

Independent Sponsors – Emerging Rock Stars in Private Equity Deal Flow

Southwest Venture Forum May 10, 2018

Moderator: Patrick F. Hamner

State of the Market

Panelists:

Jay Binkley

Hermitage Equity Partners

Co-Founder and Partner

www.hermitageequity.com

Jay Binkley is the co-founder of Hermitage Equity Partners and has been in the private equity industry since 1996. Throughout his career in the industry, Mr. Binkley has worked for leading private equity firms, including TVV Capital, Onex Corp (through an operating role at portfolio company Sitel Corp), Charterhouse Group International in New York and GTCR in Chicago. Over the course of his career, Mr. Binkley has been on the boards of numerous companies in a variety of sectors, including industrials, food processing, business services and healthcare. Through his experience arranging deals and managing investments, Mr. Binkley has developed an extensive network of relationships with corporate executives, intermediaries and financing sources throughout the country. Prior to entering the private equity business, Mr. Binkley was an investment banker with Equitable Securities (now SunTrust Robinson Humphrey). Mr. Binkley has a B.A. from the University of Pennsylvania and an M.B.A. from the University of Chicago Booth School of Business and has achieved a Chartered Financial Analyst Designation.

Matt McMurphy

Broadgate Capital LLC

Partner

www.broadgatecap.com

Matt joined Broadgate as a partner in March 2015, responsible for acquisitions and oversight of portfolio companies. Matt previously performed various executive-level operations, integration, strategy, business development, and acquisition functions at Radiant Healthcare Services and Encompass Home Health & Hospice, and served as General Counsel of both companies. Prior to joining Broadgate, Matt closed more than 25 acquisitions in a little over three years. Matt started his career as a transactional attorney focused on M&A and private equity representation. He earned a JD from The University of Texas at Austin and a BS in Policy Analysis (Economics and Government) from Cornell University.

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Panelists:

Sam Snyder

Greyrock Capital Group

Principal

www.greyrockcapitalgroup.com

Sam is a Principal at Greyrock Capital Group responsible for transaction origination, underwriting, and portfolio company management primarily in the Western US. Prior to joining Greyrock, Sam was an Associate at Goldman Sachs in the Technology, Media, and Telecommunications investment banking division helping corporate clients with financings, mergers and acquisitions, and anti-raid defense. Before Goldman, Sam worked as a Senior Research Analyst at Renaissance Capital responsible for global coverage of initial public offerings (IPOs). Sam currently serves as a board member of Allen Technologies, a provider of patient interactive systems to hospitals, Bentec Medical, a manufacturer of silicone-based medical devices and components, Blast Deflectors, Inc., a designer of blast deflection fences for airport infrastructure applications, MWA Intelligence, a provider of ERP software to the copy dealer industry, Ogle School, the largest operator of beauty schools in Texas, Paeteria La Michoacana, a leading manufacturer of Hispanic-influenced ice cream bars called “paletas”, and Solair Group, a leading fabricator of maintenance tooling and ground support equipment for commercial aircraft.

Sam earned an MBA with Honors from the Haas School of Business and an AB in History from Princeton University. Sam is also a CFA charterholder.

State of the Market

Panelists:

Todd Dauphinais

Clavis Capital Partners

Managing Partner

www.claviscp.com

Todd is the founding principal of Clavis, responsible for overseeing all aspects of the firm's investment, operational and fund-raising activities. Over his career, Todd has completed over 20 equity transactions representing in excess of \$800 million of capital deployed. He has also held senior operating and strategic roles in manufacturing and industrial companies throughout his career.

Prior to founding Clavis, Todd was the lead partner responsible for the North American operations of a large European based investment fund. Todd's primary responsibilities were establishing and launching the North American effort for the fund and sourcing, structuring, financing and execution of new investments and opportunities.

Previously, Todd served as President and CEO of EFI Electronics, an industry leading manufacturer of electrical protection & power quality products where he led his firm to record revenues and profitability for four straight years. In 2009, EFI Electronics was awarded the prestigious Shingo Prize for Manufacturing. Prior to EFI, Todd served in various strategic and operating roles at leading firms such as Schneider Electric and Rockwell Automation. He started his career as a strategy and M&A consultant with Deloitte Consulting focusing on the electric & gas utility sector.

Todd received his MBA with honors from the University of Notre Dame and received his B.A. from Texas A&M University. He is an active member of the Young President's Organization, the Association for Corporate Growth, the National Association of Corporate Directors, and various charity, faith and angel investing organizations

State of the Market

Overall N. America M&A Activity



“CLIFFJUMPS”

Posted on YouTube (2012): Today: 129,126,084 Views. Why?

