M&A Insights

Are you wired for success in 2010?

A number of mega-cap technology deals are set to complete in the next three months, presenting a strategic challenge to competitors without deals in the pipeline.

Stay ahead.

PricewaterhouseCoopers

Welcome

Welcome to the 2010 edition of Technology M&A Insights. This annual report by PricewaterhouseCoopers (PwC) forecasts the outlook for M&A activity in the global technology sector in 2010 and reviews the challenges the sector faced during 2009.

It has certainly been a turbulent year, but the technology sector has weathered the storm better than most. M&A activity was significantly down in 2009, with global deal volume and value falling by 48% and 60% respectively, but the sector was notably less moribund than many others. The tide is certainly turning; with a number of major announced transactions due to close in Q1 2010 and private equity returning to the market more aggressively, 2010 looks set to mark a major upturn in deal activity.

The headlines of the recovery are being written by a number of larger transformational deals driven out of the US. Service offerings are being broadened to meet the demands of customers for more integrated solutions, whilst cash rich corporates look to deliver bottom line returns and growth from high synergy transactions. We fully expect this increased activity to filter through to the mid-market in 2010, which remains the prime battleground for UK and European M&A activity in the technology sector.

The capital markets have bounced back strongly. The UK FTSE Software and Computer Services (SCS) Index ended 2009 up by 64% compared with rises in the FTSE 100 and NASDAQ of 22% and 44% respectively. It remains to be seen whether the momentum can be maintained through 2010; sceptics will note that there hasn't been such a notable outperformance of technology stocks since the dot com bubble of 2000.

We are now in a test period for M&A, where more quality assets are coming to market than we have seen in 18 months. Successful completions will not only depend on a continued improvement in financing liquidity and confidence, but also on an alignment in value perception and price expectations between vendors and acquirers.

There is much excitement around the growing IPO pipeline for 2010. Some technology companies have already signalled their intention to float, notably the UK security software firm Sophos, which has signalled its plans to list on Nasdaq later this year, two years after abandoning plans to list in London because of market volatility. However, many of those flagged for IPO may well succumb to the greater certainty which may be offered by the embrace of a strategic trade suitor.

The Technology Deal Team at PwC has also had an active year. In the UK, headline deals included the investment by HgCapital in Epyx, the leading automotive services SaaS platform, the acquisition of Borland by Micro Focus, the sale of secure payments software provider Orbiscom to MasterCard and the sale of broadband networking solutions provider Synetrix to Capita. We look forward to continuing to help our clients shape the future of the industry in 2010.

If you would like further information, or to discuss in more detail any of the themes raised in this report, please do not hesitate to contact either of us or your PwC relationship team.

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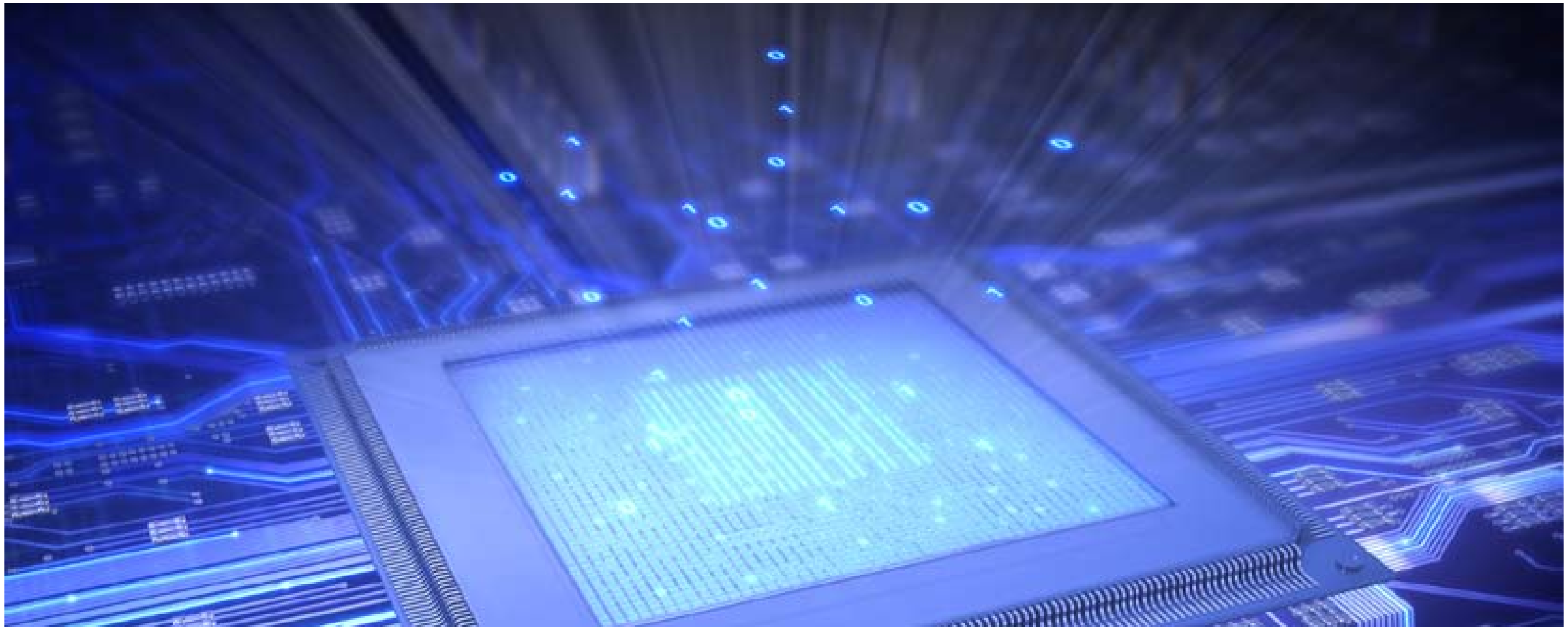
Outlook for 2010

