

PITFALLS AND PRACTICAL CONSIDERATIONS REGARDING M&A IN RUSSIA

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02.02.2011



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- Selected References

M&A in Russia

- Market overview
- Key Trends and Opportunities
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EVLI CORPORATE FINANCE IN RUSSIA

- In 2008 Evli Bank Plc acquired the strong Russian M&A boutique – Avanko Capital – which has been providing corporate finance and strategy advisory services for foreign and Russian clients since 1996
- 11 corporate finance professionals and 5 research and support staff in St. Petersburg and Moscow
- Focus on the mid-market M&A (from EUR 5 million to EUR 250 million)
- Services: buy-side and sell-side assignments, fund raising and debt restructuring, strategic advice for companies, international organizations and governmental bodies.
- 80% of the projects are cross-border
- Since July 2010 has been working under the Evli brand name

Leading M&A advisors by deal count, 1Q-3Q 2010		
Rank	Advisor	Deal count
1	Morgan Stanley	12
2	Goldman Sachs	5
3	J. P. Morgan	3
4	PricewaterhouseCoopers	3
5	Evli Bank	3
6	BMO Capital Markets	2
7	Credit Suisse	2
8	ING	2
9	Renaissance Capital	2
10	HSBC Bank	1

Source: mergemarket

Leading M&A advisors by deal count, 2009		
Rank	Advisor	Deal count
1	Deutsche Bank	6
2	Troika Dialog	5
3	Renaissance Capital	5
4	Gazprombank	5
5	J. P. Morgan	4
6	Avanko Capital (Evli Bank)	4
7	PricewaterhouseCoopers	3
8	Citi	1
9	Dashevsky & Partners	1
10	NM Rothschild & Sons	1

Source: mergers.ru

















CORPORATE FINANCE IN OTHER CIS COUNTRIES

- Supporting M&A projects in other Russian speaking CIS countries, first of all Ukraine, Kazakhstan, Belarus, and Moldova.
- In addition to the common language our team enjoys good knowledge of the local cultures and business contact networks that are closely interconnected with Russia.
- The countries of Ukraine, Kazakhstan, and Belarus (70% the total GDP of the rest of CIS) due to cultural and operational closeness, in many cases, are also the natural options for expansion together with Russia.










	Russia	Ukraine	Kazakhstan	Belarus	Moldova
Population, 2009, mn	139.4	45.4	15.4	9.6	4.3
GDP per capita, 2009, \$	15,100	6,300	11,800	12,500	2,300
Average GDP growth rate, 2000-2009, %	5.4	4.7	8.6	7.2	4.7

















EVLI'S SELECTED CF REFERENCES IN RUSSIA (1/3)

<p>October 2010</p>  <p>Coveright Rus has been sold to Interprint</p>  <p>The undersigned acted as Financial Advisor to the Seller</p> <p>EVLI ANGERMANN</p>	<p>September 2010</p>  <p>Fortum has sold Tyumenregionport</p>  <p>The undersigned acted as Financial Advisor to the Seller</p> <p>EVLI</p>	<p>September 2010</p>  <p>Fortum has sold its stake in Sare-Piteburg Sale Company</p>  <p>The undersigned acted as Financial Advisor to the Seller</p> <p>EVLI</p>	<p>March 2010</p>  <p>Fortum has sold block of shares in Federal Grid Company</p>  <p>The undersigned acted as Financial Advisor to the Seller</p> <p>EVLI</p>
<p>March 2010</p>  <p>Fortum has sold its stake in Kurgan Generation Company</p>  <p>The undersigned acted as Financial Advisor to the Seller</p> <p>EVLI</p>	<p>February 2010</p>  <p>The undersigned rendered financial advisory services to Evli Property Investments in valuation of its assets in Russia</p> <p>EVLI</p>	<p>December 2009</p>  <p>Skamol A/o has acquired a majority interest in Distriovoy Kontol</p>  <p>The undersigned acted as Financial Advisor to the Buyer</p> <p>EVLI</p>	<p>November 2009</p>  <p>The undersigned rendered strategic advisory services to Kolar Food in assessment of strategy development options in Russia</p> <p>EVLI</p>

EVLI'S SELECTED CF REFERENCES IN RUSSIA (2/3)

