Datasite®
Where deals are made

As the tide turns, what's next?

H2 2022 Market Outlook

Data provided by PitchBook

Contents

Executive summary 03

Charting the buyout boom 04

An emphasis on buy-and-build 05

Deal speed and holding periods 10

Looking ahead 12

Methodology 13

As the tide turns, what's next? The Datasite view 14

Three keys to pipeline success in an uncertain market 16

By your side across the PE spectrum 17

Executive summary

There has never been a year for deals quite like 2021. Records didn't just tumble; they were smashed. Private equity (PE) capital investment topped $2 trillion, beating 2018 by 46.7% and 2020 by 65.8%. Meanwhile, deal volume eclipsed 17,000 worldwide, soaring past the previous high of 13,000. What's more, those 17,707 deals were done in record time. On average, it took just 2.6 months from announcement to completion, 11.5% faster than the 2020 median of 2.9 months.

In the recent uncertain landscape, add-ons were hot property. They made up 52.2% of global deal flow, up from the pre-pandemic figure of 47.6% in 2019. This upward trend has continued through May 2022, with add-ons now at 53.2%. The COVID-19 pandemic also helped drive the shift toward buy-and-build. Wary of the risk of taking on a new platform company, investors preferred to put their capital to work by growing their current platform companies, with 2,000 add-ons completed per quarter between Q4 2020 and Q4 2021. For comparison, the pre-COVID-19 figure is nearer to 1,500. There were also more add-ons per platform – an average 2.1 compared with 1.8 in 2020. And the median value of an add-on deal spiked to $52.4 million as valuations rose to record levels across the board.

Nowhere was this more apparent than in the US. Already the global leader for PE activity, the US saw a staggering 71.2% growth in deal value, the highest among all major regions. But the Europe, Middle East, and Africa region (EMEA) and the Asia-Pacific region (APAC) were not far behind, at 61.8% and 59.5% growth, respectively, as PE dealmakers enjoyed favorable conditions worldwide.

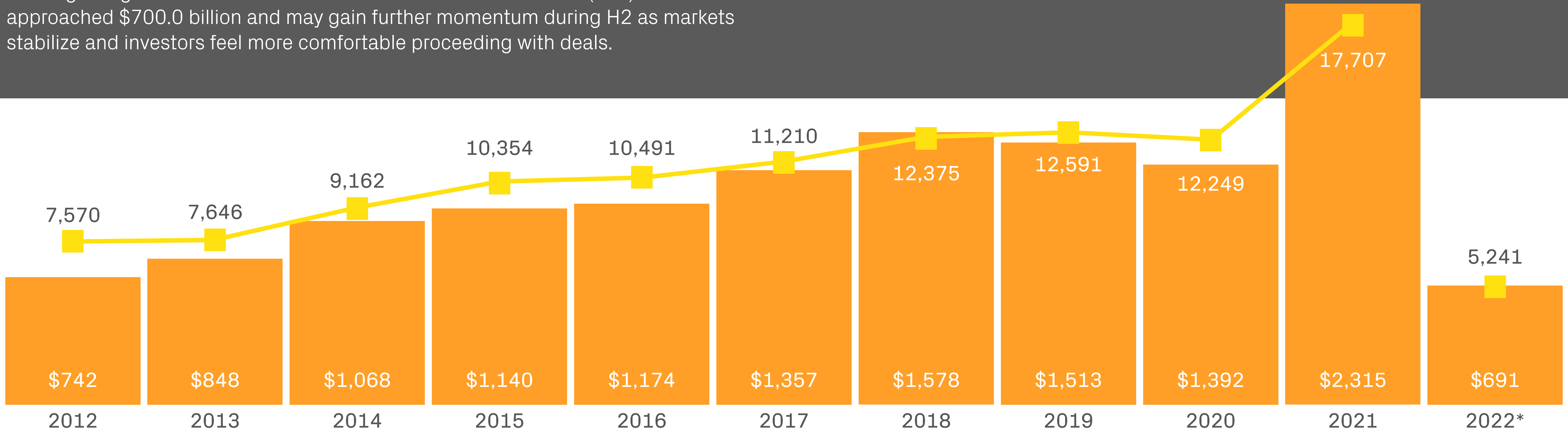
Pipeline management proved crucial in sustaining this unprecedented momentum. With pipelines bottlenecked due to the frantic PE exit activity, PE hold times plunged to their lowest in a decade as sellers raced to offload long-held assets.

It was always inevitable that such a surge of activity would eventually tail off. The start of 2022 brought rockier macroeconomic conditions, presenting investors with a more challenging road ahead. The result so far is not so much a slowdown as a rebalancing to a new normal. Although the mega-deals are drying up, the lower middle market continues to simmer, while the technology, media, and telecommunications (TMT) surge continues. Indeed, dealmakers are benefiting from the slower pace, seizing their chance to reconfigure strategies. The 2021 supernova may have flickered out, but there is still plenty of light ahead.

Charting the buyout boom

Pent-up activity in the wake of COVID-19 made the PE market pop. Deal values broke records every quarter, with Q1 2021 setting the bar and each successive quarter pushing it higher. The tide finally turned in Q1 2022, a particularly volatile quarter for broader markets, with deal value falling 19.8% from Q4 2021. The sheer volume of activity in 2021 may make 2022 look deflated in comparison, but despite the quarter-on-quarter decline, Q1 2022 deal value rose year-on-year, thus signaling that there is still air in investors' tires. Year-to-date (YTD) deal value approached $700.0 billion and may gain further momentum during H2 as markets stabilize and investors feel more comfortable proceeding with deals.

In terms of deal value, PE deals tend to dominate the wider M&A market and have become even more prevalent in recent years. In 2021, PE deals represented 77.4% of total M&A value. So far in 2022, they account for 80.7%. In part, this is because corporate M&A dealmakers have lower levels of liquidity than PE firms and so are more vulnerable to macroeconomic stressors such as rising borrowing costs and supply chain disruptions. This leads to lower activity among these players during uncertain times.

