

M&A NEWS: SOUTH AND SOUTHEAST ASIA

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Legal Briefings

As 2016 draws to a close, our team has compiled their top 10 predictions for the Southeast Asian Mergers and Acquisitions markets in the year ahead. We've included our thoughts on market and sector strengths, legislative impact, and the changing deal structures that we expect to see shape regional M&A in 2017. We hope you enjoy our predictions, and wish you all the best for the coming holiday season.

TOP 10 M&A TRENDS FOR 2017

1. Singapore will strengthen its reputation as a global asset management hub

With political uncertainty continuing in London and New York, we predict a rise in the number of Singapore-domiciled funds with tax treaties favouring Singapore, with fund managers and asset managers migrating to the city-state. Global private equity funds are already showing interest in regional IT plays, and infrastructure funds and pan-Asian funds have already established in Singapore. The funds management industry will be competing heavily for assets in the region.

2. All eyes on Chinese M&A flows

Intra-Asia M&A has been a strong trend in 2016. Chinese buyers have been important drivers and competitors for deals, including CGN's US\$2.3 billion acquisition of the energy assets of Edra Global Energy Berhad and Jiangsu Changjiang Electronics Technology Co., Ltd's US\$750 million voluntary takeover offer of SGX-listed STATS ChipPAC. Herbert Smith Freehills advised the bidders on both these transactions.

All eyes are now on the rumour that China is preparing for curbs in outbound deal-making. In early December, China acknowledged that regulators will bar significant

overseas investments while still leaving room for some strategic deals to be executed. China is likely to restrict overseas investments of over US\$1 billion which are outside companies' core businesses. The transactions we've seen in this region have been consistent with these rules so it does not follow that there will be reduced Chinese investment in Southeast Asia but it is an issue to be watched carefully in 2017.

3. India a bright spot for M&A in the region

A number of positive factors have come together for India. Relaxed FDI restrictions in certain areas, increased investor confidence in deal execution, and tax harmonization across the states are all good news for investment and potential investors. Brookfield got the ball rolling with recent billion-dollar investments in infrastructure, special situations and real estate. Expect more of the same - and more competition for India assets in 2017.

4. Asia number 1 for Fintech

In 2016, Asia became the number 1 region globally in terms of the amount invested into financial technology.¹

In Southeast Asia, the fintech industry has been growing fast, from payments and lending, to insurance, wealth management and cryptocurrency. As well as newer fintech companies, financial institutions are increasingly embracing the changes that are occurring in the industry as a result of advances in technology (including through investments into and partnerships with fintech companies).

A number of Southeast Asian countries have also committed government resources and announced 'regulatory sandboxes' or lighter touch prudential principles to allow development in this space. However, there are still challenges in bringing fintech to market, and as a result increased investment risk, particularly due to regulatory and compliance concerns.

There has been substantial seed capital as well as investment from strategic and financial buyers, in addition to M&A activity often as a way to increase scale, which we expect to continue into 2017.

5. Impact of tax amnesty in Indonesia

The Indonesian tax amnesty launched in July has not been the overwhelming success the Indonesian government had hoped for, bringing back just under one-third of fund repatriation commitments up to October 2016. At the M&A execution level, tax amnesty related issues have increasingly featured in deal structuring discussions, including a re-examination of the viability of aggressive tax structuring techniques seen in the past. We expect this trend to continue in 2017.

6. Renewed interest in Myanmar

Following the elections and the removal of US sanctions, we expect more M&A activity in Myanmar in 2017 (and now have counsel Guillaume Stafford seconded to Myanmar to assist clients on the ground). Activity this year was largely limited to the energy sector and tech deals, including Axiata Group's mobile tower company's US\$221 million controlling stake in Digicel Myanmar Tower Company Ltd, on which we advised.

7. Boosts for Islamic finance in Malaysia

Expect a renewed focus on Malaysia's burgeoning Islamic finance credentials, with the development ramping up on Kuala Lumpur's International Financial District and the legal market liberalization encouraging international law firms to bring Islamic finance capabilities and clients to the country. We have already seen increased interest in Islamic funds domiciled in both Labuan and Singapore, and expect further knock-on effects for the industry across the region.

8. Locked box structures on the increase

Locked boxed liability structures are becoming increasingly common in South and Southeast Asia, where parties are limiting their liability to leakage rather than using post-completion mechanisms to make adjustments to consideration.

When a locked box mechanism is used, the purchase price is determined pre-signing based on a balance sheet drawn up to an agreed date, meaning that the buyer takes economic risk in the target from this date. A buyer will require a number of protections in the share purchase agreement to prevent the seller being able to extract value (commonly referred to as "leakage") from the locked-box date to completion. A locked box arrangement generally favours the seller as there is no chance for the buyer to adjust the price post completion (other than through a warranty claim). We expect the trend towards using the locked box structure to continue.

9. Demand for warranty and indemnity insurance may raise deal pricing

Warranty and indemnity insurance has been prohibitively expensive in emerging markets, with most insurers and underwriters unwilling to take emerging market risk on an M&A transaction. However we have seen a shift in risk appetite recently and expect additional warranty and indemnity insurance opportunities in 2017 - but with a corresponding increase in deal pricing to cover the cost.

10. More regional harmonisation of governance standards

With perceptions that governance standards in Southeast Asia have some way to go to match established public markets, expect to see greater harmonisation between the

region's developed markets, particularly in disclosure standards and assessment of governance compliance. Expect a knock-on effect in the private markets too, with private shareholders agreements focusing more on related party issues and conflicts of interest at the outset, as these structures reach internationally accepted standards.

1. Data obtained from *Forbes* article dated 1 Nov 2016.

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