ALLEN & OVERY

Insights, **Q1 2016**

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Data provided by

Executive summary: Investor exuberance cools

The investor exuberance that drove M&A deals to record levels last year has cooled in the first quarter in the face of some significant economic and political worries. Falling oil prices, slowing growth in China, worries about the health of the financial sector and the possibility of a Brexit are all doing their part to slow down M&A activity, but with all the fundamentals that drove activity last year still present, we may see that the nervousness in the market is short-lived.

Q1 HIGHLIGHTS INCLUDE:

A SLOWER START TO 2016

Worldwide M&A has been hurt in the opening months of 2016 by falling oil prices, slowing growth in China, worries about the health of the financial sector and the possibility of a destabilising Brexit decision in the UK's forthcoming referendum. Deal volumes and values are considerably lower than the same period last year.

CONFIDENCE DIPS

Boardrooms have lost some of the confidence they had last year, tending to either pause deals while the uncertainty lasts or extending execution time. If confidence returns, there is a good pipeline of deals still to be done.

CROSS-BORDER ACTIVITY CONTINUES

Cross-border deals remain a strong feature of the market. They have accounted for just over a quarter of total deals so far this year.

CHINA OUTBOUND DEALS ACCELERATE

Chinese companies – both state-owned and private – are investing in overseas markets at an accelerating rate, with the active encouragement of the Chinese government. We are seeing both highly strategic and more opportunistic transactions, with Europe and the U.S. remaining prime target markets.

EQUITY AND DEBT MARKET VOLATILITY WORRIES U.S. INVESTORS

While transaction activity remains strong in the U.S., the recent turbulence in the equity and debt markets is a growing concern for investors. While significant deals are still being done, there is also a sense that M&A may have passed, or be near, its peak.

MEGA-DEALS GIVE WAY TO MORE MID-MARKET ACTIVITY

While Q1 saw some massive transactions announced – not least ChemChina's takeover of Syngenta, and the Johnson Controls/TYCO and Shire/Baxalta inversion deals – we expect volumes of these to diminish, with the focus shifting to mid-size deals as businesses reshape portfolios and sell non-core assets.

PRIVATE EQUITY QUIETENS DOWN

After a good spike of activity in 2015 we expect activity by PE funds to be quieter in the first half of this year as macro-economic concerns and worries about debt financing take their toll. That said, funds still have plenty of firepower to use when the right assets come to market.

TECH DEALS CONTINUE STRONGLY

The TMT sector – one of the star performers of the last two years – continues to see a good level of activity, increasingly driven by tech deals, both within the sector and across industries.

LIFE SCIENCES DEALS RETURN TO A MORE COMFORTABLE PACE

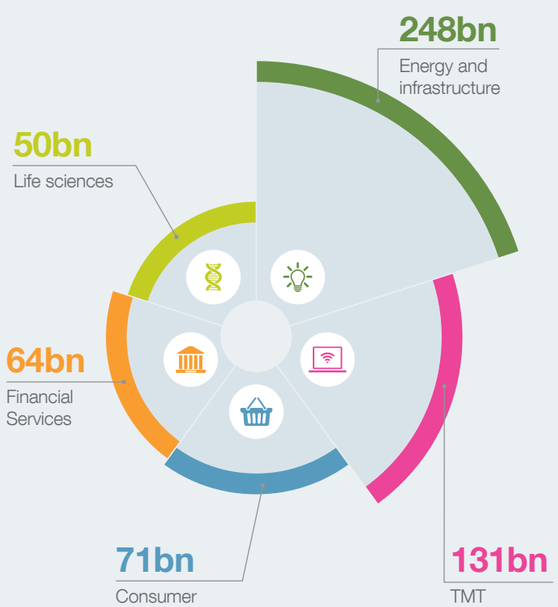
After two years of phenomenal growth and a host of massive deals, transactions in the life sciences sector have returned to a more comfortable pace and we believe the most significant M&A in the sector has been done. However, we still expect consolidation in the generics and biotech segments and a number of deals by companies reshaping their portfolios and disposing of non-core assets following a boom in transformational deals.

GOOD FUNDAMENTALS PERSIST

Despite a slower start to the year, many of the fundamentals that drove activity in 2015 are still in place – not least low interest rates, high levels of corporate cash and access to finance. If current economic worries prove to be short-lived, we could see transactions pick up quite strongly as the year progresses.

Global M&A in numbers Q1 2016

Top 5 sectors by value (USD)



Global deal volumes

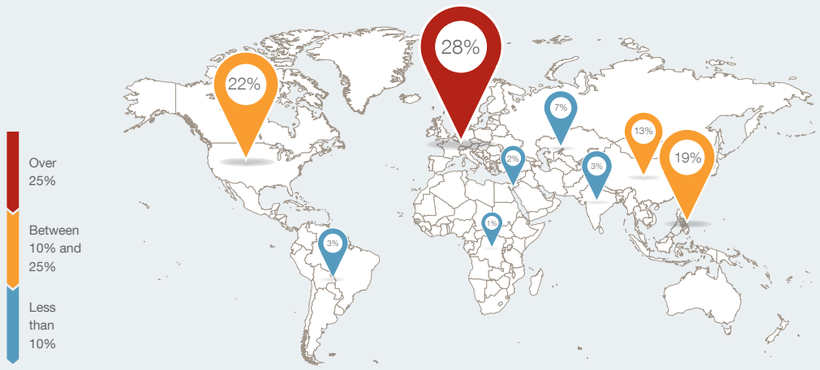
7708 Q1 2016 vs **9006** Q1 2015 — 14% DOWN

Global deal values

630bn Q1 2016 vs **685.5bn** Q1 2015 — 8% DOWN

Deal size (USD) as a percentage of total deal value for Q1 2016

Deal volumes by region



Region	% of deals by region
Western Europe	28%
U.S.	22%
Asia Pacific	19%
Greater China	13%
CEE and CIS	7%
India	3%
Latin America	3%
MENA	2%
Sub-Saharan Africa	1%
Other	2%

Data provided by THOMSON REUTERS

Note: These figures represent the total number of deals announced between 1 January 2016 and 23 March 2016.

In focus: Global trends in private M&A

Since 2012 we have been analysing the key trends in private M&A transactions that A&O has advised on across the world. In 2015, we saw more sellers embark on auction processes and buyers relaxed their position on deal terms, as confidence in the M&A market returned.

Over the last four years we have analysed the key trends in more than 600 private M&A deals that A&O has advised on, gaining an extraordinary insight into the tactics deployed in global and regional markets.

Our 2015 survey covers a period of extraordinary activity in M&A, as the market lifted itself out of the post-financial crisis slump to reach record-breaking levels. Although 2016 has opened on a noticeably more subdued note, we expect many of the recent trends in deal terms to continue, in spite of the political and economic concerns currently weighing on the minds of investors.

Auctions and competition for assets increasing

Auctions are now back in the picture. From 2012 to 2014 we saw auction activity shrink quite dramatically, with many sellers losing faith in the process thanks to the high number of failed auctions in the years immediately after the financial crisis.

But there was a change of tack in 2015. Auction activity increased for the first time since our private M&A surveys began and 39% of all our private deals in the year involved an auction, rather than a bilateral process.

Quality assets often attracted multiple bidders: the proportion of auctions that were highly competitive increased to 30%, having been 24% in 2014 and just 18% in 2013. The pace accelerated as well, with many competitive deals signed within 48 hours of the final bid deadline.

With valuations high, strategic bidders have often had the upper hand over PE funds in competitive processes. Some are prepared to pay a significant premium for assets that offer the chance to realise valuable synergies, and that's a battle PE funds are reluctant to join.

But PE houses have developed alternative strategies to increase their chances of securing assets. There's been a growth in "buy and build" deals, where funds acquire businesses that complement, and can achieve synergies with, companies already in their portfolios. Club deals – where a fund teams up with a strategic bidder – are also on the rise. Corporates won 65% of the auctions in our 2015 sample, with PE coming out on top in the rest.

The inexorable rise of antitrust regulation

In 2015 sellers were quick to reject unfinanced, or highly conditional, bids. But these days a completely unconditional M&A deal is rare, at least in the mid-market upwards.

78% of our deals were conditional, and 61% required antitrust or regulatory approval, up from 55% the previous year. This reflects the global trend towards tighter regulation, and the fact that more and more countries are now operating active merger control regimes.

Increasingly cross-border investors need to call on expert in-depth antitrust analysis to navigate this environment. Filings in multiple jurisdictions are often needed, so complex filing strategies have to be developed and implemented.

There's also far deeper co-operation and information sharing between agencies in different jurisdictions as they decide whether, and on what terms, to allow a deal on competition grounds.

Divestment is the remedy of choice for most antitrust authorities and they increasingly want the right to agree who will buy divested assets before clearing the deal. But they are also accepting more creative and innovative solutions, with behavioural commitments becoming more common.

As an indication of the emphasis that sellers put on deal certainty, 14% of the conditional deals in our 2015 sample included a reverse break fee, payable by the buyer if it failed to fund the transaction on closing, or if antitrust or regulatory approvals were not forthcoming.

Sellers gaining advantage

In the anxious years after the financial crisis, buyers certainly had the upper hand on transaction terms. But as confidence has returned, buyers have relaxed their position and sellers are starting to gain ground again.

One obvious illustration of this shifting trend is the rise and then decline of "material adverse change" conditions.

These have always been, and still are, standard practice in U.S. deals. But they were relatively rare in most other regions before the crisis, only starting to be deployed at a time when buyers were most nervous about the economic environment and dealmaking generally.

Since 2012 this trend has gone steadily into reverse as investor confidence has increased and in 2015 we saw a further decline in the use of such conditions in key markets, including the UK, Western Europe, MENA and parts of the Asia Pacific region.