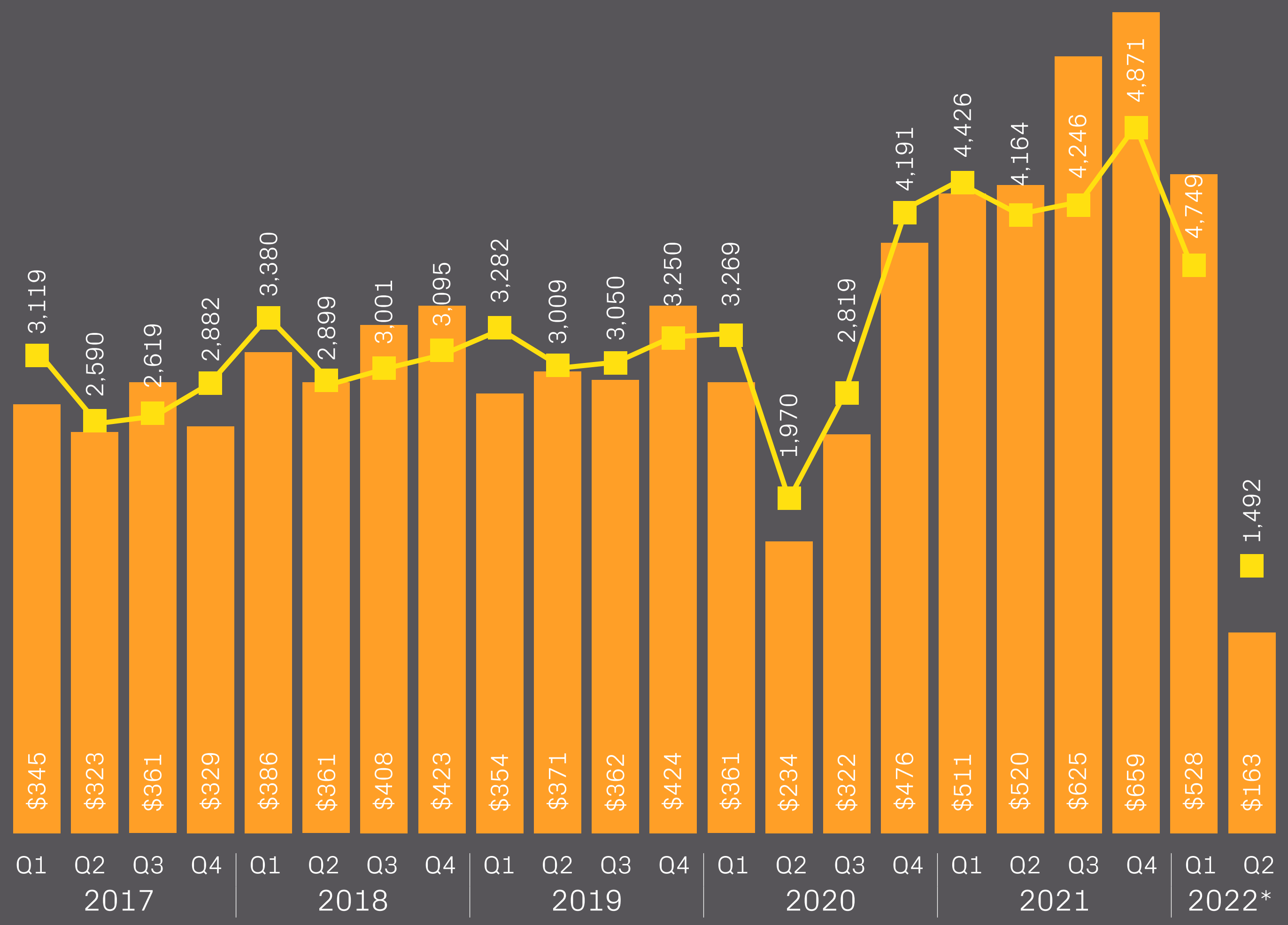


Global PE deal activity

*As of 5/20/2022, Source: PitchBook

Deal value ($bn) Deal count

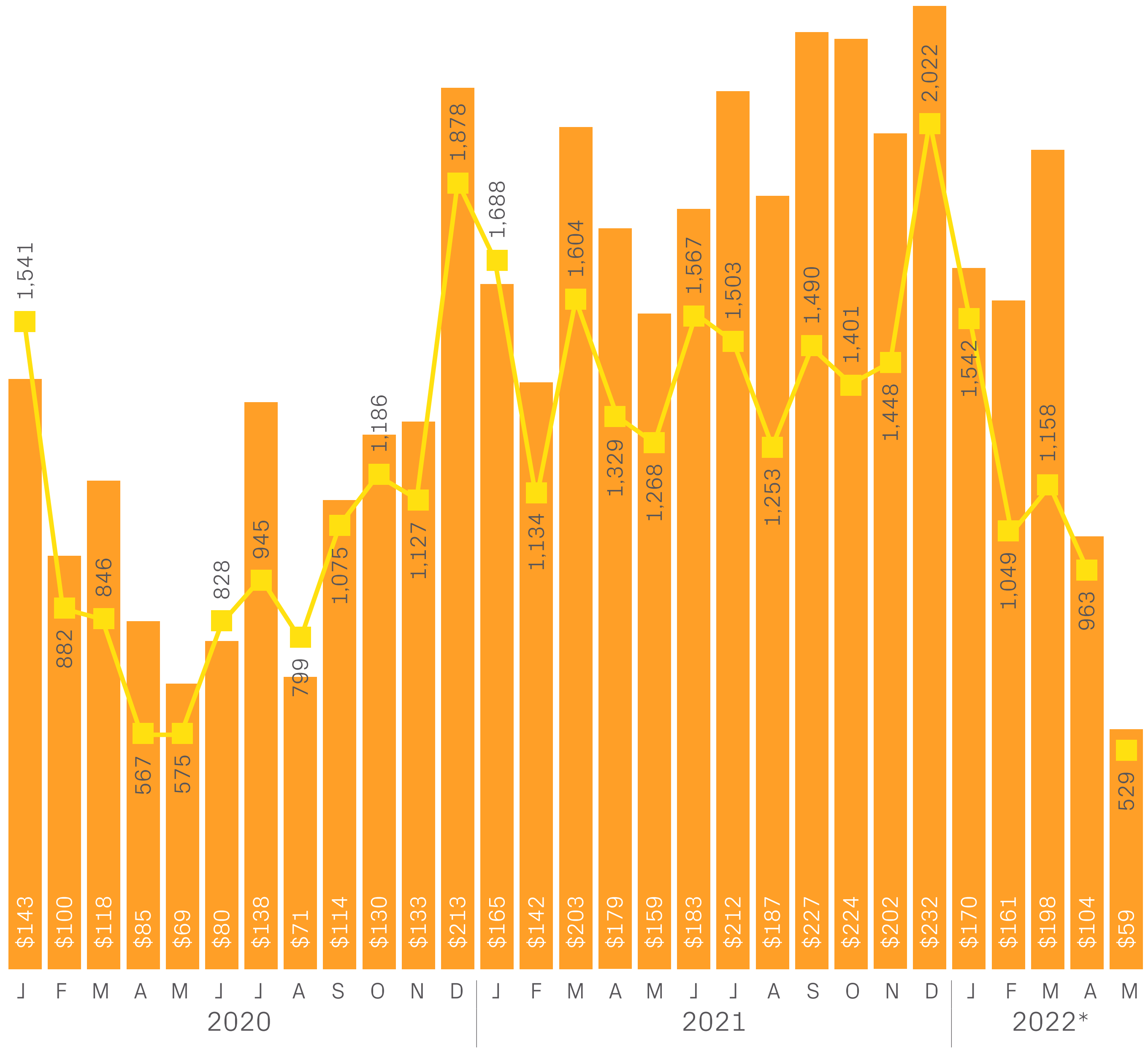
Both PE and corporate deals are historically dominated by the business products & services sector, which commanded a staggering $800.0 billion in deal value in 2021. It remains a top sector YTD but was narrowly outpaced by information technology, as PE firms gravitate toward huge opportunities for software deals in an increasingly digitized economy.



