What Private Equity Sees in Your Business

How buyers value lower middle market companies in 2026, and what owners can do about it

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Executive summary

Privately held companies remain private equity's most common target, making up about half of US PE deals each year. But PE is paying for them differently than it did five years ago. Debt is more expensive, buyers hold companies longer, and the easy gains from rising valuations are gone. Today's buyers make their returns by making businesses better, and they pay most for companies that are already well run.

That shift matters to every owner of a business with roughly $2 million to $25 million in EBITDA, whether or not a sale is on the horizon. Five takeaways:

1. **Buyers are active but selective.** US PE closed about 2,467 deals worth $233.8 billion in Q3 2026, up from Q2. Roughly half of all PE deals each year buy companies with no prior institutional investor, and about seven in ten are under $100 million in size.
2. **Size and quality drive price.** Lower middle market companies typically sell for about 6x to 9x EBITDA, while large buyouts trade at 12x to 13x. Moving up a size band is worth several turns of value.
3. **The PE playbook has changed from financial engineering to operational improvement.** With borrowing costs near 8% to 9%, buyers now need roughly 10% to 12% annual earnings growth to hit their return targets, about double the 2010s requirement.
4. **The traits buyers pay for are the traits that make a business better to own.** Disciplined pricing, a management team beyond the founder, clean financials, diversified customers, and efficient use of cash all raise value with or without a sale.
5. **Know your options before the phone rings.** Add-on acquisitions are three-quarters of all PE buyouts, so many owners will be approached by a buyer who already owns a competitor. Understanding deal structure, rollover equity, and your post-close role puts you in a far stronger position.

The state of the lower middle market

The market for buying private companies has recovered from a soft spring of 2026, but buyers are more careful about what they pay for and how they pay for it.

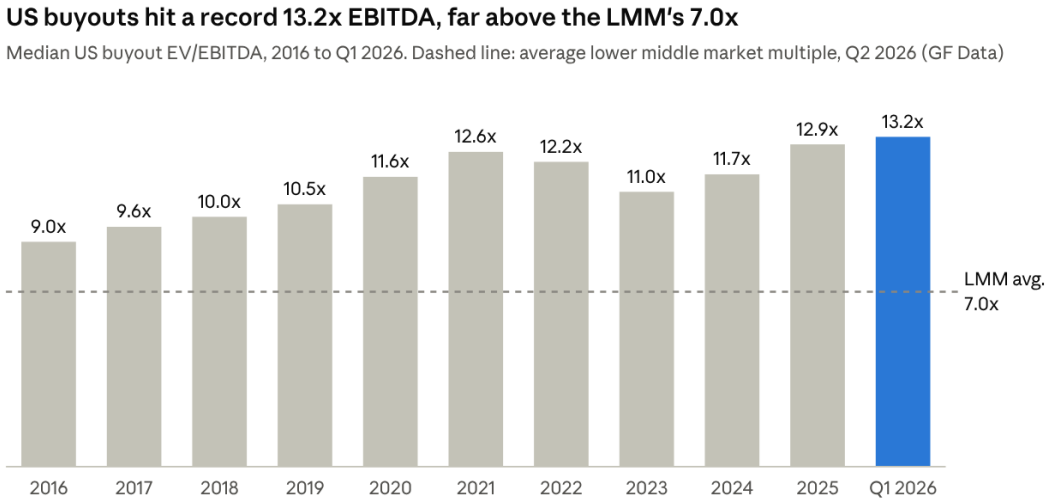
Deal activity is rebounding

US private equity firms closed an estimated 2,467 deals worth $233.8 billion in Q3 2026, up 5.9% in count and 20.9% in value from Q2. That followed the slowest quarter for deal value since late 2023. PitchBook (an institutional service that follows the private equity industry) believes that sponsors are "adjusting deal size and structure rather than stepping away from the market entirely."

Lower middle-market private equity firms are driving that activity. Every year since 2016, deals under $25 million have made up roughly 45% to 48% of all US PE transactions by count, and deals under $100 million about 70%. About half of private equity deals each year include a purchase of a company that was privately held with no prior institutional investors. In other words, the typical PE target looks a lot like your business.

