Lincoln International

DEALREADER | Distribution

The merger and acquisition newsletter for the distribution sector Q3 2008

Inside this Issue

Welcome to the inaugural issue of the Distribution DealReader, a newsletter focused on merger and acquisition trends, transactions and events of interest to owners and managers of distribution businesses and their advisors.

In this issue, we discuss the relative out-performance of industrial distribution companies, as compared to the overall market, as well as the implication of current M&A valuations.

Other topics covered in this issue include:

- Impact of the decline of credit market conditions on potentially selling a business
- Why foreign acquirer interest in U.S. companies has been increasing
- Key M&A market, lending and stock purchase agreement statistics
- Current industrial distribution public market and comparable transaction valuations
- Recent industrial distribution news
- Profile of United Stationers Inc.'s acquisition of ORS Nasco, an OK-based wholesale distributor of industrial supplies

We hope you find this newsletter a useful tool, and we welcome your comments.

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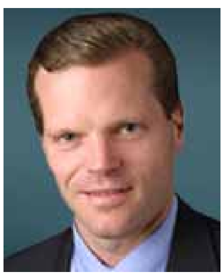
Spotlight On: Industrial Distribution

Public Company Industrial Distribution Index: Relative Out-performance Might Surprise



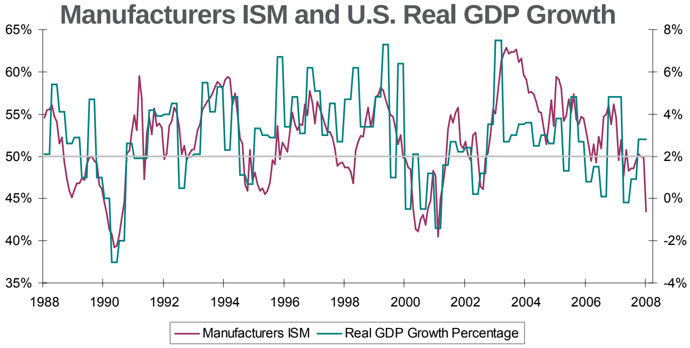
Curt Tatham

Public company valuations within the industrial distribution sector have not been immune to the broader absolute market declines realized over the last twelve months ("LTM"). Indeed, as of September 30, 2008 the Lincoln International Industrial Distribution Index[1] (the "Lincoln International IDI") is down over 25% from its 52- week high. Given industrial distribution companies' activity being tied to underlying economic activity, such declines are not surprising as a reflection of the broader slowdown in economic growth realized over the LTM period both domestically and abroad.

Historically, industrial distribution stocks have shown a correlation with the Institute for Supply Management Index ("ISM"). The ISM is a monthly survey of purchasing and supply managers aimed at providing an assessment of overall trends within the manufacturing sector compared to the previous month. As a rule of thumb, an ISM reading above 50 indicates a growing industrial economy while conversely ratings below 50 indicate a contracting industrial economy.

The charts below summarize ISM data over the last twenty years overlaid with the growth rate of the U.S. GDP which highlights the correlation between the ISM and GDP and the leading indicator nature of the ISM Index.

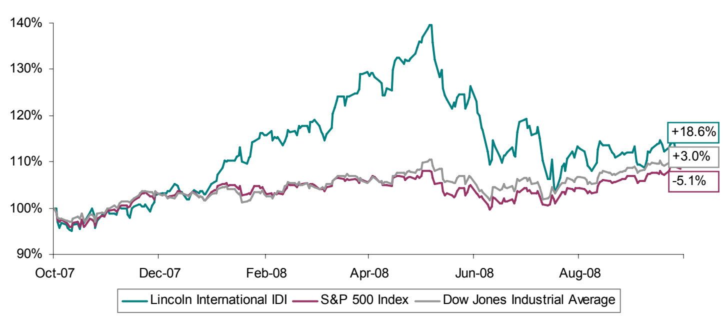
Manufacturers ISM and U.S. Real GDP Growth



Source: Institute for Supply Management and U.S. Bureau of Economic Analysis
Note: (1) See page 6 for list of included companies

The declines in <u>absolute</u> stock price performance may not come as a surprise to most readers due to slowing economic conditions and the impact of the credit crisis on virtually all stocks. However, industrial distribution industry participants can take solace in the Lincoln International IDI's <u>relative</u> out-performance of broader stock market indices as seen in the charts below.

