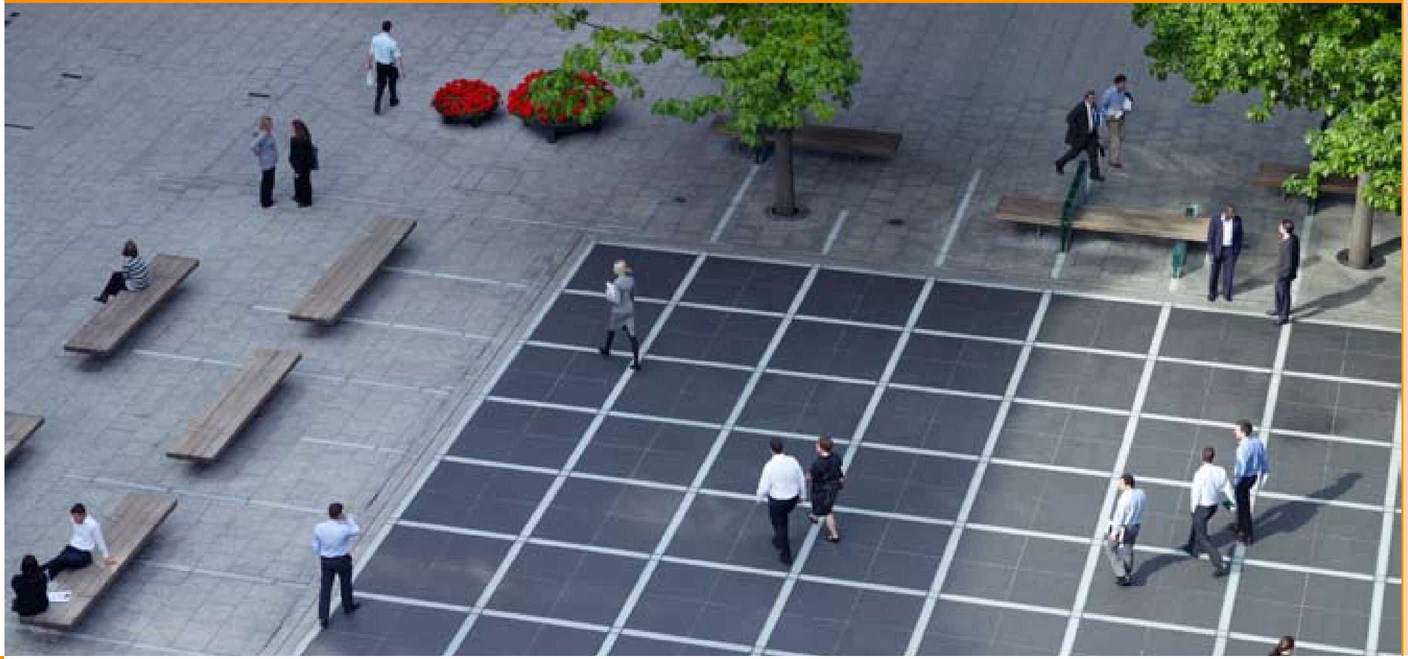
Technology M&A Insights

What's generating deals in the Technology Sector? 2011



In this publication:

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Contents

Welcome

The alignment of cash-rich trade buyers, private equity sponsors with funds to invest and continued improvement in financing liquidity is creating a window of opportunity for M&A activity.

Be prepared

Welcome to the 2011 edition of Technology M&A Insights. This annual report by PwC[1] forecasts the outlook for M&A activity in the global technology sector in 2011, building on our analysis of the trends emerging from deals completed in 2010. We identify the underlying themes driving deal activity, look at which players are active in the acquisitions market, and analyse the market segments they are focusing their attention on.

The M&A market is starting to recover with a significant rise in the value of global technology deals completed in 2010 – €76bn, up from €37bn in 2009. There was also a noteable rise in the volume of completed deals, up 32% from the lows of 2009 – more high quality assets are now being brought to market as sellers seek to take advantage of the presence of cash-rich corporates with a renewed appetite for mega-deals; aggressive private equity buyers and improving capital markets.

There are a number of key Hot Spots where we expect to see extensive deal activity in 2011. Financial regulation is a strong driver for deals in the FinTech sector, as the regulatory push coincides with a recovering IT investment spend in the financial sector and a greater focus on transparency and risk management. The rapid evolution and adoption of Cloud Services that looks set to provide strong deal flow as the larger technology players battle for position and are more proactive in broadening their product offerings. The stars are aligning as never before in the mobile data world. This sector has historically been highly fragmented but the larger players have started acquiring in all areas of mobile data – advertising, payments, messaging, gaming and content – as the growth of the smart phone market continues apace.

We are already seeing a change in deal dynamics as the appetite for mega deals returns to the market. The number of pre-emptive deals is on the rise as cash rich buyers look more aggressively at deal origination rather than relying on competing in traditional auction processes – growth is firmly back on the corporate M&A agenda. Private equity players have returned to the market as they are increasingly under pressure to deploy capital. The willingness of banks to provide debt financing for quality assets is helping PE's return to the market, both as acquirers and as providers of growth capital.

US acquirors regained their dominant position in terms of global transaction volume, accounting for 39% of global deals in 2010. They are increasingly looking to acquire in Europe in order to broaden their client base and provide a truly global offering.

The Technology Deals team at PwC has also had an active year, advising on some of the more high-profile deals of 2010. In the UK, headline deals included the acquisition of Sophis by Misys, the sale of SunGard Public Sector to Capita, the acquisition of Sophos by Apax Partners and the sale of Xafinity by Duke Street Capital to Advent International.

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 us, or your PwC relationship team.

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[1] "PwC" refers to the network of member firms of PricewaterhouseCoopers International Limited (PwCIL), or, as the context requires, individual member firms of the PwC network.

Hot Spots for Technology Sector Deals

Whilst a general upturn in M&A activity is likely in 2011, there will be some key hot spots for deals driven by the seismic shifts affecting certain segments of the market.

