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GETTING THE DEAL THROUGH

market intelligence

M&A

Global interview panel led by Alan Klein

Tech riding high

Sector focus • Keynote deals • Shareholder activism • 2017 forecast
Europe • The Americas • Asia-Pacific • Africa

M&A IN SOUTH AFRICA

Ezra Davids is the chairman of the corporate and M&A department at Bowmans, specialising in mergers and acquisitions, capital market and securities law. Some of the most recent transactions in which Ezra has advised in include his role as co-lead partner in the firm acting as South African counsel to SAB Miller in its proposed combination with AB InBev (1.5 trillion rand); as the lead partner for Tokyo Stock Exchange listed Kansai Paint Co Limited in its successful hostile bid for JSE Listed Freeworld Coatings Limited (3.3 billion rand); as lead partner advising PPC (the largest cement company in South Africa) in successfully defending itself in the most high-profile shareholders' activism in South Africa; as lead South African counsel to Bharti in its then proposed merger with MTN (US$24 billion); as lead partner advising Verizon Communications in its disposal of its subsidiary, Verizon Business (South Africa); acting as South African Counsel to M1 and Investcom in the latter's acquisition by MTN (US$5.5 billion); advising Barrick Gold Corporation in its disposal of Barrick Gold South Africa (US$1.55 billion) and acting for Goldman Sachs and Citigroup in the disposal by Polyus (Norilisk) of its entire shareholding in Gold Fields Limited (US$2.02 billion); acting for SABMiller in the US$1 billion BEE transaction for its South African subsidiary; acting for Old Mutual Plc in the aborted negotiations related to the acquisition by HSBC control of Nedbank Limited; and acting as South African counsel for PPR in the disposal of its furniture and household goods business, Conforama, to JSE-listed Steinhoff International Holdings Limited (12 billion rand).

Ezra also became the first practising African lawyer to make the full cover of *American Lawyer*. In 2015, *Chambers and Partners* ranked Ezra in Band 1 for mergers and acquisitions and equity capital markets. He is also ranked as a leading lawyer by *IFLR1000* 2016.

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What trends are you seeing in overall activity levels for mergers and acquisitions in your country during the past year or so?

Ezra Davids: International and Africa-led cross-border acquisitions continue to be on the rise across Africa, as the potential of African economies continues to be recognised. Investors, however, have become more selective and strategic about the jurisdictions in which they invest, no longer looking at Africa's success story as a whole but assessing Africa's potential with specific consideration of the growth and stability of individual countries. Private equity and venture capital activity in South Africa has intensified in 2016, building on the momentum of 2015, with investors seeking to focus on and use technology for M&A analysis and to increase competitiveness (as recognised by other professional advisers in South Africa including Deloitte).

Which sectors have been particularly active or stagnant? What are the underlying reasons for these activity levels? What size are typical transactions?

ED: M&A activity within the financial services, telecommunications, pharmaceuticals and healthcare, energy and private equity sectors continue to operate at an energetic level in South Africa. The continued urbanisation of Africa has translated into a rapid growth in consumption and the construction, energy, pharmaceuticals and healthcare, retail (including food and beverages) and financial services sectors are expanding swiftly. This trend has been reflected in the research findings of Business Monitor International (BMI).

Typical transaction sizes average around US$250 million.

Technology and telecoms remains an ever growing and robust sector as sub-Saharan Africa, and Africa in general, offers strong growth opportunities and potential for mobile data and voice service providers. M&A within this sector has been favourably affected as operators streamline their operations and strategies with the aim of operating more cost effectively. BMI research reflects these trends. Liquid Telecommunications Holdings' recently announced acquisition of Neotel demonstrates a continued belief by operators in this sector in the ambition and potential of African businesses. The South African government's upcoming policy on the creation of a single national wholesale open-access network aimed at encouraging competition and driving down broadband prices means that the landscape of this sector is constantly developing, and that the strategies of the players in the industry will similarly need to constantly evolve.

Financial service providers are continuing to innovate, which has translated into interesting and fast-paced M&A activity in this sector. Major international banks continue to seek advice in relation to, and implement, financial services transactions involving regulatory considerations and filings across the continent. Technology companies such as IRESS have invested in acquiring South African technology companies that provide live and reliable African financial markets data and analysis through products and services akin to those provided by Bloomberg, but with a particular Africa flavour.

