

STERLING PARTNERS

Sterling Partners Investment Thesis Challenge (SPITC)

November 2015

**INSPIRED
GROWTH**

30 YEAR HISTORY

of
S U C C E S S F U L
I N V E S T I N G

Institutional private equity investors
in the middle market since 2002

STERLING
PARTNERS

1983 – 2001 ENTREPRENEURIAL ROOTS

- Started in 1983 by four young entrepreneurs who built and sold a healthcare business
- 18 stand-alone buyout investments
- Deal-by-deal fundraising
- Funded by their own capital as well as friends and family
- Established foundation for working with seller/founders and entrepreneurs

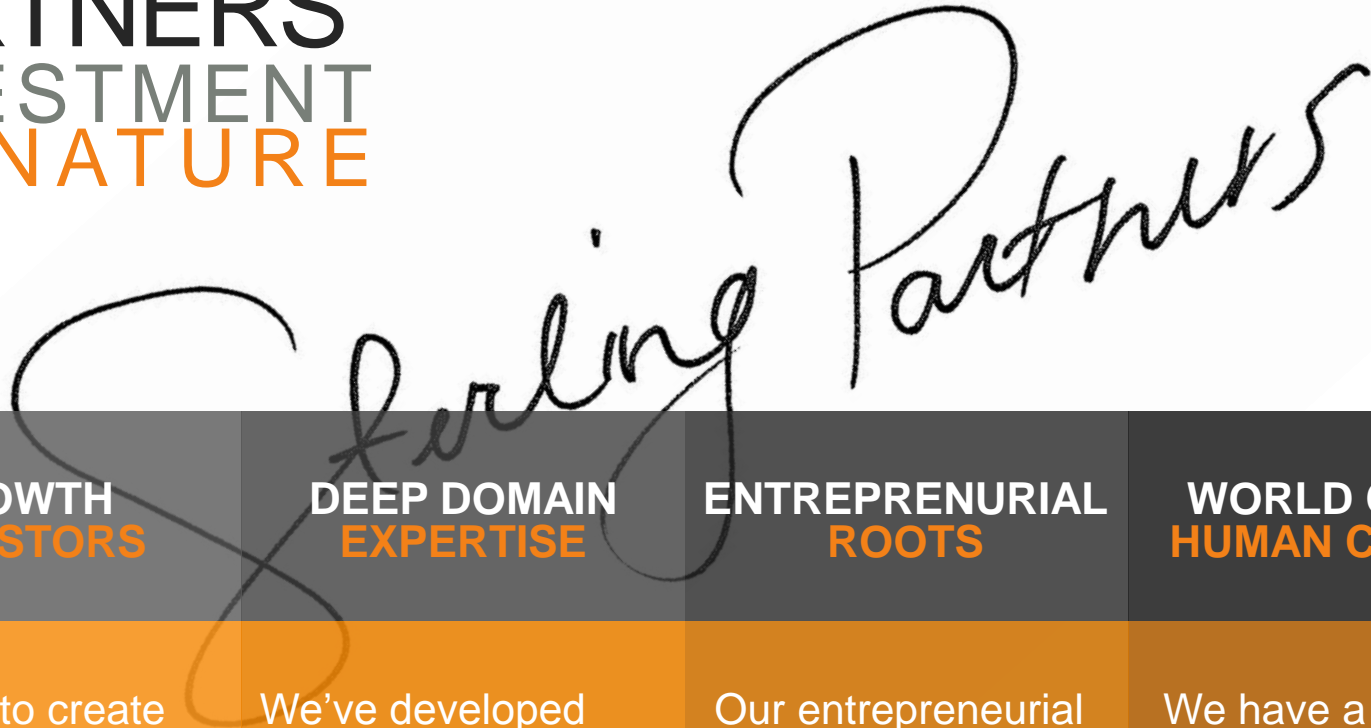
Since 2002 STERLING TODAY

- Headquartered in Chicago
- 20+ investment professionals¹
- \$3B Assets Under Management²
- Middle market growth-buyout funds
 - SCP Funds, I, II, III, & IV
 - 36 platform investments
 - Typical equity investment for SCP IV of \$35-120M
 - Primarily U.S. based businesses
- High quality institutional investor base

1. Includes associates. Excludes investment professionals fully dedicated to Sterling's Small Market Education Fund

2. AUM above is as of Q2-15. AUM = unrealized fair market value + uncalled commitments + all other fund level assets, including cash and cash equivalents (excludes the unrealized fair market value of certain co-investments in existing Sterling portfolio companies). AUM shown is only for Sterling Capital Partners (SCP) middle market buyout funds. During this period Sterling raised two venture funds, a small market growth fund and an education single-sector small market fund. Additional information available upon request

STERLING PARTNERS INVESTMENT SIGNATURE

A large, stylized handwritten signature in black ink that reads "Sterling Partners". The signature is written in a cursive, flowing style and is positioned diagonally across the upper half of the slide, overlapping the header and the table below.

