STRATEGIC ADVISORS
Middle Market Investment Bankers

Bringing Efficiency to Inefficient Markets

The Strategic Alternatives Review

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Objectives

- **Introduce *The Strategic Alternatives Review***
- **Review examples of *The Strategic Alternatives Review***
- **Review the benefits of *The Strategic Alternatives Review***

Strategic Alternatives Review - Approach

The Strategic Alternatives Review provides a framework for business owners to explore their available strategic & capital market alternatives, enabling them to meet their goals and objectives. We view the business owners' current inherent equity value as a portfolio asset that is invested or "rolled over" into the business. This rolled over equity has a clear return when viewed over a five year period. All established Strategic Alternatives are evaluated in context of risk (business and market), wealth creation, returns on equity and other alternatives that may meet stakeholder goals and objectives.

Strategic Alternatives (May include any or all of the below)

- Status Quo – what if company continues as is – provides the baseline
- Recapitalization
- Acquisition(s)
- Investment in new initiatives
- Divestiture

Approach:

- Understand the goals and objectives of the shareholders and managers
- Establish a "Status Quo" alternative of the business based upon a five year projection
- Determine Value (DCF, Market Comparables and Leverage Test)
- Develop other strategic alternatives that meet shareholder objectives
- Summarize alternatives and review business and financial impacts of implementing each alternative
- Compare alternatives on the basis of risk, wealth creation and meeting owners' objectives
- Make recommendations and assist in selecting the most appropriate alternative

Strategic Alternatives Review

The Risk / Return Profile of Invested Capital – The Effects of Leverage

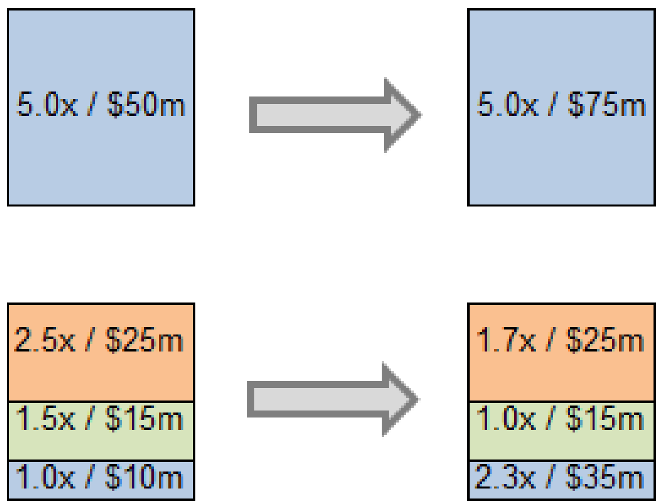
- Illustration displays effect of returns on equity under two leverage scenarios
- Illustration assumes Enterprise Value equals 5.0x EBITDA
- IRRs are based on Current Market Equity Value

Current EBITDA = $10m
Current Value = $50m

EBITDA in 5 years = $15m
Value in 5 years= $75m

<u>Scenario 1</u> -
Fully Invested:
5.0x Equity
No Debt

<u>Scenario 2</u> -
Leveraged with:
2.5x Senior Debt
1.5x Subordinated Debt
1.0x Equity



Total Equity Return = 50%

Equity IRR = 8%

Total Equity Return = 250%

Equity IRR = 28%

Strategic Alternatives Review

Possible Strategic Alternatives to be Developed

- ***Status Quo:***
  - Establishes a base line - Determines return on equity based on a five-year projection
    - Projection provided by management or based on industry estimates - organic growth only
- ***Recapitalization:***
  - Determines debt capacity and analyzes various leverage scenarios
    - On underleveraged entities, recap could be an alternative to selling
    - On leveraged entities, recap could create liquidity and/or reduce overall cost of capital
  - Determines ability to pay dividend to diversify "portfolio holdings" or to buyout current owners
  - Provides potential to increase return on equity on reinvested capital
- ***Acquisition(s):***
  - Establishes maximum acquisition size based on:
    - Current equity value that can be used to fund an acquisition
    - Current capital market constraints (leverage multiples) &Shareholders' risk tolerance
  - Allows for a diversification of "portfolio holdings" on a tax deferred basis
  - Enhances return on equity & wealth creation on invested capital through increased leverage
- ***Investments in new initiatives***
  - Explores potential benefits, costs & impact on financial risk and returns
- ***Divestiture:***
  - Explores sale to financial buyers, strategic buyers & management
  - Buyers targeted are determined by goals & objectives of owners

