M&A in Europe in 2022

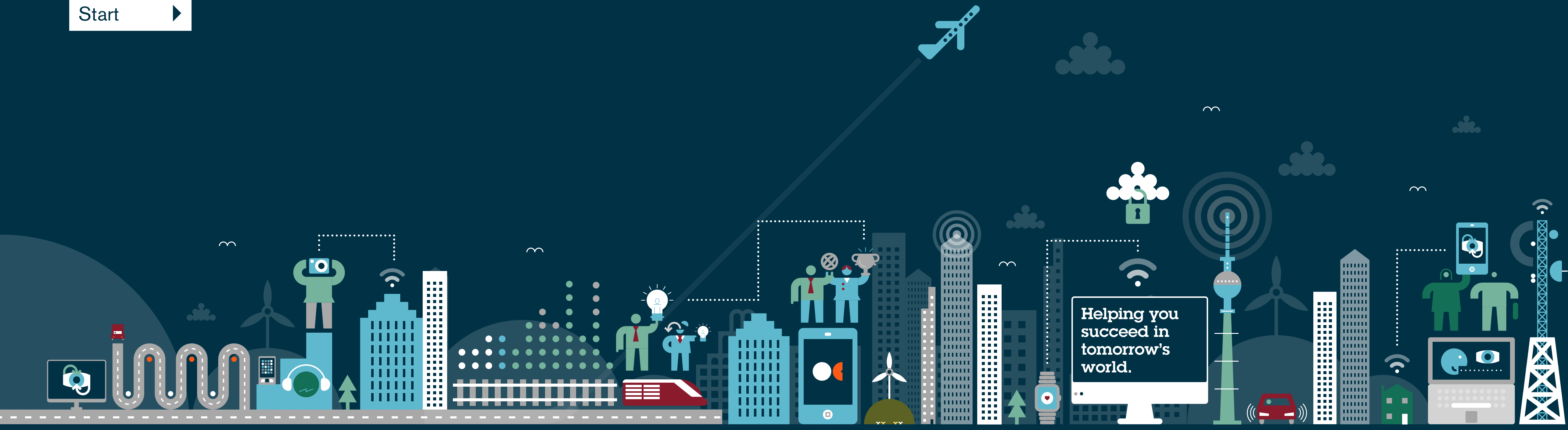
Outlook report and deal terms analysis

Osborne Clarke

2022 was expected to be stellar, but world events and regulatory developments have rendered the economic climate more volatile as the year progresses

October 2022

Start



2021 – a record breaking year

2021 was a record-breaking year for mergers and acquisitions (M&A) in Europe. Both deal volumes and values grew strongly. According to financial markets data provider Refinitiv, in its Insight "Dealmakers ring out 2021 as the year of M&A", Europe saw a 46 percent increase year on year to reach €1.37trn in deal value. Fears that the Covid-19 pandemic would lead to a sustained downturn in M&A activity were relatively short-lived and the European economies began to heal.

Growth was fuelled by tech and financial sector M&A, and private equity sponsors ready to spend after keeping large stores cash unspent in the previous year. According to Invest Europe's research report "Investing in Europe: Private Equity Activity 2021", Private equity & venture capital firms invested €138 billion into European companies in 2021, a 51% increase over 2020. Interest rates remained historically low, government support packages remained partially in place and the stock markets rebounded, giving confidence to strategic and financial buyers alike.

The pandemic accelerated the digitalisation of deal-making processes, necessitating the acceptance of virtual meetings. Many European jurisdictions brought in legislative changes to facilitate contactless arrangements, including digital filings and the use of electronic signatures, and due diligence, integration, contract review and deal negotiation saw considerable leaps forwards in technological solutions. Consequently, the deal-making experience improved as transactions could be completed more quickly and smoothly.

Greg Leyshon
Partner, UK
T +44 20 7105 7587
greg.leyshon@osborneclarke.com

Sarah Lunn
Senior Knowledge Lawyer, UK
T +44 118 925 2044
sarah.lunn@osborneclarke.com

2022 – predicted to be another stellar year

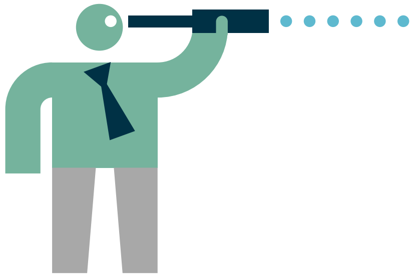
When 2022 dawned, it was anticipated that it would be another stellar year for M&A. Germany (and even more so combined with Austria and Switzerland as the DACH region – the central European region of German-speaking nations) was expected to see the highest growth in M&A deal activity, overtaking the UK and Ireland as the most active M&A markets.

But the economic climate changed and became more volatile and more fragile in the first few months of the year. As reported by ION Analytics in its article "M&A Highlights First Half 2022: Down at halftime", the region saw a total of €602bn spent across 5,493 deals. This represents a 12.7% decline versus the opening half of 2021 (€688bn), and a 28.4% fall in comparison to 2H21 (€838bn). This included a rebound in activity in Q2 (activity plummeted in February when Russia invaded Ukraine) and some big-ticket deals including Blackstone and Benetton family's takeover bid for the Italian infrastructure group Atlantia which has an enterprise value of approximately €54bn.

