

Assembling value

Second-quarter 2009 industrial manufacturing
mergers and acquisitions analysis

China: Balancing the risks and opportunities



Welcome to *Assembling value*, PricewaterhouseCoopers' 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 second quarter of 2009, we supplement this issue with a special report that highlights potential growth opportunities and considerations of industrial manufacturing companies doing business in China. Included is a discussion around China's role and stature in the international economic order, its spending priorities, and equal partner expectations of foreign investment.

Special Report:

Growing together: China looks for global partners

For US and European industrial manufacturing companies struggling through the recession, China's growth rate, which forecasters¹ in China and the U.S. now expect to approach or even exceed 9 percent for 2009, is enticing. So, too are the hundreds of billions of dollars that China has committed to bolster its domestic demand and pursue investment in a multilayered \$586 billion economic stimulus effort.

But it is important for companies that see opportunity in China's robust stimulus plans to recognize that the relationship of foreign companies to China is changing as China's role in the global economy grows and develops along with its national aspirations, financial capabilities, and the realities of the global recession. It is also important for companies to be aware that China's worldwide exports are diminishing and may not return to prerecession levels. China is unlikely to achieve its economic objectives through export-led growth alone.

In our experience, China's government and businesses are increasingly insistent that foreign companies aiming to do business in China align themselves with the government's strategic development priorities and make it clear that they are willing to offer technology and management expertise in return for market access.

A stimulus mindset

The details of the Chinese stimulus plan remain unclear. Although the Chinese central government in late 2008 announced a RMB 4 trillion (\$586 billion) spending program, the parameters, details, and funding of that program remain opaque and subject to change. It's difficult to establish, for instance, which spending was programmed for initiatives such as earthquake reconstruction and which is truly incremental.

Spending priorities appear to have shifted during the past few months, with quick-hitting health, education, and social spending accounting for a larger portion than previously anticipated, when traditional infrastructure looked to be the focus of the Beijing's fiscal stimulus plan.

Economic indicators show China's measures are producing results, with most economists crediting its aggressive fiscal and monetary stimulus policies with sustaining economic growth. At the same time, many of the same observers say that China needs to formulate a plan for ratcheting down its stimulative lending policies to a more sustainable level before they lead to inflation and asset bubbles.²

An equal partner, not a subsidiary

For many years, foreign investors have moved into China for two reasons: to capitalize on its sustained levels of growth and to pursue cost rationalization through lower-cost labor, particularly in manufacturing.

But this transactional approach to doing business in China is waning. In recent years, the Chinese government continually has shown preference in granting market access and business opportunities to companies that were willing to adopt the nation's strategic economic goals, which include increased industrialization, technological transfer, and infrastructure development.

Moving forward, companies seeking access to the Chinese market will need to show that they see China as more than a large marketplace boasting a briskly growing GDP. For example, a company that wants to sell a piece of equipment into the Chinese market or cut labor costs may find it beneficial to show it is willing to partner with the Chinese state on such government priorities as rural development.

¹ "China needs exit plan for monetary policy—economist," *Thomson Reuters*, July 28, 2009; "Merrill Lynch hikes China growth forecast," *The Wall Street Journal*, July 27, 2009

² "Reality check for China's monetary policy," *Caijing*, July 23, 2009

It is clear that China's spending and lending plans aim primarily to help Chinese citizens and Chinese companies, potentially putting foreign companies at a disadvantage. Thus, a major foreign company operating in China may enhance its revenue prospects by partnering with a strategic Chinese firm. For example, approximately a year ago, Carrier Corporation, a unit of United Technologies Corporation, and Guangdong Midea Electric Appliances Company, a unit of Midea Group, signed an agreement to form an air conditioner manufacturing joint venture.³ The Midea-Carrier joint venture produces residential and light commercial air conditioning systems for a global market.

China's strategic development goals have not changed radically, but as demand for Chinese exports declines, the state's traditional industrial, technology acquisition, and infrastructure goals will not be enough to sustain its economy. However, government programs aimed at spurring consumer confidence, such as health insurance plans and pensions, likely will create a domestic market to help compensate for this drop.

Rural development, seen as critical to long-term Chinese political and social stability, is a key priority for stimulus spending. For instance, the central government recently announced more than \$100 billion in new hospital construction for rural areas. When dealing with China, economic and social priorities often mix due to the high degree of state involvement in business.

China's global impact

That confluence of state economic and social priorities can have important consequences for companies looking to do business with China and for companies in business sectors that overlap with Chinese priorities, such as resource and technology-related sectors.

For instance, on June 23, 2009, the United States and European Union filed a WTO complaint alleging that China has been placing export restrictions on certain industrial raw materials. According to the complaint, such restrictions lead

to excess capacity within China and lower prices for domestic Chinese companies needing to purchase the materials for internal business ventures, many of which are funded by the stimulus efforts. At the same time, China has been importing many of the same raw materials, propping up international prices.

Many observers have seen these moves by the Chinese officials as an officially sanctioned stockpiling effort, and Yu Dongming, chief of the metallurgical division of China's National Development and Reform Commission's industry department, seemed to confirm as much in late June.⁴

Media reports at the time wrote that Yu said the State Reserve Bureau had ceased its purchases and that the stockpile program had run its course and achieved its objectives of price stability and replenishing of stocks.

The stockpiling effort has helped many manufacturing companies as it partly compensated for the drop in demand from the United States and European Union as the financial crisis and global recession have deepened since late 2008. While this helped some foreign companies in the metals and other industrial sectors, it had the adverse effect on others of keeping commodities prices artificially high at a time when credit and revenue were falling.

Now that China has said it has halted its stockpiling, some observers think that underlying demand for raw materials will slacken, causing prices to slide and removing the engine for what has been a mini-recovery in the metals sector while lowering commodity costs for other manufacturers.

China's ability to move prices, based on its national priorities, shows its importance as a global economic player. Companies wishing to build or maintain relationships with Chinese counterparts should be aware that they are expected to act as an equal partner and may be required to give up technological and management know-how in exchange for market access.

