

MERCER CAPITAL

Middle Market Transaction Update

Spring 2025

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Spring 2025 M&A Update

Middle market M&A activity rebounded in the fourth quarter of 2024, albeit, marginally, over the “summer slowdown” experienced in the third quarter of 2024. The 2024 year as a whole marked improvement related to overall deal activity, as its 379 completed private equity transactions surpassed the 324 and 294 completed transactions seen in 2022 and 2023, respectively. Despite a muted fourth quarter, the middle market continued to show signs of improvement at the end of 2024. Market observers point to the muted fourth quarter metrics as stemming from uncertainty regarding the election in November. The results of the election did not produce a subsequent rush to get deals closed before the end of the year.

Overall transaction volume remained steady quarter over quarter. While deal value fell slightly (5%) quarter over quarter, deal volume in the fourth quarter of 2024 outpaced the prior six quarters, showing signs of resiliency. The U.S. economy grew at an annualized rate of 2.3% in Q4 2024 while inflation pressures persisted. Although the Fed cut rates in September 2024, Federal Reserve officials are expected to remain cautious about cutting interest rates in the near future amidst inflation showing signs of resurgence. The hottest topic in the space, tariffs, has the middle market M&A space facing uncertainty, potentially leading to a “wait-and-see” approach as companies assess the long-term impact of shifting trade policies.

As shown in the accompanying charts on the next page, overall U.S. deal activity, as compiled by *Capital IQ*, in the fourth quarter of 2024 increased from the depressed levels observed in the third quarter of 2024, reaching a higher level than any quarter in 2024. *GF Data*® reports that U.S. PE middle-market activity, defined as deals with an enterprise value of less than \$500 million, increased 15% to 94 deals in the fourth quarter of 2024. Although a rebound in the fourth quarter after the summer slowdown would be expected, the number of deals during this quarter matched the number of deals seen in the first and second quarters of 2024.

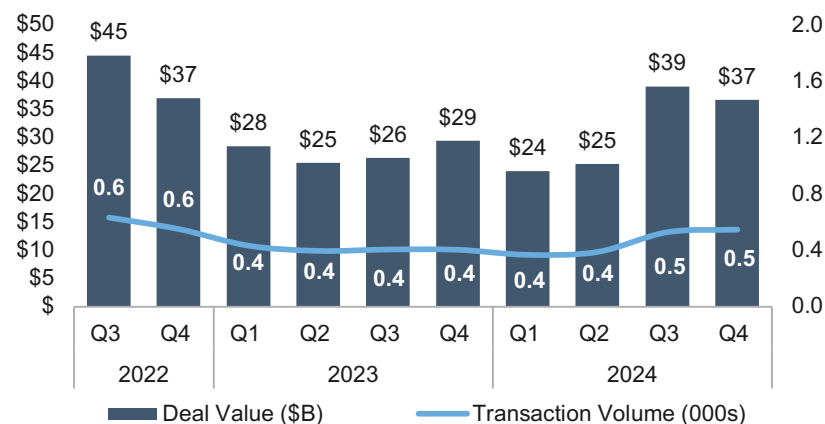
Lower middle market activity (defined as enterprise values of \$10 million to \$500 million) as compiled by *GF Data*® provides several notable observations regarding PE-backed transactions:

- Similar to the overall U.S. transaction level, lower middle market activity remains depressed relative to 2022 and especially 2021, when financing costs were historically low;
- The average EBITDA multiple for all sub-groups slightly increased to 7.3x in the fourth quarter compared to 7.2x in the prior quarter and 7.3x in the fourth quarter of 2023;
- The average EBITDA multiple for the trailing 12 months on a rolling quarterly basis remained at 7.2x quarter over quarter. The multiple was slightly higher (7.3x) for the trailing 12 months ended December 31, 2023;
- The average EBITDA multiple for the trailing 12 months by sub-group ranged from 6.5x for deals with an enterprise value of \$10-\$25 million to 10.1x for deals in the \$250-\$500 million range;
- The year-to-date average multiples by industry ranged from 6.7x for media & telecommunications to 8.1x for technology;
- Buyer transaction costs that are excluded from the multiples cited above add about 0.3x to all-in costs.

Deal volumes in both strategic and financial deals during the fourth quarter present a similar picture. The chart on next page highlights overall deal value and volume, including strategic deals. The fourth quarter of 2024 represents an uptick in deal value (28%) and volume (35%) over the last four quarters. Deal value decreased 5% quarter-over-quarter and is flat from fourth quarter 2023 metrics.

