CAPITAL MARKETS UPDATE

Middle Market M&A

Q1 2021

CAPSTONE PARTNERS

> ***"Taxes are pulling deals forward from 2022. The specter of increased capital gains taxes on high income individuals and families has undoubtedly prompted many owners, particularly those with a low basis, to rush for the exits in 2021."***

"Busier than We've Ever Been"

Deal market professionals are gasping for air as the pace of new transactions reaches a fevered pitch. We have received breathless reports of two-to-three-month delays for standard transaction services like Quality of Earnings (QoEs) reports and market studies. Who expected that just a year after the outbreak of a deadly pandemic, the U.S. would host an M&A boom for the record books? We should have seen it coming. In 2021, we are trying to shove three years of dealmaking into 12 months. Why? Three reasons:

Firstly – deals from 2020. Prospective sellers of COVID-affected businesses sat on the sidelines in 2020 waiting for trailing twelve-month (TTM) earnings to normalize. With the terrifying Q2 of 2020 sufficiently in the rearview, business owners and their advisors are now emboldened to go to market. Further, the stress and trauma of managing a business through lockdown motivated many family-and founder-owned businesses to embark on sale processes.

Secondly – taxes are pulling deals forward from 2022. The specter of increased capital gains taxes on high income individuals and families has undoubtedly prompted many owners, particularly those with a low basis, to rush for the exits in 2021. We saw this movie before when the U.S. approached the "Fiscal Cliff" of 2012-2013, raising the long-term capital gains rate from 15% to 20%.

Thirdly – the ocean of capital chasing middle market buyouts grows wider and deeper. As a result of the incredible bull run in public equities in the past 12 months, many institutional investors are under-allocated to alternative investment strategies like private equity buyouts and venture capital that don't mark to market every day. Private equity (PE) investors gleefully accept capital commitments on ever-larger investment vehicles and then grumble loudly about asset prices.

Our friend Nadim Malik of SPS by Bain & Co reported: "the median number of deals seen by PE firms in Q4 2020 and Q1 2021 were the highest fourth and first quarters, respectively, since we started tracking the data." We have seen the same and will be holding our breath for the Q2 and Q3 2021 numbers. At Capstone, we will launch a record number of new sale and financing mandates in 2021.

What does this mean for sellers?

1. **Get your deal team together pronto.** Resources are stretched across virtually all service categories. That means longer wait times and higher prices for legal, investment banking, and other services.

2. **Expect buyers to quickly pass on all but the most perfect acquisition candidates.** PE firms are declining to take books on deals they absolutely would have bid on one year ago. As a consequence, bankers are running broader processes for marginal assets. However, paradoxically, for the most sought-after properties, a process with only a handful of buyers will produce a market-clearing result.

3. **Avoid year-end bottlenecks.** For transactions above the current $92 million threshold, the Federal Trade Commission/Department of Justice will almost certainly face a huge backlog of transaction notifications pursuant to the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (HSR). Don't expect any Early Termination from regulators, so purchase agreements need to be signed and documents submitted before Thanksgiving to have a chance to close by year end.

4. **Don't be a price taker.** If we face a tax cliff on December 31st, beware of buyers repricing deals at 11:59pm when they have leverage. Advisors will resist granting exclusivity and aggressively push transaction timelines to get ahead of this.

Long Term Outlook

Taking a step back from the current rapid pace of dealmaking, underlying market dynamics give us a good sense for where transaction activity is headed. We have seen institutional ownership of middle market companies dramatically increase over the past decade. Looking at the numbers, there is no doubt sponsor-backed companies are playing a larger role in the M&A arena. In 2020, 37% of private companies in the middle market were acquired by a PE firm compared to 21% five years ago and 14% 10 years ago. What does this mean for dealmakers? A massive wave of PE exits over the next five to seven years as holding times expire.

The best sponsors differentiate themselves by investing thematically and building vertical expertise. Ten years from now we don't expect to see as many small deal generalists, as LPs have aggressively pushed for strict verticalization or situational investing. Sponsors have an opportunity to carve out a niche for themselves and not just in their sector focus. Private equity that demonstrate a track record of guiding owners through the transition to institutional ownership can set themselves apart in the market.

The past decade has seen a surge in institutional ownership, which we expect to continue into the next decade. The sponsor universe and capital levels have grown dramatically but the focus will remain on how private equity firms drive growth for their portfolio companies and returns for their LPs.

At Capstone, we have the pedal to the metal in our M&A business to position sellers to beat the year-end rush and to discuss long term transition plans for owners and entrepreneurs. We are also helping sellers and investors raise debt capital to fund transactions through our Debt Capital Advisory practice. Also, our Financial Advisory Services Group provides a whole raft of services including quality of earnings reviews, post-merger integration services and interim management solutions to private equity investors. Please reach out to discuss any of these ideas or any transaction-related projects.

Take care of yourself and take care of someone else.

Regards,

Brendan Burke
Managing Director, Head of Sponsor Coverage

MIDDLE MARKET OUTLOOK

Q1 2021 TAKEAWAYS & THEMES

We are pleased to present our Capital Markets Mergers & Acquisitions Update with a look into key trends and statistics over the past quarter.

Middle market M&A activity increased year-over-year as buyers increasingly returned to deal markets:

- Following near-record levels of deal activity in Q4, M&A volume has normalized but remains elevated year-over-year
- Private equity has been a significant driver of deal activity, allocating elevated levels of dry powder to high-growth sectors
- Valuations remain healthy, with deals in the upper middle market experiencing historic average EBITDA multiple growth

M&A volume is expected to increase in 2021, driven by factors including:

- Shifting of 2020 deals to 2021 and acceleration of future deals into 2021 to get ahead of potential tax changes
- Reorganization of many industries in the wake of the pandemic
- Pent up consumer demand driving top line growth as the COVID-19 pandemic fades
- Supportive fiscal and monetary policy creating a favorable transaction environment in 2021
- Historically low cost of capital for deal making, especially for large public companies
- Continued favorable conditions for sponsor activity

For information on the themes and trends discussed in this report, or to find out about Capstone's full suite of integrated services, please contact us.

CAPSTONE PARTNERS

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Q1 2021 BY THE NUMBERS

2.9% ⇧

INCREASE IN DEAL VOLUME

M&A volume increased 2.9% year-over-year as pent-up demand and potential near term tax implications have fueled transaction activity

4.0x ⇧

AVERAGE DEBT MULTIPLE

Debt financing has returned to pre-COVID levels with the average total debt multiple increasing to 4.0x

8.9x ⇧

EBITDA MULTIPLE, $10-$100MM

Valuations in the lower middle market have appreciated year-over-year, rising to an average of 8.9x from 8.1x

10.6% ⇧

INCREASE IN PE TRANSACTIONS

Total closed transactions by private equity increased 10.6% year-over-year, although remained below Q4 levels

$62.0M ⇧

PRIVATE COMPANY DEAL VALUE

Average deal value for acquisitions by private companies increased 4.3% year-over-year to $62 million

15.6% ⇧

DEALS BY FOREIGN BUYERS

Cross-border deal activity increased substantially year-over-year with foreign buyers accounting for 15.6% of deals

28% ⇩

PE PLATFORM INVESTMENTS

Private equity platform investments declined 28% year-over-year, while add-on acquisitions continue to proliferate

$45.2B ⇩

PRIVATE EQUITY FUNDRAISING

Private equity fundraising increased from the prior quarter but remains lower year-over-year at $45.2 billion

6.8x ⇩

PE EBITDA MULTIPLE PAID

EBITDA multiples paid by private equity firms declined in Q1, although valuations have rewarded top financial performers

CAPITAL MARKET DASHBOARD

YTD EQUITIES

S&P 500
+12.35%

Last	1Y %	P/E LTM
4,192.9	+36.4	27.1

Dow Jones Industrial
+13.96%

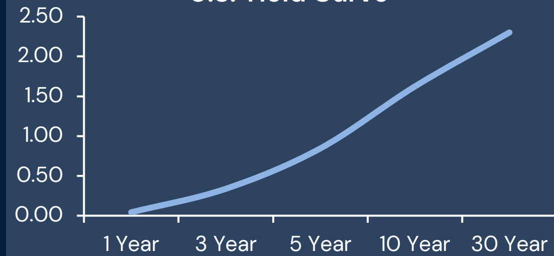
Last	1Y %	P/E LTM
34,577.0	+34.3	23.8

NASDAQ
+5.95%

Last	1Y %	P/E LTM
13,806.9	+41.7	40.5

FIXED INCOME

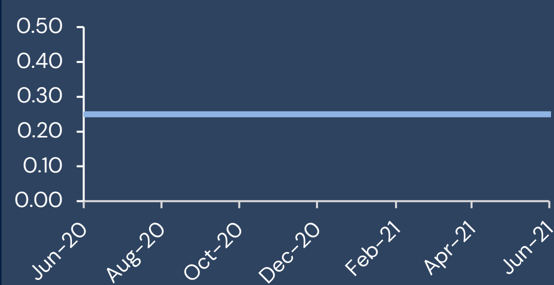
U.S. Yield Curve



1Y	3Y	5Y	10Y	30Y
0.040	0.335	0.843	1.622	2.300

POLICY RATE

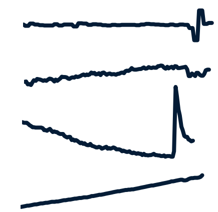
Federal Funds Target Rate



ECONOMIC INDICATORS

GDP, LABOR MARKET, & INFLATION

	Last	YOY
GDP	*6.4%*	*+11.4%*
Consumer Confidence	*117.2*	*+36.4%*
Unemployment	*6.1%*	*-8.7%*
Consumer Price Index	*273.7*	*+3.0%*



HOUSING MARKET

Housing Starts	*$1,569.0*	*+67.3%*
Total Construction	*$1,524.2*	*+9.8%*

PMI & NMI

Purchasing Managers	*61.2%*	*+18.1%*
Non-Manufacturing	*64.0%*	*+18.6%*

RETAIL

Retail Sales	*$619.9*	*+51.2%*

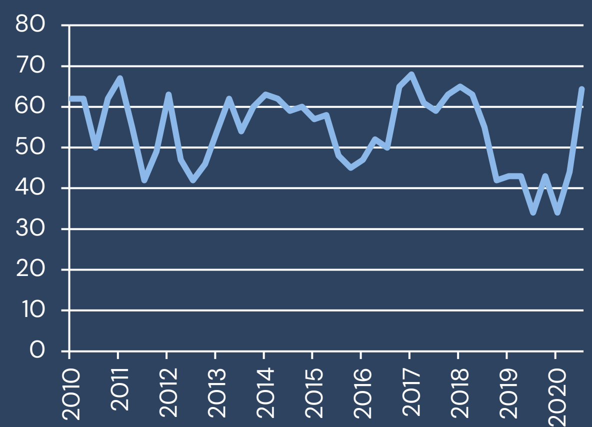
Source: FactSet as of 6/3/2021

CORPORATE DASHBOARD

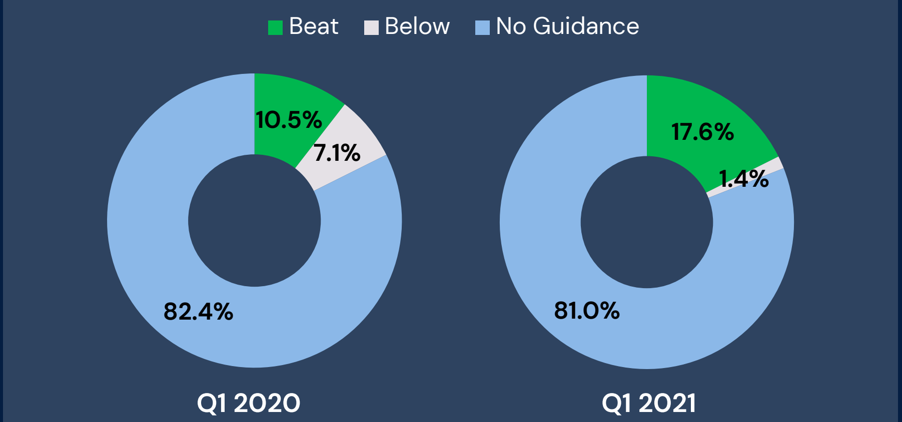
CEO CONFIDENCE

"CEOs across industries continue to adapt to COVID-19's new normal. While Q4 saw a resurgence of optimism, leaders are also cognizant of—and planning for—what may be permanent shifts in consumer preferences and organizational expectations ahead."

