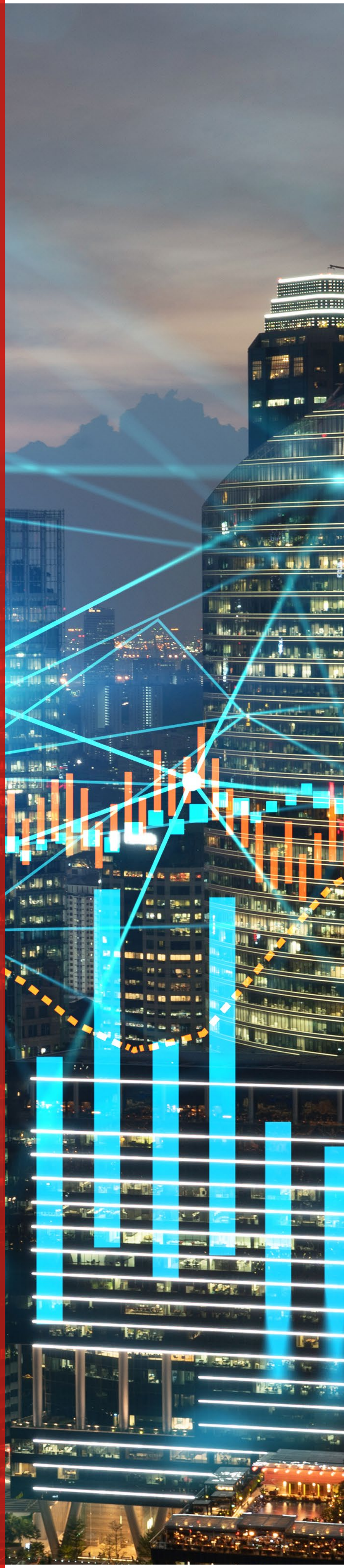
Australian private M&A deal trends report

2021 Edition



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Introduction

On behalf of Norton Rose Fulbright Australia, I am pleased to present our 2021 Australia M&A deal trends report.

This report is intended to provide an empirical benchmark of Australian market practice for key private M&A negotiation points. It is a close analysis of the 94 completed private M&A transactions that Norton Rose Fulbright Australia worked on during the 2021 calendar year, as well as a continuation of the Australian deal trends longitudinal study that we have undertaken since 2014.

The 2021 transactions included in this report involve parties from more than 14 countries with a combined deal value of $19 billion.

The Australian and global markets bounced back strongly in 2021 after a pandemic-affected 2020. M&A records were smashed as companies adapted to new ways of working and investors continued to benefit from low interest rates and easy access to capital. In Australia, the frenzied M&A market was driven by strong demand in the technology and healthcare sectors, in many cases resulting sky-high valuations.

We hope this report continues to be a useful tool for M&A practitioners and participants to understand Australian private M&A market practice, both currently and as it has evolved over recent years.

Please contact a member of our M&A team if we can be of assistance.

Best regards,

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Key Features

We acted for sellers, buyers and warranty & indemnity insurers on 94 private M&A transactions that completed during the 2021 calendar year. This allows us to conduct a broad survey of the market, taking into account not only our own firm's negotiated positions but also those of many other law firms.

94 Sale agreements
Value of deals: **$19 billion**
Average deal value: **$202 million**

Who we acted for
Seller: **4%** Buyer: **10%**
W&I Insurer: **86%**

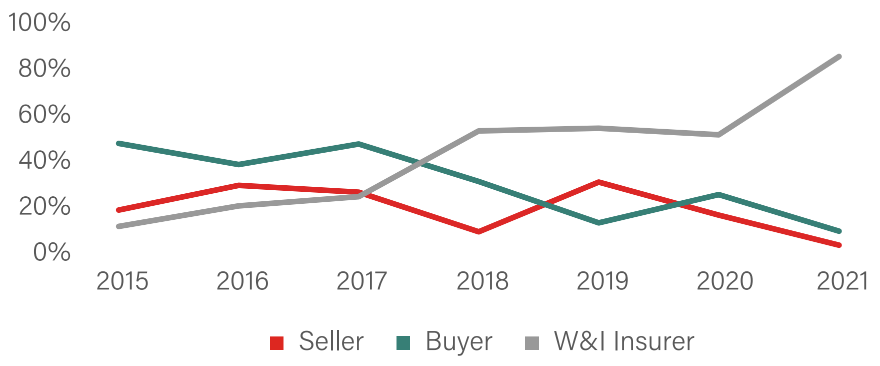
Type of transactions
Share sales: **85%**
Business sales: **15%**

Warranty & indemnity insurance

Warranty & indemnity (W&I) insurance is now commonplace in Australian M&A transactions and is a key risk management tool for both sellers and buyers. We are a market leader in advising W&I insurers on both private and public M&A transactions in Australia, including for tax regime coverage.

In W&I deals, the risk of financial loss from a breach of warranty is transferred from the buyer or the seller to the insurer. We have seen an increasing trend where prospective bidders are required to take out W&I insurance. The inclusion of W&I insurance is appealing to the seller and is sometimes used as a strategy to help the bidder win a competitive auction. W&I insurers adapted to the COVID-19 pandemic response by adopting broadly-drawn COVID-19 exclusions. This was an understandable reaction, given it is not the purpose of a W&I policy to cover systemic risk. It appears bidders are willing to assume COVID-19 risks and market appetite for deal making and W&I insurance is showing no sign of abating.

Who we represented | 2015 - 2021



[% of deals by who we acted for]

We continue to represent all sides of private M&A transactions, though our market leading W&I insurance practice continues to experience strong growth and now accounts for a substantial portion of the sale agreements covered by this study. We apply the insights from acting on so many transactions to assist all our clients, whichever side of the deal they are on.

Foreign buyers

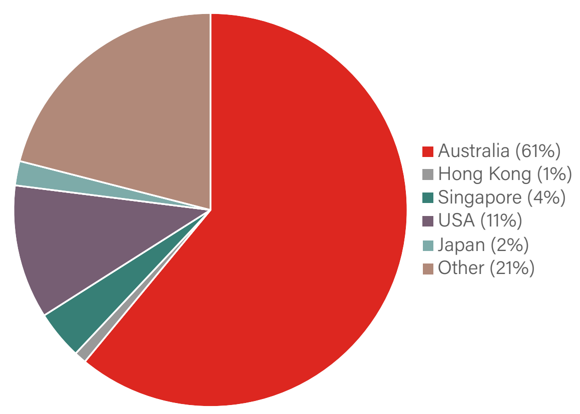
39% of the buyers in our 2021 Australian deals were headquartered in a country outside Australia. This proportion of foreign buyers is broadly consistent with previous years and demonstrates the continuing global interest in the Australian M&A market.

