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# Insiders View: M&A, Crowdfunding Trends

*By Bailey McCann*

Activity in middle-market M&A fell to its lowest level in 18 years, according to investment bank R.W. Baird & Co., there were just under 200 deals last month according to the bank – marking the lowest number of deals in a given month since 1995. Observers note that this may be an indication that the post-2008 M&A recovery was just a flash in the pan. However, there are still pockets of activity, according to John Sensiba, Managing Partner at Sensiba San Filippo LLP, Northern California-based CPA and business consulting firm.

"Right now there is a real stretch in the high tech world to get high quality people . Once you've got a team that could be attractive, the multiples to sell with that staff is higher than any product you would be able to develop," he tells Private Equity Strategies.

This reality reflects a long held contention of many businesses, that the skills gap is holding back economic growth.

"Small team acquisition is very popular right now, and those teams don't always exist in California, they could be scattered in a number of locations and working remotely. It's going to depend on what an individual firm is looking for through the acquisition. Old economy sectors like manufacturing are also seeing activity," he says.

In the industries with activity, a number of factors are driving deals – there are generational issues, and many large private and public companies with a lot of cash on hand.

"We're primed for M&A right now because there are so many private companies without succession plans in place, those issues are generational - people want to retire or do something else, and there's no one then, to take over really outside of a private equity firm," Sensiba says.

In other industries like automotive dealerships, strategic acquisitions are driving deals as many dealership groups find themselves with plenty of cash on hand. According to a semiannual report from Presidio, a San Francisco financial services company that brokers dealership sales, public auto-retail companies spent $133 million on U.S. dealership acquisitions, up 8 percent from the year-earlier period. Large privately held dealership groups are also hot on their heels.

Registered investment advisory firms are also getting into the mix, and are willing to solve some of the issues that may slow down a traditional private equity deal, according to recent analysis in Investment News.

Overall, though, activity still remains low, indicating that the recovery many hoped for is still far off. Against this backdrop some troubling trends are starting to creep back in. “It’s surprising to me a little bit, to see some of the multiples that are being paid, we tend to repeat our mistakes in the business world and I’m not saying there are ridiculous yet, but they are getting higher and there are people who are doing deals to do deals,” Sensiba says.

## Crowdfunding enters the fold

After much feet dragging, the SEC has started to deal with the rules surrounding crowdfunding, as included in the JOBS Act. The regulator was fundamentally opposed to crowdfunding, well before the JOBS Act, and still seems hesitant to put any weight behind it as an investment vehicle. However, some say crowdfunding could have real impact for M&A, growth equity and the IPO markets as well.

Critics of crowdfunding say that the opportunity for fraud is too high, and that investors in this space may not always understand what they’re getting into. While supporters argue that crowdfunding can help democratize finance and provide capital for businesses that would otherwise have a hard time.

“It’s the new money, that tends to overpay in transactions, that’s what concerns us about crowdfunding. Investors that aren’t as sophisticated might see downside from those increases in multiples,” Sensiba notes.

Both sides have solid points. In our last issue we interviewed Judd Hollas, CEO of EquityNet, who is a proponent of crowdfunding, and in that interview he noted that similar concerns were voiced when self-directed investment platforms like E*TRADE and eBay first launched in the 1990s.

“I think the fact that entrepreneurs have to verify that investors are accredited is a positive step. Arguably the same questions were raised about companies like eBay or PayPal in the early days, but there have also been a lot of technological advancements driven by those companies.

Those technologies and community self-policing will come along here too, some solutions are already in place," he said.

Companies like E*TRADE and eBay may be good examples for the crowdfunding conversation. Critics and supporters alike tend to focus on whether the average retail investor will understand the inner workings of a transaction. On platforms like E*Trade, and even to an extent on eBay, users are almost annoyingly informed by these firms about what they are getting into, and the consequences for fraud.

The same practices could be replicated on crowdfunding platforms, or, better still, regulators could engage in conversations about how to simplify and improve financial disclosure rules which are often arcane even to "sophisticated" investors and their sizeable legal and accounting teams. Financial journalists could easily only cover the steady stream of regulatory changes that are meant to provide more transparency, and instead often just result in more, and conflicting reports. In all, only holding retail investors responsible for their ability to navigate this system seems a bit disingenuous.

"There is a huge opportunity to simplify accounting practices internally and externally when you look at some of the disclosures that are required," Sensiba says. "Many times those disclosures mean nothing to average users of financial statements. When you look at Craigslist, people show the dents on their cars and they explain what they're selling, what is wrong, and why they think the value is fair. But we don't do that in the business world, instead we keep changing regulation around instead of just being transparent."

Structurally, crowdfunding may play an increasingly important role in a low liquidity environment. Crowdfunding could have implications business decisions in terms of growth opportunities, whether to stay private, or when to sell.

As banks consolidate, and are required to keep more cash on hand, providing small lines of riskier credit, rubs up against new regulations. This reality is already opening up new opportunities for private equity firms and hedge funds. Still, there are some businesses that may be sound, but aren't going to fit the mold for alternative investment firms. (Consider the troubling trend of some VC firms considering women owned businesses innately too risky, as one example.) Could these firms be a good fit for crowdfunding? Maybe. Crowdfunding may be a way for businesses to grow into something that is a better fit for investment firms. Watch this space.