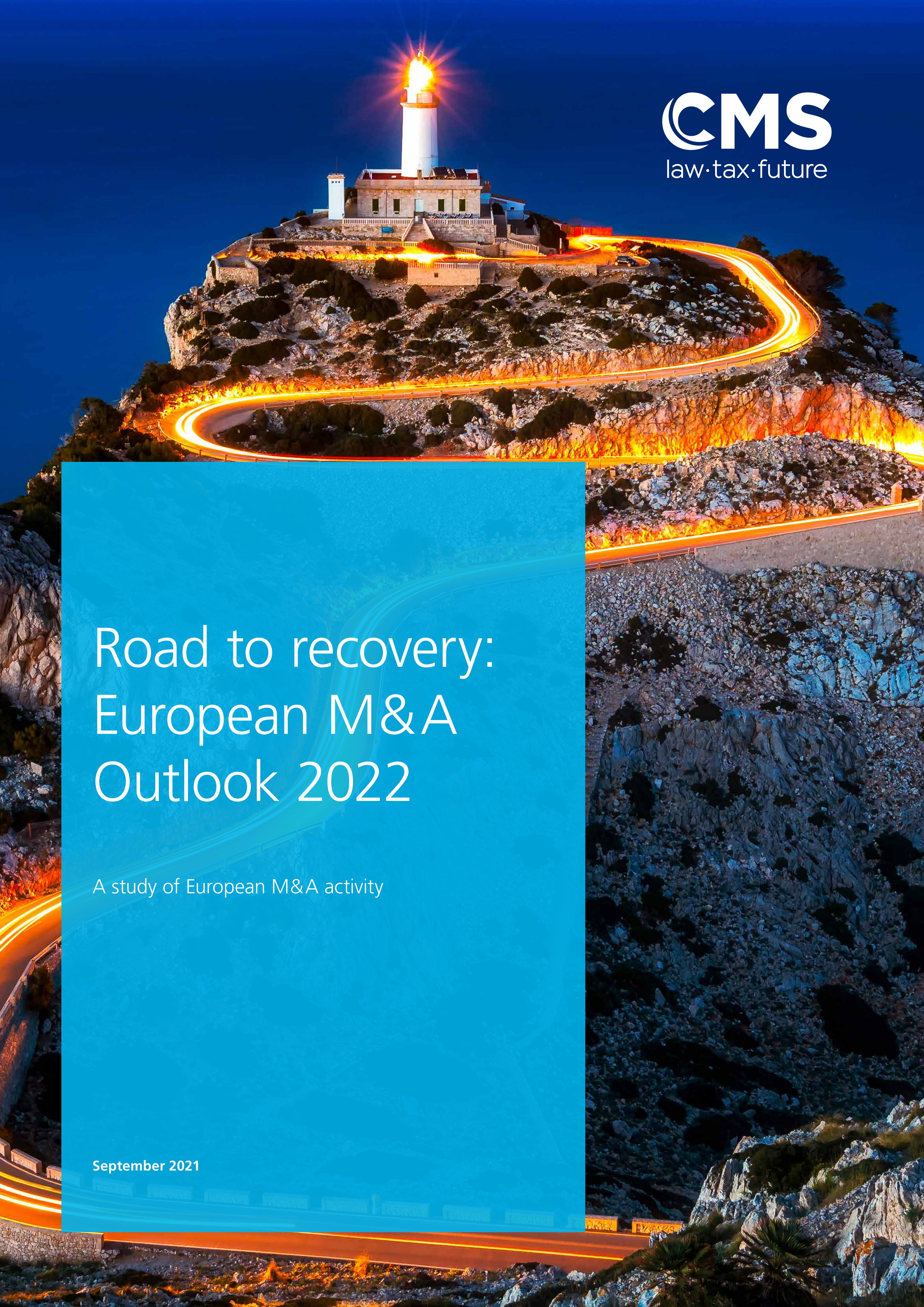

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Road to recovery: European M&A Outlook 2022

A study of European M&A activity

September 2021

Contents

Methodology

In the second quarter of 2021, Mergermarket surveyed senior executives from 240 corporates and 90 PE firms based in Europe, the Americas and APAC regions about their expectations for the European M&A market in the year ahead.

Among the 330 executives interviewed, 70% are headquartered in Europe, while the remaining 30% are equally split between the Americas and APAC regions. All respondents have been involved in an M&A transaction over the past two years and 67% of all respondents plan to undertake an M&A transaction in the coming year. All responses are anonymous, and results are presented in aggregate.

Foreword

Louise Wallace, Partner, Global Head of the CMS Corporate/ M&A Group

Stefan Brunnschweiler, Partner, Global Co-Head of the CMS Corporate/ M&A Group

Welcome to the ninth edition of the CMS European M&A Outlook, published in partnership with Mergermarket.

European M&A markets are in a much stronger position than a year ago, when COVID-19 lockdown uncertainty saw stock markets plummet and deal activity all but grind to a halt.

Europe's dealmakers, however, have adapted to COVID-19 challenges faster than many anticipated, embracing digital due diligence and deal execution and continuing to find ways to put money to work.

The COVID-19 vaccine roll-out has been the real game changer, allowing countries to reopen and supporting a revival in economic growth. Forecasts predict GDP increases of more than 4% for 2021 and M&A has surged in H1 2021 with volume up 44% and value rising 89% year-on-year.

While the pandemic is far from over, the vaccine programmes have been effective at limiting the impact of the virus and its variants, enabling investment and a return to growth.

This more positive outlook is reflected in this year's survey, with greater numbers of respondents ready to get back to doing deals after a challenging pandemic period.

Key findings from our research include:

M&A appetite rises
More than half of all respondents expect the level of European M&A activity over the next 12 months to increase. Corporates that have built up large cash piles through the pandemic and PE firms with record levels of dry powder are eager to make up for time lost in lockdowns to get deal timetables back on track.

Low prices and distress
Although asset prices have held up through the pandemic and vast government stimulus has kept businesses from insolvency, just under a quarter of respondents (24%) see undervalued targets as the most important buy-side driver of M&A activity over the next 12 months. A similar percentage (22%) identify distressed-driven M&A as the most important catalyst for sell-side activity.

PE in pole position
71% agree that financial buyers are better placed than strategic buyers to take advantage of buying opportunities presented by COVID-19. Private equity firms have limited timeframes to deploy capital so are expected to move quickly to get deployment levels back on schedule. Whilst corporates are currently focusing on reopening offices and sites as COVID-19 restrictions ease, we expect greater activity from these strategic buyers, as well as from the US and European SPACs.

What a difference a year makes

Professor Scott Moeller, Founder and Director, M&A Research Centre, Bayes Business School (formerly Cass), introduces this year's M&A Outlook by focusing on what has been a transformative year

Scott Moeller, Founder and Director, M&A Research Centre, Bayes Business School (formerly Cass)

Last year, the world was in a state of maximum uncertainty as economic activity slowed, markets declined more rapidly than at any time since 2008, and the huge human cost of the pandemic was felt around the world. This year, despite an ongoing struggle to contain the virus, in a period of less than ten days in July we saw the first two commercial tourist flights launched into space: Richard Branson's Virgin Galactic and Jeff Bezos' Blue Origin. While they headed skyward, the markets were also reaching new heights, breaking records in terms of M&A deal volumes which some observers characterised as 'stratospheric levels'.

A whole new world

In mid-2020 the world was still learning how to deal with the pandemic. Asia, having lived through SARS over a decade earlier, quickly shut down. Elsewhere, masks were being worn both indoors and outside, and there were few expectations of a quick 'return to normal'. Hospitals were full and healthcare workers were applauded. Offices were closed and the 'new normal' for many workers was quickly developing into working from home.

Executives who have previously never tried, now found themselves to be experts at manipulating the various functions of online videoconferencing. International travel had largely stopped. Likewise, the M&A markets.

But just as some airplanes continued to fly and a core group remained in some offices and trading floors, M&A activity didn't stop completely, it just adapted.

These dealmakers discovered that due diligence meetings could be held virtually on a video-call where, prior to March 2020, those same executives would have said that they could only conduct their diligence in a high-touch manner. PE funds were launched and oversubscribed without a single in-person meeting with potential investors, again something no one had ever previously attempted. Multi-million-dollar deals were closed without a physical handshake throughout the entire deal process.

This time last year, there was a level of activity well below that of the previous years, and the outlook was dim. Seventy-eight percent of market practitioners interviewed for this report last year expected that the following 12 months would see even further declines in market activity levels. As one partner at a large M&A firm told me recently: 'In March and April of last year, we told all our staff to go home, rest and stay healthy, as we expect business to dry up for the rest of the year.' She was not alone in this assessment of the markets back then, as in this report last year, 65% said that they were not considering doing an M&A deal in the next year.

Opportunity knocks

But never underestimate the creativity of M&A professionals. That same M&A partner said that within a month or two, by May, all her team were working hard on new deals and ended up doing more business than in 2019. 'All of this from their home offices, living rooms and bedrooms.' She added, 'And now 2021 looks to be setting a new record for us.'

In adversity is opportunity. Even during the pandemic, there were some activities that thrived because they were easily adapted to the new pandemic-impacted business environment that was developing globally. For example, special purpose acquisition companies (SPACs) were the M&A equivalent of Zoom for meetings. Zoom had existed before the pandemic but became an essential tool for communication in the pandemic – and likely, the post-pandemic – world. SPACs, which had been around for over 20 years, were resurrected to fill a void that allowed fundraising (instead of traditional IPOs) and acquisitions to continue during lockdown, enabled as well by the benign interest rate environment and regulatory arbitrage.

Thus, as we can see in this report, one year later the tone and expectations of the market are very different. Now, most of the M&A experts consulted for this report believe European M&A activity in the next 12 months will be stronger than the already-robust levels of the past year and 66% said they were planning to invest in Europe over the next three years.

Indeed, 51% believe that COVID-19 has actually driven this market activity, which is partly due to some distressed deals (this report notes that distressed-driven M&A is the most important sell-side driver) and the demands of PE buyers who have record levels of dry powder.

Challenges ahead

Despite their tendency to be positive and continually looking for confirmation that deal activity will be robust, the expert respondents to the survey this year did note some substantial headwinds. The largest of these 'significant obstacles' was the rise in regulatory scrutiny of M&A deals (especially antitrust); the other top obstacles were the ever-present concerns about the vendor/acquirer valuation gap, which was virtually tied for second with continuing concerns about the COVID-19 crisis.

The report points out that it is not only the pandemic that is having an impact on the markets. Within Europe, for example, Germany (and even more so combined with Austria and Switzerland in the DACH region) is expected to see the highest growth in M&A deal activity, supplanting the UK and Ireland as the most active M&A markets. As with COVID-19, we don't really yet know what the 'new normal' will look like, and the same is true with post-Brexit Britain.

Of course, one absolute in M&A markets is change. Encouraging though it may be that the markets were able to adapt to the pandemic and then even expand, another certainty about M&A markets is that they go in waves. Just as Virgin Galactic and Blue Origins returned to earth, this current, pandemic-affected wave will come to an end… just not yet, at least according to the very persuasive reasoning of the expert wisdom of the senior executives surveyed for this report.

In uncertain times, earn-outs offer valuable certainty

In light of the COVID-19 pandemic's ongoing impact on asset valuations and deal certainty, earn-out mechanisms are coming to the fore to help buyers and sellers feel more confident.

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The COVID-19 outbreak unleashed unparalleled uncertainty almost overnight, with concerns about a global downturn compounding the impact on M&A markets worldwide. A key factor contributing to that shock was the insecurity surrounding valuations and executing deals at the right price. Optimistic sellers argued that a business should be valued according to its pre-COVID-19 performance, whereas sceptical buyers argued those indicators may not adequately reflect the pandemic's effects on the market going forward and might request a lower purchase price.

Now trends are emerging where buyers and sellers implement commercial and innovative solutions to bridge valuation gaps, including the increasing use of earn-outs. This trend, in fact, was first observed in the CMS European M&A Study 2008-2011 following the global financial crisis.

Though they exist in various forms, typically an earn-out requires a buyer to make additional consideration payments to a seller following the completion of a deal if the business achieves certain performance metrics in a specified period following completion. Our 2020 and 2021 editions of the CMS European M&A Study show earn-outs featured in 21% of deals, and we expect this percentage to increase.

In the CMS European M&A Study 2021, EBITDA was the most popular financial metric on which to base an earn-out. In future, we expect a rise in popularity of turnover being used to determine the amount of an earn-out, as it is more easily verifiable than EBITDA.

Where EBITDA is used, being a non-GAAP metric, input from accountants will be necessary to define the relevant concepts. Against the backdrop of COVID-19, we could also see the rise of other alternatives to these more traditional metrics, such as EBITDAC (EBITDA adjusted for the impact of COVID-19) and non-financial metrics such as the retention of key agreements.

Instilling confidence

Certain sectors, such as the airline and travel industries, have been very negatively impacted by COVID-19, and these impacts may not be short-lived. The financial covenant strength and cash flow position of certain businesses, including those who only 18 months ago had very strong balance sheets, have been compromised. Sellers must be conscious of this and should consider whether any retention and/or security arrangements (including, for example, taking security over valuable assets) ought to be put in place to ensure certainty of funding the earn-out.

On the other hand, cautious buyers who are conscious of liquidity issues in the current climate may wish to resist retention and security arrangements and instead find comfort through alternative means, such as including parent company guarantees, an option to pay the earn-out in shares (if the buyer is listed), evidence of cash flow projections and available financing facilities. If, however, a motivated seller insists on cash-based security, a buyer may wish to consider offering this security in exchange for an early payment earn-out discount.

Both buyers and sellers will inevitably have concerns about the payment of an earn-out, including insolvency risk, uncertainty in the market and other relevant factors. Undoubtedly it is in both parties' interest to agree on a position that gives the seller comfort that the earn-out payments will be made.

To instil this confidence, the parties could consider including a provision in the contract that permits acceleration of the payment of the outstanding earn-out or an agreed portion of it. For some businesses it may even be possible to structure the earn-out such that it can be satisfied in exchange for an asset type other than cash – for example, transfer of intellectual property or data from the buyer to the seller.

Earn-out mechanisms can, of course, be the subject of disputes. Should these arise, it is important to reach an early resolution so that the payment is unlocked and the liability is resolved efficiently. It may not always be suitable for such disputes to be referred to courts or arbitration for lengthy proceedings. In those circumstances, independent expert determination can help to resolve disputes effectively.

Given the complexities expected to be introduced into valuations and resulting earn-outs, dealmakers should not underestimate the possibility of post-completion disputes. A risk mitigation strategy can be key to helping parties navigate these issues and should be considered carefully in a transaction's early stages.

Striking a compromise
Earn-out payments are typically structured to result in an increase in the purchase price that may be payable at a future date. This increase is 'earnt' by a seller if the performance of the acquired business exceeds agreed benchmarks.

When considering an earn-out's structure, parties will need to determine the payment thresholds and frequency. Generally, there are two options at hand: first, frequent milestones and payments that are paid annually or quarterly; or, second, a single milestone and bullet payment typically paid out at the end of the earn-out period.

Buyers naturally prefer higher thresholds with one milestone and payment at the end of the period, while sellers generally favour frequent milestones. As a compromise, parties might construct a method based on a sliding scale approach to paying an earn-out.

The risk of further waves of COVID-19 infections is another factor that will have an ongoing impact on earn-out calculations and payment dates. One way to address this may be for the parties to agree to defer upcoming earn-out payments in the event of a spike in infections. A buyer may be more inclined to accept this if the deferral was given to the seller in exchange for a discount in upcoming earn-out measurements and payments. A motivated seller with leverage may have success in negotiating such a deferral or alternatively negotiating the right to modify the calculation to mitigate the effect of any subsequent waves of COVID-19. This will need to be balanced against the desire to be paid, value certainty, post-deal integration plans and the longer-term damage of having a disincentivised seller, which should not be overlooked.

The sale contract could be drafted to include a defined set of trigger events that unlock the agreed upon extraordinary measures. Alternatively, language could be included to insulate an earn-out from the impact of adverse extraordinary events. Moreover, the tax implications of a proposed earn-out structure should be considered as early as possible, as the precise terms of the earn-out will determine the tax treatment of it for the parties.

Sector considerations
Earn-outs tend to be more popular in life sciences and TMT transactions, sectors that are innovative, creative and frequently involve individual owner managers. In the CMS European M&A Study 2021, we saw life sciences and healthcare remain as the most popular sector for earn-outs, encompassing 43% of such deals.

When choosing an appropriate metric or combination of metrics for a particular transaction, sector considerations are often relevant, given that earn-out metrics can be sector specific. For examples, in the renewable energy sector, common metrics include turnover, megawatt output, customer growth, production targets. In healthcare, regulatory approval is a common concern. For real estate, net asset value or EPRA earnings can be considered. In the infrastructure space, free cash flow is a common metric, as is the case for telecoms transactions, alongside EBITDA and customer churn.

