Datasite®

Where deals are made

Into the Quaternary Period of Private Equity

Data provided by

PitchBook

Executive summary

Secondary buyouts (SBOs) are now everywhere you look. This trend is an inevitable consequence of the expanding PE universe, as ever more companies seek funding via this route — and are then sold on to other PE firms. As PE firms proliferate globally, so too will SBOs.

Once viewed with suspicion as distressed sales, SBOs nevertheless play a key role in the current market. Not only do they provide exit ramps for existing investors, but they are an outlet for the PE industry's war chest of dry powder. Current PE portfolio companies provide a steady source of deals. Meanwhile, on the other end — because holding periods are so important to PE fund returns — sellers can return capital to their LPs by having other PE firms buy their existing portfolio companies. This makes SBOs a useful arrangement for both buyers and sellers, and one that helps keep the PE machine humming along.

In fact, PE firms are increasingly playing pass-the-parcel with certain companies, selling them on in tertiary and even quaternary buyouts. Three or four rounds of PE funding is becoming less uncommon, as more specialist investors move in to extract as much value from companies as possible. Among other things, that means the due diligence process becomes critical for companies undergoing their third or fourth consecutive buyout. Prospective investors need to use the due diligence stage to find new value to unlock.

SBOs are only one source of deal flow in today's dynamic PE market. The "buy-and-build" model of acquiring a platform and adding on to it multiple times has become a reliable driver of value creation. That's why add-on figures have ballooned as much as they have: Investors have identified fragmented but scalable industries that can benefit from deliberate consolidation. In a similar vein, PE sponsors have proven themselves capable of taking companies private and unlocking unseen value in a short amount of time. Global take-private deal activity hit a record in 2022, despite rich stock markets around the world. In particular, take-privates allow sponsors to move large amounts of capital in a single transaction while finding attractive premiums to woo over public shareholders. In some cases, those take-privates are sold to other PE sponsors after three-to-five years, where further value can be unlocked.

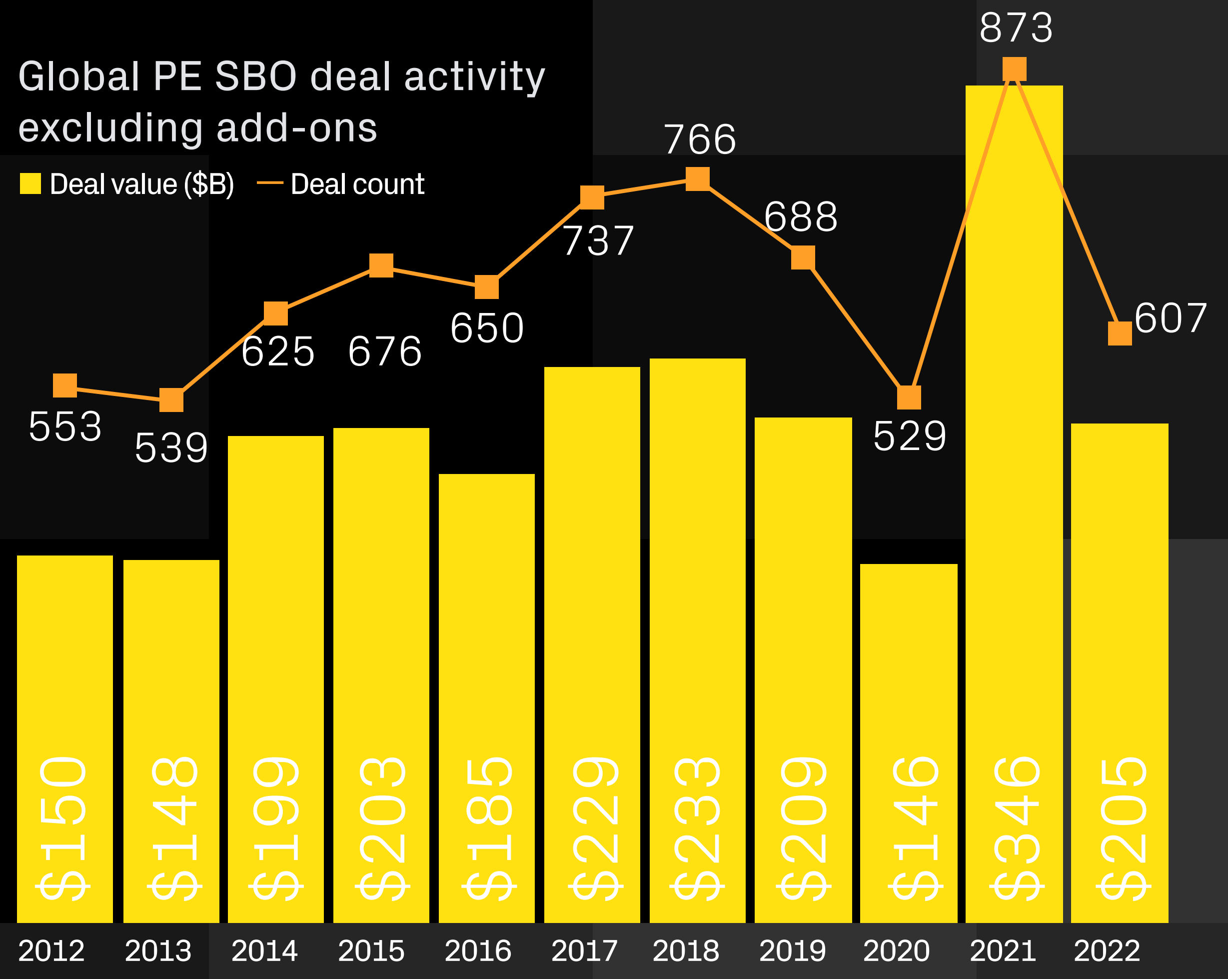
Passing parcels

For the past decade, the global PE market has averaged around 500 SBOs per year. Then came the 2021 goldrush, when buy-side and sell-side demand converged to deliver 873 transactions, totaling almost $350 billion in value. But in the following year both volume and value returned to their historical means.

