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Choose Wisely

C5 CEE Private Equity Forum
Event Summary by Squire, Sanders & Dempsey L.L.P.

Summer 2010

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INTRODUCTION

Central and Eastern Europe continues to be a challenging region for private equity. Whilst the region seems to be recovering from the impact of the global credit crisis, with debt finance once again becoming available and the market for deals improving, many industry players are finding that selectivity may be the key to their future success.

C5 and global law firm Squire, Sanders & Dempsey L.L.P. are pleased to bring you an overview of the perspectives and insights of leading industry experts from the C5 CEE Private Equity Forum held in Prague on 10-11 June 2010.

We would like to thank all presenters for their thoughtful comments on the current state of the market and the Forum delegates for their contributions to the discussions at the Forum.

Squire Sanders' CEE Private Equity Team

Summer 2010

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C5 CEE PRIVATE EQUITY FORUM: CUTTING DEALS IN THE POST-LEHMAN ERA

Private equity in Central and Eastern Europe is experiencing an increase in confidence but also an increase in conservatism. As **Garret Byrne** of **Deloitte** pointed out, “confidence is up, debt finance is stabilized, M&A activity is up . . . but it’s tough out there.” The region is recovering from the global financial crisis, and private equity players are demonstrating a cautious approach to business whilst anticipating slow but steady economic recovery in the region.

> *“Confidence is up, debt finance is stabilized, M&A activity is up . . . but it’s tough out there.”*
>
> *– Garret Byrne*

- It was widely acknowledged that the market for fundraising continued to be difficult. LPs were demonstrating nervousness towards the region and were being increasingly selective in relation to GPs and fund focus when making investments.
- The balance of power between LPs and GPs has clearly shifted in favour of LPs, who are requiring greater transparency and communication from GPs.
- The credit markets seem to be improving with senior debt available for “good” transactions on more acceptable terms than have been offered in recent times. Senior lenders are once again willing to fill the financing gap with mezzanine, whilst the CEE mezzanine lenders are frequently acting as the sole source of finance, particularly for working capital.
- Deal flow is increasing and is being driven by lower mid-market – rather than larger – deals. Succession-driven buy-outs could be a growth area within the market.
- Poland continues to be the star of the region, closely followed by the Czech Republic. There appears to be increasing interest in Turkey and the Balkans, but the Baltics remain out of favour.
- Traditional sectors have been generating considerable investment interest, with healthcare leading the way.

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WHAT THE EXPERTS SAID

Assessing the Current Environment

Garret Byrne shared certain statistics from the recent Deloitte Central Europe Private Equity Confidence Survey, observing that "65% of the people surveyed in April expected that market activity will increase and that is a big jump from two years ago where 60% expected it to decrease."

> *"It's really the smaller deal size segments that have been driving the market."*
>
> *– Brian Wardrop*

Brian Wardrop of **Arx Equity Partners** presented a review of transactions that had been completed in CEE from January 2009 to May 2010, which revealed that 71 deals were completed in this period. He explained that these figures demonstrated that "the Central European private equity market, through the crisis, was by no means dead and was still a relatively active market." Mr Wardrop noted that "it's really the smaller deal size segments that have been driving the market" with 24% of transactions completed at enterprise values above €50 million and 76% below.

Craig Butcher of **Mid Europa Partners** highlighted the lack of deal activity in the larger end of the market in the last couple of years saying that "as you couldn't get financing on an underwritten basis, all of the deals that were done in the last one to two years were really done on a bi-lateral basis, when a buyer and seller came together and worked to put together financing and get a deal structured."

Selectivity seems to be the key sentiment in the current deal environment. According to **Robert Manz** of **Enterprise Investors,** over the last 12 to 18 months "there have been a lot of deals out there available to be done but these have mostly been deals that we chose not to do." He explained that "the valuation gap has been immense" with sellers seeking premium prices and buyers "like Enterprise Investors saying, at the start of the crisis, *cut that in half and maybe we can talk.*" Mr Manz observed "that does not lead to a lot of completed transactions."

> *"The valuation gap has been immense" with sellers seeking premium prices and buyers saying, at the start of the crisis,* "cut that in half and maybe we can talk."
>
> *– Robert Manz*

It was, however, generally acknowledged that the market for executing deals, particularly larger deals, had changed following the credit crisis. Prior to the crisis, many deals were effected through auction processes, with strategic and financial investors fiercely competing for the prize. Financial investors more often than not were the victors, having used leverage to out-bid the competition. As **Thomas von Werner** of **EQT Partners** observed, following the crisis "strategics have come back much stronger" as they do not have the same financial constraints because they are able to use their corporate balance sheets.

Béla Seres of **Deloitte** reported that Deloitte's research had also noted "an increased proportion of non-core disposals, spin-offs and divestments of smaller businesses which are not performing or are sub-scale or strategically unimportant." He observed that these "can provide excellent acquisition opportunities for private equity players acting as industry consolidators and to establish their presence in another market or another sector."

