Q3 2025 EDITION

Pursant
INSPIRED PURSUIT

DEAL insider
M&A and Strategic Transaction Insights

Q3 2025 Highlights

- Deal flow slow but steady in Q3 as Buyers regained confidence and selectively pursued high-quality assets
- Valuations held firm thanks to gradually improving credit markets and stronger lender appetite
- Private Equity leaned in on add-ons, keeping the middle market active despite uneven macro signals

Pursant's Thoughts for the End of this Year

- Financing loosening up, pushing valuations and deal intensity higher, setting the stage for a favorable Q1 2026
- PE and strategics more actively hunting for high-quality, resilient middle-market companies
- Q4 primed for a pickup in activity, great news for Sellers who are ready

2025 Middle Market M&A Volume Up but Activity Remains Weak

Q3 2025 showed the first signs of a modest total value (aggregate value of deals) rebound after a lower first half. The deal value increase was driven largely by bigger, better-capitalized transactions, while overall deal activity (number of deals) remained subdued. In other words: more dollars moving, but not yet more deals in a meaningful way.

Private equity activity strengthened, with larger add-ons and platform deals pushing quarterly deal value sharply higher compared to earlier in the year. Valuation multiples in the middle market ticked up, reflecting competition for higher-quality companies and a slight easing in financing conditions.

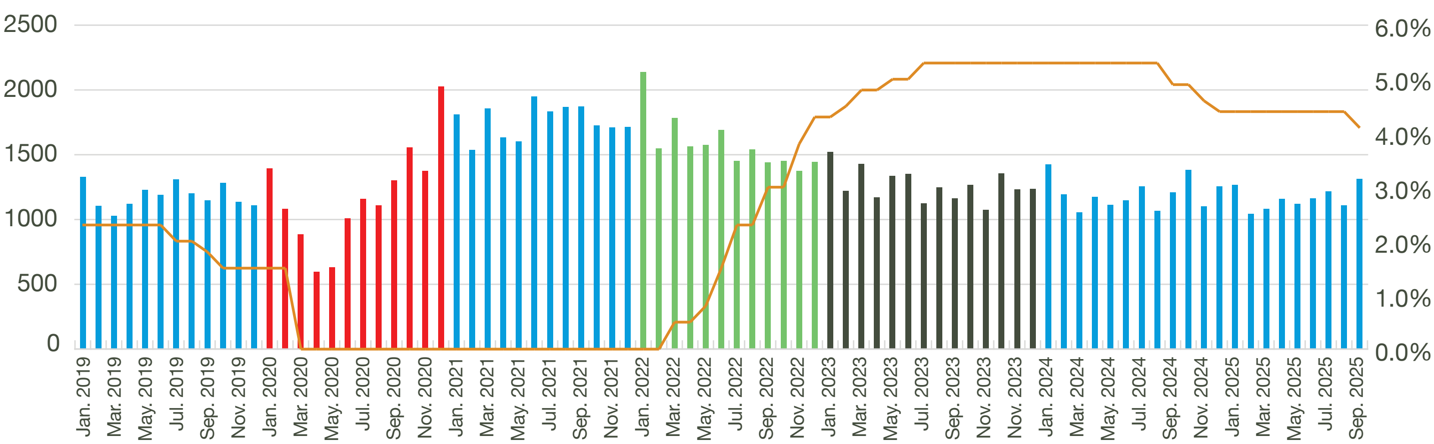
The improvement was largely seen at the upper end of the middle market, while the lower end of the middle market continues to face headwinds. Smaller transactions are still harder to get across the finish line, and many Buyers remain selective, focusing only on targets with strong fundamentals. Businesses with recurring revenue, defensible market positions, and limited exposure to global supply-chain issues or input-cost volatility continue to attract the most attention.

Sector performance in Q3 showed a shift: industrials and services remain active and resilient, while technology, infrastructure, and energy-related deals are contributing more meaningfully to overall deal value. Conversely, sectors with higher regulatory exposure or more volatile demand patterns are still seeing limited Buyer engagement.

In summary, Q3 brought improvement, but not a full recovery. Buyers are active, capital is available, and strong companies are still commanding premium valuations. However, many smaller deals remain stalled, and overall market momentum continues to build slowly rather than decisively.