Financial Technology (FinTech)

A significant increase in financial regulation in the wake of the financial crisis provides a strong driver for deal activity in the FinTech sector. A greater focus on transparency and risk management is contributing to a large increase in the volume of financial data being processed, helping fuel demand for integrated software solutions. Regulatory push is also coinciding with a recovering IT investment spend in financial services as the banking system returns to profitability – the banks have money again and are prepared to spend on IT. While some of the larger banks will design and develop their own IT platforms, many are looking to software providers to simplify this process.

For the software providers, there is an opportunity to capture synergies in a fragmented market that is ripe for consolidation, managing the cost base downwards and focusing on efficiencies. There is also an opportunity to evolve product offerings from single point solutions to more integrated systems; and in many cases it is faster and more cost effective to achieve this through acquisition rather than organic growth.

The acquisition in November by financial services software provider Misys of capital markets software vendor Sophis for €435m is a good example of this trend. The acquisition was partly financed by the sale of Misys' stake in Allscripts Healthcare Solutions, its healthcare arm. Sophis' buy-side software solutions are highly complementary to Misys' existing sell-side treasury and capital markets solutions and Misys expects to generate significant revenue synergies.

Key Messages

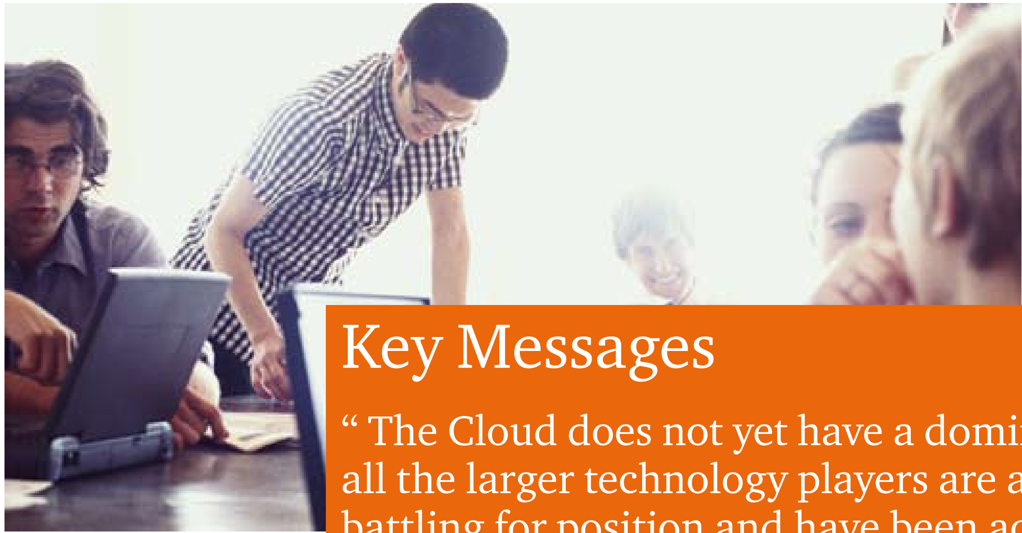
"There is an opportunity to capture synergies in a fragmented market that is ripe for consolidation, managing the cost base downwards and focusing on efficiencies"

With the prospects of FinTech companies improving, private equity groups are also being attracted by the growth potential on offer. In June, Acturis, which provides software as a service to insurance brokers, sold a minority stake to Summit Partners for an undisclosed sum. Acturis was seeking growth capital to fund an expansion of its market share in the UK and a planned roll out of its services into the highly fragmented European broker market.

The UK is widely perceived as a centre of excellence for FinTech, because of the strength of the financial services sector and the depth of service provision into it. Consequently, FinTech is a very hot sector for overseas buyers, especially Indian players, who are looking to buy into UK FinTech as a route into developing relationships with the global giants of the financial services sector.

Hot Spots for Technology Sector Deals

Seeing the Cloud through the fog



Key Messages

"The Cloud does not yet have a dominant player but all the larger technology players are aggressively battling for position and have been active in broadening their product offerings to build a full range of Cloud services."

Despite being a much over used buzzword, the "Cloud" space and related technologies has seen some genuine momentum in 2010, driving M&A activity which we expect to accelerate in 2011.

The rapid development of virtualization and security technologies has underpinned the Cloud proposition. The prospect of significant cost savings and ability to handle large data volumes, is making Corporates take notice and become more open to exploring the creation of a private Cloud or of outsourcing to public Cloud providers; paying a third party to host their data and applications and take responsibility for its security. While initial interest maybe confined to the larger companies, the SME sector can also achieve significant benefits particularly from the public Cloud and as such, have become a focal point for vendor sales efforts.

The Cloud does not yet have a dominant player, but all the larger technology players are aggressively battling for position and have been active in broadening their product offerings to build a full range of Cloud services. In many instances this has meant building scale and capabilities through acquisition.

The major M&A activity to date has focused on infrastructure and virtualization technologies which underpin the Cloud's development.

In May, telecommunications provider Cincinnati Bell expanded its data centre operations with the acquisition of CyrusOne from private equity group ABRY Partners in a cash transaction valued at approximately $525 million.

In August, HP acquired 3PAR for $2.4bn after a hotly contested bidding war with Dell (see Deal Dynamics section for further analysis). Dell responded with the purchase of data storage company Compellent Technologies, a $960m deal announced in mid-December.

