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M&A

2024

IN THE CITY

Port by Jane Hoggard

WELCOME TO M&A IN THE CITY FOR 2024

Our first edition for 2024 takes you inside the biggest Australian Public M&A deal for 2024 so far, and spotlights M&A tactics that we see shaping a cautiously optimistic outlook for the remainder of 2024.

WHY CAUTIOUSLY OPTIMISTIC?

Dealmakers in New York are reporting a new year uptick in transactional activity, with the hope this may continue to gain momentum through 2024. Sentiment in London is similar, if perhaps slightly more subdued by military endeavours in and close to Europe.

More clarity on inflation and interest rate expectations is the key driver. The US economy's resilience through the inflationary cycle positions companies to take advantage of the calmer macroeconomic conditions and underpins increasing confidence, while the UK eyes European markets which have been less lively, so far.

While geopolitical and regulatory considerations remain at the forefront of risk calculations, American deal-doers expect the biggest impact of the upcoming Presidential election to be buyers and sellers looking to bring forward prospective deals, rather than shy away from them. Consensus among deal-doers at a recent XBMA conference held in New York was that greater macroeconomic stability would serve to smooth any gyrations from political volatility.

What will this more assured medium-term outlook mean? We expect to see an acceleration in energy transition dealmaking, as well as further consolidation in the tech sector.

The global picture is a fascinating one. US-Australian cross-border deals have continued in 2024. After our team finished last year with Newmont/Newcrest and Allkem/Livent, we felt like groundhogs with Alcoa/Alumina kicking off this month. As Australian dealmakers are well aware, the most exciting uptick in outbound activity is coming from Japan. Our inside the deal podcast explaining Altium's acquisition by Japanese electronics manufacturer Renesas dives into this in more detail – you can also read a transcript of that in the following pages.

What does this mean for Australian markets? Domestic acquirers can expect strong international competition, not only from Japanese buyers but also North American sources who continue to see Australia's well-regulated companies and transparent transaction regime as an opportunity to access the Asian growth story utilising the strength of the Greenback.

MEET THE EDITORS

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IN THIS EDITION

THE ALTIUM DEAL PODCAST

Inside the $9.1bn deal for Altium - a new benchmark on reverse break fees and Japanese buyers return

KWM Corporate M&A Partners Dan Natale and David Friedlander recently advised Altium in its $9.1bn acquisition by business partner, Japanese electronics manufacturer Renesas. They spoke with fellow Partner Antonella Pacitti about the transaction - Australia's largest public M&A deal for 2024 so far. The trio discuss the strength of Japanese interest in Australian markets and analysing its most noteworthy point - the substantial reverse-break fee protecting Altium if the deal did not win regulatory approval. The key question – what does it mean for future deals?

Below is an edited transcript of that conversation. You can listen to their full discussion by searching for KWM Podcasts on Apple or Spotify.

ANTONELLA PACITTI

Dave, you've been with Altium on its journey for 20 - 25 years? From fledgling company to now… Tell us about what it does, about your relationship and our relationship with Altium as a firm?

DAVID FRIEDLANDER

Altium is an Australian founded, now multinational software company headquartered in California, with a focus on computer-assisted design of printed circuit boards and embedded system development. Founded in 1995 in Tasmania, we worked on its IPO, we helped it through all its different stages as an ASX listed company. It partnered with Renesas about 2 years ago. And that's where the negotiations [for this deal] began.

ANTONELLA PACITTI

A real credit to the power of relationships. For the benefit of the audience, let's jump a little bit forward first, Dan, can you talk us through the terms of the deal that you and Dave have extracted for this acquisition?

DANIEL NATALE

The deal values the company at about $9.1 billion. Renesas will purchase all Altium's shares for $68 50 per share in cash. It has the unanimous support of both companies' boards. The price represents a whopping premium of approximately 34% to the closing price the day prior to the transaction announcement.

ANTONELLA PACITTI

Dave, late last year we were saying 'watch out for the Japanese buyers, they're coming back'. Are they well and truly back?

