CAPITAL MARKETS UPDATE

Middle Market M&A
Q1 2022

CAPSTONE PARTNERS

MARKET COMMENTARY

Normalization in Sight?

The mergers and acquisitions (M&A) market has finally showed signs of stabilizing following two years of unpredictable activity, however, unfolding economic uncertainty might still halt normalization. Over the past two years we have seen drastic swings in M&A activity, as business owners have combated COVID-19, supply chain disruptions, and now elevated levels of inflation. The pandemic decimated transaction volume in 2020, with total deal volume falling 16.4% from 2019 as many businesses went into survival mode—bringing a temporary pause to M&A activity. As prospective sellers emerged from the pandemic, they were met with a fervent pool of buyers ready to deploy capital to make up for lost time. 2021 subsequently packed three years' worth of dealmaking into one, and middle market transaction volume reached its highest level in seven years, rising 34.1% from 2020. Q4 2021 proved to be a historic quarter with dealmakers and third-party M&A service providers encountering severe capacity constraints amid a flood of transactions. Capstone experienced this surge firsthand, with our deal closings in Q4 surpassing prior survey results.

Following a historic M&A market in 2021, middle market deal activity has returned to more normalized levels through Q1 2022 with transaction volume increasing 0.1% year-over-year (YOY). While the frenetic pace of M&A activity experienced in the second half of 2021 may be in the rearview, the market remains healthy for middle market business owners. By historic standards, the Q1 deal count of 3,789 closed transactions outpaced the pre-COVID five-year quarterly average of approximately 2,470 deals. However, headwinds cannot be ignored—Russia's war on Ukraine, rising interest rates, and elevated global inflation present significant challenges for the market. Notably, business owners in Capstone's Middle Market Business Owners' Survey have communicated uncertainty regarding the economy, with the percentage of owners holding a positive economic outlook dropping from 59.3% in Q1 to 44.2% for Q2. Despite challenges ahead, business owners still plan to pursue inorganic growth, with 29.3% planning to engage in acquisitions, an increase from both Q1 2022 and Q4 2021. Debt and equity financing also remain a top agenda item for executives, with 31.9% planning to secure additional capital, surpassing the past two quarters as well.

Valuations declined a full turn in Q1 to an average of 9.6x EBITDA compared to the full-year 2021 average of 10.7x. However, quality businesses are still receiving high bids from a competitive group of buyers. In addition, the high multiple in 2021 was largely driven by a widespread flight to quality with only the top assets trading, partly due to dealmakers and buyers facing heavy capacity constraints. Notably, larger deals have shown greater insulation from a moderating valuation environment through Q1 2022 with transactions between $250 and $500 million in enterprise value recording an average EBITDA multiple of 13.6x compared to 11.7x in full-year 2021. In addition, middle market valuations have greatly varied across industries, as discussed in Capstone's Middle Market M&A Valuations Index. The Technology, Media & Telecom (TMT) space has continued to lead M&A pricing with a three-year average multiple of 13.3x EBITDA. As we continue to operate in an inflationary environment, margins and operating efficiency will likely be emphasized in M&A processes in the near term.

M&A volume among strategic buyers has declined compared to Q1 2021 although the average transaction value for acquisitions by public and private strategic buyers rose 26.2% and 34.2% YOY in Q1, respectively. Balance sheets and liquidity positions of strategics remain healthy, which offers encouraging prospects for sustained consolidation. Supply chain strength has been a key focus over the past 24 months which will likely be a driving force for acquisitions in the near term.

MARKET COMMENTARY

Private equity (PE) firms continue to possess the luxury of vast levels of dry powder ready to be deployed into investment opportunities. However, the buying spree exhibited in 2021 has certainly slowed with middle market transactions closed by PE firms falling nearly 37% YOY in Q1. Target company growth profiles will be intensely scrutinized through the lens of an economic downturn, as sponsors seek recession resilient businesses that can generate healthy internal rates of return upon exit. Valuations paid by private equity have held strong, amounting to an average of 7.3x EBITDA in Q1 2022, matching the full year 2021 average, according to GF Data. Healthy valuations have been supported by an accommodative debt environment, with average debt multiples settling at 3.9x EBITDA in Q1, nearly mirroring the full year 2021 average of 4.0x.

Economic uncertainties will persist over the next several months, with market participants keenly monitoring the Federal Reserve's monetary policy actions. While it may be too early to decipher how the evolving economic climate will impact the direction of valuations and volumes for the remainder of the year, one fundamental driver of M&A is guaranteed—a significant portion of transaction inventory will be motivated predominately by demographics, as aging business owners increasingly seek a liquidity event. In addition, the mountain of private equity dry powder, pandemic fatigued CEOs, and talks of recession on the horizon may make the current window an optimal time for many to pursue an exit, fueling a healthy M&A environment through 2022.

"As the weather turned warm in 2022, sponsors noted a chill in new deal-flow both in volume and quality. The confluence of inflation, supply chain issues, and capital markets turbulence have prompted private equity sellers to pause their paths to exits. Meanwhile, they scour their existing portfolios for signs of financial softness and new investments for cyclicality."

Brendan Burke
Head of Sponsor Coverage

MIDDLE MARKET OUTLOOK

Q1 2022 TAKEAWAYS & THEMES

The M&A market has normalized in 2022 from the record pace observed in the prior year, amid economic uncertainty and rising interest rates

- While deal flow has normalized from record levels in Q1 2022, M&A activity remains healthy despite economic uncertainty, supply chain disruptions, and rising inflation.
- Healthy average deal value indicates strong competition for quality assets, with strategics aggressively pursuing accretive targets.
- Although private equity firms have actively deployed capital to high growth sectors, capital overhang remains healthy, encouraging elevated sponsor activity.
- The current environment is better for "story deals," presenting an opportunity for target companies with weaker sales growth, margins, or customer concentration.

Persistent buyer appetite and a backlog of businesses pursuing a liquidity event are expected to drive healthy deal activity through 2022

- With a record quantity of businesses going to market in 2021, there remains a backlog of deals that are forecast to fuel robust M&A activity through 2022.
- Private equity firms are expected to capitalize on the current environment, acquiring companies at low multiples and maximizing the rate of return upon exit.
- Rising interest rates are likely to weigh on valuations, however, quality assets will still obtain strong pricing, particularly from strategics that have identified synergies.
- Concern surrounding Russia's war on Ukraine, potential antitrust scrutiny, interest rate increases, and foreign relations will be major factors in cross-border dealmaking through the remainder of 2022.

CAPSTONE PARTNERS

TABLE OF CONTENTS

Q1 2022 BY THE NUMBERS

0.1% ⇨

INCREASE IN DEAL VOLUME

Following a historic M&A market in 2021, deal volume has normalized to pre-pandemic levels in Q1 2022, rising 0.1% year-over-year (YOY)

3.9x ⇨

AVERAGE DEBT MULTIPLE

Average debt multiples remain healthy, declining slightly to 3.9x in Q1 2022 from an elevated 4.0x in full-year 2021.

13.6x ⇧

EBITDA MULTIPLES UP MARKET

The average EBITDA multiple for upper middle market deals was 13.6x in Q1 2022 compared to 11.9x in Q1 2021

36.6% ⇩

DECREASE IN PE TRANSACTIONS

Private equity activity declined 36.6% YOY in Q1 2022 as buyers have focused on existing holdings amid uncertainty

13.5% ⇧

AVERAGE DEAL VALUE

Average deal value reached $70.2 million in Q1 2022, rising 13.5% YOY as buyers continue to pursue quality assets in growing markets

8.5% ⇩

DEALS BY FOREIGN BUYERS

The volume of transactions involving a foreign buyer has declined 8.5% YOY in Q1 2022 amid economic uncertainty

$43.7B ⇨

PE FUNDRAISING

Private equity fundraising slightly declined, falling 6.6% YOY to $43.7 billion in total capital raised in Q1 2022

34.2% ⇧

PRIVATE STRATEGIC DEAL VALUE

The transaction value for acquisitions by private strategic buyers rose 34.2% YOY, reaching $74.3 million in Q1 2022.

$1.4T ⇧

PE DRY POWDER

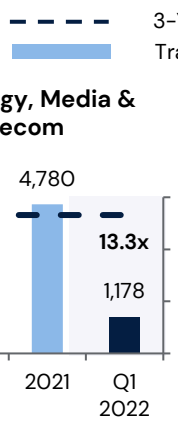
Capital overhang has remained at elevated levels, providing a favorable backdrop for healthy PE deal activity

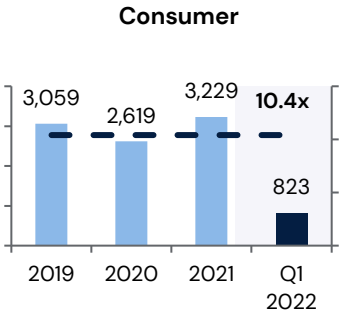
CAPSTONE'S PROPRIETARY MIDDLE MARKET VALUATIONS INDEX

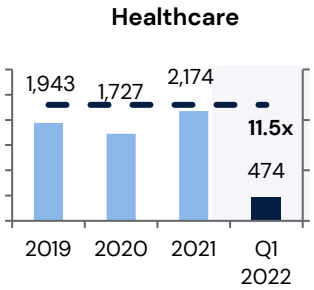
Valuation & Transaction Volume Takeaways

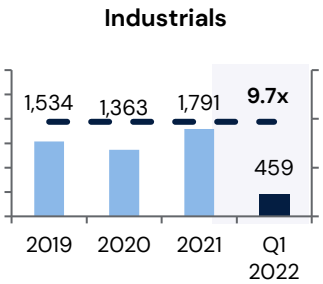
- Middle market valuations have remained healthy across verticals tracked by Capstone's Middle Market M&A Valuation Index, with Technology, Media & Telecom averaging the highest 3-year multiple at 13.3x EBITDA.
- EBITDA multiples in the Consumer industry increased modestly in the 3-year period ending in Q1 2022, averaging 10.4x.
- Rising interest rates will impact valuations as companies' future cash flows become discounted at a higher rate.

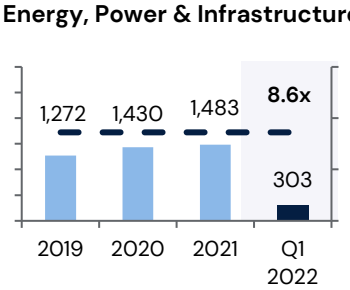
For more information on the fair value of your business, comparable transactions and public companies, contact us.