Despite the pandemic, the confidence of foreign buyers in Australian investments remained strong. Many predicted Australia to make one of the quickest economic recoveries, lending it great appeal as an investment destination.

In 2021, we acted on transactions with an unusually diverse group of buyers, with many countries of origin other than the consistently high foreign investment contributors of USA, Japan, Singapore and Hong Kong. As a connected global law firm, we were able to assist on private M&A transactions involving buyers from UK, China, New Zealand, France and Austria, as well as even Cuba and Armenia.

With a relatively stable economy and a strong appetite for Australian assets, we expect deal activity to increase in 2022, as overseas buyers continue to turn to Australia for M&A opportunities.

2021 | Buyer country of origin



[% of deals by buyer country of origin]

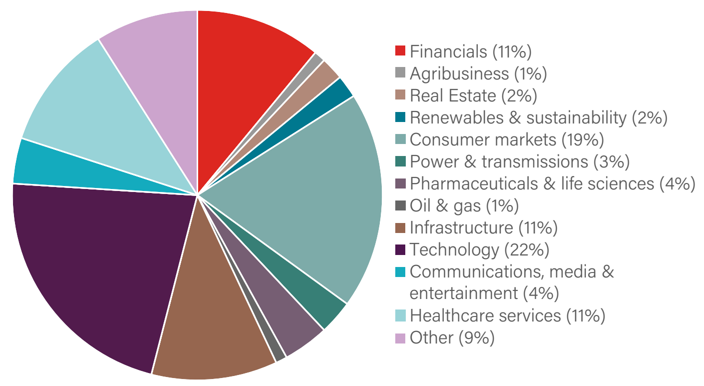
Target industries

The consumer markets sector rebounded from a slower M&A year in 2020, accounting for 19% of our deals in 2021. Many consumers saved more in reaction to government-imposed lockdowns, and resulting reductions in their opportunities for in-person spending. With increased disposable income and a return to a "covid-normal" world, there was a noticeable uptick in demand for consumer products in 2021.

The technology industry also fared well in M&A, experiencing a marked increase in the proportion of deals in that industry, compared with previous years. This reflects the macro trend of increasing digitalisation of all industries, with many players choosing to acquire businesses already proficient in their desired technology, rather than developing the expertise themselves. It also reflects the continuing rise in the economic significance of technology companies, which account for an increasing share of economic growth in developed countries. We expect technology businesses will continue to be highly sought after, as efficiencies gained through process simplification and automation continue to be important drivers for growth and increases in productivity.

Moving forward in 2022, we expect continued high levels activity in the healthcare sector, both in direct response to the pandemic and a snap back of demand for services deferred due to the earlier response to the pandemic.

2021 | Industry break-down

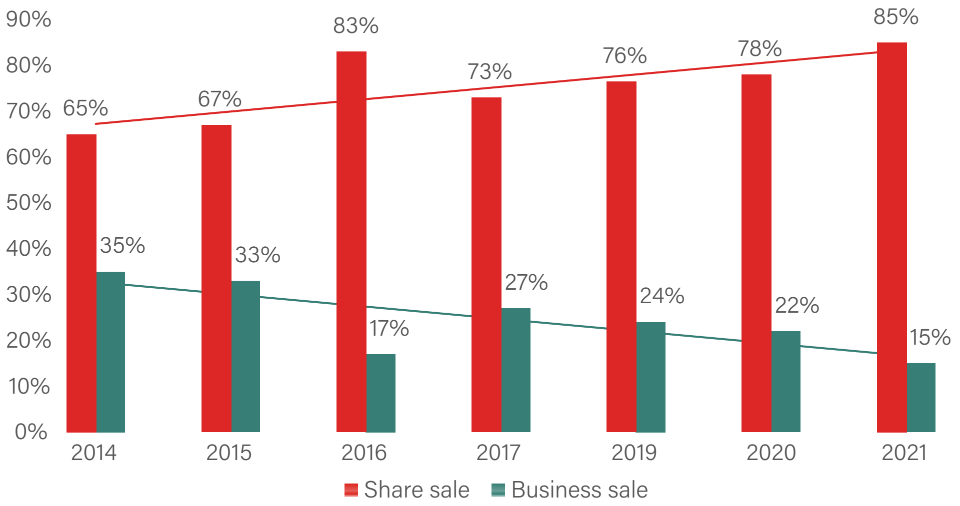


[% of deals by target industry]

Business v share sale

The proportionate increase of share sales in our data set, compared with business sales, is most likely explained by growth in the use of W&I insurance.

The overwhelming majority of transactions involving W&I insurance are share sales, rather than business sales. Share sales involve the purchaser acquiring a company complete with all its historical liabilities, meaning the assets of the target company are exposed to those liabilities. Business sales typically do not involve the purchaser assuming liability for historical liabilities, particularly not unknown ones. W&I insurance is therefore more often sought in a share sale context, with the insurer assuming the risk of unknown historical liabilities.

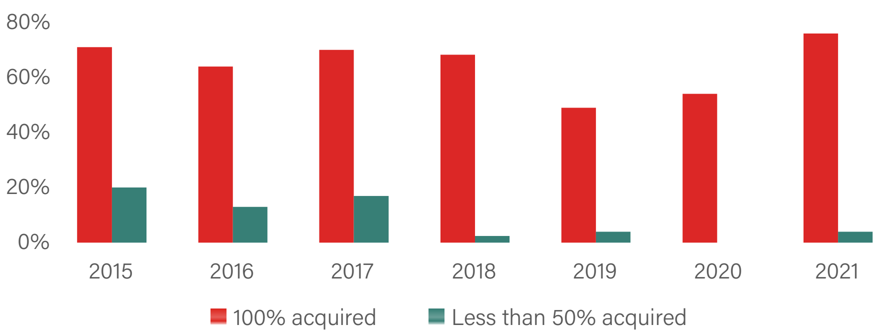


[Share sale v business sale]

More than three quarters of our 2021 share sale deals (76%) involved the acquisition of 100% of the shares in the target company. In contrast, only 4% of our 2021 share deals involved the acquisition of less than 50% of shares in the target company.

We acted on a number of larger Australian deals in 2021, increasing the average deal value in dollar terms to $202 million, up from $108 million in 2020.

