

# COMPLETION

*Getting deals done with Baker Tilly Corporate Finance*

*Issue 4*

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# WELCOME

In 1939 the slogan 'keep calm and carry on' stood for a strand of British stoicism in the face of the unthinkable – even if the public never saw it. That the Second World War propaganda poster is undergoing a revival speaks volumes about the sense of unease among businesses of all kinds.

In this issue of *Completion*, we step back, take stock and examine the main source of panic – the credit squeeze – offering practical guidance on how to survive, plan ahead and find fresh sources of finance (page 6).

Amid the prevailing anxiety, there's brighter news for those companies with cash and the courage to act. We hear how conditions are right for potential purchasers of struggling – but fundamentally strong – businesses (page 10).

Despite reports of its demise and an extremely tough 2008, AIM still has the fundamentals to continue and come back even stronger. Baker Tilly's Chilton Taylor responds to those who are reconsidering their support (page 12).

Predicting what will happen in the economy next is fraught with difficulty. We get a clear-headed view of where the recession is heading from one of the country's most respected economists, HSBC's Dennis Turner (page 18).

"The recession will end, because recessions always do. The businesses that will take advantage will be those that are getting in shape now and preparing for it," says Turner.

It is a note of reassurance and reason that should strike a chord during difficult times.

In the centre of this issue of *Completion* you will find a reader-reply card. We'd like to help you keep calm and carry on.

*Baker Tilly Corporate Finance Team*

# NETWORK

News and views from the front line

## Moving on up

As a common identity becomes a reality for its 145 independent members worldwide, Baker Tilly International CEO and President Geoff Barnes explains where the network is heading...

### **On why a common identity is important**

In 2001, we were called Summit International Associates. We wanted an identity that would grow with us as the network became global – and the Baker Tilly brand was chosen. In just seven years, the name has been adopted in more than 90 countries and has now arrived in the US. Reaching this level of recognition has been a major push for us. In this time, we have moved from the 14th to the eighth largest accountancy and business advisory network, and our commitment to achieving excellence is now recognised on a global scale.

### **On where national markets are growing**

We are in all of the world's major financial centres – and 110 countries in total – and like all global organisations, we are faced with the challenges presented by the downturn. But pockets of buoyant activity remain; our member firm in the Netherlands, for example, is enjoying a stable period because the economy isn't linked to the financial services industry in the same way many other economies are.

While Germany's economic health is faltering, Baker Tilly Deutschland has a strong restructuring practice and is reaping the rewards of a turbulent marketplace.

I was in five Indian cities recently and while their economy is also facing major issues, they are talking about growth dropping from 9% to 7%. I only wish we had that in the UK.

### **On marrying ideas with clients**

Our firms are fully fledged businesses in their own right, with sophisticated hierarchies and techniques. Each places importance on quality and is an expert in their marketplace.

Ideas from one country can be transferred to another – a big part of the network is the transfer of knowledge and skill sharing. At our world meeting in Tokyo last October, my message was clear. Now is the time to identify ways in which to help clients continue to meet their objectives without checking on the "work in progress" meter.

**On new business opportunities**

The core of our members' business is the provision of audit and taxation services, and I see this continuing. Opportunities exist in other service areas, such as forensics and corporate restructuring. And demand for our management consultancy services has rocketed as firms look to improve their performance in testing times.

The question of choice in a downturn is important. For some years, the business community has been looking for an alternative to the Big Four – and we want to be recognised as the network of choice for the middle market. The question is what is the “middle market”? I'm talking about large entrepreneurial, family businesses and listed companies with a market capitalisation of up to \$10 billion. It's a market that presents real opportunity for us to make our mark.

**On making 'exciting' investments**

Excitement isn't a word often associated with accounting, but I'm excited by the investment that has been made in the network by our members. By investment I don't just mean money, but also sharing intellectual property and time commitments.

In May, we're embarking on a global leadership development programme that is open to all of our members worldwide and designed in partnership with leading business school the University of Chicago, Booth School of Business. I'm intricately involved in designing the programme and am excited about what we are doing.

We're creating the global leaders of tomorrow in our profession, and there aren't too many networks that are doing this. We believe the calibre of our people is a fundamental part of our future strategy. Many organisations are talking about the importance of their people, but we are proud to say we are taking concrete action to demonstrate our commitment.

**On why his schedule gets his adrenaline going**

I'm out of the country for 250-260 days in the year. I spend that time talking to partners and staff in our member firms, our members' major clients, potential merger candidates, the press and the business community. At times, the schedule can be a killer. But I'm ambitious about what we can achieve and that keeps the adrenaline pumping. I am passionate about what we're trying to do in the network and how we are positioning ourselves as a real global player – that is what's driving me and our member firms.

## ALL LOCKED UP

Baker Tilly has advised G4S plc, the FTSE 100-listed security specialist, on the sale of its French businesses. Baker Tilly acted as lead adviser, including running an international auction, deal structuring, negotiations and restructuring analysis.

