



NATIONAL CENTER FOR  
THE MIDDLE MARKET

January 22, 2020

# The Market That Moves America

Findings from the 4Q 2019 Middle Market Indicator Report

Thomas A. Stewart, Executive Director | The National Center for the Middle Market

IN COLLABORATION WITH



THE OHIO STATE UNIVERSITY

FISHER COLLEGE OF BUSINESS

CHUBB®

# The National Center for the Middle Market

The National Center for the Middle Market is a collaboration between The Ohio State University's Fisher College of Business and Chubb. It exists for a single purpose: to ensure that the vitality and robustness of Middle Market companies are fully realized as fundamental to our nation's economic outlook and prosperity. The Center is the leading source of knowledge, leadership, and innovative research on the middle market economy, providing critical data analysis, insights, and perspectives for companies, policymakers, and other key stakeholders, to help accelerate growth, increase competitiveness and create jobs in this sector.

## Middle Market Research & Data



Quarterly Middle Market Indicator



Research and Expert Perspectives



Interactive Benchmarking Tools

## Expertise & Outreach



Share Research & Discuss Trends

## Education



Executive Programs



Webinars and Podcasts

# The Mighty Middle Market

## U.S. MIDDLE MARKET DEFINED



Annual Revenues Range from  
**\$10MM - \$1B**



Accounts for  
**60%** of All New  
Private-Sector  
Jobs



Nearly  
**200,000** in All Industry  
Businesses Segments and  
Geographies

Equivalent to the  
**5<sup>th</sup> LARGEST**  
global economy



Represents  
**1/3** of Private Sector  
GDP and Employment



**85%**  
of Companies  
Are Privately Held



More than  
**\$10 trillion** in annual revenue

# 4Q19 Middle Market Indicator

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# About the Middle Market Indicator

## A Quarterly National Survey



## Cut by Geography and Industry



# Headlines

- 1** The annualized revenue growth rate for middle market companies rebounded sharply from the lower growth rate posted in the 3<sup>rd</sup> quarter of 2019, with business and financial services leading the way. Private-equity-owned companies outperformed the national averages, and expect to continue to thrive.
- 2** Employment growth picked up too, but not as much as revenue growth, and employment growth forecasts are not strong. Nevertheless, the hunt for talent remains the #1 challenge middle market companies face.
- 3** Short-term expectations and confidence have bounced back, too, and the middle market's investment appetite has returned compared to last quarter. PE-owned companies have returned to their familiar role as more expansion-oriented than the middle market as a whole.
- 4** Conservative revenue and employment forecasts and expansion plans suggest that the middle market remains jittery about the economy.

