Fourth Edition | Chapter 2

M&A STRATEGY IN THE GLOBAL MARKET

WHAT MAKES A DEAL?

BEST PRACTICES OF THE BEST DEALMAKERS

2015

Introduction by

David Fergusson | Editor

"When you are using other peoples money, when you are looking at your return on investments, when you are looking at the long-term prospect of a business, having a clear strategy which the board has bought into and stakeholders have bought into is absolutely key."

– Robin Johnson, Co-Chair of Cross-Border M&A Team, Eversheds LLP

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BEST PRACTICES OF THE BEST DEALMAKERS

Drawing on the experience and expertise of the "best in class" dealmakers, The M&A Advisor (http://www.maadvisor.com), together with the leading provider of virtual deal management services, Merrill DataSite® (http://www.datasite.com), publishes the quintessential dealmakers guide series – Best Practices of the Best Dealmakers. Profiling the proven strategies and unique experiences of the leading M&A practitioners, this series is distributed in regular installments for M&A industry professionals in both print and interactive electronic media. Previously published features and chapters are also available in the online libraries of Merrill DataSite and The M&A Advisor. We are pleased to present **M&A Strategy in the Global Market: What Makes a Deal?** This installment discusses the best practices for formulating a global M&A strategy to help ensure the continued vitality and valuation growth of a company competing across borders, as well as the appropriateness of an acquisition or a sale in terms of the synergies to be realized as the transactions end product. On the following pages, you'll find helpful observations provided by candid interviews with leading dealmakers, including buyers, sellers and advisors, as well as timely insights into the most current trends.

INTRODUCTION

Do a quick Google search for "scholarly articles on global M&A" and you'll instantly get about 7,700 results. A quick look at some of those near the top Google rankings will tell you that the growth of cross-border M&A deals has been accelerating over the past decade, notwithstanding the setback caused by the global financial crisis and recession of 2008. Others will note that about half of all global mergers and acquisitions fail to achieve their expected results. You will also find lots of scholarly discussion, analysis and theoretical propositions on the subject.

What you won't find a lot of is practical advice by the practitioners of the art of deal making. Without minimizing the value of scholarship, I would like to indulge in paraphrasing a famous quotation from Theodore Roosevelt: It is not the scholar who counts...the credit belongs to the person who is actually in the arena. In our series, *Best Practices of the Best Dealmakers*, now in its 4th edition, we bring together decades of wisdom and experience of dozens of the top investment bankers, advisors, lawyers, accountants and other M&A practitioners from around the globe to offer their observations on best practices in cross-border M&A. These esteemed professionals have actually been in the M&A arena through countless deals, gaining knowledge through setbacks and being rewarded through success, and helping investors worldwide maximize their returns.

This chapter focuses on the best M&A strategies used by buyers and sellers contemplating a deal in the global arena. We include views from practitioners with experience in virtually every geographic region – from Dechert LLP's Laura Brank, who spent many years advising on deals in Russia and the former Soviet republics, to Howard Lee, who heads the Seoul office of BDA Partners, a global advisory firm, to Thomas Bieri, who founded the Swiss arm of ACXIT Capital Partners in Zurich three years ago. We also have insightful contributions from veteran M&A lawyer Robin Johnson of Eversheds LLP in London, and Anthony (Tony) Dalwood, the Board CEO of Gresham House, a top London private equity and alternative investment house. From the US, we are indebted to Kenneth S. Frieze, CEO of Gordon Brothers Group, and Kendall Stafford, Managing Director at Benchmark International, for their keen observations on strategic considerations for buyers and sellers alike.

In coming chapters of *Best Practices of the Best Dealmakers*, we will be adding new perspectives from more global dealmakers on various aspects of the art and process of bringing deals from the strategy state through negotiations, the LOI, the due diligence, the closing, and the honeymoon period after the close. As always we invite our readers to share their thoughts and observations on these topics with us for future editions.

David Fergusson
Editor
Best Practices of the Best Dealmakers

M&A Strategy in the Global Market: What Makes a Deal?

Part I: What is a Global M&A Strategy?

"Limiting outreach to a single country restricts the pool of buyers and increases the possibility of missed opportunity. The need for globalization is so high it often translates into a hefty premium for the seller." – Kendall Stafford, Managing Director, Benchmark International

Why do companies do deals? Is it to achieve synergies? Cut costs? Acquire a trophy brand? These are popular public perceptions, but as veterans of the M&A business know, they are popular misperceptions. In a seminal 2014 paper based on research and data from FT Remark and MergerMarket, the global law firm Baker & McKenzie identified the five significant motivating factors for M&A:

1. Acquisition of customers or distribution networks
2. Acquiring intellectual property
3. Adding skills and capabilities through the acquisition of human capital
4. Gaining access to natural resources
5. Building a company's strength through the purchase of industrial assets

And in a 2015 study with Oxford Economics, Baker & McKenzie projected that global M&A and IPO activity will continue to rise, peaking in 2017 in developed markets and 2018 in emerging markets. One projection in particular jumped out: "Cross-border M&A activity will outpace domestic activity this year as the share of cross-border deals rises to 38% in 2015, up from 36% in 2014. The pace of cross-border activity will slow in 2016 but rise back to a 38% share by the end of 2017."

As chronicled in Chapter 1 of this 4th edition of *Best Practices of the Best Dealmakers*, cross-border M&A has entered a steep growth curve and the strategies for virtually every non-local company in every part of the world today is taking on a global component. This is being enabled by a growing cadre of professional M&A advisors, lawyers, accountants, investment bankers and private equity investors who have gained deep experience in overcoming the hurdles of cross-border deals over the past quarter century.

One of them is Robin Johnson, who heads the global M&A practice for Eversheds, a London-based law firm. “These days virtually all I work on are [cross-border deals],” he says. “Right now, I’m working on deals in Egypt, Morocco, Germany, Sweden and Norway. I work with my French colleagues on a daily basis. My typical invoice will be for work in four or five jurisdictions.”