After a relatively quiet year in 2009, the technology M&A market is now in a test period with the highest level of quality assets coming onto the market since the first half of 2008.

At least €15 billion of announced deals are set to complete in the first quarter of 2010. Successful completions will depend on vendor price expectations coming into line with those of acquirers but if the majority of those deals currently in process close, we can expect a sharp pick up in transaction activity in 2010.

The mid-market provides the potential for a rich seam of infill acquisitions, but the dynamic of vendor price expectations relative to those of would-be buyers remains sensitive. Deals designed to plug gaps in solution portfolios and through cost synergies, drive out cash flow and boost underlying earnings, will be able to bridge the value gap. However, both buyers and sellers must embrace a new era of realism if deals are to complete.

While bottom line profitability in the UK technology sector has been managed effectively for many in 2009, achieving top line growth is a different matter. Acquisitions are likely to be an integral part of most corporate growth stories. This will be bolstered by confidence gradually returning to the market place and improving liquidity conditions, affecting an upturn in acquisition - led growth stories over the course of 2010.



Deal hot spots for 2010 (continues overleaf)

The Big Five to watch - FinTech, SaaS, Convergence, Healthcare and Security.

Financial Technology gets back on track. The financial market turmoil triggered by the high profile banking casualties in the second half of 2008 inevitably caused problems for FinTech vendors. However, a number of positive market drivers have since spurred recovery within the sector. These include the significant increase in financial regulation with a need for heightened compliance and risk management solutions and the volume of financial data being processed. In addition, the focus by institutions is on reducing their cost base and improving efficiencies which can be achieved, in part, by expanding and upgrading IT systems.

Carve-outs from financial institutions and smaller infill deals are expected to prevail within the FinTech sector over the next 12 months but M&A activity will require creativity in terms of deal structures to achieve premium valuations.

Software-as-a-Service (SaaS) moves into the mainstream. As we predicted last year this is the real hot spot in the world of applications. Whether hosted, in the cloud or managed within a customer's IT infrastructure, the SaaS model is gaining significant momentum as organisations see the benefits of moving large-scale software expenses from their capital budget to their operating budget.

Every software vendor, it seems, now needs to have a SaaS offering or at least a competitive response. It is still relatively early days in the SaaS evolution, but it is certainly driving increased M&A activity and premium valuations. The number of genuine SaaS delivery models with any scale remain limited. Those that have started to gain critical mass are increasingly attractive targets for both trade and PE, who like dynamic growth, cash profile and forward visibility.

Convergence is now taking a real grip on the deal market. Apple and Google are going head to head with Microsoft waiting in the wings, whilst HP have set out their stall to take a far greater share of Cisco's home territory. Meanwhile the hardware players are making an increasingly aggressive push into services.

Whilst we can expect some more strategic moves at the top of the food chain, this will undoubtedly have a ripple effect across the market. There will be some previously unlikely tie ups in 2010 as players from all sides look to develop the right competitive response.

Mobile access to the internet will continue to grow in importance both from a consumer and corporate perspective as evidenced by Google's 'go-it-alone' launch of the Nexus One handset. Software providers, handset manufacturers, infrastructure vendors, and carriers will all continue to vie to build successful models in the space throughout 2010. From a corporate and public sector end user perspective, successfully enabling truly mobile workers can deliver significant and much needed operational efficiencies, and it is likely that significant M&A activity will result as providers look to service this demand.

Deal hot spots for 2010

Healthcare Software and IT Services (SITS) M&A has remained buoyant and we expect this to continue with good opportunities for consolidation across health and social care solutions.

Healthcare IT is drawing attention following the review of public sector spending in the UK and the proposed Obama healthcare plan in the US. Both will be long-term growth drivers since further IT investment will be required to achieve transformational cost savings.

