CIBC

CIBC CAPITAL MARKETS

US MIDDLE MARKET MONITOR

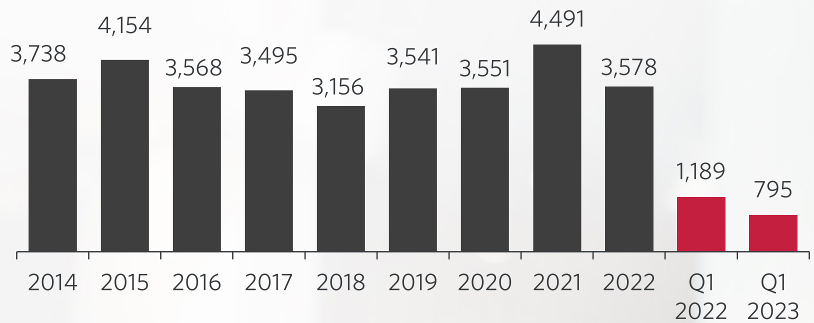
M&A and financing update

June 2023

CONFIDENTIAL

Deal volumes decline in challenging market

Annual number of US M&A transactions under $500mm



Q1 2023 deal activity was down 33% compared to Q1 2022, according to Robert W. Baird & Co. Rising interest rates, recession concerns, and a decline in public market valuations in the second half of 2022 weighed on dealmakers' willingness to transact.

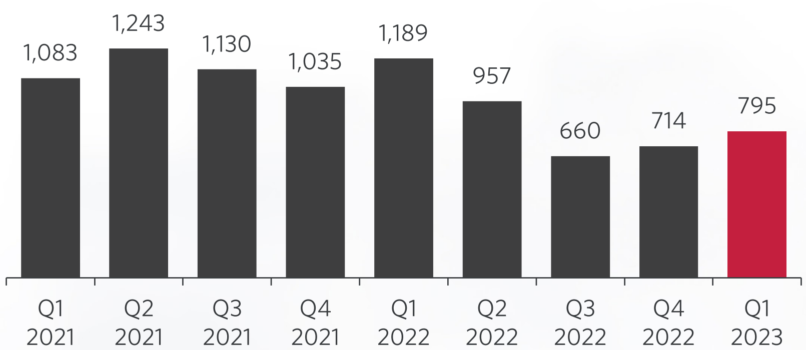
Despite headwinds, certain sectors continue to garner interest. Industrial companies with defensible market positions and attractive financials, as well as non-cyclical businesses providing facilities services, healthcare, and tech-enabled business services saw strong activity.

CIBC expects that Q2 2023 deal volumes will remain below Q2 2022 levels but anticipates increased activity in the second half of 2023 once the Fed stops hiking interest rates and buyers and sellers accept the reality of current market conditions.

Source: Robert W. Baird & Co.

Deal volumes decline in challenging market

Quarterly number of US M&A transactions under $500mm



While Q1 2023 was below Q1 2022, last quarter's deal count was 16% above the quarterly average during the second half of 2022.

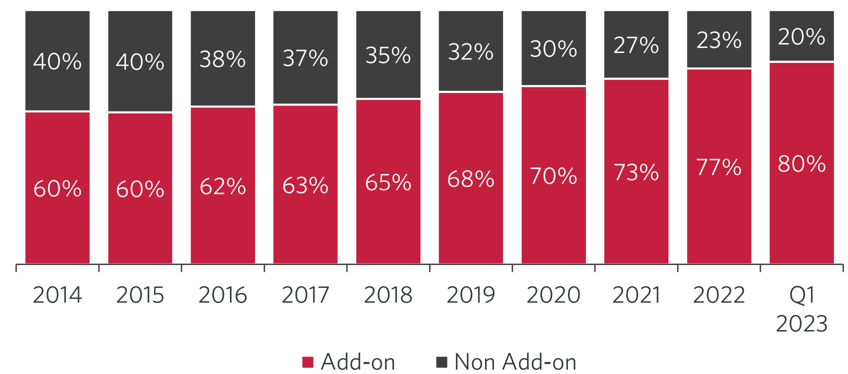
There are several positive dynamics that should support M&A activity throughout the remainder of 2023, including large cash balances on corporate balance sheets, significant levels of private equity dry powder, and a large number of portfolio companies nearing the end of their hold periods.

- At the beginning of 2023, U.S. public company cash balances exceeded $4 trillion, which is an increase of over 50% in the last four years.
- Private equity firms ended 2022 with over $775 billion of dry powder, according to Pitchbook, which is near record levels.
- Private equity firms have an increasing backlog of portfolio companies that will need to transact to return capital to LPs.