U.S. Deal Value & Volume

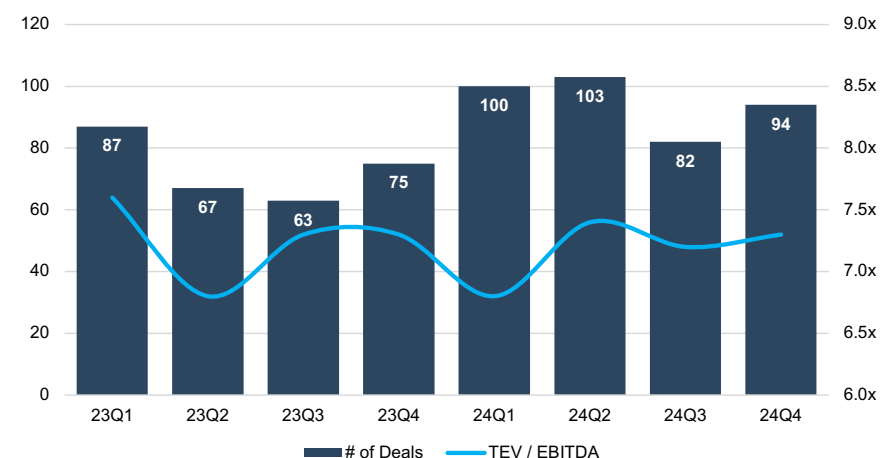
Q3-2022 to Q4-2024



Source: Capital IQ

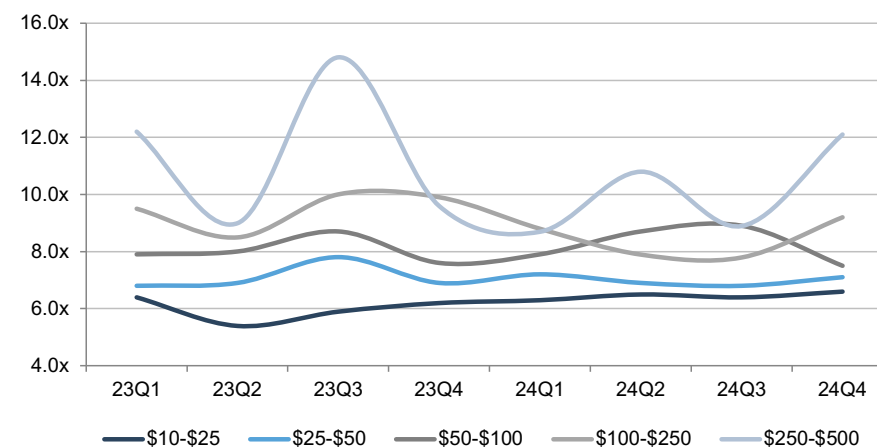
Number of Deals and Average EBITDA Multiples

