

US MIDDLE MARKET MONITOR

M&A and financing update

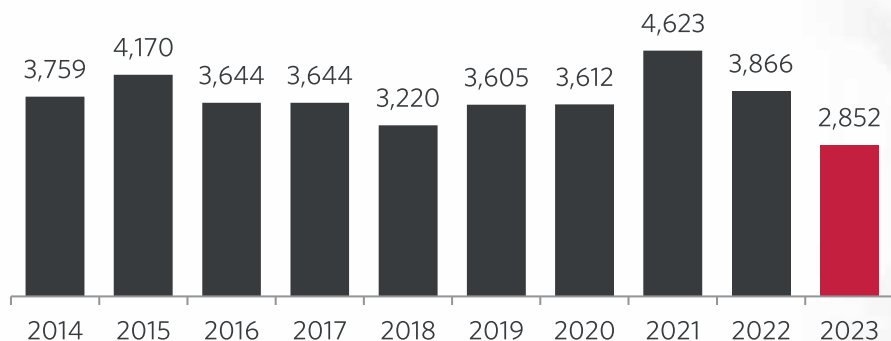
Q1 2024

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Deal volume declines

Annual number of US M&A transactions under \$500mm



US lower middle market deal volume (under \$500 million of enterprise value) declined 26% in 2023 compared to 2022 and was 46% below the 2021 peak according to Robert W. Baird. Tight lending markets, rising interest rates, lingering inflation, increasing regulatory scrutiny, and geopolitical tensions led to a general atmosphere of uncertainty. In 2023, after the collapse of Silicon Valley Bank, the syndicated bank market was basically closed for \$50 to \$250 million sale or recapitalization transactions. These factors contributed to deal volume reaching its lowest level in over 10 years. According to industry rumors, 50% to 70% of M&A deal processes in 2023 failed or were pulled because of market uncertainty, questions around sustainability of performance, or valuation gaps for “B” and “C” assets.

Despite these challenges, certain sectors such as aerospace and defense, facility services, and energy remained resilient. In addition, pockets of the industrials sector continued to attract significant interest due to aging infrastructure, reshoring, and investments in automation.

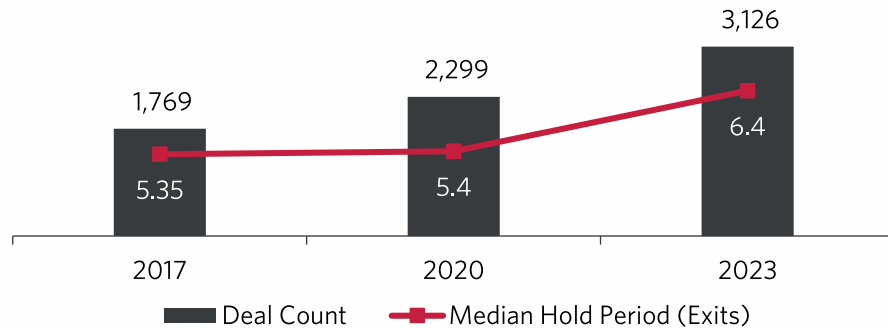
In the first half of 2024, dealmakers expect deal volume to remain below the historical average. However, dealmakers are optimistic there will be an improved environment for deal-making in the second half of the year.

Source: Robert W. Baird & Co.

