



KPMG's publication

The M&A Landscape in Romania



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Foreword

Last year was one of the most important years for the Romanian Mergers & Acquisitions (M&A) market as investor confidence continued to build up.

Stakeholders expect a further increase in M&A activity in 2020, supported by Romania's economic growth trend and favorable geopolitical position in the region.



Ramona Jurubiță

Country Managing Partner



Bodgan Văduva

Partner, Head of Deal Advisory

Romania has become a significant investment destination, over the last 15 years, for both strategic and financial investors.

Buyers find M&As to be a useful strategy to seize the moment in a rapidly growing environment, while sellers try to realize the value that has been built up in local companies.

We expect to see another busy year as positive sentiment is fostered by sustainable economic growth and increased attractiveness of Romanian targets, which are strengthening their market position and are opening new development opportunities through regional expansion.

Furthermore, Romanian entrepreneurs, in their quest for growth, continue

to be faced with a buy versus build strategy and have begun to consider M&As as an integral part of their strategy.

In the context of a booming global M&A market, our survey found a strong sense of optimism at the national level, with 67% of respondents expecting high levels of M&A activity in Romania to continue over the coming months.

Sectors such as technology, healthcare and energy are expected to be particularly attractive.

The study shows that buyers are worried about substantial differences in price expectations and global macroeconomic uncertainties. Also, at the same time, investors consider



that target readiness has a material impact on deal making.

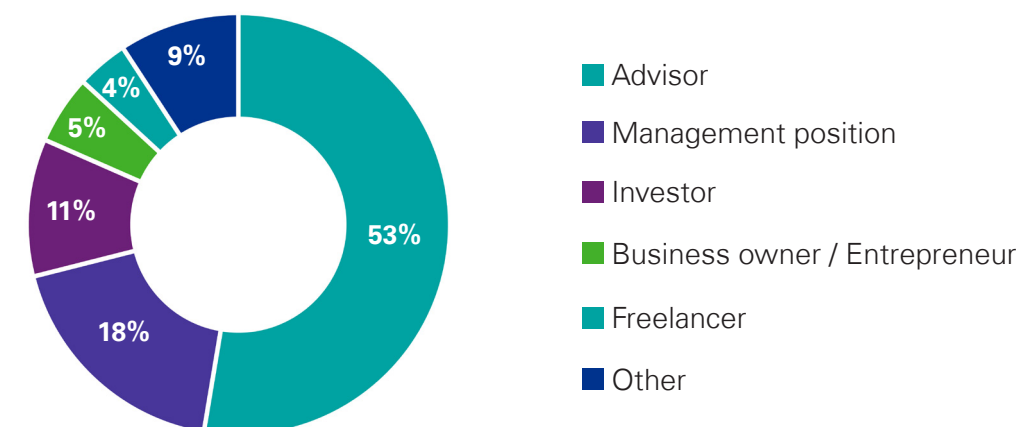
Our survey aims to provide thoughtful and valuable insights into market attitudes and expectations for the months ahead, to help our clients anticipate and make the most of future M&A opportunities.

KPMG is the leading local M&A advisor in Romania, advising corporates, financial investors and business owners.

To gain further insights into appetite for M&As and trends, we surveyed relevant stakeholders for this inaugural 2020 edition of our publication *The M&A Landscape in Romania*.

Relevant professional position

More than 64% of respondents are investors, financial and legal advisors, all of them professionals closely connected with the M&A market. Other respondents' opinions add significant value as they bring a hands-on perspective from a managerial point of view.



Findings



Optimistic prospects for M&A activity

67% of respondents expect M&A activity on the Romanian market to increase in the coming months, while only 5% expect it to decrease.



Favorable market conditions

Consolidation aims and sustainable economic growth are the main drivers of local M&A activity, while buyers are backed by solid financing options.



Growth is top of the agenda

Acquiring market share is by far the main trigger for acquisitions.



Technology in the spotlight

Technology will be the most attractive sector for M&A deals, followed by healthcare and energy & infrastructure.



Businesses should be prepared for sale

Quality of underlying earnings and assets and achievable business plan assumptions are the main area of focus for buyers, followed by a healthy tax and legal status.