– Robert Ferguson, Jr., Trustee, The Conference Board, Vice Chairman, The Business Council

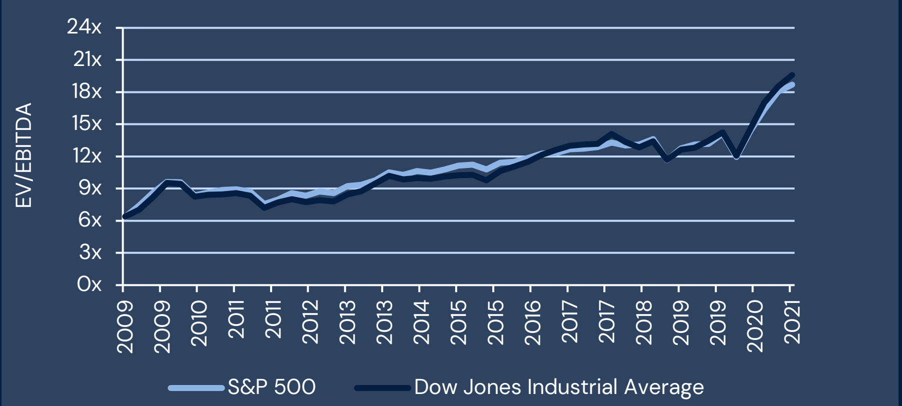


S&P 500 EARNINGS PERFORMANCE



NFIB PRIVATE BUSINESS EXPECTATIONS

S&P 500 VS. DJIA EBITDA MULTIPLES



LEVERAGED FINANCE CONDITIONS

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Key Market Stats

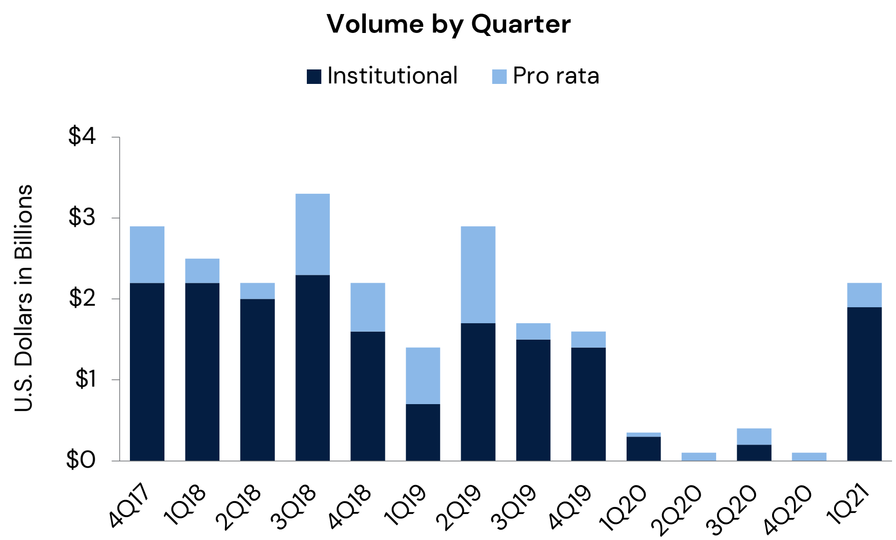
- **Volume surged in the first quarter to $2.2 billion.** This was the highest quarterly total since Q3 2019 as pent-up demand was buttressed by the sense that a return to normalcy was on the horizon. Healthcare led the way, accounting for 30% of volume; interestingly, Retail and Gaming & Hotel, two sectors that were all but banished by lenders throughout the pandemic, combined to represent ~36%. Refinancing and leveraged buyouts (LBOs) represented nearly 70% of total volume with dividends (17.6%) and mergers (12.6%) accounting for the remaining balance.

- **Leverage reached levels reminiscent of the halcyon days of 2007.** Senior and total leverage for middle market (MM) LBOs hit 5.7x and 6.1x, respectively. In particular, the senior multiple is the highest reading since 2018. This isn't entirely surprising, given the lofty valuation multiples being seen in the (M&A) market. As such, loan-to-value has taken front-and-center in lenders' underwriting decisions and equity contributions of 35-50% remain the norm.

- **Pricing remained stable relative to Q4**. Average spreads held in the 500-515 context, with a 99 original issue discount (OID) and 6.26% average yields. With limited market data in Q2 and Q3 of 2020, it's challenging to draw a longer-term trend, however, we expect to see yield compression in the months ahead. Since the end of Q1, pricing and yields have held firm.

- **Default rates declined precipitously.** After peaking at 4.64% in September, Q1 default rates declined 42% to 2.67%, in yet another sign of the market's recovery and the positive outlook for 2021. That said, excluding the 2020 spike, the default rate remains at its highest level since 2016.

- As further discussed below, many factors contributed to the frothy market including red-hot lender demand combined with a shortage of attractive new-issue opportunities leading to a technical imbalance.



Source: S&P Global Market Intelligence

LEVERAGED FINANCE CONDITIONS (CONTINUED)

Quarterly Market Observations

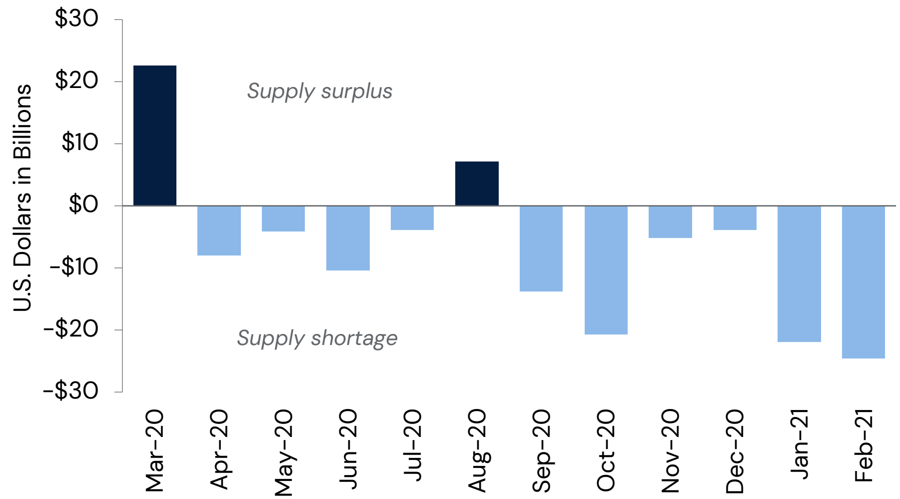
- **Direct Lending continues to dominate**. The Private Credit market has grown exponentially over the past decade and that trajectory is certain to continue. As of mid-January, there were 266 direct lending funds in market seeking to raise $150 billion of capital commitments. Comparatively, the previous high-water mark was in 2017 when 100 funds with a direct lending mandate were fundraising. The driver of this spike is clear - in a world where monetary stimulus has pushed global interest rates ever lower, direct lending provides investors with significantly more attractive risk-adjusted returns than other fixed-income alternatives.

- **Repayments…they are a coming.** Direct lenders are witnessing the beginning stages of a repayment wave, which will serve to further enhance market conditions for borrowers. Beyond the traditional reasons – opportunistic refinancings, bond-for-loan take-outs, syndicated deals, etc. – the scale and velocity of special purpose acquisition company (SPAC) formation has presented another competitive challenge for fund managers looking to deploy capital. **It took slightly more than two months this year to break the annual record for new SPAC listings – 227 - which was set last year.**

- **So, what does this all mean?** Extremely borrower-friendly market conditions for the foreseeable future. In our view, the combination of the technical imbalance as depicted to the right, continued gains in the number of vaccinated Americans and concomitant economic recovery across sectors points to a very strong 2021 for leveraged finance participants.

- **It's a great time to be a borrower.** We strongly recommend that companies and sponsors with financing needs in the next 24 months capitalize on the current environment and address those needs today.

Supply vs. Investor Demand



Source: S&P Global Market Intelligence

DEBT ADVISORY SERVICES GROUP

Capstone's Debt Advisory Services Group helps privately-owned and sponsor-backed companies secure debt capital for organic growth, acquisitions, dividend recapitalizations and refinancing. The team works closely with clients to optimize their debt structures and secure the best long-term institutional partners for their business.

FINANCIAL ADVISORY SERVICES: POST-MERGER INTEGRATION

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Maximizing Transaction Value

The success of a transaction and the optimization of returns on an acquisition depend on many factors. Acquirers and their advisors have quantifiable financial goals top of mind during the deal process, but they can sometimes underestimate other factors that can have an enormous impact – either positive or negative, depending on how they are managed – on the final outcome.

Integrating two different organizations during a transaction and having the resulting entity be more than the sum of its parts is more complicated than just combining IT, accounting, sales, and operational platforms. Most middle-market businesses are dynamic, people-driven organizations. Some even depend on the contributions of people who might be irreplaceable in the short term. They may have processes that are hardwired into their businesses, making it difficult to adopt new systems post-transaction. This is why, in addition to technical considerations, a successful merger integration plan must always consider the skill sets and culture of the combining organizations.

The best integration plan involves key people from both companies, as well as any investors, working collaboratively to identify and quantify synergies, define key milestones, set goals and accountabilities, and communicate progress to their respective organizations as well as capture feedback through regular surveys during and after the transaction. We also strongly recommend working with a professional merger integration consultant even if members of the company or investment firm have extensive experience with M&A transactions. This ties back into the cultural factor – even leaders that are enthusiastic about a merger are still human. A professional integration team can be a neutral voice to help overcome any personality issues or perceptions of bias, and to ensure the efficiency and integrity of the process.

Since preparation is key to value creation, the integration process should ideally start about the time the LOI (Letter of Intent) is signed. This does not mean, however, that an advisor can't assist you later if the process is proving to be more challenging than expected – it's never too early, but it's also never too late. We've even helped clients that have gone through the process on their own only to realize that their post-transaction operations were suffering from the effects of unresolved integration issues.

A robust, comprehensive merger integration process can help ensure a smooth and productive operational transition. It can lay the groundwork for ongoing communications in the new entity, build credibility with leaders and employees, leverage synergies across the two organizations, and contribute directly to the value of the transaction.

FINANCIAL ADVISORY SERVICES (CONTINUED)

Post Merger Integration Case Study

SITUATION
- The client, a private equity-owned distribution company, made three add-on acquisitions in short succession.
- A lack of planning and poor communication on the part of the leadership team at the company led to ineffective integration of the acquired companies with the parent company.
- Consolidation of functions created gaps throughout the order-to-cash process.
- The company suffered from improper order taking, inventory management issues, customer frustrations, collections disruptions, and financial and management reporting problems.

