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# FITNESS AND WELLNESS

CONSUMER/INTERNET/MEDIA INDUSTRY REPORT | SEPTEMBER 2008



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**Investing in “Healthy Living”**

Fitness Industry  
Spas  
Yoga/Pilates  
Wellness Products

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## Key Takeaways

**The United States is facing an obesity crisis.** Currently, 76.8 million Americans are obese — a 50% increase in the last 10 years. Public health officials predict that more than 86% of Americans are on their way to becoming obese by 2030. There is already a clear link between excessive weight gain and chronic health problems, such as diabetes and heart disease. At a time when health care costs are considered excessively high, this epidemic further compounds the problem. In fact, eight of the nine costliest diseases are directly related to excessive weight, and medical costs are typically 32% higher for inactive persons. We believe the burden that obesity places on the health care system — in cost and resources — makes this issue a national priority.

**Corporate and government define roles.** The obesity crisis costs corporations millions annually through lower productivity, higher absenteeism rates, as well as higher health care costs. Government data estimates that total health care costs related to being overweight and obese could reach \$956.9 billion by 2030. To reverse this problem, both the public and private sectors have launched health initiatives — from government bills to corporate health programs to insurance company incentives — to put a nation on the path to good health.

**Baby boomers pursue optimal health.** The golden years have finally arrived for the oldest among the baby boomers, those born between 1946-1964. However, most are eschewing the retiring or sedentary lifestyle in pursuit of health and longevity. A recent study reported that 75% of boomers lead an active lifestyle to stay healthy, and 40% even claim to be more fit than they were in their 20s. Their desire to stay ever-youthful, with the spending power to support that aim, stands to benefit the health and fitness industry. Boomers' focus on well-being becomes the perfect complement to the nation's renewed interest in reclaiming good health.

**Fitness industry finds niche.** Within the last two decades, the number of gyms has steadily increased, with memberships totaling 41.5 million in 2007. And by all accounts, we believe there is growth ahead. A particularly successful strategy, niche gyms, tailor services for a specific group historically overlooked by traditional gyms. In addition, new developments in exercise equipment are attracting members and opening novel markets. The commercial equipment manufacturers are benefiting from the domestic growth in gyms and now see the international and vertical markets (hotels and spas) as excellent opportunities.

**Spa industry broadens appeal.** Formerly considered a self-indulgent treat, spas are now increasingly seen as an essential part of a healthy regimen. The spa industry has broadened its appeal and is fast becoming a leading leisure activity. With almost 15,000 locations, the industry has been adding an average of 1,600 spas per year since 1999. One in four U.S. and Canadian adults have visited a spa, usually citing the No. 1 goal — to relieve stress.

**Yoga and Pilates' popularity endures.** Within the past decade, interest in yoga and Pilates has grown, as Americans seek to integrate mind, body and spirit with exercise. Some 9 million Americans practice Pilates, with 15.8 million practicing yoga. Yoga and Pilates studios and manufacturers of related products have all benefited from the public's, especially the boomers', interest in using low-impact exercises to stay healthy.

**Wellness products promise to improve health.** More people are paying closer attention to the quality of the foods and beverages they purchase. Consumers are keen to learn how wellness products can help stave off disease, lower cholesterol, lose weight and achieve overall well-being. Natural and organic foods and beverages, functional beverages with health-promoting and disease-preventing properties, and beauty products are appealing options for those wishing to live healthier lives while looking and feeling better. U.S. sales of health and wellness goods reached \$102.8 billion in 2007, which is expected to increase to \$170 billion by 2012. And as boomers get older, more are turning to wellness products as an antidote to the signs of aging.

*Note: Specific sources for each data point on this page are cited throughout the research report.*

## Introduction

The current obesity crisis, rising health care costs and an aging population have sparked an intense focus and diverted substantial financial resources toward improving the overall health of Americans. Given current trends, we believe individuals, corporations and the government will look for ways to lose weight, reduce stress and live an overall healthier lifestyle. We believe they will begin to take a more proactive and preventative approach to staying healthy. While staying fit and healthy will always remain a personal choice and responsibility, we believe we will begin to see companies and governments become more involved, mandating healthier living in an effort to offset prohibitively higher health care costs.

We believe that the products and services promoting healthier lifestyles — from feeling and looking better to being active, preventing disease, reducing stress and slowing down the aging process — should benefit from the growing demand. In our opinion, gyms, fitness equipment manufacturers, wellness services and related products are all poised to take advantage of this trend.

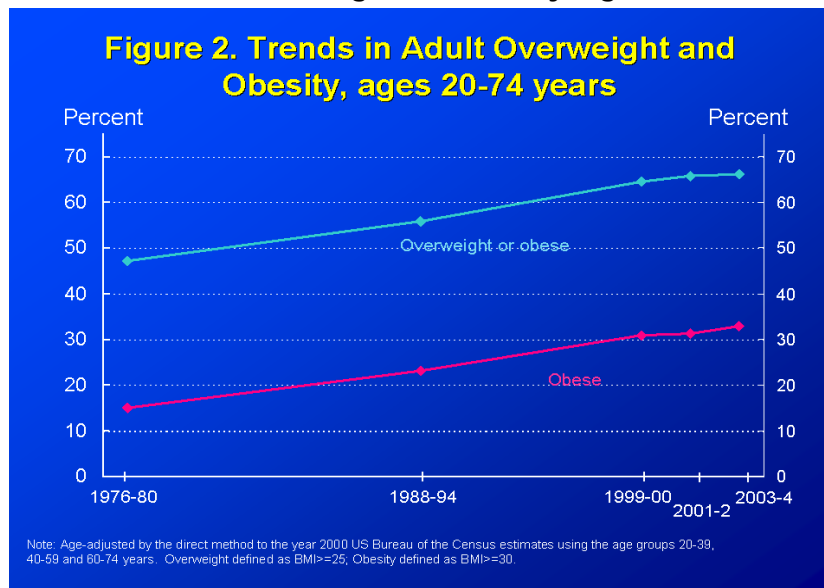
## The U.S. Obesity Crisis

In the last few decades, obesity levels in the United States have risen dramatically. Despite the general public's focus on health and fitness, the number of overweight and obese Americans is at an all-time high and continues to climb. The trend toward sedentary lifestyles and poor eating habits, along with time and financial constraints to address weight gain, all contribute to the growing problem. What's more, obesity and, to a lesser degree, weight gain, have led to a rise in preventable chronic health problems, such as diabetes and heart disease.

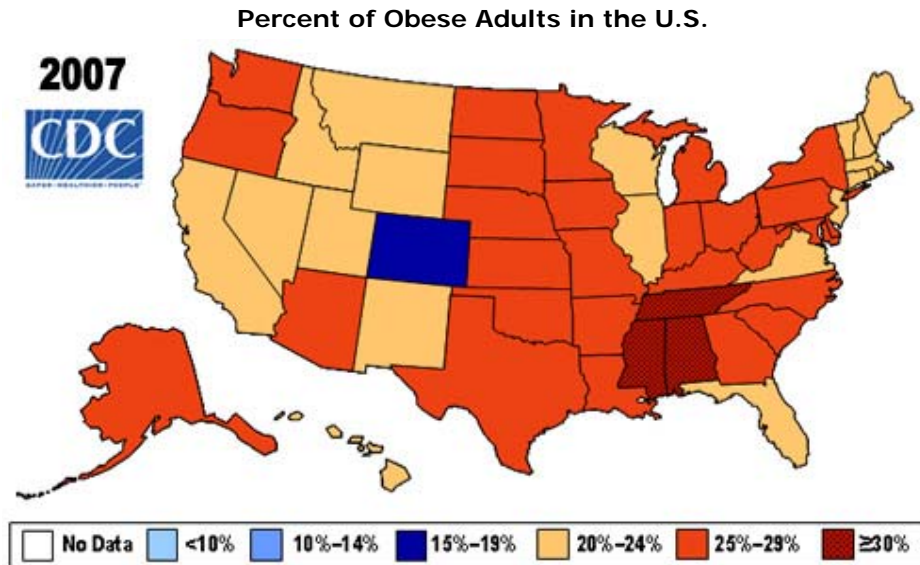
Consider these sobering statistics:

- Sixty-six percent of American adults and 32% of children are considered overweight or obese (Centers for Disease Control and Prevention, or CDC, 2006).
- Based on current trends, more than 86% of adults will be overweight or obese by 2030 ("Will All Americans Become Overweight or Obese? Estimating the Progression and Cost of the U.S. Obesity Epidemic," by Youfa Wang, et al; *Obesity*, July 2008).
- The number of obese adults has increased 50% in the last 10 years to 76.8 million — more than a third of the population (CDC estimates).

**Trends in Adult Overweight and Obesity, Ages 20-74 Years**



Source: CDC



### Impact of the Obesity Crisis: Economic Costs

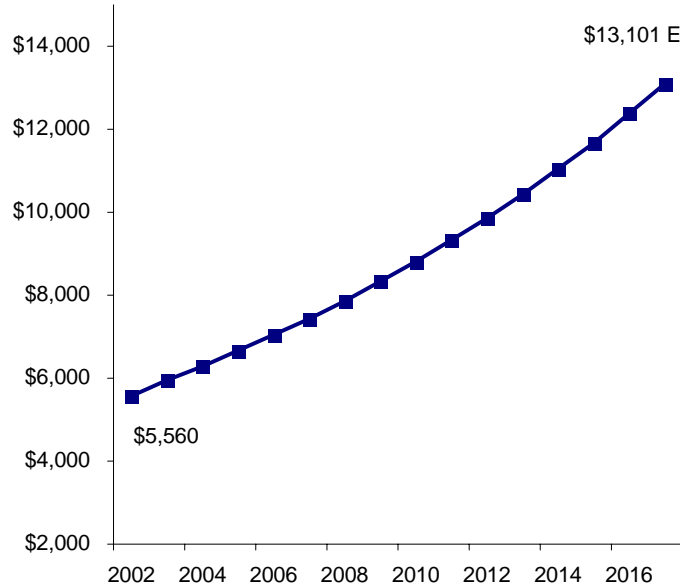
From lower worker productivity to preventable diseases, the rise in obesity is leading to a range of problems that, in turn, have an enormous social and economic impact on the United States, individuals and corporations.

