PRIVATE EQUITY BUYERS SEEKING FOUNDER-OWNED COMPANIES

And Hungrier Than Ever

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Companies without any institutional (VC, PE) ownership are often referred to as "non-backed" in the M&A marketplace, particularly for PE Buyers. These types of companies are typically led by their founders or inherited through family generational planning. Based on our research, this Founder-owned company type has played a significant role in PE deal activity, most recently accounting for more than 52% of the middle-market PE buyouts in 2023. Importantly, that share of the M&A market has risen from 47.5% in 2021 and is expected to climb higher over the next few years.

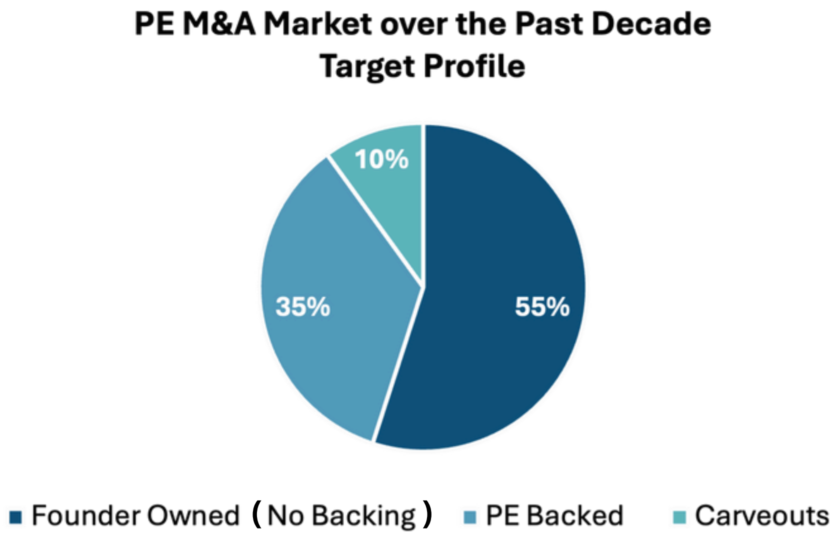
The recent increase in M&A transactions involving "non-backed" companies indicates a rebound from the 2011-2020 cycle in which larger scale and sponsor-backed transactions were more in favor. With this rebound comes a wider market caution; amid current macroeconomic conditions, many sellers, including financial sponsors and potential PE platform investments, are deferring deals as they await a more favorable interest rate climate. Non-backed sellers, often constrained by higher financing costs or demographic factors such as Founder retirement issues, may find themselves less able to postpone or select the optimal exit strategy timing.

At Greenwich Capital Group (GCG) we have made a career over the past 10 years focusing on and specializing in helping founder-led companies optimize their liquidity strategy. At GCG we understand the nuances of family relationships, appreciate the fragile histories of our clients, and value the transition of the Founders' "legacy" to the right steward, not just the highest-paying entity. Unlike their "backed" counterparts, which might wait for better market conditions, non-backed companies are often pushed towards selling. Push rationales might include a) immediate competitive or financial pressures, or b) personal circumstances (divorce, health, business partner separation). These human issues highlight a distinct dynamic in the lower half of the middle market M&A transaction landscape. We hope Founder-led companies will give us the chance to advise you on this unique milestone transition and liquidity transaction.

FOUNDER OWNED: THE LION'S SHARE

Non-backed companies have historically represented the largest portion of the US PE M&A transaction activity over the past decade. Founder-owned companies have accounted for 55% of the total number of M&A transactions since 2013. In large part, these companies represent businesses that are still in the hands of the Founders, employees (ESOPs), or families that have self-funded their growth. The non-backed share of the PE M&A pie had been on the downswing from 2011 to 2020 but has seen a resurgence from 47.5% in 2021 to 52% share in 2023.

The second largest segment of the Middle Market PE M&A pie over the past 10 years has been smaller PE-backed companies. There are at least 1,000 Lower Middle Market (LMM) PE firms in the US targeting control transactions of companies with $3mm - $10mm of EBITDA. The LMM's goal is to organically grow or buy-and-build the platform acquisition into $20mm + of LTM EBITDA. The LMM will then sell their share (with the Founder or not) to a larger Middle Market (MM) PE firm for a higher LTM EBITDA multiple (than they paid) multiplied by an EBITDA base 3-5 x the base number the LLM bought in at. The smaller PE-backed owner share of the PE M&A pie over the past 10 years was 35%.