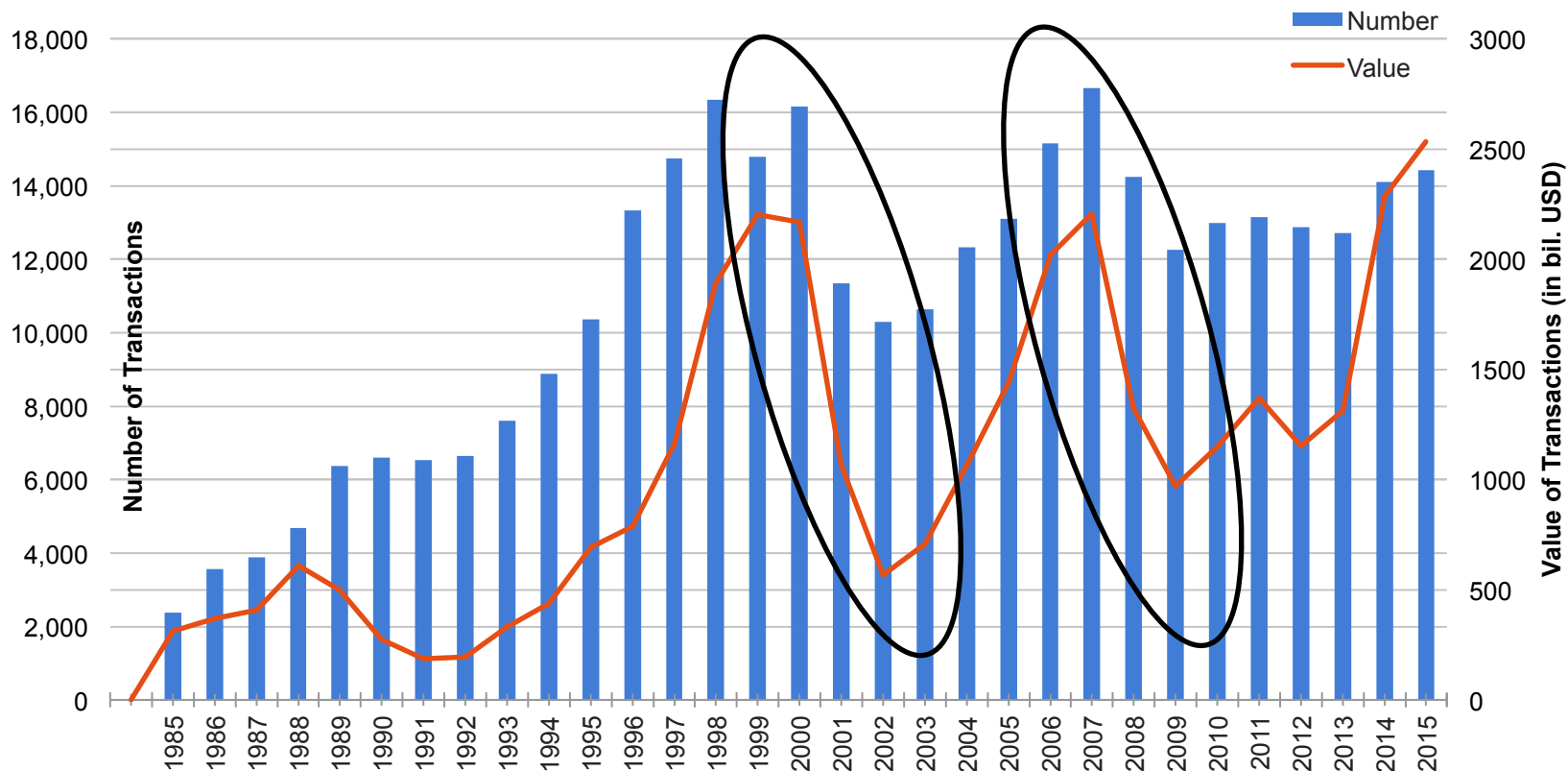
“What’s going to happen here??”

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Overall U.S. M&A Activity

With valuations at record levels at end of '15, would '16 or '17 be the deal # "Year of Correction?"

Mergers & Acquisitions North America



Source: IMAA Institute

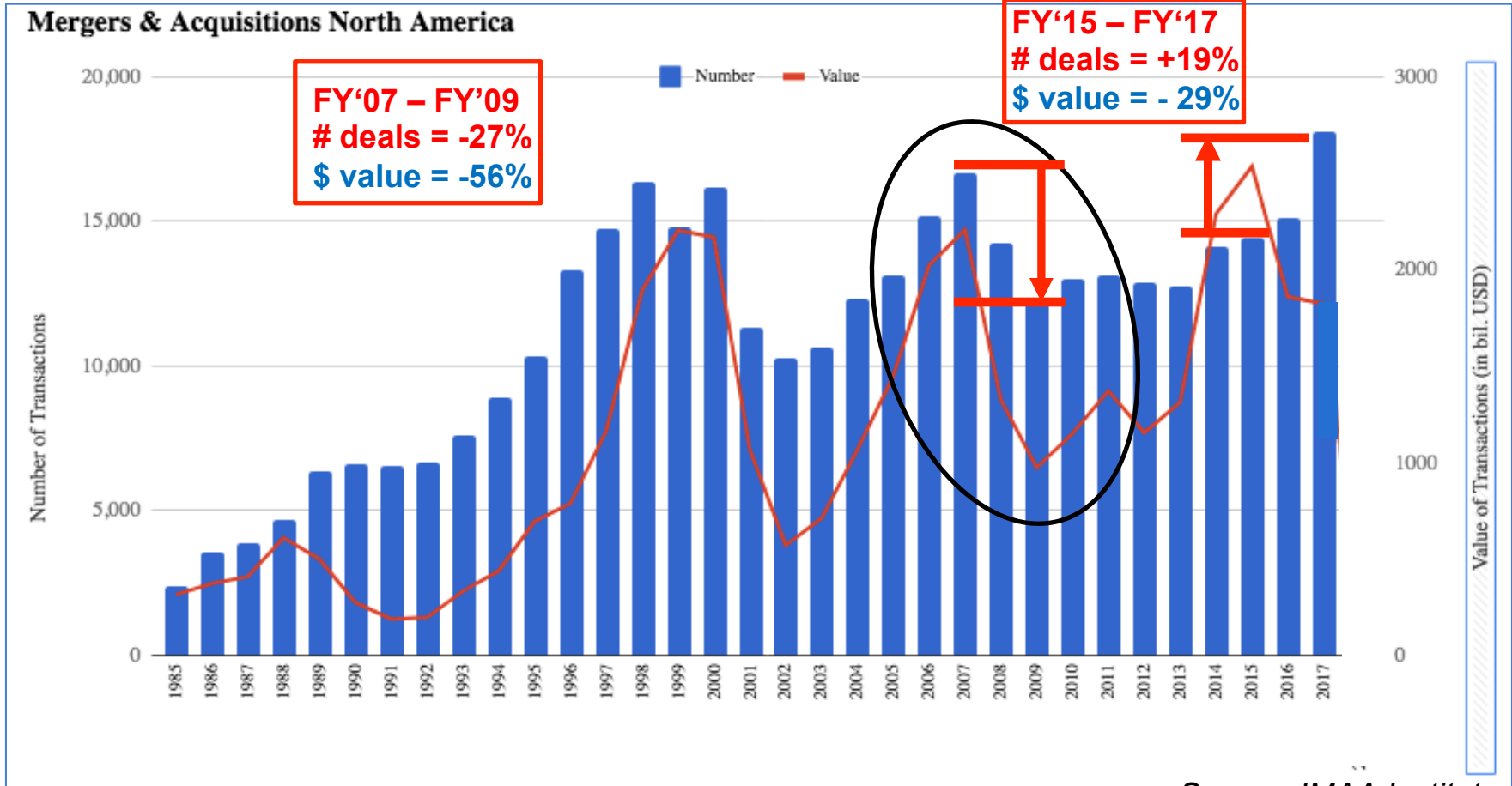
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Overall USA M&A Activity

