Our Insights into M&A Trends: Global Dynamics

December 2015

CLIFFORD CHANCE

M&A – The Global Picture

Record-breaking M&A market set to continue into 2016

- **2015 has been a bumper year for M&A** – Global M&A value has reached record levels, with over US$ 4.28trn of deals announced to date, lining up 2015 to be the best year ever for M&A. However these record levels have been driven by several mega-deals (including AB InBev/SABMiller, Pfizer/Allergan, Kraft/Heinz), which mask an underlying decline in deal volumes for the second half of the year.
- **TMT and Healthcare driving deals** – TMT has seen US$ 855.9bn of transactions in the year to date, with consolidation of mobile operators in Europe (Three/O2 and Three/Wind) as well as convergence (BT/EE). The need to increase revenues and reduce costs in order to fund additional investments in networks suggests there will be more transactions on the horizon. Healthcare is also outperforming, as acquisition-hungry US-led pharmaceutical companies with access to low cost debt, seek to increase scale and access new products.
- **US buyers leading the market** – North American buyers make up just over half of total global M&A activity (by deal value) for the year to date. Since the financial crisis, US boards had been inhibited from launching major or transformational transactions but now perceive inaction as riskier than pursuing opportunities while they are available. This, combined with favourable financing conditions and excess cash that cannot be repatriated without adverse tax consequences, is driving large and mega M&A by US companies, both within the US and overseas, particularly in Europe.
- **Inversions remain on the M&A agenda** – Mega-deal corporate inversions, particularly in healthcare (Pfizer/Allergan) and consumer goods (Burger King/Tim Hortons, Coca-Cola (bottlers)) remain part of the M&A landscape. These deals see US companies slash US corporate tax exposure by shifting the merged entity's domicile to the lower-tax jurisdiction. Legislative action limiting the tax benefits of these transactions appears unlikely given the election cycle. Whilst inversions remain controversial politically in the run up to a presidential election, and US Treasury and Revenue authorities continue to try to clamp down through new rules and guidance, Pfizer's proposed deal with Allergan shows that the perceived advantages of inversions remain powerful.
- **Significant regional M&A boom in Asia Pacific** – Despite continued international concerns over the slowdown in China, Asia Pacific M&A has increased 62% year-on-year. This 'mini boom' is being driven largely by a significant 65% increase in the value of intra-regional deals, with Chinese companies' continued pursuit of regional and global expansion and Japanese investment in the wider region (Japan Post/Toll Holdings, Mitsubishi/Olam) helping to drive activity. Another significant element of the intra-regional activity has been conglomerate restructurings (Cheung Kong/Hutchison, SK Holdings/SK C&C).

"We are seeing the pipeline of potential major M&A deals coming to fruition, many of which had been contemplated for some time. Now, as companies have built cash reserves and acquisition finance conditions are very favourable, we are seeing them come to market. However, the momentum is in the US, and European deal flow is, with a few very large exceptions, lagging behind. 2016 is expected to continue to see strong levels of high-value M&A globally, and continued strong intra-regional activity in Asia-Pacific. Increasing political tensions globally, the prospective US election and rate rises may however impact activity as the year develops."

Guy Norman
Global Head of Corporate, Clifford Chance LLP

Global activity levels

As we approach the end of 2015, we review Thomson Reuters' data for M&A activity (by value) in the first 11 months of the year.

2015 is set to be the best year for M&A deal values on record. Global M&A activity in the first 11 months increased 42% compared to the same period in 2014, with deal value totalling US$ 4.3trn (up from US$ 3.0trn).

M&A in North America increased 58% year-on-year, reaching US$2.2 trillion in 2015 to date. Asia Pacific also witnessed a significant increase (+62% year-on-year), with deal value totalling US$ 966.2bn. European M&A grew by a moderate 12% to US$ 839.7bn.

Cross-border M&A represents 34% of total M&A deal value for the year to date[1]. M&A flows between the five main regions represented 19% of total global M&A deal value. Asia Pacific M&A into Europe increased significantly year-on-year.

