

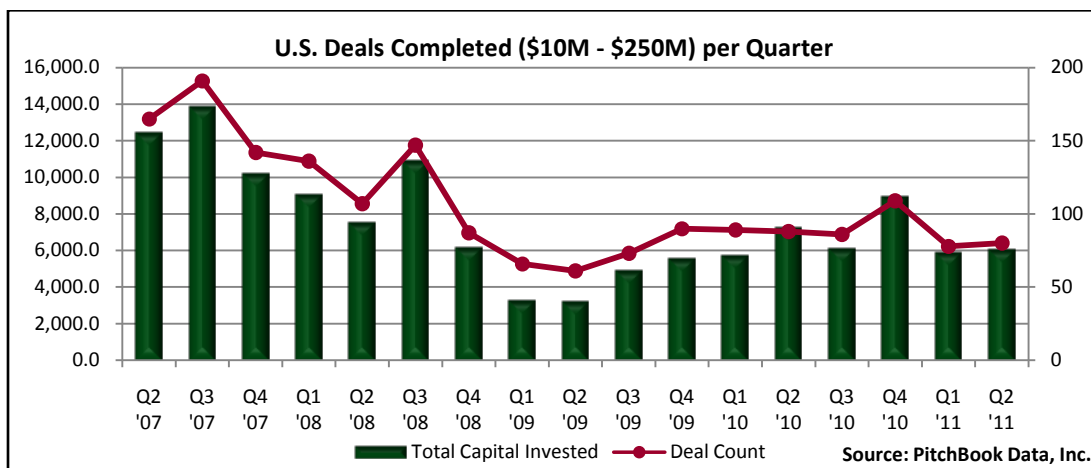
M&A Insights for Business Owners: Mid-Year Review, July 2011

Middle Market M&A Drivers Will Power Through Headwind of Slow Economy

- Middle market M&A activity will accelerate in H2 2011 and 2012 despite economic hurdles.
- Currently, it's a seller's market with a window of opportunity as valuations are trending upwards and cash-rich buyers are competing for good companies.
- Rising valuations and a wave of retiring baby boomer business owners will result in more sellers bringing companies to market. Business owners considering a transaction within the next two years should begin the process now.

M&A and the Economy

M&A market strength does not share a 1:1 correlation with the overall economy, though in recent quarters the deal flow and valuations have been trending in line with the U.S. recovery. The chart below shows deal flow in the middle market (\$10M-\$250M) from Q2 2007 through Q2 2011. After the economic crisis of 2008, we saw a steady increase in M&A activity as credit markets began to slowly open up again. Many business owners who were considering a sale in 2008, but didn't come to market in the first part of the year, struggled to find a good valuation in 2009, if they were able to complete a transaction at all. By the end of 2010, valuations started to rebound to pre-recession levels depending on industry.

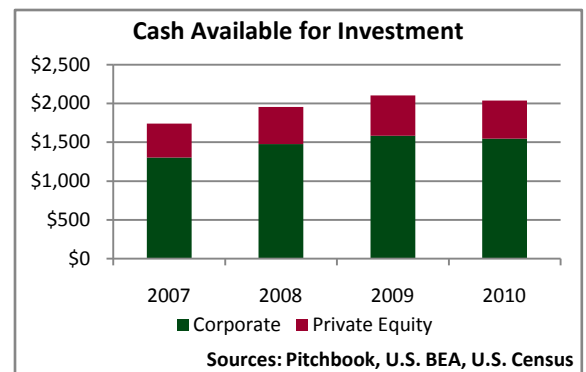


At mid-year 2011, June reports of higher unemployment, slowing GDP growth, and unprecedentedly high government debt levels cast a shadow over the U.S. economic recovery, which earlier in the year seemed slow but steady. These economic factors tended to curb M&A deal flow in recent quarters. Another possible reason for a 2011 dip is the rush to market in 2010 before the capital gains tax cuts were extended through 2012. We believe it's possible a similar spike in deals will take place in 2012 and H1 2011 could be the "calm before the storm."

