The McLean Group
INVESTMENT BANKING

M&A Market Update©

Your source for information about today's mergers & acquisitions market September 2008

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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:
Baby Boomers & Technology: Be Prepared

By Dennis Roberts, Chairman

The ubiquitous baby boomers are no less a driving force in middle-market mergers and acquisitions (M&A) as in all other aspects of the American marketplace. The eldest baby boomers of the 78 million baby boom generation turned 60 in 2006. The youngest baby boomers will turn 60 in 2024, only about 16 years from now.

Many baby boomer entrepreneurs will liquidate their middle-market businesses – and this will remain a major M&A driving force for at least another 25 years. Consider this: While census data indicates that many of the baby boomer-owned businesses are small businesses with sales under $1 million, just more than 25 percent (or 3.2 million), are middle-market firms with sales of $1 million to $1 billion annually. Collectively these 3.2 million firms had sales totaling $10.5 trillion, carrying a conservative market value of $5.25 trillion.

This will create a huge number of competing transactions during the next 20 years. We estimate that 40,000 middle-market business will compete for buyers annually, which is why early sales preparation is crucial. Such preparation includes understanding what makes a middle-market business attractive amongst its competition. Most businesses, even sizable ones, are sold with less than one year of preparation, particularly as sales are often motivated by lifestyle issues (i.e. age, retirement, health, stress, etc). Although economics is a major factor, it is not the typical decision driver; this is and will be especially true for the aging baby boomer population.

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Expert Tips:
How to Get Deals Done

By Brian Sullivan, CPA/ABV

Understanding the mergers and acquisitions (M&A) process has never been more important. Our financial markets have been seriously compromised and need restructuring.

Some believe the credit crisis may prematurely signal a stoppage in deal flow, but deals will continue to close if businesses sale processes remain well-grounded in fundamentals that intelligently work through the M&A process. In addition, many middle-market businesses' demographic profiles combined with the need to implement effective wealth transfer strategies (especially as baby boomers age and sell their businesses) will facilitate continued deal flow. Baby boomers alone will dispose of an unprecedented 42 million middle-market businesses a year for about the next 20 years.

Carefully planning deal executions is more important than ever. The following fundamental M&A elements will help guide you through your deals:

1. Understanding the Deal from Both the Buyer & Seller Perspective

Buyers and sellers come from different perspectives and require both parties to understand their similarities and differences. Sellers typically look to the market to establish a "floor price" based on comparable or similar transactions. On the other hand, buyers price the deal based on what the business is worth to them, so they look to making a minimum rate of return on cash flow (income before taxes) that meets their overall investment criteria. Typically the buyer does this with discounted cash flow models. The buyer's required Return On Investment (ROI) drives the buyer's interest to pursue a target. Businesses with good and especially stable cash flows (income) will be of the greatest interest to strategic buyers who pay the highest prices.

2. Creating the Auction Environment

After a thorough vetting of interested candidates, intermediaries are hired to sell the target company on a bid basis. The value of the auction process is to create an environment that will more than likely result in the highest and best possible deal price. It also serves to limit the search to only serious buyers.

3. Negotiating the Transaction/Deal Structure

Negotiating terms and price is as much an art as a science. Personalities, cultures and overall objectives of buyers and sellers need to be carefully identified and discussed to ensure the transaction will meet the objectives of both parties. Negotiating the role of the seller and intermediary also should be clearly defined and shared. Many serious buyers dislike (and understandably so) negotiating substantive points through intermediaries because they know it is likely to lead to a higher, but fairer price for the seller. There is a difference between deal value and price. Buyers and sellers who work with professionals that understand that difference are well served and more likely to successfully consummate a transaction. It is the bottom line cash to the seller that matters and not the announced price. In fact, most announced prices are very misleading. ◆

Trends To Act On:
Finding Value in Divested Assets

By Michael A. Keith

Recent research by The Boston Consulting Group (BCG)[1] indicates that mergers & acquisitions (M&A) involving divested assets frequently create more value than buying businesses as a whole. BCG concludes that 41.7 percent of firms acquiring entire companies produced positive returns, while 57.5 percent of firms acquiring divested assets did so. This is especially true during economic downturns as companies seek to divest unprofitable business units.