What's going to happen here?

Peak to trough '07-'09, # deals & value down -27% & -56%...

'15-'17, value down -29% (\$2.4T to \$1.7T), # deals UP 19%, surpassing '07 peak!!

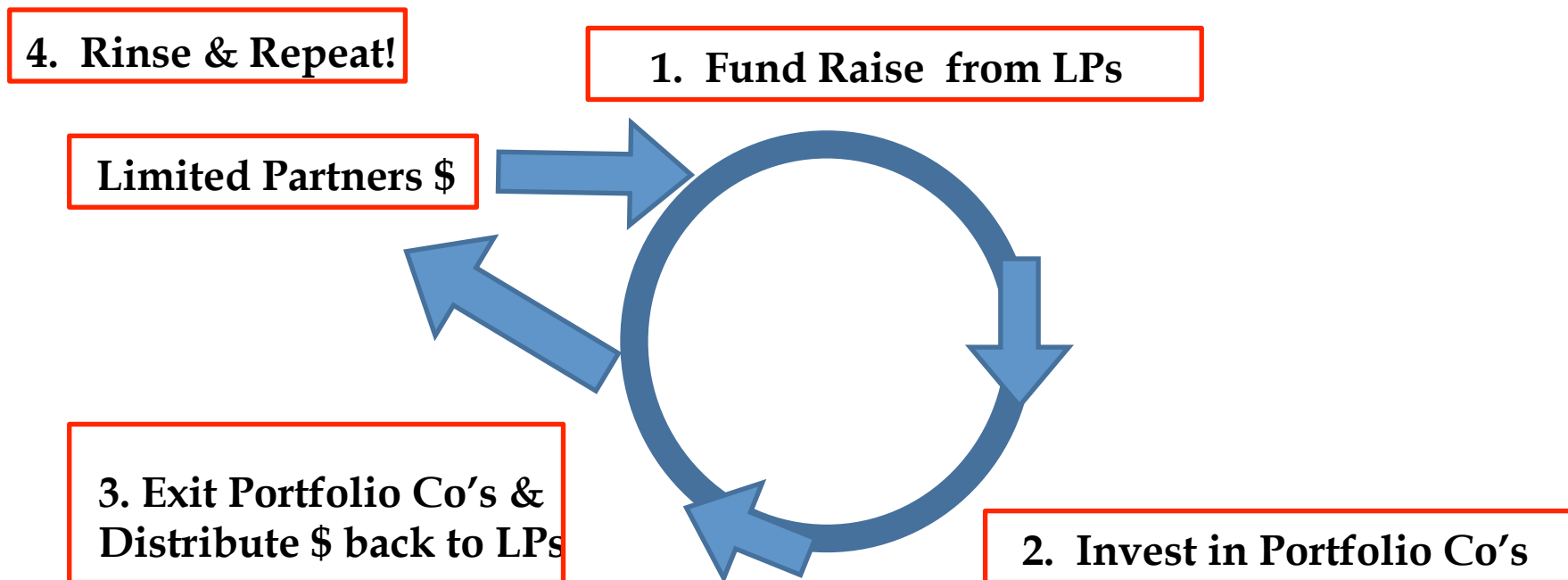


Source: IMAA Institute

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Private Equity EcoSystem Life Cycle

PE cycle = Fund Raise from LPs, Invest Capital in Portfolio Co's, Exit Portfolio Companies and Distribute \$ to LPs... Repeat!!



