

Q3 2017



Currency			BID
AUD	SGD		1.1031
AUD	USD		1.1017
AUD	USD		0.8374
EUR	USD		1.2379
AUD	JPY		1.2368
USD	JPY		100.6300
AUD	JPY		100.7100
USD	JPY		120.1700
AUD	CNY		120.2100
AUD	EUR		5.1525
USD	EUR		5.1560
AUD	EUR		0.6765
USD	HKD		0.6771
AUD	HKD		7.7513
AUD	GBP		7.7514
AUD	GBP		7.7514
AUD	NZD		0.5351
			0.5355
			1.0784
			1.0796

These quotes are delayed market rates sourced from Reuters.

INTERNATIONAL BUSINESS BROKERS ASSOCIATION | M&A SOURCE | PEPPERDINE PRIVATE CAPITAL MARKETS PROJECT

MARKETPULSE

QUARTERLY SURVEY

THIRD QUARTER 2017



A full copy of the Market Pulse survey results is available to IBBA and M&A Source members who participate in each quarterly survey. This is a 100-plus page document of up-to-date, relevant information on the state of the marketplace and compiled by Dr. Craig Everett, assistant professor of finance and director, Pepperdine Private Capital Markets Project.

To become a member, please contact the IBBA and M&A Source.

INTERNATIONAL BUSINESS BROKERS ASSOCIATION

7100 E. Pleasant Valley Road
Suite 160
Independence, OH 44131
Office: 888-686-IBBA
www.ibba.org

Lou Vescio, CBI, M&AMI
Chairman

Lisa Riley, PhD, CBI
Market Pulse Chair

Scott Bushkie, CBI, M&AMI
Market Pulse Committee

Kylene Golubski
Executive Director

M&A SOURCE

3525 Piedmont Road
Building Five, Suite 300
Atlanta, GA 30305
www.masource.org

John Howe, M&AMI
Chairman

David Ryan
Market Pulse Committee

Karl Kirsch
Executive Director

PEPPERDINE PRIVATE CAPITAL MARKETS PROJECT

Pepperdine Graziadio School of Business and Management
6100 Center Drive
Los Angeles, CA 90045
bschool.pepperdine.edu/privatecapital

Dr. Deryck J. van Rensburg
Dean

Dr. Craig R. Everett
Director

Lisa Perry, MBA
Director, Marketing & Communications

Irina Shaykhutdinova
Research Associate

© 2012-2017. All Rights Reserved

The IBBA and M&A Source Market Pulse

SURVEY REPORT Q3 2017

The quarterly IBBA and M&A Source Market Pulse Survey was created to gain an accurate understanding of the market conditions for businesses being sold in Main Street (values \$0-\$2MM) and the lower middle market (values \$2MM-\$50MM). The national survey was conducted with the intent of providing a valuable resource to business owners and their advisors. The IBBA and M&A Source present the Market Pulse Survey with the support of the Pepperdine Private Capital Markets Project and the Graziadio School of Business and Management at Pepperdine University.

The Q3 2017 survey was completed by 334 business brokers and M&A advisors. About a third of the respondents (35 percent) had at least 10 years of experience. Respondents completed 266 transactions this quarter.

FIGURE 1: MARKET SEGMENTS STUDIED

MAIN STREET	LOWER MIDDLE MARKET
Less than \$500K	\$2MM - \$5MM
\$500K - \$1MM	\$5MM - \$50MM
\$1MM - \$2MM	

According to labor statistics, the U.S. has added 16 million jobs since February 2010, and September 2017 hourly earnings increased 2.9 percent over the year. The labor market is tightening and unemployment rates remain at prerecession levels.

The challenge to find good talent could be good news for the M&A market. More than half (55 percent) of the business brokers and advisors surveyed expect the shrinking labor market will cause more business owners to expand through acquisition.

"Talent scarcity is driving M&A activity," said David Ryan, an advisor with Upton Financial Group in California. "For businesses looking to grow, acquisitions present an efficient way to land a trained and established labor force. When we talk to corporate M&A teams, we increasingly hear that talent acquisition is a key part of their strategy."

