MERCER CAPITAL

VALUE FOCUS

Professional Services Industry

Year-End 2014

Executive Summary

- Macroeconomic factors have been favorable for the professional services industry since the recession, and the second half of 2014 has seen a continuation of these trends. Unemployment dropped to 5.6% while corporate profits and private investment continue to grow in the U.S. These indicators suggest a favorable, though conservative, outlook for the professional services industry.
- Despite a stronger economy, both the staffing and consulting sectors lagged the S&P 500 over the past twelve months. The staffing sector has seen median stock price decline of 6.2% during 2014, compared to an increase of 58.5% during 2013. Current and forward EV/EBITDA multiples for the staffing sector are 10.7x and 7.7x, respectively. The consulting sector has seen a median stock price decline of 2.7% in 2014, although the sector was up 35.8% in 2013. Current and forward EV/EBITDA multiples for the consulting sector are 10.9x and 9.2x, respectively, which implies weaker EBITDA growth relative to the staffing companies. Overall, firms in the professional services industry saw exceptional growth in 2013, but lagged the S&P 500 significantly in 2014 as growth prospects have become more tempered going forward.
- M&A deal volume is on the rise for the consulting and staffing sectors. Annual volume for 2014 reached five-year high levels for each sector. Strategic buyers continue to be the driving force behind increased volume. Both sectors have experienced growth in the post-recession era, have high cash reserves, and continue to look for expansion opportunities.

What are Professional Services Firms?

The professional services industry includes consultancies, research firms, staffing and employment businesses, engineering, architecture, accounting, legal, and specialty professional practices. Many professional services firms are privately held, though two sectors include multiple public companies: consulting and staffing. This publication emphasizes market and transaction activity for these two sectors, but the economic trends and valuation drivers discussed could apply to any professional services firm.

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Macroeconomic Trends

The professional services industry is closely tied to macroeconomic trends. Three key economic indicators include the unemployment rate, corporate profit levels, and non-residential private investment expenditures. In sum, these indicators shed light on the general health of business in the U.S. As these indicators become increasingly optimistic, the outlook for companies in this sector generally improves. From mid-2008 to mid-2011, the professional services industry experienced challenging circumstances. Currently, positive economic news and outlook have created opportunities for growth.

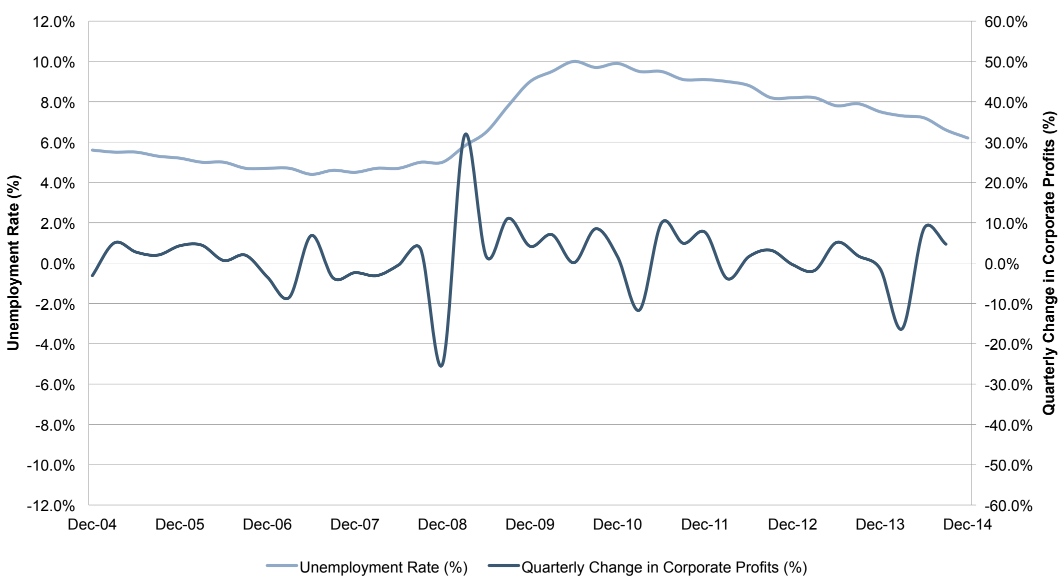
Unemployment and Corporate Profits

The staffing sector saw severe decline in 2008 as companies had to cut staff and reduce costs. Corporate profits rebounded in 2009, but a lack of economic optimism caused companies to remain conservative with staffing expenditures. Furthermore, private investment, a proxy for confidence, did not improve until late-2011. In 2011, as unemployment began its steady descent from recession highs, companies began to increase staffing levels. Initial growth occurred in the firms that specialized in temporary staffing solutions. As unemployment continued to fall, long term hires and HR expenditures grew. Since 2011, the industry has continued to strengthen and is expected to grow between 3.6% and 4.0% annually through 2019, according to IBISWorld.