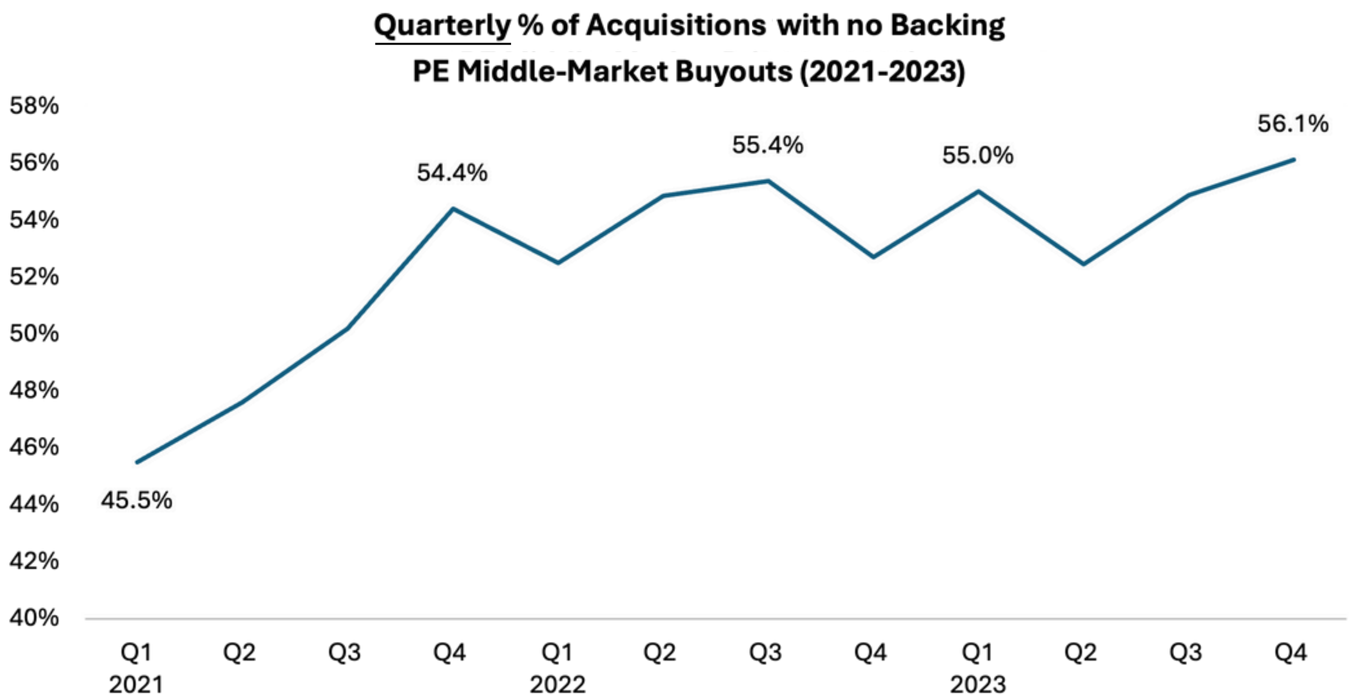
The smallest piece of the PE M&A pie is the Carveout piece at 10% of total transactions over the past decade. We would expect this segment of the market to expand over time, underscoring the role of carveouts as a vital segment within the PE deal universe – particularly in the current market where there is a wide bid-ask spread. We have seen certain Middle Market PE shops develop a focused expertise on this form of transaction including: Architect Equity, Brynwood Partners, Centre Lane Partners, KPS Capital Partners, and Pacific Avenue Capital Partners. Carveouts offer strategic sellers a unique opportunity to generate cash and enhance their strategic flexibility. This event can be crucial to the seller for paying down debt or reallocating capital towards more promising opportunities. Sellers tend to be hesitant to offload noncore assets into more volatile markets. These transactions tend to be more complex due to the need for a Transition Services Agreement (TSA) spelling out the services and their costs that the Buyer will pay the Seller during the operating transition/onboarding period (up to a year), post-closing.

If price dislocation subsides and widens the buying pool to deals of various backing types, the proportion of non-backed/Founder-owned companies as a share of the total PE M&A transaction pool, would inevitably decrease - reversing the 3-year upward trend since 2021. Likewise, reduced interest rates and improved access to leverage could facilitate a market shift back toward larger PE deals.