Post-deal integration is crucial for a successful acquisition

Overcoming cultural differences, operational integration and replacing the previous owner in management are the most common setbacks in realizing the envisaged value creation.



Challenges remain

Substantial differences in price expectations between sellers and buyers and macroeconomic uncertainty could inhibit the deal flow.





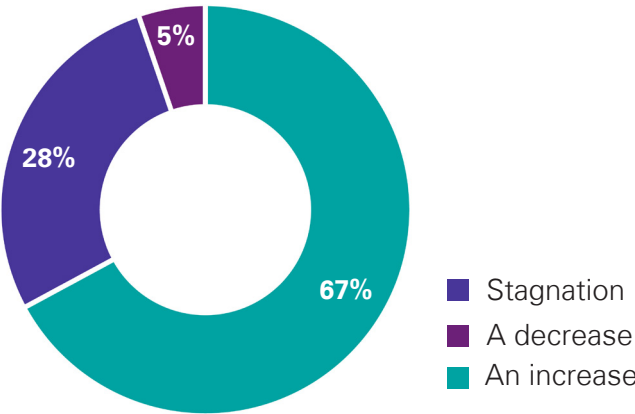
Strong confidence in M&A activity



The survey highlights a favorable scenario for this year; the market is driven by a large number of transactions currently in progress and increased appetite for M&As.

Bogdan Văduva
Partner, Head of Deal Advisory

What trend in M&A activity do you expect to see in Romania in the next 12 months?



The M&A market in Romania has seen a remarkable growth trend since 2016, which is expected to continue over the following 12 months.

Romania is an attractive market for both strategic and financial investors due to its favorable position in the CEE region (it is the 2nd biggest country in terms of population and had the fastest growing economy since 2016), low tax levels, competitive

wages and significant opportunities for market consolidation across dynamic industries.

Foreign companies turn to Romania seeking space to expand, based on sustainable economic growth and a highly qualified workforce, while Romanian entrepreneurs are starting to consider M&As as a means to catalyze expansion.

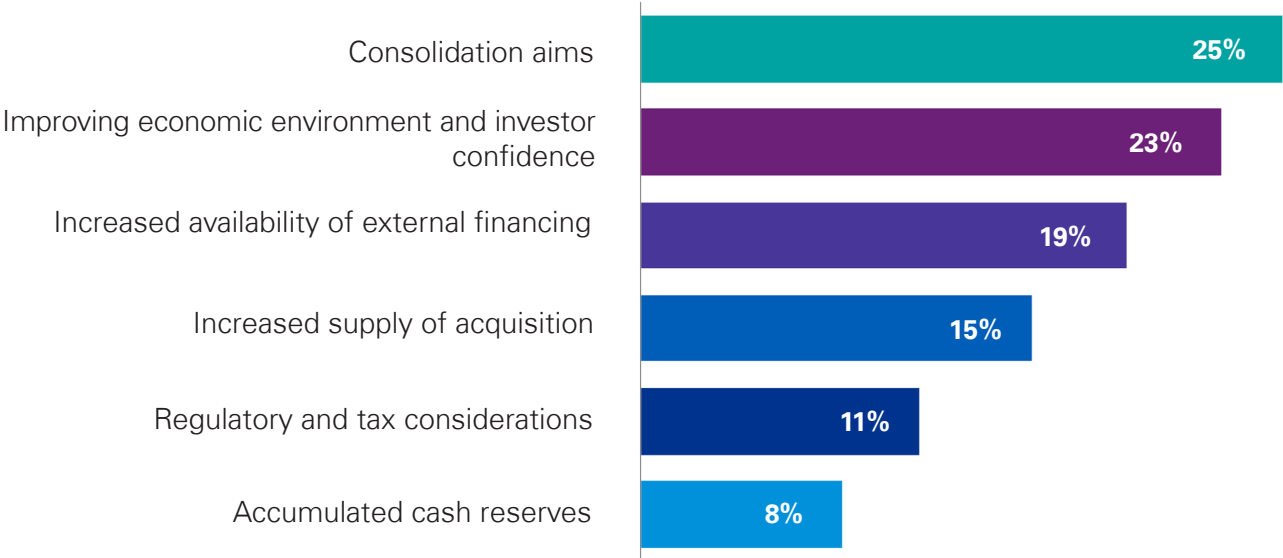
Sustainable M&A market drivers



It is probably the most favorable period to capitalize on an emerging market, due to the existence of market consolidation potential and stable economic environment

George Dumitraşcu
Director, Deal Advisory

In your opinion, what will be the main drivers of deal activity on the Romanian market in the next 12 months?