GF Data, which tracks private equity deals valued between $1 million and $500 million in enterprise value, recorded 170 transactions reported by its contributing PE firms in the first half of 2026. That puts the year on pace to finish about 10% ahead of 2025.

Prices are high at the top, lower in the lower middle market



Source: SPI by StepStone, as published in PitchBook Q3 2026 US PE Breakdown (as of March 31, 2026); LMM average from GF Data Q2 2026 (August 2026)

The median US buyout now trades at about 13x EBITDA, a new record. That headline number is driven by larger companies. In the lower middle market, average purchase multiples were 7.0x EBITDA in Q2 2026 and 7.3x in Q1. GF Data attributed the dip to the mix of deals that closed, not weaker bids.

Financing costs more

Borrowing is the biggest change from the last decade. Senior debt on lower middle market deals averaged 7.8% in Q2 2026, up from 7.2% in Q1. Average total debt fell to 2.9x (EBITDA)from 3.4x. Lenders are lending less and charging more, and PitchBook notes a rate hike in mid-September 2026, with at least one more considered likely this year.

Less debt means buyers must put in more equity, which raises the bar for every deal. It also means sellers are more often asked to share risk through rollover equity, earnouts, or seller notes.

Buyers are holding companies longer

Bain & Company reports that buyout holding periods at exit now average about seven years, up from five to six years in 2010 to 2021. About 32,000 PE-owned companies worth $3.8 trillion are still waiting to be sold, and buyout funds hold in total roughly $1.3 trillion of uninvested capital.

For owners, that has two implications. ***Plenty of money is looking for good companies***. But private equity buyers know they own a company longer, so they do more diligence and reward businesses that can grow without heavy intervention.

A generational wave of sellers

McKinsey estimates that about 6 million US small and mid-sized businesses will change hands by 2035 as baby boomer owners retire, and more than $1 million of them are viable candidates for sale, representing up to $5 trillion of enterprise value. Most of these exits are too small for private equity: nearly 80% involve businesses valued under $2 million. But owners of the slice large enough to attract PE will face more competition from other sellers, not just among buyers.

The buyer pool is also widening. More than 1,500 independent private capital firms, dealmakers who raise capital one deal at a time, are active in the US, nearly double the count of five years ago. Family offices and private funds are also competing for founder-led businesses, often with more flexible terms and longer time horizons than traditional funds.

> ***By the numbers***

- **74.9%** of US PE buyouts in 2026 are add-ons to existing portfolio companies (PitchBook)
- **~7 years** is the average buyout holding period at exit, through 2025 (Bain)
- **7.8%** is the average senior debt rate on lower middle market deals, Q2 2026 (GF Data)
- **6 million** US businesses face an ownership transition by 2035 (McKinsey)

What this means for owners: Capital is available and buyers are active. But in a market where debt is expensive and holds are long, a buyer's willingness to pay depends heavily on how ready the business is to grow without its owner.

How private equity thinks

A private equity firm's behavior makes sense once you understand three things: whose money it manages, the clock it runs on, and the return it has promised.

Whose money, and on what clock

A private equity firm raises a fund from investors such as pension plans, endowments, insurance companies, and wealthy families. The fund typically has a 10-year life. The firm invests the money over the first few years, owns each company for several years, and then sells it and returns the proceeds. The firm earns a management fee plus a share of the profits, usually around 20%, once investors get their capital back plus a minimum return.

That structure explains a lot. PE firms are not permanent owners. Every acquisition is made with an exit in mind, and every decision during ownership is weighed against what it will do to the company's value

at sale. The Pepperdine Private Capital Markets Report (2026) finds private equity investors expect returns of about 20% a year on companies with $1 million to $5 million of EBITDA, rising to about 25% for larger middle market companies.

> ***Key terms***

- **EBITDA:** earnings before interest, taxes, depreciation, and amortization. It's a rough proxy for the cash a business generates from operations, and the number most buyers use to value it.
- **EBITDA multiple:** the enterprise value is divided by EBITDA. A company with $5 million of EBITDA sold at 7x is worth $35 million of enterprise value.
- **Platform:** the first company a PE firm buys in an industry, which becomes the base for further acquisitions.
- **Add-on:** a smaller company bought and merged into an existing platform.
- **Recapitalization:** a deal in which the owner sells a majority or minority stake but keeps some ownership.

