

# U.S. Mergers & Acquisitions Q3 2018 Quarterly Insights

December 2018

## Executive Summary

This report, created by the BMO Capital Markets Mergers & Acquisitions team, provides an update on selected key trends that we are observing in the cross-border M&A market.



### Cameron M. Hewes

Managing Director  
Mergers & Acquisitions

*“We expect that U.S. M&A will continue to see robust activity due to the strong economy and readily available capital, but buyers will more likely than not be U.S.–based as long as international headwinds remain.”*

***With this year shaping up to have the smallest transaction volume for international buyers of U.S. businesses since 2013, should we be concerned about the international M&A market going forward?***

As we talk with our U.S. clients who are considering potential sale transactions, we are consistently asked about the likelihood that international buyers will be involved in their M&A processes, driven by hopes of market-topping multiples coming from overseas buyers. This is despite the fact that over the last five years U.S. buyers have accounted for over 73% of U.S. M&A transaction value, over 76% of U.S. M&A transaction volume, and have historically valued companies at a premium to international buyers.

While the overall M&A market in the U.S. continues to benefit from numerous tailwinds, international buyers have faced several headwinds leading to their decreased involvement in U.S. M&A over the past two years. Trade wars, stock market volatility, an expanded CFIUS regime, robust purchase multiples paid by domestic acquirers and the strength of the dollar have combined to dramatically slow international interest in U.S. companies. In the first nine months of 2018, international buyers have invested \$18 billion in U.S. targets, down approximately 28% from the same period last year. European buyers have been the most active, representing approximately 46% of international YTD transaction value. We expect that U.S. M&A will continue to see robust activity due to the strong economy and readily available capital, but buyers will more likely than not be U.S.–based as long as these international headwinds remain.

We look forward to your reactions to the BMO M&A team’s thoughts and analysis of market trends in the enclosed report.

# Q3 YTD 2018 U.S. Target Cross-Border M&A

**(37%)**

YTD decline in transaction value from Asian buyers

**\$105**

Billion YTD in U.S. middle market M&A transaction value

**(2.9x)**

EV/EBITDA decline YoY that all strategic buyers are paying for U.S. targets

**135**

Days it can take to complete the CFIUS review process

**(28%)**

Decline YTD in International M&A transaction value

**10.6x**

YTD EV/EBITDA purchase price multiple for total U.S. middle market M&A

**4**

U.S. M&A transactions completed by Canadian buyers YTD, down from 6 in the same period in 2017

**6**

U.S. M&A transactions completed by European buyers YTD, equal to the same period in 2017

**37%**

YTD U.S. M&A transactions occurring in the Industrial sector

**(\$7)**

Billion decline in international transaction value YTD

**9.9x**

EV/EBITDA multiple international buyers are paying for U.S. targets YTD

**45%**

Increase in CFIUS Notice filings from 2016 – 2017<sup>(1)</sup>

Note: YTD in this document is defined as through September 30, 2018. Middle Market M&A is defined as transactions with enterprise values between \$100 million and \$5 billion

1. U.S. Department of the Treasury and Wilson Sonsini Goodrich & Rosati

## Q3 2018 – Key Themes

*Despite U.S. tax reform and plentiful capital, U.S. target cross-border M&A slowed in 2018 as fears over trade wars, tariffs and an expanded CFIUS regime have given dealmakers pause*

### Q3 Tailwinds

#### Tax Reform / Plentiful Capital

- **Tax Reform:** Has caused an increase in corporate profits in 2018
  - Reduction in corporate tax rates to 21.0% has positively stimulated corporate profits
  - Plentiful corporate cash balances primed to be deployed via M&A
- **Repatriation of Cash:** Positive tax law implications allow cash to be returned from abroad and deployed domestically

#### Strong U.S. Economy

- **Strong GDP Growth:** Real GDP increased 3.5% from Q2 to Q3 2018
  - Despite a slight deceleration in growth compared to Q2's peak of 4.2% growth, Q3 GDP still grew faster than it has in prior years
- **Unemployment at 49-Year Low:** The strong U.S. economy has reduced unemployment to 3.7% and increased wages for employees
- **Low Inflation:** The price index for gross domestic purchases increased only 1.7% YTD compared to a 2.2% increase in Q3 2017

