

**M&A INTERNATIONAL:
FIRST STRATEGIC ACQUIRORS
FORUM HELD IN NEW YORK**

The JR/Janus team met with over 100 other leading M&A practitioners representing member firms from 29 countries at the M&A International Inc. semi-annual forum in New York City on May 14 and 15, 2004.

Included on the agenda was a Strategic Acquirers' Forum in which 7 acquisition groups, including such companies as Fedders Corp., Hitachi, and RPM International, met with M&A member firms to discuss the latest M&A trends and valuations, and consider acquisition targets across five continents.

Following the success of this forum, M&AI has confirmed that the next semi annual meeting will be held in October 2004 in Amsterdam, in conjunction with the M&AI Mid-Market Forum.

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Specialists in mid-market acquisitions, divestitures,
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IMPROVE THE ODDS OF A SUCCESSFUL ACQUISITION WITH STRATEGIC AUDIT

-- Jack Woodcock, President

STRATEGIC AUDIT was developed by JR/Janus to assist our clients to evaluate the strengths, weaknesses, and future possibilities of an acquisition candidate. It is equally useful for the current owner, considering present worth, and future prospects.

In our experience there are three primary reasons acquisitions fail to meet a buyers' expectations. The first is overpaying, making at least the financial targets unachievable. The second reason, about which legions have been written of late, is a cultural misfit of the combining entities. This results in "turned-off employees," the very people responsible for making the acquisition successful.

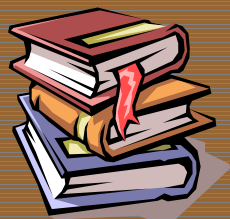
The focus of this article is on reason number three...failing to adequately assess the strategic factors that drive performance to create a successful company, which obviously can distort the assessment of risk and value. In the past 17 years, we have seen too many acquirers and their advisors spend the bulk of their "due diligence time" reviewing the accounting numbers of the acquisition target, evidencing historic performance, with painstaking detail. They identify what has happened. But they may not have gained a clear understanding of why those results were the way they were. Therefore, they may not be able to assess what future performance is likely to be, based on the "drivers" referred to above. Strategic Audit is a methodology to help a buyer make such assessments efficiently and effectively. Obviously the discipline requires collecting and inputting information tailored to a specific company.

The 5 factors we believe drive the performance of every business are: market attractiveness, competitive position, financial capability, supporting infrastructure, (including people and technology) and the current focus of the business.

When the buyer, (or the owner), is already in the space, and intimate with the market, competition and technology, the required intelligence may be readily available. When the territory is new to the buyer, substantially more "research" is mandatory. Clearly, to be useful, any assessment must be based on facts, not supposition. Guessing or ignoring the assessment of the drivers of performance altogether makes an acquisition more like a lottery than a wise business decision.

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CORNER



In an effort to reduce the complexity in M&A and Corporate Finance terminology, M&A Monitor includes a few definitions of terms whose meaning may not be obvious to those outside the industry:

LETTER OF INTENT:

The stage of an offer preceding a formal Purchase and Sale Agreement. The terms of the deal as agreed between buyer and seller are spelled out in significant detail, but most often are subject to Due Diligence. In certain circumstances, the Letter of Intent can be binding, and may be accompanied by a non-refundable deposit as a show of the seriousness of the acquirer to go forward to Closing under the terms outlined in the letter.

LEVERAGE:

This is a financing technique, whereby the proportion of debt to total capital employed is maximized, thereby minimizing the equity component. The effect of this is to increase the percentage of bottom line return over equity invested. The technique only works successfully where the EBIT of a business, as a percentage of total capital employed, exceeds the average before tax cost of debt (raw interest rate).

LIQUIDATION VALUE:

Also known as "Breakup Value", this is the likely value that could be received if the assets of a business were sold off in a piecemeal fashion. This value is usually much lower than if the assets are sold as part and parcel of a healthy, profitable, going concern business. Typically in a liquidation under strained financial conditions, the proceeds are not sufficient to pay creditors one hundred cents per dollar owed to them.

LOSS CARRYFORWARDS:

These are losses for tax purposes, incurred in prior years, which are available to a corporation to carry forward, for a prescribed number of years, and are available within that time period to reduce taxable income and the tax that would be otherwise payable. Both Capital and Non-Capital losses may be carried forward for specified periods.

M&A INTERNATIONAL ADMITS THREE NEW MEMBERS

The new members from three continents, the Americas, Africa, and Europe, brings the network's total number of firms to 37 across 29 countries.

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JANUS CORPORATE FINANCE SYNDICATES LIFE SCIENCE FUNDING

London-based nutraceutical company raises growth capital in common share private placement

On April 3rd, 2004 Janus Corporate Finance closed the syndication of a common share private placement for KGK Synergize Inc. (KGK) of London, Ontario. Originally founded as a provider of contract research services for others in the nutraceutical field, KGK has developed its own pipeline of patented nutraceutical products to treat and/or prevent some forms of heart disease, type II diabetes, and a variety of cancers through natural, food-based formulations.