Recent healthcare IT transactions include the acquisition of Scriptswitch by United Health Group of the US for €56 million and that of Liquidlogic by System C for €17 million.

Security solutions and the encrypted transmission of data will remain of paramount importance across both the public sector and commercial arenas. Transactions in the security solutions space have therefore held up well throughout the downturn with a spate of deals over the last 24 months. SaaS provides the perfect mechanism for the delivery of much security software with a number of vendors now providing a fully hosted, highly-scalable online platform.

A year-end rush re-ignites the market (continues overleaf)

M&A activity in the global technology sector was relatively quiet last year, although a spate of announced mega-cap deals in Q4 has provided promise for 2010.

Completed deal volume fell by 48% to 297 transactions in 2009 compared with 570 in 2008. Their aggregate value was down by 61% to €36.8 billion from €93.2 billion the previous year.

Although these figures present a superficially gloomy picture, dig a little deeper and a more positive perspective appears with a steady stream of deals at the top end of the market. Last year still saw eight €1 billion-plus technology deals completed (compared with ten in 2008).

The magnitude was scaled back with the largest being the €2.7 billion acquisition of Perot Systems, the US provider of IT services and business solutions, by Dell. In comparison, we saw four deals break through the €5 billion barrier in 2008.

Private equity showed it could still command a seat at the big ticket deal table with the €1.9 billion public-to-private LBO of the UK set-top box software-maker NDS Group by Permira, in conjunction with News Corporation.

Technology Sector Top 10 Global Deals 2009

Date	Bid Value (€m)	Target Full Name	Nationality	Bidder Full Name	Nationality
Nov-09	2,735	Perot Systems Corp	United States	Dell Inc	United States
Dec-09	2,042	Starent Networks Corp	United States	Cisco Systems Inc	United States
Feb-09	1,915	NDS Group Plc (77%)	United Kingdom	Permira Advisers (London) Ltd	United Kingdom
Jul-09	1,591	Data Domain Inc	United States	EMC Corp	United States
Nov-09	1,417	Skype Technologies SA (70%)	Luxembourg	Silver Lake Partners LP; Canada Pension Plan Investment Board; Index Ventures; Andreessen Horowitz Fund	United States
Mar-09	1,260	Foundry Co (66%)	United States	Advanced Technology Investment Co	United Arab Emirates
Oct-09	1,256	Omniture Inc	United States	Adobe Systems Inc	United States
Dec-09	1,112	TASC Inc	United States	General Atlantic LLC, Kohlberg Kravis Roberts & Co	United States
Oct-09	881	SPSS Inc	United States	Emerson Electric Co	United States

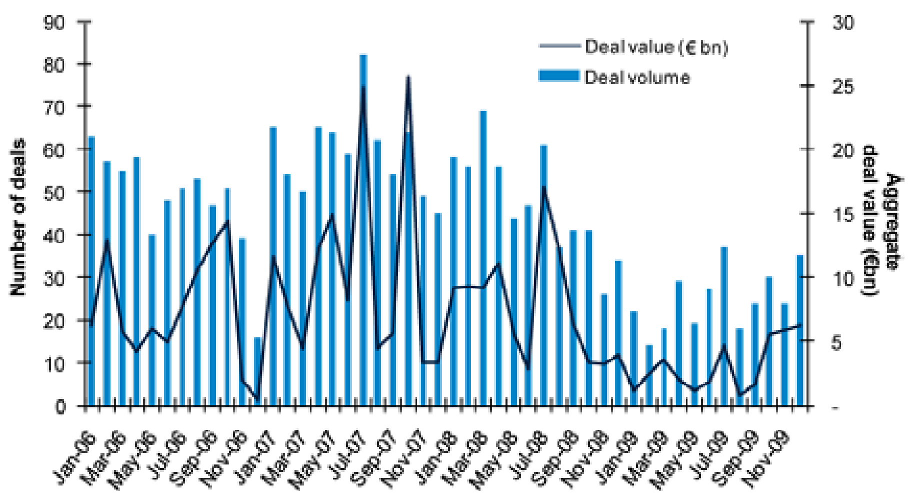
Source: Dealogic, M&A Global, Mergermarket

A year-end rush re-ignites the market

Mega-deals such as these reflect some of the defensive attributes of the technology industry, led by the fact that it is less highly geared than other sectors. The average debt to equity ratio of companies within the FTSE 100 index is in the region of 29%, but the FTSE Software and Services portfolio stands at about -2%, reflecting the net cash position of many publicly-owned technology companies.

Distressed sales were, therefore, not a major feature of the technology M&A market last year. Many cash rich corporates were searching hard for transaction opportunities to put that cash to work, with valuations for those deals that did happen holding up well, often sustained by strong strategic rationale and significant realisable synergies.