G4S Holdings (France) was sold in February to Neo Securite, a management buy-in team led by Jean-Michel Houry, previously a senior executive of Brink's Europe. The transaction concludes the divestment of the G4S businesses in Germany and France. Baker Tilly previously advised G4S on the exit of its German cash services businesses.

"The transaction required a hands-on and commercial M&A approach – it was a complicated business facing market challenges coupled with specific French regulatory issues," says Paul Elliot, Corporate Finance Partner at Baker Tilly.

He explains that the deal underlines Baker Tilly's ability to help listed groups exit complex businesses. "These deals require a lot of effort. The businesses involved might be small in the scheme of things but they often take up disproportionate management time. We know how to negotiate complicated commercial issues for businesses facing challenging outlooks, of which there are currently many examples. We also have a lot of experience of structuring deals to cope with complex situations, turnarounds and accelerated situations, together with relationships with specialist funds and other buyers who focus on difficult events."

## POLISHING A GEM

Baker Tilly's Newcastle team has advised one of the country's fastest-growing IT companies as it continues its rapid expansion.

Onyx Group, which specialises in managed networks, hosting, security and services recently completed a programme of strategic acquisitions to increase its national presence and widen its portfolio of expertise.

"The technology services marketplace is incredibly fragmented and crowded," explains Neil Stephenson, Onyx Group Chief Executive Officer. "We saw an opportunity to acquire complementary businesses, and improve our ability to cross-sell."

Onyx Group employs 100 people and has annual revenues of £15 million. It has three Scottish offices, two in north-east England and a further site in Slough. The company also manages data centres in Newcastle, Middlesbrough and Glasgow, with workplace recovery facilities in Newcastle and Glasgow and an international base in Dubai.

Onyx appointed Baker Tilly in September last year as lead adviser to assist with fundraising. Corporate Finance Partner Angela Toner and her team worked with Finance Director Tim Clark to create a compelling proposition for potential investors and help Onyx raise equity and debt.

"Onyx are bucking the trend," says Toner. "Investors can see that they have a track record of making good acquisitions and integrating them quickly."

The acquisition of Dundas IT, a managed IT services firm in Edinburgh in November last year was the the final piece in the acquisition jigsaw, according to Stephenson.

"Baker Tilly understood our business – our strengths and weaknesses," he says. "It felt like they were one of us. They put together a fantastic presentation for external funders. They were part of the whole process and gave constructive advice, rather than simply following a brief."

Baker Tilly has recently been appointed by Onyx to conduct financial due diligence on a target. "It shows that Onyx understands our wide range of capabilities," says Toner.

## RUNNING THE NUMBERS

### Baker Tilly and Feagre & Benson AIM Survey

**74%** of companies would still have listed on AIM , even if they knew how difficult 2008 would be

**67%** of companies expect to see market consolidation in 2009

**82%** of AIM investors consider UK companies to be more attractive than international concerns

**61%** of AIM companies believe their profile on AIM was either of some or of major benefit in 2008

# NO TIME TO PANIC

Companies faced with a lack of credit over the next 18 months need to keep their heads – and find creative ways to survive

**WORDS:** Joanne Hart

When the sky is blue and the sun is blazing, it is hard to imagine ever feeling cold again. And when the trees are bare, sleet is falling and the weather is grim, summer seems a distant memory.

Whatever the external environment, the climate for most companies is very bleak indeed. The carefree days of the mid-noughties, when business was booming and cash was plentiful, seem a long way away. Profligate banks have come down to earth with a bang.

Now they are either at the mercy of the Government or demanding shareholders. They are under pressure to rebuild their balance sheets – by lending less and charging more.

To many innocent victims of this credit squeeze, the banks' behaviour seems at best unfair, at worst malevolent. But for companies in need of cash, moaning about the situation won't help. Managers need to be creative and find alternative ways of survival. This is not easy.

"Businesses of all shapes and quality are facing a terrible squeeze on cash. The problem is that everything has happened at once. Trading is under pressure, banks are withdrawing credit, and many lenders, most obviously the Icelandic banks, are leaving the country," says Rob Donaldson, Head of M&A and Private Equity at Baker Tilly.

"Even in good times, there are four basic ways of raising money: go to a bank; use the public markets; use private equity; or dispose of non-core assets. All of these are less attractive than they used to be," he adds.

## Comforting noises

In other words, the situation is tough, as every business looking for credit knows only too well. But it is not impossible. There are ways of surviving the credit crunch, and those businesses that do so will almost certainly emerge stronger and fitter than ever before.

The first, and most obvious advice, is to stay calm. It is easy to become panicked when the economy is nosediving, profits are falling and banks are running scared. But taking stock and creating a strategic plan of action can be helpful for the owners of a business and their employees. It can also be reassuring for bank lenders.

"Businesses need to plan much further ahead. If they have bank facilities coming up for renewal, for instance, they should start thinking about how these will be refinanced six to 12 months ahead of time. They should talk not just to their existing lenders but to others as well," says Donaldson.

"This is particularly important as some credit teams are paralysed. They are unsure of what is happening further up the chain of command so they can make comforting noises initially and ultimately have to say no. In other words, you cannot rely on warm words from your relationship manager," he adds.

