

A Chief Executive Group Exclusive Event

MANUFACTURING M&A DEALMAKERS FORUM

M&A Due Diligence

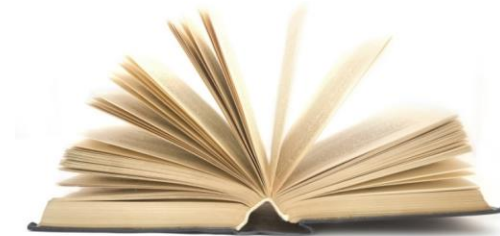
Done Right



George Casey and Clara Pang
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Discussion Outline

- > Current M&A market dynamics
- > What is due diligence?
- > Purpose of due diligence
- > How does due diligence work?
 - > One potential Buyer vs. auction sale
- > Due diligence as part of the deal process



Current M&A Market Dynamics

- **Pressure on buyers** to get things right and make an acquisition work
 - Valuation
 - Regulatory approvals
 - Cultural and ESG fit
 - Integration
- **Pressure on sellers** to get the best deal
 - Highest price
 - Deal certainty
 - Limited post-closing value impact
- **Search for growth** opportunities made the **world a global market place for M&A**
 - **Global market place** creates a particular dynamic
 - Regulatory hurdles
 - Currency issues
 - Cultural differences and expectations misalignment
 - Logistics, location and time difference



What is due diligence?

- > An information gathering and investigation of the target's **business, financial and legal affairs**
 - > Understanding, assessing and valuing
 - > the company's **business**
 - > **efficiency, reliability** and **risks** of its operations
 - > **sustainability** of the business and **growth potential**
 - > growth directly impacts value
 - > **governance** and **culture**
 - > strength of **relationships** with employees, customers, suppliers, regulators and communities in which the business operates
 - > key **dependencies**
 - > supply chain
 - > distribution channels
 - > logistics and infrastructure
 - > regulatory environment
 - > **financial results** and **business plan**
 - > actual and contingent **liabilities**
 - > **risks**



Purpose of due diligence – general

- > *Caveat emptor* – **what** do we think we are buying?
- > **Valuation**
- > Separation / **integration** / structuring
- > Pre-conditions / **consents** / **deal breakers**
- > **Liabilities**
- > Representations and warranties
- > **Indemnities**
- > Stimulate **disclosure**



Seller due diligence

The reasons why Sellers perform due diligence include:

- > Check that the business or company is in the **best possible condition** to facilitate the sale on the best possible terms
- > Prepare **financial statements** (audited) and review and test the **business plan**
- > **Identify** and assess contingent **liabilities**
- > **Identify potential issues** and the need for any **pre-sale restructuring**
- > **Assist tax structuring**
- > Assist **disclosure against the representations and warranties** in sale agreement
- > Ensure that **commercially sensitive** or **confidential documents** are not released to potential Buyers
- > **Facilitate** the **auction process**



Buyer due diligence

The reasons for Buyer's due diligence include:

- > To enable the Buyer **to check** what it is buying
- > To help the Buyer **to value the target**
- > Structuring
- > The need for **contractual protection** – e.g. indemnities and closing conditions
- > To **identify the consents** that are required
- > To **test the assumptions** made in the Buyer's business plan
- > **Integration** planning
- > To **avoid post deal disputes**



How does due diligence work?