Growth opportunities within the food and beverage sector in Southern Africa continue to abound, including in relation to the consumption of beer and malt products. Companies with diverse portfolios (including low-cost entry-level products and premium beer offerings from international brewers) and a strong geographic presence, such as SABMiller, are expected to flourish in 2017. The US$107 billion acquisition of SABMiller by ABInBev demonstrates the potential recognised by international players in the sector and the voracity of their pursuit. The combination of The Coca-Cola Company, SABMiller and Gutsche Family Investments' (majority shareholders in Coca-Cola SABCO) bottling operations in Southern and East Africa to create Coca-Cola Beverages Africa, the biggest bottler of soft drinks in Africa and the 10th largest in the world, with annual revenue of US$2.9 billion, is another example of the avid attention that this sector is receiving.

Chinese investment in sub-Saharan Africa's energy and infrastructure sector remains strong. South Africa, like the rest of sub-Saharan Africa, is turning to nuclear technology to improve energy security. The Chinese have invested significantly in this sector in commitment to their 'Going Global' investment strategy. Investment in this sector is likely to be a marathon, not a sprint, as project implementation risks and delays continue to plague infrastructure and energy development. Competing with China's bid to increase its footprint in Africa, Japan similarly aims to invest heavily in infrastructure in Africa, following its announcement in August 2016 at the Sixth Tokyo International Conference on African Development in Nairobi that it will invest US$30 billion in Africa over the next three years to boost Africa's economic growth and infrastructure. According to Japanese Prime Minister Shinzo Abe, approximately US$10 billion of Japan's planned investment is earmarked for electricity generation projects and upgrading urban transport systems and ports. Interesting M&A activity in the energy and infrastructure sector is expected in the wake of the competitive investment environment which the Chinese and Japanese are creating.

Investor confidence in other historically strong sectors in South Africa has tapered off during 2016 because of regulatory, economic and political concerns.

Ezra Davids

What were the recent keynote deals? What made them so significant?

ED: The US$106 billion acquisition of SABMiller by ABInBev was a keynote transaction for 2016. As the third-largest corporate takeover deal and the largest of a London-listed company, the transaction was significant on a global scale. It had many unique and noteworthy features, including a significant break fee (one of the largest to date in London).

On the outbound, Steinhoff's acquisition of Poundland, a UK-based variety store chain, and Truworths' acquisition of Office Retail Group, a UK-based fashion footwear chain, continued the foray of South African retailers into the UK and Europe in general.

In your experience, what consideration do shareholders in a target tend to prefer? Are mergers and acquisitions in your country primarily cash or share transactions? Are shareholders generally willing to accept shares issued by a foreign acquirer?

ED: Cash considerations (either on a fixed price basis or through a financial adjustment) are favoured by shareholders in South Africa. That being said, considerations in relation to the ultimate pricing model varies depending on the transaction and changes in South Africa's exchange control regime may give rise to a greater appetite by shareholders for share-for-share transactions.

How has the legal and regulatory landscape for mergers and acquisitions changed during the past few years in your country?

ED: South Africa's company law for both listed and unlisted companies is governed by the Companies Act, which came into effect in 2011. Significant changes were introduced at that time to the legal landscape in relation to mergers and acquisitions, including in relation to disposals of all or a greater part of a company's assets, schemes of arrangement, compulsory acquisitions of minority stakes (or squeeze-out provisions) and statutory merger procedures. During the past five years, the practicalities and nuances in the new aspects of merger and acquisition law, and company law in general, have been explored, sense checked, tested and developed by companies in their operations. South African company law pertaining to greater accountability, social responsibility, stakeholder rights and takeovers and mergers is constantly developing through case law and academic interrogation.

Legislation and regulation relating to the regulation of exchanges and securities, insider trading, market abuse, marketing of securities and the custody and administration of securities also continues to develop under the Financial Markets Act. The Financial Services Board (FSB) is mandated with promoting and maintaining a sound financial investment environment in South Africa. Financial institutions relating to insurance, securities services, pension funds, friendly societies and collective investment schemes are regulated by the FSB. In South Africa, it has been proposed that the FSB becomes exclusively a market conduct regulator and a new and separate regulator be created for prudential matters (akin to the UK 'Twin Peaks' model). While developments in this regard are yet to unfold, increased regulation and the red tape inevitably created should be carefully considered in such an important South African sector so as not to stifle business and reduce consumer access to financial services.