# Overview

## REVENUE GROWTH

7.5%

PAST 12 MONTHS

4.3%

S&P 500

4.9%

NEXT 12 MONTHS



## EMPLOYMENT GROWTH

5.0%

PAST 12 MONTHS

0.7%  
SMALL  
BUSINESS

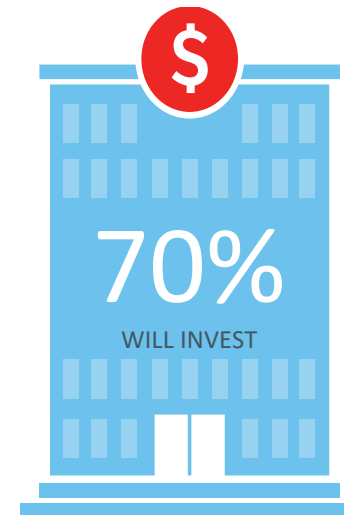
2.3%  
LARGE  
BUSINESS

3.5%

NEXT 12 MONTHS



## CAPITAL INVESTMENT



## CONFIDENCE

68%

GLOBAL ECONOMY



83%

NATIONAL ECONOMY



89%

LOCAL ECONOMY



# 4Q'19 MMI: Revenue Growth Trend

PAST 12 MONTHS

**7.5%**

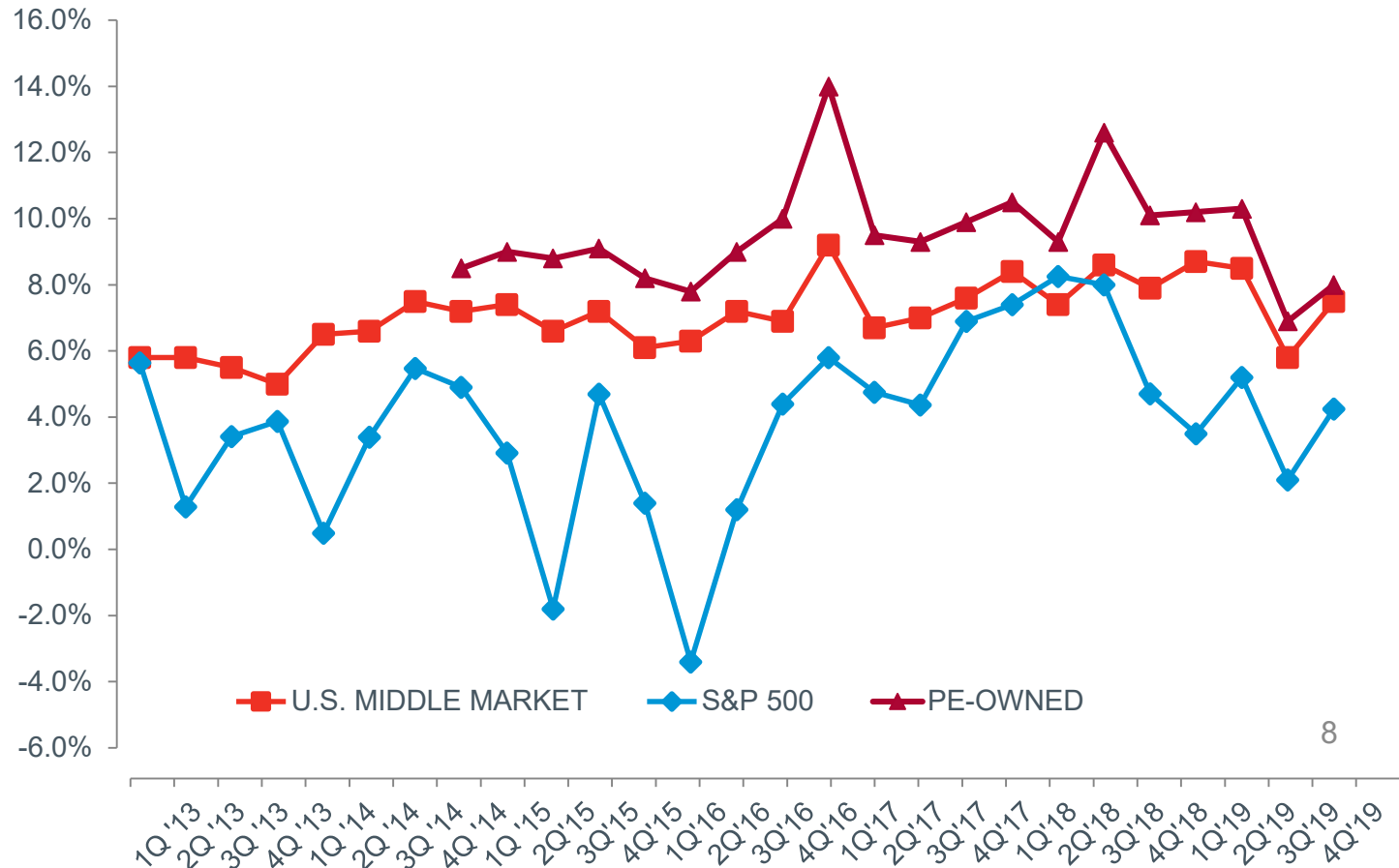
U.S. MIDDLE MARKET

**8.0%**

PE-OWNED FIRMS

**4.3%**

S&P 500\*

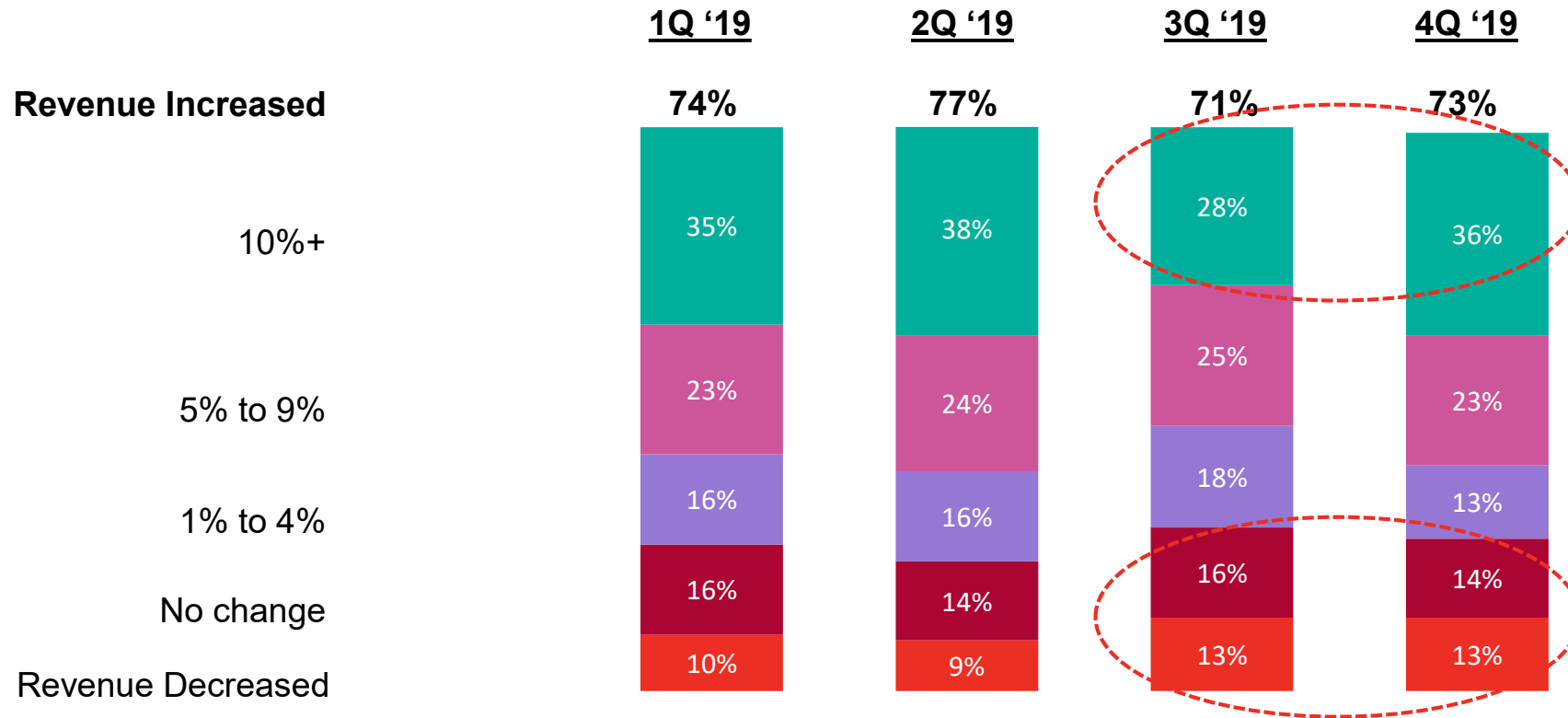


Source: 3Q'19 Middle Market Indicator Report



# 4Q'19 MMI: Strength at the Top, Softness at the Bottom

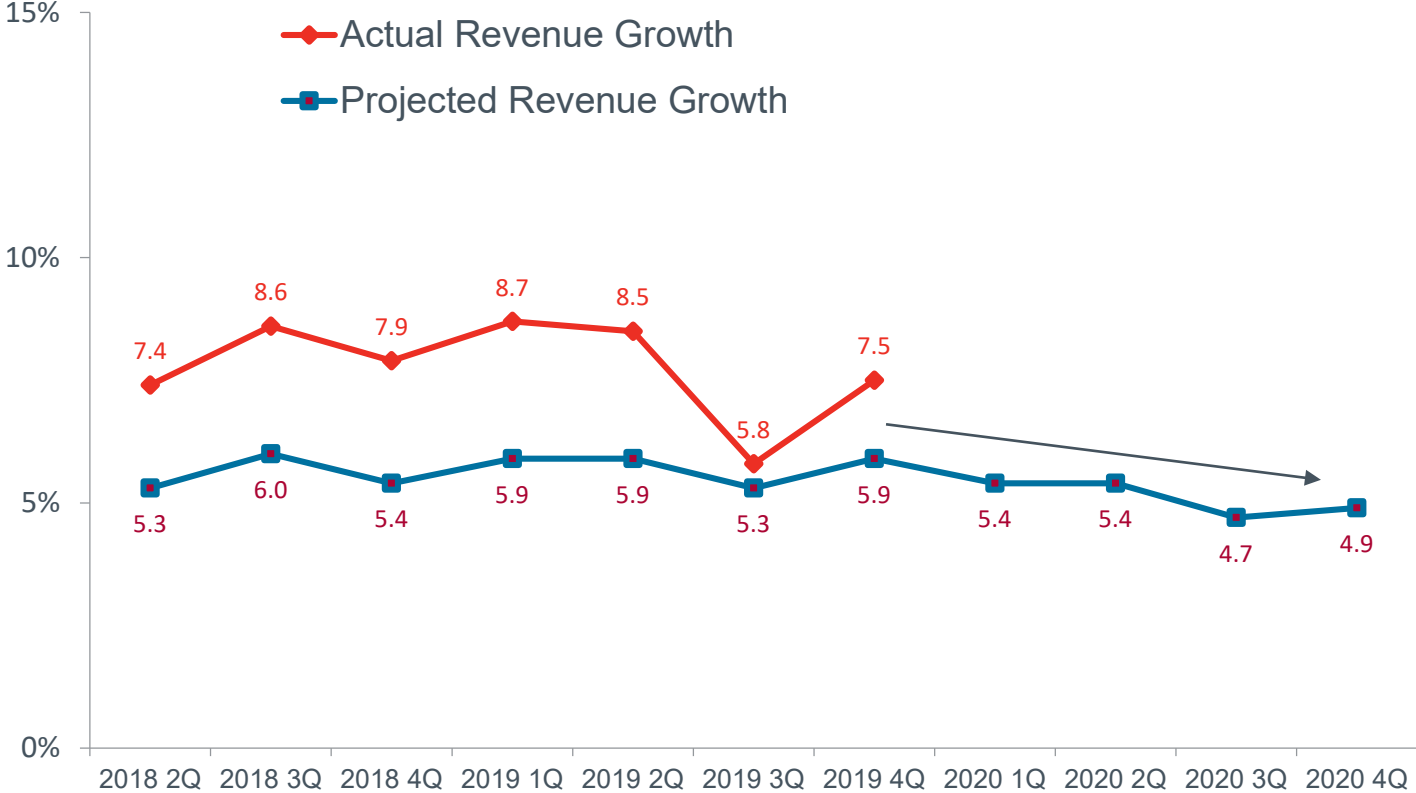
## Past Year Revenue Growth



# 4Q'19 MMI: Winners and Losers

	3Q 2019	4Q 2019
Performance improved	60%	67% ↑
Performance was unchanged	34%	25% ↓
Performance deteriorated	7%	8%

# 4Q MMI: Revenue Growth Forecast



# 4Q'19 MMI: Revenue Growth by Industry



# 4Q'19 MMI: Employment Growth

PAST 12 MONTHS

**5.0%**

U.S. MIDDLE MARKET

0.97%

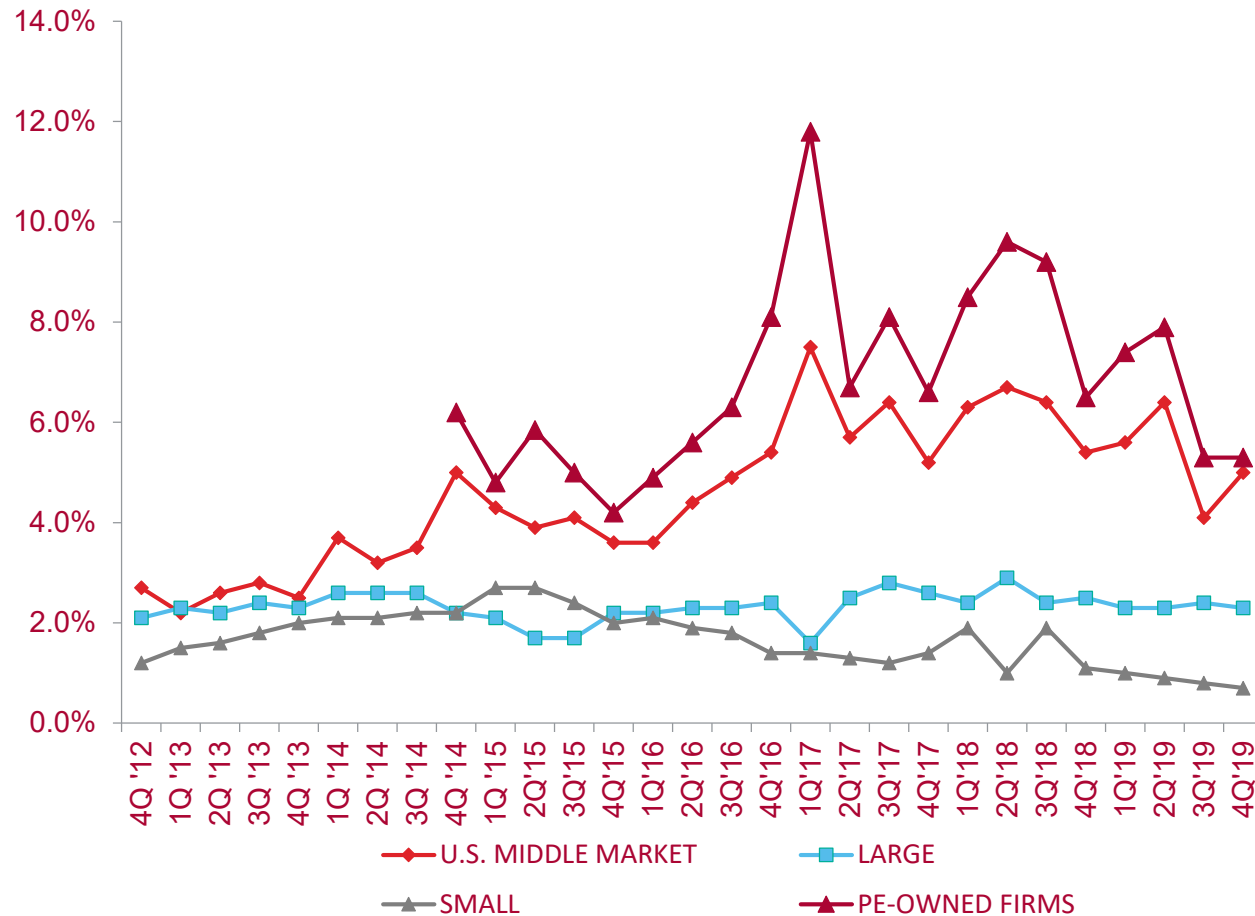
SMALL  
BUSINESS

2.3%

LARGE  
BUSINESS

**5.3%**

PE-OWNED FIRMS



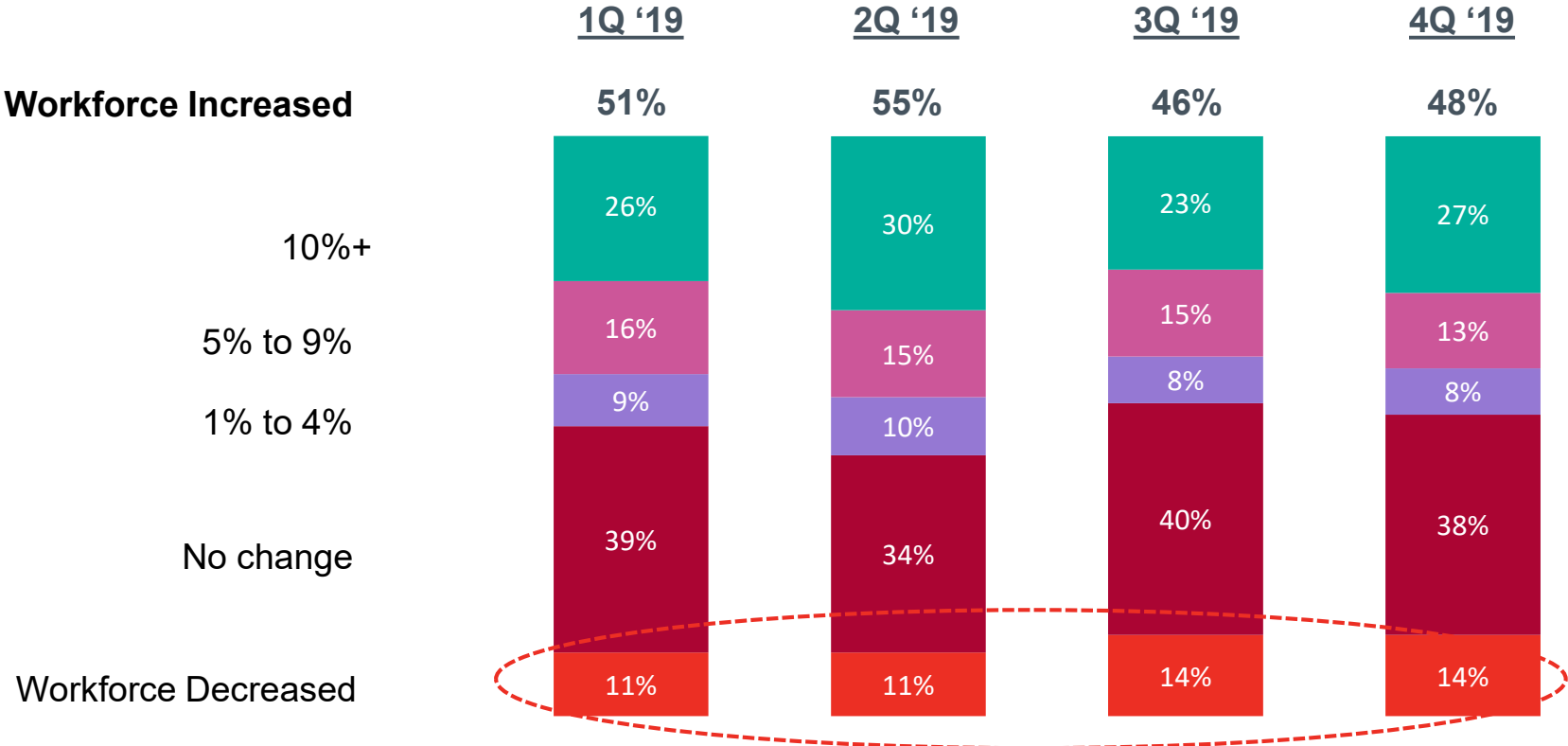
Source: 4Q'19 Middle Market Indicator Report

