The Newfound Attractiveness of European M&A

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In 2014, Europe registered its highest levels of M&A deal activity since the financial crisis. Compared to 2013, overall European M&A activity climbed 40.5 percent to $901.4 billion (the highest value since 2008).[1] Inbound M&A, at $320.6 billion, reached a record high by both deal value and deal count since 2001, mostly driven by U.S.-based acquirers (which represented 60.7 percent of the total) and Asian acquirers (with Chinese buyers alone representing 76.2 percent of all of emerging Asia's investment into Europe). Underlining the strength of European companies, outbound M&A surged to its highest level since 2007 (at $365.8 billion, it shot up 190 percent from the previous year), most of it directed toward the U.S. (71 percent of the total, the highest value since 2001). Intra-European cross-border M&A was also extremely strong at $264.5 billion (*i.e.*, more than double the 2013 figure of $131.3 billion). On average, M&A transactions were larger (deal volume was up only 4.8 percent year-on-year) and 10 deals exceeded the $10 billion mark compared to only six in 2013.

The general trend was observed in most of Europe's main markets, including France, the most active European country for M&A ($204.7 billion, the highest value since 2007 and up 327.5 percent over 2013), the United Kingdom ($154.5 billion, up 28.7 percent) and Germany ($73.9 billion). These three countries together represented 45 percent of total European activity in 2014.

Macroeconomic Trends

On a macroeconomic level, the gradual (albeit selective) recovery of European economies and financial markets, after five years of financial, credit, sovereign-debt and monetary crises, spurred increased confidence in the continent's prospects. Stronger M&A activity resumed in Europe under the combined effect of improved financing conditions, high levels of cash reserves on corporate balance sheets and, in private equity and investment funds, rising levels of investment returns, and strong equity market performance that allowed listed corporate buyers to pay all or part of their public takeovers in stock. In addition, the volume of capital available to U.S. corporations, one of the most significant groups of investors in Europe, increased substantially, and their willingness to deploy such capital grew in large part as a result of an improved U.S. economy.

The study of some of the major announced or completed transactions, and the motives underlying them, reveals a mix of opportunistic and deeper-seated reasons for the renewed vitality of European M&A in 2014.

Key Differentiating Factors Driving European M&A

High-Quality Assets. During the financial crisis, European companies were forced to reorganize their structures, clean up their balance sheets, streamline their activities and focus on their core businesses. As a result, many companies emerged with better asset quality, which made them more attractive to potential buyers, or with increased cash and/or share performance, which facilitated their acquisition strategy. Buyers were prepared to pay the price for such assets: At $365.4 million, the average price paid for European targets was the

highest in seven years. Combined with other factors, this helps explain the robust health of European M&As in 2014, as well as a wave of industry consolidations. For example, the pharmaceutical, medical and biotech industry reached an aggregate deal value of $114.9 billion in 2014, including (1) inbound transactions, such as Eli Lilly's purchase of Novartis' animal health business through an asset swap worth $5.4 billion, (2) outbound transactions, such as Merck's $17 billion acquisition of Sigma-Aldrich Corporation, and (3) intra-European transactions, such as Novartis' announced acquisition of GlaxoSmithKline's vaccines and oncology drug developing division for $14.5 billion.

Fiscal Attractiveness and General Political Stability. One of the main drivers of cross-border M&A activity into Europe in 2014 was the increase of so-called "tax inversions," *i.e.*, in a European context, a combination transaction between a U.S. and a non-U.S. company resulting in the surviving company relocating its corporate headquarters in a European jurisdiction (where it generally enjoys a lower effective tax rate). Twelve inversion transactions were announced globally in the first nine months of 2014 alone, eight of which involved a European target, for a total value of $309 billion (over four times the value for the same period of 2013), including Medtronics' $45.9 billion acquisition of Ireland-based Covidien. Other advantages of most European jurisdictions include their general political stability, the existence of an independent judicial system and general openness to foreign investment. Even the newly introduced French regime on foreign investments, which drew much criticism in connection with General Electric's announced $12.3 billion purchase of Alstom's Thermal & Renewable Power and Grid assets, remains relatively mild compared to the protectionist measures adopted in numerous other markets.

Access to Talent and Technology. Beyond the classic motives underlying strategic growth transactions, such as the desire to expand into new markets, increase revenue, increase market share and/or achieve economies of scale (*e.g.*, the planned merger of French Lafarge with former Swiss rival Holcim worth $39.6 billion, creating a European behemoth in the cement industry), European M&A in 2014 also has been characterized by a search for talent and new technologies. This has been particularly evident in the technology, media and telecommunications industry (TMT), which underwent important global consolidation and took the top spot in Europe with $120.2 billion of M&A deal value in 2014. Relevant examples include Luxembourg-based Altice's $23 billion acquisition of SFR (and $9.2 billion proposed acquisition of Portugal Telecom assets) and Vodafone's $10.1 billion acquisition of Kabel Deutschland, all of which aim to combine a mobile company with a cable or fiber assets operator, allowing the combined entity to compete with operators that are taking a competitive edge by offering quadruple-play (*i.e.*, fixed phone, wireless phone, TV and Internet) solutions to their clients.

European M&A in 2015

Will economic operators be able to build on this momentum to continue the trend into 2015? Inversion transactions from the United States may slow down as a result of recent measures adopted by the U.S. government. Economic recovery remains fragile in a number of European countries, and national governments may continue to protect their sensitive (and, in

certain cases, less sensitive) industries from foreign buyers. Geopolitical tensions in certain regions may take their toll on economic and M&A activity if they continue or worsen. This being said, the overall attractiveness of European companies should remain strong in 2015. Global factors, such as the strength and search for external growth of U.S. and Asian players, a prolonged weakness of the euro, or the recent pressure on oil prices, will provide M&A opportunities. Industry consolidations, fueled in part by regulatory efforts to increase convergence, are likely to continue, in particular in the TMT, pharmaceutical, medical and biotech, and industrials sectors. Unsolicited transactions may again become more frequent, and certain shelved transactions (including pan-European relocations) may resume if political conditions evolve favorably. All in all, 2015 is shaping up to be a promising year for European M&A.

[1] Sources regarding statistical deal activity presented in this article are mostly based on data published by mergermarket (*M&A Monthly Insider,* December 2014; and *Global and Regional M&A*: 2014) and Dealogic (Global M&A Review, Full Year 2014) as well as a variety of major news publications. Such sources may adopt different criteria or assumptions to collect or present their data, and some of them may not derive the underlying data from definitive year-end reports.