ANALYSIS OF 2015 TAKEOVER DEFENCE TACTICS

25 February 2016 | Australia, Brisbane, Melbourne, Perth, Sydney
Legal Briefings – By **Rodd Levy** and **Kam Jamshidi**

In recent years, it has become clear that the majority of public company transactions in Australia (in value terms) are effected by a target company supported scheme of arrangement.

SUMMARY

- 37% of public company transactions announced in Australia in 2015 were hostile takeover bids.
- No bid which was not recommended at some stage by target directors was successful.
- Our empirical study shows that directors can create greater shareholder value by rejecting low bids and seeking rival bidders to allow an auction to develop.

In recent years, it has become clear that the majority of public company transactions in Australia (in value terms) are effected by a target company supported scheme of arrangement.

This is driven by the general desire for bidders to undertake due diligence and to be certain of target director support before launching publicly into an acquisition proposal.

However, hostile takeover bids are far from over. Their continued presence is a reminder of the need to prepare for defence situations by understanding the tools available to target boards. In this note, we examine hostile bids made in 2015 and see what can be learned from the tactics employed.

HOSTILE BIDS IN 2015

In 2015 there was a steady flow in Australia of hostile takeover bids, that is, bids which were announced without the support of target company directors.

We calculate that, out of the 59 public company transactions announced in Australia in 2015, there were 22 hostile takeover bids.

This represents 37% of all public company transactions (by number). This is roughly the same proportion that we have seen in the market over the last 5 years.

The aggregate market cap of target companies involved in hostile bids was in excess of $3 billion.

What lessons can be learned from how target directors responded in 2015?

1. Director recommendations are critical to bid success

No takeover bid which did not at some stage during the bid receive a board recommendation was successful.

The closest to being successful without a recommendation was Bentley Capital's bid for Strike Resources, but the bidder only reached 36% at the close of the bid.

All bids which directors recommended shareholders reject were unsuccessful.

This shows the importance of the directors' view about takeovers and the influence it has on shareholders.

When a hostile takeover was eventually recommended (usually after a price increase), it was successful in 7 out of 9 instances.

2. Directors were able to use their recommendations to negotiate increases in the bid price.

In 10 out of 22 instances, the initial bidder increased their offer price to win a recommendation. In addition, there were also 4 examples where the initial rejection was followed by another bidder emerging (discussed below).

This created a significant amount of extra value for shareholders.

In fact, we calculate that the extra value available to shareholders in these bids which came about from the directors using their recommendation to extract a higher price was in excess of $300 million.

3. Independent experts played a valuable role for target boards in hostile bids.

In 16 of the 22 hostile takeover bids analysed, an independent expert was engaged to opine on the terms of the takeover bid. This highlights the importance of independent valuation as a central defence pillar for target boards.

In 14 of these 16 reports, the experts concluded the offer was 'not fair nor reasonable' or 'not fair but reasonable', supporting the notion that target boards are generally skilled in identifying bids that undervalue their company. All but one of these received a reject recommendation from the directors.

In half of these examples (7 out of the 14), the bidder responded by increasing the offer by an average amount of 22%. That led to a positive recommendation in 5 out of 7 instances. A very good outcome for shareholders.

4. Where the board was able to attract a rival bidder, the resulting additional value for shareholders was very significant

The usual aim of a target board who thinks that there is a danger that control may pass at a price they consider may not be enough is to endeavour to attract a rival bidder prepared to pay a higher price. This is usually guaranteed to produce a superior result for shareholders. 2015 was no exception.

Rival bidders emerged in 4 of the 22 transactions that were initially rejected:

- G8 Education's scrip bid with an initial value of $0.70 per share for Affinity was topped by Anchorage's successful scheme proposal at $0.92 (a 31.4% increase),
- Westside's cash offer of $0.12 per share for Armour Energy was topped by American Energy Partners' offer of $0.25 (an increase of 108.3%),
- Zijin Mining's cash offer of $0.10 per share for Phoenix Gold was topped by Evolution Mining's cash and scrip bid valued at $0.158 (an increase of 58%), and
- Pulse Group's scrip bid valued at $0.88 for Vision Eye Institute was topped by Jangho Group's cash bid of $1.10 (a 25% increase).

The average improvement in consideration from the original offer to the final price was 54%.

CONCLUSIONS

Hostile takeover bids raise hard issues for target directors. Directors are required to give careful consideration to the terms of the bid, the value of their company and how best to respond so as to maximise the interests of shareholders. All of this must be done under time pressure and usually in the glare of public attention and additional scrutiny of the bidder.

The lessons from hostile bids announced in 2015 demonstrate that companies who are:

- selective with the use and timing of their recommendation,
- prepared and able to explain their operations to an expert or to shareholders, and
- pro-active in soliciting and facilitating rival bids,

will be best placed to generate significant value for their shareholders.

KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.

RODD LEVY
PARTNER,
MELBOURNE
+61 3 9288 1518
rodd.levy@hsf.com

LEGAL NOTICE