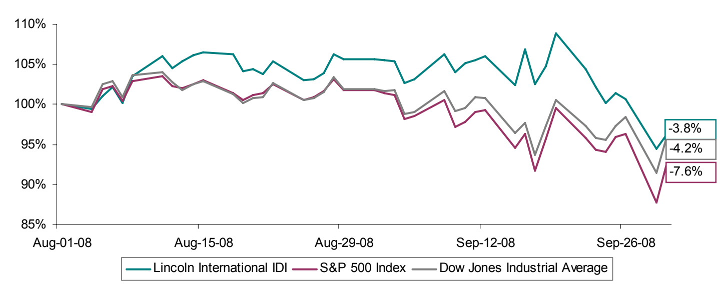
Relative Stock Price Performance: Last 3 Years



Source: Capital IQ
Note: As of September 30, 2008

As the charts indicate, while the absolute stock price performance of the sector has not been able to avoid broader market declines, the sector has outperformed the broader market over the last three years as well as more recently over the last sixty days.

Relative Stock Price Performance: Last 60 Days

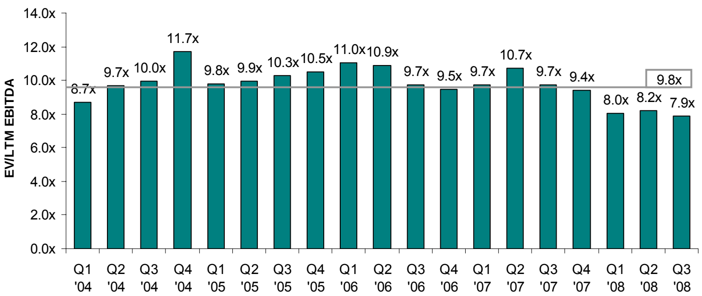


Source: Capital IQ
Note: As of September 30, 2008

(continued)

As it relates to EBITDA valuation multiples of the Lincoln International IDI, the mean multiple stood at 7.9x as of September 30, 2008 which marks the lowest quarterly reading since January, 2004 and is approximately 19% below the average quarterly reading over the same period of 9.8x. The low multiple reflects a less optimistic outlook regarding future performance that is reflected in market capitalizations (and therefore enterprise value) in addition to the fact that the LTM EBITDA remained a relatively robust figure for most companies in the index (i.e. a 'denominator effect" was at work also).

LI IDI Adjusted Mean[1] EV / LTM EBITDA



Source: Bloomberg, Capital IQ and Company Filings
Note: (1) Adjusted mean excludes the high and low values from the calculation

M&A Market Valuation Implications

Generally, M&A multiple trends ultimately have some correlation with public market valuations as both reflect the market's view of the present value of the forecasted free cash flow of the Company. However, in recent months, M&A valuation multiples within the industrial distribution sector have not generally seen a reduction similar to public multiples. In part, this is a reflection that as the M&A market has slowed down, only the highest quality companies have been brought to market for sale. Demand for such companies with attractive growth, profitability and end market dynamics remained reasonably strong through the first three quarters of 2008. As weakening global economic conditions potentially impact the performance of industrial distribution participants, it is likely that this flight to quality will continue and the number of companies able to offer recent and near-term compelling financial performance will fall, and so too will M&A volume within the sector until seller valuation expectations are adjusted downward and/or signs of economic recovery appear. However, challenging economic times often result in consolidation which supports M&A volume in the fragmented industrial distribution sector. ■

Curt Tatham, Director at Lincoln International, has over 15 years of experience advising owners and senior executives of distribution businesses. Clients have included large and mid-market public corporations, leading private equity firms and privately held or family owned businesses.

Lincoln International Performs in a Challenging Market: Five Recently Completed M&A Transactions in Eight Days

In today's economic climate, there is one question that continues to be asked:

Are deals still getting done?

With five M&A transactions completed within eight business days in Q3, the results speak for themselves. To Lincoln International, a challenging market is exactly that: a challenge.

With over 120 bankers working together across nine offices worldwide, Lincoln International has the resources and perseverance it takes to overcome challenges and exceed our clients' expectations on every assignment, in any environment.

Recently completed Lincoln International transactions—Fall 2008

D.S. BROWN has been sold to ALTUS CAPITAL PARTNERS

KATUN a portfolio company of Bank of America and SVOBODA, COLLINS LLC has been acquired by MONOMOY CAPITAL PARTNERS

RAD ELECTRONICS A portfolio company of Chrysalis VENTURES has sold ASTREX ELECTRONICS to ROCKWOOD EQUITY PARTNERS LLC

nmt has sold certain assets to nep

Baird Capital Partners has sold XALOY to INDUSTRIAL GROWTH PARTNERS

Impact of the decline of the credit market conditions on selling your business

Patricia Luscombe

With the aging of the Baby Boomer generation, many business owners will consider selling their companies in the next few years. As a result, many business owners are trying to understand how the changing tide in credit markets impacts valuation levels for their business.