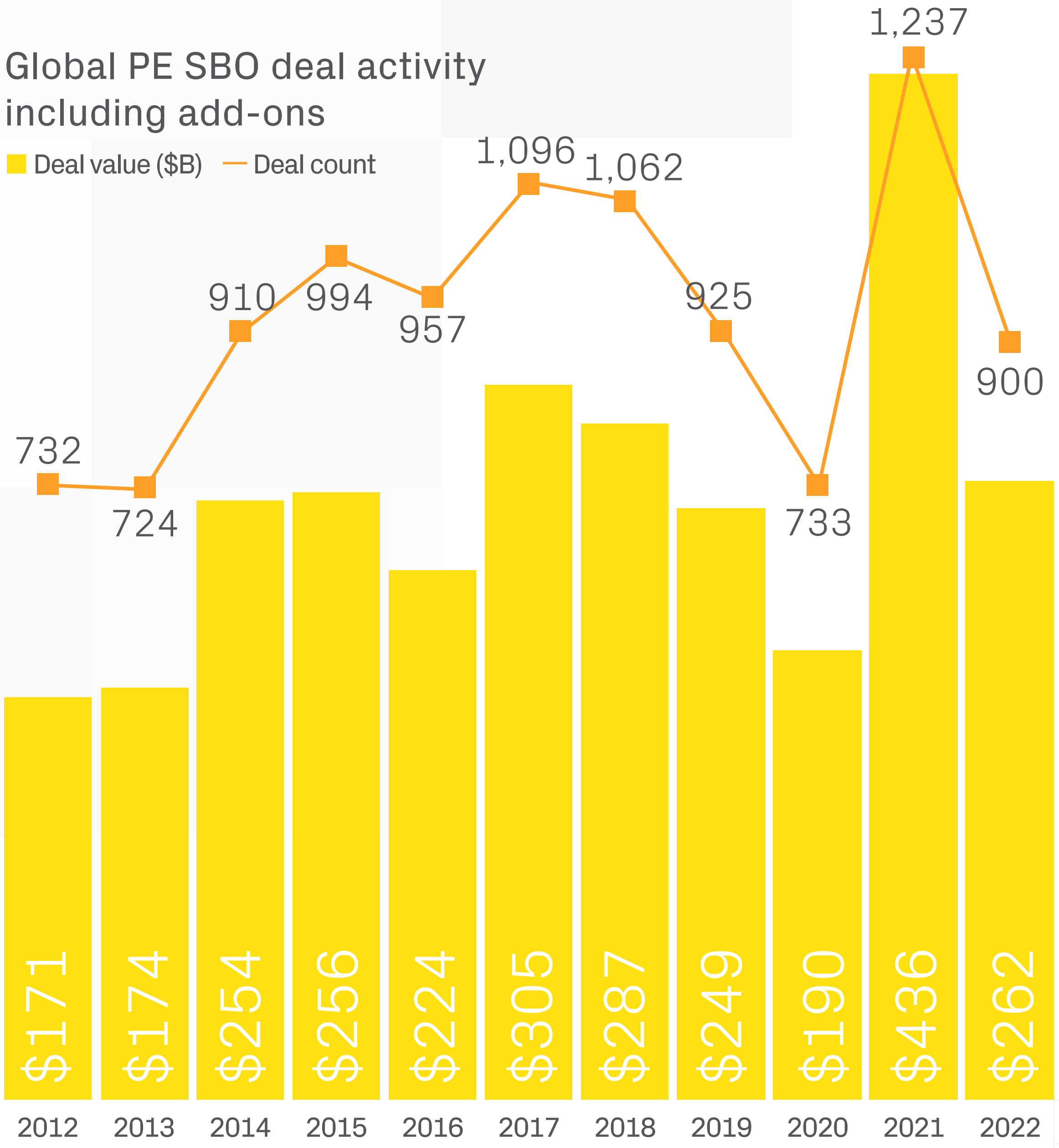
Meanwhile a popular investor strategy — though often an unnoticed one — is using SBOs as add-ons (meaning, PE-backed companies acquiring other PE-backed companies). When you include those SBO add-ons, the 873 transactions in 2021 rise to 1,237. Such companies benefit from the "one careful owner" appeal — for by being already in PE ownership, they're typically more efficient for another PE-backed company to acquire, and need lighter due diligence. This benefit can offset a higher price or the loss of the lowest-hanging fruit.

SBOs tend to be much bigger than normal buyouts. In 2022, a typical year, the median SBO deal size reached $417.0 million compared to a $100.0 million median for all buyout sizes. Part of that difference is due to PE-led growth under the previous owner, which increases the deal size by default. On the margins, SBO pricing is also more sophisticated and negotiation-heavy, with PE sellers extracting as much value as possible from their buy-side counterparts.

