

Future Trends in CEE M&A: which way forward?

2009

PricewaterhouseCoopers provides industry-focused assurance, tax and advisory services to build public trust and enhance value for its clients and their stakeholders. More than 146,000 people in 150 countries across our network share their thinking, experience and solutions to develop fresh perspectives and practical advice.

Central and Eastern Europe is changing fast. In this report, we explore the key trends affecting mergers and acquisitions in the region, both now and in the future*

*connectedthinking

Contents

Introduction by Chris Butters	1
Trends	
1. The rising middle class will drive healthcare deals	4
2. Diversifying real estate opportunities	10
3. Increasing consumerism in Russia will drive M&A	18
4. Consolidation in the electricity sector will continue apace	26
5. Competition between private equity firms for deals in the region will intensify	30
6. Central Asia and the Caucasus will see increasing foreign investment	34
7. The need for growth capital will drive IPOs	40
8. Commercial due diligence is becoming an essential part of M&A	44
In conversation with...	
Joanna Simonowicz and Geoff Upton	8
Glen Lonie	14
Radu Stoicoviciu	16
Michael Knoll	23
Chris Hemmings	24
Emilian Radu	29
Other publications	46

About this report

The M&A team

- Locally resident experts with international experience and global reach
- High-quality research capability with extensive analytical skills and tools
- Tight network of dedicated M&A professionals across CEE
- Operating regionally since 1990
- Local nationals with excellent personal networks in business and government

Our rationale

The PwC CEE M&A network provides clients with expert knowledge delivered by highly experienced deal professionals resident in CEE. Our deal makers are well connected within their business communities so are able to provide up-to-date commercial and realistic advice with immediate practical value and distinction within a deal making process. We understand the need for insightful analysis, detailed planning, focused communication and timely contact.

How this report will help deal making

- Explores key trends that will affect the M&A environment in CEE
- Offers insights into new and rapidly developing markets
- Provides intelligence and data to aid decision-making both now and in the future
- Gives direct access to sector experts

“GDP growth rates of between 5% and 10% across the region have fostered a vibrant M&A market as local and overseas businesses have sought to respond to change and take advantage of fast-growing markets”



Chris Butters
PwC Partner, CEE M&A leader
chris.butters@cz.pwc.com

Welcome to “Future Trends in CEE M&A”, our report into the key trends that we believe will drive mergers and acquisitions activity in Central and Eastern Europe, the CIS and Russia during the coming 12 to 24 months and beyond. Here we have drawn on the broad experience and in-depth knowledge of our teams on the ground across the region to identify which will be the most important themes for international and domestic buyers and sellers. We hope you enjoy the publication and find useful information, as well as some food for thought.

Central and Eastern Europe’s economies have undergone a transformation in the past few years as preparation for and accession to the European Union have stabilised the new and prospective member states, while rising commodity prices have filled the coffers of countries such as Russia. GDP growth rates of between 5% and 10% across the region have fostered a vibrant M&A market as local and overseas businesses have

sought to respond to change and take advantage of fast-growing markets.

Privatisation processes are continuing in many countries, offering a wealth of opportunities to buyers, but the region is now home to a deep and increasingly sophisticated private sector M&A market, covering a broad spectrum of sectors. Even those that were historically considered tough, such as heavy engineering and healthcare, are now actively being targeted by investors.

Our markets have been helped by the fact that, while the “credit crunch” has squeezed many parts of the world, CEE and Russia have felt less of an impact. It is still possible to obtain debt financing for good deals – even if it does take a little longer than usual – and local banks, which have historically been more conservative than their Western European or US counterparts, are still very much in the lending business.

As the M&A landscape develops, we are seeing increasing interest in the region among international private equity funds as well as larger fundraisings from local players. With global firms such as TPG and pan-European funds including Bridgepoint opening offices in CEE and Russia, as well as other firms gathering resources to invest in the region, competition is building in some parts of the market for deals. Local and international players are competing particularly in the €100m-plus deal bracket – an area where deals are few and far between in many CEE countries.

Russia’s sheer size, its power to accumulate wealth through exploitation of hydrocarbons and its rapid economic

transformation mean that it is likely to offer more €100m-plus opportunities for investment. The mega-deals are well publicised, but less well known is the fact that the country’s mid-market is now becoming an active area for M&A. Below the big league, companies are consolidating fragmented industries to tap into Russia’s vast internal market as wealth starts trickling down and creating new middle classes with increasing disposable incomes. They are also looking beyond Russia’s borders to gain access to new markets and technologies and diversify risk.

For some, venturing further eastwards to Russia and Central Asia is a natural step because the high growth and shifting frontiers promise higher returns in the form of new markets and nascent consumer cultures. Yet the fact remains that many investors are still wary about Russia and its neighbouring states. While they may have become comfortable with the idea of buying in the new European Union member states, many buyers view the political situations and the legal and regulatory frameworks as being too unstable to warrant serious attention – for now.

This polarisation of views will diminish over time, of course. Yet we believe the wider region already holds an enormous amount of opportunity for those armed with the right knowledge. We hope this report will add to your understanding of the issues affecting the different markets both today and in the future, and help you to unlock the untapped potential that Central and Eastern Europe, Russia and Central Asia could hold for your business. It continues to be an exciting time across Central and Eastern Europe.

Page 4

Trend **1**

The rising middle class will drive healthcare deals



- Disposable incomes are on the increase
- Private equity is targeting investments in clinics
- Private hospitals are becoming an active area for investment

199

the number of healthcare deals completed in CEE during 2007

\$1.9bn

the amount invested in healthcare deals in CEE during 2007

Page 30

Trend **5**

Competition between private equity firms will intensify



- Investors are looking to CEE's fast-growing economies for deal flow
- Local firms are raising larger funds
- Private equity frontier is shifting to East and South

\$406m

the amount private equity firms in the region raised during 2003

\$14.6bn

the amount private equity firms in the region raised during 2007

Page 10

Trend **2**

Diversifying real estate opportunities



- Move to urban centres away from the capitals
- Investors shifting their gaze further East
- Some maturity developing in certain markets

6

Polish towns with a population of more than a million people

5.5%

expected yield in 2008 from residential apartment rentals

Page 34

Trend **6**

Central Asia and the Caucasus will see increasing foreign investment



- High commodity prices are generating wealth
- Infrastructure and logistics offer great opportunities
- Asian investors are flooding to the region

9.4%

Georgia's GDP growth in 2007

\$25bn

the estimated amount needed for investment in Kazakh infrastructure

Trend 3

Increasing consumerism in Russia will drive M&A



- Mid-market deals are gaining momentum
- Fragmented industries are consolidating fast
- A new wave of smaller strategic buyers is targeting Russia

71%

the percentage of deals below \$100m in 2007

\$30bn

Russia's largest deal in 2007: the RUSAL-SUAL-Glencore tie-up

Trend 7

The need for growth capital will drive IPOs



- Companies cannot afford to delay IPOs if they are to take advantage of fast-growing markets
- Warsaw is becoming a regional stock exchange

25

the number of foreign companies listed on the Warsaw Stock Exchange

\$60.5bn

the amount raised by companies in CEE and Russia through IPOs in 2007

Trend 4

Consolidation in the electricity sector will continue apace



- Energy firms seeking vertical integration
- Investment need is driving sales
- Energy security and renewables demand new technologies

813%

the increase in 2007 Russian deal value in electricity over 2006 figures

\$42bn

the amount of investment needed in CEE's generation capacity

Trend 8

Commercial due diligence is becoming an essential part of M&A



- Buyers need to come to CEE with finely tuned strategies to ensure M&A success
- Investors need to find and test new angles to win deals in an increasingly competitive market
- Sellers are looking to maximise value through vendor due diligence

1. The rising middle class will drive healthcare deals

Rising disposable incomes in Central and Eastern Europe and a strong desire to catch up with Western European standards of care are bringing about a rapid rise in private healthcare spending in the region. With the sector set for double-digit annual growth over the medium term, there are plenty of opportunities for private equity and strategic buyers

Key contact: chris.butters@cz.pwc.com



“We will see a lot of investors looking at buy and build strategies over a broad set of medical services – this is an area where there is a lot of growth to come.”

Mike Wilder, PwC Partner

Private healthcare expenditure in Central and Eastern Europe is growing fast, fuelled by rapid economic growth and the resultant emergence of middle classes in the region. Disposable incomes in CEE have been on the increase for several years. They still generally trail those in Western Europe but are catching up fast. A recent study¹ even found that some areas of CEE have more income per capita than some regions of Western Europe. For example, the GDP per capita of Slovenia is higher than Portugal.

Greater spending power is leading to increased aspirations and a desire to improve standards of living, and gaining access to better quality healthcare is top of the priority list for many people.

Rising incomes alone would result in increasing use of private healthcare, but there are a number of other factors that will drive rapid growth in the sector. Poor public provision, the legacy of several decades of under-investment, incomplete reforms that result in continuing problems with allocation of resources, low wages among medical staff and a need for modernisation of facilities mean that there is increasing discontent across the region. A recent poll² found, for example, that the number of Czech

citizens satisfied with healthcare dropped by 10% to 40% compared with the previous year and those dissatisfied had increased by 5% to 25%. Those with the money available will vote with their feet and use better quality, better resourced private healthcare services.

But it is not just individuals who are funding private healthcare. Many employers are seeking to attract and retain staff as well as increase productivity by providing medical insurance, a move that will bring more of the population into the private system over the years to come.

Healthcare expenditure figures show there is a lot of catching up to do in the region. As a percentage of GDP, they were 6.2% in Poland in 2006, according to World Health Organisation figures; the comparable figure for France was 11.1% and for Europe 9.1%.

Ageing populations will also play an important role in the growth of the industry. An EBRD report³ demonstrates how much of an issue this will be. It states: “It is in the EBRD region that we will see the most rapid ageing during the next two decades worldwide (despite [a] poor longevity expectation). By 2025, the median age

will be more than 10 years greater than it is now in eight of the countries in the region. The number of elderly is already high in many countries and will continue to rise up to 2025.”

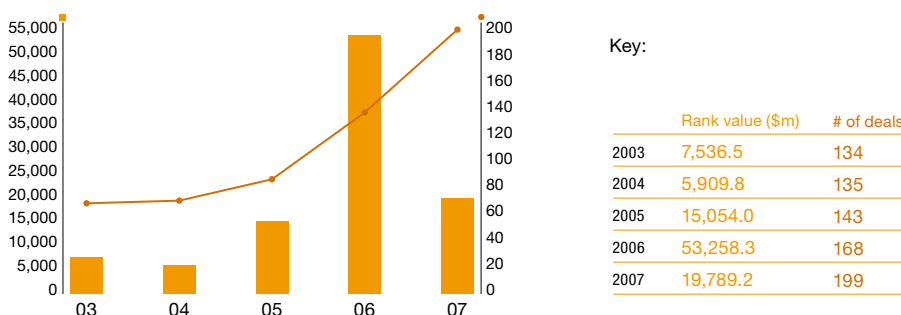
Healthcare expenditure for the elderly (over 65s) in the OECD countries is currently around 1% of GDP, but given the rapid rise in average ages in the CEE region, this can be expected to increase significantly.

All these drivers mean that investors will be increasingly attracted to the sector as high-quality companies see annual revenue growth of between 20% and 30%. Many of these businesses will need more capital to meet increasing demand for their goods and services.

Outpatient clinics are attracting private equity funding

With high growth rates, stable revenue streams from subscription models and a real estate element to private clinics, the sector is a natural home for the region’s increasing private equity capital. To date, healthcare transactions have not featured highly in CEE deal lists, but interest is rapidly gathering momentum.

CEE healthcare M&A



1 GfK Purchasing Power Europe 2007/2008
2 VVM Agency
3 Futures of the EBRD Region to 2025

Source: Thomson Reuters

Future Trend 1: The rising middle class will drive healthcare deals

“As people get wealthier, they become more health conscious and want to spend money on keeping fit and healthy – we are seeing this across CEE. It’s having a huge effect on private clinics, which are growing at tremendous rates”

Piotr Nogajczyk, PwC Slovakia

Mid Europa Partners has acquired three outpatient healthcare providers in the past 18 months (see box opposite for details) and, earlier this year, dialysis and diagnostics specialist Euromedic – one of the region’s earliest private equity investments in the sector – was sold by Warburg Pincus to Merrill Lynch.

The most popular area for investment among private equity houses in the coming 18 to 24 months and possibly beyond will be private outpatient clinics, where there are a number of well-established brands with good coverage across a given country. There are several of these types of deal already in the pipeline and many more to come. The strategy of choice, as with the Mid Europa investments, will be to consolidate chains of clinics nationally or even regionally.

These types of opportunity may well attract the attention of some of the international buyout houses, many of which have had considerable success in healthcare in Western European markets. It is likely, however, that local players, with their networks, will be more successful in their attempts to buy these businesses.

The creation of private hospitals will gather momentum

Private hospitals will become a more active area for investment. Attempts by governments throughout the region to bring in private service providers to increase efficiency are creating opportunities. The Czech government, for example, transferred a portfolio of hospitals through a long lease, allowing private operators to provide services in what are essentially still public hospitals.

The market is increasingly being controlled by a handful of chains such as Agel, which has already accumulated a portfolio of hospital operations through disposals and management contracts from the state, city authorities and the railways. Some of the smaller players in the market are also gathering steam: Privamed Healthia, for example, currently owns two hospitals and is looking for more. It recently bid for three Bohemian hospitals but did not succeed on this occasion.

In Poland, Warsaw Stock Exchange-listed company EMC Instytut Medyczny is planning either share issues or attracting capital from a strategic investor to take over two hospitals from local government, which it wants to

add to its portfolio of five hospitals and two outpatient clinics. But the opportunities in this area are not without risk as government plans to sell assets are often slow to materialise and can be derailed by political opposition.

Most opportunities therefore centre around greenfield developments, where a number of investors are taking a close look. Mid Europa-backed Lux-Med has had approval to build a hospital in Warsaw, with construction to start this year through to 2010, while Penta Investments is believed to be looking at building greenfield hospitals. Among the strategic players are Swissmed, which has said that it will set up a hospital network in Poland and the Polish arm of Swedish insurer Medicover Ubezpieczenia, which is currently building a €40m hospital in Warsaw’s Wilanów district.

Even countries without a reputation for leading-edge privatisation are getting more courageous with healthcare, leading to investment opportunities. In Georgia, for example, an innovative hospital disposal programme will involve the construction of greenfield facilities, leaving the old city centre hospitals to be redeveloped for commercial use.

Recent healthcare deals

Country	Hungary	Russia	Romania	Russia	Russia	Russia
Target	Euromedic International NV	Skopinpharm ZAO	LaborMed Pharma SA	European Medical Center	Moron Ltd; Vitim & Co.	OAO Akrihin
Sub sector	Clinics	Pharmaceuticals	Pharmaceuticals	Clinics	Pharmaceuticals	Pharmaceuticals
Bidder company	Ares Life Sciences; Merrill Lynch Global Private Equity	Nizhpharm JSC	Advent International Corporation	Goldencorp Enterprises Ltd (BVI)	Oriola-KD Corporation	Polpharma SA
Deal value (€m)	800	125	123	71	85	45



Pharmaceuticals will see more investment

Most companies in the pharmaceuticals industry have been snapped up by strategic buyers. However, private equity is becoming more interested in the sector as growth in the industry accelerates. With most companies in the region specialising in generics, these are relatively low-risk businesses with high margins. There are also still consolidation opportunities within the market, adding a further attraction in particular for private equity.