A tightening labor market could help spur the Fed to raise interest rates, with another rate increase anticipated this December. Nearly half (49 percent) of the advisors surveyed say the potential for rising interest rates has buyers and sellers pursuing aggressive timelines, hoping to get deals closed more quickly while financing is cheaper.

Meanwhile, most advisors (81 percent) say that uncertainty over Trump's tax plan is having little impact on M&A activity in the Main Street and lower middle market.

"We understand that tax uncertainty has hit the larger M&A market, as U.S.-targeted deals fell to their lowest rate since 2013," said Craig Everett, PhD, Director of the Pepperdine Private Capital Markets Project. "But here in the

Main Street and lower middle markets, sellers are maintaining a 'business as usual' approach when it comes to M&A tax issues."

"Nevertheless, Trump's efforts to reduce regulatory tax burdens have had a positive impact on some small and medium businesses," continued Everett. "The withdrawal of IRS Section 2704 means family business owners will still have access to some critical valuation discounts when transferring business shares to their kids. But essentially, the only real clarity we have right now is around taxes that support family succession plans, not outside M&A."

"If Trump's larger tax reforms go forward, we could see increased buyer demand as they have more available cash to execute deals," said John Howe, M&AMI, Director, Business Transition Strategies, M&A Source Chair. "If that happens, sellers may follow, provided they are keeping a pulse on valuation metrics. Unfortunately, sellers in this market segment aren't always proactive about working with the kind of advisor who will keep them updated on market trends."

On the other hand, more available capital might not increase deal flow.

"We're facing a shortage of high-quality acquisition targets in the lower middle market. Buyers already have the capital to spend, we just don't have the inventory to meet their needs," said Lou Vescio, CBI, M&AMI, Principal, Coastal Business Intermediaries, Inc., IBBA Chair.

In fact, advisors do not expect valuations to increase at all in the next three months. And while they report that incoming deal flow did not increase in Q3 2017, they hope for a modest uptick at year end.

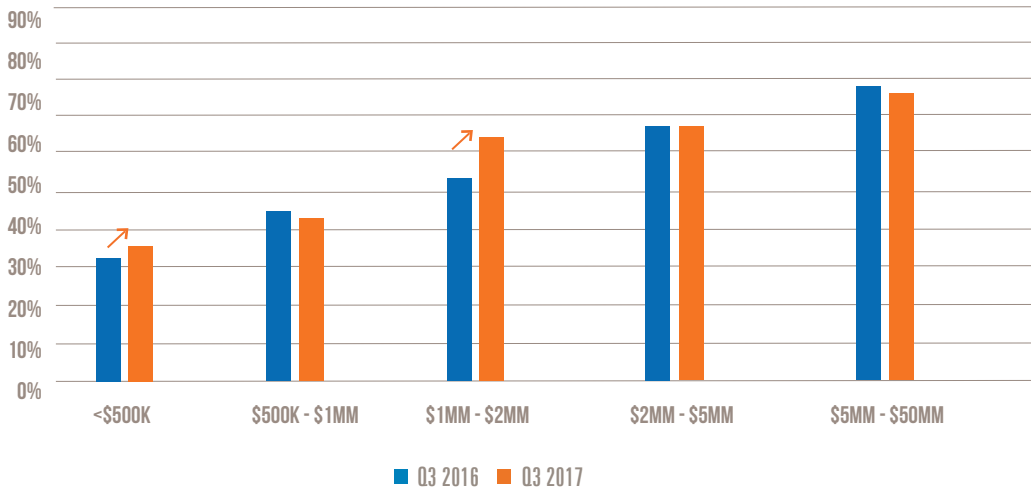
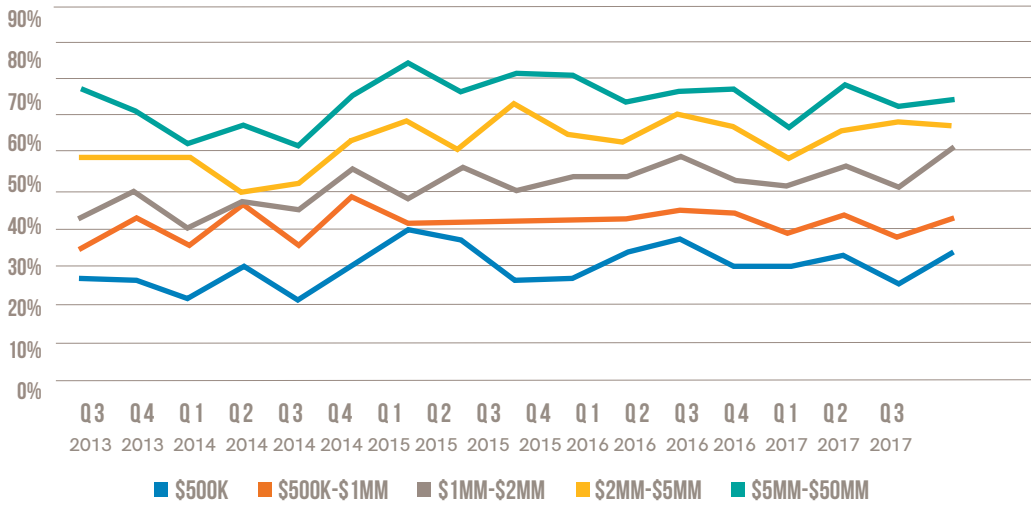
FIGURE 2: EXPECTATIONS MODEST