The health care costs associated with obesity are compounding the already dire health care situation. Consider the following **health care costs facing the nation:**

- In 2007, health care spending reached \$2.3 trillion and is projected to reach \$3 trillion in 2011 and \$4.2 trillion in 2016 (“Health Spending Projections Through 2016: Modest Changes Obscure Part D’s Impact,” by John A. Poisal, et al; *Health Affairs*, February 2007).
- Medicaid spending was estimated at \$361.2 billion in 2007 and is expected to reach \$717.3 billion by 2017 (“Health Spending Projections Through 2016: Modest Changes Obscure Part D’s Impact,” by John A. Poisal, et al; *Health Affairs*, February 2007).
- In 2000, direct and indirect costs related to being overweight and obese totaled \$117 billion (U.S. Department of Health and Human Services).
- Total health care costs attributed to obesity and being overweight are estimated to be \$860.7-956.9 billion by 2030 (“Will All Americans Become Overweight or Obese? Estimating the Progression and Cost of the U.S. Obesity Epidemic,” Youfa Wang, et al; *Obesity*, July 2008).
- Eight of the nine most expensive diseases are related to obesity (*The Problem We Are Addressing, Promoting Healthy Lifestyles Through Sports & Fitness*, 2008).
- Average annual medical costs are 32% higher for an inactive person than they are for a physically active person (*The Problem We Are Addressing, Promoting Healthy Lifestyles Through Sports & Fitness*, 2008).
- U.S. national health expenditures have been rapidly increasing and are expected to rise from \$5,560 in 2002 to \$13,101 in 2017 (Centers for Medicaid & Medicare Services estimates).

## Fitness and Wellness Industry

U.S. National Health Expenditures per Capita



Source: Centers for Medicaid & Medicare Services estimates

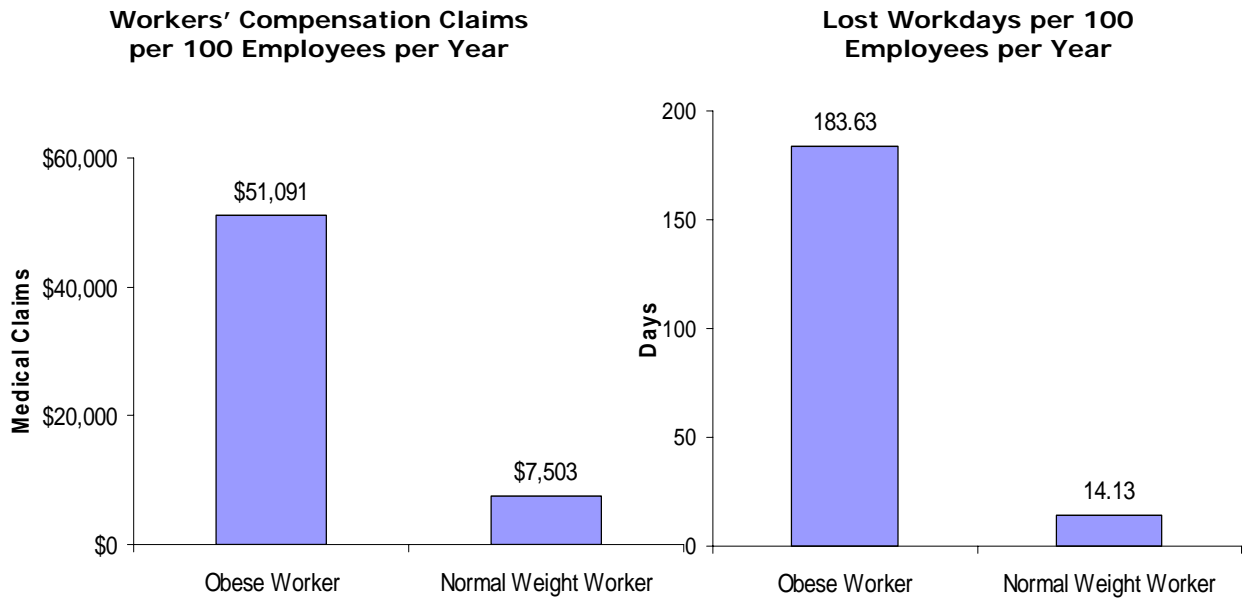
Unhealthy lifestyles also take a **toll on individuals**, often leading to a range of chronic diseases, higher health care costs and an overall lower quality of life for individuals:

- More than 85% of people with Type 2 diabetes are overweight (U.S. Department of Health and Human Services, 2007).
- Physically inactive people are twice as likely to develop coronary heart disease as routinely active people (U.S. Department of Health and Human Services).
- Approximately 20% of cancer in women and 15% in men are attributable to obesity (CDC, 2005).
- Annually, there are 300,000 U.S. deaths due to obesity-related complications; one out of every eight deaths is caused by an illness directly related to being overweight or obese (*The Problem We Are Addressing*, Promoting Healthy Lifestyles Through Sports & Fitness, 2008).
- Forty-five states allow health insurers to use health status and obesity as a factor to deny coverage or raise premiums (Trust for America's Health, 2008).
- In 2007, health insurance premiums rose an average of 6.1% (Kaiser Family Foundation).
- Severely overweight and obese children often suffer from depression, low self-esteem and isolation from peers (U.S. Department of Health and Human Services).
- During 2004-2006, 12% of adults reported a weight discrimination claim ("Changes in Perceived Weight Discrimination Among Americans," by Tatiana Andreyeva, et al; *Obesity*, February 2008).
- Overweight people earn 1-6% less than non-overweight in comparable positions ("The Wage Effects of Obesity: A Longitudinal Study," by Charles L. Baum and William F. Ford, *Health Economics*, September 2004).

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The obesity epidemic and unhealthy lifestyles of employees have led to lower worker productivity, higher compensation claims and higher health insurance costs — severely **hurting U.S. companies' bottom line**.

- Obese employees cost private employers approximately \$45 billion a year due to medical expenses and excessive absenteeism (*Weights and Measures: What Employers Should Know About Obesity*, by Barbara Rosen and Linda Barrington, The Conference Board, 2008).
- Companies are projected to pay an average of \$9,312 per employee for health care in 2008, up from \$6,385 in 2003 (*2008 Health Care Cost Survey*, Towers Perrin).
- Health insurance costs are the fastest-growing cost component for employers (“Will Health Benefit Costs Eclipse Profits?” McKinsey & Company, September 2004).



Source: "Obesity and Workers' Compensation: Results from the Duke Health and Safety Surveillance System," by Truls Østbye, et al; Archives of Internal Medicine, April 2007

The social and economic impact of the obesity crisis has caught the attention of individuals, boardrooms and governments. Fortunately, through regular exercise, proper diet and a consistent focus on overall wellness, the above health care epidemic and ensuing financial crisis are almost entirely preventable. For this reason, corporations, governments and insurers are actively encouraging the public to live a healthier life.

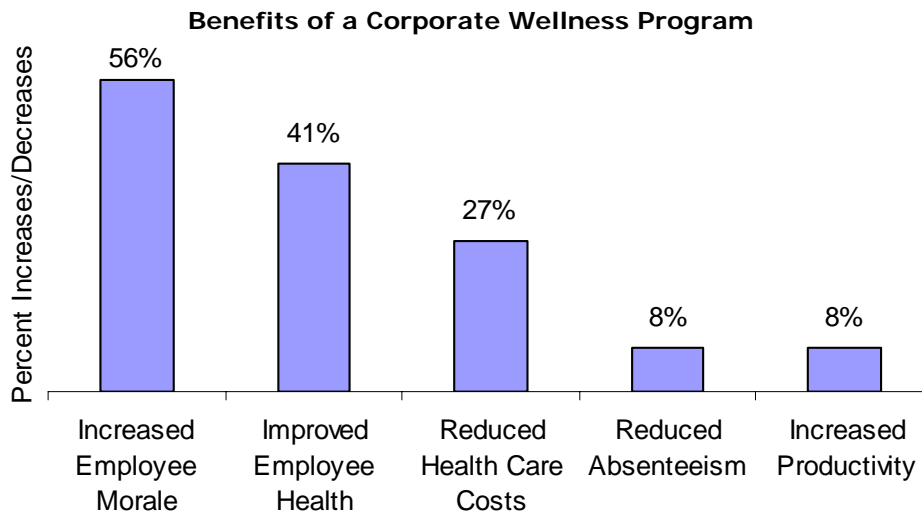
**Corporate Wellness Programs**

Many corporations have implemented corporate wellness programs precisely to mitigate future health care costs. Corporate wellness programs focus on illness prevention and usually include classes in basic nutrition, regular checkups, onsite fitness facilities and smoking-cessation programs. A recent trend is leveraging financial incentives to promote wellness and healthy behavior. Gift cards, premium reductions and even cash bonuses are rewarded to employees who complete certain health programs. According to a 2008 survey by The ERISA Industry Committee, the National Association of Manufacturers and IncentOne, the percentage of major U.S. corporations using financial incentives to promote employer-sponsored health and wellness programs rose from 62% in 2007 to 71% in 2008.

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In addition to preventing future health care costs, many corporations are finding corporate wellness programs to be successful at providing other benefits. Through increased employee morale, health, productivity and a decrease in absenteeism, employers are seeing the financial benefits from worksite wellness programs.

- Over a four-year period ending in 2002, Johnson & Johnson’s wellness program reduced health care costs by an estimated \$224.66 per employee per year (*The Cost Benefit of Worksite Wellness*, Wellness Councils of America, 2002).
- A review of 56 peer-reviewed studies on worksite wellness found that the return on investment for a dollar invested in worksite health promotion was \$5.82 (“Meta-Evaluation of Worksite Health Promotion Economic Return Studies: 2005 Update,” by Larry S. Chapman, *American Journal of Health Promotion*, July/August 2005).



Source: National Business Group on Health, 2005

According to the above chart, companies implementing a corporate wellness program noted significant improvements in a variety of indicators. For example, employers reported a 56% increase in employee morale after launching a corporate wellness program.

The success of early corporate wellness programs — particularly the positive impact on the bottom line — has been encouraging and has spurred many companies to adopt health-based programs for their own employees. Currently, 77% of employers offer some sort of formal health and wellness program, according to industry sources.

Because of the financial returns, we expect to see corporations expand offerings, especially in the fitness area, which could have a huge impact on the public’s exercise habits. A 2004 survey by the International Health, Racquet and Sportsclub Association (IHRSA) found that **82% of Americans said they would exercise regularly if their employer subsidized health care memberships**. In addition, exercise classes and health club membership ranked No. 2 and 3, respectively, behind full medical checkups, in terms of subsidized benefits that employees would like to receive. According to the Society for Human Resource Management, approximately 31% of America’s larger corporations subsidized their employees’ health care memberships in 2004. And because of the public’s desire for such benefits, we expect to see corporations take a bigger role in their employees’ fitness.

