ECONOMIC LEADERSHIP FORUM
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New Jersey's Most Important Economic Conference

Middle Market M&A and Capital Markets Update

GRIFFIN FINANCIAL GROUP LLC
A STEVENS & LEE/GRIFFIN COMPANY

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Today's Speaker

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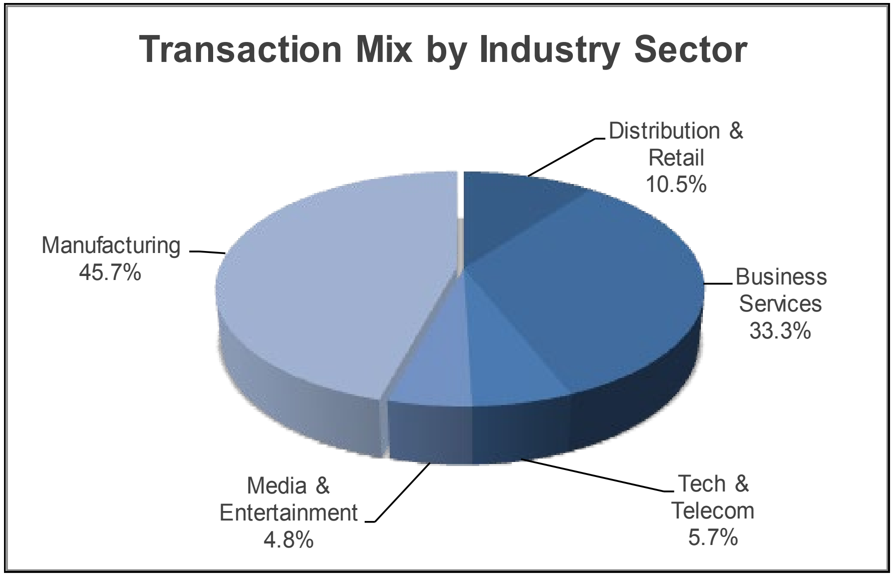
- Manages the Commercial, Industrial and Services Group for Griffin Financial Group, a leading investment bank in the Mid-Atlantic region, and part of the Stevens & Lee/Griffin multidisciplinary platform of companies
- More than 25 years of experience providing merger and acquisition advisory services, private placements of debt and equity capital, and management buyout advisory services for middle market companies in a wide range of industries
- Experience includes sourcing, initiating or managing numerous investment banking transactions for middle market business and government services, consumer and industrial manufacturing, distribution, and technology companies
- Experience includes Principal of Horizon Partners, Ltd (private equity investment firm), Director at Berwind Financial, L.P., and Investment Banking Officer at Crestar Securities Corp.
- Past President of the Association for Corporate Growth (ACG), Philadelphia Chapter. Holds Series 79, 7 and 63 licenses from FINRA

Middle Market Companies

Griffin's Commercial, Industrial & Services Practice ("CIS")

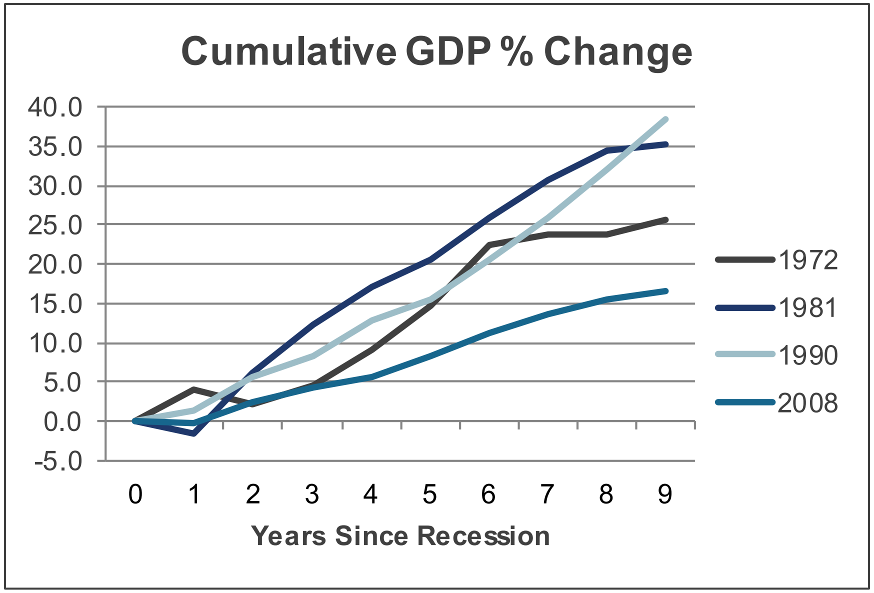
- Middle market distribution, manufacturing, retail, and services companies
- Primarily privately owned businesses and smaller public companies
  - Family held
  - Partnerships
  - CEO-owned
  - Private equity owned
- Revenue between $10-$500 million
  - EBITDA between $2-$50 million

