

Overview

Q1 2017 merger and acquisition activity for Distributors of Maintenance, Repair, and Operations (MRO) products was slightly below Q4 2016, following the general trend in transaction activity since Q4 2015. Q1 2017's 144 transactions were down 37% from Q4 2015's peak of 228 transactions. Part of M&A activity decline is due simply to limited deal flow availability. As the Distribution M&A market has matured, the availability of targets has decreased because many likely sellers have completed transactions.

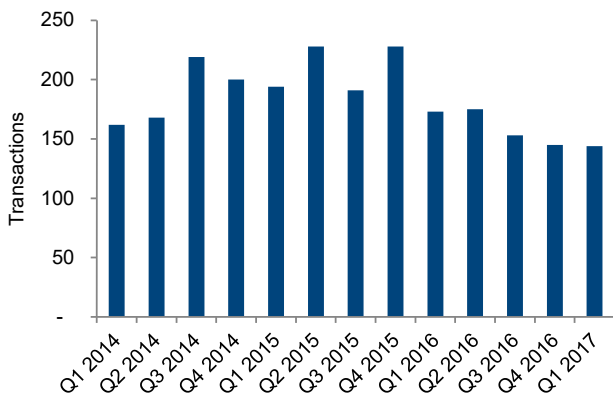
These market dynamics are interesting, on examining the public peer group's operational and financial performance. The MRO industry's overall performance slowed down over the past year, driven by decreased demand from primary end markets like oil and gas, and stagnant growth in others like industrial manufacturing and electrical. According to IBIS World, from 2012 to 2017 revenue growth amounted to 0.2% and is expected to be approximately 1% for the five years ending 2022 (slower than projected GDP growth). As seen on the next page, these metrics are reinforced by recent performance in the industry's largest public-company peer group—decreased quarterly revenue, EBITDA, and EBITDA margins since late-2015. In fact, quarterly revenue has decreased 14% since its peak in Q1 of 2015, while

EBITDA margins have decreased approximately 240 bps over the same period.

Despite decreased transaction volume observed in recent quarters, valuation multiples for the public-company peer group remain robust with an average 11.1x EBITDA at the end of Q1 2017. While growth and margins within the industry have decreased, most industry analysts maintain a positive outlook for the industry, citing stable profits, increased spending by manufacturers to maintain aging equipment, and protection from offshoring.

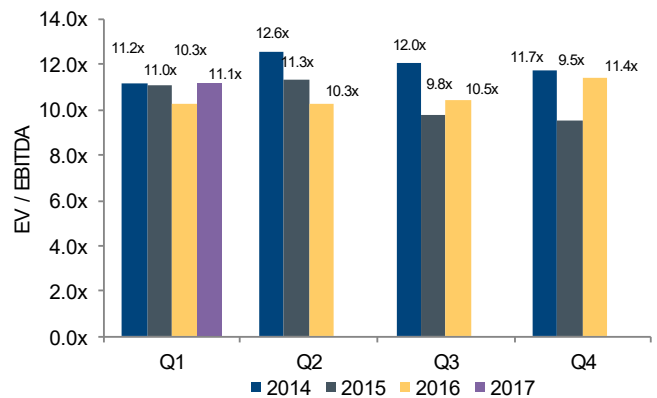
Notably, certain characteristics of the MRO industry create an attractive M&A landscape for both strategic and financial acquirers. The requirement that MRO facilities locate near customers keeps the industry highly fragmented (the largest 50 distributors represent 30% of market share, according to Morningstar). Furthermore, as large industrial manufacturers look to increase equipment longevity, operate close to full utilization, and decrease inventory on hand, they seek MRO suppliers with diversified offerings in terms of SKU-count and geography. EdgePoint believes MRO distributors seeking additional growth will attempt to grow via acquisition to expand their SKUs, value-added services, and footprint.