Advent International's investment in 2003 and subsequent exit from Romanian business Terapia demonstrated the high returns that are possible from this type of deal. Advent has since acquired another Romanian pharmaceutical company, LaborMed. Warburg Pincus has also recently sold its investment in Zentiva to Sanofi-Aventis and Anthiarose, the holding company of Dutch financial group PPF. TPG made its maiden investment in Russia earlier this year, with the acquisition of a 50% stake in pharmaceuticals distributor SIA International in an \$800m all-equity deal. There are a number of further deals in the pipeline.

Despite private equity's new interest in the sector, strategics are still very active in the market. Poland's largest pharmaceutical manufacturer Polpharma, owned by Dutch business Genefar, has been acquired by Hungarian drugs business Gedeon Richter for \$1.3bn to create one of the region's largest pharmaceutical companies. Croatian company Pliva was acquired recently by US player Barr in a \$2.2bn deal. Barr itself was then bought by Israeli generics player Teva for \$7.46bn, plus \$1.5bn in assumed debt.

But the popularity of the sector is pushing up prices, particularly for high-quality businesses. This year's LaborMed acquisition saw one of the region's highest multiples at 5x sales, higher than the 2006 Terapia sale at 4.2x. The regional average still stands at 1.9x, but this may well rise.

With increasing competition for deals in this area, as well as a dwindling supply of independent companies in some countries, investment focus may shift over the medium term to areas such as distribution, where consolidation is taking place, and possibly to drugstore networks, many of which are still in the hands of local business people.

Case study

Consolidating clinics

When Mid Europa Partners acquired outpatient clinics Lux Med and Medycyna Rodzinna last year, the company was slightly ahead of the curve. It had spotted an opportunity to capitalise on the high growth rates of Poland's private healthcare industry – currently running at between 40% and 50% a year – and create businesses of scale in a fragmented industry.

The firm has since acquired a third chain of clinics, Poland's third largest, Centrum Medyczne LIM, which serves 250,000 patients and has 15 clinics. Its growth rates are typical of companies in the sector: its H1 2008 sales grew by 30% year-on-year and its customer base grew by 35% in 2007 to 222,000. To cater for demand, it is planning to supplement its current clinics with a further three this year alone.

In addition to launching new outpatient clinics, Mid Europa may make further acquisitions in the market, although it has said it is now concentrating on integrating the three companies. The idea is to combine the back offices to create synergies while still maintaining the individual brands of each business. There will also be opportunities for cross-selling between the companies.

The opportunities for consolidation in the market are clear. Combining these three companies – all major players in the market – will give a market share of just 20%. It is hardly surprising that a number of other private equity houses are now looking seriously at this space as an area of investment.

Lithuania	Romania	Poland	Poland
Gintarine Vaistine, Limedika	Famos SA	Itero Katowice SA	Medycyna Rodzinna, LIM Lux Med
Pharmaceuticals	Medical equipment	Pharmaceuticals	Clinics
Polska Grupa Farmaceutyczna SA (PGF)	Top Genko SA	Torfarm SA	Mid Europa Partners LLP (formerly EMP Europe)
23	18	16	ND

Source: Mergermarket

Poland is one of the region's most exciting markets



In conversation with
Joanna Simonowicz and
Geoff Upton, PwC Poland

e: joanna.simonowicz@pl.pwc.com
e: geoff.upton@pl.pwc.com

Q Poland is starting to attract the attention of some of the larger private equity funds. Why?

JS Warsaw has become a hub for private equity activity in the region. Most of the funds active in Central and Eastern Europe have a base here and a lot of relationships are formed and driven from here. Many local and smaller funds that have been active in the market since the early 1990s are based here, and the private equity infrastructure, such as advisers and banks, is already here.

GU Poland's size – it's one of the largest countries by population in the region – means that there are more

deals here than in many other countries. Firms have found it harder to do significant deals in, say, Hungary or the Czech Republic; Poland's economy is larger and so that has maintained a lively deal market. We will see more private equity houses setting up here, to do deals in Poland and to use it as a regional base.

Q How is their entry affecting the Polish M&A market?

JS Many are targeting €100m-plus deals but that is a pretty limited space to be looking, so there's a lot of competition at the larger end of the transaction spectrum. At the same time, many of the local players have raised larger funds and so are also targeting bigger deals.

I think it will be harder for the international players that haven't already built up a presence here. In Poland, you really have to develop a relationship with the entrepreneurs and with the local advisory community. You need networks and connections, as well as people on the ground who speak fluent Polish.

Some funds have been successful at making investments in the region without opening an office – Warburg Pincus, for example – but that has been because they have successfully forged networks with local people. Generally, if you try to invest from afar, you're only going to be able to participate in competitive auctions.

Q Where will the most interesting opportunities be going forward?

JS We're seeing a lot of activity in construction materials off the back of the building boom here, and also in healthcare, financial services and retail. Anything to do with consumer spending will be interesting because sectors related to this are growing fast as disposable incomes rise. The economy in Poland is in good shape and, as long as that continues, deal flow in this area will be strong.

As for deal type, there are a lot of entrepreneurs in Poland who started their businesses at the beginning of the free economy in the early 90s and now have reached an interesting size for private equity funds. Some of these entrepreneurs have also reached retirement age and have no successors, others have hobbies which now preoccupy them more than their businesses or they have lost their interest for the initial business and are interested in cashing out to invest in different sectors or they have just reached the size when they need to strengthen their business and financially move up to the next level.

There are also a number of secondary acquisitions coming from the portfolios of private equity funds that invested in Polish businesses two to three years ago.

“Banks in Poland are open for business and generally aggressive in building market share. However, they are imposing more restrictive lending covenants and expecting these to be kept”

“Private equity houses are looking for bolt-ons for companies they have backed in the West. It’s a low-risk strategy because it adds value to an existing investment, there are synergies to be had, they are buying in a sector they know and they are getting access to Poland’s high-growth market”

GU We will see more public to private deals in Poland – a lot of companies on the WSE would be suitable targets. Many listed for the ability to raise further capital but, with the exception of the large companies, they have found liquidity to be an issue. For such companies private equity can offer capital for expansion.

Private equity firms are excited about the prospect, if a little daunted by the process. But there may be a delay. Shareholders need to see that the current valuations on the stock market are not just a blip – we’ve seen a realignment of valuations to more realistic levels. Once they adjust their expectations, we’ll see more activity.

Q With many industries still fragmented in Poland and the wider CEE region, how much M&A activity will be driven by consolidation strategies among private equity firms?

GU Private equity players are often very excited about the opportunities for consolidation and there have been some very successful deals based on this strategy. But I am sceptical about how well this can work extensively on a pan-regional level. It’s hard to roll out companies across the various countries, and it’s easy to underestimate the differences between the markets in CEE, especially if you have not been operating the market for long and do

not have a significant presence here. Consolidation within individual markets is much more likely.

JS However, we are seeing consolidation on a broader level. Private equity houses are looking for bolt-ons for companies they have backed in the West. We will continue to see that, especially if the difficult economic environment in many developed markets persists. It’s a low-risk strategy because it adds value to an existing investment, there are synergies to be had, they are buying in a sector they know and they are getting access to Poland’s high growth market.

Q How much of an impact is the credit crunch having in Poland – has it affected activity to the extent seen in larger markets?

GU At present, banks in Poland are open for business and generally aggressive in building market share. However, they are imposing more restrictive lending covenants and expecting these to be kept. In addition, where a deal requires syndication, there can be delays until all banks get comfortable with the deal. It’s also the case that cross-border deals are taking longer to close because they seem to require ever-increasing volumes of target analysis, commercial due diligence and more intense consideration of the investment rationale than was necessary in the recent past.

Joanna Simonowicz

Joanna has been with PricewaterhouseCoopers since 1997 and in 2002 she qualified as a member of the Association of Chartered Certified Accountants. Since 2000, Joanna has been fully dedicated to deals work. Joanna has extensive experience in transaction services, assisting multinational clients develop their presence in Poland and CEE, both through the purchase of privately held companies and privatisations. Joanna also has extensive experience in working for private equity clients on both buy-side and sell-side. During her career in PwC Joanna has been involved in more than 100 transaction assignments.

Geoff Upton

Geoff has lived in CEE since 1990, so has first-hand experience of a huge amount of change and development in the deals environment. Amongst other recent deals he has led the sale of Datart (retail chain), Pegas (non-woven textiles) which was the largest PE deal that year plus deals in supermarkets, printing ink and IT consulting. Other deals have involved privatisations, carve-outs, private equity purchases and disposals as well as refinancings such as completed with ECM in the real estate sector. Geoff is a senior Board-level adviser who provides insightful and practical value-orientated deal support.

2. Diversifying real estate opportunities

The region's real estate market is anything but homogenous. It includes the ever-escalating residential market in Moscow; newly developed commercial buildings in Krakow; industrial warehousing in Timisoara; retail parks in Ostrava, right the way through to hotel complexes on the Albanian coast

Key contact: glen.lonie@cz.pwc.com



“Russia has a number of domestic investors who are interested in real estate as well as international investors. Moscow might be the most attractive centre but there are other regional centres such as St Petersburg and Novosibirsk that are generating interest.”

Glen Lonie, PwC Partner

Each country throughout the CEE region has its own demographics and economic growth rates, ensuring that property markets are operating at different speeds. This helps to create a balanced portfolio for investors covering multiple markets.

For much of the past decade, international investors who wanted to target the region have focused on Prague, Warsaw and Budapest. Russia in general and Moscow in particular have attracted lots of interest, but the domestic market has driven much of its rise up the league tables for attracting investment.

It is of little surprise that international investors have selected the major cities in the Czech Republic, Poland and Hungary. These centres share attributes with many Western European city centres and so deliver a comforting

level of reassurance with their returns in commercial, retail, offices, residential and industrial sectors. Today these three markets are, in the eyes of many investors, overbuilt and overpriced. So the key question becomes: where should investors go to catch the next wave of returns?

This question has become increasingly complex as investors seek clarification as to the extent to which the region will be impacted by the global credit crunch. Lenders have undoubtedly become more cautious and the supply of capital is now more expensive for developers.

But real estate investors are not the sort of people to sit on their hands and do nothing. Instead they are hunting for the next tier of returns, and two strategies are emerging that will have an impact on the final months of 2008 and continue into 2009.

The first of these trends has been dubbed “second city syndrome”. Investors increasingly recognise that the urban centres away from the capital, in countries such as the Czech Republic, Poland and Hungary, are attractive centres. Prices have risen and returns have increased in these second, third and fourth cities – including Ostrava in the Czech Republic and Krakow in Poland – at a rate that exceeds the capitals in recent months. Lenders have already seen good returns delivered by those who have led projects in the capital cities in these markets and are willing to consider following up with initiatives in their second and third cities.

The second trend will ultimately have a much larger impact on the region. It is the shift eastwards as those who have made money in Central Europe have raised their appetite for risk and are

Prospects for prime yields

	Prime yields Nov 07 (%)	Expected prime yields Dec 08 (%)	Expected prime yield shift (basis points)
Apartment residential (rental)	5.26	5.53	+27
Office	6.02	6.23	+21
Central city office	5.72	5.89	+16
Suburban/out-of-town office	6.40	6.67	+27
Retail	6.14	6.26	+12
Street retail	5.91	6.02	+12
Shopping centres	5.98	6.13	+15
Retail parks	6.19	6.41	+22
Mixed use	6.67	6.74	+7
Hotel	6.69	6.91	+23
Industrial/distribution	6.97	7.09	+12
Warehouse distribution	6.85	7.00	+15
Manufacturing	7.24	7.45	+21

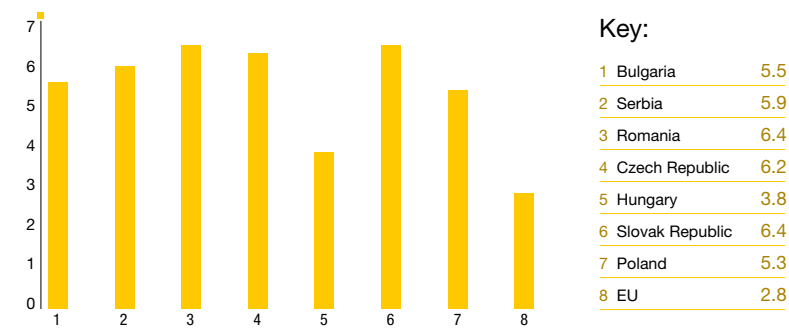
Source: PricewaterhouseCoopers

Future Trend 2: Diversifying real estate opportunities

“There are some instances where financial investors are evolving to become infrastructure investors and project developers themselves which increases the risks but can boost the project returns if they get it right”

Nick Allen, PwC Partner

GDP growth: SEE compared to CEE and Euro countries

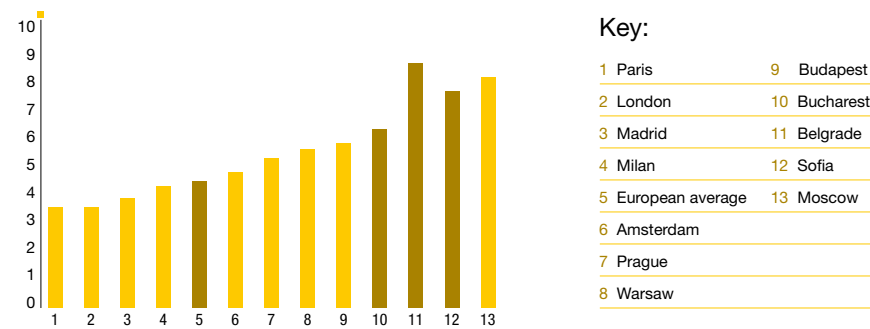


Source: PricewaterhouseCoopers

looking at investing across the wider real estate opportunities in Ukraine, Bulgaria, Serbia, Romania and other parts of South Central Europe. Russia features on this list as well but it has such extensive domestic wealth that it continues to operate as its own defined market.

Glen Lonie, the Central and Eastern Europe Real Estate Leader for PricewaterhouseCoopers, says: “Russia has a number of domestic investors who are interested in real estate as well as international investors. Moscow might be the most attractive centre but there are other regional cities such as St Petersburg and Novosibirsk that are generating interest.” In particular, he says that the amounts invested into developing Russian shopping centres is expected to be a key driver of growth in the coming times.

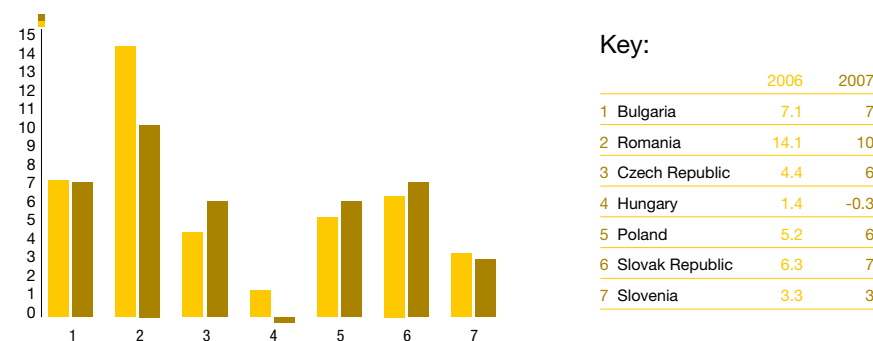
GDP growth: SEE cities compared with other European centres



Source: PricewaterhouseCoopers

One trend that is creeping on to the agenda but may have more impact in 2010 than 2009 is the development of infrastructure projects. This is more pronounced in some markets than others. For example, there is large demand in Ukraine for roads, hospitals and schools, but debates continue as to what is the most effective model to deliver it. The development of public-private partnerships, the emergence of infrastructure funds or the availability of transactional finance mean that there has yet to be a consensus developed for the best way of financing infrastructure developments in the region.