In all cases, the metric of choice could be a readily-defined and easily-measured result indicator. In the current climate, for businesses where employees are the main assets, earn-outs metrics could, in addition to any financial targets, be based on employee satisfaction and/or retention. This could be measured through an independent survey or, for a more objective test, through employee satisfaction determined by turnover or churn numbers calculated with reference to low industry turnover rates.

The ongoing fallout from the pandemic may see the increased use of earn-outs across certain sectors as dealmakers look to execute deals in the face of uncertainty. In this regard, parties should consider whether any sector-specific considerations should be taken into account in earn-out discussions.


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Rock-solid fundamentals should elicit robust rebound in CEE-6 hotel market

Though dealmaking in the region was hit harder by the pandemic than the rest of Europe, CEE-6 nations' pre-crisis performance and underlying strengths augur well for a quick turnaround for the hospitality sector

Lukáš Hejduk, Partner, CMS Czech Republic

Ana Radnev, Partner, CMS Romania

In 2020 the CEE-6 (Bulgaria, Czech Republic, Hungary, Poland, Romania and Slovakia) logged M&A deals worth EUR 370m. That aggregate value was significantly below initial expectations (EUR 1.8bn), as many deals were either put on hold or withdrawn owing to the pandemic. Of the total body of transactions completed last year, 87.6% comprised deals that had already been committed to prior to the COVID-19 crisis.

Last year's figures represent a 74.2% decline from the record EUR 1.4bn reached in the region the year prior. This was a steeper decline compared to the Europe overall, where transaction volume fell 62.8%, as pandemic-related uncertainty compelled investors to retreat to their core markets and familiar ground.

The broader CEE markets saw a similar trend, as almost all deals closed in the region in 2020 were in capital cities (98.6%). This marks a significant change from 2019, when 72.2% of transactions closed took place in capitals. This indicates that those who continued to invest in the region last year preferred to stay within the comfortable confines of key gateway cities.

Despite the decline in volumes, activity in 2020 was still significantly higher than that recorded during the 2009 economic downturn – that year, only EUR 209m worth of deals was transacted. This shows that regardless of the stage of the economic cycle, the CEE market has, in just a short space of time, become much more attractive and active.

"The decline in transaction activity was driven by a combination of factors, the most prominent one being the temporary lack of visibility on when and how the market will recover. But the clock is ticking, and some owners may soon face financial challenges, especially as government subsidies taper off or their loans come to term. Similarly, on the investor side, significant capital has been raised, and this will need to be deployed sooner rather than later to deliver the required returns. These factors, combined with improving cash flows when the market starts to recover, should help bridge the gap in expectations between buyers and sellers and lead to more transaction activity and perhaps no signs of distressed sales," says Frederic Le Fichoux, Head of Hotel Transactions, Continental Europe at Cushman & Wakefield.

Despite the relatively low transaction volume over the past year, investor activity in the region is resuming. Nearly EUR 140m worth of transactions have been concluded in 2021 so far, and aggregate value for this year is forecast at around EUR 320m.

Reopen for business

In the long term, the potential of the region's hotel market remains robust: average annual transaction volume over the past five years (2016-20) reached EUR 791m, 2.7 times higher than at the peak of the previous cycle (EUR 296m, 2002-06).

"Prior to the pandemic, the hotel sector demonstrated solid growth with investor interest peaking at an all-time high in 2019. While it is impossible to overlook the short-term challenges facing the sector, it is safe to say that there is a positive long-term outlook. Banks continue to express an interest in financing hotels in CEE, and with limited virtual alternatives but evergreen consumer appeal, we expect healthy demand to return as the world reopens for business," comments Lukáš Hejduk, CMS partner and Head of Hotels & Leisure in CEE.

The volume of hotel transactions in the region still has ample room for growth. For example, hotel transaction volume in the CEE-6 region represents only 3.4% of total volume in Europe, despite the fact that the region generates around 5.8% of European GDP and accounts for 6.2% of hotel supply (2015-19). By comparison, in neighbouring Austria, hotel transaction volume (3.1% share in Europe) was slightly higher than the share of GDP (1.9%) and hotel supply (2.3%).

"For the CEE-6 to achieve its fair market share, hotel transaction volume should average over EUR 1.5bn annually, nearly double the current average of EUR 0.8bn. The region almost achieved this figure in 2019 and was on track to exceed it based on 2020's initial expectations. In other words, it is quite evident that reaching an average annual transaction volume of EUR 1.5bn is not a far-fetched dream for the CEE-6, and such flourishing activity may well be where the region is currently headed on the road to recovery," comments Bořivoj Vokřínek, Strategic Advisory & Head of Hospitality Research EMEA at Cushman & Wakefield.

Gateways to CEE

Despite the present slump, it is important to note that the fundamentals have not changed. The current difficult situation has been caused by a health crisis, not by an economic or structural crisis. As restrictions on cross-border movement ease and people feel more comfortable about travelling, the situation in the hospitality sector is likely to improve, portending more transactional activity both in the CEE and across Europe.

Roman Tarlavski, a corporate partner at CMS hospitality sector group in Amsterdam, comments: "While the sector has been hit disproportionally by the outbreak, occupancy levels are on the rise again in Western Europe. The increase is evenly shared between the countryside and gateway cities as some travellers are hesitant to travel abroad and prefer to travel domestically, while the reduction of travel restrictions, prompted by mass vaccination programmes, encourages others to travel abroad. However, the increase is largely attributable to the leisure travellers as business travel is still limited and it is not clear how quickly it will pick up. The increase of occupancy levels is definitely good news for the sector but the lack of business travel has an adverse effect on room rates."

The M&A environment and expectations for the year ahead

European M&A activity has rallied strongly through the first half of 2021, with dealmakers returning to the market after navigating the initial wave of COVID-19 disruption and uncertainty in 2020

Top findings

53%
expect European M&A activity to increase over the next 12 months

23%
of survey respondents see regulatory changes as the principal obstacle to M&A

22%
think that distressed M&A will be the main sell-side driver of M&A

24%
think that undervalued assets will be the main buy-side driver of M&A

European dealmaking has come back with a bang in 2021. Volume has climbed 59% year-on-year to 5,024 deals through the course of H1 2021, according to Mergermarket figures, with deal value for the period rising 111% to EUR 496.1bn.

The double-digit rise in deal value and volume is reflective of a much-improved macroeconomic backdrop when compared to a year ago, and optimism that economies across the continent will see strong rebounds in GDP growth as vaccination programmes continue to roll-out and businesses impacted by lockdowns are able to reopen.

Vaccs and SPACs boost the market
COVID-19 risk remains but rising vaccination rates have reduced the chances of further lockdowns and economic disruption, supporting a positive outlook for economic growth through the second half of this year and moving into 2022. In July, the European Commission upped its forecasts for GDP growth from 4.3% to 4.8% for 2021 and from 4.4% to 4.5% to 2022. European stock markets, which rebounded swiftly following the initial round of lockdowns, have continued to trade strongly against the upbeat economic picture. The STOXX Europe 600 Index is showing gains of 15.7% for the year to date and is up more than 25% over the last 12 months.

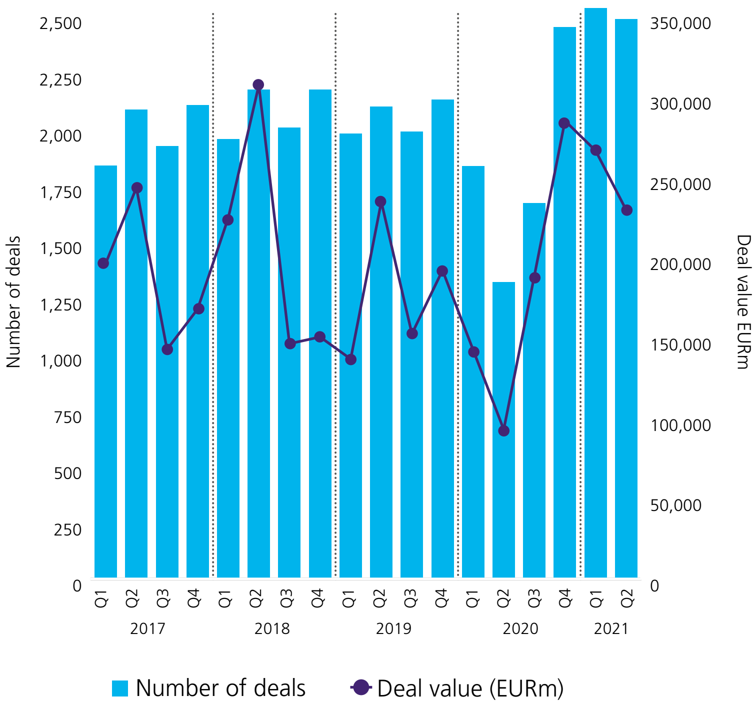
Recovering economies and resilient stock markets have created a fertile environment for M&A, and both corporates and PE firms have moved decisively to catch up on delayed deal timetables and deploy the abundant pools of liquidity at their disposal. According to Allianz research produced in April, non-financial European companies have built up cash holdings through the pandemic and are now sitting on reserves equivalent to three months of turnover, more than half a month higher than pre-crisis levels.

European PE firms, meanwhile, have USD 351.6bn of dry powder at their disposal, up from USD 305bn a year ago, according to research group Preqin.

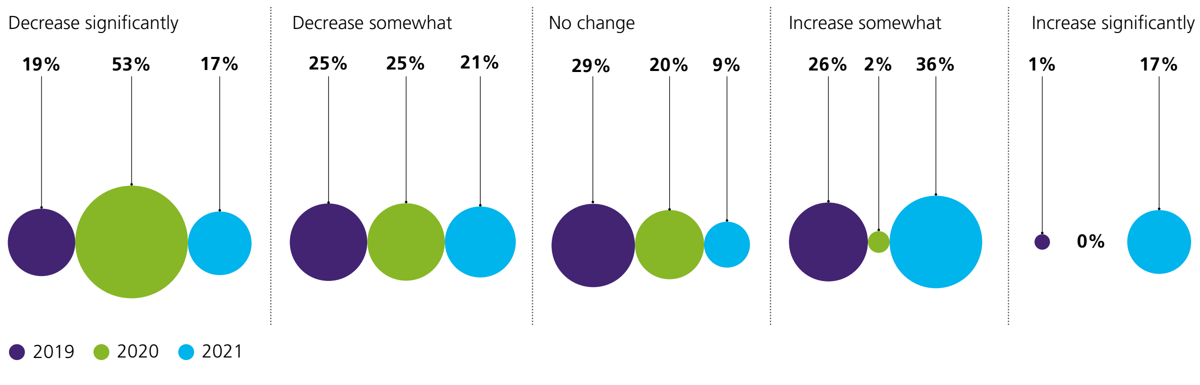
European M&A activity has also benefitted from the surge in fundraising by special purpose acquisition companies (SPACs) in the US. SPACs raise money from stock market investors and then have two years to invest the proceeds in an M&A transaction. In North America, 363 SPACs have listed in H1 2021, surpassing the 250 full-year total for 2020 and raising USD 111.7bn, which is already ahead of last year's total.

With the clock ticking on their capital, these North American SPACs have actively sought out deal targets in Europe and landed some of the biggest deals in the continent this year. For example, Gores Holdings V, a SPAC headed by veteran US private markets dealmaker Alec Gores, acquired Luxembourg-based metal packaging group Ardagh in a EUR 7.2bn deal, while Ajax 1, a SPAC run by US hedge fund billionaire Daniel Och, paid EUR 5.9bn to buy online used car sales platform Cazoo.

European M&A trends 2017-Q2 2021



What do you expect to happen to the level of European M&A activity over the next 12 months?



European M&A top 20 deals, H1 2021

Announced date	Target company	Target sector	Target country	Bidder company	Bidder country	Deal value EUR(m)
12/06/2021	Autostrade per l'Italia S.p.A (88.06% stake)	Construction	Italy	Consortium of investors led by Cassa depositi e Prestiti S.p.A.	Italy	17,975
18/03/2021	Western Power Distribution plc	Energy, mining & utilities	United Kingdom	National Grid Plc	United Kingdom	16,591
29/06/2021	Suez SA (Recycling & Recovery businesses in France); Suez Eau France SAS	Energy, mining & utilities	France	Caisse des Depots et Consignations; Global Infrastructure Partners, LLC; Meridiam SAS	France	10,700
16/03/2021	eToro Group Ltd	TMT	United Kingdom	FinTech Acquisition Corp. V	USA	8,194
13/01/2021	Telxius Telecom S.A. (telecommunications towers division in Spain, Brazil, Peru, Chile and Argentina)	TMT	Germany	American Tower Corporation	USA	7,700
23/02/2021	Ardagh Metal Packaging S.A.	Industrials & chemicals	Luxembourg	Ardagh Metal Packaging S.A.	USA	7,286
29/03/2021	Cazoo Limited	TMT	United Kingdom	Ajax I	USA	5,932
17/02/2021	Zalando SE (21.11% stake)	TMT	Germany	Kinnevik AB (Shareholders)	Sweden	5,438
03/02/2021	GW Pharmaceuticals Plc	Pharma, medical & biotech	United Kingdom	Jazz Pharmaceuticals, Inc.	Ireland (Republic)	5,336
06/01/2021	Walgreens Boots Alliance, Inc. (majority of Alliance Healthcare businesses)	Pharma, medical & biotech	United Kingdom	AmerisourceBergen Corporation	USA	5,255
03/05/2021	Roivant Sciences, Ltd.	Pharma, medical & biotech	Switzerland	Montes Archimedes Acquisition Corp.	USA	5,233
03/02/2021	Hivory S.A.S.	TMT	France	Cellnex Telecom, SA	Spain	5,200
05/02/2021	Signature Aviation plc (81.27% stake)	Industrials & chemicals	United Kingdom	Blackstone Infrastructure - Blackstone Core Equity - GIP - Cascade Consortium	USA	5,068
26/01/2021	Naturgy Energy Group (22.69% stake)	Energy, mining & utilities	Spain	IFM Investors	Australia	5,060
11/02/2021	SIA S.p.A.	TMT	Italy	Nexi S.p.A.	Italy	4,917
08/02/2021	Dialog Semiconductor Plc	TMT	United Kingdom	Renesas Electronics Corporation	Japan	4,886
29/03/2021	Klovern AB	Real estate	Sweden	Corem Property Group AB	Sweden	4,625
30/06/2021	Cerba HealthCare S.A.S.	Pharma, medical & biotech	France	EQT Partners AB; Public Sector Pension Investment Board; Bpifrance SA	Sweden	4,500
08/01/2021	CA Immobilien Anlagen AG (71.76% stake)	Real estate	Austria	Starwood Capital Group	USA	4,302
31/05/2021	DomusVi SAS	Pharma, medical & biotech	France	Intermediate Capital Group Plc; Sagesse, Retraite, Sante S.A.S.; Yves Journel (Private Investor); Merieux Equity Partners S.A.S.; BNP Paribas Agility Capital	France	4,300

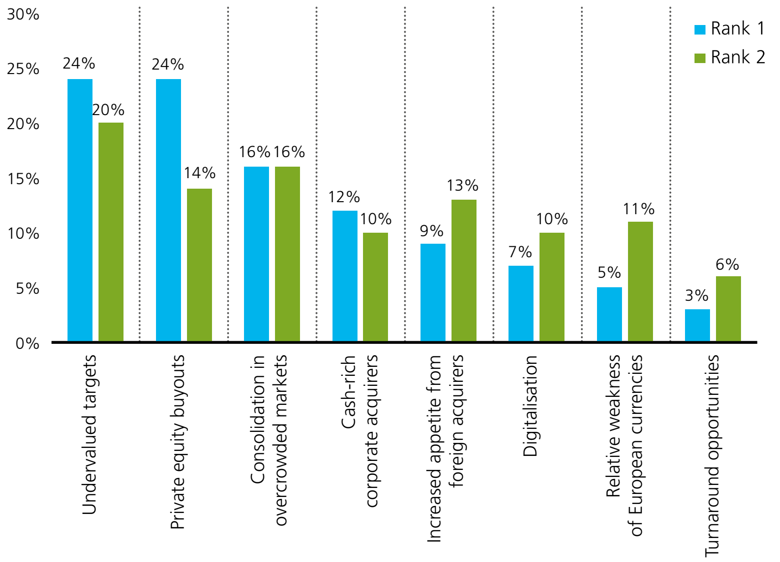
Other drivers of big-ticket deals have been jumbo investments in the technology, media and telecommunications (TMT) and healthcare sectors, which proved to be resilient throughout the pandemic and were able to continue growing earnings despite lockdown disruption. Half of the 20 largest deals in Europe have been in either TMT or pharmaceuticals, medical & biotech (PMB).

