Compass Group Diversified Holdings LLC
Form 10-K
March 06, 2013
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2012

or

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from _________ to _________

Commission File Number: 001-34927

Compass Diversified Holdings

(Exact name of registrant as specified in its charter)

Delaware	**57-6218917**
(Jurisdiction of incorporation	**(I.R.S. Employer**
or organization)	**Identification No.)**

Commission File Number: 001-34926

Compass Group Diversified Holdings LLC

(Exact name of registrant as specified in its charter)

Delaware	**20-3812051**
(Jurisdiction of incorporation	**(I.R.S. Employer**
or organization)	**Identification No.)**

Sixty One Wilton Road	
Second Floor	
Westport, CT	**06880**
(Address of principal executive offices)	**(Zip Code)**

(203) 221-1703

(Registrants telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Shares representing beneficial interests in Compass Diversified Holdings (trust shares)	**New York Stock Exchange**

Securities registered pursuant to Section 12 (g) of the Act: None

Indicate by check mark if the registrants are collectively a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ¨ No x

Indicate by check mark if the registrants are collectively not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ¨ No x

Indicate by check mark whether the registrants (1) have filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrants were required to file such reports), and (2) have been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrants have submitted electronically and posted on their corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrants knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ¨

Indicate by check mark whether the registrants are collectively a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of large accelerated filer , accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨	Smaller reporting company	¨

Indicate by check mark whether the registrants are collectively a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

The aggregate market value of the outstanding shares of trust stock held by non-affiliates of Compass Diversified Holdings at June 30, 2012 was $550,707,370 based on the closing price on the New York Stock Exchange on that date. For purposes of the foregoing calculation only, all directors and officers of the registrant have been deemed affiliates.

There were 48,300,000 shares of trust stock without par value outstanding at February 25, 2013.

Documents Incorporated by Reference

Certain information in the registrant s definitive proxy statement to be filed with the Commission relating to the registrant s 2012 Annual Meeting of Stockholders is incorporated by reference into Part III.

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NOTE TO READER

In reading this Annual Report on Form 10-K, references to:

- the Trust and Holdings refer to Compass Diversified Holdings;
- businesses , operating segments , subsidiaries and reporting units all refer to, collectively, the businesses controlled by the Company;
- the Company refer to Compass Group Diversified Holdings LLC;
- the Manager refer to Compass Group Management LLC (CGM);
- the initial businesses refer to, collectively, Staffmark Holdings, Inc., Crosman Acquisition Corporation, Compass AC Holdings, Inc. and Silvue Technologies Group, Inc.;
- the 2007 acquisitions refer to, collectively, the acquisitions of Aeroglide Corporation, HALO Branded Solutions and American Furniture Manufacturing;
- the 2008 acquisitions refer to, collectively, the acquisitions of Fox Factory Inc. and Staffmark Investment LLC;
- the 2010 acquisitions refer to, collectively, the acquisitions of Liberty Safe and Security Products, LLC and Ergobaby Carrier, Inc.;
- the 2011 acquisition refer to the acquisition of CamelBak Products, LLC;
- the 2012 acquisition refer to the acquisition of Arnold Magnetic Technologies;
- the 2007 disposition refer to the sale of Crosman Acquisition Corporation;
- the 2008 dispositions refer to, collectively, the sales of Aeroglide Corporation and Silvue Technologies Group, Inc.;
- the 2011 disposition refer to the sale of Staffmark Holdings, Inc.;
- the 2012 disposition refer to the sale of HALO Branded Solutions.;
- the Trust Agreement refer to the amended and restated Trust Agreement of the Trust dated as of April 25, 2007;

the Prior Credit Agreement refer to the Credit Agreement with a group of lenders led by Madison Capital, LLC which provided for a Prior Revolving Credit Facility and a Prior Term Loan Facility ;

the Credit Facility refer to the Credit Facility with a group of lenders led by TD Securities (USA) LLC (TD Securities) which provides for a Revolving Credit Facility and a Term Loan Facility;

the Revolving Credit Facility refer to the $290 million Revolving Credit Facility provided by the Credit Facility that matures in December 2016;

the Term Loan Facility refer to the $252.5 million Term Loan Facility, as of December 31, 2012, provided by the Credit Facility that matures in December 2017;

the LLC Agreement refer to the second amended and restated operating agreement of the Company dated as of January 9, 2007; and

we , us and our refer to the Trust, the Company and the businesses together.

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Statement Regarding Forward-Looking Disclosure

This Annual Report on Form 10-K, including the sections entitled Risk Factors, Management s Discussion and Analysis of Financial Condition and Results of Operations and Business, contains forward-looking statements. We may, in some cases, use words such as project, predict, believe, anticipate, plan, expect, estimate, intend, should, would, could, potentially, or may or other words that convey unc events or outcomes to identify these forward-looking statements. Forward-looking statements in this Annual Report on Form 10-K are subject to a number of risks and uncertainties, some of which are beyond our control,

our ability to successfully operate our businesses on a combined basis, and to effectively integrate and improve any future acquisitions;

our ability to remove our Manager and our Manager s right to resign;

our trust and organizational structure, which may limit our ability to meet our dividend and distribution policy;

our ability to service and comply with the terms of our indebtedness;

our cash flow available for distribution and our ability to make distributions in the future to our shareholders;

our ability to pay the management fee, profit allocation when due and pay the put price if and when due;

our ability to make and finance future acquisitions;

our ability to implement our acquisition and management strategies;

the regulatory environment in which our businesses operate;

trends in the industries in which our businesses operate;

changes in general economic or business conditions or economic or demographic trends in the United States and other countries in which we have a presence, including changes in interest rates and inflation;

environmental risks affecting the business or operations of our businesses;

our and our Manager s ability to retain or replace qualified employees of our businesses and our Manager;

costs and effects of legal and administrative proceedings, settlements, investigations and claims; and

extraordinary or force majeure events affecting the business or operations of our businesses.
including, among other things:

Our actual results, performance, prospects or opportunities could differ materially from those expressed in or implied by the forward-looking statements. A description of some of the risks that could cause our actual results to differ appears under the section Risk Factors . Additional risks of which we are not currently aware or which we currently deem immaterial could also cause our actual results to differ.

In light of these risks, uncertainties and assumptions, you should not place undue reliance on any forward-looking statements. The forward-looking events discussed in this Annual Report on Form 10-K may not occur. These forward-looking statements are made as of the date of this Annual Report. We undertake no obligation to publicly update or revise any forward-looking statements to reflect subsequent events or circumstances, whether as a result of new information, future events or otherwise, except as required by law.

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PART I

ITEM 1. BUSINESS

Compass Diversified Holdings, a Delaware statutory trust (Holdings , or the Trust), was incorporated in Delaware on November 18, 2005. Compass Group Diversified Holdings, LLC, a Delaware limited liability Company (the Company), was also formed on November 18, 2005. The Trust and the Company (collectively CODI) were formed to acquire and manage a group of small and middle-market businesses headquartered in North America. The Trust is the sole owner of 100% of the Trust Interests, as defined in our LLC Agreement, of the Company. Pursuant to the LLC Agreement, the Trust owns an identical number of Trust Interests in the Company as exist for the number of outstanding shares of the Trust. Accordingly, our shareholders are treated as beneficial owners of Trust Interests in the Company and, as such, are subject to tax under partnership income tax provisions.

The Company is the operating entity with a board of directors whose corporate governance responsibilities are similar to that of a Delaware corporation. The Company s board of directors oversees the management of the Company and our businesses and the performance of Compass Group Management LLC (CGM or our Manager). Our Manager is the sole owner of our Allocation Interests, as defined in our LLC Agreement.

Overview

We acquire controlling interests in and actively manage businesses that we believe operate in industries with long-term macroeconomic growth opportunities, and that have positive and stable cash flows, face minimal threats of technological or competitive obsolescence and have strong management teams largely in place.

Our unique public structure provides investors with an opportunity to participate in the ownership and growth of companies which have historically been owned by private equity firms, wealthy individuals or families. Through the acquisition of a diversified group of businesses with these characteristics, we also offer investors an opportunity to diversify their own portfolio risk while participating in the ongoing cash flows of those businesses through the receipt of distributions.

Our disciplined approach to our target market provides opportunities to methodically purchase attractive businesses at values that are accretive to our shareholders. For sellers of businesses, our unique structure allows us to acquire businesses efficiently with little or no financing contingencies and, following acquisition, to provide our businesses with substantial access to growth capital.

We believe that private company operators and corporate parents looking to sell their businesses may consider us an attractive purchaser because of our ability to:

- provide ongoing strategic and financial support for their businesses;
- maintain a long-term outlook as to the ownership of those businesses where such an outlook is required for maximization of our shareholders return on investment; and
- consummate transactions efficiently without being dependent on third-party financing on a transaction-by-transaction basis.

In particular, we believe that our outlook on length of ownership and active management on our part may alleviate the concern that many private company operators and parent companies may have with regard to their businesses going through multiple sale processes in a short period of time. We believe this outlook both reduces the risk that businesses may be sold at unfavorable points in the overall market cycle and enhances our ability to develop a comprehensive strategy to grow the earnings and cash flows of our businesses, which we expect will better enable us to meet our long-term objective of paying distributions to our shareholders and increasing shareholder value.

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Finally, we have found that our ability to acquire businesses without the cumbersome delays and conditions typical of third party transactional financing can be very appealing to sellers of businesses who are interested in confidentiality and certainty to close.

We believe our management team s strong relationships with industry executives, accountants, attorneys, business brokers, commercial and investment bankers, and other potential sources of acquisition opportunities offer us substantial opportunities to assess small to middle market businesses that may be available for acquisition. In addition, the flexibility, creativity, experience and expertise of our management team in structuring transactions allows us to consider non-traditional and complex transactions tailored to fit a specific acquisition target.

In terms of the businesses in which we have a controlling interest as of December 31, 2012, we believe that these businesses have strong management teams, operate in strong markets with defensible market niches and maintain long standing customer relationships. We believe that the strength of this model, which provides for significant industry, customer and geographic diversity, has become even more apparent in the current challenging economic environment.

2012 Highlights

Acquisition of Arnold Magnetics

On March 5, 2012, we purchased a 96.6% controlling interest (on a primary and fully diluted basis) in Arnold Magnetics, with headquarters in Rochester, NY. Arnold Magnetics has an operating history of more than 100 years and is a leading global manufacturer of engineered magnetic solutions for a wide range of specialty applications and end-markets, including energy, medical, aerospace and defense, consumer electronics, general industrial and automotive. From its nine manufacturing facilities located in the United States, the United Kingdom, Switzerland and China, the company produces high performance permanent magnets, flexible magnets and precision foil products that are mission critical in motors, generators, sensors and other systems and components. Based on its long-term relationships, Arnold Magnetics has built a diverse and blue-chip customer base totaling more than 2,000 clients worldwide.

The purchase price, including proceeds from non-controlling interests, was approximately $130.5 million (excluding acquisition-related costs) and was based on a total enterprise value of $124.2 million and included approximately $6.3 million in cash and working capital. Acquisition related costs were approximately $4.8 million. We funded the acquisition through available cash on hand and a draw of $25 million on our Revolving Credit Facility. Arnold s management and certain other investors invested in the transaction alongside us, collectively representing approximately 3.4% in initial non-controlling interest on a primary and fully diluted basis. CGM acted as an advisor to us in the transaction and received fees and expense payments totaling approximately $1.2 million.

Preferred Stock Redemption

On March 6, 2012, we redeemed CamelBak s 11% convertible preferred stock for $45.3 million plus accrued dividends of $2.7 million, from an affiliate of CGI Magyar Holdings LLC, CODI s largest shareholder. The redemption was funded with available cash on hand.

Debt Re-pricing

On April 2, 2012, we exercised our option for an incremental term loan in the amount of $30 million. The incremental term loan was issued at 99% of par value and increased the term loans outstanding under the Credit Facility from approximately $224.4 million to approximately $254.4 million. In addition, in connection with the option we reduced the margin on Term Loan Facility LIBOR Loans from 6.00% to 5.00%, Base Rate Loans from 5.00% to 4.00% and reduced the LIBOR floor from 1.50% to 1.25%. We paid an amendment fee of approximately $2.2 million, and incurred additional fees and expenses of approximately $0.6 million. Net proceeds from this incremental term loan were used to reduce outstanding loans on the Revolving Credit Facility.

Sale of HALO

On May 1, 2012, we sold all of the issued and outstanding capital stock of HALO to Candlelight Investment Holdings, Inc. The total enterprise value received for HALO was $76.5 million.

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At the closing, we received approximately $66.0 million in cash in respect of our debt and equity interests in HALO and for the payment of accrued interest and fees after payments to non-controlling shareholders and payment of all transaction expenses. We received an additional approximately $0.8 million in 2012 that were held in escrow. The net proceeds were used to repay outstanding debt under our Revolving Credit Facility. We recorded a loss on the sale of HALO of $0.5 million.

2012 Distributions

For the 2012 fiscal year we declared and paid distributions to our shareholders totaling $1.44 per share.

The following is a brief summary of the businesses in which we own a controlling interest at December 31, 2012:

Advanced Circuits

Compass AC Holdings, Inc. (Advanced Circuits or ACI), headquartered in Aurora, Colorado, is a provider of prototype, quick-turn and production rigid printed circuit boards, or PCBs , throughout the United States. PCBs are a vital component of virtually all electronic products. The prototype and quick-turn portions of the PCB industry are characterized by customers requiring high levels of responsiveness, technical support and timely delivery. We made loans to and purchased a controlling interest in Advanced Circuits, on May 16, 2006, for approximately $81.0 million. We currently own 69.4% of the outstanding stock of Advanced Circuits on a primary and fully diluted basis.

American Furniture

AFM Holding Corporation (American Furniture or AFM) headquartered in Ecru, Mississippi, is a leader in the manufacturing of low-cost upholstered stationary and motion furniture, including sofas, loveseats, sectionals, recliners and complementary products to the promotional furniture market. We made loans to and purchased a controlling interest in AFM on August 31, 2007 for approximately $97.0 million. We currently own approximately 99.9% of AFM s outstanding stock on a primary basis and fully diluted basis.

Arnold

AMT Acquisition Corporation (Arnold or Arnold Magnetics), headquartered in Rochester, NY, with nine additional facilities worldwide, is a manufacturer of engineered, application specific permanent magnets. Arnold Magnetics products are used in applications such as general industrial, reprographic systems, aerospace and defense, advertising and promotional, consumer and appliance, energy, automotive and medical technology. Arnold Magnetics is the largest U.S. manufacturer of engineered magnets as well as only one of two domestic producers to design, engineer and manufacture rare earth magnetic solutions. We made loans to, and purchased a controlling interest in Arnold on March 5, 2012 for approximately $122.4 million. We currently own 96.7% of the outstanding stock of Arnold on a primary basis and 87.6% on a fully diluted basis.

CamelBak

CamelBak Products LLC (CamelBak), headquartered in Petaluma, California, is a diversified hydration and personal protection platform offering products for outdoor, recreation and military applications. CamelBak offers a broad range of recreational / military hydration packs, reusable water bottles, specialized military gloves and performance accessories. We made loans to, and purchased a controlling interest in, CamelBak on August 24, 2011 for approximately $211.6 million. We currently own 89.9% of the outstanding stock of CamelBak on a primary basis and 79.7% on a fully diluted basis.

Ergobaby

Ergobaby Carrier, Inc. (Ergobaby), headquartered in Los Angeles, California, is a premier designer, manufacturer and distributor of baby wearing products, stroller travel systems and accessories. Ergobaby s reputation for product innovation, reliability and safety has led to numerous awards and accolades from consumer surveys and publications. Ergobaby offers a broad range of wearable baby carriers, stroller travel systems and related products that are sold through more than 600 retailers and web shops in the United States and internationally. We made loans to, and purchased a controlling interest in, Ergobaby on September 16, 2010 for approximately $85.2 million. We currently own 81.1% of the outstanding stock of Ergobaby on a primary basis and 77.1% on a fully diluted basis.

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Fox

Fox Factory Holding Corp. (Fox) headquartered in Scotts Valley, California, is a designer, manufacturer and marketer of high end suspension products for mountain bikes and power sports, which includes; all-terrain vehicles, snowmobiles and other off-road vehicles. Fox acts both as a tier one supplier to leading action sports original equipment manufacturers (OEM) and provides after-market products to retailers and distributors (Aftermarket). Fox s products are recognized as the industry s performance leaders by retailers and end-users alike. We made loans to and purchased a controlling interest in Fox on January 4, 2008, for approximately $80.4 million. We currently own 75.8% of the outstanding common stock on a primary basis and 70.6% on a fully diluted basis.

Liberty Safe

Liberty Safe and Security Products, Inc. (Liberty Safe or Liberty), headquartered in Payson, Utah, is a designer, manufacturer and marketer of premium home and gun safes in North America. From it s over 200,000 square foot manufacturing facility, Liberty produces a wide range of home and gun safe models in a broad assortment of sizes, features and styles. We made loans to and purchased a controlling interest in Liberty Safe on March 31, 2010 for approximately $70.2 million. We currently own 96.2% of the outstanding stock of Liberty Safe on a primary basis and 86.7% on a fully diluted basis.

Tridien

Anodyne Medical Device, Inc. (Anodyne , which was rebranded as Tridien in September 2010) headquartered in Coral Springs, Florida, is a leading designer and manufacturer of powered and non-powered medical therapeutic support services and patient positioning devices serving the acute care, long-term care and home health care markets. Tridien is one of the nation s leading designers and manufacturers of specialty therapeutic support surfaces and is able to manufacture products in multiple locations to better serve a national customer base. We made loans to and purchased a controlling interest in Tridien from CGI on August 1, 2006 for approximately $31.0 million. We currently own 81.3% of the outstanding capital stock on a primary basis and 67.4% on a fully diluted basis.

Our businesses also represent our operating segments. See Our Businesses and Note E Operating Segment Data to our Consolidated Financial Statements for further discussion of our businesses as our operating segments.

Tax Reporting

Information returns will be filed by the Trust and the Company with the IRS, as required, with respect to income, gain, loss, deduction and other items derived from the company s activities. The Company has and will file a partnership return with the IRS and intends to issue a Schedule K-1 to the trustee. The trustee intends to provide information to each holder of shares using a monthly convention as the calculation period. For 2012, and future years, the Trust has, and will continue to file a Form 1065 and issue Schedule K-1 to shareholders. For 2012, we delivered the Schedule K-1 to shareholders within the same time frame as we delivered the schedule to shareholders for the 2011 and 2010 taxable year. The relevant and necessary information for tax purposes is readily available electronically through our website. Each holder will be deemed to have consented to provide relevant information, and if the shares are held through a broker or other nominee, to allow such broker or other nominee to provide such information as is reasonably requested by us for purposes of complying with our tax reporting obligations.

WHERE YOU CAN FIND ADDITIONAL INFORMATION

We have filed with the SEC Forms S-1 and S-3 under the Securities Act, and Forms 10-Q, 10-K, and 8-K under the Exchange Act, which include exhibits, schedules and amendments. In addition, copies of such reports are available free of charge that can be accessed indirectly through our website http://www.compassdiversifiedholdings.com and are available as soon as reasonably practicable after such documents are electronically filed or furnished with the SEC.

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(1) CGI and its affiliates beneficially own approximately 16.4% of the Trust shares and is our single largest holder. Mr. Offenberg is not a director, officer or member of CGI or any of its affiliates.
(2) Owned by members of our Manager.
(3) Mr. Offenberg is a partner of this entity.
(4) The Allocation Interests, which carry the right to receive a profit allocation, represent less than 0.1% equity interest in the Company.
(5) Mr. Day is a non-managing member.

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Our Manager

Our Manager, CGM, has been engaged to manage the day-to-day operations and affairs of the Company and to execute our strategy, as discussed below. Our management team has worked together since 1998. Collectively, our management team has extensive experience in acquiring and managing small and middle market businesses. We believe our Manager is unique in the marketplace in terms of the success and experience of its employees in acquiring and managing diverse businesses of the size and general nature of our businesses. We believe this experience will provide us with an advantage in executing our overall strategy. Our management team devotes a majority of its time to the affairs of the Company.

We have entered into a management services agreement (the Management Services Agreement) pursuant to which our Manager manages the day-to-day operations and affairs of the Company and oversees the management and operations of our businesses. We pay our Manager a quarterly management fee for the services it performs on our behalf. In addition, our Manager receives a profit allocation with respect to its Allocation Interests in us. See Part III, Item 13 Certain Relationships and Related Transactions for further descriptions of the management fees and profit allocation to be paid to our Manager. In consideration of our Manager s acquisition of the Allocation Interests, we entered into a Supplemental Put agreement with our Manager pursuant to which our Manager has the right to cause us to purchase its Allocation Interests upon termination of the Management Services Agreement. Our Manager owns 100% of the Allocation Interests of the Company, for which it paid $0.1 million.

The Company s Chief Executive Officer and Chief Financial Officer are employees of our Manager and have been seconded to us. Neither the Trust nor the Company has any other employees. Although our Chief Executive Officer and Chief Financial Officer are employees of our Manager, they report directly to the Company s board of directors. The management fee paid to our Manager covers all expenses related to the services performed by our Manager, including the compensation of our Chief Executive Officer and other personnel providing services to us. The Company reimburses our Manager for the salary and related costs and expenses of our Chief Financial Officer and his staff, who dedicate substantially all of their time to the affairs of the Company.

See Part III, Item 13, Certain Relationships and Related Party Transactions and Director Independence .

Market Opportunity

We acquire and actively manage small and middle market businesses. We characterize small to middle market businesses as those that generate annual cash flows of up to $60 million. We believe that the merger and acquisition market for small to middle market businesses is highly fragmented and provides opportunities to purchase businesses at attractive prices. We believe that the following factors contribute to lower acquisition multiples for small and middle market businesses:

- there are fewer potential acquirers for these businesses;
- third-party financing generally is less available for these acquisitions;
- sellers of these businesses frequently consider non-economic factors, such as continuing board membership or the effect of the sale on their employees; and
- these businesses are less frequently sold pursuant to an auction process.

We believe that opportunities exist to augment existing management at such businesses and improve the performance of these businesses upon their acquisition. In the past, our management team has acquired businesses that were owned by entrepreneurs or large corporate parents. In these cases, our management team has frequently found that there have been opportunities to further build upon the management teams of acquired businesses beyond those in existence at the time of acquisition. In addition, our management team has frequently found that financial reporting and management information systems of acquired businesses may be improved, both of which can lead to improvements in earnings and cash flow. Finally, because these businesses tend to be too small to have their own corporate development efforts, we believe opportunities exist to assist these businesses as they pursue organic or external growth strategies that were often not pursued by their previous owners.

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Our Strategy

We have two primary strategies that we use in order to provide distributions to our shareholders and increase shareholder value. First, we focus on growing the earnings and cash flow from our businesses. We believe that the scale and scope of our businesses give us a diverse base of cash flow upon which to further build. Second, we identify, perform due diligence on, negotiate and consummate additional platform acquisitions of small to middle market businesses in attractive industry sectors in accordance with acquisition criteria established by the board of directors

Management Strategy

Our management strategy involves the proactive financial and operational management of the businesses we own in order to pay distributions to our shareholders and increase shareholder value. Our Manager oversees and supports the management teams of each of our businesses by, among other things:

- recruiting and retaining talented managers to operate our businesses using structured incentive compensation programs, including minority equity ownership, tailored to each business;
- regularly monitoring financial and operational performance, instilling consistent financial discipline, and supporting management in the development and implementation of information systems to effectively achieve these goals;
- assisting management in their analysis and pursuit of prudent organic growth strategies;
- identifying and working with management to execute attractive external growth and acquisition opportunities;
- assist management in controlling and right-sizing overhead costs, particularly in the current challenging economic environment; and
- forming strong subsidiary level boards of directors to supplement management in their development and implementation of strategic goals and objectives.

