

the aftermarket analyst

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

Private Equity - Then and Now

We have had several articles this year that discuss the state of Private Equity and its effect on aftermarket M&A. For readers that may not be as familiar with Private Equity, we are re-publishing the article, "Top 10 Reasons to Tap the Private Equity Capital Markets Now". The original article was published in March 2005. Seven years later the words still ring true and serve as a testament to its stability and viability.

Many auto aftermarket companies have been taking advantage of the abundant supply of private equity capital seeking a home in the industry lately. Some of the most compelling reasons business owners and executives are finding to partner with private equity groups include the following:

- 1. Private equity groups outbidding strategic buyers.** Theoretically, strategic or industry buyers should outbid their financial rivals because operating synergies allow them to pay a premium for most businesses. However, we have seen private equity groups willing to accept lower rates of return in order to win competitive auctions against strategic buyers. It seems to be a sign of the times because the private equity field has grown increasingly crowded in recent years.
- 2. Capital for growth and acquisitions.** Most closely-held companies face severe growth constraints because they lack reliable external capital sources and must finance all growth internally. Private equity groups are designed to help such businesses overcome this problem. As a result, private equity groups are usually more than willing to spend big dollars on sales and marketing, product development, management talent, capital expenditure, and acquisitions to unlock a company's full potential.

- 3. Risk reduction.** With most business owners, the vast majority of their net worth is tied up in their own companies. As a result, they face a tremendous amount of personal exposure to the various operating and financial risks associated with their businesses. Recapitalizing with a private equity group allows an owner to realize some liquidity immediately while maintaining ownership in the company going forward. This strategy can be the best of both worlds for owners who believe in their company's' future prospects, but do not want to face all of the risk alone.

- 4. Gain new expertise, talents, and resources.** Private equity groups pride themselves on being more than just deep pockets. In fact, the best ones have strong networks with management and board level talent, relationships with financial institutions, and other influential contacts. Also, many of these firms have significant expertise in international trade financing, accounting and tax issues, sourcing, and risk management. Many companies have benefited handsomely from the resources and expertise these investors provide.

- 5. Succession planning and exit strategy.** With Baby Boomers rapidly approaching retirement age, the next several years will see a large increase in the number of companies dealing with succession issues. Private equity is an ideal way to overcome the challenges of succession. These firms allow an owner to receive fair value for his life's work while not having to worry about "junior" putting the company "in the tank." A wise man once said, "The best time to sell is when you have a buyer." There are many available now.

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RECENTLY ANNOUNCED AUTOMOTIVE AFTERMARKET TRANSACTIONS

| Announce Date | Acquirer/Investor(s) | Target | Target Description |
|---------------|---------------------------------|--|---|
| 12/20/2011 | Harvest Partners, LP | Driven Brands, Inc. | a leading franchisor in the automotive aftermarket services industry with a national franchising platform in the United States and Canada. Driven's flagship service brands include Meineke and Maaco, two highly recognizable brands within the industry, in addition to several other brands. |
| 12/14/2011 | Fras-Le S.A. | Freios Control Ltd. | a manufacturer of auto parts, brake components and automotive polymers |
| 12/9/2011 | Industrial Opportunity Partners | Toledo Molding & Die, Inc. | a full-service automotive supplier that designs, develops and manufactures highly engineered molded thermoplastic components and assemblies such as interior cockpit modules and air and fluid management products |
| 12/9/2011 | Midwest Truck & Auto Parts | Richmond Gear (Regal Beloit) | manufactures ring and pinions, transmissions, and traction control devices for the racing, hi-performance and off-road aftermarkets |
| 12/9/2011 | FleetPride | Greeley Truck Parts | a Greeley, CO based independent heavy-duty parts store in operation since 1995 |
| 12/9/2011 | Bosch | Uni-Point Group | a key producer of starters, alternators, temperature control parts and wiper blades for the aftermarket |
| 12/6/2011 | Valeo | Controlled Power Technologies (Variable Torque Enhancement Systems division) | a range of electric superchargers |
| 12/2/2011 | Terry's Tire Town | Englewood Tire Wholesale | Seven retail centers. |
| 11/30/2011 | Huf Electronics | BERU Electronics GmbH | specialises in the development and production of tire pressure control systems |
| 11/29/2011 | Solutia, Inc. | Southwall Technologies | an innovator of energy-saving films and glass products for the automotive and architectural market |
| 11/18/2011 | Goodson Tools & Supplies | Goodtool Brakes Service Tools | provides brake service companies with replacement parts, cutting tips, silencers and more for brake lathes |
| 11/17/2011 | Magna International | BDW Technologies | an industry leader in vacuum high-pressure aluminum die casting |
| 11/14/2011 | Quest Specialty Coatings | Patriot Paint | one of the industry's unique producers of coatings systems for metal substrates |
| 11/11/2011 | TPG Capital, L.P. | CARDONE Industries | a world leader in the automotive parts remanufacturing industry |
| 11/10/2011 | Harvest Partners, LP | TruckPro, Inc. | one of the largest independent distributors of heavy-duty aftermarket truck parts and accessories in the U.S |