<p>November 2009</p>  <p>A part of Naftodizel Retail Chain has been sold to X5 Retail Group</p>  <p>The undersigned acted as Financial Advisor to a Seller</p> <p>EVLI</p>	<p>September 2009</p>  <p>Suomin Laittehuolto has sold its Russian subsidiary to Tanelo</p>  <p>The undersigned acted as Financial Advisor to the Seller</p> <p>EVLI</p>	<p>April 2009</p>  <p>Sportland Russia has been sold to Intersport Russia</p>  <p>The undersigned acted as Financial Advisor to a Seller</p> <p>EVLI</p>	<p>December 2008</p>  <p>Brainpower has been sold to BPI Group</p>  <p>The undersigned acted as Financial Advisor to a Seller</p> <p>EVLI</p>
<p>September 2008</p>  <p>Fazer has acquired a landlot for construction of a bakery plant from Ukraina Zavod</p>  <p>The undersigned acted as Financial Advisor to the Buyer</p> <p>EVLI</p>	<p>September 2008</p>  <p>Avanta Personnel has been sold to Adecco</p>  <p>The undersigned acted as Financial Advisor to a Seller</p> <p>EVLI</p>	<p>December 2007</p>  <p>Nefco has sold its stake in waste-processing company to Russian investors</p>  <p>The undersigned acted as Financial Advisor to the Seller</p> <p>EVLI</p>	<p>September 2007</p>  <p>Kuoni Travel Holding has acquired UTE Moskau</p>  <p>The undersigned acted as Financial Advisor to the Buyer</p> <p>EVLI</p>

EVLI'S SELECTED CF REFERENCES IN RUSSIA (3/3)

<p>November 2006</p>  <p>Troya Ultra has been sold to Lohedensky</p>  <p>The undersigned acted as Financial Advisor to a Seller</p> <p>EVLI</p>	<p>October 2006</p>  <p>Fortum has acquired shares in the Russian leading heat and electric energy producer</p>  <p>The undersigned acted as Financial Advisor to the Buyer</p> <p>EVLI</p>	<p>May 2006</p>  <p>Rautasko has acquired certain assets from Lenta</p>  <p>The undersigned acted as Financial Advisor to the Buyer</p> <p>EVLI</p>	<p>May 2006</p>  <p>MLP-KAD has been sold to MLP (Multinational Logistics Partnership)</p>  <p>The undersigned acted as Financial Advisor to a Seller</p> <p>EVLI</p>
<p>January 2005</p>  <p>A non-core assets of JT International Paper has been sold to Henry Chichester</p>  <p>The undersigned acted as Financial Advisor to the Seller</p> <p>EVLI</p>	<p>January 2005</p>  <p>Atria Group has acquired P&Product</p>  <p>The undersigned acted as Financial Advisor to the Buyer</p> <p>EVLI</p>	<p>June 2004</p>  <p>Fortum has acquired shares in Leningrad</p>  <p>The undersigned acted as Financial Advisor to the Buyer</p> <p>EVLI</p>	<p>February 2004</p>  <p>Rautasko has acquired Snyomaster</p>  <p>The undersigned acted as Financial Advisor to the Buyer</p> <p>EVLI</p>

LEADING RUSSIAN M&A ADVISORS, 2009-2010

Leading M&A advisors, Q1-Q3 2010		Leading M&A advisors, 2009		Best investment bank, 2010*		
Rank	Advisor	Rank	Advisor	Rank	Advisor	Notes
1	Credit Suisse	1	Deutsche Bank	1	Evli Corporate Finance	35%
2	VTB Capital	2	Troika Dialog	2	VTB Capital	17%
3	UBS	3	Renaissance Capital	3	Goldman Sachs	9%
4	Evli Corporate Finance	4	Gazprombank	4	Troika Dialog	7%
5	Pollyanna Capital Partners	5	J. P. Morgan	5	Renaissance Capital	6%
6	Renaissance Capital	6	Avanko Capital (Evli Group)	6	Pollyanna Capital Partners	6%
7	Baker Tilly Russaudit	7	PricewaterhouseCoopers	7	J. P. Morgan	4%
8	Gazprombank	8	Citi	8	UBS	3%
9	Advance Capital	9	Dashevsky & Partners	9	Gazprombank	3%
10	Ernst & Young	10	NM Rothschild & Sons	10	PricewaterhouseCoopers	3%

