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2014 Private Capital Markets Report

Craig R. Everett
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2014 CAPITAL MARKETS REPORT

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FORWARD

BUSINESS OWNER OPTIMISM TEMPERED BY PRIVATE CAPITAL LENDERS' DEBILITATING CONCERN ABOUT ECONOMIC UNCERTAINTY

According to the 2014 Pepperdine Private Capital Markets Survey (PPCMP), 65 percent of privately-held businesses surveyed believe that growth opportunities will increase over the next twelve months. The survey also revealed that more than a third of businesses (35 percent) think that general business conditions will improve over the next year. This is evidence that privately-held businesses are starting to see the light at the end of the tunnel.

This is good news for economic growth and stability. It is also good news for job seekers as more than half of the 951 businesses surveyed (53 percent) say they are planning to hire additional workers in the next twelve months. For businesses that plan to hire, sales and marketing skills are in greatest demand (57 percent) followed by skilled labor (45 percent) and service/customer service (36 percent).

As business owners become more optimistic about the health of the economy, they also desire economic certainty. Of the businesses that do not plan to hire, 51 percent of respondents cite economic uncertainty in the U.S. market as the main reason. This concern is echoed by capital lenders. According to the 2014 PPCMP, nearly every industry sector in the private capital markets reported that economic uncertainty is the biggest current or emerging issue facing privately-held businesses.

The cost of economic uncertainity on the private capital markets and privately-held businesses is nearly incalculable. However, we know there is a correlation between economic instability and access to capital. If private capital market providers are anxious they may hold their pursestrings tight which will limit access to capital for businesses that desperately need additional funding to grow.

This stability-access factor could be catastrophic as the majority of businesses surveyed (89 percent) say that they want to execute growth strategies. This is easier for some businesses than others as companies with smaller revenues report having lower levels of necessary resources (staff, money, etc.) to grow (46 percent) as compared to privately-held businesses with higher revenues (66 percent).

Establishing certainity in our nation's economic health is essential for private capital market lenders to feel confident that they should expand their lending capacity. Certainty also infuses confidence into privately-held businesses who are just now starting to become more optimistic about the business environment.

Unfortunately, the reality is that uncertainity pervades our business environment. The USA Today captured this sentiment perfectly: "Since the 2008 financial crisis, uncertainty — about budget battles, the new health care law, taxes and regulations — has shadowed the recovery, reducing business investment and hiring, and chilling consumer spending."

There is also uncertainty about how long interest rates will remain low, the duration of the federal government's bond buying program as well as the looming the debt ceiling debate, which Congress will take up in advance of the February 7, 2014 deadline.

Privately-held businesses are on the brink of turning a corner. Mark Zandi, chief economist at Moody's Analytics put it well when he said "every six months, we have a showdown. The constant brinkmanship has weighed on decisions to invest and hire." Businesses and private capital lenders need policymakers to provide assurance that the short-term measures are ending and that permanent solutions will be put in place. Short-term fixes alleviate the crisis atmosphere, but do not solve lingering fears about prolonged uncertainty.

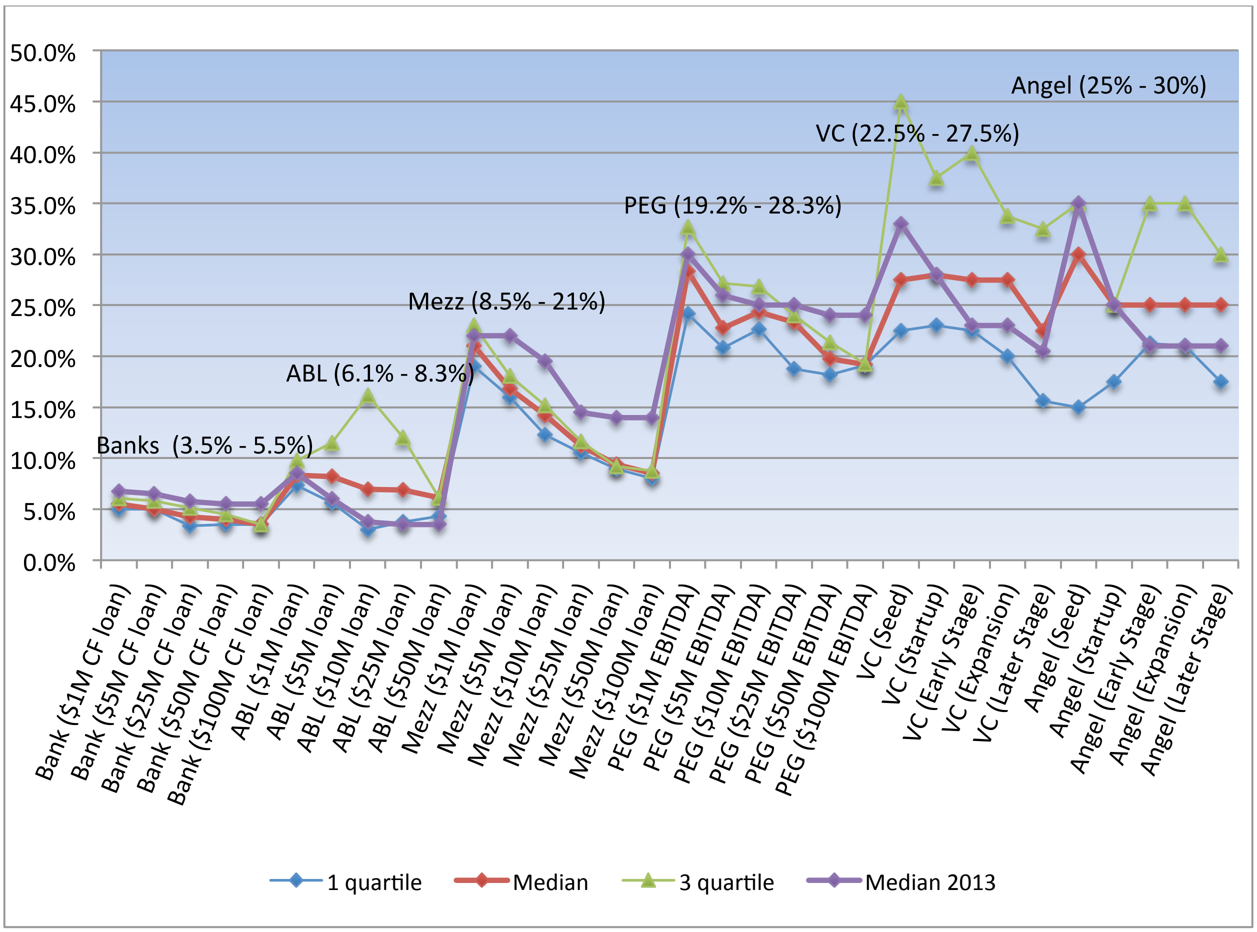
Craig R. Everett, Ph.D.
Pepperdine Private Capital Markets Project

ABOUT PEPPERDINE PRIVATE CAPITAL MARKETS SURVEY

The Pepperdine private cost of capital survey (PCOC) was originally launched in 2007 and is the first comprehensive and simultaneous investigation of the major private capital market segments. This year's survey, deployed in October 2013, specifically examined the behavior of senior lenders, asset-based lenders, mezzanine funds, private equity groups, venture capital firms, angel investors, privately-held businesses, investment bankers, business brokers, limited partners, and business appraisers. The Pepperdine PCOC survey investigated, for each private capital market segment, the important benchmarks that must be met in order to qualify for capital, how much capital is typically accessible, what the required returns are for extending capital in today's economic environment, and outlooks on demand for various capital types, interest rates, and the economy in general.

Our findings indicate that the cost of capital for privately-held businesses varies significantly by capital type, size, and risk assumed. This relationship is depicted in the Pepperdine Private Capital Market Line, which appears below.

Figure 1. Private Capital Market Required Rates of Return



The cost of capital data presented below identifies medians, 25^{th} th percentiles (1st quartile), and 75^{th} percentiles (3^{rd} quartile) of annualized gross financing costs for each major capital type and its segments. The data reveal that loans have the lowest average rates while capital obtained from angels has the highest average rates. As the size of loan or investment increases, the cost of borrowing or financing from any of the following sources decreases.

Table 1. Private Capital Market Required Rates of Return

	1st quartile	Median	3rd quartile
Bank ($1M CF loan)	5.0%	5.5%	6.1%
Bank ($5M CF loan)	5.0%	5.0%	5.8%
Bank ($10M CF loan)	3.4%	4.3%	5.1%
Bank ($25M CF loan)	3.5%	4.0%	4.5%
Bank ($50M CF loan)	3.5%	3.5%	3.5%
ABL ($1M loan)	7.3%	8.3%	9.8%
ABL ($5M loan)	5.6%	8.2%	11.5%
ABL ($10M loan)	3.0%	6.9%	16.2%
ABL ($25M loan)	3.8%	6.9%	12.0%
ABL ($50M loan)	4.3%	6.1%	6.1%
Mezz ($1M loan)	19.0%	21.0%	23.0%
Mezz ($5M loan)	16.0%	16.8%	18.1%
Mezz ($10M loan)	12.3%	14.2%	15.2%
Mezz ($25M loan)	10.5%	11.2%	11.6%
Mezz ($50M loan)	9.0%	9.4%	9.2%
Mezz ($100M loan)	8.0%	8.5%	8.8%
PEG ($1M EBITDA)	24.2%	28.3%	32.7%
PEG ($5M EBITDA)	20.8%	22.8%	27.1%
PEG ($10M EBITDA)	22.7%	24.4%	26.9%
PEG ($25M EBITDA)	18.7%	23.3%	24.0%
PEG ($50M EBITDA)	18.2%	19.7%	21.4%
PEG ($100M EBITDA)	19.1%	19.2%	19.3%
VC (Seed)	22.5%	27.5%	45.0%
VC (Startup)	23.0%	28.0%	37.5%
VC (Early Stage)	22.5%	27.5%	40.0%
VC (Expansion)	20.0%	27.5%	33.8%
VC (Later Stage)	15.6%	22.5%	32.5%
Angel (Seed)	15.0%	30.0%	35.0%
Angel (Startup)	17.5%	25.0%	25.0%
Angel (Early Stage)	21.3%	25.0%	35.0%
Angel (Expansion)	21.0%	25.0%	35.0%
Angel (Later Stage)	17.5%	25.0%	30.0%

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INVESTMENT BANKER SURVEY INFORMATION

The majority of the 141 respondents to the investment banker survey indicated increasing margin pressure on companies over the last 12 months. They also reported slight increases in deal flow, increased presence of strategic buyers, leverage and deal multiples, and improved business conditions. Domestic economic uncertainty and taxes was identified as the most important current and emerging issue facing privately-held businesses.

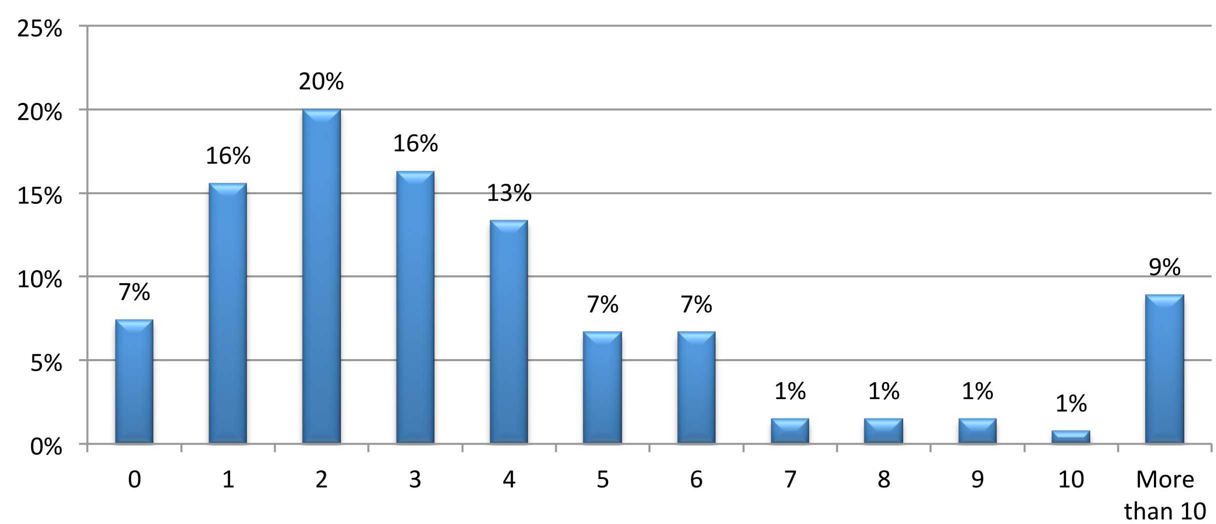
Other key findings include:

- Approximately 31 percent of respondents expect to close six or more deals in the next 12 months.
- The top three reasons for deals not closing were valuation gap (26 percent), unreasonable seller or buyer demand (21 percent), economic uncertainty (12 percent), and insufficient cash flow (12 percent).
- Respondents indicated a general imbalance between companies worthy of financing and capital available for the same. There is a reported shortage of capital for those companies with less than $10 million in EBITDA, but a general surplus for companies with $10 million in EBITDA or more.
- The most popular valuation methods used by respondents when valuing privately-held businesses were discounted future earnings and guideline company transactions approaches.
- When using multiples to determine the value of a business, the most popular methods used by respondents when valuing privately-held businesses were recast (adjusted) EBITDA multiple (58 percent), revenue multiple (13 percent) and EBITDA (unadjusted) multiple approaches.

Operational and Assessment Characteristics

Approximately 7 percent of the respondents did not close any deals in the last 12 months; 72 percent closed between one and five deals, while 21 percent closed six transactions or more.

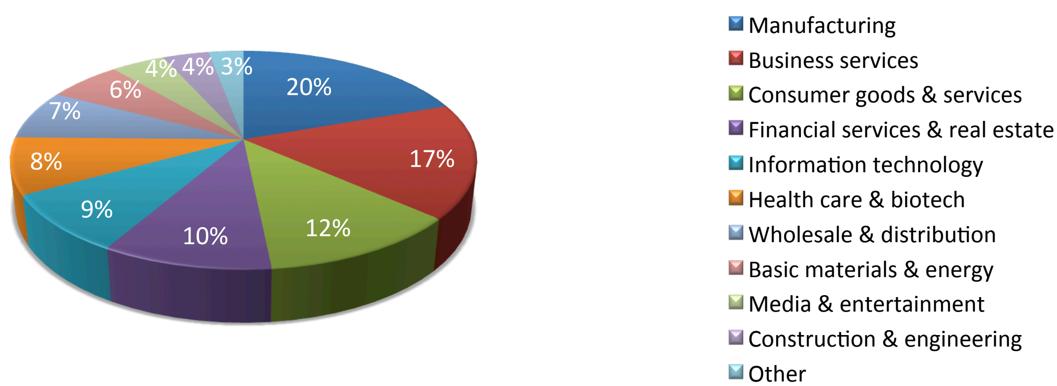
Figure 2. Private Business Sales Transactions Closed in the Last 12 Months



I-BANKER cont.

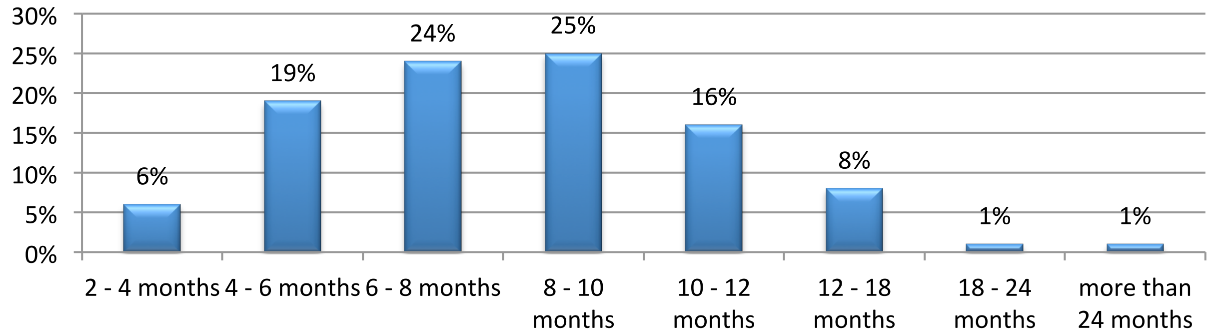
Approximately 20 percent of all transactions closed in the last 12 months involved manufacturing, followed by 17 percent that involved business services, and 12 percent that involved consumer goods and services.

Figure 3. Business Types That Were Involved in the Transactions Closed in the Last 12 Months



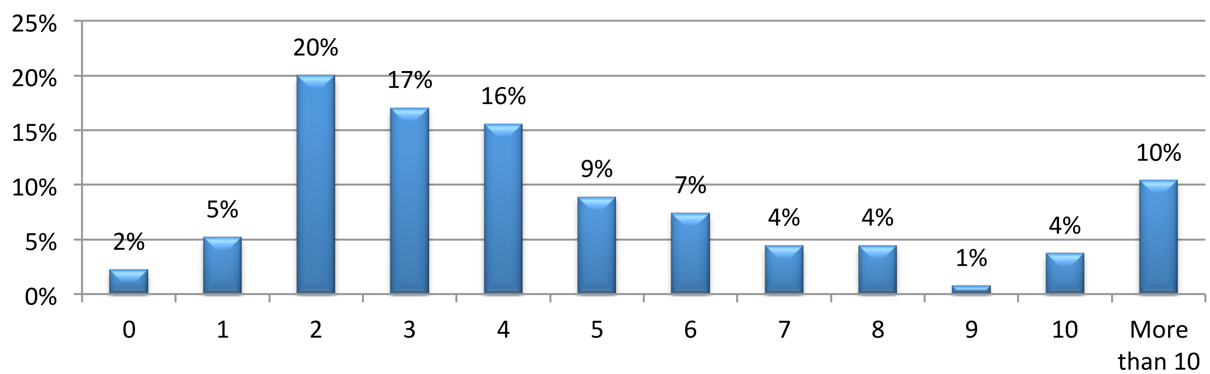
The majority of deals (68 percent) took 6 to 12 months to close. 10 percent of closed deals take more than one year to close.

Figure 4. Average Number of Months to Close One Deal



Nearly 2 percent of the respondents do not expect to close any deals in the next 12 months; 67 percent expect to close between one and five deals; and 31 percent expect to close 6 deals or more.

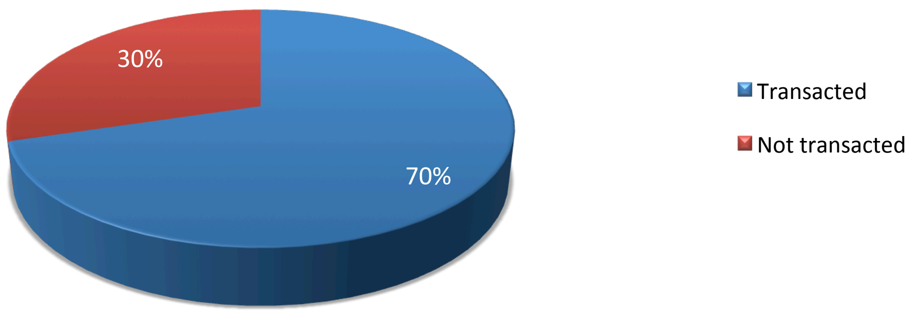
Figure 5. Private Business Transactions Expected to Close in the Next 12 Months



I-BANKER cont.

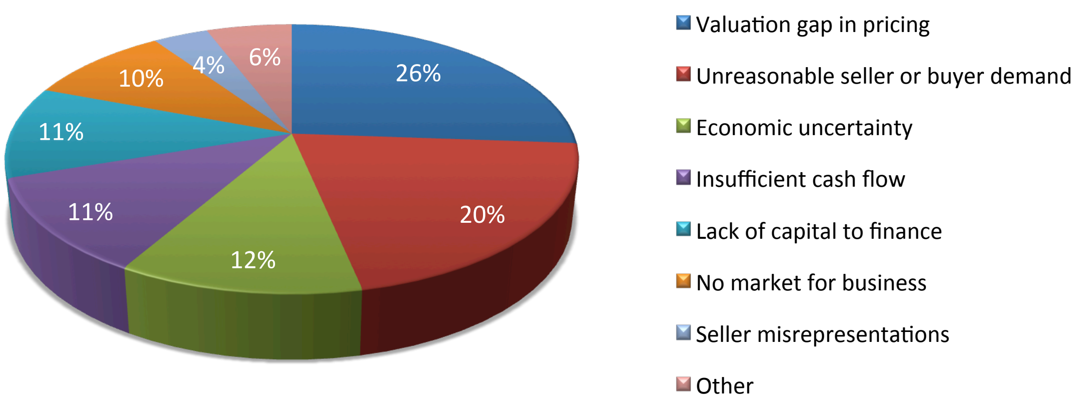
Approximately 30 percent of deals terminated without transacting over the past year.

Figure 6. Percentage of Business Sales Engagements Terminated Without Transacting



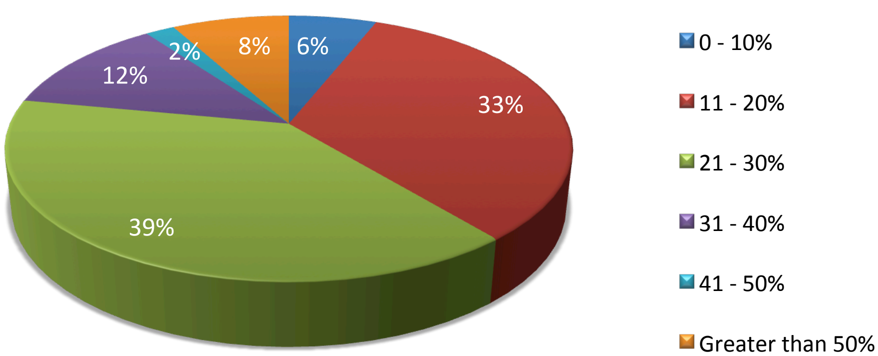
Top three reasons for deals not closing: valuation gap in pricing (26 percent), unreasonable seller/buyer demand (20 percent), and economic uncertainty (12 percent).

Figure 7. Reasons for Business Sales Engagements Not Transacting



Of those transactions that did not close due to a valuation gap in pricing, approximately 39 percent had a valuation gap in pricing between 21 percent and 30 percent.

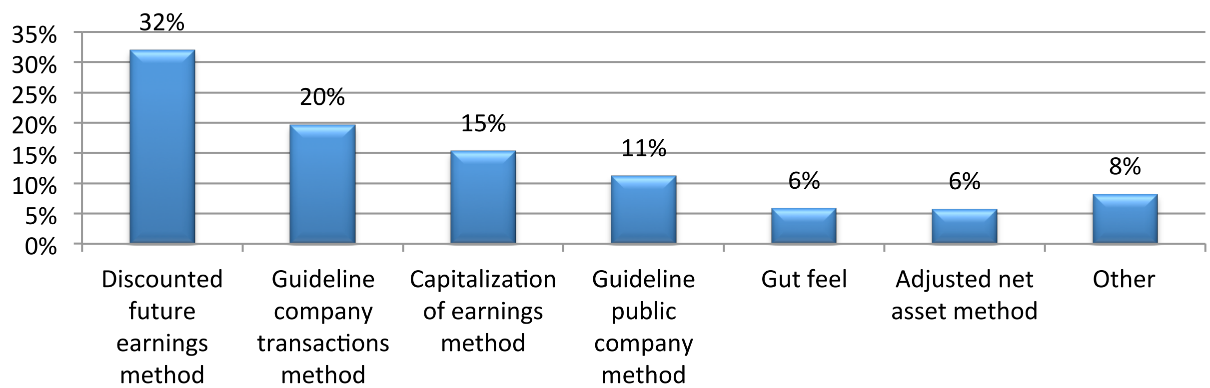
Figure 8. Valuation Gap in Pricing for Transactions That Didn't Close



I-BANKER cont.

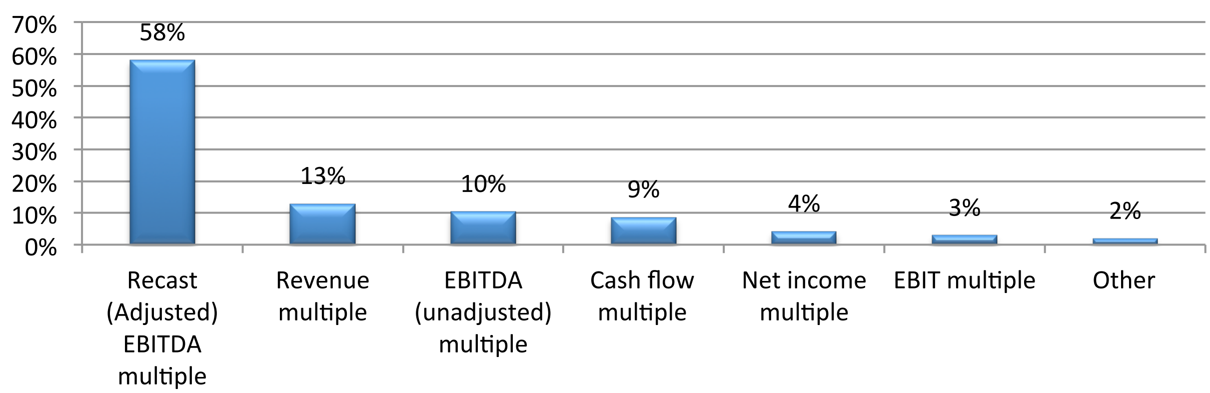
The weights of the various valuation methods used by respondents when valuing privately-held businesses included 32 percent for discounted future earnings method.

Figure 9. Usage of Valuation Methods



The weights of the various multiple methods used by respondents when valuing privately-held businesses included 58 percent for recast (adjusted) EBITDA multiple.

Figure 10. Usage of Multiple Methods



Average deal multiples on transactions from the prior 12 months as observed by respondents varied from 4.2 to 7.7.

Table 2. Median Deal Multiples by EBITDA Size of Company

EBITDA	Manufacturing	Construction & engineering	Cons. goods & services	Wholesale & distribution	Business services	Basic materials & energy	Health care & biotech	IT	Financial services	Media & entertain.	**Avg.**
$0M - $1M	3.8	3	3.5	4	4	3.5	6	5	5	4	**4.2**
$2M - $5M	5.0	4.3	5.3	5	5	4.5	6	6	5.5	4.8	**5.1**
$6M - $10M	6.0	4.3	6.3	5.3	6	5	6	6	6.3	6.0	**5.7**
$11M - $25M	6	10	6.3	7	6.5	5.0	6.5	7.5	6.3	7.5	**6.9**
$26M - $50M	6.5	n/a	6.3	7.0	6.5	7	8.8	7.5	7	n/a	**7.1**
>$50M	6.5	n/a	6.3	7	7.5	7	8.8	7.75	7.5	11	**7.7**

Average total leverage multiples observed by respondents varied from 2.3 to 4.3.

Table 3. Median Total Leverage Multiples by Size of Company

EBITDA	Manufacturing	Construction & engineering	Cons. goods & services	Wholesale & distribution	Business services	Basic materials & energy	Health care & biotech	IT	Financial services	Media & entertain.	**Avg.**
$0M - $1M	2	n/a	3	n/a	2	2	1.5	1.5	2.5	4	**2.3**
$2M - $5M	3.5	3	3.5	3.5	3.5	3	2.8	3	3	4	**3.3**
$6M - $10M	3.5	3	4	4	3.8	3	4	4	3.5	5	**3.8**
$11M - $25M	3.5	n/a	4.5	4.5	3.8	3	4	3	3.5	n/a	**3.7**
$26M - $50M	3.5	n/a	4.5	n/a	3.8	3	4	3.3	4	n/a	**3.7**
>$50M	4	n/a	4.5	4.5	3.8	3	5.8	3.8	4	5	**4.3**

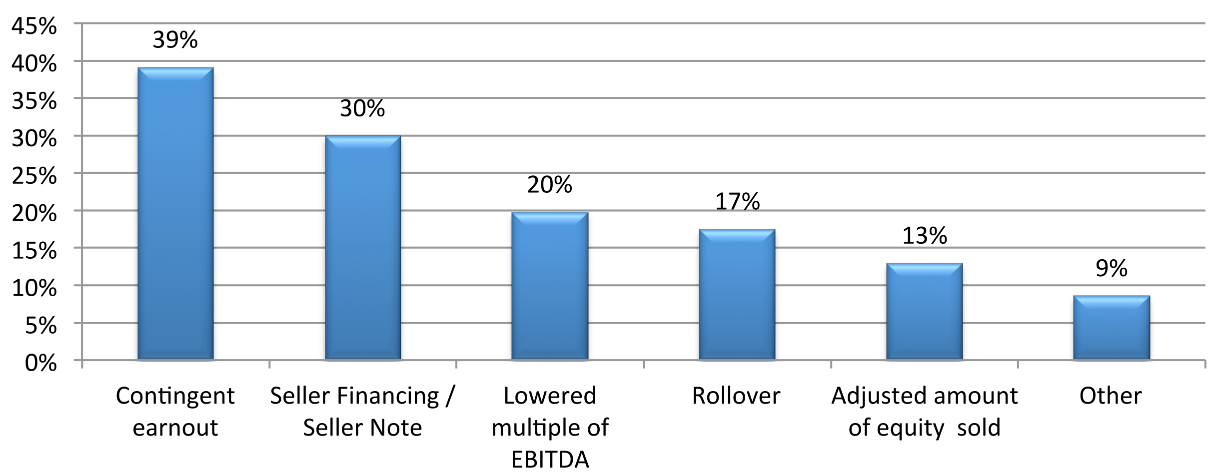
Average senior leverage multiples observed by respondents varied from 2.0 to 3.6.

Table 4. Median Senior Leverage Multiples by Size of Company

EBITDA	Manuf.	Construction & engineering	Cons. goods & services	Wholesale & distribution	Busines s services	Basic material s & energy	Health care & biotech	IT	Financial services	Media & entertain.	**Median, all industries**
$0M - $1M	1.8	2	3	2.5	2	2	3	2	2.3	2.5	**2.0**
$2M - $5M	2.5	2	3	2.5	2.5	2	3	2.5	2.8	3.0	**2.5**
$6M - $10M	3	2	3.3	4	3	3.5	3.3	2.75	3.3	3.8	**3.0**
$11M - $25M	3	n/a	3.5	4	3	3.5	3.3	3	4	n/a	**3.0**
$26M - $50M	3	n/a	4.5	n/a	3	3	3.3	3	4.5	n/a	**3.0**
>$50M	3.3	n/a	4.75	n/a	3.5	3	5.5	3.5	2.5	3.8	**3.6**

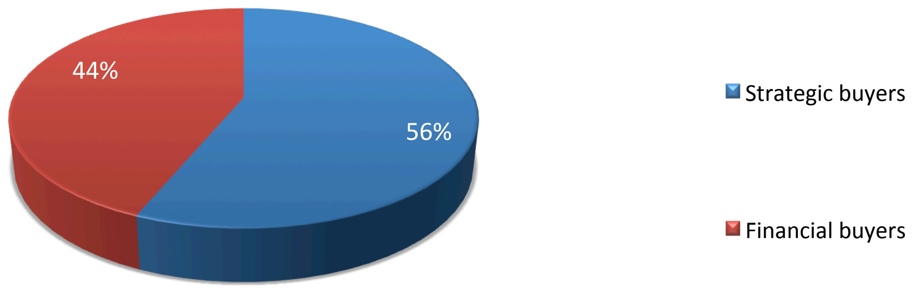
Approximately 39 percent of business sales transactions closed in the last 12 months involved contingent earn-outs.

Figure 11. Components of Closed Deals



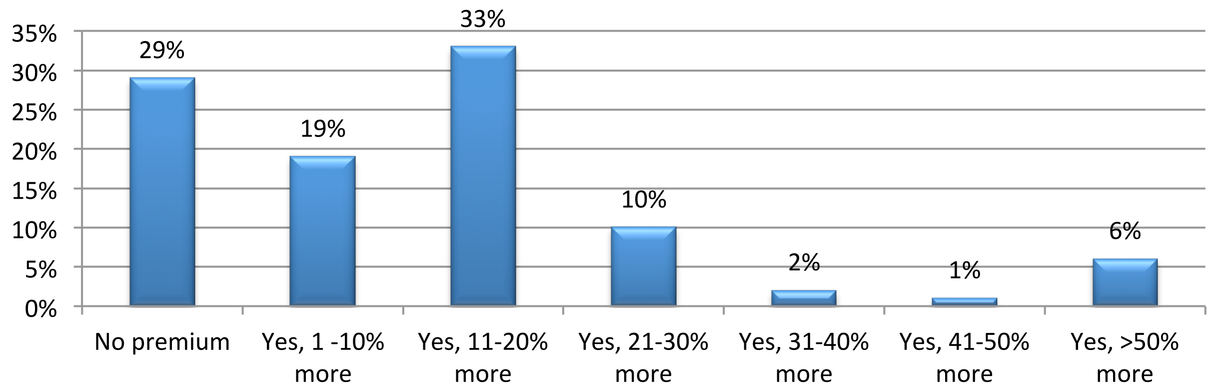
Approximately 56 percent of closed business sales transactions over the past 12 months involved strategic buyers.

Figure 12. Percent of Transactions Involved Strategic and Financial Buyers



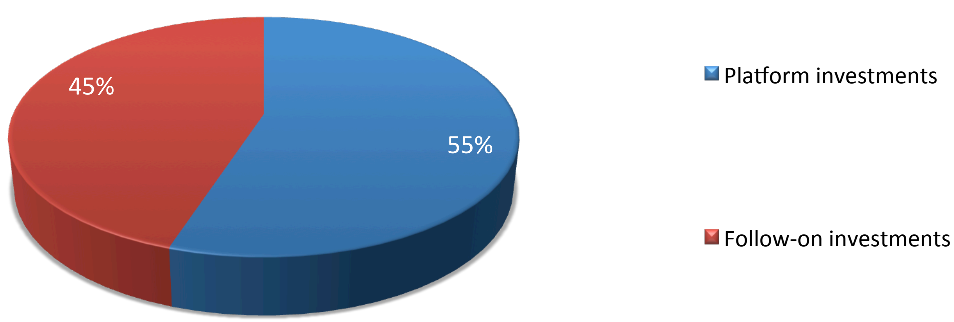
Approximately 29 percent of respondents did not witness any premium paid by strategic buyers, while 52 percent saw premiums between 1 percent and 20 percent.