A number of LPs at the Forum explained how some of their funds had taken advantage of the downturn. **Leon Hadass** of **Pantheon Ventures** pointed out how a number of deals done in 2007 and 2008 were overleveraged and "some of our GPs have taken advantage of this and have been able to

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acquire interesting deals at fairly attractive prices." **Isabelle Boujnah** of **Quilvest Private Equity** agreed, saying that "secondaries offer good opportunities to get into a market that has suffered quite a bit and to get visibility in the portfolio at the right price."

When considering returns on investments, **Richard Seewald** of **Alpha Associates** said that "over the last five to 10 years, Central and Eastern Europe and Russia have outperformed Western Europe and the United States." He noted that the historical returns were largely driven by mid-market and lower mid-market deals and speculated that was probably where the biggest opportunities exist today.

"Secondaries offer good opportunities to get into a market that has suffered quite a bit and to get visibility in the portfolio at the right price."

– Isabelle Boujnah

Fundraising

It was generally acknowledged by speakers at the Forum that the fundraising environment continued to be difficult for investments in CEE. **Paul Arent** of **Acanthus Advisers** highlighted that "in terms of funds over €100 million, we estimate that there's roughly €138 billion of dry powder out there." He went on to point out that "distributions are still very low which adds to the liquidity issues of investors."

"In terms of funds over €100 million, we estimate that there's roughly €138 billion of dry powder out there."

– Paul Arent

Helen Kenyon of **Preqin** presented the results of their recent survey of 50 LPs, 60-70% of which were based in Europe but which also included LPs from North America and the rest of the world. A third of respondents indicated that they were positive about the opportunities presented by private equity in Central and Eastern Europe at present with 27% claiming to be negative. This was down from the results of the Preqin survey in October 2009 where more than half said they were positive and just 9% were negative, demonstrating a big shift in LPs' attitudes to the region.

In terms of return expectations, Ms Kenyon reported that 31% of respondents said their expectations had increased and 31% said they had decreased. A third of LPs said they would not invest in another fund focussing on the region within the next year, demonstrating a greater aversion to risk, a retraction from non-core investments and a focus on core investments. Ms Kenyon explained that "a lot of investors just aren't sure how the financial crisis has impacted the region and which areas of Central and Eastern Europe, in particular, present the best opportunities, so there is a need for education of LPs."

Despite these negative figures, **Daniel Lynch** of **3TS Capital Partners** claimed, in relation to fundraising in 2010, that "people are back in business" but that it's "back to basics of strategy, team and track record." **Matjaz Cerjak** of **Chayton Capital** agreed and stated that, "if you haven't been in the market fundraising for two or three years, you need to know that the market has changed substantially and you need to adjust."

"If you haven't been in the market fundraising for two or three years, you need to know that the market has changed substantially and you need to adjust."

– Matjaz Cerjak

The consensus from the GPs and LPs that presented at the Forum is that LPs are conducting greater due diligence on the funds they are considering investing in. They are evaluating the track records of GPs preferring those who can demonstrate consistent returns over a number of funds. They are focussing on the management teams – whether they

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are well balanced with a cross section of skills, have been together for a long time and work well together. They are evaluating the ability of the management teams to demonstrate real added value to portfolio companies to enhance the ownership interest. They are also seeking a clear investment strategy which, as **Daniel Lynch** highlights, must "match the amount of money you are raising in the target market you are going after." **Matjaz Cerjak** advised GPs to "focus on your core advantages" and warned against pursuing ideas outside the usual focus of the firm. **Paul Arent** warned of the need for GPs to "demonstrate their differentiation."

With regard to the time it takes to launch a fund, **Matjaz Cerjak** commented that "in 2006/2007 you were counting on six to nine months to close a fund; you can safely assume that it's double that at the moment." This is due to a number of reasons including an increased focus by LPs on the way a fund is structured, due diligence, governance issues and fees, plus, as Mr Cerjak pointed out, "ticket sizes are a bit lower than they used to be" resulting in the need to engage more LPs to achieve a close.

However it was widely acknowledged that it is currently a more LP-friendly market, as **Levent Bosut** of **PDF Corporate Finance** explained, "GPs are having to be more transparent and LPs can demand more from their GPs." **Isabelle Boujnah** agreed explaining that "there is now much better interaction between LPs and GPs" continuing that "we don't know how long it will last but it is clearly a strong improvement for us!"

"GPs are having to be more transparent and LPs can demand more from their GPs."

– Levent Bosut

These opinions were backed up by data from Preqin as **Helen Kenyon** explained that 81% of respondents to Preqin's survey said that "they felt there had been a shift towards the LP in terms of the balance of power during negotiations" and it was clear that "LP expectations have become higher." Only 9% of respondents thought that this was a short-term anomaly, with a third thinking it was a medium-term change and over half thinking it was a long-term trend.