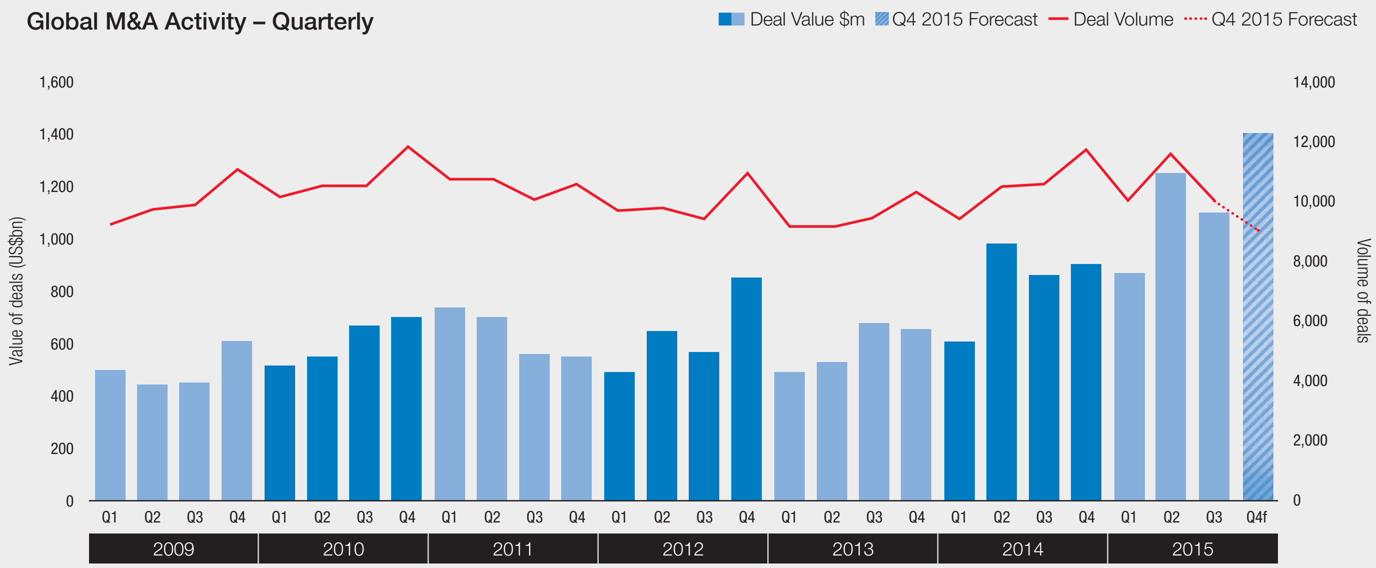
TMT (US$ 855.9bn) and Consumer/Retail (US$ 800.5bn) sectors have seen the most M&A activity (by deal value). Healthcare M&A is also a fast-growing sector (its share of total M&A +3% year-on-year). Energy, Mining and Utilities M&A saw only a small increase in absolute terms year-on-year (with Shell/BG being the major high point), as consolidation has not yet followed the pattern of the last period of depressed oil prices in the late 1990s. Infrastructure M&A remains an area of considerable activity across multiple sectors from TMT to Energy, Mining and Utilities.

The private equity market has been dominated by exits. Corporate buyers have led the type of acquirers buying from private equity as, emboldened with new-found confidence, boards seize strategic M&A opportunities. The trend for fund investors to partner with sponsors continues and will grow, with many funds on the road during 2016 raising fresh capital and using co-investment as an incentive for investors to commit to those new funds.