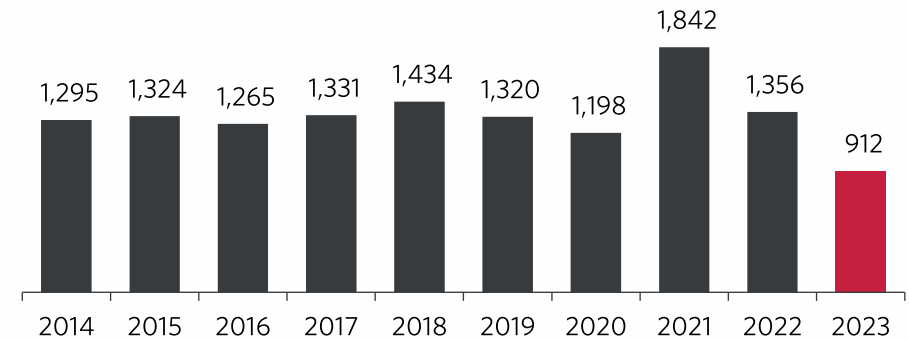


PE hold periods lengthen and exits decline

US PE holdings acquired 4-6 years earlier



US PE exit activity



As of December 31, 2023, the median hold period for private equity (PE)-backed companies in their respective funds reached 4.2 years compared to the five-year average of 3.8 years, according to Pitchbook. The median hold period for US PE investments that were sold in 2023 reached 6.4 years, which is the first time since 2015 that the median hold period for successful exits crossed the six-year mark.

PE firms are retaining their portfolio companies for longer durations due to challenging capital market conditions that are making it harder to achieve favorable returns. In addition, many portfolio companies were purchased in 2020 and 2021 at high valuations that were supported by “frothy” debt availability up to 2.0x EBITDA higher than the amount of debt that is available today. In today’s market, these same valuation levels are hard to achieve for non-“A” assets based on numerous factors, including the cost of capital and lower debt availability.

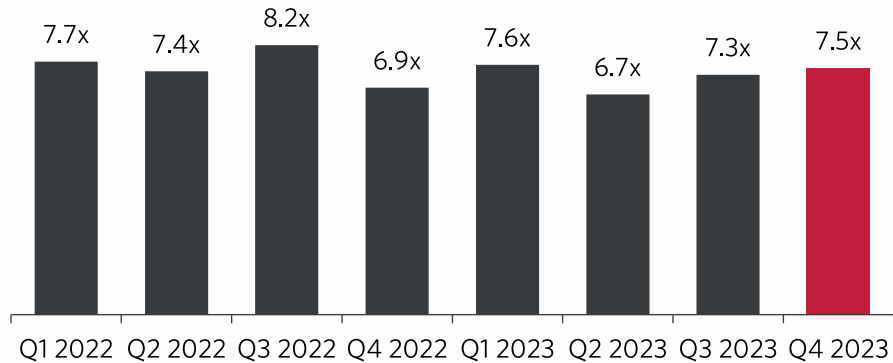
According to Pitchbook, the 912 PE exits also represented a trough in 2023, down 33% from 2022 and down 50% from 2021, further suggesting concerns about an impending “maturity wall” for investments made five to seven years ago. Based on these fund dynamics, CIBC believes it is possible that the second half of 2024 and 2025 could be a period of high exit activity for PE funds.

Source: Pitchbook.

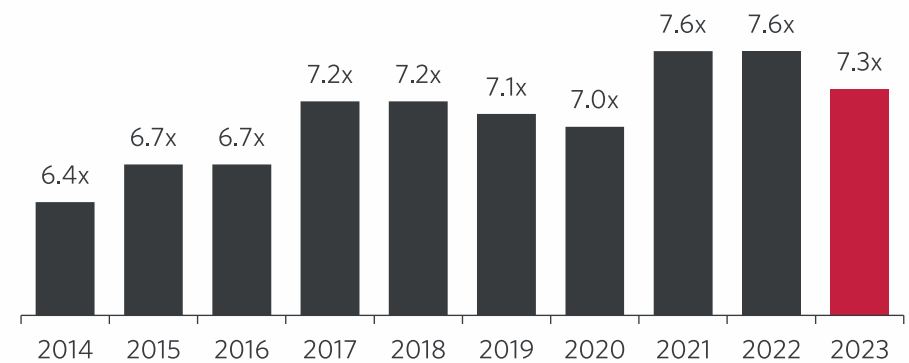


Valuation multiples remain above pre-COVID levels

Quarterly average EBITDA multiples for \$10mm - \$250mm LBOs



Annual average EBITDA multiples for \$10mm - \$250mm LBOs



In Q4 2023, EBITDA valuation multiples for PE-backed leveraged buyouts (LBOs) under \$250 million of enterprise value strengthened despite several market headwinds, according to GF Data®. The average EBITDA multiple for completed deals in Q4 was 7.5x, marking a 0.2x increase from Q3 and a 0.8x increase from the 6.7x average in Q2. Q4 valuations are most likely explained by buyers' willingness to pay premiums for quality assets.