The consulting sector experienced a negative shock at the outset of the economic downturn. However, once corporate profits returned to prerecession levels, the industry recovered and expanded with average annual growth of around 4.5% from 2010 through 2014. The massive reduction in corporate profits in 2008 caused companies to cut costs, including those deemed unnecessary to the core business. Upon recovery, companies resumed spending on consulting and research services. According to IBISWorld, the sector is expected to grow over 3.6% annually over the next five years.

The second half of 2014 showed continued signs of improvement in the macroeconomic landscape, albeit at a more conservative pace. Unemployment fell from 6.1% in June 2014 to 5.6% in December 2014. In comparison, the unemployment rate dropped by 0.8 percentage points over the same period in 2013. Corporate profits have continued their expansion as well with a 4.7% increase in profits from second quarter to third quarter, while the same period in 2013 experienced 1.7% growth. Despite a decrease in the growth rate in the second half of 2014, corporate profits continue to increase.

Historical Trends in Unemployment & Corporate Profits



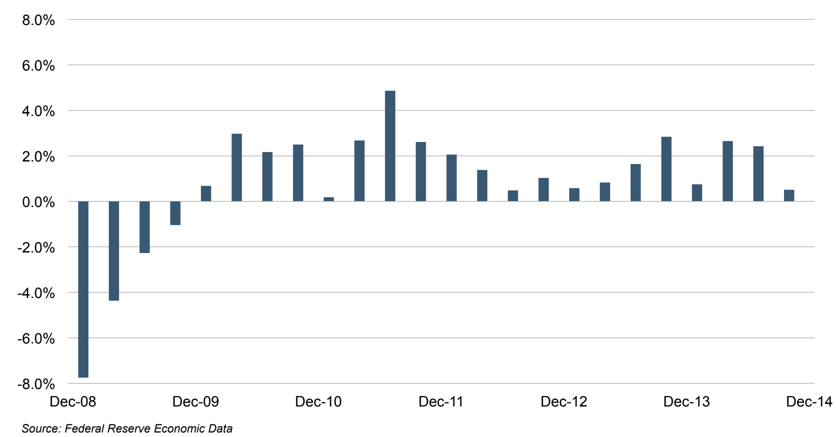
Source: Capital IQ

Macroeconomic Trends

Non-Residential Private Investment

Non-residential private investment has continued to climb, experiencing positive growth since 2010. Between second quarter and third quarter, private investment increased 0.5% compared to 2.8% in the same period in 2013. As profits continue to rise and private investment increases, revenues and profits are expected to increase for the professional services industry. Growing employment optimism can push growth for staffing firms that will be utilized for recruiting in an increasingly competitive marketplace. Future growth for professional services is expected to proceed at more moderate levels and roughly mirror GDP, compared to recent quarters that exceeded expectations.

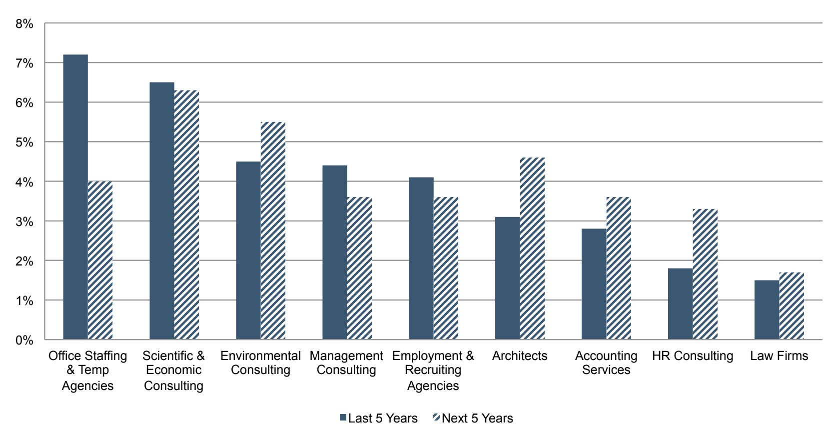
Quarterly Change in Private Non-Residential Fixed Investment



Growth Outlook

The growth outlook for the professional services industry is varied when broken into subsectors. The largest three subsectors by revenue (Law Firms, Management Consulting, and Office Staffing & Temp Agencies) expect growth in the next five years to be below 4.0%. For areas such as Management Consulting and Office Staffing & Temp Agencies, these forward growth rates represent a decrease from the growth observed in the previous five year period. The chart represents average annual growth rates for nine subsectors over the last five years and for the next five years.

