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Cross-border M&A
Springboard to global growth

M&A
Institute

Executive summary

As companies seek increased competitiveness and growth in new geographies, cross-border Mergers and Acquisitions (M&A) has emerged as one way to quickly gain new market and customer access. Historical global M&A trends, along with macroeconomic, regulatory, and market dynamics, point to increasing cross-border deal volume. In fact, 2015 saw the most cross-border deals to date in any given year, and the Baker McKenzie Cross-border M&A Index remained at a sustained high of 222 in 2016 after peaking at an average of 272 in 2015. However, many companies are weighing the value of cross-border deals against “greenfield” investing or pursuing a joint venture to expand presence in a new market—a situation we call the “cross-border M&A conundrum.”

Advantages of cross-border M&A include expediting time to market, gaining access, scale, and brand recognition, and mitigating competitive moves. At the same time, companies are acknowledging the challenges posed by cross-border deals in terms of market assessment, regulatory evaluation, cultural fit, and deal structure evaluation.

To better understand the successes and pitfalls associated with cross-border deals, Deloitte conducted a survey of more than 500 client executives with cross-border M&A experience across regions, industries, and functions. The survey results provided insight and perspective on trends, which were then supplemented with Deloitte experience.

Through our research, we have identified three key themes in cross-border M&A:

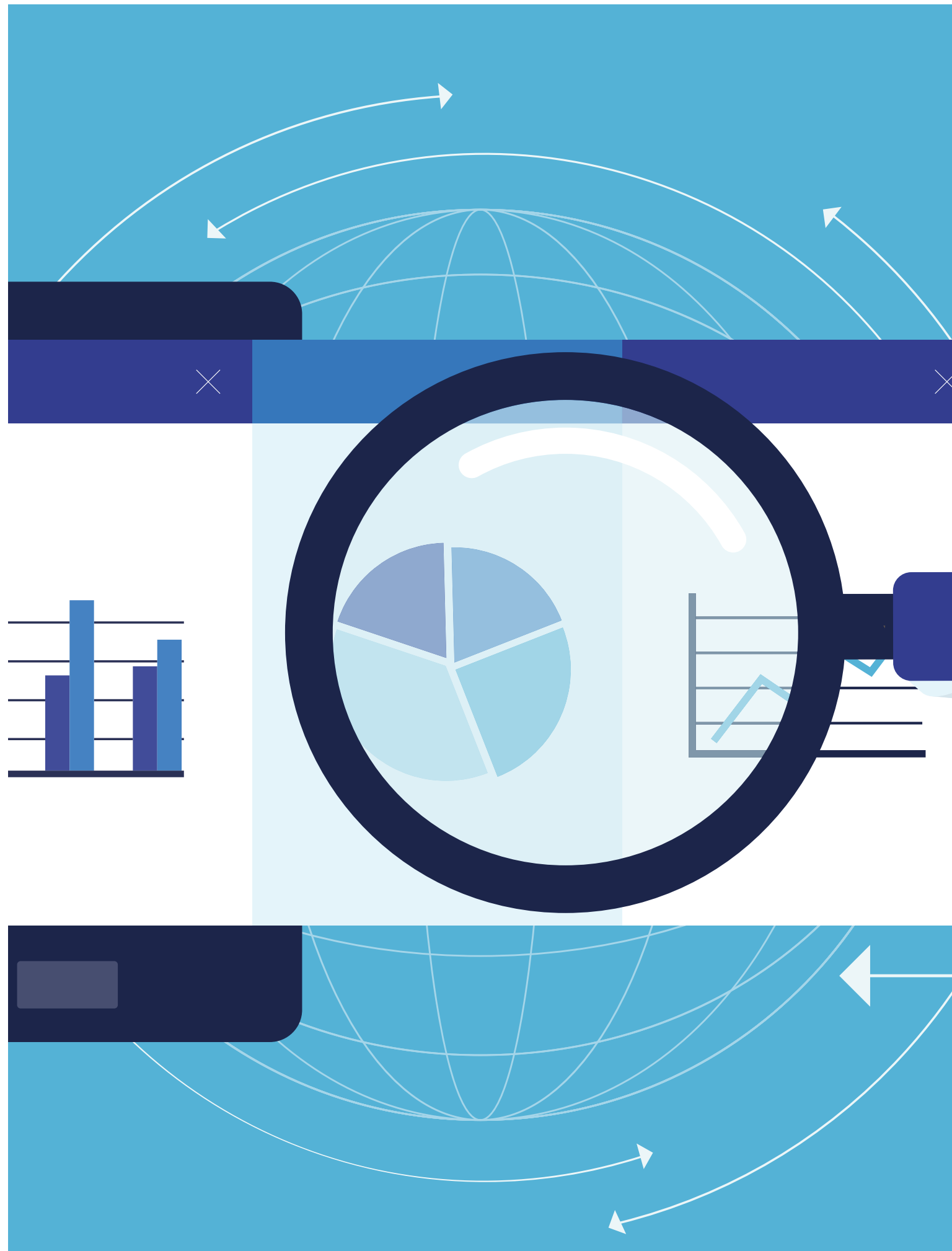
01. Stronger appetite for cross-border M&A in key deal corridors is primarily driven by revenue growth and access to new products and channels.