Source: Thomson Reuters

1 Note: Pfizer/Allergan is counted as a US domestic deal by Thomson Reuters.

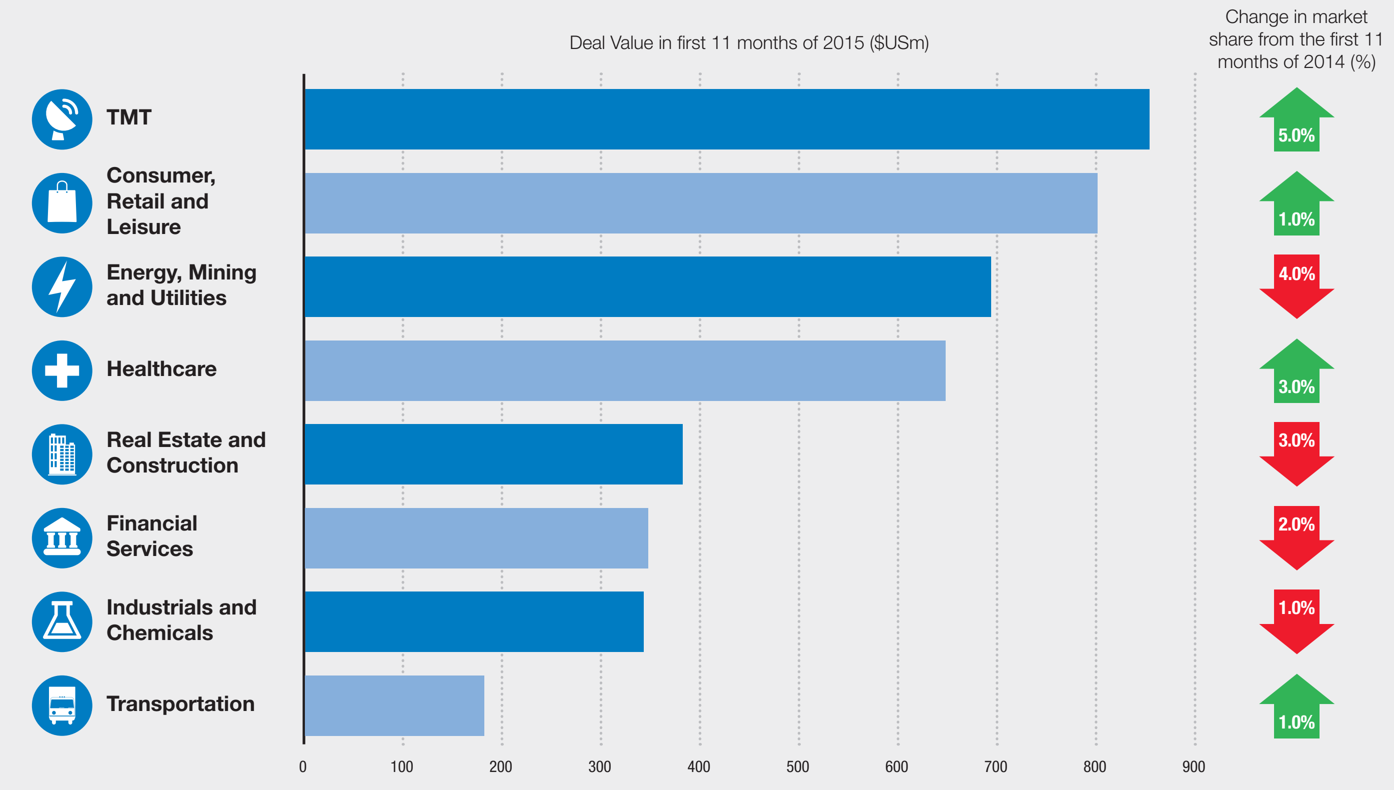
Global M&A Activity – Quarterly



Source: Thomson Reuters, except forecast Q4 2015

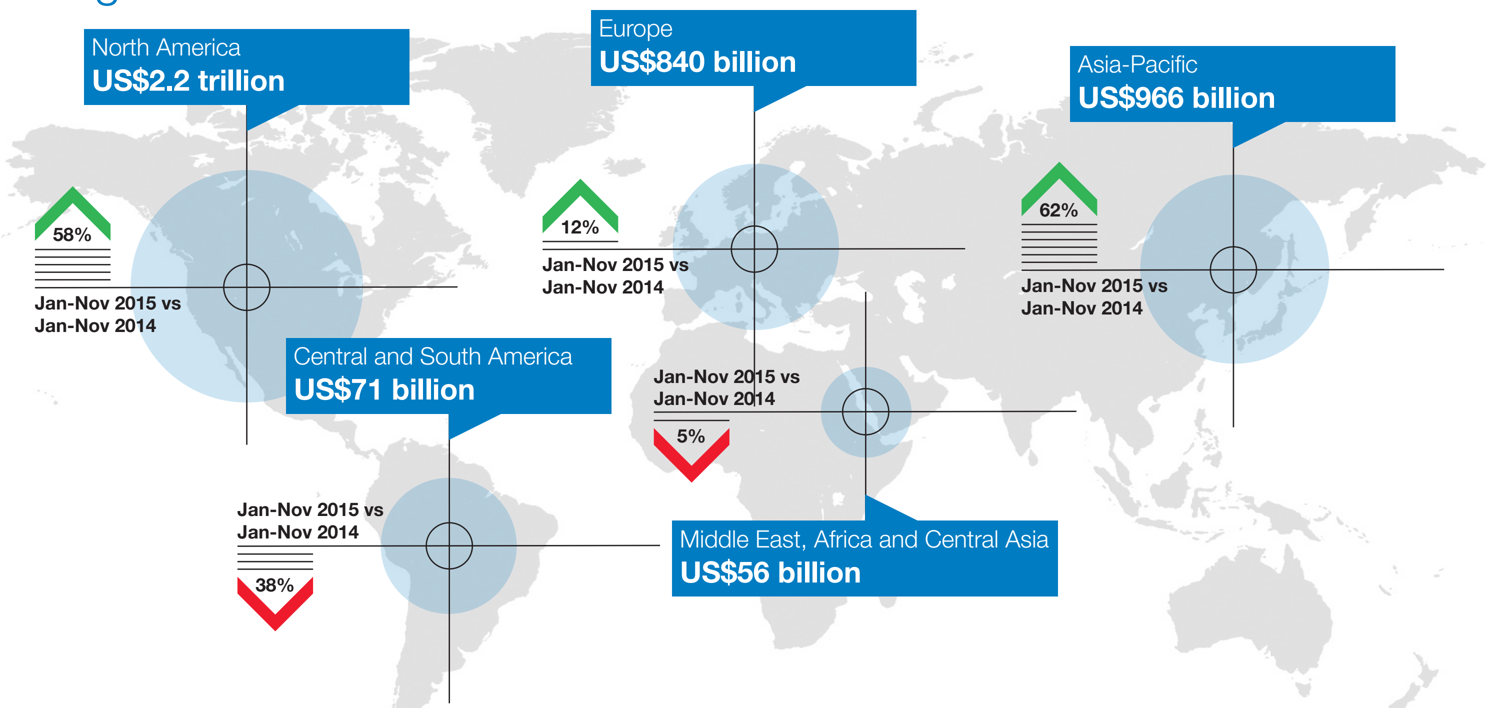
Sector variations

TMT and Healthcare are outperforming the rest of the market, with their share of total global M&A deal value rising 5% and 3% respectively in the year to date.



Source: Thomson Reuters

Regional trends



Source: Thomson Reuters

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

Views from our experts

Our experts share their views and insights on the latest trends in M&A.

M&A focus for 2016

2015 has been the strongest year for global M&A ever by deal value with large cross-border transformational M&A in the TMT, pharma, and consumer sectors in particular driving high deal values. The continuing presence, especially in the US, of companies with large cash piles, access to cheap debt and boards seeking to satisfy shareholder pressure for growth through acquisitions has maintained the positive M&A environment seen in 2014.

Despite concerns around the continued slow economic growth in many regions, particularly in Europe and Asia, ongoing geopolitical challenges (including political uncertainty in the lead up to the election in the US and the UK's possible EU exit), we expect that the key drivers of the momentum seen in 2015 are likely to remain in the short to medium term.

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Infrastructure and Energy

2015 has been characterised by fierce competition for infrastructure assets resulting in higher prices and corresponding pressure on returns. This is a result of favourable credit markets and the dramatic increase in the number of investors targeting the sector and the amount of capital allocated to infrastructure investment. Increased competition for 'core' infrastructure, such as water utilities, is encouraging infrastructure investors to look harder at 'non-core' or 'quasi' infrastructure, such as car parking, and at less mature markets.