Talking to a range of banks can be helpful in more ways than one. Many banks are reluctant to take responsibility for an entire facility, but they may feel happier sharing the load.

"Club deals are increasingly common where two or three banks come together and share a transaction," says Donaldson.

Enterprising business managers bring banks together themselves, rather than waiting for the banks to find each other. And some banks are more open to deals than others.

"The Scandinavian banks are in better shape than many Europeans, and the UK banks may begin to soften up, following concerted government action to make them lend more to small and medium sized businesses," says Donaldson.

Many businesses have already found it helpful to change banks and use new lenders. "Some banks do still have money to lend. We did several deals last year and got bank debt on all of them. The situation changes from month to month but some banks will do business with the right customers, and some want to exit certain areas but get more involved in others," says Richard Chapman, Director at mid-market private equity firm ECI Partners.

There are other borrowing options as well. Certain private equity firms are now offering debt finance not just to firms within their portfolio but to external companies as well.

## Open for business

"We raised a £50 million debt-focused fund last autumn and we are now offering a 'breathing space' product that companies can use to refinance an overdraft or make acquisitions and that private equity firms can use if they need debt finance," says Andrew Cavaghan, Director at investment company Octopus Investments.

The Octopus product is more flexible than most bank loans.

"It is a five-year non-amortising loan with nil capital repayments till maturity. We charge a margin over Libor in the early years, and the terms are similar to those on offer from a bank. Borrowers can repay after two years but if they choose to continue, the facility incurs an increasing interest rate similar to mezzanine finance. Clearly, the precise terms are dependent on the business and the quality of its earnings," says Cavaghan.

The 'breathing space' product offers businesses up to £4 million and the average amount taken so far varies between £1.5 million and £3 million. Demand has been strong, and Octopus is aiming to raise a further £25 million for the underlying fund.

"We are much more flexible than most banks. If a company is doing well and wants to repay the debt, that's fine. If they are not doing so well, we can adjust the return to reflect the risk. There is less confrontation involved," explains Cavaghan.

Mezzanine-type finance is part of the Octopus product, and it is also available from other lenders, in various guises.

"Mezzanine finance is on offer from specialist funds and niche lenders. It is more expensive than straightforward loans, but it is out there. It also tends not to involve any ongoing capital repayment," explains Chapman.

Private equity is an option in itself for companies in search of cash.

"Private equity firms will do a deal without bank debt if the transaction looks suitable. There may be a chance of bank debt materialising in the future, or a company's growth prospects may be sufficiently attractive to do a deal without any recourse to bank funding," says Chapman. "It is also possible for private equity firms to take a minority stake without bank debt."

Private equity firms are as cautious as any investor in the current climate but they are certainly open for business and some are specifically focused on helping companies in trouble.

"Private equity firms still have a fair amount of cash, and they are willing to invest in the right opportunities. If a business thinks they have funding needs coming up in the next two years, it is worth building up relationships with private equity firms now," says Donaldson.

"And some funds are looking at distressed situations in particular," he adds.

Private equity may seem a radical option to some businesses as firms tend to take a seat on the board and become involved in companies' planning and direction. But the rewards can be generous and private equity can provide valuable support.

"There are plenty of examples of companies turning down offers and then regretting it. Of course, prices are lower than they were, but they may go lower still," says Donaldson.

One funding option that is gaining traction among certain businesses is asset-based lending.

"Invoice discounting, and asset-based lending generally, can be an interesting way of raising capital. It is a lower-risk option for a bank because it is asset-backed, and for some companies, such as recruitment businesses with lots of contract workers, it is ideal," says Chapman. ■

## THREE STEPS TO FRESH FINANCE

Baker Tilly has launched a new initiative to help companies steer their way through the credit crunch. The Debt Advisory team pulls together experts from across the firm, providing practical guidance about how to renegotiate existing bank facilities or gain access to fresh finance.

Until recently, such needs were part and parcel of everyday business. Now, however, the environment has changed radically.

"Banks are on the alert for the slightest evidence that a business may be beginning to struggle. A breach of even the most modest covenant can be a trigger for additional fees, increased margins and, in the extreme, the withdrawal of facilities," says Rob Donaldson, Head of M&A and Private Equity at Baker Tilly.

"Our service is designed to help companies avoid a nasty surprise and to make sure they are prepared ahead of time and can present a compelling case," says Alistair Hynd, Head of Project Finance and Financial Modelling at Baker Tilly.

"We know the banking markets well. We know which banks are still lending, which sectors they favour and how to approach them," Donaldson adds.

The Debt Advisory team provides guidance about the most efficient way to structure (or restructure) debt and identify alternative debt providers, including those outside the banking sector. It uses a three-stage approach to guide clients through the lending maze.

"Step one is to identify the potential problem. We analyse a company; its trading position, cash flow forecast and existing balance sheet. We'll look at the current debt structure, the terms in place, the covenants attached and the risks and consequences of a breach of any of the loan covenants," says Donaldson.

"We also work closely with our Restructuring & Recovery teams, who understand the perspective of the banks' credit teams and help us gauge the likely reaction to a deterioration in trading and cash flow," adds Hynd.

