

Feeling the cold?

2008 saw a 48% decrease in the value of Russian M&A transactions but the number of transactions involving Russian and American partners did not follow the general downward M&A trends. Meanwhile, Financial Services, a sector that encountered a lot of volatility in 2008, remained steady with the volume of deals falling by just one deal and the total value increasing from US\$ 7.1bn to US\$ 11.8bn. ACQ talks to the experts to see if they are feeling the cold from the crunch.

Christopher Rose and David Wack are partners at Squire, Sanders & Dempsey LLP.

The Moscow office of Squire Sanders & Dempsey LLP is regarded as having one of Russia's leading private equity practices, representing such marquee names as Alfa Capital Partners, Baring Vostok Capital Partners, Mint Capital, Troika Capital Partners and UFG Capital Partners. Mr. Rose and Mr. Wack have authored numerous articles on private equity, including the Russian Federation chapter of the PLC Cross-border Private Equity Handbook, a leading industry resource. They were identified by Chambers Europe 2008 as two of Russia's leading private equity lawyers and were included in Euromoney's 2008 Guide to the World's Leading Private Equity Lawyers.

"At the beginning of 2008, fund managers were complaining that valuations of Russian companies were too high as competition for quality deals inflated prices. However, as the credit crisis began to worsen in Russia, tighter credit markets meant that debt financing was no longer easily accessible. In addition, larger businesses that had expected to raise funds on the capital markets were forced to consider other options. As a result, toward the end of the summer, the valuations of many companies were pressured downwards. These challenging market conditions enabled private equity firms to negotiate more aggressively, resulting in investor-friendly deal structures utilising convertible loans, investment tranches and price adjustment ratchets. Comparatively few private equity deals closed at the end of 2008 but those that did were re-priced dramatically -- often to half the valuation demanded just a few months earlier.

"The outlook for private equity in Russia in 2009 is mixed. Several of the major private equity firms are

taking a wait-and-see approach, bypassing the distressed situations that have appeared on the market and waiting for the economic climate to stabilize before making investments. Others funds intend to remain opportunistic, taking advantage of declining valuations in many cash-strapped but otherwise healthy businesses. If deals do get done in this challenging market, then 2009 will likely be remembered as the year of restructuring plays and "going private" transactions."

Anton Klyachin is a co-founding partner at Salomon Partners and head of private equity practice and employee's compensations and benefits practice.

"I am a co-founding partner of Salomon Partners, a law firm that has been established in 2006 as a local Russian independent practice by three lawyers experienced with top Russian and international law firms in Moscow. Currently we have seven lawyers.

Salomon's specialize in five interconnected areas: Corporate M&A; Private Equity / Venture Capital; Employees Compensations and Benefits; Telecom, Media and Technology; Intellectual Property.

"From the beginning of the year we have been involved in two M&A transactions, one in the forestry industry, another -- in the metal trading sector. Both transactions have been successfully closed February -- March 2008. In summer, we have participated in investment by Norum Russia (now CapMan Russia) into Region-Avia company, which transaction has been reported by ACQ. Early 2009 we have closed an investment into a small Russian satellite TV broadcaster. Now we are advising our clients on two M&A transactions in media sector and three venture capital investment deals."

"Over the last 12 months the main trend is connected with the financial crisis. Transactional landscape has undergone dramatic change -- we now see almost only rescue buy-outs, debts restructuring or sometimes recovery etc. Investment activity is pretty low these days -- everybody seems to be waiting next year.

"In 2009 we expect private equity houses to be increasingly active due to decrease of valuation expectations among Russian entrepreneurs; we also believe our M&A practice will expand on account of acquisitions of distressed assets. We also now work on expansion into contentious practices, including arbitration & dispute resolution and bankruptcy."

"We believe one of the main trends in the Russian market in 2009 will be increased M&A activity in the oil and gas and natural resources sectors. This will be a result of depressed asset values due to the low oil and other commodity prices, Russia's need for foreign capital and foreign technology to halt declining production. There will also be increased demand for refinancing of Russian companies' corporate debt"

Natalya Morozova and Rob Patterson



Rob Patterson



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Natalya Morozova and Rob Patterson are managing partners of the Moscow office of Vinson & Elkins LLP.

Natalya Morozova joined V&E in 1991 when the Firm opened its Moscow office and Rob Patterson joined in 2000 and has been permanently based in Moscow for nearly 3 years. Vinson & Elkins, one of the world's leading energy law firms, is a worldwide operation with over 700 lawyers and offices in Abu Dhabi, Austin, Dallas, Houston, New York, Washington, Beijing, Dubai, Hong Kong, London, Moscow, Shanghai and Tokyo.

"The Moscow office's main focus is servicing the needs of clients active in the energy (in particular, the oil and gas) sector, including their M&A, project development and finance needs. Our clients include oil and gas companies, oil and gas service companies, banks and private equity investors. Recent deals include significant M&A and other projects for Oman Oil Company and NOVATEK, Russia's largest independent gas producer. The Russia/CIS team, which includes lawyers based in V&E's Moscow, London and Asian offices, also handles transactions in other CIS countries, including Ukraine and Kazakhstan."

In 2008, for example, V&E advised:

- Oman Oil Company in the sale of its 7% shareholding in the Caspian Pipeline Consortium (the 1500 km pipeline connecting the oil fields of Western Kazakhstan to a marine terminal on the Russian Black Sea coast) to the Government of the Russian Federation.
- Oman Oil Company in its \$1.2 billion acquisition of an 8% equity stake in the listed company MOL Hungarian Oil & Gas in exchange for a package of international upstream oil and gas assets.
- The owner of the Russian "Yolki-Palki" restaurant chain in a leveraged buyout by a private equity fund affiliated with a major Russian industrial and financial group.
- A large US private equity group in an intended substantial investment in the Russian oil & gas sector. "Over the last 12 months a number of intended M&A transactions have been put on hold or have not closed

because of the introduction in May 2008 of the new law imposing restrictions on foreign investment in a number of strategic sectors of the Russian economy, and lack of clarity of how the new rules will be implemented. Most corporate financing projects have been cancelled or put on hold as a result of the financial crisis. Some significant investment projects by Russian companies in Russia and abroad have been delayed because of lack of funds and uncertainty as to the demand.

"We believe one of the main trends in the Russian market in 2009 will be increased M&A activity in the oil and gas and natural resources sectors. This will be a result of depressed asset values due to the low oil and other commodity prices, Russia's need for foreign capital and foreign technology to halt declining production. There will also be increased demand for the refinancing of Russian companies' corporate debt."

Chris Allen is partner, head of Moscow M&A Group at Latham & Watkins LLP

Last year the firm was involved in the acquisition of the Myagkov vodka business for the firms listed client Synergy. This was a major deal in the drink/alcohol industry.

"We advised AFK Sistema on its telecoms investment into Shyam Telelink, a first major investment by a Russian corporate into India."

"Last Summer was a huge wake up call and nobody can say when, or even approximately when, the markets will improve. I am aware of various clients with cash ready to spend, but I think it will be some time yet before they make their move. Others are too busy rescheduling debts to think much about M&A plans.

In regard to 2009 predictions: "I was in Russia after the '98 crisis and for the brave investor there will be some real opportunities, just like ten years ago. Many perfectly viable companies have been swept up in the maelstrom. There are some great valuations out there and those with cash and a discerning taste for a bargain will make money for sure." **ACQ**