Johnson emphasizes that every company must have an M&A strategy for both buying and selling: “When you are using other peoples money, when you are looking at your return on investments, when you are looking at the long-term prospect of a business, having a clear strategy which the board has bought into and stakeholders have bought into is absolutely key.” Equally important, Johnson says, is having a strategy that is understandable to the advisors of potential sellers or buyers – third parties – “to understand whether you’re the right person to either buy or sell from. If someone doesn’t know what your strategy is, you can miss out on opportunities. So making sure advisors understand your strategy makes a company more likely to get interest.”

One of the advisory companies with a keen interest in cross-border M&A strategies is Florida-based Benchmark International, which does more global deals than domestic in just about every sector. Managing Director Kendall Stafford stresses that a global M&A strategy should stress diversification. “Diversification reduces risk and thus the investors required rate of return. Sourcing revenue and materials from a variety of markets is perhaps the ultimate form of diversification,” she says. The traditional reasons that companies tended to avoid cross-border M&A – country risk, transportation costs, cultural differences, communication issues, and currency controls diminished over the past 25 years, as noted in Chapter 1. “The end of the Cold War, liberalization of tariffs and currency controls, cut-rate pricing on international communication and similar changes have decreased the risk of cross-border diversification,” Stafford says. “In addition, the invention of the Internet has blurred borders, sped the delivery of information, and transformed the way businesses do business. A global supply chain and international customer base were beneficial aspects of a company three decades ago, but now they are prerequisites for success in many industries.”

Stafford adds: “Any buy-side M&A strategy should have the purpose of finding underperforming assets, determining the delta between their current value (and ownership) and the value in the hands of the strategizing company. This is the primary purpose and value of the buyers M&A strategy. In addition,

the strategy must evaluate the buy or build options. More M&A is not always better M&A for buyers."

Kenneth S. Frieze is CEO of Gordon Brothers Group, a global advisory, restructuring and investment firm based in Boston with offices worldwide. They come at strategy from a slightly different perspective, helping growing, mature or distressed businesses manage through strategic change. "We get reasonably agnostic, theoretically, on global M&A strategy," Frieze says. "Different parts of the world have different processes, rules, laws, players… In the United Kingdom, the role of a lender much broader than in the US – there is no equitable subordination in the UK. So you have to understand the different rules of the road. The US and UK are the most liquid, objective, and transparent M&A markets. Germany, Spain and Italy are all different. Everybody involved in transacting in Japan gets together to have a consensus-driven outcome. In Japan, there is a cultural resistance to the concept of failure – which gets to bankruptcy. Japanese culture will push hard to make that look like a non-distressed sale. And they will do a lot to avoid closing down businesses and terminating people."

Thomas Bieri founded the Swiss arm of ACXIT Capital Partners in Zurich three years ago. ACXIT is a leading international corporate finance and investment advisory firm for mid-market clients and entrepreneurs in Europe and abroad. Bieri observes that strategies, particularly in mid-market cross-border deals originating in Europe, differ between publicly traded and privately held companies. "It makes a difference. There are tons of reasons for publicly listed companies to consider M&A – valuation multiples, crystallization of value. Public companies are mostly focused on shareholder value optimization," Bieri says. For privately held companies valuation is equally important, but he says this is because of these companies are generally smaller in size, more domestically focused and have less interaction with investment banks than publicly held companies. "They obviously know their competitors, but if they don't want to sell, they normally just play it by ear and don't look at opportunities. But how do you tap into opportunities if you see them?" he asks, and says that's why firms like ACXIT see a growing business in advising mid-market M&A candidates. "It's not that easy outside the US and UK to find advisors who have experience in this market segment."

London-based Gresham House is a specialist asset management group primarily focused on managing funds and co-investment as well as private

"Any Korean corporate looking to acquire or be acquired by a US or European company should have a confident strategy about customer integration, which is not easy because of language and cultural barriers." – Howard Lee, Managing Director, BDA Partners

equity. Anthony (Tony) Dalwood, an experienced investor and adviser to public and private equity businesses, is Chief Executive of the Board and Investment Committee. "The world's cross-border capital flows are substantial. Companies now don't typically operate in domestic or national silos," Dalwood says. "As a result of that, valuations tend to be globally driven rather than simply domestically focused. The transparency of information and data allows competitors to analyze what's going on in different markets and, if appropriate, to act accordingly. So you need to be aware of global themes, competitors, changes, and that was certainly less so 20 to 30 years ago."

From the investor standpoint, Dalwood also notes that 15 years ago, institutional investors – pension funds, trusts and endowments typically did not allocate to "Global Equity" but to UK, Europe, US or regional allocations. Today their exposure is increasingly global, he says. "[This] is relevant because if public markets are increasingly global, private equity is also increasingly global…The public and private markets are growing along parallel tracks, dealing in the same companies and realizing the same arbitrage opportunities, and yet they really don't directly communicate between each other as a basis of comparison."

BDA Partners is a global investment banking and advisory firm, based in New York with offices worldwide. Howard Lee was recently appointed to head the firms office in Seoul, South Korea. Before joining BDA, he led the M&A division at Samsung Securities, Koreas leading domestic investment banking firm. He was responsible for sourcing and executing domestic and cross-border M&A transactions for Korean corporations, private equity firms, and Government-related companies. From Lees perspective, companies in the Korean market keep a close eye on the frenetic cross-border M&A activity emanating from China and practically non-existent cross-border deal making coming from Japan. "Korea is in the middle," he says. "Any Korean corporate looking to acquire or be acquired by a US or European company should have a confident strategy about customer integration, which is not easy because of language and cultural barriers. [The US and Europe] are in a quite different

situation." Lee says Korean corporations are actively looking for international opportunities in M&A because domestic growth is only 2-3 percent, and the Korean population is "in shrinkage." He adds: "They have to go out to the International market, so they have to have strategies that understand global corporate communications and dealing with global corporate cultures. It's very critical."