In Romania there are many fragmented sectors, offering favorable conditions for consolidation, allowing investors to capitalize on efficiencies of scale, cost reduction and profit optimization opportunities.

The process is expected to be driven by both synergetic strategic investors, looking to improve their competitive position and private equity funds, which are building local and regional champions through buy and build strategies.

Economic environment and investor confidence complement the consolidation aims. Romanian GDP is expected to increase at an average rate of 3.1% in 2020 through 2024, almost 1 p.p. higher than the CEE average and 1.5 p.p. higher than the EU average, making Romania an attractive market for foreign and local investors.

The low interest rates environment in Romania and Europe overall, coupled with the availability of alternative financing (i.e. mezzanine and private debt), is also contributing to the creation of deal opportunities.

Growth through acquisitions is top of the agenda in board rooms

Diversified and sustainable M&A growth is expected to be a key strategic direction over the next 12 months, in addition to sole reliance on steady organic growth.

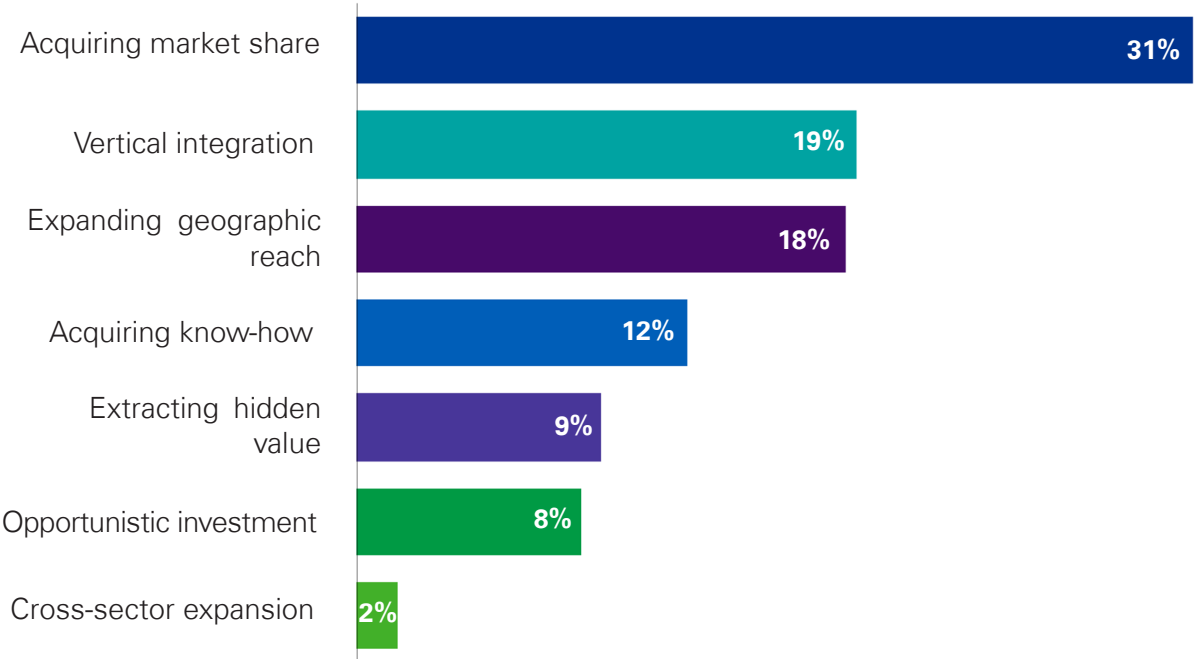
Instead of waiting for the commercial strategy to pay off, companies can rapidly accumulate market share through M&As. This way they can gain scale, benefit from different DNAs and become better equipped to face competition.