Figure 13. Premium Paid by Strategic Buyers Relative to Financial Buyers



Approximately 55 percent of closed business sales transactions that involved financial buyers over the past 12 months were platform investments.

Figure 14. Percent of Transactions Involved Strategic and Financial Buyers



I-BANKER cont.

Respondents indicated a general imbalance between companies worthy of financing and capital available for the same. There is a reported shortage of capital for those companies with less than $10 million in EBITDA but a general surplus for companies with $10 million in EBITDA or more.

Table 5. Balance of Available Capital with Quality Companies

EBITDA	Companies worthy of financing GREATLY exceed capital available	Companies worthy of financing exceed capital available	General balance	Capital available exceeds companies worthy of financing	Capital available GREATLY exceeds companies worthy of financing	**Score (-2 to 2)**
$1M	19%	43%	16%	16%	6%	**-0.5**
$5M	10%	29%	28%	22%	11%	**-0.1**
$10M	9%	13%	36%	21%	20%	**0.3**
$15M	9%	12%	26%	32%	21%	**0.4**
$25M	7%	7%	23%	34%	30%	**0.7**
$50M	9%	6%	25%	34%	26%	**0.6**
$100M	8%	4%	25%	31%	31%	**0.7**
>$100M	13%	7%	15%	24%	41%	**0.7**

Respondents indicated a general difficulty with arranging senior debt for businesses with less than or equal to $5 million in EBITDA.

Table 6. How Difficult to Arrange Senior Debt for Transactions over the Past 12 Months

EBITDA	Extremely difficult	Difficult	Somewhat difficult	Neutral	Somewhat easy	Easy	Extremely easy	**Score (-3 to 3)**
$1M	33%	32%	10%	11%	7%	6%	1%	**-1.5**
$5M	11%	11%	19%	16%	22%	20%	1%	**-0.1**
$10M	3%	11%	14%	19%	22%	16%	14%	**0.5**
$15M	2%	5%	14%	17%	29%	14%	19%	**0.8**
$25M	3%	6%	22%	9%	25%	16%	19%	**0.7**
$50M	4%	8%	17%	13%	17%	13%	29%	**0.8**
$100M+	4%	8%	12%	12%	12%	16%	36%	**1.1**

Respondents indicated slightly increased deal flow, increased leverage and deal multiples, percentage of strategic buyers making deals, and margin pressure on companies in the last 12 months.

Table 7. General Business and Industry Assessment: Today versus 12 Months Ago

	Decreased significantly	Decreased slightly	Stayed about the same	Increased slightly	Increased significantly	% increase	% decrease	**Net increase/ decrease**
Deal flow	10%	16%	32%	30%	12%	42%	26%	**15%**
Leverage multiples	3%	10%	40%	46%	2%	48%	12%	**36%**
Deal multiples	3%	5%	41%	47%	3%	50%	8%	**42%**
Amount of time to sell business	0%	8%	56%	25%	10%	35%	8%	**27%**
Difficulty financing/selling business	0%	23%	49%	21%	8%	29%	23%	**6%**
General business conditions	4%	17%	37%	39%	3%	42%	21%	**20%**
Strategic buyers making deals	3%	11%	34%	45%	7%	52%	13%	**39%**
Margin pressure on companies	1%	8%	47%	33%	10%	43%	9%	**34%**
Buyer interest in minority transactions	8%	13%	53%	23%	3%	26%	21%	**4%**

I-BANKER cont.

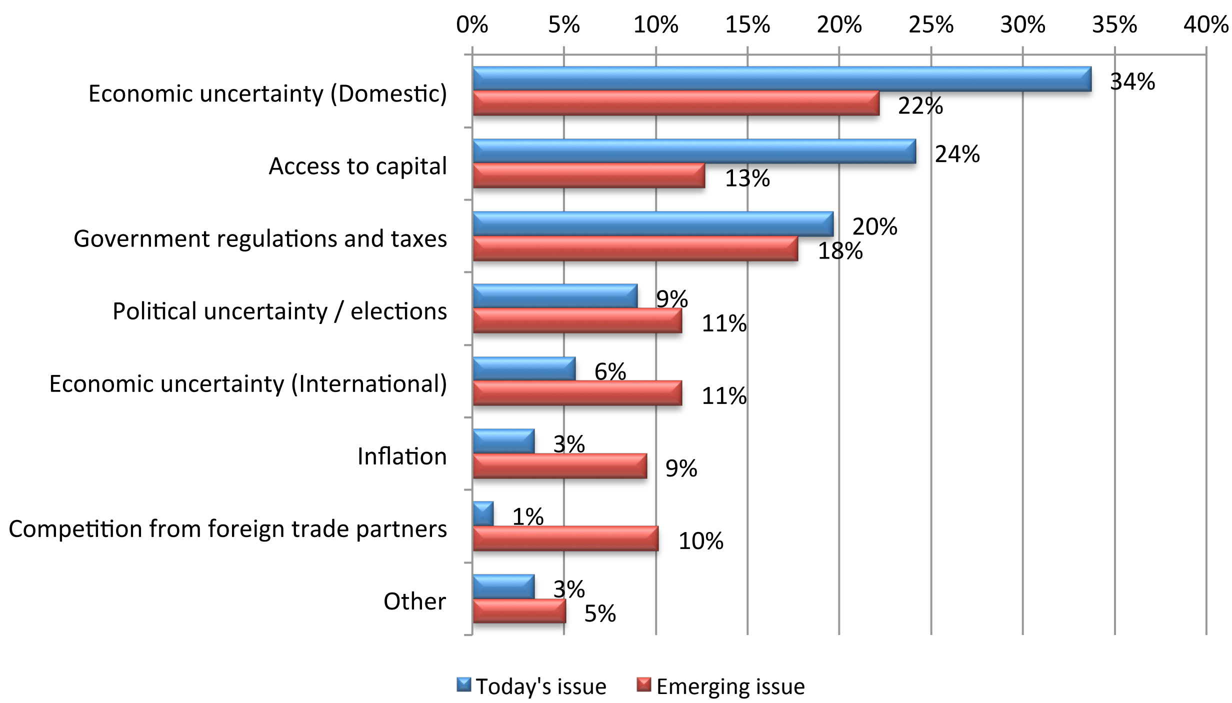
During the next 12 months, respondents expect further increases in deal flow, margin pressure on companies, strategic buyers making deals, leverage and deal multiples and general business conditions.

Table 8. General Business and Industry Assessment Expectations over the Next 12 Months

	Decrease significantly	Decrease slightly	Stay about the same	Increase slightly	Increase significantly	% increase	% decrease	**Net increase/ decrease**
Deal flow	2%	4%	33%	55%	6%	61%	6%	**55%**
Leverage multiples	0%	11%	50%	38%	0%	38%	11%	**27%**
Deal multiples	0%	8%	49%	42%	1%	42%	8%	**34%**
Amount of time to sell business	0%	13%	68%	17%	3%	19%	13%	**7%**
Difficulty financing/selling business	0%	22%	61%	14%	3%	17%	22%	**-5%**
General business conditions	3%	9%	43%	44%	2%	45%	12%	**33%**
Strategic buyers making deals	0%	3%	49%	44%	3%	48%	3%	**44%**
Margin pressure on companies	0%	10%	58%	29%	3%	32%	10%	**23%**
Buyer interest in minority transactions	6%	7%	70%	15%	2%	17%	13%	**4%**

Respondents believe domestic economic uncertainty is the most important current and emerging issue facing privately-held businesses.

Figure 15. Issues Facing Privately-Held Businesses



PRIVATE EQUITY SURVEY INFORMATION

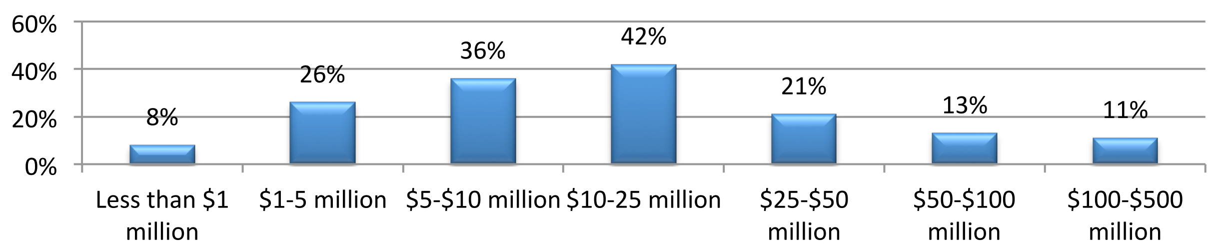
Approximately 42 percent of the 64 participants who responded to the private equity groups survey indicated that they make investments in the $10 million to $25 million range. Nearly 35 percent of respondents said that demand for private equity is up from 12 months ago, this is down from 42 percent of respondents indicating increased demand in 2013. Other key findings include:

- Respondents indicated increases in the quality of companies seeking investment. They also reported a slight decrease in expected returns on new investments, improved general business conditions and increase in expected investment holding period.
- Respondents expect further increases in demand for private equity, deal multiples, value of portfolio companies and improving business conditions.
- The types of businesses respondents plan to invest in over next 12 months are very diverse with over 19 percent targeting manufacturing and another 16 percent planning to invest in business services.
- Respondents believe domestic economic uncertainty is the most important issue facing privately-held businesses today.
- The most popular valuation methods used by respondents when valuing privately-held businesses were discounted future earnings and guideline company transactions approaches.
- When using multiples to determine the value of a business, the most popular methods used by respondents when valuing privately-held businesses were recast EBITDA multiple (33 percent) and EBITDA multiple (31 percent).

Operational and Assessment Characteristics

The largest concentration of checks written was in the $10 - $25 million range (42 percent), followed by $5 - $10 million (36 percent), and $25 - $50 million (21 percent).

Figure 16. Typical Investment Size



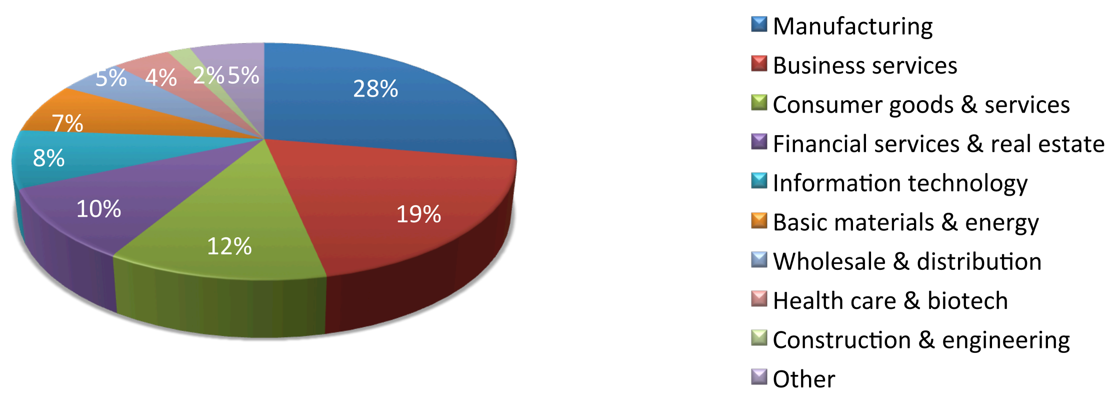
Respondents reported on business practices and the results are reflected below.

Table 9. PEG Fund Data

	1st Quartile	Median	3rd Quartile
Vintage year (year in which first investment made)	2007	2011	2012
Size of fund ($ millions)	37.5	175	350
Targeted number of total investments	8	8	13
Target fund return (gross pretax cash on cash annual IRR %)	20%	25%	30%
Expected fund return (gross pretax cash on cash annual IRR%)	18%	23%	25%

The types of businesses respondents plan to invest in over next 12 months are very diverse with over 28 percent targeting manufacturing and another 19 percent planning to invest in business services.

Figure 17. Type of Business for Investments Planned over Next 12 Months



Approximately 48 percent of respondents made between one and three investments over the last 12 months.

Figure 18. Total Number of Investments Made in the Last 12 Months

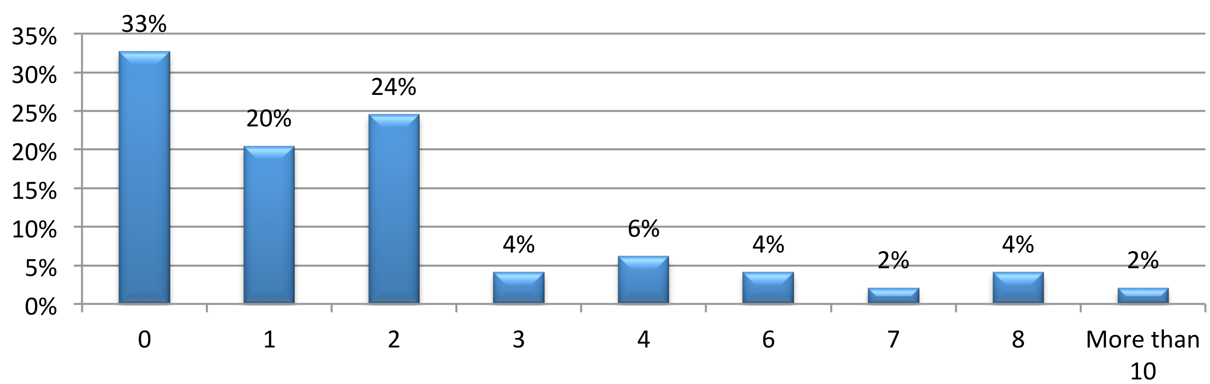
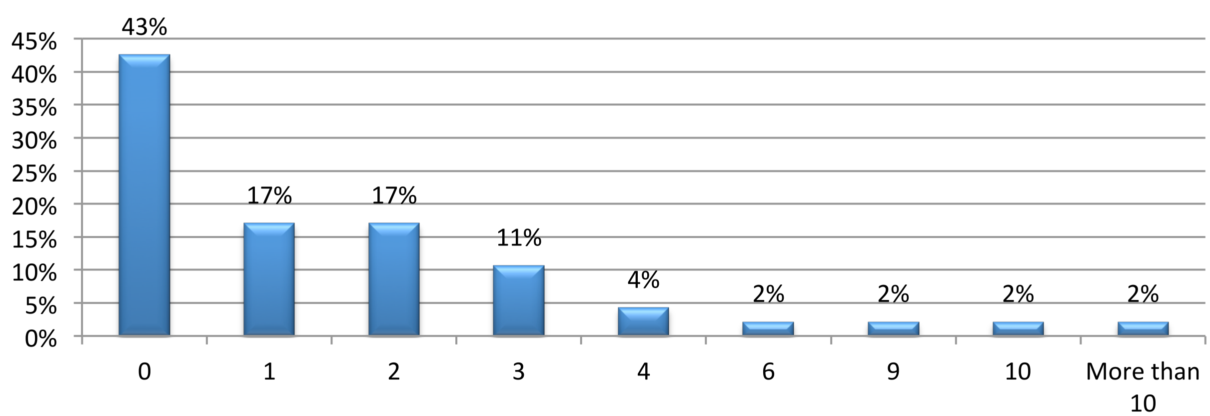


Figure 19. Number of Follow-on Investments Made in the Last 12 Months



The majority (70 percent) of respondents plan to make one to four investments over the next 12 months.

Figure 20. Number of Total Investments Planned over Next 12 Months

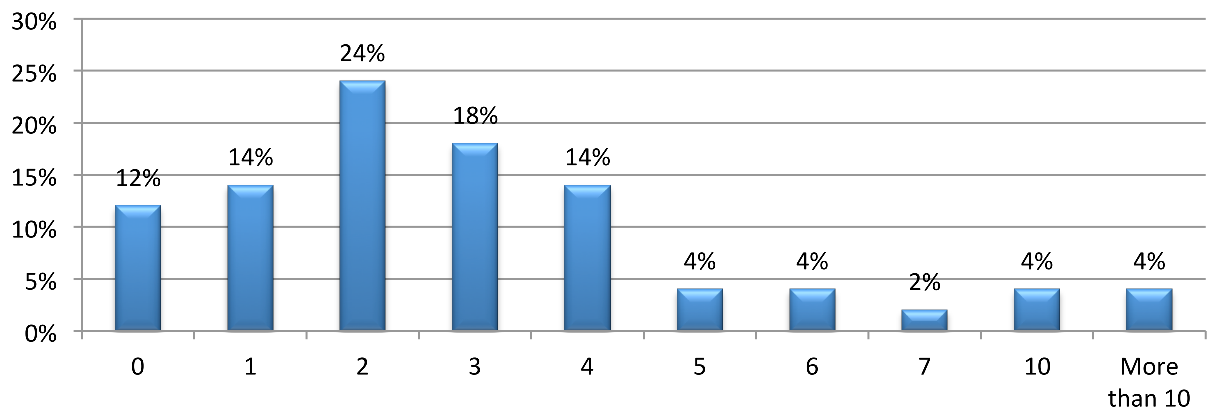
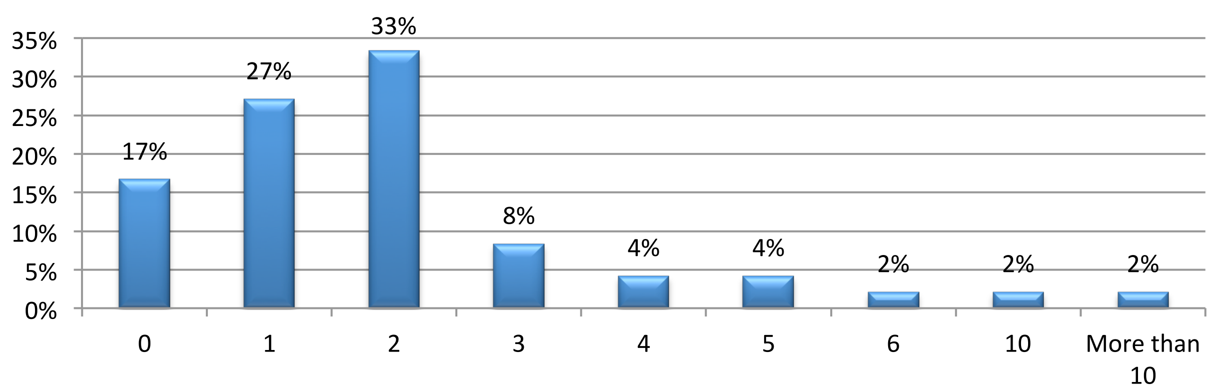


Figure 21. Number of Follow-on Investments Planned over Next 12 Months



Average deal multiples for buyout deals for the prior 12 months vary from 5.5 to 7.5 times EBITDA depending on the size of the company. Expected returns vary from 20 percent to 25 percent.

Table 10. General Characteristics – Buyout Transactions (medians)

	$1M EBITDA	$5M EBITDA	$10M EBITDA	$25M EBITDA	$50M EBITDA
Number of investments	1	1	1	1	2
Average size of investment in million USD (medians)	3	7.5	15	30	30
Expected time to exit (years) (medians)	5.8	5	4.5	4.5	5.5
Equity as % of new capital structure	80%	55%	40%	35%	30%
% of total equity purchased	80%	75%	85%	90%	100%
Average deal multiple (multiple of EBITDA)	5.5	5.8	6.3	6.5	7.5
Total expected returns (gross cash on cash pre-tax IRR)	25.0%	25.0%	25.0%	25.0%	20.0%

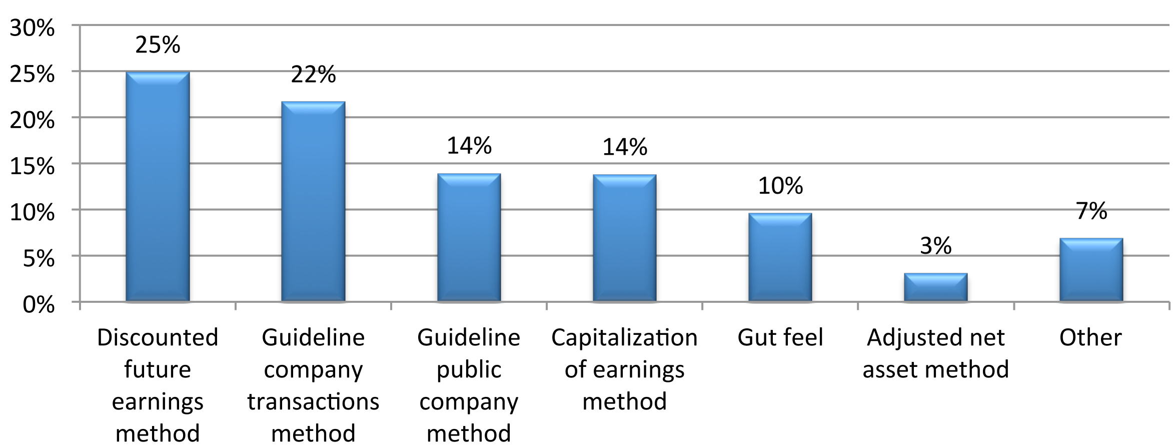
Average expected returns on non-buyout deals vary from 19.5 percent to 24.5 percent.

Table 11. General Characteristics – Non-Buyout Transactions (medians)

	$1M EBITDA	$5M EBITDA	$10M EBITDA	$25M EBITDA	$100M EBITDA	> $100M EBITDA
Number of investments	3	1	1	2	2.5	8
Average size of investment in million USD	1.5	2.5	7.5	15	60	35
Expected time to exit (years) (medians)	5	5	5	4	3.5	4.3
Equity as % of new capital structure	35%	35%	35%	35%	65%	45%
% of total equity purchased	15%	25%	25%	35%	45%	45%
Average deal multiple (multiple of EBITDA)	4.3	5	5	7	7	7
Total expected returns (gross cash on cash pre-tax IRR)	24.5%	28.5%	25%	25%	21%	19.5%

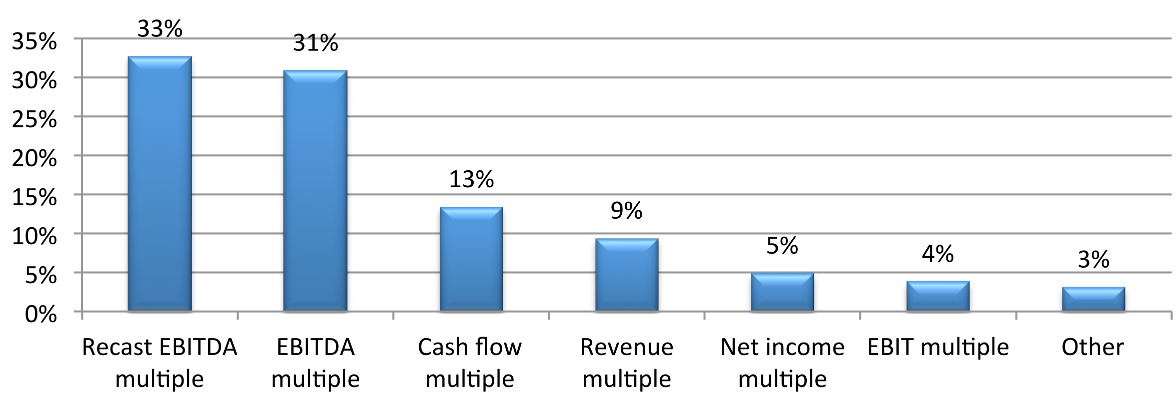
When valuing a business, approximately 25 percent of the weight is placed on discounted future earnings method.

Figure 22. Usage of Valuation Approaches



The weights of the various multiple methods used by respondents when valuing privately-held businesses included 33 percent for recast (adjusted) EBITDA multiple and 31 percent for EBITDA multiple.

Figure 23. Usage of Multiple Methods



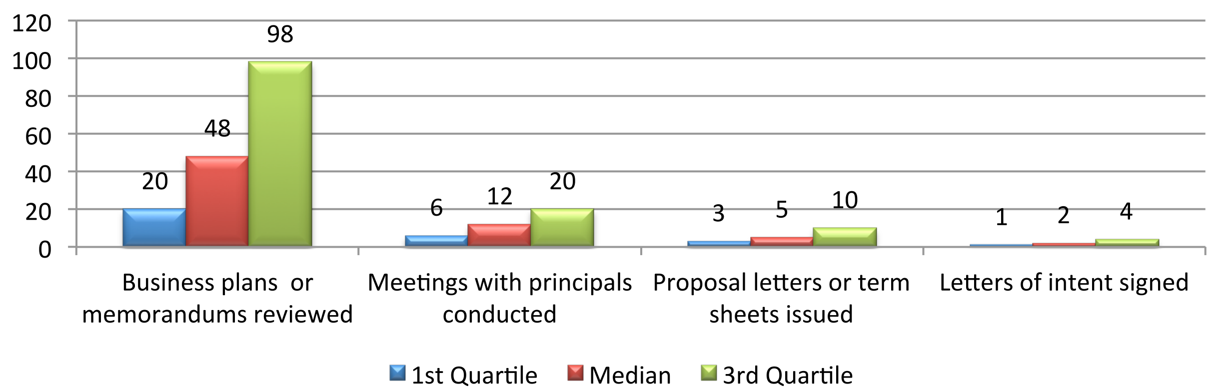
Deal multiples vary from 2.8 to 7.5, the highest multiples are indicated in consumer goods and services.

Table 12. Deal Multiples Among Industries (medians)

	$1M EBITDA	$5M EBITDA	$10M EBITDA	$15M EBITDA	$25M EBITDA	**Average**
Manufacturing	5.5	5.5	5.5	6.8	n/a	**5.8**
Construction & engineering	4	4.3	n/a	n/a	n/a	**4.2**
Consumer goods & services	6.5	6.5	7.5	7.5	7.5	**7.1**
Wholesale & distribution	3.5	3.5	4.5	7	n/a	**4.6**
Business services	4.8	5	5	7.3	7.5	**5.9**
Basic materials & energy	2.8	4	n/a	4.5	n/a	**3.8**
Average	**4.5**	**4.8**	**5.6**	**6.6**	**7.5**	**5.8**

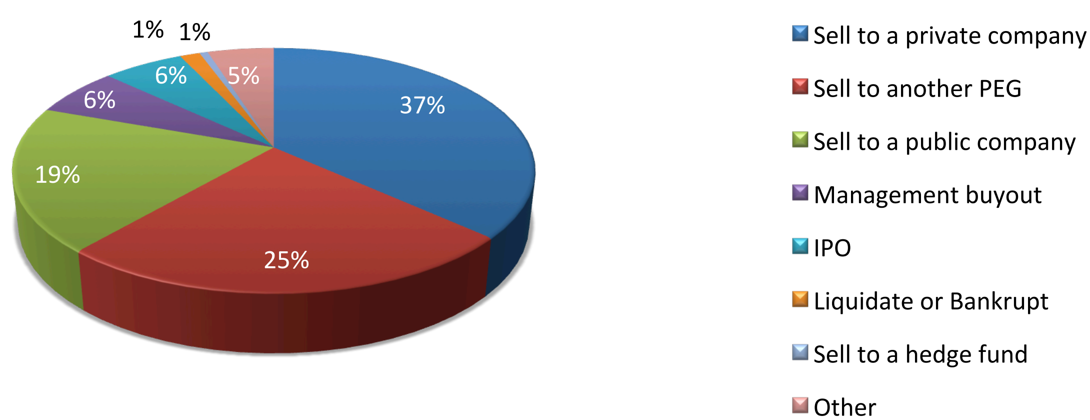
Respondents reported on items required to close one deal.

Figure 24. Items Required to Close One Deal



Respondents reported exit strategies that include selling to a private company (37 percent), selling to another private equity group (25 percent) and selling to a public company (21 percent).

Figure 25. Exit Plans for Portfolio Companies



Most of the respondents believe the number of companies "worthy of financing" exceeds "capital available" for the companies with less than $10M in EBITDA;whereas, for the larger companies, "capital available" exceeds the number of companies "worthy of financing."

Table 13. The Balance of Available Capital with Quality Companies for the Following Size

	Companies worthy of financing GREATLY exceed capital available	Companies worthy of financing exceed capital available	General balance	Capital available exceeds companies worthy of financing	Capital available GREATLY exceeds companies worthy of financing	**Score (-2 to 2)**
$1M EBITDA	26%	36%	15%	15%	8%	**-0.6**
$5M EBITDA	10%	33%	21%	23%	13%	**-0.1**
$10M EBITDA	0%	22%	30%	30%	19%	**0.5**
$15M EBITDA	0%	11%	35%	27%	27%	**0.7**
$25M EBITDA	0%	14%	22%	38%	27%	**0.8**
$50M EBITDA	0%	11%	20%	40%	29%	**0.9**
$100M EBITDA	0%	15%	15%	35%	35%	**0.9**
> $100M EBITDA	3%	12%	21%	30%	33%	**1.1**

Relative to 12 months ago, respondents indicated increases in demand for private equity, quality of companies seeking investment, amount of non-control investments, and deal multiples. They also reported a decrease in expected returns on new investments, increase in expected investment holding period, and improved general business conditions.

Table 14. General Business and Industry Assessment: Today versus 12 Months Ago

	Decreased significantly	Decreased slightly	Stayed about the same	Increased slightly	Increased significantly	% increase	% decrease	**Net increase/ decrease**
Demand for private equity	0%	8%	49%	22%	20%	43%	8%	**35%**
Quality of companies seeking investment	2%	16%	33%	39%	10%	49%	18%	**31%**
Average investment size	0%	16%	43%	39%	2%	41%	16%	**24%**
Non-control investments	0%	8%	50%	24%	18%	42%	8%	**34%**
Expected investment holding period	0%	11%	51%	26%	13%	38%	11%	**28%**
Deal multiples	0%	6%	31%	57%	6%	63%	6%	**57%**
Exit opportunities	0%	15%	38%	28%	19%	47%	15%	**32%**
Expected returns on new investments	2%	22%	53%	16%	6%	22%	24%	**-2%**
Value of portfolio companies	0%	6%	19%	56%	19%	75%	6%	**69%**
General business conditions	2%	17%	33%	40%	8%	48%	19%	**29%**
Size of private equity industry	0%	29%	37%	31%	4%	35%	29%	**6%**

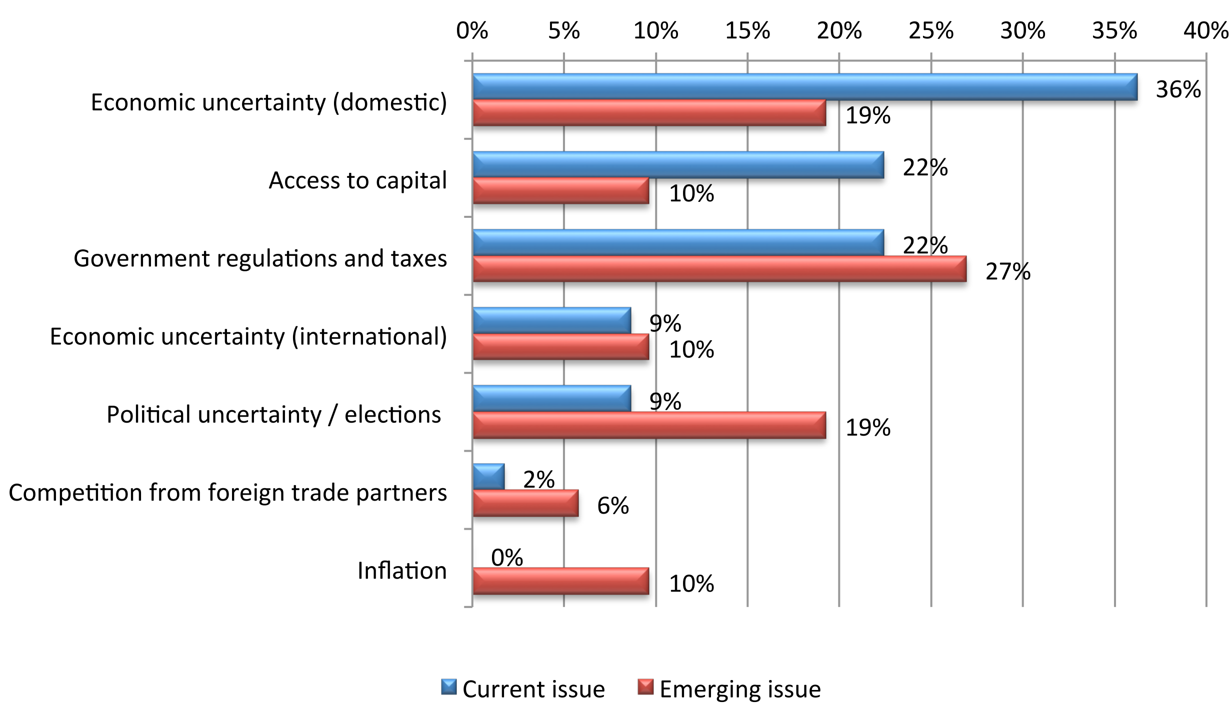
Respondents expect further increases in demand for private equity, deal multiples, value of portfolio companies, and improving general business conditions.

Table 15. General Business and Industry Assessment Expectations over the Next 12 Months

	Decrease significantly	Decrease slightly	Stay about the same	Increase slightly	Increase significantly	% increase	% decrease	**Net increase/ decrease**
Demand for private equity	0%	0%	45%	45%	10%	55%	0%	**55%**
Quality of companies seeking investment	0%	10%	39%	45%	6%	51%	10%	**41%**
Average investment size	0%	2%	55%	37%	6%	43%	2%	**41%**
Non-control investments	0%	3%	60%	33%	5%	38%	3%	**35%**
Expected investment holding period	0%	10%	60%	29%	0%	29%	10%	**19%**
Deal multiples	0%	10%	53%	35%	2%	37%	10%	**27%**
Exit opportunities	0%	6%	52%	33%	8%	42%	6%	**35%**
Expected returns on new investments	0%	12%	69%	12%	6%	18%	12%	**6%**
Value of portfolio companies	0%	4%	33%	53%	10%	63%	4%	**59%**
General business conditions	0%	12%	43%	41%	4%	45%	12%	**33%**
Size of private equity industry	0%	24%	45%	29%	2%	31%	24%	**6%**

Respondents believe domestic economic uncertainty is the most important issue facing privately-held businesses today.

Figure 23. Issues Facing Privately-Held Businesses



BANK AND ASSET-BASED LENDING SURVEY INFORMATION

There were 64 responses to the banks survey with commercial banks making up 49 percent in terms of individual lending function. Over 61 percent of respondents believe that general business conditions will improve over the next 12 months and over 49 percent said demand for loans will increase. Other key findings include:

- Over the last 12 months respondents were seeing decreased credit quality of borrowers applying for credit, with increase in demand for business loans, leverage multiples and focus on collateral as backup means of payment.