Industry Revenue Growth by Subsector



Source: IBIS World

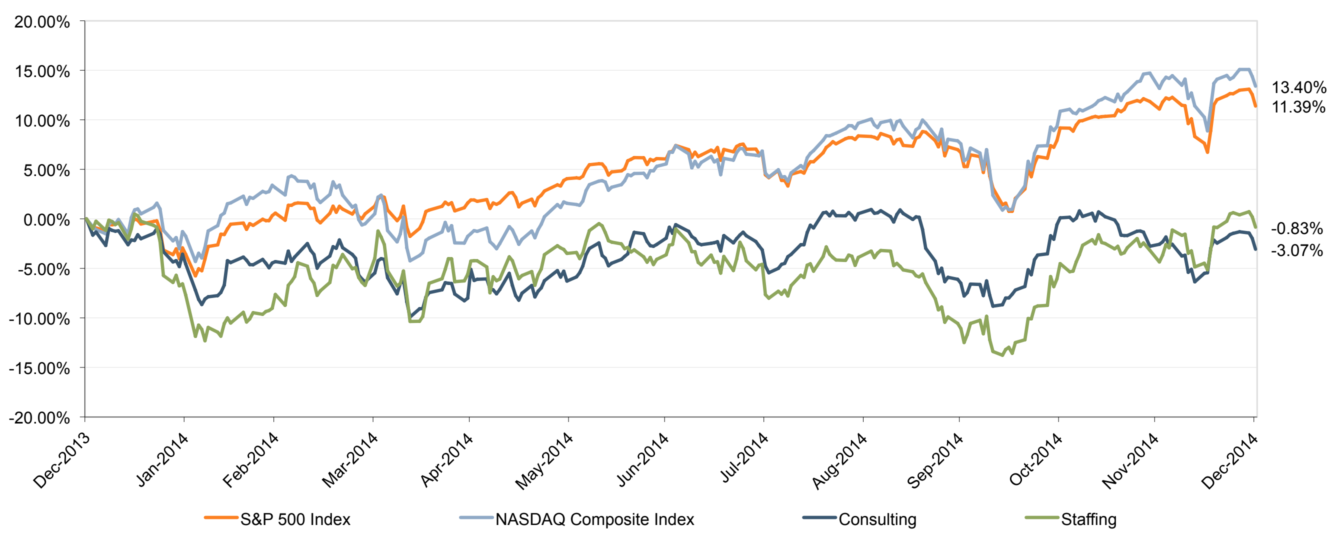
Market Performance

The staffing sector lagged the S&P 500 during 2014 with a slight decline of 0.83%, relative to growth of 11.39% for the index. After strong growth in 2013, staffing expectations have fallen more in line with market performance. Furthermore, uncertainties exist as to what role staffing companies will play as the economy strengthens. Industry observers suggest that, moving forward, individual company gains greater than GDP growth will be mostly the result of market share gains as opposed to overall industry growth. Therefore, the last six months have seen tempered expectations in the staffing sector.

The consulting sector also lagged the S&P 500 during 2014 and experienced a decline of 3.07%. Stock price performance saw a significant decline from mid-August to mid-September as economists revised full-year estimates on national GDP. The industry faces multiple headwinds such as continued uncertainty in government spending and the growth of more technology-focused consulting solutions. The information below presents median valuation multiples and stock price changes for the two groups.

In general, the professional services industry outperformed the broader market in 2013, but slower growth translated into tempered performance in 2014. Although economic outlook for the professional services industry remains positive, future growth is likely to be more in line with the general economy.

Index Performance



Source: Capital IQ. Sector Indices are weighted by market capitalization

Summary Performance and Valuation

Segment	Number of Companies	Median % Change		EV / Rev. LTM	EV / EBITDA	
		YTD	LTM		LTM	2015E
Staffing	19	-6.20%	58.45%	0.59x	10.7x	7.7x
Consulting	18	-2.70%	35.81%	1.21x	10.9x	9.2x

Source: Capital IQ

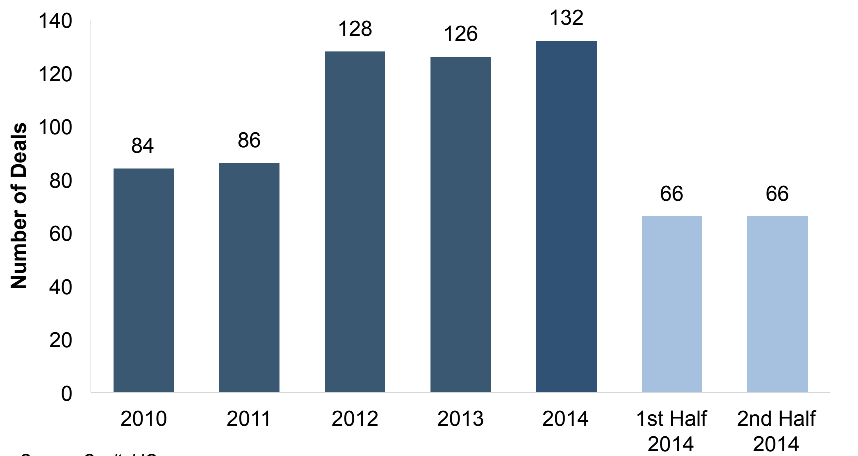
Professional Services M&A Activity // Staffing Sector

The final six months of 2014 saw 66 staffing transaction announcements by 61 different buyers. This volume is flat when compared to the first six months of 2014.

