M&A AND DEBT CAPITAL MARKETS UPDATE

FEI Central PA Chapter January 2022 Dinner Meeting
January 18, 2022
# Market Review

The global COVID-19 pandemic has overshadowed public and private markets over the past two years

<table>
<thead>
<tr>
<th>2020 MARKET REVIEW</th>
<th>2021 MARKET REVIEW</th>
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<td>• COVID-19 officially arrives in the U.S. (Jan. 2020)</td>
<td>• COVID-19 vaccines rollout to the public (Q1 2021)</td>
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<td>• Public equity markets plunge by 30%+ (Mar. 2020)</td>
<td>• M&amp;A carries 2020 backlog into 2021 (Q1 2021)</td>
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<td>• 1st federal stimulus bill becomes law (Mar. 2020)</td>
<td>• 3rd federal stimulus bill becomes law (Q1 2021)</td>
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<td>• M&amp;A activity bottoms out (May 2020)</td>
<td>• Inflation and COGS spike (Q3 2021)</td>
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<td>• Cost of debt drops to historical lows (Aug. 2020)</td>
<td>• Global travel re-opens (Q4 2021)</td>
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<td>• Public equity markets recover to pre-pandemic highs (Aug. 2020)</td>
<td>• Public equity markets achieve record highs (Q4 2021)</td>
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<td>• M&amp;A activity sharply rebounds (Dec. 2020)</td>
<td>• COVID-19 variants emerge dampening a return to normal (Q4 2021)</td>
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<td>• 2nd federal stimulus bill becomes law (Dec. 2020)</td>
<td>• M&amp;A Market perseveres despite uncertainty in macro economy</td>
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So where are we now ...

Source: Pitchbook
Current Challenge – Labor Shortage

U.S. firms must now aggressively compete to hire and maintain a skilled workforce.

U.S. LABOR PARTICIPATION & UNEMPLOYMENT RATE

COMMENTARY - 2020

- Non-essential workers furloughed
- Work from home becomes the “norm”
- 1.5 million retirements above expectation
- Congress enhances unemployment benefits
- Number of immigration visas granted falls

COMMENTARY - 2021

- Fear of the pandemic persists
- Child-care issues constrain families
- 0.8 million become self-employed
- 4.3 million fewer workers (Feb-20 vs. Oct-21)
- Remaining labor force is mostly employed
- Unemployment is 3.9% at end of year

Current Challenge – Inflation
The cost of goods and inputs have spiked for consumers and producers

U.S. CONSUMER PRICE INDEX

COMMENTARY
• Relatively stable from 2012-2019
• Noticeable decline in 2020
• Significant spike in 2021
• Peaks at 7.1% on Oct. 1st, 2021
• Decreasing at end of year

U.S. PRODUCER PRICE INDEX (YOY)

COMMENTARY
• Sustained periods of both positive and negative rates from 2012-2019
• Sharp decline then recovery in 2020
• Significant spike in 2021
• 22% (YoY) on Oct. 1st, 2021
• Increasing at end of year

Source: FRED
ONE PER CUSTOMER PLEASE
Current Challenge – Supply Chain

U.S. ports are clogged as economic demand recovers faster than supply chains can accommodate

**PORT OF LOS ANGELES - AVERAGE DAYS AT ANCHOR & BERTH**

**COMMENTARY - 2020**

- Steady and efficient in previous years
- Less than 5 days on average in previous years
- Stable during initial shutdown
- Noticeable increase around holiday season

**COMMENTARY - 2021**

- Initial jump in early 2021
- Declines during vaccine rollout
- Spikes again in Q3
- Still present at end of year
- Expectation this challenge extends into 2022

How has this impacted M&A ...
Overall Market Strong in 2021
Late 2020 market momentum carried into 2021

U.S. MONEY SUPPLY

- Strong Fed response to pandemic in 2020
- Money supply at record highs
- Interest rates at historic lows

U.S. PUBLIC EQUITY MARKETS

- Public equity markets at record highs at end of 2021
- Quick recovery from 2020 pandemic lows
- Valuations at record highs

Sources: CapIQ; FRED
Record Levels of Capital to Deploy

Strategic firms and Private Equity groups have never possessed larger cash reserves

**S&P500 CASH BALANCE**

![Graph showing S&P500 Cash Balance from 2013 to 2021.]

