VALUE FOCUS

Equipment Dealer Industry




Mid-Year 2014

www.mercercapital.com

General Overview of Equipment Dealers

The equipment dealership sector consists primarily of closely held, private entities that are contractually allied to a principal original equipment manufacturer ("OEM"). The business model of most equipment dealers is relatively similar to those of other dealership models including the automotive, trucking and vocational vehicle segments. Dealers are typically granted territory in which to sell and service an OEM's products using organizational structures and operating systems mandated by their respective OEMs. Generally speaking, equipment dealer performance corresponds to general economic activity and territory traits.

More than just wholesalers, equipment dealers are the channel through which their respective OEMs penetrate markets, providing territory development, sales, leasing, rental, and parts & service to commercial, contractor, industrial and governmental customers, usually within an exclusive geographic area. Accordingly, whether the dealer's equipment concentration is agricultural, construction, mining, transportation, material handling, or otherwise, the economic characteristics and commodity concentrations of each market dictate the product focus of each dealer regarding core line mix as well the dealer's complimentary and adjacent OEM portfolio. Most OEMs segregate their product lines by target market, using dealerships specifically for each product segment (construction, agriculture, small engine, etc.) although many dealers, such as those in the Caterpillar system, have more turnkey product offerings. Each dealer's primary OEM exerts significant influence regarding the dealer's other brand offerings because brand purity is a core mandate for most OEMs as is a well-crafted assemblage of portfolio offerings for the dealer's territory.

The largest and most recognizable OEMs are world-wide operators whose manufacturing facilities and end markets span the globe. Dealership models for the large OEMs vary significantly by the dealer's native market and the OEMs overall strategy. For example, at year end 2013, Caterpillar's approximately 50 U.S. dealers were all closely held, private entities whose operations were conducted in geographically contiguous territories. In contrast, two of the Canada-based dealers are publicly traded, one of these has multi-national operations (and is the world's largest CAT dealer) and the other has a more diverse and industrial focused revenue stream.

The table provides perspective on the scope of equipment offerings typically found in an equipment dealer's portfolio. Equipment dealers can be highly specialized regarding their product offerings, as may be the case for dealers of heavy lift machines and cranes, or may have offerings that cover a wide variety of market needs as is typical of construction equipment dealers. Many dealers carry products outside their core OEM product categories as a way of diversifying their revenue streams to benefit from territory opportunities and market trends as well as to mitigate the effects of seasonality, industry demand, customer concentration, and other downside exposures related to the core OEM product category. Large equipment dealers general fall into one of these industry groupings: construction and related; agriculture; and material handling. These dealers require relatively specialized capabilities and knowledge to service their customers. Differentiation and diversity of product mix due to territory is more prominent for dealers in the construction industry as the prevalence of forestry, mining, energy, and other resources varies significantly by geographic region. Material handling dealers are typically more homogenous in their product offerings although the capabilities of lift-trucks can vary greatly depending on a given territory's industrial, transportation and distribution infrastructure.

Markets and Industries Served

Agriculture	Forestry	Material Handling	Quarry, Aggregates & Cement
Construction	Governmental & Defense	Mining	Remanufacturing
Customer Services	Insurance	OEM Solutions	Rental
Demolition & Scrap Recycling	Landscaping	Oil & Gas	Safety
Electric Power	Locomotive & Railway	Paving	Training
Generation	Maintenance & Repair	Pipeline	Technology & Solutions
Financing	Marine	Power Plants	Waste

Agricultural Equipment Industry[1]

Agricultural equipment is used primarily for the production of food, fiber, feed grain and feedstock for renewable energy. Certain equipment is purchased for home and garden applications, and maintenance of commercial, residential and government properties. Deere & Company (DE), CNH Industrial N.V. (CNH) and AGCO Corporation (AGCO) are the largest global manufacturers of agricultural equipment and supply a full line of equipment and parts that address the primary machinery requirements of farmers. In addition to the major manufacturers, numerous short-line manufacturers produce specialized equipment that addresses regional and niche requirements of both corporate and hobby farmers. Agricultural equipment manufacturers typically grant dealers in the U.S. authorized store locations, not exclusive territories, to distribute their products.

