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## Current trends in M&A

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### Introduction

- We have been seeing an increase in Merger & Acquisition (M&A) activity in the market place over the last few years. We expect to see more activity in the market going forward due to a number of drivers.
- As part of this session, we will discuss the recent trends in the market, looking at some recent activities and exploring the drivers behind them. We will also provide a detailed walkthrough of the different phases of a deal and the considerations in each of these phases.



## Agenda

1. Trends
2. Observation of changing process
3. Summary

### Disclaimer

- The views expressed in this presentation are those of the presenter
- This presentation is of a general nature and is not intended to address the circumstances of any particular individual or entity



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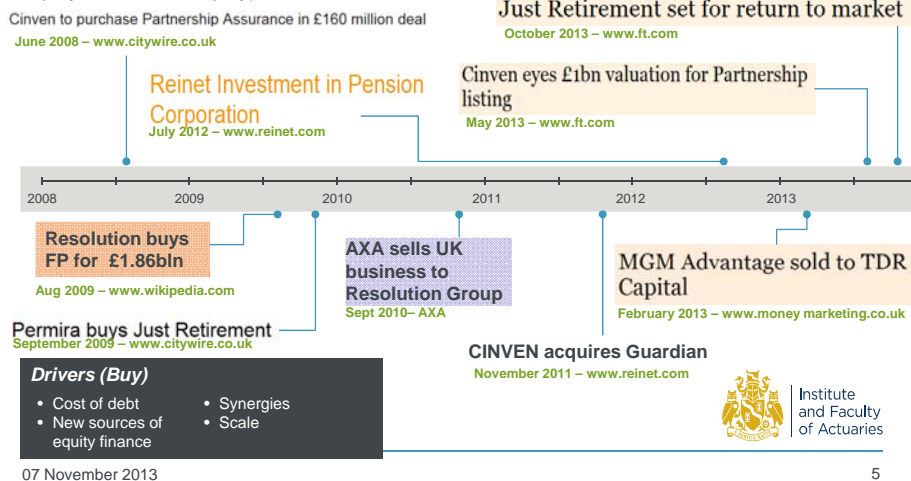
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## Trends

Expertise  
 Sponsorship  
 Thought leadership  
 Progress  
 Community  
 Sessional Meetings  
 Education  
 Working parties  
 Volunteering  
 Research  
 Shaping the future  
 Networking  
 Professional support  
 Enterprise and risk  
 Learned society  
 Opportunity  
 International profile  
 Journals  
 Support

## UK Private & Public Equity

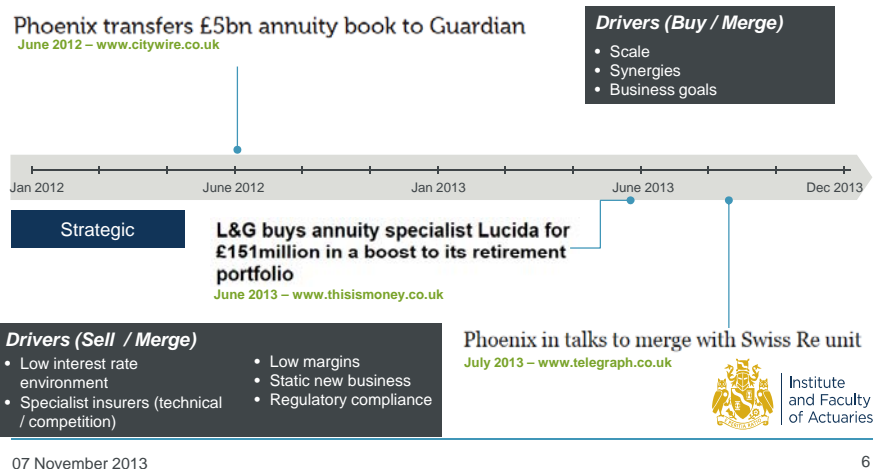
In the UK, transaction activity is starting to build up pace, driven by new money (Private Equity and Public Equity)



