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Global Overview

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Increase in private equity activity contributes to global M&A activity levels

M&A activity in 2011 benefited from the upward momentum established in the second half of 2010, with 2011 levels ending slightly higher than those in 2010. However, the impact of the sovereign debt crisis in Europe and the downgrade of the United States' credit rating, coupled with the accompanying political clashes and negotiations which ensued both in Europe and in the United States, destabilised the markets and, in particular, the debt financing markets. This resulted in a marked slowdown in deal activity in the second half of 2011 as compared to the first half of the year.

For the year, global-announced M&A deals in 2011 totalled approximately US$2.6 trillion, which represented an increase of 7 per cent from 2010 totals. However, there were slightly more than 40,000 announced deals worldwide in 2011, which represented a 5.5 per cent decrease in the number of deals as compared to 2010. Worldwide private equity backed activity totalled US$306.3 billion in 2011, representing a 32 per cent increase over 2010. As a result, financial sponsors accounted for approximately 11.9 per cent of announced M&A transactions worldwide during 2011 compared with approximately 9 per cent in 2010 and 6 per cent in 2009 (all of the above statistics supplied by Thomson Reuters).

Americas

Announced M&A deal volume in 2011 in the Americas totalled approximately US$1.25 trillion, which represented an approximately 14.4 per cent increase from the levels in 2010. US-based LBO transactions decreased to approximately US$147 billion in total in 2011, as compared to US$161 billion in 2010 (Pitchbook). However, larger private equity M&A transactions remained steady in 2011. Of the United States private equity M&A transactions with disclosed purchase prices in 2011, 7.5 per cent had total purchase prices of more than US$1 billion, compared to 5 per cent in 2010 and 2.2 per cent in 2009, and 15 per cent were valued between US$500 million and US$1 billion in 2011, as compared to 14 per cent in 2010 and 6 per cent in 2009 (Pitchbook). Notable private equity acquisitions in the Americas included the acquisition of Centro Properties Group's US shopping mall business by affiliates of The Blackstone Group for approximately US$9.4 billion, the acquisition of Samson Investment Company by a consortium comprised of affiliates of Kohlberg Kravis Roberts & Co, Natural Gas Partners, Crestview Partners and Itochu Corporation for approximately US$7.2 billion and the acquisition of Kinetic Concepts Inc by a consortium comprised of affiliates of Apax Partners, the Canada Pension Plan Investment Board and the Public Sector Pension Investment Board for approximately US$6.3 billion.

Europe, Middle East and Africa

Announced European, Middle Eastern and African (EMEA) M&A deal volume reached approximately US$760 billion in 2011, which represented a 4.7 per cent increase from the volume in 2010 (Thomson Reuters). EMEA targeted buy-side private equity sponsor activity totalled approximately US$97 billion, as compared to US$83.1 billion in 2010 (Thomson Reuters). Such financial sponsor activity declined each quarter in 2011 reaching US$19.8 billion in the fourth quarter of the year (Thomson Reuters). The declines in EMEA M&A financial sponsor activity appear to be attributable to the European sovereign debt crisis. Notable European private equity transactions in 2011 included the approximately US$3.4 billion acquisition of Securitas Direct AB by affiliates of Bain Capital and Hellman & Friedman, the approximately €2.1 billion purchase of SPIE SA by affiliates of Clayton, Dubilier & Rice, AXA Private Equity and Caisse de dépôt et placement du Québec and the agreement by affiliates of 3i BC Partners to acquire Com Hem AB for approximately US$2.6 billion.

Asia-Pacific

Announced M&A deal volume in Asia-Pacific totalled approximately US$550 billion in 2011, which represented a 4.3 per cent decrease from deal volume in 2010 (Thomson Reuters). Asia-Pacific private equity activity accounted for approximately 18 per cent of global private equity activity in 2011, compared to approximately 12 per cent in 2010 (mergermarket). India and China garnered the largest volume of private equity buyouts, followed by Australia, Japan, Korea and Southeast Asia (mergermarket). However, in terms of value, China led the region with approximately US$20 billion of volume in 2011, followed by Australia, Japan, Southeast Asia, India and Korea (mergermarket). Notable private equity transactions in Asia included the approximately US$13.7 billion sale of Nycomed AB by affiliates of Nordic Capital, DLJ Merchant Banking Partners and Avista Capital Partners to Takeda Pharmaceutical and Bain Capital's acquisition of Skylark Co Ltd from Nomura Holdings Inc for approximately US$2.1 billion. In addition, a number of private equity-led 'going private' transactions involving U.S.-listed companies, which primarily operate in mainland China were announced or consummated in 2011. These transactions included the approximately US$755 million take private of Harbin Electric Inc led by Abax Global Capital, the approximately US$443 million take private of Funtalk China Holdings led by PAG Asia Capital and the approximately US$293 million take private of Chemspec International led by Primavera Capital.

