Capital Markets and Investment Banking

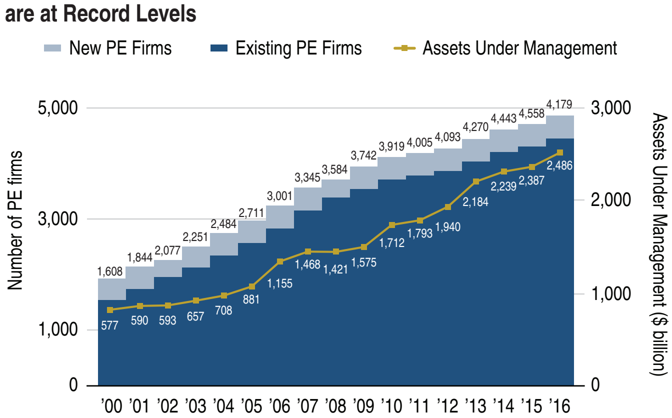
Market Update

NOVEMBER 2017

M&A Boom: Preparation is Key for Private Sellers to Achieve Optimal Results

The M&A market, particularly the middle market, has been and continues to be robust, creating a seller friendly environment for private business owners. Today, private business owners have more exit options than ever before, largely driven by the growth in private equity firms and available capital in the marketplace. The number of private equity firms has increased substantially over the past 15 to 20 years; in 2000, there were roughly 1,600 private equity firms and by the end of 2016, there were nearly 4,200.[1] Today, private equity firms manage nearly $2.5 trillion[2] of assets with approximately $960 billion[3] callable reserves ("dry powder") ready to be deployed for platform investments and add-on acquisitions for existing portfolio companies. Further demand for M&A targets is driven by strategic buyers who continue to face a low, organic growth environment. With strong balance sheets and easy access to credit, strategic buyers utilize M&A as a means to enhance their strategic position and accelerate revenue and earnings growth.

Number of Firms and Assets Under Management are at Record Levels



Notes: PE = private equity; the firms include those specializing in buyouts, the secondary market, funds of funds, and growth and venture capital.
Source: Preqin.

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The M&A market is in its fourth year of above average volume. In 2015, the M&A market hit a record high of nearly $4 trillion of transaction volume. Although 2016 M&A volume was down from a dollar perspective, the total number of transactions exceeded the prior year by 3.3%. Additionally, 2017 is on track to be another strong year of M&A.[4]

The combination of an expanding global buyer universe and a prolonged, robust M&A market has created a number of dynamics that a private seller should consider in evaluating a potential sale process. In today's market, many buyers have become averse to highly structured, broad sale processes. In evaluating new opportunities, buyers have become increasingly disciplined with how they spend their limited resources, and are prioritizing potential targets that fit squarely within their defined acquisition criteria. Given that valuations are reaching record highs for private companies, acquirers are spending additional time and resources on due diligence to ensure a thorough understanding of all risks associated with potential targets. This environment also results in failed sales processes due to a gap between buyer and seller valuation expectations, as well as processes that are stalled due to unfavorable findings during due diligence.

Mesirow Financial®

Given these dynamics in the current M&A market, there are a number of steps private sellers have taken to maximize value while increasing the certainty of a transaction being executed.

Successful exits of family businesses or owner/entrepreneur-led companies typically share some common attributes in how they approach a transaction process, which consists of three stages: (1) exploration, (2) preparation and (3) execution. Stage one involves exploring the various strategic alternatives and structures available to private companies. This allows company owners to compare and contrast options and become educated on the possibilities, as well as the implications, of different scenarios. Stage two allows for company owners to spend time and money preparing to go to market. This involves gathering existing and new information that buyers and investors typically look for during the due diligence process. Usually these requests are not “off-the-shelf” for private company owners and must be created from scratch. Stage three is focused on the successful execution of a sale process. This stage is typically led by an M&A advisor working in close coordination with the owners and management team. Company owners that have thought through the various exit options and have thoroughly prepared in advance of executing a sale transaction maximize the probability of an efficient process that yields a desired outcome. A more in-depth overview of the transaction process is further outlined below:

Exploration
Record amounts of capital raised by private investment firms, along with the pressure to deploy capital within a certain investment horizon results in greater flexibility in the types of financial structures available to private company owners. For financial investor-led transactions, company owners can choose between equity and debt investments as well as a spectrum between majority and minority control. In some situations, company owners can elect to continue running the business post-transaction or work with a partner that will help facilitate a near-term management transition. Strategic acquirers continue to be aggressive in the M&A market, but have not shown increased flexibility in structuring acquisitions. Based on company owners’ goals and objectives, a process can be designed to most effectively yield the optimal result. In addition, depending on the options that a company owner is seeking post transaction, the buyer universe can be tailored to address these preferences.

