

# TOWNS UNDER SIEGE...HOSTILE TAKEOVER BIDS ONE YEAR ON

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Legal Briefings - By **Tony Damian** and **Clayton James**

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Our survey of hostile takeovers in Australia in 2016 reveals a number of interesting findings. One key takeaway is the continuing importance of obtaining a recommendation from the target board, with bidders in many cases recognising that need and paying for a recommendation in order to improve their chances of success.

## IN BRIEF

- The key themes emerging from our survey of hostile takeover bids in 2016 are broadly consistent with those identified in our six year survey of hostile takeover bids, covering 2010 - 2015, published in *Towns under Siege*.
- Hostile bidders tended, on average, to increase the price offered during a takeover bid in an attempt to secure a recommendation from the target board.
- Where the target board did change its recommendation, control of the target (or effective control of the target) passed in every case.
- In circumstances where the target board maintained a reject recommendation, the cumulative result of our surveys suggests that only a relatively small number of hostile takeovers were successful.

# THE BOARD'S ROLE IN RESPONDING TO A HOSTILE BID

A little under a year ago, Herbert Smith Freehills, in conjunction with the Ross Parsons Centre at the University of Sydney, published *Towns under Siege* – a new book looking at developments in the law and practice of Australian takeovers and schemes (further information on the book is provided below).

Chapter 7 of *Towns under Siege* examines the role of the target board in a takeover. The Chapter provides guidance on key issues which are likely to confront a target board, including whether to disclose the bidder's approach, the provision of due diligence access to a bidder and whether it may be in the target's interests to grant exclusivity. The Chapter also explores ways in which a target board can discharge its legal duties, while maximising value for shareholders.

## A “TYPICAL” HOSTILE TAKEOVER BID? RESULTS OF THE 2010 - 2015 HOSTILE DEAL SURVEY

In looking at hostile takeover bids – one obvious question is to what extent is there a “typical” hostile takeover and, if so, what are its features and characteristics.

To provide some insights on this question we undertook a survey of hostile takeovers announced between 1 January 2010 and 31 December 2015 with a final implied bid consideration of \$250 million or more (**2010 - 2015 Survey**). Broadly, the 2010 - 2015 Survey demonstrated the value of the target board's recommendation, with only around 20% of hostile takeovers succeeding where the target board made a reject recommendation during the entirety of the bid, compared to a 100% success rate where that original reject recommendation was changed during the course of the bid.

One year on, we compared the hostile deals of 2016 with those in our initial survey findings.

## THE 2016 HOSTILE DEAL SURVEY

### WHAT IS A HOSTILE DEAL?

For the purposes of our 2010 - 2015 Survey, a hostile takeover bid was defined to be a takeover bid where, in the Target's Statement, the target's directors recommended shareholders reject the bidder's offer. Additionally, we only counted a recommendation where it was unanimous<sup>1</sup> and where it only recommended rejection of the bid.<sup>2</sup> In other words, takeovers where the bidder was prepared to launch a takeover bid against a board who were prepared to reject it. We have adopted the same definition for the purposes of identifying hostile bids announced between 1 January 2016 and 31 December 2016 (**2016 Survey**).

### THE 2016 SURVEY

Our 2016 Survey identified only five hostile bids being announced in the period between 1 January 2016 to 31 December 2016.<sup>3</sup>

From our data sample of announced public M&A deals in 2016, it is interesting to note that takeovers comprised roughly half (around 52%) of announced public M&A deals, with hostile takeover bids accounting for around one in ten of all public M&A deals in 2016.

## CONTROL AND RECOMMENDATION

We have summarised below some of our survey findings on director recommendations and deal outcomes in the table below:

Issue	2016 Survey	2010 - 2015 Survey
Hostile takeovers that ended up being recommended to either the original hostile bidder or a subsequent recommended rival	40%	54.30%
Where the board changes its recommendation from reject, percentage of hostile deals where control passes	100% <sup>4</sup>	100%
Where the target board recommends reject at all times, percentage of hostile deals where control passes	20% <sup>5</sup>	21.10%

It is interesting to note the broad similarities between the findings for the 2016 Survey and the results of the 2010 - 2015 Survey. In particular, the results reinforce one of the broad themes from our initial survey: that director recommendations clearly matter in hostile bids. For example, in 2016 where boards maintained a reject recommendation throughout the bid period, the success rate was only 20% (which is broadly consistent with the success rate of 21.1% for the 2010 - 2015 Survey).

