Hogan Lovells

POLITECNICO MILANO 1863

SCHOOL OF MANAGEMENT

Italy inbound: look no further

Foreign direct investments in Italy

Research highlights
November 2017

Introduction

As a global law firm with Italian roots, we have a keen interest in the appetite of international buyers for cross-border M&A involving businesses in the peninsula. Christine Lagarde, head of the International Monetary Fund, recently observed that the global economy is enjoying its best growth spurt since the start of the decade, as the long-awaited global recovery takes root. From our vantage point, steady growth in cross-border mergers and acquisitions seems to have played a significant role in Italy's recent economic recovery, as global corporations and financial investors seek to benefit from Italian excellence in a broad range of industry sectors.

The businesses which are the targets of such attention are often small to medium-sized enterprises, a tenacious cornerstone of the Italian economy. These companies have encountered considerable difficulties in the aftermath of the global financial meltdown of 2008: the lengthy banking crisis has served to limit their access to finance, severely testing the resilience of Italian entrepreneurs, whose businesses have also faced increasing competition from emerging markets and heavier regulation, as well as the tightening of sanctions affecting traditional export destinations such as Russia.

As part of our focus on understanding the dynamics of foreign direct investment in Italy, we commissioned the Politecnico of Milan to conduct a unique study, combining a quantitative analysis of cross border M&A over the last four years and a survey of a sample of top managers in Italian companies recently acquired by overseas investors to obtain a qualitative insight into the impact of foreign investment on their businesses. The study focusses on small to medium-sized businesses with a turnover of between Euro 50 million and Euro 500 million, given the importance of this sector to the Italian economy and the opportunities which this sector offers for strategic and financial investors.

The research confirms that Italian businesses have continued to attract foreign investment, with the number of cross-border deals increasing over the period studied. The Italian market-place offers a healthy range of attractive Italian targets, particularly those operating in the manufacturing sector, stimulating the interest of investors from many jurisdictions, with Italy's traditional trading partners – the United States, the United Kingdom and France – heading the list.

Strategic and financial buyers are competing, neck and neck, to secure investment opportunities, with greater access to acquisition finance following the steps taken to seek resolution of the banking crisis. The study shows that the multiples that buyers are willing to pay to secure their stakes in Italian companies are far from modest, and serve to underline investor confidence in businesses "Made in Italy". The survey illustrates that these cross-border deals are capable of satisfying foreign buyers' strategic demands while addressing the sellers' need for succession planning to protect business value and future growth.

This report provides illuminating insights into the phenomenon of cross-border M&A in Italy over recent years and offers a key to interpreting its future development, as increasing numbers of Italian businesses attract the interest of foreign investors.

So look no further: Italy inbound is the key.

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Methodology

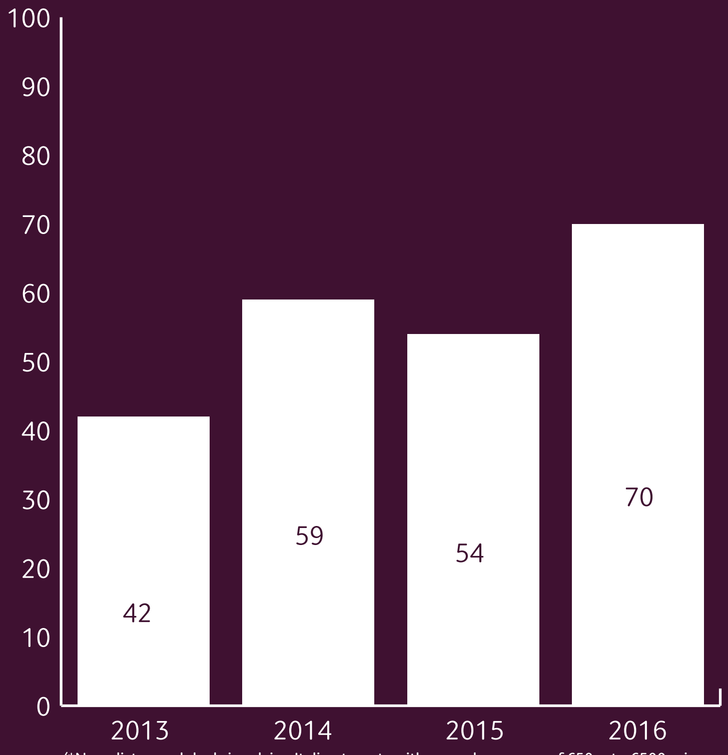
Hogan Lovells commissioned the Politecnico of Milan to conduct research into M&A transactions involving Italian target companies with annual revenues of between €50m and €500m and one or more one overseas acquirer. The research, which analyses deals completed over a four year period, from 2013 through 2016, draws on data from official sources, financial providers and specialised databases.