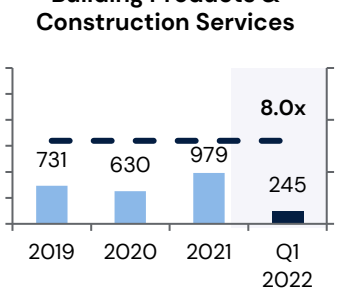


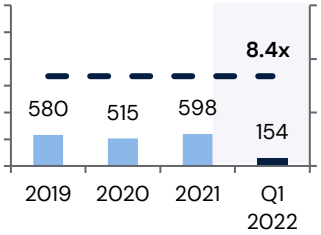


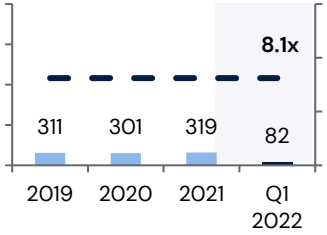


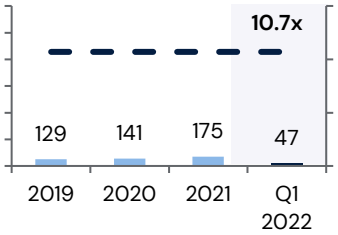


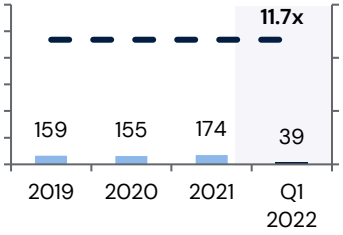












INDUSTRY SPOTLIGHT

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Financial Technology & Payments Industry Update

In 2021, there were 1,035 transactions that were either announced or completed in the Financial Technology (FinTech) & Payments sector, setting a new annual M&A volume record. Deal activity through March 2022 slightly trails 2021 levels during the same period but has continued at a strong pace with 92 transactions announced or completed compared to 107, respectively.

We have identified four key drivers behind the strong pace of M&A activity this year:

1. **Accelerated Growth in Venture Capital (VC)-Backed Startups:** FinTech companies globally raised $29.3 billion in VC across 1,233 deals in Q1 2022, representing a 13.8% YOY increase. VC funding has exponentially accelerated the growth of FinTech startups. In Q1 2022, the median pre-money valuation for VC-backed, late-stage FinTech companies increased 44.5% to $257.5 million compared to $178.3 million in Q1. Organic growth tends to decelerate for later-stage businesses, so we expect M&A activity to increase steadily as a key strategic option for these VC-backed FinTech firms looking to expand their market presence and maintain high growth rates.

2. **Consolidation of Growth Stage FinTechs:** As growth in previously early-stage VC-backed FinTechs begins to decelerate, the now later-stage firms will look to M&A to reaccelerate growth and expand their presence in the market. Other later-stage FinTechs will have trouble hitting revenue milestones to justify high valuations and will then look to M&A for other alternatives, leading to a consolidation of growth stage VC-backed FinTech companies.

3. **Diversified Product Offerings:** Recently, companies have begun to diversify their platforms and services leading to lower costs and allowing them to target a broader market. This can be seen in the Insurance Technology (InsurTech) segment, where participants have begun to add direct-to-consumer (DTC) capabilities to their platforms, which in turn has reduced the costs associated with acquiring and servicing their customers leading to economies of scale. The InsurTech market is expected to reach a market size of $152.4 billion growing at a compound annual growth rate of 51.7% between 2021 and 2030, according to Grand View Research.

4. **New Innovations:** The Financial Services ecosystem has seen many investors migrate away from centralized asset classes to self-executing blockchain contracts and digital assets including cryptocurrencies. New FinTech & Payment companies providing such services have propelled innovation among registered brokers and financial institutions to strengthen their digital tools and engagement. M&A provides these firms an opportunity to expand their offerings and modernize their services.

5. We expect M&A activity in the FinTech & Payments sector to decrease slightly compared to 2021 levels, but to remain strong in 2022. High levels of VC activity in 2021 have accelerated the maturity and growth of FinTech companies, creating an environment ripe for M&A activity to address issues of slowed growth. While we do anticipate a slight decrease in volume compared to 2021, the push to bundle capabilities has spurred M&A activity year-to-date (YTD) and will continue to do so throughout the remainder of 2022.

CAPITAL MARKET DASHBOARD

YTD EQUITIES

S&P 500
-12.2%

Last	1Y %	P/E LTM
4,132.2	+0.4	19.1

Dow Jones Industrial
-8.6%

Last	1Y %	P/E LTM
33,990.1	-8.6	17.7

NASDAQ
-7.2%

Last	1Y %	P/E LTM
12,642.1	-7.2	26.7

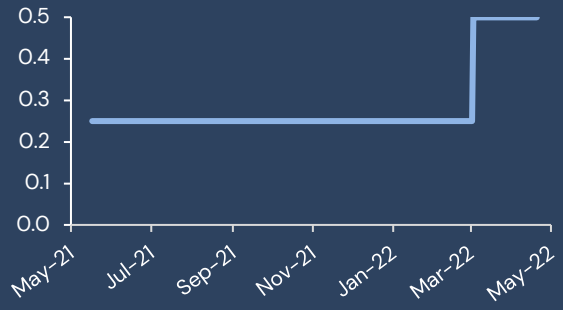
FIXED INCOME

U.S. Yield Curve

1Y	3Y	5Y	10Y	30Y
1.933	2.636	2.716	2.743	2.969

POLICY RATE

Federal Funds Target Rate



ECONOMIC INDICATORS

GDP, LABOR MARKET, & INFLATION

	Last	YOY	
GDP	*1.5%*	*+3.5%*	
Consumer Confidence	*106.4*	*-11.3%*	
Unemployment	*3.6%*	*-40%*	
Consumer Price Index	*288.7*	*+8.2%*	

HOUSING MARKET

Housing Starts	*$1,724.0*	*+14.6%*	
Total Construction	*$1,744.8*	*+12.3%*	

PMI & NMI

Purchasing Managers	*55.4%*	*-8.6%*	
Non-Manufacturing	*57.1%*	*-8.9%*	

RETAIL

Retail Sales	*$677.1*	*+8.2%*	

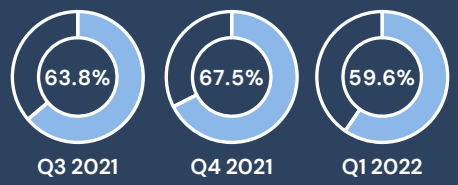
Source: FactSet as of 05/31/22

CAPSTONE'S MIDDLE MARKET BUSINESS OWNERS SURVEY

AVERAGE REVENUE GAINS SEE SLIGHT DECREASE IN Q1

Rising inflation has infringed on businesses' bottom lines, driving the number of companies with revenue increases down in Q1 compared to Q4

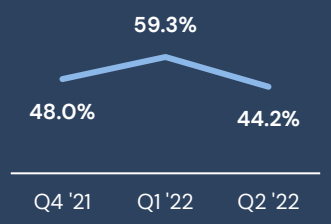
Percentage of Businesses Experiencing Revenue Increases



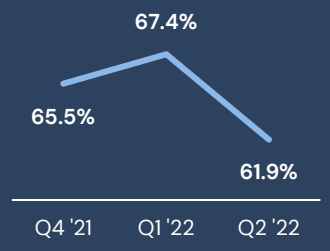
Sample Size (N): 148, 430, 436

CEO CONFIDENCE DECLINES FROM Q1

Positive Economic Outlook



Positive Industry Outlook



Sample Size (N): 148, 430, 436

BUSINESS OWNERS EXPAND INORGANIC STRATEGIES

Organic Initiatives	Q4 '21	Q1 '22	Q2 '22
Market Penetration	69.2%	45.8%	56.9%
Expanding Product/Service Portfolio	65.4%	51.0%	57.4%
Diversifying Customer Base	56.4%	47.9%	48.4%
Expanding into New Geographic Locations	42.3%	44.3%	39.9%

Inorganic Initiatives	Q4 '21	Q1 '22	Q2 '22
Engaging in Acquisitions	20.5%	26.0%	29.3%
Securing Debt or Equity Capital	21.8%	28.6%	31.9%

Source: Capstone Partners' Middle Market Business Owners Survey
Note: Blue indicates increase from Q1 to Q2
Sample Size (N): 78, 192, 188

LEVERAGED FINANCE CONDITIONS

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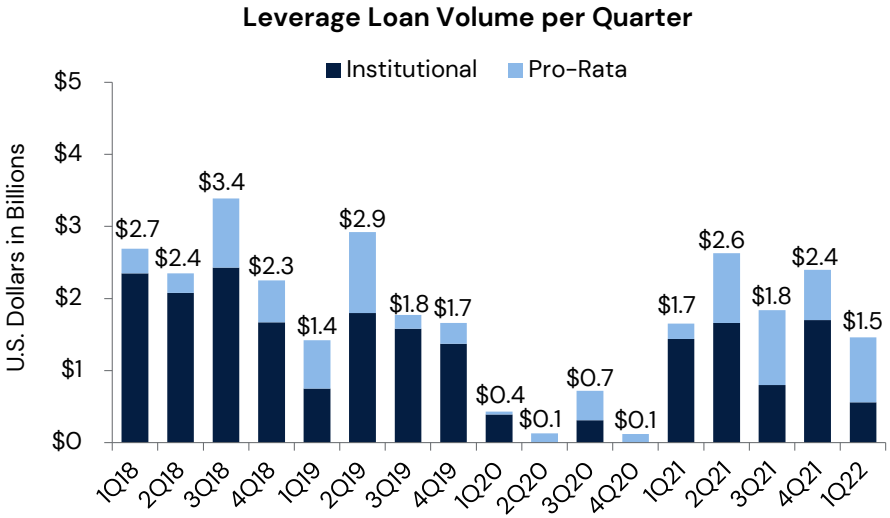
Key Market Stats

- **Significant pullback in loan volumes.** Q1 2022 middle market loan volume decreased substantially compared to Q4 2021 as the feverish M&A pace of 2021 subsided. M&A drove ~31% of overall loan volume in Q4 2021 compared to ~5% in Q1 2022. Leveraged buyout (~40% of overall volume) activity led the way in Q1 2022, supported by elevated private equity dry powder, followed by strong refinancing activity (~35%) as rates remained relatively low, particularly toward the beginning of the quarter. We expect this trend to continue reversing in the second half of the year as the Fed tightens monetary policy and raises rates. The remaining loan volume for the quarter consisted of various other corporate purposes (~25%).

- **Increased loan pricing.** Average LIBOR spreads widened to 600 basis points (bps), their highest level in the past decade, as increasing Fed benchmark rates and general economic uncertainty led to a recalibration of perceived credit risk in the broader market. Capstone expects additional rate hikes to lead to continued yield expansion in the second half of 2022 before settling at heightened levels in early 2023.

