WHITE & CASE

Peak performance: US M&A in 2018

2018 was a strong year for dealmaking in the US, particularly domestically, but when will the tide turn?


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US M&A weathers geopolitical storms

The political and economic backdrop may be unstable, but 2018 was a strong year for US M&A, especially domestically. However, a strong stock market cannot last forever, nor can a booming M&A market

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US M&A enjoyed yet another busy 12 months in 2018. Deal value climbed by 15 percent and the domestic M&A market thrived. Overall domestic deal value was up 23 percent compared to 2017, and the ten largest deals of the year were all domestic transactions.

Steady economic growth, low unemployment and interest rates, and the billions of dollars released through the Trump tax cuts all boosted domestic dealmaking. In a survey of 200 M&A executives conducted for this report, more than three quarters see the US as the most attractive M&A market in 2019, and 80 percent expect the US economy to continue expanding over the next year.

But while there is plenty of reason to be optimistic, the positive deal and economic figures can obscure growing concerns that the cycle may be close to its peak. Stock markets have been more volatile this year and businesses are worried about the impact of the Trump administration's actions.

More than half of respondents to the survey expressed their opposition to new laws that give the Committee on Foreign Investment in the United States (CFIUS) more powers to block inbound deals, and a third say they are worried about what escalating trade tensions between the US and China mean for their prospects. In what is supposed to be a strong seller's market, the fact that close to a third of those we surveyed have suffered lapsed deals is further cause for caution.

As we go into 2019, there will be much for dealmakers to look forward to. Technology continues to transform the way businesses operate and will remain a reason to transact. The economy is still in good shape too, which will sustain confidence.

Dealmakers will not feel the need to sit on their hands just yet but will need to approach prospective deals with a degree of caution over the next 12 months to mitigate against the inevitable recession and stock market pullback.

Contents

Confidence, cash and tax cuts: The US M&A landscape in 2018
Page 3

Private equity remains strong in 2018
Page 9

US M&A survey: Deal drivers and dilemmas
Page 13

Sectors overview: Tech and energy top the charts
Page 20

Technology M&A value soars in 2018
Page 23

Consumer deals slip as digital disrupts
Page 25

Financial services deals are down, but 2019 brings hope
Page 27

Stability in early 2018 fuels oil & gas M&A
Page 29

Real estate rises higher on megadeal surge
Page 31

Next big thing drives healthcare M&A
Page 33

Deal-changing decisions from Delaware
Page 34

Why, how and when should directors engage with shareholders?
Page 36

Four trends moving the US M&A needle in 2019
Page 38

Confidence, cash and tax cuts: The US M&A landscape in 2018

The US M&A market delivered another year of strong performance in 2018. Though deal volume dipped 2 percent year-on-year to 5,682 deals, deal value was up by 15 percent over the period, to US$1.5 trillion

By John Reiss, Gregory Pryor

A number of large deals in a thriving domestic M&A market drove the rise in value. The ten largest US transactions recorded over the period were all domestic deals, and domestic deal value climbed 23 percent year-on-year to US$1.2 trillion.

Domestic dealmakers have drawn confidence from the steady growth of the US economy, low unemployment, business-friendly tax cuts and strong stock market performance.

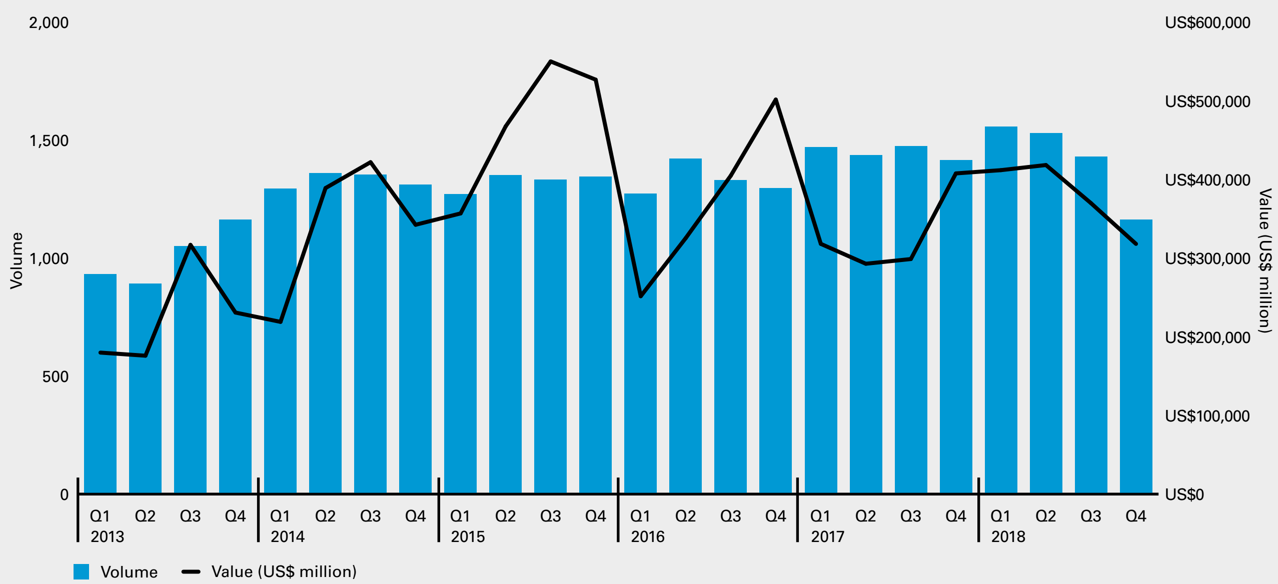
Highs and lows

Both the S&P 500 and Dow Jones Industrial Average reached record highs in 2018 and according to the US Department of Commerce, GDP grew by 4.2 percent and 3.5 percent in Q2 and Q3 respectively. Unemployment is at 3.7 percent, a 48-year low, and average hourly earnings have climbed.

Business has also benefited from the Trump administration's tax cuts, which reduced the corporate tax rate from 35 percent to 21 percent

> **"The ten largest US transactions recorded in 2018 were all domestic deals, and domestic deal value climbed 23 percent year-on-year to US$1.2 trillion.**

US M&A 2013 – 2018

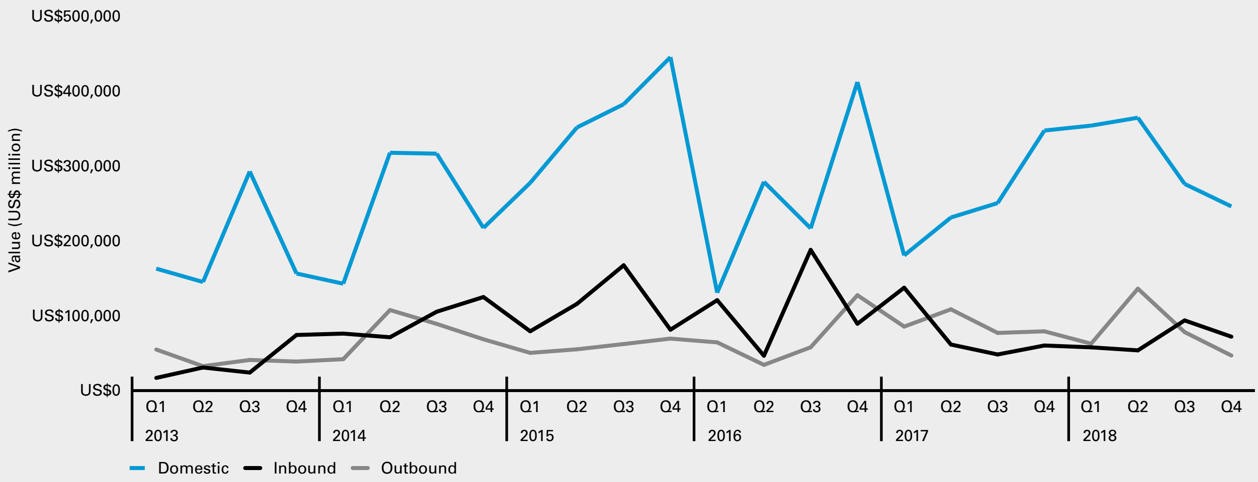


and allowed US corporates to repatriate cash held overseas at reduced rates. Warren Buffett's investment vehicle, Berkshire Hathaway, for example, said its portfolio had received a net gain of around US$29 billion as a result of the tax cuts. But although solid domestic economic fundamentals have supported US dealmaking, the M&A market has also proven more volatile and unpredictable in 2018. The White House's decision to impose steel and aluminum tariffs on China and Western allies, and a tense renegotiation of the North America Free Trade Agreement (NAFTA), which has been renamed United States-Mexico-Canada Agreement (USMCA), have caused prolonged periods of uncertainty, prompting large swings in stock markets. The Dow Jones Industrial Average suffered its largest single-day fall in February, and the Vix, an index tracking stock market volatility, reached its highest level since the Chinese currency crisis of 2015.

Top 10 US M&A deals 2018

Announced date	Target company	Target dominant sector	Bidder company	Bidder dominant country	Deal value (US$ million)
08/03/2018	Express Scripts Holding Company	Business services	Cigna Corporation	USA	67,601
29/04/2018	Sprint Corporation	TMT	T-Mobile USA, Inc.	USA	60,806
01/08/2018	Energy Transfer Partners, L.P. (97.64 percent stake)	Energy, mining and utilities	Energy Transfer Equity, L.P.	USA	59,612
28/10/2018	Red Hat, Inc.	TMT	IBM Corporation	USA	32,556
30/04/2018	Andeavor Corporation	Energy, mining and utilities	Marathon Petroleum Corporation	USA	31,327
29/01/2018	Dr Pepper Snapple Group Inc	Consumer	Keurig Green Mountain, Inc.	USA	26,801
26/03/2018	General Growth Properties, Inc. (66.2 percent stake)	Real estate	Brookfield Property Partners L.P.	USA	26,705
14/10/2018	L3 Technologies, Inc.	Defense	Harris Corporation	USA	18,362
11/07/2018	CA Technologies	TMT	Broadcom Inc.	USA	17,987
30/01/2018	Refinitiv (55 percent stake)	Business services	Blackstone Group LP; GIC Private Limited; Canada Pension Plan Investment Board	USA	17,000

US M&A 2013 – 2018: Domestic, inbound and outbound value



A new era for CFIUS

By Farhad Jalinous, Karalyn Mildorf, Keith Schomig, Stacia Sowerby

The expansion of CFIUS's jurisdiction under a new law enacted this past summer has been cited as one of the reasons for the fall in inbound US M&A activity in 2018.

In August of 2018, the president signed the Foreign Investment Risk Review Modernization Act (FIRRMA) into law. The legislation—the first statutory overhaul of the CFIUS process since 2007—expands the committee's jurisdiction in response to an evolving national security landscape.

Mandatory declarations in pilot testing

Deals in which foreign investors would have certain non-controlling yet non-passive rights, such as the right to a board seat or observer, access to material non-public technical information, or certain substantive decision-making rights, in addition to control transactions, are now included in CFIUS's jurisdiction. The legislation also captures real estate purchases and leases for properties close to certain sensitive government locations. FIRRMA also extends the CFIUS review period and grants the committee the power to run pilot programs, which allow it to test provisions in FIRRMA before new regulations are issued. One such pilot program has required that short-form declarations to CFIUS become mandatory for certain technology deals, whereas historically review was at least ostensibly a voluntary process.

Concerns about Chinese bidders mount

FIRRMA's expansions will not shift CFIUS's focus away from deals in the defense sector and those involving critical technologies and infrastructure, but the changes reflect mounting concerns with inbound investment from China. In addition to its concerns about critical technologies and critical infrastructure, CFIUS is increasingly focusing on real estate assets in close proximity to certain sensitive US government installations and any businesses that have access to large amounts of sensitive data on US citizens, along with other areas that may be sensitive for national security reasons.

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The ten largest US transactions in 2018 were all domestic deals

US $277.5 billion

The value of inbound M&A in 2018—a 10 percent fall compared to 2017

Both the Dow and S&P 500 closed 2018 weaker than they started it.

While the appetite for M&A remains strong, volatility and uncertainty make it more difficult for dealmakers to reach agreement on valuation. And against a backdrop of macroeconomic tensions, confidence in the future performance of targets will be even more important.