Specifically, while our businesses have different growth opportunities and potential rates of growth, we expect our Manager to work with the management teams of each of our businesses to increase the value of, and cash generated by, each business through various initiatives, including:

- making selective capital investments to expand geographic reach, increase capacity, or reduce manufacturing costs of our businesses;
- investing in product research and development for new products, processes or services for customers;
- improving and expanding existing sales and marketing programs;
- pursuing reductions in operating costs through improved operational efficiency or outsourcing of certain processes and products; and

- consolidating or improving management of certain overhead functions.

In terms of the difficult economic environment we are currently facing, we and each of our subsidiary management teams have been, and will continue to be, intensely focused on performance and cost control measures through this economic cycle.

Our businesses typically acquire and integrate complementary businesses. We believe that complementary acquisitions will improve our overall financial and operational performance by allowing us to:

- leverage manufacturing and distribution operations;

- leverage branding and marketing programs, as well as customer relationships;
- add experienced management or management expertise;
- increase market share and penetrate new markets; and
- realize cost synergies by allocating the corporate overhead expenses of our businesses across a larger number of businesses and by implementing and coordinating improved management practices.

We incur third party debt financing almost entirely at the Company level, which we use, in combination with our equity capital, to provide debt financing to each of our businesses and to acquire additional businesses We believe this financing structure is beneficial to the financial and operational activities of each of our businesses by aligning our interests as both equity holders of, and lenders to, our businesses, in a manner that we believe is more efficient than our businesses borrowing from third-party lenders.

Acquisition Strategy

Our acquisition strategy involves the acquisition of businesses that we expect to produce stable and growing earnings and cash flow. In this respect, we expect to make acquisitions in industries other than those in which our businesses currently operate if we believe an acquisition presents an attractive opportunity. We believe that attractive opportunities will continue to present themselves, as private sector owners seek to monetize their interests in longstanding and privately-held businesses and large corporate parents seek to dispose of their non-core operations.

Our ideal acquisition candidate has the following characteristics:

- is an established North American based company;
- maintains a significant market share in defensible industry niche (i.e., has a reason to exist);
- has a solid and proven management team with meaningful incentives;
- has low technological and/or product obsolescence risk; and
- maintains a diversified customer and supplier base.

We benefit from our Manager s ability to identify potential diverse acquisition opportunities in a variety of industries. In addition, we rely upon our management team s experience and expertise in researching and valuing prospective target businesses, as well as negotiating the ultimate acquisition of such target businesses. In particular, because there may be a lack of information available about these target businesses, which may make it more difficult to understand or appropriately value such target businesses, on our behalf, our Manager:

- engages in a substantial level of internal and third-party due diligence;
- critically evaluates the management team;

identifies and assesses any financial and operational strengths and weaknesses of the target business;

analyzes comparable businesses to assess financial and operational performances relative to industry competitors;

actively researches and evaluates information on the relevant industry; and

thoroughly negotiates appropriate terms and conditions of any acquisition.

The process of acquiring new businesses is both time-consuming and complex. Our management team historically has taken from two to twenty-four months to perform due diligence, negotiate and close acquisitions. Although our management team is always at various stages of evaluating several transactions at any given time, there may be periods of time during which our management team does not recommend any new acquisitions to us. Even if an acquisition is recommended by our management team, our board of director s may not approve it.

Upon acquisition of a new business, we rely on our manager s experience and expertise to work efficiently and effectively with the management of the new business to jointly develop and execute a successful business plan.

We believe, due to our financing structure, in which both equity and debt capital are raised at the Company level, allowing us to acquire businesses without transaction specific financing is conducive to our ability to consummate transactions that may be attractive in both the short- and long-term.

In addition to acquiring businesses, we sell businesses that we own from time to time when attractive opportunities arise that outweigh the value that we believe we will be able to bring such businesses consistent with our long-term investment strategy. As such, our decision to sell a business is based on our belief that doing so will increase shareholder value to a greater extent than through our continued ownership of that business. Upon the sale of a business, we may use the proceeds to retire debt or retain proceeds for acquisitions or general corporate purposes. We do not expect to make special distributions at the time of a sale of one of our businesses; instead, we expect to pay shareholder distributions over time through the earnings and cash flows of our businesses.

Since our inception in May 2006, we have recorded gains on sales of our businesses of approximately $198 million. We sold Crosman in January 2007, Aeroglide and Silvue in June 2008, Staffmark in 2011 and HALO in 2012. We sold Crosman, our majority owned recreational products company for approximately $143 million and our net proceeds and gain on sale were approximately $110 million and $36 million, respectively. We sold Aeroglide, our majority owned designer and manufacturer of industrial drying and cooling equipment for approximately $95 million and our net proceeds and gain on sale were approximately $78 million and $34 million, respectively. We sold Silvue, our majority owned developer and producer of proprietary, high performance liquid coating systems for approximately $95 million and our net proceeds and gain on sale were approximately $64 million and $39 million, respectively. We sold Staffmark, our majority-owned provider of temporary staffing solutions subsidiary for approximately $295 million and our net proceeds and gain on sale were approximately $217 million and $89 million, respectively We sold HALO, our majority owned fulfillment provider of promotional items for $76.5 million and our net proceeds upon sale were approximately $66.0 million and our loss on sale was approximately $0.5 million.

Strategic Advantages

Based on the experience of our management team and its ability to identify and negotiate acquisitions, we believe we are well-positioned to acquire additional businesses. Our management team has strong relationships with business brokers, investment and commercial bankers, accountants, attorneys and other potential sources of acquisition opportunities. In addition, our management team also has a successful track record of acquiring and managing small to middle market businesses in various industries. In negotiating these acquisitions, we believe our management team has been able to successfully navigate complex situations surrounding acquisitions, including corporate spin-offs, transitions of family-owned businesses, management buy-outs and reorganizations.

Our management team has a large network of approximately 2,000 deal intermediaries who we expect to expose us to potential acquisitions. Through this network, as well as our management team s proprietary transaction sourcing efforts, we have a substantial pipeline of potential acquisition targets. Our management team also has a well-established network of contacts, including professional managers, attorneys, accountants and other third-party consultants and advisors, who may be available to assist us in the performance of due diligence and the negotiation of acquisitions, as well as the management and operation of our acquired businesses.

Finally, because we intend to fund acquisitions through the utilization of our Revolving Credit Facility, we expect to minimize the delays and closing conditions typically associated with transaction specific financing, as is typically the case in such acquisitions. We believe this advantage can be a powerful one, especially in a tight credit environment, and is highly unusual in the marketplace for acquisitions in which we operate.

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Valuation and Due Diligence

When evaluating businesses or assets for acquisition, our management team performs a rigorous due diligence and financial evaluation process. In doing so, we evaluate the operations of the target business as well as the outlook for the industry in which the target business operates. While valuation of a business is, by definition, a subjective process, we define valuations under a variety of analyses, including:

- discounted cash flow analyses;
- evaluation of trading values of comparable companies;
- expected value matrices; and
- examination of recent transactions.

One outcome of this process is a projection of the expected cash flows from the target business. A further outcome is an understanding of the types and levels of risk associated with those projections. While future performance and projections are always uncertain, we believe that with detailed due diligence, future cash flows will be better estimated and the prospects for operating the business in the future better evaluated. To assist us in identifying material risks and validating key assumptions in our financial and operational analysis, in addition to our own analysis, we engage third-party experts to review key risk areas, including legal, tax, regulatory, accounting, insurance and environmental. We also engage technical, operational or industry consultants, as necessary.

A further critical component of the evaluation of potential target businesses is the assessment of the capability of the existing management team, including recent performance, expertise, experience, culture and incentives to perform. Where necessary, and consistent with our management strategy, we actively seek to augment, supplement or replace existing members of management who we believe are not likely to execute our business plan for the target business. Similarly, we analyze and evaluate the financial and operational information systems of target businesses and, where necessary, we enhance and improve those existing systems that are deemed to be inadequate or insufficient to support our business plan for the target business.

Financing

We have a Credit Facility with a group of lenders led by TD Securities that we entered into on October 27, 2011 and amended on April 2, 2012. The Credit Facility provides for a Revolving Credit Facility totaling $290.0 million, subject to borrowing base restrictions, and a Term Loan Facility totaling $255 million. The Term Loan Facility requires quarterly payments of $0.6 million, with a final payment of the outstanding principal balance on October 27, 2017. The Revolving Credit Facility matures on October 27, 2016.

The Credit Facility provides for letters of credit under the Revolving Credit Facility in an aggregate face amount not to exceed $100 million outstanding at any time. At no time may the (i) aggregate principal amount of all amounts outstanding under the Revolving Credit Facility, plus (ii) the aggregate amount of all outstanding letters of credit, exceed the borrowing availability under the Credit Facility. At December 31, 2012, we had outstanding letters of credit totaling approximately $1.8 million. The borrowing availability under the Revolving Credit Facility at December 31, 2012 was approximately $264.2 million.

The Credit Facility is secured by all of the assets of the Company, including all of its equity interests in, and loans to, its subsidiaries. (See Note I to the consolidated financial statements for more detail regarding our Credit Facility).

We intend to finance future acquisitions through our Revolving Credit Facility, cash on hand and, if necessary, additional equity and debt financings. We believe, and it has been our experience, that having the ability to finance our acquisitions with the capital resources raised by us, rather than negotiating separate third party financing specifically related to the acquisition of individual businesses, provides us with an advantage in acquiring attractive

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businesses by minimizing delay and closing conditions that are often related to acquisition-specific financings. In this respect, we believe that in the future, we may need to pursue additional debt or equity financings, or offer equity in Holdings or target businesses to the sellers of such target businesses, in order to fund multiple future acquisitions.

Our Businesses

Advanced Circuits

Overview

Advanced Circuits, headquartered in Aurora, Colorado, is a provider of prototype, quick-turn and production rigid PCBs, throughout the United States. Advanced Circuits also provides its customers with assembly services in order to meet its customers complete PCB needs. The prototype and quick-turn portions of the PCB industry are characterized by customers requiring high levels of responsiveness, technical support and timely delivery. Due to the critical roles that PCBs play in the research and development process of electronics, customers often place more emphasis on the turnaround time and quality of a customized PCB than on the price. Advanced Circuits meets this market need by manufacturing and delivering custom PCBs in as little as 24 hours, providing customers with over 98% error-free production and real-time customer service and product tracking 24 hours per day. In each of the years 2012, 2011 and 2010, approximately 60%, 63% and 64% of Advanced Circuits sales were derived from highly profitable prototype and quick-turn production PCBs. Advanced Circuits success is demonstrated by its broad base of over 11,000 customers with which it does business throughout the year. These customers represent numerous end markets, and for each of the years ended December 31, 2012, 2011 and 2010, no single customer accounted for more than 2% of net sales. Advanced Circuits senior management, collectively, has approximately 90 years of experience in the electronic components manufacturing industry and closely related industries.

For the full fiscal years ended December 31, 2012, 2011 and 2010, Advanced Circuits had net sales of approximately $84.1 million, $78.5 million and $74.5 million, respectively and operating income of $24.0 million, $26.6 million and $20.4 million, respectively. Advanced Circuits had total assets of $91.4 million, $88.7 million and $92.0 million at December 31, 2012, 2011 and 2010, respectively. Net sales from Advanced Circuits represented 9.5%, 12.9%, and 14.8% of our consolidated net sales for the years 2012, 2011 and 2010, respectively.

History of Advanced Circuits

Advanced Circuits commenced operations in 1989 through the acquisition of the assets of a small Denver based PCB manufacturer, Seiko Circuits. During its first years of operations, Advanced Circuits focused exclusively on manufacturing high volume, production run PCBs with a small group of proportionately large customers. In 1992, after the loss of a significant customer, Advanced Circuits made a strategic shift to limit its dependence on any one customer. As a result, Advanced Circuits began focusing on developing a diverse customer base, and in particular, on providing research and development professionals at equipment manufacturers and academic institutions with low volume, customized prototype and quick-turn PCBs.

In 1997, Advanced Circuits increased its capacity and consolidated its facilities into its current headquarters in Aurora, Colorado. In 2003, to support its growth, Advanced Circuits expanded its PCB manufacturing facility by approximately 37,000 square feet or approximately 150%.

In March 2010, Advanced Circuits acquired Circuit Express, Inc. (CEI) for approximately $16.1 million. Based in Tempe, Arizona and founded in 1987, CEI focuses on quick-turn and prototype manufacturing of rigid PCBs primarily for the aerospace and defense related industry customers. CEI also specializes in expedited delivery in as fast as 24 hours. CEI reported net sales of approximately $16.4 million in 2010 and $18.7 million for the full fiscal 2011 year.

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On May 23, 2012, Advanced Circuits acquired Universal Circuits for approximately $2.3 million. Universal Circuits supplies PCBs to major military, aerospace, and medical original equipment manufacturers and contract manufacturers. UCI s Minnesota facility meets certain Department of Defense clearance requirements and is noted for custom and advanced technologies. Universal Circuits sales are primarily in the long-lead sector.

We purchased a controlling interest in Advanced Circuits on May 16, 2006.

Industry

The PCB industry, which consists of both large global PCB manufacturers and small regional PCB manufacturers, is a vital component to all electronic equipment supply chains, as PCBs serve as the foundation for virtually all electronic products, including cellular telephones, appliances, personal computers, routers, switches and network servers. PCBs are used by manufacturers of these types of electronic products, as well as by persons and teams engaged in research and development of new types of equipment and technologies.

In contrast to global trends, however, production of PCBs in North America has declined since 2000 and is expected to grow slightly over the next several years according to the IPC 2010 Analysis. The rapid decline in United States production was caused by (i) reduced demand for and spending on PCBs following the technology and telecom industry decline in early 2000; and (ii) increased competition for volume production of PCBs from Asian competitors benefiting from both lower labor costs and less restrictive waste and environmental regulations. While Asian manufacturers have made large market share gains in the PCB industry overall, prototype and quick-turn production, some of the more complex volume production and military production have remained strong in the United States.

Both globally and domestically, the PCB market can be separated into three categories based on required lead time and order volume:

Prototype PCBs These PCBs are typically manufactured for customers in research and development departments of original equipment manufacturers, or OEMs, and academic institutions. Prototype PCBs are manufactured to the specifications of the customer, within certain manufacturing guidelines designed to increase speed and reduce production costs. Prototyping is a critical stage in the research and development of new products. These prototypes are used in the design and launch of new electronic equipment and are typically ordered in volumes of 1 to 50 PCBs. Because the prototype is used primarily in the research and development phase of a new electronic product, the life cycle is relatively short and requires accelerated delivery time frames of usually less than five days and very high, error-free quality. Order, production and delivery time, as well as responsiveness with respect to each, are key factors for customers as PCBs are indispensable to their research and development activities.

Quick-Turn Production PCBs These PCBs are used for intermediate stages of testing for new products prior to full scale production. After a new product has successfully completed the prototype phase, customers undergo test marketing and other technical testing. This stage requires production of larger quantities of PCBs in a short period of time, generally 10 days or less, while it does not yet require high production volumes. This transition stage between low-volume prototype production and volume production is known as quick-turn production. Manufacturing specifications conform strictly to end product requirements and order quantities are typically in volumes of 10 to 500. Similar to prototype PCBs, response time remains crucial as the delivery of quick-turn PCBs can be a gating item in the development of electronic products. Orders for quick-turn production PCBs conform specifically to the customer s exact end product requirements.

Volume Production PCBs These PCBs, which we sometimes refer to as long lead and sub-contract are used in the full scale production of electronic equipment and specifications conform strictly to end product requirements. Volume Production PCBs are ordered in large quantities, usually over 100 units, and response time is less important, ranging between 15 days to 10 weeks or more.

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These categories can be further distinguished based on board complexity, with each portion facing different competitive threats. Advanced Circuits competes largely in the prototype and quick-turn production portions of the North American market, which have not been significantly impacted by the Asian based manufacturers due to the quick response time required for these products. Management believes the North American PCB market is estimated to be approximately $3.5 billion in 2012.

Several significant trends are present within the PCB manufacturing industry, including:

Increasing Customer Demand for Quick-Turn Production Services Rapid advances in technology are significantly shortening product life-cycles and placing increased pressure on OEMs to develop new products in shorter periods of time. In response to these pressures, OEMs invest heavily in research and development, which results in a demand for PCB companies that can offer engineering support and quick-turn production services to minimize the product development process.

Increasing Complexity of Electronic Equipment OEMs are continually designing more complex and higher performance electronic equipment, requiring sophisticated PCBs. To satisfy the demand for more advanced electronic products, PCBs are produced using exotic materials and increasingly have higher layer counts and greater component densities. Maintaining the production infrastructure necessary to manufacture PCBs of increasing complexity often requires significant capital expenditures and has acted to reduce the competitiveness of local and regional PCB manufacturers lacking the scale to make such investments.

Shifting of High Volume Production to Asia Asian based manufacturers of PCBs are capitalizing on their lower labor costs and are increasing their market share of volume production of PCBs used, for example, in high-volume consumer electronics applications, such as personal computers and cell phones. Asian based manufacturers have been generally unable to meet the lead time requirements for prototype or quick-turn PCB production or the volume production of the most complex PCBs. This off shoring of high-volume production orders has placed increased pricing pressure and margin compression on many small domestic manufacturers that are no longer operating at full capacity. Many of these small producers are choosing to cease operations, rather than operate at a loss, as their scale, plant design and customer relationships do not allow them to focus profitably on the prototype and quick-turn sectors of the market.

Products and Services

A PCB is comprised of layers of laminate and contains patterns of electrical circuitry to connect electronic components. Advanced Circuits typically manufactures 2 to 20 layer PCBs, and has the capability to manufacture up even higher layer PCBs. The level of PCB complexity is determined by several characteristics, including size, layer count, density (line width and spacing), materials and functionality. Beyond complexity, a PCB s unit cost is determined by the quantity of identical units ordered, as engineering and production setup costs per unit decrease with order volume, and required production time, as longer times often allow increased efficiencies and better production management. Advanced Circuits primarily manufactures lower complexity PCBs.

To manufacture PCBs, Advanced Circuits generally receives circuit designs from its customers in the form of computer data files emailed to one of its sales representatives or uploaded on its interactive website. These files are then reviewed to ensure data accuracy and product manufacturability. While processing these computer files, Advanced Circuits generates images of the circuit patterns that are then physically developed on individual layers, using advanced photographic processes. Through a variety of plating and etching processes, conductive materials are selectively added and removed to form horizontal layers of thin circuits, called traces, which are separated by insulating material. A finished multilayer PCB laminates together a number of layers of circuitry. Vertical connections between layers are achieved by metallic plating through small holes, called vias. Vias are made by highly specialized drilling equipment capable of achieving extremely fine tolerances with high accuracy.

Advanced Circuits assists its customers throughout the life-cycle of their products, from product conception through volume production. Advanced Circuits works closely with customers throughout each phase of the PCB development process, beginning with the PCB design verification stage using its unique online FreeDFM.com tool, FreeDFM.com™, which was launched in 2002, enables customers to receive a free manufacturability assessment

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report within minutes, resolving design problems that would prohibit manufacturability before the order process is completed and manufacturing begins. The combination of Advanced Circuits user-friendly website and its design verification tool reduces the amount of human labor involved in the manufacture of each order as PCBs move from Advanced Circuits website directly to its computer numerical control, or CNC, machines for production, saving Advanced Circuits and customers cost and time. As a result of its ability to rapidly and reliably respond to the critical customer requirements, Advanced Circuits generally receives a premium for their prototype and quick-turn PCBs as compared to volume production PCBs.

Advanced Circuits manufactures all high margin prototypes and quick-turn orders internally but often utilizes external partners to manufacture production orders that do not fit within its capabilities or capacity constraints at a given time. As a result, Advanced Circuits constantly adjusts the portion of volume production PCBs produced internally to both maximize profitability and ensure that internal capacity is fully utilized.

The following table shows Advanced Circuits gross revenue by products and services for the periods indicated:

Gross Sales by Products and Services[1]

	Year Ended December 31,		
	2012	**2011**	**2010**
Prototype Production	28.4%	29.3%	28.9%
Quick-Turn Production	31.9%	33.6%	32.6%
Volume Production (including assembly)	38.1%	35.5%	36.1%
Third Party	1.6%	1.6%	2.4%
Total	100.0%	100.0%	100.0%

(1) As a percentage of gross sales, exclusive of sale discounts.

Competitive Strengths

Advanced Circuits has established itself as a leading provider of prototype and quick-turn PCBs in North America and focuses on satisfying customer demand for on-time delivery of high-quality PCBs. Advanced Circuits management believes the following factors differentiate it from many industry competitors:

Numerous Unique Orders Per Day For the year ended December 31, 2012, Advanced Circuits received on average approximately 300 customer orders per day. Due to the large quantity of orders received, Advanced Circuits is able to combine multiple orders in a single panel design prior to production. Through this process, Advanced Circuits is able to reduce the number of costly, labor intensive equipment set-ups required to complete several manufacturing orders. As labor represents the single largest cost of production, management believes this capability gives Advanced Circuits a unique advantage over other industry participants. Advanced Circuits maintains proprietary software that maximizes the number of units placed on any one panel design. A single panel set-up typically accommodates 1 to 12 orders. Further, as a critical mass of like orders is required to maximize the efficiency of this process, management believes Advanced Circuits is uniquely positioned as a low cost manufacturer of prototype and quick-turn PCBs.

Diverse Customer Base Advanced Circuits possesses a customer base with little industry or customer concentration exposure. During fiscal year ended December 31, 2012, Advanced Circuits did business with over 11,000 customers and added over 170 new customers per month. For each of the years ended December 31, 2012, 2011 and 2010, no customer represented over 2% of net sales.

Highly Responsive Culture and Organization A key strength of Advanced Circuits is its ability to quickly respond to customer orders and complete the production process. In contrast to many competitors that require a day or more to offer price quotes on prototype or quick-turn production, Advanced Circuits offers its customers quotes within seconds and the ability to place or track orders any time of day. In addition, Advanced Circuits production facility operates three shifts per day and is able to ship a customer s product within 24 hours of receiving its order.

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Proprietary FreeDFM.com Software Advanced Circuits offers its customers unique design verification services through its online FreeDFM.com tool. This tool, which was launched in 2002, enables customers to receive a free manufacturability assessment report, within minutes, resolving design problems before customers place their orders. The service is relied upon by many of Advanced Circuits customers to reduce design errors and minimize production costs. Beyond improved customer service, FreeDFM.com has the added benefit of improving the efficiency of Advanced Circuits engineers, as many routine design problems, which typically require an engineer s time and attention to identify, are identified and sent back to customers automatically.

Established Partner Network Advanced Circuits has established third party production relationships with PCB manufacturers in North America and Asia. Through these relationships, Advanced Circuits is able to offer its customers a complete suite of products including those outside of its core production capabilities. Additionally, these relationships allow Advanced Circuits to outsource orders for volume production and focus internal capacity on higher margin, short lead time, production and quick-turn manufacturing.

Business Strategies

Advanced Circuits management is focused on strategies to increase market share and further improve operating efficiencies. The following is a discussion of these strategies:

Increase Portion of Revenue from Prototype and Quick-Turn Production Advanced Circuits management believes it can grow revenues and cash flow by continuing to leverage its core prototype and quick-turn capabilities. Over its history, Advanced Circuits has developed a suite of capabilities that management believes allow it to offer a combination of price and customer service unequaled in the market. Advanced Circuits intends to leverage this factor, as well as its core skill set, to increase net sales derived from higher margin prototype and quick-turn production PCBs. In this respect, marketing and advertising efforts focus on attracting and acquiring customers that are likely to require these premium services. And while production composition may shift, growth in these products and services is not expected to come at the expense of declining sales in volume production PCBs, as Advanced Circuits intends to leverage its extensive network of third-party manufacturing partners to continue to meet customers demand for these services.