Chart #1

2019-2025 US M&A Volume (# of Deals) & Fed Funds Rate



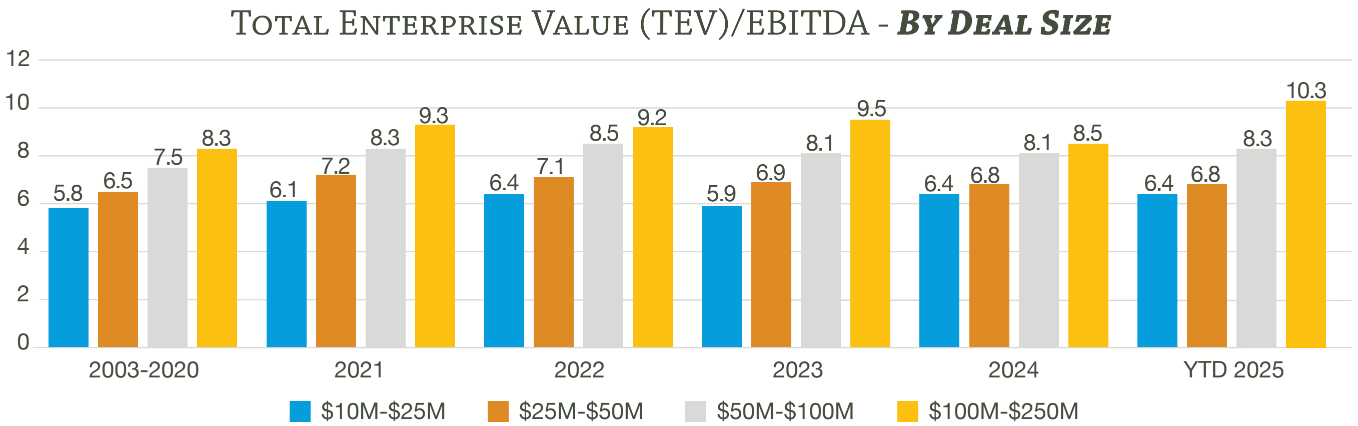
Source: Factset®

Valuation Multiples More Favorable for Larger Middle Market Deals

Chart 2 illustrates that Average purchase price multiples rebounded to 7.5x TTM adjusted EBITDA in the third quarter from 6.9x in Q2, reversing the modest decline seen earlier in the year. Valuation gains were concentrated in the $50 million to $250 million total enterprise value (TEV) tiers, where scale and access to financing provided an advantage in the current credit environment. Smaller deals continued to hold steady, facing pressure from cautious lenders.

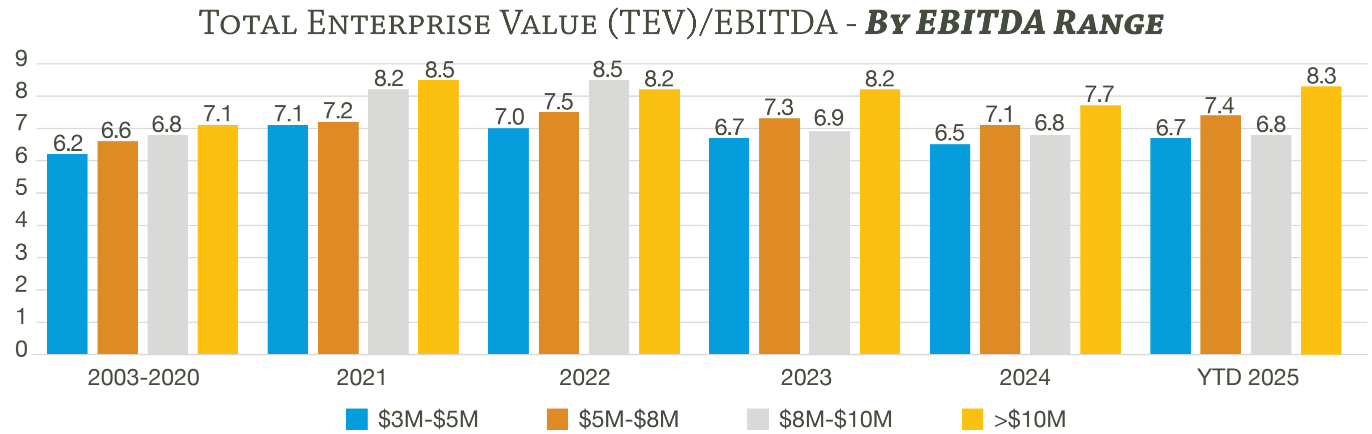
For another perspective, see Chart 3, which shows valuation multiples on an all-industries basis by EBITDA range, rather than by deal size. This chart shows that average TEV/EBITDA multiples increased slightly on a four-quarter rolling basis to 7.3x in Q3 2025 from 7.2x in Q2, signaling a modest uptick in overall valuations. The increase points to selective buyer optimism and again, steady demand for larger, higher-quality companies even as broader market conditions remain cautious.

