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Strength As A Weakness?

AMGEN, DOW LAND ON LBO LIST

Amgen, Baker Hughes, Dow Chemical and a handful of other corporations with high credit ratings and sagging share prices have become leveraged buyout candidates. Observers say that as the prospect of higher bond yields and more expensive debt appears certain, companies with the best ability to sustain debt payments will look more attractive to buyout shops.

“They’re absolutely better candidates,” said **Lance Pan**, director of investment research at **Capital Advisors Group** in Newton, Mass., who compiled the LBO list. Companies with credit ratings from **Standard & Poor’s** of A and AA used to be considered safe, Pan noted. “It’s an irony that supposedly safer names are becoming more risky than junk issuers.”

Pan’s team compiled the list to help bond investors “navigate the LBO minefield.” They screened A and AA rated names with market capitalizations below \$50 billion, lagging share prices and strong cash flow. They used nine criteria and awarded a point for each. Six scored an eight out of a possible nine (see chart).

“Nobody is safe from a buyout anymore,” said **Patrick Lawler**, an attorney who works on deal financing at **Chapman and Cutler** in San Francisco. “Size is no longer a defense. Heavy leverage is a defense.”

Pan noted a paradox of the current climate. If a portfolio manager wants to play it safe, he may want to buy a riskier credit, a BBB rated issue rather than an A or AA. The riskiest junk bonds also typically have stronger protection from buyouts in the form of covenants, although some issuers have recently managed to drop change of control puts (CFW, 5/28). Buyers have prodded **Home Depot** and other investment grade issuers to attach buyout protection to their new issues, but only in the past year.

LIKELY TARGETS?

Amgen
Baker Hughes
Bemis
Dow Chemical
Home Depot
Occidental Petroleum

—*Matthew Craft*