> *"Investor confidence in other historically strong sectors in South Africa has tapered off during 2016 because of regulatory, economic and political concerns."*

Describe recent developments in the commercial landscape. Are buyers from outside your country common?

ED: Foreign investment in M&A transactions in South Africa continues to be common. The top five foreign markets globally for outbound deals are Canada, the UK, Germany, Mexico and China, as confirmed by recent research by Deloitte. South Africa is seeing a similar trend in buyers in relation to Chinese and UK investors.

For example, we have advised as African counsel, from a competition perspective, the China National Agrochemical Corporation (CNAC) and Syngenta AG (Syngenta), as instructed by Simpson Thacher & Bartlett LLP, for the preparation and submission of a merger notification to the South African Competition Commission and the COMESA Competition commission. The transaction involves the proposed US$44 billion acquisition of sole control of Syngenta, a Swiss company active in the agricultural sector (in particular in seeds and crop protection) and listed on both the SIX Swiss and New York Stock Exchanges, by CNAC, a wholly owned subsidiary of China National Chemical Corporation (ChemChina), a state-owned enterprise established by the State Council of the People's Republic of China. CNAC is the agrochemical division of ChemChina, which manufactures and sells active ingredients and formulated products used for crop protection and non-agrochemical crop products for home and garden and pest control operations.

In relation to UK investors, Associated British Foods plc recently announced its proposed acquisition of the 48.65 per cent interest in Illovo that it does not already own. The agreed offer price per share is 25 rand representing a total consideration of 5.6 billon rand, and the Standard Bank of South Africa Limited announced the 176 million rand disposal of its entire stake in Shanduka Gold Proprietary Limited to UK corporation Pan African Resources Limited (ultimately held by Pan African Resources Plc).

South African and multinational companies are continually strategically assessing Africa in terms of investment. Decision makers are no longer lulled by overarching brush strokes of Africa as a whole as the continent for super returns. Rather, as recognised by reports from the World Economic Forum this year, a more nuanced narrative is being frequently reported on in relation to key jurisdictions in Africa as investment destinations, based on stable political environments and countries that are actively reforming their economies.

Are shareholder activists part of the corporate scene? How have they influenced M&A?[18]

ED: Still in its infancy in South Africa, shareholder activism is not prolific but the market is becoming increasingly aware of the power that shareholders have to influence transactions. Shareholder activism has generally been on the rise in South Africa, following global trends attributable to an increasingly internationalised shareholder base, for instance. The regulatory framework in South Africa, which creates platforms for shareholder engagement and the enforcement of shareholder rights, has created a somewhat enabling environment for shareholder activism. Much of the publicised shareholder activism in South Africa has been focused on aspects of corporate governance and executive remuneration, although there has also been some shareholder activism influence on other issues, such as mergers and acquisitions.

THE INSIDE TRACK

What factors make mergers and acquisitions practice in your jurisdiction unique?

Black economic empowerment in South Africa is often a key consideration in relation to in-bound investment strategies.

What three things should a client consider when choosing counsel for a complex transaction in your jurisdiction?

As South Africa is often a base for strategy throughout Africa, legal counsel with a deep knowledge of the African continent, capable of providing an integrated and seamless service offering across Africa and with solid relationships with regulators across Africa, is essential.

What is the most interesting or unusual matter you have recently worked on, and why?

Acting as counsel to Kansai Paint Co Limited, a Tokyo Stock Exchange listed entity, in its successful hostile bid for JSE Listed Freeworld Coatings Limited (a 3.3 billion rand transaction). This was the first and only successful cross-border hostile bid, to date, that occurred in South Africa.

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Shareholder activists in South Africa primarily comprise institutional investors and fund managers who have been active in seeking out greater shareholder value. Some examples of economic activists in South Africa include the Public Investment Corporation (SOC) Limited (PIC) (an investment management company which is wholly owned by the South African government); Allan Gray, a South African-based investment management firm; and other funds that hold sizeable stakes in companies listed on the Johannesburg Stock Exchange (JSE), such as Paulson & Co (Paulson), an international investment management firm that holds shares in AngloGold Ashanti.