There were fewer cross-border deals – according to ION Analytics, inbound M&A in EMEA retreated by 37.4% by value versus 1H21 (€199bn to €124bn) in the first six months of the year. Some acquirers are busy focusing on integrating the businesses they bought in 2021 so have little bandwidth to consider new targets.

There has also been a significant downturn already in larger M&A.

Comparisons with 2020 and 2021 should however be treated with some caution – valuations were extremely high and the pandemic created a very sharp decline followed by a sharp rise in M&A activity.



Which factors have increased market volatility?

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- The war in Ukraine, sanctions on Russia and Belarus (though neither is an economic powerhouse), and the related humanitarian and refugee crisis (not least in Poland); the imports of certain goods (for example, wheat, metals and oil and gas) has been impacted, as has freight across the continent.
- Rising oil, gas and energy costs due to low gas storage levels, high European Union carbon prices, fewer liquefied natural gas tanker deliveries due to higher demand from Asia, lower than normal Russian gas supplies following international sanctions and infrastructure outages.
- Supply chain disruption, increased logistics and transportation costs and labour shortages caused by trade and geo-political tensions), the war in Ukraine, the Covid-19 pandemic, Brexit, increased energy prices impacting production costs and China's zero-Covid policy creating supply chain backlogs. Disruption is notable in the energy, raw materials, semiconductor and microchip markets which impacts a wide range of sectors.
- The Covid-19 pandemic – while vaccinations and newer variants are generally leading to milder acute infections and fewer deaths, there remains the practical risk of illness of employees, decreased bandwidth and backlogs of state institutions and the risk of a more serious variant or resurgence of the virus as vaccine protection wanes. Further lockdowns, for now at least, appear unlikely but taxes are increasing to pay for the pandemic.
- Other geopolitical tensions and increasing cyberattacks by nation states and criminals.
- The rapidly growing urgency to deal with the climate emergency (and Net Zero targets agreed at COP26).
- Inflation rates growing, the cost-of-living crisis and weakened consumer spending power and confidence with wages not keeping pace with inflation. The Eurozone annual inflation rate was 8.1% in May 2022, up from 7.4% in April. A year earlier, the rate was only 2.0%. European Union annual inflation was 8.8% in May 2022, up from 8.1% in April. Inflation in Poland was 12.8% and 10.2% and 9.9% in the Netherlands and Belgium respectively in May 2022 (Eurostat Euroindicators 17 June 2022: Annual inflation up to 8.1% in the euro area). Many economists are pricing in a recession for the Eurozone either later this year or in 2023. In the UK, where inflation is expected to reach 11% later this year, the situation has been worsened by Brexit. Bloomberg has reported ("Brexit's Legacy Is Hotter UK Inflation Risk for Years Ahead") that *"Even as price pressures start to fade elsewhere, [Wall Street banks] say UK inflation will be higher-than-normal because of immigration controls and supply chain disruption,"* and that, *"Trade barriers have driven a 6% increase in UK food prices, according to a report from the London School of Economics."*

Which factors have increased market volatility?

- Higher borrowing costs and debt financing conditions tightening – central banks are increasing interest rates to try to keep inflation in check, in turn, there is an increasing pressure on returns on investments. That said, interest rates currently remain at relatively low levels.
- Lower market capitalisations of publicly listed companies.
- Weakening currencies for those countries such as Poland outside of the Eurozone; the zloty has lost over 16% of its value against the dollar and the euro so far this year. Great British pound sterling has also lost value against the dollar and the euro. A weak currency will have a negative impact on imports, but equally a positive impact on exports for some businesses.
- Governmental instability or regime change – French presidential and legislative elections (For the first time since 1997, the incumbent president of France does not have an absolute majority in Parliament), a new German Chancellor and governing “traffic light” coalition, the Swedish general election in September, a minority government in Poland, political fragmentation in Spain, a change of leader of the UK’s governing party and instability in Italy after the recent resignation of their prime minister and subsequent change of government following an election.
- A increasingly inward-looking China and a reduction in overseas investments.

What about regulatory changes negatively impacting the market?

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Foreign direct investment controls

European countries have recently been moving to enact or bolster their foreign direct investment (FDI) control legislation on national security grounds. The drive, in part, was born out of the pandemic and a need to protect key supplies and industries to support the fight against Covid-19 and countries becoming more hawkish in the face of geo-political tensions and threats, not least from China.

There was already a trend towards stronger FDI controls after the coming into effect of EU Regulation 2019/452 (the FDI Regulation), which was adopted in March 2019 and has been applied since October 2020. The FDI Regulation does not create an EU-level FDI screening mechanism but sets out minimum requirements for EU Member States' FDI screening mechanisms and a mechanism for coordinating FDI reviews. The duration of national FDI screening processes has increased as Member States are obliged to give the European Commission's opinion and other Member States' comments due consideration.

The Foreign Trade Act (*Aussenwirtschaftsgesetz*) and the Foreign Trade Ordinance (*Aussenwirtschaftsverordnung* (AWV)) provide for the review of foreign direct investments into German companies. On 27 April 2021, the German government adopted the 17th Regulation for the AWV. The regulation, which came into force on 1 May 2021 is a major overhaul of Germany's foreign direct investment screening regime. The amendments will significantly increase the scope of acquisitions that must be notified to and require clearance by the German Ministry for Economic Affairs and Energy.

