

M&A Market: Prospects for Ukraine Against the Background of World Records

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Currently, the global investment markets are on the rise, financial and strategic investors are in active search for investment objects. According to the 13th Global Capital Confidence Barometer (CCB) prepared by EY, 59% of global companies plan to be actively involved with acquisitions in the next year. This is the highest figure for the entire six-year period of the survey preparation.



In 2015, global M&A market reached USD 4.28 trillion breaking the record of 2007 by 16.6% (according to Mergermarket data). The amount of transactions exceeded the previous year by almost 30%. The largest share of the market by value of transactions accounted for the energy sector and mining industry (almost 15%).

Two of the six largest M&A transactions in history were announced in 2015. These are the acquisition of Allergan by the biopharmaceutical corporation Pfizer (the third largest deal in the history worth of USD 183.7 billion) and the acquisition by Belgian Anheuser Busch Inbev's of its rival SABMiller (the fifth largest, USD 107 billion).

Due to unstable geopolitical situation Ukraine, unfortunately, made a minor contribution to the overall standings of 2015. According to EY estimates, the amount of public mergers and acquisitions in Ukraine in the past year was approximately USD 0.6-0.7 billion, while the pre-crisis level was USD 3-3.3 billion. However, our country has a high

potential and still is of interest for both local and foreign strategic and financial investors with high risk tolerance.

Among the most attractive areas, traditionally, is the agricultural sector because of the export potential, relatively inexpensive and fertile land and cheap labor. The market consolidation trends go on. Specifically, both crop farming and livestock production (especially pigs) are attractive. Thus, the EY Corporate Finance and M&A Group experts successfully closed the sale of assets of a company specializing in breeding of commercial pig stock in the central region of Ukraine. The deal was signed in July 2014, the buyer was a foreign investor, a large European agricultural company.

Also, in December 2015, EY completed the deal on sale of the crop agricultural farm with the land bank of 6,200 hectares and 45,000 tons of storage in Poltava region to the local strategic investor. Rather than the average USD 300-400 per hectare, the company's value upon the result of the transaction amounted to USD 10.5 million.

Over the past two years, more than 60 banks were withdrawn from the Ukrainian market. This has provided a significant amount of bad assets in the financial sector for sale. The increased activity was observed in the Ukrainian insurance segment; in early 2015, EY assisted in closing two deals. We provided advisory services on sale of business to mid-size foreign insurance companies, not life sector (players from the top-20 and top-40 in terms of gross premiums). It is worthy of note that the buyers were large international financial companies, which considered as strategically correct the entrance to the market of Central and Eastern Europe as early as 2015.

These examples are the best proof of the fact that foreign investors are interested in Ukrainian companies, and with proper preparation and organization of the sales process it is possible not only to find an investor, but also to get quite adequate valuation of an asset.

IT-sector in Ukraine is one of the most interesting and sought-after for foreign investors because of the business model flexibility: the availability of the customer base abroad, foreign currency proceeds and qualified personnel. Back in December 2013, Europe Virgin Fund (EVF), a private equity fund, has acquired a controlling stake in Portmone, #1 Ukrainian operator of online payments (EY team attracted the financing). Last year, George Soros Fund, a global investor, took an interest in the Ukrainian IT companies. The acquisition of share in one of the largest Ukrainian IT-companies by the investor of such level is a positive signal not only for the industry but for the investment attractiveness of the country as a whole. As at the beginning of 2016, EY in Ukraine has a portfolio of projects in the IT and e-commerce sector at the various stages of negotiations with interested potential investors.

WHAT ATTRACTS FOREIGN AND LOCAL INVESTORS TO INVEST IN THE UKRAINIAN BUSINESS TODAY?

1. Cheap and skilled workforce
Every year about 300 of higher education providers graduate more than 640,000 professionals, including 130,000 engineers. At the same time, the cost of labor in Ukraine is extremely low. In 2015, the average salary was 5.7 times less than in Poland, 19.5 times less than in the USA and 2 times less than in China.