Source: PitchBook

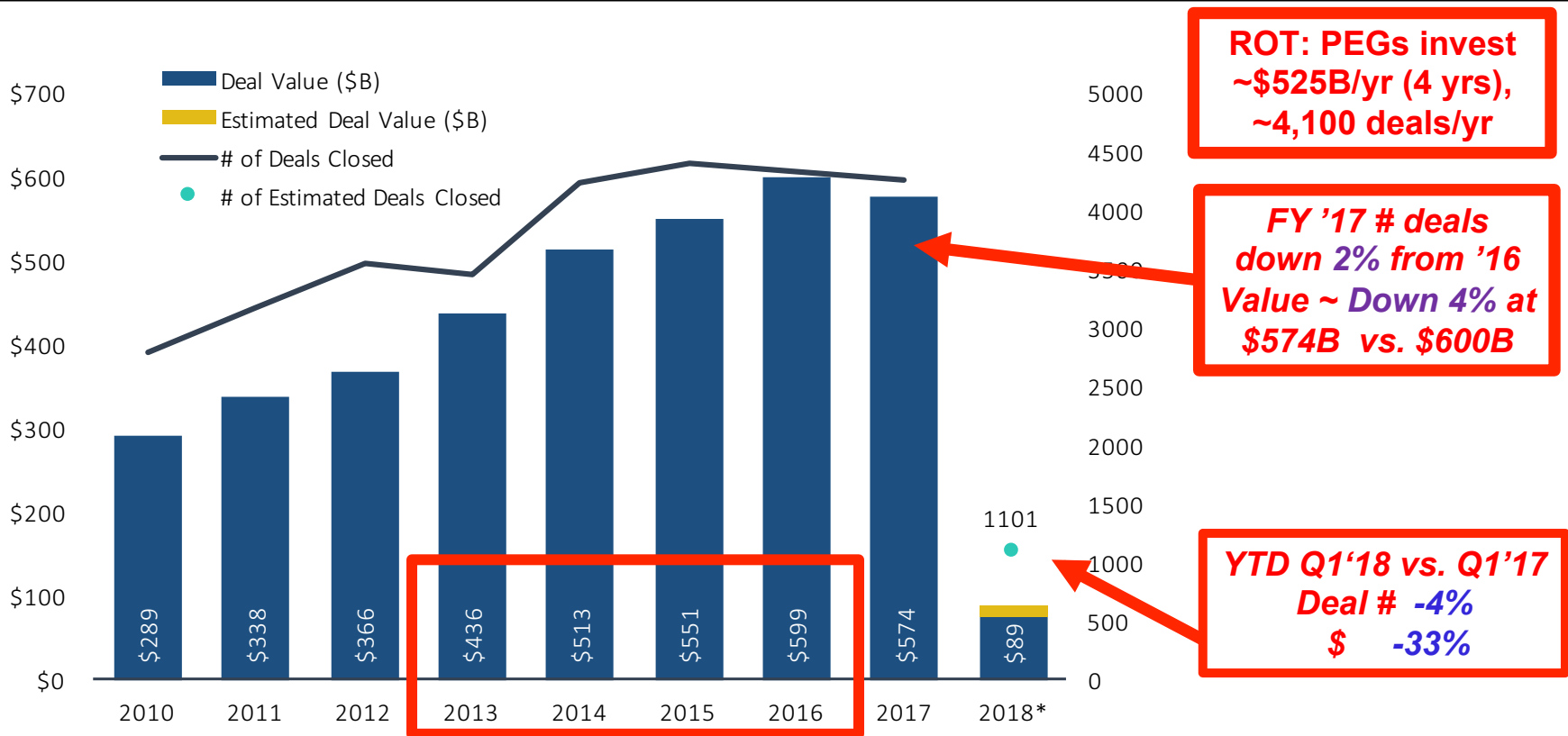
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All U.S. PE Investments by Year

After 4 good years '13 - '16 , at ~ 4,100 deals/Yr (\$525B/Year invested), the music slowed...

'17 deal flow of 4,248 flat to slightly off -2% from '16; while \$ invested off -4% to \$574B.