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## UK Strategic

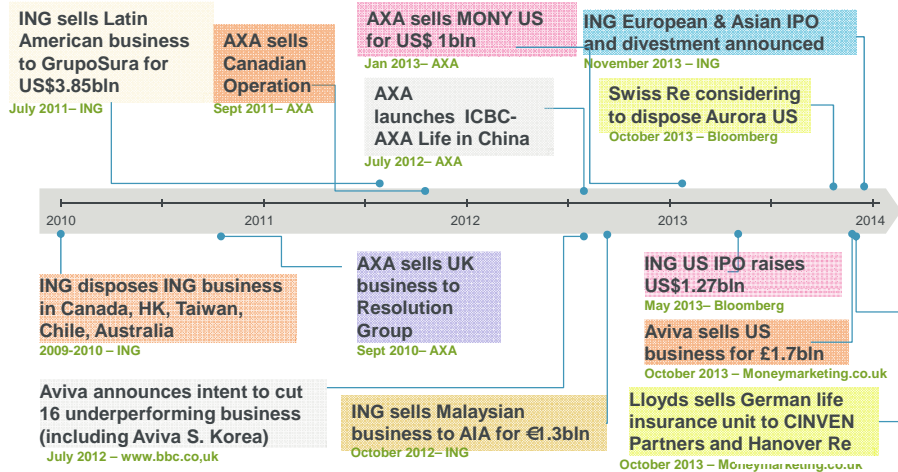
We also see strategic moves driven by either external or internal factors



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## European

There have been a number of activities in the wider European markets



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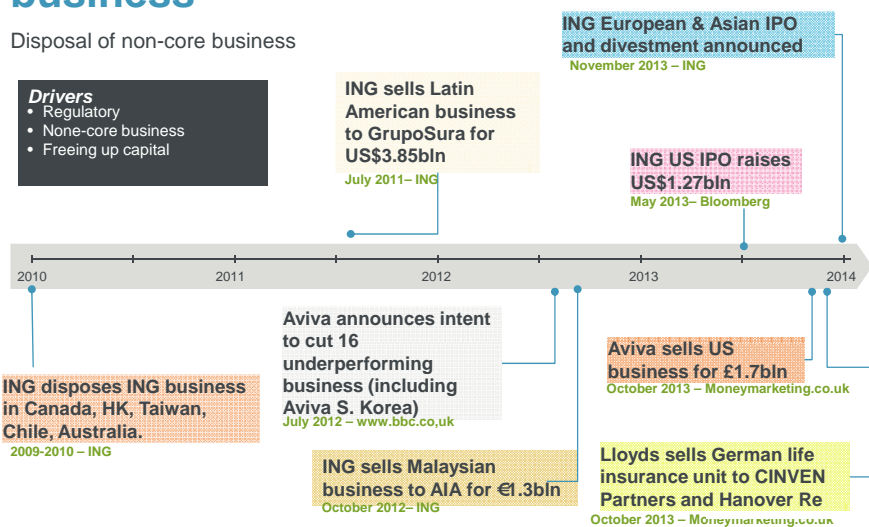
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## European – Disposal of none core business

