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M&A Activity Slows

By: John Partridge

The Canadian M&A juggernaut slowed in the third quarter as credit market turmoil derailed debt-heavy transactions, leading Toronto investment bank Crosbie & Co. Inc. to suspect that deal making may have peaked as far as the current business cycle is concerned.

"I wouldn't be surprised if May, June and July of this year don't turn out to be the high point in the cycle because we had such wonderful conditions on all fronts, including debt markets, that we may not see for a long time, if ever again, in terms of the availability of debt and the pricing of it," Crosbie managing director Ian Macdonell said. He made the remarks in a telephone interview after the release of the latest Financial Post-Crosbie quarterly report on mergers and acquisitions in Canada.

The report said a total of \$91-billion in deals were announced in the third quarter - including takeovers of Alcan Inc. and Stelco Inc. - marking the second-highest total ever after the record of \$166-billion set in the preceding quarter.

The latest performance brought the total value of Canadian mergers and acquisitions in the first nine months of 2007 to \$319-billion, already surpassing the previous 12-month high of \$275-billion set last year, the Toronto firm said.

The "core" Canadian M&A market driven by strategic buyers continued to be very strong in the third quarter, Mr. Macdonell said, helped by such positive factors as globalization, demographics, strong corporate balance sheets and a "reasonably positive" outlook.

However, the report said the credit crunch triggered by the collapse of the U.S. subprime mortgage market "virtually shut down" the market for debt-heavy leveraged buyout deals during the third quarter.

One sign of the credit crunch's toll was that capital groups, such as private equity firms (including those controlled by pension funds), accounted for just 9 per cent of the value of deals exceeding \$100-million in the quarter.

This was down from 42 per cent in the second quarter, when they were involved in the \$35-billion acquisition of BCE Inc. and the \$7.75-billion purchase of Thomson Corp.'s Thomson Learning unit.

The same sort of signals were coming from south of the border yesterday, where, Reuters news service reported, Morgan Stanley chief financial officer Colm Kelleher told a conference in New

York that he sees merger and acquisition activity slowing next year from 2007 levels as the volume of big leveraged buyouts falls.

Lawyer Richard Willoughby, co-head of mergers and acquisitions in the New York office of Toronto law firm Torys LLP, agreed. "The pace of private equity-driven LBO transactions at the very large end has clearly stalled," he said in a phone interview.

"But," he added, "the middle market transactions continue."

The Financial Post-Crosbie report said the number of Canadian M&A transactions in the third quarter dropped to 460 from 517 in the preceding three months, while the number of "mega-deals" - those worth more than \$1-billion - dropped to 12 from a record 23 in the preceding quarter, according to the report.

Mr. Macdonell is looking for at least some recovery in private equity participation. "With the amount of committed private equity and pension fund money sitting on the sidelines, it's only a matter of time before the market adjusts to the changes in debt availability and pricing and we see buyout activity pick up again," he said.

Industrial products companies were the prime targets in the third quarter, accounting for 118 transactions worth \$45-billion, led by Rio Tinto PLC's \$38-billion takeover of Alcan and U.S. Steel Corp.'s \$1.8-billion purchase of Stelco. Consumable fuels was the second most popular sector, with 87 deals worth \$17.7-billion.