Buyers are motivated by both horizontal integration, to strengthen their competitive position and extract synergies, and vertical integration, to improve

processes and systems, as well as increase financial and operational efficiencies.

Romania is starting to be perceived as a platform for regional expansion, given its relevant geopolitical position, stable political environment, macroeconomic stability and access to a wide spectrum of neighboring markets.

What do you expect to be the most important strategic objective for acquisitions in the next 12 months?



Focus on deal drivers

People focus mainly on the price, but the price is only part of the equation.

Identifying the right target is the first step in the M&A process for prospective buyers.

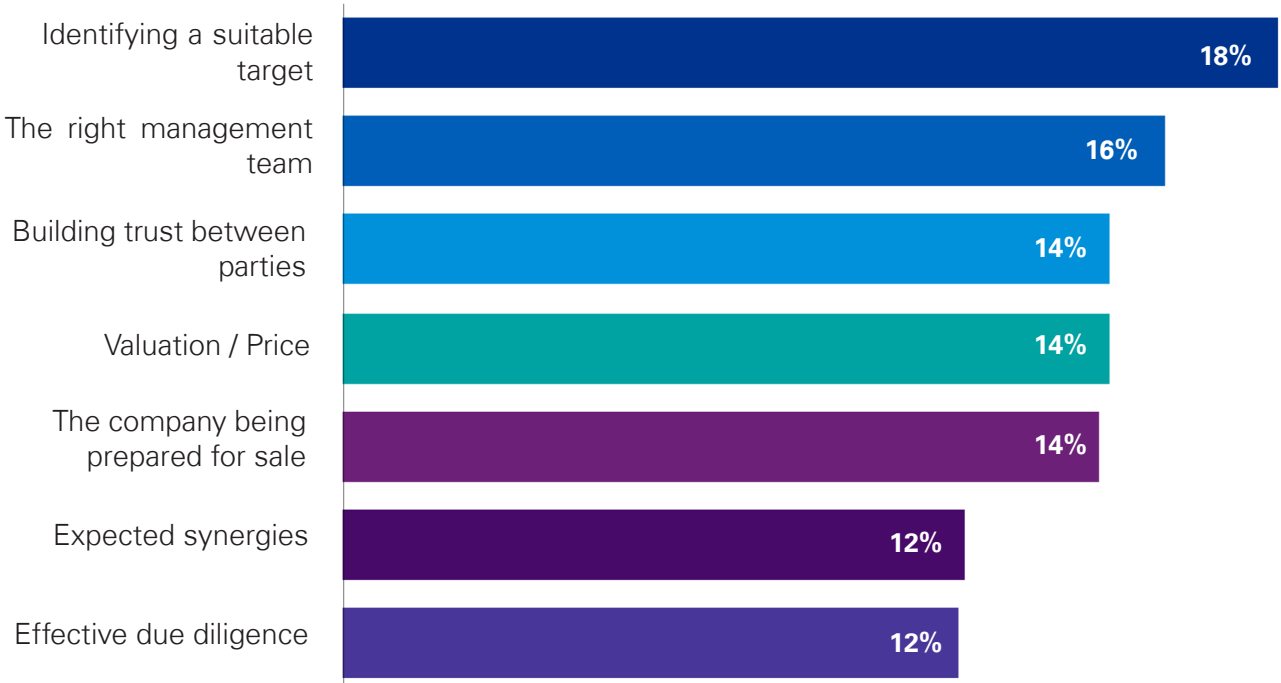
The strategic fit, focused on qualitative aspects such as product & client portfolio, earnings profile, market share and distribution channels, dictates the buyer's level of interest and creates the premises for constructive negotiations.

Having the right management team in place is of paramount importance to close a deal as buyers rely on them to implement the equity growth story.

Building trust is a necessity when conducting acquisitions in Romania. Local entrepreneurs tend to be more open with investors who validate and bring continuity to their vision. Potential buyers need to feel comfortable that the quality of the investment will be preserved and even enhanced.

