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M&A TRENDS IN THE SILICON VALLEY – SPRING 2010
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ONE – THE NUMBERS (Sources = DA Davidson, Growth Point Tech Ptners, E&YTech Services)

- M&A Volume
 - Bottom out in Q109...consecutive rises in Q309 and Q409
 - But 2009 as a whole was 29% lower than 2008
 - Tech Deal announcements in Q409 covered mobility, games, social networking, energy and health care (E&Y)

- M&A Valuations
 - Q409 total value was \$35B vs. Q408 at \$9.2B
 - 2009 as a whole was 2% lower than 2008

- Big Company buyers since 2008 – include
 - Google (AdMob for \$750M)
 - AOL (Bebo for \$860M)
 - Intel (Wind River Systems for \$884m)
 - Cisco, Intuit, Microsoft & Symantec

- Private Equity Dealflow - down 50% from 2008 and 65% for 2007

- IPO Market Trends
 - Down 81% from 2007 – down 2% from 2008 (59 IPOs priced in 2009)
 - Secondary market is active – 881 follow-ons in 2009 vs. 398 in 2008

- Predictions for 2010
 - IPO market creates hope – M&A will be active on volume, values flat
 - Pent-up supply of companies....and perhaps demand (excess cash for buyers)
 - Deals are principally strategic....buyers are companies, not private equity
 - Active sectors are currgrowth technology

TWO – WHAT WE ARE SEEING

- Auctions are impossible – Fastscale, Aurora
- Pricing after the LOI is down...and up!
 - Fastscale – projections, last quarter performance
 - Savvion – higher priced deals....timing is critical
- Middle Market Deal Drivers - Sellers:
 - Industry windows – Fastscale in Cloud Computing
 - Limited organic growth potential in immediate future (Savvion)
 - Investors want to end cash burn and take the loss (Aurora)
 - Execution risk – Nano Integrated Services in semi-conductor services
 - Dilution – Fastscale
- Middle Market Deal Drivers – Buyers
 - Strategic – technology, talent, markets – fit with existing channels
 - M&A growth to substitute for slow organic growth
 - Distress pricing
 - Excess cash (see WSJ 3/4/10)
 - From cost reductions during Global Recession
 - Dividends and buybacks is inefficient; interest returns minimal
 - Cash on balance sheet makes the Buyer a target!
 - M&A is best alternative
- Critical Deal Dynamics
 - Speed
 - Clean technology
 - Key innovators intact
 - Low burn...efficiency
 - Not distressed....have time
 - Start with partnering discussions
- Deal Killers
 - Disgruntled shareholders - Aurora
 - Complex capital structure – Inmatrix
 - Buyer instability – Nano
 - High burn rate
 - Unrealistic projections
- Large Buyer Quirks

- Residual knowledge
- Founder tie-ins/vesting
- Integration – Leadership (EMC, Ingram Micro, Google, Yahoo)
- Bugaboos...tax reporting (Google), lawsuits (EMC), fraud

- Aggregators
 - Finattech – investor and outsource driven; emerging markets
 - Nano – 3-way formation – flip within 1 year; pre-engineered
 - BlueHawk Networks – migration into managed services

- Hot Sectors – What we have sold
 - Cloud computing
 - Consumer electronics
 - Services – semi-conductor, BPO, managed services
 - Are incremental, technology and revenue extensions for larger companies

- Hot Sectors – What we think is coming
 - Data overlay technologies – organization and filtering
 - Consumer device connectivity
 - Cloud – security, integration of virtual platforms, SMB management
 - Games (from ipod to MMO), virtual goods, instructional games

- Trends on terms – more buyer friendly:
 - Higher escrows
 - Longer survival of reps
 - Dollar one baskets...baskets amounts <\$50K
 - Higher indemnity caps
 - More earn-outs
 - More seller paper

THREE – WHAT IS UNCLEAR

- Private Equity – are not players in the Valley for mid-market deals
- Are revenues/customers really important?
- Role of bankers – front end analysis is more important
- Direct CEO discussions make deals happen
- Companies doing too well not marketable?
- In this market, companies are not bought – they're sold?

FOUR – WHAT WE KNOW ABOUT GOOGLE

- Longer process: LOI...Term Sheet...Definitive Docs
- Larry and Sergey make the decision...almost always
- Talent is what they are focused on
- Founder vesting still key to deal structure – taxed as compensation
- On March 2nd announced moving away from earn-outs

- The Google way

FIVE – RULES OF ROAD MOVING FORWARD

- identify buyers now...build business towards this
- pursue logical strategic partnerships that may lead to an M&A
- cut fat – set up a lean organization – outsource non-critical functions
- don't take in a strategic investment if think this will flip into an M&A
- targets now are heavy on engineers, light on executives
- IP portfolio is critical...patents, open market rights, no source code escrows, clear assignments into the company
- Assume one year to get a deal done....
- Don't overfund the company

SIX – SELLING TO US BUYERS

- pick your buyers in advance...create a phantom auction
- set financial objectives before the sale – and sell to the 1st buyer that meets this. Hesitation will lose the deal. Don't sell before ready to move fast
- sign standard NDAs to get into the deal, build momentum, but dribble out the info
- bankers have limited utility in selling companies < \$20M in revenues; use for front end advice only....and don't sign on for big fees and long terms
- Figure out European tax issues in advance....
 - Up front tax on earn-outs and options
 - Accounting treatment
 - Full acceleration on exits
 - Labor law restrictions on terminations
 - Tax on export of IP