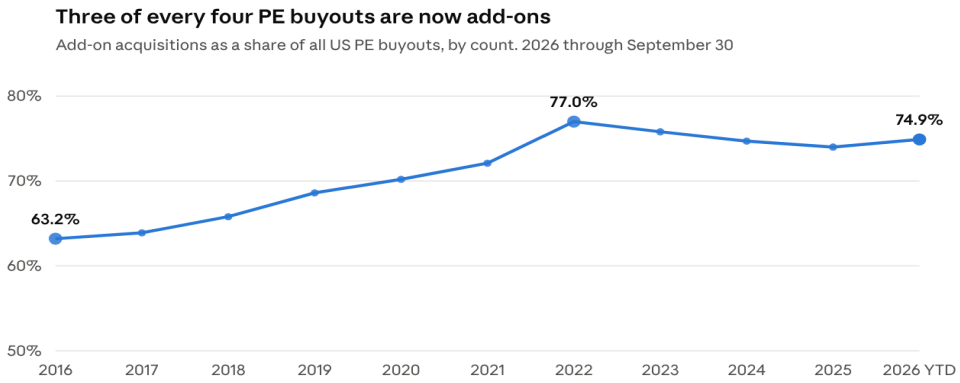
Why "12 is the new 5"

For most of the 2010s, PE firms could earn strong returns with relatively little operational work. Debt was cheap, so they could finance 65% to 70% of a purchase. And valuations rose steadily: according to PitchBook, the median US buyout multiple climbed from 9.0x EBITDA in 2016 to 12.6x in 2021, so a company could often be sold for more even if nothing changed.

Bain & Company's 2026 Global Private Equity Report sums up how that math has changed. To earn 2.5 times investors' money over five years, a buyout in the 2010s needed about 5% annual EBITDA growth. Today, with borrowing costs of 8% to 9%, leverage of only 30% to 40%, and purchase prices already at record levels, the same result requires roughly 10% to 12% annual EBITDA growth.

That is the most important thing an owner can understand about today's buyers. **They can no longer count on debt or rising prices to make their returns. They have to grow earnings, and they will pay most for businesses where they can see clearly how to do it.**

Why buyers want add-on acquisitions



Source: PitchBook Q3 2026 US PE Breakdown, US data as of September 30, 2026

The most common way a private equity firm grows its company's earnings is by buying more companies. A firm buys a platform at one price, then acquires smaller businesses in the same industry at lower multiples and folds them in. Because larger companies sell for higher multiples, the combined business is worth more than the sum of its parts. This is called a buy-and-build strategy.

This explains why many lower middle market owners hear from private equity-backed competitors rather than from private equity firms directly. It also explains why fragmented industries with many small, similar businesses attract so much private equity interest. PitchBook describes the current approach as a "barbell": lower-risk add-ons and growth equity investments on one end, a few large, high-conviction platform buyouts on the other. Growth equity, which buys a minority stake to fund expansion, is on pace for a record 24.8% of PE deal count in 2026.

How PE creates value today

Today's PE buyers make money by improving the businesses they own, and they focus first on a few levers that most founder-run companies have never fully used.

Craig Arends, managing principal of CliftonLarsonAllen's (CLA) private equity practice, described the shift in PitchBook's Q3 2026 report: "For 15 years, cheap debt did a lot of the work sponsors used to take credit for. You could buy a business at 9x EBITDA, lever it 65% to 70%, ride a rising multiple, and generate a strong IRR without ever touching the org chart. That playbook is gone." What's left, he said, "is the only lever a sponsor fully controls: making the business itself better."

In practice, that work tends to start with four levers.

1. Pricing

Pricing is often the fastest way to raise earnings, because the margin is already sitting inside the existing customer base. According to Amy Moore of CLA, many lower middle market companies "have never run a structured pricing review, segmented customers by willingness to pay, or renegotiated supplier terms with real leverage data in hand." CLA cites value-creation surveys showing pricing is now the revenue lever sponsors prioritize most, ahead of new markets or new products.

Illustrative example: A distributor has raised prices by a flat percentage each year for a decade. A new owner analyzes margins by customer and product and finds that a third of its small accounts are served at a loss. It introduces minimum order sizes, adjusts prices on low-margin products, and moves smaller customers to a self-service channel. Revenue barely changes, but EBITDA margin rises by several points within a year.