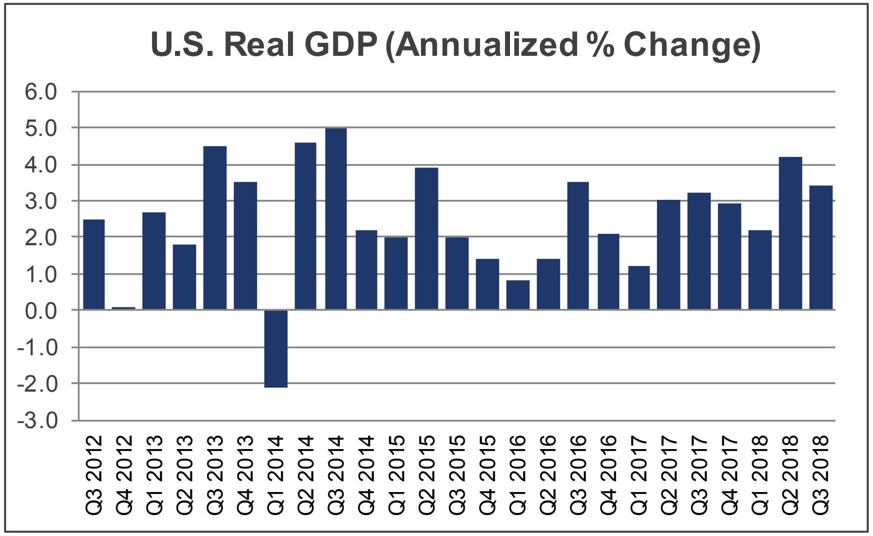


Macroeconomic Overview

Gross Domestic Product ("GDP") Breaking Slow-Growth Trend

- GDP growth since the Great Recession in 2008 has lagged far behind prior recessions
- GDP growth near or above 3.0% in four of last five quarters
- Q3 2018 GDP Breakdown:
  - + Personal Consumption Expenditures (PCE)
  - + Private Inventory Investment
  - + State & Local Gov't Spending
  - + Federal Gov't Spending
  - + Nonresidential Fixed Investment
  - – Exports
  - – Residential Fixed Investment
  - – Imports
- Political change had some effect on GDP growth in 2017 and 2018 and optimism for 2019 exists
  - Historically, tax cuts led to reduction in personal debt in the initial year of the cut, not to increased consumer spending, but in 2018 PCE is rising
  - However, subsequent years did experience consumer spending increases
- Stock Market signaling fear of recession



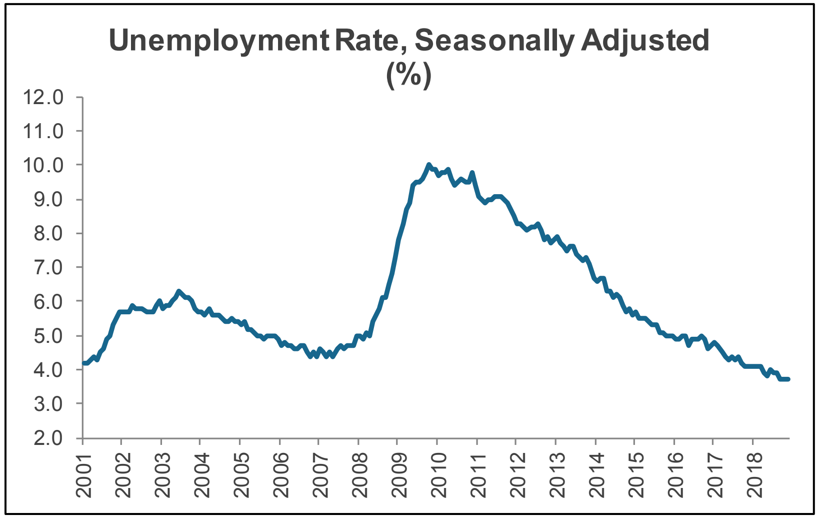


Source: Bureau of Economic Analysis (January 2019)

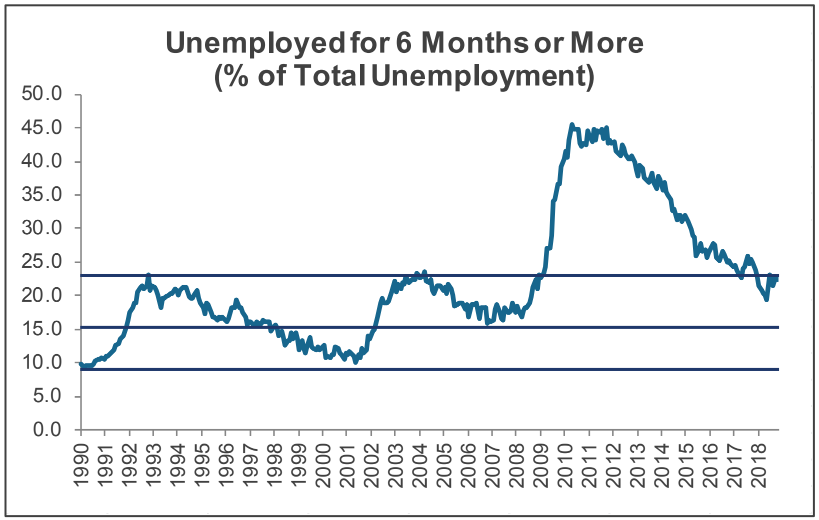
Macroeconomic Overview

Unemployment and Underemployment Have Improved Dramatically

- The national unemployment rate has decreased from a high of 9.8% in 2010 to 3.9% in December 2018
- In addition, the more comprehensive U6 unemployment rate (which includes those who are underemployed or who have given up on job searches) was 7.6% in December 2018, down from a 2009 high of 17.1%
- Long-term unemployment continues to be an issue as the percentage of workers unemployed for 6 months or longer remains higher than the rates seen in recent recessions but is coming down
- The Labor Force Participation Rate of 63.1% as of December 2018 is near the historical average of 63.0% since 1950
- Employers have added an average of just over 200,000 jobs per month during 2018, a pace that has held relatively steady for the past two years



Source: Bureau of Labor Statistics



Source: Bureau of Labor Statistics

M&A and Capital Markets for Middle Market Companies

With a Solid Economic Backdrop, M&A and Capital Raising Options for Middle Market Companies are Strong

- Strength of current M&A and capital markets is primarily driven by four factors:
  - Low interest rates and the availability of debt for acquisitions
    - Despite the recent rate increases, overall rates remain historically low
  - High corporate profits and corporate cash
  - Excess private equity to be deployed
  - Challenging internal growth prospects for most companies and industries make growth through acquisitions an attractive strategy