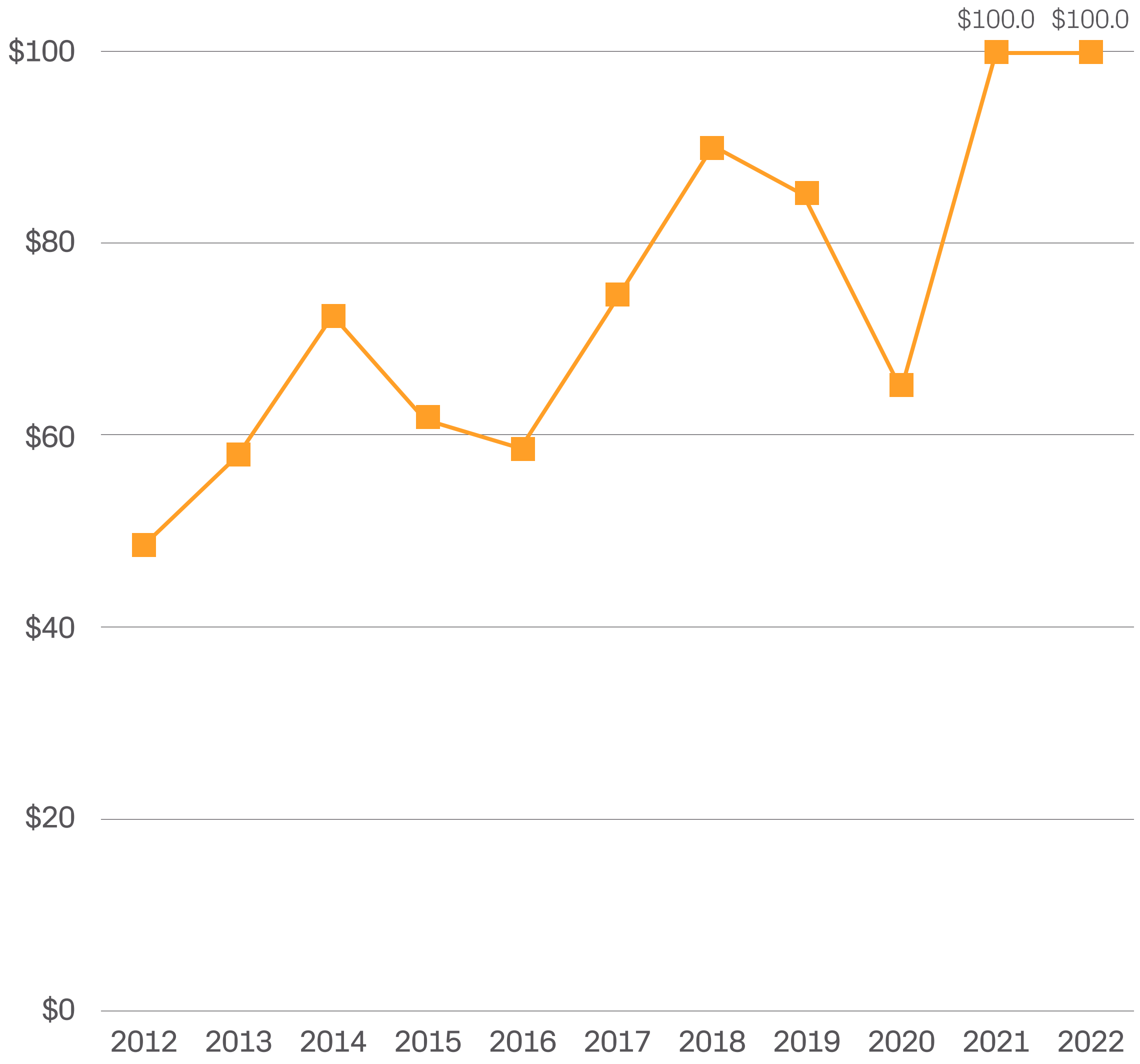
Although toppled from their 2021 peak, exit deal values in general remain robust and well above pre-pandemic levels. Furthermore, the gap between SBO and non-SBO exit values has widened, with the former now around 60% bigger.



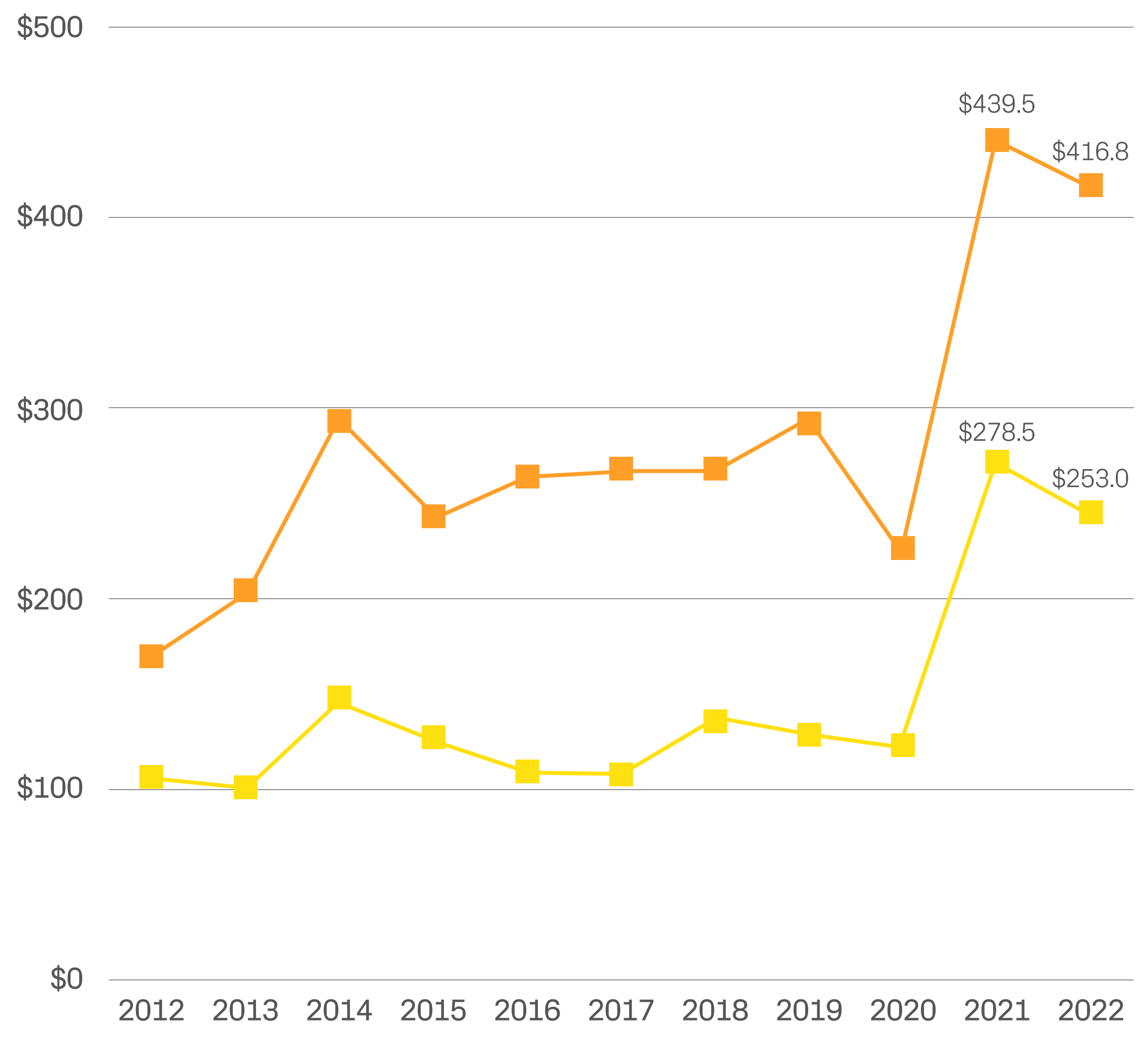
Global PE SBO deal activity including add-ons