³"Carrier Corp. and Midea Electric to form manufacturing joint venture in China," *Reuters*, July 3, 2008

⁴"As China Hoards, Concern Grows About Recovery," *The Globe and Mail*, June 24, 2009

Perspective:

Thoughts on deal activity in the second quarter of 2009

Welcome to the sixth edition of *Assembling value*, our analysis of mergers and acquisitions in the global industrial manufacturing sector. A challenging global macroeconomic environment characterized by constrained corporate profits, high unemployment, and pessimistic forecasts continues to curb investor appetite for acquisitions. Economic stimulus plans implemented by major global markets seem in some cases to be producing results. For instance, China's economic stimulus, which invests approximately \$586 billion primarily in infrastructure projects, appears to be working as expectations for its 2009 economic growth are robust, especially compared with developed countries that have invested in their own economic stimulus packages.

In this edition, we analyze year-to-date deal activity to assess how weak global economic fundamentals have depressed volume and value. Our analysis reveals that the pace of deal volume (measured by number of deals with disclosed values of at least \$50 million) remains soft relative to prior periods. Deal value (measured by total value of deals with disclosed values of at least \$50 million) also continues to trend lower, symptomatic, in part, of weak credit markets, constrained financial investor sentiments, and a focus on cash conservation and shoring up balance sheets by strategic buyers.

We continue to believe distressed transactions will drive deal activity. During the first half of 2009, two of the top 10 deals were for distressed assets. In the first one, Algonquin Power Income Fund's \$291.9 million deal for Hydrogenics Corp., a global developer of hydrogen generation and fuel cell products and services, was motivated by Hydrogenics' need for liquidity and its high level of balance sheet tax losses (\$192 million), which will offset Algonquin's tax bill as Algonquin converts from operating as a trust to a corporate entity. In the second, Milacron Inc., a plastics processing and industrial fluids company, announced the sale of its Canadian and US operations to creditors for \$155 million after filing for Chapter 11 protection due to weak demand.

Looking forward, we anticipate a limited amount of large deal activity in the industrial manufacturing sector. What deals are getting done are typically in the middle market, and a flow of distressed deals should continue. Companies are braced for challenging operating environments, and investors are maintaining a conservative stance because incontrovertible indications of a global economic recovery have been slow to materialize. However, there are signs that the global credit situation is improving. For example, LIBOR rates (the interest rate that banks charge other banks on the London interbank market) have come close to record lows. Also, a significant measure of credit risk—the so-called TED spread (the spread between the three-month LIBOR rate and three-month US Treasury bill yields)—has narrowed recently. Finally, corporate bond issuances are increasing steadily. That said, the focus remains on smaller deals that don't require assistance from the capital markets or highly leveraged loans.

We continue to believe that a wider global economic recovery is essential for a significant increase in industrial manufacturing deal activity. Although the road ahead looks challenging, the macroeconomic setting may benefit some companies, particularly those with strong business models and capital positions to increase share in existing and new markets. In addition, companies based in China and other markets that show early signs of recovery—or are the beneficiaries of major government stimulus packages, loan programs or other assistance—may have greater access to capital and, therefore, may be able to use acquisitions to better position themselves for when the market cycle swings upward.

Commentary

Industrial manufacturing deal activity remains anemic.

The pace of deal activity on a year-over-year basis has slowed substantially, with total deals declining to 26 in first-half 2009 from 90 during first-half 2008. Total deal value in first-half 2009 was approximately \$4 billion, an 85 percent decline from the \$27 billion reported in first-half 2008. In addition, first-half 2009 average deal value declined to \$153 million from \$297 million in first-half 2008, representing a 48 percent year-over-year decline.

Negative investor sentiment continues to weigh heavily on deal activity.

Activity by financial investors remains limited as available leverage remains constrained and fundraising continues to stall relative to year-ago levels. The percentage of deals completed by financial investors increased when compared with the first-half of 2008 (31 percent in first-half 2009 versus 27 percent in first-half 2008). However, the number of deals by financial investors declined from 24 in first-half 2008 to eight in first-half 2009, representing a 67 percent decline year-over-year.

Large deal activity remains encumbered by negative sentiments, valuations, and credit constraints.

Large deal activity, defined as deals with a disclosed value of at least \$1 billion, has continued to be dramatically lower than historical levels. In the first half of 2009, there were no large deals. Only 26 deals had a disclosed value greater than \$50 million versus 86 in the first half of 2008. This lull in large deal activity is expected, given continued global economic weakness and depressed asset valuations, among other factors. Industrial manufacturing will not likely see a return of large deals until investor confidence returns and a global economic and credit recovery is realized.

Valuation multiples remain depressed.

Asset valuations for targets, represented by median deal value to sales multiples and median deal value to earnings before interest, taxes, depreciation, and amortization (EBITDA) multiples, have remained depressed relative to recent historical levels. During first-half 2009, the median deal value to target sales ratio was 0.9 times versus 1.3 times in 2008, reflecting a 31 percent discount. The median deal value to EBITDA multiples in the first half of 2009 was 6.8 times versus 10.5 times in 2008, a 35 percent discount.

Interest in China's market remains strong relative to the other BRIC (Brazil, Russia, India, and China) economies.

The \$586 billion Chinese infrastructure stimulus plan implemented in late 2008 bodes well for several industrial products subsectors, including engineering and construction, transportation and logistics, and metals. However, the implications may not be as significant for industrial manufacturing, given the spending primarily is intended to finance infrastructure development. In the first half of 2009, of the four Chinese transactions worth \$50 million or more, 75 percent are categorized as within-border transactions. Furthermore, deal activity in China has continued to dominate BRIC transactions. During first-half 2009, China's four announced deals represented 67 percent of deal volume for BRIC-affiliated transactions.

Industrial manufacturing deal activity remains anemic.

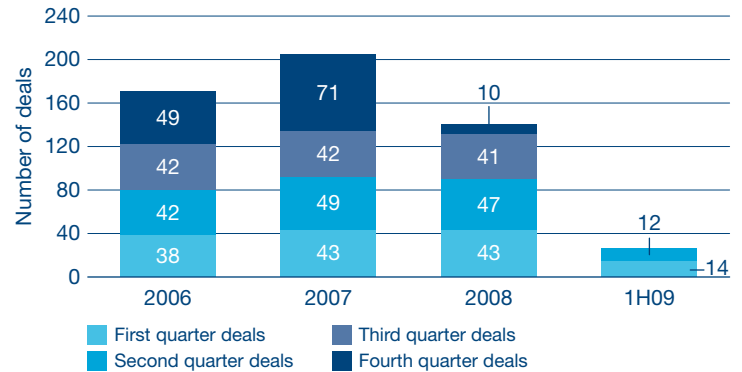
On a year-over-year basis, the pace of deal activity as measured by the number of deals during the first half of 2009 slowed substantially versus that of prior periods, with total deals declining to 26 from 90 during first-half 2008.