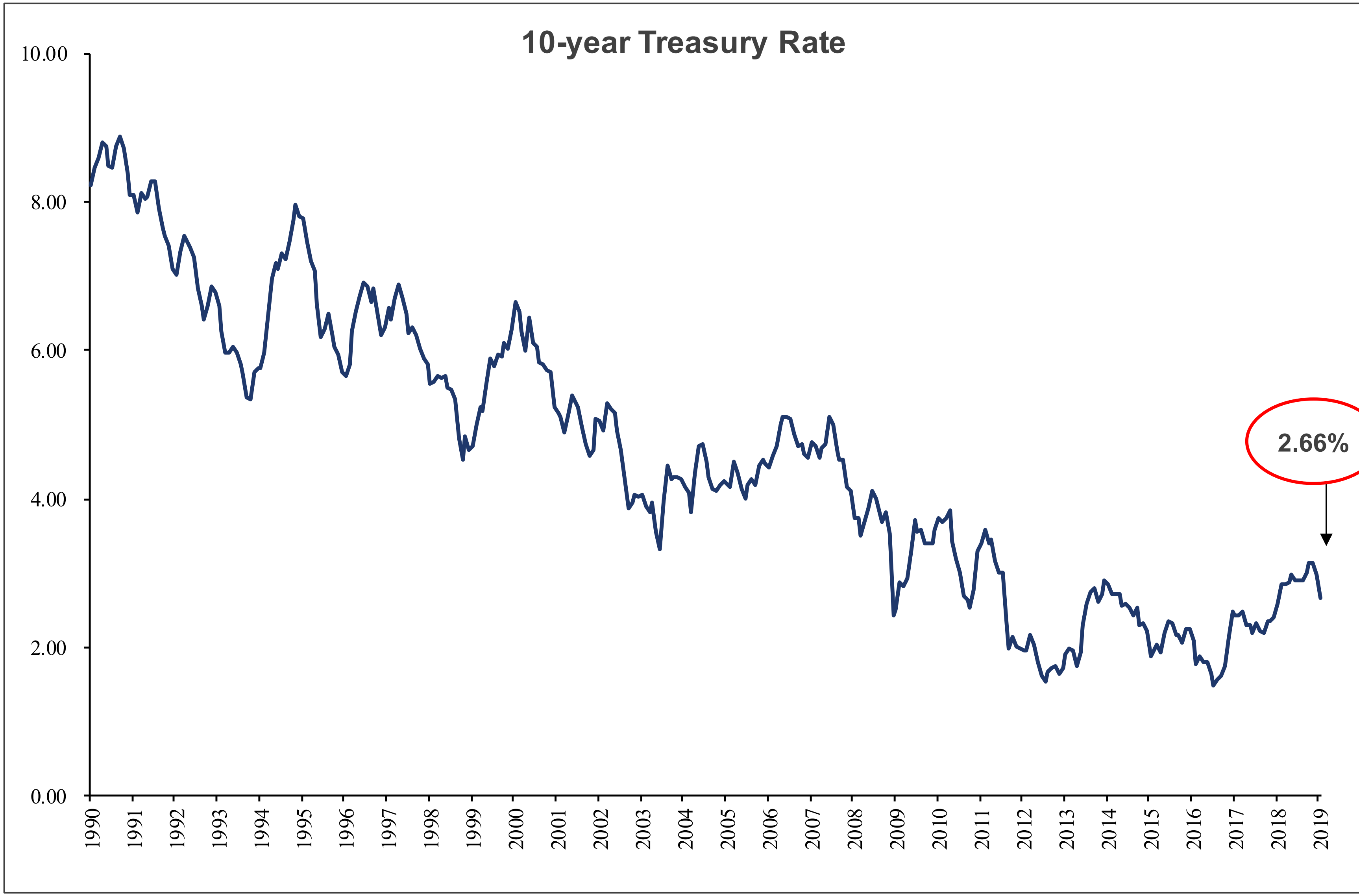
- In its US PE Middle Market report, PitchBook reports that 2018 US PE MM deal activity is on pace for a record year(1)
  - "The outlook remains favorable for US-based companies. Business and consumer confidence remains high. Job creation and unemployment trends look good, with some signs of wage increases. GDP growth has accelerated to near the 4% level of late. It may slow a bit in 2019-2020, but most economists see recession odds as relatively low," says Michael Chirillo, senior managing director with Antares Capital, a private debt capital firm

- Intralinks Deal Flow Predictor forecasts a 6% YOY increase in global M&A deals to be announced in 1Q 2019. The increase will be attributable to the activity within Industrials, Real-Estate, and Consumer & Retail sectors(2)

[1] US PE Middle Market report 3Q 2018, PitchBook Data, October 2018
[2] "Forecast of global M&A activity", Intralinks Deal Flow Predictor, November 2018

Interest Rates are at Historic Lows

Unprecedented Monetary Stimulus = Historically Low Interest Rates Despite 2018 Increase



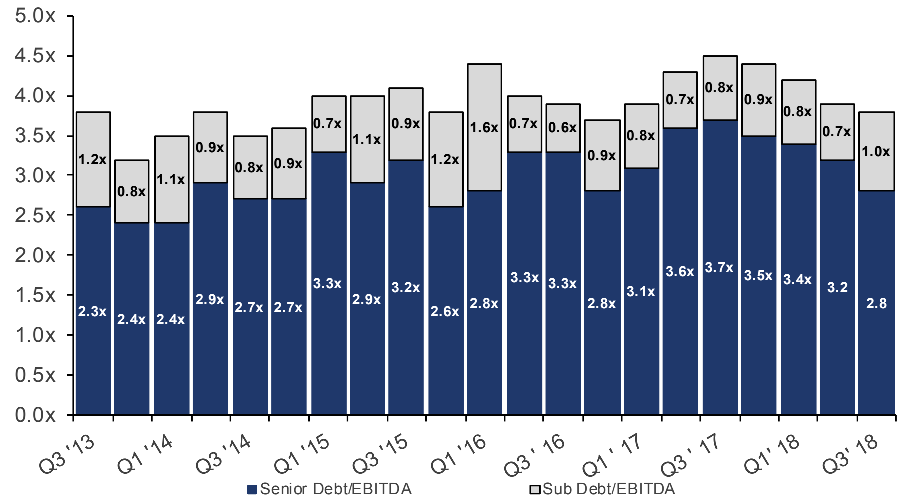
Source: US Treasury 1/3/19

Debt for Acquisitions is Abundant

Institutional Credit Markets are Broad, Deep, and Aggressive

- Senior debt/EBITDA multiples for $10 plus million EBITDA companies of 4.0-5.0x
  - Banks at 3.0-4.0x
- Senior debt/EBITDA multiples for less than $10 million EBITDA companies of 3.0-4.0x (in line with historical multiples)
  - Banks at 3.0-3.5x, some push to 4.0x
- Very attractive terms and pricing for “A” or “B” companies (e.g. LIBOR + 150-300bps from banks)
  - Non-bank lenders at LIBOR+ 700-900bps
- Subordinated debt can add another 0.5-1.0x EBITDA to bank debt with pricing between 10.6%-11.6%, paid-in-kind (PIK) rates ranging between 1.9%-2.6% and Warrant-based-returns (WBR)/ Fees of 1.4%- 2.1%, for all-in-costs of 13.3%-15.2%
  - The Bank/Sub Debt combination competes with the Unitranche option on a blended cost basis