Disposal of non-core business

### Drivers

- Regulatory
- None-core business
- Freeing up capital

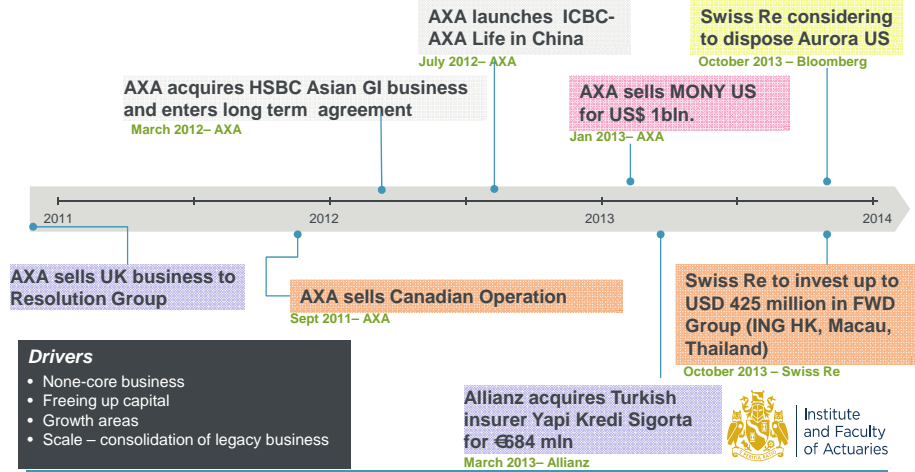


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## European - Strategic

There have been a number of activities in the wider European markets

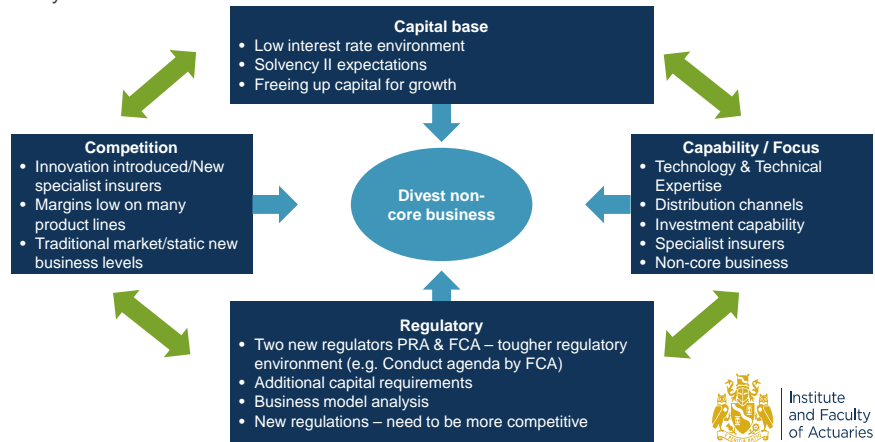


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## Drivers – Seller

There are a number of drivers for firms seeking to consolidate away from non-core activity, many of which are inter-linked.

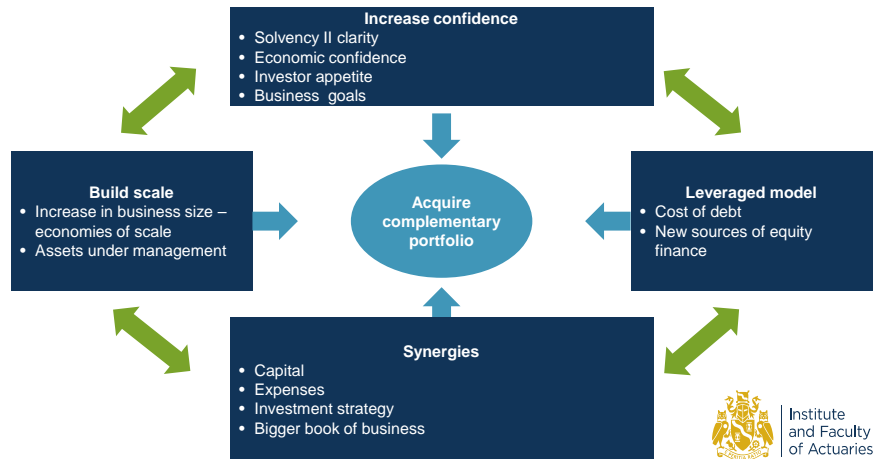


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## Drivers – Buyer

The acquiring firms are able to gain the following benefits:

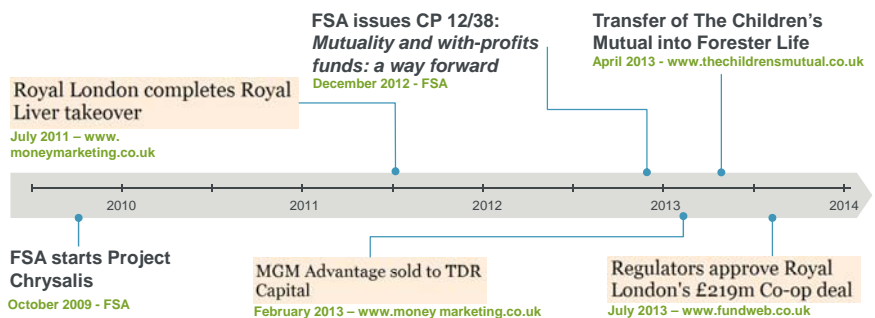


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## Mutuals

The mutual sector has continued to consolidate



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## Mutuals – Drivers and Challenges

We expect more consolidation in the Mutuals market

### Key Drivers

- **Tougher regulatory pressure:** Prior pressure from Project Chrysalis but FSA has taken a new approach through CP 12/38. What is the new FCA's view/approach?
- Close book business, business in run off. Many small and medium mutuals with **inefficiencies**.
- Increasing expense ratios
- Return on policyholder's assets becoming challenging
- Solvency II

### Challenges

- Value of independence and identity: Pride, affinity groups, history.
- Different business constitutions, rule books, charters, and even Acts of Parliament. Makes it hard to integrate.
- Member votes – different profile of members (cohorts)
- Delegate mutuals



