

US technology M&A insights Q1 2013 update

April 2013

*A publication from
PwC's Deals practice*

At a glance

By every measure, the first quarter of 2013 was a dismal one for technology M&A, with volume and value dropping precipitously

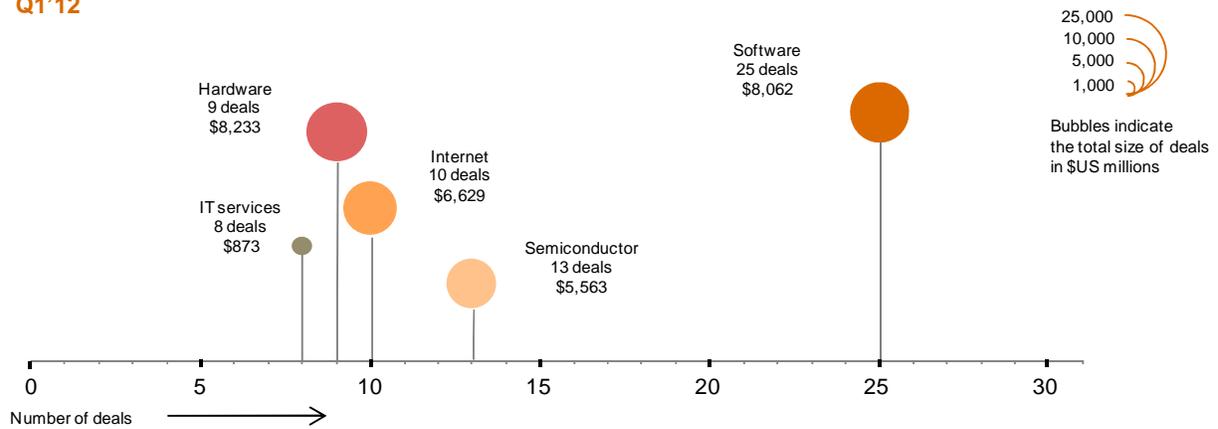
Software M&A was the sole bright spot, evidence of the cross-industry allure of these companies

Positive signs in the US economy coupled with a reduction in uncertainty are laying the foundation for more robust deal activity as the year progresses

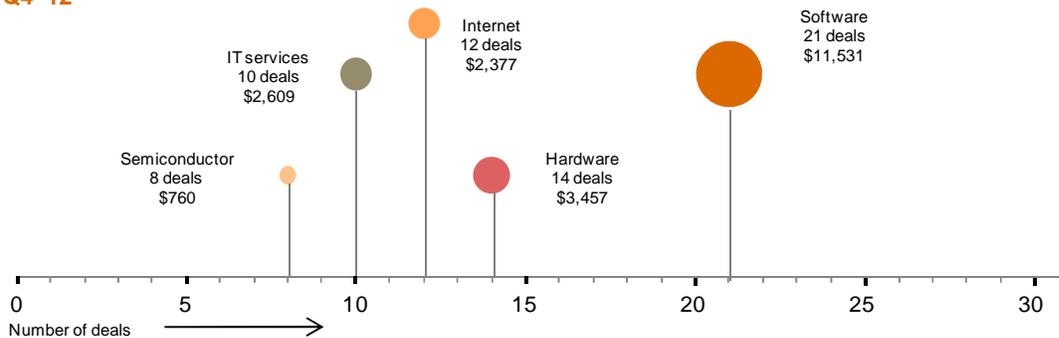
Technology deal activity drops precipitously despite overall economic recovery trends