In addition, the debt markets began to return to normal in November in support of "A" assets as regional banks returned to the syndication market after sitting on the sidelines for the first three quarters of 2023.

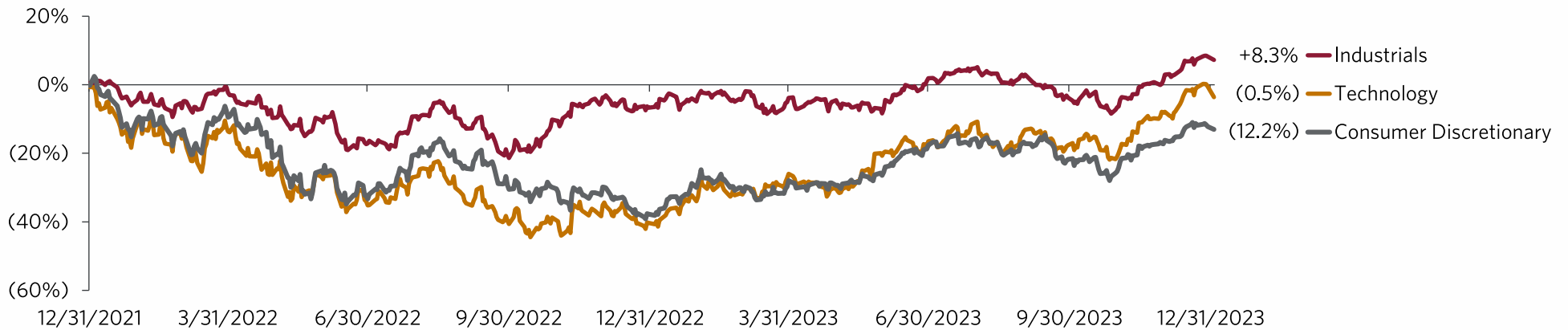
For all of 2023, the average EBITDA multiple declined slightly to 7.3x compared to an average of 7.6x in 2021 and 2022, according to GF Data®. However, 7.3x is still above long-term averages. Based on CIBC's experience, multiples on transactions over \$50 million in enterprise value declined by an average of 1.0x EBITDA during 2023 due to the impact of declining debt availability and rising interest rates.

Source: GF Data®.



Rebound in public market led by industrial sector

Public market performance



The trends in public market sectors have historically served as a data point that investors consider as part of their diligence before completing an M&A transaction.

From December 31, 2021, to December 31, 2023, the public equity market experienced significant growth in certain sectors and challenges in others. For example, the period was characterized by strong performance in the industrials sector. The industrials sector enjoyed an 8.3% return, with major contributions from companies like GE, Caterpillar, and Eaton, benefiting from infrastructure spending and end market demand. This performance was underpinned by a broader economic recovery and acknowledgement of technological advancements from companies by investors.

Conversely, not all sectors had positive returns. The technology sector lost 0.5% over the two-year period and the recovery in late 2023 was largely driven by a handful of stocks buoyed by the booming demand for AI technologies and significant earnings growth from leading companies such as Apple, Nvidia, and Microsoft. Another loser was the consumer discretionary sector, which experienced a 12.2% loss over the two-year period. The challenging performance

in the consumer sector reflects the consumer's sensitivity to inflation, diminishing discretionary income, resumption of student loan payments, and record levels of household debt.