DAVID FRIEDLANDER

Absolutely. I mean, all the conditions are right for Japanese M&A. The two biggest deals in the last few months - Link market services, and then this one - both billion-dollar deals, both Japanese acquirers.

Why do you think that is, Dan?

DANIEL NATALE

It's simple macroeconomics at one level. Low interest rates in Japan compared to the rest of the world. You've got a lot of money washing around looking for a strategic home. Australia is a particularly good jurisdiction to put that money to work. We've got a good system for takeovers, and we're part of the overall Asian growth story. We're hearing multiple inbounds from Japanese acquirers.

Download the podcast here

Spotify

Antonella, what are you seeing and hearing in Perth, the crucible for resources, energy, deal-making?

ANTONELLA PACITTI

Much more Japanese interest especially in critical minerals. There's undoubtedly more ability to partner with the Japanese commodity houses than other global partners - without potentially compromising access to all-important government funding in Australia and the US.

The Japanese are known quantity when it comes to making deals happen to support manufacturing, innovation and accessing natural resources. There's often cash involved as well. When Japanese buyers come knocking, it can be a real benefit for target shareholders.

OK Dan and Dave, let's get back to this deal. Two key points for our listeners: One, this is not the first time that Altium has been approached. Two, it's got a really noteworthy protection which you've negotiated for Altium. Dave, talk us through the earlier Autodesk approach?

DAVID FRIEDLANDER

Several years back Altium had been approached quite publicly by Autodesk, an offer that also wound up in the public domain. At that time, its strategy projected a value well in excess of the offer price. This deal ultimately proves that the strategy was right. It's significantly higher. And the Renesas negotiation importantly remained confidential right up until announcement.

ANTONELLA PACITTI

A really interesting feature - which the AFR picked up on - was the very substantial 4.5% reverse break fee. Dan, talk us through how you went about this for Altium?

DANIEL NATALE

It's tied to Renesas winning regulatory approval which includes approval from the US, which is very rare in this market at least – to have a reverse break fee tied to winning regulatory approval.

Negotiating this protection for Altium addresses an issue for target companies since Dave's earlier Pendal deal with Perpetual. There the bidder had argued that it could assume it's rather paltry reverse break fee of 1% of deal value acted like an option - they could simply pay it and walk away if they found a better deal. That was first time the Australian court considered the issue - and found a bidder couldn't simply walk away without an express right. The court had a discretion to hold the bidder to its bargain. But the important point there is, it was only ever a discretion.

Obviously a higher break fee deters any bidder from trying to walk away. That's what we've negotiated here - it heavily incentivizes them to obtain the regulatory approvals.

Antonella, you were involved in one of the largest deals of the last 12 months, Newmont's $26bn acquisition of fellow miner Newcrest. What would have happened in that case, had the deal fallen over?

ANTONELLA PACITTI

I think the key difference there is, of course, team KWM acting for the foreign bidder in that one and pushing hard in that case for suitable equivalency between the break fee and the reverse break fee! We landed on a reverse break fee of about 2.2%. – So, dwarfed by what you were able to achieve for Altium, and without a trigger for regulatory approval. That trigger was limited to reimbursement of actual third-party costs.

The point is you must take the full circumstances of bidder, target and the deal into account negotiating what is legitimate for both parties. In Newmont we viewed regulatory approval and risk as a shared problem. We had some very common shareholders already between Newmont and Newcrest. So maybe there was a broader perspective for Newcrest's board as to what they were willing to extract, to maintain deal certainty and obtain those regulatory approvals.

Dan, Dave. Any other reflections on reverse break fees before we wrap up?