However, Q1 '18 vs. Q1 '17, **deal # off -4%**, **\$ invested OFF -33% !!**

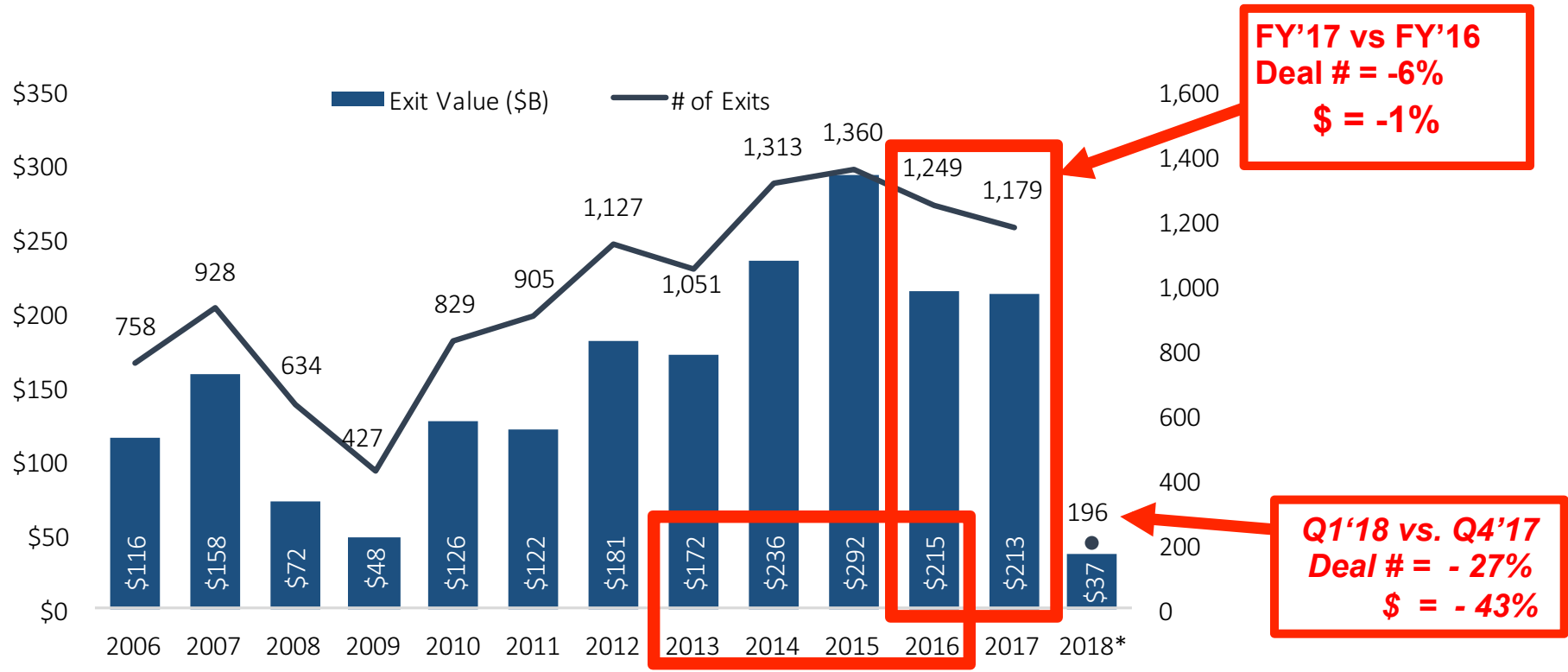


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Rule of Thumb: PEGS exit rate: \$230B+/Yr, about ~1,200 deals/yr

U.S. Private Equity Exit Activity by Year

FY'17 vs '16: 1,179 PE-backed # exits off 6% from 1,249, but \$ out were flat at ~\$213B
Q4'17 to Q1'18: 196 exits off -27%, \$ out dropped -43% to \$37B from \$64B.

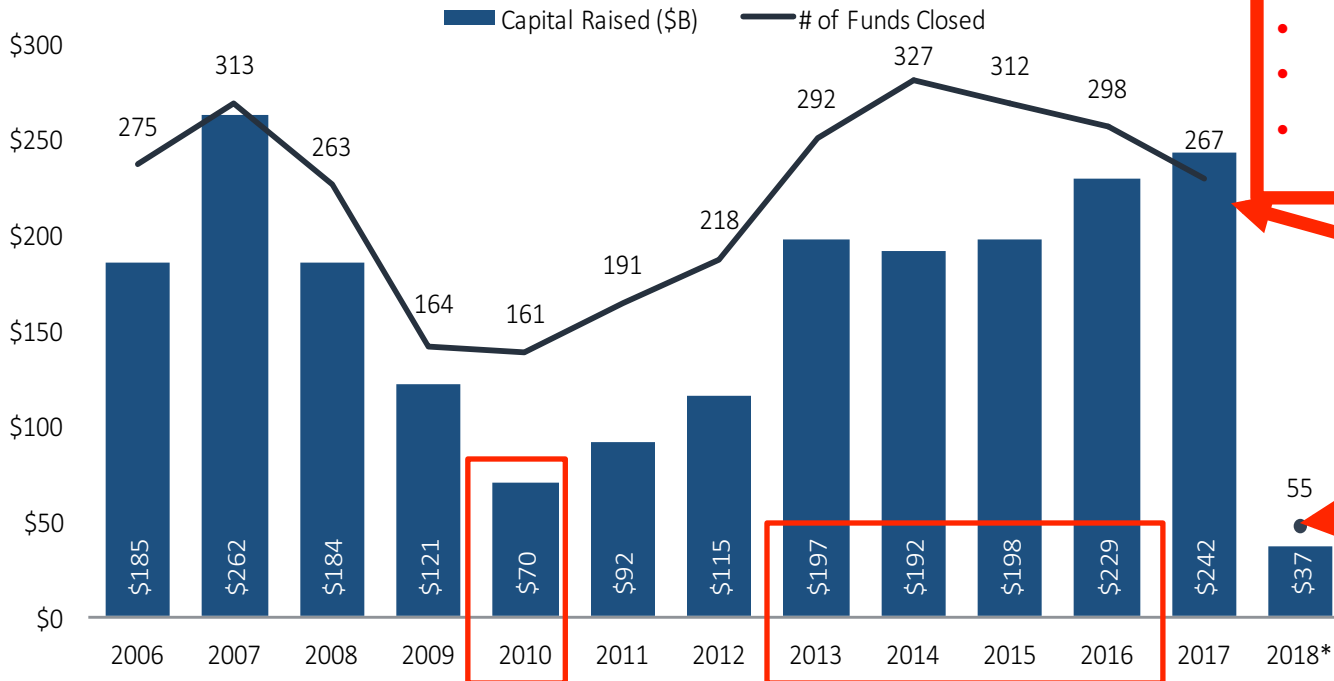


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PEG Fund Raising - Possible drop in '17 turned into 2nd highest raise since '07

From a lull in '10 to robust capital formation in '13 - '16 (Avg ~300 funds at \$200B/year), # of PE funds raised declined 5% in '15, 4% in '16 and 10% more in '17. However, the 267 funds raising capital in '17 hauled in \$242B - highest since the peak in '07!!!

However, Q1'18's decline in # and \$ could be an inflection point...