RECENT TRENDS AND EXPECTATIONS	MEAN SCORE (5-POINT SCALE)
Incoming deal flow	3.15
Expectation for new listings in next 3 months	3.50
Expectation for business valuations in next 3 months	3.07

*Mean score of 3 indicates no decline or growth (experienced or expected). Mean score averaged across all deal sectors.

FIGURE 3: SELLER'S MARKET SENTIMENT

Seller market sentiment is positive, reaching an all-time high in the \$1MM-\$2MM sector since the survey began in Q2 2012.



Year-over-year, multiples saw declines in most market segments. Nevertheless, multiples continue to remain strong. For sellers, valuations remain a compelling reason to enter the market. Meanwhile, buyers are no longer up against peak market prices, making it easier to justify an acquisition.

“Again, it is the opinion of the vast majority of deal makers that the market is going to get worse before it gets significantly better as business confidence reports indicate declines for the second consecutive quarter,” said Carlos Guevara, CBI, VR Business Brokers San Antonio.

FIGURE 4: MEDIAN MULTIPLE

	2017			2016			2015		
	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3
MEDIAN MULTIPLE PAID (SDE)									
<\$500K	2.0	2.0	2.3	2.3	2.3	2.3	2.0	2.0	2.0
\$500K-\$1MM	2.5	2.3	2.8	2.8	3.0	2.8	2.8	2.5	2.5
\$1MM-\$2MM	3.1	3.3	3.3	3.3	3.3	3.3	3.0	3.3	2.8
MEDIAN MULTIPLE PAID (EBITDA)									
\$2MM - \$5MM	4.5	4.3	5.3	4.8	4.5	4.0	4.0	4.0	4.0
\$5MM - \$50MM	5.0	5.4	5.3	5.5	5.8	5.1	5.5	5.1	5.3

FIGURE 5: COMMON MULTIPLE RANGE Q3 2017

COMMON MULTIPLE RANGE (SDE)	
<\$500K	59% between 1.5-2.5
\$500K - \$1MM	68% between 2.0-3.0
\$1MM - \$2MM	50% between 3.0-3.25
\$2MM - \$5MM	42% between 3.0-3.25
COMMON MULTIPLE RANGE (EBITDA)	
\$2MM - \$5MM	59% between 3.5-4.5
\$5MM-\$50MM	60% between 4.0-5.5