Challenging financing markets

Financial sponsors found the financing markets in 2011 to be challenging – the percentage of debt used in private equity transactions under US$1 billion dropped to a 10-year low of 46 per cent (Pitchbook). In addition, consistent with M&A activity levels during the course of the year, the first half of the year provided private equity sponsors with relatively strong debt financing markets to fund acquisitions, with debt-to-EBITDA ratios for LBOs with more than US$50 million of EBITDA reaching an average of 5.4x EBITDA in the second quarter in 2011, as compared to 4.7x and 4.0x EBITDA for all of 2010 and 2009 respectively (Standard & Poor's Leveraged

Commentary and Data). However, both financing and deal activity suffered a marked slowdown in the second half of the year. The slump was a result, in part, from the European sovereign debt crises and the political stand-off in the United States over increasing the debt ceiling. Financing for sponsor acquisitions became increasingly expensive as these issues came to the forefront and credit markets tightened.

Add-on activity remains strong

As was the case in 2010, private equity sponsors completed a robust number of add-on acquisitions to their existing portfolio companies. Private equity portfolio company add-on transactions accounted for 50 per cent of all US buyouts in 2011, as compared to 47 per cent of all US buyouts in 2010, and marked the seventh consecutive year there had been an increase in the relative percentage of add-on activity in US buyout transactions. Private equity firms and their portfolio companies completed 656 add-on transactions and spent approximately US$25 billion in add-on acquisitions in 2011, which nearly doubled the total spent in 2010. The median add-on transaction size for private equity sponsors and their portfolio companies in 2011 was US$80 million, as compared to US$51.5 million in 2010 (all of the above statistics supplied by Pitchbook).

Portfolio company sales and IPOs

Financial sponsors effected approximately US$268.1 billion of exits as compared to approximately US$221.9 billion in 2010, which represented the highest total value for exits since 2007 (mergermarket). In addition, the number of private equity sponsor exits remained relatively steady in 2011 as compared to 2010 – there were 420 exits in the United States in 2011, as compared to 434 in 2010. Interestingly, private equity sponsor exit activity in the United States avoided the second half slowdown seen in the M&A markets generally, with more exits completed in the second half of the year (213) than the first half of the year (207). Portfolio companies sold in the United States to strategic acquirers remained the most common method for private equity sponsors to exit their investments, with a total of 240 such exits in 2011 totalling over US$78 billion and with a median sale price of US$240 million, which is the highest on record (all of the above statistics provided by Pitchbook). In addition, according to Pitchbook, there was not a noticeable increase in private equity sponsors selling portfolio companies to other private equity sponsors. Notable portfolio company sales included the approximately US$8.5 billion sale of Skype Global Sàrl by affiliates of Silver Lake Partners, eBay International AG, CPP Investment Board, Joltid Limited in partnership with Europlay Capital Advisors and Andreessen Horowitz to Microsoft Corp, the approximately US$4.5 billion sale of Graham Packaging Company, a publicly traded portfolio company of The Blackstone Group, to Reynolds Group Holdings Limited and the sale by Kohlberg Kravis Roberts & Co of its stake in Seven Media Group to West Australian Newspapers Holdings for approximately A$4.1 billion.

According to a study by Ernst & Young which utilised data provided by Dealogic, private equity-backed IPOs accounted for 24 per cent of the global proceeds raised in 2011, which is the highest percentage on record. Approximately US$31.4 billion was raised in private equity-backed IPOs in the first half of 2011, although this number fell dramatically to approximately US$5.5 billion in the second half of 2011. Through November, listings on exchanges based in the Americas raised US$28.4 billion in 2011, which represented an 88 per cent increase in value over the same period in 2010. Notable private equity portfolio company listings included the approximately US$4.4 billion listing of HCA Holdings Inc, the approximately US$3.3 billion listing of Kinder Morgan Inc and the approximately US$1.9 billion listing of Nielsen Holdings NV.

In the EMEA region, there were only 12 private equity-backed deals, which raised approximately US$2.9 billion on EMEA exchanges and which represented a 71 per cent decline in value and a 45 per cent drop in volume compared to 2010. Notable listings included the approximately US$675.5 million listing of FSW Immobilien AG and the approximately US$575 million listing of Etalon Group Ltd. In Asia, private equity-backed companies raised US$5.6 billion in 25 IPOs, which represented a 36 per cent decline from the US$8.8 billion raised in 45 IPOs over the same period in 2010. Hong Kong was the most popular exchange with six IPOs raising an aggregate of US$2.8 billion, but mainland China exchanges such as Shanghai, Shenzhen main board and ChiNext are becoming more popular with five IPOs raising an aggregate of US$1.4 billion in total proceeds. Notable listings included the approximately US$1.3 billion listing of Samsonite International in Hong Kong and the approximately US$757 million listing of Far East Horizon Ltd in Hong Kong.