The ability to raise financing is critical to the successful completion of many private equity transactions. Therefore, the decline in liquidity of the credit markets has significantly lowered private equity deal activity. Overall transaction values are down as private equity deals are now being financed below 4.0x EBITDA as compared to peak EBITDA lending multiples of 6.0x or more.

In response to the decline in private equity acquisition activity, U.S. strategic buyers, including public and large private companies, have become more active in pursuing their mergers-and-acquisitions goals. Cash balances for U.S. public companies are strong and U.S. strategic buyers are typically not dependent upon the state of the financing markets to close transactions. Strategic buyers are often willing to pay premiums beyond what private equity buyers pay. Many times, they enjoy significant synergies as they fold the acquisition into their larger corporation and drive significant revenue enhancements and cost savings. And while it is true that, due to U.S. economic recession concerns, some U.S. strategic buyers are cautious, foreign strategic buyers are growing their share of U.S. M&A activity caused by the weak dollar.

What does this mean for the shareholders thinking of selling its stake in a business? Understand your intrinsic value and what competitive advantages you have to offer. Intrinsic value captures the business's true value, including tangible and intangible factors. Key to understanding intrinsic value is measuring a company's cost of capital relative to its actual profit return on its invested equity and debt capital. The business with high returns on its invested capital in this uncertain economic environment is commanding premium value with both private equity and strategic buyers.

"The time to sell is not always driven by external market factors or capturing the M&A market at its peak. There are a host of other issues that a business owner must consider when deciding whether to sell. "

The time to sell is not always driven by external market factors or capturing the M&A market at its peak. There are a host of other issues that a business owner must consider when deciding whether to sell. Whatever the reason for a possible sale, business owners should carefully consider the value their business brings to the negotiating table to find the right buyer in this time of credit market and economic uncertainty. An experienced financial advisor with a keen understanding of both intrinsic value and the M&A markets will help a business owner maximize shareholder returns. ■

Why do a formal valuation?

Recently, Lincoln International was involved in the sale of a division of a privately-owned business that was in the midst of a financial and operational turnaround. The business received an unsolicited cash offer from a strategic buyer.

Lincoln completed a valuation of the division and determined that it was an excellent offer, significantly greater than what a financial buyer could pay. The offer reflected net sales increases and cost savings synergies that the strategic buyer would receive in the future after the transaction closed.

As the division's profitability was significantly lower than it had been historically and given the state of the credit markets, a financial buyer would not have been able to bid anywhere close to what the strategic buyer was offering.

All in all, this was an excellent transaction for this business and reflected the strength of strategic buyers in the current marketplace with their cash-strong balance sheets.

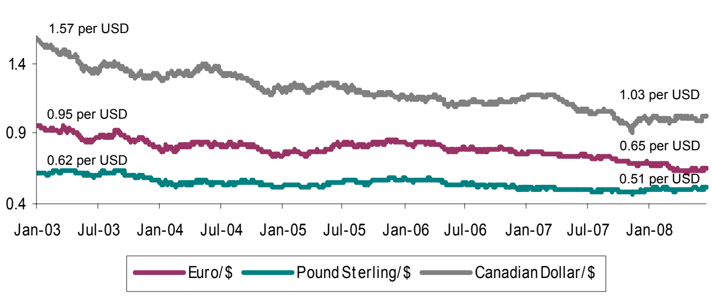
Patricia Luscombe, Managing Director at Lincoln International, has over 20 years of experience in financial advisory and valuation services. She has delivered a broad range of corporate finance advice that resulted in the successful completion of corporate transactions and valuation and fairness opinions.

Patricia is a member of the Chicago Chapter of the Association for Corporate Growth and Business Valuation Association, the Chartered Financial Analyst Society of Chicago and a Board member and former president of the Chicago Finance Exchange.

Foreign Acquirer Interest in U.S. Companies Remains Historically Strong

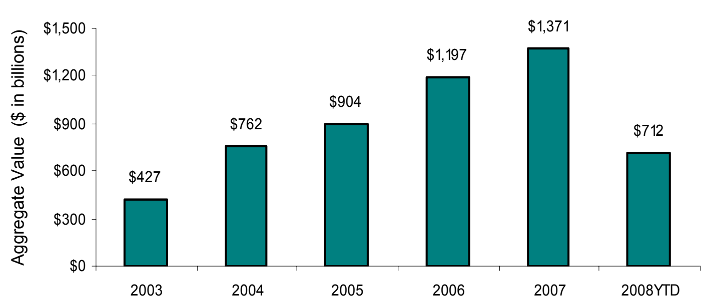
The recent weakness of the U.S. dollar has made U.S. domestic assets attractive to foreign buyers. Total aggregate deal value of U.S. businesses acquired by foreign companies in disclosed transactions increased from $427 billion in 2003 to $1,371 billion in 2007.