To ensure that the research reflected Italy's underlying economic dynamics, and was not distorted by localized or specific adverse factors, deals involving targets in financial distress or insolvency proceedings were excluded. Acquisitions of asset portfolios (including real estate, power stations and loans) were also ignored for the purposes of this study, as were deals that were funded solely by Italian investors.

The resulting sample for analysis comprised 225 transactions including Italian targets, each of which saw a foreign investor acquire a stake in the company, or increase its existing interest.

The Politecnico also conducted a survey of a sample of top managers in Italian companies which had experienced recent foreign investment, and undertook in-depth interviews with selected targets, to obtain a qualitative reaction regarding the impact of foreign investment on the target businesses.

Volume of cross-border M&A involving Italian targets increased by 67% over period



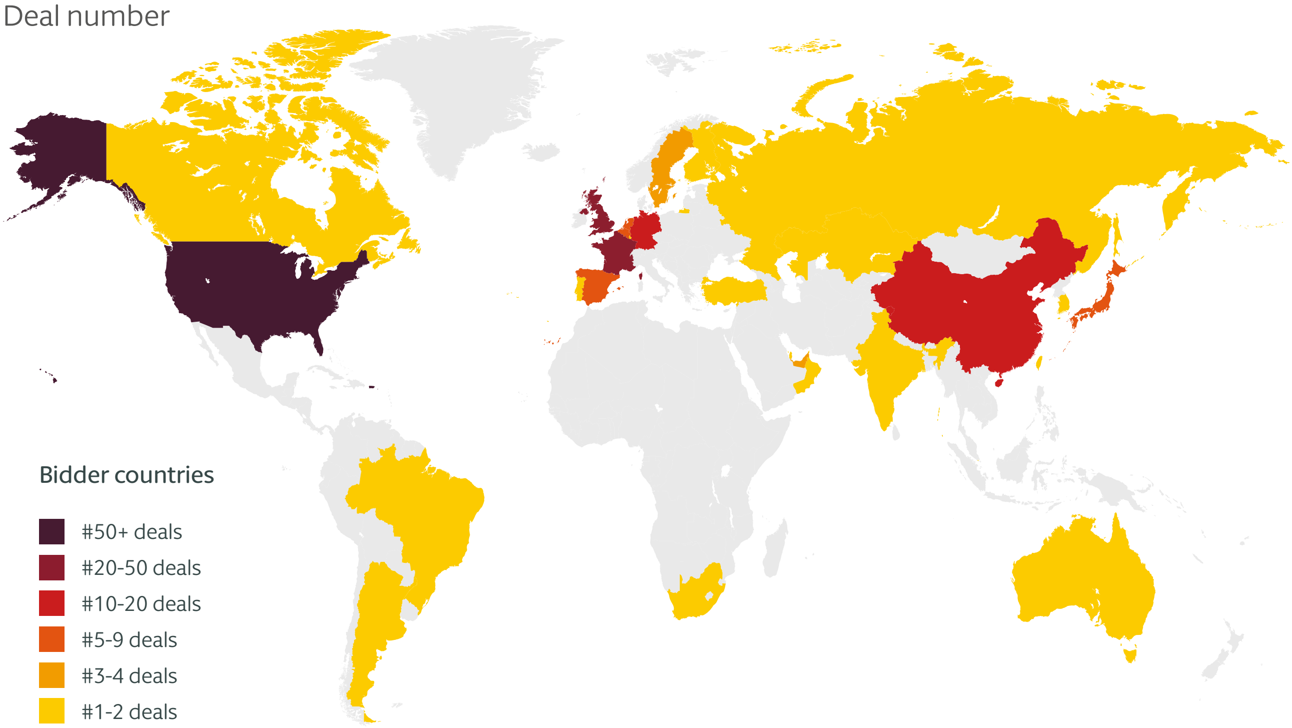
(*Non-distressed deals involving Italian targets with annual revenues of €50m to €500m in 2013 through 2016)