# 4Q'19 MMI: Employment Growth by Industry

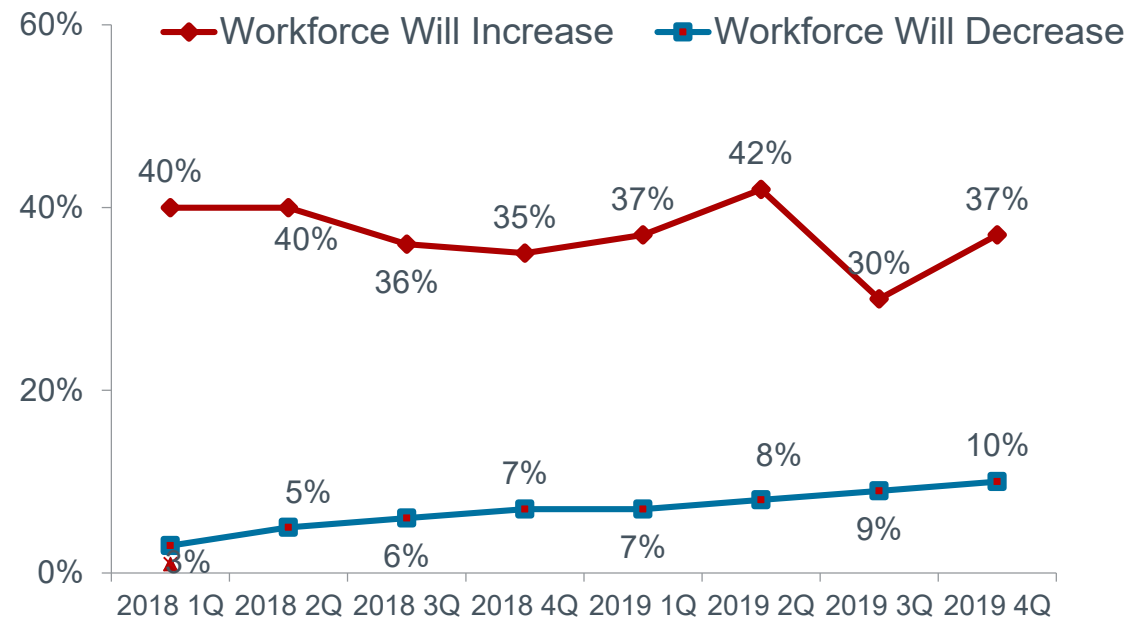


# 4Q'19 MMI: More Companies Have Reduced Workforce

## Past Year Employment Growth



# 4Q MMI: A Slowly Rising Number of Companies Expect to Cut Payrolls





# 4Q'19 MMI: Employment Growth Forecast

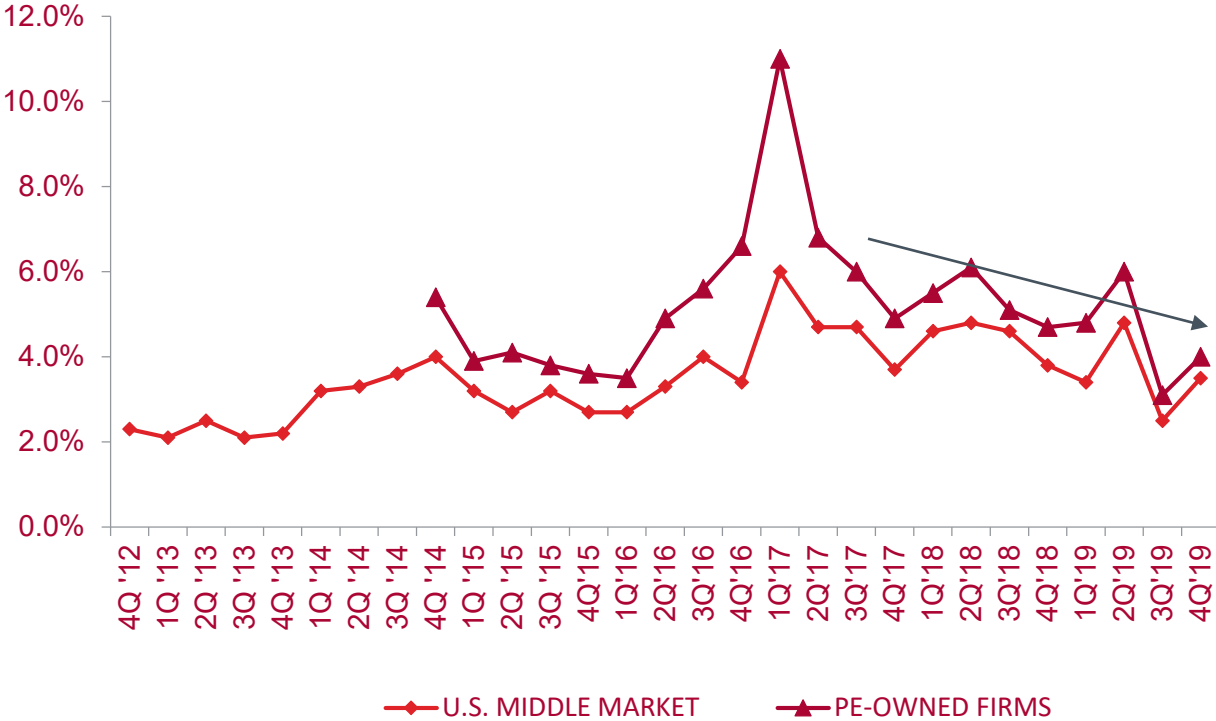
## NEXT 12 MONTHS

**3.5%**

U.S. MIDDLE MARKET

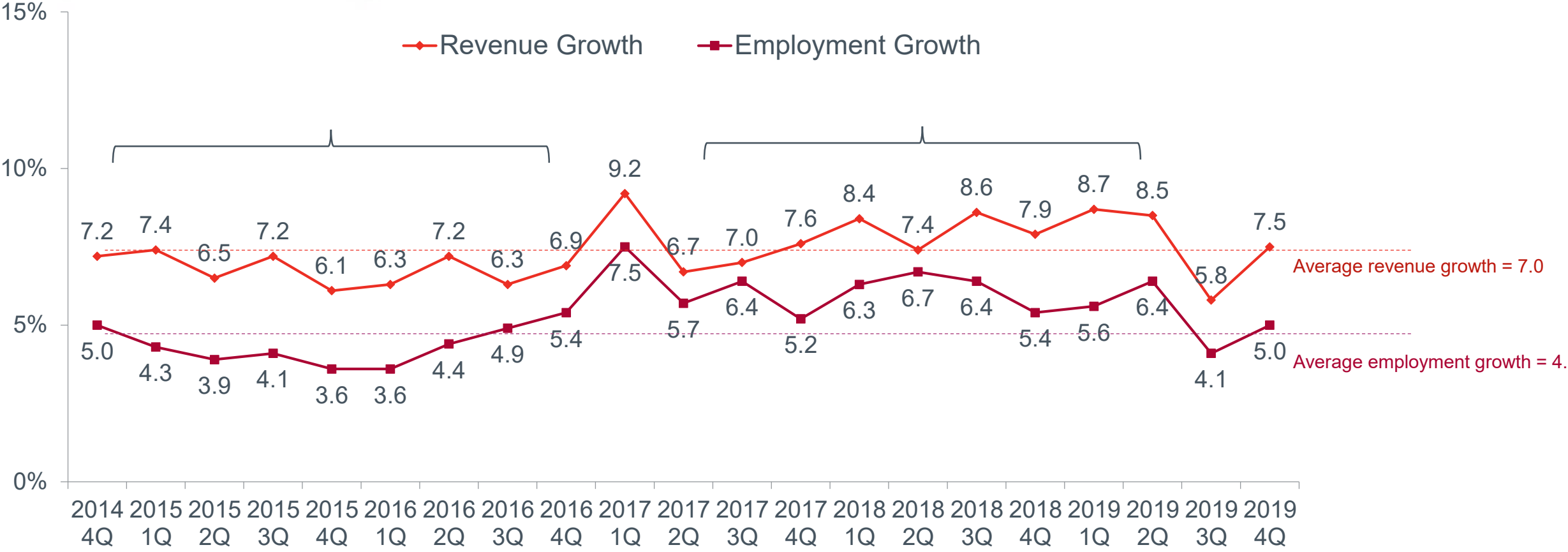
**4.0%**

PE-OWNED FIRMS



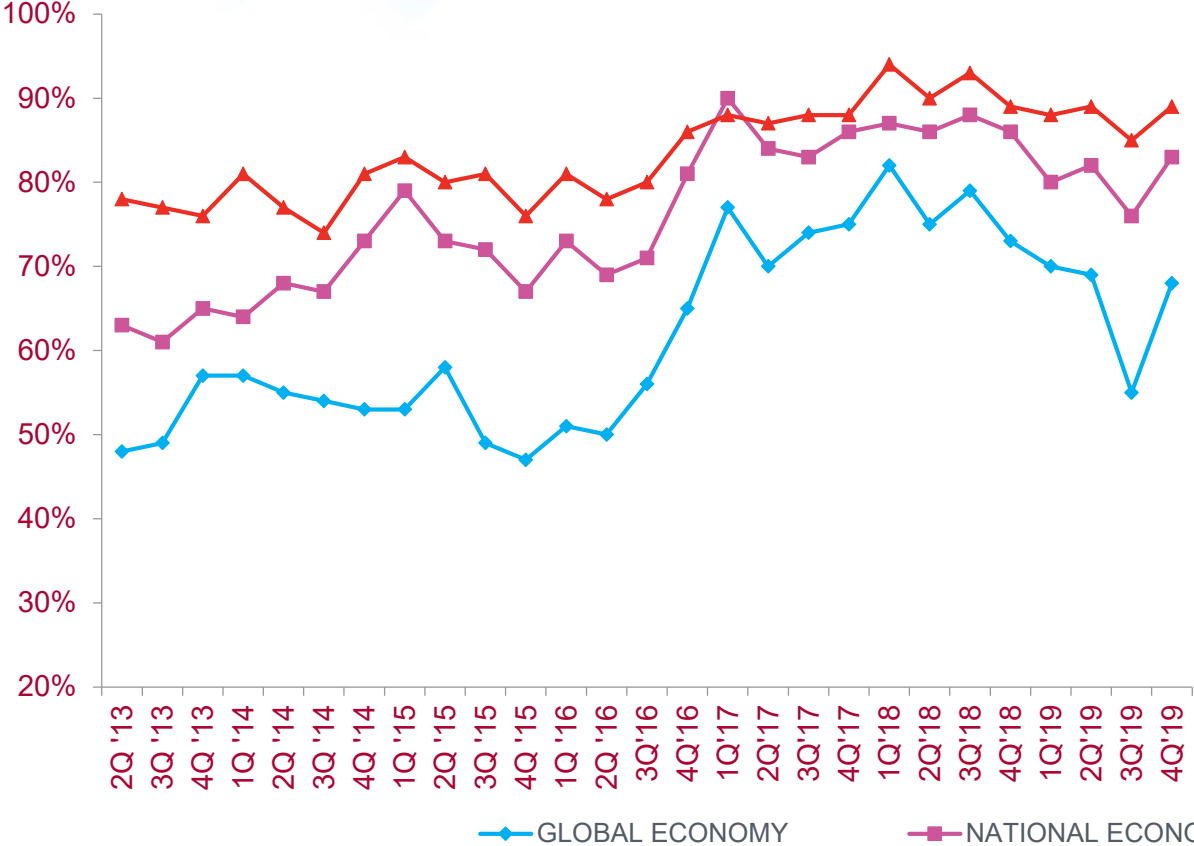
Source: 4Q'19 Middle Market Indicator Report

