STRATEGIC ADVISORS
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Bringing Efficiency to Inefficient Markets

2012

M&A AND CORPORATE FINANCE OVERVIEW

Third Quarter

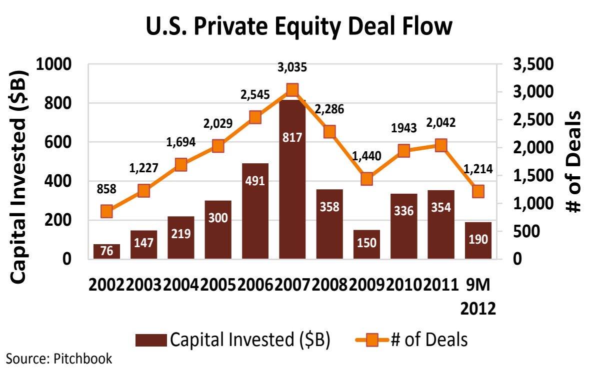
Merger & Acquisition
Corporate Finance Advisory
Strategic Consulting

400 Southpointe Boulevard, Plaza I, Suite 440
Canonsburg, PA 15317 • Tel. 724-743-5800
Fax 724-743-5870 • www.strategicad.com

Strategic Advisors is a middle market investment banking firm that helps clients achieve financial and business goals by providing merger and acquisition advisory, corporate finance advisory and strategic consulting services. Along with many years of experience in advising middle market clients, our Managing Directors have experience investing in and managing portfolio companies. As such, Strategic Advisors not only has expertise in advisory services but also firsthand knowledge of what stakeholders, investors and lenders expect and desire.

Merger and Acquisition Overview

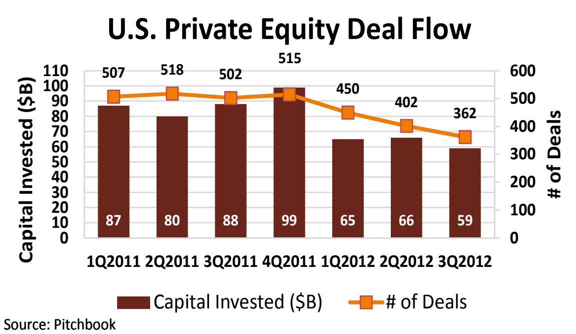
- Going into 2012 it appeared the U. S. private equity (PE) industry may finally have been primed for a full-fledged recovery following two consecutive years of impressive growth. However, after slipping in the first quarter of 2012, the PE deal-making market failed to recover and fell for the third straight quarter. The predicament in Europe continues to worsen, the U.S. economy has consistently underperformed expectations, and the impending fiscal cliff all point to a gloomy outlook.



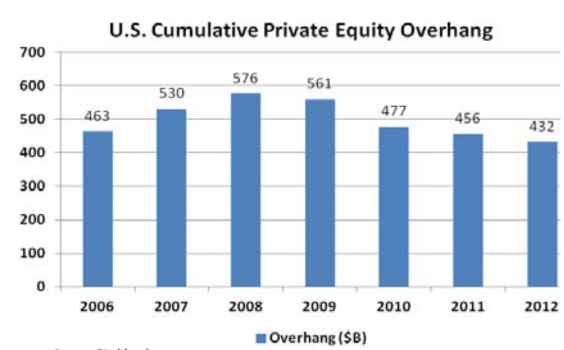
- Despite the near-term ominous outlook, it is difficult to believe that PE can continue with these low levels of investment much longer. Several industry forces including a mountain of dry powder and a deep inventory of aged PE–backed portfolio companies seem to suggest that deal making should accelerate.

- The Small Business Optimism Index as reported by National Federation of Small Businesses (NFIB) has once again declined by 0.1 in September to 92.8 after increasing by 1.7 to 92.9 in August 2012. Since monthly surveys were started in 1986, the Index has been below 93.0 only fifty-six times, with thirty-two of those readings occurring since the recovery began in June of 2009. Prior to 2008 this index averaged 100; significantly over the current reading. The uncertainty over the future of the economy, the rising cost of health care, and the cost of taxes and regulations are all impediments to a recovery. These factors make it difficult for the small business owner to make commitments to new spending and hiring.