Value of the U.S. Dollar Relative to Other Currencies



Source: Oanda.com

Total Value of U.S. Deals with Foreign Acquirers

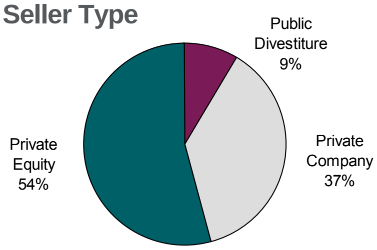


Source: Mergermarket Note: Includes only deals for which transaction values were reported
Note: 2008YTD Represents transactions through September 30, 2008

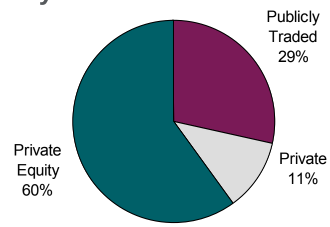
The Market Pulse: Data That Affects The Mid-Market M&A Landscape

Lincoln International Completed Transaction Data *(Last 12 months)*

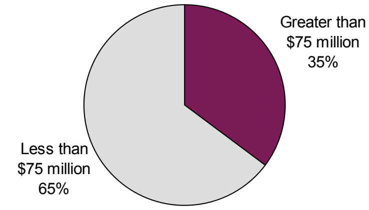
Seller Type



Buyer Profile



Enterprise Value



Valuation Statistics: Average Enterprise Value Multiples

	EV / LTM EBITDA		EV / LTM Revenue	
	Adj. Mean	Median	Adj. Mean	Median
Less than $75 million	7.65x	6.96x	1.00x	0.90x
Greater than $75 million	9.06x	8.73x	1.27x	1.18x

Note: Adjusted mean excludes high and low values prior to mean average calculation

Key Purchase Agreement Terms - Lincoln International U.S. Transactions

Escrow as a Percentage of Purchase Price

	Less than $75m		Greater than $75m	
	Mean	Median	Mean	Median
Public Buyers	8.09%	10.00%	8.00%	7.50%
Private Equity Buyers	6.47%	6.25%	4.97%	5.11%
Private Buyers	4.55%	4.55%	6.27%	6.27%
All Transactions	**6.53%**	**7.50%**	**5.95%**	**6.10%**

Indemnity Cap as a Percentage of Purchase Price

	Less than $75m		Greater than $75m	
	Mean	Median	Mean	Median
Public Buyers	18.58%	20.00%	8.55%	8.15%
Private Equity Buyers	8.96%	9.50%	9.65%	7.50%
Private Buyers	21.67%	20.00%	6.72%	6.72%
All Transactions	**13.75%**	**10.00%**	**8.94%**	**7.50%**

Basket as a Percentage of Purchase Price

	Less than $75m		Greater than $75m	
	Mean	Median	Mean	Median
Public Buyers	0.70%	0.40%	0.60%	0.75%
Private Equity Buyers	0.61%	0.55%	1.40%	0.73%
Private Buyers	2.33%	1.00%	0.65%	0.65%
All Transactions	**0.87%**	**0.55%**	**1.10%**	**0.75%**

Indemnity Term (in months)

	Less than $75m		Greater than $75m	
	Mean	Median	Mean	Median
Public Buyers	12.00	12.00	17.00	15.00
Private Equity Buyers	14.75	15.00	14.88	16.50
Private Buyers	15.33	16.00	13.50	13.50
All Transactions	**13.95**	**15.00**	**15.15**	**15.00**

Source: All Lincoln International data

Transaction Spotlight: ORS Nasco

On January 2, 2008, United Stationers Inc.'s ("United Stationers") wholly owned subsidiary, United Stationers Supply Co., acquired ORS Nasco Holding, Inc. ("ORS Nasco") from Brazos Private Equity Partners, LLC and other shareholders for approximately $184 million. Lincoln International acted as the exclusive financial advisor to United Stationers in the transaction.

Headquartered in Muskogee, Oklahoma, ORS Nasco is a pure wholesale distributor of industrial supplies, with annual sales of approximately $285 million. The company sells exclusively to independent distributors, offering them about 200,000 premium branded and private label products from over 600 manufacturers. ORS Nasco sells to more than 10,000 independent distributors in multiple channels, including industrial, maintenance, repair and operations ("MRO"), safety, construction, welding and oilfield services. The company serves a very diverse customer base through eight distribution centers strategically located across the U.S.

