

Capital Advisory Group State of the Market Webcast

September 21, 2021



Today's Speakers



Sean Bennis

Mergers & Acquisitions
Managing Director
Chicago

- 20+ years of M&A investment banking experience focused primarily in the energy, power and industrial technology markets
- Spent entire career at Lincoln, joining as the firm's sixth employee
- BS from University of Illinois



Bob Horak

Co-Head Capital Advisory Group
Managing Director
Chicago

- 30+ years of capital raising experience with long-standing industry relationships and capital market expertise
- Previously with GE Capital and Heller Financial
- MBA from Northwestern University



Alex Stevenson

Co-Head Capital Advisory Group
Managing Director
Los Angeles

- 25+ years of experience in raising debt, equity, structured capital, and advising on complex situations
- Previously with FocalPoint Securities
- BS from Michigan State University



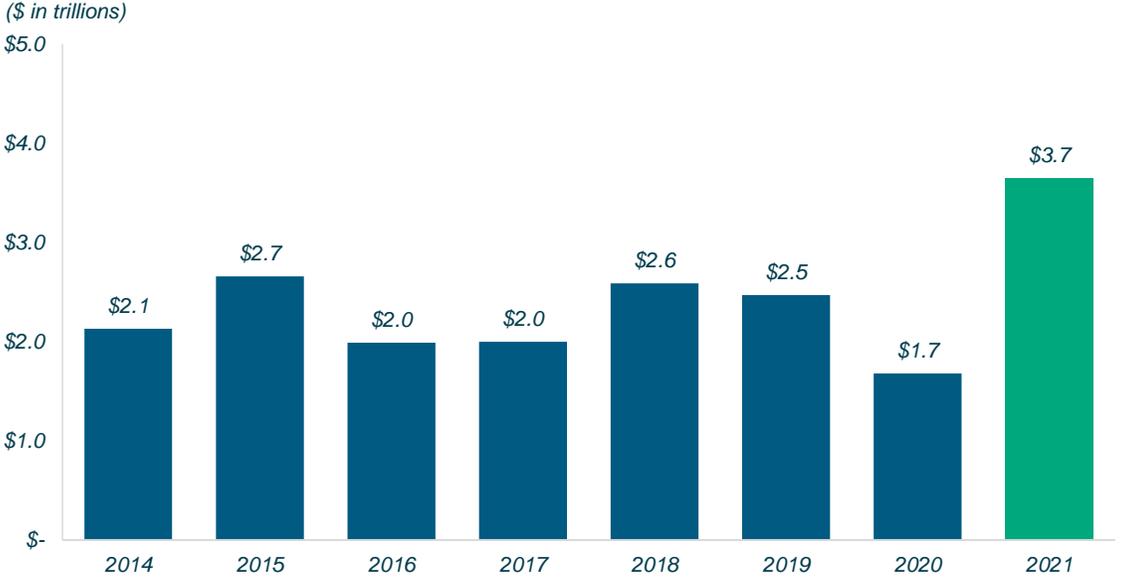
Justin May

Capital Advisory Group
Director
Chicago

- 15+ years of experience in capital raising; focused on Lincoln's capital raise transactions in the technology, media and telecom sector
- Previously with Madison Capital
- MBA from University of Notre Dame

Deal Activity is Running at Record Levels...

Global Deal Volume (January – August, all years)



Source: Dealogic.

New Issue U.S. Leveraged Loan Volume



Source: Refinitiv LPC.

Lincoln's activity mirrors this trend, with awarded sell-side mandates up 67% YTD vs prior year

...with Valuation Multiples at Post-Pandemic Highs

Purchase Price Multiples Have Stepped Up...

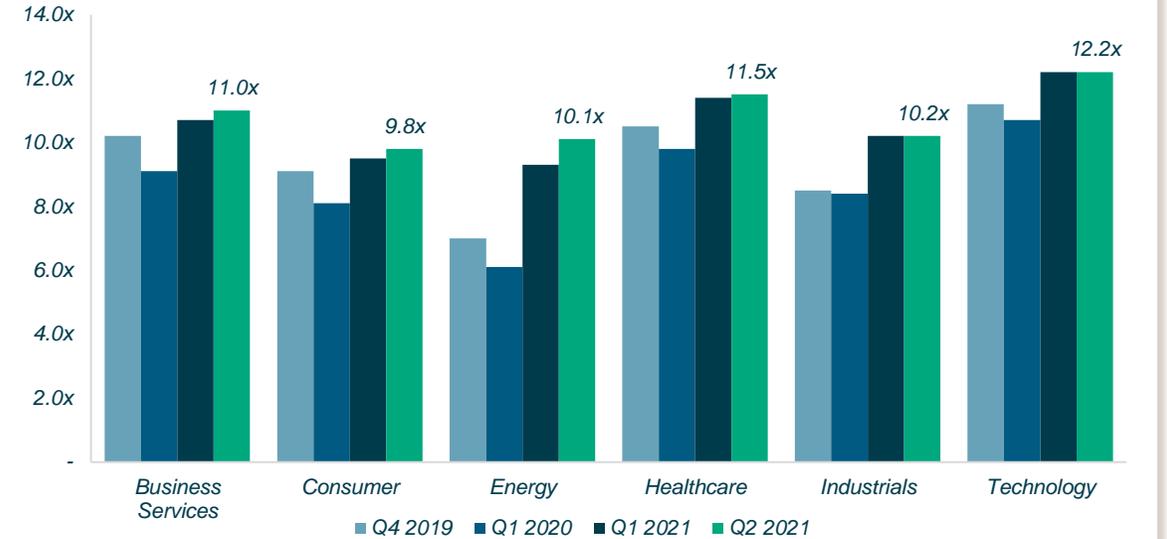
(Multiples of LTM EBITDA for Observed 3rd Party M&A Buyouts)



Source: Lincoln International Proprietary Middle Market Database.