- 2012 private equity activity is clearly lower than in recent years. Pitchbook notes the amount of capital invested in the third quarter decreased by 11% from the previous quarter. They further note that when comparing the third quarter volume to the same period in 2011, the results are even worse, showing a decline of 28% in deal volume and 33% in invested capital. The 362 deals and $59 billion invested in the third quarter are the lowest level invested since 2009.

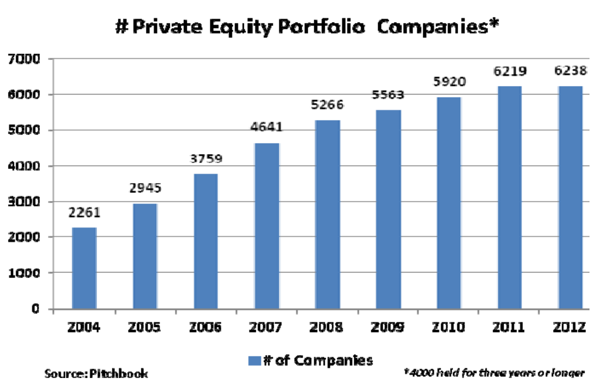


- Private equity groups (PEGs) continued to be dissuaded from completing transactions by the fear of the U.S. entering another recession. However, this trend will likely change as PE firms will have to make a concerted effort to prudently invest their more than $432 billion of dry powder.

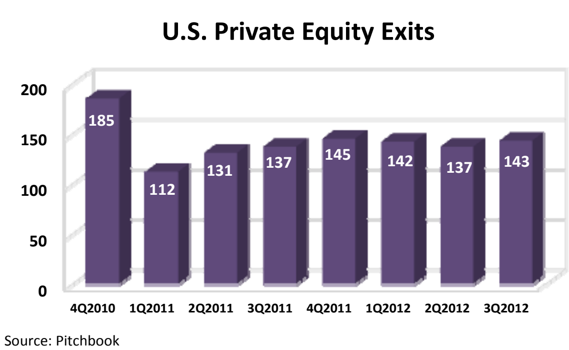


- In this report we will examine third quarter activity and review the year to date. Some of the highlights include a further drop in deal volume, which has been in a steady decline for over a year; the lowest level of PE investment since 2009; and year-over-year declines in exit volume and capital. Pitchbook, in their fourth quarter Private Equity Breakdown, notes the only optimism was the steady level of fundraising. This is normally a leading indicator of activity to come.

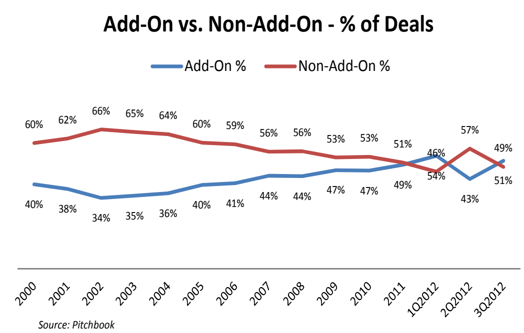
- Pitchbook also believes that PEG's with a significant inventory of PE-backed companies sitting in their portfolios, 64.5% of which have been held for three years or longer, and the looming fiscal cliff should further drive deal volume.