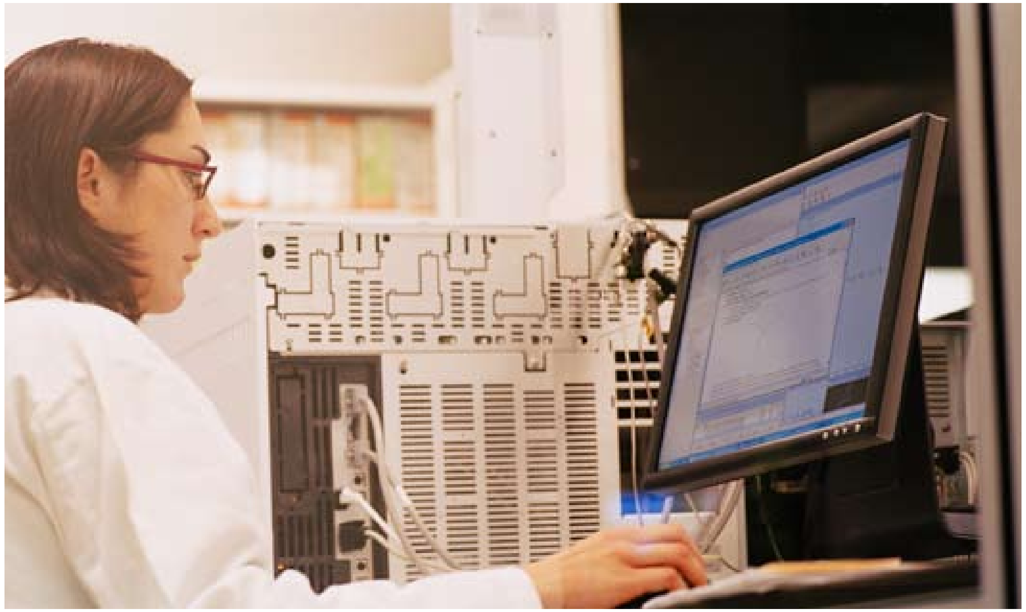
The most active acquirer in 2010 has been CA Technologies who have made 6 acquisitions in the space of 14 months totalling $1bn. A Cloud rationale was also a deal driver in Oracle's acquisition of Sun Microsystems, which finally gained EU regulatory approval at the start of 2010. "Oracle plans to engineer and deliver an integrated system—applications to disk—where all the pieces fit and work together so customers do not have to do it themselves. Customers benefit as their system integration costs go down while system performance, reliability and security go up." (Sun Microsystems press release).

Private equity is also showing interest in the infrastructure space attracted by the buy-and-build opportunities in sub-sectors such as the fragmented data centre industry. Low churn and long-term contracts add to the appeal for private equity buyers. The downside of significant capex requirements, however, can deter some private equity players.

Hot Spots for Technology Sector Deals

In September, Montagu Private Equity acquired web services company Host Europe Group from Oakley Capital for €265m. Comprised of two businesses, Webfusion and Host Europe, the company has 730,000 clients, and has a strong presence in the UK and Germany.

Deal multiples in the Cloud space are high. Demand for data centres currently outstrips supply and available capacity is being snapped up at high values. The Cyrus One and Host Europe transactions both attracted double-digit EBITDA multiples. These multiples seem quite moderate, however, when compared with the prices paid by HP and Dell in the data storage space. According to analysts' reports Dell's offer for Compellent values the company at around five times sales or almost 50 times forecast Ebitda, while HP offered multiples of over eight times sales for 3PAR.



In addition to infrastructure and data storage and management we expect data security to be a strong growth area, which will also drive M&A activity in 2011. Security is also likely to be one factor behind the expected eventual dominance of the Cloud market by the larger players. Corporates are more likely to entrust the security of their data to a large established player.

The Cloud demands a different business model with a move from a license sales and maintenance revenue approach to a usage basis. The implications for the smaller players of the Cloud trend are one of both significant opportunity but also risk. The development opens up the market to innovative new players that can grow rapidly. Existing businesses may find that their business models are inflexible or they do not have the scale to compete with the large vendors. However a business with a high quality and scalable offering may find itself highly attractive to the large players. 2011 will be a very important year for setting the stage for value creation and realisation for mid market providers serving this space.

Hot Spots for Technology Sector Deals

Mobile Data – getting smarter

Forecast as a growth area for many years, the stars are aligned as never before in the mobile data world. The rapid launch of new 'Smartphone' devices from all vendors has not only meant competition to the ubiquitous Apple but also that consumers are receiving a genuine internet experience. The success of the Smartphone means they now represent between 70-80% of new handsets sales in the UK.

All the key 'applications' in mobile data are attracting attention; advertising, payments, messaging, gaming and content. Historically these sectors were highly fragmented but the larger players, convinced now that wireless is a key area, have started acquiring.

Key Messages

"All the key applications in mobile data are attracting attention. Historically these sectors were highly fragmented but the larger players, convinced now that wireless is a key area, have started acquiring".

At the turn of the year we saw the battle between Apple and Google in the mobile advertising space – Google acquired Admob for $750m and Apple responded with the acquisition of Quattro Wireless for $275m. The two giants have also now started to move into mobile payments, an area where we expect to see rapid growth. Google has acquired Zetaware while both companies are rumored to be looking at payments start up Boku.

The applications space is also hot as businesses seek to move from the maturing traditional premium SMS model to one that takes advantage of the reach and functionality of the new smartphones. Again the larger players have swooped to pick up attractive properties – RIM acquired the white label content provider Cellmania for an undisclosed amount, while Ebay acquired mobile app developer Critical Path Software to accelerate its position in smartphone applications. Wireless gaming is another sub sector that is ripe for a thrust from the main games developers. The wireless gaming market is currently highly fragmented but we expect this to change as some of the larger players have already started to acquire smaller companies to expand their offering – EA Games has made a move, recently acquiring the Angry Birds developer Chillingo, while Disney acquired another games publisher Tapulous in July.

We expect a high degree of M&A across the wireless data space as smaller players consolidate to achieve competitive scale and the larger players engage in a land grab to develop their propositions to exploit the opening of the new frontier. A less obvious development but one where we see exciting wireless developments, is in the automotive sector. The car is one of the last bastions of 'white space' in the connected mobile environment, but the Connected Car, with access to the Internet through a SIM card, is becoming a reality.

Large manufacturers such as BMW, for example, are launching models with connectivity capability. This development opens up a large number of technology applications – from enhanced in-car entertainment and more sophisticated navigation information through to interactive traffic management. With traffic volumes continuing to grow, yet investment in road infrastructure constrained by familiar budgetary restrictions, there is a growing need for intelligent traffic management ("ITS") systems, with the ability to proactively direct cars away from congested areas. Pilot ITS projects of these 'Smart City' schemes are currently live in London and in a selection of major German cities.