2. The window of opportunities – Ukraine's economy has hit the bottom

Ukraine's economy has hit the bottom of fall and the recovery of growth is expected in the future. According to Qimiao Fan, World Bank Country Director for Ukraine, Belarus and Moldova, it is expected that in 2016 Ukraine will experience the economic growth at the level of 1%. According to the Bloomberg forecast based on the survey of leading economists, this year growth is expected at 1.4%. At the same time, Arsenii Yatseniuk, the Prime Minister of Ukraine, is more optimistic: according to him, the economy of the country should grow by 2% in 2016.

Ukraine is the largest European consumer market with a population of about 43 million people (excluding the occupied territory of the Republic of Crimea and Sevastopol). This figure is more than twice higher than the number of population of Sweden, Finland and Norway combined.

3. Huge transit potential of the country is a driver of future economic growth

Four out of ten Pan-European transport corridors pass through Ukraine. Ukrainian railway network is the 14th largest in the world (more than 23,000 km), and its operator, "Ukrzaliznytsya" is in the top-10 largest railway companies in the world.

In January, a new "Silk Road" through Ukraine bypassing Russia was launched. It includes ferries through the Black and the Caspian Seas (Illichivsk - Batumi and Aliat - Aktau Port) and has the capacity to compete with the traditional overland route. The first experimental train round trip on route Ukraine - Georgia - Azerbaijan - Kazakhstan - China from Illichivsk seaport has been made. The new transport route is supported by and attracts interest in the world community, including China.

The involvement of Ukraine in this project will not only allow attracting foreign investment in our economy, but also getting access to alternative transit routes when it comes to Russia imposing the trade restrictions. The geographical factor of location of Ukraine at the intersection of transport axes North - South and East - West, as well as geographical proximity to European and Russian markets, plays an important role.

4. High public demand and external partners pressure force the Government to reform the economy

In recent times, many deregulating initiatives were implemented: in the agricultural sector dozens of permits, veterinary certificates were cancelled, the President has signed a new wording of the Law of Ukraine "On Licensing Certain Types of Economic Activities", which dramatically reduces the number of licenses in Ukraine, etc.

The police has been reformed, the state started a gradual decentralization, the public procurement system undergoes the reform (budget savings in the e-procurement system ProZorro exceeded USD 500 million), a new wave of privatization has been planned.

It should also be noted that many important positions in the governmental agencies are held by qualified people from business, many of them have Western education and international experience.

Efforts on reforming the country find support among external partners as well. Ukraine has successfully completed the restructuring of state debt and government-backed debt of USD 15 billion. In 2016, it is expected that lending of the agricultural sector by the EBRD will increase by EUR 200 million.

In addition, this year, Poland will grant Ukraine the loan of EUR 100 million, which will be used for improving the road infrastructure, arrangement of crossing points on the border of Ukraine and Poland and other projects agreed by the parties.

5. Stabilization of situation in Donbass

In the second half of 2015 - beginning of 2016, we can observe a relative stabilization of the military conflict in Donbass, which will have a positive impact on the development of the Ukrainian economy. Petro Poroshenko, the President of Ukraine, called the stabilization of the situation in the East of the country the major achievement in defense and security areas in 2015. Also, the efforts are aimed at greater involvement of the international community in resolving the conflict. Since 24 January, the UN assessment mission for stabilization of the situation in Donbass has started its work, which will include the representatives from the UN Development Program, UN Children's Fund and the UN Mine Action Service.

FORECAST FOR 2016

Technologies and varying consumer preferences influence the existing business models and dissolve boundaries of different sectors. Therefore, the search for growth opportunities increases the importance of M&A transactions to a record level. According to the 13th Global Capital Confidence Barometer (CCB) prepared by EY, 55% of companies currently have three or more transactions in the implementation process, while 48% of companies intend to make acquisitions outside their sectors.

Thus, there is every reason to believe that in 2016 Ukraine will remain on the radars of local and international strategic and financial investors. Over the last two turbulent years, the Corporate Finance and M&A Practice of EY in Ukraine completed six transactions on sale of business in Ukraine and the CIS, and in four of them the buyers were foreign investors. This indicates that the market is not closed to investors. We believe that the most activity will be observed in the agricultural sector, IT and technologies, communications. In addition, transactions in the pharmaceutical industry (both production and trade) and food production are probable.

Comparison of the average salary in Ukraine and countries of the world, 2015

