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ACQ ASKS INDUSTRY EXPERTS HOW M&A AND INVESTMENT ACTIVITY IS SHAPING UP IN A EUROPEAN JURISDICTION THAT APPEARS TO BE DEVELOPING IN PARALLEL WITH ITS NEIGHBOURING EU MEMBER STATES.

Dr. Georg Lutz is Director of Ernst & Young's Transaction Tax Practice in Zurich. He co-ordinates a team of 22, advising on large transactions from a tax perspective.

According to Dr. Lutz, Swiss M&A activity has been rather intense over the last few months, with several mega-deals exceeding the 1bn mark and a generous volume of mid-market deals valued at between €50m and €500m.

"The reasons underpinning this rally of activity stem from the global trends that ultimately dictate the dynamics of smaller economies, leading to an increasing tendency for companies to expand their core businesses on a global level and bringing about the concurrent de-investment of non-core business elements.

"On the surface, Switzerland generally falls in line with other markets across Europe. But if we put Switzerland under the microscope, it soon becomes obvious that we have an advanced, specialist economy," he explains. "There is a unique concentration of core business development here, and this has been facilitated by the vast number of global businesses operating through Switzerland. With national interest rates remaining reasonable and the willingness of banks to finance high EBIT multiples, the transaction environment is ideal.

"Switzerland incentivizes deal activity both financially and legally. Historically, we have enjoyed low interest rates, especially when compared to the Euro and Dollar economies. From a legal perspective, the frameworks that govern Swiss law have worked to create a stable system with a high degree of transparency."

Dr. Lutz cites two large transactions Ernst & Young has advised on this year - both are cross-border. In June, French insurance firm AXA acquired Winterthur Insurance Group from Credit Suisse Group for €7.9bn (CHF12.3bn). Three months later, 3i sold Zurich-based SR Technics to a consortium of investors based in the United Arab Emirates for a consideration of €1bn (CHF1.6bn).

Looking ahead, Dr. Lutz expects deal activity to continue at the same pace over the next three financial quarters, tailing off towards the end of 2007.

"Although it is difficult to predict when the next downturn will be, I believe we're looking at the last quarter of 2007 going into 2008. By that rationale, there should be a good nine to twelve months of prosperous transaction activity remaining."

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Oyvind Bjordal is Managing Director at Sal. Oppenheim Corporate Finance in Zurich. The 30-strong team focuses on M&A, Equity Capital Markets (ECM), Financial Institutions and Real Estate Advisory services.

"Today, I would characterise the M&A market in Switzerland as very good but hasten to add that what is happening in the mid market does not mirror the "frenzy" of mega deals going on in Europe," he says.

"To date we have witnessed four large transactions in excess of €1bn - the AXA/Winterthur deal, the sale of SR Technics, the buyout of Serono by Merck for €10bn and the just announced public offer for SIG. But it is the activity in the small- to mid-market in 2006 that has proved more sustainable. Some 100 deals have so far been announced, less than 20% of which were valued at €100m or more."

"European cross-border activity is continually hotting up," he says, "but the share of cross-border transactions in Switzerland is even higher.

"It's great to see a return of trade buyers - an area that suffered between 2002 and 2004. During this time, PE houses were the only buyers, keeping things afloat. Interestingly, they are still holding their fair share of the deals - primarily driven by generous funding and low financing costs but also thanks to their now mature and professional organizations in Europe," he says.

"Legal development will be key," states Bjordal. "From January 2007, there will generally be no tax on capital gains subject to certain conditions for individuals selling their companies. I expect, therefore, to observe an upping of activity in the family-owned business segment.

Bjordal expects the positive business climate in Switzerland will last, in the medium term at least. Obviously, if there is a global slowdown, lending policies are likely to change and M&A activity will follow suit.

"I should say that since last year, the private equity market in Europe has outsized that of the US, however the States does boast a VC culture and investment activity level that is still sorely lacking in Europe. Perhaps - and hopefully - this is an area which might pick up."

Christophe Wilhelm and Michael Kenyon of RWB Advocats in Lausanne specialize in business law, tax law, transfer pricing and wealth management and transfer. They say that since Switzerland is completely integrated into the EU, M&A activity follows very similar trends to those seen in the rest of the Union. "Switzerland is not an island in Europe. It follows the same trends and is directly affected by EU and global trends."

According to Wilhelm and Kenyon, cross-border transactions are a common feature of Swiss M&A: "All the transactions in which we have been involved were cross-border transactions. In our experience this is very typical for Switzerland."