Daniel Lynch highlighted that, amongst other things, LPs are seeking "a demonstrable track record going back many years because they want to know how GPs manage through the cycles, deal with difficult times and still achieve successful exits." He said "the proof in the pudding is whether you can achieve respectable returns during difficult times."

Agreeing with this position, **Leon Hadass** said that Pantheon were interested in "identifying groups that would be able to demonstrate that they can operate in the markets in a sustainable way." Backing up the message that GP management teams were key for LPs, **Isabelle Boujnah** said that Quilvest "tends to look for teams with a good mix between westernised education and experience and local presence." **Thomas von Werner** acknowledged this preference saying "without local people and a very strong knowledge-base covering all the areas, I believe mid and long-term you will not survive."

Martin Paev of **SORTIS Invest** highlighted GP track records as a problem in raising funds for investment in South East Europe explaining that "for LPs, excluding the IFIs like EBRD and EIF, few will invest in regional focussed PE funds because there aren't enough track records to prove their returns . . . so when a GP goes to them and says 'I have only had two funds,' the response they are going to get is 'well stay in touch' which basically means come back in five years."

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Anne Fossemalle of the **EBRD** delivered encouraging news explaining that, like the EIF, the EBRD is not a commercial organisation and is "happy to invest in first time funds and to continue to support follow-on funds" as part of their strategic objective of promoting structural depth in private equity in the region and to encourage commercial LPs to invest also. Ms Fossemalle went on to say that in 2009/2010 more than 30 teams were invited to make pitches to the EBRD, of which about half continued to the next stage, commenting that "in a difficult fundraising environment, it's good to see that there are still some teams out there with spirit!"

The EBRD is "happy to invest in first time funds and to continue to support follow-on funds."

– Anne Fossemalle

Debt Finance, LBOs and the Appeal of Mezzanine

David Vials of **UniCredit Corporate & Investment Banking** delivered a relatively upbeat assessment of the credit markets observing that "we seem to have weathered the worst of what was a pretty dramatic storm." However, he added the caveat that "we're still not through the rough water and there are choppy times ahead" pointing, in particular, to the sovereign indebtedness crisis in countries such as Greece and Hungary.

Mr Vials commented that 2009 was the worst year in the past decade for European leverage loan volume, with volume and value falling by a third and two-thirds respectively for private equity-backed transactions. However, he went on to state that "activity is increasing in 2010" with European LBO loan issuances reaching their highest level in the first quarter of this year since the third quarter of 2008, up 87% to just shy of €8 billion in Q1, in comparison to a little more than €4 billion in Q4 last year, according to Dealogic.

Mr Vials described recent changes in deal terms, including that leverage multiples have decreased from their peak of a little over 6x in 2007 to under 4x in 2009, with a positive trend in the first quarter of 2010 to about 4.2x. Equity contributions are beginning to ease downwards from over 50% to more in the range of 40-50%, particularly if cushioned by mezzanine in the capital structure. Tenors are increasing to six and seven years, and there is a reducing trend on pricing from a 2009 blended average of circa 500 basis points to more in the range of 425-475. Whilst in 2009 most deals were being done on a club basis, there is now a return to underwritten transactions with flex protection, simple structures and a more cautious approach.

Banks have gone "back to basics" and have a heightened interest in strong management and, in relation to the sponsor and the GP, expertise in the relevant sector, experienced investment executives and strong relationships with banks. They are showing a continued focus on due diligence, forecast trends and down-side analysis.

"Our senior banking friends benefit from the cushion provided by mezzanine and, if the intercreditor agreement is drafted well we should never have any arguments with the banks."

– Franz Hoerhager

Mr Vials also predicted "a trend of increasing use of mezzanine in transactions, where cost effective." **Franz Hoerhager** of **Mezzanine Management GmbH** echoed this opinion explaining that "our senior banking friends benefit from the cushion provided by mezzanine and, if the intercreditor agreement is drafted well we should never have any arguments with the banks." He went on to say that "deals are starting to happen again after a draught" which he explained was in part due to the fact that acquisition prices had been too high. He added "the whole

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private equity industry in CEE has a lot of money waiting to be deployed and a lot of targets have been snapped up with equity alone."

Sean Glodek of **Darby Private Equity** concurred and referred to the change in Darby's portfolio "post-crisis" from having a significant LBO component to transactions where "often we are the sole senior lender and in which we refinance short-term debt and offer working capital." Mr Glodek went on to explain how mezzanine deal flow in 2009-2010 has fallen into four principal categories: growth capital, refinancing of short-term debt, junior debt in traditional LBO financing and secondary market liquidity, with the former two being the most active areas. He highlighted that mezzanine can play a number of different roles in restructurings, driven by the options available, and these range from being an "innocent bystander" or "Mother Theresa" to a "party pooper" or "grim reaper," with each role having slightly different pricing characteristics and expectations as to the function and engagement of the mezzanine lender.