In another indication that deal terms are moving in a seller-friendly direction, liability caps have fallen quite sharply in the four years we have been surveying the market. The average cap on sellers' liability for warranty claims was 44% of deal value in 2012, and this had fallen to just 34% by 2015.

Caps in U.S. deals were by far the lowest in our sample, averaging just 10% of deal value in 2015 and it's possible that the trend toward much lower caps in the U.S. is influencing other markets. If so, we can expect to see global averages continue to fall.

Warranty and indemnity insurance now part of the M&A toolkit

A few years ago, W&I insurance became an established feature of Australian private equity exits. Its popularity has since spread to other regions, and outside of the PE arena.

Some statistics illustrate this point: In 2013, W&I insurance was used in just 5% of the deals in our sample, and in 7% of all PE sales. In 2014, this figure doubled to 10% (and 17% of PE sales), and in 2015 it increased again to 16% (and 29% of PE sales). We expect this upward trend to continue – W&I insurance is being discussed as a solution in more and more deals.

In the PE space, the use of a 'buy-side' W&I policy is often mandated as part of the auction process, with the seller providing bidders with indicative terms that it has pre-negotiated with an insurer, or providing a stapled W&I package that the ultimate buyer is obliged to take out.

Outside of PE deals, a buy-side policy is sometimes taken out where there are multiple sellers, or the seller is distressed or closing down operations. But such policies are also used by bidders as an auction tactic, allowing them to make their bid more attractive by offering the seller a low liability cap, and topping up cover by way of insurance.

Coverage has increased and premiums have come down over recent years – the average premium in our 2015 sample was 1.6% of the sum insured.

Trends in a troubled market

With a range of macroeconomic and political worries now testing the nerves of investors – including concerns about the slowdown of growth in China, Brexit and the lower oil and commodities prices – there's a question over whether some of these trends in deal terms will go into reverse in the months ahead.

We doubt it.

Circumstances in the aftermath of the credit crunch were very different to today and gave investors real cause to look for a range of assurances and guarantees as they tried to complete deals.

Market conditions, despite those worries mentioned above, remain strong, with interest rates at historically low levels and access to cheap financing abundant. The private M&A market may not be motoring at the same pace as in 2015, but it still remains fundamentally robust.

If you would like a full briefing on our latest survey of global trends in private M&A, please get in touch with your usual A&O contact.

In focus: Global merger control enforcement

As M&A activity hit record levels in 2015 executives continued to gain the confidence to engage in more aggressive and strategic deals. And antitrust authorities have responded. Data we have collected and analysed from 16 jurisdictions, focusing on the U.S., EU and China, shows that antitrust intervention has had a clear and tangible impact on deals.

2015 saw antitrust activity impact M&A in a number of ways: deals were frustrated, subject to interference in the form of remedies, and transaction timetables were affected by lengthy investigations. We believe this trend of intervention is set to continue. However, we also found that antitrust authorities cleared the vast majority (95%) of deals at phase 1, without remedies, and, where they did have concerns, authorities were more willing to accept creative and innovative solutions. We outline below the key findings of our report Global trends in merger control enforcement, February 2016. You can access the full report at *www.allenovery.com/mergercontroltrends*

Deal breakers

Antitrust activity frustrated over EUR60bn of deals in 2015. This amounts to 20 transactions in all (seven formal prohibitions and 13 deals abandoned after the parties learned of the authority's antitrust concerns) and it represented around 2% of total global M&A in 2015.

The U.S. stood out in terms of the number and value of deals frustrated (99% of the total), primarily due to the amount of big ticket deals originating on U.S. soil, bolstered by the U.S. agencies' increased confidence in challenging transactions.

In the EU there were no formal prohibitions, but two transactions were abandoned after the European Commission (**Commission**) was unconvinced by remedies offered by the parties. And it is not just in the U.S. and the EU that antitrust can frustrate deals: transactions were also blocked or abandoned in China, Brazil, Turkey, Australia, Germany, the Netherlands and the UK.

Remedies imposed

Antitrust intervention in deal activity strikes further than just those cases that are frustrated by being blocked or abandoned. It can also interfere with the outcome of a transaction: authorities may be willing to clear a deal, but only on the basis of remedies designed to address the antitrust concerns. Often this interference is significant.

Antitrust authorities interfered with 92 deals by imposing remedies. In 38 of these cases remedies were agreed in phase 1 and the remaining 54 were subject to remedies following an in-depth investigation.

In the EU there were 20 remedies cases in 2015 and in the U.S. there were 25, both comparable to 2014 figures. In China the Ministry of Commerce (**MOFCOM**) only required remedies in two cases. In fact there have been only 26 conditional clearances in total since the Chinese merger rules came into force in 2008 – a clear contrast to the EU and U.S.

More generally we saw antitrust authorities increasingly co-operating on remedies, with some agencies unconditionally clearing deals on the back of undertakings agreed in other jurisdictions.

Not all in-depth reviews result in intervention, but they can be lengthy

The picture varies considerably from jurisdiction to jurisdiction. In the U.S. only 38% of in-depth reviews were cleared unconditionally in 2015. In the EU it was 13%. This is likely due to the fact that the Commission and U.S. agencies assess the largest deals in some of the most mature markets, resulting in a higher probability of antitrust issues. This is in contrast to the UK and Germany, where deals facing an in-depth review had the greatest chance (86% and 78%) of success. In China the picture is less clear, as not all data on in-depth investigations is published. But we believe the proportion of cases resulting in intervention in 2015 was lower than in the EU and U.S.

In-depth investigations can have a major impact on the deal timetable. In the majority of jurisdictions surveyed an in-depth review takes between five and eight months. And this is before adding on the often lengthy pre-notification discussions with an authority before the clock starts to tick. However in some jurisdictions in-depth cases took much longer than the average (one U.S. case in 2015 took around 18 months from notification). In China, MOFCOM has taken key steps to streamline the merger control process (see case study box for more details).

Whatever the length of the review, parties are likely to face considerable administrative burden. In complex EU cases we have seen the Commission request that parties submit tens of thousands of internal documents in the hope that these will inform its analysis. Similar practices are emerging in other jurisdictions.

Authorities are more open to creative and innovative solutions

Antitrust agencies traditionally favour structural remedies as they address their concerns in a clear-cut manner. But we have seen a shift away from this approach.

Last year 39% of phase 1 cases resulting in remedies involved behavioural commitments relating to future conduct, either as the whole remedy package or alongside a requirement to divest. For in-depth cases the figure was 37% (62% excluding the U.S.).

In the EU, four out of seven conditional decisions following an in-depth probe involved behavioural remedies. In China, MOFCOM remains one of the most prolific users of non-structural remedies. On the other hand the U.S. is the clear exception to the trend with structural divestments accounting for 92% of remedies in 2015.

Where structural remedies are required, upfront buyers are becoming more common. In 2015, 21 of the 23 divestment cases in the U.S. involved an upfront buyer. They were also used in the EU, UK and France.

Telecoms and life sciences were the hottest sectors for action

Telecoms and life sciences deals accounted for the highest ratio of antitrust intervention. This is when compared to the global volume of deals in these sectors in 2015.

In the jurisdictions surveyed, telecoms deals were most problematic, accounting for 10% of all transactions frustrated (compared to only 2% of global deals). Life sciences mergers attracted the most frequent antitrust interference by way of remedies, accounting for 21% of all deals interfered with (compared to 7% of global deals). The data reflect major industry consolidation in these sectors and a willingness to attempt deals which are challenging from an execution perspective due to antitrust concerns.

Looking forward

As M&A activity continues in 2016, we expect to see antitrust continuing to feature heavily in deal strategy, timetables and in shaping the outcome of problematic cases.

Case study

China: real progress in streamlining the merger process

- The introduction of a simplified procedure has been a real success. It captured 75% of cases in 2015, all of which were cleared unconditionally (78% in around 17 working days).
- In-depth cases not reviewed under the simplified procedure take longer, but not as long as parties perhaps fear: the two remedies cases in 2015 were decided in around six and eight months from the date of filing.
- Parties must factor in MOFCOM's "pre-acceptance" period before the filing is declared complete, but MOFCOM has taken steps to streamline this process by making internal changes to its case teams.

Regional insights

Despite some impressive transactions in Q1, all regions saw the volume and value of deals decline in the first three months even though there was growth in cross-border activity, led, in particular, by Chinese investors.

U.S.

Has the boom peaked?

The U.S. transactions market continued to perform strongly in the first quarter of the year with a range of sizeable transactions unveiled and investors remaining relatively sanguine about some significant macroeconomic thunderclouds looming on the horizon.

So far there is little evidence that boardrooms have lost any of the confidence that pushed the M&A market to record levels in 2015. But there is a sense that we may be entering the late stages of the extraordinary takeover boom we've witnessed in the last 18 months.

The U.S. is shielded from some of the political and economic worries that are currently besetting European investors. Brexit, for instance, gets little coverage in the U.S. press and is simply not a concern for investors at the moment. Even domestic politics – including the U.S. presidential race - is having little discernable impact on sentiment.

But two more immediate macroeconomic issues are beginning to bite.

The equity markets have been extremely volatile since the start of the year, even if the overall decline in share prices has not been as sharp as might have been expected. Some reasons for this turbulence include an ageing bull market, concerns about a China slowdown and the collapse of energy prices.

The debt markets too are challenging, particularly the high yield market. Overhung by a swathe of energy financing deals – many of them related to transactions executed in the early days of the shale boom – this segment of the market is struggling with worries that continuing low oil prices will leave a host of project backers unable to service their debts.

While corporate investors still enjoy good access to debt funding, it would not be surprising to see PE funds having more difficulty financing their deals. More generally, continued equity and debt market volatility could dampen investor confidence as the year progresses, not helped by the near certainty that U.S. interest rates will rise in the coming months.

For now, though, confidence remains high and there's still a trend towards the sort of highly strategic mega-deals we saw across sectors throughout last year.