Conversely, where the target board changed from a reject to an accept recommendation, control (or effective control) passed in every case, consistent with our finding in the 2010 - 2015 Survey.

In the 2016 Survey, the target's board recommended the original hostile transactions (or a subsequent rival deal) in 40% of cases (as opposed to 54.30% for the 2010-2015 Survey). Related to this, we note the correlation observed in 2016 between a switch in recommendation from reject to accept and an increase in offer price.

## PRICING AND INDEPENDENT EXPERT REPORTS

Again, we observed broad similarities between the 2016 Survey results and the 2010 - 2015 Survey results in terms of the pricing of hostile bids and increases during the bid period.

Issue	2016 Survey	2010 - 2015 survey
Average starting premium to 3 month VWAP	39.75%	37.5%
Average final premium to 3 month VWAP	57.86%	53.0%
Percentage of hostile takeovers where there was a price bump	80.0%	68.6%
Average price bump for hostile takeovers	66.38%	12.9%
Median price bump for hostile takeovers	51.65%	9.5%
Percentage of hostile takeovers where an independent expert's report was commissioned	60.0%	68.6%

The average starting and final premia to 3 month VWAPs was broadly consistent across data samples. Interestingly, both sets of data indicate that hostile bidders are more likely than not to increase their offer price during the course of a hostile bid (in 80% of cases for the 2016 Survey and 68.6% of cases for the 2010 - 2015 Survey) - as noted above, price increases tended to be linked with, across both data sets, a change in recommendation by the target.

In terms of the quantum of price increases, we observed a large increase in the percentage price bump for hostile deals in 2016, with an average price bump of 66.38% and median of 51.65%. We note that these results were primarily driven by two hostile deals where the increase in the bid consideration during the period was substantial, at around 100% or more.

## CONCLUSION

Overall, despite the smaller sample size, the key themes and features of the 2010 - 2015 Survey were replicated in the 2016 Survey. Specifically that:

- hostile bidders tended, on average, to increase the price offered under a takeover bid in an attempt to secure a recommendation from the target board;
- in circumstances where the target board did change its recommendation, control (or effective control) of the target was likely to pass; and
- where the target board maintained a reject recommendation, the cumulative results of our survey, when taken across the seven years, indicate that only a small number of hostile takeovers bids were successful.

These findings reinforce the importance of obtaining a recommendation from the target board, with bidders in many cases willing to pay for it in order to improve their chances of success.

## **TOWNS UNDER SIEGE**

*Towns under Siege* contains contributions from the Takeovers Panel, ASIC and around 20 partners, consultants and lawyers from Herbert Smith Freehills. Topical issues covered in *Towns under Siege* include:

- the role of the target board in responding to a takeover bid;
- shareholder activism;
- class actions in takeovers;
- Australia's revised foreign investment regime; and
- takeover funding issues.

*Towns under Siege* was officially launched by Mr David Gonski AC at the Sydney offices of Herbert Smith Freehills on 19 May 2016.

Copies of *Towns under Siege* can be purchased from the University of Sydney [here](#).

## **ENDNOTES**

1. For example, a spilt recommendation, like that seen in UGL's response to CIMIC's bid, was not considered as a reject recommendation for the purposes of our survey.
2. So where directors gave, for example, an accept / reject recommendation based on individual shareholder's short term / long term investment horizons, this was not counted as a reject recommendation for the purposes of our survey.
3. Our 2010 - 2015 Survey comprised 35 hostile takeover bids from the period between 1 January 2010 to 31 December 2015. In order to compile a meaningful 2016 Survey data sample, we did not apply the \$250 million minimum implied bid consideration threshold to our 2016 Survey sample, which we applied when compiling the data for our 2010 - 2015 Survey. The 2016 Survey included all hostile takeovers, irrespective of the implied bid consideration.
4. Noting that in one deal, the bidder acquired effective control of the target ending the bid with a holding of 47% in the target. If this is taken into account, where the target board did change its recommendation, control (or effective control) of the target passed in every case.
5. For the bid falling into this category, the bidder acquired effective control of the target ending the bid with an interest of approximately 46% in the target.

## KEY CONTACTS

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



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