Cross-border activity takes a hit

Inbound M&A into the US has slowed as a result of this volatility, falling by 10 percent year-on-year in 2018 to US$277.5 billion. The drop in inbound M&A has been exacerbated by tougher regulations and checks on foreign buyers investing in the US. In March, President Trump blocked, on national security grounds, the hostile bid for US chipmaker Qualcomm by rival Broadcom, then based in Singapore. And in April, the US government banned US companies from dealing with Chinese telecoms equipment manufacturer ZTE.

Broadcom was later allowed to acquire New York–based CA Technologies in an US$18 billion megadeal after redomiciling to San Jose, but the environment for foreign buyers investing in the US has become less friendly. In August, CFIUS had its scope broadened significantly when FIRRMA was signed into law. It is no coincidence that inbound M&A has fallen as these measures have been put into action. Inbound M&A from Chinese bidders was down 66 percent by value year-on-year, to US$3 billion, while volume was down 40 percent to 38 deals. With US economic policy following an increasingly protectionist path, deals by US dealmakers overseas have also stumbled in 2018. Outbound deal value has fallen by 8 percent year-on-year to US$324 billion in 2018.

Dealmakers will still see the value in cross-border transactions, but geopolitical and trade issues are making the landscape increasingly difficult to navigate.

Oil prices fuel deals

Despite the mixed picture for M&A, however, large strategic deals across all sectors have continued. After a period of low oil prices, activity in the energy, mining and utilities (EMU) sector has revived, with M&A from this sector accounting for two of the ten largest deals in 2018. A stable oil price (for much of the year) encouraged higher production from US shale fields, which sparked deals such as Marathon Petroleum's US$31.3 billion acquisition of rival Andeavor. Restructuring activity in the energy industry, which has seen companies unwind tax-exempt corporate structures called master limited partnerships (MLPs), has also contributed to overall energy deal value.

Digitalization drives deals

The TMT sector, which has been one of the most active industries for M&A since the financial crisis as mobile, content, internet and data services converge, has had a busy period. Sprint and T-Mobile, which called off merger talks a few years ago, have now reignited their plans with a proposal for a US$60.8 billion tie-up. The deal still requires Department of Justice (DOJ) and Federal Communications Commission (FCC) approval, but after the Supreme Court ruled against a DOJ suit to block the merger between AT&T and Time Warner, there is optimism that the Sprint and T-Mobile deal can cross the line at the second attempt.

Major strategic realignment in sectors like healthcare have also supported megadeals. The largest US deal of the year, Cigna's US$67.6 billion acquisition of Express Scripts, followed moves by technology companies to disrupt incumbent players in the healthcare industry. Amazon, for example, has partnered with Berkshire Hathaway and JPMorgan Chase to form a not-for-profit entity that will use big data and other high-tech tools to improve healthcare costs for their employees. Deals such as Cigna's move for Express Scripts and CVS's purchase of Aetna for US$67.8 billion show that established healthcare businesses are turning to M&A to build scale and take control of supply chains in response to moves from digital disruptors.

Healthcare is hardly the only sector undergoing change driven by technology, as companies in all sectors are developing tech plays

US$3 billion

The value of inbound M&A from Chinese bidders in 2018—down 66 percent compared to 2017

8%

The fall in outbound deal value in 2018 compared to 2017

Employee equity awards in spin-off situations

By Henrik Patel

Divestments and spin-offs have been a notable feature of US M&A activity in 2018.

Nestlé sold its confectionary business in the US to Ferrero for US$2.8 billion at the start of the year; Walmart agreed to a deal to offload its UK grocer ASDA; and GE chief executive John Flannery has outlined a divestiture strategy that will see the industrial conglomerate focus on its core aviation, power and renewables units.

As the cycle peaks, other companies are likely to follow suit, focusing on their best-performing divisions and carving out non-core assets.

Managing incentive programs

Retaining and incentivizing key management, however, can be difficult after a spin-off or divestiture, especially when managers are tied to the parent company's stock. How to manage the transition and entice managers to stay post-transaction is something the parties must consider, as are the costs these types of incentives may add to the deal.

Each transition incentive agreement is unique to the transaction, but usually involves the new buyer either replacing the incentive, honoring a previous incentive plan, or the seller agreeing to pay out unvested incentives on the closing of the deal.

Who stays, who goes?

A further layer of complexity comes into play when deciding which employees need to go with the divested entity and which ones should stay.

The type of buyer will affect employee moves and can influence the overall valuation. A strategic buyer is less likely to retain back-office teams such as accounting, IT and HR, while a financial buyer will likely need those resources.

These considerations will need to be addressed in an employee matters agreement. One way to handle these issues is to set up a turnkey operation with all the back office in place, and then it is presumed to be at the buyer's cost to change anything post-spin-off/divestiture. This is most common when there is a spin-off via IPO.

Among the other major challenges involved in finalizing spin-off arrangements: setting up incentives for executives when the spun-out entity is carved out from a listed business; convincing key staff to stay on when the buyer is an unknown entity; and understanding any union obligations where applicable.

Should divestment volumes increase, as many anticipate, sellers and buyers will have plenty of employee issues to consider when attempting to get these deals over the line.

Merger controls

By Rebecca Farrington

It is critical for parties to prepare for potential investigations by US and global antitrust authorities in any transaction raising competitive issues, large or small, horizontal or vertical.

Early discussions becoming more common

While pre-filing has long been standard practice for cases in front of the European Commission and other authorities around the world, this had not been common with the US authorities outside of certain industries. More recently, however, US authorities have been encouraging early discussions in transactions where the parties know there is a high likelihood of competition issues, including encouraging parties to provide voluntary submissions of business documents and information beyond what is required in their filings—and to provide it even before making their merger filings. By doing so, both parties and enforcers hope to address issues earlier in the process to streamline and focus any investigation.

Vertical mergers under scrutiny

Antitrust authorities are paying closer attention to potential competitive harms from vertical mergers. Both the DOJ and the FTC have investigated and pursued allegedly anticompetitive vertical mergers, the most notable example of which is the DOJ's attempt to block the merger between AT&T and Time Warner.

Structural remedies still favored

The FTC and DOJ continue to favor structural remedies, such as divestitures, over behavioral remedies. Bayer, for example, divested US$9 billion worth of assets, its largest divestment ever, to secure consent for the Monsanto deal. Telecommunications groups CenturyLink and Level 3 sold overlapping aspects of their businesses to obtain clearance, and Alere and Abbott Laboratories recently sold two product lines to receive the go-ahead for their merger. Despite the prevalence of structural remedies, the recent Staples/Essendant settlement is an example of a behavioral remedy—a firewall imposed to prevent access to commercially sensitive data.

and look to M&A to capture human intellectual capital and intellectual property.

US markets buffer headwinds

Dealmakers have had to negotiate an unpredictable year and headwinds are building, but corporates will continue to turn to M&A when they see strategic assets that enable them to build scale and respond to shifts in business models.

The US market is set to remain an attractive destination for investors going forward, even with material uncertainty. While a US recession may not be imminent, potential buyers must prepare for one, when considering their M&A strategies.


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Private equity remains strong in 2018

Private equity buyout activity saw an increase in 2018, with volume rising 6 percent to 1,361 deals and value up 7 percent to US$214 billion. Exit volume was down 4 percent to 1,107 deals and value dropped 5 percent to US$249.1 billion

By Oliver Brahmst, Gary Silverman, Ray Bogenrief, Luke Laumann

Deal figures have held their own despite growing edginess within the buyout community about high valuations, especially with growing pessimism about the economy towards the end of the year.

Given the high levels of dry powder at their disposal, firms remain under pressure to put their money to work, but with valuations so high, many private equity investors may welcome a correction.

US $214 billion

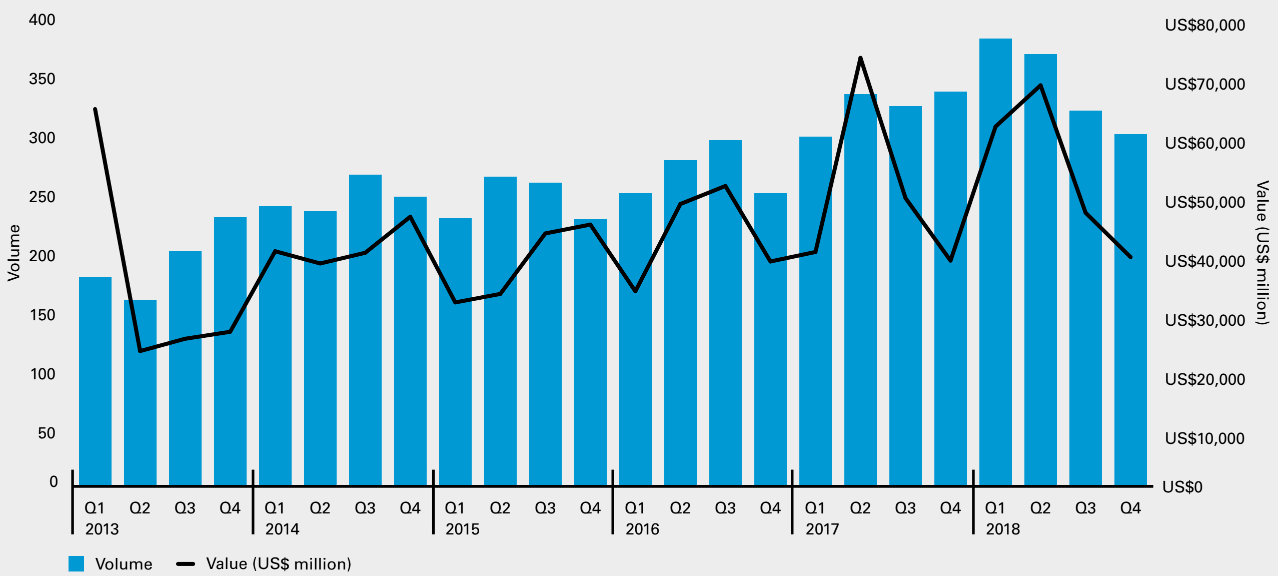
The value of US buyouts in 2018—up 7 percent compared with 2017

Caution ahead

Given these market dynamics, firms have become increasingly cautious, as even the smallest bumps in the road can negatively impact returns. After all, high multiples, and the added leverage this usually implies, mean increased risks to any investment.

> **Given the high levels of dry powder at their disposal, firms remain under pressure to put their money to work.**

Private equity buyouts, 2013 – 2018



Companies may find themselves with less margin for error in such circumstances, making covenant defaults more likely. And if there is a multiple contraction, even well-performing companies may deliver a poor or negative return on investment.

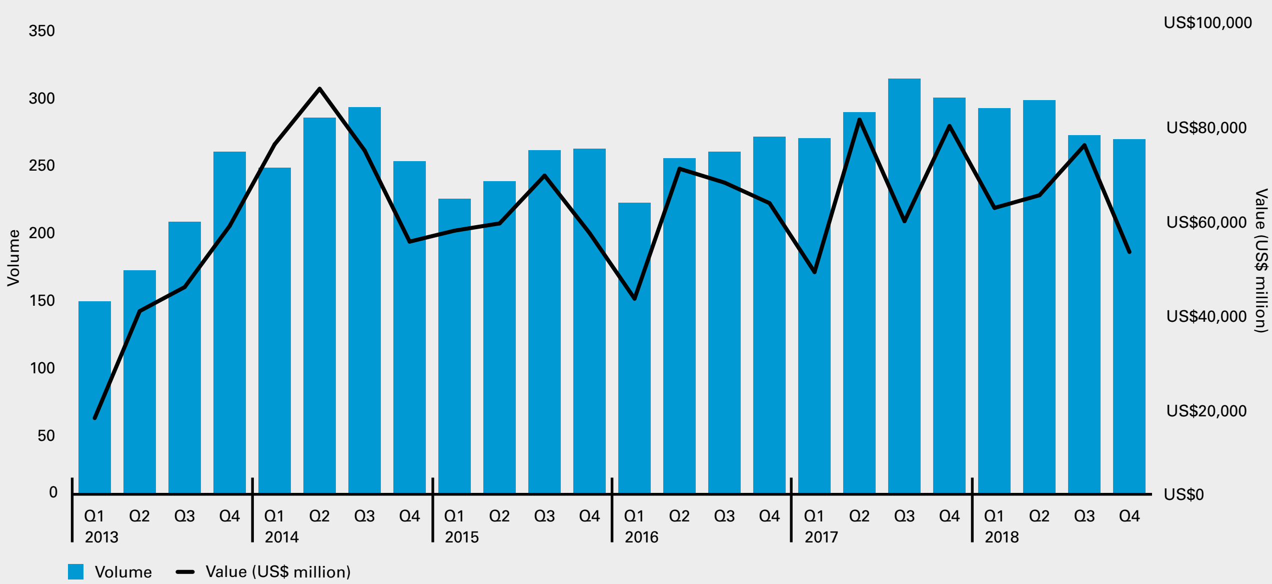
Weighing these factors, smart investors should proceed cautiously to avoid overpaying in what may be the tail end of an expansion period.