The strategic vision of the Connected Car and the Smart City is in its infancy and M&A to date has tended to focus on infrastructure providers. In November, Kapsch Trafficom , a large supplier of electronic toll equipment, snapped up rival MARK IV for €53m, which produces communication that enable electronic toll collection and automated weigh station bypass. However, we are seeing a shift with M&A increasingly focussing on leading providers offering a richer driver experience in relation to off-board navigation and multi-modal travel, as well as proactively managing traffic within the Smart City rather than merely charging for access to the transport infrastructure.

Hot Spots for Technology Sector Deals

Key Messages

"There is an opportunity for technology to transform the delivery of government services over the medium term"

UK public sector – opportunities in the cuts

The impact of central and local government spending cuts will make 2011 a very tough operating environment for technology companies providing services to the UK public sector. But we believe that there is an opportunity for technology to transform the delivery of government services over the medium term. To save costs on the scale the government requires will necessitate a different approach to outsourcing and the provision of ICT.

The public sector must slash its expenditure, but does not know how to achieve those cuts in the most efficient manner. There is an opportunity for technology companies to be proactive in approaching government with specific solutions that deliver real cost savings.

We expect to see increased collaboration between government departments and local authorities, which will drive increased demand for master data management technology. Currently, different government departments have individual contracts with IT providers, with a focus on tracking departmental spend. Government will increasingly shift towards a more holistic view of what government spends on individuals across all departments. ICT is also one of the easiest areas of government services to outsource and we expect to see increased activity in this space, particularly in local government.

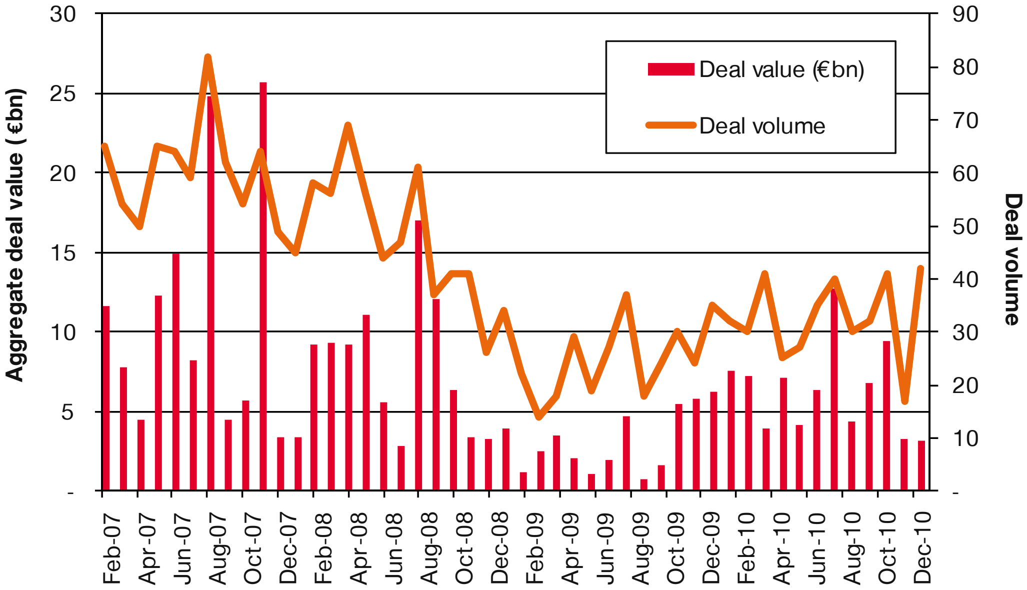
For companies with established market positions and the ability to look beyond the very short-term operating environment there will be strategic buying opportunities in 2011. Capita recently acquired SunGard Public Sector Holdings Ltd for £86m. SunGard is a supplier of ICT, radio network services and communication systems to the emergency services and to central and local government. The acquisition opens up new market opportunities for Capita, particularly in the area of ICT solutions and outsourced services to fire, police and ambulance authorities – complementing Capita's existing broad portfolio of services for the public sector.

International operators, too, recognise the UK public sector as an opportunity, and for those without an existing significant local presence acquisitions are the only method of entry. International players are currently looking aggressively at the UK to make acquisitions to take advantage of opportunities presented by the comprehensive spending review.

Changing deal dynamics

Compared with the cyclical low in 2009, technology sector deal volumes recovered over the course of 2010, while deal values rebounded more strongly. 393 deals completed in 2010, (up 32% from 2009) with a total value of €75.7bn – more than double the value completed in 2009 (€36.8bn). The recovery in M&A activity remains relatively cautious with both deal volumes and values still some way off the highs of 2007 and 2008.

Global 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

Deal dynamics, however, are changing, with several factors aligning to create a window of opportunity for increased M&A activity in the first half of 2011. More high quality assets are now being brought to the market as sellers seek to take advantage of the presence of cash-rich corporates with a renewed appetite for mega deals; aggressive private equity buyers are returning; and improving capital markets provide a supportive influence.