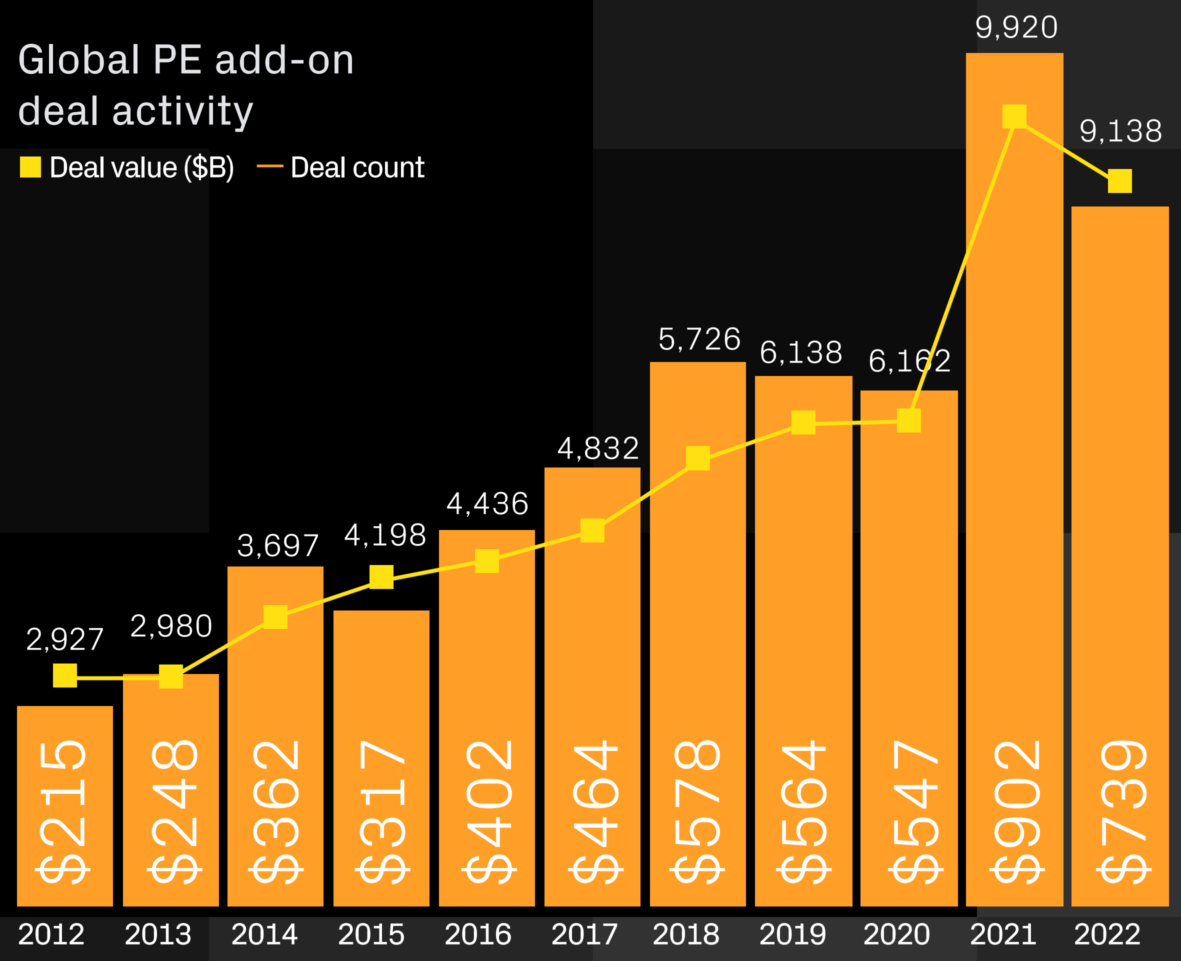
Global median leveraged buyout deal size ($M)