# 4Q'19 MMI: Revenue and Headcount Trends



Source: 4Q'19 Middle Market Indicator Report

# 4Q'19 MMI: Economic Confidence Has Bounced Back



GLOBAL ECONOMY

68%

75% PE-OWNED



U.S. ECONOMY

83%

85% PE-OWNED



LOCAL ECONOMY

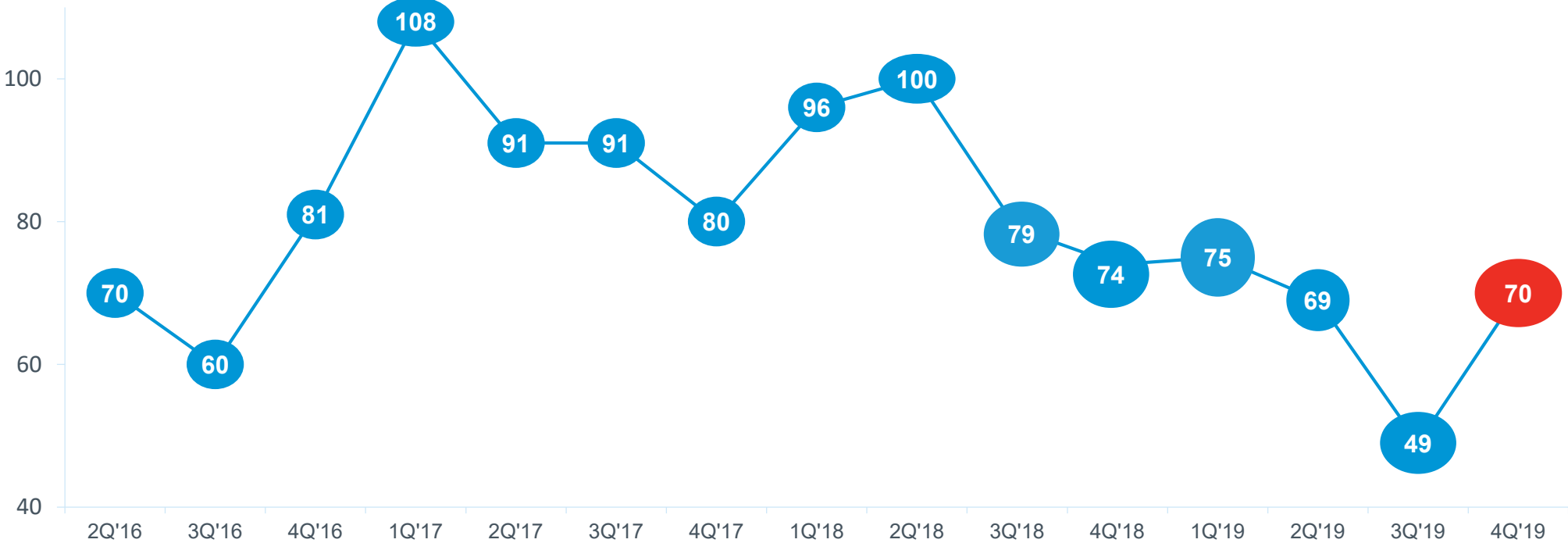
89%

89% PE-OWNED

Source: 4Q'19 Middle Market Indicator Report

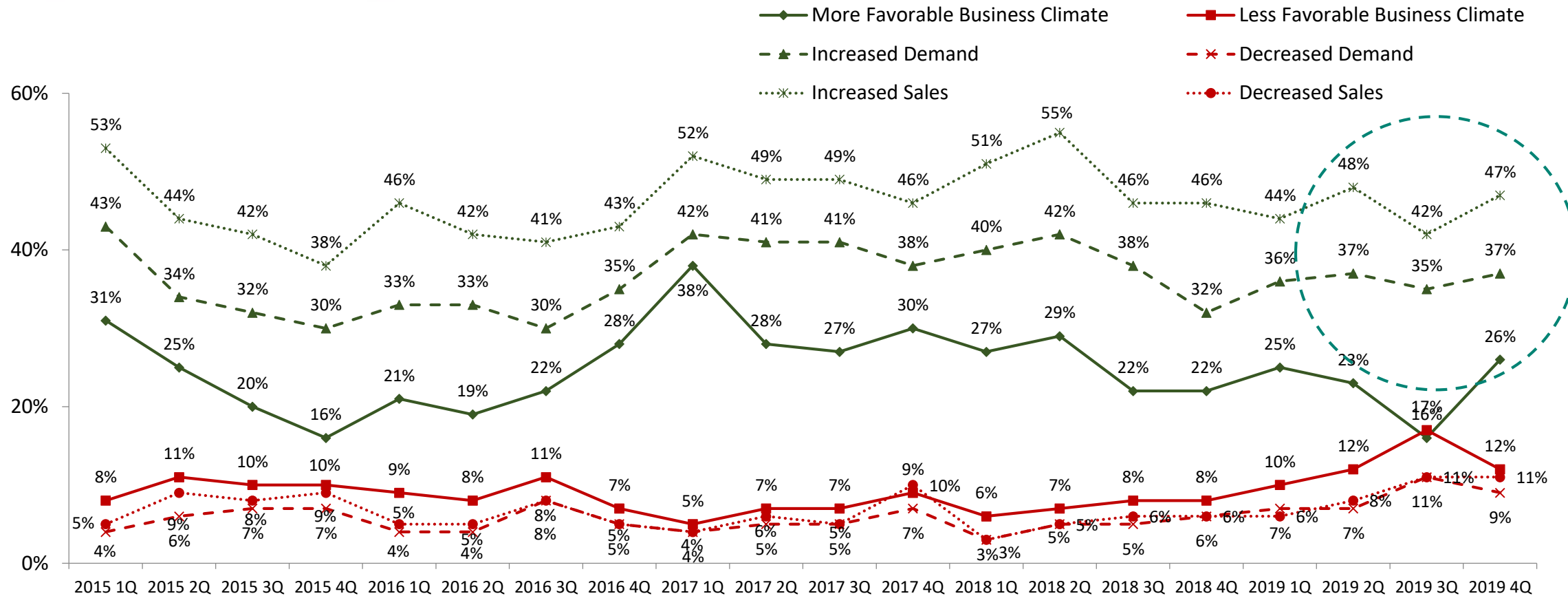
# 4Q'19 MMI: Short Term Index Has Rebounded

*Short Term Index is calculated by taking expected net positive change in business climate plus expected net positive change in demand plus expected net positive change in sales over the next 3 months.*



# Short-Term Sales Forecasts Are Up

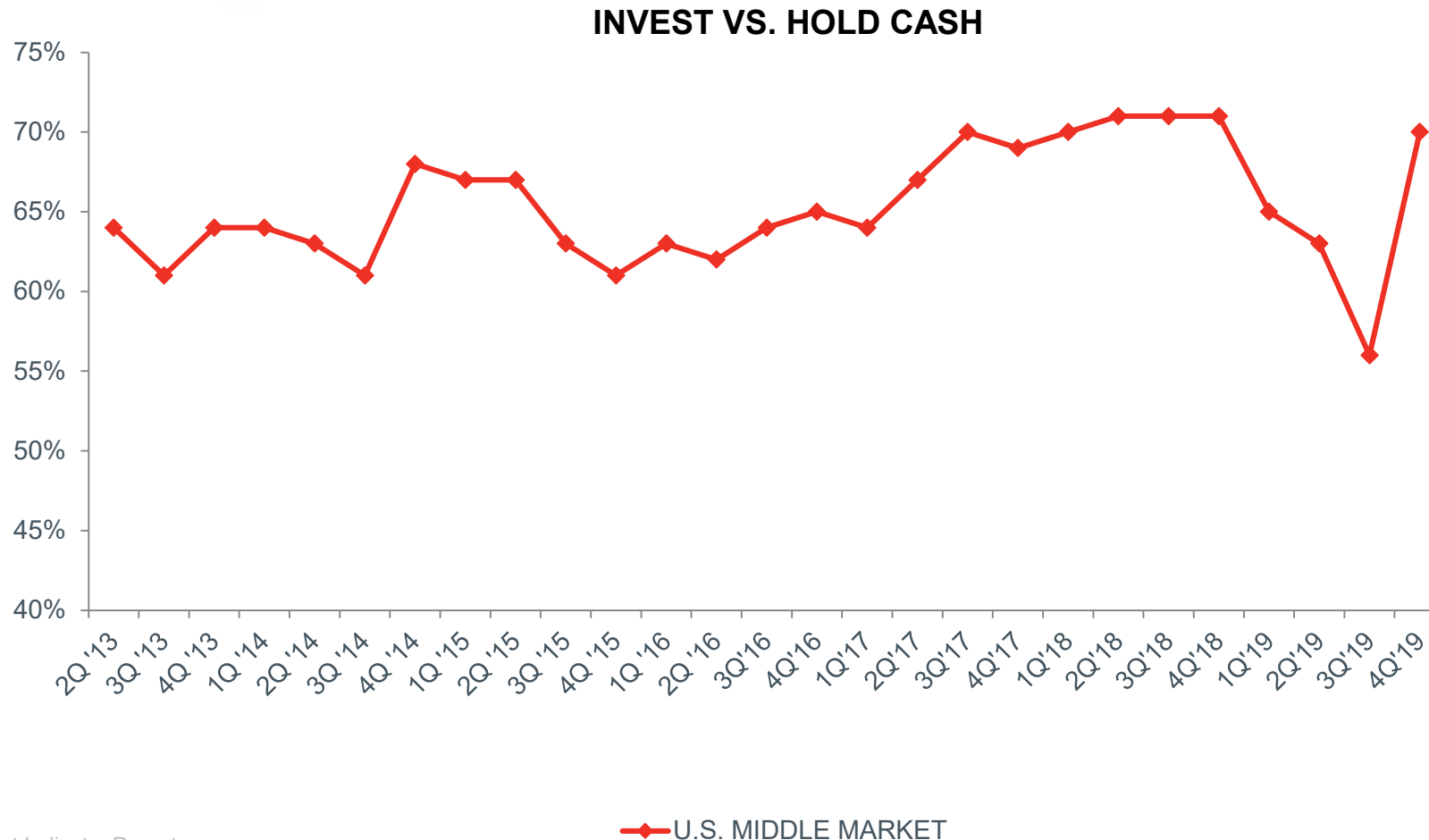
**Short Term Outlook**  
(Next 3 Months)



Source: 4Q'19 Middle Market Indicator Report

# 4Q'19 MMI: Investment Appetites Have Returned

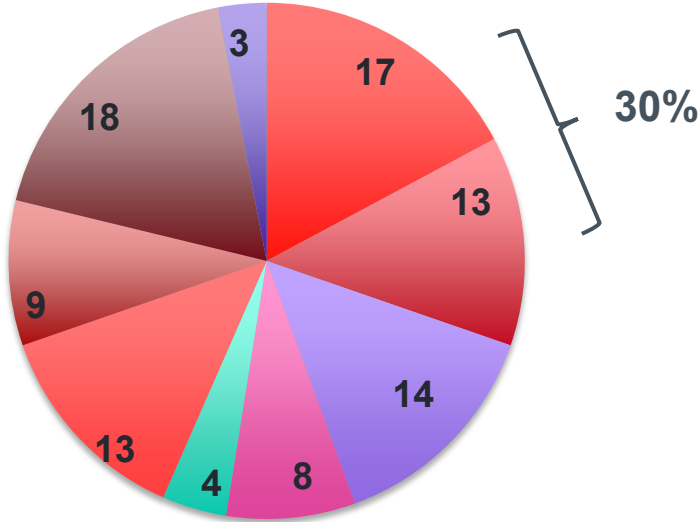
## WHAT WOULD YOU DO WITH AN EXTRA DOLLAR?