DANIEL NATALE

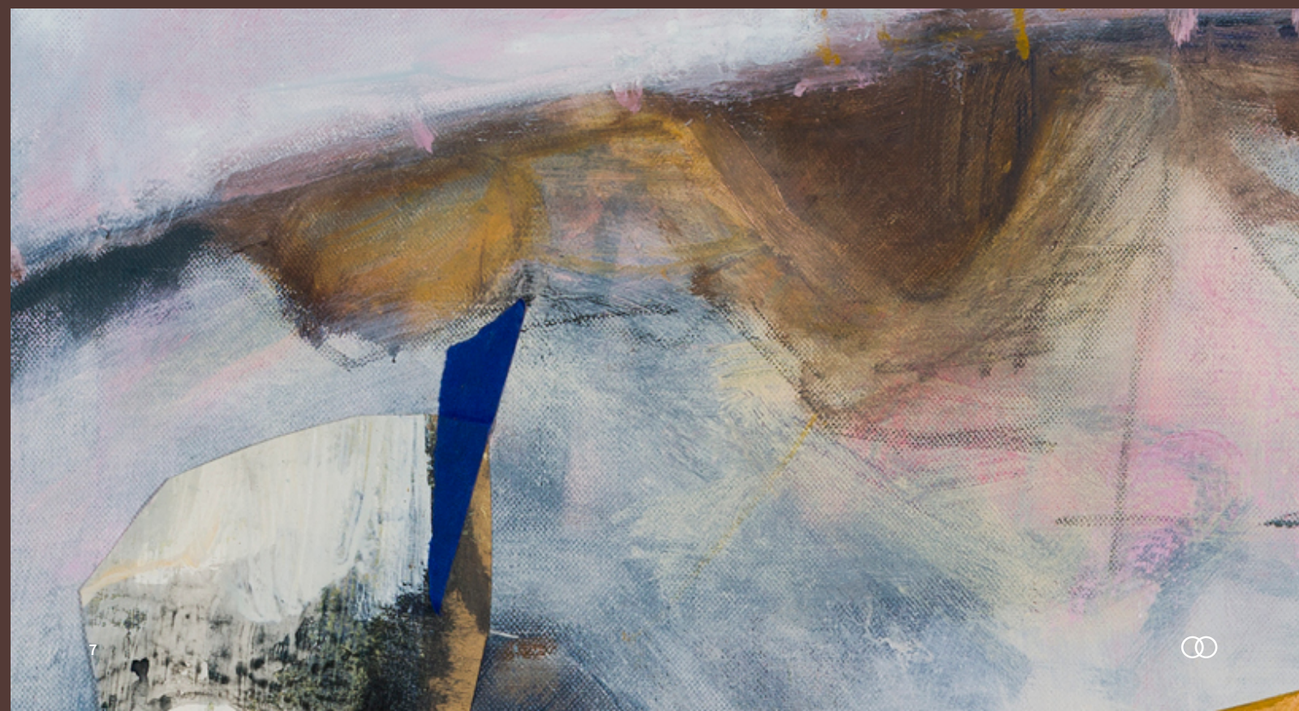
> ***We haven't heard the last on the reverse break fee dance. Our transaction marks first time we've had a fee of that magnitude, and I thin'it opens the door for the more nuanced discussion...***

than the discussion to date, which is on equivalency between the break fee and the reverse fee.

DAVID FRIEDLANDER

Having lived through Pendal - Perpetual, it's absolutely crystal clear that there's no equivalency. As the target you are toast if the bidder walks. I always say this: The bidder is the one who's marched you up the hill. It can't leave you stranded there. 1% isn't going to help you or your shareholders.

One last reflection on Altium, having been on the journey with them. There's nothing like watching a client be consistent and single minded about its strategy - and being clear to the market about its strategy. What that means is that your shareholders will have faith in you when you say no to Autodesk, but also have faith in you when you say yes to a Renesas – that we've partnered with Renesas on number of things as a client. We got to know each other, and we realize that our next stage of growth needs to be together. That's why you can look at this not from a 2023, 2024 perspective, but really as a very successful deal in the whole life of that company.



SHOULD YOU ORDER A BIG MAC, OR A SPECIAL ONE? WHAT THE DATA SAYS ABOUT QUALITATIVE VERSUS QUANTITATIVE MATERIAL ADVERSE CHANGE CLAUSES

Will Heath | Nicola Charlston

If only public M&A worked like a fast food restaurant. You could order a juicy listed entity (with a premium of fries of course) and take delivery within a few minutes after an instant cash transaction. But let's face it, dealmaking on public markets is more like the marathon you need to run after the fast food binge. You need clearance from race officials to join the queue at the starting line, there's a good chance you'll be elbowed by interlopers, and in the 42 kilometres of plodding to the line, what could possibly go wrong?

