

Steady State in Scotland's Corporate Deals Market

According to one leading financial commentator, the UK economy will only begin to grow again in any meaningful way after the Queen speaks the magic words "Let the games commence" at London's Olympics stadium in July 2012.

In other words, until next summer the business community in Scotland and elsewhere is going to have to be content with a lacklustre recovery and, for some, a further extended spell of hanging-on and hoping for the best.

As far as Scotland's corporate deals market is concerned, I still hear the comment, perhaps once or twice a week, that "surely there are no deals happening." That is certainly not the case, and it has not been the case for some time. So, while there are certainly no signs of a deals boom, there has been a steady trend of deals being done, and by no means all related to distressed asset sales.

Is there a theme with which to characterise the current corporate deals marketplace? Well, this is certainly a good time to buy if you can, though this will often have to be with funding from your own resources. I have come across a number of plcs and substantial private companies buying other businesses off their own balance sheets, not by rights issues or by bank debt.

In the property sector, where the banks have more than enough difficult situations on their books and are not interested in getting involved in any more, there are opportunities for those with substantial liquid resources to profit from the banks' willingness to resolve property problems by looking to exit.

One example of this is a recent deal where around £100m of distressed property debt, backed by assets which had declined significantly in value (having a written down value of approx 30% of loan value), was sold by a bank to a well-resourced private individual for about 10% of the level of debt. Cash in for the bank, and a good deal for the buyer.

Banks are still lending, but usually to blue chip businesses and/or in the strongest sectors. There is limited funding for deals available in the SME-market where the risk profile is seen to be higher and bankers will be cautious. Of course, customers are still, themselves, cautious about borrowing and some banks feel that there has not been a great appetite from their customers.

Another reason for bankers' caution may be the big refinancing bubble which is due to hit many companies and banks' balance sheets next year, five years after things started to go seriously wrong in the UK banking sector.

The best advice to companies facing re-financing challenges must be to start negotiating now rather than waiting until a few months before the refinancing date. I have seen a few such refinancing deals being done recently, though usually on appreciably tougher terms than those which existed beforehand.

There is still competition among the banks for top-end lending opportunities and despite the unprecedented turmoil of the banking crisis, we are fortunate in a small

country like Scotland to have six or seven major banks staffed by good, experienced banking people supporting business and looking for opportunities in our market. While not everyone will get what they want at this time, hopefully this infrastructure will stand us in good stead in the future.

Some gaps in the market for SME funding should be filled by the likes of the Scottish Loan Fund, established by Scottish Investment Bank/Scottish Enterprise with a fund of over £90m pulled from public sources and certain of the banks. We are also seeing smaller deals funded by high net worth individuals and serial investors. This sort of funding is necessary to keep breathing life into the SME deals market.

When advising on deals over the last year or two, it has occurred to me on a number of occasions that, despite these market constraints, the “age and stage” element never really goes away. That is, at any one time, there are businesses which are ready to be sold or merged with another to take them on a level – or are controlled by owners who have determined that they have simply reached the stage or, of course, the age when they consider it is time to sell up and get out.

So, even in the toughest times, people will look to buy, sell and merge, and this continues to ensure that the corporate wheel keeps turning. You might have to re-assess the terms on which you are willing to deal or look at more imaginative ways of structuring a transaction but where there is a will, there is often a way.

Finally, another theme worth reflecting upon in the current corporate market is the international element. Of course, Scottish businesses being involved with international businesses is not a new phenomenon and we do continue to see Scottish assets being attractive to overseas buyers, sometimes assisted by exchange rates or an ability to borrow abroad to fund the deal.

However, I do feel that far more businesses are now thinking on an international basis earlier in their life cycle, and sometimes from the very earliest start up stages – whether that be setting up abroad, or through exporting or establishing sales networks.

There seems to be a real appreciation that foreign markets can often be readily accessed and, indeed, that many ambitious and growing businesses must now look overseas from day one. Of course, that brings a need to consider how best to structure your business to exploit those opportunities and perhaps consideration of partnering arrangements with overseas operators and in some cases acquisitions of businesses already established abroad.

So, overall in Scotland, things have improved on the deal front from the nadir of 2009 and while there is unlikely to be an M&A boom anytime soon the market's steady state will remain and deals will be done until, perhaps, we see the world's athletes take their marks in Stratford.

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