

February 2016

M&A Predictor

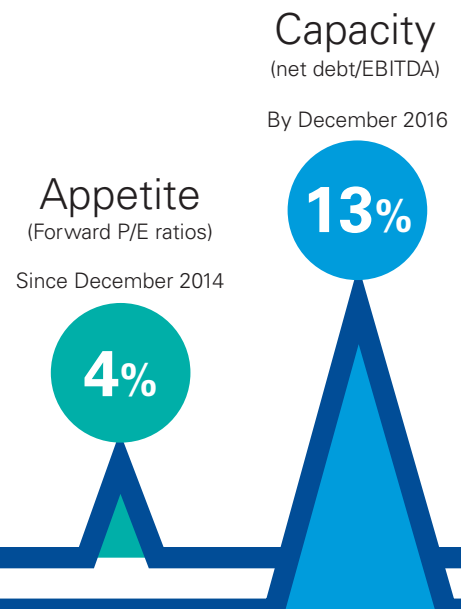
Global M&A levels expected to stay strong in 2016

After a strong year for M&A in key markets during 2015, analysts expect the world's largest corporates to maintain the positive momentum for deals in 2016, with both appetite and capacity predicted to increase globally.

The appetite for deals, as indicated by predicted forward P/E ratios (our measure of corporate appetite or confidence) is expected to rise by 4 percent over the next 12 months. Similarly, the capacity of corporates to fund M&A growth, measured by net debt to EBITDA ratios (our measure of capacity) is expected to rise by 13 percent over the same period, as companies continue to pay down debt and bolster their cash reserves.

What is KPMG's M&A Predictor?

KPMG's M&A Predictor is a forward-looking tool that helps member firm clients to forecast worldwide trends in mergers and acquisitions. The Predictor was established in 2007. It looks at the appetite and capacity for M&A deals by tracking and projecting important indicators 12 months forward. The rise or fall of forward P/E (price/earnings) ratios offers a good guide to the overall market confidence, while net debt to EBITDA (earnings before interest, tax, depreciation and amortization) ratios helps gauge the capacity of companies to fund future acquisitions. The Predictor covers the world by sector and region. It is produced twice a year, using data comprising 1,000 of the largest companies in the world by market capitalization.*



Source: S&P Capital IQ/KPMG analysis

“We expect companies will continue to pursue transactions and believe that we will see strong activity in many western economies in 2016.”

Positive expectations for appetite

The expected 4 percent growth in appetite comes amid a slightly uncertain economic picture in some markets, including China, Russia and Latin America. Globally, net profits are expected to fall by 7 percent. Nevertheless, analysts appear to be pricing this decline into their predictions, as market capitalizations demonstrate a decline of 3 percent. The fact that market capitalizations haven't declined as much as net profits equates to a 4 percent growth in appetite globally.

“With the Chinese economy cooling down, the US starting to raise interest rates and oil prices depressing the economies of oil exporting countries, uncertainty has increased significantly going into 2016. By contrast, in many mature, western economies, we continue to see healthy balance sheets and profit levels as well as strong liquidity in the debt markets. When combined with businesses facing digitalization and increased sector convergence, there will be the compelling need for strategic adjustments. Therefore, we expect companies will continue to pursue transactions and believe that we will see strong activity in many western economies in 2016. Emerging market economies are expected to remain challenging, however,” commented Leif Zierz, Global Head of Deal Advisory.

In Europe, analysts expect the growth in appetite to be more than double the global average, at 10 per cent, while Asia Pacific (Other) and Asia Pacific (Japan) recorded growth figures of 6 percent and 4 percent respectively. In North America, the decline in net profits is expected to be matched by the decline in market capitalizations, so confidence levels are forecast to remain unchanged (0 percent) on 2015 — a strong year for M&A.

According to expectations, the largest growth in appetite will be in Latin America, at 12 percent. However, there are only 24 Latin American companies among the top 1,000 corporates used for the analysis.

UK leads the pack in Europe

Out of the largest European economies, the UK shows appetite growth at 11 percent, Spain at 7 percent and Germany at 5 percent. Combined with their growth in capacity (UK: 8 percent, Spain: 12 percent, Germany: 16 percent), analysts are expecting to see a robust M&A market in Europe in 2016.

Other notable European markets include Italy (appetite up 28 percent, capacity up 8 percent) and the Netherlands (appetite up 5 percent, capacity up 11 percent).

“We expect a robust M&A market in 2016 in Europe, which is being reflected in higher volumes and higher valuations. Financial Services in particular will experience regulations-induced activity. This started in the insurance industry last year and will continue into 2016. They will be joined by banks which are now under the direct supervision of the ECB (approx. 130 European banks). Higher regulatory capital requirements will force banks to look for strategic alternatives, such as M&A or selling non-core assets. This, combined with a strong PE buyer community, sets up the ideal environment for a very active 2016,” says Giuseppe Rossano Latorre, Partner, KPMG in Italy.