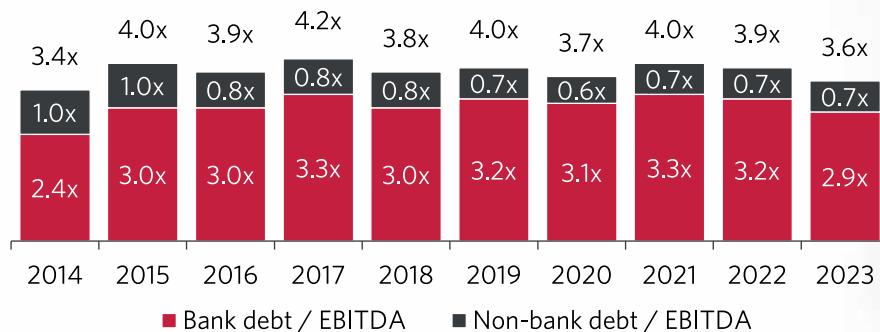
Despite a lot of noise in the public markets, the overall market performance was positive, with the S&P 500 index recovering from a down year in 2022 and returning to 2021 peaks. Trends in the public market will often be reflected later in the lower middle market, so the recovery in public market valuations is indicative of potentially increased M&A valuations and volume in the second half of 2024.

Source: S&P Capital IQ, NASDAQ.



Debt market challenges continue

Average LBO debt multiples for \$10mm – \$250mm LBOs



According to GF Data®, average PE-backed LBOs debt multiples under \$250 million of enterprise value stabilized during the second half of 2023 after declining for the first two quarters of 2023. Senior debt multiples averaged 2.9x, a nearly 10% decrease year-over-year from 2022. Subordinated debt multiples remained unchanged at 0.7x and the use of subordinated debt increased modestly during the second half of 2023 as buyers considered the benefit of fixed rates and no amortization that the product offers. Average total debt for 2023 was 3.6x, down from 3.9x in 2022 and below the historical average of 3.7x.

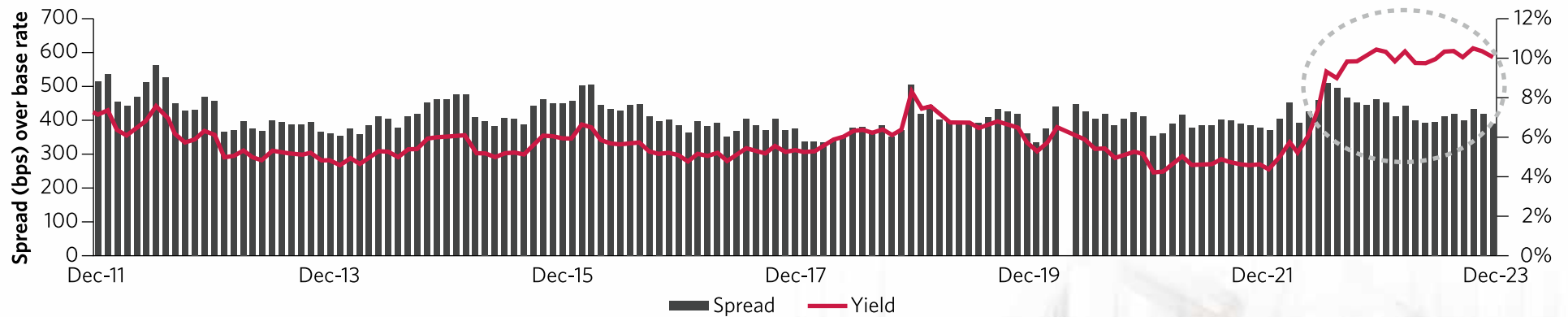
Interestingly, the decline in available leverage was more pronounced for platform deals exceeding \$25 million in enterprise value. Conversely, transactions valued between \$10 and \$25 million saw average total debt multiples hold at 3.7x in 2023, the same as in 2022.

Source: GF Data®.



Yields and spreads are tightening

New issue spreads and yields



The investment grade debt market began to strengthen in Q4 2023 with average yields for B-rated credits tightening to 10.1%, from the 2023 peak of 10.5%. Despite the market improvement, yields remain at their highest levels since the global financial crisis and remain over 500 basis points above the 2021 average. The elevated yields were attributed to fewer participants in the market early in 2023, who returned in November, resulting in competition that reduced spreads to the 10-year historical average of 400 basis points in December.

