Webinar Series

International Perspective: Drivers in the EU M&A Market

Gambit Corporate Finance LLP

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About the Speaker:

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Geraint joined Gambit in 1999 and became a partner in 2003. During his career, Geraint has advised on a significant number of transactions including management buy-outs, development capital, fundraisings and acquisitions and he has a particular focus in private equity and venture capital. He acts for a number of institutional investors in relation to their portfolio work and his sector experience includes leisure, financial services, life sciences, food and consumer goods and support services.

He graduated with a first class honours degree in Biological Science from the University of Bristol in 1993. He qualified as a Chartered Accountant in 1996 when he was placed in the ICAEW United Kingdom National Order of Merit. Geraint passed the Securities Institute Corporate Finance Examination in 1997 and was awarded the ICAEW Corporate Finance Diploma in 2007.

Geraint is Managing Partner of Gambit and also a Board Member of Gambit's global network, Corporate Finance International.

Webinar Contents

Agenda

- 30 minute presentation
- Q&A to follow the presentation
- Submit questions at any time

Key topics

- UK / European Macroeconomic Update
- UK / European M&A Markets
- US / European Cross-Border Activity

Eurozone Debt Crisis: Recent History

Timeline

April 2010

The eurozone members and the IMF agree a €110 billion bailout package to rescue Greece

May 2010

Europe’s finance ministers agree rescue package worth €750 billion to ensure financial stability across Europe

November 2010

Ireland secures a €67 billion bailout agreement from the EU, IMF and certain countries

May 2011

Eurozone leaders approve a €78 billion bailout package for Portugal

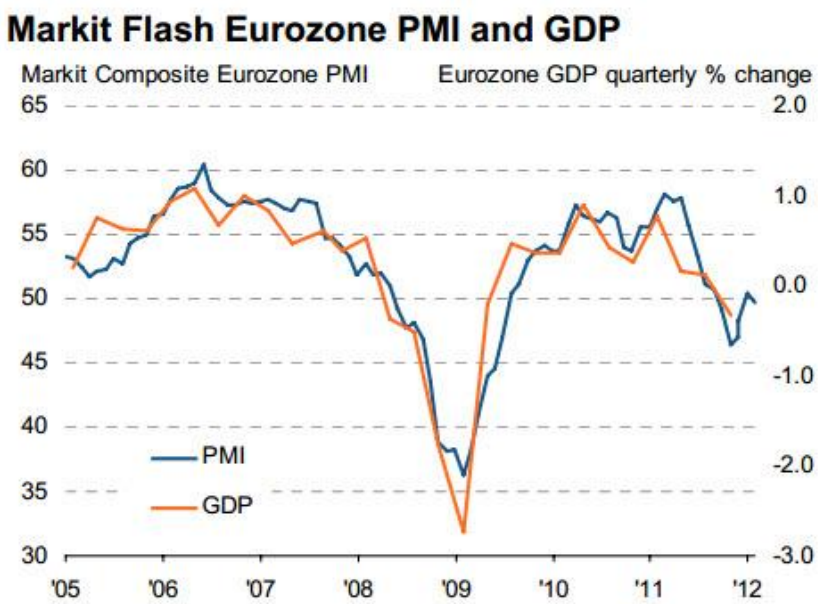
October 2011

A second bailout for Greece is agreed worth €130 billion

January 2012

Credit rating agency Standard & Poor's downgrades France and eight other eurozone countries, blaming the failure of eurozone leaders to deal with the debt crisis