The sector has seen a general trend upward in the number of transactions being completed since 2010. The economic downturn lowered cash reserves and depressed deal volume. Volume levels lagged behind the initial recovery because companies remained conservative on HR and staffing expenditures until 2011. Increased sector strength caused deal volume to increase 48.8% from 2011 to 2012.

Deal volume during 2014 exceeded 100 deals for a third straight year, and reached a five-year high of 132 announced deals. Increased activity continues to be propelled primarily by private, strategic buyers.

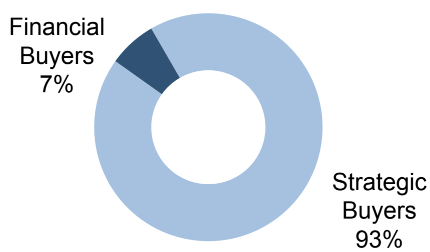
Annual Transaction Volume



Source: Capital IQ

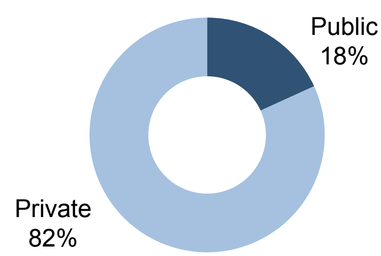
Strategic vs. Financial Buyer

YTD December 2014



Public vs. Private Buyer

YTD December 2014



Professional Services M&A Activity // Staffing Sector (cont.)

Notable Transactions in the Staffing Sector

Closing Date	Target	Acquirer	EV ($M)	LTM Rev.	LTM EBITDA	EV / Rev.	EV / EBITDA
01/09/2015	Royall & Company, Inc.	The Advisory Board Company	850.0	nm	nm	nm	nm
12/16/2014	SingleSource Services Corporation	ClearStar, Inc.	4.0	2.9	nm	1.38x	nm
10/30/2014	PRO Unlimited, Inc.	Investcorp Bank B.S.C.; Bahrain Mumtalakat Holding Company	300.0	nm	nm	nm	nm
08/01/2014	CONEXIS	WageWorks, Inc.	118.0	nm	nm	nm	nm

Source: Capital IQ

The Advisory Board Company (NASD: ABCO) completed its acquisition of Royall & Company, Inc. on January 9, 2015. Royall & Company, a Richmond, Virginia, based firm, provides strategic, data-driven student engagement and enrollment management solutions, financial aid optimization, and alumni fundraising for institutions for higher education. ABCO acquired Royall & Company to broaden its offerings to the education industry and become an industry leader in driving value for institutions of higher education.

ClearStar, Inc. (AIM: CLST) finalized its acquisition of SingleSource Services Corporation on December 16, 2014. SingleSource is a Florida-based background screening company that conducts over 2,000 pre-employment inquiries per day. ClearStar is a technology and service provider to the background check industry. Robert J. Vale, CEO of ClearStar, stated that "the acquisition of SingleSource is a dramatic acceleration for ClearStar's stated strategy of building its direct sales and [he] firmly believe[s] that this will create value for our shareholders." SingleService's CEO, Don Dymer, has entered into a consulting agreement with ClearStar to aid in the integration process.

Investcorp Bank B.S.C. and Bahrain Mumtalakat Holding Company completed their acquisition of PRO Unlimited, Inc. on October 30, 2014. PRO Unlimited is a leading provider of software and services that aid large enterprises in managing their contingent workforces. Investcorp Bank and Mumtalakat invest in alternative investments and enable businesses to strengthen and grow, while returning value.

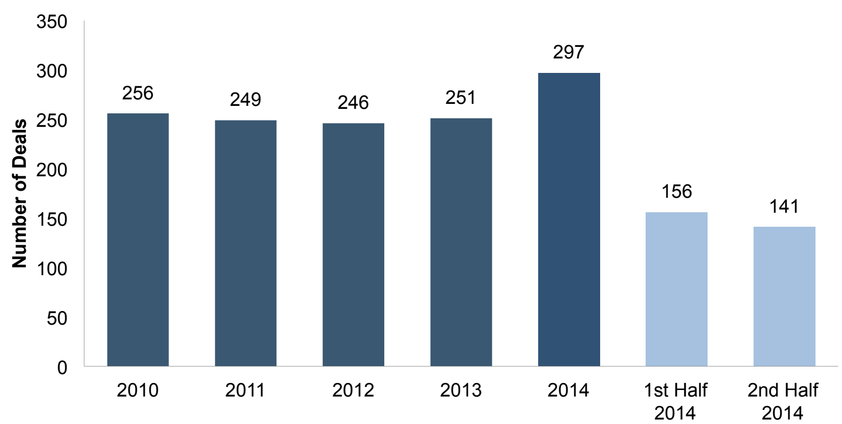
WageWorks, Inc (NYSE: WAGE) finalized its purchase of CONEXIS from Word & Brown Insurance on August 1, 2014. CONEXIS, a rival of WageWorks, administers consumer-driven health care plans and other benefits. WageWorks purchased CONEXIS in order to gain market share and strengthen its current product offerings. This merger is expected to add between $23 million and $25 million in revenue for 2014.