M&A Transactions by Quarter



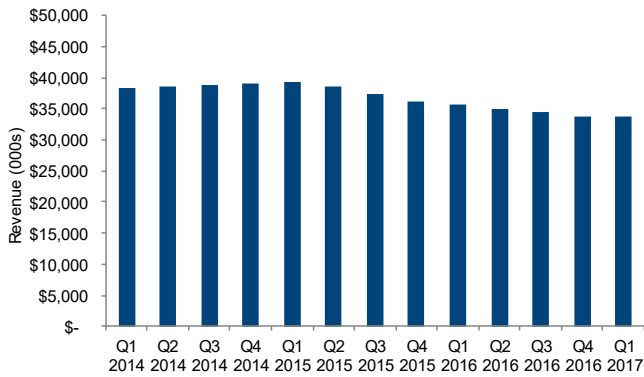
Source: CapIQ

EV / EBITDA by Quarter



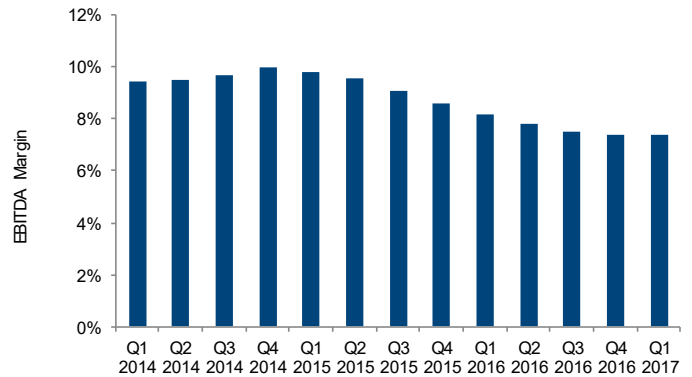
Source: CapIQ

Revenue



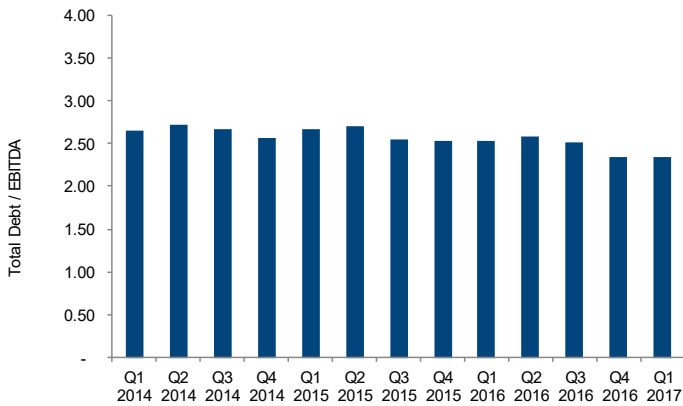
Source: CapIQ

EBITDA Margin



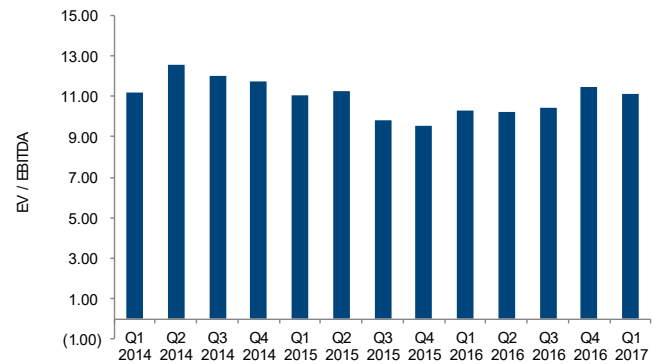
Source: CapIQ

Total Debt / EBITDA



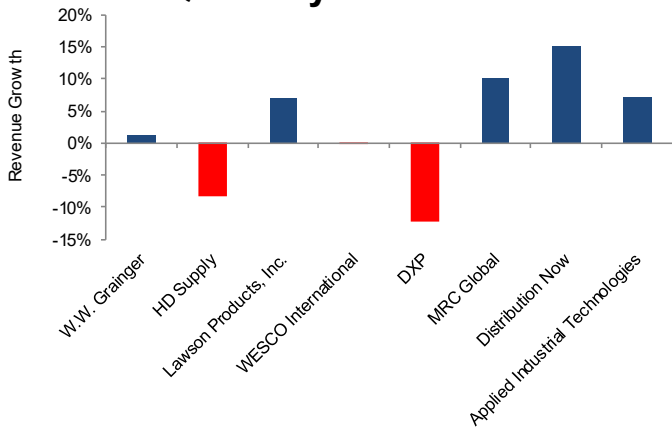
Source: CapIQ

Enterprise Value / EBITDA



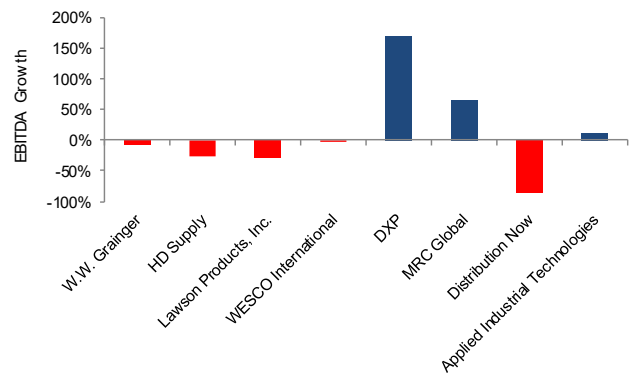
Source: CapIQ

YoY Quarterly Revenue Growth



Source: CapIQ

YoY Quarterly EBITDA Growth



Source: CapIQ

The Maintenance, Repair, and Operations public peer group indexed above includes W.W. Grainger (NYSE: GWW), HD Supply (Nasdaq: HDS), Lawson Products (Nasdaq: LAWS), WESCO International (NYSE: WCC), DXP Enterprises (Nasdaq: DXPE), MRC Global (NYSE: MRC), Distribution Now (NYSE: DNOW), and Applied Industrial Technologies (NYSE: AIT)

Reported M&A Activity

Despite lower transaction volume reported in Q1 2017, there were a few notable M&A transactions in the quarter. The vast majority of completed transactions were by strategic acquirers looking to expand via acquisitions to augment tepid organic growth. Of the 145 MRO transactions completed in Q1 2017, strategic acquisitions accounted for 88%. For financial buyers to represent less than 25% of transactions is an oddity in this recent M&A market.

Large MRO providers often seek acquisition targets that expand their product offering and geographic footprint. Applied Industrial Technologies displayed this investment thesis in acquiring Sentinel Fluid Controls in March 2017. A frequent acquirer, Applied Industrial Technologies purchased the distributor of hydraulic and lubrication components to expand its fluid-



power division, reaching additional automotive, industrial, and mining customers. Another example is Crescent Electric Supply's acquisition of Mesco Corporation. Mesco is a regional supplier of electrical products in southern Ohio and provides Crescent the opportunity to reach additional geographies and customers. Both transactions represent a robust enterprise investing in a capable mid-market company to expand product and service offerings.



Financial buyers also continue to seek investments in the MRO space, with an investment thesis like strategic buyers. These buyers target add-on acquisitions to grow existing platform companies—contemplating a larger future sale. Mill Street Venture's Q1 2017 acquisition of Calico Industries was one such transaction.

