

“ a firm belief in the entrepreneurial spirit ”

CLEARY GULL

# MARKET MONITOR

M&A AND FINANCING UPDATE



3<sup>rd</sup> QUARTER 2013

## TRANSACTION VOLUME EXPECTED TO INCREASE

Transaction volume during the first six months of 2013 was soft. The number of middle-market transactions (enterprise values less than \$500 million) declined 33% during the first half of 2013 compared to the year-earlier period, according to Robert W. Baird & Co.

The slow first half is attributed to the tax driven pull forward of transactions into 2012 and slow economic growth in early 2013.

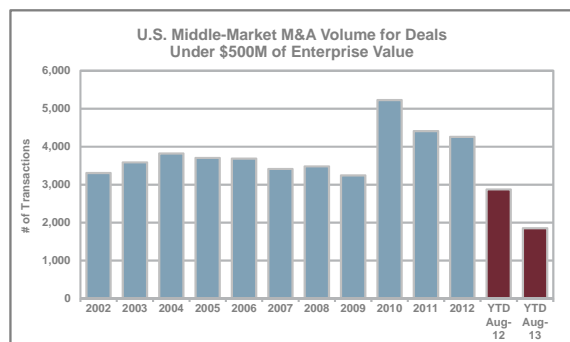
Our own experience and reports from the market indicate deal activity picked up dramatically at the end of the second quarter. Given transaction lag times, and the strong fourth quarter last year, it may be early 2014 before this increase in transaction volume appears in the published statistics.

With non-financial companies in the S&P 500 holding over \$1.2 trillion of cash according to Capital IQ, and organic growth difficult to find, strategic buyers are well positioned to benefit from M&A activity. We have seen a marked increase in strategic buyer activity in recent transactions. Our international network partners, and our European partners in particular, indicate an increasing interest in investing in the U.S.

Private equity funds are also holding a significant amount of uninvested capital. According to Pitchbook, private equity funds have \$328 billion of uninvested capital, which is less than the last few years but still a tremendous amount of capital ready to be invested.

The increase in volume, tremendous demand for transactions, and strong financing markets (see page 2), make this an excellent market for sellers.

## DEAL VOLUME REMAINS SOFT



Source: Robert W. Baird & Co.

## KEY INTEREST RATES

	9/30/2013	12/31/2012	12/31/2011
1-Month T Bill	0.03%	0.02%	0.01%
2-Year UST	0.33%	0.25%	0.25%
5-Year UST	1.39%	0.72%	0.83%
10-Year UST	2.64%	1.78%	1.89%
30-Year UST	3.69%	2.95%	2.89%
EUR/USD	\$1.35	\$1.32	\$1.30
1-Month LIBOR	0.18%	0.21%	0.30%
Federal Funds	0.75%	0.75%	0.75%
Prime	3.25%	3.25%	3.25%

Source: Capital IQ

## ATTRACTIVE FINANCING MARKETS

### Senior Debt Multiples Expanding

Senior debt market support for lower middle-market M&A transactions (enterprise values less than \$250 million) increased modestly during the first half of 2013 compared to 2012. According to GF Data, average senior debt/EBITDA multiples increased to 2.6x during the first half, compared to 2.4x during 2012. Low interest rates, improved bank performance, and competition for new assets is driving continued improvement in pricing and terms for senior debt.

With continued low interest rates, a stable to improving economic outlook, and a highly competitive banking market, it is an attractive time for companies to borrow.

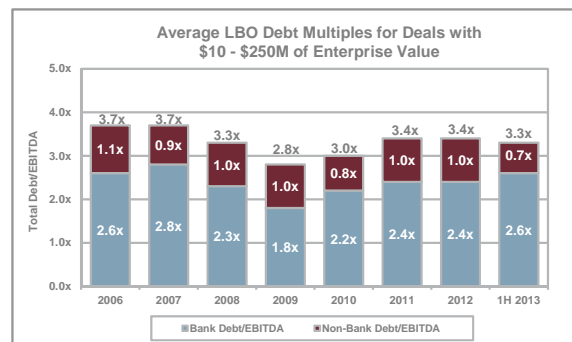
### Mezzanine Debt Squeezed

Although mezzanine debt can be a useful tool to facilitate a transaction, the use of mezzanine debt declined slightly during the first half of 2013.

According to GF Data, mezzanine debt for lower middle-market M&A transactions represented 0.7x EBITDA during the first half of 2013 compared to the more typical 1.0x it constituted in 2011 and 2012 while total debt/EBITDA multiples remained relatively stable.

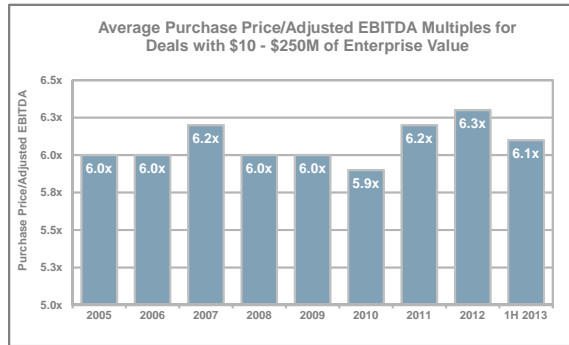
The decline in the use of mezzanine financing was predominately due to increased senior debt and not a reduction in mezzanine lenders' interest in supporting transactions.

## LEVERAGE MULTIPLES REMAIN STABLE



Source: GF Data Resources

## PURCHASE PRICE REMAIN STRONG



Source: GF Data Resources

## VALUATIONS REMAIN STRONG

### Purchase Price Remain Stable

Average middle-market purchase price multiples for LBOs remained stable at 6.1x EBITDA in the first half of 2013, slightly below the 6.3x multiple realized for the full year of 2012, according to GF Data.

Larger transactions continue to realize significantly higher multiples. Average enterprise value/EBITDA multiples reported for LBO transactions with enterprise values between \$50 million and \$100 million were 6.5x EBITDA during the first half of 2013 compared to 5.7x EBITDA for transactions with enterprise values between \$10 to \$50 million in EBITDA.

Even with low transaction volume, buyers are placing a significant premium on size, quality and management.

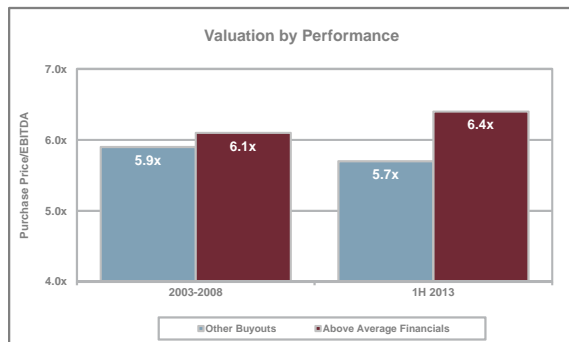
### Premium for Quality Companies

According to GF Data analysis, LBO purchase price multiples in 2012 were higher for companies with above average financial characteristics and continuing management. Companies with these characteristics sold for 6.4x EBITDA compared to 5.7x EBITDA for other transactions.

For the purposes of these calculations, “above average financial characteristics” is defined as companies having either latest twelve months (LTM) EBITDA margins and LTM revenue growth above 10%, or both metrics above 8% and combined metrics greater than 20%.

During 2003–2008, the gap was only 0.2x. As in many areas of the investment world, the emphasis on quality has increased during the last several years.

## COMPANIES WITH STRONGER FINANCIALS REALIZE HIGHER VALUATIONS



Source: GF Data

## 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 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.

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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.

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

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