# DealReader
## Valuations & Opinions
### Spring 2017

Welcome to the latest issue of the Valuations & Opinions Group DealReader, a newsletter offering insights on valuation topics of interest to financial executives, business owners, and investment and valuation professionals. We are pleased to provide commentary regarding relevant valuation topics and keep you informed about developments at our firm and in the market.

# Inside this Issue



Lincoln
INTERNATIONAL

**Article Written by**

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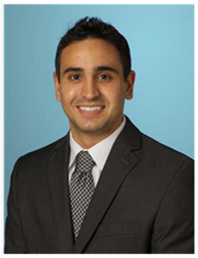


Chris joined Lincoln International in March 2014 as an Analyst. Previously, Chris spent nearly two years at Grant Thornton LLP where he was an Associate in the Valuation Services Group

**Key Contributors**

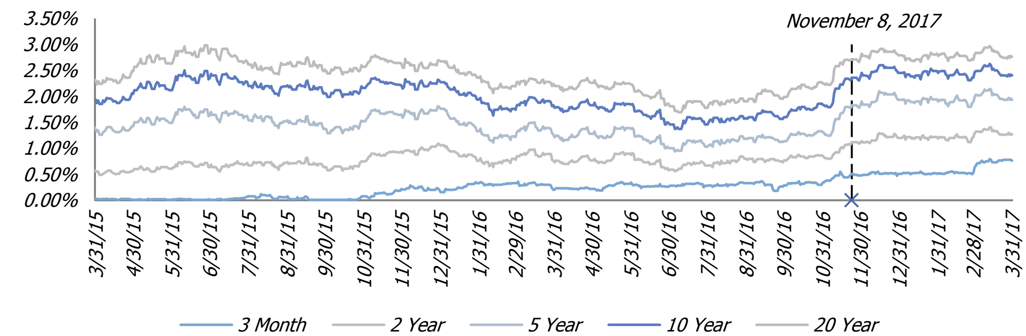
- Natalie Marjancik – MD
- Brian Garfield, CFA – D

# LIBOR Breaks Through 1.0% Floor

## Recent Market Momentum

Following the 2016 U.S. presidential election, the market reacted to the policy agenda that included initiatives ranging from defense spending, corporate tax reform, regulatory relief and infrastructure spending. The result was a sharp increase in public equity prices, inflationary expectations and U.S. Treasury rates.

**U.S. Treasury Rates**

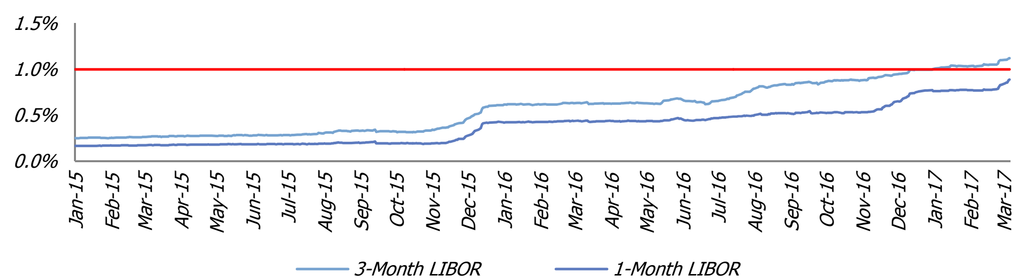



*Source: S&P CapitalIQ*

Shortly after, at the December 14, 2016 Federal Open Market Committee ("FOMC") meeting, the committee increased the federal funds target rate range by 0.25% for the second time in the past decade and the second time in a 12-month span.

The decision of the FOMC in December 2016, coupled with the market's reaction to the presidential election resulted in the 3-month LIBOR breaking through 1.00% in January 2017 for the first time since 2009.

Thereafter, this was further compounded in March 15, 2017 when the FOMC increased the federal funds target rate an incremental 0.25% to 1.00%.




*Source: S&P CapitalIQ*

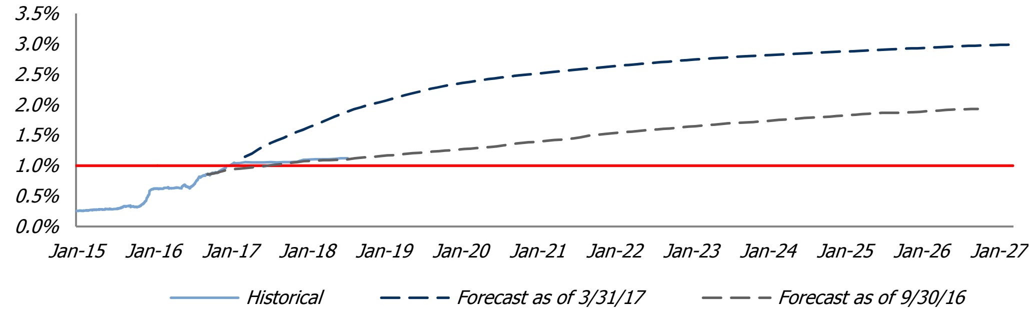
## Forward LIBOR Curve

According to the Federal Reserve Bank's press release following the March 2017 meeting, economic activity continues to expand at a moderate pace with continued job gains, strong household spending and improved consumer and business economic sentiment. Future adjustments to the target will be determined largely based on realized and expected economic conditions relative to its objectives of maximum employment and 2 percent inflation Based on this commentary, the CME Group, a derivative market place, published the below forecast for the likely target rates for each of the upcoming FOMC meetings.

| Meeting Date | 75 - 100 bps | 100 - 125 bps | 125 - 150 bps | 150 - 175 bps | 175 - 200 bps | 200 - 225 bps |
|---|---|---|---|---|---|---|
| 5/3/2017 | 93.6% | 6.4% | 0.0% | 0.0% | 0.0% | 0.0% |
| 6/14/2017 | 41.8% | 54.7% | 3.6% | 0.0% | 0.0% | 0.0% |
| 7/26/2017 | 34.5% | 52.4% | 12.4% | 0.6% | 0.0% | 0.0% |
| 9/20/2017 | 19.4% | 44.6% | 29.9% | 5.8% | 0.3% | 0.0% |
| 11/1/2017 | 17.9% | 42.6% | 31.1% | 7.7% | 0.7% | 0.0% |
| 12/13/2017 | 9.6% | 31.1% | 36.4% | 18.6% | 4.0% | 0.3% |
| 1/31/2018 | 8.6% | 28.9% | 35.9% | 20.4% | 5.5% | 0.7% |

*Source: CME Group*

Between December 31, 2016 and March 31, 2017, LIBOR has increased from 0.999% to 1.150%. As a result of the recent increase in LIBOR and the expectation for an increase in the federal-funds target rate in the future, the forward LIBOR curve has increased.