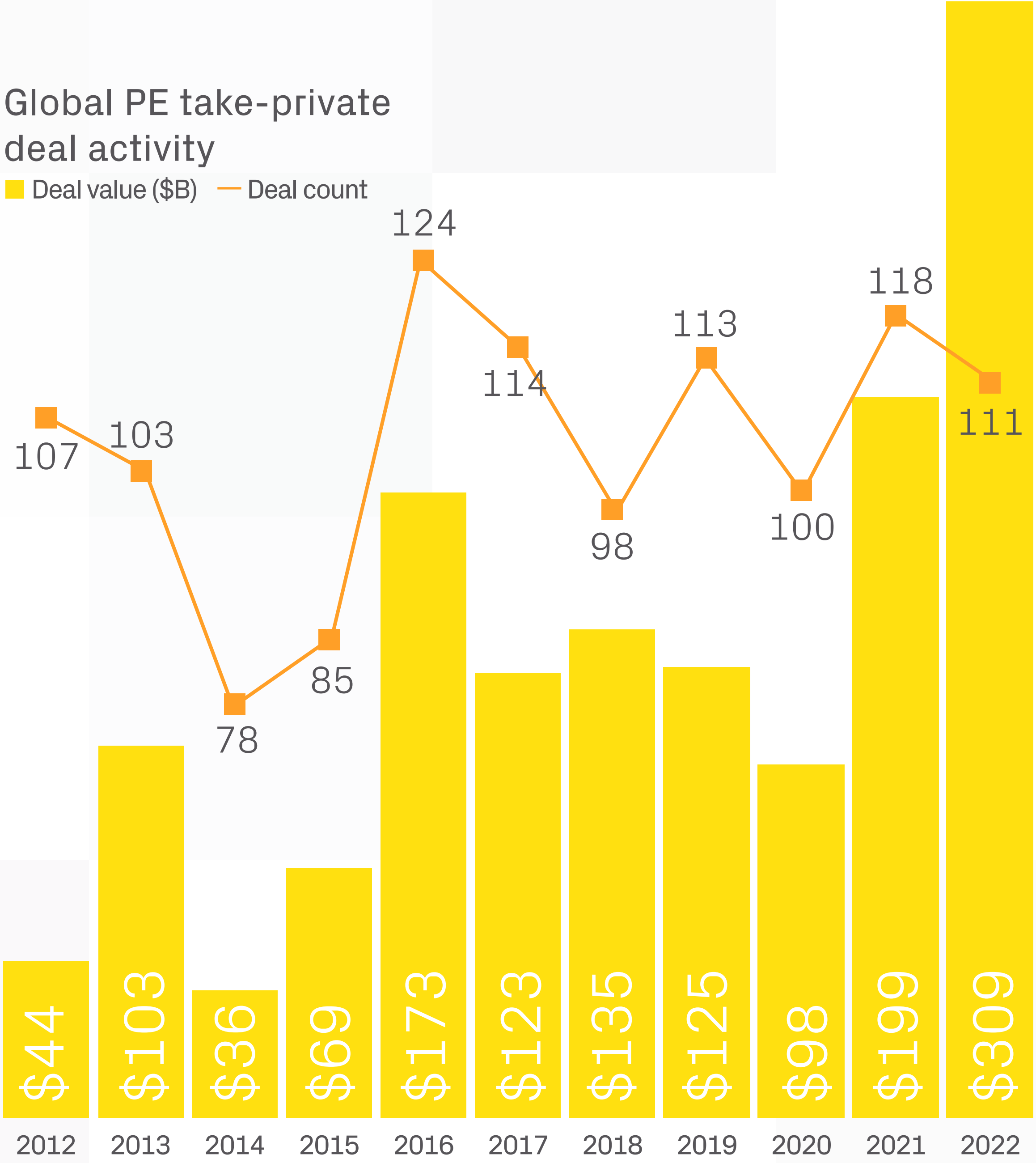


Global median SBO deal size vs median non-SBO exit size ($M)



Global PE add-on deal activity




Global PE take-private deal activity
Deal value ($B)
Deal count
107
103
78
85
124
114
98
113
100
118
111
$44
$103
$36
$69
$173
$123
$135
$125
$98
$199
$309
2012
2013
2014
2015
2016
2017
2018
2019
2020
2021
2022

Spotlight on tertiary and quaternary buyouts

Today, it's not unusual to see a company go through three or four rounds of PE ownership. Just a decade ago, tertiary buyouts were rare, with typically fewer than 100 per year; now, the figure is nearer 200.

Some find the idea of even a secondary buyout confusing. After all, if a company has already spent years under PE ownership — with all the associated changes and presumed growth — what would motivate the next buyer? That question only compounds when speaking of companies being bought and sold three or four times.

The answers vary. Some companies are simply better off under PE control, especially in steady sectors such as B2B, where there is nearly always room to grow. For investors, there's the bonus of company stability. Past PitchBook research suggests lower bankruptcy rates among secondary buyouts when compared to primary buyouts. Furthermore, PE-backed companies can grow into different market sizes and industry segments. A company's first PE buyer may not have been its ideal fit. Many SBOs are conducted by more specialized PE buyers, who can offer the potential to unlock more value via a different team of investors.

Like deal flow in general, tertiary and quaternary deals spiked in 2021. The year saw 293 companies being bought by a third consecutive PE firm, while a further 81 companies were bought by their fourth. The large majority of SBOs are happening in more developed PE markets such as the US and Europe, where there are more sponsors, more capital available, and more demand for sponsor-to-sponsor deals.

Key drivers of secondary buyouts

Sector appropriateness: Certain companies in certain industries are better off under PE sponsorship

Increased specialization of PE firms, which can find more value than generalized firms

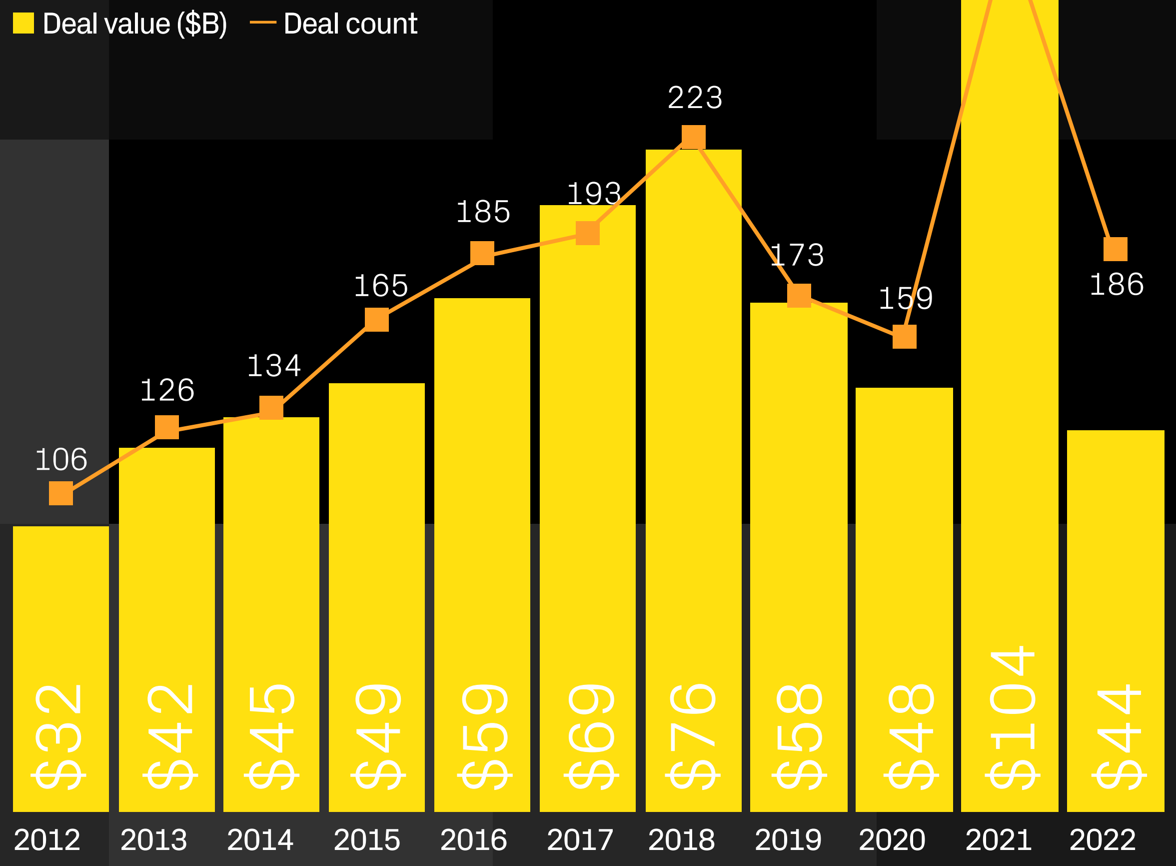
Proliferation, sophistication, and size of PE market