There are now also signs, however, of deal activity coming back to life in sectors hit hard by lockdowns as buyers see more clarity around future earnings restrictions ease. Blackstone, Cascade and Global Infrastructure Partners, for example, joined forces to acquire UK-listed private jet services company Signature Aviation in a EUR 5.1bn deal.

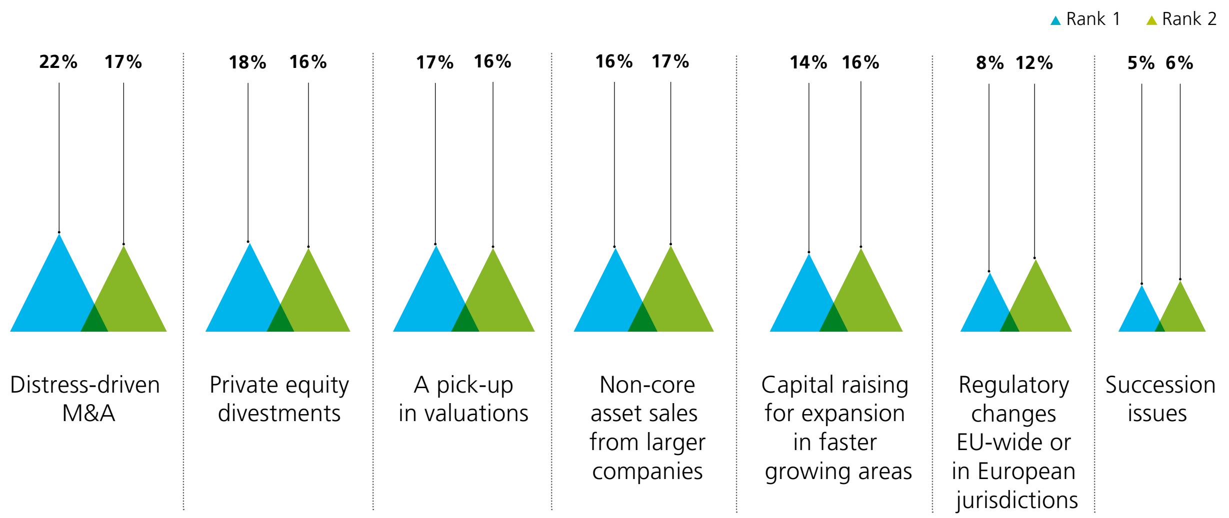
Regionally, the UK has delivered more of the 20 largest deals than any other region (seven), but large transactions have progressed across a number of countries including Italy, France, Sweden, Austria, Spain and Germany.

> There continues to be a very large amount of equity in the market which, combined with continuing low interest rates and inflation, as well as high stock market valuations and higher levels of investor confidence compared to 2020, have fuelled increased deal activity.
>
> *Charles Currier, Partner, CMS UK*

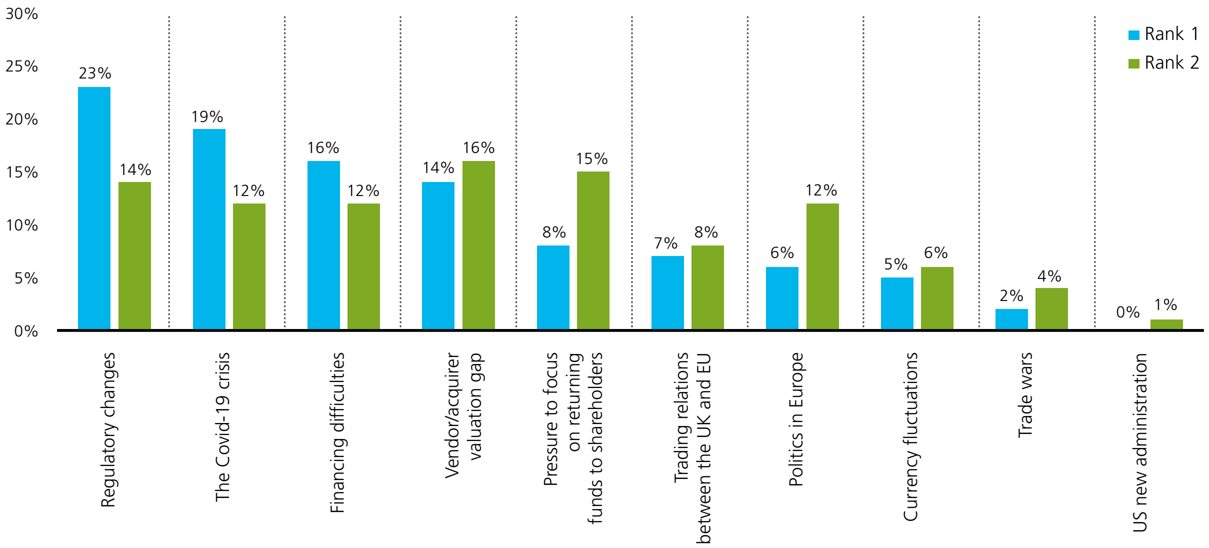
What do you believe will be the greatest buy-side drivers of M&A activity in Europe over the next 12 months? (Please select top two)



What do you believe will be the greatest sell-side drivers of M&A activity in Europe over the next 12 months?



What do you believe will be the principal obstacles to M&A activity in Europe over the next 12 months? (Please select the two most important, 1 = most important, 2 = second most important)



A brighter outlook

This combination of favourable deal dynamics has seen a clear shift in dealmaker sentiment. More than half of respondents to the CMS M&A Outlook survey expect European activity to increase over the next 12 months, 17% of which say the rise will be significant. This stands in stark contrast to last year's poll, in which 78% of participants were preparing for a decrease in M&A with only 2% anticipating an increase.

Looking ahead to the second half of 2021 and into 2022, just under a quarter of respondents (24%) see undervalued targets as the most important buy-side driver of M&A activity over the next 12 months with a fifth choosing valuations as the second most important buy-side driver. These findings are somewhat surprising, as EBITDA multiples for European mid-market companies climbed to an all-time high of 11.6x in Q2 2021 according to the Argos Index.

The survey suggests that dealmakers expect to see more value emerge in the market as deals in COVID-impacted sectors such as leisure, retail and consumer start to transact in higher volumes and at lower multiples than keenly priced technology and healthcare assets.

On the sell-side, 22% of survey respondents see distressed-driven M&A as the most important catalyst for sell-side activity with 16% selecting non-core asset disposals by corporates.

These findings indicate that dealmakers are preparing for higher levels of corporate distress and business reorganisation as government-backed COVID-19 financial support measures unwind.

With respect to the obstacles to M&A, COVID-19 remains a risk but ranks second behind regulatory obstacles, which were chosen by 23% of the firms polled by CMS. One area of particular focus is the more stringent rules around foreign direct investment and cross-border M&A, with the EU Competition Commission adopting a more hawkish stance on M&A deals for European targets backed by entities funded by foreign governments.

> In sectors that enjoyed upside potentials from the pandemic, M&A continued almost without any constraints. PE investments suffered briefly due to financing hindrances, though the industry adapted quickly to the new world. We saw increasing appetite for continuing investments in new business models, especially those focused on digitalisation. Tech M&A in DACH, for instance, was up 103% in H1 2021 compared to H1 2020.
>
> *Hilke Herchen, Partner, CMS Germany*

A post-COVID-19 Europe

Although the risk of further COVID-19 disruption and restrictions across Europe remains very much on the radar for M&A investors, there is a growing sense of optimism and confidence

Top findings

51%
say that COVID-19 has increased their deal appetite

16%
anticipate an increase in carve-outs and spin-out deals in the aftermath of COVID-19

38%
expect Germany to be the region with highest growth post-COVID-19

71%
feel that financial sponsors are better placed to take advantage of COVID-19 buying opportunities than corporates

While new strains of COVID-19 – such as the Delta variant – have been flagged as an ongoing threat to a full economic recovery by the European Central Bank, vaccination programmes are progressing. Vaccination rates have differed between countries across the bloc, but according to the European Centre for Disease Control (ECDC), 61.5% of the adult population in the EU had received the first dose of vaccine by the beginning of July, with 40.2% fully vaccinated with two doses.

With rising vaccination rates providing European countries with improved defences against COVID-19, dealmakers are feeling more comfortable about future investment prospects. Some 51% of respondents feel that COVID-19 has increased their dealmaking appetite, with 11% saying it has increased deal appetite significantly. This stands in contrast to results from 12 months ago, when 74% of those polled observed that COVID-19 would reduce their deal appetite.

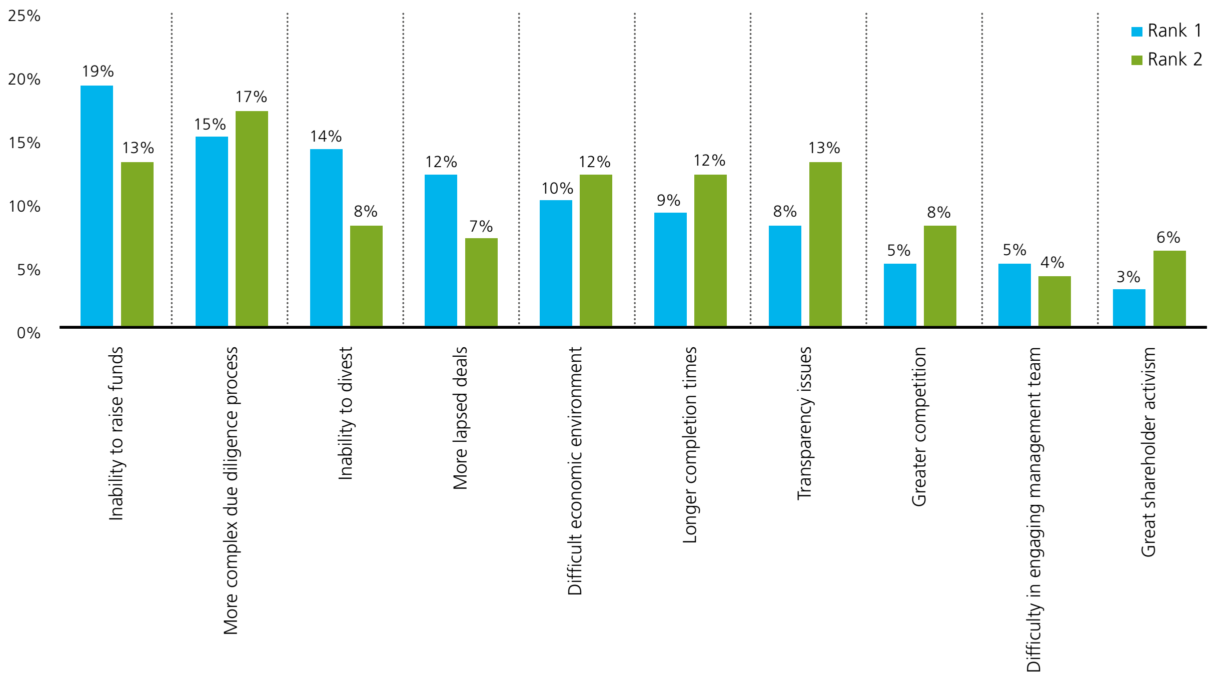
Carve-outs and core focus

But although optimism is returning to the M&A community, the survey findings do indicate that COVID-19 will make a long-term mark on the structure and functioning of deal markets across Europe.

One of the main changes anticipated by close to a fifth of survey respondents (16%) is an increase in carve-out and spin-out deals.

> The pandemic significantly disrupted the world economy. Companies are refocusing on their main strengths to increase efficiency and capitalise on their competitive advantages. Non-core assets are increasingly being divested, leading to a spike in carve-outs and spin-offs. We expect this boom to continue post-pandemic.
>
> *Clemens Grossmayer, Partner, CMS Austria*

What challenges do you expect to see in European M&A in the aftermath of COVID-19? (Please select the two most important, 1 = most important, 2 = second most important)



Carve-out and spin-out activity is usually prompted by the need to offload non-core assets and reduce debt, themes which have been amplified through the pandemic period. According to a 2021 Corporate Carve-out survey conducted by pan-European special situations investor Aurelius, 89% of the participants it polled expect carve-out activity to increase this year, up from 60% in the previous year.

Carve-outs and core focus

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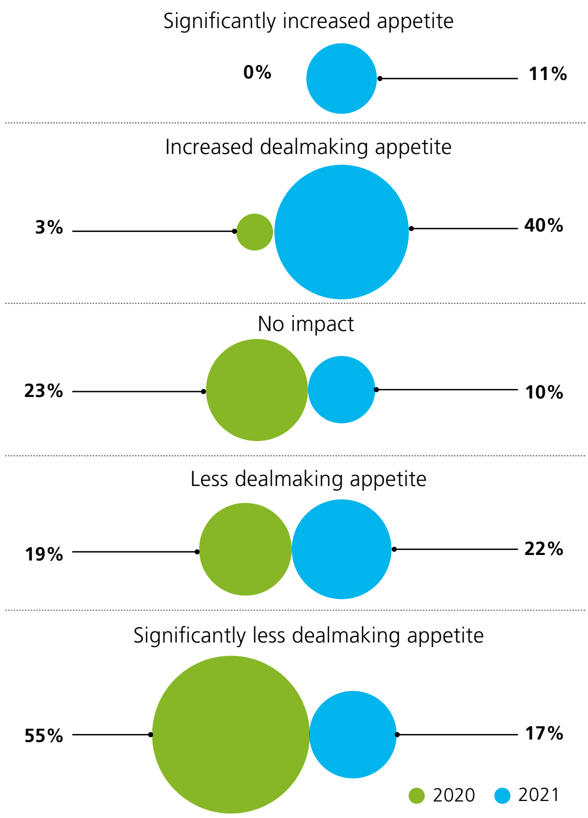
One of the main changes anticipated by close to a fifth of survey respondents (16%) is an increase in carve-out and spin-out deals.

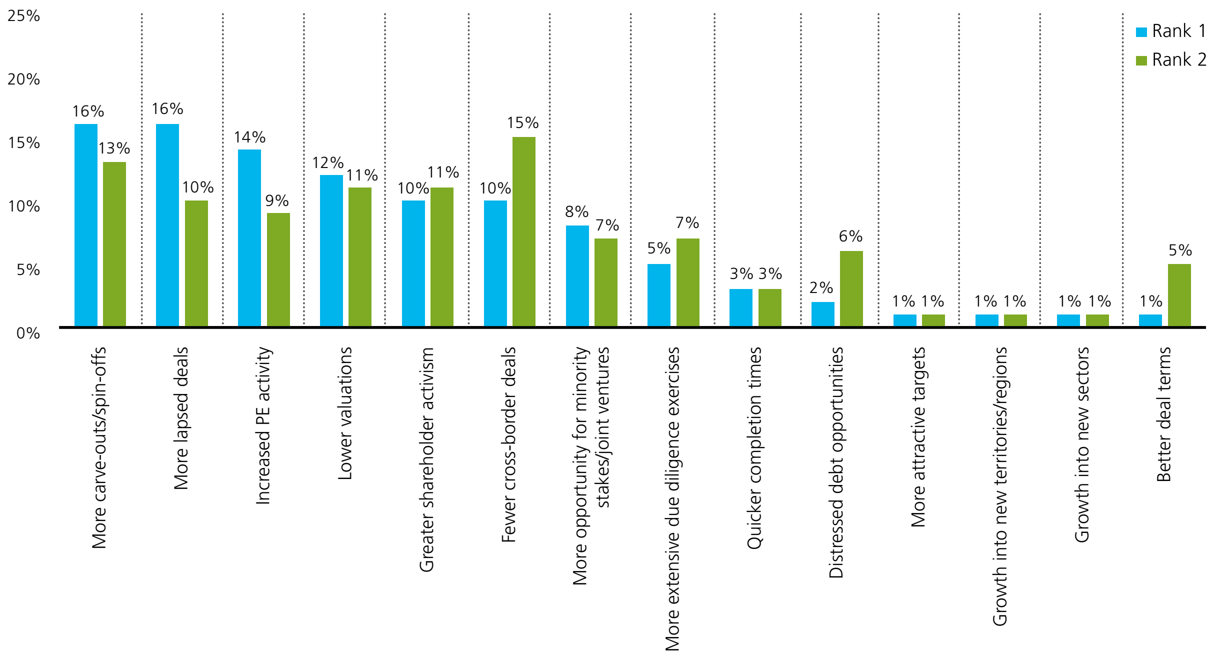
Pandemic disruption has seen all corporates run the rule over their portfolios and sharpen the strategic focus of their businesses.