**Sector Highlight: Companies That Manage Wellness Programs**

Three companies we have identified that should further benefit from the popularity of corporate wellness and fitness centers are I-trax, a subsidiary of Walgreen Co., Plus One Health Management and Health Fitness Corp. All three design and manage onsite fitness and wellness centers for leading corporations, hospitals, and residential and retirement communities. As companies look to introduce a corporate wellness plan or enhance an existing one, we believe they will look to these three companies to handle their wellness needs.

Based in Pennsylvania, I-trax is a leading designer, developer and manager of on-site fitness and wellness centers for corporations. The company integrates health, wellness and disease management services for employees through programs that emphasize preventative care, occupational health, fitness and health education. The company also provides primary care services and operates on-site pharmacies that offer prescription services. I-trax's clients include BMW, Deutsche Bank, Lowe's, Toyota and others. As of December 31, 2007, the company operated 243 on-site facilities in the United States and was acquired by Walgreens Co. in April 2008 for approximately \$278 million. Walgreens is looking to expand its presence in the worksite wellness sector and plans to operate 10,000 locations by 2012, including pharmacies and retail and worksite health centers that deliver health care solutions where people live and work.

New York-based Plus One Health Management is a leading manager and designer of corporate fitness and commercial centers, as well as spas and wellness programs. The company provides its services to Fortune 500 companies, five-star luxury properties and hospitals. In 2007, *Inc. Magazine* listed Plus One Health Management as one of the fastest-growing private companies. The company was recently contracted to handle Google's employee fitness program and its 11,000 full-time employees. In 2007, the company had \$23.5 million in sales.

Health Fitness Corp., based in Minnesota, is a leading provider of health improvement services and programs. The company currently manages 226 corporate fitness centers, 173 corporate health management sites and 104 unstaffed health management programs. The company had revenue of \$70.0 million in 2007, up from \$63.6 million in 2006.

The company has two business segments: Fitness Management Services and Health Management Services. The Fitness Management Services' offerings include designing and managing fitness centers, selecting fitness equipment, personal training, weight-loss programs and seminars. In terms of size, the company states that it is the largest provider of corporate fitness center management services in the United States. In 2007, Fitness Management comprised approximately 60% of revenue in 2007. The Health Management Services' offerings allow corporations and other organizations to assess the health characteristics of their employees, as well as providing health education programs and lifestyle coaching services. Health Management is the faster of the two segments and comprised approximately 40% of revenue in 2007.

## Government's Role

In addition to corporations, we believe the rising health care costs associated with obesity and chronic illness will spur state and federal governments to find ways to promote healthier lifestyles. Currently, three bills are before Congress, each encouraging exercise. If passed, all should help boost the fitness and wellness industry. Whatever the outcome, we believe the bills' existence indicates that policymakers recognize the critical need for fitness and are making steps in the right direction.

### Personal Health Investment Today Act of 2007 (H.R. 245)

The Personal Health Investment (PHIT) bill would let people use pre-tax dollars to pay for physical fitness programs and exercise equipment through flexible spending or health savings accounts — the same way people might pay for medications or doctor visits. The bill was reintroduced in January 2007, and was proposed during the last session of Congress, where it stalled without being voted on (few bills make it out of committee). It currently has 23 co-sponsors with bipartisan support.

By making fitness more affordable, we believe that passage of the PHIT bill can encourage people to buy fitness equipment and join gyms, leading to a healthier life. According to IHRSA's "The Importance of Exercise" survey conducted in 2007, more than 40% of Americans said they would exercise more if there were tax-free incentives.

### Workforce Health Improvement Program Act of 2007 (S.1038/H.R. 1748)

The Workforce Health Improvement Program (WHIP) bill promotes healthier employees by excluding the value of on-site employer-provided fitness fees from the employee's taxable income. In addition, the WHIP Act also allows employers a tax deduction on fees or membership dues associated with fitness facilities. The bill has currently been assigned to committee.

### Strengthening Physical Education Act of 2007 (H.R. 1224)

The Strengthening Physical Education Act aims to get students active by making physical education part of No Child Left Behind's core curriculum. The bill would also require physical education assessments throughout children's schooling. The bill is currently still in committee.

In addition to the above-mentioned federal bill, many states have published state plans focused on physical activity and healthy nutrition aimed at reducing the prevalence of overweight and obesity. Currently, 41 states have such plans in place, and 17 states have passed weight-related screening requirements for students (*F as in Fat: How Obesity Polices Are Failing America*, Trust for America's Health, 2008).

We believe the intervention of the government will have a huge impact on the exercise habits of the American public. Historically, health club participation has increased after the government has announced recommendations for exercise. In 1996, after the surgeon general recommended that Americans get at least 30 minutes of exercise a day, the number of members increased 8.0% in 1997 from 1996. The industry saw another increase in memberships of 7.4% in 2002 over 2001 after the surgeon general raised the awareness of the obesity epidemic and the impact of exercise on weight loss (see membership chart on page 12).

## Insurers' Role

Health insurers are also seeing the benefits of exercise on reducing future health care costs, and they are beginning to provide incentives to exercise. With almost half of Americans stating that paying for health care is their No. 1 economic concern (*The Wall Street Journal-NBC Survey, 2007*), incentives from insurers may provide the key to get people to exercise more.

- The Oxford Health Plan offers policyholders a \$200 rebate if they demonstrate that they have attended a health club at least 50 times in the prior six months.
- Aetna provides a discount for gym club memberships.
- Medica, a Minnesota health insurance company, offers a \$20-month gym membership credit if policyholders exercise at a participating health club eight or more days a month.

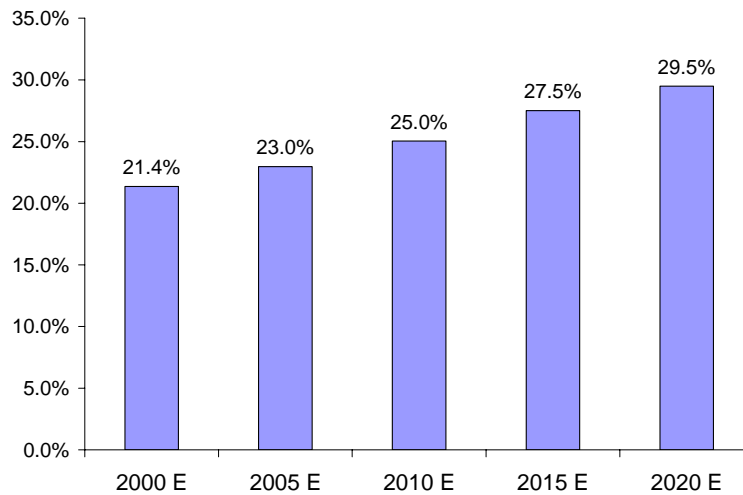
**Fitness and Wellness Industry**

**Baby Boomers Pursue Optimal Health**

The long-anticipated baby boomer trend has inspired a keen interest in longevity and optimal life. The 78 million boomers, born 1946-1964, were considered among the first Americans truly focused on health and wellness and were the first group to actively join gyms which helped spur the initial growth in the health club industry. With a strong desire to stay vital, we believe this demographic shows signs of bucking the conventional ideas of aging. Rather, their desire to stay active and ever-youthful, combined with an estimated annual spending power of \$2.1 trillion (Metlife Mature Market Institute), should have a substantial positive impact on the health and fitness industry.

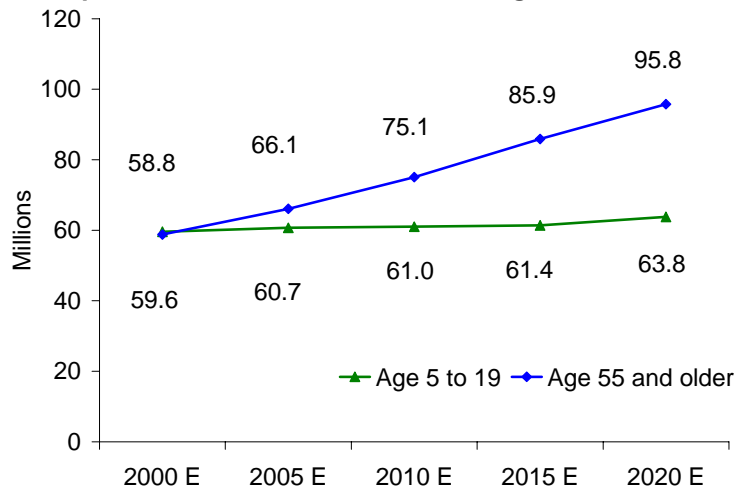
According to a 2007 survey conducted by Kelton Research, the baby boomers feel and look younger than ever, with 75% of respondents saying they keep an active lifestyle to stay healthy, and 40% responding that they are living healthier and are more physically fit than they were in their 20s.

**Percentage of Americans Older than Age 55**



Source: U.S. Census Bureau, 2000

**Expected Population Growth of Americans Ages 5-19, 55 and Older**



Source: U.S. Census Bureau, 2000

While the number of people ages 5-19 is expected to remain fairly steady, the number of people older than age 55 is expected to explode over the next 10 to 15 years (U.S. Census Bureau, 2000).

**Fitness and Wellness Industry**

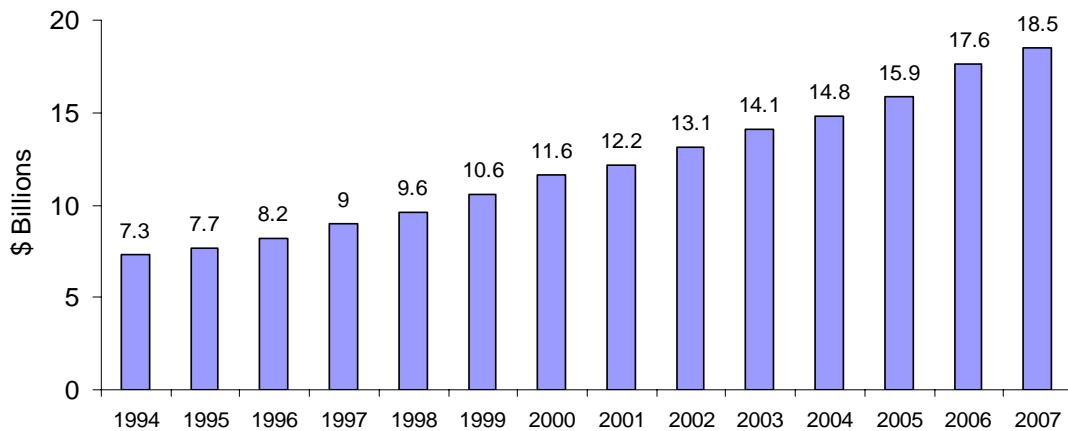
**Beneficiaries of Obesity Concern and Boomers' Aging**

We believe the obesity epidemic and its related health care costs, along with an aging population, are causing the public to reexamine their lifestyles and make taking care of their bodies a priority. Healthy initiatives put forth by corporations and the government are making it easier to live a healthier lifestyle. We believe these trends will benefit industries focused on overall wellness, notably the fitness, spa, yoga and wellness-related product industries.