Source: Mergers.ru

Source: Mergers.ru

* - more than 250 financial specialists has taken part in on-line poll organized by independent analytical agency mergers.ru

Note: the league tables do not include Captive transactions and Transaction support services

LEAGUE TABLES OF RUSSIAN M&A ADVISORS, Q1-Q3 2010 RESULTS (1/2)

Leading M&A advisors by deal count*			Leading M&A advisors by deal value*		
Rank	Advisor	Deal count	Rank	Advisor	Deal value (kUSD)
1	Evli Corporate Finance	4	1	Credit Suisse	6 400
2	Polyanna Capital Partners	4	2	VTB Capital	5 542
3	Renaissance Capital	3	3	UBS	5 639
4	Baker Tilly Russaudit	3	4	Renaissance Capital	1 556
5	Credit Suisse	2	5	J. P. Morgan	900
6	VTB Capital	2	6	Sloan Square Capital Partners	395
7	UBS	2	7	Gazprombank	300
8	Gazprombank	2	8	Evli Corporate Finance	150
9	Advance Capital	2	9	Advance Capital	140
10	Ernst & Young	2	10	Baker Tilly Russaudit	100

* - data as of 14 November 2010

Source: Mergers.ru

* - data as of 14 November 2010

Source: Mergers.ru

Note: the league tables do not include Captive transactions and Transaction support services

EVLI Corporate Finance in Russia

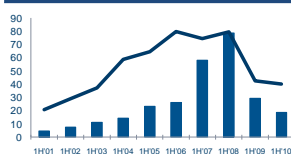
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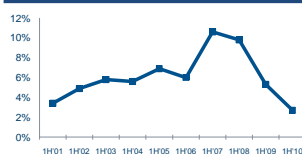
M&A MARKET IN RUSSIA

M&A Market Volume, 1H 2001-1H 2010



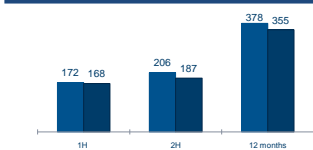
Source: Mergers.ru

M&A Market Volume/GDP Ratio, 1H 2001-1H 2010



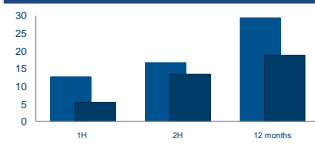
Source: Mergers.ru

Number of M&A Deals, 2009-2010



Source: Mergers.ru

Deals Volume, BUSD, 2009-2010

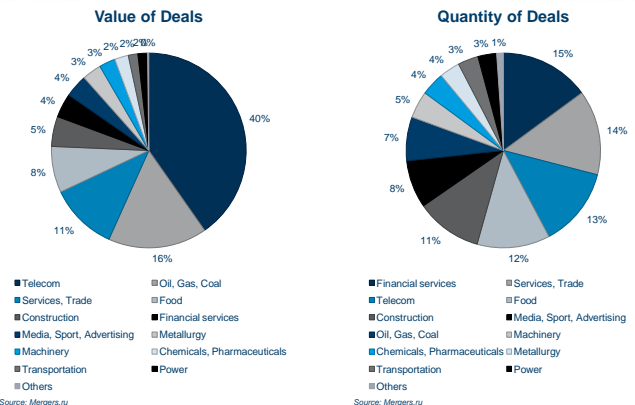


Source: Mergers.ru

M&A MARKET IN RUSSIA

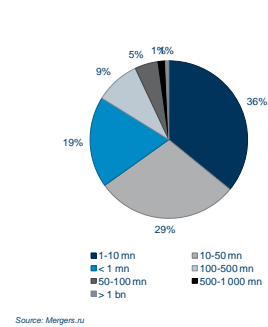
- The volume of M&A market in H1 2010 accounted for 2.7% of GDP
- Slight decrease in number of deals: 355 closed deals vs. 378 deals in H1 2009
- M&A market volume in money terms dropped.
- Aggregate value of transactions amounted to 18.7 BUSD (decline of 36% as compared to H1 2009).
- Valuations are lower and will sustain on that level for a while.
- Large-scale deals still dominate the market in size.
- Growing share of middle market.
- Most value falls at telecoms (40% of total volume) – Vimpelcom has acquired KievStar, the Ukrainian mobile operator
- Cross-border acquisitions dropped in line with the market.
- Expectations grow faster than economy recovers