Share Sale % | 2015 - 2021



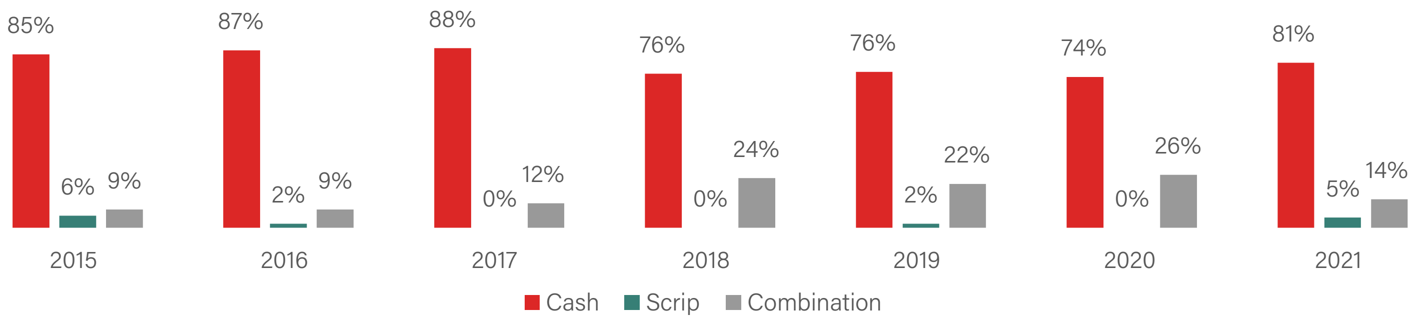
[Share sale involving 100% acquisition]

Form of payment

Cash remains king when it comes to the form of payment we are seeing in the Australian market. Consistent with previous years, our 2021 Australian deals have again featured a strong bias towards cash (81%) as consideration. Cash has long been the preferred payment method for obvious reasons. It does not require the seller to assess the value of the buyer entity and instead provides the seller with immediate liquidity and certainty of return.

With ongoing access to cheap capital, in conjunction with the abundance of money held by financial sponsors and private equity bidders, we expect to continue to see cash to be the dominant purchase consideration in 2022.

That said, one trend that we have observed is the increased use of at least some scrip consideration, compared with the years 2014-2017. Those years were characterised by the use of at least some scrip in around 12% of deals. The years 2018 onward have seen at least some scrip feature in the range of 19-26% of deals. The slight decrease in the use of at least some scrip in our 2021 Australian deals perhaps reflects buyers' preference for the certainty of cash during a period of challenging business conditions.



[% of deals involving cash, scrip, or a combination of both as payment]

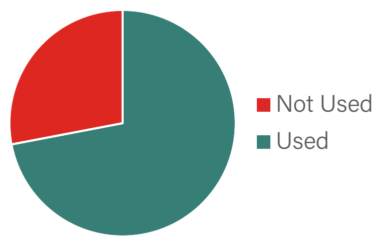
Post-completion adjustments

Post-completion price adjustments remain prevalent in a majority of our 2021 Australian deals. This continues the trend we have seen in recent years (2020: 65%, 2019: 67%, 2018: 54%), with 72% of our 2021 Australian deals including post-completion adjustment mechanisms.

Post-completion adjustment provisions adjust the purchase price up or down after completion of the sale, based on comparing an actual financial metric against a target value for that metric. The most common financial metrics are working capital, net debt and net assets, but parties also agree other metrics that are specific to the circumstances of the target business.

In 2021, where any post-completion adjustment was used, the overwhelmingly most common adjustment metric in our Australian deals was working capital (84%), followed by net debt (71%). In fact, these 2 metrics were predominately used in combination. Only 10% of our Australian deals with a post-completion adjustment used net assets as the adjustment metric.

Post-completion adjustment mechanism



[% of deals using a post-completion adjustment]

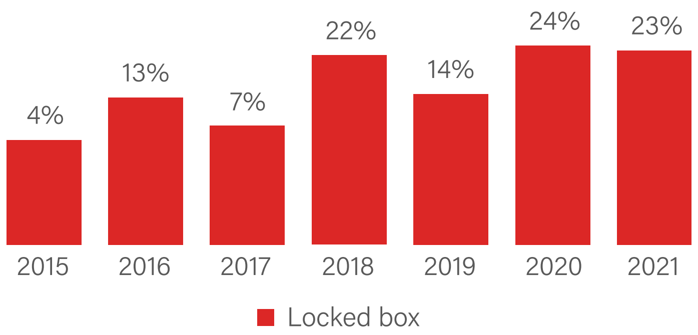
Explanations for why some parties do not include a post-completion adjustment are:

- a locked box is used;
- the parties are connected in some way and the buyer was familiar with the asset;
- it is an acquisition of a minority stake; and
- valuation is a condition to the completion of the sale.

Locked box

A locked box is a purchase price mechanism involving the parties agreeing on a fixed price based on a pre-signing balance sheet, with no post-completion adjustments based on completion accounts. The effect is to transfer the economic risk in the business at the date of the agreement. The use of a locked box mechanism favours the seller, since it gives the seller price certainty, while on the other hand the buyer must accept the risk in the performance of the business before it takes over management control.

Locked Box Used | 2015 - 2021



The longitudinal data may show a step change in the use of locked boxes in our Australian deals from 2018. Historically, Australia has seen far less of use of locked boxes than North America or Europe. The reasonably sustained use of locked boxes in the 22-24% range indicates a change in Australian market practice towards greater alignment with those major markets.

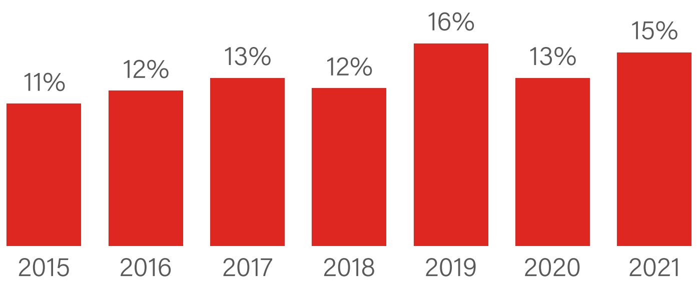
[% of deals using a locked box]

Earn out

Earn out is a mechanism part of the purchase price only payable if the target business achieves certain performance milestones after completion of the sale. These milestones can be either financial, for example reaching a certain revenue target, or non-financial, such as obtaining regulatory approval. Earn outs are more common when the seller has agreed to remain involved in the business after completion. In these cases, part of their purpose is to incentivise the seller, since to earn its maximum purchase price it must continue to strive for the target business' success. Sellers are often reluctant to agree to an earn out, since there is no certainty that they will receive the earn out payments. This is in part because the performance of the target business after completion is dependent on the buyer's actions and how it manages the business.