Eurozone: GDP and economic sentiment



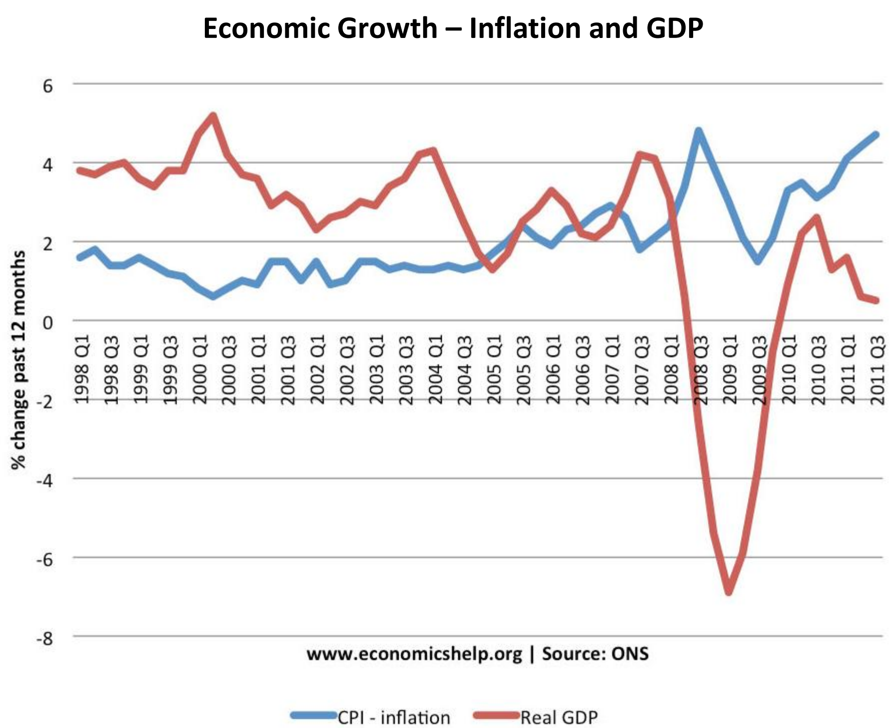
Source:
Markit, Eurostat

Key:
PMI – Purchasing Managers' Index

- The **EU** represents about **20%** of the global economy with **Germany, the UK and France** representing the **5th, 8th and 9th** largest economies by GDP
- The European economy began 2012 in **technical recession** due to financial market conditions deteriorating sharply and the global economy moving to a lower growth trajectory
- With the improvement in financial markets and significant policy action at EU level, stabilisation and confidence are set to return and **modest recovery** is expected in the second half of 2012
- GDP growth is forecast at 0%, with **negative GDP growth** expected in Greece, Portugal, Belgium, Spain, Italy, Cyprus, the Netherlands, Slovenia and Hungary
- Growth is expected in **17 member states**, including:
  Poland (2.5%) Lithuania (2.3%) and Latvia (2.1%)
- This reflects a more gradual return of **business and consumer confidence**, and therefore **investment and consumption**, as well as additional **fiscal consolidation** in a number of European countries
- Standard & Poor recently **downgraded** a number of countries including France and Austria from their AAA rating

UK / European Macroeconomic Update

UK: GDP and economic sentiment



- GDP growth for **2011** is estimated to have been **0.9%**
- Into 2012, a **fall in inflation to 2.6%** (having reached a peak of 5.2% in September 2011) is set to reduce the squeeze on disposable income, encouraging private consumption
- The large upward pressure that **rising energy prices** placed on inflation in 2011 will subside, with price reductions expected in the latter half of 2012
- **Investment is set to increase** into the second half of 2012 from a low base
- Recession should be narrowly avoided, with a modest improvement in GDP anticipated during the final two quarters aided by the London Olympics
- **External demand** is expected to be the strongest driver of GDP growth

Source:
Office for National Statistics

Key:
CPI: Consumer Price Index

UK / European Macroeconomic Update

UK: Corporate Outlook

Q1 2012 ICAEW Business Confidence Monitor ("BCM") Findings:

Business investment is important for future growth however **firms are reining in plans for capital investment**

Job creation plans remain subdued, though SMEs are more likely than larger companies to take on people in the next 12 months

Salary expectations for 2012 are depressed with businesses predicting modest increases of up to 2% - more unwelcome news for the squeezed consumer

The **BCM Confidence Index has steadied from -9.7 in Q4 2011 to -9.3.** This compares to +8.1 in Q3 2011 and shows the significant fall in confidence that businesses experienced over the last six months

19% of businesses **have above normal stock levels** due to a **lack of customer demand** and over half of businesses are **operating below capacity**

- Business leaders and investors appear to be growing used to the uncertainty, with the FTSE 100 up almost 19% in March 2012 from its low on October 4, 2011.
- BCM Confidence Index (www.icaew.com/bcm)