Preparing the business for sale in key areas such as commercial, corporate governance, tax, financial reporting, legal, human resources, IT or business processes is instrumental in maximizing the deal package and, ultimately, pricing.

In your opinion, how important are the following factors for a successful deal?



Balanced expectations across key sectors

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The technology sector has expanded and attracted significant investors during the past decade and is expected to maintain this upward trend in the future.

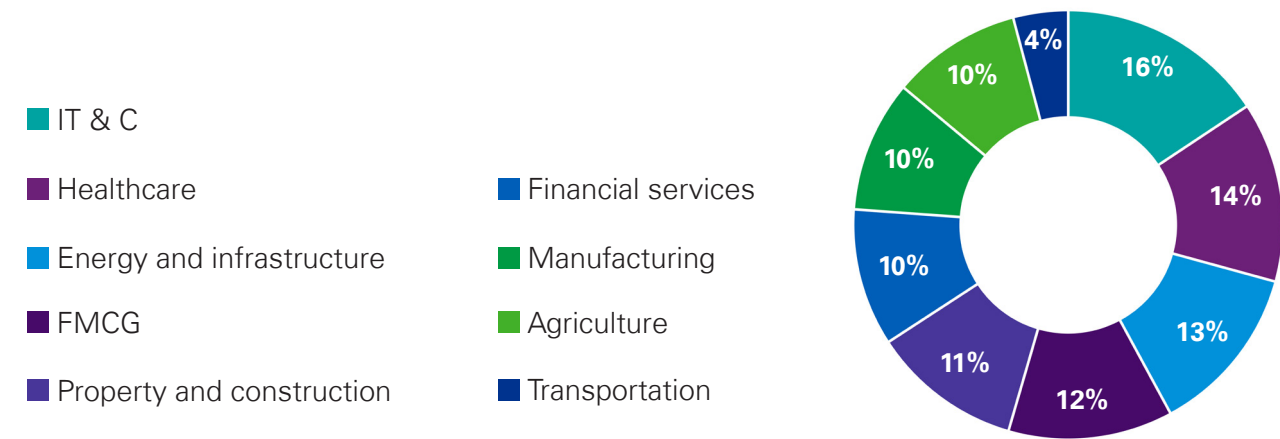
Richard Perrin
Partner, Head of Advisory

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International strategic investors in the energy sector are currently re-evaluating their presence in Romania, providing opportunities for large deals to be concluded in this sector.

Ovidiu Popescu
Director, Advisory

What sectors do you expect to be the most active in the next 12 years?



The survey shows that a large number of industries in Romania are attractive and are likely to see M&A activity in 2020.

Romania represents one of the most attractive markets in Europe for technology investments, owing to its wide pool of software service providers and the constantly increasing number of certified IT specialists.

The healthcare sector is still undergoing consolidation. The major private healthcare operators have successfully closed structural

gaps of the public sector and, therefore, have quickly developed both organically and through the completion of around 60 acquisitions.

Several energy companies are contemplating an exit and Romania is now on the radar of large infrastructure funds.

FMCG, fueled by significant increases in disposable income, is seeing continuous exponential development across the value chain.





Focus on CEE

For Romanian companies, foreign expansion, especially within CEE, represents a significant development opportunity.

The CEE region is considered one of the most attractive developing regions in terms of investment potential.

Romanian companies are starting to see it as a homogeneous space and are looking to overcome certain language and cultural barriers in order to maximize expansion potential.

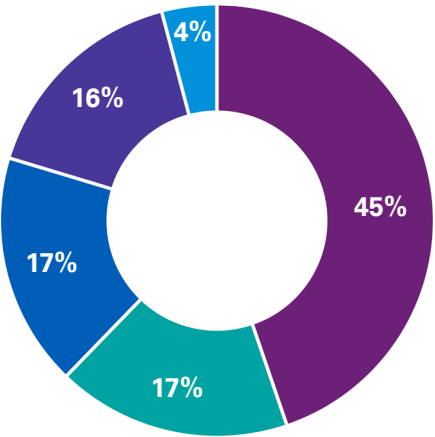
One scenario could be initiated by private equity funds deploying buy-and-build strategies across

CEE with the aim of consolidating regional market leaders, to be sold on to strategic investors as truly meaningful players in their industries.

