

the aftermarket analyst

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

Long Term Memory Gains

The investment community is one that is said to have a short memory. That may be true, but looking at historical economic trends can help more accurately shape the present and the future.

“All things considered, the last year notwithstanding, the aftermarket has historically been one of the more efficient growth models,” says Dan Smith, president of Capstone Financial Group. “I think the 30-year average is something like 6 percent. There are not a lot of industries in this world that can say that. We don’t ordinarily have that kind of steady growth, so we saw a pretty big uptick probably about 10 years ago in terms of the interest in the industry. People back then realized that the aftermarket was stable and growing and even as Detroit went down, the aftermarket went up.”

Despite today’s economic shortcomings, investors who look at the long-term trends will find that the automotive aftermarket is a solid bet with above-average returns.

But what are some of the trends that have shaped the industry we see today? One would be consolidation, as retailers, manufacturers and distributors have followed a similar path as those in parallel industries.

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And more recent merger and acquisition activity has unfortunately centered on what’s referred to as “distressed deals,” where companies sell or merge due to desperation more than growth potential.

Merger and acquisition activity is down from last year, primarily because of the credit markets and diminishment in earnings and revenue in the industry, according to Smith.

Even though consolidation has long been a key trait of aftermarket companies, the number of manufacturers has actually increased, but today’s overall numbers are comparable to those in the past.

“There are probably 50 percent more manufacturers than there were 10 years ago because of the development of new kinds of products, electronics, performance items, more sophisticated exhaust systems and computer chips and on and on,” says Smith from Capstone.

“Five years ago, we probably had about the same amount of companies. We really saw the growth between 1998 and 2005, that’s when we saw the greatest increase in companies. It has grown and now with hard times, of course, a lot of those companies have gone away. So in an ironic set of circumstances we probably have the same amount of companies now as you did in 2000,” he says.

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RECENTLY ANNOUNCED AUTOMOTIVE AFTERMARKET TRANSACTIONS

Announce Date	Acquirer/Investor(s)	Target	Target Description
8/29/2009	Manufacturas Diversas	ROL Manufacturing	assets of ROL's Engine Gasket division in the U.S., Canada, and Mexico
8/20/2009	Motorcar Parts of America	Reliance Automotive Inc.	a privately held remanufacturer of alternators and starters based in East Berlin, Conn
8/18/2009	Genuine Parts Co.	Uni-Select	assets of its Heavy Duty Group, also known as Palmar, that provides replacement parts, tools and accessories for heavy-duty vehicles
8/17/2009	Wynnchurch Capital	Centrum Equities, XV (Visteon)	a holding company that had previously acquired select aftermarket assets of Visteon Corporation in 2008, and substantially all of the North American assets and operations of Proliance International Inc.
8/10/2009	The Carlyle Group/Solus	Metaldyne	designer and supplier of metal-formed components and assemblies for engine, transmission and chassis applications
7/31/2009	Katcon	Delphi	Delphi's catalytic converter and exhaust system global business
7/23/2009	FleetPride	Panhandle Truck Parts	an independent aftermarket distributor of heavy-duty truck and trailer parts serving Amarillo and Lubbock, TX.
7/14/2009	FleetPride	Fleet Supply of Tallahassee Inc.	an independent aftermarket distributor of heavy-duty truck and trailer parts serving Florida and the panhandle
7/9/2009	CoverCraft	Global Accessories, Inc.	purchased most of the assets including the lines Wolf Automotive, Powersports and Marine covers; LeBra front-end covers; DashMat dashboard covers; Premier Floor Mats; and Spidy Gear cargo web products
7/6/2009	Uview	MotorVac Technologies	supplies professional automotive fluid maintenance equipment and service products that are distributed to more than 60 countries
7/3/2009	OpenGate Capital	ArvinMeritor	ArvinMeritor has sold the U.S. portion of its Gabriel ride control products business to OpenGate Capital
7/3/2009	Management buyout	Thule - Valley Towing Systems	the management team of Valley Towing Systems has purchased the Lodi, CA-based company from its former parent, Thule
7/1/2009	Sun Capital	Big 10 Tire Stores Inc.	one of the largest independent tire dealers in the Southeastern U.S.
6/19/2009	Cerion LLC	Contech	serve the global automotive market with highly-engineered lightweight die cast components
6/15/2009	Platinum Equity	Alcoa	divestiture of its wire harness and electrical distribution business
6/15/2009	Monro Muffler Brake	Autotire Car Care Centers	a wholly-owned subsidiary of American Tire Distributors with 26 Autotire locations
6/10/2009	Fiat	Chrysler	transfer of most of Chrysler's assets and some of its liabilities to the Fiat-led group. Unwanted assets, mostly idled plants and surplus properties, will remain in Chapter 11
6/8/2009	New Life Transport Parts Center	Trailmobile Parts	exclusive rights to the distribution of Trailmobile's aftermarket repair parts in North America
5/5/2009	Bienes Turgon	Delphi	assets and shares related to the company's global exhaust business including locations in Blonie, Poland; Clayton, Australia; Port Elizabeth, South Africa; joint venture interests in Monterrey, Mexico; technical centers in Auburn Hills, Mich. USA; and Bascharage, Luxembourg.
5/1/2009	Kelly Capital	Earl Scheib	operator of 85 automotive paint and collision repair shops across the United States and manufactures paint coating systems that are used, not only by its paint and collision repair shops, but also sold to OEMs and used by architectural construction firms