*Source: Federal Reserve Economic Data*

## LIBOR Curve's Impact on Middle Market Loan Financings

Natalie Marjancik, a Managing Director in Lincoln International's Debt Advisory Group ("Lincoln DAG"), stated, "For the last few years, LIBOR floors have been prevalent for newly issued floating rate securities. The primary purpose of these floors was to help lenders achieve certain yields in periods during which LIBOR was at historically low levels. With LIBOR now above 1.00% and the LIBOR forward curve expected to remain normal (i.e., not inverted), LIBOR floors are no longer needed for this purpose. So far, Lincoln DAG has seen very few lenders increase their proposed LIBOR floors for new financing opportunities. In the handful of cases in which we've seen lenders do this, the floors proposed have been 1.25%, up from the 1.00% regularly proposed by these institutions during the last couple of years. Also, in those situations in which we've seen higher floors proposed, we've not seen these lenders' proposed spreads decrease in a corresponding manner. In a market where there is substantial debt capital ready to be deployed, this puts these groups at a competitive disadvantage. Taking all these dynamics into account, we don't anticipate that LIBOR floor increases will be pervasive for new debt issuances." Ms. Marjancik went on to further describe the impact on companies with current floating rate securities. "As the three-month LIBOR is only slightly above the typical 1.00% threshold, there has not been a major impact on companies with floating rate securities at this point. While the LIBOR curve has steepened compared to last year, borrowers' financial covenants are typically set with meaningful cushions relative to bank case forecasts, which, in most cases, already reflect some conservatism. So, it's unlikely that the increase in LIBOR, alone, will create issues for borrowers or lenders. However, for borrowers already experiencing financial issues arising from their operations or sector-specific conditions, the impact of the increased interest expense of their floating rate securities is likely to be more material."

## Impact on Valuations

The impact from the recent increase in the forward LIBOR curve on valuation of fixed income financial instruments is dependent on whether the underlying security is floating or fixed rate.

Assuming a steady performing business with sufficient free cash flow generation, the increase in the forward LIBOR curve is expected to be value neutral for floating rate securities. The increase in the forward LIBOR curve will result in an increase in the all-in yields or discount rates utilized to value the security which will be offset by the increase in expected future cash flows of the security via the higher LIBOR forward curve. For fixed rate securities, the initial impact on valuation will be negative as yields utilized to value the security will increase while the future cash flows of the security will not receive the benefit of the increase in the forward LIBOR curve.

Another potential impact to valuation will be the ability of the underlying business to take on the incremental interest expense of floating rate securities if LIBOR continues to increase above the 1.00% LIBOR floor. To date, this impact has been minimal as LIBOR has only been slightly above the 1.00% threshold for a short period of time, but by early 2019, LIBOR is expected to break through 2.00%. As Ms. Marjancik noted, financial covenants can be set with large cushions, and lenders consider and even stress test the impact of LIBOR increases when underwriting. As long as the borrower performs in line with underwriting expectations, the increase in LIBOR alone will likely not cause issues for borrowers or lenders. However, for borrower's underperforming underwriting expectations, the increase in interest expense may start to impact cash flow generation more severely and even could lead to liquidity issues. At that point, the fair value of floating rate securities could start to be negatively impacted.

Overall, the immediate impact on valuations of the increased forward LIBOR curve will be negative to fixed rate securities and neutral to floating rate securities. However, it will be important to monitor financial covenant cushions and cash flow generation for underperforming borrowers if LIBOR continues to increase consistent with current expectations.

### About Lincoln's Valuation Database

Lincoln maintains an extensive proprietary database of private company data. The database includes financial data for a diverse group of companies across ten primary industry segments and offers a glimpse into the middle market, where reliable data is otherwise limited. Financial results reflect information available at the end of each calendar quarter (typically, financial statements for one or two months preceding the end of each calendar quarter).

**Key Contributors**

- Tarun Jain – Associate
- Al Waite – Analyst
- Lucas Weiss – Analyst

# Lincoln's Perspectives on the Middle Market

## Lincoln's Q4 Valuations Database

Lincoln's database of middle market companies indicated that on a year-over-year basis, the percentage of companies reporting revenue growth declined, while EBITDA growth grew marginally in Q4 2016 compared to the prior period. Out of ~950 portfolio companies tracked in Q4 2016, 49% of the companies' base revenue declined, while 52% grew Adjusted EBITDA. This compared to growth of 56% and 51%, respectively, in Q3 2016.

In Q4 2016, companies in the energy industry reported a total average quarterly year-over-year revenue decline of -16.8%, a decrease of 10.3% from the prior period. Of the six industries observed, Business Services, Consumer and Healthcare reported positive quarterly year-over-year Adjusted EBITDA growth, and Industrials, Energy, and Technology reported quarterly year-over-year Adjusted EBITDA declines.

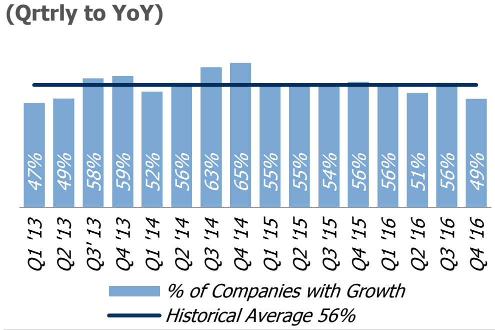
The $0 - $10 million EBITDA category experienced the greatest quarterly year-over-year EBITDA growth rate increase from the prior period of 5.3%; the > $50 million EBITDA category experienced the greatest quarterly year-over-year EBITDA growth rate decrease from the prior period of 2.2%.