Global PE deal activity by quarter

*As of 5/20/2022, Source: PitchBook

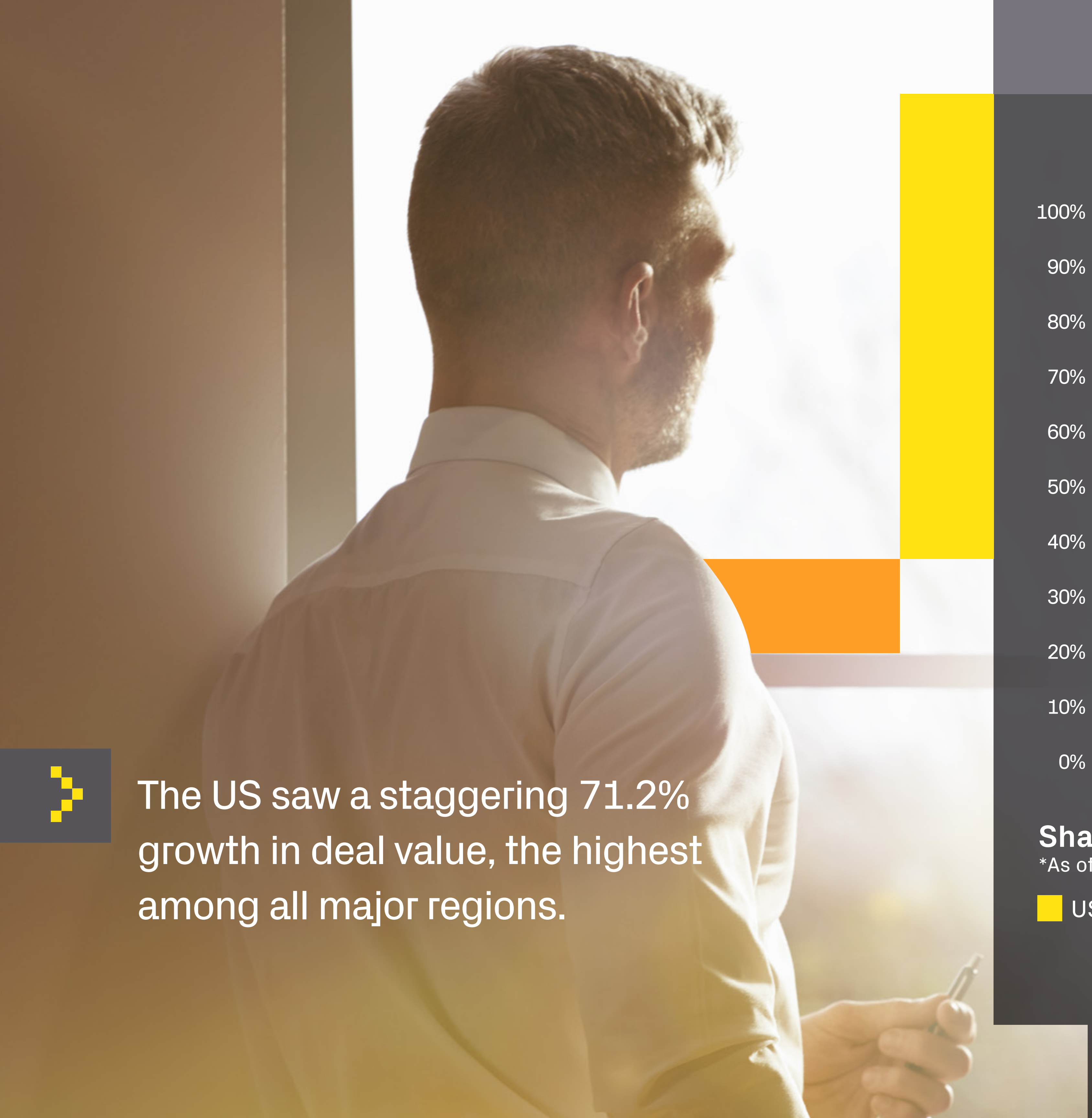
Deal value ($bn) Deal count



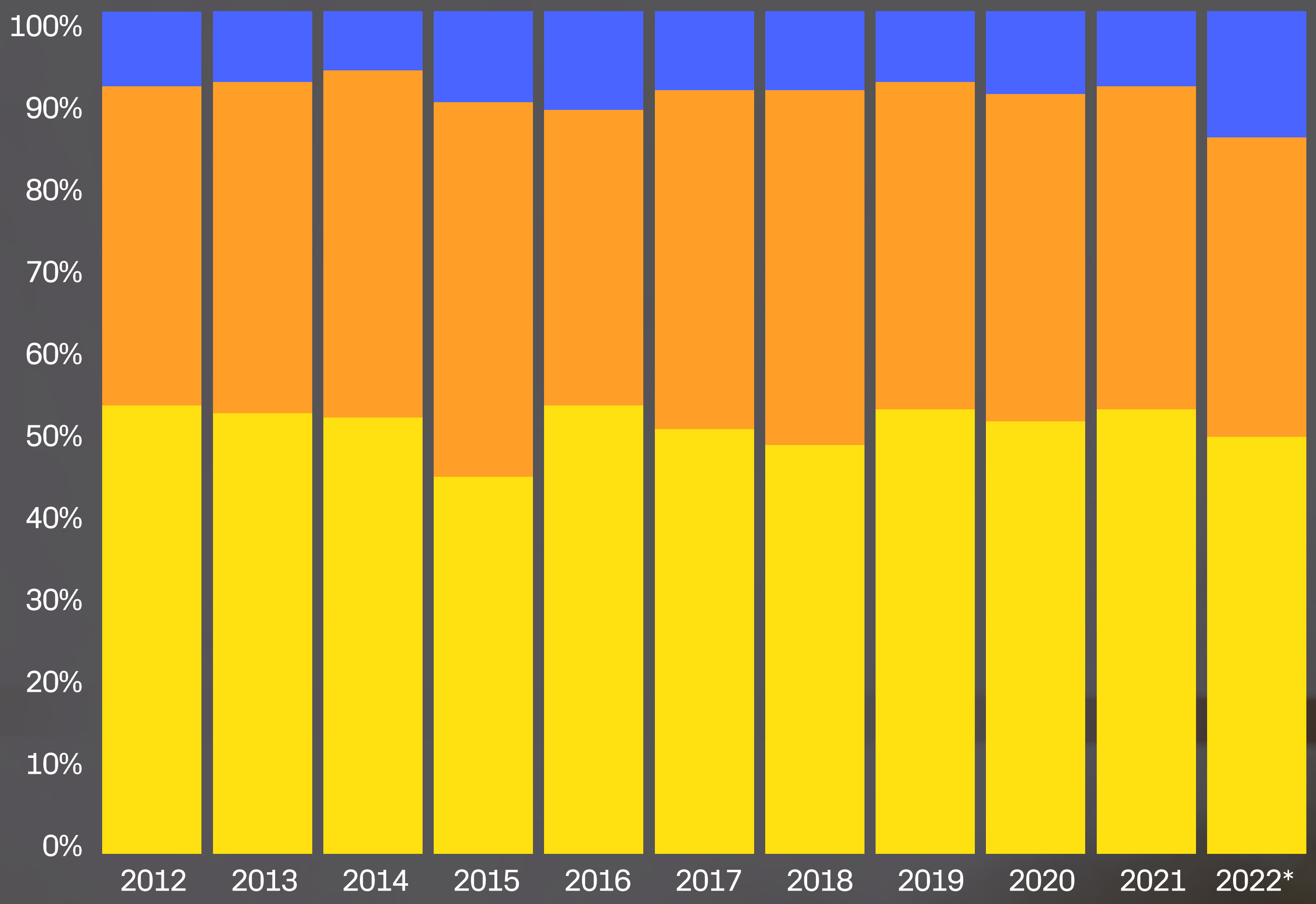
Global PE deal activity by month

*As of 5/20/2022, Source: PitchBook

Deal value ($bn) Deal count



The US saw a staggering 71.2% growth in deal value, the highest among all major regions.



Share of global PE deal value by region

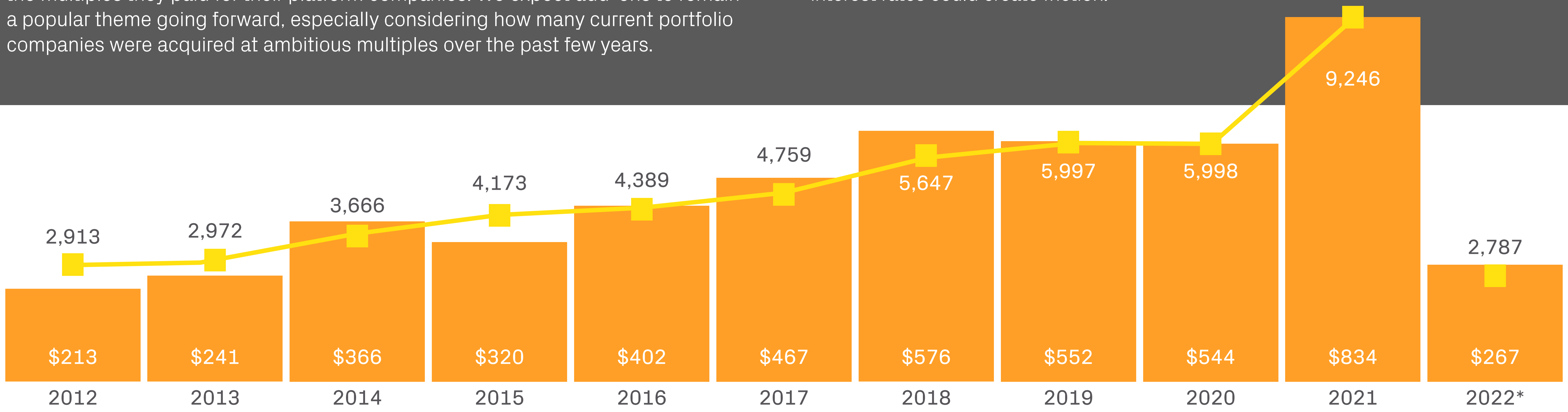
*As of 5/20/2022, Source: PitchBook

US EMEA Asia Pacific

An emphasis on buy-and-build

Over the past decade, add-on deals have made up a steadily rising proportion of PE deals. In 2021, they passed the 50% mark for the first time, as firms began adding more targets per platform in a strategic shift. In the face of pandemic pressures, consolidation within portfolios offered a more favorable outlook while allowing firms to continue deploying capital. In the same period, the median add-on deal value rose by 65.2% as firms maintained high levels of dry powder while interest rates stayed low. Among other reasons, investors initiate add-ons to help blend down the multiples they paid for their platform companies. We expect add-ons to remain a popular theme going forward, especially considering how many current portfolio companies were acquired at ambitious multiples over the past few years.