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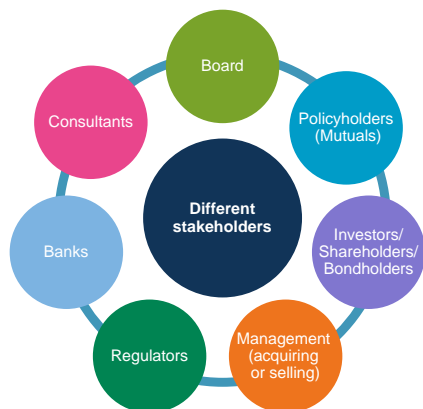
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## Observation of changing process

Expertise  
Sponsorship  
Thought leadership  
Progress  
Community  
Sessional Meetings  
Education  
Working parties  
Volunteering  
Research  
Shaping the future  
Networking  
Professional support  
Enterprise and risk  
Learned society  
Opportunity  
International profile  
Journals  
Support

## Stakeholders

- Transaction involves a number of stakeholders. Balancing these interests is key to ensuring the deal could be finalised.
- In the following slides, we walk through a transaction time-line and highlight how perceptions and views are evolving and influencing the process.



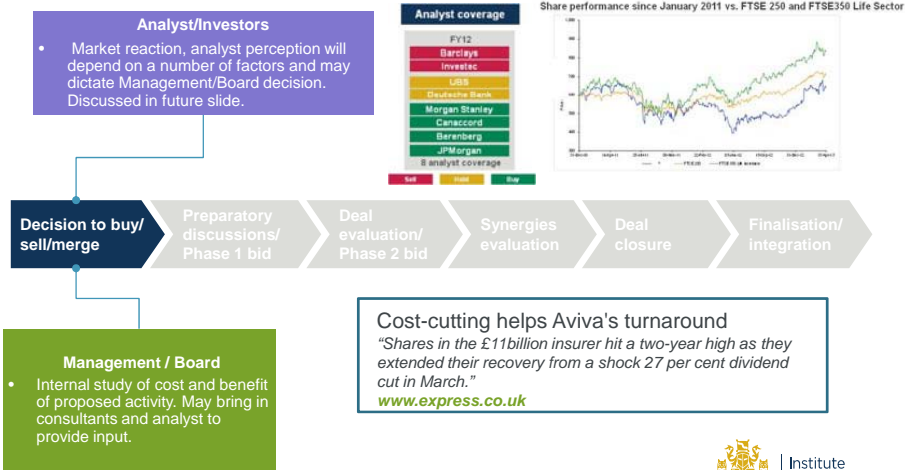
## Phases – Overview

- We have simplified the deal / transaction timeline into six separate distinct phases for simplification, as set out below:

Decision to buy/sell/merge	Preparatory discussions/Phase 1 bid	Deal evaluation/Phase 2 bid	Synergies evaluation	Deal closure	Finalisation/Integration
<b>Activities</b> <ul style="list-style-type: none"> <li>Initial decision by Insurer/Private Equity to buy, sell merge or list (IPO)</li> </ul>	<b>Activities</b> <ul style="list-style-type: none"> <li>Initial discussion</li> <li>Initial stage to shortlist potential buyers (prior to sharing proprietary information)</li> </ul>	<b>Activities</b> <ul style="list-style-type: none"> <li>Due diligence process</li> <li>Further investigation/negotiation</li> </ul>	<b>Activities</b> <ul style="list-style-type: none"> <li>Study of possible synergies</li> <li>Merger/Acquisition impact analysis</li> </ul>	<b>Activities</b> <ul style="list-style-type: none"> <li>Acquire regulatory approval</li> <li>Payment</li> <li>Agreement of T&amp;Cs</li> </ul>	<b>Activities</b> <ul style="list-style-type: none"> <li>Integration process</li> <li>Realisation of synergies</li> </ul>
<b>Outcome</b> <ul style="list-style-type: none"> <li>Decision made</li> <li>Public announcement of intent (IPO)</li> <li>Contact of potential buyers/sellers/partners</li> </ul>	<b>Outcome</b> <ul style="list-style-type: none"> <li>Demonstration of intent/interest</li> <li>Initial non-binding offer</li> </ul>	<b>Outcome</b> <ul style="list-style-type: none"> <li>Final bid/binding offer</li> </ul>	<b>Outcome</b> <ul style="list-style-type: none"> <li>Report of potential synergies including estimated value</li> </ul>	<b>Outcome</b> <ul style="list-style-type: none"> <li>Finalise M&amp;A</li> <li>Public announcement</li> </ul>	<b>Outcome</b> <ul style="list-style-type: none"> <li>New efficient entity</li> </ul>