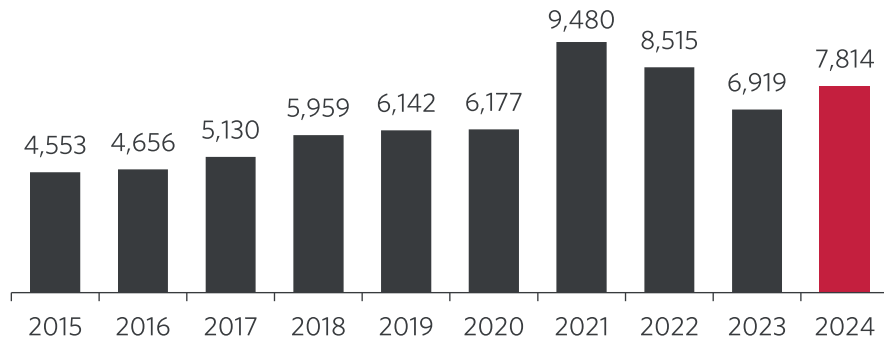
The decline in spreads at the end of 2023 reflects a more competitive market environment for strong credits, which has reopened refinancing and recapitalization availability and borrowers have taken advantage of the lower rates and greater lender receptivity. In addition, we saw investors increase their allocation to debt from equities in Q4 to lock in high yields, before the Federal Reserve begins to lower rates at some point in 2024.

Sources: GF Data[®], Pitchbook, Robert W. Baird & Co.



Outlook for 2024

US PE deal volume



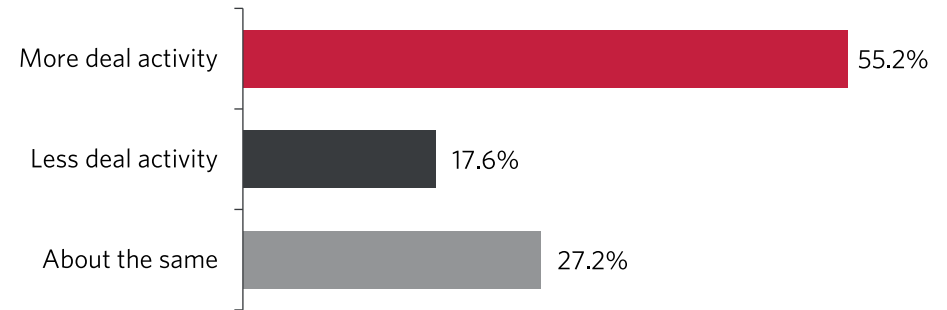
For 2024, there is a general sentiment of cautious optimism for M&A activity in the lower middle market. The EY-Parthenon Deal Barometer forecasts a 13% rebound in US PE deal volume and anticipates a 12% increase in corporate M&A activity in 2024. Factors contributing to this outlook include easing inflation, stabilization and potential decline of interest rates, increased availability of debt, and significant amounts of PE dry powder.

After 2023 produced a year with low volume of new deals, PE firms are eager to find new investments as investment periods approach term on existing funds. With unprecedented levels of cash-on-hand and expectations from their limited partners for return of capital, funds are eager to deploy capital as the economic landscape stabilizes. Strategic buyers are also pursuing M&A activity for growth given strong balance sheets and divestitures of non-core assets to streamline strategic focus.

However, there are potential challenges that could create headwinds for transaction activity, such as the unpredictability of the Fed's future actions on interest rates, ongoing conflicts in Ukraine and the Middle East, and a presidential election, which has often influenced M&A activity in advance of past elections based on candidates' tax and economic policies.

Source: EY-Parthenon, Pitchbook, Association for Corporate Growth.