Preparation
Preparing due diligence and transaction-related analyses in advance of a process typically requires additional time and expense, often resulting in greater outcomes. Some examples of impactful due diligence analyses that owners prepare include quality of earnings reports, market studies, tax analyses and audited financial statements. Typically, these analyses are prepared by third parties and completed during the due diligence phase of the process. Owners of private companies have had success in proactively commissioning these reports in order to expedite the due diligence process and minimize execution risk. In addition, owners will take time to comprehensively evaluate about the financial projections and strategic growth story that will be presented to buyers in great detail. Buyers and investors place a premium on growth and will reward companies that have been thoughtful about presenting a credible view of future growth.

Execution
Upon completion of exploration and preparation, owners will typically work with their M&A advisors to design a customized process that yields the best outcome for shareholders, while minimizing execution risk. For many private company owners, maintaining the company legacy is a high priority and ensuring the ability to choose a high-integrity partner during the execution of a transaction is critical. Once a process has launched, the company and their advisors move quickly to maintain momentum while ensuring confidentiality. In addition, owners proactively devise messaging around the transaction announcement to key constituents including customers, vendors and employees.

Since the recovery from the global recession of 2008–2010, private owners who have worked with advisors to prepare in advance of selling their businesses have benefitted from a multi-year boom in M&A activity that has resulted in record valuations. We continue to see examples of early preparation on the part of business owners driving favorable exit outcomes in the midst of a market that is difficult to navigate. Based on the current economic environment and liquidity in the financial markets, it is unlikely there will be any disincentive in the M&A market in the near term, and it is expected that prepared sellers will be best positioned to capitalize on the current market dynamics.

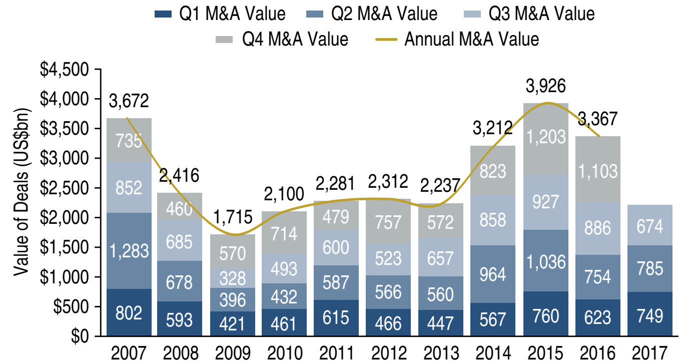
1 Preqin Private Equity Online.
2 Preqin Private Equity Online.
3 Bloomberg.
4 MergerMarket.

Market Snapshot: Middle-Market Mergers & Acquisitions

Global M&A Market Expected to End with Strong 2017 Despite Sputter in Q3 2017

- Pending regulatory and tax reform has led decision-makers to adopt a “wait and see” approach, particularly on larger deals, despite having a strong pipeline of acquisition targets.
- Global M&A values declined 1.7% during Q1–Q3 2017 with 11,824 deals worth $2.21 trillion compared to 12,283 deals worth $2.25 trillion during Q1–Q3 2016.
- U.S. M&A values declined 30.2% in Q3 2017 with 1,123 deals worth $283.7 billion, compared to 1,327 deals worth $406.7 billion during Q3 2016.
- Despite Q3 2017 deal statistics falling short of Q3 2016, Q4 2017 is expected to be a strong quarter for M&A, as conditions for deal activity remain strong.

Quarterly Global M&A Comparison

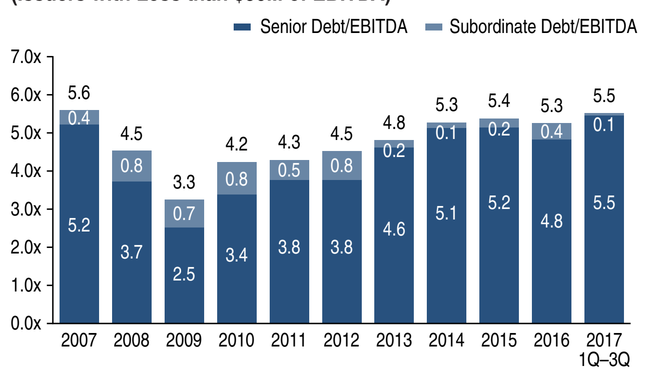


Source: MergerMarket.