Laura M. Brank lived and worked for many years in Moscow, and is now the head of the Russia and Former Soviet Union Practice for the global law firm Dechert LLP. She has represented multinational clients on cross-border M&A and joint venture transactions for more than two decades. She has particular expertise in advising on deals in emerging markets, especially in Russia, the former Soviet republics, and Eastern Europe. Brank says that in regard to a global M&A strategy it is "really important not to waste time, and its purpose is to know where you're going and have a roadmap to get there." Like Eversheds' Robin Johnson, Brank says that prior to the global financial crisis she often saw deal teams that didn't really know why they were buying or selling a company. "It's true that companies are being more selective and disciplined than pre-crisis," she says. "And they wait and hoard cash these days. So while companies have been more acquisitive in the past, they are more strategic today.

DEAL NOTES

Ten Tips for Attorneys Involved in Cross-Border M&A

Robin Johnson took over as head of the global M&A practice at Eversheds in London in 2006, just as the post-financial-crisis cycle was nearing a peak. "I took it over when the market was extremely hot. And in fact, I was pretty unhappy with some of the approaches that people were taking to deals – the lack of risk analysis, the use of money, the lack of contractual protection."

In November 2007, as the financial crisis was already taking shape, he wrote an article for London's Metropolitan Corporate Counsel, a monthly professional publication. Following are excerpts from his Top 10 Tips for lawyers involved in cross-border deals:

"Notwithstanding the fact that I act for a number of financial buyers as well as strategics, I thought the world had gone mad (in 2006-07), and the role of the M&A lawyer – both on the sell side and the buy side – seemed to be just limited

to doing the basic commoditized formalization of a stock transfer form or transfer of assets. While deal flow was very strong the actual role of the lawyer was becoming meaningless…

"I have had the benefit of a number of my clients and colleagues as well as providers giving me the benefit of their thoughts in relation to what I consider to be the top ten issues that need to be addressed on a European transaction when you are a US purchaser:

1. "Culture, Culture, Culture. Can you manage an acquisition from 4,000 miles away? Do not underestimate the difference in lifestyle approach, social protection and history. Job security is often key in Europe and the entrepreneurial spirit is not as live as it is in the States...

2. "While more typical US-style agreements are getting more recognized in Europe, you must understand the difference in transactional documentation approach. There is a lack of litigation post-deal. This doesn't mean due diligence was done better, it means that settling matters out of court and in a "handshake way" is more prevalent in Europe...

3. "Process and Timetable – scoping DD is vital. Europeans hate duplication of due diligence from different vendors. Agreeing and scoping upfront and spending some time with each provider is key. Having a central point of contact at the buyers who coordinates everything and avoids duplication is a vital role.

4. "In a structured way, and I emphasize the word structured, don't be afraid to due diligence to death to replace contractual comfort. Use due diligence as part of your integration plan, don't underestimate the value of vendor financial or legal due diligence, rely upon it, use it, update it, comment on it, use due diligence as part of integration.

5. "Anti-trust is a big issue in Europe. Build in enough time into the project plan to assess anti-trust. Each EU jurisdiction has different rules on anti-trust. Don't assume that you can just simply go to a one-stop shop in Brussels.

6. "Taxation – early structuring of deals to create a tax efficient basis should be looked at... A mixture of asset deals and stock deals should be looked at, but also, transaction costs associated with the deal, notary fess and stamp duty should not be underestimated. These often come as a surprise to a US purchaser.

7. "Most US buyers don't understand labor and social law protections that are in place. Europe has very wide social legislation. Most companies will have works counsels or unions. There is no one European law, again these, on the whole, need to be looked [at] on a country-by-country basis. Compliance programs in relation to labour law should not be underestimated

8. "If I had taken a dollar for every time that separation issues have been raised six months down the line as being a key integration cost that has been underestimated I would be a millionaire! Businesses that have to become stand alone leaving a group, licences, permits, consents, real estate, IT and pension costs, these are long term structural issues which should have been dealt with up front.

9. "Taking security on a leveraged deal is not as straightforward as it is in the [US]. There are rules against targets granting security, this is often called financial assistance. There are registration costs associated with taking security and other tax and there are antiquated processes about registering security, which often take time to put in place.

10. "Putting compliance processes in place post-deal need to be worked on straight away. Preventative and proactive legal care is going to be the only way in which you can properly manage an acquisition. Getting immediate buy-in as to your compliance ethos, i.e., from a cultural prospective (going back to Top Tip 1, of being culture, culture, culture is important) is key. There will be no European organization (that has not got a US arm) that will have compliance structures as good as you have."

Part II: Strategic Objectives in a Potential Global Deal

It is conventional wisdom in the M&A community that a significant number of deals ultimately fail to deliver the synergies that were anticipated at the beginning of the courtship. This is often due to flawed strategy and failures to identify clear objectives well before the negotiating and due diligence processes commence. M&A practitioners interviewed for this chapter agreed that buyers and sellers that tended to rush into deals without proper analysis of the myriad opportunities for synergies ran a higher risk of investor disappointment once the deal was done. Likewise, a strategy that builds in a realistic assessment of potential – but not necessarily totally achievable – synergies is more likely to meet investor expectations.

Benchmark International's Kendall Stafford identifies the following at key components for a successful global M&A strategy:

1. Local know-how and how it affects the buy/build decision
2. Competitive advantage/disadvantage
3. Country risk
4. Choice of law/arbitration/venue
5. Currency of choice
6. Local securities laws/governmental consents
7. Expectations concerning diligence
8. Expectations concerning involvement of legal team/length of documentation
9. Increased need to control higher deal costs
10. Cultural issues of post-closing integration

"The pace of change has been so rapid that the decision to buy or build heavily leans towards buy. Until technology slows or all medium to large businesses are truly global, this trend is unlikely to change," Stafford says. "For sellers, this means the best buyer can come from anywhere. Thus in today's market, limiting outreach to a single country restricts the pool of buyers and increases the possibility of missed opportunity. The need for globalization is so high [that] it often translates into a hefty premium for the seller."

