The DAK Group
Investment Bankers Optimizing the Value of Mid-Market Companies

2018 Middle-Market M&A Transaction Trends

OVERVIEW

Middle Market M&A activity was strong in 2017 driven in part, by an optimistic financial outlook following the 2016 election. This optimism positively fueled Strategic and Private Equity buyers into recognizing value and growth opportunity in middle market companies and was the catalyst for them to invest. Transactions for middle-market companies ($5 million to $500 million, including unannounced values) was up approximately 6% over 2016 with 7,465 completed deals compared to 7,051 middle market deals completed in 2016.

Middle market transactions extended across a range of industries as many owners/founders reached retirement age and looked to exit in a robust market. The aging "Baby Boomer" population has been a strong driver of M&A activity in the middle market, a trend that appears will continue well into the next decade.

Also driving activity throughout the year was the continuation of low interest rates, enabling private equity groups to use cheap financing to facilitate higher multiples. Likewise, strategic buyers with vast cash reserves continue to be strong players as they look to grow revenue, profitability and capabilities through acquisition.

From a geographic perspective, the Eastern region of the U.S. continues to be the most active part of the country with more than 3,000 transactions completed. This represents 42% of the nation's middle market deals. The Midwest was the second most active region with more than 2,300 transactions and a dramatic increase of 72%! The West ranked third, and enjoyed an increase of 12.5%, with just under 2,000 transactions.

The improving economy in the Midwest, especially in block-and-tackle sectors like manufacturing and distribution, drove M&A as sellers were able to achieve desirable multiples.

Overall, the most active sector throughout the year was Industrials (1920+ transactions) followed by Financials and Technology with more than 1,400+ transactions each. The Financials sector saw the largest increase in number of transactions, 45.5% over 2016. This was driven, in part, by consolidation of small regional banks as larger regional banks looked to gain market share.

The Technology sector continues to drive the highest multiples (8.6 x+) driven by software-as-a-service (SAAS) which is attractive due to the recurring revenue.

Positive Outlook for 2018

The uptick in number of transactions in 2017 should continue steadily throughout 2018. Private equity firms

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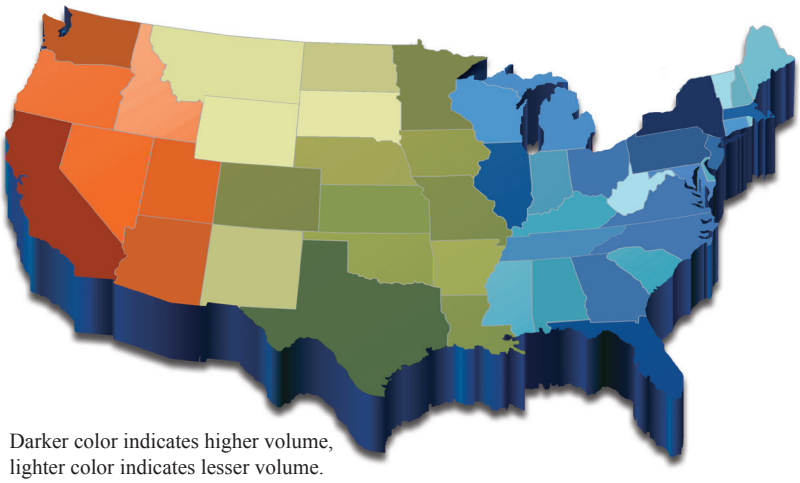
2017 Transactions for Businesses with Annual Revenues: $5MM - $500MM

WEST | MIDWEST | EAST



Darker color indicates higher volume, lighter color indicates lesser volume.

U.S. Snapshot

Representative Ranges

2017
Average Transaction Values†:
$47 million—$113 million

2017
EBITDA Multiples†:
5.9x—8.56x

2017
Average Company Revenue†:
$11.2 million—$126 million

WEST	MIDWEST	EAST
2017	2017	2017
Most Active Industry: Technology	Most Active Industry: Industrials	Most Active Industry: Industrials
Most Consistent Industry: Technology	Most Consistent Industry: Technology	Most Consistent Industry: Healthcare
Deal Volume: 1,982	Deal Volume: 2,336	Deal Volume: 3,147
Avg. Transaction Value ($M): 69.87	Avg. Transaction Value ($M): 83.21	Avg. Transaction Value ($M): 81.70

†Excludes outlier transactions during this period. All report data are based on Factset transaction information.

are aggressively looking to deploy the large amounts of capital they have been raising. Family Offices are expanding their reach into different areas, and strategic buyers are seeing acquisitions as the best way to grow and expand their companys' footprints.