...Across All Representative Industries

(Valuation Levels Based on Multiples of LTM EBITDA)

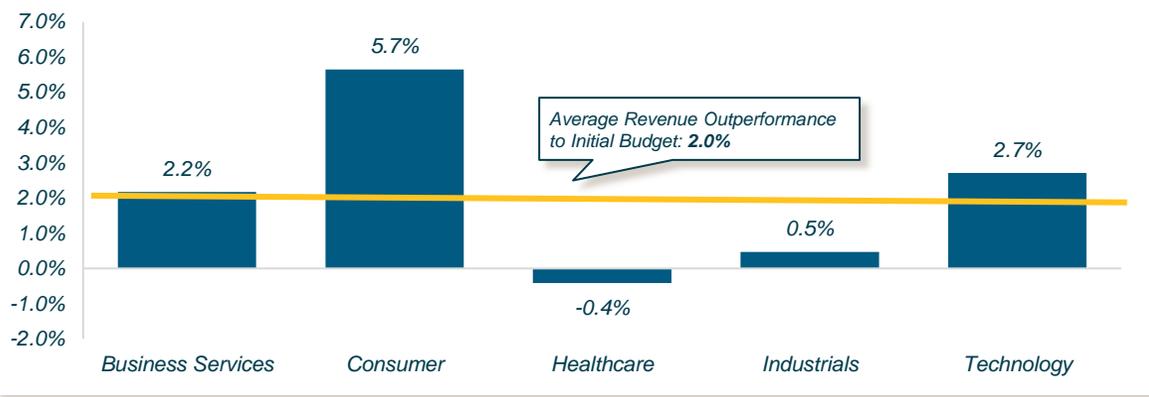


Source: Lincoln International Proprietary Middle Market Database.

Even with an aggressive financing market, high valuations are pushing sponsors to either invest more of their own capital into deals, or find creative alternatives using preferred / structured equity

Fundamentally, Buyer Optimism is Being Driven by Strong Financial Performance...

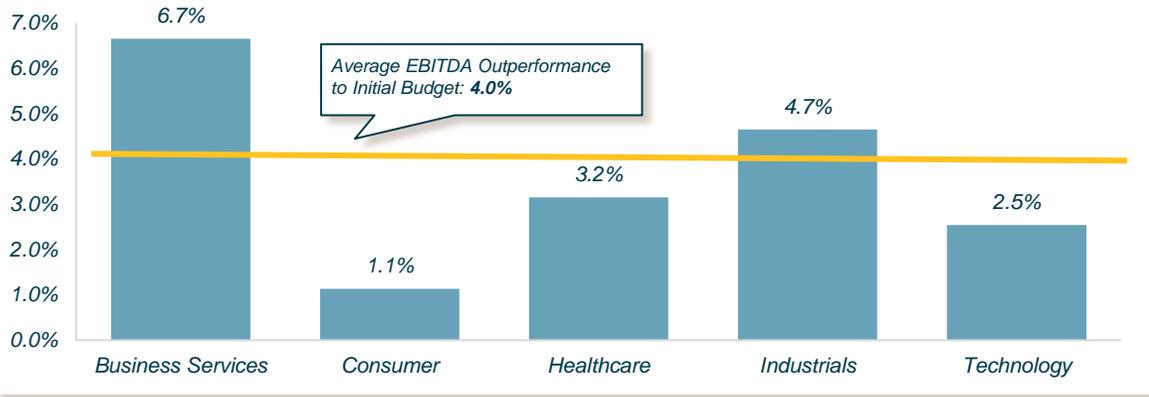
Revenue Comparison – 2021 YTD Actual vs. Initial Budget



Source: Lincoln International Proprietary Middle Market Database.

Private companies have generally outperformed their YTD revenue budgets, reflecting strong fundamental demand and recovery from the COVID-19 pandemic

EBITDA Comparison – 2021 YTD Actual vs. Initial Budget

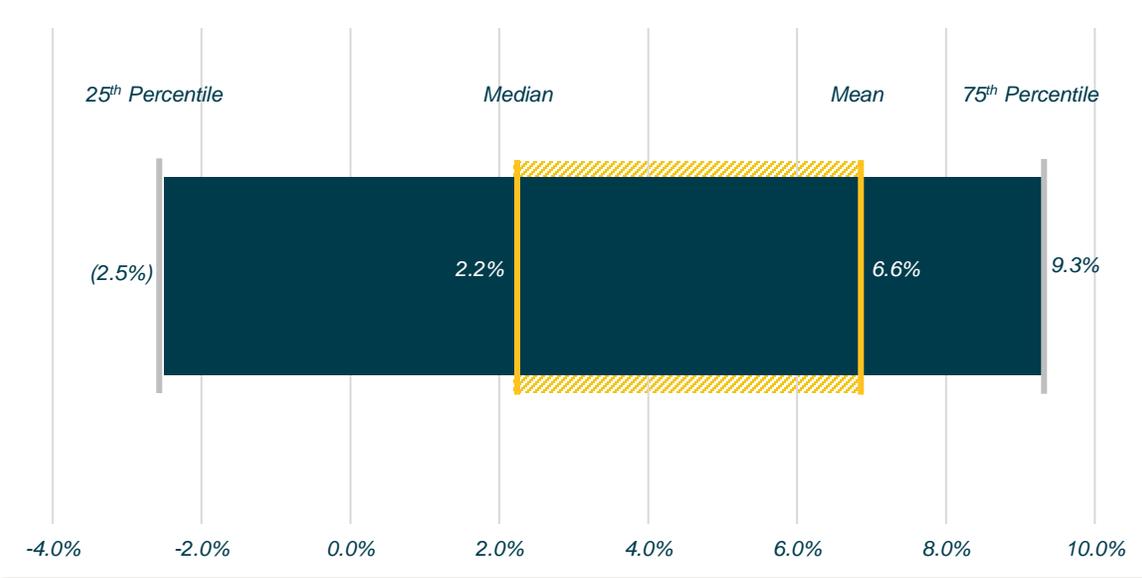


Source: Lincoln International Proprietary Middle Market Database.

As of June 30, 2021, private companies across all industries have outperformed their YTD EBITDA budgets, reflecting a combination of strong operating performance and actions taken by management and sponsors

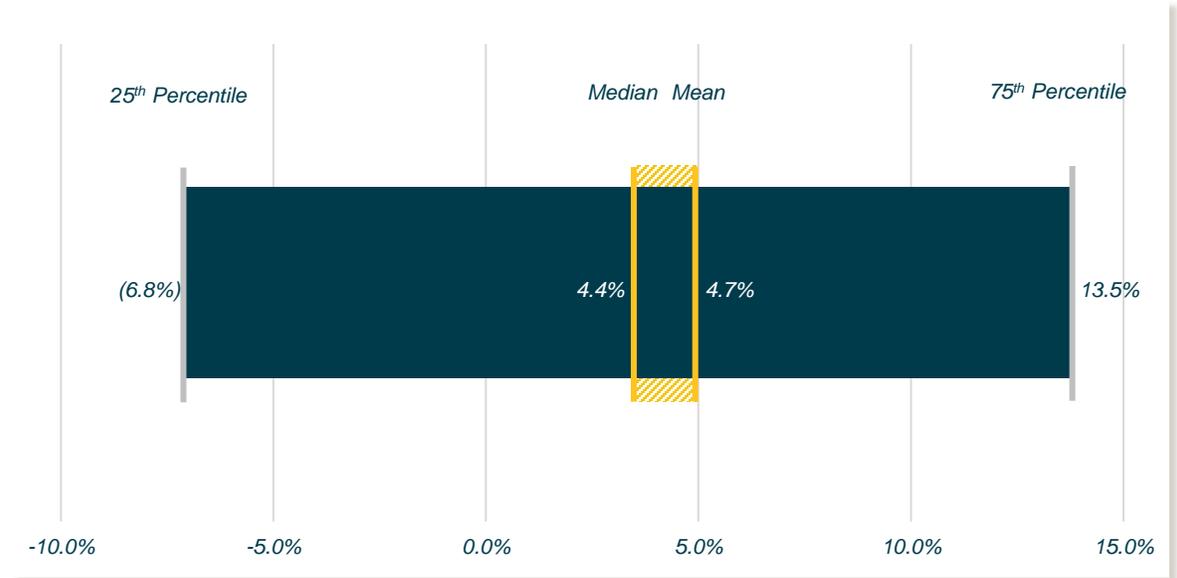
...with Many Companies Further Increasing Their 2021 Forecasts