Competition for quality

Given these risks, firms have focused their resources on buying assets with proven track records of trading through cycles, as seen when Blackstone, GIC and the Canada Pension Plan Investment Board teamed up to acquire a 55 percent stake in Thomson Reuters' Financial & Risk business for US$17 billion.

Firms have also clustered around resilient, high-growth sectors when seeking out targets. The technology sector has proven particularly attractive in this respect, thanks to its disruptive capacity. Investors have seen that high-quality tech companies can sometimes enter new industries and quickly take disproportionate market shares, making this sector a favorable investment target in an uncertain environment.

Private equity exits, 2013 – 2018



PE turns to infrastructure
In order to manage higher multiples, firms are also looking for adjacent areas where pricing and competition are sometimes not as acute, such as infrastructure and real estate. Within infrastructure, investors are drawn to areas ripe for consolidation, where they can deploy a platform play, consolidating smaller operations before selling to a large investor or strategic buyer for a higher multiple.

Conundrum for the coming year
Deployment has also been informed by previous successes, with firms seeking to replicate exits like the Sequoia Capital–led consortium selling tech business GitHub to Microsoft for US$7.5 billion and KKR's exit of Sedgwick Claims Management to The Carlyle Group for US$6.7 billion.

Against a backdrop of sky-high valuations and growing unease about macroeconomic trends, buyout firms are feeling cautious, yet must deploy the vast amount of committed capital they have. This is the conundrum most firms will be facing in the coming year.

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> **In order to manage higher multiples, firms are also looking for adjacent areas where pricing and competition aren't as acute, such as infrastructure and real assets.**

US M&A survey: Deal drivers and dilemmas

We surveyed 200 executives on their views about the future of M&A and found that most remain optimistic about 2019

By John Reiss, Gregory Pryor

On the one hand, the US economy has grown steadily, unemployment is down, interest rates remain low and the Trump administration's tax cuts have given businesses across the board a material cash boost. Domestic deal activity has benefited, with value climbing 23 percent year-on-year in 2018.

Yet, as strong as the economic fundamentals appear, volatile stock markets, an escalating tariff war and a tougher regime for screening inbound investors have given dealmakers pause.

Although the Dow Jones Industrial Average and the S&P 500 both hit record highs in 2018, they have also suffered some of their biggest one-day falls since the financial crisis.

> **When asked which country is most attractive to acquire companies from over the next 12 months, 77 percent chose the US, up from 67 percent last year.**

Inbound deal value, meanwhile, has dropped by 10 percent. New powers granted to CFIUS, which could make it tougher for foreign entities to invest in certain industries, and the Trump administration's imposition of tariffs on steel, aluminum and various Chinese imports have all weighed on investment into the US from abroad.

White & Case surveyed 200 US dealmakers to gauge how they assess the key deal drivers and dilemmas facing investors at this time.

DEAL DRIVERS

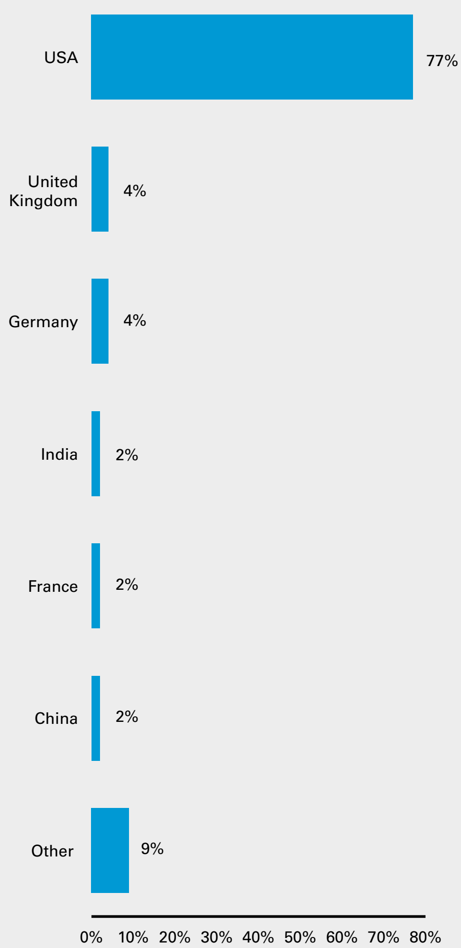
Domestic bliss

Dealmakers are upbeat about prospects for domestic dealmaking. They see positive economic signs on the horizon and, in the main, believe the economy will keep on growing.

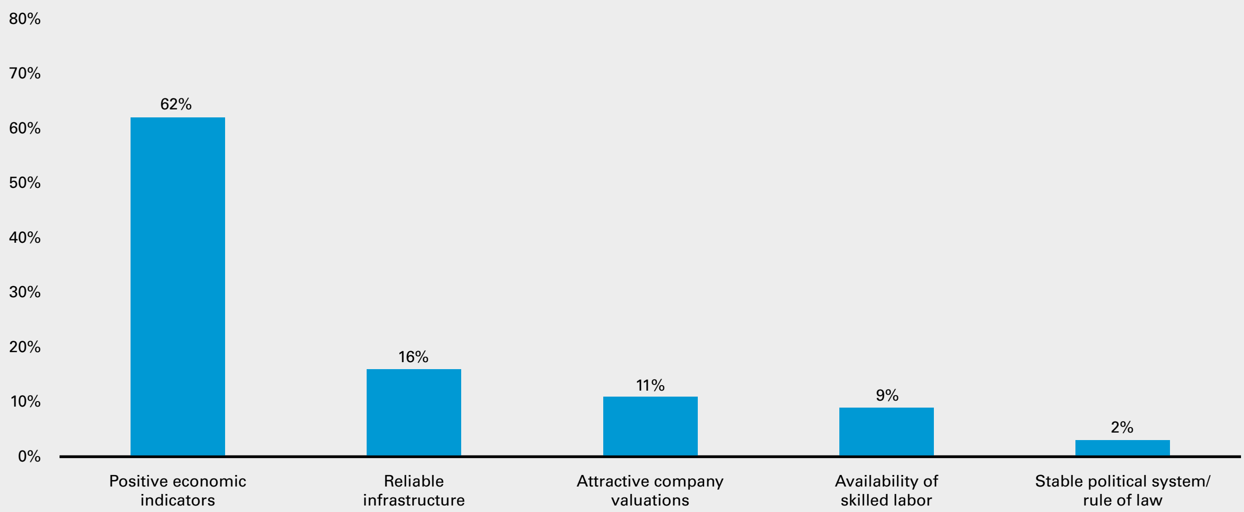
When asked from which country is it the most attractive to acquire companies over the next 12 months, 77 percent chose the US, up from 67 percent last year. Only 6 percent say entering a new geography is the key driver for M&A.

"The US market has returned to growth and the level of uncertainty is minimal—apart from Trump's policies," says the chief financial officer of a US business services company. "The outlook for future economic growth looks stable, and we prefer to grow in our core domestic market. We see no value in venturing into foreign markets at this time."

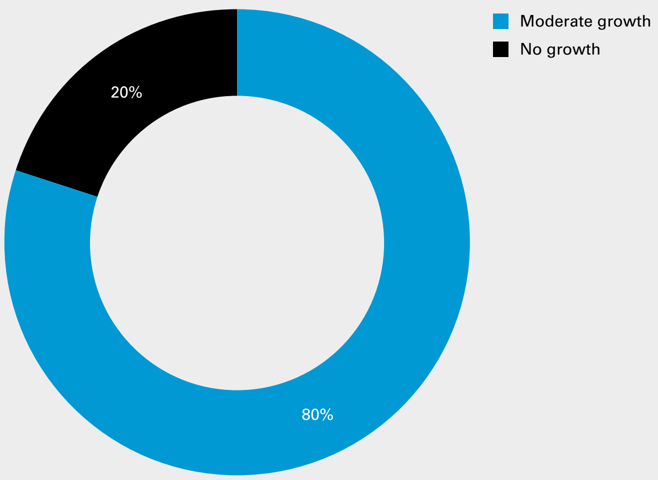
From which country is it the most attractive to acquire companies over the next 12 months?



Why is this country the most attractive? (Please select the most important)



What will happen to US GDP in 2019 in relation to the rate of growth in 2018?



80%

Percentage of respondents who predict moderate growth in US GDP in 2019

94%

Percentage of respondents who say the reduction in the rate of corporation tax has increased their company's appetite for M&A

The reason most commonly cited for their country choice was positive economic indicators. When asked about what will happen to US GDP in 2019 compared to 2018, 80 percent predicted moderate growth, 20 percent said there will be no change, and no respondents predicted a slowdown. When asked about the rate of growth in 2020 compared to the rate of growth in 2018, 17 percent say 2020 will see rapid growth, 76 percent say moderate growth and just 7 percent say there will be no change. Again, no one predicted a slowdown.

Despite the solid performance of the US economy over the last year, it is somewhat surprising that respondents weren't more concerned that the economic cycle could be peaking. Although large strategic buyers are flush with cash and eager to deploy it into acquisitions, there is growing concern among them that there may be a downturn in the near future.

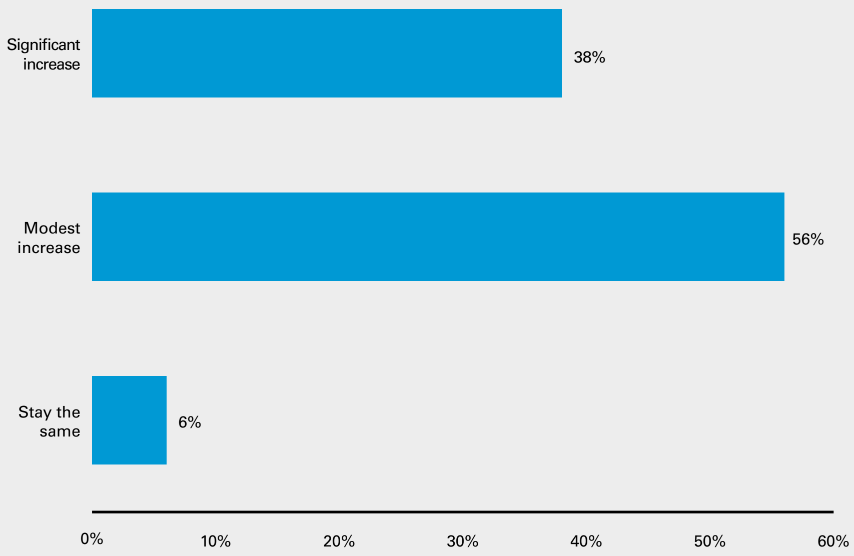
Taxing times

The Trump administration's tax reforms have been welcomed by M&A practitioners, with dealmakers saying that the tax changes have increased their confidence to pursue M&A.

