

Marketing services mergers and acquisitions

Grant Thornton Corporate Finance, Mergers and Acquisitions Summer 2010

Activity returns to pre-recession levels

M&A activity within the marketing services sector has returned to the pre-recession levels experienced in mid-2007, with the number of transactions increasing in each of the past three quarters. The first quarter of 2010 was a particularly active period, with deal volume returning to peak levels.

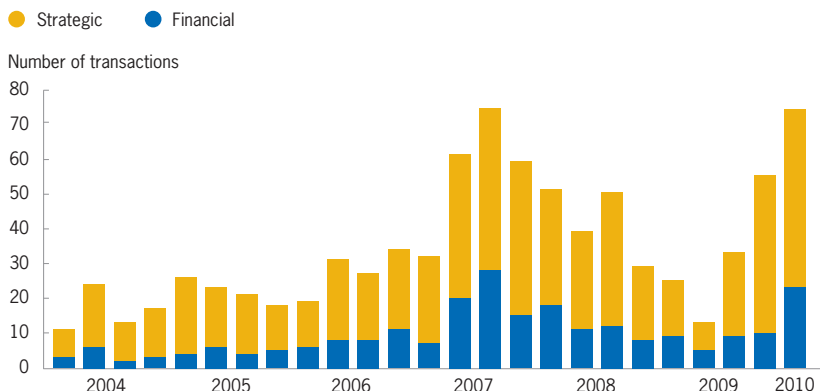
continued>



Highlights

- Marketing services M&A activity returns to pre-recession levels (by number of transactions)
- More deals between smaller buyers and sellers
- Private equity firms are active acquirers of traditional marketing firms
- Digital firms continue to be acquired by technology, media and full-service players
- Large agencies turn attention to emerging economies
- Organic revenue growth returns
- Mailing services M&A activity also rebounds

Marketing services quarterly M&A activity; number of transactions (2004–2010)



Sources: GTCF research; certain information taken from Capital IQ

Grant Thornton Corporate Finance Mergers & Acquisitions

Ian Cookson

Director, Investment Banking
T 617.848.4982 E Ian.Cookson@gt.com

Ari Goldschneider

Analyst, Corporate Finance
T 617.848.4905 E Ari.Goldschneider@gt.com

Grant Thornton Corporate Finance LLC

226 Causeway Street
Boston, MA 02114

www.GrantThornton.com

Activity returns to pre-recession levels (continued)

Shift in acquirer landscape

The acquirer landscape within marketing services has shifted since the M&A peak in mid-2007. The data supports what we are seeing in the market, namely that smaller agencies have become increasingly acquisitive and are buying close to home. The average disclosed deal size within marketing services fell from \$368 million in 2007 to \$112 million currently, while the median disclosed deal size has fallen from \$20 million to \$10 million.

Most active buyers of U.S. targets – 12 months ending April 2010

MDC Partners	4
Merkle	3
WPP	3
Barkley	2
Beckerman PR	2
Domain7 Solutions	2
Google	2
GSI Commerce	2
Invicta Group	2
Kahzam	2
Next Fifteen Comm.	2

Sources: GTCF research; certain information taken from Capital IQ

The large marketing services agencies/conglomerates, meanwhile, have focused their M&A activity overseas, particularly in emerging economies. Three-quarters of the acquisitions by large agencies in the past 12 months have been outside the United States, with one-half of those acquisitions being in emerging markets. Only three firms (MDC Partners, WPP and Merkle) reported three or more U.S. acquisitions in the past year.

The larger U.S. transactions can be summarized as digital firms being acquired by technology and full-service players, while traditional and direct marketing businesses are seeing significant acquisitions by private equity:

Marketing services transactions over \$100 million – 12 months ending April 2010

Target	Type	Buyer	Value (\$ in millions)
Omniure Inc.	Digital (analytics)	Adobe Systems Inc.	\$1,676
AdMob Inc.	Digital (mobile)	Google Inc.	\$750
infoGROUP Inc.	Direct	CCMP Capital	\$645
Razorfish	Digital (campaign)	Publicis Groupe SA	\$530
Carlson Marketing Group	Loyalty	Groupe Aeroplan Inc.	\$169
Cossette Inc.	Full service	Mill Road Capital	\$159
EyeWonder Inc.	Digital (campaign)	Limelight Networks, Inc.	\$116
Transcontinental Direct	Direct	WCO Direct (Avista Capital)	\$113

