

# Assembling value

Third-quarter 2009 industrial manufacturing  
mergers and acquisitions analysis

Climate change: Shifting the business environment  
beyond corporate responsibility



Welcome to the third-quarter 2009 edition of *Assembling value*, PricewaterhouseCoopers' (PwC) quarterly analysis of mergers and acquisitions (M&A) in the global industrial manufacturing industry. In addition to a detailed summary of M&A activity in the third quarter of 2009, we supplement this issue with a special report that addresses the impact prospective energy and climate policies may have on business transactions. Topics discussed include the role of cap-and-trade on climate change legislation, the response of the deal market, company brand and reputation considerations, and the interests of the growing number of environmentally aware stakeholders.

## Special Report:

# Sorting out the carbon effect on deal activity

Until recently, the impact of climate change policy on the deal market was barely on the radar of most businesses. But as national policy action on greenhouse gas (GhG) emissions begins to take shape, industrial manufacturing companies, in particular, must pay closer attention to the economic consequences of the proposed legislation when planning and executing deal strategy. They must also think about how competitors doing business in nonregulated countries could affect their businesses.

Regardless of the ultimate policy design, the fact remains that when GhGs are regulated, the cost of carbon will have a measurable impact on business transactions, from capital allocation decisions to merger and acquisition (M&A) strategy. Although significant uncertainty exists about the final format of the proposed environmental policies, constraints on GhG emissions may be imposed on businesses operating in the United States.

If implemented, a cap-and-trade system will require companies to measure and account for their GhG emissions and credits. Manufacturing companies will need to inventory their carbon footprints and learn how to manage carbon to minimize the impact of any resulting liability or maximize the value of any resulting asset. They will need to be able to identify what will be financially material and what they will need to disclose. They also will need to be able to distinguish a risk from an opportunity.

Manufacturing companies that participated in the 2009 Carbon Disclosure Project said opportunities from climate change regulation would come from the development of innovative products and technologies for climate protection and for energy and resource efficiency. Respondents cited an expected increased cost of doing business as a risk because it makes it more difficult to compete in a global economy. This view mirrors those held by respondents from the metals industry, who said the European Union's Emissions Trading System—or other policy instruments—create the possibility of carbon “leakage” because there are incentives to move production to locations where there are no constraints on carbon emissions.<sup>1</sup>

Regardless of what happens to climate change policy, many manufacturers have started to take action to minimize their

carbon footprints and capitalize on opportunities. By embarking on “no regret” initiatives—initiatives the company would want to complete regardless of whether the action is mandated—industrial manufacturing companies will be prepared to deal with possible reporting, compliance, and audit requirements relating to carbon emissions. “No regret” initiatives include voluntary company actions, such as reducing energy costs or improving process efficiencies that have the added benefit of reducing pollution.

### Will cap-and-trade be a part of climate change legislation?

On June 26, 2009, the House of Representatives approved the Waxman-Markey bill, which features a cap-and-trade program. The bill faces opposition in the Senate, where strong geopolitical concerns from both Democrats and Republicans may have a more significant impact on the bill's requirements. Additionally, the recent emphasis on US healthcare reform, along with a persistent weakness in the labor market, has shifted the focus away from climate change legislation.

As interest in climate policy wanes, the public's concern about the environment continues to grow. The Obama administration is also under pressure to offer some form of “green” legislation to the United Nations Climate Change Conference in Copenhagen, Denmark in December 2009.

Meanwhile, in September 2009, Senators John Kerry and Barbara Boxer introduced a bill that includes a cap-and-trade system that would require a 20 percent reduction from 2005 levels of emissions, compared with a 17 percent cut included in the Waxman-Markey bill.

The Environmental Protection Agency (EPA) also is taking steps toward GhG regulation. In March 2009, the EPA set in motion a rule that would require certain companies—including suppliers of fossil fuels and industrial chemicals, manufacturers of motor vehicles and engines, and other large, direct emitters—to report their GhG emissions regularly beginning in 2011. The EPA administrator signed the final Mandatory Reporting of Greenhouse Gases Rule on September 22, 2009.

<sup>1</sup> Carbon Disclosure Project 2009 S&P 500 With Industry Snapshots

The EPA's proposed endangerment finding<sup>2</sup> under the Clean Air Act ensures that legislative inaction by the Senate on a cap-and-trade bill does not preclude mandates to reduce GhGs. However, PwC believes manufacturing companies may find cap-and-trade legislation a preferable solution to the EPA regulation of GhGs under the Clean Air Act. In our view, an EPA regulation has the potential to require companies to meet specific performance standards on emission controls based on the best available technology. In contrast, a cap-and-trade system may allow participants to seek the most cost-effective measures to reduce carbon, which could lower compliance costs in aggregate.

### Climate change legislation can be a driver behind deal valuation

Although pending climate change legislation needs to be considered in any deal, it is becoming one of the drivers behind valuations—especially in heavy-emitting sectors—in anticipation of demand for alternative energy and regulation to reduce emissions. The impact of climate change legislation on the deal valuation of a company must be properly assessed during due diligence to understand future climate change compliance costs and possible benefits resulting from trading credits.

Understanding how a target's business is affected by climate change should be an integral part of an acquirer's risk management strategy and due diligence process. When deciding whether to provide financing, financial institutions have started assessing the possible effects climate change policy may have on a business. Companies looking to complete an acquisition should do the same. In more and more deals, the potential impacts of climate change legislation on earnings, cash flow, and target valuation, as well as any opportunities for cost reductions through synergies, should be thoroughly evaluated.

Furthermore, valuation is expected to be a significant issue in renewable energy deals. The valuation of renewable energy development assets can vary considerably depending on the stage of the development and likelihood of commercialization of the pipeline (e.g., wind, geothermal, biomass, or other types of generation). Companies may be

less willing to pay for assets that are in early-stage development and have not obtained the initial required consents. These factors should not be overlooked in the due diligence process and should be thoroughly assessed for valuation purposes.

### A climate change call to action

In addition to assessing the effect climate change has on valuations, companies must consider reputation, branding, and stakeholder interest. While climate change affects various companies in different ways, all organizations are affected by environmentally aware stakeholders including investors, communities, employees, and nongovernment organizations. Because the democratization of information has the ability to rapidly influence public perception of a company's brand, devising an effective strategy on climate change is essential in managing company reputation.