In the pharmaceuticals sector Q1 saw Shire complete a USD32bn tie-up with Baxalta, creating a drugs giant specialising in rare diseases, while in the industrial sector Johnson have announced it will join forces with Tyco in a USD20bn reverse takeover deal.

There is a sense that we may be entering the late stages of the extraordinary takeover boom we've witnessed in the last 18 months.

Controversially, both of these transactions are so-called tax inversion deals which allow the combined business to re-domicile in Ireland and escape much higher rates of U.S. corporate tax. The transactions come despite moves by the U.S. tax authorities to make inversions more difficult and in the face of strong cross-party condemnation of such schemes in the past.

Another trend we've seen in Q1 is the growing number of often very significant deals being abandoned after lengthy discussions between parties. That might be a reflection of the complexity of the deals being contemplated, but it could also be a sign that the boom is reaching its late stages.

The proposed merger between the aerospace giants Honeywell and United Technologies Corporation, where Honeywell (to date unsuccessfully) has tried to persuade UTC to join forces in a USD90bn merger, shows how difficult it is to complete these giant deals.

There will doubtless be more such ambitious deals brought to the table in the months ahead. But if growing numbers fail to complete it will raise an awkward question: Has the current boom passed its peak?

WESTERN EUROPE

Deal flow unpredictable

While deal activity in Western Europe continues to hold up relatively strongly in the face of mounting global and regional pressures, it's clear the market is more finely balanced now than it has been for some time, making it hard to predict the outcome for 2016.

The sources of uncertainty are easy to identify and are varied, ranging from the political effects of the refugee crisis, mounting tensions in the Middle East, continued weakness in oil prices, worries about growth in China, pressure on European and U.S. debt markets, and the impact of Brexit on the EU and the global economy – should that be the result of the UK referendum in June.

Overall, however, these negative influences on investor sentiment have not yet had as strong an impact as might have been expected. Q1 continued to see a good stream of major strategic and cross-border deals in many markets, and while volumes were down, values held up well.

Q1 thus saw the announcement of several really significant deals, including the planned merger of the London Stock Exchange and the Deutsche Börse, a deal that could attract rival hostile offers and significant scrutiny from financial and antitrust regulators. Deutsche Bank also successfully offloaded its 20% stake in the Chinese Bank Hua Xia for some EUR3bn to the Chinese insurer PICC.

Japan's Asahi also completed the purchase of the Peroni, Grolsch and Meantime beer brands for EUR2.6bn, a deal spilling out of the giant AB InBev/SAB Miller brewing merger last year where the partners are still offering remedies to still win clearance from the competition authorities. Vodafone and Liberty Global also announced a EUR7.5bn mobile joint venture in the Netherlands, and the bid battle for control of Home Retail by Sainsbury's and Steinhoff, like the LSE battle, is evidence that investors are still prepared to fight contested bids, even in these uncertain times.

There has also been a notable upsurge in inbound Chinese investment as well, not least the biggest-ever acquisition by a Chinese company, namely ChemChina's USD43bn takeover of Syngenta. Chinese investors often search for distressed assets at good prices, but this is a highly strategic move tied closely to China's search for long-term ways to secure domestic food production.

There have been many more inbound investments from China, including Shanghai Electric's acquisition of a stake of up to 29.9% in Manz, Beijing Enterprises' EUR1.44bn purchase of EEW Energy-from-Waste from EQT and the EUR1bn acquisition of KraussMaffei by ChemChina.

A number of big ticket deals in Italy should be completed in the months ahead, not least HeidelbergCement's acquisition of a 45% stake in Italcementi for an estimated EUR1.67bn, whilst TMT will be a particular focus of activity. By contrast, medium-sized deals dominated Q1, with the industrial and manufacturing sector in the lead, followed by energy, financial institutions and pharmaceuticals.

But balanced against those regional positives, and a continuing strong pipeline of potential deals, there are some more worrying signs.

The Netherlands has seen some significant company failures this quarter, not least the bankruptcy of the department stores group V&D, which sparked further failures down the supply chain and Jumbo's acquisition of V&D's restaurants business La Place.

We believe the next few months will be volatile. But if this period of doubt can be overcome, there is no reason why 2016 should not also end up being a strong year.

Perhaps more worryingly there have been signs of growing nervousness around financing in some key markets, with potential investors delaying deals while they make sure that debt funding from increasingly reluctant banks will be made available, a particular issue for PE investors. That has not been helped by the state of U.S. debt markets, which have been in virtual shut down.

Should UK voters opt to leave the EU, the impact would probably be drawn out rather than immediate. So it could be that anxieties about Brexit having a big bang effect on, or soon after, 23 June are overblown and the current state of nervousness will be short-lived. Nevertheless, it's clear why some inbound investors might choose to delay investment decisions until there is more clarity.

We believe the next few months will be volatile. But if this period of doubt can be overcome, there is no reason why 2016 should not also end up being a strong year.

> "2015 was *not as dire* as many experts predicted and we do not expect the economic environment to worsen in the year ahead."

CEE AND CIS

Some signs of resilience

With U.S. and EU sanctions continuing to restrict access to international capital markets and foreign investment in Russia, business and deal activity in the CIS continues to be heavily depressed. The situation has been compounded by the devaluation of the rouble and the decline in commodities, particularly the continued weakness in the oil price.

For all that, 2015 was not as dire as many experts predicted and we do not expect the economic environment to worsen in the year ahead due to a number of factors which are likely to keep activity levels in Russia simmering away, not least the long-awaited launch of a privatisation programme.

This will see the sale of state holdings in three major companies, including Rosneft, fellow oil company, Bashneft, and the world's biggest diamond company, Alrosa. The long-awaited privatisation programme has been slow to get off the ground and traditionally preparing companies for IPO or strategic sale is a lengthy task. But these three companies already have a foot in the private sector so the processes should go ahead quickly.

A number of sectors are also undergoing a period of consolidation, including financial services, as banks seek to boost their capital bases, and – for obvious reasons – oil and gas. The same is true in agricultural products, where bigger players are looking to build scale to counteract a ban on foreign imports.

Chinese investors also remain active and often work in tandem with Russia's Direct Investment Fund and, as the search for alternative sources of investment continues, Middle Eastern capital is also finding its way into the region.

In Poland, there has been some investor nervousness surrounding new Law and Justice administration, amid fears that the new government, elected last October, would be less friendly to foreign investors and may intervene in past privatisations on strategic grounds. It is the first time politics has been a feature of the Polish investment scene for many years.

But so far there has been little effect on actual activity, which remained quite lively in the first quarter. There were, for example, five public tender offers in the first three months, and, with share prices depressed, company valuations are looking more attractive to potential buyers.

Market players also expect increased M&A activity in the energy sector, with EDF putting the majority of its Polish assets up for sale at the end of February.

There has been plenty of activity in private deals too including Bridgepoint's USD258.3m acquisition of the children's clothes and toy retailer, Smyk, from EM&F. Foreign banks and financial services companies, including GE, also continue to seek buyers for their Polish operations.

> We do not expect the economic environment to worsen in the year ahead due to a number of factors which are likely to keep activity levels in Russia simmering away.

Hungary's private sector continues to shrink as the government looks to exert control over more areas of the economy. But we continue to see plenty of activity in the real estate sector with some sizeable real estate deals taking place, such as TPG Real Estate's acquisition of TriGranit and Immofinanz's sale of its logistics portfolio to Blackstone. The sale of non-performing loan portfolios is also fuelling real estate transactions, with NPL buyers looking to sell the property on which the debts are secured. Technology is another lively sector, as IBM's purchase of UStream for a reported USD130m and GE's acquisition of Metem demonstrate.

Continued worries about the Eurozone and more immediate concerns about the refugee crisis do not, as yet, appear to be depressing investor sentiment in Central and South Eastern Europe, where several markets remain busy. Two sectors in particular are seeing good activity – TMT, for example in broadcasting and online services, and industrials. More widely a fairly robust pipeline of activity continues.

The Czech Republic continues to benefit from its recent strong economic growth and there are a number of deals in the pipeline in the retail, e-commerce, real estate, financial services and manufacturing sectors.

GE is getting ready to sell its Czech banking operations and has launched a dual track sale that is expected to attract both strategic and financial investors. Japanese, Chinese and Korean investors also remain active in the Czech market and are predominantly looking at manufacturing assets.

The Czech energy group EPH has also continued to acquire assets outside of the Czech Republic, following the announcement at the end of 2015 that it has agreed with Enel to buy up to 66% of Slovenské Elektrárne, the largest Slovak energy company, for EUR750m. EPH announced in January that it has now also acquired the Lynemouth power plant in the UK from Germany's RWE.

MIDDLE EAST AND NORTH AFRICA

Low oil prices take their toll

The beginning of 2016 has seen slightly subdued M&A activity in the region, with the volumes and values of deals down when compared with both the previous quarter and with the same period last year.

Factors such as China's slowdown and the stronger U.S. dollar all play a part, but with many of the region's economies dependent on oil revenues, the effects of continued low oil prices are also beginning to show.

This, coupled with lower liquidity and geopolitical tensions, means the confidence of some dealmakers in the MENA region has been shaken, and lending has slowed.

In the GCC, the construction, oil and gas and real estate sectors have been particularly badly hit by low oil prices. Concerned about the long-term impact, the rating agency Standard & Poor's has downgraded Bahrain, Saudi Arabia and Oman. Fellow rating agency Moody's has downgraded Bahrain and put the UAE, Saudi Arabia, Kuwait and Qatar (among others) on review for a possible downgrade.

> The confidence of some dealmakers in the MENA region has been shaken, and lending has slowed.

Years of high oil prices mean that cash reserves are still high in the region for the time being, but given elevated spending requirements, these could be depleted rapidly. Without access to the excess of reserves to which they are accustomed, governments could be forced to reassess spending plans, many of which are intended to diversify economies away from their dependence on oil.