02. Commercial and operational diligence, along with a thorough understanding of tax, regulatory, and political risks, are imperative to cross-border deal success.

03. Early and focused integration planning has an outsize impact on overall deal success.

Based on our survey and lessons learned from Deloitte’s cross-border M&A experience, it is critical that deal thesis and objectives drive all phases of the M&A lifecycle from target screening to due diligence and integration, especially for cross-border deals. Organizations need to integrate pre-deal due diligence with pre-close planning activities to prevent handoff misses, define the overall integration approach, and plan for achieving both legal close and end-state goals.

This article reviews cross-border M&A trends; identifies potential challenges to cross-border deals; offers insights into how companies can manage these complexities; and shows that cross-border M&A may provide a better opportunity for growth than a greenfield investment.



Introduction

The globalization imperative comes with a host of opportunities and risks. Cross-border M&A has emerged as a key tool in pursuit of new markets, technologies, capabilities, and products in order to drive growth, innovation, and transformation. As cross-border deal activity continues, companies will need to weigh the risks and rewards of engaging in these ventures against making greenfield investments. Further, companies will need to display agility and preparedness to cash in on opportunistic deals arising from emerging economic and political

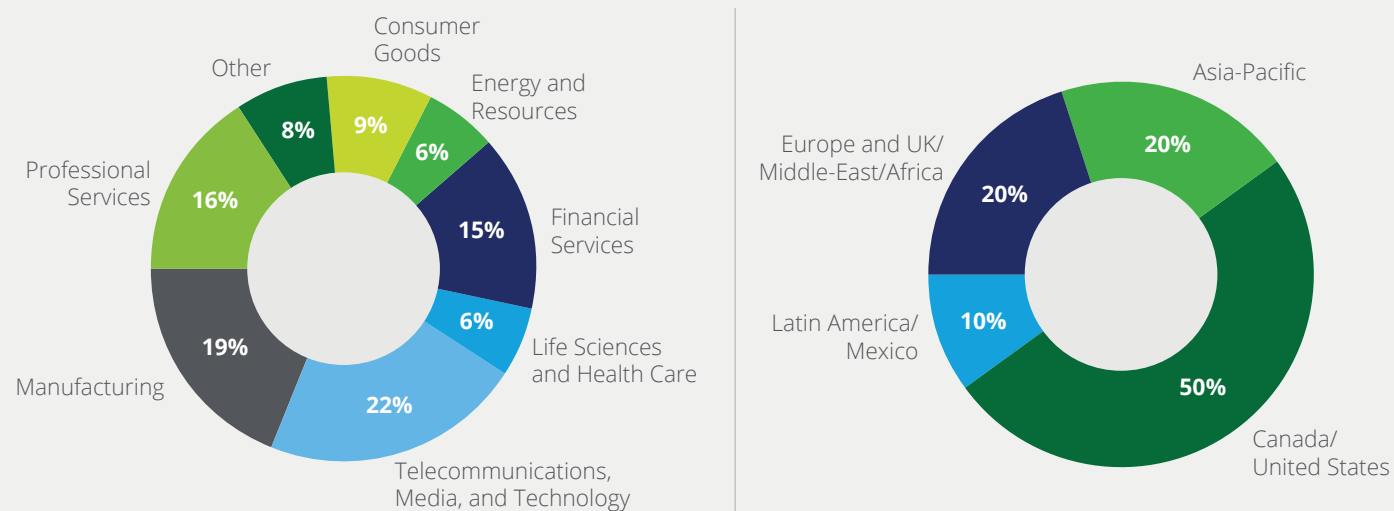
events like “Brexit”, the recent US election, and the referendum in Italy. While it is too soon to estimate and/or quantify the impact on M&A from such events, there is no question that the status quo will be challenged to a significant degree.

What are the issues companies must prepare for when engaging in cross-border deals? The following analysis delves into the success rate of cross-border deals across geographies and industries, and offers our observations on the future of cross-border M&A.

Survey approach

Deloitte conducted a survey of executives with previous experience undertaking cross-border deals. We gathered insights from nearly 500 executives across regions and industries, and supplemented it with our experiences and additional research. All of the respondents reported personal experience with their companies’ mergers or acquisitions, with the majority (69 percent) indicating extensive experience (i.e., participation in three or more deals in the past five years).

Figure 1: Respondents’ primary industry and region by percentage



Source: Deloitte analysis through primary survey. Value might not add up to 100 percent because respondents could select more than one answer.