Lower Middle Market Financial Buyers | Last 8 Quarters



TEV/EBITDA Multiples

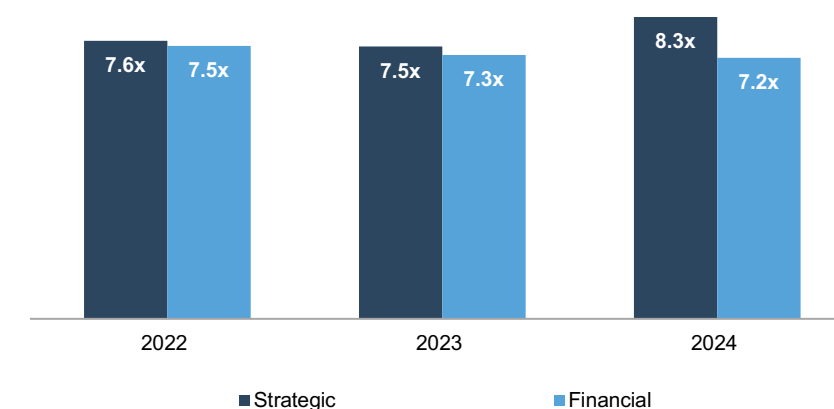
Financial Buyers | Last 8 Quarters



Source: GF Data®

EBITDA Multiples by Buyer Type

2022 to 2024

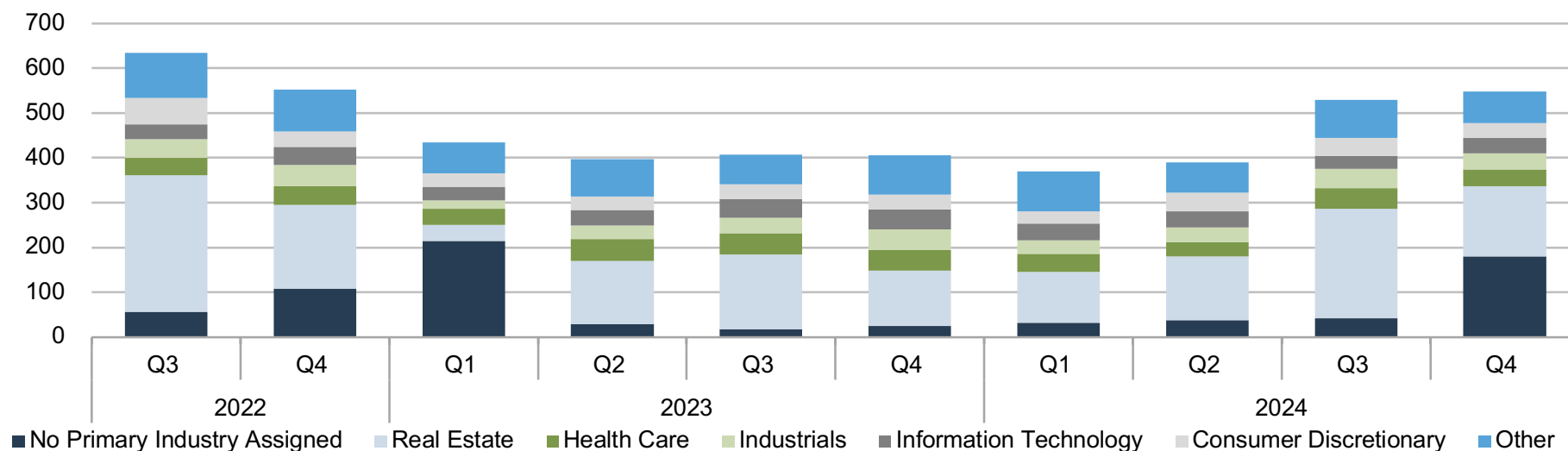


Source: Capital IQ (strategic) and GF Data (financial)

Strategic multiples exclude outliers (defined as EBITDA multiple > 18x)