Stagnant private equity fundraising

The downward trend in private equity fundraising continued through 2011. Despite a strong second quarter in 2011, in which 189 private equity funds raised a total of approximately US$88.4 billion, private equity firms around the globe only raised a total of approximately US$263 billion for the full year in 2011, which was a decrease from approximately US$274 billion raised in 2010 (Preqin). In particular, private equity fundraising finished the year poorly in 2011, with a total of 108 funds raising approximately US$54.4 billion in the fourth quarter, which represented the lowest quarterly total since the beginning of the financial crisis (Preqin). Buyout funds were the most active in the fourth quarter of 2011, with 19 funds raising a total of approximately US$18.4 billion (Preqin).

However, private equity fund raising in the United States was strong in 2011. A total of 404 private equity funds completed a final close in 2011 in the United States, raising approximately US$122.4 billion, as compared to US$100.5 billion raised by 409 funds in 2010. In the United States, buyout and corporate finance funds raised US$86.7 billion across 175 funds in 2011, which represented a 42 per cent increase from the levels in 2010. Buyout and acquisition fundraising alone increased significantly as 75 funds raised approximately US$43.3 billion, which is more than twice the 2010 totals (all of the above statistics provided by Dow Jones).

In Europe, 140 private equity funds raised a total of US$52.9 billion of capital. European buyout and corporate finance funds raised approximately US$42.1 billion in 2011, which represented an 88 per cent increase from the previous year. Buyout and acquisition funds alone accounted for 40 such closings and raised approximately US$28.4 billion, which represented a 165 per cent increase from the levels in 2010 (all of the above statistics provided by Dow Jones).

According to the Emerging Markets Private Equity Association, fundraising in Asia, buoyed by China, remained strong in 2011. Private equity funds focused on Asia raised US$23.7 billion, capturing 73 per cent of all capital raised through September, which represented a 167 per cent increase from the US$14.2 billion raised for the region in all of 2010. In addition, private equity fundraising in Brazil reached a record US$4.5 billion, surpassing the 2008 peak of US$3.6 billion, and which also represented a 400 per cent increase over the fundraising levels in 2010 (all of the above statistics provided by Emerging Markets Private Equity Association).

Outlook for 2012

Many M&A practitioners and industry participants expect that global M&A activity and private equity deals will remain somewhat flat until there is clarity on the European sovereign debt crisis as well as an understanding of the long-term future of the Euro.

In a Bloomberg survey of over 1,000 industry participants, survey participants indicated their belief that, for 2012, weak economic growth will be the most significant obstacle to M&A activity. Many believe that the Asia-Pacific region will have the largest increase in M&A activity in 2012, bolstered by the marked increase in M&A activity in Japan in 2011 (Deloitte). As was the case in 2011, the energy and power sector is widely considered to present the greatest opportunities for M&A activity in 2012. Capital investment in the energy and power sector by private equity sponsors totalled approximately US$24.96 billion in 2011, which represented a nearly 50 per cent increase from the levels in 2010 and double the levels in 2009 (Pitchbook). The energy and power sector totalled 19.8 per cent of global M&A activity in 2011, and may remain one of the most active areas for mergers and acquisitions activity and private equity sponsors in 2012 (Thomson Reuters).

It remains to be seen when private equity mergers and acquisitions activity will begin a turnaround from the second half swoon in 2011. An increase in private equity mergers and acquisitions activity will be dependent on a number of factors. A critical factor will be the availability of debt financing on acceptable terms. Many industry participants and practitioners believe that improvements in the financing markets and the availability of leveraged loans will be tied to the resolution of the Eurozone sovereign debt and currency issues.

In addition, stemming partly from Bain Capital co-founder Mitt Romney's participation in the Republican Party's primary race leading up to the 2012 US presidential election, there has been renewed public debate regarding the private equity industry and its impact on the US and global economies. Industry critics argue, without the support of empirical data, that private equity sponsors extract value from their portfolio companies while over-leveraging company balance sheets and laying-off employees to cut costs. This debate will likely make private equity a politically sensitive issue in the United States during the pendency of Mr Romney's campaign, and could impact overall activity levels for private equity firms.

With respect to realisations, despite a strong year for private equity sponsor exits, there remains a great deal of pressure on financial sponsors to sell their portfolio companies and return capital to investors. The pressure to complete these exits resulted in private equity sponsors selling portfolio companies at an average enterprise valuation of 11.9x EBITDA in 2011, which is a decrease from 12.5x EBITDA in 2010 and the lowest level since 2004 (all of the above statistics provided by mergermarket). It is expected that there will be an ongoing focus on private equity sponsor exits in 2012, although this will depend on the state of the capital markets and whether there remain attractive opportunities to exit via initial public offerings or sales of portfolio companies, or both.

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