CLIFFORD
CHANCE

A GLOBAL SHIFT

SEPTEMBER 2017 UPDATE:
Our M&A insights and
deal intelligence 2017

C L I F F O R D

C H A N C E

LOOKING AHEAD TO THE END OF 2017.

"There was a slow start to the year, with mergermarket figures showing M&A activity down 24% (by value) in H1 as compared to the previous 6 months, and particularly sharp falls in the US and the Asia Pacific region. Even the strong fundamentals of low interest rates and benign debt financing conditions could not arrest the slide. We see three principal reasons for this.

First, a 'wait and see' approach for many multinationals, as they continue to observe the regular flow of geopolitical chaos. Secondly, outbound foreign investment restrictions in China put a strong brake on Chinese investment overseas. Thirdly, in today's politically-charged environment, rising government, antitrust and regulatory hurdles are increasing implementation risk and complexity, with big deals either taking longer to land or often failing to leave the starting blocks at all.

We nevertheless expect that the global M&A market will strengthen in the final months of the year. The past few weeks have seen some bold cross-border deals announced, including Vantiv/Worldpay, Cheung Kong's purchase of ista* and the US$12bn take private bid by a Chinese Consortium for Singapore's Global Logistic Properties*. The picture around China's curbs on capital outflow may also be brightening. Shareholder voices and activism are leading to corporate break-ups, sales of non-core assets and new acquisitions. In certain sectors, the low-growth environment continues to drive boards to take action, which is promising for activity levels as we head to the year end.

Record levels of dry powder are driving activity in private equity as financial investors look to capitalise on volatile currency markets and corporate break-ups. Also, firms across all sectors are focusing on lower-value but strategically-critical investments and partnerships in digital technology and innovation."

Guy Norman,
Global Head of Corporate,
Clifford Chance LLP

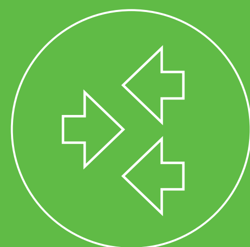
* Clifford Chance is advising on these transactions

THE TRENDS WE ARE SEEING

2017 TO DATE, AND OUR EXPECTATIONS FOR THE REST OF THE YEAR:

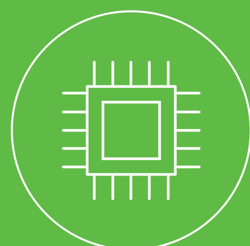
China outbound deals paused – As we predicted at the start of the year, the uncertainty around China's restrictions on capital outflows has led to a sharp decline in Chinese outbound activity. We are now seeing the pipeline strengthening, as clarity emerges over regulatory attitude, and we expect more China outbound activity in the final months of the year.

A surge in Consumer sector M&A in H1 – Consumer M&A announced in the first half of 2017 beat the value for the sector's M&A activity in the whole of 2016, as sluggish organic growth in mature markets drove consolidation. Consolidation will be a feature of the market for the remainder of the year.



Increased Antitrust deal scrutiny – Acquisitions of data-rich companies now raise full-blown competition issues, at least in Europe, which makes multi-jurisdictional transactions far more likely to be scrutinised or challenged when there is a significant data element.

European M&A market is strengthening – Europe surfaces from a prolonged 'soft' M&A period, and we are seeing increasing deal activity across the continent as a result of regional M&A activity and inbound acquirers from North America. M&A in Germany and Spain is expected remain strong as we head to the year end.



Non-controlling stakes to secure strategic opportunities – Businesses are focussing on strategic opportunities, particularly around digital/innovation, through minority investments in innovative businesses. These strategic stakes are key to secure access to new technologies without over-burdening the balance sheet or creating a cluster risk.

Private equity revival – Strong buyout levels in Europe are due to a relatively weak £, continuing availability of cheap debt and record levels of dry powder. Investors are however wary of paying ever higher prices in the highly competitive environment. In the US, exits continue to surpass buyouts. Funds are looking to hold assets for longer through long term holding vehicles or strategic funds. We expect to see ever more complex corporate carve outs and "bolt-on" strategies.

CHINA'S RESTRICTIONS ON CAPITAL OUTFLOWS: WHAT'S NEW?