Sources: GTCF research; certain information taken from Capital IQ

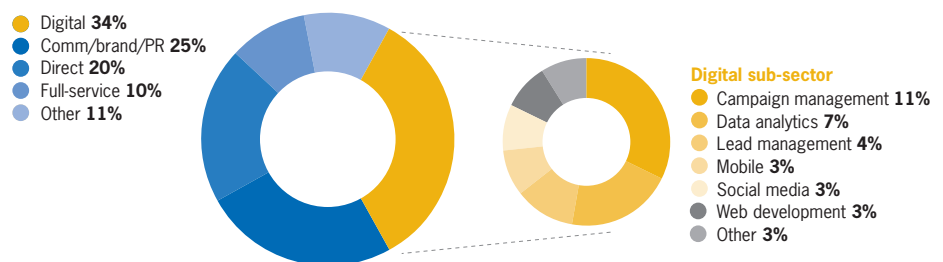
- On the digital side, Adobe acquired online marketing analytics provider Omniure; Google purchased mobile advertiser AdMob; Publicis Groupe bought digital firm Razorfish from Microsoft; and Limelight Networks purchased interactive agency EyeWonder.
- Among direct marketing and full-service businesses, where private equity has been active, CCMP Capital acquired infoGROUP; IWCO Direct (owned by Avista Capital) bought Transcontinental Direct; and Mill Road Capital purchased Cossette.

Breadth of acquisition targets

Digital firms have continued to be attractive targets, comprising around one-third of marketing services transactions. Roughly one-half of digital transactions have been executed by full-service firms and other digital agencies seeking to build out their interactive activities by acquiring online advertising campaigners; online lead management companies; online data analytics providers; mobile and social media firms; and website developers. The remaining transactions have been acquisitions by technology and media players purchasing online data analytics and mobile advertising firms to access new capabilities and leverage their service offerings.

continued>

Marketing services transactions by target sub-sector – 12 months ending April 2010



Sources: GTCF research; certain information taken from Capital IQ

Activity returns to pre-recession levels (continued)

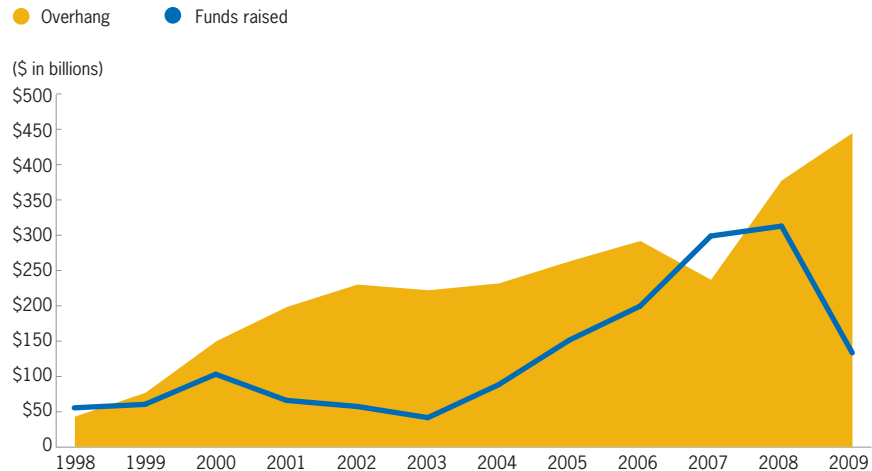
Traditional marketing services businesses, which accounted for around two-thirds of M&A activity and normally trade at lower multiples, have seen greater interest from private equity.

As with the acquisition of digital firms, we typically find that the best buyer is one positioned to address the challenges the target faces and/or a transaction enables the buyer to overcome issues it is wrestling with. Consequently, ideal buyers — even for smaller firms — often operate in adjacent spaces (whether those be sector, functional or geographic) where the buyer and seller are able to tap into each other's skills and client relationships for mutual benefit.

Often, our clients have built their businesses beyond a size suitable for individual ownership. As each business matures, the needs, interests and cash requirements of the owner and the business tend to diverge. Consequently, the primary shareholders may feel that they are more likely to hinder rather than help the future progress of the company. We have found private equity buyers to be particularly adept at not only providing liquidity, but also addressing the softer areas (creativity, motivation and assistance) to enable a transition to the next generation of management.

Digital firms have continued to be attractive strategic acquisition targets while traditional marketing services businesses have seen greater interest from private equity.

U.S. private equity overhang and funds raised



Source: PitchBook Data Inc.

Private equity: An attractive option for sellers

As noted above, private equity continues to play a major role in sector consolidation, accounting for roughly one-quarter of deal volume (versus 16% across all sectors of U.S. M&A activity). Private equity is comfortable investing in the sector, with more than 100 firms completing marketing services acquisitions in the past five years (roughly one-quarter have made two or more sector acquisitions). Recently, we have witnessed an increasing number of financial sponsors pursuing roll-up strategies through their existing portfolio businesses, with add-on acquisitions comprising roughly one-third of private equity activity over the past 12 months.

