

MULTIPLE FACTORS DRIVE RECORD LEVELS OF M&A ACTIVITY



Up 28% in the U.S. and 37% worldwide in 2005, according to market researcher Dealogic, merger and acquisition activity shows no signs of cooling off. The volume of private-equity backed deals in the U.S. has hit record levels this year, with the 500 transactions worth \$157.4 billion completed through June 14, 2006 eclipsing the previous record established in 2000. Experts attribute the frenzied pace of activity to a variety of factors.

“A key factor is the abundant amount of capital and credit available in the marketplace,” notes Frank Cannone, chair of the corporate department at Gibbons, Del Deo, Dolan, Griffinger & Vecchione, a 200-plus attorney regional law firm with offices in New Jersey, New York and Philadelphia. “There is an increased number of buyers and investors around the world, which is driving the supply-and-demand dynamic, and the secondary market for financial paper is strong.”

“It is a very good time for mergers and acquisitions,” agrees Barry Curtis, national managing partner, private equity services, at Deloitte in New York. “Interest rates have remained relatively low, credit market liquidity is strong, and we have a very stable economy. Private equity funds are raising record amounts of money, and we expect that to continue.”

AMPLE CREDIT AND AVAILABLE CASH

Industry participants describe the current debt market as the best since 1999. The percentage of banks relaxing their credit standards in 2005 was at its highest level in a decade, according to the Federal Reserve Bank, while default rates continued a downward slide to a 10-year low. Purchase price multiples in mid-market (up to \$50 million) leveraged buy-out deals hit a 10-year high, averaging 8.5 times before EBITDA (earnings before interest, taxes, depreciation and amortization), up from 5.9 times in 2001, according to Standard & Poor’s Leveraged Commentary & Data.

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Mark Kuehn, a corporate and transactional attorney at Gibbons, Del Deo and president of the New Jersey chapter of the Association for Corporate Growth (ACG), believes macroeconomic factors are also playing a role. “There are paradigm changes taking place in the global economy. Production and other activities are shifting out of the U.S., leaving fewer opportunities to invest directly in domestic operating enterprises,” he says. “But there is still plenty of capital available. With more cash and fewer things to buy, prices get driven up.”

Indeed, acquisition-minded companies—many of which are finding organic growth more difficult to achieve as they max out on cost-cutting benefits—are facing stiff competition from hedge funds and private equity firms for the complementary companies they would most like to acquire. In a break with their past, hedge funds are no longer limiting objectives to short-term returns. Many are actively seeking deals, especially leveraged buyouts, and have greater latitude than some of their competitors when it comes to the size, industry involvement and price of their acquisition targets.

DESIRE TO INCREASE REVENUE SPURS ACQUISITION FRENZY

However, while M&A volume and the price multiples commanded by acquisition targets are up, there is less speculation

evident in the marketplace than was the case when it last peaked. Today's dealmakers are more disciplined and transact deals only after lengthy due diligence, according to Daniel Varroney, chief executive officer of ACG. They continue to make strategic deals versus the more speculative ones of the past, he says.

The greatest number of investment bankers and other M&A professionals polled for the ACG/Thomson Mid-Year 2006 DealMaker's Survey, 46%, said their primary merger and acquisition objective was to increase revenue and profitability. A third were looking to grow market share and 5% were chasing new technology.

From an industry perspective, the sectors expected to be hottest through the remainder of 2006 are technology, cited by 27% of survey respondents, healthcare and life sciences (18%), and manufacturing and distribution (17%). The most important company attribute that matters to an acquirer today is sales and revenue growth (32%), followed by an attractive business sector (21%) and management strength (19%).

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