Middle Market LBO Debt Multiples
Enterprise Value Between $10-$250 Million



All-In Sub Debt Pricing - Q1-Q3 2018					
TEV	**Coupon**	**PIK**	**WBR/ FEES**	**Total**	**N**
10-25	11.6%	2.3%	2.1%	15.2%	20
25-50	11.1%	2.2%	1.6%	13.9%	25
50-100	10.8%	2.6%	1.4%	13.3%	18
100-250	10.6%	1.9%	1.8%	13.9%	10
Total	**11.1%**	**2.3%**	**1.7%**	**14.1%**	**73**

Source: GF Data

Bank Leveraged Lending Restricted

Leveraged lending guidelines have been implemented by the FDIC that penalize banks for Highly Leveraged Transactions (“HLT”)

- FDIC is concerned with Bank participation in HLT market
- HLT guidance applies to loans with the following characteristics:
  - $5 million or higher
  - Proceeds used for buyouts, acquisitions, or capital distributions
  - Total debt/EBITDA or senior debt/EBITDA exceeds 4.0x or 3.0x, respectively
- Banks tend to have a “bucket” amount of HLT loans they are willing to make each year
  - HLT loans penalize banks with higher capital requirements and fees
- Non-Bank Lenders offering Unitranche products are filling the void, BUT at a higher cost

STEVENS&LEE GRIFFIN

Case Study - Capital Raise Advisory

CORE STATES GROUP

Has been provided senior debt capital by

Citizens Bank®

For the repayment of subordinated debt and to provide acquisition and working capital financing

Griffin Financial Group served as exclusive financial advisor and placement agent to ***Core States Group***

November 2018

Core States Group

Transaction Type: Capital Raise Advisory
Industry: Architecture/Engineering Services

Key Transaction Points

- Core States, based in Ambler PA, provides engineering, architecture/design, program management, signage, and construction services for the small-box multi-site retail petroleum, convenience store, restaurant, retail, and banking sectors
- Griffin was engaged by Core States as its exclusive investment banker to assist the Company in raising new senior debt facilities to
    - (i) provide "dry-powder" acquisition financing, and
    - (ii) refinance the Company's existing secured and unsecured debt
- Griffin procured multiple financing offers, and the Company ultimately selected Citizens Bank as its senior lender for the transaction

Case Study - Capital Raise Advisory

e&e
IT Consulting Services, Inc.

a portfolio company of ***IMB Development Corporation****,*
has been provided senior and junior debt capital by

M&T Bank

GRAYCLIFF PARTNERS

Griffin Financial Group served as exclusive financial advisor and placement agent to ***e&e IT Consulting Services, Inc.*** *and* ***e&e Technical Consultants, LLC***

September 2018

e&e IT Consulting Services, Inc.