Acquire Customers from Local and Regional Competitors Advanced Circuits management believes the majority of its competition for prototype and quick-turn PCB orders comes from smaller scale local and regional PCB manufacturers. As an early mover in the prototype and quick-turn sector of the PCB market, Advanced Circuits has been able to grow faster and achieve greater production efficiencies than many industry participants. Management believes Advanced Circuits can continue to use these advantages to gain market share. Further, Advanced Circuits continues to enter into prototype and quick-turn manufacturing relationships with several subscale local and regional PCB manufacturers. Management believes that while many of these manufacturers maintain strong, longstanding customer relationships, they are unable to produce PCBs with short turn-around times at competitive prices. As a result, Advanced Circuits sees an opportunity for growth by providing production support to these manufacturers or direct support to the customers of these manufacturers, whereby the manufacturers act more as a broker for the relationship.

Remain Committed to Customers and Employees Advanced Circuits has remained focused on providing the highest quality products and services to its customers. We believe this focus has allowed Advanced Circuits to achieve its outstanding delivery and quality record. Advanced Circuits management believes this reputation is a key competitive differentiator and is focused on maintaining and building upon it. Similarly, management believes its committed base of employees is a key differentiating factor. Advanced Circuits currently has a profit sharing program and tri-annual bonuses for all of its employees. Management also occasionally sets additional performance targets for individuals and departments and establishes rewards, such as lunch celebrations or paid vacations, if these goals are met. Management believes that Advanced Circuits emphasis on sharing rewards and creating a positive work environment has led to increased loyalty. As a result, Advanced Circuits plans on continuing to focus on similar programs to maintain this competitive advantage.

Research and Development

Advanced Circuits engages in continual research and development activities in the ordinary course of business to update or strengthen its order processing, production and delivery systems. By engaging in these activities, Advanced Circuits expects to maintain and build upon the competitive strengths from which it benefits currently. Research and development expenses were not material in each of the years 2012, 2011 and 2010.

Customers

Advanced Circuits focus on customer service and product quality has resulted in a broad base of customers in a variety of end markets, including industrial, consumer, telecommunications, aerospace/defense, biotechnology and electronics manufacturing. These customers range in size from large, blue-chip manufacturers to small, not-for-profit university engineering departments. The following table sets forth management s estimate of Advanced Circuits approximate customer breakdown by industry sector for the fiscal years ended December 31, 2012, 2011 and 2010:

Industry Sector	2012 Customer Distribution	2011 Customer Distribution	2010 Customer Distribution
Electrical Equipment and Components	28%	30%	29%
Measuring Instruments	8%	8%	10%
Electronics Manufacturing Services	20%	19%	18%
Engineer Services	5%	8%	10%
Industrial and Commercial Machinery	12%	10%	6%
Business Services	1%	1%	1%
Wholesale Trade-Durable Goods	1%	1%	1%
Educational Institutions	10%	8%	7%
Transportation Equipment	9%	9%	8%
All Other Sectors Combined	6%	6%	10%
Total	100%	100%	100%

Management estimates that over 90% of its orders are generated from existing customers. Moreover, approximately two-thirds of Advanced Circuits orders in each of the years 2012, 2011 and 2010 were delivered within five days (not including CEI orders.)

Sales and Marketing

Advanced Circuits has established a consumer products marketing strategy to both acquire new customers and retain existing customers. Advanced Circuits uses initiatives such as direct mail postcards, web banners, aggressive pricing specials and proactive outbound customer call programs as part of this strategy. Advanced Circuits spends approximately 1% of net sales each year on its marketing initiatives and advertising and has 57 employees dedicated to its marketing and sales efforts. These individuals are organized geographically and each is responsible for a region of North America. The sales team takes a systematic approach to placing sales calls and receiving inquiries and, on average, will place over 250 outbound sales calls and receive approximately 140 inbound phone inquiries per day. Beyond proactive customer acquisition initiatives, management believes a substantial portion of new customers are acquired through referrals from existing customers. In addition, other customers are acquired over the internet where Advanced Circuits generates over 90% of its orders from its website.

Once a new client is acquired, Advanced Circuits offers an easy to use customer-oriented website and proprietary online design and review tools to ensure high levels of retention. By maintaining contact with its customers to ensure satisfaction with each order, Advanced Circuits believes it has developed strong customer loyalty, as demonstrated by over 90% of its orders being received from existing customers. Included in each customer order is an Advanced Circuits pre-paid bounce-back card on which a customer can evaluate Advanced Circuits services and send back any comments or recommendations. Each of these cards is read by senior members of management, and Advanced Circuits adjusts its services to respond to the requests of its customer base.

Substantially all revenue is derived from sales within the United States.

Advanced Circuits, due to the volume of prototype and quick turn sales, had a negligible amount in firm backlog orders at December 31, 2012 and 2011.

Competition

There are currently an estimated 250 active domestic PCB manufacturers. Advanced Circuits competitors differ amongst its products and services.

Competitors in the prototype and quick-turn PCBs production industry include larger companies as well as small domestic manufacturers. The two largest independent domestic prototype and quick-turn PCB manufacturers in North America are TTM Technologies, Inc. and Viasystems Group, Inc. Though each of these companies produces prototype PCBs to varying degrees, in many ways they are not direct competitors with Advanced Circuits. In recent years, each of these firms has primarily focused on producing boards with greater complexity in response to the off shoring of low and medium layer count technology to Asia. Compared to Advanced Circuits, prototype and quick-turn PCB production accounts for much smaller portions of each of these firm s revenues. Further, these competitors often have much greater customer concentrations and a greater portion of sales through large electronics manufacturing services intermediaries. Beyond large, public companies, Advanced Circuits competitors include numerous small, local and regional manufacturers, often with revenues under $20 million that have long-term customer relationships and typically produce both prototype and quick-turn PCBs and production PCBs for small OEMs and EMS companies. The competitive factors in prototype and quick-turn production PCBs are response time, quality, error-free production and customer service. Competitors in the long lead-time production PCBs generally include large companies, including Asian manufacturers, where price is the key competitive factor.

New market entrants into prototype and quick-turn production PCBs confront substantial barriers including significant investments in equipment, highly skilled workforce with extensive engineering knowledge and compliance with environmental regulations. Beyond these tangible barriers, Advanced Circuits management believes that its network of customers, established over the last two decades, would be very difficult for a competitor to replicate.

Suppliers

Advanced Circuits raw materials inventory is small relative to sales and must be regularly and rapidly replenished. Advanced Circuits uses a just-in-time procurement practice to maintain raw materials inventory at low levels. Additionally, Advanced Circuits has established consignment relationships with several vendors allowing it to pay for raw materials as used. Because it provides primarily lower-volume quick-turn services, this inventory policy does not hamper its ability to complete customer orders. Raw material costs constituted approximately 20%, 17.8% and 17.9% of net sales for each of the fiscal years ended December 31, 2012, 2011 and 2010, respectively.

The primary raw materials that are used in production are core materials, such as copper clad layers of glass and chemical solutions, and copper and gold for plating operations, photographic film and carbide drill bits. Multiple suppliers and sources exist for all materials. Adequate amounts of all raw materials have been available in the past, and Advanced Circuits management believes this will continue in the foreseeable future. Advanced Circuits works closely with its suppliers to incorporate technological advances in the raw materials they purchase. Advanced Circuits does not believe that it has significant exposure to fluctuations in raw material prices. The fact that price is not the primary factor affecting the purchase decision of many of Advanced Circuits customers has allowed management to historically pass along a portion of raw material price increases to its customers. Advanced Circuits does not knowingly purchase material originating in the Democratic Republic of the Congo or adjoining countries.

Intellectual Property

Advanced Circuits seeks to protect certain proprietary technology by entering into confidentiality and non-disclosure agreements with its employees, consultants and customers, as needed, and generally limits access to and distribution of its proprietary information and processes. Advanced Circuits management does not believe that patents are critical to protecting Advanced Circuits core intellectual property, but, rather, its effective and quick execution of fabrication techniques, its website *FreeDFM.com*™ and its highly skilled workforce are the primary factors in maintaining its competitive position.

Advanced Circuits uses the following brand names: *FreeDFM.com*™, *4pcb.com*™, *4PCB.com*™, *33each.com*™, *barebonespcb.com*™ and *Advanced Circuits*™. These trade names have strong brand equity and are material to Advanced Circuits business.

Regulatory Environment

Advanced Circuits manufacturing operations and facilities are subject to evolving federal, state and local environmental and occupational health and safety laws and regulations. These include laws and regulations governing air emissions, wastewater discharge and the storage and handling of chemicals and hazardous substances. Management believes that Advanced Circuits is in compliance, in all material respects, with applicable environmental and occupational health and safety laws and regulations. New requirements, more stringent application of existing requirements, or discovery of previously unknown environmental conditions may result in material environmental expenditures in the future. Advanced Circuits has been recognized three times for exemplary environmental compliance as it was awarded the Denver Metro Wastewater Reclamation District Gold Award for the seven of the last ten years.

Employees

As of December 31, 2012, Advanced Circuits employed 517 persons. Of these employees, there were 57 in sales and marketing. None of Advanced Circuits employees are subject to collective bargaining agreements. Advanced Circuits believes its relationship with its employees is good.

American Furniture

Overview

American Furniture, headquartered in Ecru, Mississippi, is a manufacturer of upholstered furniture sold to large-scale furniture distributors and retailers. American Furniture operates almost exclusively in the promotional upholstered segment of the furniture industry which is characterized by affordable prices, standard designs and immediate availability to retail consumers. American Furniture was founded in 1998. American Furniture s products are adapted from established designs in the following categories: (i) stationary, (ii) motion, (iii) recliner and (iv) other related products including accent tables and rugs. American Furniture s products are manufactured from common components and offer proven select fabric options, providing manufacturing efficiency and resulting in limited design risk.

For the full fiscal years ended December 31, 2012, 2011 and 2010, American Furniture had net sales of approximately $91.5 million, $105.3 million and $136.9 million, respectively, and operating losses of $1.5 million, $35.2 million and $37.1 million, respectively. American Furniture had total assets of $32.3 million, $30.0 million and $78.4 million at December 31, 2012, 2011 and 2010, respectively. Net sales from American Furniture represented 10.3%, 17.4% and 27.1% of our consolidated net sales for the years ended December 31, 2012, 2011 and 2010, respectively.

History of American Furniture

American Furniture was founded in 1998 with an exclusive focus on promotional upholstered furniture, offering a unique value proposition combining consistent high-quality, attractively priced products and 48-hour quick-ship service. AFM began operations with four assembly lines housed in a 60,000 sq. ft. facility. By 2002, American Furniture had achieved revenues in excess of $120 million and grew operations into a 600,000 sq. ft. facility in Houlka, MS. In 2004, American Furniture was sold by its founder to a group of private investors who installed a new management structure and hired a new executive team and grew American Furniture s administrative infrastructure in order to build a solid foundation to support future growth. In 2005, American Furniture aggressively pursued Asian sourcing for fabrics and other assorted materials. Today American Furniture is a leading manufacturer of promotional upholstered furniture operating from an approximately 1.1 million sq. ft. manufacturing and warehouse facility.

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For the year ended December 31, 2011 net sales at American Furniture declined $31.6 million, which represents a 23% decline over 2010 sales. In addition, write downs to goodwill, other intangible assets and property, and equipment totaled $27.8 million and $38.8 million in the years 2011 and 2010, respectively. In all cases, the write downs were triggered by a significant deterioration in American Furniture s operations and profitability caused by the unprecedented drop in the promotional furniture market and demand for its product. The combination of increased unemployment, together with significant decreases in home purchases, availability of consumer credit and rising fuel costs has created the worst market for promotional furniture sales over the last two years than has been experienced over the last two decades.

During 2011, American Furniture implemented a revised standard costing system which required American Furniture to reclassify certain costs between cost of sales and selling, general and administrative expenses. The change in format consists of reclassifying the trucking fleet expenses from selling, general and administrative expenses into cost of sales, as well as re-classifying certain manufacturing related expenses included in rent, insurance, utilities and workers comp from selling, general and administrative costs to cost of sales. Management believes that the format of reporting cost of sales together with the revised standard costing system and the revaluation of standard costs allows management to react timely to changes in supply costs, product demand and overall price structure going forward, which in turn eliminated the accumulation of lower margin product and allow for more advantageous product procurement and the proper utilization of available assets. In addition, American Furniture enlisted the assistance of an outside consulting firm in 2011 to assist them in right-sizing its operations in order to operate more efficiently and respond to the significantly changed promotional furniture marketplace. To that end, American Furniture has outsourced the majority of delivery and its trucking operations as well as sub-contracted its frame cutting process during 2012.

We acquired a controlling interest in American Furniture on August 31, 2007.

Industry

AFM is a manufacturer of upholstered furniture serving the promotional segment of the U.S. furniture industry. Overall conditions for the furniture industry have been difficult over the past two years. New housing starts are down significantly and consumers continue to be faced with general economic uncertainty fueled by deteriorating consumer credit markets, rising fuel costs and lagging consumer confidence as a result of erratic financial markets. All of this has significantly impacted big ticket consumer purchases such as furniture over the last several years.

AFM participates largely in the promotional upholstered furniture industry. Within the U.S. residential retail furniture marketplace, products are typically positioned in the promotional , good , better , or best category. The scale of the categories is intended to reflect an increasing level of quality, appearance and corresponding price. At the wholesale level, the promotional segment of the upholstered furniture industry we believe accounts for over $3 billion in sales. Promotional upholstered furniture manufacturers typically offer a limited range of products in a discrete number of styles and/or designs, allowing immediate delivery to retail customers at well-established retail price points. Specifically, promotional upholstered furniture is generally priced by product at the retail level from $199 for recliners and up to $1,500 for motion sectionals.

The popularity of promotional furniture is attributable to (i) the segment s consistent product quality (based on focused manufacturing on a few key furniture pieces), and (ii) its value pricing, which appeals to the broadest cross-section of the furniture consumers.

AFM competes exclusively in the promotional segment, selling upholstered furniture in both the stationary and motion categories. In the retail furniture landscape, promotional furniture can be a growing catalyst of floor traffic and sales volumes for mass market furniture retailers. Recurring promotional programs have often become core to retailer strategies given its immediate availability to customers and just-in-time strategies employed within the industry which limit retailer inventory requirements.

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Within the wholesale market, wholesale shipments from Asian suppliers, we believe, have grown steadily as a percent of total wholesale shipments. Asian upholstered imports have grown significantly in the past ten years. We believe their impact on AFM has been far less than the industry as a whole within the promotional upholstered furniture, due to the low price points and resulting shipping costs as a percent of a piece s total value.

Off-shore Imports

Furniture manufactured in Asia emerged as an important driver of the U.S. residential furniture market beginning in the mid-1990s. While off-shore manufacturers, particularly Chinese and Vietnamese manufacturers, have affected the entire industry, the import trend, has impacted different segments of the industry at varying levels.

Case-goods and metal furniture have proven to be more susceptible to Asian competition than upholstered furniture, due to the stack ability and assembly characteristics, resulting in efficient freight consolidation. Upholstered furniture cannot be broken down and shipped efficiently to the U.S. such that the resulting freight costs tend to outweigh the labor and material savings achieved through offshore manufacturing. As a result, domestic upholstered manufacturers have largely managed to compete effectively against Asian competitors when compared to other segments of the furniture industry. In addition, manufacturers in the promotional segment of the upholstered industry are even further insulated from offshore competition due not only to overall freight costs but also freight costs when compared to wholesale price of the product together with the prolonged lead-times to retailers and end customers in a market segment characterized by very short lead-times and immediate delivery to the end consumer.

Retail price points in the promotional segment of the upholstered industry range from $199 $1,500, whereas shipping costs from Asia on a per piece basis are generally in excess of $100 per piece ($3,000 $4,000) per standard 40 foot container not including domestic shipping and insurance costs.

In addition to the increased cost, lead times also hinder Asian manufacturers ability to effectively compete in the promotional upholstered industry. As mentioned previously, retailers use promotional furniture to drive store traffic and provide immediate delivery to the end-user of value-priced, quality upholstered furniture products. AFM aims to ship customer orders 48 hours following receipt of an order with delivery occurring 1 3 days later depending on the customers location within the U.S. Asian manufacturers typically require at least 50 days (or 7 8 weeks depending on business days) from order receipt to customer delivery, resulting in a significant amount of increased inventory management and advertising planning in order to effectively source upholstered product from overseas manufacturers.

Products and Services

AFM manufactures two basic categories of promotional upholstered products, stationary and motion. Stationary products include sofas, loveseats and sectionals, these products accounted for approximately 72%, 75% and 70% of sales in fiscal 2012, 2011 and 2010, respectively. Motion products include single rocking recliner chairs, sofas with reclining end seats, loveseats with seats that rock together or separately and reclining sectionals with storage compartments. Motion and reclining products contributed approximately 27%, 23% and 25% of fiscal 2012, 2011 and 2010 gross sales, respectively. Beginning in 2005, AFM added a line of imported rugs and accent tables to its product mix to provide customers with complimentary accessory offering to AFM s core furniture lines. For 2012, 2011 and 2010, accent tables and other miscellaneous revenue accounted for less than 2% of gross sales. AFM s core product offerings with average retail prices are summarized below:

25 styles of stationary sofas, loveseats and chairs $299 $499

10 styles of recliners $199 $399

5 styles of motion sofas $499 $599

6 styles of stationary sectionals Up to $799

1 style of motion sectional $999 $1,399

AFM s products utilize common components and frames with limited fabric options, allowing AFM to reproduce established styles at value prices. Since its inception, AFM has continuously introduced new styles which typically replace older designs and are primarily slight variations to existing products. AFM builds its products to stock and maintains adequate inventory levels to facilitate shipment to customers on time. AFM s quick-ship strategy allows customers to better manage inventory and product promotions, yet maintain the ability to provide immediate availability to retail customers, a key attribute within the promotional furniture segment of the furniture industry.

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Product Development

AFM can re-engineer a new design, create a prototype and begin to solicit customer feedback within two weeks. AFM carefully controls its product line such that new styles typically replace older designs. As a result, AFM requires up to 120 days to wind-down a discontinued line and beginning shipping truckload quantities of new designs to customers.

Manufacturing

AFM utilizes an assembly-line manufacturing process with a four day production cycle divided into four functions, cutting, sewing, backfill and upholstery. Employees are specialized by function and are compensated on a piece-rate basis. The limited number of styles and designs minimizes scheduling and line changes and each function is simplified by the use of common components. AFM uses one standard seat spring, one standard back spring and one standard cushion in each category of upholstery. AFM s piece-rate compensation plan and streamlined manufacturing process combine to give AFM a low cost structure. Prior to 2009, American Furniture utilized pre-assembled cut and sewn fabric kits for approximately 20% of its upholstered furniture. These fabric kits replace the cutting and sewing function in the manufacturing process. Over the several years AFM has increased the use of these fabric kits and as of December 31, 2012 virtually all of the upholstered furniture that it manufactures used the imported cut and sewn fabric kit. The use of these fabric kits reduces the labor component related to the cutting and sewing process in-house. Theses fabric kits are imported from Asia. American Furniture also eliminated its in-house frame cutting operations in 2012 and currently 100% of the frames for upholstered furniture are cut by third party providers.

AFM currently delivers the majority of its products through third-party freight service providers. Freight costs are generally paid by the customer, including fuel surcharges. AFM utilized third-party freight providers for approximately 80% of its customer shipments in 2011 and 2010 compared to approximately 50% or lower in prior years. We estimate that this saved approximately $1.0 million in 2010 and 2011 in overall freight costs when this strategy was first instituted. American Furniture eliminated its in-house trucking operations in 2012.

Competitive Strengths

We believe that AFM is among the lowest-cost domestic manufacturers of promotional upholstered furniture. AFM maintains a competitive cost basis through an assembly-line production model and build-to-stock strategy. Specifically, AFM generates economies of scale through:

- Long runs of a limited number of standardized frames;
- The application of common components throughout the entire production line; and
- A standard offering of only two to four fabric options per frame.

In addition, management has aligned AFM s high-volume manufacturing strategy with a piece-rate incentive structure for its direct labor force. This structure drives workforce productivity. The incentive system also provides floor personnel with the opportunity to earn annual compensation at or above local standards, thereby facilitating AFM s recruiting and retention efforts.

AFM s efficient build-to-stock manufacturing operation facilitates AFM s strategy of offering its customers on time shipment of product. In turn, AFM s customers are able to offer their retail customers quality, value-priced, upholstered furniture for immediate delivery upon the day of sale, while only maintaining limited quantities of product inventory.

AFM serves a diverse base of approximately 700 customers. Within its broader customer base, AFM specifically targets independent furniture retailers at the national, multi-regional and regional levels. AFM s value proposition and the ability to ship most products within 48 hours, is highly valued by this segment of the marketplace that focuses broadly on demographic segments that demand immediate delivery of popular styles at competitive prices.

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Barriers to Significant Asian Competition

The availability of low-cost Asian products has had a far-reaching impact on the broader home furnishings market in the United States over the past ten years, contrasted to manufacturers serving other segments. Until recently, AFM has had minimal exposure to off-shore competition due to the following:

AFM s efficient, low-cost production model;

Mass retailers short lead-time demands and unwillingness to accept excess inventory risk; and

High costs (e.g., freight, damage, shrink) of shipping upholstered furniture direct from Asia.

Recently, we have begun to see more competition in the motion product category from imported Asian product. These products typically offer customers better value in terms of construction and price when compared to our motion product. Our margin for motion product has typically been less than stationary.

Business Strategies

Increase profit with new and existing customers While AFM currently supplies many of the top furniture retailers, AFM believes it can further augment its customer base and is pursuing new business opportunities with selected national and regional furniture retailers, as well as in other channels, including Rent-To-Own (RTO) and mass merchandisers. In addition, many existing customers currently purchase only a portion of AFM s product line, representing an opportunity for AFM to increase sales to existing customers by augmenting customers entire promotional product line. In order to focus additional attention to major customers and expand product line sell-through to these customers, AFM added significant infrastructure to its sales and marketing organization since 2005, increasing its sales representative network while also subdividing sales territories to allow representatives to focus more closely on the expansion of existing relationships and the addition of new customers.

Product development AFM s merchandising strategy focuses on satisfying the changing needs of retailers and consumers in a manner that meets AFM s production strategy. AFM s management and sales staff monitor the furniture market to identify new trends and popular styles at higher price points. AFM subsequently ensures that it can cost effectively replicate a new style with standardized components and limited cover options, after which AFM will build a prototype to determine if the product can be reproduced at acceptable margin levels.

Pursue cost savings initiatives Aggressively pursue expense reduction in the manufacturing process and overhead areas, cost cutting programs and cash preservation initiatives throughout all parts of its business.

Reduce the number of SKUs American Furniture manufactures a limited number of SKUs in three categories: stationary, recliners and motion. The strategy has been to continually manage the number of groups or styles in each category so that the combined active style SKU count does not exceed 500.

Revise kit purchasing American Furniture, with the help of an outside consultant, has revised the manner in which it orders fabric kits to provide a more efficient flow of kits and reduce the possibility of obsolescence. A process has been developed taking into account rate of sale, sales order rate, customer projections, current inventory levels, delivery lead times and safety stock for each individual SKU. A review is completed no less than weekly by SKU and orders are placed accordingly. Managing this process ties kit acquisition more closely to actual production needs and either increases or decreases the quantity of kits based on demand for the particular SKU.