France has significantly strengthened its FDI control laws over the last few years, not least through the Pacte Law of 22 May 2019 and measures adopted in reaction to the pandemic, broadening its scope for pre-completion authorisations and allowing severe sanctions in case of non-compliance. Action taken in 2020 in response to the onset of the pandemic, to reduce of the threshold of control from 25% to 10% of voting rights for non-European investments in listed companies, applies until 31 December 2022. Control is defined differently for unlisted companies, but the sensitive sectors defined in law apply regardless of whether the French target is listed or not.

In Italy, the supplemental provisions to the long-established, so-called "golden power" rules, which were enacted during the pandemic with the aim of imposing prior clearance with the government before non-Italian entities could complete the acquisition of Italian companies operating in a broad number of industries deemed "strategic" have been confirmed rather than cancelled, and the golden power rules further strengthened in March 2022.

In Poland, FDI control is regulated under the Act of 24 July 2015 on the Control of Certain Investments. It was amended during the pandemic to widen its scope and Poland has extended those controls until mid-2025.

What about regulatory changes negatively impacting the market?

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Spain brought in modifications to existing FDI control legislation (Law 19/2003 of 4 July on the Legal System of Transfers of Capital and of Economic Transactions with Foreign Countries) during the pandemic. Its enhanced powers which suspended liberalisation of investments by EU/EFTA investors currently last until the end of 2022. There are some issues with the interpretation of existing legislation and so the parties to a transaction often adopt a conservative position and request authorisation which can add months to a deal timetable. As a consequence, there is currently a draft regulation that aims to bring clarification.

On 1 January 2021, an amended version of the Swedish Security Act (SFS 2018:585) entered into force. The amendment serves to protect infrastructure of a potentially sensitive nature for Sweden's security in connection with transfers of the infrastructure.

On 17 May 2022, the Cross-Sector Foreign Direct Investment Screening Act (*Wet veiligheidstoets investeringen, fusies en overnames*) was adopted by the Dutch Senate. The Act will serve as a review mechanism for investments that could pose a risk to the national security of the Netherlands. The implementation date of the new regime has yet to be set by royal decree.

In Belgium, a legislative proposal to introduce a broad FDI screening mechanism has been pending in Parliament since 2021. In June 2022, the governments of Belgium's nine federated entities agreed on the main outstanding element of the new screening mechanism, being the cooperation agreement that structures how the different governments can provide feedback on foreign investments that are notified to the new central screening commission. The screening mechanism is expected to enter into force on 1 July 2023, but further delays in the Parliamentary process might occur.

But FDI control is not the only area of increased regulation.

Competition regulation

On 30 June 2022, the EU co-legislators (the European Parliament and the Council) agreed on a regulation to control foreign subsidies that distort the EU internal market (Foreign Subsidies Regulation or FSR). The FSR, which is expected to enter into force by mid-2023, will affect companies engaging in M&A and joint ventures in the EU that have received financial contributions from non-EU governments or non-EU State-owned companies.

The German Digitalisation Act, which came into force on 19 January 2021, widens German competition law to tackle presumed enforcement challenges in the digital economy but on a positive note raised merger control thresholds across all industries. in order to relieve mid-sized companies from notifying economically insignificant transactions.

Regulators (including those overseeing merger control) have tightened up their review and scrutiny of transactions using their existing powers, increasing the risk of challenge.

Technology assets are in the firing line. Competition authorities (for example, in the EU, UK, and Germany) are scrutinising technology transactions aggressively.

What about regulatory changes negatively impacting the market?

Regulators are being more bullish in their assertion of jurisdiction. The European Commission has published new guidance (Article 22 Guidance) on the application of the referral mechanism set out in Article 22 of the EU Merger Regulation allowing for mergers falling below national merger thresholds to be referred to it. The reason for this change is to catch transactions that would not otherwise have been subject to merger review, particularly so-called "killer acquisitions" which involve targets that do not yet have sizeable revenues. The Article 22 Guidance singles out digital and pharma/biotech as sectors in which potentially anti-competitive mergers have escaped scrutiny, but it also permits the referral for transactions in any sector.

As a result of Brexit, some acquirers now face potential parallel EU and UK competition investigations, where the merger satisfies the jurisdictional thresholds in the EU Merger Regulation and the UK's Enterprise Act 2002.

Purchasers are increasingly requested to make "hell or high water" commitments and other undertakings in connection with the issuance of clearances (for example, to protect jobs and industrial capabilities).

With the goal posts moving, there is increased uncertainty as to the deliverability of transactions; this will continue until new regulatory regimes or policies become more established. There is some evidence that US and other overseas buyers are looking closer to home for acquisition targets to avoid the regulatory friction of European deals.

Is a slowdown on the way in the second half of 2022?

In its article "EMEA M&A: A New World with New Questions", Intralinks has predicted a decrease of 10-15 percent in deal volume in EMEA beginning at the end of Q3.

PWC's "Global Industry Trends report: 2022 Mid-Year Update" forecasts that *"Looking to the second half of the year, dealmakers are facing arguably one of – if not the – most uncertain and complex environments in recent memory."*

While the outlook may be uncertain, and there may have been a drop off from 2021's record level in M&A, the volume of Q3 2022 deals is still predicted to be better than Q3 in 2019 and Intralinks is predicting a -5%-+5% change in deal value year on year against 2021 Q3.

