

# the aftermarket analyst

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

## Market Update: M&A in the Automotive Aftermarket

One of the most common questions we are asked is, “What’s the M&A market like these days?” This is especially true when the economy appears to be headed for a slowdown. While the simple answer is “excellent”, it’s important to understand the “macro” level growth drivers affecting the M&A market as well as the “micro” level growth drivers that move the automotive aftermarket.

The M&A market is comprised of financial and strategic buyers, each of which has their own unique drivers and formulas for successful investing. Strategic buyers have a presence in the industry and look for acquisitions which will yield synergistic benefits. Financial buyers (private equity groups) rely on their own operational expertise, or that of their management partners, to add value to the organization with the stated goal of reselling the business at some point in the future for a profit. Strategic and financial buyers do have one thing in common: unprecedented levels of capital to pursue mergers and acquisitions.

Private equity groups have benefited from their past accomplishments, both in the attraction of new investors looking for these heightened returns and re-investment by satisfied limited partners from prior funds. What surprises many newcomers to private equity is the people and organizations that participate in these funds. Conventional wisdom is that only wealthy individuals participate in private equity funds. In reality, over 50% of private equity dollars are from pension funds. For example, California Public Employees' Retirement System (CalPERS) has \$15.0 billion invested in private equity. Only 7% of private equity funds

come from individual investors.

Record capital inflows and low interest rates have lead to a blistering M&A market for financial buyers. According to Factset/Mergerstat, through April 30, 2007, private equity has accounted for \$127.0 billion in transactions, a 209% increase over last year’s \$41.0 billion for the same period. Through April 30, 2007, financial buyers represented 19% of all M&A transactions by dollar volume, up from 9% during the same period last year.

Strategic buyers have not been sitting idly by; through April 30, 2007 they have participated in \$558 billion in transactions, a 35% increase over the \$408 billion in transactions during the same period in 2006. Strategic buyers have been buoyed by strong corporate earnings evidenced by the record-breaking equity indices in April 2007. Strategic buyers also benefit from low interest rates which allow them access to “cheap” capital in the form of debt.

M&A in the automotive aftermarket has behaved in the same way as the broader M&A market. As we discussed in last month’s *Aftermarket Analyst*, M&A transactions continued at a frenzied pace during the first quarter of 2007. This pace is also attributable to “cheap” debt and excess cash.

We have established that these buyers are very eager to invest their capital. Now we must address the question, “What makes the auto aftermarket so attractive to a

*Continued on Page 3*

## in this issue

Recently Announced Transactions.....	2
Public Company Valuations.....	4

## RECENTLY ANNOUNCED AUTOMOTIVE AFTERMARKET TRANSACTIONS

Announce Date	Acquirer/Investor	Target	Target Description	Firm Value (\$mil.)	Rev. FV / Rev.	EBITDA FV / EBITDA
5/9/2007	Moog, Inc.	Thermal Control Products Inc.	Thermal Control Products, a Camarillo, CA company, specializes in the design, prototype and manufacture of electronic cooling and air moving systems for the automotive, telecommunications, medical, server and electronic storage markets.	\$ 7.5	1.5x	—
5/1/2007	Thule	Case Logic	Storage solutions and lifestyle accessories in both the U.S. and Europe	—	\$ 140.0	—
5/1/2007	Transtar Industries	Axiom Automotive	Major supplier of original equipment (OE) and aftermarket transmission replacement parts	—	—	—
4/30/2007	IMCO	Tubex Manufacturing	Maker of pre-bent exhaust pipes.	—	—	—
4/24/2007	THK Company, Ltd	Rhythm Corp.	Rhythm Corp. designs and manufactures automotive parts	106.0	.40x	—
4/20/2007	Collins & Aikman Corp - Soft Trim Business Unit	International Automotive Components Group North America Inc	Manufacturer of Automobile Flooring	134.0	.22x	—
4/19/2007	Industrial Enterprises	Hi-Tach Oil	Automotive aftermarket supplier that specializes in the sale of anti-freeze, auto fluids, charcoal fluids, and other additives and chemicals	0.35	—	—
4/9/2007	International Automotive Components Group	Lear Corp.'s North American Interiors Systems Division	European Interiors Systems Division	—	—	—
4/6/2007	Autobacs Seven	Strauss Discount Auto	Retail auto-parts and service center business with 91 locations in New York, New Jersey, and Pennsylvania.	55.0	—	—
4/5/2007	American Industrial Partners	Quality Measurement	The Company is the leading global provider of precision measurement equipment and aftermarket support to the tire and automotive industries in both developed and emerging markets.	—	—	—
4/4/2007	Keystone Automotive Industries	Auto Panels Plus	Privately held aftermarket parts business	—	5.0	—
4/3/2007	Neapco	Automotive Components Holdings	Produces driveshafts, halfshafts, and other driveline products and catalytic converters. Formerly owned by Visteon.	—	—	—
3/29/2007	Uni-Select	Thompson & Co.	Operates a distribution center in Union, NJ, as well as eight branch locations and one store in New Jersey and Pennsylvania.	—	—	—
3/28/2007	Kinderhook Industries	Koneta, Inc.	Pickup truck bed mat and truck/trailer splashguard manufacturing operation owned by Lancaster Colony.	—	—	—

*Continued from Page 1*

potential buyer?" The four main growth drivers in the auto aftermarket are:

- increases in the size of the country's automotive fleet;
- increases in the age of the country's automotive fleet;
- increases in the number of miles driven annually per vehicle; and
- the higher cost and increased technology of new cars.