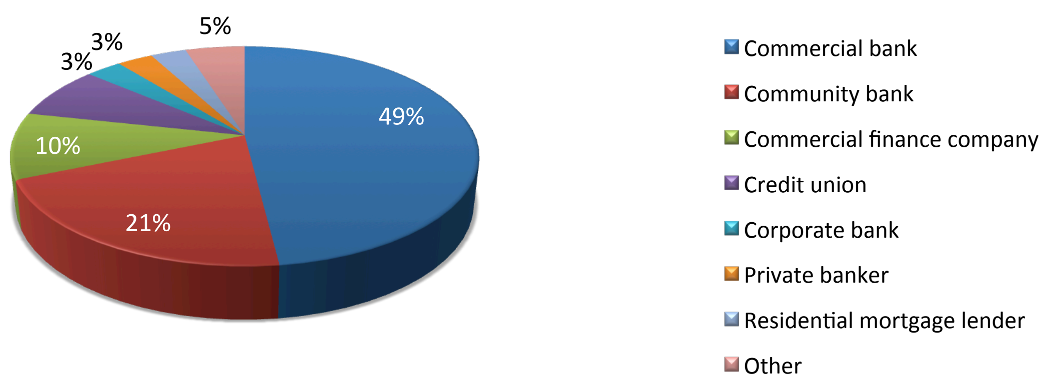
- Respondents also expect flat lending capacity of banks, increases in due diligence efforts, credit quality of borrowers, average loan size and loan maturity, and further pricing compression.

- Currently, 41 percent lenders see government regulations and taxes as the top issue facing privately-held businesses.

Operational and Assessment Characteristics

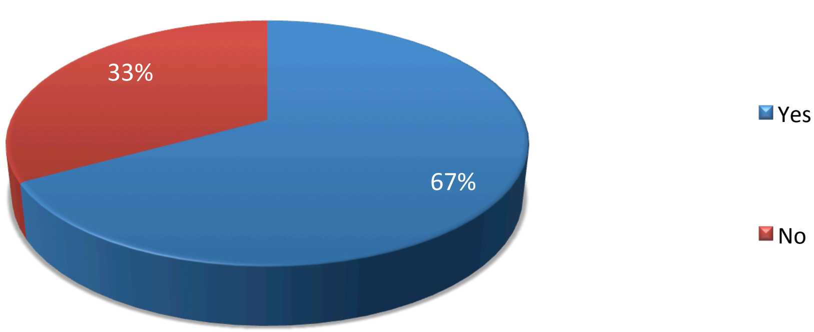
Respondents reported on the type of entity that best describes their lending function.

Figure 26. Description of Lending Entity



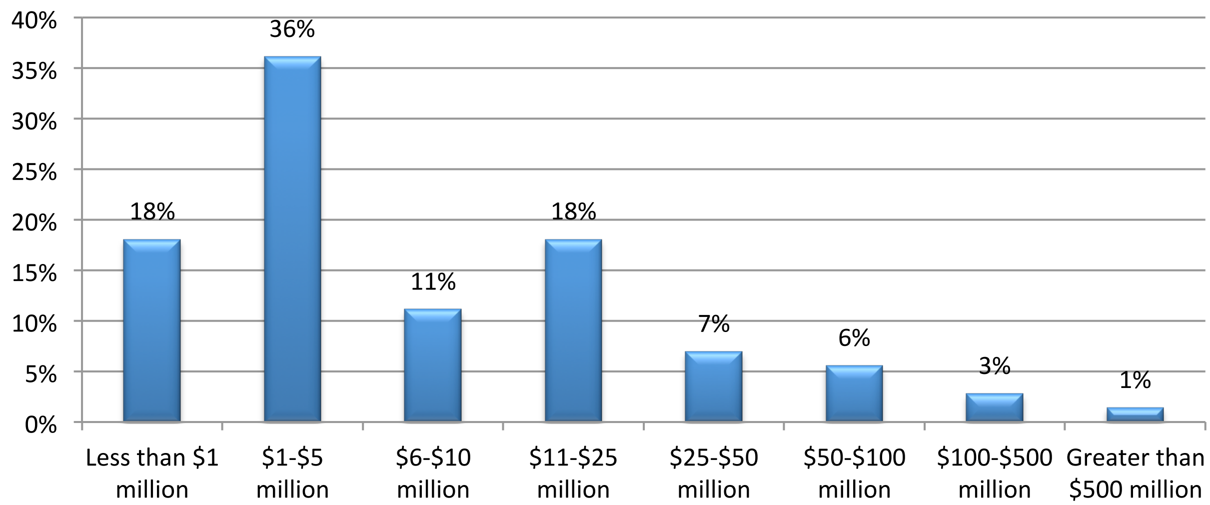
The majority (67 percent) report participating in government loan programs.

Figure 27. Participation in Government Loan Programs



The largest concentration of loan sizes was between $1 million and $5 million (36 percent).

Figure 28. Typical Investment Size



Respondents reported on all-in rates for various industries.

Table 16. All-in Rates by Loan Size and Industry

	$1M	$5M	$10M	$25M	$50M	$100M
Manufacturing	5.0%	4.8%	3.5%	3.0%	n/a	n/a
Consumer goods and services	5.5%	5.0%	4.0%	3.0%	n/a	n/a
Wholesale & distribution	4.8%	5.0%	4.0%	3.0%	n/a	n/a
Business services	4.5%	5.0%	4.0%	n/a	n/a	n/a
Basic materials & energy	4.5%	4.5%	4.0%	3.0%	3.0%	n/a
Health care & biotech	4.8%	5.0%	4.0%	n/a	3.0%	n/a
Information technology	4.8%	5.0%	4.0%	4.0%	3.0%	n/a
Financial services	5.0%	5.0%	4.0%	n/a	3.0%	n/a

Table 17. All-in Rates by Loan Type

	$1M	$5M	$10M	$25M	$50M	$100M
Cash flow loan	5.5%	5.0%	4.3%	4.0%	3.5%	5.5%
Working capital loan	6.0%	5.0%	4.0%	4.0%	3.0%	6.0%
Equipment loan	4.3%	5.0%	4.3%	3.0%	4.0%	4.3%
Real estate loan	4.8%	5.0%	3.5%	3.0%	4.5%	4.8%
Typical Fixed-Rate Loan Term (months)	60	60	60	60	48	60

BANKS cont.

Senior leverage multiples are reported below for the various industries and EBITDA sizes.

Table 18. Senior Leverage Multiple by EBITDA Size

	$1M EBITDA	$5M EBITDA	$10M EBITDA	$25M EBITDA	$50M EBITDA	$50M+ EBITDA
Manufacturing	1.5	2.0	2.5	2.6	3.1	3.3
Construction & engineering	1.1	1.3	2.0	2.0	2.0	2.0
Consumer goods & services	1.3	1.8	2.5	2.5	2.6	3.0
Wholesale & distribution	1.5	1.8	2.5	2.5	2.5	2.8
Business services	1.3	1.5	2.3	2.6	2.8	2.8
Basic materials & energy	1.0	1.4	2.0	2.1	2.3	2.6
Healthcare & biotech	1.0	1.3	2.3	2.5	2.6	2.8
Information technology	1.8	1.9	1.9	2.5	2.9	2.9
Financial services	1.5	2.0	2.5	3.0	3.0	3.3
Media & entertainment	0.9	1.5	2.1	2.3	2.3	2.4
Average	**1.3**	**1.8**	**2.3**	**2.5**	**2.5**	**3.0**

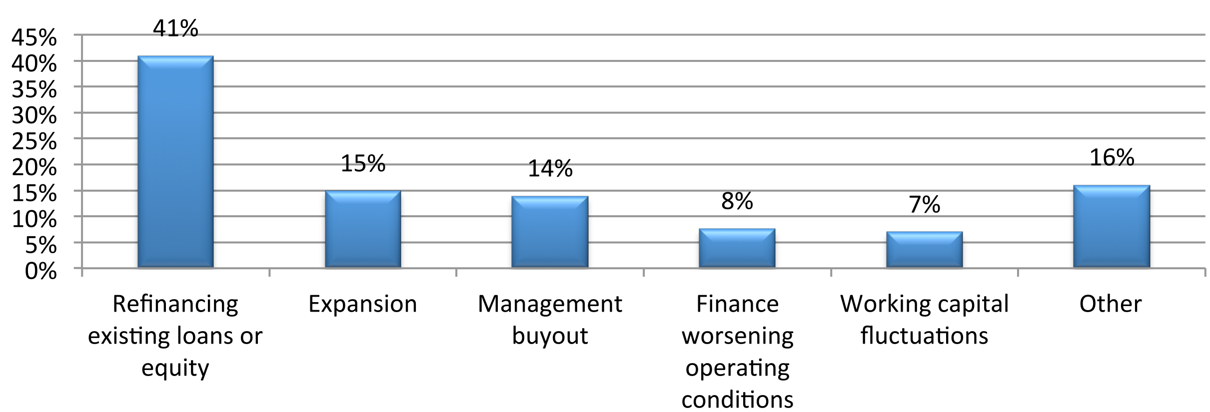
Various fees as reported by lenders are as follows.

Table 19. Fees Charged

	1st Quartile	Median	3rd Quartile	% Reporting
Closing fee	0.5	1.0	1.3	17%
Modification fee	0.3	0.5	0.7	12%
Commitment fee	0.5	0.9	1.1	14%
Underwriting fee	0.4	1.0	2.0	10%
Arrangement fee	0.5	1.0	1.5	11%
Prepayment penalty (yr 1)	1.0	3.0	3.0	13%
Prepayment penalty (yr 2)	1.0	2.0	2.8	12%
Unused line fee	0.2	0.5	0.5	12%

Refinancing was the most commonly described financing by buyers at 41 percent, followed by expansion at 15 percent.

Figure 29. Borrower Motivation to Secure Financing (past 12 months)



Total debt-service coverage ratio was the most important factor when deciding whether to invest or not.

Table 20. Importance of Financial Evaluation Metrics

	Unimportant	Of little importance	Moderately important	Important	Very important	Score (1 to 5)
Current ratio	16%	26%	32%	21%	5%	2.7
Senior DSCR or FCC ratio	5%	5%	9%	9%	73%	4.4
Total DSCR or FCC ratio	0%	0%	9%	18%	73%	4.6
Senior debt-to-cash flow	5%	16%	26%	16%	37%	3.6
Total debt-to-cash flow	0%	11%	32%	26%	32%	3.8
Debt-to-net worth	10%	14%	38%	14%	24%	3.3

Table 21. Financial Evaluation Metrics Average Data

	Average borrower data	Limit not to be exceeded
Current ratio	1.3	1.0
Senior DSCR or FCC ratio	1.5	1.2
Total DSCR or FCC ratio	1.3	1.2
Senior debt-to-cash flow	2.3	3.0
Total debt-to-cash flow	3.3	4.0
Debt-to-net worth	3.8	4.5

Respondents reported on the percentage of loans (by size) that require personal guarantee and collateral.

Table 22. Personal Guarantee and Collateral Percentage of Occurrence by Size of Loan (%)

	$1M loan	$5M loan	$10M loan	$25M loan	$50M loan	$100M loan
Personal guarantee	97%	95%	76%	75%	51%	51%
Collateral	100%	94%	83%	75%	72%	63%

Approximately 53 percent of cash flow applications were declined.

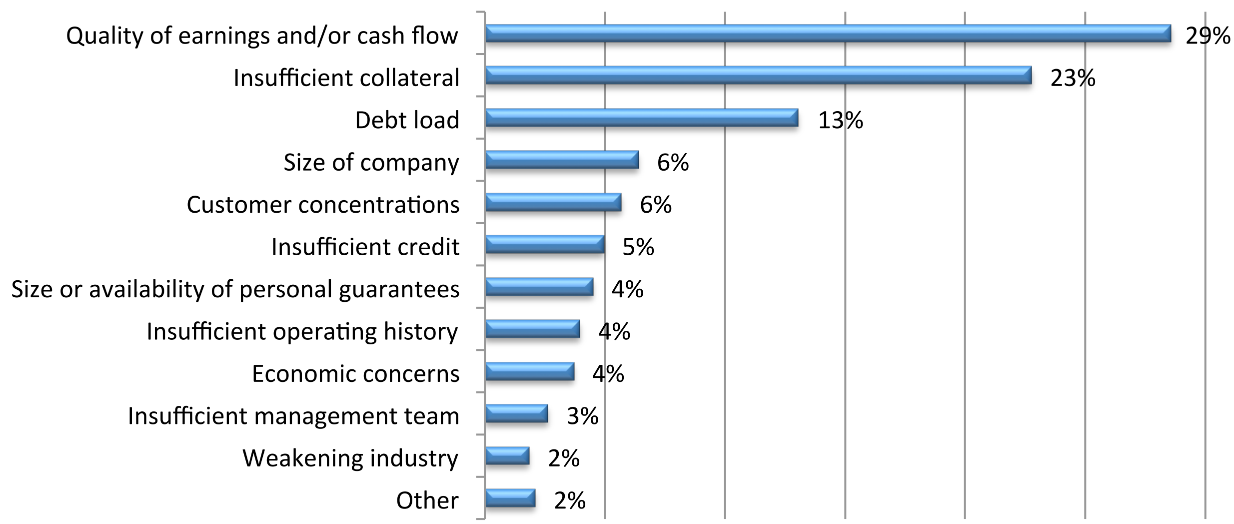
Table 23. Applications Data

	Reviewed	Offered	Booked	Declined
Cash flow based	662	55%	40%	37%
Collateral based	460	58%	28%	30%
Real estate	393	50%	21%	33%
Average	**505**	**55%**	**30%**	**34%**

BANKS cont.

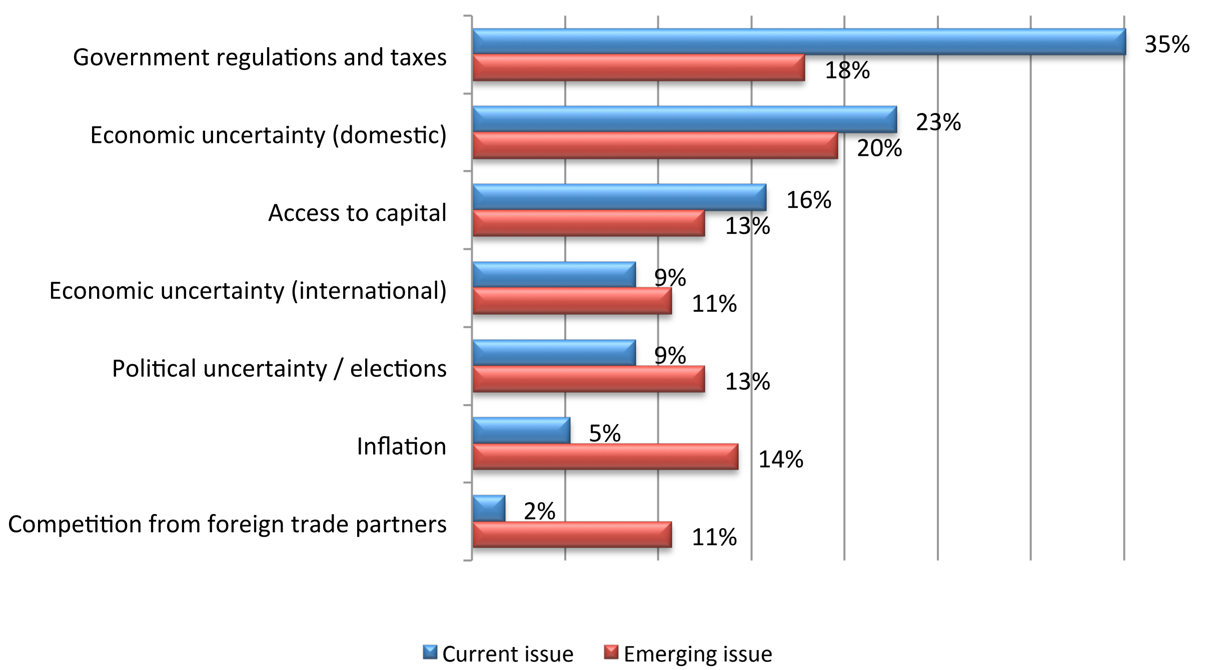
Approximately 29 percent of applications were declined due to poor quality of earnings and/or cash flow followed by 23 percent that were declined due to insufficient collateral.

Figure 30. Reason for Declined Loans



Respondents believe government regulations and taxes is the most important issue facing privately-held businesses today.

Figure 31. Issues Facing Privately-Held Businesses



BANKS cont.

Respondents indicated increases in almost all general business characteristics except general underwriting standards, average loan size and business conditions.

Table 24. General Business and Industry Assessment: Today versus 12 Months Ago

	Decreased significantly	Decreased slightly	Stayed about the same	Increased slightly	Increased significantly	% increase	% decrease	**Net increase/ decrease**
Demand for business loans (applications)	14%	14%	22%	22%	28%	50%	28%	**22%**
General underwriting standards	0%	25%	58%	13%	4%	17%	25%	**-8%**
Credit quality of borrowers applying for credit	3%	16%	39%	34%	8%	42%	18%	**24%**
Loans outstanding	0%	0%	50%	50%	0%	50%	0%	**50%**
Number/ tightness of financial covenants	0%	8%	42%	45%	5%	50%	8%	**42%**
Due diligence efforts	0%	8%	71%	18%	3%	21%	8%	**13%**
Average loan size	0%	18%	68%	9%	5%	14%	18%	**-5%**
Average loan maturity (months)	0%	4%	78%	13%	4%	17%	4%	**13%**
Percent of loans with personal guarantees	4%	50%	29%	17%	0%	17%	54%	**-38%**
Percent of loans requiring collateral	0%	51%	43%	5%	0%	5%	51%	**-46%**
Size of interest rate spreads (pricing)	0%	0%	55%	45%	0%	45%	0%	**45%**
Loan fees	0%	5%	50%	45%	0%	45%	5%	**40%**
Standard advance rates	0%	14%	62%	24%	0%	24%	14%	**10%**
Senior leverage multiples	8%	8%	46%	31%	8%	38%	15%	**23%**
Total leverage multiples	0%	5%	27%	55%	14%	68%	5%	**64%**
Focus on collateral as backup means of payment	6%	8%	47%	31%	8%	39%	14%	**25%**
SBA lending	0%	14%	45%	36%	5%	41%	14%	**27%**
Lending capacity of bank	0%	14%	0%	43%	43%	86%	14%	**71%**
General business conditions	13%	25%	38%	25%	0%	25%	38%	**-13%**
Appetite for risk	8%	25%	58%	8%	0%	8%	33%	**-25%**

Respondents expect further increases in all business characteristics except size of interest spreads (pricing), loan fees, and percent of loans with personal guarantees.

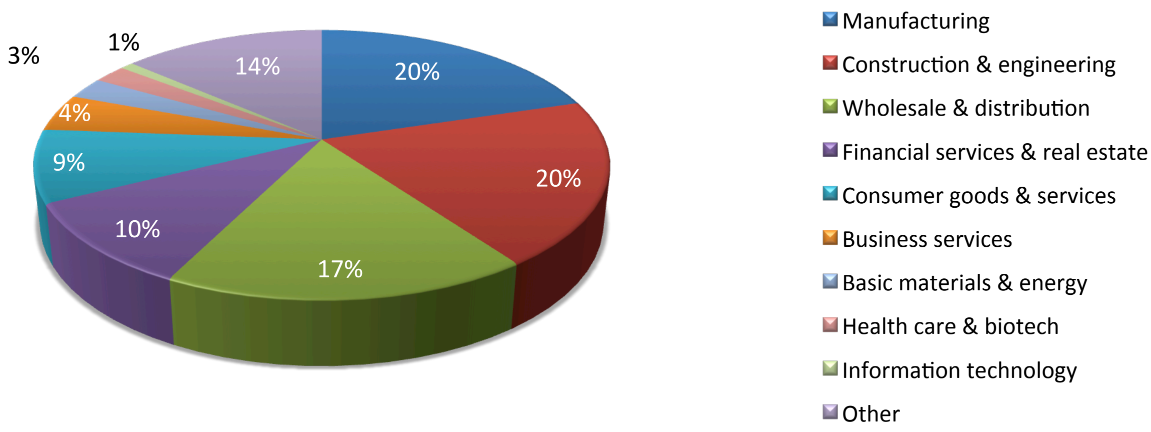
Table 25. General Business and Industry Assessment Expectations over the Next 12 Months

	Decrease significantly	Decrease slightly	Stay about the same	Increase slightly	Increase significantly	% increase	% decrease	**Net increase/ decrease**
Demand for business loans (applications)	0%	8%	35%	35%	22%	57%	8%	**49%**
General underwriting standards	0%	13%	63%	25%	0%	25%	13%	**13%**
Credit quality of borrowers applying for credit	0%	11%	58%	29%	3%	32%	11%	**21%**
Due diligence efforts	0%	0%	79%	21%	0%	21%	0%	**21%**
Average loan size	0%	5%	47%	47%	0%	47%	5%	**42%**
Average loan maturity (months)	0%	3%	78%	19%	0%	19%	3%	**16%**
Percent of loans with personal guarantees	0%	14%	82%	5%	0%	5%	14%	**-9%**
Percent of loans requiring collateral	0%	9%	83%	9%	0%	9%	9%	**0%**
Size of interest rate spreads (pricing)	0%	38%	33%	29%	0%	29%	38%	**-8%**
Loan fees	0%	24%	62%	14%	0%	14%	24%	**-11%**
Senior leverage multiples	0%	5%	65%	30%	0%	30%	5%	**25%**
Total leverage multiples	0%	5%	67%	29%	0%	29%	5%	**24%**
Focus on collateral as backup means of payment	0%	10%	71%	14%	5%	19%	10%	**10%**
SBA lending	7%	7%	64%	14%	7%	21%	14%	**7%**
Lending capacity of bank	0%	4%	30%	52%	13%	65%	4%	**61%**
General business conditions	3%	24%	29%	42%	3%	45%	26%	**18%**
Appetite for risk	0%	17%	43%	35%	4%	39%	17%	**22%**

Asset-Based Lending Specific Characteristics

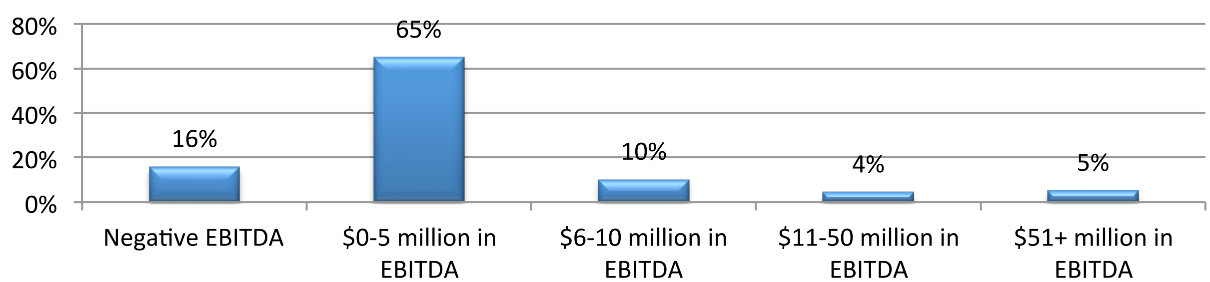
According to respondents approximately 20 percent of asset-based loans were issued for manufacturing companies.

Figure 32. Industries Served by Asset-Based Lenders



Approximately 81 percent of the companies that booked asset-based loans in the last 12 months had EBITDA size less than $5 million.

Figure 33. Typical EBITDA Sizes for Companies Booked



Respondents reported on all-in rates by type and size of current booked loans and the results are reported below.

Table 26. All-in Rates on Current Asset-Based Loans (medians)

	Accounts Receivable	Inventory	Equipment	Real estate	Working capital	Typical Fixed-Rate Loan Term (months)
Less than $1 million	8.3%	9.5%	16.0%	21.0%	15.0%	36
$1-5 million	8.2%	5.8%	13.5%	19.0%	13.0%	24
$5-$10 million	6.9%	4.8%	11.0%	16.0%	9.5%	24
$10-25 million	6.9%	2.3%	5.8%	14.0%	9.5%	24

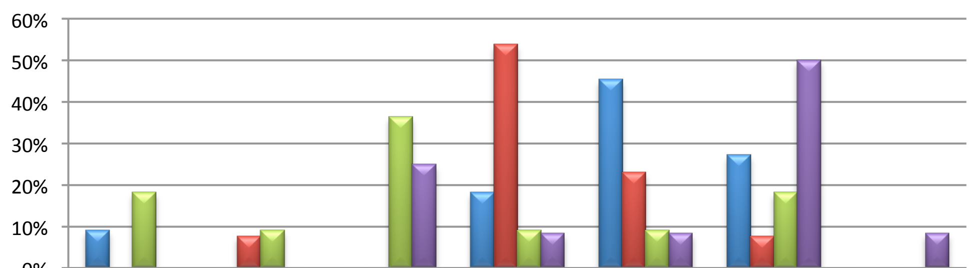
Respondents reported on standard advance rates and the results are reflected below.

Table 27. Standard Advance Rate (or LTV ratio) for Assets (%)

	Typical Loan			Upper Limit		
	1st quartile	**Median**	**3rd quartile**	**1st quartile**	**Median**	**3rd quartile**
Marketable securities	50%	50%	50%	80%	85%	85%
Accounts receivable	80%	80%	85%	16%	28%	46%
Inventory - low quality	5%	20%	20%	25%	35%	45%
Inventory - intermediate quality	21%	28%	35%	50%	50%	65%
Inventory - high quality	43%	50%	60%	56%	75%	75%
Equipment	50%	70%	75%	58%	70%	73%
Real estate	58%	60%	65%	35%	50%	51%
Land	25%	40%	40%	n/a	n/a	n/a

Respondents reported on valuation standards used to estimate LTV ratios.

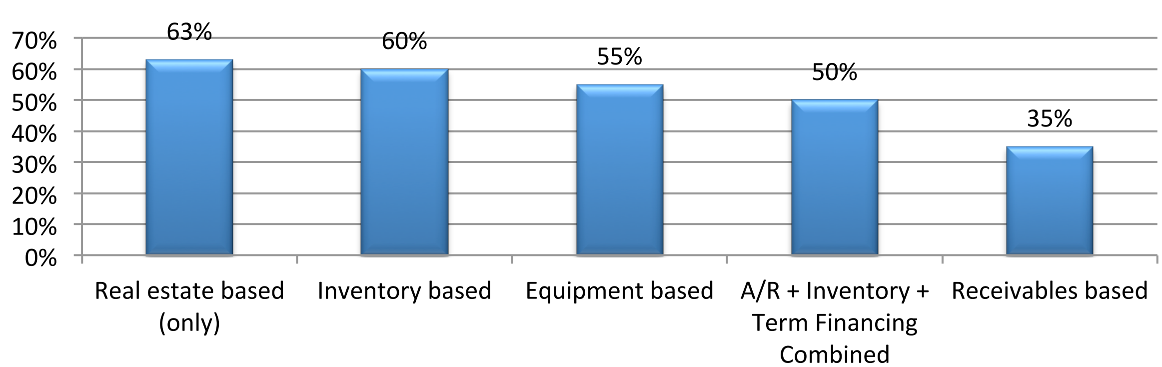
Figure 34. Valuation Standards Used to Estimate LTV Ratio



	Purchase price	Depreciated Value (Book)	Face value	Fair Market Value	Forced liquidation	Orderly liquidation	Other
Equipment	9%	0%	0%	18%	45%	27%	0%
Real estate	0%	8%	0%	54%	23%	8%	0%
Accounts Receivable	18%	9%	36%	9%	9%	18%	0%
Inventory	0%	0%	25%	8%	8%	50%	8%

According to respondents receivables-based loans had the smallest decline rate (35 percent) over the last 12 months.

Figure 35. Asset-Based Loans Decline Rate



MEZZANINE SURVEY INFORMATION

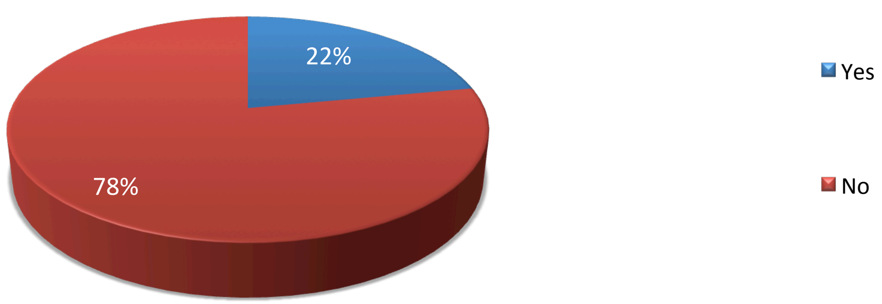
Of the 20 participants that responded to the mezzanine survey, 50 percent reported making deals over the past 12 months in the $10 million to $25 million range. Over 21 percent plan on investing in manufacturing companies over the next 12 months, followed by 18 percent in business services. Other key findings include:

- Relative to 12 months ago, respondents indicated increases in demand for mezzanine capital, leverage multiples, appetite for risk and flat general business conditions. They also reported decreases in general underwriting standards, warrant coverage, loan fees, and expected returns on new investments.
- Respondents expect further increase in demand for mezzanine capital, credit quality of borrowers, leverage multiples, and appetite for risk; relatively flat loan fees, expected returns on new investments, underwriting standards, and general business conditions; and decrease in warrant coverage.
- Approximately 38 percent of respondents believe access to capital is the most important issue facing privately-held businesses today.

Operational and Assessment Characteristics

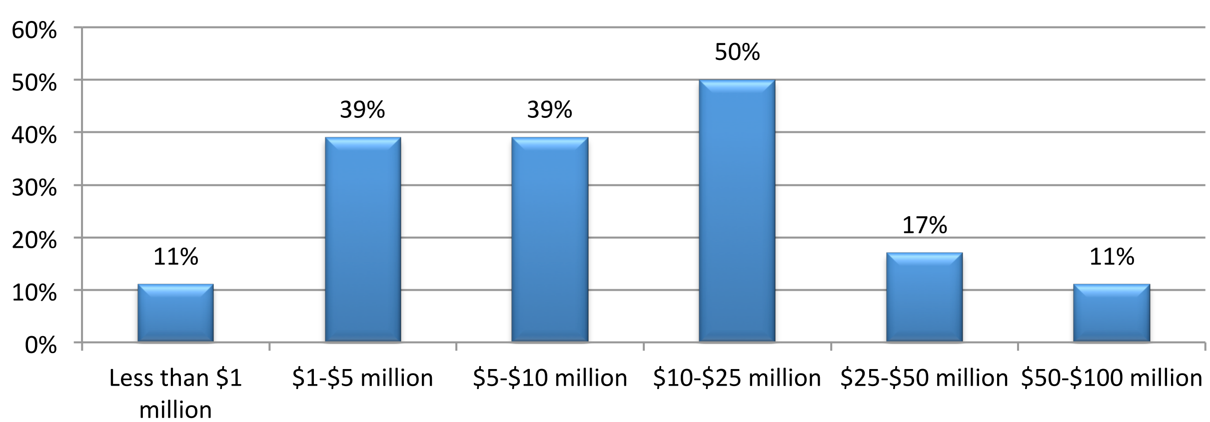
Approximately 22 percent of respondents are SBIC Firms.

Figure 36. SBIC (small business investment) Firms



The largest concentration of loan sizes was between $10 million and $25 million (50 percent).

Figure 37. Typical Investment Size



MEZZANINE cont.

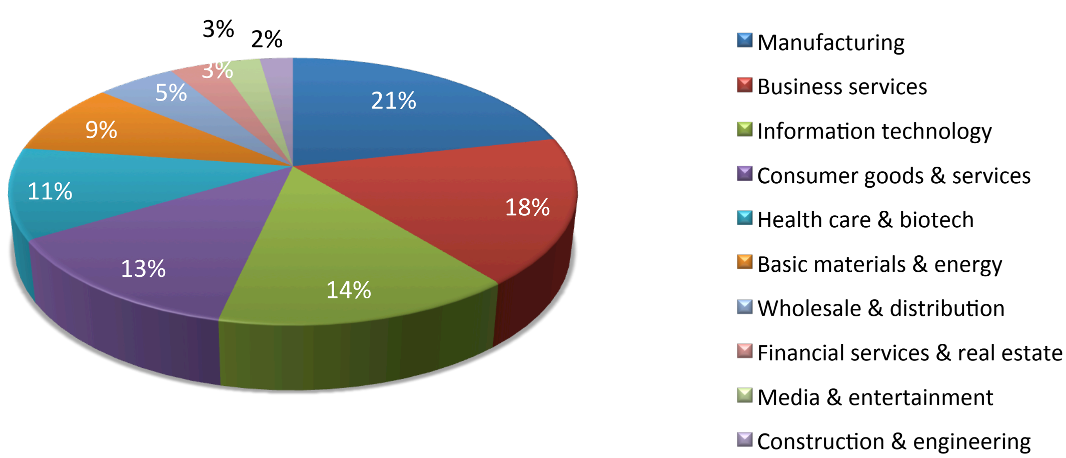
Respondents reported on business practices and the results are reflected below.

Table 28. Mezzanine Fund Data

	1st quartile	Median	3rd quartile
Vintage year (year in which first investment made)	2008	2011	2013
Size of fund ($ millions)	75	125	325
Targeted number of total investments	13	18	28
Target fund return (gross pretax cash on cash annual IRR %)	13.5%	17.5%	18.8%
Expected fund return (gross pretax cash on cash annual IRR %)	11.3%	17%	19.5%

The types of businesses respondents plan to invest in over next 12 months are very diverse with over 21 percent targeting manufacturing, followed by 18 percent who plan to invest in business services.

Figure 38. Type of Business for Investments Planned over Next 12 Months



Approximately 56 percent of respondents made 6 investments or more over the last 12 months.