Monetize excess stock During 2012, American Furniture aggressively moved to reduce excess levels of finished goods and raw materials. This has been done through a series of product promotions that have been successful while not impairing the sales of the current product line. The company developed a new system to monitor each category on an ongoing basis to more quickly identify potential slow-down in specific SKU activity. This process has been integrated with the kit purchasing procedure mentioned above.

Customers

AFM serves a base of approximately 700 customers comprised of retailers and distributors at the regional, multi-regional and national levels. In 2012, 2011 and 2010, AFM s top 20 customers accounted for approximately 67%, 66% and 67%, respectively, of AFM s total sales. In 2012 two customers (Value City and Big Lots) each accounted for approximately 12% of gross sales.

Sales and Marketing

AFM has a sales force consisting of independent, outside representatives that exclusively sell AFM s products in an assigned geographic territory of up to six states. Sales representatives are compensated on a 100% commission basis. AFM maintains two permanent showrooms in High Point, NC and Tupelo, MS, host cities for furniture industry trade shows (High Point in April and October and Tupelo in January and August).

American Furniture s business is seasonal. Net sales have historically been higher in the period of January through April of each fiscal year. We believe this seasonality is due in part to consumer demand increasing resulting from income tax refunds. Substantially all revenue is derived from sales within the United States.

Marketing at the retail level is typically handled by AFM s customers. AFM does not advertise specific products on its own, but provides product information and pictures for retailers to include in newspaper and various insert advertisements. AFM s products are typically included in retailers recurring promotional programs as the products drive floor traffic and sales volume due to low price points.

American Furniture had approximately $5.4 million and $8.4 million in firm backlog orders at December 31, 2012 and 2011, respectively.

Competition

AFM competes with selected large national manufacturers that produce and sell promotional products. However, promotional upholstered furniture often represents only a small percentage of revenue for these participants. Also, large diversified manufacturers tend not to place specific emphasis on developing quick-ship capabilities specifically for their promotional offerings. Therefore, AFM competes primarily with several smaller manufacturers that are typically thinly-capitalized, family owned businesses that we believe do not have the capacity, manufacturing capabilities, sourcing expertise or access to capital in order to build critical production volumes. Competition within the segment is largely based on value and delivery lead times, as opposed to product differentiation, providing AFM and its quick-ship capabilities with a key competitive advantage within the industry. AFM s primary competitors include United Furniture Industries, Albany Industries and Hughes Furniture, Ashley Furniture and Affordable Furniture.

Suppliers

AFM s top supplier, Independent Furniture Supply (Independent), was 50% owned by Mr. Thomas, AFM s former CEO. Mr. Thomas divested his interests in Independent in November 2012. AFM does not have long-term supply contracts with Independent or any other supplier. A majority of AFM s domestic suppliers are located near AFM due to a concentration of furniture manufacturers in northeastern Mississippi. Several of AFM s key raw materials, including lumber, plywood and polyfoam, are sourced locally with alternative suppliers available at competitive prices, if necessary. In order to continually manage material costs, AFM actively sources products from Asia. AFM imports legs, show wood, accent tables and the majority of its fabric from China-based suppliers. The prices charged by manufacturers of products such as petro-chemicals and wire rod, which are the primary materials purchased by our suppliers of foam and drawn wire effect the ongoing cost of our raw materials. Raw material cost as a percentage of sales was approximately 67%, 69% and 62% in 2012, 2011 and 2010, respectively.

Regulatory Environment

AFM s manufacturing operations, facilities and operations are subject to evolving federal, state and local environmental and occupational health and safety laws and regulations. Such laws and regulations govern air emissions, wastewater discharge and the storage and handling of chemicals and hazardous substances. AFM believes that it is in compliance, in all material respects, with applicable environmental and occupational health and safety laws and regulations. New requirements, more stringent application of existing requirements, or discovery of previously unknown environmental conditions could result in material environmental expenditures in the future.

Employees

As of December 31, 2012, American Furniture employed 484 persons. Of these employees, 425 were in production, shipping and purchasing with the remainder serving in executive, administrative office and other capacities. None of AFM s employees are subject to collective bargaining agreements. We believe that AFM s relationship with its employees is good.

Arnold

Overview

Founded in 1895 and now headquartered in Rochester, New York, Arnold Magnetic Technologies Corporation is a manufacturer of engineered, application specific magnet solutions. Arnold manufactures a wide range of permanent magnets and precision magnetic assemblies with facilities in the United States, the United Kingdom, Switzerland and China. Arnold has hundreds of customers in its primary markets including aerospace and defense, consumer, industrial, medical, automotive as well as oil and gas exploration. Arnold is the largest and, we believe, most technically advanced U.S. manufacturer of engineered magnets. Arnold is one of two domestic producers to design, engineer and manufacture rare earth magnetic solutions. Arnold serves customers and generates revenues via three business units:

PMAG Permanent Magnet and Assemblies Group- High performance magnets and assemblies for precision motors/generators, Hall Effect sensor and beam focusing applications. PMAG also manufactures assemblies for the reprographic industry used in printing and copying systems.

Rolled Products Ultra thin gauge metal strip and foil products utilizing magnetic and non-magnetic alloys

Flexmag Flexible bonded magnets for specialty advertising, industrial and medical applications.

Arnold operates a 70,000 sq. ft. manufacturing assembly and distribution facility in Rochester, New York with nine additional facilities worldwide in countries including the UK, Switzerland and China. The Company employs a total of approximately 750 people.

For the fiscal year ended December 31, 2012, (from date of acquisition), Arnold had net sales of approximately $104.2 million and an operating loss of $0.5 million. Arnold had total assets of $155.9 million at December 31, 2012. Net sales from Arnold (from acquisition date to December 31, 2012) represented 11.8% of our consolidated net sales.

History of Arnold

Arnold was founded in 1895 as the Arnold Electric Power Station Company. Arnold began producing AlNiCo permanent magnets in its Marengo, Illinois facility in the mid-1930s. In 1946, Allegheny Ludlum Steel Corporation (Allegheny) purchased Arnold, and over the next few years began production of several additional magnetic product lines under license agreement with the Western Electric Company. In 1970, Arnold acquired Ogallala Electronics, which manufactured high power coils and electromagnets.

SPS Technologies (SPS), at the time a publicly traded company, purchased Arnold Engineering Company from Allegheny in 1986. Under SPS, Arnold made a series of acquisitions and partnerships to expand its portfolio and geographic reach. At the end of 2003, Precision Castparts, also a publicly traded company acquired SPS. In January 2005, Audax, a Boston-based private equity firm acquired Arnold from Precision Castparts.

In February 2007, Arnold Magnetic Technologies completed the acquisition of Precision Magnetics with operations in Sheffield, England; Lupfig, Switzerland; and Wayne, New Jersey. The Wayne, New Jersey facility was relocated

to Rochester, NY later that year. In addition, Arnold s Lupfig, Switzerland operation is a joint venture partner with a Chinese rare earth producer. The joint venture manufactures RECOMA® Samarium Cobalt blocks for the Asian market.

Industry

Permanent Magnets

There exists a broad range of permanent magnets which include Rare Earth Magnets and magnets made from specialty magnetic alloys. Magnets produced from these materials may be sliced, ground, coated and magnetized to customer requirements. Those industry players with the broadest portfolio of these magnets, such as Arnold, maintain a significant competitive advantage over competitors as they are able to offer one-stop shop capabilities to customers.

Rare Earth Magnets

Samarium Cobalt (SmCo) SmCo magnets are typically used in critical applications that require corrosion resistance or high temperature stability, such as motors, generators, actuators and sensors. Arnold markets its SmCo magnets under the trade name of RECOMA ®.

Neodymium (Neo) Neo magnets offer the highest magnetic energy level of any material in the market. Applications include motors and generators, VCM s, magnetic resonance imaging, sensors and loudspeakers.

Other Permanent Magnet Types

AlNiCo The AlNiCo family of magnets remains a preferred material for many mission critical applications. Its favorable linear temperature characteristics, high magnetic flux density and good corrosion resistance are ideally suited for use in applications requiring magnetic stability.

Hard Ferrite Hard ferrite (ceramic) magnets were developed as a low cost alternative to metallic magnets (steel and AlNiCo). Although they exhibit lower energy when compared to other materials available today and are relatively brittle, ferrite magnets have gained acceptance due to their low price per magnetic output.

Injection Molded Injection molded magnets are a composite of various types of resin and magnetic powders. The physical and magnetic properties of the product depend on the raw materials, but are generally lower in magnetic strength and resemble plastics in their physical properties. However, a major benefit of the injection molding process is that magnet material can be injection or over-molded, eliminating subsequent manufacturing steps.

Magnetic Assemblies Arnold offers complex, customized value added magnetic assemblies. These assemblies are used in devices such as motors, generators, beam focusing arrays, sensors, and solenoid actuators. Magnetic assembly production capabilities include magnet fabrication, machining, encapsulation or sleeving, balancing, and field mapping.

Precision Strip and Foil

Precision rolled thin metal foil products are manufactured from a wide range of materials for use in applications such as transformers, motor laminations, honeycomb structures, shielding, and composite structures. These products are commonly found in security tags, medical implants, aerospace structures, batteries and speaker domes. Arnold has the expertise and capability to roll, anneal, slit and coat a wide range of materials to extremely thin gauges (2.5 microns) and exacting tolerances.

Flexible Magnets

Flexible magnet products span the range of applications from advertising (refrigerator magnets) to medical applications (surgical drapes) to sealing and holding applications (door gaskets).

Products and Services

PMAG

Arnold s Precision Magnets and Assemblies (PMAG) segment is a leading global manufacturer of precision magnetic assemblies and high-performance magnets. The segment s products include tight tolerance assemblies consisting of many dozens of components and employing RECOMA® SmCo, Neo, and AlNiCo magnets. These products are sold to a wide range of industries including aerospace and defense, alternative energy (hybrids/wind), automotive, medical, oil and gas, and general industrial.

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PMAG is Arnold s largest business unit representing approximately70% of Arnold sales on an annualized basis (including Reprographics) with a global footprint including manufacturing facilities in the U.S., U.K., Switzerland, and China.

PMAG Products and Applications:

High precision magnetic rotors for use in electric motors and generators. Typically used in demanding applications such as aerospace, oil and gas exploration, energy recovery systems and under the hood automotive

Sealed pump couplings

Beam focusing assemblies such as traveling wave tubes

Oil & Gas NMR tools as well as pipeline inspection and down hole power generation

Hall affect sensor systems

Arnold s reprographics unit, which is part of the PMAG segment, produces systems and components for copier systems. The business unit s state-of-the-art, high-volume precision magnetic assembly facility produces over 150,000 assemblies per year. The reprographics unit utilizes components produced by the Flexmag segment.

Reprographics products and applications:

Complex, multi-component, high-accuracy copier assemblies

Toner rolls

Toner and fuser assemblies

Rolled products

Arnold s rolled products segment manufactures precision thin strip and foil products from an array of materials and represents approximately 10% of Arnold sales on an annualized basis. The rolled products segment serve the aerospace & defense, power transmission, alternative energy (hybrids, wind, battery, solar), medical, security, and general industrial end-markets. With top-of-the-line equipment (Sendzimir mills) and superior engineering, rolled products has developed unique processing capabilities that allow it to produce foils and strip with precision and quality that are unmatched in the industry (down to 1/10th thickness of a human hair). In addition, the segment s facility is capable of increasing production from current levels with its existing equipment and is, we believe, well-positioned to realize future growth with little incremental investment required.

Rolled products Products and Applications:

Electrical steels for hybrid propulsion systems, electric motors, and micro turbines

Security and product ID tags

Honeycomb structures for aerospace applications

Irradiation windows

Batteries

Military countermeasures

Flexmag

Arnold is one of two North American manufacturers of flexible rubber magnets for specialty advertising, medical, and reprographic applications. Flexmag represents approximately 20% of Arnold sales on an annualized basis. It primarily sells its products to specialty advertisers and original equipment manufacturers. With highly automated manufacturing processes, Flexmag can accommodate customer s required short lead times. Flexmag benefits from a loyal customer base and significant barriers to entry in the industry. Flexmag s success is driven by superior customer service, and proprietary formulations offering enhanced product performance.

Flexmag products and applications:

Extruded and calendared flexible rubber magnets with optional laminated printable substrates

Retail displays

Seals and enclosures

Signage for various advertising and promotions

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Competitive Strengths

Competitive Landscape

The specialty magnets industry is highly fragmented, creating a competitive landscape with a variety of magnetic component manufacturers. However, few have the breadth of capabilities that Arnold possesses. Manufacturers compete on the basis of technical innovation, co-development capabilities, time-to-market, quality, geographic reach and total cost of ownership. Industry competitors relevant to Arnold s served markets range from large multinational manufacturers to small, regional participants. Given these dynamics, we believe the industry will likely favor players that are able to achieve vertical integration and a diversification of offerings across a breadth of products along with magnet engineering and design expertise.

Barriers to Entry

- ***Low Substitution Risk*** Arnold s solutions are typically specified into its customers program designs through a co-development and qualification process that often takes 6-18 months. Arnold s customers are typically contractors and component manufacturers whose products are integrated into end-customers applications. The high cost of failure, relatively low proportionate cost of magnets to the final product, sometimes lengthy testing and qualification process, and substantial upfront co-engineering investment required, represent significant barriers to customers changing solution providers such as Arnold.

- ***Equipment and Processing*** Arnold s existing base of production equipment has a significant estimated replacement cost. A new entrant could require as much as 2-3 years of lead time to match the process performance requirements, customization of equipment and material formulations necessary to effectively compete in the specialty magnet industry. Further, given the program nature of a majority Arnold s sales, management estimates that it could take 5-10 years to build a sufficient book of business and base of institutional knowledge to generate positive cash flow out of a new manufacturing plant.

Competition

Management believes the following companies represent Arnold s top competitors:

- Thomas & Skinner
- Magnum Magnetics
- Electron Energy
- Vacuumschmelze Gruner, Germany-based

Business Strategies

Engineering and Product Development

Arnold s engineers work closely with the customer to co-develop a product or process to provide system solutions, representing a significant competitive advantage. The Company s engineering expertise is leveraged by the state-of-the-art Technology Center working together with the various business units located in North America, Europe and Asia Pacific. This cooperative engineering effort allows Arnold to support customers and projects on a global basis. Arnold s engineers work with customers on a global basis to optimize designs, guide material choices, and create magnetic models resulting in Arnold s products being specified into customer designs.

Arnold has a talented and experienced engineering staff of design and application experts, quality personnel and technicians. Included in this team are engineers with backgrounds in materials science, physics, and metallurgical engineering. Other members of the team bring backgrounds in ceramics, mechanical engineering, chemical engineering and electrical engineering.

Arnold continues to be an industry leader with regard to new product formulations and innovations. As evidence of this, the Company currently relies on a deep portfolio of trade secrets and internal intellectual property. Arnold continuously endeavors to introduce magnet solutions that exceed the performance of current offerings and meet customer design specifications.

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Growth in Arnold s business is primarily focused in three areas:

(i) Growing market share in existing end-markets and geographies

(ii) Developing new products and technologies

(iii) Completing opportunistic acquisitions

Existing End-Markets and Geographies

Oil & Gas

Arnold currently provides magnets and precision assemblies for use in oil and gas exploration and production, applications which typically require exceptional collaboration and co-development with its customers. The Company supplies products used in applications such as a new oil well shutoff valve, a new down-hole logging while drilling tool, and a down-hole magnetic transfer coupling. Other applications for which the Company is actively involved include pipeline inspection, wireless tomography tools, and chip collection.

Power Transmission

The Company s Rolled Products segment supplies grain-oriented silicon steel produced with proprietary methods for use in transformers and inductors. These cores allow for the production of very efficient transformers and inductors while minimizing size. In addition, the Company s magnet solutions can be found in advanced automatic circuit re-closer solutions that substantially reduce the stress on system components on the grid. Arnold s solutions are also present in new power storage systems. The permanent magnet bearings used in new designs improve the efficiency of the flywheel energy storage system.

Automotive

In the automotive sector, the Company is selling magnets and magnetic assemblies primarily to Tier 1 and 2 companies. It is estimate that the current automobile contains over 50 magnetic systems, and this number is expected to grow due to vehicle electrification initiatives in order to meet increasing fuel efficiency standards. Typical applications include magnets for Hall Effect sensors that are used in braking, passenger restraint, and steering and engine control systems. Emerging magnetic applications include electric traction drives, regenerative braking systems, starter generators, and electric turbo charging. The auto industry continues to adopt increasingly sophisticated technology to reduce vehicle weight and improve fuel efficiency. As much of this technology utilizes magnetic systems, the Company expects to benefit from this trend.

Aerospace and Defense

In the aerospace and defense sector, the Company is selling magnets, magnetic assemblies and ultra-thin foil solutions. Specifically, in the aerospace industry, Arnold s assemblies have been designed into products, which enables the Company to benefit from the market growth and a healthy flow of business based on current airframe orders. Through its OEM customers, essentially all new commercial aircraft placed in service contain assemblies produced by Arnold. Arnold s sales to large aerospace and defense manufactures includes magnetic assemblies used in applications such as motors and generators, actuators, trigger mechanisms, and guidance systems, as well as magnets for these and other uses. In addition it sells its ultra-thin foil for use in military countermeasures, honeycomb structures, brazing alloys, and motor laminations.

General Industrial

Within the industrial sector Arnold provides magnet assemblies as well as magnets for custom made motor systems. These include stepper motors, pick and place robotic systems, and new designs that are increasingly being required by regulation to meet energy efficiency standards. An example is a motor utilizing Arnold s bonded magnets for use in commercial refrigeration systems. Arnold also produces magnetic couplings for seal-less pumps used in chemical and oil & gas applications that allow chemical companies to meet environmental requirements.

Medical

Within the medical sector, Arnold provides magnetic assemblies, magnets, flexible magnets, and ultrathin foils. Its magnet assemblies and magnets are critical parts of motor systems for dental instruments as well as saws and grinders. Magnet assemblies are also provided for skin expansion systems, shunt valves, and position sensors. In addition, its Rolled Products business unit is providing a specialty alloy for advanced breast cancer treatment.

New Products & Technologies

Flexcoat EZ (Flexmag)

Flexcoat EZ is a patent pending technology launched in April 2010. The product was engineered to eliminate the issues associated with the conventional flexible magnetic product laminated with a printable surface. The solution is a printable coating that is applied to the magnet, which replaces substrates such as vinyl and paper that are currently adhered to the base magnet material. This results in a printed magnet that is now completely recyclable and is easier to process.

Research and Development

Arnold has a core research and development team, which has collectively over 30 years of combined industry experience. In addition to the core engineering group, a large number of other Arnold staff members assigned to the business units contribute to the research and development effort at various stages. Product development also includes collaborating with customers and field testing. This feedback helps ensure products will meet the company s demanding standards of excellence as well as the constantly changing needs of end users. Arnold s research and development activities are supported by state-of-the-art engineering software design tools, integrated manufacturing facilities and a performance testing center equipped to ensure product safety, durability and superior performance.

Customers

Arnold s focus on customer service and product quality has resulted in a broad base of customers in a variety of end markets. Products are used in applications such as general industrial, reprographic systems, aerospace & defense, advertising and promotion, consumer and appliance, energy, automotive and medical.

The following table sets forth management s estimate of Arnold s approximate customer breakdown by industry sector for the fiscal year ended December 31, 2012 and 2011:

Industry Sector	2012 Customer Distribution	2011 Customer Distribution
General industrial	30%	25%
Aerospace and defense	15%	15%
Advertising and promotion	12%	14%
Consumer and appliance	5%	5%
Energy	7%	5%
Automotive	4%	4%
Medical	3%	4%
Reprographic	21%	26%
All Other Sectors Combined	3%	2%
Total	100%	100%

Arnold has a large and diverse, blue-chip customer base. With the exception of Xerox, no other customer represents greater that 10% of the company s annual revenue. Sales to Arnold s top ten customers were 31%, 35% and 38% of total sales for the date of acquisition through December 31, 2012 and the years ended December 31, 2011 and 2010, respectively.

Sales and Marketing

PMAG Arnold s PMAG segment supports a global team of direct sales and marketing professionals and critical design and application engineers. The PMAG sales force is organized for regional coverage with a focus on sales in U.S., Europe, and South East Asia. Arnold serves over 500 active customers globally. As the majority of revenues are project based in the PMAG business unit, technical sales are critical to the segment s success. Arnold s highly-qualified

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application engineers are often integrated into its customers   product design, planning, and implementation phases, offering the most cost effective solution for demanding clients. The resulting intimate customer relationships yield a high close rate, with revenue achieved primarily after the prototype phase.

Rolled Products   Similar to the Company   s PMAG segment, the vast majority of Rolled Products   sales are technically driven engineered solutions. These teams communicate closely in order to take advantage of potential cross-selling opportunities. Approximately 75% of sales are domestic, with the balance of sales to Western Europe.

Flexmag Products   The Flexmag business segment services over 300 customers globally. Its sales force is comprised of seven total sales professionals and supported by seven design and application engineers. This segment is primarily book/bill and has limited revenue subject to long-term purchase commitments.

The following table sets forth Arnold   s net sales by geographic location for the fiscal years ended December 31, 2012 and 2011:

Geographic location	**2012**	**2011**
North America	56%	55%
Europe	34%	35%
Asia Pacific	8%	8%
All Other Locations Combined	2%	2%
Total	100%	100%

Arnold had firm backlog orders totaling $35 million at December 31, 2012.

Suppliers

Raw materials utilized by the Company include nickel and cobalt, stainless steel shafts, Inconel sleeves, adhesives, laminates, aluminum extrusions and binders. Although the Company considers its relationships with vendors to be strong, Arnold   s management team also maintains a variety of alternative sources of comparable quality, quantity and price. The management team therefore believes that it is not dependent upon any single vendor to meet its sourcing needs. Arnold is generally able to pass through material costs to its customers and believes that in the event of significant price increases by vendors that it could pass the increases to its customers.

Intellectual Property

The Company currently relies on a deep portfolio of   trade secrets   and internal intellectual property.

Patents

Arnold currently has thirteen patents and one in process; over half of the patents were granted in the U.S. with the remaining patents granted in European countries such as Germany, Great Britain, France and the Netherlands. Ten of the patents are related to methods of making magnetic strips. In 2004, the company was granted a patent related to a thermally-stable, high-temperature, SmCo molding compound. The most recent pending patents are related to the methods of production involving flexible magnets having a printable surface as well as shaped field magnets

Trademarks

Arnold currently has 86 trademarks, 12 of which are in the U.S. The most notable trademarked items are the following: RECOMA ,   PLASTIFORM ,   FLEXMAG   &   ARNOLD . Application dates for various trademarks date back to as early as 1961.

Regulatory Environment

Arnold s domestic manufacturing and assembly operations and its facilities are subject to evolving Federal, state and local environmental and occupational health and safety laws and regulations. These include laws and regulations governing air emissions, wastewater discharge and the storage and handling of chemicals and hazardous substances. Arnold s foreign manufacturing and assembly operations are also subject to local environmental and occupational health and safety laws and regulations. Management believes that Arnold is in compliance, in all material respects, with applicable environmental and occupational health and safety laws and regulations. New requirements, more stringent application of existing requirements, or discovery of previously unknown environmental conditions could result in material environmental expenditures in the future.

