Corporate Financier

GROWTH | OPPORTUNITIES | EXPERTISE

ICAEW CORPORATE FINANCE FACULTY

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CRACKING CHINA

WITH GROWTH SLOWING, WHAT ARE THE M&A OPPORTUNITIES FOR THE PEOPLE'S REPUBLIC?

SWITCHED ON TO GROWTH: DELOITTE ON ITS MAMMOTH YEAR OF M&A DEALS
EXIT SIGNS: BREXIT'S KNOWN UNKNOWNS FOR PRIVATE EQUITY

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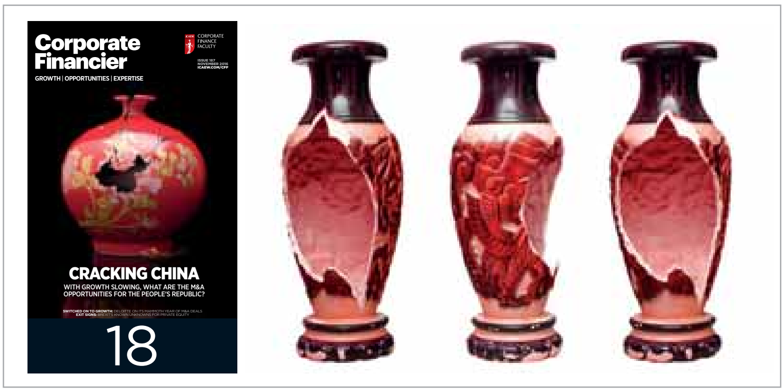

COVER: GETTY, DAN MURRELL

Work to rule

CORPORATE FINANCE FACULTY

The importance of controlling the means of production to shape an economy was extolled by Karl Marx in *Das Kapital* almost 150 years ago. And nearly a century before that, in *Wealth of Nations*, political economist Adam Smith

highlighted the importance of advances in production for developing an economy. Times may well have changed now – consumerism could be the primary driver of the global economy.

M&A trends have often been viewed as a precursor to wider business ones. Interestingly, industrials M&A has been the best-performing sector for 2016. During the first nine months, industrial acquisitions globally has been at its highest level since Thomson Reuters began measuring this back in the 1970s. So far, the sector has accounted for 11.9% of global M&A – its biggest share of the pie for more than 20 years.

Taking control of the means of production, it could be argued, may still be the name of the game. The most 'acquired' nation was the US, and the most 'acquisitive' was China. With growth slowing, Chinese businesses and government-backed funds are investing outside of the People's Republic.

In this issue's cover story (on page 18), David Prosser looks at the nature of capital flows involving China. There were three industrial M&A deals involving Chinese targets in the top 10 (by value) so far in 2016. The acquirers? In each case it was a Chinese buyer. Why are the transactions (almost) always a one-way street? Growth in China may have slowed, but it still outstrips that of industrials in Europe and the US.

In July, British prime minister Theresa May unveiled plans for an 'industrial strategy' for the UK. We still eagerly await details. The Corporate Finance Faculty together with the Institute of Engineering & Technology has published *Boosting Finance for Engineering & Technology* (see page 6). This policy discussion document sets out the key financing considerations for developing a modern investment strategy for UK engineering and advanced manufacturing.

The sector's intensive capital requirements and longer investment horizons mean there does need to be action if more investment is to be attracted from the private sector. If Great Britain Plc waits for Chinese investors to tell it that engineering and manufacturing have overtaken consumerism as the opiate for the masses, it could be too late.

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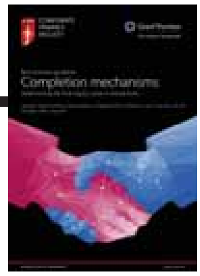


CRUCIAL FACULTY M&A GUIDE LAUNCHED AT GT

If there is one thing that is a crucial part of all M&A, it is that deals are completed. At the very heart of deal-doing are completion mechanisms, which include the detail of how the final purchase consideration is derived. Therefore a thorough understanding of completion mechanisms is both a core skill and a source of personal comparative advantage for all professionals involved in corporate finance, whether as advisers or as principals.

Last month, with Grant Thornton and the assistance of the faculty's Technical Committee, the Corporate Finance Faculty published its latest best-practice guideline, *Completion mechanisms: Determining the final equity value in transaction* (a copy of which is enclosed with this issue of *Corporate Financier*).

The new guide was launched at Grant Thornton's Finsbury Square offices in London at an event introduced by the firm's CEO, Sacha Romanovitch, who said: "This guide is about people with real insight coming together to produce a guideline that will help promote trust and integrity in M&A. It will demystify the principles behind how equity value adjustments are applied. It is about being in a position where there is an opportunity to give clarity to the completion process. Knowing what the contentious areas are to look at can provide real value to clients."

Co-authored by Grant Thornton's Patrick O'Brien, Nick Andrews, Philippa Hill and Eli Hillman (with the faculty's Katerina Joannou as technical editor), the guideline has two distinct sections.

> "This is about people with real insight coming together to produce a guideline that will help promote trust and integrity in M&A"
>
> **Sacha Romanovitch,** CEO, Grant Thornton

ALEXANDER CAMINADA

Top: Sacha Romanovitch, chief executive of Grant Thornton. Above: panellists Patrick O'Brien, Nick Andrews, Ian West and panel chairman David Petrie

The first looks at how to arrive at an equity value, covering the core principles of valuation, and what the likely contentious areas are. The second section covers the two widely accepted mechanisms –completion accounts and the 'locked box'. It also looks at latest developments in hybrids of the two.

"It is the first time the faculty has put out there what the contentious areas of the two mechanisms are, and how the buyer and seller might look to apply these differently," O'Brien told the audience of about 200 advisers, businesses and investors.

Presenting the guideline, Andrews pointed out that since the financial crash the use of the locked box had increased, so that it is now deployed in about half of all deals. He raised the question: "While locked box means certainty of price, does it always lead to certainty around what the buyer gets?"

There was a lively question and answer session, chaired by ICAEW's head of corporate finance, David Petrie. Insight and practical experience from the panel came from highly experienced deal-doers: Ian West, Capita Group Plc's acquisitions director and a faculty board member; Gary Narunsky, Grovepoint partner, and the guideline's co-authors Andrews and O'Brien.

West said that while the locked box was often viewed as "more vendor friendly", as an acquirer, he saw big advantages in that it minimised the distracting impact of the process on the management team of the business being acquired.

Narunsky said both techniques had pros and cons, but that the locked box does not always provide certainty over value, particularly when there is also scope for additional value adjustments. However, he added that for serial deal-doers it made a lot of sense, and in examining research about the use of mechanisms, PE-to-PE deals deployed locked box in around 90% of transactions.

On the important role of the faculty in professional standards, Romanovitch added: "The role of the Corporate Finance Faculty is so important. They are actively involved in shaping the system, rather than moaning about it. Initiatives like this show how they really have influence."

Petrie emphasised the importance that all corporate financiers ought to place on understanding these technical approaches: "Being completely *au fait* with completion mechanisms is a core skill. Get it wrong, and as a seller you will almost certainly be leaving money on the table. As a buyer, you will overpay, and that is the most common – some say the only – reason that a deal is considered a failure."

Industrial strategy special

BETTER BY DESIGN

A faculty report on engineering outlines exciting times ahead for the sector, says Grant Murgatroyd

It is not necessarily shouted from the rooftops, but Britain is good at making things. The UK's engineering sector employs 5.5 million people and accounts for 27% of GDP, with £455.6bn in sales. But it is not easy to build a successful engineering business. It takes expertise, time and a lot of money. Start-ups can access grants, tax credits and tax-advantaged investment schemes to become profitable; much of this provided by British and (for the moment) EU state agencies.

The bigger sticking point is when these start-ups need scale-up finance. There is a mismatch between opportunities available and finance options. But "a gap is not the same as market failure", argued Better Capital's Jon Moulton at the September launch of *Boosting Finance for Engineering & Technology: important considerations for the UK's new industrial strategy*, the collaborative report by the ICAEW Corporate Finance Faculty and the Institution of Engineering & Technology (IET).

BRIDGING THE GAP

The policy discussion document set out seven key questions (see box, right). It was co-authored by Shaun Beaney of the Corporate Finance Faculty; Stephanie Fernandes, the IET's principal policy adviser for education & innovation; David Petrie, ICAEW's head of corporate finance; and Dave Smith, managing director for Europe at Ricardo Plc MD and chairman of the IET's innovation & emerging technologies policy panel.

"The discussion paper is aimed at providing insights into financing issues for the engineering and technology sectors," said Beaney. "We interviewed founders and directors of genuinely innovative companies across Britian. They've direct experience of the range of investment sources."

Interviewees include Warren East CBE, CEO of Rolls-Royce (which produces £1 of every £50 of UK-produced goods exported), and Alastair Waite, CEO of Altec Engineering - a North East buy-and-build business that has been on the acquisition trail over the past two years. Other innovative engineering contributors included Bladon Jets, Cyberhawk Innovations, Dearman Engine Co, Perpetuum and Blippar.com - an innovative new technology company that, with VC backing, has expanded into the US.

"An important aim of our report is to help inform the debate about industrial strategy," said Petrie, who chaired the forum panel at the launch of the report held at the IET's Maxwell Library in Savoy Place, London. The high-profile panel included Dr Ruth McKernan CBE, Innovate UK's chief executive; Dan Horner, Blippar.com vice-president of growth; Paul Barrett, Bladon Jets chief executive; Toby Peters, Dearman's chief executive and Dave Smith.

FIRST STEPS

Much of the early-stage access to grants and other funding for engineering companies is co-ordinated by Innovate UK. Since 2007 it has committed more than £1.8bn to innovation, matched by a similar amount in partner and business funding. More than 7,600 organisations with projects estimated to have added more than £11.5bn to the UK's economy and to have created 55,000 new jobs have been supported.

"Innovate UK has a conveyor belt for funding great projects, starting from SMART grants and building through to much bigger things," said Peters. "Innovation is 50% invention and 50% adoption. Without the adoption, it's not innovation." It is the step from innovation to adoption that requires the funding,

> "An important aim of our report is to help inform the debate about the UK's industrial strategy"
>
> **David Petrie,** head of corporate finance, ICAEW

according to Peters. The government has committed £5.9bn to its Science and Innovation Strategy, but the UK remains an investment laggard. The country only invests about 1.6% of its GDP in R&D via business, the state and academia. In both the US and Germany, the equivalent figures are 2.8%, and in France it is 2.2%.

In the November 2015 Autumn Statement, the UK government said it was seeking to shift £165m of the £600m annual innovation budget away from grants to loan-based programmes over the next five years, which has led to a great deal of concern in high-tech, R&D-reliant sectors.