The mezzanine panel agreed that there was a place for mezzanine in the capital structure because, as a passive financial instrument with cash interest not much higher than a senior loan, it was still much cheaper than equity. The mezzanine lenders highlighted that they would always take equity upside in the form or warrants or equivalent, and as **Claire Scott-Priestley** of **Squire, Sanders & Dempsey** explained, "the equity kicker aligns the interests of the mezzanine lender with investors and in this way a mezzanine lender is encouraged to work with a borrower through any bumpy patches. Therefore, mezzanine lenders are more likely to permit relief for covenant breaches, in the form of equity cures, within certain restricted parameters."

"The equity kicker aligns the interests of the mezzanine lender with investors and in this way a mezzanine lender is encouraged to work with a borrower through any bumpy patches."

– Claire Scott-Priestley

Market Trends

Several presenters gave their opinion on the countries and sectors that seemed to be generating the most interest.

David Vials highlighted that for lenders, "focus and selectivity are key," with "stronger economies, such as the Czech Republic, Poland and Slovenia, seeing more appetite for lending." He went on to state that sector is important, with the favourites being "non-cyclical, high margin businesses with strong cash flow cover."

Franz Hoerhager explained that manufacturing, telecoms and healthcare were traditional industries attractive for investments in CEE. Healthcare was a definite buzz-word with almost all speakers expressing an interest in this sector. However, Mr Hoerhager was more cautionary saying "it sounds great because we have an aging population and everyone wants healthcare, but one has to keep in mind that healthcare in most countries in CEE is funded by state budgets which are not a great source of money at the moment so this is a key risk factor one has to keep in mind." **Richard Seewald** supported this position and said that healthcare needed to be assessed on a country-by-country basis across the region.

"One has to keep in mind that healthcare in most countries in CEE is funded by state budgets which are not a great source of money at the moment so this is a key risk factor one has to keep in mind."

– Franz Hoerhager

Speakers at the Forum indicated a number of other sectors as being attractive for private equity investment, including telecoms, manufacturing, FMCG, retail and wholesale, energy, construction and infrastructure. **Jean-Philippe Burcklen** of the **EIF** reinforced the strength of interest in the sectors highlighted by other speakers but pointed out that the EIF were not “big fans of the financial sectors or real estate.”

Brian Wardrop’s figures showed that 14% of deals completed in CEE between January 2009 and May 2010 were in the healthcare services sector. With regard to geography, Poland dominated with 41% of all deals completed, but he claimed that “the Czech Republic has been host to the highest number of deals per capita ratio during the crisis” and only two of 71 deals were completed in Hungary.

It was universally acknowledged by the speakers that CEE and South East Europe should not be viewed as one region as they are not homogenous. It was also indicated that those private equity participants who had on the ground presence and local offices in the region were most likely to understand the local sensitivities.

Paul Arent delivered the results of an Acanthus survey which showed that 86% of respondents saw Central Europe as the most attractive sub-region over the next three years followed by 12% indicating Russia/CIS and 2% for South East Europe.

Martin Paev indicated that investors wanting to invest in South East Europe needed to identify whether they were interested in the whole region or only part “because investing in different economies in South East Europe has different motivations. For example if you are seeking a big market you should look to Turkey or Romania but if you are looking for a low risk market then you should focus on Bulgaria and Romania because they are part of the EU.”

“If you are seeking a big market you should look to Turkey or Romania but if you are looking for a low risk market then you should focus on Bulgaria and Romania.”

– Martin Paev

From an economic perspective, **Vladimír Dlouhý,** a former Minister of Industry in the Czech Republic, highlighted Armenia, Bulgaria and Estonia as being problematic CEE countries with the Czech Republic, Poland, Slovakia and Slovenia coming out best. However he predicted that “the growth path for the next decade will be lower, on average, for every country than was the reality before.”

Turkey was stated by many as being a new focus for investment activity. **Sean Glodek** pointed out that Turkey “is about a third of Darby’s current fund,” and **Isabelle Boujnah** said “I would think that Turkey is probably the next interest for us.”

Levent Bosut tried to explain the attraction of Turkey in the current market highlighting that “the crisis kicked in in Turkey much later than elsewhere in the region and Turkey emerged from the crisis earlier than its peers.” He pointed out that Turkey had an average 7% economic growth rate in the years 2003 to 2008 driven by deregulation, privatisation and fiscal policies. Underpinned by a strong banking system, favourable demographics and fiscal position, growth from 2010 onwards was expected to be 4.5% to 5% which is “the highest expectation in the entire region.”

Mirna Marovich of the **Croatian Venture Capital and Private Equity Association** explained that the "credit crisis has really affected South Eastern Europe." This was backed up by **Martin Paev** who pointed out the risk that "many investors are worried about how the economic situation in Greece is going to affect the region because of its proximity and the fact that it is considered as one of the leading countries."

Prospects for 2010 and Beyond

Paul Arent explained that Acanthus' research amongst LPs demonstrated positive mid-term expectations for the region, with 60% of respondents to their survey indicating that they expect their allocation to the region to increase over the next five years and 56% expecting an increase in the number of GPs.

