

A surreal image of a warehouse fire. In the background, a large fire burns through the structure, with thick black smoke billowing out. In the foreground, rows of laundry racks filled with various coats and shirts are visible. To the right, two large industrial washing machines stand. In the center, a wooden table with a metal frame is positioned. Two mice are present: one is perched on the edge of the table, and the other is on the floor nearby. The overall atmosphere is one of chaos and neglect.

*"Uniformly Bad Business Practices"*

/ STRONG SELL OPINION /

Cintas Corp. | NASDAQ:CTAS



SPRUCE POINT  
CAPITAL MANAGEMENT

INVESTMENT RESEARCH REPORT



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# Spruce Point's Success Shorting S&P 500 Companies

Quote From  
Ben Axler

*"Being an S&P 500 company is a validation of absolutely nothing, and can be a wasteland of corporate mediocrity. It affords investors zero protections against companies and their ability to scheme investors. Buyer beware!"*

|                    |   |    |    |    |
|--------------------|--|--|---|---|
| Index              | S&P 500  | S&P 500  | S&P 500   | S&P 500   |
| Report             | NYSE: CHD   <a href="#">9/5/19</a>   | NYSE: AME   <a href="#">11/14/14</a>   | NYSE: MTD   <a href="#">7/24/19</a>   | NYSE: AOS   <a href="#">5/16/19</a>   |
| Market Cap         | \$22.7 billion   | \$12.3 billion   | \$21.8 billion  | \$6.1 billion   |
| Company Promotion  | Best of breed roll-up acquiror of personal care and consumer products with the core Arm & Hammer brand providing a stable backbone to diversify into other products  | Best of breed roll-up in the test and measurement equipment space with world class EBITDA margins and an ability to never miss Wall St estimates through any economic cycle  | Best of breed weights, test and measurement equipment company with superior margins and an ability to never miss Wall St. EPS targets   | Leading maker of water heaters and treatment products, boilers, and air purifiers. Fast and sustainable growth in China, allowing for corporate gross margins in excess of industry peers   |
| Our Criticism      | New management has become more aggressive, using financial and accounting tactics to inflate the share price. The recent acquisition of FLAWLESS hair care was expensive and will disappoint investors. Governance lapses have allowed mgmt. to reap unjust bonuses based on non-cash gains. Shares at \$80 trade 8% above analyst targets | We argued AMETEK was not creating any value by delivering zero organic growth and that its financial statements showed signs of strain with aggressive accounting. We believed its premium valuation multiple could not be sustained as the quality of its acquisitions deteriorated | Excessive cost capitalization from a 12 year "Blue Ocean" ERP implementation. Unusual corporate structure that omits product level margin discussion. Closeness of mgmt with PwC its auditor. Financial strains being signaled and anomalies in China. Extreme valuation with price 14% over avg analyst price target | China capital expenditure anomalies, notably consistent mis-forecasting. Capex issues often linked to gross margin inflation. Excessive spending on a protracted ERP implementation also often linked to accounting and financial issues    |
| Successful Outcome | Within the first quarter after our report, CHD <a href="#">reported</a> disappointing Q3 sales results, cut its full year revenue guidance, and issued Q4 earnings at \$0.54, well below the \$0.62 expected. Management blamed higher sales and marketing expenses on FLAWLESS  | By early 2016, AMETEK began guiding down sales and earnings expectations for multiple quarters. Its <a href="#">CEO</a> and <a href="#">CFO</a> abruptly retired. Its share price fell nearly 20% from our initial report date   | <a href="#">Q2 2019</a> missed sales estimates by the widest margin in years, and initial 2020 guidance issued in <a href="#">Q3 2019</a> , missed estimates with lower sales and earnings growth. Management failed to address any of the issues identified by Spruce Point. The share price corrected by 22%        | AOS <a href="#">admitted</a> an undisclosed material supply chain partner following a report by firm J Capital. In <a href="#">Q2 2018</a> , AOS substantially revised guidance, showing weakness in China with sales projected down 16-17% |



# *Table of Contents*

|                          |  |
|--------------------------|--|
| <u><a href="#">1</a></u> | <b>Executive Summary</b>   |
| <u><a href="#">2</a></u> | <b>Evidence That Cintas' Fastest Growing Business, Fire Protection Services, Is Breaking The Law And Putting Lives At Risk</b> |
| <u><a href="#">3</a></u> | <b>Evidence of Mounting Financial Struggles In The Core Uniform Business Post G&amp;K Acquisition</b>                          |
| <u><a href="#">4</a></u> | <b>Dubious "Beat And Raise" Story Designed To Fool Computers, Not Spruce Point</b>   |
| <u><a href="#">5</a></u> | <b>Governance And Auditor Concerns</b>   |
| <u><a href="#">6</a></u> | <b>Valuation And Downside Case</b>   |



## *Executive Summary*



# *Spruce Point Estimates 60% – 75% Downside Risk (\$69 - \$107/sh) At Cintas Corp. (NYSE: CTAS)*

Based on a new public FOIA and our research, we believe Cintas' Fire Protection Services business has committed fraud and is causing a public safety hazard by having workers conduct fire and safety inspections without proper licenses or permits, and falsify inspections. We call on Cintas to conduct a review to assure stakeholders it's not a systemic issue placing Cintas in non-compliance with its credit agreement. Fire Protection is its fastest growing segment. Our research indicates that Cintas' has a poor reputation, and that new private equity and public money is entering the space, which will compress its growth and margins. In addition, we believe that Cintas is facing financial strain in its core uniform rental business from its 2017 levered acquisition of G&K for \$2.1bn. With sell-side analysts failing to acknowledge any of these problems, or conduct a nuanced valuation of its various business segments to reflect divergent growth and risk profiles, our variant view suggests 60%-75% downside.

**Core Uniform  
Business  
Under  
Pressure Post  
Levered \$2.1bn  
G&K  
Acquisition In  
2017**

## **We Believe Cintas Overpaid For G&K, Is Struggling To Integrate It, And Spinning A Weak “Beat And Raise” Story**

- To consolidate share and extract synergies, Cintas acquired G&K Services in 2017 for \$2.1bn with new debt. Based on proxy statement disclosures, Cintas paid an additional \$425m above its initial offer to acquire a business that was described to us as having a poor reputation
- Cintas touted a “Beat and Raise” story post acquisition, but based on our forensic review, it appears that Cintas may have suppressed G&K's sales, only to raise sales guidance by a similar amount to the sales that had been suppressed
- Even worse, evidence points to Cintas over-estimating expenses, only to roll-them back and claim outperformance. In addition, Cintas said one thing, but did another by subtly changing capital priorities (cutting capex, increasing share repurchases) in an effort to artificially grow EPS. For FY 2019, we estimate Cintas had no underlying outperformance relative to initial guidance
- There are classic signs of a mismanaged acquisition and financial stress post acquisition:
  - COO and 22yr Cintas veteran J Phillip Holloman “retired” in mid 2018
  - Post deal closing, receivables are growing at nearly 2.0x sales; DSOs are at record levels; inventory growth is diverging from sales growth. Cintas' credit facility size has increased 3x in size despite sales up only 40%
  - Working capital to sales and bad debt has exploded to 20% of sales and 4% of receivables, respectively: both metrics are higher than Cintas and G&K on a standalone pre-acquisition basis. Cintas has still failed to consolidate its national receivables collections practice, while scores of customers are complaining about billing practices
  - Cintas's leverage is higher than it appears with material cash that is restricted and trapped abroad. We observe the Company is becoming more dependent on short-term financing with commercial paper as cash collections worsens
  - Cintas recently sold a \$73m investment for a reported 35x return, yet won't disclose any details about the mysterious divestiture. The timing of the sale to generate cash is suspicious in context
  - Weakness in oil and gas is emerging. Cintas took on added exposure to this industry from acquiring G&K
- Based on our analysis, ex: G&K's financial contributions to Cintas, we find no underlying EBITDA margin improvement in the core Cintas business, and that earlier leverage benefits of EBITDA growing faster than revenues have evaporated



# *Spruce Point Estimates 60% – 75% Downside Risk At Cintas Corp. (NYSE: CTAS)*

## Investors Misunderstand The Risks Associated With Fraud Conducted At Cintas' Fast Growing Fire Protection Business



**Fastest  
Growing Fire  
Inspection  
Business  
Operating  
Fraudulently  
While Putting  
Lives At Risk;**

**Competition  
Rising**

- Recent changes in revenue disclosure reveal for the first time that Cintas' fastest organically growing business is fire inspection, which has grown at a 3 year CAGR of 14%, above the historical and projected industry growth rate of 8% as illustrated by National Fire Prevention Association
- Based on our research, the biggest fundamental challenge in the industry is a qualified labor shortage. Cintas has used an "affiliate network" to expand its reach, but this approach brings challenges such as monitoring the quality and capability of its workforce
- Using a Freedom of Information Act (FOIA) request, we find that Cintas was charged with fraudulent business practices. Upon a fire outbreak in Aurora, IL, it was determined that Cintas had 8 of 12 inspectors unlicensed and unfit to carry out inspection duties for the 22 properties within Aurora's jurisdiction. These inspectors were thus falsifying inspection records. Based on our research, we believe this may not be an isolated incident, and that Cintas may have breeched its credit agreement by incorrectly representing that it holds all the necessary licenses to conduct its business in compliance with the law
  - Cintas must conduct an independent and formal review to assure all its stakeholders that it is in compliance with all applicable laws, and holds all necessary permits when conducting life-critical inspection operations
- Cintas is also being sued in a wrongful death lawsuit for inaccurate inspections in a mining accident that was documented by the Mine Safety and Health Administration. Incidents such as this, while very unfortunate, add complex tail risks to its business
- Given lapses in judgement such as this, and based on industry conversations, it doesn't appear to be a secret in the industry that Cintas has a poor reputation. As a result, new money is flooding into the industry to disrupt Cintas' national market position
  - We find evidence that historical contracts that locked in customers for 3-5 years are being shortened to just 1 year, and that prices are compressing; both are negative outcomes for Cintas
- Fueled by cheap financing and the ability to leverage contractually mandated inspection revenues, private equity players are creating regional platform acquisition vehicles to seize market share from disgruntled Cintas customers. In addition, APi Group, a large national competitor was just acquired by a UK SPAC, and will be listed on the NYSE, giving it broader access to public capital to compete against Cintas



## Warning On Audit Partner And Management Extracting Unjust Compensation With Questionable Results



Governance  
Concerns  
Include  
Closeness of  
Management  
With The  
Auditor

Current Audit  
Partner Linked  
To Papa John  
Accounting  
Fiasco

- Spruce Point has various concerns about the Board including a lack a separation between its Chairman and CEO, Board and family relationships that are not independent, unjust compensation practices, and the closeness of Cintas with its auditor
- Ernst & Young has been Cintas' auditor since 1968. The engagement partner at Ernst & Young is Craig Andrew Marshall. Mr. Marshall is also the audit engagement partner at Papa John's International (Nasdaq: PZZA)
  - Papa John's dismissed Mr. Marshall and E&Y in 2018. Since hiring KPMG in early 2019, Papa John's disclosed a new material weaknesses of financial controls and reporting
  - Both Cintas' CFO J Michael Hansen and its VP/Treasurer Paul Adler both worked at Ernst & Young
  - Spruce Point believes it is time Cintas shareholders appoint a new auditor and fresh eyes to look at its accounting practices
- Cintas' just appointed Karen Carnahan to its Audit Committee. Cintas claims she is "independent", yet as a 30 year former Cintas veteran and Treasurer connected to CEO Farmer, we question why is she joining now in light of our views that Cintas is experiencing financial stress? Furthermore, we find that she serves as a Trustee of another Audit Director's company, and is likely paid; can she act independently?
- Cintas management, with the blessing of the Board, claimed great performance for the G&K deal. Special bonuses were awarded to executives for completing the deal, despite our evidence it has weakened the overall financial profile of Cintas
- Cintas' annual incentive plan is based on sales and EPS growth, along with non-financial goals. In 2019, 41.75% of CEO Farmer's bonus was tied to EPS performance, while for most other executives, it accounted for 50% of the bonus. Cintas conveniently achieved almost the maximum EPS target within one penny, and claims its \$7.60 EPS took into consideration various "one-time items". Yet, in FY 2019, Cintas adopted a new revenue recognition method that boosted pre-tax income by \$22.3m and Diluted EPS by \$0.15 cents. Why wasn't this considered a "one-time" or "extraordinary" boost to income?



## *Spruce Point Estimates 60% – 75% Downside Risk At Cintas Corp. (NYSE: CTAS)*

**Trading Near All-Time High Share Prices, Above Analyst Average Price Target, And With An Expanded Multiple, Owning Cintas Is A Poor Risk / Reward; Sell-side Valuation Models Fail To Appreciate The Various Growth Risk Profiles For Each of Cintas' Business Segments**



**60% - 75%  
Downside For  
A Sum-of-The-  
Parts  
Valuation of a  
Structurally  
Disliked And  
Misunderstood  
Company**

- Analysts and investors love Cintas for its consistent ability to grow earnings, while returning capital through share repurchases, and a modest dividend yield. The consensus view is that it can produce 5-6% organic sales growth and 10-11% EPS growth by using its market dominance in stable industries to satisfy customers
- As a result, analysts' reward Cintas with the highest multiple among its commercial and safety publicly traded peers. The average analyst price target is \$255 per share. Yet, at the current share price of \$259, there's 1% implied downside on valuation alone, and materially more downside based on increasing business pressures
- Our view of Cintas is markedly different from consensus and we believe:
  - There is a uniform displeasure with Cintas' billing practices, one-style approach to customers, and willingness to skirt the law with fraudulent business practices that place lives at risk
  - The G&K acquisition has worsened Cintas' overall financial profile through greater capital intensity, bloating of receivables and bad debts, and greater exposure to cyclical industries such as oil and gas
  - Cintas corporate governance is substandard for its size and position as an S&P 500 company. Notably the CEO/Chairman roles are not split, it allows pledging of stock by executives, and the Board is stacked with long-time allies of the CEO with business connections between Board members
  - As a result, the expansion of Cintas' valuation multiple over the past few years is unwarranted
- Analysts fail to critically evaluate each of Cintas' business lines and apply a proper valuation to reflect the different growth and risk profiles
- Despite trading a 4x sales and 18x EBITDA, not a single one of Cintas' business lines can be justified at this valuation by looking at recent acquisitions completed. Transaction values are closer to 1x - 2x of revenues. When summed together, the fair value of Cintas' business is \$69 - \$107, or 60% – 75% downside



# *Cintas Stakeholders Deserve A Full And Independent Review of Its Fire Inspection Business*

Cintas has a sordid history in dealing with labor unions, settling lawsuits related to employment discrimination, and environmental compliance. Spruce Point finds it particularly troubling that individuals at Cintas committed fraud by misrepresenting that 8 of 12 inspectors in Aurora, Illinois were certified to conduct fire inspections, which are critical to protecting the public. Cintas needs to conduct a fully independent, and audited review of its Fire Protection Services workforce to make sure it is conducting its business in compliance with the law. Innocent people should not be put at risk by unqualified inspectors hired by Cintas.

**The Public And Our Children**



**Our Brave Firefighters**



**Unions And Employees**



**Shareholders**

**BlackRock®**

**Wall St Analysts**



**Banks**

**KeyBank** 

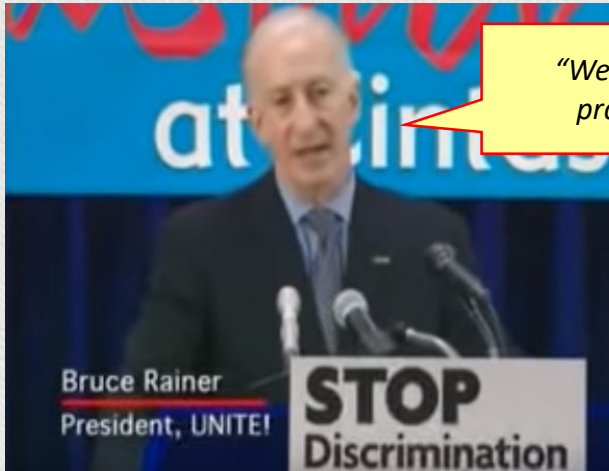
  
**FIFTH THIRD BANK**

  
**Vanguard®**

  
**Fidelity**  
INVESTMENTS®



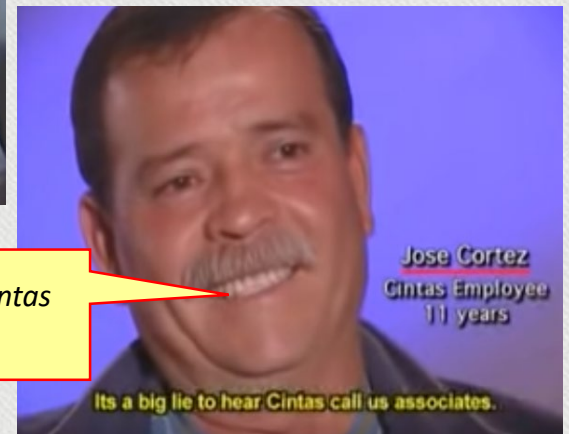
# Food For Thought: Does History At Cintas Repeat?



*"We found a company that has a practice of breaking the law."*



*"They treat you like garbage."*



*"It's a big lie to hear Cintas call us associates."*





*Evidence That Cintas' Fast Growing  
Fire Protection Business Is Breaking  
The Law, Putting Lives At Risk*



# Cintas Fastest Growing Organic Revenues Are From Fire Protection Services

Starting in FY 2019, Cintas started to break out revenues in its “Other” segment between Fire Protection and Uniform Direct sales. We can now observe that Fire Protection has been its fastest growing business line, with double digit organic growth.

| \$ in mm                        | FY 2017        | FY 2018        | FY 2019        | 3-Year CAGR  | Q1 2019       | Q1 2020        | YoY Growth   |
|---------------------------------|----------------|----------------|----------------|--------------|---------------|----------------|--------------|
| Uniform Rental and Facility     | \$4,202.5      | \$5,247.1      | \$5,552.4      | 6.6% (1)     | \$1,374.9     | \$1,454.5      | 5.8%         |
| First Aid and Safety Services   | \$508.2        | \$564.7        | \$619.5        | 10.4%        | \$153.4       | \$172.1        | 12.2%        |
| <b>Fire Protection Services</b> | <b>\$311.4</b> | <b>\$350.0</b> | <b>\$405.5</b> | <b>14.1%</b> | <b>\$98.1</b> | <b>\$110.1</b> | <b>12.2%</b> |
| Uniform Direct                  | \$301.2        | \$314.8        | \$314.9        | 2.3%         | \$71.5        | \$74.4         | 4.0%         |

Cintas growth has generally outperformed the U.S. Fire Safety market. However, NFPA projects the market growth at 8%, and Spruce Point believes Cintas’ period of double digit growth will moderate.

## U.S. Fire Safety Market (\$ billion)

2018-2025E CAGR: +8%



Source: Cintas FY 2019 [10-K](#) and Q1 2019 [10-Q](#)

And National Fire Prevention Association (“NFPA”)

1) G&K acquired in 2017. Based on average organic growth



# Growth Coming At The Expense Of Losing Control Over The Services Providers?

In FY 2016, Cintas started an “Affiliate Network” to recruit other business owners to provide fire safety services. Affiliates are essentially independent contractors, must provide a W-9 Form, and allow Cintas to lower its employment costs. The affiliate application requires applicants to provide a copy of the “*State Contractors License and all required licenses*”. On the surface, it seems like Cintas has a legitimate concern for recruiting the appropriate workers to extend its business. However, what’s happening in practice in the field paints an entirely different story.....

## Was The “Affiliate” Program Started In Response To A Dept of Labor Investigation About Underpaying Fire Protection Employees?

### Cintas Subsidiary Agrees To Pay Workers \$1.3 Million In Overtime Case

**Jan 19, 2017:** The U.S. Department of Labor announced today that a subsidiary of Cintas Corp. has paid \$1.3 million to compensate 81 fire sprinkler testers and installers for allegedly unpaid overtime. Cintas, based in Cincinnati, provides work products and services, including uniforms. The wage case investigated by the Labor Department concerned overtime pay for workers based in the San Jose office of the company's Cintas Fire Protection Services subsidiary. The department concluded that the company failed to pay the sprinkler workers the overtime due for an average of three hours per week spent on off-site tasks such as completing reports, sending emails and filling out time sheets, according to Deputy District Director Michael Eastwood.. ([Source](#))

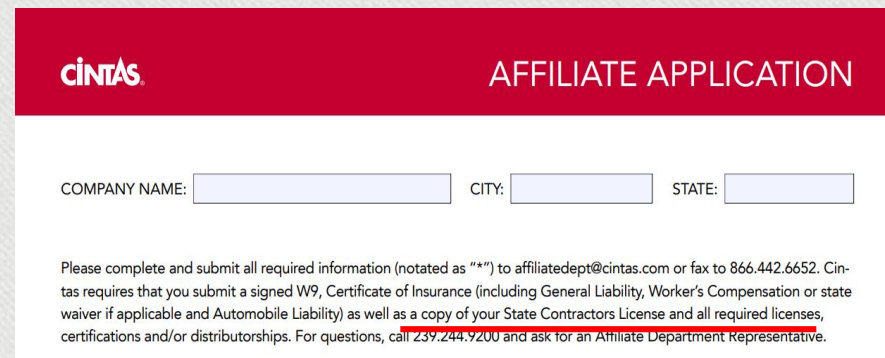


**JOIN OUR NETWORK OF PREFERRED AFFILIATES**

Extinguisher Inspection   Sprinkler Systems   Fire Extinguisher Training   Fire Alarm Monitoring   Value Inspection Program  
Fire Alarm Panels   Emergency Lights   Kitchen Suppression   Hazard Suppression   National Fire Protection

## A STRATEGIC RELATIONSHIP TO HELP YOUR BUSINESS GROW

At Cintas, we believe a strong affiliate relationship provides a seamless service experience for the customers and builds more value for your business and employees. That is why we strive to be a valuable resource and dedicated advocate for all our affiliates and their employees.