Consumption of households (real change in % against preceding years)



Source: PricewaterhouseCoopers

The rise of South Eastern Europe

Visitors staying in the Sheraton Sofia Hotel Balkan in Bulgaria need only stand for a few minutes on the Italian marble floor that outlines the lobby before they hear investors talking into their mobile phones about a new real estate investment opportunity. Property

“Albania could be the new Croatia”

Ivailo Vatev, PwC Bulgaria

investing throughout Central and Eastern Europe is hardly new. But what will distinguish the final weeks of 2008 and into 2009 is the increasing appetite of investors to target South Eastern Europe.

Sofia in Bulgaria, Belgrade in Serbia and Bucharest in Romania are emerging as the most likely new centres of regional investment in this block. Ivailo Vatev of PricewaterhouseCoopers says: “Some parts of CEE are at a relatively mature stage of development. But there are some pockets of embryonic opportunities. The SEE region is under developed and packed with opportunities.”

The newly defined SEE region expands beyond those three countries. Vatev explains that it includes Slovenia, Croatia, Bosnia & Herzegovina, Montenegro, Macedonia and Albania. Each market is developing at its own speed, but Vatev is convinced that it represents a new opportunity for real estate investors.

“Take the holiday sub-sector,” he says. “Albania is blessed with a natural beauty and costs are up to 10 times lower than other markets in the region. It is going to become a hugely popular holiday destination in the future, so investors might consider it as an early stage opportunity.” The risks may be higher, but the potential return for a hotel developer who can then persuade Western Europe that Albania is the new Croatia for summer breaks could make significant returns.

The residential sub-sector operates at a different pace, dependent on the town and city in question. A centre that is attracting ever increasing amounts of attention is Belgrade. Less than two years ago it was possible to acquire real estate assets outside the city centre for less than \$500/sq metre.



Three cities update

The following information comes from the “Emerging Trends in Real Estate Europe 2008” report produced by PricewaterhouseCoopers and the Urban Land Institute.



Prague

Prague has become the most mature market in the whole of Central and Eastern Europe. It retains good prospects and is an attractive investment for conservative investors because rents are expected to rise slightly in the coming 12 months.

2008	Prospects	Rating	Ranking
Investment prospects	Modestly good	5.7	12th
Development prospects	Modestly good	5.8	7th
Risk	Moderately low	5.5	15th

Warsaw

The economic outlook in Poland is strong and large cities – other than Warsaw – are attracting significant investment and development. The prospects are good, although the returns are unlikely to be spectacular given the low level of risk.

2008	Prospects	Rating	Ranking
Investment prospects	Modestly good	5.5	16th
Development prospects	Modestly good	5.8	8th
Risk	Moderate	5.4	19th

Budapest

Budapest has become the weakest of the three major markets in the region. The Hungarian economy is suffering from high taxes and austerity measures that have been designed to address the budget deficit. The risk has risen for investors in the region and has outpaced the potential returns, making it less attractive to invest in for the next year.

2008	Prospects	Rating	Ranking
Investment prospects	Fair	5.0	26th
Development prospects	Fair	5.2	20th
Risk	Moderate	4.9	25th

In conversation with...
Glen Lonie, PwC Partner
e: glen.lonie@cz.pwc.com



Real estate: the lowdown

Q Can you sum up what is happening in CEE real estate in 60 seconds?

GL There is an increasing volume of investments across the region but the yields are decreasing, making properties more expensive. Investors are now looking at new opportunities to the South and to the East where the yields are higher.

There are some instances where investors are evolving to become developers themselves, which increases the risks but can boost the returns if they get it right.

The debt crisis means banks are backing those they know and trust. Speculators will not get the support they once did. Lenders are employing stricter criteria and are charging more for their finance. Consequently the real estate owner is having to manage the asset and improve its underlying performance more effectively.

The need for infrastructure throughout much of the region is leading to a lot of opportunities. For instance, there are lots of infrastructure projects in Russia, Poland and Ukraine related to the Winter Olympics and European Championships which are being hosted, but there is no set model for structuring the projects.

Q Which part of the region has the best investment prospects?

GL Investors need to understand their attitude to risk before it is possible to answer that question. But we recently published “Emerging Trends in Real Estate Europe 2008” with the Urban Land Institute and came up with some interesting findings. At one end of the scale Russia and Turkey are booming, but we are seeing the emergence of very different real estate markets in Europe.

Q Have prices topped?

GL It is impossible to generalise about the whole CEE region. For instance, there is increasing consensus that the Czech market is mature, has high stability and lower investment risks. But if you go further East and South, there may be more opportunities at a different price, but the risk profile will be different.

Q How available is debt financing?

GL Finance is no longer available in 32 flavours. But good projects that have been well thought through and have an angle will get funding. It may be more expensive than 12 months ago and take more time to be signed off by the credit committees, but the money is available.

Glen Lonie

Glen Lonie leads PricewaterhouseCoopers Real Estate industry team in Central and Eastern Europe and CIS. He is a Tax Partner based in the Czech Republic. Glen is a member of PricewaterhouseCoopers European real estate leadership team and is the champion for Real Estate Deal Support Services, the platform under which PricewaterhouseCoopers provides services in relation to Real Estate transactions. He has broad experience managing projects and providing due diligence, tax advice and other services to a number of major real estate investors and developers. He has worked in the Czech Republic and Slovakia for 15 years and manages deals for clients across the CEE/CIS region. He has also worked for a major international construction group as International Tax Manager having responsibility for tax affairs in countries of Central Europe. Glen is an Australian CA and holds Bachelor of Commerce and Master of Taxation degrees.

Future Trend 2: Diversifying real estate opportunities

Today that price has nearly doubled. That said, PricewaterhouseCoopers is convinced that prices will continue to grow in Belgrade, arguing that it is now enjoying the same development that took place in Warsaw, Prague and Budapest a decade ago. In particular, the New Belgrade suburb has become a highly desirable business location. It is providing a home to multinationals and fast-growing domestic firms that want to have a modern base from which to grow throughout Serbia and the wider region. In recent times Unilever, Cisco and Renault have all moved in.

Vatev says: “The reality of SEE is better than the perception. Currencies are stable and income levels are rising, as is the spending power. There is high potential across all sectors.” It will not be long before a smart fund manager decides to launch a separate SEE property fund, focusing on the returns available in this part of Europe.

Green buildings in the East

Ecologically sound buildings and green infrastructure projects may be of growing interest in the West but this remains a marginal area of interest across the CEE region.

Will that change in the next year?

Visitors to a recent conference – the Central & East European Real Estate Quality Awards – would have been hard pressed to find any discussion about the subject.

Developers do not seem concerned about constructing energy-efficient buildings. If there is any change in outlook, it is being driven by the returns that may be available. For instance, there is a small number of architects who are planning to create such buildings as investors ask them to make their buildings stand out, generating higher rental and resale values.

AukettFitzroyRobinson, the international architect, has recently received outline planning consent on behalf of client OOO Parus for the scheme to develop a mixed-use apartment-hotel scheme on the Russian Black Sea coast of Sochi.

The scheme consists of two curved 35-storey hotel towers with linked podiums and it is intended to be an energy-efficient building. By the time the Winter Olympics are being hosted by Sochi in 2014, there will probably be a few more of these towers in place.

Four recommendations for 2009 in South Eastern Europe

- Consider development opportunities rather than existing property stock
- Find a local partner and check them thoroughly
- Create a network of reliable feeders to ensure project pipeline
- Do not underestimate the need for review of legal documentation

Eight cities to watch

01 Ostrava Famous throughout the Czech Republic for its industrial strength in steel-making and now one of the epicentres of the ArcelorMittal empire. The town is attracting increasing interest from international firms looking to open operations inside the Czech Republic.

02 Brno Brno is also competing with Ostrava for more foreign and direct investment into the Czech Republic. It is geographically fortunate to be very close to both the Austrian border – not far from Vienna – as well as the burgeoning Slovakian market.

03 Bratislava The Slovak capital is a fast-growing centre enjoying a booming growth in its residential property prices. There are nearly 500,000 people living in Bratislava, which is the political, cultural and economic centre of Slovakia.

04 Krakow Krakow in South East Poland is a historical city with a bright future. It is increasingly becoming a hub for outsourced service centres for a number of international organisations. It provides lots of employment for graduates who begin their working lives with these firms, and is developing an increasingly bohemian feel that is fuelling growth in residential property prices.

05 Gdansk Gdansk continues to be an important port city and a hub of Polish industrial activity. Its proximity to Russia's Kaliningrad gives it a dimension of increasing interest to those seeking to do business there.

06 Varna Varna is the largest city and seaside resort on the Bulgarian Black Sea coast and the second largest city in the country after Sofia. There is increasing interest by developers in hotel projects and residential homes for people who want to live by the sea. It is also the headquarters of the Bulgarian navy and a seaport with a thriving industry.

07 Timisoara Timisoara is the fourth largest city in Romania. It is nicknamed Little Vienna as it used to be part of the Habsburg Empire. Today it is a university town that has developed an industrial hub attracting an increasing number of businesses to the region.

08 Krasnaodar The literal translation of this city is "beautiful gift" in recognition of the gesture made by Catherine the Great when she bestowed the land to the Black Sea Cossacks. By the end of the 19th century it had become a vital trade centre in Southern Russia. Fast forward to today and there are now more than 650,000 people in the city which is near Sochi, set to become internationally famous for hosting the forthcoming Winter Olympics.

Romania is fast becoming an investment hotspot



In conversation with
Radu Stoicoviciu, PwC Partner

e: radu.stoicoviciu@ro.pwc.com

Q Romania has seen a dramatic increase in M&A over the last two years. What's been driving it?

RS Romania has only recently risen up the agenda of international investors. Let's put this into context. In the early years of the post-Communist period, Romania was something of a Cinderella state in the region. For the 10 years since 1995, everyone was looking at countries such as Hungary, the Czech Republic and Poland because they felt they were safer bets. Romania didn't attract anyone's attention, despite its large population.

However, once the country entered NATO and it became clear that it was going to accede to the European Union, international investors suddenly discovered Romania – the risk-reward equation worked for them as EU membership brought more stability and predictability to the market. Since then, we've seen a snowball effect as the market has gained momentum and Romania has become one of the fastest growing economies in the region.

The increased interest is demonstrated by the figures. According to our estimates, the number of deals in Romania almost doubled between 2006 and 2007, with values increasing by well over 50%. Last year, there were nearly \$8.5bn worth of deals in Romania. In 2003, the deal value was just \$550m.

Q How do you see the market developing over five years?

RS I think it will become more aligned with the world economy. In many respects, Romania is atypical. In the 20 years that it has been a capitalist state, it has remained decoupled from the economic cycles we've seen elsewhere.

This is partly because it went unnoticed for so long by international investors and had little access to international finance so has, until recently, developed along its own path. The country has seen rapid

change and growth over the years. But this won't last for ever. There will be a downturn at some point in the future – and Romania's businesses need to be prepared for that eventuality.

Q Which sectors are currently most active for M&A and why?

RS There has been a real estate frenzy in Romania during the past three to four years – it's a very important part of Romania's M&A. Of the 14 transactions in excess of \$100m last year, 10 were in real estate. There is a lot of interest among foreign investors in commercial property, particularly Austrian investors such as Immoeast. There was a bit of a lull at the beginning of this year but activity has started picking up again – we recently saw two deals by Deutsche Bank and DEGI signed, each worth around €500m.

A number of other sectors are outstripping Romania's high growth rates. With so much demand for new retail, commercial and residential property, construction materials is a particularly attractive market for private equity investors.

Enterprise Investors' recent investment in concrete specialist Macon Deva is a case in point. Financial services is another popular area as disposable incomes increase and product penetration rates

“We've seen a snowball effect as the market has gained momentum and Romania has become one of the fastest growing economies in the region”

“Romania is now reaching a point where it needs a second generation of business owners to come in. The country was a land of opportunity in the early 1990s, leading to the creation of many Romanian high net worth individuals with portfolios of diverse businesses. Many of them now wish to focus and sell off non-core assets”

rise in areas such as insurance and savings. Pharmaceuticals has been another interesting area in recent times – Advent International has acquired two Romanian pharmaceuticals businesses recently, Terapia and LaborMed.

The Romanian population is learning to become consumers, so any product that is driven by an increasingly affluent lifestyle will attract attention. The \$460m acquisition of sweets manufacturer Kandia Excellent by Cadbury Schweppes last year is just one example of what is happening.

Q Even so, private equity activity has been fairly limited to date in Romania. How do you think that will change?

RS We will undoubtedly see an increase in private equity activity. There are already a lot of firms interested in Romania, but the problem is that, especially for the larger players, there are not yet enough targets for them to acquire. There are very few \$100m-plus deals in the market. Until there are, I think we may see some firms targeting smaller deals of, say, \$50m instead.

Private equity firms will have an important role to play in Romania in building businesses of scale by consolidating industries and, as a result, creating further deal flow for firms at the very large end of the deal spectrum.

Q Where will most opportunities for buyers come from?

RS Romania is now reaching a point where it needs a second generation of business owners to come through. The country was a land of opportunity in the early 1990s when entrepreneurs were able to acquire assets cheaply in a poor condition, with little or no competition. This led to the creation of many Romanian high net worth individuals with portfolios made up of diverse businesses. Many of them now wish to focus their activities and sell off non-core assets. These people are seeing an opportunity to cash out now before they are faced with the threat of competing against more efficient, experienced and better resourced strategic players.

Many are also reaching retirement age and are facing issues of succession. Many of them sent their children to good quality international management and business schools, and many are now returning to take the helm at family businesses. With their experience, they are able to modernise and implement international best practice, building strong companies as a result. We will see a series of deals, both now and in the future, as the entrepreneur-run businesses of the 1990s evolve into traditional corporates either by disposal or generation shift to their children.

Radu Stoicoviciu

Radu Stoicoviciu is Partner and leader of the Corporate Finance Services in Romania, having extensive knowledge of privatisation, project finance, mergers and acquisitions and valuations.

In his 16 years spent with PwC Romania, he has assisted clients operating in a variety of industries with feasibility studies, finance raising and valuations, as well as M&A negotiations on both the buy- and sell-side. Radu acted as project manager for the lead advisory sell-side privatisation mandate of Electrica Muntenia Sud (an electricity distribution company) which was successfully sold to ENEL for more than €820m.

He led the selling process of Artima (a supermarket chain controlled by Enterprise Investors) to Carrefour for €55m. He assisted Resource International to acquire Constanta Shipyard (the largest Romanian shipyard). Radu was also a member of the team advising Fadesa to dispose of Diana Forest (a Romanian wooden products manufacturer) to Barlinek.