Total quarterly year-over-year revenue declined from 2.1% in Q3 2016, to 0.8% in Q4 2016.

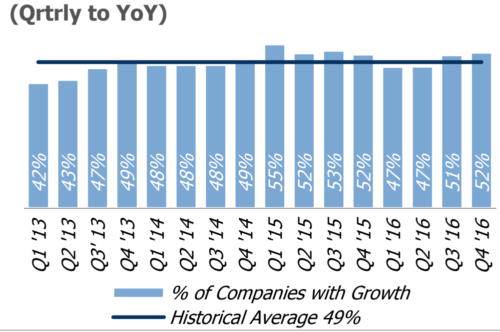
The $30 - $50 million and >$50 million EBITDA categories reported the greatest increase in growth rates from the prior period with 1.6% and 2.8% increases, respectively.

### Revenue & EBITDA Trends

**Revenue Growth % of Companies (Qrtrly to YoY)**




**EBITDA Growth % of Companies (Qrtrly to YoY)**



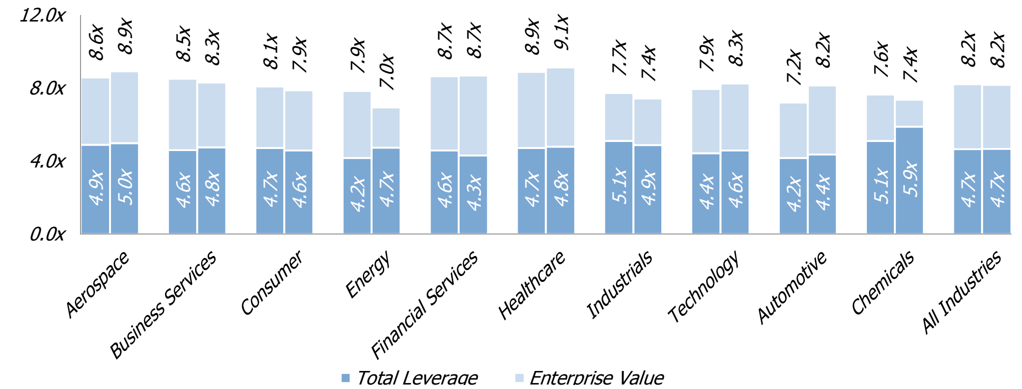
### Lincoln's Estimated Enterprise Value and Leverage Observations

- During the fourth quarter of 2016, observed enterprise value multiples have remained relatively constant from the prior quarter (~8.2x)
- Total leverage also remained relatively constant from the prior quarter, with an average total leverage multiple across all industries of 4.7x as of Q4 2016
- Automotive experienced a ~0.9x increase in average enterprise value multiples and Energy experienced a ~0.9x decrease in average enterprise value multiples

### Lincoln's Sponsor Backed M&A Observations

- Lincoln observed 27 acquisition transactions in Q4 2016
- Q4 2016 average TEV / EBITDA multiple of 8.7x declined by 0.9x compared to the Q3 2016 average multiple of 9.6x. Much of the decline was skewed by higher technology transactions observed in Q3 2016 relative to Q4 2016
- Q4 2016 total and senior leverage multiples of 4.7x and 3.6x, respectively were relatively in line with the 5-year average total and senior leverage of multiples of 4.5x and 3.5x, respectively

## Enterprise Value and Leverage by Industry (Q1 2016 vs Q2 2016)




*Note: Q3 2016 values on Left, Q4 2016 values on Right*
*Source: Lincoln International proprietary database*

## Quarterly M&A Transactions

| | Q4 '14 | Q1 '15 | Q2 '15 | Q3 '15 | Q4' 15 | Q1' 16 | Q2' 16 | Q3' 16 | Q4' 16 |
|---|---|---|---|---|---|---|---|---|---|
| **TEV / EBITDA** | 8.6x | 9.1x | 9.6x | 9.3x | 9.1x | 7.6x | 9.1x | 9.6x | 8.7x |
| **Total Debt / EBITDA** | 4.7x | 4.7x | 4.9x | 4.8x | 4.6x | 4.2x | 4.5x | 4.8x | 4.7x |
| **Senior Debt / EBITDA** | 3.7x | 3.4x | 3.5x | 4.2x | 3.7x | 3.4x | 3.5x | 3.8x | 3.6x |
| **Equity % of Total Cap** | 42% | 46% | 46% | 48% | 45% | 44% | 50% | 50% | 42% |
| **LTM EBITDA (Median)** | $20 | $14 | $25 | $29 | $26 | $26 | $33 | $38 | $48 |
| **Count** | 48 | 16 | 50 | 27 | 32 | 17 | 30 | 37 | 27 |

## Lincoln's Leverage and Junior Financing Observations

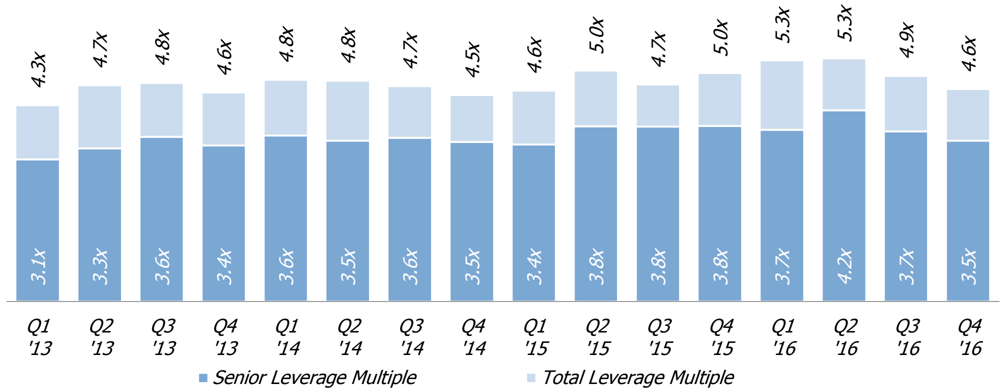
- Summarized on the right are the average leverage and junior financing statistics for recent transactions, including leveraged acquisitions, add-on acquisitions, refinancings, and dividend recapitalizations
- Total and senior leverage have declined in two consecutive quarters, from 5.3x / 4.2x in Q2 2016 to 4.6x / 3.5x in Q4 2016. Full year 2016 average total and senior leverage was 5.0x and 3.8x, respectively
- Q4 2016 Junior and Unitranche pricing was 9.2% and 8.9%, respectively, which was the lowest in 2016 and below the 5-year average Junior and Unitranche pricing of 11.1% and 9.3%, respectively

