

M&A and restructuring trends in Asia-Pacific

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Development drivers

Over the last two years, Asia-Pacific has experienced secular growth in mergers and acquisitions, with transaction volumes growing at 25 per cent a year since 2003. Six key developments should continue to drive M&A and restructuring activity in this region in 2006.

1. Supportive regulatory environment

To create stronger national champions and improve industry standards, regulators and governments have encouraged foreign investment and domestic consolidation in several markets. This trend has been particularly visible and pronounced in the banking sector in markets such as the Republic of Korea, the People's Republic of China, Taipei, China and Indonesia (see Table 1).

2. Private equity and financial investors

Since 2004, the region has witnessed a dramatic increase in successful exits by financial investors which started making meaningful investments in Asia-Pacific a few years ago. Evidence of this trend has particularly been seen in the Republic of Korea, with Newbridge's sale of Korea First Bank to Standard Chartered, Carlyle's sale of Koram Bank to Citigroup and the sale of Jinro to Hite Brewery. With large amounts of new capital raised by financial sponsors in the last 12 months for investment in Asia – from both local and international participants – private equity is expected to play a major buy-side role in 2006 and beyond.

3. Globalisation and regionalisation of local champions in several markets

Leading companies in Southeast Asia, the People's Republic of China and Hong Kong, China have been making acquisitions to access growth opportunities outside their home markets. Singapore Power's acquisition of TXU Australia, Lenovo's acquisition of IBM's PC business, Hutchison's (AS Watson's) acquisition of Marionnaud Perfumeries in Europe and Telekom Malaysia's acquisition of Excelcomindo in Indonesia are all expressions of this trend.

4. Access to critical natural resources

State-owned companies in the People's Republic of China and India are increasingly looking to acquire access to critical natural resources across the globe to secure national supply – examples include CNPC's acquisition of Petrokaz, the acquisition of Encana Corp's Ecuador assets by a PRC consortium, CNOOC's unsuccessful bid for Unocal and several bids for upstream assets by ONGC and IOC from India.

Table 1: Top 10 Asia-Pacific Financial Industry M&A Deals 2004-2005

Date	Target	Acquirer	Deal size (US\$ MM)
January 10 2005	Korea First Bank	Standard Chartered	3,278
August 18 2005	Bank of China	Investor Group	3,100
August 31 2005	Bank of China	Asia Financial Holdings	3,100
June 16 2005	China Construction Bank	Bank of America	2,500
June 24 2004	BoCOMM	HSBC	1,749
February 22 2004	Koram Bank	Citigroup	1,637
June 30 2005	International Bank of Taipei	SinoPac Financial Holdings	1,548
October 26 2004	ANZ-Project Finance Business	Standard Chartered	1,500
June 28 2005	China Construction Bank	Temasek Holdings	1,400
July 22 2005	Chang Hwa Commercial Bank	Taishin Financial Holdings	1,156

Source: Thomson SDC

5. Western companies looking to expand their footprint into faster-growing Asian markets

This is possibly the least surprising trend, but one that is gaining momentum with the ongoing deregulation of markets within the region and the lifting of limitations on foreign ownership. In the People’s Republic of China and India in particular, Asia’s two major growth markets, this has been a major driver of deal activity. Some of the most notable examples include Bank of America and RBS buying strategic stakes in PRC banks, Philip Morris acquiring Sampoerna in Indonesia, Holcim acquiring a strategic stake in Gujarat Ambuja Cement in India, and Vodafone acquiring a strategic stake in Bharti, India’s largest cellular company.

6. Strong capital markets

Over the last two years, the maturing and strengthening of the region’s capital markets have made it easier for companies to raise funds for acquisitions. With many Asian stock markets having risen between 20 per cent and 45 per cent between January 2004 and late 2005, a more positive outlook for investors and stakeholders has helped support corporate acquisitions.

Threats to development

Despite these developments, and the expectation of increasing M&A and restructuring volumes in Asia-Pacific in 2006, there are risks that could impede the growth of this market:

- Political instability, higher oil prices and interest rates and other external shocks could affect growth rates in the region and limit access to capital, both of which have been important catalysts for mergers and acquisitions.
- Increased protectionism and nationalist sentiments in certain markets could dampen enthusiasm for cross-border activity, and must be anticipated and managed carefully in any situation where a foreign entity is entering a new market or attempting to take over what is considered a major ‘national’ asset or icon through an acquisition.
- Lack of transparency or weak disclosure standards in certain Asian markets could lead to surprises that were not anticipated during due diligence.
- The pace of regulatory change and, in some industries and markets, reversal of regulation is a risk that needs to be assessed and taken into account, as far as possible.

Table 2: How Investment Banks Add Value in M&A and Restructuring

Strategic business issues	<ul style="list-style-type: none"> • Synergies assessment, quantification (cost and revenues) and timing • Combined strategy, including strategic rationale for the transaction
Potential partner search and consortium formation	<ul style="list-style-type: none"> • Assist in searching and evaluating potential partnership with financial investors and others • Facilitate consortium formation, including identification and resolution of partnership issues
Valuation and negotiation	<ul style="list-style-type: none"> • Due diligence • Relative valuations (market valuation based on comparables, precedent transactions and discounted cash flows, contribution analysis on both stated and adjusted figures) • Calculation and negotiation of exchange ratio • Capital management policy, including combined capital structure • Merger consequences analysis, including financial and capital impact
Structuring	<ul style="list-style-type: none"> • Explore creative structuring alternatives to provide most efficient solution • Coordinate other advisers in resolving legal, tax and accounting issues
Financing	<ul style="list-style-type: none"> • Determine optimal funding mix for acquisition • Provide advice in equity and debt capital raising and securitisation as funding alternatives • Potential provider of bridge loan financing
Negotiations with regulators	<ul style="list-style-type: none"> • Assist in developing tactics and executing an overall negotiation strategy with the government, including on transaction structure options, price, contractual arrangements etc
Presentation of transaction	<ul style="list-style-type: none"> • Communications timetable • Analyst/press/rating agency presentations • First day external communication plan (investors, press meetings, government meetings) • Internal communication plan (presentation to staff, unions) • Logistics (printers, conference facilities, war room) • Investor road show
Other	<ul style="list-style-type: none"> • Assess potential interloper/provide street intelligence • Help to identify and address corporate governance issues • Review the M&A rules in the country and their impact on the financial terms of the transaction • Regulatory filings in-market and overseas as appropriate • Merger timetable, including regulatory approvals