Number of closed technology deals and deal value by sector, \$US millions

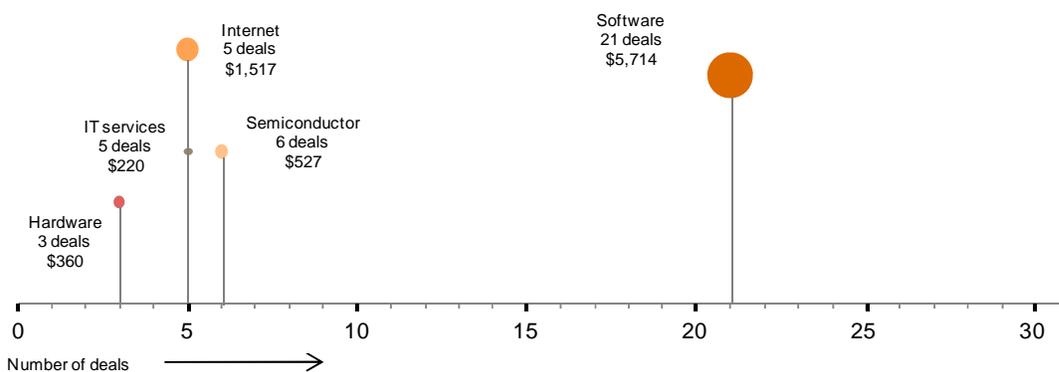
Q1 '12



Q4 '12



Q1 '13



Source: Thomson Reuters

Positive signs lay the foundation for a rebound in technology deal activity as 2013 progresses

Welcome to the first-quarter 2013 issue of PwC's *US technology M&A insights*. The first quarter of 2013 showed numerous signs of a recovering US economy. The unemployment rate stabilized around 8%, interest rates remained at 50-year lows, housing prices and new housing starts were on the rise, technology spending forecasts held steady, and the stock markets soared upward with the Dow Jones and S&P500 reaching all-time highs and the NASDAQ returning to levels not seen since late 2000. All the while, cash stockpiles at technology corporates continued to reach unprecedented levels. Yet, technology deal volume and value took precipitous drops, reaching a four-year low. With all of this positive news and market momentum, what happened to technology deals?

At the risk of repeating ourselves, uncertainty happened (or, should we say, continued?). In the background of all of the good news, the first two months of the quarter were filled with debate on the impending US government sequestration and prognostications of its impact on the broader economy. Government budget cuts and their knock-on effect on commercial enterprises and their employees were originally touted as "catastrophic" before being toned down to "inconsequential" as the March 1 deadline neared. With customers and consumers uncertain which forecast to believe, historically active technology acquirers looked inward to cost reduction efforts and realignments and away from M&A.

Instability abroad in Europe and Asia, with high unemployment rates in select European countries and revised growth estimates for the emerging economies of Asia, also played a part. The European debt crisis claimed a new casualty, Cyprus, casting a further pall on the region. Surprisingly, though, cross-border deals comprised a larger portion of closed deal volumes (57%), well in excess of historical quarterly run-rates. The flow went both ways, with overseas acquirers looking to the United States and vice versa, albeit at much lower transaction values.

After a moderate decline in the US equity markets at the tail end of 2012, investors welcomed positive returns as the Dow Jones, NASDAQ, and S&P 500 increased 11.3%, 8.2%, and 9.6%, respectively, during the first three months of the year. As the markets rose, so too did the prospects for technology initial public offerings (IPOs), signalling that investors may have finally shaken off the jitters generated by Facebook's post-IPO 2012 performance. Seven technology IPOs were

placed in the first quarter of 2013 with total proceeds of just under \$1 billion, still below the volume and value of IPOs in the fourth quarter of 2012 but a strong start to the year. More importantly, these new listings registered a one-day average return of 27%, the highest of any industry. With new registrations increasing 41% in the first quarter, along with improved returns and high public filing activity late in the quarter, the technology industry may well be poised for a more active IPO market as the year progresses.

The low volume of deal activity in the first quarter of 2013 highlights the varied approaches technology companies employ to stay innovative and achieve high growth targets. Pivoting away from all-out acquisitions, technology businesses once again converted traditional acquisition efforts into minority investments and alliances with companies holding technologies and product offerings that hold promise. While technology businesses often use alternative approaches, activity appears to have increased in the first quarter. To wit, adding minority investments to the volume of deals in 2013 would result in incremental transaction volume of 15% on top of the 40 deals closed in the quarter.

The overall decline in volume was felt across all sectors within technology save one: software. This is to be expected, as software tools become integrated into products and services across all industries, thereby creating efficiencies and enabling core business functions. It therefore follows that not just pure technology companies will add the innovators that develop these tools to their M&A shopping list.

With major US political and economic uncertainties largely now past, we expect technology companies will again look to opportunities for growth on the horizon. Sequestration, rather than a "catastrophe," may ultimately turn in their favor as technology businesses provide government organizations innovative tools to reduce costs and drive efficiencies. On a further positive note, a flurry of (smaller) deal announcements at the end of March by a host of key technology players may point to the start of a more robust deal environment to come.