- **Sustained leverage multiples.** Middle market leverage multiples remained elevated for the quarter. While rates increased somewhat, significant dry powder among fund managers resulting from unprecedented fundraising in recent years continued to support high leverage multiples in the market.

- **Decreased inflows of debt capital.** The vast amounts of dry powder combined with general economic uncertainty led to decreased fund inflows through March of 2022. Approximately $2.5 billion was raised in Q1 2022 compared to $4.1 billion for the same period in 2021 and down from $9.5 billion raised in Q4 2021. With that said, the perceived hedge that private credit provides in a rising interest rate environment, coupled with a search for yield among institutional investors, should continue to support a relatively healthy fundraising environment moving forward.



Source: S&P Global Market Intelligence

LEVERAGED FINANCE CONDITIONS (CONTINUED)

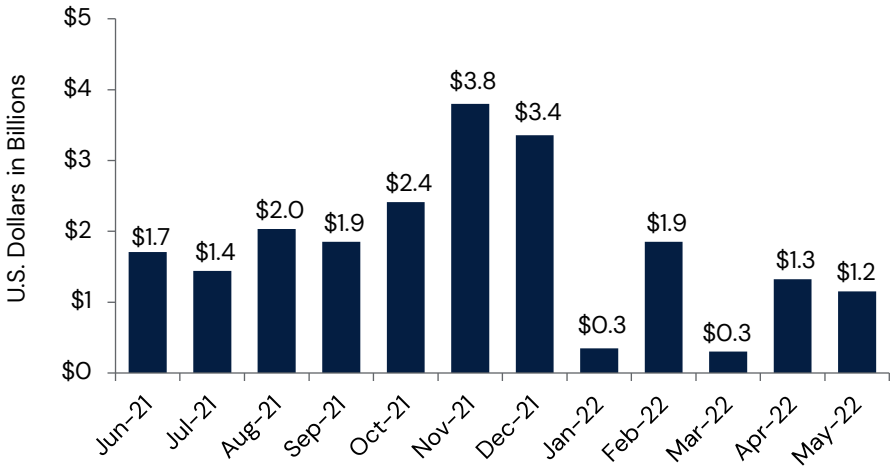
Quarterly Market Observations

- **More of the same…for now.** Despite recent trends in the public markets, borrower-friendly conditions persist within the Direct Lending market due to a continued supply and demand imbalance and a lack of quality deal flow in the first half of 2022. While increased competition among lenders has sustained market strength, recent data points to the potential of a recession as soon as the end of 2022 as continued inflation, a historically tight labor market, and supply chain challenges permeate the overall economy and require continued action from the Fed in response.

- **Private credit continues to gain share.** Private credit continues to gain market share at the expense of the Broadly Syndicated Loan (BSL) and High Yield Bond (HYB) markets. Increasingly large direct lending funds with growing hold positions and an appetite for higher leverage and looser credit agreement terms have made direct lending competitive with more liquid credit sources. Additionally, spreads have widened more rapidly within the BSL and HYB markets, eliminating the cost of capital advantage those offerings have historically enjoyed. However, the advantage could be short-lived. Direct lending has historically lagged the more liquid markets and recent trends indicate the likelihood of choppiness in Q3 and Q4.

- **Credit Agreement terms revert to the mean.** Further supporting the shift toward direct lending is the convergence of terms between direct and syndicated loans. Historically less flexible on terms (EBITDA addbacks, financial covenants, etc.), direct lenders have become more accepting of terms formerly reserved only for the BSL and HYB markets. Despite expected market volatility, these conditions will likely continue in the near term as competition for quality deals remains elevated.

Monthly Inflows to the Middle Market Loan Asset Class



Source: S&P Global Market Intelligence

DEBT ADVISORY GROUP

Capstone's Debt Advisory Group helps privately-owned and sponsor-backed companies secure debt capital for organic growth, acquisitions, dividend recapitalizations, and refinancings. 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

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The Importance of Understanding Value

Valuation influences nearly every aspect of corporate finance. Having a comprehensive understanding of how it is impactful is critical to the decision-making process for business owners, investors, lenders, and creditors alike. Most third-party valuation experts will have similar experience and expertise in the analysis process, which is one of the reasons valuations are sometimes viewed as a commodity. However, in the context of middle market businesses, there is a strong case to be made for selecting a provider that specializes in working with companies at that market level.

Capstone professionals possess deep finance and accounting proficiency and combine the application of sophisticated valuation methodologies and technical knowledge with decades of practical middle market M&A experience. This results in objective, independent assessments of value that are informed by relevant, real-time market insights for middle market companies. Some of the types of assignments we undertake, our approach, and the secret ingredient that helps our clients obtain the most value are outlined below.

Fairness Opinions: Informed Opinions of Value

A fairness opinion is an expert analysis that assesses whether a proposed purchase price is fair. It is usually completed when an M&A transaction is imminent but has not yet closed. Companies, boards of directors, and key stakeholders will rely on these independent value assessments to affirm that they are upholding their fiduciary responsibilities in approving the transaction.

Capstone performs rigorous valuation analysis informed by extensive practical M&A experience that provides clients with independent assessments that mitigate risk, enhance transparency with stakeholders, and enable informed decision making when assessing transactions that can have a material impact on shareholder value.

Dispute Resolution: Preserving Business Value

Conflict happens. It is common for business owners to disagree on management approach or decision making, which can lead to contentious disputes. In many cases, these disputes can significantly erode the enterprise value of the business that owners have spent decades building, simply because the owners can no longer co-exist.

Capstone's dispute resolution and mediation support services allow business owners to preserve company value while avoiding lengthy and costly legal battles. We leverage a practical, hands-on approach and decades of valuation experiences that can be used to find a middle ground and settlement that is mutually agreeable to both parties.

Strategic Alternatives Assessment: Identifying and Unlocking Value

Businesses are continually growing and evolving. Business owners are constantly faced with the strategic decisions: Is now the time to sell? Should we invest more capital in growth? Are all products and services core to the business? Capstone's combination of experience valuing and operating businesses allows us to help owners lay out strategic alternatives and understand the valuation implications of their

FINANCIAL ADVISORY SERVICES (CONTINUED)

decisions. Whether through a sale of the business, a restructuring of operations, or the divestiture of non-core assets—there are many alternatives to enhance shareholder value. Capstone helps owners choose the right path with confidence.

Informed Valuations Improve Decision Making and Outcomes

Industry specific, in-depth client knowledge is critical, as sector specific growth prospects, headwinds, and investor interest will impact the valuation. This is the point where Capstone's position as a leader in middle market investment banking and advisory services provides our team with unique insights.

Capstone's banking teams cover 12 defined industry groups each with a multitude of related sectors, executing numerous transactions for and with middle market businesses throughout the year. This activity offers our advisory teams an unprecedented amount of current market information that isn't as available to firms that rely on published public company data.

In addition to all the other information we review, we can also provide real-time analysis of what other businesses are selling for in a given industry.

Valuation drives decision making on a daily basis in corporate finance for all stakeholders. Having a trusted advisor in Capstone that understands the technical and practical sides of valuation empowers our clients to make informed decisions with confidence and leads to better outcomes.

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 Advisory Services
- Court-appointed Receiver and Chief Restructuring Officer

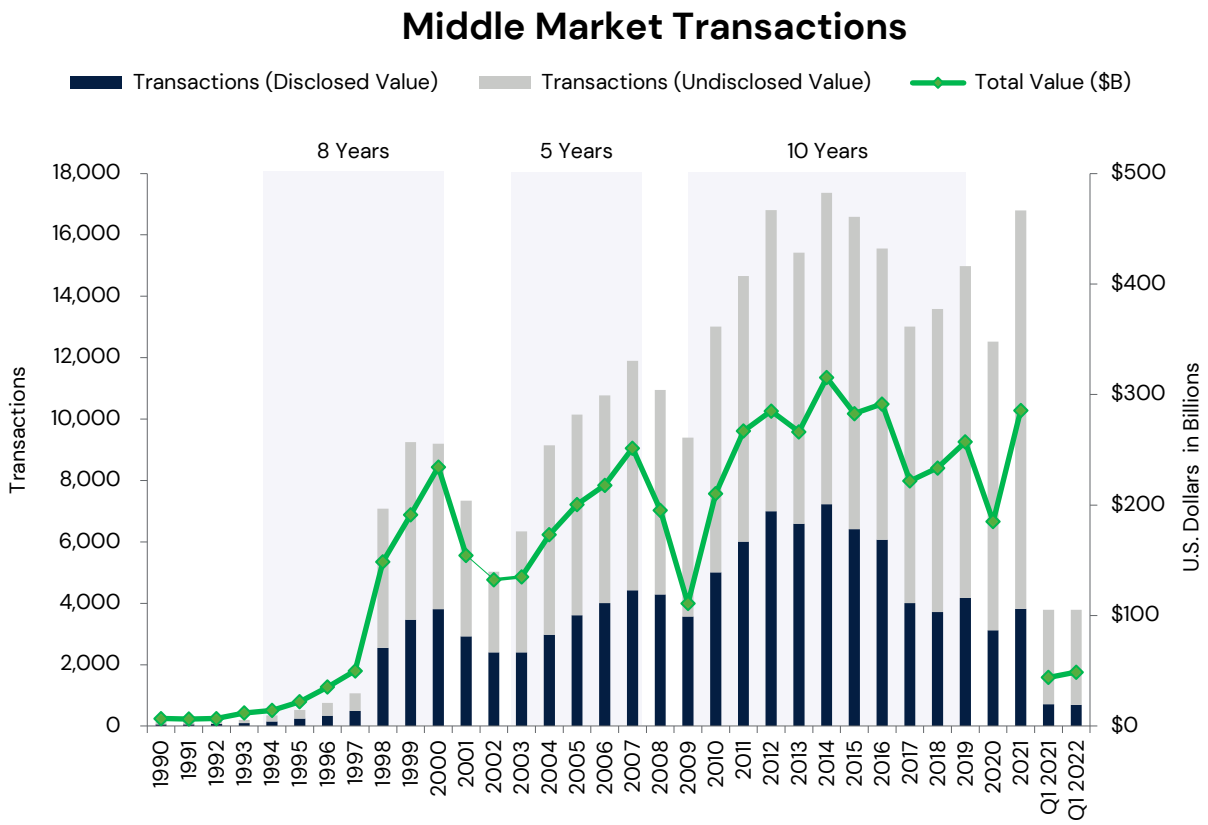
Insolvency
- Debtor and Creditor Representation Services
- Chapter 11 and Chapter 7 Services
- Section 363 Asset Sale

MIDDLE MARKET M&A ACTIVITY

M&A AMID ECONOMIC CYCLES

MIDDLE MARKET M&A SLOWS FROM FRENETIC PACE

- Following a blistering M&A market in 2021, deal volume has normalized in Q1 2022, increasing 0.1% year-over-year (YOY). While many dealmakers are noting declines in prospective opportunities, the M&A market remains healthy despite economic uncertainty, ongoing supply chain disruptions, and rising inflation.
- Total deal value increased 10.9% YOY to $48.9 billion in Q1 2022 as buyers continue to pursue high-quality assets in growing markets.
- Interest rate hikes are top-of-mind for business owners as the Federal Reserve aims to curb inflation while minimizing the adverse economic effects.