## Phases – Decision

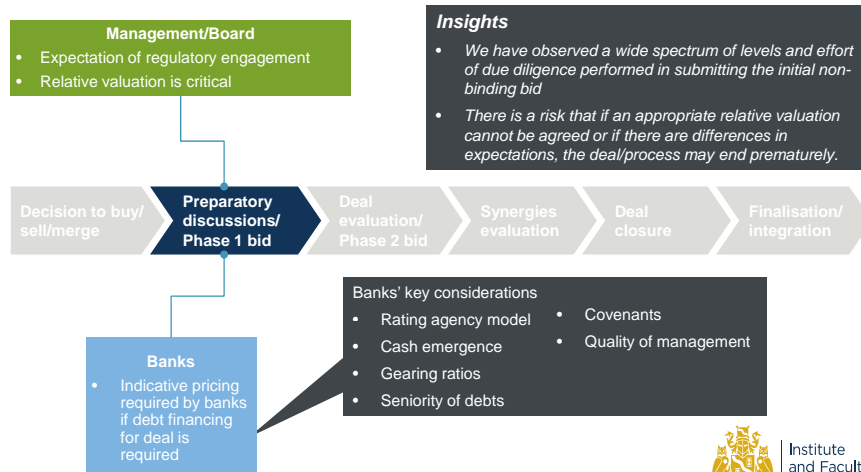


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## Phases – Preparatory discussion / Phase 1 bid

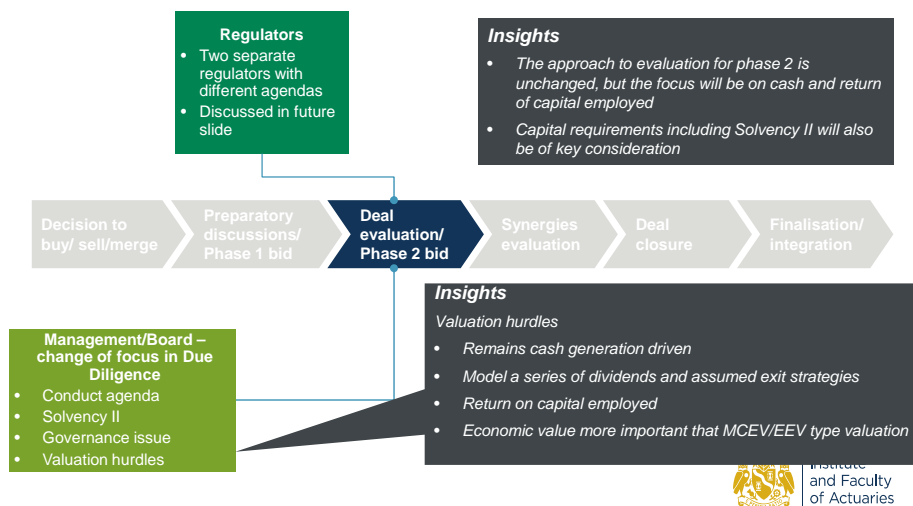


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## Phases – Phase 2 bid



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## Regulators – PRA/FCA

The split of the FSA into the PRA and the FCA has created two organisations with different objectives when assessing M&A activity

### PRA

- Change in control opportunity to impose additional buffers.
- Solvency II – preparedness/integration/approaches
- Group capital adequacy/Capital requirements post merger (Solvency Risk)
- Level of supervision
- Use of own advisors

### FCA

- Governance of organisation
- Outsourcing arrangement
- Market competition
- Fair treatment of policyholders (especially With Profits policyholder)
- Different views on ICA and limited discussion.
- Conduct issues

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## Solvency II

Solvency II is back on the agenda

- All deals must provide forecasted Solvency II figures – to consider impact of M&A under Solvency II framework.
- Not just the figures
  - How to integrate IMAP
  - ORSA processes
  - Disclosure
  - Governance
  - Data systems
  - Legal structure