Chart #2



Source: GF Data®

Chart #3



Source: GF Data®

EBITDA Defined *– For most middle-market businesses, valuation is typically expressed in the form of a multiple of EBITDA (earnings before interest, taxes, depreciation, and amortization)—a measurement of a company's ability to generate cash flow. EBITDA figures also serve as a barometer of the company's health and performance. Multiples of EBITDA vary greatly depending on a company's risk profile, the markets in which it operates and the likelihood of continued returns.*

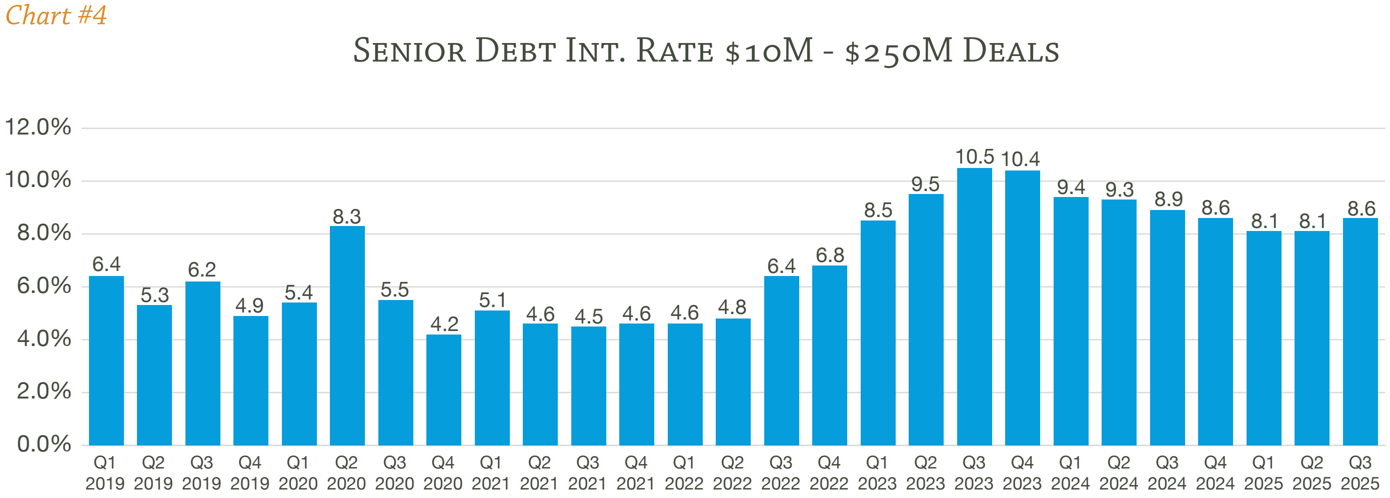
M&A Lending Shows Minimal Change in Leverage Levels and Pricing

Chart 4 reflects Senior debt pricing reversing course slightly, increasing by roughly 50 basis points to 8.6% in Q3 from 8.1% in the second quarter. This uptick follows six quarters of declining senior pricing, signaling renewed upward pressure on borrowing costs as competition among non-bank lenders softens and banks become more selective. For platform deals, pricing for bank-led senior tranches remained in the 7.5–8.0% range, while non-bank and ***unitranche credit facilities priced between 8.5–12.0%***.

Subordinated debt pricing, meanwhile, dropped to its lowest level in eight quarters, ranging between 11.2% and 12.7% across size tiers, after reaching a peak in the second quarter. Mezzanine lenders continue to maintain spread discipline despite limited volume, reflecting persistent perceived risk in smaller and cyclical credits. ***All-in pricing on subordinated debt including PIK and fee components held steady at approximately 15.4% year-to-date***, compared to 15.5% in 2024.