Significant Opportunities Exist to Capitalize on the Favorable Financing Environment

- Borrowers continue to capitalize on the favorable financing environment.
  - Loan terms continue to be covenant-lite.
  - Interest rates remain near historic lows.
- Total leverage in Q1–Q3 2017 for middle-market issues with less than $50 million of EBITDA averaged 5.5x, which is higher than the 2016 average.
- Equity contribution for middle-market LBOs averaged approximately 46% in Q1–Q3 2017, which is a slight increase from the average level during 2016.
- Senior stretch loans (hybrid asset-based and cash flow loans) are prevalent given current market dynamics.
  - Conditions exist for debtors to cover all leverage needs with senior debt at senior debt pricing (versus higher mezzanine debt pricing).

Average Debt Multiples of Middle-Market LBO Loans (Issuers with Less than $50M of EBITDA)



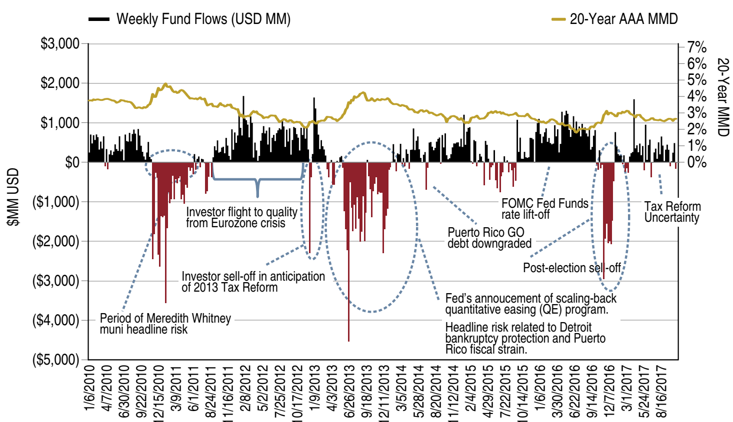
Source: S&P Capital IQ LCD.

Market Snapshot: Municipal Bonds

Municipal Bond Fund Flows and Municipal Market Data (MMD)

Over the past year, municipal markets gradually settled from the turbulence that arose from the presidential election in November of 2016, only to experience a recent resurgence in volatility from tax reform negotiations. This past quarter, municipal markets saw a partial relief from the passage of the State of Illinois budget, which helped to move an average of more than $260 million into municipal funds per week. The 20-year MMD continues to remain attractive on a historical basis, and is currently trading at more than 50 basis points below levels seen in the first half of 2017. The tax bill introduced by the House of Representatives roiled municipal markets at the end of the third quarter. The House tax bill, as proposed, would make significant changes to tax rules that apply to tax-exempt bonds, specifically impacting private activity bonds (PABs) and advance refunding bonds. The tax proposal released by the Senate dampened some of the market's concerns, but it still remains to be seen as to what shape tax reform will take, or if a tax reform bill will pass at all. In addition to tax reform, market expectations of a December interest rate hike from the Federal Reserve, Puerto Rico concerns and market uncertainties arising from State of Connecticut budgetary difficulties may impact weekly fund flows going forward into 2018.

Municipal Bond Fund Flows and 20-Year MMD



As of the weekly reporting date of 11/01/2017.
Source: EPFR Global Fund Flows and Allocations Data – All Muni Funds (Retail and Institutional Funds).

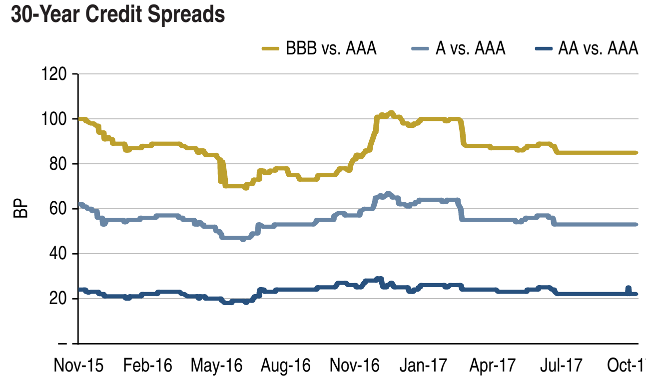
Trailing 16-Week Data

Muni Fund Reporting Date	Weekly Fund Flow ($MM USD)	20-Yr AAA MMD (%)
7/19/2017	247.68	2.58
7/26/2017	343.43	2.57
8/2/2017	85.95	2.56
8/9/2017	503.01	2.55
8/16/2017	199.78	2.59
8/23/2017	650.26	2.54
8/30/2017	420.78	2.51
9/6/2017	28.80	2.49
9/13/2017	317.32	2.54
9/20/2017	444.30	2.59
9/27/2017	314.35	2.64
10/4/2017	(97.26)	2.64
10/11/2017	24.19	2.62
10/18/2017	241.66	2.51
10/25/2017	484.19	2.63
11/1/2017	165.44	2.64