The company's first fully developed and patented nutraceutical product is Sytrinol™, proven in three separate human trials to significantly lower LDL cholesterol and triglyceride levels in humans. Sytrinol™ is currently being launched in the U.S. and European markets in a number of major retail chains by SourceOne Global of Chicago, IL, a licensee firm.

While details of the private placement financing are not disclosed at the client's request, the fresh equity capital will allow KGK to commercialize the company's remaining pipeline of patented nutraceutical products, and expand its contract research unit.

"The Janus Corporate Finance team did a terrific job of preparing us for investor presentations by bringing focus to our strengths and core competencies" said Najla Guthrie, CEO. "We were also extremely pleased with the variety of funding sources identified in the private placement process which ultimately provided us with the flexibility to choose our new equity partners carefully. Overall, the disciplined approach and experienced insights of the Janus Corporate Finance team really paid off for us. For anyone looking to raise capital, I would strongly recommend a call to Janus Corporate Finance."

STRATEGIC AUDIT (cont'd)

The 5 categories and 46 factors identified by Strategic Audit, each of which can be a harbinger of success – or failure, must be “scored” according to one of three grades: an exceptional opportunity; satisfactory; or very importantly, a “rethink” category, either because of the “facts” or because the answers to the questions raised could threaten the viability of future performance.

For example, growth is a critical driver within the Market Attractiveness category. In this case, using our experience in the food industry, we suggest that a market (or niche / segment) growing in excess of 10% per year represents an exceptional opportunity. Growth of 0 to 5% probably should be deemed satisfactory. And when a market is shrinking (negative), we suggest that is reason to question an entry / acquisition decision.

	EXCEPTIONAL	ACCEPTABLE	RED LIGHT - RE-THINK
Growth			
- Historic	> 10	0 – 5	Negative
- Future	> 10	0 – 5	Negative

Obviously, the intent is to distinguish how each factor will contribute to the success of a business in the future, or pose a threat. When a factor is scored “rethink,” the buyer must pause and consider (a) whether the factor can be altered to become acceptable at minimum; (b) whether the implied weakness can in fact lead to failure.

A strategic acquirer should predict the impact their existing operations could have on where a factor is ultimately categorized. However, any strategic driver not meeting an acceptable standard should be cause for concern. Satisfactory can become exceptional; and “rethink” perhaps can be moved to Satisfactory, but that will demand a commitment to a very specific plan of action.

The bottom line of Strategic Audit is much more than the numbers / financial analysis so common in due diligence. Rather, applied in a disciplined manner, the tool gives the assessor a meaningful appreciation for the strengths and weaknesses implicit in the performance drivers that will most influence future success. Clearly, Strategic Audit must be translated into an action plan which can and should influence the go / no go decision, plus consideration of the purchase price, with logic that goes well beyond multiples of EBITDA, PE ratios, or even our favourite, Discounted Cash Flow. (The examples shown in the following use quantitative measurements derived from our experience in the food industry. Obviously the measurements must be tailored to the specific industry situation.)

Without question, in spite of a dedication to fact-finding, Strategic Audit will require a lot of professional judgment. The bias of the tool therefore is not on arithmetic precision, but rather ensuring that the ultimate decision covers all the bases – in this case the performance drivers, and how they are likely to influence future success. And that is the true measure of business “worth.”

The following below outlines the factors falling within the five most common performance drivers. As stated earlier, the process may have to be adapted to each specific industry situation.

MARKET ATTRACTIVENESS

“...and may the wind be always at your back”. That Irish saying is excellent advice to anyone assessing their market. Modest performance in a positive, growing market can produce substantial rewards, whereby even relatively outstanding accomplishment in a negative market environment may produce unsatisfactory results.

	EXCEPTIONAL	ACCEPTABLE	RED LIGHT – RE-THINK
Growth			
- Historic	> 10	0 – 5	Negative
- Future	> 10	0 – 5	Negative
Life Cycle	Early Growth	Mature	In decline
Seasonality	NIL	Modest	Pronounced
Reliance on Supply / Suppliers	No shortage of suppliers)	A few sources	No alternate source
Size			
- Total			
- Niche			
Available Info			
- Competitors	Lots – recent – factual	Partial	Speculation only
- Customers / Consumers	Lots – recent – factual	Partial	Speculation only
Customer / Consumer Trends	End-use exploitative of trends (i.e. demography)	Neutral	Contradictory (i.e. buggy whip) 1 = 25 – 50%
Distribution Channel Leverage	Partnership	Balance	Absolute freedom to dictate terms & discontinue. Difficult / impossible to pass on price increases.
Technology	Evolution	Static	Impending revolutionary change that will obsolete product or production infrastructure.
Barriers to Entry			New entrants can easily access capital, infrastructure & technology required.