Quicker holding periods for sell-side investors, who can return capital to LPs and maintain healthy returns

Lower bankruptcy rates, offsetting lack of low-hanging fruit and providing better risk-adjusted returns in down markets

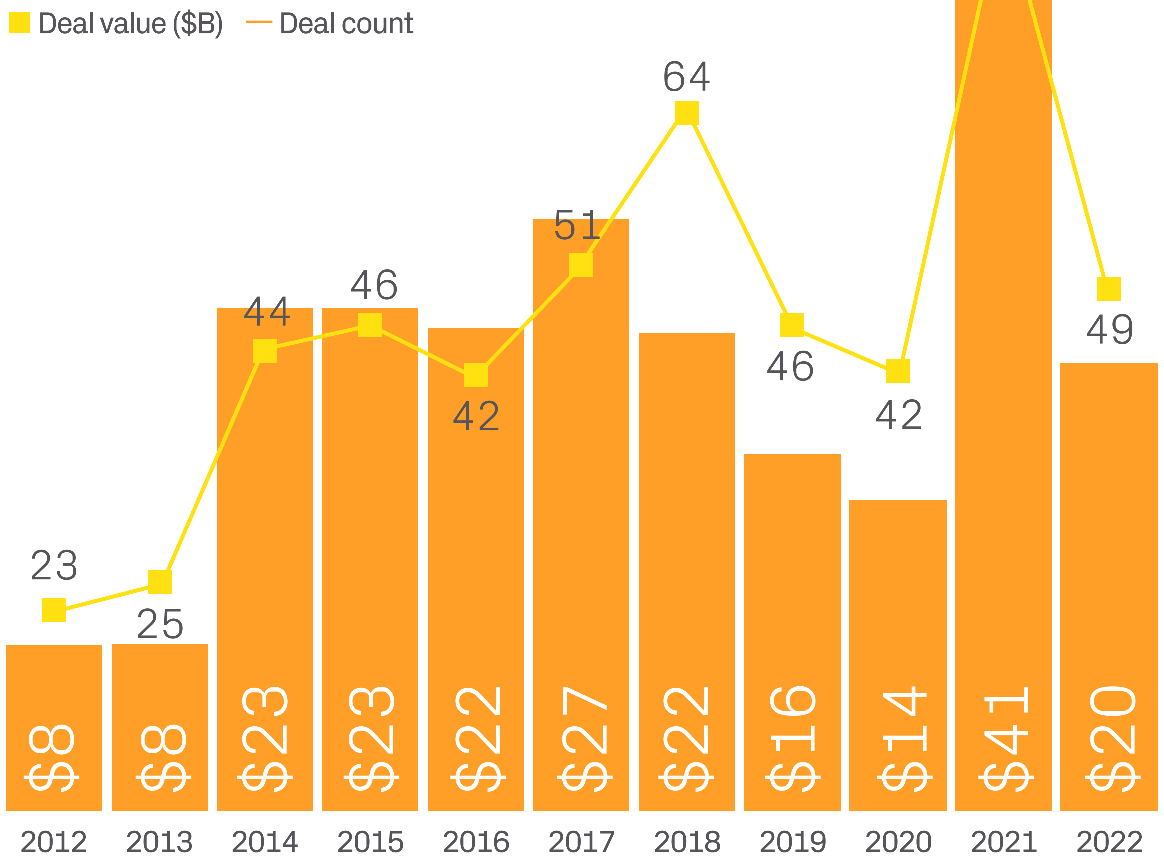
Dry powder levels are one reason median SBO deal sizes and exit sizes have gone up over time. In addition, SBO-appropriate companies tend to be larger thanks to value creation initiatives from previous PE sponsors.