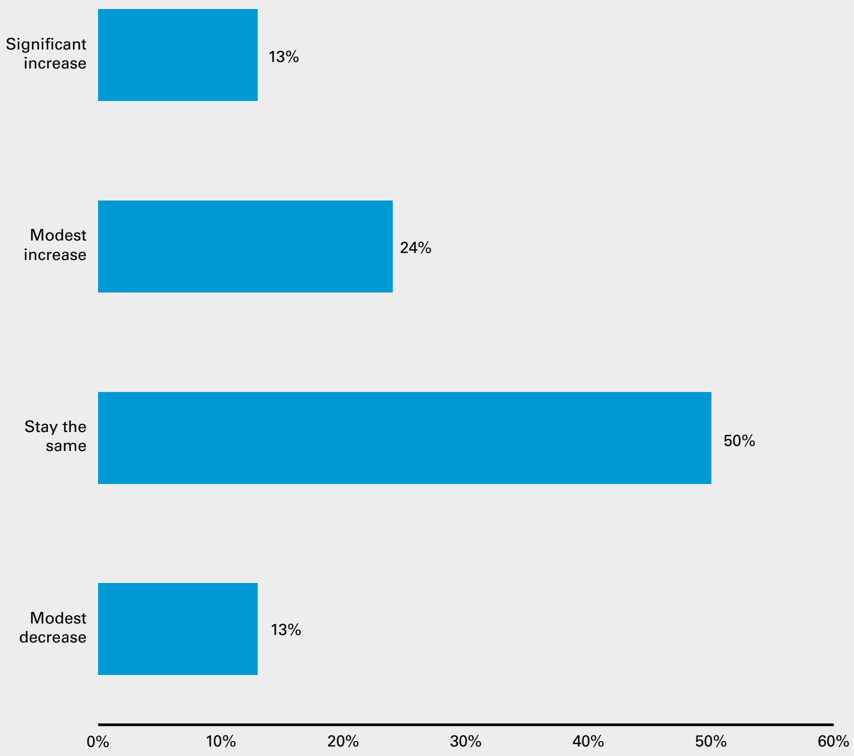
The lower corporate tax rate has allowed companies to retain more earnings, which they have been able to deploy into acquisitions. The immediate deductibility of certain hard assets included in transactions has made M&A even more attractive for some companies.

Almost all of the respondents (94 percent) say the reduction in the rate of corporation tax from 35 percent to 21 percent has increased their company's appetite for M&A, with 38 percent saying the tax breaks have significantly increased deal appetite.

What has been the impact of the reduction of the federal corporation tax rate from 35 percent to 21 percent on your company's appetite for M&A?



What has been the impact of the one-off tax on all repatriated non-US earnings on your company's appetite for M&A?



When it comes to the introduction of a one-off tax on all repatriated non-US earnings, some 37 percent say this has increased their appetite for M&A, while 50 percent say it has had no impact and 13 percent say it decreased their appetite. Interestingly, 5 percent see tax savings as the primary driver for M&A activity. Although these respondents represent only a small proportion of those polled, they do illustrate the extent to which the Trump tax cuts have freed up capital for deals.

"Low tax rates will have a significant positive impact on the overall economy and we will see growth in new investment, employment and wages. Positive sentiments in the market give us confidence to execute our acquisition plans," an executive vice president at a TMT business says.

The tax cuts put more money into the economy and may have helped boost stock market valuations. Yet, their effect on M&A may be more limited. The lower rates are unlikely to have made a dramatic impact on valuations in M&A—the market was already operating in a competitive market with high multiples, even before the cuts came into effect.

Tech and IP are prized

Technology and IP are cited as the main reasons for pursuing a deal, and are expected to remain major drivers for dealmaking over the next 12 months. A quarter of respondents see it as their key deal driver—the same proportion as in last year's survey.

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> **The lower corporate tax rate has allowed companies to retain more earnings, which they have been able to deploy into acquisitions.**

"As long as new technologies continue to disrupt entire markets, acquiring new technology and expertise will be a top reason for us to engage in acquisitions so that we can defend our market position and stay ahead of the curve," says a corporate development director at a TMT company.

Revenue synergies and diversifying products or services were the next most popular deal drivers, each polling at 20 percent.

"If we are to meet the new product demands of customers, we can't only rely on internal or organic development of new products. Developing new products is time consuming and not always suitable in the current competitive market," says the head of corporate development at a consumer company.

A key to growth

The positive sentiment towards M&A that emerged in the survey can also be explained by the fact that all respondents have seen the benefits of deals done in recent years.

When asked how much M&A has driven average annual growth in the previous three years, 32 percent say it has driven 1 to 2 percent of growth (compared to 38 percent of respondents in last year's survey); 66 percent say it has driven growth of 3 to 4 percent (compared to 51 percent who said this last year); and 2 percent put the total at 5 percent or more (down from 7 percent in last year's survey). No respondents say M&A has had a negative impact on growth or that it has not driven growth at all.

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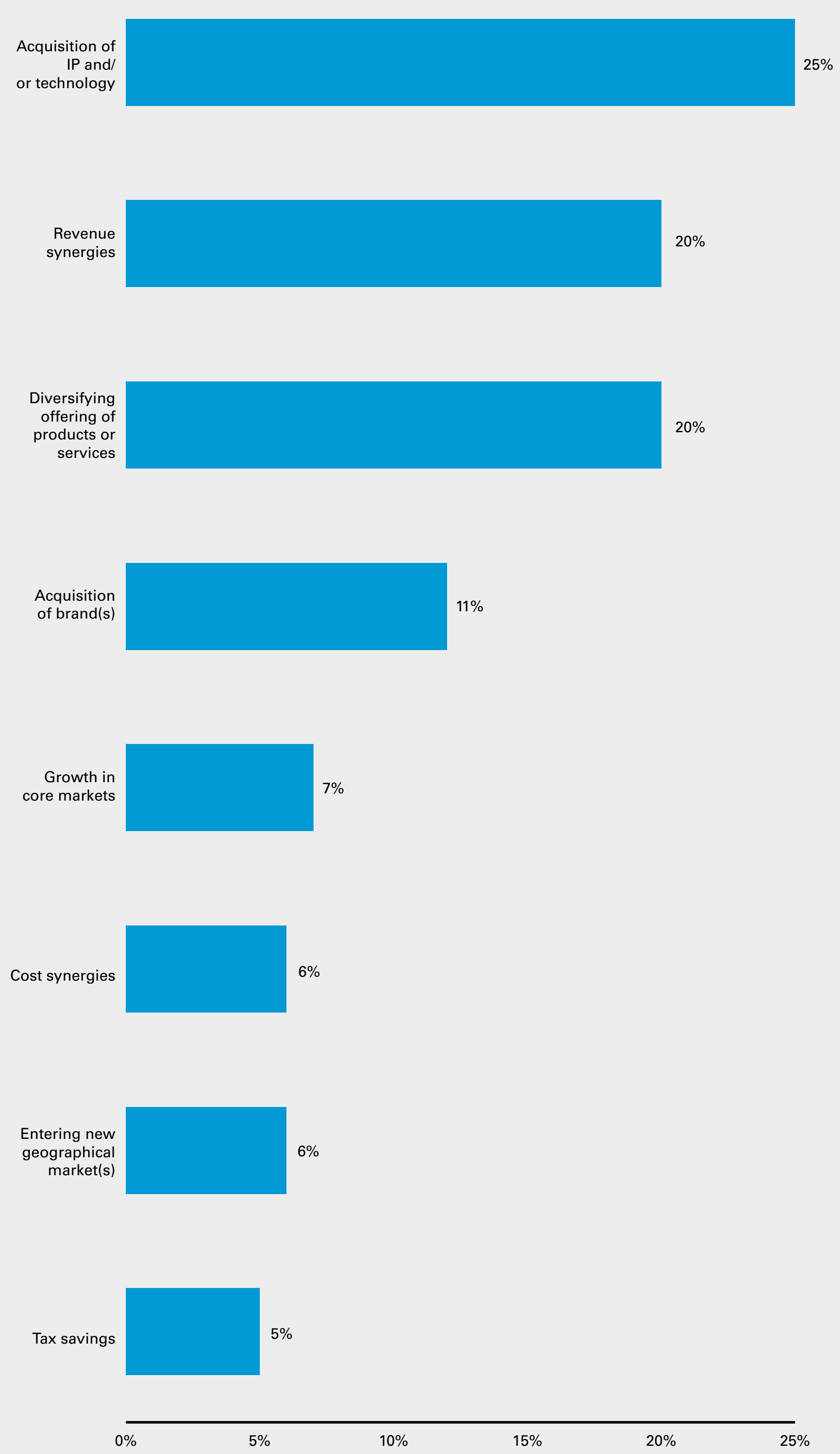
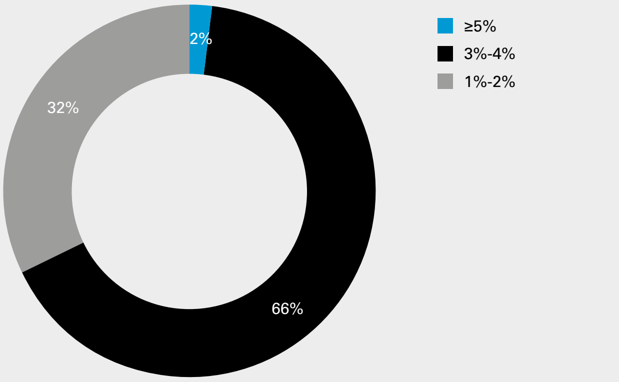
When asked how much M&A has driven average annual growth in the previous three years, 66 percent say it has driven 3 to 4 percent growth.

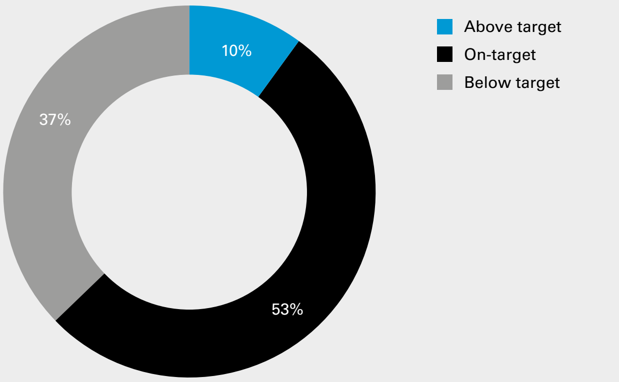
What are the key drivers for your M&A activity over the next 12 months? (Select the most important)



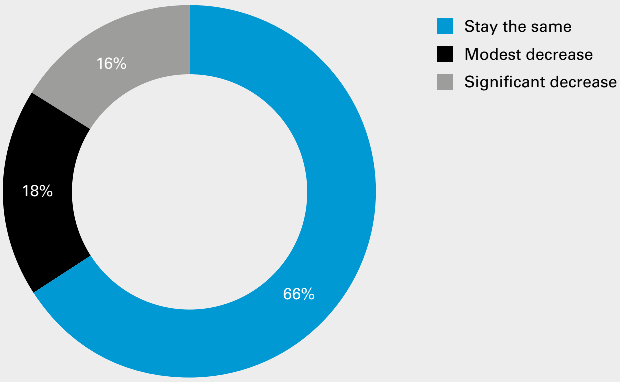
How much has M&A driven average annual growth in your company over the previous three years as measured by underlying earnings per share, in your estimation?



Was this…?



What would be the impact on your company's appetite for M&A if the US imposes new additional tariffs on Chinese goods?



More than half (53 percent), meanwhile, say average annual growth was on-target, with 10 percent saying it was above target and 37 percent saying it was below target.

Although the outlook is less certain, the fundamentals remain the same. The reasons for undertaking M&A—to grow, to expand your customer base and geography and to increase more intellectual capital—continue to drive deal activity.

DEAL DILEMMAS

Tariff troubles

Although a majority of respondents say more tariffs on China will have no impact on their businesses, more than a third say an escalating tariff war could cause a downturn in the market.

Of those surveyed, 66 percent say tariffs would have no effect on their company's appetite for M&A, but 34 percent say it would decrease their appetite.

"Considering the hardline approach of Trump, we were expecting the new tariffs, so we had prepared our business already. We had to be proactive, as we could have faced supply and operational issues. These are political and business scenarios we always prepare for. I don't think we will restrict our strategic activities because of the tariffs," an executive at a US consumer business says.

For any decent-sized cross-border transaction, the future of trade relations will have significant consequences. However, for middle-market transactions, the increases in tariffs will not have as much of an impact.

CFIUS issues

Even though two-thirds of respondents were unconcerned with the imposition of tariffs, more than half of those surveyed disagreed (52 percent) with legislative changes that expand the jurisdiction of CFIUS, which can block inbound M&A on national security grounds.