There are many factors that influence demand for agricultural equipment, parts and repair and maintenance services, including commodity markets, interest rates, government policies, tax policies, weather and general economic conditions. Any of these conditions can change materially in a short time period, creating volatility in demand for products and services. Federal legislation, such as the recently enacted Farm Bill, attempts to stabilize the agriculture industry through various policies including (i) commodity programs consisting of direct, counter-cyclical and price support payments to farmers; (ii) conservation programs; (iii) crop insurance programs; and (iv) disaster relief programs. These various federal policies reduce financial volatility and help ensure that farmers operate their farms and equipment during economic down cycles, thus stabilizing demand for equipment, replacement parts, and repair and maintenance services.

Construction Equipment Industry[2]

Construction equipment is purchased primarily for commercial, residential and infrastructure construction, as well as for demolition, maintenance, mining, energy production and forestry operations. The market for construction equipment is segmented across multiple categories including earth moving, lifting, light industrial, asphalt and paving, and concrete and aggregate equipment. As in the agricultural equipment market, distribution of construction equipment in the U.S. is executed primarily by manufacturer authorized dealers; however, manufacturers' dealership agreements in the construction industry typically assign exclusive distribution territories.

Construction machinery is generally divided into "heavy" and "light" subgroups. Heavy machinery includes large wheel loaders, large tracked excavators, cranes, crawler dozers, motor graders and articulated haul trucks. Light machinery includes backhoe landscape tractors, forklifts, compact excavators and skid steers. Heavy machinery is generally purchased by construction companies, municipalities, local governments, rental fleet owners, quarrying and mining companies, waste management companies and forestry-related organizations. Typically, light machinery is purchased by contractors, rental fleet owners, landscapers, logistics companies, farmers and recreational users. Although demand for construction equipment is affected by weather and seasonal factors, it is usually less susceptible to seasonal changes than the agricultural equipment industry.

Demand for construction equipment is driven by several factors, including (i) public spending on roads, highways, sewer and water projects, and other public works projects; (ii) public and private expenditures for the energy and mining industries, which is driven in part by demand for fossil fuels, metals and other commodities; and (iii) general economic and market conditions of the construction sector for residential and commercial buildings.

Material Handling Industry

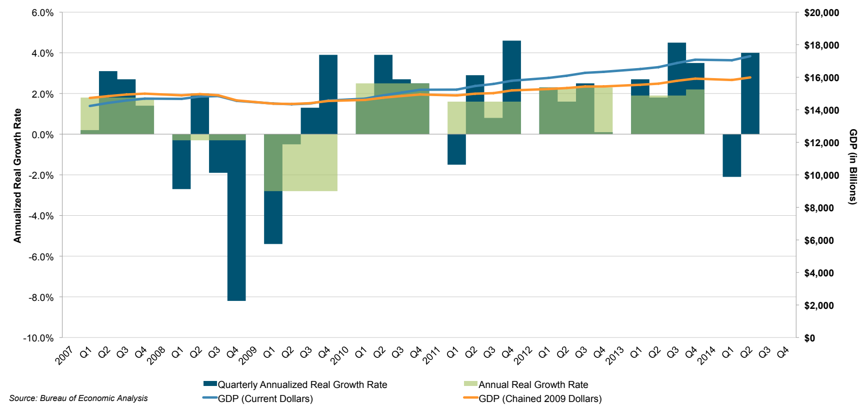
The material handling industry encompasses the equipment, systems and technology solutions for managing, transporting and storing a wide variety of bulk materials, processed goods and final products. There are numerous diverse OEMs that manufacture lift trucks, racking systems and mechanical conveyors that comprise the industry. Material handling equipment is a vital aspect of industry supply chains and distribution channels in the economy. Material handling equipment is used by virtually all sectors and industries to manage goods and materials through the processing, manufacturing, staging, and transportation phases in route to final markets.