Earn Out Used | 2015 - 2021

The longitudinal data indicates that earn outs are relatively consistently used in Australia in the range of 11% - 16% of our Australian deals. There is some small variation between years, but the broader picture is of consistent use, rather than significant increases or decreases in use over time.



The data also indicates that they are more usual in lower value deals. For example in 2021, our Australian deals involving an earn out had the average deal value of $57 million, compared with an average deal value of $231 million for our Australian deals that did not involve an earn out.

[% of deals using a locked box]

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Conditionality

Material Adverse Change

Generally, the inclusion of a no material adverse change (**MAC**) condition will mean the buyer has the right to pull out of the transaction if there are events that negatively impact the target's business or assets between signing and completion of the sale. MAC conditions allow the parties to allocate the risks of adverse developments in the period between signing and closing a transaction. MAC conditions typically exclude adverse developments in general business or economic conditions that do not have a disproportionate effect on the target business.

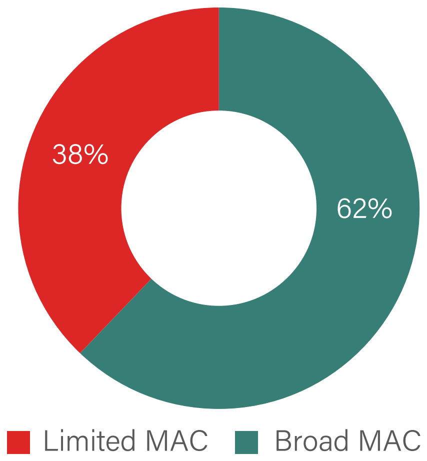
The longitudinal data indicates that MACs are used in 25-36% of Australian deals, with most years featuring MAC use in a narrower 28-33% range.

Despite the uncertain business conditions during the pandemic, 28% of our Australian deals in 2021 and 30% of our Australian deals in 2020 included a MAC condition. This is squarely within the usual 28-33% range and does not suggest a change of frequency of use of MAC conditions in response to the pandemic.

The drafting of MAC conditions did change in response to the pandemic. Following the initial emergence of COVID-19, many MAC conditions carved-out COVID-19 events from the definition of 'material adverse change', meaning the acquirer accepted the risk of further COVID-19 impacts.

When MAC was included as a condition, a "broad MAC" (i.e. where material adverse change was defined very broadly as an event which had a materially adverse impact on the target) was used 62% of the time whereas a "limited MAC" (i.e. a MAC which referred to specific indicators, such as the percentage impact on EBITDA) was used 38% of the time.

MAC | 2021



28% of deals had a MAC condition

Where MAC was used,
38% were a limited MAC &
62% were a broad MAC

A limited MAC uses specific indicators to define when MAC occurs, such as % impact on EBITDA

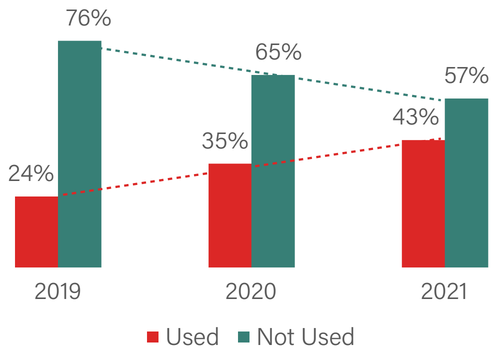
Regulatory approval condition

In 2021, 43% of our Australian deals included a regulatory approval condition.

That is, the deal was conditional on a party or parties (usually the buyer) receiving approval from a regulator such as the Foreign Investment Review Board (**FIRB**) or the Australian Competition and Consumer Commission (**ACCC**). With Australia's continued commitment to improving data security and increased regulatory scrutiny over more deals, bidders and their advisers need to be agile and efficient in navigating the regulatory approval process. The focus for foreign bidders will be to proactively engage FIRB to ensure that they are addressing issues that may put them at a disadvantage to local bidders. This will be particularly important in a competitive bidding environment. Regulatory approvals are set to be significant issues in the infrastructure and technology sectors which are expected to remain highly active in the coming year.

15% of our 2021 Australian deals had a buyer-friendly condition that "all necessary" government waivers and approvals are obtained.

Regulatory Approvals | 2019 - 2021



[Share sale involving 100% acquisition]

The increase in the use of regulatory approval conditions in 2020 and 2021 may be in part be attributable to changes in Australia's foreign investment regime during that period. The focus for foreign bidders will be to proactively engage FIRB to ensure that they are addressing issues that may put them at a disadvantage to local bidders. This will be particularly important in a competitive bidding environment. Regulatory approvals are set to be significant issues in the infrastructure and technology sectors which are expected to remain highly active in the coming year.

We have seen FIRB experience delays in processing applications, due to the sheer volume of applications and the need for a case-by-case analysis. Foreign buyers should bear this in mind as it could impact transaction close dates, noting that sales cannot be closed if the FIRB process is not completed.

The *Competition and Consumer Act* prohibits mergers that are considered anti-competitive as they substantially lessen competition in a market. As a result, many significant transactions are conditional on receiving ACCC approval. There have not been significant changes to the merger approval requirements or process in the past 2 years and we have not observed practices to have significantly changed on the use of ACCC approval conditions. Rather the size and value of transactions may be higher, resulting in it being more likely that merger approval is required.

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Other common conditions

There are a variety of other conditions that are commonly seen in sale transactions:

Retention of key employees
condition seen in **18%** of deals

This condition was seen in 18% of our Australian deals in 2021, which is slightly higher but broadly consistent with figures in recent years *(2020: 15%, 2019: 14%, 2018: 12%, 2017: 15%).* Retention of key employees is often important to acquirers, but it can be achieved through direct agreements with employees, meaning the issue does not necessarily rise to the level of requiring a condition in the sale agreement.

Due diligence
condition seen in **5%** of deals

This is a condition precedent that the buyer completes its due diligence and is satisfied with the results. It was only seen in 5% of our Australian deals in 2021 (down from 11% of deals in 2020). Sellers typically resist due diligence conditions, since these are seen as amounting to giving the buyer an option as to whether to complete the sale. Sellers do not typically want the sale of their business to be announced and the arrangements required to complete the sale commenced if the buyer is not committed to completing the sale.