The expansion of CFIUS's jurisdiction puts it at the forefront of any regulatory issues dealmakers need to address when handling cross-border transaction involving a target company based in the US.

"Foreign companies face so many regulatory restrictions and if CFIUS's jurisdiction is expanded, foreign companies will have another reason to worry about looking to the US for acquisitions. If the market is to grow continuously, there should be greater international cooperation," a senior vice president of corporate development at a consumer company says.

Just under a quarter of respondents (24 percent), however, believe the extended powers are necessary, while 24 percent neither agree nor disagree.

"I think it is required to safeguard the interest of American businesses and keep the credibility of our domestic market," a finance director at a financial services group says. "I would want CFIUS to have the powers it needs to block all those investments it thinks are a concern and can harm the harmony of our market."

28%

Percentage of respondents who say a deal they have worked on in the past two years has lapsed

Lapsed deals

Aside from CFIUS, the other major concern expressed by respondents in the survey is the high volume of lapsed deals.

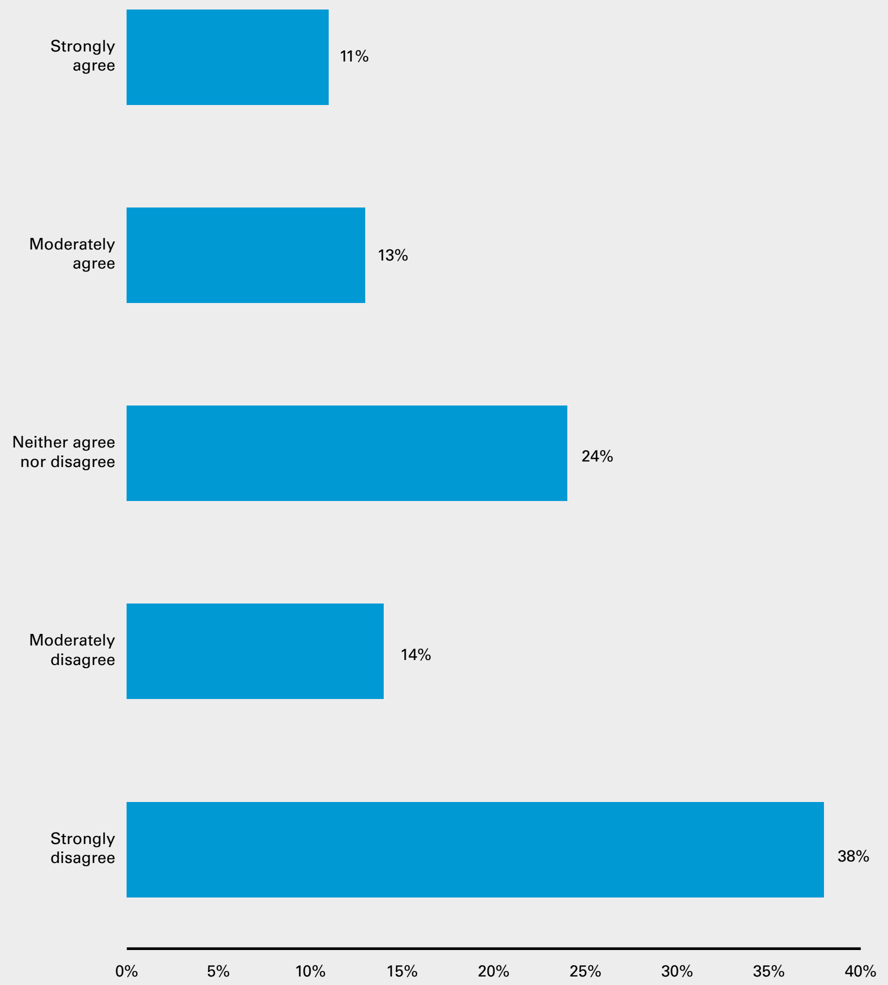
There have been a number of high-profile lapsed deals in 2018, reflecting the concerns of survey respondents. President Trump blocked then-Singapore-based semiconductor firm Broadcom's hostile bid for US peer Qualcomm on national security grounds, and Qualcomm abandoned its bid for NXP Semiconductors after the deal was blocked by Chinese regulators.

Twenty-eight percent of respondents said a deal they have worked on in the past two years has lapsed. Among those respondents, 89 percent say factors uncovered during due diligence caused the deal to fail and 68 percent say changes in market conditions played a role, while 44 percent cited antitrust regulatory issues.

The findings mirror those of a similar survey of 150 technology executives by White & Case, who also cited antitrust and issues uncovered in due diligence as the main causes of failed deals.

While 2018 has been an active year for M&A, buyers are acting carefully, and the increased volatility means that both sides of a transaction may find it difficult to feel confident that they are doing a deal at the right time and for the right price.

Do you agree with legislative changes to expand the jurisdiction of CFIUS to review foreign investments in US businesses?



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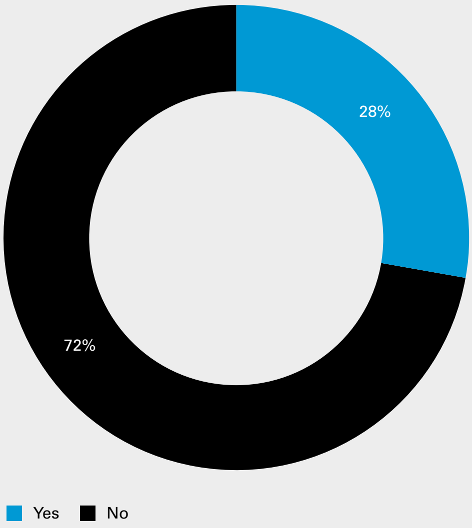
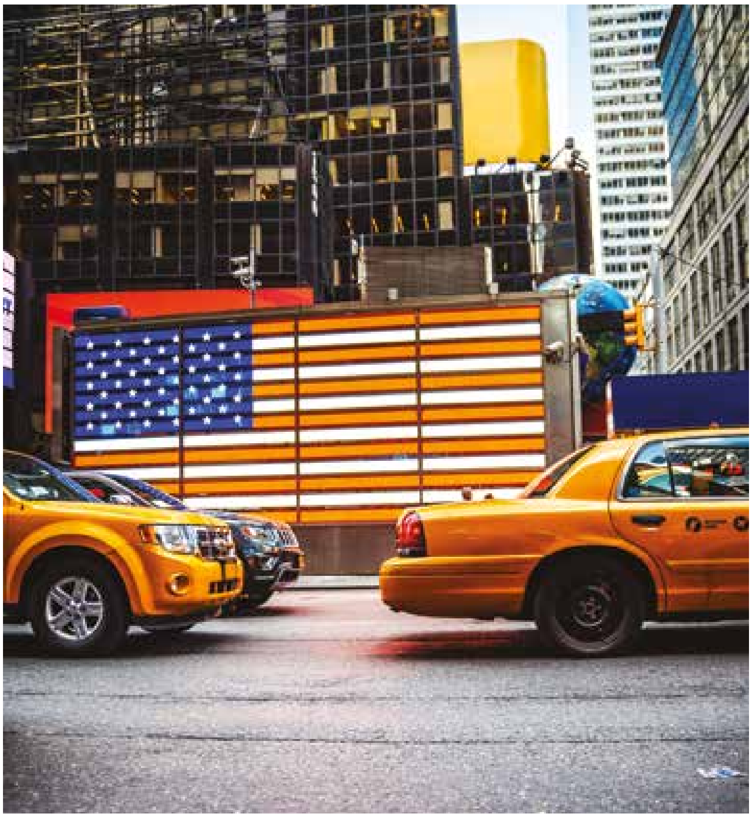
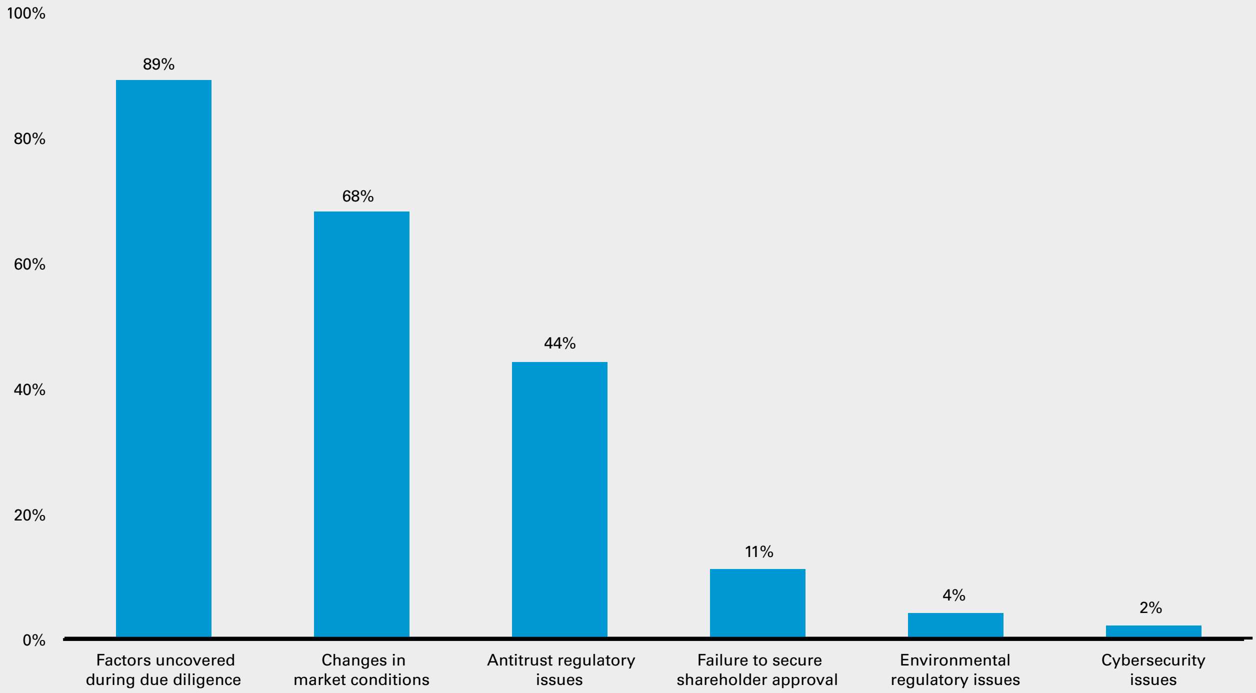
There have been a number of high-profile lapsed deals in 2018, reflecting the concerns of survey respondents.

In the past two years, has a merger or acquisition that your company has announced subsequently been withdrawn or lapsed before completion?





Why did your company's most recent withdrawn or lapsed deal fail to complete? (Select all that apply)



Sectors overview: Tech and energy top the charts

TMT and energy were the top two sectors by value; fintech is poise to invigorate dealmaking in the financial services sector

By John Reiss, Gregory Pryor

Digitalization spreads

US technology M&A totaled US$217.2 billion in deal value in 2018, an 89 percent increase from the previous year, even as the number of deals only increased 2 percent to 1,068 deals during the same period. Large deals such as IBM's US$32.6 billion acquisition of open-source software provider Red Hat were responsible for the jump in value. Even now, after several years of strong tech M&A figures, digitalization is still spreading to different industries. Amazon, for example, this year shook traditional drug stores with its acquisition of PillPack, an online prescription drug-delivery service, as well as an undisclosed stake in video doorbell maker Ring for US$853 million in a reported effort to boost its logistical capability.

With innovation everywhere and companies collecting and using ever more data, technology is poised to receive far greater regulatory scrutiny, which could lead to a fall in M&A in 2019 and beyond.