### Q3 Headwinds

#### Protectionism

- **CFIUS:** FIRMMA<sup>(1)</sup> amendment will significantly impact cross-border M&A of U.S. targets
  - CFIUS caused delays to Broadcom's acquisition of Qualcomm, which was eventually blocked by President Trump in March 2018
- **Brexit:** If the deal agreed to by EU leaders and PM May isn't ratified by parliament, European trade wars and further reduction in global M&A may continue

#### Trade Wars & Tariffs

- **NAFTA:** Uncertainty around NAFTA and implementation of USMCA will continue to drive change across various industries in the marketplace
- **Trade War with China:** Steel and aluminum tariffs imposed on foreign imports set in motion a slew of retaliatory tariffs from China
  - Affected industries include food & beverage, aerospace, energy, automotive, technology, agriculture and finance

#### Interest Rates & Market Fluxes

- **Rising Interest Rates:** Fed Funds Rate increased from 1.1% in Q3 2017 to 2.2% in Q3 2018. The Fed has indicated plans to raise rates to 3.1% by the end of 2019
- **Market Volatility:** Volatility in U.S. equity markets have slowed M&A investments YTD
- **Strong U.S. Dollar:** Q3 2018 U.S. Dollar Index is at 16-month high and up 5.5% YoY

Source: Factset, Macrotrends, U.S. Bureau of Economic Analysis

1. On August 13, 2018, President Trump signed into law the Foreign Investment Risk Review Modernization Act of 2018 (FIRRMA) to help mitigate national security threats

# Spotlight on CFIUS

**CFIUS gains expanded power over foreign investments with procedural changes taking effect that have serious implications for U.S. target cross-border M&A**

## What is CFIUS?

- The Committee on Foreign Investment in the United States (“CFIUS”) was formed by President Ford in 1975 to review foreign investments in U.S. businesses for potential national security concerns
- In 2007, Congress passed the Foreign Investment and National Security Act (FINSA), which broadened the definition of "national security" for CFIUS review
- CFIUS has authority to approve pending transactions, require national security risk mitigation or recommend the President block them
- New legislation in 2018 requires Declaration filing to precede Notice filing; mandatory for “critical” industries

## New CFIUS Regulations Implemented in Q3 2018

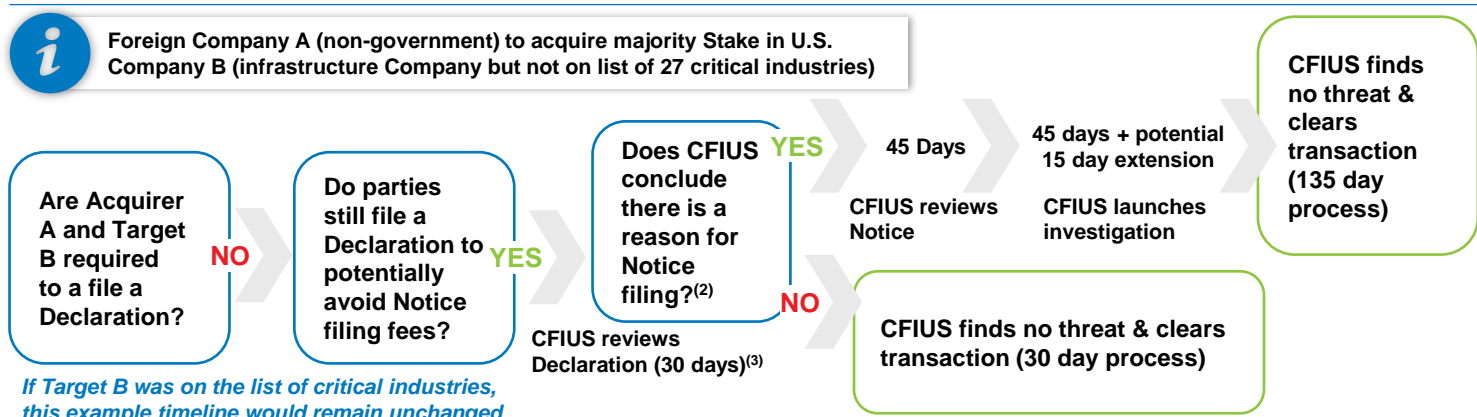
- On August 13, 2018, President Trump signed into law the Foreign Investment Risk Review Modernization Act of 2018 (FIRRMA) to help mitigate national security threats
- Key changes to the CFIUS review process due to FIRRMA:
  - **Expansion of CFIUS jurisdiction, including non-controlling investments** and real estate
  - Specific carve-outs for private equity funds with foreign investors
  - **Introduction of Declarations** (abbreviated, 5-page filings)
  - As of November 10, 2018, **Declarations are mandatory for transactions involving U.S. targets in 27 “critical” industries** such as technology, infrastructure, and defense
  - Penalties for failure to file are severe
  - **Extension of the CFIUS timeline for filing a Notice from 30 days to 45 days** before a transaction closes (Notice filing is still voluntary)
  - Addition of Notice filing fee up to \$300,000
  - Grant of authority for CFIUS to suspend transactions
  - Implementation of a new export control regime