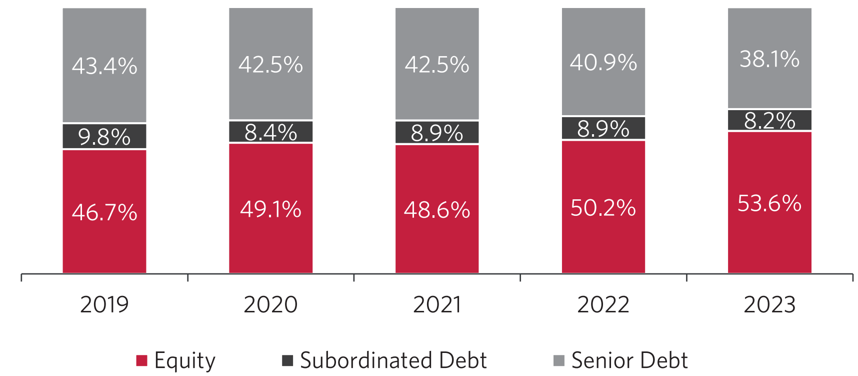
Source: Robert W. Baird & Co.

PE Sponsors adjust to new environment

Add-on % of US PE buyout transactions



Capital structure for $10 - $250mm deals



Last year was a record year for add-on activity, and that trend has continued in Q1 2023 with add-ons making up 80% of buyout transactions, according to Pitchbook.

Existing portfolio companies typically have available leverage and generally greater access to credit than new platforms, making acquisitions easier to finance as long as they are able to stay within their current credit agreement parameters. In the current valuation environment, platform companies can also often benefit from multiple arbitrage when making add-on acquisitions by either buying the add-ons at lower multiples or achieving sufficient scale to achieve multiple accretion.

Similarly, carveout transactions have had a resurgence in the past several quarters as public companies shed non-core assets and sponsors look for more attractively priced assets. From the end of 2021 to the end of 2022, carveout activity increased from 5.1% to 7.6% of total deal activity, representing a 49% increase.

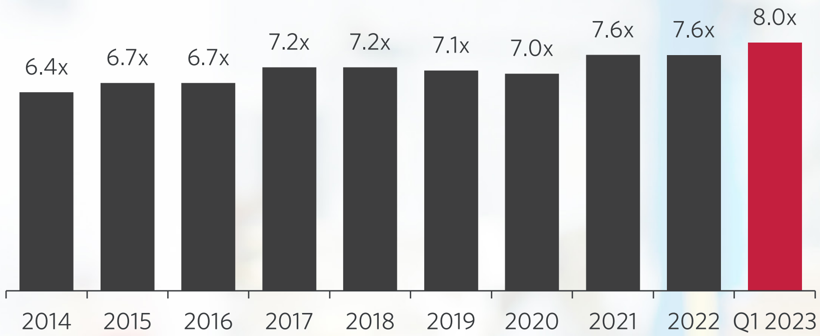
Sources: Pitchbook, GF Data®.

In Q1 2023, the average equity contribution across all transactions increased more than 3% from the 2022 average because valuation multiples have held for "A" assets and private equity funds are conservatively capitalizing transactions to account for higher interest rates and recession concerns. The equity contribution for new platform deals increased by over 4%, highlighting the challenges of financing standalone portfolio companies.

While larger buyouts have typically relied on direct lenders to support the leverage needs for transactions, smaller buyouts have required PE firms to invest more equity to support LBOs in the face of lower total debt availability. In a market with a limited supply of deals, PE firms are supporting transactions with more equity to provide higher surety to close for high-quality companies.

Valuations remain strong for high-quality companies

Average EBITDA multiples for $10mm - $250mm LBOs



Average EBITDA valuation multiples for LBOs under $250 million notched a strong start to 2023 at 8.0x, rebounding from 6.9x in Q4 2022.

Valuations in the lower middle market typically follow the broader market and many industry experts are anticipating reported valuation multiples will decline over the remainder of 2023 due to the effect of credit tightening and transactions for “average companies” closing at lower valuation multiples. Over the last several quarters there has also been a valuation gap between buyers and sellers, resulting in only the highest quality companies transacting which has influenced the higher average when compared to prior years when lower quality companies were transacting.

Source: GF Data®.

