

Q&A

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FINLAND: A FAVORABLE OUTLOOK

As the Finnish M&A market continues to perform strongly, Helsinki-headquartered law firm Borenius highlights the increasing convergence of capital markets with traditional M&A.

Finland's M&A environment remains robust. Figures from corporate intelligence agency Mergermarket show that during the first 11 months of 2014, deal volume climbed to 134 deals, up from 130 during the same period in 2013. Importantly, Finland's transactional performance is supported by several factors, with good access to financing being a prominent driver of M&A.

Finland's private equity scene also continues to look healthy. The first six months of 2014 represented one of the most active years ever for private equity in Finland, with 223 private equity investments made in Finnish companies, according to figures from the Finnish Venture Capital Association (FCVA). Most notably, early stage companies attracted a record amount of foreign investment, with foreign venture capitalists investing around \$24 million (EUR20 million) through a total of 22 investments - the highest number of investments since 2008.

As foreign investors flock to Finland, partners from Attorneys at law Borenius discuss the key trends affecting the country's M&A market.

Established in 1911, Attorneys at law Borenius is one of the largest and most experienced law firms in Finland. The firm's services cover all areas of corporate law.

In addition to its national offices in Helsinki and Tampere, the firm also has a well-established office in St. Petersburg, which regularly advises both Russian and foreign clients in cross-border transactions involving Russia. The firm also has a representative office in New York.

WHAT IS THE CURRENT ENVIRONMENT FOR M&A DEALS IN FINLAND?

BORENIUS: Activity in Finnish M&A remained

strong in 2014 after a busy 2013. According to data compiled by Mergermarket there were 134 announced deals during the first 11 months of 2014, compared to 130 deals during the same period in 2013. The aggregate disclosed deal value for announced acquisitions of Finnish targets decreased slightly to approximately EUR9.8 billion in the first 11 months of 2014, compared to EUR10.1 billion in the same period in 2013. Part of the reason for the slight year-on-year decline in value was Nokia Corporation's EUR5.44 billion sale of its mobile phone business to Microsoft in 2013.

The deal-making environment remained on a similar level to 2013, despite the turmoil in Russia, which is providing a challenging outlook for the Finnish economy. The availability of financing has remained good, with the adoption of the Finnish high-yield bond market in the beginning of 2014 adding liquidity to the leveraged finance market.

There are certain signs that the market will continue to improve, which is supported by the increased level of large structured deals and the enhanced presence of dual-track processes. Most deals are still being prepared and negotiated quite extensively and the number of failed structured sales processes has increased. The number of IPOs have also contributed to the market in 2014, as the market regulated (MTF) First North Helsinki NASDAQ OMX has attracted several growth companies to seek listings. There have been six completed listings to the NASDAQ OMX Helsinki First North market in 2014 and two listings to the NASDAQ OMX Helsinki official list.

WHAT HAVE BEEN THE MOST ACTIVE INDUSTRY SECTORS FOR M&A DEALS IN FINLAND OVER THE PAST YEAR?

BORENIUS: We saw a rebound in big-ticket

deals within the more traditional sectors during 2014. In the biggest deal of the year, valued at EUR3.24 billion, Finnish banking group Pohjola acquired the shares it did not own in its subsidiary Pohjola Bank. In another sizeable deal, Swedish steel company SSAB acquired Finnish metal company Rautaruukki in a EUR1.8 billion transaction. In October 2014, Danish energy company Danfoss made a EUR1.04 billion tender offer for Finnish electric drive maker Vacon.

Activity in the healthcare sector has remained strong and the expected growth in future spending in the public health and social services sector has resulted in numerous deals and a strong pipeline. Headline healthcare transactions in 2014 included Nordic Private equity fund CapMan's public tender offer for Finnish nationwide dental clinic Oral Hammaslaakarit Plc, Swedish private equity fund Adelis' acquisition of healthcare provider Med Group, Finnish private equity fund Intera Partner acquiring Finland's largest eye care provider and second-largest optical retailer Silmäasema, as well as Triton and KKR-owned healthcare provider Mehiläinen acquiring healthcare provider Mediverkko.

Activity also remained strong in the energy and infrastructure sectors. In November 2014, E.ON and Fortum sold their shareholdings (20 percent and 31 percent, respectively) in Finnish gas company Gasum to the Finnish State for an aggregate compensation of EUR510 million.

THE FIRST HALF OF 2014 SAW 223 PRIVATE EQUITY INVESTMENTS MADE INTO FINNISH COMPANIES, WHAT IS ATTRACTING PE HOUSES TO THE FINNISH MARKET?

BORENIUS: The activity of private equity investors remained relatively high during 2013–2014, with the majority of deals falling into the midsize category. Many private equity investors are still

expected to come under increased pressure to dispose of portfolio companies already held beyond the planned investment horizon and to invest committed capital. In sales processes, the trend has moved towards a higher level of differentiation in terms

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of structure, with the popularity of large-scale controlled auctions decreasing and the focus instead shifting to more concentrated efforts with a limited number of bidders. Also the above mentioned healthcare sector has been one significant driver, although some sponsors are arguing that the valuation levels in healthcare are already too high.

