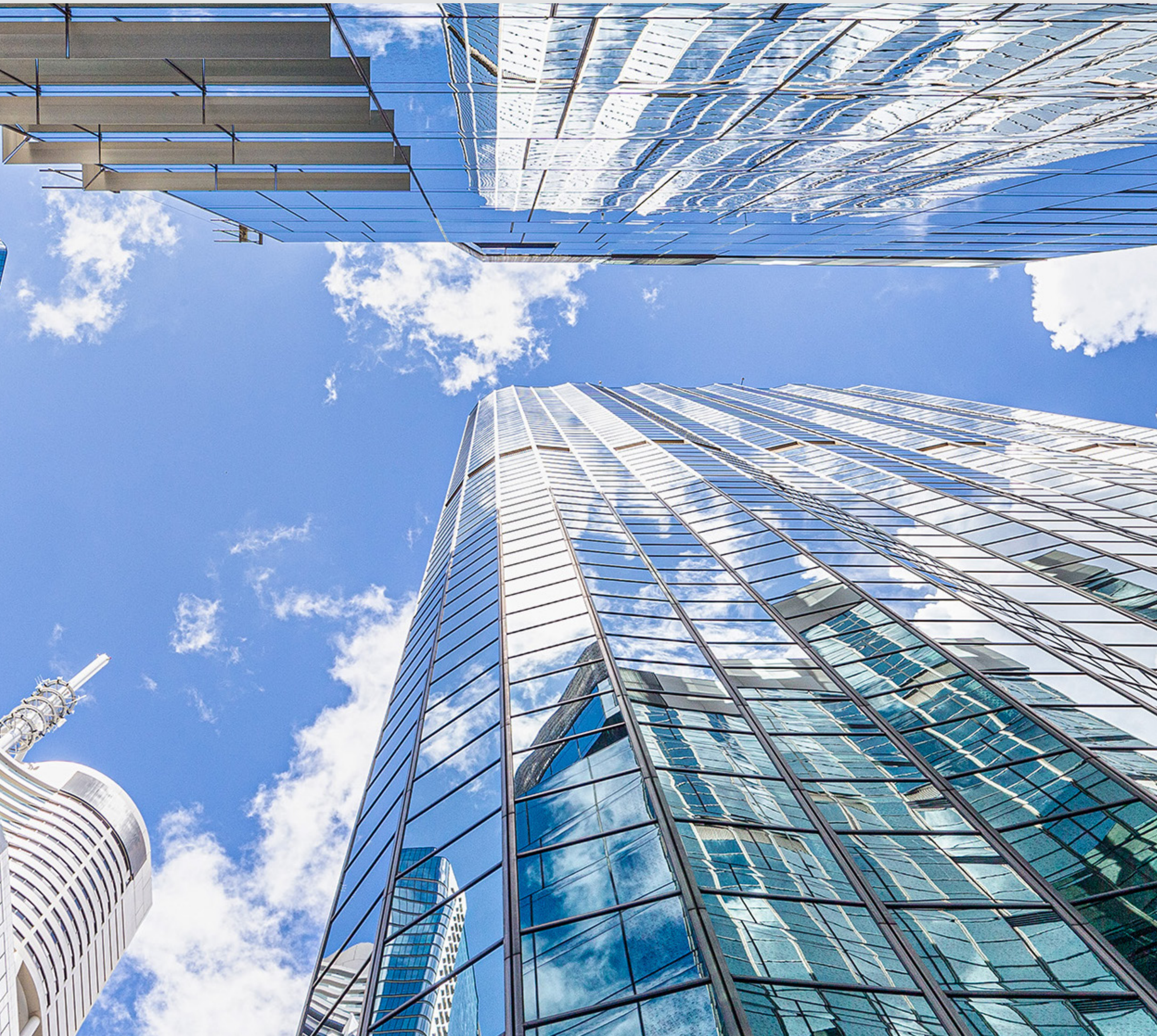
M&A IN THE CITY



WELCOME TO M&A IN THE CITY 2022

If 2021's dealmaking frenzy was driven by cheap funding, active institutional and private capital, companies adapting to environmental, social and governance pressures, and COVID-fuelled shifts in technology… what will set the agenda in 2022?

KWM has identified several key sectors and players likely to define dealmaking in the year ahead - tech & data, ESG and the energy transition, health, the role of super funds and private capital, and Government (it is a Federal election year after all!)

Big economic questions lie ahead. Inflation and the cost of credit will factor prominently in the minds of deal doers, alongside the heightened risk of election-year policy change. But are they enough to dampen the animal spirits?

SUPER FUNDS AND PRIVATE CAPITAL

Sarah Yu & Will Heath

Fuelled by the flow of super money to industry funds and the need to deploy that capital to avoid cash drag, 2021 saw the biggest deals all influenced by super funds – Sydney Airport, Spark Infrastructure, and Vocus to name a few. Acting in consortia, the acquisition appetite was voracious. Private capital sought out the few remaining opportunities.