Global PE tertiary deal activity

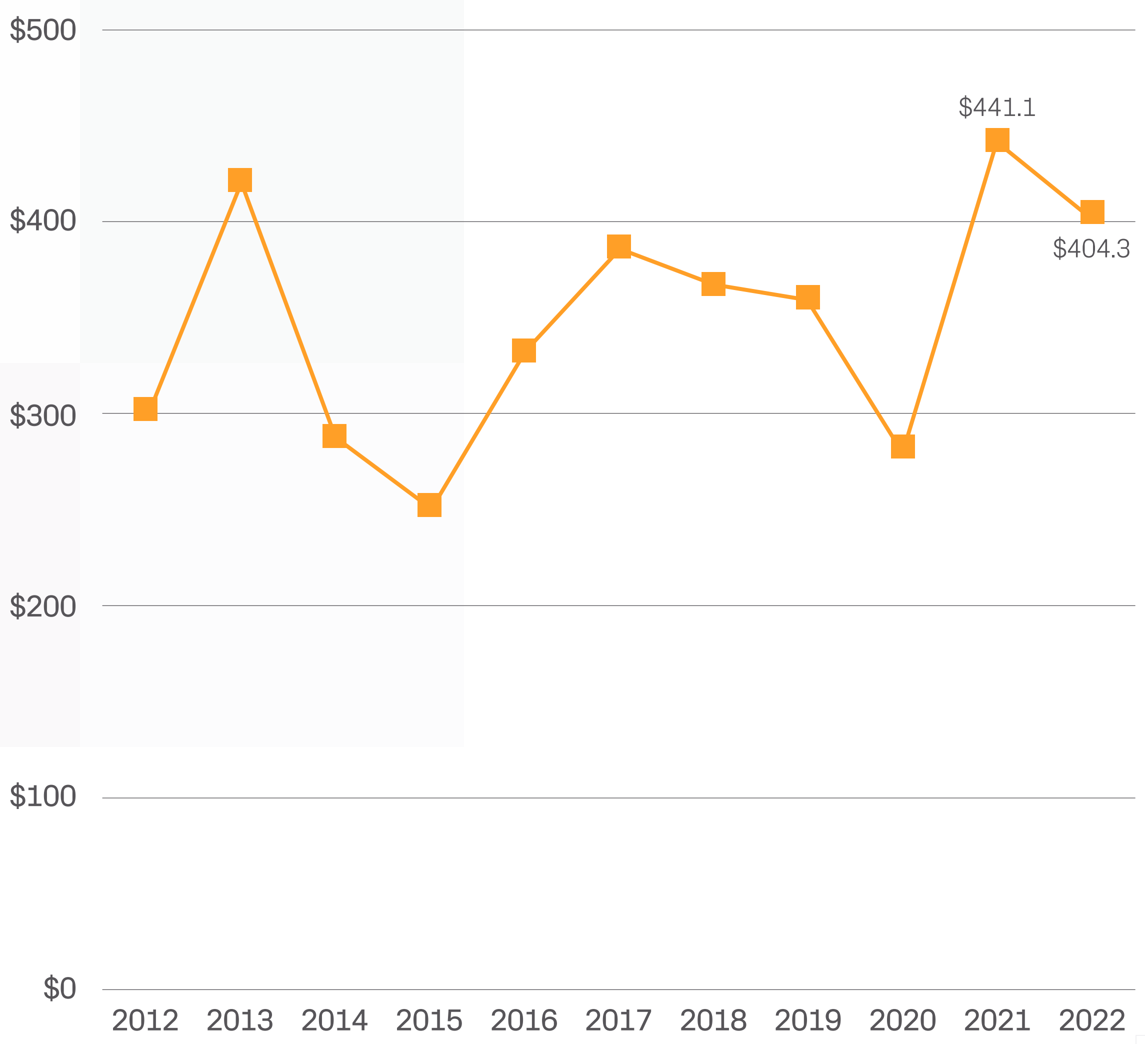


It's not uncommon for an initial PE sponsor to acquire a lower-middle-market company and transform it into an upper-middle-market one. At the same time, sponsors are careful to leave more room for growth for future buyers, whether they're financial or strategic buyers, to entice them to pay up for their growing portfolio companies.

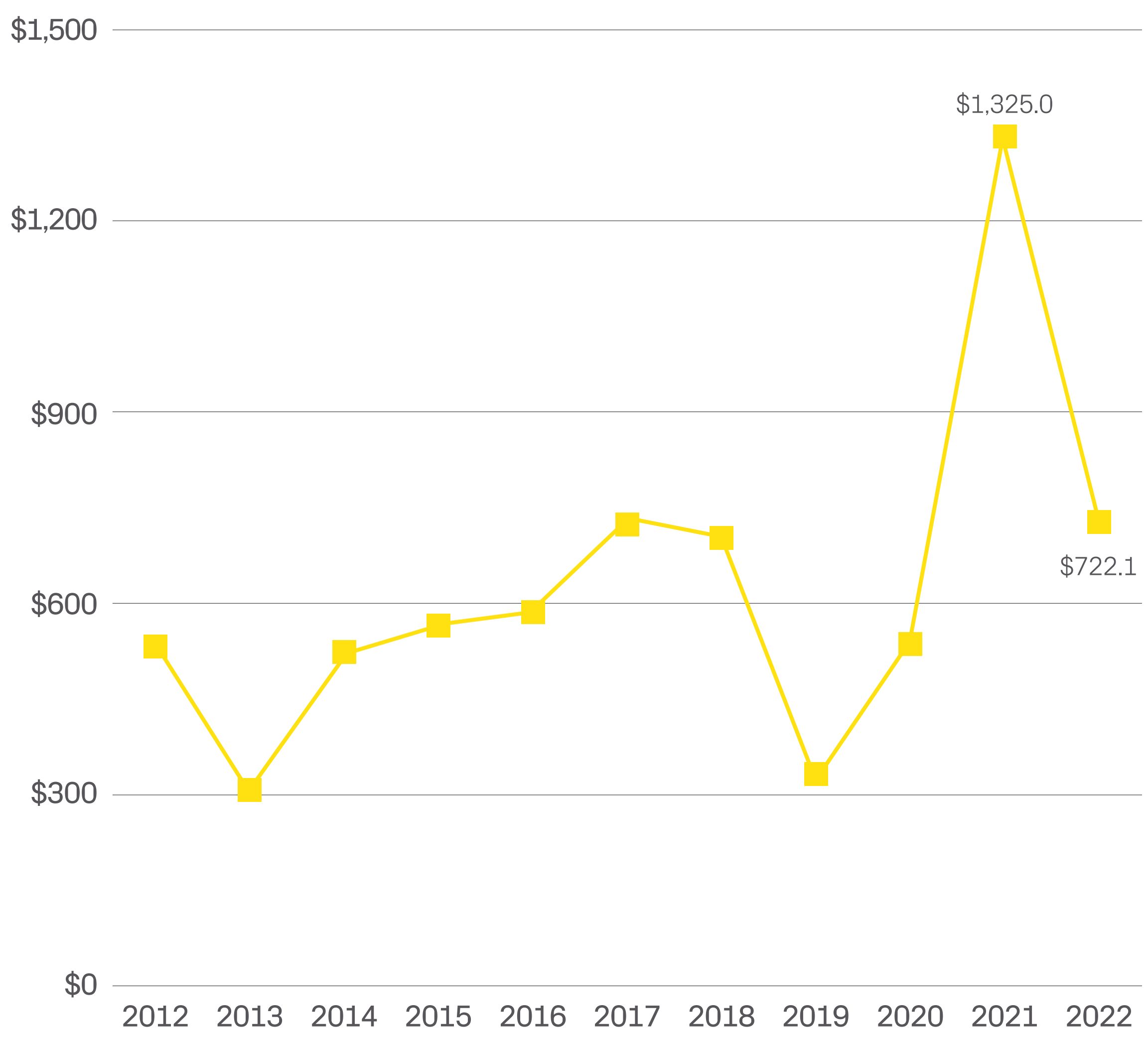
Global PE quaternary deal activity



Global PE tertiary deal activity — median buyout size ($M)



Global median quaternary buyout deal size ($M)*



*All values are based on non-normative samples due to small data counts each year.