Key players in the lift truck segment of the industry include Toyota, Linde, Hyster-Yale, Mitsubishi, and Crown. Lift trucks are the principal product of the industry's dealer network. OEMs and their underlying brands and products are differentiated by size and load capacity, fuel type, and wheel type. For example, machines operated in close, environmentally contained facilities are typically powered by electric batteries while large machines operating in open environments may be diesel powered in order to manage large and/or heavy loads. Demand for material handling equipment is driven by several factors but is principally correlated to the overall economy and the movement of goods and materials through industrial, commercial and consumer markets.

Macroeconomic Overview

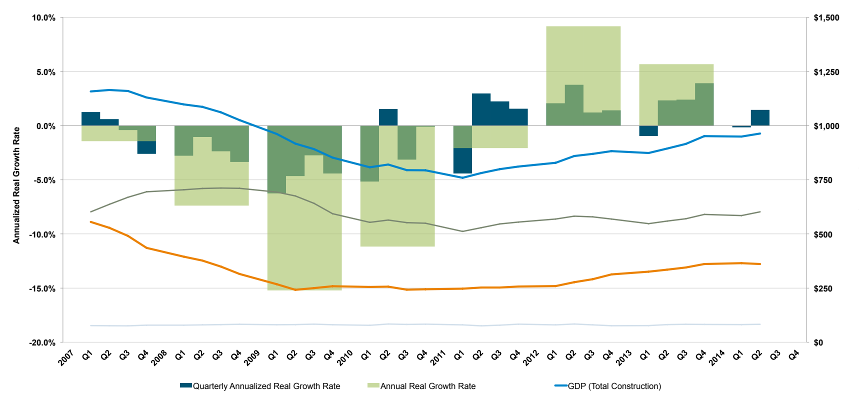
Gross Domestic Product

The real Gross Domestic Product ("GDP") increased 4.0% during the second quarter of 2014, following a decline of 2.1% in the first quarter of 2014 and an increase of 3.5% in the fourth quarter of 2013. Economists attribute the GDP growth in part to improving customer spending, which was in turn driven by labor market improvement. Following last quarter's slower growth in durable good purchases, this quarter's purchases of durable goods rose at the fastest rate since the recession's end. Economists generally anticipate growth to continue, although GDP growth is expected to decelerate.



Construction Gross Domestic Product

Spending on construction increased 10.8% in 2013 to $942 billion. During the year-to-date period ending June 2014, construction spending totaled $950 billion and increased 5.5% over the year-to-date period ending June 2013. Public construction has stalled in the recent period, but private residential and nonresidential activity is expected to pick up as the economy improves and consumer spending increases as employment improves.[3]



Macroeconomic Overview (cont.)

Value of Construction

(millions)

							YTD		
	2009	2010	2011	2012	2013	12-'13 Chg.	June 2013	June 2014	Chg.
Total Construction	$654,207	$554,915	$543,014	$566,794	$580,682	2.5%	$562,840	$588,816	4.6%
Residential	$253,577	$248,706	$244,391	$283,404	$361,213	27.5%	$337,494	$361,338	7.1%
Nonresidential	$654,207	$554,915	$543,014	$566,794	$580,682	2.5%	$562,840	$588,816	4.6%
Lodging	$25,474	$11,329	$8,515	$11,075	$16,630	50.2%	$12,986	$15,449	19.0%
Office	$52,717	$37,573	$34,415	$36,456	$41,840	14.8%	$36,856	$44,479	20.7%
Commercial	$55,042	$40,522	$43,488	$47,153	$53,122	12.7%	$49,497	$54,282	9.7%
Health care	$45,111	$39,879	$39,694	$40,655	$39,209	-3.6%	$41,276	$38,973	-5.6%
Educational	$102,907	$88,227	$84,692	$84,961	$79,123	-6.9%	$80,499	$75,651	-6.0%
Religious	$6,206	$5,208	$4,152	$3,894	$3,303	-15.2%	$3,625	$3,781	4.3%
Public safety	$14,099	$11,118	$9,895	$10,122	$9,306	-8.1%	$9,793	$9,289	-5.1%
Amusement and recreation	$18,901	$15,959	$15,527	$16,052	$14,989	-6.6%	$15,297	$16,709	9.2%
Transportation	$38,459	$38,232	$35,438	$37,632	$42,181	12.1%	$39,813	$42,190	6.0%
Communication	$19,754	$18,261	$17,817	$17,101	$17,516	2.4%	$17,900	$15,587	-12.9%
Power	$89,405	$78,540	$89,528	$92,390	$88,327	-4.4%	$87,208	$103,797	19.0%
Highway and street	$82,028	$82,657	$78,881	$79,462	$85,178	7.2%	$82,303	$75,316	-8.5%
Sewage and waste disposal	$24,410	$26,063	$23,156	$22,087	$21,384	-3.2%	$20,410	$21,993	7.8%
Water supply	$15,561	$15,305	$14,022	$13,155	$12,646	-3.9%	$13,363	$12,758	-4.5%
Conservation and development	$5,624	$6,937	$6,926	$6,094	$6,176	1.3%	$5,517	$8,143	47.6%
Manufacturing	$58,513	$36,106	$36,888	$48,505	$49,753	2.6%	$46,497	$50,420	8.4%
Total Private Construction	$592,326	$500,597	$504,134	$574,562	$667,480	16.2%	$627,598	$685,455	9.2%
Residential	$245,621	$238,801	$236,168	$276,827	$355,979	28.6%	$331,308	$355,915	7.4%
Nonresidential	$346,705	$261,796	$267,966	$297,735	$311,500	4.6%	$296,290	$329,540	11.2%
Total Public Construction	$315,459	$303,024	$283,271	$275,636	$274,416	-0.4%	$272,736	$264,699	-2.9%
Residential	$7,956	$9,905	$8,223	$6,577	$5,234	-20.4%	$6,186	$5,423	-12.3%
Nonresidential	$307,502	$293,119	$275,048	$269,059	$269,182	0.0%	$266,550	$259,276	-2.7%