Step two is to identify and evaluate the options available. The team can assess whether a company is likely to continue to receive support from its existing lenders and if so, on what terms. If it seems likely that the terms or availability of funding will change significantly, the Debt Advisory team can identify and assess the likely alternatives i.e. how to secure finance from elsewhere and where that finance might come from.

This leads to step three: implementation of a solution. This will involve finding and approaching alternative finance providers and helping to negotiate the terms of alternative debt or possibly assistance in raising some equity to give the business breathing space.

*For more information, contact Rob Donaldson on 020 7002 8713 or Alistair Hynd on 020 7002 8732.*

## **MAKE YOUR BUSINESS FLEXIBLE**

- Take a radical look at the cost base
- Make early cuts in fixed costs
- Ensure you have breaks in new leases; use serviced accommodation
- Invest properly in your sales resource
- Use invoice discounting
- Cut all non-essential costs
- Encourage your suppliers and customers to share the burden
- Sell non-core parts of your business

## **HUNTING FOR CASH**

- Change banks, enlarge the banking group
- Use alternative debt providers, such as asset-based lenders
- Use alternative funders, such as niche mezzanine funders or new "private equity" debt providers
- Raise private equity funding to replace debt, providing working capital
- Consider an M&A deal, or find a partner

## RICH PICKINGS

In this battered economy, many companies are struggling simply to survive. But for stronger, cash-rich businesses with vision, now is the time to start the search for potential acquisition targets

**WORDS:** Brian Bollen

Every cloud has a silver lining. Every challenge creates an opportunity. Choose your proverb, and apply it to the current economic climate. The consensus at Baker Tilly and beyond is that conditions could be right for companies with the cash, courage and vision to begin snapping up what could be copper-bottomed bargains. A company experiencing short-term difficulties could turn out to be fundamentally sound.

Bruce Mackay, Restructuring & Recovery Partner at Baker Tilly, agrees with the broad thrust of the sentiment, as does the latest issue of *The McKinsey Quarterly*. It predicts a more rapid revival of M&A activity than seen in previous downturns. In the next year or so, transactions will close much faster to avoid complications from market swings – the average time from deal announcement to closing has already fallen from 130 days (1995-2007) to 60 days last year.

Companies will have to build immediate board-andshareholder support for a deal, and expectations for growth and profitability must be realistic. And the kinds of assets opportunistic buyers might successfully target look a lot different than they did a year ago. “Now is the right time to put aside conventional thinking about M&A and take a fresh look at your industry,” McKinsey adds.

However, Mackay warns: “Get proper advice and do thorough legal, financial and commercial due diligence. Certain sectors, for example retail and leisure, could experience significantly more difficulties before the upswing comes.”

Paul Johnson, a Corporate Finance Partner at Baker Tilly in Birmingham and a specialist in due diligence, suggests the fundamentals of what constitutes a good business haven’t changed – acquirers still need to be looking for businesses with a strong customer base, strong management, and ideally a market niche with relatively high barriers to entry. “A lot of Midlands businesses have gone through a lot of change, and are incredibly well run – but because their markets have collapsed, they can be bought very cheaply. Multiples have dropped back from the very high levels that we were seeing – in the teens for some very hi-tech companies. Today, in some sectors, anything more than four to five times EBITDA can look racy, but the fundamentals of a good business are what will drive the price.”

The key with assessing any business is to understand its current financial performance. A downturn that can’t be readily explained may be masking deeper problems. Also, particularly in a distressed sale situation, the time available for due diligence is likely to be short, so it must focus on the key risk areas.

### Change of mindset

The early 1990s recession demonstrated that smart investors can make significant profits by buying at or near the bottom of the market. The major difference now is the lack of available credit. “In the depths of the 1990s recession, it wasn’t easy for insolvency practitioners to find buyers as supply outstripped demand – but they were there, and many had solid access to funding,” says Mackay. “Today, the appetite for distressed assets is thin, and there is little credit available for acquisitions. Many of those with cash are holding on to it to bolster their balance sheet and ride out the economic storm.”

“A change of mindset is needed. At Baker Tilly, we operate across national regions and sectors. Our team of 28 Restructuring & Recovery Partners talk to each other a lot – we work closely with and share our market intelligence with our corporate finance colleagues. Between us, we know what’s happening out there and can add great value to potential purchasers.”

Mackay believes that, at least in the early stages of recovery, there will be more emphasis on economic and business fundamentals. “There has to be an understandable and viable business at the core for anyone seeking expansion or acquisition finance; business plans will have to be a lot more transparent and robust; and appetites for proper due diligence will return to former levels, thank goodness.”

Accelerated mergers and acquisitions (AMA) activity has become an established part of the commercial scene. Trying to sell a business through an AMA process will often be a last effort to achieve a sale to avoid insolvency. But it conveys that it is a corporate finance, rather than an insolvency solution, so hopefully upholding inherent asset values. From a buy-and-build perspective, purchasers may find good-value acquisitions through the AMA process.