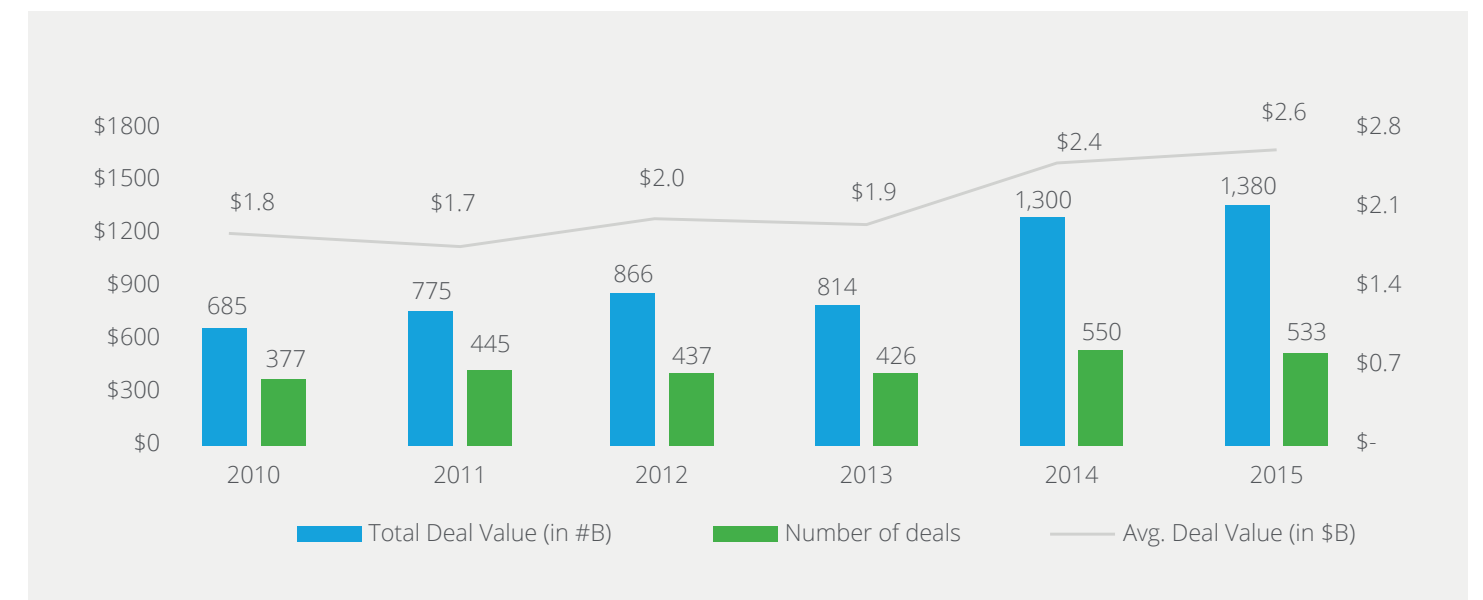
Strong appetite for cross-border M&A

Stronger appetite for cross-border M&A in key deal corridors is primarily driven by revenue growth, access to new products, and channels

Cross-border M&A in 2015 set records, with announced deal value exceeding \$1.38 trillion¹ and comprising more than 31 percent of the year’s total M&A deal value.² The period between 2010 and 2015 witnessed cross-border M&A deals worth \$5.8 trillion, growing at a combined annual growth rate (CAGR) of 15 percent (Figure 2).³ While this growth has plateaued to some extent in 2016—

Baker McKenzie’s cross-border M&A index was at 238 in Q3 2016, down 10 percent compared to Q3 2015—interest in cross-border M&A remains strong. As further evidence of this trend, the number of cross-border M&A deals as a percentage of total deals increased from approximately 27 percent to 31 percent over the past two years.⁴

Figure 2: Cross-border M&A deal activity 2010-2015



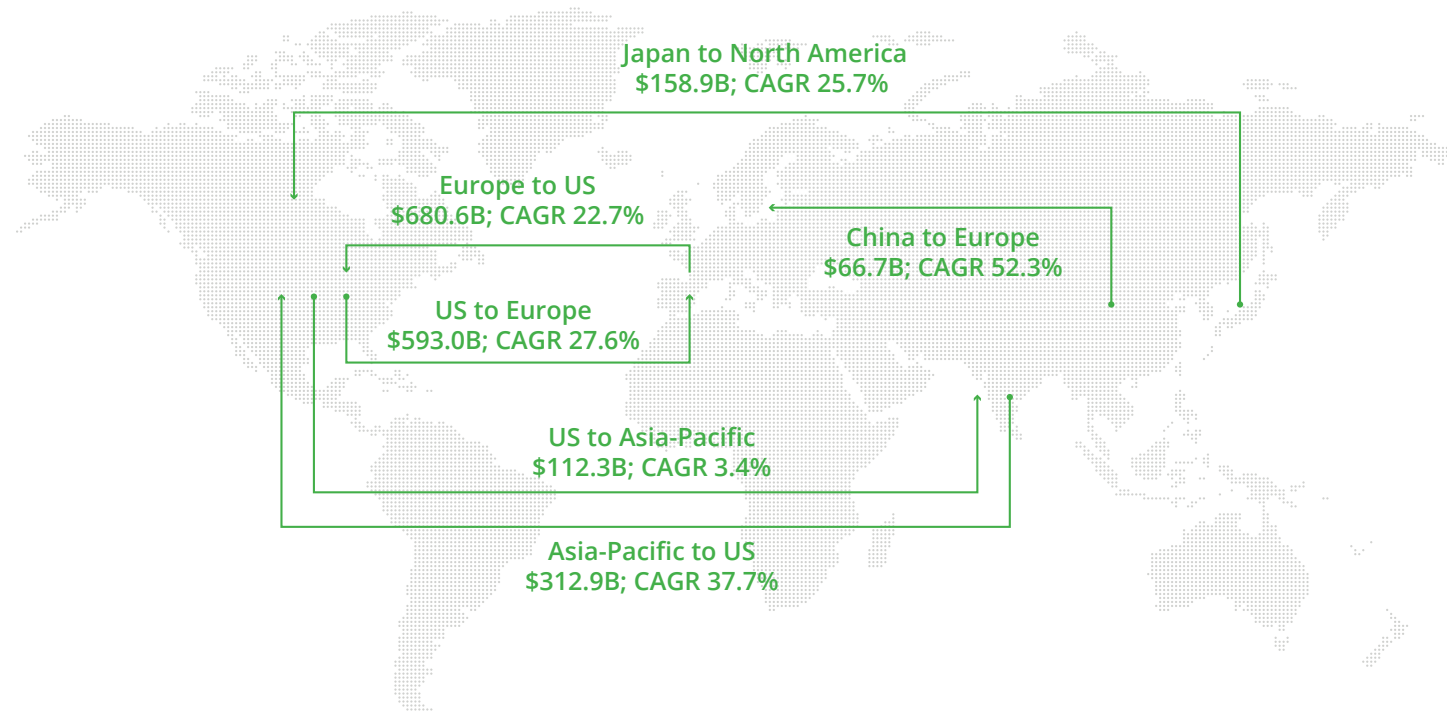
The trend toward larger deals continued from 2015 into 2016, as evidenced by recent big-ticket transactions. The top three investors in the first quarter

