



2018 STATE OF THE INDUSTRY

---

# The Current State of the Capital Markets

BOYAR  MILLER  
ATTORNEYS AT LAW

# Hello Friends,

We have all heard the phrase “money makes the world go ‘round.” For businesses, it is indeed the availability of capital that fuels business and economic growth like what we are enjoying today, especially here in Texas. But how will increasing interest rates affect that growth and what should you do about it?

Those questions were a significant part of the discussion at our annual Capital Markets Breakfast Forum. Our friends and business colleagues, Mark Montgomery, Ali Nasser and Scott Winship, provided perspectives on the current business environment and expectations for the coming years. We have captured the highlights in this eBook and we hope you find the information of value.

At BoyarMiller, it is our goal to arm you with insights that may bring new possibilities into focus as you examine your business and goals for the future. We are here to help you with that process.



My best,

*Chris Hanslik*

**CHRIS HANSLIK**  
*Firm Chairman*

## CONTACT

---

2925 Richmond Avenue, 14th Floor  
Houston, Texas 77098

713.850.7766

Visit [boyarmiller.com](http://boyarmiller.com)

[LEARN MORE ABOUT THE FORUM](#)

## TABLE OF CONTENTS

---

- 03 : By the Numbers
- 04 : Expert Panelists
- 05 : Panelist Discussion
  - The Economy & Capital Markets
  - Mergers & Acquisitions
  - Advice to Middle Market Businesses
- 08 : Attorney Insights: What About Now for M&A?
- 09 : BoyarMiller Capital Markets Practice Leaders





# By the Numbers

**EVERY  
5-7 YEARS**

Typical Recession Cycle

**4.2%**

U.S. GDP Growth Rate,  
as of Q2 2018



The M&A market has  
a very distinct

**6-YEAR  
CYCLE**



**5%**

Expected Houston Business  
Cycle Index for the Third Quarter



**20%  
HIGHER**

Asset Valuations



Interest Rates Up

**QUARTER  
PERCENTAGE  
POINT**

**ATRILLION  
& A HALF  
DOLLARS**

Approximate Leveraged  
Buying Power in the U.S.  
Domestic Private Equity Market

# Expert Panelists



**MARK W. MONTGOMERY**  
*Houston Market CEO*  
BBVA Compass

Mark is the Houston CEO of BBVA Compass and is responsible for management of all aspects of commercial and wealth banking. Mark's 34 years in banking includes loan work-outs, loan reviews, and CRA lending. He has managed teams, both large and small, through a lens of strategy, value creation, and results.

“

2018 has been a good year. Our phones are ringing and transactions are happening.

Nationally, the economy is in great shape and that should continue for a while.

We should see 5% GDP for the third quarter in Houston. We are now outpacing other Texas cities.



**ALI A. NASSER, CFP, AEP**  
*CEO and Founder*  
AltruVista

Ali is the CEO and Founder of AltruVista and an Instructor at Rice University's Certified Financial Planning Graduate Program. He is an expert on the entrepreneurial mindset and how it relates to wealth and financial strategy. His professional life is solely dedicated to helping business owners capture and maximize their success. Ali's upcoming book, *The Business Owner's Dilemma*, will address the critical decisions facing highly successful entrepreneurs.

“

Economists may have the right data, yet they often have the wrong timing.

Every business owner is wondering when a recession will hit, because it is inevitable since the last recession was in 2008.

Plan, don't panic.



**SCOTT D. WINSHIP**  
*Managing Director*  
GulfStar Group

Scott joined GulfStar in 2010 with more than 23 years of experience advising clients in the consumer products and information technology industries. He has successfully closed more than 50 transactions with an aggregate value in excess of \$18 billion across a broad range of public and private market equity and debt financings, mergers and acquisitions, and strategic advisory assignments.

“

Right now we are enjoying a very dynamic market and we are cautiously optimistic regarding 2019 and 2020, barring some sort of system shock.

There is no doubt that if tariffs get aggressive, it will impact a broad range of businesses.

A lot of psychology goes into getting a deal done and clients have to manage their emotions during the process.



## PANELIST DISCUSSION

# The Economy & Capital Markets

## What is the current state of the economy and capital markets?

### LATE STATE ECONOMIC CYCLE

Currently, we are in a late stage economic cycle. We have experienced accelerated growth in GDP and high corporate profits by many S&P companies. While some of the profits can be attributed short-term to tax reform, they still look strong moving forward.