On a quarterly basis only 12 deals were announced in second quarter 2009 versus 47 in the second quarter 2008. Sequentially, the number of deals declined from 14 deal announcements in the first quarter of 2009.

While overall global deal activity has continued to decline relative to prior periods, the percentage of deals associated with US-based targets or buyers also has fallen. The number of deals associated with US-based targets or buyers represented 27 percent of announced deals during first-half 2009, compared with 36 percent in 2008, 40 percent in 2007, and 46 percent in 2006.

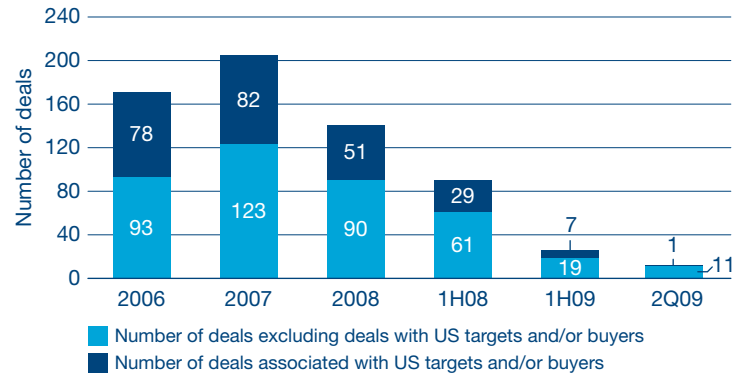
Deal activity measured by volume of deals

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



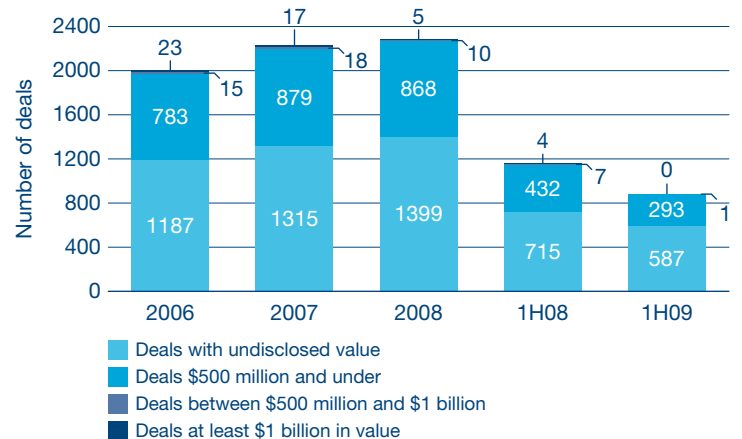
Deal activity measured by volume of deals

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



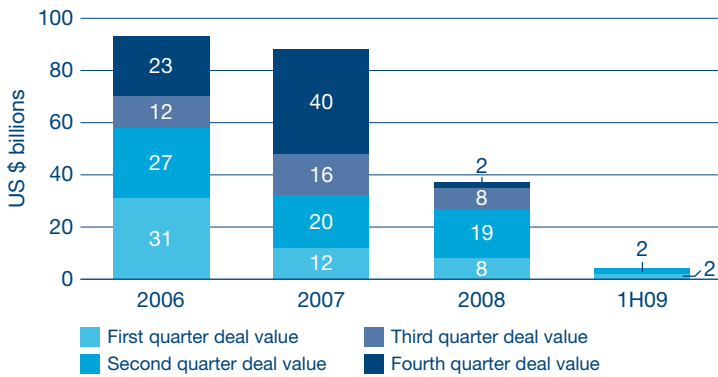
Deal activity by range of deal value

Measured by number of deals



Deal activity by total value of deals

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

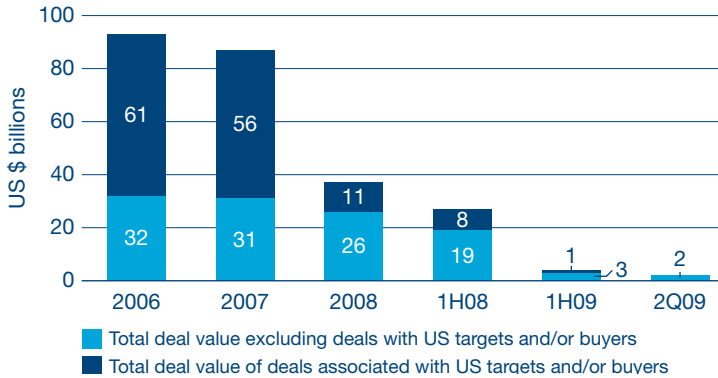


The total value of deals announced during the first half of 2009 was approximately \$4 billion, substantially less than total deal values in first-half 2008 (\$27 billion), representing a decline of 85 percent year over year. Sequentially, total deal value declined 62 percent from approximately \$10 billion in second-half 2008. On a quarterly basis, the total value of deals announced in second quarter 2009 was \$2 billion versus \$19 billion in the second quarter 2008.

Total deal value for deals with US targets and/or buyers during first-half 2009 was approximately \$1 billion (versus \$8 billion in first half 2008), representing a decline of approximately 88 percent year over year, while the total deal value excluding deals with US targets and/or buyers during first-half 2009 was approximately \$3 billion (versus approximately \$19 billion in first-half 2008), representing a decline of approximately 84 percent year over year.