Credit Spreads

- October's spreads describe a slightly flatter yield curve against a background of positive institutional cash flows and tightening credit spreads. However, the President's recently announced tax reform package, "Tax Cuts and Jobs Act," will be the main driver of municipal market activity for the foreseeable future.
- The critical story lies in the tension between the House's version of the Act's proposed elimination of tax-exempt private activity bonds and proposed restrictions on advance refundings versus what we might see from the Senate Finance Committee's markup of their version, and the final bill that emerges from the Congressional reconciliation process.
- The final outcome of the political back and forth, that is an integral part of the "sausage-making" involved in federal tax policy changes, is unknown. However, market participants should be prepared for considerable spread volatility as the final joint House/Senate version of the bill takes shape, and the market assigns a probability of its passage.

30-Year Credit Spreads



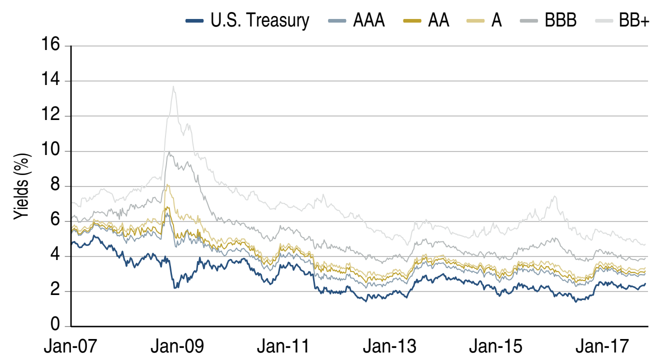
Source: The Municipal Market Monitor (TM3).

Market Snapshot: Corporate Debt and Infrastructure Finance

Corporate Debt Spreads – Finance Market Summary

- Yields in the corporate bond market have remained steady in 2017 and spreads continue to tighten. Since the end of 2016, the Fed raised rates twice and could raise them once more before the end of the year. Despite this, 10-year corporate rates across credit categories are down approximately 20 basis points for the year with the exception of the 10-year U.S. treasury, which is roughly where it started the year at 2.44%. Moreover, spreads are currently the lowest they have been in over five years across all credits categories.
- This highly favorable market has led U.S. corporate bond issuances to continue to grow year over year for the sixth consecutive year. Total dollar volume is up 2.3% from September of 2016. High yield issuances have been the primary driver of growth this year, increasing in dollar volume by 13.4%.[1]

Historical Corporate Bond Yields – 10-Year Maturity



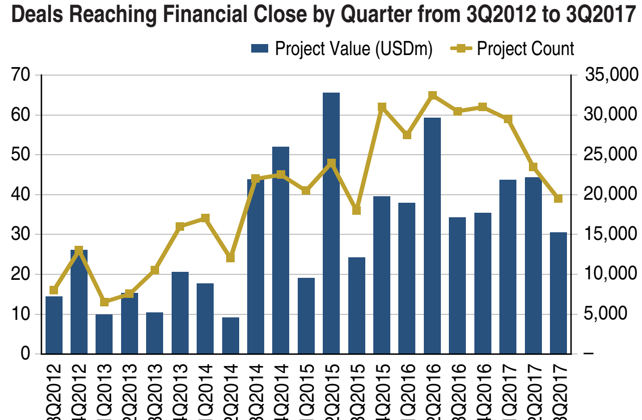
Data as of October 25, 2017.
Source: S&P Global Fixed Income Research.

1 SIFMA.

Infrastructure Finance: U.S. Market Continues to Ebb and Flow

- Private investment in the U.S. infrastructure market has ebbed and flowed over the last five years depending on the availability of direct investment opportunities. Nevertheless, public-private partnerships (P3) have been instrumental in delivering a number of infrastructure projects, with several states and municipalities having used this delivery model, and many more becoming educated on the benefits of the delivery model.
- U.S. infrastructure market activity in 2017 lagged behind 2016 with approximately $59 billion in transactions reaching financial close after three quarters. The drop in project activity comes largely due to a drop-off in greenfield activity, while the brownfield market has been relatively strong. Across greenfield and brownfield transactions, renewables and power assets, followed by transportation, have led the way in terms of activity.
- Future U.S. federal policy decisions around infrastructure, including the outcome of certain proposed revisions in tax policy and the prospects of the $1 trillion infrastructure plan, will influence future P3 activity. However, an increasing number of state and local governments have begun taking steps to make P3s more commonplace for stakeholders.