U.S. Deal Volume by Industry

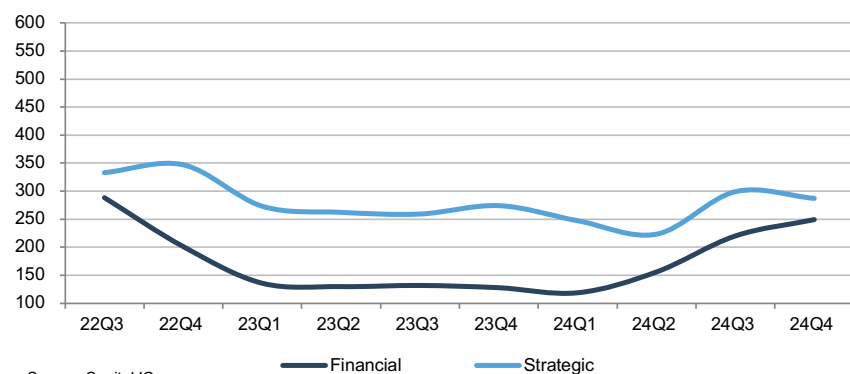
Q3-2022 to Q4-2024



Source: Capital IQ

Number of Deals by Buyer Type

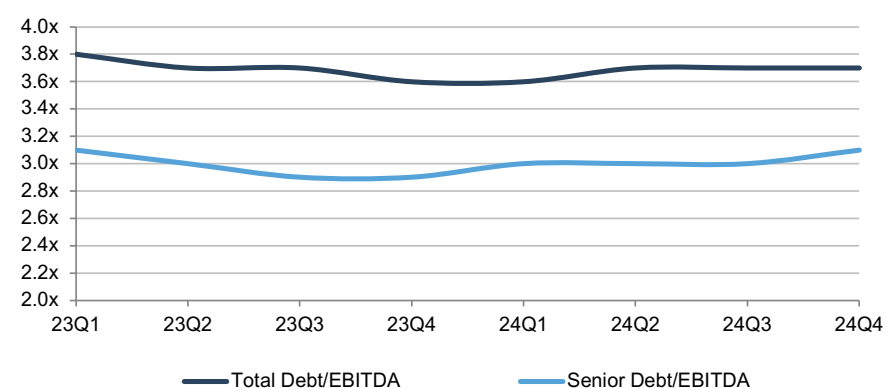
Q3-2022 to Q4-2024



Source: Capital IQ

Debt Multiples

Financial Buyers | Last 8 Quarters



Source: GF Data®

Negotiating Net Working Capital Targets in a Transaction

In 2025, we plan to highlight certain key aspects of the transaction process in our quarterly update. In this issue, we focus on the importance of working capital targets in middle market transactions.

In middle market transactions, some of the most crucial points of negotiation are the net working capital targets agreed upon by the buyer and seller. Net working capital targets set a defined minimum amount of working capital that the buyer requires the seller to leave in the business at the close of a transaction.

Given that net working capital targets can have a direct effect on the final purchase price of a transaction, understanding the how and why of these types of negotiations is crucial for buyers looking to negotiate deals that not only look good at closing but also pass the test as the buyer takes over the operation of the newly acquired business.

Defining Net Working Capital

By the book, net working capital is defined as current assets less current liabilities. While this definition is acceptable for financial statement analysis and other accounting-adjacent applications, in the M&A universe, the most commonly used measure of net working capital is cash-free, debt-free net working capital. This is the standard definition of net working capital in a deal setting because it assumes that a seller will retain the cash in the business after paying off any short-term debts that the business owes. These debts could potentially include related party notes and lines of credit with banks.

In an M&A transaction, net working capital and net working capital targets are often defined terms in both the letter of intent and the purchase agreement. For buyers, it is crucial to understand these definitions because the basis of the net working capital calculation could directly affect the final purchase price.

Why Are Net Working Capital Negotiations Necessary in a Deal?

Net working capital targets are necessary in deal settings because the amount of net working capital in a business often fluctuates from month-to-month and even week-to-week. Therefore, it is important that a benchmark or base level of net working capital to be left in the business at closing is agreed upon by both the buyer and the seller. If net working capital levels at closing are not in line with the targets established in the negotiation process, an adjustment to the purchase price can be triggered.

Negotiating Net Working Capital Targets

The most practical and commonly used method of setting net working capital targets and benchmarks is to calculate a historical average amount of net working capital needed to fund a company's operations. This is most often done by calculating the average net working capital on a monthly basis over the twelve months preceding the valuation date used in the transaction.

While conducting due diligence, buyers may find potential adjustments to certain balance sheet items that comprise net working capital, which can affect the calculation of the net working capital target. Buyers will want to confirm that the seller has properly accrued (both historically and at closing) for certain items such as accrued vacation, payroll, bonuses, warranty obligations, etc. These potential adjustments can add another layer of complexity to the negotiation of net working capital targets, as buyers may find that there is an excess or deficiency of net working capital at certain points in the historical lookback period.

Sellers will often make the argument that they have historically operated with excess working capital based on comparisons to industry averages. It can be difficult to convince the buyer of this excess working capital argument absent compelling evidence. With further analysis, there is often an explanation as to why the historical level of working capital has been carried on the company's balance sheet. The question as to whether this level is excess or not is up for negotiation.

Concluding Thoughts

Having a team of seasoned advisors to assist with the acquisition and due diligence process can ensure buyers that the net working capital targets, and thus the purchase price, are set at levels that are appropriate and fair to the buyer.

Since 1982, Mercer Capital has offered M&A advisory services to a diverse range of public and private companies, leveraging extensive valuation and investment banking experience to guide clients through complex transactions. While our team provides objective advice, we also advocate for our clients while navigating the competitive marketplace of private equity groups, family offices, and strategic buyers. We facilitate informed decision-making with a tailored, multi-phased approach to planning and executing transactions. For confidential consultation on your transaction-related needs, contact us today.



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Mercer Capital's Recent Transactions

First Missouri Bancshares, Inc.

 Brookfield, Missouri


has agreed to acquire

CCSB Financial Corp.