Figure 39. Total Number of Investments Made in the Last 12 Months

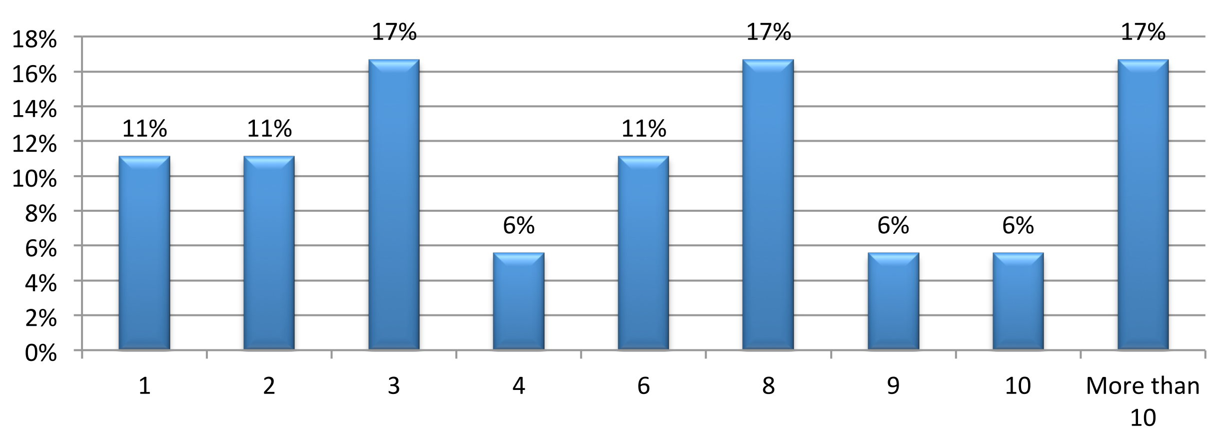
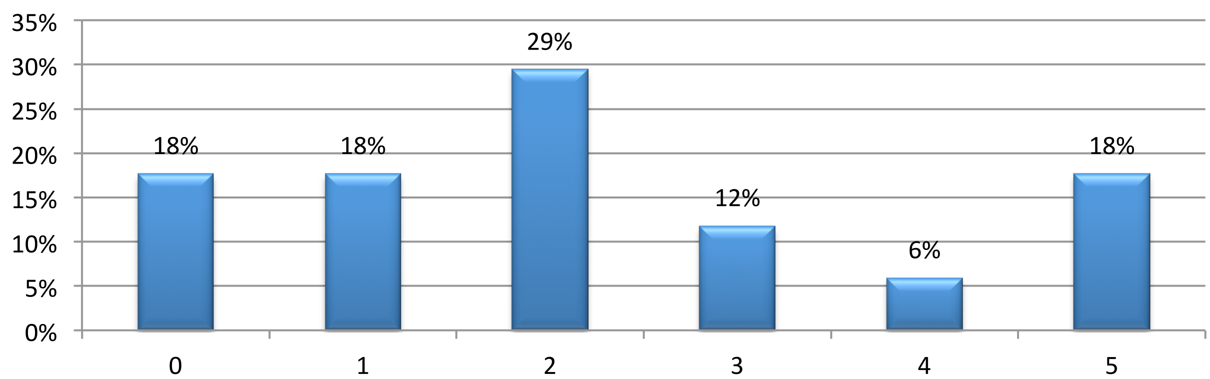


Figure 40. Number of Follow-on Investments Made in the Last 12 Months



Approximately 59 percent of respondents plan to make six investments or more over the next 12 months.

Figure 41. Number of Total Investments Planned over Next 12 Months

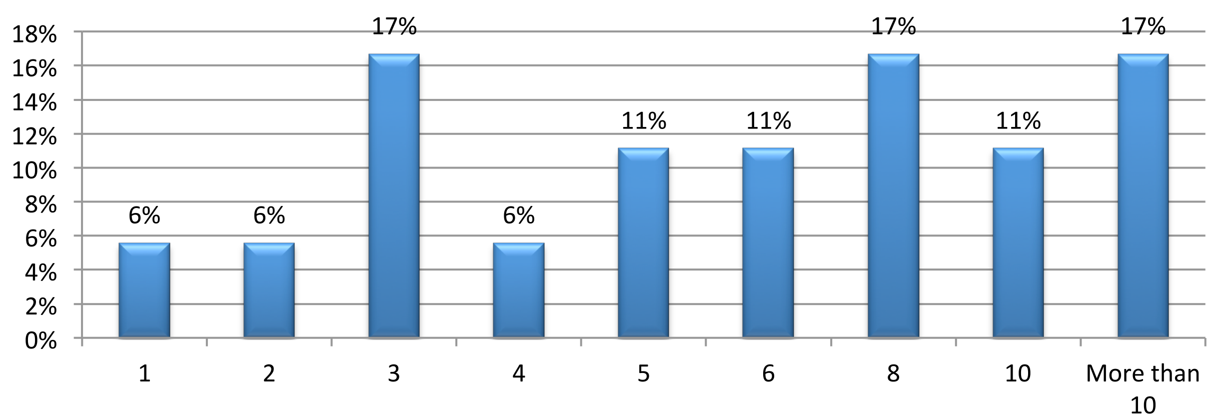
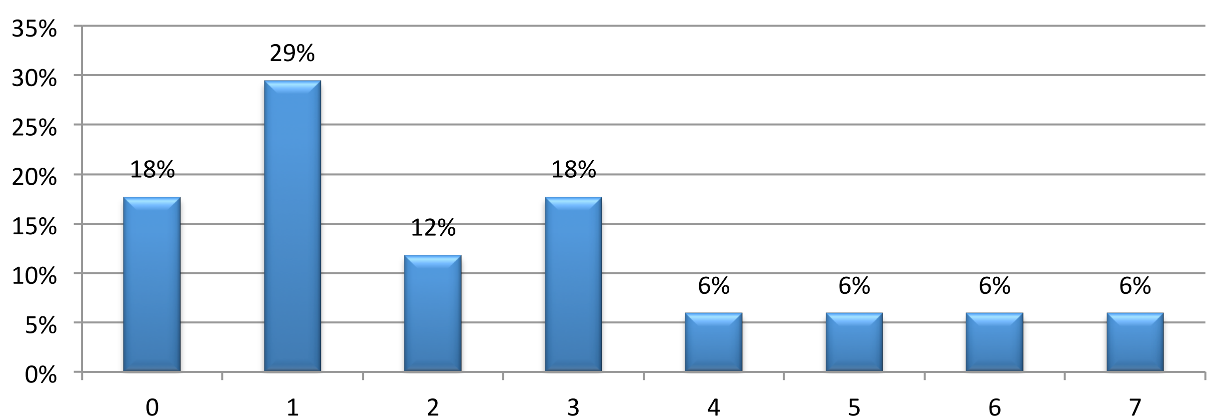


Figure 42. Number of Follow-on Investments Planned over Next 12 Months



MEZZANINE cont.

Results of responses to sponsored deals based on size of investee EBITDA are reported below.

Table 29. Sponsored Deals by EBITDA Size (medians)

	$1M - $5M EBITDA	$5M - $10M EBITDA	$10M - $25M EBITDA	$25M - $50M EBITDA	$50M+ EBITDA
% of deals with warrants	50%	50%	67%	n/a	n/a
Average loan terms (years)	5	4	5	6	5
Senior leverage ratio (multiple of EBITDA)	1	2	2.5	3.5	3.5
Total leverage ratio (multiple of EBITDA)	3	3	3.3	4.5	4.8
Average loan size ($ millions)	7.5	15	15	20	20
Cash interest rate	12%	11%	11%	11%	11%
PIK	0%	0%	2%	n/a	2%
Warrants expected return (IRR contribution)	5%	3%	2%	n/a	2%
Total expected returns (gross cash on pre-tax IRR)	21.0%	16.8%	14.2%	11.2%	9.4%

Results of responses to non-sponsored deals based on size of investee EBITDA are reported below.

Table 30. Non-Sponsored Deals by EBITDA Size (medians)

	$1M - $5M EBITDA	$5M - $10M EBITDA	$10M - $25M EBITDA	$25M - $50M EBITDA	$50M+ EBITDA
% of deals with warrants	100%	100%	100%	n/a	80%
Average loan terms (years)	4.5	4	4	6.3	6.3
Senior leverage ratio (multiple of EBITDA)	2	2	2	2.5	2.5
Total leverage ratio (multiple of EBITDA)	2.8	3	3	3.3	3.3
Average loan size ($ millions)	0.5	4	7.5	8	8
Cash interest rate	11%	11%	9%	6%	6%
PIK	1%	1%	1%	n/a	2%
Warrants expected return (IRR contribution)	10%	8%	4%	n/a	n/a
Total expected returns (gross cash on pre-tax IRR)	18%	15%	15.0%	8.5%	8.5%

Financing growth was reported by 35 percent of respondents as a motivation to secure mezzanine funding, followed by acquisition loan at 27 percent.

Figure 43. Borrower Motivation to Secure Mezzanine Funding (past 12 months)

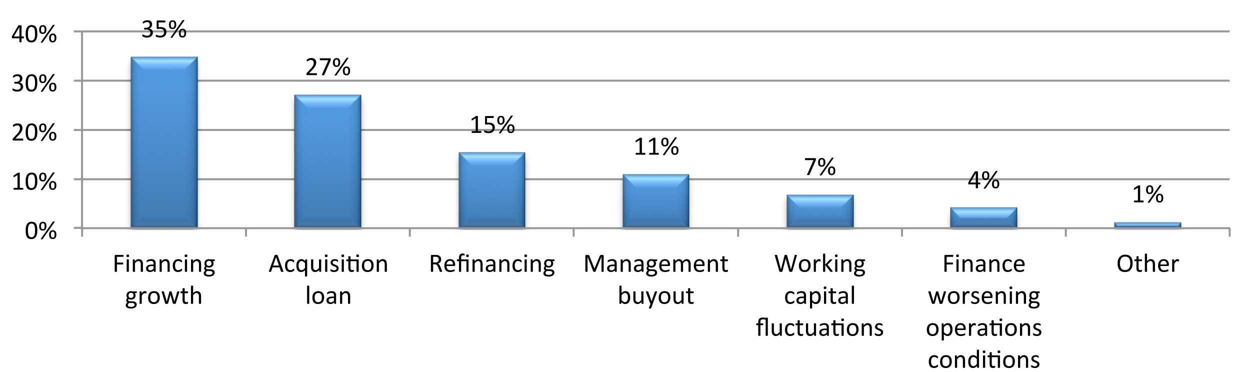
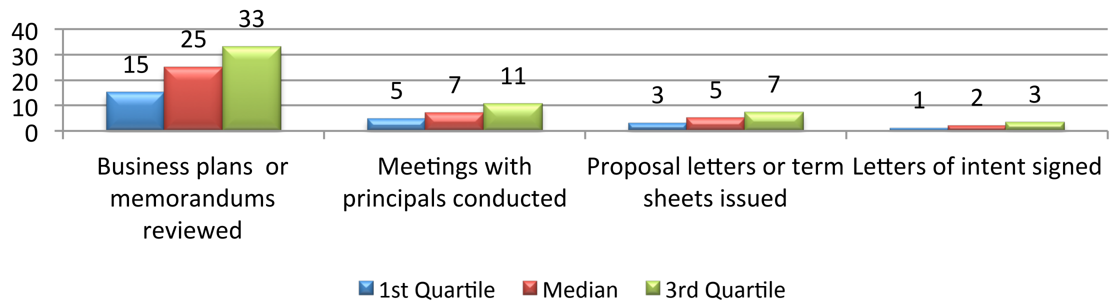


Figure 44. Items Required to Close One Deal



Total debt-to-cash flow ratio was the most important factor when deciding whether to invest or not, followed by total debt service coverage ratio.

Table 31. Importance of Financial Evaluation Metrics

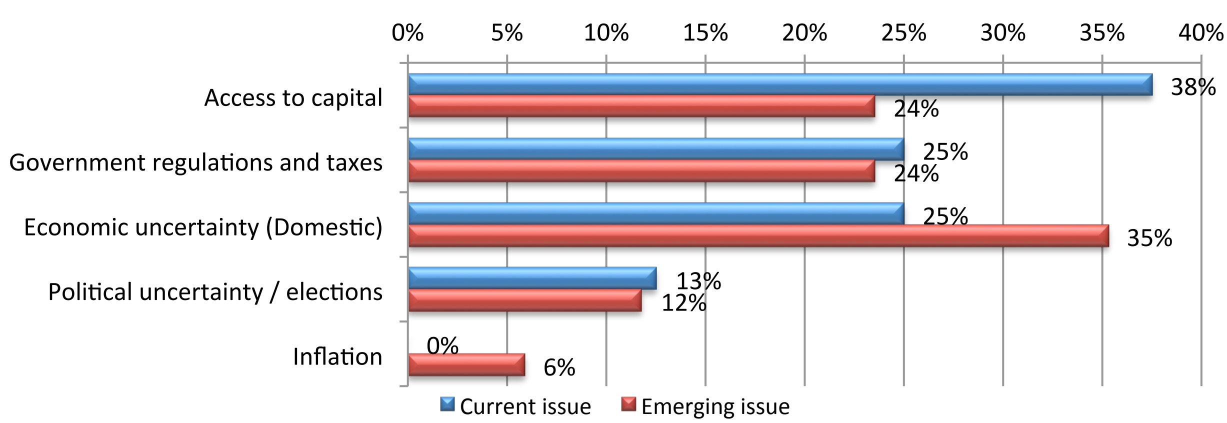
	Unimportant	Of little importance	Moderately important	Important	Very important	Score (1 to 5)
Senior DSCR or FCC ratio	0%	20%	27%	40%	13%	3.5
Total DSCR or FCC ratio	0%	13%	7%	53%	27%	3.9
Senior debt-to-cash flow ratio	0%	29%	14%	29%	29%	3.6
Total debt-to-cash flow ratio	0%	7%	21%	36%	36%	4

Table 32. Financial Evaluation Metrics Average Data

	Average borrower data	Limit not to be exceeded
Senior DSCR or FCC ratio	1.5	1.5
Total DSCR or FCC ratio	1.5	1.5
Senior debt to cash flow ratio	1.8	2.5
Total debt to cash flow ratio	2.7	3.6

Respondents believe access to capital is the most important issue facing privately-held businesses today.

Figure 45. Issues Facing Privately-Held Businesses



Relative to 12 months ago, respondents indicated increases in demand for mezzanine capital, leverage multiples and appetite for risk. They also reported decreases in general underwriting standards, warrant coverage, loan fees, and expected returns on new investments.

Table 33. General Business and Industry Assessment: Today versus 12 Months Ago

	Decreased significantly	Decreased slightly	Stayed about the same	Increased slightly	Increased significantly	% increase	% decrease	**Net increase/ decrease**
Demand for mezzanine capital	7%	13%	33%	33%	13%	47%	20%	**27%**
Credit quality of borrowers seeking investment	0%	27%	27%	40%	7%	47%	27%	**20%**
Average investment size	0%	13%	47%	33%	7%	40%	13%	**27%**
Average investment maturity (months)	0%	0%	86%	14%	0%	14%	0%	**14%**
General underwriting standards	7%	27%	47%	13%	7%	20%	33%	**-13%**
Warrant coverage	8%	38%	46%	8%	0%	8%	46%	**-38%**
PIK features	0%	15%	69%	15%	0%	15%	15%	**0%**
Loan fees	0%	20%	73%	7%	0%	7%	20%	**-13%**
Leverage multiples	0%	13%	40%	47%	0%	47%	13%	**33%**
Expected returns on new investments	0%	47%	27%	20%	7%	27%	47%	**-20%**
General business conditions	7%	13%	60%	20%	0%	20%	20%	**0%**
Appetite for risk	0%	13%	33%	53%	0%	53%	13%	**40%**

Respondents expect further increases in all business characteristics except warrant coverage, loan fees, and expected returns on new investments.

Table 34. General Business and Industry Assessment Expectations over the Next 12 Months

	Decrease significantly	Decrease slightly	Stay about the same	Increase slightly	Increase significantly	% increase	% decrease	**Net increase/ decrease**
Demand for mezzanine capital	0%	0%	33%	47%	20%	67%	0%	**67%**
Credit quality of borrowers seeking investment	0%	13%	47%	40%	0%	40%	13%	**27%**
Average investment size	0%	0%	53%	40%	7%	47%	0%	**47%**
Average investment maturity (months)	0%	13%	67%	20%	0%	20%	13%	**7%**
General underwriting standards	0%	13%	67%	20%	0%	20%	13%	**7%**
Warrant coverage	0%	31%	54%	15%	0%	15%	31%	**-15%**
PIK features	0%	8%	69%	23%	0%	23%	8%	**15%**
Loan fees	0%	13%	73%	13%	0%	13%	13%	**0%**
Leverage multiples	0%	7%	53%	40%	0%	40%	7%	**33%**
Expected returns on new investments	0%	13%	73%	13%	0%	13%	13%	**0%**
General business conditions	0%	7%	73%	13%	7%	20%	7%	**13%**
Appetite for risk	0%	13%	47%	33%	7%	40%	13%	**27%**

LIMITED PARTNER SURVEY INFORMATION

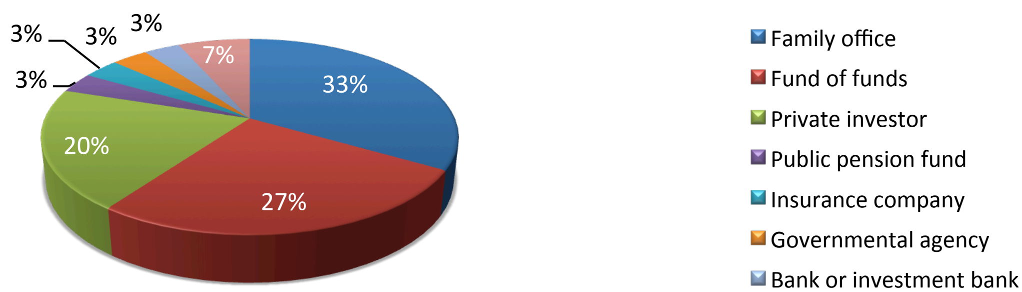
Approximately 21 percent of the 35 respondents in the limited partner survey reported distressed private equity as being the best risk/return trade-off investment class, another 21 percent reported direct investments as being the best risk/return trade-off investment class. When asked about which industry currently offers the best risk/return trade-off, 33 percent of respondents reported healthcare and biotech, followed by 19 percent reporting consumer goods and services. Other key findings include:

- On average respondents target to allocate 17 percent of their assets to growth private equity, 15 percent to real estate funds and 14 percent to buyout private equity. Respondents expect the highest returns of 16 percent from investments in venture capital, 13 percent from direct investments, and another 13 percent from investments in growth private equity.
- Respondents indicated increased allocation to private equity, direct investments and venture capital, and decreased allocation to all other alternative assets in the last 12 months. They also reported improved business conditions but relatively flat expected returns on new investments.
- Respondents also expect further increases in allocation to direct investments, private equity, and venture capital, improving business conditions and flat expected returns.

Operational and Assessment Characteristics

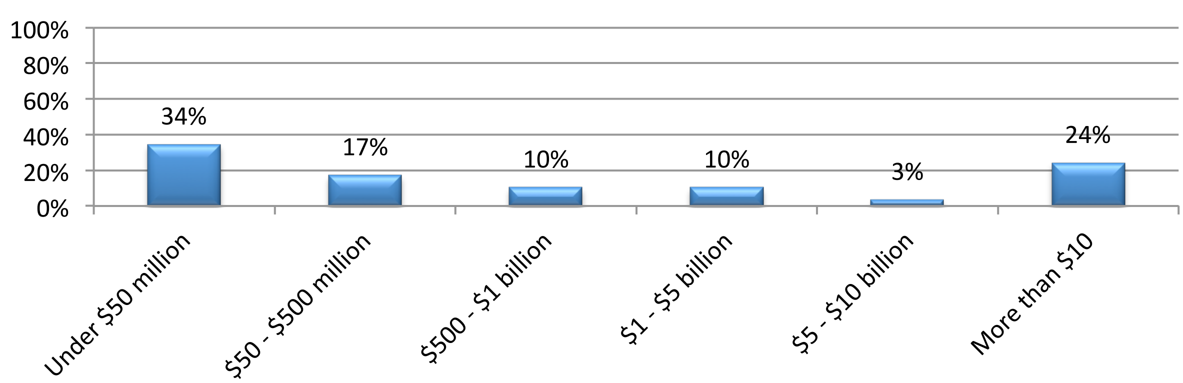
Approximately 33 percent of respondents indicated being family office followed by fund of funds (27 percent).

Figure 46. Entity Type



Approximately 34 percent of respondents reported their asset category being less than $50 million, while 17 percent were between $50 million and $500 million.

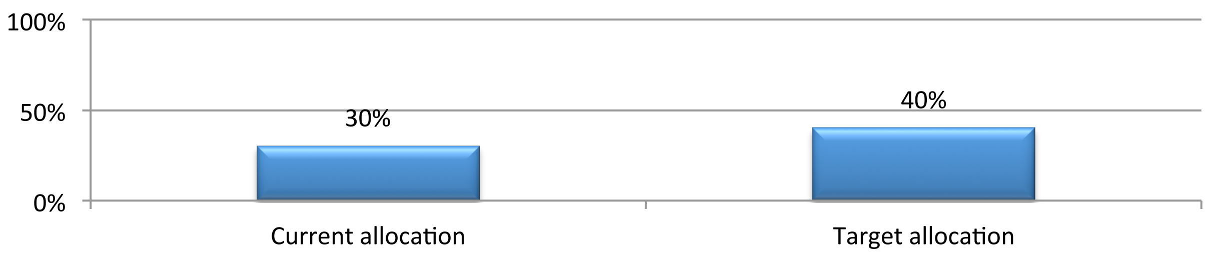
Figure 47. Assets under Management or Investable Funds



LP cont.

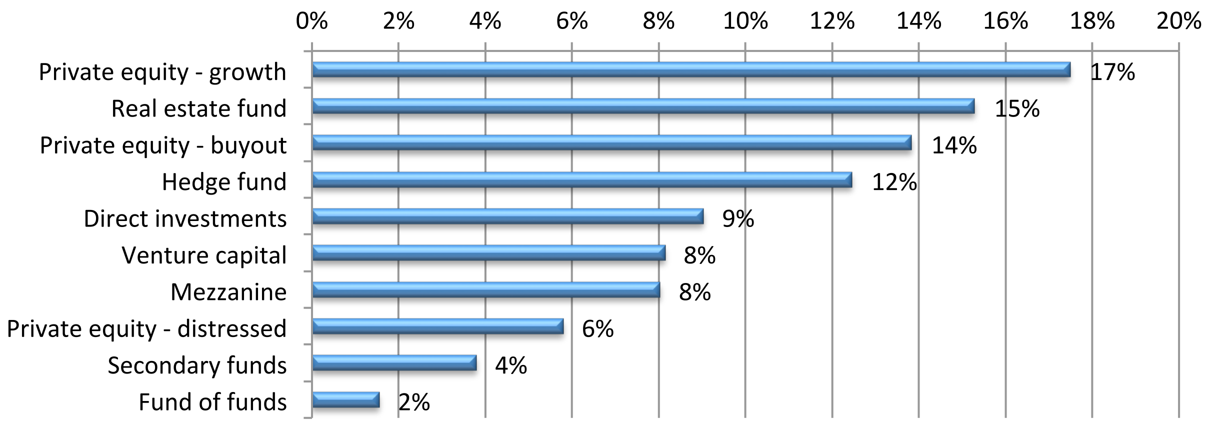
Respondents reported on their percent of total asset allocations for "Alternative Assets".

Figure 48. Current and Target Asset Allocations for "Alternative Assets" (% of total portfolio)



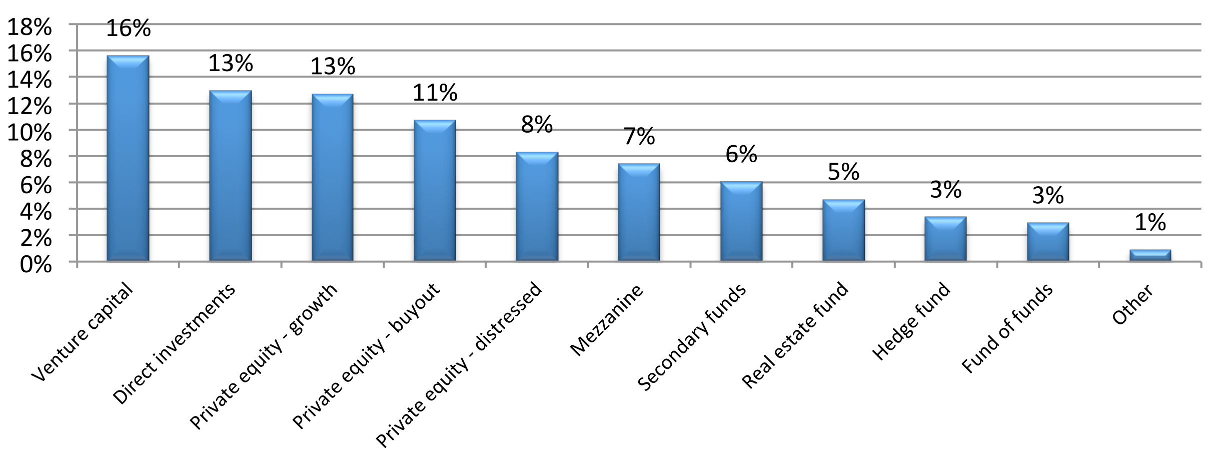
On average, respondents target to allocate 17 percent of their assets to growth private equity, 15 percent to real estate funds, and 14 percent to buyout private equity.

Figure 49. Current Target Asset Allocation



On average, respondents expect the highest returns from investments in venture capital, direct investments, and growth private equity.

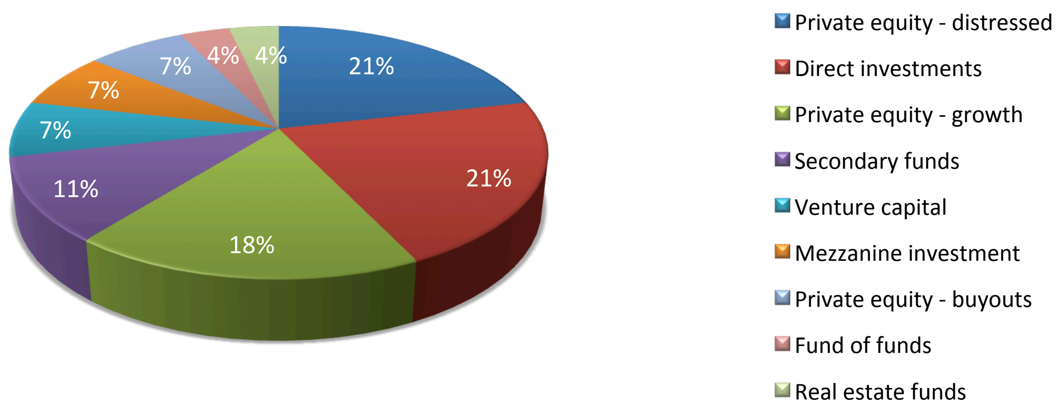
Figure 50. Annual Return Expectations for New Investments



LP cont.

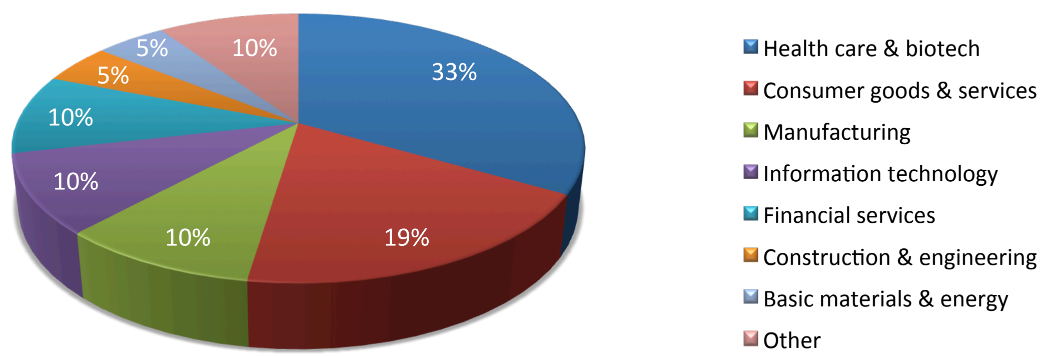
Approximately 21 percent of the 35 respondents in the limited partner survey reported distressed private equity as being the best risk/return trade-off investment class, another 21 percent reported direct investments as being the best risk/return trade-off investment class.

Figure 51. Assets with the Best Risk/Return Trade-off Currently



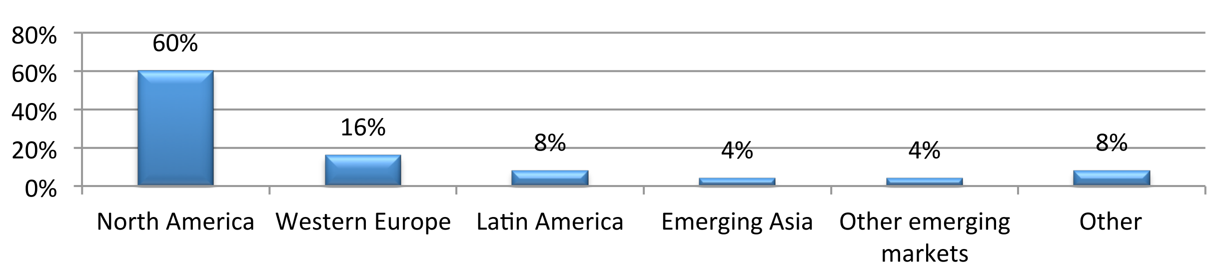
When asked about which industries currently offer the best risk/return tradeoffs, 33 percent of respondents reported health care & biotech, followed by 19 percent reporting consumer goods & services.

Figure 52. Industry with the Best Risk/Return



In regard to the geographic regions with the best risk/return trade-offs, 60 percent of respondents reported North America, followed by Western Europe (16 percent), and Latin America (8 percent).

Figure 53. Geographic Regions of the World Offering the Best Risk/Return Tradeoff Currently



LP cont.

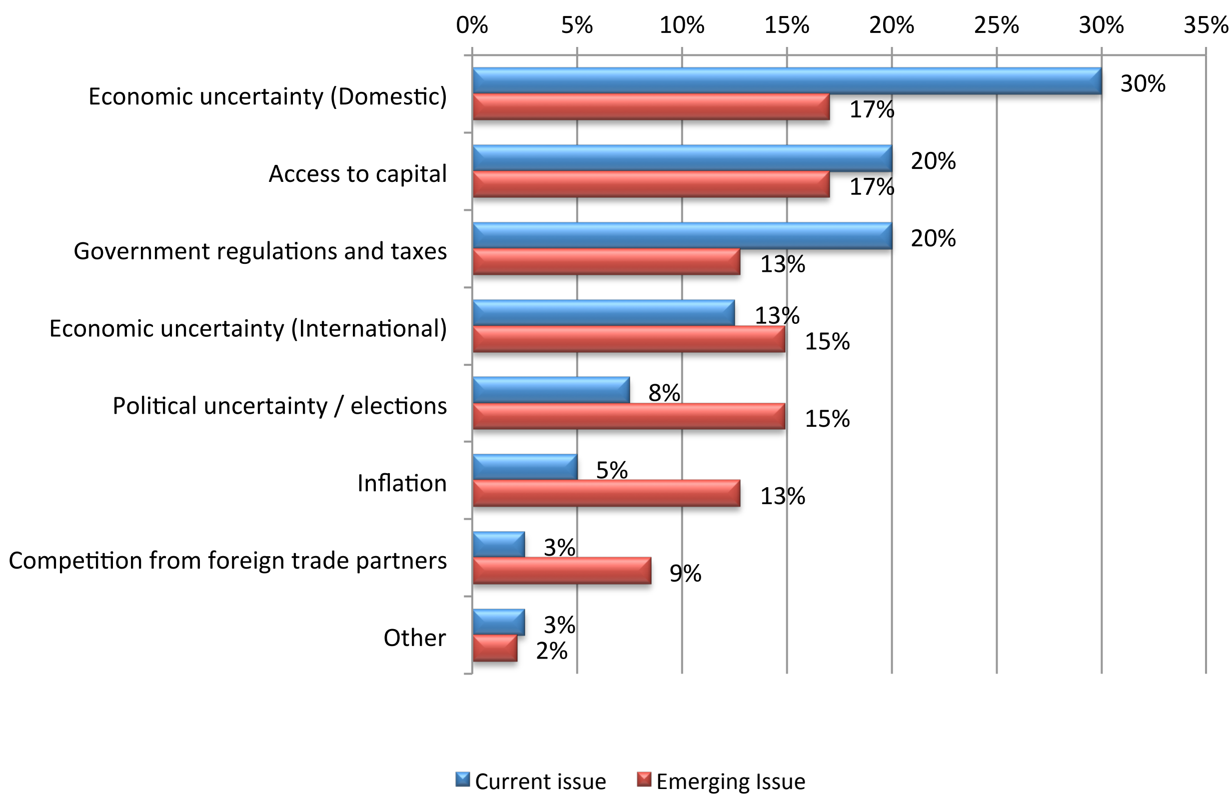
According to respondents, historical fund performance on all funds and specific strategy are the most important factors when evaluating investment followed by residual value of most recent fund.

Table 35. Importance of Factors When Evaluating

	Unimportant	Of little importance	Moderately important	Important	Very important	**Score (1 to 5)**
Historical fund performance on all funds	0%	0%	0%	69%	31%	**4.3**
Returned capital from most recent fund (Distribution to Paid-in or DPI)	0%	4%	27%	58%	12%	**3.8**
Residual value of most recent fund (Residual Value to Paid-in or RVPI)	0%	4%	42%	38%	15%	**3.7**
General partner	0%	4%	8%	54%	35%	**4.2**
Specific strategy	0%	4%	8%	42%	46%	**4.3**
Specific location	8%	35%	19%	27%	12%	**3.0**
Gut feel/instinct	0%	40%	28%	20%	12%	**3.0**

Respondents believe domestic economic uncertainty is the most important issue facing privately-held businesses today. Access to capital is indicated as the most important emerging issue.

Figure 54. Issues Facing Privately-Held Businesses



LP cont.

Respondents indicated increased allocation to private equity, direct investments and venture capital, and decreased allocation to all other alternative assets in the last 12 months. They also reported improved business conditions but relatively flat expected returns on new investments.

Table 36. General Business and Industry Assessment: Today versus 12 Months Ago

Characteristics	Decreased significantly	Decreased slightly	Stayed about the same	Increased slightly	Increased significantly	% increase	% decrease	**Net increase/ decrease**
Allocation to venture capital	4%	4%	77%	15%	0%	15%	8%	**8%**
Allocation to private equity	0%	4%	50%	31%	15%	46%	4%	**42%**
Allocation to mezzanine	17%	13%	46%	25%	0%	25%	29%	**-4%**
Allocation to hedge funds	11%	17%	56%	11%	6%	17%	28%	**-11%**
Allocation to secondary funds	9%	18%	59%	14%	0%	14%	27%	**-14%**
Allocation to real estate funds	15%	15%	45%	10%	15%	25%	30%	**-5%**
Direct investments	5%	9%	36%	36%	14%	50%	14%	**36%**
General business conditions	4%	13%	21%	50%	13%	63%	17%	**46%**
Expected returns on new capital deployed	0%	28%	40%	28%	4%	32%	28%	**4%**

Respondents also expect further increases in allocation to direct investments, private equity and venture capital, improving business conditions and flat expected returns.

