

## Mergers and Acquisitions

# From Private Equity to Privatization: The Deal Climate is Fast and Furious

Last year set a record for mergers and acquisitions worldwide. According to data from Thomson Financial, deals totaled \$3.79 trillion in 2006, 38% higher than in 2005. The U.S. came in at \$1.56 trillion, 36% higher than the year before. New Jersey, with its large corporate landscape and abundant small and middle market firms, reflects the national M&A market. Frank Cannone, chair of the corporate department at Gibbons, PC in Newark, and Cheryl Gorman, a Gibbons partner who heads the law firm's private equity group, help make sense of the deal-making frenzy.



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—Cheryl Gorman

**NJBIZ:** Has M&A in the region indeed been frenetic?

**Cannone:** The economy has been consistently strong. There's an incredible influx of capital that needs to be deployed—over \$1 trillion in private equity. Folks need to invest that capital or they are basically out of business. If they're not investing the capital, they're not creating returns. They're looking for opportunities. Those opportunities usually manifest themselves through acquisitions or joint ventures.

**NJBIZ:** What's driving the pace?

**Gorman:** There's a lot of money in the private equity funds right now. Some of the major funds had exceptional fundraising years, so I think you're going to continue to see a lot of capital deployed through the private equity side.

**Cannone:** What you notice is that even these large private equity buyout funds with billions and billions of dollars at their disposal are in dire need of transactions. They've moved into the middle-market area into relatively smaller transactions, those of a few hundred million dollars. They are evaluating these and deciding if they should make an investment.

**NJBIZ:** How is Gibbons involved in the private equity market?

**Gorman:** In the last few years we have been working with the State of New Jersey on the development of their alternate investment program. We were the lead outside counsel in helping them structure investments in private equity and real estate. They've also invested in hedge funds, so we've been representing investors in private equity funds and limited partnerships for the last couple of years.

**Cannone:** A private equity arrangement is one in which you've got a pool of capital at the disposal of business-minded folks that are looking to deploy it to realize certain returns, usually in a five to 10-year time period and they can do that by buying in certain industries or business sectors where they have requisite experience. The firm goes out in the marketplace and raises dollars from investors. At the top of the food chain you go to institutions and universities, endowments and state pension funds. We have been involved with the State of New Jersey's Division of Investments Alternative Investment Program. We help them as outside counsel in structuring that program. With the program in place, they've been deploying capital and we've been outside counsel on a significant number of their investments.

**NJBIZ:** Is New Jersey a hotspot for private equity deals?

**Cannone:** There are quite a few funds based in New Jersey and with a focus on

New Jersey. It's more the portfolio companies, the targets of those investment dollars, that would be located here because New Jersey is such an incredibly robust economic marketplace that runs the spectrum from biotech to real estate. Folks around the country and globe are looking for opportunities where New Jersey lends itself as a good place to acquire a company.

**Gorman:** The larger private equity funds are shifting a little more into the middle markets, which are companies between \$20 and \$500 million in revenues. A couple of the really big funds, Texas Pacific Group and Silver Lake Partners, formed their own smaller funds this year that are designed to go into the market and look for middle-market companies. New Jersey may well benefit from that.

**NJBIZ:** Despite the significance of M&A, the success rate is low. What are your thoughts on successful versus failed M&A?

**Gorman:** There are a couple of things a portfolio company can do to bring itself into a good position for a successful acquisition by a strategic buyer or private equity firm. These include keeping their house in order, keeping their audited financials up to date and making sure their contracts can be assigned and that they have an attractive asset base.

**Cannone:** It comes down to due diligence during the acquisition and in the marketplace and understanding why you're buying it and what you're buying. Also that you transition employees in an effective manner that allows the business to operate as efficiently as before. Recognize the incredible disruption that a seller experiences after the acquisition. You've got new owners, a new business plan and there's a good chance that senior management may no longer be a part of that company. That transition is critical to the success of that business and to the acquirer's business. It comes down to diligence and integration. You can't just buy a company and go on to the next deal.

**NJBIZ:** ACG-NJ, an organization focused on deal making, recently held a forum on global investing that featured The Tata Group discussing Indian acquisitions of U.S. companies. Are you seeing a great deal of foreign investment in the regional marketplace?

**Cannone:** We're definitely seeing it. You'll have multinational companies that are looking to tap into expertise in the area. The value of the U.S. dollar is less than foreign currency so there's an inherent value there. Private equity overseas is more and more prevalent. In addition, U.S.-based companies and others looking for capital have gone to Europe to raise capital. That capital gets deployed to a large degree in the U.S. For example, we recently represented Schmolz + Bickenbach AG, a Swiss company, with respect to a major acquisition of all of the A. Finkl & Sons steel operations in North America. This is a major corporation with in excess of \$260 million in revenue and over 900 employees. That's a perfect example of the influence of foreign investors in the U.S.