Eversheds' Robin Johnson maintains that "a key part of an M&A strategy is not the deal itself but the inspiration for the deal." Companies that are serial buyers usually have an integration team that is a key component of the overall deal team, says Johnson: "They are already working on what's going to happen, what they're going to do, after the closing. If you don't do proper integration strategies you're not going to get synergies." Some obvious red flags that buyers should look for when assessing potential synergies include how dependent the company to be acquired is on its management and its customers. "If you can [incentivize] middle management going forward, that's a green light," Johnson adds. "They can see themselves as part of the organization long-term. It's always a good idea to bring in the benefits people at an early stage. The red flags are always the same – overconcentration on a small group of customers. A good data room is always a green flag – it says that a company has spent a lot of time putting its strategy together." On cross-border deals in particular, Johnson adds: "You've got to understand the culture of the company you're buying, you've got to understand the regulations in regards to the business

"You've got to understand the culture of the company you're buying, you've got to understand the regulations in regards to the business you're buying" – Robin Johnson, Co-Chair of Cross Border M&A Team, Eversheds LLP

you're buying. The more you're going into the emerging markets, the more you've got to understand whether you can actually take a majority stake."

Howard Lee, head of BDA Partners in South Korea, believes that the deals that achieve the best synergies historically result from companies watching and assessing each others capabilities for a number of years before actually discussing a combination. "Clearly then they know each other," Lee says. "They know synergies can be created or generated." In deals that fail to achieve the anticipated synergies, Lee says, "It's not necessarily because there was no synergy, but because of execution of the merger strategy post-closing. So if a buyer never knows much about the seller company, and all of a sudden they love the idea, and decide to team up and cut and deal, there could be a lot of problematic issues."

"I would always do deals based not on cost benefits, but on revenue synergies," says ACXIT's Thomas Bieri. "Cost synergies are mostly hugely overestimated, and in cross-border deals even more. It has a lot to do with the heterogeneous environment globally. Public companies are more tempted to pursue cost synergies that may not materialize. Private companies should not be tempted." In mid-market, cross-border M&A, Bieri says, "There are tons of market opportunities for revenue synergies out there, but you need to get access to distribution channels. Revenue synergies can be in multiples, but they're mostly driven by the domicile of the target company."

Tony Dalwood says that over two decades in M&A, he has seen many companies tending to be aggressive in building in revenue synergies to their M&A strategies. "You need to be wary of building in too many or any at all," Dalwood states. "As far as cost synergies go, you need to be very focused on detail or the implementation of those." Costs can go to one or one and a half times the expectations because of variables like union involvement, labor laws, regulatory constraints and other country-specific factors. "You need to really probe the spreadsheets," he adds.

Dechert's Laura Brank finds that sellers are generally more aggressive in promoting potential synergies with buyers. "The danger is that they're just not true," she says. "Buyers need to stick with that whole strategy – do you know why you're buying this company, and what are the synergies that are going to be important for you?" She says the red flags in cross-border deals are often cultural. A buyer may have the expectation of having more control than is realistic – "or that they'll want to run it the way you want to run it. Those are extremely important points in the beginning, and the red flag is if you start to argue already and cant see eye-to-eye in the beginning." Too often, Brank says, parties that have experienced early disagreements but continue to move forward will find themselves too vested in the deal-making process to avoid a bad outcome. "It's just like a snowball effect. And you don't want to kill a deal. But if you're seeing that cultural clash right up front, its often not going to get better unless you're taking over the company and getting rid of senior management that are obstructionist."

DEAL NOTES

Strategy and Synergy Bring Together Deals within the M&A Community

With all the aforementioned pitfalls of synergies failing to achieve expectations, it should be expected that the best practitioners of M&A would have a good strategic vision when it comes to their own businesses. Such was the case in April 2015 when Gordon Brothers Group, the global advisory, restructuring and investment firm headed by Kenneth Frieze, acquired AccuVal-LiquiTec, an industry leader in corporate valuation, advisory and disposition services, to form Gordon Brothers-AccuVal. The transaction marked the union of two of the longest-standing valuation firms in the industry, boasting a nearly 140-year combined heritage. The new company is the premier asset appraisal firm in the world, conducting over $60 billion of appraisals annually, serving 18 countries from 25 offices globally. The acquisition will broaden the range of available services offered by the new firm, providing access to related disposition services through the broader Gordon Brothers Group organization, as well as debt financing through Gordon Brothers Finance Company.

"AccuVal's appraisal expertise in the commercial and industrial sector is the perfect complement to Gordon Brothers long-standing dominance in the retail

"Typically, a private equity company wants to write the smallest possible equity check so they're going to try to get the maximum amount of financing."
– Kenneth Frieze, CEO, Gordon Brothers Group

and consumer industries," Frieze said in announcing the combination. "Joining forces provides our clients with deep, asset-specific valuation advice backed by our market-leading disposition guarantees and tranche B lending through Gordon Brothers Finance Company. We are very excited for what the future holds for Gordon Brothers-AccuVal." Rick Schmitt, co-founder of AccuVal-LiquiTec and now the president of the Gordon Brothers-AccuVal subsidiary, added: "Our combined capabilities are unmatched in terms of scale and expertise. With Gordon Brothers' $10 billion of annual dispositions backing us up, there is no equal."

Part III: PE Firms in the Global M&A Market – Strategic Considerations

In 2014, exits by private equity firms from buyouts exceeded $450 billion, surpassing the all-time high by a wide margin, according to Bain & Company's annual global private equity report. The dramatic increase in exits marked the fourth consecutive year distributions outpaced capital calls for the LP community. By the end of 2014, freshly committed dry powder hit a global record of $1.2 trillion, including $452 billion earmarked for buyouts alone, Bain said. However, the supply of companies to buy remained limited, and more PE money chasing the same assets has led to stubbornly high pricing. "If too much capital in the hands of a growing number of PE funds chasing too few good assets is a classic prescription for inflated acquisition prices, then the US is ground zero for asset-bidding wars," said the Bain report. "So thick are the ranks of prospective buyers that a PE firm's ability to quietly line up a proprietary deal has all but disappeared. Nearly every company that puts itself up for sale is the object of a hotly contested auction." The forces that are driving up valuations are structural and very difficult to change, Bain said. Other ongoing headwinds for PE cited by Bain were the ongoing structural problems in the Eurozone and the Asia Pacific regions slowing GDP growth.