A consortium of private equity investors led by TDR Capital, for example, spun off online used car marketplace CarNext from its parent company LeasePlan for EUR 400m. The deal is expected to see the two separated entities achieve higher valuations than when combined, as well as free CarNext to work more easily with a broader pool of automotive manufacturers and

What impact has COVID-19 had on your dealmaking appetite? (Please select only one)



What trends do you expect to see in European M&A in the aftermath of COVID-19? (Please select the two most important, 1 = most important, 2 = second most important)



fleet companies as an independent business. Buyout firms Bain Capital and Cinven, meanwhile, agreed a EUR 3.9bn deal to carve out the specialty ingredients unit of Swiss pharmaceuticals group Lonza. Lonza offloaded the division to focus on its core pharmaceuticals and biotech business, which has been boosted by the push to accelerate COVID-19 vaccine manufacturing.

Some 16% of respondents also expect that higher volumes of lapsed deals will become a more prominent trend in European M&A markets. As the first lockdowns came into force across Europe in 2020, a number of high-profile deals that were expected to proceed broke down as a result of COVID-19 concerns. French insurer Covea, for example, stepped back from its planned EUR 8.1bn acquisition of PartnerRe, a Bermuda-based reinsurer owned Italian holding company Exor, because of COVID-19 uncertainty.

New diligence

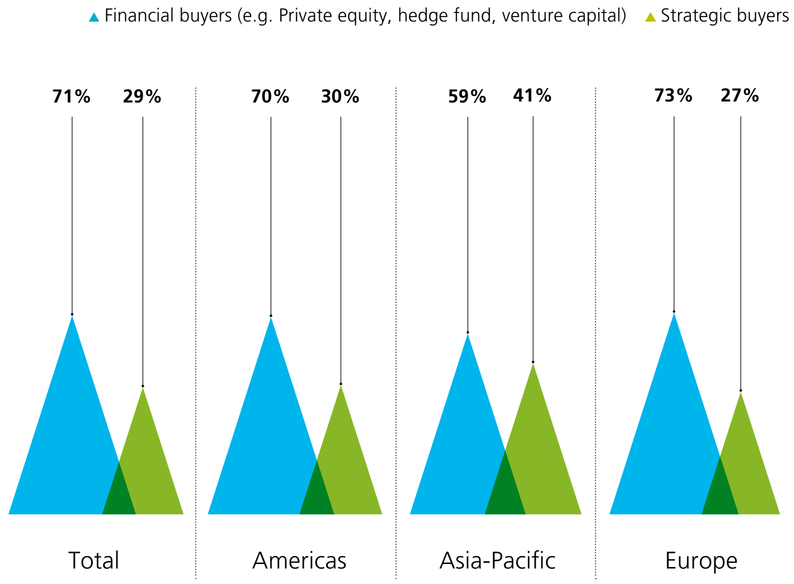
Although deal markets have stabilised this year, the survey findings indicate that broken deal risk continues to be a concern for M&A investors.

This finding dovetails with the view from 19% of respondents that see inability to raise funds as the most important challenge for deals, with 17% citing a more complex due diligence process as the second most important challenge.

Social distancing and travel restrictions saw dealmakers obliged to switch to remote due diligence tools, including replacing site visits with drone footage. Personal interaction has been limited, which has added additional friction to deal processes and prolonged negotiations. The scope of the due diligence exercise has also become broader and more complex as potential buyers forensically examine deal targets to cover off risks in a still uncertain environment.

> Most tools for remote dealmaking, such as virtual data rooms and teleconference negotiations, were already in place before the pandemic. But COVID-19 broke through the last of the resistance and necessitated the acceptance of virtual meetings. Progress has been made in legislative changes to facilitate contactless arrangements, including digital filings and use of electronic signatures.
>
> *Rodica Manea, Partner, CMS Romania*

Which of the following do you feel is better placed to take advantage of buying opportunities presented by COVID-19?

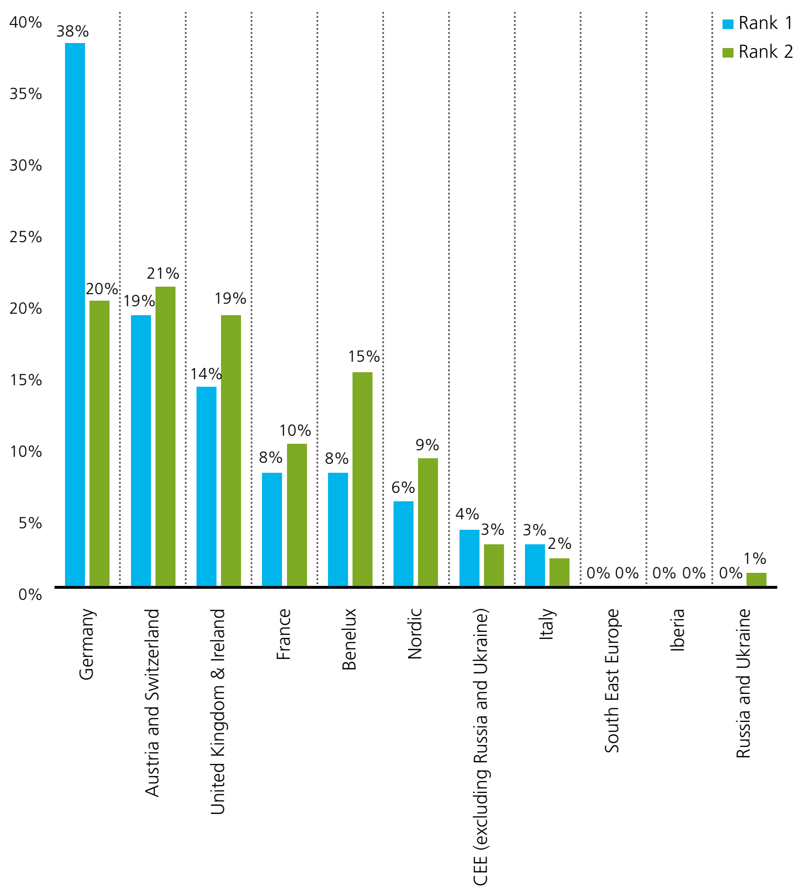


> The scope of the M&A due diligence exercise is now broader and more complex. This includes stricter ESG scrutiny, as targets are investigated to cover off risks in an uncertain environment. But investors have adapted to these COVID-19 challenges faster than anticipated, and are embracing digital due diligence and deal execution.
>
> *Daniela Murer, Partner, CMS Italy*

PE firms have been relatively adept at adjusting to remote due diligence and taking additional complexity in their stride. According to a private equity general partner survey by Investec, 94% of private dealmakers have conducted investment due diligence virtually through the pandemic period. This could be one of the reasons why 71% of respondents to the CMS research agree that financial buyers are better placed than strategic buyers to take advantage of the buying opportunities presented by COVID-19 (although there are regional variations, with only 59% of APAC respondents favouring financial buyers).

The large proportion of respondents expecting PE to be the best positioned to take advantage of post-COVID-19 buying opportunities could also be because of the large sums of dry powder that firms have to invest within set periods of time, whereas corporates are as focused on trimming down

Which regions will see highest growth post-COVID-19? (Please select the two most affected, 1 = highest growth, 2 = second highest growth)



portfolios and selling assets as they are on acquisitions.

Growth in Germany
In terms of regions, well over two-thirds of respondents (38%) expect Germany to see the highest deal growth, followed by Austria and Switzerland (19%), with the UK and France only polling 14% and 8% respectively.

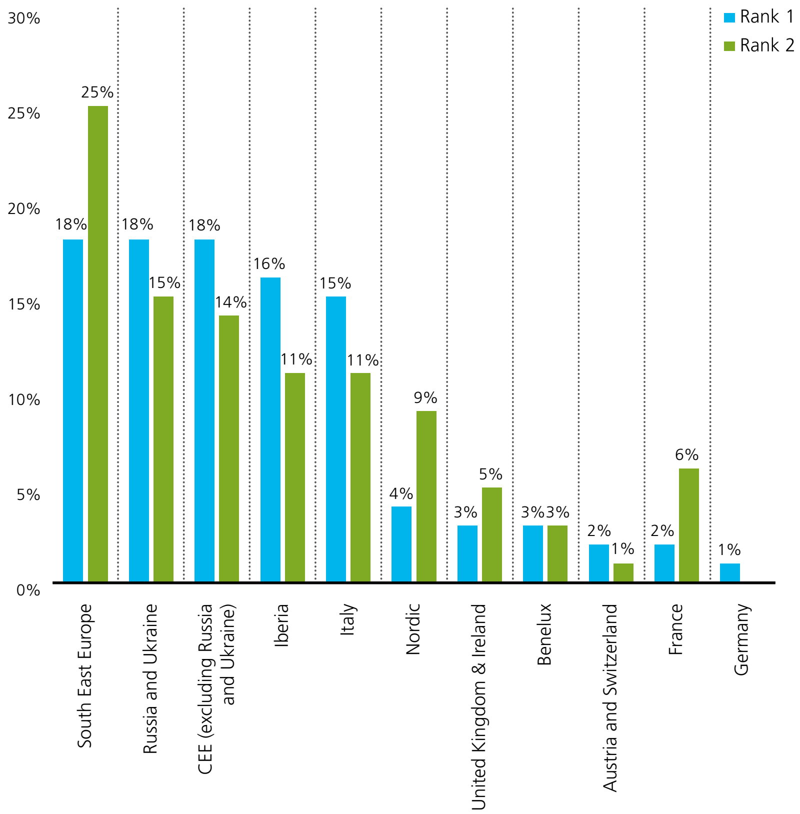
Germany ranks highly even though it has been only the fifth largest bidder for European assets in the first half of this year, trailing the US, France, the UK and Italy.

Survey responses could point to building momentum in the German market and the anticipation of more megadeals in the country like the potential EUR 29bn merger between Germany's two biggest residential real estate companies Deutsche Wohnen and Vonovia.

> Germany, Austria and Switzerland fared well during the pandemic. Their economies remained mostly intact or recovered quickly from the initial shock in March 2020. Politically, the region stayed stable, which from investors' perspective is always preferred. And in the end, DACH remains a major economic centre with great potential for further growth.

Jacob Siebert,
Partner, CMS Germany

Which regions will see lowest growth post-COVID-19? (Please select the two most affected, 1 = lowest growth, 2 = second lowest growth)



Sector watch

Spotlight on TMT
No industry has weathered pandemic disruption better than the TMT sector.

Companies, employees, consumers and students have all relied heavily on technology to maintain business continuity and for shopping, learning, work and entertainment.

Technology giants like Amazon, Facebook, Google parent Alphabet and Microsoft have posted bumper profits through the pandemic period, while the STOXX Europe 600 Technology Index has made gains of 35% over the last 12 months.

The strong performance of technology has made it a go-to sector for M&A dealmakers, who have clustered around technology assets with solid growth fundamentals and clear visibility on future earnings.

As a result, TMT deal value more than doubled in Europe in 2020, despite COVID-19 dislocation, rising from EUR 107.5bn in 2019 to EUR 245.4bn in 2020.

Momentum has continued in 2021, where H1 2021 TMT deal value reached EUR 122.2bn, up year-on-year from EUR 52.4bn.

Platforms that digitise sales channels or harness technology to reach consumers have been a key theme for dealmakers in the space, as seen in the EUR 5.9bn deal for online used car sale platform Cazoo by US SPAC Ajax 1; and the EUR 8.2bn swoop for share trading platform eToro by FinTech Acquisition Corp, also a SPAC.

Given the high levels of technology M&A, it is somewhat surprising to see that survey respondents only rank TMT fourth in terms of sectors likely to see deal growth. The responses suggest that dealmakers are now more comfortable investing in assets that were hit by lockdowns but are rebounding as economies around Europe reopen. With deal activity stagnant in certain sectors for much of 2020, deal pipelines are likely to be overflowing in these industries. TMT dealmakers could also be pausing for breath as regulators scrutinise the technology sector more closely and pursue enforcement of antitrust and data protection compliance more proactively.

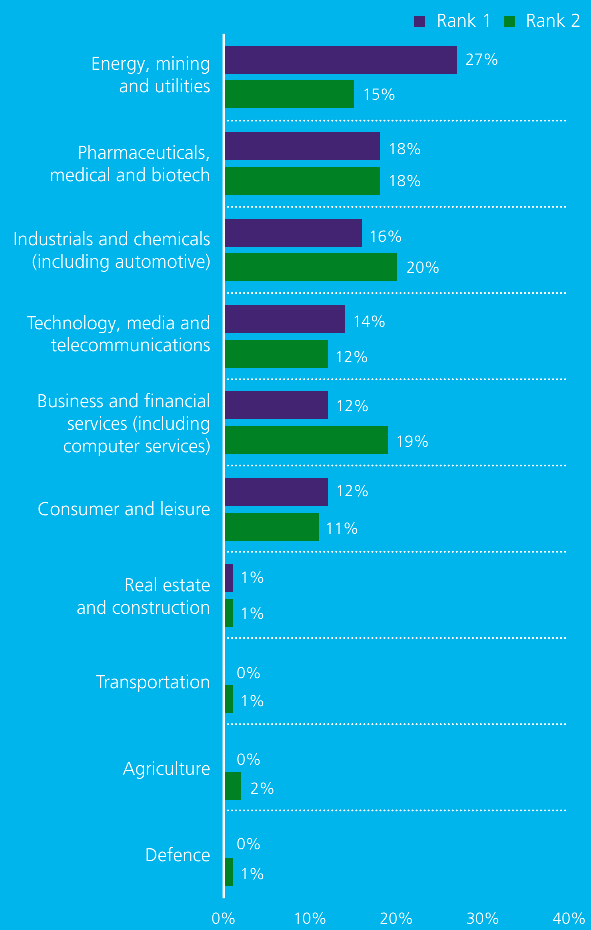
Spotlight on PMB
Deal activity in the European pharmaceuticals, medical and biotech sector has shown steady year-on-year growth in 2021. Deal value for the half-year came in at EUR 50.5bn, a more than three-fold increase from the EUR 15.6bn posted over the same period in 2020.

Sustained healthcare M&A activity has illustrated the sector's appeal as one that presents protection against downside risk as well as long-term underlying growth drivers, including an ageing population and rising demand for medical services. Steady healthcare stock markets – the STOXX Europe 600 Health Care Index is up 14.5% for the year to date – have provided dealmakers with further confidence to pursue transactions in the sector.

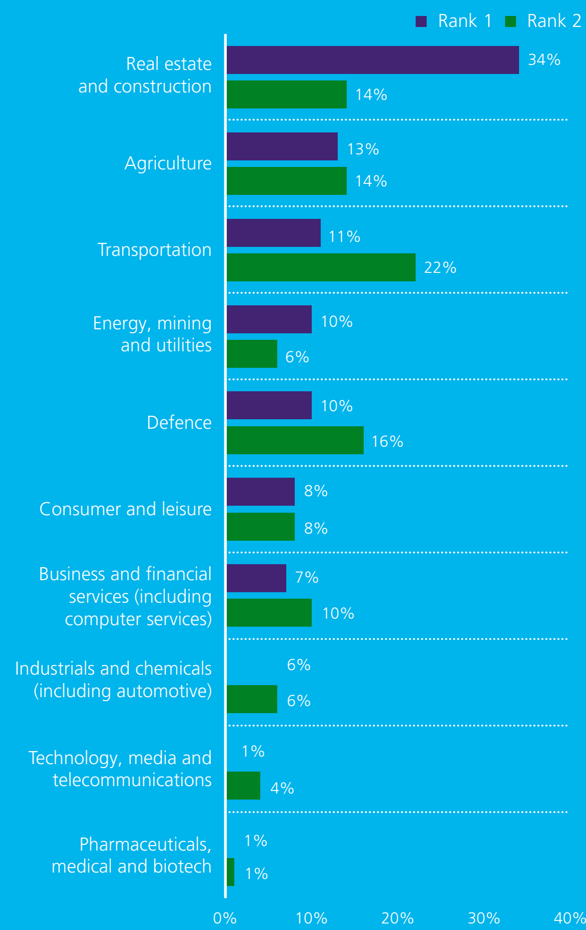
The pharmaceuticals sector has been a major contributor

> In H2 2021, we expect TMT M&A to maintain the strong pace observed during the first six months of the year. Dealmaking in the space will continue to rise, and TMT will stand out as one of the main sectors for M&A. In Spain, transactions will focus on the sale, purchase and deployment of fibre networks for the development of 5G technology.
>
> *Ignacio Zarzalejos, Partner, CMS Spain*

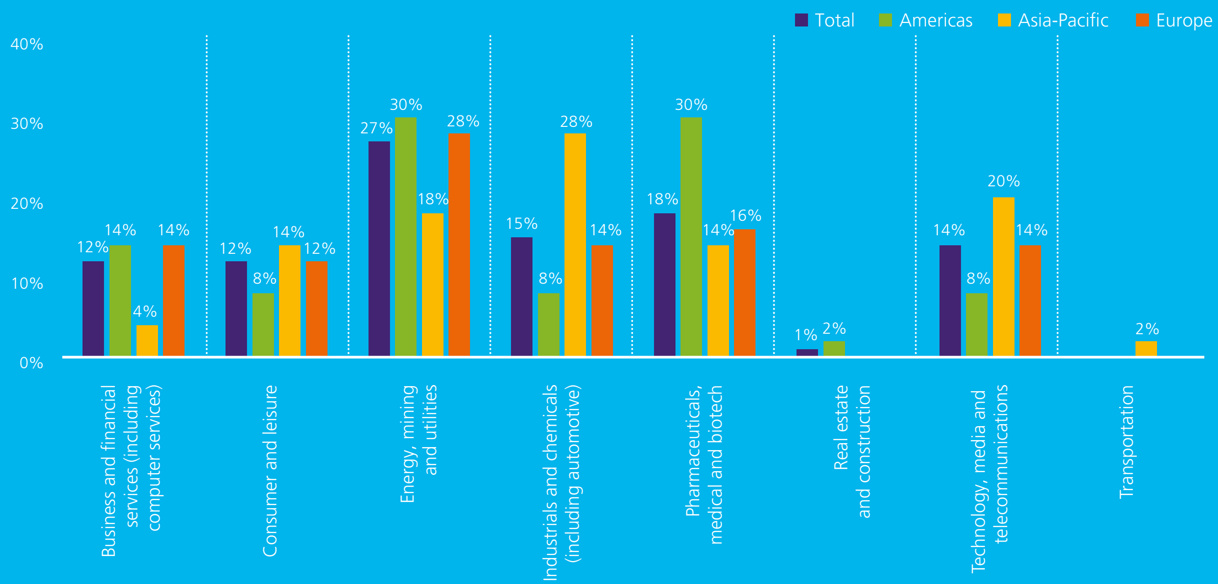
Which sectors will see highest growth post-COVID-19? (Please select the two most affected, 1 = highest growth, 2 = second highest growth)



Which sectors will see lowest growth post-COVID-19? (Please select the two most affected, 1 = lowest growth, 2 = second lowest growth)



Which sectors will see highest growth post-COVID-19?



to European PMB deal value, with large corporates actively seeking opportunities to build scale and expand into new markets through acquisition.