Source: Morgan Stanley, 2005

To help manage these risks, many companies and governments rely on advisers such as investment banks, law firms and accountants to help them explore or consummate a transaction most effectively.

Key Trends in Asia-Pacific

So what types of transaction are we likely to see more of in 2006 and beyond? The authors have identified the following key trends for the region.

1. Increase in M&A volumes in all markets, including historically inactive markets

Compared to 2003 and 2004, M&A volumes in all Asia-Pacific markets were up in 2005. The authors anticipate the following market-by-market developments.

Australia: Australia has been the largest M&A market in Asia-Pacific in the last few years and this is unlikely to change in 2006. Volumes in 2005 were driven primarily by domestic consolidation across various sectors such as consumer and retail, basic materials, transportation and utilities, as well as Macquarie’s purchase of infrastructure-related assets globally. These trends are expected to continue in 2006, together with a step-up in cross-border activity.

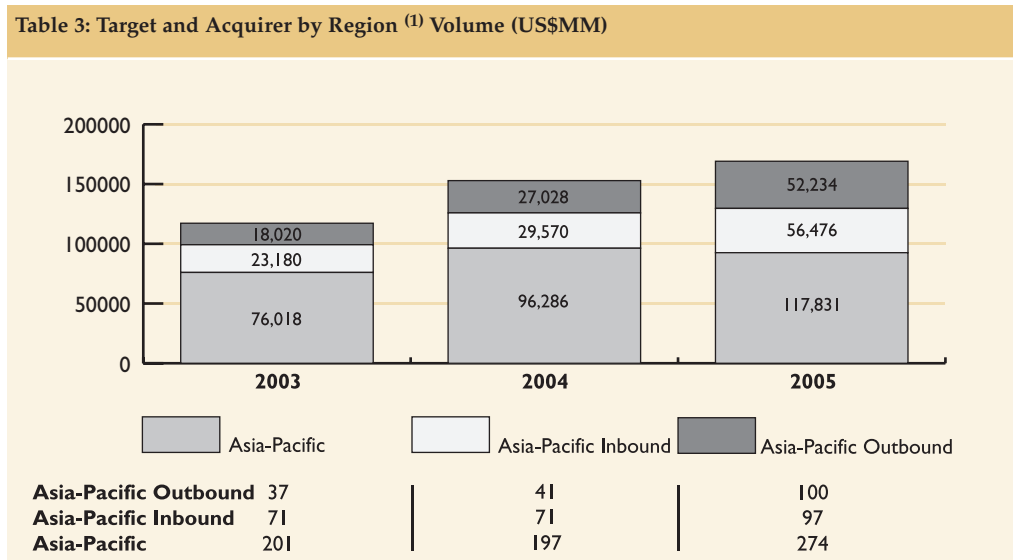
People’s Republic of China: The People’s Republic of China is emerging as the largest M&A market in Asia-Pacific after Australia, with active domestic, inbound and increasingly outbound M&A activity. A substantial increase in outbound M&A activity is expected in 2006 as PRC companies develop into global players and buy overseas assets.

India: The Indian M&A market grew rapidly in 2005, with volumes more than four times of those in 2004. Increasing cross-border activity is expected in this market, particularly in the technology, natural resources and pharmaceutical sectors.

Republic of Korea: M&A volumes will continue to be driven primarily by sales of companies owned by creditor banks and financial sponsors. Activity in 2006 is likely to be dominated by the financial services and general industrial sectors.

Singapore and Southeast Asia: Singapore is expected to be the largest M&A market in Southeast Asia, driven by cross-border activity, with Temasek being a major contributor. Other markets may see domestic consolidation, particularly in the banking sector.

Taipei, China: Significant M&A activity is expected in the banking sector, a trend which started a couple of years back but picked up significantly in 2005.



Source: Thomson SDC (1) Deal size above US\$100MM

2. Significant increase in outbound M&A

In addition to an overall increase in M&A and transaction volumes, the proportion of outbound mergers and acquisitions in the region is increasing rapidly as Asian companies seek to become not only Asian champions but global winners in their industries by acquiring assets and companies outside the region. Whereas the percentage of inbound M&A activity (non-Asia-Pacific acquirers buying targets in Asia-Pacific) has been fairly stable, the percentage of outbound transactions (Asia-Pacific companies acquiring targets outside of the

region) has risen from 11.9 per cent of all regional M&A activity in 2003 to 21.2 per cent in 2005, surpassing the number of inbound transactions (20.6 per cent in 2005) for the first time.

3. Increase in the average size of deals

Over the last three years, the number of M&A deals in the range of US\$1 billion-plus by transaction value has risen steadily, from 25 in 2003 to 50 in 2005. In the authors' view, this trend looks set to continue as industries across the region are deregulated.

Table 4: Asia-Pacific M&A Deals Above US\$1 Billion in Value

Year	Volume (US\$MM)	Number of deals
2002	57,454	29
2003	53,721	25
2004	82,320	36
2005	110,175	50

Source: Thomson SDC data

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