SOLUTION
- After assessing the situation, a PMO (Project Management Office) was created to map the order-to-cash process, determine where integration issues created problems, and to identify and implement the appropriate solutions.
- The PMO created procedures to harmonize order entry and fulfillment process and complete warehouse consolidations and developed KPI (Key Performance Indicators) and financial reporting tools to provide real-time information on the consolidated organization and make the financial reporting process more accurate and efficient.

RESULT
- The company was able to return to same day order fulfillment and accurately track inventory.
- They implemented processes to ensure accuracy of invoicing and collections, bringing DSO (Days Sales Outstanding) back to normalized levels.

FINANCIAL ADVISORY SERVICES OVERVIEW

Capstone's FAS Group specializes in enterprise-wide solutions aimed at performance improvement and increased shareholder value, including:

TRANSACTION ADVISORY AND INTERIM MANAGEMENT
- Sell-side Readiness
- Financial and Operational Due Diligence
- Quality of Earnings Review
- Integration Consulting and Post-merger Integration
- Field Examination

MANAGEMENT CONSULTING
- Business Performance Improvement
- Project Management
- Accounting & Audit Support
- Public Company Readiness and Public-to-Private Planning

SPECIAL SITUATIONS INVESTMENT BANKING
- Strategic Alternatives and Contingency Planning
- Buy- and Sell-Side Distressed M&A
- Debt & Equity Capital Markets
- Balance Sheet Restructuring

TURNAROUND AND RESTRUCTURING ADVISORY
- Turnaround Consulting
- Crisis Management
- Debtor & Creditor Advisor Services
- Court-appointed Receiver and Chief Restructuring Officer

INSOLVENCY
- Debtor and Creditor Representation Services
- Chapter 11 and Chapter 7 Services
- Section 363 Asset Sale

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Aerospace, Defense & Government M&A Trends

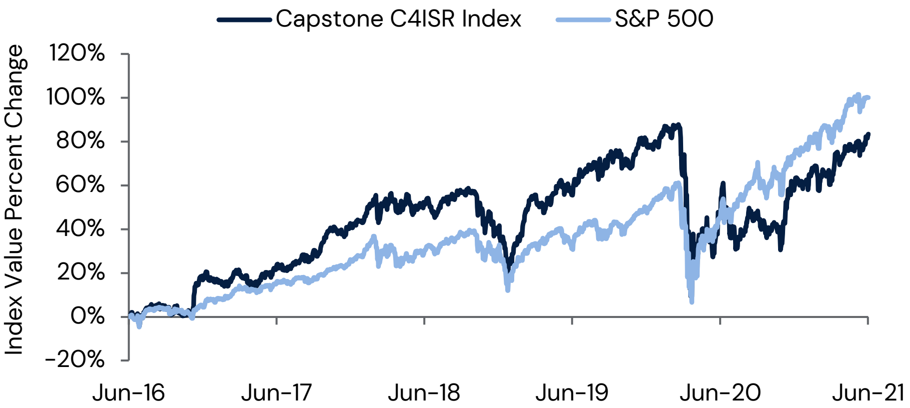
Overview – The number of Aerospace, & Defense (A&D) transactions fell 32% in 2020, higher than the 13% decline in M&A across all industries in North America, due to declining profitability in commercial aerospace. The total value of disclosed Aerospace, Defense, Government & Security (ADGS) transactions was even more pronounced, down 85% compared to a 37% decline across all industries. The number of transactions greater than $1 billion fell to seven from 17 and total value was $22 billion versus $171 billion in 2019, with a five-year average of $71 billion. This highlights not only the 2020 decline, but also the number of large transactions in 2019. Valuation multiples in private transactions remained strong falling by about one turn of EBITDA across A&D deals.

C4ISR Spotlight – Command, Control, Communications, Computers, Intelligence, Surveillance, and Reconnaissance (C4ISR) continues to serve as primary "enabling technologies" across military air/land/sea/space platforms and the joint networks that allow for interoperability across these mission critical systems. Many C4ISR companies were deemed essential at the onset of the pandemic and The Defense Production Act further buoyed the sector by authorizing federal loans and prioritizing government contracts to ensure continuity of supply.

In late May, President Biden released a $6 trillion Fiscal Year (FY) 2022 federal budget, with a flat Pentagon budget of $715 billion, a funding shift from legacy systems to nuclear arsenal modernization, while also developing future warfare technology (e.g., hypersonics, AI [artificial intelligence], cyber). It includes the largest research funding in Pentagon history of $112 billion, up 5.1% from FY 2021.

C4ISR M&A deal volume has climbed annually as the sector continues to play a crucial role in the National Defense Strategy. In Q1 2021, M&A activity increased 33% year-over-year (YOY) with 32 announced or closed transactions. This followed a 15% YOY increase in deal volume from 2019 to 2020. Private equity firms equipped with historic levels of dry powder have accounted for a growing share of M&A deals, attracted the industry's recession resilient nature. Notably, this included private equity firm AE Industrial Partners' newly formed Redwire space-focused platform, which is expected to go public via a $615 million SPAC merger with Genesis Park Acquisition Corporation (NYSE: GNPK).

Capstone's C4ISR Index vs. S&P 500 Market Index



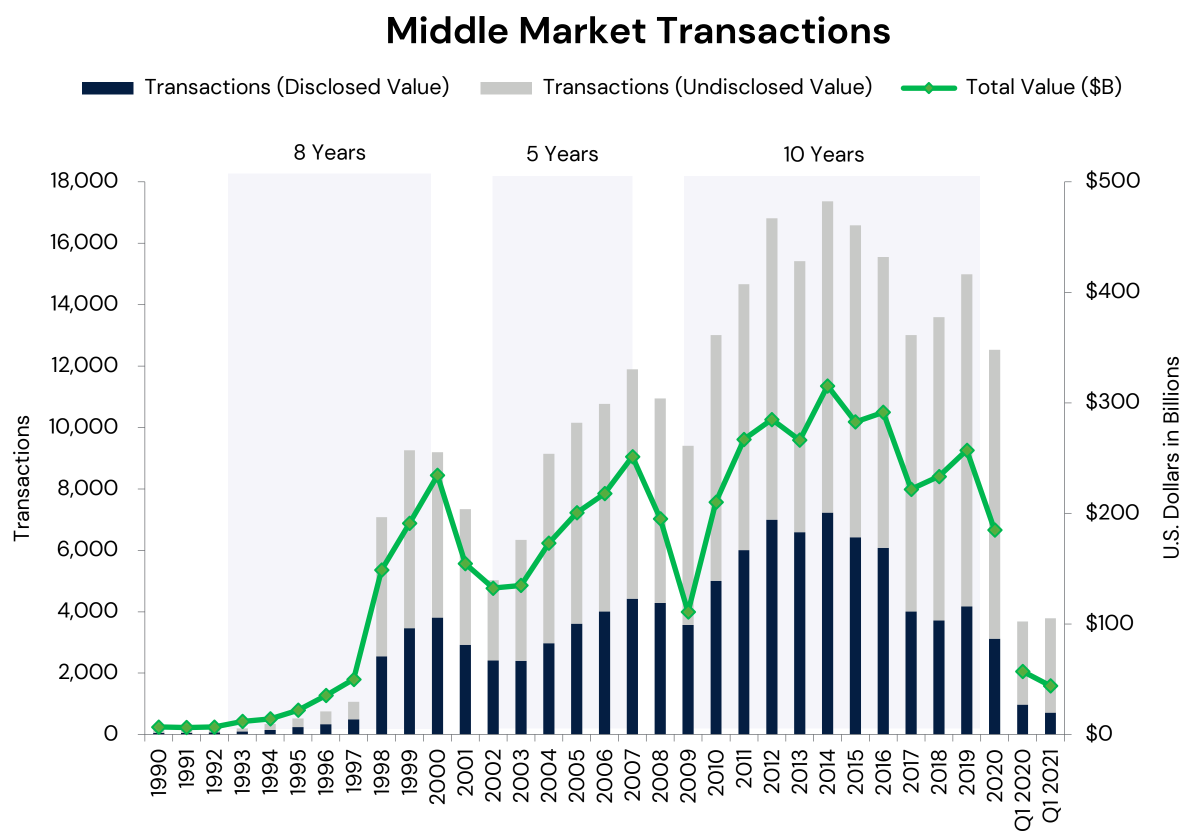
Index includes: ACM, BAH, CACI, DXC, ESLT, GD, HXL, ICFI, J, LDOS, LHX, LMT, MANT, NOC, RTX, SAIC, SPR, TDG, VEC, VSAT, VSEC
Source: Capital IQ and Capstone Research

MIDDLE MARKET M&A ACTIVITY

M&A AMID ECONOMIC CYCLES

M&A VOLUME INCREASES 2.9% YEAR-OVER-YEAR

- Total transaction volume increased 2.9% in Q1 2021 compared to Q1 2020. Aggregate deal value fell to $44.1 billion, marking a year-over-year decline of 23%.
- The pandemic has uncovered vulnerabilities within many businesses, with M&A serving as a valuable tool to address gaps and strengthen supply chains, product diversification, and digital capabilities.
- The reemergence of battered sectors during COVID-19, cheap access to capital, and business model changes are expected to be key drivers of M&A activity in 2021.



Note: Shaded areas indicate expansion
Source: Capital IQ
Enterprise Value < $500mm

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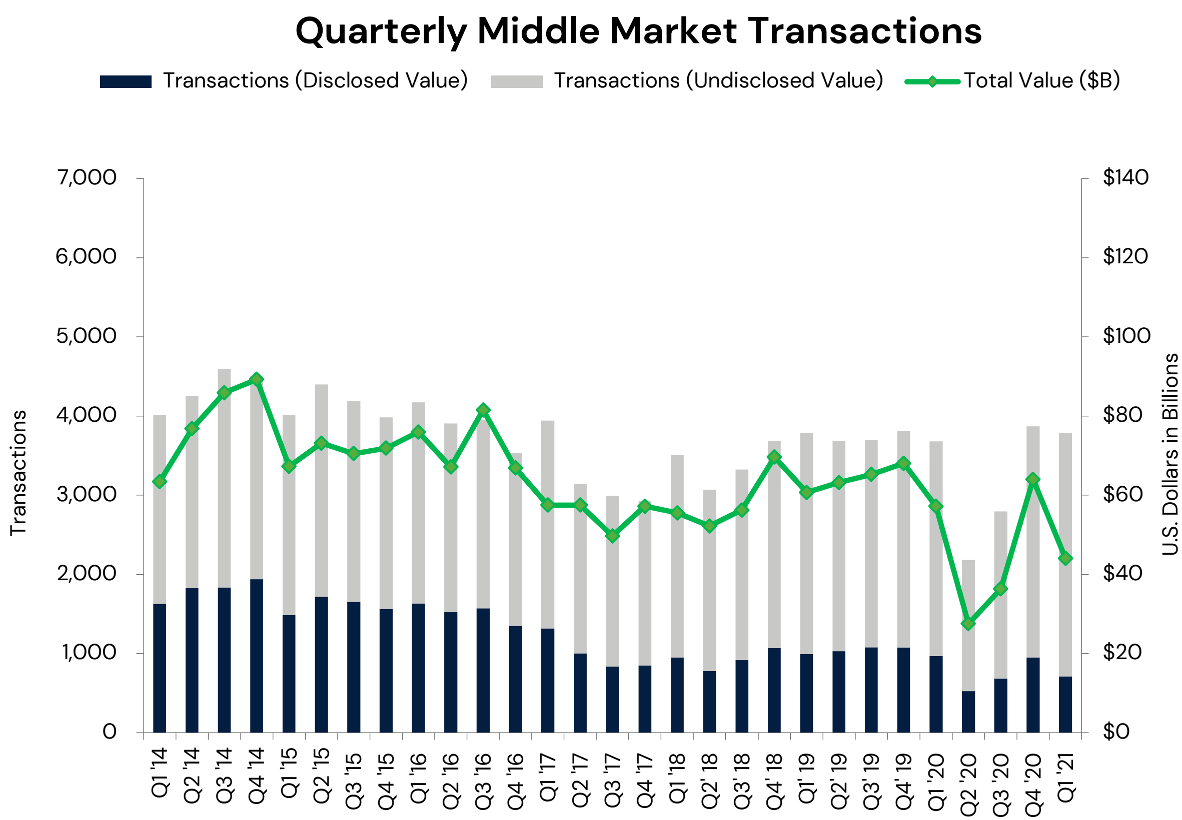
QUARTERLY M&A VOLUME

M&A VOLUME NORMALIZES FOLLOWING AN ACTIVE Q4

- M&A volume declined 2.2% compared to Q4 which likely indicates a normalization of activity in the market rather than a lack of demand. Q4 recorded the highest quarterly volume since Q1 2017, largely driven by the resumption of many deals placed on hold early in 2020.