Return of the mega deal

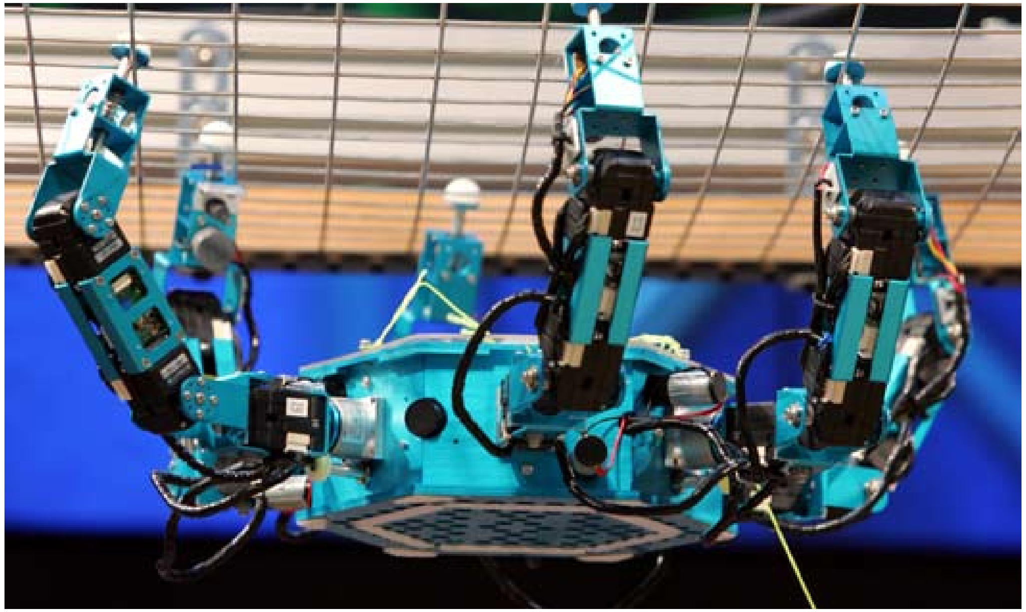
During the downturn, corporates addressed their cost bases, improved their operational efficiency and are now looking to deploy the cash accumulating on their balance sheets to buy growth in an environment where organic growth prospects are more challenging. As a result, the number of mega deals (18 deals over €1bn in value) more than doubled in 2010 compared to 2009 figures.

Key Messages

"The increased confidence and activity by the large trade players in the global technology market will filter down into deal activity within the UK and European mid-market"

Changing deal dynamics

The Top 10 deals of 2010 illustrate the renewed appetite of the technology sector's largest players to complete mega-deals, with the likes of Oracle, SAP, Hewlett Packard ("HP") and NTT all completing multi-billion Euro transactions over the course of the year.



Technology Sector Top 10 Global Deals 2010

Completion Date	Bid Value (Euro m)	Target Full Name	Target Nationality	Bidder Full Name	Bidder Nationality
January 2010	5,841	Sun Microsystems Inc	United States	Oracle Corp	United States
July 2010	5,595	Sybase Inc	United States	SAP AG	Germany
February 2010	5,536	Affiliated Computer Services Inc	United States	Xerox Corp	United States
April 2010	2,798	Renesas Technology Corp	Japan	NEC Electronics Corp	Japan
October 2010	2,457	Dimension Data Holdings plc	South Africa	Nippon Telegraph & Telephone Corp – "NTT"	Japan
April 2010	2,127	3Com Corp	United States	Hewlett-Packard	United States
September 2010	1,837	3PAR Inc	United States	Hewlett-Packard	United States
October 2010	1,687	Intergraph Corp	United States	Hexagon AB	Sweden
May 2010	1,516	SkillSoft plc	Ireland	Berkshire Partners LLC; Advent International Corp; Bain Capital Partners LLC	United States
November 2010	1,466	Netezza Corp	United States	IBM	United States

Source: Dealogic and mergermarket

Changing deal dynamics

HP is a particularly good illustration of the trend, announcing four deals of significant size in 2010 – two in the Top 10 – as it re-positions itself away from lower-growth commodity computer and printer sales by expanding into higher margin software and services. In April, HP paid $2.7bn for 3Com, the data and voice networking services group and in July bought Palm, the global provider of handheld computing devices for $1.2bn. In September it added Arcsight, a security and compliance management company for $1.5bn, and fought off competition from Dell in a fierce bidding war for 3PAR, the storage technology company. HP eventually paid $33 per share, equivalent to an enterprise value of $2.35bn, which was more than three times 3PAR's closing stock price the day before Dell's initial bid was made public.

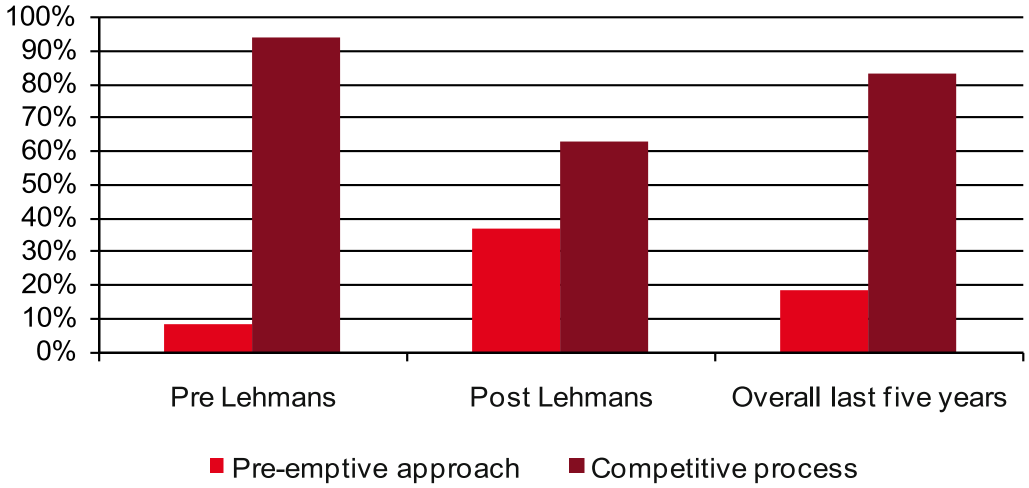
This flurry of acquisition activity is significant for several reasons. Firstly, it clearly shows that appetite has returned for €1bn plus mega deals in the global technology market, which will have a trickle-down effect. We expect the increased confidence and activity by the large trade players in the global technology market will filter down into deal activity within the UK and European mid-market in the first half of 2011.

Secondly, the frenzied bidding war for 3PAR, as well as Dell's recent announcement in December of the acquisition of Compellent Technologies illustrates the importance technology companies are attaching to the Cloud computing phenomenon, which we have analysed more fully in the Hot Spots section of this report. High quality assets in high growth segments are seeing the selective return of aggressively competed M&A auction processes.

Pre-emptive deals on the rise, for the right assets

Although competitive processes are still at the forefront of deal activity, we have seen a significant rise in the number of pre-emptive approaches unlocking deals in the period since the height of the global economic crisis. While there have still been a handful of high profile, tightly run auctions, the way companies are pursuing acquisition opportunities is changing, with cash rich buyers looking more aggressively at deal origination, rather than relying on competing in traditional auction processes. Growth is firmly back on the corporate M&A agenda.

