

“ a firm belief in the
entrepreneurial spirit ”

CLEARY GULL

MARKET MONITOR

FINANCING UPDATE



4TH QUARTER 2010

THE ECONOMY, LENDING, AND M&A MARKETS ALL IMPROVING

The Building Recovery

There are increasing signs of a sustainable recovery. During the third quarter of 2010, GDP in the U.S. grew at a compound annual rate of 2.0%, personal consumption increased 2.6%, industrial production soared 5.2%, and corporate profits increased 17.0%.

The employment market, which has been slow to recover, is also beginning to improve. Employment in the private sector has risen by more than 1.1 million since December 2009. However, it appears a higher rate of growth in the economy may be needed to restore full employment.

Perhaps even the housing market has found its “bottom,” although it seems there is no end to the mortgage mess.

Interesting Times

As 2010 comes to a close, we cautiously watch economic developments and political announcements in Washington and countries around the world. The decisions being made will affect exchange rates, trade balances, interest rates, and taxes for many years.

The continuing European debt crisis reminds us how interconnected our global markets are, as well as how varied the circumstances are of different world economies.

Meanwhile, the debate in the U.S. rages on over near-term tax rates and long-term deficit reduction. At least healthcare has been resolved – for now – or has it?

The soon-to-expire Bush era tax cuts, which were expected to be an impetus for transactions in 2010, are looking more likely to be extended for another two years.

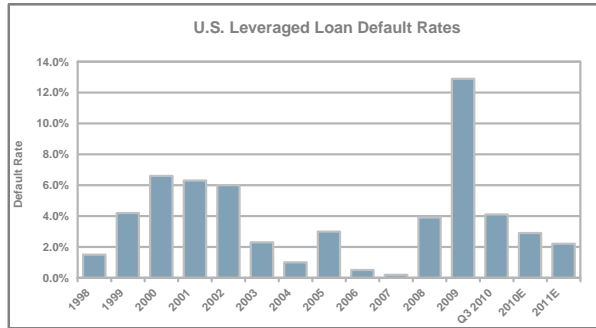
We have also noticed a decisive improvement in the financing markets during 2010 and, in particular, lending by regional banks in support of lower middle-market M&A financings.

KEY U.S. INTEREST RATES

| | 12/1/2010 | 12/31/2009 | 12/1/2008 |
|----------------|-----------|------------|-----------|
| 3-Month T Bill | 0.16% | 0.06% | 0.07% |
| 2-Year UST | 0.53% | 1.14% | 0.90% |
| 5-Year UST | 1.64% | 2.69% | 1.71% |
| 10-Year UST | 2.97% | 3.85% | 2.72% |
| 30-Year UST | 4.24% | 4.63% | 3.22% |
| EUR/USD | \$1.31 | \$1.43 | \$1.26 |
| 1-Month LIBOR | 0.27% | 0.23% | 1.90% |
| 6-Month LIBOR | 0.47% | 0.43% | 2.61% |
| Prime | 3.25% | 3.25% | 4.00% |

Source: Capital IQ, St. Louis Fed

DEFAULT RATES DECLINING



Source: Moody's Investors Service

Improving Senior Debt Market

Banks seem eager to grow their loan portfolios after the record declines in commercial bank loans in 2009. Much of this decline was due to loan pay-downs but, unfortunately, too much was the result of write-downs and write-offs. According to Standard & Poor's, bank loans increased in October, following 13 consecutive months of declines.

Many regional banks are aggressively pursuing lower middle-market lending, filling the void left by the retreat of finance companies, hedge funds, and larger banks which have largely exited the market.

Banks are typically quoting credits at LIBOR + 225 – 375 bps and non-bank lenders typically at 450 – 600 bps over LIBOR. Although credit spreads are higher than in 2008, the near record low interest rates make borrowing extremely affordable right now.

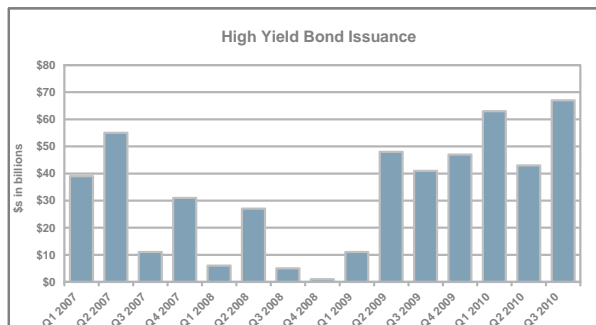
Low Default Rates and Quest for Yield Driving High Yield Demand

The general credit quality of corporate loans has improved dramatically as reflected in the large decrease in speculative debt defaults. According to Moody's Investors Service, the U.S. speculative default rate fell to 3.6% in October, down from 14.6% one year ago. Moody's is now forecasting that the default rate for U.S. speculative-grade issuers will fall to 2.9% by December 2010 and to 2.2% a year from now.