Professional Services M&A Activity // Consulting Sector

The consulting sector has experienced high deal volume since 2010. The economic downturn provided an opportunity for large firms to adsorb smaller, distressed companies. Large consulting companies experienced growth after an uptick in corporate profits following 2009. Volume for the final six months of 2014 reached 141 transactions, which is a 9.6% decline from the first half of 2014.

The consulting sector is a highly fragmented industry with many small firms specializing in certain niches. It appears that positive economic trends are continuing to drive consolidation as deal volume increased 18.3% from 2013 to 2014. Increased activity in 2014 appears to be driven primarily by private, strategic buyers.

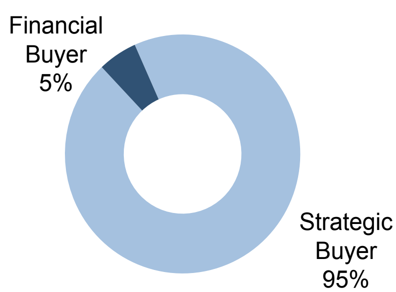
Annual Transaction Volume



Source: Capital IQ

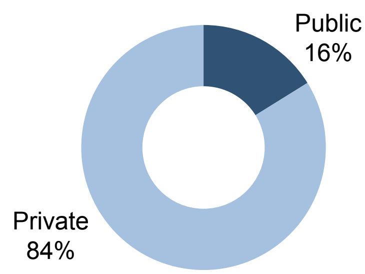
Strategic vs. Financial Buyer

YTD December 2014



Public vs. Private Buyer

YTD December 2014



Professional Services M&A Activity // Consulting Sector (cont.)

Notable Transactions in the Consulting Sector

Closing Date	Target	Acquirer	EV ($M)	LTM Rev.	LTM EBITDA	EV / Rev.	EV / EBITDA
Q1 2015	Prism Technologies, LLC	Internet Patents Corporation	81.9	40.0	nm	2.05x	nm
10/23/2014	Santa Barbara Tax Products Group, LLC	Green Dot Corporation	389.2	88.0	46.2	4.42x	8.43x
10/17/2014	Callison, LLC	Arcadis NV	181.19	167.0	25.0	1.08x	7.25x

Source: Capital IQ

Internet Patents Corporation (NASD: PTNT) announced its agreement to purchase Prism Technologies, LLC. on November 11, 2014. The deal is expected to close in the first quarter of 2015. Prism Technologies focuses on intellectual property licensing and technology research and development. Internet Patents Corporation purchased Prism Technologies in order to grow strategically by expanding and diversifying IPC's portfolio of patents as well as adding experienced members to IPC's management team.

Green Dot Corporation (NYSE: GDOT) finalized its acquisition of Santa Barbara Tax Products Group, LLC. on October 23, 2014. Santa Barabara Tax Products Group ("TPG") provides tax-related financial products and services to tax professionals and taxpayers in the United States. Green Dot purchased TPG to expand their reach into their core customer group by providing tax refund processing services.

Arcadis NV (Euronext: ARCAD) closed its purchase of Callison, LLC on October 17, 2014. Callison is a global provider of architecture and design services. Arcadis NV is a Netherlands-based and leading global provider of natural and built asset design and consultancy services, with many subsidiaries across the globe. This merger will make Arcadis the largest retail architecture firm in the world and will offer greater opportunities for Arcadis to better serve clients by leveraging Callison's wide range of capabilities, market reach, and scale throughout the world.

Guideline Company Pricing

Staffing Sector

($ Millions, except per share data. Sorted by equity market capitalization)