Looking ahead

Secondary buyouts have always been with us. But there are signs that the role they play is evolving. Once virtually a by-word for a "fire sale," they appear to be playing an increasingly important role. Several years of high PE dry powder, coupled with the proliferation of PE firms globally, has naturally increased the number of SBOs — and in the process may be helping to reinvent them.

SBOs already provide a viable alternative if IPO windows close and corporate buy-side demand wanes. But there are further reasons to suppose that this type of deal will grow in importance. The biggest is that PE continues to specialize. Every year, more PE firms are formed by dealmakers looking to make their marks under their own names. They bring with them certain skillsets with which to carve their own unique routes to success.

Even more crucially for the industry, these fledgling firms have the motivation to become specialized operators, targeting niche industries and companies. This is music to the ears of LPs; institutional demand for specialization is a major evolutionary driver of the PE industry. Such specialization will play an increasingly key role in SBOs, as buyers continue to find ways to unlock value that eluded the previous owners.

Resilient, relentless, reinventing

The Datasite view on PE

It's been a turbulent, even tempestuous year for M&A. But PE dealmakers have proved more than capable of riding those choppy seas, changing tack to seek out the calmer waters ahead. Strategies have been recalibrated; playbooks have been optimized. And — judging by our survey of 600+ dealmakers — key habits and characteristics are continuing to evolve.

Here's how the shift is playing out:

54% of PE dealmakers work on a mix of buy- and sell-side deals

- Dealmakers are shifting away from binary buy- or sell-side role definitions.
- They see diversification of deal types as the way forward as PE opportunities proliferate.
- The trend continues to develop, suggested by similar responses in our 2020 and 2021 corporate development surveys.
- PE dealmakers are spending roughly equal time on buy-side (30%) and sell-side (30%).
- They are spending 26% of their time on fundraising and LP reporting.
- Dealmakers are devoting the remainder of their time (14%) on other tasks (such as invoicing, researching, and networking).

PE dealmakers work on the widest range of deal types - an average of 3.6 transaction types in a given year

- Momentum is critical in PE, with multiple firms chasing the same opportunities.
- 2023 has dawned with significant investment pressures, alongside the need to deploy dry powder reserves.
- PE is doing well to weather the macroeconomic conditions — including interest rate hikes, global supply chain issues, and increased ESG scrutiny — and is proving both resilient and relentless.

PE dealmakers are paying for M&A tools

- A significant proportion have these tools paid for either by their PE firm or their department:
  - 76% pay for market data
  - 70% pay for pipeline management tools
  - 72% pay for a buy-side data room
  - 77% pay for a sell-side data room
- Given their dynamic deal flow, PE firms need purpose-built M&A tools. It's no surprise that many more are now willing to "pay to play." In so doing, they can increase efficiencies, collaborate faster and more easily, and automate their workflows.

Optimizing for opportunity: Three simple hacks

1 Central platform = streamlined workflow

How do you give your team the smoothest, fastest runway? Make everything happen in one place. Remove the countless everyday frictions that squander time and energy, causing delays that may, in turn, cost you deals. Here are some simple ways to do that:

- Create a central repository for your targets. Instantly reclaim all those hours you spent searching through old emails.
- Equip your whole team with the tools to manage workstream tasks — tools such as AI categorization for content, automated redaction, and watermarking. Efficiencies accumulate, potentially saving you weeks.
- Run due diligence your way, using a data room suited to both buy- and sell-side.

2 Perfect your pipeline playbook

Your pipeline is your lifeline. Take it seriously. End the chaos of disparate spreadsheets and channel all your opportunities in one dedicated space. Central control means you can have:

- One dynamic dashboard on which to compare and prioritize potential targets, drill down on data, and report weekly.
- All contacts, documents, activities, and tasks readily accessible — and linked to their relevant targets.
- A trusted data room standing by, so you can bounce into due diligence when opportunity strikes.

3 The best security is easy

You need to be able to store sensitive documents with confidence — but without complex procedures that create vulnerabilities. Facilitate access for the entire deal team with advanced permissions controls, while blocking unwanted users.

Based on our survey of 600+ dealmakers, 222 PE dealmakers responded indicating that a week's worth of due diligence costs around $104,000.

Giving PE the momentum it needs

Datasite has been the essential PE partner for over half a century, supporting the top 20 global PE firms. By removing the doubts that put a brake on dealmaking, and eliminating the friction of collaboration, Datasite's combined technology and service let the PE engine run at full capacity.

Every transaction is smoother. Deals become faster and easier. Your entire workstream becomes one end-to-end process that never leaves the safety of the data room. On one platform you can fundraise, acquire, exit, and repeat — with the same support and security at every level. It's the key to remaining ultra-competitive in a rapidly evolving PE market.

Power your entire PE lifecycle with Datasite Cloud™

Maximize dealmaking, portfolio company initiatives, and higher investor returns. Datasite Cloud is the all-purpose launchpad for PE professionals to complete transactions with ease.

Fundraising	Acquisition	Restructuring	File sharing	Exit preparation	Deal marketing	Value capture
Raise funds with confidence. You control the process.	Source and secure your next target with tools made for the buy-side.	Focus on the best deal with easy-yet-secure file sharing among lenders and deal team.	Support improvement initiatives with ongoing portfolio company and deal team file sharing.	Bring your deal to market faster with AI-enabled preparation.	Cultivate the most interested buyers with automated outreach and analytics.	Spot high-interest buyers for a successful exit, with the help of advanced Q&A and analytics.

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