Nevertheless, several factors outlined below should culminate in an active M&A market that delivers a window of opportunity to sellers.

Strategic and Financial Buyers Flush with Cash

Financial and strategic buyers are currently holding approximately \$500 billion and \$1.6 trillion in "dry powder," respectively. These amounts represent two and a half years' worth of un-invested capital. In order for private equity groups to meet the return rates their investors demand, they must deploy this capital soon. Strategic buyers, also have certain growth rates that they must achieve to satisfy shareholders. One of the easiest ways to achieve this growth is through acquisitions, particularly in times of slow organic growth.

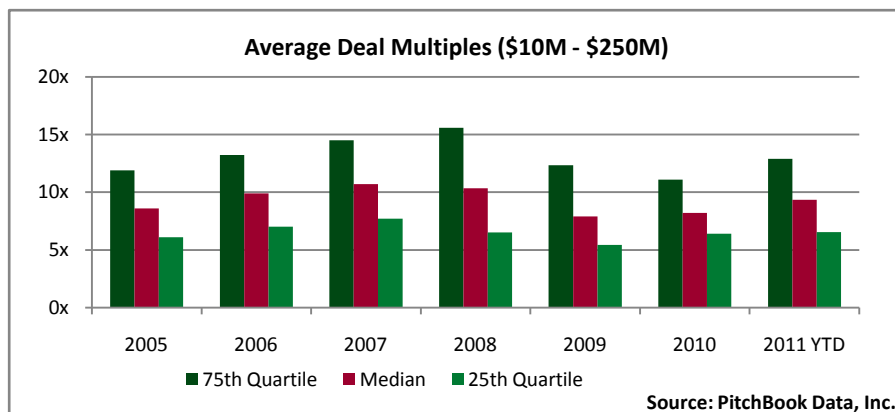


Globalization, Technology and a Weak Dollar = More Cross Border Deals

At the conclusion of a well-run M&A process, U.S. companies may find that the ideal acquirer, and the one who will offer the best price, more and more often falls outside the traditional list. The explosion of social networking has allowed communication between the world of buyers and sellers like never before on web sites such as PE Nexus and LinkedIn. Databases and M&A platforms have been developed to allow highly detailed matchmaking to thousands of private equity groups and corporate development divisions globally. This expanded access to global acquirers, combined with the weak dollar, brings more competition for U.S. companies and cross-border deals where valuations can significantly beat industry norms.

Higher Valuations, Baby Boomer Retirements Will Bring More Sellers to Market

2011 brought a significant increase in average deal multiples compared to 2009 and 2010. We believe that this trend will continue into 2012 due to increased competition for quality companies and relaxed lending parameters. However, change is on the horizon.



In the U.S. someone turns 60 every 11 seconds. With 30% of family-owned businesses estimated to change leadership due to retirement in the coming decade, you can expect a huge wave of baby-boomer-owned companies for sale as the market rebounds. This increased “supply” of acquisition targets will eventually consume the idle capital and exhaust banks’ lending coffers as buyers slowly work through the most attractive targets first, all eventually resulting in downward pressure on deal multiples as a result.

We recommend business owners considering a transaction within the next two years begin the process now. Most M&A transactions require an average of nine months to complete. In 2008, when deal multiples were peaking, many business owners made the mistake of waiting too long and missed the window. Our advice to business owners is to take advantage of the current high multiples, otherwise you may be leaving a significant amount of money on the table or you may be forced to wait several years for the next peak in valuations.

About Allegiance Capital

Headquartered in Dallas, Allegiance Capital has offices nationwide and a 13-year history of closing transactions for private companies in the middle market. Business owners considering their options related to an exit, selling a business or recapitalization, can obtain information about the process from Allegiance Capital by calling 214-217-7750. For more information, view a video about our firm on [YouTube](#) and visit [AllCapCorp.com](#). Receive regular information on financing and selling businesses in the middle market by subscribing to the [Capital Ideas blog](#) and following Allegiance Capital on [LinkedIn](#), [Facebook](#), and Twitter: @ALLCAP.

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