These positive predictions for M&A in Europe are supported by KPMG's *US M&A Outlook Survey 2016*, which predicts Europe to be the top region for investment outside of the United States.

In India, appetite is predicted to be flat at 0 percent. An increase in capacity of 24 percent, however, suggests that Indian companies are improving their financial results, but not anticipating inorganic growth.

“We expect a robust M&A market in 2016 in Europe, which is being reflected in higher volumes and higher valuations.”

Capacity growth to exceed appetite

The capacity to transact of the world's largest corporates is predicted to show even stronger growth than appetite, up 13 percent globally. North America and Europe are both expected to show significant increases in capacity, at 15 percent and 12 percent respectively. Capacity in Asia Pacific (Other) is forecast to be even higher, at 19 percent, as is Africa and the Middle East, at 18 percent.

The only two regions expecting a below average growth in capacity are Asia Pacific (Japan) and Latin America, where the figures are 1 percent and 8 percent respectively. However, Latin America's predicted increase in capacity, combined with the growth in appetite, suggests there are still continued opportunities in the region, despite its issues.

Confidence strong in Asia Pacific

Asia-Pacific's predicted capacity growth is boosted by big increases in Taiwan (85 percent), South Korea (41 percent), India (24 percent) and China (19 percent). South Korea in particular, with its exceptional growth in capacity combined with an 8 percent growth in appetite, is expected to have a strong year in 2016.

“The Korean M&A market was mainly driven by large intra-group transactions as well as reorganization-related disposals and distressed M&A, etc. Between further inter-group activity and the distressed M&A area, we anticipate a very active 2016,” says Sung-Won Park, Partner, KPMG in Korea.

China, too, is looking very positive, combining a 9 percent increase in appetite with its 19 percent capacity growth.

“There are still large amounts of capital to deploy in China, along with pressure to grow in an increasingly

challenging economy. We expect continued strong M&A activity as a result. China institutions will continue to direct capital to outbound investments, and ongoing State Owned Enterprise reforms will drive further domestic consolidations. The recent market turmoil may also assist the very active PE community, which is seeking more reasonable valuations,” says Ryan Reynoldson, Head of Transaction Services, KPMG China.

Many other Asia Pacific countries also posted impressive capacity numbers: Malaysia (26 percent), Indonesia (17 percent) and Singapore (15 percent). Capacity growth in Japan is more muted, however, at 1 percent.

United States drives capacity growth in North America

The growth in North American capacity is led by the United States at 16 percent. Mexico contributes with 10 percent and Canada trails at 6 percent. With US appetite predicted to remain the same, the increase in capacity means the United States is still on track to match last year's blockbuster year. This ties in with the *M&A Outlook Survey 2016*. The survey found that the high level of M&A activity is expected to continue into 2016, with record cash balances seen as the major driver by 51 percent of respondents.

“Numerous factors indicate that the high level of activity in 2015 will carry over into 2016. As US companies continue their quest for growth, many companies are choosing to include M&A as an integral part of their strategy,” says Dan Tiemann, Head of Deal Advisory, KPMG in the US.

All of these big capacity numbers are mostly based on reduction of debt, with some help from positive EBITDA.

“Appetite is expected to stay the same as 2015 in the Technology sector.”

Mixed expectations for key industry sectors

In terms of sectors, the strongest performers in terms of appetite are expected to be: Energy, with a 23 percent increase expected in 2016, Basic materials at 12 percent and Consumer Staple at 6 percent. There are some significant declines in other sectors, however. Most notably Utilities, where appetite is expected to decrease by 6 percent.

Technology is the star performer for capacity growth, with analysts expecting an increase of 90 percent in 2016, as tech companies continue to increase their cash stockpiles. Appetite is expected to stay the same as 2015 in the Technology sector. But given that 2015 was a strong year for Technology M&A, maintaining appetite at the same level is a positive sign — and one that is consistent with the findings of the *KPMG US M&A Outlook Survey*, in which respondents expected Technology to be the most active sector in 2016.

