

the aftermarket analyst

A PUBLICATION FOCUSED ON MERGERS, ACQUISITIONS AND CORPORATE FINANCE IN THE AUTOMOTIVE AFTERMARKET INDUSTRY

The China Syndrome II: Is the Tide Starting to Turn?

In April, we outlined the reasons why U.S. manufacturers can't compete with their Asian counterparts. Having the advantage of low business costs (labor, construction, machinery, raw materials, etc.) and needing only a 5 percent gross profit margin to stay viable, Asian manufacturers were holding all the cards.

We pointed out that their American competitors have to earn a 20 percent gross profit margin just to break even with them. But we think the tide may be starting to turn, thanks to a nepotistic shift in thinking on the part of the Chinese government that is starting to put the brakes on foreign investment. To understand why this is happening, consider the business environment over the last decade or two:

- First, we let the Chinese start making our products for us. Drastically lower costs made this logical.
- Then, we started buying facilities in China. U.S. manufacturers built factories there with our money and resources.
- Now, the Chinese government is reacting to protect its own by establishing policies designed to restrict foreign investment.

A front-page article in The Wall Street Journal on August 30 reported the shift as a strategy for keeping

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Time at Hand for Important Symposium

AAIA will host the 2nd annual **Aftermarket Financial Symposium** at the Hyatt Regency O'Hare in Chicago on Tuesday, Sept. 26 and Wednesday, Sept. 27. The Symposium will provide top speakers and presenters who will address key financial issues and trends in

- mergers and acquisitions,
- accounting,
- fringe benefits,
- technology,
- risk management,
- investments,
- strategic planning,
- research and
- bank financing.

In light of the many global economic factors affecting aftermarket manufacturers, distributors and retailers, all industry stakeholders are encouraged to attend this timely and important event. Capstone is offering readers of The Aftermarket Analyst a \$200 registration discount. For details, please see www.capfg.com.

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RECENTLY ANNOUNCED AUTOMOTIVE AFTERMARKET TRANSACTIONS

| Announce Date | Acquirer/Investor(s) | Target | Target Description | Firm Value (\$mil.) | FV / Rev. | FV / EBITDA |
|---------------|--|--|---|---------------------|----------------|---------------|
| 9/1/2006 | Asahi-Tec | Metaldyne | A leading designer and producer of engine, driveline, and chassis products | \$1,200.0 | — | — |
| 8/31/2006 | Champion Parts | Tomco | Supplier of remanufactured carburetors | 11.0 | — | — |
| 8/29/2006 | Wrenthead, Inc. | Icarz, Inc. | Provider of web-based point of sale and warehouse solutions for the auto aftermarket | — | — | — |
| 8/28/2006 | Graham Capital Partners | Transaxle, LLC | Remanufacturer of transmissions, differentials, and hydraulic pumps for medium and heavy duty trucks | — | — | — |
| 8/23/2006 | BLP Products | Roan Manufacturing | Designs and manufactures racing products | — | — | — |
| 8/23/2006 | PROformance Technologies | Aftermarket Technology Corp.'s PROformance Powertrain Products | Remanufacturer of engines | — | — | — |
| 8/18/2006 | Proquest Business Solutions | Dealer Computer Services Inc.'s CPD business | Electronic Parts Catalog | — | — | — |
| 8/18/2006 | Baxter Auto Parts | Davis Auto Parts | Salem, Oregon based auto parts retailer | — | — | — |
| 8/18/2006 | Schumacher Electric Corp. | Midtronics, Inc.'s professional battery charger product line | Develop and market innovative technologies for battery management | — | — | — |
| 8/9/2006 | Crane Co. | Noble Composites | Manufacturer of premium, high glass finished composite panels used by auto industry | 72.0 | 45.0 1.60x | — |
| 8/8/2006 | Allied Capital Corp. | Penn Detroit Diesel Allison Inc. | Provides over-the-counter parts, original equipment sales and maintenance repair and overhaul services | 59.1 | — | — |
| 8/3/2006 | Mikronite Technologies | Crane Technologies Group | Manufactures camshafts, engines, and ignition systems | — | — | — |
| 8/3/2006 | GKN plc | Stellax Aerostructures Inc. | Manufacturer of complex, metal structural components | — | — | — |
| 8/3/2006 | GKN plc | Rockford Powertrain Inc. | Manufacturer of high-speed driveshafts | 50.0 | 60.0 0.83x | — |
| 8/2/2006 | Uni-Select Inc. | local auto parts distributor businesses | 5 U.S. and 1 Canadian auto parts distributors | — | — | — |
| 8/1/2006 | Titan Tire Corp. | Off the Road (OTR) facility of Continental Tire | Manufacturer of off road tires | 53.0 | 125.0 0.42x | — |
| 7/27/2006 | Dubin Clark & Co. | Featherlite Inc. | Aluminum trailer and container maker | 108.6 | 227.1 0.48x | 11.9 9.12x |
| 7/26/2006 | General Parts Inc. | Worldwide Auto Parts | Supplier of new and remanufactured parts for vehicles | — | — | — |
| 7/25/2006 | Transition Capital Partners | Continental Commercial Products' manufacturing division | Manufactures aluminum and steel powder coated work-boxes that are used in pick-up trucks and on job sites, as well as liquid-storage tanks used primarily by industry and agriculture | — | — | — |
| 7/25/2006 | AVM Industries LLC | ArvinMeritor's light-weight vehicle division | Producer of gas springs and vacuum actuators | — | — | — |
| 7/25/2006 | Transition Capital Partners | Continental Commercial Products' manufacturing division | Manufactures aluminum and steel powder coated work-boxes that are used in pick-up trucks and on job sites, as well as liquid-storage tanks used primarily by industry and agriculture | — | — | — |
| 7/23/2006 | UAP Inc. (subsidiary of Genuine Parts Co.) | Pieces d'autos Paul Lavigne Inc | Operates 3 east-Montreal stores of automotive aftermarket parts | — | 11.0 | — |