Company Name	Ticker	Price 12/31/14	Stock Price Change 2014	Stock Price Change 2013	Market Cap	Ent. Value	LTM Rev.	EBITDA LTM	EBITDA 2015E	LTM EBITDA Margin	EV / Rev. LTM	EV / EBITDA LTM	EV / EBITDA 2014E	Projected Growth Rev.	Projected Growth EBITDA
Towers Watson & Co.	TW	$113.17	-11.3%	127.0%	$7,936.5	$7,630.4	$3,619.8	$690.6	$752.2	19.1%	2.11	11.0	10.1	1.7%	8.9%
Robert Half International Inc.	RHI	58.38	39.0%	32.0%	7,935.2	7,645.6	4,695.0	546.3	635.2	11.6%	1.63	14.0	12.0	10.5%	16.3%
ManpowerGroup Inc.	MAN	68.17	-20.6%	102.3%	5,395.0	5,218.2	20,762.8	810.5	803.8	3.9%	0.25	6.4	6.5	-6.8%	-0.8%
TriNet Group, Inc.	TNET	31.28	NM	NM	2,177.0	2,629.2	2,071.5	171.1	185.2	8.3%	1.27	15.4	14.2	17.8%	8.3%
On Assignment Inc.	ASGN	33.19	-5.0%	72.2%	1,737.4	2,111.2	1,859.9	183.7	203.0	9.9%	1.14	11.5	10.4	0.5%	10.5%
Korn/Ferry International	KFY	28.76	10.1%	64.7%	1,448.6	1,174.4	1,000.8	129.7	161.9	13.0%	1.17	9.1	7.3	5.7%	24.9%
TrueBlue, Inc.	TBI	22.25	-13.7%	63.7%	946.0	1,092.2	2,174.0	116.4	139.7	5.4%	0.50	9.4	7.8	19.5%	20.0%
Insperity, Inc.	NSP	33.89	-6.2%	11.0%	858.5	633.1	2,357.8	68.4	100.0	2.9%	0.27	9.2	6.3	13.2%	46.1%
Kforce Inc.	KFRC	24.13	17.9%	42.7%	738.1	750.4	1,217.3	58.9	76.5	4.8%	0.62	12.7	9.8	10.4%	29.9%
Kelly Services, Inc.	KELY.A	17.02	-31.8%	58.4%	641.9	679.0	5,562.7	55.6	72.5	1.0%	0.12	12.2	9.4	4.6%	30.4%
GP Strategies Corp.	GPX	33.93	13.9%	44.3%	580.0	575.7	501.9	52.4	57.8	10.4%	1.15	11.0	10.0	4.2%	10.3%
Heidrick & Struggles International Inc.	HSII	23.05	14.4%	32.0%	420.5	291.8	494.3	43.8	44.6	8.9%	0.59	6.7	6.5	2.3%	1.8%
CDI Corp.	CDI	17.71	-4.4%	8.2%	347.4	307.1	1,133.4	37.2	41.0	3.3%	0.27	8.3	7.5	0.5%	10.3%
Barrett Business Services Inc.	BBSI	27.40	-70.5%	143.5%	195.0	113.4	636.2	(43.5)	41.9	NM	0.18	NM	2.7	NM	NM
Corporate Resource Services, Inc.	CRRS	1.20	-54.4%	484.4%	189.6	307.7	942.5	18.4	NM	2.0%	0.33	16.7	NM	21.9%	NM
CTPartners Executive Search Inc.	CTP	15.19	171.3%	22.8%	110.3	125.6	164.7	15.0	NM	9.1%	0.76	8.4	NM	NM	NM
Hudson Global, Inc	HSON	3.10	-23.0%	-10.3%	102.5	92.4	682.1	(5.0)	(2.7)	NM	0.14	NM	NM	-11.7%	NM
BG Staffing, Inc.	BGSF	13.00	NM	NM	72.9	105.3	173.7	10.7	NM	6.1%	0.61	9.9	NM	NM	NM
Mastech Holdings, Inc.	MHH	10.62	-24.1%	246.3%	45.7	43.2	113.5	5.7	NM	5.0%	0.38	7.6	NM	NM	NM
Median			**-6.2%**	**58.4%**	**$641.9**	**$633.1**	**$1,133.4**	**$55.6**	**$100.0**	**6.1%**	**0.59x**	**9.9x**	**8.6x**	**4.6%**	**10.5%**
Average			**0.1%**	**90.9%**	**$1,677.8**	**$1,659.3**	**$2,640.2**	**$156.1**	**$220.8**	**7.3%**	**0.71x**	**10.6x**	**8.6x**	**6.3%**	**16.7%**

Guideline Company Pricing

Consulting Sector

($ Millions, except per share data. Sorted by equity market capitalization)

