Overview

• VMI Index – Federal Services Company Outperform Broader Markets
• Debt and Equity Markets
• Defense M&A
  – ‘08–’09 Transactions
  – Changes in Contracting/Procurement
  – ’09 Defense M&A Outlook
Federal Services Company Outperform Broader Markets

Gain/Loss from 12/31/04 Values

- VMI Index: 10.0%
- Spade: -3.7%
- S&P: -23.3%

Source: Spade Index, Yahoo Finance and Venture Management
## Total Enterprise Value/LTM EBITDA

<table>
<thead>
<tr>
<th>Name</th>
<th>Ticker</th>
<th>Stock Price*</th>
<th>% of 52 Week High</th>
<th>LTM EBITDAX</th>
</tr>
</thead>
<tbody>
<tr>
<td>Applied Signal Technology, Inc.</td>
<td>APSG</td>
<td>19.20</td>
<td>89.1%</td>
<td>9.39x</td>
</tr>
<tr>
<td>ARGON ST, Inc.</td>
<td>STST</td>
<td>18.82</td>
<td>69.0%</td>
<td>9.12x</td>
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<tr>
<td>CACI International Inc</td>
<td>CACI</td>
<td>39.85</td>
<td>74.7%</td>
<td>7.36x</td>
</tr>
<tr>
<td>Dynamics Research Corporation</td>
<td>DRCO</td>
<td>8.73</td>
<td>81.2%</td>
<td>5.18x</td>
</tr>
<tr>
<td>ManTech International Corporation</td>
<td>MANT</td>
<td>37.41</td>
<td>60.9%</td>
<td>8.07x</td>
</tr>
<tr>
<td>SRA International, Inc.</td>
<td>SRX</td>
<td>16.75</td>
<td>68.2%</td>
<td>7.61x</td>
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<tr>
<td>VSE Corporation</td>
<td>VSEC</td>
<td>27.03</td>
<td>56.6%</td>
<td>3.83x</td>
</tr>
</tbody>
</table>

* As of 5/8/09

Source: Capital IQ and Venture Management, Inc.
It’s A Lender’s Market

We interviewed senior lenders that finance M&A for defense and federal contractors.

Their current thinking:
• Easier to get smaller deals completed
• Tighter loan terms:
  • More collateral
  • Higher fees
  • Harsher consequences for covenant breaches
  • Shorter term payback periods
  • More equity required in financed M&A deals
  • Greater diligence on contracts, backlog, financials
  • More ‘structured’ transactions – seller notes, earn-outs
  • Lower multiples on cash flow in determining maximum debt
  • Interest floors instituted on revolvers
Capital Markets: Public Equity

- IPO Window Closed

Source: IPOBoutique.com
Private Equity Total Deal Flow

Source: PitchBook Platform
Impact on M&A Transaction Process

- Due diligence
- Bank approval
- ‘Structured’ Transactions
- Indemnity risk
Steady Decline in Activity

2008 - 2009 Defense Transactions

<table>
<thead>
<tr>
<th>Series1</th>
<th>Q1 08</th>
<th>Q2 08</th>
<th>Q3 08</th>
<th>Q4 08</th>
<th>Q1 09</th>
<th>Q2 09*</th>
</tr>
</thead>
<tbody>
<tr>
<td>No. of Transactions</td>
<td>22</td>
<td>23</td>
<td>22</td>
<td>13</td>
<td>10</td>
<td>7</td>
</tr>
</tbody>
</table>

* Through May 15, 2009  
Source: Venture Management, Inc.
Changes in Defense Sector

- **Obama Directive:**
  - More full and open competition,
  - Fixed price contracts,
  - Limit government outsourcing

- **Funding priorities** shifting toward
  - Education
  - Energy
  - Environment
Budget/Contract Environment for Federal Contractors

- Transparency
- Accountability
- Small business set-asides
- Tighter sole-source justifications
- DoD: bring more work in-house
- Fixed price contracts
- Funding uncertainties
- Acquisition workforce
Procurement Changes

Stimulus funding
- Quarterly progress reports
- Added disclosure for executive pay

DCAA Policy
- Culture shift
- Penalties for non-compliance
2H09 Outlook for Defense Buyers

- **Private equity groups** still active, waiting for return of debt markets
- **New funds** emerging from prior CEO/founders
- **Larger defense companies**, underleveraged and flush, motivated to acquire
- **Foreign appetite** for US companies
2H09 Outlook for Defense Sellers

- Small business re-certification impinges value
- Mid-tier defense pure-plays more apt to sell
- M&A market increasingly bifurcated, favoring companies with priority sectors/customers and distinguished capabilities
  - cyber-security
  - re-set/logistics
  - military health care IT
  - soft power
  - information assurance
  - intelligence
  - infrastructure
  - Collaboration/interoperability
  - Unmanned surveillance/warfare
  - Stealth technologies
Lots of Buyers of Defense Companies…

- Defense Contractors are flush with cash and excess debt capacity
  - $41.2B amongst top Tier A&D companies
  - +$2.1B among publicly traded Government Service pure plays
- Private Equity building pipeline, poised to launch
… but not a lot of deals

**Hurdles to closed transactions**

- Valuation expectations of sellers
- Banks and investors: less tolerance for risk
- Federal Spending shakeout
- “Time Kills All Deals”
- Hitting tolerance limits on Deal Terms
Commitment – Integrity – Performance

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