With so much PE capital chasing a limited supply of acquisitions, how do buyers and sellers assess the pros and cons of involving private equity in deals?

Benchmark's Kendall Stafford says: "The key is to determine the strategy of the PE fund. PE funds typically buy low and sell high, but how does the particular firm achieve that goal? Do they do use debt? Inflate multiples? Grow revenues or enhance margins? Does that methodology match the objectives of a strategic buyer or for the seller that is rolling over a partial interest?"

Eversheds' Robin Johnson recommends that sellers always consider bringing private equity into the M&A process "to give competitive tension to a strategic buyer. If you can get a PE person interested, they can help the deal." On the other hand, Johnson says, private equity does not always offer the certainty that a seller can expect from strategic buyers. "A strategic will be less likely to be fishing than a PE player will," he says. Johnson also observes that private equity and strategic buyers had very different approaches to risk and due diligence prior to the last recession, but have since come into closer alignment. "Private equity [firms do not] tend to know the market as well as strategic buyers," adds Johnson. "Private equity may have a slightly more relaxed view on contractual documentation – that's my view."

Gordon Brothers' Kenneth Frieze notes that private equity firms can sometimes reduce uncertainties for sellers by producing appraisals and valuations early in the M&A process. "Certainly, there are private equity backed companies or companies in private equity portfolios looking to do rollups or what-have-you and the private equity will get very involved along with management to pursue that strategy. We've gotten involved in situations like that," Frieze says. "But there's also just a regular old PE firm saying 'I'm going to buy a company.' Typically, that private equity company wants to write the smallest possible equity check so they're going to try to get the maximum amount of financing. And so to do that they use staple-on appraisal and staple-on financing to reduce unknowns and get a valuation on the table for everyone to see."

"Private equity firms can also bring in resources that more parochial sellers lack," says Dechert's Laura Brank. "PE firms can bring in resources in terms of talent, sector knowledge, marketing strategies," she says. But at same time PE funds can be very active and "can be pretty tough" for sellers to deal with. "If you're someone used to running your own show," that can be difficult. " Its a trust issue. PE funds have a shorter horizon. They want to turn the company

“With the multitude of private equity houses, it gives the management team the ability to pick and choose the investor that suits their objective best.” – Tony Dalwood, Chief Executive of the House Board and Investment Committee, Gresham House

around and sell it. They have a very focused strategy – increasing revenues and profits. The seller may want the same thing but maybe in a different way.”

Adds Benchmark’s Stafford: “It is important to review the track record of the PE firm to ease a sellers fears that the company they have worked so long and hard to build will be destroyed. In addition, there tends to be a larger knowledge and trust gap between PE firms and less sophisticated sellers than what exists for the same seller and a trade buyer. The questions posed by a PE firm may often seem foolish to sellers leading to posturing that reflects, They don’t even know my industry. Why are we wasting time with them?” She adds: “The growth of fund-less sponsors in the marketplace has marred the landscape and complicated the decision to include private equity in a deal. Whoever invites a PE fund into the mix needs to be sure they fully understand that entity’s ability to finance the transaction and live up to their offers.”

“At the moment there’s a tremendous amount of private equity money – ‘dry powder’, they call it,” says Tony Dalwood of Gresham House “Its a very competitive private equity market at the moment, plus there’s a lot of debt availability, since debt financing has returned since the financial crisis. The debt-EBITDA multiples are averaging above five times – so why is that relevant? The seller obviously gets a very competitive market when he’s offloading or selling a business, so that’s very useful.” Dalwood adds that from the buyers point of view, private equity involvement can be positive because the management team can choose the teams from competing private equity houses. “They can get the best teams, the best chemistry, the best strategy, the fit that they want to achieve,” he says. Additionally, private equity firms differ on the length of holding periods for their portfolio companies, giving the sellers more choice. Some firms have sector specialties, rather than being a “generic private equity house.” Says Dalwood: “With the multitude of private equity houses, it gives the management team the ability to pick and choose the investor that suits their objective best.”

ACXIT's Thomas Bieri says the sell-side should always involve private equity in an M&A Strategy. "Private equity broadens the universe of potential buyers. They're always looking for interesting opportunities," he says. "They are a good testing mark for sellers. On the buy side, private equity firms hold assets that they want to dispose of. So once you know what you want, they can bring you access." As far as the negatives of involving private equity, Bieri says the buyer or seller needs to be aware of the PE firms' track record in areas such as value maximization and retention of management. "Involving them in your strategy doesn't mean that you buy or sell assets to them but you use them to get an optimal outcome," Bieri says. "On the buy side it's really not an issue; you buy from private equity, and you integrate, and it's your problem after that. If you are contemplating selling to private equity, you may think twice whether you want to get involved with a PE firm that might lever it up to the roof and get into trouble."

DEAL NOTES

Could the Private Equity Capital Overhang Reduce Investment Returns?

The following is excerpted from a paper written in 2010 for clients of SVG Advisors by Tony Dalwood. The themes regarding private equity remain constant five years later:

"While the potential remains strong for private equity, today's environment is different to previous recessionary periods – namely there are a larger number of players in the industry and there remains a lot of dry powder left to invest following the heady fundraising days and recent slowdown in deals. Skeptics have highlighted the impact this capital overhang could have on pricing, with some commentators suggesting it could take 15 years 'to clear'. Whilst this may have been a factor in recent private equity transactions, we believe that the impact of this overhang may not be as great as critics suggest.

"Reasons for this include the extent to which this capital will actually enter the market, as Limited Partners (LPs) become increasingly reluctant to continue backing poorer performing managers, or perhaps start refusing extensions to funds with unspent capital at the end of the investment period – possibly withdrawing commitments and re-allocating to managers who have generated strong returns from a robust investment process. Despite all of this, we believe

picking managers who are able to find pockets of value and take advantage of situations that the economic turbulence creates remains crucial to strong private equity returns.