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Gabelli & Company, Inc. has held an automotive aftermarket symposium for the past 32 years in Las Vegas, where the firm thoroughly explores the automotive aftermarket as an investment vehicle.

“Consolidation has been the one constant we’ve seen at our conference for the past decade,” says analyst Brian Sponheimer with Gabelli. “The consolidation of the jobber market has led to the rise of the aftermarket retailers. While still a fragmented market, dominant brands have gained share of wallet and mind over the course of the past decade.”

In recent years, Gabelli & Company has expanded the scope of the conference to include publicly traded automotive retailers, along with original equipment suppliers. This year marks the 33rd year of the conference, which will take place Nov. 2 through 4 at the Bellagio in Las Vegas, in sync with this year’s AAPEX show.

While word from the investment sector is mainly positive these days, the aftermarket has had a historical image problem due to its association with similar segments.

“Investment analysis on Wall Street is typically carried out around long-defined silos, and historically many investors did not know what to do with the automotive aftermarket,” says Jonathan Carey, vice president of BB&T Capital Markets. “They lumped the retailers together with other hard-line retailers like Home Depot

and would look at aftermarket manufacturers with other industrial manufacturers, or worse, Detroit.

“While it has taken time to develop, smart investors have begun to view the automotive aftermarket as we at BB&T view it and as industry participants have long viewed it – as a standalone industry with its own unique set of growth drivers. This view of the entire channel has enabled investors to identify trends earlier and thereby uncover opportunities that others might simply miss,” he says.

The association with Detroit and the Big Three still continues to tarnish the aftermarket’s image in some investors’ eyes.

The OEM and aftermarket are often lumped together as one “automotive industry” from the view of investors, says Jeremy Thompson, managing director for ONCAP, and an investment banker who has stakes in the Mister Car Wash and Caliber Collision Centers chains.

“Therefore, when the automotive sector is out of favor from the perspective of a lender or a credit officer due to some of the troubles of the manufacturer, the aftermarket is often lumped into this sector.”

Another investment setback is the notion that historically, the aftermarket has been slow to change, says Kristin Newhall, partner for the Riverside Company. “I think it’s historically been slow to change,” she says. “It has taken longer for efficiencies in terms of the supply chain, and in going direct to consumers so it can be sort of slow.”