Developing the Status Quo Analysis – Six-Step Approach

1. **Identify specific shareholder goals and objectives**
2. **Establish a five-year “normalized” projection**
3. **Formulate a SWOT analysis (Strengths, Weaknesses, Opportunities & Threats)**
4. **Develop an industry & competitive profile**
5. **Determine Value (DCF, Market Comps & Leverage Test)**
6. **Assess other stakeholder objectives**

Strategic Alternatives Review

CURRENT STATUS

STATUS QUO ANALYSIS

- SWOT Analysis
- Industry Dynamics
- Valuation
- Other Stakeholders' Objectives
- Five-Year Forecast
- Owners' Objectives

FUTURE ALTERNATIVES

STATUS QUO

- No major changes
- Normal growth
- Base case
- 5 year forecast
- Current equity value
- Future equity value
- Determines 5 yr IRR
- Used as "hurdle rate"

RECAP

- Tests debt capacity
- Max leverage found
- Could use sub debt
- Diversifies holdings
- Min. equity dilution
- Max. current cash
- Retains control
- Reinvestment IRR

ACQUISITION GROWTH

- Models investments
- Leverages equity
- Tests debt capacity
- Establishes criteria
- Max deal size
- 5 year forecast
- Determines 5 yr IRR
- Proj. wealth created

DIVESTITURE

- Market comps
- Val: financial buyer
- Val: strategic buyer
- Max. current $$
- Diversifies all risk

Example – Pinnacle Electronics – EMS contract manufacturer

Scenario	Pinnacle initially purchased by Main Street Capital (MSC) for $7MM MSC helped grow company to sales of $38MM & EBITDA of $7MM; SA valuation was at $37 to $41MM Company had no debt; therefore value to owners equaled $37 to $41MM ($39MM) Company faced potential "Asia threat" in future; manager (25% owner) wanted to explore exit MSC hired SA to explore strategic alternatives
Alternatives	**Status Quo**: Estimated a five-year IRR on equity at 14.8% **Recap**: Estimated a dividend of $21MM (58% of value) while giving up 9% warrant Total debt to EBITDA of 3.75x IRR on reinvested capital increased from 14.8% to 23.1% **Acquisition**: Acquire two smaller EMS firms over next two years @ $6MM each Leverage with senior debt Diversify customer base IRR on reinvested $39MM equity increased to 28.3% 5th year equity value increases to $136MM vs $77MM on Status Quo **Divestiture**: Sale to financial buyer estimated @ $37MM; sale to strategic buyer @ $41MM MBO not considered as manager desired exit
Conclusion	SA hired to sell company Goal was to maximize proceeds while keeping entity intact in Pittsburgh Sale was completed to strategic buyer @ $43MM

Example - Project Tools

Scenario	Family-owned, second-generation-controlled business Sales of \$60MM & EBITDA of \$8MM; SA valuation was at \$40 to \$44MM Company had no debt; therefore value to owners equaled \$40 to \$44MM (\$43MM) Company forecast 3.7% growth over next five years; faced cyclicality risks SA completed *Strategic Alternatives Review* Company concluded acquisition strategy was optimal to meet objectives
Alternatives	**Status Quo**: Estimated a five-year IRR on \$42MM equity estimated at 12.4% **Recap**: Estimated a dividend of \$30MM (75% of value) while giving up 15% warrant Total debt to EBITDA of 3.75x IRR on reinvested capital increased from 12.4% to 22.5% **Acquisition**: Model one acquisition maximizing senior debt for \$41MM Fifth year equity value increased from \$72MM to \$97MM IRR on \$40MM equity increased from 12.4% to 19.2% Modeled second acquisition maximizing all debt (senior & sub) @ \$71MM Larger acquisition strategy eliminated as return on equity only rose to 22.5% **Divestiture**: Sale to financial buyer estimated @ \$40MM; sale to strategic buyer @ \$44MM
Conclusion	SA hired to conduct acquisition search