Monthly deal value and volume



This chart covers completed global M&A transactions, involving stakes greater than 10%, where the deal value was disclosed and greater than €10 million

Source: Dealogic, M&A Global, Mergermarket

Game changing deals accelerate activity

With a number of bulge bracket deals set to complete in the first quarter of 2010, a significant revival in global technology M&A is almost a certainty.

Further significant transactions are likely to follow, giving a fillip to the sector and presenting a strategic challenge to competitors who will need to plan a suitable response.

Although the technology M&A market was relatively subdued for much of 2009, it sprang back to life in the final four months of the year with the announcement of five €1 billion-plus deals. A number of these could be potentially game changing and signal a renewed convergence battle ground, as the sector's global giants continue to invade each others' territories to become 'one-stop' providers of computing, networking and data storage solutions.

In September, the growing strategic imperative for hardware vendors of an integrated services proposition underpinned Dell's €2.7 billion purchase of the IT services provider Perot Systems. Hard on its heels came Xerox's planned €4.4 billion acquisition of the business process outsourcing business Affiliated Computer Services (ACS) and the €1.4 billion acquisition by Silver Lake Partners of a 65% stake in the online communications business Skype Technologies.

These mould-breaking deals were followed in October by news of the €1.2 billion acquisition by Adobe Systems of the web-analytics company Omniture. In November, Hewlett Packard clearly announced its ambitions in Cisco's home territory in the network space, as it unveiled its €2.1 billion proposed acquisition of 3Com.

Another potentially transformative transaction is the long running saga of Oracle's proposed €5.6 billion acquisition of the network infrastructure company Sun Microsystems. Launched in April 2009 and combining enterprise software and computing systems, it has been delayed by an EU Commission competition inquiry.

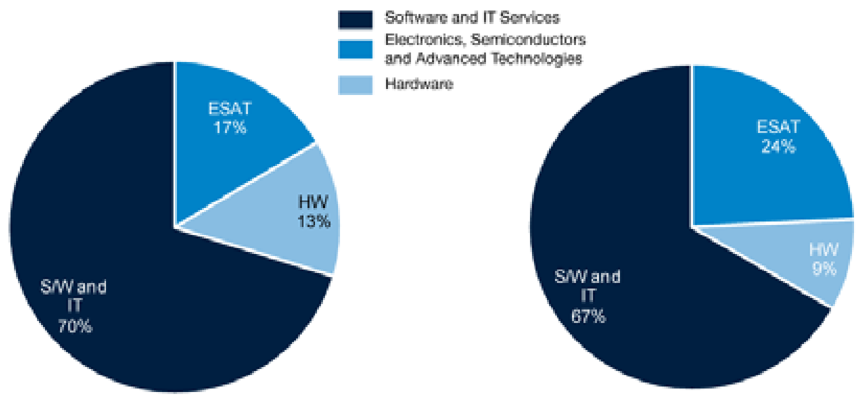
Bigger is better for SITS

The reshaping of the Software and IT services (SITS) landscape remains the dominant driving force for technology M&A, accounting for 70% (by value) and 67% (by volume)

The appetite among SITS companies for scale and global delivery capability over the last three years shows no signs of abating. The ability to drive tangible cost synergies, and the attractive cash profile of ongoing maintenance and support revenues, continue to make software deals a compelling financial proposition for many.

The question for 2010 will be whether it is more of the same, in a world where customers want more for less, or are there deals which will really drive top line organic growth as well as bottom line returns?

Global sub-sector split by value and volume



This chart covers completed global M&A transactions, involving stakes greater than 10%, where the deal value was disclosed and greater than €10 million

Source: Dealogic, M&A Global, Mergemarket

East follows West

As Asia catches up with the US, the margin between the most active bidding and target regions last year in terms of deal volume narrowed, with both the US and Asia accounting for 35% of global transaction activity.

In value terms, the US continues to dominate as the prime consolidating force accounting for 51% of bidder activity worldwide (2008 – 45%). Asia continued to step up the scale of its ambitions, with its acquisitive share of global deal values increasing significantly to 25% (up from just 13% in 2008).

Much of the relative rise of Asia was at the expense of Europe, where the leading protagonists took a more cautious approach to M&A. Europe's share of the market fell dramatically from 39% of global bid activity in 2008 to just 17% in 2009 by value.

We expect activity in Europe to pick up in 2010, as corporate confidence returns and weaker exchange rates make certain European markets look more attractively valued.