The decline in default rates is due in part to improved corporate performance, but also to a significant amount of refinancings and restructurings.

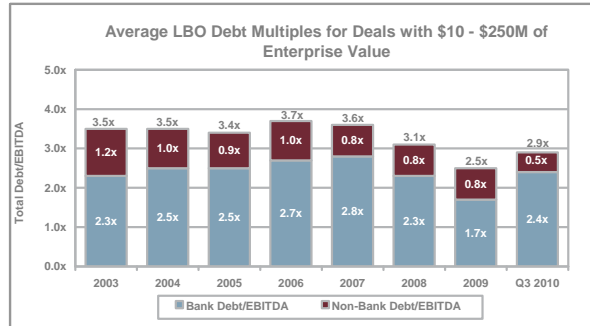
The expected low default rates, combined with investors thirst for yield, has driven significant flow into all types of fixed income, including bank deposits, high yield debt, and mezzanine loans.

HIGH YIELD BOND ISSUANCE INCREASING



Source: S&P LCD

DEBT MULTIPLES BEGINNING TO REBOUND



Source: GF Data Resources

M&A Lending on the Rise

Debt market support for lower middle-market M&A transactions (enterprise values less than \$250 million) has significantly improved this year. Average total debt/EBITDA multiples increased by 0.4x to 2.9x during the third quarter of 2010 compared to 2009 and average senior debt/EBITDA increased by 0.7x to 2.4x.

However, the debt market is even stronger than these ratios suggest. For a “sponsored” M&A transaction (a change of control financed in part with a significant equity investment), we are seeing senior debt for companies with less than \$10 million in EBITDA in the range of over 2.0x to nearly 3.0x EBITDA. For companies with EBITDA greater than \$10 million, senior debt can approach 3.5x.

Total debt remains at 3.5x to 3.75x for companies with less than \$10 million in EBITDA compared to 4.0x, or even 4.5x for companies with greater than \$10 million in EBITDA.

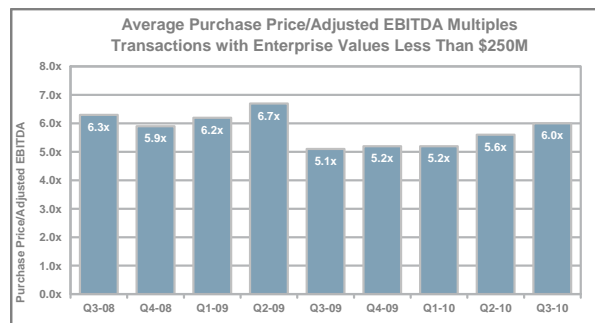
M&A Volume and Pricing Improving

The third quarter of 2010 was the fifth consecutive quarter of increased middle-market deal volume. Average EBITDA purchase price multiples reported for transactions with enterprise values less than \$250 million increased for the fourth consecutive quarter to 6.0x compared to 5.7x EBITDA for all of 2009.

Size also matters in valuation, with year-to-date purchase price multiples of 6.3x EBITDA for companies with enterprise values between \$100 and \$200 million, compared to 5.2x EBITDA for companies with enterprise values between \$10 and \$25 million.

According to GF Data Resources, during 2010 companies with above average financial characteristics achieved premium valuations, on average 11%, greater than on other transactions.

“REPORTED” PURCHASE PRICE MULTIPLES CONTINUE TO IMPROVE



Source: GF Data Resources

FIRM OVERVIEW

Cleary Gull Inc. is an employee-owned firm providing specialized financial services since 1987 to individuals, institutional investors, and middle-market companies through two operating divisions: Investment Banking and Investment Management Services. "A Firm Belief in the Entrepreneurial Spirit" is our core ideology and the foundation for all of our client engagements.

Cleary Gull's investment bankers help our clients throughout the U.S. achieve their financial and business goals with advice on exclusive sales, mergers, acquisitions, raising debt and equity in private capital markets and other transactions, working through complex financial, legal, tax, accounting and other technical issues, and delivering superior results.

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CONTACT

The Cleary Gull Investment Banking team has completed more than 120 transactions since 1995, representing over \$6 billion in transaction value. We are dedicated to providing unbiased, conflict-free advice to middle-market companies.

Contact us for more information on Cleary Gull and our Investment Banking services.

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