"There are several characteristics of the private equity model which enable it to drive outperformance of public equities:

1. A long-term approach is adopted in order to create value (typically a four to five year investment horizon)
2. The ability to affect change through operational improvements
3. Alignment of shareholder and management interests through long term investment partners
4. Access to fuller information to conduct detailed due diligence (thus reduced risk)

"We are experiencing an unusual economic and asset market cycle. For equities, we may well be at a similar point in the equity cycle to the 1930s and 1970s where longer-term investors were rewarded with significant returns from that point. Equity returns can be further enhanced through investing in private equity, and while the capital overhang is perceived by some commentators as an issue, many factors in the current environment play into the hands of this asset class. It is this, coupled with private equity's model of value creation, that has been proven to enhance returns over public equities over the longer term and should see this asset class benefit. It is important that investors looking for exposure to private equity recognise manager selection is crucial to generating top quartile investment returns."

"Historically, a lot of these assets would have would have been left to just wither on the vine or been shut down."
– Robin Johnson, Co-Chair of Cross-Border M&A Team, Eversheds LLP

Part IV: M&A Strategies for Disposal of Non-Core Assets and Spin-Offs

In the aforementioned 2015 study of the global M&A markets by Baker & McKenzie and Oxford economics, the authors forecast that large manufacturing companies will continue shedding non-core operations, freeing up capital to acquire other high-quality manufacturers to expand their consumer bases." In addition, they expected the global banking sector to rebound, "driven by increased regulation and capital requirements that will force banks to sell off their non-core businesses." The disposal of non-core assets and spin-offs plays a significant role in the overall level of global M&A activity. Practitioners interviewed for this edition of *Best Practices of the Best Dealmakers* cited asset disposal as a key component of companies overall M&A strategies.

Playing an outsized role in the disposal segment of the M&A market is Gordon Brothers. "We go from healthy to distressed," says CEO Kenneth S. Frieze. Gordon Brothers Group has the ability to prefund disposition transactions to provide clients with additional liquidity in advance of asset disposal. The firm can deploy up to $250 million in capital for any one transaction, either as an outright purchase or a unique structured arrangement with participation on the part of the client. Gordon Brothers thus buys the non-core asset and takes it to market, freeing the company of the task of including the disposal in its overall M&A strategy. "We can take that off their hands in advance or even as a staple-on process – and therefore they can go to market with only the most attractive parts of their business," he says. "You can partner with Gordon Brothers and we will take ownership of those plants, divisions, assets and you don't have to come up with the capital, financing, wind-down. We are the perfect temporary partner." Frieze cited numerous examples of cross-border deals in which Gordon Brothers bought non-core assets from clients prior to the sale of the larger company. In one case, Gordon Brothers bought the entire accounts receivable of an athletic shoe company in order to allow the parent to sell the brand, unencumbered by outdated inventory.

"The red flags in cross-border deals are often cultural." – Laura M. Brank, Head of Russia and Former Soviet Union Practice, Dechert LLP

Eversheds' Robin Johnson says he has been seeing a lot of big multi-billion dollar cross-border deals recently in which the disposal of non-core assets played a key role. "Historically, a lot of these assets would have been left to just whither on the vine or been shut down," Johnson says. But in today's M&A market advisors and corporate understand that these assets can be disposed of aside from the main deal. Or, after an acquisition, if the combined company decides there are elements of the acquired company that it doesn't want to invest in, there are M&A specialist firms that can sell the assets in a third-party role. "We represented a large chemical company that bought a division as a whole from other chemical company," Johnson said. "They had to buy the division as a whole. But there were certain elements of that division that they didn't want. So they appointed a separate banking firm, different than the banking firm that they had used on the deal, specifically to sell non-core assets. They managed to reduce cost of their original investment significantly and they made a profit off of the sale of the non-core assets." Johnson says having an acquisition strategy that assesses what the firm does not want – as well as what it does want – is very topical and is generating more business in the mid-market M&A segment today than in the very recent past. Some – but not all – of the impetus is coming from activist investors. "We're obviously seeing a lot of spins at the moment. And there's a lot of opportunity for financial sponsors to take non-core assets in large chunks from businesses. I can see this only increasing," Johnson says.

BDA's Howard Lee observes that the same trend in the Asian markets. "A typical area that we see is a Korean company with a non-core asset in Korea, or in China, or in Vietnam," Lee says. "BDA gets the mandate to spin off the non-core assets. Or there might be a big corporate buyer from the US or UK that is expansionary and trying to acquire manufacturing facilities in Korea or China. They will typically want to divest non-core assets as well. These are key areas that our professionals are working right now."

Dechert's Laura Brank cited a mining and minerals company that she represented in acquiring another very large mining and metals company

DEAL NOTES

Inventory, Intellectual Property and Branding: A Fascinating M&A Case Study

The following is excerpted from a case study provided by Gordon Brothers Group of a complex, three-way, two-year transaction in which they played a significant role by purchasing and disposing of outdated athletic shoe inventory in order to facilitate a larger merger between global brands (the full case study can be downloaded here).

"American Sporting Goods, Inc. was the Aliso Viejo, California-based athletic footwear division of Brown Shoe, Inc., a $2.6 billion global footwear company. The independent operating entity designed and manufactured men's and women's running, walking, and cross training sneakers that were sold at major retailers throughout the US and Canada as well as through the company's direct, online channel. In late 2012, Galaxy Brand Holdings Inc., a brand development licensing company financed by The Carlyle Group, began discussions with Brown Shoe to purchase all of the assets of American Sporting Goods (ASG), including the Avia and Nevados Brands, via a 100% stock purchase. Galaxy and Carlyle executed a "no-shop" agreement while Brown Shoe cleared Hart Scott Rodino (HSR) requirements.

"Galaxy approached Gordon Brothers Group's Commercial & Industrial Division via its investment banker, initially as a potential buyer of the accounts receivable. Upon learning more about the transaction, Gordon Brothers Group realized that it could add significant operational and financial support in the disposition of assets included in the purchase that were not desirable to Galaxy.