1,068

Number of deals in the US technology sector in 2018—a 2 percent rise compared with 2017

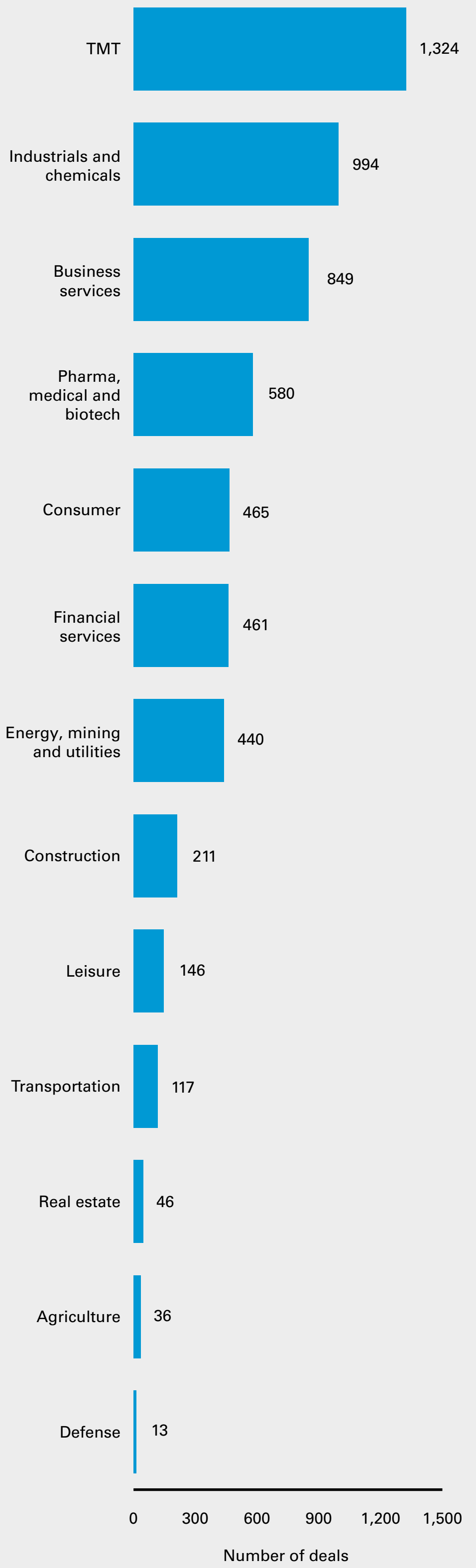
Stable prices fuel energy M&A

With oil prices stable for much of the year, the energy, mining and utilities sector felt comfortable striking deals, leading to a 34 percent increase in deal value, to US$350.1 billion in 2018. Larger deals, such as Marathon's US$31.3 billion acquisition of Andeavor, which created the US's biggest refiner, drove up total deal value, as deal count fell 8 percent to 440 deals compared to 2017. Deal value in the sector was further buoyed by the trend of unwinding master limited partnerships, in deals like Energy Transfer Equity's acquisition of its MLP, Energy Transfer Partners, for US$59.6 billion, the largest deal of the year in the sector.

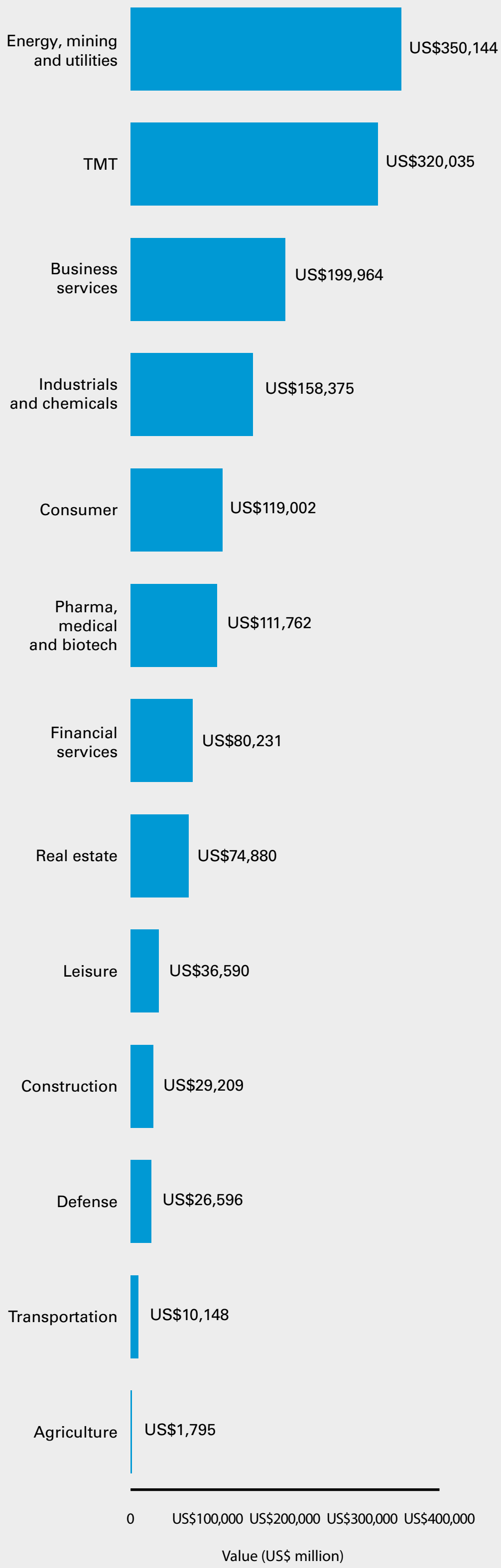
Better days forecast for financial services

Though financial services M&A had a disappointing year, with total deal value declining 48 percent over 2018 to US$80.2 billion, improved growth figures, strong potential in innovative fintech solutions, and a regulatory rollback all point to a recovery in 2019. The lifting of the systemically important financial institution (SIFI) threshold from US$50 billion to US$250 billion in assets, in particular, could encourage M&A among mid-market US banks.

US M&A 2018—sectors by volume



US M&A 2018—sectors by value



Technology M&A value soars in 2018

After a period of frenetic dealmaking in technology over the last few years, which saw businesses across all industries scramble to adjust to the rapid shifts driven by digitalization, 2018 has seen value climb in the tech M&A sector

By Arlene Arin Hahn

Tech M&A value increased 89 percent to US$217.2 billion in 2018, year-on-year. This was a result of an increase in large deals, as volume increased only 2 percent to 1,068 deals during the same period. There have been a number of deal highlights, including IBM's US$32.6 billion acquisition of open-source software provider Red Hat and Saleforce's US$5.9 billion purchase of data and integration platform provider MuleSoft.

Data and cloud services platforms are increasingly attractive as M&A targets. As the amount of data increases, so does demand for the computer power and storage needed to fully leverage that data, driving some of the larger deals in the tech sector in 2018.

The cross-sector convergence trend, meanwhile, which has sparked so many tech deals in recent years, also continued to drive deal flow. Amazon acquired an undisclosed stake in video doorbell maker Ring for US$853 million in a reported effort to boost its logistical capability, while its purchase of PillPack, an online prescription drug-delivery service, reflects its ongoing ambitions to grow its healthcare interests.

Tech under regulatory inspection

Although the deal fundamentals supporting tech transactions remain in place, the sector has been weighed down by growing regulatory concerns around the impact of inbound tech purchases on national security.

A proposed deal involving chipmaker Broadcom, based at the time in Singapore, and its US rival Qualcomm, which would have been the largest-ever tech deal, was blocked by the White House on national security grounds. As technology becomes increasingly embedded across all aspects of life and tech companies continue to gather data on billions of citizens, deals in the sector are likely to face increased regulatory scrutiny, particularly when foreign buyers are involved.

US $217.2 billion

The value of 1,068 deals targeting the US tech sector in 2018

89%

Percentage increase in tech M&A value compared to 2017

Top tech deals FY 2018

1. IBM acquires Red Hat for **US$32.6 billion**
2. Broadcom acquires CA Technologies for **US$18 billion**
3. Microchip Technology acquires Microsemi for **US$9.8 billion**

Consumer deals slip as digital disrupts

Digital disruption and its impact on physical retailers once again weighed on the consumer sector in 2018. Consumer M&A volume was down 13 percent year-on-year to 465 deals in 2018. Value decreased 28 percent to US$119 billion

By Gary Silverman, Ray Bogenrief

Retail consumer behavior has undergone a seismic shift as a result of technology, and the survival of the traditional retail consumer business is in question.

Well-known retail brands such as Sears and Carson's, which both went into bankruptcy in 2018, and Toys 'R Us, which was saved from going bust at the 11th hour after a period of heavy restructuring, were some of the iconic retail brands hit by the shift in spending from bricks-and-mortar to online.

New channels, new products

When traditional retailers have pursued deals, they have either sought to boost their online offerings, as seen in deals like Walmart's US$16 billion acquisition of Indian online retailer Flipkart, or to increase foot traffic.

The consumer sector has been more stable than retail, and multinational consumer corporations have had the confidence to pursue megadeals that expand their presence in key markets and product verticals.

Keurig Green Mountain, the coffee group owned by European investment vehicle JAB Holdings and others, acquired Dr Pepper Snapple Group for US$26.8 billion to strengthen its position in the US beverage market, while the second-largest deal of the year saw tobacco company Altria buy a 35 percent stake in JUUL, the manufacturer of a trendy electronic cigarette, for US$12.8 billion.

Looking ahead to 2019, the outlook for M&A in the sector is mixed. On the downside, potential tariffs could increase costs and hit consumer spending. Meanwhile, an increase in interest rates could put a squeeze on financing.

However, technology and changing consumer tastes are transforming the sector all the time, and businesses will need inorganic growth to stay ahead of the curve. Corporates still have an abundance of cash on the balance sheets and are willing to buy. In addition, the positive dynamics in the market for sellers mean that private equity will be selling portfolio companies into the market. While there may be some caution around macroeconomic trends in the early part of the year, the need to stay on top of changing trends will continue to drive the market forward.

US $119 billion

The value of 465 deals targeting the US consumer sector in 2018

28%

Percentage decrease in consumer M&A value compared to 2017

Top consumer deals FY 2018

1

Keurig Green Mountain acquires Dr Pepper Snapple Group for **US$26.8 billion**

2

Altria acquires a 35 percent stake in JUUL Labs for **US$12.8 billion**

3

ConAgra Brands acquires Pinnacle Foods for **US$10.8 billion**

Financial services deals are down, but 2019 brings hope

Financial services sector M&A volume decreased by 6 percent to 461 deals in 2018, with value decreasing 48 percent to US$80.2 billion. But there are signs that the sector's M&A market is moving in the right direction going into 2019

By Ben Saul

Congress and the Federal Reserve have moved to ease some of the tough regulation imposed on financial institutions following the financial crisis, and after years spent retrenching to domestic markets and rebuilding balance sheets, banks and insurers are moving back into the black. According to the Federal Deposit Insurance Corp (FDIC), Q3 US bank net income climbed to US$62 billion, a 29.3 percent increase compared to the same period last year.

As part of the regulatory rollback, the definition for what constitutes a systemically important financial institution (SIFI) was changed from institutions with at least US$50 billion in assets to those with at least US$250 billion. The raising of this threshold eased a major deterrent to banking M&A, especially for mid-size US banks, which, under the previous regulatory regime, had been wary of becoming subject to much more onerous requirements with respect to capital and liquidity.

Back to growth

As lenders have returned to profitability and regulation has rolled back, banks have shifted their focus to growth. Fifth Third Bancorp's acquisition of Chicago-based MB Financial for US$4.6 billion is its largest deal since 2001 and third-largest ever. The MB Financial deal will increase the bank's presence in one of its core growth markets. Meanwhile, at the end of January this year, two Midwest banks, Chemical FInancial and TCF Financial, joined forces in a deal worth US$3.6 billion. The merger will create one of the biggest banks in the MIdwest region.

In the insurance sector, institutions have also turned to M&A to drive growth. Lincoln National's purchase of rival insurer Liberty Life Assurance Company of Boston for US$3.3 billion has positioned it as the US's largest provider in fully insured disability sales with a group benefits business serving some ten million customers.

Further opportunities in fintech

In addition to a rise in M&A involving traditional financial institutions, deal activity in financial services has also been lifted by the emergence of the fintech industry. Concerns around how fintechs will be regulated has given some banks pause when considering fintech deals, but with the likes of Goldman Sachs acquiring personal finance startups like Final and Clarity Money, US financial institutions have accepted that they need to serve the digital needs of customers with new platforms and modern services.

According to CB Insights, 40 of the 50 largest banks in the US made no fintech investments in the five-year period from 2013 to the beginning of 2018. The ten banks that had invested in fintech had made only 18 such deals between them, but five of these deals came in 2017 alone, suggesting that higher volumes of fintech deals could be on the way as banks move to upgrade their platforms.