(Continued from page 1)

China's growth "sustainable, more domestically focused and less wasteful of resources" – a change of direction from its former emphasis on fast, export-led growth.

Let's take a look at what might be driving the Chinese government's change of heart:

- Twenty years ago, the goods were predominantly low tech and required only low tech workers.
- Today's products are more high tech. They require more and more higher skilled workers, straining China's labor supply.
- So manufacturers are turning to places like Indonesia, where labor costs are even lower, and India, which has a higher proportion of trained, educated labor.

Simply put, China is at risk of being outsourced. To prevent a mass exodus or backlash against business, the government is increasingly using provisions that allow it to intervene in business transactions by curbing the acquisitions of Chinese companies by foreign firms. Using the Toyota approach, it is limiting output so demand will stay high.

This is good news for the U.S. and potentially quite beneficial for aftermarket manufacturers who can hang in there. With China's government diminishing the amount of capital U.S. companies can put into Chinese companies, some of the manufacturing base that has been lost to China could come back to this country. As aftermarket products made in China become more high tech and labor rates keep going up, even China doesn't have the labor pool to produce those products.

As the tide shifts – and we think this marks the beginning of the shift – U.S. companies could salvage their manufacturing base and even become newly attractive to foreign investment. Things may be coming full circle for aftermarket manufacturers, with opportunities to save money and grow their business looming just over the horizon.

About Capstone

Capstone Financial Group is an investment banking firm which assists owners of middle market companies with their financial needs - including mergers and acquisitions, recapitalizations, private placements, divestitures, and other financial advisory services. Capstone is backed by a highly experienced and knowledgeable team of financial professionals with firsthand knowledge of starting, operating, growing, and selling middle market companies. Visit us online at www.capfg.com.

Selected Public Company Capitalization and Operating Figures
(\$ in millions, except per share data)

| Company | Price as of 8/31/06 | Enterprise Value | | | | Last Twelve Months (LTM) | | | Net Income |
|---------------------------------------|---------------------|------------------|-----------|---------|----------------------|--------------------------|------------|-----------|------------|
| | | Market Cap | Debt | Cash | Enterprise Value (1) | LTM Date | Revenue | EBITDA | |
| Manufacturers | | | | | | | | | |
| Tenneco Automotive Inc. | \$22.75 | \$1,039.5 | \$1,369.0 | \$123.0 | \$2,371.5 | 6/30/06 | \$4,514.0 | \$380.0 | \$51.4 |
| Aftermarket Technology Corp. | 20.18 | 446.1 | 49.2 | 5.6 | 499.3 | 6/30/06 | 496.4 | 68.0 | 33.4 |
| Directed Electronics, Inc. | 14.67 | 363.4 | 165.8 | 15.6 | 513.5 | 6/30/06 | 348.8 | 31.6 | 1.8 |
| Standard Motor Products, Inc. | 11.08 | 205.6 | 291.6 | 11.2 | 486.4 | 6/30/06 | 835.8 | 47.6 | 6.9 |
| Dorman Products, Inc. | 10.50 | 185.9 | 34.2 | 4.9 | 221.2 | 6/30/06 | 291.3 | 35.4 | 15.1 |
| Milemarker International Inc. | 2.55 | 25.4 | 5.0 | 0.3 | 30.1 | 6/30/06 | 23.5 | 4.2 | 2.3 |
| Wholesalers & Distributors | | | | | | | | | |
| Genuine Parts Company | \$41.33 | \$7,080.2 | \$500.0 | \$189.1 | \$7,509.1 | 6/30/06 | \$10,180.5 | \$803.5 | \$454.5 |
| LKQ Corporation | 20.77 | 1,103.4 | 107.5 | 4.2 | 1,302.3 | 6/30/06 | 664.7 | 75.9 | 38.6 |
| Keystone Automotive Industries, Inc. | 34.39 | 558.7 | 0.2 | 5.4 | 562.4 | 6/30/06 | 651.2 | 48.1 | 23.6 |
| The Coast Distribution System, Inc. | 9.59 | 42.4 | 26.9 | 0.7 | 71.4 | 6/30/06 | 183.0 | 10.1 | 4.7 |
| Retailers | | | | | | | | | |
| Autozone, Inc. | \$90.30 | \$6,708.8 | \$1,825.1 | \$84.0 | \$8,552.4 | 5/6/06 | \$5,789.9 | \$1,102.9 | \$567.7 |
| Advance Auto Parts, Inc. | 30.12 | 3,166.1 | 468.7 | 13.1 | 3,663.2 | 7/15/06 | 4,484.3 | 541.4 | 237.2 |
| O'Reilly Automotive, Inc. | 29.69 | 3,366.7 | 100.9 | 55.2 | 3,485.6 | 3/31/06 | 2,185.6 | 341.3 | 181.7 |
| The Pep Boys - Manny, Moe & Jack | 12.84 | 696.6 | 581.0 | 51.7 | 1,225.9 | 4/29/06 | 2,227.6 | 74.6 | (34.2) |
| CSK Auto Corporation | 11.47 | 502.5 | 395.1 | 19.3 | 882.3 | 10/30/05 | 1,594.5 | 121.9 | 31.3 |