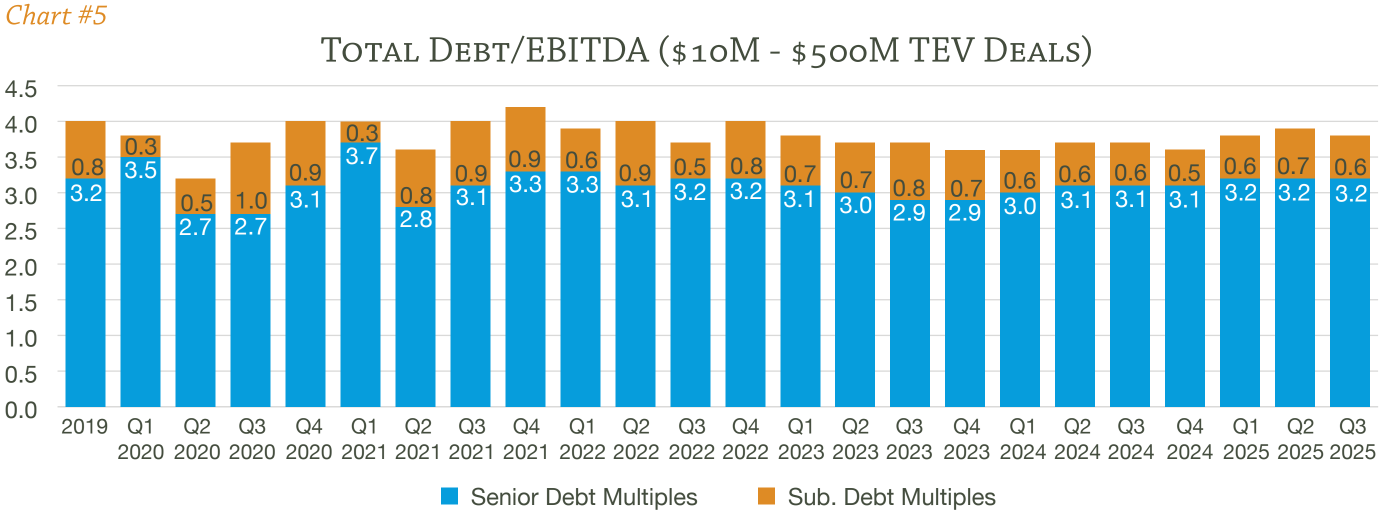
Chart 5 shows us that we aren't seeing much movement in the leverage multiples Buyers are getting middle market deals funded at.

Chart #4



Source: GF Data®

Chart #5



Source: GF Data®

Pursant watches these macroeconomic indicators because the direction and performance of the greater economy give us an indication of whether the M&A business transfer cycle is heading toward a more or less favorable phase.

The US Macroeconomic Picture for Q3 2025

Pursant watches these macroeconomic indicators because the direction and performance of the greater economy give us an indication of whether the M&A business transfer cycle is heading toward a more or less favorable phase. The performance of these four macro-indicators keeps us in a neutral to Buyer-favorable phase of the business transfer cycle, benefiting neither the Buyer nor Seller disproportionality in most cases, but in some cases in which a sector is negatively impacted by certain macroeconomic conditions, such as the cost of capital, the Buyer has the edge.

