The McLean Group
INVESTMENT BANKING

M&A Market Update©

Your source for information about today's mergers & acquisitions market January 2009

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About Us

The McLean Group is a national, middle market investment bank serving businesses generating up to $500 million in annual revenues. For more information, visit www.mcleanllc.com.

Feature Article:
Rethinking the Value of Net Operating Losses After the Bailout

By Brian A. Sullivan CPA/ABV, CVA, CBA, CFE

Without a doubt, 2008 will go down in the history books as one to remember. As 2009 begins, the unparalleled uncertainty facing the global financial markets will give many middle market business owners reason to pause and focus their efforts on survival. Yet, in this troubled time, there will be opportunities for those businesses that can take advantage of their positions in the marketplace and with the help of specific and focused legislation may find some value where there once was only despair.

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Expert Tips:
How Much Are You Worth?

Determining Value and the Value of Equity in Your Business

By Dennis Roberts, CPA*/ABV, CVA

Edited by Jen Jackson

In the current buyer's market it is very important that sellers understand what a buyer wants and needs out of an acquisition. It is also key that sellers understand where the value in their business lies. Although cash flow of a business is significant in the decision making process, it is not the only factor in the value and price that a business will sell for. Sellers who understand the components that buyers use to assess value in business, they may be able to enhance the value of their businesses as they continue the selling and negotiating processes.

Components that increase the value of a company may include net operating assets, non oper-

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*Formerly practicing CPA

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ating assets as well as the business' intangible value which itself is usually a function of cash flow (net income). The net operating assets of a company include assets used in the business, including property or other inventory, accounts payable and other accumulated liabilities (not including financial long term debt used to finance or acquire the business in lieu of equity put into it by the owners). The intangible assets include the company's good name and good will, brand recognition and its current customer base. Intangible assets are implicit benefits of acquisition and as aforesaid are usually valued based on the business cash flows or net income.

Additionally, buyer may foresee post-acquisition synergies between their current businesses and those they are seeking to acquire. For example if Company A, a smaller company with a strong emphasis in one area, is sold to Company B, a large company with a weakness in that same area, then the Company B buyer is going to realize that the business could grow exponentially with the acquisition of Company A. Whilethis could add a great deal of value to the purchase, however post-acquisition synergies are unique to every buyer, and the seller does not have much influence on this component. A qualified investment banker is paramount in pinpointing synergistic relationships between buyers and sellers, and will provide both parties with invaluable insight into the benefits of the acquisition.

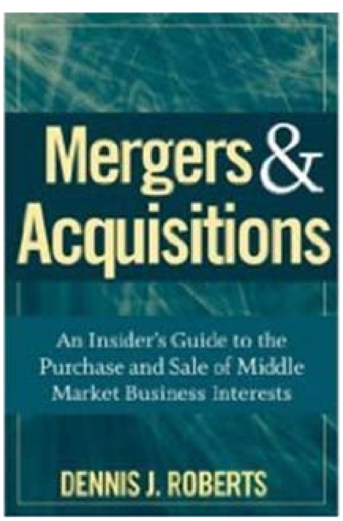
Conversely, the value of a business' equity will diminish by the amount of its financial liabilities. Financial liabilities include bank loans, term loans, mortgages and any other debts (interest bearing or not) that are used in long term business financing. It does not include the liabilities that are taken in to consideration in determining net operating assets (see above).

Determining the "worth" of a business might be one of the harder parts of the transaction process. Both buyer and seller assess worth on different facets of a company. If a seller is more aware of what the buyer is looking for they may be able to enhance the value of their company and therefore increase their profit once a transaction has been completed.

Source: *Mergers & Acquisitions: An Insider's Guide to the Purchase and Sale of Middle Market Business* by Dennis Roberts, See below.

Release of Chairman's Book:

Mergers & Acquistions: An Insider's Guide to the Purchase and Sale of Middle Market Business Interests



Available February 3, 2009 at amazon.com

The above article was a chosen edited selection from Dennis Roberts' new book. Roberts is the Chairman of The McLean Group, and his book is set to be released on February 3, 2009. The book was designed not only for owners and managers of middle market businesses but as a training text for middle market M&A investment bankers and consultants. It discusses the art and science of middle market M&A as well the all-important psychology and behind-the-scenes negotiations pursued with a particular emphasis on obtaining the absolute highest value when selling a business. Subjects addressed include valuation, taxation, negotiations, M&A conventions, among many others from the buy-side and sell-side perspectives.

Subtitled "Tales of A Deal Junkie," this serious but occasionally irreverent book tells it like it is, including anecdotes to provide a "feel" for what really goes on in middle market transactions. The author, a former practicing CPA and a business valuation expert, is a veteran M&A investment banker with many years of real life experience. He also is a widely-acclaimed instructor in the M&A field and a nationally-respected practitioner who has trained thousands of investment bankers. No comparable book on the market today provides this degree of comprehensive and invaluable insight.

Trends To Act On:
Paradigm Shifts in Waning Economy

By Sam H. Huang

Tight credit markets are forcing deal sponsors to invest more equity per transaction with less borrowed capital, resulting in approximately 10% decline in target valuations since the third quarter of 2007. This market change, together with frozen credit markets, has shifted the negotiating leverage from Sellers to Buyers. The following M&A market trends are likely to persist in 2009:

- The return of traditional "financing out" conditions to Buyers based on credit market turmoil with fewer "reverse breakup fees" for middle market transactions.
- An increasing percentage of purchase price considerations paid in Buyer's cash/stock as opposed to debt financing proceeds.
- Increased prevalence of Seller take-back financing, retained equity or purchase price earn-outs to satisfy declining lender leverage ratios and to bridge Seller valuation/purchase price expectations.
- More frequent post closing purchase price adjustments to reflect adverse changes in pre-closing net working capital or post closing EBITDA results secured by post closing escrows...
- Extended due diligence periods enabling Buyers and lenders to discern, if possible, unforeseen consequences of the current economic slowdown.
- Further implementation of specific provisions and benchmarks allowing Buyers to walk away from transactions without liability should Seller-related financial and business conditions deteriorate following the signing M&A agreements.