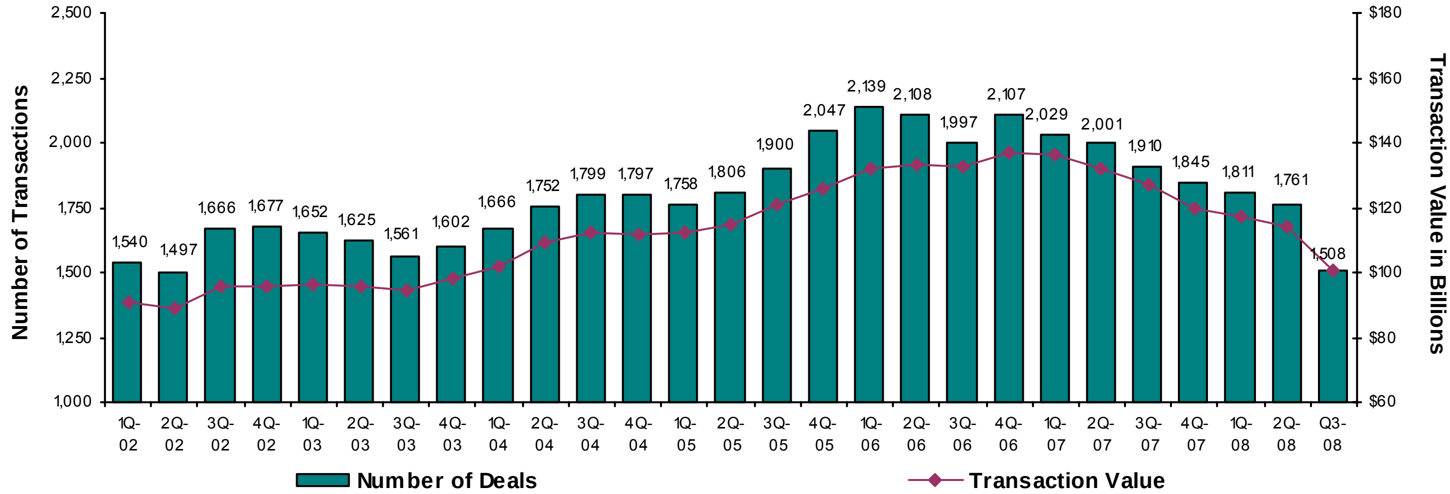
United Stationers sought to strategically add a new industrial products platform and engaged Lincoln to review the acquisition target and complete a thorough and detailed evaluation of the opportunity. Lincoln utilized its mid-market expertise and industrial distribution experience to compile an extensive valuation assessment, including synergy and sensitivity analysis.

The acquisition of ORS Nasco builds on Lincoln International's strong industrial distribution and business services experience. The Lincoln International transaction team worked closely with United Stationers' senior management to evaluate the acquisition and provide valuable insight and assistance. ■

Mid-Market M&A Activity and Outlook

- Mid-market M&A activity has continued to decline through Q3 2008
- Leverage multiples have come down from their 2007 peak but have increased in Q3 2008 as compared to the first half of the year
- As leverage levels have come down, buyers' percentage equity contributions increased substantially in the first three quarters of 2008

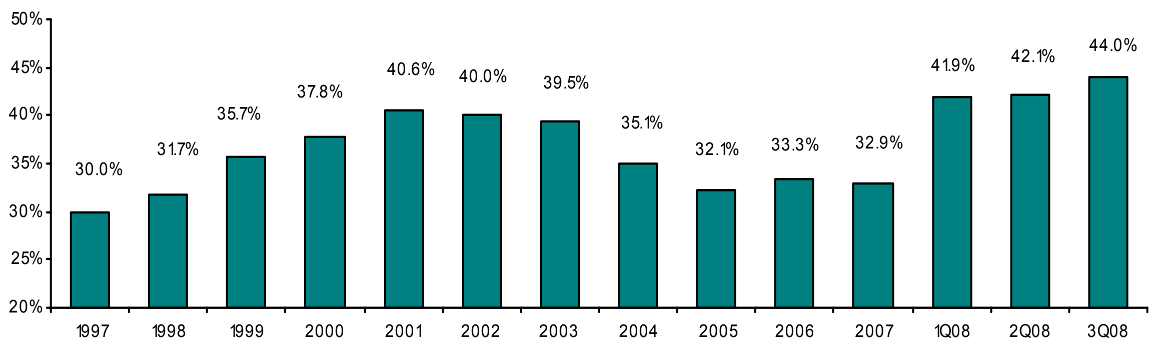
Mid-Market M&A Transaction Volumes *(Rolling 12 months)*



Source: Factset Mergerstat
Note: Transaction values between $10 million and $250 million