Increase in Revenue vs Initial Budget through FY 2021



Source: Lincoln International Proprietary Middle Market Database.

Increase in EBITDA vs Initial Budget through FY 2021



Source: Lincoln International Proprietary Middle Market Database.

Considering actual YTD 2021 outperformance compared to YTD 2021 budgets, many companies have re-forecasted FY 2021E and anticipate an average additional increase in Revenue and EBITDA of 6.6% and 4.7%, respectively.

In Addition, Other Unique Dynamics Are At Play

Additional drivers of 2021 deal volume include the following...



1

Transactions re-started following COVID delay in 2020



3

Transactions pulled forward by a very strong / “hot” market



2

Anticipated tax law changes in 2022



4

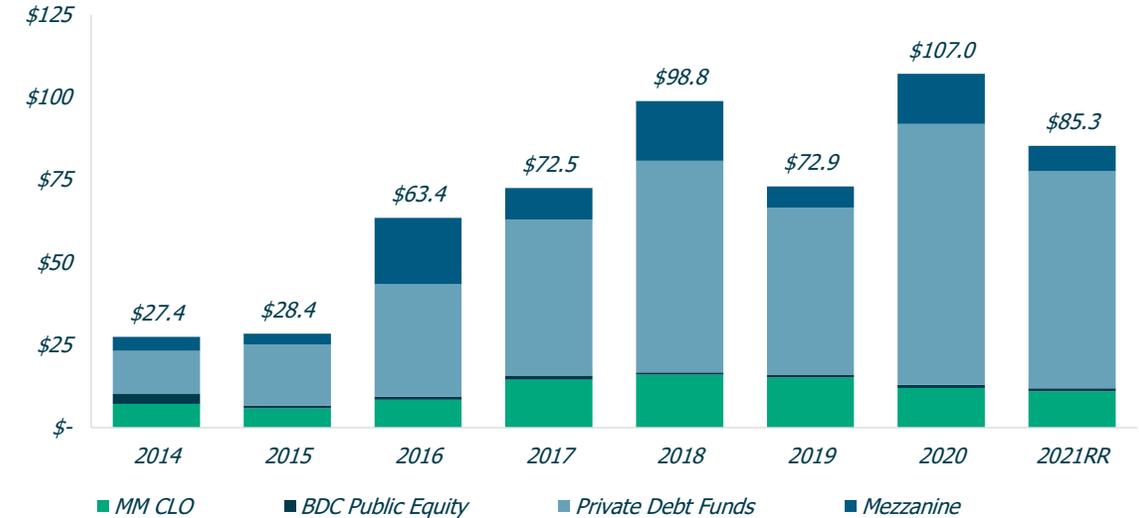
Aggressive Financing Markets

The shift to a more virtual work environment has also accelerated the pace of deal-making and activity

A Highly Competitive Lending Environment is Supporting This Record M&A Activity...

Strong Demand from Investors for Private Debt

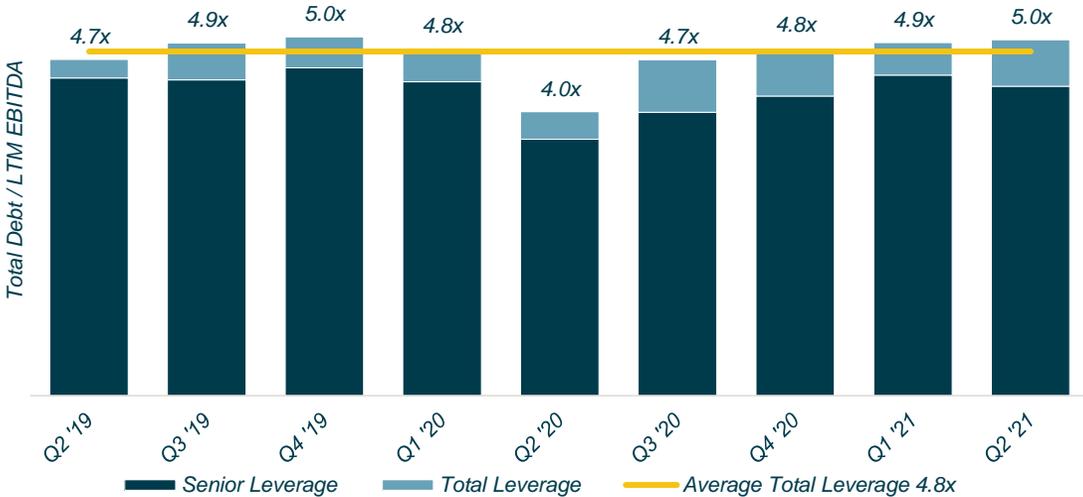
(Middle Market Loan Fundraising (\$ in billions))



Source: LCD, an offering of S&P Global Market Intelligence.