Example - Summary of Alternatives

Statistics	Prior Year
Sales	$60.0
EBITDA	$6.5

Value	Financial	Strategic
Enterprise Value	$35.6	$39.2
Less Debt	($4.3)	($4.3)
Equity Value	**$31.3**	**$34.9**

Alternative	Reinvested Equity	5th Year Equity Value	Return on Reinvested Equity	Equity PV at Hurdle Rate	Comments
Status Quo	$31.3	$60.6	14.1% (Hurdle Rate)	$31.3	• Concentration of wealth remains • Must continue to grow at 3.7% • Does not diversify strategy
Recapitalization $19.5MM pre-tax dividend $0.9MM transaction costs	$31.3 (19.5) (0.9) $10.9	$36.4	24.8%	$17.1 19.5 $36.6	• Increases equity return via leverage • Addresses concentration of wealth • Conservatively utilizes mezzanine debt • Retention of 85% economic equity
Acquisition Purchase Price of $30.7MM No synergies	$31.3	$74.8	19.0%	$38.7	• Increases IRR through leverage • Potential for diversification of earnings • Could address Asian issue • Concentration of wealth remains
Management Buyout Sale to Mgmt. for $31.3MM Financial Buyer price	NA	NA	NA	$31.3	• Addresses concentration of wealth • Allows for Management succession • Keep company intact • $1.0MM required investment by Mgmt.
Divestiture Sale to Strategic Buyer @ $34.9MM	NA	NA	NA	$34.9	• Goal is to keep the company intact • Maximizes shareholder's current wealth • Owners have reinvestment risks

Strategic Alternatives Review

Benefits to Clients

- Establishes a five-year baseline projection
- Determines market value of enterprise and owners' equity
- Brings management & owners together on an agreed projection
- Helps owners view their equity in their business as an "IRR portfolio asset"
- Begins process of long-term financial planning by establishing goals and objectives
- Provides framework to explore strategic and capital market alternatives
- Concludes with selection of agreed-upon strategy

Strategic Alternatives Review

Timetable for completing the *Strategic Alternatives Review*

Execution of engagement letter	
Due diligence	**2 – 3 days**
Industry research, financial modeling and valuation	**2 weeks**
Report preparation	**1 week**
Preliminary review with management	**3 days**
Final presentation to shareholders	**1 day**
Estimated time to complete	**One month**

Sample Transaction – Strategic Alternatives Review/Divestiture

Company	***Pinnacle Electronics***	
Description	**Electronic Contract Manufacturing Services Company and manufacturer of Javelin POS terminals**	
Finanicals	**Sales**	**$38MM**
	EBITDA	**$7MM**

Situation

> Company was purchased in 2001 by Main Street Capital and Management

> Company had grown significantly over the last three years and paid down debt, despite being in an industry that was hit hard by the recession

> Board of Directors wanted to review strategic alternatives including a divestiture, recapitalization, acquisition strategy, and status quo alternative

> CEO desired to cash out significant equity interest and exit the business

> Other Management wanted to remain employed and keep business in Pittsburgh

Solution

> SA presented to the Board of Directors an analysis of all the strategic alternatives showing value created to the owners over five years under each scenario

> Valued the Company at $37MM (financial) to $41MM (strategic)

Outcome

> Based upon the analysis, Board of Directors decided to divest

> Prepared sale memorandum and targeted both strategic and financial buyers

> Sold the Company for $43MM to LaBarge, Inc., a St. Louis based public company

> CEO exited the Company and existing Management remained with LaBarge, Inc.

> The business remained in Pittsburgh

Sample Transaction – Representation for PEG

Company ***Susquehanna Capital***

Description

Central Pennsylvania Private Equity Fund that invests in regional middle market companies
Owners of five privately-held companies with revenues ranging from $30MM to $130MM

Sold York Label and York Barbell
Arranged LBO of Interface Solutions, Cooper Manufacturing Co., Herculite Products and New York Wire

Services Provided

- Representation for Acquisition and Divestiture Activity
- Investment Opportunity Review
- Risk Assessment
- Valuation
- Financial Modeling
- Capital Structure Alternatives
- Capital Formation
- Letter of Intent / Purchase Agreement Advice
- Due Diligence Review

Structure

- Acquisition Advisory - Success fee based on debt commitments raised
- Divestiture Advisory - Success fee based on aggregate purchase price

Sample Transaction – Advisory & Divestiture

Company ***Pyott-Boone Electronics, Inc.***

Description A leading developer, manufacturer and marketer of extensive and technologically-advanced communication, tracking, and monitoring products for underground mining and tunneling.