The passage of the new tax bill looks to free up significant cash for corporations adding to already flush balance sheets. This will be used to spur M&A activity as they look for accretive destinations for their money.

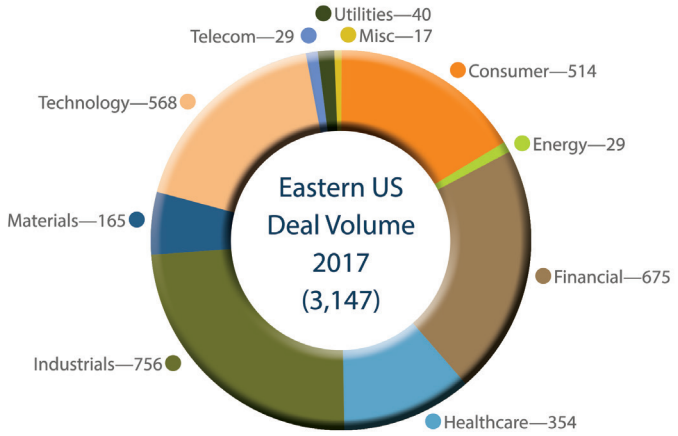
We see many fragmented industries continuing to experience disruption and consolidation. As technology enables businesses to operate more efficiently, gaining new capabilities and intellectual property through M&A becomes a simpler solution than building from scratch. We also see a lot of interest in companies that have a solid digital strategy as being highly desired targets for other middle-market companies looking to acquire a "turnkey" digital solution versus developing one internally.

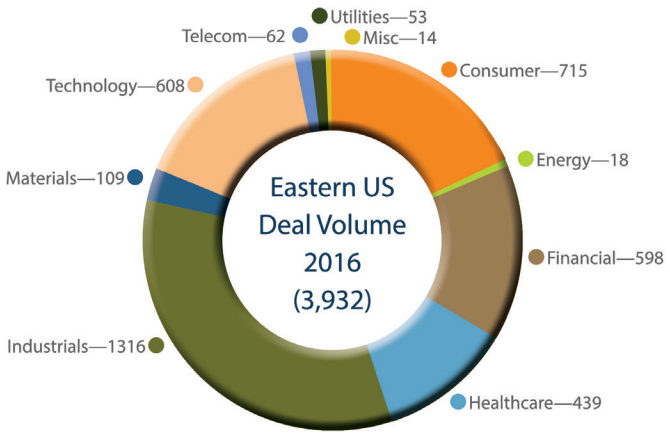
Eastern Activity

The Eastern Region continues to lead the way for middle market deals representing 42% (3,147) of the total deal volume in the United States. However, total transactions in the East declined by 20% in 2017, compared to 3,932 transactions in 2016.

The Industrial sector once again leads the East in number of transactions for the fourth year in a row, accounting for 24% of the deals. Industrials were consistently strong across the country representing 26% of all transactions nationwide. Mirroring the national trends, the next two most active sectors were Financial and Technology, accounting for approximately 21% and 18% of deal volume respectively, in the Eastern Region. Part of what has been driving M&A in the Industrials sector is technology. Manufacturing is evolving and technologies such as additive manufacturing, autonomous robots, and the Internet of Things are changing the sector significantly.

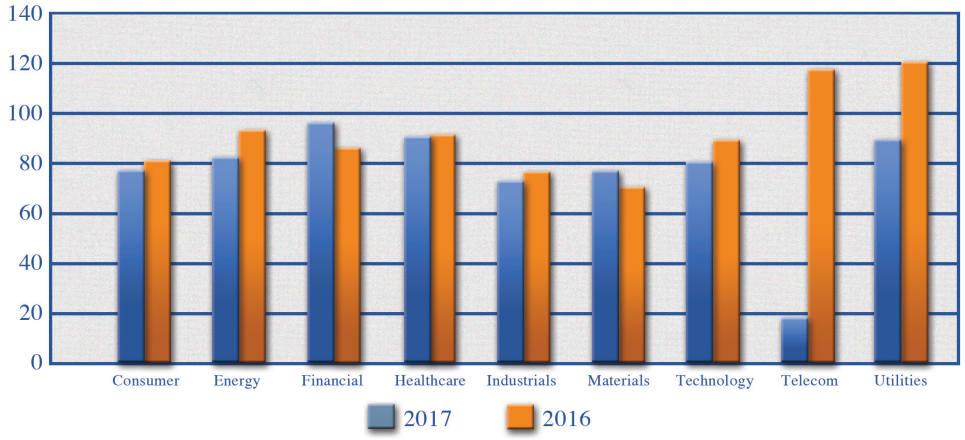
Eastern US Industry Deal Volume*





Transactions that occur in the broad industry classifications like manufacturing, distribution and logistics are included in specific sub-sectors. For example, a transaction involving the manufacturing of food products would be reported under the Consumer sub-sector.