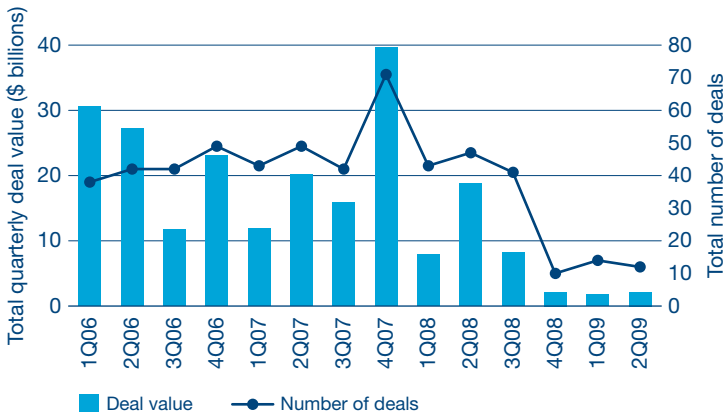
Deal activity by total value of deals

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



Historical perspective of deal volume and value, quarterly statistics

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

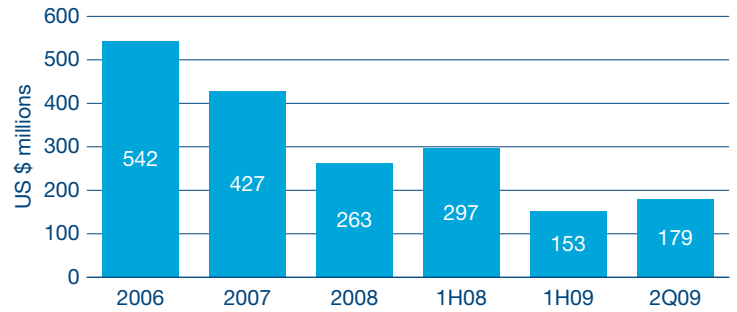


Since 2006, the average deal value has declined at an accelerated annual rate (down 21 percent in 2007 and 38 percent in 2008). In the first half of 2009, this trend continued, with the average deal value declining to \$153 million from \$297 million in the first half of 2008, representing a 48 percent decline. From a quarterly perspective, the average deal in second quarter 2009 was \$179 million versus \$399 million in the second quarter last year, a 55 percent decline.

Average deal value for deals associated with US targets and/or buyers during first-half 2009 was \$129 million versus \$268 million in first-half 2008, representing a 52 percent decline, while the average deal value excluding deals with US targets and/or buyers during first-half 2009 was \$162 million versus \$311 million in first-half 2008, representing a 48 percent decline. These results suggest that the market's downward adjustment to asset prices has been seen around the globe.

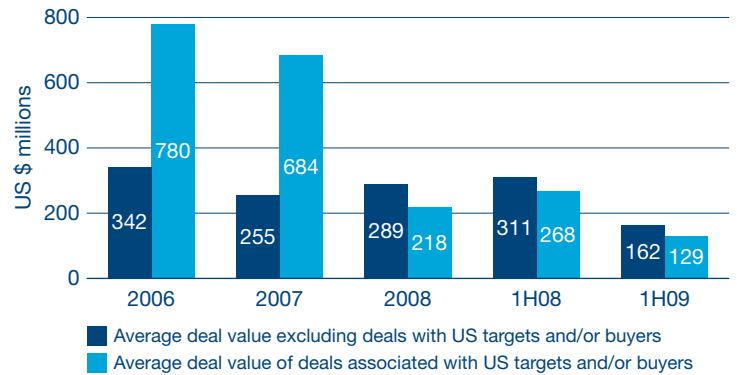
Deal activity by average deal value

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



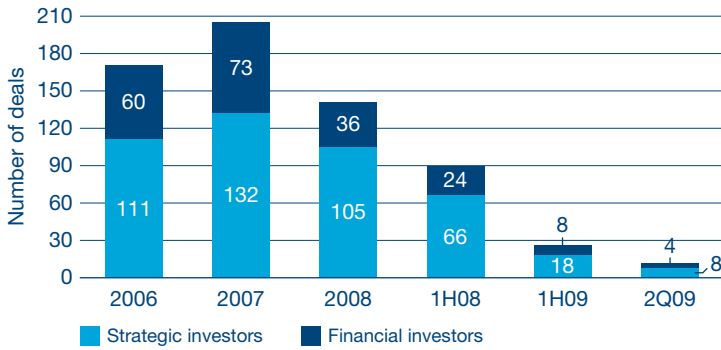
Deal activity by average deal value

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



Deal activity by investor group

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



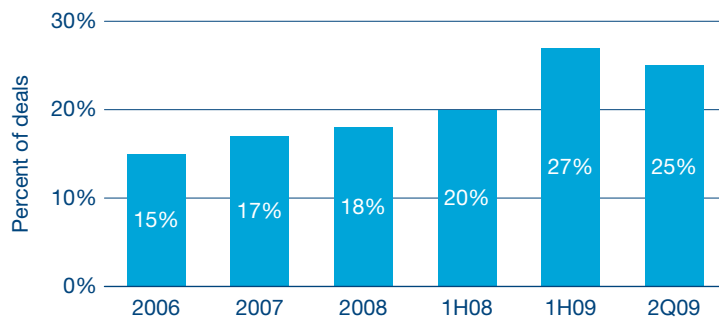
Negative investor sentiment continues to weigh heavily on deal activity

Financial investors remain on the sidelines as fundraising continues to lag year-ago levels. The Wall Street Journal recently reported that US-based private equity firms raised approximately \$55 billion across 173 funds in the first half of 2009, representing a 64 percent decline from approximately \$153 billion raised by 261 funds during first-half 2008. Although those numbers are specific to US-based private equity firms, we believe they capture the trend underlying the global private equity arena, due in part to globalization, capital mobility, and capital market interconnectedness. Although many governments have rolled out fiscal stimulus plans, investors, both strategic and financial, have maintained pessimistic outlooks. Whereas the percentage of deals completed by financial investors increased when compared with the first-half of 2008 (31 percent in first-half 2009 versus 27 percent in first-half 2008), the number of deals declined substantially, from 24 in first-half 2008 to eight in first-half 2009, representing a 67 percent decline year-over-year.

In our view, with financial investors on the sidelines, the lower demand, in part, is continuing to place downward pressure on asset and firm valuations, which ordinarily would be a boon for strategic buyers able to buy assets and companies at steep discounts. However, the current global economic environment and the unfavorable dynamics shaping investor sentiments and outlooks have resulted in many strategic buyers focusing more intently on efficiently managing their businesses and assets. Many are conserving cash amid liquidity concerns and adjusting strategies in the face of weak demand and fewer mergers and acquisitions. Nevertheless, deals are taking place as stronger strategic buyers take advantage of opportunities to expand and weaker firms employ exit strategies. Although the percentage of deals driven by strategic activity in the first-half of 2009 (69 percent) declined relative to the first-half of 2008 (73 percent), results compare favorably with the three-year average (2006-2008) of approximately 68 percent.

First-half 2009 results also indicate that buyers are continuing first quarter 2009 trends and purchasing minority stakes in targets to a greater degree versus prior periods, possibly to hedge market risks or complement cash conservationist strategies. During the first half of 2009, minority stake purchases accounted for 27 percent of announced deals versus 20 percent in the first half of 2008 and 18 percent in all of 2008. During the second quarter of 2009, minority stake purchases accounted for 25 percent of announced deals versus 22 percent in second quarter 2008. We believe minority stake purchases may continue to account for a larger percentage of announced deals during the rest of the year as strategic buyers manage liquidity positions, investor sentiments remain pessimistic, and credit markets, although improving, remain constrained.