Competition authority clearance
condition seen in **33%** of deals

Competition authority clearance was required in 33% of our Australian deals in 2021, a big jump from previous years *(2020: 26%, 2019: 24%, 2018: 20%, 2017: 5%)*. This was a feature of the higher value deals as transaction parties sought assurance that their deal will not be affected by competition authorities further down the track.

Pre-completion restructuring
condition seen in **21%** of deals

The amount of deals which require a pre-completion restructure varies significantly year by year. Although it was at a similar rate (12%) compared with last year, we have seen this figure fluctuate in previous years *(2020: 13%, 2019: 6%, 2018: 7%, 2017: 14%)*. The nature of condition is such that we would not expect any obvious trend of increased or decreased use to emerge in future. There are also no clear links between the inclusion of this condition and the value of the deal.

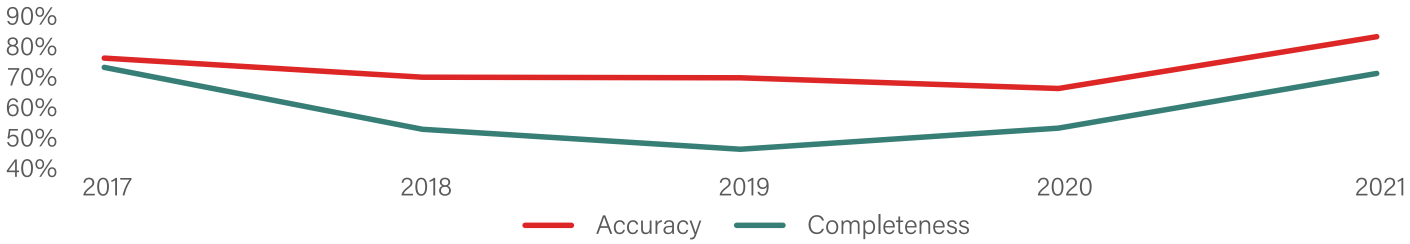
Warranties and liability limitations

Buyers and sellers in the Australian market are usually more flexible and willing to negotiate to come to a commercial arrangement on warranties and limitations. This is in contrast to other jurisdictions, such as in Asia, where parties typically insist on a more standard position.

Accuracy of disclosure materials

84% of our Australian deals in 2021 included warranties regarding the accuracy of disclosure materials. The accuracy of disclosure materials is of fundamental importance to acquirers, since the whole of their diligence process relies on the information provided by the seller to be true.

Warranties - accuracy and completeness of disclosure materials | 2017 - 2021



[% of deals using an accuracy or completeness warranty of disclosure materials]

Completeness of disclosure materials

A completeness warranty involves the seller warranting to the buyer that it has disclosed all information which a reasonable buyer would require to make an informed decision. In 2021, we saw a significant uptick in the percentage of our Australian deals that included a completeness warranty (72% compared to 54% in 2020 and 47% in 2019). This was a reversal of a downward trend last seen in 2019, perhaps indicating a post-pandemic increased sensitivity on the part of buyers to ensure that they have all of the available information before making an investment.

Anti-bribery and corruption warranties

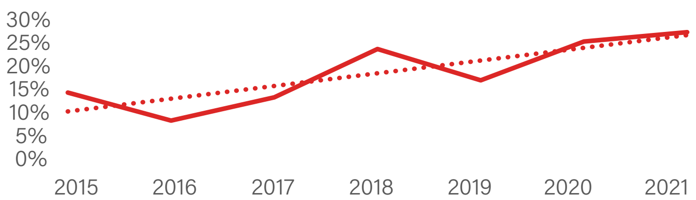
We continue to see an upward trend in the usage of anti-bribery and corruption (**ABC**) warranties since 2015. 2021 set a new record (28%) since our study commenced, with ABC warranties now present in more than a quarter of our Australian deals.

An ABC warranty is a warranty (usually by the seller) that the target and its related entities have not breach any of the anti-money laundering (or similar) laws.

Australia's ABC laws have become more stringent in recent years, driven by international, high-profile prosecutions of corruption around the world. As with conditions for FIRB approval, we expect to see more deals including ABC warranties to give the buyer comfort that they are not inheriting unwanted future liabilities.

With the increasing spotlight on ABC, and AUSTRAC's growing presence in the M&A environment, we expect this upwards trend to continue.

Anti-bribery and corruption warranties | 2015 - 2021



[% of deals using an anti-bribery and corruption warranties]

Monetary liability cap on warranty claims

The average maximum liability caps as a percentage of the purchase price for the different types of warranties (title, general and tax) in our 2021 Australian deals remained similar to those in 2020 for maximum aggregate liability and title warranties and noticeably decreased for general warranties and tax warranties. The lower average liability caps in 2018 and 2019 appear to be an anomaly in the context of the longitudinal data.

	Maximum aggregate liability	Title warranties	General warranties	Tax Warranties
2016	100%	100%	50%	63%
2017	93%	99%	72%	88%
2018	54%	77%	45%	54%
2019	67%	62%	49%	60%
2020	81%	89%	72%	86%
2021	80%	83%	62%	63%

Limitation of liability - time limits

The table below examines the time limits within which a buyer was required to bring a claim for a breach of warranties in our 2021 Australian deals. The data is broken down to illustrate time limits for three categories of warranties: title warranties, general warranties and tax warranties.

		General warranties (months)	Title warranties (months)	Tax warranties (months)
Uncapped		10% of deals had uncapped time limits for general warranties	14% of deals had uncapped time limits for title warranties	13% of deals had uncapped time limits for tax warranties
Capped deals	Mode	36	84	84
	Average	30	56	67
	High	84	84	84
	Low	9	6	2

The longitudinal data indicates that every year a substantial proportion of Australian deals have no time limit within which the buyer must bring any claim against the seller. The time bar is a powerful mechanism for limiting the seller's liability for warranty claims. It cuts off all claims after an agreed period after sale completion elapses. It is one of the most basic protections for the seller, allowing the seller to rest easy after the agreed period, knowing that no further claim can be made. 90% of our 2021 Australian deals included a time bar applying to at least some warranties, a higher proportion than in any other year since our longitudinal study began in 2014.

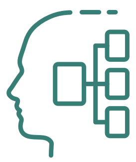
We typically see a higher proportion of our Australian deals have no cap for title (2021: 14%) and tax warranties (2021: 13%), than no cap for other warranties (2021: 10%). This differential has typically been even more marked in earlier years of our study. Title and tax warranties are often called out for separate treatment, as they are seen as of fundamental importance. Where time bars apply, title and tax warranties typically have longer time bar periods than other warranties.

