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interview with

Rodney
Cohen

Managing Director,
The Carlyle Group

Q3 2016 Dealmaker Roundup

Featured Topics

Software Companies in PE's Sights
Certainty to Close is a Hot Differentiator
Are Financial Buyers the New Strategics?

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About This Report

This publication is a companion to Privcap's Dealmaker Roundup, a quarterly video program on the latest trends in private equity dealmaking.

[You can watch the full program here.](#)

About the Experts



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Michael Fanelli is a partner in the Transaction Advisory Services practice at RSM US LLP, focusing on retail and consumer products and business and professional services. He performs transaction advisory services on both buy-side and sell-side transactions, assisting both financial and strategic buyers. Prior to his transaction advisory experience, Fanelli worked as a controller of a middle-market company and as an auditor at a Big Four accounting firm.

[Learn more about RSM here.](#)



Samuel Hendler is a managing director in the Technology, Media & Telecom Group at Harris Williams & Co. and leads the firm's Healthcare IT practice. He has extensive experience advising both public and private technology companies on M&A transactions, private placements, and corporate divestitures with a focus on SaaS software and technology-enabled services businesses. Previously, Hendler worked as an associate with Quellos Private Capital Markets, L.P., and as an M&A analyst with Broadview International, LLC.

[Learn more about Harris Williams here.](#)



Mark O'Hare was one of the founders of Preqin in 2003 and is responsible for the company's strategic development. O'Hare was previously a manager with Boston Consulting Group and founded Citywatch, the equity shareholdings information service that is now part of Thomson Reuters.

[Learn more about Preqin here.](#)



David Snow is CEO and co-founder of Privcap Media, the leading channel for thought leadership in private capital investment.

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Software Companies in PE's Sights

David Snow, Privcap: We know that 2016 is on track to being another robust year for the private-equity-backed deal market, but we also saw a slight downtick in the number of deals that got done. What is behind that trend?

Samuel Hender, Harris Williams: What we're seeing is there's tremendous activity in the market, and a kind of a flight to quality. So while volume may be down a little bit, value and multiples are up materially.

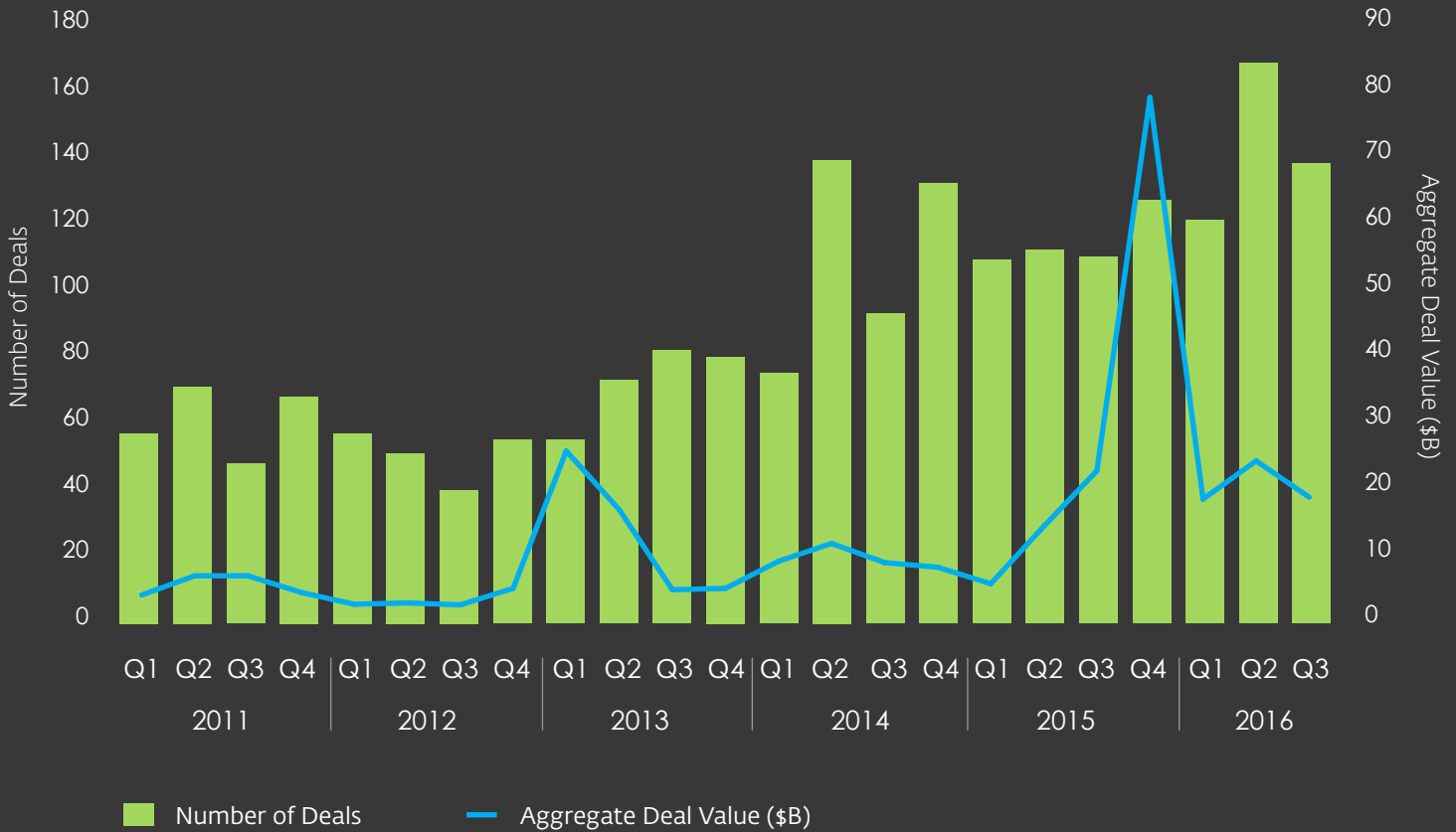
Mark O'Hare, Preqin: You know, we worry about the economy, but it's a relatively benign economy, and [there is] the ready availability of debt at remarkably good prices.

