Trends & Developments

Contributed by Niederer Kraft & Frey AG

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Ulysses von Salis Dr von Salis specialises in complex domestic and cross-border M&A, private equity transactions and financings. His experience includes transactions in various industries and extends to private equity investments (including buyouts and venture capital investments), acquisitions, divestitures, spin-offs, corporate structurings and reorganisations, and joint ventures. He has extensive experience in advising funds and private investors on investments, founders and managers on their participations, and shareholders of privately held companies as well as companies on financings (equity, mezzanine, debt etc). Dr von Salis regularly acts for banks, issuers and borrowers on loan facilities, convertibles and other structured finance transactions. Further areas of expertise are corporate governance and law, contract law and securities law. Professional memberships: Swiss Bar Association, Zürich Bar Association and International Bar Association (IBA).

The Swiss market

Despite its relatively small size, Switzerland is home to several large and well-established international corporations spanning a diverse range of industries, from major banks like Credit Suisse and UBS, large insurance corporations such as Swiss Re and Zurich Insurance, and food and pharmaceutical firms such as Nestlé, Novartis and Roche to commodities producers and marketers like Glencore/Xstrata. These industries combined contribute considerably to Switzerland's economy and GDP.

Amid continuing economic uncertainty following the global financial crisis and the European sovereign debt crisis, the recovery of the Swiss economy continues and Switzerland seems to be emerging less bruised than many other developed economies. In the course of 2012, legal work in Switzerland continued to partly bounce back to a more 'courant normal' (normal state), including an increase in volume of M&A transactions.

According to a survey conducted by Ernst & Young for the year 2012, 606 M&A transactions with an approximate deal volume of CHF111 billion were reported, representing a decrease of 16% in terms of number of deals, but an increase of about 116% in deal volume compared to 2011. However, the significant rise in deal volume is primarily attributable to the Glencore/Xstrata merger announced in 2012. Another sizeable transaction was the strategic partnership between Swiss domiciled Alliance Boots GmbH and US-based Walgreens, involving the sale of a 45% stake held by KKR in Alliance Boots to Walgreens for approximately USD6.9 billion with an option to acquire the remaining 55% for approximately USD9.5 billion at a later stage.

Key industries

In terms of industries, according to a recent KPMG study, approximately 20% of Swiss M&A transactions in 2012 related to industrial markets, followed by TMT (14%), commodities (12%) and consumer markets (12%). Interestingly, the long-expected consolidation in the financial services industry has yet to gain momentum. The number of 2012 deals in the financial services declined by 35% with a corresponding decline of 15% in deal volume compared to 2011, despite the USD880 million acquisition of Bank of America Merrill Lynch's non-US private banking business by Julius Bär. Interestingly, energy only accounted for 3% of the 2012 M&A deals, which differs from certain other European jurisdictions where energy has been an important sector for M&A. However, it is expected that as a result of the new 'Energy Strategy 2050' announced by the Swiss Government in 2012, Swiss energy companies will need to adapt their business plans, which may lead to further divestments abroad and a re-focusing on the Swiss and selected foreign markets.

Exchange rate intervention

The adverse effects of the strong Swiss franc on inbound investments have partly been mitigated by the Swiss National Bank's exchange rate intervention. De facto this has led to a pegging of the Swiss franc to the euro, which has arguably facilitated acquisitions of Swiss assets by foreign buyers. In addition, the strong yen has continued to fuel interest from Japanese investors. Notable transactions involving Japanese buyers in 2012 include the public takeover of SIX-listed Uster Technologies by Toyota, the purchase of SIX-listed OC Oerlikon's solar business by Tokyo Electron, and the sale of Pago Group to Fuji Seal. These transactions followed several multibillion Swiss franc deals in 2011, such as the acquisition of Swiss-domiciled Nycomed by Takeda and of Landis+Gyr by Toshiba. However, the impact of the yen's recent drop on M&A activity remains to be seen.