The study shows that the volume of completed cross-border M&A deals involving Italian targets increased by 67% over the four-year period, from 42 in 2013 to 70 in 2016.

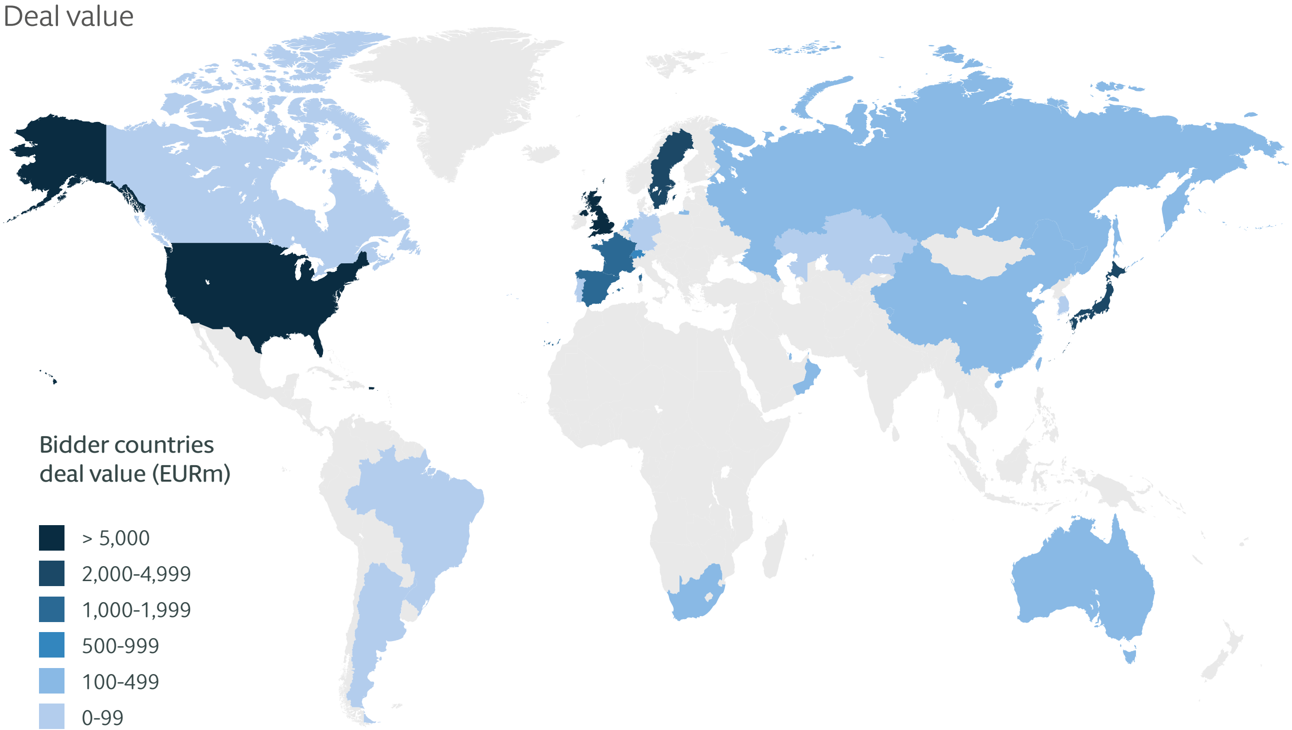
Geographical insights

Fig. 1 – Year 2013/2016 – Country of Bidder

Deal number



Deal value

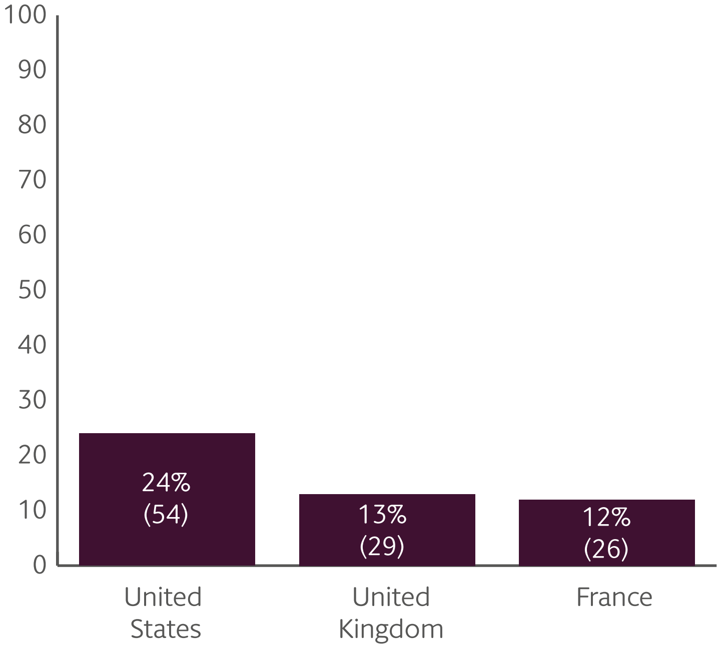


Note for deal value: total deal value per country of Bidder company. Note for deal number: 13 additional deals related to bidder companies based in Italy and US (3), Italy and France (3), Italy, Hong Kong and UK (1), Italy and Lebanon (1), Italy and Switzerland (1), UK and Switzerland (2), US and UK (2). Note for deal value: data not available for Finland, India, Oman, Qatar, Turkey, US and UK, Italy and Lebanon, Italy and Switzerland. Partial data on deals based in