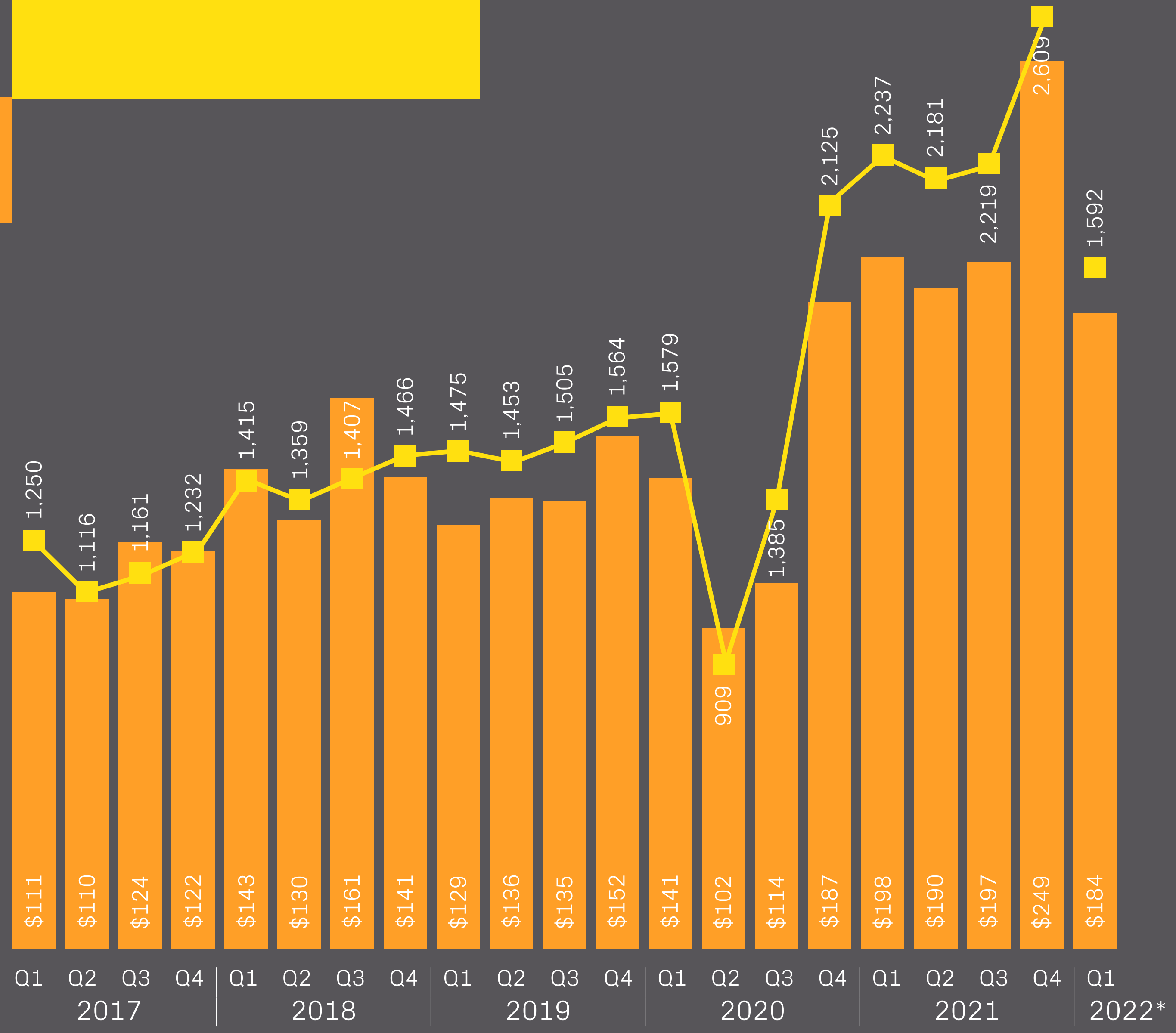
The most active add-on facilitators include several of the most prominent PE firms. The top three add-on investors of the past six months were HarbourVest, Shore Capital Partners, and Silver Lake. Silver Lake's penchant for growth-stage technology deals may prove lucrative due to the current state of the public markets, wherein firms with significant dry powder are seeing discounted prices for tech companies whose stocks struggled in the early part of the year. Firms now have more opportunities to complete cheaper take-private deals and achieve multiple arbitrage. That said, rising interest rates could create friction.