Noteworthy Maintenance, Repair & Operations Transactions | Q1 2017

M&A Closed Date	Target/Issuer	Buyers/Investors	Target Description	Price (\$USDmm)	Target Country
1/1/2017	Mesco Corporation	Crescent Electric Supply Co., Inc.	Distributes electrical products including pump rebuild kits, mechanical seals, shaft sleeves, and gaskets.	ND	United States
1/3/2017	Jensen Tools & Supply	TestEquity LLC	Supplies products and services for electronics manufacturing, assembly, diagnosis, and repair professionals.	ND	United States
1/3/2017	Kevin Distributing, Inc.	IDI Distributors Inc.	Distributor of spray polyurethane foam for insulation and elastomeric coatings, as well as single and plural component proportioning spray equipment, parts and supporting services.	ND	United States
1/4/2017	Soluble Solutions Inc.	Butler Brothers Supply Division Inc.	Distributes industrial tools and accessories to the aerospace, medical, automotive, and industrial manufacturing industries.	ND	United States
1/9/2017	Eco Insulation Supply, Inc.	Beacon Roofing Supply, Inc. (NasdaqGS:BEEN)	Distributes insulation products.	ND	United States
1/10/2017	J&N Auto Electric, Inc.	Arrowhead Electrical Products, Inc.	Distributes rotating electric units and parts for OEM starters and alternators, including starters, service parts, DC motors, electrical accessories, gauges and instrumentation.	ND	United States
2/10/2017	Calico Industries, Inc.	Mill Street Ventures LLC	Distributes restaurant equipment, foodservice supplies, and janitorial supplies.	ND	United States
2/21/2017	AquaPower Ltd	StoneAge Inc.	Distributes waterblast tools and equipment, including nozzles, jets, jetting guns, and foot valves.	ND	United Kingdom
2/20/2017	Primet Fluid Power, Inc.	Ritter Technology, LLC	Distributes hydraulic, pneumatic, lubrication systems, and automation components.	ND	United States
2/7/2017	Brammer plc	Advent International Corporation	Distributor of industrial maintenance, repair, and overhaul products such as bearings and seals, mechanical power transmission parts, electric power transmission parts, fluid power components, and tools and maintenance products.	\$417	United Kingdom
2/2/2017	TMC Materials Inc.	Ravago Holdings America, Inc.	Supplier of chemical raw materials and containers to various industrial manufacturers.	ND	United States
2/1/2017	Rubber Supply Co., Inc.	R/W Connection, Inc.	Distributes hoses, valves, belts, and other products made of rubber and metal.	ND	United States
2/1/2017	Global EDM Supplies, Inc.	Single Source Technologies, Inc.	Distributes EDM machine parts and supplies, including wire, filters, wear parts, resin, fluids and lubricants, and electrodes. It also offers customer support and preventative maintenance services.	ND	United States
3/1/2017	IMCD US, LLC	IMCD N.V. (ENXTAM:IMCD)	Engages in the distributions of specialty chemicals and food ingredients.	ND	United States
3/6/2017	Hodell-Natco Industries, Inc., Fastener and Master Distribution Business	Lindstrom Metric, LLC	Distributes packaged fastener and master products.	ND	United States
3/21/2017	Cole-Parmer Instrument Company, LLC	Golden Gate Capital	Supplies laboratory and industrial fluid handling products, instrumentation, equipment, and supplies.	ND	United States
3/6/2017	Sentinel Fluid Controls	Applied Industrial Technologies, Inc.	Offers hydraulic and lubrication components, systems, engineering, service and repair to industrial customers.	ND	United States
3/14/2017	LMS Bearings Inc.	P.T. International Corp.	Supplies power transmission products including bearings, cam followers, oil seals, timing belts, pulleys, hoses, hose fittings, engineered class chains, gear motors, custom machined parts.	ND	United States
3/28/2017	The BAASE Company, Inc.	Tozour Energy Systems, Inc.	Distributes plumbing, heating, and air conditioning products for commercial customers.	ND	United States
3/30/2017	Warehouse Equipment Products Inc	Crown Battery Manufacturing Company	Distributes and services industrial batteries and chargers.	ND	United States

Drivers of Future M&A Activity

MRO Distribution industry performance over the past two years is characterized by decreasing revenues and EBITDA margins, and was influenced by lower demand from major end markets and the emergence of e-commerce competitors in the industry.

Although the largest MRO Distribution end markets—like industrial manufacturing—are growing at modest rates, this growth is overshadowed by declines in oil and gas and other energy segments. The net impact on the public peer group has been a 14% decrease in quarterly revenue since Q1 of 2015.

Meanwhile, MRO Distributors experience margin erosion as revealed by decreasing EBITDA margins. The industry experiences significant disruption from e-commerce platforms, and more manufacturers selling direct to customers rather than through distribution. E-commerce marketplaces like Amazon Supply allow manufacturers of industrial fluids, adhesives, fasteners, and other MRO supplies to interact directly with customers. Although a new market entrant, Amazon Supply already offers 2.2 million industrial-supply products compared to Grainger’s 1.2 million (despite having the largest e-commerce platform among traditional MRO Distributors). The increasing role of e-commerce activity in the industry fosters significant pricing pressure and a general decrease in gross margins.

Due to the MRO Distribution industry’s rapidly changing landscape, EdgePoint expects M&A activity in the MRO segment to continue at current levels, as strategic participants seek to maintain a competitive advantage through consolidation. Despite stagnant growth in the overall industry, high fragmentation levels and significant pressure posed by dominant players like Amazon Supply have created an environment ripe for another wave of M&A activity .



Representative EdgePoint Transactions

Sell-Side Advisory

E.J. Thomas Company and AristoCraft Supply have sold to Strength Capital Partners

Sell-Side Advisory

S.G. Morris Company has sold to Applied Industrial Technologies

Sell-Side Advisory

Motor City Fastener, Inc. has sold to Kian Capital

Sell-Side Advisory

Lake Erie Abrasive & Tool has sold to Motion Industries

Service Offerings

Sell-Side Advisory

- Third-Party Sale
- Sale to Management
- Recapitalization
- ESOP

Buy-Side Advisory

- Buy-Side Search
- Buy-Side Diligence & Financing
- Targeted Buy-Side
- Management Buyout

Financing Advisory

- Senior & Sub Debt
- Asset Based Lending
- Mezzanine Debt
- Private Placements



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M&A
Advisory

RESULTS *with*
INTEGRITY™