Table 37. General Business and Industry Assessment Expectations over the Next 12 Months

Characteristics	Decrease significantly	Decrease slightly	Stay about the same	Increase slightly	Increase significantly	% increase	% decrease	**Net increase/ decrease**
Allocation to venture capital	4%	8%	65%	23%	0%	23%	12%	**12%**
Allocation to private equity	0%	4%	65%	27%	4%	31%	4%	**27%**
Allocation to mezzanine	5%	9%	68%	18%	0%	18%	14%	**5%**
Allocation to hedge funds	6%	6%	78%	11%	0%	11%	11%	**0%**
Allocation to secondary funds	0%	15%	60%	20%	5%	25%	15%	**10%**
Allocation to real estate funds	10%	14%	52%	14%	10%	24%	24%	**0%**
Direct investments	0%	0%	52%	43%	4%	48%	0%	**48%**
General business conditions	4%	17%	38%	42%	0%	42%	21%	**21%**
Expected returns on new capital deployed	0%	24%	52%	24%	0%	24%	24%	**0%**

VENTURE CAPITAL SURVEY INFORMATION

Of the 33 participants who responded to the venture capital survey, approximately 33 percent of respondents expect a shrinking of the venture capital industry. The majority (59 percent) of respondents plan to make four investments or more over the next 12 months.

Other key findings include:

- The types of businesses respondents plan to invest in the next 12 months are very diverse with over 46 percent targeting information technology and another 11 percent planning to invest in basic materials & energy.
- Respondents' exit strategies include selling to a public company (35 percent) followed by selling to a private company (23 percent).
- Respondents believe access to capital is the most important issue facing privately-held businesses today.

Operational and Assessment Characteristics

Approximately 41 percent of respondents made five investments or more over the last 12 months.

Figure 55. Total Number of Investments Made in the Last 12 Months

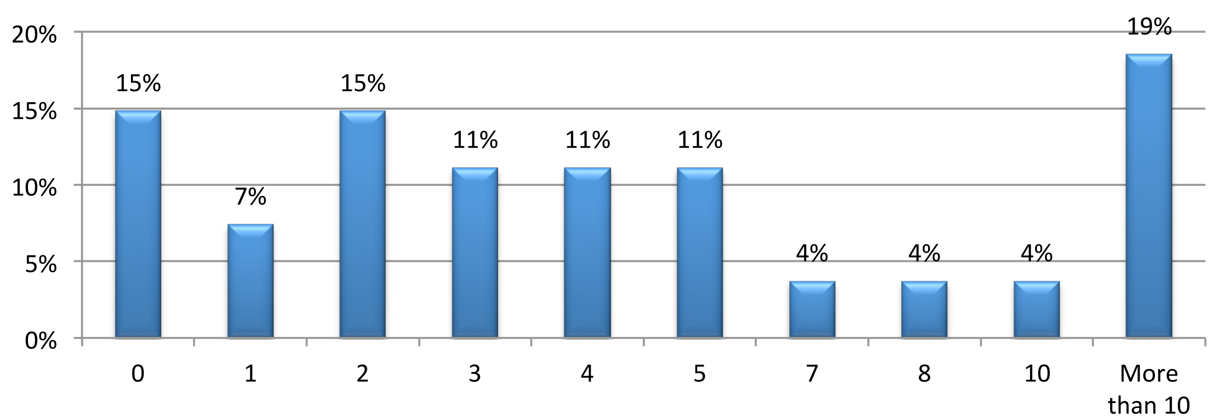
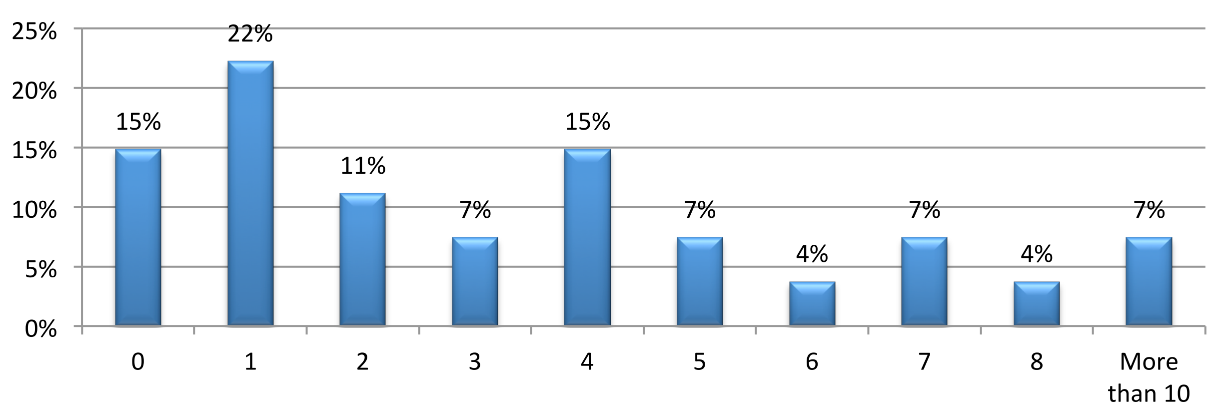


Figure 56. Number of Follow-on Investments Made in the Last 12 Months



The majority (59 percent) of respondents plan to make four investments or more over the next 12 months.

Figure 57. Number of Total Investments Planned over Next 12 Months

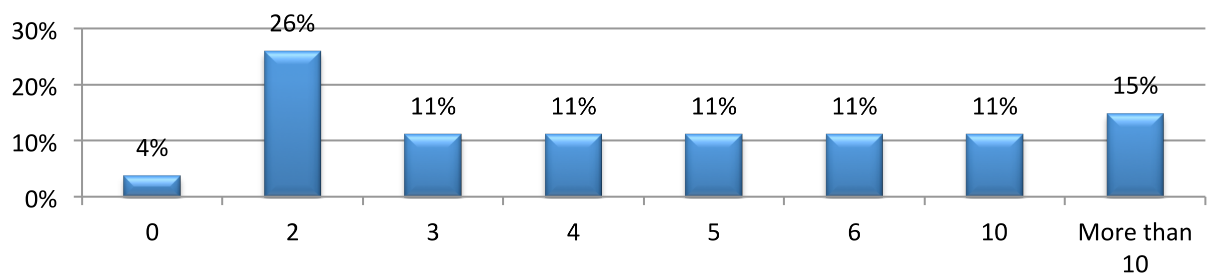
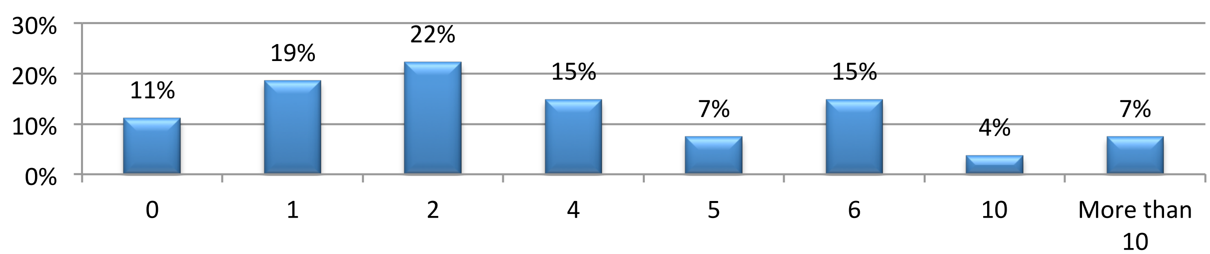


Figure 58. Number of Follow-on Investments Planned over Next 12 Months



Respondents

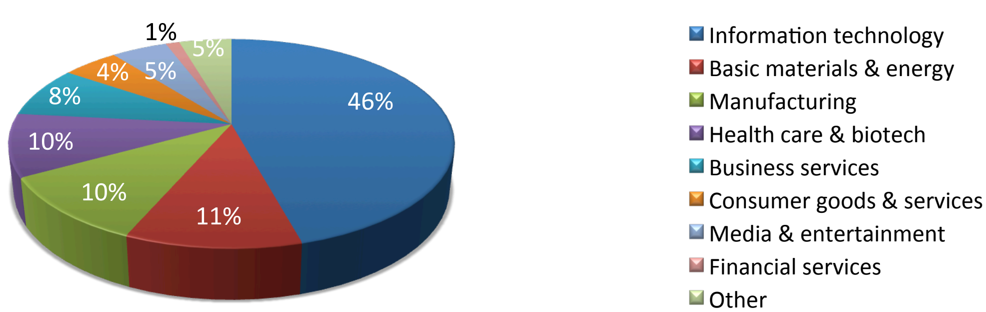
reported on business practices and the results are reflected below.

Table 38. VC Fund Data

	1st quartile	Median	3rd quartile
Vintage year (year in which first investment made)	2005	2010	2011
Size of fund ($ millions)	$37.5	$75	$125
Targeted number of total investments	13	18	25
Target fund return (gross pretax cash on cash annual IRR %)	20%	25%	35%
Expected fund return (gross pretax cash on cash annual IRR %)	15%	25%	25%

Respondents plan to invest in very diverse types of businesses over next 12 months with over 46 percent targeting Information technology and another 11 percent planning to invest in basic materials & energy.

Figure 59. Type of Business for Investments Planned over Next 12 Months



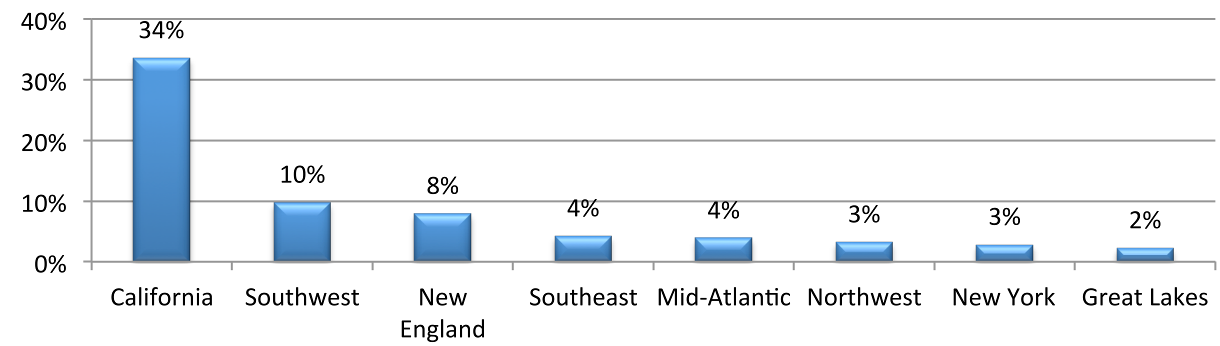
Respondents reported on a variety of stats pertaining to their investments.

Table 39. General Information on Investments by Company Stages

	Seed	Startup	Early Stage	Expansion	Later Stage
Number of Investments Made in Last six months					
1st Quartile	1	1	1.8	1.3	1
Median	**1.5**	**2**	**4**	**2**	**3**
3rd Quartile	2	2	5.8	4.8	6
Average Size of Investment ($ million)					
1st Quartile	0.5	0.5	1.5	1.5	1.6
Median	1	1.5	2.5	2.5	4
3rd Quartile	1.5	2.5	3.5	3.3	7.5
Average % of Total Equity Purchased (fully diluted basis)					
1st Quartile	15%	25%	15%	5%	5%
Median	**15%**	**30%**	**15%**	**15%**	**10%**
3rd Quartile	35%	35%	20%	15%	15%
Total expected Returns (gross cash on cash pretax IRR) on new investments					
1st Quartile	23%	23%	23%	20%	16%
Median	**28%**	**28%**	**28%**	**28%**	**23%**
3rd Quartile	45%	38%	40%	34%	33%
Expected Time to Exit (years)					
1st Quartile	5	4.3	4	2	1.8
Median	**5.5**	**5**	**5**	**3**	**2**
3rd Quartile	7	6	5.5	5	2
Average company 'pre-money' value ($ million)					
1st Quartile	0.8	1.8	5.0	4.5	7.0
Median	**2.5**	**2.5**	**8.0**	**15.0**	**25.0**
3rd Quartile	3.5	2.5	15.0	15.0	35.0
Average Company Value at Time of Investment (post-money $ millions)					
1st Quartile	1.8	2.5	8.0	15.0	10.0
Median	**3.0**	**4.5**	**15.0**	**15.0**	**25.0**
3rd Quartile	8.0	7.0	25.0	25.0	35.0

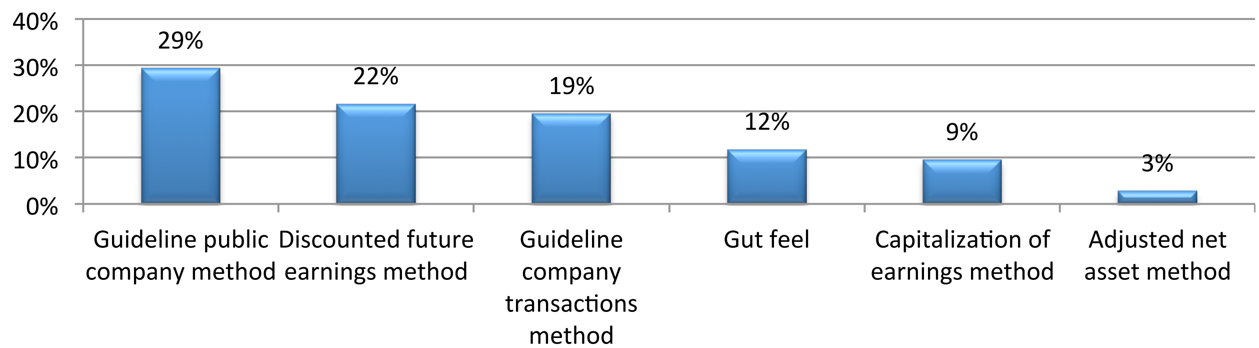
Respondents reported on where they plan to invest over the next 12 months. The results reflect investment throughout the U.S.

Figure 60. Geographic Location of Planned Investment over Next 12 Months



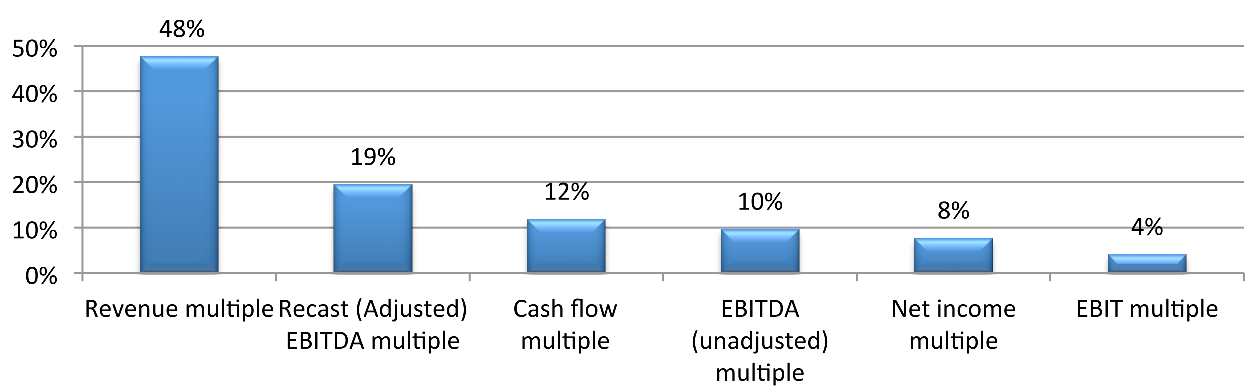
When valuing the company, approximately 29 percent of respondents use guideline public company method analysis when valuing privately-held businesses.

Figure 61. Usage of Valuation Methods



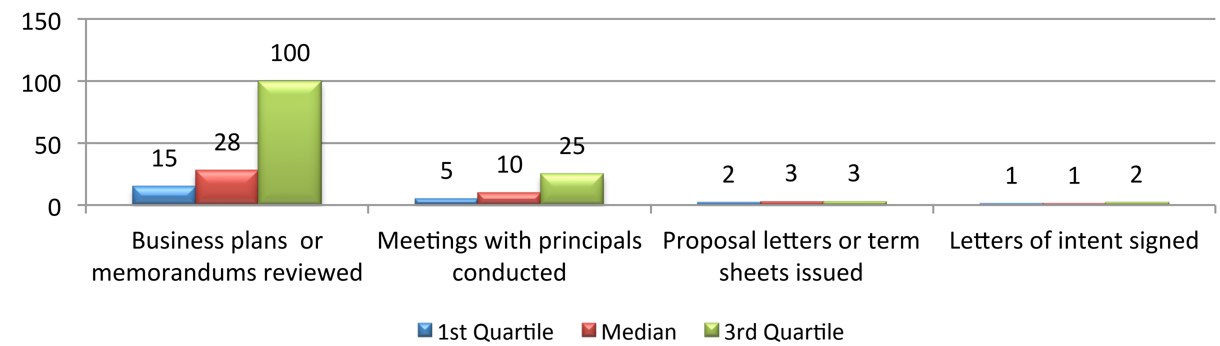
The weights of the various multiple methods used by respondents when valuing privately-held businesses included 48 percent for revenue multiple and 19 percent for recast (adjusted) EBITDA multiple methods.

Figure 62. Usage of Multiple Methods



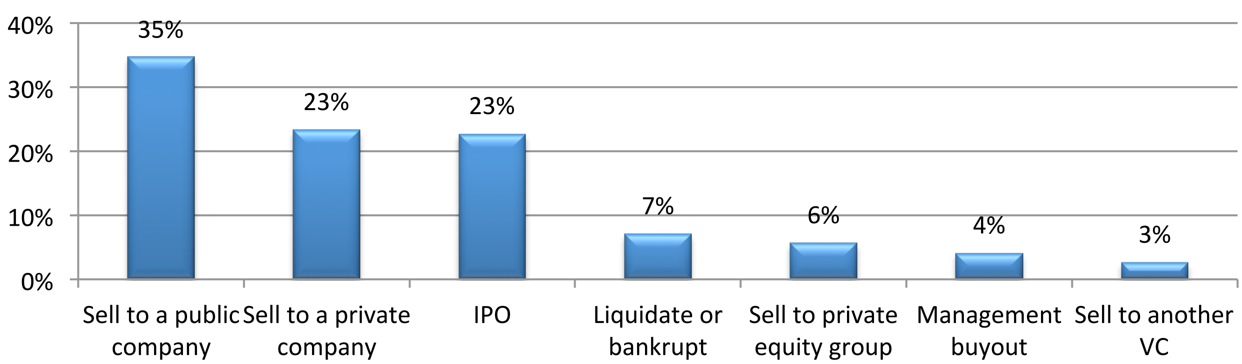
Respondents reported on items required to close one deal.

Figure 63. Items Required to Close One Deal



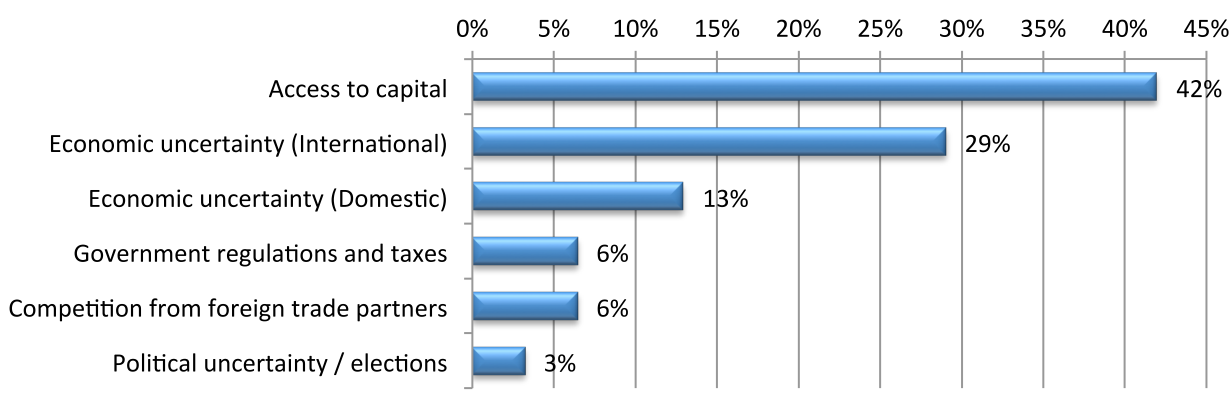
Respondents' exit strategies include selling to a public company (35 percent) followed by selling to a private company (23 percent).

Figure 64. Exit Plans for Portfolio Companies



Respondents believe access to capital is the most important issue facing privately-held businesses today.

Figure 65. Current Issues Facing Privately-Held Businesses



Respondents indicated increases in demand for venture capital, follow-on investments, value of portfolio companies and presence of super angels in space formerly occupied by VCs. They also reported decreases in quality of companies seeking investment, expected returns on new investments, size of venture capital industry and appetite for risk.

Table 40. General Business and Industry Assessment: Today versus 12 Months Ago

	Decreased significantly	Decreased slightly	Stayed about the same	Increased slightly	Increased significantly	% increase	% decrease	**Net increase/ decrease**
Demand for venture capital	4%	4%	24%	52%	16%	68%	8%	**60%**
Quality of companies seeking investment	8%	28%	40%	8%	16%	24%	36%	**-12%**
Follow-on investments	4%	0%	48%	16%	32%	48%	4%	**44%**
Average investment size	4%	4%	60%	24%	8%	32%	8%	**24%**
Exit opportunities	0%	29%	33%	33%	4%	38%	29%	**8%**
Time to exit deals	0%	13%	29%	33%	25%	58%	13%	**46%**
Expected returns on new investments	8%	20%	52%	16%	4%	20%	28%	**-8%**
Value of portfolio companies	4%	4%	21%	58%	13%	71%	8%	**63%**
General business conditions	12%	16%	28%	44%	0%	44%	28%	**16%**
Presence of super angels in space formerly occupied by VCs	4%	13%	46%	25%	13%	38%	17%	**21%**
Size of venture capital industry	16%	32%	32%	20%	0%	20%	48%	**-28%**
Appetite for risk	8%	48%	28%	8%	8%	16%	56%	**-40%**

Respondents expect further increases in all business characteristics except size of venture capital industry and appetite for risk.

Table 41. General Business and Industry Assessment Expectations over the Next 12 Months

	Decrease significantly	Decrease slightly	Stay about the same	Increase slightly	Increase significantly	% increase	% decrease	**Net increase/ decrease**
Demand for venture capital	0%	0%	25%	50%	25%	75%	0%	**75%**
Quality of companies seeking investment	8%	13%	38%	38%	4%	42%	21%	**21%**
Follow-on investments	0%	0%	33%	46%	21%	67%	0%	**67%**
Average investment size	0%	0%	38%	46%	17%	63%	0%	**63%**
Exit opportunities	0%	13%	52%	26%	9%	35%	13%	**22%**
Time to exit deals	0%	9%	52%	17%	22%	39%	9%	**30%**
Expected returns on new investments	4%	8%	58%	29%	0%	29%	13%	**17%**
Value of portfolio companies	0%	8%	38%	42%	13%	54%	8%	**46%**
General business conditions	4%	17%	33%	46%	0%	46%	21%	**25%**
Presence of super angels in space formerly occupied by VCs	5%	14%	59%	14%	9%	23%	18%	**5%**
Size of venture capital industry	8%	25%	38%	21%	8%	29%	33%	**-4%**
Appetite for risk	13%	21%	42%	17%	8%	25%	33%	**-8%**

ANGEL INVESTOR SURVEY INFORMATION

The majority (57 percent) of respondents plan to make between two and four investments. Other key findings include:

- Approximately 41 percent of respondents base valuations on gut feel when valuing privately-held businesses.
- When using multiples to determine the value of a business, the most popular methods used by respondents were EBITDA multiple (27 percent), revenue multiple (26 percent) and net income multiple (20 percent).
- The types of businesses respondents plan to invest in over next 12 months are very diverse with over 30 percent targeting information technology and another 19 percent planning to invest in health care or biotech.
- Respondents indicated a sharp increase in demand for angel capital, increases in size of angel industry, follow-on investments, time to exit deals and improved general business conditions. They also reported decreased opportunities to exit, expected returns on new investments and appetite for risk.
- Respondents' exit strategies include selling to a private company (51 percent) and selling to a public company (24 percent).

Operational and Assessment Characteristics

Approximately 27 percent of respondents made either five investments or more over the last 12 months.

Figure 66. Total Number of Investments Made in the Last 12 Months

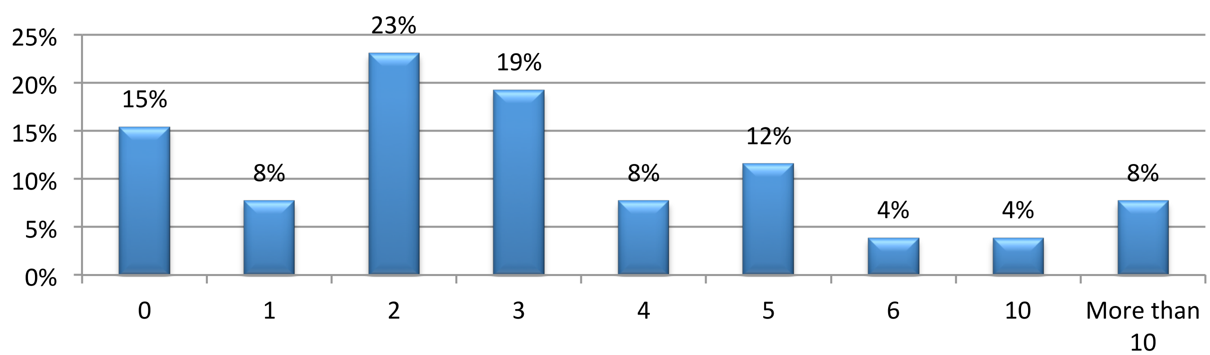
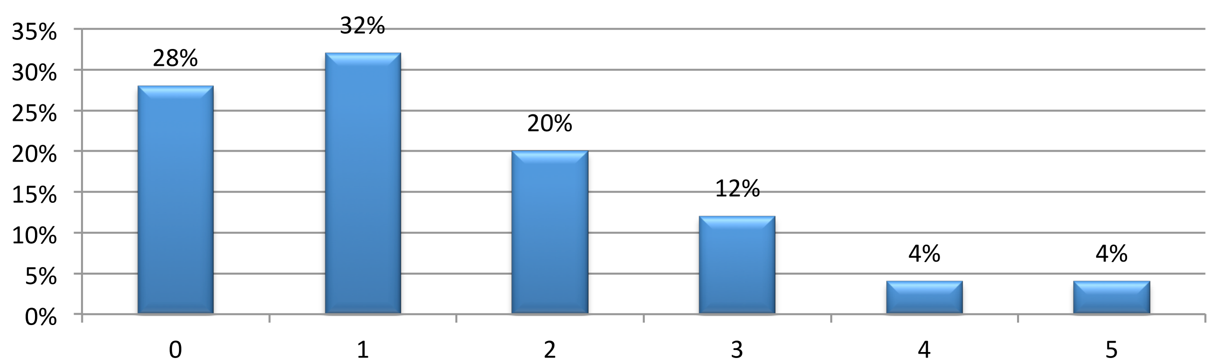


Figure 67. Number of Follow-on Investments Made in the Last 12 Months



The majority (58 percent) of respondents plan to make between two and four investments over the next 12 months.

Figure 68. Number of Total Investments Planned over Next 12 Months

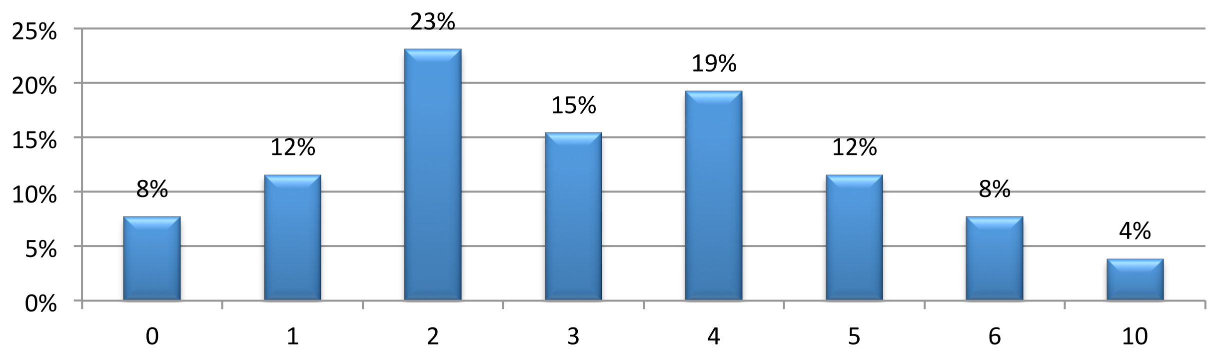
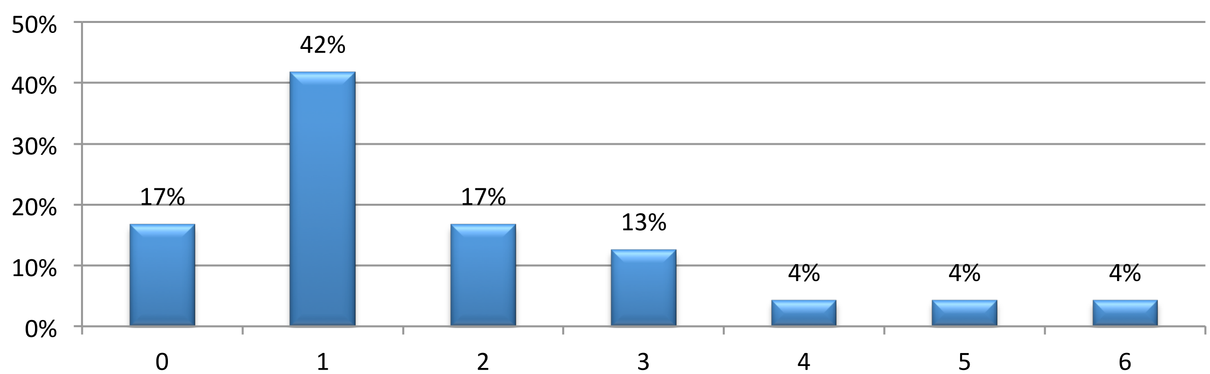
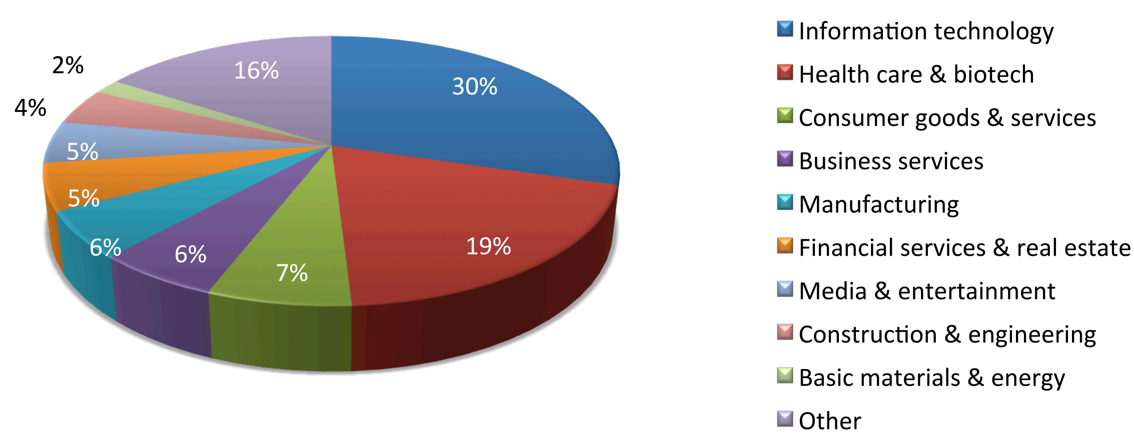


Figure 69. Number of Follow-on Investments Planned over Next 12 Months



The types of businesses respondents plan to invest in over next 12 months are very diverse with over 30 percent targeting information technology and another 19 percent planning to invest in health care & biotech.

Figure 70. Type of Business for Investments Planned over Next 12 Months



Respondents reported on a variety of stats pertaining to their investments.

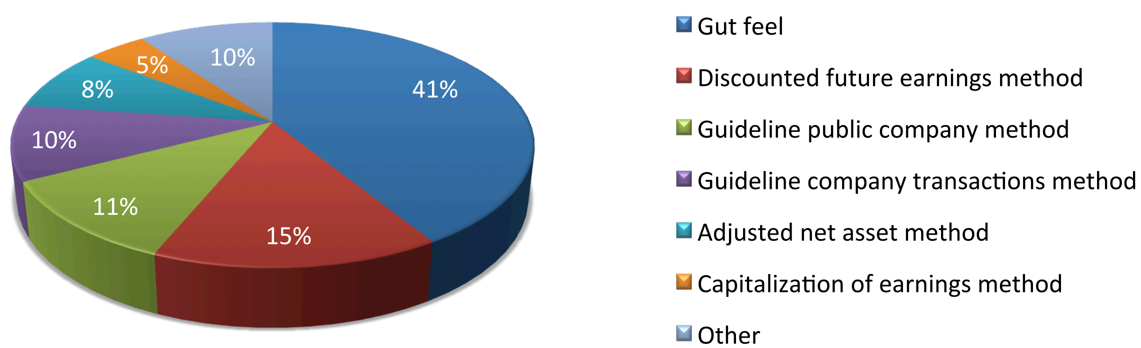
Table 42. General Information on Investments by Company Stages

	Seed	Startup	Early Stage	Expansion	Later Stage
Number of Investments Made in Last six months					
1st Quartile	2.0	1.5	2.0	1.3	1.0
Median	**2.0**	**3.0**	**2.0**	**2.0**	**1.0**
3rd Quartile	3.0	3.0	4.0	2.8	1.5
Average Size of Investment (in thousands)					
1st Quartile	$25	$25	$25	$37.50	$300
Median	**$75**	**$75**	**$150**	**$150**	**$450**
3rd Quartile	$175	$150	$250	$325	$850
Average % of Total Equity Purchased (fully diluted basis)					
1st Quartile	5%	5%	3%	2%	2%
Median	**10%**	**5%**	**3%**	**3%**	**2%**
3rd Quartile	10%	10%	10%	5%	11%
Total EXPECTED Returns (gross cash on cash pretax IRR) on New Investments (%)					
1st Quartile	15%	18%	21%	21%	18%
Median	**30%**	**25%**	**25%**	**25%**	**25%**
3rd Quartile	35%	25%	35%	35%	30%
Expected Time to Exit (years)					
1st Quartile	3	4	4	3	2
Median	**5**	**5**	**5**	**3**	3
3rd Quartile	7	5	5	4	4
Average company 'pre-money' value (in millions)					
1st Quartile	$0.45	$0.75	$2.5	$2.5	$2.5
Median	**$0.85**	**$1.5**	**$2.5**	**$2.5**	**$2.5**
3rd Quartile	$1.5	$1.5	$3.5	$7.5	$4.5
Average Company Value at Time of Investment (post-money $ millions)					
1st Quartile	$0.3	$0.75	$2.5	$4.5	$8.0
Median	**$1.0**	**$2.0**	**$3.5**	**$8.0**	**$12.0**
3rd Quartile	$2.0	$2.5	$5.0	$14.0	$13.0

ANGEL cont.