Leverage Has Returned to Pre-Pandemic Levels

(EBITDA Multiples)



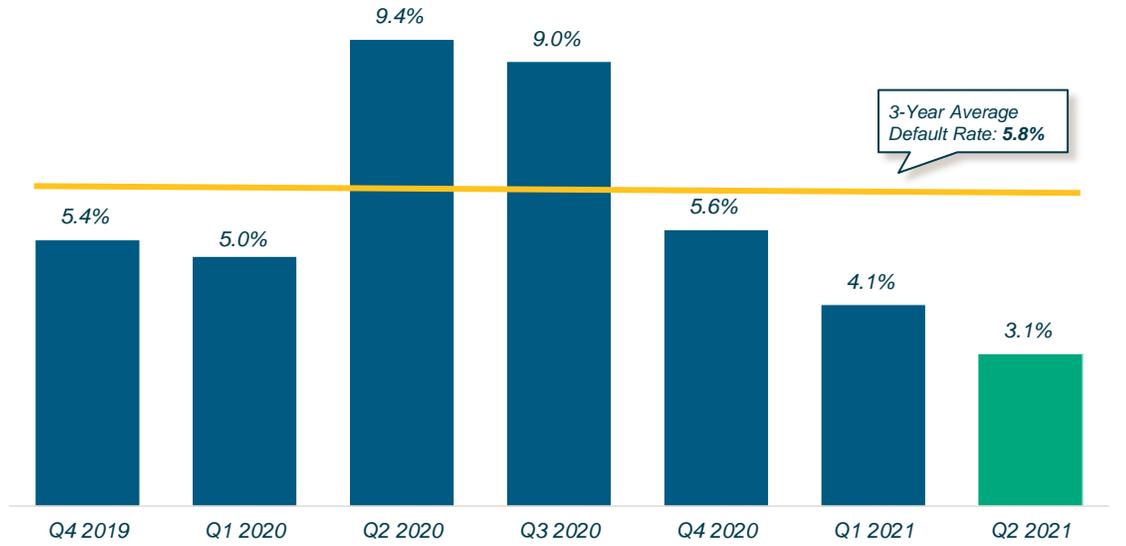
Source: Lincoln International Proprietary Valuations Database

In addition, increased M&A activity is causing lenders to be refinanced out of deals sooner, with this “run off” putting added pressure on lenders to redeploy capital in order to maintain AUM

... With Low Default Rates Enhancing Lenders' Confidence

Declining Technical Covenant Default Rates

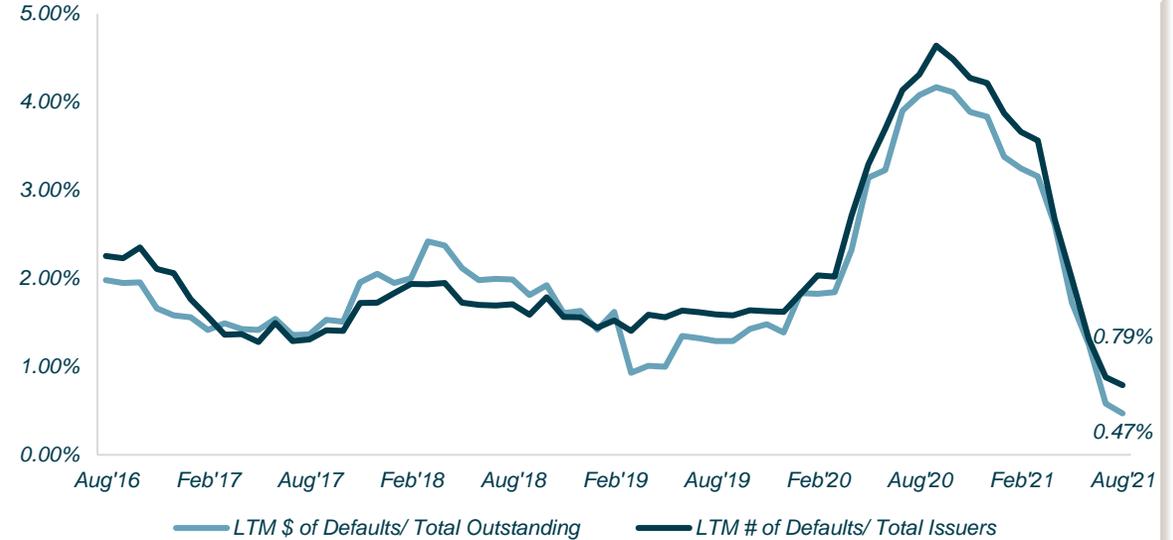
(Historical Size-Weighted Default Rates)



Source: Lincoln International Proprietary Valuations Database.

Declining Monetary Default Rates Across Broader Leveraged Loan Market

(S&P/LSTA Leveraged Loan Index Default Rates)

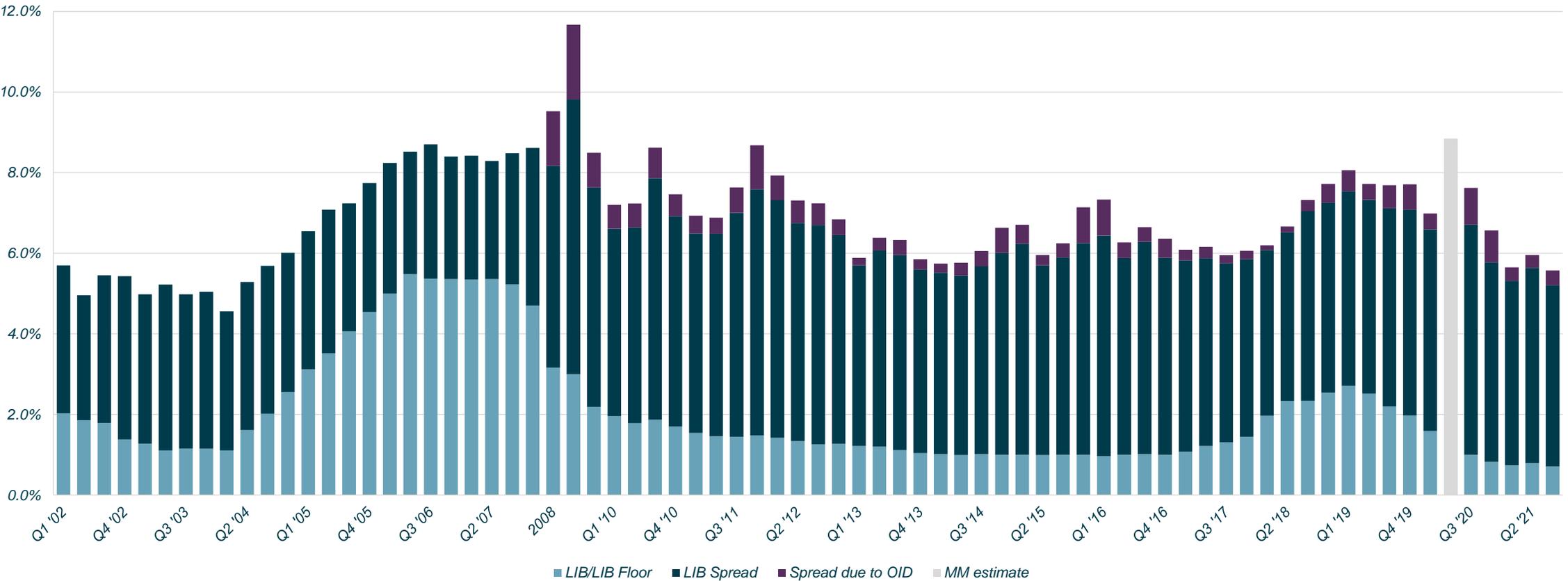


Source: LCD, an offering of S&P Global Market Intelligence.