Rule of Thumb:

- PE = \$550B (Dry Powder)
- Corps/Strategics = \$1.9T
- 300 PEGS raise ~ \$200B/Yr (past 4 yrs '16)

FY'17 vs. FY'16

= -10% 267
\$ = +6% \$242B

Q1'18 (ann.) vs. FY'17

= -18% 220
\$ = -39% \$148B

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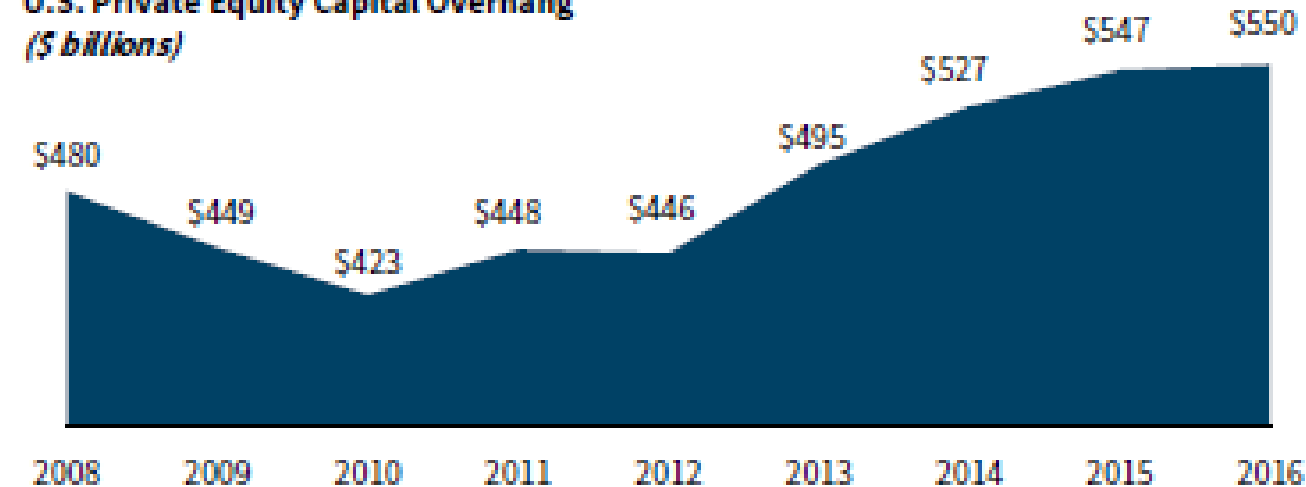
Serious PEG Dry Powder ...

Significant increase in Exits past 3 years... boosted fund raising... producing \$550M in Dry Powder in FY'16 - Pitchbook estimates 75% un-invested for more than two years

Un-Invested Capital of U.S. PE Investors (\$ in billions)

**ROT: PEGs
Dry Powder
\$550B**

U.S. Private Equity Capital Overhang (\$ billions)



Source: Pitchbook

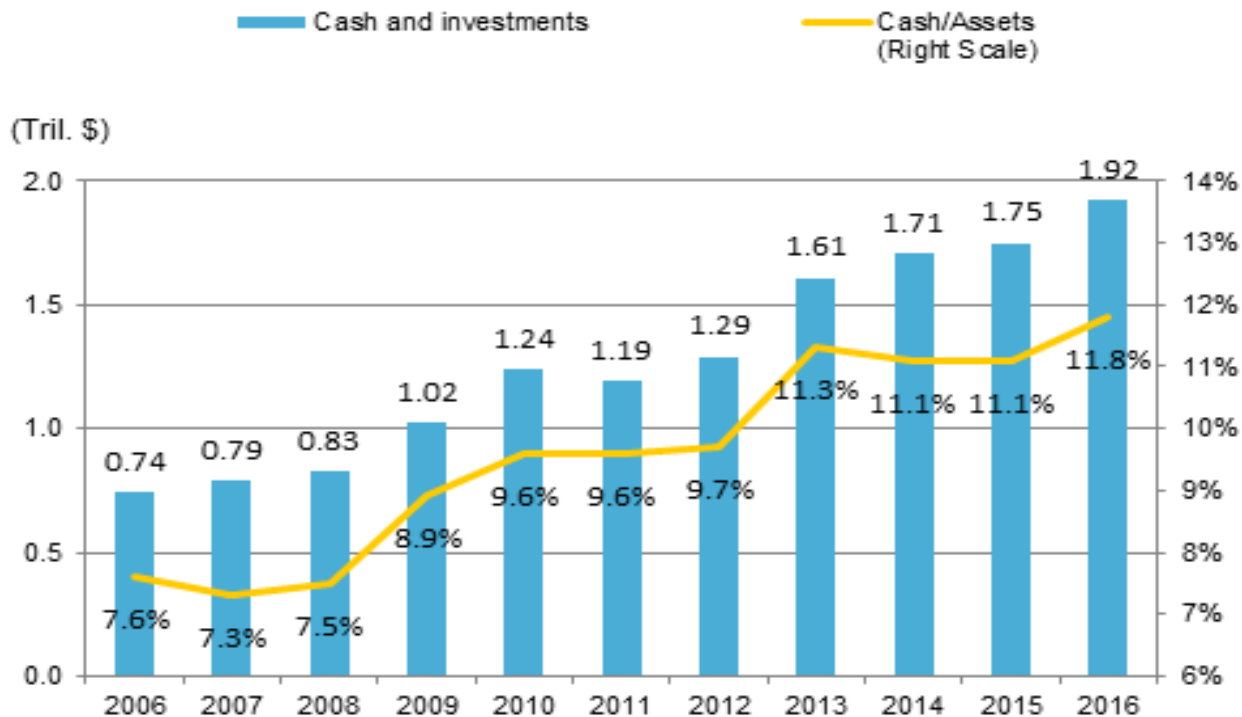
Source: PitchBook

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S&P rated non-financial corporate borrowers (~2,000), i.e. "Strategics" sitting on \$1.9 Trillion of cash, with another \$2.8 Trillion overseas, possibly to be repatriated.....