WHAT ARE THE MOST COMMON FINANCING ALTERNATIVES FOR TRANSACTIONS?

BORENIUS: Most investments take the form of equity. There is a tendency towards preference shares replacing traditional shareholder loans. The reasons for this relates to new restrictions in the deductibility of interest in loans from related parties as well as to the fact that without a shareholder loan the parties may avoid the need for an intercreditor agreement. There also are some mezzanine funds actively operating in the market, but given the relatively small deal sizes and good availability of senior

financing, mezzanine is quite seldom used.

Deals are also leveraged, as everywhere else in Europe, depending on the market conditions and availability of debt financing. In 2014, we saw a strong emergence of the Finnish high-yield bond market and some of the deals were financed by high-yield.

A traditional senior secured term loan facility made available by a bank or a club/syndicate of banks is still the most common source of debt financing in the Finnish private equity market. Credit funds and other non-traditional lenders have not been active in Finland so far.

In 2014, high-yield bonds made their foray into Finland, both as corporate bonds as well as private equity bonds, and instantly became a real alternative to replace part of the senior financing (or the entire mezzanine financing). Investors seem to have an increasing appetite for them. Similarly, the absence of maintenance-based financial covenants is deemed by private equity sponsors as a key benefit of high-yield bonds. For example, in May 2014, Paroc Group, which was taken over by its lenders in 2009, issued a EUR430 million six-year U.S. high-yield bond and Elematic Oy Ab, a portfolio company of Pamplona Capital Management, issued a EUR35 million four-year high-yield bond. In September, AC Alpha Oyj, a portfolio company of Ahlstrom Capital Oy, issued a EUR65 million unsecured and unguaranteed high-yield bond to finance the acquisition of Destia Oy, a Finnish infrastructure company. We expect more private equity sponsors to tap the high-yield bond market in the future, particularly as a source of refinancing existing portfolio company debt.

WHAT ARE THE PREFERRED STRATEGIES FOR EXIT IN FINLAND?

BORENIUS: The most common exit strategy is still through a trade sale. However, unlike in the past, genuine

dual-track sale processes have become much more popular. This is due in great part due to the demand for European equity by many institutional investors and due to successful IPO exits in Sweden.

Trade sale

Finnish funds generally limit their liability extensively in sale and purchase agreements when exiting an investment. Usually, only the most fundamental warranties (title, capitalization) are given in the name of the funds, and management shareholders tend to take on more extensive liability. It is very typical for general liability to be limited to 10-30 percent of the exit value and for warranties to be in force for no longer than 12–18 months (usually liability past the next audited accounts is accepted). Title and capitalization warranties are usually excluded from the general limitations of liability.

It is not uncommon for escrow structures to be used in order to guarantee the availability of funds in cases of breach. A typical escrow period tends to reflect the agreed claim period and covers some 10 percent of the purchase price paid, again depending on the agreed total liability cap.

However within the last 12 months Finland has seen a surge in the use of W&I insurances. Although the insurance is usually taken by the buyer, especially in an auction process it is often encouraged to do so by a private equity seller.

IPO

While the London Stock Exchange saw 10 times as many IPOs in the first half of 2014 as in the first half of 2013 and while the Swedish market also had very increased activity in terms of private equity exits, this unfortunately has not materialized as an exit strategy in Finnish leveraged buyouts. There have been a few dual-track processes, which in the end have led to trade sales. The rather small size of the private equity target companies is one of the primary reasons

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for the unattractiveness of the IPO exit market in Finland. At the same time, the trade sale exit alternative has proven faster and cheaper to implement and generally more effective to investors and shareholders.

The substantive liability of the investors as selling shareholders depends largely on the detailed contents of the underwriting agreement or similar contractual arrangement with the lead arranger of the IPO. Typically, the issuing company itself will give more extensive warranties to the underwriter. The selling majority shareholders (such as private equity investors) generally succeed in limiting their warranties to the fundamental facts such as ownership and authority etc. It is more likely that the management or other private shareholders have to agree to more extensive substantive warranties as well as lock-up periods, which usually range from six to 12 months. Also private equity shareholders often have to agree to lock-up periods. As the board of directors of the issuer is required to guarantee the accuracy of the IPO prospectus, the composition of the board of an IPO candidate is sometimes changed prior to the IPO itself as the investor's representatives in the board may wish to drop out and other outside industry experts or professional board members and corporate governance

specialists join the company. The current Finnish Corporate Governance Code requires that the majority of the directors shall be independent of the company and in addition, at least two of the directors representing the majority shall be independent of the significant shareholders of the company.