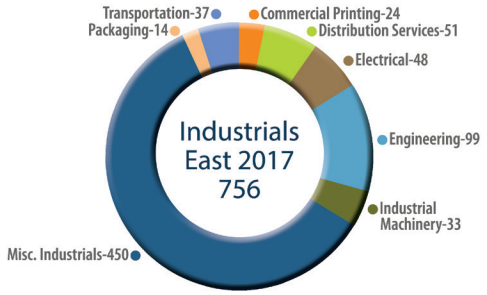
Eastern US Industry Average Transaction Value ($MM)*

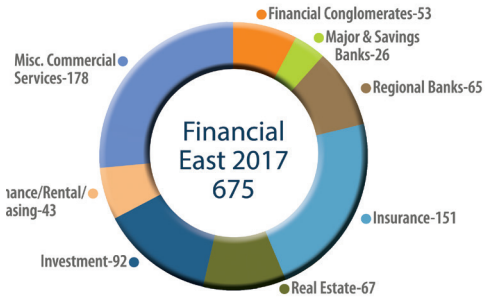


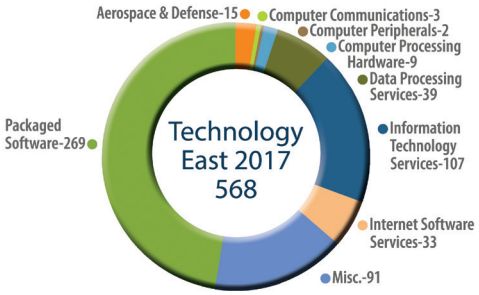
* All report data is based on Factset transaction information. Outliers omitted.

Eastern Region
US Leading Sectors Deal Volume

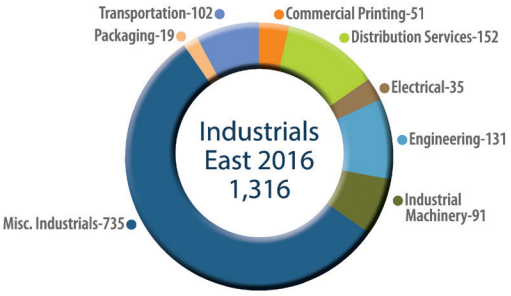
2017

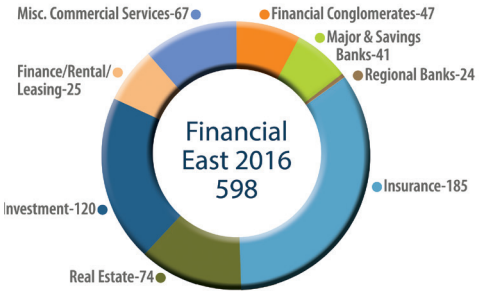


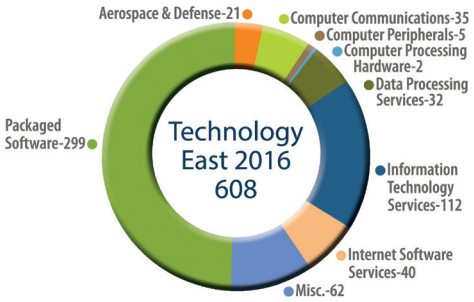




2016







The sub-sectors that led a large amount of Industrial deals were Industrial Engineering, Distribution Services and Electrical, all combined accounting for roughly 26% of all the transactions in the sector. Electric Engineering alone had a 37% increase in transactions over 2016 driven, in part, by transactions focused around additive manufacturing design and implementation.

The Financial Sector ranked second in 2017, up from its third position in 2016. The Insurance sub-sector led the way, accounting for about 22% of the deals. The US insurance market continues to attract the interest of foreign investors, especially Chinese and Japanese companies looking for places to invest their capital. Large insurers have also been divesting non-core assets to mitigate regulatory concerns.

The number of regional banks involved in a transaction more than doubled over 2016 transactions, as local banks are merging and acquiring each other.