3. Increasing consumerism in Russia will drive M&A

M&A activity is picking up fast among Russia's huge number of medium-sized businesses – they are consolidating fragmented industries to scale up and exploit rapidly growing demand for their products and services

Key contact: michael.knoll@ru.pwc.com



“Companies have grown quickly and many are now recognising the need to upgrade both their corporate organisation and infrastructure in order to improve transparency and governance, which will allow them to be able to attract necessary expansion capital and compete on global markets”

Cherie Hunt, PwC Partner

Multi-billion dollar mega-deals in Russia tend to dominate the headlines, but the real story is the increasing activity in the mid-market. Overall M&A value in Russia rose by 61% to reach \$179bn in 2007, more than three times the \$53bn value registered in 2005.

Three large deals – the three-way RUSAL-SUAL-Glencore merger, which created a \$30bn aluminium giant, followed by its \$15.7bn acquisition of a minority stake in Norilsk Nickel; the \$31bn Yukos auctions; and the \$20bn sell-off of generating assets by Unified Energy System – account for more than half of activity by value in 2007. Yet M&A was brisk in deal sizes well below this level: 71% of deals in 2007 were below \$100m and 33% were between \$50m and \$499m.

Mid-market deals are starting to come into their own as momentum builds around Russia’s transforming economy. There are currently strong drivers for activity in the lower and mid-market segments, meaning that we will see much more activity during the next two to three years in these deal ranges.

Mid-market companies will need to scale up

Companies in the mid-market are facing much greater competitive

pressures than in the past, and are starting to turn to M&A as a powerful tool for value creation. As the Russian economy matures and larger players develop, mid-sized companies are finding that they need to build scale to compete effectively. They need to invest in production, marketing and sales to remain competitive in a rapidly growing market, leading some owners to conclude that remaining independent is no longer viable.

Many small local players have already developed into regional ones and are now looking to become national businesses. With many industries still highly fragmented, consolidation is an attractive growth strategy. For instance, one of Russia’s largest retailers, X5, has a market share of around 5% and is now acquiring local chains to exploit growing consumer demand and benefit from synergies and economies of scale.

Some of the most active sectors will be those capitalising on the growth in disposable incomes among Russia’s vast population. Consumer goods, retail and financial services are all set to be hot areas in the next few years. Russia saw the highest growth in consumer spending of all CEE countries between 2002 and 2006, registering a 106% increase¹. Retail

saw year-on-year growth in 2007 of more than 15% – double the country’s real GDP growth of 7.5%².

The food and beverage sub-sectors are currently experiencing high levels of activity as private equity and strategic buyers enter the market, attracted by such rapid growth. Lion Capital has already completed two deals in this area: number two juice producer Nidan Soki and Russian Alcohol. And foreign drinks companies such as Coca-Cola Hellenic Bottling have been looking to acquire brands as well as bottling facilities and warehouse space in Russia.

In financial services, the need for additional capital, improved technology and a desire to expand into new areas of Russia will drive M&A. A recent PricewaterhouseCoopers survey, “Financial Services in Russia”, found that 74% of respondents (from 80 Russian financial services companies) thought M&A in the sector would increase, with retail banking witnessing the most activity and the \$100m to \$499m deal range as being the most highly sought-after.

IT will be another interesting area as demand for new systems increases from Russia’s corporates. The IT market, which is growing at 25% a

¹ Mintel
² Economist Intelligence Unit



Future Trend 3: Increasing consumerism in Russia will drive M&A

Quick facts

Russian M&A and privatisation market in 2007

01 Top three inward investing countries by number of transactions:	United Kingdom, United States, Germany
02 Top three inward investing countries by value:	Italy, Germany, United Kingdom
03 Top three outward destination countries by volume:	Ukraine, Germany, Armenia
04 Top three outward destination countries by value:	Canada, Ukraine, United States
05 Average deal size of deals below \$100m:	\$27m
06 Proportion of deals below \$100m:	71%
07 Average deal size of deals over \$100m:	\$977m
08 Proportion of deals over \$100m:	29%
09 The largest transaction:	Russian Aluminium OAO – RUSAL acquired two large companies, Siberian-Urals Aluminium Co Holding OAO and Glencore International AG, with a total value of \$30bn
10 The largest privatisation:	Mechel Steel Group OAO acquired Yakutugol Co OAO (75% / 68.8%); Elgaugol OAO for a consideration of \$2.34bn

Source: PricewaterhouseCoopers

year, according to PricewaterhouseCoopers report, “Private Equity in Russia”, is extremely fragmented and gives ample scope for consolidation in all areas, but particularly retail, wholesale and implementation.

A second wave of strategic buyers is entering the market

Inbound acquisitions in Russia are no longer the preserve of multinationals; smaller overseas companies are starting to gain a toehold in the market, enticed by high growth rates, a desire to tap into one of the world’s largest consumer markets and a need to expand production capacity. Their interest is aimed squarely at the mid-market, boosting the opportunity for deals in this range to be completed.

European companies are the most actively acquisitive in the market, with increasing interest from CEE countries and Ukraine. Smaller Asian players are also coming to Russia from countries such as Japan and Korea, as are Middle Eastern investors.

The European players, in particular, may become important acquirers as their desire to establish a presence in a quickly developing market with high growth potential could be driven even more by an expectation that developed

markets will underperform because of slow growth.

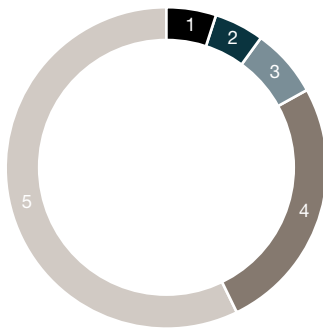
A recent PricewaterhouseCoopers survey of CEOs across the globe³ found that respondents in industrialised nations have become much more guarded about their expectations for growth over the coming year. Only 44% of Western European CEOs said they were very confident about short-term prospects, down considerably from 52% the previous year.

For sellers, the attraction of these strategic buyers will include fresh capital, an opportunity to update technology, improve know-how and quality control, access to fresh brands and best practice and perhaps access to new markets.

Private equity will be an increasingly important feature of the market

Market consolidation will be aided by the increasing participation of private equity players in the market. Russia is already home to a growing population of domestic firms, such as Troika Dialog, Delta Private Equity, Baring Vostok Capital Partners, Alfa Capital Partners and Renova Capital, many of which have raised large funds over recent times.

Share of deals by value in 2007

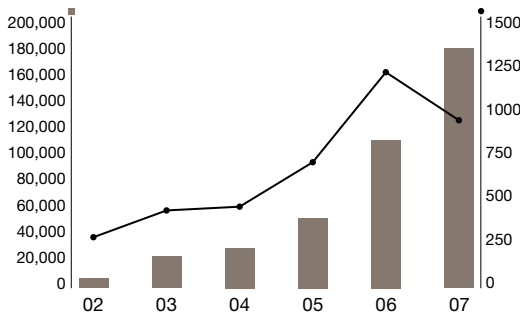


Source: PricewaterhouseCoopers

Key:

1	\$1bn+	5%
2	\$500m-\$999m	5%
3	\$250m-\$499m	7%
4	\$50m-249m	26%
5	< \$50m	57%

Russia's M&A market



Source: PricewaterhouseCoopers

Key:

	Rank value (\$m)	# of deals
2002	7,468	286
2003	23,703	436
2004	30,379	457
2005	52,517	706
2006	110,971	1,210
2007	179,349	941

“We are seeing mid-market activity across the board, but the most active areas are consumer products and retail, entertainment, IT and other services. There are a lot of consolidation opportunities in these areas”

Mark Hannye, PwC Partner

Future Trend 3:

Increasing consumerism in Russia will drive M&A

See also pages 46-47

- Mid-market eating a quarter of the pie
- Compete & Collaborate report
- Shopping for the future – Russian retail market survey
- M&A in the financial sector in Russia

These are being joined by newer local firms set up by experienced industrialists, such as Trifecta Private Equity; regional houses, such as Penta; and by international players, such as TPG, which opened an office in Moscow last year. Lion Capital is also targeting deals from its London HQ.

Most deals in Russia still go to domestic and foreign strategic players. However, private equity will start to become serious competition as more firms enter the market looking for a shelter from the global financial storm and access to high growth markets, and as they become more comfortable with Russia's unique challenges.

Their main strategy will be “buy and build” as they seek to consolidate across Russia's huge geography and many large cities. One of the key sources will be entrepreneurs looking to resolve succession issues: while many are still in their forties, a large proportion are now in their fifties and want to sell at a good time. Another good source of deal flow will be younger entrepreneurs, who are often keen to retain control of their businesses but who recognise the need for expansion capital and more sophisticated management techniques found in larger companies.

Yet private equity players and foreign strategic buyers in particular will need to tread carefully. With the exception of recently established businesses, many mid-cap companies still use tax optimisation schemes and there is often a wide variance between management and statutory reporting. Even where a company has been cleaned up, it may still have liabilities.

Before entering a deal, companies will need to understand accounting and reconciliation issues thoroughly to ensure that deal value is properly understood at the bidding phase and not destroyed after purchase. Thorough due diligence will be essential to the success of any M&A strategy in Russia, although this is not an uncommon feature in any emerging market.

“Private equity activity in Russia will more than double over the next few years. The deals we have done so far are just the tip of the iceberg – there is enormous potential in the market to buy fast-growing companies and consolidate industries and international firms are waking up to this.”

Jonathan Thornton, PwC Partner

In conversation with...

Michael Knoll, PwC Partner
e: michael.knoll@ru.pwc.com



Russia is too big to ignore

Q Why Russia now?

MK We are seeing a lot of foreign mid-tier strategics and international private equity houses now looking at Russia more seriously – they can't afford to ignore it. Strategics are primarily looking for access to Russia's vast internal market – with more than 140 million people, Russia is one of the largest and most important consumer markets in the world and demand is growing rapidly. With many European buyers facing low growth and saturation in markets closer to home, Russia presents an exciting, if more risky, expansion proposition.

Many of the international private equity firms are very bullish about Russia. Faced with a lack of new opportunities in traditional markets, they are looking for high-growth markets where competition for deals is low. In Russia, they see top line growth in many companies of between 20% and 30%, a need for expansion capital among the country's mid-market companies, the ability to source deals away from competitive auctions and the opportunity to consolidate highly fragmented markets.

Q To what extent is this optimism justified?

MK There is no doubt that Russia will offer some exceptional investment opportunities during the next few years for strategic and financial buyers. But there is an element of over-optimism, particularly among buyout houses. Many private equity firms believe that Russia is immune to the credit crunch, for example. It isn't. I see entrepreneurs on a daily basis who cannot get the loans

they need to expand. Their growth assumptions may be a little over-confident, too. Russia's economy is growing fast, but it is developing at such a rapid pace that it will mature quickly. Growth will slow down over the medium term and competition will drive down margins. As a result, they may not always achieve the 30%+ IRRs they are targeting.

Q How do you see the market developing?

MK Most deals, particularly in the mid-market, are still done by Russian companies. Given their sheer number, and closeness to and understanding of the market, they will account for a large proportion of the deals completed. But private equity and smaller foreign strategics will make significant inroads into the market, particularly in sectors such as retail and consumer goods, financial services and other services such as IT, real estate agencies and travel agents. All these areas will expand rapidly in response to demand from consumers and Russia's growing corporate landscape.

There are still risks inherent in doing deals in the market, such as the grey area of tax optimisation schemes, but some of these are starting to work through as authorities start clamping down on questionable practices.

But the economy is becoming fundamentally sound as the government takes a prudent approach to managing the vast inflow of capital from oil and other commodities by putting it into a stabilisation fund. As long as investors enter the market fully understanding the issues and research target companies thoroughly, Russia will provide a wealth of opportunities during the next few years.

Michael Knoll

Michael Knoll is a Partner in charge of the M&A (Lead Advisory) unit of the Corporate Finance department of PricewaterhouseCoopers Moscow. Michael transferred to PwC Russia on 1 October 2006. Before moving to Russia Michael worked for PricewaterhouseCoopers Switzerland for six years where he has built and led the Financial Institutions Group of the Corporate Finance department. In addition he acted as Banking Leader for PwC Advisory Switzerland. Prior to that Michael had worked for UBS in Wholesale Corporate Banking, Structured Finance and Real Estate Investment Banking both in Switzerland and abroad (Luxembourg and New York). In the last 16 years he has gained extensive national and international experience in M&A and Equity Capital Market Advisory with banks, investment management, insurance and real estate companies. Michael holds a degree in business administration (BBA) as well as an Executive MBA degree in Financial Services and Insurance from the University of St Gallen, the Vlerick Leuven Gent Management School and the University of Nyenrode. In addition, he is a Chartered Financial Analyst (CFA).

The M&A market is finally becoming truly global



In conversation with...
Chris Hemmings,
PwC Partner, Global Head
of Corporate Finance

e: chris.hemmings@uk.pwc.com

Q Global M&A values are down. How much is that to do with slowing private equity investment at the larger end?

CH By far the dominant influence in this is private equity. Buyout firms are unable to get leverage to acquire bigger value assets and so their buying activity is severely reduced. But it is also down to the fact that buyout houses are not selling because it is very much a buyer's market. Together, these two factors are having a big impact on overall M&A figures.

Corporates, on the other hand, have remained active. In fact, they now believe that, for the first time in years, they have a competitive advantage at the larger end because they do not have to raise debt for their deals. Corporates are continuing their M&A ambitions as a result of their strategic decisions if they are financially stable. Those in a weaker position will raise cash through disposals. Private equity will remain slow at the larger end for some time to come, but the corporate market will remain active.

Q We are seeing a shift in emphasis among private equity houses from developed to emerging markets. To what extent is this a permanent change in strategy?

CH There is a lot of activity in emerging markets, particularly in Central and Eastern Europe, Russia, India, China and, to a certain degree, Latin America. Many private equity players are setting up in these markets and/or being more active there. It will still be hard for them to do large deals there, but these regions are more insulated from the credit crisis than the US and Western Europe. The move into these markets is an acceleration of an existing strategy. They would have looked there anyway, but the credit crisis has forced them to go there sooner than they might otherwise have done.

The changed market conditions have made private equity firms look for new places to do deals, and to become more proactive about helping their portfolio companies become more active in emerging markets – they are building networks and intellectual property now.

Having said that, when conditions improve, we will see something of a shift back. There are some fantastic opportunities in emerging markets, but it is hard to get deals done. Firms will do a cost-benefit calculation: if you can get three deals done in a developed market for every one you complete in emerging markets, then it is obvious where you are going to focus your attention.

Q At the same time, we're seeing corporates in emerging markets increasingly acquiring Western business. To what extent are we now seeing a genuinely global M&A market?

CH We are definitely seeing more of a global M&A market, but the question is how smooth it is. Strategic buyers from markets such as India, Russia and China have cash and plenty of liquidity and they are in a strong position against private equity. But it's not straightforward for them to acquire in the West. Their appraisal of the markets and opportunities is very

“The changed market conditions have made private equity firms look for new places to do deals, but also to become more proactive about helping their portfolio companies become more active in emerging markets – they are building networks and intellectual property now”

“Corporates now have an advantage over private equity for the first time in years. They are continuing their M&A ambitions as a result of their strategic decisions if they are financially stable. Those in a weaker position will raise cash through disposals”

different from the approach in Western markets and so is the process of buying and selling. If that were not the case, there could be more deals than we are currently seeing.