Middle market M&A activity outlook



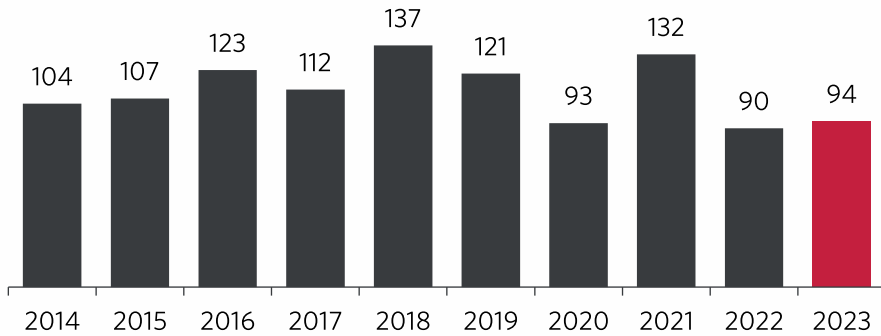
The Association for Corporate Growth survey revealed that 55% of respondents expect an increase in deal activity in 2024, while 27% expect activity to remain in line with 2023.

Increased deal volume, will largely be driven by dynamics in the debt market. The bank syndication market has reopened for recapitalizations and spreads have tightened. As the debt market fully returns to supporting mega LBOs, there will be a trickle-down effect into the lower middle market.

Overall, the 2024 outlook for M&A activity in the lower middle market is positive, with expectations of at least a modest increase in deal volume compared to 2023. Despite ongoing concerns about the pace of economic growth, numerous analysts and company leaders have published positive outlooks for 2024, suggesting a conducive environment for private equity and strategic transactions.

Consumer sector shows signs of optimism

US M&A consumer transactions



According to Robert W. Baird, transaction volume in the consumer sector increased by 4% in 2023 compared to 2022 but it was down 29% from 2021. The consumer sector continued to struggle in 2023 as it tried to find its new normal post-COVID. In addition, high interest rates, retailers rightsizing inventory levels, and unpredictable consumer confidence tied to inflation created uncertainty and headwinds within several consumer sectors.

The consumer market also continues to face supply chain challenges, commodity input pricing volatility, and uncertainty related to profitability as consumer product companies face pressure to moderate price increases and even reduce prices.

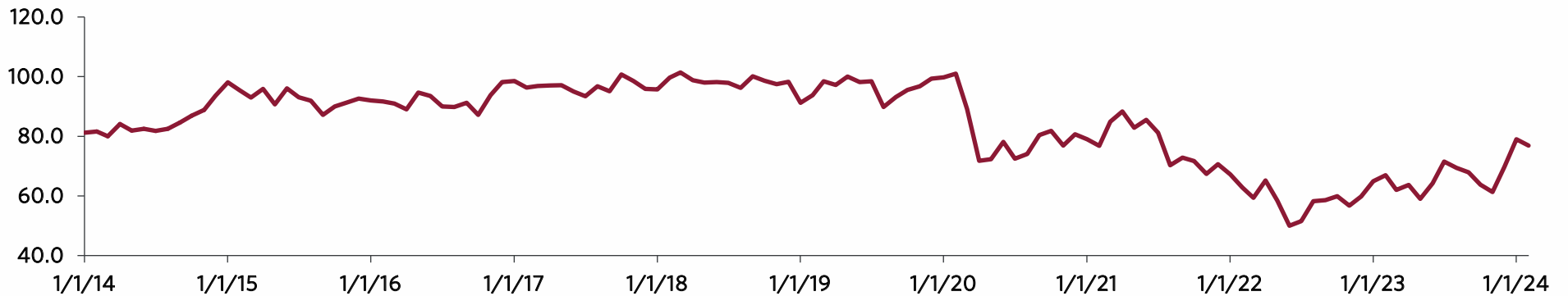
As 2024 begins, there is optimism in the market that the deal volume in the consumer sector will improve assuming interest rates decline, inflation moderates, and consumer confidence grows. We anticipate that consumer products deal volume will increase in Q2 and Q3 in advance of the election. However, we believe that this segment of the consumer sector has inputs, such as an Asian supply chain, which have been negatively impacted by past administrations' trade positions.

Source: Robert W. Baird & Co.