BREAKDOWN BY SECTORS



INVESTMENT BANKING & WEALTH MANAGEMENT

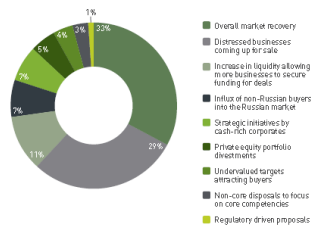
BREAKDOWN BY DEAL VALUE (NUMBER OF DEALS)



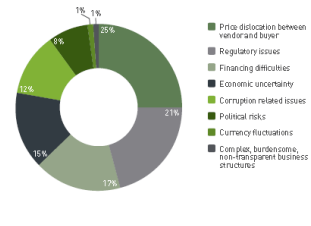
INVESTMENT BANKING & WEALTH MANAGEMENT

M&A MARKET IN RUSSIA: CURRENT ISSUES (1/4)

What do you think will be the primary deal driver to Russian M&A activity?



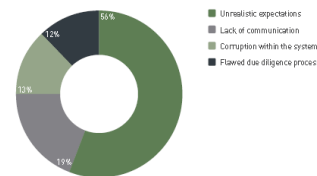
What do you think will be the primary obstacles to Russian M&A activity?



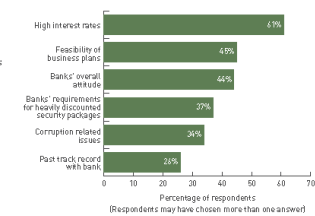
INVESTMENT BANKING & WEALTH MANAGEMENT

M&A MARKET IN RUSSIA: CURRENT ISSUES (2/4)

What in your opinion is the most important factor leading to the failure of an M&A transaction?



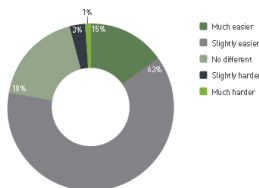
What are the biggest challenges Russian businesses are facing when trying to secure funding?



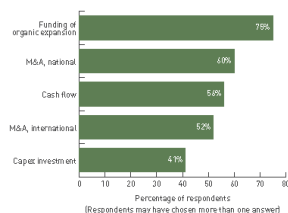
INVESTMENT BANKING & WEALTH MANAGEMENT

M&A MARKET IN RUSSIA: CURRENT ISSUES (3/4)

Compared to 12 months ago, how would you describe the current financing situation?

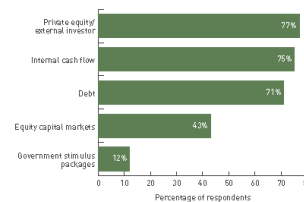


What are Russian companies currently seeking funding for?

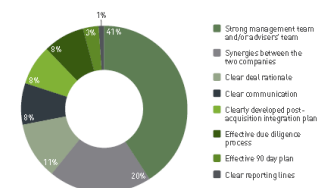


M&A MARKET IN RUSSIA: CURRENT ISSUES (4/4)

How do you expect the majority of Russian buyers to finance their acquisitions over the next 12-24 months?



What, in your opinion, is the most important factor leading to the success of an M&A transaction?



CONSIDERATIONS REGARDING M&A IN RUSSIA (1/2)

Key Considerations	Implications/comments/recommended actions
Tax optimization Russian companies quite often employ aggressive tax optimization schemes.	- implied risk and legalization costs assessment; - analysis of impact of termination of tax optimization on the business model; - normalization of accounts for valuation purposes; - preparation of the legalization plan.
Reporting – statutory vs. management Companies usually have two kinds of accounting – statutory for tax authorities and management for internal use. They may differ substantially.	- analysis of the principles behind management accounting (quite often a mixture of CFS and P&L); - transformation and normalization of accounts; - valuation based on normalized management accounts; - listing of main assumptions in the LOI.
Complicated business structures Dozens of legal entities might serve one business and one legal entity might operate a number of businesses.	- analysis of costs/benefits (Russia specific risk management vs specific business conduct risks management); - re-defining scope of the transaction (before DD); - restructuring of the business as a precondition for completion as according to the separate plan.

