

BMO Middle Market M&A update

Trump's "Big Beautiful Bill" Could Be a Big Beautiful Catalyst for M&A

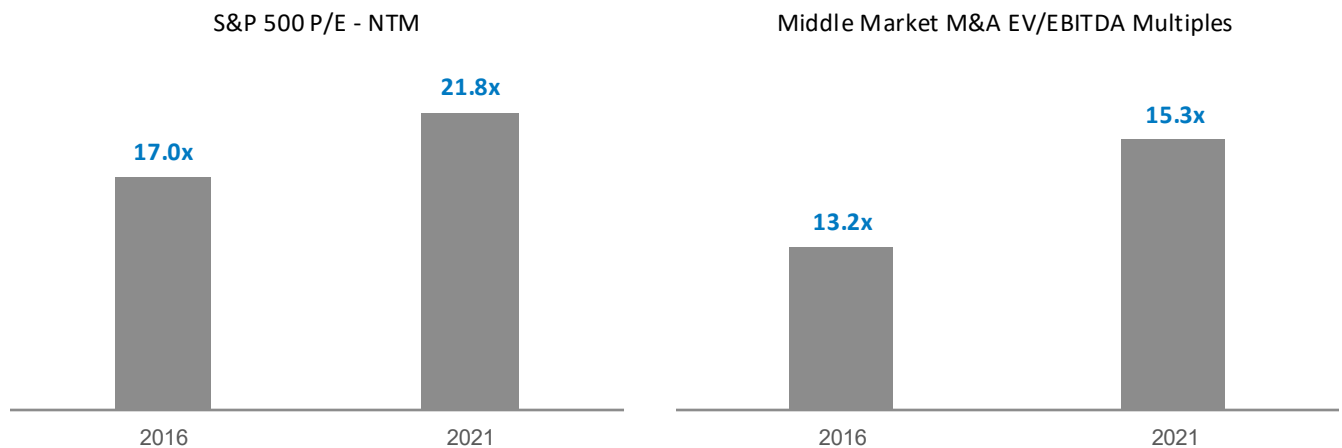
As we enter Q4 2025, business owners, investors, and advisors are closely watching to see if recent changes to the tax code will have a meaningful impact on M&A activity. The Opportunity, Business Building, and Budget Act (OBBBA), dubbed the "Big Beautiful Bill," includes a series of tax provisions aimed at improving cash flow, simplifying succession planning, and enhancing deal economics—many of which build on the framework established by the 2017 Tax Cuts and Jobs Act (TCJA).

The TCJA had a measurable effect on the M&A landscape. Data shows that public company valuation multiples increased ~30%⁽¹⁾ and Middle Market M&A EBITDA multiples increased ~15%⁽²⁾ post-TCJA pointing to the powerful role tax reform can play in driving deal value.

Today's market is more selective. Buyers are narrowing their focus and extending diligence timelines, making it harder for sellers to achieve premium outcomes without clear differentiators. Companies that demonstrate strong cash flow, scalable operations, and tax-efficient structures are consistently outperforming peers in valuation and deal velocity.

The OBBBA provides immediate opportunities to strengthen free cash flow. By making the QBI deduction permanent, expanding Section 179 expensing, restoring EBITDA-based interest deductibility, and increasing estate tax exemptions, the bill would improve after-tax earnings and reduce friction in ownership transitions. These changes would make businesses more attractive to buyers and easier to prepare for sale.

Valuation Multiples Increased Post TCJA (2016-2021)^(1,2):



1. FactSet
2. MergerMarket – M&A Transactions with Enterprise Values Between \$50M–\$500M

Policy Mechanics and Deal Implications

The OBBBA introduces a series of structural tax reforms that are likely to influence both the economics and timing of middle market transactions. The permanent extension of the Qualified Business Income (QBI) deduction at the 20% rate, coupled with expanded income thresholds, enhances after-tax earnings for a broad range of pass-through entities. This change is particularly relevant for professional services firms and founder-led businesses, where tax efficiency directly impacts valuation.