## Impact of CFIUS on M&A<sup>(1)</sup>

Year	Number of Notices	Number Investigated	President Decision to Block	Notices Rejected	Notices Withdrawn / Abandoned
2014	147	51	0	1	12/2
2015	143	66	0	1	13/3
2016	172	79	1	0	27/5

~250 Notices were filed in 2017, an increase of 45% over 2016; further increasing delays in the approval process<sup>(2)</sup>

## CFIUS Review Process Timeline<sup>(1)</sup>:



Source: Harvard Law Review, U.S. Department of the Treasury, WSGR White Paper “CFIUS in 2017: A Momentous Year”

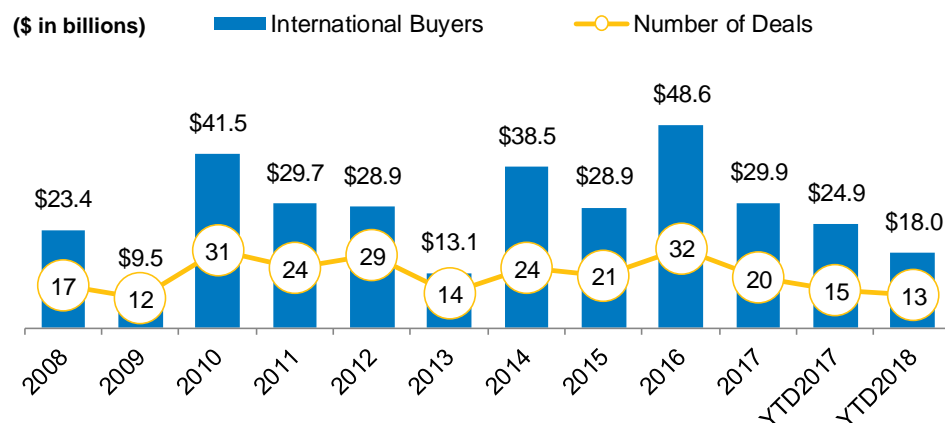
1. U.S. Department of the Treasury  
 2. Wilson Sonsini Goodrich & Rosati  
 3. Upon receipt of a declaration, CFIUS will have 30 days to review and may conclude by: (1) requesting the parties file a joint voluntary notice; (2) initiating a unilateral review of the transaction; (3) informing the parties that it is unable to take action based on the declaration alone; or (4) informing the parties that there are no unresolved national security concerns and CFIUS has completed its review of the transaction

# U.S. Target Cross-Border Middle Market M&A

**International acquisitions of U.S. targets has slowed dramatically in the first nine months of 2018, with the number and dollar value of such acquisitions declining by 13% and 28%, respectively**

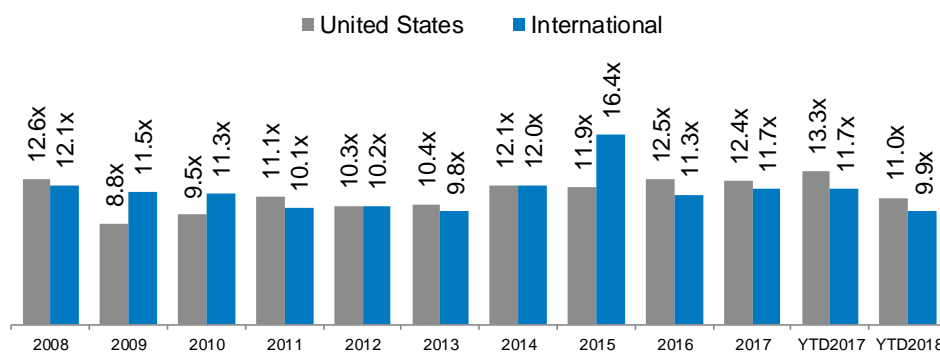
International buyer involvement in U.S. middle market M&A continues to soften from its peak in 2016 as international buyers face increasing challenges to invest in the U.S.