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6. Flexibility in deal structuring. Most business owners reluctant to partner with private equity groups are wary of ceding control of their businesses. Fortunately, private equity groups have become increasingly willing to make investments of every shape and size to accommodate the preferences of all types of business owners. In fact, we have recently seen well-known firms who previously made only control investments publicly advertise their willingness to be minority investors in some deals. We believe the competition for investing in quality businesses has become so fierce that these firms now have no choice but to invest their capital in virtually any way they can.

7. Ability to attract the best possible financing. The importance of financing in deal making cannot be understated since it affects so many aspects of the process including investor returns, management compensation, financial and operating flexibility, purchase price, and certainty of closure. Private equity groups usually obtain more favorable borrowing terms than their strategic counterparts because they tend to put more equity in their deals, have better relationships with lenders, and be better financial engineers overall.

8. Large private equity capital overhang remains. Recent figures from Thomson Venture Economics show a capital overhang (the difference between capital committed to private equity groups and what they have invested) of about \$99 billion for the buyout and mezzanine markets. Also, the overall private equity industry is estimated to have a current \$206 billion overhang. (Note: overhang at close of 2011 is in excess of \$500 billion) Consequently, the supply of private investment capital greatly exceeds demand — making this one of the best seller's markets in recent memory.

9. Industry consolidation. The auto aftermarket is currently experiencing a rapid consolidation trend as companies are merging, acquiring, and going out-of-business at faster rates than ever before. Only the strongest and most defensible companies will survive over the next 10 years. Partnering with a private equity group and using its capital and resources is one of the best ways to ensure prosperity during this traumatic phase of the industry's life cycle.

10. Favorable economic environment. One of the reasons private equity groups have been as active as they are is because the US economy is currently in very good shape. After growing 4.4 percent in 2004 (biggest annual gain since 1999), US gross domestic product is expected to average 3.6 percent growth in 2005. Inflation is expected to average 2.3 percent in 2005 and 2006, well within the 2 to 3 percent target set by most economists. Analysts forecast the unemployment rate will average 5.2 percent in 2005, and will fall to an annual average of 5.0 percent in 2006. By almost any standard, these are excellent economic statistics. While the economy remains healthy, we believe private equity groups will continue to deploy their capital at a rapid rate. Should the economy take a turn for the worse, there is more than a good chance that private equity groups will become more tight-fisted. *Note: Contrary to popular belief, the economic uncertainty we are currently facing has not been a deterrent for Private Equity buyers. Private Equity is "driven" by access to debt capital. With leverage as inexpensive and readily available as it currently is, Private Equity remains an active buyer.*

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.