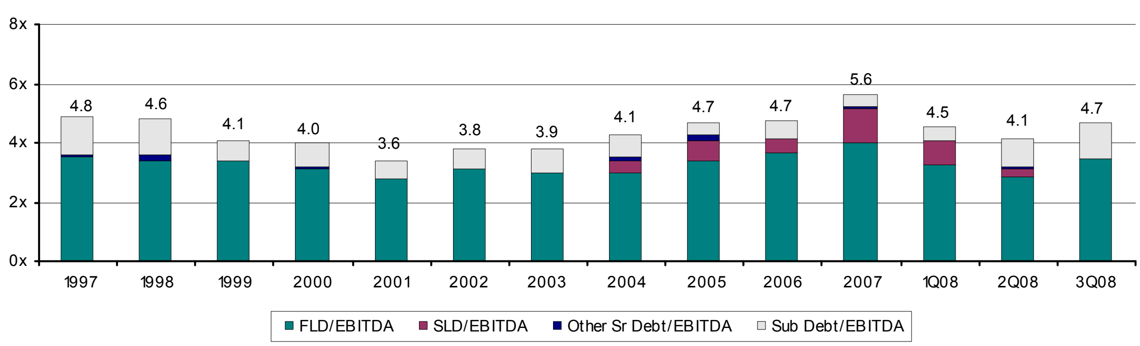
Current Financing Market Statistics

Equity as a Percentage of Total LBO Capitalization



Source: Standard & Poor's Leveraged Commentary and Data
Note: Transactions for companies <$50mm EBITDA, with average EBITDA at $29 million

Average Debt Multiples of Mid-Market LBO Loans



Source: Standard & Poor's Leveraged Commentary and Data

Valuation Update: Lincoln International IDI

Select Industrial Distribution Public Comparables: As of September 30, 2008

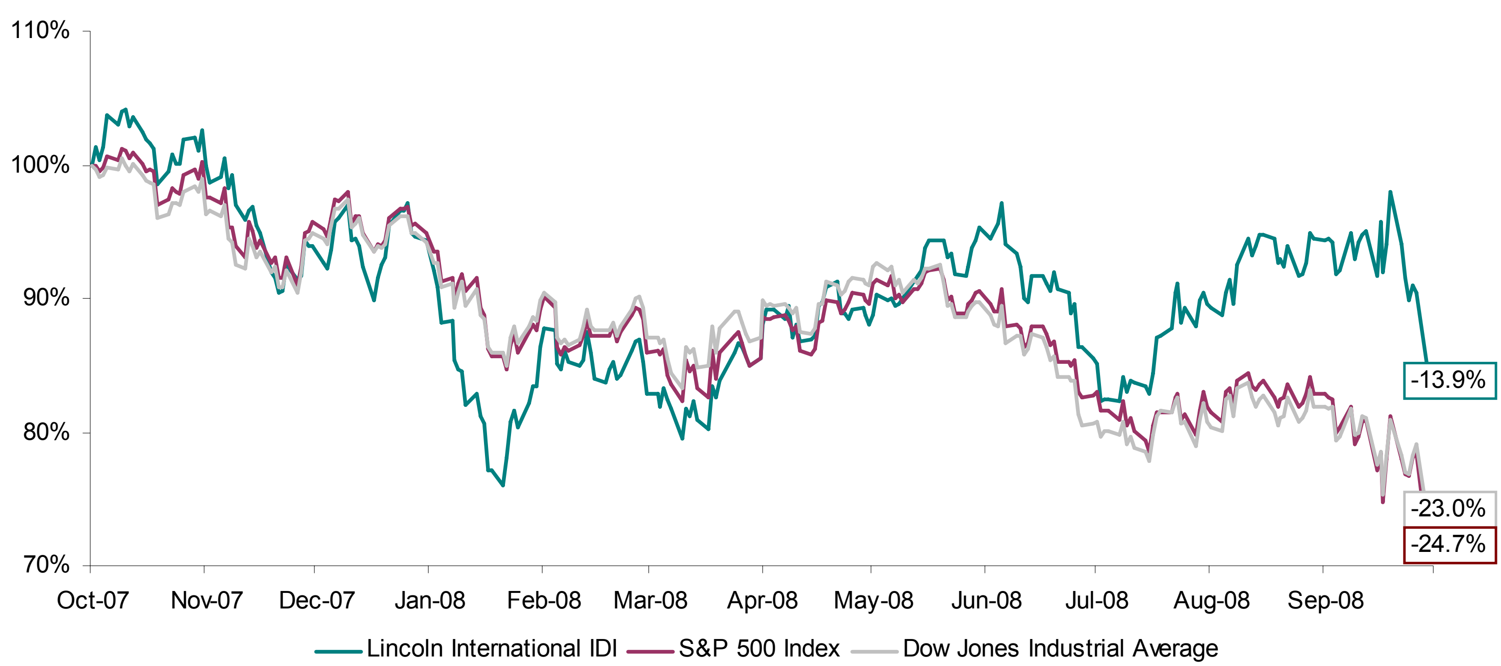
(Dollars in millions except per share data)