Number and \$ Value of International Middle Market M&A of U.S. Targets



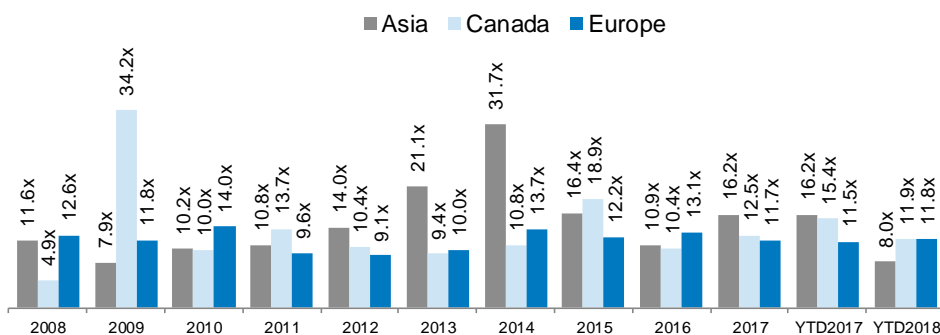
While international buyers are actively looking to make middle market acquisitions in the U.S., U.S. buyers have paid an average 1.0x premium as compared to international buyers over the last three years.

Median EV/EBITDA Multiples Paid by International vs. U.S. Buyers



Asian acquisition multiples of U.S. companies decreased dramatically this year and are at their lowest levels since 2009.

Median EV/EBITDA Multiples Paid By International Buyers



Source: FactSet

Note: Data includes all public and private announced and closed deals with U.S. targets with enterprise values between \$100 million and \$5 billion and EV/EBITDA multiples between 3x - 40x



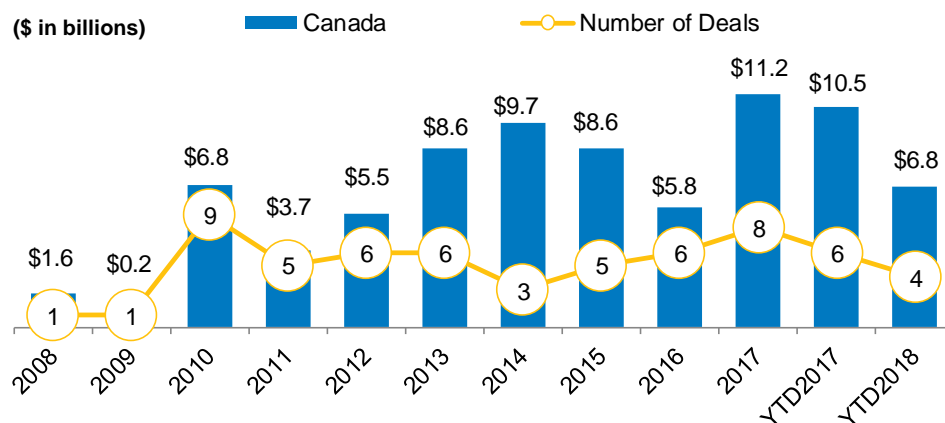
# U.S. Target Cross-Border Middle Market M&A

**Tariffs and increased CFIUS scrutiny have reduced the quantity of M&A transactions from Canada, Asia, and Europe as compared to 2017**

## Canadian Buyers

NAFTA negotiations and political turmoil with the U.S. have impacted the amount of cross-border transactions completed YTD, reducing the value of transactions by over 35% YoY.