Lender behavior is also being driven by healthy portfolios; however, features such as low or no scheduled amortization and “cov-wide” or “cov-lite” structures are supporting historically low default rates

Competition has Driven Yields to a 17-Year Low in the Syndicated Market...

Middle market first-lien institutional primary term loan yields have tightened to 5.57% so far in Q3'21



Source: Refinitiv LPC.
 Note: Due to lack of activity, 2Q20 MM yield level is an estimate assuming a 1.21% MM yield premium (avg. MM premium from 2009-1Q20).

...and Private Market Spreads are At or Near All-Time Lows

Private Market Pricing Continues to Trend Lower

(Middle Market 1st-Lien Spread)



Source: Refinitiv PLC.

Unitranche Pricing is Following a Similar Pattern

(Average Unitranche Blended Spread)



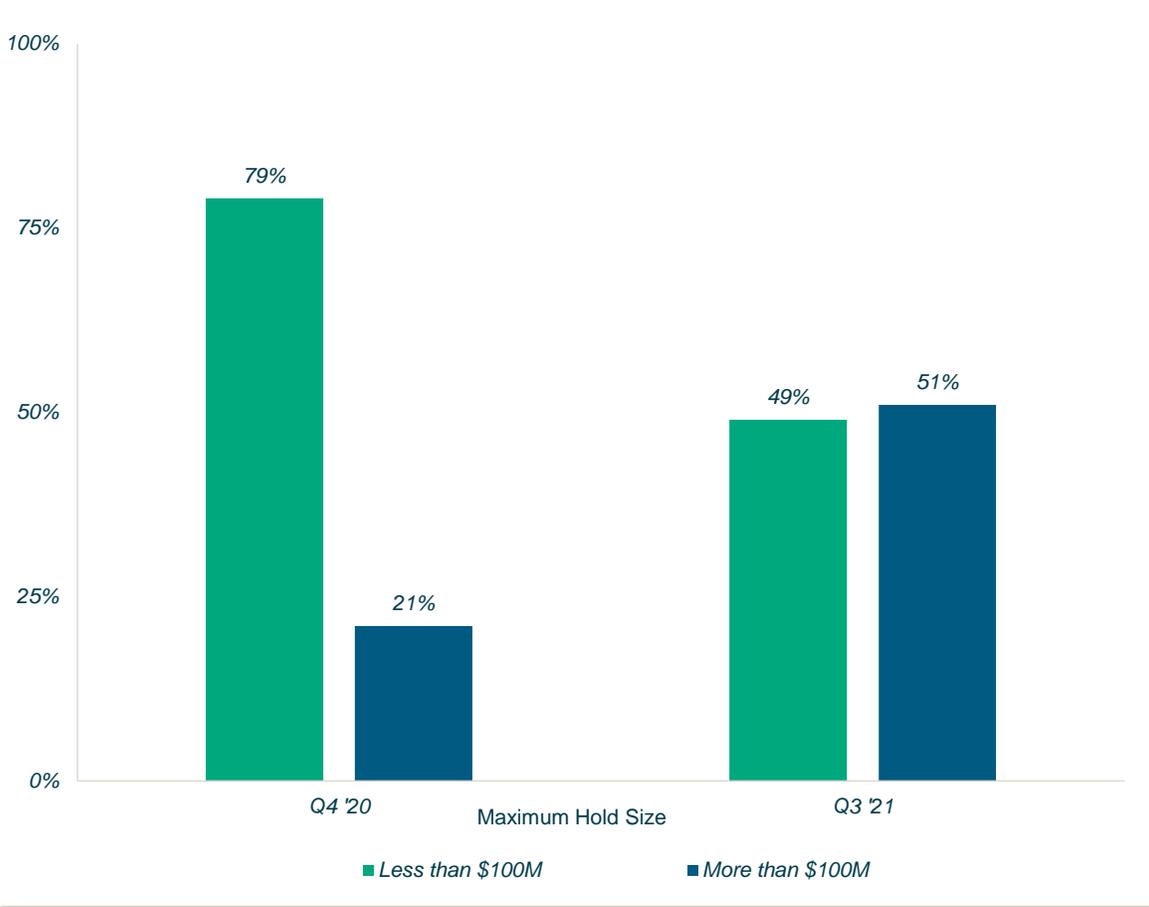
Source: Refinitiv PLC.

New funding vehicles and heavy competition are causing private credit funds to stretch on pricing to win deals

The New Frontier is Now Increased Hold Sizes...

Direct Lenders have Shown Desire to Increase Hold Sizes Significantly

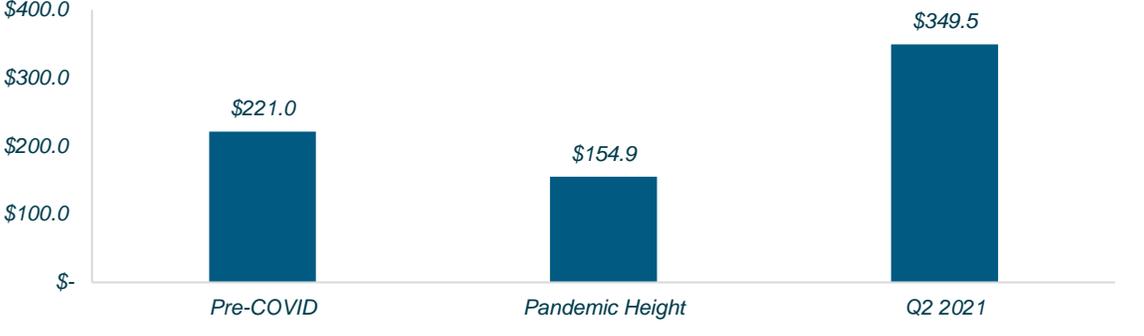
(% of Direct Lenders Surveyed)



Source: Refinitiv PLC.