Company Name	Market Cap	Enterprise Value	Enterprise Value / LTM Revenue	Enterprise Value / LTM EBITDA	Enterprise Value / LTM EBIT	Stock Price	% of 52 Week High
Fastenal Co.	$ 7,336	$ 7,259	3.3x	15.7x	17.1x	$ 49.39	87.4%
W.W. Grainger, Inc.	6,630	6,894	1.0x	8.1x	9.6x	86.97	90.6%
Airgas Inc.	4,095	5,667	1.3x	8.0x	11.1x	49.65	75.9%
Rexel SA	3,544	8,003	0.5x	8.3x	9.4x	13.88	64.7%
MSC Industrial Direct Co. Inc.	2,897	3,079	1.7x	8.8x	9.5x	46.07	84.4%
Anixter International Inc.	2,091	3,097	0.5x	6.2x	6.7x	59.51	68.4%
Watsco Inc.	1,424	1,443	0.8x	12.5x	13.3x	50.28	82.3%
WESCO International Inc.	1,361	2,531	0.4x	6.1x	6.6x	32.18	63.1%
Applied Industrial Technologies, Inc.	1,140	1,063	0.5x	6.4x	7.0x	26.93	75.5%
Barnes Group Inc.	1,100	1,544	1.0x	6.7x	8.7x	20.22	54.8%
Kaman Corp.	723	807	0.7x	10.4x	12.1x	28.48	72.4%
Interline Brands Inc.	525	878	0.7x	7.1x	8.2x	16.21	64.1%
DXP Enterprises Inc.	341	445	0.7x	9.1x	10.8x	26.66	78.1%
UMECO plc	325	428	0.7x	7.9x	9.9x	6.76	59.0%
Houston Wire & Cable Company	304	353	0.9x	7.2x	7.3x	17.17	75.5%
Lawson Products Inc.	236	244	0.5x	5.6x	6.8x	27.65	71.4%
Bossard Holding AG	173	277	0.5x	5.3x	6.7x	57.49	65.3%
Mean			**0.9x**	**8.2x**	**9.5x**		**72.5%**
Adjusted Mean[1]			**0.8x**	**7.9x**	**9.1x**		**72.5%**
Median			**0.7x**	**7.9x**	**9.4x**		**72.4%**

Source: Bloomberg, Capital IQ and company filings
Note: (1) Adjusted mean excludes the high and low values from the calculation

LTM Relative Stock Price Performance:

(October 1, 2007 through September 30, 2008)



Source: Capital IQ

Precedent Transaction Update

Select Precedent M&A Transactions: Industrial Distribution *(Dollars in millions)*

Date	Target Company	Acquiring Company	Implied Transaction Value	Transaction Value / LTM Revenue	Transaction Value / LTM EBITDA
Pending	Albedo Limited	HealthTrends Medical Investments Pte.	N/A	N/A	N/A
Pending	Maurice Electrical Supply Co. Inc.	U.S. Electrical Services Inc.	N/A	N/A	N/A
Pending	CJ's Sales and Service of Ocala, Inc.	Titan Energy Worldwide, Inc.	N/A	N/A	N/A
Oct-08	Industrial Rubber and Mechanics Inc.	Kaman Industrial Technologies Corp.	N/A	N/A	N/A
Oct-08	Rubber Belting and Hose Inc.	Lewis-Goetz and Co. Inc.	N/A	N/A	N/A
Sep-08	North Coast Instruments	FCX Performance Inc.	N/A	N/A	N/A
Sep-08	Drago Supply Co.	Motion Industries Inc.	N/A	N/A	N/A
Sep-08	ActionEmco Holdings, LLC	United Stationers Inc.	15.0	N/A	N/A
Aug-08	Fluid Power Resources	Applied Industrial Technologies Inc.	169.0	N/A	N/A
Aug-08	Higiene en Colectividades S.A.	Bunzl plc	N/A	N/A	N/A
Aug-08	Industrial Distribution Group Inc.	Luther King Capital Management	133.0	0.3x	14.8x
Aug-08	Industrial Power Sales, Inc.	Atlas Copco Group	N/A	N/A	N/A
Aug-08	Quality Screw & Nut Company	Anixter International Inc.	80.0	N/A	N/A
Jul-08	Honeywell Consumables Solutiont	BE Aerospace	1,063.0	1.9x	N/A
Jul-08	Heaps & Partners	Management	N/A	N/A	N/A
Jun-08	Suministros Industriales Enol, S.A. de C.V.	Applied Industrial Technologies Inc.	N/A	N/A	N/A
Jun-08	Excel Industriel	Acklands-Grainger Inc.	N/A	N/A	N/A
May-08	Callaway Safety Equipment Co., Inc.	Total Safety U.S., Inc.	N/A	N/A	N/A
May-08	NuCO2 Inc.	Aurora Capital Group	470.2	3.5x	11.3x
May-08	N. H. Bragg & Sons	Valley National Gases Inc.	N/A	N/A	N/A
Apr-08	SIA Tapeks Noma	Cramo plc	N/A	N/A	N/A
Mar-08	A.E. Hydraulic (Pte) Ltd.	Tomkins plc	N/A	N/A	N/A
Jan-08	GA Industries	Rexnord LLC	76.0	N/A	N/A
Jan-08	Wolfenden Industries, Inc.	Valley National Gases Inc.	N/A	N/A	N/A
Jan-08	Tri-County Petroleum, Inc.	KRG Capital Partners, L.L.C	N/A	N/A	N/A
Jan-08	Pima Welding Supply, Inc.	Airgas Inc.	N/A	N/A	N/A