FIGURE 6: MOST COMMON MULTIPLE TYPE BY DEAL SIZE

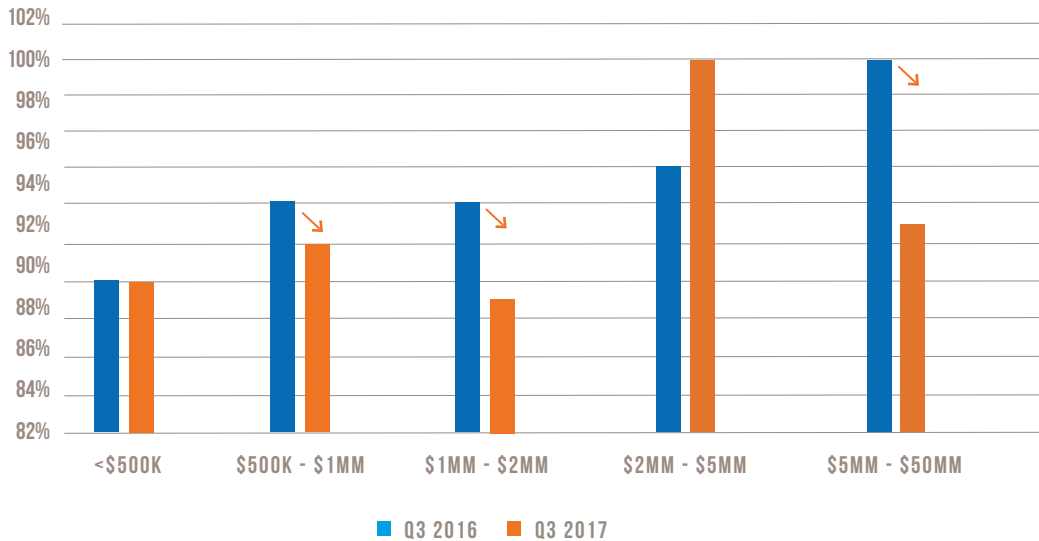
DEAL SIZE	MOST COMMON MULTIPLE TYPE
\$500K	SDE w/o working capital
\$500K - \$1MM	SDE w/o working capital
\$1MM - \$2MM	SDE w/o working capital
\$2MM - \$5MM	EBITDA incl. working capital
\$5MM - \$50MM	EBITDA incl. working capital

*SDE Sellers Discretionary Earning

*EBITDA Earnings Before Interest, Taxes, Depreciation and Amortization



FIGURE 7: FINAL PRICE REALIZED VS. ASKING PRICE



Year over year, time to close has shrunk in most sectors with progress accelerating significantly in the \$500K-\$1MM and the \$5MM-\$50MM sectors.

FIGURE 8: TIME TO CLOSE

BUSINESS VALUE	Q3 2017		Q2 2017		Q3 2016	
	MONTHS TO CLOSE	LOI TO CLOSE	MONTHS TO CLOSE	LOI TO CLOSE	MONTHS TO CLOSE	LOI TO CLOSE
<\$500K	6	2	6	2	7	2
\$500K - \$1MM	6.5	2	6	2	8	3
\$1MM - \$2MM	7.5	3	7	3	8	3
\$2MM - \$5MM	9	3	9	3	8	3
\$5MM - \$50MM	10.5	3.5	9	5	12	4.5

“Time frames may be lower due to sellers being more prepared and having a team that can help them move through the due diligence process more efficiently. The less prepared the seller and their team is the longer the process drags out and we all know the phrase, ‘Time Kills All Deals’ is all too true,” said Michael Fekkes, M&AMI, CBI, of Enligh Advisors.



In this quarter, owners received 71 percent or more cash at close. The majority of the balance came from seller financing, along with some earn outs to close the valuation gap. Trends remain relatively stable year-over-year.

FIGURE 9: PORTION OF SALE RECEIVED AS CASH AT CLOSE

	Q3 2017			Q3 2016		
	CASH AT CLOSE*	SELLER FINANCING	EARN OUT	CASH AT CLOSE*	SELLER FINANCING	EARN OUT
<\$500K	84%	12%	2%	83%	15%	1%
\$500K - \$1MM	83%	11%	1%	80%	17%	1%
\$1MM - \$2MM	71%	17%	7%	80%	12%	3%
\$2MM - \$5MM	86%	14%	1%	78%	12%	10%
\$5MM - \$50MM	73%	10%	4%	75%	8%	4%

*Cash at close reflects a combination of buyer's equity and senior debt.

In Q3 2017, retirement continues to lead as the number one reason to sell across all sectors, followed by burnout and new opportunities.