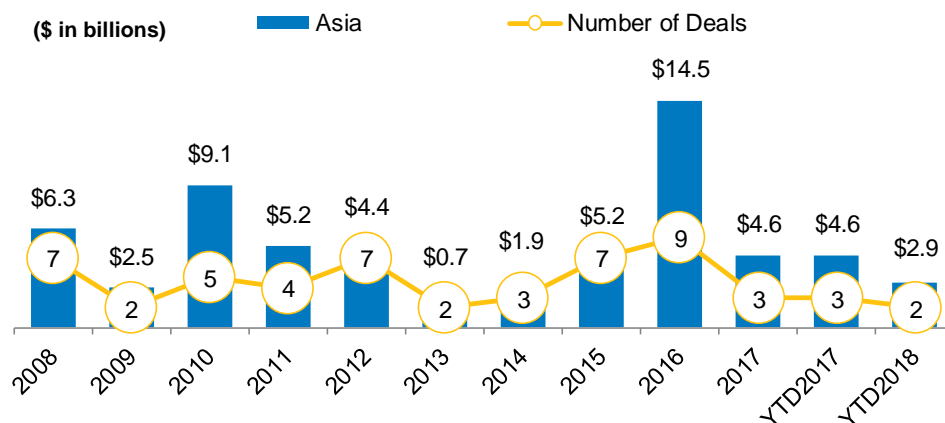
**Number and \$ Value of Canadian Transactions with U.S. Targets**



## Asian Buyers

The number of M&A transactions between an Asian buyer and a U.S. target declined by 67% in 2017 and continues to soften in 2018. YTD value of transactions have declined by over 36%.

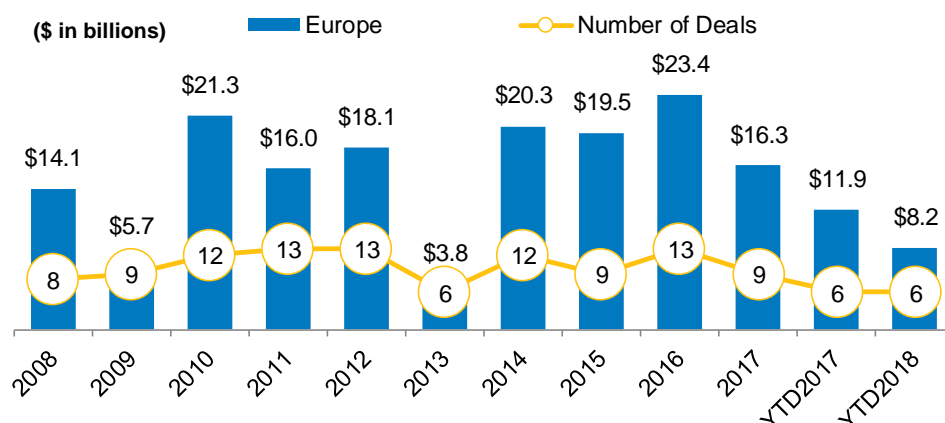
**Number and \$ Value of Asian Transactions with U.S. Targets**



## European Buyers

European buyers have averaged ~10 U.S. transactions per year since 2014, investing over \$87 billion in U.S. companies. YTD value of transactions have declined by over 31%.

**Number and \$ Value of European Transactions with U.S. Targets**



Source: FactSet

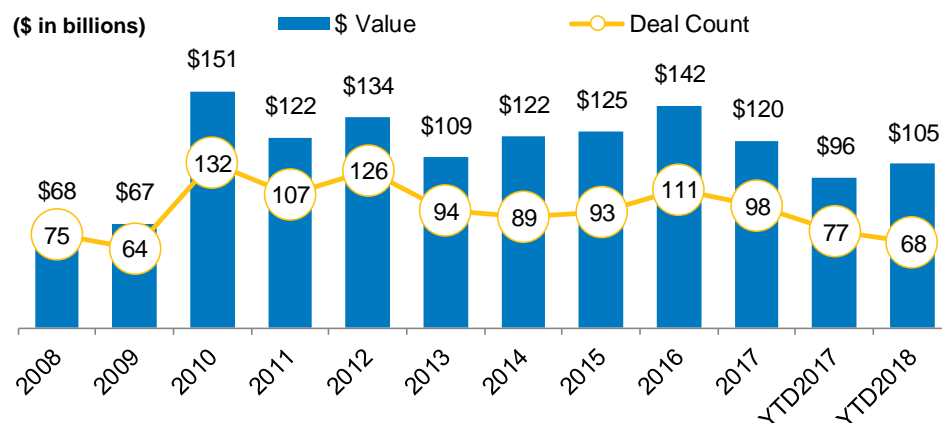
Note: Data includes all public and private announced and closed deals with U.S. targets with enterprise values between \$100 million and \$5 billion and EV/EBITDA multiples between 3x - 40x