Despite the challenging market conditions, there are still reasons to be positive. Deals are being done – albeit at a slightly more cautious pace – and the very same factors that have the effect of dampening the market could also spur inbound M&A opportunities in the region for the right investors. PE investors continue to show interest in the region while local investors are still looking to the wider region, particularly Africa, for investment openings.

The majority of deals seen in this quarter have been small scale, with increases in existing shareholdings and acquisitions of minority stakes taking place across the region. This continues the trend of consolidation and strategic acquisitions that has been seen in previous quarters.

In a deal which gives a welcome boost to Q1's M&A activity, a consortium of investors based in the region is seeking to acquire 69% of the Kuwait Food Co (Americana).

The consortium is headed by Mohammed Alabbar, the chairman of Emaar Properties (the company behind the world's tallest tower, the Burj Khalifa). The consortium has valued Americana – a food packaging and restaurant franchise business with the franchise rights to KFC, Pizza Hut and TGI Friday's in the MENA region and owned by the Kuwait-based Kharafi family – at USD4bn.

Following the acquisition, the consortium will begin a mandatory takeover offer under the rules of the Kuwait stock exchange to acquire the remaining share capital, with the intention of taking the company private. The sale process has been a long one for Americana. The Kharafi family first tested market interest in 2014, when KKR and CVC Partners made an offer.

Following the acquisition of a 49% stake in Network International (NI) by U.S. PE firms Warburg Pincus and General Atlantic, which closed in December, NI has now signed a bolt-on acquisition in agreeing to acquire Emerging Markets Payments (EMP) from the private equity investor Actis for USD340m.

The EMP Group serves more than 130 banks and 30,000 retailers and other merchants across 45 countries in Africa and the Middle East and offers the full range of card schemes. The acquisition is another deal illustrating the increasing interest in Africa from the region.

In March, Mumtalakat Holding Company, the investment arm of the Bahraini government, acquired a minority stake in Gulf Cryo, a Kuwait-based gas manufacturer. Gulf Cryo produces and supplies gases to a wide range of industries, overseeing a network of over 30 production and distribution sites operating in 12 countries, including the GCC countries, Jordan, Syria, Egypt, Iraq, Turkey and Austria.

The pipeline for IPOs is not as healthy as in recent years, but there is still appetite from regional companies interested in going to market when conditions improve.

SUB-SAHARAN AFRICA

The slowdown continues

The slowdown in deal activity across sub-Saharan Africa continued in the first quarter of 2016 with lacklustre commodity prices, concerns about China's growth and political turmoil in key economies all playing a part.

Those issues are particularly acute in South Africa. What little domestic activity we are seeing right now is focused on continuing discussions about the disposal of commodity assets as mining companies look to reduce their portfolios to counteract continuing rock bottom prices.

Inbound activity has declined markedly, with investors deterred by a series of long-running industrial issues, not least labour unrest and regular disruptions in energy supplies, which have been compounded by the devaluation of the rand and growing concerns about the direction of government policy. This was illustrated starkly in December with the appointment of two finance ministers within three days, a move that caused the currency and stock market to tumble.

> South African investors continue to rebalance their own international portfolios and to look for opportunities in overseas markets, not least Europe and the U.S.

Barclays also chose this quarter to announce plans to sell its African operations, although questions remain as to whether it will be able to find a suitable buyer for its extensive operations in the region. The move is unlikely to boost already fragile confidence even though it is much more about the bank's global strategy rather than the state of the market.

South African investors continue to rebalance their own international portfolios and to look for opportunities in overseas markets, not least in Europe and the U.S. That was a trend that started in 2015 where we saw, for instance, Brait acquire the New Look fashion retail chain in the UK and a majority stake in Virgin Active.

In Q1 the process continued with a range of deals including furniture retailer Steinhoff's tilt at the UK's Home Retail Group – a bid subsequently withdrawn, leaving the way clear for Sainsbury's to make a formal offer. Steinhoff has now disrupted another ongoing merger proposal, bidding GBP673m for the electronics retail group, Darty, which had been discussing a tie-up with Groupe Fnac.

South African property groups are also looking to diversify their holdings by buying overseas, with Eastern Europe in general, and Poland in particular, a target market. Following an earlier excursion by Rockcastle, the property fund Redefine has now agreed to take a 75% stake in a EUR1.2bn block of 18 retail and office properties in Poland.

We expect the domestic transactions market to slowly improve as the year goes on, helped by the government's ongoing effort to stimulate investment in vital infrastructure. That remains an important process, even if the latest budget faced criticism for doing too little to encourage growth.

Elsewhere in the region, the financial services sector remains a focus for consolidation, not least in electronic payments. Actis has agreed to sell its Emerging Markets Payments business to Network International, a PE-backed platform based in Dubai, for USD340m in a move that will create the biggest payment processor in the Middle East and Africa.

Tech companies also remain in the spotlight in the region, where Nigerian start-up, Africa Internet Group, has successfully raised EUR225m from a range of investors including Goldman Sachs and telecoms group MTN. Investors are now said to be valuing the business, described by some as Africa's answer to Amazon, at more than USD1bn.

Morocco continues to attract international investment, mostly from Europe and the UAE, and has become a hive of activity for local investors, with the retail, real estate, financial services, renewable energy, industrial and food production sectors all remaining active, all of which bodes well for a pick-up in transactions later in the year.

Increasingly it is also seen both as a hub for inbound manufacturers looking to export across the continent and as a base for European investors seeking to reduce their reliance on domestic markets by tapping into Africa's long-term growth prospects.

That's certainly the motive for Peugeot's decision to build a EUR557m, 90,000 vehicle a year car plant in the coastal city of Kenitra – its first direct investment in Africa and its first wholly owned facility on the continent. Peugeot, whose rival Renault is already established in Morocco, has talked openly about its need to reduce its dependence on the European market and its ambition to sell one million vehicles a year in Africa by 2025. In addition, large-scale investments such as Peugeot's attract component suppliers, bringing global players to the country.

INDIA

Slow progress

After signs of some improvement in India's M&A market in 2015, activity started this year on a much quieter note, with fewer big deals being completed than expected, volumes lower by 34% and values some 42% below where they were this time last year.

That, in part, reflects the continuing uncertainties investors have about the pace of economic reform, which many had expected to be much quicker after the election, 21 months ago, of Prime Minister Narendra Modi's majority government. Promised economic reforms are working their way through the system but more slowly than hoped, and we believe this is persuading some potential dealmakers to stay their hand.

February saw the unveiling of the government's annual Union Budget, and it is common to see investors wait for this to see what changes in tax, regulation and policy are in the pipeline for the next 12 months, before committing to investments. That certainly seems to have been the case this year.

> Promised economic reforms are working their way through the system but more slowly than hoped, and we believe this is persuading some potential dealmakers to stay their hand.

There have, though, been some positive developments that we think will help to stimulate activity as the year progresses.

The Government has acted, in the public interest, to increase the threshold levels above which deals are required to be referred to the Competition Commission of India for review and approval, a process that can often take several months. The thresholds, in terms of value of assets and turnover, have been raised. We, therefore, expect more transactions to proceed without competition scrutiny and this will help to boost activity in the market.

The government's Make in India campaign, a Modi innovation designed to attract manufacturers to invest in India, also appears to be making good progress, and several deals are reported to be either already sealed or close to signing.

Furthermore, while transaction activity was lower in Q1, there were some interesting inbound and domestic deals completed in the first three months.

E-commerce was once again a busy sector. Quikr, India's fast-growing online classified advertising portal, boosted its presence in real estate by acquiring the estate agency website, CommonFloor for USD200m.

Q1 also saw the leading online travel agencies in China and India forge an important alliance, with China's Ctrip investing USD180m in MakeMyTrip.com – continuing a growing trend of Chinese investment in India's increasingly dynamic e-commerce and IT sectors.

In infrastructure, Cube Highways – the Singapore-based infrastructure fund backed by ISquared Capital and the World Bank's International Finance Corporation - also acquired Western UP Toll.

With good levels of behind-the-scenes activity in a number of other sectors, including pharmaceuticals, healthcare and hospitality, we expect transaction levels to improve as the year unfolds. Progress is slow, however, and whether activity will reach the same level as 2015 remains open to question.

"The steep *devaluation* of the real against the dollar ought to suggest that this would be a prime time for foreign investors, particularly from the U.S., to pick up Brazilian assets at much lower prices."

LATIN AMERICA

Awaiting change

With so many Latin American economies dependent on demand for commodities it is hardly surprising that many economies are struggling to achieve growth and that transaction activity across the region remains heavily depressed.

Indeed, activity slumped in 2015 to its lowest level since 2009, the first year after the financial crisis, with the continuing decline in commodity prices, particularly for oil and key minerals like iron ore and copper, and weaker demand from a slower growing China the main factor behind that performance.

Investor confidence is also being hit by political turmoil in some key economies, not least Brazil where the so-called "Car Wash" corruption scandal – concerning alleged kick-back payments to politicians by the oil giant Petrobras – continues to embroil increasingly senior politicians, the latest being former president Luiz Inácio Lula da Silva.

Despite that difficult backdrop, the sharp decline in transactions is, in one sense, quite surprising. The steep devaluation of the real against the dollar ought to suggest that this would be a prime time for foreign investors, particularly from the U.S., to pick up Brazilian assets at much lower prices.

But worries about the political instability and the fact that buyer and seller price expectations remain significantly out of line with each other, appear, for now, to be holding back a wave of potential deals. That's as true for PE funds as it is for corporate investors.

Worries about the political instability and the fact that buyer and seller price expectations remain significantly out of line with each other, appear, for now, to be holding back a wave of potential deals.