Our 2021 Australian deals demonstrated a widespread preference for longer than usual warranty periods. The uncertain business conditions in the wake of the pandemic may explain buyers' insistence on longer periods for warranty breaches to emerge.

Limitation of liability - buyer knowledge

The study examined whether the buyer's knowledge qualified the warranties. That is, whether a buyer is contractually prohibited from bringing a claim against the seller for a breach of warranty if the Buyer knew (before signing the sale agreement) that the warranty was not accurate.

As a general common law principle, a buyer cannot bring an action for breach of warranty if the buyer was aware of a breach of warranty before signing. Alternatively, the damages awarded will be reduced to take into account the knowledge of the buyer. In some jurisdictions, parties can seek to contract out of this. In the US, buyers will often include a provision which provides that it will not be restricted from bringing a claim due to knowledge of a breach. The final position will often depend on the bargaining power of the parties.



In **82%** of agreements, buyer knowledge limits seller liability on warranty claims

10% of these agreements were limited by the constructive knowledge of the buyer

90% of these agreements were limited to the actual knowledge of the buyer

In 82% of our 2021 Australian deals, the buyer's knowledge that a warranty was not true qualified the seller's warranties.

In 90% of our 2021 Australian deals that included buyer knowledge as a warranty qualifier, the seller's liability was only limited by the *actual knowledge* of the buyer. With this drafting, the seller would have to demonstrate that the buyer had direct and clear knowledge, and actually knew of a breach. Actual knowledge is difficult to prove, and the seller may need to find circumstantial evidence showing the buyer's actual knowledge to successfully qualify the relevant warranty.

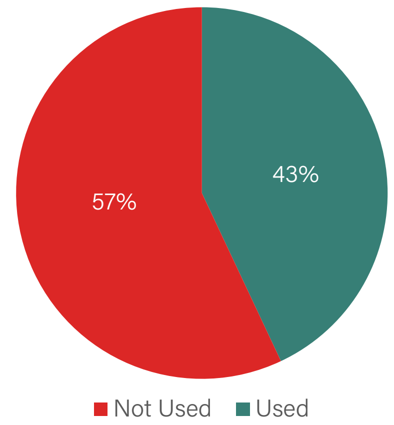
Constructive knowledge is knowledge that a reasonable person is presumed to have, regardless of whether the buyer actually possessed it or not. There is often room for dispute about the extent of constructive knowledge. As such, buyers typically resist agreeing to qualify the seller's warranties by their constructive knowledge. They also typically do not like the idea that their recovery for warranty that the seller has wrongfully given should be limited by the buyer being held to a standard of conduct that it has not achieved. In this light, it is surprising that as many as 10% of buyers in our 2021 Australian deals accepted the constructive knowledge of the buyer should qualify the seller's warranties.

Limitation of liability - disclosure materials

The seller's warranties were qualified by the seller's disclosure materials or other information that the seller disclosed to the buyer in 93% of our 2021 Australian deals.

During the whole of our longitudinal study, disclosure materials have qualified the seller's warranties in a range of 63% - 83% of Australian deals. Half of the studied years saw percentage use of this qualifier in a narrower band around the mid-70s. The increase to 93% in our 2021 Australian deals is very marked and indicates a near-uniform market practice has emerged.

Regulatory Approvals | 2020



[% of deals involving disclosure in respect of some warranties v all warranties]

Warranties qualified by public searches

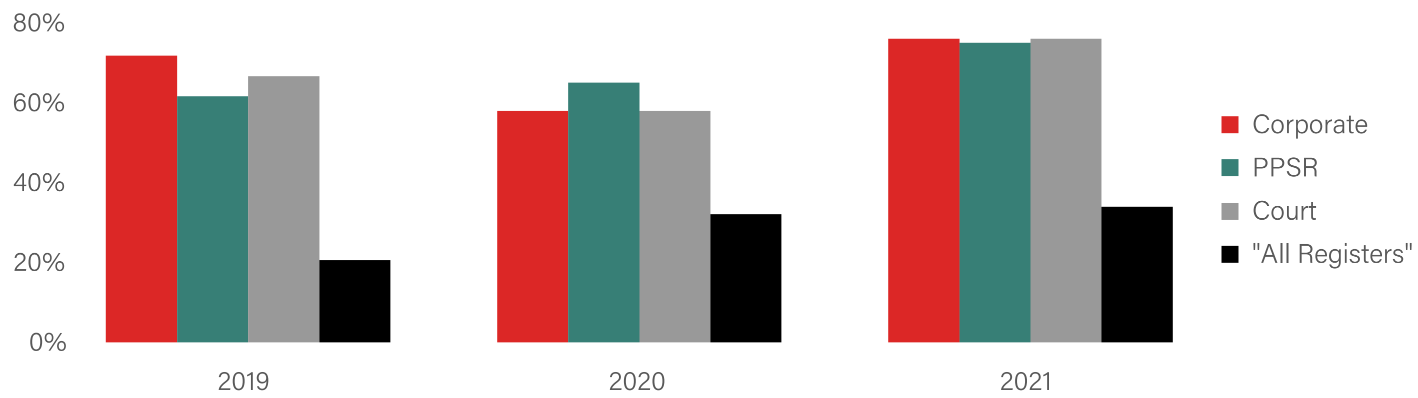
The inclusion of a warranty qualifier for information available in public searches puts the onus on the buyer to perform the specified searches before proceeding with the transaction.

The seller's liability for breach of warranty was qualified by information available in public searches in 90% of our 2021 Australian deals. This is a significant increase from previous years (2020: 67%, 2019: 76%), suggesting it has become a more uniform market practice to qualify warranties for information available in common public searches.

Of the deals which had some form of public search limitation of liability, we found that seller liability would typically be limited by these searches:

- corporate searches (in 76% of our 2021 Australia deals with a public search warranty qualifier)
- PPSR searches (in 75% of our 2021 Australia deals with a public search warranty qualifier)
- litigation searches (in 76% of our 2021 Australia deals with a public search warranty qualifier)
- "all registers open to the public" (in 34% of our 2021 Australia deals with a public search warranty qualifier).