Fintech allows financial institutions to reduce their costs as well as gain more of their customers' wallet shares. In addition to helping financial services companies open new distribution channels, fintech can also help back-office functions, such as reducing the risk of identity fraud.

US $80.2 billion

The value of 461 deals targeting the US financial services sector in 2018

48%

Percentage decrease in financial services M&A value compared to 2017

Top financial services deals FY 2018

1. Invesco acquires OppenheimerFunds for **US$5.7 billion**
2. Fifth Third Bancorp acquires MB Financial for **US$4.6 billion**
3. Lincoln National Corporation acquires Liberty Life Assurance Company of Boston for **US$3.3 billion**

Stability in early 2018 fuels oil & gas M&A

A stable oil price (for the majority of 2018) saw deal value climb in the energy, mining and utilities sector in 2018, despite volume falling

By Steven Tredennick

Energy, mining and utilities deal value climbed by 34 percent to US$350.1 billion over 2018, despite deal volume falling 8 percent year-on-year to 440 transactions.

The oil & gas industry, which benefited from an oil price that,for most of the year, had stabilized at approximately US$60 per barrel, was the primary driver of the increase in deal value. Oil majors with good cash balance sheets felt more comfortable taking a view on the targets that would deliver long-term growth, many shifting towards long-term shale-producing assets, and away from assets like those in the Gulf of Mexico.

Refiner Marathon Petroleum Corporation, for example, acquired rival Andeavor for US$31.3 billion, while BP placed a bet on the long-term viability of shale with the US$10.5 billion purchase of Petrohawk, a portfolio of US shale assets, from BHP Billiton. Transactions unwinding master limited partnership structures, such as Energy Transfer Equity buying a 97 percent stake in Energy Transfer Partners for US$59.6 billion, also lifted headline figures.

Companies returning cash to investors attracted increased investment over 2018, allowing them to raise the capital to execute deals.

Further volatility ahead

A sharp fall in the price of oil towards the end of 2018, when the price per barrel dipped below US$50, however, could put a brake on the steady M&A activity observed in the sector in 2018.

With investors expecting as much as IRRs of 20 percent over three years, renewed volatility in oil prices may slow transaction activity.

US $350.1 billion

The value of 440 deals targeting the US oil & gas sector in 2018

34%

Percentage increase in deal value compared to 2017

Top oil and gas deals FY 2018

1. Energy Transfer Equity acquires Energy Transfer Partners (97.64 percent Stake) for **US$59.6 billion**
2. Marathon Petroleum Corporation acquires Andeavor for **US$31.3 billion**
3. Dominion Energy acquires SCANA for **US$14.3 billion**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Real estate rises higher on megadeal surge

Real estate M&A value jumped 116 percent to US$74.9 billion in 2018, with deal volume staying flat at 46 deals

By Eugene Leone, David Pezza

The large spike in value in the real estate sector has been driven by attractive pricing on prime assets that has resulted from falling stock prices.

The disparity between stock prices and underlying real estate values has led over the past year to a decrease in single-property transactions and an increase in transactions involving portfolio companies.

Declining stock prices have been particularly acute in the retail sector. Brookfield, the Canada-based alternative assets manager, for example, took control of General Growth Properties (GGP), the second-largest shopping mall owner in the US, in a US$26.7 billion deal. Valuations for retail property have plummeted, as e-commerce keeps shoppers at home and retailers close stores. Investors like Brookfield, however, see an opportunity to invest and redevelop sites in attractive urban locations.

Many companies holding retail assets are facing pressures as a result of tensions in the wider physical retail business. However, occupancy levels in prime locations remain strong, and in areas that have seen some large retailers leave, there are opportunities for redevelopment and the potential for good returns on investment.

PE turns to real estate

Private equity managers, meanwhile, have raised huge levels of cash for real estate strategies. According to data provider Preqin, there is at least US$266 billion worth of real estate dry powder available for deals, pushing up private equity activity in the sector. Blackstone, for example, acquired LaSalle Hotel Properties in a US$3.7 billion buyout.

The influx of private equity into the sector has led to an increase in M&A activity—and larger deals. Large, well-capitalized investors are capable of taking down dozens of properties in a single transaction whether as a portfolio transaction or a corporate acquisition.

As for what to expect in 2019, industrial real estate is one category that will continue to attract interest from investors. Such properties are solid performing assets that are set to appreciate steadily year after year. There is strong demand for industrial space to house distribution centers close to cities. There are just not enough good sites, and demand continues to outstrip supply.

US $74.9 billion

The value of 46 deals targeting the US real estate sector in 2018

116%

Percentage increase in value of US real estate M&A compared to 2017

Top real estate deals FY 2018

1. Brookfield Property Partners acquires General Growth Properties (66.2 percent stake) for **US$26.7 billion**
2. Brookfield Asset Management acquires Forest City Realty Trust for **US$9.5 billion**
3. Prologis acquires DCT Industrial Trust for **US$8.06 billion**

Next big thing drives healthcare M&A

Although deal volume and value in the pharma, medical and biotech sector fell in 2018, down by 3 percent to 580 deals and 27 percent to US$111.8 billion respectively, pharma companies have invested aggressively in strategic deals throughout the year

By Morton Pierce

Companies are under pressure to renew pipelines as drugs go off patent and to keep pace with new treatment technologies. Companies in the sector have also encountered a squeeze on pricing, with the Trump administration pressuring the industry to keep prices down. In May, the President put forward proposals obliging firms to list prices in advertisements and took a tough stance against companies trying to delay drugs coming off patent.

Buying drug pipelines

In response to these challenges, pharma groups continue to use M&A to add new drugs and technology to their portfolios and stay on top of costs.

For the pharma industry, it is imperative to continuously regenerate product pipelines, as a way for companies to protect themselves against competition and generics. Specialty drugs, gene-based drugs and interventional medicines are especially difficult to develop, and therefore make attractive M&A targets.

French group Sanofi, for example, paid US$10.9 billion for Bioverativ, a haemophilia specialist, to increase its presence in the rare diseases market. Novartis added AveXis, a gene therapy business focused on rare and life-threatening neurological genetic diseases, to its portfolio in a US$7.4 billion deal, and GlaxoSmithKline announced it would acquire oncology-focused biotech Tesaro for US$5.1 billion.

This appetite for gene-based and specialty therapeutics is continuing. In the first few weeks of 2019, Eli Lilly announced the US$7.1 billion acquisition of Loxo Oncology, which develops drugs for genetically defined cancers.

Nor was this the only significant healthcare deal so far in 2019. On the third day of the year, Bristol-Myers announced it would acquire biopharmaceutical company Celgene for US$89.5 billion. The two companies have complementary portfolios and the deal would expand a number of Bristol-Myers's assets and ensure another healthy year for healthcare M&A.

Contract research organizations consolidate

The contract research organization (CRO) provider space has also performed strongly, as pharma companies increasingly outsource complex protocols for drug development and approval to third-party experts. This has encouraged consolidation, as CROs seek scale to serve a global customer base across a range of treatment areas. Charles River Laboratories, for example, has moved to strengthen its offering with the acquisition of MPI Research for US$800 million.

Healthcare companies are streamlining processes as much as possible and looking to refocus on their core businesses and products.

US $111.8 billion

The value of 580 deals targeting the US pharma, medical and biotech sector in 2018

3%

Percentage decrease in deal value compared to 2017

Top healthcare deals FY 2018

1. Sanofi acquires Bioverativ for **US$10.9 billion**
2. Kohlberg Kravis Roberts acquires Envision Healthcare for **US$9.4 billion**
3. Celgene acquires Juno Therapeutics, Inc. (90.37 percent Stake) for **US$8.8 billion**

Deal-changing decisions from Delaware

In the second half of 2018, the Delaware courts once again produced decisions that will guide M&A transactions in the future

By Daniel Kessler

There were three cases affecting US M&A that stood out in 2018.

1. First-of-its-kind Material Adverse Effect ruling

The Delaware Supreme Court recently affirmed a first-of-its-kind decision by the Delaware Chancery Court, ruling that German pharmaceuticals company Fresenius Kabi AG was not required to close its US$4.3 billion merger agreement with pharmaceutical company Akorn Inc. because, after signing, Akorn suffered a Material Adverse Effect.

In April 2017, Fresenius entered into a merger agreement to acquire Akorn. Under the agreement, Fresenius agreed to acquire Akorn for US$34 per share, subject to certain customary closing conditions, including Akorn not suffering an MAE and Akorn's representations being true and correct at closing except as would not reasonably be expected to have an MAE.

Immediately after signing the agreement, despite showing persistent growth over the previous five years, Akorn's financial performance "dropped off a cliff" (for the full year 2017, Akorn's revenue, operating income and earnings fell by 25 percent, 105 percent and 113 percent respectively).

Moreover, in October of 2017, Fresenius received anonymous whistleblower letters alleging pervasive flaws in Akorn's data integrity systems, and, after engaging an investigative team that found significant issues, Fresenius notified Akorn that it was terminating the agreement. In response, Akorn filed a claim against Fresenius in the Chancery Court requesting specific performance of the merger, while Fresenius counterclaimed that it had terminated the agreement in accordance with its terms.

The Chancery Court ruled that Fresenius had properly terminated the merger agreement. In determining that Akorn had suffered an MAE, the Chancery Court noted that an MAE must "substantially threaten the overall earnings potential of the target in a durationally significant manner", and that the relevant period is "measured in years rather than months"—Akorn's downturn had subsisted for a year and showed no signs of abating.

In also determining that Akorn had breached its representation to be in full compliance with its regulatory obligations, and such breach would reasonably be expected to result in an MAE, the Chancery Court noted that Akorn's regulatory issues were both qualitatively and quantitatively material (US$900 million in this case, which was a 21 percent decline in Akorn's implied equity value)—however, the Chancery Court stressed that it was not establishing a "bright-line test".

The Supreme Court affirmed the Chancery Court's findings concerning the occurrence of an MAE, though specifically declined to "address every nuance of the complex record".

Importantly, the Akorn decision is regarded as the first Delaware decision to find that a buyer may use an MAE clause to terminate an acquisition. On the one hand, the case demonstrates the extreme circumstances that are required before a buyer may use an MAE clause to terminate an acquisition. However, on the other hand, it also demonstrates the importance of carefully drafting and negotiating a provision in an acquisition agreement that many parties have traditionally regarded as being merely formalistic.

2. Deal price less synergies drives fair value determination

In an important appraisal decision, the Chancery Court rejected the argument of certain shareholders of digital technology business Solera Holdings, that the value of their shares when exercising appraisal rights should be calculated solely using a discounted cash flow analysis. The court instead concluded that the deal price, which was achieved in an arm's-length and open sales process, after adjusting for synergies, was the most reliable evidence of the fair value of the shareholders' shares.

After Vista Equity Partners acquired Solera at a price of US$55.85 per share, certain of Solera's shareholders exercised appraisal rights requesting that the Chancery Court determine the fair value of their shares. Such shareholders argued that the fair value of their shares was

US$84.65 based on a discounted cash flow analysis. Meanwhile, Solera argued that the fair value was the deal price less synergies, which was US$53.95 per share.

The Chancery Court decided in favor of Solera. In reaching a conclusion that the deal price less synergies was the appropriate method of determining fair value, the determinative factors included the following:

- Solera's sale process involved robust public information concerning the company (including the view of analysts, buyer and debt providers)
- A deep base of public shareholders
- Easy access to non-public information for potential buyers
- Cooperation from management
- A special committee composed of independent and experienced directors that had the power to say "no", advised by competent legal and financial advisors
- The sale was achieved in an arm's-length transaction with a third party

With respect to synergies, the Chancery Court agreed with Solera's argument that a financial buyer, like a strategic buyer, could realize synergies in connection with a transaction, and subtracted the estimated synergies of US$1.90 from the deal price of US$55.85 in reaching its conclusion that the fair value of Solera's stock was US$53.95 per share.

The decision should give increased comfort to buyers that the deal price in an arm's-length transaction from a fair and open sales process will be given significant deference by Delaware courts in appraisal proceedings.

In addition, the decision shows that in certain circumstances, financial buyers can argue that the fair value of a shareholder's shares in appraisal is, in fact, less than the deal price based on the synergies that the financial buyer expected to realize from the transaction.