Companies within the region are currently far more focused on restructuring and selling assets to reduce debts than on making acquisitions, either at home or abroad. Mining giant Vale, announcing record losses of USD12.1bn for 2015, made it clear it was considering selling both core and non-core assets to reduce debts which have mounted sharply in recent times. It made USD3.53bn of disposals last year, but we can expect more in the near future.

These issues are being replicated in many of Latin America's biggest economies, not least Colombia, Peru and - despite the arrival of a new, more investor-friendly government - even Argentina. Chile – despite feeling the blast of the commodities crash – has a more stable economy, and Mexico continues to benefit from recent economic reforms and its closeness to the U.S. economy.

Some sizeable deals continue to get done. Q1 saw the Spanish infrastructure group, Abertis Infraestructuras, cement its position as Chile's biggest toll-road operator when it bought the 50% it did not already own in Autopista Central, the Santiago motorway concession, from Alberta Investment Management for USD1bn. It already controls six other concessions in Chile.

The quarter also saw the eventual completion of the privatisation of Colombia's power generation group, Isagen, with the Canadian alternative investment fund, Brookfield, paying USD2bn for control of a group with major hydroelectric power resources. The sell-off launched in 2013 but had been delayed by lawsuits, with all other competing bidders gradually dropping out of the process.

Notwithstanding the state of the commodities markets, we continue to believe that activity will pick up strongly again in the coming months, although in Brazil an upturn is likely to depend on political reform – for example, President Dilma Rousseff faces a potential impeachment proceeding in Congress. That certainly seems to be the view of the markets – with both the stock market and the real surging in early March, after the press disclosed elements of the latest round of "Car Wash" leniency agreements.

Greater alignment between asset buyers and sellers over price will also be an important ingredient in re-igniting the deal market.

ASIA PACIFIC (INCLUDING GREATER CHINA)

Outbound adventure accelerates

In common with many other markets, overall deal activity in the Asia Pacific region slowed significantly in the first quarter of the year, and the value of domestic deals within China, a driving force in past quarters, was also markedly lower.

But the pace of outbound investment accelerated dramatically, led by Chinese companies looking for new growth markets.

With China's economy slowing, the government is urging and incentivising companies to boost the number of assets they hold overseas. With the value of the renminbi also falling, Chinese companies are anxious to secure assets denominated in other currencies. As a result, we are seeing an extraordinary growth in foreign deals across a wide variety of sectors.

The pace of outbound investment accelerated dramatically, led by Chinese companies looking for new growth markets.

The standout deal in Q1 was the USD43bn acquisition of the food technology giant Syngenta, by China National Chemical Corporation – commonly known as ChemChina. It is the biggest ever overseas deal by a Chinese company.

This forms part of a clear long-running, strategy by the Chinese government to boost food security. In pursuit of that goal, China has, in the past, acquired significant tracts of agricultural land in Africa and elsewhere, often through government-to-government agreements, and is attempting to acquire agricultural land in Australia and New Zealand, although opposition has been greater in these jurisdictions. Gaining access to Syngenta's biotechnology expertise in developing GM crops and seeds is a significant further plank in that strategy.

Many of the outbound deals are more opportunistic. Chinese investors are proving increasingly adept at finding well-priced, often distressed assets in numerous markets, notably Europe and the U.S.. If local investment activity begins to slow in these markets this could play into Chinese hands, bringing asset prices down and reducing bid competition. We expect China's outbound adventure to continue strongly.

Q1 saw Haier agree to buy GE's appliance unit for USD5.4bn, while in the high tech sector, air transport and logistics group HNA acquired California-based Ingram Micro for USD6bn, overcoming some resurgent U.S. worries over national security and high tech. In Europe, Shanghai Electric acquired a stake of up to 29.9% in Manz, Beijing Enterprises paid EUR1.44bn for EQT's Energy-from-Waste business, EEW, and ChemChina continued its acquisition spree by buying KraussMaffei for EUR1bn.

But the outbound story is not solely a Chinese one. Japanese and Korean companies continue to be significant players in investment across the Asia Pacific region, with financial services a particular focus. For example, the quarter saw Bank of Tokyo Mitsubishi UFJ's successful acquisition of a 20% stake in the fifth biggest bank in the Philippines, Security Bank, for USD847m.

Japanese businesses also continue to search further afield for great brands to help grow their global footprint and shore up their position at home. This was a clear

"The pace of outbound investment *accelerated* dramatically, led by Chinese companies looking for new growth markets."

motivation for Asahi's EUR2.6bn acquisition of the Peroni, Grolsch and Meantime beer brands from SAB Miller. But investment is flowing into Japan as well. Taiwan's Foxconn have announced it will take over Sharp in a USD3.5bn deal. This deal is the first foreign takeover of a major Japanese electronics company.

After a lacklustre 2015, there are signs of increased activity in South East Asia, and it is notable that PE funds are becoming more active as asset prices begin to fall to more competitive levels.

We continue to see disposals in the region by foreign businesses whose own domestic operations are under financial stress. Up to now, banks and energy companies have been at the forefront of this activity. But Q1 also saw Groupe Casino's sell its stake in Thailand's Big C hypermarket business as part of a EUR4bn deleveraging plan that could also involve asset sales in Vietnam. Its 59% stake in Big C is being bought by Thailand's TCC Group.

While activity in Australia also tailed off in Q1, we continued to see the emergence of a number of significant public-to-private transactions. PE funds TPG and Carlyle, for instance, have joined forces to bid for the veterinary and pet store business, Greencross, although their USD770m approach has so far been rejected. Allnex of Belgium, backed by Advent, has agreed a USD1.05bn merger with Nuplex, which will create one of the world's largest coatings and resins businesses.

Following the sale of the New South Wales electricity business, TransGrid, we expect to see further power privatisations in the state and the sale of publicly owned assets in Western Australia in the months ahead. The Australian government continues to increase the rigour of its foreign investment approval process, including introducing conditions with which foreign acquirers must comply.

Indonesia's own efforts to reclassify its foreign investment rules over a range of assets, including infrastructure, could, by contrast, open the door to increased foreign investment, but this is likely to take some time.

Consolidation in the stock exchange sector is once more in the spotlight, following the proposed merger of the London Stock Exchange and Deutsche Börse, with possible competing interest from ICE, owners of the New York Stock Exchange. There has been speculation that some of the main Asia Pacific exchanges might also become embroiled. Even if they do not, it would not be surprising to see consolidation between some of the region's main exchanges – Hong Kong, Singapore and Australia – come back on the agenda.

Sector insights

The slowdown in transactions was seen across all sectors, although activity remains good in TMT, life sciences and infrastructure. Financial services is looking uncertain again and mining remains deeply depressed.

CONSUMER

Getting the big deals done

The macroeconomic headwinds bearing down on the transactions market have a particular force where this sector is concerned, because they can have a significant and direct impact on the pound or dollar in the consumer's pocket.

So – in these slightly more nervous times – it is, perhaps, not surprising that the volume of consumer industry deals declined on a like-for-like basis in the first three months of 2016, compared to the year before.

By contrast, deal values held up quite well, reflecting the fact that there are still a number of large strategic transactions in the market, continuing a trend that lifted the sector to record highs in 2015.

While the position on higher value deals is encouraging, this trend may be about to run its course. Most of the deals in that bracket have been designed to consolidate or strengthen businesses and, for many companies, that work is now almost complete. But not for all.

A live deal that illustrates the trend well is the tense two-way battle for Home Retail Group, which saw Sainsbury's make a formal GBP1.4bn offer in late March after Steinhoff, the South African furniture retailer, finally withdrew from the competition.

For Sainsbury's, the deal is about searching for growth beyond its core bricks and mortar food retail offering, which operates in a market that is highly competitive and under increasing pressure from the discount retailers, such as Aldi and Lidl.

Rather than see its main offering inexorably decline in the short to medium term, Sainsbury's solution seems to be to broaden its base to become an omnichannel, food and non-food retailer. A further motivation for Sainsbury's reported GBP1.4bn offer is Home Retail's highly efficient UK distribution network. The acquisition of Home Retail would, if successful, position Sainsbury's as the UK's largest general merchandiser.

Steinhoff has since made another disruptive GBP673m takeover bid, this time for the electrical retailer, Darty, eclipsing a bid from Groupe Fnac.

The successful acquisition by Asahi, the Japanese brewer, of the Peroni, Grolsch and Meantime beer brands for EUR2.55bn flows directly out of the giant AB InBev/SAB Miller brewing merger announced late last year, where the new partners are being forced to make disposals to win antitrust clearances for their alliance.

But it is still a highly strategic transaction for Asahi – a key move to develop its global footprint in the face of a challenging core domestic market. The fact that Asahi was able to fight off competing interest from a range of PE funds is continuing evidence of the willingness and ability of corporate buyers to pay strong prices for assets that offer real strategic benefits or synergies.

We would not be surprised to see deal values flatten as the year goes on, given the future market unknowns.

But as these latest deals play out, there is a question whether corporates are anticipating volatility in the market and pre-emptively working to complete transactions before headwinds gather strength and any market risks start to crystallise.

However, it is also worth noting that the overhanging threat of Brexit does not, so far, seem to show significant signs of deterring some ambitious investors. It has not, for instance, stopped the U.S. giant Sysco from launching a USD3.1bn bid for the UK catering supplier, Brakes Group, during this last quarter.

"funds remain confident to pursue *long-term* returns despite mounting short-term risks."

Furthermore, Kuoni's decision to accept a USD1.4bn takeover from the Swedish buyout fund, EQT, arguably represents a vote of confidence in EU-based M&A, regardless of the fact that holidays can be regarded as "luxury" purchases and a product to be cautious about when there are uncertainties ahead.

Consumer groups tend to have plenty of tangible assets on which to secure their borrowing and there has been no recent sign that access to debt financing is drying up. The greater concern could perhaps be an increasing dearth of obvious targets as consolidation deals, begun in 2015, complete, and as businesses cautiously wait to see how politics will affect economics.