As uncertainties subside, look for dealmakers to return to the table

Closed transaction volumes were down 38% while value plummeted 72% versus Q1 2012

Key announced transactions

The first quarter of 2013 met with mixed results as blue chip technology players paused to reassess strategic priorities and address product and service portfolio offerings no longer in line with long-term objectives. Such activity was evident as media rumblings of divestitures and buyouts permeated the market and acquisitions above \$1 billion were few. Dell announced talks with Silver Lake Partners and founder Michael Dell for a potential \$24.4 billion buyout. The announcement, along with subsequent counterproposals, makes the proposed Dell deal not only the largest technology buyout since the KKR-led \$29 billion buyout of ecommerce giant FirstData in 2007, but also one of the largest buyouts in history. Additional corporate deals above the \$1 billion mark announced in the first quarter were limited but included:

- Oracle's plans to acquire public company, Acme Packet, the Massachusetts-based developer of Internet signaling systems, for \$1.7 billion. Oracle continues its billion-dollar acquisition spree in 2013, after closing the Taleo and RightNow acquisitions in 2012 and the Eloqua transaction in February for less than \$1 billion.
- Scientific Games, a supplier of systems, software and equipment to the gaming industry, agreed to acquire WMS, a manufacturer of lottery terminals and slot machines, for more than \$1.5 billion. With Nevada passing legislation to approve online poker activities, we can expect new deals directed at Internet gaming to follow.
- Total System Services, an electronic payment solutions provider, agreed to acquire NetSpend, a provider of general-purpose reloadable prepaid debit cards and related financial services, for \$1.4 billion.

Many of the key technology players announced deals toward the end of the quarter, including Amazon, Cisco, Google, and Yahoo. Additionally, HP announced the sale of webOS to LG Electronics, Microsoft announced the sale of Atlas to Facebook, and Cisco announced the sale of its Linksys division to Belkin, providing further evidence of strategic adjustments among large technology companies.

Aside from several of the large private equity firms vying for a chance to acquire Dell, announced transactions among financial buyers were few during the first quarter.

Key closed transactions

After quarterly declines in deal volume and value in 2012, the first quarter of 2013 encountered its most challenging M&A scenario since 2009. Volume decreased 38% to 40 deals in the first quarter compared with 65 deals closed in the last quarter of 2012. Deal value fared worse as a result of few deals in excess of \$1 billion closing by March. First-quarter deal value dropped 60% to \$8.3 billion from the previous quarter.

Compared with deal activity in the first quarter of 2012, deal volumes and values decreased 38% and 72%, respectively, in the first quarter of 2013.

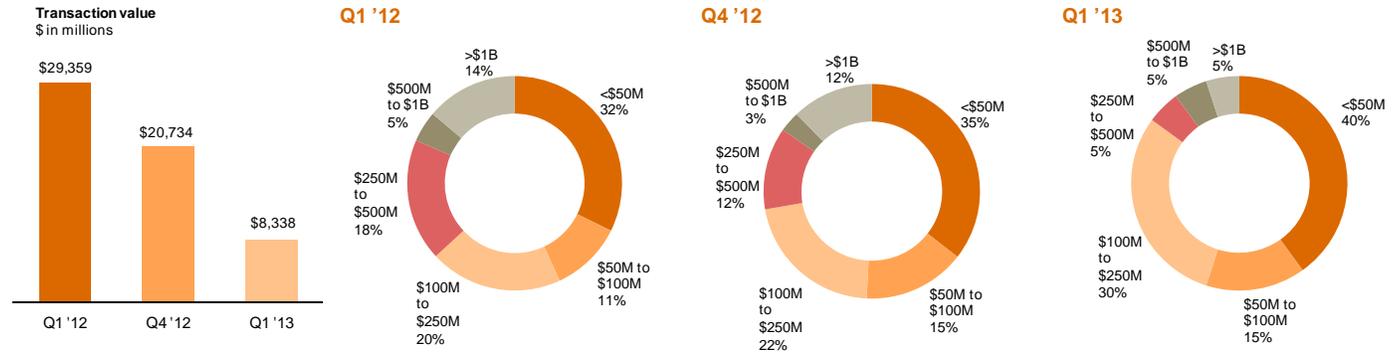
As would be expected, with only two transactions in excess of \$1 billion, average deal values declined 50%, from an average of \$415 million for the full year 2012, to \$208 million in the first quarter of this year. The largest transactions closed during the quarter include:

- Private equity firm Apollo's acquisition of McGraw Hill Education for \$2.4 billion. With the introduction of technology tools in both K-12 and higher education classrooms, traditional publishing companies such as McGraw Hill have integrated software and online education platforms into their offerings to enhance the learning experience, making them largely technology-driven enterprises.
- Fiserv's acquisition of Open Solutions, a provider of enterprise software to the financial services industry, for \$1 billion, including assumed debt.
- Oracle's acquisition of Eloqua, a provider of on-demand revenue performance management software, for \$871 million.

