

Global M&A's Bright Spot – China Outbound Activity

Coming off a record 2015, M&A activity is down 10% globally this year and lagging last year's data in most areas. Except for China outbound M&A.

As of the end of May 2016, China year-to-date (YTD) outbound M&A deal count and deal value were up 63% and 145% respectively compared to YTD 2015. Indeed, the growing prominence of Chinese buyers is proving to be a bright spot for relevant North American and European sellers.

To explore this trend in greater detail, we spoke with a team of Baird experts – Chris McMahon, Head of Global M&A, David Silver, Head of European Investment Banking, and Anthony Siu, Head of Asia Investment Banking – and asked them to share their insights on where this trend might be headed next.

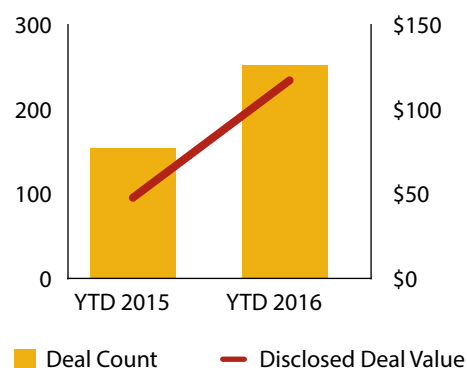
M&A EXPERTS HAVE BEEN DISCUSSING THE FUNDAMENTAL CATALYSTS PROMPTING CHINESE BUYERS TO CHASE WESTERN ASSETS FOR YEARS, BUT IT HAS ONLY BEEN IN THE LAST 6 MONTHS WHERE WE HAVE SEEN THE M&A ACTIVITY SUPPORT THESE OBSERVATIONS IN SUCH A MEANINGFUL WAY. WHY NOW?

Siu: The drivers of Chinese outbound M&A remain intact: slowing domestic GDP growth; loosening of Chinese outbound regulations; globalization strategies of state-owned and privately-owned enterprises; abundant liquidity in

the form of cash or debt; and potential valuation arbitrage with Western targets typically trading at lower valuation than publicly listed Chinese stocks.

McMahon: These are compelling drivers. Many of these have been a long time in the making, so it was only a matter of time until we saw the activity reflected in the M&A data. Chinese buyers are accessing established brands, new technologies and additional geographies through M&A. We believe these strategic motivations will only become stronger into the rest of 2016 and 2017.

CHINA OUTBOUND M&A ACTIVITY



Source: Dealogic.

HOW HAVE YOU PERSONALLY WITNESSED THE SHIFT IN THE BEHAVIOR OF POTENTIAL CHINESE BUYERS IN SELL-SIDE M&A PROCESSES OF NORTH AMERICAN OR EUROPEAN BASED TARGETS?

Siu: Chinese buyers have started demonstrating a higher level of confidence. They are increasingly willing to pay premium valuations upfront for quality Western businesses and 'trophy assets,' as well as take a long-term view and invest significantly in companies post-acquisition. With this confidence and increased experience they have

been more aggressive with their participation in Western M&A processes and processes involving highly attractive assets in other geographies.

Siu: We recently advised on the sale of Modern Metal, a Hong Kong based company and market leader in high-pressure aluminium die-casting, through a competitive auction process to JD Capital, one of the largest private equity firms in China. JD Capital recognized Modern Metal as a well-established platform upon which they can expand its global footprint via acquisitions of advanced industrial technology opportunities in the US and Europe. That was attractive to them, and they did not shy away from pursuing the target because it was cross-border.



Silver: Another example is our work advising British private equity firm 3i Group plc on its sale of Mayborn Group, the owner of award-winning global baby brand Tommee Tippee, to Shanghai Jahwa (Group) Co Ltd. In that deal, there were multiple interested potential buyers, from both North America and Asia. We progressed with the most serious Chinese buyer, Shanghai Jahwa (Group) Co Ltd, and structured the deal to minimize lengthy shareholder approvals.



GIVEN THE INCREASED PARTICIPATION OF CHINESE BUYERS IN WESTERN SELL-SIDE PROCESSES, DO YOU ADVISE YOUR NORTH AMERICAN OR EUROPEAN CLIENTS ANY DIFFERENTLY?

Silver: While I would not want to generalize too much about certain buyer groups, we do advise our sell-side clients to take certain steps to help Chinese buyers and bridge any potential gaps. Early senior-level contact between the parties is critical. The education and due diligence timeline can be longer for Chinese strategic buyers, so including adequate time for prospective buyers to build familiarity with the target is important in the M&A process.

McMahon: Deal certainty remains a concern for Western sellers when negotiating with Chinese buyers. Regulatory risk, particularly for larger transactions, will continue to receive significant regulatory scrutiny. Chinese buyers may need to compensate sellers with higher valuations in order to overcome seller concerns

around deal certainty. Nonetheless, there is no question we are seeing Chinese buyers be more sensitive to Western sellers concerns and more Chinese buyers are not only competing more effectively but winning Western style auctions with much greater frequency than even 12 months ago.

Siu: We also encourage Chinese buyers to hire experienced cross-border M&A advisors. While these buyers are becoming more accustomed to Western M&A processes, they are still well served by experienced advisors who can help them through due diligence as well as local M&A nuances.

HOW DO CHINESE BUYERS FINANCE M&A DEALS?

Siu: It really depends on the type of buyer. State-owned enterprises often receive support or financing from the Chinese government. Privately-owned companies are accessing funds through bank debt, IPOs or private placements. Private equity firms are raising funds from global investors.

Silver: On the Mayborn deal, we saw some hesitancy from UK banks to lend to Chinese private equity firms. We believe that this will change over time as more Chinese private equity firms successfully compete in outbound M&A and build working relationships with Western lenders.

WHERE DO YOU SEE THIS CHINA OUTBOUND M&A TREND HEADING?

McMahon: We could very well be in the early stages of a movement that will have a significant impact on the global M&A market. We see China outbound M&A accelerating for the balance of 2016 and into 2017.

Siu: The Chinese buyer universe is increasingly diverse and potential buyers are willing to take a relatively broad view on strategic rationale. We are seeing more types of buyers, whether strategic or private equity, and we are seeing investment across more sectors, from industrial and consumer to technology and services. Instead of just state-owned enterprises using M&A to secure natural resources, we are seeing privately-owned companies and Chinese private equity firms seriously invest in North America and Europe, especially in the middle-market.



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