- Average transaction value fell quarter-over-quarter, amounting to $61.9 million compared to $67.4 million.

- Potential tax increases under the Biden administration are expected to drive a robust pipeline of deal activity in the next 12 months as many business owners look to expedite their exit timeline.



Source: Capital IQ
Enterprise Value < $500mm

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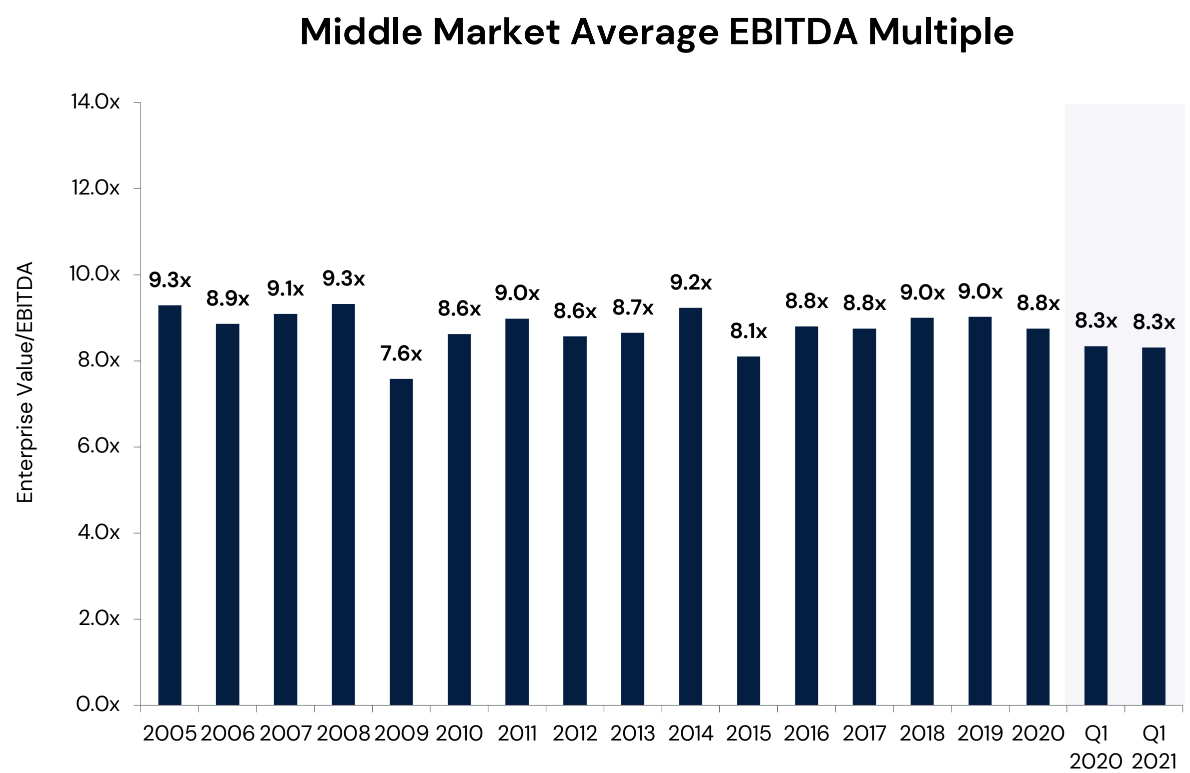
PRICING TRENDS

AVERAGE EBITDA MULTIPLE MEETS PRIOR YEAR LEVEL

- The average EBITDA multiple in Q1 mirrored year-over-year levels at 8.3x, although the average declined from the previous quarter's elevated multiple of 9.6x.
- In line with historic trends, private strategic buyers paid heightened multiples to complete deals in Q1, compared to private equity which paid lower than the market average.
- Increased competition in deal markets is expected to drive strong pricing for quality assets in the near-term as pent-up demand is forecast to fuel strong M&A participation.



Source: Capital IQ
Includes multiples 3x-16x
Enterprise Value < $500mm

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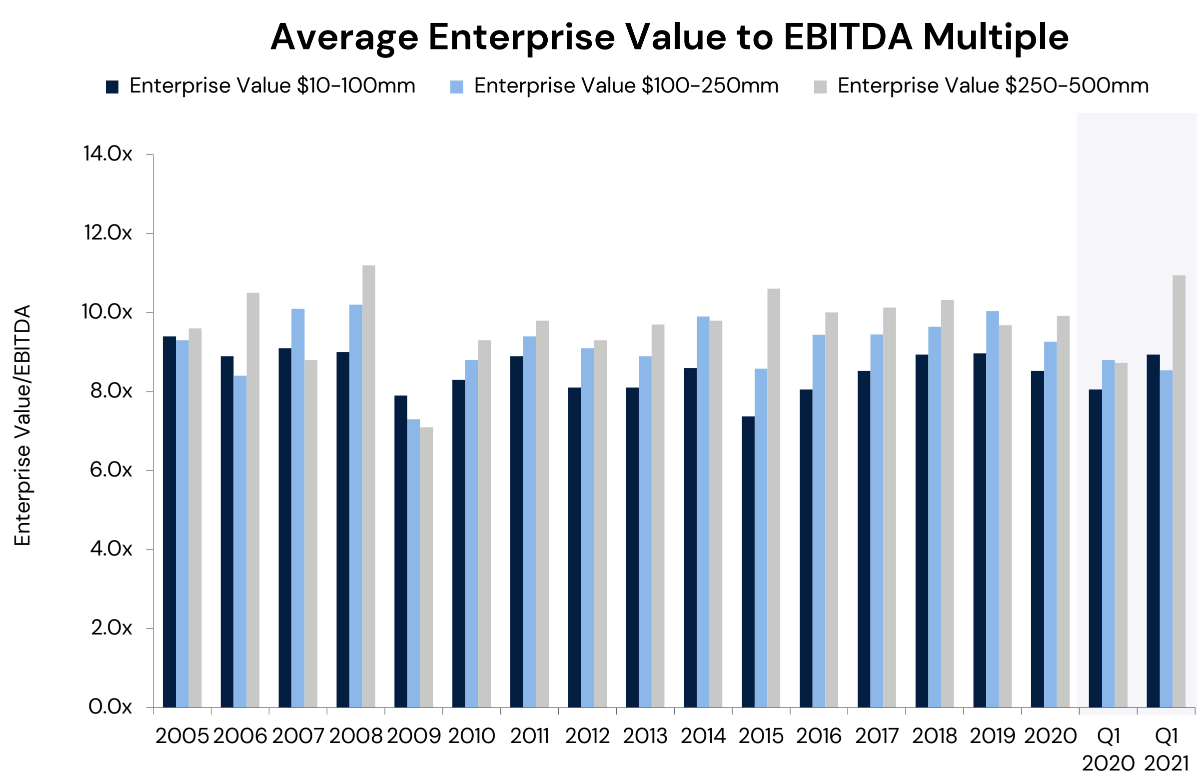
BREAKING IT DOWN BY SIZE

LARGER DEALS CONTINUE TO ATTRACT HIGH MULTIPLES

- Transactions in the $10-$100mm and $250-$500mm market segments experienced year-over-year increases in average multiples at 8.9x and 11.0x, respectively. The $100-$250mm market declined to 8.5x in Q1 2021 from 8.8x in Q4.
- The $250-500mm market recorded an increase in average multiple compared to the prior quarter as buyers continued to pay premium valuations for large assets with scale and market share.
- Targets lacking significant industry penetration and revenue growth have struggled to attract heightened multiples through Q1.



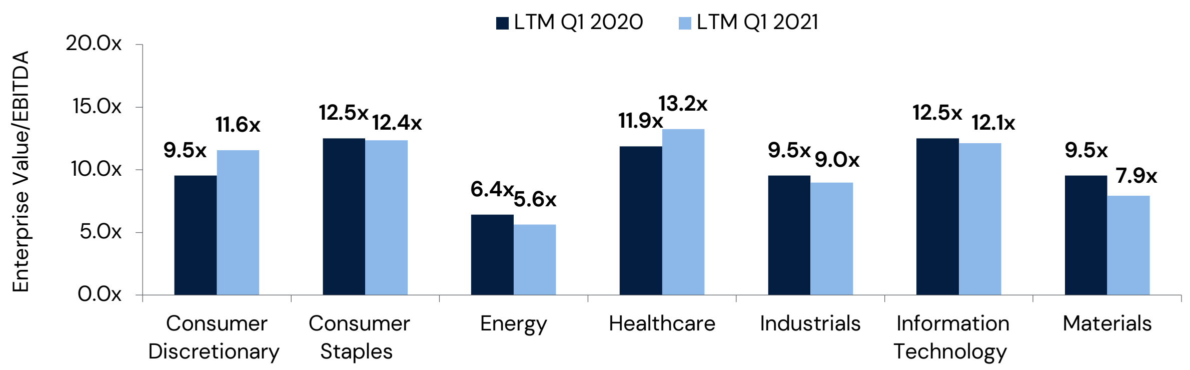
Source: Capital IQ
Includes multiples 3x-16x

BREAKING IT DOWN BY SECTOR

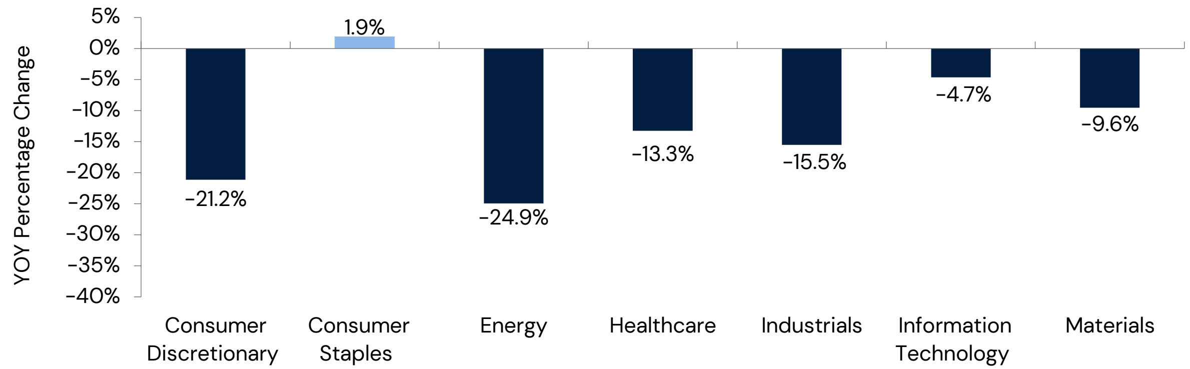
HEALTHCARE CONTINUES TO ATTRACT HIGH VALUATIONS

- The Healthcare sector has continued to attract premium valuations with the average multiple reaching 13.2x. Clinical and contract research organizations and healthcare technology providers have garnered heightened valuations, with several deals closing above 18x EBITDA.
- Pricing in the Consumer Discretionary sector also demonstrated growth, rising to 11.6x, as subsectors such as Outdoor Recreation have capitalized on demand for outdoor and active lifestyle pursuits amid the pandemic.
- The Consumer Staples sector registered the only increase in deal volume year-over-year.

