

Los Angeles Business Journal – July 19, 2004

M&A Activity Makes Strong Swing Upward As Normalcy Returns

By AMANDA BRONSTAD

The floodgates finally opened for local mergers and acquisitions in the second quarter as investors demonstrated renewed confidence in the overall economy.

Activity had already picked up earlier this year in Los Angeles County, but the availability of capital and affordable lending options spurred substantially more deals involving private equity funds during the most recent quarter.

In addition, corporate investors – particularly those in the entertainment and media sector – opened their pocketbooks again after several years of belt-tightening.

“The market over the past six months has changed dramatically,” said Scott Adelson, senior managing director of Houlihan Lokey Howard & Zukin. “It’s a return to what appears to be normalcy.”

A total of 137 deals involving buyers or sellers based in Los Angeles County were announced during the second quarter of 2004, according to Greenwich, Conn.-based Factset/Mergerstat, which tracks M&A activity nationwide. Deal volume increased 24 percent from the first quarter and almost 40 percent from the like period in 2003.

In terms of second quarter deal value, L.A. County saw a quadrupling from the previous three months, to \$8.9 billion. Much of the increase comes from two large deals: DirecTV Group Inc.’s \$3.5 billion sale of its PanAmSat Corp. satellite operator unit and Oaktree Capital Management LLC’s \$1.4 billion sale of movie theater chain Loews Cineplex Entertainment Corp.

If these two deals were excluded, the sequential increase in deal value would have been 40 percent, and the year-to-year increase would have been 2 percent in the second quarter.

While deal activity still falls short of the 1999 and 2000 bubble years, L.A. County appears to be doing better than most parts of the country. Looking at all of North America, the number of M&A deals totaled 2,281 in the second quarter, an increase of only five deals from first quarter. Aggregate deal value was \$136.5 billion, down 60 percent from the first quarter, according to Factset/Mergerstat.

“L.A. County does stand out a little bit and tends to be a little healthier because we are middle-market driven,” Adelson said. “It’s far less volatile than larger markets.”

Private equity cycle

In L.A., private equity funds continue to unload large capital holdings raised two to three years ago, said Richard Haigh, principal at private investment bank Mayfair Associates LLC in Los Angeles. Investment cycles of those

funds are nearing their end at a time when available debt has increased and lenders are more willing to take risks.

At the same time, many private equity funds are selling off portfolio companies as their partnerships reach seven- to 10-year maximums, often referred to as “harvest” time.

“There have been, more than I’ve ever seen, a supply of companies coming from portfolios of old partnerships,” Haigh said. “And, in the last six months, they’re selling to private equity buyers. In the old days, private equity sellers would be more likely to sell through a strategic buyer.”

Meanwhile, entertainment, media and other types of companies are dipping their toes back into the dealmaking waters after several quarters of downsizing and cutting costs.

Santa Monica-based Entravision Communications Corp. purchased the Sacramento radio station KBMB-FM, for \$17.4 million, for example, and Liberman Broadcasting Inc. in Burbank purchased KNOR-FM in Krum, Texas for \$15.5 million.

Several investment bankers said the re-entry of corporate investors is a sign the economy’s health is improving and will continue during the year.

Large corporations are still rejiggering their operating portfolios. DirecTV Group’s sale of PanAmSat to New York-based Kohlberg Kravis Roberts & Co. is among a number of assets divested by DirecTV’s parent, News Corp., since it acquired a controlling interest in the El Segundo-based satellite television provider last year. News Corp. sold two other divisions totaling \$331 million during the second quarter.

Oaktree’s sale of Loews Cineplex last month to Bain Capital, Carlyle Group and Spectrum Equity Investors also involved entertainment assets.

“You have players making acquisitions, shifting business models and all trying to re-shuffle,” Adelson said. “Anytime you have an industry going through fundamental change, you’ll have a lot of M&A activity. And media and entertainment is undergoing a significant change.”

Variety of sectors

Other major deals struck during the quarter included the \$740 million sale of Advanced Bionics Corp. to Boston Scientific Corp. in Natick, Mass., and the \$396 million sale of Santa Fe Springs-based shoe manufacturer Vans Inc. to VF Corp. in Greenboro, N.C.

Local big buys include JAKKS Pacific Inc.’s \$116 million purchase of Play Along Inc. in Deerfield Beach, Fla., and Teledyne Technologies Inc.’s two purchases, totaling \$133.3 million, of Isco Inc. in Lincoln, Neb., and Reynolds Industries Inc. in L.A.

Increased deal activity is expected to continue during the year, but some bankers have concerns about the potential negative impacts of rising interest rates and the upcoming presidential election in November.

So far, interest rates have remained low and debt remains affordable. But if interest rates rise sharply, M&A activity may slow. The uncertainty of the election's outcome, may affect deal making, as well.

One investment banker, Robert Bertagna, head of the Los Angeles office of Lehman Brothers, said he expects interest rates and the election to slow deal activity as early as next quarter.

“In terms of our dialogue between CEOs, we’re sensing a leveling out in anticipation of the election,” he said. “If I would project, it could be flat or slightly down.”