### CONFIDENCE

The tax policy has created much confidence; there is a lot of positive momentum among businesses currently.

### +.25%

On September 26, the Federal Reserve announced it would raise short-term interest rates by a quarter-percentage point and also said it expected to raise them again this year and through 2019 to keep "a strong economy on an even keel," reported [The Wall Street Journal](#).

### SLOWING ECONOMY

As interest rates increase, the economy has to slow down a little. But you can't predict the markets.

### 4.2%<sup>GDP</sup>

Nationally, the economy is strong with a four percent GDP. Even with all the "noise" regarding trade and tariffs, growth will continue for a while—or perhaps the GDP will dip to three percent.

### 5%<sup>GROWTH</sup> RATE

Texas has had outstanding economic growth and other cities in the state were outpacing Houston. Now, Houston is on the verge of outpacing the rest of Texas since oil prices have rebounded. Expect a five percent growth rate for the quarter in Houston.

### 18-24 MONTHS

We have to be looking down the road if we expect a recession to come in the next 18 to 24 months. Business owners need to plan and prepare, not panic.



## PANELIST DISCUSSION

# Mergers & Acquisitions

## What is the state of mergers and acquisitions and what can we expect moving forward?

**6-YR CYCLE**

The M&A market has a very distinct six-year cycle yet we have strong activity continuing because of the robust economy.

**ASSET VALUATIONS  
HIGH**

Over the last two years, asset valuations have been high because lending has been easy to accommodate business borrowers and private equity firms.

**\$1.5T.**

The private equity asset class has gotten wide in the last five years and that may create buoyancy in a down cycle—something we haven't seen before. The leveraged buying power in the U.S. domestic private equity market is about a trillion and a half dollars.

**LESS SEVERE  
MARKET LOWS**

Because of the access to private equity capital, when we see a downturn—which is inevitable and will happen at some point—the low in the market could be higher than it has been in the past.

**INTEREST RATE  
SENSITIVITY**

The M&A market is obviously sensitive to interest rates. Cost of capital factors into the return profile for both strategic acquisitions and private equity firms.

**TIME IS THE  
ENEMY**

The biggest challenge in any M&A deal is to compress it into the shortest possible timeframe. Time is the enemy of everything good and given enough time, something bad will happen.

**+DILIGENCE  
OUTSOURCING**

We have seen increased amount of diligence outsourcing, and while fair, sometimes the process creates redundancy and injects a lot of time into the deal. There must be a balance to accommodate the buyer and protect the seller.



## PANELIST DISCUSSION

# Advice to Middle Market Businesses

## What should businesses consider before going to market to maximize their valuation?

**PREPARATION IS CRITICAL**

Preparation is critical to a successful outcome. Every buyer looks at a transaction through the lens of risk.

**GET THE FINANCIAL HOUSE IN ORDER**

Before businesses go to market, it is imperative to get their financial house in order. The integrity of the financials, depth of the management team, quality of the infrastructure, and illustration of how business challenges have been managed all significantly influence the value of a business.

**STRESS TEST**

Business owners need to do a stress test. Determine what will happen if they lost a few customers or clients. What happens if increased interest rates result in a one to two percent increase in your debt service? Will you have enough liquidity to run your business?

**THINK ABOUT THE FUTURE**

Operate with a healthy concern about the future and don't be a fatalist. Right now is a good time to be a seller; just take into account the risks and unknowns of the future.

**DON'T PANIC**

Entrepreneurs are passionate about what they built and can make bad decisions if they panic. We know a recession is coming; it happens typically every five to seven years. But it is not a time to panic.

**DO NOT BE REACTIVE**

Don't change your business strategy just because you fear a recession could be coming. Stay on course and continue to participate in growth. Do not be reactive.

**BE CAUTIOUSLY OPTIMISTIC**

No one has a crystal ball. Be cautiously optimistic for 2018 and 2019.



# Attorney Insights

## What About Now for M&A? 2018: A Great Time to Buy or Sell in the Middle Market

**PHILIP DUNLAP**  
Shareholder, Business Group

**CYRUS CHIN**  
Associate, Business Group

2018 is a great time to be a buyer or seller in the middle market. In the first half of 2018, private equity firms completed nearly 1,400 middle market deals with a value totaling \$178 billion, beating 2017's first half performance. As oil prices have stabilized and companies have found creative ways to control costs, we are seeing greater momentum in the economy. Better cost controls should offset the negative impacts of new tariffs, which will eventually increase the cost of doing business in certain sectors of the market.