**Gym Industry**

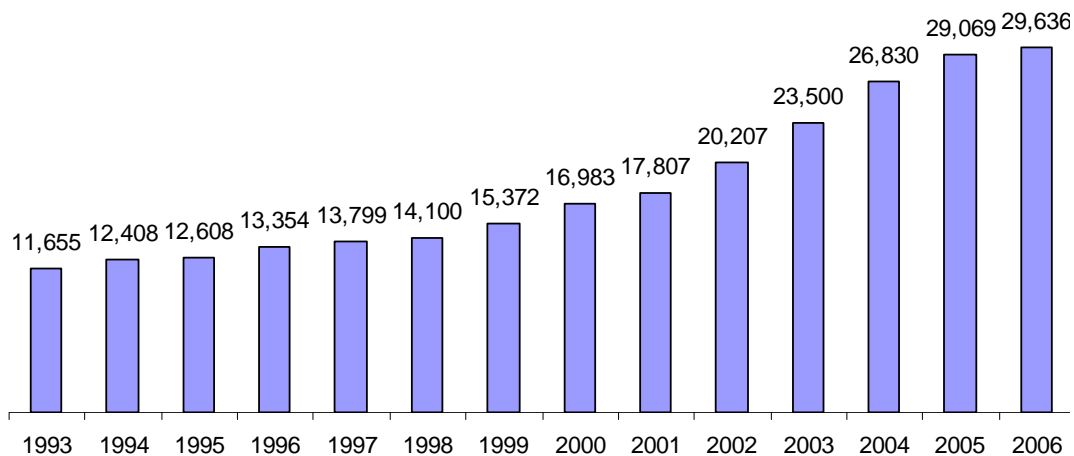
Through the media, education, and government and medical studies, we believe the majority of the public is aware of the benefits of staying active, with 99% of Americans believing regular exercise helps maintain good health (Trust for America's Health, 2007). As the general public pursues leading a healthier lifestyle, we believe the fitness industry (including gyms and fitness equipment manufacturers) is poised to benefit. Within the last 15 to 20 years, the number of gyms and memberships has greatly increased, which we expect to continue. While we believe there will always be a consistent demand for gyms, with 84% of the public not belonging to a gym (IHRSA, 2008) and with 60% not getting the recommended amount of exercise (U.S. Department of Health and Human Services, 1999), we believe there exists an enormous opportunity to attract new members and grow.

**U.S. Gym Revenue**



Source: IHRSA

**Number of Gyms in the U.S.**



Source: IHRSA

Fitness and Wellness Industry

Leading U.S. Gym Chains

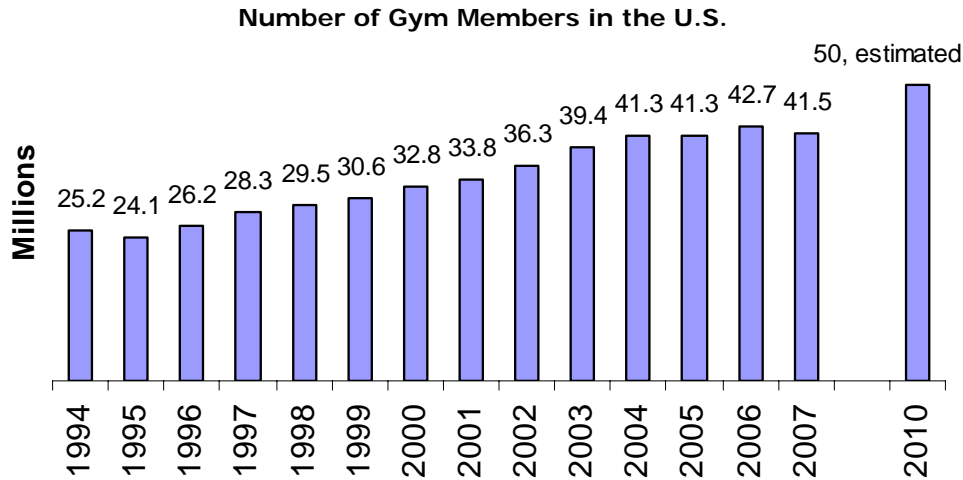
Company	Ticker (or Private)	2007 Revenue	Description
24 Hour Fitness Worldwide Inc.	Private	\$1.3 B*	Owens 401 gyms in the U.S. and 24 in Asia.
Anytime Fitness Inc.	Private	\$35 M	Franchiser of 596 and owner of 12 low cost 24 hour gyms across the U.S.
Bally Total Fitness Corporation	Private	\$1.1 B*	Owner of 322 gyms and franchiser of 37 across the U.S.
Club One, Inc.	Private	\$82 M	Owens 14 gyms and manages 75 across U.S.
Clubcorp	Private	\$950 M	Owens 135 gyms and manages 14 in the U.S. China and Mexico.
Contours Express International, LLC	Private	NA	Has 700 franchised gyms across the world.
Crunch	Private	\$83 M	Owens 29 gyms and manages 1 across the U.S.
Curves International, Inc.	Private	\$200 M	Has 10,600 franchised women only gyms across the world.
Equinox	Private	N/A	Owens 41 premium gyms across the U.S.
Fitness Together Franchise Corp.	Private	\$92.2 M	Has 350 Franchised gyms.
Gold's Gym International, Inc.	Private	\$121.6 M*	Owner of 53 gyms and 557 franchised across the world.
Healthy Inspirations, LLC	Private	\$1.6 B*	Has 145 gyms across the U.S.
Jazzercise, Inc	Private	\$85 M	Has 7,200 franchised clubs across the world.
L.A. Fitness International, LLC	Private	NA	Owens 231 gyms in the U.S. and Canada.
Lifestyle Family Fitness, LLC	Private	\$79.4 M*	Owens 53 gyms
Life Time Fitness, Inc	LTM	\$656	Owens 74 family oriented resort style gyms across 17 states.
Planet Fitness	Private	\$48 M	Owens 27 gyms, 207 franchised and 5 licensed.
Powerhouse Gyms	Private	NA	Owens 10 gyms and licenses 340 across the world.
Snap Fitness, Inc.	Private	\$10 M	Owens 27 gyms and 599 franchised 24 hour key card gyms across the U.S.
Town Sports International	CLUB	\$473	Owens 147 gyms in the northeast and manages 2 in Switzerland.

\*Revenue in 2006

Source: Company reports, IHRSA and Merriman Curhan Ford estimates

Fitness and Wellness Industry

According to IHRSA, the number of fitness club memberships in the United States has grown from 26.2 million in 1996 to 41.5 million in 2007. More important, **the percentage of the population that joined has also dramatically increased from 12.0% in 1996 to 14.1% in 2001 and then to 16.0% in 2006** (IHRSA). At the current penetration level of 16%, we believe there still remains a lot of room for further growth in both new gyms and members. In fact, the strong demand is expected to continue, with an estimated 50 million members by 2010 (IHRSA).



Source: IHRSA

A large portion of the growth in the fitness industry has come from the rise in popularity of smaller gyms, most notably “24-hour key-card” gyms and “express” gyms. These gyms are usually 2,500-5,000 square feet, much smaller than the big-box gyms, and are thus able to open in smaller communities and in high-traffic areas, usually near offices. Because of their low overhead costs, these gyms are able to offer lower membership fees and an opportunity for franchisees. Because of their convenience and low membership costs, these gyms are providing an alternative to traditional gyms and are attracting new members that want a no-frills workout.

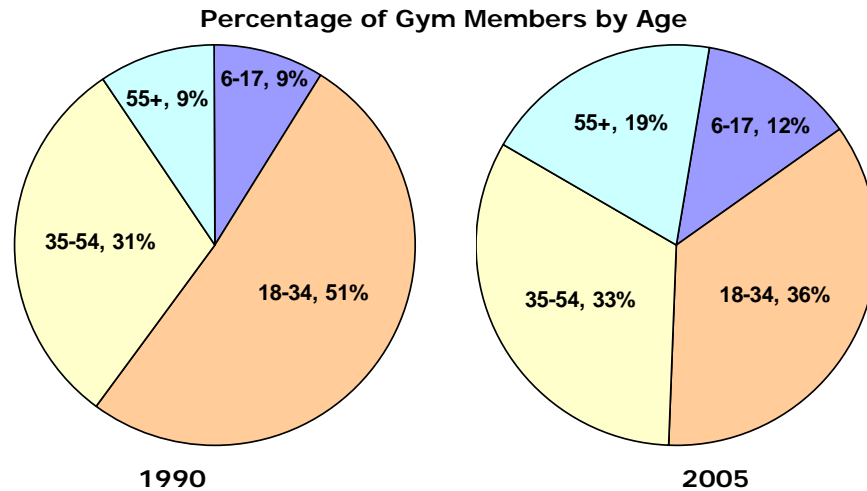
Another notable trend attracting new members are the niche gyms. Coming off the success of Curves (a chain of small women’s-only gyms), many chains have found success by targeting groups historically overlooked or neglected by the industry. These gyms appeal to people who want to work out with others like themselves, without intimidation. And just as Curves opened up fitness for women who previously avoided gyms, these fitness centers provide members a novel and non-threatening environment for exercise and are thus able to attract new members who would have otherwise never joined a gym.

We expect to see continuing market segmentation in the industry, as gyms gear their offers to specific audiences, such as seniors, families and children. We believe that as new niche gyms open, the industry will attract more members. And, **with an estimated 84% of Americans not belonging to a gym, there remains a huge opportunity to attract and gain new members** (IHRSA, 2008).

Helped by the growth in gyms and programs with older Americans in mind, the graying of America is fueling much of the growth in gym memberships. The age 55 and older group is the fastest-growing demographic in gym memberships and now represents approximately a quarter of all memberships, according to IHRSA. As the first generation to exercise, many baby boomers have indicated that they are continuing their fitness routines, while others are joining gyms for the first time in an effort to stay active and healthy in their golden years.