China is restricting outbound foreign investment through a tightening of its approval and filing regimes in a bid to curb depleting FX reserves. Largely as a result of this, Chinese outbound M&A announced in the first six months of 2017 is down 42% on the previous six month period. However a good number of outbound deals, including big-ticket M&As, are still being done.

Greater clarity around regulatory attitude

- On 18 August 2017, the Chinese government published a set of outbound investment guidelines aimed at regulating "irrational" overseas acquisitions by restricting investments in certain sectors such as real estate, hotels, movie studios, entertainment and sports clubs. However, outbound transactions that are consistent with China's 'Going Out' policy from a sector perspective or reflective of Chinese Government's 'One Belt One Road' strategy will continue to receive strong support.

- The recent guidance effectively formalises previously published piecemeal rules as well as unofficial measures, and helpfully classifies types of investment and sectors as 'encouraged', 'restricted' or 'prohibited'.

Rumoured relaxation of FX policy

- As the foreign exchange reserve of China has stabilised in recent months, it has been rumoured in the market that some of China's local foreign exchange authorities (SAFEs) are starting to relax to a certain degree their tightening of cross-border remittance in some cases. It remains to be seen how far this goes in practice.

Impact on deal terms

- China's restrictions cause significant nervousness among foreign sellers around the ability and feasibility of Chinese bidders to close an outbound transaction, particularly from the funding perspective. Reverse break-up fees and signing deposits payable by Chinese bidders have become standard market practice, with a higher amount typically requested than in previous years.

Innovative deal structures

- On large or complex outbound deals, we are seeing PRC strategic investors increasingly team up in a consortium structure with one or more PE investors who have funds available offshore. Alternative offshore financing arrangements, e.g. bridge financing or full leverage financing, are also increasingly considered by Chinese bidders in the current environment.

ENCOURAGED:

- Support for 'One Belt and One Road'
- Export of China's advanced production technology and capacity
- High-tech investment/offshore R&D
- Energy/mining exploration; agriculture; commerce, culture, logistics
- Growth of Chinese financial institutions

RESTRICTED:

- Investment in sensitive regions
- Real estate, hotels, movie studios, entertainment industry, sports clubs
- Equity investment where no substantive project
- Violation of the host's environmental, energy or safety standards

PROHIBITED:

- Export of military technology/products
- Banned exports
- Sex industry and gambling
- Violation of China's international treaties
- Harm to national interests/security

"Using innovative security and funds flow structures, we are helping bidders address the regulations in a meaningful way while ensuring the deals get done"

Glen Ma,
Corporate M&A Partner,
Shanghai

5 PRACTICAL TIPS TO GET THE DEAL DONE

Outbound deals are undoubtedly more difficult to execute than was the case pre-November 2016. A number of outbound deals have run into difficulties due to increased uncertainty surrounding governmental approval and the timescale for obtaining clearance for funds to be remitted outside China. Chinese bidders should be prepared to structure deals with offshore funds and commit significant deposits or reverse break up fees early in the deal process, to address regulatory concerns.

Commit a deposit at signing

It is increasingly common to see Chinese bidders pay a significant deposit, placed in an escrow account outside China, at deal signing. We are also seeing demands for evidence of the buyer's ability to fund.

Address concerns on deal certainty early

Chinese buyers need to proactively address foreign sellers' concerns about deal certainty, including: Which government approvals or filings are required in order for funds to be remitted? How will the purchase price be funded? Are the funds already offshore? If debt financing is used, how certain is the bank's commitment to fund?

Engage with authorities asap

Chinese buyers are encouraged to consult with the competent Chinese authorities and the relevant bank in charge of remittance of funds out of China as early as possible, to obtain their clear support for the transaction and take into account the additional time that may be required to secure the relevant approvals and filings.