## Lincoln's Distressed Valuation Observations

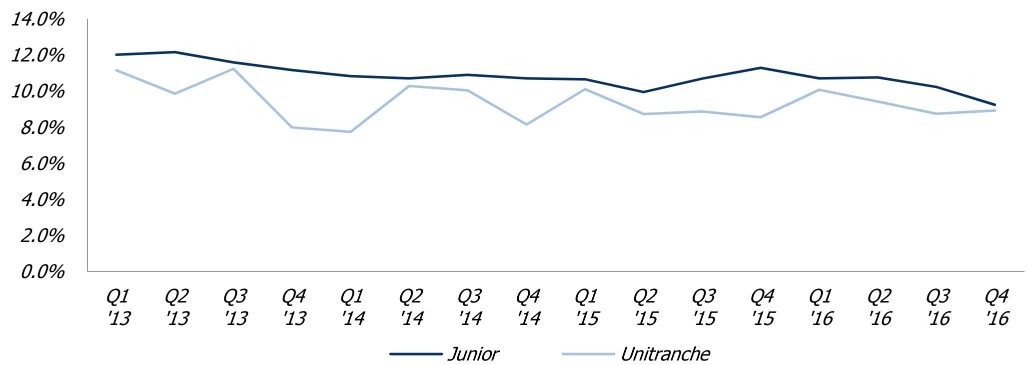
- Summarized on the right are the proportions of loans observed with values below 95%, 80% and 50% of par. The universe consists of mostly illiquid middle market loans valued by Lincoln and includes primarily first liens, unitranche, second liens, and mezzanine loans
- The proportion of loans valued below 95.0% of par peaked in Q1 2016 but remains above historical averages. These loans account for approximately 18.9% of the total dataset
- Energy companies' account for 25.3% of the issuances valued less than 80.0%, a lower percentage than the prior quarter, as energy markets improved in Q4 2016

## Leverage and Junior Financing

**Senior Leverage & Total Leverage Levels**

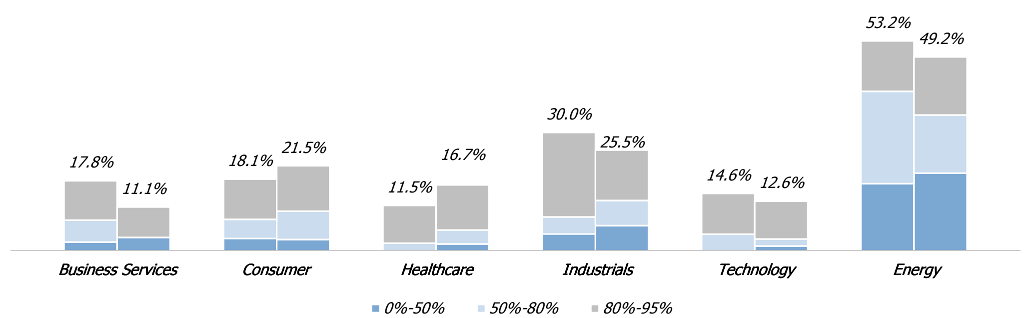



**Total Junior Pricing**



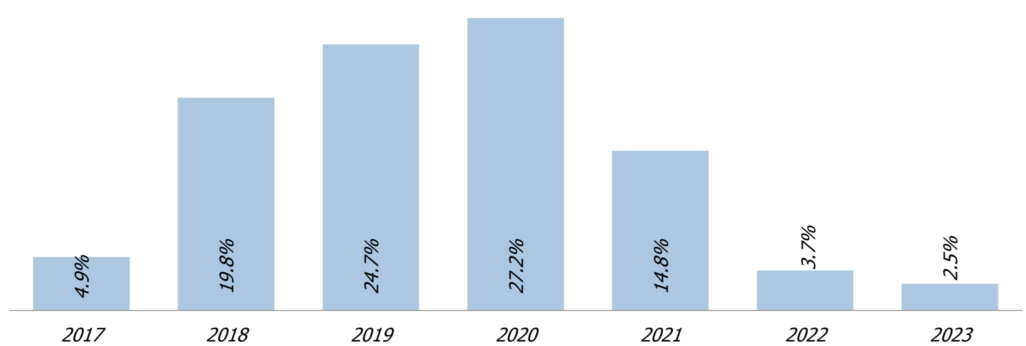

## Distressed Trends

**Loan Pricing Relative to Par**




*Note: Q3 2016 values on Left, Q4 2016 values on Right*

**Distressed Issuances Maturities**




*Note: Pricing is represented on a per issuance basis and all issuances have been weighted equally.*

## About Lincoln's Regulatory Section

Lincoln monitors key regulatory action changes which have a direct impact on the alternative asset industry. This section offers a glimpse into the views and findings of key regulatory agencies, financial accounting standard boards, and related industry groups.

**Key Contributors**

- Patrick Waite – Analyst

# Regulatory Update

## SEC Announces 2017 Examination Priorities

In January 2017, the Securities and Exchange Commission ("SEC") announced its Office of Compliance Inspections and Examinations' ("OCIE") 2017 priorities. Two of the three priorities are consistent with the thematic areas as those identified in the 2016 OCIE priorities; protecting retail investors and assessing market-wide risks. The OCIE is expanding its focus on senior investors and retirement investments in 2017 while reducing its emphasis on data and analytics.