Shareholder activism has influenced M&A activity in South Africa and has been used to push some unique agendas. One of the most notable cases of shareholder activism is the PIC's involvement in pharmaceuticals firm Adcock Ingram Holdings Limited's (Adcock) proposed takeover by a Chilean competitor. The PIC held shares in both Adcock and in the Bidvest Group Limited (Bidvest). Despite the Chilean competitor's deal being more favourable, Bidvest, acting on recommendations from the PIC (its shareholder) put in a last-minute offer to become a significant shareholder of Adcock. Ultimately, on this basis, the deal with the Chilean competitor fell through.

Take us through the typical stages of a transaction in your jurisdiction.

ED: M&A transactions in South Africa must comply with both statutory and common law requirements. Public M&A transactions, kick-started once a firm offer is made, are strictly regulated by the fundamental transaction and takeover provisions of the Companies Act and the Takeover Regulations, the listings requirements of the JSE and insider trading restrictions in the Financial Markets Act. Initiated usually through the CEOs of the listed companies, transactions proceed through various regulated and self-imposed milestones and timing hurdles, including due diligence exercises, signature of transaction agreements, regulatory approvals (with the Takeover Regulation Panel as the primary regulator) and ultimately culminate in closings and settlements.

Private M&A transactions are less regulated, and similarly to other jurisdictions, are to a large degree regulated by the parties themselves, operating within the parameters of the law of contract and common law principles. Due diligence exercises and comprehensive transaction agreements are common, as are regulatory approvals.

Legal due diligence in relation to cross-border transactions are on the rise. The trend is for acquirers to focus on high-priority entities and jurisdictions, and red-flag issues. The best approach to managing pan-African due diligence exercises, from the perspective of both cost and time, is to centrally manage the due diligence from one office. A centralised pan-African approach that provides the acquirer with a seamless and integrated due diligence in cross-border transactions is a differentiating factor for many companies looking to engage legal service providers in their M&A transactions across the continent.

Are there any legal or commercial changes anticipated in the near future that will materially affect practice or activity in your country?

ED: Thus far, Brexit has been the biggest commercial change globally of 2016. The impact on South Africa will depend on the ultimate scenario that unfolds following the UK's strategy and negotiations with the EU, and the manner in which South Africa is affected by those negotiations. Economic commentators expect that the short-term impact will, however, be minimal. In the long term, certain commentators are concerned that South Africa will be exposed negatively as a result of its integration into global financial markets, including its investment and financial links with the UK. According to economists, the worst-case scenario will occur if the EU or UK puts up significant trading barriers that will make it more difficult to export or import goods and services between the EU and UK. According to economists, the best case scenario for South Africa's trade relations with the UK would be if it develops a liberalisation trade policy, as opposed to the status quo or a protectionist policy.

South African's credit rating downgrade is another significant commercial factor that will have an impact on investment into South Africa. Prudent local investors and advisers have factored the potential downgrade of the country's sovereign credit rating to non-investment grade levels by global ratings agencies into their investment planning, by diversifying their investment portfolios. The South African government is also strategising and implementing measures to minimise the impact of downgrades. In February 2016, Finance Minister Pravin Gordhan unveiled a package of spending cuts, civil service job freezes and moderate tax hikes, partly to avoid credit rating downgrades.

Economists comment that investors with existing exposure to the bond market would see their capital values suffer a negative impact, and stock market investors may be negatively impacted. However, they also correctly point out that existing investments actually stand to benefit in terms of higher interest rates that will attract bolder, yield-seeking international investors seeking to capitalise on attractive interest rates, despite the perception of risk.

What does the future hold? What activity levels do you expect for the next year? Which sectors will be the most active? Do you foresee any particular geopolitical or macroeconomic developments that will affect deal sizes and activity?

ED: We expect the private equity sector to continue to boom. Pharmaceutical and healthcare investment in Africa and in South Africa remains a hot topic for investors as companies capitalise on the demand for healthcare in Africa.

We also expect the significant investments from China, Japan, Europe and the US to create an uptick in M&A activity within the power and infrastructure sector. Access to financial services in developing markets will remain a key driver going forward, as will the demand for bigger and better and more competitive expansion within the telecoms and technology sector in South Africa and across the continent.

Also available online

www.gettingthedealthrough.com