3. Clarification of "Ab Initio" requirement

The Delaware Supreme Court clarified the circumstances under which a party can obtain the benefit of business judgment rule treatment (and avoid the more stringent "entire fairness" standard) in connection with controlling stockholder transactions.

In *Kahn v. M&F Worldwide Corp ("MFW")*, the Supreme Court had previously ruled that the business judgment rule applies to a controlling shareholder transaction if such transaction is conditioned "ab initio" upon the approval of the informed vote of a majority of the minority shareholders and upon the approval of an independent special committee of directors.

In the October 2018 case of *Flood v. Synutra International, Inc*, the Supreme Court clarified that the controlling shareholder satisfied MFW's "ab initio" requirements by conditioning the transaction on such requirements before substantive economic negotiations had begun.

In *Flood*, Liang Zhang and his affiliates controlled 63.5 percent of Synutra's stock. In January 2016, Zhang wrote a letter to the Synutra board proposing to take the company private, but did not provide that such transaction would be conditioned on the safeguards established in MFW (i.e., the informed vote of a majority of the minority shareholders and the approval of an independent special committee of directors). One week after receipt of the letter, the board formed a special committee to consider the offer, and one week after that, Zhang sent a second proposal with the same economic terms, but this time conditioning his offer on the MFW procedural safeguards. After another eight months, the special committee and Zhang agreed on a price of US$6.05 per share.

The plaintiff minority shareholders argued that because the MFW procedural safeguards were not included in Zhang's initial letter, the "ab initio" requirement of MFW was not satisfied and as such, the business judgment standard of reviewing the transaction had been forfeited.

The Supreme Court affirmed an earlier Chancery Court decision that the business judgment rule applied. The Supreme Court ruled that "ab initio" should not be understood as meaning any fixed point in time, but should be understood as meaning the early stages of a transaction up until substantive economic negotiations commence. In this case, the committee only began substantive negotiations with Zhang regarding price after seven months of due diligence, so economic negotiations had clearly not begun until after Zhang sent his second proposal, which conditioned his offer on the MFW procedural safeguards.

Why, how and when should directors engage with shareholders?

Activism among investors is on the rise across the globe. Companies that empower directors to engage with shareholders can optimize investor relations, if they follow some simple but important guidelines

By Michelle Rutta

Over the past half-decade, shareholder activism has become a staple of corporate life. Formerly passive institutional investors have developed strong governance profiles and are more assertive than ever. Meanwhile, environmental and social issues have become priority matters for many shareholders. As a result, board members are increasingly being asked to engage directly with shareholders. In the 2018 PWC Annual Corporate Directors Survey, almost half (49 percent) of public company directors stated that a member of their board (other than the CEO) engaged directly with investors in 2018 (up from 42 percent in 2017).

Director engagement allows shareholders to express their concerns while also gaining the board's perspective on issues such as strategic planning. It also gives the company an opportunity to learn about shareholder priorities, and changes in investor sentiment. It also creates goodwill by demonstrating that the company appreciates and values shareholder input.

However, the board needs to plan engagements carefully, by asking and answering the following eight questions:

When should the meeting take place?
A quieter time, outside of proxy season, is usually a good time to request a meeting. In periods outside the proxy season, engagement can help establish rapport and relationships before an issue arises. Late summer through fall is relative downtime for most institutional investors.

Who should directors be talking to?
It is generally prudent to visit with the largest shareholders, as well as other influential or proactive shareholders such as pension funds.

What should be on the agenda?
The company should collaborate with shareholders on the attendees and the list of topics to be covered. Shareholders generally want to hear about long-term strategic vision and significant drivers of growth, in addition to relevant environmental, governance and social issues.

When should directors attend?
Director attendance is not necessary at every shareholder meeting. If issues related to compensation, board refreshment/composition, internal controls over financial reporting, capital allocation or strategic alternatives are on the agenda, the relevant director who can speak to these issues should attend. Consideration should also be given to the directors' communication skills, knowledge and experience addressing investors.

How should directors prepare?
Directors should understand the investors' holdings, their views on governance issues and whether and how they use proxy advisory firms.

Directors should be well versed in the company's position on the agenda topics, and should have the necessary information to explain and support that position. Directors should also be reminded about Regulation FD's prohibitions on the selective disclosure of material non-public information and about legal restrictions on insider trading.

Meetings should never be conducted alone. It is generally appropriate for someone from investor relations to attend any meeting with shareholders, and other participants may include the general counsel or corporate secretary, or the CFO and/or CEO, as appropriate.

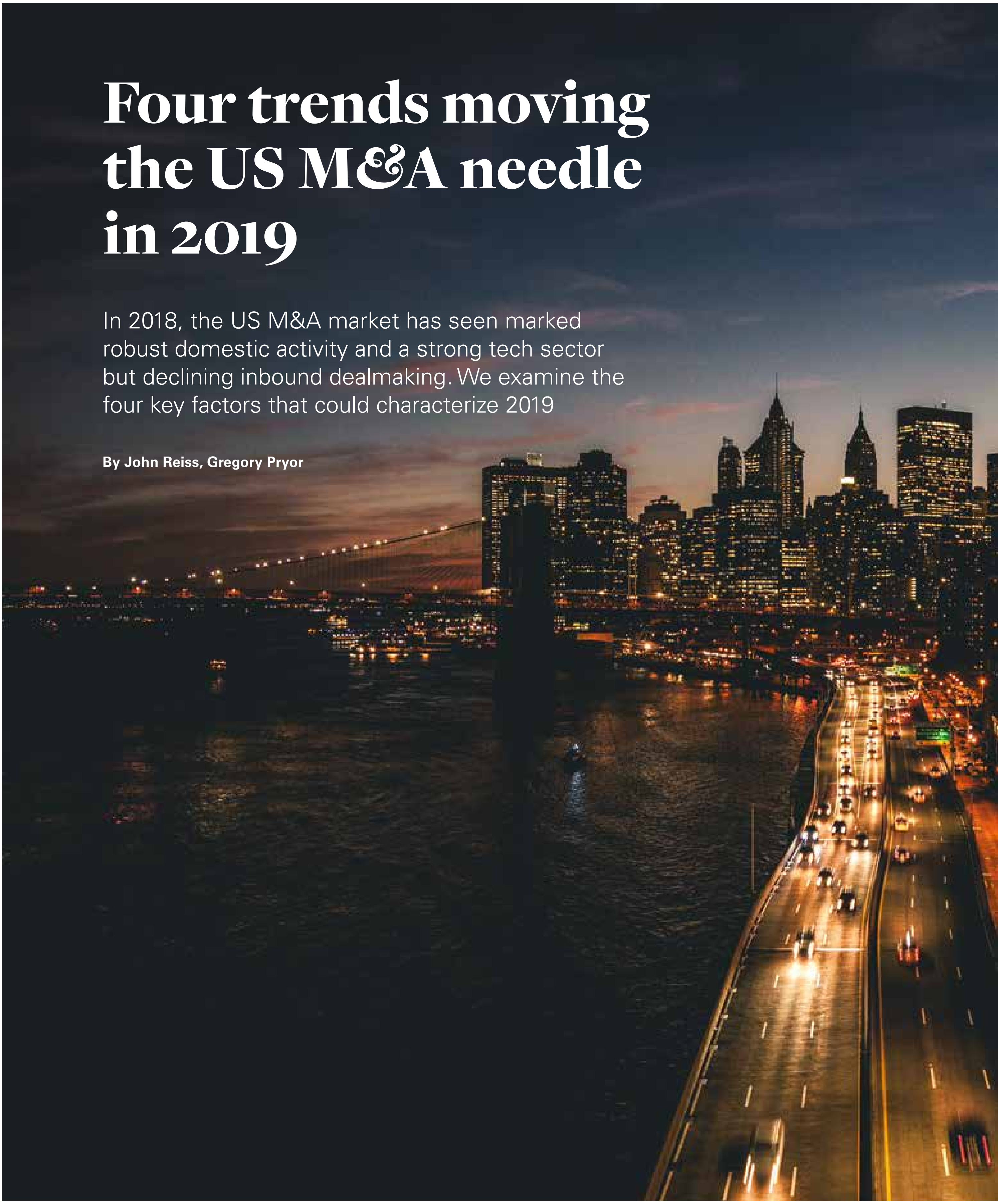
How should directors approach the meeting?
Shareholders want to leave the meeting feeling confident that the board understands their concerns, so they must be permitted to express their opinions. Directors should listen with an open mind, and relay the shareholders' perspectives back to the board.

How should directors follow up the meeting?
Directors should bring shareholders' concerns to the board for discussion and consideration. In addition, they should work with management to formulate responses to any follow-up requests from shareholders.

How should companies reflect shareholder engagement in proxy disclosures?
Management should use the company's proxy statement to give a complete picture of the company's engagement efforts. This may include detailing the number or proportion of shareholders with whom meetings were held; listing the topics discussed during the meetings; and noting the changes the company is considering as a result of these meetings (or the reasons for not implementing suggested changes). Companies should also consider shareholder priorities when drafting proxy disclosure generally. Utilizing the proxy statement to provide insight into areas of investor concern can serve as another way to communicate effectively with shareholders.

Shareholder engagement can prove invaluable to all parties. Shareholders can learn the company's approach to long-term growth and strategic planning, and gain confidence that the company is open to hearing their suggestions. Directors can better understand shareholder concerns and the driving forces behind their voting decisions. Moreover, engagement can be particularly valuable for the company in establishing a baseline of support from investors should a crisis arise in the future.

"Shareholders generally want to hear about long-term strategic vision and significant drivers of growth, in addition to relevant environmental, governance and social issues.



Four trends moving the US M&A needle in 2019

In 2018, the US M&A market has seen marked robust domestic activity and a strong tech sector but declining inbound dealmaking. We examine the four key factors that could characterize 2019

By John Reiss, Gregory Pryor

The past year has been mixed for US M&A markets. Deal value is up by more than a quarter and domestic dealmaking is thriving. However, inbound deal activity, by contrast, has plummeted and dealmakers are wary about the impact that tariffs, a tougher CFIUS regime and a downshift in the cycle could have on deal markets in the year ahead.

Here are four trends that will shape dealmaking in 2019:

1

Domestic market remains buoyant

Domestic transactions are likely to thrive in 2019. Corporate balance sheets are still healthy, which could enable companies to pursue deals, despite geopolitical and economic uncertainty.

Our survey bears this out. More than three-quarters of respondents see the US as the most attractive country for M&A in the next 12 months. And many feel that a stable economy and moderate GDP growth will lead to an increase in domestic dealmaking. Meanwhile private equity is becoming even more competitive and has near-record dry powder to put to use. The battle for the best assets is likely to drive valuations even higher, but even high prices are not likely to deter more determined dealmakers.

2

Global risks present overhang

The Trump administration's protectionist inclinations, the looming possibility of continuing trade wars between the US and its biggest trading partners, the ongoing struggles to define Brexit, the rise of global debt and, most importantly, the risk of a recession—all represent a considerable overhang when considering M&A in 2019. Against this backdrop, a downturn in dealmaking is inevitable, but predicting its timing is difficult. Buyers and sellers will likely take these factors seriously and proceed with caution in coming months. Yet, the dealmakers that we surveyed have shown considerable optimism. The vast majority of respondents predict moderate growth in the US economy in 2019, and 94 percent say that their company's appetite for M&A has increased thanks to the Trump administration's tax reforms. If we're lucky, the downturn won't materialize until 2020.

3

More lapsed deals

Despite the anticipated rise in domestic deals, there are reasons to be wary. Even though economic headwinds are building, deal multiples remain stubbornly high and the margin for error on entry evaluation is narrow. As a result, buyers may be looking over assets in increasingly fine detail and stepping away when any wrinkles in a deal emerge. Don't be surprised if the number of broken deals and failed auction processes increase, as buyers think twice about paying up when processes hit a snag.

4

Inbound deal flow falls further

The last year has been a difficult one for inbound investors, and things are likely to get worse for foreign buyers in 2019. Tariffs will make global companies with international supply chains think twice about pursuing US deals, and overseas investors face tougher scrutiny from regulators who are worried about the national security risks that could emerge from foreign ownership.

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