### Insights

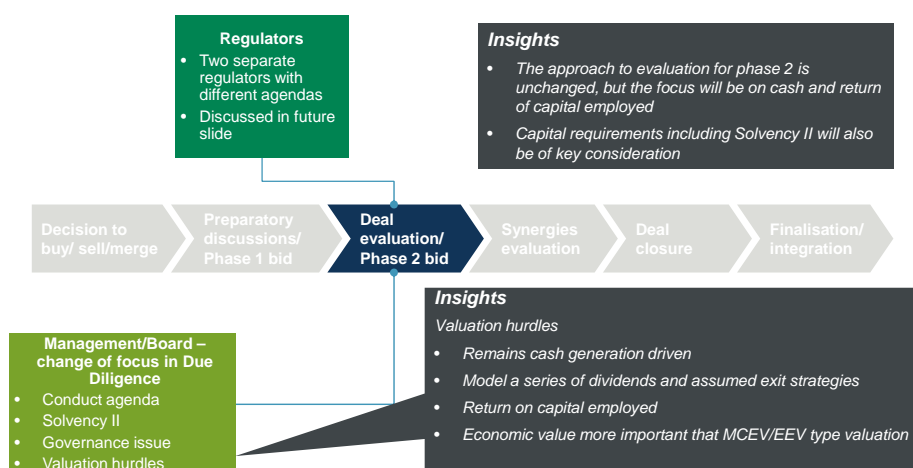
*We are however still seeing some uncertainties in the final form of Solvency II and a reluctance to allow potential impacts to derail potential deals*



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## Phases – Phase 2 evaluation and bid

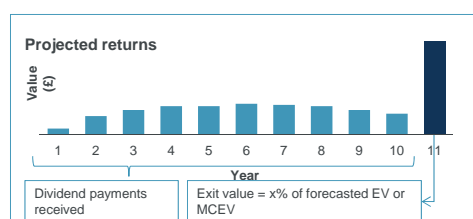


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## Valuation methods

- EV (MCEV or EEV) is a start point
- **The appropriate is the EV valuation method is less relevant to a mature market, where focus is on cash generation and economic value** with focus on the size and timing of the cash emergence.
- There have been a number of papers written on reconciling EV to Market Cap in the past <sup>1,2,3</sup>.
- NBV remains a key measure in high growth emerging market areas.

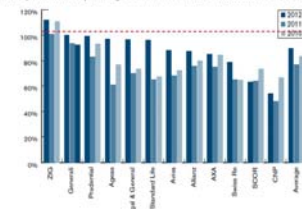


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1. [http://www.towersperrin.com/rfs/2001-3\\_New%20Improved%20EV%20for%20MCEV%20thought%20leadership.pdf](http://www.towersperrin.com/rfs/2001-3_New%20Improved%20EV%20for%20MCEV%20thought%20leadership.pdf)
2. <http://www.towersperrin.com/tp/getwebcachedoc?webc=TILL/USA/2001/200103/2002041913.pdf>
3. [https://www.towersperrin.com/tillinghast/publications/presentations/Market\\_Consistent\\_Valuations/MCV\\_IAAust.pdf](https://www.towersperrin.com/tillinghast/publications/presentations/Market_Consistent_Valuations/MCV_IAAust.pdf)

### EV - comparison

Market capitalisation as a percentage of embedded value as at 31 December 2010, 2011 and 2012



Source: Morningstar, 2012 Embedded Value Reports Generating Value

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## Phases – Synergies/Integration

Capital synergies can be used to release cash or to reduce strain of funding in a deal. We will provide an example of how capital synergy could be achieved



Capital synergy	Acquirer		Target		Combined co. - less assumed purchase price of £210m	
	Pillar 1	Pillar 2	Pillar 1	Pillar 2	Pillar 1	Pillar 2
Cap Rescrs.	1,000	1300	200	300	990	1,390
Cap Rescrs. Req.	400	700	60	100	460	720
Cap Mgmt Pol.	200	245	30	35	230	252
Excs. CR over CMP	400	355	110	165	300	418
Excs. P2 headroom ovr P1		-45		55		118

Assume 10% additional diversification benefit

Combined entity is P1 constrained meaning that the excess headroom of P2 over P1 can be used to reduce the strain of funding the deal.

The net capital outlay reduced by 47.