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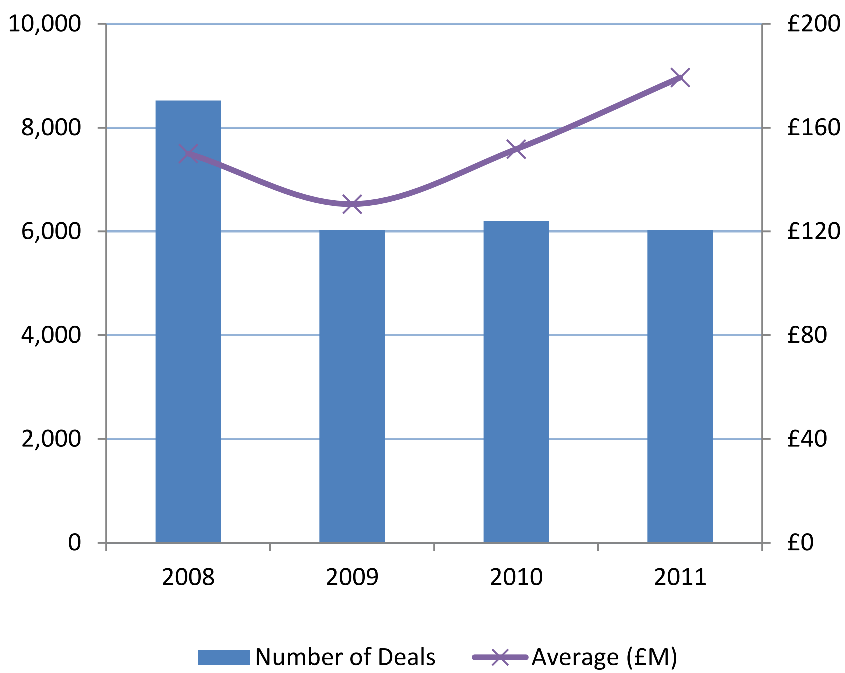
UK / European M&A Market

Merger and Acquisition Transactions Volume and Value



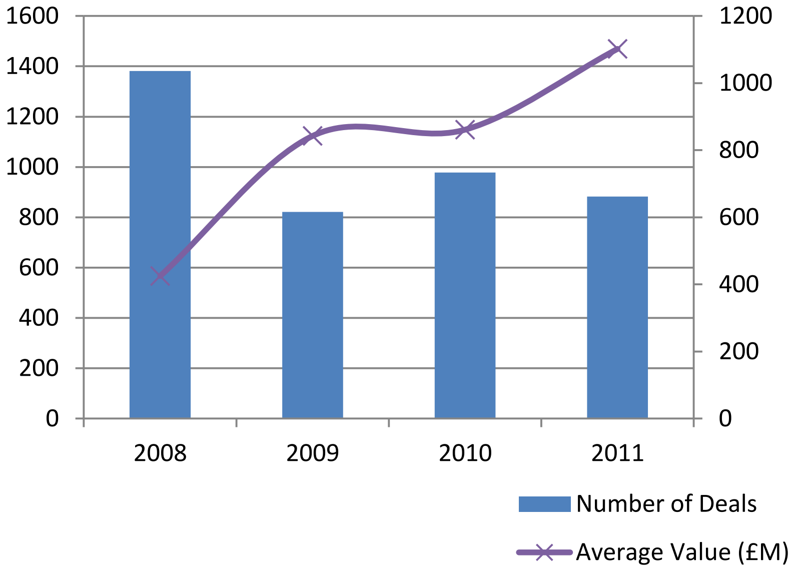
- European transaction activity continues to be affected by the **sovereign debt crisis** and consequent political upheaval
- There was a **reduced number of transactions** in the final quarter of 2011 and a 3% decrease between 2010 and 2011
- 2011 saw an **18% increase** in average transaction value from the previous year
- 2011 experienced a number of collapsed deals including the $8bn acquisition of ISS by G4S, a sign that markets were no longer comfortable with deals of such size and scale
- The **outlook for European countries** varies significantly between member states
- The strong **German economy** places it in a position set to see an increased number of deals completing in 2012

Source:
Corpfin/Gambit

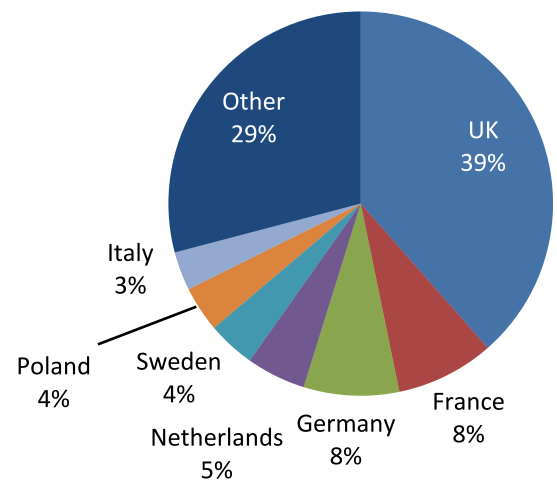
UK / European M&A Market

Inbound M&A: Cross-border Transaction Trends

Inbound EU transactions (European Targets)