FIGURE 10: TOP 2 REASONS SELLERS WENT TO MARKET Q1

DEAL SIZE	#1 REASON	#2 REASON	#3 REASON
<\$500K	Retirement	New Opportunity	Burnout
\$500K - \$1MM	Retirement	Burnout	New Opportunity
\$1MM - \$2MM	Retirement	New Opportunity	Health
\$2MM - \$5MM	Retirement	Burnout	Family Issues
\$5MM - \$50MM	Retirement	(tie) Family Issues, Burnout	

"It can't be stressed enough how much better chance of success a business owner will have selling their business if they have the right team around them and proactively set an exit strategy and then execute on the plan versus reacting to a negative trigger in their business or personal life," said Scott Bushkie, M&AMI, CBI, President of Cornerstone Business Services.

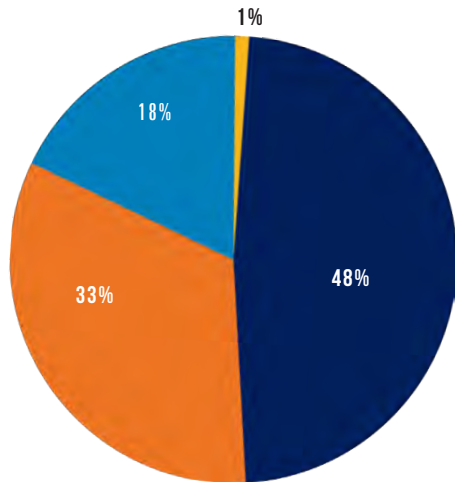


KNOW YOUR BUYER

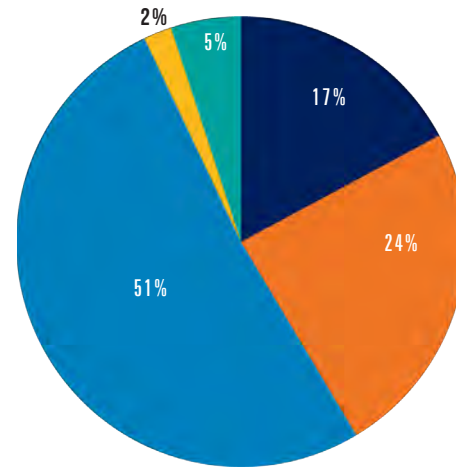
In the Main Street market, first time buyers accounted for the largest buyer segment (48 percent). Meanwhile, in the lower middle market, existing businesses accounted for 51 percent of buyers, followed by 24 percent experienced business owners.

FIGURE 11: BUYER COMPARISON BY SMALLEST/LARGEST MARKET SECTORS

MAIN STREET



LOWER MIDDLE MARKET



■ 1ST TIME INDIVIDUAL ■ INDIVIDUAL WHO OWNED BUSINESS
■ EXISTING COMPANY/STRATEGIC BUYER ■ PE FIRM - PLATFORM

■ 1ST TIME INDIVIDUAL ■ INDIVIDUAL WHO OWNED BUSINESS
■ EXISTING COMPANY/STRATEGIC BUYER ■ PE FIRM - PLATFORM ■ PE FIRM - ADD ON

"I think we're seeing significant activity from existing businesses for several reasons: We have a strong lending environment, corporate balance sheets are strong, and stock values are at record highs," said Mike Camerota, JD, M&AMI, of Touchstone Advisors. "It's an ideal time for companies to borrow."

WHAT MOTIVATES THEM?

Looking at buyer motivation reveals an uptick in activity by private equity and strategic corporate buyers, when compared to Q2.

FIGURE 13: BUYER MOTIVATION SHIFTS WITH TRANSACTION SIZE

	BUYING A JOB		GROWING VIA ACQUISITION/ADD-ON		BETTER ROI THAN OTHER INVESTMENT	
	Q3	Q2	Q3	Q2	Q3	Q2
<\$500K	52%	60%	26%	22%	7%	6%
\$500K - \$1MM	39%	52%	38%	27%	9%	13%
\$1MM - \$2MM	23%	24%	36%	20%	36%	28%
\$2MM - \$5MM	13%	19%	48%	47%	16%	24%

"Our economy is growing at just two percent. That, combined with the tight labor market, means organic growth is a real challenge right now," said Andrew Rogerson, M&AMI, CBI, Principal of Rogerson Business Services. "There's a strong demand for add-on acquisitions in the lower middle market."