Domestic and international technology deals map

North America
86 domestic deals ↓
Disclosed value €16,603m ↓
International deals
Europe
19 deals ↓
Disclosed value €2,734m ↓
Asia
3 deals ↓
Disclosed value €73m ↓
Rest of the World
1 deal ↓
Disclosed value €113m ↓

Rest of the World
8 domestic deals ↑
Disclosed value €486m ↑
International deals
North America
4 deals ↓
Disclosed value €1,355m ↑
Europe
0 deals ↓
Disclosed value €0m ↓
Asia
1 deal →
Disclosed value €11m ↓

Europe
57 domestic deals ↓
Disclosed value €4,604m ↓
International deals
North America
10 deals ↓
Disclosed value €1,513m ↓
Asia
4 deals ↓
Disclosed value €165m ↓
Rest of the World
0 deals ↓
Disclosed value €0m ↓

Asia
88 domestic deals ↓
Disclosed value €8,054m ↓
International deals
North America
6 deals ↓
Disclosed value €122m ↓
Europe
6 deals ↓
Disclosed value €828m ↓
Rest of the World
4 deals ↑
Disclosed value €173m ↑

↓ reduction from previous year
↑ increase from previous year
→ same as previous year

This chart covers completed global M&A transactions, involving stakes greater than 10%, where the deal value was disclosed and greater than €10 million
Source: Dealogic, M&A Global, Mergermarket

Domestic deals dominate

Global deal values and volumes last year were driven largely by intra-regional transactions in the US and Asia.

Despite the favourable exchange rate for US to UK deals last year, US bidders secured relatively few UK targets, the largest being the €267 million acquisition of the social gaming company Playfish by Electronic Arts and the €140 million acquisition of the hardware distributor Abacus Group by Avnet.

We expect cross-Atlantic deals to make a come-back in 2010, as confidence and earnings visibility strengthen. Landmark US domestic technology deals included Dell's acquisition of Perot, Cisco's acquisition of Starent, EMC's takeover of Data Domain and Adobe's acquisition of Omniture.

Key Asian domestic transactions included Toshiba's €670 million acquisition of Flash Partners in Japan alongside, in India, Tech Mahindra's €441 million acquisition of a 51% stake in Satyam Computer Services.

Top 10 European Deals 2009

Date	Bid Value (€m)	Target Full Name	Nationality	Bidder Full Name	Nationality
Feb-09	1,915	NDS Group Plc (77%)	United Kingdom	Permira Advisers (London) Ltd	United Kingdom
Nov-09	1,417	Skype Technologies SA (70%)	Luxembourg	Silver Lake Partners LP; Canada Pension Plan Investment Board; Index Ventures; Andreesen Horowitz Fund	United States
Mar-09	600	Interwoven Inc	United States	Autonomy Plc	United Kingdom
Apr-09	450	Fujitsu Siemens Computers GmbH (50%)	Germany	Fujitsu Ltd	Japan
Oct-09	434	IDS Scheer AG (90%)	Germany	Software AG	Germany
Dec-09	285	LifeSize Communications Inc	United States	Logitech International SA	Switzerland
Nov-09	267	Playfish Ltd	United Kingdom	Electric Arts Nederland BV	Netherlands
Jul-09	246	Indra Sisternas SA (10%)	Spain	Corporation Financiera Alba SA	Spain
Nov-09	243	Infineon Technologies AG (Wireline Communications WLC) business)	Germany	Golden Gate Capital Corp	Germany
Mar-09	218	Wavecom SA	France	Sierra Wireless Inc	Canada

Source: Dealogic, M&A Global, Mergermarket

UK decline follows global trend

The decline in global deal volumes and values in the technology sector was mirrored in the UK with completed deals down by 62%.

The combined value of these deals fell by 52% to €3.3 billion from €6.8 billion the previous year. Nevertheless, average deal values remained relatively stable and exceeded 2008 in both the SITS and hardware segments.

While the recovery in UK technology M&A appears less pronounced than in the US where momentum is building strongly thanks to the mega-deals announced since September, confidence is starting to return.

Deal pipelines and activity levels in the UK are increasing, although extended transaction timetables remain a feature of the market.

Technology Sector Top 10 UK Deals (UK as a target) 2009

Date	Bid Value (€m)	Target Full Name	Nationality	Bidder Full Name	Nationality
Feb-09	1,915	NDS Group Plc (77%)	United Kingdom	Permira Advisers (London) Ltd	United Kingdom
Nov-09	267	Playfish Ltd	United Kingdom	Electronic Arts	United States
Jan-09	140	Abacus Group Plc	United Kingdom	Avnet Inc	United States
Aug-09	132	Exchange FS Ltd	United Kingdom	Lloyds Development Capital Ltd	United Kingdom
Apr-09	95	Eidos Plc	United Kingdom	Square Enix Holdings	Japan
Dec-09	84	Synetrix (Holdings) Ltd	United Kingdom	The Capita Group Plc	United Kingdom
Mar-09	81	Snell & Wilcox Ltd	United Kingdom	Pro-Bel Ltd	United Kingdom
Dec-09	71	SpinVox Ltd	United Kingdom	Nuance Communications Inc	United States
Nov-09	56	ScriptSwitch Ltd	United Kingdom	UnitedHealth Group Inc	United States
Jun-09	41	Carillion IT Services Ltd	United Kingdom	The Capita Group Plc	United Kingdom

Source: Dealogic, M&A Global, Mergermarket

Private equity still a player in the tech game (continues overleaf)

Bucking the trend, PE in the technology sector has remained very much a player, leading some €6.7 billion of transactions globally. This actually represents an increase on the €5.2 billion delivered in 2008, albeit from a transaction base down by over 20% in volume.