As always, in good times and challenging ones, the support and insights of an investment banker can help middle market sellers and buyers alike identify unique opportunities while others remain on the sidelines.

Source: "M&A Trends in Today's Turbulent Credit and Economic Market", *Corporate & Finance Alert.*

Exit Planning:
When is the Right Time to Sell a Business?

By Enrique Brito, CFA, AVA, CM&AA

Determining the right time to sell a business is often a matter of making an educated choice. Although there are some instances in which a business owner is forced to sell, the decision to sell can be anticipated and planned for. Once the decision to sell has been made, the next question is when it is the right time to sell. Businesses operate in an environment governed by cycles and thus the decision to "time the market" is not a trivial one, as it can greatly impact the ultimate value realized by a business owner.

Markets go through a series of recurring cycles—a dynamic that often leads to supply/demand imbalances. When these circumstances are extreme, we tend to regard them as "bubbles" and business owners who recognize these conditions will try to sell into the bubble. However, bubbles are quite difficult to identify and they tend to collapse rather abruptly. But, there are some pointers that can be helpful. For the most part, bubbles tend to last three to four years—although this is just a rough generalization. Their emergence is probably preceded by some form of "buzz," and as a result, valuation multiples begin to exceed the norm (usually 60% - 100% above). Also, the highest multiples are likely to be paid when the bubble is about 75% through its ascent.

History tells us that temporary industry imbalances are unlikely to be repeated in the same way for the same causes. Nevertheless business owners, regardless of their age, who operate in an industry which is undergoing bubble conditions, should seriously consider taking advantage of the increasing valuations that result before the inevitable collapse.

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"Rethinking the Value..." continued from p. 1

As the merits of a government bailout were being hotly debated among the news media and the populace, a number of tax provisions in the Housing and Economic Recovery Act of 2008 and the Emergency Economic Stabilization Act of 2008 were enacted with little fanfare or notice. With a flurry of IRS newly issued Treasury Regulations, Revenue Rulings and Notice, relief was sought and granted to certain specific banking and financial institutions that allows for waiving some of the harsh restrictions imposed by Section 382, which limit the ability of acquiring corporations to use net operating losses where there is more than 50% change in ownership.

Experienced tax professionals are well aware of the significant limitations imposed on the ability of acquiring companies to use net operating losses where there is more than a 50% change in ownership. These rules are both cumbersome and complex and can significantly limit the ability of acquiring companies to get the tax benefit of these losses.

Although this legislation, as originally written, was directed and limited to benefit specific federal and financial banking institutions such as Fannie Mae, Freddie Mac, Wells Fargo Bank and Wachovia, it does signal a mood swing in Congress that hopefully will initiate relief to the private sector and the middle market, where a good business strapped with too much debt is unable to turn a profit, but does have value. The waiver of the loss limitation rules would be welcomed and would serve to creatively finance transfers and sales of businesses that can jump start our economy, create jobs and get the US economy moving in the right direction once again. Time will tell if a change in law will be written to benefit a broader audience. We will just have to wait and see.

Editor's Note: As of press time, the Obama tax plan is seriously considering revising the carry back provisions from 2 to 5 years, but a prior proposal concerning legislation was rejected during the initial bailout.

Fast fact: The largest deal made in North America this year - and indeed the world - was Wells Fargo's purchase of Wachovia for $68.1 billion.

Source: ZEPHYR published by BvDEP

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About The McLean Group

The McLean Group is a national, middle market investment bank providing mergers & acquisitions (M&A), capital formation, market intelligence, business valuation, litigation support and exit planning services. The McLean Group serves businesses generating up to $500 million in annual revenues. Headquartered in Northern Virginia's technology, communications and government contracting corridor, the firm is among the largest independent middle market investment banks in the Washington, DC area. The McLean Group is a FINRA Registered Broker/Dealer and Member FINRA/SIPC.

- M&A: The McLean Group uses its considerable expertise in a wide variety of industries to identify the most probable and suitable candidates to complete transactions under the most favorable terms for its clients.
- Capital Formation: The McLean Group arranges private equity, venture capital, senior debt and subordinated debt in amounts ranging from $5 million to $250 million to support clients' expansions, mergers & acquisitions (M&A), refinancings, recapitalizations, leveraged buyouts and shareholder liquidity objectives.
- Market Intelligence: By leveraging superior competitive analyses, the firm provides business executives with comprehensive market intelligence reports, which provides the market insight and analytical expertise required to reduce risk and uncertainty in strategic decision making.
- Business Valuation: As a core competency and complement to its M&A business, The McLean Group provides business valuation services, including intangible asset and financial security valuations for a variety of transactions, financial reporting and tax purposes.
- Litigation Support: From quantifying economic damages to valuing a minority interest in a business, the firm has the business valuation experience and credentials to support cases involving a variety of legal issues.
- Exit Planning Services: Based on its extensive experience advising owners of middle market businesses, The McLean Group has developed a proprietary process that analyzes more than 60 value/risk drivers that can have a significant impact on the value of a business.

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Investment Bankers to the Middle Market