We would not be surprised to see deal values flatten as the year goes on, given the future market unknowns.

ENERGY AND INFRASTRUCTURE

Stiff competition boosts multiples

Despite signs of growing investor nervousness in some sectors, infrastructure continues to see some significant deals, underlining the fact that funds remain confident to pursue long-term returns despite mounting short-term risks.

The reported GBP2bn plus sale of London City Airport by U.S. PE funds Global Infrastructure Partners and Oaktree Capital is a case in point. It is proof that prized assets can still attract high multiples – in this case, if press reports are to be believed, some 30 times earnings – and widespread international interest from investment consortia, mostly made up of insurers, pension funds and sovereign wealth funds.

The eventual winner was a consortium comprised of Ontario Teachers' Pension Plan, Borealis, Alberta Investment Management Corporation and Wren House, the infrastructure platform of the Kuwait Investment Authority. But the highly competitive auction for London City attracted a wide number of potential bidders, many of whom were reportedly involved in the process right up to the final few days – amongst them Hong Kong's CKI, the Canadian pension fund PSP and the Chinese airline group HNA.

With the UK's National Grid planning to sell a majority interest in its gas distribution network, probably later this year, it is possible that many of the same bidders will resurface in what would be another multi-billion headline deal. Once again, we expect to see stiff competition.

Middle Eastern and Canadian funds were also involved in the successful AUD10.3bn acquisition of TransGrid, privatised by the New South Wales government in Australia in an auction in the infrastructure market in Australia. This deal is likely to be the precursor to a further raft of infrastructure privatisations as the State administration seeks to raise a projected AUD20bn. A number of other Australian States are also pursuing infrastructure asset sales this year.

Other developing infrastructure markets (outside Europe, North America and Australia) are showing renewed signs of life, such as Indonesia, which is relaxing foreign investment rules across a wide variety of sectors – amongst them a range of infrastructure assets such as toll roads.

Chinese investors continue to make their presence increasingly felt in international markets, notably in Europe. The EUR1.4bn sale by Swedish fund EQT of its German waste-to-energy business EEW to Beijing Enterprises in Q1 was the biggest investment to date by a Chinese enterprise in a German business.

The investment by longer term investors such as pension funds and sovereign wealth funds in top-end deals is incentivising closed-end funds to focus increasingly on mid-market deals and bilateral opportunities away from the regulated infrastructure sector. As a consequence, infrastructure investors are pursuing a wider range of assets that may share some of the long-term attractions of core infrastructure assets – leasing, district heating and oil storage, for instance – but without necessarily having all of the same monopolistic features.

Pension funds continue to expand their direct investment teams, with a focus on their global footprints. Many are opening offices in key global cities outside of their home jurisdictions.

These trends are not going unnoticed in markets that do not have classic sovereign wealth funds or pension funds of any size. With a view to building domestic investors of sufficient size to make meaningful investments, the UK government, for instance, is now urging the 89 Local Government pension schemes to join forces and form six wealth funds.

By contrast, outside energy infrastructure, the energy sector is feeling the full force of continuing low oil prices, both in terms of company performance and M&A activity. Recent weeks have seen some firmness in the oil price with the promise of slightly improved stability, but while matters remain so uncertain we expect caution to remain. Q2 may bring some opportunities as distress bites on some smaller and mid-sized players, however.

FINANCIAL SERVICES

Fortunes turn

After a resurgence in financial services transactions in 2015 – mostly driven by consolidation activity in the insurance sector – the market has swiftly returned to familiar doldrums at the start of this year, with the number of deals in sharp decline, although values held up better.

Clues as to why that is were placed in sharp relief during the UK and U.S. bank reporting season in late February when it became increasingly evident that the list of major international banks still struggling to sort out deep-seated problems exposed during the financial crisis is, if anything, longer than expected.

We saw a raft of fairly dire results, driven in part by the terrible conditions in the wholesale markets, coupled with dividend cuts and news of further restructuring moves ahead, not least from Barclays which announced that it will look to exit the African market. HSBC, which exited Brazil last year, has now announced that it will retain its Turkish banking interests, but that looks like a reluctant decision driven by a failure to find a suitable buyer.

Times are better for those banks with simple business models focused on the more routine business of lending money and issuing mortgages. The market for investment banking products is extremely tough, and the list of walking wounded is long.

The big U.S. banks – that got on with the business of restructuring earlier and are buoyed by a still growing domestic market – appear to be an exception to that rule, with operators like J.P. Morgan, Bank of America and Citigroup looking in much better shape. By contrast RBS, Deutsche Bank, Barclays and Standard Chartered continue their search for a workable way forward.

The list of major international banks still struggling to sort out deep-seated problems exposed during the financial crisis is, if anything, longer than expected.

There are also growing worries that, as the Chinese economy decelerates, the scale of non-performing loans could reach staggering proportions, as its debt pile is now an estimated 275% of GDP. Concerns continue to be expressed about the Indian banking sector as well.

Of the few significant deals that did get announced in Q1, the proposed tie-up between the London Stock Exchange and Deutsche Börse, creating Europe's biggest exchange valued at an estimated GBP21bn, is the continuation of a long-running global consolidation story. Along the way there have been a string of mergers and attempted, but often thwarted, deals.

The LSE is now firmly in play, so the likelihood of a transaction looks high. The question remains whether a rival bid will surface, with New York Stock Exchange owner ICE seen as a possible front-runner but with potential interest also from Hong Kong. Despite regulatory and national political hurdles to such deals, the trend towards the creation of a few big global operators in the sector looks pretty firmly set.

The consolidation between mid-tier insurers squeezed between the biggest players and niche operators, particularly in London, appears to have quietened down after last year's run of deals. However, focus has shifted to Australia where Nippon Life announced plans late last year to buy 80% of NAB's life business for USD1.7bn,

whilst Macquarie has recently agreed to sell its life business to Zurich, and ANZ and CBA are said to be reviewing the future of their own life businesses.

The outlook for the banking sector remains relatively bleak with investor sentiment clouded by a host of significant uncertainties. Brexit poses obvious potential problems for London as a financial centre, but the wider ramifications for global GDP, trade and banking activity look to be even greater if the UK referendum goes in favour of demerging the world's fifth biggest economy from so powerful a market.

Other pressures are crowding in too, not least concerns about the outcome of the U.S. presidential election, slowing global GDP growth and the health of China's economy. It remains possible that banks will begin to pursue more radical options to shake up their operations in the months ahead and this could have a positive impact on deal activity, helped by continuing low interest rates. The challenge, however, may be whether buyers can be found should banks push ahead with disposals.

LIFE SCIENCES

A more comfortable pace

After the huge volume of life sciences deals in the last two years – totalling some USD630bn – it is, perhaps, not surprising to see the market begin 2016 on a slightly quieter note. In fact, Q1 saw both the value and volume of deals fall quite sharply compared to comparable quarters in 2014 and 2015.

We continue to believe that the tide of mega-deals in the industry has probably already reached its high point with the USD160bn Pfizer/Allergan merger at the end of last year – the biggest-ever pharmaceutical deal. Scanning the market, there are few obvious huge tie-ups left to be done.

So while we will still see a good stream of transactions in the months ahead, it is likely that values will remain at a lower level. Instead we expect more mid-market deals of the sort just announced by Vectura and Skyepharma, who are coming together to create a specialist respiratory inhalation group in a GBP441m merger.

This is not to suggest that Q1 itself did not see any large deals. In January, Baxalta finally agreed to Shire's USD32bn takeover. This deal creates a powerful force in the treatment of rare or "orphan" diseases, a highly lucrative area of the market where companies are often incentivised to create new drugs.

The Shire/Baxalta combination also points to the continued heat in the biotech market, where we expect to see considerable activity in 2016. Biotech companies have not, until now, had the same "patent cliff" anxieties as their small molecule cousins. But the gradual coming of age of the biotech market and the rise in the number of approved biosimilars will start to create more pipeline pressure. That could well persuade some of the bigger players to emulate the major pharma companies and try to complement their R&D efforts with more acquisitions.

Within the biotech sector, immunology is likely to be an area of particular M&A activity. Baxalta's appeal to Shire was no doubt further enhanced by the news that Baxalta had agreed to pay USD1.6bn to the Danish biotech group, Symphogen, for the rights to co-develop six cancer immunotherapies in pre-clinical development.

Consolidation in the generics sector is another continuing trend, as we saw in Q1 with the USD9.9bn merger of Mylan and the Swedish group, Meda.

Mylan – a leading, although not always successful, player in this rolling consolidation story – tried to merge with Meda two years ago, and the rekindling of the transaction is evidence of its continuing determination to do deals. It is also significant that the two groups already had an existing commercial relationship, with Meda handling the European sales of Mylan's EpiPen. Such ties can often precede M&A transactions.

> While we will still see a good stream of transactions in the months ahead, it is likely that values will remain at a lower level.

Medical equipment makers were also active in Q1, when we saw Abbot Laboratories acquire diagnostic company Alere for USD5.8bn, and Stryker complete two deals – paying USD2.8bn to buy Sage and USD1.2bn for Physio-Control. This segment has been increasingly busy in the past 12 months, not least since the huge merger between Medtronic and Covidien.

An interesting market development worth watching is the increasing inroads made by technology companies into the life sciences sector – not least in the sometimes controversial area of artificial intelligence.

IBM Watson Health, the healthcare arm of IBM, has acquired Truven Health Analytics from Veritas Capital for USD2.6bn with the aim of positioning itself as the world's leading health data analytics company delivering "unique cognitive capabilities". Deepmind, Google's UK-based artificial intelligence subsidiary currently working with the NHS to develop patient-care apps, has also predicted that AI will be an increasingly important area of healthcare in the future.