Deals Reaching Financial Close by Quarter from 3Q2012 to 3Q2017



Graph includes Greenfield, Brownfield and Refinancing transactions.
Source: Inframation.

Featured Mesirow Financial Deals

CAD $40,000,000
Acquisition Financing
Synthetic Credit Structure

7 ELEVEN

Portfolio
(Tenant)

Cross-Border Acquisition Financing for a 7-Eleven Portfolio

Mesirow Financial successfully structured and arranged for a permanent acquisition credit tenant lease (CTL) financing package for a retail portfolio comprised of 11 free-standing convenience stores and fuel stations located in various locations throughout Alberta, Canada. The subject financing represented a portion of a larger portfolio of units recently sold by 7-Eleven to a private equity source. The financing structure, which represented approximately 90% of costs, consisted of a single-secured CTL note with an insured balloon payment due at maturity. This transaction represents the first cross-border and cross-currency CTL financing consummated by Mesirow's CTL group. While the structure of the transaction carried many cases of first impression, some notable complexities of the deal included: (i) implementation of currency derivatives associated with exchange rate risk, (ii) multiple insurance policies underwritten by foreign counterparts, (iii) multiple trustees needed to properly satisfy various legal security and tax withholding matters, and (iv) a borrower organizational structure consisting of various sub-entities and key principals domiciled in different countries. Despite the complexities, Mesirow Financial was able to satisfy the request for high-leverage and tax efficiency.

POHLIG PACKAGING
a company owned by
WestRock
and Management
has been acquired by
OLIVER PRINTING & PACKAGING CO.
a portfolio company of
PFINGSTEN
— Sell-side Advisor —

M&A Sell-side Advisor to Pohlig Packaging

Mesirow Financial acted as the exclusive financial advisor to Pohlig Packaging, a company owned by WestRock Company and Management, on its sale to Oliver Printing & Packaging Co., a portfolio company of Pfingsten Partners, L.L.C. Headquartered in Richmond, VA, Pohlig is a manufacturer of folding cartons, micro-fluted corrugated boxes and setup boxes, serving the food and grocery, consumer products, automotive aftermarket and healthcare markets. Dedicated to environmental stewardship, Pohlig is committed to manufacturing value-added products sourced from sustainable managed forests, along with a balance of renewable and recycled materials. This transaction is yet another example of the strength of Mesirow Financial's relationships with key strategic acquirers in the packaging industry.

CITY OF HUTTO TEXAS

City of Hutto, Texas
$80,070,000
Tax and Waterworks and Sewer System
(Limited Pledge)
Revenue Certificates of Obligation
Series 2017

— Senior Manager —

Senior Managing Underwriter for the City of Hutto, Texas

Mesirow Financial served as senior managing underwriter for the $80,070,000 Certificates of Obligation Series 2017 bonds on behalf of the City of Hutto (the "City"). The Series 2017 bonds were issued to fund the City's acquisition of a private water company to help resolve the City's issue of rising water costs. One of the fastest-growing cities in the country, Hutto's drinking water was supplied by three wholesale water suppliers, each under long-term contracts. Take-or-pay provisions of one of these contracts led to substantial City rate hikes and the highest water rates in the region. The City renegotiated the contract twice, to no avail. Mesirow Financial underwrote nearly half of the bonds offered due to weak market conditions, ensuring the City achieved the lowest possible interest rates. The City has since taken control of the water system, resulting in long-term cost savings for the City and its rate payers. This transaction gave further evidence of Mesirow Financial's banking and underwriting capabilities in the public-private partnership (P3) market.

Capital Markets

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- Fixed Income Sales and Trading
- Public Finance
- Sale-Leaseback Capital
- Structured Debt Products

Investment Banking

Boutique M&A advisor serving the middle-market and providing customized solutions to meet the unique needs of our clients.

About Mesirow Financial
Mesirow Financial is an independent, employee-owned firm founded in 1937. As specialists in investment, risk management and advisory services, we are committed to helping our institutional, corporate and individual clients achieve their objectives. Our professionals are inspired by an entrepreneurial desire to develop tailored solutions designed to deliver measurable results. To learn more, please visit mesirowfinancial.com.

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