Transaction Type: Capital Raise Advisory
Industry: Technology Services

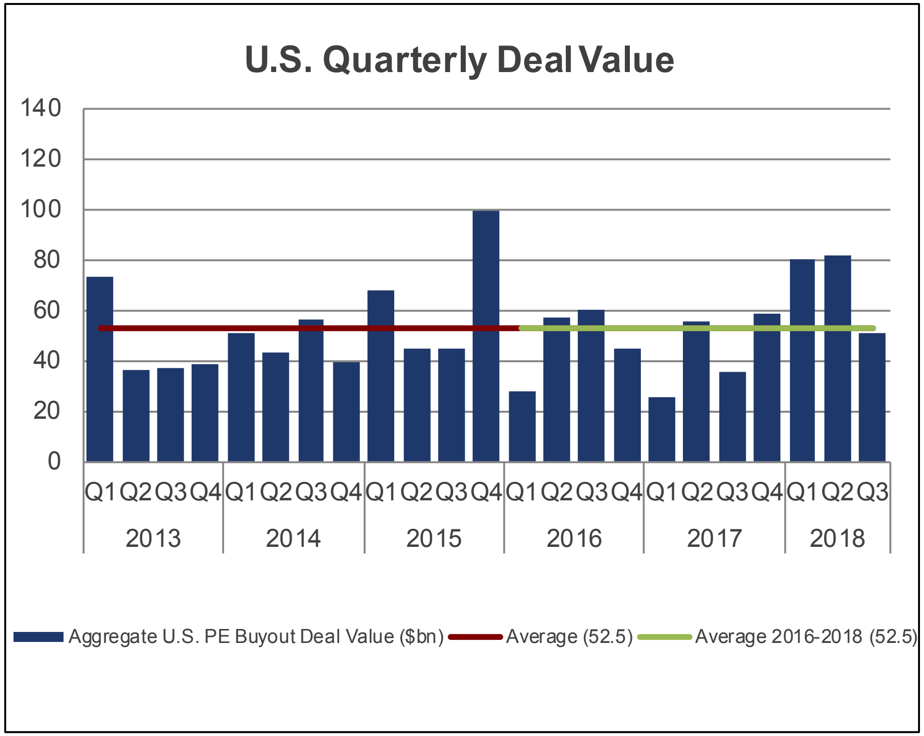
Key Transaction Points

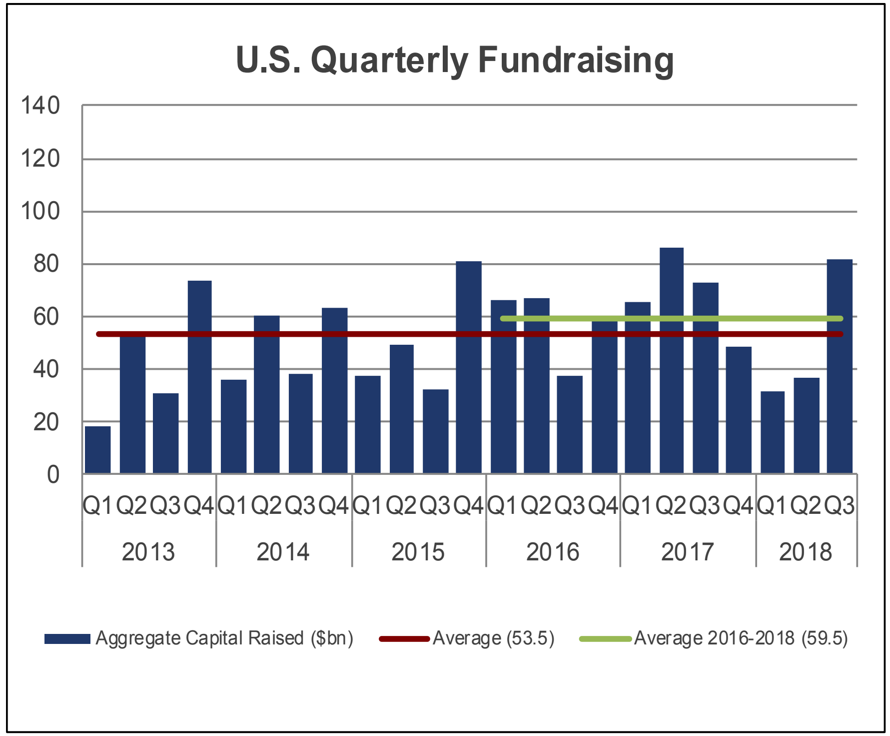
- e&e IT Consulting Services, Inc. based in Harrisburg, PA, provides IT consulting and staffing services to commercial, federal and state government clients
- Griffin was engaged by e&e IT Consulting Services, Inc. to assist the Company in raising new senior and junior debt capital to
  - (i) refinance the Company's existing secured and unsecured debt
  - (ii) fund a dividend to shareholders, and
  - (iii) provide e&e with greater financial resources to fund future strategic initiatives, such as potential acquisitions
- Griffin managed a competitive capital raising process to privately place the senior and junior debt
- Griffin procured multiple financing offers, and the Company ultimately selected M&T Bank Bank and Graycliff Partners as its senior and junior lenders for the transaction

Private Equity Funds – Fundraising vs. Investment

$51.2bn Aggregate U.S. Private Equity Deal Value in Q3 2018

$81.6bn U.S. PE Funds raised in Q3 2018

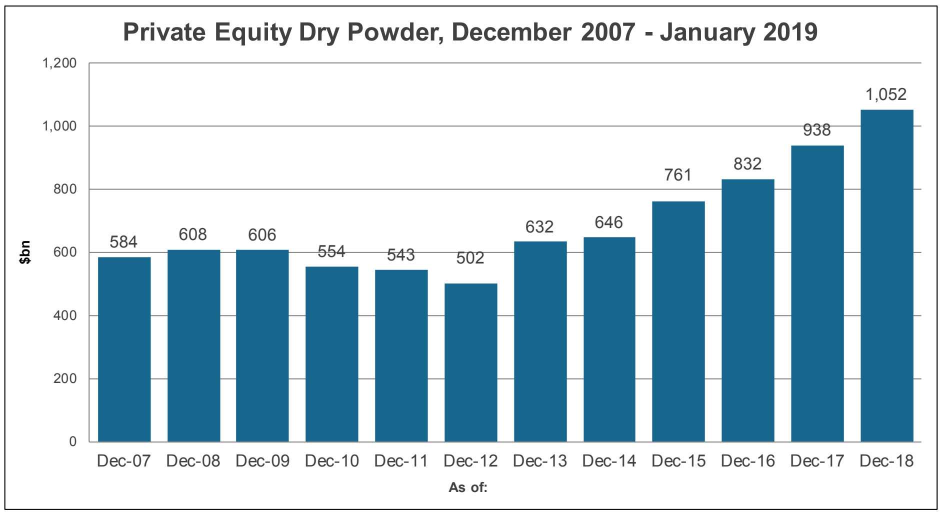




Record Private Equity Dry Powder

Private Equity Markets Overview

- Private equity markets remain very active with a greater number of firms and higher amounts of capital chasing after a shrinking number of attractive acquisitions
  - Total dry powder for private equity firms continued to climb in 2018, rising from $838 billion at the end of 2016 to reach a record exceeding ***$1.05 trillion*** as of the end of December 2018
  - Aggregate buyout deal value decreased 5% in 2018 after achieving a record high in 2017 of $637 billion
- Private equity markets are currently saturated with a record number of funds seeking capital and steadily increasing assets under management
- The closing of multiple mega-funds in 2018 caused U.S. fundraising activity to dip below the post-recession peak seen in 2017; PitchBook expects an uptick in future fundraising efforts with the opening of new funds