LTM Average EBITDA Multiple by Sector



LTM Transactions by Sector



Source: Capital IQ
Includes multiples 3x-30x; Enterprise Value < $500mm

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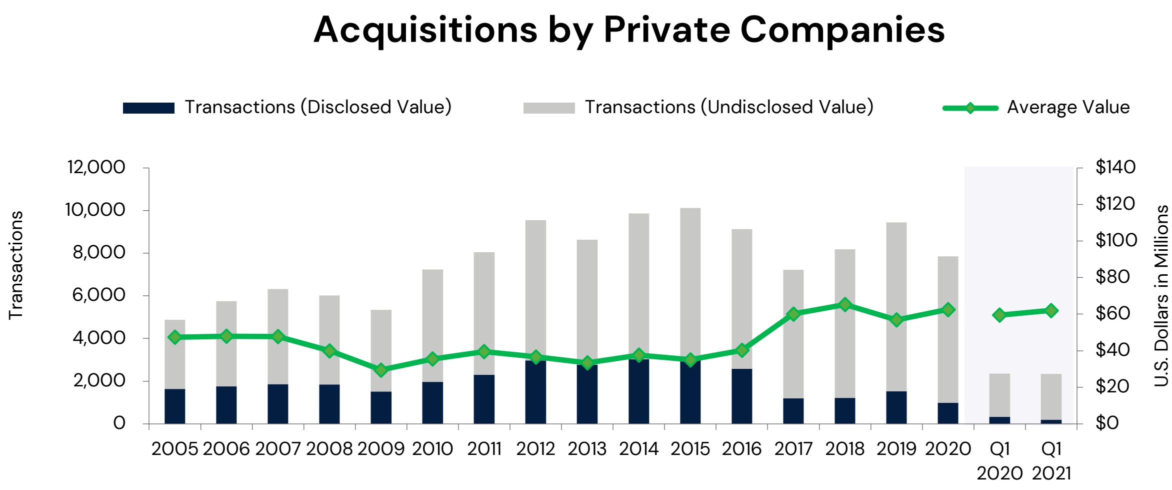
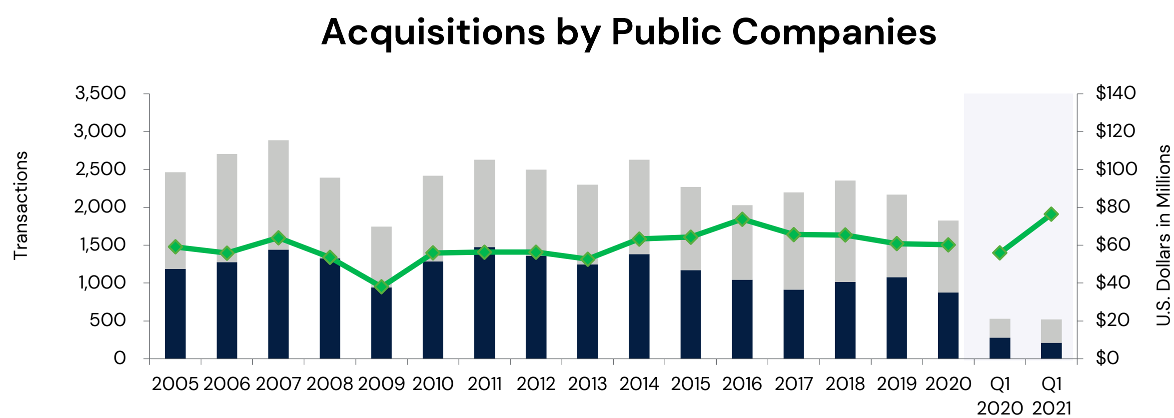
STRATEGIC ACQUIRERS

AVERAGE DEAL VALUE INCREASES FOR STRATEGICS

- Private company acquisitions have declined 1.2% year-over-year although average deal value increased slightly to $62 million. Total closed transactions declined 5.7% compared to Q4.
- Public company acquisitions declined 1.3% year-over-year and fell 2.6% compared to Q4. However, average deal value increased substantially compared to the prior year quarter, rising nearly 37%.
- Potential interest rate increases and rising inflation will be carefully monitored by deal makers, having benefited from a historically low-rate macroeconomic environment in recent years.





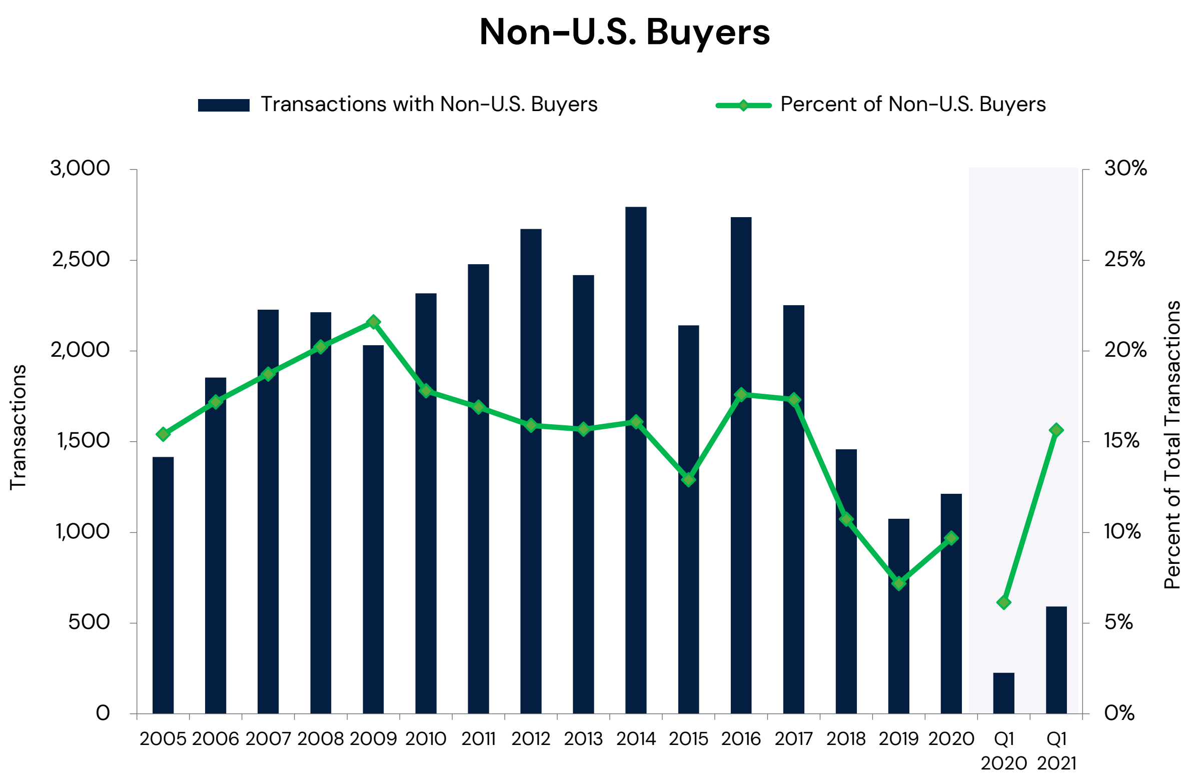
Source: Capital IQ
Enterprise Value < $500mm

CAPSTONE PARTNERS

FOREIGN ACQUIRERS

CROSS-BORDER DEAL ACTIVITY IMPROVES

- Non-U.S. buyers accounted for 15.6% of total transactions in Q1, the highest level since 2017. The United Kingdom has been the most active acquirer of U.S.-based targets through Q1, followed by France and Germany.
- Software providers with recurring revenue streams, asset-light business models, and strong consumer bases proved to be especially attractive targets, according to Capstone's AppDev & Deployment Industry Update.
- Foreign relations and the regulatory environment will remain key factors in cross-border transactions throughout 2021.



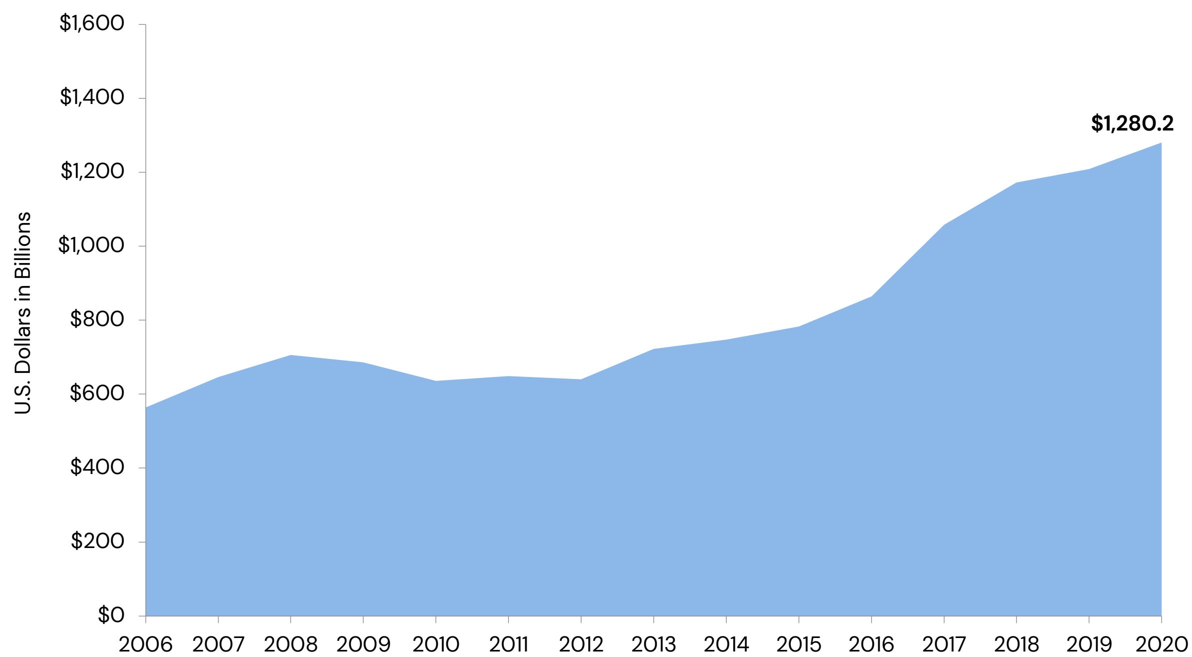
Source: Capital IQ
Enterprise Value < $500mm

PRIVATE EQUITY DRY POWDER

DRY POWDER LEVELS REMAIN FAVORABLE FOR PE DEALS

- Capital overhang, or equity that private equity (PE) firms need to deploy into investment opportunities, has surged since the Great Recession and reached historic levels in 2020, approaching $1.3 trillion.
- PE firms supported portfolio companies amid the height of the pandemic, providing cash to keep operations afloat and generating cost-saving solutions.
- Prospective deal flow has been rampant through Q1 2021, which has led to increased selectivity among many private equity firms, choosing to pursue quality companies with favorable growth prospects and strong management teams over "story" deals.