Technology dropped to the number three ranking of deals, from number two in 2016. Leading the Technology sub-sectors were Packaged Software (47%) and IT Services (19%), the same pattern and rankings as 2016. Multiples in the Software sector have been driven by software-as-a-service providers (SAAS) that have strong recurring revenue.

The largest factor behind Technology M&A is the rise in acquisitions of Technology companies by non-tech acquirers. These buyers seek to expand capabilities and strengthen footholds in their respective markets by gaining technological advantages through acquisition.

What Trends Mean to Business Owners

M&A activity was strong in 2017 in both volume and values. The outlook for 2018 is positive and is expected to bring more activity than last year based on lower corporate taxes, a strong economy and "baby boomer" business owners looking to exit.

While M&A volume and valuation trends are cyclical, there is no way of predicting how long a positive window will last. We are seeing an increase in the pipeline of businesses being offered for sale. Most of this jump is being fueled by business owners concerned that the market may be peaking, and their desire not to "miss the boat."

We recommend that owners think carefully about the timing of their exit, and how current market forces might impact the value of their company, and their overall plans. In most cases, it would be unwise for business owners to not at least track the M&A climate in 2018, and keep apprised of what other business owners in their sectors are doing. It would also be wise to consult with professionals, even on a casual basis, to be informed on what is needed to make an exit, as in some cases it can take 2-3 years to get a business ready in order to achieve the maximum value.

About The DAK Group

Maximizing the Value of a Lifetime's Work

The DAK Group is the leading investment bank in the northeast for middle-market, privately held businesses. Our exclusive focus is on helping entrepreneurs, family business owners and other mid-market stakeholders navigate financial options for growth and expansion, as well as to pursue successful exit strategies.

We support client M&A needs in the areas of:
- Full or Partial Sale of the Business
- Mergers/Acquisitions
- Recapitalizations/Financial Restructuring
- Valuations and Fairness Opinions

The DAK Group was founded in 1984, and has successfully completed over 650 transactions worldwide across the full range of major industries. The DAK team includes senior level investment bankers who understand the intricacies of working with business owners making, what could be, the largest financial decision of their lives. Our proprietary process ensures that each transaction meets the goal of *maximizing the value of a lifetime's work*.

*For more information on other critical factors that will impact valuation, please contact Joan McGeough at jmcgeough@dakgroup.com.

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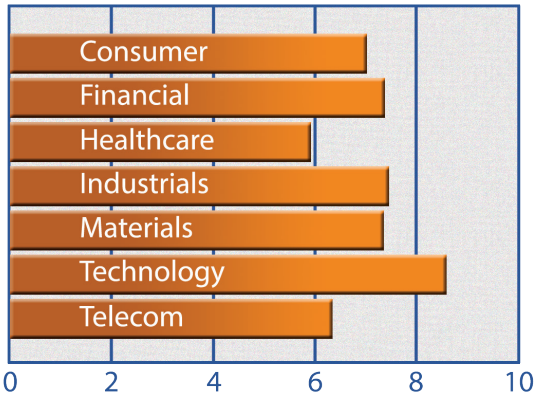
EBITDA Multiples 2017

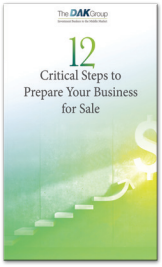


An important measure of a company's cash flow is EBITDA (Earnings Before Interest, Taxes, Depreciation and Amortization). The EBITDA multiple serves as a barometer of how an individual company or industry is doing compared to others. It is frequently one of the cursory factors used to determine enterprise value as part of a transaction. Multiples of EBITDA vary greatly depending on the specific market, size of the company, key technology, and other factors.

The average EBITDA multiple across all sectors was 6.7 The sector that generated the highest average value was Technology (8.6x) driven by software-as-a-service. Industrials had the second highest average EBITDA multiple at 7.4x.

While EBITDA is one of the factors in determining the value of a business for sale or acquisition, it should not be the only factor taken into consideration. Business owners should not make the mistake of using EBITDA multiples alone to guide the valuation of the business. Instead, they, along with their advisors, should understand what the value of the business is to the buyer, and what the combined synergistic value could be. This understanding often creates increased value.

Request *12 Critical Steps to Prepare Your Business for Sale.*



Whether you're planning to sell in the near term, or well down the road, it pays to be prepared. Request your copy of *12 Critical Steps to Prepare Your Business for Sale* and learn what you can do now to ensure that you get the maximum value for your business when the time comes to sell.

Request your copy of *12 Critical Steps* today.
Your request will be kept strictly confidential.

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