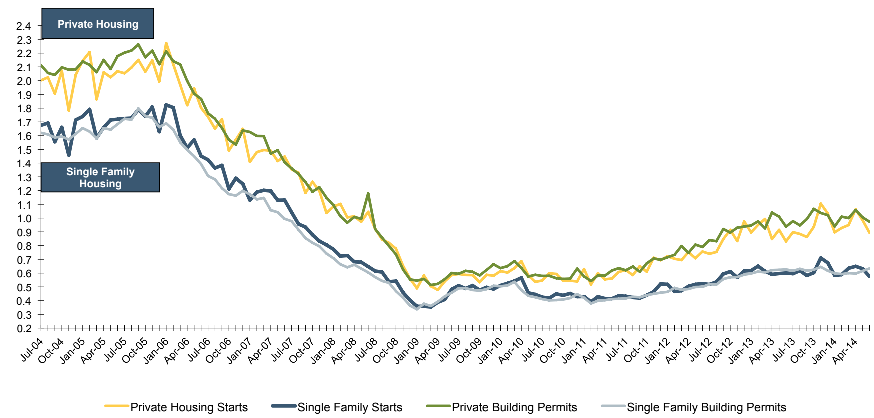
Source: US Census Bureau

Macroeconomic Overview (cont.)

Housing Starts

(millions of units)

New privately owned housing starts were at a seasonally adjusted annualized rate of 893,000 units in June 2014, 9.3% below the revised May rate of 985,000 units, but 7.5% above the June 2013 level. The June 2014 level of housing starts represents a nine-month low, with the decline largely driven by a record drop of starts in southern states. The seasonally adjusted annual rate of private housing units authorized by building permits (considered the best indicator of future housing starts) was 963,000 units in June 2014, 4.2% below the revised May estimate of 1,005,000, but 2.7% above the June 2013 level. Overall, the June 2014 data indicates that the housing market recovery has slowed, while higher interest rates and tighter underwriting standards for mortgages pose additional risks going forward.