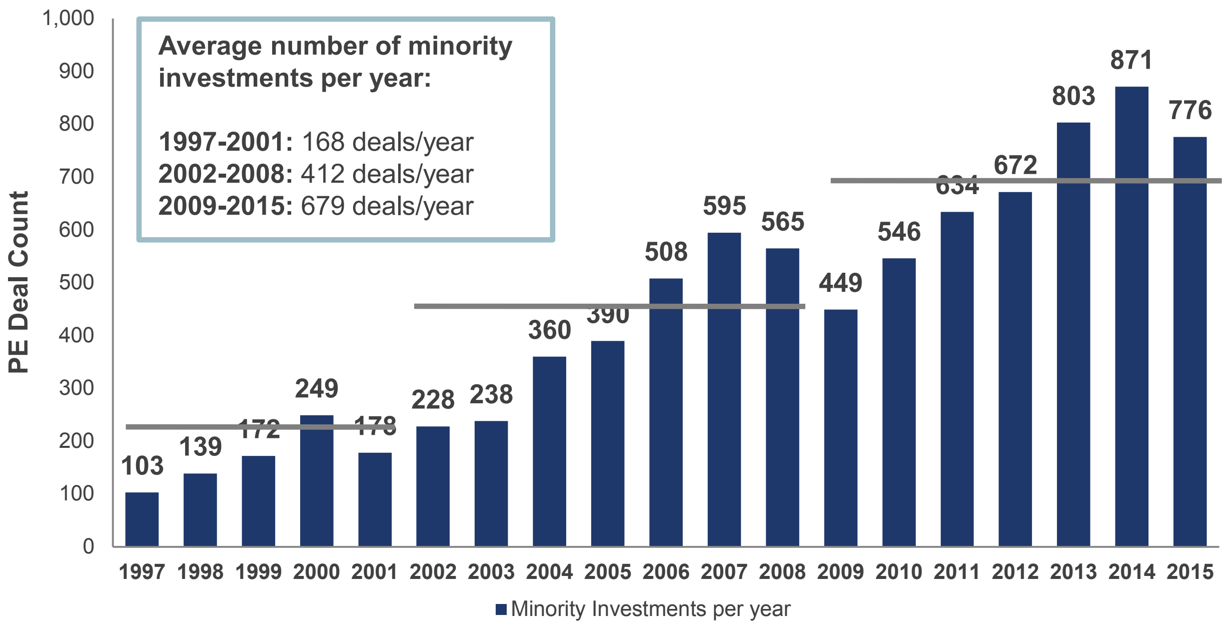


Sources:
Preqin, January 2019
“US PE Breakdown”, PitchBook Data, October 2018

Equity Markets

Minority Equity Overview

- Minority investments, which have been a common feature among smaller growth-equity deals, have become increasingly prevalent in larger PE transactions
  - Buyout funds are holding record levels of dry powder, driving them toward minority transactions in order to deploy capital
- Based on recent research by Boston Consulting Group, motivations for over 90% of minority transactions included access to capital either for growth or restructuring
  - Research also suggests that companies may opt for minority equity as an alternative to a buyout to avoid adverse publicity and customer fallout

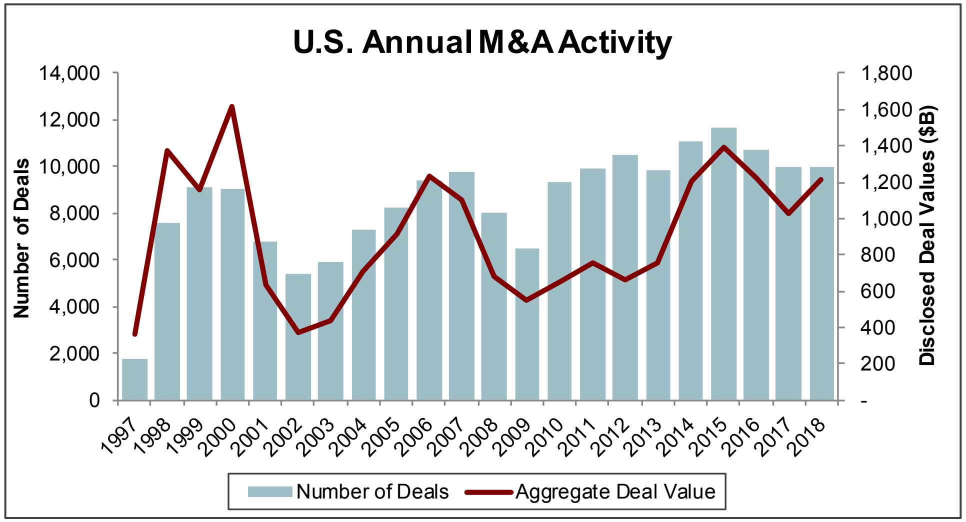


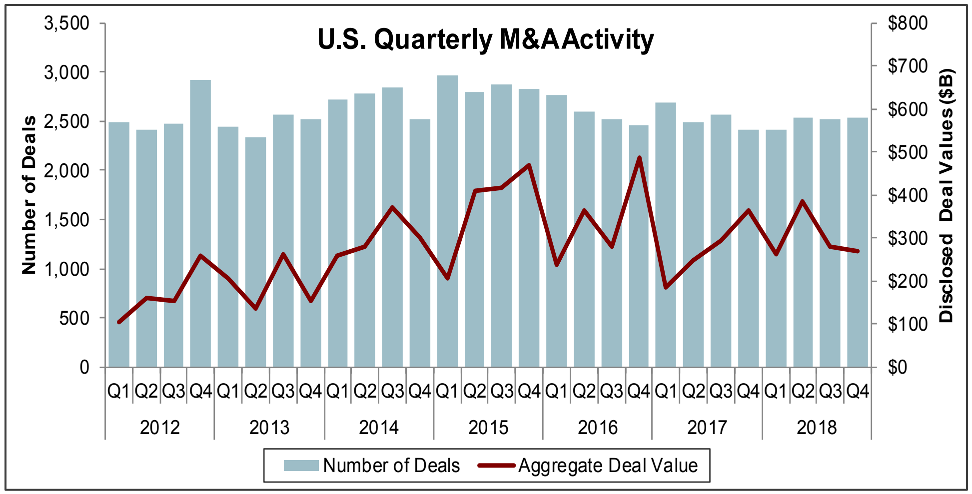
Source: Pitchbook

High Levels of M&A Activity

Record Debt Availability, Low Interest Rates, Corporate Profits and Cash, and Private Equity Overhang are Driving M&A Activity

- Significant climb in the number of deals from the depths of the recession in 2009 to a record level in 2015
- 2015 was a record year for M&A, both in terms of number of deals and deal value, and both 2016 and 2017 saw small decreases in deal activity
  - Total M&A activity has modestly increased in Q4, valuation multiples remain at record-highs and premiums for high quality businesses continue to drive median deal size higher
  - According to GF Data®, M&A appetite in the middle market remains strong despite recent trade policy concerns
- The number of announced or closed deals with deal values greater than $10 billion decreased from 39 in 2015 to 16 in 2017, but jumped to 19 during 2018