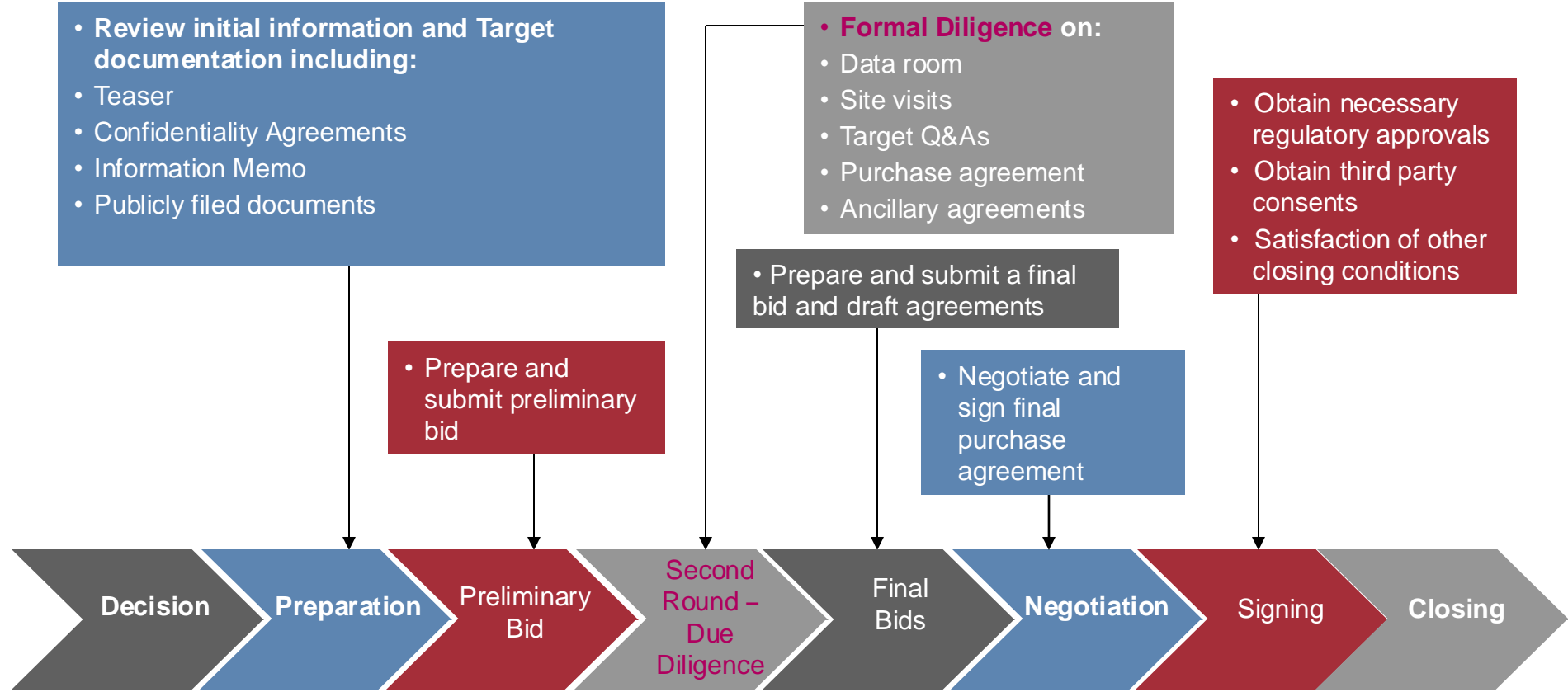
Bilateral sales (Buyer driven)

- > Buyer sends Due Diligence request list
- > Seller gathers documents for data room
- > Buyer reviews and follows up – Q&A?
- > Buyer feeds into negotiations and documentation
- > DD report – exceptions only trend

Auction sales (Seller driven)

- > Seller prepares information memorandum / data room
- > Buyers submit preliminary bids based on information memorandum VDD Report / data room, management presentation and site visits
- > Buyer's team may also produce Due Diligence report

Typical auction process



Notwithstanding the formal Due Diligence Phase, Buyer should start “diligence” early and continue until closing

Integration planning

The most **successful** “serial” **buyers** start integration planning when they start due diligence

- > Assemble a **separate team** that works alongside the deal team
 - > Joint meetings
 - > Testing and **challenging** due diligence findings
 - > Assessing **how** the business will **integrate structurally**
 - > Identifying and quantifying **synergies**
 - > Preparing for “**day one**”
- > Antitrust laws allow integration **planning** by Buyer **but not implementation/control** of operations and business decisions of Seller until the deal is done (in some jurisdictions, until antitrust clearances are received)



Identifying ultimate goals and tactical goals in deal process and negotiations

Ultimate goals:

- > Total **maximum value** we are prepared to allocate to the asset
- > Cash or stock
- > **Upfront purchase price**
- > How will it be **financed**
- > Purchase price **adjustment**
- > **Liabilities, risks** and potential **value exposure**
- > **Deal risks** – what may derail the deal
 - > What is the “**regulatory price**” for doing the deal?

Tactical goals

- > **Buyer without an auction**
- > Buyer in an **auction**
- > **Seller without an auction**
- > **Seller** in an **auction**

Don't let deal momentum take hold and **shift you away from the ultimate goals**

On the other hand, **focusing too much on tactics** to take advantage on the counterparty **may backfire** long-term



How CEO/Lead Executive should organize the deal team and process

Have the **best team** for the job – internal and external

Check on the team's **progress**

- > Ask for a **realistic assessment** of
 - > Due diligence findings and the open **issues**
 - > **Timing** of solving them

Don't hold the team in fear – people will not be open about real issues and will have hard time making decisions if they are not empowered

Trust and delegate to the team, agree on positions and do not get directly involved unless and until needed

When getting involved **in negotiating key aspects** of the transaction with the direct counterparty:

- > **Get briefed** by the deal team
- > Prepare to **address key issues** but be **cognizant of other issues** that are open
- > Have the deal **team leader and your counsel with you** for the meeting
 - > Often **miscommunications** happen if CEOs meet just by themselves
 - > Your **counterparty** can “**play games**” if there is no one else in the room
- > **Stick to the agenda** and discuss the **key issues and let the deal team work out the details**
- > Do not assume that the deal is “done” after that meeting
 - > Is there such a thing as “**details**”?
- > **Don't let the deal team fall in love with the business you are considering buying**