Arnold is a major producer of both Samarium Cobalt permanent magnets under its brand name RECOMA® and Alnico (in both cast and sintered forms). Both materials from Arnold meet the current Berry Amendment or Defense Acquisition Regulations Systems (DFARS) requirements per clauses 252.225.7014 252.225.7014 further described under 10 U.S.C. 2533b. This provision covers the protection of strategic materials critical to national security. These magnet types are considered specialty metals under these regulations.

Employees

Arnold is led by a capable management team of industry veterans that possess a balanced combination of industry experience and operational expertise. The current senior management team has approximately 100 years of cumulative experience with an average tenure of approximately 16 years at Arnold. Current management has implemented numerous operational, strategic, and financial initiatives over the past several years, including almost 100 unique lean initiatives and kaizen events.

Arnold employs approximately 750 hourly and salaried employees located throughout North America, Europe and Asia. Arnold s employees are compensated at levels commensurate with industry standards, based on their respective position and job grade.

The Company s workforce is non-union except for approximately 70 hourly employees at its Marengo, Illinois facilities, which are represented by the International Association of Machinists (IAM). Arnold enjoys good labor relations with its employees and union and has a three year contract in place with the IAM, which will expire in June of 2013.

CamelBak

Overview

CamelBak, headquartered in Petaluma, California, is a diversified hydration and personal protection platform, offering Products for outdoor, recreation and military applications. CamelBak offers a broad range of recreational / military hydration packs, reusable water bottles, specialized military gloves and performance accessories. As the leading supplier of hydration products to specialty outdoor, cycling and military retailers, CamelBak maintains the #1 market share position in domestic recreational markets (80%-85%), per management estimates, for hands-free hydration packs and the #1 market share position for reusable water bottles in specialty channels (30%) per management estimates. CamelBak is also the hydration pack of choice for the warfighter, with an estimated 85% market share in post-issue hydration packs. Over its more than 20-year history, CamelBak has developed a reputation as the preferred supplier for the hydration needs of the most demanding athletes and warfighters. Across its markets, CamelBak is respected for its innovation, leadership and authenticity.

For the fiscal years ended December 31, 2012 and 2011, CamelBak contributed net sales of approximately $157.6 million and $42.7 million, respectively, and operating income of $25.5 million in 2012 and an operating loss of $6.8 million in 2011. CamelBak had total assets of $259.1 million and $262.0 million at December 31, 2012 and 2011, respectively. Net sales from CamelBak represented 17.8% of our consolidated net sales in the year ended December 31, 2012 and 7.0% of our consolidated net sales in 2011 (from acquisition date).

History of CamelBak

Founded in 1989 and headquartered in Petaluma, California, the company initially gained a following among mountain bikers in the early 1990 s through its first product, the ThermoBak . As the company grew among this base of users, its products continued to gain acceptance within other arenas where participants needed easy access to water to achieve optimal performance in their activity.

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The hands-free feature of CamelBak s products proved to be appealing to outdoor sports enthusiasts and critical to others, including the U.S. Military. After successfully developing the hands-free hydration category, the company in 2006, recruited new management, including industry veteran and Board member Sally McCoy in the role of CEO, and acquired Southwest Motorsports (since rebranded CamelBak Gloves). With a strong market presence in hydration packs, the management team focused on continued expansion into adjacent markets and developing and executing on a consistent strategy of innovation. Since this time, CamelBak has steadily grown sales and earnings and has enhanced its relationships with suppliers to strengthen its supply chain, reengineered its product distribution capabilities and tightly controlled operating expenses to match the needs of the business.

In 2006, CamelBak expanded its recreational business into the fast growing bottle category. The company s initial launch of the innovative Better Bottle was followed by numerous successful bottle product introductions for everyday users, road cyclists, kids and recreational enthusiasts, including eddy and the podium collection . CamelBak was first to market with an entirely BPA-free plastic bottle product line.

We purchased a majority interest in CamelBak on August 24, 2011.

Industry

Recreation Market With over 100 million participants, the outdoor recreational activity market represents a large, attractive and stable group of consumers. CamelBak s legacy products have historically been focused on a subset of this group, consisting of cyclists, mountain bikers and other passionate outdoor enthusiasts who tend to be loyal and consistent buyers of premium and performance-enhancing offerings. CamelBak s core customers are typically outdoor enthusiasts who exhibit very high participation rates and frequent purchasing behavior. In addition to CamelBak s legacy consumer group, the company has increasingly used its brand authenticity, credibility and broadening product portfolio to reach athletes in adjacent sporting activities.

Long-term growth in the hydration and personal protection industry is driven by a number of factors. Consumer recognition of personal hydration s importance to health and well-being has been a growing and enduring trend, reflected by the proliferation of bottled water and functional beverages. The importance of water as a healthy choice has become even more prominent as a key component to healthy living. Further, people are increasingly aware of the effects of even minimal dehydration on multiple functions of the body, including brain function, digestion, metabolism and skin health. CamelBak s products have proven their ability to provide greater hydration. An independent study conducted by Pepperdine University found that people utilizing CamelBak s Bite Valve technology consume 24% more than those using single serving disposable bottled water or less innovative products. In addition, recently there has been a reduction in disposable bottled water consumption in the U.S., primarily as a result of price and the wide-spread awareness of the negative environmental impact of disposable water bottles. According to the Beverage Marketing Corporation, the economy was the primary cause of the decrease in U.S. disposable bottled water sales in 2008 and 2009. With respect to the environment, the disposable water bottle s environmentally harmful lifecycle is generating significant backlash. The reliance on oil in the production and transportation of the bottles and the fact that over two-thirds of bottles are not recycled is driving consumers to seek alternatives to disposable bottles. Further, there are a number of government mandates forcing the elimination of disposable bottles. Nationwide, local governments are enacting these curbs to combat the cost and waste of disposable bottles. In recent years, governments of all levels have received scrutiny for fiscal irresponsibility and a number of municipalities have launched initiatives focused on curbing disposable water bottles in their communities. In 2006, a San Francisco investigation revealed that the city spent over $500,000 per year on bottled water. This revelation triggered a nationwide analysis of government spending on bottled water with public funds.

U.S. Government & Military Market The military acquisition process has responded to the demands of modern warfare which require forces to be more agile and flexible than ever before. This trend has been highlighted by the increased use of multiple funding and procurement mechanisms such as Rapid Fielding Initiatives (RFI) and Joint Urgent Operational Needs Statement (JUONS). These programs provide funding for mission critical operational needs such as IED detection and defeat and lifesaving warfighter equipment purchases without the normal bid and proposal process that can take months and even years to get equipment in the hands of the end user.

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In addition to responsive procurement contracts such as the RFI, the military has continued a gradual decentralization of purchasing which allows decision makers closer to the front line to select what specific items need to be acquired for a unit. Unit and individual equipment purchases are made primarily through U.S. Government Services Administration (GSA) contracts or at military exchange and supply locations. Warfighters and their families frequently purchase supplemental gear that is superior to standard issue products. CamelBak is well positioned to benefit from continued decentralized purchasing.

The U.S. defense budget has increased dramatically in the last decade in response to terrorism attacks at home and increased state and non-state threats abroad. Since 1998, Department of Defense (DoD) spending has increased over 90% primarily as a result of the two major wars in Iraq and Afghanistan. The 2012 DoD budget requested $531 billion in base spending with an additional $115 billion in overseas contingency operations (OCO) spending. By way of comparison, 2011 s budget was $687 billion, with a $528 billion base budget and the remaining $159 billion used for OCO. The reduced request for OCO is the direct result of reductions in troop deployment in Iraq and Afghanistan.

Recently, the DoD released its 2013 budget request which calls for a decrease in base budget spending to $525.4 billion, with an additional $88.5 billion dedicated to OCO. The budget estimates released, forecast a negative 0.3% real growth rate for the base budget from 2013 2017.

Products and Services

CamelBak focuses on offering high quality, industry leading hydration and performance equipment. The company s products fall into four key categories:

Hydration Packs CamelBak s heritage and legacy is in hydration packs and the company maintains the broadest and deepest line of packs in the industry. CamelBak s core hydration product consists primarily of an easily cleaned and filled polyurethane reservoir, a connecting tube and a self-sealing mouthpiece, or bite-valve, which facilitates simple and intuitive drinking. The CamelBak hydration system allows users to conveniently carry one to three liters of water, which can be easily accessed without interruption of the user s task or activity. The system is most often sold as an integrated backpack or waist-pack, which is uniquely designed for a specific use, such as biking, running or military applications. Hydration packs represented 50% and 44% of CamelBak s gross sales in the twelve months ended December 31, 2012 and 2011, respectively.

Recreation Packs

Having created the hands-free hydration category, CamelBak continues to be the dominant market leader in the recreational sector since its inception. After starting with a mountain biking product, CamelBak developed a host of other types of biking hydration packs that are designed to match specific types of biking. The company sells classic cycling packs that are lightweight and streamlined. CamelBak also sells larger more durable packs designed for long off-road rides and a Downhill/Freeride line designed for specific types of mountain biking activities. By starting with a focused line and expanding it to cover many different types of biking activities, CamelBak has created the deepest, broadest line of hydration packs in the industry.

As CamelBak extended its packs to cover different biking niches, top athletes from other outdoor sports began to clamor for product. To meet this demand, the company has created lines that cater to the diverse set of outdoor athletes:

- Hike / Alpine consists of lightweight packs with extra back panel padding and air flow for breathability
- Ski / Snowboard has attachments for helmets, boards and shovels
- Multi-sport are ultra-light and include wearable hydration units for use in almost any athletic activity
- Run includes hip packs designed to hold as many as four water bottles in a remarkably stable set up

These customized solutions have all been developed with an eye towards enhancing the performance of each activity s respective athletes. That customization is part of the innovative difference that allows CamelBak to differentiate itself in a competitive market.

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Military Packs

CamelBak sells a wide selection of category leading military packs. Management estimates the company has in excess of 85% market share in post-issue military hydration packs. It is also one of only a few brands sold to U.S. Military personnel that is allowed to prominently display the brand name on the outside of the product. The packs include features such as easy armor integration and extreme durability appropriate for use in the harshest conditions.

Bottles In 2006, CamelBak parlayed its credibility in hands-free hydration and expanded into bottles. The company introduced the Better Bottle , subsequently replaced by eddy , incorporated a number of features that quickly established it as a best-in-class hydration solution. These features include: (i) the patented spill-proof Bite Valve, (ii) the first insulated stainless steel water bottle and (iii) in 2008, the first all BPA-free line of plastic water bottles.

The success of the Better Bottle led the company to design a complete line of bottles that would mirror the pack line s legacy of customization. CamelBak developed a line for children, which included bite valves that have to be removed from the inside of the bottle to prevent choking. The company also released the Podium® insulated and non-insulated line, which includes features such as the patented Jet Valve .

The company s bottle offering has continued to evolve to meet the specific demands of consumers. These demands have included activity-based needs such as customized cycling bottles. They have also included health concerns, including the consumer backlash against BPA. CamelBak recognized this concern early and became the first to offer an entire line of BPA-free hard plastic bottles in May of 2008.

The company s bottle offering Groove , provides users the ability to filter water in any place at any time through its integrated straw assembly. Users simply fill the bottle with tap water, screw the cap on and start sipping. The integrated plant-based carbon filter reduces chlorine taste and odors found in tap water thus improving taste and eliminating the desire to purchase disposable bottles of water. Bottles represented approximately 34% and 31% of CamelBak s gross sales for the twelve months ended December 31, 2012 and 2011, respectively.

Gloves The evolution of CamelBak gloves parallels that of the pack business in the Government / Military channel. Initially created for pit crews in the auto racing market, members of elite squads who became aware of the product were impressed with its dexterity and durability. Following this unofficial endorsement, members of the U.S. Armed Forces began requesting CamelBak gloves. The gloves are highly-technical and difficult to produce, with some styles requiring 44 individual pieces for the assembly of the final product. Today, CamelBak gloves are exclusively a Government / Military product, as their technical characteristics exceed that which a non-military user would desire. Gloves represented approximately 6% and 14% of the company s gross sales for the twelve months ended December 31, 2012 and 2011, respectively. The reduction in Glove sales over the past two years is consistent with the reduction of deployed troops.

Accessories CamelBak offers various accessories to complement its hydration systems. Accessories are available for each product line and include items that are made to enhance hydration performance and others for maintenance or replacement parts.

CamelBak s goal is to reinvent the way that individual athletes, warfighters and every day users hydrate and perform. To that aim, the company has developed a number of products that help to further enhance the already innovative way that its products deliver water:

- Elixir is a flavored electrolyte tablet that is designed to work in concert with CamelBak s reservoirs. Elixir improves alertness and hydration.

- All Clear is a water purification solution that is integrated with CamelBak s bottles.

CamelBak products are known for their high quality and durability. The company provides products to help maintain this durability and offers replacement parts in the rare instance that the products cease to perform at the optimal levels:

- Reservoir cleaning kits are designed to optimally clean the reservoirs that are inside of each pack. Properly cleaning and drying the reservoirs promotes longevity.

Replacement reservoirs are made for each pack. This ensures that in the rare case that a reservoir must be replaced, the athlete or warfighter does not need to replace the entire pack but can easily swap out the necessary components. Many users also like to have multiple reservoirs.

In addition to recreational accessories, the company offers a specialized line associated with its military products. These accessories help enhance the performance of military products by adding resistance to chemical and biological agents or allowing connection to standard issue gas masks. For example, the HydroLink allows warfighters to replace their bite valve with a connector, allowing them to hydrate while wearing their gas mask. Accessories accounted for approximately 10% and 11% of CamelBak s gross sales for the twelve months ended December 31, 2012 and 2011, respectively.

Competitive Strengths

Leading Brand Recognition & Market Share CamelBak believes it has a #1 market share in the following areas: (i) recreational hands- free hydration packs, (ii) reusable water bottles for specialty channels and (iii) post-issue hydration packs for the U.S. military. The company enjoys outstanding awareness and a reputation for superior performance with consumers, retailers and warfighters. For example, within the Armed Forces, CamelBak is one of only a few companies allowed to prominently display its brand name on active military products.

Preferred Partner CamelBak is a preferred partner to leading retailers and the military. The company is a supplier to leading national specialty and sporting goods retailers, including REI, EMS, Dick s Sporting Goods and The Sports Authority. In addition, CamelBak does business in over 400 military retail exchanges.

Business Strategies

Introducing Technically Superior Products in Core Categories The company s core categories include hydration packs, bottles and warfighter protection products, and CamelBak s mission is to continuously reinvent the way people hydrate and perform. To meet this goal, the company will continue to create innovative, technical solutions that exceed the demands of its customers. The company s product pipeline for its core customers remains robust.

Expanding Product Suite in Everyday Hydration to Reach New Customers and Channels The CamelBak brand is synonymous with personal hydration, and this credibility grants the company permission to enter broader aspects of hydration. The company is committed to continuing to broaden its portfolio of personal hydration solutions to reach new customers, and, under the leadership of Ms. McCoy, has proven that it can extend its brand beyond hard-core athletes. For example, the company has successfully reached new consumers and channels through its water bottle product line, which offers the features desired by its core customer base of performance athletes to the everyday customer shopping at Target. As the company continues to expand its relevance to everyday users, its authenticity will allow the company to enter other areas such as purification and other products.

Broadening International Opportunities Management believes there is significant potential to expand its international sales in the consumer market. Currently, CamelBak s recreational business is sold through a network of approximately 65 foreign distributors. With improved distribution in the recreational market, the company would have a number of opportunities to expand throughout Europe, Asia and South America.

Penetrating Select Areas of Specialty Retail CamelBak aspires to build a product portfolio that shapes the way consumers and warfighters perform across all activities. To that aim, CamelBak has made significant strides introducing new products that target activities outside of its core biking and hiking audience. Past examples include multi-sport enthusiasts and runners. The company targeted the multi-sport category with highly- functional wearable hydration, which consists of a wearable shirt with built in hydration pack that allows enthusiasts to hydrate hands-free without a traditional pack.

CamelBak keeps an open dialogue with the athletes it endorses and is thus able to gain real-time feedback on the products it produces. By learning the needs of these consumers and others, CamelBak is able to identify other areas to develop ground-breaking solutions. As CamelBak continues to innovate and create new products to serve the needs of more diverse consumers, it will further grow sales to these retailers. As a sports subculture brand, CamelBak is able to migrate to different activities without losing the authenticity and credibility it has developed as a leading product innovator. As examples, skiers and kayakers alike have adopted the brand as their own without even realizing that other sports enthusiasts have done the same.

CamelBak launched its own direct to consumer E-Commerce site during the fourth quarter of 2012.The site initially offered bottles and accessories along with water packs. In 2013 the site is expected to expand and will offer more hydration packs which will coincide with CamelBak s annual pack launch.

Research and Development

CamelBak s hydration products are among the most technically advanced and rigorously engineered in their markets. They are specifically designed to function and perform under diverse and extreme conditions. CamelBak s research and development effort is at the core of its strategy of product innovation and market leadership. CamelBak s products feature a combination of innovative design, high-quality materials, and superb functionality and performance elements and are recognized as being the leaders or among the leaders in all of the market segments in which they participate.

CamelBak has a robust core research and development team, which has collectively over 36 years of combined industry experience. In addition to the core engineering group, a large number of other CamelBak staff members, who also use the company s products, contribute to the research and development effort at various stages. Product development also includes collaborating with customers and field testing. This feedback helps ensure products will meet the company s demanding standards of excellence as well as the constantly changing needs of end users.

CamelBak s research and development activities are supported by state-of-the-art engineering software design tools, integrated manufacturing facilities and a performance testing center equipped to ensure product safety, durability and superior performance. The testing center collects data and tests products prior to and after commercial introduction. Research and development costs (from the date of acquisition) totaled $3.0 million and $0.8 million during the years 2012 and 2011, respectively.

Customers and Distribution channels

CamelBak offers a unique value proposition for its customers. As an innovative subculture sports brand, CamelBak has the authenticity and credibility to defend market share, command premium prices and leverage into new categories. The brand strength allows retailers to hold prices and thus protect margins. Further, the company s Got Your Bak lifetime warranty speaks to the level of quality and customer service offered. The company s products, which are sold domestically and internationally, are segmented into two major end markets: Recreational and Government/Military. CamelBak s powerful product distribution network is comprised of long-standing, entrenched relationships with a diversified set of customers. CamelBak s top ten customers comprised approximately 49% and 52% of gross sales in the year ended December 31, 2012 and 2011, respectively, with no single customer accounting for greater than 9% of gross sales.

Recreational Distribution CamelBak markets its hydration and performance products to several channels in the recreational market. Management estimates that the company currently holds in excess of 85% of the market share of the hands-free hydration market. A share this large demonstrates the strength of the brand and the credibility that the products have with consumers. CamelBak invented the category in 1989 and although competitors have introduced a number of similar products, the company has held on to its base.

Recreational Domestic Distribution: The Recreational Domestic Division is focused on product distribution through a variety of retail accounts in the United States. Particular emphasis is placed on premium active lifestyle retailers across a broad spectrum of channels, including camping/outdoor, bike, natural foods, housewares, hunting/fishing, paddle sports and surf/skate.

The division manages approximately 2,600 retail customers with over 9,500 retail storefronts. Current distribution channels range from specialty bicycle, outdoor, paddle sports, hunting stores and catalogs to large outdoor and sporting goods chains that reach the broader market. Importantly, the company has selectively expanded and diversified its distribution channels over time. Today, notable customers include REI, Dick s Sporting Goods, EMSTarget, Whole Foods Market, Academy and The Sports Authority.

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The company s entrance into the reusable bottle category in 2006 resulted in a notable broadening of distribution, as the company made the decision to strategically expand into new channels. The company felt it was important to reach an even broader consumer base to further its vision of obsoleting bottled water as the most common way to hydrate. The bottle business has also enabled CamelBak to achieve penetration in the college and corporate sponsorship markets.

Recreational International Distribution: The Recreational International division is focused on product distribution through outdoor, sporting goods and specialty retailers that are managed through local distributors focused on premier retail accounts. The company maintains an office in Europe to provide oversight of distributor performance, market intelligence and limited supplemental marketing support, including event staffing, trade show management, athlete sponsorships, public relations and market/product intelligence gathering. Order scheduling, fulfillment and logistics support for the company s international operations are provided from CamelBak s Petaluma headquarters.

Key international markets include the United Kingdom, Germany, France, Australia, Japan, Canada, Norway and Korea. As is the case in the United States, the CamelBak brand is widely recognized and respected by enthusiasts and maintains a dominant market share.

Military Retail Exchange Distribution Military retail exchanges, including the Army and Air Force Exchange Service (AAFES), the Navy Exchange Service Command (NEXCOM) and the Marine Corps Exchange (MXC), are essentially large retail chains serving the military community. Military personnel, veterans and their families are strongly incentivized to shop at exchanges given that the store markup is typically less than the off base markup from other retailers, exchanges do not charge sales tax and a portion of the exchanges earnings often go towards funding expenditures related to the military s morale, welfare and recreation. Furthermore, the exchanges provide an added benefit to consumers, given the convenience they provide to troops deployed in nearby locations.

The military retail exchanges represent large distribution platforms extending across many different countries. CamelBak sells through over 400 locations. CamelBak pioneered the adoption of hands-free hydration systems by U.S. and foreign militaries and is today, we believe, the preferred brand of warfighters. As a result, CamelBak has dominant market share throughout the military retail channel. CamelBak is one of AAFES largest vendors and has a strong, long-term relationship with the retailer.

Government / Military Distribution In the Government / Military division, CamelBak sells products and accessories related to both hydration and performance. CamelBak continues to expand its Government / Military market by increasing penetration into foreign governments and militaries. A key component of U.S. foreign policy is the replacement of some deployed troops with those of foreign militaries. CamelBak s success in the U.S. Military carries tremendous credibility abroad, which has enabled the company to achieve meaningful adoption outside the U.S.

Domestic Government / Military Distribution CamelBak sells its products through a range of domestic Government / Military channels:

GSA: The GSA provides a channel for all federal government agencies and government end-users to procure items easily. All products sold through the GSA must be pre-approved to get listed on GSA schedules. Once products are listed, thousands of Government / Military units and agencies purchase through this channel knowing that all pricing and legal obligations have already been negotiated and approved.

Direct Department of Defense Procurement: The U.S. Military will, from time to time, request for proposal a large amount of a given product. In addition, this request can oftentimes require that the product be manufactured with domestic content and other various specific rules. As it relates to CamelBak s business, the company calls such direct contracts DFAR business. This is patterned after the Defense Federal Acquisition Regulation (DFAR) set of rules used by the government. Selling through the direct government channel entails abiding by specific sourcing guidelines and responding to a solicitation. Typically, a branch of the military will identify a need, issue a solicitation and multiple parties will bid to win the contract. While these orders are intermittent and often large, CamelBak has developed a strong supply chain to deal with these types of orders.

International Government / Military Distribution International Sales in the Government / Military is driven by ordinary replenishment and large solicitations that occur on an irregular basis to meet the equipment needs of each individual country. CamelBak has consistently participated in these solicitations with significant historical success.

Sales and Marketing

CamelBak approaches marketing from a unique point of view that is meant to inspire customers. CamelBak is engaged in small endorsement deals that provide gear to actual users as well as athletes who bike, climb and hike professionally as opposed to entering into large multi-year contracts. Second, the company s marketing campaign uses photographs and videos shot from a user s perspective. This photographic style encourages the consumers viewing the ad to imagine they are engaging in the activity shown. This experience serves to promote the inspirational nature of CamelBak s brand by liberating people to go further.