Financials

Sales	$45.5MM
EBITDA	$12.0MM

Situation

- Pyott-Boone was 99.8% owned by Fetterolf Group, Inc.
- During 33 years of ownership, Fetterolf Group achieved its business goals and was seeking to monetize its investment in the Company.
- Pyott-Boone had been growing rapidly after capitalizing on increased regulation to create safer and more productive underground mining environments.
- The Company was looking for strategic investors to build on its past success by expanding the Company’s product offering and service solutions for existing customers, as well as new customers in international markets and in other industries.

Solution

- Fetterolf Group engaged Strategic Advisors to advise on valuation and run a controlled auction process to sell the Company.
- Ran controlled auction process, targeting over 150 buyers comprised of private equity and strategic buyers
- Generated significant interest, receiving 10 indications of interest ("IOI") and turning away additional offers that couldn't meet valuation expectations

Outcome

- Company was sold to Vierville Capital and Prairie Capital
- This combination of equity partners brought a strong and experienced investment team with significant international relationships.
- Company sold for $68.0MM, and the Fetterolf Group also received an additional $10MM+ of balance sheet cash on a tax-free basis.
- Management and Fetterolf Group rolled over $2.0MM+ into the transaction in order to participate in the company’s future growth.

Sample Transaction – Public to Private / Cradle to Grave

Company	***The Lion Brewery***	
Description	Contract packager in beverage industry	
Financials	Sales	$40.0**MM**
	EBITDA	$5.0**MM**

Situation

- Management team acquired the Company in 1999 with a financial partner (Mgmt 46%, Partner 54%)
- In 2005, Strategic Advisor assisted the Company in completing a recap, allowing Management to acquire 100% of the business.
- Beverage industry experiences shift to healthy drinks at the expense of carbonated, high-sugar drinks
- Company needed substantial investment to expand production facilities and modernize plant
- Financial and strategic players seek to consolidate beverage producers

Solution

- Strategic Advisors advised management on business value and structure
- Advised Management on the Company's favorable position within the industry
- Prepared memorandum and targeted financial and strategic investors
- Strategic Advisors conducted a Controlled Auction to maximize value and goals and objectives of shareholders

Outcome

- Sold to financial buyer as platform for industry consolidation
- Management team received contracts to remain with Company
- Value of Company increased significantly through competitive process

Sample Transaction - Restructuring

Company ***Houghton International***

HOUGHTON INTERNATIONAL
Specialty Chemicals, Oils and Lubricants for Metalworking and Manufacturing Processes

Description Manufacturer of Specialty Chemicals and Lubricants

Financials	Sales	$310	MM
	EBITDA	$24	MM (Normalized)

Situation

> Economic downturn - rising oil and energy prices impacted business
> Selling off non-core assets and reducing overhead
> Chemical management segment rapidly growing
> Senior lenders desired a restructuring
> Needed capital formation services to execute debt restructuring

Solution

> Determined market debt structure based upon normalized earnings, mitigated downside risk by emphasizing enterprise value
> Developed full understanding of cost initiatives and non-recurring expenses
> Raised $25 million of subordinated debt to ease senior bank pressure
> Restructured senior debt with existing bank group to avoid harsh senior debt market conditions

Outcome

> $60 million Revolving Line of Credit, $8 million Senior Term Loan and a $25 million eight year subordinated note (bullet amortization) issued with a detachable warrant

Sample Transaction – Advisory & Divestiture (Family Owned)

Company ***Cygnus Manufacturing Company***

Description Contract manufacturer of highly-complex medical instruments and industrial products

Financials

> Sales $16.0MM
> EBITDA $1.8MM

Situation

> Owner desired to sell the business and move out of the area
> Goal was to keep the Company intact, yet achieve desired selling price
> Company's largest customer represented more than one-half of total revenues

Solution

> Advised owner as to an expected valuation range
> Prepared memorandum; identified potential financial and strategic investors
> Developed strategy for minimizing customer concentration issues
> Successfully positioned Company as key supplier of mission-critical parts and components
> Ran broad auction process to both financial and strategic buyers

