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Foreign Buyers are a Boon to U.S. M&A

By Sheon Karol, The DAK Group

The United States is the world's number one investment destination. Foreign direct investment in the U.S. reached a record $348 billion in 2015.

We predict the appetite for U.S. acquisitions will continue to grow in 2017 and beyond. According to a recent Baker & McKenzie report, cross-border M&A made up 44% of all deal value and 34% of all U.S. deal volume in Q3 2016, compared to 41% and 36% for the same period in 2015.

This experience is reflected across the board, both in mega-deals and in middle market M&A. In our own practice at The DAK Group we have seen the percentage of middle market M&A deals with foreign purchasers grow from 10% in 2010 to 50% in 2015.

(Although some anticipate the incoming presidential administration will introduce policies that may engender higher interest rates, the increases after the initial period are not expected to be significant as Congress is likely to limit stimulus plans. In addition, M&A activity historically has increased after a period of uncertainty during U.S. presidential elections.)

Increased cross-border M&A isn't just good for buyers — it's also a boon for sellers. American business owners can benefit in a variety of ways from considering a sale to foreign companies. At the simplest level, selling prices increase when there are more bidders. In addition, due to the geographic distance from their foreign headquarters, overseas buyers may retain more employees than domestic acquirers.

Access to foreign markets is another advantage, as is the introduction of new management practices and/or technical processes.

Where Will Foreign Acquirers Come From?

We predict both emerging and advanced economics will continue to pursue U.S. acquisitions.

Eurozone: Structural elements of the developed world's economies encourage M&A activity in the U.S. The developed economies have low-cost capital and need outlets for growth. The primary source of inbound investment, the Eurozone, is expected to experience continued low-growth. The Baker & McKenzie report reflects that in Q3 2016 deals from the European Union into North America reached record values of $105bn. This was an increase of 32% over Q3 2015.

China: Chinese companies have been voracious in seeking cross-border acquisitions. The slowing of the Chinese economy will encourage this trend as the companies seek new markets. Foreign acquisitions are also part of the Chinese government's geo-political goals. The Wall Street Journal has recently reported that outbound Chinese investment has accelerated so dramatically that governmental controls are planned to limit the outflow. However, according to the report, the Chinese government's focus will be on "extra-large" foreign acquisitions.

Emerging markets: Although most foreign acquirers of U.S. businesses will come from the advanced economies, we predict an increasing number will also come from emerging markets. McKinsey has found that more emerging-market companies have begun using M&A to tap into new markets. These acquirers are no longer only seeking strategic and natural resources but are looking to penetrate new markets just like multinationals in developed markets do.

We expect emerging market companies to continue internationalizing their holdings in order to reduce business exposure to relatively small economies and often unstable political conditions.

For example, South Korea's direct foreign investment in the U.S. has more than doubled from $17 billion in 2010 to $38 billion in 2015. Liberalization in emerging markets countries is also encouraging companies to engage in cross-border M&A.

Tips for Sellers

1. **Cast a wide net**: Large companies benefit from specialized professionals who provide access to foreign buyers and transactional expertise. Similarly, the middle market seller should develop relationships with professionals who specialize in middle market transactions and have this access. The seller should engage professionals who have access to European companies, but who also look beyond the Eurozone for other sources of potential buyers.

2. **Emphasize preparation**: Professionals for the seller and buyer must review tax structures and accounting standards earlier in the process to account for any nuances specific to cross-border M&A.

3. **Develop a legal strategy**: Foreign buyers often fear the litigation-oriented U.S. business environment, so a strategy for existing and potential litigation that provides comfort should be furnished.

4. **Create a retention plan**: A coherent and convincing approach for retention of key employees should be provided as the operations and management of foreign buyers are geographically distant.

5. **Be sensitive to cultural concerns**: Don't underestimate cultural differences. Be sensitive to the financial and cultural concerns of buyers from countries with a shorter track record of U.S. acquisitions.

Overall, as the presence of foreign buyers increases in U.S. M&A, business owners should proactively include them in the sale process. However, be sure to engage an investment banker or M&A advisor to help — working successfully with foreign buyers requires nuance and skill that is difficult to obtain without dedicated transaction experience.

***Sheon Karol** is a managing director of The DAK Group, an investment bank specializing in middle-market, privately-held companies, advising business owners on sell-side and buy-side transactions, financial restructuring, capital advisory and valuations & fairness opinions.*

Email Sheon at skarol@dakgroup.com.