Valuations remain strong for high-quality companies

Average EBITDA multiples by Industry

Industry	2003 - 2018	2019	2020	2021	2022	Q1 2023
Manufacturing	6.8x	6.5x	6.7x	7.1x	7.3x	7.0x
Business services	7.1x	7.2x	7.1x	7.3x	7.4x	9.0x
Healthcare services	7.8x	8.0x	7.6x	8.1x	8.4x	9.5x
Retail	8.1x	9.3x	6.5x	8.3x	8.0x	5.7x
Distribution	6.9x	7.0x	7.5x	7.2x	7.2x	6.5x
Media & Telecom	7.8x	9.4x	8.3x	6.3x	9.1x	NA
Technology	9.6x	10.0x	7.6x	10.3x	8.1x	7.8x

GF Data's Q1 2023 breakdown of multiples by industry highlighted that healthcare services, business services, and manufacturing companies continue to trade at premium levels. These companies are either less cyclical or are benefiting from secular trends.

Not surprising, given the level of economic uncertainty, persistent inflation, and declining consumer spending, valuations on retail transactions declined 2.3x from the 8.0x average in 2022. Valuations for distribution and technology deals have also declined from 2022 highs due to softening demand and the collapse of Silicon Valley Bank roiling the lending market for technology deals.

Source: GF Data®.

Valuations remain strong for high-quality companies

Buyout quality premium

Description	2003 - 2018	2019	2020	2021	2022	Q1 2023
Above Average Financials	7.8x	7.6x	7.7x	8.2x	7.9x	9.2x
Other Buyouts	6.4x	6.3x	6.2x	6.4x	6.5x	6.4x
Premium / (Discount)	22%	21%	24%	28%	23%	44%
Incidence	58%	51%	54%	64%	67%	53%

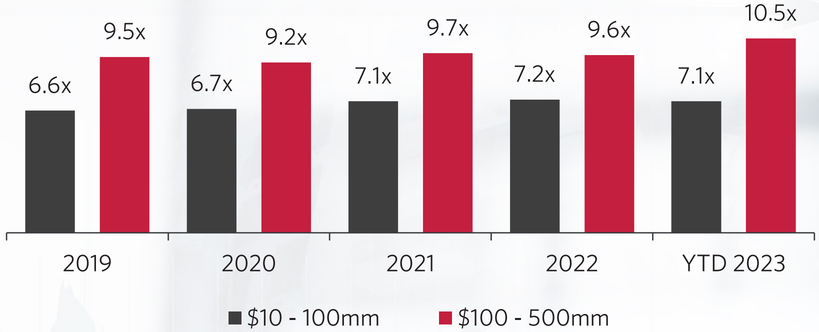
High-quality companies continue to attract premium prices. With more money chasing a limited number of deals, high-quality companies continue to trade at strong premiums. During Q1 2023, PE firms paid, on average, 44% more for companies with above-average financial performance. Although high-quality assets continue to trade at 2021 premiums due to scarcity, there are some significant differences in current processes:

- More thorough due diligence than in 2021 due to the benefit of additional time and resources.
- Significant attention paid to sustainability of margins given the impact of inflation and supply chain disruptions.
- Higher scrutiny on aggressive or unsubstantiated EBITDA add-backs and adjustments.

Source: GF Data®.

Valuations remain strong for high-quality companies

Buyout size premium



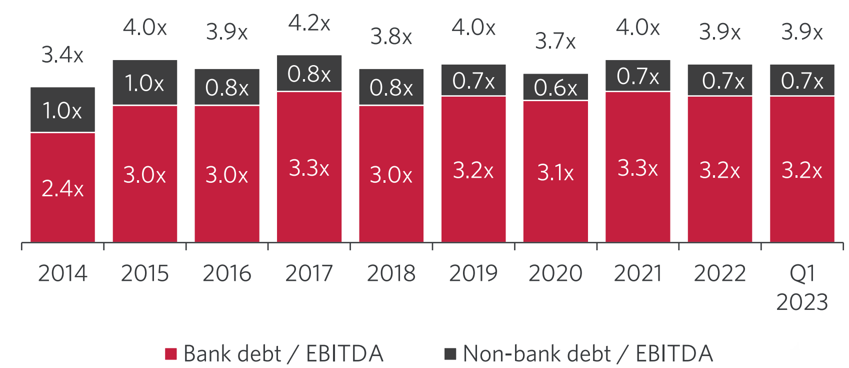
Larger companies continue to trade at premium multiples, despite a challenging syndicated debt market. The spread between $10 to $100 million and $100 to $500 million deals has increased to 3.4x, compared to 2.4x in 2022.