Ample Liquidity? - S&P Rated Co.s - Cash Balances (\$ in billions)

Chart 1
Cash Reaches \$1.9 Trillion



**ROT:
Strategics
~\$1.9T Cash**

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Source: S&P Global Ratings 5/25/17

Lower Middle-Market Credit Opportunity: Supply Side

Market Returns and Spreads: Source PNC Mezzanine

	1995	2000	2015	2016	2017
Five-Year Treasuries	7.8%	5.0%	1.4%	1.2%	1.8%
Average Mezzanine Targeted IRR	22.7%	19.1%	16.5%	16.6%	16.0%
Spread Over Treasuries	14.9%	14.1%	16.1%	15.4%	14.2%
High Yield ^{(1) (2)}	9.8%	14.6%	6.1%	7.3%	5.5%
Spread Over Treasuries	2.0%	9.5%	4.7%	6.1%	3.7%
Average Buyout Equity Targeted IRR ⁽³⁾	30.0%	27.5%	18.5%	18.5%	17.5%
Spread Over Treasuries	22.2%	22.5%	17.1%	17.3%	15.7%
Buyout Equity Targeted IRR Less Mezzanine Targeted IRR	7.3%	8.4%	2.0%	-1.9%	1.5%

Source: Atlantic Conferences Inc. PNC Mezzanine Capital May 2017

1995 and 2000 are end-of-year yields (Source: Citigroup's High Yield Composite Index)

2015 reflects the yield as of April 24, 2015, 2016 reflects the yield as of May 4, 2016 and 2017 reflects the yield as of April 28, 2017 (Source: S&P 'B' Rated High Yield Index)

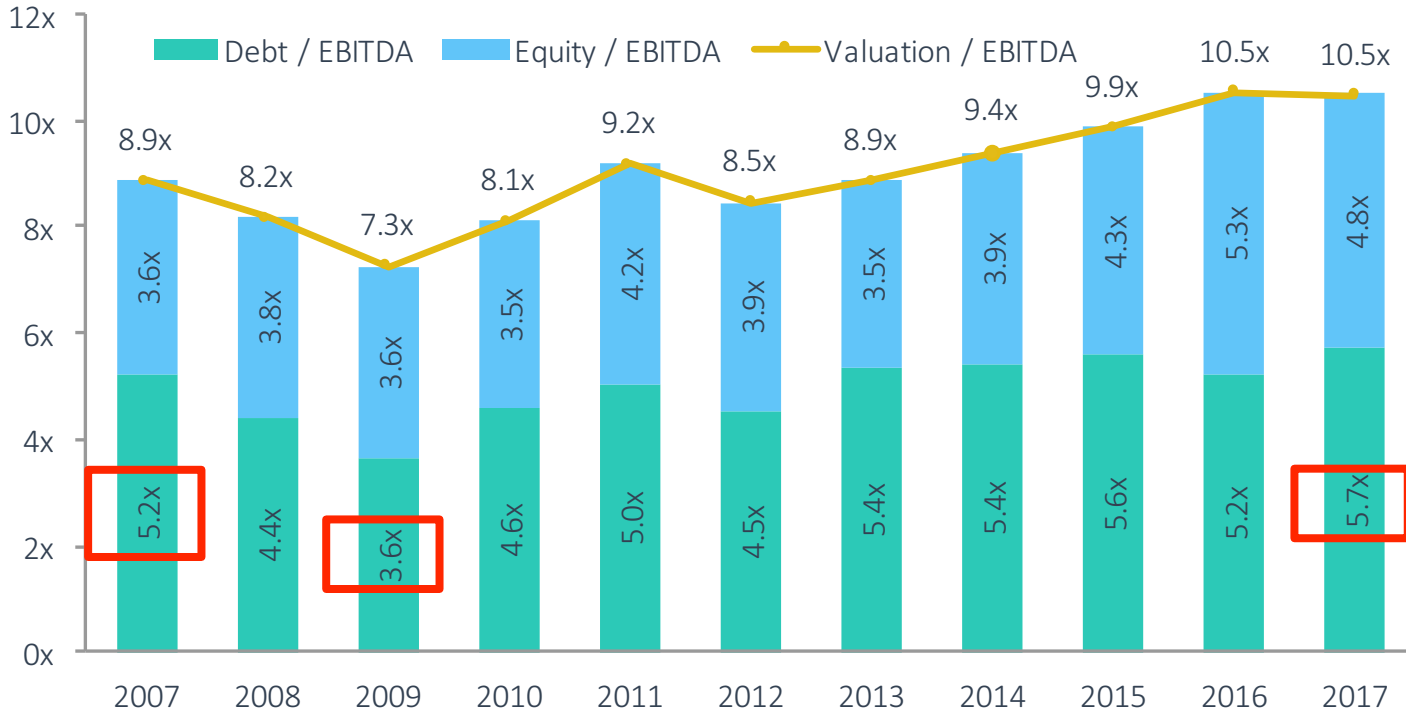
Approximations based on market data (for illustration purposes)

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All US M&A (including PE Buyouts): Equity as % of the Cap. Stack

Equity as % of Cap ~ up '13 to '16 to 50% ,
slight dip in '17 to 46%, as more debt available for all deals

ROT: Avg. % Equity Cap Stack = 40% w/ range of 40%-50%



ROT: Larger LBOs Total Leverage = 5-6X TTM EBITDA

Fear/Greed Meter

Source: PitchBook

Take aways for a discussion on Independent Sponsors:

- **Near record activity level for PE investing: \$525B**
- **Stable exit activity: \$200B**
- **Strong fund raising momentum in '17: \$245B**
- **Enormous dry powder for PEGs \$550B and Strategics \$1.9T**
- **Abundant debt available, leverage multiples 5.7X**
- **Highest Purchase Price multiples in years: 10.5X**
- **IRRs and return on capital under pressure – sub 20's?**
- **Where does PE go for profitable DEAL FLOW???**