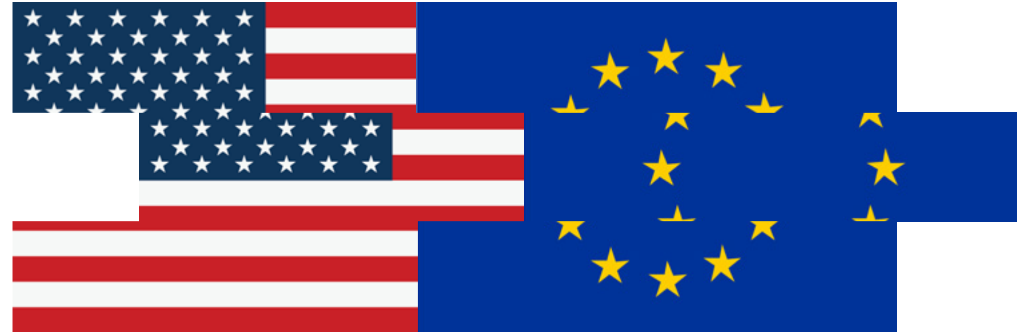
Letters of credit

To offer more comfort to foreign sellers, Chinese buyers may seek to provide letters of credit/guarantee given by either a foreign bank or an offshore branch of a Chinese bank, to secure the payment obligation of the Chinese buyers in favour of the foreign sellers. The banks issuing such letters would typically rely on a back-to-back guarantee/credit of the top parent company of the Chinese buyers.

Raise offshore funds

To the extent possible, Chinese buyers may seek the opportunity of using an existing offshore vehicle for the purposes of financing on an offshore basis. For example, Hong Kong listed Chinese buyers utilising their existing funds available outside China, or Chinese buyers issuing offshore bonds.

ANTITRUST DEAL SCRUTINY



WHAT'S CHANGING AND WHAT DO DEAL-MAKERS NEED TO KNOW?

Acquisitions of data-rich companies now raise full-blown competition issues, at least in Europe, which makes multi-jurisdictional transactions far more likely to be scrutinised or challenged when there is a significant data element.

- Antitrust is of critical interest to any CEO or leadership team that has ambitions to advance through M&A transactions. With antitrust and regulatory rules and cultures radically diverging in the EU and the US, a significant increase in time, care, sophistication and attention is needed to get deals done.
- The European Commission has toughened its stance, adopting robust positions on procedural infringements relating to data, market concentration and innovation. Antitrust authorities in Asia are showing signs of following suit, while the intervention by US agencies appears to be softening under the current administration.
- In the high stakes contest of a full-blown antitrust review, what is it that will assist your deal go through? Planning, preparation and focus are of course essential, but navigating the following is increasingly important:
  - **Shift in emphasis to deals that increase concentration levels**, rather than only those that achieve or enhance dominance, meaning the authorities look at the market not the deal. A combination of the smallest two players in a narrow market could trigger a concern, even if this does not create a market leader.
  - **Focus on procedural infringements**, which can involve significant fines. Facebook was fined €110 million by the European Commission (EC) for 'misleading' the EC during its WhatsApp acquisition and Altice was fined €80 million by the French Competition Authority for getting involved in the target's business decisions prior to closing.
  - **Innovation** – authorities are focusing on R&D in the broader market and not only in specific markets where overlaps exist between the merging parties. This has led to more sweeping remedies in cases like Dow/DuPont than might otherwise have been imposed.
- Deal teams also need to evaluate non-antitrust concerns (including consumer protection concerns) as these are weaving their way into the merger control analysis, especially in the US.

"Globally, we are seeing increasing proliferation of inconsistent merger control procedures and greater scrutiny of foreign takeovers on non-competition grounds. Navigating these complexities requires careful planning, understanding of local sensitivities and early identification of remedies."