PE Capital Overhang by Year



Source: PitchBook

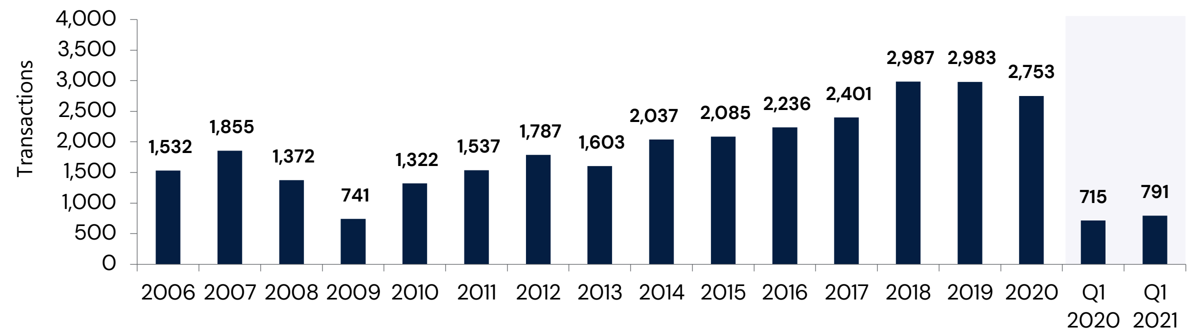
CAPSTONE PARTNERS

PRIVATE EQUITY ACTIVITY

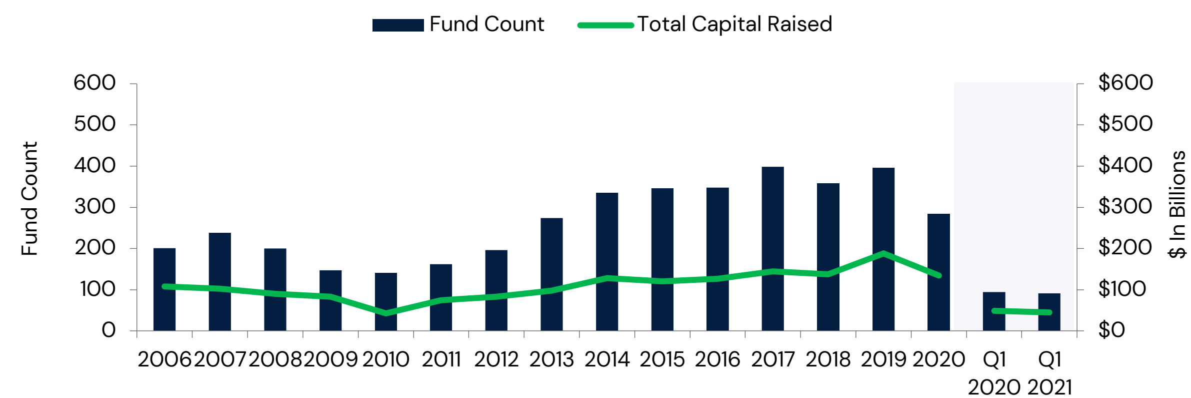
PE CLOSED TRANSACTIONS INCREASE YEAR-OVER-YEAR

- PE middle market deal activity increased 10.6% in Q1 year-over-year. However, deal volume failed to match the rapid pace experienced in Q4, with transaction volume falling nearly 24%.
- PE deal activity has normalized following a record Q4, however sponsors anticipate pent-up demand and potential tax increases to provide a healthy backdrop for deal activity.
- PE fundraising increased from the prior quarter to $45.2 billion in Q1 but remains slightly lower year-over-year. Increased adoption of remote due diligence has likely driven some of the gains in fundraising activity.

Middle Market Transactions Closed by Private Equity Firms



Middle Market Fundraising by Private Equity Firms



Source: PitchBook
Note: EV; $25-$500mm, Fund size < $5B

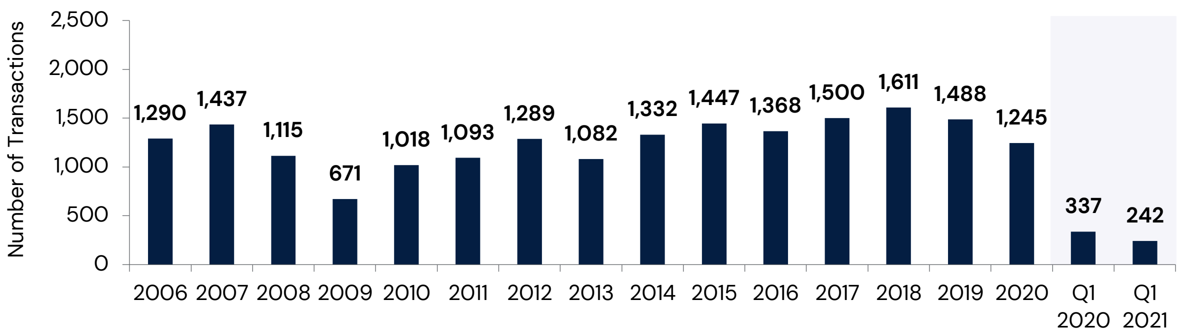
CAPSTONE PARTNERS

PRIVATE EQUITY TRANSACTION TYPES

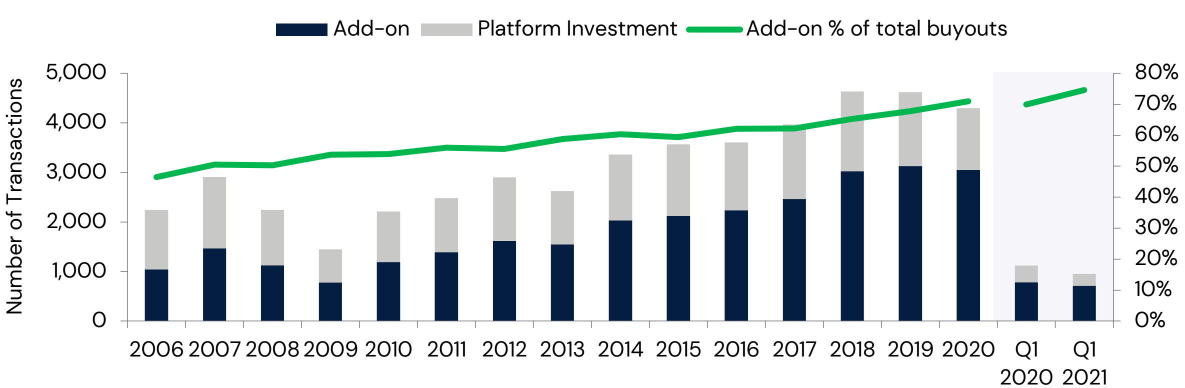
ADD-ONS REMAIN ELEVATED, PLATFORMS FALL

- Platform investment volume declined 28% year-over-year, and fell over 47% compared to the prior quarter. Deal making is expected to increase as sponsors look to deploy capital to high growth sectors.
- Inflation concerns may also bring increased allocation to countercyclical industries as PE look to bolster portfolio defensibility and hedge risk.
- Sponsors have continued to pursue buy-and-build strategies to drive premium multiples upon exit. Add-on acquisitions accounted for 75% of total buyouts in Q1, surpassing prior year levels.

PE Platform Investments



PE Add-On Acquisitions



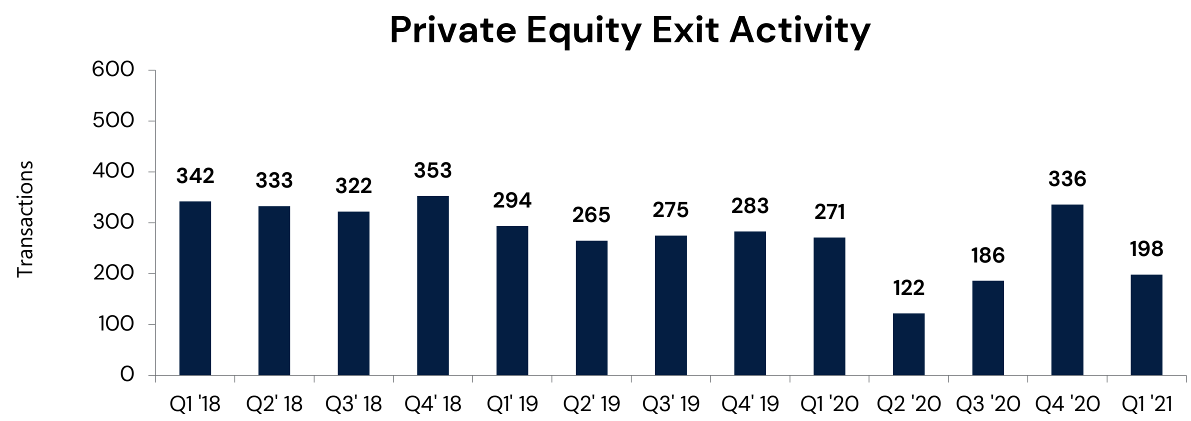
Source: PitchBook
Note: Includes all U.S. PE transactions

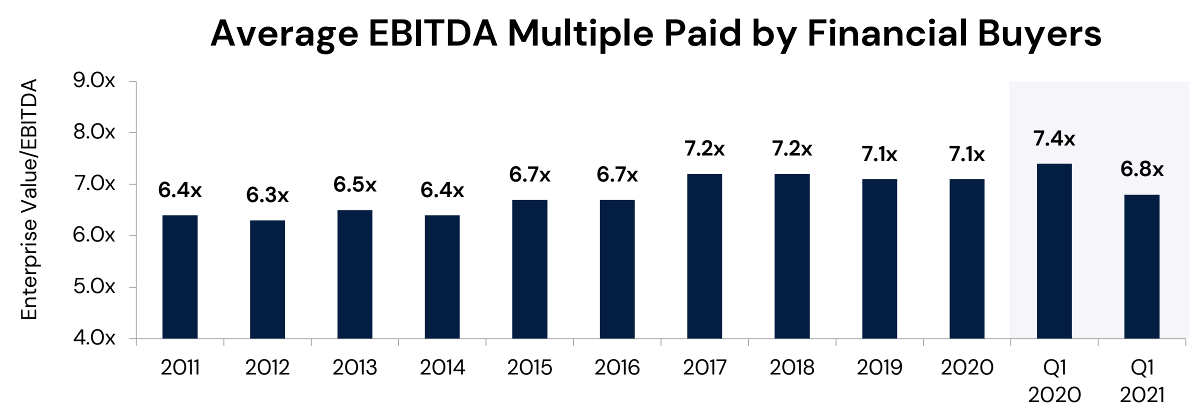
CAPSTONE PARTNERS

PRIVATE EQUITY ACTIVITY

PRIVATE EQUITY EXITS NORMALIZE IN Q1

- PE exit activity provides significant insight to sponsors' view of market conditions. While many awaited pricing transparency in Q2 and Q3 to avoid selling at discounted valuations, sponsors drastically increased exit activity in Q4 with pace normalizing in Q1 2021.
- EBITDA multiples paid by private equity declined year-over-year to 6.8x. Seller financing or earnouts have been increasingly utilized, placing downward pressure on valuations.
- Sponsors are expected to continue to build sector-focused portfolios, with heightened competition for high-quality businesses.