Fitness and Wellness Industry

In addition, the opposite end of the age bracket is also driving gym membership growth. The second-fastest growing demographic is the under-17 crowd. For those who don't like sports yet want to stay in shape, many gyms now have special programs designed for young adults. According to industry sources, many children are going to the gym with their parents through family plans. This is a trend that we believe should benefit Life Time Fitness as the company focuses on families through family memberships, children-focused programming and family-oriented amenities such as pools and basketball courts. We see this as a good sign, as the gyms are teaching children at an early age the importance of exercise, ingraining in them the importance of adopting healthy habits — a lesson they can carry with them throughout their lives.



Source: IHRSA

**Impact of a Recession on Gyms**

Historically, the health and fitness industry has been recession-resilient. Although not immune to economic downturns, gyms usually weather tough economic times better than other industries according to industry sources. For many, we believe fitness is a way of life, and giving up a gym membership is usually one of the last things a person does when budgets tighten. While we may expect to see fewer people initiating gym memberships in a slow economy, we typically don't expect to see a substantial increase in attrition rates. Yet there have been conflicting reports about how the current economic environment — with falling to flat wages and inflation, leaving the average consumer with less discretionary income — is affecting the gym industry.

According to a recent IHRSA survey, the health club industry remains strong. In a poll of 18 leading chains, comprising 193 facilities, **IHRSA found that those surveyed grew their total revenue by an average of 15% in 1Q08. In addition, clubs averaged an increase of 9.7% in total membership accounts over the same period last year.** Anecdotally, Life Time Fitness and Town Sports International posted strong results in 2Q08. Life Time Fitness had an increase of 19% and 12% in revenue and memberships, respectively, over the previous year. And Town Sports International had an 8% increase in revenue over the same period a year ago and a lower than expected 3.2% attrition rate.

However, *Fitness Business Pro* published a 2008 independent study of more than 100 clubs, which revealed that since the end of 1Q08, attrition levels increased more than 25% versus the same period last year. In addition, new memberships were flat compared to the same period as before.

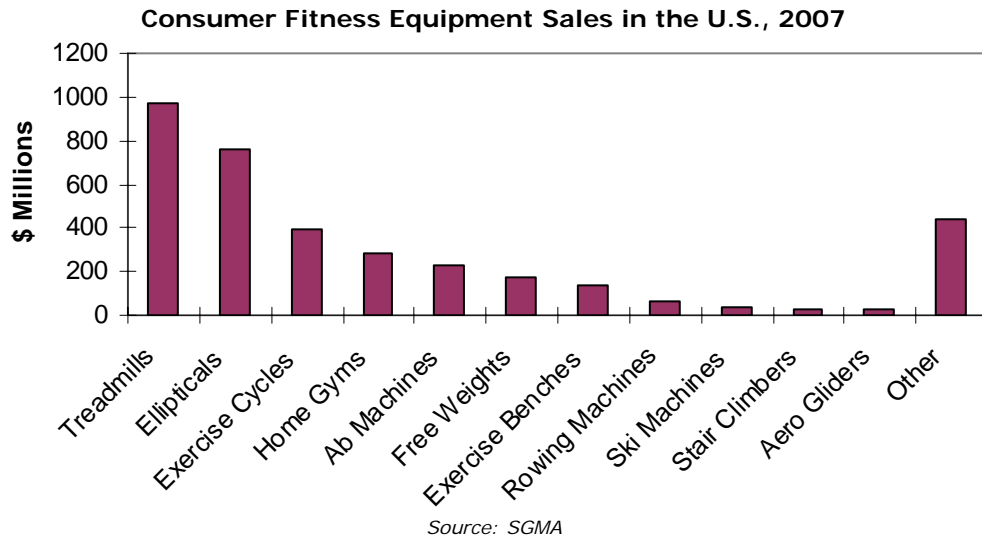
Although it may be difficult to reconcile the two reports and draw conclusions, we believe the economic environment is having some impact on the gym industry. We also believe that some of the smaller gyms, most notably franchises, may suffer from the recent credit crunch. As credit tightens, it may be hard for franchisees to obtain financing and open up new facilities. However, we believe that the well-established clubs, high-end clubs with many services, especially family packages, and lower-priced gyms should still perform fairly well and continue to attract members and replace their worn and outdated fitness equipment at a normal pace.

Fitness and Wellness Industry

**Fitness Equipment Market**

**Consumer Market**

The consumer fitness equipment market is very fragmented, with low-end products ranging from abdominal machines and Thigh Masters to premium cardio and strength-building equipment costing thousands of dollars. Despite growth in the domestic consumer equipment market from approximately \$2.4 billion in 1996 to approximately \$3.5 billion in 2006 (Sporting Goods Manufacturers Association, or SGMA), we believe that sales in the higher-priced home equipment market will be weak in the near term as consumers ride out a tougher economy. We believe companies that sell premium home fitness equipment will be under pressure as consumers forgo larger purchases given the current economic environment. Underscoring this point are that leading fitness equipment manufacturers reported weak consumer demand for fitness equipment sales in 2008. Precor (a unit of Amer Sports) reported that fitness equipment sales are down 17% to date due to weak consumer demand. Life Fitness reported consumer equipment sales down 30% to date, and Nautilus' direct-to-consumer business sales are down 24% to date.

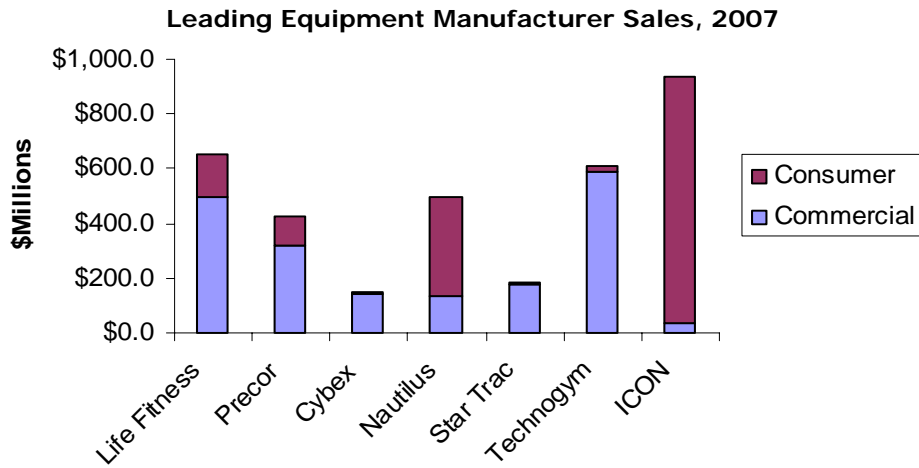


In the above chart, the "other" category represents a sizeable portion of the consumer fitness equipment market and includes products such as jump ropes, medicine balls, as well as yoga- and Pilates-related equipment (see sections covering yoga, Pilates and GAIAM).

**Commercial Market**

Although the *consumer* equipment market sales may be weak, we believe the *commercial* fitness market is still poised for strong growth. The commercial fitness equipment market — which includes fitness clubs, YMCAs and Jewish Community Centers — represents an estimated \$1.5 billion global market and growing, according to industry sources. We believe the growth in the gym and fitness club industries will, in turn, determine the demand for commercial fitness equipment, and while the economic environment is causing some uncertainty in the gym industry, due to the historical resiliency of gyms and because they need to continually buy new equipment, we believe the commercial equipment manufacturers should continue to do well. In fact, equipment manufacturer Precor reported that the commercial business continues to remain solid, and Life Fitness and Cybex have also had strong commercial sales so far this year, and to date, they are up year-over-year.

**Fitness and Wellness Industry**



*Source: Company reports and Merriman Curhan Ford estimates*

Two areas further driving strong commercial sales have been the growth in the light commercial and international markets — both provide opportunities for expansion, in our view.

**Light Commercial Market**

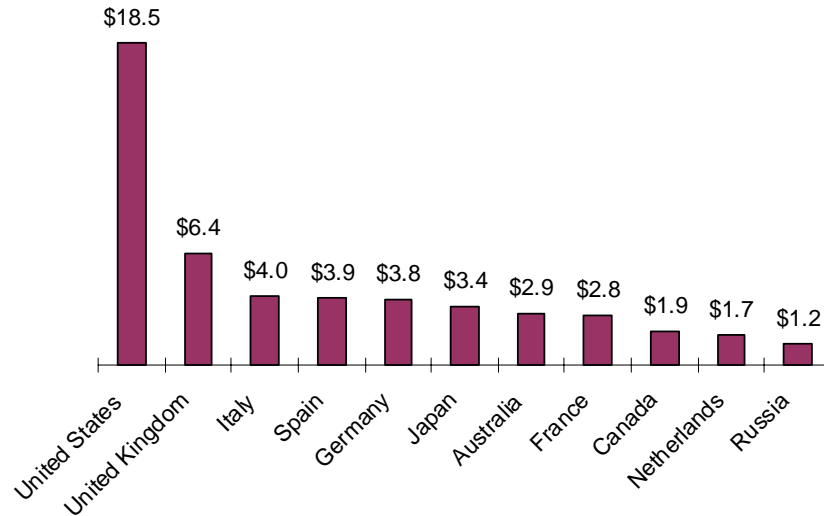
The light commercial or vertical market — which includes hotels, spas and corporate fitness centers — represents an increasing market for equipment manufacturers. According to industry sources, more and more hotels are finding that a fitness center is not only a differentiating product, but practically a necessity. Fitness-minded consumers value the spa and fitness center experience and expect equipment on par with high-end fitness clubs. According to the American Hotel and Lodging Association’s 2008 survey, 79% of respondents had an exercise/fitness facility in 2008, up from 48% in 1998. However, the needs and limitations of hotels are a little different than those of a big-box gym. One is size limitation, and we believe that equipment manufacturers who can address these needs will stand to benefit.

**International Market**

The international market remains fertile ground for commercial fitness equipment manufacturers and, thus, a very promising opportunity, in our view. We believe the international market is similar to the way the U.S. market was in the 1980s and represents a huge opportunity for the fitness industry. While still in a development stage, gym penetration rates are very low, with an estimated 65.2 million members outside of the U.S. currently belonging to a gym. We expect this to change as incomes rise and the international public learns the importance of a healthier lifestyle. We expect to see strong demand across Europe, Asia Pacific and Latin America, and we believe that any domestic weakness will likely be offset by international strength.

## Fitness and Wellness Industry

International Gym Revenue, 2007



Source: IHRSA

**Sector Highlights: Cybex International and Technogym**

Among the various fitness equipment providers, we believe manufacturers Cybex International and Technogym are poised to take advantage of current positive fitness trends and take additional market share in the exercise equipment market.