Company Name	Ticker	Price 12/31/14	Stock Price Change 2014	Stock Price Change 2013	Market Cap	Ent. Value	LTM Rev.	EBITDA LTM	EBITDA 2015E	LTM EBITDA Margin	EV / Rev. LTM	EV / EBITDA LTM	EV / EBITDA 2014E	Projected Growth Rev.	Projected Growth EBITDA
Verisk Analytics, Inc.	VRSK	$64.05	-2.5%	28.9%	$10,563.1	$11,403.6	$1,746.7	$790.1	$878.7	45.2%	6.53	14.4	13.0	8.0%	11.2%
IHS Inc.	HIS	113.88	-4.9%	24.7%	7,763.5	9,413.5	2,230.8	510.6	749.1	22.9%	4.22	18.4	12.6	5.8%	46.7%
Dun & Bradstreet Corp.	DNB	120.96	-1.5%	56.1%	4,343.7	5,675.7	1,681.8	507.7	513.0	30.2%	3.37	11.2	11.1	1.3%	1.0%
Corporate Executive Board Co.	CEB	72.53	-6.3%	63.1%	2,439.9	2,861.0	909.0	206.4	246.1	22.7%	3.15	13.9	11.6	6.9%	19.2%
The Advisory Board Company	ABCO	48.98	-23.1%	36.1%	1,765.9	1,743.4	574.2	63.7	170.5	11.1%	3.04	27.4	10.2	36.7%	167.7%
FTI Consulting, Inc.	FCN	38.63	-6.1%	24.7%	1,584.7	2,117.0	1,756.2	206.0	229.0	11.7%	1.21	10.3	9.2	3.8%	11.1%
Huron Consulting Group Inc.	HURN	68.39	9.1%	86.0%	1,495.3	1,631.2	889.2	156.8	178.6	17.6%	1.83	10.4	9.1	2.3%	13.9%
Exponent Inc.	EXPO	82.50	6.8%	38.4%	1,061.5	919.9	288.6	67.0	77.2	23.2%	3.19	13.7	11.9	5.1%	15.2%
ICF International Inc.	ECFI	40.98	18.1%	48.1%	795.0	902.7	1,003.5	89.2	126.1	8.9%	0.90	10.1	7.2	21.3%	41.4%
Navigant Consulting Inc.	NCI	15.37	-19.9%	72.0%	745.4	899.1	766.6	116.7	115.3	15.2%	1.17	7.7	7.8	8.5%	-1.2%
Resources Connection Inc.	RECN	16.45	14.8%	20.1%	626.5	526.4	584.5	49.9	62.6	8.5%	0.90	10.5	8.4	6.0%	25.5%
CBIZ, Inc.	CBZ	8.56	-6.1%	54.3%	422.2	625.8	719.5	75.5	NM	10.5%	0.87	8.3	NM	4.7%	NM
Franklin Covey Co.	FC	19.36	-2.6%	54.1%	326.7	343.6	209.6	30.7	39.5	14.7%	1.64	11.2	8.7	10.0%	28.7%
CRA International Inc.	CRAI	30.32	53.1%	0.2%	288.9	245.9	303.6	29.7	51.9	9.8%	0.81	8.3	4.7	3.6%	74.7%
Hill International, Inc.	HIL	3.84	-2.8%	7.9%	193.4	302.2	558.0	39.4	56.0	7.1%	0.54	7.7	5.4	17.4%	42.1%
Quest Resource Holding Corporation	QRHC	1.44	-31.4%	-27.6%	160.7	159.3	165.5	1.2	2.9	0.7%	0.96	NM	NM	17.6%	132.9%
RCM Technologies Inc.	RCMT	7.00	0.3%	35.5%	87.9	79.6	190.3	11.4	NM	6.0%	0.42	7.0	NM	NM	NM
Ecology & Environment, Inc.	EEI	9.13	-17.0%	-1.1%	39.2	39.5	126.9	1.9	NM	1.5%	0.31	21.0	NM	NM	NM
Median			**-2.7%**	**35.8%**	**$770.2**	**$900.9**	**$652.0**	**$71.3**	**$126.1**	**11.4%**	**1.19x**	**10.5x**	**9.2x**	**6.5%**	**25.5%**
Average			**-1.2%**	**34.5%**	**$1,928.0**	**$2,216.1**	**$816.9**	**$164.1**	**$233.1**	**14.9%**	**1.95x**	**12.4x**	**9.4x**	**9.9%**	**42.0%**

Mercer Capital

Professional Services Industry

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

Mercer Capital provides business valuation and financial advisory services to professional services firms throughout the nation. We provide valuation services for tax purposes, buy-sell agreements, partner buyouts, and other corporate planning purposes. Mercer Capital also works with owners who are considering the sale of their firm or the acquisition of other professional services firms.

Services Provided

- Valuation of professional services companies
- Transaction advisory for mergers, acquisitions and divestitures
- Valuations for purchase accounting, impairment testing, and other fair value measurement
- 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.

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Fairness Opinions

Evaluating a Buyer's Shares from the Seller's Perspective

M&A activity in the U.S. (and globally) has accelerated in 2014 after years of gradual improvement following the financial crisis. According to Dealogic, M&A volume where the target was a U.S. company totaled $1.4 trillion YTD through November 10, the highest YTD volume on record and up 43% from the same period last year. Excluding cross-border acquisitions, domestic-only M&A was $1.1 trillion, which represented the second highest YTD volume since 1999 and up 27% from last year. Healthcare and telecommunications were the first and second most targeted sectors.

The improvement has taken a long time even though corporate cash is high, financing costs are very low and organic revenue growth in most industries has been sluggish. Aside from improving confidence, another key foundation for increased M&A activity fell into place in 2013 when equity markets staged a strong rally as the S&P 500 rose 30% (32% with dividends) and the Russell 2000 increased 37% (39%). The absence of a meaningful pullback in 2014 and a 12% advance in the S&P 500 and 2% in the Russell 2000 have further supported activity.

The rally in equities, like low borrowing rates, has reduced the cost to finance acquisitions because the majority of stocks experienced multiple expansion rather than material growth in EPS. It is easier for a buyer to issue shares to finance an acquisition if the shares trade at rich valuation than issuing "cheap" shares. As of November 24, the S&P 500's P/E based upon trailing earnings (as reported) was 20.0x compared to 18.2x at year-end 2013, 17.0x at year-end 2012 and 14.9x at year-end 2011. The long-term average P/E since 1871 is 15.5x (Source: http://www.multpl.com).