Searches qualifying warranties | 2019 - 2021

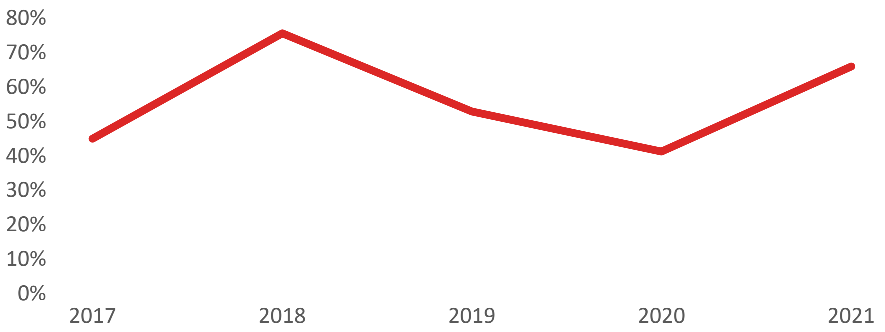


When the seller's disclosures qualified the seller's warranties, the qualification applied all warranties in 55% of our 2021 Australian deals. During our study, there has been a downwards trend in whether seller disclosure qualifies all warranties. It therefore appears that while there is now a near-uniform market practice for seller disclosure to qualify warranties, buyers are increasingly requiring that the qualification only apply to some warranties. Warranties that are typically carved out from being qualified by seller disclosure are title and tax.

Our 2021 Australian deals also saw a greater use of disclosure letters – at 67% of our 2021 Australian deals – noticeably more than the typical percentage use in the high 50s during the other years of our study.

In terms of the standard to which seller disclosure was required to be made, "fairly disclosed" was the most common standard (76% of our 2021 Australian deals), followed by "disclosed" (17%) and "fullly and fairly disclosed" (7%).

Management Accounts Warranties | 2017 - 2021

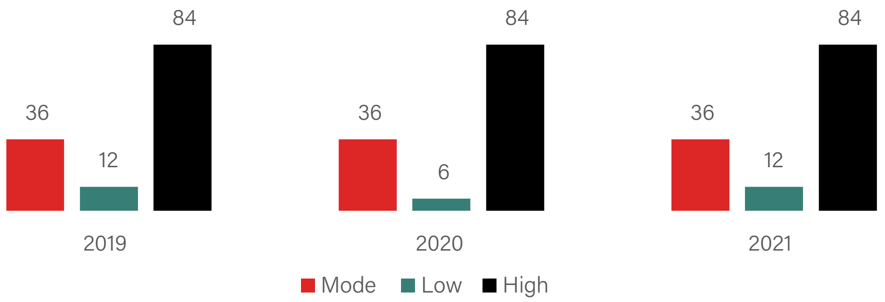


[% of deals where seller disclosure materials qualified the seller's warranties]

Restraints

A 'restraint' is a restriction on a seller (or an employee or personnel of the seller) which stops them from competing with the target business for a certain period after completion. Restraints were included in 66% of our Australian deals in 2021, more than in any other year in our study and in the order of double the percentage use in the years since 2018.

Restraint period in months | 2019 - 2021



[Number of months where a restraint period was applied]

Restraint provisions prevent the seller from setting up a competing business or operation following completion. Buyers typically do not wish to pay for businesses that lose value because customers follow the seller in a new incarnation of the old business.

The restraint period varies widely – from 12 months to 7 years, but in recent years the consistently most commonly agreed restraint period is 3 years. In seeking a certain duration for the restraint period, sellers should consider what their legitimate business interests really require, as courts are unwilling to enforce restraints they determine exceed this standard.

Australian private M&A deal trends report
2021 Edition

Deal Protection

Deposit

The use of deposits returned to trend in 2021 Australian deals, at 11%. Use of a deposit in Australian deals since 2014 has typically been in the 10-13% range, with a couple of years unusually high at 19% and 2020 unusually low at 4%.

Deposits represent a commitment by the buyer, giving them "skin in the game" – a sunk cost incentivising them to complete the transaction.

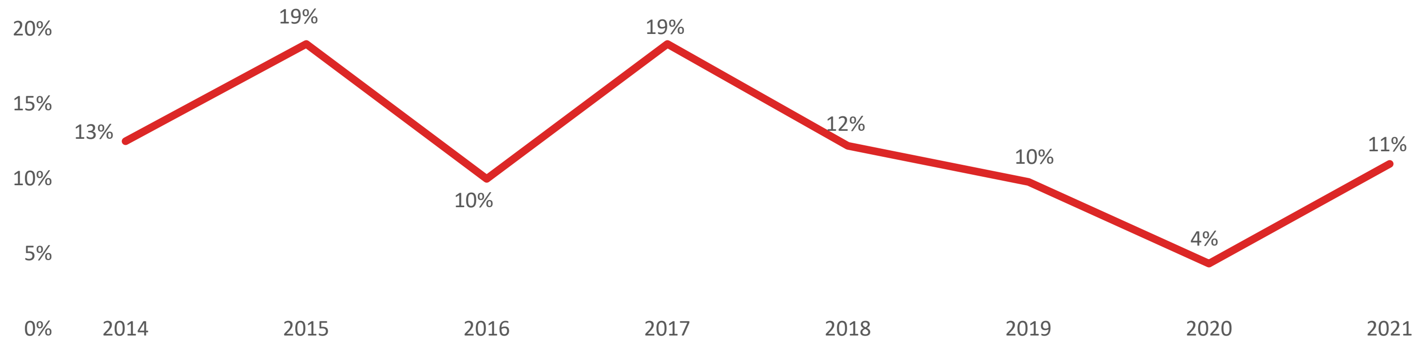
Reliance on deposits as a method of deal protection is not common in larger Australian deals. We typically see very few deals in excess of $50 million involving the use of a deposit. We would expect acquirers to resist providing a deposit in larger deals, in part relying on market practice and in part asserting their bona fide intent to complete the transaction is beyond question.

In **11%** of deals a deposit was paid by the buyer

Average deposit: **7%** of purchase price

Highest deposit: **20%**
Lowest deposit: **1%**

Number of deals where deposit was paid | 2014 - 2021

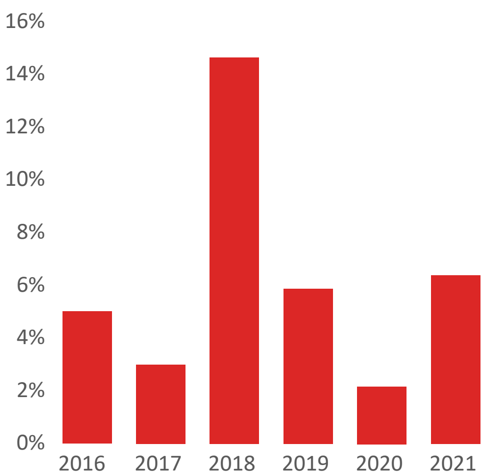


[% of deals using a deposit]

Break fees

It is relatively rare for private M&A deals in Australia to include break fees – which is a payment made by the seller (or the target itself) to the buyer if the deal once signed does not complete. In even rarer instances in private M&A, a reverse break fee may be payable, with the buyer liable to pay the seller a fee if the deal does not complete. A break fee was only included in 6 of our 94 Australian deals in 2021 (6%).