In addition to brand and reputational considerations, manufacturing companies also look to capitalize on economic stimulus programs. For example, appliance makers are hoping a US government rebate program will spur demand for energy-efficient household appliances, air-conditioning systems, and furnaces. Similar to the Cash-for-Clunkers automotive program, the appliance rebate program aims to stimulate consumer spending and address environmental issues.<sup>3</sup>

The challenge for industrial products companies is to anticipate how they will operate in a carbon-constrained environment by discerning whether their product inventories are right, assessing to what degree those products will be exposed to climate change regulation, and developing a least-cost compliance strategy.

To manufacturing company executives and corporate development teams, climate change is not about the science; it's about the need to appreciate how climate change regulation affects their businesses, the information they report, and the impact it may have on deal value.

<sup>2</sup> US Environmental Protection Agency, April, 2009

<sup>3</sup> First Research, Manufacturing Sector Alert, Oct. 5, 2009

## Perspective: Thoughts on deal activity in the third quarter of 2009

Although the global economy continues to be relatively weak, during the third quarter of 2009 there were some signs that the deal environment may have turned a corner. Our analysis revealed that the pace of third-quarter deal activity (measured by number and total value of deals with disclosed values of at least \$50 million) continued to exhibit the year-over-year decline of the first and second quarters of 2009. However, on a sequential basis, the third quarter's deal activity showed a marked improvement, both in terms of deal number and value, compared to the first half of 2009.

Although there have been no large deals (deals at least \$1 billion or more) for the year-to-date, there were several larger middle-market transactions (deals greater than \$500 million but less than \$1 billion). Satipel Industrial's (Brazil) \$963 million acquisition of Duratex SA (Brazil), which was announced during the second quarter of 2009, remains the largest transaction announced for the year so far.

The absence of financial investors and the complications prevalent in syndicated lending have clearly affected the level of large transactions. Interestingly, although strategic interests drive most deal activity (deals worth \$50 million or more), large deal activity (deals greater than \$1 billion) has historically been driven more by financial investor interests. For instance during 2006–2008, of the 46 large deals announced, approximately 60 percent were attributable to financial buyers. In contrast, of the 516 announced deals worth \$50 million or more that were unveiled during the same period, approximately 33 percent were attributable to financial investors.

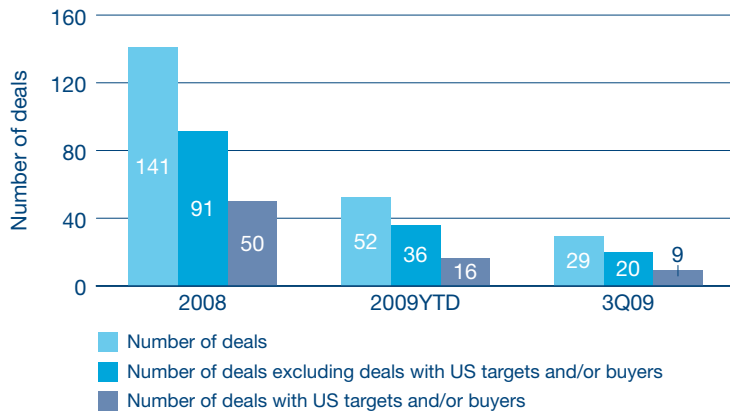
Looking forward, we continue to expect a limited amount of large deal activity in the industrial manufacturing sector. Although access to credit continues to improve and the pace of deal activity is picking up, we still believe the focus will remain on smaller deals that do not require much help from the capital markets, as is often the case in leveraged buyouts. We also believe that middle-market activity, distressed deals, and minority interest investment will continue to drive deals in the current environment. Lastly, in our opinion strategic motivation will drive activity in the near term as financial investor appetite remains suppressed and as companies acquire assets to make their businesses stronger by accessing new markets, building density in current markets; enhancing supply chains, or filling gaps in product lines.

Even as macroeconomic fundamentals begin to improve, we continue to believe that a sustained global economic recovery will be essential before we see a significant increase in industrial manufacturing deal activity. In the current environment, the companies best positioned to benefit from mergers and acquisitions will continue to be those with strong and defensible business models and favorable capital positions.

# Commentary

## Deal activity measured by number of deals

Measured by number of announced deals worth \$50 million or more



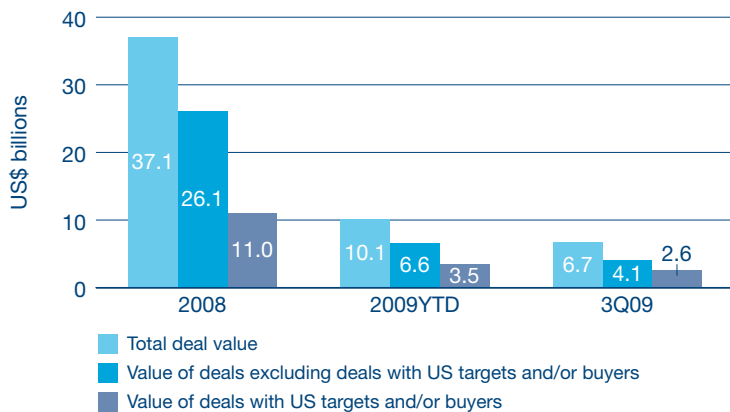
## Deal activity exhibits sequential improvement

The pace of deal activity as measured by the number of deals year-to-date continues to exhibit bearishness compared to a year ago. However, sequentially the number of deals during the third quarter improved considerably compared with the number of deals in the second quarter of 2009, increasing from 10 to 29.

In a similar trend, the total value of announced transactions worth \$50 million or more exhibited sequential improvement, increasing from \$1.8 billion in the second quarter to \$6.7 billion in the third. Year-to-date deal activity remained constrained relative to a year ago, possibly because of the lull in activity by financial investors and the persistent (although improving) weakness in the capital markets.

## Deal activity by total deal value

Measured by value of announced deals worth \$50 million or more



During the third quarter, transactions involving US targets or buyers also exhibited sequential improvement as the number and total value of deals showed relative strength. In fact, of the total number of deals involving US entities year-to-date, 56 percent were announced during the third quarter. Of the total deal value for transactions involving US entities year-to-date, 74 percent were attributable to third-quarter activity. This favorable momentum may indicate that US deal activity has turned a corner. Similarly, the number and value of deals excluding deals with US targets or buyers have also exhibited sequential improvement as 56 percent of the number of deals and 62 percent of total deal value year-to-date involving non-US entities occurred in the third quarter. We believe this trend may signal the start of a recovery in the non-US deal market as well.