REPLACEMENT FUNDING

The engineering sector needs clarity about the potential impact of Brexit. As well as being dependent on European markets for its products, the UK has benefited from EU-originated funding, such as Horizon

Top: IET president Naomi Climer. Middle: panellists (left to right) Dan Horner, Paul Barrett, Ruth McKernan, Toby Peters and Dave Smith. Above: Q&A with the expert audience

JOHN DEEHAN

SEVEN KEY QUESTIONS

1 Given the engineering and technology sector's vital contribution to economic growth, skilled employment and productivity, how might the UK boost investment in engineering and technology?

2 How might the UK increase public and private investment in the commercial adoption and exploitation of R&D, expanding current government and private investment?

3 How might the government further support innovative early-stage businesses by co-financing, through Innovate UK, thereby reducing risk to attract even more private investors?

4 How effective are the UK's current fiscal incentives for R&D, tech transfer and commercialisation?

5 What additional policy and practical measures could help emerging ventures to work with large corporations even more effectively?

6 Could more be done by the UK government, market participants and professional institutions to ensure a wide variety of sources of private investment – including debt and equity?

7 Could emerging advanced engineering and technology companies benefit from even better advice and information about sources of investment and raising finance?

icaew.com/industrialstrategy

2020, which is providing nearly €80bn over the next seven years.

How the government's industrial strategy is fleshed out is crucial for engineering and technology in the UK, for a sector that needs more scale-up capital. And for corporate financiers looking for future M&A and investment deals, it is absolutely critical that UK engineering businesses get through this stage.

To increase funding for engineering and technology businesses, the private sector has to be encouraged to invest in the sector. For smaller amounts, the Enterprise Investment Scheme and Venture Capital Trusts have shown that preferential tax treatment can encourage investment, but the big issue for private investors is returns.

If the risk-return profile is attractive, then capital will flow into engineering companies. Historically it has not been. With a 14.9% return over the 10 years to December 2014, UK private equity has outperformed total pension fund assets (7.8%) and the FTSE All Share (7.5%), according to data from the BVCA and PwC.

However, returns from the kind of scale-up capital that engineers need have not been recorded as a separate category since 1996, when they were the worst performing sub-class with lower returns than venture capital.

MAKING A DIFFERENCE

By 2014, 1.6 million cars were built in the UK, including many premium marques. Although 924,000 cars were made in 1980, the design, technology and build quality was often inferior to overseas competitors. In the intervening decades, there was a push by auto manufacturers, politicians and financiers to attract more investment.

Corporate financiers have a big role to play in raising capital for bespoke products that could match the needs of innovative, high-growth companies with the needs of investors. It might not be enough to lobby government for an ever-larger slice of a diminishing pie, or another tax break.

"There has never been a more important time to support the growth of UK engineering, and technology to make us globally competitive," said IET president Naomi Climer. "We want to see it at the heart of the government's industrial strategy, with the right levels of investment and a particular focus on supporting the SMEs that are so important to our success as a global innovation centre."

Steve Turley, chief executive of Perpetuum, had a opportunity to input his expert knowledge

THE UK'S ENGINEERING SECTOR

5.5M
PEOPLE EMPLOYED

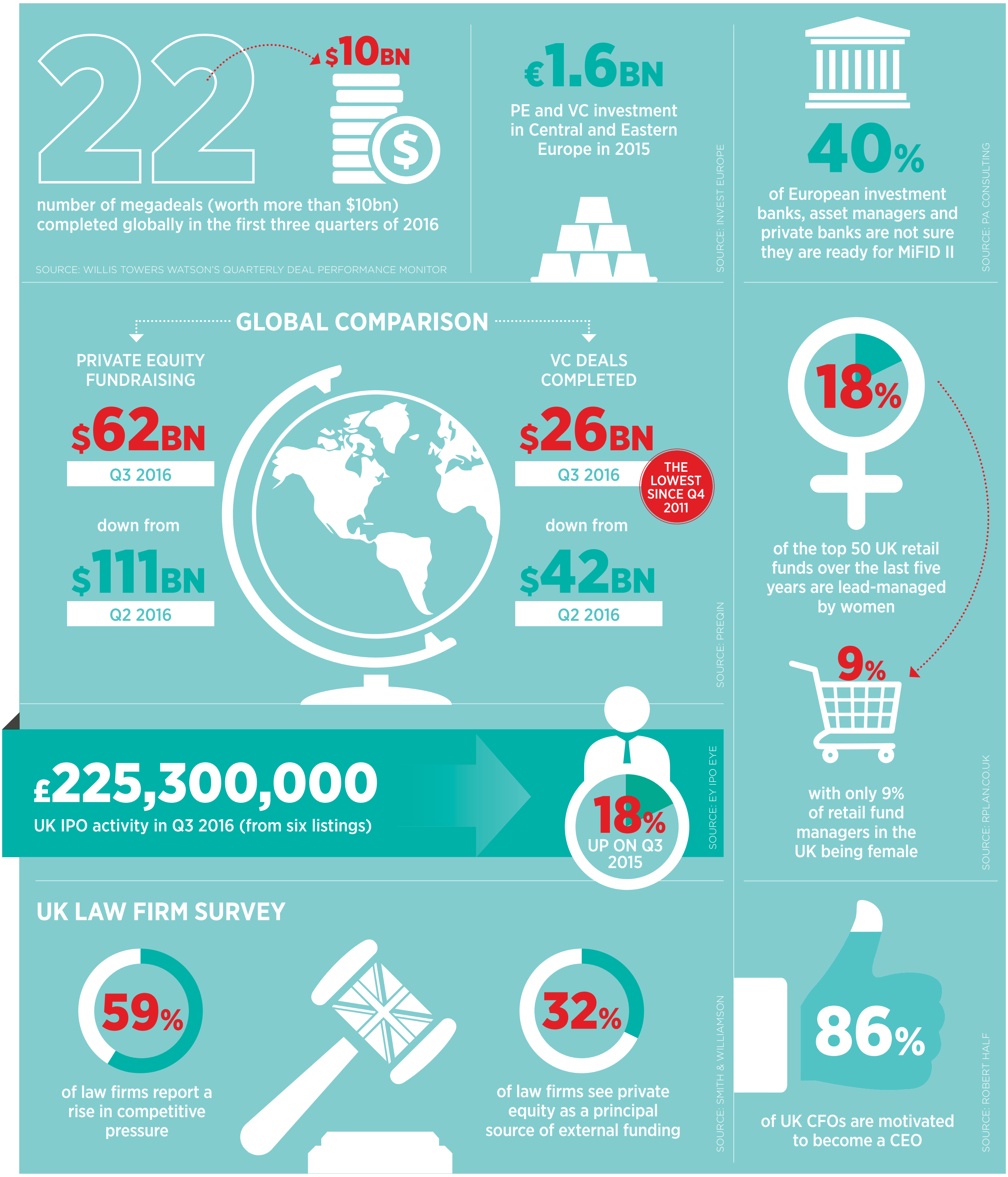
27%
OF GDP

£455.6BN
IN SALES

SOURCE: ENGINEERINGUK

In numbers

Megadeals completed globally, the UK's IPO activity, and a global comparison between private equity fundraising and VC deals



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Cheap crystal balls

The FRC has demanded that Plc directors take a view on the viability of their businesses. **Jon Moulton** muses on the silly stuff that is the result

For accounting periods starting since October 2014, the FRC has pronounced: "Companies should state whether they believe they will be able to continue in operation and meet their liabilities taking account of their current position and principal risks, and specify the period covered by this statement and why they consider it appropriate".

Two years on, and 'suitably compliant' accounts are now being published. As yet I have not seen any estimates of solvent life less than a couple of years, and nothing over five years.

Now if it were truly the case that this narrow range was a realistic estimate of the survival period of these companies, then the Stock Market would be going downhill quicker than an England football team manager's job prospects.

CAUSE FOR ALARM?

Let's take a look at a fairly random sample of reports: Royal Mail, BT, Unilever, Tesco and RBS. All of these show three years post-balance sheet date (33 months post-publication, say) as the chosen period for which the directors are prepared to say the magic words, about continuing in operation, and meeting their liabilities.

Clearly, this is potentially quite alarming in the case of RBS - is three years really the limit of the bank's directors' confidence in the business? And the language in their report is for reporting connoisseurs - apparently they use "a realistic downside scenario", which is not a "stress scenario" to form their view. Perhaps I am just being a bit thick, but...

What is interesting is that all these companies adopt three years because it fits with their stated financial planning periods. So there we have it. The viability reporting requirements simply make companies state their planning horizons.

FALSE HORIZON

International Airlines Group, despite being a highly dynamic and leveraged business, came out with a more robust five years - but again primarily because that's their planning horizon.

If this narrow range was a realistic estimate of the survival period, then the Stock Exchange would go downhill quicker than an England football team manager's job prospects

One hopes they will last longer. I'm pretty certain there are leasing companies they know who are hoping they last longer than that - they have over £6bn of lease payments due beyond that.

HOW LONG IS PERPETUITY?

These periods make no sense when you look at accounting for intangibles and pension deficits. These companies all compute intangibles over a lot longer than their projected survival. Even perpetuity is used in these computations.

BT funds pension deficits over 20 years. There are actually quite a lot of numbers in the accounts based on long-term solvency. Or certainly longer term solvency than they explicitly say they envisage being solvent for. Companies have long-term debts - Unilever, for instance, has debt maturing in 2097 - do their directors believe that they will be repaid? Even some of these companies' executive pay schemes last longer than the survival promise.

The other defects of viability reports remain. They will provide a most unwelcome acceleration into failure for companies that have to shorten their estimates. There are potential liabilities for directors. They cost money to produce. And so on.

And what has actually been achieved? We now know the medium-term planning horizons of companies.

Well done FRC.

RICHARD ANSETT

BREXIT

NEGOTIATIN

Ross Butler, director at Ten50, looks at the consequences for private equity of the different interpretations of Brexit

Every cloud does seem to have a silver lining for managers of self-terminating fixed-life private equity funds. Financial crisis? “The perfect buying opportunity”. Asset bubble? “Time to sell”. Credit dearth? “Buy for less, refinance later”. And, when it comes to deals at least, Brexit is no exception.

Many private equity managers see the uncertainty as a chance to push down ‘toppy’ acquisition multiples. And, if the economy holds up better than expected, that’s fine too. Larger international private equity players with euro or dollar funds are also bullish, viewing British assets as a foreign exchange opportunity, perhaps even with the weakening of sterling, within reason. Those investing to financially engineer infrastructure, and larger stable assets are less welcoming of the uncertainty.

MANAGERS’ VIEWS

Portfolio companies face the same issues as British business generally - the effect on employees regarding freedom of movement, and trade with the EU being the biggest issues. A post-referendum survey by Preqin found that 68% of fund managers thought the impact of Brexit was uncertain or negative, with 32% being of the view that it would at best have no impact.

In addition, 30% of managers expected to make more investments in the UK post-Brexit vote, against 20% who expect to make fewer.