Where to in 2022? Expect super funds and private capital to remain in the box seat for acquisitions. These funds' cash reserves provide flexibility should credit markets tighten or become more expensive in the face of inflation pressures, and their generally positive reputation means they face lower regulatory and geopolitical risk doing deals.

Where to watch? Funds' investments will not only ride the M&A rollercoaster in Australia but will continue abroad in key sectors including infrastructure, real estate and adjacencies – think infrastructure service businesses, technology services like data centres and registry businesses, and a more sophisticated venture-style approach to fast-growing fields like FinTech.

For private capital, the climate imperative and environmental, social and governance (ESG) pressures will present challenging investment decisions. Decarbonisation requires mid-term capital investment for reducing reliance on traditional energy sources, which will deliver returns through the transition decades and enable sustainable investing impact beyond energy – expect to see more interest in materials and methods able to improve food yields (such as potash). Renewables and emerging energy sources like hydrogen will continue to be prized. Expect competition via consortia and more sale processes akin to the $3bn take private of Tilt Renewables, which had funds involved in a number of competing consortia. And with ESG issues continuing to be top-of-mind for listed companies, we expect super funds to be an active and guiding stakeholder voice.

Finally, as the influence of super funds in both capital and debt markets continues to increase, super trustees should plan for increased regulation and regulatory scrutiny of their governance regimes.

ESG

INCLUDING GOVERNANCE, CLIMATE & ENERGY TRANSITION

Edwina Kwan & Vishal Ahuja

In 2021 we saw increased demand for ESG due diligence by investors and acquirers, especially around climate change, modern slavery and human rights, anti-bribery and corruption, diversity and corporate governance risks. We expect ESG priorities to increasingly dominate the corporate agenda in 2022 and compel growing expectations of enhanced ESG due diligence and corporate compliance frameworks.

As interest groups, shareholders and communities around the world bring more (and novel) climate change actions to court, the key decision-makers (governments and corporations) are going to be challenged in ways that will continue to impact everything from M&A strategies and diligence, to disclosures and decarbonisation plans. Organisations will need to demonstrate they have reasonable grounds to support any representations contained in those disclosures, at the time which those disclosures were made. The questions likely to be put to companies, including directors and boards are what did you know; when did you know it; and, what did you do about it?

Decarbonisation of the Australian economy was a big theme last year with COP 26 in Glasgow and will continue to be a major driver of change in the coming decades. Meeting emission reduction targets set by governments and companies requires action now and there will be a continuation of "Renewables 1.0", including renewable developments, green investments and financing, corporate PPAs, offset acquisitions, planning issues and green strategies, disclosures and marketing. However, this year, we expect an escalation of our current work in "Renewables 2.0" which involves major energy market reforms, renewable energy zones, green litigation, batteries, data and cyber security, electric vehicles, hydrogen and offset projects and offset exchanges. The energy transition will touch all sectors.

DATA & TECH

Anthony Boogert & Kate Creighton-Selvay

Can 2022 match 2021 for tech M&A? We see four key considerations determining the answer.

How resilient will tech companies' valuations be? Investors pushed up share prices for growth-focussed companies in the second half of 2020 and most of 2021, which enabled scrip-based acquisitions such as Block's acquisition of Afterpay (where KWM is advising the acquirer). However, a rocky start to 2022 has left the valuations of many of these companies well down from their previous highs. We may see more cash deals as scrip becomes more expensive acquisition currency.

Tech companies remain attractive targets. COVID-fuelled changes to consumer and business norms will continue to create new markets and opportunities for innovative companies. Entrepreneurs bringing new tech solutions to market will continue to enjoy attractive exit options given the pressure on legacy businesses to deliver growth and the 'dry powder' sitting with Private Equity.

Election-year regulatory attention. Debate over increasing concentration and consolidation within the tech sector will likely mean continued scrutiny from the ACCC for tech deals. Outgoing ACCC Chair Rod Sims' proposed merger control reforms, which call for a tailored merger test for digital platforms and a higher level of scrutiny, cite that narrative. Founders investors etc now await next steps in the reform process under the incoming chair Gina Cass-Gottlieb, who commences in March.

Cross-border deals can also expect the spotlight. FIRB's focus on national security, critical infrastructure and data protection (especially under new Security of Critical Infrastructure legislation which has significantly expanded the number of transactions requiring FIRB approval) will require foreign buyers to navigate the increasing complexity of obtaining FIRB approval for their transaction.