## The lull in large deals continues to suppress average deal values

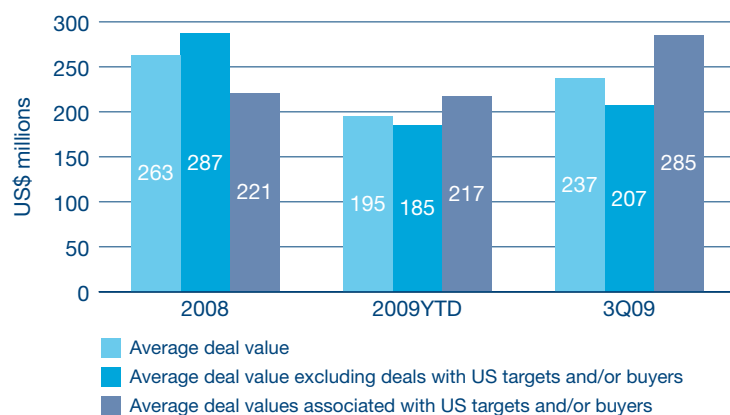
The absence of large transactions continues to drive average deal values lower. However, the trend in the third quarter of 2009 exhibited an improvement versus year-to-date levels as the number and total value of announced deals has sequentially improved. During 2008, the average deal value declined 38 percent to \$263 million. Continuing the trend, during the first half of 2009 the average deal value declined 42 percent to \$153 million compared with 2008 levels. However, the third quarter saw this trend reverse, as the average deal value increased to \$237 million driven primarily by the sequential increase in total deal values.

The average deal value for deals associated with US targets and buyers in the third quarter increased substantially to \$285 million compared with \$217 million year-to-date due to the sequential improvements in total deal value. The average deal value excluding deals with US targets and/or buyers during the third quarter was \$207 million versus \$185 million year-to-date.

Although there was a sequential increase in the number of larger middle-market transactions during the third quarter of 2009, the percentage of all announced deals remains strongly weighted toward deals equal to or less than \$500 million. Notably, a substantial percentage of transactions have undisclosed values. Of the 891 total announced deals with disclosed values in 2008, 876 (98 percent) were for deals with values equal to or less than \$500 million. Similarly, of the 504 announced deals with disclosed values year-to-date, 500 (99 percent) were for deals with values equal to or less than \$500 million. This rate continued in the third quarter when 196 (99 percent) of the 199 announced deals with disclosed values were valued equal to or less than \$500 million. We believe this trend confirms our view that smaller, less capital-intensive transactions may continue to drive near-term activity until credit markets and investor confidence are strong, rather than just improving.

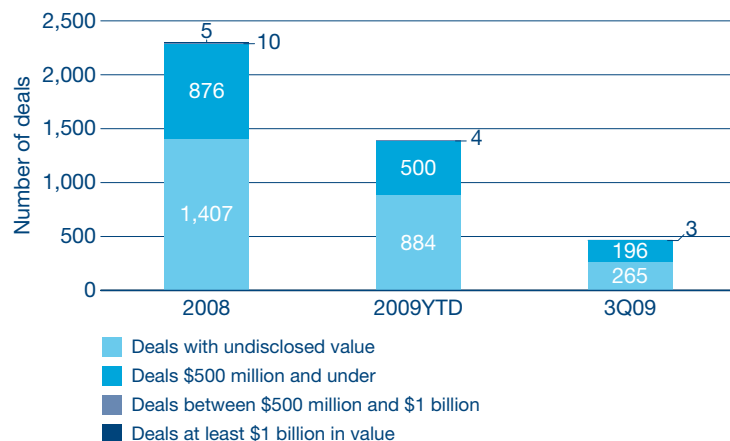
## Deal activity by average deal value

Measured by average value of total announced deals worth \$50 million or more



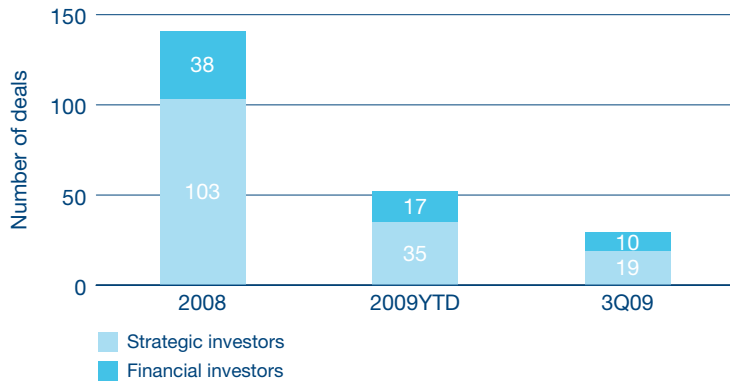
## Deal activity by number and range of deal value

Measured by number of announced deals



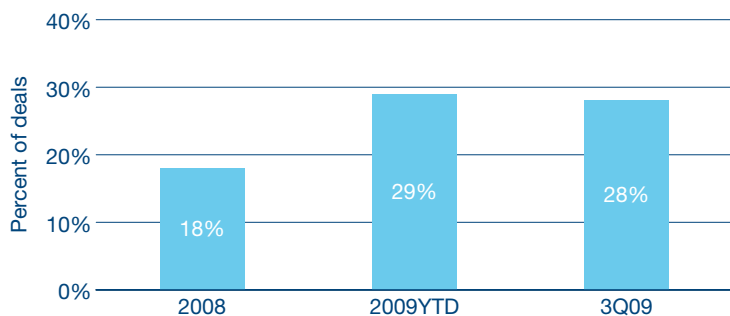
### Deal activity by investor group

Measured by number of announced deals worth \$50 million or more



### Minority stake purchases (less than 50% ownership)

Measured by number of announced deals worth \$50 million or more



### Financial investors remain cautious

As the global economy continued to struggle with credit market disruption and weak demand, financial investor activity in industrial manufacturing mergers and acquisitions remained restrained. In its most recent update, the Wall Street Journal reported that for the year-to-date, US-based private equity firms have raised \$79.9 billion across 265 private equity funds, representing a 59 percent decline from \$195 billion raised by 315 offerings during the first nine months of 2008.<sup>4</sup> Using US-based private equity firms as a global proxy, we believe cautious financial investor sentiment pervades the global private equity environment. Although the percentage of deals worth \$50 million or more associated with financial investors increased slightly in the third quarter of 2009 (34 percent) compared with year-to-date (33 percent), financial investors have not been a significant factor in driving the larger middle-market transactions that have been announced for the year so far.

The percentage of deals driven by strategic investors declined slightly in the third quarter (66 percent versus 67 percent year-to-date and 73 percent in 2008); however, strategic buyers have been the primary force supporting larger middle-market deal activity as all of the larger middle-market transactions announced year-to-date involved strategic buyers. We continue to believe that in the near-term, strategic buyers with stronger business models and capital positions will be best positioned to grow their businesses. Nonetheless, we believe many prospective strategic buyers remain focused on improving operating efficiencies, conserving cash amid liquidity concerns, and realigning strategic emphasis to meet the changing demand landscape. Still, some opportunities may be too good to turn away from for those companies willing to take some risk.