of 2016 were China, Canada, and the US, and the top three investment destinations were the US, Switzerland, and the United Kingdom (UK).⁵

A sense of uncertainty was introduced into international M&A markets by the result of the Brexit referendum in June 2016. Deloitte’s analysis⁶ suggests that many dealmakers are in a “wait and see” mode, approaching the post-Brexit world in a rational and considered way. However, M&A appetite has traditionally been driven by intrinsic factors (such as valuation and growth prospects of the asset) in addition to external factors like overall business confidence and stable

macro environment. Following Britain’s decision to exit the EU, overseas acquirers may likely be attracted to British assets, which are now available at cheaper valuations driven by the depreciation of the pound. A snap poll conducted by Deloitte indicates far greater numbers are considering incremental M&A opportunities from Brexit than those looking away from the UK as a target destination.

Figure 3: Cross-border M&A by target regions, 2010 to 2015⁷

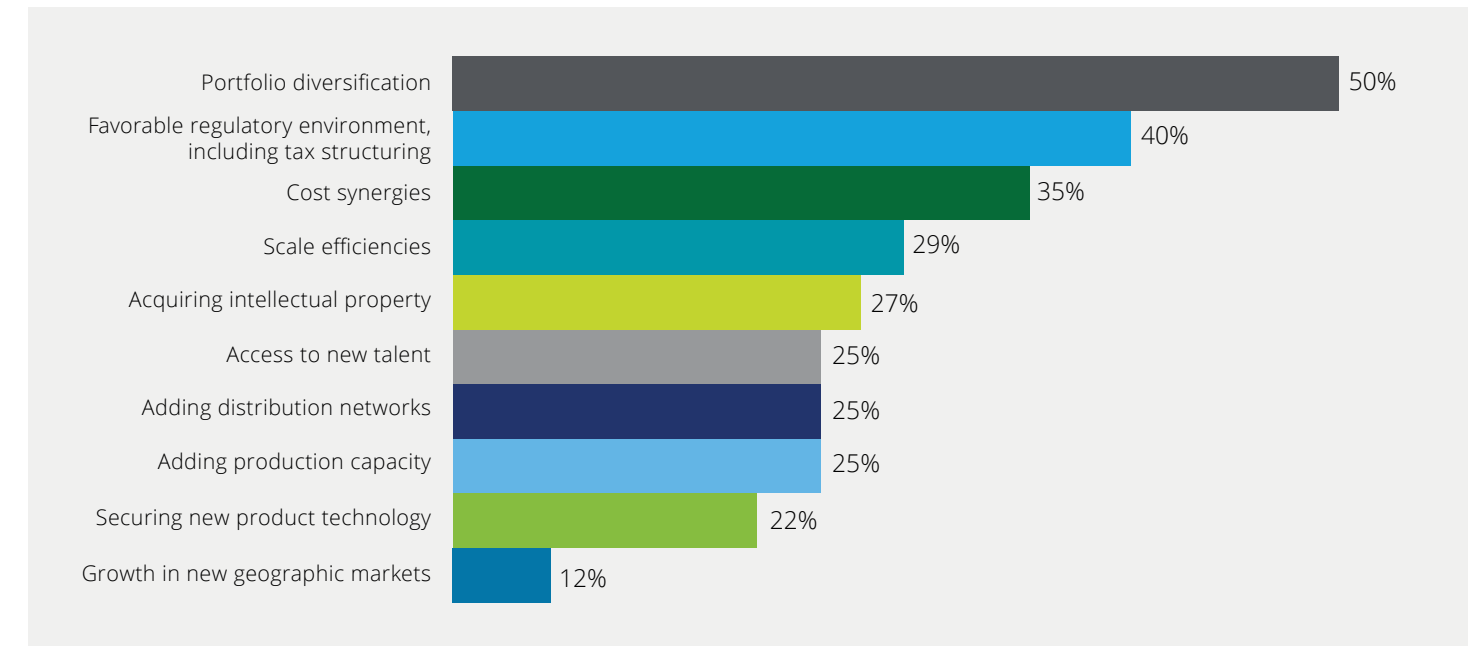


Region	Outbound deals (% of total deal value)	Inbound deals (% of total deal value)
North America	C&IP and TMT (35%, 21%)	C&IP and TMT (29%, 21%)
Europe	C&IP and E&R (39%, 20%)	C&IP and TMT (41%, 19%)
Asia-Pacific	E&R and C&IP (32%, 28%)	C&IP and E&R (34%, 30%)
South America	C&IP and FSI (35%, 28%)	E&R and C&IP (38%, 24%)
Africa/Middle-East	LSHC and C&IP (35%, 27%)	C&IP and TMT (38%, 27%)