Average Middle Market Security Tranche Size

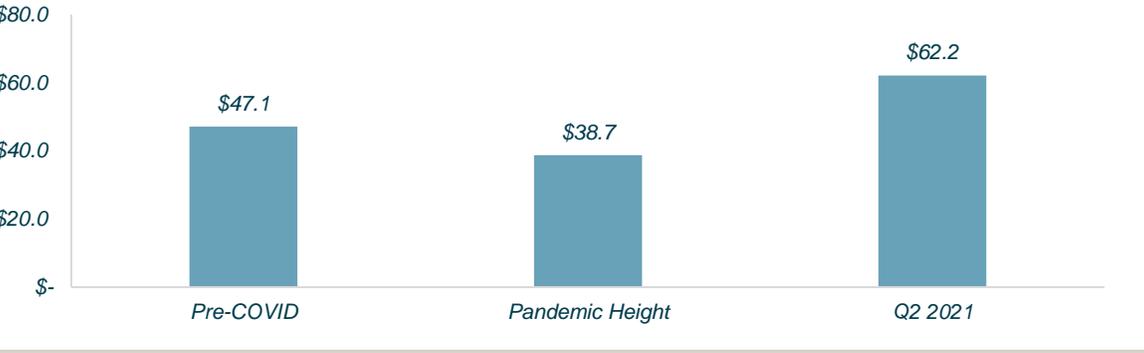
(\$ in millions)



Source: Lincoln International Proprietary Middle Market Database.
 Note: "Pre-COVID" refers to Q1 2019 to Q1 2010; "Pandemic Height" refers to Q2 2020 to Q4 2020.

Average Middle Market Lender Hold Size

(\$ in millions)

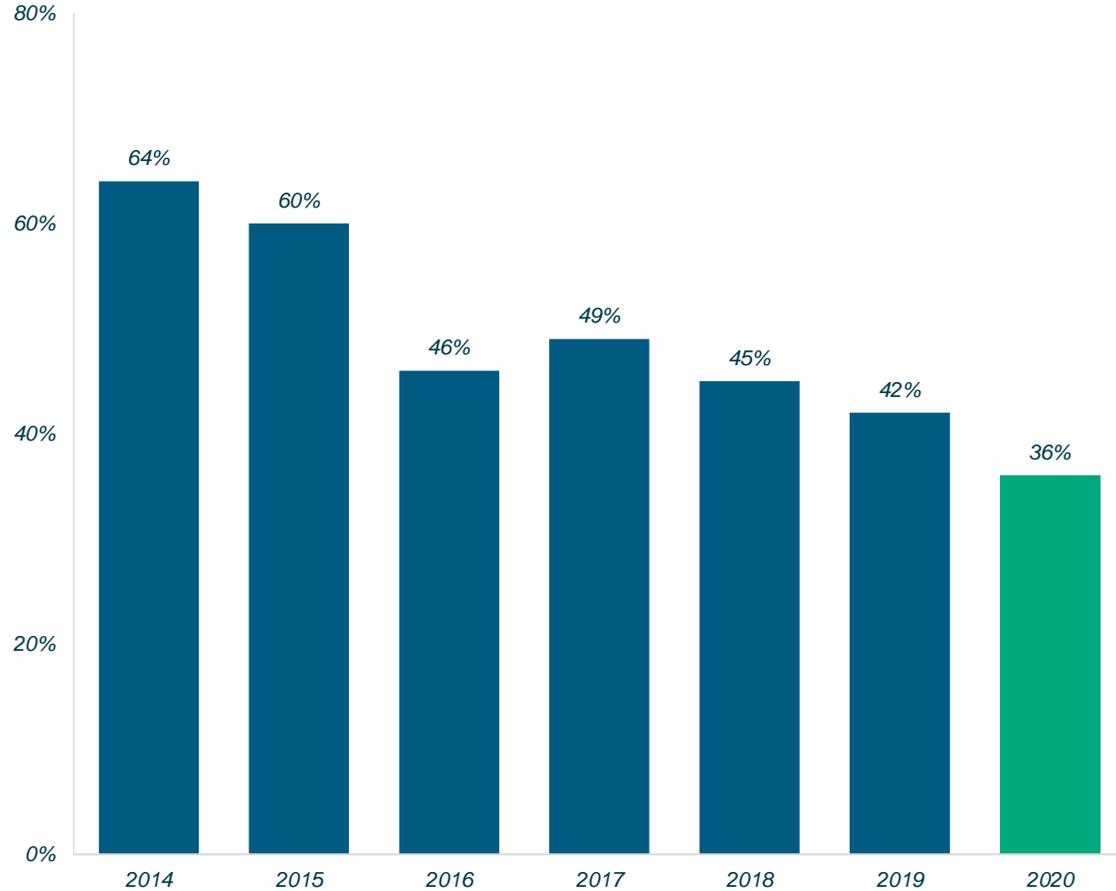


Source: Lincoln International Proprietary Middle Market Database.
 Note: "Pre-COVID" refers to Q1 2019 to Q1 2010; "Pandemic Height" refers to Q2 2020 to Q4 2020.

...Causing a Shift in Market Share on Larger Deals to Private/Club Executions

Significant Decline in Broadly Syndicated Deals < \$500 million...

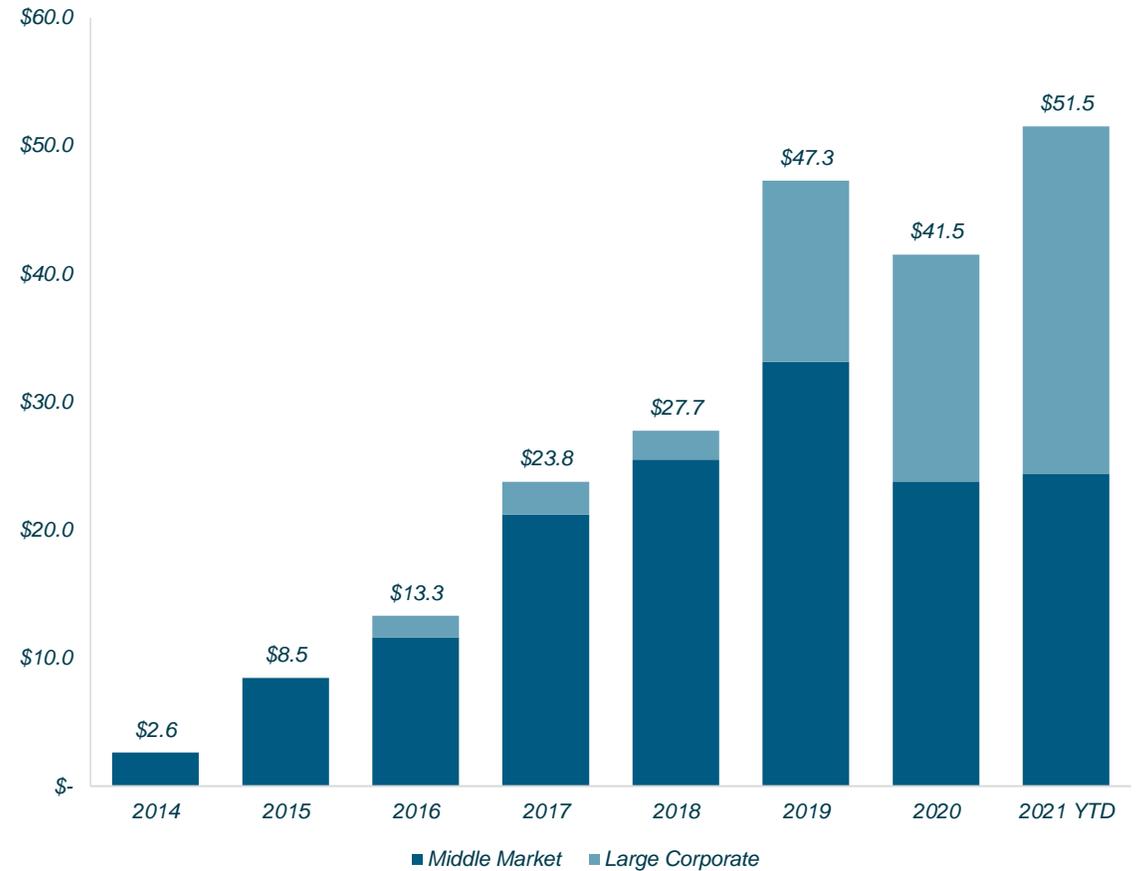
(% of all Broadly Syndicated Loans Under \$500M)