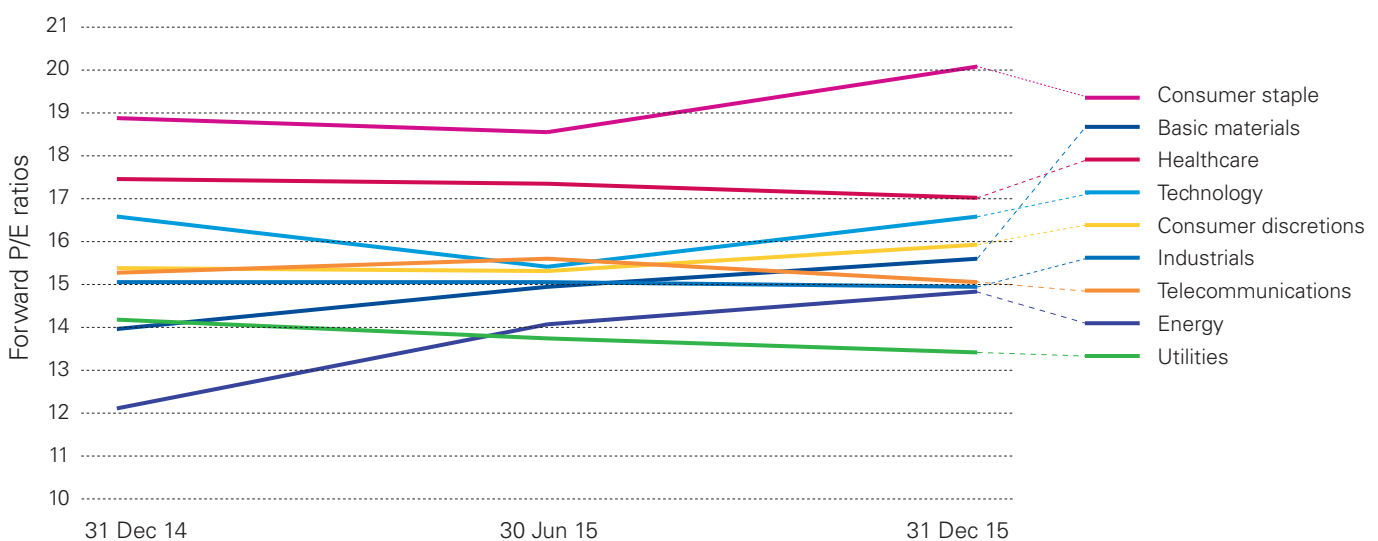
Additionally, we can see corporate appetite for technology through their investments in Venture

Capital. Globally, corporates have participated in 25 percent of deals for three quarters straight, as corporates continue to open venture investment arms “at a feverish pace,” states KPMG and CB Insights in the recently published *Venture Pulse, Q4’15*. In Asia, corporates accounted for 1/3 of deals.*

Healthcare is predicted to see the second highest rise in capacity, at 30 percent. With market capitalizations (up 7 percent) and net profits (up 10 percent) also forecast to rise, a strong year is anticipated for Healthcare companies. This, too, is supported by the *US M&A Outlook Survey*, which anticipates that four of the seven most active M&A sectors next year will be healthcare-related.

Analysts are not expecting Energy, on the other hand, to see any growth in capacity, despite its healthy growth in appetite of 23 percent. Given the record low price levels in the global energy market recently, particularly oil, such a cautious prediction is perhaps not surprising.

Market confidence by industry sector



Source: S&P Capital IQ/KPMG Analysis

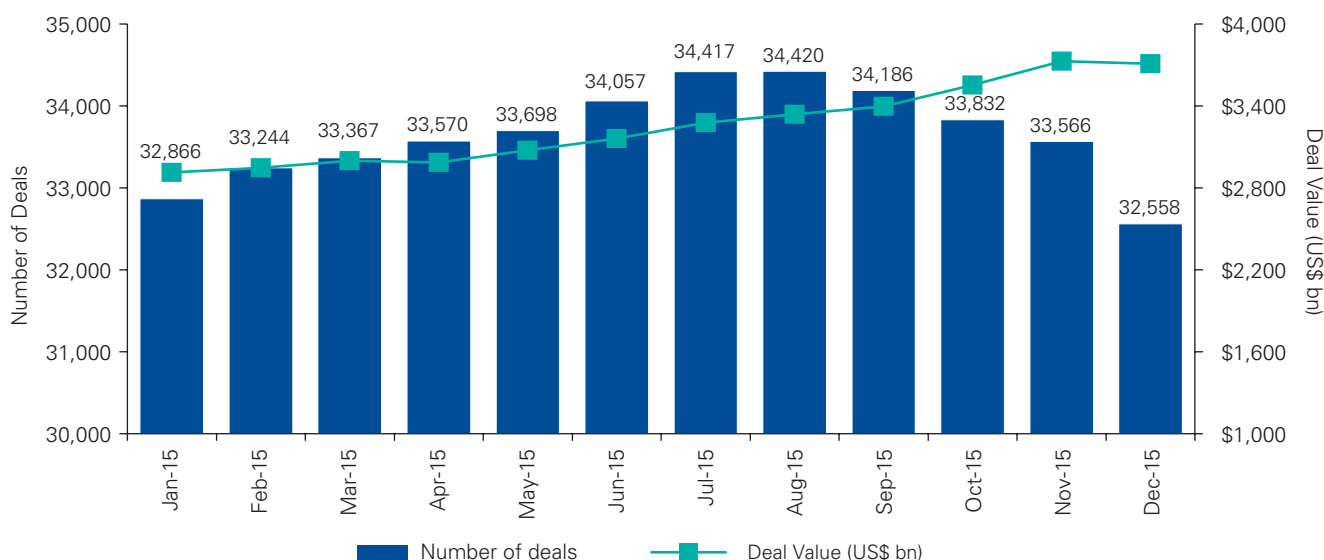
*Source: Venture Pulse, Q4’15, Global Analysis of Venture Funding, KPMG International and CB Insights (data provided by CB Insights) January 19th, 2016