### Looking up

“This should be seen as a positive development, making a ‘distressed’ sale more of an M&A process than an administration process,” says Jon Brooks, a Partner at Rutland Partners, traditionally a turnaround specialist but, in the more benign, pre-recession environment, a trouble-shooting enhancer of performance. AMA remains at heart, though, essentially unchanged, with the emphasis on price and rapidity of movement. The recession will bring more

administrations, Brooks believes, but banks will strive to avoid pushing companies over the brink to avoid lowering a company's value.

Brooks argues that the closer a company is to consumers, though, the more difficult it will be to avoid failure and redundancies. "We believe we've seen only the first wave so far. It will take years to restructure and reinvigorate UK businesses where the model was based on banking and valuation terms that are now unsustainable." But he forecasts that companies with investment firepower – almost by definition a very limited and shallow pool – can start buying at low multiples.

"Trade buyers who know their industry really well will spot potential purchases, but they might lack the funding and managerial skills to make them work. A number of mainstream private equity houses retain the capability to do deals, as a lot of funds are unspent, but private equity has become risk-averse." His conclusion, though, is that those with longer memories and greater stores of bravery could work together with management teams to take on more difficult transactions than in recent years. With the right combination of talent and techniques, a profitable business can be extracted from one that is overgeared and struggling. ■

## Clinging to the wreckage

AIM has not escaped a battering in the current financial crisis, with recent months seeing low levels of activity and a sharp rise in the number of companies de-listing. Here, Completion lays out the options for firms re-evaluating the potential of the market

**WORDS:** TONY McCAULEY

There can be no hiding the fact: these are the worst of times for London's Alternative Investment Market (AIM), the London Stock Exchange's equity market for smaller, growth companies, which has suffered considerably more than its big sister, the LSE Main Market, during the financial crisis.

For Adam Hart, Head of Corporate Finance at investment bank Fairfax I.S. and Chairman of the LSE's AIM advisory group, this is as bad as he's seen it in more than two decades of small-cap equity dealings. It feels as though the entire market is trying to round Cape Horn in a gale, he says. "A lot of people are just battening down the hatches and trying to ride out the storm." Hart, like many of his fellow AIM specialists, struggles to find any good news in the situation, except to say that companies that make it through will be the stronger for having survived, while patient, canny investors who've clung onto cash might find tasty spoils among the wreckage.

Notwithstanding this, Baker Tilly's 2009 annual Taking AIM Survey of more than 150 companies and institutional investors revealed that 74% of companies would still have listed even if they had known of the current economic turmoil. The principal reasons for this are (i) the access to capital. More than £3bn was raised on AIM in 2008 for existing listed companies which, although significantly down on the previous year, was still a substantial and important sign of the maturity of the market, which is a lifesaver as banks have restricted lending, and (ii) the increased profile an AIM listing provides with customers and suppliers can be important to differentiate companies from their competitors.

Nearly 70% of respondents to the survey predict that recovery is most likely to come in 2010. Largercap Main List companies are likely to recover first but then investors will seek to find value within the smaller caps.

In the meantime, the number of initial public offerings (IPOs) has dried up almost entirely: there were just two IPOs from August through to December, raising a total of £11 million. For the whole of 2008, there were just 38 IPOs raising £917 million, compared to 182 launches the previous year, which raised nearly £6.6 billion.

Nevertheless, there were more IPOs on AIM than on any other growth company market. In the secondary market, according to figures from the LSE, trading volume on AIM has also fallen. The overall value of shares traded last year fell to £49 billion from £75 billion. Trading became progressively thinner through the latter half of the year, so that average daily volume by December had shrunk to just £75 million compared to around £250 million in the first six months of 2008.

### Wherefore a listing?

The lack of liquidity is driving a lot of companies to rethink the role of the market in their corporate lives. "The lack of liquidity is making capital-raising very difficult," says Paul Elliot, Head of Plc Advisory at Baker Tilly Corporate Finance. "A number of small companies are wondering whether the benefits they can achieve from being on AIM are outweighed by the costs and other disadvantages." Many have already de-listed.

While the number of companies tapping the market, whether through IPOs or other routes, has shrunk, the number of companies leaving AIM has shot up. This rush to de-list has meant that AIM has suffered a net loss of 144 listings in the past year, the first net decline in company listings since the market's inception in 1995.

From the investors' perspective, too, the numbers are grim. The three AIM indices lost about two-thirds of their value last year. That was about twice the loss for the FTSE 100 share index, and investors continue to favour the larger, more liquid stocks in this market.

As a market for smaller growth companies, the lack of liquidity has always been an issue for AIM. But, as Chilton Taylor, Head of Capital Markets at Baker Tilly, and a member of the London Stock Exchange's AIM Advisory Group, notes: "Indices on AIM have always been largely irrelevant in view of the large diversity of companies in size, sectors and stage of maturity. AIM has always been a market for careful stock-pickers."

The number of AIM companies whose market cap has fallen below £5 million has doubled in six months, to around 600. Indeed, some 75% (more than 1,100 companies) now have a valuation of less than £25 million. "That's a situation we've never seen before," Taylor says. And as much of the investor base for AIM is comprised of institutional funds, who typically invest in companies with a minimum market capitalisation of £25 million and some only over £50 million, many companies are now too small to be of interest to such investors.