Private equity buyers comprised a small portion of closed deal activity in the first quarter but represented half of the quarter's deal value, thanks to the Apollo-McGraw Hill Education transaction. Of the 40 deals closed during the quarter, eight (20%) were acquired by financial investors or backed by financial sponsors. Private equity deal volume slowed in the first quarter after robust activity in the latter half of 2012. The proportion of private equity-backed transactions to corporate sponsors is relatively consistent with historical trends that place private equity deals at 15% to 25% of deal volume in a given quarter.

Closed US deals by value

Comparison of total deal value

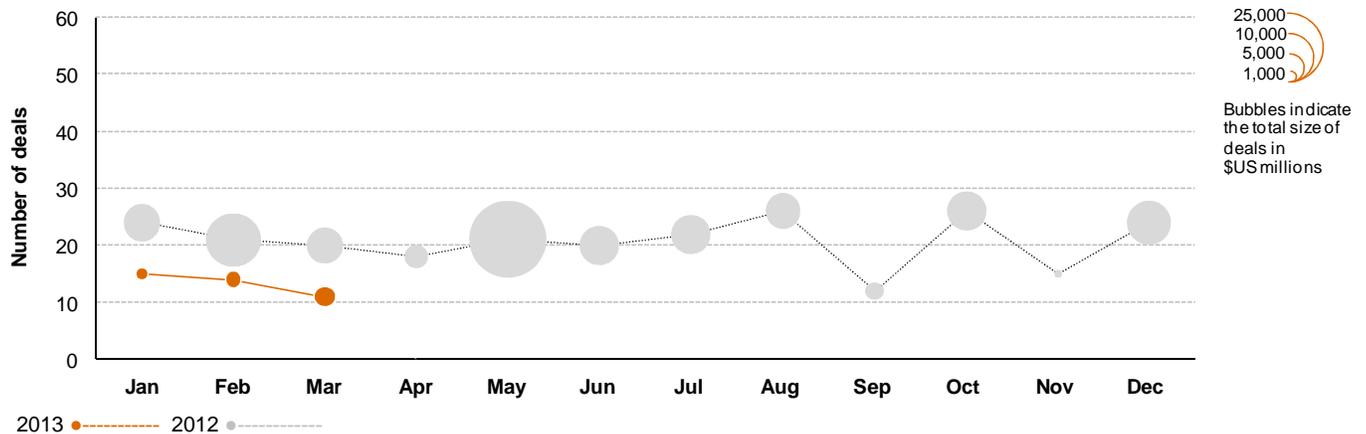


Source: Thomson Reuters

\$ in millions, except #	Q1 '12		Q4 '12		Q1 '13	
	Number of deals	Total deal value	Number of deals	Total deal value	Number of deals	Total deal value
<\$50M	21	600	23	744	16	387
\$50M to \$100M	7	486	10	644	6	442
\$100M to \$250M	13	2,052	14	1,989	12	1,804
\$250M to \$500M	12	4,103	8	2,749	2	768
\$500M to \$1B	3	1,588	2	1,156	2	1,521
>\$1B	9	20,530	8	13,453	2	3,415
Total	65	29,539	65	20,734	40	8,338

Source: Thomson Reuters

US technology deals by month, 2012 and 2013



Source: Thomson Reuters

Software transactions are likely to continue their dominance as deal activity rebounds

The software sector dominated transaction activity in the first quarter of 2013, comprising 53% of deal volume and 69% of deal value. Software transactions impacted a variety of industries, demonstrating the increasing significance of software-driven functionality and automation to products and services. Software deals included companies providing solutions to the education, manufacturing, banking, retail, entertainment and other industries, with tools to enable interactive entertainment, gaming, investment analysis, 3D technology, mobile banking, data analytics, and enterprise management. M&A continues to provide businesses with expedited access to innovative software solutions designed to transform internal processes and enhance customer experiences.