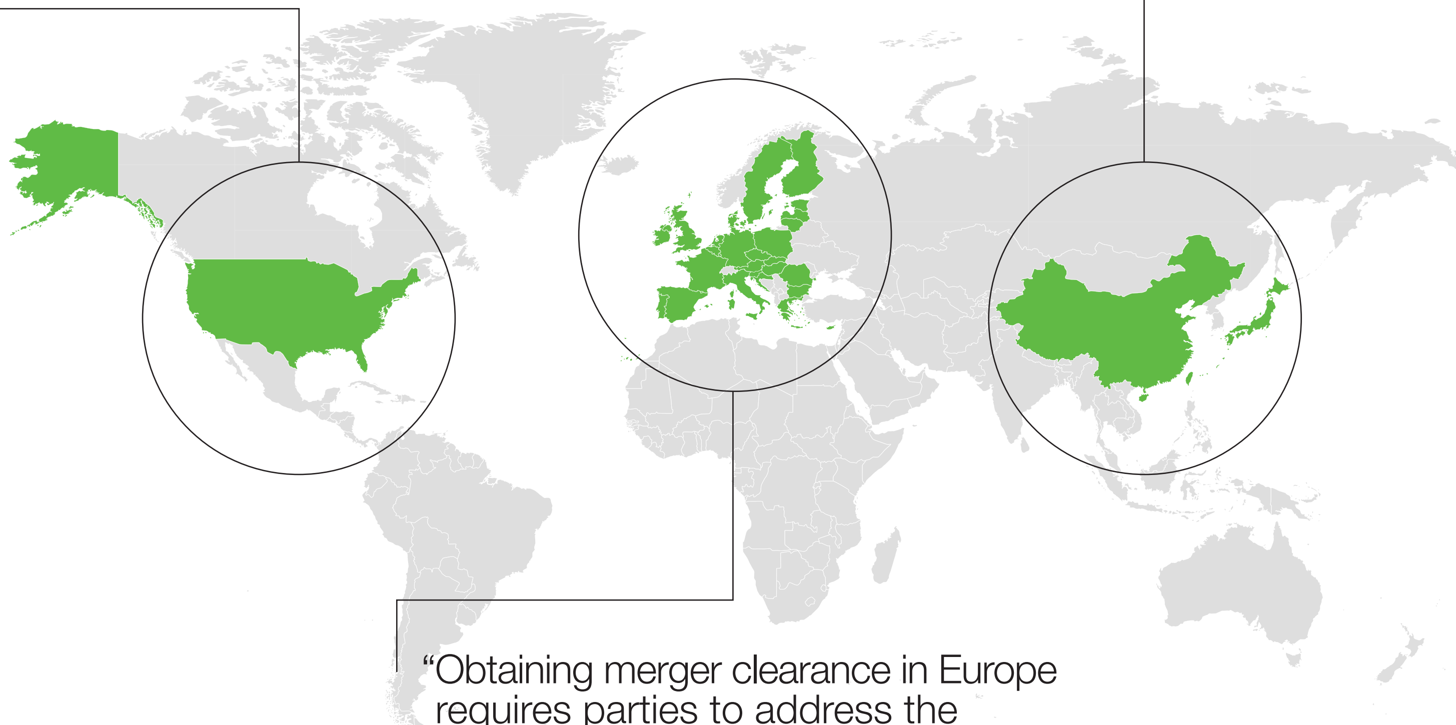
Nelson Jung,
Antitrust Partner, London
(former Director of Mergers at the UK CMA)

"US merger control enforcement is unlikely to change dramatically, although non-antitrust factors may influence key decision makers – many of whom have yet to be appointed."

Timothy Cornell,
Head of US Antitrust Practice, Washington

"Increasing cooperation between APAC authorities and their EU and US counterparts has seen concerns over innovation surface in China and Japan in particular"

Richard Blewett,
Head of China Antitrust Practice, Beijing



"Obtaining merger clearance in Europe requires parties to address the authorities' toughened substantive criteria as well as significantly heightened procedural demands."