There is still plenty of capital in the market (unlike the 2008-2009 recession and the related credit crunch and Eurozone crisis), the situation is not deterring all buyers and while deals may be taking longer to execute, there is cause for some optimism.

Are there opportunities for M&A growth in 2022 and 2023?

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Yes. We predict that there are a number of opportunities for growth, despite the ongoing uncertainty in the market:

Cash-rich purchasers and deadlines to invest

Some strategic purchasers have built up large reserves of cash during the pandemic and are keen to invest it.

Special purpose acquisition company (SPAC) IPOs with listings on European exchanges had a record year in 2021; SPACs which completed an IPO with a listing in Europe in 2021 were about 35 in number. Listings have decreased so far in 2022, because of an expectation of rising interest rates and due to concerns relating to regulatory considerations. However, the SPACs need to be acquisitive within a limited timescale, and so we expect a series of de-SPACs across the continent in the coming months.

Private equity sponsors still have plenty of buying power and will pounce on attractive targets with lower valuations – it is estimated they are sitting on record levels of cash and have limited timescales in which to deploy it.

It is anticipated that sponsors may focus efforts on more attractive targets and be more selective about, and push harder in, auction processes they get involved in.

There is a trend for auction processes to be limited to a smaller group of potential bidders that are most likely to be serious in their intent. However, with very competitive processes come higher valuations and lower returns so we expect private equity sponsors to increasingly apply their resources to bolt-on acquisitions or roll-up acquisitions to enable them to make higher aggregate valuation multiple returns on the whole acquired group.

Investments made by financial sponsors in EMEA hit €169bn, equating to a staggering 28.2% of the region's total value in the first half of 2022, up from 22% seen during 2021 (ION Analytics: M&A Highlights First Half 2022: Down at halftime).

Smaller deals

Mid-market deals which are less reliant on bank financing will have less barriers to closing.

Alternative financing; ESG credentials increase access

Principally thanks to private equity, and as the risk appetite of traditional lenders such as banks decreases, we will see an increasing role for credit funds (which are more flexible) in financing transactions.

Positive ESG credentials of a transaction also improve access to financing on good terms.

Fragmentated sectors ripe for consolidation

Some sectors in certain European jurisdictions remain fragmented and ripe for consolidation. This is a lead cause of a buoyant M&A market in Poland, for example.

Are there opportunities for M&A growth in 2022 and 2023?

Hurry to complete before prevailing conditions worsen

Dealmakers are keen to complete deals before there is a decline in deal activity and bank interest rates rise further, so there may be a slight uptick in deal volume before any significant reduction.

Sectors bucking a downward trend

Certain sectors are buoyant, for example technology, media and telecommunications (despite lower valuations), biotech, pharma, healthcare, fintech, renewables, oil and gas (where shelved projects are again being looked at to remove reliance on Russian and other overseas supplies). Consumer and retail sectors are, for now, more resilient than expected with consolidation in their markets, though some slowdown is being seen.

Transformative acquisitions

For some, the negative factors, the economic tightening and potential downturn are driving dealmaking – there is a strong need to undertake transformative acquisitions to be competitive in today's economic climate and to protect against impacts of future crises. This includes tech M&A to effectively buy in digital and automation solutions, acquiring businesses with strong ESG credentials and buying targets to bring supply chains or logistics concerns in house. Acquisition as a route to transformation can be more efficient than organic growth and adaptation.

Carve-out transactions and reorganisations

Companies seeking to find efficiencies and focus on core operations or pursuing a different strategy after the pandemic and during these fiscally challenging times are continuing to put business divisions up for sale, mostly through auctions.

Groups are also undertaking reorganisations to benefit from efficiencies and cost cutting.

Distressed M&A

With the wind-down of government support, and the challenging economic outlook we expect there to be more business failures and sales of insolvent and struggling businesses or their assets. Some jurisdictions such as Germany and Spain have brought in legislation recently to facilitate restructuring of struggling companies.

In the end, these levels of economic disruption all create drag, which means slower or negative growth in M&A.

Deal term summary for 2022

Deal types

General trend

We expect to see more asset deals or distressed sales where buyers seek to cherry pick less risky assets and leave behind liabilities.

We also expect private equity structured transactions to continue to feature frequently in both sales and acquisitions.

Distressed M&A may lead to novel and complex deal structures.

Trends in Europe

In Italy, both share deals and assets deals are common. The choice mainly depends on tax matters and, sometimes, on specific conditions of the deals (cherry picking of specific business lines). We continue to see private equity structured transactions, even if leveraged finance is less used and sometimes substituted with other forms of financing (private debt). The new reform of the bankruptcy regulation is expected to facilitate and accelerate the already positive trend regarding distressed businesses.

Spanish M&A is typically structured by share deals, either by way of private auctions or proprietary deals, with asset purchases coming in second place. Corporate reorganisations (such as mergers or spin-offs) are less common in the Spanish market.

Under the current market conditions, it is expected some deal opportunities will grow. Big conglomerates will begin re-thinking about what is core and non-core for them; therefore, we expect to see some carve-outs or divestments of non-strategic businesses. Also, the Insolvency Law that the Spanish government has just approved will encourage the use of what is called “loan to own” to help fund deals.

Deal term summary for 2022

Consideration type

General trend

We expect that we may see an increase in alternatives to cash consideration on completion to aid cash flows while purchasers manage their cash with increased costs due to inflation. This may include more shares or loan notes, or deferred cash consideration.