From an asset management perspective, the situation is more nuanced. Should there be a so-called ‘soft Brexit’, in the sense that Britain remains a member of the EU Single Market, then very little will change for

UK-based private equity managers. ‘Hard Brexit’ scenarios on the other hand present numerous ‘known unknowns’.

First, a little context: the one sweetener in the Alternative Investment Fund Managers Directive (AIFMD) was a fund marketing passport, allowing EU managers to raise money across the bloc while bypassing national private placement regimes. ‘Third-country’ managers and funds from outside the EU could potentially also qualify for the passport under equivalence provisions.

TOUGH LOVE

The hardest Brexit scenario is one where Britain negotiates only third-country status with the EU without automatic access to this passport. But there is every reason to believe the UK will maintain a national regulatory regime that meets AIFMD requirements at a minimum, and so be in a position to qualify for the passport under equivalence provisions.

The European Securities & Markets Authority has already suggested that jurisdictions such as Singapore and Hong Kong should be eligible for equivalence. Only political hardball would deny Britain the same. A similar situation would be likely for UK-based advisers under MiFID II, albeit applying only to professional investors.

Use of the third-country passport would require that managers be regulated both in their home country and a “member state of preference”. The requirements of such oversight should be clarified in any delegated act, and are unlikely to be particularly onerous, but it would mean an increase in red tape.

NG THE EXIT

30% OF MANAGERS EXPECT TO MAKE MORE INVESTMENTS POST-BREXIT

20% OF MANAGERS EXPECT TO MAKE FEWER INVESTMENTS POST-BREXIT

GETTY

One complication is that the implementation of the third-country passport is subject to a "delegated act", which has been delayed to the extent that some have questioned whether the can was being kicked towards the scheduled review of the Directive in 2017-2018. The latest rumblings are that the European Commission is readying a draft delegated act to animate the third-country passport for Jersey, Guernsey and Switzerland.

ADDITIONAL RESOURCE

For now, though, uncertainty reigns. Adrian Brown, a partner at global law firm King & Wood Mallesons, says UK-based managers might consider various strategic options to cover any period of uncertainty: "Managers may prefer to establish an Alternative Investment Fund Manager (AIFM) in the EU, with Luxembourg often being a jurisdiction of preference. This clearly requires some expense and commitment of resource."

To take such advantage of the EU passport from, say, Luxembourg or Dublin, would mean boots on the ground with sufficient experience and expertise to create a substantial entity that complies with AIFMD rules on 'letter-box' entities.

"An alternative is to use AIFM platforms or hotels, which already have a license to operate," says Brown. "These can be hired to act as AIFM, handling risk management, with the portfolio management function delegated out."

Of the two approaches, platforms are a straightforward option, with several organisations offering off-the-shelf solutions. The use of a third party could weaken a firm's brand, but Brown says that if more firms take this route, it could gain acceptance as a standard way of operating.

While there is likely to be hassle and expense, even the worst-case scenarios aren't game-changing for those in the UK. "I don't see a mass flight of managers out of the UK and into the EU," says Brown. "There will always be ways to structure funds to benefit from the AIFMD passport."

THE EIF

For others, a critical question is the role of the European Investment Fund (EIF), which is a major LP in UK venture capital funds (see *Add venture, Corporate Financier* June 2016). UK funds currently comprise about a quarter of the EIF's total portfolio. The EIF is not an EU institution, and is governed by its own treaty as part of the European Investment Bank - however in practice they are closely linked.

The EIF has a mandate to invest in non-EU funds, but it's hard to imagine the organisation maintaining such a large allocation to Europe's largest private equity market post-Brexit. All options are open.

Managers on the road are also keeping their options open, with Brexit clauses in fund terms that allow the manager to unilaterally restructure a fund although, given the uncertainty ahead these are broadly worded clauses, not detailed terms.

Right now, no one knows very much, so quite rightly, no one is saying much. It is not the time for the private equity industry to issue statements or try to agitate for outcomes in public. Successful negotiations are often about what you don't say. Who knows, private equity's natural reticence could work in its favour for once.

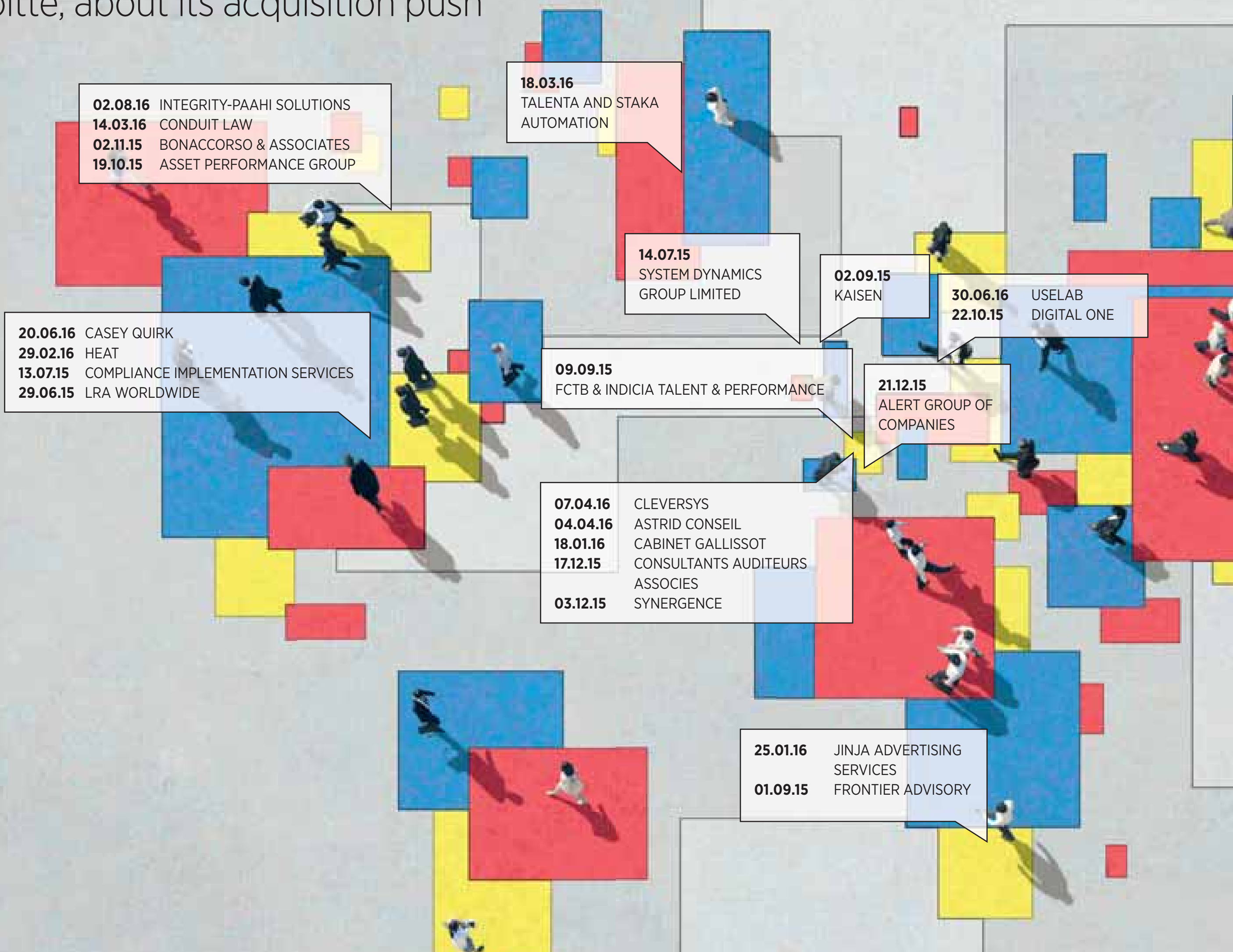
Ross Butler, founder and director of Ten50, an investment industry communications consultancy

SWITCHED ON DELOITTE

In our latest of a series about member firms' approaches to their own M&A and growth, Jason Sinclair speaks to **Marcus Boyle**, chief strategy officer at Deloitte, about its acquisition push

Q How does M&A fit in with your general plans for growth?

A M&A is a major part of Deloitte's overall strategy. Our aspiration is to be the undisputed market leader at advising firms globally. From time-to-time we identify organisations that have skills or expertise they have built that really fits with that ambition. By bringing these businesses into Deloitte not only do we become stronger, but also our clients get a better service. And crucially it gives us a competitive advantage in retaining clients, or attracting new ones.



A BROAD SPECTRUM

The past year has been a big one for Deloitte where acquisitions are concerned. Publicly announced deals alone totalled 27 from August 2015 to August 2016. The deals involved businesses based in 11 different countries. The sectors, too, are wide ranging. They encompass businesses in digital content, cyber security, strategy and digital design, asset management strategy, ERP planning, IT and analytics, finance and innovation consultancy, SAP and IT integration, legal services, advertising, audit services, sustainability strategy consulting, accounting services (including for SMEs), HR advisory and cloud, research and strategic investment advice, healthcare, brand and customer experience measurement and Oracle implementation.

Q What do you look for in an acquisition?

A The choice is whether you grow a service line organically or look externally. What we're looking for are people who want to join up with us, not sell up. We're looking for people who can come in and start to build their careers within the Deloitte network and infrastructure, both here in the UK and internationally. We have been pretty successful at that. In the past five years we've done about 100 deals that are in the public domain and various additional things with under-the-radar deals and team hires. It's a pretty big component of what we do.

Q Is the focus on sector or territory?

A There are two parts to this. First, we have our strategy to grow - so we go assiduously for organisations that are out there. We do our screening, our market assessment, and work out who's out there on a proactive basis. The second part is that others come to us. It is quite consistent across the globe. We are active in most territories, but although we have got a strategy to back various technologies, a lot of these are really emerging. As a result, it is impossible to know every single technology that will be successful. So when that happens, and we find a business that's brought a technology up to a certain level, and we can see that is going to be successful, it can make sense to buy that organisation and merge, rather than building it organically within our firm. Then we can get to that market-leading position quicker. We are certainly keen to make more acquisitions in all sectors at the moment.

Q Apart from M&A, what else do you invest in for growth?

A We do invest in fledgling businesses and individuals, in ideas that come from our employees or from external investor nodes. We do a lot of work in

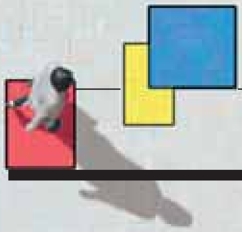
ALL IN THE EXECUTION

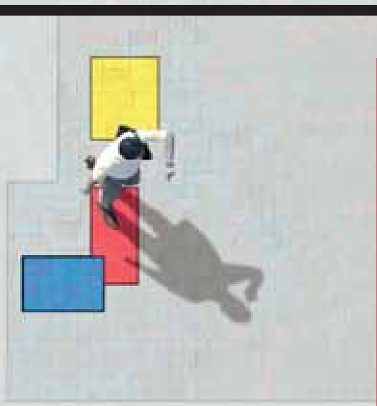
When it comes to doing the deal, Deloitte has a methodical approach. Mark Taylor, head of corporate development, explains his involvement: "I lead the transaction teams right from the start of the process. From the initial screening, I ensure everything consistently flows through to execution, and on to the handing over to the integration team. We have a due diligence team that we use – the same team with a consistent approach. They not only work on our transactions, but they are typically people who work in the professional services space, and have that specialism and understand the dynamics of other businesses like our own.