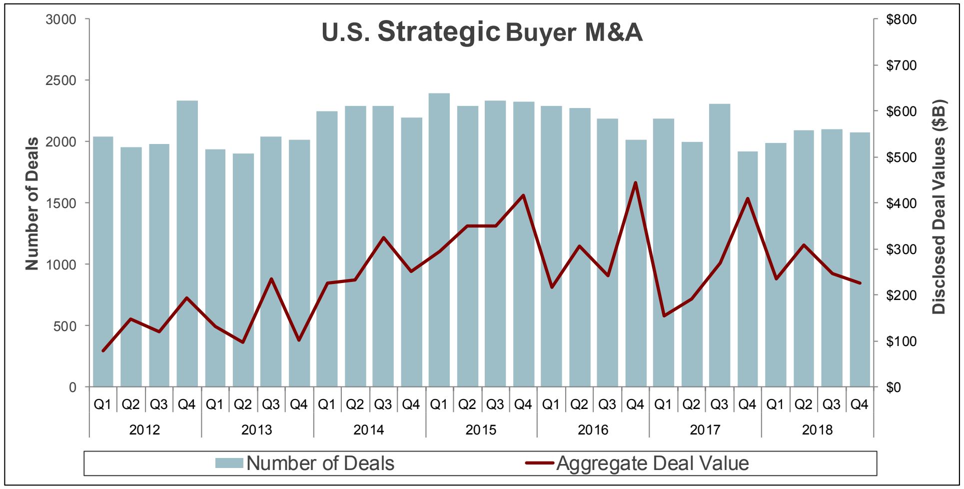


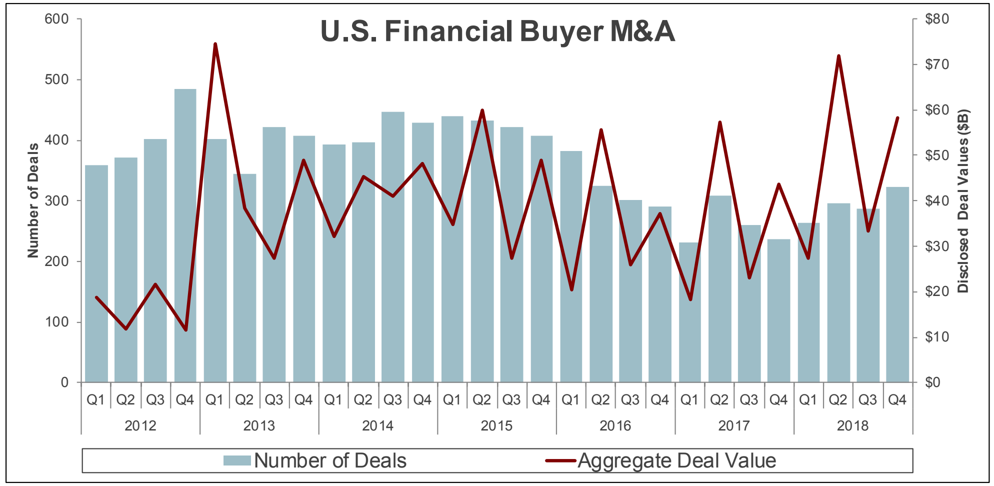


Sources:
S&P Capital IQ, January 2019
"M&A Report", GF Data®, November 2018

M&A Activity – Strategic vs. Financial Buyers

Strategic Buyers Remain More Active Than Financial Buyers





- Strategic buyers continue to be very active in pursuing M&A targets; buyers find value in growth and expense synergies, deploying cash on the balance sheet, and leveraging debt over combined companies
- Financial buyer transactions have slowed since the 2015 peak due to higher-than-expected valuations, a lack of worthwhile targets, and overheated competition
  - Financial buyer exits expected to continue at a decent clip through 2019

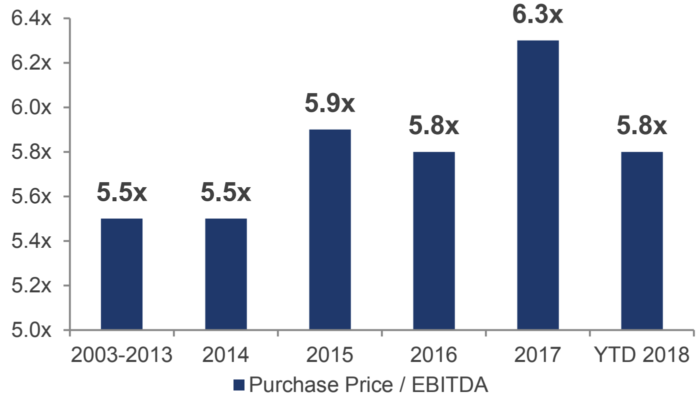
Source: S&P Capital IQ, January 2019

Includes Announced and Closed transactions in the U.S. (excluding asset/product purchases, government organizations, and charitable organizations and foundations)
Excludes transactions with unknown buyer type

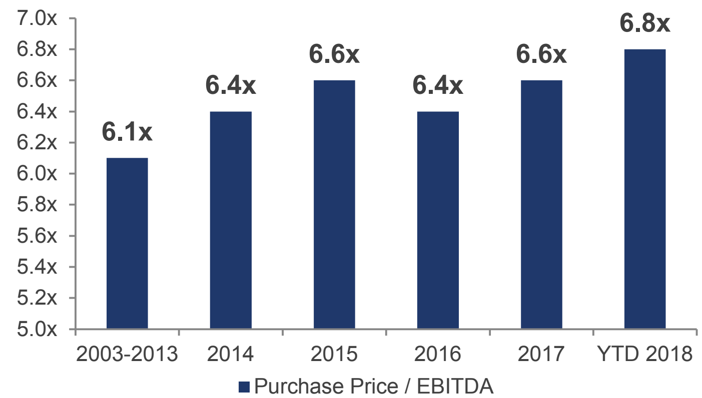
Private Equity M&A Activity – Historical Valuations

- Valuation multiples are heavily influenced by the size of a transaction, the industry, and the revenue model
- Valuations in all sectors of the middle market are at or near multi-year highs