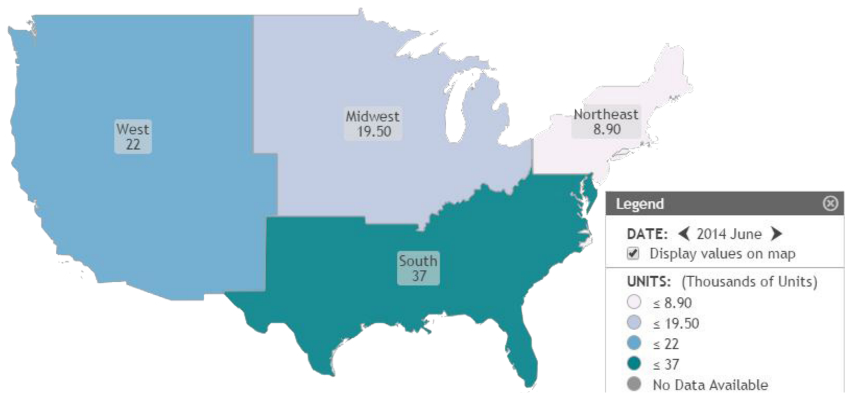
Source: U.S. Census Bureau
Note: Permits at a given date are generally a leading indicator of future starts. Beginning with January 2004, building permit data reflects the change to the 20,000 place series.

Macroeconomic Overview (cont.)

Regional Housing Starts

June 2014

Spending on construction increased 10.8% in 2013 to $942 billion. During the year-to-date period ending June 2014, construction spending totaled $950 billion and increased 5.5% over the year-to-date period ending June 2013. Public construction has stalled in the recent period, but private residential and nonresidential activity is expected to pick up as the economy improves and consumer spending increases as employment improves.[4]

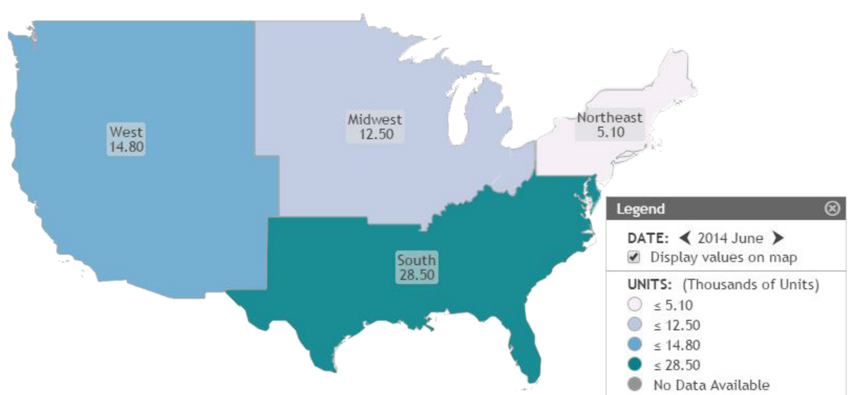


Source: US Census Bureau

Regional Housing Starts – Single Family

June 2014

Construction of single-family homes was up 4% in the second quarter of 2014 from a year before, with housing starts increasing 7.5% over the same period. However, new applicants for building permits declined 4.2% in June from the previous month.[5]

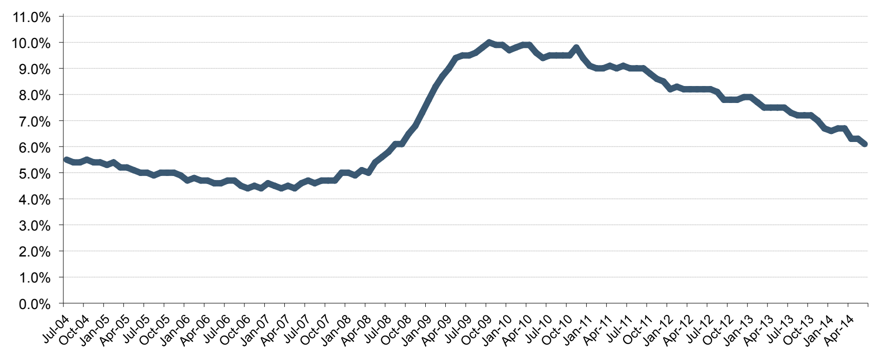


Source: US Census Bureau

Macroeconomic Overview (cont.)