Trends in Europe

In Italy, Deferred payment mechanisms have been often used as a way to retain key managers and/or to finance the acquisition (i.e. vendor loans). We are seeing, and expect to see, an increase also of alternative structures which provide completion of the transaction in several steps (immediate purchase of a shareholding and call/put option on the remaining shareholding based on agreed formulae).

We expect that cash deals will continue to be more common than paper deals in Spain.

Deal term summary for 2022

Price adjustment mechanisms

General trend

Locked box arrangements have been very popular in recent times, on auction sales and in a seller-friendly market. Due to current uncertainty and instability, and moving to a more buyer- friendly market, we are seeing an increased use of completion accounts mechanisms, while locked boxes remain popular.

Trends in Europe

Locked boxes have never been very popular in Italy, especially for domestic deals. Completion accounts mechanisms (based on Net Financial Position and Net Working Capital) remain popular.

In Sweden, locked boxes are still very popular due to their simplicity, especially in midmarket deals.

Most Spanish M&A transactions include a price adjustment mechanism which takes a financial indicator as reference (in most cases, net debt, followed by EBITDA and working capital), although the use of locked-box mechanisms is increasing significantly.

Deal term summary for 2022

Earn-outs

General trend

Due to difficulties valuing assets in the current economic climate, earn-outs are increasingly being used to bridge valuation gaps and to address the possibly unrealistic expectations of some sellers (particularly on tech transactions), as we head into a period of potential economic decline.

As emerging technology and life sciences/biotech deals are numerous in Europe and we expect them to continue to feature highly, and these are deals where the knowledge of a few individuals is key to the success and a fair valuation of a target based on current KPIs is challenging, we predict that earn-outs will continue to be popular. That said, we equally expect the wider use of earn-outs to increase.

EBITDA has historically been the metric used, but we envisage that other measures such as turnover or more creative measures may start to also be used, particularly in newer innovative businesses.

Non-ordinary course circumstance such as a further Covid-19 wave may lead to terms allowing for an extension to an earn-out period or the right to adjust earn-out calculations, though this would only be the case for a seller with a strong negotiating hand.

Trends in Europe

Earn-out mechanisms are quite common in Italy and are linked not only to economic results but also to retention of customers/key employees.

Earn-outs may be challenging from a tax perspective in Sweden, but in the current climate we have seen an increased interest in the use of earn-out models.

Earn-outs are commonly used in Spain. Certain earn-out mechanisms have been used to minimise purchasers' uncertainty on valuations as a consequence of Covid-19.

Deal term summary for 2022

Conditionality and gap covenants

General trend

There is an increase in conditional sale and purchase arrangements, due to an increase in regulatory approvals needed for transactions (e.g. Foreign Direct Investment (FDI) and national security approvals).

If Covid-19 risk or risks relating to the conflict in Ukraine increase we expect to see MACs and interim obligations (such as conducting the business in the ordinary course) being more hotly debated in conditional sale and purchase agreements, particularly for industries more likely to suffer disruptions (e.g. travel, leisure, logistics, healthcare).

With increased regulatory interventions, there is an increased risk of undertakings being imposed to permit the transaction to complete and we anticipate that this will lead to greater scrutiny at the outset to assess the potential impact of these on deal terms.

Trends in Europe

In a recent case before the District Court of Amsterdam, Nordian Capital was seeking to argue that the Covid-19 pandemic was a force majeure type event and so it did not have to complete the SPA. The SPA did not contain a MAC clause. The court ruled that the Covid-19 pandemic did not qualify as an “unforeseen circumstance” and it is seen therefore that trying to rely on the legal concept of *force majeure* may be insufficient. Accordingly a specific MAC provision would be advisable in a conditional SPA where there is concern about a further Covid-19 wave.

In Italy, there is an increase in conditional sale and purchase arrangements, due to an increase in regulatory approvals needed for transactions under the so-called “Golden Power” regime. Covid-19 and the war in Ukraine are a frequent and complicated topic of discussion in M&A transactions, as sellers tend to exclude them from MAC clauses, while buyers request to include them. Also, under Italian law, the concept of “force majeure” is not codified into law but specific remedies are provided by the Italian Civil Code in case of impossibility of the performance (extended by case law also to the “unusability” of the performance) or hardship (*eccessiva onerosità sopravvenuta*).

Polish law provides limited and uncertain relief from contractual obligations in the event of an extraordinary change in circumstances such as the Covid-19 pandemic. Consequently, since the beginning of the pandemic, it has become more popular for contracting parties to include MAC clauses with specific reference to Covid-19 and to regulate force majeure events explicitly in their agreements.

In Spain, the number of purchases subject to conditions has increased due to the FDI regulations that entered into force during the Covid-19 pandemic which require prior administrative authorisation in certain M&A transactions.

The potential impact of Covid-19 is still being considered (and will be very likely throughout 2022) by the purchaser as one such risk that may be deemed to have a potential material adverse effect, and is therefore included within the MAC clause.

Deal term summary for 2022

Warranty & Indemnity insurance

General trend

There is a continuing trend towards greater use of warranty & indemnity (W&I) insurance and on terms with limited recourse to the seller(s).

W&I has been the norm for private equity purchasers for a number of years across Europe, but we expect it to be used on a wider range of deals this year. This can address concern about a seller's financial covenant in the current economic climate.