US investment

Despite the relatively weak US dollar, US companies are very active buyers. This can be explained, in part, by the fact that many US companies with an international presence hold large (foreign) cash reserves that cannot be repatriated in a tax-efficient manner. However, this is not the only reason, as evidenced by a series of very notable transactions in 2012, such as the aforementioned USD6.9 billion acquisition of a 45% stake in Alliance Boots GmbH by US national pharmaceutical chain Walgreens, the multibillion-franc acquisition from Generica of Swiss pharmaceutical company Actavis by US Watson Pharmaceuticals, and the acquisition of SIX-listed Clariant's Emulsion, Paper Specialities and Textile Chemicals businesses by SK Capital Partners. By contrast, there continue to be very few Chinese buyers, but the most prominent transaction was the acquisition of OC Oerlikon's natural fibres and textile components business by Jinsheng Group at an enterprise value of CHF650 million announced in December 2012.

Swiss companies

On the other hand, many Swiss companies hold large cash amounts, but they continue to be prudent, with regard to both domestic and cross-border acquisitions. Due to the continuing economic uncertainty, they take more time for their due diligence review of potential targets. They have also become more selective and tend to defer execution to the end of reporting periods in order to base the deal on full or half-year accounts. Somewhat linked to this and similar to other European markets, we note an increasing trend in the Swiss M&A market in the use of the 'locked box' approach to determine the price for a target business in the context of a private M&A transaction instead of the completion accounts (i.e. net asset value, net cash/debt, and/or working capital based) approach.

Regulatory issues

The long-predicted consolidation in the banking sector still lacks momentum. However, it is fair to assume that the additional capital requirements under Basel III, as well as the ever-increasing regulatory pressure and costs of compliance, will eventually be a catalyst for more M&A activity in this sector. While small financial institutions may be left with no other option than liquidation, larger institutions will again be looking at acquisitions (or mergers) in their core businesses while disposing of non-strategic assets. Recent examples which illustrate this trend include the USD880 million acquisition of the non-US private banking business of Bank of America Merrill Lynch by SIX-listed Julius Bär, the initial public offering and subsequent full disposal of EFG Financial Products by Swiss-based international private banking group EFG International in 2012, and the sale of Credit Suisse's ETF business to BlackRock in January 2013.

Sale of non-core assets

More generally, the sale of non-core assets has been an important source for M&A work in all industries. Recent examples in the non-financial services industries are the above-mentioned disposals of OC Oerlikon's solar and natural fibres and textile components businesses, and the sale of Clariant's Emulsion, Paper Specialities and Textile Chemicals businesses.

Transfer of domicile

Switzerland continues to be a preferred jurisdiction for the re-domiciliation of large international companies. The most recent example is the transfer of domicile of Coca-Cola Hellenic, the largest listed company in Greece, to Switzerland.

Public M&A

Public M&A continues to be very slow. In 2012, less than a handful of public tender offers were announced. Likewise, despite a very positive development of the Swiss stock market, the IPO market was closed for almost all of 2012. The only IPOs on the SIX Swiss Exchange in 2012 were DKSH in spring 2012 and EFG Financial Products in October 2012.

Private equity

Private equity continues to struggle with the challenges of getting debt financing for new acquisitions on the one hand, and working through the exit backlog on the other hand. PE-backed sales to strategic buyers, normally the mainstay of buyout exits, remained relatively slow, IPOs could not get out of the gate and sponsor-to-sponsor deals almost stalled. While there are some signs of improvement, it is still difficult to see how exit opportunities will improve until the clouds of uncertainty lift. Despite this difficult environment, there have been some important transactions in 2012 on both the sell- and buy-side, including the above-mentioned sales of KKR's 45% stake in Alliance Boots, of Actavis by Novator Partners LLP to Watson Pharmaceuticals, and of Clariant's Emulsion, Paper Specialities and Textile Chemicals businesses to SK Capital Partners. Another noteworthy transaction was the CHF2 billion acquisition of Orange Communications (Switzerland) by Apax completed in spring 2012, which was financed by bank loans and high-yield notes.

Real estate M&A

2012 has been a very active year for real estate M&A, culminating with the CHF1 billion sale of Credit Suisse's Uetlihof building in Zurich to Norges Bank Investment Management. At the same time, Swiss Prime Site, Switzerland's largest listed real estate company, successfully completed a rights offering providing it with further cash for new acquisitions.

Conclusion

On balance, the Swiss M&A market remains challenging. However, there are positive signs for growth as the gap between buyers and sellers appears to be narrowing. This could provide further momentum and, in turn, increased activity in the Swiss M&A sphere in the future.