Based out of Massachusetts, Cybex is a leading manufacturer of premium exercise equipment primarily for the commercial and light commercial industries. The company has a strong brand name and a full line of innovative products — from strength-building equipment, treadmills, bikes and cross trainers, including the award-winning Arc Trainer, a unique cardio machine that combines the elements of an elliptical and stepper machine. New product introductions have fueled top-line growth, and the company reported sales of \$146.5 million in 2007, up 15% from 2006.

Cybex is well positioned for the positive trends in the international and vertical markets, in our view. The company has an office in the United Kingdom, and 30% of sales in 2007 were from international markets. In addition, it has a full line of equipment specifically designed for the hotel and corporate fitness sectors that should address the demand for the growing hotel segment. Because the company generates very little revenue from the consumer equipment market, we do not expect consumers' current weak spending to have much of an impact on business, unlike what Nautilus and Life Fitness have been experiencing. We estimate that this puts Cybex in the position of being the only publicly traded company primarily focused on the commercial fitness equipment business.

Technogym, based in Italy, is one of the largest makers of fitness equipment and the leader outside of North America. Technogym calls itself "the wellness company," and in addition to its strength-building and cardio equipment, the company addresses overall wellness through products it calls "movement products" (exercise equipment that closely mimic natural movements to increase flexibility and improve posture and coordination). According to industry sources, we estimate that Technogym had revenue of more than \$600 million last year, averaging growth of approximately 30% over the last three years.

Because of its leading position in the international fitness market, Technogym is poised for strong growth outside North America, notably in Dubai, Russia and China. Due to the quality of Technogym's equipment, the company has been named as the official sponsor of equipment for the last four Olympics, including most recently in Beijing, China.

**Fitness and Wellness Industry**

The company is setting the standard in fitness equipment, with many industry experts believing that Technogym's products are some of the most innovative and aesthetically pleasing equipment currently available in the market. In addition, the company is one of the leaders in implementing technology in its equipment (as covered in the next section). We believe Technogym's wide range of products from strength-building and cardio equipment should satisfy the growing needs of gyms, corporate fitness centers, community centers, hotels and spas. And its "movement products" should be very popular with an aging population focused on low-impact exercises and staying vital.

**Trend in Fitness Equipment: Technology and Equipment**

We believe that the biggest trend in fitness equipment is the implementation of technology in fitness equipment. It was not too long ago that having a monitor on a piece of a cardio machine was considered cutting-edge. However, as more people have become tech-savvy, many exercisers are now incorporating the latest gadgets into their workouts — for instance, iPods to play MP3s and plug-and-play devices, such as USB keys, to access personal fitness software.

As new technology rolls out to enhance workouts, we expect more exercisers to incorporate fitness software into their routines to track progress and stay motivated. The shift toward computer-driven workouts will likely spawn a new generation of fitness equipment, loaded with the latest technology, to engage existing exercisers as well as attract new ones.

Examples of fitness equipment incorporating the latest technology

- Life Fitness' Elevation cardio series lets users download workouts on a USB stick and keep track of progress online.
- Star Trac has predesigned programs to help users track progress online and via USB sticks.
- 24 Hour Fitness is the first gym to offer the new Nike+iPod-enabled gym equipment from Technogym that keeps track of workouts connecting equipment with Nike-brand shoes and iPod.

These new types of equipment are differentiating products for gyms. In an increasingly competitive environment, we believe club operators will purchase this new equipment to set themselves apart from their competition and to attract new members. Much like televisions in the gym, we believe this new technologically advanced fitness equipment will soon become a necessity.

**Sector Highlight: Espresso Fitness**

Espresso Fitness is taking the technology and fitness trends to the next level and, in our opinion, represents the future of cardiovascular exercise equipment. Espresso Fitness combines the excitement of a video game with the benefits of exercise, providing what we view to be one of the most entertaining forms of indoor exercise.

A monitor is attached to the front of an upright or recumbent exercise bike, where the exerciser can choose to ride along one of more than 30 virtual paths. Like a video game, the user can race against other virtual riders, and how fast the user pedals determines how fast he or she can ride. In addition, riders can shift gears and move the handlebars as the terrain changes — providing a realistic outdoor biking experience indoors.

These systems are connected to the Internet, with live access to Espresso servers, and lets riders race against friends and even compete against their own personal best time. A small monthly subscription fee gives users access to workout tracking services, which provides another revenue stream for both Espresso and the fitness center.

The demand for Espresso's bikes has been significant, as many of the leading fitness centers are using this novel bike to attract and retain members and offer additional services. Revenue has grown from less than \$1 million in 2005 to a projected \$17 million in 2008. With an elliptical and treadmill product in the works, Espresso management believes that the revenue opportunity is more than \$200 million.

Fitness and Wellness Industry

Selected Private Equity Activity Transactions in the Fitness Sector

Date Announced	Target/Issuer	Transaction Value (M)	Buyers/Investors	Description
6/30/2008	Technogym	-	Candover	Fitness Equipment
6/23/2008	AlterG, Inc.	-	Funk Ventures, Astrolabe Ventures	Fitness Equipment
6/30/2008	Technogym	-	Candover	Fitness Equipment
6/3/2008	Snap Fitness, Inc	-	Summit Partners	Gyms
1/25/2008	Titan Fitness	-	Westview Capital Partners	Gyms
12/11/2007	GoodLife Fitness Centers, Inc.	\$39.6	Penfund	Gyms
6/1/2007	Alaska Club	-	Lincolnshire Management	Gyms
3/15/2007	Espresso Fitness Corporation	\$21.3	Enterprise Partners, Sierra Ventures, Physic Ventures,	Fitness Equipment
9/12/2006	Fitlinxx	-	North Atlantic Capital	Fitness Equipment
8/29/2006	David Barton Gyms	-	Praesidian Capital	Gyms
8/11/2006	California Family Fitness	-	Bunker Hill Capital, L.P.	Gyms
6/19/2006	Extreme Fitness	-	Falconhead Capital	Gyms
9/19/2005	Crunch	\$45	Angelo Gordon	Gyms
5/6/2005	LA Fitness	\$261	MidOcean Partners	Gyms
5/3/2005	24 Hr. Fitness Worldwide Inc.	\$1,600	Fortsmann Little	Gyms
1/10/2005	Octane Fitness	-	North Castle Partners	Fitness Equipment
10/15/2004	Fitness Quest	-	JW Childs, Brantley Partners	Fitness Equipment
7/9/1999	Icon Health & Fitness	\$40	Bain Capital, CSFB Private Equity, Inverness Management	Fitness Equipment
12/1/1996	Town Sports International	-	Bruckmann Rosser, Sherrill Farallon Capital	Gyms
-	PaceMaster	-	Nautic Partners	Fitness Equipment
-	York Barbell Company	-	Susquehanna Capital	Fitness Equipment

Source: Capital IQ, Merriman Curhan Ford estimates

Fitness and Wellness Industry

Selected Companies Participating Within This Industry

Company	Ticker (or Private)	Price*	Enterprise Value (M)*	CY07 Sales (M)	CY08 Sales (M)**	Description
Cybox International	CYBI	\$3.35	\$74	\$147	\$152	Manufacturer of primarily commercial fitness equipment.
Espresso Fitness	Private	-	-	\$7	-	Manufacturer of video game-inspired stationary bicycles.
Hoist	Private	-	-	-	-	Manufacturer of strength-building fitness equipment.
ICON Health & Fitness	Private	-	-	-	-	Manufacturer of exercise equipment under brands Pro-Form, NordicTrack, and others.
Brunswick Corp.	BC	\$13.79	\$1,540	\$5,671	\$5,333	Manufacturer of fitness equipment through subsidiary Life Fitness
Nautilus, Inc.	NLS	\$5.32	\$159	\$501	\$454	Manufacturer of primarily commercial fitness equipment.
PaceMaster	Private	-	-	-	-	Manufacturer of treadmills, elliptical and exercise cycles.
Amer Sports	AMEAS (OMX)	9.50 €	1,172 €	1,652 €	1,611 €	Manufacturer of fitness equipment through subsidiary Precor.
Star Trac	Private	-	-	-	-	Manufacturer of a full line of fitness equipment.
Technogym	Private	-	-	-	-	Manufacturer of primarily commercial fitness equipment.
TRUE	Private	-	-	-	-	Manufacturer of cardio fitness equipment.

\*Prices and enterprise values as of September 2, 2008

\*\*CY08 sales estimates are Merriman Curhan Ford estimates when available; First Call consensus otherwise  
Source: Company reports, First Call, Merriman Curhan Ford estimates

## Spa Industry

At one time, a visit to a spa was perceived as a self-indulgent treat. However, spas are now increasingly seen as being part of a healthy regimen. The spa industry has been working to broaden its consumer appeal and is quickly becoming a leading leisure activity. By reducing stress, soothing sore muscles, eliminating toxins and allowing people to feel better emotionally and mentally, spas are now synonymous with well-being.

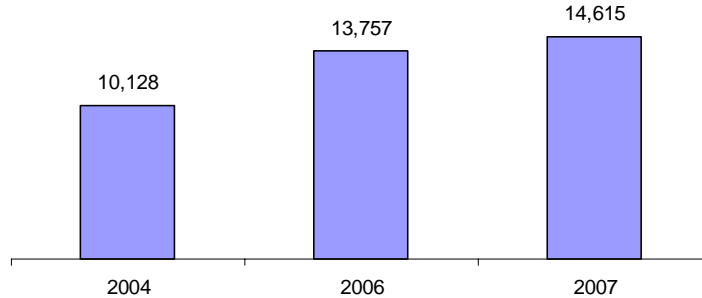
The following data offers a snapshot of the spa market (International Spa Association, or ISPA, 2007):

- In 2006, there were 110 million spa visits
- There are 32 million active spa-goers
- Spas are the No. 1 leisure activity at meeting and corporate events
- One in four U.S. and Canadian adults have visited a spa
- Sixty-nine percent of spa-goers are female and 31% are male
- Reducing/relieving stress is the No. 1 reason people go to spas

### Growth

The number of spas in the United States has grown at an average of 1,600 spas per year since 1999 and has increased 44% since 2004, according to ISPA. However, while growth may have slowed in recent years (6% growth in 2007 according to ISPA), the actual number of spas continues to increase.