On the other hand, in the event of economic uncertainty turning into a “mild” recession in 2025, there could be forced or pressured selling from various backing types. Consequently, the proportion of M&A transactions from non-backed companies could diminish.

RECENT FOUNDER M&A SHARE TRENDS

Since the beginning of 2021, there has been an upswing in the share of all PE deals represented by these non-backed companies. From a starting point of 45.5% in Q1 2021, this percentage has risen to 56.1% of all M&A transactions as of Q4 2023. However, this falls short of the Q1 2020 peak when non-backed companies reached 65.3% of all private equity buyouts, capping a nine-year upward trend. The COVID-19 pandemic caused PE interest in Founder companies to nosedive during that span, as Founders were generally less equipped and capitalized to absorb the financial shock from the universal health crisis.



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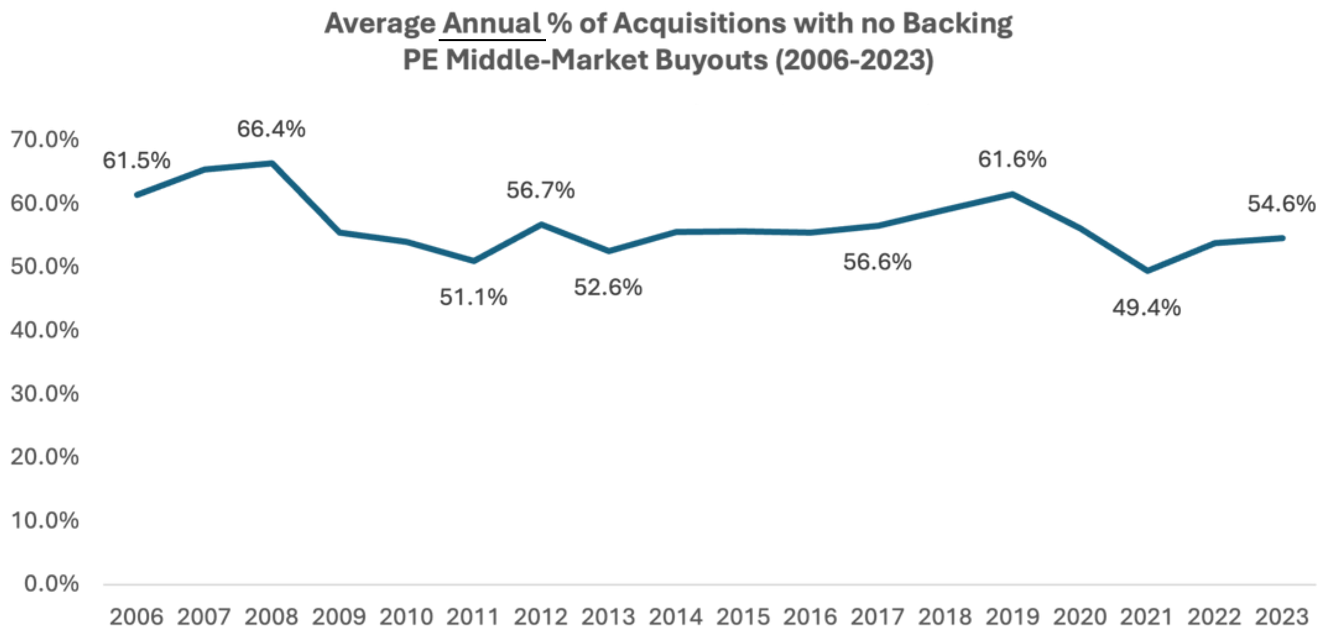
So, in many respects, the recent rise in non-backed companies, as a share of total M&A, is about regaining lost ground, but it also reflects the reluctance of other seller types – LMM PE and Carveouts. Those "backed" companies that can afford to wait out the current adverse interest-rate cycle are doing so.



We anticipate that GPs of middle market PE shops will continue to support and turn toward non-backed, Founder-owned companies to operate their value-add strategies in an efficient manner. Founder-owned businesses also tend to offer slightly cheaper purchase price multiples – a welcome offset to currently higher borrowing costs.