Marketing CamelBak uses a two pronged approach to marketing:

CamelBak has set out to aggressively pursue new users and expand its customer base while remaining true to its authentic, innovative ideals. Given the customization that has occurred across the company s product lines, CamelBak created a unique, highly targeted marketing plan to acquire new users for specific products. In the case of Groove , CamelBak set out to expand its customer base of 25-45 year old women. To that end, the company designed print and web ads with a message that appeals more directly to this group and placed these advertisements in the appropriate women s lifestyle magazines. The company also has a strong presence on the internet and uses instructional videos and direct marketing through social media sites such as Facebook.

CamelBak also makes a point to continue cultivating the passionate consumer base that already admires and respects the company and its products. A recent example is the release of the Antidote Reservoir. The company uses a unique marketing approach for different target users. Since these products are geared towards passionate outdoor athletes, CamelBak placed ads in forums including: (i) bicycling and mountain bike magazines, (ii) backpacking and hiking magazines and (iii) internet and social media sites that cater to active men and women.

Sales Organization CamelBak s in-house sales team consists of dedicated sales people and customer service employees. The sales organization is strategically aligned by product category/sales channel. The sales managers split coverage for major national accounts with one team responsible for maintaining and growing sales to established channels and the other for business to larger national retailers and natural foods stores. With an average tenure of 5 years with the company, CamelBak s sales team maintains enduring and entrenched relationships with each of its customers.

The Recreational Domestic division manages customers through both an in- house sales management staff and a network of sales agencies consisting of a number of independent sales representatives. The Recreational International division manages its international customers through local distributors focused on premier retail accounts. The company maintains an office in Europe with two employees to provide oversight.

CamelBak had sales backorders totaling $29.3 million and $29.4 million At December 31, 2012 and 2011, respectively.

Competition

CamelBak pioneered the hydration category with the introduction of the hydration pack more than 20 years ago. CamelBak s brand admiration and customer loyalty, which are driven by its innovative products, have allowed the company to continuously defend its market position in packs. These traits also allowed the company to successfully enter the bottle category where it holds a leading market position.

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A summary of CamelBak s competitors in hydration packs, bottles and reservoirs is listed below:

Hydration Packs	Bottles	Reservoirs
Osprey	Nalgene	Platypus
The North Face	SIGG	Hydrapak
DaKine	Nathan Performance Gear	Source
	Polar	
	Kleen Kanteen	
	Contigo	

Across its military product set, CamelBak competes against a wide variety of industry players which include large prime and tier two defense companies, small and mid-sized companies specializing in warfighter equipage and companies focused predominantly on the consumer or materials market with a limited number of defense product offerings. CamelBak is recognized as a high-end supplier in each of its product categories (hydration and gloves). Management believes CamelBak is the leading supplier of post-issue hydration packs with over 85% of the market share and among the leading providers of specialized tactical gloves which are worn by some of the most elite users in the world.

Suppliers

CamelBak s product manufacturing is based on a dual strategy of in-house manufacturing and strategic alliances with select sub-contractors and vendors. CamelBak operates a scalable, low-cost supply chain, sourcing materials and employing contract manufacturers from across the Asia-Pacific region, the U.S. and Puerto Rico. Once manufactured, products are shipped directly from overseas manufacturers to CamelBak s distribution center in San Diego for receiving and stocking and thereafter distributed to retail locations or third-party distributors.

CamelBak has developed an efficient and low-cost supply chain. The company s deep understanding of military procurement requirements has allowed it to build a flexible network of vendors to reliably meet large military orders on short notice and to shift orders to vendors to be compliant with military requirements for its products. While striving to maximize the profitability of its products, the company is also keenly aware of its corporate responsibility and, thus, holds itself and its vendors to the highest supply chain practices. As a result of the company s dedication to superior supply chain and manufacturing practices, the U.S. Military s GSA named CamelBak the Green Contractor of the Year in 2009 and MAS Contractor of the year in 2011 .

In recent years, the company has streamlined its operating expenses, tightening cost controls and maintaining a cost structure more in line with the size of its platform. Additionally, the company has driven cost improvements by negotiating prices with vendors using an open book policy, in which each vendor s profit margins, labor rates and material costs are agreed to upfront. This allows the company s operations group to negotiate reductions in component prices from raw material manufacturers resulting in cost savings that are passed through to CamelBak.

The company s primary raw materials are fabric, resin, polyurethane film and various resins for which the company and/or its supplier partners receive multiple shipments per week. The company purchases its materials from a combination of domestic and foreign suppliers.

Intellectual Property

Hydration priorities include easy cleaning and filling, freshness and taste, durability, temperature, water purity, leak-proof products and sustainability, all of which improve a customer s overall hydration experience or enable the customer to perform at high levels. As a reflection of this focus, CamelBak holds 39 active patents and 16 pending patent applications.

Regulatory Environment

Management is not aware of any existing, pending or contingent liabilities that could have a material adverse effect on the company s business. The company is proactive regarding regulatory issues and is in compliance with all relevant regulations. Management is not aware of any potential environmental issues.

Employees

As of December 31, 2012, CamelBak employed approximately 297 persons. None of CamelBak s employees are subject to collective bargaining agreements. CamelBak s relationship with its employees is good.

Ergobaby

Overview

Ergobaby, headquartered in Los Angeles, California, is a premier designer, marketer and distributor of baby wearing products, stroller travel systems and accessories. Ergobaby offers a broad range of wearable baby carriers, stroller travel systems and related products that are sold through more than 650 retailers and web shops in the United States and internationally in about 50 countries.

Ergobaby s reputation for product innovation, reliability and safety has led to numerous awards and accolades from consumer surveys and publications, including babycenter, Parenting Magazine, Pregnancy magazine and Wired magazine.

For the fiscal years ended December 31, 2012, 2011 and 2010, Ergobaby had net sales (from the date of acquisition) of approximately $64.0 million, $44.3 million and $12.2 million, respectively. Ergobaby had operating income totaling $10.9 million and $7.9 million in the years ended December 31, 2012 and 2011, respectively, and an operating loss of $2.4 million from its date of acquisition through December 31, 2010. Ergobaby had total assets of $117.7 million, $118.4 million and $95.7 million at December 31, 2012, 2011 and 2010, respectively. Ergobaby s net sales represented 7.2% and 7.3% of our consolidated net sales for the year ended December 31, 2012 and 2011 and 2.4% of our consolidated net sales for the year ended December 31, 2010 (from acquisition date).

History of Ergobaby

Ergobaby was founded in 2003 by Karin Frost, who designed baby carriers following the birth of her son. The product line has since expanded into seven primary product lines: the Original, Designer, Organic, Sport, Performance, Travel, and Options carriers with multiple style variations. In its second year of operations, Ergobaby sold 10,500 baby carriers and by 2012 sold over 890,000 in the year. In order to support the rapid growth, in 2007, Ergobaby made a strategic decision to establish an operating subsidiary (EBEU) in Hamburg, Germany. We purchased a majority interest in Ergobaby on September 16, 2010.

On November 18, 2011 Ergobaby acquired Orbit Baby for approximately $17.5 million. Founded in 2004 and based in Newark, California, Orbit Baby produces and markets a premium line of stroller travel systems, including car seats, strollers and bassinets that are interchangeable using a patented hub ring.

Both brands are well regarded in the infant and juvenile industry. Ergobaby was named to the 20 Best Products in the Last 20 Years by Parenting Magazine (2007), and continues to be recognized for its quality evident by recently being named babycenters 2012 Moms Pick for best Baby Carrier. While The Orbit Baby Infant System has received vast honors, including, 2007 iParenting Media Award for Best Product, Baby Gizmo s Editor s Choice 2012, babble.com favorite Car Seats 2012, She Knows Parenting Stroller Award 2011, and lilsugar Best Stroller of 2010.

Industry

Ergobaby competes in the large and expanding infant and juvenile products industry. The industry exhibits little seasonality and is somewhat insulated from overall economic trends, as parents view spending on children as largely non-discretionary in nature. Consequently, parents spend consistently on their children, particularly on durable items, such as car seats, strollers, baby carriers, and related items that are viewed as necessities. Further, an emotional component is often a factor in parents purchasing decisions, as parents desire to purchase the best and safest products for their children. As a result, parents spend from $8,480 to $23,690 on their child on an annual basis for related housing, food, transportation, clothes, healthcare, daycare and other items, depending on age of the child & annual income. On average, households spent from 12-25 percent of their before-tax income on a child, according to the USDA s most recent report (May 2011). Similar patterns are seen in other counties around the world. According to a Mintel report published in March 2010, estimated 2010 retail dollars spent on baby durables reached approximately $10.3 billion in the U.S., up compared to approximately $9.5 billion in 2004, with a considerably larger market worldwide. The U.S. retail market is expected to continue its growth trajectory through 2014 with an anticipated market size of approximately $12.0 billion.

Demand drivers fueling the growing spending on infant and juvenile products include favorable demographic trends, such as (i) an increasing number of births worldwide; (ii) a high percentage of first time births; (iii) an increasing age of first time mothers and a large percentage of working mothers with increased disposable income; and (iv) an increasing percentage of single child households and two-family households.

Given that the child s safety is paramount, many parents do not want to compromise a baby or child s safety by purchasing secondhand products to save money. In many cases, when purchasing secondhand, the parent does not know key facts about the product they are buying, such as the age of the product, history of the item, or potential recalls by the manufacturer. Furthermore, the safety standards for the product may have changed since the version being resold, resulting in a product that does not meet the most rigorous safety standards. Consequently, as parents consider purchases of important necessities such as baby durables, they typically favor new products. According to Mintel Research, approximately 83% of baby carrier purchases were first-time purchases, with the remainder being either purchased second hand or borrowed.

Safety influences not only whether parents purchase new or used products, but also which brands parents choose, which consequently impacts pricing and competition within the infant and juvenile products market. In purchases of baby durables, parents often seek well-known brands that offer a sense of comfort regarding a product s reliability and safety. As a result, brand name and safety certifications can serve as a barrier to entry for competition in the market, as well as allow well-known brands such as Ergobaby to charge a premium.

Wearable Carriers and Baby Wearing Trends

Within the broader market for infant and juvenile products, Ergobaby operates specifically within the market for child mobility and transport products. According to the Juvenile Products Manufacturers Association (JPMA), reported child mobility and transport manufacturer dollar sales, which includes sales of carriers, strollers, travel systems, and related products, totaled approximately $349.1 million in the U.S. in 2009. Penetration of baby carriers currently trails that of strollers, car seats, and other infant and juvenile products. JPMA manufacturer sales growth from 2008 to 2009 suggests that the soft carrier segment is growing more rapidly than other infant and juvenile product categories, with 7.8% unit growth and dollar growth. Comparatively, stroller shipments and convertible car seat shipments decreased 1.6% and 8.3%, respectively, over the same period

Management believes that continued growth within the market for wearable baby carriers is driven by several trends, including (i) lower relative penetration of baby carriers versus other infant and juvenile products; (ii) favorable demographics; (iii) increasing focus on the popularity of baby wearing; and (iv) convenience and mobility of wearable products.

Products and Services

Ergobaby- Baby Carriers

Ergobaby has two main baby carrier product lines: baby carriers and accessories. Ergobaby s baby carrier design supports a natural sitting position for babies, eliminating compression of the spine and hips that can be caused by unsupported suspension. The baby carrier also balances the baby s weight to parents hips and shoulders, and alleviates physical stress for the parent. The organic carrier line uses 100% organic cotton from India. Additional accessories are provided to complement the baby carriers.

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Within the carrier category, Ergobaby sells seven primary product lines: the Original, Designer, Organic, Sport, Performance, Travel, and Options carriers and; within each line, Ergobaby offers multiple style variations. Amongst the carrier category, Original carriers represented 48% of 2012 and 39% of 2011 carrier sales, respectively, and Organic carriers represented 22% and 37%, of 2012 and 2011 carrier sales, respectively, with all other carriers representing the remaining sales in each year. Carrier sales were approximately $44.6 million; $37.8 million and $30.0 million in the years ended December 31, 2012, 2011 and 2010, respectively, and represented approximately 70% of total sales in 2012, and 86% of total sales in 2011 and 2010.

Within the accessories category, Ergobaby sells twelve primary product lines: back packs, bibs, changing pads, chest strap, doll carrier, front pouch, hood replacement, Infant Insert, papoose coat, teething pads, waist extension and a weather cover. Within each line, Ergobaby offers multiple style variations including color and organic/non-organic fabric. The Infant Insert is the largest sales component of the accessory category, representing more than half of total accessory sales for 2010 and 2011. Accessory sales were $6.0 million, $6.5 million and $4.4 million and represented approximately 9%, 15% and 13% of total sales in 2012, 2011 and 2010, respectively.

Ergobaby s core baby carrier product offerings with average retail prices are summarized below:

6 styles of baby carriers $115 $195

1 style of organic carrier in 7 colors $135 $160

5 styles of Infant Inserts $25 $38

12 different accessory products $10 $64

Orbit Baby Infant Systems

The Orbit Baby Infant System has three main product groups: stroller travel systems, product extensions and accessories.

The Orbit Baby Stroller Travel System is a three-piece kit that includes an infant car seat, car seat base, and stroller. Unlike traditional infant travel systems, the Orbit Stroller Travel System s unique docking technology, or SmartHub™ , allows for easy interchange of four different seats, including the Infant Car Seat, Stroller Seat, Bassinet, and Toddler Car Seat.

The Orbit Baby car seat base (which stays in the car when not in use) is touted as the easiest, quickest base to safely install. The base s patent-pending StrongArm™ technology allows a secure installation in 60 seconds and easily docks the car seat from almost any angle, allowing the parent to ergonomically transport the child.

The Orbit Baby Infant Car Seat is the common plug-in for the three-in-one system and can be moved effortlessly from the car seat base to the stroller. As a result of the SmartHub technology, Orbit is the only infant car seat that ergonomically rotates for simple docking and undocking to and from the car and stroller.

The third member of the Stroller Travel System is Orbit s modern and easy-to-use stroller. As is the case with the car seat base, the circular SmartHub allows the infant car seat to dock on the stroller from any angle, and with 360 degree rotation, the baby can face rear, forward, or sideways to view the world from different perspectives.

Orbit Baby offers product extensions including additional seats and strollers, including the Double Helix, to accommodate growing children and families.

Orbit Baby also offers a wide range of accessories including the Sidekick Stroller Board, Stroller Panniers, Weather Pack, Color Pack, Footmuffs, Stroller Travel Bag and Baby Gear Spa Kit.

Orbit Baby s core product offerings, extensions and accessories and suggested retail prices are below:

Stroller Travel System (includes Infant Car Seat, Car Seat Base, Stroller)	$940
Stroller	$280-$750
Car Seats and Car Seat Base	$380 $440
Bassinet Cradle	$295
Accessories	$50-$195

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Competitive Strengths

Ergobaby Carriers are known for their unsurpassed comfort Ergobaby s superior design results in improved comfort for both parent and baby. Parents are comfortable because baby s weight is evenly distributed between the hips and shoulders while baby sits ergonomically in a natural sitting position. The concept of baby carrying has increased in popularity in the U.S. as parents recognize the emotional and functional benefits of carrying their baby. Consumers continually cite the comfort, design, and convenient hands free mobility the Ergobaby carrier offers as key purchasing criteria.

Orbit Baby Innovation With 14 patents and 10 patents pending, Orbit Baby offers a complete child travel system, from stroller to car seat and beyond. A favorite with moms and dads alike, the integrated Orbit Baby system is designed to take your child everywhere with unprecedented ease and style. With an emphasis on advanced safety and engineering, Orbit Baby is continually recognized for its innovation, ergonomic design and environmentally friendly focus. Orbit Baby applies hands-on experience and extensive research to create products that are elegantly simple, intuitive to use, and unsurpassed in real-world safety.

Business Strategy

Increase Penetration of Current U.S. Distribution Channels Ergobaby continues to benefit from steady expansion of the market for wearable baby carriers and related accessories in the U.S. and internationally. Going forward, Ergobaby will continue to leverage and expand the awareness of its outstanding brands (both Ergobaby and Orbit Baby) in order to capture additional market share in the U.S., as parents increasingly recognize the enhanced mobility, convenience, and the ability to remain close to the child that Ergobaby carriers enable. The company currently markets its products to consumers in the U.S. through brick-and-mortar retailers, including specialty boutiques; online web shops; and directly through its website. Management has developed a targeted strategy to increase its penetration of these currently underpenetrated distribution channels that includes: (i) improved retain presence, including new packaging and in-store support materials; (ii) improving the effectiveness of marketing programs including utilization of social sites, digital marketing, and improved consumer engagement, and (iii) development of new products and designs.

Cultivate Attractive New Distribution Channels In addition to its existing retail customer base, comprised primarily of small specialty retail stores and boutiques, there are numerous other retail channels that offer tremendous growth opportunities for Ergobaby products. Specifically, management recently began targeting several types of retailers as the company continues its growth trajectory, including (i) multi-store maternity and infant and juvenile products chains; (ii) on-line retailers; (iii) organic and natural specialty retailers; (iv) department stores; and (v) mass retailers.

International Market Expansion Testimony to the global strength of its lifestyle brand, Ergobaby derives nearly 58% of its sales from international markets. Similar to the U.S., Ergobaby can continue to leverage its brand equity in the international markets it currently serves to aggressively drive future growth, as well as expand its international presence into new regions. The market for the company s products abroad continues to grow rapidly, in part due to the growth in the number of births worldwide and the fact that in many parts of Europe and Asia, the concept of baby wearing is a culturally entrenched form of infant and child transport.

New Product Development Management believes Ergobaby has an opportunity to leverage its unique, authentic lifestyle brand and expand its product line.

Since its founding in 2003, the company has successfully introduced new carrier products to maintain innovation, uniqueness, and freshness within its product line. Specifically, 20 new SKUs were added in 2012, 23 new SKU s added in 2011 and 22 new SKU s added in 2010. These product introductions include both evolutionary product introductions, such as new colors and patterns for the company s current carriers and associated products, as well as entirely new product categories. Major recent new product introductions include the Ergobaby infant insert

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Heart2Heart, which modifies the Ergobaby carrier to provide additional support for a baby s developing spine. Additionally, in 2010, Ergobaby launched the Performance carrier and the Option carrier, the latter which allows the consumer to customize the look of the carrier with optional colored fabrics and designs. In 2011, Ergobaby launched the Daypack which is a hybrid of a Backpack and Diaper Bag that snaps around the Ergobaby Carrier straps to provide a comfortable, hands-free way to tote the day s supplies in addition to all of your baby essentials. In 2012 Ergobaby introduced the Stowaway Carrier, and a designer carrier collection to include a matching diaper bag. The Stowaway Carrier has the padded straps and waist belt that make all Ergobaby carriers comfortable, yet easily folds into its own front pouch for compact storage.

Orbit Baby was founded in 2004 using its original design of the Orbit Infant System which is a three-piece kit that includes a base, infant car seat, and stroller, using the unique docking technology, (SmartHub). Since then, Orbit Baby has successfully introduced the Orbit Bassinet Cradle, and various accessories that has increased its versatility and kept them trend forward. In 2012, Orbit Baby introduced the Double Helix Stroller Frame, Orbit Baby s complete double stroller solution. The innovative design features a narrow frame with front and back rotating seats. With two SmartHub rings parents have the option to use any existing Orbit Baby seat.

Customers

Ergobaby primarily sells its products through brick-and-mortar retailers, online retailers and distributors and derives approximately 58% of its sales from outside of the U.S. Within the U.S., Ergobaby sells its products through over 650 brick-and-mortar retail customers and small infant and juvenile products chains, representing an estimated 2,000 retail doors. Ergobaby products are sold through its German based subsidiary, Ergobaby Europe, which services brick-and-mortar retailers and online retailers in Germany and France as well as services a network of distributors located in the United Kingdom, Austria, Finland, Russia, Switzerland, Belgium, the Netherlands, Sweden, Norway, Spain, Denmark, Italy, Turkey and the Ukraine. Sales to customers outside of the U.S. and European markets are predominantly serviced through distributors granted rights, though not necessarily exclusive, to sell within a specific geographic region.

Sales & Marketing

Within the U.S., Ergobaby directly employ sales professionals and utilizes independent sales representatives assigned to differing U.S. territories managed by in-house sales professionals. Independent salespeople in the U.S. are paid on a commission basis based on customer type and sales territory.

In Europe, Ergobaby directly employs its salespeople. In Europe, salespeople are paid a base salary and a commission on their sales, which is standard in that territory. Ergobaby Europe handles all Ergobaby distributor orders within the European countries including Russia and Ukraine; all other orders are handled through Ergobaby s U.S. offices.

Ergobaby has implemented a multi-faceted marketing plan which includes (i) targeted print advertising; (ii) online marketing efforts, including online advertisement, search engine optimization and social networking efforts; (iii) increasing tradeshow attendance; and (iv) increasing promotional activities.

Ergobaby had approximately $10.0 million and $3.5 million in firm backlog orders at December 31, 2012 and 2011, respectively.

Competition

The infant and juvenile products market is fragmented, with a few larger manufacturers and marketers with portfolios of brands and a multitude of smaller, private companies with relatively targeted product offerings.

Within the infant and juvenile products market, Ergobaby s Carriers primarily compete with companies that market wearable baby carriers. Within the wearable baby carrier market, several distinct segments exist, including (i) slings and wraps; (ii) soft-structured baby carriers; and (iii) hard frame baby carriers.

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The primary global competitors in this segment are Baby Bjorn and Manduca, which also market products in the premium price range. Especially in the US, Ergobaby also competes with several smaller companies that have developed wearable carriers, such as Beco, Boba, and L il Baby. Within the soft-structured baby carrier segment, Ergobaby benefits from strong distribution, good word of mouth, and the functionality of the design.

The Orbit Baby Infant System principally competes with the following premium brand stroller manufacturers:

- Chicco
- Bugaboo
- Maclaren
- Baby Trend
- Stokke
- Quinny Baby
- UPPAbaby

Suppliers

Ergobaby sources its products from China, Vietnam and India. In 2012, Ergobaby began sourcing non-organic carriers and accessories from a manufacturing facility in Vietnam. China and Vietnam accounted for approximately 69% of Ergobaby s purchases in 2012. Ergobaby partnered with a manufacturer located in India in 2009, which manufactures Ergobaby s organic carriers and accessories, and represented approximately 31% of Ergobaby s purchases in 2012. Ergobaby s manufacturers in China, Vietnam and India have the additional capacity to accommodate Ergobaby s projected growth.

Intellectual Property

Ergobaby maintains a utility patent on its standard carrier, which was filed in 2003 and issued January 29, 2009. Notwithstanding this patent, Ergobaby primarily depends on brand name recognition and premium product offering to differentiate itself from competition. Ergobaby also maintains three utility patents for its Orbit Baby SmartHub technology.

Regulatory Environment

Management is not aware of any existing, pending, or contingent liabilities that could have a material adverse effect on the company s business. The company is proactive regarding regulatory issues and is in compliance with all relevant regulations. Ergobaby maintains adequate product liability insurance coverage and to date has not incurred any losses. Management is not aware of any potential environmental issues.

Employees

As of December 31, 2012 Ergobaby employed 86 persons in 6 locations. None of Ergobaby s employees are subject to collective bargaining agreements. We believe that Ergobaby s relationship with its employees is good.

Fox

Overview

Fox, headquartered in Scotts Valley, California, is a branded action sports company that designs, manufactures and markets high-performance suspension products and components for mountain bikes, snowmobiles, motorcycles, all-terrain vehicles (ATVs), and other off-road vehicles.