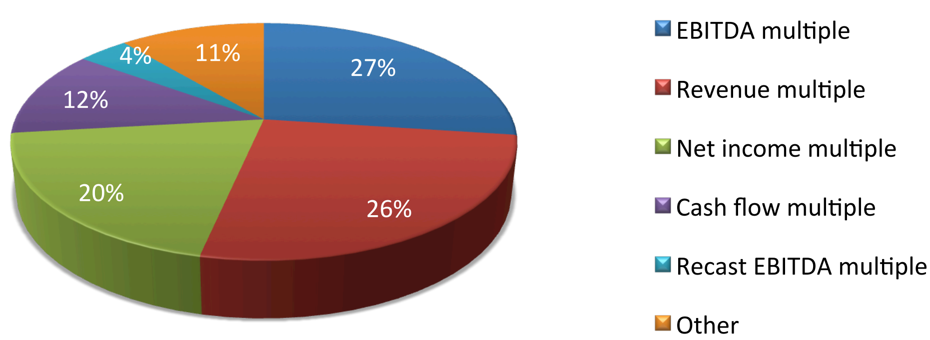
Approximately 41 percent of respondents base valuations on gut feel when valuing privately-held businesses followed by discounted future earnings method (15 percent).

Figure 71. Usage of Valuation Methods



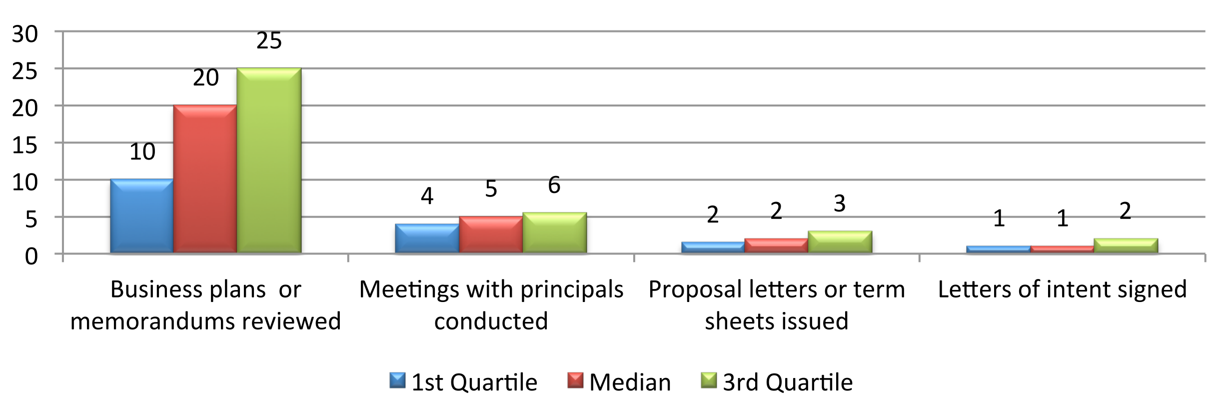
The weights of the various multiple methods used by respondents when valuing privately-held businesses included 27 percent for EBITDA multiple and 26 percent for revenue multiple methods.

Figure 72. Usage of Multiple Methods



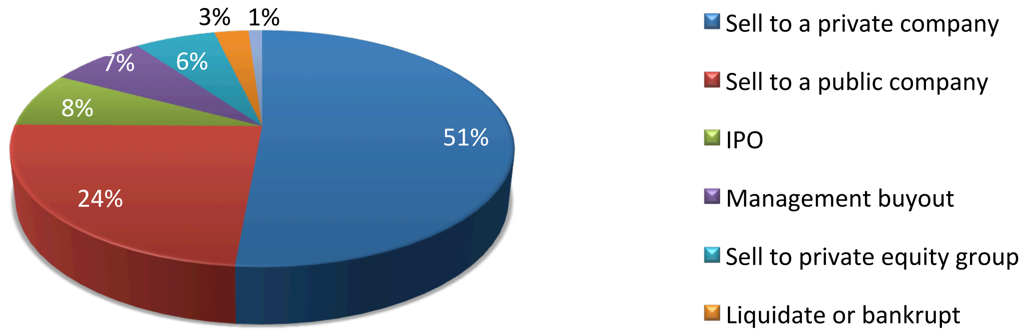
Respondents reported on items required to close one deal.

Figure 73. Items Required to Close One Deal



Respondents' exit strategies include selling to a private company (51 percent) and selling to a public company (24 percent).

Figure 74. Exit Plans for Portfolio Companies



Respondents indicated a sharp increase in demand for angel capital, increases in size of angel industry, follow-on investments, time to exit deals and improved general business conditions. They also reported decreased opportunities to exit, expected returns on new investments and appetite for risk.

Table 43. General Business and Industry Assessment: Today versus 12 Months Ago

	Decreased significantly	Decreased slightly	Stayed about the same	Increased slightly	Increased significantly	% increase	% decrease	**Net increase/ decrease**
Demand for angel capital	5%	0%	32%	32%	32%	63%	5%	**58%**
Size of angel finance industry	6%	17%	22%	39%	17%	56%	22%	**33%**
Quality of companies seeking investment	11%	11%	33%	22%	22%	44%	22%	**22%**
Follow-on investments	6%	12%	29%	18%	35%	53%	18%	**35%**
Average investment size	6%	17%	44%	22%	11%	33%	22%	**11%**
Exit opportunities	17%	17%	50%	17%	0%	17%	33%	**-17%**
Time to exit deals	0%	6%	28%	28%	39%	67%	6%	**61%**
Expected returns on new investments	11%	28%	50%	6%	6%	11%	39%	**-28%**
Value of portfolio companies	6%	22%	33%	28%	11%	39%	28%	**11%**
General business conditions	17%	11%	28%	39%	6%	44%	28%	**17%**
Appetite for risk	11%	28%	39%	17%	6%	22%	39%	**-17%**

ANGEL cont.

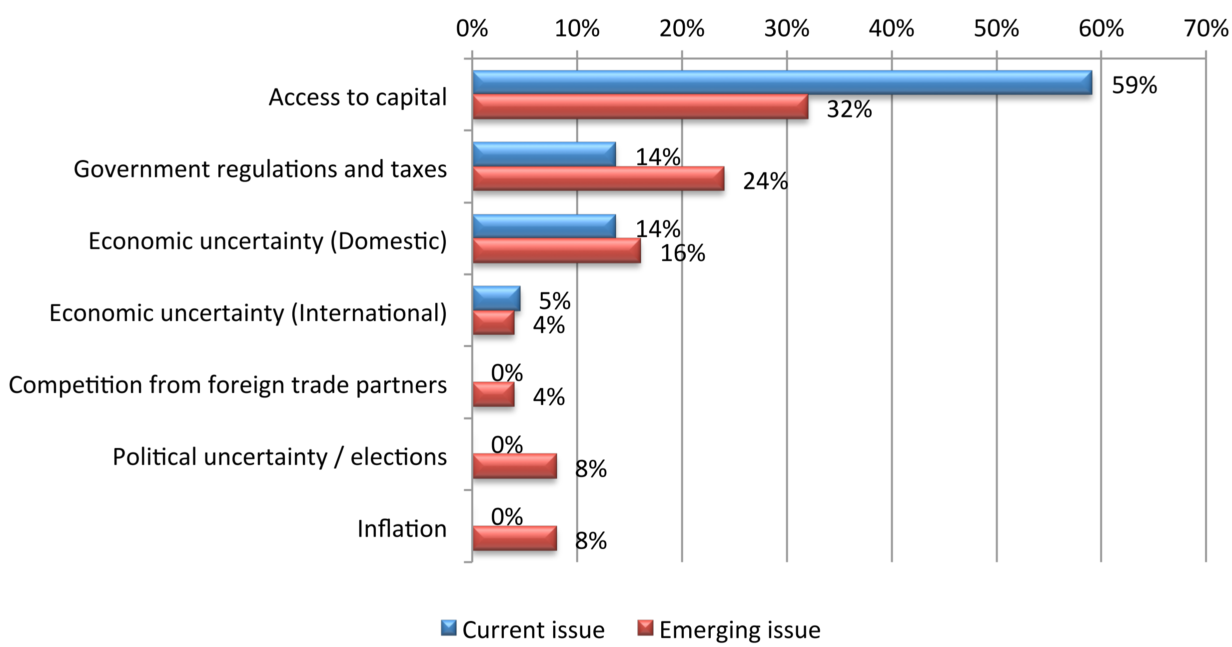
Respondents expect further increases in business characteristics except exit opportunities.

Table 44. General Business and Industry Assessment Expectations over the Next 12 Months

	Decrease significantly	Decrease slightly	Stay about the same	Increase slightly	Increase significantly	% increase	% decrease	**Net increase/ decrease**
Demand for angel capital	0%	0%	24%	47%	29%	76%	0%	**76%**
Size of angel finance industry	0%	0%	44%	38%	19%	56%	0%	**56%**
Quality of companies seeking investment	13%	6%	38%	25%	19%	44%	19%	**25%**
Follow-on investments	6%	13%	25%	31%	25%	56%	19%	**38%**
Average investment size	0%	6%	31%	38%	25%	63%	6%	**56%**
Exit opportunities	0%	25%	56%	13%	6%	19%	25%	**-6%**
Time to exit deals	0%	6%	50%	25%	19%	44%	6%	**38%**
Expected returns on new investments	0%	19%	56%	19%	6%	25%	19%	**6%**
Value of portfolio companies	0%	6%	38%	31%	25%	56%	6%	**50%**
General business conditions	6%	13%	25%	50%	6%	56%	19%	**38%**
Appetite for risk	0%	13%	38%	44%	6%	50%	13%	**38%**

Respondents believe access to capital is the most important current and emerging issue facing privately-held businesses.

Figure 76. Issues Facing Privately-Held Businesses



BUSINESS APPRAISER SURVEY INFORMATION

According to the 166 survey respondents believe domestic economic uncertainty is the most important issue facing privately-held business today. Respondents indicated increases in number of engagements, time to complete a typical appraisal, fees for services, and competition over the last 12 months. They also expect decreases in all general business characteristics over the next year.

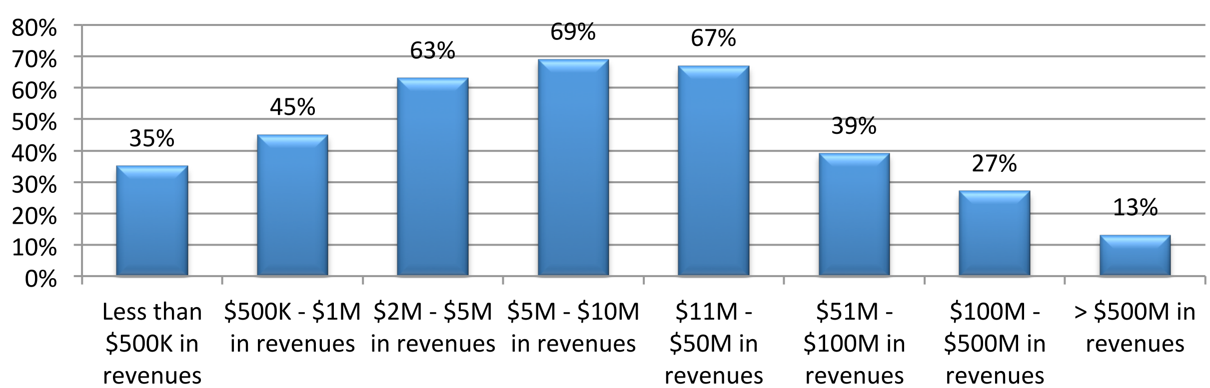
Other key findings include:

- Discounted future earnings valuation method is the overwhelming favorite among respondents
- Recast (adjusted) EBITDA multiple is the most popular when using multiple valuation method
- Respondents use an average risk-free rate of 3.4 percent and a market (equity) risk premium of 6.3 percent
- Average long-term terminal growth is estimated at 3.2 percent

Operational and Assessment Characteristics

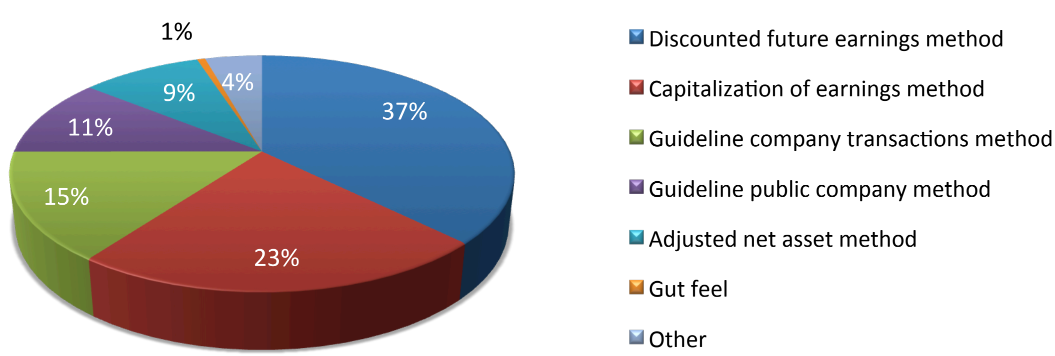
Most of the companies valued by respondents have annual revenues from $2 million to $50 million.

Figure 75. Annual Revenues of Companies Valued



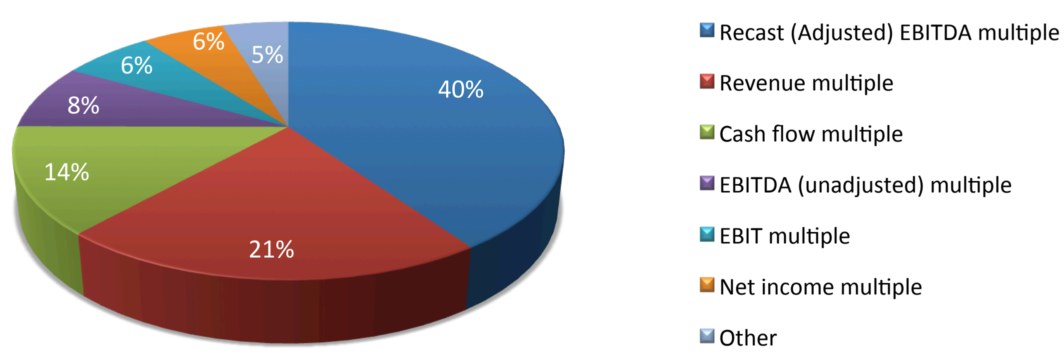
Appraisers, on average, apply a 37 percent weight to discounted future earnings method when valuing a privately-held business.

Figure 76. Usage of Valuation Methods



Respondents using multiples-based approaches indicate a preference for using recast (adjusted) EBITDA multiples (40 percent), followed by revenue multiples (21 percent).

Figure 77. Usage of Multiple Methods



Respondents indicated using an average risk-free rate of 3.4 percent, average market (equity) risk premium of 6.3 percent and average long-term growth rate of 3.2 percent.

Figure 78. Average Risk-Free Rat and Market (equity) Risk Premium and Long-Term Growth Rate

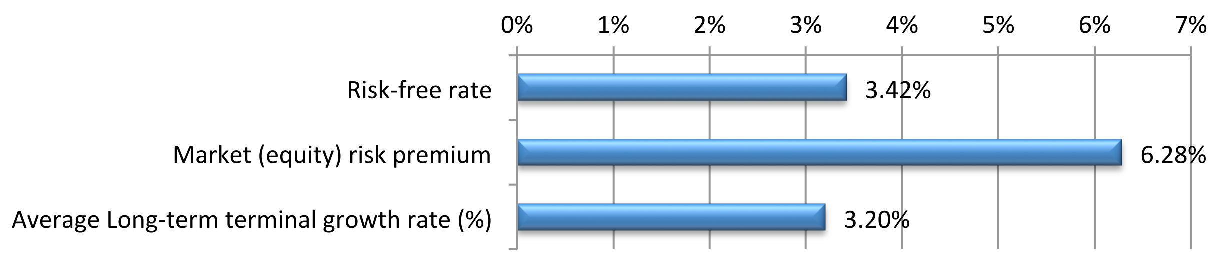
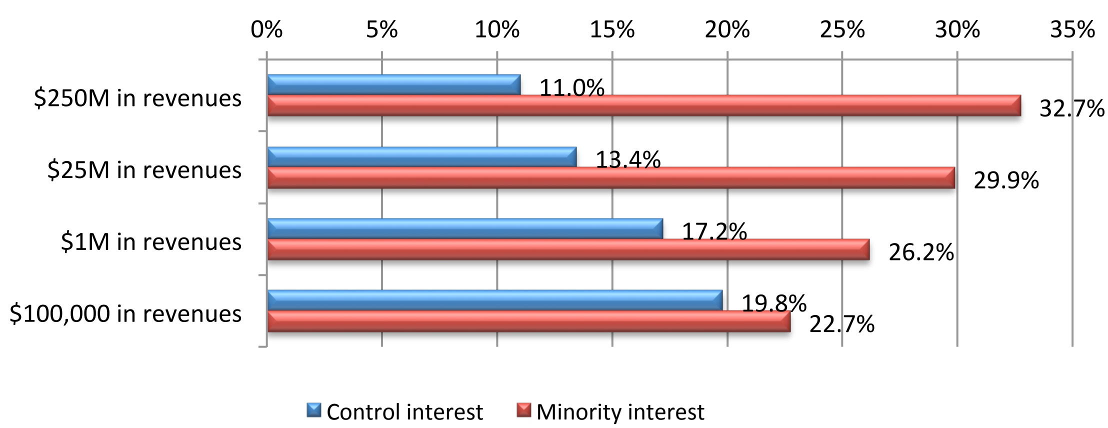


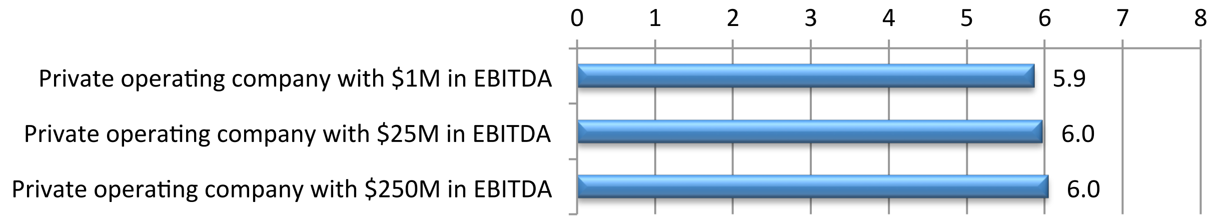
Figure 79 indicates considerable differences in DLOMs across sizes of companies and subject interests.

Figure 79. Discount for Lack of Marketability (DLOM) by Revenue Sizes



APPRAISERS cont.

Figure 80. Explicit Forecast Period for High-Growth Companies by Revenue Sizes (years)



Respondents indicated increases in number of engagements, time to complete a typical appraisal, fees for services, and competition over the last12 months.

Table 45. General Business and Industry Assessment: Today versus 12 Months Ago

Characteristics	Decreased significantly	Decreased slightly	Stayed about the same	Increased slightly	Increased significantly	% increase	% decrease	Net increase/ decrease
Number of engagements	8%	17%	32%	23%	20%	43%	25%	**18%**
Time to complete a typical appraisal	1%	12%	68%	14%	6%	19%	13%	**6%**
Fees for services	2%	12%	54%	31%	1%	33%	14%	**19%**
Competition	0%	5%	57%	31%	7%	38%	5%	**34%**
Cost of capital	1%	15%	59%	22%	3%	25%	16%	**9%**
Market (equity) risk premiums	0%	11%	72%	13%	3%	17%	11%	**5%**
DLOM	0%	8%	85%	7%	1%	8%	8%	**0%**
Company specific risk premiums	0%	11%	66%	19%	3%	22%	11%	**11%**
General business conditions	1%	14%	48%	35%	1%	36%	16%	**21%**

Respondents expect decreases in all general business characteristics except DLOMs over the next year.

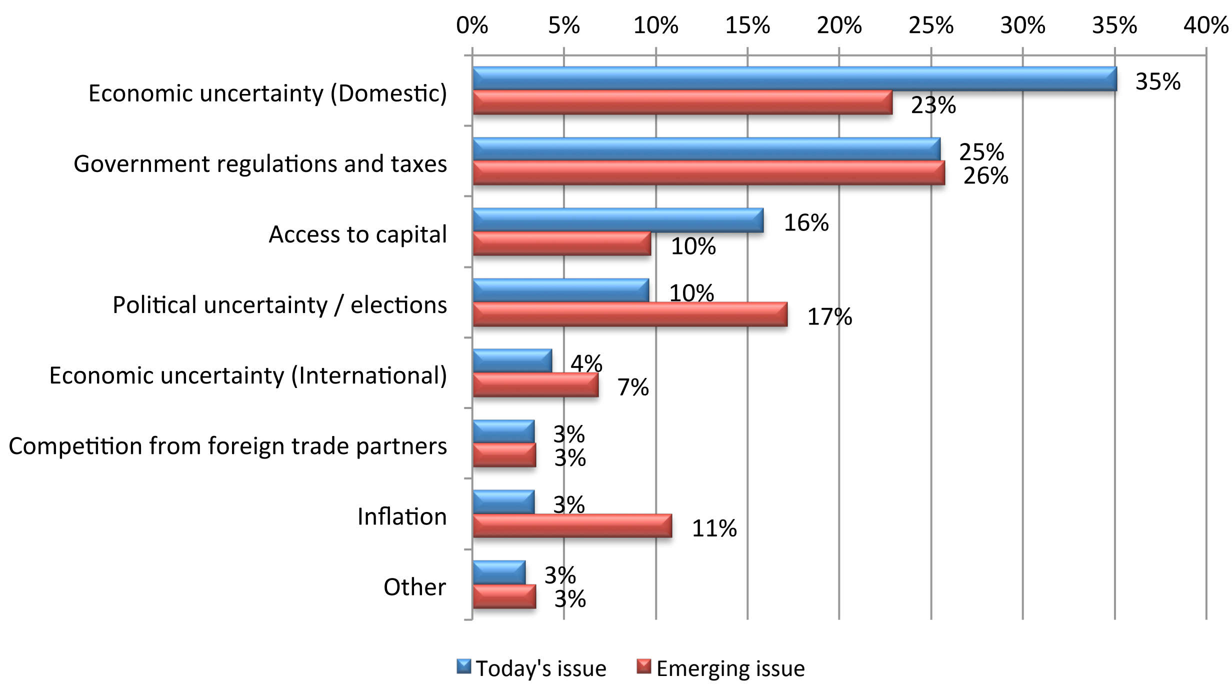
Table 46. General Business and Industry Assessment Expectations over the Next 12 Months

Characteristics	Decrease significantly	Decrease slightly	Stay about the same	Increase slightly	Increase significantly	% increase	% decrease	Net increase/ decrease
Number of engagements	3%	13%	37%	41%	7%	0%	16%	**-16%**
Time to complete a typical appraisal	1%	10%	82%	7%	1%	0%	10%	**-10%**
Fees for services	0%	4%	62%	31%	2%	1%	4%	**-3%**
Competition	0%	1%	68%	28%	2%	1%	1%	**-1%**
Cost of capital	0%	5%	58%	33%	3%	1%	5%	**-3%**
Market (equity) risk premiums	0%	3%	69%	22%	3%	3%	3%	**-1%**
DLOM	0%	5%	82%	6%	2%	6%	5%	**1%**
Company-specific risk premiums	0%	7%	77%	11%	1%	4%	7%	**-3%**
General business conditions	1%	10%	49%	38%	2%	0%	11%	**-11%**

APPRAISERS cont.

Respondents believe domestic economic uncertainty is the most important issue facing privately-held businesses today.

Figure 81. Issues Facing Privately-Held Businesses



BROKER SURVEY INFORMATION

Approximately 31 percent of the 40 participants in the broker survey said they expect to close six deals or more in the next 12 months. Respondents believe domestic economic uncertainty is the most important issue facing privately-held businesses today. Government regulations and taxes and domestic economic uncertainty is indicated as the most important emerging issue.

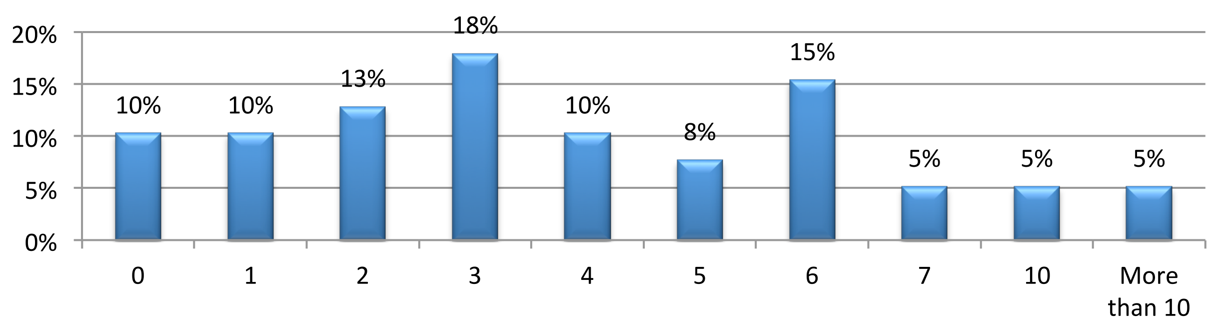
Other key findings include:

- The majority of deals (86 percent) took less than 1 year to close with the largest concentration being the nine to ten month category. Another 12 percent took about a year and a half.
- Respondents indicated increases in deal flow, ratio of businesses sold to total listings, business exit opportunities and difficulty selling business.
- Top three reasons for deals not closing: unreasonable non-price seller or buyer demand (21 percent), valuation gap in pricing (21 percent), and economic uncertainty (14 percent).

Operational and Assessment Characteristics

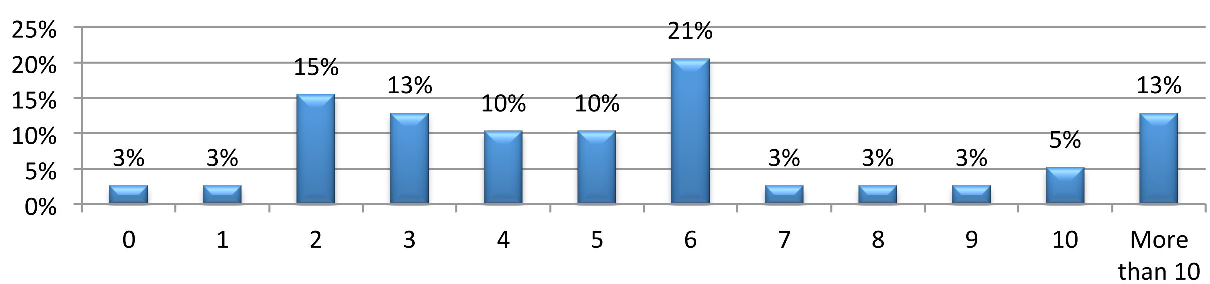
Approximately 10 percent of the respondents didn't close any deal in the last 12 months; 59 percent closed between one to five deals, while 31 percent closed six or more transactions.

Figure 82. Private Business Sales Transactions Closed in the Last Twelve Months



Approximately 51 percent of respondents are planning to close between one and five business sales transactions in the next 12 months.

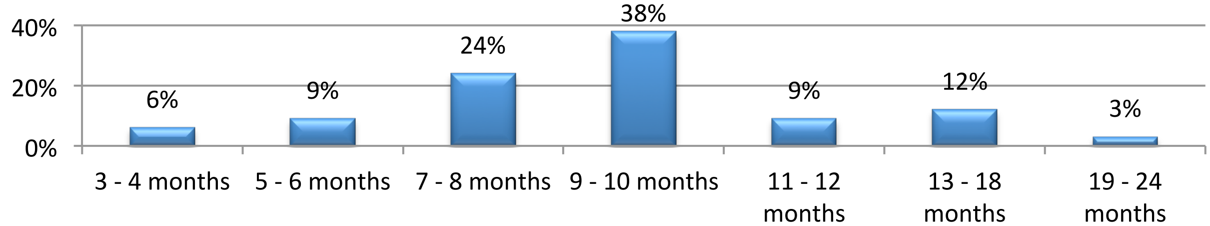
Figure 83. Private Business Sales Transactions Expected to Close in the Next Twelve Months



BROKER cont.

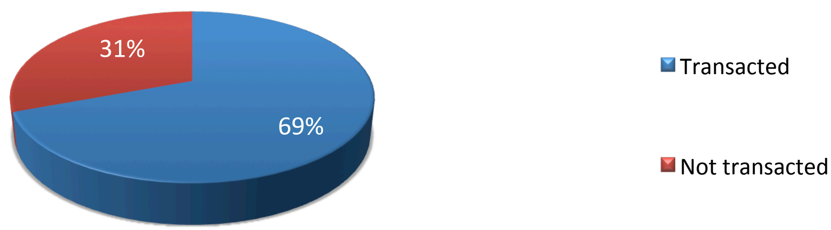
The majority of business transactions (62 percent) took 7 to 10 months to close.

Figure 84. Average Number of Months to Close One Business Transaction



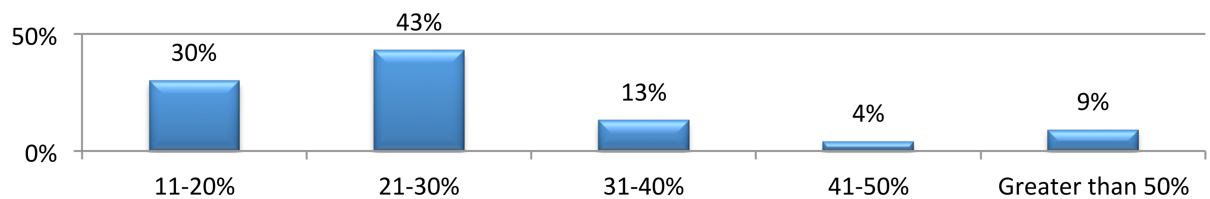
Approximately 31 percent of deals terminated without transacting over the past year.

Figure 85. Percentage of Business Sales Engagements Terminated Without Transacting



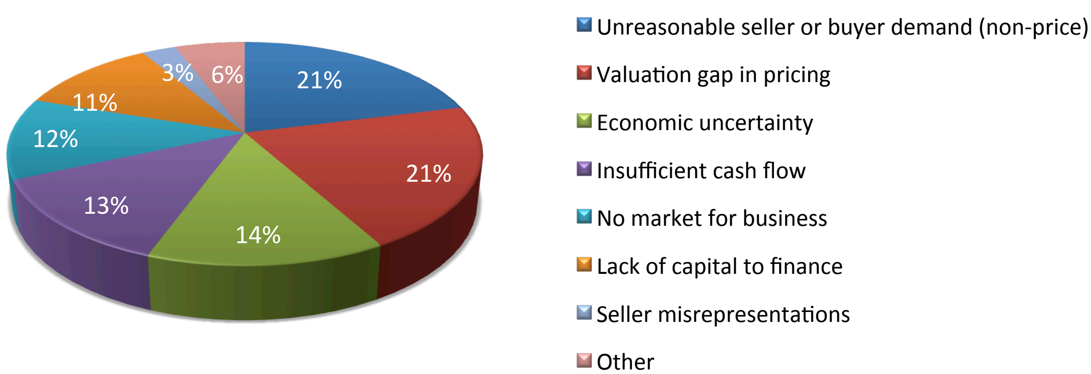
Approximately 43 percent of deals that were not transacted had a valuation gap in pricing between 21 percent and 30 percent.

Figure 86. Valuation Gap in Pricing for Transactions That Didn't Close



Top reasons for deals not closing: valuation gap in pricing (21 percent) and unreasonable seller/buyer demand (21 percent).

Figure 87. Reasons for Business Sales Engagements Not Transacting



BROKER cont.

The most popular valuation method used by respondents when valuing privately-held businesses was capitalization of earnings method.

Figure 88. Usage of Valuation Methods

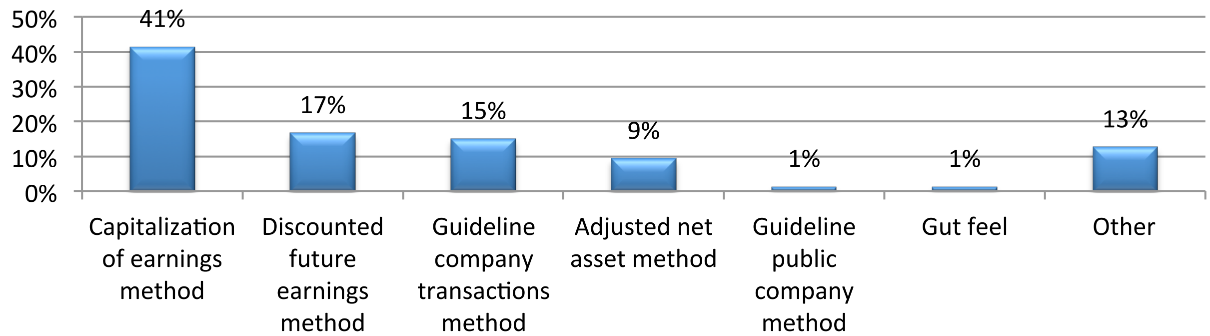
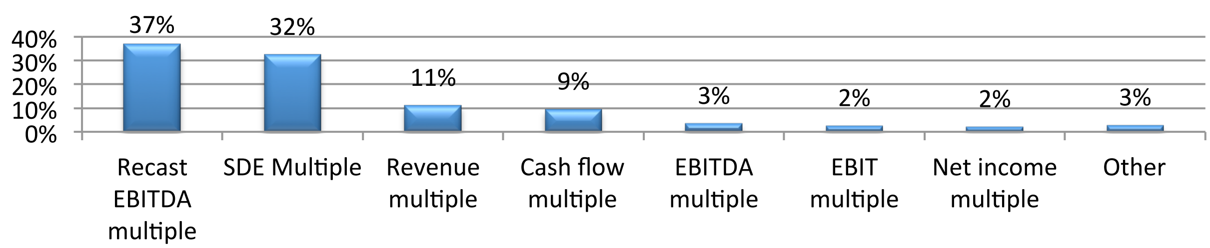


Figure 89. Usage of Multiples



Approximately 50 percent of business sales transactions closed in the last 12 months involved seller financing or seller note.