**COMMENTARY**

- S&P Cash balances exceeding $3.8T
- Sizeable increase during pandemic years of 2020 and 2021
- Nearly tripled since 2016

**PRIVATE EQUITY OVERHANG**

![Graph showing Private Equity Overhang from 2011 to 2021.]

**COMMENTARY**

- Private equity ‘dry powder’ exceeding $1.4T
- Pressure to deploy capital in vintage funds
- $1.4T represents nearly $5.0T of purchasing power on a leveraged basis

Sources: CapIQ; Pitchbook
Monthly M&A Activity 2017-2021
2020 trends differently than other years

**U.S. TOTAL M&A ACTIVITY**

- **# of Deals**:
  - January 2017: 1,024
  - March 2018: 1,093
  - May 2019: 1,047
  - July 2020: 997
  - September 2021: 1,165

**AVERAGE MONTHLY DEAL COUNT**

- January 2017: 1,024
- March 2018: 1,093
- May 2019: 1,047
- July 2020: 997
- September 2021: 1,165

**U.S. MIDDLE MARKET\(^1\) M&A ACTIVITY**

- **# of Deals**:
  - January 2017: 76
  - March 2018: 81
  - May 2019: 73
  - July 2020: 64
  - September 2021: 82

**AVERAGE MONTHLY DEAL COUNT**

- January 2017: 76
- March 2018: 81
- May 2019: 73
- July 2020: 64
- September 2021: 82

**COMMENTARY**

- Snap back from below average 2020 deal count
- Pull forward of 2021 activity due to potential tax changes
- Incredibly aggressive buyer activity from both strategic and financial players

1) Middle market defined as deal size between $50 - $500 million

Source: Pitchbook

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PRIVATE & CONFIDENTIAL
Overall Market Strong in 2021
Late 2020 market momentum carried into 2021

COMMENTARY

- Noticeable 2020 trough in deal volume
- Depressed deal value in middle 2020
- Significant rebound in deal volume in Dec. 2020
- Deal volume stabilizes in 2021
- Deal value increasing throughout 2021

Source: Pitchbook

COMMENTARY

- Overall U.S. M&A rebounding from 2020 dip
- YTD 2021 Deal Count above YTD 2020
- YTD 2021 Deal Value above YTD 2020
Middle Market Strong in 2021
U.S. middle market continues to recover

**COMMENTARY**

- Same trends as U.S. Total M&A
- Deviations from these trends include
  - Larger deal count growth from ’20 to ’21
  - Deal value relatively stable throughout

Source: Pitchbook
1) Middle market defined as deal size between $50 - $500 million
M&A Multiples Strong in 2021
U.S. market continues to recover from 2020

**U.S. TOTAL M&A MULTIPLES**

- Overall M&A multiples rebounding from 2020 dip

**U.S. MIDDLE MARKET M&A MULTIPLES**

- Middle market M&A multiples also rebounding from 2020 dip

Source: Pitchbook
1) Middle market defined as deal size between $50 - $500 million
Key Takeaways
Summary of 2021 markets

• Global and U.S. markets were strong in 2021 with momentum carrying into 2022

• Strategic firms and Private Equity groups have record-levels of cash to deploy

• Increasing labor and input costs are challenging business operations and profitability

• Global supply chains have not recovered to pre-pandemic efficiency

• Managing risk becoming more important in the “new normal” environment

• Increasing focus around technology and automation with respect to M&A process

• Decreasing risk of capital gains tax changes

• Capacity constraints for M&A service providers

• Buyers’ willingness to “underwrite” pro-forma adjustments is driving valuation multiples
Looking Ahead to 2022
Strong 2021 momentum carrying into 2022

2022 OUTLOOK

• Increasing M&A competition from strategic and private equity war chests

• Strong key performance indicators and outcomes will command premium valuations

• Operational and economic risk management will play a greater strategic role

• Rising regulatory scrutiny over antitrust and merger control issues

• ESG diligence becoming more important
# M&A Sector Coverage

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2021 – A Banner Year Across the Debt Capital Markets

**Pro Rata “Bank” Market**

*Shift in focus from significant amendment activity in 2020 to generate loan growth in 2021*

Overall loan volume up nearly 60% compared to 2020, driven by strong M&A activity (M&A volume up 98% year over year) and high refinancing volume (up 219%).

**Institutional Market**

*Record year driven by M&A financing and sponsor activity*

$615 billion in new loan volume set a new watermark, shattering the prior high of $503 billion in 2017 due to record years in M&A and sponsor-related financings.