Thomas Vinje,
Head of Global Antitrust Practice, Brussels

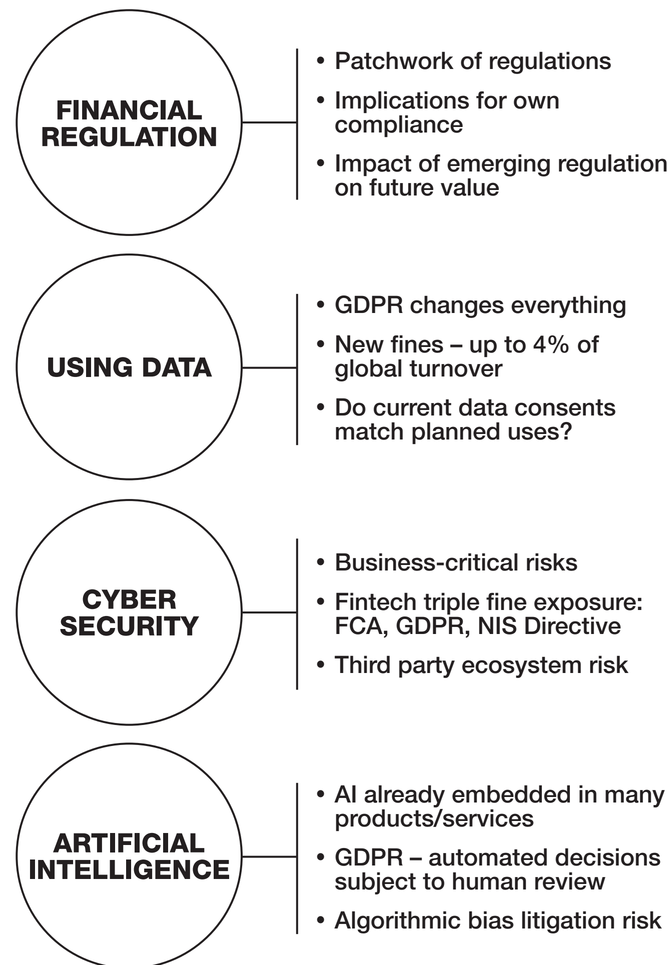
STRATEGIC OPPORTUNITIES THROUGH MINORITY STAKES

Businesses are focussing on strategic opportunities, particularly around digital/innovation, through minority investments in start-ups. These strategic stakes are seen as key to secure access to new technologies without over-burdening the balance sheet or creating a cluster risk.

FINTECH M&A FOCUS

Strategic minority investments in fintech businesses are on the rise. We are increasingly seeing corporates, banks and other financial institutions investing in strategically critical and innovative technology to increase efficiency, reduce cost or improve access to and delivery of financial services.

Fintech investments require a particularly careful balance to be struck between agility of commercial decision making, entrepreneurial spirit and regulatory and internal compliance. We have identified 4 