However, there are still Romanian companies currently enjoying the consolidation opportunities on the local market, with expansion to other proximity markets being a secondary priority. Nevertheless, we expect this to change in the long run.

In which geographical areas do you expect that Romanian companies will look to expand their operations in the next 12 months?

- Central and Eastern Europe
- Republic of Moldova
- Western Europe
- No geographical expansion expected
- Other areas



Investor profiles

Strong interest is observed from both private equity funds and strategic players.

In the context of increased presence of private equity funds on the local market, our survey found that their confidence is expected to remain linear, translating into new acquisitions in 2020. We expect to see increased private equity activity in consumer driven markets.

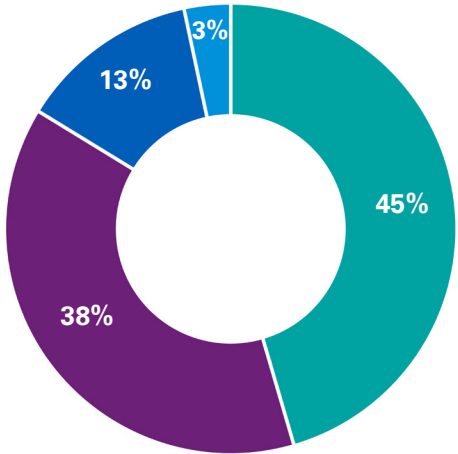
At the same time, the market is allowing funds to successfully exit investments which have reached the maturity stage at some of the highest industry multiples recorded during recent years.

International companies, either by entering or increasing market share, are expected to produce roughly as many deals as financial investors, in the same time frame. This is largely due to the Romanian market's attractiveness, the accessibility of both cash reserves and low interest debt, and due to the possibility of enhancing their existing value chain and acquiring market share.

Developed Romanian companies are likely to increase their M&A appetite in order to remain relevant in a changing environment.

In your opinion, how likely are the following actors to complete acquisitions in Romania in the next 12 months?

- Private equity funds
- International companies present on the Romanian market
- International companies not present on the Romanian market
- Romanian companies





The implications of Due Diligence

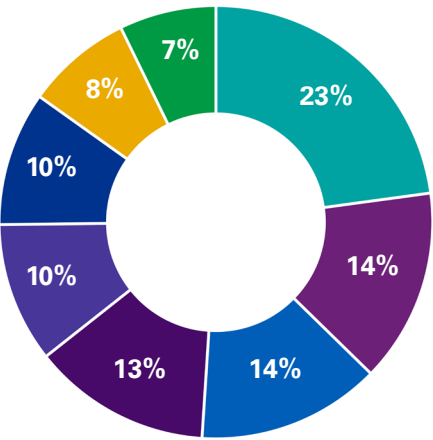


In recent years, the relevance of the due diligence process has increased, driven by the higher complexity of transactions and the expectations of our clients. Our support goes beyond the due diligence report. We work together with our client to define the price mechanism, and we prepare and verify the completion accounts.

Mihai Zoescu
Director, Transaction Services

In your opinion, how important are the following Due Diligence areas in completing a successful transaction?

- Quality of underlying earnings (EBIT/ EBITDA) and operating cash flow
- Assessment of assumptions behind the target's predictions (business plan)
- Quality of assets
- Tax and legal considerations
- Net debt
- Cost synergies
- Quality of reporting (RAS, IFRS, management accounts)
- Underlying working capital



Tax and legal considerations during the transaction process and thus also during due diligence help the buyer to protect the agreed transaction value.

René Schöb
Partner, Head of Tax & Legal



Due Diligence is a key step in the M&A process, defining transaction terms and highlighting any areas of concern to be addressed in the transaction documents.

