The Pulse of Private Equity: Buyouts & Add-Ons

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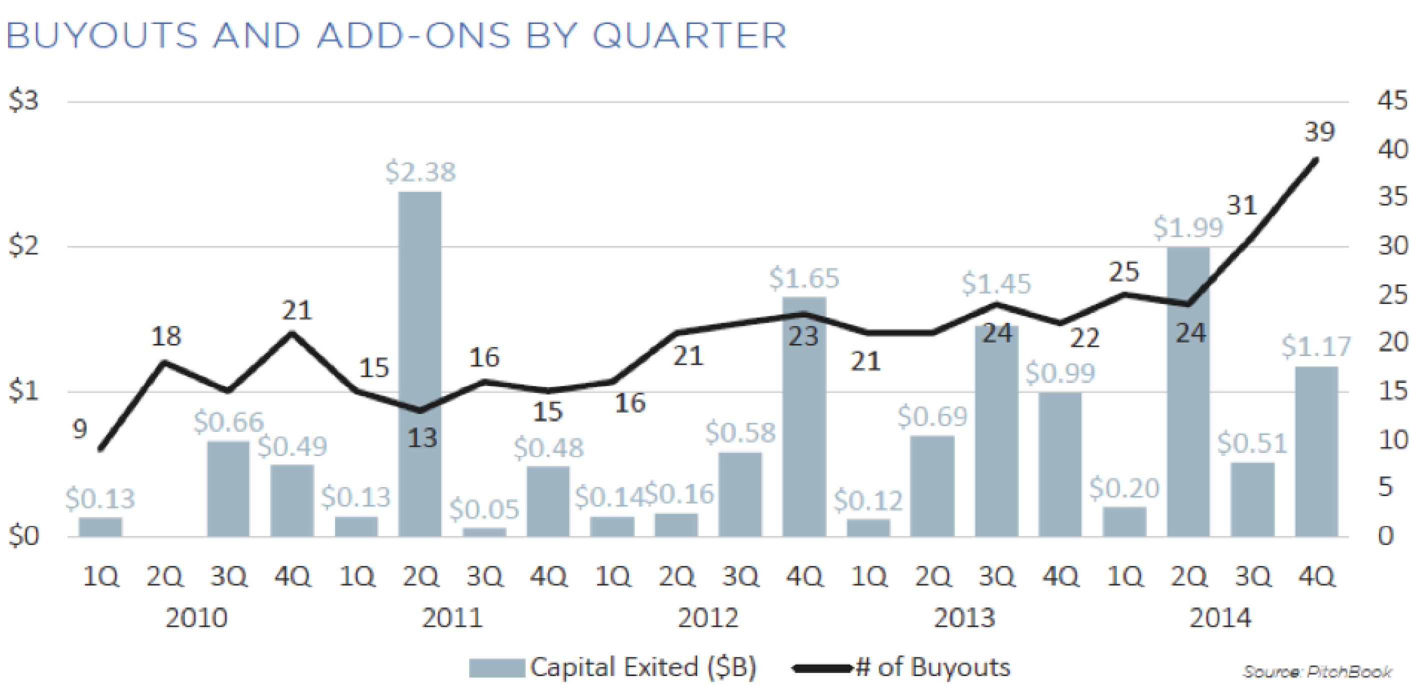
Private equity is buying startups more often

Private equity isn't known as a big buyer of VC-backed startups, but that's beginning to change. There were 119 buyouts of VC-backed companies in 2014, a substantial increase (35%) from the 88 recorded in 2013. The 39 buyouts completed in 4Q 2014 were the most of any quarter in history.



Two things are going on today that help explain this. For one thing, PE firms have shifted to more of a buy-and-build approach, growing their existing platforms through smaller add-on acquisitions. A number of VC-backed companies fit that bill, given their size and market share. But the bigger factor behind the VC-to-PE trend goes back to the PE industry itself. As we've said in previous articles, private equity has become much more specialized and knowledgeable in niche sectors, particularly within the healthcare and IT industries. Specialty SaaS providers and medical device manufacturers, for example, have become much more viable investment options for PE, and many of those companies have already been financed and nurtured by VC investors for years. For PE buyers looking to build out their platforms, the issue of anemic cash flow hasn't been as problematic, since investors can factor in synergy capture through add-ons as opposed to buying startups as platform investments. As long as the PE industry continues to develop and gain expertise in these niches sectors, we should see PE and VC investors connect more often down the road.

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