## 2017 FINRA Regulatory & Examination Priorities

In January 2017, the Financial Regulatory Authority ("FINRA") released its 2017 Regulatory and Examination Priorities. The focus of which addressed five broad issues: (1) high-risk and recidivist brokers, (2) sales practices, (3) financial risks, (4) operating risks, and (5) market integrity. In his cover letter, newly appointed FINRA President and CEO, Robert Cook stated, "a common thread in this year's priorities is a focus on core blocking and tackling issues of compliance, supervision and risk management." Many of the topics contained in the priorities letter are consistent with the prior year, with enhanced focuses on areas such as liquidity, cybersecurity, and market manipulation. A major priority in 2016 which is noticeably absent from the 2017 priorities is FINRA's formalized assessment of "firm culture".

Since Mr. Cook joined FINRA in August 2016, he has been meeting with member firms, regulators, and investor groups as part of a "listening tour" to gain feedback and identify opportunities to improve the organization's activities. The president stated in his cover letter as a takeaway from the "listening tour" that, starting this year, FINRA will be publishing a report that outlines key findings from examinations in selected areas. Additionally, small firms would like FINRA to provide more compliance tools and resources to assist their compliance efforts. FINRA is in the process of developing new resources along these lines.

## Protecting Retail Investors

**Protecting Retail Investors:** The OCIE will continue several 2016 initiatives related to exchange traded funds, fee programs, and multi-branch offices. The new areas of focus include broker-dealers offering advice through electronic mechanisms, or "robo-advisors", recidivist representatives, and never-before examined investment advisers.

**Market-Wide Risks:** In order to facilitate the SEC's mission to maintain fair, orderly, and efficient markets, the SEC will examine structural risks and trends that may involve multiple firms or entire industries. The 2017 initiatives focus on cybersecurity, FINRA, money market funds, clearing agencies, payment for order flow, and Regulation SCI.

**Senior Investors and Retirement Investments:** In 2017, the OCIE is devoting increased attention to issues affecting senior investors and those investing for retirement. As part of the increased attention, the OCIE is continuing its ReTIRE initiative from 2016. This year, the examinations will focus on registrants' recommendations and sales of variable insurance products and management of target date funds. Additionally, the OCIE will focus on public pension advisers and services offered to senior investors.

# Middle Market Private Equity Snapshot

## Middle Market Snapshot

### Key Contributors

- Mac Fillet – Analyst

### Deal Flow

- In 2016, U.S. Middle Market private equity M&A activity experienced the lowest aggregate deal value and deal volume since 2013.

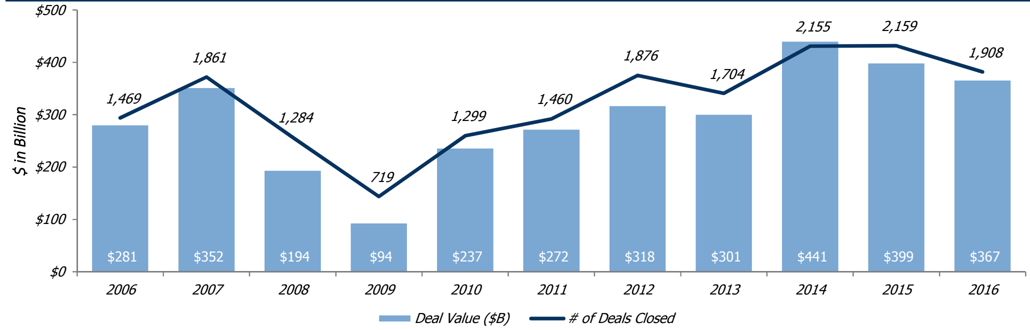
### Deals by Sector

- The Core Middle Market represented the most deals closed relative to the Upper Middle market (deals >$500 million) and Lower Middle Market (deals <$100 million) and the largest aggregate deal value of the three segments, with 879 transactions totaling $172.8 billion in Q4 2016
- The IT sector continued its trend of the most active sector for Upper Middle Market. Combined, the business to business and business to consumer sectors represented more than 50% of deal activity for both the core and Lower Middle Markets

### Leveraged Buyouts

- According to S&P LCD data, LBO purchase price multiples averaged ~0.5x less in 2016 than 2015, but still averaged above all other years since 2006
- The 2016 average equity cushion of ~43% approximated the ten year average of ~41.1%. The average equity cushion for 2016 decreased ~2.0% compared to 2015

### Middle Market Deal Flow by Year




*Source: Pitchbook*
*Note: All data for historical years represents annual results. 2016 year data is through December 31, 2016.*

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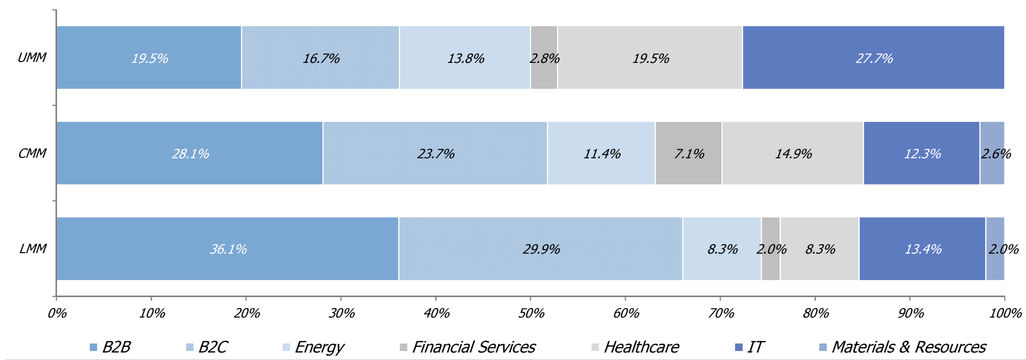
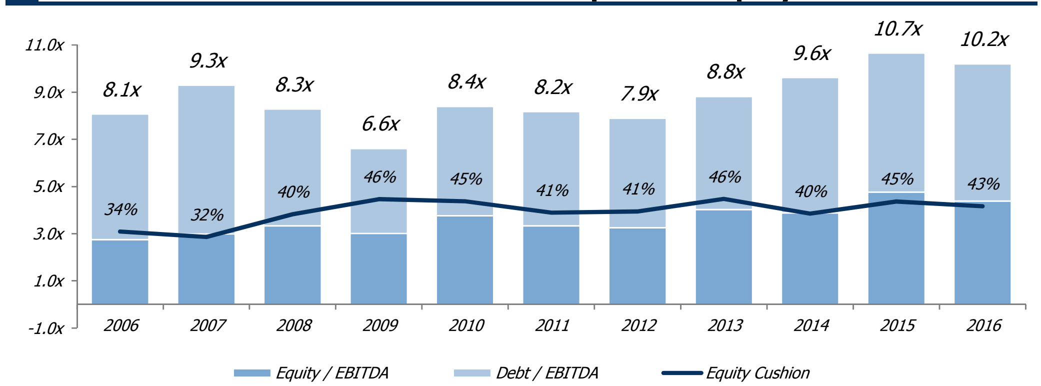
*1. Includes (1) limitation on the owner's ability to liquidate an interest (2) limitation on liquidation proceeds to an amount that is less than a minimum value (3) deferment of payment of liquidation proceeds for more than six months (4) provision that permits repayment in anything other than cash or property (e.g. a promissory note)*