However, we have seen steady-to-strong growth in the economy for the past six to eight years—*this can't last forever, right?* Are we heading for another recession, and if so, when will it hit? Will rising interest rates do anything to slow down M&A and private equity activity? *Our belief is that we are in the late stages of a strong economic cycle, so as a business owner or an investor, if you are thinking of selling or buying in the near future, you should be concerned about when—not if—the markets will slow down.*

In the near term (through 2019), the deal-making environment should remain healthy. Middle market deals are experiencing higher than normal valuations—up to 1.5x turns on EBITDA higher than historical averages—primarily due to two factors: (1) private equity firms having “dry powder” that they must invest (or risk having to return to their investors), and (2) strategic investors' willingness to pay more to promote growth and to capitalize on synergies with target companies.

On the flip side, as interest rates rise, and the Fed has indicated it will continue to raise interest rates over the next 12–18 months, the cost of capital will also rise. As a result, the deal-flow for middle market M&A may slow down as private equity buyers will have less leverage to finance new acquisitions. Additionally, because private equity buyers are increasingly spending more time and energy on due diligence than strategic buyers, the time frame for closing deals coupled with the higher cost of capital could make closing deals with private equity buyers more difficult than for strategic buyers.

Finally, the tariffs companies will be facing as a result of doing business in China in 2019 will likely cause companies in certain industries to have lower EBITDA which would lower the purchase price for deals in those industries. As purchase price decreases, getting deals closed in certain industries will be more difficult for sellers and buyers in the latter part of 2019 and beyond.

While the outlook for middle market M&A activity remains strong for the end of 2018 and 2019, business owners and investors should prepare now for a time in the not too distant future when the economy and prospects for middle market deals will be weaker. Business owners should consider that the near term may be the best time to sell. Potential buyers should likewise consider that while valuations are higher now, the ability to close on deals after 2019 may be significantly more difficult. As a result, all parties in the middle market should look to make good strategic decisions regarding M&A in the next 12–15 months.





# Capital Markets Practice Leaders

**BILL BOYAR***Founding Shareholder, Business Group*

---

Represents the various parties involved in the acquisition, disposition, capitalization and financing of national and international businesses. Served as lead counsel for numerous complex, multi-party acquisitions and project financings with significant experience in corporate finance, mergers and acquisitions, private equity and structure finance.

**GARY MILLER***Founding Shareholder, Business Group*

---

Represents numerous domestic and offshore-based companies in connection with acquisitions and divestitures, financings, joint ventures and general corporate matters in the United States.

**STEVE KESTEN***Chair, Business Group*

---

Represents multiple international energy and energy services clients with outbound expansion (i.e., U.S. companies expanding internationally) and inbound expansion (international companies expanding to the U.S.), including start-up expansion or expansion by acquisition, as well as in connection with financing and merger and divestiture transactions.

# Capital Markets Practice Leaders, cont.



**GUS BOURGEOIS**

*Shareholder, Business Group*

Represents clients doing business domestically and internationally in connection with mergers and acquisitions, finance and multi-jurisdictional transactions, including negotiation of contracts for sales of goods and services (including master service agreements), technology licensing, joint-venture agreements, and employment agreements, with significant experience in assisting foreign businesses in establishing and growing their U.S. operations.



**PHILIP A. DUNLAP**

*Shareholder, Business Group*

Represents clients for corporate and private securities transactions as well as serving as outside general counsel in a variety of matters, including mergers and acquisitions, financing, employment agreements and raising capital through private offerings.



**SHAY JOHANSON**

*Of Counsel, Business Group*

Represents clients in various industries in connection with mergers and acquisitions, dispositions, joint ventures, private securities offerings, corporate restructuring, venture capital, private equity financings, corporate governance matters, cross-border transactions, and general contracts.



# Capital Markets Practice Leaders, cont.



**BLAKE D. ROYAL**

*Shareholder, Business Group*

---

Represents corporations and businesses in corporate transactions, contracts, private equity investments, mergers and acquisitions, corporate restructuring and capital formation strategy and structure.



**LAWRENCE E. WILSON**

*Shareholder, Business Group*

---

Represents public and private businesses in acquisitions, divestitures, corporate finance and general corporate matters and provides corporate and commercial counseling – acting as an outside general counsel to various businesses – regarding complex mergers and acquisitions, initial capitalization and growth financing and restructuring transactions.