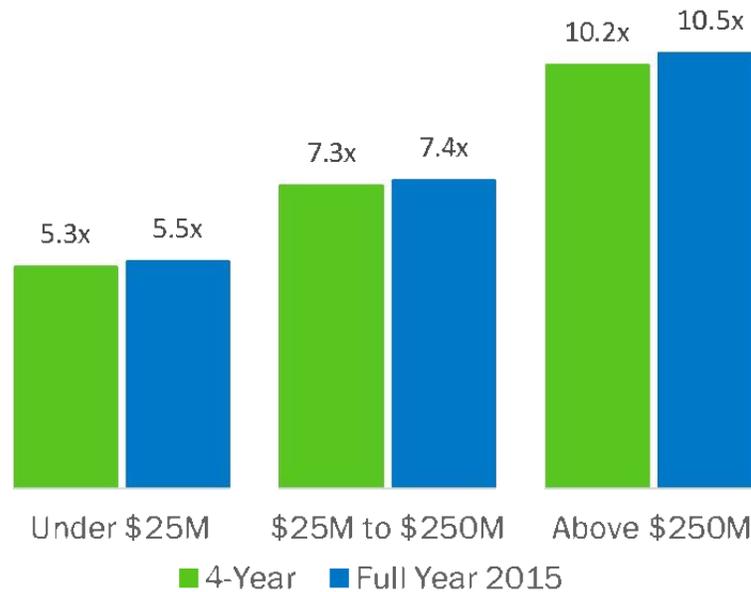


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This private equity (PE) activity makes sense to us for several reasons. We [previously discussed](#) the value of making frequent, smaller acquisitions as part of a “programmatic” M&A strategy. Evidence suggests this strategy is agnostic as it relates to economic environment – that is, programmatic acquirers create relative value in good times and bad. While the move towards add-on acquisitions doesn’t necessarily define current PE investor activity as programmatic, it is an important value-creating element of that strategy.

In addition, this add-on activity makes sense in today’s environment where PE’s compete against strategic buyers for a shrinking pool of targets, with strategics typically better positioned to justify higher valuations for large acquisitions.^[1] In pursuing add-ons to an existing platform, PE’s can take a strategic buyer perspective. The platform company already has infrastructure and management in place, and there is the potential benefit of cost-side and distribution synergies and [multiple arbitrage](#). Thus, PE’s are better able to compete with strategic buyers at the add-on level.

Median EV/EBITDA Multiples by EV



Finally, there is a clear relationship between valuation and size of target. With valuations reaching lofty new heights, the pursuit of smaller, add-on acquisitions at lower multiples is an effective gateway to value creation.

[i](#) Although [we've argued before](#) that these justifications often fail to materialize