Given a potential to encounter obstacles along the marathon course for a public M&A deal to reach the finishing line, bidders will typically insist on material adverse change (**MAC**) risk protection. The MAC risk protection mechanism is typically triggered if an event occurs which significantly and detrimentally impacts the target company. It's a break-a-leg moment. Or a cold-feet one, if you're Elon Musk having second thoughts about Twitter.

In negotiating a deal, it can be tempting to take the drive through option. Why jeopardise that bonhomie with the other side through the time-consuming and sometimes difficult hours in the negotiation kitchen to agree upon the right recipe for a MAC? As we'll discuss, it is well worth investing the time and effort required to craft a home-cooked meal deal. Its key benefit is clarity – a vital ingredient to the race nutrition to sustain parties to the contractual finish line.

As deals in 2024 continued to be slowed by increasing regulatory intervention, shareholder and stakeholder activism and uncertain economic and global factors (did someone say US election?), our recent experience on public M&A deals has seen parties focus on MAC clauses. It prompted us to don our chef hats and revisit deal recipe books to analyse the data and guidance on MAC clauses. Here are our kitchen tips.

Qualitative or Quantitative?

First, how is the MAC trigger event defined? 18 months ago after a one-off stoush in the WA Supreme Court,[1] ASIC publicly stated that MAC triggers should contain objective and quantifiable standards which the bidder, target and target shareholders can understand. While ASIC's statement caused some huff and puff speculation about the future of qualitative MACs, it arguably overstated the options available to bidders and targets in framing and negotiating MAC triggers.

1 *Re Vimy Resources Ltd* [2022] WASC 233.

THE DATA SAYS...

We reviewed 34 scheme implementation agreements negotiated and published since ASIC's statement. In brief, here's what we found:

All of the SIDs had a MAC clause[2]

All of the SIDs had a "no MAC" condition precedent (CP)

3 of the SIDs had a 'qualitative only' MAC clause (with the other 31 having quantitative or quantitative and qualitative elements)

13 SIDs had both a quantitative and qualitative MAC clause

6 SIDs had a standalone termination right for the occurrence of a MAC

10 SIDs included a "no MAC" target warranty

16 SIDs (nearly half of the data set) contained a MAC clause that had a qualitative component. Often, the qualitative element is a catch-all and might be defined by reference to the target losing its key assets (think a mining company having its tenements expropriated) or being banned from doing business (lest we mention regulators again!). These schemes were successfully implemented, so it's puffery to say that qualitative MACs can't be drafted in an understandable way. On the other hand, our data set also demonstrated that 'qualitative only' MAC clauses are relatively rare. Parties tend to include a quantitative test in their MAC clause which aids objectivity and certainty. And, in the event of a dispute, a quantitative element will generally be easier to prove.[3]

Which measure?

This leads to a second key point - if the parties are negotiating a quantitative limb to a MAC, should it be focused on balance sheet or P&L impact? The answer is – unsurprisingly – it depends. Some targets don't have stable or sizeable earnings and so a P&L measure may not be appropriate. On the other hand, while balance sheet-based measures work well for diggers, they don't hold up so well for intangibles. And the choice here isn't binary. In certain cases, listed entities have also agreed to MACs based on cash balances and other bespoke quantitative measures.

The third and final point is 'so what?'. While we lawyers could readily write more than 42 kms of paper on MACs, there is a simple point. MACs matter because, if they arise, they can end a public M&A deal. The nuance is how the MAC operates and whether it is an automatic end to a deal or something short of that. Do you really need to negotiate with race officials if you break your leg? Our data shows that there isn't a uniform approach to whether and how MACs feature in condition precedent regimes, termination rights, warranties or other provisions. However, one point is clear. Whatever your MAC ingredients, it is vital the recipe for its use be straightforward and easy for both parties to follow. In M&A and in the kitchen, uncertainty can spell disaster.