Statistics for the third quarter of 2009 indicate that buyers continue to purchase minority stakes in targets, possibly in an attempt to hedge market risks or conserve cash. During the third quarter, minority stake purchases accounted for 28 percent of announced deals compared with 18 percent in 2008. Year-to-date, minority purchases represent approximately 29 percent of all deals. Over the near term, we continue to believe minority stake purchases will account for a large portion of deals as strategic buyers manage risk and liquidity positions, and financial investors remain cautious.

<sup>4</sup> The Wall Street Journal, Private Equity Beat, October 8, 2009

## Large deals remain absent; larger middle-market deal activity driven by strategic buyer interests

For the year-to-date, large deal activity (defined as deals with a disclosed value of at least \$1 billion) remains nonexistent, as no deals were announced during the period. There were four transactions with values above the \$500 million threshold, all driven by strategic buyer interests. Announced during the second quarter of 2009, Satipel Industrial's (Brazil) \$963 million acquisition of Duratex SA (Brazil) remains the largest transaction announced so far this year. However, there was a noticeable increase in the number of larger middle-market transactions, as three were announced in the third quarter alone, compared with just one in the first half of 2009.

The largest transaction during the quarter was Precision Castparts Corp.'s (US) \$850 million acquisition of Carlton Forge Works (US), which should broaden Precision's product depth and market reach. The second-largest deal was Hitachi Group's (Japan) \$827 million acquisition of Hitachi Maxell, Ltd. (Japan) as a wholly owned subsidiary. The transaction is expected to improve operating efficiencies for both companies through integrated management, increased scale, and enhanced collaboration, among other things. Lastly, Doosan Heavy Industries & Construction's (South Korea) \$658 million acquisition of Skoda Power (Czech Republic) was likely motivated by business need, given Skoda's proprietary turbine technologies and Doosan's focus on growing its global turbine market share. Although these deals span disparate geographies and were motivated by unique circumstances, they were all attributable to strategic buyer interests.

In the near-term, considering the ongoing limited access to syndicated loans to finance large transactions, we believe strategic focus will continue to drive larger transactions as companies focus on building market share or improving operating and supply chain efficiencies. We expect the lull in large deal activity to persist; although the third quarter's sequential improvement could mark a turning point.

## Large deals in 2008

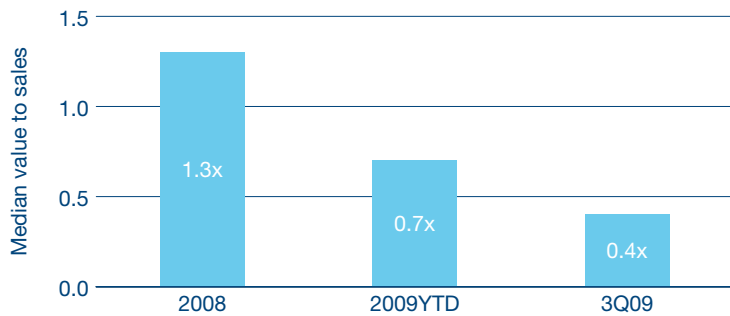
| Month announced | Target name  | Target nation  | Acquirer                   | Acquirer nation | Status    | Value of transaction in US\$ bln | Category                          |
|-----------------|--|----------------|----------------------------|-----------------|-----------|----------------------------------|-----------------------------------|
| Jun             | Graham Packaging Co LP                                 | United States  | Hicks Acquisition Co I Inc | United States   | Withdrawn | 3.20                             | Rubber & Plastic Products         |
| Jun             | Converteam Group SAS                                   | France         | Investor Group             | France          | Completed | 2.95                             | Electronic & Electrical Equipment |
| Apr             | Enodis PLC   | United Kingdom | MTW County Ltd             | United Kingdom  | Completed | 2.40                             | Industrial Machinery              |
| May             | Enodis PLC   | United Kingdom | FNI Ltd                    | United Kingdom  | Withdrawn | 2.01                             | Industrial Machinery              |
| Dec             | Jiangsu Shagang Group<br>Huaigang Special Steel Co Ltd | China          | Gaoxin Zhangtong Co Ltd    | China           | Pending   | 1.06                             | Fabricated Metal Products         |

## Deals greater than \$500 million—2009YTD

| Month announced | Target name         | Target nation  | Acquirer                                      | Acquirer nation | Status    | Value of transaction in US\$ millions | Category                          |
|-----------------|---------------------|----------------|---|-----------------|-----------|---------------------------------------|-----------------------------------|
| Jun             | Duratex SA          | Brazil         | Satipel Industrial SA                         | Brazil          | Completed | 962.51                                | Fabricated Metal Products         |
| Aug             | Carlton Forge Works | United States  | Precision Castparts Corp                      | United States   | Pending   | 850.00                                | Fabricated Metal Products         |
| Jul             | Hitachi Maxell Ltd  | Japan          | Hitachi Ltd                                   | Japan           | Pending   | 827.89                                | Electronic & Electrical Equipment |
| Sep             | Skoda Power AS      | Czech Republic | Doosan Heavy Industries & Construction Co Ltd | South Korea     | Pending   | 658.38                                | Industrial Machinery              |

### Deal valuation by median deal value to sales

Measured by announced deals worth \$50 million or more

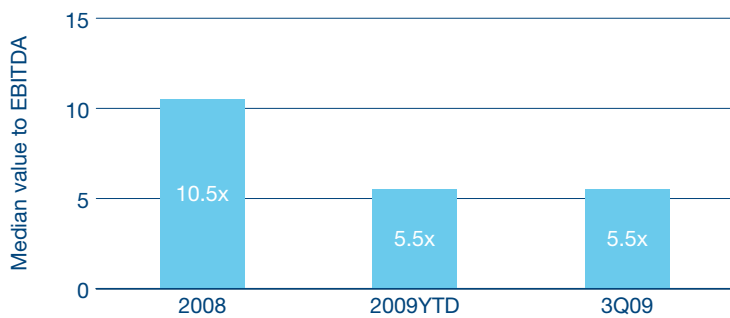


### Weakness in the deal market presents buying opportunities

Valuations for targets, represented by median deal value to sales multiples and median deal value to EBITDA multiples, remain depressed relative to historical levels. Year-to-date, the median deal value to target sales ratio was 0.7 times, reflecting a 46 percent discount to the deal value to the median sales multiples of deals announced in 2008 (1.3 times). Considering the median deal value to EBITDA multiple, which measures the amount buyers paid for each dollar of EBITDA (a proxy for cash flow), valuations also continue to be cheap relative to earlier periods. Year-to-date, the median deal value to EBITDA multiple was 5.5 times versus 10.5 times in 2008, reflecting a 48 percent discount.