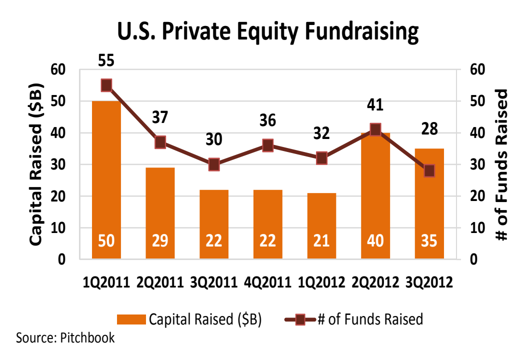
- For the fifth consecutive quarter, U.S. PEGs exited over 100 investments. Since hitting a nadir of 233 exits in 2009, activity rebounded strongly and is back to pre-recession levels. The number of quarterly exits has remained remarkably steady for the last six quarters. PE firms executed 143 exits in the third quarter, but capital exited dropped to $20 billion. This is lowest level in more than two years. Sales to strategic acquirers (corporate acquisitions) remained the most common exit strategy, representing 78% of exit activity.



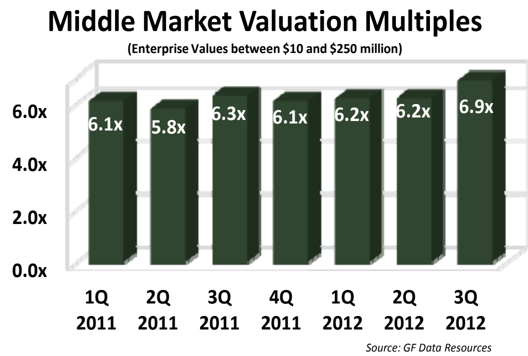
- Add-ons accounted for more than half (51%) of the buyout activity in the third quarter of 2012. Add-on deals have typically been used as a means of increasing the operational capacity of portfolio companies, but PE firms are increasingly viewing add-on as a viable way to put capital to work as well. Since 2005, add-ons, as a percentage of yearly buyout activity, have been on a steady upward trend. Five years ago, add-on transactions comprised approximately 40% of all U.S. PEG transactions.

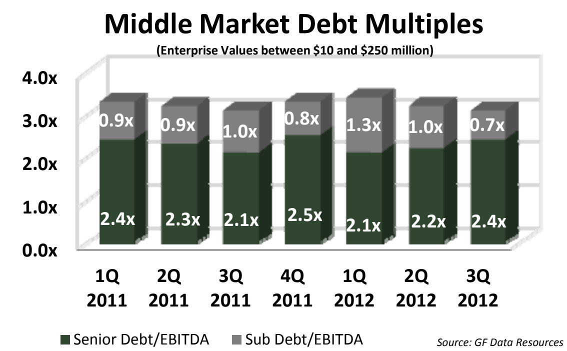


- As seen in the chart below, U.S. Private Equity fundraising declined slightly in the 3rd quarter of 2012; however, it was still relatively strong in comparison to 2011. Although dealmakers were frustrated by the declining deal volume, institutional investors seem to be bullish on the future of deal-making. In the third quarter of 2012, twenty-eight (28) funds closed with a total of $35 billion in capital commitments, which was a marked improvement over the third quarter of 2011.

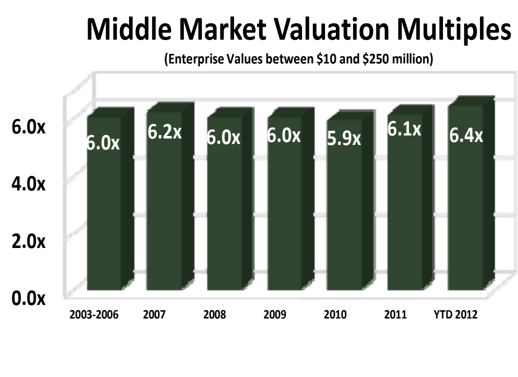


The runoff of the dry powder and the healthy level of exits seem to have convinced fund managers and investors that the PE industry has found its footing; finally adapting to the current economic environment and the subdued deal-making markets.





- U.S. middle market transaction multiples for businesses sold to financial firms averaged approximately 6.9x EBITDA in the third quarter of 2012, according to GF Data Resources, reaching their highest level in the last ten years. Small transactions ($10-25 million) accounted for the majority of the pick-up, with their total enterprise values (TEV) averaging 6.3x in the third quarter versus 5.4x in the second quarter of 2012. GF Data makes an interesting observation that individual owners of small business are anxious about the larger economy and reinvestment options, so they are not adverse to holding on to their businesses. As a result, they have been less willing to make a concession on price. Also, larger ($50-250 million) and higher quality transactions continue to demand a premium.