**cintas** AFFILIATE APPLICATION

COMPANY NAME:  CITY:  STATE:

Please complete and submit all required information (notated as “\*\*”) to [affiliatedept@cintas.com](mailto:affiliatedept@cintas.com) or fax to 866.442.6652. Cintas requires that you submit a signed W9, Certificate of Insurance (including General Liability, Worker’s Compensation or state waiver if applicable and Automobile Liability) as well as a copy of your State Contractors License and all required licenses, certifications and/or distributorships. For questions, call 239.244.9200 and ask for an Affiliate Department Representative.

Source: [Cintas](#)



# *But Results Are Not Sustainable:*

## *Four Negative Trends In Fire Inspection*

Through our conversations with fire inspection industry professionals, we believe there are four very large challenges facing Cintas that will impede its growth and profit potential in the industry.



### **Not Enough Skilled Labor To Deliver Services In Compliance With The Law**

- It's universally agreed among people we spoke to that there's not enough skilled and licensed inspectors
- It can take between 3 – 5 years between apprenticeship to fully licensed worker
- **There is evidence that Cintas committed fraud by allowing unlicensed workers to falsify inspection reports**



### **Private Equity And New Money Is Flooding Into The Industry To Disrupt Cintas**

- Cintas does not have a good reputation in the industry, as reflected by numerous internet complaints, and our primary research
- The opportunity to displace market share from Cintas, and the allure of recurring revenues from services mandated by law, is what is driving substantial private equity money in the industry
- There are new platform acquisition companies being launched to consolidate regional market share:
  - APi Group, one of Cintas' largest competitors, was just acquired by a SPAC in London and will be listed on the NYSE, giving it broader access to public capital



### **Contract Lengths Are Shortening**

- Historically, commercial contracts could be negotiated for 3 - 5 years, giving longer visibility to service providers
- This would allow Cintas to implement annual price increases easily
- Now, commercial and national contracts are being shortened to 1 year, allowing customers greater flexibility to price shop



### **Margins Are Coming Under Pressure From Greater Competition**

- For services such as fire extinguisher inspection, Cintas has historically been able to command \$2.85 - \$3.25 per unit
- According to our industry sources, Cintas has been willing to price as low as \$1.50 per unit to win business. At this level, competitors we spoke to believed it was simply not economical to justify trying to match the price





# Cintas Placing Lives At Risk, Breaking The Law, And Committed Fraud With Unlicensed Fire Inspectors

**Upon a fire outbreak in the city of Aurora, IL, it was determined that Cintas was charged with fraudulent inspection practices. The city found that 8 of 12 Cintas inspectors were not licensed to carry out inspection duties for the 22 properties within its jurisdiction.** Illinois state law clearly mandates a license for inspections.<sup>(1)</sup> Although it is possible this is an isolated incident, the mere fact that two-thirds of Cintas inspectors were not licensed suggests that Cintas growth in the Fire Protection business has come at the cost of violating the law, and putting lives at risk.

## City of Aurora

Law Department | Division of Legal Counsel  
44 E Downer Pl | Aurora, IL 60507  
Phone: (630) 256-3060 | Fax: (630) 256-3069 | Web: www.aurora-il.org

August 20, 2019

Cintas Fire Protection  
Attn: Jason Adessa, General Manager  
11 Eisenhower Lane  
Lombard, IL 60148

Cintas Corporate Headquarters  
Attn: Mike Greve, Regional Business Manager  
6800 Cintas Boulevard  
Suite 9151  
Mason, OH 45040

Mr. Greve and Mr. Adessa:

On May 26, 2019, the Aurora Fire Department (AFD) responded to a fire at 800 N. Highland, Aurora, Illinois. After a thorough investigation, AFD determined that the building's sprinkler system was not working as it should have been. The investigation also revealed that **Personal** is a Cintas employee, completed paperwork indicating that he had tested and inspected the sprinkler system, when in fact, he had not.

AFD further determined that **Personal** was not certified by the State of Illinois to perform sprinkler inspections. At the City's request, Cintas subsequently provided the City with a list of 22 additional buildings within the City whose sprinkler systems Mr. Cintas purportedly inspected.

As I am sure you will agree, this is an unacceptable situation. The failure of the sprinkler system at 800 N Highland could easily have contributed to the building's occupants and the City's first responders suffering serious injuries. While it is fortunate that no one was hurt as a result of this fire, the result could easily have been different.

The City expects that Cintas will immediately, through the use of State-certified inspectors, and at its own expense, re-inspect each of the 22 facilities that **Personal** purportedly inspected. The City also expects that **Personal** will not be a part of any of these re-inspections, or subsequent inspections of any kind in the City of Aurora even if he is now, or later becomes certified by the State to do so. I am enclosing the list of facilities requiring re-inspection for your review.

Through our investigation, we learned that eight of Cintas's twelve fire protection inspectors for Cintas are not state certified. Those inspectors should not be inspecting any properties or businesses in the City going forward until they obtain the proper certifications. We expect that Cintas will use State-certified inspectors as it continues to do business in Aurora, as the current practice is not acceptable and has the potential to lead to additional serious life safety concerns.



## Complaint Form

Fire Sprinkler Contractor Licensing Act

Public Act (PA 92-871)

This form is to be used by any citizen that witnesses violation of the Fire Sprinkler Contractor Licensing Act (PA 92-871). This form can be filled in on-line and sent automatically or you can download the form and mail it to: Office of the State Fire Marshal, Attention: Robert Wetzel, 1035 Stevenson Drive, Springfield, IL 62703. Email: Robert.Wetzel@illinois.gov

Date of Incident: 05/26/2019

Please use the drop down arrow to select date of incident

Location: River Valley Coatings, Inc.

Address: 800 N. Highland Avenue, Aurora, IL 60506

Distributor/Contractor Name: Cintas Fire Protection

Address: 11 Eisenhower Lane S Suite 200, Lombard, IL 60148

Phone: (630) 524-9508

Illinois Distributor License # FSC0354

Technician Name: **Personal**

Nature of Complaint: **Unqualified inspector and fraudulent inspection**

(Please include reference to NFPA Standard or State Law this violation is in regards to)

1) According to Section 30 (Subsection (f)) of the Professions, Occupations, and Business Operations Fire Sprinkler Contractor Licensing Act, inspections and testing of existing fire sprinkler systems and control equipment must be performed by a licensee or an individual employed or contracted by a licensee. Any individual who performs inspection and testing duties under this subsection must possess proof of (i) certification by a nationally recognized certification organization at an appropriate level, such as NICET Level II in Inspection and Testing of Water Based Systems or the equivalent, by January 1, 2008 or (ii) satisfactory completion of a certified sprinkler fitter apprenticeship program approved by the U.S. Department

Updated 12/2014



of Labor. There is no evidence on the NICET website or Local 281 that the inspector possesses the necessary qualifications.

2) There is documentation of a partial trip test of the dry system on December 19, 2018. There was no corroboration of the

inspection on the Customer Activity Report provided by the monitoring company. Scrutiny of the maintenance record

was prompted by a failure of the sprinkler system to function during a fire on Sunday May 26, 2019.

Submitted By: Fire Marshal Javan Cross

Company: City of Aurora Fire Department Prevention Bureau

Address: 5 E. Downer Place, Aurora, IL 60505

Phone: (630) 256-4131

Complaint filed by: Fire Marshal Javan Cross

Phone: (630) 256-4131

[Submit to Recipient Via Email](#)

Updated 12/2014



## *Not An Isolated Incident*

It is clearly not a one-off situation in Aurora. We also find another instance of Cintas doing inspection work without either a permit, or a contractor's license.

### Violation Citation

**2017-01:** Cintas Fire Protection – James Morris

**Violation:** Working without a contractor's license at:  
TJ Maxx – 1684 East 80<sup>th</sup> Avenue, Merrillville, IN 46410

**Purpose:** Required to appear before the Contractor's Licensing Board.

Mr. Hannigan stated that the complaint was filed by the City of Hobart Fire Marshall, Joshua Magner. Mr. Magner was present and addressed the Board. He stated that while doing an inspection of the location for a Certificate of Occupancy he noticed that Cintas had performed work without a permit or a contractor's license. They also had not called for a fire watch while the fire system was down. Mr. Jim Morris, Operations Manager of Cintas Fire Protection, was present and addressed the Board. He stated that his company was contracted to perform an inspection of the fire system and found that it was not up to code. He agreed that the system should not have been disabled during the work and that he should have checked on permits. Mr. Magner stated that he never heard from Cintas during this time. Mr. Stephens motioned to fine Cintas Fire Protection \$300.00 for working without a license to be paid within 30 days. Mr. Maggio seconds. All ayes. (6-0)

[Source](#)

## *And Someone Even Died....*

A mining worker died recently from injuries sustained from an improper inspection by a Cintas worker as detailed in the Mine Safety & Health Administration fatality report. Cintas is being sued by the worker's family for wrongful death.

### Wrongful Death Lawsuit

16. Despite the knowledge and CINTAS' purported expertise, CINTAS did not sleeve the hoses with an extreme temperature heat-resistant fire jacket.

17. In addition to CINTAS' paid installation, the mine operator further paid CINTAS to perform semi-annual inspections and to complete maintenance of the fire suppression system it had installed on the haul truck.

18. On July 31, 2017, CINTAS conducted an inspection of the fire suppression system and failed to discover and correct its negligent installation.

19. On January 26, 2018, CINTAS conducted an additional inspection of the fire suppression system and again failed to discover and correct its negligent installation.

Source: Angela Grostefon vs. CINTAS Corp No 2 (d/b/a Cintas Fire Protection)

### Wrongful Death Lawsuit

#### ROOT CAUSE ANALYSIS

MSHA conducted an analysis to identify the most basic cause or causes of the accident that were correctable through reasonable management controls. Root causes were identified that, if eliminated, would have either prevented the accident or mitigated its consequences.

Listed below are the root causes identified during the analysis and the corresponding corrective actions which were implemented to prevent a recurrence.



Root Cause: The mine operator and Cintas did not ensure the fire suppression system on the Caterpillar 793C haul truck, company number 2-170, was installed and maintained in accordance with manufacturer's recommendations.


Source: Mine Safety & Health Admin [Final Report](#) – Sept 7, 2018



# Cintas Potentially Not In Compliance With Its Credit Agreement

Cintas made certain Representations and Warranties to its bankers that it “holds permits, certificates, licenses... necessary for the conduct of its business in compliance with all applicable Laws”.... **Is this really true?** If the licensing issue is systemic in its Fire Safety business, would this be deemed a Material Adverse Effect? Cintas needs to conduct a full audit of its workforce.

Section 6.3. Compliance with Laws and Contracts. Each Company:

- 
- (a) holds permits, certificates, licenses, orders, registrations, franchises, authorizations, and other approvals from any Governmental Authority necessary for the conduct of its business and is in compliance with all applicable Laws relating thereto;
  - (b) is in compliance with all federal, state, local, or foreign applicable statutes, rules, regulations, and orders including, without limitation, those relating to environmental protection, occupational safety and health, and equal employment practices;
  - (c) is not in violation of or in default under any agreement to which it is a party or by which its assets are subject or bound;
  - (d) has ensured that no Person who owns a controlling interest in or otherwise controls a Company is (i) listed on the Specially Designated Nationals and Blocked Person List maintained by the Office of Foreign Assets Control (“OFAC”), Department of the Treasury, or any other similar lists maintained by OFAC pursuant to any authorizing statute, executive order or regulation, or (ii) a Person designated under Section 1(b), (c) or (d) of Executive Order No. 13224 (September 23, 2001), any related enabling legislation or any other similar executive orders;
  - (e) is in compliance with all applicable Bank Secrecy Act and anti-money laundering Laws and regulations;
  - (f) is in compliance, in all material respects, with the Patriot Act;
  - (g) has ensured that no Company, or to the knowledge of any Company, any director or officer of a Company, is a Person that is, or is owned or controlled by Persons that are (i) the subject of any Sanctions, or (ii) located, organized or resident in a country or territory that is, or whose government is, the subject of Sanctions;
  - (h) has ensured that no Company, or to the knowledge of any Company, any director or officer of a Company, is a Person that is, or is owned or controlled by Persons that are (i) the subject of any Sanctions, or (ii) located, organized or resident in a country or territory that is, or whose government is, the subject of Sanctions; and
  - (i) is in compliance, in all material respects, with Anti-Corruption Laws, and has implemented policies and procedures reasonably necessary to ensure that no Company, any director, officer, agent, employee or other person acting on behalf of a Company has taken any action, directly or indirectly, that would result in a violation by such Person of Anti-Corruption Laws, and the Companies have taken such actions they deem reasonably necessary to ensure continued compliance therewith;

except in the case of any of subparts (a) through (f) above, where the failure to hold such permits, certificates, licenses, orders, registrations, franchises, authorizations or approvals, or where any such non-compliance or violation, would not reasonably be expected to have a Material Adverse Effect.



# Cintas Prices And Margins Appear To Be In Contraction

Core fire extinguisher inspection pricing is contracting. Based on our industry conversations, we understand that Cintas has been willing to price as low as \$1.50 per extinguisher, particularly to commercial and national customers, which are more price savvy. Recent prices suggest \$2.85 - \$3.25 per extinguisher. At \$1.50 pricing, some competitors thought it was not even economical to do the business. Some municipalities are being charged more, but as word spreads that Cintas is willing to do it for much cheaper, there is downside risk to pricing as contracts are renewed.

## \$3.25 Contract From 2017



Cintas Fire Protection  
15533 w 100th terrace  
lenexa ks 66219  
913.708.3441  
Location #F58  
Customer #

### Fire Protection Services Agreement

Fire Extinguishers / Emergency Lighting / Restaurant / Industrial Systems / Fire Alarms / Fire Sprinklers

Customer Name: St Joseph School District Effective Date: 7-11-17  
Service Address: See Addendum (A) City: \_\_\_\_\_ State: MO Zip: \_\_\_\_\_  
Phone: \_\_\_\_\_ Fax: \_\_\_\_\_  
Contact Name: Roy Lashbrook Contact Title: Purchasing Manager E-mail: roy.lashbrook@sjds.k12.mo.us

Billing Name: St. Joseph School District Billing Address: 1000 S 9th St  
City: St Joseph State: MO Zip: 64503 Billing Phone: 816.671.4000 Billing Fax: 816.671.4484  
AP Contact Name: Kim Waller AP Contact E-Mail: kim.waller@sjds.k12.mo.us  
Payment Terms: Net 10 Days PO/Blanket PO# \_\_\_\_\_ PO Date: \_\_\_\_\_

Term: The term of this Agreement is 1 year (s), commencing on the effective date above. In the event of a service issue, the Customer agrees to submit their complaint in writing and allow the Seller sixty (60) days from the date the written complaint is received to remedy the service issue. In the event the service issue is not remedied to the reasonable satisfaction of Customer, Customer can cancel this Agreement but the Customer shall pay any outstanding charges for services rendered prior to termination. This Agreement may be extended in accordance with the renewal provision.

Renewal Provision: This Agreement shall self-renew for successive annual periods unless either party delivers written notice of termination within sixty (60) days prior to the renewal date. Seller shall have the right to increase the charges provided for herein at any time after expiration of the initial period upon giving the Customer notice in writing prior to the expiration of the then-current annual term.

Repairs: Customer hereby authorizes repairs up to \$500 to correct deficiencies found during the system inspection.

| Quantity | Service Description                                      | Next Service Date | Frequency | Cost    |
|----------|--|-------------------|-----------|---------|
| +/- 800  | Annual Fire Extinguisher Inspection Per NFPA CODE 10     | TBD               | Annual    | \$3.25  |
| TBD      | Recharge of 10lb ABC (all parts included)                |                   |           | \$35.00 |
| TBD      | Recharge of 5lb ABC (all parts included)                 |                   |           | \$25.00 |
| TBD      | 6 / 12 Year Maintenance on 10lb ABC (all parts included) |                   |           | \$45.00 |
|          | 6 / 12 Year Maintenance on 5lb ABC (all parts included)  |                   |           | \$35.00 |

Source: [St Joe's School](#)

## \$2.85 Contract From 2017

### PROPOSAL FIRE EXTINGUISHER MAINTENANCE FOR THE CITY OF OSHKOSH DEPARTMENTS BID SUBMITTAL FORM

#### SECTION I - DRY CHEMICAL STORED PRESSURE

| Bid Item | Qty<br>More or Less | Description                                   | Each Price      | Total             |
|----------|---------------------|---|-----------------|-------------------|
| 1        | 752                 | Annual Maintenance Check                      | \$ <u>2.85</u>  | \$ <u>2143.20</u> |
| 2        | 385                 | 5.5 - 6# Extinguisher Recharge                | \$ <u>12.00</u> | \$ <u>4620.00</u> |
| 3        | 344                 | 10 - 30# Extinguisher Recharge                | \$ <u>12.00</u> | \$ <u>4128.00</u> |
| 4        | As needed           | Per pound dry chemical added to extinguishers | \$ <u>2.25</u>  | \$ <u>2.25</u>    |
| 5        | As needed           | 5.5 - 6# Extinguisher 6 Year Maintenance      | \$ <u>6.00</u>  | \$ <u>6.00</u>    |
| 6        | As needed           | 10 - 30# Extinguisher 6 Year Maintenance      | \$ <u>6.00</u>  | \$ <u>6.00</u>    |
| 7        | As needed           | 5.5 - 6# 12 Year Hydro Test                   | \$ <u>11.00</u> | \$ <u>11.00</u>   |

Source: [Oshkosh](#)





# Enlightening Interview With Former Senior Business Leader At Cintas Fire Safety

Spruce Point spoke with Cintas' former fire inspection business leader. He agreed that skilled labor shortage is a real business challenge, and that it would be fraudulent to represent oneself as a licensed inspector, without having the credentials.

## Spruce Point Question

*"Talk about the challenges or, or maybe no challenges as the case may be, of finding skilled people to do these jobs, to go out and do the fire inspections."*

## Former Cintas Fire Inspection Safety Business Leader

*"Yeah. There's no question there's a constraint. I mean, every business in North America has fire extinguishers in their business, about 70% of businesses, maybe 60% of businesses, have a fire alarm system, and then you might back that number down, but somewhere around 50% that have a fire sprinkler system. So you can execute fire extinguisher inspections quite easily. I mean, you could hire someone that you know, has aptitude and hustle and you know, maybe slight mechanical ability and get them operational within 60 or 90 days pretty easily. When you get into alarm and sprinkler, uh, if you just went from someone that was competent and capable but didn't know anything about fire and you got them all the way to a fire alarm or sprinkler certification within a town, state or city; that could be a three year proposition.... And I mean there is that labor constraint out there. Um, so you're either going to find someone that already has their license, and try to take them away from your competitor, right? Or, you have a really advanced training program where you constantly have apprentices and helpers around these certified technicians, so you're raising up and grooming a group of future inspectors. If there's a bottleneck in this business, that's it."*

## Spruce Point Question

*"What happens if Cintas sent someone who is supposed to be licensed, and in fact, that person isn't licensed, and something goes wrong. That's a bad outcome."*

## Former Cintas Fire Inspection Safety Business Leader

*"You wouldn't be able to send somebody out there that's not licensed, right? I mean you're holding a man, again to just keep it simple, like a driver's license, here's my sprinkler license it has an expiration date, it has a number on it that can be easily verified through website. So there would never not be a scenario where you'd send someone out to do an inspection that didn't have their certification. Yeah. I mean it is a felony for example. If you went out and inspected a fire alarm in Texas, and you inspected it, and said "you're good to go", but didn't have your license. That is a felony for the individual that would do that."*

## Spruce Point Question

*"What is driving private equity led M&A in the fire inspection and services industry right now?"*

## Former Cintas Fire Inspection Safety Business Leader

*"I think a couple things. One, Cintas does a pretty good job of becoming hated in the spaces that they operate in, not by their investors, but by the industry patrons. So you know, the, the small businesses that are left out there, would have a bad taste in their mouth selling to Cintas. And there's people that are aware of that...."*

# Cintas Now Competing With Fresh Private Equity Money

If, as suggested by its former business manager, that Cintas is disliked by many in the industry, it would create a ripe opportunity for private equity to expand into the fragmented fire protection and inspection services space. Perhaps, a more customer friendly approach will enable it to win share from Cintas.