### Navigational choices

Taylor adds: "This places increased importance on UK government tax incentive schemes, such as Venture Capital Trusts (VCTs) and Enterprise Investment Scheme (EIS) funds, both of which are aimed at providing (risk) equity finance for such companies." However, the availability of VCT funds has significantly reduced in recent years.

Chilton Taylor points out that four years ago nearly £800 million of new funds were raised by VCTs but last year only £200 million was raised. Indeed, only £30 million has been raised to date in this tax year and around only £50 million is likely to be raised in total. As such funds must be invested within three years, it is clear that this important pool of funding has not been replenished. This is because over this period, individual investor income tax breaks have fallen by 10% and the size of companies that are now eligible for investment has been halved to those with gross assets of only £8 million. There have been further restrictions on the number of employees and total funds that a company may attract from such schemes – all such factors have reduced the attractiveness of VCTs to private investors.

Chilton and many other advisers are urging the Government to enhance the tax benefits in the forthcoming Budget so that more funds are available for equity finance.

### Share-pickers market

Paul Elliot says that for companies weighing their options, there are basically three routes: 1) they can take their companies private by buying it off the public market using private equity or other financial funding; 2) they can simply de-list the company; or 3) they can find a corporate buyer for the company.

The first of these options, while tempting in view of such low market valuations, can be difficult to execute. The costs and risk involved in successfully completing take privates mean that small-scale companies are typically not pursued, and in the current market, although there is substantial private equity still available for the right deal, debt funding is severely restricted. Of the second alternative, rather than make an offer for the plc, companies can simply de-list, requiring 75% shareholder approval. This can be accompanied by a share buy-back for example, to assist a cash exit for institutional and other shareholders who do not wish or are unable to hold shares in private companies.

While he expects the pace of these transactions to pick up, Taylor says: "While there will continue to be some take privates and take private lights, the major challenge will be to raise the required funding and for investors to accept valuations which do not reflect their perceived value of the underlying businesses. It is likely under current market conditions that AIM companies will take over other listed competitors largely through share issues rather than cash."

At some stage though the bottom will be reached, and at that point, AIM will show real value opportunities. Taylor says: "You have to be able to find sellers as well as buyers. Once we reach the turnaround stage, AIM will return to what it has always been: a share-pickers market," he says. "We will see a market with fewer but stronger companies – and that can only be a good thing." ■

## THE DECLINE OF AIM 2007-09

### Number of companies listed

December 2007: 1,694 (peak)

January 2008: 1,693

February 2008: 1,683

March 2008: 1,681

April 2008: 1,675

May 2008: 1,659

June 2008: 1,657

July 2008: 1,639

August 2008: 1,626

September 2008: 1,609

October 2008: 1,597

November 2008: 1,580

December 2008: 1,550

January 2009: 1,530

February 2009: 1,524

# SEARCHING FAR AND WIDE

When Christopher Westcott came to sell clean technology business, Wilson Taylor Asia Pacific, he was keen to make sure the company went to the right buyer. Fortunately, Baker Tilly was able to find the perfect match

**WORDS:** CHRISTIAN DOHERTY **IMAGE:** DAVID VINTINER

Ask the average man on the street what cathodic protection involves, or whether FPSO is the way of the future, then you'd more than likely be met with blank looks. But Christopher Westcott, along with his colleague Pang Kok Wa, have built a serious business on just these things.

Westcott and Pang started Wilson Taylor Asia Pacific (WTAP) in 1997, providing anti-corrosion products and services to the marine industry. The company initially based itself in Singapore, where it served the thriving shipping industry. Oil rigs, shipping and marine infrastructure all benefited from the anti-corrosion solutions that WTAP pioneered. These effectively increased the lifecycle of infrastructure and pipelines, leading to reduced spillages and leaks. In an age of increased scrutiny over the environmental impact of industry, providing assurance and protection against pollution was a good business to be in.

By 2007, the company had achieved pre-eminence in its field, and was a market leader in the Far East. "Wilson Taylor became a well established provider of corrosion control solutions – their reputation in the industry and the region was first class," says Ali Aneizi, Baker Tilly Partner in charge of finding a buyer for WTAP.

Westcott and Pang had succeeded in developing the business to a point where it had also expanded into China, with the Shanghai office opening in 2004. The company had diversified into the maintenance and protection of Floating Production, Storage and Offloading vessels (FPSO), now widely used in the offshore oil industry.

Westcott had assembled a local management team to run the company as he gradually took a back seat, chairing the firm from his London base. The team, still based in Singapore, ran the day-to-day operations and oversaw a period of attractive growth. Eventually, they ended up holding a significant stake in WTAP.

However, in 2007, Westcott decided the time was right to sell. "The reason to sell was partly that I'm well past retirement age and I wanted to be less involved," he says. But rather than simply find the highest bidder, Westcott wanted to secure the long-term future of the business. "We were very keen to find a strategic partner who we could work with, who could get us into new territories and who has complementary products to ours," he recalls. "We didn't just want to find the highest bidder and wash our hands of it. The company is like a family business and we've worked with the employees for a long time so we wanted the business to continue to grow in the right hands."