Source: LCD, an offering of S&P Global Market Intelligence.

...while Unitranche Continues to Grow and Moves Into the Large Market

(Unitranche Loan Volume (\$ in billions))



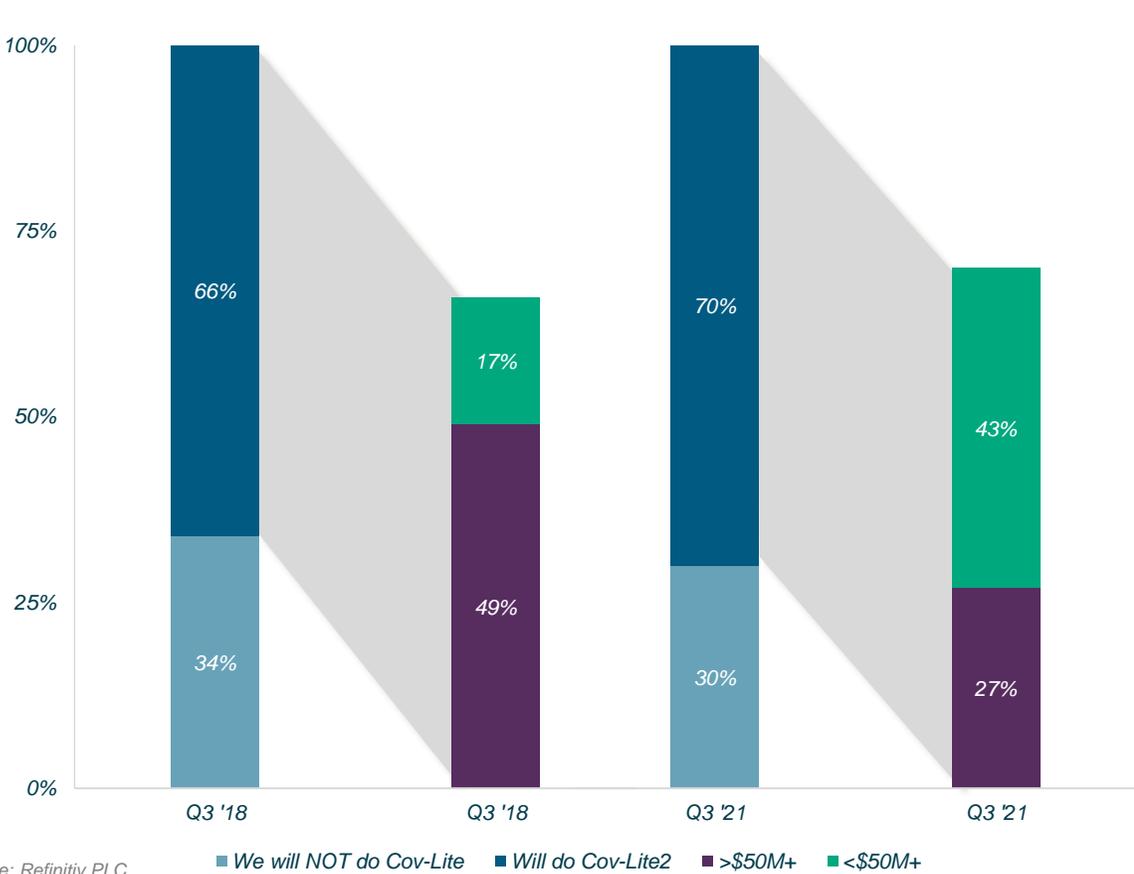
Source: Refinitiv PLC.

Lenders are Willing to Stretch on Covenants and EBITDA Definitions to Win Deals

Lenders Who are Doing Cov-Lite Deals are Reducing Minimum EBITDA Thresholds

(Refinitiv PLC Survey - % of Respondents)

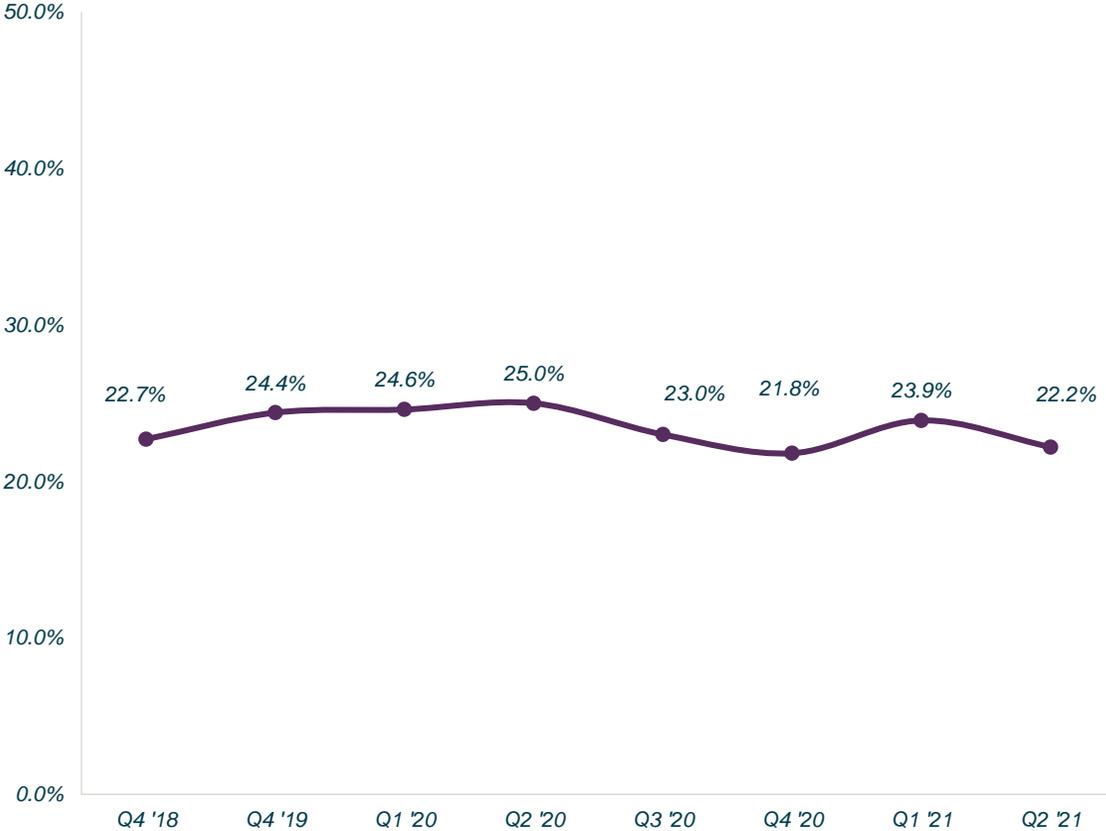
What is your Minimum EBITDA threshold for doing covenant lite transactions?