"We also have our in-house corporate lawyers dealing with legal diligence, and our consulting practice assisting on commercial diligence, alongside the sponsoring business unit. We do sometimes use external legals for bandwidth and complexity, but almost everything is done in-house."

"From the initial screening, I ensure everything consistently flows through to execution"

Mark Taylor, head of corporate development, Deloitte





“We don’t look at acquisitions for defensive reasons... we have a positive way of thinking”

Marcus Boyle, chief strategy officer, Deloitte

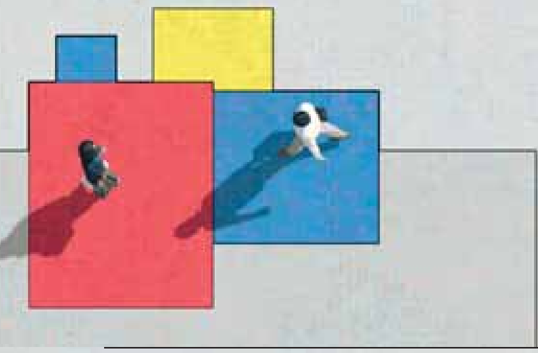
consortia - together with other businesses both large and small - to help meet a client’s needs. As our business has developed, we found there’s an ecosystem that has built up of different partners playing different roles. It is certainly a lot more complicated than it was five years ago.

Q How do you approach integration?

A We have a very successful post-merger and integration business in our suite of services that we take out to our clients. We use them to help on the integration of the businesses that we bring in.

Q How do you sell the positives to targets?

A In several acquisitions I have done, I have spent a great deal of my time with both the senior and junior people who were coming in, because it’s so important to show them and tell them what being part of our business is going to be like - because it is different. First, they chose, originally, to join that organisation rather than ours. But a really powerful part of the deal for most of these individuals is that, with our network of client contacts, we have an ability to take their products or services to a much wider audience than would have been possible before they were part of Deloitte.



Q And how do you paint the post-acquisition picture?

A Essentially, when we invest in their business and they come on board what they want is to grow their business, and we offer them that possibility. Of course, we are a big organisation, and we have got more regulatory scrutiny than they probably would have had, but this is part of being in a large global network. Being upfront and truthful about what it is really like on the inside means you can work out whether those individuals are going to want to come in. And of course, for it to be a success they have to want to come in on exactly the basis that they will be coming in.

Q Are acquisitions ever made for defensive reasons?

A We don’t look at acquisitions for defensive reasons - the overriding rationale always comes back to the question of how we better serve clients, and strive to make sure we are the market-leading organisation. How does it help us? We have a positive way of thinking about acquisitions.

Q Do you compete with other Big Four firms for targets?

A Sometimes we find ourselves in competition with other members of the Big Four, and we would stress the full extent of our global reach, the sheer size of our advisory business, and our culture.

Q Are you investing in data analytics businesses?

A Developments in data analytics are a subset of the increase in artificial intelligence (AI - see *Big Data Big Bang, Corporate Financier* July/August 2016). Businesses like ours use AI and robotics to augment all the services we offer, and in simple terms get much more done. That is one of a number of things we are doing at the moment (see box, For starters). We have a fund of money investing in disruptive businesses. We have started over 20 of these in the last year or so. The ideas come from our own people or externally. A lot of our investment is in cloud or analytics to enable our services to take advantage of evolving technology.

FOR STARTERS

Deloitte says that as well as acquiring firms, an important part of its strategy is investing in start-ups. During the last year the firm has invested in more than 30 “disruptive” start-ups, and about 20 of those came from Deloitte’s own employees.

‘Propel by Deloitte’ is a cloud-based accounting and analytics service to help fast-growing SMEs and start-ups grow. Deloitte funded this start-up through its £2.5m Innovation Investments scheme. This scheme encourages employees to turn start-up ideas into businesses. It has helped embed a culture of innovation in the firm.

Deloitte UK chief executive David Sproul is very proud of the scheme: “We’ve invested in developing our capability across emerging business disruptors, such as blockchain, crowdsourcing and robotics, working to ensure we can help our clients position their businesses for future growth.”

The business finance guide

New edition

A journey from start-up to growth

The business finance guide provides a comprehensive overview of the financing options available to growing businesses. Whatever the challenges faced, the right decisions and professional advice are critical.

The new online version of *The business finance guide* includes an interactive tool which will guide you through every stage of the journey.

BRITISH BUSINESS BANK

ICAEW CORPORATE FINANCE FACULTY

IN CHINA'S HANDS

The great haul of China continues apace as Chinese outbound M&A reaches new heights. Will it continue, or are cracks beginning to appear? David Prosser reports

Global M&A activity in 2016 may have slowed as anxieties about the world economy and political uncertainties have come to the fore. But nothing could be further from the truth when it comes to China. The country's companies agreed $121.1bn worth of cross-border deals during the first half of the year – and by the middle of September the total had climbed to $142.6bn. This already dwarfed last year's figures, which at $115.5bn represented a record year.

Chinese companies accounted for 21% of all international cross-border M&A during the first half of 2016. Led by government-linked enterprises such as ChemChina – which agreed to pay $44.6bn for Swiss chemicals company Syngenta in February – Chinese acquirers have swooped on a broad range of sectors. Once upon a time, Chinese acquirers concentrated on natural resources or technology (accounting for $26bn worth of deals in the first half), but now consumer-facing industries and healthcare are on their radars.

While Chinese businesses no doubt remain acquisition targets, inbound M&A is down this year compared with 2015. In the first eight-and-a-half months of the year, international buyers committed $28.8bn to 502 Chinese acquisitions, according to Thomson Reuters – well off the $43.8bn during the same period of last year, which came from 500 transactions.

GETTY

CHINA'S DRIVERS

However, Chinese demand for overseas acquisitions remains the story of the year for M&A markets. "The appetite for outbound acquisitions remains very strong," says Fang Xue, partner at the Beijing office of Gibson Dunn. "As we head towards 2017, it seems that Chinese business has developed to a stage where outbound acquisitions are an important step in moving up the value chain and competing on more than just price."

There are at least three factors which are driving Chinese companies' outbound deal-making strategies. The first is simply that, as the country's economy matures, its leading businesses are naturally keen to increase their share of the global market, as their overseas competitors have done in the past. In some cases, there is a political aspect to that too, with the Chinese government welcoming this expansion as an expression of economic might.

The second factor is that China's middle class is growing rapidly, in both wealth and numbers. The consultancy McKinsey forecasts that by 2022, China will have 225 million upper middle class consumers. Businesses in China recognise the

"THE APPETITE FOR OUTBOUND ACQUISITIONS REMAINS STRONG"

Fang Xue,
partner, Gibson Dunn's Bejing office

75%

OF CHINA'S URBAN CONSUMERS WITH AN ANNUAL INCOME BETWEEN $9,000 AND $34,000 A YEAR BY 2022
(MCKINSEY)

333%

RISE IN CHINESE M&A VALUES OVER PAST THREE YEARS
(CHINA M&A FORUM)

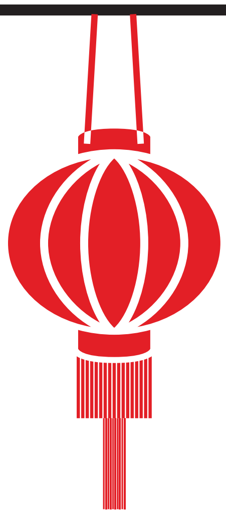
INVESTING IN CHINA

Overseas investors considering China for the first time often assume their biggest problem is going to be navigating foreign ownership rules. In fact, the Chinese government has become relatively relaxed about investment from overseas – the guidelines it produces detailing restrictions on foreign investment in certain industries covered 432 areas when they were last updated in 2015 – 48 fewer than in 2011. Restrictions have been relaxed in industries ranging from real estate to mining. Even where rules remain in place, these tend to limit foreign ownership, rather than banning it altogether.

This is not to say buyers in China do not have to worry about regulation. Research published earlier this year by Herbert Smith Freehills found that half of all companies doing deals in China felt anti-trust regulation had been their biggest challenge; the other half cited labour and employment regulation. In the case of the former, the Chinese competition regulator, Mofcom, is renowned for its willingness to intervene aggressively – it can also take its time to review deals.

Acquirers will need to consider all these issues very carefully as part of the deal process – but they'll also need to conduct extensive due diligence during an acquisition, looking at both the company itself, including its group structures, and the management team. Getting local advice is crucial.

There's also the cultural aspect of doing business in China, particularly around organisational structures, which buyers will need to address. "Chinese companies are often driven by strong personalities rather than management processes," warns a report by management consultants BCG. It also suggests that Chinese companies have more focus on top-line growth than the bottom line.



"THE PRIORITY IS ON INTELLECTUAL PROPERTY AND BRANDS"

Steve Krouskos,
global vice-chairman, EY Transaction Advisory Services

huge increases in demand this will create in some industries. In travel, for example, where Chinese companies have been big buyers of hotel chains and holiday companies; in leisure, where acquisitions have ranged from computer games producers to film studios; and in healthcare, which is another focus for Chinese buyers.

The third factor is that China's economic growth is slowing - GDP grew by only 6.9% last year, the lowest rate for 25 years. That is prompting many businesses to look abroad for new growth. A study published by law firm O'Melveny in February, found that 84% of respondents (nearly two thirds of whom were based in China) said their investment in the US would be higher in 2016 than previous years because of the growth prospects of the US economy.

INTELLECTUAL PROPERTY

The pressure to do these deals quickly, meanwhile, has been ramped up by a sharp depreciation in the value of the yuan. China's government is said to be relaxed about the weakening of its currency, as it gives exporters a lift. Against a basket of international currencies, the yuan was down 7% over the year to the end of August, according to the Bank for International Settlements (BIS), and with the decline continuing, outbound M&A gets more expensive by the day.

The broad range of companies now being targeted by Chinese businesses reflects these different strategic drivers, which look set to continue.

"China needs to acquire intellectual-property-rich assets to support the rebalancing of its domestic economy, while the upwards move of Chinese companies along the value chain in sectors, including industrials and consumer products, is also boosting demand," says Steve Krouskos, global vice-chairman of EY Transaction Advisory Services. "In both cases, the priority has been placed firmly on buying high-quality assets, intellectual property and brand, especially in Western Europe and the US."