"Gordon Brothers Group structured a solution in which it purchased outright at closing the assets not desired by Galaxy, which allowed Galaxy to focus all of its attention on growing the licensing and marketing of the Intellectual Property (IP). Through its partnership, Galaxy was able to acquire the (IP), design capability, and the marketing entity without assuming any responsibility for the supply chain orderly wind-down…

"Galaxy successfully licensed the IP and began to supply new product to the marketplace almost simultaneous with Gordon Brothers Groups completion of its wind down activities. All excess inventory was sold overseas and in certain discreet domestic channels so as to not dilute the brands launch by the new licensee at major retailers, including Wal-Mart Stores.

> "In August of 2014, Carlyle Group successfully exited the majority of its Galaxy Brands investment to Sequential Brands (NASDAQ:SQBG), one of the largest publicly traded brand licensing companies in the world. Avia and Nevados are now a vital part of its growing portfolio of brands."

several years ago. Recently, the combined company returned to her to help dispose of non-core assets. "It's extremely interesting to watch this process," Brank says. When the acquiring company made the initial acquisition they maintained that all of the assets they acquired were extremely important. But over time, management began to reassess its M&A strategy and came to the conclusion that there were indeed non-core assets that they could dispose before getting into further deals. "You realize what's essential for your business and where the growth areas are for your business," she says.

Tony Dalwood of Gresham House agrees that a key component of today's global M&A strategies is to get the businesses focused on core missions. "It can be either to get the core business focused and spin off peripheral assets, or to possibly find a hidden gem which somebody else could value very highly, but you don't, and you're going to focus on another part of the business."

Part V: Maximizing Synergies in Cross-Border Deals

"The ability to cross-sell products and services is increasingly on the rise. After years of nearly stagnant markets almost across the board, the opportunity to cross-sell seems to be a major component of buyers M&A strategies." – Kendall Stafford, Managing Director, Benchmark International

Notwithstanding the concerns expressed in Part II of this chapter regarding synergies of deals failing to achieve expectations, the best dealmakers interviewed by The M&A Advisor held a consensus view that goal of achieving meaningful synergies is the fuel that powers most of today's deals. The drivers of success in a synergy-motivated deal are 1) having a realistic strategy before entering a deal and 2) identifying, managing and executing on synergy opportunities once the deal is closed.

Stand-alone middle market companies offer potential buyers the following opportunities for synergy:

"For the seller, if you are unsure that you can attract the interest of a buyer to a process, then actually emphasizing synergies to buyers is a good tactic." – Robin Johnson, Co-Chair of Cross-Border M&A Team, Eversheds LLP

1. Access to new products, technologies, customer segments or geographic markets
2. Accelerated time to market
3. More management depth and experience

Kendall Stafford says her advisory colleagues at Benchmark International primarily see buyers looking for the opportunity to remove, or greatly reduce, customer and supplier concentration. "Expanding geographic reach is another major synergy we see routinely," Stafford says. "The ability to cross sell products is increasingly on the rise. After years of nearly stagnant markets almost across the board, the opportunity to cross-sell seems to be a major component of buyers M&A strategies. Reducing back office overhead is always an option but is rarely discussed until post-closing."

Sellers are often advised to promote potential synergies early in the sales cycle to whet buyer interest and improve valuation. Stafford says sellers typically are "more focused on the sellers personal objectives. While market timing is a consideration, personal life cycle issues are more relevant in most every case. The sell-side strategy must therefore balance price, terms, and personal objectives. As a result, sell-side strategies are more diverse and unique making for a rougher guide. The true purpose and value of a seller's strategy becomes clearer once the owner has made the decision to go to market."

Eversheds' Robin Johnson says: "For the seller, if you are unsure that you can attract the interest of a buyer to a process, then actually emphasizing synergies to buyers is a good tactic. If in fact you're pretty confident you know who's going to buy your business, it's less important for you to be promoting the synergies because the buyer should know anyway. But if you're in doubt and the business is not performing quite as you'd like, and there's a reason why you're selling, then actually emphasizing synergies is important because you get that interest." From a buyer's perspective, Johnson says, "It's not a

matter of knowing [what] the synergies are, it's a matter of knowing whether you're paying for them or not…[if] sellers are inflating their EBITDA bases on inflated synergies, or are adjusting their expected EBITDA based the synergies they think the merger will create – [it] could mean that the [buyer is] paying too much money. So the buyer needs to say, 'Hold on, let's look at what your numbers really are.'"

Adds Gresham House's Tony Dalwood: "As far as cost synergies go, one should be very focused on the detail of implementation and execution of those synergies, so instead of just assuming that costs of one plus one goes to just one-and-a-half costs, one really needs to understand the process of that and the risk of everything involved."

ACXIT's Thomas Bieri observes that the identification of synergies is particularly problematic for companies domiciled outside the US or the UK that are looking to expand abroad. "Accounting differences and cultural issues are almost always the same," he says. "The books you're looking out at can be unreliable because of off-balance sheet things. China can always bring huge surprises. So you need to be prudent about those things." Bieri stresses the theme of finding good advisors. "Today, there is no established mid-market, cross-border advisory business outside of the US or the U.K. But soon there will be. In fact, these services are growing faster outside the US and UK now. It's pretty much an open field."

Conclusion

Successful mergers and acquisitions begin with a well-formed strategy and today – as opposed to even 10-15 years ago – that includes a global M&A component. Strategic buyers and private equity firms are actively engaged in finding global deals that will expand customer bases, acquire intellectual property (including top consumer brands) and bring country-specific talent to their management ranks. The pace of cross-border M&A has now reached par with purely domestic M&A and is expected to continue as part of long-term globalization trends.

In the next chapters of *Best Practices of the Best Dealmakers,* 4th Edition, we will be sharing insights from top M&A practitioners on negotiations leading up to letters of intent, due diligence leading up to closings, and navigating the post-closing integration in today's cross-border deals. Readers are invited to share their views and experiences on these topics.