US, UK, France, Germany, China, Switzerland, Japan, Spain, Netherlands, Belgium, Luxembourg, Sweden, EAU, South Korea, UK and Switzerland (550), Italy and France (152). Deals based in Italy and US (2,918) and Italy, Hong Kong and UK (390).

Investments from the US, UK, France, Japan, Sweden and Spain accounted for a total value of €24.4bn (84% of total deal value) over the period.

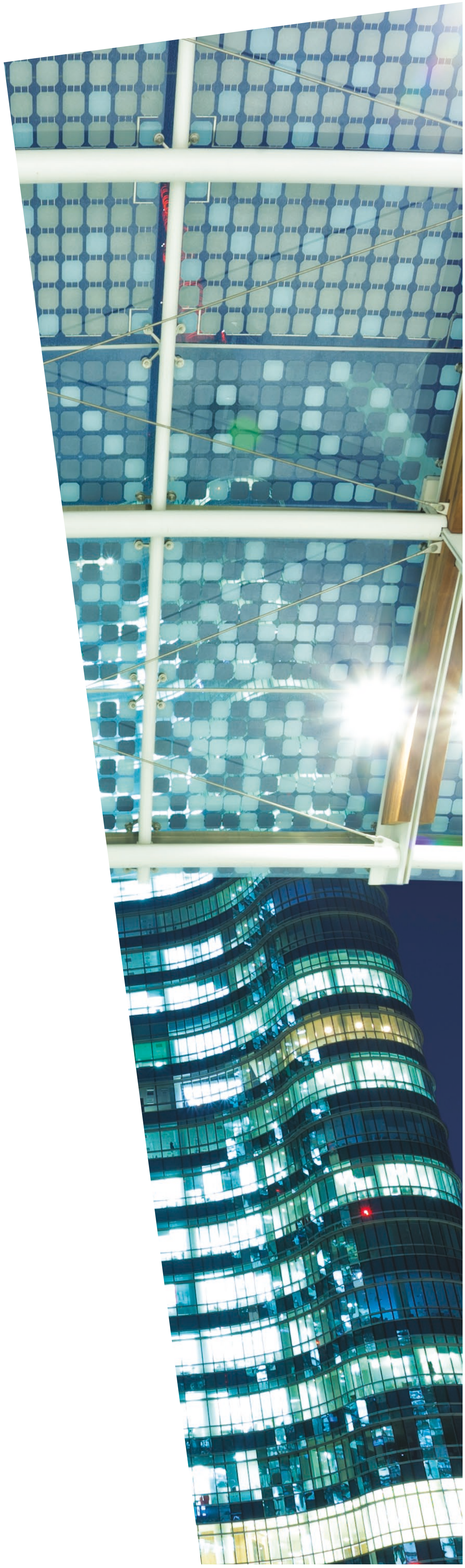
The research confirms that despite globalisation and the growing status of China and other developing economies, the lion's share of foreign investment into Italy continues to come from traditional trading partners such as the United States, United Kingdom and France. Investments from the US, UK, France, Japan, Sweden and Spain over the period under review accounted for a total value of €24.4bn, equal to 84% of total deal value.