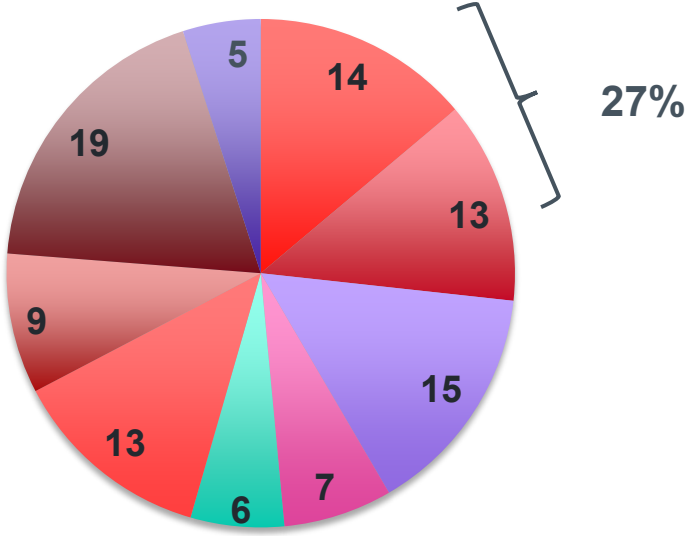
# 4Q'19 MMI: But Rainy-Day Funds Are Still Growing

## WHAT WOULD YOU DO WITH AN EXTRA DOLLAR TO INVEST?

- Save It-Hold as Cash
- Save It--for Making Investments
- CapEx--Plant & Equipment
- CapEx--Facilities
- Acquisitions
- Add to HR--More Personnel
- Add to HR--Training & Development
- IT
- Other



U.S. MIDDLE MARKET



PE-OWNED

Source: 4Q'19 Middle Market Indicator Report

# An Extra Dollar: Priorities

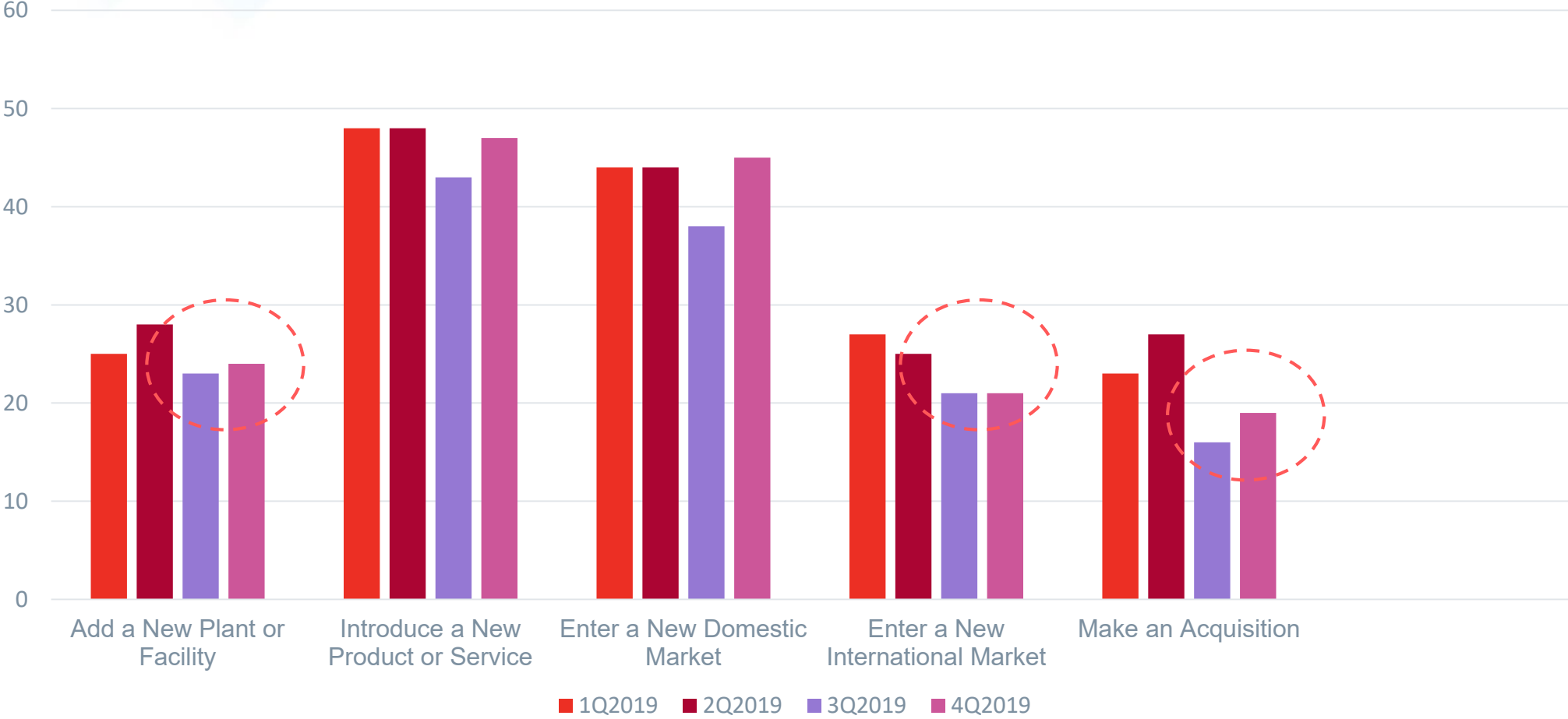


■ IT  
 ■ Cash Reserve  
 ■ Plant / Equipment  
 ■ Hiring  
 ■ Investment  
 ■ Training  
 ■ Facilities  
 ■ Acquisitions  
 ■ Other



# 4Q'19 MMI: Expansion Plans Are Changing Slightly

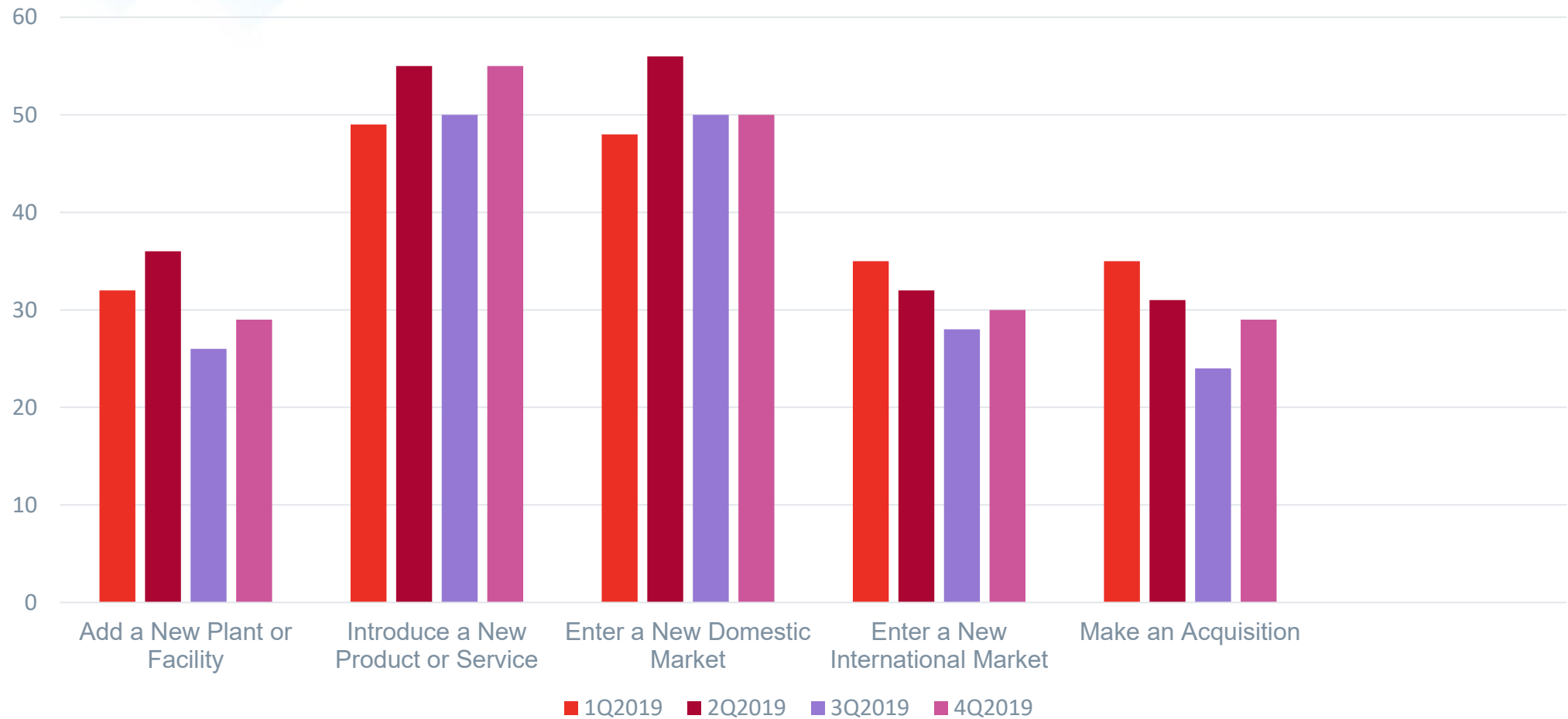
Extremely / Very Likely in the Next 12 Months



Source: 4Q'19 Middle Market Indicator Report

# 4Q'19 MMI: PE Expansion Plans

Extremely / Very Likely in the Next 12 Months



Source: 4Q'19 Middle Market Indicator Report

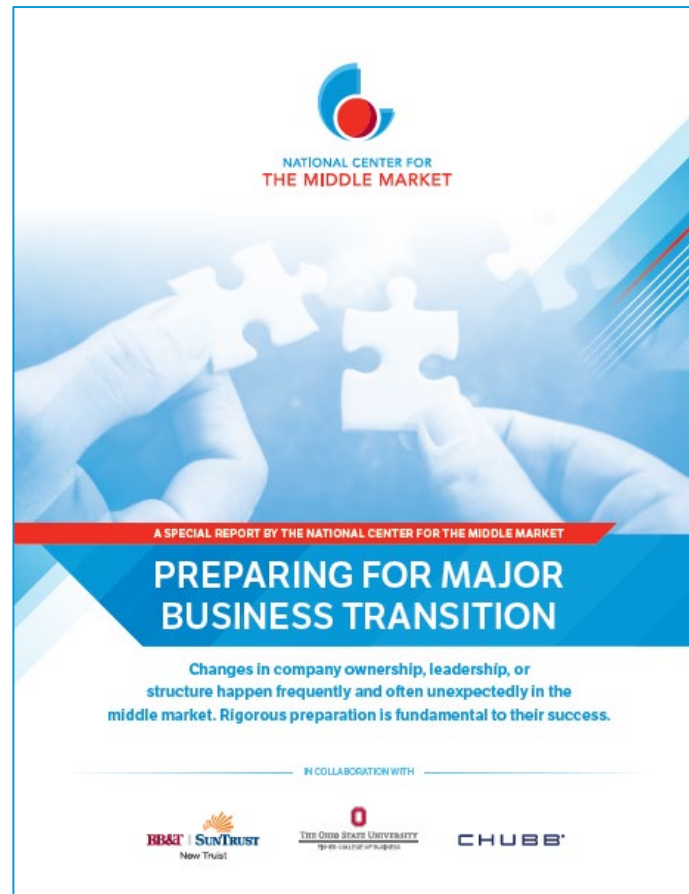
# Preparing for Major Transition

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NCMM Research Report, January 2020

