

INTERVIEW

Ginny Heine

Senior Vice President & Regional Manager, National Capital Region
Citizens Bank

Few bankers have better insight to the financing of government contractor acquisitions than Ginny Heine, Senior Vice President and Regional Manager, National Capital Region for Citizens Bank. She oversees the bank's regional commercial lending efforts, including the Government Contracting unit located in Vienna, Va. A veteran of government contracting lending, she has helped arrange financing for contractor luminaries such as Anteon Corp. and Mantech International Corp.

With M&A continuing apace in the government services sector, DM&A columnist Paul Serotkin caught up with Ginny to gather her views on the market.

DM&A: Why does Citizens find the government market so attractive?

GH: Several reasons . . . not the least of which is that government contractors use leverage to improve their ROE more than companies in other industries. Therefore, we are attracted to the government market, because there is a high demand for our product – we lend money and take deposits; it's a nice fit.

Equally as attractive is the risk profile of government contractors. At first blush, they appear more risky in comparison to the metrics of commercial companies. Understanding the unique characteristics of this industry, including their risk/return model, the FAR/DFAR, the procurement evolution and current environment (CICA, FASA, etc.), the unique accounting issues and application of CAS, the impact of politics and world events, the regulations and oversight, etc. has enlightened us to be attracted to the government contracting industry rather than shy away from it. Candidly, our businesses are not so dissimilar (use of leverage, criticality of integrity, environment of regulation and oversight).

DM&A: How does this market alignment play into your assessment of risk?

GH: As a lending risk, we feel that government contractors are relatively stable. Having closed many working capital credit facilities and M&A financings in the sector, we understand how to mitigate industry specific risks.

We'll flag firms that may be pushing the risk envelope. When a company doesn't exhibit the requisite internal finance and accounting controls, for example, we stay away from the opportunity or factor the risk into terms and pricing.

DM&A: What factors should an acquisitive government contractor seek in a commercial lender?

GH: Industry, industry, industry! The bank should be committed to the government sector, as evidenced by line and credit personnel with a depth of experience in lending to government contractors. Ask specifically whether the bank has structured and closed credit facilities for government contractors, both to support operations and M&A. In my view, the bank with these qualifications should be considered as the lender of choice.

As a bank with broad national coverage, our group provides industry-specific support to Citizens' regional offices, leveraging this resource when servicing a government contractor outside the Beltway.

DM&A: How does the bank evaluate a proposed loan for an acquiring company?

GH: We always start out with the 'soft' aspects of a deal, getting to know the management, owners and specific dynamics of the company/transaction. Do we want to work with the management of the buyer and seller? Are they reliable in

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bundled with E&S Systems.”

Acting on the advice of its financial advisor, William Blair & Co., LLC, **Reinhold Industries, Inc.** (NASDAQ: RNHDA) announced it has decided not to sell the company at this time. But it has adopted a policy of issuing a regular quarterly cash dividend.

In September 2003 the company had commenced a review of strategic alternatives for maximizing shareholder value.

Reinhold manufactures advanced custom composite components, sheet molding compounds, and graphic arts and industrial rollers for a variety of applications in the U.S. and Europe.

Homeland Security

CompuDyne Corp. (NASDAQ: CDCY) acquired **90 Degrees, Inc.** of Yakima, Washington.

90 Degrees, Inc. is a provider of mission critical fire and emergency medical information management systems for public, military and private public safety agencies. The company, which only recently emerged from the development stage, is expected to generate modest revenues in the “low millions” in 2005

BIO-key International, Inc. (OTC Bulletin Board: BKYI.OB) signed a definitive agreement to acquire the Mobile Government Division of **Aether Systems, Inc.** (NASDAQ: AETH) for \$10 million in cash.

BIO-key officials said that the combined companies will be the largest U.S. provider of wireless information technologies for law enforcement and public safety organizations.

AMG solutions are currently deployed in state and local police, fire and rescue and emergency medical services organizations and are fully integrated into 47 different state information

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meeting their numbers? What is the outlook for their business, programs, contract backlog? On top of this subjective evaluation, of course, we evaluate the metrics, factoring in the level of collateral coverage and the total debt to the company's trailing twelve month EBITDA - earnings before interest, depreciation and amortization (*ed. note - often used as a proxy for one measure of cash flow*).

In today's environment, banks are lending to government contractors at total debt to EBITDA multiples of anywhere from 3.0X to 4.5X.

DM&A: How has the lending environment for government contractors changed in the past year?

GH: Lending multiples have been fairly steady over the past 12 months. I think this is the right place for them. Companies have been somewhat whipsawed by credit ebbs and flows over the past several years; the current lending environment seems to capture today's market risk just right.

DM&A: For first-to-market government acquirers, how should they assess the importance of the EBITDA multiple?

GH: Using EBITDA for the sellers' trailing twelve months is a good place to start. Sellers will also present their EBITDA on an adjusted basis, taking into account costs that will not continue post-closing. They also will provide projections for future years. Our job, in concert with the borrower, and often independent of them, is to understand the plausibility of such claims, since they affect the lending appetite of the bank in that deal.

DM&A: How would you characterize the competitive environment for lenders in the government sector?

GH: It has become very competitive in the last several years.

Even before the increased federal funding, largely as a result of 9/11, Beltway area banks had gravitated to the government sector in response to the weakened general economy and the fact that the DC metro economy is largely made up of government contractors.

Five years ago, federal contractor growth was slower than today, as commercial IT firms attracted some of the best people with the allure of stock options and outsized salaries. So the government market itself was not as appealing to many in the banking world.

DM&A: For first time federal contractor acquirers, at what point in the M&A process should they approach their bank about the proposed transaction?

GH: Maybe this is obvious, but the sooner the better. You do not want to be very far down the road with a target seller and not have gotten the view of your bank. Even if the deal does not go through, it is important to have your banker as a partner during this process; you can certainly learn about the process for the next deal. ♦