Note: Exit activity inclusive of all enterprise value ranges
Source: PitchBook and GF Data®

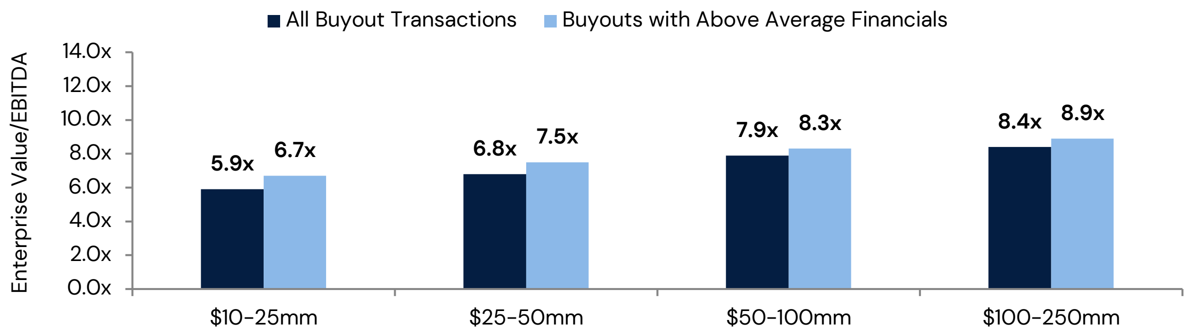
CAPSTONE PARTNERS

PRIVATE EQUITY VALUATIONS

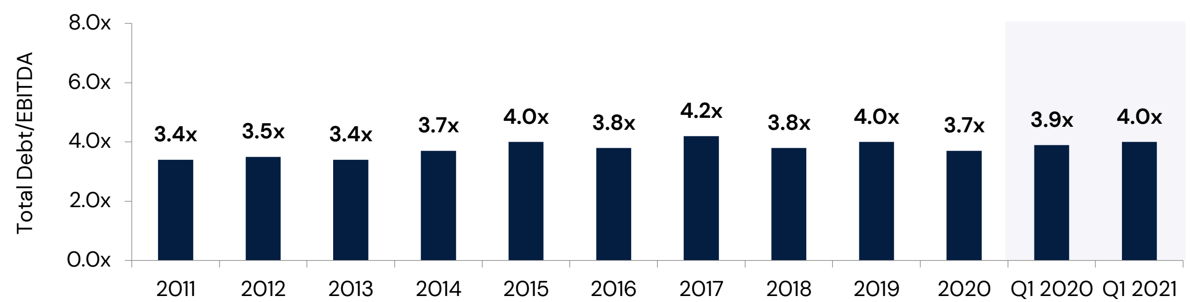
DEBT MARKETS RETURN TO PRE-COVID LEVELS

- Above average financial performers have attracted premium multiples from PE buyers, especially at the lower middle market levels. Sellers in the $10-$25mm and $25-$50mm range have closed at valuation premiums of 14% and 10%, respectively.
- Debt availability has returned to pre-COVID levels, with the average total debt multiple reaching 4.0x, with senior debt improving to 3.7x.
- Business owners and sponsors with financing needs in the next 24 months are forecast to take advantage of the current lending environment.

All Buyouts vs. Above Average Financials



Average Debt Multiple of Middle Market LBO Transactions



Source: GF Data®
GF Data® defines Above Average Financial Performers as businesses with TTM EBITDA margins and revenue growth above 10%, or one above 12% and the other metric at least 8%
Includes multiples 3x-15x; Enterprise Value $10mm-$250mm

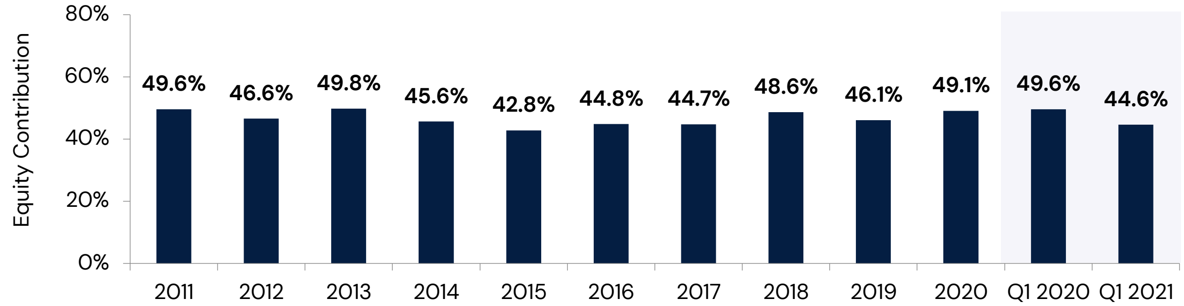
CAPSTONE PARTNERS

PRIVATE EQUITY VALUATIONS

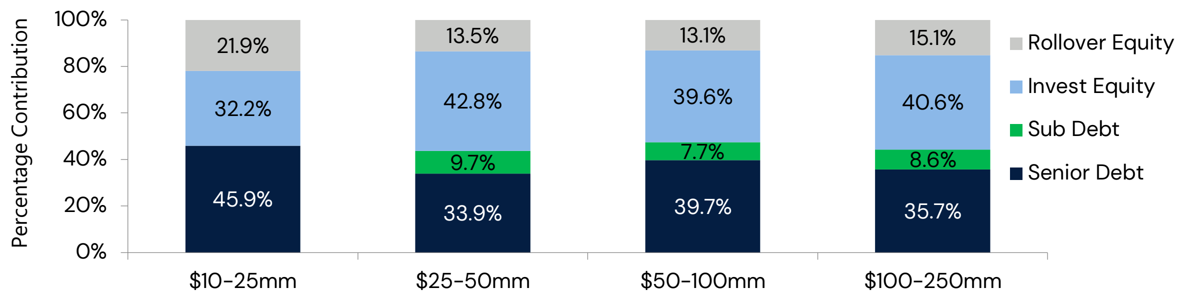
EQUITY CONTRIBUTION DECLINES YEAR-OVER-YEAR

- Increased debt utilization has fueled lower equity contributions through Q1 2021 which amounted to 44.6%, marking the lowest composition since 2015. In platform deals alone, overall equity contribution has declined to more normalized levels, falling to 53.7% in 2021.
- Smaller platform deals, in the $10-$25mm enterprise value range, utilized the largest percentage of senior debt at nearly 46%. Transactions in the $50-$100mm range employed the most overall debt at 47%.
- Platform deals in the $100-$250mm range have used the largest percentage of equity at 55.7% through Q1.

Average Middle Market LBO Equity Contribution



Equity and Debt Contribution by Enterprise Value



Source: GF Data®
Includes multiples 3x-15x; Enterprise Value $10mm-$250mm

CAPSTONE PARTNERS

CAPSTONE BAROMETERS

CAPSTONE PARTNERS' FULLY INTEGRATED EXPERTISE

We have developed a service delivery model that can address the needs of any client situation, supported by vast internal resources. These capabilities are delivered together with deep domain expertise across 12 dedicated industry groups with an established, real-time access to the private equity community.

Mergers & Acquisitions
- Sell-side Advisory
- Buy-side Advisory
- Recapitalizations
- Mergers & Joint Ventures

Capital Advisory
- Equity Advisory
- Debt Advisory
- Infrastructure Finance

Financial Advisory
- Transaction Advisory
- Interim Management
- Performance Improvement
- Valuation Advisory
- Litigation Support

Special Situations & Restructuring
- Special Situations
- Turnaround
- Restructuring
- Bankruptcy
- Insolvency

ESOP Advisory
- Preliminary Analysis
- Feasibility Study
- ESOP Implementation
- Design & Execution
- Lability Study

Industry Groups

- Aerospace & Defense
- Building Products & Services
- Business Services
- Consumer & Retail
- Education & Training
- Energy & Power
- Financial Services
- Health & Medical
- Industrials
- Industrial Technology
- Technology, Media & Telecom
- Transportation & Logistics

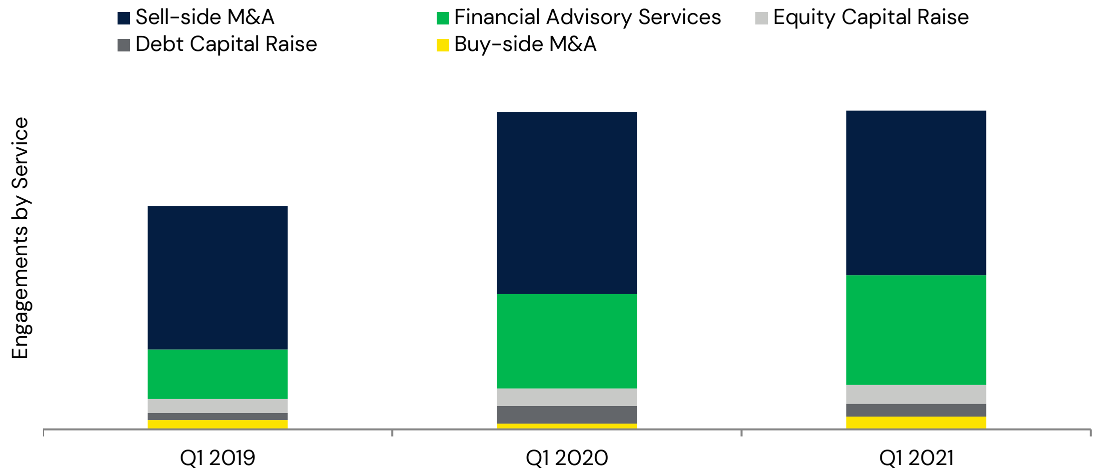
Sponsor Coverage Group

FIRM DATA

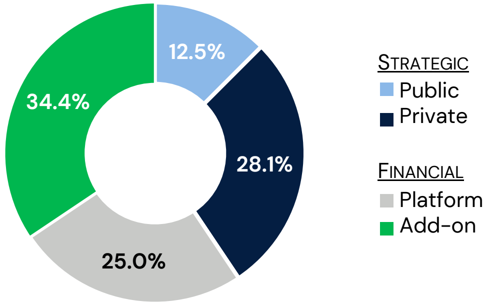
SELL-SIDE M&A POISED FOR HISTORIC YEAR

- Sell-side M&A has been strong year-to-date and 2021 is expected to be a historic year for middle market transaction volume as business owners look to lock in potentially favorable tax rates.
- Sponsors are expected to continue to aggressively compete for high quality businesses to build out robust sector specific portfolios.
- Private equity firms have increasingly utilized add-ons to enhance returns as 34.4% of our clients sold their business to a sponsor-backed portfolio company over the trailing twelve-month period (TTM).

