DEALMAKERS PREDICT WHATS IN STORE FOR AUSTRALIAN MERGERS AND ACQUISITIONS IN 2016

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News

Herbert Smith Freehills' mergers and acquisitions partners, Tony Damian and Rodd Levy have compiled a list of top 10 predictions for the Australian M&A market in the coming year. Their predictions, which suggest another positive year for deal activity, include:

1. CONTINUED STRONG ACTIVITY LEVELS

The factors at play during 2015 will continue to drive strong M&A activity in Australia in 2016. We predict deal number and values to continue at similar levels to 2015. Major drivers include the lower Australian dollar, some renewed confidence in the economy due to the change of Prime Minister to Malcolm Turnbull, a desire by some foreign investors (including many in China) to invest in a relatively stable economy which is perceived as having low political risk and the entry into various Free Trade Agreements and the Trans-Pacific Partnership.

2. FOREIGN CAPITAL MAKES ITS MARK

Another driver will be the pools of foreign capital that are now available to deploy in M&A situations. In recent times, there have been what could be described as new sources of capital from foreign players, beyond the usual private equity or sovereign wealth funds. Thus the emergence of the "ultra high wealth individual" in the Scepter approach to Santos is but one illustration of the significant pools of capital abroad that are looking for equity investments in stable jurisdictions such as Australia. The market has not yet felt the full force of those pools of capital, but we expect that more of this will be seen in 2016.

3. MORE BIG DEALS

Confidence is a key ingredient to boards signing off on transformational M&A deals. It often takes a few big deals to unlock further big deals. We think that the string of large M&A deals in 2015 will continue to drive confidence for the execution of significant deals in 2016.

4. EVEN FEWER HOSTILE BIDS

The number of hostile bids in Australia has declined significantly over the last 5 years as bidders have put a high value on having a recommended deal and the benefit of due diligence. We expect this trend will continue. That is not to say there won't be hostile bids - there will be - but their share of the mix will fall.

5. SECTORS TO WATCH

2015 saw activity across a range of sectors. Two sectors that we would call out for heightened activity in 2016 include resources and financial services, two of our perennial favourites over the years. In resources, we see a continuation of consolidation driven by cost concerns, as well as divestments driven by deleveraging concerns of major players, as driving M&A activity. In financial services, the relentless consideration by banks of the capital costs of certain of their operations is likely to see divestment activity, coupled with some of the smaller and foreign players being in a position to take advantage of those divestments.

6. MORE SCRUTINY FROM FIRB

An on-going theme over the last few years has been Australia's ever-tightening approach to foreign investment approval. While Australia has a very welcoming attitude to foreign investors, it is a sensitive political issue and the government has responded by proposing lower thresholds for some categories of investment and by seeking to impose tougher conditions on investment proposals. We expect this to continue.

7. THE RISE AND RISE OF SHAREHOLDER ACTIVISM

The past few years have seen a significant uptake in the level of shareholder activism in Australia. This ranged from board spills (such as the recent changes at Resource Generation), to trying to start or drive particular transactions or corporate activity, or preventing a particular corporate action (e.g. the Allan Gray/Roc Oil scenario). We expect to see more of this in 2016.

8. PRIVATISATIONS

The Queensland election at the start of 2015 saw an end to an ambitious privatisation program in that State. Nonetheless, there has been significant privatisation activity throughout the remainder of the year and the successes achieved, as well as the wide-ranging benefits from applying the funds from those privatisations, will see a number of quality assets offered for sale by various governments throughout 2016. We expect the universe of bidders on a number of these assets to be a large one, with the consequence that governments should again do well from these transactions next year.

9. FOCUS ON DEAL PROTECTION

As the market becomes more sophisticated with rival bids, we expect that bidders and targets will renew their focus on deal protection measures, such as break fees, no shop/no talk arrangements, notification rights and matching rights. We expect that the detail of these arrangements will vary more from deal to deal depending on the risk profile of each party. We do not expect a winding back of these arrangements (as has been seen in the UK).

10. FEWER TAKEOVERS PANEL APPLICATIONS

The number of applications to the Panel has drifted downwards over the last few years as the Panel's positions on various issues becomes settled and the Panel has been more prepared to dismiss applications that do not merit its attention. Absent a spate of applications driven by on-going contested bids, we see this trend continuing.

REVIEW OF 2015 PREDICTIONS

Mr Damian and Mr Levy have been making their annual predictions on the state of the M&A market for around a decade. Every 12 months they also reflect on the previous year's predictions, assessing which came true.

The partners did well with their predictions for 2015 and for the first time in a decade have declared that all of their predictions came to pass. The predictions for 2015 were:

- Increased M&A activity
- Sectors to watch (property, resources and financial services)
- Increased M&A activity from Chinese acquirers
- Developments in Chinese regulatory approvals (witness MOFCOM's continuing efforts to streamline processes)
- Target companies to focus more on bidder risk and uncertainties
- Current practice of not disclosing approaches to encourage more approaches to be made (e.g. Japan Post/Toll Holdings)
- Competition law to reform public interest to offset lessening of competition to proceed (note the Government's response to the Harper Review)
- Truth in takeovers rule to remain in full force (e.g. the clarificatory statements by Zijin and Woodside in respect of certain attributed statements in the press)
- Creative deal structures (e.g. the Iron Mountain/Recall solution as regards the cash/scrip consideration mix)
- Limited law reform (claiming this one may have been thrown into doubt by the legislative changes to the foreign investment regime, but let's not get too pedantic).

KEY CONTACTS

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

TONY DAMIAN
PARTNER, SYDNEY

+61 2 9225 5784
Tony.Damian@hsf.com

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

MEDIA CONTACT

For further information on this news article, please contact:

KELLY MURRAY, EXTERNAL COMMUNICATIONS LEAD

SYDNEY
Tel: +61 2 9322 4472
Mob: +61 429 115 625
Email: kelly.murray@hsf.com