A good example of this, he suggests, is the focus of Chinese companies on the acquisition of industrial robots and related software - especially by those businesses that target European companies. China is already the world's largest user of industrial robots, and it is steadily moving towards becoming the leading supplier. Midea Group's \$4.4bn takeover of Germany's Kuka is just one example of deals in this field.

Chinese companies are also looking for even more deals within Asia. For example, China's Alibaba, along with the Japanese company Softbank, which has a large shareholding in it, have made a series of \$1bn investments in internet, technology and media companies across Asia.

"The cash reserves of China's companies makes them capable of large-scale investments in companies in emerging industries,"

CHINESE FOREIGN ACQUISITIONS IN 2016

Target nation	Value ($M)	Rank Date	Target name	Target macro Sector	Acquiror name
Switzerland	46,596	03/02/16	Syngenta AG	Materials	CNAC Saturn (ChemChina)
Finland	8,600	21/06/16	Supercell Oy	High technology	Tencent Holdings
Brazil	7,716	23/09/16	CPFL Energia SA	Energy and power	State Grid Brazil Power
United States	6,258	17/02/16	Ingram Micro Inc	High technology	Tianjin Tianhai Invest Co
United States	5,600	15/01/16	General Electric Co-Appl Business	Consumer staples	Qingdao Haier Co
Germany	4,461	18/05/16	KUKA AG	Industrials	MECCA International
Israel	4,400	30/07/16	Playtika Ltd	High technology	Investor Group
Israel	4,031	14/09/16	Adama Agricultural Solutions	Materials	Hubei Sanonda Co
United States	3,605	19/04/16	Lexmark International Inc	High technology	Ninestar Holdings Co
United States	3,500	11/01/16	Legend Pictures LLC	Media and entertainment	Dalian Wanda Group Co

SOURCE: THOMSON REUTERS DATE: 10/05/2016

6.5%

FORECAST CHINESE GROWTH IN 2016
(OECD)

6.2%

FORECAST CHINESE GROWTH IN 2017
(OECD)

SELLING TO CHINA

The first major consideration for any business considering an approach from a Chinese buyer is whether their suitor can get the deal over the line. While this year has seen a record number of deals, there have also been many high-profile failed completions.

One difficulty is getting the deal past domestic authorities, because Western governments are not always sympathetic – although such protectionism is also common in Asia too. Chinese venture capitalist GO Scale had to drop a $3bn deal to buy a lighting business from Philips earlier this year following an intervention from the US Committee on Foreign Investment. Chinese authorities must also clear acquisitions – this year's deal between Anbang and Starwood Hotels & Resorts appears to have collapsed because of such an issue. Assuming the deal does proceed, target companies need to understand that, while some bigger Chinese acquirers have successfully navigated their way through lots of deals, others are less experienced in M&A. Mid-market Chinese acquirers with less expertise in overseas markets have become increasingly active overseas investors recently.

"Chinese buyers face challenges such as flawed or unclear M&A strategies and ineffective deal management and communication with target companies," says Nelson Lou, a consulting partner at PwC China. "Difficulties in understanding overseas culture and business environments, poorly-executed post-merger integration and synergy capture can also be concerns." The key is to "really know your partners" adds Fang Xue, partner at the Beijing office of Gibson Dunn. "The legal documentation may be as tight as you like, but it's impossible to eliminate all business risk."

POST-BREXIT RELATIONS

The UK chancellor Philip Hammond hopes a new trade deal with China will be one of the first agreements the UK makes once it leaves the EU. He met Chinese officials in July at the G20 meeting of finance ministers in Chengdu. While formal negotiations can't be conducted until the UK invokes Article 50, Hammond said it would be appropriate to hold initial discussions. Chinese state media has also reported that its ministry of commerce is keen to do a deal.

But reaching an agreement will not be straightforward. The tortured and protracted saga of the Hinkley Point nuclear power station damaged UK-Chinese relations. Other fractious issues include allegations that China is fond of "dumping" cheap imports on the UK – steel for instance. The UK will also be aware that China is a much-coveted trading partner for many other countries. Hammond may not find himself at the front of the queue once he is ready to begin formal negotiations.

> China's shopping spree during the first half of the year depended, in part, on $34.5bn of syndicated loans

says Nicola Yeomans, partner at Herbert Smith Freehills.

Another regional phenomenon is the Chinese 'Belt and Road' initiative which aims to develop closer links between China and other Asian and Eurasian countries, along the original Silk Road trade route. There has been a steady rise in deals, joint ventures and memorandums of understanding this year linked to the project, mainly in infrastructure, energy and manufacturing.

TACIT APPROVAL

So will the levels of outbound M&A continue? Rules requiring Chinese firms to get their government's approval for such deals have largely been abolished - which is a fillip for both state-backed enterprises and private concerns alike. The latter do have to rely on support from capital markets, which isn't always guaranteed.

There is growing nervousness that some of China's businesses may have over-borrowed. Dealogic highlighted the fact that China's shopping spree during the first half of the year depended, at least in some part, on $34.5bn of syndicated loans. The BIS warned in September that China's debt is at levels that in other countries in recent times had been associated with a crisis. But China's corporates aren't the only game in town. PwC research shows that Chinese investors are working closely with private equity firms on M&A transactions abroad.

Krouskos sees the biggest single threat to Chinese outbound M&A coming from outside of the country rather than within China. Some countries have become more interventionist in blocking Chinese buyers of domestic companies (see *Investing in China*, page 20). The irony here is that China itself is moving away from such restrictions - its own foreign ownership rules have been significantly relaxed in recent times (see *Selling to China*, page 21). Notwithstanding the decline in the value of inbound deals seen so far this year, anecdotally, interest in investing in Chinese businesses seems to be increasing.

$8TRN

COMBINED MARKET CAPITALISATION OF THE SHANGHAI AND SHENZHEN STOCK EXCHANGES
(FORBES)

$121BN

VALUE OF CROSS-BORDER DEALS WITH CHINESE COMPANIES DURING FIRST HALF OF 2016
(THOMSON REUTERS)

"KEY AREAS FOR FOREIGN INVESTORS ARE INTERNET AND TECHNOLOGY"

Nandu Lau,
corporate partner, Shanghai office, Herbert Smith Freehills

"OVERSEAS INVESTORS MAY FACE CHALLENGES AND DIFFICULTIES IN UNDERSTANDING CHINESE CULTURE"

Nelson Lou,
Beijing advisory leader and M&A partner, PwC China

DOORS AJAR

Nandu Lau, a corporate partner based in the Shanghai office of Hebert Smith Freehills, says the relaxation of Chinese regulation has enabled overseas acquirers to target an ever-broader range of industries in the country. "Key areas for foreign investors are internet and technology, consumer businesses, automotive and manufacturing, with niche areas such as education, healthcare and pharmaceuticals also attracting established overseas expertise seeking new markets."

This is not to suggest dealmaking in China is always plain sailing. As with any investment in an overseas market, buyers in China need to understand the economic, regulatory and political context in which their target operates.

"Your approach will vary depending on whether you deal with a state-owned or private enterprise company and you must understand the different regulatory and political imperatives for each," says Lau. "For instance, regulation changes in August made senior management of state-owned enterprises liable for company problems, including those linked to M&A and investments. That has significantly changed the dynamic in M&A negotiations in the space of just a few weeks."

Nelson Lou, Beijing advisory leader and M&A partner at PwC China, also has a warning for buyers in the country: "Overseas investors may face challenges, such as poor quality of information, reliance on related parties, incompliances in tax and social insurance, and difficulties in understanding Chinese culture, and the business environment." Crucially, China is not one ubiquitous market.

The same demographic factors driving Chinese companies to look overseas for growth are equally attractive to inbound investors, who can bring experience of consumer-facing operations to one of the world's biggest markets. To take just a single example, the $500m takeover of Hefei Sanyo by the home appliances company Whirlpool in 2014 has already added substantial value to the US company, which now has a $1bn business in China. This success sums up the opportunity. There is one inescapable fact to acknowledge - the size of the prize in China is too valuable to ignore even with its flaws.

FIVE OF THE BEST

Chinese companies that complete overseas acquisitions must work hard on integration plans. But the combination of Chinese capital investment and distribution opportunity, combined with the target's advanced technology and management experience, can prove powerful, as these examples show:

IBM Personal Computing – it's now more than a decade since Chinese computing giant Lenovo paid $1.75bn for IBM's personal computing subsidiary. The business is now the world's largest PC manufacturer, boasting double-digit rates of growth in recent years.

Smithfield Foods – China's largest pork producer Shuanghui paid around $7bn for its US counterpart Smithfield Foods in 2013. The acquisition has given the US firm access to China's enormous domestic market, while Shuanghui has imported Smithfield's operational expertise.

Volvo Cars – US automotive giant Ford couldn't hold on to its Swedish asset following the crash. Volvo was sold to China's Geely for $1.5bn. The deal has brought together a Western marque associated with top-end cars and advanced technologies with one of China's mass-market brands.

House of Fraser – the UK department store chain was snapped up by Chinese conglomerate Sanpower in 2014. The subsequent investment programme saw profits at the business rise sharply in 2015. However, the planned expansion into China has yet to materialise.

Waldorf Astoria Hotel – one of New York's landmark hotels, the Waldorf Astoria was sold to China's Anbang Insurance Group in 2014 for $1.95bn. The hotel is set to close for refurbishment next year. Rumours persist that Anbang is planning huge investment to convert many of the rooms into luxury apartments.

RISK FACTOR

The nature of environmental due diligence is changing. Rather than purely assessing liabilities from past activities, specialist advisers are turning to look at future risks and opportunities, says **Jenny Cope**

Environmental due diligence is a prudent part of any transaction when operational businesses or real estate assets are involved. Vendors, purchasers and lenders simply have to consider these issues, particularly as the affect they can have on a deal can be habitually missed from conventional balance sheet assessments.

It has become increasingly acknowledged that environmental health and safety (EHS), energy and sustainability issues can require enhanced Capex commitments, or that these issues may add to operational costs, create reputational risks, divert management resources or reduce asset values. The change in focus that specialist environmental advisers are now seeing is that investors and their funders are not only looking at traditional liabilities, but also whether or not their investments are fit for the future.

The risks and opportunities vary from business to business. They relate to sites, processes, products, services, and an organisation's history or as a result of its geography.