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Purchase Price Multiples in Lower Middle Market

GF Data: \$10 -\$25M TEV hit 6.4X EBITDA for '17, ALL LMM deals '17 at 7.4X - highest ever

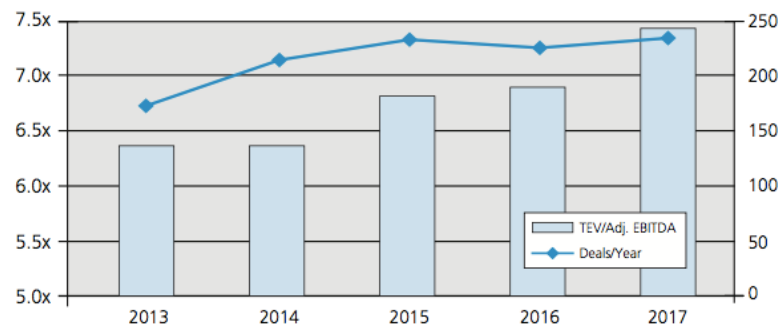
Total Enterprise Value/EBITDA

Average Multiples and Deal Volume

TOTAL ENTERPRISE VALUE (TEV)/EBITDA

TEV	2003-2012	2013	2014	2015	2016	2017	Total	N =
10-25	5.5	5.8	5.5	5.8	5.9	6.4	5.6	1132
25-50	6.1	6.8	6.4	6.6	6.5	6.7	6.3	819
50-100	6.7	6.6	7.5	7.8	7.3	8.3	7.0	564
100-250	7.2	7.1	7.5	9.0	9.0	9.2	7.9	282
Total	6.0	6.4	6.4	6.7	6.8	7.4	6.3	
N =	1735	163	211	237	220	231		2797

AVERAGE MULTIPLES AND DEAL VOLUME



Please note that N for 2003-12 encompasses ten years of activity.

Rule of Thumb: Most Lower Middle Market Buyouts trade at Purchase Price = 5-7X TTM EBITDA

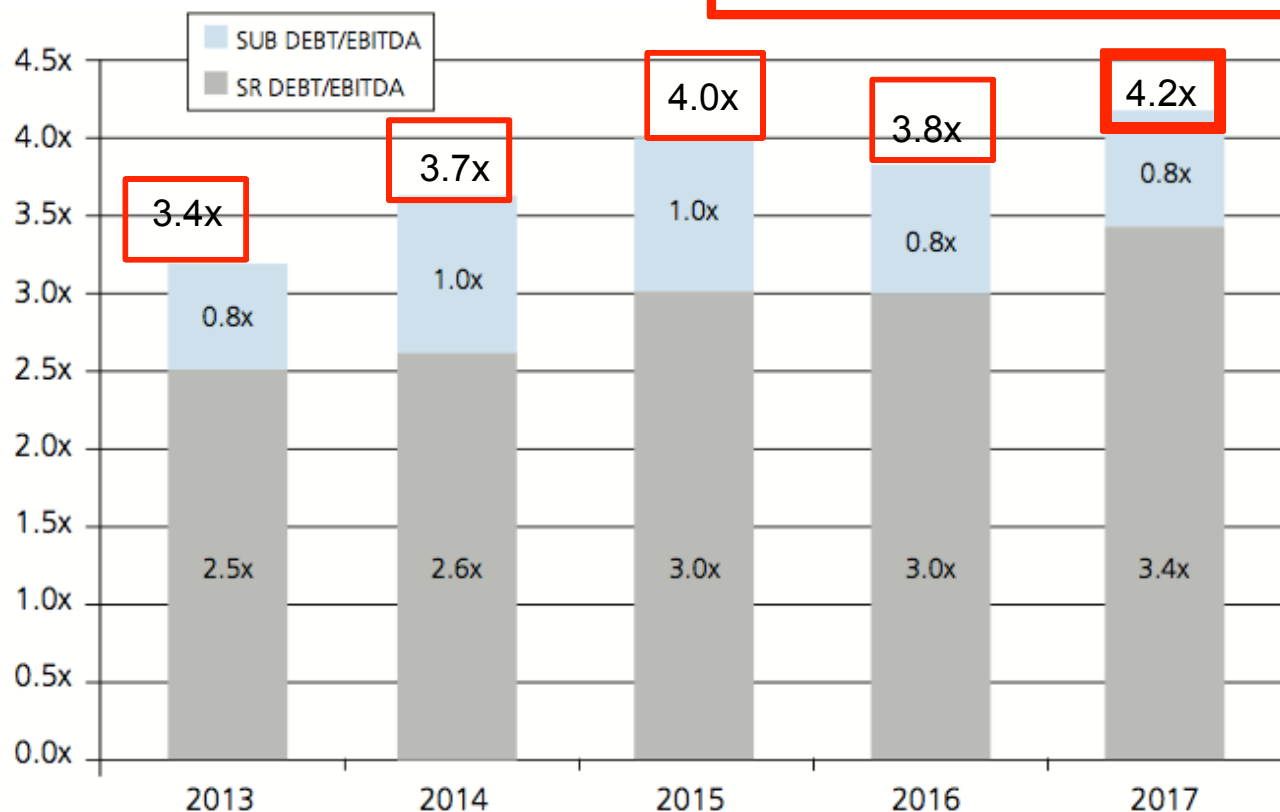
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Leverage Multiples for Lower Middle Market (\$10 to \$250M Enterprise Value)

GF Data - LMM total leverage hit 4.0X in '15, then surged in '17 to 4.2X Record!!

ROT: OCC's "3X4" Box caps at 3X Sr, 4X Total Debt, but Sr. debt X up 13% in 17!!



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