- **The US economy grew an annualized unknown % in Q3 2025—**Q3 2025 GDP growth likely brought a mixed but generally stabilizing picture for the U.S. economy. After strong 3.8% growth in Q2, early estimates suggest GDP expanded at a more moderate pace in Q3. Official government reporting is delayed, but most economic models point to continued positive growth, albeit at a slower rate as consumers, lenders, and businesses adjusted to ongoing macro uncertainty. The broader takeaway: the economy is still expanding, just at a more measured and sustainable clip.
- **U.S. Inflation at 3% in Q3 2025—**Inflation remained elevated at the end of Q3, but the pace has cooled down somewhat. As of September 2025, headline inflation (CPI) stood at roughly 3.0% year-over-year. Core inflation (excluding food and energy) is hovering around 3.0% as well, a modest deceleration from prior months. That said, price pressures haven't disappeared. Energy costs, especially fuel, have spiked, and certain items such as new vehicles and shelter remain sticky. Meanwhile, categories like used cars and some services have seen slower increases. In short: inflation isn't roaring down, but it's not fully receding either. Households and businesses are still navigating a higher-cost environment, which continues to influence consumer behavior, deal valuation, and deal activity across the middle market. *
- **Business Confidence finishes Q3 2025 in a state of contraction—**The ISM US Manufacturing PMI finished Q3 at 49, slightly above market expectations of 49.0. The reading marked the seventh consecutive month of contraction, though it was the strongest in the current downturn. A PMI reading above 50 percent indicates that the manufacturing economy is generally expanding; below 50 percent indicates that it is generally declining. *
- **The FOMC lowered the federal funds rate to 4.00% – 4.250% in Q3 2025—**In September 2025, the Fed trimmed its benchmark interest rate by 25 basis points, a move that lowered the cost of capital across the board. That cut immediately resonated with the M&A and private-equity markets. Cheaper borrowing makes leveraged buyouts and acquisitions more attractive again, unlocking financing that had been constrained under higher-rate conditions. As a result, deal-makers are growing more optimistic. If this trend continues, expect to see renewed sponsorship of new deals, rising valuations, and a lift in M&A activity, particularly among middle-market and lower-middle-market targets.

**Trading Economics®*

State of Middle Market Private Equity

The year began with very bullish expectations that were quickly tempered by tariff disruption. As tariff volatility settled into the “new normal,” several other factors added positive momentum including improved policy visibility, moderating inflation, a Federal Reserve rate cut with guidance for additional cuts, a more competitive debt market, increased corporate spending, and strengthening executive confidence. While the larger buyout segments and Wall Street have been slower to react to these developments, the US private equity middle market demonstrated resiliency and adaptability. It is now positioned to be on pace for one of the strongest years on record. As a result, the middle market reaffirmed its role as a core driver of private equity activity in the US and appears poised to end the year with strong energy and optimism.

Listed below are key and notable trends related to the US private equity middle market.

• Deal Value Up

For the first half of 2025, middle market deal value reached approximately $200B across several thousand transactions which represents an increase of almost 20% compared to the same period last year. At this pace, deal value will be second only to 2021 which benefited from the “COVID bump.” This suggests that private equity firms are continuing to deploy capital despite ongoing macro uncertainty. Deal activity has also been supported by a competitive lending environment that has kept credit accessible and interest rates and other credit terms such as covenants attractively priced. Businesses being acquired are generally smaller as these owners tend to be event driven rather than market driven and are seeking liquidity and strategic partners. Private equity investors across the middle market are shifting away from defensive strategies and are increasingly orienting around growth, a trend that is expected to continue.

• Valuations Holding Strong

Continued demand for quality assets and a gradual normalization of financing conditions have kept valuations toward the higher end of the typical range. This stability signals a healthy reset following the repricing cycle that began in 2022, with Buyers and Sellers achieving greater alignment on valuation expectations. The market is favoring companies with strong operations and predictable earnings rather than relying on leverage driven expansion which creates a more sustainable foundation for future transactions.

• Sustainable Leverage Levels

Financing structures have become more balanced. Lenders are generally accepting equity contributions of around 50% of the total new capital required. This level has decreased and is now more consistent with pre-pandemic norms.

• Competitive Debt Markets

Private credit rather than traditional banks continues to dominate the middle market, particularly the lower end. The private credit environment is highly competitive with lenders actively competing for mandates and contributing to tighter spreads.

• Constrained Exit Conditions

The private equity community continues to face significant pressure to return liquidity to investors. After several years of depressed exit activity, limited partners now prioritize receiving capital back rather than simply achieving high returns. Many private equity managers, however, remain reluctant to sell and are waiting for improved conditions which only exacerbates fundraising challenges. There are an estimated six thousand private equity backed companies currently held in inventory which equates to roughly seven years of supply at today’s exit pace. For this reason, continuation funds remain an important liquidity tool because they allow private equity funds to deliver liquidity to their investors while retaining ownership of the company.

• Changing Definition of a Platform

The traditional definition of a platform investment has evolved. A platform was once characterized by scale and stability but often carried high levels of leverage. Today, many sponsors are starting smaller and scaling more quickly through add ons which account for almost three quarters of buyouts, with many involving businesses valued under $25M. The concept of a platform has shifted from a mature anchor investment to simply the first deal within a broader strategy.