Q What can sellers do to make their companies more attractive to some of these buyers?

CH There is a lack of awareness among Western vendors about how buyers from some of the emerging markets appraise opportunities. The kind of teaser you would send out in Europe, giving a brief description and EBITDA figures, does not mean anything to many Asian buyers, for example. Japanese buyers want to know the net asset position of a business. The information has to be properly structured for different buyers.

Another problem is that the decisions about M&A might be taken in a different part of the corporate structure from that in the West. So you quite often have the wrong information going to the wrong person. That is acting as a brake on investment from emerging markets. As both sides gain a greater understanding of each other, that will be worked through, but it may take some time.

Q What are buyers from emerging markets looking for?

CH Buyers in countries with large internal markets, such as Russia, want access to technologies. They also want branded goods. With brands, they are looking to bring high-value, premium brands to their own fast-growing markets. With technology, we're not necessarily talking leading-edge – just technologies that can give companies significant growth when applied to their emerging markets. So they may be buying businesses that are unloved in the West but their technology can bring significant competitive advantages.

Q To what extent will volatility in the public markets bring about a new wave of public to privates?

CH We will see an increase in public to private deals. Public company valuations tend to come off faster than private ones and we are seeing this happening now. Despite the fact that the credit crunch hit about a year ago, private company valuations have fallen only by about 5%. Couple that with the fact that private equity houses have a lot of money to invest from the large rounds of fundraising they have done in the past couple of years, and it becomes clear that public companies will become an important target for them.

Chris Hemmings

Chris Hemmings has been active in the private equity market for 20 years. In 1988 Chris returned to PricewaterhouseCoopers' then recently formed Corporate Finance department following a secondment to Doughty Hanson. He is the Global Head of Corporate Finance and the Head of European Private Equity Advisory.

UK

- Adviser to Dubai International Capital on the IBO of Tussauds
- Adviser to management on the IBO of Chancellor Care by LOC
- Adviser to management on the IBO of Volution Holdings by AAC

Germany

- Adviser to HgCapital on the IBO of Hirschmann AG
- Adviser on the IBO of FTE Automotive by HgCapital
- Adviser to HgCapital on the IBO of WET Automotive
- Adviser on the IBO of Addison Software
- Adviser to MPE on the IBO of Stabilus
- Adviser on the IBO of AP Automotive

Chris is a well respected and well known deal maker in London with an extensive network of contacts.

4. Consolidation in the electricity sector will continue apace

Continued privatisation, a need for massive investment and increased focus on diversified and renewable energy sources are acting as forces for consolidation in the electricity market across CEE and Russia

Key contact: emilian.radu@ro.pwc.com



“Years of under investment in generation and a dramatic increase in demand means there will be a shortage of electricity supply in the region by 2020 if significant amounts of money are not put into building new plants, finding new sources of energy and improving existing assets”

Emilian Radu, PwC Partner

Electricity industries across each of the countries in Central and Eastern Europe and Russia have been privatised at different rates and in different ways. Earlier entrants to the European Union are generally among the most advanced in terms of taking assets out of state hands as they have sought to meet entry criteria.

The processes have brought rich pickings for many international strategic acquirers, mainly from Western Europe, seeking to gain from the region’s increasing demand for electricity supply as their economies have grown, and to gain access to new customers.

The privatisation of Romania’s distribution companies demonstrates this clearly (see box, p29). But, as with privatisation programmes across the region and elsewhere, the Romanian government’s plans have evolved as more assets have been sold. Its intention with the three distribution companies still in state hands is now not to sell them separately but to integrate them with the country’s power transmitters and nuclear, thermal and hydroelectric generators under a holding company, with the ultimate aim of selling it to the private sector.

Poland is taking a similar approach by grouping together generators and distributors with a view to floating the two largest companies on the stock exchange.

The need to diversify energy sources will create opportunities

This state-led consolidation is a reflection of what is happening in the private sector across the region as companies attempt to increase efficiency, restructure, diversify energy sources and boost renewables – Romania’s plan, for example, is to ensure that renewable energy accounts for a third of overall power consumption by 2010.

Many of the privatisations that occurred during the past decade were in distribution, leaving some acquirers such as Germany’s EON with large numbers of customers but little generation capacity to sell them. The issue has been exacerbated by the fact that generation assets have suffered from years of under-investment; many of them are reaching closure dates and others are in need of large-scale modernisation. The generation sector requires massive investment if it is to keep pace with increasing demand, with some estimates as high as €42bn (excluding Russia) in the next few

years. Some are predicting that the region will face shortages by 2020 if drastic measures are not taken.

With rising oil and gas prices, concerns about energy security and EU legislation surrounding emissions, there is also a need among electricity suppliers to diversify their energy sources. In some countries, such as Romania, this translates into increasing capacity through nuclear power. Czech national champion CEZ has said that it will fund the construction of units 3 and 4 at nuclear reactor site Cernadova.

Where the expansion of nuclear energy is unpalatable to populations and governments, the focus is on finding new technologies to use existing sources of fuel more effectively, or on developing renewables. In Poland, for example, where there are still large coal reserves, the gasification of coal was considered unviable until the recent increases in oil and gas prices; now it is looking increasingly attractive.

Generating power from sun, wind, biomass, waste and hydroelectric plants are all options being explored. Swiss electricity company Atel, which has fast-growing electricity trading operations in Poland, recently acquired Bulgarian wind farm developer Vetrocom, which has plans to install

Electricity deals in the Russian Federation 2007

	Value of deals	% change compared with 2006		Number of deals	% change compared with 2006
Domestic	\$63.8bn		Domestic	77	
Cross-border	\$15.6bn		Cross-border	9	
Total	\$79.4bn	813	Total	86	72

Source: PricewaterhouseCoopers

Future Trend 4: Consolidation in the electricity sector will continue apace

“Concerns over energy costs and security of supply are creating M&A opportunities as the incumbents find that they need more exposure to renewable energy sources”

Olga Grygier, PwC Partner

20 wind turbine generators near the city of Kazanluk. Czech alternative energy newcomer Energy 21, owned by investment firm Natland Group, has opened three solar power plants in South Moravia in the past year.

All these factors mean that smaller players are at a distinct disadvantage. Today's electricity companies in the region need scale to be able to invest in new plants and modernise existing ones. They also need access to technology to develop new sources of power. This will prompt increasing consolidation in the industry as smaller operations look to sell and larger players seek diversification and generation capacity.

Combined heat and power plants ripe for consolidation

The move towards greener sources of energy and the EU member states' commitment to cut carbon emissions by 8% during the next few years mean that the region's combined heat and power plants are attractive assets as they provide one of the most efficient sources of energy. Many were built by

municipalities to supply electricity and heat to local areas. Some have been privatised, with local entrepreneurs among the most active acquirers, but many are still in state hands.

There are also many plants owned by industrial companies that were built to supply factories. As companies focus on core activities, a large number of these are likely to come on the market. There is a significant opportunity for local entrepreneurs and private equity firms – such as the newly established EnerCap which specialises in renewables in the region – to buy portfolios of these CHP assets and consolidate them.

Russia will see more deals as a result of privatisation

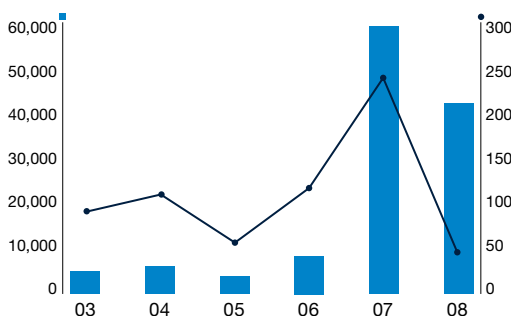
Prompted by a desperate need for modernisation, the restructuring of the Russian electricity industry is creating an enormous amount of opportunity, mainly for domestic players but also for some international ones. The value of deals in the sector increased by more than 800% last year, largely because of the reorganisation of the Unified Energy System (UES). In reality, much of the

activity was a result of purchases of additional shares by existing shareholders or share swaps rather than mainstream deal activity. The largest deal was the spin-off of the Federal Grid Company and transfer to it of government stakes in generating companies.

Under the restructuring, generation assets have been consolidated into two types of inter-regional companies: wholesale generation companies (OGKs) and territorial generation plants (TGKs). The government has sweetened the process with promises of imminent liberalisation of electricity prices, which should make these firms very profitable.

In Russia, unlike in CEE, domestic energy companies have taken most of the stakes in the privatised assets, with companies such as Gazprom buying control stakes in two OGKs and one TGK as well as minority stakes in another three TGKs. It is also the largest shareholder UES after the government. Siberian Coal Energy Company and mining giant Norilsk

CEE Utilities M&A



Key:

	Rank Value (\$m)	# of Deals
2003	5,039.5	127
2004	6,088.2	143
2005	3,847.7	98
2006	8,539.8	149
2007	59,936.5	252
2008 (H1)	42,678.8	89

Source: Thomson Reuters

See also [pages 46-47](#)

- Power Deals 2007
- Energy and Efficiency
- Electricity trading in Central and Eastern Europe

Nickel are the other two main domestic investors in the Russian electricity sector, with the latter mulling over plans to spin off its electricity assets into a holding company.

Some international strategic companies, such as EON and Enel, have acquired stakes in these businesses as foreign investors were actively welcomed in some instances for their technological and management expertise as well as capital. There could be scope for more international strategic acquirers to enter the market; the opportunities are huge in a market as vast and rapidly growing as Russia, especially as many assets are still undervalued.

Yet for many, Russia may represent too high a risk. Investors may recall the reversal of some oil and gas privatisations and conclude that electricity is too much of a strategic asset for the government. Many of those already in the market, however, will be looking at consolidating assets in the coming 18 to 24 months as the privatisation process beds down.

Future privatisations

- [Poland – 12 distribution companies. Process to start in Nov/Dec 2008](#)
- [Bulgaria – 52% of generation and 33% of distribution is still state-owned](#)
- [Slovenia – 80% of distribution is state-owned. There are intentions to initiate privatisation](#)
- [Hungary – 64% of the generation is state-owned. Privatisation of national power group MVM to restart in the near future](#)
- [Slovakia – 34% of generation is state-owned](#)

In conversation with...

Emilian Radu, PwC Partner
e: emilian.radu@ro.pwc.com



International appetite

Q You advised the Romanian government on the privatisation of EMS. What was the background to the sale?

ER Electrica Muntenia Sud was the fourth of eight regional distribution companies to be privatised, and it had some of the country's most interesting assets in the sector serving Bucharest and Ilfov. It attracted bids from Enel, RWE, CEZ, Gaz de France, Iberdrola, AES Corporation, EVN and Union Fenosa. There is much more international appetite for EMS than for the other Romanian distribution companies.

Q Why was there so much international interest this time?

ER This was a larger auction process, but it also had a lot to do with the timing. International strategics are now very interested in CEE and Romania in particular. The country's plans to double its power output and become a major exporter during the next 15 years are attractive to international companies.

Overall, it was an excellent outcome as we were able to secure a good price for it – as good as any international electricity asset. Enel was the winning bidder and paid €425m for a 67.5% stake.

Q Why was Enel in particular so keen to acquire?

ER Enel has been very active in the region in the past few years. It had already acquired 66% of CEE's second-largest generator Slovenské Elektrárne and majority stakes in two other Romanian distribution companies. The prize for Enel was to consolidate its position in the distribution field with the aim of acquiring generation capacity through the government's privatisation of the nuclear, hydroelectric and thermal plants in the coming years.

Q What will happen with the remaining distribution companies in Romania?

ER The government is planning to sell these as vertically integrated companies by grouping them together with power transmitters – it has seen the success of some of the international electricity companies such as Enel, EON and EDF and wants to replicate their model.

The plans need further clarification – one option may be to float parts of the businesses because one of the government's key issues with privatisation is that the energy sector remains independent to ensure security of supply.

Owners of privatised Romanian distribution companies

Distribution company	Acquirer	Stake	Deal value
Electrica Moldova	EON	51%	€68.6m
Electrica Oltenia	CEZ	51%	€151m
Electrica Banat and Electrica Dobrogea	Enel	51%	€112m
Electrica Muntenia Sud	Enel	67.5%	€425m

Source: PricewaterhouseCoopers

5. Competition between private equity firms for deals in the region will intensify

CEE has come on to the radar screens of many of the large buyout houses, which are now actively seeking deals in the region. These new entrants, coupled with the successful fundraising of local firms, mean that competition is increasing

Key contact: mike.wilder@pl.pwc.com



“Western funds are increasingly coming to CEE to shelter from the credit crunch and to search for low-hanging fruit. They believe there are opportunities to consolidate industries, professionalise businesses and benefit from higher margins. All are possible, but getting the deals in the first place may be problematic as competition is building in the market”

Viera Kucerova, PwC Partner

Private equity is reaching a tipping point in Central and Eastern Europe. After steady but slow growth in activity from the mid-1990s, there has been an explosion in the region in the past 18-24 months, particularly towards the larger end of the deal spectrum. While the number of deals has remained relatively stable, deal values are shooting up. Last year saw private equity deals more than double in value to \$2.9bn.

A small part of this has to do with businesses in the region gaining a certain critical mass as the economy develops. Deal values are naturally set to increase over the medium to longer term, and some of this may be accounted for by the devaluation of the US dollar in a region that is largely euro-denominated. But there are other forces at play and these will have a more significant impact on the structure and nature of the private equity market.

Local firms will have greater firepower

Local players are raising larger funds than ever. With extra capital at their disposal, they will have the capacity and the need to invest in larger deals. Historically, these local and regional

funds have raised relatively small funds and generally concentrated on the sub-€50m market. There was little debt available to them until recently and competition between the funds was low.

But this is changing rapidly. Last year’s fundraising figures broke the records in a big way: firms in CEE and Russia raised \$14.6bn, up from just \$3.3bn in 2006 and \$406m in 2003¹. And with continued brisk fundraising activity this year, such as the closing of Advent International’s fourth CEE fund at €1bn, still more capital looks set for the region’s private equity funds.

International firms are joining the fray

At the same time, international private equity houses are heading towards CEE. Bridgepoint and Carlyle have already established offices in Warsaw and TPG has set up in Moscow. Many other international firms are gathering resources. CVC Capital Partners, 3i, Warburg Pincus, Montagu, Lehman and Oaktree have all hired professionals specifically to originate and complete deals in the region. Even those without dedicated CEE teams are dipping their toe into the market, attracted by some of the region’s largest deals. Lion

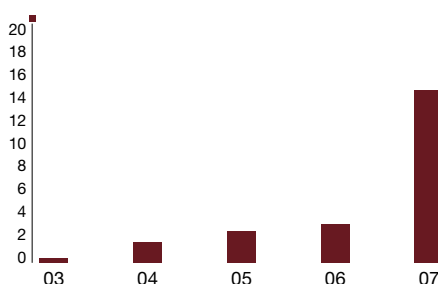
Capital has made two investments in Russia – juice producer Nidan Soki and vodka distiller Russian Alcohol. Blackstone acquired Latvian telecoms business Lattelecom last year for \$178m and Columbia Capital and M/C Venture Partners bought pan-regional telecoms company GTS Central Europe in 2007.