Pre-emptive versus competitive process



Source: PwC analysis

Key Messages

More than a third of deals are being engineered through pre-emptive approaches. How are you positioning yourself to differentiate your proposition and secure the key strategic assets?

Changing deal dynamics

Part of this trend may reflect the specific market conditions since Lehman Brothers' demise, with low transaction volumes, constrained capital markets and a large gap between buyer and vendor expectations. As market conditions continue to normalise the trend towards pre-emptive deals may slow, but there will always be buyers who will choose not to participate in auctions unless there is no alternative. Timing is key and some strategic trade buyers may value synergies more fully if they have the opportunity to acquire assets at the point of the cycle that is right for them.

Private equity bounces back

The renewed appetite of financial buyers lends further support to the prospects for an increase in M&A activity in the next six months. Private equity buyers under pressure to deploy capital are active in the technology sector, both as acquirers and providers of growth capital. The combined value of all PE deals in the sector in 2010 was €10.7bn, up almost 60%. In May, SSI Investments Ltd, a company formed by Berkshire Partners LLC, Advent International Corporation and Bain Capital Partners LLC, acquired SkillSoft, the US-listed Ireland based Software as a Service provider for €1.5bn.

Financial buyers also provide an alternative source of capital to the continued vagaries of the public equity market, as demonstrated by Sophos, a UK anti-virus software company focused on the business market, which had planned a US IPO for 2010, but elected instead to sell a majority stake to private equity group Apax Partners in a deal which valued the company at $830m. Sophos had previously pulled a planned London IPO at the end of 2007.

Key Messages

" More high quality assets are now being brought to market as sellers seek to take advantage of the presence of cash-rich corporates with a renewed appetite for mega-deals; aggressive private equity buyers and improving capital markets."

Carve outs on the block

Large corporate vendors, meanwhile, faced with an improving balance of trade and private equity interest and a narrowing of the gap between buyers' and sellers' value expectations as trading conditions have improved, are starting to carve out assets that have been on their non-core lists for some time. In December, Siemens announced the sale of Siemens IT Solutions and Services to Atos Origin for €850m, which will create a new company with expected revenues of €9bn-€10bn. Accompanying the sale, the two companies have agreed one of the world's largest outsourcing contracts, signing a seven-year contract worth €5.5bn under which Atos will provide Managed Services and Systems Integration to Siemens.

Banks regaining their appetite

The final factor that has helped create some deal momentum is the improved environment in the capital markets. This is reflected both in the willingness of banks to provide debt financing for quality opportunities and in the appetite of equity investors for high growth opportunities in an overall low growth environment.

Debt financing is available for the 'right' kind of technology businesses – those which have high levels of contracted and recurring revenues, good visibility on forward order books, strong defensible intellectual property positions and a blue chip customer base. Banks are becoming more selective about the market segments they wish to back and who they expect the long-term winners in those markets to be. They are building relationships over time with a view to capturing a larger share of banking income streams by providing ancillary services rather than single lines of credit.

Providers of equity capital – either public market shareholders or private equity capital providers – take a longer-term view of the technology sector's value creation prospects. The IT market in general terms is now a mature market that is likely to track, rather than significantly outperform, growth in GDP, but there is a huge variation in growth prospects in different segments of the market. While equity appetite for perceived high growth segments pushes up valuations, it also helps ensure that transactions attract the necessary funding support.

Changing deal dynamics

The stars are aligning

The near-term prospects for improved M&A activity look good, and the alignment of positive factors creates a window of opportunity. But that window will not remain open indefinitely – the balance of probability more than six months ahead suggests that downside risks predominate. Capital markets are at risk from the continued rumblings of sovereign debt concerns, while banks' appetite for new lending may be impacted by the need to start refinancing the heavily publicised "maturity wall" of corporate debt facilities that expire in 2012-14. Improved corporate trading performance, meanwhile, may be adversely affected by downward pressure on economic growth from governments' efforts to rein in their budget deficits.

Now is certainly a good time to realise value as quality businesses with a strategic position and scale will be able to attract strong prices. Smaller infill deals remain popular, but average deal values and pricing metrics are rising – the average monthly deal size was €197m in 2010, up 61% from €122m in 2009. We expect that trend to continue in the first half of 2011 as part of the trickle-down effect from mega deals, in what remains a risky economicy climate.

Potential vendors need to use this window of opportunity to position themselves to be more attractive to buyers. The key to giving buyers comfort is educating decision makers in really understanding the dynamics of the business, its growth story and why the business may be selling now.

From a buyer's perspective more quality assets are coming to the market but getting deals across the line still remains challenging. Due diligence has become a more onerous process with acquirers looking to probe beneath the financial headlines. Buyers need to trust the numbers, the company's accounting policies and its management teams – they must "lift the lid on the financials". Business sponsors need to convince their Boards and Shareholders that it is the right deal on the right terms in a risky economic climate.

The return of Private Equity

The heavily leveraged private equity business model of the credit boom years came to grief when the supply of cheap debt, which supported its highly financially engineered capital structures, evaporated in the wake of the sub-prime crisis. Without access to bank financing and facing withdrawals of capital by investors, private equity's ability to complete new deals was severely reduced.

However, private equity is definitely back. With the gradual return of bank appetite for acquisition finance, debt leverage multiples in buyout transactions are creeping higher, although they remain well below the 2006-07 peak. Partly out of necessity, private equity is writing bigger equity cheques, is accepting lower returns and has reverted to an earlier version of its business model. The focus is no longer on debt maximization and financial engineering but on the quality of management teams and the potential for value creation through operational improvements. Seeking out target companies with the potential for fast growth – both organic and through acquisitions – is of vital importance and, unsurprisingly, the technology sector is a key area of investment opportunity.

Private equity is increasingly active on both sides of the technology market. The reduced deal volume of the last couple of years has increased the pressure on funds needing to exit from current portfolio assets within their investment term. On the buy side, pent up demand from funds with committed capital to invest and signs of improvement in the fundraising market are underpinning a more aggressive presence from private equity. Improving financing liquidity, meanwhile, is allowing private equity to complete larger deals.