# U.S. Target Total Middle Market M&A

**Middle market M&A in the U.S. continues to be active, but slightly down YTD, with 68 transactions and \$105 billion transaction value as of Q3 YTD 2018**

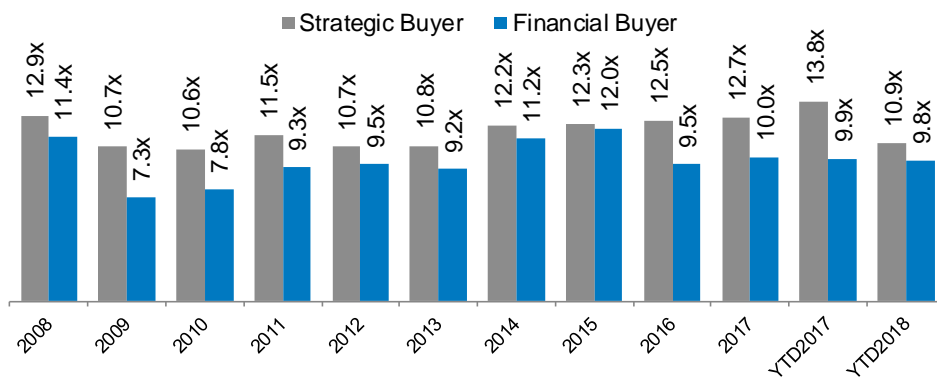
U.S. middle market M&A market is trending up YoY in total transaction value, but has seen fewer transactions, driven partially by lower cross-border M&A activity.

**Number and \$ Value of Announced and Closed Transactions for U.S. Targets**



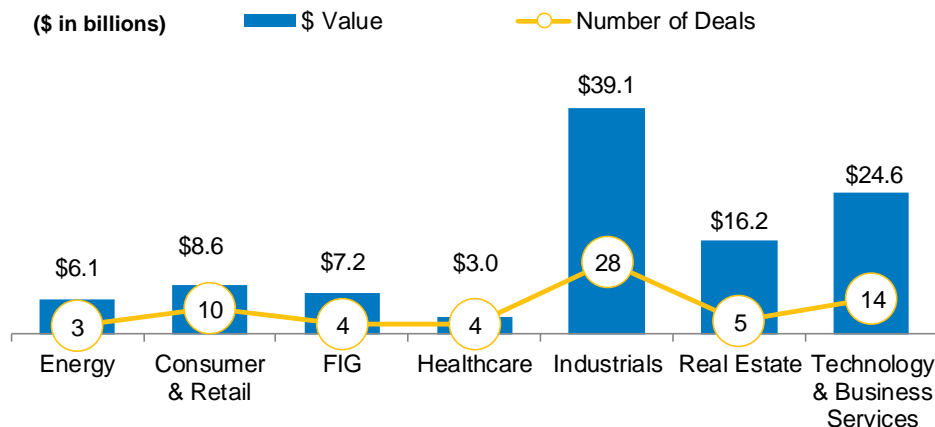
Strategic buyers have completed approximately four times as many transactions as financial buyers YTD, equating to 83% of the U.S. transaction value.

**EV/EBITDA Paid by Strategic and Financial Buyers**



Industrials and Technology & Business Services M&A continue to experience strong momentum, and represent over 60% of U.S. transaction value YTD.

**YTD 2018 M&A \$ Value by Sector for U.S. Targets**



Source: FactSet

Note: Data includes all public and private announced and closed deals with U.S. targets with enterprise values between \$100 million and \$5 billion and EV/EBITDA multiples between 3x – 40x



# About Us: BMO Capital Markets

- As a member of BMO Financial Group (NYSE, TSX: BMO), we leverage the financial strength and capabilities of one of North America’s leading financial services organizations
- BMO Capital Markets is a single-stop provider. Depending on your needs, you may use a combination of our capabilities, or only one. Our experience and deep sector knowledge enable us to develop the solution that fits you best



## We offer a complete suite of products and services:

### Access to Capital

- Initial public offerings
- Debt financing
- Equity financing
- Private equity financing
- Corporate lending
- Structured & project financing
- Securitization

### Distribution

- Institutional
  - Equity sales & trading
  - Fixed income sales & trading
- Retail
  - Direct brokerage
  - Private banking