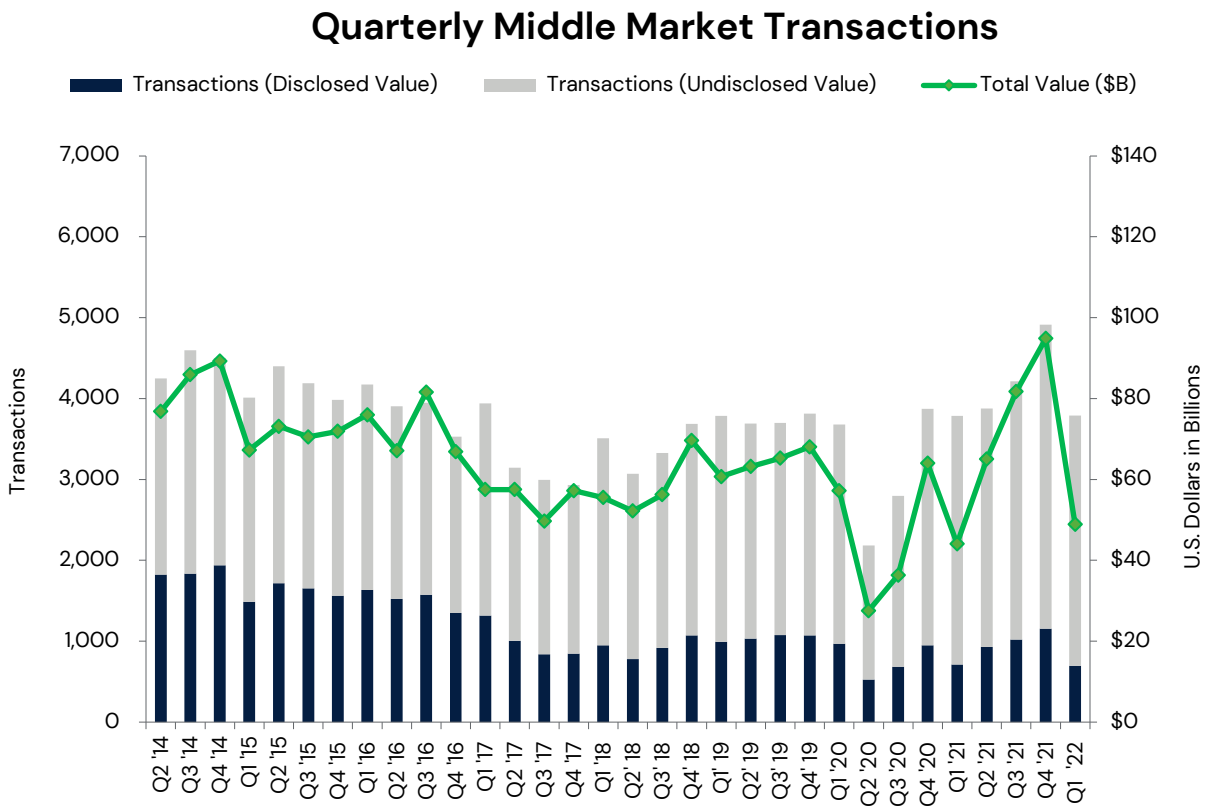
Note: Shaded areas indicate expansion
Source: Capital IQ
Enterprise Value < $500mm

CAPSTONE PARTNERS

QUARTERLY M&A VOLUME

DEAL ACTIVITY NORMALIZES IN Q1 AMID UNCERTAINTY

- Deal volume in Q1 2022 fell 22.9% from a historic quarterly level in Q4 2021. Record M&A activity in the prior quarter has made quarter-over-quarter (QOQ) comparisons difficult.
- Despite recording a YOY increase, average deal value fell a considerable 14.6% QOQ to $70.2 million in Q1 2022 as buyers rushed to close marquee deals before 2021 year-end amid capacity constraints.
- Due to the unprecedented quantity of businesses pursuing a liquidity event in 2021, there remains a significant backlog of deals that are expected to supplement robust transaction volume through 2022.



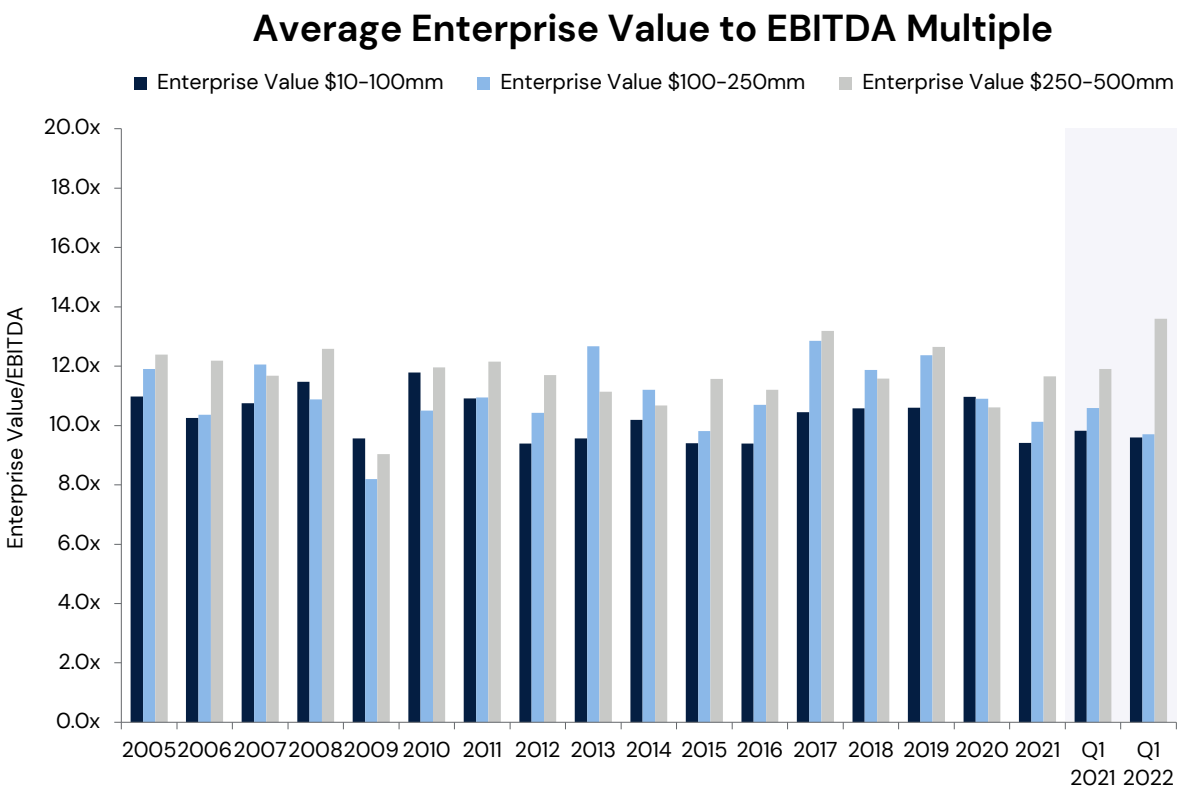
Source: Capital IQ
Enterprise Value < $500mm

CAPSTONE PARTNERS

BREAKING IT DOWN BY SIZE

VALUATIONS DEMONSTRATE DEFENSIBILITY UP MARKET

- The average lower middle market EBITDA multiple, characterized by enterprise values between $10-100 million, declined to 9.6x in Q1 2022 from 9.8x in Q1 2021 as the valuation environment has normalized for smaller deals.
- EBITDA multiples in the $100-$250 million enterprise value range also fell, averaging 9.7x compared to 10.6x in Q1 2021.
- Larger target companies are often more insulated from pricing pressure. Valuations for upper middle market transactions ($250-$500 million in enterprise value) averaged 13.6x EBITDA in Q1 2022, a significant rise from 11.9x in Q1 2021 and 11.7x in full-year 2021.



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

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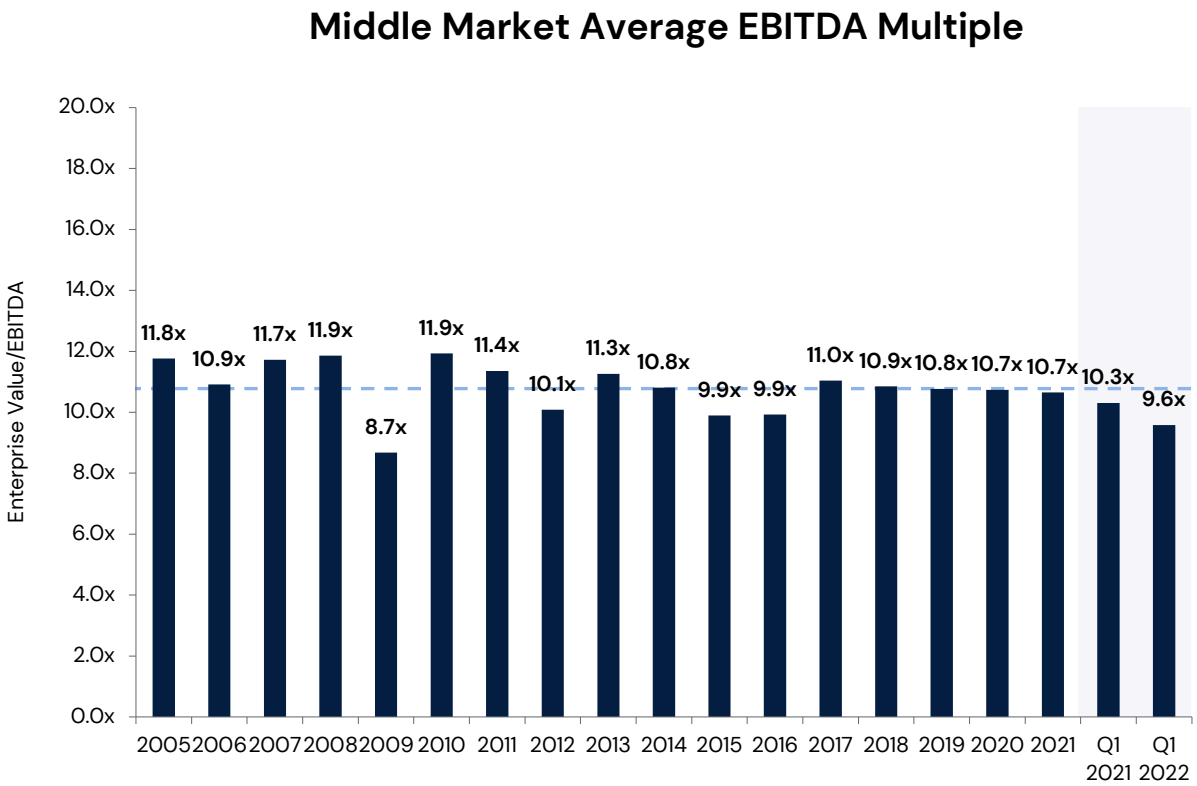
PRICING TRENDS