Regarding rationale for the deal, survey respondents identified a number of drivers that create a compelling business case for cross-border M&A (Figure 4). These include saturation or slowdown in core markets and need for diversification; regulatory uncertainty in home markets (e.g., Latin American—LATAM—outbound) and high repatriation costs of overseas earnings (e.g., US tax inversion outbound deals); technology and productivity

enhancement synergies (e.g., APAC inbound deals, North America inbound deals). Note, however, that recent US Treasury rules would restrict the practice of earnings stripping often undertaken following an inversion and other related party debt structures.

Figure 4: Top strategic deal objectives



Source: Deloitte analysis through primary survey. Value might not add up to 100 percent because respondents could select more than one answer.

Not surprisingly, our survey shows that deals driven by technology and productivity enhancement are more common in industries that place a premium on innovation, such as technology, media and telecom (TMT), and life sciences

& health care (LSHC). Specific drivers include high US technology company valuations and an increased focus on acquiring drug pipelines versus organic research and development.

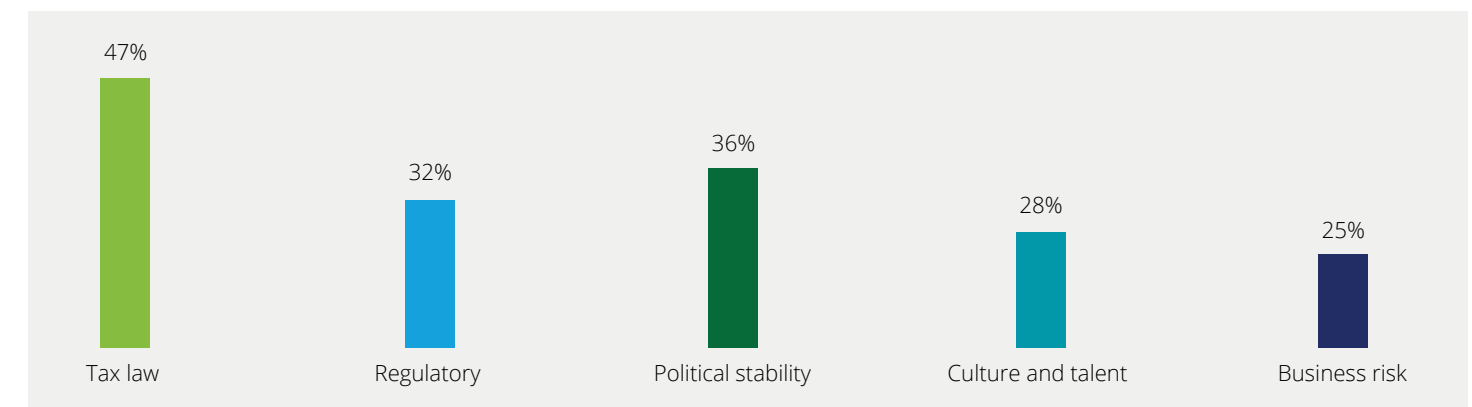
Unique due diligence considerations

Commercial and operational diligence—along with a thorough understanding of tax, regulatory, and political risks—are imperative to cross-border deal success

Acquiring companies may have to recalibrate their perceptions of risk and their traditional due diligence process to address both common and unique risk factors that accompany cross-border M&A transactions. The deal team will need to focus on common risk factors such as national and regional tax laws;

the availability, accuracy, and reliability of the target company's financial information; the country's political stability; and the target's compliance with the US Foreign Corrupt Practices Act (FCPA) and similar anti-bribery and anti-money laundering (AML) regulations (Figure 5).

Figure 5: Top risk factors for cross-border M&A deals



Source: Deloitte analysis through primary survey. Value might not add up to 100 percent because respondents could select more than one answer.

A company can also adjust its due diligence approach to identify and address a target's unique mix of geographic and industry risk factors. To illustrate, regulatory complexities in Asia-Pacific (ACPA) countries may discourage EMEA and Americas investors that are accustomed to a more business-friendly environment. The cautious approach of certain acquirers

in the immediate aftermath of Brexit, the Italian referendum, and the US elections is another case in point as overseas acquirers are expected to lay greater emphasis on pre-deal diligence, especially in areas such as forex risk and trade agreements. Similarly, political stability is a top risk concern from LATAM companies (Brazil, Venezuela).