WHAT IS THE PLAYING FIELD FOR PUBLIC-TO-PRIVATE TRANSACTIONS?

BORENIUS: We occasionally see private equity players launching tender offers for listed companies in Finland. Such deals are often friendly negotiated deals with an attractive premium where the majority stakeholders are committed to the deal. A few years ago, despite lower valuations, the unavailability of acquisition finance hindered such offers, but more recently the market has picked up and deals have been announced, or are being negotiated or proposed. Under the Finnish takeover rules, a bidder must disclose the financing arrangement necessary to consummate the bid, and the target's board will most likely require that a financing commitment be in place at the time of the execution of the combination agreement.

The Finnish mid-cap listed companies have been attractive acquisition targets due to their small size and concentrated ownership pools, combined with strong local positions in their respective markets and global potential.

The key issues in a public tender offer in Finland for a private equity fund are no different from other markets. Financing is clearly a concern, as well as getting firm commitments from main shareholders and negotiating the terms of the deal (including pricing, premium and closing conditions among other things) with the target's board. Larger cross-border deals would naturally be subject to competition law scrutiny as well. The acquisition of a Finnish target company in a defense-related or otherwise

strategically crucial sector may also be subject to government approval.

An updated and slightly revised Takeover Code came into force on 1 January 2014. Much like its predecessor, the new Takeover Code contains recommendations regarding the actions applicable to public takeover bids. The Helsinki Takeover Code addresses questions and practices related to the actions of both the bidder and the target company, as well as the management and shareholders of the target company. The obligation to comply with the Helsinki Takeover Code is based on the provisions of the Finnish Securities Markets Act and the 'comply or explain' principle. Hence, in its announcement, the bidder must also declare whether it will adhere to the Code or not and give a reasonable explanation for non-adherence, if any. The Code is also available in English, as are the Finnish Securities Markets Act and all of the regulations issued by the Finnish Financial Supervisory Authority.

WHAT SUPPORT CAN BORENIUS PROVIDE TO CLIENTS LOOKING AT M&A AND PRIVATE EQUITY TRANSACTIONS?

BORENIUS: Our strategic initiatives that derive from the 1990s private equity environment in Finland have helped us to secure a leading position both in fund formation and deal making. Our market share in fund formation and secondaries has for many years been over 50 percent, giving the firm unprecedented access to both to private equity funds and their investors. We have represented a deep list of private equity and venture capital houses in making investments and exits, as well as target companies' management in these transactions. Additionally our tax practice, which is the largest of any Finnish law firm, puts us in the excellent position where we can provide 'the whole deal' to our PE customers.

We advised on 30 M&A transactions

during the first 11 months of 2014. These transactions included, among others, the voluntary public tender offer for the shares in NASDAQ OMX Helsinki-listed

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Oral Hammaslääkärit plc, where we acted as the legal advisor to the offeror CapMan, the sale of Paroc Oy to the funds managed by CVC for EUR700 million, which was preceded by the EUR430 million high-yield bond Paroc issued a few months earlier, and most recently the sale of a 50 percent stake in Gasum to the Finnish State for EUR510 million, where we represented the sellers E.ON and Fortum.

In 2014 our capital markets practice was particularly active in high-yield transactions for corporate and private equity issuers. In the first eleven months in 2014, we advised on six completed high-yield deals, which is more than any other Finnish firm on the market. In addition to our high-yield experience, we have also been involved in IPOs as an exit alternative for private equity and corporate shareholders.

ABOUT THE AUTHORS:

Jari Vikiö, managing partner
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Jari advises on banking and finance, M&A and private equity related transactions with particular emphasis on large and medium size deals.

Jari has been involved in numerous large domestic and cross border mergers and acquisitions and frequently represents various domestic and international private equity houses and other companies in transactions. He also acts as a member of the board of directors in many portfolio companies advising on corporate issues.

Jari has been a partner at Attorneys at law Borenius since 2001, and managing partner since 2008.

Juha Koponen, partner and head of capital markets

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Juha Koponen is a dual-qualified (Finland and New York) transactional lawyer, who focuses his practice on capital markets, M&A and private equity transactions. He has advised issuers and underwriters on public and private offerings of equity and debt securities, including IPOs, high-yield debt offerings, convertible debt issuances and rights offerings. He has also advised bidders and target companies on tender offers.

Prior to joining Attorneys at law Borenius in March 2014 as the head of capital markets, Juha was a partner with another major Finnish law firm. His prior experience includes working as an associate at Fried, Frank, Harris, Shriver & Jacobson LLP for three years (New York and London) and as a corporate legal counsel at Nokia Corporation focusing on securities regulation.

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Johannes advises clients on a wide range of issues relating to private equity, mergers and acquisitions, ownership structuring and fund formation.

Johannes has been involved in numerous domestic and cross-border transactions acting for both private equity sponsors and industrial clients. Further he has advised clients in ownership and equity structuring in infrastructure projects, and in general corporate matters.