Richard Seewald delivered some general predictions for the near future, saying "an imbalance of supply and demand of capital and attaractive in-going valuations in certain CEE countries should drive attractive returns at the lower mid-market for investments made in the current cycle, challenges at the higher end of the market with respect to quality of deal flow and debt financing and Central and Eastern Europe outperforming Western Europe on the back of continued convergence and growth."

David Vials was "cautiously optimistic" about the Central European debt market. This position was supported by **Daniel Lynch** who observed that "cheap debt as the main driver for mega-buy-outs is over, though the banks are back in the market and there is debt available for good companies that are stable and have predictable cash flows."

> *"Cheap debt as the main driver for mega-buy-outs is over, though the banks are back in the market and there is debt available for good companies that are stable and have predictable cash flows."*
>
> *– Daniel Lynch*

Brian Wardrop presented the case for succession driven buy-outs explaining that there was prospective growth in this area due to the fact that "a number of companies were established in the region in the early 90s by groups of entrepreneurs that were around 30 years old at the time. Those companies have grown and many of them have now reached the threshold, in terms of sales and size, where they are interesting buy-out targets for private equity and many of the owners of these businesses are now reaching retirement age and facing succession issues."

Mr Wardrop explained the drivers for growth in this market as being the availability of acquisition debt (subject to the usual restrictions) and the fact that one or two of the existing owners are often keen to reinvest – this being "a highly unusual characteristic of Central Europe," that classic family-owned businesses take the form of entrepreneurial partnerships created by three, four or five individuals with different needs. These more complex situations are "relatively difficult to auction and ideally suited to private equity investors who are looking for exclusive or proprietary situations." In addition, these owners have often over-extended in non-core ventures and are forced to sell, and these businesses present excellent buy-and-build opportunities for industry consolidation.

Béla Seres confirmed the belief that opportunities are available for succession driven investment saying "crises may come and crises may go, markets may be up or down but succession of entrepreneurs will always be an issue."

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The difficulties of executing cross-border deals in the region were discussed, with **Justin Fancher** of **Benson Oak** emphasising the cultural aspects, stating that "it simply might be that somebody from country A doesn't see eye-to-eye with someone from country B." **Ronny Grosman** of **Blackwood Capital Group** highlighted economic difficulties as being a factor, explaining that "when you're not doing so well internally in your own country the tendency is to fix what's closest to you first before you venture into a country you may never have invested in before." However, **Daniel Lynch** suggested that certain sectors were better placed for scaling businesses, such as technology, which "lends itself well to not only doing cross-border acquisitions but actually going worldwide." However, he warned of the risks associated with "management's ability to actually take on regional expansion which requires a different skill set."

> *"When you're not doing so well internally in your own country the tendency is to fix what's closest to you first before you venture into a country you may never have invested in before."*
>
> *– Ronny Grosman*

Robert Manz referred to a general sense of relief in the post-Lehman era as "the markets were getting overheated, valuations were getting higher and higher, debt levels were rising and we had a lot of interest in Central Europe coming from non-Central European players." He continued that he was happy "from the point of view of GPs focussing on this region, for Central Europe not to be the flavour of the day any more because it means less competition from non-regional players." Mr Manz emphasised that "the core teams who are focussed on the region and have people on the ground doing business here for a long time are best placed to make investment decisions in CEE."

Martin Paev believes that deal flow in South East Europe will increase by the end of 2010 and into 2011 and that there will be investment opportunities for distressed and special situations due to a lack of available funding. Therefore, investors may be able to obtain significant stakes in companies seeking working capital for relatively smaller capital contributions.

Laszlo Olah of the **Hungarian Venture Capital and Private Equity Association** summarised the opinions of many of the speakers by saying that "the crisis has changed a lot in the industry for the better."

> *"The crisis has changed a lot in the industry for the better."*
>
> *– Laszlo Olah*

WHAT THE NUMBERS SAY

Below is a sample of slides that were shared by some of the speakers in their presentations. Thank you to **Anne Fossemalle** of the **EBRD, Brian Wardrop** of **Arx Equity Partners, Daniel Lynch** of **3TS Capital Partners, Paul Arent** of **Acanthus Advisers, Franz Hoerhager** of **Mezzanine Management GmbH** and **Sean Glodek** of **Darby Private Equity** for permitting us to include these in our event summary.