The credit crunch and its effects on debt provision in more developed markets are undoubtedly part of the reason for this move eastwards. CEE, by contrast, is seeing less of a fallout as local banks have little or no exposure to international markets and some foreign lenders will look to diversify their portfolio to growing emerging markets.

Yet this is more than a temporary phenomenon. CEE will see much more activity in the longer term from international private equity firms. They are facing ever-intensifying competition in the traditional markets of the US and Western Europe, where economic growth is slowing and firms are having to work ever harder to add value to their investments. They are also getting much more comfortable with the opportunities CEE has to offer: high-growth markets supported by increasing economic and political stability.

Private equity fundraising CEE/Russia

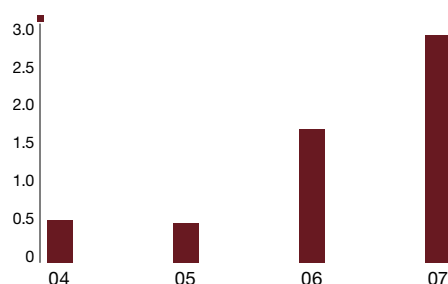
Amount (\$bn)



Source: Emerging Markets Private Equity Association

Value of private equity deals in CEE

Equity value only (€bn), excluding Russia



Source: EVCA/Thomson/PwC/PEREP_Analytics

1 Emerging Markets Private Equity Association

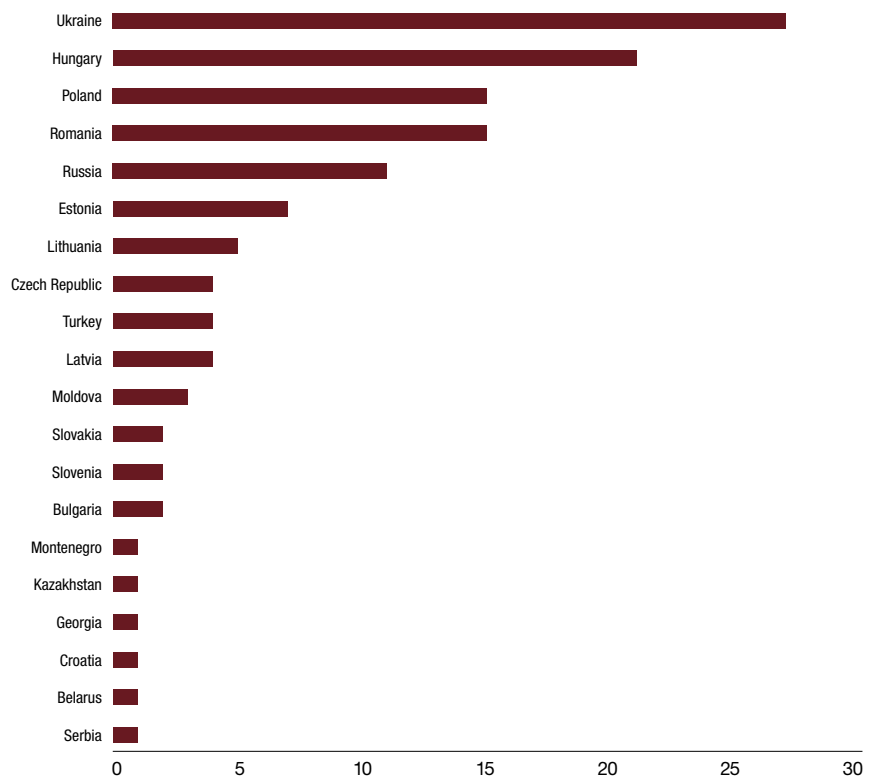
Future Trend 5:
Competition between private equity firms for deals in the region will intensify

Competition for deals will increase

There are still plenty of opportunities for private equity deals in the region, mainly in the form of entrepreneurs seeking to cash in and find successors for the businesses they have built up during the past 10 to 15 years. But competition will increase, particularly for deals of around €100m, where many of the larger local players and international firms see their sweet spot, but where deal flow is thin. This is an area where strategic buyers will be more active, too.

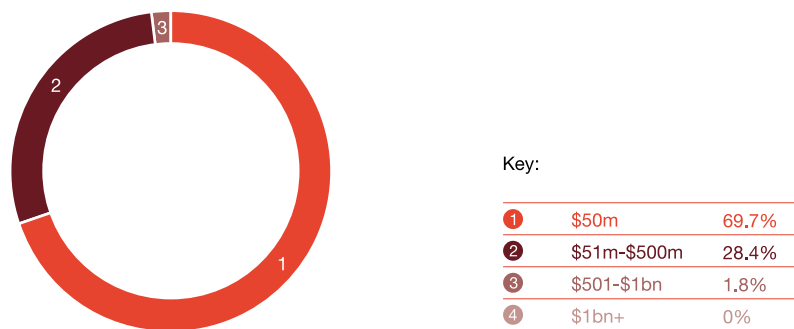
Auctions will become a more prominent feature of the market, although proprietary deals will still be there for the taking, provided that buyout houses take the right approach: in CEE, long-term personal relationships and the ability to speak the local language are still highly important. For this reason, local firms and those with established networks will have a distinct advantage. Newcomers will need to work quickly to establish a rapport with entrepreneurs and local advisers if they are to succeed in getting the best deals.

Volume of private equity deals in Eastern Europe 2006 and 2007



Source: EVCA

CEE (excluding Russia) buy outs in 2007, split by investment size



Source: PEREP_Analytics

- Shelter from the storm:
Private equity investment in Russia

“Too many private equity houses are setting their investment sweet spot at the €100m-plus mark rather than considering smaller deals or consolidation platforms. This may keep sellers happy, but it increases auction competition for these deals and may leave management teams with undeployed capital”

Tomas Horáček, PwC Czech Republic

Firms without an established presence or dedicated CEE resources will find the market harder to crack. They will generally have access only to deals intermediated by the international deal brokers in what will be highly competitive processes, eroding one of the advantages of investing in CEE.

They may have some success in taking public companies private because the research involved in identifying suitable targets tends to be more straightforward. But these are by no means easy deals to complete. There have been some public to privates, such as Advent International's acquisition of pharmaceuticals business Terapia in 2003, but there are, as yet, no established frameworks for this type of deal. Those with an in-depth knowledge of individual markets – the local funds and firms with an established presence – are again likely to be most successful in this area.

Secondary buyouts, which are increasing as a proportion of overall deals as the market matures, may be one area in which they can gain access to CEE companies. Secondary buyout activity is already present among local firms, such as Enterprise Investors' sale of healthcare company Medycyna Rodzinna to Mid-Europa last year, but there will be room for international players to enter the market.

Much of the value to be gained from professionalising, modernising and increasing efficiency in these companies will already have been extracted and so firms will need to find new angles to generate superior returns.

The private equity frontier will shift

As competition intensifies in markets such as Poland and Romania, more knowledgeable and experienced investors in the region will start looking for deals in less developed markets.

A number of firms are already eyeing opportunities in Ukraine – Advent recently established an office in Kiev, for example – attracted by its large population, its recent entry into the World Trade Organisation and, vitally, the need among its businesses to modernise. Other established firms, such as Penta Investments, are actively looking for deals outside their traditional geographic region of post-accession countries.

Companies that establish a reputation and networks in these countries early on will have a first-mover advantage as the private equity frontier shifts eastwards and southwards.

Recent fundraising

Firm	Fund	Value (€m)	Status	Date
Advent International	ACEE IV	1,000	closed	Apr 08
BaltCap	BaltCap Private Equity Fund	58	first closing	Dec 07
Mid Europa	Mid Europa Fund III	1,500	closed	Oct 07
ALPHA Associates	ALPHA CEE II	309	closed	Oct 07
Pamplona	Pamplona Capital Partners II	1,300	first closing	Sep 07
Darby Overseas Investments	Darby Converging Europe Mezzanine Fund	313	closed	Aug 07
The Riverside Company	Riverside Europe Fund III	315	closed	Jul 07
Krokus	Nova Polonia Natexis II	100	closed	Jun 07

Source: PricewaterhouseCoopers

6. Central Asia and the Caucasus will see increasing foreign investment

Rich in minerals and energy resources, Central Asia and the Caucasus are in an enviable position at a time of prolonged rising oil and commodity prices. This is giving many local companies the financial liquidity and ambition to acquire domestically and overseas. Closer to home, the need for infrastructure is creating massive opportunities for investment

Key contact: vadim.khrapoun@ru.pwc.com



“The empire-building of the early post-Soviet times is now over in Kazakhstan. Companies understand the need to focus: they want to sell their non-core assets and build a professional corporate culture”

Raikhan Kozhamseitova, PwC Kazakhstan

Of all the countries in the region, Kazakhstan holds the most economic promise over the medium term. With a more developed financial system than Russia and Ukraine, it is one of the most prosperous members of the Commonwealth of Independent States – Kazakhstan accounts for 90% of the capital equity and debt markets in Central Asia and the Caucasus¹. It is also the country that has attracted most foreign direct investment in Central Asia and the Caucasus, with \$8.3bn recorded in 2007, a 34.4% increase on 2006², most of it centred on developing its oil and gas reserves and a range of extractive industries.

Kazakhstan has been hit by the global financial crisis because its banks have relied heavily in the past few years on foreign lending. GDP growth rates were more than 10% for several years until last year, but are projected to slow to between 5% and 7% in 2008. But this could well be a blip: the economy has a large scope for growth through foreign and domestic investment driven by international commodity markets.

Developing the economy and attracting foreign investment has been one of the Kazakh government’s key objectives. Central to this aim has been the creation of Samruk, a state-run holding company modelled on Singapore’s Temasec, and through which the government owns stakes in Kazakhstan’s major assets, such as KazMunaiGaz, Air Astana, Kazpost and Kazakhtelecom. As a signal to the outside world that Kazakhstan is open to foreign investors, the government chose to appoint a Western European chairman to head up Samruk in the form of ex-British Aerospace chief executive Dick Evans.

The need to exploit natural resources will drive M&A

With oil and gas as well as vast reserves of metals – the country has 20% of the world’s gold reserves, 17% of its uranium deposits, 7.6% of its zinc and 2% of its copper³ – Kazakhstan has been accumulating serious wealth, a process accelerated by today’s climate of high commodity prices. Much of that wealth will undoubtedly translate into Kazakh companies

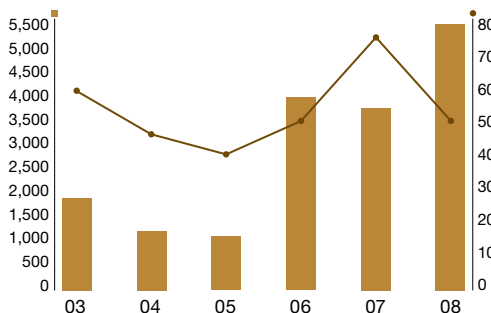
acquiring strategic assets at home and, importantly, overseas as a means of boosting their export capabilities.

The sheer spending power of some of these companies is demonstrated by the surprise \$1.65bn acquisition by KazMunaiGaz of Romanian Rompetrol, giving it a refining asset and the ability to sell oil products in Europe. KazMunaiGaz had also been eyeing a number of other overseas assets and its westward expansion is surely not finished.

There are plenty of other examples of the activity surrounding Kazakhstan’s extractive industries. The London-listed Kazakh copper producer Kazakhmys has bought a stake of more than 22% in larger domestic rival Eurasian Natural Resources Corporation (ENRC), and is also in talks with Russia’s Metalloinvest about a possible \$40bn tie-up.

Meanwhile Kazatomprom acquired a 10% stake in Westinghouse for \$540m to gain access to technologies and help it sell nuclear fuel on the world’s markets, and KazakhGold made \$152m

Central Asia M&A



Key:

	Rank value (\$m)	# of deals
2003	1,898.6	59
2004	1,219.4	46
2005	1,111.0	40
2006	3,965.0	50
2007	3,752.0	75
2008	5,492.1	50

Source: Thomson Reuters

1 Renaissance Capital
2 UNCTAD
3 Renaissance Capital



The Caucasus: untapped potential

The three countries that make up the Caucasus – Azerbaijan, Armenia and Georgia – are incredibly different nations, but they are bound together by their geography. This is likely to be their strongest asset. Sandwiched between the Black Sea, the Caspian Sea and neighbouring Russia and Turkey, the region is an important logistics hub. Transportation currently represents nearly 10% of Georgian GDP⁴. Ports and shipping are already significant sectors in the region, with Poti and Batumi on the Black Sea among the most prominent.

Rail, however, shows the most potential. As a corridor between Europe and the rapidly developing countries of Central Asia, such as Kazakhstan, rail will be a vital link as a new line serving Turkey, Georgia and Azerbaijan is due for completion in 2011.

The region's developing logistics will be an advantage, not only for trade between continents but also for the Caucasus' export market. As a mineral-rich area, with gold, copper, manganese and iron ore as well as oil in Azeri, it is experiencing rapid economic development, mainly on the back of rising commodity prices. Many of these assets are under-developed and offer huge future potential. With high GDP growth rates – Georgia's hit 9.4% in 2007⁵ – local populations are fast becoming consumers as wealth accumulation trickles down.

M&A activity remains limited in the region, but it will pick up. With business-friendly reforms, such as those in Georgia that resulted in the country coming 18th out of 178 in a league of business-friendly economies this year, while just three years ago, it ranked 112th⁶, will help boost investment confidence in the region. Middle Eastern investors are starting to look seriously at the Caucasus, as the acquisition of Georgia's Standard Bank by Abu Dhabi Group earlier this year demonstrates. Other deals of note include Swiss Multiplus Solutions' \$85m acquisition of state-owned Tbilisi Water last year and KazMunaiGaz's purchase of 50% of Batumi Oil Terminal.

“Georgia is opening up free industrial zones and developing its infrastructure – Poti, for example, is fast becoming an import and export hub for the region”

Clifford Isaac, PwC Partner

⁴ American Chamber of Commerce in Georgia
⁵ World Bank
⁶ Doing Business 2008, published by the World Bank

Future Trend 6: Central Asia and the Caucasus will see increasing foreign investment

of acquisitions in 2007, including a majority stake in Turkey's Marakand Minerals and Norox Mining, which gives it access to a mining enrichment plant in Kyrgyzstan. The drive to exploit resources is also being seen in Kazakh companies listing as they seek to raise capital for investment in developing assets. Two Kazakh companies now feature in the FTSE 100: ENRC, which floated 20% of its shares at the end of last year, raising £1.36bn to expand its four existing divisions and expand into new metals such as lead, zinc and uranium; and Kazakhmys, which listed in 2005.

Kazakh companies in the extractive sectors will also be attractive targets for foreign acquirers. Russian businesses are likely to continue

being the most active buyers, but Kazakhstan's proximity to, and links with, a number of Asian markets mean that Eastern acquirers are prevalent, with China and South Korea being the most acquisitive.

The need for infrastructure will bring in investment

In order to export its natural resources, Kazakhstan will need substantial investment in its crumbling infrastructure. As the ninth largest country in the world – roughly the size of Western Europe – transport and logistics projects will have to be large-scale. After decades of under-investment, the country is now starting to address the problem. The government has projected that \$25bn will be needed through to 2030 for

investment in transport, logistics, communications and energy supply, although most believe this will be far from enough.