### 2016 Q4 Middle Market Deals by Sector




*Source: Pitchbook*
*Note: Data for deals in the Upper Middle Market ("UMM") (EV of $500 million to $1 billion), Core Middle Market ("CMM")(EV of $100 million to $500 million), and Lower Middle Market ("LMM") (EV of $25 million $100 million)*

### Middle Market LBO Purchase Price Multiples and Equity Contribution

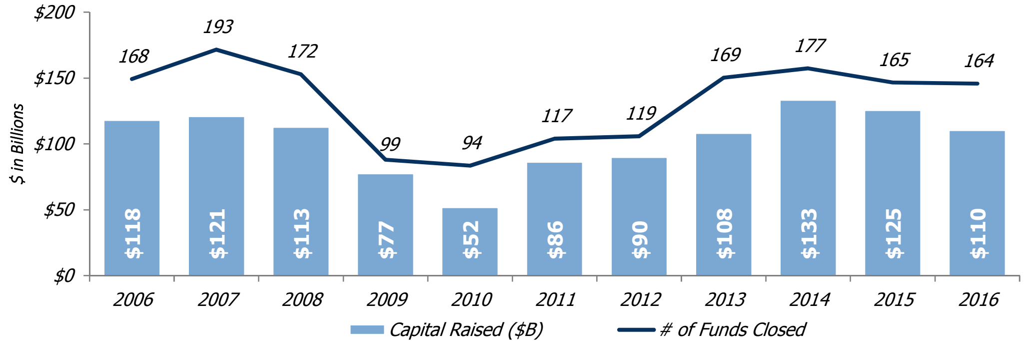



*Source: S&P LCD*
*Note: All data for historical years represents annual results. 2016 year data is through December 31, 2016.*

## Private Equity

- 2016 finished with 164 total funds closed, in line with 2015 and in line with the expectation noted in Q3 2016
- Total capital raised declined 12% compared to 2015, a greater year over year decrease than the September YTD period, signaling a comparatively weak Q4 2016

### Middle Market Private Equity Fundraising

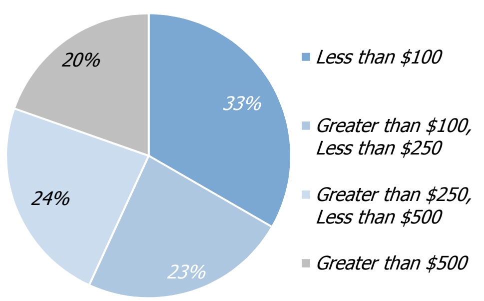



*Source: Pitchbook*
*Note: All data for historical years represents annual results. 2016 year data is through December 31, 2016.*

## Select Middle Market Transactions

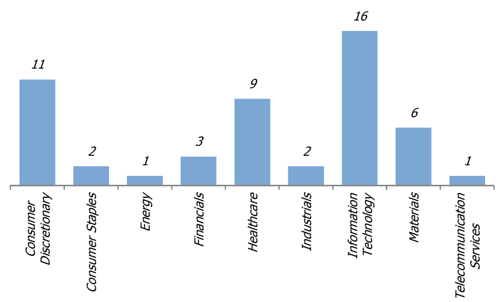
- According to Capital IQ, 51 sponsor-involved middle market transactions have closed in Q1 2017 through mid-March 2017
- Similar to the prior quarter, the "Less than $100 million" bucket represented one third of the identified middle market transactions in the quarter, while the other three buckets split the balance almost evenly
- Similar to Pitchbook's data presented above and the Q4 2016 Capital IQ data, IT remains a favorite industry of middle market PE with 16 closed transactions in Q1 through mid-March. Consumer Discretionary and Healthcare were the second and third most active industry with 11 and 9 transactions, respectively