Private equity firms will likely remain active acquirers, as they have raised record amounts of capital that has yet to be invested. Cumulative overhang, the gap between funds raised and equity invested, has reached historic levels (currently at \$445 billion), and managers are seeking additional venues to deploy capital.

Unlike transactions between smaller strategic players, where payouts often comprise a sizable component of deferred consideration (either through an earnout or a seller note), we have been able to help create outcomes with private equity that provide sellers with more flexible transaction structures. These have ranged from complete sales to transactions involving significant up-front cash while retaining management control and access to additional capital for business expansion.

continued>

Activity returns to pre-recession levels (continued)

Public company valuation levels rebound

The market value of our public company marketing services index has increased by more than 50% over the past 12 months, as valuation multiples have rebounded on relatively flat earnings. In the public markets, large agencies and database marketers are trading around 8x EBITDA (up from their low of around 5x over a year ago), digital firms are trading around 11x EBITDA, and printing/direct mail businesses are trading around 6x EBITDA. Notably, as digital marketing has become mainstream the valuation gap between traditional and digital firms has narrowed considerably.

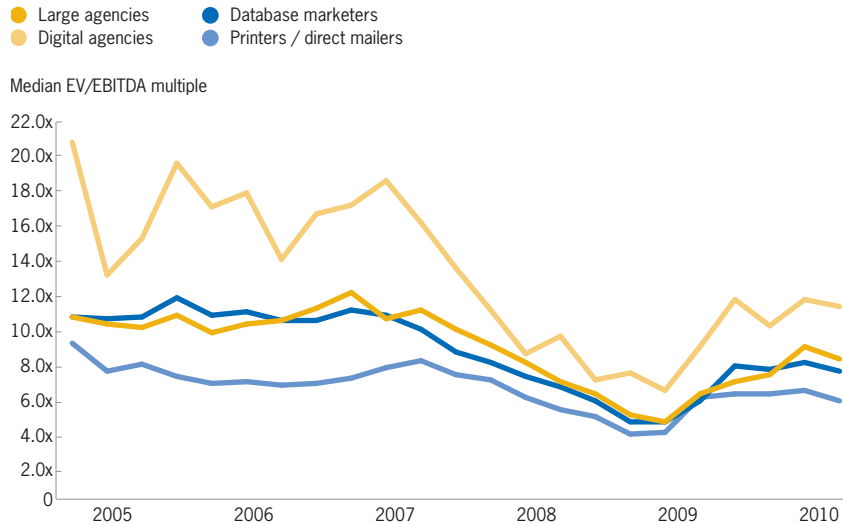
Large-company transaction multiples broadly reflect these public market valuations: Marketing firms infoGROUP (\$637 million) and Cossette (\$131 million) were acquired at multiples of 7.5x and 7.0x EBITDA, respectively, while analytics firm Omniture (\$1.7 billion) was acquired by Adobe at a sizable premium.

Interestingly, despite the doom and gloom, earnings (as measured by EBITDA) of publicly traded marketing firms in our index have declined less than 13% from their peak in mid-2007. There are more signs that the economy may be improving: Large marketing agencies have experienced an increase in median EBITDA profitability to 14.2% from 12.9% in 2008, and Q1 2010 saw growth in organic revenue for the first time in more than two years.

continued>

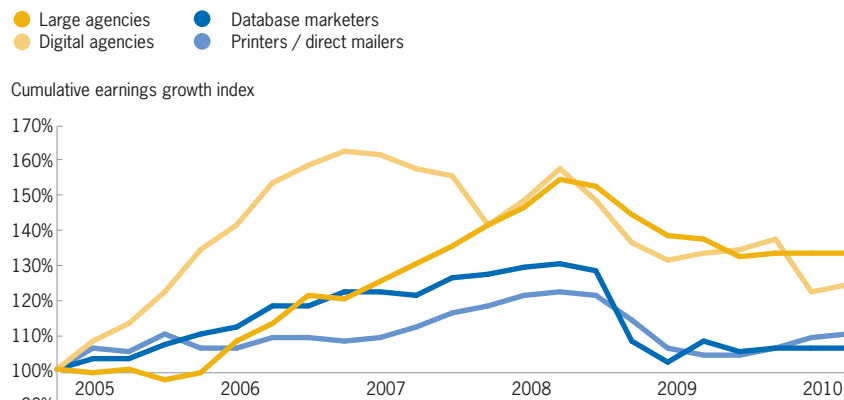
The market value of our public company marketing services index has increased by more than 50% over the past 12 months, as valuation multiples have rebounded on relatively flat earnings.