US drug wholesaler AmerisourceBergen, for example, agreed a EUR 5.3bn deal to acquire the distribution business of Walgreens Boots Alliance as part of its plans to grow its European presence.

Dealmakers have also been attracted to fast-growing healthcare subsectors like healthtech, with consultancy Bain & Co calculating that healthcare IT deals have accounted for just under a quarter (23%) of disclosed healthcare buyout value. Swiss-based biopharma and healthcare technology company Roivant, for example, drew a EUR 5.2bn deal from Montes Archimedes, a SPAC sponsored by Patient Square Capital, a specialist US healthcare private equity investor.

In addition to new opportunities in healthtech, dealmakers have also pursued assets in emerging therapeutic areas with strong growth prospects.

US-based pharma group Jazz Pharmaceuticals, for example, agreed a EUR 5.3bn acquisition of GW Pharmaceuticals, a UK-based developer of cannabis-based medicines. GW is developing a drug to treat childhood epilepsy and the deal will expand Jazz's neuroscience portfolio.

Financial buyers have been active players in PMB deals too. Private markets firm Intermediate Capital Group (ICG), for example, acquired DomusVi, a provider of elderly care in France, Spain and China, in a secondary buyout from PAI Partners valued at EUR 4.3bn.

> The last 12 months have been very active for PMB, particularly the medical biology subsector. For the next 12 months, the pace of acquisitions should sustain itself. The pandemic has been an accelerator of growth and EBITDA, with significant free cash flows and a high debt capacity. Mid-cap deals above EUR 500m should remain frequent.
>
> *Christophe Blondeau, Partner, CMS France*

Global M&A in context

Global M&A has rebounded strongly through the first half of 2021 as economies around the world have reopened in earnest and vaccine programmes have rolled out.

Deal value has almost tripled from EUR 849.8bn in H1 2020 to EUR 2.4tn in H1 2021, with all the key global jurisdictions enjoying strong rises in deal value when compared to 12 months ago.

European M&A has mirrored the patterns seen globally, with deal activity falling precipitously in Q2 2020 as investors put new transactions on hold and focused on stewarding existing portfolio companies through the initial wave of pandemic disruption. Dealmakers then gradually started returning to market and building back momentum in the second half of 2020 and into 2021.

European deal value hasn't climbed at the same rate as global figures but has nevertheless shown encouraging improvement, with deal value almost doubling from EUR 236bn in H1 2020 to EUR 496.6bn over the same period this year. Asian deal value has rebounded at a similar rate, improving year-on-year from EUR 260bn to EUR 490bn.

North American M&A markets, however, have supercharged the global deal rebound, with deal value in the region almost quadrupling from EUR 285.6bn over the first six months of last year to EUR 1.2tn in H1 2021.

> Compared to Europe, the US has a huge domestic M&A market and an immense amount of investment capital. Fuelled by PE's excess of dry powder and the funds raised through SPACs, it's unsurprising that this post-election year is setting records.
>
> *Reinout Slot, Partner, CMS Netherlands*

In addition to the post-COVID-19 trends that have boosted deal numbers across all regions, North America has also enjoyed additional tailwinds thanks to the completion of the US Presidential election and the inauguration of President Joe Biden, as well vast Federal infrastructure and COVID-19 relief spending plans.

US dealmakers tapped down on investment ahead of the US poll, but now have clearer visibility on the political backdrop, encouraging dealmaking. The Biden administration has also injected vast sums of capital into the US economy, bringing forward a USD 1.9tn coronavirus relief bill in the early Spring. There is also growing bipartisan support to sign off on a USD 1tn infrastructure package. US dealmaking has also benefitted from the record levels of fundraising by SPACs.

With these dynamics at play in the US, North American M&A has accounted for an outsized share of overall global M&A value. This has meant Europe's share of global M&A value slid from 28% a year ago to 21% for H1 2021, despite the year-on-year recovery in European M&A value in 2021 so far.

Deal dynamics

Even though M&A activity across Europe has surged in 2021, a large proportion of European dealmakers are still taking a wait-and-see approach

Top findings

24%
of survey respondents are considering acquisitions

25%
are considering divestments

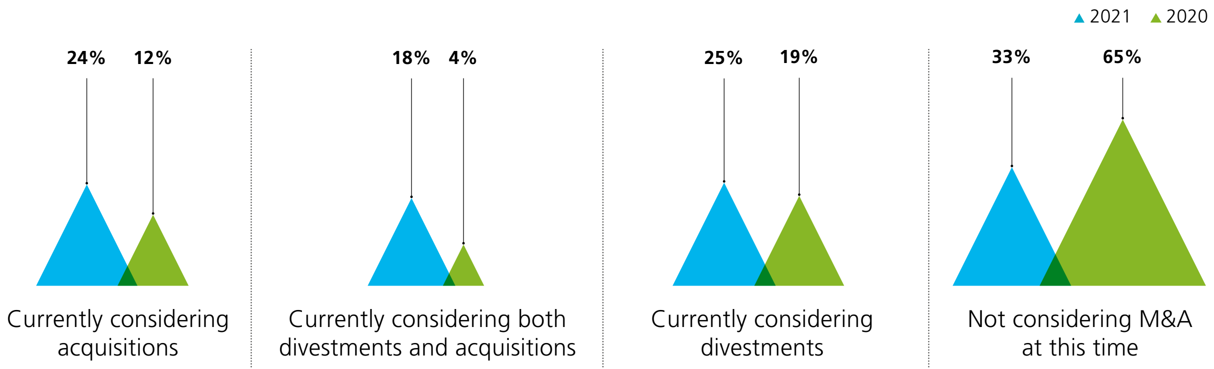
29%
of respondents say appetite for M&A would increase if the EU does much more together across all policy areas

31%
think that the UK will become less attractive for M&A post-Brexit

Our survey reveals that a third of respondents (33%) are not considering deals at this time when asked where M&A fits into their corporate strategy. Although a vast improvement on survey findings from a year ago, when almost two-thirds (65%) of those polled were not considering M&A, this still represents a sizeable minority who are not looking at deals. When M&A is on the table, there are as many corporates looking to divest assets (25%) as there are considering acquisitions (24%). When firms are looking at new deals, appetite is equally split between smaller bolt-on deals and large transformational deals. Both options polled 19% in the survey.

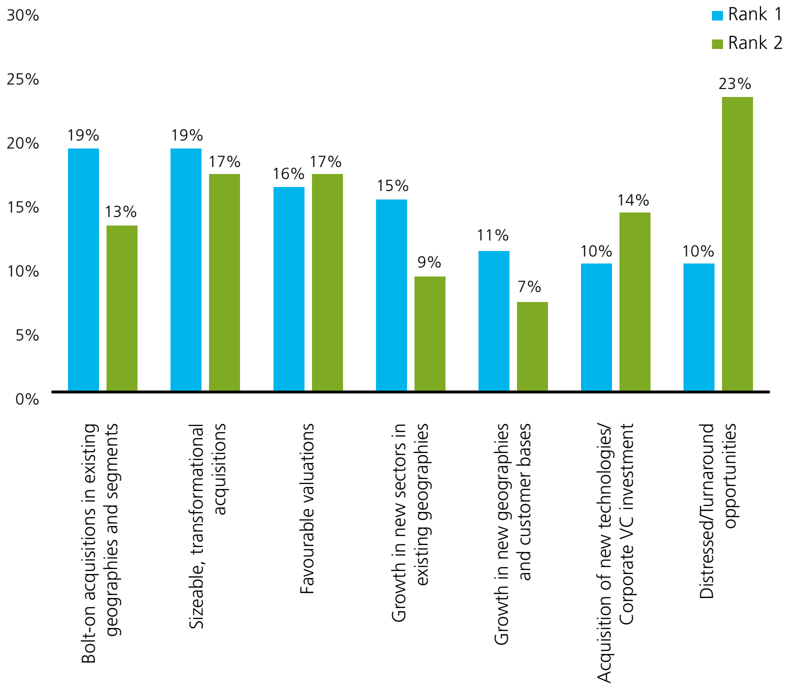
For many corporates the focus now is on fully reopening businesses and offices as COVID-19 restrictions ease, which explains why more manageable bolt-on deals have been preferred by some. In some industries, however, the acceleration of digitalisation and importance of scale has made transformational deals necessary, as seen in the EUR 4.9bn merger between Italian payments processing groups SIA and Nexi. The merger follows an acceleration in the switch away from hard cash during the pandemic as well as a period of ongoing consolidation in the European payments space.

Where does M&A currently fit into your corporate strategy? (Please select only one)

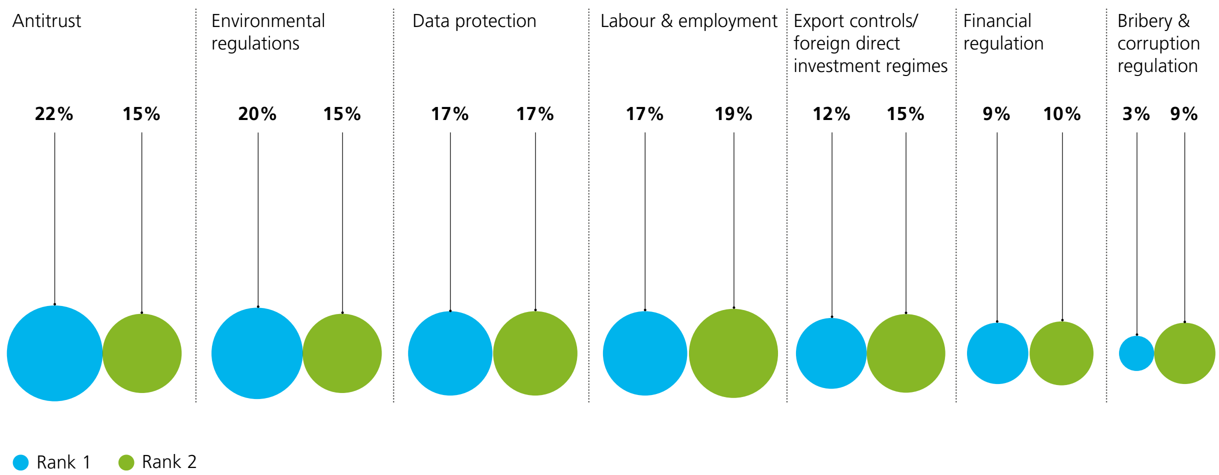


> Dealmakers perceive FDI control regulations as difficult and hard to predict, which can make the M&A process more burdensome. Now it is often the case that FDI issues are front-loaded and, every once in a while, a transaction is stopped before negotiations can even begin.
>
> *Stefan Brunnschweiler, Partner, CMS Switzerland*

If you are considering acquisitions in Europe, what is the motivation for this? (Please select the two most important, 1 = most important, 2 = second most important)



Which form of regulation do you find most challenging when doing a deal in Europe? (Please select the two most important, 1 = most important, 2 = second most important)



Regulatory headaches

In terms of regulatory challenges, antitrust (37%) is the form of regulation that respondents find most challenging. Although down from 50% in last year's survey, dealmakers remain sensitive to antitrust interventions and have noted how the US has boosted its technology antitrust capabilities. Large deals, such as a planned EUR 31.1bn merger between Aon and Willis Towers Watson, meanwhile, have been called off because of antitrust headwinds.

After antitrust, labour and employment law also ranks highly (36%) and is up from 20% in the 2020 survey. Employee activism, cultural issues in the workplace and the changing nature of work through the course of the pandemic have all added additional complexity to employment considerations in M&A deals and due diligence.

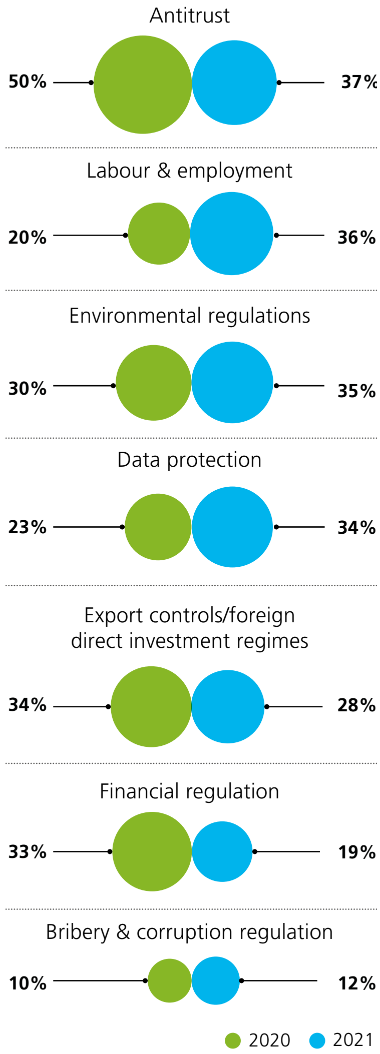
Deal drivers

In terms of catalysts for M&A, 29% of respondents say appetite for M&A would increase if the EU does much more together across all policy areas. This is down from 50% in last year's survey and the dip could reflect acknowledgement that various EU-led COVID-19 relief packages have been effective and encouraged investment.

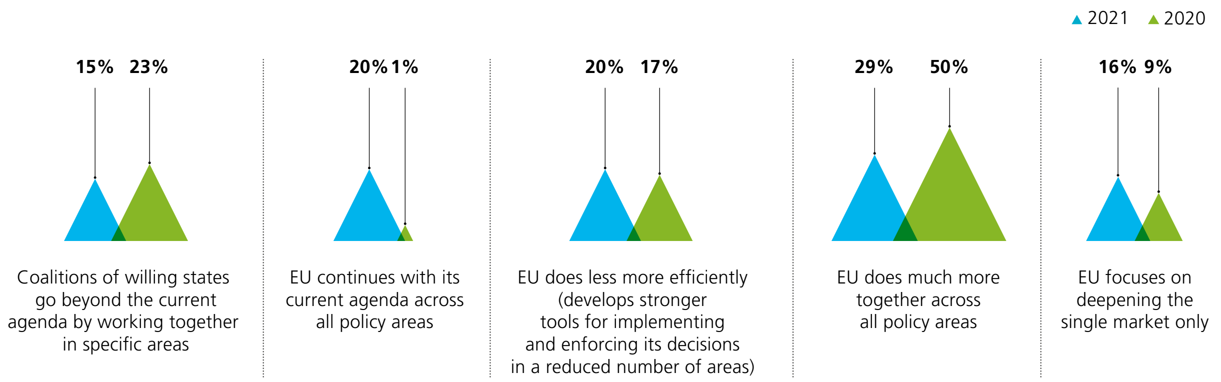
> Individual European member states' foreign investment screening regulations can vary greatly. Especially in periods when regulators are increasingly interested in protecting national interests, this can make the M&A process much more complex. Where most targets have a presence in more than one member state, Europe-wide legislation could help to reduce such uncertainties.
>
> *Alexandra Rohmert, Partner, CMS France*

The EU, for example, has made EUR 800bn available through grants and loans to member states to repair COVID-19 economic damage. The funding is supported by ground-breaking collective borrowing by the European Commission and underwritten by member states. The capital will be focused on green and digital projects and improving public sector efficiency.