2. Procurement

Procurement is the cost-side mirror of pricing. Consolidating spending across locations or acquired companies, standardizing vendor terms, and catching bad contract terms at renewal rather than at exit can "move EBITDA meaningfully within two or three quarters," according to CLA. Buy-and-build strategies make this lever stronger, because each add-on increases purchasing power.

3. Working capital

Working capital is the cash tied up in receivables and inventory, net of what the company owes suppliers. When money was nearly free, a slow collections process or bloated inventory didn't cost much. Now, as Arends puts it, "every dollar trapped in the balance sheet is a dollar that either can't be distributed or has to be financed at a real interest rate." CLA reports seeing engagements where tightening the order-to-delivery cycle freed "millions in cash within the first year without a single new sale."

4. Processes and technology

Buyers increasingly invest in systems, data, and automation, but they are skeptical of technology that doesn't show up in the financial statements. John Cordio of CLA draws a line between tools that "save people a few minutes here and there" and rebuilding a process end to end, such as the monthly close, order-to-delivery, or contract review, "so the gain is structural rather than incremental."

Illustrative example: A professional services firm closes its books 25 days after month-end, using spreadsheets maintained by one long-tenured controller. A new owner installs a modern accounting system, standardizes the chart of accounts across offices, and builds a weekly dashboard of utilization and billing. The close drops to eight days, billing errors fall, and management can see problems a month earlier than before.

Professional management and the 100-day plan

Behind all four levers is a broader change: buyers are professionalizing management. That can mean adding a CFO, building a real budgeting process, or installing a board that meets regularly and tracks a defined set of metrics.

The first 100 days after a deal closes have become especially important. Five years ago, Moore said, the 100-day plan "was often a slide in a board deck. Today, it's an operating document with named owners, weekly cadence, and dollar targets attached to specific levers." Buyers increasingly build this plan before the deal closes, which is why diligence now includes so many operating questions.

> ***Owner takeaway***
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> *None of these four levers requires a buyer. Any owner can run a pricing review, renegotiate major supplier contracts, shorten collection times, or modernize the monthly close. Every dollar of EBITDA you add yourself is a dollar you get paid for at sale rather than one the buyer captures afterward.*

What makes a business attractive

The two biggest drivers of price in the lower middle market are size and risk. Larger companies sell for higher multiples, and buyers discount anything that makes future earnings less certain.

Size: every band up is worth more

GF Data's analysis of PE platform acquisitions in the first nine months of 2025 shows how steeply multiples rise with company size:

Enterprise value of the business	Average purchase multiple (x trailing EBITDA)
$10M to $25M	5.9x
$25M to $50M	6.6x
$50M to $100M	8.7x
$100M to $250M	10.0x

Source: GF Data, Q3 2025 M&A Report, January 2026. Based on 211 transactions contributed by 437 PE firms.

The gap between larger and smaller platforms widened to 2.8 turns through the first nine months of 2025, above its long-term average of 2.6. At the top of the market the gap is even wider: according to PitchBook, US companies valued at $1 billion or more sold to PE at a median 16x EBITDA in 2025, versus 10.8x for those under $1 billion. Sources differ on exact levels, so treat the lower middle market range as roughly **6x to 9x EBITDA**, depending on size, sector, and quality.

This is why buyers pursue add-ons. It is also why an owner who grows from $3 million to $6 million of EBITDA can more than double the value of the business: earnings grow, and the multiple on those earnings may grow too.

Risk: what buyers reward and penalize

Buyers don't price a business on last year's earnings alone. They price the likelihood that those earnings will continue and grow under new ownership. Traits that make earnings more predictable earn a premium. Traits that make them fragile earn a discount, or more often a tougher deal structure such as an earnout or a larger rollover requirement.