 Liberty, Missouri

Mercer Capital served as financial advisor to First Missouri and rendered a fairness opinion

— January 2025 —



 Panama City, FL

has acquired


**FIRST NATIONAL BANK
NORTHWEST FLORIDA**
 Panama City, FL

Mercer Capital provided valuation and advisory services to Innovations

— August 2024 —


 Louisville, KY

has partnered with


 Chicago, IL


Mercer Capital served as financial advisor to Aspirant

— May 2024 —

U.S. Based Manufacturer of Flow Control and Process Equipment


Mercer Capital rendered a solvency opinion for the manufacturer related to payment of a \$200 million dividend following the sale of a business unit

— June 2024 —



Specialty Construction Materials Dealer / Distributor

Mercer Capital served as financial advisor to the seller in connection with an \$81 million transaction

— May 2024 —



 Olive Branch, MS

sold the majority of its assets to



 Chicago, IL

Mercer Capital served as financial advisor to The Neverleak Company LP

— April 2024 —



 Sioux Falls, SD

has announced its intent to acquire a bank branch in Sioux City, Iowa from



 Spicer, MN

Mercer Capital served as financial advisor to Levo

— April 2024 —


 Corpus Christi, Texas

has formed a partnership with


 Owings Mills, Maryland

Mercer Capital served as financial advisor to Hose of South Texas

— April 2024 —

Mercer Capital provides investment banking, transaction advisory, and restructuring services to a broad range of public and private companies and financial institutions. >> [View All Transactions](#) <<

Other Resources



WHITEPAPER

Quality of Earnings

What Buyers and Sellers Need to Know About Quality of Earnings Reports

For buyers and sellers, the stakes in a transaction are high. You only get one chance to do it right. Commissioning a quality of earnings report is an essential step in getting the transaction right.

In this whitepaper, we illustrate how buyers and sellers benefit from a quality of earnings report that extracts a company's sustainable earning power from the thicket of historical GAAP earnings. We review the most common earnings adjustments applied in QofE analyses and review the role of working capital and capital expenditures as the links between EBITDA and cash flow available to buyers.

[DOWNLOAD PDF](#)



WHITEPAPER

Selling Your Business

Practical Steps Business Owners Can Take to Ready Their Businesses for the Best Transaction Outcome

Selling your business is a daunting exercise that requires careful preparation and real-time vigilance. In this whitepaper, we define some practical steps business owners can take to ready their businesses for the best transaction outcome. These steps include identifying the right kind of buyer and transaction design, setting expectations for the timeline to consummate a transaction, hiring an advisor, understanding the various advisory fee structures that best suit each transaction scenario, as well as a few considerations every owner should contemplate before bringing their business to market.

[DOWNLOAD PDF](#)



WHITEPAPER

Buy-Side Considerations

Middle Market Companies Looking to Enter the Acquisition Market

Many observers predict that the market is rife for an unprecedented period of M&A activity, as the aging of the current generation of senior leadership and ownership pushes many middle market companies to seek an outright sale or some other form of liquidity. Obviously, not all companies are in this position. For those positioned for continued ownership, an acquisition strategy could be a key component of long-term growth.

In this whitepaper, we cover buy-side topics from the perspective of middle market companies looking to enter the acquisition market.

[DOWNLOAD PDF](#)

Transaction Advisory Services

In addition to our corporate valuation services, Mercer Capital provides investment banking and transaction advisory services to a broad range of public and private companies and financial institutions.

Mercer Capital has been successfully executing mergers & acquisitions for a broad spectrum of middle-market companies since the mid-1980s.

We specialize in providing merger & acquisition services to sellers or buyers of private businesses or public companies divesting divisions and subsidiaries. In addition, Mercer Capital assists clients in industry consolidations, roll-ups, and refinancings.

Mercer Capital leverages its historical valuation and investment banking experience to help clients navigate a critical transaction, providing timely, accurate and reliable results. We have significant experience advising boards of directors, management,

trustees, and other fiduciaries of middle market public and private companies in a wide range of industries. Our independent advice withstands scrutiny from shareholders, bondholders, the SEC, IRS, and other interested parties to a transaction, and we are well-versed in the new industry standards.

The professionals of Mercer Capital guide you through the uncharted waters of selling your business, acquiring another business or division, mergers, valuations, fairness opinions, and other transaction advisory needs. Rely on the experience, independence, and transaction know-how of Mercer Capital.

Transaction Advisory Services

- M&A Representation
- ESOP Installation, Termination, and Transactions
- Squeeze-Out Transactions
- Fairness and Solvency Opinions
- Minority Shareholder Stock Repurchases
- Corporate or Partnership Recapitalizations



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