

## Middle-Market Review Summer 2009

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**WEST RIDGE ASSOCIATES, LLC** provides merger and acquisition, corporate finance and related investment banking services to established middle market businesses, earlier stage companies with high growth potential, and commercialization stage companies in all industries.

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## WEST RIDGE ASSOCIATES, LLC SUMMER 2009 MID-MARKET REVIEW

### CURRENT ECONOMIC CONDITIONS

In the midst of the worst economic recession that the U.S. has faced in five decades, there appear to be signs that conditions have bottomed out and are beginning to improve:

- The Dow Jones Industrial Average, often viewed as a leading economic indicator, has surpassed the 9,000 level, after dropping to a decade low of 6,542 in March.



- There are signs that the rate of decline in GDP growth is slowing. GDP shrank at a better-than-forecast 1 percent annual pace after a 6.4 percent drop the prior three months, reported the Commerce Department on July 31.
- The housing market is showing signs of stabilization. New home sales rose 11% in June to a 384,000 annual pace. Existing home sales have risen for the past three months. The S&P/Case-Shiller home-price index, a gauge of U.S. home prices, rose 0.5 percent in May from the prior month, the first gain since July 2006 and biggest since May of that year.

## CURRENT ECONOMIC CONDITIONS (cont.)

However, there are signs that the economy is still weak and has a way to go before we dig our way out of this recession:

- The credit crunch continues and lending continues to slow. According to the Wall Street Journal, the total amount of loans held by 15 large U.S. banks shrank by 2.8 percent in the second quarter and more than half of the loan volume came from mortgage refinancings and credit renewals to businesses, not new loans. Also, loan sales by banks to other institutions continue to fall.
- Massive U.S. government bond sales to fund the stimulus and the budget deficit continue to fuel inflation fears.
- Interest rates on U.S. Treasury securities have increased at recent auctions.
- Unemployment shows no signs of slowing and is expected to reach or exceed 10 percent this year. Lawrence Summers, director of the White House National Economic Council, said that while the economy will resume growth in the second half of the year, the job picture “will be serious for some time to come.”

So what's the good news?

- With valuations down and some indications that we may have passed the bottom of the recession, strategic buyers appear to have increased interest in acquisitions.
- A consensus appears to be building that the recovery will be slow, of the “U” shaped variety rather than the “V”. While that is not great news for sellers of businesses in terms of valuations, at least there is increased predictability that supports M&A activity.
- Government pressure to increase lending activity and more predictability generally should continue the slow thaw in credit availability. Private equity buyers appear to be resigned to less leveraged transactions. There is considerable incentive for private equity funds to put capital to work.
- Investors may be coming to grips with a new reality in which their choices are an adjustment in expectations or ceasing activity. We believe they will continue to make the best of a bad situation for the time being.

## LOWER MID-MARKET M&A ACTIVITY

<b>U.S. Lower Mid-Market<sup>(1)</sup> M&amp;A Transaction Metrics</b> (comparing Q2 year-over-year)						
Deal Size (\$ in MM)	Number of Deals			Aggregate Value(\$ in MM)		
	Q2 2008	Q2 2009	Q/Q % Change	Q2 2008	Q2 2009	Q/Q % Change
\$200-\$250	23	18	-21.7%	\$5,131.5	\$4,021.2	-21.6%
\$150-\$200	32	17	-46.9%	5,562.8	2,970.2	-46.6%
\$100-\$150	58	30	-48.3%	7,101.1	3,694.4	-48.0%
\$50-\$100	129	54	-58.1%	9,278.2	3,738.1	-59.7%
Under \$50	729	546	-25.1%	8,508.1	5,556.4	-34.7%
<b>Total</b>	<b>971</b>	<b>665</b>	<b>-31.5%</b>	<b>\$35,581.7</b>	<b>\$19,980.3</b>	<b>-43.8%</b>