GROWTH INVESTORS

We seek to create value by investing in transformational growth

DEEP DOMAIN EXPERTISE

We've developed extensive knowledge, experience and industry networks through 25+ years of successful investing in our three core sectors

ENTREPRENEURIAL ROOTS

Our entrepreneurial roots and firm culture provide differentiated seller/founder deal flow, which is fertile ground for our value creation strategy

WORLD CLASS HUMAN CAPITAL

We have a long history of infusing high-caliber executive talent, starting with CEO, into our portfolio companies to drive growth and value creation

Healthcare Services

- Supply/Demand imbalance (primary care physician shortage)
- Aging population, longer life expectancy
- Inefficiencies, opportunities to take costs out of the delivery market
- Retail-based, alternate site model (“consumerism” trends)
- Payor focus on patient outcomes (vs. fee for service)
- Opportunities in technology rollout for delivering and monitoring quality care delivery

Business Services

- *Subsector focus:*
 - *Asset Light Logistics*
 - *Industrial and Maintenance*
 - *Outsourced Professional Services*
 - *Information Services*
- Pressing need to maintain and replace aging infrastructure
- Increased regulatory oversight driving need for service and support solutions
- Re-industrialization of America, driven by resurgence in domestic energy production
- Continued shift towards specialization and service outsourcing

Education Services

- Traditional not-for-profit institutions seeking new ways to generate revenue
- Changing demographics (minority/adult students) and re-skilling of workforce driving demand in postsecondary space
- Continued growth in online programs, adult education and alternative learning models
- Increased opportunities for private solutions amidst declining K-12 government funding
- NOTE: Challenging regulatory climate has caused us to proceed with caution. Very high bar for investments at this time.

EXAMPLES OF STERLING DEALS BY SECTOR

Healthcare Services



Network of free-standing emergency rooms



Core measure and registry abstraction services to hospitals



Outsourced hospital services provider

Education



Aviation maintenance, training and flight school



Network of ABA accredited law schools



Provides instrument and vocal training to kids

Business Services



Comprehensive water flow solutions services provider



Data center manager and operator



Ecommerce fulfillment provider

STERLING PARTNERS INVESTMENT THESIS CHALLENGE (SPITC)

- › Sterling Partners is sponsoring an investment thesis competition for students at the Kellogg School of Management
- › SPITC debuted in 2011. Multiple Chicago-area private equity firms participated including Sterling Partners, Madison Dearborn, and Lake Capital
- › Goal is to provide (i) opportunity for students to work with private equity professionals to develop an investment thesis and (ii) idea generation for participating firms
- › Investment thesis focus
 - Focused on industry segment, not specific deal opportunity (eg take private of a specific company)
 - Selected industry segment should provide opportunities for late stage buyout or growth equity investments (as opposed to venture)
- › Sterling primarily invests in service companies; sectors of focus include healthcare, education and business services

HOW DOES IT WORK?

Phase 1

- › Form 2-3 person teams
- › *Kellogg students work with Heizer Center advisors (professors and PE professionals)*
- › Preliminary investment thesis submission due Thursday, January 21, 2016
 - Up to 8 page slide deck or word document
 - Identify thesis and rationale, team members and project plan/milestones

Phase 2

- › Sterling Partners selects investment theses which it is interested in pursuing
 - Sterling assigns a “sponsor” to selected student teams and works with teams to further develop theses through Q1 and early Q2 2014
- › *Kellogg students selected for Phase 2 receive course credit*
- › Selected teams acknowledge Sterling’s exclusive right to use the investment thesis
- › Financial support / expense coverage of up to \$2,000 per team
- › Other private equity firms may choose to participate, although there will be no overlap in theses
 - Almost half of teams submitting theses last year were sponsored by a PE firm

Phase 3

- › Teams present theses to Sterling Investment Committee in May (date determined between Sterling sponsor and team)
 - **Winning teams receive \$5,000 prize (multiple winners may be selected)**

INVESTMENT THESIS: KEY ELEMENTS

Investment Thesis Overview

- **Why the Industry**

- › Long term trends
- › Market size & breakdown
- › Market growth
- › Growth drivers
- › Industry dynamics

- **Why the Business Model**

- › Business model characteristics
- › Map the market & value chain
- › Addresses key pain point
- › Fits PE model
- › Targets exist

- **Why Now**

- › Timing impetus
- › Market impetus
- › Path to invest
- › POV on market evolution

- **Post Closing Strategy to Win**

- Operational value adds
 - Strategy
 - Human Capital
 - IT
 - Governance
- Other value adds

Sample *Long Term* Trends

- Population changes
- Compliance and risk management
- Suppressed natural gas prices
- Environmental sustainability
- Aging infrastructure

Sample Business Model Characteristics

- Platform capable of high growth
- Sustainable and scalable
- Differentiated strategy
- Recurring revenue
- Attractive exit alternatives
- Low customer concentration
- Opportunities for operational improvement
- Entrenched customers (e.g. stickiness)
- Defensible position/barriers to entry
- Profitable and positive cash flow
- Operating leverage
- Minimal adoption risk
- High value proposition

New investment: Innotrac

Investment Thesis

Market

Ecommerce Fulfillment

- › Strong growth and runway - eCommerce is projected to grow greater than 10% per year from 2012 to 2017.¹
- › Mobile and tablet will drive continued growth

Business Model

Outsourced Fulfillment Provider
focused on General Retail and
Apparel eCommerce Brands

- › Picks and shovels of eCommerce
- › Flexible trough to peak staffing model
- › High quality, back-end service offering (not end-to-end)

The Platform

Innotrac

- › Best-in-Class operations and blue-chip customer base
- › Strong industry position with no channel conflict
- › Significant room for growth (organic and acquisitions)

Post-Close

Strategy to Win

- › Sales pipeline development and conversion
- › Acquisition, domestic and international expansion
- › Service area development
- › Opportunities to automate/streamline warehouse ops

(1) Forrester Research /U.S. Census Bureau (2013)