The number of vehicles on the road in the U.S. has increased significantly in recent years, so there are now more vehicles than ever in need of aftermarket products. Between 1996 and 2005, U.S. motor vehicle registrations increased more than 21.3% to 232 million total units. The aging of vehicles currently in use has also been a significant factor contributing to the growth in demand for aftermarket products. For example, as the average age of autos in use increases, owners are more likely to purchase aftermarket products to enhance or repair their aging vehicles.

The aftermarket is growing because the vehicle population is getting older, with approximately 39% of cars more than 10 years old. The average vehicle age has grown significantly over the last few years, with the average age for passenger cars reaching 10 years. Between 1996 and 2005, the average age of all passenger cars on the road increased from 8.6 to 10.0 years. The average age of light trucks increased from 8.4 to 8.7 years during the same period. This trend is expected to continue for the

foreseeable future, further accelerating growth in demand for aftermarket parts.

An increase in total miles traveled has an obvious positive influence on the aftermarket in terms of consumable products such as oil and tires. According to the Auto Aftermarket Industry Association (AAIA), total miles traveled has increased from 2.4 trillion miles in 1996 to 2.95 trillion in 2005. This reflects a 25% increase and, more importantly, miles driven per vehicle is trending up, so each of these vehicles will need more service repair parts.

Relative to average family income levels, new vehicles have become more expensive, with the average unit costing about \$22,000. The result is that consumers are increasingly seeking ways to protect or enhance their investment. At the same time, more middle and lower income families opt for well-equipped used cars, rather than stripped-down, smaller new cars. Consequently, demand for aftermarket products has increased dramatically. New vehicle technology has increased the cost of replacement parts and vehicle complexity. As a result, fewer people are desirous or even capable of repairing their own vehicles – opting instead to have them serviced by professional mechanics.

Excess capital and low interest rates are the "fuel" that is powering the current M&A market. While their source of capital differs, strategic and financial buyers appear to be well suited for another strong year of merging or acquiring businesses. This is true not only for the broader US M&A market, but also for the auto aftermarket which remains poised for growth and continues to be an attractive industry for investment.

## 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](http://www.capfg.com).

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

Company	Enterprise Value					Last Twelve Months (LTM)			
	Price as of 4/30/07	Market Cap	Debt	Cash	Enterprise Value (1)	LTM Date	Revenue	EBITDA	Net Income
<b>Manufacturers</b>									
Tenneco Automotive Inc.	\$29.95	\$1,370.8	\$1,378.0	\$202.0	\$2,635.7	12/31/06	\$4,685.0	\$382.0	\$51.0
Aftermarket Technology Corp.	27.63	603.5	17.8	7.8	626.3	12/31/06	498.0	63.8	28.9
Directed Electronics, Inc.	10.00	252.0	342.2	9.9	584.4	12/31/06	437.8	58.4	21.0
Standard Motor Products, Inc.	18.33	342.4	238.3	22.3	562.8	12/31/06	812.0	52.7	10.3
Dorman Products, Inc.	12.33	218.3	29.2	5.1	249.7	12/31/06	295.8	36.5	15.6
Milemarker International Inc.	2.01	20.0	5.4	0.2	25.3	9/30/06	21.9	3.1	1.4
<b>Wholesalers &amp; Distributors</b>									
Genuine Parts Company	\$49.41	\$8,424.0	\$500.0	\$136.0	\$8,936.4	12/31/06	\$10,457.9	\$870.1	\$475.4
LKQ Corporation	22.58	1,203.8	100.1	4.0	1,400.5	12/31/06	789.4	89.3	44.4
Keystone Automotive Industries, Inc.	33.26	543.2	0.2	6.5	541.0	12/29/06	693.7	53.9	26.4
The Coast Distribution System, Inc.	7.25	32.0	24.5	0.7	56.7	12/31/07	179.1	7.2	3.0
<b>Retailers</b>									
Autozone, Inc.	\$133.04	\$9,402.8	\$1,854.3	\$86.1	\$11,348.1	2/10/07	\$6,049.9	\$1,187.0	\$584.8
Advance Auto Parts, Inc.	41.20	4,353.5	477.2	11.1	4,906.0	12/31/06	4,616.5	542.8	230.7
O'Reilly Automotive, Inc.	35.60	4,057.8	110.5	29.9	4,236.5	12/31/06	2,283.2	347.3	178.1
The Pep Boys - Manny, Moe & Jack	18.65	1,014.5	657.5	21.9	1,655.2	2/3/07	2,272.2	109.2	(11.3)
CSK Auto Corporation	16.62	728.2	395.1	19.3	1,116.2	10/30/05	1,594.5	121.9	31.3
US Auto Parts Network, Inc.	5.80	173.0	32.9	2.4	203.6	12/31/06	120.1	12.3	3.5