Capstone Engagements By Service



Capstone TTM Buyer Breakdown

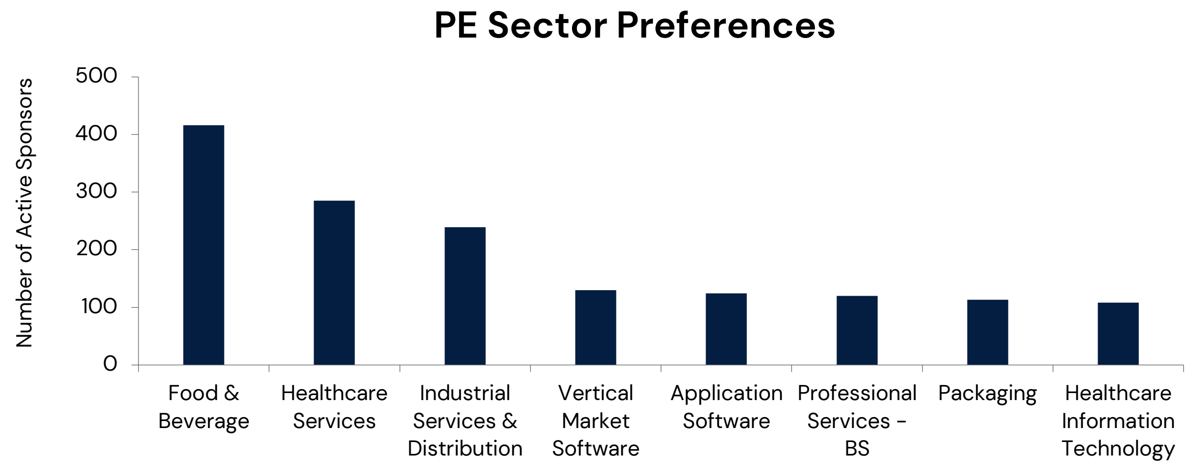


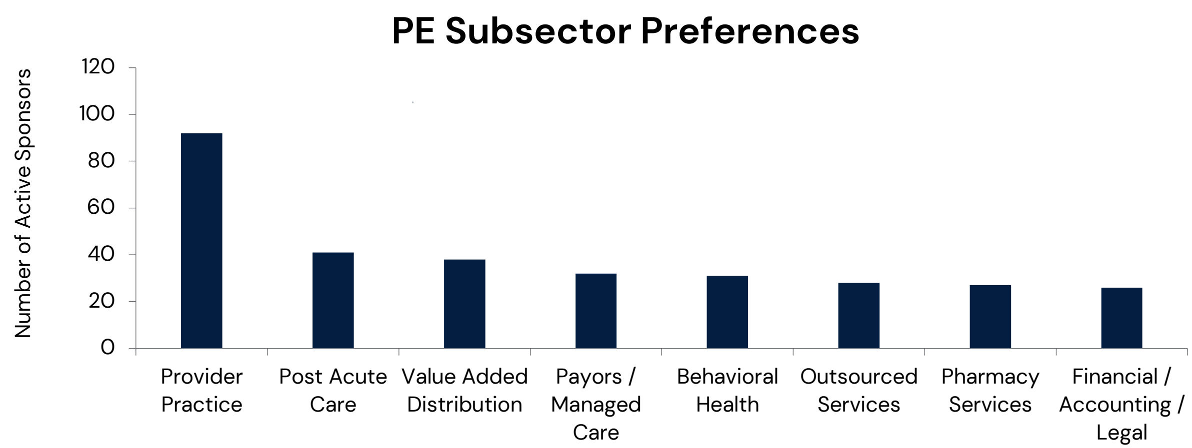
Source: Capstone propriety data based on live engagements and closed sell-side engagements

PRIVATE EQUITY PREFERENCES

HEALTHCARE SECTOR HIGHLY TARGETED BY PE FIRMS

- Capstone's conversations with PE firms have indicated a strong preference for middle market targets in the Food & Beverage and Healthcare Services industries. Industrial Services & Distribution and Vertical Market Software have also garnered robust interest.
- Healthcare subsectors including Provider Practice and Post Acute Care providers have been high on sponsor's target lists.
- PE firms are expected to continue to build out sector portfolios in the Healthcare industry, especially as the demand for sophisticated and interoperable healthcare information technology remains elevated.





Source: Capstone proprietary data

CAPSTONE PARTNERS

RECENT DEAL CLOSINGS

Capstone is an active leader in middle market M&A advisory and has closed a number of deals this year, serving clients and their needs despite the unprecedented disruptions to the economy. Select the deal tombstones below to read the full press release.

Provides Branded Camping Hammocks

WISE OWL OUTFITTERS

HAS BEEN ACQUIRED BY

THRASIO

Provides E-Commerce Gift Delivery Service

URBANSTEMS

HAS COMPLETED A SERIES C FUNDING ROUND CO-LED BY

SWANLEGEND

DFE

Provides Soy-Free Asian Sauces

Coconut Secret

HAS BEEN ACQUIRED BY

nutiva®

NURTURE VITALITY™

Provides Revenue Cycle Management Solutions

Professional Claims Bureau, Inc

pcb

HAS BEEN ACQUIRED BY

meduit

A portfolio company of

NexPhase CAPITAL

Provides Branded Pet Care Products

worldwise

better products. better planet.®

HAS SECURED DEBT FINANCING FROM

Wingspire CAPITAL

Provides Minerals and Mining Services

HAS SECURED A $45 MILLION SENIOR CREDIT FACILITY FROM

Provides Turnkey SaaS Application

SEDARU

HAS BEEN ACQUIRED BY

DANAHER

Provides Behavioral Health Services

EBS HEALTHCARE

We're Making a Difference

HAS BEEN ACQUIRED BY

THE STEPPING STONES GROUP

Transforming Lives Together

Comprises Two Milk Processing Plants

DFA

Dairy Farmers of America

HAS DIVESTED ASSETS TO

NDSM Holdings LLC

a joint venture entity formed by

BORDEN

Select Milk Producers, Inc.

Setting a Higher Standard

Provides Non-Toxic Insect Control Products

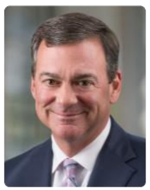
Spalding Laboratories

HAS BEEN ACQUIRED BY

EQUINE NETWORK

LEADERSHIP TEAM

JOHN FERRARA, FOUNDER AND CEO
jferrara@capstonepartners.com | 617-619-3325
John has dedicated 30+ years to serving as a trusted advisor to privately held businesses. Representative of over 200 engagements, he has acted as investment banker, management consultant, interim executive, investor, founder and board member. John has been recognized as one of the Top 50 M&A advisors in the U.S. and honored as an M&A Advisor Hall of Fame inductee. Under his leadership, Capstone has expanded to 19 offices in the U.S., U.K., and Brazil with an international platform that spans over 450 professionals in 40 countries worldwide. John graduated from Wesleyan University with an MBA from UCLA and The London School of Economics.



PHIL SEEFRIED, VICE CHAIRMAN
pseefried@capstonepartners.com | 303-572-6004
Phil has 30+ years of experience across most major financial markets. He was the co-founder and CEO of Headwaters MB until the acquisition by Capstone in 2017. He started his career with Bankers Trust, later working for Credit Suisse/First Boston. He was named Co-Head of Leveraged Finance at CSFB, responsible for managing close to 200 deals totaling $40 billion. Seefried was then named CFO of the 350-person Global Credit Group. He left Credit Suisse in 2000 and spent a year as CFO of Open Access Broadband Services before launching Headwaters in 2001. Phil holds an MBA from Stanford University and a BA from Williams College.

PAUL JANSON, COO
pjanson@capstonepartners.com | 303-887-0174
With 25 years of executive experience, Paul manages all administrative, legal and compliance matters for the firm and serves on Chairman of the Investment Banking Committee. On the M&A Advisory side, he is active in telecommunications services, manufacturing and infrastructure. Previously, Paul served as President & CEO of Camiant, a Packet Cable Multimedia broadband company. Paul was also CEO of Worldbridge Broadband Services Inc, a broadband and telecommunications company that was later acquired by C-Cor. Paul then became President of C-Cor's Global Services Division. He earned a BA-Business from Saint Anselm College.

JACOB VOORHEES, HEAD OF M&A
jvoorhees@capstonepartners.com | 617-216-1543
Jacob brings over 15 years of experience to the Capstone Partners investment banking team. As one of the founding members of Capstone Partners, he helped build Capstone's brand over the past decade until the merger with Headwaters MB in late 2017. Today, Jacob serves as the Head of Global M&A and is responsible for spearheading our international capabilities and coverage. Jacob received an MBA from the Sloan School of Management at Massachusetts Institute of Technology (MIT) and a BS from Cornell University.

TODD MCMAHON, HEAD OF INVESTMENT BANKING
tmcmahon@capstonepartners.com | 617-619-3334
Todd McMahon possesses over 20 years of transaction, financial services and corporate executive experience. Prior to Capstone Partners, Todd was President of Array Financial Services, a Boston based boutique M&A advisory firm he founded in 2002. He began his career at Putnam Investments, later moving to Bank Boston's investment banking group. He earned his MBA from Boston University and his BA from the University of Massachusetts.

LEADERSHIP TEAM (CONTINUED)

DANIEL MCBROOM, HEAD OF PRIVATE CAPITAL MARKETS

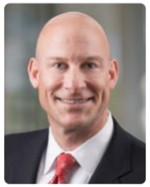
dmcbroom@capstonepartners.com | 303-951-7128

Daniel has 15 years of private and investment banking experience and is responsible for sourcing and analyzing hundreds of companies a year introduced by the firm's institutional clients and partners. Select companies are engaged and his team will stay involved until the transaction is closed. Before his financial career, Daniel spent seven years as a pilot in the United States Air Force. He earned an MBA from the University of Notre Dame and a BS from the United States Air Force Academy.

BRENDAN BURKE, HEAD OF SPONSOR COVERAGE

bburke@capstonepartners.com | 303-531-4603

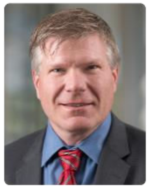
Brendan has 16 years in investment banking experience. He oversees the firm's outreach to private equity sponsors and recruitment of senior investment bankers. Since joining Headwaters MB (now Capstone) in 2004, he has held roles in transaction execution, business development, recruiting and marketing. In 2012, he was awarded 40 UNDER 40 by the M&A Advisor. He received a BA in Politics, Philosophy, Economics from Pomona College.



PETER ASIAF, HEAD OF BUSINESS DEVELOPMENT

pasiaf@capstonepartners.com | 617-619-3368

Peter has more than 20 years of experience as a senior business development executive across the professional and financial services industries. He has been a growth-oriented leader in early-stage, middle-market and Fortune 500 enterprises, helping them to design and execute strategic expansion plans, optimize brand positioning and strengthen key market relationships. Peter is a Certified Exit Planning Advisor (CEPA) designated by the Exit Planning Institute



BRIAN DAVIES, MANAGING PARTNER, FINANCIAL ADVISORY SERVICES GROUP

bdavies@capstonepartners.com | 617-619-3328

Brian has 20+ years of experience working in the fields of corporate recovery, business reorganization and interim management services. He has provided financial advisory services to lenders, debtors, creditors' committees, trustees and equity holders in bankruptcy matters and out-of-court restructurings. Brian has provided assistance to under-performing businesses, acquirers of distressed companies. He has worked with companies to develop cost containment and asset rationalization plans, improve liquidity, re-engineer financial and other back-office functions. He received a MS from Bentley University and MSF from The McCallum School, Bentley University.

KENT BROWN, HEAD OF DEBT ADVISORY GROUP

kbrown@capstonepartners.com | 303-951-7127

Kent brings over 30 years of corporate debt placement and advisory experience. He has extensive experience in arranging various forms of middle-market corporate debt, including leveraged loans, asset-based loans, subordinated debt, second-lien and uni-tranche facilities, syndicated credit facilities, venture debt, equipment leases, private securitizations, sale-leasebacks, and mortgages, among other structures. He earned an MBA from the University of Chicago and a BS from the University of Colorado at Boulder.

Capstone Partners is one of the largest independently owned investment banking firms in the United States. For over 20 years, the firm has been a trusted advisor to leading middle market companies, offering a fully integrated range of expert investment banking and financial advisory services uniquely tailored to help owners, investors, and creditors through each stage of the company's lifecycle. Capstone's services include M&A advisory, debt and equity placement, corporate restructuring, special situations, valuation and fairness opinions and financial advisory services. Headquartered in Boston, the firm has 175+ professionals across the U.S. and an international presence including over 450 professionals in 40 countries. With 12 dedicated industry groups, Capstone delivers sector-specific expertise through large, cross functional teams on a global basis. For more information, visit www.capstonepartners.com.

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