Global add-on activity by year

*As of 5/20/2022, Source: PitchBook

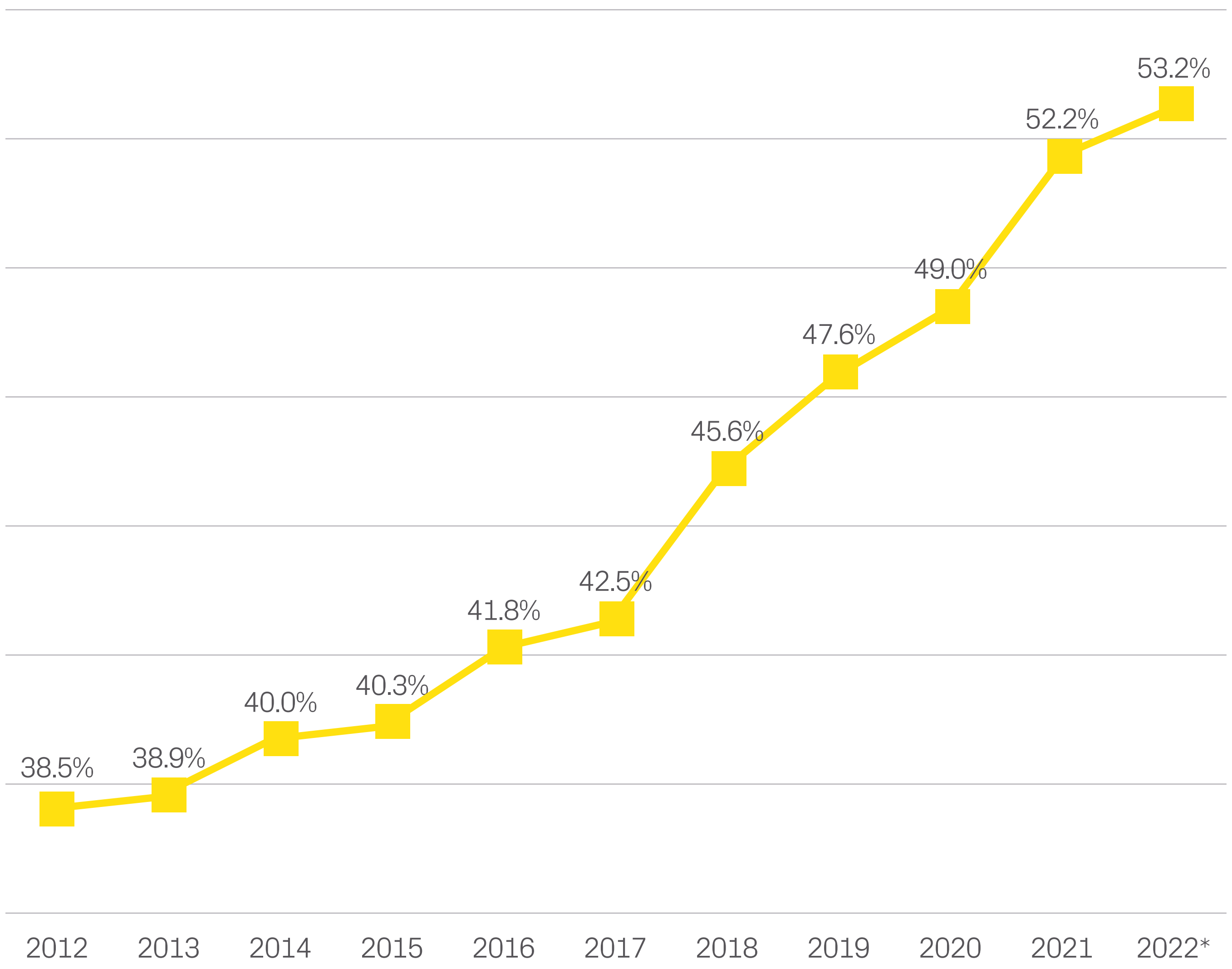
Deal value ($bn) Deal count



Global add-on activity by quarter

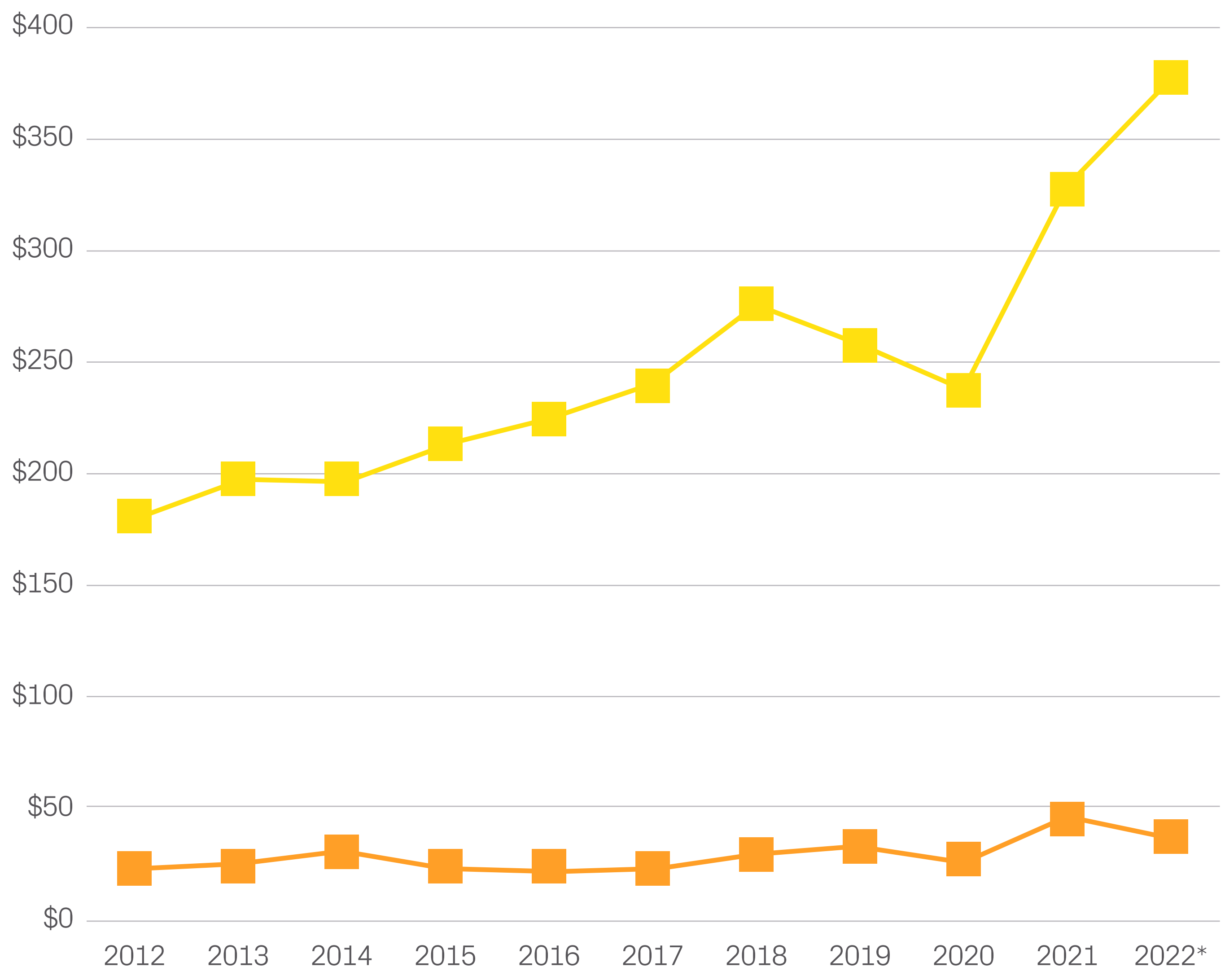
*As of 5/20/2022, Source: PitchBook

Deal value ($bn) Deal count



Add-ons as a share of global PE deals

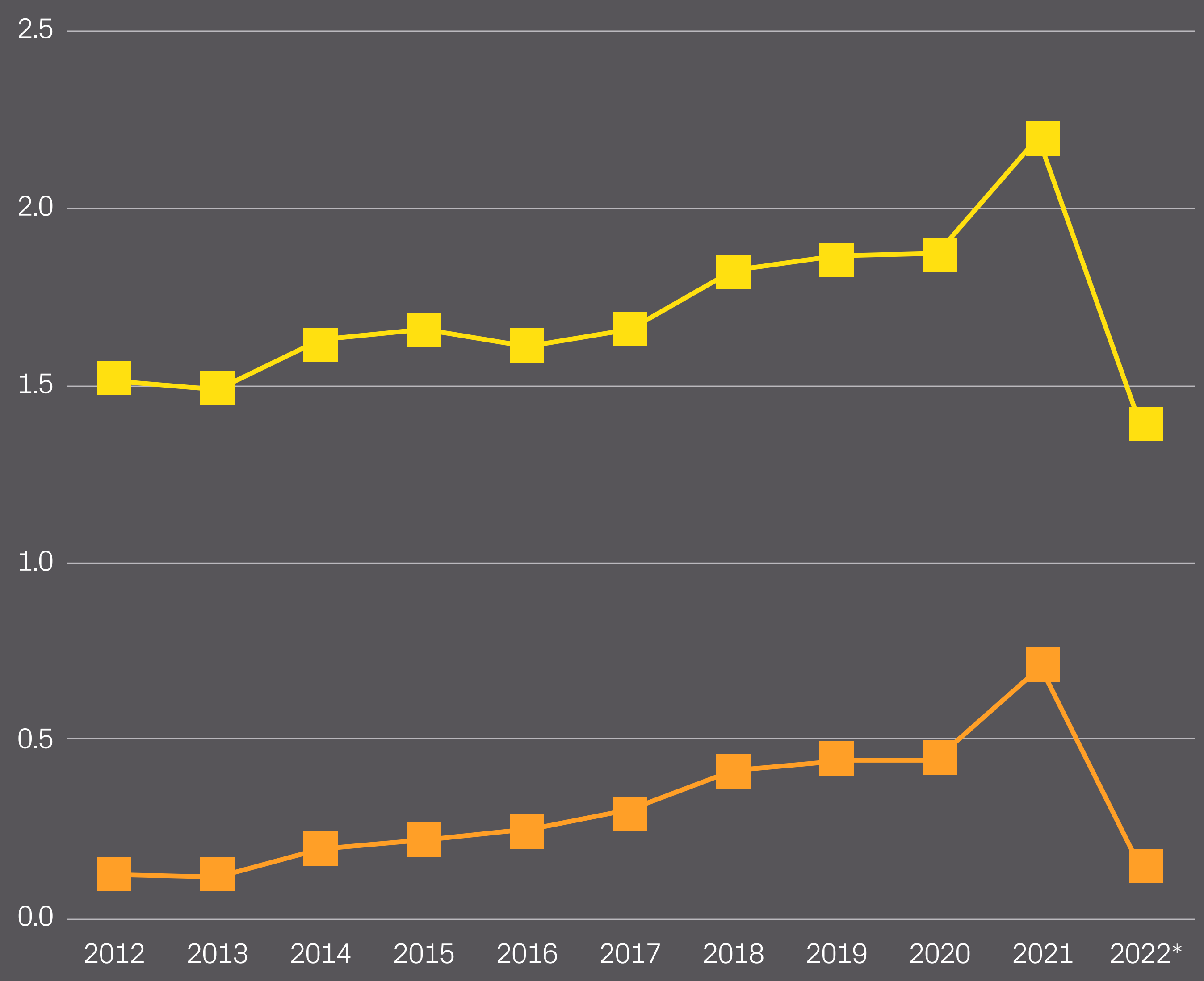
*As of 5/20/2022, Source: PitchBook



Median add-on deal value ($M)

*As of 5/20/2022, Source: PitchBook

Median Average



Average add-on count by platform type

*As of 5/20/2022, Source: PitchBook

All platforms Only platforms w/ add-ons

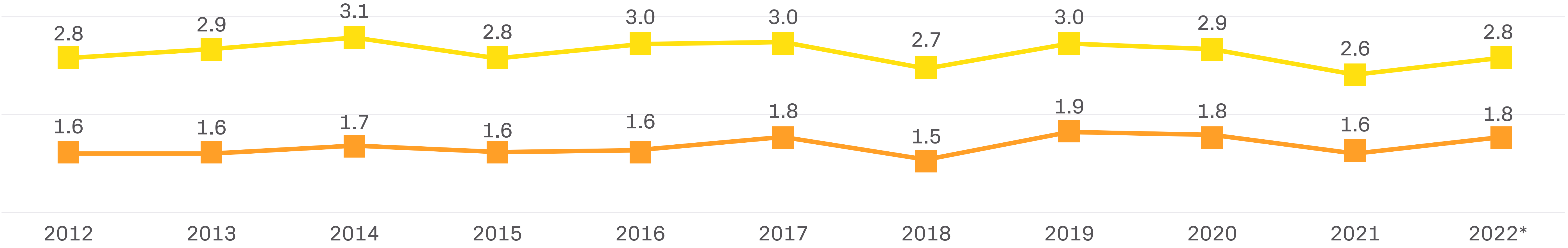
Deal speed and holding periods

As easy as it is to measure completed deals, it's much harder to gauge what may be in the pipeline. The evidence available is generally anecdotal, but in 2021, pipelines were so full that most such anecdotes held true.

Though 2020 itself was a strong year, 2021 saw 45% more PE deals. These were generally crammed into shorter timeframes, with the average time from announcement to completion falling from 2.9 months to 2.6 months – a 12% acceleration to achieve the fastest dealmaking in at least one decade. Taken together, those two datapoints show investment hitting a historic pace.

A surge in PE exit activity also kept pipelines full. One telltale sign of sell-side urgency is the drop in PE hold times, or the amount of time investors held their portfolio companies before exiting in that year.

The median PE hold time in 2021 fell to 5.2 years, down from a median of 5.3 years for 2020 exits, and the lowest seen in at least one decade. The landscape had a significant impact on long-held portfolio companies. The top decile median, or the longest-held portfolio companies, fell from 11.6 years in 2020 to 10.5 years in 2021, one full year's difference. Often, such companies have underlying issues that prevent a quicker exit. But since 2021 was both a buy-side and sell-side frenzy, sellers seized their chance to offload assets that had been in their portfolios for more than a decade. Those exits came as the PE industry warms to so-called continuation funds, which are becoming popular vehicles that help investors harvest more value from funds that have reached their shelf lives.