Nationality of most frequent foreign acquirers of Italian targets during the period studied



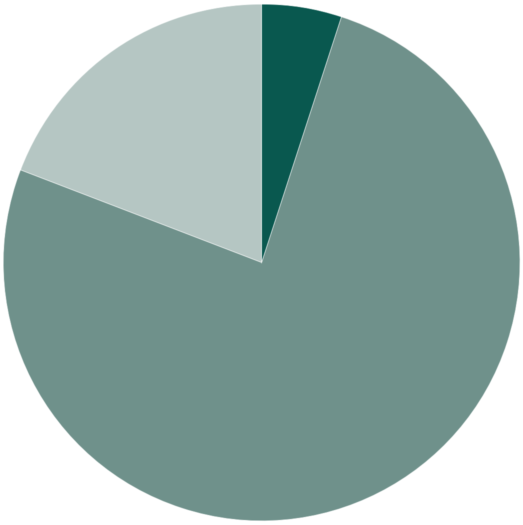
Over the four-year period, global bidders from 39 different countries acquired stakes in the cohort of Italian targets under study. The countries whose investors most frequently acquired stakes in Italian targets were the United States (54), the United Kingdom (29) and France (26).

Just over three-quarters (77%) of those deals where it was possible to extract the relevant information (123 in total, over half of the cohort of 225 targets) saw Italian companies divesting to foreign investors, while the remainder featured deals between foreign counterparties involving a target based in Italy which was already under foreign ownership.