> "Significantly, as many of the majors look to slim down their *operations* it's not just non-core assets that are being prepared for disposal."

Meanwhile, the fierce patent war over the invention of the groundbreaking CRISPR gene-editing technology, currently the subject of an investigation by the U.S. Patent and Trademark Office, will undoubtedly have far-reaching commercial implications.

While the outcome of this IP feud is still uncertain, we are sure that – with an estimated USD1bn of venture capital already invested by companies exploring gene snipping solutions – there will be deal activity in this area in the future, whether through IPOs or trade sales.

MINING

A long hard road

The mining sector remains depressed as operators struggle to restructure their operations in the face of continuing weak commodity prices, a steep drop in demand from China and continued oversupply in many commodities.

With many of the mining majors racking up record losses and announcing cuts or suspensions in dividend payments to shareholders, the focus remains firmly on trying to reduce mounting debts by a combination of cuts in capital and operational costs and asset disposals.

Significantly, as many of the majors look to slim down their operations, it's not just non-core assets that are being prepared for disposal. Anglo American, Vale, BHP Billiton and Glencore have all got significant debt reduction programmes in place and, increasingly, core operations are being considered for sale, a trend we are also seeing in the oil and gas sector.

But even if they put more attractive assets up for sale the question remains: can they find suitable buyers willing to take a long-term view on the recovery in key commodities?

It is possible that we will see interest from Chinese and Japanese buyers in the months ahead and it is significant that one of the few reasonably sized mining deals in Q1 emanated from Japan.

Sumitomo Metal Mining Co has paid USD1bn to increase its minority stake in the Morenci copper mine in Arizona, North America's biggest copper mine. The mine is owned by Freeport-McMoRan, which, like its bigger rivals, is also selling core assets to reduce debt.

The slight recovery in commodity prices in recent times should be enough to keep operators in business while these debt reduction and restructuring moves are pushed through, but, at this level, they are hardly likely to spark a spate of deal activity. What's more, if we see prices plunge further, this could lead to insolvencies, especially among more junior players who do not have the balance sheets to ride out the current downturn.

One area where we could see some signs of life, however, is the gold mining sector. The price of gold has strengthened in recent months as it traditionally does when other economic indicators begin to turn negative. The gold mining industry is generally considered ripe for consolidation so there may be deal activity in this area.

Furthermore we have seen some M&A transactions with novel features designed to bridge the value gap between owners and investors and to convince owners to

complete those transactions at the current low commodity prices. Clawbacks and trailing contingent payments are two of the features that have been utilized. In an environment of declining minerals prices, deferred consideration, with payments contingent on factors out not within control of the parties', is becoming more common. When the trigger is the trading price of a particular metal both parties face a similar risk. However, when the deferred consideration is at the option or control of one party (usually the incoming party) this may add to the due diligence process but may favour the buy-side as it puts the buyer in a position of control. Particularly where the life of the asset is difficult to estimate or there is unknown potential to develop an aspect of a project, and if the market for minerals remains volatile, we expect deferred consideration triggers to continue to be used and in more creative ways.

Accordingly, opportunities exist in the market for experienced, resilient and creative management teams with a strong track-record to generate value by acquiring stalled or unloved projects with a minimum up-front cash spend.

Nevertheless, the outlook for the remainder of the year remains fairly bleak. The mining industry faces a long hard road ahead.

PRIVATE EQUITY

Uncertainties return

After a much busier year for PE funds in 2015 – when sellers took advantage of high valuations and good credit terms to sell or IPO the best asset in their portfolios and buyers went back on the front foot for the first time since the financial crisis – there has been a distinct change of mood.

This year a lack of attractive, "ready for sale" assets, plus the uncertainties caused by a plethora of macroeconomic and political headwinds, have already conspired to depress activity and we expect the first half of 2016 to be considerably quieter.

In Europe it's clear that Brexit is preying most acutely on the minds of dealmakers, whether they are buyers or sellers.

For buyers the difficulty lies in trying to envisage what a UK or Eurozone business might look like should the 23 June vote go in favour of Britain leaving the EU. For sellers, when able to find a purchaser, there is the worry that asset prices may have been reduced because of the buyer's worries about the impact of Brexit on the performance of the business and on the wider Eurozone economy. These are imponderables – but until they are resolved they are acting as a brake on activity.

For the first time in many quarters we have seen some concerns raised about access to debt financing, a particular issue for PE funds.

In Europe, sellers and buyers are focused on assurances that certain funds financing has been put in place. In the U.S. the problem has been more acute, with the debt markets generally a great deal more shaky and the high yield markets, in particular, seizing up. We are, however, starting to see the first signs of confidence gradually returning to those markets, such as inflows into U.S. high yield funds (with a record inflow of USD4.97bn in the week ended 2 March).

Corporate buyers, still enjoying good access to debt financing, continue to pay premiums to capture prized assets and so outbid PE investors in competitive auction processes. That was certainly the case in the EUR2.6bn acquisition of the Peroni, Grolsch and Meantime beer brands by Asahi, where a handful of PE funds were at one stage reported to be in the running.

Significant deals are still getting done. Apollo, the U.S. investment fund, completed one of the biggest leveraged buyouts of recent times with its USD6.9bn acquisition of the home security business, ADT, which will now be folded into Prime Security, another recently acquired Apollo company serving complementary markets.

PE funds remain under pressure from their limited partners to deploy the huge amounts of dry powder they have accumulated in recent years and to return value to investors. In a relatively rare secondary direct investment move, for example, Bridgepoint is returning liquidity to investors by selling interest in a EUR2bn portfolio of European businesses, spanning Germany, the Netherlands, Poland and Italy, in a deal led by Compass Partners.

For the first time in many quarters we have seen some concerns raised about access to debt financing, a particular issue for PE funds.

But pressure from investors to deploy capital is often matched by nervousness that hastily completed deals could fall foul if Brexit, a hard landing for the Chinese economy or recession in the U.S. create much greater turbulence for the global economy.

"The sector continues to see *high levels* of activity, with technology, in particular, remaining very busy – a trend we expect to continue.

Attractive assets which do become available in the coming months, and which are seen as 'resilient' or counter-cyclical, will be the subject of highly competitive auctions and 'frothy' valuations. We expect that the management teams of such assets will push for extremely generous re-investment terms as bidders jostle for position and try to win their favour in order to try to gain a competitive advantage.

TELECOMS, MEDIA AND TECHNOLOGY

Tech deals drive activity

While TMT transactions were quieter in the first quarter of 2016, after two years of extraordinary growth the sector continues to see high levels of activity, with technology, in particular, remaining very busy – a trend we expect to continue.

One reason for this is the growing presence of Chinese investors in the technology M&A market. The first quarter of the year saw the tide of outbound investment continue to grow, with the active encouragement of the Chinese government, as Chinese firms seek access to key technologies and content to exploit at home and in new growth markets.

The U.S. and, increasingly, Europe are the prime target markets. Standout Q1 deals included HNA's USD6bn acquisition of the California-based technology distributor, Ingram Micro. Dalian Wanda also made the biggest-ever Chinese investment in film production when it acquired Legendary Entertainment, co-financier of blockbuster films like Jurassic World, for USD2.5bn.

In Europe, Opera Software, the Norwegian web browser maker, was bought for USD1.3bn by a consortium of Chinese technology and financial groups, including the mobile games and apps group, Kunlun and the internet security firm, Qihoo.

Another driver of tech activity is cross-sector acquisitions and investments. Established players in industries as diverse as financial services, healthcare and automotive are looking for ways to harness technology to revitalise business models and to defend themselves against disruptive technology companies entering their markets.

In a battle with the likes of Google to develop driverless cars, General Motors has, for instance, completed a string of recent deals aimed at developing an on-demand network of self-drive taxis and cars. These include a USD500m investment in the ride-sharing software group, Lyft, and the USD1bn acquisition of the driverless car start-up, Cruise Automation.

The social media giants continue to compete hard for cut-through apps and content particularly in instant messaging services, where the battle for young users between Facebook and Snapchat is intensifying.

At the end of Q1, Facebook snapped up Masquerade, the Belarus-based imaging start-up behind the MSQRD app, allowing users to add fun filters to video selfies. It is evidence that the U.S. tech giants still have the appetite and the firepower, helped by a strong dollar, to move fast in the acquisitions market – even at a time of greater economic uncertainty.

"The U.S. and, increasingly, Europe are the *prime target* markets."

Increasingly diverse sources of finance remain readily available for tech companies in the later stages of development alongside traditional venture capital. As companies stay private longer we are seeing sovereign wealth, hedge and mutual funds join the fray as we saw when Blippar, the augmented reality search company, raised USD54m during the quarter from a group of investors including the Malaysian Government's Khazanah Nasional Berhad investment fund.

As companies stay private longer, we predict a rise in the number of secondary sales as investors push to find liquidity in this part of the market. This is an area that is already well developed in the U.S.

The biggest telecoms deal of the quarter was the move by Vodafone and Liberty Global to merge their Dutch operations to create a combined mobile, fixed-line broadband and cable-TV offering, continuing the move to "quadplay" strategies by some players.