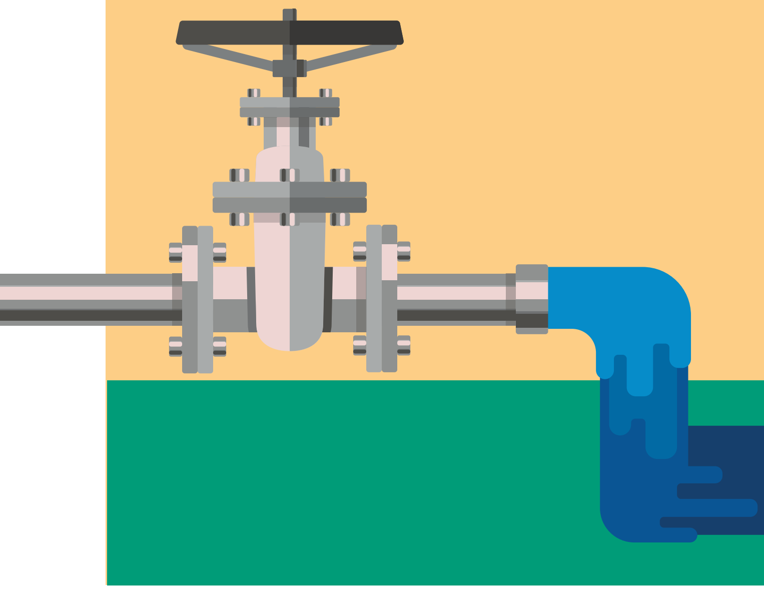
ENERGY AND THE UK

In the UK, Energy Performance Certificates (EPCs) have needed to be in place for both the sale and lease of property since 2007. In most cases, as long as a valid certificate existed, little attention was paid to the EPC rating.

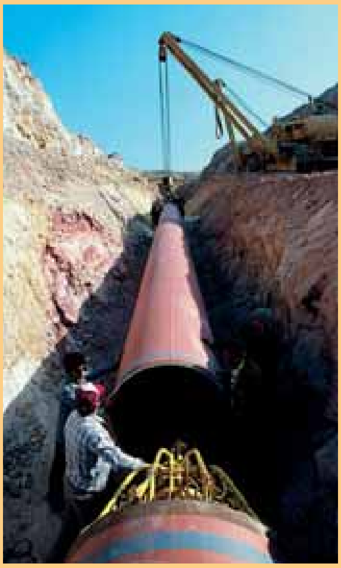
However, that has all changed, because recent regulations mean that from April 2018 properties cannot be let to a new tenant, nor a lease renewed with an existing tenant, unless the EPC certificate has a minimum E efficiency rating. There is now a direct link between a property's EPC rating and the ability to lease that property, and therefore its value. As a result, during the due diligence process for real estate transactions, there an is increasing focus not only on a property's EPC rating, but on the robustness of the assessment and identifying opportunities to improve the performance of the building.

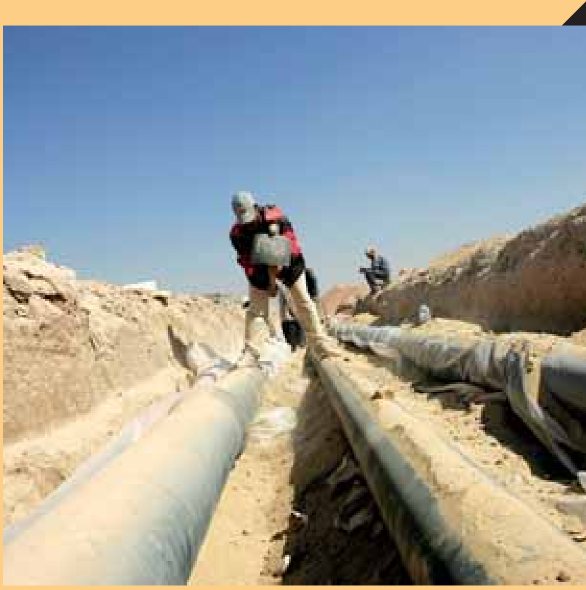
For example, Aberdeen Asset Management (AAM) has incorporated these considerations into its due diligence process for both the sale and acquisition of property assets. AAM was an early mover in understanding its exposure as a result of a minimum E rating, appointing WSP Parsons Brinckerhoff to review its UK property portfolio back in 2012.

This demonstrated the value of a robust EPC assessment, and AAM continues to review the EPC status of existing assets on a business-as-usual basis. This ensures that when an asset is earmarked for sale, any risk of the property not achieving a minimum E rating is already understood, and can be factored into the disposal strategy. For the acquisition of new property, AAM either wants to see that the current rating is D or above or, if not, that a plan's in place to improve the rating. This improvement strategy has allowed AAM to invest in property that may currently be poorly rated, while still retaining the potential to add value where possible.



There's an increasing need to look ahead to climate change and energy legislation





REFINE AND REFOCUS

Traditionally, the emphasis of environmental due diligence has been on legacy issues (such as contaminated land or asbestos management), and as such typically focused on immediate asset-value impact. Environmental due-diligence specialists would find out the background story of a property – whether or not the otherwise innocuous building is built on a former petrol station, coal mine shaft, chemical works or landfill, or whether the building fabric was packed with asbestos.

Although these are still important considerations, there is increasing need to look ahead and quantify risks associated with climate-change aspects, and associated energy legislation.

Climate-change aspects can affect the ability of a business to trade on a day-to-day basis. The obvious example is flood risk, in particular examining how a storm event may impact a business today, and any potential change in impact in five or 10 years' time.

As a second example, new legislation driving energy-efficiency measures may well affect the practicality of a site's operations or its real estate. Investors are compelled to ensure that their businesses are future ready, and many have internal requirements to consider environmental and social governance as part of their investment decision. Relevant expertise can ensure that clients' investments are sustainable in the broadest sense of the word, by looking at energy management and best-practice improvements, as well as considering the commercial merit of renewables or reducing energy consumption.

It is not just property and general site operations that require a look to the future. At a process level, there is a crucial role for EHS compliance specialists in assessing whether substances currently used in the life cycle of a product have longevity, or if are they scheduled to be banned by registration, evaluation, authorisation and restriction of chemicals regulations. Additionally, energy engineers can examine how a process runs and whether savings can be made. In essence, environmental due diligence no longer simply stands still and glances in the rear-view mirror, but also questions the future and seeks to identify opportunities as well as liabilities and risk.

The earlier environmental specialists are brought in, the more options are available to an investor if risks or opportunities are identified. Being informed from an early stage can reduce costs and provide the opportunity for negotiation, insurance or warrantees or, if need be, further assessment.

Jenny Cope, principal consultant, WSP Parsons Brinckerhoff's environmental due diligence team

CASE STUDY: JORDAN

As part of a wider due diligence exercise involving the assessment of a portfolio of power and water assets owned by GAMA Enerji, WSP Parsons Brinckerhoff carried out a detailed environmental and technical assessment of the Disi-Mudawarra to Amman water conveyance system in Jordan. The impressive feat of engineering involves extracting 100 million cubic metres of water annually for 25 years from underground reserves located under the Disi region and pumping it through a 325km-long steel pipeline to the reservoirs in Amman. The project aims to stabilise Jordan's water distribution programme and increase the amount of drinking water the public receives.

The challenge was to quickly assess the project to support inward investment into GAMA Enerji by Malaysian electricity firm Tenaga Nasional Berhad and supporting financial institutions. Over a three-month period, involving desktop reviews and two targeted due diligence visits, all aspects of the project were examined, from the well fields close to Jordan's border with Saudi Arabia, along the transfer pipeline to the reservoirs close to Amman.

Specialist advisers confirmed that the project followed correct design and construction practices that should, with reasonable maintenance and use of its inbuilt contingency, be able to maintain its performance over the 25-year period. The well field was also assessed to ensure that the drawdown on the water reserves was well managed, with appropriate rest allowances.

While there were many positives from the assessment, there were definitely opportunities for improvement. These included sustaining good operational, social and security practices across remote sites, chlorine management and monitoring of radioactive waste from sediment pump-out.

100

CUBIC METRES OF WATER TO BE PUMPED ANNUALLY TO AMMAN

325KM

OF STEEL PIPELINE TO BE USED TO TRANSFER THE WATER

GETTY

KEEP YOUR FRIENDS CLOSE

Steve Ivermee, EY's transaction advisory services managing partner in the UK, tells Marc Mullen why he thinks the three Cs are the way ahead for professional services

The three Rs are the traditional foundations for learning; even if the first thing to learn is that they aren't actually three Rs. For Steve Ivermee, EY managing partner of UK transaction advisory services, (TAS), three Cs define its strategy - continuity of strategy, change and collaboration. Ivermee has been with the advisory firm for 26 years, and in April assumed the head role.

In 2013, EY announced its Vision 2020 strategy, with the central aim of growing revenue to $50bn by 2020. The TAS business is targeting a doubling of its revenues over that period, which would require a composite growth rate of 13% a year - over the last two years it was 18%. EY's "capital agenda" approach to providing advice, established in 2013, continues to be central to growth plans (more on this later). Collaboration may well be something that EY says it has done well over the years, but for Ivermee it means working together to an even greater extent across service lines, and internationally.

The deployment of disruptive new technologies is critical - as it is for all big advisory firms (see *Big data bang*, *Coprorate Financier* July/August 2016). Ivermee predicts some very interesting changes over the next four years - robotics, AI and data analytics combining to shift the emphasis of the TAS skill base: "There will be more demand for those who can work with those new tools. We have a lot of market opportunity to grow into. It means the trend, which sees us competing beyond the Big Four, with a much broader competitor set - strategy houses, boutiques and analytics businesses - will accelerate."

MOVING ON

Having begun by training as an auditor in 1990, how did Ivermee ascend to his current role in transactions? The pivotal moment was in 2000, when he was on the partner track programme, and spent a year on secondment at BBA Group. "My role was to help the CFO fix his most pressing challenges," says Ivermee. The projects included a six-month stint in South Carolina. "I wanted to expand my horizons beyond audit, and beyond London, to experience much more commercial challenge, and the secondment certainly did that."

In 2000, British Belting & Asbestos, which had been given the acronym BBA for obvious reasons, was a conglomerate. Helping the CFO with divestments was Ivermee's role, as the business embarked on its transformation into an aviation services businesses - it is now the FTSE 250-listed BBA Aviation.

In June 2001, he was made partner. He was almost immediately asked to move into transaction support (TS). "It was a business that was growing. It had come out of our assurance practice in the mid-1990s, and they felt it had a lot of potential. I enthusiastically said yes, and started out working on mostly large-scale corporate divestments."

The divestment experience he'd gained at BBA proved very useful. BBA itself became a major client for Ivermee and the EY TS team, as the business was in the middle of its divestment programme.

Another major client was Invensys, the multinational engineering and IT business,

"I wanted to expand my horizons beyond audit, and beyond London, to experience much more commercial challenge"

formed through the merger of BTR and Siebe in 1999. It was quickly forced into a major restructuring programme to cut costs, as falling sales and large debts had left it in a precarious state."We were working with Invensys on a series of complex carve-outs and divestments for three to four years," says Ivermee. The work culminated in a £2.7bn refinancing and debt restructuring in 2004 that saved the business. "For me, and the team, such a multifaceted engagement was exciting and absolutely fascinating."

BOOM TIME

Divestments may have opened the M&A door for Ivermee, but after 2004, the booming private equity industry became a focus. Private equity and divestments converged in the transaction Ivermee is most proud of. Completed in December 2015, it was Bridgepoint Capital's sale of life sciences measuring and testing company, LGC, to global investment firm KKR (for an undisclosed sum). Bridgepoint had acquired LGC in 2010, and Ivermee acted as buy-side adviser.