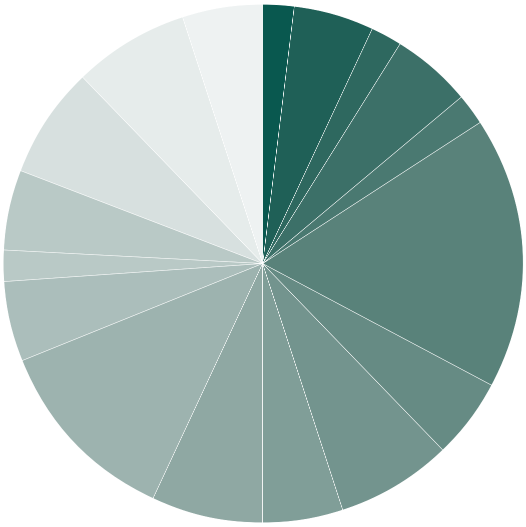
Industry insight

Fig. 2 – Deal volume by sector



Financial 5%
Industrial 76%
Services 19%

Fig. 3 – Year 2013/2016 – Target companies by industry



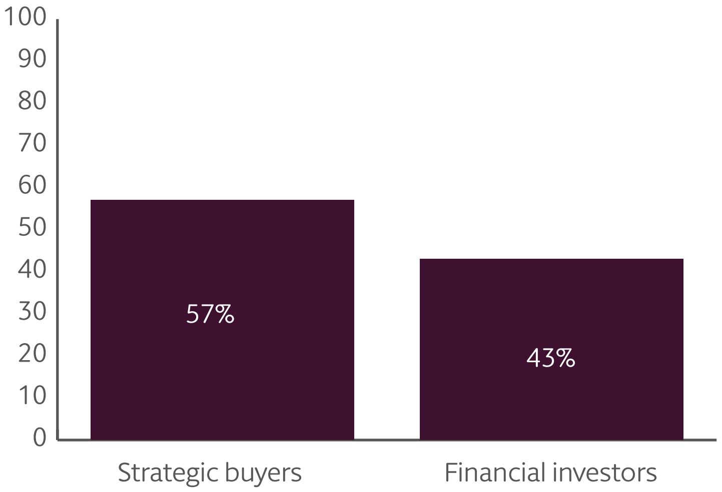
Auto / Truck 2%
Computers & Electronics 5%
Construction / Bldg Prods 2%
Consumer Products 5%
Finance 2%
Food & Beverage 17%
Forestry & Paper 5%
Healthcare 7%
Leisure & Recreation 5%
Machinery 7%
Metal & Steel 12%
Professional Services 5%
Real Estate 2%
Retail 5%
Textile 7%
Transportation 7%
Utility 5%

Industrial targets most frequently draw the interest of foreign investors representing 71% of the deals included in the study, followed by services (24%) and the financial sector (5%).

The most frequent industrial targets are Italian companies operating in the food and beverages sub-sector (12%), followed by targets in machinery (8%), metal/steel (7%) and consumer products (7%).

Control is key

Percentage of deals from 2013 through 2016 by type of buyer

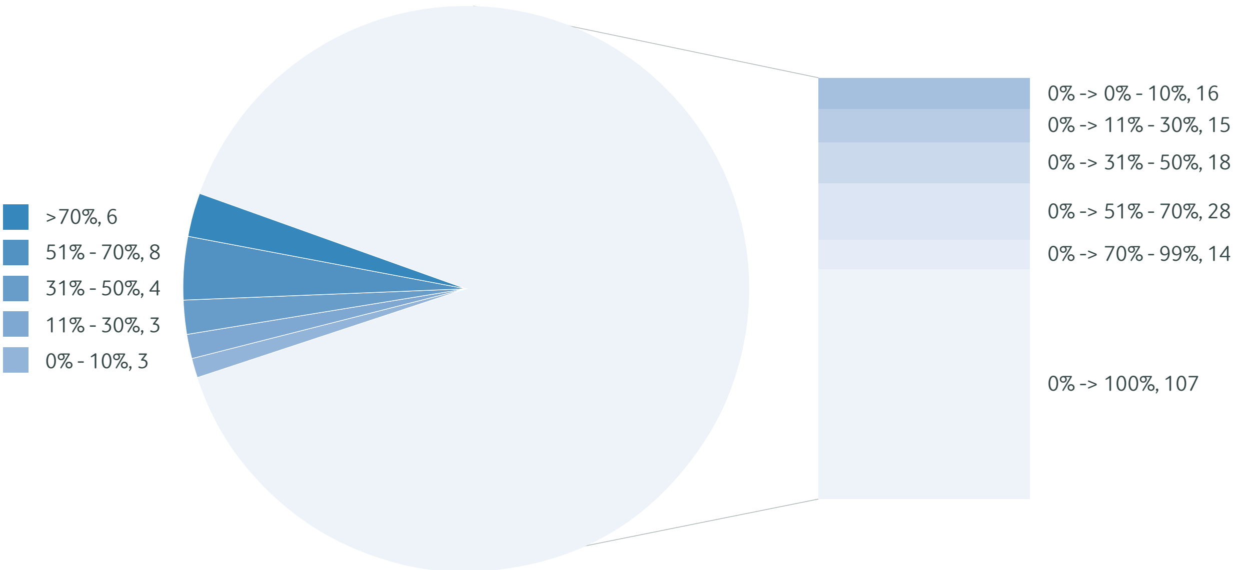


The research also reveals that financial investors, including private equity houses, have become a significant source of inbound investment, accounting for a sizeable 43% of buyers of Italian targets.