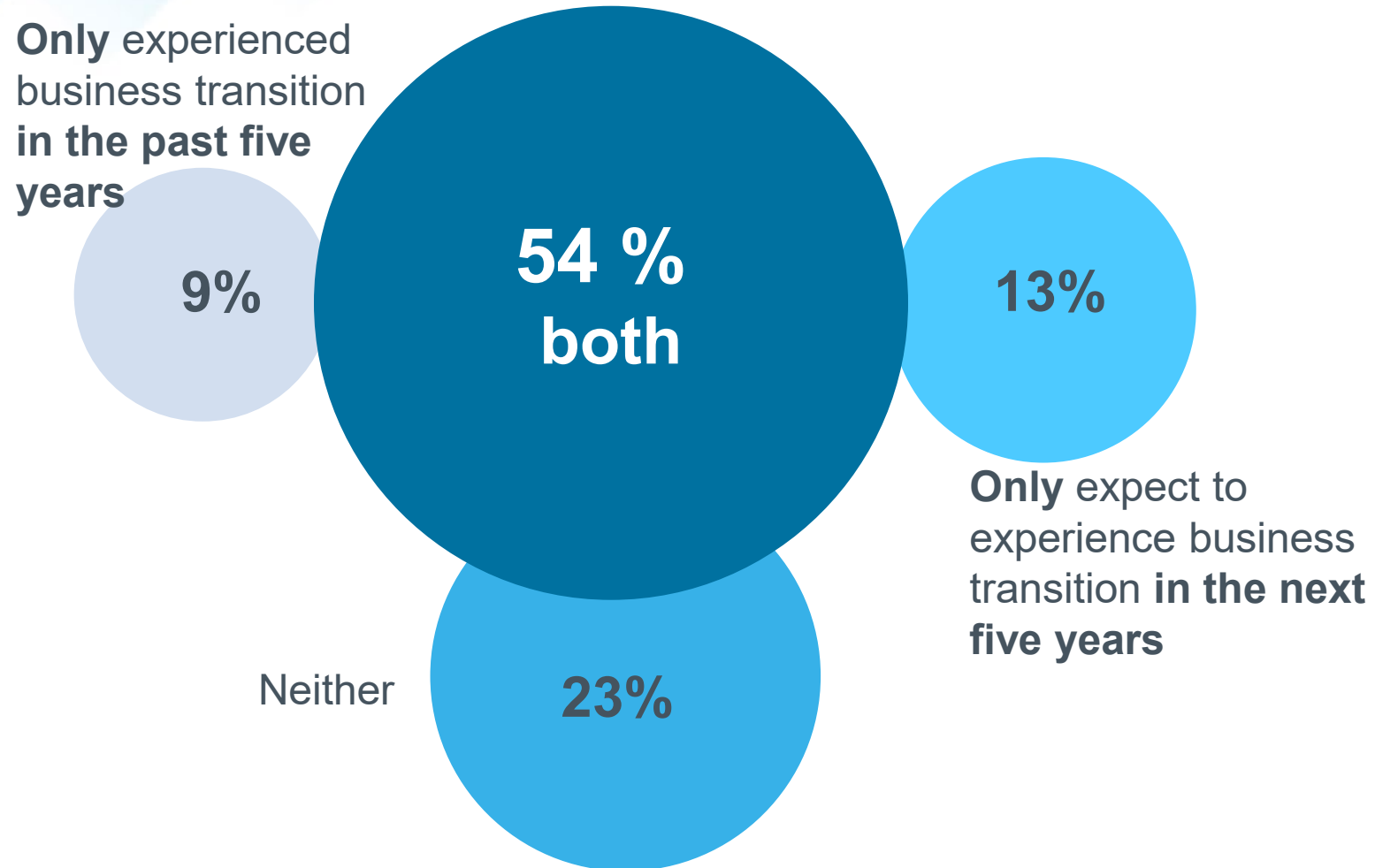
# This research

- Major transitions defined as sale of the company (including strategic, PE, ESOP, going public), merger, bringing in major investor, CEO succession (including intra-family), transformative alliance or JV, restructuring, major divestiture
- Survey of 400 financial decision-makers at middle market companies, conducted November 2019
- Special support and subject-matter expertise from Chubb, SunTrust Banks (now Truist), and Prof. Oded Shenkar, Fisher College of Business, The Ohio State University



- How often do transitions occur?
- How successful are they? What goes right? What goes wrong?
- How well prepared are middle market companies for major transitions?
- What factors influence the success of transitions?
- What is the role of outside advisors in middle market transitions?
- What can companies do to increase their chance of navigating transitions successfully?