What buyers look for	Why it matters	Red flags
A management team beyond the founder	The business must run without you after you sell	Every key decision, customer, and vendor relationship runs through the owner
Diversified customers	Losing one customer shouldn't threaten the business	A single customer over 15% to 20% of revenue, or top five over half
Recurring or repeat revenue	Contracts, subscriptions, and service agreements make cash flow predictable	Mostly one-time, project-based, or bid work
Healthy, stable margins	Shows pricing power and operating discipline	Margins that swing widely year to year without explanation

What buyers look for	Why it matters	Red flags
Clean, credible financials	Buyers can trust the earnings they are paying for	Cash-basis books, commingled personal expenses, many "adjustments"
Untapped improvement potential	Gives the buyer a clear path to the 10% to 12% annual growth it needs	No obvious next step, or a business already fully optimized
A defensible niche	Protects margins from competitors	Commodity product with price-driven customers
A fragmented industry	Creates add-on opportunities for a buy-and-build strategy	A market dominated by a few large competitors

CLA's 2026 outlook highlights two traits that matter more than they did a few years ago: tariff resilience and predictable cash flow. It names business services, healthcare, and tech-enabled platforms as sectors that remain attractive. PitchBook data also shows B2B companies are growing as a percentage of private equity deal count, while buyers of software companies are concentrating on business tools they believe are protected from AI disruption.

> ***Key term: quality of earnings***
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> *A quality of earnings (QoE) report is an accounting review a buyer commissions, or a seller commissions in advance, to test whether reported EBITDA reflects the real, repeatable earning power of the business. It scrutinizes the owner's "add-backs" such as personal expenses and one-time costs, revenue recognition, and working capital. Surprises in a QoE are one of the most common reasons deals are repriced or fall apart.*

Does quality still earn a premium?

The evidence here is mixed. GF Data found that companies with above-average financial performance sold for 7.3x in 2025, versus 7.1x for other buyouts. That 2% premium is the smallest in its tracked history. CLA argues the opposite: that "the gap between top-tier and average assets remains wide."

Both may be true. Average multiples measure only the deals that close. Weaker companies often never reach a signed deal, or they close with more of the price deferred into earnouts and seller notes, which a headline multiple doesn't capture. Quality may show up less in the multiple than in whether a deal happens at all and how much of the price is paid at closing.

Lessons for owners, whether or not you sell

The practices that make a business attractive to private equity also make it more profitable, more resilient, and less dependent on you. You don't need a buyer to start on any of them, and you capture the full benefit if you do them yourself.

1. Run a pricing review

Look at profitability by customer, product, and channel, not just in total. Most owners find some customers and products that earn far less than they thought, and others that could bear higher prices. If you haven't revisited your pricing structure in three years, start here. It's the lever buyers reach for first because it's usually the fastest.

2. Build a management team that can run without you

Identify the two or three roles that would most reduce your personal involvement, often a finance leader and an operations or sales leader, and fill them with people who can make decisions. Move customer and vendor relationships onto your team. A buyer who sees the business running well while you're on vacation will pay more and ask for less of the price to be deferred.

3. Get your financials to investor grade

Move to accrual accounting if you haven't, close the books monthly within two weeks, and separate personal expenses from the business. Consider a reviewed or audited financial statement, and for owners thinking about a sale in the next two or three years, a sell-side quality of earnings report. Clean books shorten diligence, reduce price renegotiation, and give you better information to run the business.

4. Reduce customer concentration

If one customer accounts for a large share of revenue, make diversification a strategic goal with a target and a timeline. Where you can't reduce the share quickly, lengthen and formalize the relationship with multi-year contracts.

5. Put your working capital to work

Measure how many days it takes to collect receivables, how many days of inventory you hold, and how quickly you pay suppliers. Tightening collections and right-sizing inventory frees cash you can reinvest or distribute. In today's rate environment, that cash is worth more than it has been in 15 years.

6. Document how the business works

Write down your key processes, from quoting and order fulfillment to hiring and the monthly close. Documentation makes the business easier to train, scale, and integrate, and it shows a buyer that the company's know-how doesn't live only in a few people's heads.

7. Grow recurring revenue

Look for ways to turn one-time sales into ongoing relationships: service contracts, maintenance agreements, subscriptions, or replenishment programs. Predictable revenue makes the business easier to plan and finance, and buyers value it more highly than the same dollars earned project by project.