2 This data set excludes the recently announced Alcoa/Alumina scheme implementation agreement, which does not have a MAC clause. We are acting for Alumina on the transaction.

3 The argument against quantitative thresholds is that they provide a bright line for ending a deal, in contrast with qualitative measures that can leave wriggle room and "productive opportunities for renegotiation": see the Delaware Court of Chancery's decision in Akorn, Inc. v Fresenius Kabi AG (2018) at 119 (https://courts.delaware.gov/Opinions/Download.aspx?id=279250).

WHAT DOOMSDAY PREPPER AND OPPORTUNIST BOARDS SHOULD BOTH KNOW ABOUT DISTRESS

Jack Hill | Amanda Isouard | Samantha Kinsey

Unless you've been living under a rock, you'll know that commodity prices are in the doldrums and that the outlook in the near term from those in the know is not particularly positive. Combine that with current inflation, interest rate and other cost of living pressures that continue to dominate public discourse and you can understand why many Boards and executives in the resources sector are having some sleepless nights. FY24 is also on track to have more insolvencies than FY23. By December FY24 insolvency activity was up 33.79% on the same time in FY23. But it is not necessarily bad news for everyone, with current market conditions creating the potential for consolidation in various markets through distressed M&A opportunities for those with the capacity to take advantage. This article looks at a couple of key issues to keep in mind if you think you might be a distressed M&A participant.

1

Opportunistic M&A: We expect to see a spate of opportunistic M&A deals during 2024 as corporates look for ways to grow their businesses through acquisitions at discounted prices and divest their non-core assets to help shore up balance sheets. In particular, ASX listed corporates that have been struggling in the current market conditions and trading below market value may be ripe for the taking. If this sounds like the situation you are currently in, now is the time to be engaging with takeover defence advisers so that you are on the front foot should your chairperson get approached by a bidder after market close on a Friday.

2

Insolvency opportunities: Increased insolvencies will also create unique opportunities to acquire desired assets or restructured businesses out of insolvency. Recent transactions (for example, the sale of the Probuild and Clough construction businesses as going concerns) demonstrate how those opportunities can be used to acquire a highly sought after workforce and a workbook of profitable renegotiated contracts.

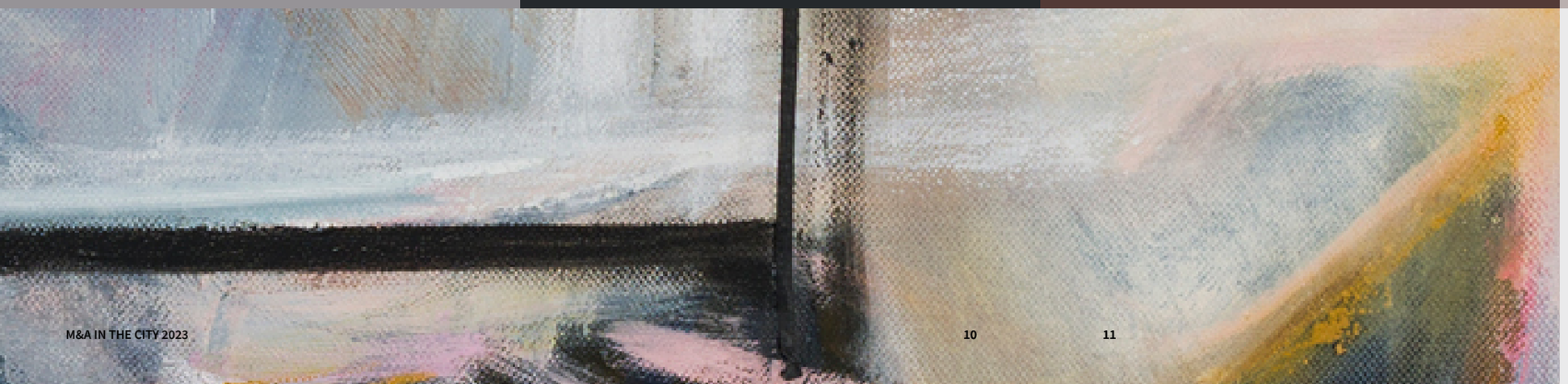
3

Secondary capital market remains open for M&A: While the IPO market is still in hibernation waiting for a big bang to wake from its slumber, secondary capital raisings in the whole are still being well supported by the market, particularly when the funds are being raised to support attractive M&A activity. Since mid-2023 the largest raisings have generally been to fund acquisitions – APA, Orora, Treasury Wines and Metcash to name a few. We expect that trend to continue in the near term.