Minority stake purchases (<50% ownership)
Measured by number of deals worth \$50 million or more



Large deal activity remains encumbered by negative sentiments and credit constraints

Large deal activity, defined as those with a disclosed value of at least \$1 billion, has continued to decline dramatically. There were 23 large deals in 2006, 17 in 2007, and five in 2008. In the first half of 2009, there were no large deals and only 26 deals with a disclosed value greater than \$50 million, versus 86 in the first half of 2008. Satipel Industrial's pending acquisition (announced June 22) of Duratex SA, valued at \$963 million, hit closest to the \$1 billion mark, and it was by far the most substantial in first-half 2009. The deal was motivated by synergies and cost reduction, as Satipel is a Brazilian manufacturer of wood panels, particle board, and wood components for the furniture industry, and Duratex is a Brazilian manufacturer of finished wooden products, vitreous china products, and brass bathroom fixtures, among other products. As was the case in the Satipel-Duratex deal, we expect more transactions to be driven by necessity due to overcapacity and weak demand, particularly for companies operating in adjacent markets. However, we expect the malaise of large deals to persist, as global economic weakness is expected to continue. One thing is a near certainty: Industrial manufacturing will not likely see a return of large deals until investor confidence returns and a global economic recovery is realized.

Large deals in 2008

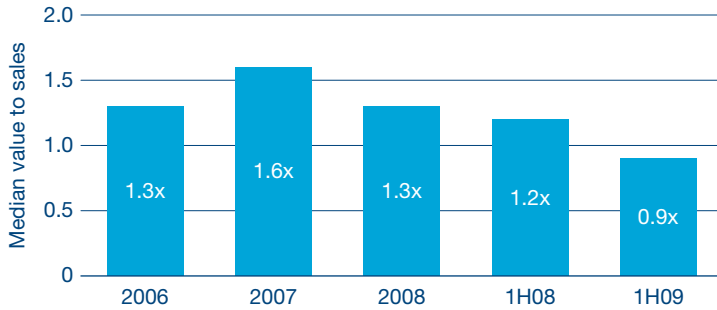
Month announced	Target name	Target nation	Acquirer	Acquirer nation	Status	Value of transaction in US\$ bln	Category
Jun	Graham Packaging Co LP	United States	Hicks Acquisition Co I Inc	United States	Pending	3.20	Rubber & Plastic Products
Jun	Converteam Group SAS	France	Investor Group	France	Completed	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 Grp Huaigang	China	Gaoxin Zhangtong Co Ltd	China	Pending	1.06	Fabricated Metal Products

Deals greater than \$50 million – 1H09

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	Pending	962.51	Fabricated Metal Products
Jun	Hydrogenics Corp	Canada	Algonquin Power Income Fund	Canada	Pending	291.86	Electronic & Electrical Equipment
Mar	PSV Holdings Ltd	South Africa	Iandra Industries Ltd	United Kingdom	Pending	208.85	Industrial Machinery
Mar	Sensor Switch Inc	United States	Acuity Brands Inc	United States	Completed	207.52	Electronic & Electrical Equipment
May	Qingdao Hisense-Asts(6)	China	Hisense Kelon Electr Hldgs Co	China	Pending	200.68	Industrial Machinery
Jan	Hitachi Koki Co Ltd	Japan	Hitachi Ltd	Japan	Completed	182.43	Industrial Machinery
Mar	Milacron Inc	United States	Creditors	United States	Pending	175.00	Industrial Machinery
Mar	Scotsman Group LLC	United States	Braveheart Acquisition Inc	United States	Completed	160.00	Industrial Machinery
May	Quadrant AG	Switzerland	Aquamit BV	Netherlands	Intended	140.32	Rubber & Plastic Products
Feb	Bayou Cos LLC	United States	Insituform Technologies Inc	United States	Completed	132.50	Fabricated Metal Products
Feb	SEN Corp	Japan	Sumitomo Heavy Industries Ltd	Japan	Completed	131.85	Industrial Machinery
Mar	Filtrona Extrusion Inc	United States	Saw Mill Capital LLC	United States	Completed	115.00	Rubber & Plastic Products
Jun	A2SEA A/S	Denmark	DONG Energy A/S	Denmark	Completed	108.19	Industrial Machinery
Feb	Qiqihar Heavy CNC Equip Corp	China	Zhejiang Tianma Bearing Co Ltd	China	Completed	102.50	Industrial Machinery
Feb	Praia do Morgado	Brazil	Cemig	Brazil	Completed	93.05	Electronic & Electrical Equipment
Jan	Citra Tubindo Tbk PT	Indonesia	Kestrel Wave Investment Ltd	Indonesia	Completed	88.49	Fabricated Metal Products
Feb	CI Kasei Co Ltd	Japan	ITOCHU Corp	Japan	Completed	87.74	Rubber & Plastic Products
Mar	Tangshan Fengrun Hengfeng-Asts	China	Tangshan Fengrun Zhengda Iron	China	Pending	87.50	Fabricated Metal Products
May	Kingboard Copper Foil Hldg Ltd	Bermuda	Kingboard Laminates Hldg Ltd	Hong Kong	Pending	75.88	Fabricated Metal Products
Jun	Doosan Mottrol Holdings Co Ltd	South Korea	Doosan Corp	South Korea	Pending	71.19	Industrial Machinery
Apr	Eagle Ind Co-Mechanical Ops	India	Burgmann Indus-Mechanical Ops	India	Completed	70.00	Rubber & Plastic Products
Apr	Undisclosed Energy Transformer	India	EFACEC Capital SGPS SA	Portugal	Pending	65.70	Electronic & Electrical Equipment
Apr	National Coupling Co Inc	United States	Hunting PLC	United Kingdom	Completed	60.00	Fabricated Metal Products
Mar	Jinzhou Jin Tai Welding	China	Lincoln Electric Holdings Inc	United States	Pending	56.00	Industrial Machinery
Apr	Eliiy Power Co Ltd	Japan	Investor Group	Japan	Completed	51.73	Electronic & Electrical Equipment
Apr	Scanvaegt Nordic A/S	Denmark	Grundtvig Family	Iceland	Completed	50.13	Industrial Machinery