Internet transactions comprised 13% of total deal volume and 18% of total deal value for the period, a 58% decline in volume from the prior quarter and a 36% decrease in value. IT services and semiconductor businesses also experienced declines, with semiconductor deals dropping 25% from last quarter and IT services declining 50%.

The hardware sector was the hardest hit with hardware deal volume decreasing 79% from the prior quarter and 67% from the first quarter of 2012. Hardware deal values were

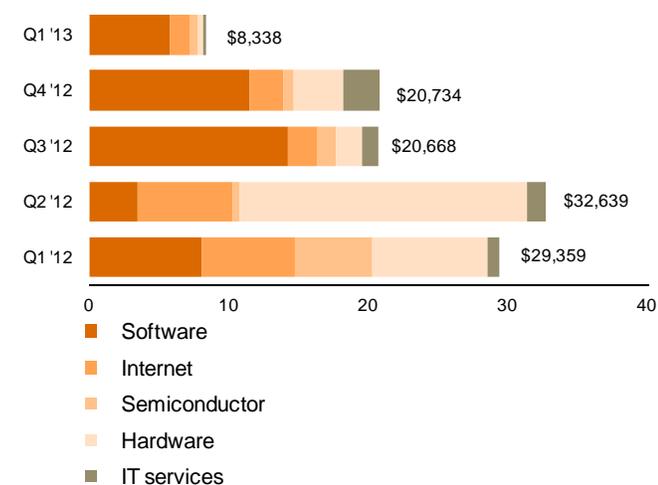
down even further in the quarter, decreasing 90% and 96% from the prior quarter and the first quarter of last year, respectively. With focus placed on enhancing current product offerings and shedding unwanted assets, a shift away from hardware and toward software was a natural result that manifested in the quarter. This trend is likely to continue in coming quarters, with deal activity focused on software tools and other product enhancements.

Conclusion

By every measure, the first quarter of 2013 was a dismal one for technology M&A. Yet, we believe that positive signs in the US economy are laying the foundation for more robust deal activity as the year progresses.

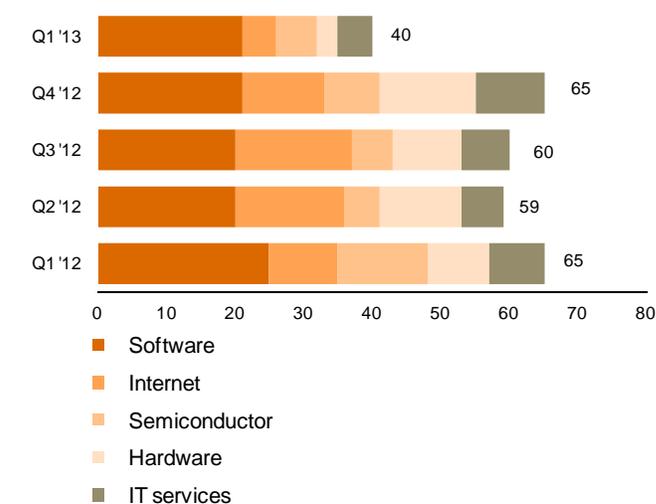
Software transactions are likely to continue their dominance of deal volumes because of their importance to businesses both inside and outside the technology industry. Deal announcements by large technology companies in the latter part of the quarter suggest that historically acquisitive players are coming back to the deal table. These factors, combined with the record levels of cash remaining on hand at technology majors give us confidence that deal activity will rebound in the quarters to come.

Closed deal value by sector, \$US millions



Source: Thomson Reuters

Closed deal volume by sector



About PwC's Deals practice

Smart deal makers are perceptive enough to see value others have missed, flexible enough to adjust for the unexpected, aggressive enough to win favorable terms in a competitive environment, and circumspect enough to envision the challenges they will face from the moment the contract is signed. But in a business environment where information can quickly overwhelm, the smartest deal makers look to experienced advisors to help them fashion a deal that works.

PwC's Deals group can advise technology companies and technology-focused private equity firms on key M&A decisions, from identifying acquisition or divestiture candidates and performing detailed buy-side diligence, through developing strategies for capturing post-deal profits, to exiting a deal through a sale, carve-out, or IPO. With more than 9,800 deals professionals in 75 countries, we can deploy seasoned deals teams that combine deep technology industry skills with local market knowledge virtually anywhere and everywhere your company operates or executes transactions.