Marketing services public company valuation multiples by sub-sector



Sources: GTCF research; certain information taken from Capital IQ

Marketing services public company earnings by sub-sector



Sources: GTCF research; certain information taken from Capital IQ



Activity returns to pre-recession levels (continued)

Mailing services M&A returns

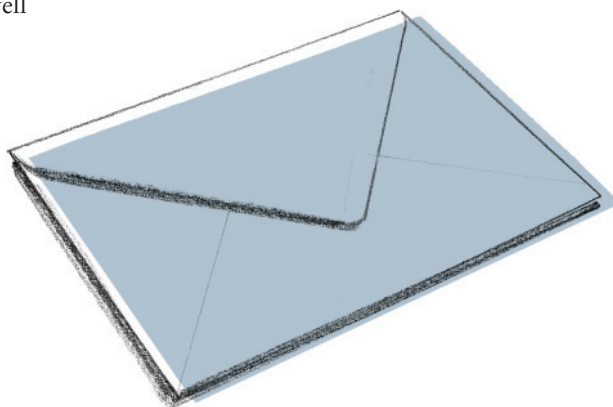
In the adjacent sector of direct mail, list management and fulfillment, M&A also took off during the first quarter of 2010, returning to quarterly levels last seen in 2007 (after a significant downturn). Private equity has been exceptionally active, accounting for almost one-half of sector buyer activity over the past 12 months. This disproportionate interest from private equity has been split almost equally between direct investments in new-platform companies and add-on acquisitions for their existing portfolio businesses pursuing consolidation strategies.

This is despite declining mail volumes — down 17% from their 2006 peak — driven by a weak economy and the structural migration to electronic alternatives. A 2010 Government Accountability Office report tellingly titled “U.S. Postal Service: Strategies and Options to Facilitate Progress Toward Financial Viability” demonstrates the severe impact falling volumes have had on profitability given the USPS’ relatively fixed cost base.

Within printing, we have seen activity by larger players, including RR Donnelley’s purchase of information provider Bowne (\$480 million), as well as transactions by Quad/Graphics, Consolidated Graphics, Cenveo and IWCO.

Summary

- After bottoming out in Q2 2009, marketing services deal volume has trended upward, with activity in Q1 2010 returning to peak levels.
- The buyer landscape has changed, with a greater portion of strategic transactions involving smaller acquirers and targets, while large agencies have turned their attention to emerging markets.
- Private equity is active in the sector, comprising roughly one-third of deal volume and providing attractive exit opportunities for sellers of traditional marketing services firms.
- Digital acquisitions continue to be sought after by full-service, technology and media players.
- Public company valuation levels have rebounded substantially from the lows experienced in early 2009.
- In Q1 2010, public marketing firms realized quarter-over-quarter organic revenue growth for the first time in more than two years.
- Direct mail, list management and fulfillment experienced significant increases in M&A transaction volume in Q1 2010. •



The factual statements, including data from third-party sources, contained herein are taken from sources believed to be reliable, but such statements are made without any representation as to accuracy or completeness or otherwise. Grant Thornton Corporate Finance LLC does not engage in the business of recommending or effecting transactions in securities. The above information is presented solely in connection with describing Grant Thornton Corporate Finance LLC’s mergers and acquisitions services and should not be considered as constituting a research report or as providing information reasonably sufficient upon which to base an investment decision.

About Grant Thornton Corporate Finance

Grant Thornton Corporate Finance provides boutique investment banking services to privately held middle-market businesses in the United States and around the world. As a recognized advisor on middle-market mergers and acquisitions, we offer a range of investment banking services including sell-side advisory, buy-side advisory, management buyouts, restructurings and capital raising. Grant Thornton LLP provides investment banking services through its wholly owned broker-dealer subsidiary, Grant Thornton Corporate Finance LLC, member FINRA, SIPC.

About Grant Thornton LLP

The people in the independent firms of Grant Thornton International Ltd provide personalized attention and the highest-quality service to public and private clients in more than 100 countries. Grant Thornton LLP is the U.S. member firm of Grant Thornton International Ltd, one of the six global audit, tax and advisory organizations. Grant Thornton International Ltd and its member firms are not a worldwide partnership, as each member firm is a separate and distinct legal entity.

www.GrantThornton.com

© 2010 Grant Thornton LLP
All rights reserved
U.S. member firm of Grant Thornton International Ltd