Private equity deal volumes and values increased in the technology sector over the course of 2010 and we expect financial sponsors to continue to be a deal driver in 2011. The total value of all PE deals in 2010 was €10.7bn, up almost 60% from last year.

Key Messages

"Seeking out target companies with the potential for fast growth is of vital importance to private equity and, unsurprisingly, the technology sector is a key area of investment opportunity".

The return of Private Equity

Financial sponsors are actively involved in a wide range of transaction types, as illustrated by the 2010 deal flow involving UK-based companies.

1

Trade infill deals:

In September, Palamon Capital Partners, a European mid-market private equity group, sold UK-headquartered OmniBus Systems to Canada's Miranda Technologies for €36m in cash. OmniBus is a developer of software systems for television broadcasters and video content distributors over mobile and Internet platforms. Palamon acquired OmniBus from the administrators of its former German listed parent and the sale realises a profit for Palamon at a time when the broadcast sector is coming out of a downturn caused by the recent global recession.

2

Buy and build platforms:

In September, Montagu Private Equity acquired web services company Host Europe Group from Oakley Capital for €265m. Comprised of two businesses, Webfusion and Host Europe, the company has 730,000 clients, and has a strong presence in the Cloud computing sectors of the UK and Germany. The two businesses will now be merged into a single platform with a view to growth through M&A going forward.

In November, Accel KKR backed Kana Software, a provider of software solutions for customer service experience management acquired Lagan Technologies, a provider of government to citizen technology, from venture capital group DFJ Esprit for an undisclosed sum. The transaction will complement Kana's capabilities in the communications, financial services, healthcare, retail and technology sectors.

3

Secondary (or tertiary) Buy Outs:

Advent International acquired Xafinity in January, an employee benefits and pension specialist from Duke Street Capital for €317m. Xafinity has been combined with Advent's existing investment in share registration business Equiniti to form the Equiniti Group – a specialist provider of BPO solutions.

In September, KKR acquired Visma AS, a Norwegian accounting and payroll software provider, from HgCapital for €1.4bn. KKR's acquisition, its first in Norway, brings to twelve the number of technology companies in its portfolio.

The return of Private Equity

4

Selective return of Public to Private activity:

In February, Inflexion Private Equity, the mid-market private equity investor, completed the take-private acquisition of AIM-listed FDM Group, for an enterprise value of £28.4m. FDM specialises in the provision of IT solutions to large blue-chip organisations including HSBC, The AA and BSkyB.

In June, US private equity firm Battery Ventures took AIM-listed Vero software private. Battery paid £7.2m to acquire Vero, which is a developer of CAD / CAM / CAE software for the mould & die industry.

Also in June, US private equity group Vector Capital bought UK-listed vehicle tracking company Trafficmaster for £73m. Vector Capital paid Trafficmaster shareholders 47p a share, a 40% premium to the average price over the three months before the announcement of the first approach on April 27.

5

PE filling the IPO gap:

In May, Sophos, A UK anti-virus software company focused on the business market, which had planned a US IPO for 2010, sold a majority stake to private equity group Apax Partners in a deal which values the company at $830m. Sophos had previously pulled a planned London IPO at the end of 2007.

6

Trade carve outs:

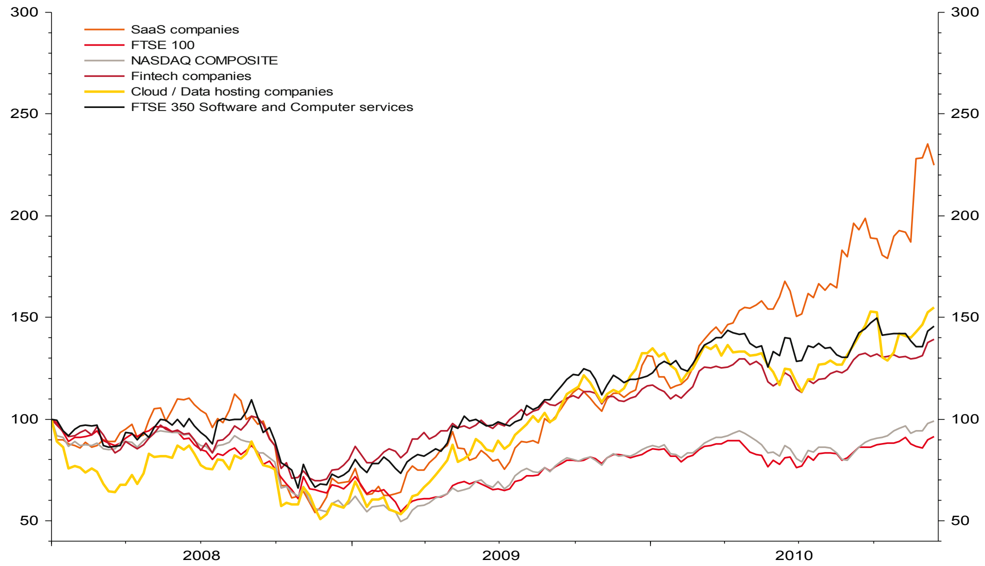
In March, HgCapital, the European private equity group, announced the acquisition of UK-headquartered StepStone Solutions, the wholly owned talent management subsidiary of Germany-based publishing and media group Axel Springer, for €110m. StepStone Solutions is one of the biggest European SaaS companies. Over 1,400 organisations use StepStone's Talent Management Solutions to recruit, retain and develop talent. Axel Springer retained ownership of the online division of StepStone.

Tech Stocks Outstrip the market

Proving their resilience once again, technology stocks significantly outperformed the FTSE 100 and NASDAQ Composite indices on the public markets in 2010. The UK FTSE Software and Computer Services (SCS) Index rose 25.1% over 2010, whilst the FTSE 100 saw a rise of just over 10%.