EBITDA MULTIPLES SIGNAL POTENTIAL BUYER'S MARKET

- The surging valuation environment in 2021 appears to be moderating. The average middle market EBITDA multiple declined to 9.6x in Q1 2022 from 10.3x in Q1 2021.
- Lower valuations are a harbinger of a buyer's market. Capstone expects opportunistic private equity firms to capitalize on these conditions, acquiring companies at low multiples and maximizing the internal rate of return upon exit.
- The current market is a better environment for "story deals" involving target companies that may have weaker sales growth, customer concentration, tight margins, or require additional positioning in sales processes.



Dotted line indicates 2005 to 2021 average of 10.8x
Source: Capital IQ and Capstone Partners
Includes multiples 3x-30x
Enterprise Value < $500mm

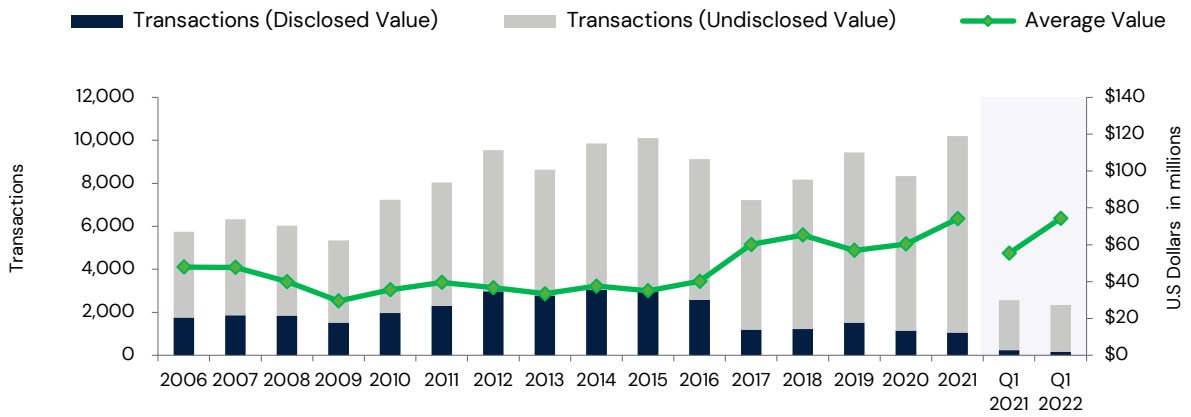
CAPSTONE PARTNERS

STRATEGIC ACQUIRERS

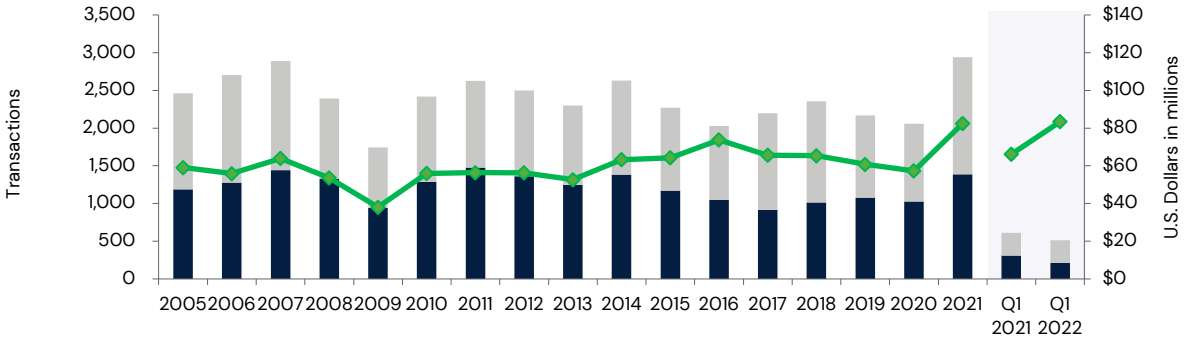
STRATEGIC DEALMAKING DECLINES FROM RAPID PACE

- Following a record 2021, strategic M&A has normalized with transactions closed by public and private companies falling 16.5% YOY and 8.7% YOY respectively in Q1 2022.
- Acquisitions by public strategic acquirers averaged $83.5 million in deal value in Q1 2022, rising 26.2% YOY. The transaction value for acquisitions by private strategic buyers rose 34.2% YOY, reaching an average deal value of $74.3 million.
- Healthy average deal value indicates strong competition for quality assets, with strategics voracious for targets that expand geographic footprint, create synergies, strengthen supply chains, or add scale.

Acquisitions by Private Companies



Acquisitions by Public Companies



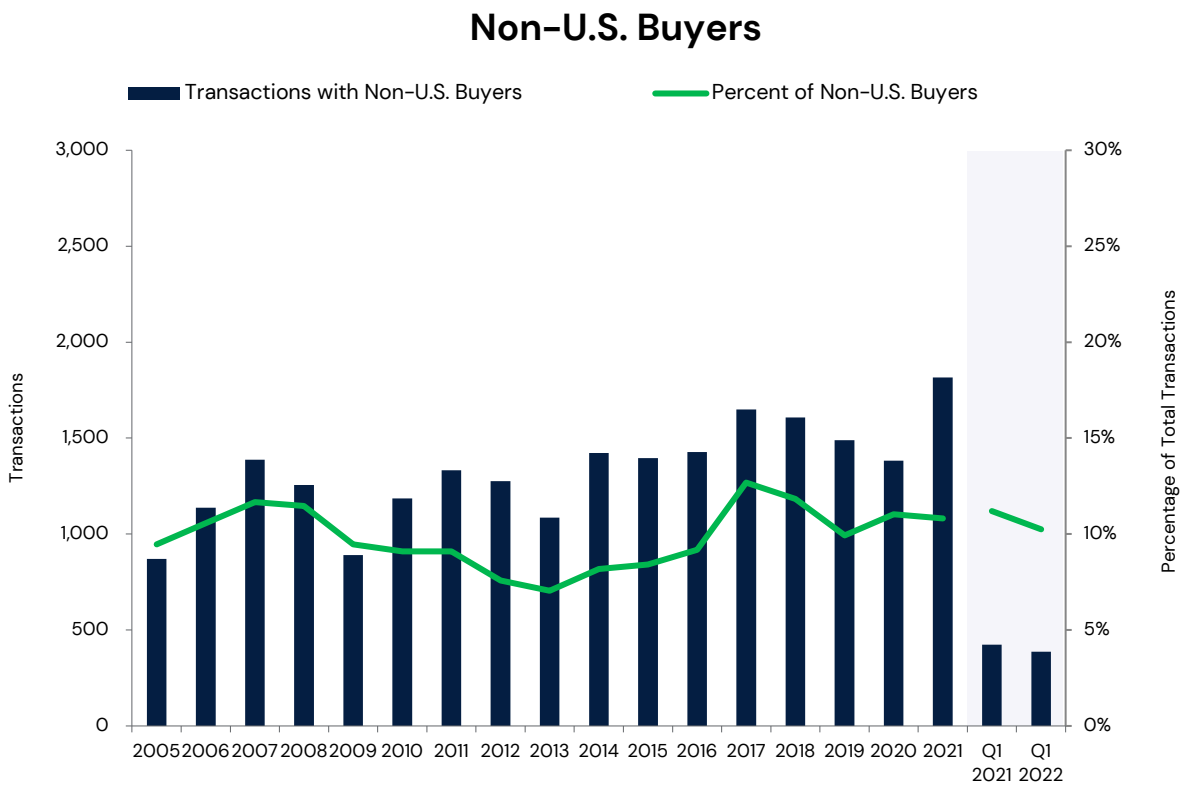
Source: Capital IQ
Enterprise Value < $500mm

CAPSTONE PARTNERS

FOREIGN ACQUIRERS

MACROECONOMIC FACTORS LIMIT CROSS-BORDER DEALS

- Despite loosened pandemic restrictions, the volume of deals involving a foreign acquirer has declined 8.5% YOY in Q1 2022 amid economic uncertainty.
- Concern surrounding Russia's war on Ukraine, potential antitrust scrutiny, interest rate increases, and foreign relations will be major factors in cross-border dealmaking throughout the remainder of 2022.
- The U.K. has continued to lead acquisitions of U.S. companies by foreign buyers through Q1. The Application Software sector has continued to attract the most buyer attention from foreign buyers amid heightened demand for digital solutions.



