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It's slow going out there in the marketplace. Yet despite that guarded view, we're optimistic that at least the economy appears to be moving in the right direction. And, as the two articles below make clear, even caution doesn't preclude opportunities to both create and reap value.

Cheresh Casinelli and Derek Dowsett lay out several strong possibilities in the technology and health care sectors, for example. And Taft Kortus provides a blueprint for sellers looking to optimize their assets.

These upside prospects must be tempered, however, by the fact that many companies are still struggling and by the fear that weak job creation, the European debt crisis, or the oil leak in the Gulf of Mexico could force the economy to take several giant steps backward.

While we're waiting for the macro tea leaves to settle, though, it's important to stay positive and take constructive action that positions your company for the eventual recovery, which is sure to come at some point. To paraphrase Kortus, sticking closely to fundamentals is probably the best operating philosophy for the remainder of 2010.

—Ken Salgado, Chair,  
Technology & Life Sciences Group

## The Financial Markets: A Mixed Midyear Report

by Cheresh Casinelli, Partner, Transaction Services Group, and Derek Dowsett, Northern California Practice Lead, Technology & Life Sciences Group

So far 2010 appears to be one of the more interesting financial years in recent memory. It's certainly not as glum as 2009, but it's not as ebullient as the pre-meltdown era either.

In terms of merger and acquisition activity, the strategic market is the most active. In terms of the source and nature of deals, we're seeing dispositions from many large companies that are attempting to get their financial houses in order. On the buy side, many businesses are trying to grow their revenue bases through acquisitions. There are also a number of strategic business partners that are coming together in more formal ways; these moves are an effort by smaller players to partner rather than going it alone in these uncertain times. Finally, there's lots of roll-up activity and lots of smaller deals (less than \$50 million) being closed.

It's true that 2009 was virtually moribund, so year-over-year figures look great so far in 2010. But even beyond simply comparing against low numbers, the first quarter of

this year we saw a significant pickup in the transaction market overall.

That's one aspect of the market today. The other is less positive. There are many companies that are simply in dire straits. They need money to stay in business, and so they're eager—at times anxious—to do a deal, especially given the tight credit markets, which



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have squeezed liquidity. Targets now have new, realistic expectations about purchase prices. They know they're not going to see ten times EBITDA, and they're willing to accept four to six times EBITDA instead. For their part, buyers are looking at targets as real opportunities. They see real values, and they want to act and acquire.

There are other factors at play too. The recent unraveling in Europe, for example, has penetrated the IPO market, which may not open up in the way people anticipated. Many IPOs have already delivered diminished

profitability versus forecast, and these deals aren't going up 20–40 percent. They're staying flat. That's why we believe venture capitalists and private equity firms will start to become flexible in terms of exit strategies for their companies; the high-valuation IPO may no longer be the answer it once was.

Now is also probably the right time to put the overall stock market in perspective. The brutal truth is that it's been flat for a decade. IPOs don't drive the economy, but they're definitely affected by it, and we continue to see that reflected in deal activity and valuations.

We do see growth opportunities, however, and they can—and should—be leveraged in the second half of the year.

In technology, for example, there are several good behind-the-scenes plays. One we like is back-office support and systems in the mortgage industry. The health care sector employs technology in the same way, and the data-management part of the business should expand, given the dynamic reorganization we expect to see in this industry.

Online gaming and social networks that are add-ons to other products and make the user experience more interesting are also going to be bright spots for the remainder of 2010 and into 2011.

When it comes to software, we're watching Internet-based software as a service (popularly known as SaaS). This new business model has proved itself and is now moving to a more mature growth phase.

Biotechnology is less robust. We see lots of deals forming in the future—but not today.

People use the word recovery loosely. But what does it really mean? Given the mixed data, it's difficult to call 2010 a year of economic recovery. The economy does appear to be firming, but the labor markets remain in disarray. The financial markets appear to have settled down, although they can still plunge without notice. And while the transaction markets appear to have some momentum, M&A activity is often defensive and IPOs are often underwhelming.