# Three out of four middle market companies have experienced transitions or expect to



# Several Factors Increase the Likelihood of Transitions

## ➤ Demographics



40%  
boomer  
owners

## ➤ Dry powder



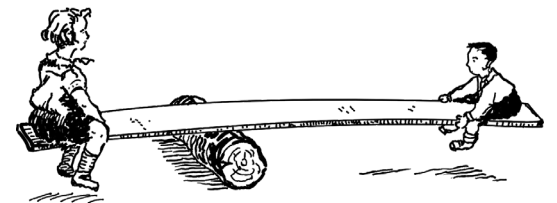
\$2.1  
trillion

## ➤ High valuations



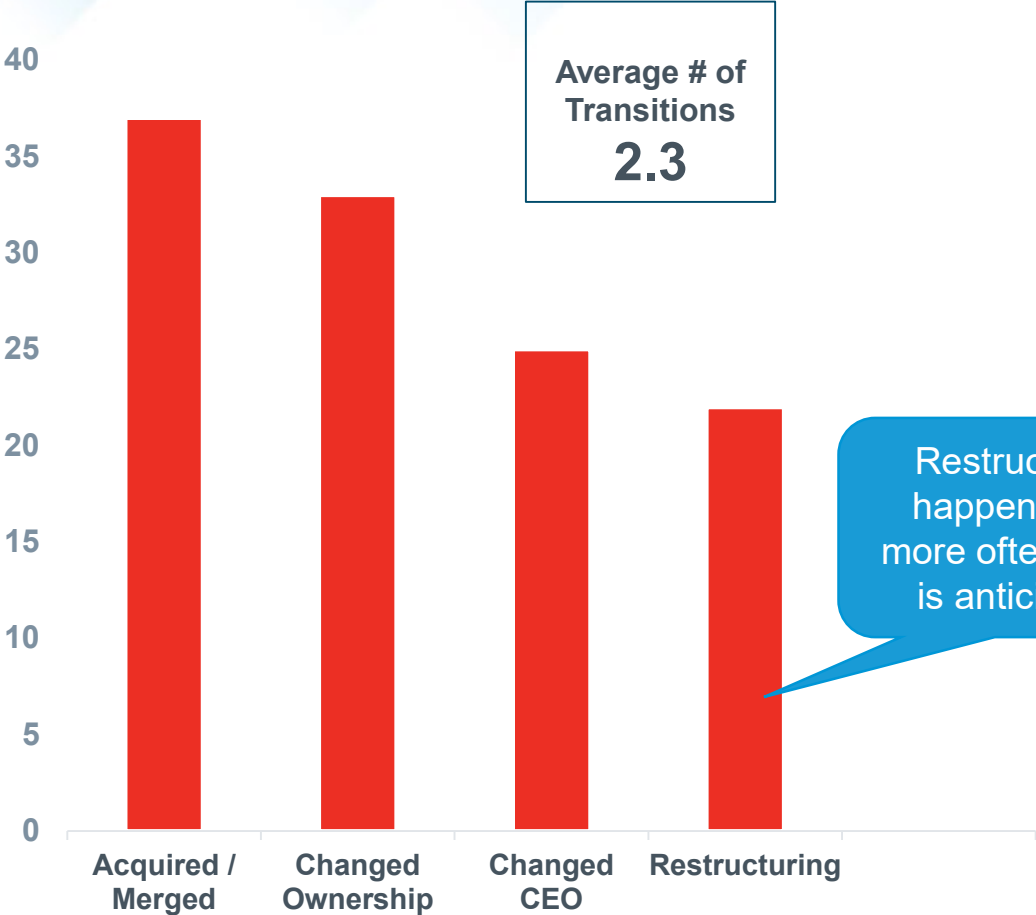
11.1  
X EBITDA

## ➤ Low interest rates

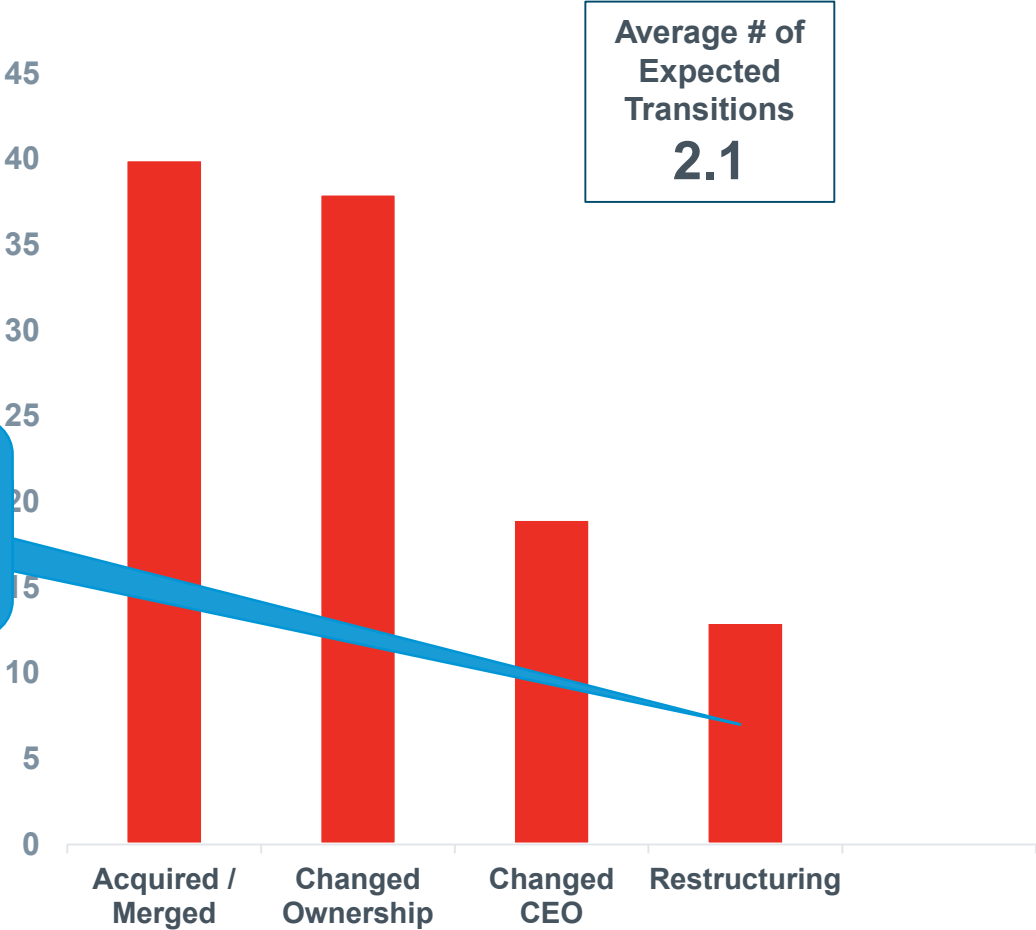


# Acquisitions and Ownership Changes Dominate

Transitions Experienced in Past 5 Years \*



Transitions Likely To Experience in Next 5 Years\*



Source: NCMM, Preparing for Major Business Transition, 2020

\*Among companies that expect to experience one or more transitions

# Positive Outcomes Usually Outweigh Negatives

## NEGATIVE OUTCOMES



**49%**  
had some  
negative  
outcomes

## POSITIVE OUTCOMES



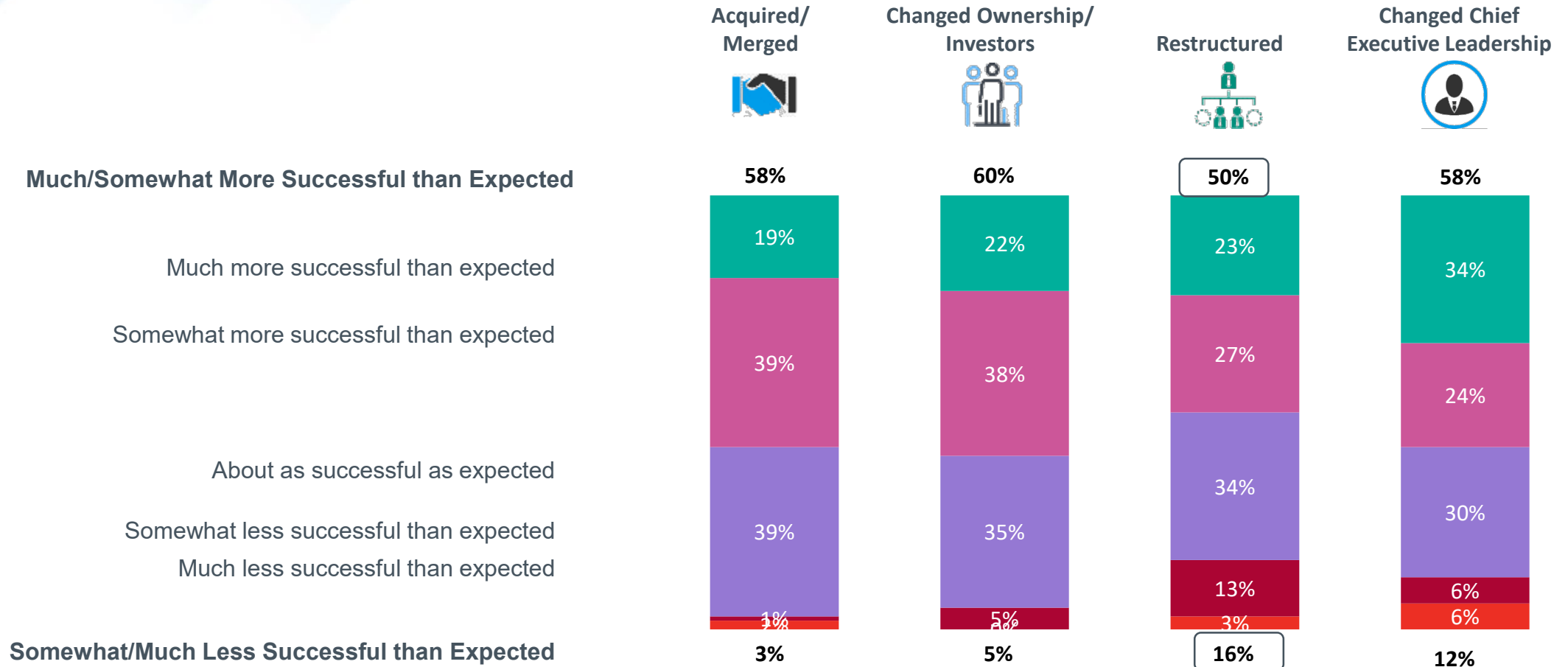
**77%**  
had some  
positive  
outcomes

**BIGGEST NEGATIVES: PEOPLE ISSUES**  
**BIGGEST POSITIVES: FINANCIAL GAINS**



# Success in Restructuring Lags Other Transitions

## SUCCESS OF MOST RECENT BUSINESS TRANSITION COMPARED TO EXPECTATIONS



# Top Challenges Vary Depending on Transition Type

PERCENT CITING AN ISSUE AS EXTREMELY OR VERY CHALLENGING

## Acquired / merged

Assessing fit / culture	36%
Understanding and working through options	32%
Assembling the right internal / external team	31%
Assessing risks	30% (tie)
Dealing with tax issues	
Maintaining confidentiality / controlling rumors	

## Changed ownership / took on investor

Valuation	48%
Handling due diligence	41%
Getting alignment from family members	38%
Maintaining confidentiality / controlling rumors	37% (tie)
Ensuring business continuity	

## Changed Chief Executive

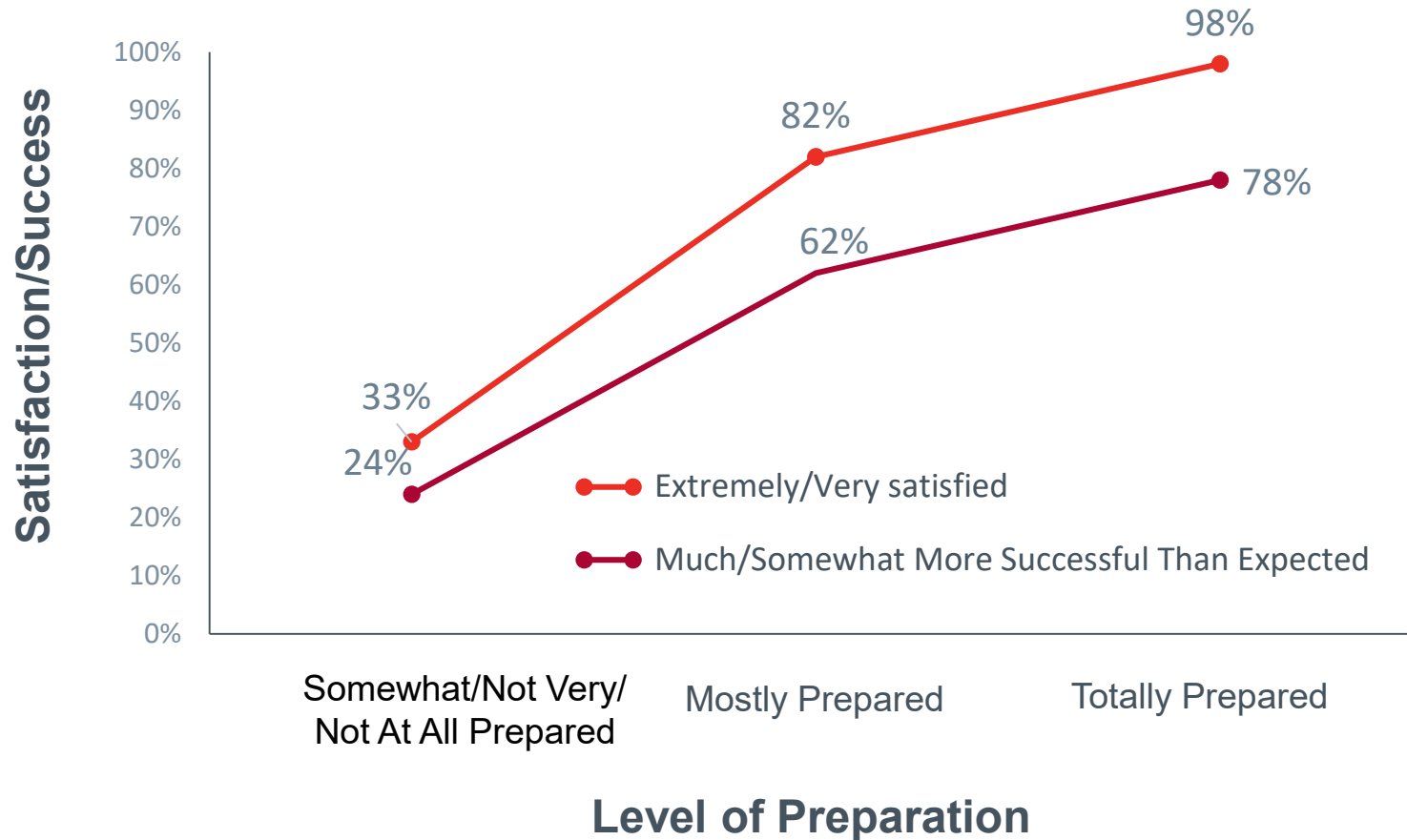
Getting alignment from company leaders, key employees	38%
Deciding who will take over	36%
Maintaining confidentiality / controlling rumors	29% (tie)
Assembling the right internal / external team	
Assessing risks	

## Restructured

Maintaining confidentiality / controlling rumors	47%
Assessing risks	42% (tie)
Employee communications	
Assembling the right internal / external team	41% (tie)
Getting alignment from company leaders, key employees	
Getting alignment from family members	

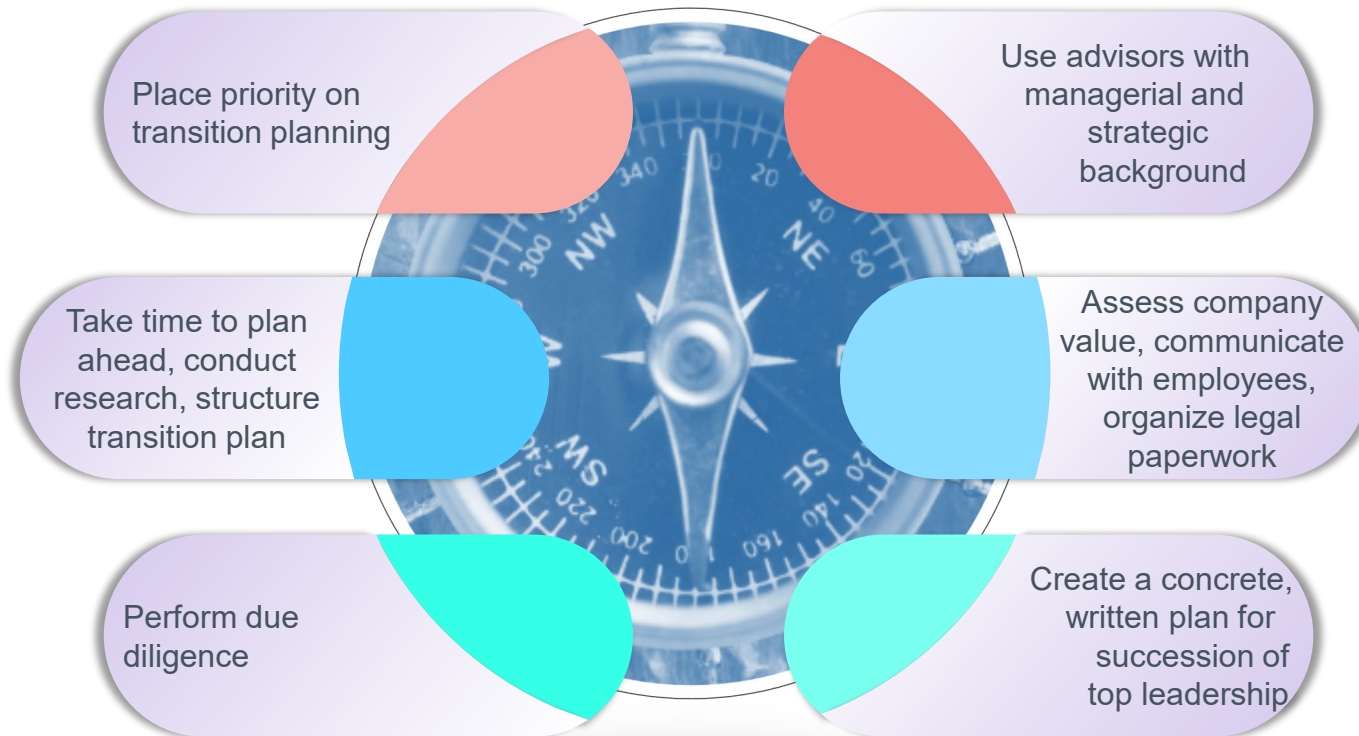
# The Essential Ingredient for Success: Preparation