**Number of Spas in the U.S.**



Source: ISPA

According to ISPA, with total revenue of more than \$9 billion dollars per year, the spa industry represents a sizeable market. Despite the drop in revenues from \$9.7 billion in 2005 to \$9.4 billion in 2006 (a statistically insignificant amount), many industry experts believe that the industry is healthier than ever. Average profit margins have increased from 8% in 2003 to 17% in 2006 (ISPA), demonstrating that clubs are becoming more focused on the bottom line and are finding ways to run more efficiently, which is leading to higher profits despite lower revenues.

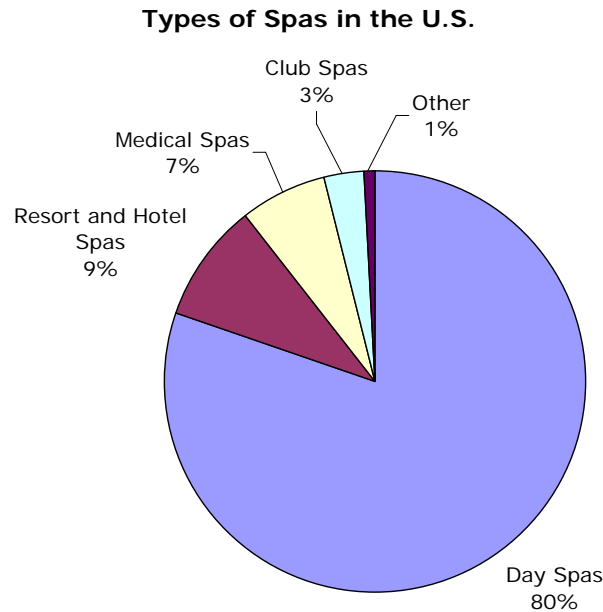
**Annual Spa Revenues in the U.S.**



Source: ISPA

## Fitness and Wellness Industry

With almost 12,000 locations, the most prevalent type of spa is the day spa, followed by resort and hotel spas, then medical spas. However, while day spas account for 80% of all types, they only represent 56% of the spa industry revenue (ISPA).



*Source: ISPA, 2007*

Medical spas are currently the fastest-growing segment in the spa industry according to industry sources. Medical spas run programs supervised by licensed health care professionals, focusing on medical beauty procedures. Popular procedures include natural weight-loss measures (such as body wraps), Botox and Restylane injections, medical peels and microdermabrasion. In addition, they offer traditional spa treatments, such as massages and facial and body treatments.

According to ISPA, the number of medical spas increased at an average rate of 19% per year from 2004 to 2006 and now comprises the spa industry's third-largest segment. In turn, while spa industry revenue fell from 2005 to 2006, medical spa revenue more than doubled, bringing in \$1,063 billion in 2006, up from \$469 billion in 2005. And despite only representing 7% of total spa locations, medical spas comprise more than 11% of total spa revenue. We expect the medical spa trend to continue, as more people look to the latest medical technology to help make them look and feel better.

As the spa industry broadens its appeal, we expect to see more people incorporate spa treatments into their healthy lifestyles. According to the ISPA, in 2007, more than one in 10 spa-goers incorporate spas as part of a larger health and wellness lifestyle. In addition, as the spa industry targets specific demographics — such as men, couples, pregnant women and seniors with tailored packages — we expect the demand for spa treatments to increase. In 2007, 48% of spas had packages for men, 46% for couples, 45% for pregnant women, 34% for teens and 20% for seniors (ISPA 2007). As it has been for the fitness industry, we believe the segmentation will further attract new members, especially in the senior and teen demographics.

Two firms we expect to benefit from the positive trends in spa-going are Elizabeth Arden Spas and Spa Chakra, which both operate full-service salons in the United States and internationally and focus on comprehensive wellness.

## Fitness and Wellness Industry

## Selected Companies Participating Within This Industry

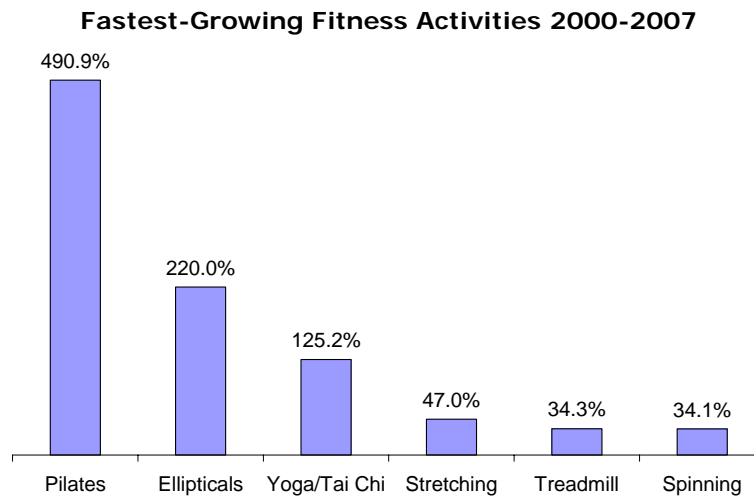
Company	Ticker (or Private)	Price*	Enterprise Value (M)*	CY07 Sales (M)	CY08 Sales (M)**	Description
Coldwater Creek, Inc	CWTR	\$7.28	\$587	\$1,151	\$1,140	Specialty retailer of women's apparel. Opened 3 day spas in 2007.
Elizabeth Arden Spas	Private	-	-	-	-	Owns and operates over 30 full-service salons and day spas in the U.S. and Europe.
Sleek Medspa	Private	-	-	-	-	Operator of 7 medical spas on the East Coast
Spa Chakra, Inc.	Private	-	-	-	-	Owns and operates over 20 luxury, urban and resort spas.
Steiner Leisure Limited	STNR	\$35.40	\$552	\$529	\$559	Provides spa services to cruises and resorts worldwide.

*\*Prices and enterprise values as of Sept 2, 2008*

*\*\*CY08 sales estimates are Merriman Curhan Ford estimates when available; First Call consensus otherwise  
Source: Company reports, First Call, Merriman Curhan Ford estimates*

## Yoga/Pilates

Another trend that we believe will continue is the growing popularity of yoga and Pilates. Within the last 10 years, yoga and Pilates' growth has been explosive, as the American public has looked to integrate mind, body and spirit in their physical activities. According to the SGMA, the number of people participating in Pilates and yoga/tai chi in 2007 grew 490.9% and 152.2%, respectively, from 2000, and yoga and Pilates are expected to be the hottest forms of exercise for sales growth in 2008.



Source: SGMA

According to SGMA, there were 9.2 million Americans practicing Pilates in 2007. In addition, a 2008 Ideal survey showed that 68% of fitness centers offered Pilates, and, of those, 61% believe demand will continue to grow, ranking Pilates as one of the most popular activities with growth potential.

According to *Yoga Journal's* 2008 study, "Yoga in America," the number of Americans practicing yoga is 15.8 million. The yoga market is estimated at \$5.7 billion annually, including revenues from classes, equipment, vacations and magazines, an 87% increase from 2004.

The "Yoga in America" study revealed other highlights as well:

- Some 18.3 million Americans expressed being "very interested" or "extremely interested" in yoga, which is triple the number in 2004.
- Seventy-two percent of U.S. yoga practitioners are female, a drop from the 77% female in 2004, demonstrating that more men are taking up yoga.
- Forty-four percent of U.S. practitioners have annual household incomes exceeding \$75,000, and 24% have more than \$100,000.

We believe the boomer generation will generate even more interest in yoga and Pilates, further fueling the popularity. Approximately 27% of yoga practitioners are ages 45-54, and as the aging population looks for low-impact activities that put less strain on their bodies, we expect to see an increasing number of yoga and Pilates participants as well as studios.

We also believe that as the medical benefits of practicing yoga and Pilates become more widely recognized, we will see an increase in demand. In fact, 14 million people say that a doctor or therapist recommended yoga, and 49.4% of all yoga practitioners indicated that they started practicing yoga to improve their overall health, up from 5.6% in 2003 (*Yoga Journal*).

## Fitness and Wellness Industry

We are also seeing an increase in demand for yoga- and Pilates-related apparel. Lululemon, which sells yoga and other apparel, has seen its revenue explode from \$18.2 million in 2004 to \$274.7 million in 2008. The increased demand in yoga has attracted some of the biggest retailers from J. Crew to J.C. Penny to launch their own lines of yoga wear. We expect the arrival of new players in the yoga soft goods market to help make the exercise more mainstream and increase the overall market, further benefiting industry-established companies such as Lululemon and GAIAM, which also sells yoga clothing and related products.

**Sector Highlight: YogaWorks**

In our opinion, YogaWorks is poised to benefit from the increase in yoga and Pilates' popularity. Founded in 1987, YogaWorks is one the leading yoga chains, offering yoga classes of various styles and levels. The company also offers teacher training, nutrition counseling, and Pilates programs and yoga retreats. YogaWorks has 18 locations in Los Angeles, Orange County and New York.

In addition, given the popularity in corporate wellness programs, YogaWorks can benefit from corporate programs that include on-site classes and corporate discounts. The company lists Fortune 500 companies, law firms, entertainment companies, universities, and health and hospital organizations as some of their clients. Corporations are discovering that the benefits of yoga can help reduce health care costs and increase productivity by decreasing absenteeism and reducing stress, fatigue and back pain.

As more people look to low-impact exercises to stay fit and reduce stress, we believe the demand for yoga will grow. And as yoga becomes mainstream, we believe companies will offer more yoga services, and established companies, such as YogaWorks, should benefit.

**Selected Companies Participating Within This Industry**

Company	Ticker (or Private)	Price*	Enterprise Value (M)*	CY07 Sales (M)	CY08 Sales (M)**	Description
GAIAM, Inc	GAIA	\$12.73	\$243	\$263	\$285	Sells and manufactures consumer lifestyle products, including yoga related products
Lululemon Athletica, Inc.	LULU	\$19.37	\$1,280	\$275	\$405	Designer and retailer of yoga-inspired apparel.
YogaWorks	Private	-	-	-	-	Owns and operates 18 yoga and Pilates studios.

*\*Prices and enterprise values as of September 2, 2008*

*\*\*CY08 sales estimates are Merriman Curhan Ford estimates when available; First Call consensus otherwise  
Source: Company report, First Call, Merriman Curhan Ford estimates*

## Fitness and Wellness Industry

**Wellness Products**

Given the aging population and obesity crisis, we believe more people are paying closer attention to the quality of the products, food and beverages they consume. As part of a healthier lifestyle, they use these products to help stave off disease, lower cholesterol, lose weight and achieve an overall better well-being. Natural and organic food and beverages, functional beverages (which offer health-promoting or disease-preventing properties) and all-natural beauty products promise to help people live healthier and feel and look better. We believe more people, especially boomers, are looking to healthy food and wellness products as the antidote to the negative effects of aging.