As a result, while 2010 may be a much better year than 2009, it's not the kind of year that makes investors and deal makers truly happy to be in the game.

## Obtaining Maximum Value for Your Company in Today's M&A Market

by Taft Kortus, Northwest Practice Lead,  
Technology & Life Sciences Group

At the end of 2009, we were optimistic that the M&A markets would pick up and become the key near-term source of liquidity for investors before any real momentum in the IPO and capital markets kicked in. We also believed the technology sector, led by reemerging growth and profitability, would be at the forefront of the deal flow. And finally, we envisioned a good M&A ecosystem, with sellers motivated by the need for exits and buyers in search of much-needed new products, innovation, and revenue growth.

But our fairly positive stance for the technology sector was tempered by caution, given the cloud of uncertainty surrounding the economy and its fragile recovery. So, as we approach the middle of 2010, are we sticking to our guns?



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The short answer is yes. But acquirers and investors are still wary, and they're doing much more diligence before closing deals. They're also more partnership-focused—that is, they view an acquisition as the continuation or initiation of a partnership with the former management or founders of the purchased company. Thus, their diligence expands beyond the traditional financial or technology variables.

The current consolidation trends will continue, and as a result it's critical for sellers to understand how to demonstrate and maximize their value in the eyes of the consolidators. So what should those who are positioning themselves for liquidity do to improve their prospects? Based on our insight and conversations with key industry leaders, here's our best counsel on the subject:

- *Focus on building value.* Create value in your products, for your customers, and in your underlying industry segment. Value will always be recognized and rewarded. This means you can't set out to be bought or sold; you need to focus on the core business and establish value through your product in order to achieve strategic and financial success.
- *Understand where your company, technology, or service sits in the overall ecosystem of your segment.* Know who all the players are, how you match up, who your competitors are, and where you provide value. By understanding your ecosystem, you'll be better able to guide your company and your product or service toward true value creation. You'll also learn how you fit into current consolidation trends and, ideally, gain insight on how acquirers view your company from the outside. In many cases, this can differ from your internal viewpoint.
- *Stay close to your strategic partners.* Form close relationships with strategic customers, resellers, and industry leaders—but don't get so close that you lose competitiveness or independence. When you develop these relationships, a host of potential acquirers is only a phone call away, and they already understand your value proposition. Be sure not to sign exclusivity agreements, joint ventures, or any other arrangement that could potentially lock other interested parties out of a potential deal or force an acquirer to be locked into business with a competitor.
- *Make sure your company's overall strategy is aligned.* This means your acquisition criteria are shared—and agreed on—by key members of management, the board, and investors. A lack of alignment can distract your company from building value, and it can

be seen as a weakness by potential acquirers. It's easy for values to shift during transaction negotiations, so having core fundamentals is key to maintaining solidarity.

- *Make sure you have the best management team possible in place.* Your company's leadership is more important than ever. And many acquisitions are now being carried out as a way for acquirers to bring on thought leaders or a great management team. Retention of that great management team will likely be an important component of any transaction's negotiations. This requires planning and forethought with incentive plans and equity structures long before the transaction is realized.
- *Understand the metrics that will best demonstrate your company's value proposition.* Many acquisitions focus solely on profitability or revenue growth, but other core trends—such as showing a strong ability to monetize a historically free product or service—let an acquirer know that the product or service has real value to customers. Understand how to demonstrate the value in your pitch.

- *Don't let a possible or pending transaction consume your business and management.* Again, focus on building value in your prime area of expertise, and when a transaction possibility becomes active, ensure that your management team remains focused. Transactions generally take longer and are more complicated than originally estimated,

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and this can distract management for an extended period of time.

- *Be bought, not sold.* As a seller, you can gain a better deal by positioning your company in such a way that an acquirer can't pass you up. The best marketing is to demonstrate value and threaten your segment's ecosystem with innovation so that acquirers need your business to stay competitive as part of their long-term strategy.

There's no simple way to maximize value as a seller in today's uneasy marketplace. But by adhering to fundamentals, companies seeking liquidity can achieve many, if not all, of their goals.

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