So Westcott held a beauty parade of advisers before mandating the Baker Tilly team, led by Aneizi. "We talked to a number of people who could advise on the sale. We liked Baker Tilly and in particular Ali. I was impressed with him and the effort he and his team made in understanding our niche business. It made a huge difference – they put a lot of work in and took great effort to find us the right deal."

For Aneizi, it was a great mandate to win. "WTAP was an attractive business, operating in a great sector and in a growth region. It was always going to attract great interest."

However, Baker Tilly's challenge was to find the right partner for WTAP. The shareholders didn't want a competitor from the immediate region. Westcott and the Singapore team saw the sale as a beginning rather than an end: the chance to develop and grow the business internationally.

## Global search

Aneizi took up the challenge. "We conducted a global search, and identified potential purchasers from four different sectors, pretty much across all five continents."

Once the potential buyers had been shortlisted, Baker Tilly began the process of soliciting interest. "The shareholders were sensitive about confidentiality and so we ran a discreet process. We approached a well-researched and limited number of buyers – those we thought had a solid and strategic reason to buy the business," Aneizi says. "We got offers from the US, the Middle East and Europe. Ultimately, we ended up with a Middle Eastern buyer."

That was APS, a UAE-based supplier of industrial coatings and linings run by a UK expat management team. Interestingly, they were going through a transaction of their own at the same time, a private equity fundraising that would also fund the acquisition of WTAP.

"This was a complicated deal with many moving parts," says Aneizi. "We had a Singaporean-based management team who wanted to stay with the business, a UK resident shareholder who wanted to retire, and a purchaser based in Dubai in the midst of their own PE transaction... all of which was taking place across three different time zones. It

wasn't easy." The challenge of managing these moving parts and representing the interests of all the shareholders underlined the complexity of the deal.

That has been achieved, according to Westcott. "The deal is such that APS acquired 80% and the remaining 20% remains with the former shareholders of our group," he says. "We were able to cash out substantially. But the management team and Pang are still very much involved in the running of the business."

Crucially, the deal will allow the enlarged group to expand beyond its current area of operations. "The deal will enable us to get our products into the Middle East, and the APS products into ours," says a clearly happy Westcott. "The synergy is very good and their products are complementary rather than competitive." ■

## How long will this be going on?

Economists are divided on what the recession will do to the economy. Is the UK heading for its worst year since the Second World War, or will businesses be through the worst of the downturn by the time 2010 comes around?

**WORDS:** ANDREW CAVE

Planning ahead is difficult enough for businesses in stable economic times, given ever-changing financial markets and the dynamic nature of competition, so how should they go about it in the current recession? What economic trends should they expect in the coming months and what are the prospects and opportunities for businesses looking to grow?

It's a subject of lively debate among economists and Dennis Turner, Chief Economist at HSBC plc, is in the more optimistic camp.

"How long and how deep will the recession be?" is the question that most people are asking at the moment," he surmises. "A slowdown or adjustment was long overdue. We needed a correction and an adjustment because we had pushed the economy in terms of growth and jobs on the back of spending and borrowing by consumers and government.

"It created a horribly unbalanced economy and we needed to slow down, but the fact that the slowdown took so long to happen means that the bump will be bigger than it should have been. So what should have been an adjustment becomes a nasty recession, irrespective of the credit crunch."

Indeed, Turner says the combination of the two will make the collateral damage worse than it would have been, and the recovery will also take longer than normal.

"If we were talking only about the economy, you would say we're not too far from the bottom," he adds. "You could expect gross domestic product to level out probably by the fourth quarter of this year, because all the conventional levers that can be pulled have been pulled more decisively than in any other recession I can remember."

### Cash squeeze

"So this should have been a very short-lived and not very deep recession. But it's not only about the economy and that's the problem. The more I talk to businesses across the country, the more it seems to me that it's not the price of money that matters at the moment. It's actually getting the cash. Good businesses that need credit on a day-to-day basis can't get the money they need, and that's going to slow down activity."

On the question of finance, Howard Archer, Chief UK and European Economist at analysis house IHS Global Insight, agrees: "Obviously, there is concern about funding availability for businesses and I do think this is going to be a problem, despite all the government's attempts to stop it from becoming so."

Archer, however is in the more bearish camp of economists. He believes the UK economy will contract by 3.3% in 2009, making this year's performance the worst since the immediate aftermath of the Second World War. He forecasts gross domestic product will be flat in 2010 and that the British economy will not grow again until 2011, when he thinks GDP will increase by 1.5%-1.75%.

"However, there's a very real risk that we will see further contraction next year," he warns. "In addition, because of the horrible state of the public finances, as soon as a recovery has been established, the Government will have to tighten fiscal policy, which will have some limited impact.

"The problem is that all the risks are to the downside of these forecasts at the moment. We're still at the stage where when we revise our forecast – it's more likely that we will reduce them, rather than anything else."