Although every deal is unique, most will benefit from the broad experience we bring to delivering strategic M&A advice, due diligence, transaction structuring, M&A tax, merger integration, valuation, and post-deal services.

In short, we offer integrated solutions tailored to your particular deal situation and designed to help you complete and extract peak value within your risk profile. Whether your focus is deploying capital through an acquisition or joint venture, raising capital through an IPO or private placement, or harvesting an investment through the divesture process, we can help.

For more information about M&A and related services in the technology industry, please visit www.pwc.com/us/deals or www.pwc.com/technology.

About the data

We define M&A activity as mergers and acquisitions where targets are US-based companies acquired by either US or foreign acquirers or foreign targets acquired by US technology companies. We define divestitures as the sale of a portion of a company (not a whole entity) by a US-based seller.

We have based our findings on data provided by industry-recognized sources. Specifically, values and volumes utilized throughout this report are based on completion date data for transactions with a disclosed deal value greater than \$15 million, as provided by Thomson Reuters as of April 1, 2013, and supplemented by additional independent research. Information related to previous periods is updated periodically based on new data collected by Thomson Reuters for deals closed during previous periods but not reflected in previous data sets.

Because many technology companies overlap multiple sectors, we believe that the trends within the sectors discussed herein are applicable to others as well. Technology sectors used in this report were developed using NAIC codes, with the semiconductor sector being extracted from semiconductor and other electronic component manufacturing codes by reference to SIC codes. In certain cases, we have reclassified deals regardless of their NAIC or SIC codes to better reflect the nature of the related transaction.

Focus Article

Addressing BPSI earlier in deals accelerates integration, realizes synergies and maintains business momentum

In March 2013, we hosted a Silicon Valley BPSI Roundtable of 15 technology companies to share knowledge and best practices on business process and systems integration (BPSI). Here are some of the key takeaways.

A critical component of the deal

All participants agreed that a distinct emphasis on BPSI during a deal is a measurable differentiator for success. There are myriad reasons why business processes and their supporting IT systems are a critical component in realizing the goals of any merger integration. For example:

- With retirement of legacy systems and related processes, a company **realizes cost synergies**
- Early transition to a common platform **accelerates integration** by enabling global standard processes, adjusting scale, and facilitating cross-selling
- A thoughtful, robust approach to systems leads to a smooth transition that **maintains momentum** and critical business capabilities

So what exactly is BPSI and what leading practices do Silicon Valley veterans employ in the planning, execution, and accountability for this critical workstream?

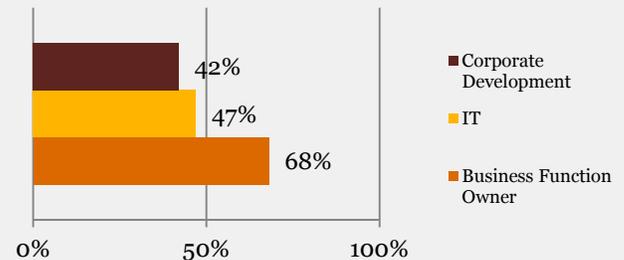
BPSI defined

BPSI is a methodology that starts with documenting the processes of the to-be-acquired company (target), and mapping and gapping them against the buyer's processes. The gaps must be resolved either as capabilities required to support the target business model or gaps that aren't expected to drive incremental value. The new capabilities must be built out in the form of policies, processes, and systems functionality. Simultaneously, data cleansing, systems testing and training are delivered in preparation for a successful go-live.

Joint business function and IT responsibility most effective

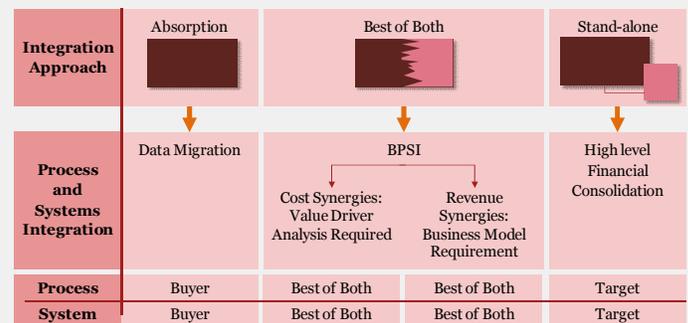
Our participant survey findings show strong consensus on questions of ownership and approach. Responsibility for execution and related budgets in a joint leadership model between business function owners (68%) and IT (47%) was

the favored approach, while corporate development was noted as potentially sharing some responsibility.