This resilience is perhaps surprising given that across all sectors PE investors have been frequently forced to step aside for strategic trade buyers for much of the last 18 months, with deteriorating confidence, difficult debt market conditions and portfolio preoccupations keeping many on the side lines.

The PE deals in the technology sector included three €1 billion-plus PE transactions, the most significant being Permira's Public To Private of NDS. Completed in February 2009, this deal was launched at the peak of the market in August 2008. Clearly the economic downturn has posed a challenge and NDS's desire to play a leading role in future consolidation in the industry will test Permira's restructuring and re-engineering skills to the full.

Technology Sector Top 10 PE Deals 2009

Date	Bid Value (€m)	Target Full Name	Nationality	Bidder Full Name	Nationality
Feb-09	1,915	NDS Group Plc (77%)	United Kingdom	Permira Advisers (London) Ltd	United Kingdom
Nov-09	1,417	Skype Technologies SA (70%)	Luxembourg	Silver Lake Partners LP; Canada Pension Plan Investment Board; Index Ventures; Andreessen Horowitz Fund	United States
Dec-09	1,112	TASC Inc	United States	General Atlantic LLC; Kohlberg Kravis Roberts & Co	United States
Oct-09	277	MSC Software Corp	United States	Symphony Technology Group LLC	United States
Jan-09	246	MYOB Ltd	Australia	Archer Capital; HarbourVest Partners LLC	Australia
Nov-09	243	Infineon Technologies AG (Wireline Communications (WLC) business)	Germany	Golden Gate Capital Corp	Germany
Nov-09	142	Broadleaf Co Ltd	Japan	Carlyle Group Inc; Existing Management	Japan
Oct-09	141	AVG Technologies NV (11%)	Czech Republic	TA Associates Inc	United States
Aug-09	132	Exchange FS Ltd	United Kingdom	Lloyds Development Capital Ltd	United Kingdom
Mar-09	109	Aladdin Knowledge Systems Ltd	Israel	Vector Capital	Israel

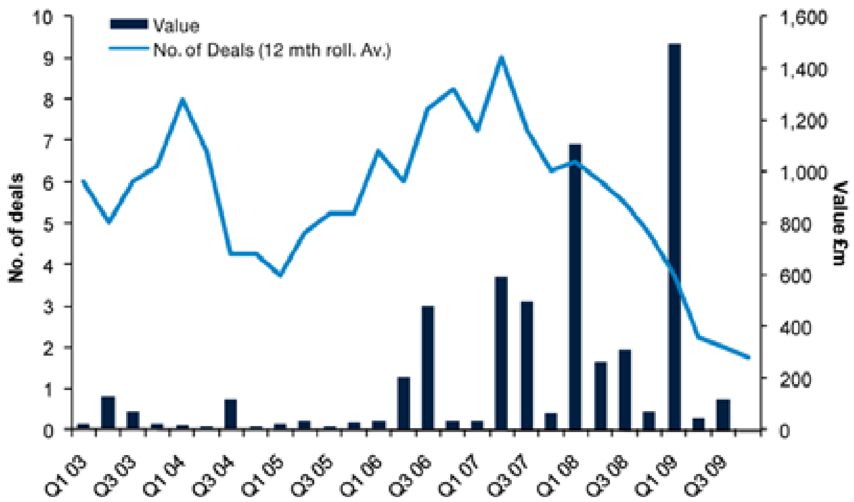
Source: Dealogic, M&A Global, Mergermarket

Private equity still a player in the tech game

In the UK the PE picture was more gloomy with (outside of the NDS transaction) only a handful of technology buyouts completed worth a combined €2.2 billion (including NDS), compared with 19 totalling €1.7 billion in 2008.

Alongside NDS, other PE-backed deals in the UK technology sector last year were the €132 million acquisition by Lloyds Development Capital (LDC) of a controlling stake in the financial software company Exchange FS; LDC and Advent Ventures completing the €81 million merger of Snell & Wilcox and Pro-Bel, two providers of broadcasting technology; ECI Partners backing a €37 million Public To Private of the healthcare software business Ascribe; HgCapital supporting a buyout of Epyx, and Close Growth Capital backing management to acquire the UK IT services businesses of Sword SA to form Amor Group.