Fig. 4 – Year 2013/2016 – Pre-deal and post-deal stake

Initial Stake in the Target; # deals
Presence of the Bidder in the Target capital pre-deal; # of deals

Stake after the deal; # deals (only for Initial Stake 0%)
Presence of the Bidder in the Target capital post-deal; # of deals



Note: 3 missing data.

The research shows that foreign acquirers generally seek control of the target: 107 transactions (48%) resulted in buyers achieving a 100% stake, while in 149 deals (66%) buyers acquired a stake of more than 50%. Most of the investments (89%) were by buyers that had no initial stake in the target.

Strategic value

Attractive multiples paid by foreign acquirers for Italian targets.

The average EBITDA multiple paid by acquirers for those targets where deal values were available was 8.65x, with certain sectors commanding higher multiples, such as consumer products (17.5x), retail (15.7x), transportation (13.4x), chemicals (10x) and telecommunications (9.2x).

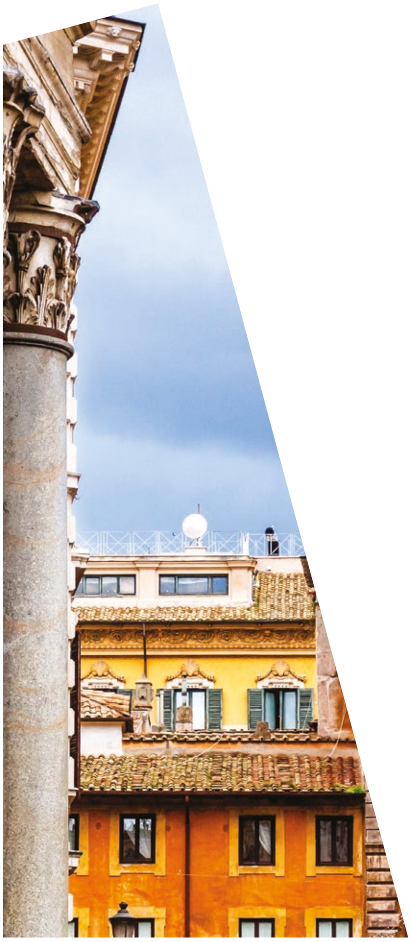
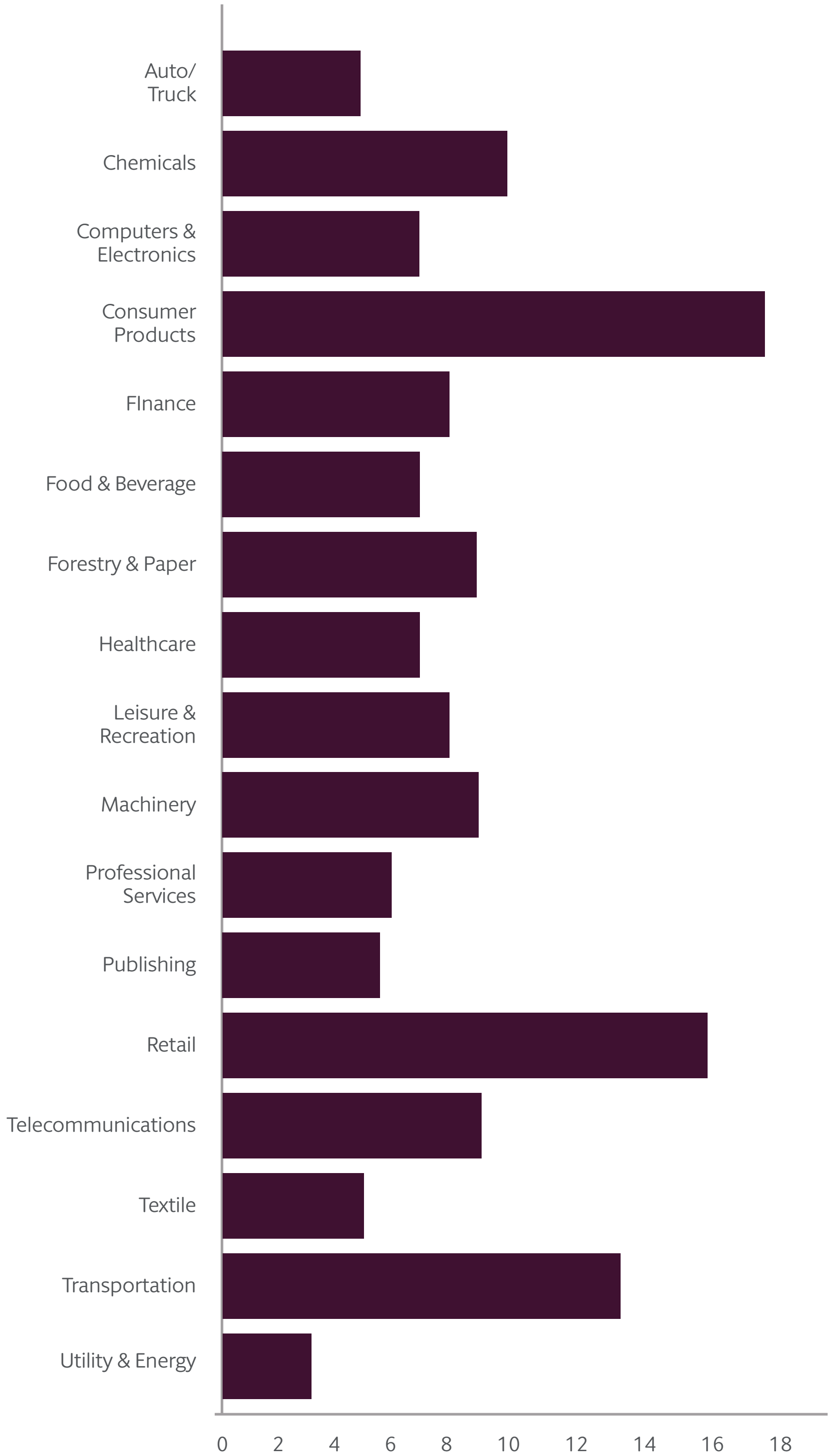