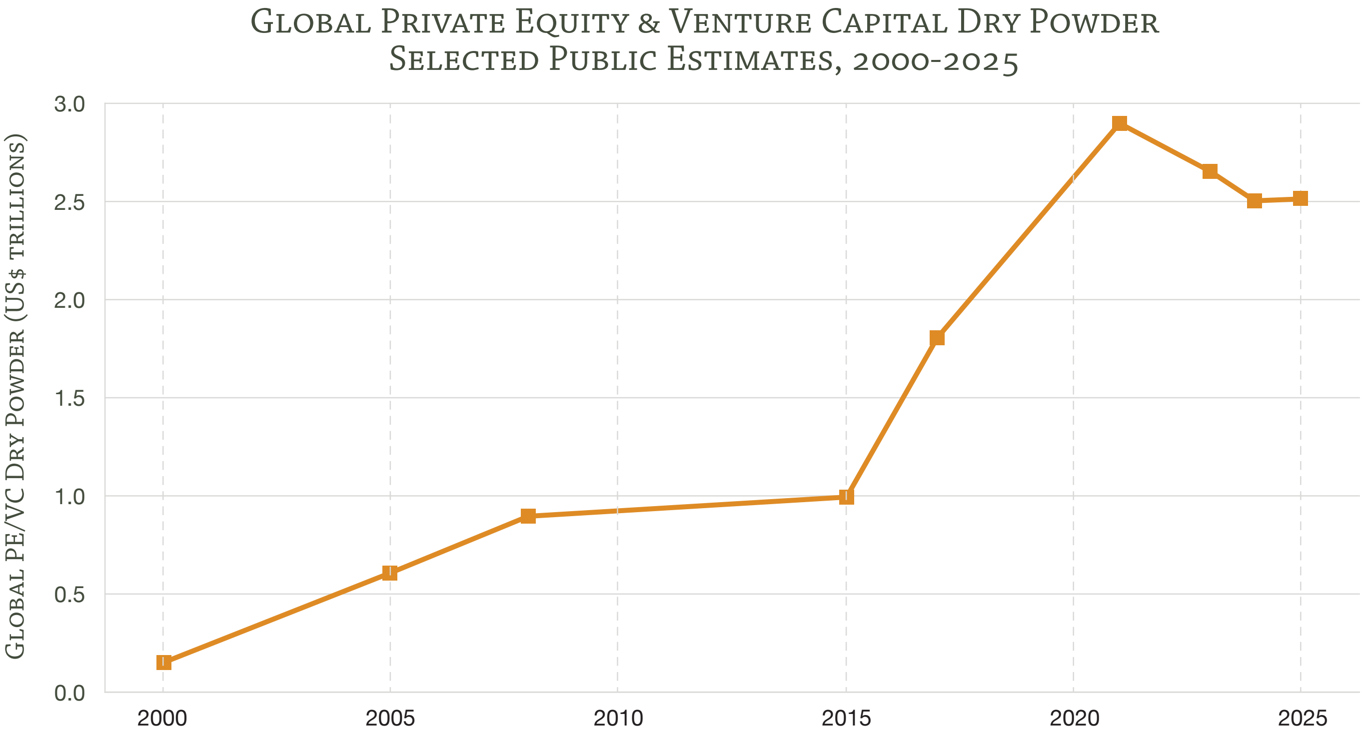
- **Challenging Fundraising Environment**

Although middle market deal activity has been a bright spot, as we can see in Chart 6, fundraising remains a challenge. We see that Global PE/VC dry powder has grown from roughly $150B in 2000 to more than $2.5T today, highlighting the long-term build-up of uncalled capital in private markets. (sources: S&P Global Market Intelligence, McKinsey, Bain, Preqin).

Exit delays create a circular strain since many investors prefer to recycle capital from prior funds into new commitments. Established private equity funds with track records are experiencing far better success raising new capital compared to newer funds entering the market even when those new entrants offer fee reductions or early commitment incentives.

In closing, the US private equity middle market remains resilient, active, and a major force in driving overall private equity activity. It continues to demonstrate greater stability and opportunity than larger buyout segments and is expected to remain a strong performer for many future cycles.