## Audax Private Equity Announces the Acquisition of Academy Fire Life Safety

April 19, 2017 11:06 AM Eastern Daylight Time

[Source](#)

## Thompson Street Capital Partners Acquires Marmic Fire & Safety Co.

ST. LOUIS (September 10, 2018) – Thompson Street Capital Partners (TSCP), a private equity firm based in St. Louis, has partnered with management to acquire Joplin, Missouri-based Marmic Fire & Safety Co. (Marmic), a provider of fire suppression installation and inspection services, hazard analysis, and fire and personal safety products. Terms of the transaction were not disclosed.

Marmic ([www.marmicfire.com](http://www.marmicfire.com)) is a leading commercial fire and life safety platform in the midwestern United States. The Company provides recurring inspection, test, and maintenance services conforming to OSHA mandates, government codes, and NFPA standards. Marmic also offers sales, installation and repair of a large selection of fire safety products and fire suppression and security systems.

[Source](#)

## Ares Management to Acquire Convergent Technologies

**FEB 2 2018** LOS ANGELES—February 2, 2018—Ares Management, L.P. (NYSE:ARES) announced today that a fund managed by its Private Equity Group has acquired Convergent Technologies, a leading global independent security integrator, from investment funds affiliated with KRG. Terms of the transaction were not disclosed.

Based in Schaumburg, Illinois, Convergent provides comprehensive security integration and fire and life safety services in more than 80 locations across four continents. Since its founding in 2001, Convergent has grown to employ more than 3,400 colleagues as the business continues to expand its security offerings and geographic footprint. Central to this growth is Convergent's strong corporate culture, which focuses on providing best-in-class service to meet its customers' unique security needs.

[Source](#)

## Blue Point Completes the Acquisition of Fire & Life Safety America

CHARLOTTE, NC (February 22, 2017) – Blue Point Capital Partners announced today the acquisition of its seventh Blue Point III platform investment, Fire & Life Safety America ("FLSA"), a leading provider of fire and life safety system inspection, maintenance, repair and installation services.

[Source](#)

## Riverside Forms Latest Portfolio Company Certasite

July 11, 2019

### CertaSite Committed to Acquiring Additional Fire Protection Companies

The Riverside Company, a global private equity firm, has formed [CertaSite](#), a fire and life safety platform that is committed to the highest levels of customer service, responsiveness, building safety and code compliance. To date, the Certasite family includes County Fire Protection, Company One, Approved Protection Systems, Field's Fire Protection and Spears Fire and Safety Services.

"We are thrilled to work with Certasite CEO Jeff Wyatt to build a business in the fire and life safety market," said Riverside Managing Partner Loren Schlachet. "During our partnership, we look to bring additional businesses under the Certasite umbrella, assisting with improvements in technology and innovation, growth-driven sales strategies and professional development opportunities for their employees."

[Source](#)

## Align Capital Partners Ignites Growth with Merger of ISA and ABCO Fire Protection

by Align Capital Partners | Aug 13, 2018 | Uncategorized

Align Capital Partners' ("ACP") announced today the strategic merger of its most recent platform investment, ISA Fire and Security ("ISA"), with Cleveland-based ABCO Fire Protection ("ABCO"). ABCO is a regional provider of fire safety and security system inspection, maintenance, and repair services for thousands of commercial customers in a variety of end-markets. The company goes to market under the ABCO, Trico, and Superior Fire brands.

[Source](#)

## Highview Capital Acquires Frontier Fire Protection

April 04, 2019 04:15 PM Eastern Daylight Time

LOS ANGELES & DENVER--(BUSINESS WIRE)--Highview Capital, LLC ("Highview"), a Los Angeles-based middle-market private equity firm, today announced its acquisition of Frontier Fire Protection, LLC ("Frontier Fire" or "the Company"), a leading provider of fire and life safety solutions in the U.S. Mountain West and Southwest regions. Frontier Fire's management team, including Chief Executive Officer Greg Londo, will continue to lead Frontier Fire and remain shareholders of the Company.

[Source](#)

June 10, 2016 – Carousel Capital announced today that it has partnered with management to recapitalize Pye Barker Fire & Safety ("Pye Barker" or the "Company"), the leading provider of route-based fire protection services in the Southeast. Based in Atlanta, Georgia, Pye Barker operates from 17 branches strategically located in Florida, Georgia, North Carolina, South Carolina and Tennessee providing best in class service to its diverse customer base. Founded in 1946, Pye Barker route-based services include monitoring, inspection, maintenance and repair of fire detection and suppression products. The Company also provides commercial cleaning services to restaurants and food service companies. Pye Barker's highly trained technicians deliver services on a recurring, planned or responsive basis to tens of thousands of sites per year for a large customer base. Pye Barker serves customers across its strategic Southeastern

[Source](#)

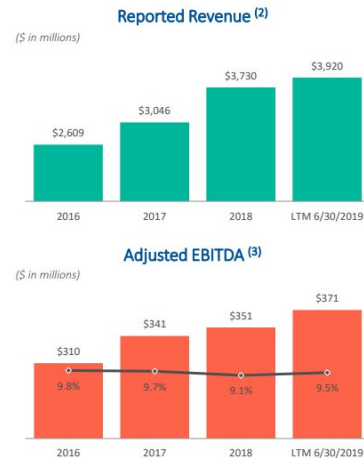


# Cintas' Fire Competitor APi Group To Be Publicly Listed

APi Group is a national, market leading provider of commercial life safety solutions and industrial specialty services, and expects to deliver ~\$4 billion in revenue and Adj. EBITDA margins of ~10% for the full year 2019. On September 2, 2019, J2 signed an agreement to acquire APi for \$2.9 billion, representing a transaction multiple of 7.4x LTM June 2019 Adjusted EBITDA of \$371 million net of tax benefits. The deal closed in early October 2019, and it's expected that APi will trade on the NYSE. As a newly formed public company, it will have better access to capital, and a public currency to attract and motivate employees.

APi is a credible national competitor to Cintas that offers a full suite of safety solutions including engineering, design, installation, inspection, repair and monitoring. We believe Cintas offers a narrower range of services, and does not do the more lucrative repair business

## INDUSTRY LEADING FINANCIAL PROFILE



1. Indicative percentages based on the company's proposed reporting segments, which are unaudited and in process of review.  
2. Reported Revenue, excluding the acquisitions of Northland and Texas Sprinkler in 2016, and Mid-Ohio and MP Nexlevel in 2018.  
3. Adjusted EBITDA pro forma for acquisitions and non-recurring seller related and other costs. For more detail, please refer to the Appendix.



## SEGMENT OVERVIEW

### Safety Solutions

- > Leading independent integrator of safety systems
- > #1 fire protection and sprinkler provider
- > Mission critical service offerings including life safety, emergency communication systems and specialized mechanical services
- > Full suite of life safety solutions focused on alarm & detection systems including:
  - > Engineering & Design
  - > Fabrication & Installation
  - > Inspection, Repair, Monitor
  - > Retrofit & Upgrade
- > Large installed base drives significant recurring revenue through service and monitoring agreements
- > Driven by non-discretionary regulatory spend, providing a stable annuity stream of revenues

### Specialty Services

- > Leading provider of infrastructure services and specialized industrial plant solutions
- > Service offering includes installation, maintenance and repair of critical infrastructure such as underground electric, gas, water, sewer, telecom infrastructure, specialty construction projects and diversified civil construction
- > Customers include public and private utilities, communications, industrial plants and government agencies
- > Multi-year unit price / T&M agreements provide a recurring revenue base without customer concentration risk
- > Positioned to capitalize on secular industry tailwinds

### Industrial Solutions

- > Provider of niche specialty contracting services to diversified end markets
- > Leading regional transmission and distribution specialty services contractor
- > Provides full suite of solutions to midstream oil and gas to build new pipeline and perform ongoing integrity management and maintenance services
- > Provides other specialized services including structural steel fabrication







## *Evidence of Mounting Financial Struggles In The Core Uniform Business Post G&K Acquisition*



# Cintas Wildly Overpays For G&K

Cintas appears to have desperately needed to purchase G&K, raising its initial bid of \$76.00 all the way to \$97.50 per share. The final cost of \$2.1 billion cost Cintas shareholders an additional \$425 million over the initial price. The \$97.50 per share purchase price represented a 68.7% premium to GK's 52 week low share price.

Jan 12, 2016

*Mr. Farmer (Cintas CEO) met with Mr. Milroy (CEO of G&K) as scheduled. At the meeting, Mr. Farmer proposed in writing that Cintas acquire all of the outstanding common shares of **G&K for \$76.00 per share in cash**. Mr. Milroy said he would discuss Cintas' proposal with the Company Board.*

May 12, 2016

*Mr. Milroy met with Messrs. Farmer and Hansen. At the meeting, Mr. Farmer presented a proposal to acquire all of the outstanding common shares of **G&K for \$86.00 per share in cash** and confirmed the offer in writing.*

June 29, 2016

*Mr. Farmer contacted Mr. Milroy and presented a proposal whereby Cintas would acquire all of the outstanding common shares of **G&K for \$94.00 per share in cash**.*

Aug 3, 2016

*Mr. Farmer delivered to Mr. Milroy a written confirmation of Cintas' proposal to acquire all of the outstanding common shares of **G&K for \$97.50 per share in cash**, in which Cintas expressed its commitment to take certain actions with respect to regulatory approvals if necessary to provide for certainty and timeliness of closing the transaction and to pay a termination fee in certain circumstances if regulatory approval is not obtained.*

# Pressures Mounting In Cintas Core Business

In FY 2018, the last year that G&K can be unraveled from Cintas core business, we find that EBITDA growth fell below revenue growth and margins stalled. The CFO claims that legacy Cintas gross margins continued to expand, which is hard to disprove with limited disclosures; however, we believe legacy Cintas EBITDA margins did not expand.

| \$ in mm   | FY 2016                          | FY 2017                           | FY 2018                           | Note   |
|--|----------------------------------|-----------------------------------|-----------------------------------|--|
| Reported Total Sales   | \$4,795.8                        | \$5,323.4                         | \$6,476.6                         |  |
| Less: G&K Revenue Contribution                               | --                               | (\$187.7)                         | (\$950.0)                         | FY 17 revenue disclosed <a href="#">10-K</a> p. 56<br>FY 18 revenue estimated based on Q1-Q3 and full year disclosure of revenue growth attributed to acquisitions |
| <b>Normalized Total Sales</b><br>% growth                    | <b>\$4,795.8</b><br>9.8%         | <b>\$5,135.7</b><br>7.1%          | <b>\$5,526.6</b><br>7.6%          | Limited underlying growth 2017-18  |
| <b>Reported EBITDA</b><br>% margin                           | <b>\$934.2</b><br>19.5%          | <b>\$1,049.5</b><br>19.7%         | <b>\$1,311.1</b><br>20.2%         | Margins appear to be expanding   |
| Less: G&K EBITDA Contribution                                | --                               | (\$30.3)                          | (\$160.4)                         | EBITDA margin estimated based on <a href="#">deal proxy</a> projections from management  |
| Less: Reported Synergies                                     | --                               | --                                | (\$58.0)                          | Synergies disclosed <a href="#">Q1'19 conf call</a>  |
| <b>Est. Underlying Cintas EBITDA</b><br>% growth<br>% margin | <b>\$934.2</b><br>11.4%<br>19.5% | <b>\$1,019.2</b><br>9.1%<br>19.8% | <b>\$1,092.7</b><br>7.2%<br>19.8% | EBITDA growth lower than sales growth shows diminishing earnings leverage<br>Underlying margins for Cintas are flat  |

Cintas CFO  
Q1 2018  
Earnings Call  
Sept 26, 2017

CFO: **"The Cintas legacy gross margins continue to expand and the G&K gross margins will too as we realize the acquisition synergies."**  
Spruce Point: Hard to disprove this statement on gross margins due to limited disclosures, but it's clear to us that EBITDA margins did not expand





# Management's Gross Margin Expansion Claims Now Appear Baseless

Management repeatedly claimed that G&K's gross margins will improve to Cintas' legacy margins as it was marketing the transaction to investors. Yet, it's now very evident that management never had a way to measure or track it, thus calling its claims into question. As a result, management is now dodging direct follow-up questions on the issue.

Cintas CFO  
Q1 2018  
Earnings Call  
Sept 26, 2017

***"The Cintas legacy gross margins continue to expand and the G&K gross margins will too as we realize the acquisition synergies."***

Cintas Treasurer  
Q3 2018  
Earnings Call  
March 22, 2018

*"While the assimilation of the G&K business continues at a great pace -- Mike mentioned 95% of duplicate operations have been closed, more work remains. **The G&K gross margins will improve to Cintas legacy levels as we further integrate this business and we increasingly realize more of the synergies. We are on track.**"*

Analyst  
Kevin Damien  
McVeigh  
Q1 2020  
Earnings Call  
Sept 24, 2019

*"Really, really nice job. At this point, given the gross margins, is it fair to say -- and I know we're not just [interviewing] G&K, **but is G&K up to the corporate average at this point?** Or would you expect that to get continue to kind of narrow relative to where Cintas is relative to GK?"*

CFO Response  
Q1 2020  
Earnings Call

***"Well, as you referred to (gross margins), it's really hard to say.** So for example, a lot of that G&K volume resides in legacy Cintas locations. So when you think about that volume, it certainly has helped us in those kinds of locations create more capacity utilization, create a little more density. And so there certainly is a benefit. From stand-alone locations, many of them have inherited some legacy Cintas volumes, but they're not quite to where we would see the rest of the Cintas legacy locations, but they're making nice progress. So we hope to continue to see improvements as we move forward."*

# Obvious Signs of Financial Strain At Cintas

While analysts laud Cintas's performance, and management talks up great execution and record results, there are clear signs of financial strains emerging in its business. We observe a spike in allowance for doubtful accounts, record working capital to sales, and expanded DSOs and DPOs.

|   | G&K Services Pre-Acquisition And Last Quarter Prior To Acquisition |                                   |                                   | Cintas Pre-Acquisition And Last Quarter Prior To Acquisition Close 3/21/17 |  | Combined Current Cintas Showing Strain |                                       |  | Notes   |
|---|--|-----------------------------------|-----------------------------------|--|--|--|---------------------------------------|--|---|
| \$ in mm  | FY 15<br>6/27/2015   | FY 16<br>7/2/2016                 | LTM<br>12/31/16                   | FY 16<br>5/31/16   | LTM<br>2/2/17                          | Q3 19<br>2/28/19                       | FY 2019<br>5/31/19                    | Q1 20                                  |   |
| Accounts Receivable, net (A)  | \$100.4  | \$102.6                           | \$108.7                           | \$563.2  | \$598.9                                | \$878.8                                | \$910.1                               | \$917.5                                |   |
| Allowance For Bad Debts (B)   | \$3.5  | \$3.6                             | \$4.3                             | \$19.6   | \$20.5                                 | N/A                                    | \$37.8                                | N/A                                    |   |
| Gross Receivables (A+B)<br>% Allowance of Gross   | \$103.9<br>3.3%  | \$106.2<br>3.4%                   | \$113.0<br>3.8%                   | \$582.8<br>3.4%  | \$619.4<br>3.3%                        | N/A                                    | \$947.9<br>4.0%                       | N/A                                    | Highest Allowance Ever At 4%  |
| Current Assets<br><u>Less: Cash and Securities</u><br>Adj. Current Assets (C)           | \$317.2<br><u>16.2</u><br>\$301                                    | \$313.4<br><u>24.2</u><br>\$289.1 | \$321.8<br><u>29.9</u><br>\$291.1 | \$1,590.0<br><u>210.0</u><br>\$1,380.0                                     | \$1,629.9<br><u>147.2</u><br>\$1,482.7 | \$2,233.8<br><u>80.9</u><br>\$2,152.9  | \$2,236.3<br><u>96.6</u><br>\$2,139.6 | \$2,289.8<br><u>102.1</u><br>\$2,187.7 |   |
| Current Liabilities<br><u>Less: NTM Debt Maturities</u><br>Adj. Current Liabilities (D) | \$123.5<br><u>0.2</u><br>\$123.3                                   | \$117.5<br><u>0.0</u><br>\$117.5  | \$141.0<br><u>22.0</u><br>\$119.0 | \$815.5<br><u>250.0</u><br>\$565.6   | \$944.0<br><u>399.4</u><br>\$544.6     | \$994.4<br><u>217.5</u><br>\$776.9     | \$1,127.7<br><u>312.3</u><br>\$815.5  | \$1,122.9<br><u>338.8</u><br>\$784.1   |   |
| Adj. Working Capital (C-D)<br>% of LTM Sales  | \$177.6<br>18.9%   | \$171.5<br>17.5%                  | \$146.4<br>17.6%                  | \$814.7<br>16.7%   | \$938.1<br>18.6%                       | \$1,376.0<br>20.3%                     | \$1,324.2<br>19.2%                    | \$1,403.6<br>20.0%                     | Working capital strain evident with highest working capital / sales |
| Days Sales Outstanding (DSO)<br>Days Payable Outstanding (DPO)                          | 38.9<br>27.8   | 38.5<br>28.0                      | 39.8<br>29.4                      | 39.8<br>14.9   | 41.6<br>18.2                           | 44.7<br>18.7                           | 45.4<br>21.1                          | 45.7<br>21.5                           | DSOs rising rapidly and hit an all-time high. DPOs being stretched  |

Source: Cintas and G&K financials, Spruce Point analysis



# Obvious Signs of Financial Strain At Cintas (Cont'd)

A classic sign of accounting shenanigans is when accounts receivable are growing faster than reported sales. It is often cited as a top red flag to predict fraud or accounting irregularities.<sup>(1,2)</sup> This phenomenon may suggest aggressive revenue recognition practices at best, a change in credit terms to customers, or at worst foul play such as channel stuffing. We observe that prior to acquiring G&K, Cintas' cumulative sale and accounts receivables growth tracked each other very closely. However, we find that post deal closing, receivables are growing at nearly 2.0x sales.

|                           | Cintas Normal   |         |         |         |         |         | Cintas + G&K = Irregular   |         |         |         |         |         |         |         |         |
|---------------------------|---|---------|---------|---------|---------|---------|--|---------|---------|---------|---------|---------|---------|---------|---------|
|                           | Pre-G&K Acquisition, We See That Cintas' Cumulative Sales Growth Tracks Accounts Receivable Growth Reasonably Close |         |         |         |         |         | Post-G&K Closing Mid-Quarter Q4 2017, We Observe That Cumulative Accounts Receivable Growth Is Now 2.0x Sales Growth |         |         |         |         |         |         |         |         |
| \$ in mm                  | FY 2011   | FY 2012 | FY 2013 | FY 2014 | FY 2015 | FY 2016 | Q1 2018  | Q2 2018 | Q3 2018 | Q4 2018 | Q1 2019 | Q2 2019 | Q3 2019 | Q4 2019 | Q1 2020 |
| Total Net Sales           | \$3,810   | \$4,102 | \$4,317 | \$4,194 | \$4,370 | \$4,796 | \$1,611  | \$1,606 | \$1,589 | \$1,669 | \$1,698 | \$1,718 | \$1,682 | \$1,793 | \$1,811 |
| Cumulative % Sales Growth | --  | 7.7%    | 13.3%   | 10.1%   | 14.7%   | 25.9%   | --   | -0.3%   | -1.4%   | 3.6%    | 5.4%    | 6.6%    | 4.4%    | 11.3%   | 12.4%   |
| Accounts Receivable, Net  | \$429   | \$451   | \$497   | \$508   | \$496   | \$546   | \$731  | \$763   | \$779   | \$804   | \$838   | \$904   | \$878   | \$910   | \$918   |
| Cumulative % A/R Growth   | --  | 5.1%    | 15.7%   | 18.4%   | 15.6%   | 27.4%   | --   | 4.4%    | 6.5%    | 10.0%   | 14.6%   | 23.6%   | 20.1%   | 24.4%   | 25.4%   |

Source: Cintas financials, Spruce Point analysis

- 1) "How to Predict the Next Fiasco In Accounting and Bail Early", [Wall St Journal](#), Jan 2002
- 2) "How To Detect And Prevent Financial Statement Fraud", [ACFE](#) – Association of Certified Fraud Examiners,

# New Disclosure On Discounts And Rebates Validates Concerns

We observe that Cintas made its first disclosure in October 2018 about certain contracts including “discounts and rebates” earned through specified volume levels. This indicates a more competitive environment. G&K did not make any such disclosures prior to its acquisition. While Cintas says it maintains a liability within its accounts for these discounts and rebates, it does not break out the specific line item. However, as a whole, both long and short-term accrued liability accounts have grown from \$600m to \$764m since FY 2017.