"After getting to know the management team through that initial engagement, we built a relationship, as we supported them through all 12 of their bolt-on acquisitions," he says. "In five years, they transformed the business. I'd been advocating that all our TS partners follow management teams post-deal, get to know the companies and support them through that period, and that is what happened with this relationship."

Getting close to management teams, understanding the business strategy and understanding the capital cycle of the business sums up the capital agenda approach. For Ivermee, being

THE CV

Steve Ivermee left the University of Oxford in 1990 with a degree in physics. He started training as an auditor with Arthur Young just in time to witness a merger up close – Arthur Young and Ernst & Whinney were in the process of integrating to form Ernst & Young (now EY).

He audited a range of industries, but most significantly insurance, and primarily for Lloyds syndicates – he was auditor for Lloyds of London. He had also worked on a lot of industrial products and engineering businesses.

While on the partner track programme in 2000, he was seconded for a year to industrial conglomerate BBA Group. Having gained real M&A experience Ivermee was made partner and, in 2001, he moved into transaction support.

As well as further assignments for BBA, he worked on deals for Invensys and later for Clayton Dubilier & Rice, Warburg Pincus and Bridgepoint Capital. He is global service partner for Bridgepoint.

From 2010, he took on leadership roles – such as transaction support leader for the UK – splitting his time 50:50 between running the practice and his clients.

In 2013, he was made leader for EMEA TS – about 1,700 professionals in 87 countries. In 2015 he became COO for the UK TAS practice and then in April 2016, he took over as managing partner for TAS in the UK.

appointed ahead of the banks was the high point: "Usually it is the other way round. We were not simply positioning ourselves to carry out vendor due diligence for LGC, but to support them in the fullest possible way, articulate their investment story, and prepare the information to support that equity story."

There was a highly competitive auction for LGC, with trade and private equity interest. It took six months from JP Morgan and HSBC being appointed to completion in December 2015. The process was then a classic three-month, two-round process.

EY's capital agenda approach was a strategy developed in the wake of the global downturn. In no small part it was to counter the downturn in the volume of transactions. But for clients it is about preserving cash, optimising operating structures, through legal entity rationalisation, or through making tough capital allocation decisions. Ivermee says it remains a completely relevant approach today - hence the continuity of the strategy.

THE NEAR FUTURE

Ivermee says one of the critical success factors will be to continue investing in origination capabilities: "we have invested in our origination hubs [where the focus is on deal origination] in London, New York and Frankfurt, and have one being built up in Singapore."

The investment started in London when they hired investment banker Hugo Parsons, from Morgan Stanley, in 2012. "He was made partner last year and is someone with an origination mindset."

Parsons is EY's head of origination for EMEIA, and he now has more than 15 people in the UK focused on private equity sponsor coverage. They are now building out sector-based origination teams, whose purpose is not just to win M&A mandates, but to pull together sector and new market insights, to lead dialogues with clients.

Ivermee feels very passionate about the investment, feeling that it provides the catalyst for a good client contact and provides valuable sector insights. Progress, Ivermee notes, needs to continue over the next for years.

EY, like the other Big Four firms, has been investing in analytics and recruiting a large number of data analytics specialists who are comfortable innovating with new tools, and developing bespoke tools to solve problems.

Another area of innovation for the CF strategy team is in the development of more sophisticated strategic portfolio optimisation tools. "While that is something that exists as a service offering already, it is about bolting that together with a more analytical approach to optimisation scenarios [involving using the latest developments in tech and data analytics] - the tax consequences, the operational consequences - a much more thorough assessment of that portfolio operation."

In the wake of the UK's Brexit vote, Ivermee says there has been something of a pause-and-assess, but not a freeze on recruitment. "There are parts of our business that will be in high demand - strategic services, decision support, modelling scenarios, for instance - and we will continue to recruit people into those areas.

"Maybe we will be a little more cautious of how many deal professionals we bring in, but we hope to return to more normal business levels in Q1 2017."

In broader terms when it comes to the impact of Brexit, Ivermee is of the opinion that the devil will be in the detail - and that it will become much clearer when there is more clarity over the trajectory of negotiations by the UK government and the other EU members.

However, Ivermee does see a more medium-term upside to a sentiment-driven drop in M&A volumes. It may result in a sellers' price-expectation adjustment. And that could mean that 2017 and 2018 prove vintage years. "Private equity and corporates have a huge amount of dry powder available to deploy."

MARTIN BURTON

FIGHTING FIT

As long as the public keeps spending on leisure, it will remain a hotbed of M&A. Grant Murgatroyd looks at a UK sector that's in rude health

When times are tough, consumers tighten their purse strings and concentrate on the necessities. Discretionary spending - money spent by consumers on things like holidays and luxuries - is cut back. That's the theory, but what's the practice?

Consumer spending in Britain fell by almost 5% in 2008, but has since recovered, rising by about 2% annually since 2011, according to Deloitte's UK Consumer Tracker. No doubt low interest rates and the ready availability of consumer credit have buoyed such spending.

Going out, eating in restaurants and taking long holidays have been among the best performing sub-sectors. Brexit may have killed the mood, with 37% of consumers no longer confident about non-essential spending over the next 12 months, but overall the leisure sector is still in rude health.

"Consumers are not cutting back on their leisure spend," says David Burns, managing partner at Phoenix Equity Partners. "People are doing, rather than wearing. There is a polarisation. Value-for-money is incredibly important, but premium is also doing well. It is the guys in the middle who are finding it more difficult."

"WE LOVE DISRUPTION AND ALWAYS TRY TO FIND IT"

Daniel Smith,
partner,
Livingbridge

PUMP IT UP

Gyms illustrate the investment trends perfectly. Private equity (PE) investors got on the fitness bandwagon in the 1990s and have had an on-off relationship with it ever since. Fitness First, Esporta, Virgin Active and David Lloyd are all owned by PE firms.

More recently the focus has been on low-cost providers. In November 2015, economical operator Gym Group floated on the London Stock Exchange. Originally backed by Bridges Community Ventures, and later Phoenix, the £250m IPO gave Phoenix a 2.5x return, and an IRR of 45%.

In 2015, there were 39 UK leisure sector deals, with a combined value of £4bn. The massive increase from $736m in 2014 was

Visitor attraction: Fubon Life Insurance Co Consolidation is buying the Tussauds Group for $540m

down to a handful of mega deals, including the (still pending £2bn) acquisition of Gala Coral Group by Ladbrokes, the acquisition of Virgin Active by Brait, and the sale of Tussauds Group to Fubon Life Insurance Co Consolidation, and the desire to bring growing brands into the stable, is driving corporate M&A.

"Some sub-sectors have reached high multiples," says Deloitte's Ed Jenkins. "If you've got a good brand and are demonstrating strong metrics from the consumer, people are prepared to pay more than has been seen in the past. PE is looking for high-growth businesses with brands they can roll out."

SHAKE IT OFF

Leisure is a sector where investors are not so risk averse, perhaps because it is perceived as being easy to understand. The risk is in the execution.

"We love disruption and always try to find it," explains Daniel Smith, partner at Livingbridge. "We love eating and drinking, because there is always innovation and the next entrepreneur with a great format that they can take from one to 5-20 sites. In travel, technology has completely disrupted the market and transformed it. TUI Group may have survived as an integrated travel business, but it is an anomaly."

Livingbridge made a £54m growth capital investment in Sykes Cottages in December

ALAMY

2014. It is a distribution, not an asset ownership business. "Booking.com is a great example of this," says Smith. "It doesn't own any assets but is absolutely dominant in that market. At the heart of that business is fantastic technology. It's about online marketing, the quality of the website and the user experience. You have to be better at those things than everyone else."

As always, strength of management is the key to successful investing. "Focusing on what the customer really wants is going to be much more prevalent going forward," says Deloitte's Jenkins. "It's about the expertise within the company."

Leisure buyers are drilling into the data. In 2015, 76% of PE owners globally used data analytics on potential portfolio companies, before completing M&A transactions (up from 68% in 2014), while 66% of corporates do (up from 55% a year earlier), according to Deloitte's *M&A Trends 2015 report*.

"Buyers have to be very wary of forex movements in travel. None of us know how long this volatility is going to last, so that would be one of the big flags in that industry," says Jenkins. "Companies also need to be aware of the minimum wage issue and have mitigation plans. We've seen the PR hit you take if you get that wrong."

"BECAUSE WE DON'T HAVE A FUND, OUR OVERHEADS ARE LOWER"

Mark Harms,
founder and chairman, Global Leisure Partners

ONE MORE WAFER-THIN MINT?

In 2015, average multiples on US leisure sector M&A hit 16x Ebitda, beating 2007's record of 14.3x, according to Thomson Reuters. Leisure has fantastic dynamics, but investors have made mistakes before.

"We were doing captive co-investing alongside the large PE firms from 2005-2008," says Mark Harms, founder and chairman of Global Leisure Partners (GLP), one of the largest specialist merchant banks in the sector. "That was not a great time to be investing. It was the top of the cycle and we watched a lot of train wrecks take place. When it comes to overpaying, we've got the T-shirt, but we've learned a lot of lessons."

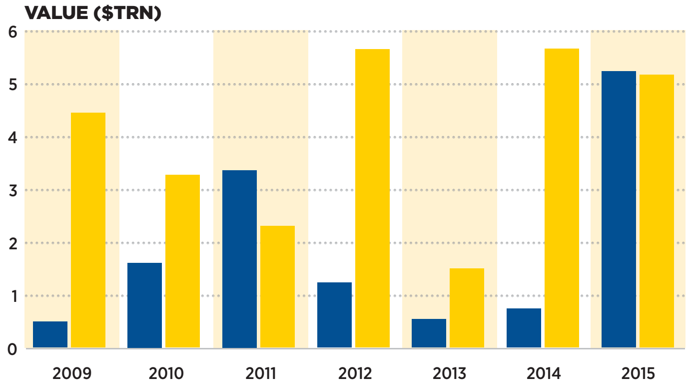
The key for GLP now is flexibility. The firm may advise or structure an investment package, calling on a network of LPs for deal-by-deal funding and using capital and loan markets where appropriate. "We bring together deal sourcing, operational and investment expertise," says Harms. "Because we don't have a fund, our overheads are lower, and we can structure a deal to make two-and-a-half to three times the money, sometimes over a longer hold period. One of the issues with PE is if you have a great business, by the time you've learned what makes it tick you've got to sell it to return capital to investors."