The National Institute of Economic and Social Research report in February 2009 forecast that the UK economy will experience its biggest decline for six decades this year, with consumer spending falling by 3.8% and business investment declining by 8.8%. Better news, it says, is that exports should increase by 2.4% next year, driving a "modest recovery" in GDP in 2010.

By contrast, Turner expects the worst of the recession to be over by the end of this year, with recovery towards an annual growth trend of about 2.5% a year starting in 2010. He warns: "The problem we have is actually less to do with how deep and how long the recession will be and more to do with what the post-recession economy is going to look like."

### Change of focus

Turner's view is that much of Britain's growth in the past decade has come from retailing, financial services and property, the three industries that will probably suffer most in the current downturn.

"If we're going to grow and those three industries are going to be on the back burner for a while, what industries have we got that are going to stimulate growth?" he asks. "Things like manufacturing, exporting and investment start to matter again."

In the small business economy, Turner believes firms that rely heavily on subcontracting from major multinational companies will find economic conditions most difficult because their customers will be making cutbacks and will also typically take longer to turn around than smaller, fleeter-footed businesses.

In contrast, he says, firms that rely on public-sector outsourcing or spending should be better placed than most because he expects public sector spending to continue to grow in 2009 and 2010. Companies that are geared towards exports will have a short-term advantage from sterling's current weakness and a long-term one because of the potential domestic demand from fastgrowing Asian economies such as China.

Firms in specialised markets such as medical and biotechnology firms should also have an advantage. Archer says: "There are always some areas of the economy that are more resilient than others and I am sure that's going to be the case again this time. There are always companies that fulfil special niches."

### Prospects for growth

In the long term, Turner sees attractive prospects for Britain's alternative energy technology companies. "It's easy to exaggerate the impact of the recession," he says, "but if 6% of the labour force is unemployed, 94% is not. And if consumer spending falls by 2% this year, there's still £750 billion-£800 billion going to be spent so there's a lot to play for. Businesses will have to get in shape, pay attention to competitiveness and productivity and stay close to customers because service and value matter as much as price.

"But, similarly, there will be prospects for growth. If the economy shrinks by 2%, you are taking 2% off £1.4 trillion. That still leaves a lot to go for and you can do it by being smarter than your nearest competitors.

"So much of business today is about being smart, not being cheap and it's about the concept of value rather than a bargain. If you can get the money, it is also a great time to borrow and to invest because if you're doing that you're not responding to the downswing but preparing for the next upswing and by the time the market picks up, you'll have everything in place."

However, Archer believes the risks of small businesses being unable to get enough credit are easily understated and that this remains a real danger. In such times, he says, firms fall back on the strength of their client and supply chain relationships. Where solid relationships exist, there may be flexibility on payment terms.

No matter how long the recession lasts, the way businesses behave in this downturn will shape their prospects when the recovery comes.

"The recession will end, because recessions always do," says Turner. "The economy will stop shrinking, stall for a little while and then it will start to grow.

"The businesses that will take advantage of that growth will be those that are getting in shape now and preparing for it. Companies need to be flexible. The economy that comes back after this recession will not be the same as the one that went into it." ■

## FANTASY FINANCE 2009: YOUR PREDICTIONS ON THE ECONOMY

Following a year of unprecedented uncertainty, when economists and investors got their forecasts wrong, Baker Tilly asked the City for economic predictions for 2009. Those surveyed were asked how optimistic they felt about a range of economic issues, including the strength of the pound, the housing market, the FTSE index, and the number of company insolvencies. Overall, respondents appear bullish about the prospects for the UK economy. Mean figures indicate that the Bank of England base rate will be 1.5, as opposed to 0.5 at the end of March 2009, and the UK three-month Libor % will be 2.4 – at the end of March 2009, it was 1.649.

## WHERE IS THE ECONOMY HEADING?

### BRITISH CHAMBERS OF COMMERCE

- 2.8% fall in GDP, before a 0.8% rise in 2010
- Sharp fall in manufacturing output (down 9% in 2009) and plunging capital investment (down 9.9% in 2009)
- "Distinct risk of deflation second half of 2009"

## **CBI**

- 1.7% fall in GDP, revised downwards from 0.3% growth in preceding report
- 10.5% fall in fixed investment
- 1.8% fall in household spending

## **EEF/OXFORD ECONOMICS**

- 1.8% fall in GDP in 2009
- 6.3% fall in engineering output; 5% fall in manufacturing output
- 7.7% unemployment rate, from 5.8% last year

## **OECD**

- 1.1% fall in GDP, followed by 0.9% rise in 2010
- 1.8% fall in exports of goods and services
- 3.4% fall in imports of goods and services

Sources: *British Chambers of Commerce, CBI, EEF, OECD*

## **In need of direction?**

Is your business taking an unplanned detour?

Have current conditions placed you in uncharted territory?

Do you feel lost and in need of direction? Baker Tilly can guide you through the downturn and help you find your way again

To talk to us about your business, contact Lindsey Thompson on 020 7002 8763 or at [lindsey.thompson@bakertilly.co.uk](mailto:lindsey.thompson@bakertilly.co.uk)

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