Cintas 10-Q  
First Reference Filed  
October 2018

*“Certain of our customer contracts, primarily within our Uniform Direct Sales business, include pricing terms and conditions that include components of variable consideration. The variable consideration is typically in the form of consideration paid to a customer based on performance metrics specified within the contract. **Specifically, some contracts contain discounts or rebates that the customer can earn through the achievement of specified volume levels.** Each component of variable consideration is earned based on the Company's actual performance during the measurement period specified within the contract. To determine the transaction price, the Company estimates the variable consideration using the most likely amount method, based on the specific contract provisions and known performance results during the relevant measurement period. When determining if variable consideration should be constrained, the Company considers whether factors outside its control could result in a significant reversal of revenue. In making these assessments, the Company considers the likelihood and magnitude of a potential reversal. The Company's performance period generally corresponds with the monthly invoice period. No constraints on our revenue recognition were applied during the three months ended August 31, 2018. The Company reassesses these estimates during each reporting period. **Cintas maintains a liability for these discounts and rebates within accrued liabilities on the consolidated condensed balance sheets.**”*

Source: [CTAS 10-Q](#)



# CFO Statement About Working Capital And Inventory Not Mirroring Reality

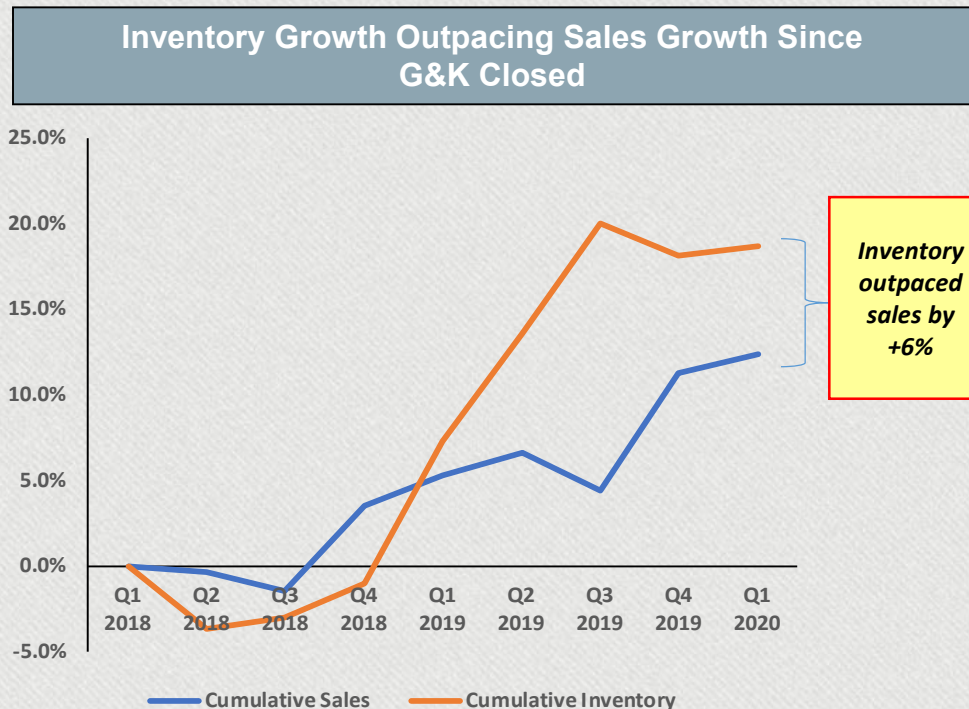
If inventory and working capital growth is a signal of Cintas' flourishing business, as suggested by the CFO's recent quote, then investors' should be concerned that inventory growth has slowed for three quarters. Inventory growth historically outpaced sales by an uncomfortable amount.

CFO  
Q1 2020  
Earnings Call

"Yeah, when we -- **our thoughts on working capital are when we are growing, we're going to use some working capital.** So for example, if we're growing the way we want to grow. Accounts receivable is going to grow. Inventories are going to grow, in-service inventory is going to grow because we are injecting new inventory into new customers and penetrated customers. So generally speaking, we expect in a growth environment, we expect to use working capital."

| Inventory Growth Now Slowing |         |         |         |         |         |
|------------------------------|---------|---------|---------|---------|---------|
| \$ in mm                     | Q1 2019 | Q2 2019 | Q3 2019 | Q4 2019 | Q1 2020 |
| Inventory                    | \$303.8 | \$321.9 | \$339.8 | \$334.6 | \$336.3 |
| QoQ Inventory Growth         | 8.4%    | 6.0%    | 5.6%    | -1.5%   | 0.5%    |

Source: Cintas financials





# Accounts Receivable Dysfunction

Cintas appears to have organizational dysfunction when it comes to A/R collections. Rather than centralizing collections in one location, the Company employs hundreds of collection agents in locations across the country. It even still appears to have active G&K collection agents despite completing the deal more than two and half years ago. Management is claiming success with cost synergies, yet wouldn't some of the easiest cost synergies have been from centralizing collection agents?

Accounts Receivable Clerk at Cintas  
Jackson, Mississippi Area

Accounts Receivable  
Fort Wayne, Indiana Area

Accounts Receivable at G&K Services  
St. Cloud, Minnesota Area

Accounts Receivable at Cintas  
Greater Minneapolis-St. Paul Area

Accounts Receivable Specialist at Cintas  
Greater Omaha Area

GK Services, a division of Cintas  
Accounts Receivable/Collections  
Longview, Texas Area

Accounts Receivable at Cintas  
Dayton, Ohio Area

Accounts Receivable Specialist at Cintas  
Greater Detroit Area

Accounts Receivable Specialist at Cintas Corp.  
Greater Los Angeles Area

Accounts Receivable at Cintas  
Dallas/Fort Worth Area

Accounts Recieveable Specialist  
Orlando, Florida Area

Accounts Receivable Specialist  
Greater San Diego Area

accounts receivable at Cintas  
Baton Rouge, Louisiana Area

Accounts Receivable Clerk at Cintas  
Portland, Oregon Area

Accounts Receivable Specialist  
Pittsfield, Massachusetts Area

Accounts Receivable Rep at Cintas  
Columbia, South Carolina Area

Accounts Receivable and Payables at Cintas  
Daytona Beach, Florida Area

Accounts Receivable at Cintas Corp  
Davenport, Iowa Area



# Accounts Receivable Dysfunction: From An Insiders Perspective

## A/R Staffed By “Temp” Agency

### Cons

The Accounts receivable is all staffed by a temp agency so that's telling you something. The company held a meeting where they explained their way to get out of having to pay taxes; they set up an employee fund for employee hardships (like if you lose your house in a tornado). Cintas puts some money in the pot and then encouraged employees to take a portion of their paycheck into the pot. They actually admitted they want to do this so they can get out of paying taxes. So now you know one of the ways big companies get out of paying thousands maybe millions in taxes.

For their accountants, they hire kids fresh out of college. They sent a company-wide email saying that the new accountant had messed up the company taxes and was therefore sacked. I feel bad for the kid.

Accounts receivable mostly consisted of elderly cranky women, so that means low wages and no career advancement. They recently fired almost all of mgmt for unknown reasons so everyone is walking on eggshells, especially the new mgmt. The people that are high up in the food chain, treat everyone else like peasants. Not at all a family friendly place either. I explained to mgmt a family member was in hospital expecting the worse, I needed time off. Mgmt said it was OK, then let me go the next day. I took off 4 days.

## “Telephone Collections”

### "Its really telephone collections"



Current Employee - Accounts Receivable Specialist in Raleigh, NC

### Pros

health, dental, vision benefits.

### Cons

401k no company match, basic benefits, micromanaging management, short-staffed so you get overloaded with work. no work-life balance

Source: [Glassdoor](#)

## “Corruption”

### "AR representative for fire protection (Pittston, PA)"



Former Employee - Accounts Receivable in Pittston, PA

Doesn't Recommend Positive Outlook Disapproves of CEO

I worked at Cintas full-time for more than a year

### Pros

Decent insurance, okay pay, Okay PTO plan. But nothing is worth the things Cintas will put you through. A sick monopoly game they are playing and they don't care who get screwed in the end.

### Cons

Harassment, corruption, lack of compassion, too cut throat. I have post traumatic stress disorder from this company and wish it would stand up in court. You could see corruption easily in my office cause we had access to the whole country and the drama that unfolded at each location. Fired, hire, moved. If you have an interview here.....run.

Source: [Glassdoor](#)



# Dysfunction: From Customers Perspective

With scores of complaints about over-billing, is it any wonder that customers don't end up paying and Cintas' accounts receivable and bad debt expense are ballooning?



Selene L



06/12/2019

Let me start by saying that my review is based on the billing and customer service. I have tried contacting my account representative over a hand full of times to resolve a few issues with my the billing on my account and I have not seen any of the issues corrected. He does not respond to emails and when I call him, he assures me that the account is being reconciled. We have been trying to reconcile the account since mid last year and he has not made any changes. I called one day and was left on hold and somehow the call was linked with another customer who was also calling to complain about similar issues. The original invoices are given to the person that receives the uniforms during drop off. This does not work well with corporate accounts that have their billing department out of state or in a different office. Cintas, you need to make changes quick before you lose your customers!



Jospeh D



10/30/2018

Unresponsive, inaccurate invoices, billing issues and more billing issues, change of prices without notification.



Sarah S.



03/21/2018

Cintas, at least in regards to small businesses, seems to be intentionally evil. We hired them for our toilet paper, paper towels, sanitizer, rags, and mops - pretty simple stuff. Our payments started around \$100/week. What we didn't realize was that their automatic payment system was terrible, and it was charging us monthly but only for one week out of the month. In the midst of this, they jacked up the cost of basic service, and added all sorts of services that we didn't ask for. Over the course of a year our payments doubled and sometimes tripled PER WEEK, and no one alerted us that they weren't receiving our payments (which was on them, as their online payment system wasn't working) until we owed them thousands of dollars. Once we caught on, we looked back through our invoices and discovered that they had charged us for DAYS WHEN THEY DIDN'T COME 5+ times over the course of a year. I have no idea if they are as evil when they are servicing large organizations, but if you are a small or medium business, run. I could have paid myself the \$700-\$1000/month that we ended up paying them.



Isesia M



12/19/2018

If I could give them -10 I would. We own a business and we have hired Cintas 8 months ago to get our uniforms and mats to look professional well, it has taken them 5 months to get our mats ordered, 3 months for our shirts. For past 6 months it has been horrible communication on their part, constantly over charging us, not picking up or delivering our garments. Constantly an issue. Michael and Ben have been a nightmare to deal with. I have asked them several times about the issues I am having and all I get is they are sorry. I dont need excuses I need change and someone to start delivering my clean garments. On top of these issues drivers dont ever come at the same time and when they do they aren't the most pleasant people to deal with. I REGRET doing business with them.



Gary E.



02/17/2018

most dishonest company in the industry. Over billing and I found out drivers get commission on what is put on their trucks, so you return product and still get billed. I am very worried that this happens to a small restaurant what about the huge companies that just pay their bills and not check on what they get or are billed for. My bills when from 300-500 month up to 2200. I am a small 100 seat restaurant; seriously? No remedy either.

## Cintas in Cary, Illinois - Deceitful billing

They charge you for services and product that are not delivered or wanted.

[View full review >](#)

[Comment](#)

[4](#) [0](#)



1 comment

[SparseGalapagosTortoise561](#) May 28 #1693034

Agree. Remember Cintas spelled backwards is Satanic.

Watch all aspects of billing, price increased, small incremental charges. Watch those smiling faces and hidden meanings behind to meet their own metrics.

Aug 12 [PissedConsumer1620901](#)

## Cintas in Prescott, Arizona - NOPE.

[5](#) [4](#) [3](#) [2](#) [1](#) 1.0 [Details](#)

Cintas is a joke for a company. Extremely outdated software that will generate inaccurate invoices on accounts you don't even have open with them anymore. This has been going on for months now and their "customer service" wont even respond to the reasoning why I will not pay these invalid invoices for supplies we didn't order on an account that doesn't exist. Now our account is saying "past due" on Invoices that aren't even real.

May 23 [PissedConsumer1541253](#)

## Cintas in Berkeley, California - Terrible customer service!

For one thing, prices rise every other month! They told me if I signed a contract, it would hold a price, but it didn't matter. A few months later, a price hike without telling me. The last straw is when I took a closer look at the invoice and saw that I was getting charged every month for a broom handle that was never ordered. I talked to customer service to complain, but nothing happened. G & K was much better. I finally cancelled and went to a local vendor. Much better.





# Spruce Point Interview With Uniform Industry Expert

Spruce Point spoke with a 20+ year industry expert in the uniform rental business, who worked at a competitor, and expressed a desire not to work at Cintas. We asked for his opinion on Cintas' contract billing practices and its acquisition of G&K.

Spruce Point

*"One consistent critical theme we see of Cintas in particular, but possibly industry-wide, is that contracts tend to lock customers in and then customers find out that prices are rising, automatically after certain periods of time. I mean, is this an industry that has good ability to pass on prices to customers? If you're putting through, price increases without, warning the customer, obviously that could irritate them, but there has to be some sort of pricing limit to the point where a customer might want to go somewhere else?"*

Industry  
Expert

*"Yeah, you're hitting on a good point there. And let me say, you asked me earlier if I'd like to comment about why I didn't want to work for Cintas. You're hitting on exactly why I didn't want to work for Cintas. Cintas is the 10,000 pound gorilla. They do a good job of service. I'm not going to say they don't, they do a really nice job of servicing and many times they're long term customers like them well. The ones that like to be coddled and to be personalized, do not like them at all because Cintas has one way of doing business and only one way of doing business and so for that they kind of have a reputation of being a little bit hard nose, a little bit cold. **They have a reputation of excessive billing** and their excessive billing, which is not tied to a weekly amount. It's back tied to just what you started asking about the contracts, and the things of that nature, and that the terms of the contracts is enabled them to be able to do. On a national scale that I worked from, for the last 20 years, all of my contracts were completely custom crafted. I worked directly for an attorney and we literally had a boiler plate that we offered to our customer's counsel in the beginning, but it was a back and forth, red line changes, et cetera; four, five, six times before we could come to the agreement of the language that we could all agree upon. We saw that Cintas didn't do that so much. Instead they offered a stock standard contract that had such vague terms in it so that the client didn't understand what he was agreeing to. And that is where a lot of the Cintas pain originates from."*

*"I really specialized in fire retardant clothing. And that is something that Cintas is just huge in they were the kind of the industry leader into rental of fire retardant clothing. **But their national contracts were so vague that anytime a client was unhappy with their service and wanted to exit them, it costs them such a tremendous amount of money, because again, the contract vaguely said that if we believe that this merchandise is special, you agreed to buy it.** Nowhere on that piece of paper does it say that the merchandise that I'm selling you, or I'm renting you, is considered specialty. So therefore when (customers) get ready to exit, Cintas comes to them and says, "Oh, well you owe me \$9,000 for all the goods that we put upon your people". And that then became a prohibitive to them to using other companies. **And that in itself then is where they really got the bad reputation for contracts.** Later in the years they got a little better."*

Spruce Point

*"Can I ask you your perception of the company called G&K? A couple of years ago Cintas bought G&K. What was your understanding of their reputation in the industry?"*

Industry  
Expert

*"**G&K had a terrible reputation. Cintas has the problem to fix.** G&K's service was more industrial than Cintas'. In other words, more of the welders or of the heavy construction type businesses, that sort of thing. Not so much hospitality. I think Cintas tends to have a little more hospitality, a little more health care. But I don't have much of a good opinion candidly of G&K. They were a contender. They were one of the big four that showed up always for RFPs, et cetera. And they, you know, they won their fair share, but they had some pretty ongoing serious service problems. **They didn't have a good national program at all, and what I heard most of the really bad talk from them was about their national program.** So maybe Cintas by owning them they brought them some structure in that regard, and that may have improved them somewhat"*



# Pricing Commentary From A Competitor....

Two different views on pricing, depending on which CEO you ask. Cintas sees no change, yet Unifirst sees consolidation causing disruption, customer dissatisfaction and prices tightening at big accounts.

Analyst  
Mazari  
Q4 2018 Earnings  
July 7, 2018

"The first question is just on consolidation in the space broadly. I know you've sort of outlined cost synergies. Maybe if you could touch on -- there's been another uniform deal in the space. Could you maybe touch on the revenue side? **Do you expect pricing to get better in the space post-consolidation?** I realize it's a local business, so there may be some nuances there. So maybe if you could touch on that and then how to think about G&K revenue synergies.."

Cintas CFO  
Response

**"So from the standpoint of pricing, the pricing environment, I would say, hasn't changed much in the last 90 days since we spoke last. And quite honestly, I don't expect that the consolidation that has happened will have much of an impact on the pricing environment.** It's still a very competitive environment. We face legacy like competition as well as other catalog type competitors, and so that's not going away. So I don't think that's going to have much of an impact on the pricing environment."



Cintas



Unifirst

Analyst  
Baird Conference  
June 5, 2018

"Is there anything that's changed from the competitive landscape or pricing environment or things that you found that you need to do from a scale perspective that's changed."

CEO UniFirst  
Steven Sintros

"Yeah. I think as you can imagine and we know this as much as anyone in the industry, when you do acquisitions of the size of an Arrow or even the smaller acquisitions we do; there is disruption in those local operations as you integrate the operations. In our business, to really take advantage of the synergies of these acquisitions, the route structure and the optimizing of the route structure is really very important. But that doesn't happen overnight. When you think about it, when we provide our garments to our customers; half the garments are with our customers, some of whom are with their employees at their houses, some of them are back in the plant. And when you go to reroute customers, there can be disruption on that flow of the product. So it's not something you take on very lightly. **And doing it on the scale that Cintas and Aramark will be doing it over the next couple of years is something that will lead to some disruption.** In terms of what we're seeing in the market right now, we're seeing some of that disruption. And I think customers like stability and they like knowing that their service is going to be consistent. They don't want to change route drivers and so on and so forth. So some of that is leading to opportunities, I think, for us who can offer more stability during this time. As far as pricing goes, I don't think we've seen much change in the environment. I think where there is a change most notably is on the large account selling. If you're sitting at the table with a national account which maybe has one of our competitors as the incumbent and they're looking to make a change because **there's some service dissatisfaction**, now there's really only two players at the table. So it does provide a little bit more transparency and maybe simplicity to the process. And we know who we're going against and what we might need to do and the advantages or disadvantage that we might have bidding on that account, whereas previously when there was maybe four or five people practically bidding on that account, including some larger regional players like an Arrow depending on the market; **it can lead to challenges and one of those competitors potentially coming in with a very aggressive offer. So I think that's where you may see some of the pricing tightening.** But at the same time, it's not necessarily because I think any of the competitors individually are being less aggressive than they were in the past."



# Expert Weighs In On Pricing Discussion And The “Darker Side” Of Industry Practices

When we asked the same industry expert, who admittedly worked at a competitor, and was not interested in working for Cintas, to opine on industry pricing, he revealed that prices have generally gone down, but industry players have used more aggressive tactics such as pushing nebulous fees for loss and ruin higher.

Spruce Point

***“Cintas has maintained that the pricing environment hasn't changed much or been stable throughout this whole industry consolidation period? Unifirst’s CEO, was commenting a year ago that basically, and I’m paraphrasing, service disruptions in the industry has created a change and allowed them to be more competitive and poach clients. So, I mean, do you take Cintas verbiage at face value that the pricing environment has been stable while they're trying to digest a huge acquisition of G&K?”***

Industry Expert

***“And not only that, but I'll say this, the pricing environment in the rental uniform industry is, is within 10% of where it was back in the late eighties. And I'm really not exaggerating now. Whilst loss prices have gone up substantially because merchandise cost has gone up. But as far as the unit costs for a specific type of a towel or a specific type of a format for a specific type of a uniform, it's still pretty much the same. When I began in the industry, we would see large national uniform paying about 90 cents a day or up for us, 65/35 shirt and a pants. Today that cost is more like 60 cents per man per day. It is actually gone down on some items. Some items have gone up a little bit, so it's probably about a 10% wash. But, but in regard to uniforms, it literally has gone down to the point, from competitive pressure, but guess what, the uniform companies, they're willing to do that because there's so many other ways that they can make a profit. So what I, what I call it is creative marketing. They've, they literally will, we'll dangle a carrot to get their foot in the door. And I've had, I've had GMs all through my career no matter the uniform company that I worked for, so you go get me the business. It's my job to make it profitable and the way they do that is by collecting those fees and those fees that we're talking about is for the loss and the ruining, that 30% that I was mentioning to you earlier about, that's a cost that they just can't measure very well. You can measure what I'm going to charge you for a shirt or for pants, but you can't measure the amount of times I'm going to charge you for that shirt or that pant. The sheer incident rate is the hard part in that industry. So when I would call them clients, I would tell them point blank. I'd say, are you aware that your uniform cost is not going to be this dollar but it's going to be a dollar about 25 to 30% higher at this dollar? And very often I would find clients not expecting that at all.”***

Industry Expert

***“Naturally occurring loss and ruin is around 16 to 18%... But as time evolved, and as we started hitting those numbers more and more, guess what they climbed to 28% and 30%. 30% is about the norm now. And I heard that number for years. So, I believe it's not just a single company number. I think it's pretty much an industry-wide. That's kind of the goal that most uniform companies shoot toward. Again, I have no problem collecting from customers what is naturally destroy. I have a problem going out and getting aggressive looking for it. To me, that's the era that the industry evolved into, and they did it simply by keeping their prices so low, they had to go out and find a way to make money.”***

# Under Pressure, Cintas Makes Shady Investment Sale

As we believe Cintas' cash flow quality has worsened post the acquisition of G&K, we observe that management reported the sale of a cost method investment in Q2'19, and provided no information about what was sold, and who was the buyer. However, based on the disclosure that Cintas received \$73.3m and booked a \$69.4m pre-tax gain, we estimate its book value was \$3.9m. Yet, Cintas reduced the book value of cost investments by only \$2.0m. Something doesn't seem correct here: Cintas produced a 35x cash return on investment and won't explain how.