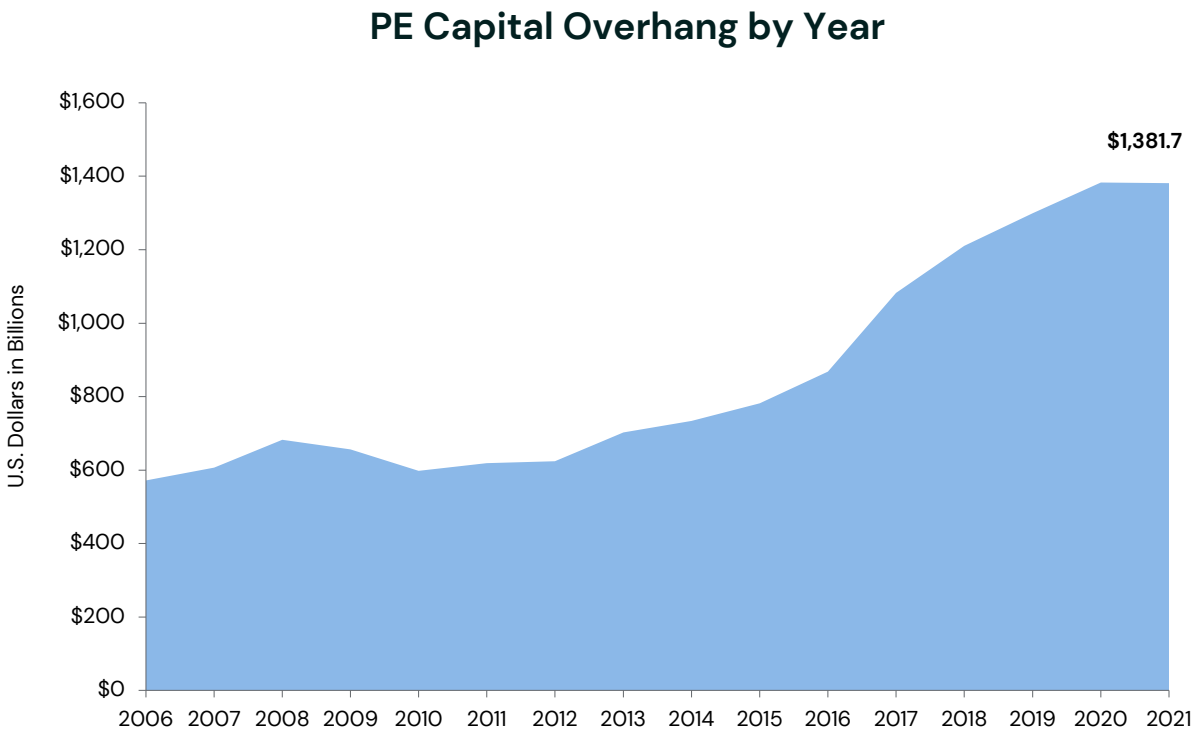
Source: Capital IQ
Enterprise Value < $500mm
Note: To ensure accuracy, data methodology has changed as of 2022 publication

CAPSTONE PARTNERS

PRIVATE EQUITY DRY POWDER

ELEVATED DRY POWDER SUPPORTS PE DEALMAKING

- While private equity firms have actively deployed capital to high growth sectors, capital overhang remains healthy at $1.4 trillion in June 2021, signaling elevated sponsor activity in the near term.
- Private equity firms continue to utilize sponsor-to-sponsor deals to rapidly scale platforms, increasing returns upon exit and spending down record levels of dry powder.
- Private equity firms have increasingly considered environmental, social, and governance (ESG) factors in investment theses, utilizing a holistic approach spanning the entire value chain to increase returns while rewarding sustainable business practices.



2021 dry powder figure as of June 30, 2021
Source: PitchBook

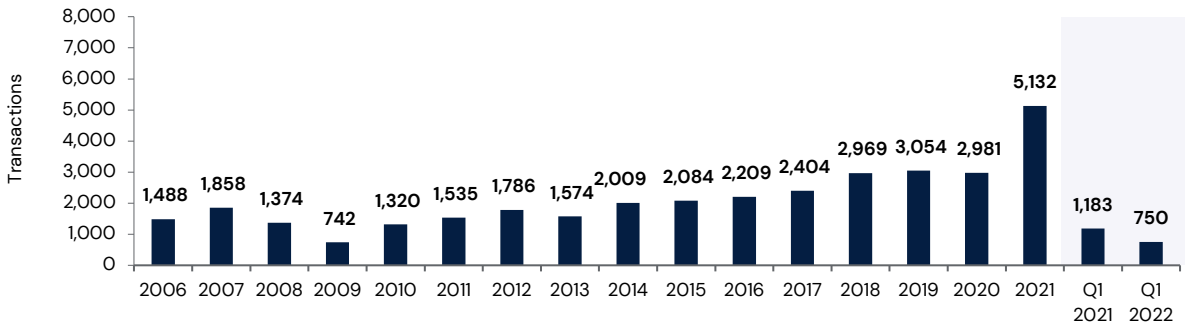
CAPSTONE PARTNERS

PRIVATE EQUITY ACTIVITY

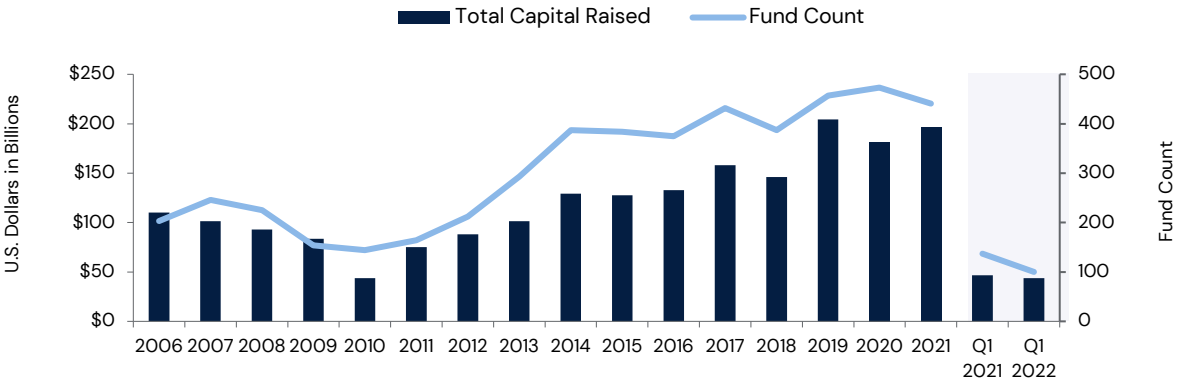
PE ACQUISITIONS DECLINE FROM HISTORIC HIGHS

- Private equity activity declined significantly from a historic 2021 with transactions closed by PE buyers falling 36.6% YOY in Q1 2022 and 52.2% from Q4 2021.
- Private equity fund count and total capital raised also endured YOY declines of 6.6% and 27% respectively as sponsors have slowed the speed at which they raise and deploy capital.
- 2021 was an unprecedented year for private equity firms as full-year closed deals increased 72.2% YOY. While private equity activity recorded a substantial decline from the rapid acquisition pace of 2021, deal volume has been healthy in 2022 relative to pre-pandemic years.

Middle Market Transactions Closed by Private Equity Firms



Middle Market Fundraising by Private Equity Firms



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

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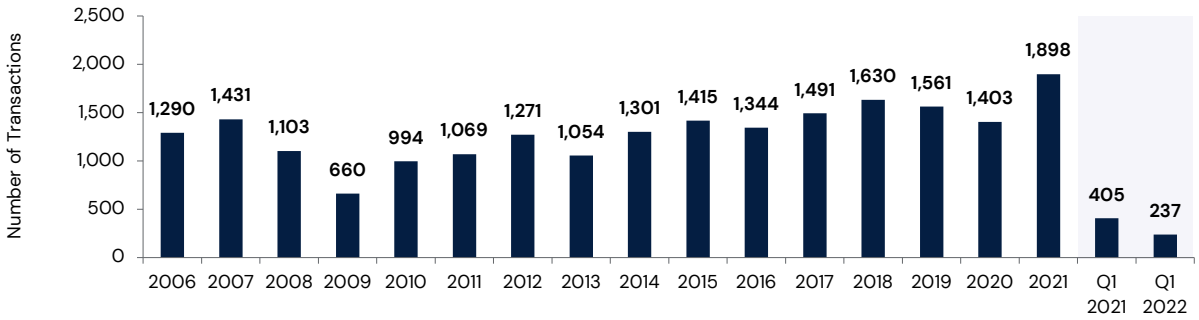
PRIVATE EQUITY TRANSACTION TYPES

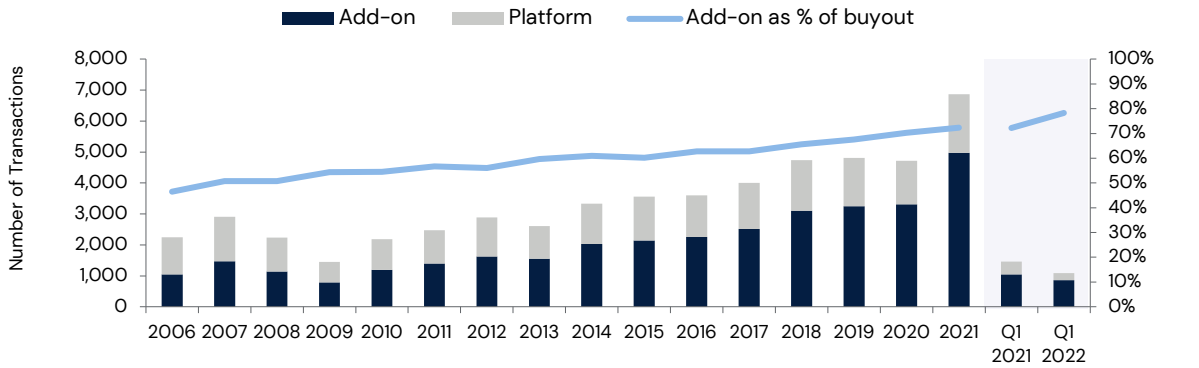
ADD-ONS COMPRISE GROWING SHARE OF PE DEALS

- Private equity platform acquisitions recorded a significant drop in quantity, falling 41.5% in Q1 2022 YOY as sponsors have focused on strengthening existing holdings following 2021's buying spree.
- Add-ons as a percentage of buyouts continue to rise as sponsors enhance platforms in promising sectors. Add-ons comprised 78.3% of buyouts in Q1 2022, compared to 70.9% in Q4 2021.
- With record capital overhang, private equity firms are expected to continue engaging in add-on acquisitions, bolstering market share in defensible spaces and ensuring liquidity for portfolio companies.