Fox s products are recognized by manufacturers and consumers as being among the most technically advanced suspension products currently available in the marketplace. Fox s technical success is demonstrated by its dominance of award winning performances by professional athletes utilizing its suspension products. As a result, Fox s suspension components are incorporated by OEM customers on their high-performance models at the top of their product lines. OEMs leverage the strength of Fox s brand to maintain and expand their own sales and margins. In the Aftermarket segment, customers seeking higher performance select Fox s suspension components to enhance their existing equipment.

Fox sells to over 175 OEM and over 7,800 Aftermarket customers across its market segments. In each of the years 2012, 2011 and 2010, approximately 81%, 80% and 78% of gross sales were to OEM customers with the remaining sales to Aftermarket customers. Fox s senior management, collectively, has over 100 years of experience in the suspension design and manufacturing industry and other closely related industries.

For the fiscal years ended December 31, 2012, 2011 and 2010, Fox had net sales of approximately $235.9 million, $197.7 million, and $171.0 million and operating income of $26.2 million, $22.6 million and $19.6 million, respectively. Fox had total assets of $142.8 million, $130.0 million and $130.8 million at December 31, 2012, 2011 and 2010, respectively. Fox s net sales represented 26.7%, 32.6%, and 33.9% of our consolidated net sales for the years ended December 31, 2012, 2011 and 2010, respectively.

History of Fox

Fox was founded by Bob Fox in 1974 when, having participated in motocross racing, he sought to create a racing suspension shock that performed better than existing coil spring shocks. Working in a friend s garage, Mr. Fox created the Fox Air-Shox . The product was successful and within two years it was used to win the U.S. 500cc National Motocross Championship.

In 1978, Fox began producing high performance suspension products for off-road and motorcycle racing. From 1978 to 1983, Fox suspension users won the 500cc Grand Prix (motocross), Baja 1000 (off-road), AMA Super Bike (motorcycle road racing) and Indy 500 (auto racing) generating greater market awareness for the Fox brand especially among racing enthusiasts.

As Fox grew, the company applied the same core suspension technologies developed for motocross racing to other categories. In 1987, Fox entered the snowmobile market. By 1993, Fox began supplying the mountain bike industry with rear shocks before offering front fork suspensions in 2001. Fox entered the ATV and other off-road markets in the mid-1990s.

We purchased a majority interest in Fox on January 4, 2008.

Industry

Fox provides suspension products for mountain biking and powered vehicles, such as, snowmobiles, all-terrain/utility vehicles, motorcycling/motocross and off-road/specialty vehicles. Over the last three fiscal years mountain biking has represented approximately 67%, 69% and 75%, of Fox s gross sales and powered vehicles have represented the remainder of gross sales. Fox has focused on the performance and racing segments of the markets noted below, which are considerably smaller than the entire markets.

Mountain Biking In 2011, the North American bike market generated over $6.0 billion of sales according to the National Bicycle Dealers Association. Mountain bike related sales accounted for approximately 23% of this total according to U.S. Department of Commerce statistics, Gluskin Townley Estimates. These sales were primarily conducted through three channels: mass merchants, chain sporting goods and Independent Bike Dealers (IBDs). These channels are differentiated by the price, quality and selection of the mountain bikes they offer, with the IBD segment, in which Fox competes, consisting of premium priced and highly technical performance bikes.

Mountain biking enthusiasts typically have strong preferences concerning not only the OEM brand but also for the components used by OEM manufacturers. Shocks, forks, wheels and drive-trains strongly influence customers buying decisions. OEMs have formed partnerships with premium component manufacturers having strong brands in order to generate increased sales of their fully assembled bikes. Fox s components are generally selected by OEMs participating in the IBD segment and by Aftermarket consumers seeking increased performance characteristics which is a small portion of the total market

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Snowmobiles In 2011, management estimates that the North American market for new snowmobiles was $1.4 billion. Snowmobiling can be segmented into the following categories: performance/crossover snowmobiles used for a variety of activities including racing; touring/utility snowmobiles that are more comfortable and often seat two people; mountain snowmobiles that are performance-oriented, focusing on vertical geography; trail snowmobiles that are primarily used for riding groomed and un-groomed trails; and youth snowmobiles. Fox provides suspension products in each of these categories.

As a way to stimulate demand for new snowmobiles and entice customers to purchase more premium priced snowmobiles, OEMs will select Fox shocks. Additionally, OEMs offer the Fox s shock absorbers as upgrades on less expensive models. Aftermarket customers will select Fox components for increased performance characteristics.

All-Terrain Vehicles In 2011, the North American ATV market was $2.6 billion according to management s estimates. The market for all-terrain vehicles (ATVs) and utility vehicles can be divided into four segments: Recreation/Utility ATVs that are primarily used for trail riding, hunting and farming; Sport ATVs that are high performance, two-wheel drive machines used for racing and aggressive trail riding; Youth ATVs; and Side-by-Side ATVs. Fox develops and sells shocks into the performance and racing sport, youth and side-by-side sub-segments of the ATV market.

Similar to the snowmobile industry, OEMs will stimulate demand for new ATVs and entice customers to purchase more premium priced ATVs by selecting Fox s shocks for their premium models. Additionally, OEMs offer the company s shock absorbers as upgrades on less expensive models. Aftermarket sales are comprised of customers seeking enhanced performance characteristics.

Motorcycles/Motocross In 2011, the North American sales of motorcycles was $4.5 billion according to management estimates. The motorcycle market consists of all classes of on-road and off-road motorcycles. There are three main categories: On-highway motorcycles that are primarily used on paved roads; Dual motorcycles that are used for both on and off-road activities; and Off-highway motorcycles that are only certified for off-road use. The Off-road category is further segmented into motocross, off-road which includes youth motocross and youth off-road. Currently, OEM needs for suspension products are largely filled by captive suppliers in this category. As such, Fox has focused on the Aftermarket performance racing segments which is considerably smaller than entire motorcycle market. Aftermarket sales are comprised of customers seeking enhanced performance characteristics.

Off-Road Vehicles In 2011, the North American retail sales of specialty automotive products were $30 billion according to the Specialty Equipment Market Association. Off-road vehicles can be divided into five segments: off-road trucks, buggies, sand buggies, rock crawlers and lifted trucks. Consumers in the truck, buggy, sand buggy and rock crawler categories range from serious racers and enthusiasts to individuals involved primarily in recreational activities. The lifted truck segment, which consists of vehicles that in many cases never leave the highway, is divided generally by price point. Fox s products target the high-end price point for each of these five segments. Off-road vehicles are generally customized vehicles with Aftermarket components unlike OEM vehicles although some OEM manufacturers are offering limited edition vehicles. Fox primarily sells to Aftermarket consumers seeking increased performance characteristics but has begun some limited sales to OEM manufacturers. FOX also provides suspension to the U.S. Government either directly or through tier one manufacturers.

Products and Services

Fox designs and manufactures suspension products that dissipate the energy and force generated by various ride sport activities. A suspension product allows wheels to move up and down to absorb bumps and shocks while keeping the tires in contact with the ground for better control. Fox s products use adjustable suspension, progressive spring rates, and low weight combined with structural rigidity. Fox suspension products improve user control for greater performance while maximizing comfort levels.

Each suspension product built at Fox s manufacturing facilities is assembled according to precise specifications at multiple stages throughout the assembly process to ensure consistently high performance levels and customer satisfaction. Finished parts are built in multiple assembly cells and on an assembly line using precise tooling to ensure manufacturing consistency and product functionality. Fox has developed a number of highly sophisticated assembly machines to ensure consistent high quality.

Competitive Strengths

Proprietary Engineering Expertise Fox maintains a broad base of technical innovation and design that has been developed over the past 38 years. Fox s technical expertise enables the development and production of some of the most advanced suspension products available in the market. With its history of innovation and design, Fox has created a deep portfolio of key intellectual property related to suspension technology and applications.

Highly Recognizable Brand Driven by a long history of innovation, Fox has created a highly respected and well-known brand for advanced suspension products. A product branded with the FOX logo represents the highest level of technical performance for enthusiasts and professionals who require suspension systems capable of handling demanding conditions. The FOX logo is prominently displayed on all of Fox s products and provides a halo effect for complementary products.

Strong Blue-Chip Customer Relationships Given the long history of performance for Fox s suspension products, OEM customers seeking the highest level of quality and technical features for suspension have developed strong long-term relationships with the company.

Business Strategies

Expand Revenues from Powered Vehicles Business Fox s focus on developing premier suspension technologies continues to create complementary opportunities across this segment.

Continue to Expand Aftermarket Sales The sale of Aftermarket parts typically carries higher gross margins than a similar OEM sale. Fox is further investing in its Aftermarket sales infrastructure to foster sales growth in 2013 and beyond. One of the simplest and most effective ways for customers to improve their performance is the purchase and installation of an aftermarket Fox suspension product when compared to the expense of purchasing an entirely new platform.

International Growth Due to the successful efforts of Fox s operations teams, distribution to foreign OEMs and distributors is well-established. By selectively increasing infrastructure and honing its focus on identified opportunities, Fox plans to continue its international sales growth. Further, management plans include investigation of other international market opportunities, such as Asian and South American markets. International sales aggregated $149.6 million, $129.9 million and $113.6 million in fiscal 2012, 2011 and 2010, respectively.

Pursue New Market Trends and Opportunities New trends in action sports can lead to significant market opportunities. Fox s close association with racing and its professionals allows it to see new trends as they emerge. Depending on the trend, Fox will develop new products that address these needs.

Fox established a manufacturing operation in Taiwan during 2012 and intends to capitalize on new opportunities in Taiwan, as many of Fox s customers are in Asia.

Research and Development

We believe Fox s products are among the most technically advanced and rigorously engineered in their markets. They are specifically designed to function and perform under diverse and extreme conditions. Fox s research and development effort is at the core of its strategy of product innovation and market leadership. Fox s products feature a combination of innovative design, high-quality materials, and superb functionality and are recognized as being the leaders or among the leaders in all of the market segments in which they participate.

Fox has a robust core research and development team, which has a significant amount of industry experience. In addition to the core engineering group, a large number of other Fox staff members, who also use the company s products, contribute to the research and development effort at various stages. This may take the form of initial brainstorming sessions or ride testing products in development. Product development also includes collaborating with customers, field testing by sponsored race teams and working with grass roots riders. This feedback helps ensure products will meet the company s demanding standards of excellence as well as the constantly changing needs of professional and recreational end users.

Fox s research and development activities are supported by state-of-the-art engineering software design tools, integrated manufacturing facilities and a performance testing center equipped to ensure product safety, durability and superior performance. The testing center collects data and tests products prior to and after commercial introduction. Suspension products undergo a variety of rigorous performance and accelerated life tests. The research and development portion of our total engineering costs totaled $5.7 million, $5.1 million and $4.2 million in each of the years 2012, 2011 and 2010, respectively.

Customers

Fox s reputation for product quality, durability and technical excellence has resulted in a customer base that includes some of the world s leading OEMs and a loyal following of knowledgeable and experienced end users. Fox s OEM customers are market leaders in their respective categories, and help define, as well as respond to, consumer trends in their respective industries. These customers provide exceptional market support for Fox by including the company s products on their highest-performing models. OEMs will often use Fox s components to improve the marketability and demand of their own products.

Fox sells to over 175 OEM customers and over 7,800 Aftermarket customers across its market segments. One customer accounted for approximately 7.0%, 8.1% and 11.0% of net sales for the years ended December 31, 2012, 2011 and 2010, respectively. Fox s top 10 customers accounted for approximately 51.1%, 51.6% and 53.2% of net sales in 2012, 2011 and 2010, respectively. International sales totaled $149.6 million, $129.9 million and $113.6 million in each of the years 2012, 2011 and 2010, respectively. Sales attributable to countries outside the United States are based on shipment location. The international sales amounts provided do not necessarily reflect the end customer location as many of our products are assembled at international locations with the ultimate customer located in the United States.

Sales and Marketing

Fox employs a number of dedicated sales professionals. Each sales person is fully dedicated to servicing either OEM or Aftermarket customers ensuring that Fox s customers receive only the most capable person to address their unique needs. Fox strongly believes that providing the best service to its end customers is essential in maintaining its reputational excellence in the marketplace. The sales force receives training on the latest Fox products and technologies in addition to attending trade shows to increase its market knowledge.

The primary goal of the marketing program is to strengthen and promote the FOX brand in the marketplace. Fox increases brand awareness and equity with through a number of marketing channels including: advertisements in publications and websites; team and individual sponsorships; support and promotion at outdoor events; trade shows; website development; and dealer support.

Fox s business is somewhat seasonal. Historically, net sales and earnings are highest during the third quarter. We believe this seasonality is due to delivery of new products containing our shocks related to the new bike season.

Fox had approximately $43.0 million and $37.0 million in firm backlog orders at December 31, 2012 and 2011, respectively.

Competition

Competition in the high-end performance segment of the suspension market revolves around technical features, performance and durability, customer service, price and reliable order execution. While price is a factor in all purchasing decisions, we believe customers consider Fox s products to be an outstanding value proposition given their significant performance and other attributes.

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Fox competes with several large suspension providers as well as numerous small manufacturers who provide branded and unbranded products. These competitors can be segmented into the following categories:

Mountain Biking Fox competes with several companies that manufacture front and rear mountain bike suspension products. Management believes these include RockShox (a subsidiary of SRAM Corporation), Tenneco Marzocchi S.r.l. (a subsidiary of Tenneco Inc.), Manitou (a subsidiary of HB Performance Systems), SR Suntour and DT Swiss (a subsidiary of Vereinigte Drahtwerke AG).

Snowmobiles Within the snowmobile market, Management believes its main competitor is KYB (Kayaba Industry Co., Ltd.). Other suppliers include Öhlins Racing AB, Walker Evans Racing, Works Performance Products and Penske Racing Shocks / Custom Axis, Inc.

All-Terrain Vehicles A large percentage of the shocks supplied to OEM ATV manufacturers are the result of either long-term supplier relationships or captive business units associated with a specific OEM. Alternatively, ATV manufacturers source suspensions from a variety of suspension manufacturers depending on the final application and performance requirements.

Fox s management believes its primary competitor outside of captive OEM suppliers is ZF Sachs (ZF Friedrichshafen AG) and Walker Evans Racing. Aftermarket shocks are available from large OEMs plus a number of primarily Aftermarket suppliers including Elka Suspension Inc., Öhlins Racing AB, Works Performance Products and Penske Racing Shocks / Custom Axis, Inc.

Off-Road Vehicles Within the off-road vehicle category, Fox competes with both branded and unbranded competitors. The two largest competitors to Fox in management s opinion are ThyssenKrupp Bilstein Suspension GmbH (Bilstein) and King Shock Technology, Inc. (King Shock). Other competitors include Icon Vehicle Dynamics, Sway-A-Way, Pro Comp Suspension and Rancho (Tenneco).

Suppliers

Fox works closely with its supply base, and depends upon certain suppliers to provide raw inputs, such as forgings and castings and molded polymers that have been optimized for weight, structural integrity, wear and cost. Fox typically has no firm contractual sourcing agreements with these suppliers other than purchase orders.

Depending on component requirements, raw material inputs go through a combination of machining processes including computer numeric control machines, drill stations and lathes. Fox utilizes manufacturing models and workflow analysis tools to minimize bottlenecks and maximize capital asset utilization. After initial machining, components are then outsourced to specialized manufacturers for plating, grinding, anodizing and honing.

Fox s primary raw materials used in production are aluminum and magnesium. Fox uses multiple suppliers for these raw materials and believes that these raw materials are in adequate supply and are available from many suppliers at competitive prices. Prices for these materials have been increasing but the company is implementing sourcing strategies and value engineering initiatives to offset them.

Intellectual Property

Fox relies upon a combination of patents, trademarks, trade names, licensing arrangements, trade secrets, know-how and proprietary technology in order to secure and protect its intellectual property rights.

Fox s in-house intellectual property department and in-house counsel diligently protect its new technologies with patents and trademarks and vigorously defend against patent infringement lawsuits. Fox currently owns 31 patents on proprietary technologies for shock absorbers and front fork suspension products and has an additional 78 patent pending applications at the U.S. and European Patent Offices. Fox s patent portfolio makes it an impediment to competitors to introduce products with comparable features.

Regulatory Environment

Fox s manufacturing and assembly operations, its facilities and operations are subject to evolving federal, state and local environmental and occupational health and safety laws and regulations. These include laws and regulations governing air emissions, wastewater discharge and the storage and handling of chemicals and hazardous substances. Management believes that Fox is in compliance, in all material respects, with applicable environmental and occupational health and safety laws and regulations. New requirements, more stringent application of existing requirements, or discovery of previously unknown environmental conditions could result in material environmental expenditures in the future.

Additionally, Fox is subject to the jurisdiction of the United States Consumer Product Safety Commission (CPSC) and other federal, state and foreign regulatory bodies. Under CPSC regulations, a manufacturer of consumer goods is obligated to notify the CPSC, if, among other things, the manufacturer becomes aware that one of its products has a defect that could create a substantial risk of injury. If the manufacturer has not already undertaken to do so, the CPSC may require a manufacturer to recall a product, which may involve product repair, replacement or refund. Fox has never had any of its products recalled.

Employees

As of December 31, 2012, Fox employed approximately 534 persons. None of Fox s employees are subject to collective bargaining agreements. We believe that Fox s relationship with its employees is good.

Liberty Safe

Overview

Liberty Safe, headquartered in Payson, Utah and founded in 1988, is the premier designer, manufacturer and marketer of home, gun and office safes in North America. From its over 204,000 square foot manufacturing facility, Liberty Safe produces a wide range of home, office and gun safe models in a broad assortment of sizes, features and styles ranging from an entry level product to good, better and best products. Products are marketed under the Liberty Safe brand, as well as a portfolio of licensed and private label brands, including Remington, Cabela s and John Deere. Liberty Safe s products are the market share leader and are sold through an independent dealer network (Dealer sales) in addition to various sporting goods and home improvement retail outlets (Non-Dealer sales or National sales). Liberty Safe has the largest independent dealer network in the industry.

Approximately 60% of Liberty Safe s sales are Non-Dealer sales and 40% are Dealer sales.

For the fiscal years ended December 31, 2012, 2011 and 2010, Liberty Safe had net sales of approximately $91.6 million, $82.2 million and $49.0 million (from its acquisition date), respectively, and operating income of $6.0 million, $4.3 million in the years ended December 31, 2012 and 2011 respectively, and an operating loss of $0.8 million in 2010. Liberty Safe had total assets of $82.4 million, $85.9 million and $83.3 million at December 31, 2012, 2011 and 2010, respectively. Net sales from Liberty Safe represented 10.4%, 13.6% and 9.7% of our consolidated net sales for the year ended December 31, 2012, 2011 and 2010 (from acquisition date), respectively.

History of Liberty Safe

The Liberty Safe brand and its leading market share has been built over a 24 year history of superior product quality, engineering and design innovation, and leading customer service and sales support. Liberty Safe has a long history of continuous improvement and innovative approaches to sales and marketing, product development and manufacturing processes. Significant investments over the last five years have solidified Liberty Safe s reputation for providing substantial value to retailers and enhanced its long-standing position as the leading producer of premium home, office and gun safes.

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Liberty Safe started operations in 1988 and throughout 1991 and 1992, increased its distribution capabilities, establishing a regional sales force model to better serve the Dealer channel. This expanded sales coverage gave Liberty Safe the needed organizational structure to provide ready support and products nationwide, helping to establish its reputation for service to its customers. On the strength of its growing reputation and national sales presence, Liberty Safe achieved the status of the #1 selling safe company in America in 1994, according to Sargent and Greenleaf data, the major lock supplier to the industry, a position that it has maintained to this day. In 2001, Liberty Safe opened its current 204,000 square foot state-of-the-art facility in Payson, UT and consolidated all of its manufacturing and distribution operations to a centralized location. As the only facility in the industry utilizing significant automation and a streamlined roll-form manufacturing process, it represented a significant step forward when compared to the production capabilities of its competitors. Incremental investments following the consolidation have solidified Liberty Safe s position as the pre-eminent low-cost and most efficient domestic manufacturer.

Beginning in 2007, Liberty Safe reorganized its manufacturing process, retooled its product line for increased standardization throughout the production process and realigned employee incentives to increase labor efficiency. These improvements enabled Liberty Safe to shift from build-to-stock production to build-to-order with shorter lead time requirements, greater labor efficiency and reduced working capital.

During 2011 Liberty Safe constructed a new production line that has allowed Liberty to build entry level safe products in- house. This product was previously sourced from an Asian manufacturer. The production line began operations in February 2012 and Liberty is currently manufacturing two different models of safes on this line which translates into five new SKUs. Liberty invested over $9.0 million to build the line. This investment in production capacity now makes Liberty Safe the largest manufacturer of home, office and gun safes in the world. This added investment in capacity in the U.S. will allow Liberty Safe to provide shorter lead times and competitive pricing to its North American customer base. This will allow Liberty safe to capture additional market share, growing its revenue base and adding more margin dollars to the bottom line. In addition, Liberty Safe will be able to reduce its investment in inventory by no longer having to rely upon long lead times and the inaccuracies of forecasting.

We purchased a majority interest in Liberty Safe on March 31, 2010.

Industry

Liberty Safe competes in the broadly defined North American safe industry which includes fire and document safes, media and data safes, depository safes, gun safes and cabinets, home safes and hotel safes. According to Global Industry Analysts, (GIA) March 2008 report, the global safe industry was estimated to be approximately $2.9 billion of wholesale sales in 2008, and grew consistently at an estimated CAGR of 4.3% from 2000 to 2009. Consistent growth has been one of the defining characteristics of this industry, and GIA anticipates it will continue at a rate of 4.4% from 2009 through 2015.

Products & Services

Liberty Safe offers home, office and gun safes with minimum retail prices ranging from $400 to $8,000.

Liberty Safe produces 39 home and gun safe models with the most varied assortment of sizes, feature upgrades, accessories and styling options in the industry. Liberty Safe s premium home and gun safe product line covers sizes from 12 cu. ft. to 50 cu. ft. with smaller sizes available for its personal home safe. Liberty Safe markets its products under Company-owned brands and a portfolio of licensed and private label brands, including Remington, Cabela s, John Deere and others. Liberty Safe also sells commercial safes, vault doors and a number of accessories and options. The overwhelming majority of revenue is derived from the sales of safes.

Competitive Strengths

#1 Premium Home and Gun Safe Brand with Strong Momentum in the Market Liberty Safe achieved the status of #1 selling safe company in America in 1994 (per statistics provided by Sargent & Greenleaf, the primary lock supplier to the industry) and maintains this prominent position today. The market for premium home and gun safes is highly fragmented, and management estimates that Liberty Safe s net sales are over twice those of its next largest competitor in the category. Liberty Safe continues to gain market share from the various smaller participants who lack the distribution and sales and marketing capabilities of Liberty Safe.

State-of-the-Art and Scalable Operations Over the past five years, management has constructed a highly scalable operational platform and infrastructure that has positioned Liberty Safe for substantial sales growth and enhanced profitability in the coming years. Under current ownership, the company has transitioned itself from a manufacturing oriented operating culture to a demand-based, sales-oriented organization. The company s strategic transition required the implementation of a demand-based sales and operating platform, which included (i) new equipment to drive automation and capacity improvements; (ii) reengineered product lines and production processes to drive efficiency through greater standardization in production; and (iii) new employee incentives tied to labor efficiency, which has improved worker performance as well as employee attitude. These initiatives are enhanced by an experienced senior executive team, a balanced sourcing and in-house manufacturing production strategy, advanced distribution capabilities and sophisticated IT systems. Liberty has combined its demand-based sales and operating initiatives with upgraded production equipment to drive multiple operational improvements. Since 2007, the company has reduced its lead times from 4 6 weeks to approximately seven days. These shorter production cycles coupled with better demand forecasting have significantly reduced working capital needs for the business by reducing domestic inventory from approximately 7,000 units to 3,000 units since 2007. Improved automation and workflow organization have decreased labor hours over 20% per safe from 8.3 in 2005 to 6.3 in 2012 for rolled steel safes. These recent initiatives combined with the company s cumulative historical investments in operational capabilities have created a lasting competitive advantage over its smaller competitors, who utilize labor-intensive operations and lack the company s lean manufacturing culture.