Outcome

> Received multiple interest letters from both financial and strategic buyers
> Negotiated letter of intent with a financial buyer who desired to use Company as a platform for growth
> Buyer negotiated employment contracts with key people
> Owner achieved higher-than-expected selling price
> Real estate was also sold to further meet owner's objectives

Firm Overview – Professionals

Andrew J. Bianco - Managing Director Prior experience includes three years as a Principal with Main Street Capital Holdings, Inc., a middle market private equity firm and eight years as Managing Director within the Mellon Strategic Advisors Group which provided merger & acquisition and private placement advisory services to its clients. At Mellon, he headed the Acquisition and Private Placement Group and grew fee income significantly. Furthermore, Mr. Bianco was responsible for originating and completing various acquisition, divestiture and corporate finance engagements. In addition to his technical expertise, Mr. Bianco has developed an extensive national network of lenders and investors. Other experience includes nine years at Westinghouse Financial Services and three years at Corporate Development Partners, Inc., a regional investment banking firm focused on merger & acquisition and private placement services to middle market companies. At Westinghouse Financial Services' Corporate Capital Group, he was intimately involved in establishing and providing private placement capabilities to the group and liquidity to its $3.5 billion debt and equity portfolios and was directly involved in the sale of numerous investments including senior, mezzanine, equity and limited partnership interests. As a Managing Director and Principal at Corporate Development Partners, Mr. Bianco was responsible for originating and completing corporate finance engagements with middle market clients. Mr. Bianco has been a guest speaker at numerous conferences and a guest lecturer at Pittsburgh-based universities colleges including the ACG, National Wealth Management, Carnegie Mellon, Duquesne, and St. Vincent. Certified in Mergers &Acquisitions by the AMAA. Successfully completed the Series 7 and 63 exams. M.S., Corporate Taxation, Robert Morris College. B.S., Accounting, Duquesne University.

Anthony J. Ventura – Managing Director Mr. Ventura has a decade of experience in middle market investment banking. Prior to joining Strategic Advisors he was a Director of Corporate Finance at Schneider Downs, which provided merger and acquisition and private placement advisory services to its clients. He worked for a growth-oriented investment bank now known as Headwaters SC. Prior to his career in investment banking, Mr. Ventura served as an investment and treasury analyst at Carnegie Mellon University and a commercial credit underwriter at PNC Bank. Mr. Ventura is a member of the Association of Corporate Growth and has judged its M.B.A case competition. Completed the FINRA Series 7, 63, and 79 exams. B.A. Managerial Economics, Allegheny College. M.B.A. Finance, Tepper School of Business at Carnegie Mellon University.

Firm Overview – Professionals

Eric A. Wissinger – Managing Director Prior to joining Strategic Advisors, Mr. Wissinger was Managing Director and Head of the Pittsburgh office at Valuation Research Corporation, an international valuation services firm focused on merger & acquisitions, financial restructuring and fairness and solvency opinions. Prior to Valuation Research Corporation, Mr. Wissinger was a Co-Founder, Principal, and Managing Director of Commonwealth Capital Group, L.P., a regional private equity fund dedicated to alternative asset investing in micro-market industrial businesses. In addition, while associated with Commonwealth Capital Group, Mr. Wissinger became President and CEO of a portfolio company of the fund and was responsible for managing all business operations, sales activities and product development. Mr. Wissinger has originated, structured and executed equity transactions with companies ranging from small, closely-held businesses to divisions of international, multi-billion dollar public companies. Mr. Wissinger has developed a significant national network of equity investors and mezzanine and debt providers. Other experience includes a number of years at Arthur Andersen, LLP and Mark I. Wolk and Associates, P.C., a boutique investment banking and financial consulting firm. At Arthur Andersen, Mr. Wissinger was a Senior Manager within the Economic and Financial Consulting practice where he conducting financial valuation studies, investment banking services and restructuring consultation. At Mark I. Wolk and Associates, Mr. Wissinger was a Director and ran the New York office and was responsible for originating and completing valuation analyses and corporate finance engagements with middle market clients. Mr. Wissinger currently serves on the Boards of Directors of McKees Rocks Industrial Enterprises, Inc. and Engineered Plastics, Inc. Mr. Wissinger received his Bachelor of Business Administration degree from Roanoke College.

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