The premium continues to be influenced by these companies having well-established strategies and management teams, customer and product diversification, and institutionalized processes and procedures. While less common, smaller companies with these characteristics are also fetching premium multiples.

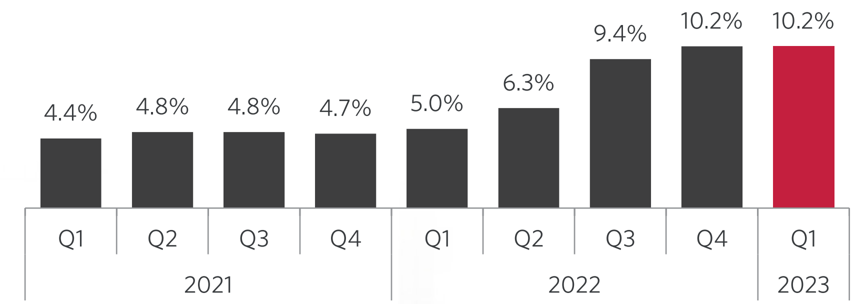
Source: GF Data®.

Debt markets remain challenging

Average LBO debt multiples for $10mm - $250mm LBOs



Quarterly average cost of debt



Although the data shows a modest decline in leverage, over the course of 2022, financing became more challenging as the cost of debt increased and availability decreased. Credit markets have continued to tighten in 2023 with rising interest rates and bank failures like Silicon Valley Bank. Direct lenders remain active in the LBO market; however, their pricing is up, total leverage is down, and hold sizes are smaller.

Rising interest rates have negatively impacted free cash flow and fixed charge ratios, limiting credit availability. CIBC expects credit availability to expand as lenders and dealmakers get more visibility into the trajectory of Fed rate hikes and the economic cycle. However, leverage availability will continue to be constrained compared to total debt availability over the last five years until rates decline.

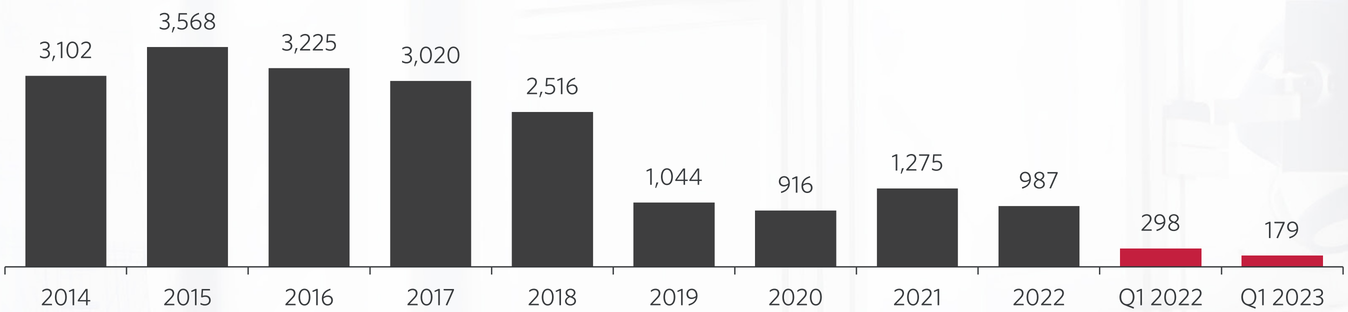
During 2022, dealmakers witnessed the fastest credit tightening cycle in decades. The average cost of debt more than doubled and caused a significant pullback in the amount of available leverage.

Although elevated interest rates do not significantly impact investor returns, they do impact available leverage and, ultimately, valuation. According to Robert W. Baird & Co., transactions are able to support 1.0x - 1.5x fewer turns of debt in Q1 2023 when compared to Q1 2022.

Source: GF Data®, Pitchbook, RW Baird & Co.

Hot M&A market for “A” industrial companies

US industrial M&A transactions



The industrial M&A market has been strong for high-performing companies with defensible market positions and lower-quality companies have struggled to transact. CIBC has noted several strategic characteristics in each of the “A” companies that have transacted since COVID. These characteristics include:

- **Commitment to automation and capacity growth** – “A” companies have invested in high-ROI projects that have positively impacted gross margins, operational efficiencies, capacity, and reduced overall headcount.
- **Strong engineering and technical knowledge** – The companies have filled the engineering gap created by OEM’s underinvesting in their engineering teams during and after COVID. Suppliers that hadthe engineering depth to supplement the OEM’s team became “strategic partners” and often avoided competitive request for proposal processes for new production work.
- **Strategic customer focus** – Strong management teams recognized the opportunity to become a critical and strategic partner with a focus on high-margin, collaborative work. To free up capacity for strategic partners, they fired small or low margin customers.
- **Visionary leadership** – Strong C-level executives with a clearly articulated and defined 3- to 5-year strategic growth plan that the company is executing and achieving.
- **Outstanding financial performance** – These companies all are achieving 10-30% annual sales growth, 25-50% gross margins, and 20-40% EBITDA margins with a multi-year history of margin expansion.