CONSIDERATIONS REGARDING M&A IN RUSSIA (2/2)

Considerations	Implications/comments/recommended actions
Limited financial skills Limited understanding of the key concepts and terminology of M&A reflected in the normal SPA (EV, Net Debt, reps and warranties, "business as usual", "arms length", indemnities, etc)	- owners need extensive explanations; - owners need time to grasp/digest the ideas; - presence of owners' professional advisors (especially lawyers) helps a lot.
Owners often have very operational views Owners quite often play the core role in the business of a target, understanding the role of Company as a part of bigger set-up might require significant efforts.	- assessment of real role of the owners in the business; - structuring the earn-out proposition (time, performance yardsticks, authority, control, succession plan, etc); - planning and formalization of business processes; - analyzing the impact on business from the normalized accounts.
Renegotiations in the course of the process It should not be a surprise if the owners would start renegotiating the price and other conditions even though they have been agreed in a signed LOI due to various reasons. They learn in the process.	- good speed of the process is the key to success; - if the seller is squeezed too much at the LOI stage it may backfire during the process via renegotiation of terms; - ensure that lawyers and auditors have enough resources and motivation to work hard and fast; - normally it pays to make the signing documents detailed and have number of respectable witnesses/advisors at place of signing; avoid "face losing" if renegotiation starts by the Buyer.

CASES

Failure	Success story
<ul style="list-style-type: none"> 1993 - the company entered the Russian market with opening one store in St.Petersburg. It pioneered in the Petersburg's market in the modern retail format, was very successful in the first years of operations, and defined the development of many Russian players. Still no further expansion was made. In 1995 and 2005 – two more stores opened, no clear expansion strategy was adopted, very little action in practice. From mid 90s the excellent starting point has gradually evaporated, the appeal and consequently market share was lost to the Russian competitors. In 2006 as a first try to establish a meaningful presence in the market the company considered an acquisition of a local player. The deal was finally abandoned after long consideration due to high entry barriers at that time. In 2009 the company exited its loss-making operations in Russia by selling its shops to a Russian investor. <p>The main reason for failure: passive approach and attempt to averse risk as much as possible</p>	<ul style="list-style-type: none"> 2005 – The Company expanded into Russia by acquiring a strong regional player (#3), retail chain. 2006 - the first store operating in line with the new concept was opened. The existing stores of the chain were converted to the acquirer's brand since August 2006. In 2009 the first new hypermarket was opened in Yaroslavl, in 2010 – in Tula and in Kaluga. Total investments in the Russian market accounted for about EUR 100 million. The Company's sales grew by 47% and about 30% correspondingly in 2007 and 2008. 17% market share in the first location The company actively looks for locations in Volga and Central regions on Russia Another business unit of the acquirer is seeking to benefit from established platform <p>The main reason for success: active consistent position and moderate, well-timed risk taking</p>

Do's

- Be ready to modify your business model in accordance with local specifics
- Be prepared to move quickly once a good opportunity has been open
- Be ready to take reasonable risk and do not wait until all uncertainties are completely cleared up – the latter never happens
- Learn the Russian management practices – there are nuances very important for success in the local market
- Have enough management capacity and advisory resources to invest into cases when a breakthrough is needed
- Try to understand and quantify growth potential. None can afford not to take future growth into account when buying a successful company in Russia.
- If your today's valuation does not correspond the sellers expectations – stake on an aggressive earn-out proposal.
- Be ready to invest in development of the business – stable market share is not about Russia where customers' preferences and incomes change every year

Pitfalls

- Preparation phase
 - Identifying of the right targets is carried out too quickly, is based on public information, little additional work is made outside the traditional domain
 - Timing and complexity of deal is underestimated
 - Overestimation of potential synergies and effects from the deal
 - Underestimation of local diversity and practices, of importance of local connections and the system of relationships.
- Deal phase:
 - Cost of due diligence and analysis,
 - Resources,
 - Deal structure and legal set-up (motivation, possibility to exit, reps and warrants etc),
 - Controlled risk taking,
 - Time management.
- Post-merger integration:
 - Underestimation of timing, complexity, amount of effort to fix things
 - Availability of capable management



"If the facts don't fit the theory, change the facts."

Albert Einstein



*"Someone's head is going to roll for this!"
The Duchess. Lewis Carroll.
Alice in Wonderland.*



"We can't solve problems by using the same kind of thinking we used when we created them."

Albert Einstein



"We learn from experience that men never learn anything from experience."

George Bernard Shaw

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