Figure 90. Components of Closed Deals

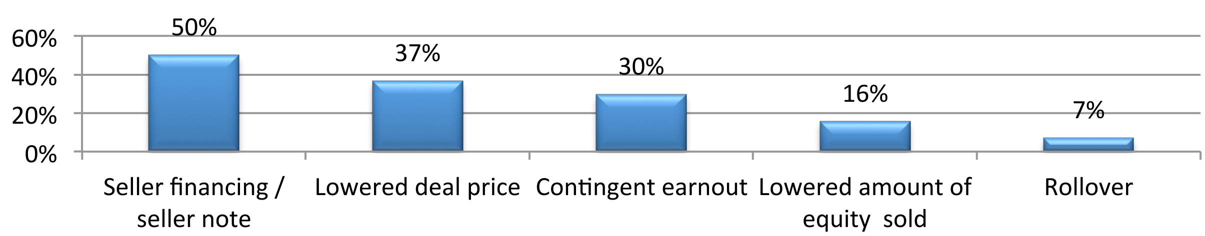


Figure 91. How Difficult to Arrange Senior Debt for Transactions over the Past 12 Months

Revenue size	Extremely difficult	Difficult	Somewhat difficult	Neutral	Somewhat easy	Easy	Extremely easy	**Score (-2 to 2)**
$100K	79%	7%	7%	7%	0%	0%	0%	**-2.57**
$500K	45%	15%	10%	15%	15%	0%	0%	**-1.6**
$1M	29%	24%	14%	10%	14%	10%	0%	**-1.14**
$5M	25%	10%	25%	20%	15%	5%	0%	**-0.95**
$10M	23%	8%	31%	31%	8%	0%	0%	**-1.08**
$15M	20%	0%	30%	30%	10%	10%	0%	**-0.6**
$25M+	17%	8%	17%	8%	42%	8%	0%	**-0.25**

BROKER cont.

Average deal multiples on transactions by revenue size from the prior 12 months as observed by respondents varied from 0.2 to 2.4.

Table 47. Median Deal Multiples by Revenue Size of Company

Revenue	100K revenue	500K revenue	$1M revenue	$5M revenue	$10M revenue	Greater than $10M revenue
Manufacturing	0.2	0.4	0.6	0.9	1.4	2.2
Retail & consumer services	0.2	0.6	0.7	1.4	1.4	1.4
Wholesale & distribution	0.2	0.4	0.4	1.1	1.1	2.2
Business services	0.3	0.6	0.7	1	1.4	2.1
Basic materials & energy	n/a	n/a	n/a	1.2	1.2	1.2
Health care & biotech	0.6	0.6	0.8	1	1.6	2.4
Information technology	0.4	0.6	1	1.2	1.2	1.2

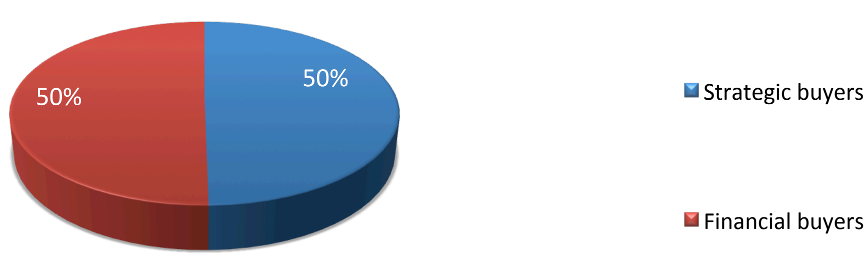
Average deal multiples on transactions by EBITDA size from the prior 12 months as observed by respondents varied from 1.5 to 6.

Table 48. Median Deal Multiples by EBITDA Size of Company

Revenue	100K EBITDA	500K EBITDA	$1M EBITDA	$5M EBITDA	Greater than $5M EBITDA
Manufacturing	2.3	3	3.5	4.5	5
Retail & consumer services	1.5	3	3	3.5	4.8
Wholesale & distribution	2.5	3	3	4.5	4.8
Business services	2	3	3.5	4	4.8
Health care & biotech	3	4	5	5	6
Information technology	2	2.8	3	4.5	4.8

Approximately 50 percent of closed business sales transactions over the past 12 months involved strategic buyers.

Figure 92. Percent of Transactions Involved Strategic and Financial Buyers



BROKER cont.

Approximately 51 percent of closed business sales transactions over the past 12 months involved strategic follow-on investments.

Figure 93. Percent of Transactions Involved Platform and Follow-on Investments

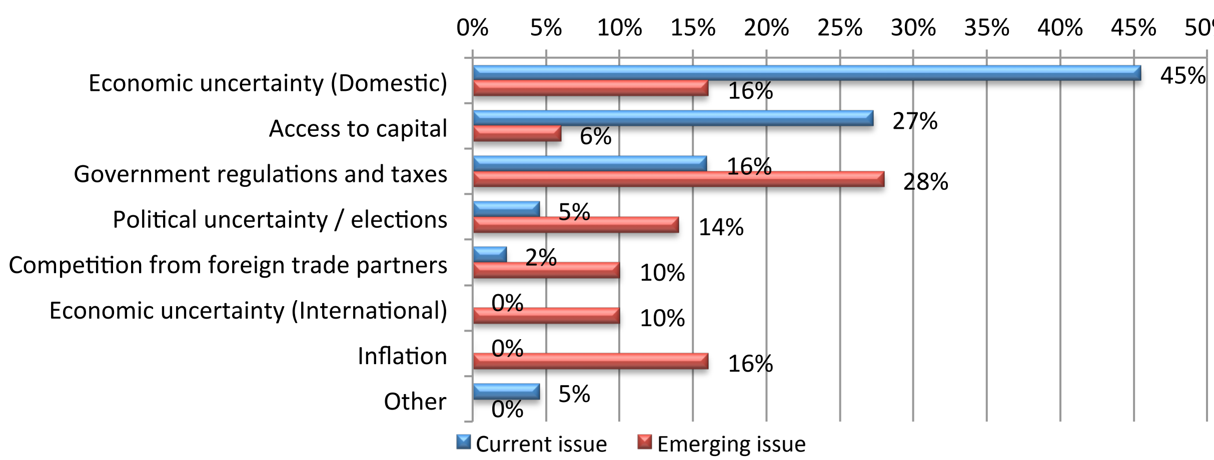
Compared to 12 months ago, respondents indicated increases in deal flow, ratio of businesses sold to total listings, business exit opportunities and improved general business conditions.

Table 49. General Business and Industry Assessment: Today versus 12 Months Ago

	Decreased significantly	Decreased slightly	Stayed about the same	Increased slightly	Increased significantly	% increase	% decrease	**Net increase**
Deal flow	6%	24%	18%	44%	9%	53%	29%	**24%**
Ratio of businesses sold / total listings	0%	12%	56%	26%	6%	32%	12%	**21%**
Deal multiples	0%	12%	65%	24%	0%	24%	12%	**12%**
Business exit opportunities	3%	19%	25%	53%	0%	53%	22%	**31%**
Amount of time to sell business	0%	12%	53%	32%	3%	35%	12%	**24%**
Difficulty selling business	0%	12%	50%	32%	6%	38%	12%	**26%**
Business opportunities for growth	6%	21%	32%	38%	3%	41%	26%	**15%**
General business conditions	6%	18%	27%	42%	6%	48%	24%	**24%**
Margin pressure on companies	0%	16%	53%	25%	6%	31%	16%	**16%**

Respondents believe domestic economic uncertainty is the most important issue facing privately-held businesses today. Government regulations and taxes are indicated as the most important emerging issues.

Figure 94. Issues Facing Privately-Held Businesses



BUSINESS OWNER SURVEY INFORMATION

Of the 951 privately-held businesses that responded to the survey, 12 percent had businesses that involved manufacturing, 10 percent were in professional, scientific or technical services, 9 percent were in finance and real estate, and 9 percent were in retail trade. Approximately 50 percent of businesses have annual revenues less than $1 million. Nearly 89 percent of business owners report having the enthusiasm to execute growth strategies, yet just 46 percent report having the necessary financial resources to successfully execute growth strategies. Other findings include:

Of the respondents who were seeking financing in the last 12 months, approximately 47 percent anticipated to raise less than $100,000 in capital. Approximately 44 percent of respondents reported that they were seeking bank business loans or business credit card financing as a source of funding, followed by friends and family (14 percent). Of all financing options, bank loans emerged as the financing source with highest "willingness" for small business to use, followed by grants and credit unions. Results also showed that 69 percent of privately-held businesses that sought bank loans over the past 12 months were successful. Survey results indicated that business owners who raised capital on average contacted 2.4 banks.

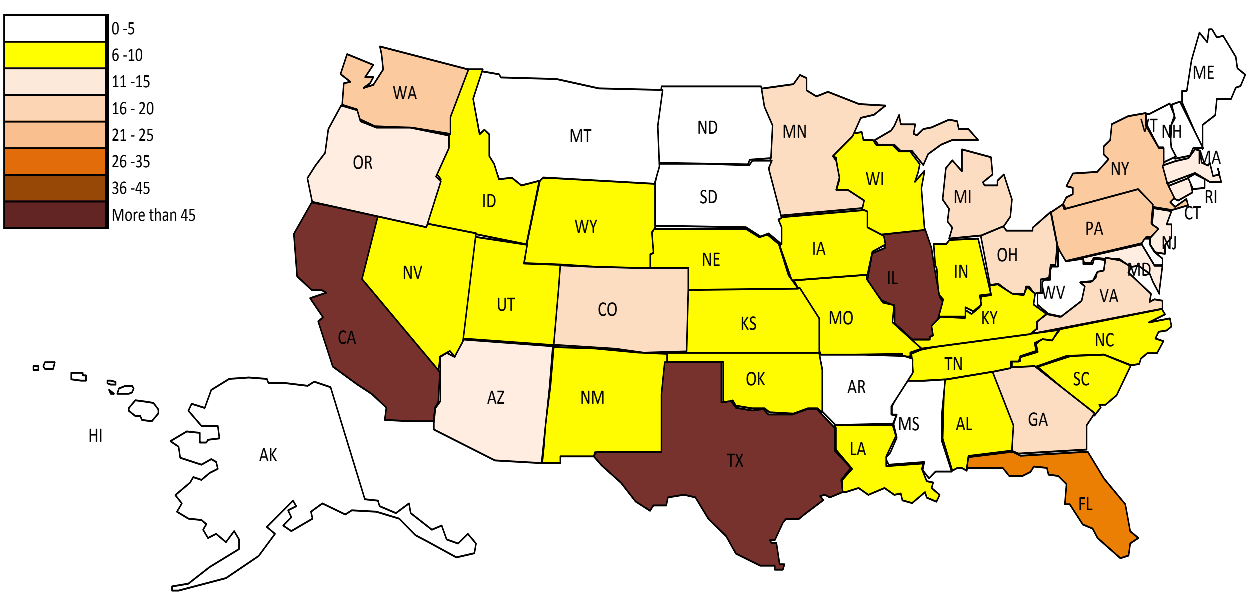
Nearly half of small businesses (53 percent) are planning to hire additional workers. Nearly 22 percent of respondents believe domestic economic uncertainty is the number one issue small businesses face today, another 22 percent believe government regulations and taxes is the most important current issue, followed by access to capital (17 percent). According to small businesses, of those policies most likely to lead to job creation in 2014, "repeal or modify affordable care act" emerged as number one (31 percent) followed by increased access to capital (24 percent), and regulatory reform (15 percent). The study showed that of those that do plan to hire, sales and marketing skills are in greatest demand (57 percent) followed by skilled labor (45 percent) and service/customer service (36 percent). Also, 85 percent of companies planning to hire indicate they'd need to train those they hire.

Three percent of respondents believe that general business conditions improved in the 12 months compared to 29 percent surveyed year ago.

Operational and Assessment Characteristics

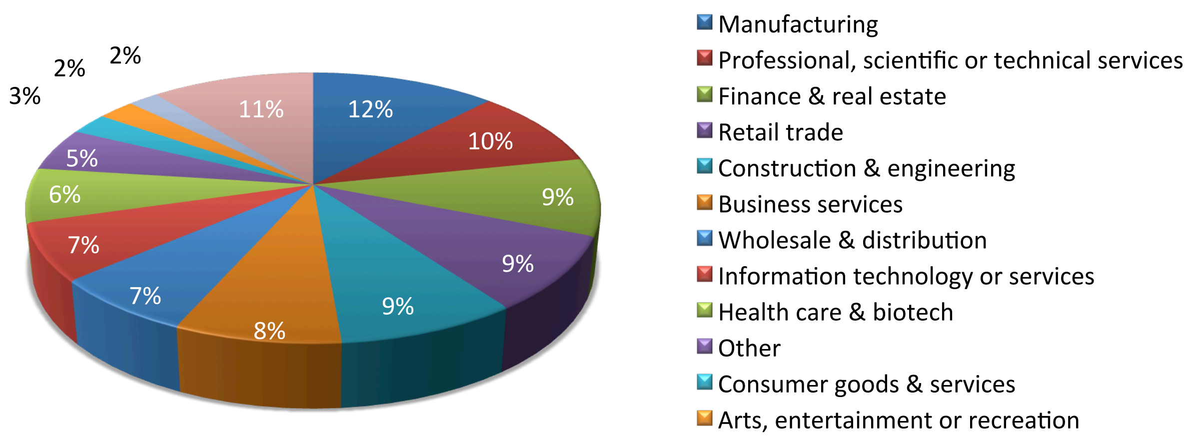
The privately-held business survey results were generated from 951 participants. The locations of businesses are distributed over all regions of the United States.

Figure 95. Respondents Distribution by State



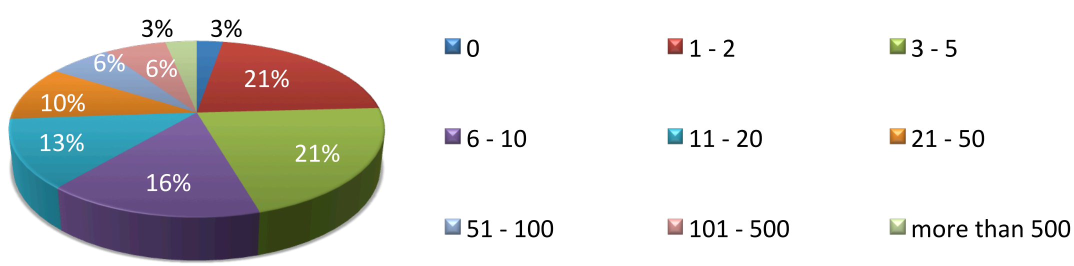
Businesses involved in services accounted for 12 percent of respondents followed by professional, scientific or technical services (10 percent) and other services (11 percent).

Figure 96. Description of Entity



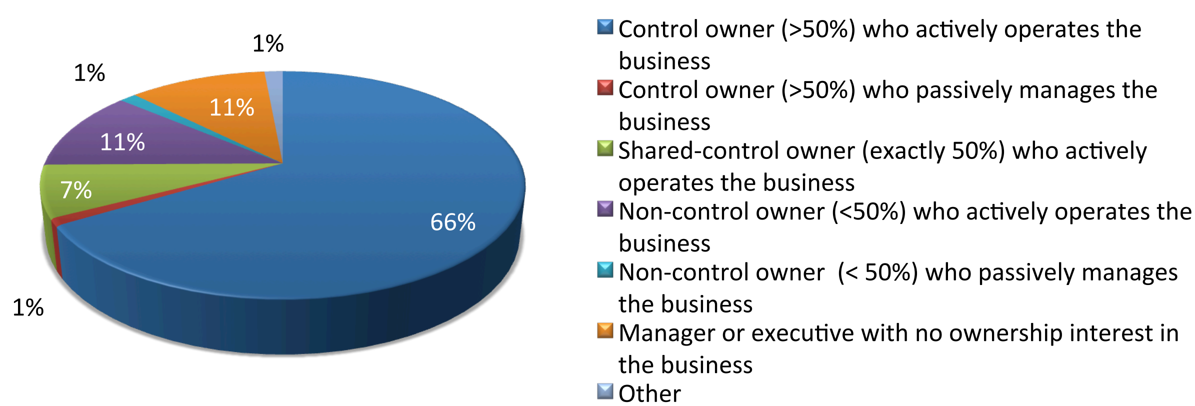
Approximately 38 percent of businesses have less than or equal to five employees.

Figure 97. Number of Employees



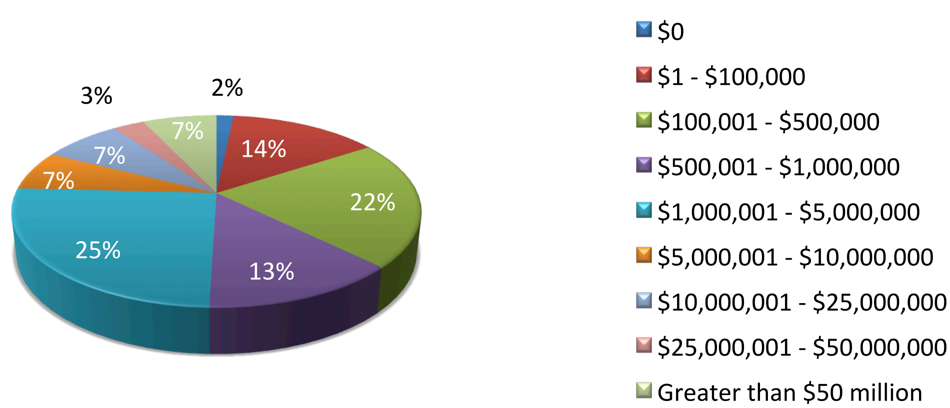
Approximately 68 percent of the respondents are active control owners of their businesses.

Figure 98. Ownership Role



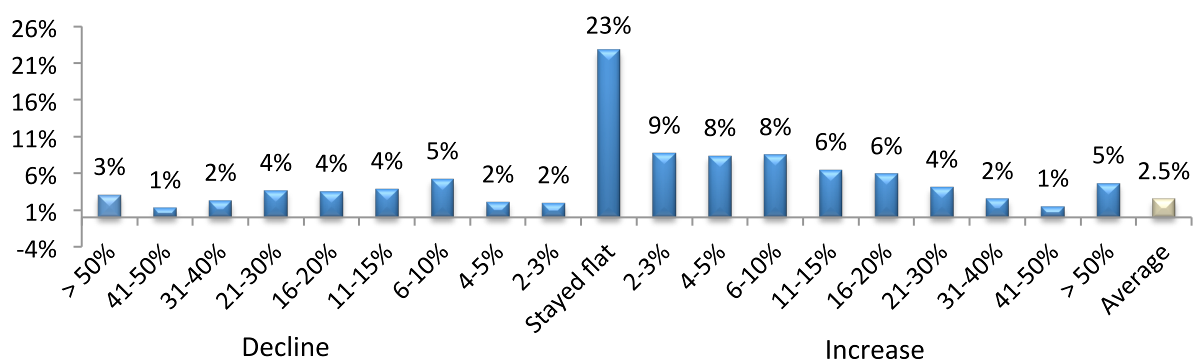
Approximately 50 percent of respondents have less than or equal to $1M in annual revenues, followed by 25 percent reporting between $1M and $5M.

Figure 99. Annual Revenues



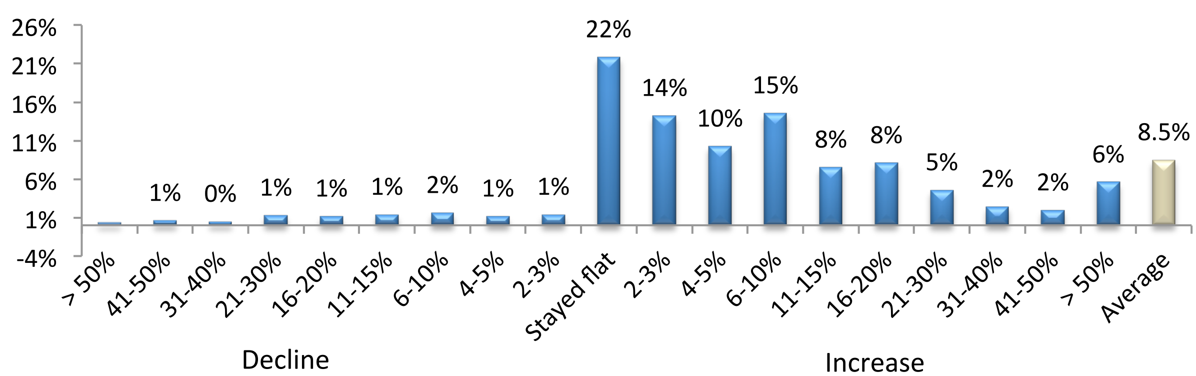
Average change in annual revenues in the last 12 months was 2.5 percent.

Figure 100. Annual Revenues Change in the Last 12 Months



On average respondents expect their annual revenues to grow by 8.5 percent in the next 12 months.

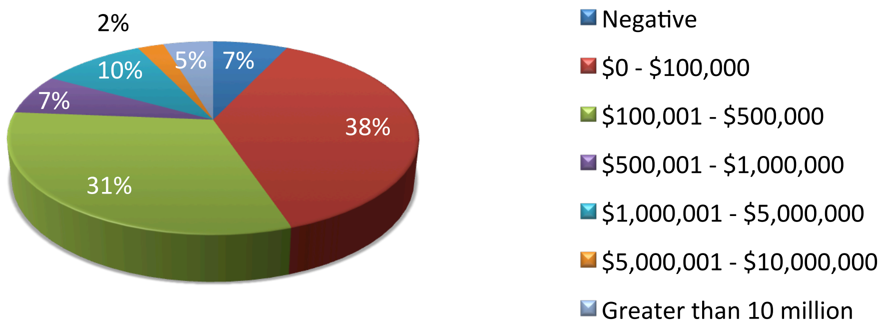
Figure 101. Annual Revenues Change Expectations in the Next 12 Months



BUSINESS OWNER cont.

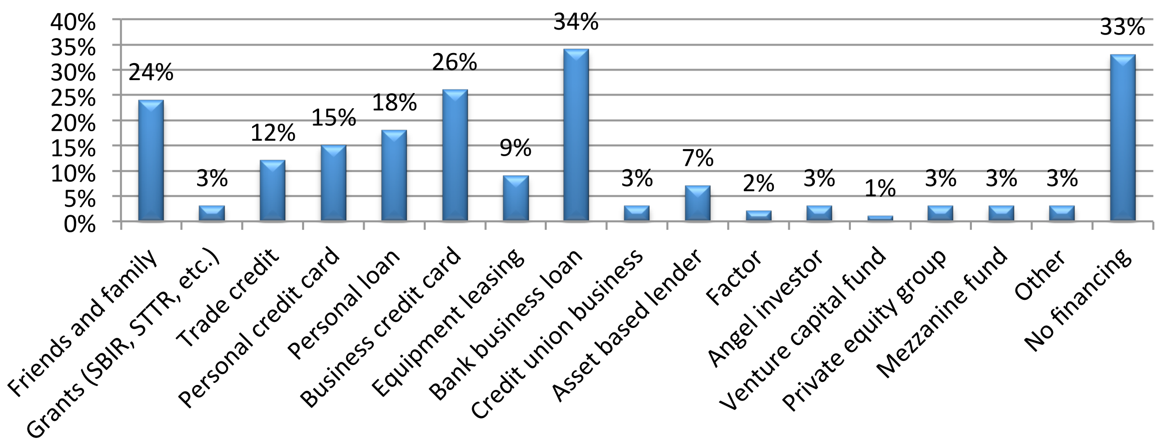
Approximately 76 percent of businesses have net income less than or equal to $500,000, 7 percent of those have negative net income.

Figure 102. Net Income



Approximately 33 percent of respondents are currently not financed by any external capital sources. Nearly 34 percent and 26 percent of respondents' businesses are financed by bank business loans and credit card financing, respectively.

Figure 103. Current Sources of Financing



Among the businesses that tried to raise capital in the last 12 months 31 percent applied for bank business loan and 69 percent were successful, whereas 37 percent of respondents did not try to raise capital from any source.

Figure 104. Capital Sources Contacted To Raise Capital in the Last 12 Months

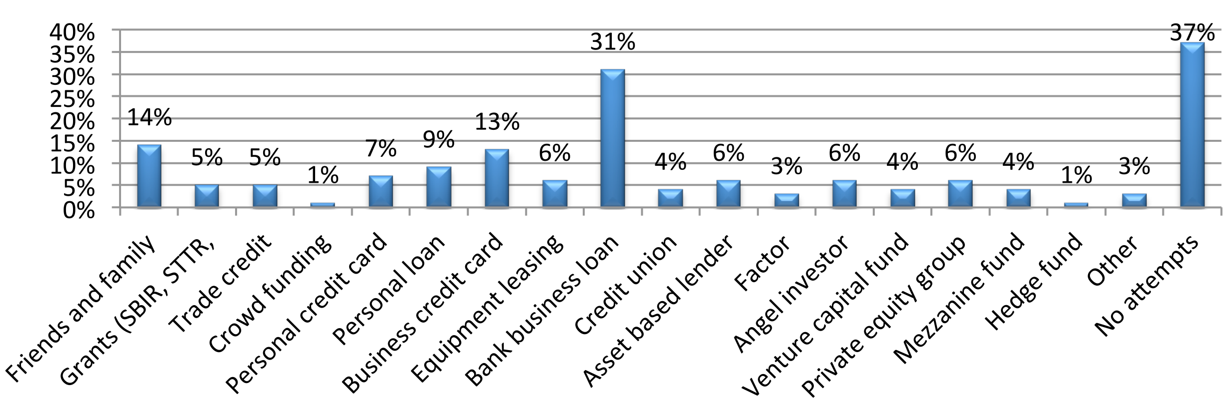
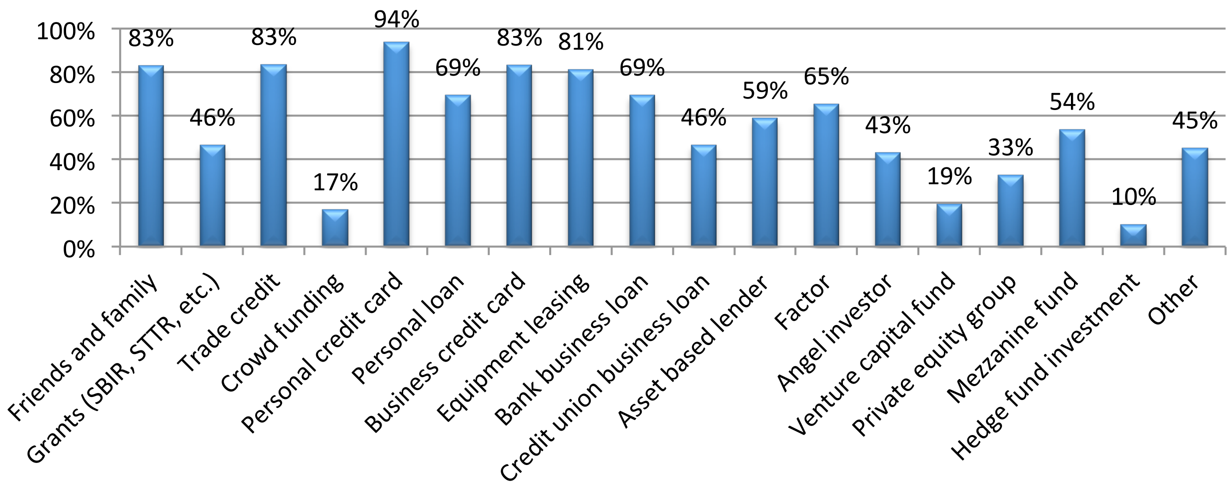
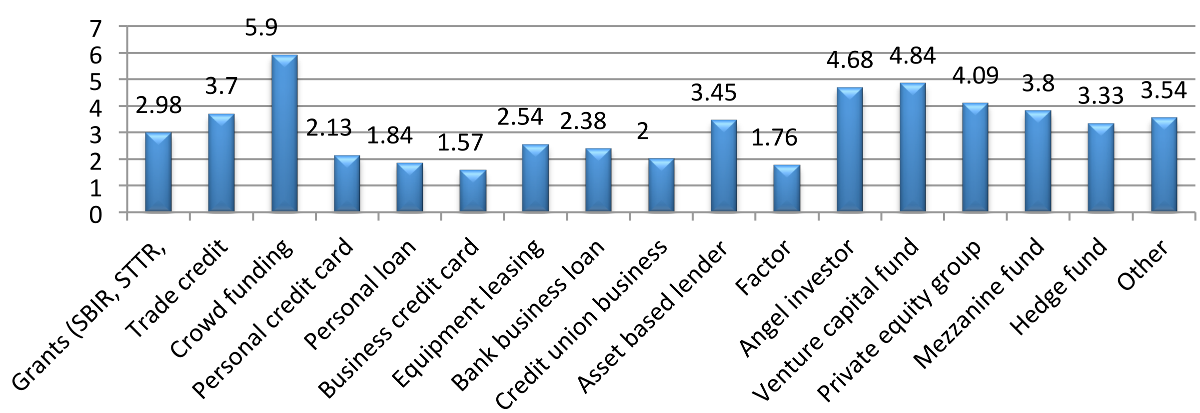


Figure 105. Success Rates



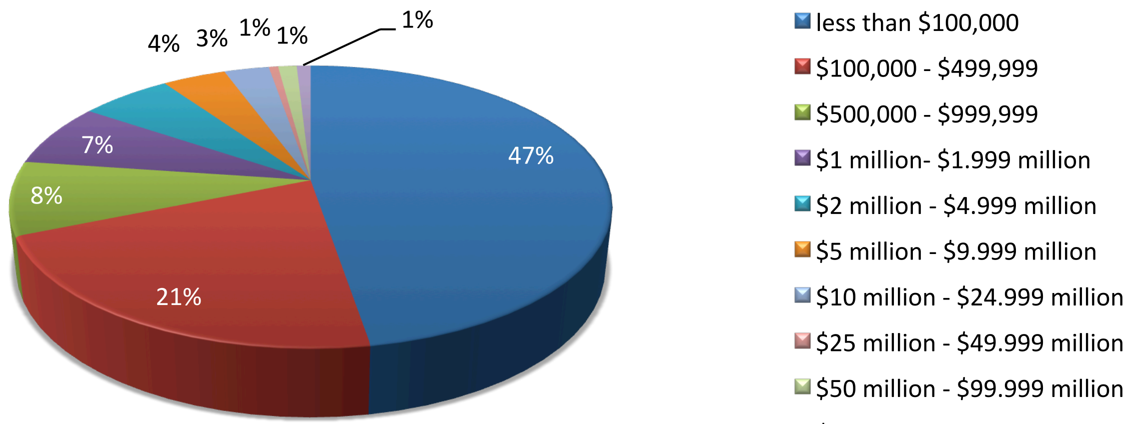
Among respondents who successfully raised capital the average number of capital providers contacted was 2.8.

Figure 106. Average Number of Capital Providers Contacted



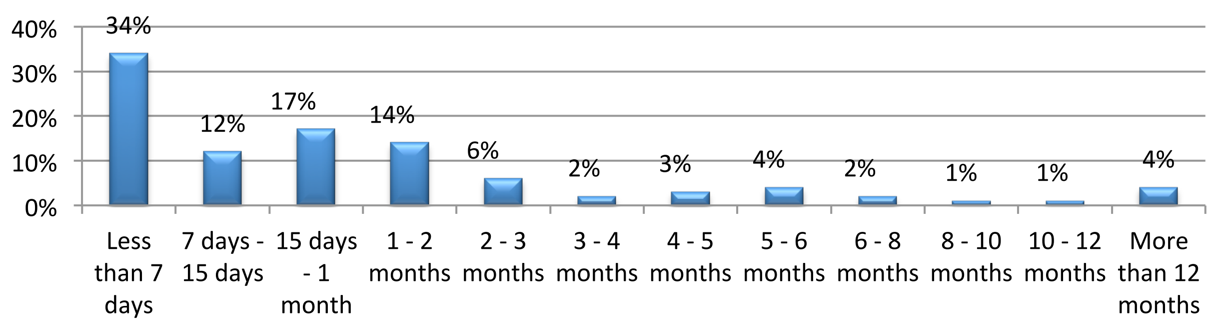
Approximately 76 percent of respondents attempted to raise less than $1 million in the last 12 months.

Figure 107. Amount of Capital Attempted to Raise in the last 12 Months



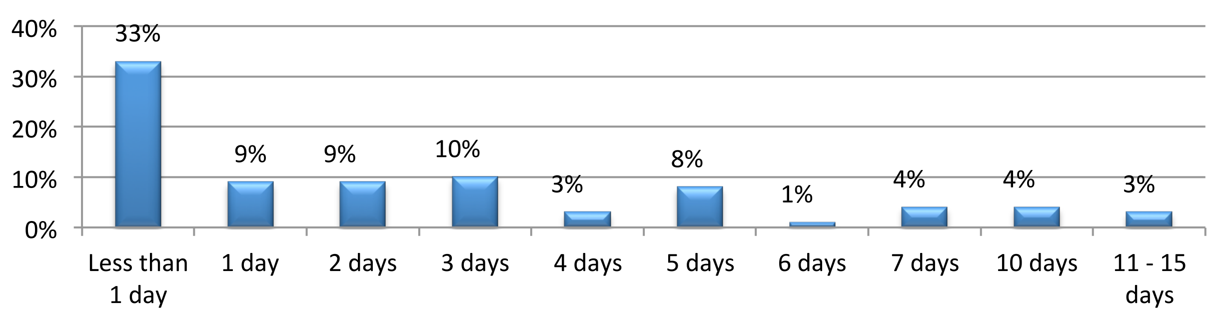
Approximately 34 percent of respondents took less than 7 days to complete financing process.