Selected Public Company Multiples and Operating Statistics

| Company | Enterprise Value / | | | | | P / E Ratio | Margins | | |
|---------------------------------------|--------------------|--------------|--------------|--------------------|--------------|--------------|---------------|----------------|-------------|
| | Revenue | EBIT | EBITDA | Free Cash Flow (2) | Net Income | | Gross Margins | EBITDA Margins | Net Margins |
| Manufacturers | | | | | | | | | |
| Tenneco Automotive Inc. | 0.5x | 11.7x | 6.2x | 11.2x | 46.1x | 20.2 | 15.3% | 8.4% | 1.1% |
| Aftermarket Technology Corp. | 1.0x | 9.2x | 7.3x | 8.7x | 14.9x | 13.3 | 22.3% | 13.7% | 6.7% |
| Directed Electronics, Inc. | 1.5x | 19.9x | 16.3x | 17.3x | NM | NM | 30.3% | 9.1% | 0.5% |
| Standard Motor Products, Inc. | 0.6x | 15.7x | 10.2x | 13.3x | 70.9x | 30.0 | 23.8% | 5.7% | 0.8% |
| Dorman Products, Inc. | 0.8x | 7.6x | 6.3x | 7.8x | 14.7x | 12.3 | 35.2% | 12.1% | 5.2% |
| Milemarker International Inc. | 1.3x | 7.7x | 7.2x | 7.6x | 13.1x | 11.0 | 43.1% | 17.9% | 9.8% |
| Mean | 0.9x | 12.0x | 8.9x | 11.0x | 31.9x | 17.4x | 28.3% | 11.1% | 4.0% |
| Median | 0.9x | 10.5x | 7.3x | 9.9x | 14.9x | 13.3x | 27.0% | 10.6% | 3.2% |
| Wholesalers & Distributors | | | | | | | | | |
| Genuine Parts Company | 0.7x | 10.2x | 9.3x | 10.7x | 16.5x | 15.6 | 31.4% | 7.9% | 4.5% |
| LKQ Corporation | 2.0x | 19.8x | 17.2x | 32.9x | 33.7x | 28.6 | 46.2% | 11.4% | 5.8% |
| Keystone Automotive Industries, Inc. | 0.9x | 14.6x | 11.7x | 15.5x | 23.8x | 23.6 | 44.8% | 7.4% | 3.6% |
| The Coast Distribution System, Inc. | 0.4x | 7.6x | 7.0x | 8.0x | 15.0x | 8.9 | 19.4% | 5.5% | 2.6% |
| Mean | 1.0x | 13.1x | 11.3x | 16.8x | 22.3x | 19.2x | 35.5% | 8.1% | 4.1% |
| Median | 0.8x | 12.4x | 10.5x | 13.1x | 20.2x | 19.6x | 38.1% | 7.6% | 4.0% |
| Retailers | | | | | | | | | |
| Autozone, Inc. | 1.5x | 8.8x | 7.8x | 10.4x | 15.1x | 11.8 | 48.8% | 19.0% | 9.8% |
| Advance Auto Parts, Inc. | 0.8x | 8.9x | 6.8x | 11.7x | 15.4x | 13.3 | 47.4% | 12.1% | 5.3% |
| O'Reilly Automotive, Inc. | 1.6x | 12.7x | 10.2x | 29.2x | 19.2x | 18.5 | 44.0% | 15.6% | 8.3% |
| The Pep Boys - Manny, Moe & Jack | 0.6x | NM | 16.4x | NM | NM | NM | 22.9% | 3.3% | NM |
| CSK Auto Corporation | 0.6x | 10.3x | 7.2x | 9.8x | 28.2x | 16.1 | 45.4% | 7.6% | 2.0% |
| Mean | 1.0x | 10.2x | 9.7x | 15.3x | 19.5x | 14.9x | 41.7% | 11.5% | 6.3% |
| Median | 0.8x | 9.6x | 7.8x | 11.0x | 17.3x | 14.7x | 45.4% | 12.1% | 6.8% |

(1) Enterprise Value equals market cap, plus debt, minus cash

(2) Free Cash Flow equals EBITDA less capital expenditure

"NM" is not meaningful