About Capstone

Capstone Financial Group, Inc. 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	Enterprise Value					Last Twelve Months (LTM)			
	Price as of 8/31/09	Market Cap	Debt	Cash	Enterprise Value (1)	LTM Date	Revenue	EBITDA	Net Income
Manufacturers									
Federal-Mogul Corporation	\$12.58	\$1,250.5	\$2,862.2	\$687.3	\$3,482.4	6/30/09	\$5,553.1	\$381.6	(\$239.3)
Aftermarket Technology Corp.	20.92	415.3	70.0	99.0	386.3	6/30/09	497.3	69.3	22.7
Tenneco Automotive, Inc.	15.70	742.3	1,520.0	111.0	2,176.4	6/30/09	4,778.0	231.0	(439.8)
Dorman Products, Inc.	14.06	247.9	10.9	4.5	261.1	6/30/09	354.6	40.3	20.7
Standard Motor Products, Inc.	12.38	236.3	136.0	14.5	357.9	6/30/09	721.5	34.0	5.9
Wholesalers & Distributors									
Genuine Parts Company	\$37.04	\$5,909.0	\$500.0	\$238.6	\$6,170.4	6/30/09	\$10,381.8	\$792.6	\$411.6
LKQ Corporation	17.36	2,433.9	636.6	129.5	3,057.1	6/30/09	1,971.7	236.1	102.4
The Coast Distribution System, Inc.	2.41	10.7	11.5	2.6	19.7	6/30/09	107.9	(2.4)	(2.3)
Retailers									
Autozone, Inc.	\$147.25	\$7,912.3	\$2,405.9	\$94.3	\$10,403.3	5/9/09	\$6,663.6	\$1,332.4	\$656.7
Advance Auto Parts, Inc.	42.30	4,037.5	279.6	126.4	4,215.7	7/18/09	5,386.8	582.5	254.5
O'Reilly Automotive, Inc.	38.28	5,193.0	796.6	41.0	6,095.4	6/30/09	4,641.0	543.7	239.5
The Pep Boys - Manny, Moe & Jack	8.93	467.1	334.0	21.3	779.7	5/2/09	1,926.2	64.5	(25.6)
US Auto Parts Network, Inc.	5.45	162.7	0.0	32.6	130.1	6/30/09	153.8	3.0	(4.0)

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									
Federal-Mogul Corporation	0.6x	77.4x	9.1x	28.8x	NM	NM	14.7%	6.9%	NM
Aftermarket Technology Corp.	0.8x	7.0x	5.6x	6.1x	17.0x	18.3	22.0%	13.9%	4.6%
Tenneco Automotive, Inc.	0.5x	NM	9.4x	36.9x	NM	NM	14.3%	4.8%	NM
Dorman Products, Inc.	0.7x	8.0x	6.5x	7.9x	12.6x	12.0	32.6%	11.4%	5.8%
Standard Motor Products, Inc.	0.5x	18.9x	10.5x	14.4x	60.3x	39.8	23.8%	4.7%	0.8%
Mean	0.6x	27.8x	8.2x	18.8x	30.0x	23.3x	21.5%	8.3%	3.7%
Median	0.6x	13.4x	9.1x	14.4x	17.0x	18.3x	22.0%	6.9%	4.6%
Wholesalers & Distributors									
Genuine Parts Company	0.6x	8.8x	7.8x	8.9x	15.0x	14.4	29.6%	7.6%	4.0%
LKQ Corporation	1.6x	15.3x	12.9x	17.3x	29.8x	23.8	44.1%	12.0%	5.2%
The Coast Distribution System, Inc.	0.2x	NM	NM	NM	NM	NM	17.4%	NM	NM
Mean	0.8x	12.0x	10.4x	13.1x	22.4x	19.1x	30.4%	9.8%	4.6%
Median	0.6x	12.0x	10.4x	13.1x	22.4x	19.1x	29.6%	9.8%	4.6%
Retailers									
Autozone, Inc.	1.6x	9.0x	7.8x	9.6x	15.8x	12.0	50.1%	20.0%	9.9%
Advance Auto Parts, Inc.	0.8x	9.7x	7.2x	10.2x	16.6x	15.9	48.8%	10.8%	4.7%
O'Reilly Automotive, Inc.	1.3x	14.0x	11.2x	63.3x	25.5x	21.7	46.7%	11.7%	5.2%
The Pep Boys - Manny, Moe & Jack	0.4x	NM	12.1x	25.1x	NM	NM	24.2%	3.4%	NM
US Auto Parts Network, Inc.	0.8x	NM	43.1x	NM	NM	NM	35.6%	2.0%	NM
Mean	1.0x	10.9x	16.3x	27.1x	19.3x	16.5x	41.1%	9.6%	6.6%
Median	1.0x	9.7x	11.2x	17.7x	16.6x	15.9x	47.7%	11.3%	5.2%

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

(2) Free Cash Flow equals EBITDA less capital expenditure

"NM" is not meaningful