### Middle Market Transactions by Implied Enterprise Value




*Source: Capital IQ*

### Number of Middle Market Transactions by Industry



## Select Q1 2017 Middle Market Transactions Involving Sponsors to Date

| Date | Target | Industry | Transaction Size | Sponsor Role |
|---|---|---|---|---|
| 3/24/2017 | SummitReheis, Inc. | Materials | $360.0 | Seller |
| 3/22/2017 | Invincea, Inc. | Information Technology | 120.0 | Buyer |
| 3/21/2017 | Ready Pac Produce, Inc. | Consumer Staples | 409.0 | Seller |
| 3/20/2017 | Arctic Sand Technologies, Inc. | Information Technology | 68.0 | Seller |
| 3/15/2017 | HealthHelp Inc | Healthcare | 95.0 | Seller |
| 3/14/2017 | Packaging Holdings, Inc. | Materials | 230.0 | Seller |
| 3/10/2017 | Lightlife Foods, Inc. | Consumer Staples | 140.0 | Seller |
| 3/8/2017 | JP Energy Partners LP | Energy | 477.1 | Seller |
| 3/8/2017 | Pacific Island Restaurants, Inc. | Consumer Discretionary | 105.0 | Seller |
| 3/7/2017 | Alarm Funding Associates, LLC | Financials | 200.0 | Both |
| 3/3/2017 | 3i Debt Management Investments Limited | Financials | 270.0 | Both |
| 3/3/2017 | Permian Basin Sand Company LLC | Materials | 275.5 | Seller |
| 3/2/2017 | Grindmaster-Cecilware Corporation | Industrials | 108.0 | Seller |
| 3/1/2017 | Cypress Foundry Solutions (nka:SkyWater Technology Foundry) | Information Technology | 30.0 | Buyer |
| 2/28/2017 | CoLucid Pharmaceuticals, Inc. | Healthcare | 960.8 | Seller |
| 2/28/2017 | SimpliVity Corporation | Information Technology | 650.0 | Seller |
| 2/28/2017 | Lionbridge Technologies, Inc. | Information Technology | 459.1 | Buyer |
| 2/28/2017 | Viv Labs, Inc. | Information Technology | 211.6 | Seller |
| 2/28/2017 | UniRush, LLC | Financials | 160.7 | Seller |
| 2/27/2017 | Avure Technologies, Inc. | Industrials | 57.0 | Seller |
| 2/24/2017 | Kimball Bridge Holdings LLC | Information Technology | 30.0 | Buyer |
| 2/24/2017 | Limited Stores LLC, Certain Related Assets | Consumer Discretionary | 25.8 | Buyer |
| 2/23/2017 | Skip Hop, Inc. | Consumer Discretionary | 150.0 | Seller |
| 2/23/2017 | RainDance Technologies, Inc. | Healthcare | 87.0 | Seller |
| 2/23/2017 | Infoaxe, Inc. | Information Technology | 30.0 | Seller |
| 2/17/2017 | Blue Nile, Inc. | Consumer Discretionary | 496.5 | Buyer |
| 2/16/2017 | Anthelio Healthcare Solutions Inc. | Healthcare | 275.0 | Seller |
| 2/14/2017 | Racing Winning Brands | Consumer Discretionary | 150.0 | Buyer |
| 2/13/2017 | New Moosejaw, LLC | Consumer Discretionary | 51.0 | Seller |
| 2/1/2017 | Apollo Education Group, Inc. | Consumer Discretionary | 1,158.7 | Buyer |
| 2/1/2017 | Fidelity National Information Services Inc, | Information Technology | 850.0 | Buyer |
| 2/1/2017 | Grande Communications Networks LLC | Telecommunication Services | 650.0 | Both |
| 2/1/2017 | Affinity Gaming | Consumer Discretionary | 591.4 | Both |
| 2/1/2017 | Garden Fresh Restaurant Intermediate Holding, LLC | Consumer Discretionary | 97.9 | Both |
| 2/1/2017 | Niara, Inc. | Information Technology | 40.0 | Seller |
| 1/31/2017 | Catheter Connections, Inc. | Healthcare | 38.0 | Seller |
| 1/30/2017 | Constellation Healthcare Technologies, Inc. | Healthcare | 294.9 | Buyer |
| 1/27/2017 | IDV Solutions, LLC | Information Technology | 27.5 | Seller |
| 1/26/2017 | C.B. Fleet Company, Inc. | Healthcare | 825.0 | Buyer |
| 1/24/2017 | Performance Assessment Network, Inc. | Information Technology | 271.0 | Buyer |
| 1/24/2017 | Quarto Pate Mill in New Castle, Indiana, US | Materials | 28.0 | Seller |
| 1/19/2017 | IntraLinks Holdings, Inc. | Information Technology | 902.4 | Buyer |
| 1/19/2017 | Accriva Diagnostics Holdings, Inc. | Healthcare | 356.0 | Buyer |
| 1/17/2017 | Five TV Stations | Consumer Discretionary | 115.0 | Seller |
| 1/17/2017 | Rubicon Genomics, Inc. | Healthcare | 75.0 | Seller |
| 1/13/2017 | Smith Mountain Industries, Inc. | Consumer Discretionary | 100.0 | Seller |
| 1/11/2017 | Operative Media, Inc. | Information Technology | 200.0 | Seller |
| 1/10/2017 | ServiceMax, Inc. | Information Technology | 915.0 | Seller |
| 1/6/2017 | Anvil International, LLC | Materials | 315.0 | Buyer |
| 1/5/2017 | Revitas Inc. | Information Technology | 60.0 | Seller |
| 1/3/2017 | Continental Structural Plastics Inc. | Materials | 825.0 | Seller |

*Source: CapIQ Screening Tool*
*Note: USD in millions*
*Search Criteria: Implied Enterprise Value < $1 billion, Transaction Type: Merger/Acquisition, Geographic Location: United States of America, Transaction Closed Date: 1/1/2017 to 3/26/2017, Investment Firm Type: PE / VE, Showing: All results with > $20 million Implied Enterprise Value excluding acquisitions of Real Estate Assets*

## About Lincoln's Earnings Call Blog

Lincoln actively monitors the earnings releases of the public alternative asset industry. The select quotes found in this section offer a glimpse into the views and findings of companies within the alternative asset industry during the past quarter's reporting period.

**Key Contributors**

- Anthony Pedota – Analyst

# Earnings Call Blog

### 2016 Year End Alternative Asset Industry Earnings Call Blog

**Reflecting on 2016…**

"While some years could be described as years of reaping, at Apollo 2016 was clearly a year of sowing. The funds we managed, together with co-investment partnerships, invested $16 billion in aggregate during the year. More capital in a calendar period than ever before in our history. This result may surprise you, given the prolonged high-valuation environment we have been operating in over the past years. Despite this backdrop, however, across our integrated global platform, we remained committed to our value orientation and continued to embrace complexity in order to identify a variety of attractive investment opportunities at discounted valuations. We're particularly active in private equity, where the funds we manage deployed nearly $10 billion in 2016, well in excess of the $4 billion to $5 billion per year historical average, due to opportunities that arose more recently as well as deal flow that had been in the works for the past several years."
*— Leon D. Black, Founding Partner & CEO, Apollo Global Management*

