



8<sup>th</sup> June 2006

Dear Colleagues

A few questions have been raised recently about how sustainable is the recent revival in the fortunes of the technology industry. Some interesting dynamics emerged in the early months of 2006. Merger and acquisition (M&A) slowed slightly, IPO actions failed to match the talk as the number of technology floats dipped again. And stock markets have looked anything but stable.

### **ARE TECHNOLOGY ACQUISITIONS PEAKING?**

After twelve quarters of continuous increases in the number of European technology acquisitions, the 1<sup>st</sup> quarter 2006 saw the first reversal of the trend. The number of transactions in the quarter was 790, down 5% on the 828 deals in Q4 2005, but well up on the 679 acquisitions one year ago in Q1 2005. However, although the number of transactions is down, the combined value of all deals was substantially higher at \$150.7 billion when compared to Q4 2005 (\$93.1b) and Q1 2005 (\$54.0b).

The UK maintained its position as the country where most buyers are based. It is followed by Scandinavia and then by France, Germany and Benelux, which all showed good gains over the past year. USA and Canadian buyers slowed slightly accounting for about 11% of all deals - down on the all time high of 15%. Interestingly, Eastern and Central European companies were by far the most active buyers in the telecom sector.

Private equity investors have been major players in the divestment process by funding institutional or management buy-outs or buy-ins or by taking direct stakes in the company concerned. They have accounted for over 15% of all acquisitions in the first three months of the year.

The median valuations of all technology company acquisitions as measured by the price to earnings (PE) ratio have held reasonably steady over recent quarters. The median PE ratio during Q1 2006 was 17.06. However, price to sales (PS) ratio finished the quarter at 1.47, well up from 1.01 one year ago. This has come about because of recent increases in corporate profits. The same effect has been seen on the public markets where the stock prices have increased but the PE values have declined.

The answer to the headline question above is that acquisition activity may well have peaked simply because it has been running at a very high level and at some stage there was always going to be a quarterly dip. The good news is that there are no indicators that suggest there is going to be any significant decline in the immediate future. For those shareholders who are considering the sale of their business over the course of the next six to twelve months, only a significant decline in economic conditions would be likely to impact the valuation.

If you would like a copy of the Q1 2006 Review please click:

<http://www.regent.co.uk/news/newsview.asp?n=236>

## **STOCK MARKET VOLATILITY - THE GOOD, THE BAD AND THE UGLY**

After a few years of relatively steady upward movement in the world's stock markets, we have now seen a decline in the last six weeks of 9% in both the Nasdaq and UK Techmark indices. However it is not the absolute decline that is worrying - all stock markets overheat at times and need correction. Many market analysts had been suggesting that we were due some readjustment and now it has happened - and is possibly still happening. What is worrying is the daily volatility.

First - the Ugly. The stock price of a company is meant to represent the value of that business when multiplied by the number of shares. Management of listed companies need that valuation guidance as an important input in determining the level of funding that could be available for the development of the business both by organic and acquisitive expansion. Hedge funds however are now having a significant influence on share prices through their trading activities. Their motivation, whether to buy or sell, has nothing to do with the value of the business but merely whether the share price is likely to go up or down in the immediate future. On most days, after the effect of the hedge funds, share movements are determined by economic factors and competitive performance. Only occasionally are the changes in the valuation of a stock based on the actual performance of the company concerned.

Next - the Bad. Stock markets are an essential component of business infrastructure for certain types of companies. AIM has very successfully positioned itself as the champion of smaller growth companies that need liquidity. Quite correctly, many technology companies have looked to AIM to provide such resources. It is attracting IPO candidates from around the world because of its ease of entry and lack of Sarbanes Oxley regulations. 56% of all the European technology IPOs in 2005 were on AIM. Unfortunately it is attracting many companies that are simply not stable enough for the fish-bowl type examination that goes with a listing. Most institutional investors do still not understand technology. Volatility amongst the larger non-tech companies that they do comprehend is one thing. But instability in performance amongst smaller tech companies produces "volatility-on-steroids" in share prices.

Finally - the Good. Two factors stand out in examining technology acquisition valuations. The first is that there is less volatility than the public markets. Companies are valued based on all the usual attributes of performance and positioning, and in the main, deals are struck within a relatively narrow and predictable range depending upon these attributes. The second is that the discount that generally exists for private companies compared to publicly listed companies, which over the years has typically been assumed at about 30%, is now much less. For example, the median PE and PS ratios for listed UK software and service companies were 21.5 and 1.47 at the end of April 2006. The comparable ratios for acquired companies were 18.5 and 1.38 respectively giving a median discount of less than 10% .

The industry needs a healthy stock market that will accommodate the requirements of companies and investors alike. At the same time, the industry has a duty to make sure that companies seeking a listing are ones that will give comfort to the institutional investors over the long-term.

## **JEREMY ASHER REJOINS REGENT**

Some six years after leaving us, Jeremy Asher has rejoined Regent. He has an extensive track record of M&A deal execution and strategic advisory projects gained over the last eleven years.

He has completed over thirty international M&A transactions including the sale of shareholder-managed businesses, corporate divestments and acquisition mandates. Amongst others, Jeremy has completed projects and divestments for corporates such as

Mitel, Buhrmann, Misys, Telenor, Autocue, Severn Trent IT Services, Fujitsu (most recently the sale of their Finnish Mobile Billing software operations) - as well a sales of entrepreneurial and VC invested companies such as Cimage Novasoft to Sword Group and Intuitive to IMR Global.

Jeremy is a qualified accountant with over thirty years of industrial and commercial experience as a specialist technology sector Corporate Finance advisor and formerly as CFO of International Companies in the IT and communications sectors, working in Europe, the USA and Japan for such companies as Index Technology, Uniplex, IXI and Finnigan MAT (Scientific Instruments)

### **REGENT'S STRONG START TO THE YEAR**

I am pleased to report that the year has started very well for Regent. Some of the transactions we have completed in the first five months include the sales of:-

- SwissQual to Spirent,
- Safe Computing to an MBO financed by HSBC
- Wight Cable to a management buy-in team
- 3i-backed MI Services to Business and Decisions in France
- Room Solutions to the Indian organisation NIIT
- Talisman in Switzerland to the Dutch headquartered Vedior Group

Mervyn Waite, CEO of Talisman, felt compelled to write to us about the assignment "It is clear that the professionalism and willingness by Regent to put in the time necessary made the difference" and "Regent came in with a first class service for me and my fellow shareholders".

Regent offers the largest European-based team specialising in technology acquisitions. Our research capability, international network and continuing contact with top executives of all the major technology companies ensures that we will maintain our leadership position.

With best wishes

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Chairman

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