Unemployment

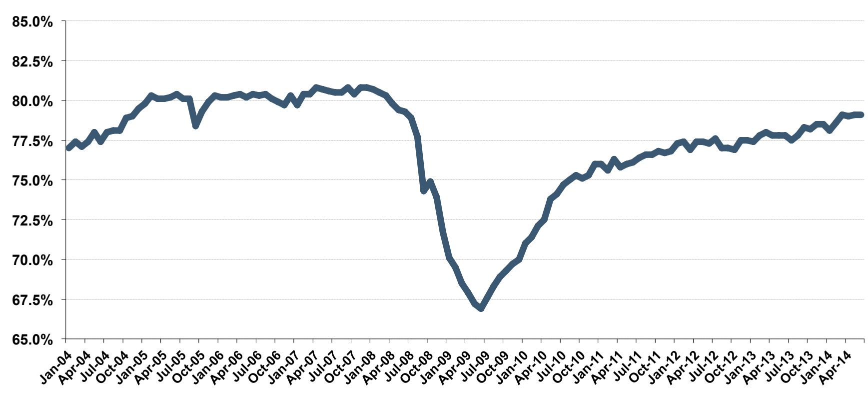
The unemployment rate was 6.1% in June 2014, down slightly from 6.3% in both April and May. The June 2014 rate is the lowest rate since September 2008, but the labor force participation rate is also generally lower. As job availability increases, the labor force will likely increase as individuals re enter the workforce, which could lead to an increase in the unemployment rate in the short term.



Source: Bureau of Labor Statistics

Capacity Utilization

The capacity utilization rate of the U.S. economy measures the extent to which factories are in use, and is largely considered an indicator of future downturns. As of the second quarter of 2014, the capacity utilization rate was 79.1% and has increased steadily since the Recession.[6]



Federal Reserve Bank of St. Louis

Bellwether Stocks and Industry Participants

					Operating Benchmarks				Comparable Multiples				
									EV/ Revenue		EV/EBITDA		
	Price as of 6/30/14	52-Week High	% of 52-Week High	Enterprise Value	Revenue	TTM Revenue Growth	TTM EBITDA Growth	EBITDA Margin	TTM	2014E	TTM	2014E	Debt/ EBITDA
Dealer/Distributor													
Titan Machinery, Inc.	16.5	21.0	78.5%	1,297.1	2,213.0	-3.6%	-18.3%	4.0%	0.6	0.6	14.6	20.0	12.4
Finning	26.5	28.2	93.9%	5,854.9	6,222.6	7.7%	20.9%	9.7%	0.9	0.9	9.3	8.0	2.3
Toromont Industries Ltd.	23.3	24.2	96.2%	1,884.6	1,420.0	-0.9%	-4.3%	14.6%	1.4	1.3	9.4	8.7	0.6
Rush Enterprises, Inc.	31.5	31.6	99.4%	2,474.6	4,307.3	35.0%	37.2%	5.6%	0.6	0.5	11.0	12.1	5.5
			Average	**2,877.8**	**3,540.7**	**9.5%**	**8.9%**	**8.5%**	**0.9**	**0.8**	**11.1**	**12.2**	**5.2**
			Median	**2,179.6**	**3,260.2**	**3.4%**	**8.3%**	**7.7%**	**0.8**	**0.8**	**10.2**	**10.4**	**3.9**
Rental/Secondary													
United Rentals, Inc.	104.7	108.5	96.6%	16,999.2	5,459.0	12.2%	24.1%	28.9%	3.5	3.1	12.0	6.4	5.1
Wajax Corporation	31.3	35.1	89.2%	717.9	1,272.8	1.2%	-9.8%	5.6%	0.6	0.6	10.2	7.9	2.7
Ritchie Bros. Auctioneers Incorporated	24.7	25.7	95.8%	2,506.2	477.4	8.6%	14.8%	37.3%	5.2	5.0	14.0	12.8	0.9
			Average	**6,741.1**	**2,403.1**	**7.3%**	**9.7%**	**23.9%**	**3.1**	**2.9**	**12.1**	**9.0**	**2.9**
			Median	**2,506.2**	**1,272.8**	**8.6%**	**14.8%**	**28.9%**	**3.5**	**3.1**	**12.0**	**7.9**	**2.7**

Source: Capital IQ

Bellwether Stocks and Industry Participants (cont.)