> ***Owner takeaway***

> *Start two to three years before you might want to sell. Most of these changes take time to show up in your financial results, and buyers want to see a track record, not a recent promise. Owners who begin early can sell on their own timeline rather than a buyer's.*

Owner's self-assessment scorecard

Rate your business from 1 to 5 on each criterion below, using the descriptions as anchors. A total of 40 or more suggests a business that buyers would see as well prepared. A score of 2 or less on any line is worth addressing regardless of your total, because buyers tend to focus on the weakest link.

Criterion	1: Needs work	5: Investor ready	Your score
Owner independence	Owner holds key customer, vendor, and operating decisions	Leadership team runs daily operations; owner focuses on strategy	
Management depth	No second layer of leaders	Finance, operations, and sales led by capable, retained managers	
Customer diversification	One customer is more than 25% of revenue	No customer above 10% of revenue	
Revenue predictability	Mostly one-time or project work	Majority of revenue is contracted, recurring, or reliably repeat	
Financial reporting	Cash-basis books, closed quarterly or later	Accrual books closed monthly within 15 days; reviewed or audited	
Margin and pricing discipline	Pricing set by habit; margins not tracked by customer or product	Regular pricing reviews; margin tracked by customer and product	
Working capital	Collections and inventory not measured	Receivable and inventory days tracked and managed to targets	
Documented processes	Know-how lives in a few people's heads	Core processes written down and followed	

Criterion	1: Needs work	5: Investor ready	Your score
Growth path	No clear plan beyond current customers	Specific, credible plan for new customers, markets, or acquisitions	
Market position	Competes mainly on price	Defensible niche, specialty, or reputation that supports pricing	
Total			**/ 50**

Questions to ask if a Private Equity firm calls

An unsolicited call from a buyer is flattering, and it's often the start of a long process. Before you share financials, ask questions that reveal what the buyer really wants and how the deal would work. Good buyers welcome them.

About the buyer

- What kind of capital do you invest: a committed fund, deal-by-deal money from an independent sponsor, or a family office? How much is left in the fund, and when does it need to be returned?
- Would we be a platform or an add-on to a company you already own? If an add-on, which company, and how would we be combined with it?
- How long do you typically hold companies? What happened to the founders and employees of businesses you've sold?
- Can I speak with owners of companies you've bought, including one where things didn't go as planned?

About the deal

- Are you proposing to buy a majority or a minority stake? What decisions would I be allowed to make post the investment, and which would require your approval?
- How much of the purchase price would be paid in cash at closing, and how much through rollover equity, earnouts, or seller notes?
- If I roll over my equity, what do I own, on what terms, and how is it treated when you sell?
- How much debt will the business carry after closing, and what happens if we miss a covenant?
- Will you use representation and warranty insurance, and how would that affect any escrow or holdback of my proceeds?

> ***Key term: rollover equity***
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> *Rollover equity is the portion of the sale price an owner reinvests in the business alongside the buyer, usually a minority share of the proceeds. It keeps the owner aligned with the buyer and offers a "second bite" if the business is sold again at a higher value. It also means part of your proceeds stay at risk until the buyer's exit.*

About you and your people

- What role do you expect me to play after closing, for how long, and with what compensation?
- What changes do you expect in the first 100 days? Can I see the draft of a value-creation plan you would likely put in place?
- Do you plan to keep our name, location, and leadership team? Will employees have the opportunity to share in the equity?
- What would you need to see in diligence to confirm your valuation, and what typically causes you to change the price?

An experienced M&A adviser, attorney, and tax adviser are worth engaging before you sign a letter of intent. Many of the most important terms are set at that stage, when the seller has the most leverage.

Conclusion

Private equity is one of the most active buyers of lower middle market businesses, and with millions of owners approaching retirement, it will remain so for years. But today's private buyers are paying for something different than they were a decade ago. Without cheap debt and rising valuations to rely on, they need businesses with dependable earnings and a clear path to growth.

That gives owners an opportunity. The things private equity firms do after they buy a company, such as disciplined pricing, smarter purchasing, tighter cash management, professional management, and modern systems, are things owners can do themselves. Done well, they make a business more profitable and less dependent on its founder. If a sale does come, the owner who has done that work is paid for it and negotiates from a position of strength.

Whether you plan to sell in two years, 20 years, or never, it pays to look at your business the way a buyer would.

Sources and disclosures

Sources

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Examples labeled "illustrative" are composites created for explanation and don't describe any specific company or transaction.

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