Implies target has £200m net assets and £100m VIF. Assume purchase price is 70% of EV = £210m

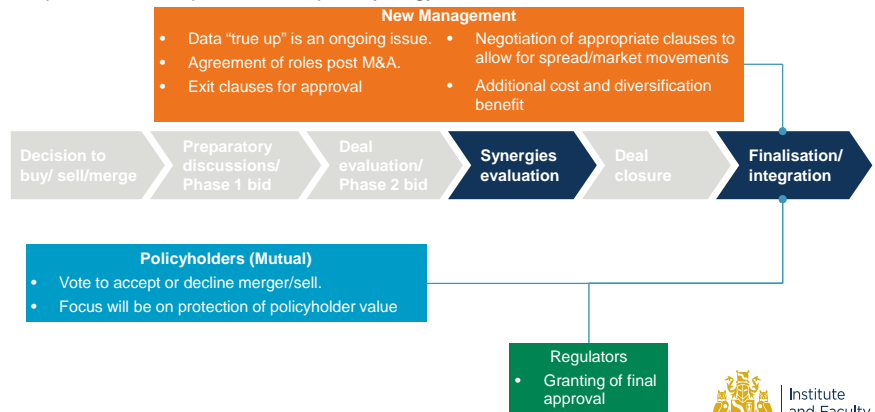
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## Phases – Synergies/Integration

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## Summary

- While we have seen an increase in activity M&A space in the recent years. We expect this to continue.
- Review of cash generation remains the key focus
- Broader focus of due diligence (not just EV). Considerations around governance, conduct and integrations issues are becoming more central to the due diligence process.
- Solvency II is now becoming clearer (hopefully), we expect with the details of Solvency II becoming more "set in stone"

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# Questions

# Comments

Expressions of individual views by members of the Institute and Faculty of Actuaries and its staff are encouraged.

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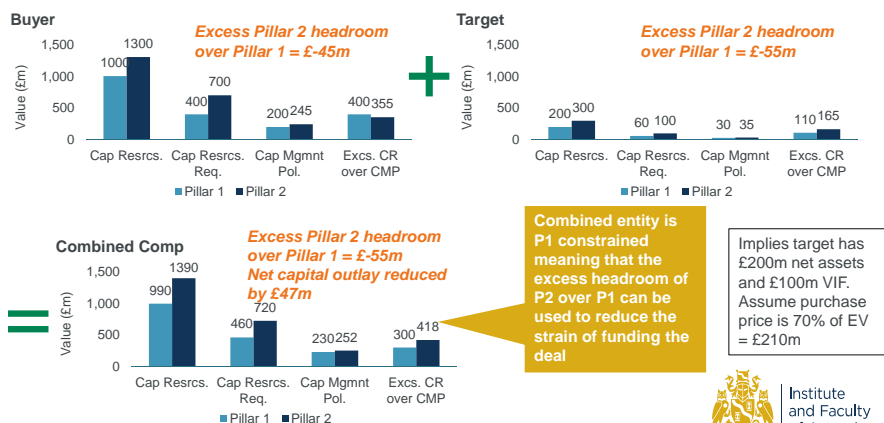


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## Synergies: Capital

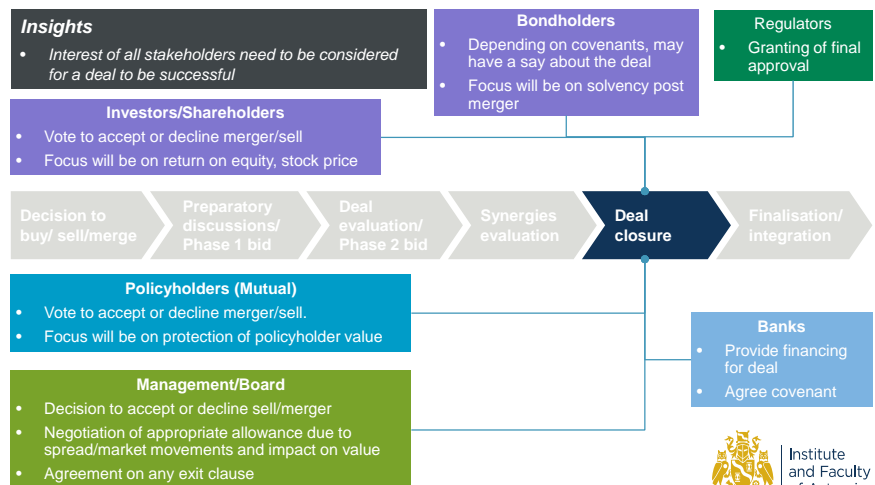
Capital synergies can be used to release cash or to reduce strain of funding in a deal. We will provide an example of how capital synergy could be achieved.



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## Phases – Deal closure



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