					Operating Benchmarks				Comparable Multiples				
	Price as of 6/30/14	52-Week High	% of 52-Week High	Enterprise Value	Revenue	TTM Revenue Growth	TTM EBITDA Growth	EBITDA Margin	EV/Revenue TTM	EV/Revenue 2014E	EV/EBITDA TTM	EV/EBITDA 2014E	Debt/EBITDA
OEM													
Construction													
Komatsu Ltd.	21.0	23.3	90.1%	25,163.3	17,474.5	4.7%	14.2%	17.5%	1.6	1.6	8.8	8.9	1.8
Astec Industries, Inc.	43.9	46.0	95.4%	965.7	959.9	2.5%	-1.5%	7.8%	0.9	0.8	11.4	8.9	-
Caterpillar inc.	108.7	109.9	98.9%	101,977.5	55,342.0	-3.5%	0.4%	16.1%	1.8	1.7	11.0	11.2	4.4
			Average	**42,702.2**	**24,592.1**	**1.2%**	**4.4%**	**13.8%**	**1.4**	**1.4**	**10.4**	**9.7**	**3.1**
			Median	**25,163.3**	**17,474.5**	**2.5%**	**0.4%**	**16.1%**	**1.6**	**1.6**	**11.0**	**8.9**	**3.1**
Agriculture													
Buhler Industries Inc.	5.6	6.5	85.8%	206.6	288.7	-8.4%	-23.2%	7.4%	0.6	-	8.6	-	3.4
AGCO Corporation	56.2	64.6	87.0%	6,407.5	10,098.2	-5.0%	-8.2%	10.0%	0.5	0.6	5.0	8.0	1.4
Alamo Group, Inc.	54.1	61.3	88.3%	615.3	717.9	11.8%	9.9%	9.0%	0.9	0.8	10.4	8.0	2.9
CNH Global N.V.	-	-	-	-	20,949.0	4.1%	11.4%	14.8%	-	1.3	-	11.9	6.2
Deere & Company	90.6	94.9	95.4%	66,046.7	36,552.6	-4.2%	-1.1%	17.3%	1.8	2.1	10.2	15.2	5.8
Kubota Corporation	12.8	16.5	77.5%	21,045.5	13,449.6	13.2%	36.8%	16.3%	1.8	1.8	11.1	11.2	2.5
			Average	**18,864.3**	**13,676.0**	**1.9%**	**4.3%**	**12.5%**	**1.1**	**1.3**	**9.1**	**10.9**	**3.7**
			Median	**6,407.5**	**11,773.9**	**0.0%**	**4.4%**	**12.4%**	**0.9**	**1.3**	**10.2**	**11.2**	**3.2**
Other													
Joy Global Inc.	61.6	64.8	95.0%	7,056.4	3,826.5	-29.5%	-49.3%	16.6%	1.6	1.6	9.6	-	2.0
Gencor Industries, Inc.	11.0	11.6	94.8%	13.4	42.7	-22.9%	26.7%	7.0%	nm	nm	nm	nm	-
Terex Corporation	41.1	45.5	90.4%	6,230.0	7,331.3	10.2%	37.6%	8.9%	0.6	0.6	7.0	5.6	2.8
Columbus McKinnon Corporation	27.1	31.0	87.3%	575.5	595.5	3.5%	6.4%	11.8%	1.0	1.0	8.6	7.7	2.1
			Average	**3,468.8**	**2,949.0**	**-9.7%**	**5.4%**	**11.1%**	**1.1**	**1.1**	**8.4**	**6.6**	**2.3**
			Median	**3,402.8**	**2,211.0**	**-9.7%**	**16.6%**	**10.4%**	**1.0**	**1.0**	**8.6**	**6.6**	**2.1**
			High	**101,977.5**	**55,342.0**	**35.0%**	**37.6%**	**37.3%**	**5.2**	**5.0**	**14.6**	**20.0**	**12.4**
			Low	**13.4**	**42.7**	**-29.5%**	**-49.3%**	**4.0%**	**0.5**	**0.5**	**5.0**	**5.6**	**0.6**
			Average	**14,107.3**	**9,450.0**	**1.8%**	**6.2%**	**13.3%**	**1.4**	**1.4**	**10.1**	**10.1**	**3.6**
			Median	**2,506.2**	**4,066.9**	**3.0%**	**8.2%**	**10.9%**	**1.0**	**1.1**	**10.2**	**8.9**	**2.8**

Source: Capital IQ

Equipment Dealership Valuation Considerations

Equipment networks of all types have and continue to experience dealer consolidation. Some dealer networks have achieved their respective OEM's desired composition while others are still working towards tomorrow's dealership/distribution system. Mercer Capital has direct and indirect exposure to a significant amount of equipment dealer consolidation over the past 20+ years.