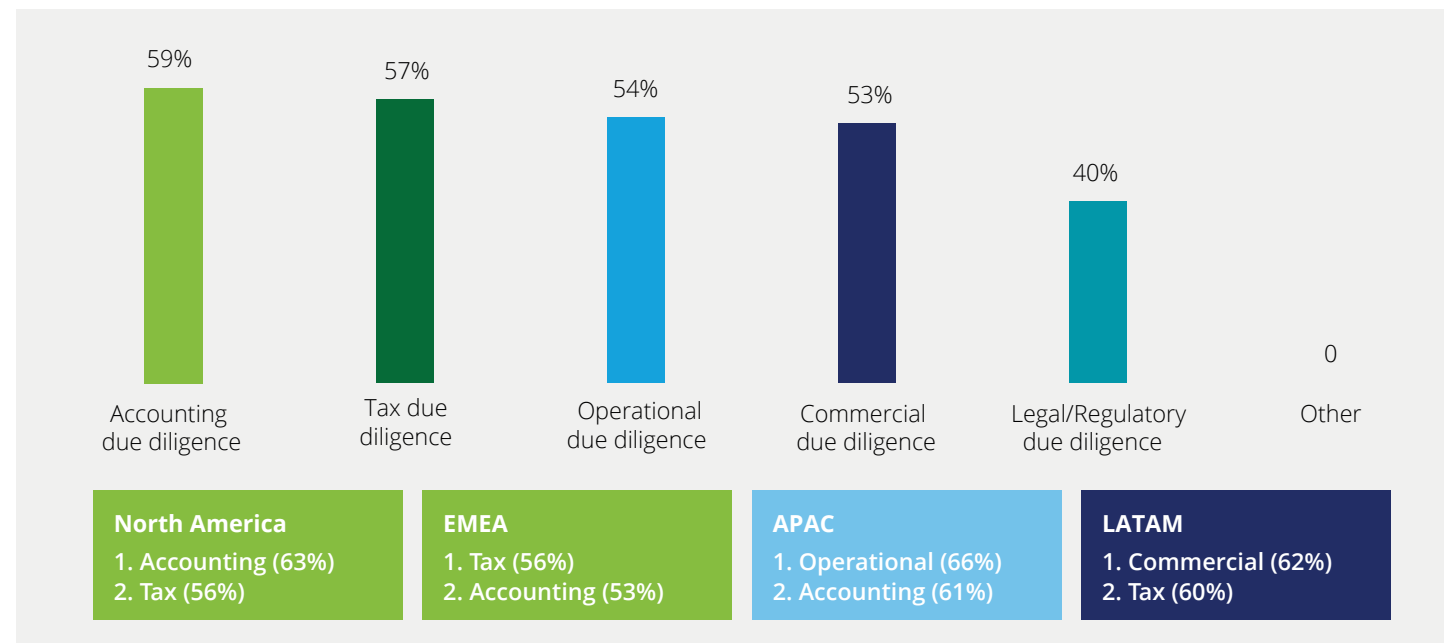


From Deloitte’s experience, challenges that add complexity during the target identification and transaction execution phase may include sectoral caps for foreign investment, lack of reliable information on the target, different official languages, disclosure and reporting requirements, coverage of data aggregators, complicated tax structures, cultural and language barriers, multiple levels of complex legal processes, and divergent expectations on acquisition price. Similarly, navigating stringent labor laws and gaining approval from work

councils may significantly lengthen deal timelines for European transactions. Survey respondents judged research from a consultancy and third-party advisory support to be the most helpful information for evaluation of potential targets, especially acquirers with headquarters in APAC.

Survey respondents assigned significant importance to reliable accounting, tax, operational, commercial, and legal/regulatory due diligence when transacting cross-border (Figure 6).

Figure 6: Critical aspects of due diligence



Source: Deloitte Analysis through primary survey

Value might not add up to 100% because respondents could select more than one answer