Chart #6



Source: GF Data®

The Buyer/Seller Valuation Gap is Finally Closing

The valuation gap between Sellers and private equity Buyers is narrowing across the middle market, and it's reshaping deal flow. Stabilizing macro conditions, normalized expectations on valuation, and renewed pressure on sponsors to deploy capital, are all contributing to a healthier and more active deal market.

After two years of stalled deal flow, 2024 – 2025 data show private equity deal activity and exits rebounding as pricing expectations come back into alignment. Global PE deal volume rose roughly $1.3 trillion in 2023 to about $1.7 trillion in 2024, reversing a two-year decline. More recently, as reported by Ernst & Young LLP, Q3 2025 PE deal volume hit a record $310 billion, with advisers explicitly siting "narrowing valuation gaps" as a key driver of the surge.

Let's take a look at what is driving the alignment and what it means for current and prospective Sellers.

1. <u>Market Stability is Restoring Pricing Confidence</u>
   During 2022 – 2023, volatile rates, tightening credit, and unclear growth outlooks made it difficult for Buyers to underwrite deals, and impossible for sellers to anchor to a valuation.

   Today, the picture is clearer:

   - Interest rates have plateaued, improving visibility into cost of capital.
   - Lenders are back with more predictable leverage levels.
   - Broader M&A activity has risen, giving both sides better benchmarks.

   This stability makes buyers more willing to stretch and sellers more confident in valuations that reflect current conditions rather than 2021 peaks.

2. <u>The Pressure on PE Firms to Deploy Capital and Exit Aging Portfolios</u>
   It is no secret that PE Firms are sitting on significant dry powder while also bumping up against longer-than-usual hold periods. As deal activity rebounds, sponsors are becoming more flexible on multiples for high-quality middle-market assets. They are leveraging creative deal structures to protect returns in industries where headline multiples became the norm.

3. <u>Creative Deal Structures are Doing Part of the Work</u>
   Even when valuations don't align, deal advisors are structuring agreements that often bridge the gap by offering rollover equity, extended term earn-outs, preferred equity, seller notes, and other hybrid tools to increase proceeds while protecting the downside. What were often viewed as deal breakers in negotiations are now the catalyst for getting deals across the finish line.

4. <u>Sellers Have Adjusted Their Price Expectations</u>
   In 2023, as reported by Grant Thornton UK, PE deal activity in the US fell to its lowest point since 2016. The driver? Owners were delaying a sale in what they felt was a discounted market in comparison to 2021 peak multiples. Two years later, expectations are starting to normalize, and many can see that healthy exits still exist. Owners are now coming to the market prepared to sell with cleaner books, more realistic expectations on valuation, and stronger proof points around growth.

Bottom Line

- **It's a good time to engage in the market.** Quality businesses with clean financials, recurring revenue, and clear growth levers are receiving strong attention from buyers.
- **Preparation still drives premium outcomes.** Coming to the market with a polished Confidential Information Memorandum, robust quality of earnings, and a strong organizational chart remain crucial in driving valuation.
- **Flexibility can increase total value.** Considering rollovers or earn-outs can materially enhance outcomes, while giving sellers meaningful participation in future growth, and protecting buyers on the downside.

Private Credit's Move Downstream: What It Means for the Lower Middle Market

Over the past decade, private credit has evolved from an alternative asset class into a dominant force in the middle market. But the most notable shift in the past 12–18 months is happening below the traditional middle-market threshold: more private-credit funds are moving downstream and actively targeting lower middle-market (LMM) borrowers, companies with roughly $3-10 million of EBITDA.

What was once the territory of regional banks, small business investment companies (SBICs), and a handful of independent lenders is now increasingly populated by institutional private-credit providers competing for yield, diversification, and deal flow.

Why Private Credit Is Moving Downstream

- ***Dry powder needs a home***
  After a strong fundraising cycle, many credit funds are sitting on abundant capital. As competition for larger deals compresses spreads, managers are looking to the LMM where yields are higher and structures are more lender-friendly.

- ***Banks remain cautious***
  Regulatory pressure and higher capital requirements continue to limit banks' appetite for cash-flow lending. Even as some banks tiptoe back in, underwriting standards remain tight, leaving a gap that private credit is eager to fill.