Inbound Transactions by Geography in 2011



Source: Corpfin/Gambit

- **Fall in number of deals in 2011** but still above level for 2009
- The trend in inbound European cross border M&A is towards **consolidation**
- **Bolt-on acquisitions** are being prioritised as a way of growing businesses without the higher levels of risk associated with large acquisitions
- Large cross border acquisitions are still being completed, however, leading to an **increase in the average transaction value** over the past four years

- The **UK** continued to **dominate activity** during 2011
- Deal volume in Europe's largest economies saw a **general decline** through the year
- Second and third quarters of 2011 saw **highest** number of acquisitions by **US purchasers since 2000**
- 2012 will see an **increase** in US cross-border activity in Europe to take advantage of **attractive valuations**

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US / European Cross Border Activity

Key Drivers

Currency	▪ **Euro currency risk** is impeding transaction volumes ▪ The inclusion of **material adverse change (MAC) clauses**, pertaining to the collapse or partial break-up of the Euro became more common in 2011 ▪ Movements in US$ / Euro and US$ / Sterling exchange rates have **reduced entry cost** for European assets
Taxation	▪ Potential **financial transaction** tax could affect the UK's and Europe's standing as a cross-border M&A marketplace in 2012 but employment and social taxes also substantially differ ▪ Corporate **tax rates differ** across Europe: 20% in the UK, 33% in France, 29.8% in Germany, 31.4% in Italy
Regulatory	▪ The financial crisis brought a proliferation of **merger control regulations** ▪ **Regulatory burden** likely to increase in the rest of Europe
Labour Laws	▪ **Labour laws** and their impact are seen as unattractive and prohibitive in some countries e.g. France ▪ Most countries in the EU have made great strides towards more **investor-friendly** and **flexible labour markets** through initiating reforms in recent years ▪ Some **changes still evolving**, particularly in Eastern Europe, where most countries' labour laws still retain some of the original socialist tone

US / European Cross Border Activity

Key Drivers

Transaction Considerations	▪ The European debt crisis will **spur US cross-border activity** as acquirers take advantage of attractive valuations ▪ Acquisition of **key strategic assets and skill bases** will drive activity levels in 2012
Valuations	▪ Good assets still attract **good valuations** ▪ Valuation improvements are likely to be **sector specific**, such as the financial services sector
Sector Preferences	▪ The **energy sector** dominated markets in 2011, with improved valuations expected into 2012 ▪ Other **sectors exhibiting deal volume growth** in 2011 were Health Services, Insurance, Leisure and Business Services ▪ Industrial and financial institutions still have **strong assets** to dispose of which will keep markets active
Financing availability	▪ Financing remains a **significant stumbling block,** with acquisition financing bridge loans being replaced by high yield bonds as syndications are delayed ▪ Private equity players increasingly looking at **debt underwriting** ▪ An increasing number of deals are being signed subject to financing, adding a **level of conditionality** ▪ **Timing** for deal execution has substantially **increased**

UK/European Macroeconomic Update

Financing Markets

Current Debt Trends

- **Debt / EBITDA multiples increased** from 4.2x to 4.4x between 2010 and 2011 (average for 2000 to 2011 was 4.6x)
- **Average margin** on European deals **increased** from 250 bps to 450 bps between 2007 and 2011
- **Equity contribution** on LBOs has **increased** from 34% to 48% over the same period

Debt: Equity Ratios

- **Mid market companies** in the UK, France, Germany, Italy and Spain are **holding surplus cash** with cash-to-equity ratios 8.2% in 2010, compared with 6.8% in 2007 (€60 billion impact)
- **Gearing** has begun to **decline** falling to 24.9% in 2010, a decrease of 1.7% on prudent pre-crisis levels (€60 billion impact)
- More than **half of the mid size companies in the EU's** five leading economies have gearing levels of less than 10%
- Almost a third of UK companies had a **gearing ratio of less than 10%** in 2011
- The **lowest-performing 50%** of mid market European companies could release **some €125 billion in cash** for self-funding by improving management of working capital – largely inventory

Debt Pricing

- **Pricing expectation gap** between private equity firms seeking leveraged deals and banks seeking to mitigate losses continues to restrict deal volumes
- **ECB injected** three year funds totalling **€550 billion** in February 2012
- Benchmark **three-month euro Libor rates** fixed a basis point lower at 0.896% (February 2012)

Summary

- Eurozone GDP growth is nil as a whole
- Substantial economic variations within Eurozone, e.g. Greece vs Poland
- Eurozone confidence and consumption returning
- UK growth positive; inflation under control
- Eurozone companies have focused on liquidity
- Debt financing availability still an issue but freeing up gradually
- UK, Germany and emerging Eurozone seeing increasing activity
- Valuations vary across sectors
- Good assets still attract good valuations

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