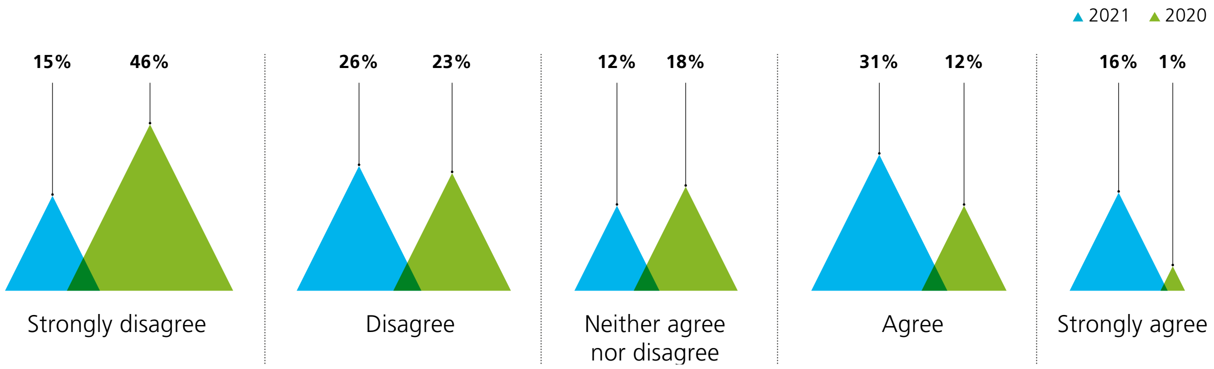
Which form of regulation do you find most challenging when doing a deal in Europe?



Looking at the future direction of the EU, which of the following scenarios would most increase your appetite for M&A in Europe over the next three years? (Please select one)



To what extent do you agree with the introduction of a mechanism for European screening of foreign direct investments into the EU?



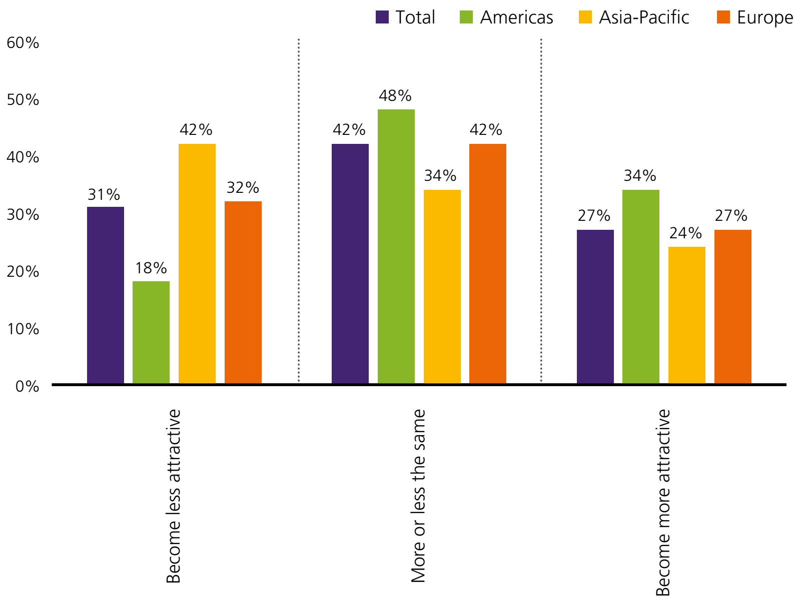
Along similar lines, this year's survey also reveals growing support for the EU's plans to screen foreign direct investment into the continent with a European-wide framework, rather than leaving screening to individual states.

Some 47% of survey participants (16% strongly) agree with the introduction of a mechanism for the European screening of foreign direct investments into the EU. Some 41% (15% strongly) don't agree. This represents a noticeable shift from last year's survey, when 69% disagreed with the introduction of a mechanism for European screening of foreign direct investments into the EU, including 46% who strongly disagreed.

Regarding country prospects, close to a third of respondents (31%) think the UK will become less attractive for M&A, even though deal value in the UK has outpaced other European jurisdictions by some margin this year. APAC respondents are especially bearish on UK deal prospects post-Brexit, with 42% expecting the UK to be less attractive for inbound deals. This could reflect the more hawkish stance from the UK government towards China and ongoing tensions between the two countries over Hong Kong.

> Despite Brexit, the UK's M&A market remains strong. While overseas companies looking to establish a European presence may consider other jurisdictions, currency fluctuations are still likely to make UK companies attractive targets for international buyers.
>
> *Helen Johnson, Partner, CMS UK*

How do you see the UK market developing post-Brexit in terms of desirability for inward investment?



Private equity overview

PE managers have come through pandemic disruption with portfolios intact and with sustained appetite for deploying capital into new deals and realising proceeds by pursuing exits.

There have been 1,139 buyouts in Europe over the first half of this year, with buyout deal value coming in at EUR 186.9bn. This marks a significant improvement on the 603 buyouts worth EUR 79.9bn posted over the first six months of 2020.

Exit activity has bounced back in similar fashion, with 631 exits worth EUR 97.8bn secured over H1 2021, up from 337 sales valued at EUR 43.4bn posted for H1 2020.

The year-on-year rise in European buyout and exit deal value and volume is illustrative of how private equity firms initially put new investment and exits on hold through the first weeks of pandemic lockdowns but have since moved aggressively to catch up on lost time and put capital deployment timetables back on track.

European PE managers have seen dry powder levels increase over the last 18 months to reach a record USD 351.6bn. Robust fundraising activity has supported swelling private equity war chests, with European firms clocking up their second-highest annual total for fundraising in 2020 according to Pitchbook figures.

According to the Argos Index, which tracks the valuations paid for private European mid-market M&A deals, investment funds have paid record-level multiples of up to 12.9x EBITDA on average in Q2 2021.

> Despite the recent challenging fundraising environment, we see many European PEs as having accumulated relatively significant dry powder that puts them in competitive stead with, in particular, their US peers active across the same European hotspots.
>
> *Victoria Henry, Partner, CMS UK*

> It remains to be seen whether exits by sale to a SPAC will proliferate in Europe – in the region, SPACS have not yet commercially outperformed and are less established than in the US.
>
> *Ralf Kurney, Partner, CMS Germany*

Hungry to deal
Capital-rich buyout investors have been eager to transact and are prepared to meet high valuations. Full multiples have given managers the confidence to bring assets to market for sale, which accounts for the strong growth in exit activity.

That said, firms have been selective in pursuing assets of the highest quality. Initially this saw dealmakers focus on technology and healthcare, although firms are now starting to look beyond these 'safe haven' sectors, as in the EUR 5.1bn deal for aircraft business Signature Aviation. Against a more stable backdrop, some managers are seeing opportunities beyond the pandemic. Starwood Capital, for example, successfully pursued a EUR 4.2bn buyout of Austrian Commercial real estate group CA Immobilien Anlagen, anticipating a recovery in demand for commercial office space post-pandemic.

PE firms have also been innovative and open to deploying capital in flexible ways. PE-sponsored corporate carve-out activity has accelerated, and firms have expanded beyond control buyouts to deploy capital piles in minority deals and growth equity investment structures.

The UK has accounted for the lion's share of European PE deal flow, with exit, buyout and secondary buyout activity totalling EUR 69.5bn in H1 2021. France ranked second with a total of EUR 44bn, while Italy showed strongly with overall deal value of EUR 28.4bn for the period. Germany's total came in at EUR 17.2bn. The UK, historically the region's largest PE market, received a lift going into 2021 after the negotiation of post-Brexit free trade deal with the EU at the end of 2020 and an increasing volume of inbound investment from US SPACs.

Foreign direct investment environment

COVID-19 took a heavy toll on foreign direct investment (FDI) into Europe in 2020, with research from EY showing a 13% decline in European FDI in 2020 when compared to 2019. This represents the first double-digit drop since 2009.

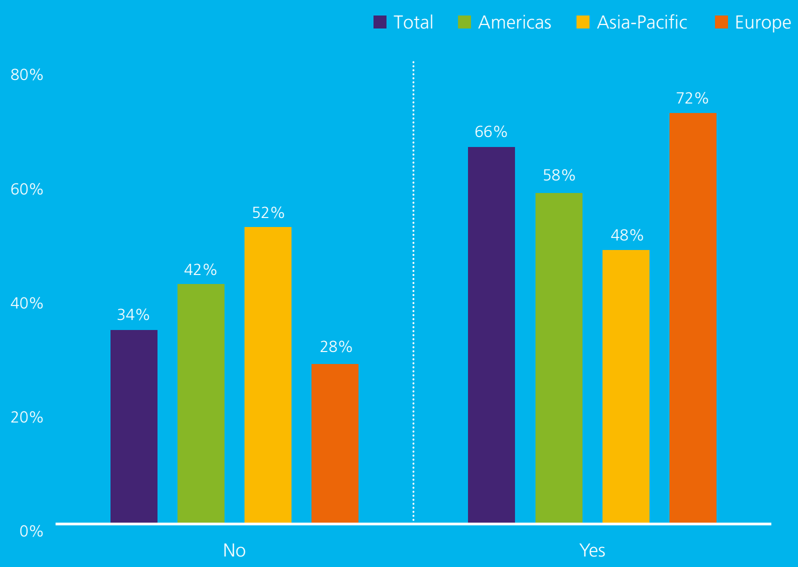
Pandemic travel restrictions and the fact that investors put projects on hold through the COVID-19 dislocation period would have contributed to the decline, but the survey shows that a large proportion of respondents are not planning to accelerate investment into Europe even as coronavirus risk subsides.

More than a third of respondents (34%) are not planning to invest in Europe in the next three years, with APAC respondents especially bearish on the continent. More than half (52%) of APAC survey participants say they have no plans to invest in Europe.

The muted appetite for European FDI is partly down to the long-term impacts of COVID-19 on deal markets, with a fifth of respondents citing COVID-related challenges, such as more complex due diligence, as a bigger obstacle for overseas investors than domestic players. COVID-19 has seen a pivot by European businesses to near-shoring and on-shoring supply chains too, another factor that could dampen FDI appetite.

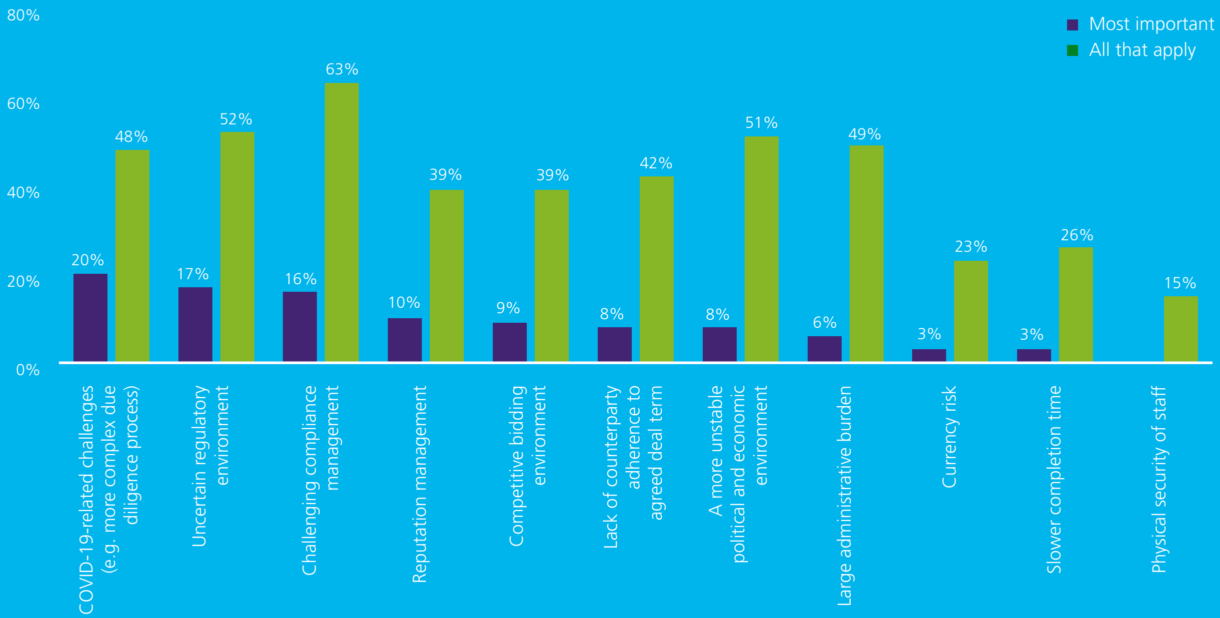
An uncertain regulatory environment, chosen by 17% of participants, also ranks

In the next 3 years, are you planning to invest in Europe?

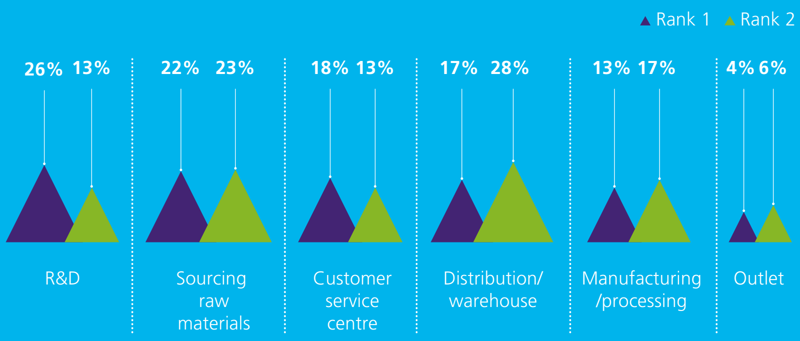


> An increase in protectionist measures in some jurisdictions, juxtaposed with a relaxation of protections in others, means investors are having to search further for the right opportunity. With many investors well capitalised and feeling the pressure to deploy, we expect cross-border activity to grow through 2022, particularly in foodtech, healthtech, fintech, cybersecurity and e-commerce solutions.
>
> *John O'Connor, Partner, CMS UAE*

What do you expect will be the biggest risks to investing in your country of choice?



What type of facility is your organisation planning to build overseas? (Please select the two most important, 1 = most important, 2 = second most important)



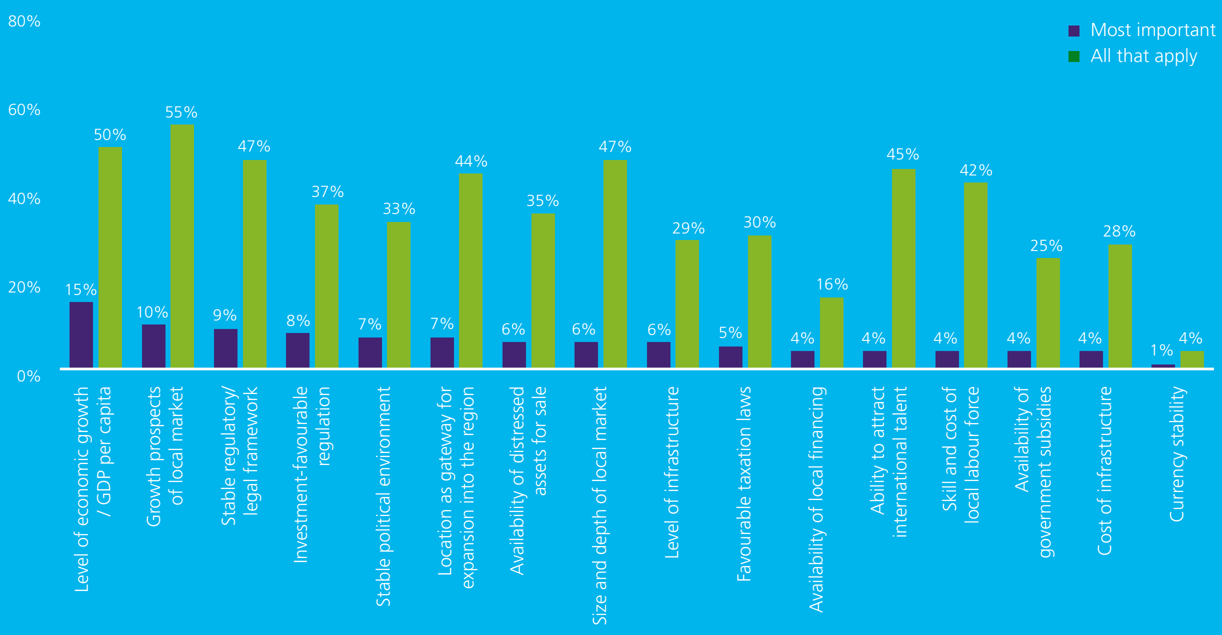
> Most respondents are displeased with the introduction of a screening mechanism for FDI into the EU. But similar measures have been in place for long periods elsewhere, including China and the US. It seems these mechanisms will become the norm more or less everywhere. Though they add red tape, lead to delays and some uncertainty, overall investment opportunities remain strong.
>
> *Ulrike Glück, Partner, CMS China*

highly as an FDI risk. Indeed, European regulators have moved to put more stringent procedures in place for clearing inbound foreign investment.