RECREATION AND LEISURE M&A

NUMBER OF DEALS (UK | USA)

2009	2010	2011	2012	2013	2014	2015
33 | 72	41 | 70	38 | 47	44 | 71	20 | 74	43 | 73	36 | 69

VALUE ($TRN)



SOURCE: THOMSON REUTERS

Gambling: a £2bn Ladbrokes take over of Gala Coral Group is still in train

Appointments

DELOITTE PARTNER PROMOTIONS

Deloitte has made five partner promotions in UK transaction services: Caroline Ward (left), Will Geer (left, middle), Baber Din (left, bottom), Chris Wildsmith and Duncan Down.

Ward trained as an ACA with Deloitte, and spent three years working at the FSA. She rejoined the firm in 2011 and focuses exclusively on equity capital markets, advising clients through the IPO process.

Geer joined the firm in 2005 and focuses on M&A in the insurance sector. He has been key in building relationships with large insurers in the London Market, Lloyds and Switzerland.

Din has more than 17 years' financial services sector experience, advising Plcs, multinationals and PE clients.

Wildsmith has 12 years' M&A experience and focuses on mid-market transactions. He has a specialism in non-standard lending.

Down joined Deloitte in 2007 from KPMG. He focuses on working with mid-market PE houses and PE-backed businesses in London and the South. Based in Bristol, he leads a team of 15 transaction services professionals.

The firm has also promoted two to partner in portfolio lead advisory in London. Benjamin Collet joined Deloitte in 2011 and has 20 years' experience as adviser and principal investor across Europe and Asia. He focuses on banking restructuring and distressed assets. David Lane joined Deloitte in 2013 as senior director from EY. He has more than 16 years' experience in financial services, having previously worked at Signature Capital and Investec.

Nick Soper has also been promoted to partner in London. He joined Deloitte in 2012 from Investec, and has led the establishment of the firm's debt advisory offering to UK mid-market corporates, focusing on FTSE 250, Small Cap and AIM borrowers.

Deloitte has also promoted the following to partner: Katie Jackson and Biren Shah (London forensic team); real estate specialists Anita Aul (London) and John Cooper (Manchester); and Jacquie Beanland and Nick Wood (financial Advisory).

SCOTTISH EQUITY APPOINTMENTS

Scottish Equity Partners (SEP) has promoted Tony Robinson (left, top) and Keith Davidson (left, center) to partner, and recruited Sarah Roughead (left, bottom) as director of fund reporting.

Robinson joined SEP in 2011. He previously worked with high-growth technology companies. he is focused on portfolio management and deal support.

Davidson joined SEP in 2015, from August Equity, having spent the previous decade in the private equity industry. He focuses on new growth capital investments across the IT sector.

Other new recruits include Verena Rathgeber, as principal focused on renewable energy investments, and Tim Ankers, investment analyst who joined the firm from Deutsche Bank. Rathgeber previously worked at WHEB, Climate Change Capital and Rothschild.

NEWS IN BRIEF

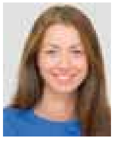
Former BVCA CEO, Mark Florman, has taken over as chairman of **LPEQ**, from Tim Spence, who had been chairman since July 2015. Florman said: "I firmly believe that the public markets will play an ever greater role in the funding of the private equity industry, and the private companies they support." Florman worked at Doughty Hanson from 2001 to 2008, and then formed private equity firm 8 Miles alongside Bob Geldof. He became chief executive of the BVCA in 2011, where he remained until April 2013. In 2014 he became a BBC trustee.

Bart Somerville has joined **RSM** from BDO (where he was director in the valuation team), as corporate finance director, focusing on business and asset valuations. Based in the London office, he will assist Simon Martin, a partner in RSM's project finance, modeling and valuations practice, in developing and expanding the business and share valuation offering.

Jon Pickering has been promoted to head up **NorthEdge Capital**'s Manchester office, and will lead the firm's investment operations across the North West. He has worked in the region's private equity market since 2002, and joined NorthEdge in 2013 from LDC. NorthEdge also opened an office in Birmingham in September.

Roger Lambert is joining **Peel Hunt** as partner in the broking and advisory firm's corporate department, in January 2017. He leaves Canaccord Genuity, where he has been chairman of its corporate broking practice since January 2010. Prior to that, he spent 26

GARLAND JOINS MOBEUS AS INVESTMENT MANAGER



Danielle Garland has joined Mobeus Equity Partners as investment manager in the private equity firm's buy-out investment team.

Garland joined from KPMG, where she spent nearly eight years in a variety of roles. her final role was as a manager in the transaction services team of the private equity group. She is an ACA and a chartered financial analyst.

Ashley Broomberg, Mobeus partner, said: "In the wake of changes to the VCT rules, we continue to invest in our business to enable us to pursue a broader investment strategy which includes growth and buy-out capital and to continue delivering strong returns to our retail and institutional investors."

CAVENDISH CORPORATE FINANCE MAKES HAY HEAD OF DEBT

Cavendish Corporate Finance has appointed Alistair Hay to partner and leader of its debt advisory service. Hay has joined from EY, where he was a director in its capital and debt advisory business. He previously spent 11 years at Royal Bank of Scotland, where he worked in the leisure and TMT sectors, debt origination, and latterly as a director in the structured finance corporate team.

He has a bachelor's degree from the Wisconsin School of Business at the University of Wisconsin-Madison. He is also a member of the Association of Corporate Treasurers.

MARSDEN CLARK SHARES EXPERTISE WITH S&W

Marsden Clark Corporate Finance and Smith & Williamson Corporate Finance have joined forces. Jim Clark (left, top) has joined as a director of Smith & Williamson Corporate Finance, and Philip Marsden (left, bottom) as a consultant.

Smith & Williamson is one of the top 10 largest firms of accountants in the UK. Its investment management business has around £16bn of funds under management, and it employs more than 1,600 people in 13 offices across the UK, Ireland and Jersey.

Clark said: "We chose Smith & Williamson because they share the same values with regard to client service and focus. Also, their corporate finance practice is part of M&A International, an independent alliance of specialist merger and acquisition firms operating in every major financial centre in the world."

Brian Livingston, head of M&A at Smith & Williamson, said: "Jim and Philip are veterans of numerous M&A transactions and have an excellent cultural fit with Smith & Williamson. They are service driven, create long-term relationships and give independent advice focused on the needs of the client."

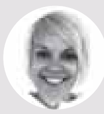
years in corporate finance at JP Morgan Cazenove, where he was partner and then a senior managing director.

Pagemill Partners, the Silicon Valley-headquartered tech-focused division of Duff & Phelps, has recruited Rory O'Sullivan as managing director to lead European technology M&Ain London. He previously set up US firm Bulger Partners' European investment banking arm, and served as head of European M&A at Canaccord Genuity.

Joanna Hislop has joined **CDC International Capital** as member of its investment committee and as independent administrator. She started at Goldman Sachs in 1995, and was partner at Park Square Capital for six years.

Michael Collins has taken over as chief executive of **Invest Europe** from Dörte Höppner, who has moved on after five years at the helm. Prior to that he was managing director for European government affairs at Citigroup.

Gervais Williams, chief executive of Miton Group Plc, has taken over as chairman of the **Quoted Companies Alliance** from Michael Higgins, who had been in the role for three years.



Lesley Rolfe has been appointed head of asset finance operations at **Aldermore**. Joining from Barclays she also joins the specialist lender's business finance senior leadership team. She previously worked at AA Insurance Services, Lloyds Banking Group and Sun Life.

Johnny Colville has joined **Houlihan Lokey** as MD in its financial sponsors group, having previously held the same position at HSBC and Deutsche Bank. In Amsterdam, Laurens van Asselt has joined as managing director from Rabobank to support the firm's power & utilities, environmental, and infrastructure coverage in Benelux.

Kevin Craven has joined **Metro Bank** as head of invoice finance from Bibby Financial Services, where he was corporate risk director and previously led the corporate sales team.

Another brick in the wall

THE CV

Adrian Lamasz is senior partner of the UK retail M&A practice in JLT Specialty. He started his career in insurance with Minet, before joining Jardine Lloyd Thompson (for the first time) in 1995. In 1999 he joined Alexander Forbes, before co-founding a risk consultancy (Lamasz Hettie) in 2002. In 2006 he joined JLT Specialty.

Recent deals

- Caledonia on the £118m MBO of The Liberation Group in September 2016
- Equistone and Inflexion on UK Power Reserve investment in December 2015
- LDC on the £175m secondary buy-out of CitySprint in February 2016

Insurance due diligence proved crucial for the success of Westleigh's buy-out, explains **Adrian Lamasz**

WHAT WAS THE DEAL?
The Palatine Private Equity-backed MBO of Westleigh Partnerships, which valued the business at £65m. Westleigh, Leicestershire, was founded in 1985 and has a focus on building affordable homes. it has turnover of roughly £100m, which is forecast to grow to £165m by 2018. In 2015 to 2016 it achieved an EBITDA in excess of £9m. The transaction was significant for Palatine - the first for their Midlands office, which opened last December.

HOW WERE YOU INTRODUCED?
Richard Thomas joined Palatine from Lloyds Bank, where he had been working in the acquisition finance team. He is well known in the Midlands. We had previously carried out similar work for him when he was at Key Capital Partners.

WHAT WAS YOUR ROLE?
We carried out insurance due diligence on Westleigh. We told Palatine what we thought the risks were, how they mitigated those risks, and the adequacy of the insurance that sits behind those risks. We looked at any losses incurred or claims made by Westleigh and then with reference to our view on the total cost, recommended action on their insurance cover. The major thing they wanted to understand was the professional liability risk. Design and construct is a specialised area of insurance. At JLT we have specialists in construction risk insurance. We used their expertise to get their latest understanding of what could be achieved. We assessed the management rigour in the business, and benchmarked how it performed against similar businesses.

WHO ADVISED?
The sell-side corporate finance advisers were Clearwater, who also gave debt advice. Catalyst Corporate Finance advised the acquirer. CIL carried out commercial due diligence for Palatine. Gateley provided legal advice, KPMG financial due diligence and GK Strategy political due diligence. We provided insurance.

WHAT WERE THE TIMESCALES?
It was not a superfast timetable. Palatine worked with the management team to structure the deal, not only to meet the shareholders' objectives, but also provide the business with the capital structure to support its growth. The property element, along with Brexit, meant the deal took around eight months. This enabled us to understand the business and the aims of the investors. That said, we did most of our work over a six-week period.

ANY HURDLES?
There was a significant property dimension to the business, which is usually more the domain of specialist equity or property firms. Getting our heads around that was a factor, but not an insurmountable one, because of the expertise we were able to call on. Westleigh is involved in the manufacture and assembly of structural construction materials, so understanding the supply chain - and the potential interruption scenarios - was also key.

LESSONS LEARNED?
Don't judge a book by its cover. It is quite easy to have a preconception of a business because it is in a certain sector. I think the construction sector gets quite a bad rap, which is undeserved largely. Westleigh was a professional, exceptionally well managed business, and gave us high-quality information when we needed it.

ROBIN PALMER

The Corporate Finance Faculty would like to thank its many member organisations for their support in 2016

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