Although capital raisings are never easy, those being undertaken for acquisition funding throw up some unique issues that boards and executive teams need to navigate, including how to structure your team internally so it has the bandwidth to deal with the both the acquisition and the raising (and their usual day jobs!), how to integrate the acquisition and capital raising due diligence processes, how much information on the target to disclose in the offer documents and what type of comfort you require over that information, how to co-ordinate any wall-crossing of investors with finalisation of the acquisition documentation and what you will do with the funds if the acquisition doesn't proceed. The earlier you start thinking about these and other issues (for example, what type of structure you'll use), the easier you will make it on yourself.

4

Secondary capital market can also be used to support balance sheets: With commodity prices down, debt expensive and the market focussed on leverage, the secondary capital market can also be used by companies as a defensive tool to support their balance sheet and ride out the cycle. These types of raisings give rise to different types of issues – the most important being cost and whether there might be other more attractive alternatives available (e.g. disposal of non-core assets or businesses).



WHETHER PLAYING OFFENCE OR DEFENCE, EARLY PLANNING AND PREPARATION IS KEY TO ENSURE THAT YOU ARE POSITIONED TO ACT QUICKLY WHEN THE OPPORTUNITY OR NEED ARISES. LIKE EVERYTHING, THE MORE DETAILED THE PLANNING, THE BETTER.

THE NOMINEE DIRECTOR - A STAKE-BUILDER'S SECRET SOURCE, OR BOUND TO THE BOARD THEY SERVE?

David Friedlander | Genovieve Lajeunesse

Stake-building is officially back in vogue,[4] with bidders of high conviction using the tool to get their foot in the door and get the ball rolling. Some superannuation funds are already seeking to nominate directors to Boards of listed companies. But what's a shareholder to do once it gets the stake? A US court recently curtailed the infamous activist investor Carl Icahn from using information obtained by his nominee director after a small share raid. It's a timely reminder to shareholders that they can't assume that their nominee directors have an unfettered discretion to share information with them, particularly in the context of a control transaction.

As we already exposed,[5] it is a corporate myth that large shareholders are entitled to a seat on the Board. The next myth to be busted is the idea that if a shareholder does get a nominee director, that director is per se permitted to share information with its nominating shareholder.