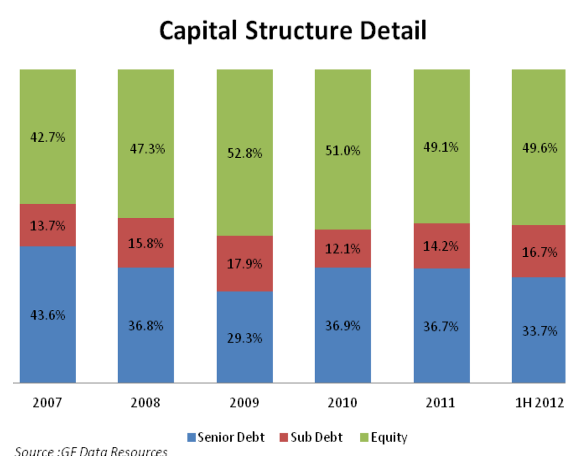


- Looking at the year to date rather than the individual quarter smoothes out the spike, but the trend is still unmistakable. Valuations for the first nine months of 2012 are up sharply. Given the significant private equity overhang and the scarcity of high quality deals financial buyers are working hard to find platforms to invest in, often paying a quality premium for a business with above-average financial characteristics.

- Leverage multiples remained in the low threes for total debt and the low twos for senior debt. More liberal debt structures continue to be available for larger deals. Senior debt spreads over LIBOR have been 4.8% to 4.9% throughout 2012.

- The growing presence of the one-stop financing approach, as well as an increasing number of mezzanine lenders, continue to become a greater part of capital structures and stand ready to fill any void in the market. Mezzanine investors are more aggressively pricing transactions (current interest) with the average spread over LIBOR falling to 11.1% in the third quarter of 2012 from 12.3% in the second quarter.

- Although bank financing is plentiful and aggressively priced, banks have become more conservative on structure, resulting in senior debt accounting for only about one third of an average buyout transaction's capital structure. These conservative leverage ratios are establishing upper limits on financial buyer valuations.



Capital Markets Overview

- The equity contribution to a capital structure in the third quarter of 2012 made up 49.6% of a transaction's capitalization.

- In forecasting M&A activity for the remainder of 2012, the overall health of the global economy continues to be the primary factor that must be evaluated. The volatility of the European Union causes concern amongst investors. The underperforming U.S. economy and the uncertainty of the tax environment is causing investors to pause and proceed with extreme caution. At this point, the near-term outlook for deal activity looks gloomy for the remainder of 2012. However, glimmers of hope are beginning to emerge, creating some optimism that 2013 may be a more robust year.

For more information, please contact any of the professionals listed below or visit our website at www.strategicad.com

Andy Hays	*Managing Director and Founder*	arhays@strategicad.com	724-743-5810
Andy Bianco	*Managing Director and Founder*	ajbianco@strategicad.com	724-743-5820
Matt Steve	*Senior Associate*	masteve@strategicad.com	724-743-5830
Marcia McCracken	*Administrative Assistant*	mjm@strategicad.com	724-743-5800

When considering a sale of your business, the acquisition of a business, or the restructuring or recapitalization of your balance sheet, the best pathway for achieving your expectations is a well-run sale process that addresses all your business and personal goals. Strategic Advisors is accustomed to working with business owners to determine the best pathway to achieve their goals and objectives. Give us a call to discuss your possibilities.

Authors: Andy Hays, Managing Director and Founder
Andy Bianco, Managing Director and Founder
Matt Steve, Senior Associate

Sources: Pitchbook - The Private Equity 4Q 2012 Breakdown; GF Data Resources November 2012 Report; NFIB Small Business Economic Trends, October 2012

Important Information