### Deal valuation by median deal value to EBITDA

Measured by announced deals worth \$50 million or more

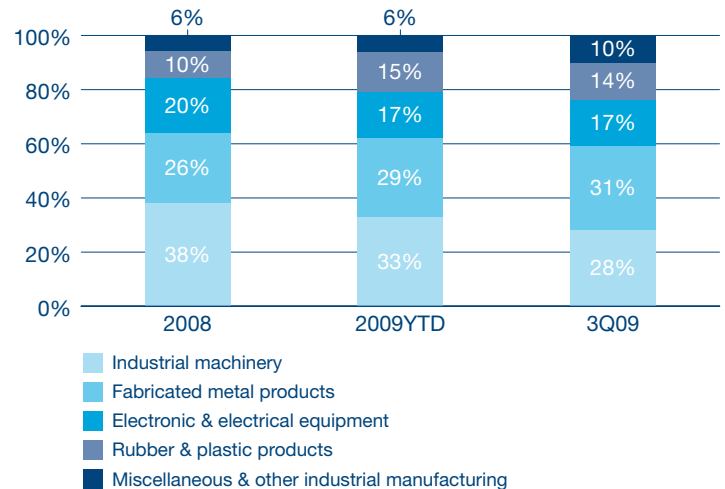


## Industrial machinery transactions drive year-to-date deal volume

For the year-to-date, 33 percent of deals (measured by volume) were for industrial machinery manufacturers compared with 38 percent in 2008. The deal weighting for fabricated metal products manufacturers increased to 29 percent from 26 percent in 2008 as the deal mix primarily shifted from electronic and electrical equipment manufacturers. From a quarterly perspective, although deals for industrial machinery manufacturers continued to fuel deal activity during the third quarter of 2009, manufacturers of fabricated metal products announced a greater portion of transactions. Although still a relatively small percentage, deals for rubber and plastic product manufacturers increased significantly to 15 percent year-to-date from 10 percent in 2008.

## Deals by industrial manufacturing category

Measured by number of announced deals worth \$50 million or more

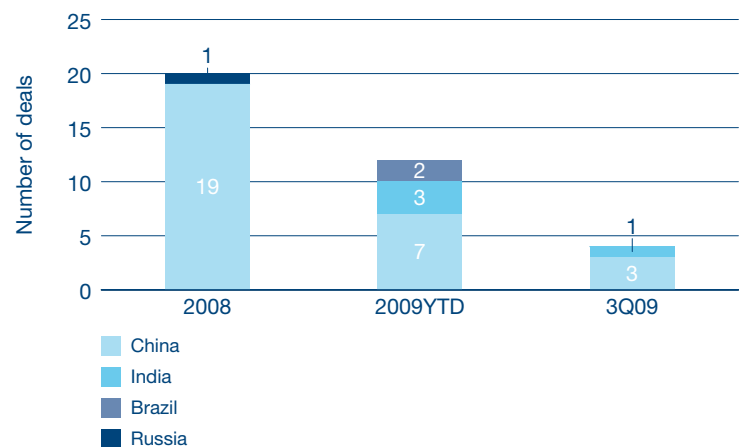


## Interest for BRIC targets continues to be driven by Chinese transactions

There have been 12 BRIC deals worth \$50 million or more so far this year, representing approximately 23 percent of total transactions. Most of the activity involves China (seven deals), with 58 percent of BRIC deals year-to-date, down from 95 percent of deals in 2008. Most deals involving Chinese targets were within-border transactions, which is consistent with trends experienced in prior periods. Year-to-date, approximately 57 percent of deals for Chinese targets were classified as within-border compared with approximately 79 percent in 2008.

## Distribution of BRIC deals by target nation

Measured by number of announced deals worth \$50 million or more



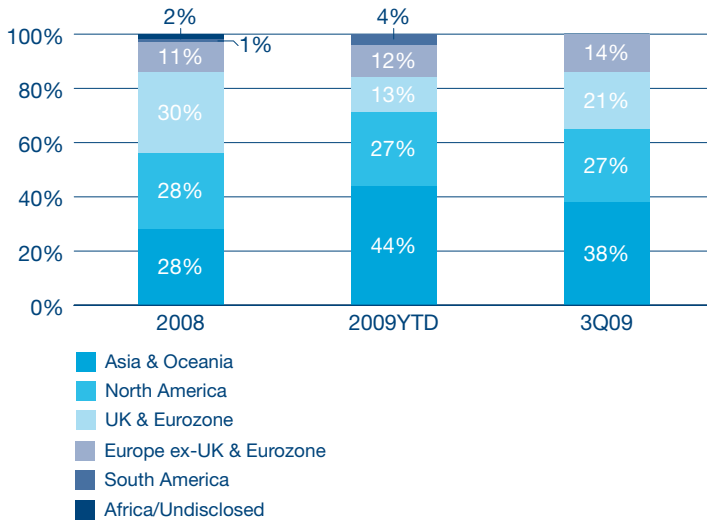
However, during the third quarter non-Chinese buyers drove a greater portion of deals for Chinese targets. Of the three deals announced for Chinese targets, two were cross-border transactions. In the first transaction, Siemens China Ltd. (a subsidiary of Germany-based Siemens AG) acquired a 6.3 percent interest in Shanghai Electric Power Generation Equipment Co. Ltd. for US\$104 million. The acquisition increases Siemens China Ltd.'s interest in the firm to 40 percent. In the second cross-border transaction, A.O. Smith, a US-based firm, agreed to purchase a majority interest in the water treatment business of Tianlong Holding Co. Ltd. of Hong Kong for \$77 million.

The sole within-border transaction involved Jiangyin Hongsheng Special Steel Com., Ltd.'s acquisition of a minority stake (20.7 percent) in Jiangsu Fasten Co. Ltd. for US\$59 million.