As transaction values are usually linked either to the company's EBITDA and present or future cash flows, such indicators are usually under heavy scrutiny during Due Diligence:

- Earnings, net debt and net working capital need to be adjusted to reflect the normal course of business as the way they are defined can have a significant impact on the transaction value;
- The business plan should depict realistic expectations of the management in normal market circumstances and should be consistent with historical performance;

- Buyers expect businesses to be fully capitalized, thus replacement and growth capital expenditures should meet the company's needs to maintain a healthy asset base.

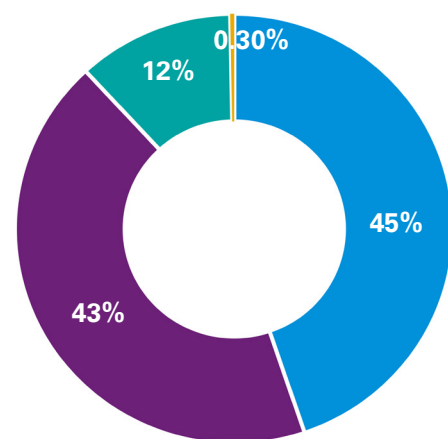
Tax and legal considerations are also important for a successful transaction. Today, tax transparency is a must and has to be managed proactively. Tax risks resulting from transactions and detected during the due diligence phase have to be addressed and provided for at the earliest possible opportunity. Furthermore, legal considerations define the boundaries of the deal and protect the buyer's investment and thus the agreed transaction value.

No preferred exit strategies

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Ultimately, when a business owner decides to sell, whether or not the buyer is a strategic player or a private equity house becomes something of a secondary concern.

Laura Toncescu
Partner KPMG
Head of KPMG Legal



How likely do you think the following will be the preferred exit strategy for Romanian business owners in the next 12 months?

- Exit to a strategic buyer
- Exit to a financial buyer (private equity funds)
- Initial public offering
- Management buy-out

No preference between financial and strategic buyers has been signaled.

In the end, the most important aspect of completing a successful exit, regardless of the buyer's profile, is obtaining a maximized deal package, considering value in connection with the terms of a transaction.

Sellers need to align their personal agenda with that of the potential buyers and consider multiple deal aspects such as full vs. partial exit, transition periods, earn-out schemes, deferred payments,

escrow accounts, and any other factors which may alter post transaction value.

Most respondents did not consider an IPO on the local stock exchange to be a likely successful exit strategy. This is due to the high level of complexity to complete a full exit through subsequent public offerings, after a successful IPO. Most transactions in Romania represent the sale of 100% of company shares, while Stock Exchange listings are usually minority stake sales or capital increases.

Post Merger Integration

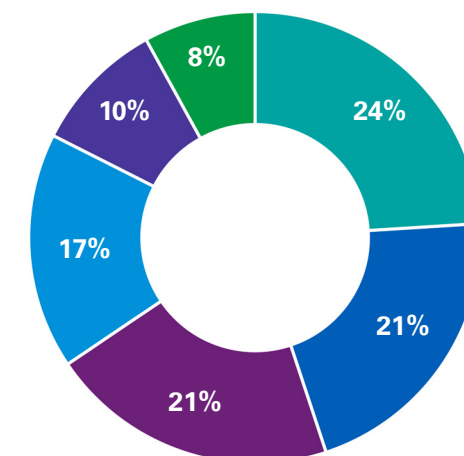
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The best approach to conduct the M&A process is with post-merger integration in mind.

George Dumitrașcu
Director, Deal Advisory

In your opinion, how challenging are the following areas when integrating an acquired company?

- Overcoming cultural differences/ HR issues ■
- Operational / Supply chain integration ■
- Involvement of the previous owner in management due to dependency issues ■
- Merging IT systems ■
- Tax optimization ■
- Accounting and finance transformation ■



Post-merger integration is a significant corporate issue, with comparable success and failure rates. Within this context, failure does not mean a successful business becoming an unprofitable one, but rather a failure to meet the expectations of the synergies identified in the M&A process.

Buyers should focus on identifying, prioritizing and monitoring the main value drivers in order to create the envisaged value.

The Romanian market has seen its fair share of integration difficulties.

Cultural issues are often quoted as being the root of the problem, together with significant failures in achieving complete operational integration.

