M&A Interactive

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INDIAN INVESTMENTS IN EUROPE

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A supportive environment, domestically and overseas, is imperative for M&As

Although uncertainty on account of geopolitical issues around the world continues and despite slow progress on Brexit, the positive election results in the Netherlands, France and now Germany have kept European deal activity buoyant. This was evident in the value of European mergers and acquisitions (M&As), which were up by 30.1 per cent in the first six months of 2017.

Inbound investments in Europe amounting to almost USD 211.1 billion have been announced till June, the highest year-to-date value since 2001 as per Mergermarket data. However, there was 65.7 per cent drop in the value of Chinese investments in Europe to USD 25.6 billion (59 deals), as compared to the same period last year (86 deals, USD 74.8 billion). Indian companies, on the other hand, displayed more appetite for deal making in Europe as compared to previous years.

Indian investments in Europe have been on the rise on account of many factors including liberalisation of its overseas direct investment norms from time to time. Europe no doubt offers appealing investment opportunities for Indian companies now, as many of them are available at attractive valuations.

Besides liberalisation in overseas investment norms, a strong growth rate in the domestic market has led to Indian companies actively scouting for overseas expansion. Restrictions on overseas investments imposed in 2013 were subsequently rolled back and limits were increased in 2014. Share swap was also allowed without any regulatory approval a couple of years ago. Further as recently as this April, the RBI also allowed Indian companies to merge with foreign firms subject to its approval and other requirements.

But the question is whether Europe is ready to receive greater investments from India?

In principle Indian companies mostly being family owned businesses may be a natural fit for their European counterparts given shared democratic values, commonality of philosophy and the complementary nature of offerings. However, the European M&A landscape throws many challenges for Indian firms. A few are as follows:

- New investment barrier introduced at the EU level: In July Germany introduced investment review norms on the lines of review by the Committee of Foreign Investment in the US. This would involve case-by-case threat assessment of investments in "critical infrastructure" made by non-EU/non-European Free Trade Association companies. Other nations such as Italy, France and the UK are likely to introduce similar processes that may extend to review of transaction involving key technologies. Many transactions may become subject to investment review at the EU level which may create obstacles to deal closing and enhance uncertainty.
- Non-existence of EU trade treaty and heterogeneous market: After the US, some jurisdictions such as the UK, Germany, France and Italy have been the top overseas direct investment destinations for Indian companies. EU's single market offers a large opportunity to Indian businesses to increase their global market share. However, non-existence of trade agreement with EU poses a major challenge for Indian firms in expanding outreach. Further, although India is as diverse as many countries in Europe, difference on account of local employment and tax laws, market, culture and language poses major entry barriers.
- Acquisition financing: Although credit is cheaper in Europe compared to India and distressed assets may be available at low valuation, financing an acquisition via a European bank remains a challenge. Overcoming it entails complex debt structures. In countries such as Italy, Spain and Portugal which are still recovering from the Eurozone crisis, it further gets difficult for Indian firms to obtain finance for acquisition or new projects. Further, small and medium companies in their initial overseas endeavour find it difficult to prove creditworthiness, which automatically increases the cost of credit.
- Good, bad and ugly experience: Many European firms have been involved in inbound and outbound ventures with Indian companies. Indian companies are preferred by many European firms struggling with succession planning. While some major firms have gained the requisite knowledge to deal with complex issues, many midsize European companies have had varied levels of experience. So, European companies remain cautious while choosing India acquirers/partners.
- Lack of information networks: In the absence of established information network for screening of M&A opportunities, Indian firms are placed in a disadvantageous position. To complicate further, Indian regulatory restriction and challenge on acquisition financing increases the lead period on a deal. As a result, the parties in the deal are sometime seen hesitant in involving an Indian bidder only due to the longer time period involved.

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From Europe's perspective, some of the solutions to the above challenges may require structural and political changes. On the other hand in the longer run, cultural adaptability of Indian firms coupled with rich intellectual capital will provide a competitive advantage to Indian buyers and European sellers. Consequently, a supportive and conducive environment both domestically and overseas is imperative for successful Indo-European M&As.

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