**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
<b>Manufacturers</b>									
Tenneco Automotive Inc.	0.6x	13.3x	6.9x	12.9x	51.7x	26.9	14.2%	8.2%	1.1%
Aftermarket Technology Corp.	1.3x	12.6x	9.8x	12.1x	21.7x	20.9	21.0%	12.8%	5.8%
Directed Electronics, Inc.	1.3x	11.3x	10.0x	10.4x	27.8x	12.0	28.0%	13.3%	4.8%
Standard Motor Products, Inc.	0.7x	15.1x	10.7x	13.2x	54.7x	33.3	25.3%	6.5%	1.3%
Dorman Products, Inc.	0.8x	8.4x	6.8x	8.5x	16.0x	14.0	35.0%	12.3%	5.3%
Milemarker International Inc.	1.2x	9.3x	8.3x	9.1x	17.6x	13.9	42.3%	13.9%	6.5%
<b>Mean</b>	<b>1.0x</b>	<b>11.7x</b>	<b>8.8x</b>	<b>11.0x</b>	<b>31.6x</b>	<b>20.2x</b>	<b>27.6%</b>	<b>11.2%</b>	<b>4.1%</b>
<b>Median</b>	<b>1.0x</b>	<b>11.9x</b>	<b>9.1x</b>	<b>11.3x</b>	<b>24.8x</b>	<b>17.5x</b>	<b>26.6%</b>	<b>12.6%</b>	<b>5.0%</b>
<b>Wholesalers &amp; Distributors</b>									
Genuine Parts Company	0.9x	11.2x	10.3x	12.0x	18.8x	17.7	31.3%	8.3%	4.5%
LKQ Corporation	1.8x	18.1x	15.7x	26.4x	31.5x	27.1	45.3%	11.3%	5.6%
Keystone Automotive Industries, Inc.	0.8x	12.5x	10.0x	13.8x	20.5x	20.6	44.7%	7.8%	3.8%
The Coast Distribution System, Inc.	0.3x	8.8x	7.8x	8.6x	19.1x	10.8	18.8%	4.0%	1.7%
<b>Mean</b>	<b>0.9x</b>	<b>12.7x</b>	<b>11.0x</b>	<b>15.2x</b>	<b>22.5x</b>	<b>19.0x</b>	<b>35.0%</b>	<b>7.9%</b>	<b>3.9%</b>
<b>Median</b>	<b>0.8x</b>	<b>11.9x</b>	<b>10.2x</b>	<b>12.9x</b>	<b>19.8x</b>	<b>19.1x</b>	<b>38.0%</b>	<b>8.0%</b>	<b>4.2%</b>
<b>Retailers</b>									
Autozone, Inc.	1.9x	10.9x	9.6x	12.1x	19.4x	16.1	49.4%	19.6%	9.7%
Advance Auto Parts, Inc.	1.1x	12.2x	9.0x	17.3x	21.3x	18.9	47.7%	11.8%	5.0%
O'Reilly Automotive, Inc.	1.9x	15.0x	12.2x	35.8x	23.8x	22.8	44.1%	15.2%	7.8%
The Pep Boys - Manny, Moe & Jack	0.7x	79.9x	15.2x	28.1x	NM	NM	25.2%	4.8%	NM
CSK Auto Corporation	0.7x	13.0x	9.2x	12.4x	35.7x	23.3	45.4%	7.6%	2.0%
US Auto Parts Network, Inc.	1.7x	37.7x	16.6x	19.6x	58.2x	49.5	34.6%	10.2%	2.9%
<b>Mean</b>	<b>1.2x</b>	<b>26.2x</b>	<b>11.9x</b>	<b>21.1x</b>	<b>25.0x</b>	<b>26.1x</b>	<b>41.1%</b>	<b>11.5%</b>	<b>5.5%</b>
<b>Median</b>	<b>1.1x</b>	<b>13.0x</b>	<b>10.9x</b>	<b>17.3x</b>	<b>22.5x</b>	<b>20.8x</b>	<b>45.4%</b>	<b>11.8%</b>	<b>6.4%</b>

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

(2) Free Cash Flow equals EBITDA less capital expenditure

"NM" is not meaningful