However, the survey suggests that when the initial owner stays on with the company following the sale and is involved during the transition period, post-deal integration is a smoother process.

Mitigating potential deal breakers

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During M&A negotiations, the first deal breaker that needs to be managed is any difference in price expectations.

Cosmin Comsa
Manager, Deal Advisory

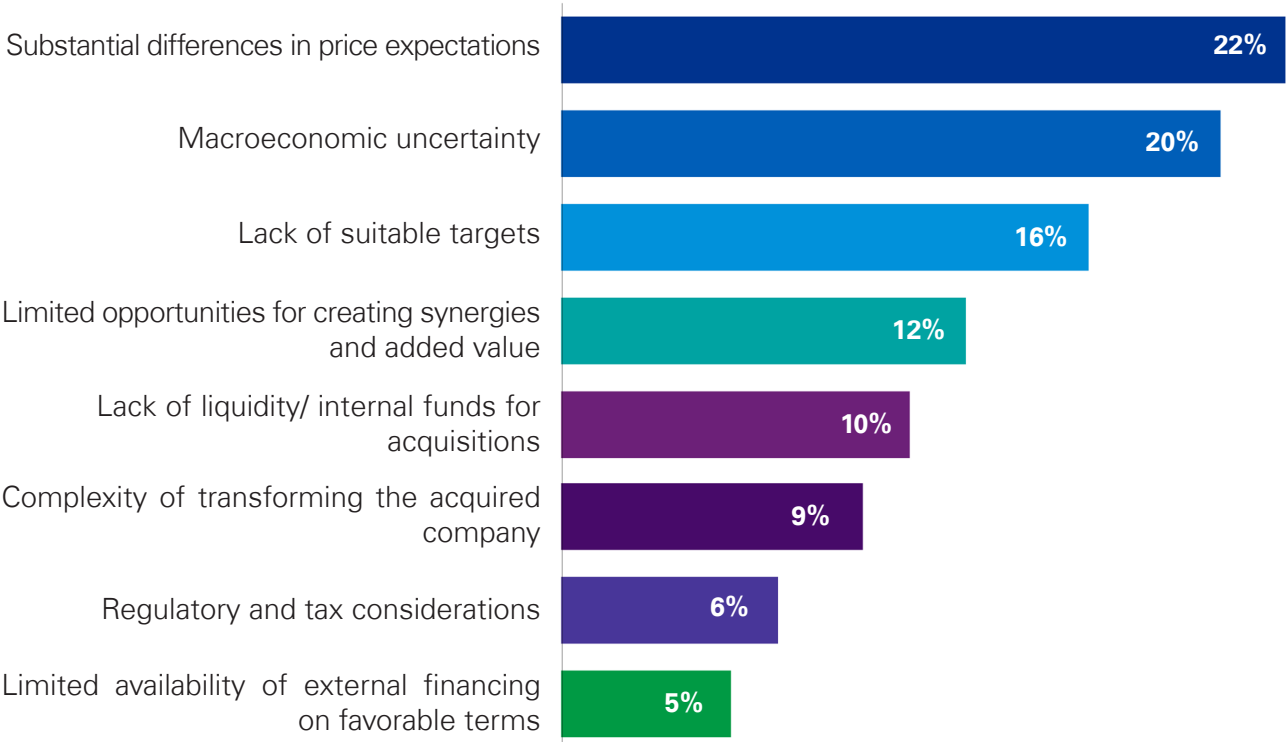
Price differences are perceived as the main inhibitor of deal-flow in Romania in 2020. In order to bridge this gap more easily, we recommend a holistic view of the offers from both the buyer's and the seller's perspectives. Pricing should be considered in conjunction with other terms and conditions of the offer.

Macroeconomic uncertainties, which vary across geographies, can also trigger substantial differences

in adjusted valuation multiples across the same industry, distorting price expectations from both sellers' and buyers' perspectives.

As Romania is a developing market, the availability of sizeable targets has been limited so far. This is changing, as companies are scaling up their operations, consolidating market share and adopting a more corporate approach.

How important do you consider the following factors could be in inhibiting deal activity in the next 12 months?



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