## Quarter Before Cost Method Investment Sale

*"Investments at August 31, 2018 of \$180.3 million include the cash surrender value of insurance policies of \$160.2 million, equity method investments of \$14.9 million and cost method investments of \$5.2 million. Investments at May 31, 2018 of \$175.6 million include the cash surrender value of insurance policies of \$154.0 million, equity method investments of \$16.4 million **and cost method investments of \$5.2 million**. Investments are generally evaluated for impairment on an annual basis or when indicators of impairment exist. For the three months ended August 31, 2018 and 2017, no impairment losses were recorded. **Subsequent to August 31, 2018, Cintas reached an agreement to sell a cost method investment to a third party. The anticipated gain on the sale will be recorded upon consummation of the sale.**"*

## Quarter Of Cost Method Investment Sale

*"Investments at November 30, 2018 of \$183.5 million include the cash surrender value of insurance policies of \$165.4 million, equity method investments of \$16.9 million and cost method investments of \$1.2 million. Investments at May 31, 2018 of \$175.6 million include the cash surrender value of insurance policies of \$154.0 million, equity method investments of \$16.4 million **and cost method investments of \$5.2 million**. Investments are generally evaluated for impairment on an annual basis or when indicators of impairment exist. For the six months ended November 30, 2018 and 2017, no impairment losses were recorded. **During the three months ended November 30, 2018, Cintas sold a cost method investment to a third party. Proceeds from the sale were \$73.3 million, which resulted in a pre-tax gain of \$69.4 million.**"*

## Quarter After Cost Method Investment Sale

*"Investments at February 28, 2019 of \$191.8 million include the cash surrender value of insurance policies of \$170.2 million, equity method investments of \$18.4 million and **cost method investments of \$3.2 million**. Investments at May 31, 2018 of \$175.6 million include the cash surrender value of insurance policies of \$154.0 million, equity method investments of \$16.4 million and cost method investments of \$5.2 million. Investments are generally evaluated for impairment on an annual basis or when indicators of impairment exist. For the nine months ended February 28, 2019 and 2018, no impairment losses were recorded. During the second quarter of fiscal 2019, Cintas sold a cost method investment to a third party. Proceeds from the sale were \$73.3 million, which resulted in a pre-tax gain of \$69.4 million."*





# Cintas Increased Exposure To Oil And Gas And Mining Post G&K Acquisition

Cintas took on more exposure to the oil, gas and mining sectors with the acquisition of G&K Services. This may turn out to hurt it as pressures continue to rise with layoffs in the oil field as prices remain subdued and production falls. Various news outlets are suggesting that the oil and gas market will shed all its job gains this year and next.<sup>(1,2)</sup>

G&K Baird Conf  
June 2016

G&K Q3 2016  
Earnings Call  
April 2016

***"Oil and gas was an important segment for all of us, not just hard-core center of oil and gas but the collateral, the related businesses to it, and everybody knows that story."***

***"We continue to see significant wearer losses with oil and gas and other mining customers, and there is clearly some spillover into related markets."***

Cintas Q1 2020  
Earnings Call

Sept 24, 2019

***"What I was referring to was our customers in the oil, gas, mining areas that generally, when you see the prices of the gas at the pump come down in the past, when we've seen those prices really come down, it kind of hurts that business here in the U.S. And so the -- we saw some benefit in that price at the pump, as we said, 25 basis points in rental. But we also saw a little bit of softening in the business side of it from a customer perspective. And so that's what we're keeping our eyes on."***

Unifirst Q4 2019  
Earnings Call

Oct 23, 2019

***"One area of caution with respect to growth relates to ware accounts within our existing customers. Additions versus reductions as we commonly refer to it, which slid some in our fourth quarter, partially due to some weakening in the oil and gas sector."***

1) [Houston Oil and Gas Jobs Set To Decline Through 2020](#) – Oct 28, 2019  
2) [Employment in Texas Oil Fields Falls As Industry Contracts](#), [San Antonio Journal](#), Sept 27, 2019

# Leverage Rising And Slightly More Levered Than It Appears

As Cintas financial strain rises, it's leverage is now at a multi-year high with increasing need for short-term borrowing. We believe its leverage is even higher than optically being portrayed. Cintas' \$102m of cash on the balance sheet should not be considered freely available to pay down debt. \$57m of it is restricted and domiciled in foreign jurisdictions.

## Recent Credit Increase Shows Evidence of Strain

*"The credit agreement that supports our commercial paper program **was amended and restated on May 24, 2019. The amendment increased the capacity of the revolving credit facility from \$600.0 million to \$1.0 billion and created a new term loan of \$200.0 million.** The credit agreement has an accordion feature that provides Cintas the ability to request increases to the borrowing commitments under either the revolving credit facility or the term loan of up to \$250.0 million in the aggregate, subject to customary conditions"*

## Not All of Cintas' Cash Is Available To Freely Satisfy Debt Obligations

*"**Cash and cash equivalents.** Cintas considers all highly liquid domestic investments with a maturity of three months or less, at date of purchase, to be cash equivalents. **At May 31, 2019 and 2018, cash and cash equivalents includes \$31.4 million and \$30.9 million, respectively, of restricted cash used as collateral associated with the general insurance program. Cash and cash equivalents as of May 31, 2019 and 2018 include \$28.5 million and \$33.9 million, respectively, that is located outside of the United States.**"*

| \$ in mm                        | FY 2013          | FY 2014          | FY 2015          | FY 2016          | FY 2017          | FY 2018          | FY 2019          | 8/31/19          |
|---------------------------------|------------------|------------------|------------------|------------------|------------------|------------------|------------------|------------------|
| Cash and Equivalents            | \$358.0          | \$513.3          | \$433.2          | \$209.8          | \$191.5          | \$138.7          | \$96.6           | \$102.1          |
| Less: Restricted Cash           | (\$28.5)         | (\$33.5)         | (\$40.3)         | (\$50.6)         | (\$30.6)         | (\$30.9)         | (\$31.4)         | (\$31.4)         |
| Less: Foreign Cash              | (\$50.7)         | (\$40.2)         | (\$109.8)        | (\$96.5)         | (\$125.5)        | (\$33.9)         | (\$28.5)         | (\$25.4)         |
| <b>Total Adj. Cash</b>          | <b>\$278.8</b>   | <b>\$439.6</b>   | <b>\$283.1</b>   | <b>\$62.7</b>    | <b>\$35.4</b>    | <b>\$73.9</b>    | <b>\$36.7</b>    | <b>\$45.3</b>    |
| Total Debt                      | \$1,309.2        | \$1,301.0        | \$1,300.0        | \$1,294.4        | \$3,133.5        | \$2,535.3        | \$2,849.8        | \$3,045.5        |
| Plus: Lease Liabilities         | 209.5            | 184.5            | 98.6             | 134.0            | 176.0            | 196.7            | 223.2            | 168.7            |
| <b>Adj Total Debt</b>           | <b>\$1,518.7</b> | <b>\$1,485.5</b> | <b>\$1,398.6</b> | <b>\$1,428.4</b> | <b>\$3,309.5</b> | <b>\$2,732.0</b> | <b>\$3,073.0</b> | <b>\$3,214.2</b> |
| <b>Headline Net Debt/EBITDA</b> | 1.3x             | 0.9x             | 1.0x             | 1.2x             | 2.8x             | 1.8x             | 1.8x             | 1.9x             |
| <b>Adj. Net Debt/EBITDAR</b>    | 1.5x             | 1.2x             | 1.3x             | 1.4x             | 3.0x             | 1.9x             | 1.9x             | 2.0x             |



# Dependence On Short-Term Financing Rising

Cintas credit facility size has tripled from \$300m (pre G&K) to now \$1.0 billion, despite the size of sales only growing ~40% and accounts receivable by 67%. Historically, Cintas did not use its commercial paper program for funding. However, recently its usage has been steadily growing.

FY  
2016

***"Cintas' commercial paper program has a capacity of \$300.0 million that is fully supported by a backup revolving credit facility through a credit agreement with its banking group. This revolving credit facility has an accordion feature that allows for a maximum borrowing capacity of \$450.0 million. The revolving credit facility was amended on May 29, 2014 to extend that maturity date from October 6, 2016 to May 28, 2019, to adjust the applicable margin used to calculate the interest payable on any outstanding loans, and to adjust the facility fee payable under the agreement. In June 2016, the revolving credit facility was amended to extend the maturity date from May 28, 2019 to June 22, 2021, increase the capacity to \$450.0 million, and add an accordion feature that allows for a maximum borrowing capacity of \$600.0 million. We believe that this program, along with cash generated from operations, will be adequate to provide necessary funding for our future cash requirements. No commercial paper or borrowings on our revolving credit facility were outstanding at May 31, 2016 or 2015."***

FY  
2017

***The credit agreement that supports our commercial paper program was amended on September 16, 2016. The amendment increased the capacity of the revolving credit facility from \$450.0 million to \$600.0 million and added a \$250.0 million term loan facility. The \$150.0 million increase in the revolving credit facility took effect upon the consummation of the merger (Merger) contemplated by the Merger Agreement among the Cintas, G&K and Bravo Merger Sub, Inc. (Merger Sub), a wholly-owned subsidiary of Cintas. The term loan was funded upon the consummation of the Merger. The credit agreement has an accordion feature that provides Cintas the ability to request increases to the borrowing commitments under either the revolving credit facility or the term loan of up to \$250.0 million in the aggregate, subject to customary conditions. The maturity date of the agreement is September 15, 2021. As of May 31, 2017, there was \$50.5 million of commercial paper outstanding with a weighted average interest rate of 1.24% and maturity dates less than 30 days and no borrowings on our revolving credit facility. No commercial paper or borrowings on our revolving credit facility were outstanding at May 31, 2016***

FY  
2019

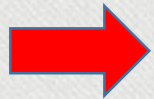
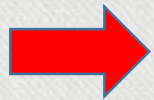
***The credit agreement that supports our commercial paper program was amended and restated on May 24, 2019. The amendment increased the capacity of the revolving credit facility from \$600.0 million to \$1.0 billion and created a new term loan of \$200.0 million. The credit agreement has an accordion feature that provides Cintas the ability to request increases to the borrowing commitments under either the revolving credit facility or the term loan of up to \$250.0 million in the aggregate, subject to customary conditions. The maturity date of the revolving credit facility is May 22, 2024, and the maturity date of the term loan is May 22, 2020, which can be extended 12 months, annually, for up to four years. As of May 31, 2019, there was \$112.5 million of commercial paper outstanding with a weighted average interest rate of 2.7% and maturity dates less than 30 days and no borrowings on our revolving credit facility. No commercial paper or borrowings on our revolving credit facility were outstanding at May 31, 2018***

Q1 2020

***As of August 31, 2019 and May 31, 2019 there was \$139.0 million and \$112.5 million of commercial paper outstanding with maturity dates less than 30 days and with a weighted average interest rates of 2.36% and 2.68%, respectively. There were no borrowings on our revolving credit facility as of August 31, 2019 and May 31, 2019.***

# Can't Be Good For Margins When....

“Support” and “Accounting” job openings growth are the biggest needs.



| Job openings growth | 3m   | 6m    | 1y     |
|---------------------|------|-------|--------|
| ● Operations        | ▼ 2% | ▼ 2%  | ▲ 37%  |
| ● Support           | ▲ 8% | ▲ 19% | ▲ 65%  |
| ● Sales             | ▼ 8% | ● 0%  | ▲ 38%  |
| ● Accounting        | ▼ 4% | ▼ 8%  | ▲ 129% |
| ● Other             | ● 0% | ▲ 7%  | ▼ 27%  |
| Total               | ● 0% | ▲ 6%  | ▲ 15%  |





## *Dubious “Beat And Raise” Story Designed To Fool Computers, Not Spruce Point*



# Evidence Suggests Cintas Engineers Its Guidance To Make It Appear As If It's Outperforming Expectations

A classic example of earnings management is when management over-estimates expenses, and claims great performance when results are better than expected. A brazen example is when Cintas offered guidance for intangible amortization expenses related to G&K. Cintas twice cut the estimate of intangible asset amortization. In its first pro-forma G&K disclosure, it estimated \$68.5m and said the contracts had a 10 year estimated life.

Cintas Corporation + G&K Services, Inc.  
Unaudited Pro Forma Consolidated Statements of Income  
(In thousands except per share data)  
Twelve Months Ended

|  | Cintas Corporation<br>May 31,<br>2016 | G&K Services, Inc.<br>July 2,<br>2016 | Adjustments | Total       |
|--|---------------------------------------|---------------------------------------|-------------|-------------|
| Revenue:                                     |                                       |                                       |             |             |
| Uniform rental and facility services         | \$3,777,801                           | \$ 978,041                            | —           | \$4,755,842 |
| Other  | 1,127,657                             | —                                     | —           | 1,127,657   |
| Total revenue                                | 4,905,458                             | 978,041                               | —           | 5,883,499   |
| Costs and expenses:                          |                                       |                                       |             |             |
| Cost of uniform rental and facility services | 2,106,793                             | 643,067                               | —           | 2,749,860   |
| Cost of other                                | 668,795                               | —                                     | —           | 668,795     |
| Selling and administrative expenses          | 1,348,122                             | 212,334                               | 68,573 f    | 1,629,029   |
| Operating income                             | 781,748                               | 122,640                               | (68,573)    | 835,815     |

(f) Amortization of intangible assets for customer contracts - The unaudited pro forma condensed consolidated statements of income for all periods include an adjustment for the amortization of newly acquired intangible assets related to customer contracts, net of the current amortization of G&K Services for customer contracts. Intangible assets related to customer contracts are estimated to have a useful life of 10 years and will be amortized on a straight-line basis over that period.

Source: Cintas [8-K](#) 3/6/17





# Evidence Suggests Cintas Misguided Expenses To Inflate EPS

Four months later on the conference call, Cintas offered guidance of \$50m of intangible amortization expenses, down from the \$68m estimate originally provided. Yet, by closely evaluating the 10-K that was filed shortly after the conference call, it's clear that management should have given \$40m of guidance. Actual amortization was reported at \$38.9m. Thus, we can say with confidence that management issued an inaccurate measure of amortization expense, potentially to misguide investors to optically deliver better results. The net benefit to FY 2018 EPS from this expense mismanagement was \$0.24, or approximately 3.5%.

CFO  
Q4 2017  
Earnings Call  
  
July 20, 2017

*"Our guidance includes the following assumptions related to the acquired G&K business: no transaction and integration expenses; revenue of \$870 million to \$900 million, compared to a prior year run rate of \$965 million; synergies of approximately \$50 million to \$55 million; **purchase price amortization expense related to intangible assets of \$50 million**; interest expense on G&K acquisition debt of about \$65 million; and an EPS contribution of \$0.15 to \$0.17."*

The table below sets forth the preliminary valuation and amortization period of identifiable intangible assets:

| Identifiable intangible assets: | Preliminary Valuation | Amortization Period |
|---------------------------------|-----------------------|---------------------|
| Service contracts               | \$ 519,000            | 15 years            |
| Trade names                     | 17,000                | 3 years             |
| <b>Total</b>                    | <b>\$ 536,000</b>     |                     |

Cintas estimated the preliminary fair value of the acquired property, plant and equipment using a combination of the cost and market approaches, depending on the type of asset. The preliminary fair value of property, plant and equipment consisted of real property of \$141.8 million and personal property of \$112.2 million.

Source: FY 2017 [10-K](#) p.54 Filed 7/31/17

## Management Should Have Said \$40m

| \$ in mm                 | Amt. (A)     | / (B) Term        | = (C) Annual Amortization |
|--------------------------|--------------|-------------------|---------------------------|
| <b>Service Contracts</b> | \$519        | 15 <sup>(1)</sup> | \$34.6                    |
| <b>Trade Names</b>       | \$17         | 3                 | \$5.7                     |
| <b>Total</b>             | <b>\$536</b> |                   | <b>\$40.3</b>             |

1) Note the original amortization period was 10yrs, and then increased to 15yrs

Increase in annual amortization only \$38.9m which is very close to our estimate of \$40.3m, and well below the original \$68m (then \$50m) guidance issued by management

|   | Fiscal Years Ended May 31, |            |           |
|---|----------------------------|------------|-----------|
| (In thousands)  | 2018                       | 2017       | 2016      |
| Cash flows from operating activities:   |                            |            |           |
| Net income  | \$842,586                  | \$ 480,708 | \$693,520 |
| Adjustments to reconcile net income to net cash provided by operating activities: |                            |            |           |
| Depreciation  | 215,476                    | 171,565    | 149,691   |
| Amortization of intangible assets   | 63,940                     | 25,030     | 15,588    |

# Evidence Suggests That Cintas Spring-Loaded G&K's Financial Results

Commentary from G&K and its financial projections illustrated how it expected to achieve approximately 3.5% - 5.3% annual revenue growth from 2016 – 2018. Yet, when Cintas issued guidance for FY 2018 including G&K, it implied a -4.2% annual revenue decline at the guidance midpoint! Pay close attention, and notice that CTAS' revenue guidance was ~\$165 - \$195m below G&K projections.

**G&K CEO**  
Discussing Revenue  
Outlook At Baird  
Conference

June 9, 2016

*"We're not yet giving our 2017 guidance in total but we did give some light on how we thought the top-line might shape up. And what we said is, **it'll be at the low-end of the organic revenue range you've seen from us in the last several years**. So, that was the qualitative comment. **So, I can put numbers around that, our organic growth rate has ranged from 3.5% to 6.5% over the last call it three years**"*

**G&K Standalone**  
**Projections**  
Imply 4.3% and 6.4%  
Revenue Growth In  
2017 and 2018

Per Proxy (1)  
Sept 14, 2016

## Summary of the G&K Projections

(dollars in millions, except per share data)

|                                | Projected Fiscal Year |         |         |         |         |         |
|--------------------------------|-----------------------|---------|---------|---------|---------|---------|
|                                | 2016(1)               | 2017    | 2018    | 2019    | 2020    | 2021    |
| Total Sales                    | \$ 960                | \$1,001 | \$1,065 | \$1,133 | \$1,210 | \$1,293 |
| EBITDA(2)                      | \$ 155                | \$ 169  | \$ 194  | \$ 218  | \$ 239  | \$ 260  |
| Operating Income               | \$ 123                | \$ 130  | \$ 149  | \$ 169  | \$ 187  | \$ 211  |
| Adjusted Net Income(3)         | \$ 70                 | \$ 74   | \$ 86   | \$ 98   | \$ 109  | \$ 124  |
| Adjusted Earnings Per Share(3) | \$ 3.49               | \$ 3.78 | \$ 4.44 | \$ 5.15 | \$ 5.84 | \$ 6.71 |
| Unlevered Free Cash Flow(4)    | \$ 64                 | \$ 66   | \$ 69   | \$ 97   | \$ 109  | \$ 122  |

**Cintas CEO**  
Giving FY 2018  
Guidance For The  
First Time Including  
G&K Services

July 20, 2017



***"And finally, we are excited about our recent acquisition of G&K. Preliminary results are very encouraging. We are on track to meet our financial and non-financial objectives and look forward to the many opportunities G&K provides"***

***"Our guidance includes the following assumptions related to the acquired G&K business: no transaction and integration expenses; revenue of \$870 million to \$900 million, compared to a prior year run rate of \$965 million"***



# “Beat And Raise” Story Not As Strong As It Actually Appears

Cintas raised revenue guidance twice in 2018. The final revenue figure outperformed initial guidance by the amount of G&K revenue that was talked-down. At best a pure coincidence, or at worst highly engineered results designed to portray great outperformance.

| \$ in mm                   | Q4 17<br>7/20/17  | Q1 18<br>9/6/17  | Q2 18<br>12/21/17  | Q3 18<br>12/21/17   | Full Year<br>Actual   |
|----------------------------|-------------------|--|--|---|---|
| Sales Guidance             | \$6,270 - \$6,360 | \$6,325 - \$6,400  | \$6,365 - \$6,430  | Didn't Provide Full Year Guidance.<br>Issued Q4:<br>\$1,625 - \$1,645 |   |
| Midpoint of Sales Guidance | \$6,315           | \$6,362  | \$6,398  | --  | \$6,476.6<br>Actual Results<br>+\$161m<br>Higher Than Initial<br>Guidance |

Recall on the [previous slide](#), G&K revenue guidance was suppressed ~\$165-\$195 below G&K projections. Is it a coincidence that Cintas actual results came in above the initial range by an amount close to the reduced G&K revenue?