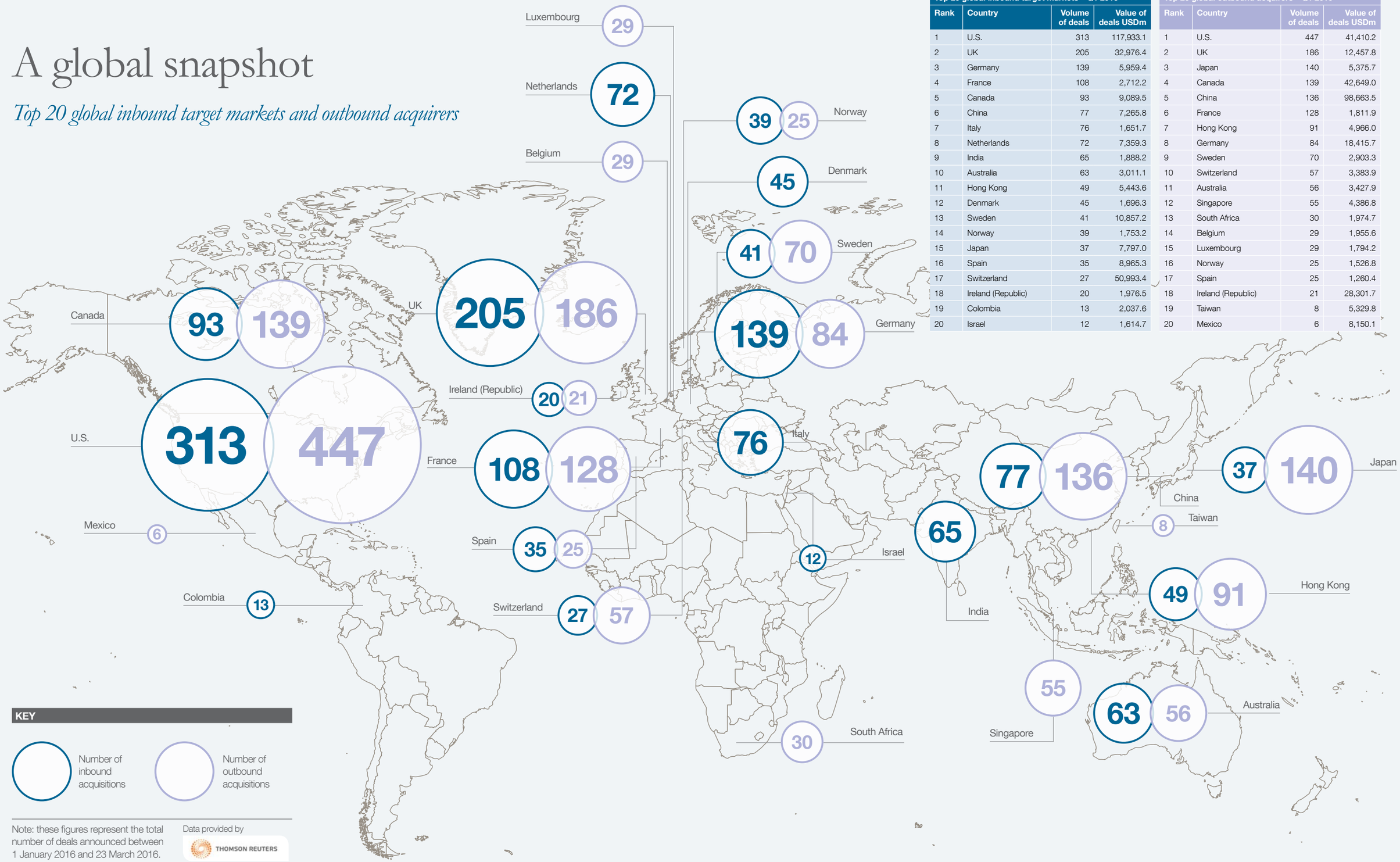
Consolidation remains the ongoing theme in telecoms, particularly in Europe where we continue to await crucial rulings by the European Commission on a number of mobile-to-mobile mergers, not least the proposed GBP10bn merger between O2 and Three in the UK.

In another important regulatory development, the EU Commission has made it clear that it will continue to look closely in merger reviews at the impact proposed deals have on research, innovation and product development. This is also a growing focus for U.S. competition regulators, as we saw last year in the proposed tie-up between Applied Materials and Tokyo Electron, which was subsequently abandoned.

This means that even acquisitions of embryonic or niche businesses, which have limited market power but nevertheless perform innovative or "disruptive" roles in certain markets (not just TMT), may risk running into serious roadblocks in the merger review process.

A global snapshot

Top 20 global inbound target markets and outbound acquirers



Note: these figures represent the total number of deals announced between 1 January 2016 and 23 March 2016.

Data provided by THOMSON REUTERS

Top 20 global inbound target markets – Q1 2016

Rank	Country	Volume of deals	Value of deals USDm
1	U.S.	313	117,933.1
2	UK	205	32,976.4
3	Germany	139	5,959.4
4	France	108	2,712.2
5	Canada	93	9,089.5
6	China	77	7,265.8
7	Italy	76	1,651.7
8	Netherlands	72	7,359.3
9	India	65	1,888.2
10	Australia	63	3,011.1
11	Hong Kong	49	5,443.6
12	Denmark	45	1,696.3
13	Sweden	41	10,857.2
14	Norway	39	1,753.2
15	Japan	37	7,797.0
16	Spain	35	8,965.3
17	Switzerland	27	50,993.4
18	Ireland (Republic)	20	1,976.5
19	Colombia	13	2,037.6
20	Israel	12	1,614.7

Top 20 global outbound acquirers – Q1 2016

Rank	Country	Volume of deals	Value of deals USDm
1	U.S.	447	41,410.2
2	UK	186	12,457.8
3	Japan	140	5,375.7
4	Canada	139	42,649.0
5	China	136	98,663.5
6	France	128	1,811.9
7	Hong Kong	91	4,966.0
8	Germany	84	18,415.7
9	Sweden	70	2,903.3
10	Switzerland	57	3,383.9
11	Australia	56	3,427.9
12	Singapore	55	4,386.8
13	South Africa	30	1,974.7
14	Belgium	29	1,955.6
15	Luxembourg	29	1,794.2
16	Norway	25	1,526.8
17	Spain	25	1,260.4
18	Ireland (Republic)	21	28,301.7
19	Taiwan	8	5,329.8
20	Mexico	6	8,150.1

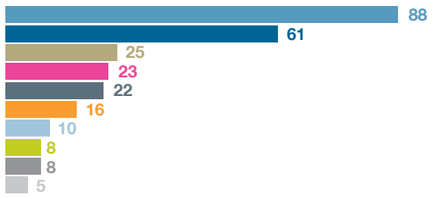
A global snapshot

Top target markets for the world's largest acquiring countries

U.S. – the world's largest acquiring country

Value of deals (USDm)

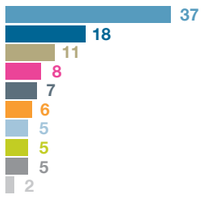
UK	12,590	Brazil	1,138
Canada	6,110	Italy	483
Australia	2,308	Sweden	9,937
Germany	1,402	Ireland (Rep)	704
Japan	2,092	Denmark	1,080



UK

Value of deals (USDm)

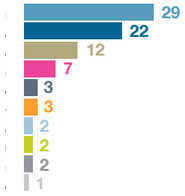
U.S.	1,459	South Africa	280
France	378	Canada	1,663
Italy	784	Poland	339
Netherlands	6,557	Brazil	166
Denmark	213	Portugal	123



China

Value of deals (USDm)

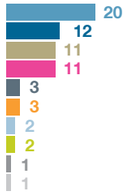
U.S.	38,602	UK	562
Hong Kong	4,269	Norway	1,363
Germany	2,932	Canada	497
Malaysia	386	Greece	402
Switzerland	46,843	Russian Federation	1,207



France

Value of deals (USDm)

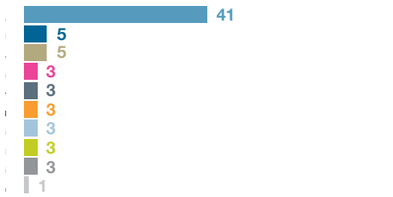
U.S.	370	Romania	98
Germany	184	Switzerland	385
Belgium	145	Spain	224
UK	18	Dem Rep of the Congo	160
China	173	Finland	36



Hong Kong

Value of deals (USDm)

China	3,247	British Virgin Islands (UK)	130
U.S.	688	Australia	98
South Korea	32	France	73
Malaysia	208	Indonesia	25
UK	183	Germany	251



Germany

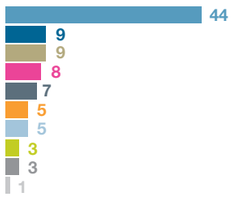
Value of deals (USDm)

U.S.	1,420	Italy	74
UK	14,748	Brazil	41
Netherlands	61	Switzerland	800
Belgium	544	Ireland (Rep)	200
India	479	Mexico	33

Japan

Value of deals (USDm)

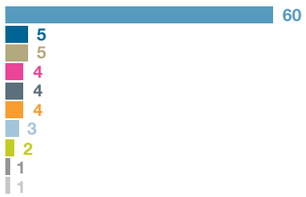
U.S.	2,745	Vietnam	128
UK	375	China	66
Singapore	77	Philippines	778
Malaysia	122	Norway	96
France	601	Israel	212



Canada

Value of deals (USDm)

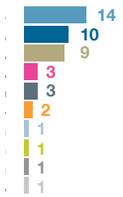
U.S.	39,922	Ireland (Rep)	22
Colombia	2,002	Mexico	75
Brazil	22	Romania	28
Australia	66	Costa Rica	360
Germany	27	Malta	94



Sweden

Value of deals (USDm)

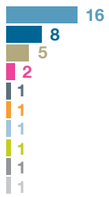
Denmark	38	Belgium	33
Norway	43	Lithuania	239
Finland	822	France	54
Switzerland	1,548	Estonia	34
Italy	75	Iceland	9



Switzerland

Value of deals (USDm)

Germany	6	Israel	843
U.S.	730	Morocco	500
UK	131	Canada	203
Norway	21	Russian Federation	40
Ireland (Rep)	895	Ivory Coast	10



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About the research

The underlying data for this research comes from Thomson Reuters.

– The data contained in this publication spans 1 January 2016 and 23 March 2016 inclusive.

Data provided by THOMSON REUTERS

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