Deal valuation by median deal value to sales multiples

Measured by median deal value to sales for deals worth \$50 million or more

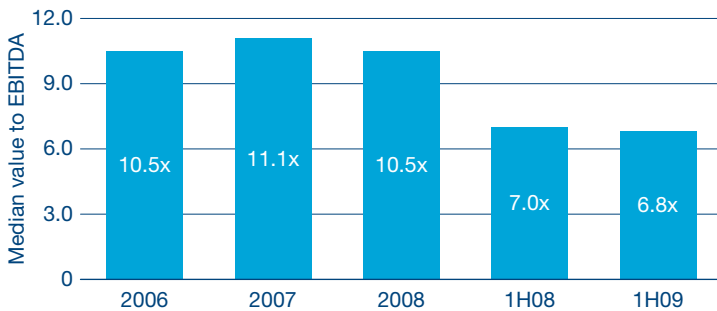


Valuation multiples remain depressed

Asset valuations for targets, represented by median deal value to sales multiples and median deal value to EBITDA multiples, have remained depressed relative to historical levels. During the first half of 2009, the median deal value to target sales ratio was 0.9 times, reflecting a 31 percent discount to the deal value to the median sales multiples of deals announced in 2008 (1.3 times), 44 percent lower than the 2007 multiple (1.6 times), and 31 percent lower than the 2006 multiple (1.3 times). Evaluating the amount buyers paid for each dollar of EBITDA reveals a similar trajectory. During the first half of 2009, the median deal value to EBITDA multiple was 6.8 times versus 10.5 times (35 percent discount) in 2008, 11.1 times (39 percent discount) in 2007, and 10.5 times (35 percent discount) in 2006.

Deal valuation by median deal value to EBITDA multiples

Measured by median deal value to EBITDA for deals worth \$50 million or more



Industrial machinery category continues to be a strong driver of deal activity in first-half 2009

During the first half of 2009, 42 percent of deals (measured by deal volume) were in the industrial machinery category versus 39 percent in first half 2008. The deal weighting of fabricated metal products decreased to 23 percent from 26 percent in first-half 2008 as the mix shifted to rubber and plastic products and electronic and electrical equipment categories.

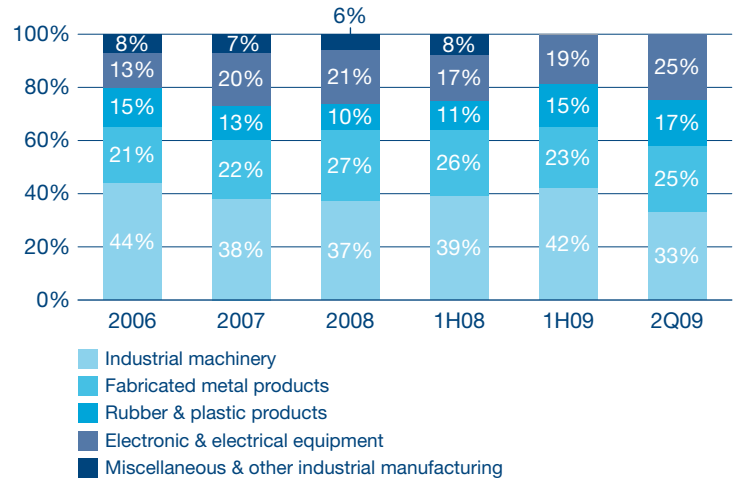
From a quarterly perspective, although industrial machinery deals continued to drive activity during the second quarter of 2009, a greater proportion of transactions were announced for fabricated metal products and electronic and electrical equipment targets relative to past periods.

Public, subsidiary targets continue to drive deal flow

During the first half of 2009, the distribution of ownership status of industrial manufacturing deal targets (i.e., government-owned, joint venture, private entity, public entity, and subsidiary) remained relatively steady. The allocation continued to tilt mostly toward public and subsidiary (i.e., assets and/or business units) targets, accounting for 70 percent of deals. On a year-over-year basis the percentage of public and subsidiary deals slightly increased from 69 percent in first-half 2008. First-half 2009 deal contribution of private targets (27 percent) has remained relatively in line with the historical average of approximately 28 percent. Should the global economic slowdown persist longer than expected, it would not be surprising to see an uptick in the level of deals for private companies as they seek exit strategies, as capital markets are often closed to them.

Deals by industrial manufacturing category*

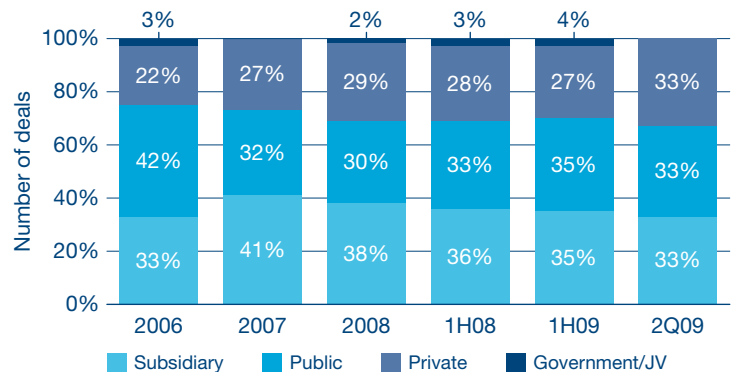
Measured by number of deals worth \$50 million or more



* Percentages may not sum to 100% due to rounding.

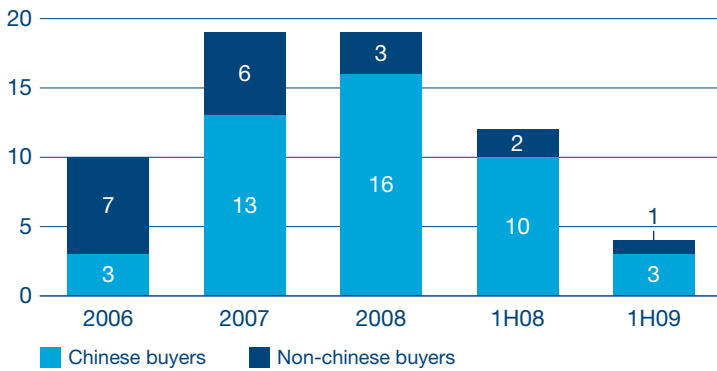
Deals by ownership status*

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

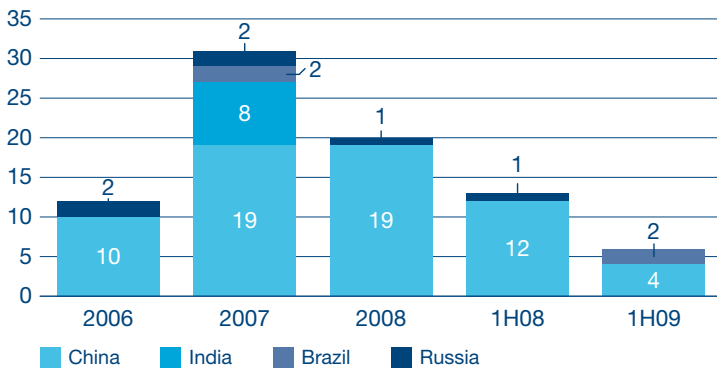


* Percentages may not sum to 100% due to rounding.