(1) Lower middle-market defined as transaction value < \$250MM

(2) Based on announced transactions

Source: Capital IQ

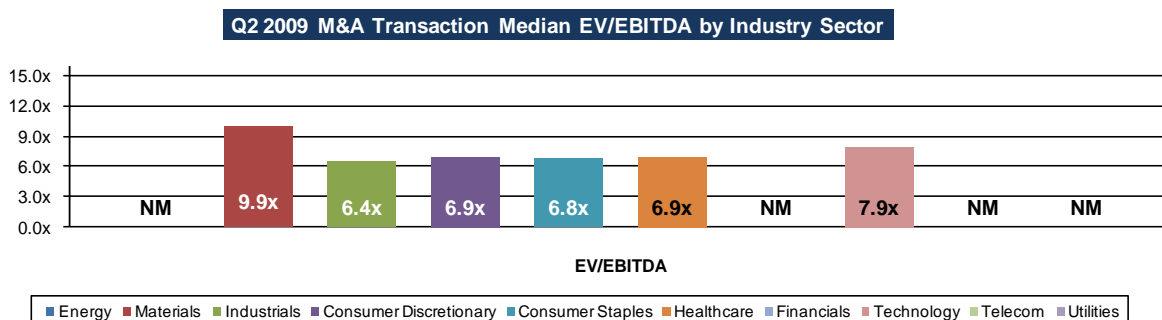
<b>U.S. Lower Mid-Market<sup>(1)</sup> M&amp;A Transaction Metrics</b> (comparing consecutive quarters)						
Deal Size (\$ in MM)	Number of Deals			Aggregate Value(\$ in MM)		
	Q1 2009	Q2 2009	Q/Q % Change	Q1 2009	Q2 2009	Q/Q % Change
\$200-\$250	9	18	100.0%	\$1,943.5	\$4,021.2	106.9%
\$150-\$200	14	17	21.4%	2,286.6	2,970.2	29.9%
\$100-\$150	25	30	20.0%	3,060.3	3,694.4	20.7%
\$50-\$100	40	54	35.0%	2,792.6	3,738.1	33.9%
Under \$50	510	546	7.1%	4,638.3	5,556.4	19.8%
<b>Total</b>	<b>598</b>	<b>665</b>	<b>11.2%</b>	<b>\$14,721.3</b>	<b>\$19,980.3</b>	<b>35.7%</b>

(1) Lower middle-market defined as transaction value < \$250MM

(2) Based on announced transactions

Source: Capital IQ

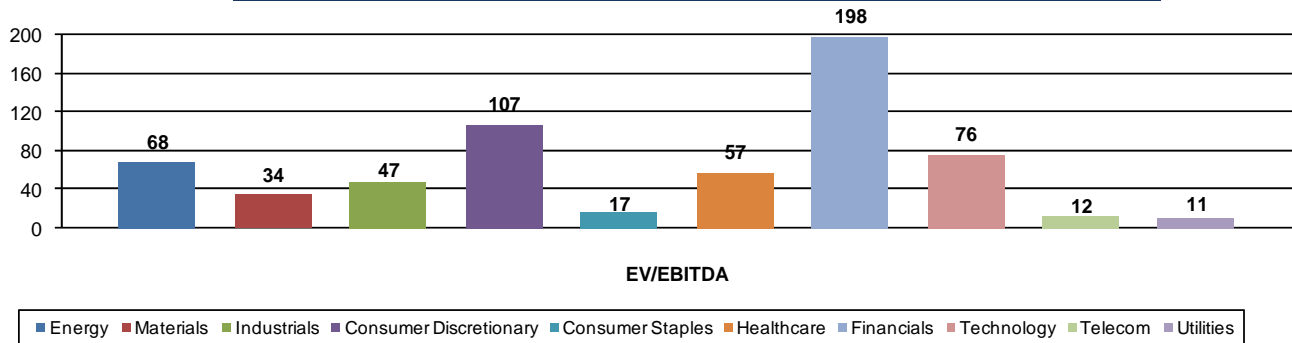
- The pace of lower-middle market M&A in Q2 2009 remains significantly down from Q2 2008 levels. However, the approximately 11 percent increase in transaction volume and approximately 36 percent increase in aggregate transaction value in Q2 2009 versus Q1 2009 suggests we may have passed the nadir or at least see the beginning of some stabilization.



Source: Capital IQ

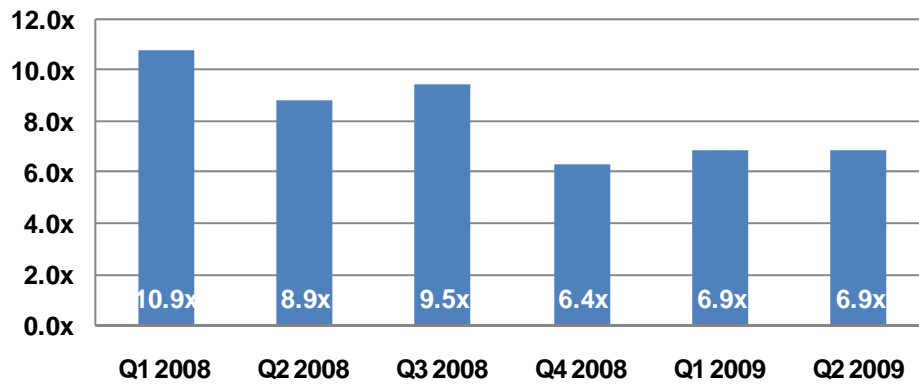
## LOWER MID-MARKET M&A ACTIVITY (cont.)

