



2011 TRENDS

Blakes
CANADIAN LAWYERS

PRIVATE EQUITY

STEADY LBO ACTIVITY WITH A FOCUS ON THE MIDDLE MARKET:

Amidst a more robust M&A marketplace and improved access to deal financing, including the emerging Canadian high-yield debt market, private equity funds are expected to be in an acquisitive mode this year as the investment periods of 2006 and 2007 vintage funds begin to expire and GPs look to put their committed capital to work. While still considerably off from the peak in 2007, published reports indicate Canadian buyout volume and deal value last year increased seven per cent and 21 per cent, respectively, over 2009, and we expect mid-market LBOs to continue to dominate the Canadian market, having accounted for a reported 64 per cent of all buyout deal value in 2010. We also expect large-cap buyout funds to continue to look to mid-market LBOs, although some mega buyout deals will get done.

STRONGER IPO MARKET FOR PORTFOLIO COMPANY EXITS:

Renewed investor confidence in 2010 resulted in a strong Canadian IPO market with published reports indicating approximately C\$5.5-billion raised in corporate IPOs, representing a three-fold increase from the prior year. We see signs of continued improvement in the Canadian IPO market in 2011 which could facilitate IPO portfolio company exits.

STRATEGIC BUYERS TO REMAIN ACTIVE:

Strategic buyers have recently provided strong competition to private equity buyers for targets, reportedly accounting for 92 per cent of all Canadian M&A transaction volume last year, and we expect this activity to continue in 2011. Strategics with available cash reserves and investment grade ratings are actively looking to do deals in the current market and are demonstrating a willingness to aggressively bid against private equity funds in competitive auctions.

SPONSOR-TO-SPONSOR TRANSACTIONS TO CONTINUE:

With fierce competition for quality targets, we expect LBO funds to continue to acquire solid portfolio companies from other private equity firms, with sponsors appreciating the upside of a company that has undergone strategic and financial improvements through private equity ownership.

FAVOURABLE TAX CHANGES:

In the coming year, we expect private equity funds to continue to take advantage of amendments to the *Income Tax Act* implemented in 2010 which have significantly liberalized tax laws applicable to foreign buyers of Canadian businesses. Positive tax changes have resulted in non-resident investors no longer being subject to the invasive "section 116" tax, withholding and compliance burdens applicable to equity dispositions (except where the equity constitutes a real property interest), the elimination of the need for "blocker" entities in many cross-border acquisition structures and the removal of withholding tax on arm's-length and certain non-arm's-length cross-border interest payments.

CANADIAN PUBLIC PENSION PLANS TO CONTINUE GLOBAL DEALMAKING:

As was the case in 2010, Canada's public pension plans are expected to continue very active private equity strategies this year, particularly in respect of direct investments in Canada and abroad. Published reports indicate that the most active pension plan investors accounted for a majority of all Canadian private equity activity transaction volume last year. With a strong Canadian dollar and low interest rates, we expect Canada's pension plans to continue to capitalize on international investment opportunities, including in the infrastructure and energy sectors.

FOLLOW-ON ACQUISITIONS AND CONTINUED FOCUS ON OPTIMIZING PORTFOLIO COMPANY PERFORMANCE:

We expect that GPs will continue to devote substantial time to optimizing returns for existing investments, including pursuing attractive follow-on acquisition opportunities to ready portfolio companies for sale. We also expect sponsors to focus on increasing investment performance, including by undertaking dividend recapitalization transactions which were prevalent last year.

continued on reverse.

NEW TELECOM AND SATELLITE OPPORTUNITIES:

Industry Canada is expected to make a decision in mid-2011 regarding the direction to be taken in the liberalization of foreign investment restrictions on Canadian telecommunications companies, which could result in (i) an increase in the direct foreign ownership limit on all telecom companies to 49 per cent from the current effective limit of 47 per cent, (ii) removal of foreign ownership restrictions entirely for smaller telecom companies having less than a 10 per cent market share, (iii) removal of foreign investment restrictions entirely for all telecom companies, regardless of size, or (iv) the status quo. This potential change follows the recent lifting of foreign ownership restrictions on Canadian telecom satellites, opening the door to foreign acquisitions of Canadian satellite companies by LBO funds.

SHAREHOLDER ACTIVISM:

The need for potential private equity and other acquirers to negotiate simultaneously with both the board of a target and its key securityholders has been underscored recently by the increased willingness of institutional shareholders to voice their displeasure with incumbent directors and management in response to underperformance in the capital markets and a reliance on relatively liberal Canadian laws permitting shareholders to call special meetings and seek to replace directors. We expect challenges to board decisions by shareholders to continue in the coming year.

FOREIGN INVESTMENT UNDER SCRUTINY:

The Canadian government's decision to block BHP Billiton's proposed US\$39-billion acquisition of PotashCorp represented only the second time (and first in the resource sector) that a foreign acquisition has been rejected under the *Investment Canada Act*. As has been widely reported, the deal was blocked despite unparalleled proposed commitments from BHP to both Canada and Saskatchewan and the action has raised questions as to whether the Canadian government has become protectionist. The Canadian government has promised increased guidance for future foreign investments and a review of the *Investment Canada Act*. While we expect future reviews will proceed as they have in the past, foreign acquisitions involving "strategic resources," national security, state-owned enterprises or sovereign wealth funds, or which are particularly large and unsolicited, are likely to receive heightened scrutiny and could be the most challenging to complete.

STABLE FUNDRAISING AND "FLIGHT TO QUALITY" BY LPS:

With reports indicating over C\$1.4-billion of capital commitments raised in 2010, we expect to see a stable fundraising environment this year characterized by a continued "flight to quality" by LPs to top-performing and experienced sponsors as well as those funds with investment strategies that fill gaps in current LP portfolios. We expect that GPs will face continued pressure from LPs on key deal terms such as management fees and an increasing demand for more GP "skin in the game." In addition, the best practices outlined in the Institutional Limited Partners Association Private Equity Principles, including the most recently released capital call and distribution templates, will continue to be top negotiation points for LPs.