areas of focus for businesses undertaking these deals: **Emerging Financial Regulation**; **Using Data**; **Cyber Security**; and **Artificial Intelligence**.



"The era of sucking up lakes of data for profit without thought or care for the individual is coming to an end. Those who are ready for the next data age will be richly rewarded.

The upcoming changes in law when the GDPR comes into force in May 2018 will put the individual back in control of their data universe.

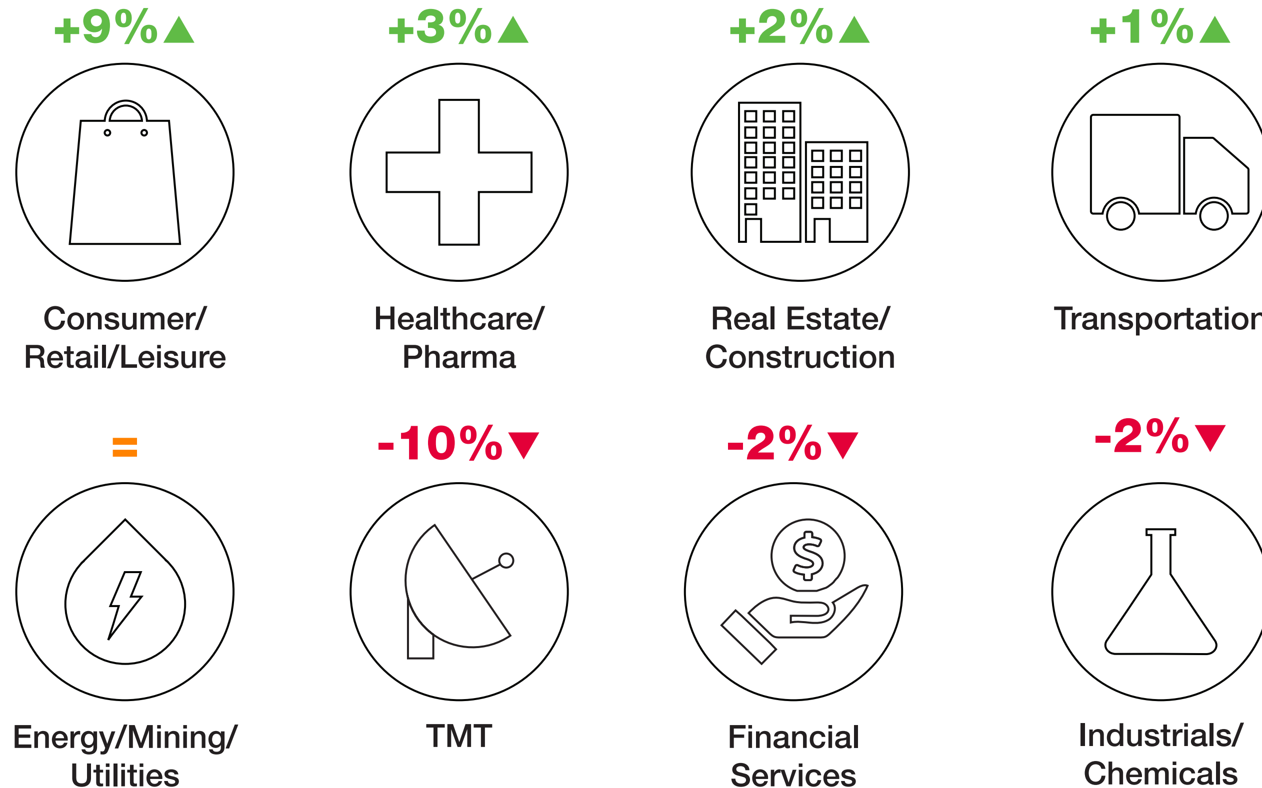
These changes will also create opportunities for businesses able to remodel themselves around the new requirements (and around customers) in response to this shift. Financial institutions already control huge databases of customer data. The burden of ensuring compliance will grow, but those financial institutions that can navigate the privacy rules while fully putting their data to work will leave their less adaptable competitors behind."