We are increasingly seeing W&I used on smaller as well as mid-market deals, not just the larger transactions.

It is anticipated that W&I insurers will look to exclude matters relating to the invasion of Ukraine and international sanctions on Russia and Belarus. However, we have not yet seen any impact on pricing of policies; war tends to impact coverage rather than price.

Trends in Europe

The use of W&I in Italy has become a frequently used method for smooth closure of the deals. During the past two years, we have seen an increase of volume of W&I (particularly for PE, operating companies, real estate and renewables deals). In Italy the M&A insurance market is really active in providing add-on products to the W&I insurance to deal with contingent risks.

W&I is very popular in Sweden, even in smaller midmarket deals where there are management sellers. PE deals are typically insured.

In Belgium, use of W&I on larger deals is becoming common practice (whereas until a few years ago this was still exceptional in the Belgian M&A market; this is probably due to the fact that the market is dominated by small and mid-sized transactions). We are now increasingly seeing W&I insurance being used on smaller as well as mid-market deals, facilitated by a growing number of brokers dedicated to the Belgian market. The increase of W&I insurance premiums over the last 12 months in Belgium could however slow down the further growth of W&I insurance coverage in mid-market transactions.

Though W&I insurance is less popular in the Spanish market than in other countries, the use of this type of this insurance is gradually increasing year by year. However, this upward trend seems to have slowed down after the Covid-19 pandemic.

Deal term summary for 2022

Price

General trend

Valuations are contentious and, among other things, need to take into account inflationary and supply impacts. Due to market uncertainty, we envisage solid due diligence and rigorous price negotiations, renegotiations and financial analysis, meaning amendment to sale and purchase agreement drafts to accommodate altered pricing structures and consideration.

For private equity sponsors, inflation will impact investment returns, and we are expecting to see deals fall over after due diligence where returns forecasted are inadequate.

Trends in Europe

In Italy, prices are normally evaluated on the enterprise value of the transaction. They can be even higher depending on the complexity of the deal and the evaluation of the risk.

We are seeing renegotiations based on uncertain forecasts and difficult market conditions in Sweden.

In Belgium, with interest rates increasing, we have seen renegotiations of the purchase price (even shortly before signing), especially for technology or other early stage companies.

In Spain, It is difficult to foresee the behaviour of the supply chain crisis caused by factors such as significant increases in energy prices (which continue to rise as a result of the war in Ukraine) and its specific impact on the business plan of each company, which makes it complicated to determine the effects on the valuation of the target companies. Within the framework of certain M&A transactions, price adjustment clauses are being included in the purchase and sale agreements based on the impact that the supply crisis may have on the target in question.

Deal term summary for 2022

Warranty cap and coverage

General trend

We consider that it is likely that warranty caps may increase slightly due to the market turning in favour of purchasers, uncertainty and potential for more warranty claims.

We anticipate that through 2022 we will continue to see new specific warranties break through for ESG, technology, cybersecurity and other areas of increasing importance to buyers.

Trends in Europe

In Italy, the cap as well as other monetary limits are normally defined as negotiated in the transaction documents. Coverage is often full in respect of all the matters reviewed in the course of the due diligence exercise.

In Spain, before ESG matters became a trend in the M&A market, traditional deal documentation already foresaw a general representation (compliance with laws), the aim of which was to cover these matters. However, the current context demands specific representations covering such aspects and ensuring particular commitments from the seller within its liability regime.

Deal term summary for 2022

Security for payments

General trend

Buyers' and sellers' financial covenants may weaken in the coming months, and we anticipate that use of escrows, parent or bank guarantees or other security for payments may become more popular.

Trends in Europe

In Italy, we are seeing an increase of requests of W&I and we do not foresee any particular reason for a decrease.

We expect that warranty claims will continue to be mostly covered by means of a retention of part of the price (deferred payment) or an escrow account. Bank guarantees or other financial guarantees are less frequent.

Deal process summary for 2022

Due diligence

General trend

Buyers are undertaking more robust, deeper and lengthier due diligence exercises, to mitigate the current risk environment and to verify valuations that are challenging due to market volatility.

In particular we are seeing buyers taking their time to assess target businesses and pricing, which is meaning deals are starting more slowly.

We are increasingly seeing buyers undertake due diligence on ESG matters, privacy, regulatory matters, inflationary and supply chain impacts (e.g. supplier contract terms, pricing review terms), compliance with Covid-19 rules, cybersecurity and technology ownership and contracting. Many of these are areas that W&I insurers are showing a growing interest in, and for some may seek exclusions.

With more deals being backed by W&I insurance, on a minimal recourse basis, due diligence is more often needing to be completed in a compressed timescale.

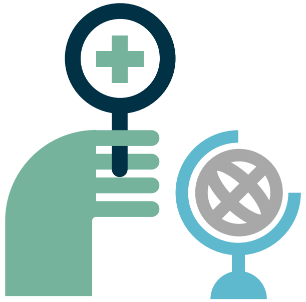
Trends in Europe

In Italy, for legal matters, the most common instructions are to conduct a high level red flag due diligence. Legal due diligence is often started only after satisfactory completion of business and accounting (and sometimes tax) due diligence.

In Sweden, we are moving towards more robust DD exercises, but the most common instructions are to conduct a high level red flag review.