STRATEGIC AUDIT (cont'd)

COMPETITIVE POSITION

A David may slay a Goliath, but it better have some relevant strength that is treasured by the customer base.

	EXCEPTIONAL	ACCEPTABLE	RED LIGHT – RE-THINK
Share Position	# 1	#3	< #3
Absolute Share of Market or Niche	> 30	10 - 20	< 10
Distribution	Approaching 100% coverage	Covers all key markets	Partial of market distribution
Uniqueness	Proprietary advantage patented	Parity	< Parity
Price / Value Relationship	Superior	Parity	< Parity
Dominance	Most influential competitively	Equal to	Insignificant market impact
Core Competence			
Low Cost Producer	Lowest	Parity	Higher than
Substitution	None available		Commodity
“Brand” Loyalty	Customers perceive superiority - choose every time	Choose frequently - one of two or three	No meaningful difference
Price Sensitivity	Consumers prepared to pay premium price	Will choose product / service when priced at parity	Consumers don't have a regular brand. Consumers buy lowest price – on special.
Strength	Stronger than principal competitors		Competitors are dominant, much larger / stronger

INFRASTRUCTURE

Tackling any job requires the proper tools. A company is no different conceptually than a carpenter or plumber; just a grander scale. If a company doesn't have, or can't quickly get resources in keeping with the challenge, failure is highly probable.

	EXCEPTIONAL	ACCEPTABLE	RED LIGHT – RE-THINK
Sales Capacity			
R & D	Unique skills	At par	Not at par with principal competitors
Manufacturing Equipment	State-of-the-art	Old, but competitively efficient	Obsolete
Technology - Production - Life Cycle	Clear leadership & lead time to next generation	Parity	Obsolete relative to competition
Location(s)	Proximity to key markets which creates competitive advantage	Geography not a factor	Distance from key markets creates disadvantage
Staff - Operations - Management - Labour Relations	Highly qualified people you can bet on, non-union, tangible evidence of excellent relationships	Union; no track record of serious problems	Extremely vulnerable to “hard to find” people. Hostility between labour and management or threatened unionization.
Capital Intensity	Cash flow positive after WC & capital needs		Negative cash flow
Succession	Backstop in very position or replacements readily available		Goodwill associated with current people because of personal qualities, no backups in place

STRATEGIC AUDIT (cont'd)

FINANCIAL

Some financial weakness can be remedied with a cheque book, which is fine if that is factored in to the valuation/evaluation of a business. However, certain performance realities, such as Sales Trend and Gross Margin are much harder to alter.

WEIGHT	EXCEPTIONAL	ACCEPTABLE	RED LIGHT -- RE-THINK
Debt / Equity	< 30 / 70	50 / 50	> 50 / 50
Interest Coverage	> 2	1.0 – 1.5	< 1
Sales Trend (last 3 year average)	+ 10	1 -- 5	< 1 -- Negative
Gross Margin	> 30	20 -- 25	< 20
Credit Usage	< 50	75 -- 100	> 100
Acid Test			
Cash Flow (next 5 years)	++	Neutral	Negative
Annual Inventory Turns			
WC / Sales			
Capital Expenditures (CAPX)	Will not need depreciation	Depreciation = CAPX	Cannot replace assets with existing capital structure
Capital Structure	Major redundant financial capacity	Can withstand temporary downturn	Hand to mouth, re: cash

CURRENT FOCUS

"Keep your eye on the ball". "Many hands make light work". "A chain is only as strong as its weakest link". These simplest expressions provide the most sophisticated counsel as to how to determine if a company is truly focused on its mission. The CEO can state the company's goals in the annual report, but the true test is whether those in the "ranks" understand what is expected, and internalize how their individual role relates the "grand plan". Obviously this plan must be reasonable in the context of the other factors, market, competition and available resources.

	EXCEPTIONAL	ACCEPTABLE	RED LIGHT -- RE-THINK
Strategy	Defined strategy understood top to bottom	Defined strategy generally understood	Not defined
Goals	Individual mandates exist in context of corporate strategy & goals	Corporate goals generally understood	Individuals do not connect personal challenges to corporate goals
Portfolio	Single focus or complementary, counter-cyclical & / or synergistic		Diverse, no connection, similar volatility / cyclicity
Vision / Foresight	A fix on possible futures that reflect understanding of trends in demand & technology in context of the organization's current & potential capabilities	Assume future will be linear, but have some competitive advantage which can continue to be exploited	Assumes future will be linear & already lacks clear cut competitive advantage
Meets Shareholder Needs	Specific fit, re: risk, return & values	Complementary	No confirmation, no mechanism to do so

Strategic Audit is certainly not a replacement for the traditional numerics of due diligence. But the reverse is also true. A careful scrutiny of relevant performance drivers will most definitely flag the realities and risks. Used effectively, it can validate (or negate) an acquisition, contribute to action plans to optimize the odds of a success, or help improve an existing business. We'd be delighted to speak with you about this tool.

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