



Valuable Advice from Workshop 2

Mergers & Acquisitions Update: Emerging Trends, NZ's M&A Outlook and Opportunities

Held on Tuesday 13 June 2017

Executive Summary

In the face of global volatility, New Zealand has had a steady appetite for M&A activity. Domestic and Australian activity has been high, and there is continuing interest from international investors.

Reported surveys indicate that New Zealand's M&A activity peaked in 2015, with a lower level of activity in 2016 and a slower start to 2017. However, New Zealand and Australian private equity is cashed up, financing is available, and there is a lot of money looking for high quality assets.

The question is, how do you position yourself in this environment to take advantage of the opportunities?



(L-R) Kerri Dewe (Chair) with Grant Houghton, Matt Riley and Murray Schnuriger

The Speakers

Murray Schnuriger is a PwC partner and leads the PwC NZ Deals team. He has advised on M&A transactions for the past 20 years. Murray has a focus on M&A lead advisory, in particular private company sell-sides as well as corporate and private equity buy-sides.

Grant Houghton is a director in ANZ's Leverage & Acquisition Finance team in Auckland. Grant is responsible for deal origination and execution with a focus on offshore sponsors.

Matt Riley founded Waterman Capital with fellow director Chris Marshall in 2004. He has worked in the New Zealand private equity industry for almost 20 years, and is Chairman of the NZ Private Equity and Venture Capital Association.

CHAIR

Kerri Dewe: Principal, Lowndes

Kerri has extensive experience in mergers, acquisitions and disposals. Her corporate and commercial practice is focused on transactional M&A matters, business establishment, restructuring, and joint venture advisory work.

What They Said

Global investor activity has fallen consistently for a year, driven in part by Brexit, the US election result, and UK's hung Parliament. However, the New Zealand market is different than most, and New Zealand continues to have a sustained level of deal activity.

Everyone agreed that 2017 is a seller's market for high-quality assets, that strategic acquirers are increasingly active, and that there is an abundance of capital in the market ready for deployment.

An important part of having a high-quality asset is having a tangible point of difference, and being able to clearly articulate that. Growth potential is also critical. There is a real divergence in multiples between assets with growth potential and other solid, but less strategic, assets.

Murray Schnuriger: Plenty of money looking for good buys

Murray has previously spoken in the Business Intelligence forum, advocating NZ business to take a more aggressive approach to M&A activity if we aren't to see good assets going into offshore hands. He noted that there have been positive signs of that, as with Vector acquiring HRV.

Last year, New Zealand deal activity continued upwards. Despite popular perceptions, about 60% of deals are domestic, and Australia is still the dominant force from overseas. Not only that, Australian investment grew 27 percent in 2016. The idea of getting corporates to buy into New Zealand from further afield, like North America, is appealing, but he noted it's a hard sell for two reasons: New Zealand is a long way away, and our market is relatively mature. However, if those buyers see good intellectual property, they will come.

That said, Asian interest, especially from China, continues to be high. Murray is impressed by their level of sophistication. To attract their interest, sellers need "an Asian angle" such as the product being exported to Asia, and there must also be scale.



Closer to home, in addition to the \$1 billion fundraising activity in New Zealand last year Murray estimates there is over \$1 billion in Australian equity looking for a New Zealand home. Add debt to that, and you have \$3 billion of assets that people are looking for. The question is, are there enough good businesses to go around?

With all this interest, sellers need to know what investors want. In short, that's quality. That includes strong management teams, strong market position, and good growth prospects, preferably into Asia or other export markets, or in line with major trends such as the ageing population. Murray sees prices remaining strong, driven by competition, the continued strength of the listed market, and the fact that debt is still relatively inexpensive. However, he doesn't think we're going to see values "pop" like they did in 2006-07. That was debt fuelled; this time it's equity fuelled.

Murray did raise some concerns with regulatory issues. Industry disruption is complex and can make it challenging to judge whether a merger subject to Commerce Commission approval is likely to be approved. Likewise, while some important work has been done to shorten lead times for Overseas Investment Office decisions, damage may already have been done for some disillusioned overseas investors.

Finally, Murray commented that his view is that a recent spike in takeover activity is likely to be just that – a spike. Valuations are relatively strong, and by the time you add on a takeover premium, you have a high price. Couple that with the fact that takeovers generally involve some kind of dogfight, Murray doesn't see a strong appetite for them in the immediate future.

Grant Houghton: Keeping the deal pipeline going

Grant confirmed Murray's assertion that we are currently in a strong seller's market.



Grant articulated how New Zealand is unlike other markets. New Zealand's SMEs can establish themselves as key participants in often attractive sectors – as long as they demonstrate stable cashflows and good growth prospects, two attributes important to both PE and trade buyers. However, he noted this introduces a potential complication to M&A activity here, namely the impact of owners' personal circumstances (for example, an owner's illness) and a relatively illiquid market, can have a disproportionate impact on overall M&A activity. Contrast this with the US, for example, where a large liquid market means most activity is driven by macro trends.

One notable and seemingly enduring trend is the prevalence of Australian PE activity in New Zealand. This has been driven not just by liquidity, said Grant, but also a track record of success here, including companies like Tegel, Kathmandu, Griffins, Somerset and others. Grant believes Australian interest will remain high, an assertion supported by the establishment of new funds like Adamantem Capital and Odyssey Private Equity, and Adamantem's swift purchase of their first New Zealand acquisition, Heritage Lifecare. Other international

private equity is also looking here. US private equity firm Platinum Equity recently bought Australasian assets in the form of OfficeMax and Staples; Malaysian firm Navis Capital acquired Mainland Poultry.

The limited and infrequent supply of quality assets, coupled with a high supply of funds and the attractiveness of New Zealand assets, has created the perfect storm. As a result, speed of execution is a distinct competitive advantage.

Grant commented that banks have deep liquidity – for the right deals. And the pool of financiers is getting deeper and broader. Offshore banks will support larger transactions in particular. Different banks have different investment appetites and focus, so who will participate depends a lot on the nature of the deal, sector, terms, and returns.

Reflective of pipeline activity, lender appetite, and a benign credit environment, the strong seller's market means sponsors are pushing bank parameters. However, although debt/high yield funds have created opportunities to carve out super senior working capital positions, Grant emphasised the need to still be mindful of the overall leverage and structure around deals.



Matt Riley: Hunting for a good deal



Matt sees M&A activity remaining strong for the next few years. At least \$2 billion of local and Australian capital is looking for a home. We are already seeing the impact, with 2016 PE investment/divestment the highest ever on record.

Quality management, products and cashflow remain critical to attracting investment but Matt also emphasised the importance of having a tangible point of difference and the ability to articulate it.

Of the challenges facing investors, being disciplined around pricing and identifying quality rank highly. Identifying the risks, structuring as much out of the deal as possible and managing the risk that's left is also key.

As for disruption, Matt acknowledges the threats, with clear examples in transport logistics and retail, but points out the opportunities that are also created.

For information on or to register for upcoming workshops in the Business Intelligence Series, please visit:
<http://www.business-intelligence.co.nz>.

Hosted by:



Supporters:



Business Intelligence Series - PO Box 7314, Auckland | Phone +64 9 373 7712 | info@business-intelligence.co.nz