Buyers are paying premium prices for these “A” companies and processes for lower quality companies are either failing or the deals are getting pulled. We expect this trend to continue in 2023.

Source: Pitchbook.

Hot M&A market for "A" industrial companies

M&A multiples for $10mm to $250mm industrial transactions

Transaction Size	2003 - 2018	2019	2020	2021	2022	Q1 2023	Above Average
$10 – 25mm	6.3x	5.6x	5.9x	6.0x	6.2x	5.7x	6.3x
$25 – 50mm	6.1x	6.3x	6.6x	6.8x	7.2x	7.0x	7.1x
$50 – 100mm	8.3x	6.9x	7.7x	8.0x	8.2x	7.0x	8.3x
$100 – 250mm	7.7x	8.7x	7.4x	8.5x	9.0x	9.7x	9.9x
Total	**6.8x**	**6.5x**	**6.7x**	**7.1x**	**7.3x**	**7.0x**	**8.1x**

According to GF Data, EBITDA transaction multiples for $100 to $250 million transactions have increased 2.0x from 7.7x in 2018 to 9.7x in 2022. The significant premium being paid for these industrial businesses are driven by the flight to quality for "above average" companies (defined as institutional ownership, 15% EBITDA margins and continuing management). The chart above shows that on average, above-average companies are transacting at an 8.1x average EBITDA multiple, which is a full turn above industrial companies that only have one or two of the above average characteristics.

The emergence of growth equity buyers in the industrial market has created unexpected competition for many of the operationally-focused industrial private equity funds who rarely had premium payers competing for good deals just four years ago. The growth buyers have entered the industrial market and brought with them: speed to close (30 days or less), no financing contingencies (including closing all equity), and deep pockets to support organic and inorganic growth initiatives.

We expect that despite a few headwinds, valuations and the outlook for "A" industrial assets will remain frothy for the remainder of 2023.

Source: GF Data®.

CIBC US Middle Market at-a-glance

Highlights

Provide M&A advisory services to CIBC clients and other relationships.

24 professionals in Milwaukee collaborating seamlessly with other CIBC business units.

Clients include **private companies, private equity funds, and corporations.**

Differentiated approach to achieving client goals through disciplined and transparent transaction processes.

Investment banking services

M&A Advisory

- Execute transactions up to $500 million in enterprise value
- Specialize in sell-side transactions
- Conduct targeted buy-side advisory services

Capital Placement

- Raise up to $250 million in debt and/or equity
- Provide capital structure advice for management buyouts and recapitalizations

Financial Advisory

- Strategic alternative analyses
- Special situations transactions

Focus industry verticals

Consumer

Business Services

Healthcare

Industrials

Software & Technology

Recent CIBC US Middle Market transactions

STOCKD SUPPLY
has been acquired by
BLACKHAWK INDUSTRIAL
a portfolio company of
TRUARC PARTNERS

AAR
has acquired
Trax

LAKE AIR PRODUCTS
has been acquired by
P4G CAPITAL

GT GOLF SUPPLIES
a portfolio company of
HADLEY
has been acquired by
KINZIE CAPITAL PARTNERS

TRANSHIELD
Advanced Protective Cover Technology
has been acquired by
PATRICK

AMEREQUIP
has been acquired by
JMC FAMILY OFFICE

KOREOUTDOOR
a portfolio company of
FULCRUM CAPITAL PARTNERS
has been acquired by
Ironbridge EQUITY PARTNERS

LIGCHINE
a portfolio company of
Blue Sage Capital
HANOVER PARTNERS, INC.
has been acquired by
RAF

united envelope
has been acquired by
CenterGate CAPITAL

FIBERESIN INDUSTRIES, INC.
has been acquired by
ABET LAMINATI
Unlimited selection

BELLA ELEVATOR
has been acquired by
Cibes

MIRAGE TRAILERS
a portfolio company of
CRESCENDO CAPITAL PARTNERS
OFS
FIDUS Capital
has been acquired by
Novae
a portfolio company of
BRIGHTSTAR CAPITAL PARTNERS

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