Historically, Liberty Safe maintained an optimal mix of in-house and Asian-sourced manufacturing in order to improve its ability to meet customer inventory needs. Beginning in 2012 Liberty Safe began manufacturing entry level safes that were previously sourced from an Asian manufacturer, on its new production line. As a result, over 90% of Liberty Safe products will now be made in the U.S. The average labor hours per entry level safe on this new production line is two hours. The increased capacity also positions Liberty Safe to grow its revenue base by more than was otherwise possible and profit from the product produced when compared to the all-in cost of the Asian sourced product.

The company has leased for the past ten years a manufacturing and distribution facility in Payson, Utah that represents the most scalable domestic facility in the industry. The company s multi-faceted production capabilities allow for substantial flexibility and scalable capacity, thus assuring a level of supply chain execution far superior to any of its competitors.

Reputation for High Quality Products Liberty Safe is passionate about offering only the highest quality products on a consistent basis, which over the years has gained it an enviable reputation and a key point of differentiation from its competitors. Liberty Safe distinguishes its products through tested security and fire protection features and industry leading design focused on functionality and aesthetics. The design of its safes meet rigorous internal benchmarks for security and fire protection, with most receiving certification from Underwriters Laboratory, Inc. (UL), the leading product safety standard certification, for its security capabilities. Additionally, Liberty Safe s investment in accessories and feature options have made Liberty safes the most visually appealing and functional in the industry, while providing more customized solutions for retailers and consumers.

Trusted Supplier to National Retailer and Dealer Accounts Liberty Safe s comprehensive, high-quality product offering and sophisticated sales and marketing programs have made it a critical supplier to a diverse group of national accounts and dealers. Initially a key supplier primarily to the dealer channel, it has expanded its business with national accounts, such as Gander Mountain, Cabela s and Lowe s. Liberty Safe provides a superior value proposition as a supplier for its national retailers and dealers via its well-recognized brands, lifetime product warranty, tailored merchandising, category management solutions and superior supply chain execution. Further, Liberty Safe s products generate more profitable floor-space, with both high absolute gross profit and retail margins over 30%. High retail profitability plus increased inventory turns has entrenched Liberty Safe as a key partner in customers success in the safe category. As a core element of building its relationships, Liberty Safe has invested significantly in making its retailers better salespeople through a proprietary suite of training tools, including in-store training, new product demonstrations, online education programs and sales strategy literature.

Business Strategies

Liberty has experienced strong historical growth while executing on multiple new sales and operational initiatives, positioning it to continue to increase its scale and improve profitability. Liberty s growth strategy is rooted in the sales and marketing and operational initiatives that have spurred its expansion into new accounts and increased penetration of existing accounts. Liberty has significant opportunity in its existing channels to continue to build upon its already strong market share. In addition to growth within its current channels, Liberty s core competencies can be successfully applied to ventures in the broader security equipment market. Liberty has explored certain of these opportunities, but due to the prioritization of operational initiatives and expansion opportunities within existing channels, they have not been aggressively pursued. Potential near-to-medium term areas for expansion of Liberty s platform include:

Expand Liberty s product line into the broader home and office safe market through current customers or new distribution strategies;

Enter the military secure enclosures market;

Further develop international distribution by entering new countries and expanding current limited presence in Canada, Mexico and Europe;

Enter the residential security market through a strategic partnership with a provider of residential security service solutions to provide a more complete physical and electronic security solution; and

Acquire businesses within the premium home and gun safe industry and/or leverage Liberty s platform into new products or channels

Offer additional accessory products to existing distribution networks

Customers

Liberty Safe prides itself on its ability to provide high-quality, innovative products and industry-leading customer service. As a result, it has fostered long-term relationships with leading national retailers (National or Non-Dealer) as well as numerous Dealers, enabling Liberty Safe to achieve considerable brand awareness and channel exposure. Traditionally, the Dealer channel has accounted for the majority of the Liberty Safe s net sales, but through significant investment in its national accounts sales and marketing efforts, Liberty Safe has also become the leading supplier to National accounts. Expansion into National accounts is part of Liberty Safe s strategy to reach a broader customer base and more varied demographics. National account customers include sporting goods retailers, farm & fleet retailers, home improvement retailers and club retailers. As of December 31, 2012, 2011 and 2010, Liberty Safe had 16, 16 and 22 National account customers, respectively, that are estimated to have accounted for approximately 57% of net sales.

Dealer customers include local hunting and fishing stores, hardware stores and numerous other local, independent store models. As of December 31, 2012, 2011 and 2010, there were 343, 325 and 322 Dealers that accounted for 43%, 39% and 38% of net sales, respectively.

Cabela s, Liberty Safe s largest customer accounted for approximately 15.0%, 13.2% and 15.2% of net sales in 2012, 2011 and 2010, respectively.

Sales & Marketing

Liberty Safe possesses robust sales and marketing capabilities in the safe industry. Liberty Safe utilizes separate sales teams for National accounts and Dealers, which enables it to provide more focused and effective strategies to manage and develop relationships within different channels. Liberty Safe has made significant recent investments in the development of a comprehensive sales and marketing program including merchandising, sales training and tools, promotions and supply chain management. Through these various initiatives, Liberty Safe offers highly adaptable programs to suit the varying needs of its retailers. This has enabled Liberty Safe to become a key supplier across diverse channels. Liberty Safe began advertising nationally on the Glen Beck show in the second half of 2010. This advertising has been highly successful and

Liberty has continued this advertising in 2011 and 2012.

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Liberty Safe s comprehensive service offering makes it uniquely suited to service national retailers in a variety of channels. Liberty Safe has designed a Store-within-a-Store program and a more comprehensive Safe Category Management program to build relationships and increase its importance to retailers. Primarily utilized with sporting goods retailers, the Store-within-a-Store concept successfully integrates the effective sales strategies of its dealers for selling a high-price point, niche product into a larger store format. Centered on communicating the benefits of its products to customers, the program enables retailers to more effectively up-sell customers through a good-better-best merchandising platform, increasing margin and inventory turns for its retailers. Liberty s Safe Category Management program builds on the Store-within-a-Store concept to provide greater sales and marketing control and more complete inventory management solutions. This program facilitates Liberty Safe becoming the sole supplier to retailers, providing large incremental expansion and stronger relationships at accounts. No other market participant has the capabilities to provide a comprehensive suite of customer service solutions to national retailers, such as customized SKU programs, a Store-within-a-Store program and a Safe Category Management program.

Competition

Liberty Safe is the premier brand in the premium home and gun safe industry, with an estimated 34% market share in the category, two times the next competitor. Liberty is in a class by itself when it comes to manufacturing technology and efficiency and supply chain capabilities. Competitors are generally more heavily focused on either smaller, sourced safes or large, domestically produced safes. Competitive domestic manufacturers run blacksmith type factories that are small, inefficient and require a tremendous amount of manual labor that produces inconsistent product. In addition, many of Liberty s competitors are directly tied to a third-party brand, such as Browning, Winchester or RedHead / Bass Pro.

Liberty competes with other safe manufacturers based on price, breadth of product line, technology, product supply chain capabilities and marketing capabilities.

Channel diversity in the premium home and gun safe industry is rare, with most companies having greater concentration in either the dealer channel or national accounts, but rarely having the supply chain capabilities or sales and marketing programs to service both channels effectively. Major competitors have limited sales and marketing departments and programs, making it difficult for them to expand sales and gain market share.

Suppliers

Liberty s primary raw materials are steel, sheetrock, wood, locks, handles and fabric, for which it receives multiple shipments per week. Materials, on average, account for approximately 65% of the total cost of a domestically produced safe, with steel accounting for approximately 55% of material costs. Liberty purchases its materials from a combination of domestic and foreign suppliers. Historically, Liberty Safe has been able to pass on raw material price increases to its customers.

Liberty purchased over 29 million pounds of steel in 2012 primarily from domestic suppliers, using contracts that lock in prices two to three quarters in advance. Liberty Safe purchases coiled and flat steel in gauges from four to 14. Liberty Safe specifies rigorous requirements related to surface and edge finish and grain direction. All steel products are checked to ASTM specification and dimensional tolerances before entering the production process.

Liberty Safe had approximately $13.2 million and $8.1 million in firm backlog orders at December 31, 2012 and 2011, respectively.

Intellectual Property

Liberty Safe relies upon a combination of patents and trademarks in order to secure and protect its intellectual property rights.

Liberty Safe currently owns 25 trademarks and 2 patents on proprietary technologies for safe products.

Research and Development

Liberty s approach to R&D and innovation drives customer satisfaction and differentiation from competitive products. Liberty is the engineering and design leader in its sector, due to a history of first-to-market features and standard-setting design improvements. The Company s proactive solicitation of feedback and constant interaction with consumers and retail customers across diverse channels and geographies enables the Company to stay at the forefront of customer demands. The Company s approach to product development increases the likelihood of market acceptance by creating products that are more relevant to consumers demands. Research and development costs were $0.8 million, $0.7 million and $0.1 million in 2012, 2011 and 2010, respectively.

The below charts represents some of the recent innovations in product design (and functionality) that have come about from the Company s dedication to R&D:

Product	Function / benefit
Cool Pocket	Keeps documents 50% cooler than rest of safe
Integrated lighting system	Automatic on/off interior lights
Palusol Heat activated door	Seal expands to 7 times its size in a fire
Liberty Tough Doors	Enhanced protection against side bolt prying
Marble gloss powder coat paint	Provides smooth glass finish
4-in-1 Flex storage system	Adjustable shelving configurations
Door panels	Pocket variety to store handguns and other items

In addition to product enhancements, new products, such as the *Fatboy® Series,* have been launched from Liberty s commitment to R&D.

Based on consumer feedback, Liberty saw demand for safes that were capable of holding more valuables within the safe but at a lower price point than Liberty s current large safe models. Within 3 months of conception, the Company introduced the successful *Fatboy®* series in February 2010. The *Fatboy®* and *Fatboy Jr.®* models, which are wider and deeper than traditional safes, were a natural complement to Liberty s current products, targeted at a specific customer need. The introduction and success of the *Fatboy®* series demonstrates Liberty s proven ability to recognize market opportunities, engineer a responsive product and execute market delivery. Beginning in 2012 Liberty Safe will introduce five new SKUs, manufactured on its new production line, with a unique locking system to service the entry level safe market.

Regulatory Environment

Liberty Safes management believes that Liberty Safe is in compliance, in all material respects, with applicable environmental and occupational health and safety laws and regulations.

Employees

Liberty Safe is led by a highly knowledgeable management team of sporting goods and consumer products industry veterans that possess a balanced combination of industry experience and functional expertise. The majority of the team members have worked together since 2000.

As of December 31, 2012, Liberty Safe had 342 full-time employees and 113 temporary employees. The Company s labor force is non-union. Management believes that Liberty Safe has an excellent relationship with its employees.

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Tridien

Overview

Tridien, headquartered in Coral Springs, Florida, is a leading designer and manufacturer of powered and non-powered medical therapeutic support surfaces and patient positioning devices serving the acute care, long-term care and home health care markets. Tridien is one of the nation s leading designers and manufacturers of specialty therapeutic support surfaces with manufacturing operations in multiple locations to better serve a national customer base.

Tridien, together with its subsidiary companies, provides customers the opportunity to source leading surface technologies from the designer and manufacturer.

Tridien develops products both independently and in partnership with large distribution intermediaries. Medical distribution companies then sell or rent the therapeutic support surfaces, sometimes in conjunction with bed frames and accessories to one of three end markets: (i) acute care, (ii) long term care and (iii) home health care. The level of sophistication largely varies for each product, as some patients require simple foam mattresses (non-powered support surfaces) while others may require electronically controlled, low air loss, lateral rotation, pulmonary therapy or alternating pressure surfaces (powered support surfaces). The design, engineering and manufacturing of all products are completed in-house (with the exception of a select group of products, which are manufactured in Taiwan) and are FDA compliant.

For the fiscal years ended December 31, 2012, 2011 and 2010, Tridien had net sales of approximately $55.9 million, $55.9 million and $61.1 million, and operating income of $3.7 million, $5.0 million and $8.0 million, respectively. Tridien had total assets of $44.5 million, $42.8 million and $44.2 million at December 31, 2012, 2011 and 2010, respectively. Net sales from Tridien represented 6.3%, 9.2% and 12.1% of our consolidated net sales for fiscal years 2012, 2011 and 2010, respectively.

History

Tridien was initially formed in February 2006 by CGI and Hollywood Capital, Inc., a private investment management firm led by Tridien s former Chief Executive Officer, to acquire AMF and SenTech, located in Corona, CA and Coral Springs, FL, respectively. AMF Support Surfaces, Inc. is a leading manufacturer of non-powered mattress systems, seating cushions and patient positioning devices. SenTech is a leading designer and manufacturer of advanced electronically controlled, powered, alternating pressure, pulmonary therapy, low air loss and lateral rotation specialty support surfaces for the wound care industry. Prior to its acquisition, SenTech had established a premium brand as a result of its proprietary technologies, in the less price sensitive therapeutic market while AMF competed primarily in the preventive care market.

On October 5, 2006, Tridien acquired the patient positioning device business of Anatomic Concepts. The acquired operations were merged into Tridien s operations. Anatomic is a leading supplier of operating suite patient positioning devices and support surfaces focused on the price sensitive long term care and home healthcare markets.

On June 27, 2007, Tridien purchased PrimaTech, a lower price-point distributor of powered medical support surfaces to the long term care and home healthcare markets. PrimaTech s products are predominately designed in the U.S. and manufactured pursuant to an exclusive manufacturing agreement with an FDA registered manufacturing partner located in Taiwan.

In October 2009, Tridien and Hollywood Capital, Inc. terminated their management services agreement which provided for, among other things, two principals of Hollywood Capital, Inc., resigning from their roles of Chief Executive Officer and Chief Financial Officer of Tridien. Upon termination of the agreement, Tridien appointed a new Chief Executive Officer and a new Chief Financial Officer.

We purchased a controlling interest in Tridien from CGI on August 1, 2006.

Industry

The medical support surfaces industry is fragmented and comprised of many small participants and niche manufacturers. Tridien s consolidation platform allows customers to source all leading support surface technologies for the acute care, long term care and home health care from a single source. Tridien is a vertically integrated

company with engineering, design and research, manufacturing and support performed in house to quickly bring new, innovative products and technologies to market while maintaining high quality standards in its manufacturing process.

Immobility caused by injury, old age, chronic illness or obesity is the main cause for the development of pressure ulcers. In these cases, the person lying in the same position for a long period of time puts pressure on the bony prominence of the body surface. This pressure, if continued for a sustained period, can close blood capillaries that provide oxygen and nutrition to the skin. Over a period of time, these cells deprived of oxygen, begin to break down and form sores. In addition to constant or excessive pressure, other contributing factors to the development of pressure ulcers include heat, moisture, friction and sheer, or pull on the skin due to the underlying fabric.

The prevalence rate of pressure ulcers in acute care facilities has been seen as high as 34%, with costs of treatment as high as $70,000 per ulcer, causing an estimated burden of an additional 22 million Medicare hospital days. Further it has been reported that another 2% to 28% of all nursing home patients suffer from pressure ulcers. We believe that providing the right therapeutic support surfaces is a necessary intervention for these ulcers. Management believes the need for medical support surfaces will continue to grow due to several favorable demographic and industry trends including the increasing incidence of obesity in the United States, increasing life expectancies and an increasing emphasis on prevention of pressure ulcers by hospitals and long term care facilities.

According to the Centers for Disease Control and Prevention, between the years 1980 and 2000, obesity rates more than doubled among adults in the United States. Studies have shown that this increase in obesity has been a key factor in rising medical costs over the last 15 years. According to one study done at Emory University, increases in obesity rates have accounted for 27% of the increase in health care spending between 1987 and 2001. As an individual s weight increases, so too does the probability that the individual will become immobile and, according to studies performed at the University of North Carolina, greater than 40% of obese adults aged 54 to 73 were at least partially immobile. As individuals become less mobile, they are more likely to require either preventative mattresses to better disperse weight and reduce pressure areas or therapeutic mattresses to shift weight and pressure. Similar to how obesity increases the occurrence of immobility, so too does an aging society. As life expectancy expands in the U.S. due to improved health care and nutrition, so too does the probability that an individual will be immobile for a portion of their lives. In addition, as individual s age, skin becomes more susceptible to breakdown increasing the likelihood of developing pressure ulcers.

Beyond favorable demographic trends, Tridien s management believes healthcare institutions are placing an increased emphasis on the prevention of pressure ulcers. According to Medicare guidelines, hospitals are no longer able to be reimbursed for the treatment of in-house acquired wounds, resulting in continued focus by hospitals in preventing and treating such wounds. The end result is that if an at-risk patient develops pressure ulcers while at the hospital; the hospital is required to bear the cost of healing. As a result of increasing litigation and the high cost of healing pressures ulcers, healthcare institutions are now focusing on using pressure relief equipment to reduce the incidence of in-house acquired pressure ulcers.

Products and Services

Specialty beds, mattress replacements and mattress overlays (i.e. therapeutic surfaces) are the primary products currently available for pressure relief and pressure reduction to treat and prevent decubitus ulcers. The market for specialty beds and therapeutic surfaces include the acute care centers, long-term care centers, nursing home centers and home healthcare settings. Medical therapeutic surfaces are designed to have preventative and/or therapeutic uses. The basic product categories are as follows:

Powered Support Surfaces: Mattresses which can be used for therapy or prevention and are typically manufactured using an electronic power source with air cylinders or a combination of air cylinders and foam and provide Alternating Pressure, Low Air Loss, or Lateral Rotation. Alternating Pressure Systems are designed to inflate alternate cylinders while contiguous cylinders deflate in an alternating pattern. The alternating inflation and deflation prevents sustained pressure on an area of skin by shifting pressure from one area to another. This type of therapy provides movement under the patient s skin to eliminate both excessive and constant pressure, the leading cause of pressure ulcers. The powered control unit provides automatic changes in the distribution of air pressure. Tridien s Alternating Pressure Systems in the SenTech line incorporate its intellectual property in the way these automatic changes take place. This patented technology allows for a more comfortable surface with aggressive therapeutic alternating pressure. Another typical type of powered surface is Lateral Rotation which can aid in laterally turning a patient to reduce risks associated with fluid building up in a patient s lungs. A feature often found in Powered Surfaces is Low Air Loss that allows air to flow from the mattress to address the moisture and temperature environment on the patient s skin, contributing factors to pressure ulcers. Tridien currently produces patented designs for the performance of both Alternating Pressure and Low Air Loss mattress systems which management believes provides the optimum healing therapy for the patient. Powered support surfaces are typically used in acute care settings and when more aggressive therapy is needed. Powered Support Surfaces represented approximately 18.7% of net sales in 2012 and 19.6% of net sales in 2011 and 2010.

Non-Powered Support Surfaces: Consists of mattresses which have no powered elements. Their support material can be composed of foam, air, water, gel or a combination of these. In the case of water, air or gel materials, they are held in place with containment bladders. Non-powered mattress replacement systems help redistribute a patient s body weight to lessen forces on pressure points by envelopment into the surface. These products address the excessive pressure under a patient, but do not address the constant pressure applied to an area. Non-powered surfaces are generally used for prevention rather than treatment and currently comprise the majority of support surfaces. Currently Tridien manufactures a broad range of non-powered mattress systems using air, foam and gel. Non-powered support surfaces represented 53.6%, 53.1% and 53.2% of net sales in each of the years ended December 31, 2012, 2011 and 2010, respectively.

Positioning devices: Positioning devices are used to position patients for procedures as well as to minimize the likelihood of developing a pressure ulcer during those procedures. Tridien offers a complete range of foam positioning devices. Patient positioning devices represented 27.7%, 27.3% and 25.6% of net sales in each of the years ended December 31, 2012, 2011 and 2010, respectively.

Competition

The competition in the medical support surfaces market is based predominantly on product performance, features, price and durability. Other factors may include the technological ability of a manufacturer to customize their product offering to meet the needs of large distributors. Tridien competes with manufacturers of varying sizes who then sell predominantly through distributors to the acute care, long term care and home health care markets. Specific competitors include, Span America and other smaller competitors. Tridien differentiates itself from these competitors based on its patented technologies, quality of the products it manufacturers as well as its design and engineering capabilities to produce a full spectrum of surfaces that provide the greatest therapeutic outcome for every price point. While many competitors specialize in the production of a single type of support surface, and often outsource certain manufacturing as skills required to develop and manufacture products vary by materials used, Tridien is able to offer its customers a full spectrum of support surfaces nationwide.

Span America Medical Systems (NASDAQ: SPAN): ($76 million in fiscal 2012 sales) Span America s medical division includes the sales of skin care products, bedside mats, and foam mattress overlays and replacement mattresses, including the PressureGuard therapeutic mattress, Span-Aid patient positioners (used to elevate and support body parts) and Dish pressure-relief seat cushions to aid wound healing. Span America reported that approximately 30% of their revenue in 2012 was attributed to their therapeutic support surface segment. Span America also supplies safety catheters and makes specialty packaging products for use in outdoor furniture.

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Business Strategies

Tridien s management is focused on strategies to grow revenues, improve operating efficiency and improving gross margins. Of particular note, Tridien has completed four acquisitions since its inception and has achieved numerous benefits to this consolidation within the support surfaces industry. The following is a discussion of these strategies:

Offer customers high quality, consistent product, on a national basis Products produced by Tridien and its competitors are typically bulky in nature and may not be conducive to shipping. Management believes that many of its competitors do not have the scale or resources required to produce support surfaces for national distributors and believes that customers value manufacturers with the scale and sophistication required to meet these needs. Tridien offers its customers the highest standards of quality through its robust Quality Management Systems. All Tridien facilities are ISO 13485 registered.

Leverage scale to provide industry leading research and development Medical therapeutic surfaces are becoming increasingly technologically advanced. Tridien s management believes that many smaller competitors do not have the resources required to effectively meet the changing needs of their customers and believes that increased scale and investments in engineering and technology will allow it to better serve its customers through industry leading research, technology and development.

Pursue cost savings through scale purchasing and operational improvements Many of the products used to manufacture medical support surfaces are standard in nature and management believes that increased scale achieved through acquisitions will allow it to benefit from lower cost of materials and therefore lower cost of sales.

Research and Development

Tridien develops surfaces both independently and in partnership with large distribution intermediaries. Initial steps of product development are typically made independently. Larger distribution market participants will typically require further product development testing to ensure mattress systems have the desired properties while smaller distributors will tend to buy more standardized products, especially on the non-powered products. Tridien has dedicated professionals, including individuals focused on process engineering, design engineering, and electrical engineering, working on the development of the company s next generation of therapeutic surfaces and is currently investing in its future focus of advanced wound care technologies.

Tridien is working to develop the next generation of products in surfaces. The new product development process often requires 2 to 6 months for prevention products and 12 to 24 months for treatment products, of research, engineering and testing cooperation. Tridien will provide technical support and repair services for its products as well, a differentiating characteristic valued by its customers. The expected increase in spending will allow Tridien to focus on the next generation products. During the years ended December 31, 2012, 2011 and 2010, Tridien incurred $2.1 million, $1.8 million and $1.3 million, respectively, in research and development costs.

Sales and Marketing