# Regional analysis

## Regional distribution of deals by target region

Measured by number of announced deals worth \$50 million or more



## Interest in Asia and Oceania, North American targets still strong

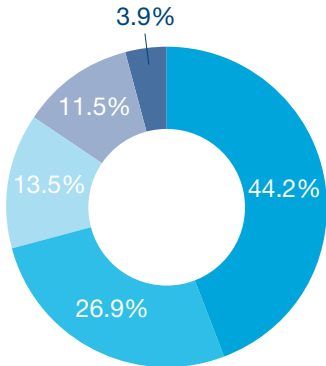
For the year-to-date, 44 percent of deals for targets (as measured by deal volume) were in the Asia and Oceania region. This compares with 28 percent in 2008. Also year-to-date, the allocation of deals for targets in North America (27 percent) remained relatively in line with that of 2008 (28 percent). During the third quarter of 2009, although interest for targets in the UK and Eurozone increased to 21 percent versus 13 percent year-to-date, the weighting is significantly lower than the 30 percent allocation experienced in 2008.

Year-to-date, most deal activity, as measured by both deal volume and value, has been driven by acquirers from Asia and Oceania, North America, and the UK and Eurozone. We believe this may be partly attributable to regulatory environments in these regions that are generally supportive of foreign investment or domestic consolidation. In addition, regionalization and globalization efforts may be stronger considerations for acquirers in these regions as they look for ways to strengthen business models and competitive positioning. Lastly, capital markets in these regions are generally stronger, relative to other regions (South America and Africa), which could make it easier to raise funds for mergers and acquisitions.

## Regional distribution of 2009 year-to-date deals

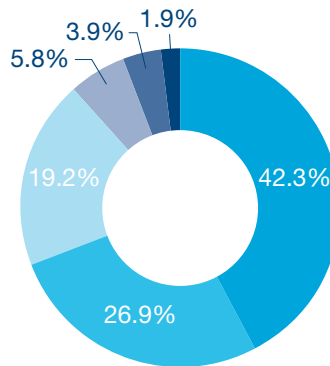
### Number of deals by target region

measured by number of announced deals worth \$50 million or more



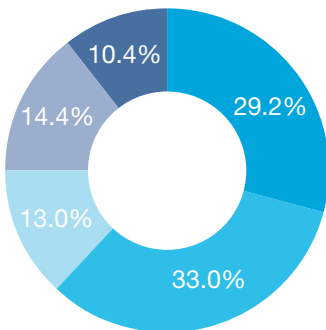
### Number of deals by acquirer region

measured by number of announced deals worth \$50 million or more



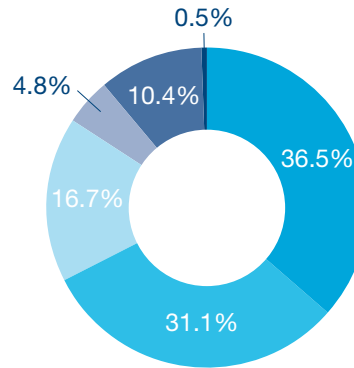
### Value of deals by target region

worth \$50 million or more



### Value of deals by acquirer region

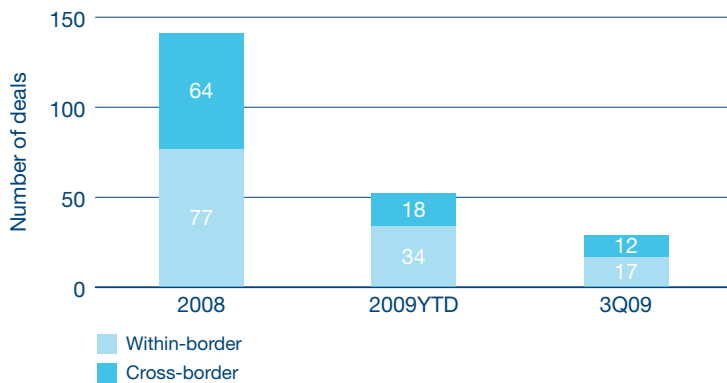
worth \$50 million or more



■ Asia & Oceania
 ■ North America
 ■ UK & Eurozone
 ■ Europe ex-UK & Eurozone
 ■ South America
 ■ Africa/Undisclosed

### Within-border vs. cross-border deals (all nations)

Measured by number of announced deals worth \$50 million or more

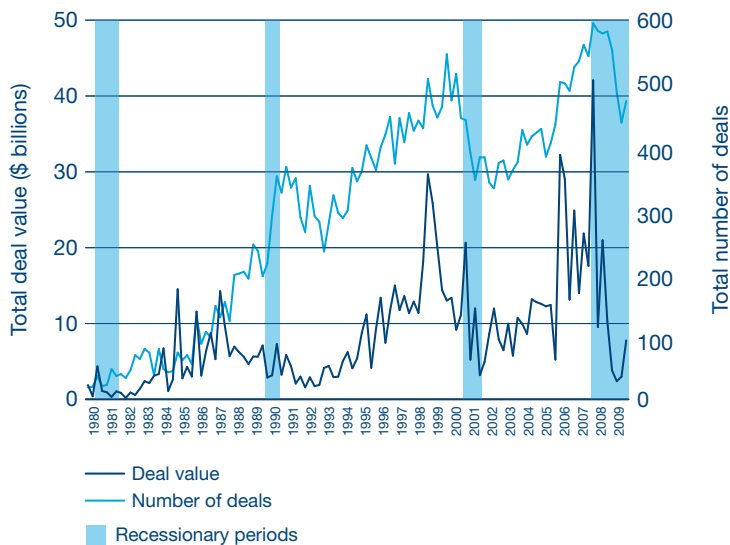


### Within-border transactions surge for the year-to-date

The proportion of deals involving within-border transactions relative to cross-border transactions has exhibited a meaningful increase, rising to 65 percent for the year-to-date from 55 percent in 2008. Several factors likely contributed to this trend, including acquirers using mergers and acquisitions to build scale and density in familiar geographies. Risk minimization strategies also play a likely role, as cross-border deals often involve greater risks than within-border. In addition, the rise of protectionist sentiment in the face of concern over the global economy may have also contributed to the jump in within-border transactions.

### Historical industrial manufacturing deal activity and the business cycle

Measured by number and value of all industrial manufacturing deals (1981–3Q09; quarterly observations)



### Was the third quarter a pivot-point for industrial manufacturing M&A activity?

The pattern for industrial manufacturing M&A activity coming out of the past three recessions indicates that the deal environment improves as the overall economy comes out of a downturn. For example, coming out of the 2001 recession, M&A activity as measured by deal values appeared to bottom near the end of the downturn. Based on this pattern, for this recession both deal volume and value appear to have reached bottom and deal activity may be about to accelerate given the sequential improvement experienced in the third quarter of 2009. Certainly, the past is not always an accurate indicator of future performance, but trends coming out of the 2001 recession, coupled with the sequential improvements in the third quarter of 2009, provide some comfort heading into 2010. With one quarter remaining in 2009, we are cautiously optimistic. Of course, the depth of this recession, the overhang created by years of significant balance sheet leveraging, and the build-up in excess capacity are significant factors that could alter how closely this recovery tracks to the recovery that followed the 2001 recession. Nonetheless, it is reasonable to believe that an improving operating environment could provide a catalyst for companies to focus less on internal initiatives like cost reduction and more on potential value-enhancing initiatives such as mergers and acquisitions.