Jonathan Kewley,
Tech Partner, London

GLOBAL M&A DATA SET

The Consumer/Retail/Leisure sector is seeing a surge in M&A activity, with the announcement of several big ticket deals leading to a 9% rise in its share of M&A activity as compared to a slow 2016. Real Estate/Construction and Healthcare/Pharma are also seeing comparatively strong activity.

M&A TRENDS THROUGH THE SECTOR LENS
CHANGE IN MARKET SHARE IN H1 2017 COMPARED TO FY 2016:



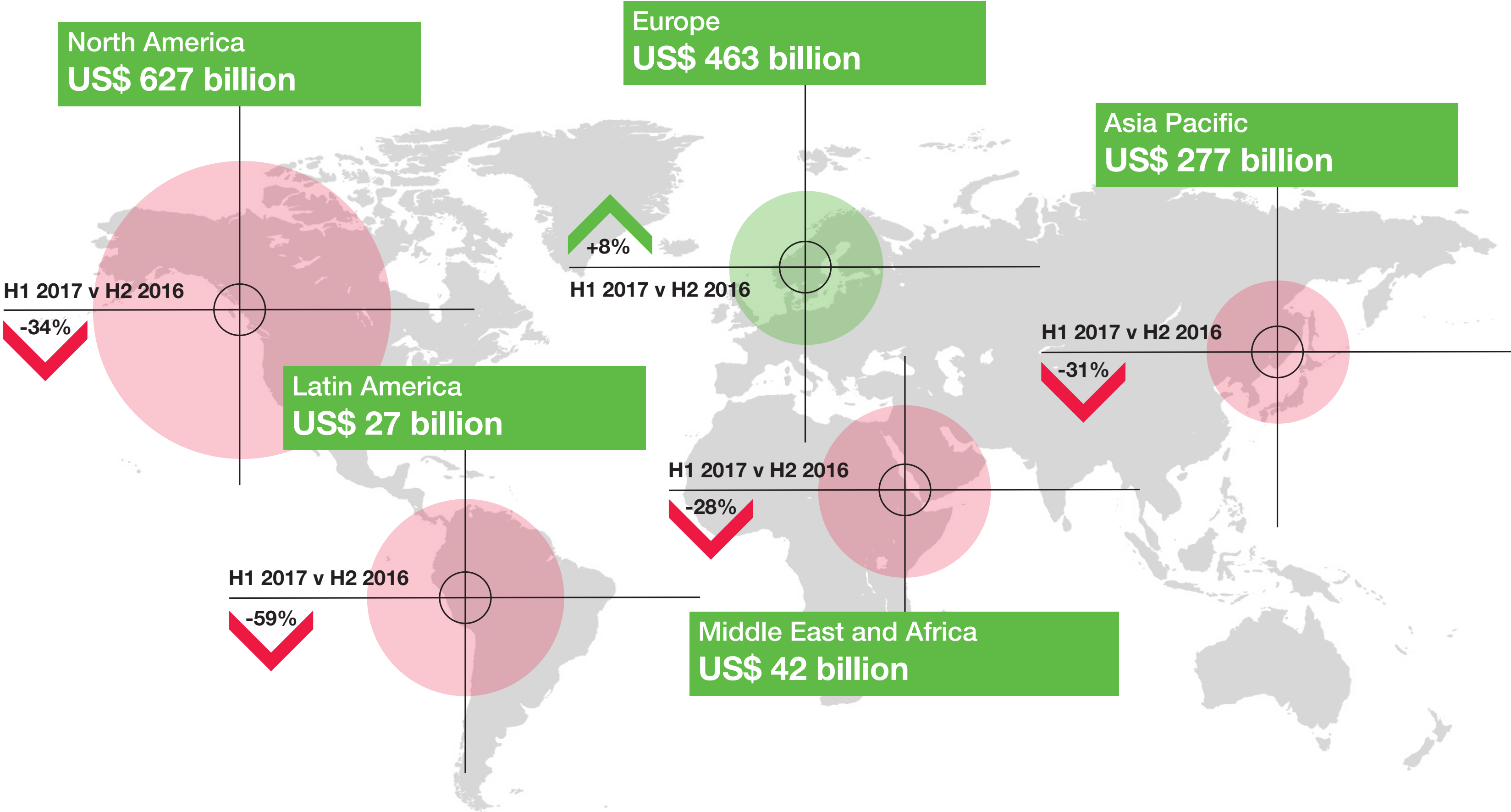
Source: Mergermarket. This publication includes data produced by Mergermarket, for the period 1 January to 26 June 2017.

"The surge in megadeals in the Consumer sector is a consequence of sluggish growth, which is driving companies, particularly in the US, to consolidate both nationally and internationally, so as to maintain or increase market share and drive cost savings in a tough low-margin environment. Consolidation will continue to be one of the primary features of the market for the remainder of the year."

Dessislava Savova,
Consumer Goods
& Retail Partner, Paris

GLOBAL M&A DATA SET

M&A TRENDS ACROSS THE GLOBE - SHOWING THE VALUE OF M&A IN H1 2017 COMPARED WITH THE PREVIOUS HALF YEAR PERIOD



Source: Mergermarket

Note: Interactive maps showing investment flows into and out of each region are available on the Clifford Chance Global M&A Toolkit

US

- US M&A in the first half of the year is more or less flat from H1 2016, however compared to H2 2016 deal value is down significantly. The size of mega deals involving US targets has decreased, with only one deal over $25 billion (BAT/Reynolds American at $61 billion).
- Inbound US M&A is buoyed by several large inbound deals from Europe (including, perhaps surprisingly in view of the fall in the £, two UK bids - BAT/Reynolds American and Reckitt Benckiser/Mead Johnson). This helps counter the decrease in Chinese bidders. Outbound US M&A remains strong (+10%), particularly into Europe - deals include Praxair/Linde and Johnson & Johnson/Actelion Pharmaceuticals.

LATIN AMERICA

- Economic slowdown and the economic and political turbulence currently facing the region (particularly Brazil, Chile and Peru) is reflected in the sharp slowdown of M&A activity in the region. However, M&A activity is expected to increase during the remainder of the year. Mexico and Argentina energy auctions are attracting a lot interest from investors from all over the world. In Colombia, we expect to see more privatization of state assets as well as increased activity in the infrastructure sector.
- Inbound investment in particular is down (-71%), although notable inbound acquisitions include Aerostar Airport in Puerto Rico, Brasil Kirin in Brazil and Barrick Gold's Veladero mine in Argentina. The most targeted region for outbound M&A was North America.