Fig. 5 – Average EV/EBITDA by Target Industry



Note: based on a subsample

Foreign investment as a catalyst for business growth

The top managers surveyed mentioned the role of foreign investment in their companies as a catalyst for business growth and diversification, increasing internationalization but at the same time bringing changes in governance for a more sustainable future.

Responses to the survey indicate that with the entrance of a new foreign investor, companies experienced:

- entry into new markets and internationalization, increased product diversification, new commercial partnerships and greater attention on sustainability;
- changes in governance, such as the appointment of new directors, a new CEO and/or top managers, the exit of minority shareholders and new remuneration plans;
- increased bargaining power with suppliers and greater synergies;
- new customers, increased bargaining power with existing customers and enhanced visibility and reputation;
- improvements in terms of sales, margins, CAPEX, employment and personnel remuneration.

Contacts

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Change is happening faster than ever, and to stay ahead, you need to anticipate what's next. Legal challenges come from all directions. We understand and work together with you to solve the toughest legal issues in major industries and commercial centers around the world. Whether change brings opportunity, risk, or disruption, be ready by working with Hogan Lovells.

We have over 2,500 lawyers, including more than 800 partners, operating out of more than 45 offices in the United States, Europe, Latin America, the Middle East, Africa, Asia and Australia.

Hogan Lovells opened in Italy in 2000 and now counts a team of around 100 professionals, including 20 partners working, as one integrated team, in its Milan and Rome offices.

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