Source: Refinitiv PLC.

Adjustments Represent ~20-25% of EBITDA

(% Difference Between Adjusted EBITDA and Reported EBITDA)



Source: Lincoln International Proprietary Valuations Database.

In This Environment, What Could Go Wrong?

What is keeping lenders up at night? Potential performance concerns in Q4 2021 and Q1 2022



1 Supply chain disruption / delays



3 Delta COVID-19 variant impacting top line performance



2 Labor supply issues and labor cost increases



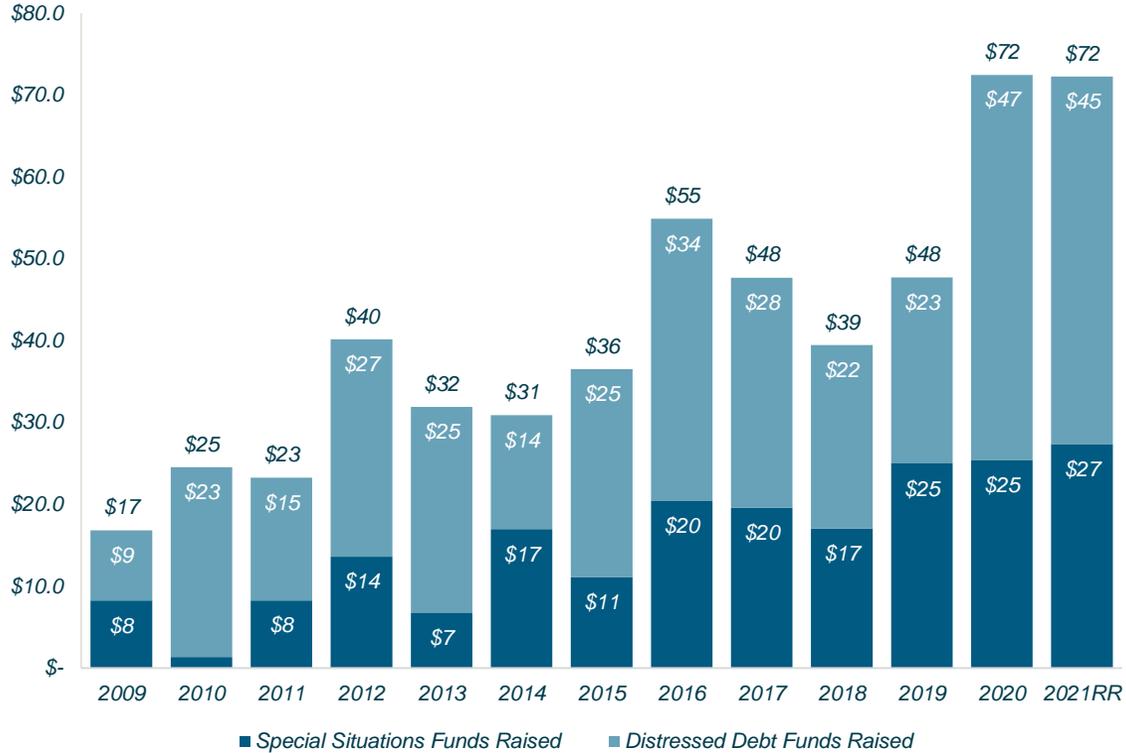
4 General inflationary pressures on margins

However, solutions are readily available in the market for companies impacted by these issues or facing high leverage for other reasons

Solutions for Storied Companies are Readily Available

Significant Capital in the System for Storied Companies

(Size of Funds Raised (\$ in billions))



Source: Prequin.

In response to COVID-19, investors raised significant capital to pursue storied / stressed situations. However, due to the robust M&A markets, much of that capital remains sidelined which has created a competitive market to deploy that capital amongst investors

Recent Lincoln Capital Raises in Similar Scenarios

Situation	<ul style="list-style-type: none"> COVID-19 related shutdowns adversely impacted the business resulting in lower order volumes and revenue/EBITDA contraction Fundamentally strong business with leading market share in their sector 	Consumer Products <i>Confidential</i>
	Outcome	
		
Situation	<ul style="list-style-type: none"> Widespread school closures from COVID forced the Company to halt nearly all operations Large restart costs required a capital injection to fund ongoing liquidity and working capital needs 	Healthcare Services <i>Confidential</i>
	Outcome	
		

Factors to Consider Going into Q4 2021

Performing Companies

1 Increasing lender hold sizes and continued competition are driving borrower-friendly terms and alternatives to public markets

2 Lenders are picking and choosing where to spend their time on the underwriting side (observing emerging capacity constraints)

3 Timing of a process in crowded market is critical to achieve desired financing outcomes

Storied Companies

1 Given capital availability and structure options, now is an opportune time to evaluate capital structure considerations and key stakeholder interests

2 Due to capacity constraints, sponsors need to fully understand timing to engage third-party providers (i.e., market study, QoE, etc.)

3 A continuation vehicle or structured capital solution can also be useful to provide additional time for a storied company or to refinance out fatigued lenders

To take advantage of the strong market conditions and close deals by year-end, sponsors will need to be creative and efficient with financing, including being prepared to approach a broader set of lenders

Q&A



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