



CREDIT CRUNCH: TRICKLING DOWN TO THE MID-MARKET?

During the nine months since the US sub-prime mortgage crisis emerged, we have witnessed a marked slowdown in activity in the M&A and private equity markets. Much of this slowdown is attributed to deals in excess of \$1 billion ("mega-deals"), and while mid-market M&A activity has softened, this segment has largely been able to weather the storm. We continue to hold the view that transaction activity in the mid-market (deals in the \$10 – \$100 million range) in Canada will remain stable for the balance of 2008.

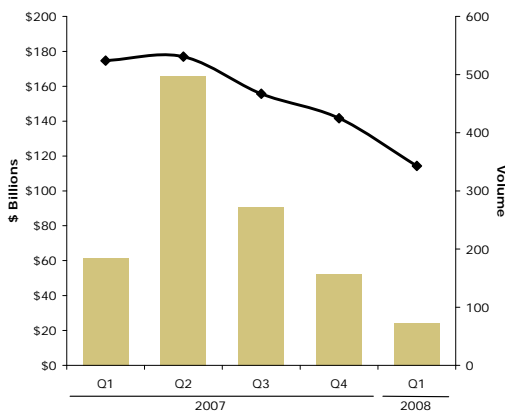
M&A MARKETS

Canadian M&A activity hit a record high in 2007, with a total of \$370 billion in deals announced, a 44% increase over 2006, according to Financial Post Crosbie. The first half of 2007 accounted for 1,049 deals valued at \$227 billion (including the \$52 billion BCE deal), followed by 892 deals valued at \$143 billion in the second half (including the \$40 billion Alcan deal), as credit market tightening began to take hold. Deal flow retreated substantially in the first quarter of 2008, with a total announced value of \$24.3 billion, a decline of 61% over the same period last year and 54% over the prior quarter. The volume of deals was also down in the quarter, at 343 deals, a decline of 35% over the same period last year and 19% over the prior quarter. Q1/08 represents a return to average quarterly values seen prior to the 2006 spike in M&A. Following the sharp drop from last year's unprecedented levels, overall M&A activity is expected to continue at a slow pace in the near term as the financial market recovery gradually progresses.

MID-MARKET PERSPECTIVE

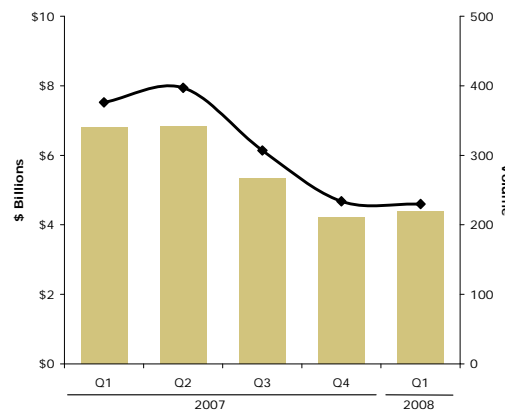
While tightened credit market conditions have hampered mega-deals, their impact on the mid-market has been less pronounced. Year to date (as of March 31), 230 mid-market deals valued at \$4.4 billion were announced, according to Financial Post Crosbie. This represents a decline of 36% in value and 39% in volume over the same period last year. Quarter over quarter, however, deal volume was nearly constant while deal value increased by 4%. While funding for large leveraged buyouts is much harder to come by today, Canadian lending for mid-market leveraged transactions has remained consistent over the past several quarters. Canadian mid-market transactions have typically been more traditionally financed than their larger counterparts, and therefore have not seen the same level of tightening from lenders.

Canadian M&A Activity



Source: Financial Post Crosbie

Canadian Mid-Market M&A Activity



Deal Size: \$1 million - \$100 million
Source: Financial Post Crosbie



PRIVATE EQUITY

Private equity fundraising in Canada totaled \$3.2 billion in 2007, returning to a more normal level after reaching a record \$10.2 billion in 2006, according to Thomson Financial. The value of private equity buyouts was a record US\$65.5 billion in 2007, compared to US\$8.2 billion in 2006. After peaking in the second quarter, with 55 deals valued at US\$8.6 billion (excluding BCE), buyouts declined steeply in Q3, with 36 deals valued at US\$2.8 billion. Despite an increase in deal volume (42 deals), the fourth quarter saw a further decline in deal value, to US\$2.3 billion. Fourth quarter activity was largely driven by mid-market deals, with only one mega-deal announced during the period. As mega-deals continue to be hindered by the scarcity and cost of leveraged buyout financing, financial sponsors have shifted their focus to mid-market transactions. This trend is expected to continue through the next several quarters, providing a stable rate of activity for private equity in Canada, albeit considerably below 2007 levels due to the absence of blockbuster buyouts.

VALUATIONS

The fallout of the credit crunch has reduced valuations on large deals over the past several months. Mid-market valuations, however, while not fully unscathed, have remained relatively stable. According to Standard & Poor's Leveraged Commentary and Data, Total Enterprise Value/EBITDA multiples for US deals in the \$25 - \$100 range averaged 6.0x in the latter half of 2007, compared to approximately 7.0x in the first half. While these are US multiples, we believe the trends are consistent with activity in Canada. Our view on valuations has not changed - they are determined by a combination of company fundamentals, industry dynamics, a strong transaction process, and to some extent by the state of debt and equity markets.