The European Commission, for example, published proposed regulation and an impact assessment report targeting potential distortions to its single market caused by foreign subsidies. Under the proposed rules, companies will have to notify the European Commission of any transaction financed by overseas subsidies as well as make additional disclosures when participating in any public procurement deals valued at EUR 250m or more.

At the end of 2020, the UK, Germany and France also put in place additional investment screening regulations governing the clearance of M&A activity on national security examples. This followed a broader global trend of governments overhauling national security rules governing inbound M&A from abroad.

What are the factors that will most impact your choice of your investment(s) outside your home country?



Economic growth in regions selected for investment outside of home countries (15%) is also a key factor when considering FDI, as are the growth prospects in the local markets of potential FDI investors.

Given the added regulatory and deal execution friction that now comes with cross-border deals and investment, there needs to be a compelling case for looking abroad to invest. Although forecasts for European growth are an upbeat 4.8% for 2021, the US is expected to grow 6.7% this year and China is on track for an 8.4% GDP rise. Investors in these two nations, and in other countries, are likely to consider investments here first before looking to European options.

For participants that are considering FDI projects, investing in R&D facilities abroad is chosen by the largest proportion of respondents with FDI plans. More than a quarter (26%) of respondents plan to plough capital in R&D initiatives abroad.

Although it is difficult to pinpoint why R&D is particularly appealing for FDI projects, one explanation could be the example of the COVID-19 vaccine development project, which saw multiple parties working around the world to develop a vaccine, with funding from multiple countries and multinationals driving the progress of the vaccine's development.

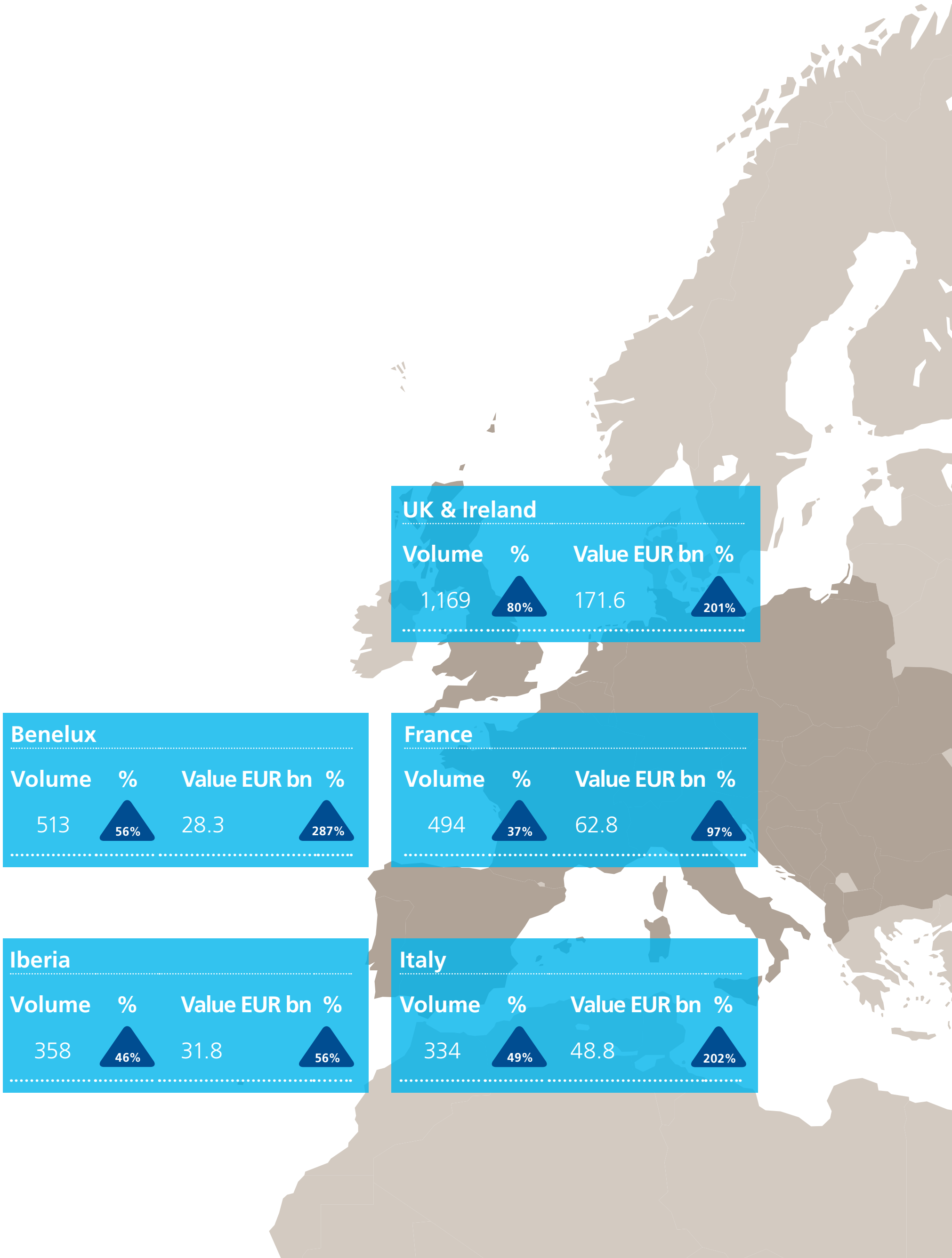
> FDI screening rules have already been extended in some European nations. This applies notably to 'critical technology' businesses, which gained particular importance over the last few years. We expect several other European countries to follow suit.
>
> *Błażej Zagórski, Partner, CMS Poland*

Regional round-up

Compared to H1 2020, M&A activity in Europe rose dramatically, in both volume and value terms, in the first half of 2021.

The UK & Ireland remains the region's lead market, accounting for 34.6% of total deal value and 23.3% of total deal volume.

France and the Nordics were the next most important markets, contributing 12.7% and 10.2%, respectively, of Europe's aggregate deal value. The Nordics also accounted for an impressive 19.2% of total deal volume.



Nordics

Volume	%	Value EUR bn	%
966	105%	50.6	431%

Russia & Ukraine

Volume	%	Value EUR bn	%
69	-4%	4.9	-36%

Germany

Volume	%	Value EUR bn	%
554	34%	47.2	-9%

CEE

Volume	%	Value EUR bn	%
287	50%	12.6	54%

Austria & Switzerland

Volume	%	Value EUR bn	%
190	47%	23.5	17%

SEE

Volume	%	Value EUR bn	%
83	32%	9.4	70%

This infographic compares H1 2020 with H1 2021

ESG factors in Europe

The fall-out from the pandemic and intensifying focus on mitigating climate change have thrust environmental, social and governance (ESG) to the forefront of M&A strategies and due diligence

Top findings

72%
expect ESG scrutiny to increase during the next three years

65%
predict that ESG due diligence will be subjected to more scrutiny

18%
point at water management as the most important ESG issue

66%
chose energy, mining and utilities as the sector that would be most affected by wider ESG implementation

The pandemic has highlighted how business profitability is inextricably linked to public health and social and environmental stability, prompting dealmakers to build ESG criteria into their M&A strategies.

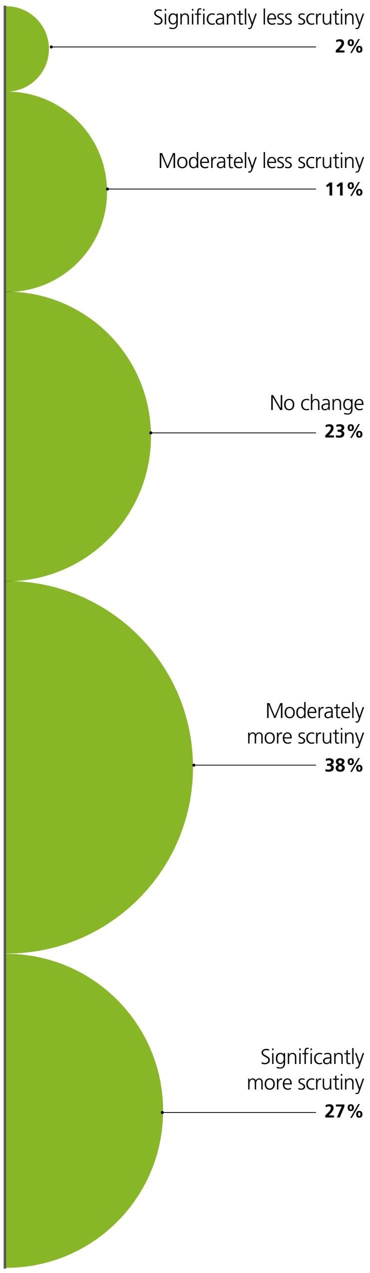
Survey respondents see this as only the beginning, with 72% expecting ESG scrutiny to increase during the next three years, and 65% predicting that due diligence will be subjected to more scrutiny in terms of ESG factors over the same period.

Doing good to perform well
There is also growing evidence to show that companies and dealmakers who assign higher priority to ESG in their processes outperform their peers. Good corporate citizenship and financial performance are no longer deemed mutually exclusive.

According to a 2021 corporate divestment survey compiled by EY, almost three-quarters of PE firms (72%) factor in an ESG premium on valuation when selling assets that have specific ESG capabilities. Indeed, investors are noticing the financial and risk benefits of backing managers and businesses that have credible ESG strategies in place, and there has been an almost 50-fold increase in the number of signatories to the UN Principles for Responsible Investment (UNPRI) between 2006 and 2020.

ESG is also becoming increasingly important for securing financing. Companies with green and sustainability goals built into business strategies have been able to tap into burgeoning green and sustainability-linked pools of capital. Ratings agency Standard & Poor's is forecasting record issuance of sustainability-linked debt in 2021, with activity expected to exceed USD 200bn. Swedish oat milk producer Oatly, for example, raised a sustainability-linked financing package to finance the construction of two new factories.

How do you expect due diligence to change in terms of ESG factors in transactions in the next three years?

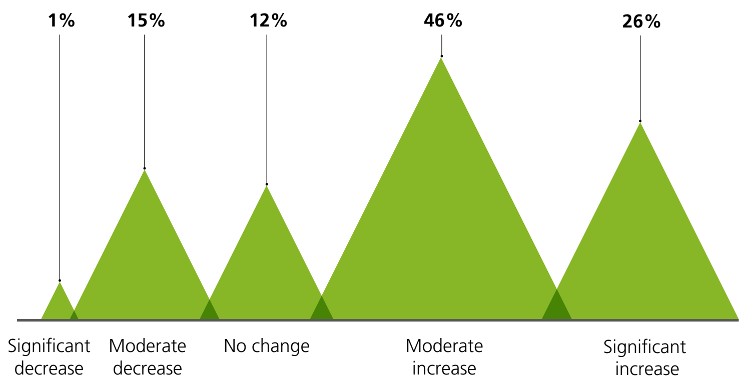


The European green bond market, the largest in the world, meanwhile, has driven record issuance of green bonds in Q1 2021, with more than USD 53.6bn of green bond financing secured over the period – just over half of the global total of USD 106.9bn.

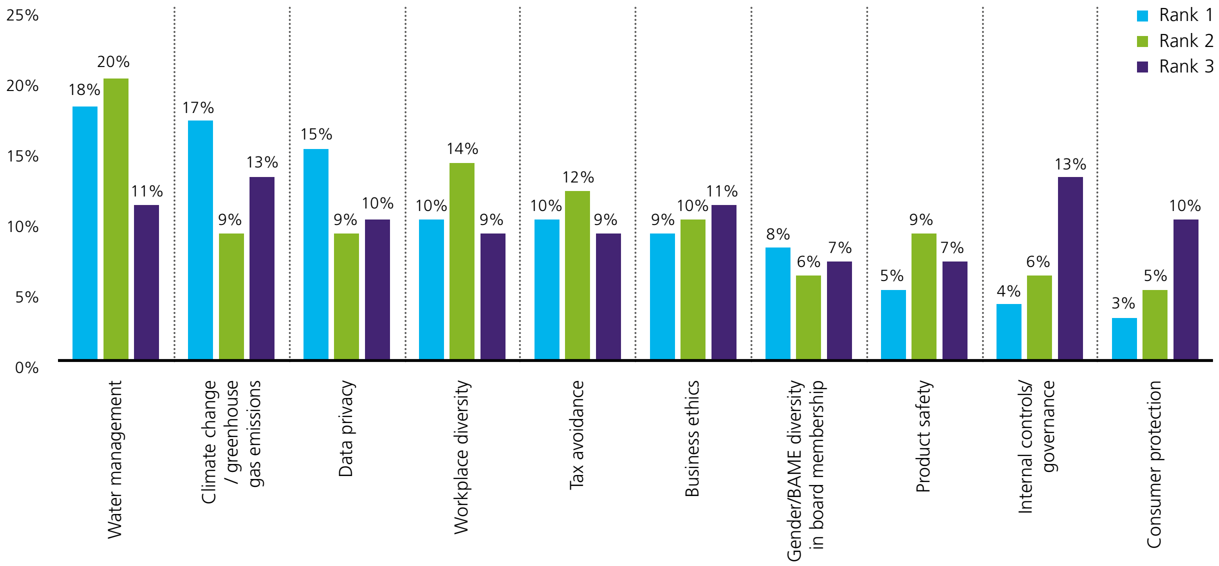
Even mainstream debt products are now including ESG terms. European lenders and borrowers have led world markets here, pioneering the inclusion of ESG ratchets in debt agreements. These ratchets either increase or decrease the margins payable by borrowers on their debt, depending on compliance with pre-set ESG key performance indicators. French biosecurity and food safety business Kersia, for example, included an ESG-linked margin ratchet as part of the financing package for its acquisition by pan-European buyout firm IK Investment Partners.

> Over the past 18 months, many companies have looked with envy at the multiples that newly-listed 'ESG companies' have attracted on the Euronext Growth trading market. That has generated a huge number of spin-offs and IPOs. The 'E' in ESG has been the common denominator, but the 'S' and 'G' must be carefully managed as well.
>
> *Johan Svedberg, Partner, CMS Norway*

How do you expect ESG scrutiny to change in deals over the next three years?



Which ESG issues are most important to your firm and your current investor base? (Rank from 1 to 3, where 1 = most important)



Priorities, industries and challenges

Although ESG is fast becoming a standard feature of deals, it covers a wide range of bases and for now dealmakers are prioritising certain aspects of ESG as they build their reporting and due diligence infrastructure. Survey respondents, for example, pointed to water management (18%) and climate change/greenhouse gas emissions (17%) as the most important ESG issues for firms and their investor bases.

When it comes to sectors that respondents believe will be the most affected by wider ESG implementation, 66% chose energy, mining and utilities and 48% opted for industrials and chemicals. One explanation for the selection of these industries is the fact that they will have to go through periods of transformation as part of wider energy transition plans and government ambitions to achieve net zero emissions by 2050.

> The lack of a shared framework for assessing ESG credentials is a key challenge. Common standards help to build trust and stability, which can otherwise take years to develop. The businesses we have worked with focus mainly on governance and establishing a resilient business with stable and updated solvency planning.
>
> *Alexandra Schluck-Amend, Partner, CMS Germany*

According to asset manager Aberdeen Standard, retrofitting and rebuilding energy infrastructure to deliver net zero carbon emissions by 2050 will require investment of between USD 1tn and USD 2tn per year between now and 2050.