Looking at a further breakdown within the technology sector reveals a similar trend. FinTech companies rose by 24% in 2010, while Cloud companies saw a rise of 20%. SaaS companies were the stock market stars in 2010 delivering a stellar rise of 78%.

Valuation trends



Source: Thomson Reuters, Datastream

In 2011 we expect that the stock of UK-listed technology companies will decrease further as more listed businesses will be acquired than there will be new listings. The number of UK-listed technology stocks has been steadily dwindling over the last few years. Just 185 technology companies (including 37 techMARK stocks) were capitalized at a total of £105.1bn on AiM and the main London stock exchange at 30 November 2010. This compares with 268 (including 64 techMARK stocks) worth an aggregate £108.5 bn at 30 November 2007 – a fall of 30% in number over just three years.

2010 saw only three new listings of technology companies on the UK markets, all on London's junior AiM market. Digital Barriers, a digital security and surveillance firm joined AiM in March, raising £20m. Yorkshire-based healthcare software supplier EMIS Group raised £50m in a placing that valued the company at £175m. Completing the trio, private equity group Apax Partners earned an estimated 2.5 times return on its investment with the IPO of Promethean World, the interactive whiteboard company, which valued the business on float at £400m. But after this flurry of listings the pattern for the rest of the year was the more familiar one of trade consolidation and a return to private equity activity.

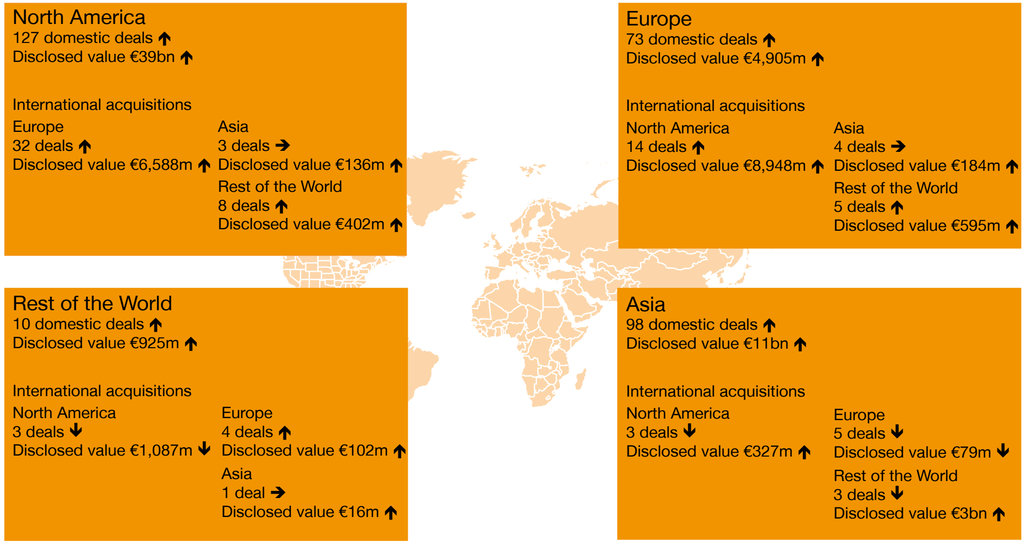
Part of the reason for the challenges of the UK listed market is that scale of end market is important to technology companies and end markets are bigger in the US and Asia, making them more attractive as places to list. There is also a tendency for small technology companies incubated in the UK to look for an exit or to move to a different geography before gaining real scale. In the US and Asia by comparison there is greater support, through incentives and tax breaks, for entrepreneurs to remain for the long term and to gain real scale. Other European jurisdictions, too, offer greater tax incentives to companies locating in their jurisdiction – such as the tax credits on R&D offered in Ireland and the low corporate tax regime in Switzerland.

The UK government is making positive noises about encouraging innovation and there are initiatives – such as the recent announcement of a reduction in tax from 24% to 10% on the commercialisation of new patents – that suggest the direction of travel is moving the right way. But the reality remains that early stage investment in the UK technology space is still a tough place and we do not expect a significant shift in the availability of capital. In these circumstances, we expect that UK technology companies, particularly small and mid-cap firms, will continue to be vulnerable to overseas trade and private equity buyers in 2011.

Geographic Trends: the West steps up

After the gap narrowed last year, 2010 saw US players regain their dominant position in terms of global transaction volume, accounting for 39% of all global deals. In 2009 Asia matched the US in terms of deal volume, however it has been unable to sustain its momentum and slipped back slightly to account for just 28% in 2010 (versus 35% in 2009). European companies are also back in the M&A market, rising from a low of just 17% of deal activity in 2009 to 25% in 2010.

Domestic and international technology deals map



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

Cross-border deals are on the rise, particularly driven by US acquirers. The number of US bidders acquiring European targets has risen 68% in 2010, with a combined deal value of €6.6bn (a figure that has more than doubled from €2.7bn in 2009). UK-based and European technology companies are continuing to be attractive targets for overseas acquirers, particularly US trade and private equity players looking for geographic expansion and a platform with access to a tier 1 financial services client-base. High profile cross border PE transactions included KKRs acquisition of Norwegian business and accounting software provider Visma for €1.4bn, Advent International's €317m acquisition of outsourcing and consultancy specialist Xafinity and Spectrum Equity's acquisition of risk and compliance solutions provider Trintech for €65m.

On the trade side, In June, Pitney Bowes, the US provider of software, hardware and services that integrate physical and digital communication channels agreed to buy UK-listed Portrait Software, a provider of customer interaction optimisation software, for £44m in cash. Other 2010 acquisitions by US buyers include Kana Software's acquisition of public sector software provider Lagan Technologies and ADP's acquisition of HR and payroll solutions provider OneclickHR.

Thus far most of the acquisitions of UK companies by international buyers have been relatively small-scale in-fill deals. But, in an environment where the multi-billion deal has reappeared and large trade players are making significant moves, we would not be surprised if one of the larger UK-based technology companies was swallowed up in 2011.

Key Messages

"We're currently seeing a number of financial and trade buyers that are expressing a renewed interest in making strategic acquisitions in the UK and Europe in 2011"

Tom Fenton - Head of US Corporate Finance

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