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## 2005 Middle-Market M&A Outlook

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The rebound in M&A activity, which began in earnest in the second half of 2003, carried over into 2004. We believe that the outlook for continued improvement in M&A activity in 2005 exists given that the positive factors driving this rebound in M&A activity remain in place. As we discuss in this report, several factors have combined to drive this increased M&A activity, including improved economic conditions, increased corporate profits, higher stock prices, the return of corporate buyers, strong debt and equity financing market conditions, greater corporate/CEO confidence and growth in the amount of private equity capital chasing investments. These factors have helped drive M&A activity to its first back to back positive increase since the 1997/1998 time period.

As we analyzed the data, we observed several key trends that helped shape M&A activity during the year. Among these observations, which are discussed in greater detail in this report, are the following:

- \* Global private equity activity continued to be a major driver of transaction activity, recording a 60% increase in dollar value activity and accounting for 15% of the total dollar volume.
- \* The strongest segment of the U.S. M&A market was in the billion dollar plus transactions, with a 55% increase in the number of deals.
- \* Acquisitions by public companies rose 19% and accounted for 49% of all U.S. deals up from 45% in 2003.
- \* The average U.S. deal size rose 47%, to \$261 million.
- \* Divestiture activity remained strong, representing 42% of all U.S. middle-market deals and 50% of the dollar volume.
- \* Technology remained the most active U.S. sector, with 21% of the total number of deals, while the Healthcare sector showed the largest increase, at 20.2%.
- \* Average lending multiples rose to 4.2x EBITDA, a level not seen since 1999
- \* Valuation multiples continued to improve, with the median LTM EBITDA multiple for the middle-market (through 11/30) at 9.4x vs. 7.9x in 2003 and 7.0x in 2002.
- \* Despite the improving economy, bankruptcy and distressed M&A transactions remained a sizable source of activity.
- \* Cash continued to be king in the U.S. middle-market, with 74% of all transactions consisting of all cash, the second-highest level in more than ten years.

Given the solid rebound in M&A activity, particularly with respect to the dollar volume, we are optimistic that this trend will continue in 2005 and into 2006. We believe that we will continue to see an increase in the quality of transactions, which should continue to drive higher dollar volume.

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