## Red Flag: Cintas Says One Thing And Does Another Thing On Capital Priorities To Inflate Results

Cintas repeatedly claimed in 2019 that capex, acquisitions, dividends and lastly share repurchase were its capital priorities. Yet, with capex stated as the #1 priority, it cut its capex guidance three times, and share repurchases soared to \$1bn – making repurchases clearly the largest capital priority despite management saying otherwise.

Cintas CFO  
Q4 2018  
Earnings Call  
July 19, 2018

*“One important area in which fiscal '19 will differ from fiscal '18 is in capital allocation. With \$600 million of acquisition debt repaid and our leverage target achieved, **we returned to our historical priorities for deployment of cash, which our CapEx, acquisitions, dividend payments and share repurchases.**”*

Cintas CFO  
Q1 2019  
Earnings Call  
Sept 25, 2018

*“Yeah. I would say the capital allocation is similar to a pre-G&K acquisition philosophy and that is we want to grow organically and we are going to invest in the business in the way that that we need to in order to continue to grow. **That means CapEx will be important for us** both in adding plant capacity, adding route capacity and other system investments...**We love tuck-in acquisitions** and acquisitions that are in our current businesses. And so, we will continue to look for those kinds of opportunities...**We have raised our dividend for every year since we went public. I would expect that we will evaluate then that and that's very important to us.** And then, **if we have additional cash and we have an opportunity to be opportunistic with that cash, we will execute on the buyback program.**”*

Cintas CFO  
Q3 2019  
Earnings Call  
March 21, 2019







*“**Our CapEx, I would expect to continue, kind of, in that 4% to 4.5% range and that's very important to us. Aside from that, we certainly love the tuck-in acquisitions and we'll continue to look for opportunities there** as best we can in our rental First Aid and Fire businesses. **And then there may be a buyback opportunity.** And as we've shown so far this fiscal year where we've acquired almost \$550 million through our first three quarters, we like that program, we like the momentum of the business and I would expect that we'll continue to look at that opportunistically.”*



# Cintas Says One Thing And Does Another Thing On Capital Priorities To Inflate Results (Cont'd)

For Q4'19 Cintas explicitly guided to no repurchases, yet conducted its biggest buyback in Q4'19. Cintas originally guided to \$7.00 - \$7.15 of EPS from continuing operations (ex: items) in FY 2019, and kept raising guidance all year to end at \$7.60. However, we believe financial and accounting gamesmanship accounted for more than the earnings beat for the year management proclaimed was a "very successful year".

## Progression of FY 2019 Guidance by Quarter

| \$ in mm                  | Q4 2018         | Q1 2019   | Q2 2019   | Q3 2019   | Q4 2019     | FY 2019   |
|---------------------------|-----------------|---|---|---|-------------|-----------|
| Continuing EPS (ex items) | \$7.00 - \$7.15 | \$7.19 - \$7.29  | \$7.30 - \$7.38  | \$7.42 - \$7.48  | --          | \$7.60    |
| Tax Rate                  | 21.7%           | 21.7%   | 21.7%   | 20.6%            | --          | 19.9%     |
| Capex Guidance            | \$290 - \$320   | \$275 - \$300    | \$270 - \$285    | \$270 - \$285   | --          | --        |
| Actual Capex              | --              | \$64.5  | \$73.1  | \$70.2  | \$68.9      | \$276.7   |
| Acquisitions              | --              | \$7.6   | (\$1.0)   | \$0.8   | \$2.4       | \$9.8     |
| Dividend                  | --              | \$0.0   | \$0.0   | \$220.7   | \$0.0       | \$220.7   |
| Share Repurchases         | --              | \$139.5   | \$368.7   | \$99.9  | \$408.3 (1) | \$1,016.3 |

1) In [Q3'19](#), Cintas issued guidance assuming no future share repurchases. Yet, it's largest repurchase came in the following quarter

# When Asked About Share Buybacks, Management Gave A Ridiculous Response

Management won't admit it uses stock buybacks to manage market expectations and to engineer low quality "beat and raises" stories to get analysts giddy. Instead management spins a non-sensical explanation of its share repurchase strategy calling it "*consistently inconsistent*". This should hardly inspire any confidence from investors.

Analyst Shlomo

Q1 2020  
Earnings Call

*"Usually when companies don't buyback stock and their leverage is below the level that the -- consider a target level there is usually something that is a potential out there, is that an unfair assumption for us to make that there might be something in the near to intermediate term?"*

Cintas CFO  
Response To  
Question About Its  
Buyback Strategy

Q1 2020  
Earnings Call

*"We've always looked at that buyback as we've executed as an opportunistic program. And if you go back over the course of the last 10 years, **we are not consistent from quarter-to-quarter and that's by design.** We kind of look at a bunch of different things. We look at the performance of the business, the investment needs of the business. We look at M&A opportunities on the horizon. We look at things like upcoming dividends **and we have a consistent history of not being consistent in the way that we execute on that buyback program. And I'm not sure I look into anything more than that.**"*



## *In Our View, 2019 Had No Outperformance Relative To Initial Guidance*

We estimate that, at best, EPS would have been flat or modestly down without Cintas' crafty financial and accounting gamesmanship that involved lowering its tax rate, redirecting capital towards share repurchases despite repeatedly saying it was the lowest capital priority, and lowering amortization expense for G&K service contracts.

| \$ in mm                                      | Initial FY 2019 Guidance | Actual FY 2019 | Note   |
|---|--------------------------|----------------|--|
| Continuing EPS (ex items)                     | \$7.00 - \$7.15          | \$7.60         | On the surface, management beat its initial guidance by 7% at the midpoint   |
| Less: Tax Rate Benefit                        |                          | (\$0.18)       | Cintas cut its tax guidance from 21.7% to 19.9% actual   |
| Less: Net Benefit From \$1bn Share Repurchase |                          | (\$0.23)       | Cintas talked down repurchases all year, only to spend \$1bn to retire 5.1m shares. Initial share count guidance was 114m. We assume interest 1% would have been earned on cash absent repurchases |
| Less: Incremental Amortization Expense        |                          | (\$0.20)       | Reduction of G&K contract amortization expense from \$68m to \$40m   |
| <b>Spruce Point Pro Forma Adjusted EPS</b>    |                          | <b>\$6.99</b>  | <b>We estimate that, at best, EPS would have been flat or modestly down without Cintas' crafty financial and accounting gamesmanship</b>   |



## *Governance And Auditor Concerns*



# Numerous Governance Shortfalls For An “S&P 500 Caliber” Company

Institutional investors should demand greater governance standards from Cintas Corp.



## **Chairman And CEO Roles Not Separated**

- Best practices dictate the separation of Chairman and CEO roles, but Cintas has repeatedly rebuffed this claiming that Farmer provides invaluable leadership and direction for the success of the Company
- Yet, Spruce Point sees no evidence management has been held accountable for Cintas’ weakening financial profile with the acquisition of G&K. Instead, the Board granted a special bonus to executives claiming it was a successful deal, and management has been receiving double digit salary increases. Furthermore, the compensation committee appears willing to grant management bonuses purely for income generated by implementing accounting policy changes



## **Questionable Business Links And Relationships Between Directors Compromise Objectivity**

- The CEO is the brother-in-law of Director Coletti and directs business to Coletti’s law firm
- Newly appointed audit Director Carnhan is a long-time former employee of Cintas, and sits on the Board of another audit Director’s company, and is likely paid



## **Pledging of Stock Allowed By Executives**

- Both CEO Farmer, and Director Coletti’s spouse (a relative of Farmer), have been allowed to pledge stock, which is typically frowned upon among better governed companies



## **Connections Between Management And 50 Year Auditor Relationship**

- E&Y has been Cintas’ auditor for 50 years. Investors should demand the appointment of a new auditor to take a fresh inspection of its books and records. Cintas audit engagement partner also audited Papa John’s. Subsequent to his departure, Papa John’s new auditor disclosed a “material weakness of financial controls” warning
- Both Cintas’ CFO and Treasurer worked at E&Y, which could compromise the objectivity and independence required between client and auditor

# *It's Time For An Auditor Change And Fresh Independent Evaluation of Cintas' Books*

Spruce Point is concerned with the closeness of Cintas with its auditor E&Y. The relationship dates back over 50 years, and both the current CFO and Treasurer worked there. It's time for a new auditor and a fresh look at Cintas' books.

## **E&Y Lauds Founder Farmer With An Award**

Farmer was inducted into the Greater Cincinnati Business Hall of Fame in 1996, named Ernst & Young's Entrepreneur of the Year in 1995, and honored by the Cincinnati USA Regional chamber in 2010 as one of the Great Living Cincinnatians. He is the recipient of Doctor of Laws degrees from Miami University and Xavier University, CEO of the Year awards from *Financial World* magazine in 1994 and 1995, and the 1992 Executive of the Year Award from Sales and Marketing Executives Cincinnati. In 1999, United Way of Greater Cincinnati thanked Farmer for his steady friendship by presenting him with its Alexis de Tocqueville Society Award.

Source: [Miami Ohio](#)

## **E&Y As Auditor for More Than 50 Years**

/s/ ERNST & YOUNG LLP

We have served as the Company's auditor since 1968  
Cincinnati, Ohio  
July 26, 2019

Source: Cintas [10-K](#)

## **Cintas CFO Worked At E&Y**

### **J. MICHAEL HANSEN**

Mike Hansen joined Cintas in October, 1995, as Treasury Manager, after previous positions with Ernst & Young and Rockwell International. Mike has served Cintas in many roles including: First Aid Controller, Global Accounts Controller in Chicago, General Manager of the Cincinnati Fire Location, Corporate Controller and Vice President and Treasurer. Mike was promoted to Vice President – Finance and Chief Financial Officer on February 1, 2015, responsible for the company's accounting and finance functions. Mike was promoted again to Executive Vice President and Chief Financial Officer in July 2018.

Source: Cintas Biography on [website](#)

## **Cintas VP / Treasurer Also From E&Y**

Adler joined Cintas in 1997 as a Corporate Development Analyst, and has also held the roles of National Accounts Controller, Global Supply Chain Controller, Rental Division Controller and most recently Corporate Controller.

Adler is a 1993 graduate of the University of Dayton and began his career at Ernst & Young in Cincinnati.

Cintas [Press Release](#)

Note: His website [biography](#) omits his role at E&Y



# Cintas' Audit Partner Linked To Papa John's Accounting Fiasco

Cintas' audit engagement partner at Ernst & Young is Craig Andrew Marshall. Mr. Marshall is also the audit engagement partner at Papa John's International (Nasdaq: PZZA).<sup>(1)</sup> Papa John's dismissed E&Y in 2018. Since hiring KPMG, Papa John started to disclose material weaknesses of financial control over financial reporting. Papa John's has since dismissed KPMG and re-hired E&Y.<sup>(2)</sup>

## Papa John's Dismisses E&Y, Hires KPMG

### Change in our Certifying Accountant for 2018

The Audit Committee of the Board of Directors has selected KPMG as the Company's independent auditors, to audit the consolidated financial statements of the Company for the fiscal year ending December 30, 2018. Ernst & Young has audited the Company's consolidated financial statements since 1990, including the fiscal years ended December 31, 2017 and December 25, 2016.

Source: Papa John [Proxy](#) – March 2018

## Papa John's Notes A Material Weakness Under KPMG

### (c) *Changes in Internal Control over Financial Reporting*

During the quarter ended December 30, 2018, management remediated an identified material weakness in internal control over financial reporting related to the review of manual journal entries. No misstatement arose as a result of this deficiency. For the year ended December 30, 2018, management remediated the material weakness by adding controls over the review and approval of manual journal entries. The Company will continue to monitor these new controls and implement additional enhancements in 2019.

Source: Papa John [10-K](#) – Feb 2019

## Material Weakness Issue Escalates Under KPMG With An Amended 10-K Filing

Papa John's International, Inc. (the "Company") is filing this Amendment No. 1 on Form 10-K/A (this "Amendment") to its Annual Report on Form 10-K for the fiscal year ended December 30, 2018, originally filed with the Securities and Exchange Commission ("SEC") on March 8, 2019 (the "Original Filing") to amend Item 8 of Part II, "Financial Statements and Supplementary Data" and Item 9A of Part II, "Controls and Procedures," related to (1) our conclusions regarding the effectiveness of our disclosure controls and procedures and internal control over financial reporting and (2) KPMG LLP's related opinion on management's assessment of our internal control over financial reporting. We are also filing as exhibits currently dated certifications by our Chief Executive Officer and Chief Financial Officer and an updated Consents of Independent Registered Public Accounting Firms. For the convenience of the reader, this Amendment sets forth the Original Filing in its entirety, as amended to reflect these changes. No attempt has been made in this Amendment to update other disclosures presented in the Original Filing.

Subsequent to the Original Filing, the Company's management re-evaluated the effectiveness of our internal control over financial reporting and determined that our internal control over financial reporting was not effective as of December 30, 2018 due to the identification of material weaknesses in our internal control over financial reporting relating to the consolidation of a variable interest entity ("VIE"), as described below. The relevant accounting literature governing VIEs is highly complex and requires the exercise of significant judgment in determining whether an entity is a VIE and whether that VIE should be consolidated. This evaluation included consideration of an error related to our VIE consolidation accounting for the Papa John's Marketing Fund, Inc. ("PJMF"), which had not been consolidated since its inception in 1991, as historically disclosed in the notes to the Company's consolidated financial statements. The Company has determined that it is appropriate to consolidate PJMF in its consolidated financial statements. As a result of these material weaknesses, we have restated our report on internal control over financial reporting from the Original Filing, and we have also concluded that our disclosure controls and procedures were not effective as of December 30, 2018. See Item 9A of Part II, "Controls and Procedures."

Source: Papa John [10-K/A](#), May 2019

1) [PCAOB record](#) for Craig Andrew Marshall

2) KPMG dismissed, E&Y rehired [8-K](#)

# Dubious EPS To Reap Unjust Bonuses

Cintas' annual incentive plan is based on sales and EPS growth, along with non-financial goals. In 2019, 41.75% of CEO Farmer's bonus was tied to EPS performance while for most other executives, it accounted for 50% of the bonus. Cintas conveniently achieved almost the maximum EPS target within one penny, and claims its \$7.60 EPS took into consideration various one-time items. We will demonstrate why we believe this to be inaccurate.

*The Grants of Plan-Based Awards for Fiscal 2019 table outlines estimated possible payouts under this non-equity incentive plan award. Based on Cintas' EPS and sales growth for fiscal 2019, Mr. Farmer and Mr. Schneider earned an annual cash incentive payout of \$1,726,322 and \$934,552, respectively. **The fiscal 2019 Cintas EPS used in the incentive plan calculations was \$7.60. This EPS figure differs from the Company's reported diluted EPS from continuing operations because it takes into consideration various one-time, extraordinary financial impacts that occurred during the fiscal year, which consisted of acquisition-related integration expenses and a gain on the sale of an equity method investment.***

The potential annual cash incentive payout percentage multiplier for each component of Mr. Farmer's and Mr. Schneider's target annual cash incentive is provided in the following tables (for each participating named executive officer, annual cash incentive payouts are interpolated on a straight-line basis for achievement between the levels of achievement established for all components of the annual cash incentives):

| EPS Component Level of Achievement | EPS Goals | Annual Cash Incentive Payout |
|------------------------------------|-----------|------------------------------|
| Below Threshold                    | <\$6.81   | 0%                           |
| Threshold                          | \$6.81    | 25%                          |
| Target                             | \$7.14    | 100%                         |
| Maximum                            | \$7.61    | 200%                         |

Source: 2019 [Proxy Statement](#), p. 46

|  | Twelve Months Ended |              |                    |
|--|---------------------|--------------|--------------------|
|  | May 31, 2019        | May 31, 2018 | Growth vs. FY 2018 |
| EPS - continuing operations              | \$ 7.97             | \$ 7.03      |                    |
| G&K integration expenses                 | 0.10                | 0.26         |                    |
| One-time cash payment to employees       | —                   | 0.24         |                    |
| Non-recurring gain on sale of investment | (0.47)              | —            |                    |
| One-time deferred tax benefit of Tax Act | —                   | (1.59)       |                    |
| EPS excluding above items                | <b>\$ 7.60</b>      | \$ 5.94      | 27.9%              |

Scott D. Farmer, Cintas' Chairman and Chief Executive Officer, stated, "We are pleased with these fourth quarter financial results which conclude a very successful year. For the ninth consecutive year, our organic revenue growth was in the mid- to high- single digits and EPS grew double digits when adjusted for one-time and special items. Additionally, our strong cash flow and balance sheet enabled us to deploy cash to increase shareholder value. In fiscal 2019 we paid an annual dividend of \$220.8 million that increased 26.5% over the prior year, and we purchased 4.8 million shares of company stock in a total amount of \$953.4 million."

Source: Fiscal Year 2019 results [press release](#)



# Dubious EPS To Reap Unjust Bonuses (Cont'd)

In FY 2019, Cintas adopted a new revenue recognition method that boosted pre-tax income by \$22.3m and Diluted EPS by \$0.15 cents. Why wasn't this considered a "one-time" or "extraordinary" boost to income?

| Consolidated Statement of Income<br>(In thousands) | Fiscal year ended May 31, 2019 |                           |                                |
|--|--------------------------------|---------------------------|--------------------------------|
|  | As Reported                    | Under Historical Guidance | Impact of Adopting ASU 2014-09 |
| Revenue:   |                                |                           |                                |
| Uniform rental and facility services               | \$ 5,552,430                   | \$ 5,557,056              | \$ (4,626)                     |
| Other  | 1,339,873                      | 1,337,954                 | 1,919                          |
| Total revenue                                      | 6,892,303                      | 6,895,010                 | (2,707)                        |
| Costs and expenses:                                |                                |                           |                                |
| Cost of other                                      | 736,116                        | 735,703                   | 413                            |
| Selling and administrative expenses                | 1,980,644                      | 2,006,134                 | (25,490)                       |
| Operating income                                   | 1,133,534                      | 1,111,164                 | 22,370                         |
| Income before income taxes                         | 1,102,399                      | 1,080,029                 | 22,370                         |
| Income taxes                                       | 219,764                        | 214,306                   | 5,458                          |
| Income from continuing operations                  | 882,635                        | 865,723                   | 16,912                         |
| Net income   | \$ 884,981                     | \$ 868,069                | \$ 16,912                      |
| Diluted earnings per share                         | \$ 7.99                        | \$ 7.84                   | \$ 0.15                        |

Source: FY 2019 [10-K](#) p. 25

|  | Twelve Months Ended |              |                    |
|--|---------------------|--------------|--------------------|
|  | May 31, 2019        | May 31, 2018 | Growth vs. FY 2018 |
| EPS - continuing operations              | \$ 7.97             | \$ 7.03      |                    |
| G&K integration expenses                 | 0.10                | 0.26         |                    |
| One-time cash payment to employees       | —                   | 0.24         |                    |
| Non-recurring gain on sale of investment | (0.47)              | —            |                    |
| One-time deferred tax benefit of Tax Act | —                   | (1.59)       |                    |
| EPS excluding above items                | \$ 7.60             | \$ 5.94      | 27.9%              |

Source: FY 2019 [Cintas earnings release](#)

Why Wasn't The \$0.15 Cents Benefit From ASU Adoption Called Out As A Driver of EPS Growth?

## Warning: When Given Bonuses For Deals

In light of all our concerns about Cintas overpaying for G&K, increasing the financial stress to the overall pro-forma company, and management using aggressive measure to manage Wall Street expectations in a way to make itself look like business is improving, we find it absurd that Cintas claimed the deal was a “success”.

Cintas paid special cash bonuses to management for what Spruce Point believes is a terrible deal.



*At the discretion of the Compensation Committee, bonuses can be paid outside the Management Incentive Plan, typically to reward exceptional outcomes and successes in extraordinary business situations. In fiscal 2018, **as a result of their significant involvement and success with the fiscal 2017 acquisition of G&K**, Mr. Hansen and Mr. Frooman each received a discretionary cash bonus of \$132,500. The Compensation Committee arrived at \$132,500 by considering the extra effort, time commitment and individual expertise that was required of Mr. Hansen and Mr. Frooman to successfully close the transaction, which led to additional revenues and profits for the Company.*

Source: [Proxy](#) p. 19



# *Convenient Time For The COO And Chairman Emeritus To Retire*

Cintas patriarch Richard Farmer retired from the Board in August 2018, while COO and 22 year veteran J. Phillip Holloman also left Cintas. In light of our belief that the core business is struggling, it would appear to be a natural time for each person to coast into retirement.

## **First The COO Retires**

June 15, 2018 04:00 PM Eastern Daylight Time

CINCINNATI--(BUSINESS WIRE)--Cintas Corporation (NASDAQ: CTAS) today announced that J. Phillip Holloman has informed the company of his intention to retire as President and Chief Operating Officer effective July 31, 2018.