CONTRIBUTORS' BIOGRAPHIES

Thomas Bieri is a Managing Partner of ACXIT Capital Partners, and Founder and CEO of the Swiss entity of ACXIT. Mr. Bieri has over 18 years of corporate finance/IBD experience, 16 years of which with top tier Global Investment Banks, always with a strong focus on Switzerland. From 1997 – 2007, he was a member of the Investment Banking Department of UBS Investment Bank in Zurich. From 2007-2009, he was head of the Equity Capital Markets Switzerland division of UBS Investment Bank, responsible for all their equity and equity-linked transactions in the Swiss market. From 2010-2013, He was co-head of IBD Switzerland of Nomura (who had acquired the European and Asian activities of Lehman Brothers), building up very successfully the Swiss corporate finance franchise of the firm. At the beginning of 2014, he founded the Swiss arm of ACXIT Capital Partners in Zurich. Over the last 18 years, Mr. Bieri has advised clients on more than 100 M&A transactions and Capital Markets Transactions. He holds an MSc in Economics & Finance from the London School of Economics and a BSc in Economics and Business Administration from the University of Berne.

Laura M. Brank is the Head of Dechert LLP's Russia and Former Soviet Union Practice. She has been representing multinational clients on cross-border M&A and joint venture transactions for more than two decades. She has particular expertise in advising on deals in emerging markets, especially in Russia, the former Soviet republics, and Eastern Europe. Ms. Brank has been listed in major legal publications as a leading lawyer in Corporate/M&A and Banking/Finance and also listed in Legal Media's Guide to the World's Leading Women in Business Law. Along with just eight other lawyers, The Lawyer selected Ms. Brank for their Hot 100 survey (2010) in the corporate category. She was also recently recognized with the 2014 Leadership Award for her significant contributions to cross-border M&A at the 6th Annual M&A Advisor International M&A Awards. Ms. Brank serves on the Board of Directors of the US-Russia Business Council. She holds a JD and a MSFS from Georgetown University, and a BA in Eastern European Studies from the University of Maryland. She is fluent in Russian.

Anthony (Tony) Dalwood is Chief Executive of the Board and Investment Committee of Gresham House. He is an experienced investor and adviser to public and private equity businesses. Mr. Dalwood established SVG Investment Managers (a subsidiary of SVG Capital plc), acted as CEO and chairman of this entity, and launched Strategic Equity Capital plc. His previous appointments include CEO of SVG Advisers (formerly Schroder Ventures [London] Limited), membership of the UK Investment Committee of UBS Phillips & Drew Fund Management (PDFM), Chair of Downing Active Management Investment Committee and the Board of Schroders Private Equity Funds. He is currently chair of the investment committee of the London Pensions Fund Authority and a Director of Branton Capital limited.

Kenneth S. Frieze is Chief Executive Officer of Gordon Brothers Group, a global advisory, restructuring and investment firm that helps growing, mature or distressed businesses manage through strategic change. Mr. Frieze sets the strategic vision for the firm, and has over 20 years of leadership experience in restructuring, consulting, brand redevelopment, appraisal and asset disposition. For nearly 15 years he has served in executive positions at Gordon Brothers Group, including most recently as their president. Prior roles included leading the firms business development efforts as well as the brand and appraisal practices. Prior to joining Gordon Brothers Group, Mr. Frieze served as CEO of RetailExchange.com, a management consultant with Bain & Company and a turnaround consultant with The Recovery Group, now part of Deloitte CRG. Mr. Frieze currently serves on the Polaroid board, is a former board member of The Sharper Image and served on the board of the Turnaround Management Association for six years. He holds a BA from Lehigh University and an MBA from the Wharton School of the University of Pennsylvania.

Robin Johnson is Co-Chair of Eversheds Cross Border M&A Team and runs a team across 30 jurisdictions of over 100 lawyers. He is also Sector Chair of the Diversified Industrial Sector Group. Mergermarket has placed Mr. Johnson regularly in the top 10 of their Rainmaker leagues in the last 8 years. Legal Business recently voted him as one of the top ten M&A lawyers in the UK. From 2010-2011, Mr. Johnson had a secondment to Parker Hannifin to assist in a major European restructure, and in 2013 spent 4 months as Interim European and Asian GC for Archer Daniels Midland. In 2012, he spent 4 months researching and writing Eversheds' award-winning "M&A Blueprint: Inception to Integration" report. Mr. Johnson has authored many articles including being published in the Baird Monthly M&A Monitor, International Financial Law Review, The Journal of Private Equity and the Metropolitan Corporate Counsel and European Private Equity Journal. He is a member of the ABA International M&A Task Force, a member of the Canadian Chamber of Commerce, and is a non-executive director of the University of Leeds, one of the largest universities in England and Wales.

Howard Lee is a Managing Director at BDA Partners in Korea. He joined BDA in 2015 as head of the BDA Seoul office. Before joining BDA, he led the M&A division of Samsung Securities, Koreas leading domestic investment banking firm, for four years. He was responsible for sourcing and executing domestic and cross-border M&A transactions for Korean corporates, private equity firms, and government-related companies. His clients include several Samsung Group entities, Affinity, Carlyle, CVC, Goldman Sachs, Hyundai, Kolon, Korea Telecom, KTB, LG, Lotte, MBK, POSCO, SK, Standard Chartered and Visteon. Between 2004 and 2011, Mr. Lee worked as an Associate Director at Macquarie Securities M&A group in Seoul. He holds a BA, International Economics from Seoul National University. He is fluent in Korean and English.

Kendall Stafford is Managing Director of Benchmark International, and holds a Bachelor of Science in Business Administration with a concentration in Finance from East Carolina University, and a Master of Business Administration from Saint Leo University. Ms. Stafford is at Benchmark International's US headquarters in Tampa, Florida. She was raised in an entrepreneurial family, where she learned the important aspects of starting, running and selling a successful business. Ms. Stafford began her career at BB&T, a regional bank, where she held various positions in the wealth management and commercial loan departments. The wealth management position allowed her to work closely with clients to implement business succession planning as well as address an owners personal financial needs. During her role in the commercial loan department, Ms. Stafford underwrote new loans and analyzed risk factors for various client relationships. She was one of a few chosen to participate in the banks nationally recognized leadership program because of her demonstrated traits as a corporate leader. Ms. Stafford's appreciation for entrepreneurs, her ability to quickly analyze and grasp financial information, and the desire to continue her work in a transactional environment led to her joining Benchmark International in April 2012.

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