**High Yield Market**

*Another banner year with issuers proactively getting ahead of expected rate hikes*

$464 billion in 2021, breaking the prior year record ($445 billion) for highest annual issuance in history, with a healthy mix of refinancing and M&A activity.

*The US Leveraged Finance Market had its busiest year ever, characterized by record-breaking volume in both the loan and bond markets with many factors playing into the unprecedent year*

Sources: Bloomberg; Citizens Capital Market; Credit Flow Research; LCD
The Global Hunt for Yield Continued to Provide Strong Liquidity

A confluence of factors continue to drive markets forward:

1. Low-Rate Environment

10YR TREASURY YIELDS REMAINED RELATIVELY LOW AND...

... MORE ATTRACTIVE TO INVESTORS THAN OTHER BENCHMARKS

Sources: Bloomberg; Citizens Capital Markets; LCD
Companies Credit Profiles Have Recovered to Very Healthy Levels Post-Pandemic as Growth has Accelerated

Debt Default Rates at Lowest Levels Since 2014

LOAN DEFAULT RATES RETURN TO HISTORIC LOWS...

... RESULTING IN A WAVE OF CREDIT UPGRADES IN 2021

Sources: Citizens Capital Markets; LCD
New Money Trades Buoy New Issue Volume to All-Time Records

M&A Activity Fueled 2021 Loan Volume While HY Issuers Largely Opted to Refinance Existing Debt

INSTITUTIONAL LOAN VOLUME DOMINATED BY M&A...

...WITH HY ISSUERS CONTINUING TO LOCK-IN ATTRACTIVE RATES

Sources: Citizens Capital Markets; LCD; LevFin Insights
Note: $ in billions
Interest Rates in Loans and Bonds Remain Attractive for Issuers, Borrowers, and Investors Alike

Today’s Highly-Liquid Investor Base Looks to the US HY & Institutional Loan Markets to Generate Returns

ALL-IN-YIELDS FOR NEW LOANS HAVE SIMMERED SINCE 2020...

... WHILE THE BOND MARKET REMAINS RANGE BOUND

Sources: Citizens Capital Markets; LCD; LevFin Insights
Equity Performance Continues to Trend Upward

Rising Equity Valuations

Strong momentum across the primary equity indices... with the market capitalization of the S&P skyrocketing.

Sources: Bloomberg; CapIQ; Citizens Capital Markets
Note: Market capitalization $ in trillions
M&A Leverage Multiples Continue to Rise Amidst High Valuations

Leverage Multiples Continue to Move Up

AVERAGE M&A LEVERAGE LEVELS CONTINUE TO INCREASE...

... WITH THE SHARE OF HIGHLY LEVERED FINANCINGS RISING

Sources: Citizens Capital Markets; LCD; Refinitiv LPC
Key M&A and Leverage Drivers and Usual Financing Routes

M&A and Leverage Drivers

- Growth
- Valuation Multiples
- Excess Capital
- Fund Formation
- Low Rates
- Low Defaults

Usual Debt Financing Preferences

- Pro Rata
- Institutional
- High Yield

- Lower Leverage, Lower Cost
- Higher Leverage, Higher Cost

Source: Citizens Capital Markets
Debt Market Expectations are Equally as Robust for 2022

**Macro Factors to Watch**

- **Economics**
  - Hawkish Fed, Treasuries and Impact of a Rising Curve
  - Growth Concerns and Supply Chain Disruption
  - Effects of COVID-19 Variants

- **Government**
  - Biden Policy Agenda
  - Rising Geopolitical Tensions

**Micro Factors to Watch**

- **Heightened Market Volatility**
  - Quickly Shifting Issuance Windows
  - Execution Favorability for Investors

- **Primary and Secondary Market**
  - Spread Activity
  - Frontloaded 1H-22 Primary Issuance
  - Loan vs. Bond Relative Value Opportunities

**GOALS FOR BORROWERS AND ISSUERS IN THE COMING YEAR**

- ✓ Push Button and Be Ready to Launch
  - Companies should be prepared to hit the right market windows
- ✓ Launch Coming Off a Good Earnings Print, Ideally in 1H-22
  - Expectations are primarily built off of a strong expected start to the year
- ✓ Make Hay While The Sun Shines
  - The current market backdrop and strong technicals will not last forever
- ✓ Be Opportunistic For The Long Term
  - Not all trades will be short-term NPV positive, but may be long-term winners

Source: Citizens Capital Markets
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