Michael Fanelli, RSM: Dry powder's at one of the highest levels ever. It's just a matter of, like you said, a flight to quality. Are there enough quality companies out there in the middle market for these private equity firms to acquire?

The volume of software deals continues to rise. Private equity is very interested in software, and that spike that you see was actually the Dell and EMC merger, backed by Silver Lake. But even if you look at the number of software deals overall, it continues to grow. Mike, what's behind private equity's interest in software?

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PE Buyout Deals on the Rise in Software Sector



Source: Preqin

Fanelli: Every company is now technology-enabled, so there's more software as a service-type business out there. You have a lot of these SaaS-based business that are starting up, seeing revenue growth, getting investors in quickly, turning over quickly, and having multiple sponsors come in. And so there's just even more opportunity for investment, and the private equity firms are seeing the returns from that.

Hendler: So you take those very strong tailwinds and combine them with what is basically a business model tailor-made for private equity—high recurring revenue, good margins with scalability capability, and low capex—and that's why you're seeing such a boom in activity.

O'Hare: You talked about the multiples that people are paying. Where can you generate the growth to justify those multiples? It's in the more rapidly

growing parts of the economy, and hence software is doubly attractive for a private equity buyer.

It's worth noting that just as the rise of energy as a sector of focus influenced the rise of several energy-specialist private equity firms like Riverstone and EnCap, we're now seeing the rise of some specialist private equity firms like Vista Equity that focus only on software. And these are firms that are raising substantial amounts of money.

O'Hare: I just looked at the five largest buyout deals in the U.S., in Europe, and in Asia this year-to-date, and five out of five in the U.S. are IT, software, media, intellectual property. Europe has property, has consumer, has industrial in there, and ditto Asia. So, yes, software is a really important and dominant part of the industry, and thank goodness it's as strong as it is here in the U.S.



Certainty to Close is a Hot Differentiator

Sam, what does “certainty to close” mean from a seller’s perspective?