We expect to see continued growth in 'platform' style investments, which provide investors with a steady flow of transactions on which to deploy capital, an increased focus on partnering with industry, and a greater willingness to take on construction/development risk.

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Trends in M&A financing

The market for M&A financing for large transactions has proven to be very strong in the last year and with debt facilities for individual transactions reaching record breaking levels in the recent past. The market for M&A financing for the mega-deals remains a market dominated by banks, both in respect of bridge transactions executed in the loan market and in relation to longer term take-out financings in the capital markets.

Looking ahead for 2016, recent levels of liquidity made available for M&A financings for mega-deals is clearly encouraging, but the availability of M&A financing and the successful execution of transactions in this category will also depend on the individual borrowers, their bank relationships and track record of executing highly complex transactions.

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Tax trends

Much recent transatlantic M&A has been driven by 'corporate inversions' – US headquartered groups merging into new non-US parents to reduce US tax exposure. A Treasury/IRS Notice published in November will make it harder to structure some inversions, and will limit the advantages for others. However we expect much of this activity will continue.

The other major tax development is the OECD's BEPS project, which has made a series of proposals to prevent 'base erosion and profit shifting' by multinational companies. It is still unclear which jurisdictions will implement BEPS, and how the details of implementation will work, but it is likely that many jurisdictions will restrict the tax deductibility of hybrid debt, shareholder debt and even external bank debt, potentially reducing the return on capital for equity investors.

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This publication includes data produced by Thomson Reuters, for the period 1 January 2015 to 26 November 2015.

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