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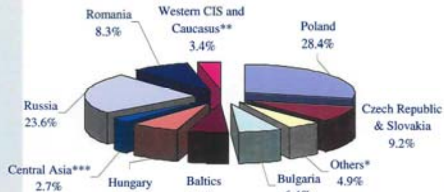
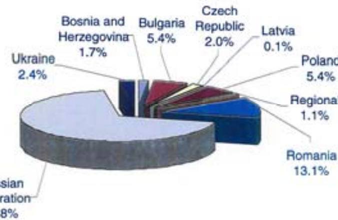
Investments by Country

By investment cost, since inception to end 2008



By investment cost, 2009 investments, including 42 investments of which 26 were follow on investments



*Others include: Albania, Bosnia, Croatia, Macedonia, Kosovo, Serbia and Slovenia
** Western CIS and Caucasus include: Azerbaijan, Georgia, Moldova and Ukraine
***Central Asia include: Kazakhstan, Kyrgyz Republic and Turkmenistan
Note: Excludes investments made to non-EBRD countries of operation

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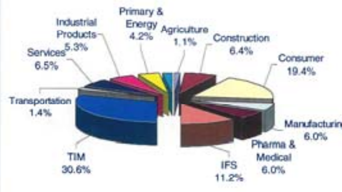
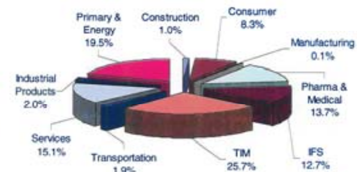
Investments by Sector

Since inception to end 2008



Investments in 2009, including 42 investments of which 26 were follow on investments



Note: in EUR, CSE and CIS
Note: Excludes exit proceeds on fund investments into non-EBRD countries.

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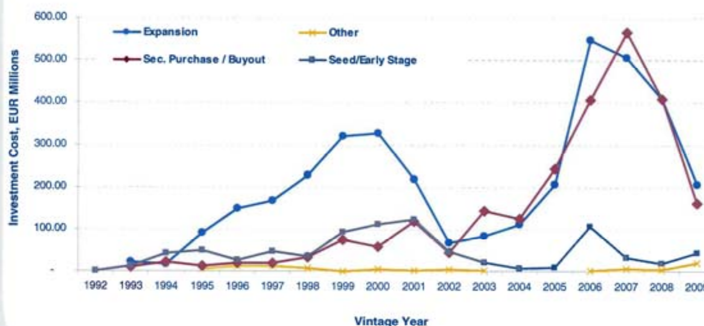
Investments by Stage Over Time



Note: CSE and CIS, data as of December 2009

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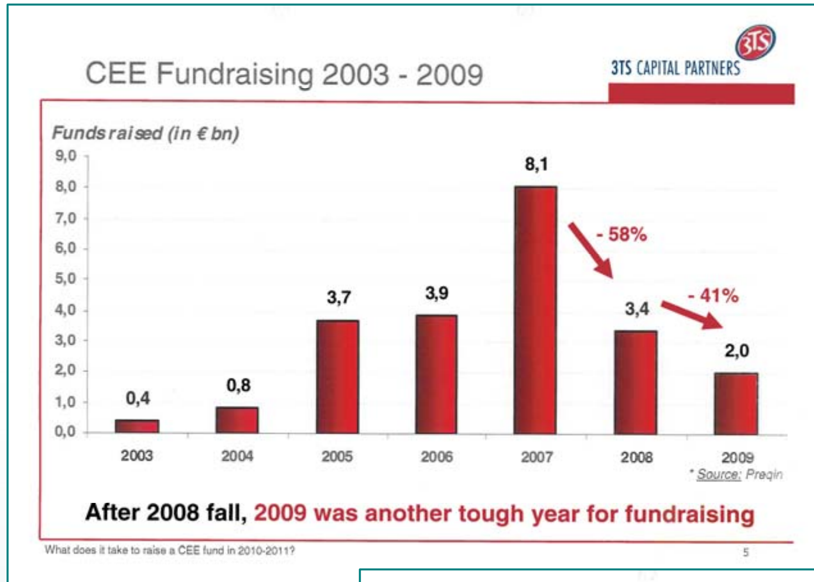