PE Platform Investments



PE Add-On Acquisitions



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

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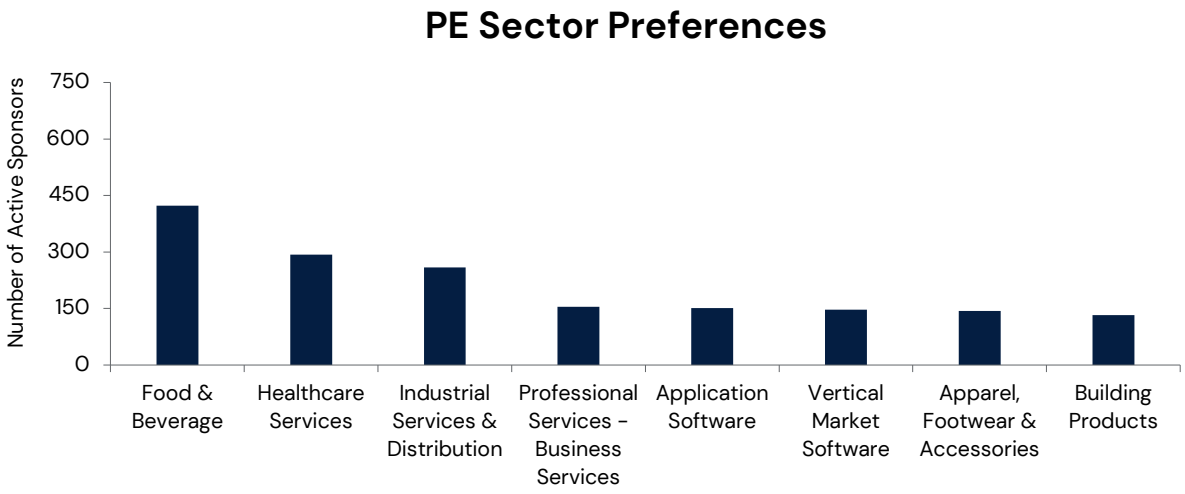
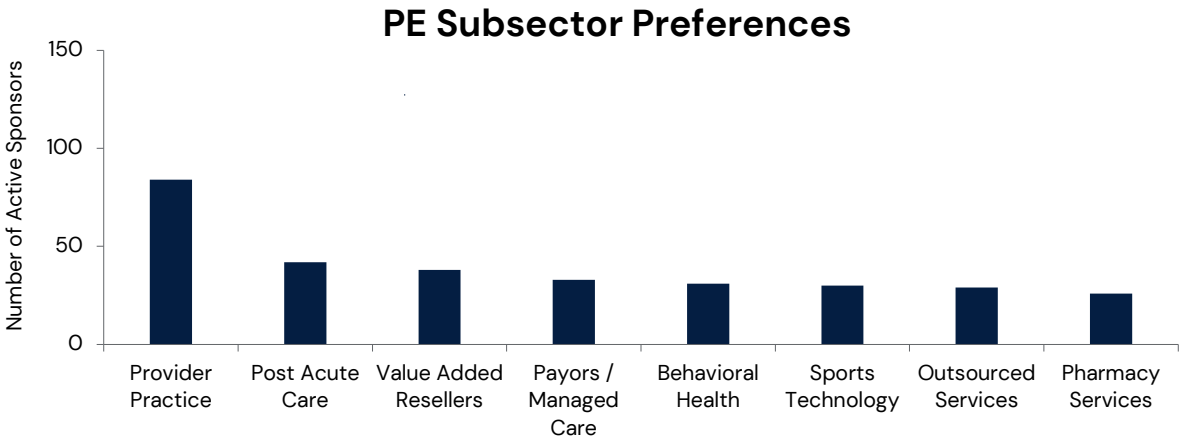
CAPSTONE'S PRIVATE EQUITY NETWORK PREFERENCES

FOOD & BEVERAGE CONTINUES TO BE TARGETED BY SPONSORS

- Sponsor activity has normalized to pre-pandemic levels in Q1 2022 as dealmakers carefully navigate economic uncertainty and focus on existing holdings.
- The Building Products sector has experienced increased sponsor interest in Q1 2022 as healthy construction backlogs, and the persistence of Residential and Nonresidential Construction markets supports a favorable market outlook.
- Valuation normalization is expected to support private equity acquisition activity as sponsors purchase quality assets without paying the premiums that buyers did throughout 2021.





Source: Capstone proprietary data

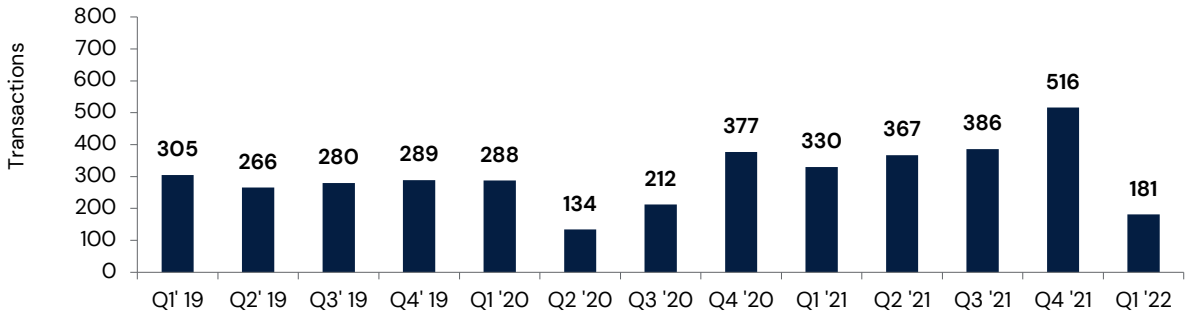
CAPSTONE PARTNERS

PRIVATE EQUITY ACTIVITY

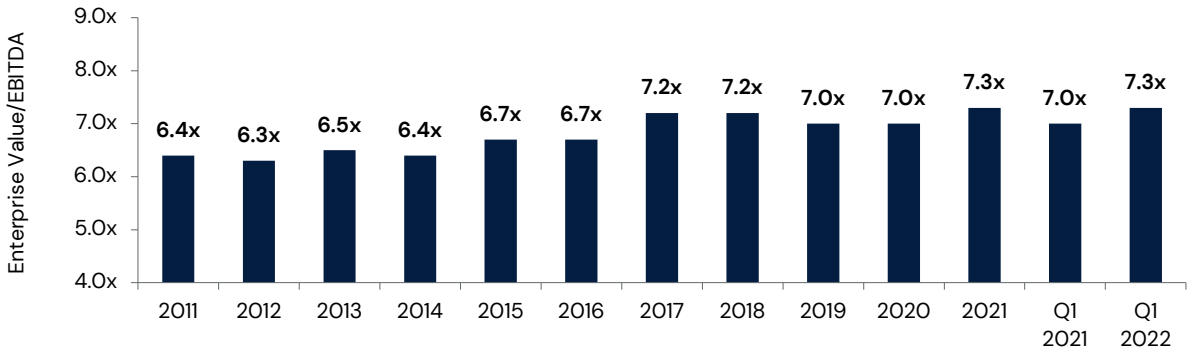
PE EXITS FALL AMID LOWER VALUATION ENVIRONMENT

- In Q1 2022, exit activity declined to its lowest level since Q2 2020 falling 64.9% from Q4 2021, as many sponsors extended hold periods for their portfolio companies due to volatility in performance driven by supply chain and labor challenges, and elevated input costs.
- The average transaction multiple paid by private equity firms rose to 7.3x EBITDA in Q1 2022, compared to 7.0x in Q1 2021. However, valuations fell from Q4 2021, which averaged 7.5x.
- Among sponsors, competition for high-quality assets remains elevated following an exceptional volume and valuation environment in 2021.

Private Equity Exit Activity



Average EBITDA Multiple Paid By Financial Buyers



Note: Exit activity inclusive of all enterprise value ranges
Source: PitchBook and GF Data®
Includes multiples 3x-15x; Enterprise Value $10mm-$250mm

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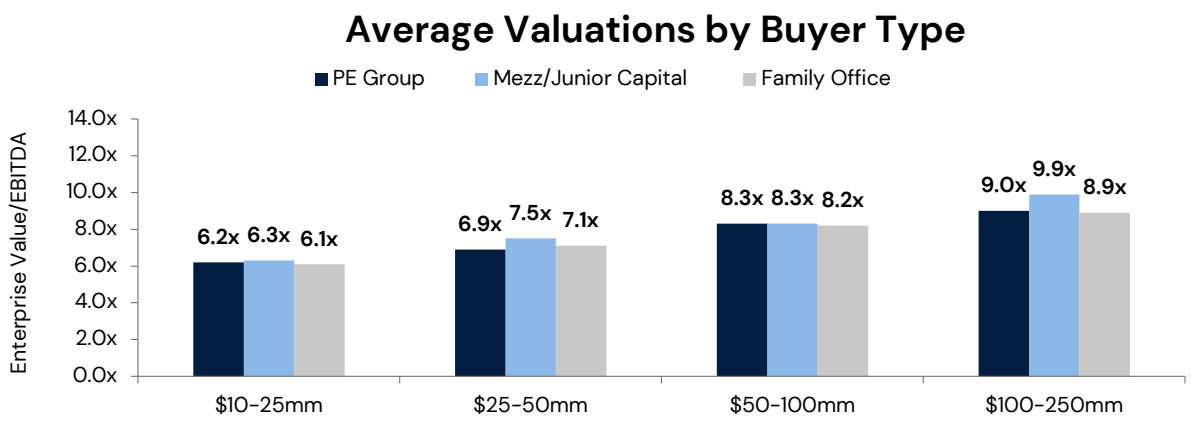
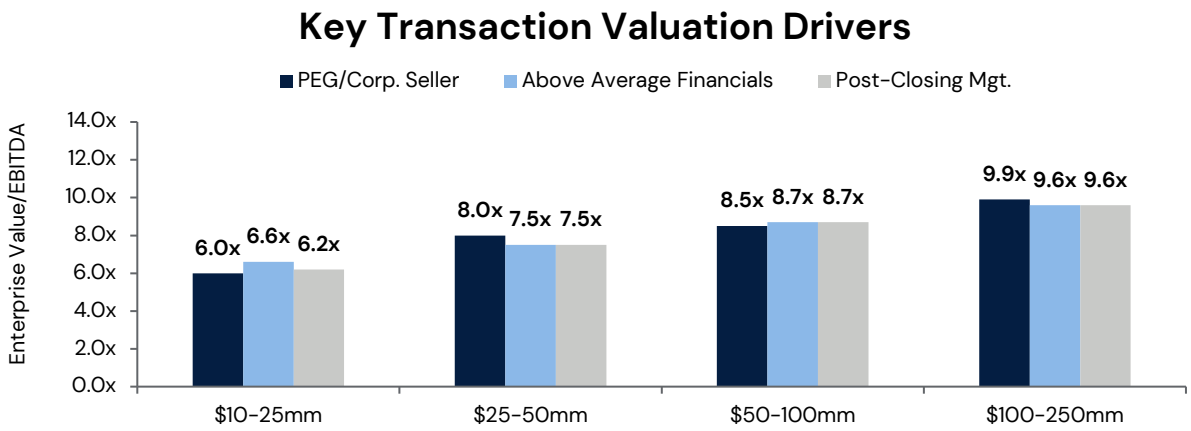
PRIVATE EQUITY VALUATIONS

EBITDA MULTIPLES PAID BY PE REMAIN ELEVATED

- While smaller businesses with differentiated offerings have garnered strong valuations in recent quarters, businesses in the larger enterprise value ranges continue to benefit from favorable pricing characteristics.
- Despite economic uncertainty, acquirers continue to pay premium multiples for companies with proven financials in growing markets, as well as larger assets being sold by private equity groups and other institutions.
- Companies with above average financials attracted the highest pricing in the $10-$25 million enterprise value range, demonstrating that buyers are pursuing stability amid volatility.