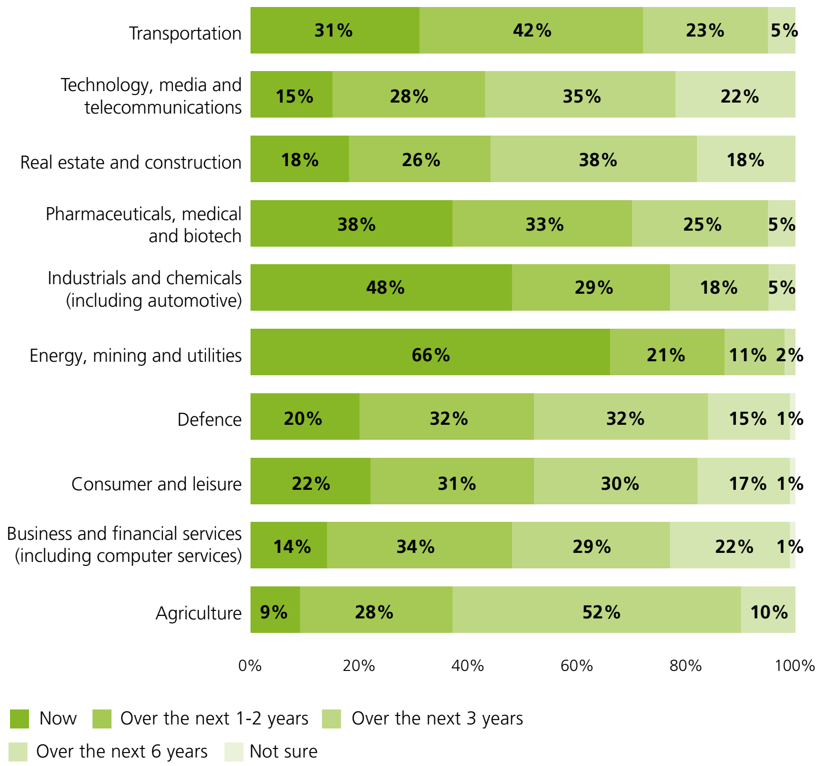
ESG-focused reporting and M&A is expected to play a key role in delivering the required investment, and energy companies have already started to pivot their businesses towards renewables as revenues from oil and gas production reduce. French oil major Total, for example, has undertaken a series of acquisitions to diversify away from oil and gas and reposition as a broader energy business.

The biggest challenge for dealmakers attempting to address ESG, across all industries, is how to choose ESG KPIs and what frameworks to apply when assessing the ESG maturity of a target company. ESG reporting is still nascent and ESG benchmarks and standards have proliferated. Many dealmakers are still grappling with how to assess and report on ESG in companies and are nervous about applying bespoke ESG assessments in case these are deemed to be superficial or mere window dressing.

Investors recognise these challenges and in the absence of standardisation have given dealmakers and management teams the room to set out ESG criteria that are relevant and achievable for their companies.

ESG policies, however, must be coherent and meaningful. Companies and M&A investors who don't back up ESG claims with substance, or take a superficial approach to ESG due diligence, run the risk of reputational and business damage.

When do you think the industries below will be affected by a wider implementation of ESG factors?



Financing conditions

Access to financing in Europe has rarely been this benign and both the market and our survey results bear this out

Top findings

46%
of respondents expect financing market conditions to become easier in 2021 compared to 2020

26%
of respondents picked PE as the most important source of financing for the next 12 months

28%
see availability and cost of leverage as the single greatest challenge to financing deals

28%
think that underlying economic weakness is the biggest challenge

Abundant liquidity and low interest rates have supported a robust recovery in debt and IPO issuance across Europe, with private equity firms also active and open for business. High yield bond and leveraged loan issuance in Western Europe has increased from EUR 206.1bn in H1 2020 to EUR 249.5bn H1 2021. Banks and institutional investors have been eager to deploy capital in fixed income assets in a low interest rate environment, a trend likely to continue with the European Central Bank pledging to keep rates low for the foreseeable future.

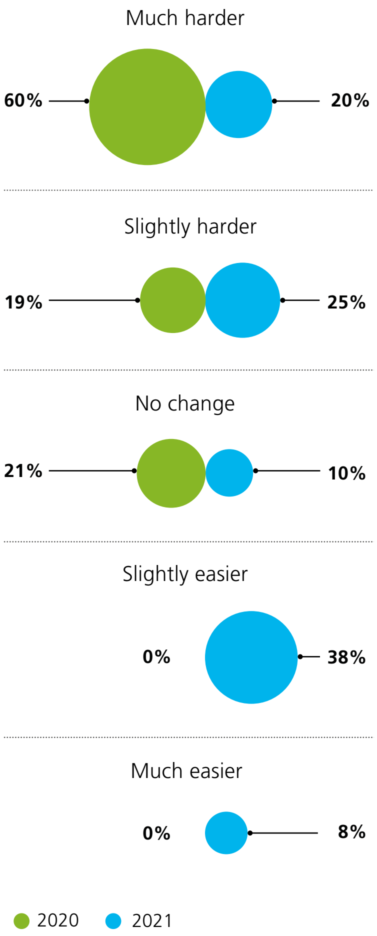
IPO candidates have also benefitted from strong investor demand, with the 223 IPOs recorded in Europe over the first half of 2021 securing EUR 44.6bn in proceeds, according to PwC figures. This marks a significant improvement on figures for the same period in 2020 when there were only 31 successful IPOs securing proceeds of EUR 5.5bn.

PE leads the financing pack
Buoyant lending and IPO markets have supported a significant shift in survey respondent sentiment. A year ago, 79% of respondents said they expected financing conditions to be harder in 2020 compared to 2019, but this year 38% of respondents expect financing market conditions to become slightly easier in 2021 compared to 2020.

> The strong economic recovery and accommodative monetary policy and have significantly increased the volume of deal financings in 2021. More attention is being paid to ESG criteria, which now feature in a large number of deals. In the future, this may create difficulties for the financing of deals that are less ESG-friendly.
>
> *Vivian Walry, Partner, CMS Luxembourg*

> Although Europe's IPO market has been stronger in 2021 so far and equity financing has been widely used for UK M&A, debt remains historically cheap and readily available for companies looking at M&A. This is particularly true for PE, with the result being that PE is running rampant in Europe's M&A market.
>
> *Charles Howarth, Partner, CMS UK*

How do you expect financing market conditions to be in 2021 compared to 2020?



But even though stock market and lending statistics show that debt and IPO capital are readily available, the majority of survey respondents see private equity capital as the most important source of financing for deals during the next 12 months. More than a quarter of those polled (26%) picked PE as the most important source of financing for the next 12 months, with 23% selecting it as the second most important source of capital. Only 5% see equity capital markets as the most important source of financing, with 9% opting for it as the second most important source of capital.

Despite pandemic uncertainty, European private equity fundraising posted its second-highest annual value figure on record in 2020, according to Pitchbook figures, while Preqin data shows European private equity firms sitting on more dry powder than at any other time in history.

Direct lending on the rise

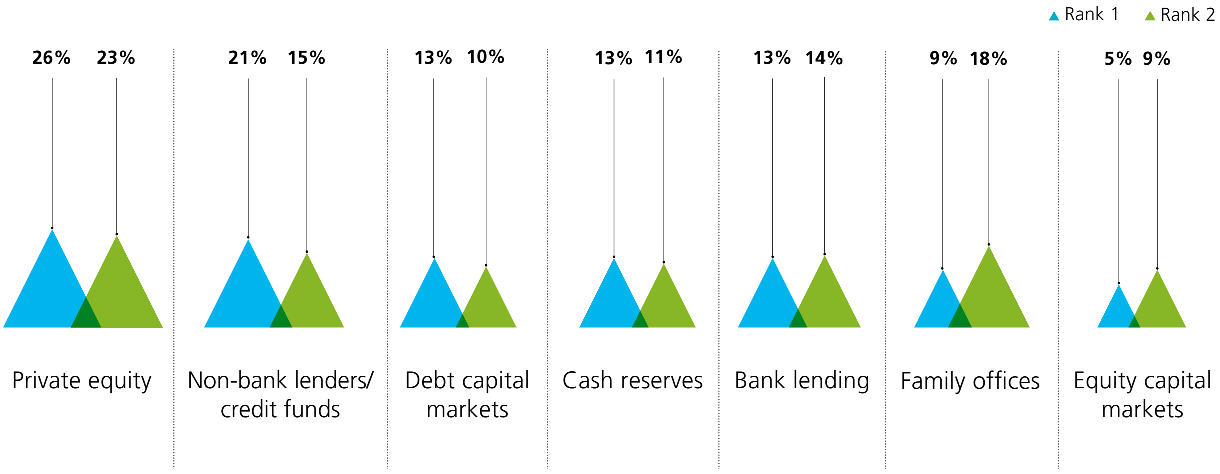
After private equity, non-bank lenders and credit funds ranked the next most likely source of finance, with 21% saying it is the most important pool of capital and 15% identifying these lenders as the second-most important financing option.

Like PE firms, European direct lenders and credit funds have been able to continue securing large allocations of capital to manage from investors and institutions. Private markets firms Ares and ICG, for example, are targeting USD 10.1bn and USD 9bn respectively for their most recent European senior debt direct lending funds. Another European direct lender, Hayfin, landed EUR 5bn for its newest senior debt vehicle.

In addition to securing backing for senior debt strategies, credit funds have also raised significant sums for distressed debt funds focused on European opportunities. LCM and Strategic Value partners are both raising distressed debt funds, targeting USD 4.4bn and USD 4bn respectively.

Successful fundraisings by private credit managers across a variety of strategies is one explanation for the high rankings survey respondents attribute to credit funds, as these

What sources of financing do you think will be most available over the next 12 months? (Please select the two most important, 1 = most important, 2 = second most important)



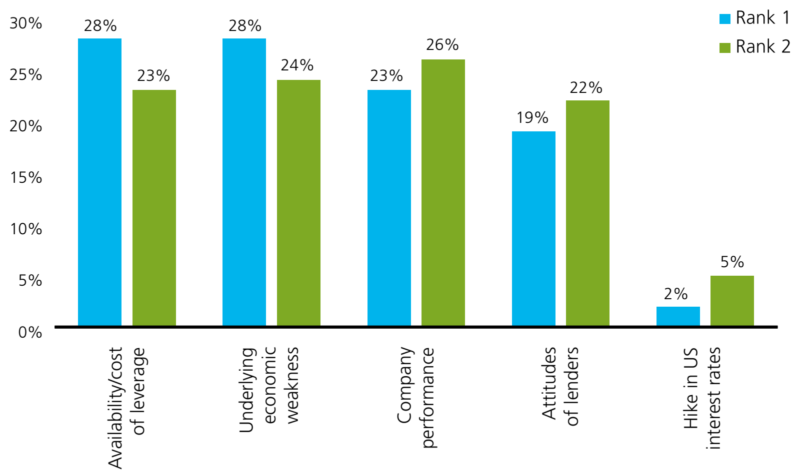
vehicles are well-positioned to provide flexible financing at scale for a broad universe of lenders across a wide range of scenarios.

But although private, public and debt capital markets appear to be replete with cash and ready to put money to work, more than a quarter (28%) of respondents see availability and cost of leverage as the single greatest challenge to financing deals over the next 12 months. This could be a sign that dealmakers have taken note of rising inflation in Europe, which exceeded the ECB's 2% target in July. If inflation continues to climb this could see interest rates go up, which would see borrowing costs increase.

The survey also reveals that dealmakers are still cautious about the recovery of the wider economy while COVID-19 and the spread of variants remains a risk. Some 28% of respondents chose underlying economic weakness as the biggest challenge to financing deals over the next 12 months, with 24% seeing this as the second main challenge to deal financing during the year ahead.

> Direct lending is much more common than five or ten years ago. The market continues to expand confidently across Europe, offering enough flexibility to be an alternative to bank lending and financing ever larger transactions. As an asset class, however, it is yet to be tested in a downturn.
>
> *John Dawson, Partner, CMS UK*

What do you view as the greatest challenge to financing acquisitions over the next 12 months? (Please select the two most important, 1 = most important, 2 = second most important)



Conclusion

The outlook for European M&A over the next six to 12 months is positive, with dealmakers taking confidence in the success of vaccination roll-outs, improved prospects for economic growth and steady stock markets.

In addition to the stabilising macroeconomic backdrop, corporate and private equity buyers are sitting on large cash piles waiting to be deployed. Deal financing is also abundant, with debt and capital markets highly liquid and very much open for business.

The market is not without its challenges. Antitrust and cross-border merger controls are on the radar for dealmakers and assets prices are full, despite lingering COVID-19 risk. Inflationary pressures also seem to be emerging, which could impact interest rates over the longer term.

Overall, however, European M&A investors are in a much stronger position than a year ago. As dealmakers and companies move into the second half of 2021 and start planning for 2022, here are some of the key themes expected to inform dealmaking in the coming months:

High prices but high quality
Deal multiples are reaching record highs in 2021 and dealmakers are having to meet full valuations to secure assets. Bidders, however, are only paying high prices for assets of the highest quality that meet their deal criteria. Dealmakers are honing very specialised deal rationales so that they can run hard at deal targets they really want. Vendors will narrow the field when selling assets and provide handpicked buyers with more time to get comfortable with deal targets rather than running aggressive, truncated auction processes with multiple, undifferentiated buyers.

ESG to the fore
During the last 12 months ESG has emerged as a key priority in deal selection and due diligence. Institutional investors and consumers have become more attuned to how capital is invested and want to see evidence that deals are incorporating a wider view on sustainability and financial performance. Companies with robust ESG credentials will become increasingly sought after by buyers, and ESG will become a bigger theme in due diligence and prove an increasingly important factor in establishing valuations.

Deal activity in a wider range of sectors
Through the pandemic period dealmakers coalesced around a select group of high-quality companies in a narrow range of sectors, such as healthcare and technology, where there was earnings visibility and protection against downside risk.

Technology and healthcare will remain popular sectors, but as economies reopen and restrictions ease, opportunities to buy attractively priced companies in COVID-impacted industries that are back on growth trajectories are emerging. More activity in sectors such as leisure, hospitality, travel and consumer is now anticipated.

About CMS

CMS is a full service top global law firm with more than 4,800 lawyers in 77 offices providing clients with specialist business focused advice. With more than 1,300 corporate lawyers, CMS advises on all aspects of M&A, corporate finance and private equity transactions and is regularly ranked among the top M&A advisers in Europe and beyond. CMS features among the league table leaders both for Europe as a whole and for many of the individual European countries. We are service-driven and relationship focused, priding ourselves on our responsiveness and "can do" attitude.

We strive to develop long-term relationships with our clients, giving prompt, straightforward and commercial legal advice. We draw on renowned industry expertise in a number of sectors including Financial Institutions and Services, Energy and Climate Change, Technology, Media and Telecommunications (TMT), Life Sciences & Healthcare, Consumer Products, Construction and Development, Hotels, Leisure and Sport, Infrastructure and Project Finance.

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Our latest CMS Corporate/ M&A headline deals

Rohlik Group
CMS acted for the lead investor, Partech (a growth fund from France) in its investment in start-up online grocer Rohlik, which is the leading online grocer in the Czech Republic.

Turn/River Capital
A pan-European CMS team has advised US PE house, Turn/River Capital, on the USD 314m acquisition of the international tech automation solutions group, Redwood. The acquisition is a transformational deal for Turn/River, representing its largest acquisition to date, and continuing its pursuit of the SaaS marketplace.

Macquarie Capital
CMS has advised investment fund Macquarie Capital as main investor, together with Daiwa Energy & Infrastructure and Aberdeen Standard Investments, on the acquisition of a majority stake in the fibre optic network in rural areas owned by MásMóvil, which will cover more than 1.1 million Spanish households.

Worldline
CMS has advised longstanding client, Worldline, a leading European player in payment services, on its divestment of business assets in Austria, to buyer, Global Payments s.r.o. (GPSRO), and in Belgium and Luxembourg to BNP Paribas Fortis (BNPPF).

Equinor
CMS has advised Norwegian energy company Equinor (formerly Statoil) on the purchase of Wento, a Polish company which focuses on the development of photovoltaic (PV) and wind projects, from private equity fund Enterprise Investors.

Big Yellow Group
CMS advised Big Yellow on its approximately GBP 100m fundraising by way of a placing of new ordinary shares with existing and new institutional investors and on the subsequent acquisition of Armadillo.

InPost
CMS advised InPost on its IPO on the Euronext Amsterdam Stock Exchange. CMS advised InPost on acquisition of Mondial Relay, a leading parcel courier in France for EUR 513m.

Volkswagen Group
CMS advised Bugatti, a part of VW Group on its combination with Croatian Rimac Automobili, to create a new auto company – Bugatti Rimac.

Grupa Azoty Polyolefins S.A.
Advised on the Polimery Police investment project–the largest chemical investment in Poland and CEE with the estimated budget of USD 1.8bn.

Discovery
Advised on the taking over the TV channel TELE 5 and a long term content agreement with LEONINE.

NH Hotels
Advised in relation to acquisition of operations of a portfolio of eight hotels in Italy, Czech Republic, Hungary and France, in the context of the acquisition of the above portfolio by Covivio Hotels, as lead purchaser and property investor.

RWE AG
CMS advised RWE, one of the world's leading renewable energy companies, on an agreement to sell a 49% stake in the Humber Gateway offshore wind farm to Greencoat, a UK-based investment company focusing on renewables projects, for a total cash consideration of GBP 648m.

News Corp UK & Ireland Ltd
CMS advised NewsCorp UK on the sale of Unruly Media, a global programmatic advertising group to AIM quoted New York-based adtech group Tremor International.

Allianz
Advised on EUR 214m acquisition to expand Munich office portfolio and on EUR 500 mln joint venture with developer VGP.

Equinor
Advised on its agreement with BP to sell 50% of its interests in the Empire Wind and Beacon Wind assets on the US east coast for a total consideration of USD 1.1bn.

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An Acuris company

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