Announced deals on the up

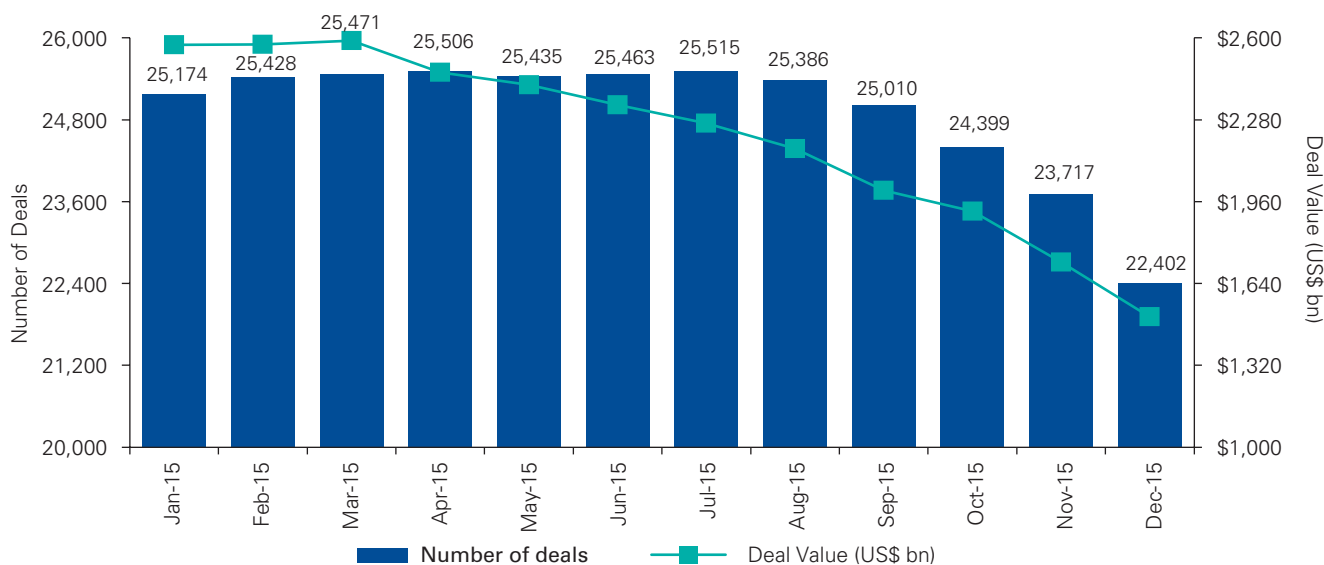
The total value of all announced transactions worldwide climbed by 31 percent in value from US\$2,828B to US\$3,709. This diverged significantly from the total value of all completed transactions worldwide, which declined by 40 percent during 2015 (from US\$2,513.5B to US\$1,510.3B).

“Despite recent market jitters, the expectation that M&A activity will remain robust in 2016 is well-founded based on corporates’ ample cash reserves and their desire for growth coupled with consistent demand for quality opportunities from private equity sponsors,” commented Phil Isom, Global Head of M&A.

Worldwide announced deals: 1 year trailing — Jan 15 — Dec 15



Worldwide completed deals: 1 year trailing — Jan 15 — Dec 15



Source: Thomson One, accessed on January 12th, 2016.

Deal Advisory: Delivering real results

KPMG's integrated team of specialists works at deal speed to help you find, secure and drive value throughout your business transformation and transaction lifecycle. By thinking like an investor, our M&A specialists can support you – whether you are on the buy side or the sell side – to see beyond immediate challenges to drive strategic change.

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*The financial services and property sectors are excluded from our analysis, as net debt/EBITDA ratios are not considered relevant in these industries. All the raw data within the Predictor is sourced from S&P Capital IQ. Where possible, earnings and EBITDA data is on a pre-exceptionals basis with the exception of Japan, for which GAAP has been used.

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