HEALTH

Jason Watts & Nicola Charlston

The combined effects of the pandemic and ongoing developments in the regulatory landscape might suggest volatility, but the Australian health sector continued to see buoyant M&A activity throughout 2021. Health is fast becoming the new "infrastructure". We expect 2022 will see more participation by traditional infrastructure investors in the health sector, as traditional infrastructure opportunities become scarcer and those investors look elsewhere for opportunities for resilient long term returns.

In 2022, we expect this dynamic to keep asset valuations high, while the cumulative impact of COVID, digital transformation and some regulatory uncertainty will provide deal-conducive market conditions. We expect Private Equity's love affair with the health sector to continue, as well as increased activity from industry players investing in adjacencies as they seek growth. As the pandemic abates we expect focus on the aged care sector which - post Royal Commission - faces a greatly increased compliance burden and regulatory uncertainty with ongoing consolidation a likely outcome.

Globally, there is a clear trend towards building capacity to treat lifestyle diseases such as obesity and diabetes (eg CSL's Vifor acquisition), as well as investment in health technology. Expect strategic M&A that delivers exposure to these growth streams and capitalises on consumers' increased willingness to receive remote and digitised care: specifically, opportunities which enable greater personalisation of healthcare and more bespoke health services.

GOVERNMENT

Mark Upfold & Annabel Griffin

Framed by a Federal election, 2022 promises to be an eventful year in the Government sector. Expect the theme of unpredictability to dominate – from COVID variants, their economic and fiscal impacts, and how the Federal and State Governments respond to both.

Regardless of what the virus may have in store, political leaders will seek to offer a 'post pandemic' vision. The challenge for those steering (or seeking to steer) the nation will be fiscal – how to encourage recovery and govern responsibly at the same time, especially in the face of global inflationary pressure.

Achieving the former will require major spending, and innovation in Government's financing and management in a way that is fiscally responsible. This may provide an opportunity for unsolicited proposals, transactions monetising Government assets (such as registries) and public-private partnerships. The NSW Government's successful sale of its remaining 49% stake in Westconnex to Transurban & Sydney Transport Partners (advised by KWM) demonstrates the value Government can create with innovative project thinking. In addition to infrastructure and adjacent services, there will be opportunities in health as States and Territories transition to living with COVID.

LOOKING FORWARD, LOOKING BACK – THOUGHT LEADERSHIP IN 2021

As the saying goes "there's a reason the windscreen is bigger than the rear-view mirror." Eager as we are to look ahead, we also remember that other line – the one about those who fail to learn the lessons of history… So, with that in mind, below is a brief look back at 2021 through the lens of our thought leaders, who shared their perspectives on a few of the more interesting issues, trends and topics in M&A.

Links are to the Australian Financial Review where each piece can be found in full, or please contact us if you are having trouble accessing any piece that interests you.

We began 2021 coming off mute to assess the technological changes to corporate Australia's most enduring piece of pageantry – the AGM. Hybridisation has brought some positive developments, we suggested.

Taking a (virtual) trip abroad, we assessed the SPAC (special purpose acquisition company) phenomenon driving deals in the USA and elsewhere – acknowledging that while Australian markets are certainly different, regulators should consider SPACs' potential benefits for investors and companies seeking to connect capital with opportunity.

Capital raising rules attracted much attention in companies' 2020 fight for survival. In 2021, as many tapped markets for acquisition funding, we made the case for speeding up rights issues in the interests of companies and investors. A period of slower-than-normal snail mail was no reason to delay (and dilute), we argued.

Continuing the regulatory theme, we supported an expanded role for the Takeovers Panel in vetting schemes of arrangement. A structure by which around half of Australia's takeovers are done, schemes would be more consistent and efficient under the panel's jurisdiction, we suggested.

Casting a thoughtful eye into the ESG world (with the benefit of KWM research on the climate disclosures of Australia's biggest listed companies) led us to conclude that public pressure to go 'net zero' was creating litigation and reputation risk – anything less than a fully formed plan would surely be met with accusations of greenwashing.

By mid-year, and with the M&A boom in full swing, we took a history lesson to (attempt) an answer to the grandest question – just how long might the seventh great M&A wave last?

The level of activity has prompted interesting questions – ought companies immediately disclose a takeover offer? We argued they should not, concluding as a UK panel did that distortionary impacts outweighed any transparency gains.

The annual **M&A Conference**, hosted jointly by KWM, HSF and Allens brought together keen minds on topics of universal interest – a global lens on the boom's likely longevity, the factors turning superfunds into takeover titans, and the critical importance of an 'open for business' stance on foreign investment.

Amid political debate on investor protection, determining who ought be deemed 'sophisticated' enough to assess riskier financial products was more complex than a dollar threshold, we reasoned. And on that same theme, we shared some suggestions on how to reform Australia's confusing patchwork of rules on when a company needs to issue a prospectus.

And kicking off early in 2022, we suggest **innovation in M&A** will help determine how long this boom lasts.

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