"I thank Phillip for the tremendous contributions he has made during his many years with Cintas. Those of us who have had the privilege of working with Phillip know that Cintas is a better company because of him and he will be missed"

 [Tweet this](#)

Mr. Holloman has been with Cintas for 22 years and has held many positions including Vice President of Engineering/Construction, Vice President of Distribution/Production Planning, Executive Champion of Six Sigma Initiatives, Senior Vice President of Global Supply Chain Management, Rental Division President & COO and President & COO. Mr. Holloman is a founding member of Cintas' Diversity Committee and also received the Excalibur Award, the company's highest award reserved for business executives who demonstrate excellence during their tenure.

Source: [Company Press Release](#)

August 03, 2018 08:30 AM Eastern Daylight Time

CINCINNATI--(BUSINESS WIRE)--Cintas Corporation (NASDAQ: CTAS) today announced that Richard T. Farmer has informed the company's board of directors that he will not seek re-election to Cintas' board. Mr. Farmer will retain the chairman emeritus title but will not take part in board meetings or other activities after October 30, 2018.

Source: [Company Press Release](#)

## **And Then Chairman Farmer Steps Back From The Board**

# Audit Committee Expanded With Questionably “Independent” Former Treasurer

In light of our belief Cintas is experiencing operational and financial stress, we find it interesting that former Treasurer Karen Carnahan just joined the Board, and notably the Audit Committee. She is claimed to be an “independent director”, and while technically having been removed from Cintas for three years this may be true, we are concerned that she has been affiliated with Cintas for 30 years. Furthermore, Ms. Carnahan was just appointed on May 15, 2019 as a Trustee of Touchstone Investments (a member of Western & Southern Financial). Cintas other audit director John F. Barrett is the CEO of Western & Southern. Touchstone Trustees typically earn \$128k - \$152k per year.<sup>(1)</sup>  
Could this impair her judgement to act independently?

**In Our Opinion,  
Ms. Carnahan Is Not  
Entirely Independent**

**Karen L. Carnahan**<sup>(2)(4)</sup>  
65

Karen L. Carnahan was appointed a Director of Cintas in fiscal 2020 and is recommended as a Director nominee by the Nominating and Corporate Governance Committee. Ms. Carnahan was recommended to the Nominating and Corporate Governance Committee by Mr. Scott D. Farmer, our Chief Executive Officer. Ms. Carnahan was an employee-partner of Cintas for more than 30 years, where she served at an executive level for more than 20 years, including the roles of Vice President and Treasurer, Vice President of Corporate Development and President and Chief Operating Officer of Cintas' document management division. In 2014, Ms. Carnahan joined Shred-it International Inc. (Shred-it) as chief operating officer when Cintas' document management business merged with Shred-it, from which she then retired in 2015. Ms. Carnahan is on the Board of Trustees of Touchstone Investments (a member of Western & Southern Financial Group) and is a member of the Board of Directors of the Boys & Girls Club of West Chester/Liberty. In addition, Ms. Carnahan has received several prestigious awards including being named a Woman of Excellence by the West Chester, Ohio Chamber Alliance in 2007, a Greater Cincinnati YWCA Career Woman of Achievement in 2009 and receiving the Ohio Diversity Council's Glass Ceiling Award in 2013. The Board believes that Ms. Carnahan's understanding of Cintas through her many years as a trusted employee-partner at Cintas, her status as an independent director and the fact that she is an "audit committee financial expert" under SEC guidelines, makes her service on the Board beneficial to Cintas.

**Is Ms. Carnahan Likely  
To Rock the Boat On  
The Audit Committee If  
She's Being Paid By  
Mr. Barrett's Company?**

**John F. Barrett**<sup>(2)(4)</sup>  
70

John F. Barrett was elected a Director of Cintas in 2012. Mr. Barrett is the Chairman, President and Chief Executive Officer of Western & Southern Financial Group, a Cincinnati-based diversified family of financial services companies. He has been Chief Executive Officer since 1994. He served as a director of Convergys Corporation from 1998 to 2016, The Fifth Third Bancorp and its subsidiary, The Fifth Third Bank, from 1988 to 2009, The Andersons, Inc. from 1992 to 2008 and Cincinnati Bell Inc. from 1992 to 1998. The Board believes that Mr. Barrett's principal executive officer experience and service as a director of other publicly-traded companies, which have provided him with a deep understanding of business matters, his broad financial acumen and his status as an independent director, makes his service on the Board valuable to Cintas.

1) Touchstone [Form N-1A](#)  
Source: [Company Press Release](#) and [proxy statement](#)



# Mysterious Audit Charter Changes Made

Cintas has reported making “minor changes” to its Audit Committee Charter in early 2019, yet has not updated the document on its website. However, all other committee charter documents have been updated. Shareholders should not be kept in the dark as to what these changes were.

**Cintas Made Changes  
To Its Audit  
Committee Charter,  
But Investors Cannot  
Evaluate What  
Changes Were Made**

- (i) reviewed and monitored the progress and results of the testing of internal control over financial reporting pursuant to Section 404 of SOX, reviewed a report from management and internal audit regarding the design, operation and effectiveness of internal control over financial reporting and reviewed an attestation report from the independent registered public accounting firm regarding the effectiveness of internal control over financial reporting; and
- (j) examined the Audit Committee Charter to determine compliance by Cintas and the Audit Committee with its provisions and to determine whether any revisions to the Charter were advisable. The Cintas Audit Committee Charter was approved at the January 9, 2019 Audit Committee Meeting. Only minor changes to the Charter were required.

**Cintas Still Has It's  
Old Audit Charter On  
Its Website**

## **7. COMMITTEE MEMBER DEVELOPMENT AND PERFORMANCE REVIEW**

- (1) The Chair shall coordinate orientation and continuing director development programs relating to this Charter for Audit Committee members.
- (2) At least annually, the Audit Committee shall evaluate and review the performance of the Audit Committee and the adequacy of this Charter. This review will be undertaken in consultation with the Nominating and Corporate Governance Committee of the Board.

## **8. CURRENCY OF THE AUDIT COMMITTEE CHARTER**

This Charter was re-affirmed by the Audit Committee on January 8, 2018 and by the Full Board on January 9, 2018.

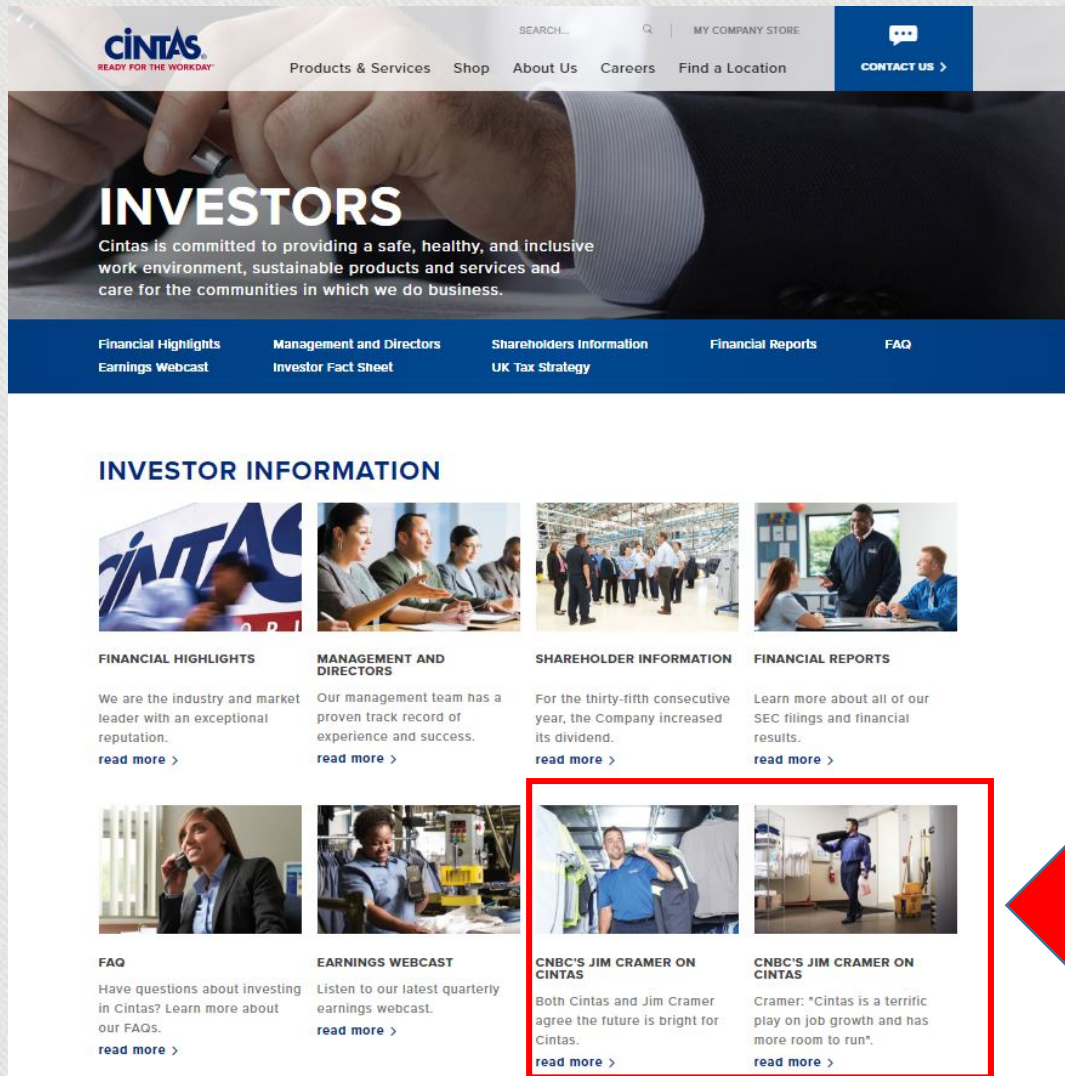




## *Valuation And Downside Case*



Does a legitimate S&P 500 company need to prominently feature endorsements from Jim Cramer on its website?



**CINTAS**  
READY FOR THE WORKDAY™

SEARCH... | MY COMPANY STORE


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## INVESTORS

Cintas is committed to providing a safe, healthy, and inclusive work environment, sustainable products and services and care for the communities in which we do business.

[Financial Highlights](#) | [Management and Directors](#) | [Shareholders Information](#) | [Financial Reports](#) | [FAQ](#)  
[Earnings Webcast](#) | [Investor Fact Sheet](#) | [UK Tax Strategy](#)


### INVESTOR INFORMATION



**FINANCIAL HIGHLIGHTS**

We are the industry and market leader with an exceptional reputation.


[read more >](#)



**MANAGEMENT AND DIRECTORS**

Our management team has a proven track record of experience and success.


[read more >](#)



**SHAREHOLDER INFORMATION**

For the thirty-fifth consecutive year, the Company increased its dividend.


[read more >](#)



**FINANCIAL REPORTS**

Learn more about all of our SEC filings and financial results.


[read more >](#)



**FAQ**

Have questions about investing in Cintas? Learn more about our FAQs.


[read more >](#)



**EARNINGS WEBCAST**

Listen to our latest quarterly earnings webcast.


[read more >](#)



**CNBC'S JIM CRAMER ON CINTAS**

Both Cintas and Jim Cramer agree the future is bright for Cintas.

[read more >](#)



**CNBC'S JIM CRAMER ON CINTAS**

Cramer: "Cintas is a terrific play on job growth and has more room to run".

[read more >](#)

# Terrible Risk / Reward With 1% Implied Downside Risk

Cintas' share price appears to be fully valued with limited upside at the current level. There are more downside risks than appreciated by the investment community, including growing financial strain and fraudulent business practices giving rise to greater competitive threats in fire inspection.

| Analyst                            | Recommendation      | Price Target       |
|------------------------------------|---------------------|--------------------|
| Goldman                            | Outperform          | \$300              |
| Baird                              | Buy                 | \$300              |
| Barclays                           | Overweight          | \$295              |
| JP Morgan                          | Overweight          | \$283              |
| RBC                                | Outperform          | \$275              |
| Stifel                             | Hold                | \$256              |
| Credit Suisse                      | Neutral             | \$225              |
| Morgan Stanley                     | Underweight/In-Line | \$223              |
| Morningstar                        | Sell                | \$141              |
| Average Price Target<br>(Downside) |                     | \$255 <b>(-1%)</b> |

1) Downside based on \$259 per share. Source: Bloomberg



# Negative Sentiment Indicators

There appears to be a consensus among independent analysts that are not compensated by Cintas, that its shares are overvalued. Yet, we don't believe any analysts have conducted an extensive forensic analysis of Cintas earnings quality, or its fraudulent business practice in fire inspection, to assess tail risks.

## Analysis

All ▼



### Cintas: An Expensive Representation Of The Magical Reoccurring Revenue Model

Joseph Kowaleski • Mon, Oct. 28 • 1 Comment



### Though Cintas Had A Good Q4 Earnings Call, I'm Not Convinced Completely On Its Future

Andrew Sather • Tue, Jul. 23 • 5 Comments



### Cintas: A 10-Year, Full-Cycle Analysis

Cory Cramer • Thu, May 16 • 2 Comments



### Cintas Fails To Make It To My Watchlist

Dilantha De Silva • Mon, Mar. 25 • 1 Comment



### Cintas: Another Cheap Stock

ChartMasterPro • Dec. 15, 2018 • 1 Comment



### Cintas: Great Company, Expensive Stock

Strubel Investment Management • Nov. 7, 2018  
• 2 Comments

Source: [Seeking Alpha](#)

## Cintas Firing on All Cylinders, but Shares Look Rich



**Matthew Young**  
Equity Analyst

**Business Strategy and Outlook** | by Matthew Young [Updated Oct 02, 2019](#)

Cintas is the largest provider in the route-based uniform solutions industry, with a market share in the ballpark of 35%, and its immense distribution network bestows industry-leading efficiency and top-tier operating margins. Cintas' performance is

Source: [Seeking Alpha](#)

# Comparable Acquisitions In The Uniform and Commercial Service Space

**We've reviewed comparable acquisitions in the uniform rental and services space. Transaction multiples suggest businesses in this sector should be valued at approximately 1.8x and 9.5x sales and EBITDA.**

\$ in millions

| Announced                | Acquiror    | Target                   | Description  | Deal Value | Est. Sales | Est. EBITDA (margin) | EV / Sales  | EV / EBITDA |
|--------------------------|-------------|--------------------------|--|------------|------------|----------------------|-------------|-------------|
| March 2002               | Cintas      | Omni                     | Uniform rental company based in Virginia   | \$660      | \$320      | \$57 / 18%           | 2.0x        | 11.6x       |
| Oct 2007                 | Eurazeo     | Elis                     | European leader in rental and cleaning of textile and hygiene services           | \$3,148    | \$1,420    | \$456 / 32%          | 2.2x        | 7.0x        |
| May 2008                 | Clothesline | Angelica Corp            | Provides textile rental and linen management services to U.S. healthcare clients | \$297      | \$452      | \$47 / 11%           | 0.7x        | 6.3x        |
| Aug 2016                 | Cintas      | G&K Services (1)         | Service-focused provider of branded uniform and facility services programs       | \$2,100    | \$960      | \$169 / 18%          | 2.2x        | 12.5x       |
| Sept 2016                | UniFirst    | Arrow Uniform            | Workplace uniforms and facility services   | \$122      | \$60       | NA                   | 1.9x        | NA          |
| June 2017                | Elis        | Davis Service Group (UK) | Textile maintenance services   | \$3,316    | \$1,436    | \$436 / 30%          | 2.3x        | 7.6x        |
| Oct 2017                 | Aramark     | AmeriPride (2)           | Uniform and linen rental and supply company in the U.S. and Canada               | \$850      | \$600      | \$71 / 12%           | 1.4x        | 12.0X       |
| <b>Average Multiple:</b> |             |                          |  |            |            |                      | <b>1.8x</b> | <b>9.5x</b> |

Source: Deal Announcements

1) G&K multiple based on 2017E figure from [deal proxy](#)

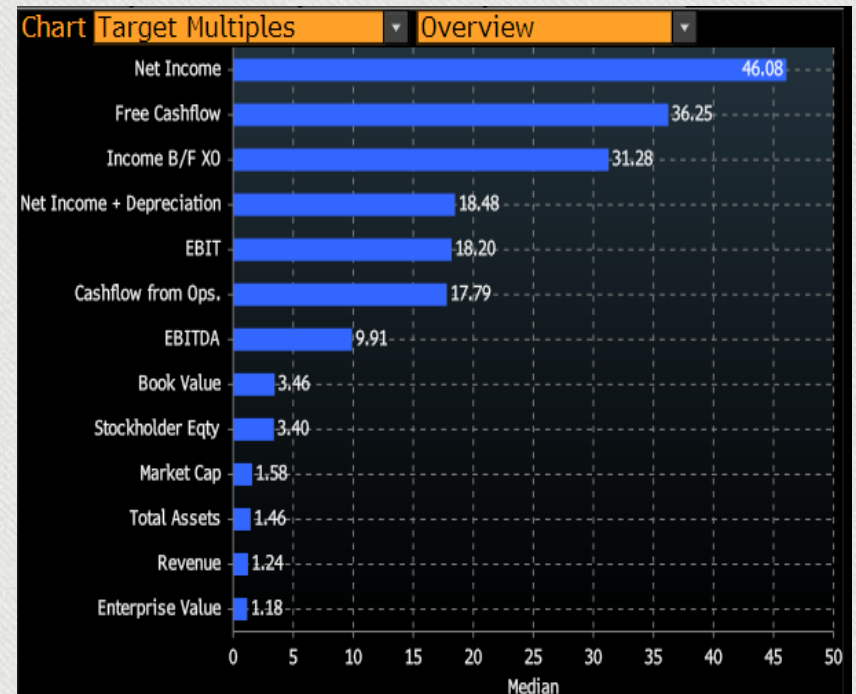
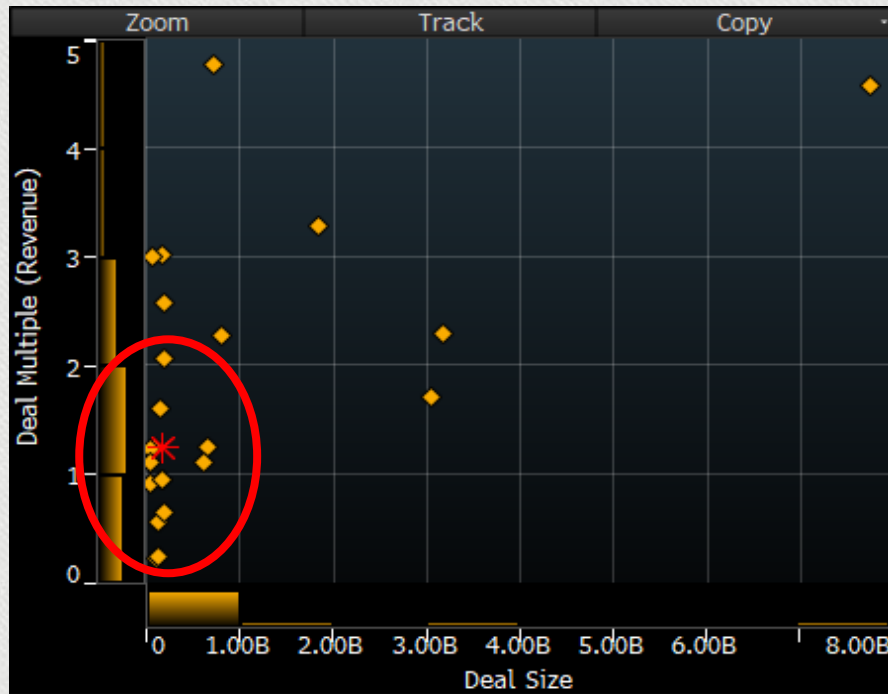
2) EV adjusted for \$150m transaction tax benefit



# Comparable Acquisitions In The First Aid And Safety Space

Analyzing recent commercial protection and safety deals, we find that revenue deal multiples are in the 1x – 2x range.

| Selected Search Criteria   | Matches |
|--|---------|
| 101) Country : Include : United States, Apply to Target or Seller... | 321535  |
| 102) Sector/Industry : Include : Protection-Safety, Apply to Tar...  | 651     |
| 103) Deal Size : (50, 100000000) Mln                                 | 60      |



# Benchmark Acquisition In Fire And Security: Convergent Technologies

Ares Capital Management acquired Convergent Technologies in Feb 2018, a company that designs, installs, and services integrated building systems, including electronic security, fire alarm, and life safety systems.<sup>(1,2)</sup> During the course of our research, Convergent was consistently mentioned as a credible competitor to Cintas. Terms of the transaction were undisclosed, but based on a credit report, we see that Convergent was acquired for \$1.62bn and was expected to grow organically by double digits to \$950m in revenue with ‘low double digit EBITDA margins’, implying the business was valued at approximately 1.7x projected revenues and 15x EBITDA.