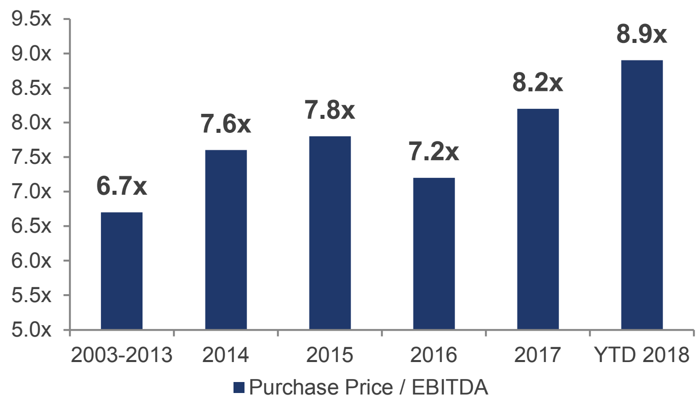
Purchase Price $10mm - $25mm



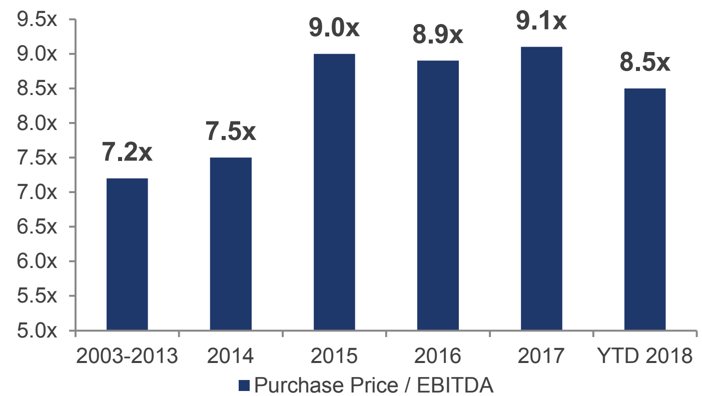
Purchase Price $25mm - $50mm



Purchase Price $50mm - $100mm



Purchase Price $100mm - $250mm



Source: GF Data November 2018 M&A Report

Case Study – Sell-Side Advisory

IBS Direct, Inc.

Transaction Type: M&A – Sell-Side Advisory
Industry: Printing & Manufacturing

Key Transaction Points

- IBS Direct, Inc. ("IBS"), headquartered in King of Prussia, PA, has been providing high-quality printing solutions for over 40 years
- IBS was managed by George Schnyder until 2011, when he decided to hire a new CEO and CFO as the initial phase of a long-term succession plan. After new management successfully grew IBS, George wished to complete the succession plan by selling the company and having a new owner continue its growth. Although IBS had grown substantially, the post-recession printing industry had performed poorly, leaving a lack of potential strategic buyers
- IBS engaged Griffin to manage a broad competitive sale process to supplement the lack of potential strategic buyers. Griffin approached a wide range of financial buyers, including private equity firms and family offices, in addition to strategic buyers. The process produced multiple offers, and IBS ultimately selected Logan Marketing Group ("LMG") as purchaser
- Griffin was also engaged by LMG to raise the debt capital required to support the IBS acquisition via a competitive capital raising process. LMG ultimately selected Bank of America as its lending partner, which provided both acquisition and working capital financing

Case Study – Sell-Side Advisory

KDH Defense Systems, Inc.

Transaction Type: M&A – Sell-Side Advisory
Industry: Defense Manufacturing

Key Transaction Points

- KDH Defense Systems, inc. is a manufacturer of protective apparel for the U.S. military and other governmental agencies, and is based in the Southeastern United States
- After operating at lower capacity for several years, the Company was recently awarded multiple major contracts with governmental agencies to be delivered over the next several years. As production has ramped up, the Company decided to hire Griffin to assist in soliciting offers for the purchase of the business to maximize realizable value for the selling shareholders
- Griffin managed a competitive sale process with companies within KDH's industry, and select private equity firms, which produced multiple purchase offers
- KDH selected Armor Express, a strategic portfolio company owned by a Private Equity firm

Takeaways

- **Current M&A activity is strong:** Economic growth is stronger
- Post-recession deal activity and valuations for middle-market businesses reached record levels in 2015-2017
  - Private equity deal activity is off in 2018 due to higher-than-expected valuations, a lack of worthwhile targets, and overheated competition
  - Private equity investment return expectations decreasing – too much capital improves deal activity, lowers cost of capital
- Senior debt is readily available relative to EBITDA as an acquisition currency at good terms despite HLT curbs on banks
- Mezzanine debt is abundant, and in some cases, without warrants or other ‘equity kickers’
- Some private-equity-backed deals are being completed with lower levels of debt and more equity, and in some cases, with rolled equity contributions from sellers for a “second bite of the apple”
- Strategic buyers are doing better vs. PEGs in competitive processes
- **But…**

Takeaways

…the current M&A and Capital Raising environment may be at a peak:

- A "Blue Wave" in 2020 could ultimately roll back corporate-friendly tax and regulatory policy
- The Federal Reserve raised its benchmark interest rate four times in 2018, and has raised rates nine times since it began raising rates from near-zero three years ago. While rate increases are a sign of optimism regarding economic conditions, an overly aggressive path by the Federal Reserve could create significant economic headwinds
  - Federal Reserve officials signaled that they would implement two more rate increases in 2019. However, recent Federal Reserve statements have indicated flexibility depending on economic conditions
  - The rising cost of capital for acquisitions will most likely create a headwind for valuations. The full impact on middle-market companies remains to be seen
- Retiring baby-boomers will increase supply of companies for sale
- Unexpected geopolitical or economic shocks could negatively affect the market
  - Increased U.S. tariffs could ignite a trade war
- Looming possibility of a recession in the next two to three years
  - Among the economists included in a survey by the Wall Street Journal, 59% predicted a slow-down in the U.S. economy by 2020, while 22% foresee a recession starting in 2021[1]
  - Stock market volatility signaling recession fears

(1) Wall Street Journal, May 2018