Satisfaction & Success of the Most Recent Business Transitions Based on Preparation Level



# What Preparation Entails

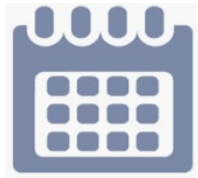
## Key Elements of a Successful Transition



# Most Companies Start Planning Late

## WHEN PROCESS OF PREPARATION FOR THE MOST RECENT BUSINESS TRANSITION BEGAN

Mean:  
1.3 years  
before the transition occurred



Acquired/Merged  
1.2 years



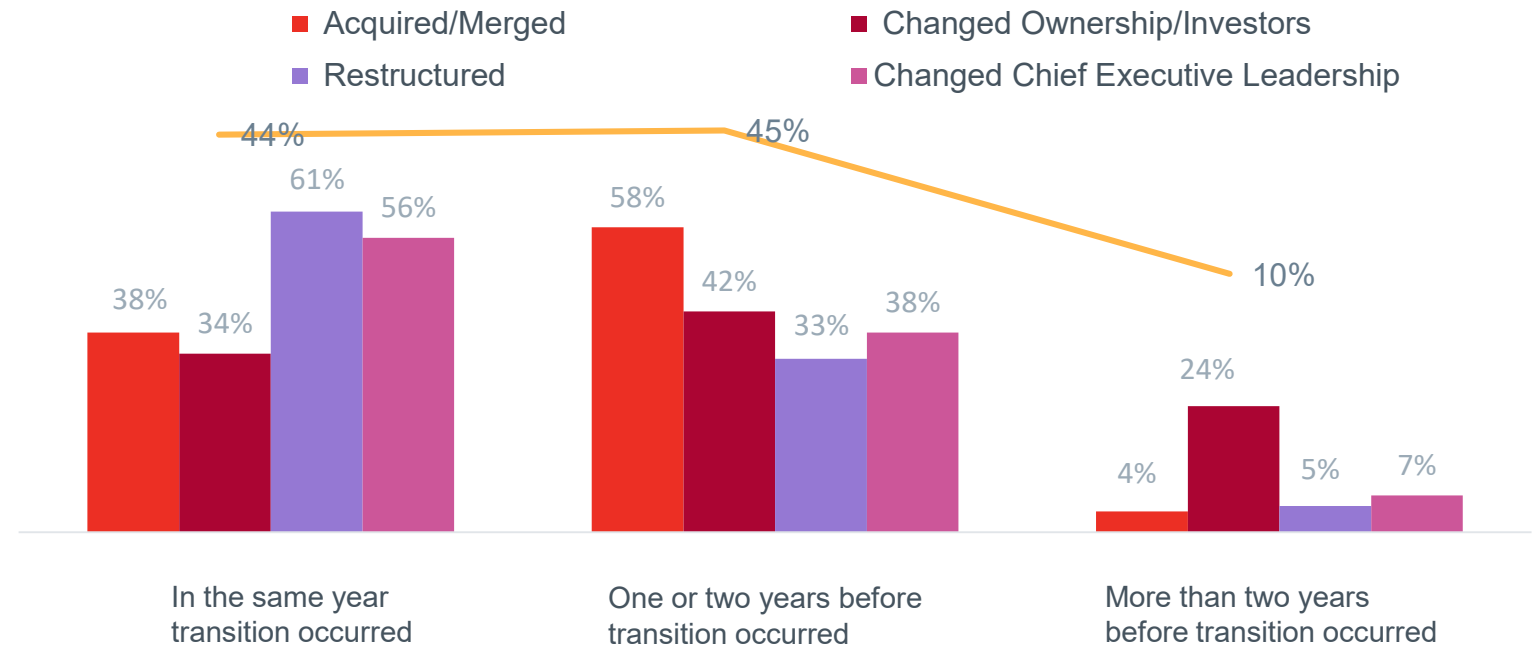
Changed  
Ownership/Investors  
1.6 years



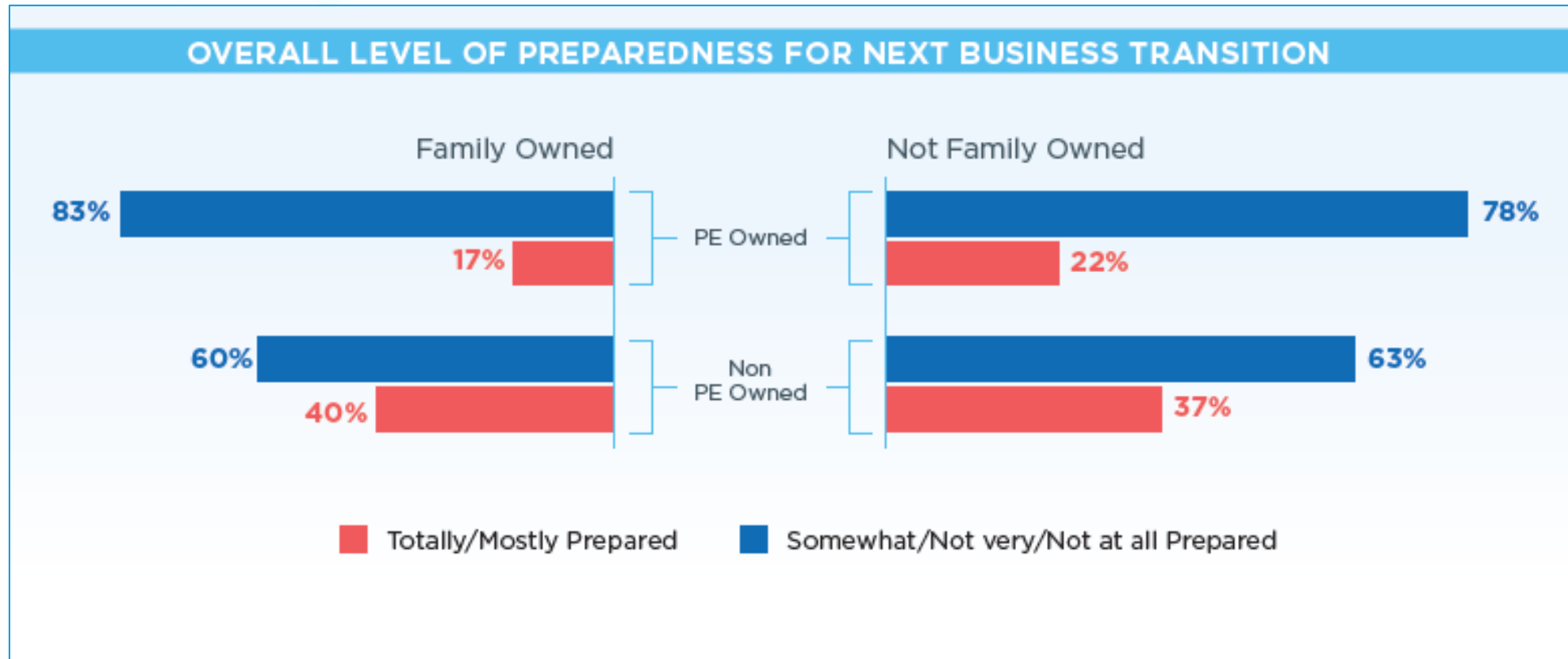
Restructured  
1.0 years



Changed Chief Executive  
Leadership  
1.1 years

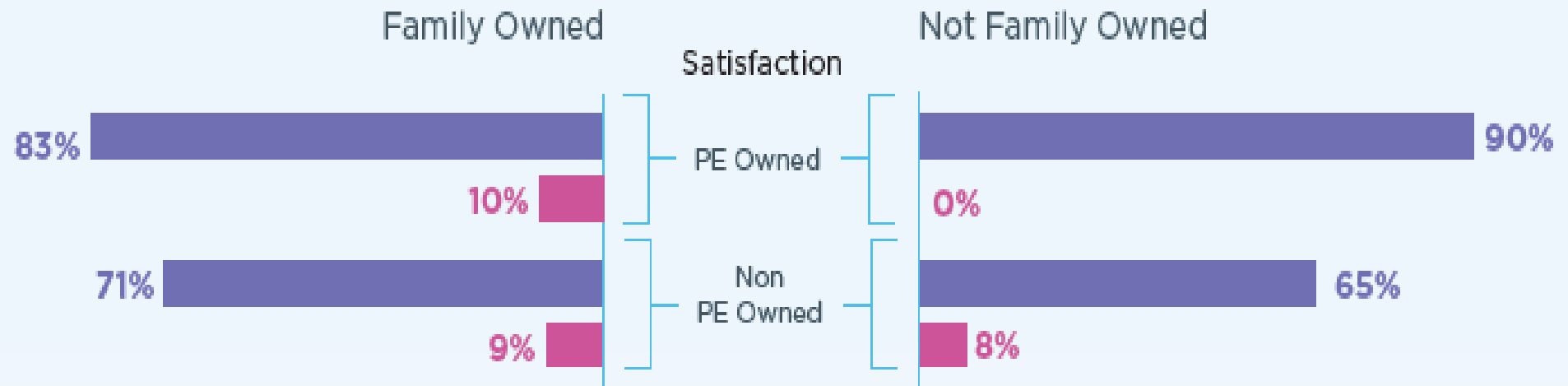


# Family Businesses with PE Investment Are the Most Prepared ...



# Family Businesses with PE Investment Are the Most Prepared ... and the Most Satisfied

## TRANSITION SATISFACTION AND SUCCESS IS HIGHER IN COMPANIES WITH PE FUNDS



# Leaders Are Confident of General Management Ability, But Not Transition Expertise





# The Green Zone and the Red Zone

## PLAN IN THE GREEN ZONE

The business is humming, with stable leadership and satisfied investors; the issues it faces are “good problems”—strategy, growth, profitability, customer satisfaction, etc. No transition is visible on the horizon.

**TAKE CHARGE OF YOUR FATE BEFORE  
SOMEBODY ELSE DOES**

## ACT IN THE RED ZONE

Something happens that makes you realize a transition will come very soon: health problems, divorce, family issues, an unsolicited offer, planned retirement, competition changes, loss of a major customer, etc. The clock is ticking.

**TRANSITION IS THE #1 PRIORITY OF  
TOP MANAGEMENT AND OWNERS**

# What Leaders Should Do in the Green Zone

- Have “the talk.” Begin with the end in mind. Include personal as well as professional
- Clean up your books. You’ll run a better business, and get a better deal
- Upgrade your stable of advisors to include people with transition expertise
- Clarify decision rights—now, rather than when transition is imminent
- Improve daily management: strategic planning, operations, working capital
- Check and upgrade risk management, including cybersecurity
- Deepen your ties to your best customers and employees

# What Leaders Should Do in the Red Zone

- Don't panic. If you planned in the Green Zone, you're ahead of the game. Regardless, you probably have many elements of a plan, however informal
- Appoint a transition war room. Separate the transition from the need to run the business. Make sure the continuing operations team has the authority it needs
- Rank your priorities. Price? Speed? Legacy? Decide which outcomes matter most
- Assemble a savvy advisory team. There is no time for a learning curve in the red zone! Clarify their roles. Banker, lawyer, consultant, tax expert—different transitions require different advisory skills
- Communicate as much as you dare, then communicate more. Employees, customers, and others will know something is up; the less you say, the more they will imagine the worst—and the less likely they will be there post-transition



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