UK based private equity deals in software and IT services



This chart covers completed UK private equity transactions, involving stakes greater than 10%, where the deal value was disclosed and greater than €10 million
Source: Thomson SDC
Note: Q109 includes the Permira acquisition of stake in NDS group for £1,465m

On the exit front, most PE houses were in hold mode waiting for markets to stabilise, buyers to return and trading conditions to improve. There are signs the freeze is starting to thaw as December 2009 saw the sale of Synetrix, the provider of managed ICT solutions to education and the public sector, by Apax Partners to Capita for €84m, and the sale of SpinVox, the troubled voice to text provider, to Nuance for €71m.

PE exits are likely to return to the agenda, particularly in the second half of 2010, as PE houses look to generate returns for their investing partners and raise further funds. PE funds will be keeping a close eye on the window of IPO opportunity as an alternative to the refinancing options which were the default option pre credit crunch.

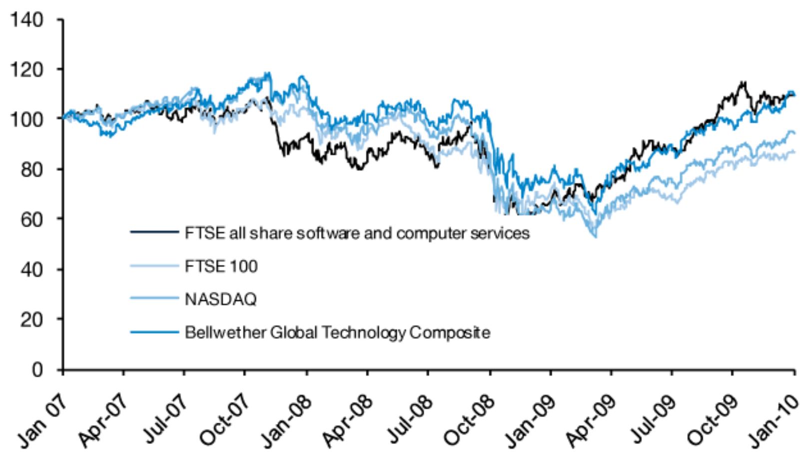
Is there a danger of overheating?

In the public markets there was a significant divergence between the performance of the FTSE100 and the UK FTSE Software and Computer Services (SCS) Index last year.

While the FTSE100 ended the year up by 22%, the FTSE SCS Index raced ahead by 64%. This differential has raised the spectre of the sector overheating. Certainly there hasn't been such a performance gap between these indices since the beginning of 2000 and the dot com bubble.

It may be that the sector is just ahead of the recovery curve, having proved more resilient in the face of the recession and learnt some harsh lessons with a renewed sense of realism.

Valuation trends



Source: Datastream; Note: Bellwether index comprises Microsoft, Oracle, SAP, HP and IBM

The universe of publicly-quoted technology stocks has been steadily shrinking in the UK over the last two years. Just 199 technology companies (including 49 techMARK stocks) capitalised at a total of €92 billion were on AiM and the main London stock market at 30 November 2009. This compares with 268 (including 64 techMARK stocks) worth an aggregate €121 billion at 30 November 2007.

Public To Privates have played a part in the reduction, as have UK public takeovers, which have been relatively few in 2009. With only four UK technology companies – Autonomy, Capita, Sage and Serco – included in the FTSE100, greater scale is required if UK companies are to compete successfully on a global basis. The €0.6 billion acquisition of Interwoven in the US by Autonomy showed the global ambition is still there, but the fact that no European acquirers made the Top 10 global deal list in 2009 (compared to 5 in 2008) tells its own story.

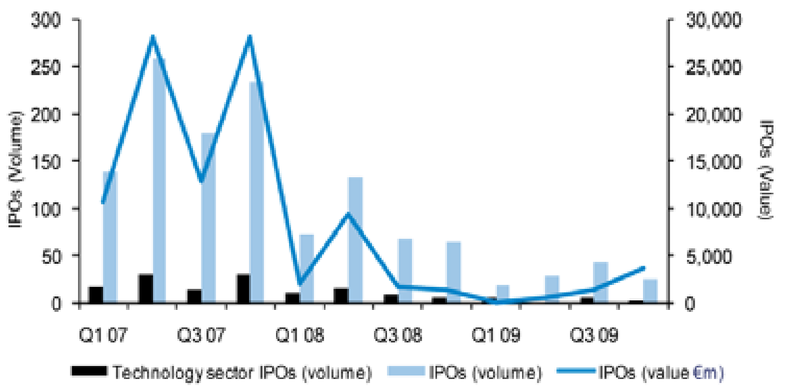
IPOs line-up for lift-off?

Will technology stocks be at the front of the queue when the IPO window opens?

With the strengthening global economy, the stock market rally, a line of long over-due PE exits and corporate spin-offs and demergers returning to vogue, there is much expectation being hyped on the strength of the IPO pipeline.