In the current context in Spain, there is a greater need to carry out a solid process of due diligence (more in-depth analysis beyond the traditional topics) in order for the purchaser to be comfortable with the investment, the company projections, the competitive landscape and the impact of the increase of the rate of inflation.

ESG and digitalisation topics have become more important within the scope of due diligence, including new specific areas (many of them linked to the value chain verification) or simply expanding the scope of the more generic traditional areas, such as equal employment opportunities, environmental checks, internal anti-corruption and bribery measures, full compliance with data protection matters and cybersecurity.



Deal process summary for 2022

Deal timetable

General trend

Timetables lengthening considerably to permit more in-depth due diligence (DD) to support valuations, to factor in regulatory approvals needed and other conditionality, to deal with increased deal risks due to the current economic climate; in turn we may see a decrease in deal activity as limited dealmaker resource focuses on key transactions.

Some deals may equally be rushed to get them completed before market uncertainty and adverse conditions increase further.

Trends in Europe

The length of the M&A deal process may vary on a case-by-case basis and depends on the structure of the transaction and on the complexity of negotiations in Italy.

We experienced several practical delays in the transactions in 2020 and 2021, mostly due to the Covid-19 pandemic and relating lockdown measures, but players were able to quickly implement and accustom themselves to digital means.

In addition, from a regulatory standpoint, other emergency governmental interventions caused slowdowns in the acquisition/sale processes, in particular in case of foreign investments, due to the Golden Power regulation according to which, subject to certain conditions, it is necessary to submit a notification of the intended investment to the Italian authorities. This notification process may have a delaying impact on the completion of a transaction.

Deals are taking longer and particularly start slower in Sweden. Sellers may still try to rush deals but seem to accept the buyers taking their time.

In an uncertain economic climate, we expect that deals will take longer to exchange and complete. Once the new Belgian FDI regulation will enter into force (currently expected by 1 July 2023), it is expected that deals will take significantly longer to complete given the complexity of the screening process that requires the collaboration of nine federated entities.

In Spain, M&A processes are being delayed either because the conservative purchaser prefers to wait a few months to observe the company's financial performance, or because due diligence processes are lengthened so that the purchasers can carry out a thorough review that will reassure them when deciding to acquire a target.

Spanish FDI regulations have raised many interpretative doubts, mainly as regards the determination of the strategic sectors and investors affected by such regulations, which have led the parties to a transaction often to adopt a conservative position and request authorisation in order to avoid uncertainties as to the validity of the relevant transaction. Taking into account that obtaining such authorisation may take up to six months, this circumstance is delaying many M&A processes.

Deal process summary for 2022

Deal deliverability

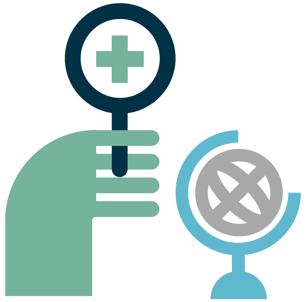
General trend

In the current landscape, we unfortunately predict that more deals will fall over or go on hold. This will be due to uncertainty as to pricing, the inability to source committed financing or a reduced risk appetite. With more conditional sale and purchase agreements, we also anticipate this will reduce slightly the number of transactions proceeding to completion.

The lack of in-person interaction through negotiations being dealt with online could contribute to the failure, or protracted nature, of negotiations, though generally we do not see barriers increasing as a result of moving the legal negotiations online.

Trends in Europe

The higher capital costs and the increasing pressure on investment returns that the Spanish M&A market is currently facing could result in the boards of directors and investment committees of companies to be more cautious in the near future, even delaying some deals due to the rising inflation, energy supply concerns, labour shortages and supply chain disruptions.



Deal process summary for 2022

Digitalisation of processes

General trend

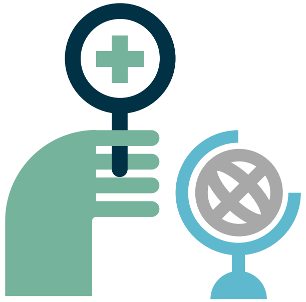
Due to the pandemic, deal processes needed to be digitalised to enable deals to continue to be closed. E-signing, electronic filings, remote completions and the like have become more the norm. In addition, processes for due diligence and integration have become more automated, and some AI used to aid document review. Drafting of agreements is increasingly automated. Drone use to carry out site visits for due diligence (e.g. on properties) has been a new tool. We are starting to see use of digital payment platforms for completion monies (paying agents) and escrow funds, and see the potential for the use of smart contracts and other technological solutions in M&A. We expect this trend to continue at pace.

Trends in Europe

In Italy, we have experienced a quick and almost full digitalisation of deal processes. Players were able to evolve and adapt and we expect that online negotiations will continue to be the norm even after the termination of the Covid-19 emergency.

In Sweden, deals have been digital for some time and we expect them to continue to be. Most actions can be taken digitally, which are appreciated by deal teams and clients alike.

In Spain, technology and tools to manage the M&A process, such as VDRs or cloud-based storage of transaction documents and resources during due diligence will continue to be essential. Thanks to AI, deal timings have been reduced and are expected to continue to be reduced in the near future, so that industry professionals have more time to concentrate on higher value-added activities.