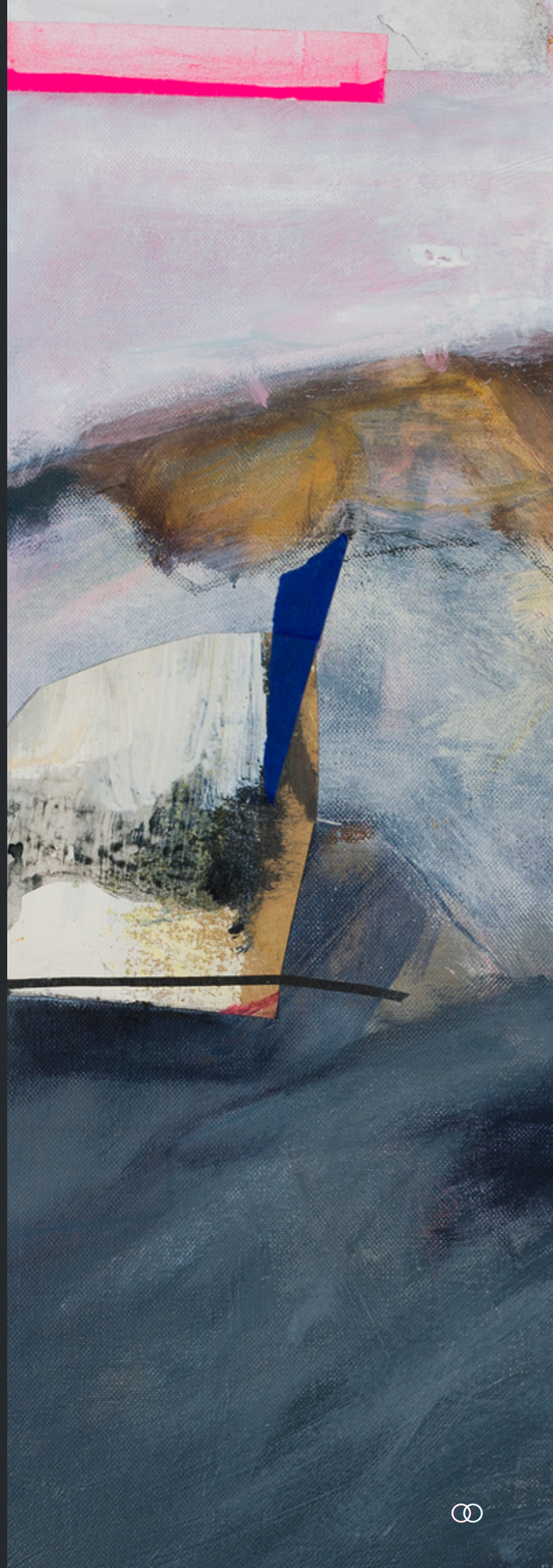
The Wall Street titan Carl Icahn recently faced this issue.[6] Funds controlled by Carl Icahn (Ichan Funds) acquired a small stake in the NASDAQ listed Illumina, and then got a nominee director appointed at the AGM. The nominee director provided the Icahn Funds with confidential and privileged Illumina information which was then used by those funds to bring legal proceedings against certain Illumina directors for a breach of directors duties case. Unsurprisingly, a Delaware Court ruled earlier this year that the Icahn nominee director was not permitted to share confidential and privileged information about Illumina to the Icahn Funds in that manner.

Delaware Courts have in the past permitted nominee directors to share company confidential information with its appointing shareholder – generally where the shareholder has the right to nominate a director (either by contract or through voting power), or where the nominee director serves as a controller or fiduciary of the shareholder (such that the nominee director can't split their brain between their position as nominee director, and controller of the shareholder).

Importantly, no such right exists under Australian law. If an appointing shareholder wants access to company information, it must negotiate the right to do so and cannot expect its nominee director to have an unfettered discretion to share confidential company information.[7]

The Icahn scenario is incredibly unique (i.e. involving information being used for a derivate claim). A more common scenario is the flow of information from a nominee director to a nominating shareholder in circumstances where the shareholder is considering a control transaction. Public companies have navigated this in the past through a conflict-of-interest policy, requiring the nominee director to agree not to share company confidential information to a third party and not to use company confidential information for any purpose other than in discharging their duties as a director (see approach taken by Atlas Arteria in granting IFM a Board nominee).[8]

Of course, this does not mean that stake-building cannot be an effective component in the chemistry of public M&A. Like all matter it has is strengths and weaknesses. But let buyers be aware, you can't expect your nominee director to share inside information with you.



4 https://www.afr.com/chanticleer/how-to-spot-the-next-m-and-a-target-20240205-p5f2cr.
5 https://www.afr.com/companies/financial-services/corporate-myths-that-should-die-by-christmas-20221204-p5c3h1.
6 Icahn Partners LP et al. v. Francis deSouza et al., C.A. No. 2023-1045-PAF; chancerydaily.com/documents/65a7bf4c0280a.
7 See in particular s183(1)(a) of the Corporations Act which prohibits a director from using information to gain an advantage for themselves or somebody else.
8 https://www.atlasarteria.com/stores/_sharedfiles/AGM/2023/ASX_Release_-_2023_AGM_Speeches_-_FINAL.pdf and https://www.atlasarteria.com/stores/_sharedfiles/Corporate_governance/2022/Conflicts_of_Interest_(Directors)_Policy_(ATLAX)_-_December_2022.pdf.

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