- ***LMM private-equity activity is resilient***
  While mega-deals slowed, LMM sponsors remained active throughout the past year. Funds looking to finance platform acquisitions and add-ons are increasingly turning to private-credit providers who can move quickly and commit flexibly.

- ***Under-served borrowers, attractive risk-adjusted returns***
  Historically, the LMM has been underserved with fewer institutional lending options. For private-credit funds that can underwrite smaller, nuanced businesses, the risk/return equation remains compelling.

What This Means for LMM Borrowers

For LMM companies, the expansion of private credit brings both benefits and new considerations.

- ***More options — and more negotiating leverage***
  Borrowers now have access to capital sources that previously focused only on $10M+ EBITDA deals. This influx is creating competitive tension and improving terms in many situations.

- ***Faster execution and greater certainty***
  Private-credit lenders can typically underwrite and close more quickly than traditional banks, especially valuable in M&A processes or time-sensitive refinancings.

- ***More tailored structures***
  Unitranche facilities, delayed-draw term loans, add-on acquisition lines, and other flexible structures are becoming more accessible to smaller companies and giving them more credible non-bank financing options than ever before.

- ***Higher costs, but more flexibility***
  Private credit typically runs higher than bank debt. But the trade-off—speed, deal certainty, and structure continues to attract borrowers who value flexibility.

According to Capstone Partners Middle Market Leveraged Finance Report (Summer 2025), middle-market senior/ ***unitranche loans are pricing around SOFR + 500 bps for strong credits, implying all-in interest of ~9.00% at this time. For lower-middle-market companies, spreads are generally 50-100 bps higher, meaning roughly 9.5-10% all-in rates*** depending on credit stats. Note that credit spreads for middle market and lower middle market loans continue to trend downward for the reasons discussed above.

Conclusion

Private credit's move into the lower middle market isn't a temporary shift, it's a structural change. For LMM companies seeking capital, the expanding lender universe represents an opportunity to secure creative, flexible financing that wasn't available even a few years ago. Moreover, spreads continue to improve as more lending competition targets the LLM.

Looking ahead to Q4, the ingredients are in place for a meaningful uptick in activity.

Pursant's Expectations for the Near Future

As we head into the final quarter of the year, the middle-market M&A landscape is showing more promise than we've seen in some time. Financing conditions have meaningfully improved, with lenders stepping back into the market and leverage levels rising. This renewed credit availability is helping valuations stay firm, particularly for high-quality companies with durable cash flow, strong customer retention, and clear paths to growth.

While overall deal volume remains relatively steady, we're seeing a shift toward higher-value transactions and more competitive processes. Private equity remains active and is increasingly willing to pay up for scale or strategic fit, while corporate Buyers are resurfacing with a renewed appetite for bolt-ons and synergistic plays. Industries like industrial services, healthcare, tech-enabled business services, and essential consumer categories continue to attract the most attention thanks to their resilience and operational predictability.

Looking ahead to Q4, the ingredients are in place for a meaningful uptick in activity. Sellers who have been waiting for clearer pricing signals may decide it's time to move, and Buyers eager to deploy capital before year-end could accelerate timelines. Multiples are expected to hold steady, though selectivity remains the name of the game. Businesses with clean financials, recurring or reoccurring revenue components, and strong leadership teams are positioned to command premium outcomes.

Conditions are aligning for a stronger finish than many expected at the start of the year. For owners considering a future exit, or even just wanting to understand their valuation, it's a smart moment to evaluate readiness and tighten the playbook to hit the market in 2026.

The Pursant Deal Insider is a quarterly publication offering analysis of the marketplace and climate for middle market mergers, acquisitions, and strategic transactions. Our emphasis is on transactions with a total enterprise value of less than $250M. Our goal is to arm business owners and dealmakers with the insights needed to optimize transaction outcomes.

Pursant is a middle market advisory firm specializing in M&A, private capital market financing, transaction advisory, financial leadership support and business value enhancement consulting. Our powerful, integrative, and customized suite of services deliver the insight and guidance parties seek to:

- Confidently navigate strategic transactions and complex financial matters
- Enhance enterprise value
- Optimize leadership performance

We use a deep immersion process, our expansive networks and experience as owner/operators, dealmakers and financial professionals to achieve optimal outcomes throughout the lifecycle of a company.

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