**Q2 2009 Number of Lower-Middle Market<sup>(1)</sup> M&A Transactions by Industry Sector**



Source: Capital IQ

**Median Disclosed EV/ EBITDA Values for Lower-Middle Market<sup>(1)</sup> M&A Transactions**



(1) Lower-middle market defined as transaction value < \$250 MM  
Source: Capital IQ

## LOWER MID- MARKET PRIVATE EQUITY FINANCING ACTIVITY

Q2 2008/Q2 2009 Private Equity Investments Below \$25MM Transaction Value						
Deal Size (\$ in MM)	Number of Deals			Aggregate Value(\$ in MM)		
	Q2 2008	Q2 2009	Q/Q % Change	Q2 2008	Q2 2009	Q/Q % Change
\$20.0 - \$25.0	57	46	-19.3%	\$1,279.4	\$994.2	-22.3%
\$15.0 - \$19.9	72	33	-54.2%	1,179.9	520.2	-55.9%
\$10.0 - \$14.9	101	87	-13.9%	1,167.0	986.1	-15.5%
\$5.0 - \$9.9	184	173	-6.0%	1,219.3	1,140.5	-6.5%
Under \$5.0	559	765	36.9%	946.2	963.1	1.8%
<b>Total</b>	<b>973</b>	<b>1,104</b>	<b>13.5%</b>	<b>\$5,791.8</b>	<b>\$4,604.1</b>	<b>-20.5%</b>

Source: Capital IQ  
Based on announced transactions

- Middle-market private equity transactions are showing signs of revitalization. The number of private placements with transaction values of less than \$25 million increased approximately 14 percent Q2 2009 vs. Q2 2008. This compares with a decrease in such transactions of approximately 31 percent Q1 2009 vs. Q1 2008. While the Q2 2009 over Q2 2008 increase gives us reason for optimism for the resurgence of private equity financings, we are still cautious. Many of these transactions may represent equity infusions by private equity firms into their portfolio companies to provide liquidity no longer provided by the credit markets.
- Venture Capital investments increased by 15 percent in terms of dollars in Q2 2009 from Q1 2009, but remains at mid-1990 levels according to the MoneyTree™ Report from PricewaterhouseCoopers and the National Venture Capital Association (NVCA). Mark Heesen, president of the NVCA, remarked, "Halfway through 2009 we are seeing more positive signs than at the beginning of the year, including an ongoing interest in seed and early stage funding."

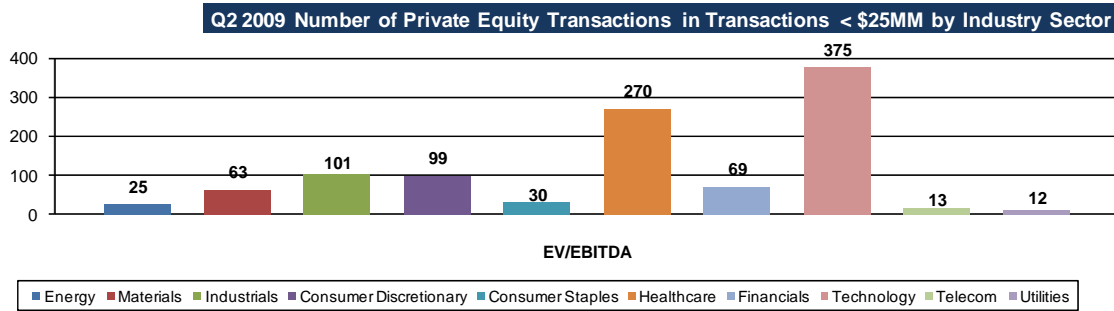
### Q2 2009 Most Active Private Equity Investors in Transactions < \$25 MM

Firm	# of Deals
Ben Franklin Tech. Ptrs.	10
Iroquois Capital	10
Kleiner, Perkins, Caufield & Byers	9
Alpha Capital	7
DAG Ventures	7
Polaris Venture Partners, Inc.	7
Venrock	7

- Ben Franklin Technology Partners and Iroquois Capital led all institutional investors in private equity transactions of less than \$25 million with each completing 10 private placements in Q2 2009.

Source: Capital IQ

## LOWER MID- MARKET PRIVATE EQUITY FINANCING ACTIVITY (cont.)



Source: Capital IQ

- The vast majority of the private equity financings in Q2 2009 occurred within the Healthcare and Technology industries. Within the Healthcare industry most of the financings took place within the life sciences sector (primarily biotechnology and medical devices). Within the Technology industry, most of the financings took place within the software sector. The clean technology sector, which crosses over primarily into the Energy, Industrials, Materials, and Technology industries saw a healthy increase in financing activity in Q2 2009, probably spurred by the stimulus package and clean energy legislative activity.
- According to MoneyTree™, seed and early stage investing skyrocketed 67 percent in terms of venture capital dollars invested in Q2 2009 versus Q1 2009, while expansion stage investments increased 19 percent. Q2 2009 first-time financing (companies receiving venture capital for the first time) dollars increased 9 percent compared to Q1 2009. Investments in later stage deals, however, decreased 20 percent in dollars in Q2 2009.