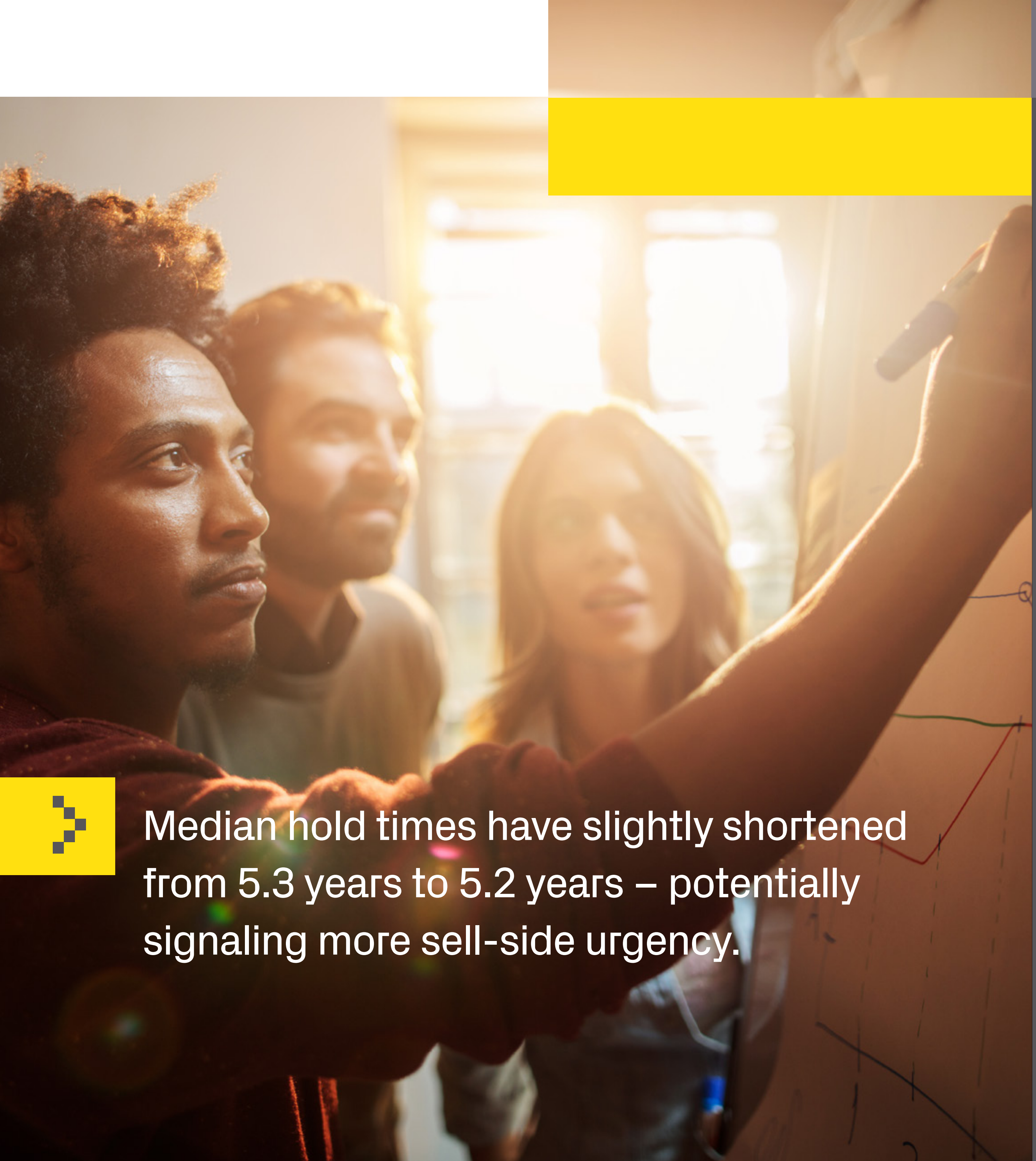


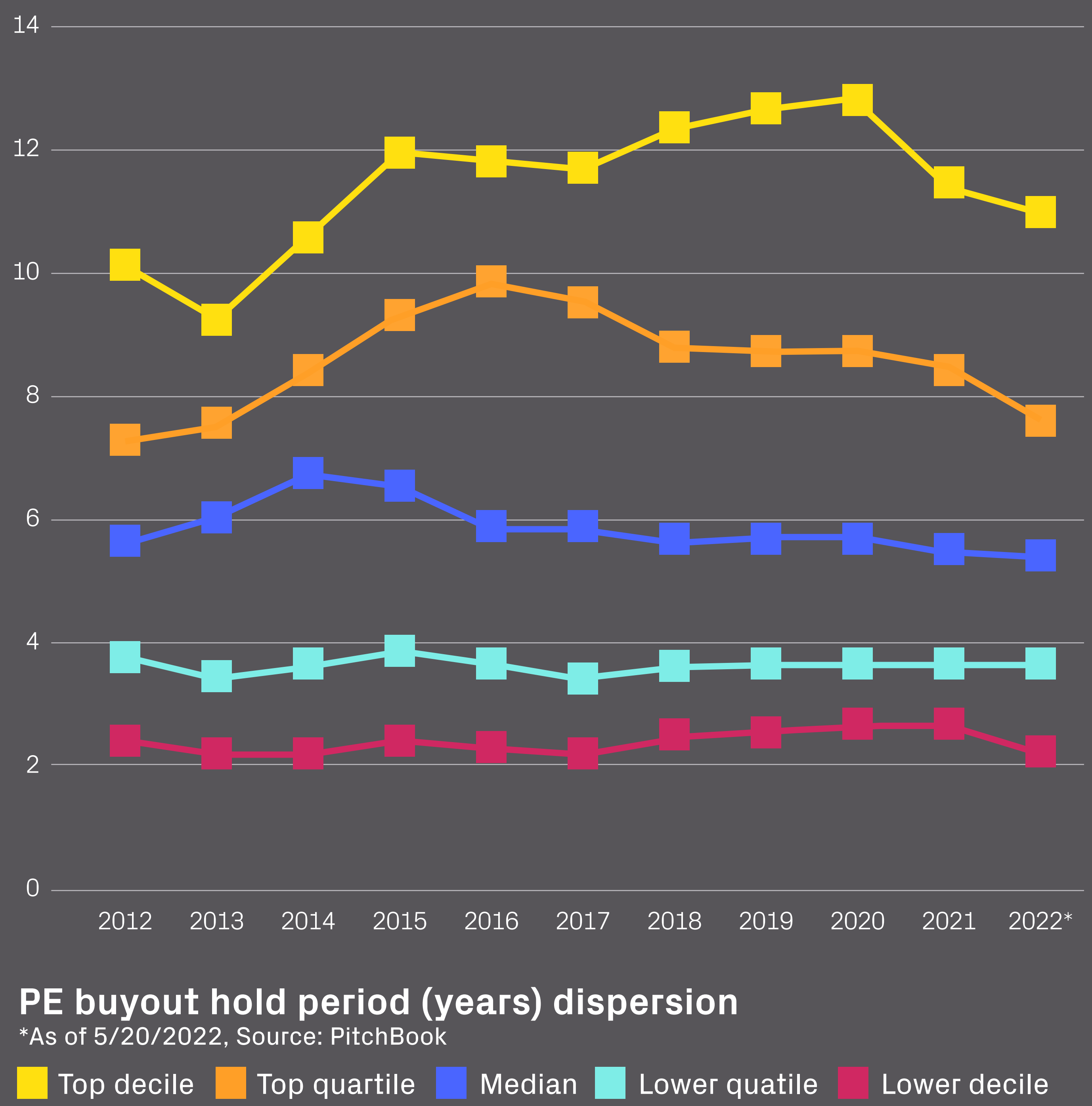
Median and average time (months) between PE deal announcement and completion

*As of 5/20/2022, Source: PitchBook

Median Average

Median hold times have slightly shortened from 5.3 years to 5.2 years – potentially signaling more sell-side urgency.





PE buyout hold period (years) dispersion
*As of 5/20/2022, Source: PitchBook

Looking ahead

After the record-breaking 2021, the easing down in Q1 2022 came as no surprise. Investors were exhausted, as were their lawyers, accountants, bankers, and advisors. Stories abounded about ‘the ones that got away’, or good deals that would have been done in a typical year but were passed over because something even better came along. Remarkably, opportunity exceeded capacity.

More braking factors kicked in by Q2 2022, as broader economic developments clouded the horizon. The first interest rate rise is expected to be the first of several heading into 2023. Consequently, deal flow has slowed since March 2022, when 1,158 PE deals were completed globally, valued at a combined $197.7 billion. By April, this had declined to 963 deals worth just $104.4 billion in aggregate. Given the typical deal timeline, this could be related to Russia’s invasion of Ukraine and the ensuing war, which began in late February.

May 2022 saw both deal counts and value continue to fall, with just 529 PE deals completed globally by May 20, totaling $58.8 billion. With just two datapoints, it is difficult to extrapolate future deal activity, but the 2021 frenzy is clearly over. Thanks to big fundraising hauls over the past two years, PE investors still have plenty of dry powder to work with, but it appears that the best opportunities were prioritized in 2021, especially in H2. Going forward, PE investors should see lower EBITDA valuations – at least relative to recent levels – paired with escalating leverage costs for future portfolio companies. The bigger mystery, which is reflected in both interest rate increases and valuation drops, is the overall economic uncertainty. This will weigh on investors throughout 2022 and beyond.

Methodology

M&A is defined as the substantive transfer of control or ownership. We track only completed control transactions. Eligible transaction types include control acquisitions, leveraged buyouts (including asset acquisitions), corporate divestitures, corporate asset purchases, reverse mergers, spinoffs, and asset divestitures.

- Debt restructuring or any other liquidity, self-tenders (in which a company undertakes an offer for a typically limited number of its own shares to ward off a hostile takeover) or internal reorganizations are not included.
- Announced, rumored, or canceled deals are not included.
- Aggregate transaction value is not extrapolated using known deal values, unless otherwise noted as estimated.

Capital invested is defined as the total amount of equity and debt used in the transaction. PitchBook's total capital invested figures include deal amounts that were not collected by PitchBook but have been extrapolated using a multidimensional estimation matrix. Some datasets will include these extrapolated numbers, while others will be compiled using only data collected directly by PitchBook; this explains any potential discrepancies.

Due to the nature of private market data, information often does not become available until well after a transaction takes place. To provide the most accurate data possible, we estimate how much of this new information will become available in the next quarter by calculating the average percentage change in deal flow from the first to second reporting cycle over the trailing 24 months. We then add this estimate to the reported figure for the most recent quarter. Both the original reported figure and the estimated figure are provided for your reference.