High multiple stocks can be viewed as strong acquisition currencies for acquisitive companies because fewer shares have to be issued to achieve a targeted dollar value. As such, it is no surprise that the extended rally in equities has supported deal activity this year. However, high multiple stocks may represent an under-appreciated risk to sellers who receive the shares as consideration. Accepting the buyer's stock raises a number of questions, most which fall into the genre of: what are the investment merits of the buyer's shares? The answer may not be as obvious as it seems, even when the buyer's shares are actively traded.

Our experience is that some, if not most, members of a board weighing an acquisition proposal do not have the background to thoroughly evaluate the buyer's shares. Even when financial advisors are involved there still may not be a thorough vetting of the buyer's shares because there is too much focus on "price" instead of, or in addition to, "value."

A fairness opinion is more than a three or four page letter that opines as to the fairness from a financial point of a contemplated transaction; it should be backed by a robust analysis of all of the relevant factors considered in rendering the opinion, including an evaluation of the shares to be issued to the selling company's shareholders. The intent is not to express an opinion about where the shares may trade in the future, but rather to evaluate the investment merits of the shares before and after a transaction is consummated.

Key questions to ask about the buyer's shares include the following:

- **Liquidity of the Shares.** What is the capacity to sell the shares issued in the merger? SEC registration and even NASDAQ and NYSE listings do not guarantee that large blocks can be liquidated efficiently. Generally, the higher the institutional ownership, the better the liquidity. Also, liquidity may improve with an acquisition if the number of shares outstanding and shareholders increase sufficiently.

- **Profitability and Revenue Trends.** The analysis should consider the buyer's historical growth and projected growth in revenues, and operating earnings, (usually EBITDA or EBITDA less capital expenditures) in addition to EPS. Issues to be vetted include customer concentrations, the source of growth, the source of any margin pressure and the like. The quality of earnings and a comparison of core vs. reported earnings over a multi-year period should be evaluated.

- **Pro Forma Impact.** The analysis should consider the impact of a proposed transaction on revenues, EBITDA, margins, EPS and capital structure. The per share accretion and dilution analysis of such metrics as earnings, EBITDA and dividends should consider both the buyer's and seller's perspectives.

- **Dividends.** In a yield starved world, dividend paying stocks have greater attraction than in past years. Sellers should not be overly swayed by the pick-up in dividends from swapping into the buyer's shares; however, multiple studies have demonstrated that a sizable portion of an investor's return comes from dividends over long periods of time. If the dividend yield is notably above the peer average, the seller should ask why? Is it payout related, or are the shares depressed? Worse would be if the market expected a dividend cut. These same questions should also be asked in the context of the prospects for further increases.

- **Capital Structure.** Does the acquirer operate with an appropriate capital structure given industry norms, cyclicality of the business and investment needs to sustain operations? Will the proposed acquisition result in an over-leveraged company, which in turn may lead to pressure on the buyer's shares and/or a rating downgrade if the buyer has rated debt?

- **Balance Sheet Flexibility.** Related to the capital structure should be a detailed review of the buyer's balance sheet that examines such areas as liquidity, access to bank credit, and the carrying value of assets such as deferred tax assets.

- **Ability to Raise Cash to Close.** What is the source of funds for the buyer to fund the cash portion of consideration? If the buyer has to go to market to issue equity and/or debt, what is the contingency plan if unfavorable market conditions preclude floating an issue?

- **Consensus Analyst Estimates.** If the buyer is publicly traded and has analyst coverage, consideration should be given to Street expectations vs. what the diligence process determines. If Street expectations are too high, then the shares may be vulnerable once investors reassess their earnings and growth expectations.

- **Valuation.** Like profitability, valuation of the buyer's shares should be judged relative to its history and a peer group presently as well as relative to a peer group through time to examine how investors' views of the shares may have evolved through market and profit cycles.

- **Share Performance.** Sellers should understand the source of the buyer's shares performance over several multi-year holding periods. For example, if the shares have significantly outperformed an index over a given holding period, is it because earnings growth accelerated? Or, is it because the shares were depressed at the beginning of the measurement period? Likewise, underperformance may signal disappointing earnings, or it may reflect a starting point valuation that was unusually high.

- **Strategic Position.** Assuming an acquisition is material for the buyer, directors of the selling board should consider the strategic position of the buyer, asking such questions about the attractiveness of the pro forma company to other acquirers.

- **Contingent Liabilities.** Contingent liabilities are a standard item on the due diligence punch list for a buyer. Sellers should evaluate contingent liabilities too.

The list does not encompass every question that should be asked as part of the fairness analysis, but it does illustrate that a liquid market for a buyer's shares does not necessarily answer questions about value, growth potential and risk profile.

We at Mercer Capital have extensive experience in valuing and evaluating the shares (and debt) of financial and non-financial service companies garnered from over three decades of business. Feel free to contact us to discuss your situation in confidence.

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