

“ a firm belief in the  
entrepreneurial spirit ”

CLEARY GULL

# MARKET MONITOR

FINANCING UPDATE



4TH QUARTER 2009

## THE RECOVERY: IS IT SUSTAINABLE?

### A Tortoise or Hare?

Third quarter GDP growth of 3.5% technically ends the recession. However, mixed signals from the economy and the stock market have led many economists to debate whether the recovery is sustainable.

An unprecedented amount of fiscal stimulus has prevented another Great Depression. Residential real estate values, the root cause of the recession, have begun to turn. The Standard & Poor's Case-Shiller 20-City Home Price index improved for the fourth consecutive month; and with decreased inventories and increased affordability, we have built a solid foundation for a housing recovery.

Corporate earnings are rebounding, albeit still more from expense reduction than sales growth, and the financial crisis has abated.

However, with unemployment near the highest level since 1982, state and local budgets are more stressed than ever and the strength of the economy after the stimulus abates is unclear.

### Interest Rates and Taxes Are Low ... For Now

The Fed announced that interest rates will remain low, indicating cheap money will continue to be available.

Nevertheless, the dollar continues to decline and commodity prices are rallying. The question appears to be when, not if, interest rates will rise.

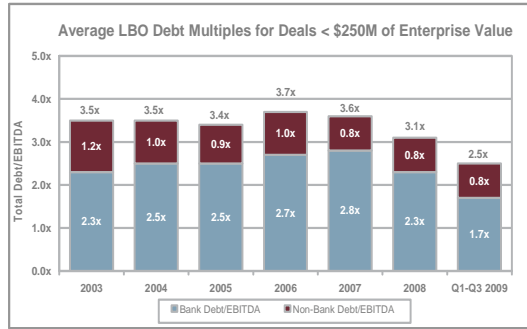
Taxes are also expected to rise. This change could spur merger and acquisition activity in 2010 as the timing and increases become more clear to business owners.

### KEY U.S. INTEREST RATES

	11/30/2009	12/31/2008	11/28/2008
3-Month T Bill	0.06%	0.11%	0.07%
2-Year UST	0.67%	0.76%	0.92%
5-Year UST	2.01%	1.55%	1.72%
10-Year UST	3.20%	2.25%	2.72%
30-Year UST	4.19%	2.69%	3.24%
1-Month LIBOR	0.24%	0.44%	1.91%
6-Month LIBOR	0.49%	1.75%	2.61%
Prime	3.25%	3.25%	4.00%

Source: Capital IQ, St. Louis Fed

## DEBT MULTIPLES



Source: GF Data Resources

### Debt Multiples Decline Further

Average total debt/EBITDA multiples for small LBOs (borrowers with less than \$250 million enterprise value) declined 0.6x to 2.5x during the first three quarters of 2009 compared to 2008. Senior debt/EBITDA declined 0.6x from 2.3x to 1.7x. Subordinated debt remained stable at 0.8x EBITDA.

However, during the first three quarters of 2009, smaller transactions were less leveraged. Average total debt/EBITDA for transactions with less than \$50 million enterprise value was 2.3x compared to 2.9x for transactions with \$50 to \$250 million enterprise values.

Despite the rebound in the broader credit markets during the year, the quarterly trend in leverage ratios continues to decline, with Q3 2009 total debt averaging only 2.2x EBITDA.

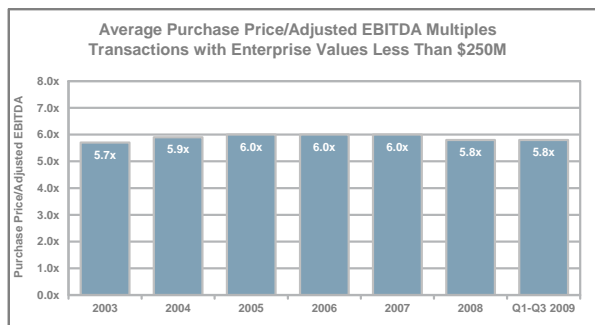
### Seller and Buyer Expectations More in Sync?

During the first three quarters of 2009, average EBITDA purchase price multiples reported for leveraged buyout transactions with enterprise values less than \$250 million declined by 0.1x to 5.8x EBITDA compared to 5.9x EBITDA in 2008.

However, purchase price multiples in Q3 2009 declined dramatically to 5.1x EBITDA. We believe lower multiples are due to increased M&A activity with underperforming businesses in Q3 compared to earlier in the year when only businesses with very strong financial characteristics were able to consummate transactions.

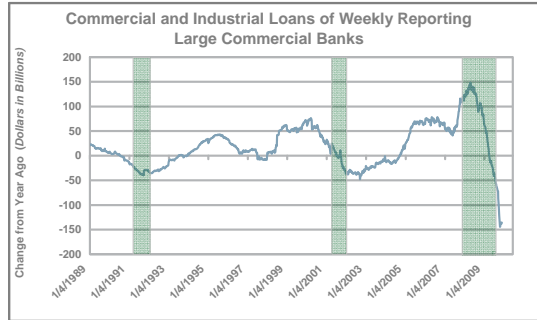
Despite these lower multiples, the data also suggests that seller and buyer expectations are more in sync than a year ago.

## PURCHASE PRICES



Source: GF Data Resources

## WHEN WILL THE BANKS EASE CREDIT?



Source: St. Louis Fed

### Banks Still Cautious

Bank balance sheets are still contracting. During the first nine months of 2009, large commercial banks had \$135.8 billion in outstanding loans, down from a high of \$148.5 billion in April 2008.

Despite more than \$700 billion in TARP money and \$787 billion of spending as a result of the American Recovery and Reinvestment Act of 2009, outstanding lending continues to decline. The inflows of capital (governmental and equity offerings) continue to be used to deleverage and recent equity raises have been used to fund loan losses and increase capital ratios, not corporate growth.

### Broader Debt Markets Improving

The bid on high yield debt has increased from a low of below 60 to almost 90 in November.

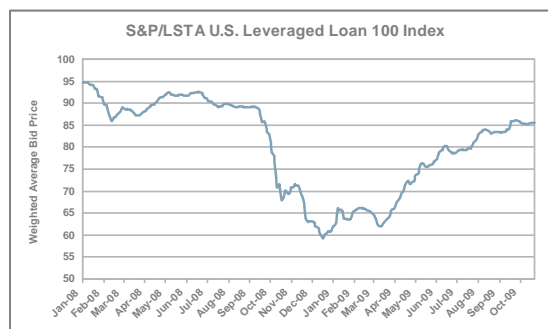
Given the depressed prices of existing debt, during the last nine months debt capital has been invested in higher yielding distressed or discounted debt rather than new loans.

Now, with debt trading near 90, lenders and other debt investors are more willing to lend directly to corporations, not only focused on buying distressed debt.

In fact, banks are showing new interest in lending and we expect the market to slowly improve in Q4 and into 2010.

Although leverage has yet to increase, credit spreads have declined by more than 100 bps for most new borrowers.

## LEVERAGE LOAN PRICING CONTINUES TO IMPROVE



Source: Bloomberg

## 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 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 approximately \$6 billion in transaction value. We are dedicated to providing unbiased, conflict-free advice to middle market companies.

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