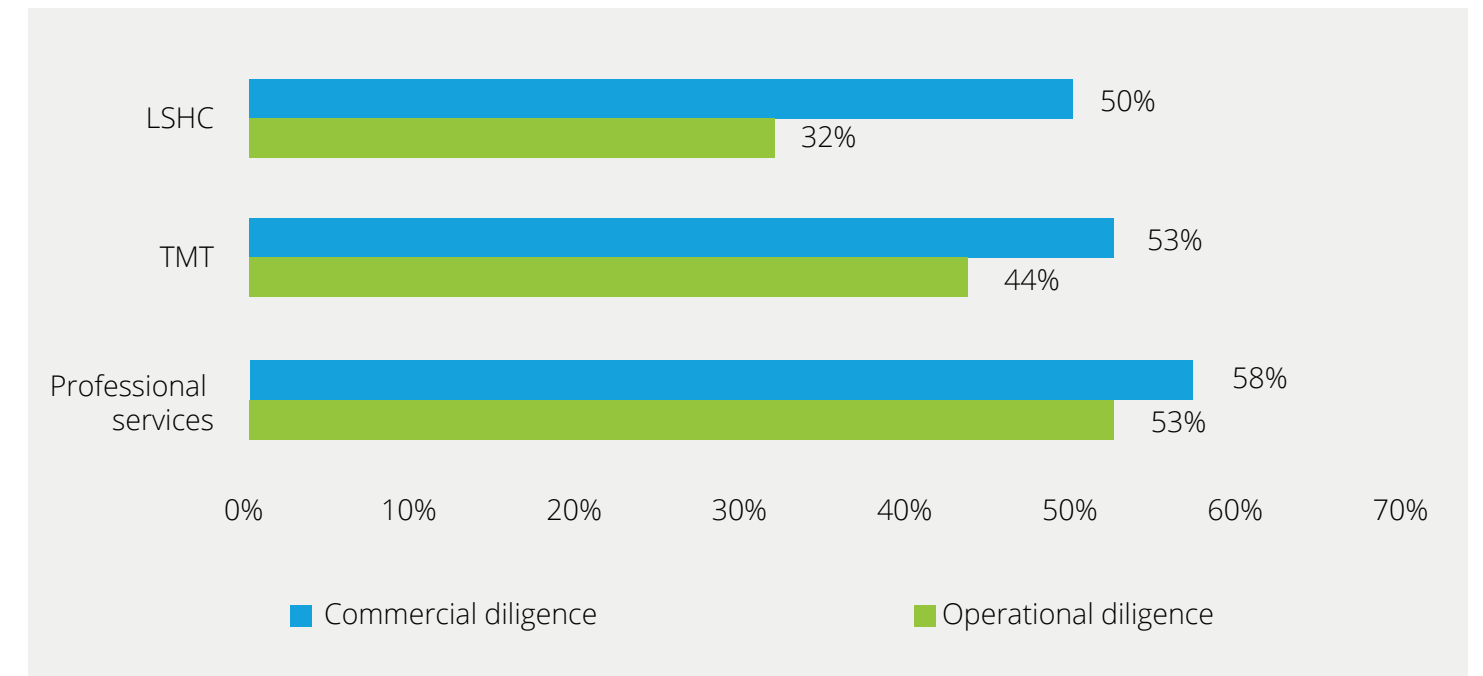
Our experience with multiple cross-border deals suggests that companies should conduct due diligence early in the deal cycle to identify common pitfalls and integrate pre-deal due diligence with pre-close planning activities to prevent handoff misses. In addition to identifying potential deal-breakers, the due diligence process is

extremely important when assessing the buyer’s deal rationale and risk mitigation plan. From an industry perspective, LSHC and TMT survey respondents said they place greater emphasis on commercial rather than operational due diligence (Figure 7), presumably in order to accelerate topline growth.

Interestingly, the survey shows that acquirers from the North America and APAC regions rated commercial due diligence as a key determinant when making a purchase decision (more than 50 percent of respondents); however, these respondents placed more emphasis on extracting cost synergies from the deal, as evidenced by the higher importance attached

to operational findings. Additionally, executives in financial services and insurance (FSI) and manufacturing overwhelmingly selected accounting and tax due diligence as most important, while those in the heavily regulated energy and resources (E&R) industry leaned toward legal/regulatory due diligence.

Figure 7: Due diligence priorities by industry and region



Source: Deloitte Analysis through primary survey

When further questioned about which deal structure, in their experience, proved most effective in past deals, the majority of respondents identified either full acquisitions (63 percent) or majority stake ownership (51 percent). Sixty-nine percent of survey respondents did not view joint ventures (JVs) favorably; those working in TMT and manufacturing indicated the highest level of dissatisfaction with this structure, likely due to these industries’ unique intellectual property considerations. Respondents

attributed their dissatisfaction with JVs primarily due to a lack of strategic goal alignment among the JV partners. In our experience, misalignment can occur due to the absence of a detailed business plan, an ambiguous operating and governance model, mismatch in capital injection expectation versus growth, and unclear boundaries between JVs and the core business. In addition, local partners often lack the operating capital of their larger multinational counterparts, which can cause JVs to miss growth expectations.

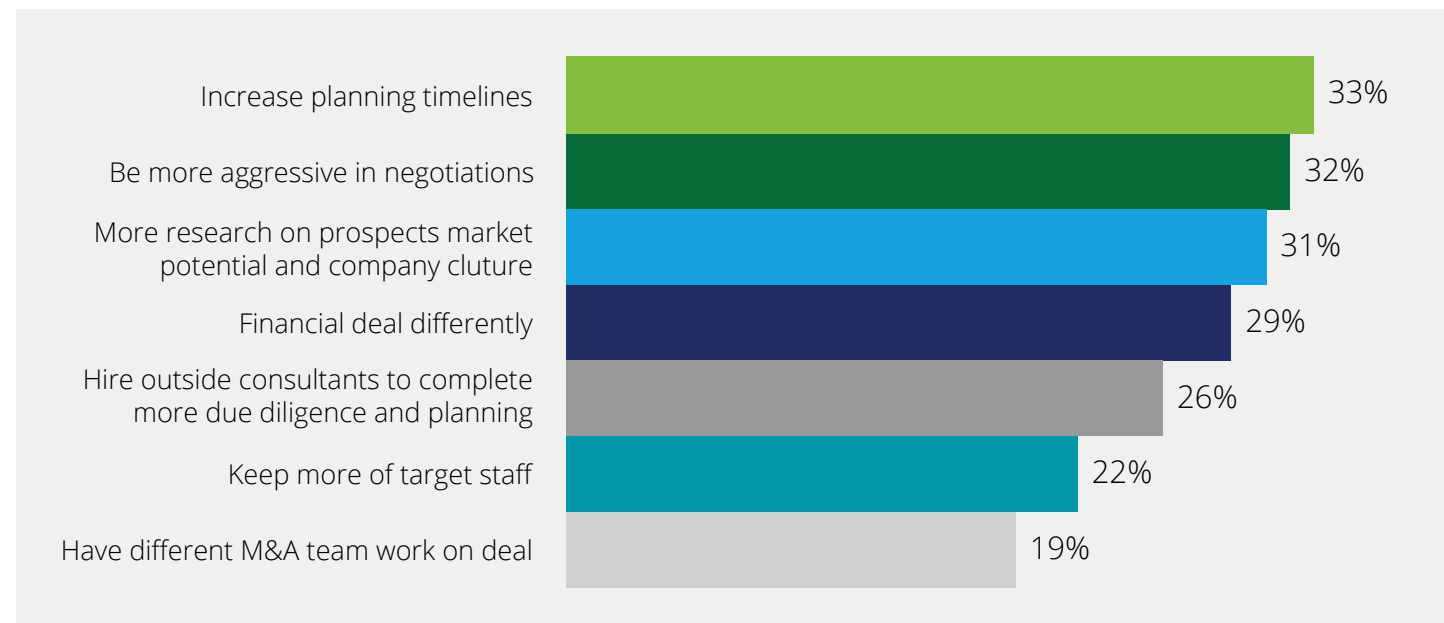
The critical importance of integration planning