Chinese/Non-Chinese buyers of China-based IM companies
Measured by number of deals worth \$50 million or more



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



Interest in China’s market remains strong relative to the other BRIC economies

In the wake of China’s \$586 billion stimulus package, Bank of America Merrill Lynch is forecasting China’s 2009 economic growth rate to increase 8.7 percent, while most developed economies are mired in recession. Although the stimulus does not hold great promise for industrial manufacturing companies because most of the money will finance infrastructure development rather than shore up its weakened manufacturing sector, a stronger overall economic environment is likely to bode well for the industrial manufacturing sector.

If that is the case, it is not yet reflected in M&A volume numbers. First-half 2009 deal-making was limited to four transactions worth less than half a billion dollars total. Additionally, the majority of those transactions were within-border deals (75 percent or three of the four deals), compared with 83 percent (10 deals) in first-half 2008. Of the three within-border deals during first-half 2009, two involved the purchase of assets (the Hisense Kelon—Qingdao Hisense deal, valued at \$201 million, and the Tangshan Zhenda—Tangshan Hengfeng deal, valued at \$86 million). The third, the Zhejiang—Qiqihar deal, increased Zhejiang’s interest in Qiqihar from approximately 74 percent to approximately 88 percent (\$103 million).

The lone cross-border transaction involved an Asian subsidiary (Lincoln Asia Pacific) of US-based Lincoln Electric, which seeks to purchase a remaining 52 percent interest in Jin Tai Welding for \$56 million in cash and debt assumption to further expand its welding consumables business in China.

Still, deal activity in China has continued to outpace deal activity in other BRIC nations. During the first half of 2009, China’s four announced deals represented 67 percent of deal volume for BRIC-affiliated transactions.

Regional analysis

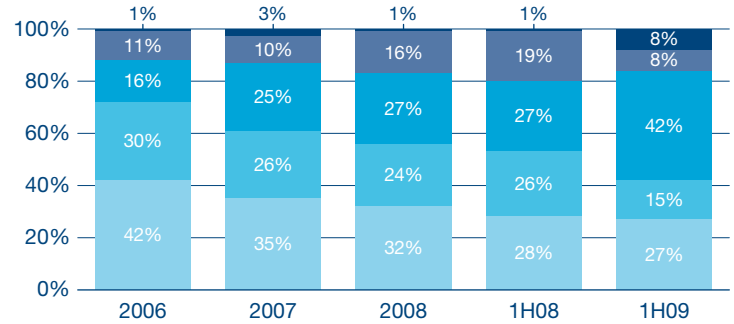
Buyers from Asia and Oceania and North America continue to drive deal activity

During the first half of 2009, North American and Asia and Oceania buyers were responsible for 69 percent of M&A activity (as measured by deal volume), a significant increase when compared with 55 percent in the first half of 2008. On a standalone basis, the proportion of deals with Asia and Oceania buyers increased substantially relative to prior periods. For instance, in the first half of 2009, Asia and Oceania buyers accounted for 42 percent of deal volume, versus a three-year historical average (2006-2008) of approximately 23 percent. This substantial increase may suggest that Asia and Oceania businesses are taking advantage of declining asset values and an opportunistic buying scale. In addition, increasingly, a greater percentage of Asia and Oceania buyers are investing in the Asia and Oceania region. In the first half of 2009, 93 percent of Asia and Oceania buyer capital was spent on investments in the Asia and Oceania region, a much greater percentage than that of past periods (65 percent in 2008, 54 percent in 2007, and 59 percent in 2006). This may indicate that protectionist economic policies are taking root.

Proportionally, North American buyers have continued to drive industrial manufacturing deals. However, the magnitude of deal involvement has fallen from historic levels (27 percent in first-half 2009 versus an average 36 percent during 2006-2008). During the first half of 2009, similar to the near-term trend for Asia and Oceania buyers, North American buyers spent a significant portion (95 percent) of dollars on North American assets. However, the North American trend is less significant relative to that of Asia and Oceania contemporaries as North American buyers traditionally have been significant purchasers of assets in North American markets.

The percentage of buyers from the United Kingdom and Eurozone region declined significantly, to 15 percent from 26 percent in first-half 2008. In addition, UK and Eurozone buyers spent significantly less for regional assets in first-half 2009 than they have in the past, as total spending in the UK and Eurozone region declined to 30 percent from 76 percent in 2008.

Regional distribution of deals by buyer region*
Measured by number of deals worth \$50 million or more



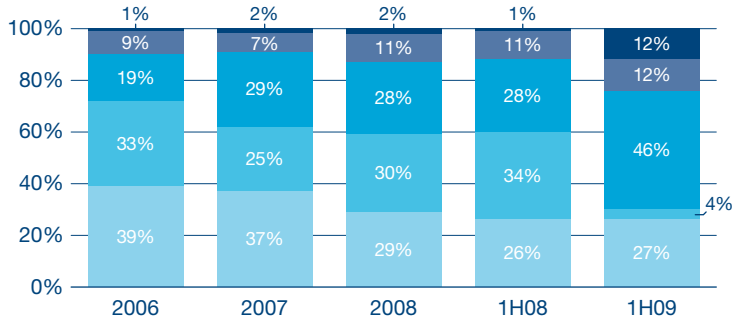
* Percentages may not sum to 100% due to rounding.



Deal Volume
2006—171
2007—205
2008—141
1Q08—90
1Q09—26

Regional distribution of deals by target region*

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



* Percentages may not sum to 100% due to rounding.