Asset sales often are attractive to buyers due to challenges facing sellers in negotiations: many sellers face difficulties valuing underperforming stand-alone assets or setting a pricing "floor." BCG's report observes that sellers often "screw up" asset sales because, "they don't want to spend a lot of corporate time managing the process."

When sellers fail to focus on asset sales, buyers that do their homework may well find values the sellers overlooked. Either way, for sellers and buyers alike, the counsel and support of a professional middle market investment banker often can make the difference between a successful transaction and one that fails to meet expectations. ◆

Exit Planning:
Assessing Your Company's Competitive Position

By Enrique Brito, CFA, AVA, CM&AA

Competitive analysis evaluates a company's strategic position and its ability to compete in its market against its peers. The objective is to assess characteristics of the business, economy and industry as a whole that affect the firm's future and determine whether or not its performance will be consistent with past results.

There are several techniques for identifying a company's competitive advantage such as customer segmentation analysis, competitive business systems analysis and industry structure analysis. But perhaps one of the most influential analytical models for assessing the nature of competition in an industry is Michael Porter's Five Forces of Competitive Position model, which he describes in his seminal book Competitive Strategy (1980). Porter explains there are five forces that determine industry attractiveness and long-term industry profitability:

1. The treat of entry of new competitors
2. The threat of substitutes
3. The bargaining power of buyers
4. The bargaining power of suppliers
5. The degree of rivalry among existing competitors

Conducting a competitive analysis helps you evaluate how industry factors will affect your business' ability to compete. It will assist you in identifying strategies to capitalize on your business' strategic advantages while minimizing or neutralizing the consequences of its disadvantages. But this requires a clear understanding of the overall profitability constraints in the industry in which you operate, the characteristics most likely to change that level of profitability and the strategies and resources required to compete successfully in that environment. ◆

The Exit Strategies Institute

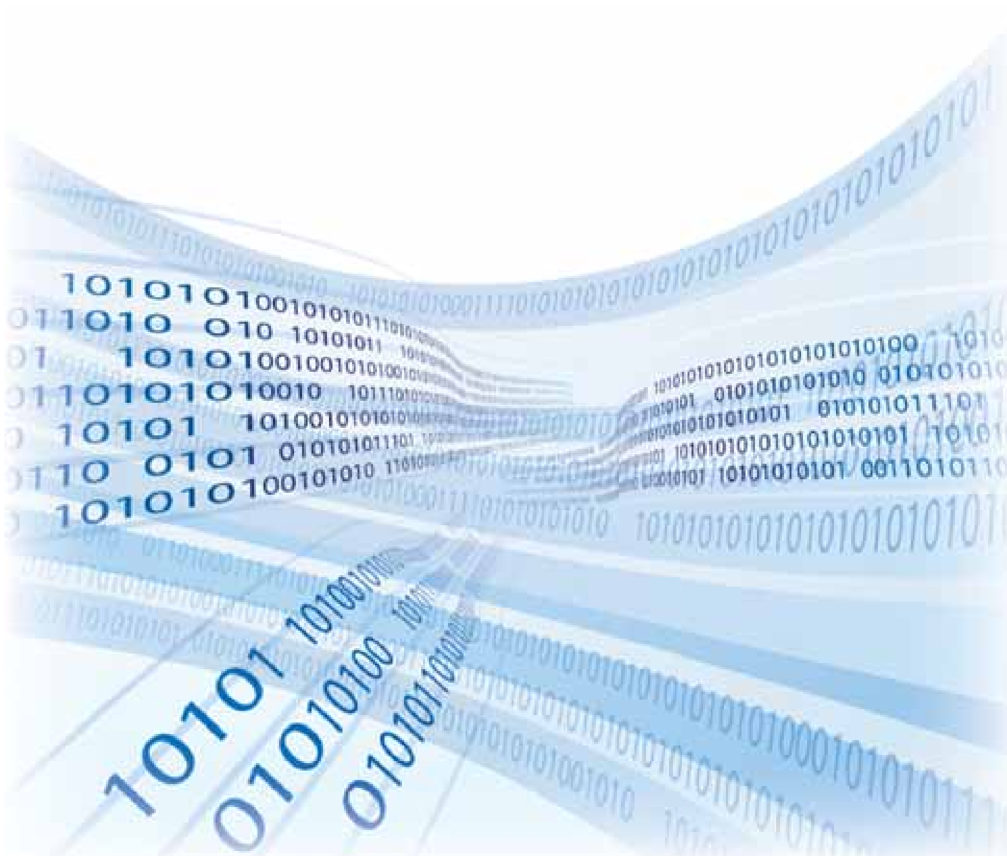
The McLean Group's Exit Strategies Institute works with business owners to develop a multi-year program that provides a road map to maximize the business' value at the time of exit. In this comprehensive process each business is evaluated at three levels: business strategy, value proposition and current execution. Each of these levels is carefully evaluated to develop an action plan outlining specific steps to capitalize on the business' strengths to enhance its value and marketability. For more information, please visit www.PlanYourExit.org.