Figure 108. Average Time to Complete Financing Process in Days



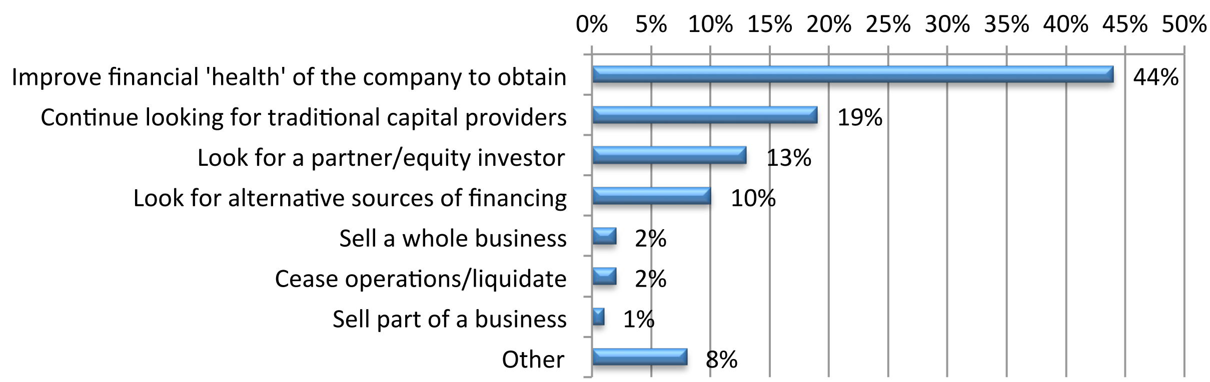
33 percent of respondents spent less than one day during the process to successfully obtain financing (time spent by all employees and hired outsiders making inquiries, submitting proposals, meeting with capital providers, furnishing documents).

Figure 109. Days Spent During the Process to Successfully Obtain Financing



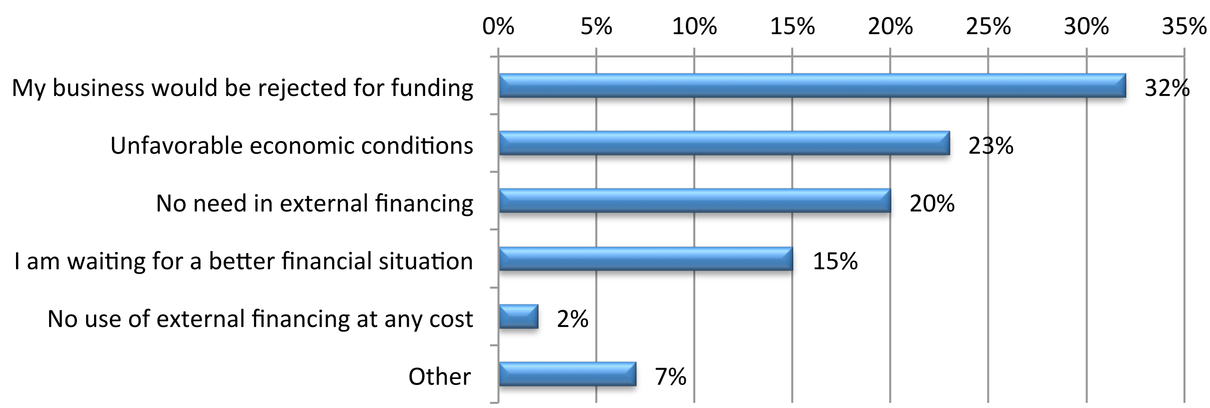
Among those respondents who were not able to obtain external financing in the last 12 months 44 percent are planning to improve the financial health of their businesses before attempting to raise capital in the future.

Figure 110. Next Steps to Satisfy Financial Needs



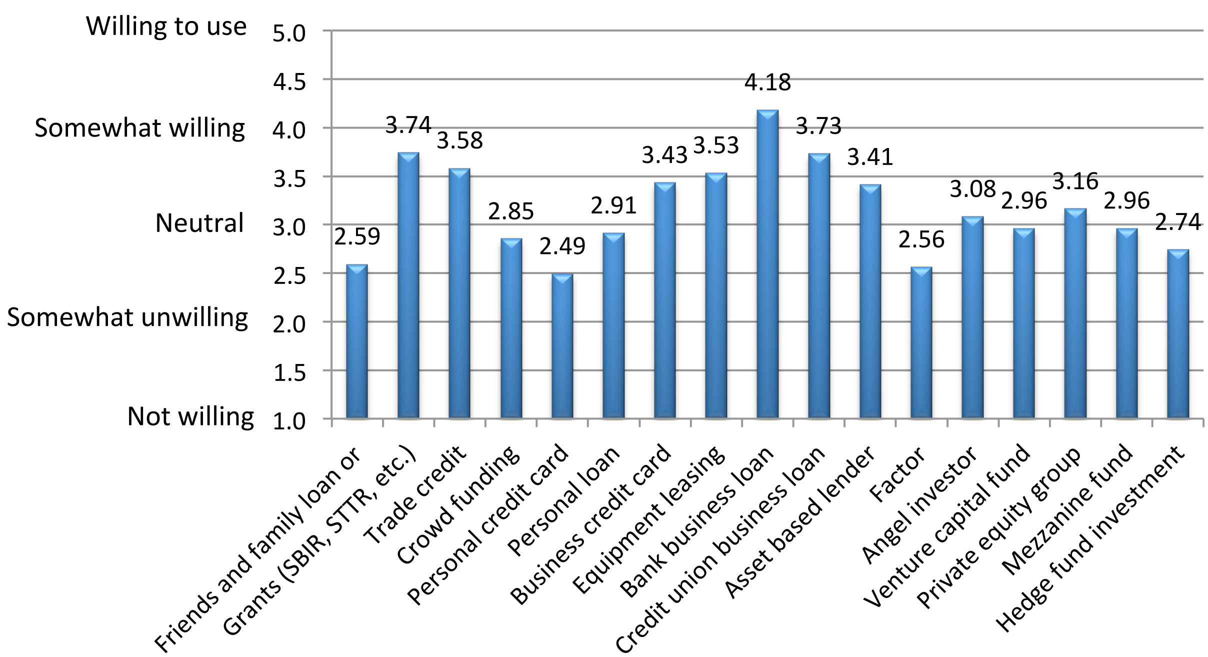
Among those respondents who did not attempt to obtain any external financing in the last 12 months 32 percent said their business would be rejected for funding, followed by 23 percent who mentioned unfavorable conditions as a main reason for not trying to obtain capital. 20 percent of respondents had no need for external financing.

Figure 111. Reasons for Not Trying to Obtain Capital in the Last 12 Months



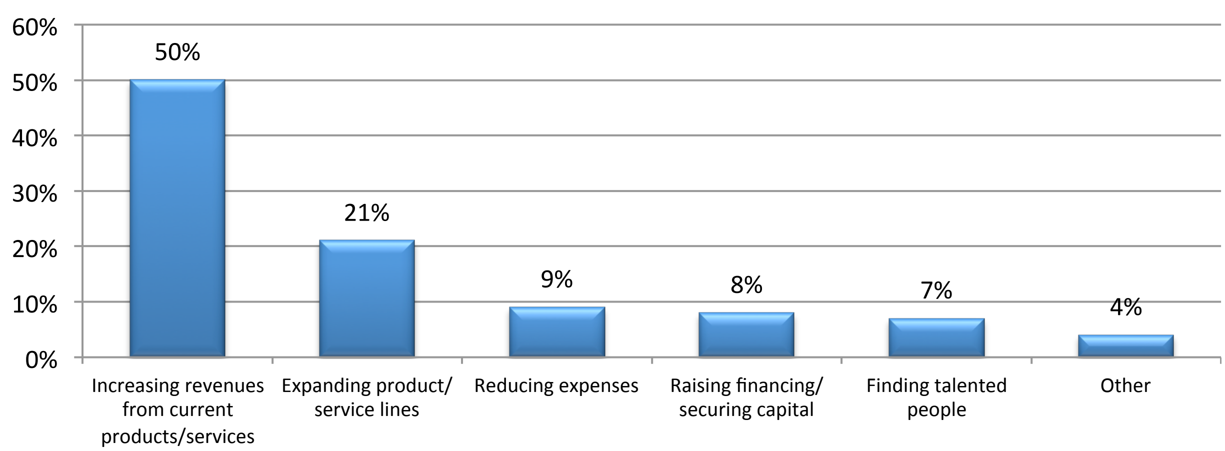
According to the respondents, “bank loans” as a category is the most appealing option to obtain financing, whereas “personal credit card financing” is the least desirable source of capital to obtain.

Figure 112. Willingness to Obtain Financing



Approximately 50 percent of respondents indicated increasing revenues from current products or services as the area their businesses are most focused on today.

Figure 113. The Most Important Area to Focus On

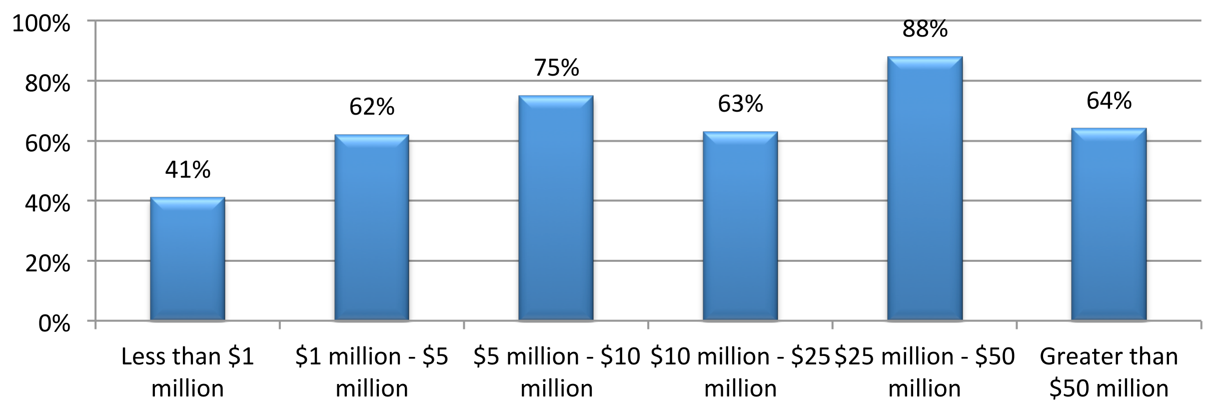


Approximately 53 percent of respondents are planning to hire additional workers in the next 12 months.

Figure 114. Plans to Hire Additional Workers in the Next 12 Months

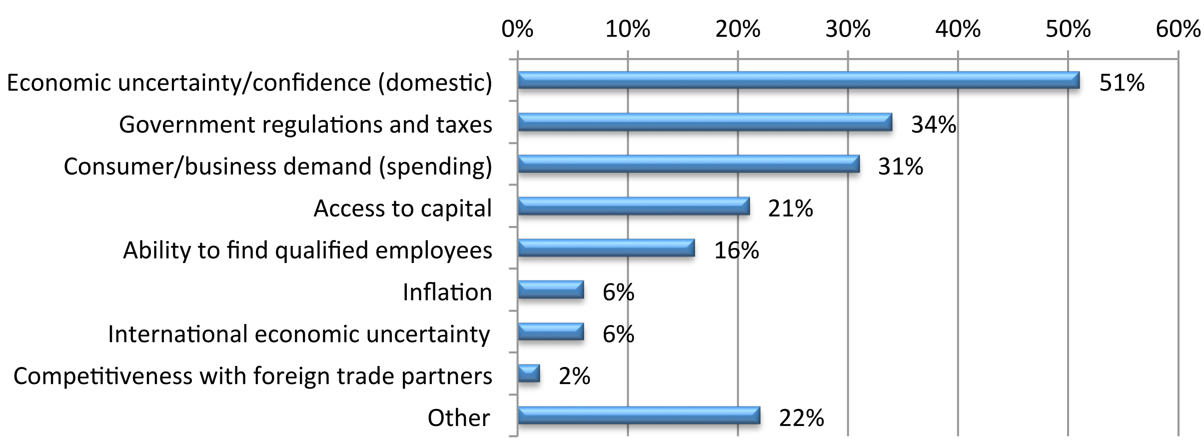
Only 41 percent of privately-held businesses whose annual revenues are less than $1 million are planning to hire additional workers in the next12 months.

Figure 115. Plans to Hire Additional Workers by Annual Revenues Sizes



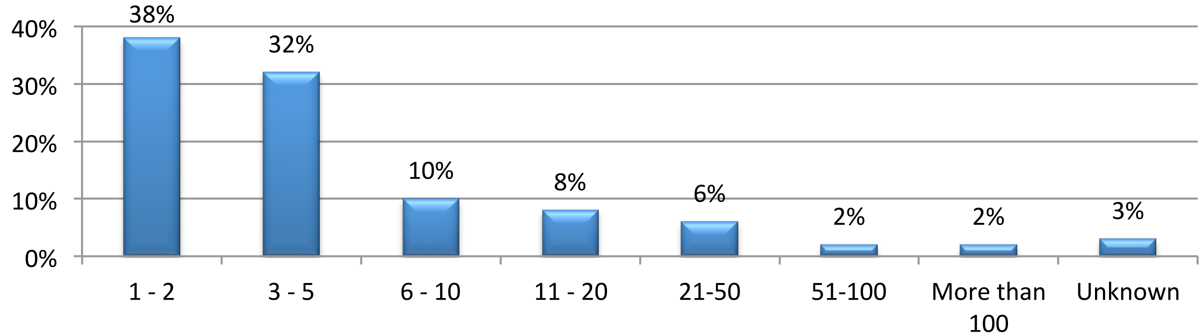
Approximately 51 percent of respondents believe economic uncertainty in the U.S. market is the reason preventing them from hiring, followed by government regulations and taxes (34 percent).

Figure 116. Reasons Preventing Privately-Held Businesses from Hiring



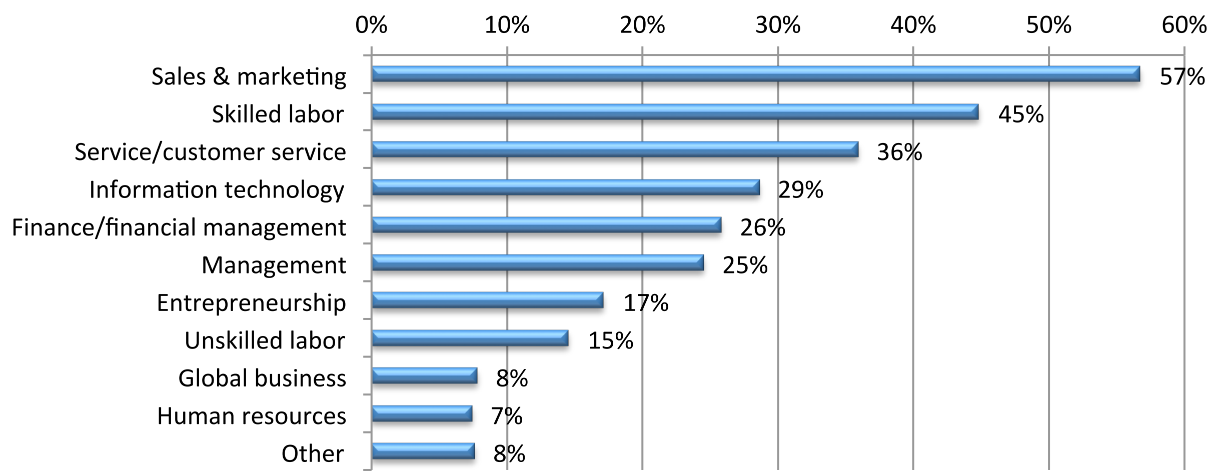
Among those respondents who do expect to hire, 38 percent are planning to hire one or two additional employees in the next 12 months.

Figure 117. Amount of Employees Planned to be Hired



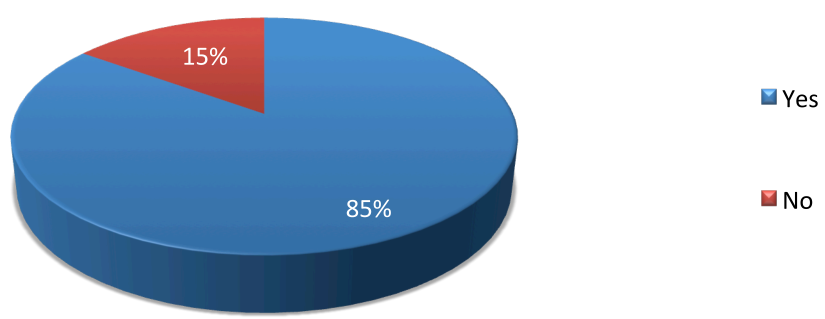
For those businesses who do plan to hire, sales and marketing skills are in greatest demand (57 percent) followed by skilled labor (45 percent) and service/customer service (36 percent).

Figure 118. The Skills in Demand for New Hires



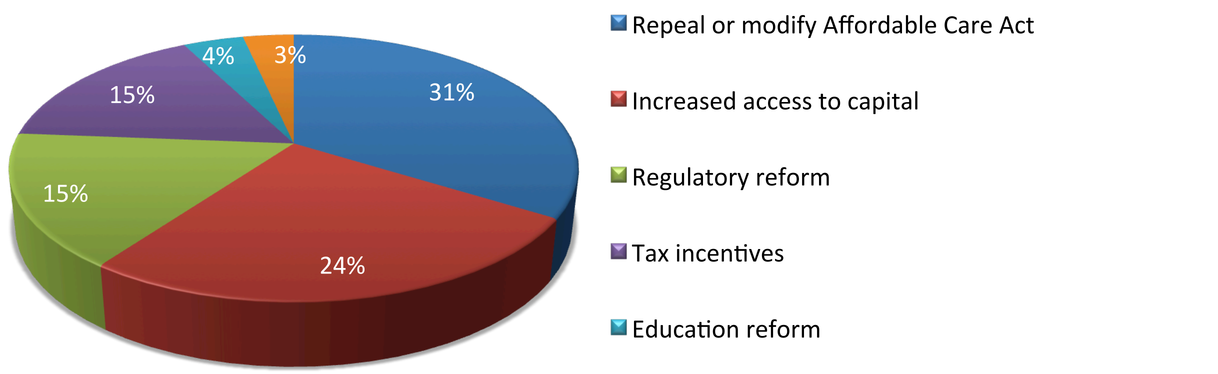
85 percent of business planning to hire indicate they would need to train those they hire.

Figure 119. Need for Training of New Hires



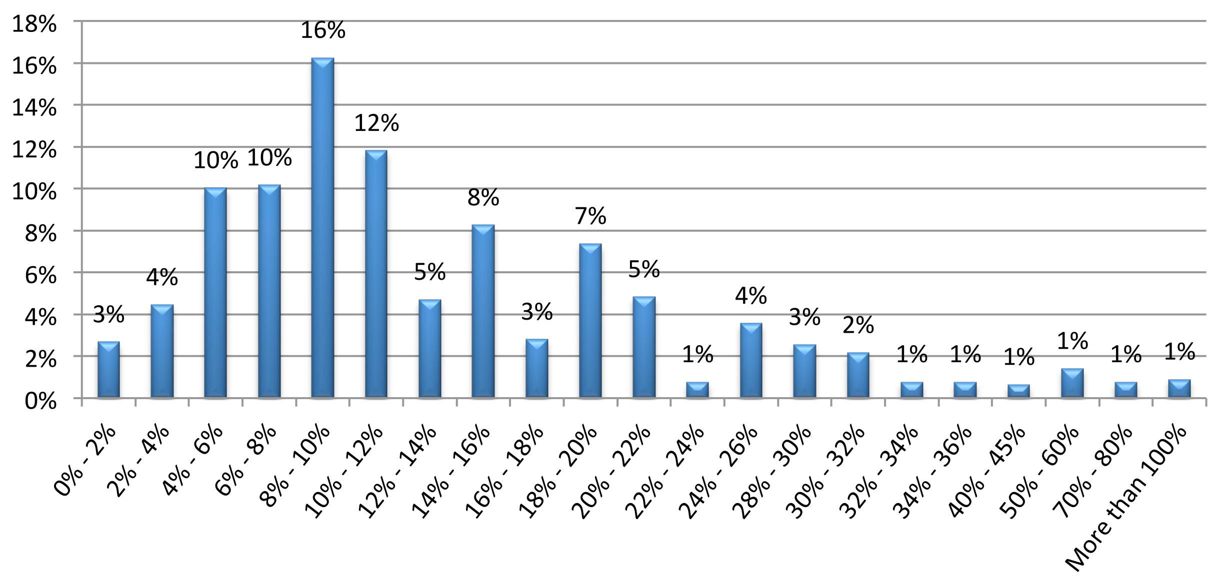
According to respondents of those policies most likely to lead to job creation in 2014, "repeal or modify affordable care act" emerged as number one (31 percent) followed by 'increased access to capital' (24 percent).

Figure 120. Government Policies to Lead to Job Creation



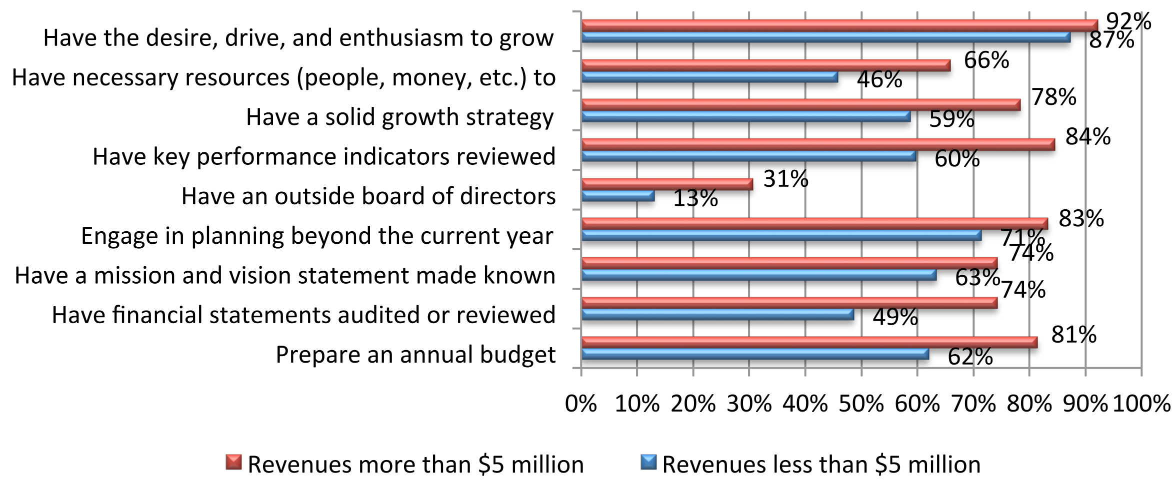
Approximately 16 percent of respondents indicated their business cost of equity capital is in the range of 8 percent - 10 percent.

Figure 121. Cost of Equity Capital



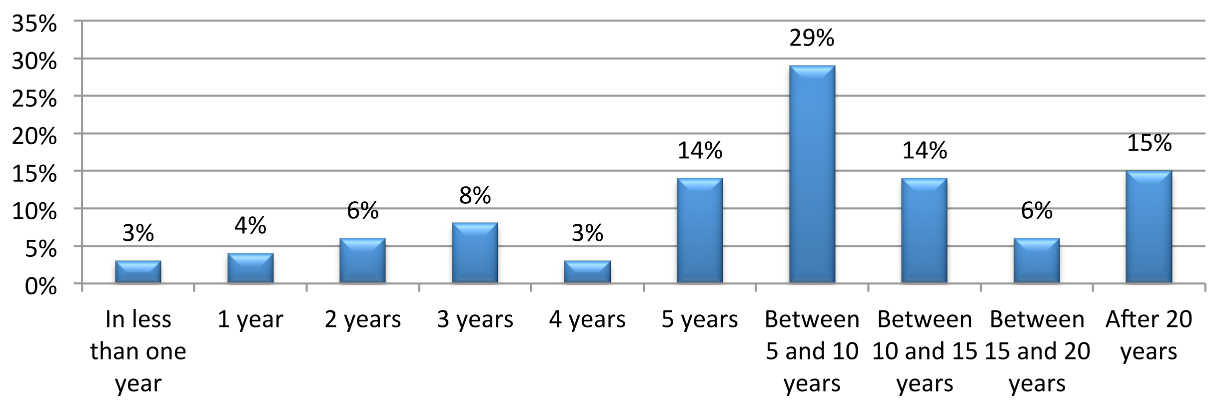
Privately-held businesses with revenues less than $5 million on average have almost the same desire to execute growth strategies (87 percent) as privately-held businesses with revenues greater than $5 million. However, privately-held businesses with smaller revenues report lower levels of necessary resources (people, money, etc.) to grow (46 percent) as compared to privately-held businesses with higher revenues (66 percent).

Figure 122. Usage of Financial Analysis by Revenue Sizes



Most of the respondents are planning to transfer their ownership interest in more than five years from now while only 3 percent plan to transfer their ownership at the first available opportunity.

Figure 123. Anticipation of the Ownership Transfer



Privately-held businesses with annual revenues less than $5 million are much more concerned about access to capital than those with revenues greater than $5 million. Larger privately-held businesses are more concerned about government regulations and taxes.

Figure 124. The Number One Issue Facing Privately-Held Businesses Today by Revenue Sizes

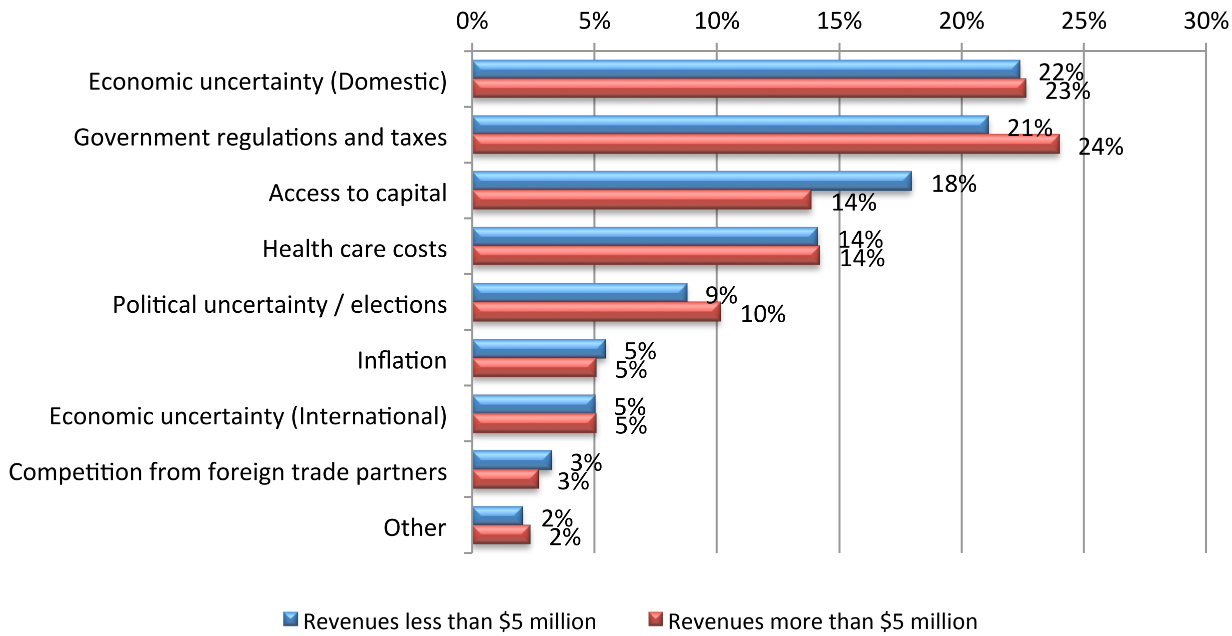
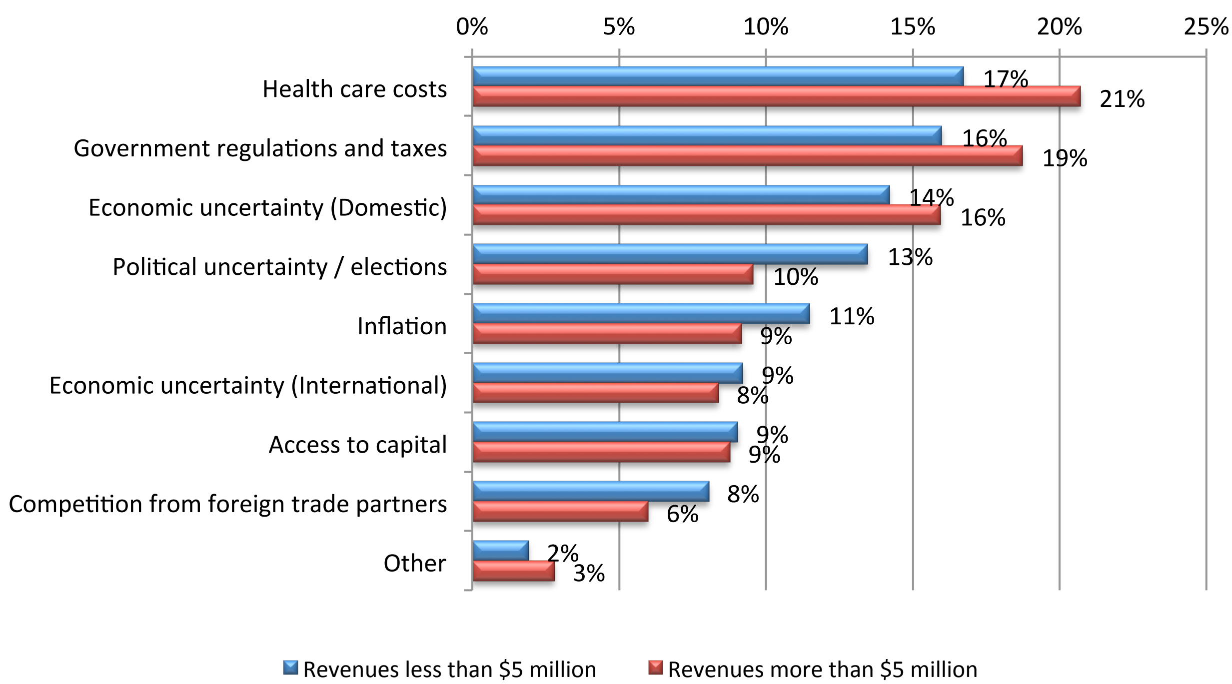


Figure 125. The Number One Emerging Issue Facing Privately-Held Businesses by Revenue Sizes



Most of respondents indicated slightly increased unit sales and prices of labor and materials, decreased access to capital, and worsened general business conditions.

Table 50. General Business and Industry Assessment: Today Versus Twelve Months Ago

Characteristics	Decreased significantly	Decreased slightly	Stayed about the same	Increased slightly	Increased significantly	% increase	% decrease	Net increase/ decrease
Unit sales	10%	14%	24%	32%	19%	52%	24%	28%
Prices of labor and materials	1%	3%	32%	49%	16%	65%	4%	61%
Net income	11%	14%	27%	32%	16%	48%	25%	22%
Inventory levels	6%	13%	52%	23%	6%	29%	19%	10%
Capital expenditures	7%	11%	43%	29%	10%	39%	18%	21%
Opportunities for growth	6%	11%	26%	35%	22%	57%	17%	40%
Access to bank loans	14%	14%	50%	18%	5%	23%	28%	-5%
Access to equity capital	15%	14%	53%	14%	5%	19%	28%	-9%
Prices of your products or services	1%	7%	44%	42%	6%	47%	8%	39%
Time to collect receivables	2%	8%	56%	25%	9%	34%	10%	24%
Number of employees	3%	8%	61%	24%	4%	29%	11%	18%
Competition	1%	10%	52%	28%	10%	38%	10%	27%
General business conditions	8%	21%	38%	27%	6%	33%	30%	3%
Appetite for risk	7%	15%	49%	23%	5%	29%	22%	7%
Probability of business closure	18%	19%	46%	12%	5%	16%	38%	-21%
Time worrying about economy	5%	14%	38%	22%	21%	43%	19%	24%

Participants of the survey believe almost all general business characteristics will increase slightly in the next 12 months.

Table 51. General Business and Industry Assessment Expectations Over the Next 12 Months

Characteristics	Decreased significantly	Decreased slightly	Stayed about the same	Increased slightly	Increased significantly	% increase	% decrease	Net increase/ decrease
Unit sales	2%	5%	20%	50%	23%	73%	6%	**67%**
Prices of labor and materials	0%	2%	31%	59%	9%	67%	2%	**65%**
Net income	2%	7%	21%	50%	20%	69%	9%	**60%**
Inventory levels	1%	7%	57%	29%	5%	35%	8%	**27%**
Capital expenditures	4%	6%	48%	33%	9%	42%	10%	**32%**
Opportunities for growth	2%	5%	28%	41%	24%	65%	7%	**57%**
Access to bank loans	6%	6%	60%	23%	5%	28%	12%	**15%**
Access to equity capital	6%	7%	61%	20%	6%	27%	13%	**14%**
Prices of your products or services	1%	4%	40%	51%	4%	55%	4%	**51%**
Time to collect receivables	1%	4%	73%	16%	5%	21%	5%	**16%**
Number of employees	1%	3%	43%	46%	7%	53%	4%	**49%**
Competition	1%	5%	59%	29%	6%	35%	6%	**29%**
General business conditions	4%	16%	45%	29%	6%	35%	20%	**15%**
Appetite for risk	5%	10%	54%	25%	6%	31%	15%	**16%**
Probability of business closure	17%	19%	53%	7%	3%	10%	37%	**-27%**
Time worrying about economy	6%	14%	48%	18%	14%	32%	20%	**12%**

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Craig R. Everett is an assistant professor of finance at Pepperdine University's Graziadio School of Business and Management and director of the Pepperdine Private Capital Markets Project. His teaching and research interests include entrepreneurial finance, private capital markets, business valuation and behavioral corporate finance.

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His research has appeared in the *Wall Street Journal*, CNBC, *USA Today*, and the *New York Times*, been published in a number of journals and been presented at domestic and international conferences. Craig Everett is member of the Beta Gamma Sigma Honor Society, Financial Executives International, and the Los Angeles World Affairs Council. Dr. Everett is a certified mergers & acquisitions advisor (CM&AA), and a registered investment advisor (RIA) with the state of California.

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