This will provide ample opportunity for private investors to get involved. With similar needs in many of Kazakhstan's neighbouring countries, investors are starting to look seriously at the region as a source of good returns. Macquarie and Renaissance Capital have just joined forces to create an infrastructure fund focused on the CIS, and Middle Eastern Ithmaar Bank has formed the Ithmaar Kazyna CIS Energy Partnership with Kazyna Capital.

Clearly, one of the beneficiaries of this investment will be the construction sector, which has already received

Central Asia and Caucasus statistics at a glance

	Population, millions	2007 nominal GDP, \$bn	2007 nominal GDP, capita, \$	2010 nominal GDP, capita, \$
Azerbaijan	8.0	30.9	3,888	11,307
Armenia	3.2	8.9	2,794	5,000
Georgia	4.7	9.4	2,017	3,219
Total Caucasus	15.8	49.3	3,115	7,649
Kazakhstan	15.2	100.0	6,579	9,803
Kyrgyzstan	5.3	4.0	764	1,140
Tajikistan	6.7	2.6	394	522
Uzbekistan	27.8	19.9	716	1,120
Turkmenistan	5.1	10.5	2,059	2,368
Total Central Asia	60.0	137.1	2,283	3,359
Total CCA	75.9	186.3	2,456	4,523

Source: Renaissance Capital

Future Trend 6: Central Asia and the Caucasus will see increasing foreign investment

a boost in the past decade as the Kazakhstan government moved the country's capital city from Almaty to Astana and set about developing it lavishly, including buildings such as the Pyramid designed by Lord Foster. With the process of urbanisation taking place, other cities will see more building work, making real estate and related areas interesting investment prospects. Almaty, which remains Kazakhstan's economic centre, is seeing large amounts of construction activity.

Financial services deals will return

Before the credit crunch started to bite, Kazakhstan had an active M&A market in the banking sector, with significant interest from foreign strategic buyers looking for a toehold in this promising and fast-growing market.

The first half of 2007 saw brisk activity, with the acquisition of ATFBank by Unicredit, worth \$2.175bn, and the acquisition of a 30% stake in JSC CenterbankCredit by South Korean bank Kookmin as notable deals. The second half of the year saw an abrupt end to banking deals.

However, financial services transactions will pick up again. Faced with increased competitive pressure and shortage of accessible funds, when the foreign markets have closed or raised the cost of capital with know-how and technology enter the market, incumbents will need to sell.

Despite the M&A downturn in the sector and the resultant reduction in valuations, there are still a number of banks on the market and many more that are looking at a sale. These could be attractive assets for banks less affected by the credit crisis.

Business restructuring will create M&A opportunities

In common with Russia, the years following the fall of the Soviet Union in Kazakhstan saw asset accumulation on a large scale. Companies are now reaching a new phase: they are more mature and understand the need for focus. Some of this shift has been the result of a trend witnessed 18 to 24 months ago that saw many businesses considering an IPO.

Simply looking at a listing as an option has been a useful exercise for many as they realise they are far from ready and are now seeking to professionalise their businesses and put in place best practice. Many of those with diverse portfolios will be looking to sell non-core assets, creating a healthy deal flow in the mid-market. They are looking in particular at selling to private equity houses.

While there is currently little private equity activity in Kazakhstan, the opportunity to acquire these businesses may attract some of the more adventurous firms already active in Russia and CEE.



“IPOs were flavour of the month a couple of years ago in Kazakhstan. The problem was that companies did not really understand why they wanted to be listed, what was required for a successful listing and what would be the associated costs. The process of exploring an IPO as a possibility of raising finance has improved since then, with management now seeking to implement more professional reporting systems, and considering other opportunities, like attracting private equity funds”

Dmitry Levin, PwC Kazakhstan

Recent large deals in Central Asia

Target country	Target company	Bidder company	Seller company	Deal dom.industry	Deal value £(m)
Kazakhstan	Eurasian Natural Resources Corporation	Kazakhmys Plc	Government of Kazakhstan	Mining	1,306
Kazakhstan	Oriel Resources	Mechel OAO	shareholders	Mining	800
Kazakhstan	AES Ekibastuz and Maikuben West	Kazakhmys Plc	AES Corporation	Mining	754
Kazakhstan	Caspian Investments Resources	Mittal Investments SARL	OAO Lukoil	Energy	578
Kazakhstan	JV Kazgermunai	JSC Exploration Production KazMunaiGas	KazMunaiGaz	Energy	489
Kazakhstan	Eurasian Natural Resources Corporation Plc	Kazakhmys Plc	Vladimir Kim (private investor)	Mining	401
Kazakhstan	Limnotex Developments	VimpelCom	Crowell Investments Limited	Telecoms: Carriers	284
Uzbekistan	Uzdunrobita	Mobile TeleSystems OJSC	private investors	Telecoms: Carriers	125
Tajikistan; Kyrgyzstan	Akjilga Silver Project	Eurasia Gold Inc	state & private investors	Mining	85
Kyrgyzstan	Norox Mining Company	KazakhGold Group Limited	Oxus Resources Corporation	Mining	81

Source: Mergermarket

7. The need for growth capital will drive IPOs

International and local stock markets may be volatile at the moment, but there is still appetite among CEE and Russian companies for going public. Many businesses simply cannot wait for better conditions to access growth capital: if they delay, they will miss out on valuable growth opportunities. The IPO pipeline remains full

Key contact: alexander.sinyavsky@ru.pwc.com



“We will see many more Russian companies choosing to list locally, particularly through dual listings with London. The market needs regulatory reform to make it a truly significant financial centre, but there is political will behind this”

Alexander Sinyavsky, PwC Russia

There is no doubt that economic uncertainty and the resultant volatility on the world's major stock markets has had an effect on Central and Eastern European and Russian companies' appetite to list either domestically or overseas. Some of the larger deals to be pulled include Russia's Nitel Solar and CoalCo Development, both of which had planned a London Stock Exchange listing in the first half of this year and the second half of 2007, respectively.

Local stock exchanges may not have been quite as affected by the credit crunch and the prospect of US recession, but they have not been immune. The Warsaw Stock Exchange has been on a downward trajectory since the beginning of 2008, with the WIG Index seeing a fall of just over 26% for the first six months of the year. Most other stock exchanges in the region are down 20% to 30%. The impact on Russia's exchanges has been less dramatic, but they have still been volatile during the past year.

Yet the falls on local markets are likely to be little more than corrections over the longer term, when some of the high valuations seen in 2006 and the first half of 2007 level out to more realistic levels. These adjustments have affected IPO activity to some degree as management and/or owners find they are unable to raise as much capital as they had initially planned.

Some may be pinning their hopes on a return to bull markets – after several

years of growth, there is often a time lag between vendors' price expectations and market realities – and holding back for better times.

Local IPOs will be spurred by growth

Many companies are still deciding to float despite more difficult market conditions. Last year saw just three IPOs on the Bucharest Stock Exchange, yet in the first half of 2008 alone, nine companies went public – the most for nearly a decade. The WSE has also seen brisk activity in the first half of this year with 22 new issues. This is down on 2007, when a record 81 companies floated on the exchange over the whole year (second in the European Union only to London, which saw 99 IPOs), but it compares favourably with 2006, when 36 IPOs were completed.

In fact, based on the pipeline of deals scheduled for the second half of 2008, there are likely to be between 70 and 80 IPOs on the WSE this year. As further evidence of an appetite for listings in the region, the WSE's growth market New Connect, launched only last year, has already attracted 60 companies.

It's a similar story in Russia. While a number of companies delayed their float plans just as the credit crunch started to bite last September, leading many in the market to expect a weak final quarter for 2007, many Russian businesses still managed to raise \$8bn through IPOs.

The reason for this is clear. While IPO activity has dampened in response to market sentiment, the need for growth capital among the region's companies continues unabated. The rationale for most IPOs last year was to gain access to growth funding; the pipeline of companies looking to list shows that this is still the most popular reason to go public.

In CEE and Russia in particular, where industry consolidation is happening at breakneck speed, companies need to build scale to become competitive in their local and regional markets. If they cannot grow quickly, either through acquisition or organic growth, they will be left behind.

Despite tougher market conditions, IPOs will be an attractive option in part because other sources of capital are currently harder to come by. The debt markets will continue to be constrained by the effects of the credit crunch over the short to medium term: banks are tightening their lending criteria and offering more onerous terms at higher rates, making debt finance a less attractive source of growth capital.

Private equity will fill the gap to a certain degree, but it, too, is dependent on the availability of debt on reasonable terms. For the three months to May 2008, average equity contribution has risen from 32% to 45.5%¹ and unless firms can see extraordinary growth potential, they are unlikely to be able to increase equity ratios much further.

Future Trend 7:
The need for growth capital
will drive IPOs

“Companies looking to list have to decide which exchange suits their requirements the most. Local exchanges may be more suitable for smaller and medium-sized companies, but international listings can add significantly to a company’s prestige”

Robert Paterson, PwC Partner

As Gennady Margolit, Deputy CEO, MICEX, put it in a recent interview: “In 2008, there will be a healthy number of IPOs [in Russia]. One reason is the difficulty in attracting debt funding – for second and third tier companies, an IPO will be almost the only way to attract financing.”

The other attraction of an IPO is the ownership structure. A large number of relatively small shareholders is quite disempowered, whereas a single minority investor or bank creditor is more likely to be hard to manage. An IPO may be the best option for many companies looking for growth capital – but only as long as they understand the long-term pressures and reporting obligations they face as a public company.

WSE will increasingly become the market of choice for CEE companies

The WSE is making much of its status as one of the most developed capital markets in CEE. It is already the market

of choice for Polish issuers, but WSE is also increasingly seeking to attract companies from around CEE in an attempt to become a regional player. It has established an IPO partner initiative through which it is signing up investment banks in countries such as Belarus and Ukraine, it is the first foreign stock exchange to open a representative office in Kiev, and is undergoing a privatisation programme that should enable it to take stakes in other exchanges in the region.

Its efforts are paying off: in 2003, WSE had just one foreign listing; by June this year it had 25. Czech business AAA Auto is just one example of a recent listing on WSE, and last year saw large, multinational businesses, such as financial services company Unicredito Italiano and Austrian construction business Immoeast, choose to list their shares on WSE.

Many more foreign businesses are considering floating on WSE. Among those looking to list are Lithuania’s

aircraft leasing company Aviation Asset Management, Lithuanian aircraft maintenance company FlyLAL Technics, Austrian consumer electronics business Advanced Technology Solutions and Lithuanian pharmaceuticals company Sanitas.

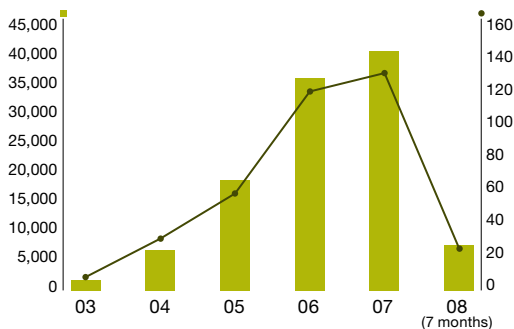
Many CEE companies that may once have considered London’s Alternative Investment Market as their best venue are now thinking more seriously about listing closer to home as the market develops further.

More Russian companies will list domestically...

Russia’s stock markets will become an increasingly attractive place to list for local companies. Historically, many firms looking to go public have gone to markets such as London for its liquidity and prestige.

But efforts by the government to make Moscow an international financial centre, although in their infancy, are starting to bear fruit. Last

CEE IPOs



Source: Thomson Reuters

Key:

	Proceeds amount (\$m)	# of issues
2003	1,706	8
2004	6,756	31
2005	18,598	58
2006	35,785	119
2007	40,280	130
2008	7,670	25

“Company owners need to consider the regulatory and governance impacts of becoming quoted. A large group of unhappy shareholders makes for a stressful AGM and frustrated equity analysts will attract a lot of media attention – all of this is a huge distraction to management”

Michelle Moore, PwC Partner

year saw an aggregate value of 43% of Russian IPOs being completed domestically through MICEX, the Moscow Stock Exchange and the Russian Trading System Stock Exchange; in 2005, the London Stock Exchange accounted for 94% of the value of IPOs by Russian companies.

There still needs to be much more reform, particularly in the area of investor protection, to attract international funds, but local investors are increasingly investing in domestic equities. With pension reform under way, growing savings and insurance industries and the increasing participation of retail investors – last year’s float of state-owned VTB bank attracted 131,000 Russian retail investors, for example – capacity in the market will expand dramatically over coming years.

We will also see a shift by sectors of Russian companies coming to market. Banking, oil and real estate have been the most active sectors to date, but

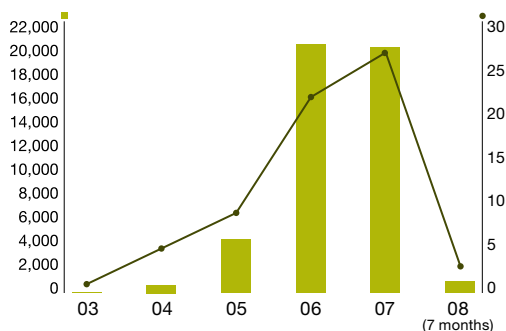
IPOs during the next 12 to 18 months are likely to reflect Russia’s increasingly diverse economy and the need for new infrastructure. Last year saw IPOs by vodka producer Synergia, pharmacy chain 36.6, retailer Dixys and Novorossiysk Sea Port. More companies in consumer products, retail, transport and logistics as well as financial services will float to gain access to growth capital to take advantage of increasing domestic demand.

...but overseas and dual listings will continue to be popular

Despite the development of local markets, larger companies will still seek to list on deeper and more liquid markets, with London as the location of choice. Russian-listed retailer Magnit floated on the LSE as well earlier this year to finance its expansion plans while metals giant Rusal is considering a listing in London, Hong Kong and/or Russia.

The London Stock Exchange is actively marketing in a number of CEE countries, with a particular push in Ukraine where, despite its stock market being the world’s fastest growing in 2007, large companies need access to deep pools of capital. Interpipe and Milkiland are two Ukrainian companies currently considering a London listing. The added advantages of prestige and increased visibility on an international level are still compelling reasons for companies to list on foreign exchanges.

CIS & Russia IPOs



Key:

	Proceeds amount (\$m)	# of issues
2003	14.4	1
2004	664.3	5
2005	4,384.8	9
2006	20,433.5	22
2007	20,231.8	27
2008	941.3	3

Source: Thomson Reuters

8. Commercial due diligence is becoming an essential part of M&A

Commercial and operational due diligence is becoming an essential part of M&A. As competition for deals increases and banks become more considered in their lending, buyers will need to have a more robust understanding of the businesses they buy and a clear plan to create value post acquisition. Rigorous due diligence is becoming a crucial tool in helping them achieve these objectives

Key contact: daniel.cappelletti@cz.pwc.com



“Commercial and operational due diligence is becoming a vital tool in the armoury of buyers, especially private equity firms. Buyers understand the advantage that this will give them in terms of winning deals and raising finance. On the sale side however the understanding of the benefits is weaker – we know of at least two large deals that will come on the market in Q4 2008 which are not underpinned by thorough due diligence. Whether these deals are completed on time and for the right value is an interesting question”

Danny Cappelletti, PwC Partner, Transaction Strategy

Competition for deals is increasing, and buyers in Central and Eastern Europe can no longer rely on general market growth trends and an ability to cut fat to make their acquisitions successful. They must come to the market with a finely tuned strategy, knowing what they want from their acquisitions and how they are going to achieve it. This has to be validated and clearly understood by acquisition finance houses.