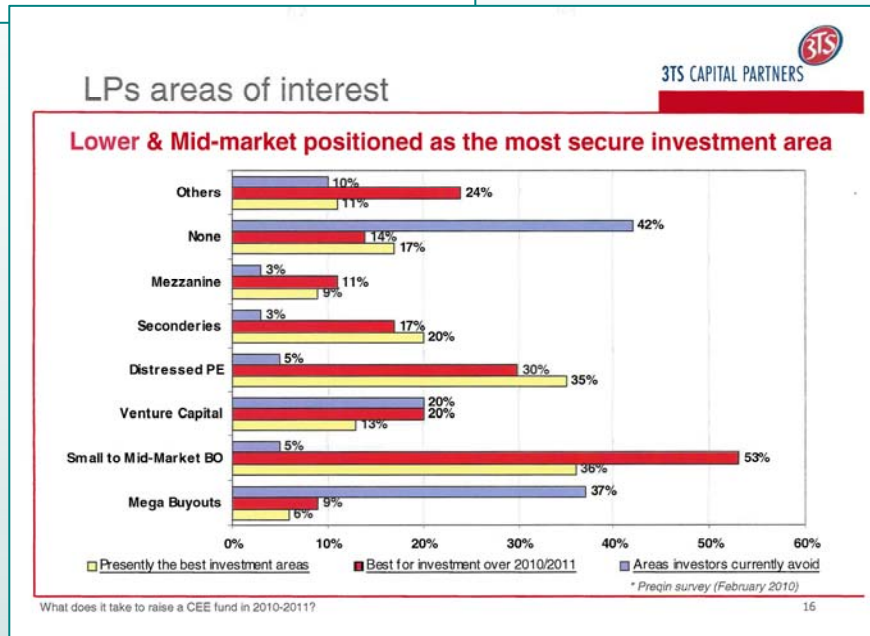

New metrics

3TS CAPITAL PARTNERS

- Expect more detailed DD, particularly on Team
- Expect longer time to finally close the fund
- Have realistic fund size matching strategy
- Demonstrate real value-added and ability to harvest value in successful Exits (for re-ups too)
- Expect lower commitments than originally targeted

What does it take to raise a CEE fund in 2010-2011? 21

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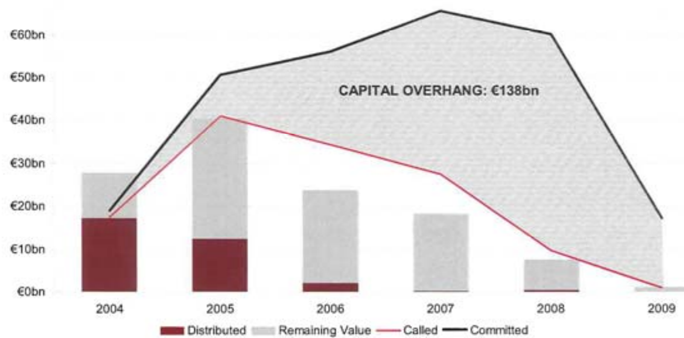
Dry powder, distributions and valuations

Distributed, Remaining Value and Called-up Ratios by Vintage Year



Source: Acanthus Preqin, January 2010. Includes all European buyout funds above €100m

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Acanthus

2009 – May 2010 CEE PE deals

52% of transactions in EnV € 10 – 50 M range; 76% < € 50 M EnV

Target Company	Country	Acquirer	Deal size
Air Maintenance Estonia	EST	BaltCap	in the range
Banco Populare Cesko	CZ	AnaCap	in the range
CMU	RO	Advent	in the range
BTV plast	CZ	Benson Oak	in the range
Devin	BG	Advent	in the range
Diamedix	RO	GED	in the range
Eesti Vijasalv	EST	Eestiland	In the range
ETOS	PL	Syntaxis	in the range
Euroclinicum	CZ	PPF	in the range
Expander	PL	Innova	In the range
Expert Petrolium	RO	Lime Rock Partners	in the range
Fabryka Lin i Drutu Drumet	PL	Penta	in the range
FIRO Tour	CZ	Odien	in the range
Frost	SK	Bancroft	in the range
Good Food	PL	Avallon	in the range
Hyperion	PL	Mid Europa	in the range
Infopress	RO	GED	In the range
INFO-TV-FM	PL	NFI	in the range
Interaktivni Tehnologii	BG	Mid Europa	in the range
Kakadu	PL	ARX	in the range
KCI Krowodrza	PL	Jupiter	in the range
Konsalnet	PL	SGAM	in the range
Kordama	CZ	Jet Investment	in the range
Lexum	CZ	ARX	in the range
Mediatel	PL	NFI	in the range
Noriel Group	RO	BAF	in the range
Noves okna	SK	Penta	in the range
Ozone	RO	Advent	in the range
Polske Biuro Podrozy	PL	EI	in the range
Polmed	PL	Krokus	in the range
PR Market	CZ	Penta	in the range
Rio TV	CZ	Argus	in the range
Rurgaz	PL	Tar Heel	in the range
Solar 21	CZ	Mid Europa	In the range
Svet Zdravia	SK	Penta	in the range
TEB	RO	GED	in the range
Way Industries	SK	Slavia Capital	In the range

Target Company	Country	Acquirer	Deal size
AmRest	PL	Warburg Pincus	larger
Anheuser Busch	CEE	CVC	larger
AVG	CZ	TA Associates	larger
Cabletel	BG	EQT	larger
CE Wood	CZ	RP Investors	larger
CIG Panonia	HU	MFB Invest	larger
HTL Strefa	PL	EQT	larger
Invitel	HU	Mid Europa	larger
Libet/Tamrac Polska	PL	Innova	larger
Masterlease	PL	Abris	larger
Medlife	RO	SocGen	larger
Profi	RO	EI	larger
Studio Moderna	SLO	Templeton	larger
Transpetrol	SK	CAPPA Fund	larger
UPC Telemach	SLO	Mid Europa	larger
WestLB Polska	PL	Abris	larger
Wydawnictwa Szkolne	PL	Advent	larger
III DC	BG	NEVEQ	smaller
Activ	CZ	Royalton	smaller
Ad-Vice	PL	Xevin	smaller
Bio-Profil	PL	EI Venture Fund	smaller
BKS	CZ	3i	smaller
DD Labs	PL	Penta	smaller
Dystrybucja Polska	PL	EI Venture Fund	smaller
Grapo Technologies	BIH	Benson Oak	smaller
Intermedica	PL	ARX	smaller
MIFAM	PL	AKJ	smaller
PBMK	PL	EI Venture Fund	smaller
PLOH	PL	Oresa Ventures	smaller
Pro Life	RO	Bedminster, SEEF	smaller
R&C Union	PL	EI Venture Fund	smaller
Smartree	RO	Venture Fund	smaller
Vltava Stores	CZ	Milestone Partners	smaller
Web Inn	PL	EI Venture Fund	smaller