New York, January 22, 2018 -- Moody's Investors Service ("Moody's") has assigned ratings to Gopher Sub Inc. (dba "Convergent"), including a B3 Corporate Family Rating ("CFR"), a B3-PD Probability of Default Rating, and respective B2 and Caa2 instrument ratings on the security-systems integrator's new first- and second-lien credit facilities. Nearly \$750 million in secured debt proceeds, plus a substantial equity contribution from Ares Management ("Ares"), will help fund Ares's \$1.62 billion acquisition of Convergent from another private equity owner. Upon closing of the transaction, certain subsidiaries of the Gopher Sub Inc. entity will merge or "collapse" into one another. After that consolidation, the surviving entity, the borrower, will be called DG Investment Intermediate Holdings 2, Inc. ("DG2"), while the company will continue doing business as Convergent. The rating outlook is stable.

While double-digit organic revenue growth supports the rating, it has been a function of a very active acquisition program aimed at small, fast-growth targets, and Moody's believes the company's having to operate under very high financial leverage may exacerbate the normal stresses that integrations pose. The company has modest, very-low-double-digit-percentage EBITDA margins, but Moody's expects it can generate free cash flow of nearly \$40 million in 2018, or in the low- to mid-single-digits as a percentage of debt, about average for the B3 ratings category. Moody's believes, however, that incremental expenses associated with acquisition integrations will prevent debt-to-EBITDA leverage from declining quickly, and we expect the measure to hover near 7.0 times through 2019.

Gopher Sub Inc. (dba "Convergent") is a service-based organization that designs, installs, and maintains building systems, with a focus in the areas of security systems, and with ancillary services in fire alarm/notification and life safety. The corporate entity was formed to facilitate Ares Management's early 2018 acquisition of Convergent from another private equity sponsor. Moody's expects the company to generate 2018 revenues of more than \$950 million.

Source: [Moody's](#)

1. [Ares Management to Acquire Convergent Technologies](#)
2. [Convergent Fire Alarm and Life Safety Business](#)



# Relative Valuation

Valuation of other commercial service and public safety companies suggests that Cintas is materially overvalued. Investors receive neither above market sales, earnings growth, or a dividend for Cintas' valuation premium.

\$ in mm, except per share figures

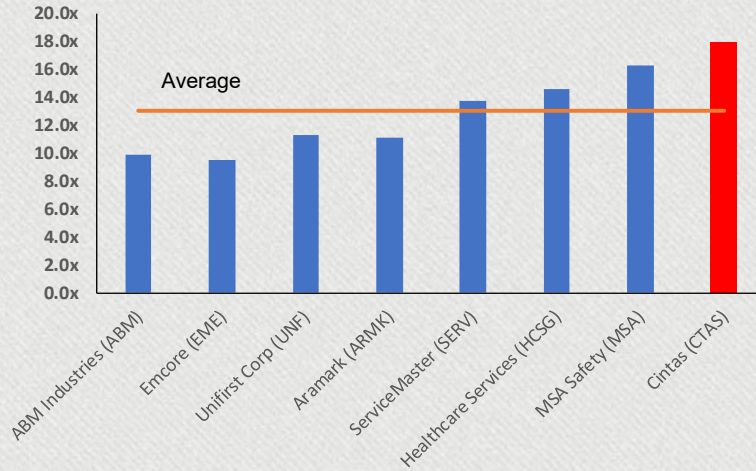
| Name (Ticker)              | Stock      | Adj      | 2019E  | '19E-'20E |        | Enterprise Value |       |        |       |       |       |                |                        |                   |
|----------------------------|------------|----------|--------|-----------|--------|------------------|-------|--------|-------|-------|-------|----------------|------------------------|-------------------|
|                            | Price      | Ent.     | Gross  | Sales     | EPS    | P/E              |       | EBITDA |       | Sales |       | Price/<br>Book | Net Debt<br>19E EBITDA | Dividend<br>Yield |
|                            | 11/12/2019 | Value    | Margin | Growth    | Growth | 2019E            | 2020E | 2019E  | 2020E | 2019E | 2020E |                |                        |                   |
| Aramark (ARMK)             | \$47.46    | \$18,963 | 11.0%  | 2.5%      | 11.4%  | 20.6x            | 18.5x | 11.9x  | 11.1x | 1.2x  | 1.1x  | 3.6x           | 4.5x                   | 1.0%              |
| ServiceMaster (SERV)       | \$34.35    | \$6,115  | 44.1%  | 7.3%      | 8.3%   | 25.8x            | 23.9x | 14.6x  | 13.8x | 2.9x  | 2.7x  | 2.0x           | 3.4x                   | NA                |
| MSA Safety (MSA)           | \$125.14   | \$5,213  | 45.7%  | 4.7%      | 8.2%   | 25.7x            | 23.7x | 17.6x  | 16.3x | 3.7x  | 3.5x  | 6.9x           | 1.0x                   | 1.3%              |
| Emcor Group (EME)          | \$90.00    | \$5,417  | 14.8%  | 6.0%      | 5.3%   | 15.8x            | 15.0x | 9.9x   | 9.5x  | 0.6x  | 0.6x  | 2.7x           | 0.6x                   | 0.4%              |
| Unifirst Corp (UNF)        | \$209.60   | \$3,630  | 37.8%  | 3.7%      | 5.2%   | 26.1x            | 24.8x | 11.8x  | 11.3x | 1.9x  | 1.9x  | 2.4x           | -1.2x                  | 0.5%              |
| ABM Industries (ABM)       | \$38.28    | \$3,413  | 10.9%  | 2.1%      | 5.2%   | 18.1x            | 17.2x | 10.0x  | 9.9x  | 0.5x  | 0.5x  | 1.7x           | 2.5x                   | 1.9%              |
| Healthcare Services (HCSG) | \$25.14    | \$1,774  | 12.8%  | -0.4%     | 12.0%  | 23.5x            | 21.0x | 16.0x  | 14.5x | 1.0x  | 1.0x  | 4.1x           | -0.9x                  | 3.2%              |
|                            |            | Max      | 45.7%  | 7.3%      | 12.0%  | 26.1x            | 24.8x | 17.6x  | 16.3x | 3.7x  | 3.5x  | 6.9x           | 4.5x                   | 3.2%              |
|                            |            | Average  | 25.3%  | 3.7%      | 7.9%   | 22.2x            | 20.6x | 13.1x  | 12.3x | 1.7x  | 1.6x  | 3.4x           | 1.4x                   | 1.4%              |
|                            |            | Min      | 10.9%  | -0.4%     | 5.2%   | 15.8x            | 15.0x | 9.9x   | 9.5x  | 0.5x  | 0.5x  | 1.7x           | -1.2x                  | 0.4%              |
| Cintas (CTAS)              | \$258.41   | \$30,653 | 33.6%  | 5.9%      | 10.6%  | 31.8x            | 28.6x | 19.5x  | 18.0x | 4.3x  | 4.1x  | 9.1x           | 1.8x                   | 1.0%              |

Source: Company financials, Bloomberg consensus estimates

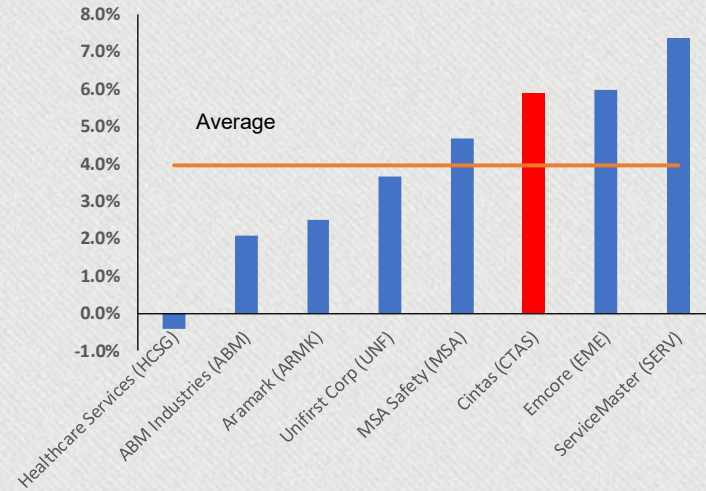


# Highest Valuation In Sector Unwarranted

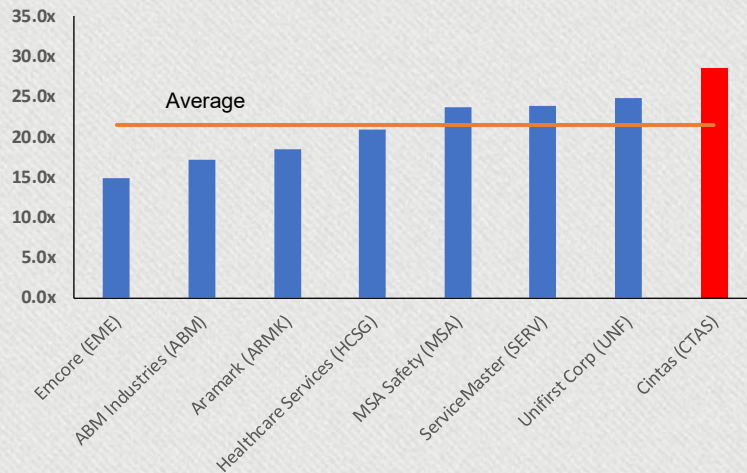
EV / 2020E EBITDA



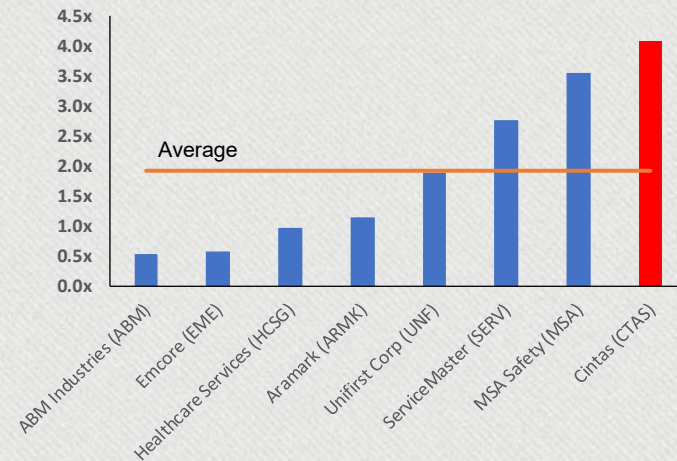
2020E Sales Growth



Price / NTM Price Earnings



EV / 2020E Sales

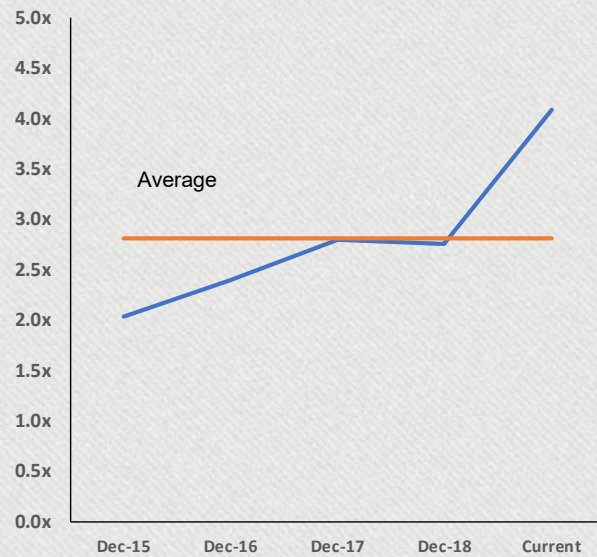




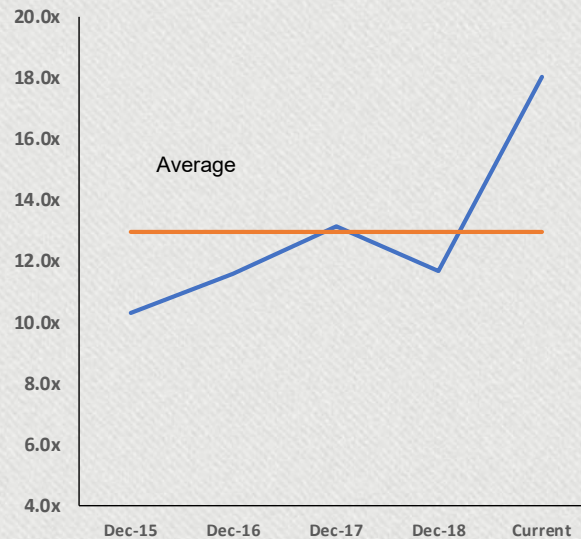
# All-Time High Valuation Makes No Sense

In light of irrefutable evidence that Cintas is breaking the law an endangering lives with shoddy fire inspection services, and financial stress rising, it makes absolutely no sense why the business valuation has increased to all-time highs.

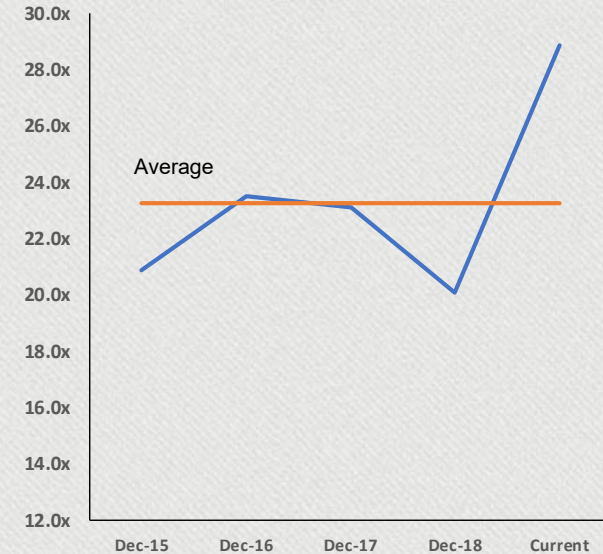
EV / NTM Sales



Price / NTM EBITDA



Price / NTM EPS



Source: Bloomberg

# Analysts Don't Model The Fire Safety Business Appropriately

**Sell-side analysts fail to carefully evaluate the nuances between Cintas' various businesses. Notably, as we've demonstrated, the Fire Safety and Inspection business has a very different growth and risk profile. Given that this business has demonstrated to be conducting fraudulent inspections, and new competitors are circling to displace Cintas, we believe it should be valued lower than other businesses.**

## Analysts Don't Take A Nuanced Approach To Valuing The Various Businesses Lines, And Instead Place A Blanket Multiple On Each Business

### Target/Upside/Downside Scenarios

#### Price target/base case

Our \$275 price target applies a ~28.5x P/E multiple on our FY21 adj. EPS estimate of \$9.65, a 5-10% premium to its 5-yr average. Our base case assumes FY20E/21E revenue growth of 6.1%/6.3% and 70bps/30bps of gross margin expansion in FY20E and FY21E.

#### Upside scenario

Our upside scenario could result in FY21 EPS in the mid-\$10 range. Applying a slightly higher multiple than our base case could therefore translate to an incremental \$32 of upside to our current \$275 price target, or a \$307 price scenario. This scenario includes FY20/21 revenue growth of 7.6%/8.0% and higher incrementals on better operating leverage.

#### Downside scenario

Our downside scenario could result in FY21 EPS in the low/mid-\$8 range. Assuming a lower multiple of ~25x could therefore translate to an incremental \$61 of downside to our current \$275 price target, or a \$214 price scenario. This scenario includes slower FY20/21 revenue growth of 5.0%/4.8% with some margin pressure.

### Valuation

During the last economic expansion (2002-07), we observed CTAS's forward P/E multiple trending downward from a peak of 38x in 2002 to a low of 14x in 2007. The median P/E from 2002 to 2007 was 23x. The multiple compression that began in 2002 reflects the transition of Cintas and the uniform services sector from a period of hypergrowth during the 1990s to having more "normalized" growth characteristics. Interestingly, the current expansion has seen the opposite dynamic, with CTAS's P/E rising during the period alongside the company's lift in organic revenue growth. Since hitting a low of 9x P/E in March 2009, the median P/E (2009 – present) for CTAS shares has been 21x. More recently, CTAS's P/E has moved from mid 20s to high 20s starting in 2018; after a bump down in late 2018, the multiple has fully rebounded this year, and the stock now trades at 28x our NTM EPS estimate.

CTAS stock has performed admirably over time and recently (+50% YTD versus S&P +19%) due to its best-in-class organic constant currency revenue growth and margins. While the company reports EPS from continuing ops, we believe that a non-GAAP adjusted EPS figure (adding back our estimates for M&A amortization and one-time GK acquisition costs) is a more appropriate methodology when valuing the company.

We are raising our Dec 2020 price target to \$283 (previously \$275; 12% upside) based on 27x our CY2021 adjusted EPS estimate. This target implies an EV/EBITDA multiple of 18x. We think this valuation approach appropriately reflects the momentum in the business, Cintas's best-in-class growth/margins, and the company's consistent cash flow generation qualities, while also balancing some legitimate concerns around CTAS's cyclicality.

## Analysts Fail To Call Out Fraudulent Business Practices, Greater Oil Industry Exposure, As Risks

### Risks to Rating and Price Target

#### Cyclical exposure

Uniform rental companies like Cintas are more cyclical than some of the other services companies we cover and are sensitive to changes in macroeconomic factors such as GDP growth and employment.

#### Potential impact from trade war/tariffs is yet to be determined

The direct impact to CTAS's cost base from tariffs is likely minimal, but the indirect impact from higher costs for CTAS's vendors (e.g., fabric mills, garment manufacturers) and CTAS's customers is challenging to estimate now.

#### SAP system implementation

Cintas is converting its software platforms to an SAP-based ERP system. The implementation has already—and will continue to—run across multiple years (F2017 through F2020) and bears execution risk. Moreover, the investment is expensive (>\$100mln) while cost structure benefits will not be realized until F2021 and beyond.

**Risks to our thesis:** 1) Hiccups related to G&K acquisition as integration efforts continue; 2) incremental cost pressures (wages, energy, hangers); 3) ERP rollout hiccups 4) elevated valuation; 5) slowing U.S. economy.



# Spruce Point Estimates 60% – 75% Downside

Because each of Cintas' business lines have a different growth and risk profile, it's appropriate to do a sum-of-the-parts valuation.

| Valuation                                      | Low Price       | High Price      | Note   |
|--|-----------------|-----------------|--|
| \$ in mm, except per share figures             |                 |                 |  |
| <b>Fire Protection Services Sales Multiple</b> | <b>1.0x</b>     | <b>1.5x</b>     | <b>Fire Protection Services</b> <ul style="list-style-type: none"> <li>Above market organic revenue slows to 8-10% from 12% as private equity backed regional platforms take share and price concessions intensify</li> <li>Fraudulent activity of having unlicensed inspectors weighs on reputation</li> <li>Key competitor Convergent just acquired for 1.7x projected sales. Cintas should trade at a discount</li> </ul> |
| <u>Estimated Sales</u>                         | <u>\$434</u>    | <u>\$446</u>    |  |
| <b>Implied Enterprise Value (A)</b>            | <b>\$434</b>    | <b>\$669</b>    |  |
| <b>Uniform Rental and Facilities</b>           | <b>1.5x</b>     | <b>2.0x</b>     | <b>Uniform Rental And Facilities</b> <ul style="list-style-type: none"> <li>Stable 5-6% organic growth in core rentals and 2-3% for uniform direct sales</li> <li>Acquisition multiples average 1.8x sales</li> <li>Unifirst is the best public comp in the space, and also trades at 1.8x sales</li> </ul>  |
| Est. Uniform Rental and Facilities Sales       | \$321           | \$327           |  |
| <u>Est. Uniform Direct Sales</u>               | <u>\$5,830</u>  | <u>\$5,886</u>  |  |
| Total Revenues                                 | \$6,151         | \$6,213         | <b>First Aid And Safety</b> <ul style="list-style-type: none"> <li>10-12% organic growth</li> <li>Acquisition multiples suggest 1x-2x sales</li> </ul>   |
| <b>Implied Enterprise Value (B)</b>            | <b>\$9,227</b>  | <b>\$12,426</b> |  |
| <b>First Aid And Safety</b>                    | <b>1.0x</b>     | <b>2.0x</b>     |  |
| <u>Estimated Sales</u>                         | <u>\$681</u>    | <u>\$694</u>    |  |
| <b>Implied Enterprise Value (C)</b>            | <b>\$682</b>    | <b>\$1,387</b>  |  |
| <b>Total Cintas Business Value (A+B+C)</b>     | <b>\$10,342</b> | <b>\$14,482</b> |  |
| Less: Existing Debt (and Leases)               | (\$3,032)       | (\$3,032)       |  |
| Plus: Cash and Equivalents (1)                 | \$41            | \$41            |  |
| <b>Equity Value</b>                            | <b>\$7,351</b>  | <b>\$11,492</b> |  |
| <u>2019E Diluted Shares</u>                    | <u>107.0</u>    | <u>107.0</u>    |  |
| <b>Price Target</b>                            | <b>\$69/sh</b>  | <b>\$107/sh</b> |  |
| <i>% Approximate Downside</i>                  | <i>-75%</i>     | <i>-60%</i>     |  |

1) Excludes restricted cash and applies a 15% repatriation tax to cash in foreign subsidiaries

Note: Cintas segment reporting shows no "intersegment" revenues or "corporate" SG&A expenses, which supports our view that a sum-of-the-parts valuation is justified