Source: Bloomberg, Capital IQ, Industrial Distribution Magazine and company filings

Recent Industry News and Notes: Industrial Distribution

- 10/16/2008: **Sterling Investment Partners,** along with management, acquired a majority stake in **FCX Performance Inc.**, from **Truflo International Group**
- 10/3/2008: **Anixter International Inc.** acquired the operations of **World Class Wire & Cable Inc.,** for $62 million in cash and the assumption of undisclosed liabilities
- 10/3/2008: **High Road Capital Partners** completed the acquisition of **All Current Electrical Sales, Inc**., a wholesale reseller of electrical parts and components
- 10/2/2008: **Fastenal Co.** released comments on its strong September sales. **Sales grew 26.4%** during the month, as compared with the same period last year.
- 10/2/2008: **Valley National Gases, LLC** agreed to acquire **General Welding Supply** and plans to continue its strategy of growth through selective acquisitions
- 9/30/2008: **Revenues for Brady Corp. rose 11.8%** during the fiscal year ended July 31, 2008, topping $1.5 billion compared with $1.4 billion during the prior year
- 9/25/2008: **DXP Enterprises Inc.** was named the **fifth fastest-growing company** in the U. S. by Fortune magazine, citing a three-year annual growth rate of 50%
- 9/11/2008: **McJunkin Red Man Corp**. named Andrew Lane, former COO of Halliburton Co., as its new CEO effective immediately
- 9/11/2008: August **sales for W.W. Grainger Inc. rose 7%,** compared with the same period last year. Branch-based sales rose 6% compared with August 2007.
- 9/10/2008: **Fastenal Co.** will be **listed on the Standard & Poor's 500 Index**, replacing mortgage backing firm Fannie Mae
- 9/3/2008: **Kinecor LP** agreed to acquire Montreal-based **Weir Process Equipment**, for $25.4 million. **Weir** posted sales of approximately $50 million in 2007.
- 9/2/2008: **Genuine Parts Company** acquired **Drago Supply Company**, a regional industrial supplies distributor headquartered in Port Arthur, Texas
- 9/2/2008: **United Stationers Supply Company** signed a definitive agreement to acquire New Jersey-based **ActionEmco Holdings, LLC**, for $15 million in cash
- 8/28/2008: **DXP Enterprises, Inc.** announced the acquisition of Rhode Island-based **PFI, LLC (Vertex Distribution, Inc.)**, for approximately $65 million

Lincoln International's Global Footprint

More than 70 professionals in the U.S.

More than 55 professionals plus a 19-person advisory board in Europe

Office in Japan and strategic partnerships in China and India

Indicates Lincoln International office

Indicates strategic partnership and/or Lincoln International personnel

About Lincoln International

Lincoln International specializes in merger and acquisition services, debt advisory services, UK pensions advisory and providing fairness opinions and valuations for leading organizations involved in mid-market transactions. With offices in Chicago, Frankfurt, London, Los Angeles, New York, Madrid, Paris, Tokyo and Vienna and strategic partnerships with China Everbright and other partner firms in Asia, Lincoln International has strong local knowledge and contacts in the key global economies. The organization provides clients with senior-level attention, in-depth industry expertise and integrated resources. By being focused and independent, Lincoln International serves its clients without conflicts of interest. More information about Lincoln International can be obtained at **www.lincolninternational.com**

Industry Groups

Lincoln International dedicates teams headed by senior professionals in each of its global offices to the following industries:

- Aerospace and Defense
- Automotive and Truck
- Building and Construction
- Business Services
- Chemicals
- Consumer
- Distribution
- Electronics
- Industrials
- Packaging
- Technology

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