Commercial and operational due diligence is therefore becoming a key element in deal-making and financing documentation. In an increasingly competitive environment, buyers need to know the drivers of a business's performance and how it is likely to evolve over time. As wages and exchange rates rise this becomes increasingly vital – the following are some of the questions that we have supported clients to answer:

- How will demand and pricing for the businesses' output develop?
- What does the business need to do to maintain competitiveness – will it be able to compete in the face of a slowdown in some other economies and the associated targeting of CEE markets?
- How will national and EU regulation impact the business?
- Can it pass on the increased costs of raw materials and wages?

However, going forward, we expect the nature of the questions to change as key influences in the region and in the global economy shift. Examples would be that there will be more emphasis on the ability of management to adapt to rapid change, on how the ongoing consolidation of distribution networks will affect businesses, and on how a business is positioned to take advantage of fast-paced growth in nearby countries such as Russia and Ukraine.

By stress-testing these and other areas vital to a company's competitive position, buyers can not only ensure they are acquiring the right business, they can also gain valuable inputs for their strategy following the acquisition.

Commercial and operational due diligence also helps win deals. Rigorous research into how the company is situated in its current and future markets can be used as a means of finding or testing an angle in a deal that others might not have spotted, enabling firms to pay a higher price for a business than their competitors – but being clear that this is justified.

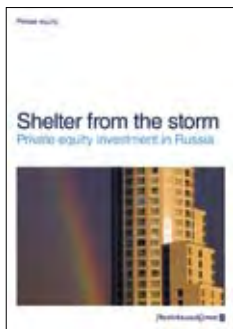
As deals get larger, the banks providing leverage will increasingly demand this kind of due diligence to ensure the key assumptions in the business plan are fully tested.

Much of the above applies specifically to private equity players. However, this is also useful for international strategic buyers. They may have detailed knowledge about the countries in which they are already present, but acquiring and operating in newer markets can present unusual challenges. Even those that have already acquired in the CEE region may gain from high-quality commercial/operational due diligence as the dynamics in each country can vary more than might be apparent from the outside.

In the Polish construction materials market, for example, the players are uniformly positioned at the value end of the market; in the Czech Republic, they operate at the mid and upper ranges. Knowing this and understanding its implications for opportunities in the respective markets is key to ensuring a successful acquisition strategy.

Finally, we also expect that vendors will increasingly use commercial vendor due diligence – although the understanding of the benefits that this brings is growing only slowly. As more deals in the region are done by buyers using sophisticated due diligence techniques, vendors will come to appreciate the control this gives them over the process.

For further insights into specific markets PwC produces a broad range of publications



Shelter from the storm
Private equity investment in Russia
This overview looks at the current state of the private equity sector in Russia. Increasingly, investors are turning to Russia as a shelter from the global financial storm. The experts expect to see the existing volume of private equity investments in Russian companies more than double over the next three years. Russian private equity houses will also become more active. More foreign money, bigger deals, better access to debt funding and more IPO exit possibilities.



Emerging Trends in Real Estate in Europe
A joint undertaking of the Urban Land Institute (ULI) and PricewaterhouseCoopers, Emerging Trends in Real Estate® Europe is a trends and forecast publication now in its fifth edition. It provides an outlook on European real estate investment and development trends, real estate finance and capital markets, property sectors, metropolitan areas, and other real estate issues. The researchers personally interviewed over 210 individuals, and survey responses were received from 277 individuals.



Power Deals
2008 Annual Review
This survey monitors the development in the power utilities sector in 2007. The year 2007 saw a continued remarkable expansion in the total number and value of deals in the sector worldwide. A 25% increase put the total power deal value of US\$372.5bn nearly nine times above the US\$43bn recorded just four years earlier in 2003. There were fewer mega-deals, reflecting the complexity of getting really huge deals over the political and regulatory hurdles, but this was more than compensated by a rise in mid-size deal numbers. There was no clear evidence of a fall-off in deal activity in the second half of the year as the credit crisis broke.



Flying High: Aerospace & Defence M&A
The latest edition of Flying High covers a review of M&A activity and key trends within the global aerospace and defence sector. Last year's review of M&A activity concluded that the total value of disclosed transactions in the sector in 2006 was comfortably the highest since 2000. Meanwhile 2007 saw disclosed transactions totalling nearly \$31bn, confirming our view that the industry remains strong despite recent downturns in other sectors.



Forging ahead – M&A in the global metals industry
The fourth edition of Forging Ahead, a global publication and summary of M&A activity in the metals sector in 2007, shows that deal-making in the industry has soared to unprecedented levels. This year's issue also includes a discussion of the key differences in the opinions of chief executives in the metals industry and those in all industries, based on data drawn from the PwC 11th Annual Global CEO Survey; and an analysis of how the regulation of carbon emissions is likely to affect metals companies.



Mergers & Acquisitions in the Financial Sector in Russia
This survey provides information about M&A activity and deal drivers in the financial sector in Russia in 2007. Measured by dollar volume, M&A activity in 2007 in Russia rose 61% on 2006, registering an estimated \$179bn. However, the estimated average size of deals in 2007 jumped 107%, from \$92m to \$190m. Greater competition drove consolidation in numerous industries. Russian firms sought vertical as well as horizontal integration.



Technology M&A Insights 2008

The 2008 edition of Technology M&A Insights provides an overview of global M&A activity in the technology sector during 2007, with analysis and comment on the market's principal trends, driving forces and outlook for 2008.



Energy and efficiency

In this report we examine the sector's thinking about the "big leap forward" that needs to be made if the sector is to address the immense challenges posed by security of supply and climate change. We found a sector that recognised the need for change but remained hesitant about when and how it could be achieved against a background of continuing regulatory uncertainty. We find huge increases in the extent to which renewable and nuclear power are at the top of company agendas. We find an industry that believes that technological advances can take us into a new era of energy efficiency.



Electricity Trading in CEE

This survey analyses regulatory, administrative and information-related impediments to electricity trading in the following seven countries of that region: Austria, Czech Republic, Germany, Hungary, Slovakia, Slovenia and Poland. Each of these countries has implemented a national energy market system which differs from the neighbouring countries. To connect them together to one market, different obstacles have to be remedied. PricewaterhouseCoopers started a survey to illustrate the different barriers.



Media M&A Insights 2008

The 2008 edition of Media M&A Insights provides an overview of European M&A activity in the media industry throughout 2007 and outlines our thoughts for 2008 and beyond.



Mid-market eating a quarter of the pie

This report on Russia's M&A market in 2007 shows that M&A values have grown 61% on the previous year, bringing the year's total deal value to \$179bn. The number of deals year-on-year actually fell by 22%, from 1,210 in 2006 to 941 in 2007. Major mergers and acquisitions and also large-scale IPO's continued to make the headlines, but 2007 was also a good year for mid-sized business. Deals worth under \$50m made up 57% of all M&A activity. The main factors driving the increase in the number of deals in the mid-market are tougher market competition.



Compete and Collaborate

This year's 11th Annual Global CEO Survey examines how CEOs perceive the business environment in which they are operating, and how an increasingly connected world affects the way their companies function and achieve success.



Telecoms M&A Insights 2008

In this edition we have expanded our coverage from an exclusive focus on Europe to include major telecommunications deals in all regions of the world. The paper provides an overview of M&A in the global telecommunications sector during 2007, with analysis and comment on the market's principal trends, driving forces and outlook for 2008.



Russian Retail Market Survey

Globally, the retail sector's strategic focus is moving towards the emerging economies and expanding consumer markets of Asia, Central & Eastern Europe, Russia and other CIS countries. The development of modern retailing in these markets and growing local disposable income offer new opportunities for growth as well as the possibility of global sourcing and offshoring. The Russian retail sector has experienced enormous growth in recent years, driven by the growing purchasing power of Russian consumers, a trend that is expected to continue in the near term. In Russia, growth has been experienced in every segment from discount to luxury. Consumers' increasing maturity and sophistication have stimulated the luxury sector in particular; Russia is currently the fastest growing market for luxury goods. While there is still room for further penetration through modern retail formats and brands and huge potential for growth, companies in Russia face a number of challenges.

How to order your copy

Please contact:

email: pavel.curda@cz.pwc.com
phone: +420 251 151 218

Key contacts

Country Leaders

CEE Advisory Regional Leader

Mark Okes-Voysey
okes-voysey.mark@ru.pwc.com
+7 495 232 5713

Baltics

Teet Tender
teet.tender@ee.pwc.com
+372 614 1800

Bulgaria/Bosnia/Slovenia/Croatia

Bojidar Neitchev
bojidar.neitchev@bg.pwc.com
+359 2 93 55 288

Czech Republic

Jiri Moser
jiri.moser@cz.pwc.com
+420 251 152 048

Georgia/Armenia/Azerbaijan

Clifford Isaak
clifford.isaak@ge.pwc.com
+995 32 50 80 61

Hungary

David Wake
david.wake@hu.pwc.com
+36 1 461 9514

Kazakhstan/Central Asia

Vadim Khrapoun
vadim.khrapoun@ru.pwc.com
+7 495 232 5709

Macedonia/Albania

Laura Qorlaze
laura.qorlaze@al.pwc.com
+355 4 242 254 / 280 423

Poland

Olga Grygier
olga.grygier@pl.pwc.com
+48 22 523 4214

Romania

Emilian Radu
emilian.radu@ro.pwc.com
+40 21 202 8610

Russia

Bob Gruman
robert.gruman@ru.pwc.com
+7 495 232 5725

Serbia/Montenegro

Tania Gligorevic
tanja.gligorevic@yu.pwc.com
+381 11 33 02 100

Slovakia

Matt Pottle
matt.pottle@sk.pwc.com
+4212 59350 402

Ukraine

Nilesh Lad
nilesh.lad@ua.pwc.com
+380 444 906 777

Transactions

Transactions Leader

Financial Due Diligence

Mike Wilder
mike.wilder@pl.pwc.com
+48 22 523 4413

Mergers & Acquisitions

Chris Butters
chris.butters@cz.pwc.com
+420 251 151 203

Commercial/Strategic

Due Diligence

Danny Cappelletti
daniel.cappelletti@cz.pwc.com
+420 251 151 333

Project Finance & Infrastructure

Nick Allen
nick.allen@cz.pwc.com
+420 251 151 330

Capital Markets

Alexander Sinyavski
alexander.sinyavski@ru.pwc.com
+7 495 232 5469

Valuation

Tibor Almassy
tibor.almassy@hu.pwc.com
+36 1 461 9644

Dispute/Forensic Analysis

Roger Stanley
roger.stanely@ru.pwc.com
+7 495 232 5420

Performance Improvement Consultancy

Performance Improvement

Consultancy Leader

Bob Gruman
robert.gruman@ru.pwc.com
+7 495 232 5725

People

John Wynn
john.wynn@hu.pwc.com
+44 7802 948 447

Technology

Philip Gudgeon
philip.gudgeon@ru.pwc.com
+7 495 232 5434

Operations and Restructuring

Rafal Krasnodebski
rafal.krasnodebski@pl.pwc.com
+48 22 523 4498

Governance, Risk and Compliance

Michelle Moore
michelle.moore@ru.pwc.com
+7 495 967 6150

Finance and Accounting

Marc Goessi
marc.goessi@ch.pwc.com
+41 79 342 03 89

Real experience, real M&A deals in Central and Eastern Europe From Almaty to Zagreb

<p>Sale of</p>  <p>non-core business</p> <p>Lead advisor to seller</p> 	<p>Sale of 66% of SLOVENSKÉ ELEKTRÁRNE, a.s. to</p>  <p>Lead advisor to Slovak Government</p> 	<p>Disposal of 100% stake in</p>  <p>(steel materials merchant) to</p>  <p>Lead advisor to seller</p> 	<p>Acquisition of DELTAX SYSTEMS (software firm) by</p>  <p>Lead advisor to buyer</p> 	<p>Sale of 66% stake in subsidiary of</p>  <p>to a consortium of</p>  <p>Lead advisor to seller</p> 
<p>Long term lease of the enterprise formed by 3 hospitals for</p>  <p>Financial advisor to Olomouc Region</p> 	<p>100% acquisition of ARTIMA supermarkets from</p>  <p>by Carrefour Romania for €55m</p> <p>Lead advisor to seller</p> 	<p>Acquisition of a hydrocarbon exploration license in Libya by</p>  <p>Financial advisor</p> 	<p>Joining the Consortium SKANLED which is developing gas pipeline from Norway to Sweden and Denmark</p>  <p>Financial advisor</p> 	<p>Acquisition of</p>  <p>by</p>  <p>Financial advisor</p> 
<p>Acquisition of</p>  <p>by</p>  <p>Financial advisor</p> 	<p>Acquisition of Germanos Polska</p>  <p>by</p>  <p>Financial advisor</p> 	<p>Acquisition of</p>  <p>by</p>  <p>Financial advisor</p> 	<p>Acquisition of</p>  <p>by</p>  <p>Financial advisor</p> 	<p>ALBINUȚA</p> <p>Sale of Albinuta Shops (supermarket chain) by Maxima to Profi Rom Food</p> <p>Seller advised by</p> 
<p>Siemens financial services</p>  <p>Sold its Hungarian subsidiary</p> <p>to De Lage Landen</p> <p>Siemens advised by</p> 	<p> (electricity distribution & supply)</p> <p>Sale of Electrica Muntenia Sud to ENEL for €820m</p> <p>Seller advised by</p> 	<p> Sale of 99.9% of Diana Forest by Fadesa to Barlinek Poland for €23m</p> <p>Seller advised by</p> 	<p>75% stake in Megaink Digital purchased by INX Group Limited a wholly owned subsidiary of Sakata INX</p>  <p>Buyer advised by</p> 	<p>SUMMIT AUTÓ HUNGARY</p>  <p>Sold its Hungarian subsidiary to Gablini</p> <p>Summit advised by</p> 

For any information or questions relating to deals in Central Eastern Europe please call:

Chris Butters	M&A Leader	+420 602 714 492	Raikhan Kozhamseitova	Kazakhstan	+7 3272 980 448
Tomas Horacek	Czech Republic	+420 251 151 111	Tanja Gilgorevic	Serbia	+381 11 3302 100
Gennadiy Greblov	Ukraine	+380 44 490 6777	Ivailo Vatev	Bosnia	+359 2 9355 200
Bojidar Neitchev	Slovenia/Bulgaria	+359 2 9355 288	Radu Stoicoviciu	Romania	+40 21 202 8640
Geoff Upton	Poland	+48 22 523 4000	Emilian Radu	Romania	+40 21 202 8610
Michael Knoll	Russia	+7 95 967 6000	Zuzana Lachova	Slovakia	+421 259 350 111
Clifford Isaak	Georgia/Azerbaijan/ Armenia	+995 32 508061	Laura Qorlaze	Albania	+355 4 242 254
Philippe Bozier	Macedonia	+389 2 3116 638			
Ferenc Geist	Hungary	+36 1 461 9100			

PRICEWATERHOUSECOOPERS 

Contributors

Pavel Curda
Lenka Filipova
Peter Sampar

Credits

Editor: Vicky Meek
Chris Butters
Design: Bladonmore Design, London +44(0)20 7631 1155