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

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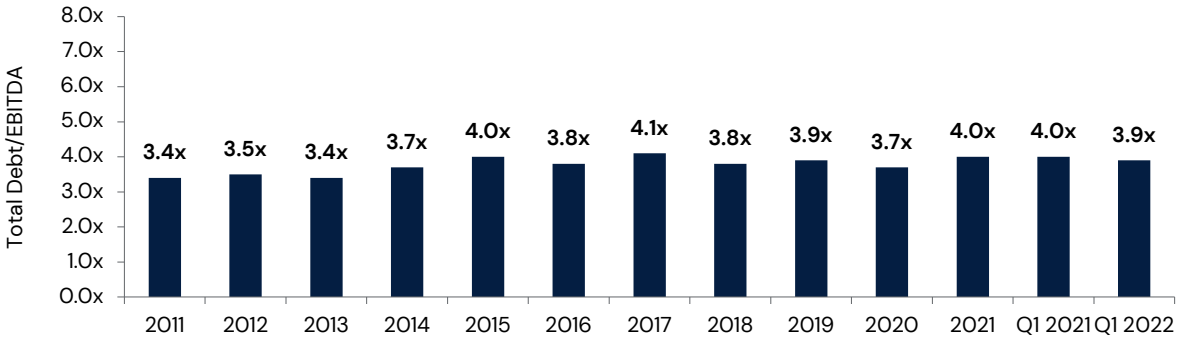
PRIVATE EQUITY VALUATIONS

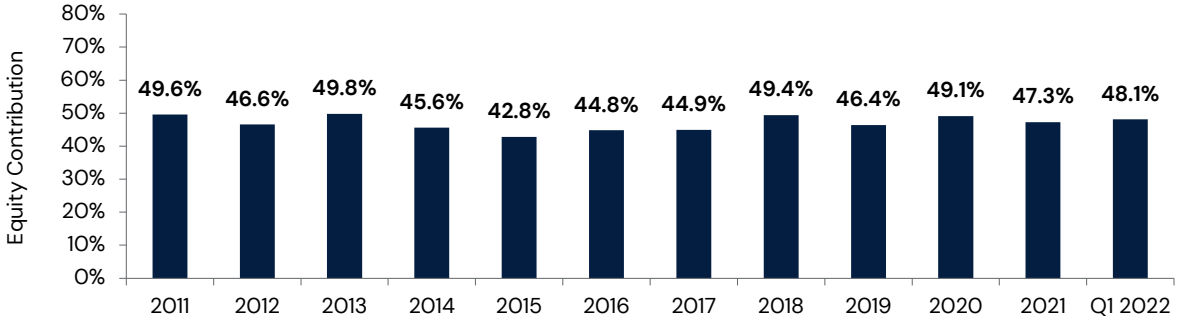
DEBT MULTIPLES DECLINE SLIGHTLY FROM 2021

- Average debt multiples remain healthy at 3.9x EBITDA in Q1 2022 as lenders continue to utilize leverage to win bids for strong assets.
- Average equity contributions reached 48.1% to-date, rising slightly from the full-year 2021 average. Equity contributions increased most dramatically for deals with enterprise values between $10-$25 million, rising to 50.5% from 35.6%.
- While buyer competition in M&A markets remains strong, a slight decline in debt multiples and a higher share of equity contribution in LBO deals may be attributed to a moderating valuation environment.

Average Debt Multiples of Middle Market LBO Transactions



Average Middle Market LBO Equity Contribution



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

Industry Groups

- Aerospace, Defense, Government & Security
- Building Products & Construction Services
- Business Services
- Consumer
- Education & Training
- Energy, Power, & Infrastructure
- FinTech & Services
- Healthcare
- Industrials
- Industrial Technology
- Technology, Media, & Telecom
- Transportation & Logistics

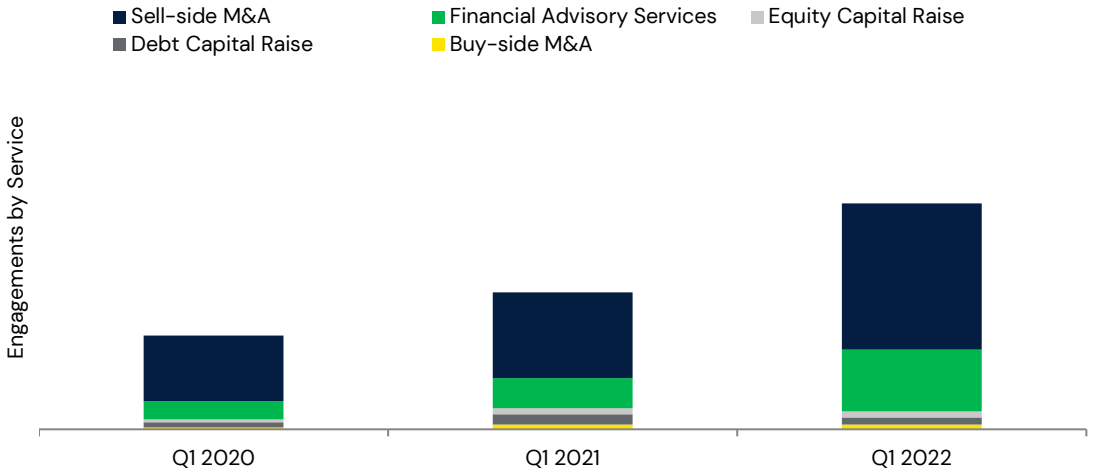
Sponsor Coverage Group

FIRM DATA

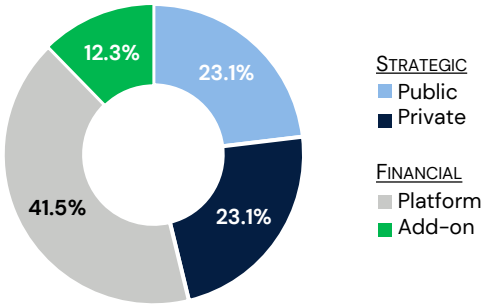
M&A VOLUME STAYS STRONG DESPITE UNCERTAINTY

- Sell–side M&A volume remained healthy in Q1 2022 as deal processes that were launched in the prior year closed and buyers continued to demonstrate an appetite for proven assets amid economic uncertainty.
- Private equity acquirers, leveraging elevated levels of capital overhang, have comprised the lion's share of activity. Financial buyers continue to build platforms in defensible sectors that stand to benefit from pandemic tailwinds.
- Rising inflation and interest rate increases will be major considerations for acquirers and business owners considering a liquidity event in 2022.

Capstone Engagements By Service



Capstone TTM Buyer Breakdown



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

CAPSTONE PARTNERS

RECENT DEAL CLOSINGS

Capstone is an active leader in middle market M&A advisory, serving many clients and their needs, despite the unprecedented disruptions to the economy. Select our recent tombstones below to read the full press release.

RESIDENTIAL WARRANTY SERVICES, INC. HAS BEEN ACQUIRED BY Porch	HAS BEEN ACQUIRED BY NAVIGANT OAK	MonroneyLabels.com HAS BEEN ACQUIRED BY LEADVENTURE a portfolio company of TRUE WIND	NOR-CAL CONTROLS STRATEGIC AND TRANSACTION ADVISORY SERVICES	HAS BEEN RECAPITALIZED BY maranon PROMISE HOLDINGS LLC.	MENOLABS HAS BEEN ACQUIRED BY amyris	Eaglestone HAS RECEIVED DEBT FINANCING FROM BMO Harris Bank
nationalgrid HAS DIVESTED VAMCO Water Heater Rentals	AATCarriers HAS BEEN ACQUIRED BY LOUISIANA TRANSPORT	Bolton REMOTE HAS BEEN ACQUIRED BY SUPPORT NINJA a portfolio company of bv	PROVISION CARES FINANCIAL ADVISORY AND INSOLVENCY SERVICES	innovate MR HAS RECAPITALIZED WITH CIVC PARTNERS	WEP HAS BEEN ACQUIRED BY E-CAPITAL EQUITY MANAGEMENT	sentara HAS BEEN ACQUIRED BY IBM
Aquasol CORPORATION HAS BEEN ACQUIRED BY GENCAP AMERICA	AMERICAN FARMS HAS BEEN ACQUIRED BY OSPREY CAPITAL	SIEGEL EGG CO. HAS BEEN ACQUIRED BY Rotunda Capital Partners	INKCUPS HAS BEEN ACQUIRED BY MPE PARTNERS	BRICATA. HAS BEEN ACQUIRED BY AN UNDISCLOSED STRATEGIC BUYER	VANGUARD HAS BEEN ACQUIRED BY FIDELITY NATIONAL FINANCIAL	COMMONWEALTH HAS BEEN ACQUIRED BY a portfolio company of Atarian

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.

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
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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.

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
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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.

LEADERSHIP TEAM (CONTINUED)

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
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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.

JIM CALANDRA, HEAD OF FINANCIAL ADVISORY SERVICES GROUP
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Jim has more than 25 years of experience in turnaround management consulting, interim management, fraud and forensic accounting, mergers and acquisitions, and recapitalizations. He has advised more than 50 companies through significant strategic transitions involving both public and private middle market companies with varying situations. Jim received a BS in Accountancy from Bentley University and an MS in Accountancy from The McCallum Graduate School of Business, Bentley University.

SARAH DOHERTY, DIRECTOR OF MARKET INTELLIGENCE
sdoherty@capstonepartners.com | 617-619-3310
Sarah has nearly 10 years of professional research, writing, and data visualization experience and leads the strategic coverage and development of Capstone's middle market insights. She manages the firm's Market Intelligence Team, which produces 150+ reports, articles, white papers, surveys, and capital markets updates each year. Her team's award-winning M&A commentary and analysis has been featured in more than 50 of the nation's top news outlets. Sarah earned a BA from Biola University and was recognized in 2021 with the "Emerging Leader Award" by the M&A Advisor.

Capstone Partners, a subsidiary of Huntington Bancshares Incorporated (NASDAQ: HBAN), has been a trusted advisor to leading middle market companies for over 20 years, offering a fully integrated range of 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 in multiple offices across the U.S. With 12 dedicated industry groups, Capstone delivers sector-specific expertise through large, cross-functional teams. For more information, visit www.capstonepartners.com.

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- Emerging industry trends
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