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

Deal Volume
2006—171
2007—205
2008—141
2H08—90
2H09—26

Investment interests in the Asia and Oceania region ramp up significantly

During the first half of 2009, 46 percent of deals for targets (as measured by deal volume) were announced in the Asia and Oceania region. This compares with 28 percent in the first half of 2008. The allocation of deals for targets in North America (27 percent), although significantly lower than 2006 (39 percent) and 2007 (37 percent) levels remained relatively in line with the allocation in first half 2008 (26 percent). For the UK and Eurozone region, deals for targets during the first half of 2009 trended substantially lower than the historical average (2006–2008) of 29 percent as 4 percent of deals were for assets in that region.

Preparing your company to enter the Chinese marketplace?

China's reported 7.9 percent growth for the second quarter of 2009 is creating hope that the world recession may be easing. Bank of America Merrill Lynch recently raised its forecast for this year's China economic growth rate to 8.7 percent from 8 percent. In late July, copper reached its highest price since early October.⁵ Also in July, a Sino-US strategic and economic dialogue, the first of its kind, took place in Washington, D.C. Amid these developments, recent surveys show that US, European and other Asian company CEOs and boards are spending time considering their China strategies. However, in their effort to align the opportunity and achieve greater partnership balance, there is also increasing concern about the potential risks and penalties involved, which is requiring more thoughtful analysis.

Industrial product company executives thinking about entering China must ask themselves several questions:

- **What do we each bring to the party?** Perhaps most important to ensuring success in China is to not show up empty handed. China is acutely aware that its market is highly attractive to foreign investors, and officials know that this gives them leverage to make demands. Chinese laws and regulations preferentially encourage foreign companies that bring R&D capabilities, advanced technology, other forms of intellectual property, environmental protection systems, innovative manufacturing processes, or a combination thereof to the market.
- **Am I willing to share what I have?** In almost every case, the government aims to take foreign technology and produce its own version. That may be the price of admission to the Chinese market, but not all companies are willing to pay.
- **Am I aware of all potential risks?** The media attention around the recent arrest of four Rio Tinto staff members in China on charges of spying highlights a potential risk of doing business in China.

- **Am I in this for the long haul?** Consider the current and future objectives in China. Do you want to outsource materials/components, or assemble finished products? Or make products for consumption in the local market?
- **Have I clearly mapped all relevant supply routes?** This includes thinking about backup routes or modes of transportation that can be used in the event of a disruption.

Finding the right entry strategy

After a company has assessed its preparedness and feels ready to navigate the various obstacles posed by China's regulatory and logistical infrastructure, it must focus on a strategy that emphasizes collaboration over pure control by adhering to the following practices:

- Harmonize company goals and objectives with those of stakeholders in China. Map out stakeholders in China, beyond factory workers and immediate consumers, to include local, regional, and national government, local community, regulatory bodies, etc.
- Ensure corporate headquarters understands the needs and aspirations of these stakeholders and understands existing and potential conflicts. Where conflicts exist, establish broad guidelines that can be applied and understood by all so that conflicts are resolved strategically rather than tactically.
- Instead of selling specific products, understand the objectives of the local community, such as rural and infrastructure planning, and cater to these needs.

With the emergence of China as a world economic power, its attitude toward international companies' participation has changed. The Chinese people, while providing a source of labor for mass market products, also represent a source of growth. Additional Chinese attributes that should be

understood by industrial products companies considering expansion into China include:

- Chinese firms appear to lag international companies in management processes, value creation for shareholders, and brand perception among consumers.
- Existing Chinese-owned-and-operated companies dominate the low-end market, Western companies predominate the high-end luxury good market, but the mid-level market is up for grabs.
- Since joining the WTO, China has gradually eased its regulatory structure and has become more "corporate" friendly.
- China's new generation of young managers appear to be well-educated and sophisticated. Although they may lack real world training, they eventually will bridge the gap between global multinational corporations and the Chinese market.

PricewaterhouseCoopers' Transaction Services group advises corporations and private equity firms on acquisitions, divestitures, joint ventures, initial public offerings, and other capital market transactions. Our practice consists of dedicated, experienced deal and industry professionals providing financial, tax, and other due diligence advisory services. With global transaction experience serving corporate and private equity clients, we can provide information and assistance to help you choose the right deals and enhance your ability to negotiate with power and control, which could create opportunities for greater returns from transactions. Our integrated M&A services are designed to help you minimize your transaction risks and maximize returns on investments. Our services span your entire deal continuum from target identification and screening to execution to capturing synergies to exit. PwC offers services designed to help you achieve greater returns over your deal continuum.

⁵ "Metals—China demand helps copper rally to 10-month high," *Reuters*, July 27, 2009

Specialty case study:

A European company looks to increase China exports through the acquisition of a Chinese company

Client: global manufacturing company

Client Issue	A European company in the auto repair and equipment manufacturing industry with limited exports into China wanted to acquire an auto repair and manufacturing company based in China to enhance its market exposure. Due to the immaturity of the industry in China, most competitors had built out sales and distribution too quickly, and as a result were now restructuring their networks. Hence there was a lot of “noise” in the system that made any announced figures on number of dealers, sales offices, and sales staff difficult to interpret. Therefore, the client needed to better understand the auto repair equipment industry growth potential and the competitive landscape within the Chinese market.
Approach	A PricewaterhouseCoopers strategy team was engaged to bring about an understanding of the market dynamics, the current installed base of the company’s product types, and forecast the market demand by 2015. The engagement team conducted a primary research campaign, performing more than 100 interviews mainly with end-customers in tier one and tier two cities, including collision repair garages, dealerships, and repair shops. The team also spoke with industry exporters and distributors to identify key purchasing criteria and to compare the target with competitors based on specific criteria.
Impact	The PwC team helped the client understand the market demand for the company’s products. The team also identified key manufacturing and foreign competitors currently importing products into China. The team assessed the strength of the target’s sales and distribution systems versus those of key competitors to assist the client in determining whether acquisition of the target company would result in a competitive advantage.

PricewaterhouseCoopers' industrial manufacturing experience

Deep industrial manufacturing experience

PwC has the leading Fortune Global 500 market share in the industrial manufacturing industry. 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 in solving complex business challenges. Our highly skilled team encourages dialogue 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 having approximately 9,000 professionals who serve the industrial manufacturing industry, our team is part of an Industrial Products Group that consists of more than 28,700 professionals, including approximately 16,700 providing Assurance services, more than 7,000 providing Tax services, and 5,000 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 comprises a global network of industry professionals serving manufacturing clients strategically located in more than 30 countries around the world. 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

June 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.

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