However, technology stocks are unlikely to be at the vanguard of any IPO revival. Many candidates will also be pursuing trade sale alternatives in parallel with their IPO plans with a good proportion – particularly the mid-market players – likely to find that, ultimately, their strategic value is better realised via a trade or financial sale.

European IPO activity by volume and value - all sectors



Source: PwC IPO Watch Europe report

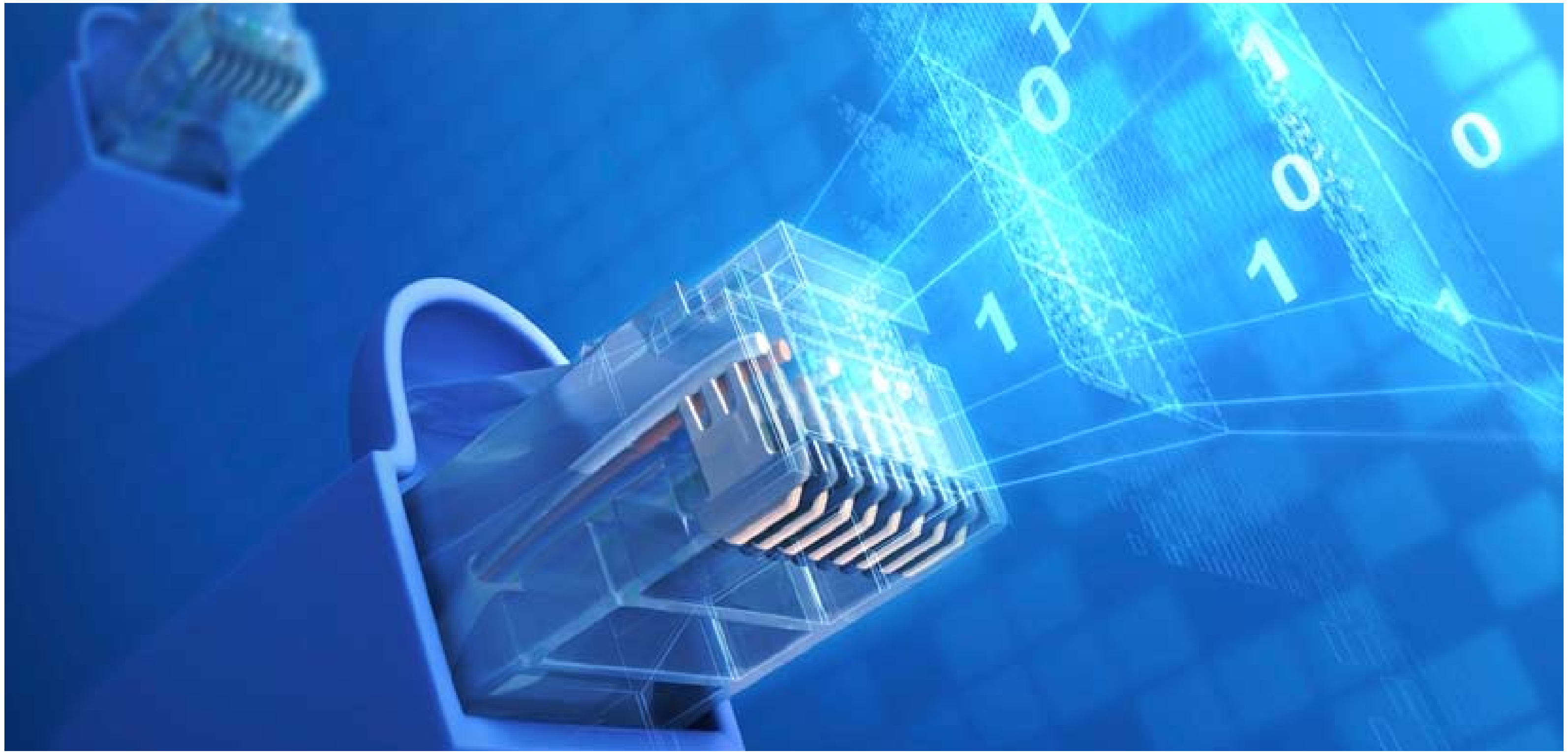
2010 - M&A ready to emerge from hibernation

On reflection, 2009 saw a low ebb for M&A. However, the right conditions appear to be in place to create an inflexion point for the deal cycle.

Increased positive sentiment, along with a gradual improvement in liquidity conditions, should fuel M&A over the course of the forthcoming year. Vendors are gradually realising that valuations are unlikely to return to the lofty levels seen at the height of the M&A cycle in 2007.

Private equity and strategic buyers have become increasingly aware of this and are waiting for the right opportunity to strike as sellers fall in line with the new valuation paradigm.

However, wider economic uncertainty remains and the challenge for policymakers is to withdraw unprecedented levels of fiscal and monetary support to reduce public borrowing levels and head off inflationary pressures, without putting the recovery at risk.



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