Early and focused integration planning has an outsize impact on overall deal success

When reflecting on their regrets from prior cross-border M&A deals and opportunities for improvement, 33 percent of executives said they want to place more emphasis on comprehensive pre-and post-deal planning; 32 percent want to be more aggressive in negotiations; and 31 percent want to conduct more research on a target's market potential

and company culture (Figure 8). Based on Deloitte's experience with a \$5B cross-border transaction in the consumer products space, pre-deal planning through constant interaction between the buyer and target, and a thorough analysis of competitively sensitive information undertaken in clean rooms were all key in expediting post-close integration.

Figure 8: Opportunities for improvement in future cross-border M&A deals



Source: Deloitte Analysis through primary survey

From a regional perspective, respondents in LATAM and APAC shared similar regrets around integration and initial target research. 52 percent of LATAM respondents and 43 percent of APAC respondents desired a more complete integration plan for future deals. According to survey respondents, 91 percent of the deals they executed in the previous five years were all or mostly successful, and respondents indicated that their prior experiences make them more likely to pursue future cross-border deals. Note that executives in LSHC (29 percent) were the only ones to significantly indicate past experience as a negative influence. When asked about the likelihood of pursuing deals

in the next two years, 92 percent of executives responded positively. However, those in some industries, such as Professional Services and Life Sciences & Health Care, have reservations about pursuing future cross-border deals, likely due to the country-specific nature of drug- and hospital-related regulations and operations. Irrespective of region or industry, respondents indicated that their successful experiences with prior cross-border deals will embolden them to pursue additional deals in the future. Overall, the future of cross-border M&A remains bright, and the number of deals will likely continue to grow as the global marketplace becomes more and more borderless.

Our perspectives for executives considering cross-border M&A

Companies can achieve substantial financial, market, and competitive value through cross-border M&A, and executives should plan ahead, conduct thorough due diligence, and closely manage pre- and post-deal execution. Based on our M&A experience, we have identified a handful of leading practices that executives and deal members should consider:

- Ensure that the deal thesis and deal objectives drive all phases of the M&A lifecycle, from target selection to due diligence to execution and to integration
- Adapt the deal methodology and playbook to specific deal circumstances to pre-empt global M&A challenges

- Integrate pre-deal due diligence with pre-close planning activities to prevent handoff misses
- Structure the deal so it has the best chance of meeting its objectives—knowing that full integration may not always be the right choice
- Define the overall integration scope, approach, and plan for achieving both Day 1 and end-state goals
- Organize a global integration program that has representation from both acquirer and target around key work streams and regions/countries
- Focus efforts on effectively planning pre- and post-close integration in detail, with dependencies and critical path clearly outlined

Conclusion

Companies are becoming bolder in their use of cross-border M&A to ignite growth and/or acquire critical capabilities in an increasingly competitive, global marketplace. Cross-border deals can be a springboard to help companies bolster their technological relevance, operational competency, and geographical diversity.

Our survey indicates that firms are becoming more competent and experienced in cross-border acquisitions—acknowledging the importance of comprehensive planning, tapping the expertise of external advisors, using thorough due diligence—and are thus able to deliver on their deal objectives. However, executives remain cautious as they navigate the murky waters of global economic and political instability.

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End Notes

1. Deloitte Research & Analysis, Based on 2010-2015 data from MergerMarket (Cross-Border M&A deals with value >\$500 million are captured; deals which have lapsed/withdrawn have not been considered)
2. J.P. Morgan, "2016 M&A Global Outlook," www.jpmorgan.com/country/US/EN/insights/maglobaloutlook
3. Deloitte Research & Analysis, Based on 2010-2015 data from MergerMarket
4. J.P. Morgan, "2016 M&A Global Outlook", www.jpmorgan.com/country/US/EN/insights/maglobaloutlook
5. Deloitte Research & Analysis, Based on data from Thomson Reuters
6. Deloitte Research & Analysis, Detailed in "Plotting a new course: The impact of Brexit on M&A activity"
7. Deloitte Research & Analysis, Based on 2010-2015 data from MergerMarket

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