4 | ARX Equity Partners

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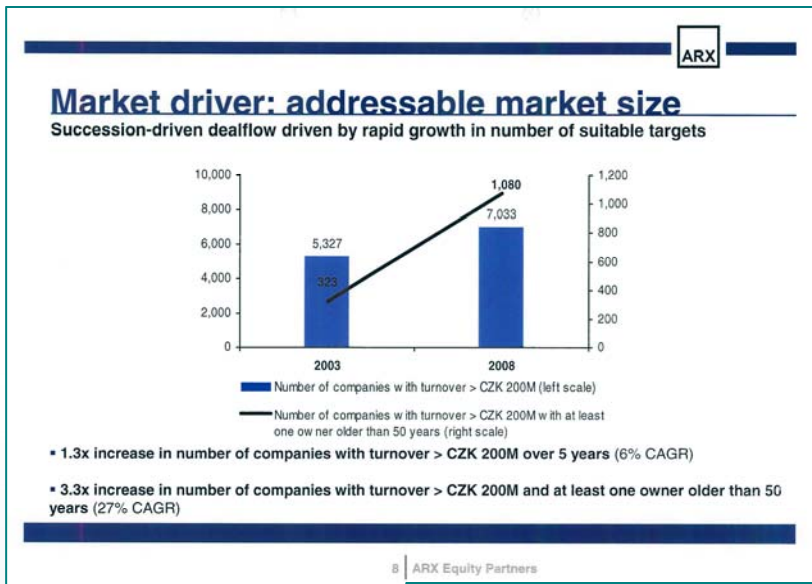

The Leveraged Finance

A product comparison

Lower credit risk ←→ Higher credit risk

	Senior Debt	Mezzanine	Equity
Ranking	Senior	Contractually subordinated	Junior
Security	Yes — 1st ranking	Yes — 2nd ranking	None
Covenants	Comprehensive Restrictive	Track Senior but looser	None
Term	5 - 9 years	6 - 10 years	Open ended
Cash interest	Cost of fund + 200 – 325 bps	150 – 300 bps above senior	None
Repayment	Amortizing from cash flow	Bullet at exit or maturity	None
Warrants	None	Almost always	Not applicable

| MEZZANINE MANAGEMENT CENTRAL EUROPE | PAGE 4 |

Darby Mezzanine Investment Indicative Terms

DARBY PRIVATE EQUITY

Mezzanine Loan Amount	€7 million to €25 million with an additional underwriting / bridge financing capacity of up to €25 million
Use of Funds	Leveraged buyouts, capital expansion, recaps and financial restructuring
Type of Obligation	Subordinated loan obligation typically with Cash Interest, PIK-Interest and Equity Kicker component
Cash Interest	Typically payable semi-annually in arrears; floating rate above 3 or 6-month EURIBOR
PIK Interest	Capitalized interest added to loan principal or paid in cash at the option of the borrower
Equity Kicker	Depending on jurisdiction; typically in the form of penny warrants for common shares, conversion rights of redeemable preferred shares, or profit participation rights
Maturity and Amortization	Up to 10 years final maturity; flexible amortization schedules including grace periods
Ranking	Contractually or structurally subordinated to senior debt, but senior to equity
Security	Generally secured by a second-ranking lien on the collateral security package available to senior lenders and first-ranking pledge of the sponsor's shares in the borrower
Target Return	18% to 25% target return depending on macro (country / sector) and company specific considerations

FRANKLIN TEMPLETON INVESTMENTS — 10 — DARBY PRIVATE EQUITY FRANKLIN TEMPLETON INVESTMENTS

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About Squire Sanders

Founded in 1890, Squire, Sanders & Dempsey L.L.P. has lawyers in 32 offices and 15 countries around the world.

On the ground in seven CEE countries, and backed by the global expertise of our Emerging Markets Private Equity Group, our tightly integrated CEE Private Equity Team works together to seamlessly serve our clients' transactional needs – whether the deal is undertaken in one of our resident countries or across multiple borders.

We advise on all types of private equity investments and exits and have a deep understanding of the issues peculiar to key industry sectors including chemicals, communications, energy, food and beverage, financial services, hospitality and leisure, logistics and infrastructure, media, natural resources, real estate and technology.

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About C5

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