Deal process summary for 2022

Deal planning

General trend

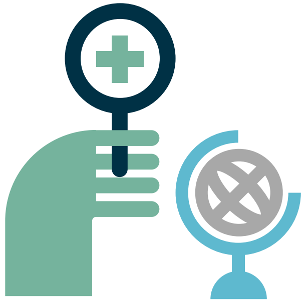
We predict that purchasers will put a greater emphasis on deal planning and assessment of regulatory and other key risks. Greater assessment time may be needed to analyse whether a transaction will be in scope of recently introduced FDI control regulations and to plan the deal process to accommodate a filing or to assess whether the amended approach taken recently by some regulatory bodies will mean an otherwise out of scope transaction is caught by a regulatory regime.

Due to the increased risk that transactions may be scrutinised by multiple regulators, we expect deal teams will need to be better at timetable and critical path planning, support in making filings and allocation of resources.

Trends in Europe

Preliminary analyses under the Golden Power regime are becoming frequent (also from a seller's perspective, in particular in case of auction process) in Italy.

This year, we predict that purchasers will include assessment time to analyse whether a transaction will be in scope of FDI control regulations. This assessment time is likely to be reduced once the new draft of FDI control regulation is approved by the Spanish government. Prior voluntary and non-binding consultations are becoming more frequent (and we expect they will continue to be so until the new FDI regulation is published) and therefore assessment time will still be needed to plan the deal process to accommodate a filing of an FDI application summarising the main aspects of the M&A transaction.



Deal process summary for 2022

Auction processes

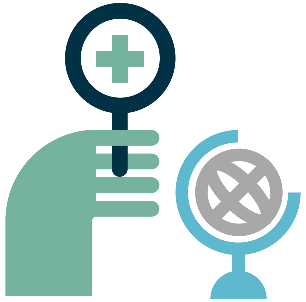
General trend

We have seen and expect to continue to see an increase in the use of auction sale processes.

Trends in Europe

During the pandemic, in Italy we experienced a decrease in auction sale processes, in favour of one-to-one negotiations.

Sales of companies by auction have become increasingly popular in Spain and we expect them to continue to be so.



Deal process summary for 2022

Local company law

General trend

Various European jurisdictions are overhauling their company law to attract investment in the competitive European market by making corporate transactions simpler and reducing paperwork, delays and barriers to closing.

Trends in Europe

Italy has not implemented significant changes in company law, while other kind of measures have been introduced by the Italian government in 2021 which may have some (positive or negative, as the case may be) impact on the M&A deals, including: (i) employment and social policies aimed at supporting companies operating in sectors materially hit by the pandemic (real estate, tourism, food and beverage); (ii) information filing requirements for delocalisation of activities outside Italy; (iii) financial benefits to companies investing in Research, Development and Innovation (so-called "New Italian Green Deal"); (iv) reform of the justice system aimed at speed up commercial litigation; and (v) reform of the bankruptcy code.

In 2019, the new Belgian Code of Companies and Associations (BCCA) came into force. Among other things, the BCCA allows for much more flexible company structures (although the number of company types has been reduced), with or without capital, with single or multiple voting rights, using electronic, written or remote decision processes, etc. In certain circumstances, the directors' liability is now capped for Belgian companies.

This year there are planned amendments to Polish corporate law including a mechanism for squeeze outs. Recently, the law was also simplified for joint stock companies (*spółka akcyjna*) which tend to be the larger businesses – all registered shares were dematerialised, share certificates lost their legal force and the electronic only registers held by a certified body.

In 2021, a simplified joint stock company was introduced which would be an attractive form of running start-ups. Selling and encumbering shares in these entities is streamlined as can be done in document form which could include e-mail. This allows remote transacting more easily. These entities have various other simplifications.

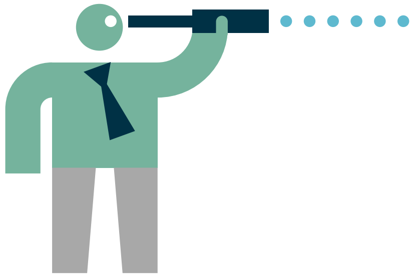
There is currently a draft regulation (pending approval from the Spanish government) that aims to resolve the interpretive doubts raised by the prior authorisation regime provided for in Law 19/2003, as amended in 2020 and 2021, in order to provide greater legal certainty to investors. This draft regultion will clarify, among other things, which strategic sectors will be subject to prior authorisation and will set forth a specific procedure for the interested parties to submit a prior voluntary consultation, which will be binding for the Spanish authorities, on whether it is necessary to submit a specific M&A transaction for prior authorisation. The Spanish authorities will have up to 30 working days to respond.

Likewise, a recent modification in the Spanish Companies Law allowing the holding of General Shareholders` Meetings by electronic/remote means may facilitate the management of acquired companies.

Osborne Clarke comment

Uncertainty reigns, and it is likely this will impact market confidence to some extent, as we head through Q4 of 2022, into 2023.

The war in Ukraine remains one of the largest uncertain factors, which European governments have little control over, making 2023 difficult to predict. Despite the uncertainty, M&A activity is currently holding up well, and we see that there is plenty of capital available still to spend and there remain very good opportunities that we have outlined for dealmaking later this year and in 2023. Indeed, there may be better prospects for decent returns on acquisitions in today's environment as valuations return to more realistic levels. European jurisdictions are well placed to confront the challenges being faced, and dealmaking will adapt to the new market trends, ways of doing deals and the increasing complexity and challenges of M&A.



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