Number of deals with a break fee | 2016 - 2021



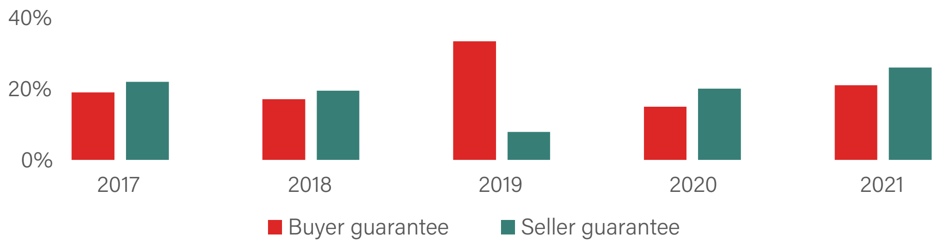
[% of deals with a break fee]

Guarantees

Guarantees are used where, in the opinion of one party, another party does not have the requisite financial capacity to complete its obligations under the transaction.

The most common example of when the seller may require a guarantee is if the buyer is using a special purpose vehicle to make the acquisition. The most common example of when the buyer may require a guarantee is in an asset sale, which will result in the seller becoming a cash box for a time, with proceeds then likely to be distributed to its shareholders.

Buyer and Seller Guarantees | 2017 - 2021



[% of deals where there were guarantees]

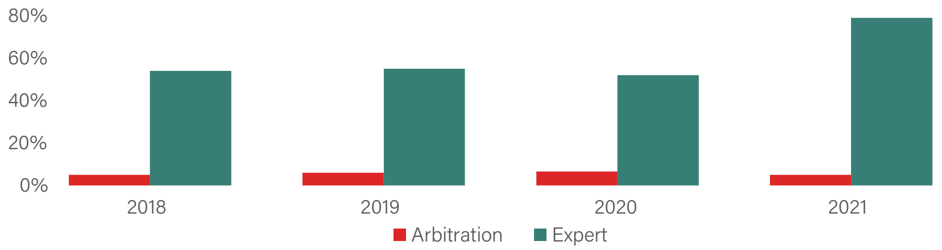
In 2021, a buyer guarantee was given 21% of our Australian deals and a seller guarantee was given in 26%. This was a moderate rise for the use of both a buyer's guarantee (15% in 2020) and a seller's guarantee (20% in 2020). The results indicate that whilst guarantees are not the norm in Australia, they are not out of the ordinary, as they are seen in at least one in every four deals.

Dispute Resolution

As expected, litigation was the default dispute resolution mechanism applicable to almost all of our 2021 Australian deals. However, parties also elected to use arbitration and/or experts to resolve disputes. Unsurprisingly, given earlier results of our study, arbitration clauses were only present in a small minority of our 2021 Australian deals (5%). This is consistent with the use of arbitration in Australian over the course of our longitudinal study, which is typically in the 5-7% range. Arbitration tends only to be used where one of the parties is located in another country. This is on the basis that arbitral awards are typically easier to enforce in other countries, compared with decisions of Australian courts.

Since we started tracking the use of expert determination as a dispute resolution mechanism in 2018, we have seen almost all parties use expert determination as their only alternative dispute resolution mechanism. Expert determination was used in 79% of our Australian deals in 2021. Expert determination typically only applies to a limited issue, such as for disputes about the preparation of completion accounts and their resulting impact on the post-completion adjustment mechanism (such as for working capital or net assets). Litigation is still applicable for disputes on the remainder of the deal, meaning the overwhelming number of our Australian deals rely on litigation as the primary dispute resolution mechanism.

Dispute Resolution | 2018 - 2021



[% of deals using experts or arbitration]

M&A trends to look out for in 2022

Divestures, demergers – a focus on core capabilities

Divesture activity is on the rise, particularly among large corporations, which have begun reviewing business portfolios and selling underperforming or non-core businesses in order to achieve greater financial and operational agility. Larger cash reserves mean businesses have more opportunity to acquire targets that will bolster the performance of their core business. Similarly, disposing of business arms riddled with operational complexity encourages companies to focus on achieving their long term strategies.

Supply chain

Major supply chain issues are expected to persist in 2022. We expect companies, particularly in the manufacturing industry, to strengthen their supply chains and become more self-sufficient by seeking vertical integration transactions in order to secure and supply raw materials and control distribution channels. Supply chain woes may also see earn-outs being favoured by acquirers as confidence declines over forecasts based on estimates excluding supply chain delays.

Digital transformation

The focus on digital transformation in business operations has been gathering pace over the past several years. With benefits such as process simplification and automation, it should come as no surprise that one to two years of remote working caused by COVID-19 has only accelerated the scale and speed of this adoption.

Technology has the ability to accelerate all parts of a transaction's deal process and execution. Many companies have begun utilising a range of technologies at their disposal. In order to maximise opportunities and stay with the pace of digital disruption, companies need to ensure the right technology partners are brought on board. Once again, data analytics and cybersecurity are primed to be trends that impact the M&A process and pursing digital transformation will be an M&A driver.

Spotlight on ESG

Environmental, social and corporate governance (ESG) is set to take centre stage this year. Deal makers have acknowledged an increasing regard for ESG considerations in the transaction process. For reasons including portfolio rebalancing and differentiation, sustainability has begun featuring in many corporate strategies as companies look to revalue their businesses. Global concerns ranging from addressing climate change to diversity and inclusion have attracted increased attention from investors, stakeholders, regulators and governments. The push for business transparency by the public has also forced executives to place these growing concerns at the top of the corporate agenda. According to experts, companies showing stronger ESG commitments have generated larger financial returns and are more resilient to economic shocks. This realisation may result in a flurry of deal activity in the coming few years as CEOs look to revaluate their environmental and social footprint by purchasing or divesting assets in line with this strategy. Additionally, operating model decisions are impacted as they become subjected to more stringent sustainability requirements. For this reason ESG has the potential to become a central deal driver and executives should expect to spend more time on ESG due diligence in the transaction process.

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Our office locations

On 7 March 2022 we announced that we are winding down operations in Russia and closing our Moscow office.

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