

The New Wave of Mergers and Acquisitions

A Road Warrior Group(RWG) Whitepaper by Jeff Weigel

Abstract: *Using mergers and acquisitions as a way to contain research and development cost is diagnosed. Through several case studies, lower cost and more effective ways to research, negotiate and structure acquisitions are reviewed. The skill sets to put this next wave of M&A activity is examined.*

A new way of looking at it: The current worldwide market meltdown is accelerating our clients' interest in growing products and capabilities through the judicious acquisitions of organizations not well positioned to survive in the new market reality. This is a cost containment, rather than time to market strategy. Simply, it can be cheaper to acquire new products and capabilities than it is to develop them internally. Product positioning, detailed market analysis, product compatibility, time to revenue and risk assessment are critical to success. Traditional investment bankers are not generally positioned to find, evaluate and structure this round of acquisitions. The Road Warrior Group (RWG) is. Lets look at the differences.

Case study: In this environment a shotgun M&A approach doesn't work. Each discussion needs to be targeted at how the acquired company fits into the acquiring company. It is more than just an analysis of product features. A detailed look includes introduction timing, manufacturing technology, manufacturability, design environment, interoperability with current products, market acceptance, risk factors, price targets, impact on total and served markets. In 2007 the RWG worked with a twelve person Swedish firm to find an acquiring company. We presented the company to a limited number of targeted companies in three distinct market areas. Every presentation was customized to how we saw our client's product fitting into the targeted company's strategy. Conversations started at a much higher level and, by doing our homework, we were able to structure an acquisition where the software offering from the target acquirer bundled with the hardware product of our client had a market value much higher than the two stand-alone offerings.

In June of 2007 Synplicity announced the acquisition of HARDI Electronics for \$24.2M, or \$2M per employee. The addition of HARDI's hardware prototyping capability opened a whole new emulator market for Synplicity. A year later, based largely on this new capability, Synplicity was acquired by Synposys for \$220M. When you get the strategy right, everybody wins. For more information see "1 Day Business Development: A navigation tool from the start to finish" by Doug Lyons - another white paper on this site.

The size of the deal: The acquisition of HARDI Electronics in 2006 was a relatively small acquisition. Many of the acquisition targets today are companies that have paired down both their product definition and their operating costs to

the bare minimum – and still can't quite see a path to a stand-alone cash break-even operation. Couple this with the all time low market values of the potential acquiring companies and one soon understands that these bargain basement deals require more marketing understanding and strategic development. Further, they will not support the traditional investment banker fee plus five percent cost. Success requires a deal that provides lower costs, lower risks and a shorter time to return as compared to organic research and development.

Looking in unique places: The RWG is working with a publicly traded semiconductor company to acquire a team in a new market area that our client will be entering in 2010. It was relatively straightforward to identify six start-up companies that, at first pass, could meet our client's profile. It took a little longer to find three semiconductor companies that would consider selling off one group of their company. It took even longer to find two equipment companies with internal semiconductor design organizations that would consider breaking them off. This ongoing worldwide search is breaking new ground to find the right solution. We are in discussions with organizations in Germany, Greece, Egypt, Denmark, Ireland, The United Kingdom and the USA.

Success in this type of search depends on the nuances of strategic product integration. It takes the experience and skills acquired through over 30 years in technology business management to work independently discovering and qualifying potential targets before revealing the client's identity. Product strategy, market development status, risk analysis and current market value need to be openly discussed and evaluated – with the structure of the deal becoming a natural extension of this analysis.

Marrying new capabilities: In another semiconductor search a new strategy is being employed. Our client is looking to acquire a well-positioned FPGA Design House. Once considered a competitive design approach, the evolution of encrypted FPGAs, intermediate -lower cost structured cell implementations and FPGA to full custom design conversion tools have made selling FPGA implementations a viable product strategy for semiconductor companies, especially as the first step in a roadmap to a full custom implementation of a standard product. Some forward-looking semiconductor companies have embraced this approach. Looking to acquire well-positioned design houses, however, is new to the industry. It's success will ride on the technical and operational detail as well as the business culture of the design house. An understanding the quality of the intellectual property of the design house is key. Maybe more important, however, is the ability of the design house to develop, verify and document standard IP blocks and to lead customers toward standard solutions - to work as the leading edge of a semiconductor company's product portfolio. This kind of search requires an understanding of the markets,

applications, strategies and business cultures of both the client company and the design houses being considered.

Term sheets and legal council: The cleanest way to effect an acquisition is to generate and negotiate a draft of the term sheet before lawyers on either side are involved. Once mutual business terms are agreed its time for legal review. There are talented legal services available without the overhead cost of a major firm. For legal council in the HARDI acquisition we recruited an ex-Brobeck, Phleger & Harrison, LLP lawyer who had started his own practice. Both HARDI got the talent of a senior partner of a large, experienced law firm without the overhead cost. Transactions are straightforward when a private company, such as HARDI is acquired. In cases where a public company seeks to acquire another public company the disclosure rules are very specific and so in this case we've worked with an investment banker advisor.

Getting real on value: We all remember fondly when leadership product start-up companies could demand ten times forward sales projections as an acquisition price. Today two to three times actual sales, with a clear, short-term path to cost breakeven is more the current reality – if a buyer can be found. The danger for start-ups today is in waiting too long before finding a harbor. The value of a company drops dramatically as it runs out of runway.

A current client of ours, not that long ago, acquired a start-up processor company for less than \$5M. This foreclosure price was a fraction of the original proposed price put on the table less than six months earlier. The start-up waited too long.

Marks of excellence: The skill set that is required to put together this generation of mergers and acquisitions are:

- An understanding of product market strategies
- The ability to look at two market positions and find common ground
- A practical understanding of market timing and customer risk analysis
- A hands-on feel for how things could fit together
- A realistic understanding of market value
- A feel for the motivations and business cultures of organizations
- The ability to work with both acquirer and acquiree in crafting a winning term sheet

The days of shot-gun investment banker led acquisition searches are gone. Strategy grounded in current market reality is driving this next round of deals. Financial evaluation is secondary to practical success analysis. This is a place for gray haired long-term technical market executives who can work confidentially and independently of their client to evaluate potential opportunities. This is a

place for market participants who can call on their years of experience and contacts to focus on survival approaches to put things together. This is a place for the Road Warrior Group.

About the Author: Jeff Weigel's experiences, prior to forming the Road Warrior Group in 2001, include Managing Director – Europe and Vice President of Strategic Customer Sales at Vitesse Semiconductor. Prior to Vitesse, Jeff was Vice President of GARCO, a subsidiary of National Semiconductor. He started his sales career at Motorola Semiconductor where he instituted a country-wide independent sales program for emerging systems products. He gained his engineering experience at Westinghouse and Vitro Labs.



Jeff has spoken to groups world-wide about penetrating North American markets, the evolution of product in start-ups, effective sales organization structure, recruiting and motivating independent sales representatives and the marks of excellence in sales management.

Jeff has a BSEE from Lafayette College and 30 years of Electronics industry experience.

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