Furthermore, with US PE firms sitting on $1 trillion of dry powder that needs to be put to work in the next 5 years, balanced against a more limited universe of sellers, private equity buyers will be incentivized to actively seek non-backed, Founder-owned targets.

WHAT'S THE DIFFERENCE?

PE Buyers are currently placing a greater emphasis on operational improvements rather than relying solely on financial engineering to generate rates of return. When acquiring a Founder-owned business, there has been no outside capital previously injected to make long-term infrastructure investments. The other side is PE owners can start with a clean slate, free from baggage or conflicting cultures from prior owners.

Acquirers of Founder-owned businesses are entering these companies on the ground floor in terms of value creation opportunities, such as organically scaling or through a buy-and-build M&A strategy as well as improving cost efficiencies and return on labor investment.

There are some fundamental Human/Financial/Legal differences to typically evaluate when looking at acquiring a Founder-led company vs a PE-backed platform:

	Founder Owned	Private Equity Owned
Human		
Management	Family Member	Professional Executive
Labor	Friends and Family	Qualified Backgrounds
Open Positions	Two Hats	Key Positions Filled
Outsourcing	Whenever Possible	Insource Preference
Financial		
Financial Statements	Quickbooks – Reviewed	QOE – Audit
EBITDA Adjustments	Hide for Taxes	Expose for EV
Tax Structure	Minimize Income	Maximize EV
Working Capital	Unpredictable	Consistent
Balance Sheet	Conservative	Levered Returns
Legal		
Corporate Structure	LLC to C-Corp	C-Corp to S-Corp
Concentration Risk	Loyal Large Customer	Balance Through Growth
Lenders	Community Banks	Money Center Banks
Environmental	Kick the Can	Cleaned Up and Settled
Lawsuits	Avoid, Maybe a Partner	Aggressively Defend & Deny

Non-backed companies, typically family or Founder owned, tend to operate at the lower end of the middle market – i.e. Lower Middle Market. In general, we at GCG see more attractive purchase price multiples for PE Buyers in the Lower Middle Market (LMM). Most of the M&A transactions in the LMM are valued between $25 million and $100 million of Enterprise Value (EV). A smaller subset of these LLM transactions will fall under $25 mm of EV. Our experience at GCG reveals that these LLM M&A transactions usually occur at a slightly discounted transaction multiple, relative to larger, sponsor backed Middle Market (MM) transactions.

Middle Market (MM) M&A transactions over the past decade have posted a median Trailing Twelve Months (TTM) EV/ EBITDA multiple of 11x vs the LMM median TTM EV/ EBITDA multiple over the same time period of 8.2x for M&A transactions under $100 million of EV. Similarly, EV/ LTM Revenue multiples for the MM over the past decade have averaged 2x while LMM M&A transactions over the same time period have been closer to 1x, for under $100mm EV transactions.

At Greenwich Capital Group (GCG) we see this size and ownership dynamic as an attractive "arbitrage" opportunity for PE Buyers to find great companies with great people, at attractive pricing. The financial and human dynamics behind Founder-led companies can create distinct valuation metrics that make non-backed businesses particularly compelling to PE Buyers, especially in the context of demographic shifts and retirement planning among Founder-led management teams. At GCG we have been advising on this large and distinct Founder-led sell-side Advisory market for more than a decade. Our track record speaks for itself, and our reputation is our bond. Please give us a chance to speak with your Founder/Family-led company and you will see and feel the GCG difference in M&A Advisory services.

Authors:

Alex Chefetz
Managing Director
achefetz@greenwichgp.com

Isabel Farnsworth
Analyst
afarnsworth@greewichgp.com

ABOUT US

GREENWICH CAPITAL GROUP

Greenwich Capital Group LLC ("GCG") is a leading investment bank that advises clients including closely-held and family-owned businesses, private equity firms, and public companies. GCG's senior bankers have collectively advised on hundreds of transactions over many years of experience in mergers and acquisitions, with most having backgrounds with large U.S. and global firms. GCG is focused on advising clients in key industry verticals throughout the U.S.

GCG was founded by entrepreneurially minded investment banking professionals focused on building an organization centered around advising clients. We strive to build relationships by representing our clients' long-term interests and earning their trust. In contrast to the practice of pushing transaction responsibilities to junior resources, our philosophy is to deliver personalized, senior-level attention and experience to every GCG engagement. We are proud to offer references that will speak to a differentiated level of service and results.