## Preparing your company to manage carbon as an asset

Although the United States has not yet passed comprehensive climate change legislation, 23 US states are either active in cap-and-trade systems or working to design them. Numerous bills have been introduced in Congress, with the most recent narrowly approved by the House of Representatives in June 2009.

Any system that places a monetary value on carbon requires companies to consider carbon management in corporate objectives and growth plans. Whether organizations are directly or indirectly affected by comprehensive climate-change regulation, they need to take practical steps to get ready. A good first step is to ensure internal financial teams understand the financial impacts of participation in cap-and-trade systems as part of setting a clear strategy that accounts for changes in climate laws and energy policy.

### Why is this issue so important?

Climate change legislation is looming in the future. As North American companies either expand into countries where carbon is already regulated or are acquired by companies in those countries, they must take action to compete successfully in a carbon-constrained world. They must recognize that environmental factors, accounting concerns, and broader issues regarding corporate responsibility can significantly influence the value of transactions. Buyers and sellers want to know the environmental, social, ethical, and economic risks related to their transactions that can affect operating costs, compliance, and financial reporting.

### What are the required first steps to prepare for a GhG cap-and-trade system?

- It is imperative to know your carbon footprint. Companies that have not done so should identify the sources, types, and magnitude of GhG emissions they produce and compare them with those of their industry peers. As outlined in *The Greenhouse Gas Protocol*,<sup>5</sup> developing a measure of your carbon footprint includes addressing the following:
  - **Setting organizational boundaries:** This relates to determining what approach to take when accounting for emissions from joint ventures, subsidiaries, and other organizations.
  - **Setting operational boundaries:** Companies need to determine the scope of emissions they will include in their reporting. *The GhG Protocol* divides these into Scope 1 (direct emissions), Scope 2 (indirect emissions, such as from purchased electricity), and Scope 3 (other indirect emissions, accrued via employee travel, waste, contractor vehicles, product use, etc.).
  - **Determining a base year for carbon footprint reporting:** This includes determining the timing of when a company should recalculate its emissions due to business changes—e.g., acquisitions or divestitures, new calculation methodologies, etc.

- **Identifying and calculating GhG emissions:** This covers inventorying emissions sources, defining calculation methods and approaches, collecting data, selecting emissions factors, applying the calculation methods, and compiling the emissions data at the corporate level.
- **Addressing footprint quality:** Companies should address issues such as quality-control and management review, and implementation of robust processes and controls for routine data collection and compilation.
- Companies should consider conducting an assessment that includes all direct and indirect carbon emissions to understand where the best opportunities to reduce emissions may lie, and to determine whether their role in carbon trading will be that of net buyer or seller.

### Our approach

PricewaterhouseCoopers' Transaction Services group undertakes a systematic review of the risks and liabilities arising from a transaction and assesses their financial reporting impacts. This includes risks related to operational environmental performance, legal compliance, reputation, and stakeholder pressures. PwC also provides ongoing support in transaction negotiations, and in the development of systems to manage significant risks and liabilities. In addition, we advise companies on sustainability and climate change-related financial accounting and reporting issues.

<sup>5</sup> World Resources Institute and World Business Council for Sustainable Development, *The Greenhouse Gas Protocol: A Corporate Accounting and Reporting Standard* (March 2004): [www.ghgprotocol.org/files/ghgprotocol-revised.pdf](http://www.ghgprotocol.org/files/ghgprotocol-revised.pdf).

# Specialty case study: Transaction support for environmental health and safety

## Client: International industrial manufacturing business

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|              |   |
|--------------|---|
| Client issue | <p>Our client, a leading international manufacturing business, was considering the divestiture of its manufacturing operations, which included more than 60 sites worldwide. As part of their preparation, the client asked PwC to undertake an environmental review of their businesses and also assess country-specific tax and regulatory issues.</p>  |
| Approach     | <p>PricewaterhouseCoopers' team of environmental health and safety and due diligence specialists focused its environmental assessment on the removal of ozone depleting substances (ODS). An example of an ODS is the coolant used in refrigerators and freezers. The team provided the client with detailed information in the following areas:</p> <ul style="list-style-type: none"><li>• Business and financial reviews including a market analysis and revenue projections</li><li>• Information technology, controls, and related tax issues</li><li>• Environmental, health, and safety desktop reviews of all sites</li><li>• Insurance and pension reviews for all sites</li></ul> <p>The engagement team conducted 45 site visits, including visits to facilities in Thailand, the United Kingdom, the United States, Canada, China, Spain, and Australia. During each site visit, the team identified risks in relation to future EU directives on disposal of electrical equipment and removal of ozone depleting substances.</p> |
| Impact       | <p>With the analysis provided by the PwC team, the client was able to provide the appropriate and complete due diligence information to prospective purchasers and was able to successfully complete the divestiture.</p>   |

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# PricewaterhouseCoopers' industrial manufacturing experience

