The Pulse of Private Equity – 1/5/2015

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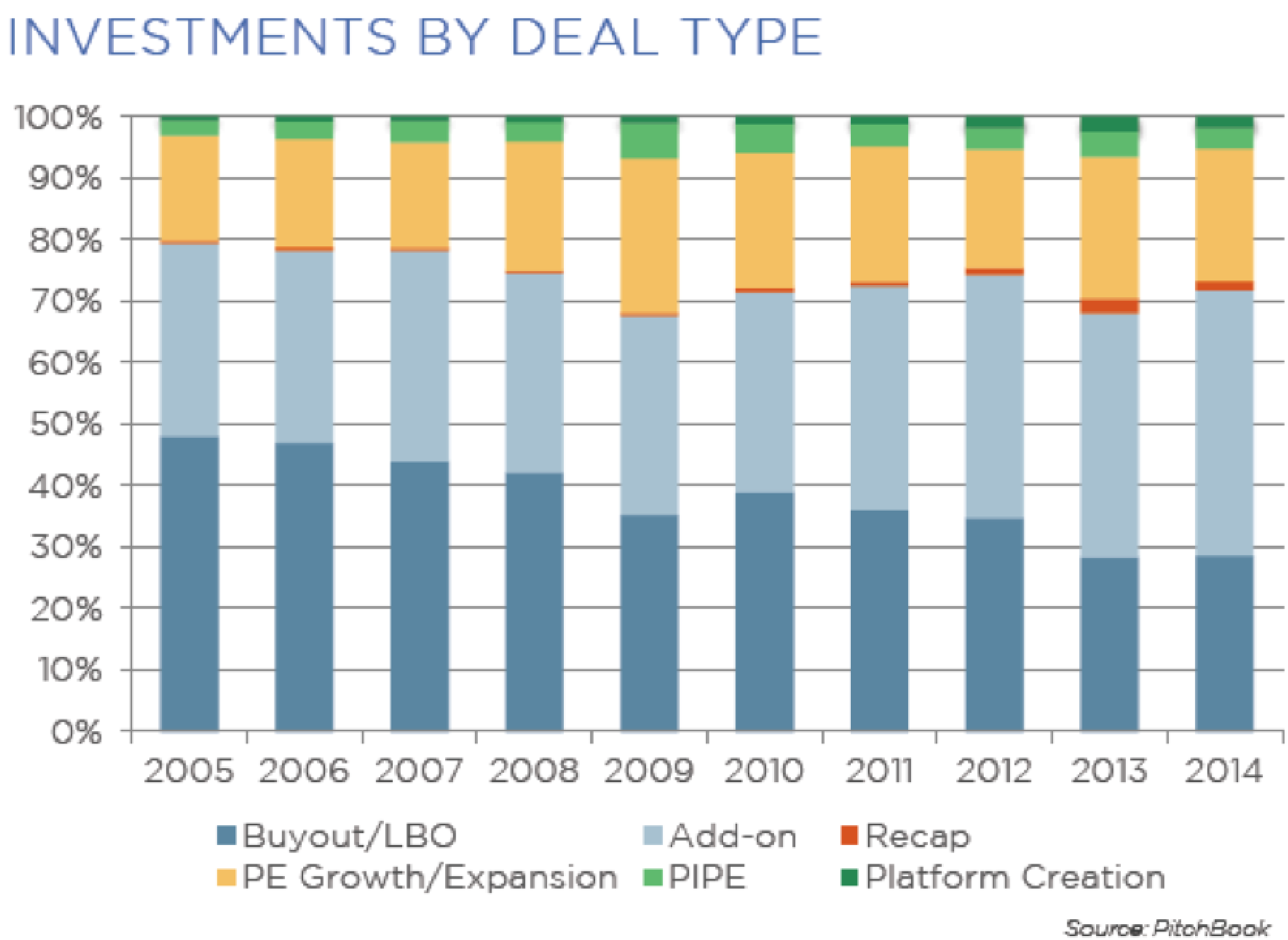
The "new normal" has arrived

We've been highlighting the increase in add-on and minority deals for a while. In some respects the rise of buy-and-build and non-control deals has reflected the tough deal-making environment for PE firms. Instead of stretching platform bids to unjustifiable levels, investors have taken to cheaper minority deals and add-ons, the latter of which can add significant value to current portfolio companies without costing an arm and a leg. Investors are "getting creative" instead of becoming wallflowers, in other words. There's some truth to that, but it implies the increases are temporary, that investors will revert to their old ways once the environment goes back to normal.



It's likely that both strategies are here to stay, though, regardless of conditions. As a percentage of deal flow, platform buyouts keep declining, down to 29% of total activity in 2014. In the lead-up to the crisis, they accounted for about half of all PE deals. Notice the gradual shrinking in the dark blue bars below (LBOs) and the inverse trend for add-ons and minority deals. In 2014 add-on and minority deals accounted for about 65% of all PE deals, up from less than 50% pre-crisis. Both strategies have been popular in good and bad years, and they keep climbing, with add-ons making up 60% of all control deals in 2014, a new record. That’s more than a reflection of temporary market conditions. What those numbers show is a maturing PE industry, which is more specialized and industry-focused today. They better understand their markets and can still add value to portfolio companies with or without control — or heavy leverage.