WHAT ARE THEY BUYING?

Looking at the overall market, manufacturing and construction/engineering led among hot industries.

FIGURE 14: TOP INDUSTRIES BY MARKET SECTOR

<\$500K	Restaurants	Personal Services	Consumer Goods
\$500K - \$1MM	Personal Services	Restaurants	Manufacturing
\$1MM - \$2MM	Manufacturing	(tie) Consumer Goods/Construction/Engineering	
\$2MM - \$5MM	Manufacturing	Business Services	Construction/Engineering
\$5MM - \$50MM	Manufacturing	Construction/Engineering	

"Manufacturing companies are really hot right now. The manufacturers we've been taking to market are getting strong values," explains Lisa Riley, CBI, Principal of LINK Business-Phoenix. "Even manufacturers with significant issues like customer concentration are getting good looks, and it's a sign of how keyed in the market is to manufacturing right now."



ABOUT PEPPERDINE GRAZIADIO SCHOOL OF BUSINESS AND MANAGEMENT

Anchored in the core values of integrity and innovation, the [Pepperdine Graziadio School of Business and Management](#) challenges individuals to think boldly and drive meaningful change that positively impacts their organizations and communities. With an entrepreneurial spirit, the Graziadio School advances experiential learning in small classes that deepen connections and stimulate critical thinking. Through our wide continuum of MBA, MS and Executive degree programs offered across six California campuses, Graziadio faculty inspire full time students and working professionals to realize their greatest potential as values-centered, "best for the world" leaders. Follow Pepperdine Graziadio on [Facebook](#), [Twitter](#), [Instagram](#), and [LinkedIn](#).

The Pepperdine Private Capital Markets Project reports on the current climate for privately held companies to access and raise capital, as well as the conditions influencing the decisions of lenders and providers serving small businesses and the lower middle market. Our ongoing research engages in multiple survey research initiatives and publishes an annual Capital Markets Report, an annual economic forecast, the PCA Index Quarterly Report in partnership with Dun & Bradstreet and Market Pulse Quarterly Report in cooperation with the International Business Brokers Association and M&A Source.

ABOUT INTERNATIONAL BUSINESS BROKERS ASSOCIATION

Founded in 1983, IBBA is the largest non-profit association specifically formed to meet the needs of people and firms engaged in various aspects of business brokerage, and mergers and acquisitions. The IBBA is a trade association of business brokers providing education, conferences, professional designations and networking opportunities. For more information about IBBA, visit the website at www.ibba.org or follow the IBBA on [Facebook](#), [Twitter](#), and [LinkedIn](#).

ABOUT THE M&A SOURCE

Founded in 1991, the M&A Source promotes professional development of merger and acquisition professionals so that they may better serve their clients' needs, and maximize public awareness of professional intermediary services available for middle market merger and acquisition transactions. For more information about the M&A Source visit www.masource.org or follow The M&A Source on [Facebook](#), [LinkedIn](#), or [Twitter](#).



Earn A Certificate in Private Capital Markets



PEPPERDINE | GRAZIADIO SCHOOL OF BUSINESS AND MANAGEMENT

Enroll in Pepperdine University Graziadio School of Business and Management three-day Private Capital Markets Project Certificate program. Dr. Craig R. Everett, director of the ground-breaking Pepperdine Private Capital Market Project research, leads this dynamic program designed for business and financial



professionals to gain knowledge, skills and insights to succeed in the Private Capital Markets industry.

Driving Leadership:

Explore an in-depth overview of the Private Capital Markets, earning a valuable credential from the top ranked Pepperdine Graziadio Business School.

Tackle the Complexity of Today's Capital Markets:

Gain critical analysis and evaluating skills for transacting successful financing deals, learning valuation methods, essential in accurate valuation.

Build Value by Making Better Investment and Financing Decisions:

Analyze various types of capital in the private markets from bank loans and asset based lending to equity funding.

ELEVATE YOUR CAREER

**ENROLL IN THE PRIVATE CAPITAL MARKET
CERTIFICATE PROGRAM.**

bschool.pepperdine.edu/cipcm