Hendler: We always preach, when we’re working with companies, what we’re looking for—a combination of price, terms, and speed in certainty to close. So how does a buyer go about demonstrating certainty to close? To the extent a party can come in and say, “we’ve done our work, we can move, we can get this done quickly and we can meet the terms, and we’ve already done our Q of E,” you can get a lot more comfortable that there are no surprises that are coming once you grant exclusivity or move towards a close deal.

A lot of times there are multiple buyers coming down to the line. There’s four to five buyers coming in to say, “Give me your best and final offer, and we want the least amount of contingency.” So then

the buyers need to make a decision. Do I spend money? Do I want this asset? Do I think I’m going to win it, no matter what? If I want it bad enough, do I think I’m going to win it because of price, because of bringing an operator partner in that’s going to increase top line or bottom line or otherwise?

O’Hare: All of that is absolutely happening, and it’s happening globally. And it’s yet another notch in raising the stakes for buyers. You have to either invest in all the factors of due diligence you talked about ahead of time, before you know you’re on the short list, or you have to, frankly, cut corners in that, both of which are raising your risk [profile].

Hendler: And we’re increasingly seeing a lot of our clients move to almost more of the European model of doing some of the vendor due diligence, if you will, prior to even initiating a process or initiating reach-out.

Fanelli: Sell-side due diligence almost seems like the new normal. It’s not on 100 percent of projects, but it’s so prevalent now. I mean, five years ago it was probably 5 percent of our transaction advisory group. Now it’s 30 percent, because of wanting certainty to close, and a fast close process, too.

Are Financial Buyers the New Strategics?

Historically, financial buyers—aka equity firms—have not often bid as high as strategic buyers, and that gap appears to be closing. What is behind that trend?

O'Hare: The availability of debt finance has a huge factor to play there. The current market conditions make it feasible for financial sponsors to offer very full valuations.

Hendler: We're absolutely seeing financial sponsors being highly competitive in deals. If you then dial into specific sectors—for example, healthcare—roughly 60 percent of our deals go strategic. In tech, roughly 70 percent of our deals go strategic. In healthcare IT, 85 percent of our deals have gone to strategic buyers.

At the same time, there's been substantial private equity interest in a number of those assets, and when they have prevailed it's because they have an angle—an operating partner, a thesis, a way to take this platform and expand it rapidly. And they're, in some cases, particularly for platform-oriented assets, better suited to pursue an acquisition and build [on a] strategy than a strategic might be.

Is the phenomenon of a private equity buyer placing a bid that's almost equal to—or, in some cases, exceeding—the bid of the strategic buyer a reflection of, number one, the incredible competition in the market now from so much capital chasing deals, and, number two, the increasing specialization of these private equity firms that have a strategic angle as they go into bid for some of these assets?

Fanelli: A lot of times [firms are] having these external advisors—sometimes they're even internal to the private equity firm—where they're going to market with an operating partner who can get that company into a new channel, a new division, maybe a new supplier to reduce costs, so they're adding value in different ways.

O'Hare: Absolutely, and your point about the financial buyer having a thesis often relates to your point about how incredibly specialized some of these fundraisers are. Not just software—it's SaaS-based B2B businesses. And therefore the financial buyer can come to that auction with some fairly powerful weapons of his own. ■





Rodney Cohen
Managing Director,
The Carlyle Group

POWER BROKERS: Rodney Cohen

Insights from the world's leading investors and dealmakers



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Don Lipari
National Private Equity Leader,
RSM US LLP

RSM national private equity leader Don Lipari interviews The Carlyle Group managing director Rodney Cohen about what he has to do to get deals done.

Don Lipari, RSM: What's your day like when you're in investing mode?

Rodney Cohen, Carlyle: There are periods where you're incredibly busy, and then there are periods that are somewhat more challenging. We tend to find, in our sizes, there's always something to do. But it's all about processing. It's all about opportunity identification. And good or bad, like it or not, a tremendous amount of this business is still face-to-face. You have to get in a room with people and hear their story and listen to what they're saying.

Unfortunately, it's a lot of frog kissing. So it's all about volume of meetings, volume of opportunities. I always say to people, "I don't really think of myself as working or not working." I could be at a cocktail party on a Saturday night and someone comes up to me and says, "I have a business that I..." And my ears totally perk up. ■