Consumer confidence uncertain

Index of consumer sentiment



Consumer confidence experienced three consecutive months of expansion from November 2023 to January 2024 before taking a surprising step backwards in February. The decline in consumer confidence in February, reflects the consumer's persistent concerns about their discretionary income and purchasing power in the face of persistent inflation and mixed signals about the US economy. Consumer confidence forecasts for the next six months have also deteriorated, driven by renewed pessimism surrounding the business and labor markets. Consumers were also less optimistic about their personal financial health as available discretionary income for autos, homes, big-ticket appliances, and vacations declined.

On a positive note, the 12-month average for inflation declined to 5.2%, its lowest level since March 2020, which is 2.7% off the peak of 7.9% in 2022. Consumers also remain upbeat about the public equity market. Rising optimism in consumer confidence in early 2024 has been offset by dips in both current economic conditions and expectations resulting in range-bound consumer confidence which is likely to remain until after the presidential election.

In 2024, we believe the M&A markets will continue to support the sellers of top-performing consumer products companies that have a track record of growth,

have proven resilient regardless of economic conditions, and have consistent, sustainable profits and margins. For the companies with these credentials, we believe 2024 represents a good opportunity to go to market and benefit from scarcity value and command a premium for an "A" asset.

Source: University of Michigan.



CIBC US Middle Market at-a-glance

Highlights



Nationally recognized middle market investment banking team with global reach.



Experienced and talented team has completed hundreds of transactions representing billions in transaction value



Clients include **private companies, private equity funds, and corporations.**



Differentiated approach to achieving client goals through disciplined and transparent transaction processes.

Investment banking services



M&A Advisory

- Execute transactions up to \$500 million in enterprise value
- Specialize in sell-side transactions
- Conduct targeted buy-side advisory services



Capital Placement

- Raise up to \$250 million in debt and/or equity
- Provide capital structure advice for management buyouts and recapitalizations



Financial Advisory

- Strategic alternative analyses
- Special situations transactions

Focus industry verticals



Consumer



Business Services



Healthcare



Industrials



Software & Technology



Recent CIBC US Middle Market transactions

<p>VAPOR POWER INTERNATIONAL a portfolio company of</p> <p>Stone Pointe, LLC M MIDWEST MEZZANINE FUNDS</p> <p>has been acquired by</p> <p>THERMON</p>	<p>ARMOR ANIMAL HEALTH DETECT. DEFEND. DELIVER.</p> <p>a portfolio company of</p> <p>GOLDNERHAWN</p> <p>has been acquired by</p> <p>VSI</p>	<p>Manix Vango TRAINING SOLUTIONS</p> <p>a portfolio company of</p> <p>SAFE SF FLEET</p> <p>has been acquired by</p> <p>OAK HILL CAPITAL</p>	<p>IDENTITI</p> <p>has partnered with</p> <p>KEYSTONE CAPITAL</p>
<p>pfi:inStore a portfolio company of</p> <p>CFB KVCI Mid States Capital L.P.</p> <p>DIAMOND STATE VENTURES NORTH CREEK</p> <p>has been acquired by</p> <p>ONWARD CAPITAL</p> <p>MERIT CAPITAL PARTNERS</p>	<p>MUTHIG INDUSTRIES, INC.</p> <p>has been acquired by</p> <p>LFMcapital</p>	<p>STOCK SUPPLY</p> <p>has been acquired by</p> <p>BLACKHAWK INDUSTRIAL</p>	<p>AAR</p> <p>has acquired</p> <p>Trax</p>
<p>LAKE AIR PRODUCTS</p> <p>has been acquired by</p> <p>P4G CAPITAL</p>	<p>EGT GOLF SUPPLIES</p> <p>a portfolio company of</p> <p>HADLEY</p> <p>has been acquired by</p> <p>KINZIE CAPITAL PARTNERS</p>	<p>TRANSHIELD Advanced Protective Cover Technology</p> <p>has been acquired by</p> <p>PATRICK</p>	<p>AMEREQUIP</p> <p>has been acquired by</p> <p>JMC FAMILY OFFICE</p>

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