### Strategy & Growth

- Strategic advisory
- Mergers & acquisitions, including cross-border opportunities
- Valuations & fairness opinions
- Acquisition & divestitures
- Leverage buyouts
- Restructurings & recapitalizations
- Take-over & activism defense
- Share buybacks
- Joint ventures and other partnership models

### Treasury & Risk Management

- Commodity products
- Money markets
- Trade finance
- Cash management
- Foreign exchange

### Research

- Economics
- Commodities
- Debt
- Corporate

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	<b>Asia &amp; Australia</b>	Beijing Guangzhou Hong Kong Melbourne Mumbai Shanghai Singapore Taipei		
		<b>2,500+</b> professionals	<b>30</b> locations	<b>5</b> continents

Note: As of September 30, 2018.

# BMO M&A Overview and Recent Highlights

## Experienced Team

- Global M&A practice with ~115 M&A professionals in nine offices around the world, with ~85 M&A professionals in the U.S.
- Including over 40 Managing Directors and Directors

## Full Product Capabilities

- Sell-side, buy-side and cross-border advisory
- Recapitalizations and restructurings
- Fairness opinions
- Takeover defense
- Activism defense
- Leveraged and management buyouts
- Strategic alternatives review

## Proven Results

- U.S.\$353 billion of transaction value in 500+ deals since 2011

## Approach

- Deep sector expertise in close alignment with BMO's industry groups
- M&A professionals partner with industry experts to drive enhanced insights and execution
- Dedicated capabilities in both large cap and middle market M&A advisory and financing

## Q3 2018 Cross-Border M&A Transactions

**Loblaw Companies Limited**

**C\$5.2 billion**

Advisor on Spin Out of 62% interest in **Choice Properties Real Estate Investment Trust** to **George Weston**

**Exclusive Financial Advisor**  
September 2018

ASSOCIATION MÉDICALE CANADIENNE | CANADIAN MEDICAL ASSOCIATION

**C\$2.585 billion**

Sale of

**MD**

MD Financial Management CMAA Corporation

to

**Scotiabank**

**Exclusive Financial Advisor**  
September 2018

**sonobello**  
BODY CONTOUR CENTERS

Dividend Recapitalization by **Alaris Royalty**

**Financial Advisor**  
September 2018

**FINASTRA**

(Formerly D+H Corp – DH:TSX)

Portfolio Company of **VISTA**  
EQUITY PARTNERS

Sale of **D+H Collateral Management Services** business to

**TERANET**  
Portfolio Company of **OMERS**

**Financial Advisor**  
July 2018

## Select Recent M&A Transactions

**QEP RESOURCES**

**U.S.\$1.7 billion**

Sale of Williston Assets to

**VANTAGE ENERGY**

**Exclusive Financial Advisor**  
Pending

**CoreLogic**

**C\$128 million**

Acquisition of

**SYMBILITY**

**Exclusive Financial Advisor**  
Pending

**Ricker's**

Sale to

**GIANT EAGLE**

**Exclusive Financial Advisor**  
Pending

**AMERICAN SECURITIES**

Acquisition of

**CPh**

Portfolio Company of **Gilbert Global Equity Partners**

**Exclusive Financial Advisor**  
November 2018

**INSTITUTE FOR INTEGRATIVE NUTRITION**

Sale to

**NEP**

Norwest Equity Partners

**Exclusive Financial Advisor**  
October 2018

**ELITE BODY SCULPTURE**

Recapitalization by

**VESEY STREET CAPITAL PARTNERS** and **BURCH CREATIVE CAPITAL**

**Exclusive Financial Advisor**  
October 2018

**SFG SPECIALTY FOODS GROUP, LLC**

Sale to **INDIANA PACKERS**

Subsidiary of **Mitsubishi Corporation**

**Exclusive Financial Advisor**  
October 2018

**Basic Fun!**

Has sold a minority interest to

**FALCON**

**Financial Advisor**  
August 2018

**SEARCHLIGHT**

**\$2.1 billion**

Acquisition of

**Mitel**

**Financial Advisor**  
July 2018

**PROXIMAGEN**

**\$370 million**

Sale of the rights to U.S.L261 to

**ucb**

**Financial Advisor**  
June 2018

Source: Bloomberg, completed deals where an acquirer or target is located in North America. Data as of October, 2018.

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