## Deep industrial manufacturing experience

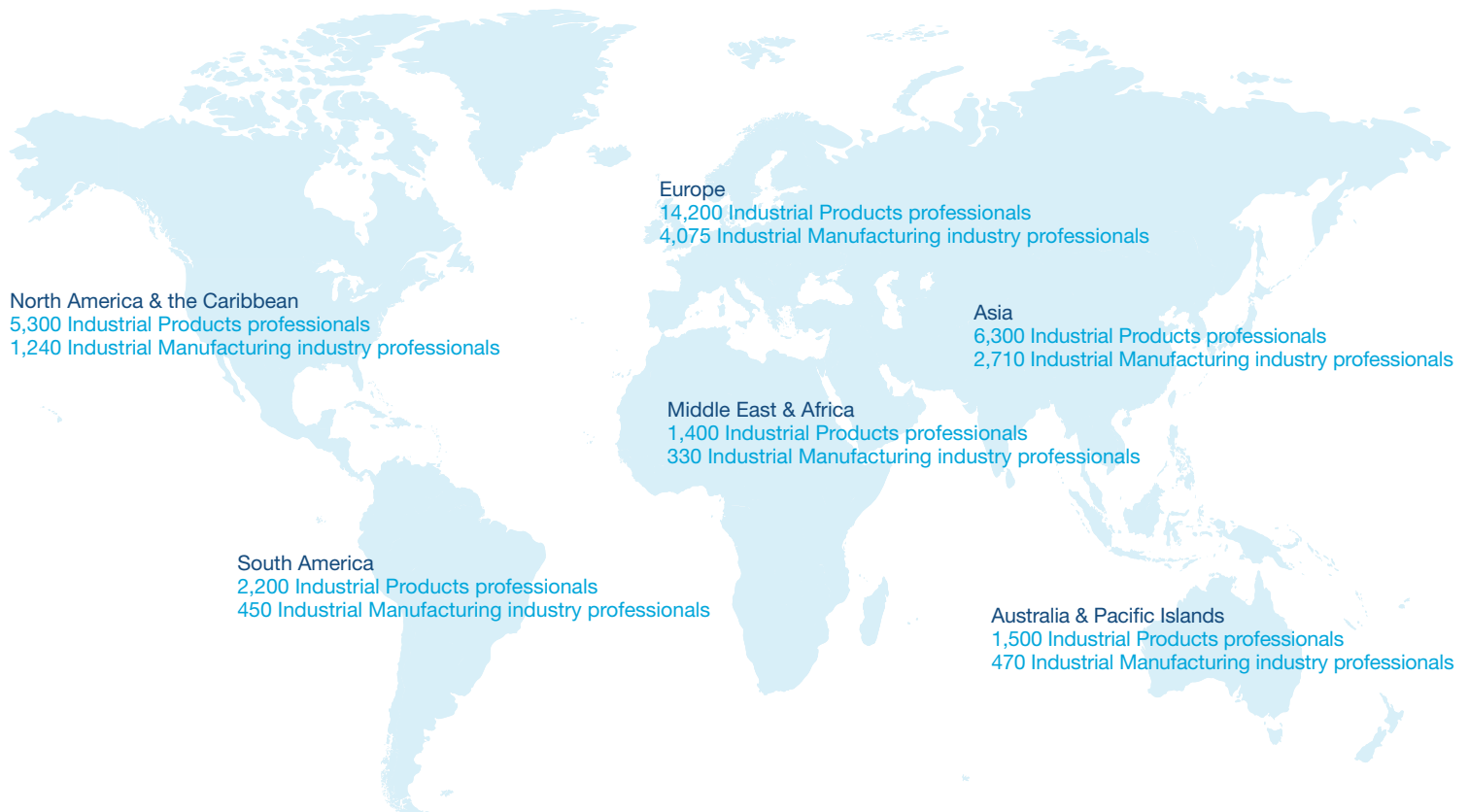
Our Industrial Manufacturing practice is comprised of a global network of industry professionals who provide assurance, tax, and advisory services to public and private companies around the world. Central to the successful delivery of our services is an in-depth understanding of today's industry issues, in addition to a wealth of specialized resources and "best practices" that help solve complex business challenges. Our highly skilled team encourages conversations on top-of-mind trends and issues through active participation in industry conferences and associations, as well as through industry-focused publications and Web forums. To address your industry needs wherever they arise, our professionals are concentrated in areas where the industrial manufacturing industry operates today and in the emerging markets where it will operate in the future.

## Quality deal professionals

PwC's Transaction Services practice, with more than 3,800 dedicated deal professionals worldwide, has the right industry and functional experience to advise you on factors that could affect a transaction, including market, financial accounting, tax, human resources, operating, IT, and supply chain considerations. Teamed with our Industrial Manufacturing practice, our deal professionals can bring a unique perspective to your deal, addressing it from a technical aspect as well as from an industrial manufacturing industry point of view.

## Local coverage, global connection

In addition to the approximately 9,300 professionals who serve the industrial manufacturing industry, our team is part of an Industrial Products group that consists of 31,000 professionals, including approximately 15,800 providing Assurance services, more than 9,000 providing Tax services, and 6,200 providing Advisory services. This expands our global footprint and enables us to concentrate efforts in bringing clients a greater depth of talent, resources, and know-how in the most effective and timely way.



# Contacts

## PricewaterhouseCoopers Industrial Manufacturing practice

Our Industrial Manufacturing practice, strategically located in more than 30 countries around the world, comprises a global network of industry professionals serving manufacturing clients. We bring experience, international industry best practices, and a wealth of specialized resources to help solve business issues.

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# Methodology

*Assembling value* is an analysis of deals in the global industrial manufacturing industry. Deal information was sourced from Thomson Financial and includes deals for which targets have primary SIC codes that fall into one of the following SIC industry groups: millwork, plywood and structure; wood buildings and mobile homes; partitions, shelving, and lockers; gaskets, packing, and sealing devices; fabricated rubber products; miscellaneous plastics products; heating equipment, except electric air; fabricated structural metal products; bolts, nuts, screws, and other machine products; metals forgings and stampings; coating, engraving, and allied services; miscellaneous fabricated metal products; engines, and turbines; farm and garden machinery; metalworking machinery; special industry machinery; general industrial machinery; refrigeration and service industry machinery; miscellaneous industrial and commercial machinery; electric transmission and distribution equipment; electrical industrial apparatus; electrical lighting and wiring equipment; miscellaneous electrical machinery and equipment; and miscellaneous manufacturing industries.

This analysis includes all individual mergers and acquisitions for disclosed or undisclosed values, leveraged buyouts, privatizations, minority stake purchases, and acquisitions of remaining interest announced between January 1, 2006, and September 30, 2009, with a deal status of completed, intended, partially completed, pending, pending regulatory approval, unconditional (i.e., initial conditions set forth by the buyer have been met but deal has not been completed), or withdrawn.

Regional categories used in this report approximate United Nations (UN) Regional Groups, as determined by the UN Statistics Division, with the exception of the North America region (includes Northern America and Latin and the Caribbean UN groups), the Asia and Oceania region (includes Asia and Oceania UN groups) and Europe (divided into UK and Eurozone and Europe ex-UK and Eurozone regions). The Eurozone includes Austria, Belgium, Cyprus, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Malta, Netherlands, Portugal, Slovenia, and Spain. Oceania includes Australia, New Zealand, Melanesia, Micronesia, and Polynesia. Overseas territories were included in the region of the parent country and China, when referenced separately, includes Hong Kong. The term “deals,” when referenced herein, refers to deals with a disclosed value of at least \$50 million unless otherwise noted.

Visit our industrial manufacturing industry website at  
[www.pwc.com/us/industrialproducts](http://www.pwc.com/us/industrialproducts)

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