It is no secret that many equipment dealership valuations have certain gravitational norms. Some networks report valuations that are substantiated primarily by adjusted asset values while others are driven by cash flow performance. In many cases a mix of both income and asset based indications is required to properly develop a credible valuation. As with valuations in general, rules of thumb often fall short of properly articulating the value of a given equipment dealership due to many underlying issues. A rule of thumb for the core OEM business activity may be more or less appropriate; however, many dealers have adjacent and/or complimentary business activities that must be viewed with special consideration and in some cases using separate or distinct modeling. Capital structure, balance sheet treatment of rental fleets, and numerous other financial and operational attributes can cause one dealership valuation to differ materially from another. Trends in construction do not follow those of agriculture. More specialized equipment dealers may have unique attributes that significantly differentiate their valuation from larger more diverse dealers.

Another complicating challenge regarding dealership valuation is the uniqueness of the overall business model and the significant influence and control of the OEMs. The definition of "fair market value" postulates a buyer and a seller with no compulsion, equal capability and knowledge, and willingness. In the real world, most equipment dealerships are at best tenants in their territories and transactions of both the dealership as a whole and ownership interests therein are strictly overseen by and subject to the approval of the respective OEMs. Most dealership agreements contain strict guidelines regarding a primary owner's active business participation, approved succession and contingency plans, and numerous other vital operational and financial requirements. Accordingly, valuations must reflect a proper understanding and consideration of a dealership's real world circumstances.

Sources

1. Summary narrative from Titan Machine, Inc. Form 10-K, filed with the U.S. Securities and Exchange Commission for the fiscal year ended January 31, 2014.
2. Ibid.
3. http://www.aia.org/practicing/AIAB104284.
4. http://www.bloomberg.com/news/print/2014-07-17/housing-starts-in-u-s-unexpectedly-fall-on-plunge-in-south.html.
5. http://online.wsj.com/articles/housing-starts-sank-9-3-in-june-1405600397#printMode.
6. http://www.bloomberg.com/portfolio-impact/2012-04-24/number-of-months-capacity-utilization-rose-since-june-2009.html#why_it_matters.

Mercer Capital

Equipment Dealer Industry Services

Mercer Capital has expertise providing business valuation and financial advisory services to companies in the equipment dealer industry.

Mercer Capital has an extensive background servicing the financial advisory and business valuation needs of equipment dealers throughout the country and across numerous OEM networks. We assist dealers and their shareholders in wide range of activities including sales and acquisitions, ownership planning and succession, estate tax compliance and IRS audits, corporate reorganizations, marital dissolution, OEM purchases, financial reporting pertaining to consolidation activities, among other purposes. We also assist OEMs in promoting efficient dealer succession and ownership transition. Our publications and insights are often the basis for proactive planning and dispute resolution.

Services Provided

- Valuation of equipment dealerships and OEMs
- Transaction advisory for acquisitions and divestitures
- Valuations for purchase accounting and impairment testing
- Fairness and solvency opinions
- Litigation support for economic damages and valuation and shareholder disputes

Contact a Mercer Capital professional to discuss your needs in confidence.

Contact Us

Timothy R. Lee, ASA
901.322.9740
leet@mercercapital.com

Nicholas J. Heinz, ASA
901.322.9788
heinzn@mercercapital.com

Matthew R. Crow, ASA, CFA
901.685.2120
crowm@mercercapital.com

Madeleine L. Harrigan
901.322.9756
harriganm@mercercapital.com

Mercer Capital
5100 Poplar Avenue, Suite 2600
Memphis, Tennessee 38137
901.685.2120 (P)

www.mercercapital.com