Consensus view: BPSI responsibility and ownership

Nearly two-thirds (63%) of respondents apply a standard integration approach, completely absorbing the target and thereby transitioning the legacy business processes and systems into the acquirer's IT infrastructure and business processes. The remainder (37%) selected the best of both breeds for BPSI between the buyer and the target.



Integration approaches from full to stand-alone

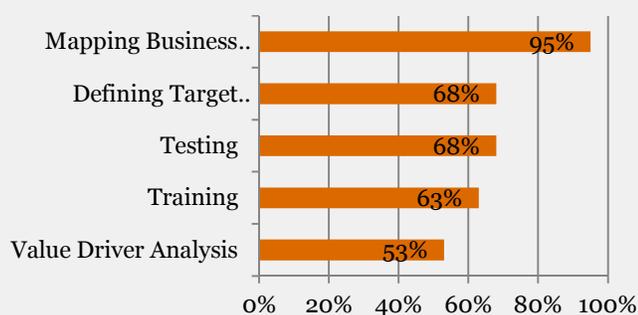
Almost three-quarters of the participants (74%) indicated that the business function leads the overall BPSI rather than solely the IT function. This supports the importance of a joint business and IT leadership model, either through the Integration Management Office or through a parallel governance model.

Start earlier to validate possible synergies

We have seen BPSI increasingly become a major component of the pre-deal diligence process, particularly where contemplated synergies are playing a larger role in the valuation.

A majority of companies planned their initial BPSI activities during the due diligence phase, although execution timing of these activities varied from pre-deal diligence through to 180 days post close.

Mapping “as-is” and “to-be” business processes is almost ubiquitous (95%), and in our experience can also be the most time consuming. Defining the end state, testing and training were evenly weighted. Value driver analysis (53%) garnered the fewest votes although, based on our experience, we recommend increased emphasis here to ensure post-close accountability for pre-deal promises of synergy returns.



Most frequently followed approaches to BPSI

Dedicated resources, sponsorship and funding a must

Roundtable participants were unanimous that the most critical factors for successful execution of BPSI are the availability of dedicated resources, a BPSI Integration Management Office with an active and empowered sponsor and, of course, adequate funding.

Because BPSI analysis is increasingly a critical component of the business case behind a transaction, the validation of that business case is occurring earlier in the process. Based on our experience, we recommend companies involve BPSI as soon as possible in the due diligence process to ensure they properly assess and quantify decisions that affect transaction value. In particular is the inclusion of necessary funding in the deal model.

A central IMO keeps the integration on track

BPSI is best managed and measured through a centralized Integration Management Office (IMO) with processes and

tools that are part of a repeatable integration framework on each transaction.

All companies at the roundtable have a centralized IMO responsible for driving integration to completion and delivering on deal objectives. They varied in the details of their implementation according to whether the IMO was a permanent function or assembled in response to a particular transaction.

It was generally agreed that the variability in the scale of transactions presents challenges to even the most robust team and framework. These challenges are greatest when dissimilar companies are combined, such as when a hardware company acquires a software company. In these cases, where customer and product directions are different, BPSI might need detailed attention.

The IMO decisions should bear in mind that customer and product directions drive BPSI process complexity. Once the strategic intent of the transaction is clear, the tactical implementation of BPSI is the result. In our experience, this is where a BPSI workstream at the IMO level is invaluable to address cross-functional issues.

Methods and techniques used to track synergies, deal objective attainment, and time frames varied and included embedded measurement within existing financial systems as well as stand-alone tracking in separate reports and spreadsheets. The solutions correlated to deal size, with the solution tending to correspond to deal-specific challenges (e.g., earn-outs, acquired employee retention).

BPSI: accelerating, realizing, and maintaining value

Once viewed as a necessary, but not always critical, aspect of the post merger integration process, BPSI is increasingly recognized as an integral part of pre-deal analysis and post-deal value acceleration. By moving these activities earlier in the deal cycle, companies are increasing accountability with quantifiable business cases for both cost-saving and revenue-generating synergies.

While companies may vary on the specific roles, responsibilities, approaches and tools, there is general agreement among the assembled Silicon Valley deal veterans that the time has come for BPSI to play both a larger role in pre-deal validation activities and an accelerated role in post-deal synergy realization.



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