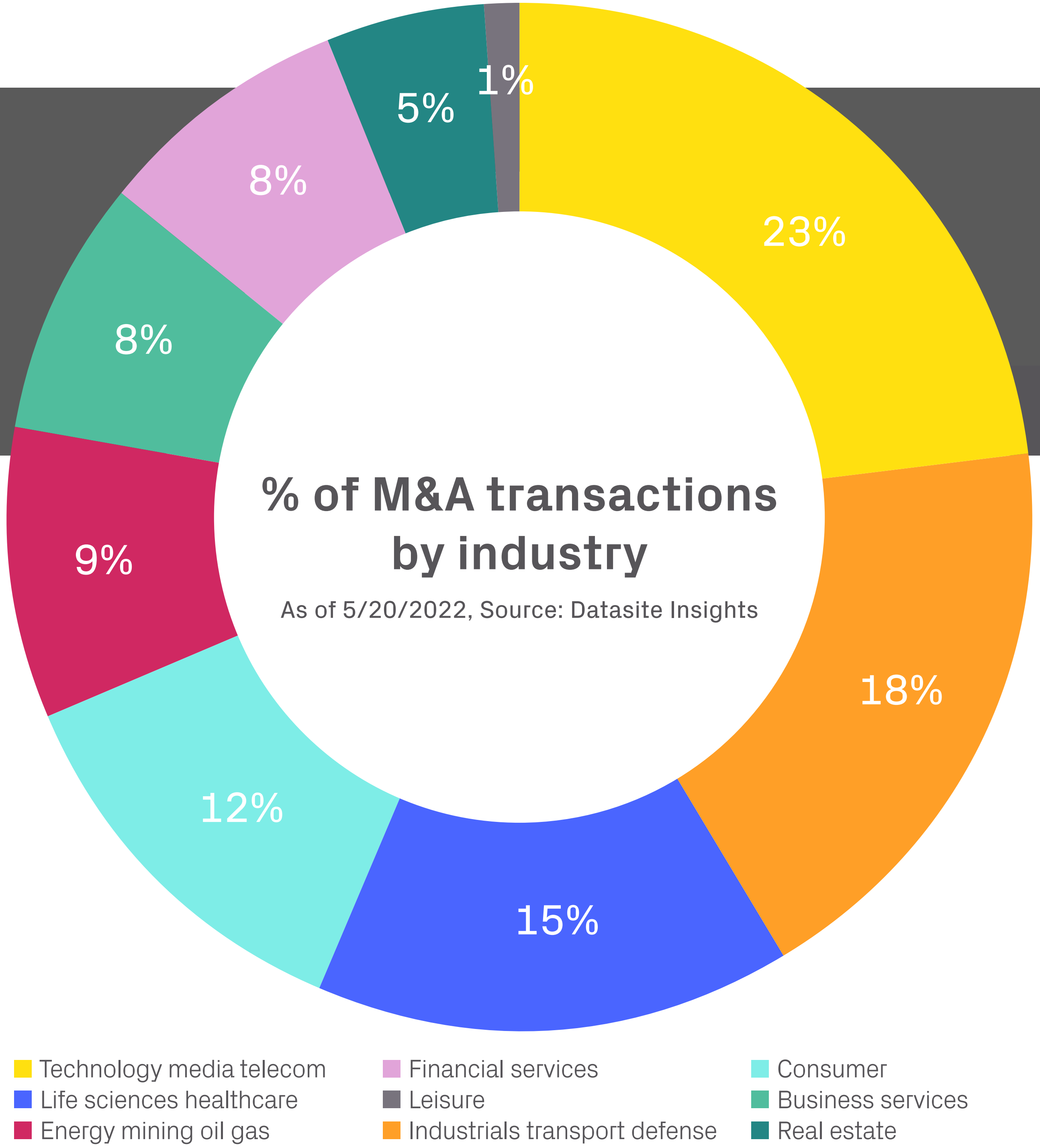
As the tide turns, what's next? The Datasite view

It's clear enough that the market is leaving one weather system for another. The big question is what do those clouds mean? Some do look ominous: inflation, high interest rates, layoffs, and the ongoing war in Ukraine. Yet their ultimate effect on deal activity is still far from certain. To make any kind of prediction, we need to look at the impact so far in 2022.

What we've seen: January to May 2022

Globally, announced deal flow has slowed since March 2022, but behind the scenes, deal activity remains strong. The number of Datasite-hosted deals has increased 10% YoY. As the M&A market becomes more challenging, it is likely that dealmakers are turning to platforms that offer the greatest agility and support. In fact, according to a Datasite survey of 500+ dealmakers, the majority believe that a greater focus on technology to boost productivity will be a result of the Great Resignation.

TMT deal activity continues to soar. This sector accounts for the most transactions by industry and represents 23% of Datasite's M&A transactions. The surge began with the pandemic, so it will be interesting to track its course through the aftermath. With tech companies making layoffs at the highest rate since 2020, how will this affect transaction volumes as both private and public companies look to conserve their cash?



Deal sizes are also down. The average size of a deal made in Datasite is around 12% smaller than in 2022. Again, this is no surprise, with a more conservative market shying away from mammoth deals. What we're seeing now is lower-middle-market activity.

The average length of an M&A deal made in Datasite has risen by eight days. This is around 5% slower than the blazing speeds seen in 2021. The brakes went on hardest in February 2022, when Russia invaded Ukraine, highlighting the new 'wait and see' mood. Overall, dealmakers are treading more carefully in this more disrupted landscape.

Following a record-shattering year, the change in pace is certainly felt by all – and even, arguably, appreciated. Dealmakers largely see 2021 as a phenomenon – remarkable, but a freak event rather than the start of a trend. In other words, the apparent slowdown we are seeing now can be explained by the market settling down to a new normal.

Nevertheless, companies face increasing pressure to accelerate deals and generate results in the face of fresh obstacles such as tougher regulation, supply chain issues, and labor shortages. Ironically, such headwinds are catalysts for stronger dealmaking practices. Embarking on the second half of 2022, dealmakers are taking advantage of the slowdown as a breathing space in which to reflect on and rethink strategies. In an uncertain market, the key to success is tight deal pipeline management.

Three keys to pipeline success in an uncertain market

1 Build strong relationships

55% of dealmakers rely on direct or self-sourced deals.[1] This makes it especially vital to have strong pipeline management practices.

Direct channels are your treasure map, so take care of them. Create a central repository of all your own contacts. Nothing is worse than sifting multiple year-old emails for a name or key information. Whenever you meet someone, whether for the first time or tenth, make notes of personal details and conversation specifics. Then set calendar reminders to check in with your contacts, using your notes to create a strong pretext for reconnecting.

For example:

- Three months have passed. That's a good time gap to justify a courtesy call.
- Maybe their child was about to graduate. Time to offer your congratulations?
- You learned that they are a Rafael Nadal fan. You could ask if they went to the French Open.

2 Use better tools

75% of dealmakers manage their pipelines in Excel.[1] Without purpose-built tools, strategies get lost in spreadsheets.

Huge amounts of energy are still going to waste as a result of dealmakers sticking with outdated pipeline management tools – namely, spreadsheets and emails. Work gets duplicated. Version control runs out of control. Messages get lost, and opportunities get missed. It doesn't just add to workload – it invites much more risk into the process.

That's why more PE firms are ditching yesterday's tools for new ones made for the task. These enable the airtight pipeline management needed to juggle multiple transactions,

Ask your deal team these questions:

- Do your tools work, or do the workarounds make them seem to work?
- What pain points do you still have with your current solution, even with the workarounds?
- Is everything in one central, secure place?

3 Serial acquirers demand serious considerations

86% of dealmakers typically do bolt-on or tuck-in acquisition strategies.[1] For these serial acquirers, a healthy pipeline is vital.

Do not sacrifice the health of favorable opportunities and long-term strategy for the sake of closing imminent deals. Understand the investment thesis for every acquisition, and prioritize. Will this build your market share or help you enter an adjacent vertical? Are there strong synergies?

Tomorrow's deals are just as important – that's why we talk about 'dealing in next'. Look ahead. Create repeatable playbooks for your deal teams – especially when voluntary turnover is high. If someone leaves, in what state does that leave your team? How are your pipeline meetings run, and can they be more efficient? If you create time savings for the juniors gathering the materials, that's extra time for due diligence and, ultimately, more deals.

With the right tools, you can amplify your team's abilities to manage deals at scale. When you remove data silos, everyone is looking at the same views of the data, and you have one source of truth. In a time of uncertainty, you can bring more certainty than you've ever had.

[1] Source: Datasite survey of 400+ M&A professionals, February 2022

By your side across the PE spectrum

Datasite offers more than just the world's most trusted data room. We've been a core feature of the M&A landscape for over half a century, supporting PE firms of every size. This historic legacy, combined with tomorrow's technology, gives PE dealmakers unrivalled confidence, whether it's sell-side or buy-side deals, fundraising, asset readiness, or IPOs.

Your PE deal never leaves the safety of the data room. Fundraise, acquire, and exit in one seamless process, with security and support at every step. It's not just dealmaking any longer; it's dealing in next.

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