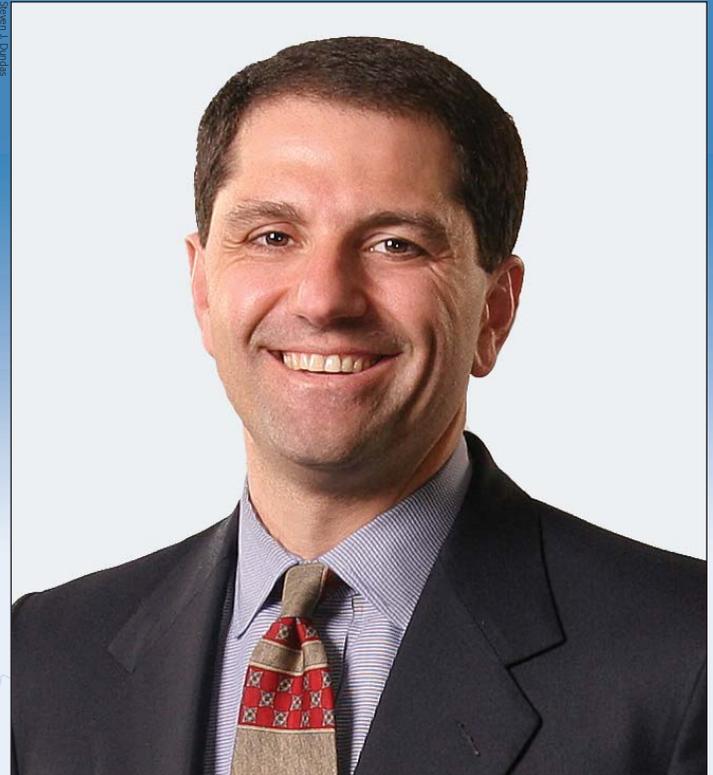
**NJBIZ:** What else can we expect from the M&A market in 2007?

**Gorman:** With all the money in the private equity community right now and with their focus, their entire job is 24/7 looking for deals. I think you're going to see a lot more private equity deals in the market in 2007.

**Cannone:** One other thing you are seeing a lot of on the private equity side are club deals, which are arrangements where one or more private equity organizations get together and joint venture a deal. They would do that maybe because there is a limitation on that particular fund's ability to be in a certain industry. Say that particular fund is only allowed to deploy 20% to biotech or 30% in real estate. They'll team up with another fund. Although they are all competitors, they are also colleagues because it's not that big of a universe. IP-based businesses or businesses that have intellectual property assets has also become a fundamental aspect of what buyers in M&A are looking for.

**NJBIZ:** Can you explain further how intellectual property fits with M&A?

**Cannone:** You're trying to find an unlocked value. For instance, we represent a Japanese public company's U.S. operations for intellectual property and other matters. We represent them in connection with acquisitions based on intellectual property assets. In one particular situation, a company owned the proprietary rights to this asset, a kind of technology, that this client wanted. We went through protracted negotiations of buying out that business. The key revenue generation



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—Frank Cannone

here was intellectual property-oriented, but we acquired the whole company—the employees, the real estate, all the nuts and bolts. The underlying asset, the value, was the intellectual property. The future of M&A is intellectual property-related assets. It can be anything: copyrights, trademarks, patents. As an advisor, you need to understand the underlying asset or value of what you're buying.

**Gorman:** I work closely with a company, Elusys Therapeutics in Pine Brook, that is working on an anthrax therapeutic. That is another example of intellectual property. They're working with a technology that will result in a shot that you can give to a mailman that might be exposed to anthrax.

**NJBIZ:** Life science businesses like Elusys are fundamental to the growth of the New Jersey economy. What else do you consider key to economic development?

**Cannone:** The business community in New Jersey has a challenging regulatory framework that needs to be addressed by Trenton, from employment laws to regulations that inhibit a business's ability to grow and expand.

**Gorman:** I also think you're going to see more active development of Asbury Park, Newark, the major cities. That is going to be more of an attraction for businesses looking to move into New Jersey. The state has made it less restrictive to move into urban areas. You see capital going into the urban areas for real estate development purposes.

**NJBIZ:** What are your thoughts on the privatization of public infrastructure?

**Cannone:** These states are trying to create liquidity out of their assets and securitize them. The tension you have is that you are going to give up entitlements to those assets for future generations. And will those funds be used for the proper designated purposes? This is another situation where private equity has pooled billions of dollars in anticipation for states around the country to start to securitize their assets. They're waiting on the sidelines for it to happen. Does it make sense? It's on a case-by-case basis. ■ M&A