"2016 was a turbulent year for investors, whether institutions or individual investors, one that no one fully predicted. Global political events like Brexit, the U.S. political -- U.S. presidential election and the Italian referendum has forced many of our clients and also ourselves to rethink our assumptions and our perceptions of the world. Even with some political surprises, the global economy began to show signs of optimism throughout 2016."
*— Laurence Douglas Fink, Chairman & CEO, BlackRock, Inc.*

"We've delivered these good results during what was -- in a really unprecedented period for markets and active managers, in particular. Last year, January 2016 marked the worst start to a year for equities in history, then came the Brexit referendum and its subsequent violent fallout across many asset classes and then, of course, the unexpected U.S. presidential election. The fact that the S&P ended up 9.5% on the year with positive momentum and surging investment confidence, in fact, it's the highest confidence level in 15 years, is really extraordinary. Needless to say, many active managers didn't participate in this 9.5% gain."
*— Stephen Allen Schwarzman, Co-Founder, Chairman & CEO, The Blackstone Group L.P.*

"As we discussed last quarter, the competitive environment in middle-market lending has grown more challenging. And in particular, it grew more challenging over the course of calendar 2016, went from a relatively lender-friendly environment to the beginning of calendar 2016 to a relatively borrower-friendly environment toward the end of 2016."
*— David B. Golub, CEO, President, Interested Director & Investment Committee Member, Golub Capital BDC, Inc.*

**Thoughts as we approach 2017…**

"We are nervous about retail and restaurants frankly these days because we've seen a weak consumer, and in retail in particular we've seen real changes in the way people buy things, i.e., online versus in stores and in malls in particular."
*— Kip deVeer, CEO, Ares Capital Corp.*

"So we're looking to the future now, we're mindful of shifting political environments and the effects that they have on the economy as well as the business we lend to you today. The credit markets are quite active which is one of the strongest market places I've seen. There has been significant cash inflows into the syndicated loan marketplace and private loan funds all of these are focused on the middle market. This may lead to a reduction in interest rates that we can charge borrowers as competition continues to cut rates, we haven't seen much of that yet but I'm sure it will happen if money keeps coming rolling in."
*— David Gladstone, CEO, Gladstone*

"America's PE valuations were high before the election and have become even higher after the election. And so we're working to be creative to find value, I guess, would be the high-level summary, and looking at opportunities where we can leverage our industry expertise, our operational capabilities, to really find something that's more idiosyncratic. And so we're having to be patient to find good opportunities."
*— Scott C. Nuttall, Global Head of Capital & Asset Management, KKR & Co. L.P.*

"Clearly, dry powder for these folks is at or near at all-time high. So our expectation is that deal flow will continue. We did see as the year ended and turning into 2017, more activity than the same time in the prior year… The general sense is that people are getting more positive. I'd say post-election; it feels like people are being more constructive as it looks -- looking forward with respect to GDP,

regulatory environment and tax. In terms of concerns they have which we share, prices are high. So looking at opportunities to buy is challenging in some cases. However, I think the average PE sponsor is still in their minds, finding opportunities that are attractive for them and we are supporting that."
*— Brook Taube, CEO, President, Managing Partner, Chairman, & Investment Committee Member, Medley Capital Corp.*

"All of the positive trends that our market exhibited in 2016 have continued in 2017. Many investors are opportunistic -- optimistic about the economy, and have shown strong desire for enhanced yield. As a result, we have seen consistent fund flows into leverage credit, a gradual tightening of CLO financing spreads. While deal activity was very strong in Q4, it is apt in January and February, which is also seasonally weak period for our market. Fortunately, we have seen significantly more deal opportunities in late February, and expect to be busy in the coming months. While we do see pressure on spreads in our markets, we continue to find investment opportunities that are consistent with our credit standards."
*— John R. Kline, COO & President, New Mountain Finance Corporation*

"The market environment today stands in stark contrast to what it was a year ago, when concerns about China's growth and downturn in the energy sector drove over 10% declines in the equity market and spread expansion in the credit markets. By year-end however, the S&P 500 high-yield and leverage loan indices all achieved double-digit returns as global growth showed signs of stabilization and the outcome of the U.S. Election boosted hopes for pro-growth economic policies. Also during 2016, there were significant fluctuations in the currency market related to Brexit and movements in interest rates, related to the Fed policy and the U.S. growth outlook. Through the market noise, we remain focused on identifying and managing the impact of risk which we could control for, such as sector and borrower selection and certain non-credit risks, including foreign currency, interest rate and reinvestment risks. The later which is mitigated by call protection in the 80% of our investments. As a result of our hedging strategy, we experienced de minimis currency related impact to NAV in 2016. While sentiment in the broader investment community has been generally positive, our outlook for 2017 remains cautious due to a number of risks surrounding fiscal policy and the protectionist rhetoric that exists. One of example of impact of tax reform on various sectors, while Wall Street research indicates the potential border adjustment tax could reduce, but could not eliminate corporate earnings upside as a result of tax reforms, the impact of the border adjustment tax could vary widely by sector with consumer staples and discretionary spending and these sectors likely to be most adversely affected."
*— Joshua Easterly, Director & Chairman of the Board, Co-CEO, Co-CIO, TPG Specialty Lending*

*Source: Bloomberg Earnings Call Transcripts*

**Global Industry Groups**

Aerospace & Defense
Automotive & Truck
Building & Infrastructure
Business Services
Chemicals
Consumer
Distribution
Electronics
Energy & Power
Financial Institutions
Food & Beverage
Healthcare
Industrials
Packaging
Technology & Media

**Global Locations**

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Beijing
Chicago
Dallas
Frankfurt
London
Los Angeles
Madrid
Milan
Moscow
Mumbai
Munich
New York
Paris
São Paulo
Tokyo
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**Advisory Services**

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# About Lincoln International

Lincoln International specializes in merger and acquisition advisory services, debt advisory services, private capital raising and restructuring advice on mid-market transactions. Lincoln International also provides fairness opinions, valuations and joint ventures and partnering services on a wide range of transaction sizes. With eighteen offices in the Americas, Asia and Europe, Lincoln International has strong local knowledge and contacts in key global economies. The firm 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 can be obtained at www.lincolninternational.com.

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