[1] The Boston Consulting Group. (May 21 2008). "Economic Slowdowns Are Ideal Times for Mergers and Acquisitions, BCG Finds." Press Release. Retrieved 2008-09-08.

"Is This a Good Time to Make Acquisitions?"...continued from p. 1

Technological advances also have dramatically transformed today's middle market from that of just 15 years ago. New technologies launched by middle-market firms routinely disrupt other middle- and upper-market firms, and sometimes entire industries. Light speed advancement in such technologies forces survivors to become increasingly proactive and responsive with clients and prospects. Many middle-market firms will adapt throughout the global economy and dramatically shorten business life cycles, while those firms that grow complacent with past achievements will soon awaken to find themselves in the "buggy whip business."

Creative destruction always has been a force to be reckoned with in capitalist systems. It existed in the US in 1908 and 1808. But in 2008, the ever-increasing speed of technological advances has accelerated the process to an astonishing degree. As a result, it has dramatically shortened business life cycles (or at least "business as normal") among businesses that rely on technology more than those that develop technology. Ten years ago, the Internet was in its infancy for the vast majority of the world. Since then, the Internet has radically transformed our world, our economy, and virtually every business in the US and elsewhere. A good illustration of this is that the average existence of a company in the S&P 500 index as measured by annual turnover 50 years ago was 25 to 35 years, versus today which is 12 to 14 years.



The middle-market business life cycle – the time elapsed from founding to exiting or growing through acquisitions of other middle-market business – has gone from 25 years or more to two to three years in some technology or technology-dependent businesses, with most of that acceleration realized in the last ten years. The radical shortening of business life cycles in turn has had an enormous impact on middle-market business operations and the timing and execution of middle-market sales.

The key? Be prepared.

The sale of a middle-market business is a complex transaction involving adequate advanced preparation and planning, contract law, accounting, complex taxation, business valuation, negotiation and deal structure, finance and many other issues that can either help or hinder owners from achieving maximum value. ◆

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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 Washington, DC's technology, communications and government contracting corridor, the firm is among the largest independent middle market investment banks in the region. 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' expansion, mergers & acquisitions (M&A), refinancing, recapitalization, leveraged buyout and shareholder liquidity objectives.
- **Market Intelligence:** By leveraging superior competitive analyses, we provide business executives with comprehensive market intelligence reports, which give 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.

The McLean Group
Investment Bankers to the Middle Market