

Mergers and Acquisitions: 2016 Update

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Global mergers and acquisitions volume in 2016 declined from the record levels set in 2015, but activity was nonetheless strong by historical standards. Value of global deals was approximately \$3.7 trillion, an annual total behind only 2015 and 2007, according to Thomson Reuters. The value of U.S. transactions was approximately \$1.7 trillion. Despite unexpected political and economic developments, M&A activity in 2016 reflected many of the trends of 2015.

Market Drivers

Mergers and acquisitions volume in 2016 again was dominated by strategic activity driven by fundamental forces — the need to grow revenues and earnings in a low-growth environment and to be competitively positioned in the global marketplace. Given these conditions, M&A has provided corporations a means to grow revenues faster than would be possible organically, and synergies resulting from transactions have provided opportunities to expand margins and drive more rapid earnings growth. Deal activity also has allowed strategic players to enhance geographic or portfolio footprints, or to position themselves as industry disruptors through the acquisition of new technologies.

These fundamental imperatives driving corporations' rationale for pursuing mergers and acquisitions were coupled with a continued benign environment conducive to M&A, particularly in the United States. Favorable factors included stable equity markets, strong corporate balance sheets and the availability of acquisition financing at historically attractive rates. Importantly, C-suite and boardroom confidence about long-term opportunities continued, supporting deal initiatives. Additionally, shareholder support for deals in 2015, while not universal, in large part continued in 2016.

One noteworthy development was an increase in inbound U.S. M&A activity to record levels. The United States consistently has been an attractive destination for M&A due to factors including large market size, a growing (albeit slow-growth) economy, relatively stable capital markets and the rule of law. With actual or potential economic dislocations and political uncertainties threatening many of the world's markets, it is no surprise that the U.S. continued to attract foreign investment in 2016. Inbound deal volume surpassed \$500 billion, with significant transactional activity coming from Canada, China and the United Kingdom. Notably, Chinese outbound activity was at record levels — \$221 billion, according to Thomson Reuters. While robust asset prices, a strong dollar, the potential impact of changes in Chinese policies affecting outbound transactions from China and concerns regarding the potential for growing economic nationalism may act as headwinds tempering this trend, significant cross-border deal flows into the U.S. appear likely to continue. (See "[Regional Focus: Asia](#).")

Unsolicited Activity

Hostile and unsolicited mergers and acquisitions continued to play a small but important role in the M&A market. In 2016, unsolicited transactions accounted for nearly \$400 billion in global deal value.

The varied fates of unsolicited proposals in 2016 again demonstrated the uncertainty of outcomes in hostile activity. As in prior years, while hostile offerors in some situations successfully consummated transactions, success was by no means universal. In other cases, targets of unsolicited proposals ultimately were sold, but to a party other than the original offeror. As in 2015, there also were several examples of target companies successfully defending against unsolicited proposals without an alternative transaction.

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One notable example was the withdrawal by Canadian Pacific Railway of its unsolicited offer for Norfolk Southern Corp. after Norfolk Southern determined that the value generated under its own strategic plan was superior to that in Canadian Pacific's offer and that the proposed transaction was highly unlikely to receive regulatory approval.

For a corporation driven by the fundamental imperatives discussed above, a hostile offer is sometimes the only path to pursue a strategically critical transaction. While commencing a hostile public offer is generally not a would-be acquirer's preference given the cost and uncertainty of the outcome, the elimination of most target takeover defenses as a result of ongoing campaigns to implement governance "best practices" and the evolution of many companies' shareholder bases make unsolicited activity an alternative in appropriate situations.

Abandoned Transactions

A number of large proposed transactions were withdrawn in 2016 after announcement, with estimates indicating that these abandoned deals represented over \$800 billion globally, almost one-fifth the dollar value of transactions announced during that period of time. This statistic reflects transactions abandoned for a number of reasons, and at various stages, such as announced unsolicited offers that never progressed and deals that were signed but ultimately terminated as a result of shareholder dissatisfaction, emergence of a topping bid or regulatory issues.

Several large pharmaceuticals transactions were terminated following administration changes to tax regulations to halt so-called "inversion" transactions in which a U.S. company would be acquired by a smaller foreign company, effectively moving the home tax jurisdiction of the publicly traded parent outside the United States. A continuation of the trend of aggressive antitrust enforcement at the Department of Justice and the Federal Trade Commission — reflecting increased willingness on the part of the government to litigate rather than accept proposed settlements in transactions that raise substantive antitrust issues — led to several large transactions being abandoned. It is unclear how regulatory policy may change under a new administration in the U.S. and how that will impact deals this year. (See "[Antitrust Enforcement in the Trump Administration](#).")

Impact of Activism on M&A Activity

Despite some signs that hedge fund activism may have hit its high-water mark, including commentary from passive investors

and other long-term institutional holders seeking to encourage long-term decision-making by corporate management, shareholder activists have continued to have a meaningful impact in the M&A market. (See "[Directors Must Navigate Challenges of Shareholder-Centric Paradigm](#).")

In an environment supportive of mergers and acquisitions activity, and with both strategic and private equity buyers seeking targets, "sell the company" or "sell a business" platforms can be attractive to activist investors and other active managers looking for short-term returns. Activist campaigns have preceded sales at a number of companies this year. In other cases, activists have sought to block or renegotiate transactions. Appraisal litigation is another area where hedge funds have sought to use M&A transactions to harvest additional returns. (See "[Key Developments in Delaware Corporation Law in 2016](#).")

Activism is not going away, and market participants accordingly need to continue to factor in the potential for activist intervention and how best to respond.

Potential Impact of Administration Change on US M&A Activity

Equity markets to date have reacted favorably to the outcome of the presidential election and the resultant prospect of changes to fiscal and regulatory policies. The makeup of the Trump administration continues to take shape, and perspectives on likely administration policies continue to develop, making speculation regarding the new administration's impact on M&A activity just that — speculation. In the shorter term, uncertainty as to policy could impact the pace of deal activity. However, signals as to potential policy direction indicate areas of likely change that could result in meaningful, and generally favorable, impact on the M&A environment, such as adoption of a more business-friendly approach to regulation, increased competitiveness of the [U.S. corporate tax regime](#) and adoption of incentives to repatriate corporate cash held offshore. The impact of possible changes to fiscal policy, [trade policy](#) and [national security review](#) are more difficult to predict and could lead to positive or negative effects on the deal environment.

Given the significance of some potential changes and the active dialogue of the administration with the corporate community, boards and executives considering extraordinary transactions should carefully consider the possible impact of administration policy.