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

| Company | Enterprise Value | | | | | Last Twelve Months (LTM) | | | |
|---------------------------------------|----------------------|------------|-----------|---------|----------------------|--------------------------|------------|-----------|------------|
| | Price as of 11/30/11 | Market Cap | Debt | Cash | Enterprise Value (1) | LTM Date | Revenue | EBITDA | Net Income |
| Manufacturers | | | | | | | | | |
| Federal-Mogul Corporation | \$14.60 | \$1,444.0 | \$2,834.0 | \$931.0 | \$3,446.0 | 9/30/11 | \$6,844.0 | \$645.0 | \$198.7 |
| Tenneco Automotive, Inc. | 28.96 | 1,746.2 | 1,304.0 | 163.0 | 2,979.7 | 9/30/11 | 6,998.0 | 583.0 | 115.7 |
| Dorman Products, Inc. | 38.68 | 698.2 | 3.8 | 45.6 | 679.8 | 9/24/11 | 512.8 | 86.8 | 48.9 |
| Standard Motor Products, Inc. | 19.53 | 442.0 | 42.1 | 14.9 | 471.6 | 9/30/11 | 873.4 | 78.9 | 38.0 |
| Wholesalers & Distributors | | | | | | | | | |
| Genuine Parts Company | \$58.06 | \$9,037.2 | \$500.0 | \$534.8 | \$9,127.2 | 9/30/11 | \$12,252.5 | \$980.4 | \$548.8 |
| LKQ Corporation | 30.53 | 4,474.9 | 632.6 | 45.1 | 5,265.1 | 9/30/11 | 3,004.3 | 399.2 | 202.0 |
| The Coast Distribution System, Inc. | 2.54 | 12.1 | 10.9 | 5.7 | 17.3 | 9/30/11 | 107.1 | 0.2 | (1.2) |
| Retailers | | | | | | | | | |
| Autozone, Inc. | \$328.38 | \$13,647.6 | \$3,351.7 | \$97.6 | \$17,417.4 | 8/27/11 | \$8,073.0 | \$1,691.0 | \$849.0 |
| Advance Auto Parts, Inc. | 69.16 | 5,010.4 | 600.4 | 65.9 | 5,724.0 | 10/8/11 | 6,113.0 | 810.1 | 376.4 |
| O'Reilly Automotive, Inc. | 77.24 | 9,912.1 | 797.8 | 276.7 | 10,927.4 | 9/30/11 | 5,707.8 | 987.9 | 499.1 |
| The Pep Boys - Manny, Moe & Jack | 11.50 | 605.8 | 295.4 | 80.7 | 826.1 | 10/29/11 | 2,035.7 | 161.9 | 41.9 |
| US Auto Parts Network, Inc. | 4.11 | 125.9 | 19.4 | 15.2 | 130.2 | 10/1/11 | 330.3 | 7.2 | (11.0) |

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 | 0.5x | 10.0x | 5.3x | 12.4x | 17.3x | 7.3 | 15.8% | 9.4% | 2.9% |
| Tenneco Automotive, Inc. | 0.4x | 8.0x | 5.1x | 7.6x | 25.8x | 15.1 | 16.4% | 8.3% | 1.7% |
| Dorman Products, Inc. | 1.3x | 8.6x | 7.8x | 10.0x | 13.9x | 14.3 | 36.2% | 16.9% | 9.5% |
| Standard Motor Products, Inc. | 0.5x | 7.3x | 6.0x | 6.7x | 12.4x | 11.6 | 25.9% | 9.0% | 4.3% |
| Mean | 0.7x | 8.5x | 6.1x | 9.2x | 17.4x | 12.1x | 23.6% | 10.9% | 4.6% |
| Median | 0.5x | 8.3x | 5.7x | 8.8x | 15.6x | 13.0x | 21.2% | 9.2% | 3.6% |
| Wholesalers & Distributors | | | | | | | | | |
| Genuine Parts Company | 0.7x | 10.2x | 9.3x | 10.3x | 16.6x | 16.5 | 28.8% | 8.0% | 4.5% |
| LKQ Corporation | 1.8x | 15.0x | 13.2x | 16.8x | 26.1x | 22.2 | 42.9% | 13.3% | 6.7% |
| The Coast Distribution System, Inc. | 0.2x | NM | NM | NM | NM | NM | 16.8% | 0.2% | NM |
| Mean | 0.9x | 12.6x | 11.2x | 13.5x | 21.3x | 19.3x | 29.5% | 7.2% | 5.6% |
| Median | 0.7x | 12.6x | 11.2x | 13.5x | 21.3x | 19.3x | 28.8% | 8.0% | 5.6% |
| Retailers | | | | | | | | | |
| Autozone, Inc. | 2.2x | 11.7x | 10.3x | 12.7x | 20.5x | 16.1 | 51.0% | 20.9% | 10.5% |
| Advance Auto Parts, Inc. | 0.9x | 9.0x | 7.1x | 10.4x | 15.2x | 13.3 | 49.8% | 13.3% | 6.2% |
| O'Reilly Automotive, Inc. | 1.9x | 13.3x | 11.1x | 16.7x | 21.9x | 19.9 | 48.7% | 17.3% | 8.7% |
| The Pep Boys - Manny, Moe & Jack | 0.4x | 9.9x | 5.1x | 9.8x | 19.7x | 14.5 | 25.6% | 8.0% | 2.1% |
| US Auto Parts Network, Inc. | 0.4x | NM | 18.1x | NM | NM | NM | 33.5% | 2.2% | NM |
| Mean | 1.4x | 11.0x | 10.3x | 12.4x | 19.3x | 15.9x | 41.7% | 12.3% | 6.9% |
| Median | 1.4x | 10.8x | 10.3x | 11.6x | 20.1x | 15.3x | 49.3% | 15.3% | 7.5% |

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

(2) Free Cash Flow equals EBITDA less capital expenditure

"NM" is not meaningful