In terms of how legal and financial factors influence Swiss deal activity, the lawyers stress that the nation's legal system/climate certainly helps.

"Swiss negotiations are typically influenced by the concept of "fairness"; in general neither party wishes to obtain an unfair advantage at the other's expense. Lawyers active in Swiss M&A tend to keep a sharp focus on the client's business goals and to save the battles for what is important for the client, not what seems important from a purely legal viewpoint."

Looking ahead, Wilhelm and Kenyon say: "As is the case everywhere, M&A activity is buoyant and we expect it to continue if not increase in the medium term. The patterns are influenced by the same factors as elsewhere, especially in the EU: EU integration - the rush to win the battle to be biggest and best in the EU; globalization - achieving critical mass to serve customers on a global basis; restructuring of the large multinationals, shedding non-core activities, and the concomitant opportunities for niche players to build their markets in the new outsourced world. There are no "Switzerland-specific" factors, other than Switzerland's increasing psychological proximity to the EU."

Dr Wolfgang Zuercher is a Joint Managing Partner of law firm Wenger & Vieli based in Zurich. His responsibilities cover M&A transactions and capital markets.

He says that Swiss M&A levels are picking up with core mid-market activity in the CHF20-50m range.

"Companies have completed their restructurings and are preparing to exercise an active approach to the market," says Dr Zuercher. "It follows that there is mounting interest in acquiring new entities and it's a good time to sell.

"The Swiss M&A market is fairly reflective of other European markets," Zuercher believes. "Money is back and banks are willing to provide favourable debt packages."

He sees a dip in FDI from the US, marking a shift from US-European to continental-oriented deals. National trade buys are becoming more frequent in fact.

"A recent change in tax law has re-ignited the buyout scene, especially when it comes to private individuals. It will provide legal comfort once again and I am convinced there will be an upturn in MBOs as a result," he says.

"There are positives in the financial structures in Switzerland too. Banks are still interested in providing debt and there is a very low default rate which increases the possibility of financing transaction activities."

But Dr Zuercher maintains a realistic overview of the country's financial health, believing that sooner or later transactions may be over-leveraged.

The law firm has been involved in a number of IPOs this year as well as several mid-size and smaller M&A transactions between CHF5m and CHF50m.

In future terms, Dr Zuercher is relatively positive: "The M&A business has recovered and will continue to develop into next year. Sooner or later, takeover companies will default. This will cause banks to become more restrictive, which will in turn affect their debt finance policies causing investors to reconsider."

An interesting development in the local cap segment is the growing media speculation suggesting the Bern Exchange could become a Swiss alternative to AIM.

"Since its entry thresholds are lower than the Zurich Stock Exchange (SWX), it has attracted a spate of younger companies, which has led to discussions in the press. So, we may see a gentle shift in emphasis, although it will be in response to demand, if and when it happens."

Dr. Markus Berni is a Partner at Baker & McKenzie's Zurich office. His legal practice centres around M&A, PE and IT. He has seen a definite switch in the direction of M&A activity since Spring 2005.

"We are seeing an increase in forward-looking deals based on strategies with a clear future focus. Now, there is an encouraging rise in investors that are willing to take risks, so much so that PE houses are sometimes reluctant to wait too long before making a play on target companies," he explains.

"At one stage there was concern about Switzerland's operating externally of the EU. Anxiety was mostly related to the very real possibility of a backlog in legislation and reform. But there was little to no backlog - at least not in comparison to other European markets," says Berni.

Berni has seen a lot of in-bound FDI. "By the same token," he says, "there has been a clear rise in domestic activity fuelled by the maturing of home-grown SMEs that have been restructuring and streamlining in an attempt to re-focus their strategies. Many are now fit for growth.

"GDP growth will be more than 2% - and we expect it to hit the same range next year. There are still deals out there for SMEs literally waiting to be discovered and the changing attitude of more traditional PE firms is only complimenting and enhancing an increasingly favourable climate."

Legislative developments, although formally divorced from the EU, are running in parallel, and along similar tracks. "Our antitrust law has been increasingly aligned to that of other European jurisdictions. The Corporate Act, too, is in the process of reform, the implementation of the first stage of which we can expect to see next summer. And finally, tax reform that will alleviate the tax burden of companies and investors is under way.

"On the financial side, Swiss interest rates are at historic lows.

"The prognosis for the Swiss market is very good," says Berni. "I could well imagine an even more intense year of activity in 2007. The stock market is developing favourably, fed by the speed and momentum in the M&A market. And there is plenty of cash available in private equity. I believe too that there are still pearls to be discovered..." ACQ

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