Capital investment incentives are also strengthened. The increase in Section 179 expensing to \$2.5 million, with a \$4 million phase-out threshold, allows businesses to immediately deduct qualifying equipment and property. This provision immediately improves after-tax cash flow for businesses, driving strategic reinvestment into operations. When paired with the reinstatement of 100% bonus depreciation and permanent R&D expensing, the bill further provides an avenue to reduce taxable income, creating a favorable environment for growth initiatives and capacity.

The restoration of EBITDA-based interest deductibility under Section 163(j) is another notable shift. By lowering the after-tax cost of debt, this provision improves the viability of LBOs and supports more flexible capital structures. After the TCJA, switching to EBIT-based limits made it harder to structure leveraged buyouts efficiently. The OBBBA reverses that change, making it easier to use debt creatively in deal structures again.

Sector-Specific Effects and Strategic Considerations

The implications of the OBBBA vary across sectors. Manufacturing businesses, which tend to be capital-intensive, are likely to benefit disproportionately from the expensing and accelerated depreciation provisions. Historical data from the TCJA period shows that manufacturers experienced valuation uplifts exceeding 65%¹, driven in part by bonus depreciation and improved cash flow.

Technology and tech-enabled services businesses, especially those with recurring revenue and scalable models, could see stronger valuations. With more room to invest and fewer tax related hurdles, growth strategies may accelerate, particularly in fragmented sectors where consolidation is already underway.

Family-owned enterprises face a more favorable succession planning landscape. The increase in estate and gift tax exemptions to \$15 million per individual (\$30 million per couple), indexed for inflation, simplifies ownership transitions and supports cleaner cap tables. This change may encourage earlier engagement with exit planning and transaction readiness.

Capital Formation and Investment Incentives

The OBBBA includes several provisions that could make it easier for private equity sponsors and institutional investors to structure and deploy capital. Keeping long term capital gains treatment for carried interest helps maintain the economics of sponsor returns and gives LPs more confidence in fund performance. The updates to Qualified Small Business Stock, including higher gain exclusions and shorter holding periods, may also encourage earlier stage investments and speed up exits. In addition, making Opportunity Zones permanent with rolling ten-year windows starting in 2027 gives investors a longer runway to pursue tax advantaged deals in underserved markets.

1. Norwegian School of Economics (2020)
2. BMO Economics, U.S. Economic Outlook, September 5, 2025

Market Conditions and Outlook

Q3 2025 was marked by cautious optimism in the middle market. While diligence timelines remain extended and valuation discipline persists, deal flow has stabilized in sectors with resilient margins and defensible business models. Buyers continue to prioritize operational scalability and financial transparency, and sellers who meet these criteria are achieving favorable outcomes.

Macroeconomic indicators provide additional context for the current M&A environment. According to BMO Economics (September 2025), real GDP growth is projected to reach 2.4% in Q3 and 3.1% in Q4, driven by resilient consumer spending and a rebound in business investment, particularly in non-residential construction and intellectual property. These trends align with the Opportunity, Business Building, and Budget Act's incentives for capital deployment, and may further support deal activity in asset heavy and innovation driven sectors.

The interest rate environment remains elevated, with the Federal Funds Rate expected to stay above 5% and 10-year Treasury yields stabilizing around 4.2%. While higher rates continue to pressure financing costs, the OBBBA's restoration of EBITDA-based interest deductibility may help mitigate these headwinds, particularly for leveraged transactions.

Corporate profitability is also expected to improve, with real disposable income and personal income trending upward. These indicators suggest that middle market businesses may enter 2026 with stronger balance sheets and improved cash flow, factors that enhance valuation and transaction readiness.

Conclusion

The OBBBA represents a significant shift in the tax landscape with direct implications for middle market M&A. By enhancing cash flow, reducing tax liabilities, and supporting capital deployment, the legislation creates conditions conducive to higher valuations and more efficient transactions. Stakeholders across the M&A ecosystem should evaluate the structural implications of the bill and consider how its provisions may influence strategic planning and execution over the coming quarters.

Let's connect

Whether you're expanding through acquisition or ready to transition ownership of the business, our middle-market M&A experts are ready to help you take your company to the next phase.



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