EUROPE

- M&A remains robust (+8%), benefiting from investment from the US and intra-European investment (including Atlantia/Abertis and Essilor/Luxottica). We are seeing a sharp decline in investment from Asia Pacific into Europe (-52%).
- Germany continues to out-perform, with strong domestic activity and notable inbound activity from the US (Praxair/Linde) and prioritisation by Asia Pacific bidders. Brexit and political uncertainty is resulting in a decrease in UK M&A (-32%) and foreign acquisitions of UK targets (-49%) although UK domestic M&A remains strong.

AFRICA

- M&A activity in Africa is weaker both for domestic (-17%) and inbound (-50%) activity, mainly due to the impact of the weakening macro-economic environment on valuation and pricing. Continuing weakness in key markets – Nigeria (oil price, currency devaluation), Egypt (currency devaluation), Kenya (run up to elections), and South Africa (political and fiscal uncertainty) affected the continent as a whole. However, this has underlined the current strategy of investors looking to build pan-African businesses to drive growth and diversify revenue streams.
- Policy decisions enacted during the period (e.g. in relation to currency in Egypt and Nigeria) have stabilised the situation to a degree, and this is expected to feed through to M&A activity in the second half of the year. Key consumer-driven sectors (power, education, pharma, FMCG, logistics, industrials, agribusiness) remain the focus for foreign investors, particularly where dollar-based revenue streams can be accessed.

ASIA PACIFIC

- M&A activity in Asia Pacific is seeing a marked drop-off in activity (-31%), with intra-regional activity surprisingly down 29%, and European and US derived investment down 84% and 37% respectively. There has been an uplift in investment from the Middle East into the region. Foreign inbound investment into China, however, remains strong (+14%).
- As predicted at the start of the year, the uncertainty around China's restrictions on capital outflows has led to a sharp decline in Chinese outbound activity (-42% as compared to H2 2016), with a large drop off in investment into the US (-79%).

MIDDLE EAST

- The Middle East has seen strong activity in the year to date, with rising inbound investment from North America in particular (Tronox/National Titanium Dioxide Company; Amazon/Souq). We continue to see government-driven consolidation, especially in Abu Dhabi (commercial banks and investment firms).
- There is good momentum in diversification efforts through selective outbound investments, especially in the US with increasing use of co-investment structures. The implications of the diplomatic rift with Qatar (which could last for some time) remain to be seen, but some downturn in investments in and out of Qatar is expected. The Saudi M&A market has been fairly buoyant as Vision 2030 has generated a number of infrastructure investment-related opportunities for investors.

C L I F F O R D

C H A N C E

Editors for this publication:

CHRISTOPHER SULLIVAN
T: +44 20 7006 5050
E: christopher.sullivan@cliffordchance.com

ISABELLE HESSELL TILTMAN
T: +44 20 7006 1681
E: isabelle.hessell-tiltman@cliffordchance.com

JOHN COLEMAN
T: +44 20 7006 2861
E: john.coleman@cliffordchance.com

ERIKA BUCCI
T: +1 212878 8142
E: erika.bucci@cliffordchance.com

EDWARD FREEMAN
T: +44 20 7006 2277
E: edward.freeman@cliffordchance.com

STEFAN BRUDER
T: +49 697199 1771
E: stefan.bruder@cliffordchance.com

ROBYN JONES
T: +44 20 7006 8323
E: robyn.jones@cliffordchance.com

Clifford Chance Global M&A Toolkit
The Clifford Chance Global M&A Toolkit comprises a growing collection of web-based transaction tools, video content and in-depth analysis of the most important market and regulatory developments in M&A regimes across the globe.
Available 24/7. Easy to access. – **www.cliffordchance.com/GlobalM&AToolkit**

© Clifford Chance, 2017
Clifford Chance LLP, 10 Upper Bank Street,
London, E14 5JJ.

www.cliffordchance.com
This publication does not necessarily deal with every important topic or cover every aspect of the topics with which it deals. It is not designed to provide legal or other advice.

Clifford Chance LLP is a limited liability partnership registered in England and Wales under number OC323571. Registered office: 10 Upper Bank Street, London, E14 5JJ.

We use the word ‘partner’ to refer to a member of Clifford Chance LLP, or an employee or consultant with equivalent standing and qualifications.