According to the Natural Marketing Institute (NMI), retail sales of U.S. consumer packaged health and wellness goods was \$102.8 billion in 2007, up 15% over 2006, and expected to reach \$170 billion by 2012.

- In 2005, global sales of health and wellness products exceeded \$420 billion (Agri-Food Trade Service).
- Sales of organic foods and non-alcoholic healthy beverages were up 25.0% in the 52 weeks ended April 2008, versus 4.4% growth in non-organic counterparts (Food Marketing Institute).
- Sixty-nine percent of Americans are incorporating foods such as products high in Omega-3 fatty acids to prevent diseases, like heart disease (Food Marketing Institute, 2007).
- Eighty-two percent of stores in 2008 featured natural or organic foods, up from 72% in 2006 (Food Marketing Institute).

**Wellness Product Revenues in 2007**

Categories	2007 Product Sales	% Growth YOY
Natural/Organic Personal Care	\$7.8 Billion	29%
Organic Foods and Beverages	\$19 Billion	25%
Natural Organic General Merch.	\$1.5 Billion	21%
Functional Foods	\$38.6 Billion	12%
Vitamins/Minerals/Herbal and Dietary Supplements	\$21.7 Billion	7%
Natural Foods/Beverages	\$14.1 Billion	4%

Source: NMI

**Sector Highlight: GAIAM, Inc.**

In our opinion, GAIAM will benefit from the healthy living trends described in this report. GAIAM is a vertically integrated lifestyle media company that provides a wide range of products and services focused on health and wellness, personal development, and social and environmental responsibility. This Lifestyle of Health and Sustainability (LOHAS) sector, a term GAIM coined, has a strong and devoted following of 41 million and represents a \$209 billion market in the United States (NMI, 2007). The company reported revenue of \$262.9 million in 2007, up from \$219.5 million in 2006 and \$142.5 million in 2005.

We believe GAIAM is a leader in the LOHAS space, making sales directly to consumers via Internet and catalog, as well as through retailers. The company's products are currently sold in more than 72,000 retail stores, including Target and Best Buy, and it has 7,500 "stores-within-stores" that integrate a section of GAIAM-only products into the existing space of a larger store to further showcase their products.

GAIAM is well-known for its fitness media, including award-winning yoga and Pilates videos. We believe that the company's line of yoga- and fitness-related products — such as DVDs, apparel and low-impact exercise equipment — should benefit from the positive yoga and exercise trends.

In addition to the fitness products, GAIAM sells many other products now in growing demand, such as natural beauty and household supplies, environmentally friendly products and natural health remedies. GAIAM continues to expand its footprint in stores and gain loyal customers, and we believe the company is well positioned to benefit from current trends and is poised for further growth.

## Fitness and Wellness Industry

## Selected Companies Participating Within This Industry

Company	Ticker (or Private)	Price*	Enterprise Value (M)*	CY07 Sales (M)	CY08 Sales (M)**	Description
Attune Foods	Private	-	-	-	-	Sells and develops probiotic snack bars, that aid in digestion.
Dean Foods Co.	DF	\$25.17	\$8,401	\$11,822	\$12,732	Under labels Horizon and Silk Soymilk sells Organic and Soy-based dairy products.
Dreamerz Foods	Private	-	-	-	-	Sells and develops all natural food products that aid sleep.
GAIAM, Inc	GAIA	\$12.73	\$243	\$263	\$285	Sells and manufactures consumer health and wellness products
LightFull Foods	Private	-	-	-	-	Sells and develops satiating 90 calorie smoothies.
NBTY, Inc.	NTY	\$33.24	\$2,103	\$2,019	\$2,315	Manufactures and retails nutritional supplements.
Organic to Go Food Corp.	OTGO	\$1.12	\$41	\$16	N/A	Prepares, serves, and caters meals using organic products.
Pharmaca Integrative Pharmacy	Private	-	-	-	-	Operates 23 stores integrating conventional prescriptions with natural health solutions.
Schiff Nutrition International, Inc	WNI	\$6.69	\$133	\$168	\$186	Develops and markets private label vitamins, nutritional supplements and nutrition bars.
Smart Balance, Inc	SMBL	\$6.40	\$660	\$111	\$216	Markets heart healthy food products such as spreads, oils and popcorn.
Tofutti Brands, Inc.	TOF	\$2.76	\$14	\$19	N/A	Develops and markets non-dairy, soy-based frozen desserts.
Whole Foods Market, Inc.	WFMI	\$18.31	\$3,401	\$6,592	\$8,152	Owens and operates 236 natural and organic foods supermarkets.

\*Prices and enterprise values as of September 2, 2008

\*\*CY08 sales estimates are Merriman Curhan Ford estimates when available; First Call consensus otherwise

Source: Company reports, First Call, Merriman Curhan Ford estimates

## Conclusion

Rising obesity levels and health care costs are providing a enormous opportunity for companies focused on reversing these negative trends. In addition, aging boomers' interest in well-being and longevity is a perfect complement to the nation's renewed interest in health. Gyms, fitness equipment, spas, yoga studios and wellness products are providing the tools for individuals to reclaim and maintain their health. And as individuals become more aware of the benefits of a healthy lifestyle, we believe these industries are poised to benefit.

**Greg Scott****Vice President, Equity Research*****Fitness and Wellness***

Greg Scott is a Vice President at Merriman Curhan Ford within the Consumer/Media/Internet group covering the Fitness and Wellness industry. Prior to joining Merriman Curhan Ford, he was a lecturer at the Department of Economics at the University of California, San Diego, where he taught courses in Microeconomics and Econometrics. He started his career as an intern with the domestic hedge fund at Nicholas Applegate Capital Management.

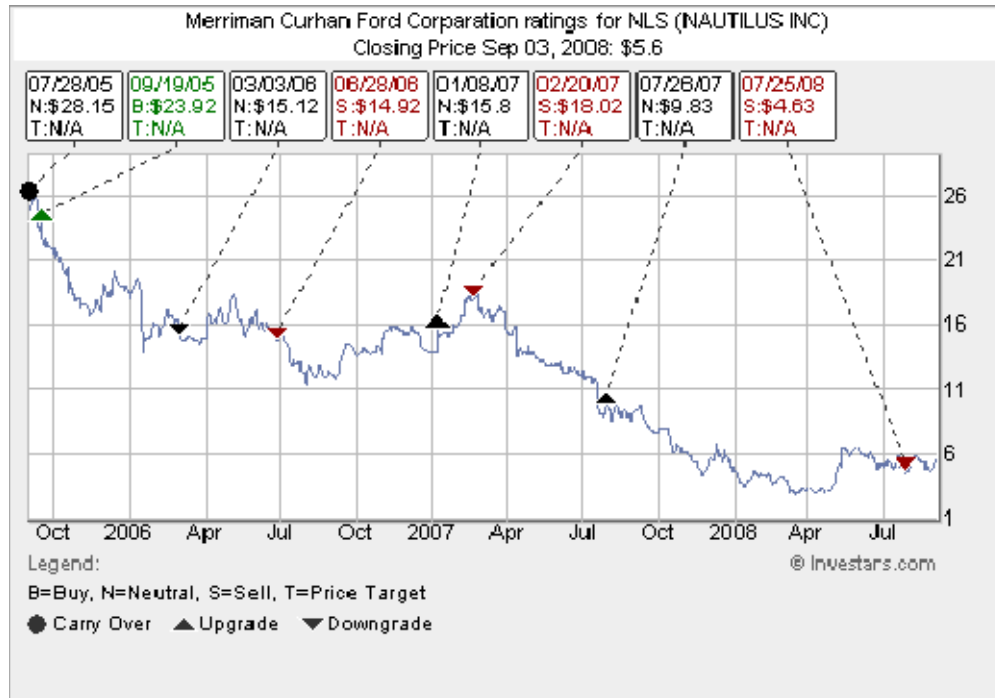
Mr. Scott is a member of the Consumer/Internet/Media research group covering the consumer health, fitness and wellness sector, with a focus on companies that offer products and services that help people to lead a healthier and more active lifestyle.

Mr. Scott earned both his M.A. and B.A. in economics from the University of California, San Diego, where he was also an NCAA All-American swimmer. Mr. Scott is based out of our New York office.

**Public Companies Mentioned in This Report***(Priced as of September 2, 2008)*

Aetna, Inc. (AET \$43.14, Not Rated)  
Amer Sports (OMX: AMEAS €9.50, Not Rated)  
Apple, Inc. (AAPL \$169.53, Not Rated)  
Best Buy, Inc. (BBY \$44.77, Not Rated)  
Brunswick Corp. (BC \$13.79, Not Rated)  
Cold Water Creek, Inc. (CWTR \$7.28, Not Rated)  
Cybex International, Inc. (CYBI \$3.35, Not Rated)  
Deutsche Bank AG (DB, \$85.86, Not Rated)  
Dean Foods Co. (DF \$25.27, Not Rated)  
GAIAM, Inc. (GAIA \$12.73, Not Rated)  
Google, Inc. (GOOG \$463.29, Not Rated)  
Health Fitness Corp. (HFIT \$1.75, Not Rated)  
J.C. Penny Co., Inc. (JCP \$38.97, Not Rated)  
J. Crew Group, Inc. (JCG \$26.41, Not Rated)  
Life Time Fitness, Inc. (LTM \$35.35, Not Rated)  
Lowe's Companies Inc. (LOW, \$26.33, Not Rated)  
Lululemon Athletica, Inc. (LULU \$19.37, Not Rated)  
Nautilus, Inc. (NLS \$5.32, Sell)  
NBTY, Inc. (NTY \$33.24, Not Rated)  
Nike, Inc. (NKE \$60.61, Not Rated)  
Schiff Nutrition International, Inc., (WNI \$6.69, Not Rated)  
Smart Balance, Inc. (SMBL \$6.40, Not Rated)  
Steiner Leisure, Ltd. (STNR \$35.40, Not Rated)  
Target Corp. (TGT \$53.02, Not Rated)  
Tofutti Brands, Inc. (TOF \$2.76, Not Rated)  
Town Sports International, Inc. (CLUB \$10.48, Not Rated)  
Toyota Motor Corporation (TM, \$88.83, Not Rated)  
Walgreen Co. (WAG \$36.00, Not Rated)  
Whole Foods Markets, Inc. (WFMI \$18.31, Not Rated)

Fitness and Wellness Industry



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Neutral	30%	42	MCF & Co believes the stock price is fairly valued at current levels. Maintain position or take no action.	1%
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