

Inside German Public Tender Offers

Drilling down on investor tender and ownership behaviour during M&A transactions



Introduction

The Strategic Governance & M&A Advisory team at IHS Markit, now part of S&P Global, has been involved in over 20 public tender offers in Germany over the past 36 months, representing approximately 70% of total transaction value during the period. Our analysis¹ focuses on some of the most critical and commonly queried themes to get a better understanding of the capital market dynamics in a public tender offer, including the overall acceptance level uptick, investor tender behaviour and timing as well as target company's share ownership developments during the offer period.

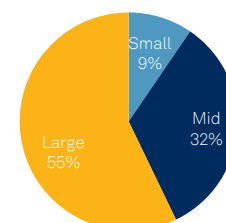
- Firstly, we explore the typical development of acceptance levels during the offer period and illustrate how acceptance levels tend to rise significantly during the final stages.
- Secondly, we discuss the timing around when key conditions to the offer are satisfied, e.g., when the 50%, 75% and 90% acceptance level thresholds are achieved.
- Finally, we demonstrate how the composition of the target company's shareholder base typically evolves during the various stages of a takeover offer.

Whilst each transaction has its unique characteristics, we find that by aggregating proprietary data from a robust and extensive sample of transactions, we can report findings that are sufficiently representative of general market trends, such as the ownership shift to event driven funds, the restrictions for most passive investors from tendering, and the general tender behaviour and support levels from long-only and retail investors.

Key Facts:

- 20+ transactions reviewed
- Time period 2019 - 2022
- \$60bn+ transaction volume

Market Cap Composition of Target Companies



Source: S&P Global © 2022 S&P Global

Market Cap Segments

Above \$1.5bn	Large Cap
Above \$500m	Mid Cap
Below \$500m	Small Cap

Source: S&P Global © 2022 S&P Global

¹ All transaction data was aggregated, anonymized and ensure data cannot be attributed.

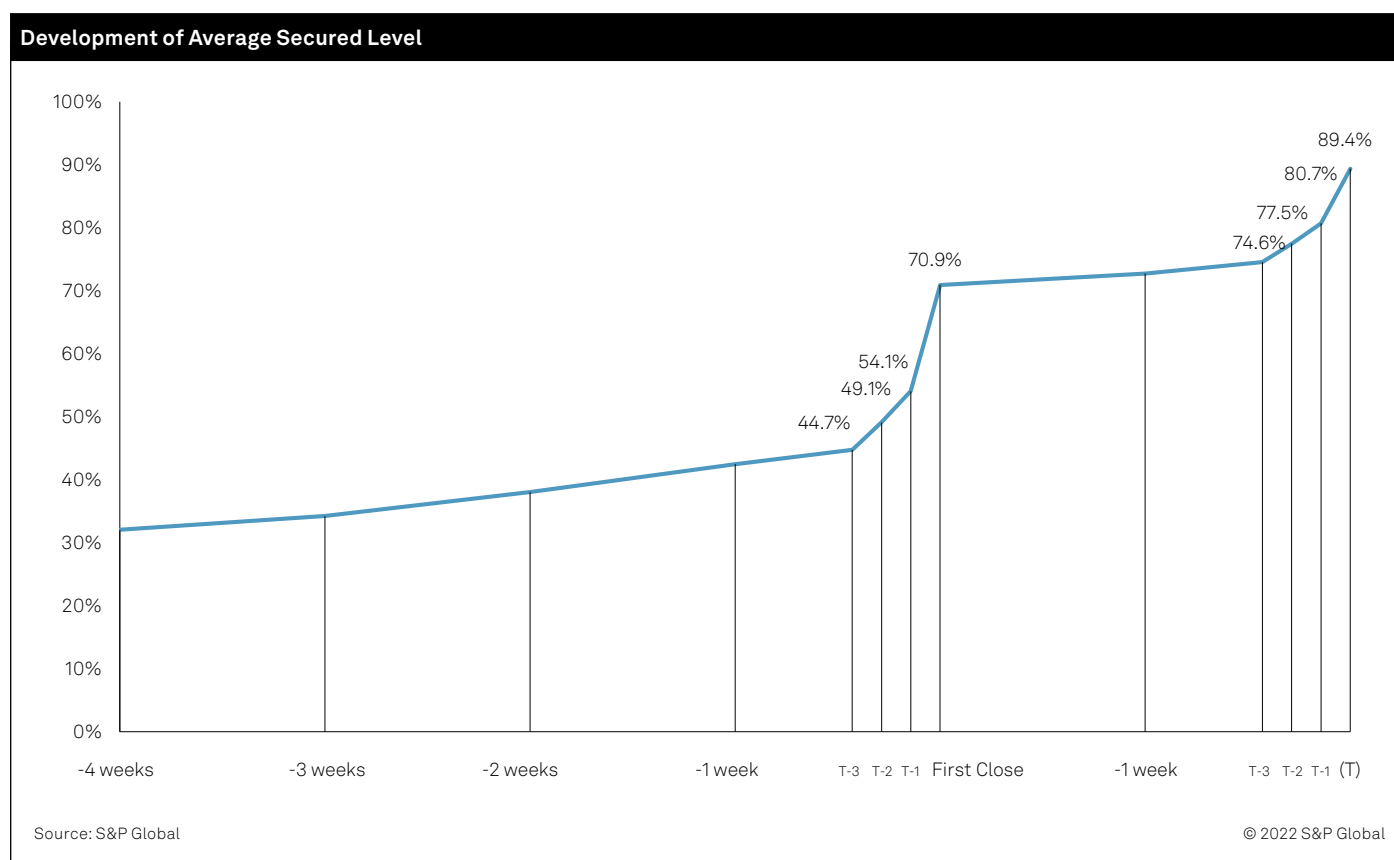
Development of Acceptance Levels

This section explores the typical development of acceptance levels during German public takeover offers.

Exhibit 1 illustrates the average secured tender level during the initial and additional acceptance periods, tracking secured shares as percentage of all outstanding shares, including the bidders direct and indirect holdings, as well

as potential irrevocable undertakings and any tendered shares from the free float. As demonstrated below, the greatest increase in secured levels occurs in the latter stages of the acceptance periods. Notably, many recent transactions were launched with a high level of ownership by the bidder.

Exhibit 1:



Note: "Secured Level" refers to the total ownership secured by the bidder and includes, in addition to shares tendered into the takeover offer, the direct ownership stake held by the bidder, irrevocable tender agreements, and share purchase agreements.

Exhibit 2 focuses only on the shares being tendered into the takeover offer. The results are summarized below:

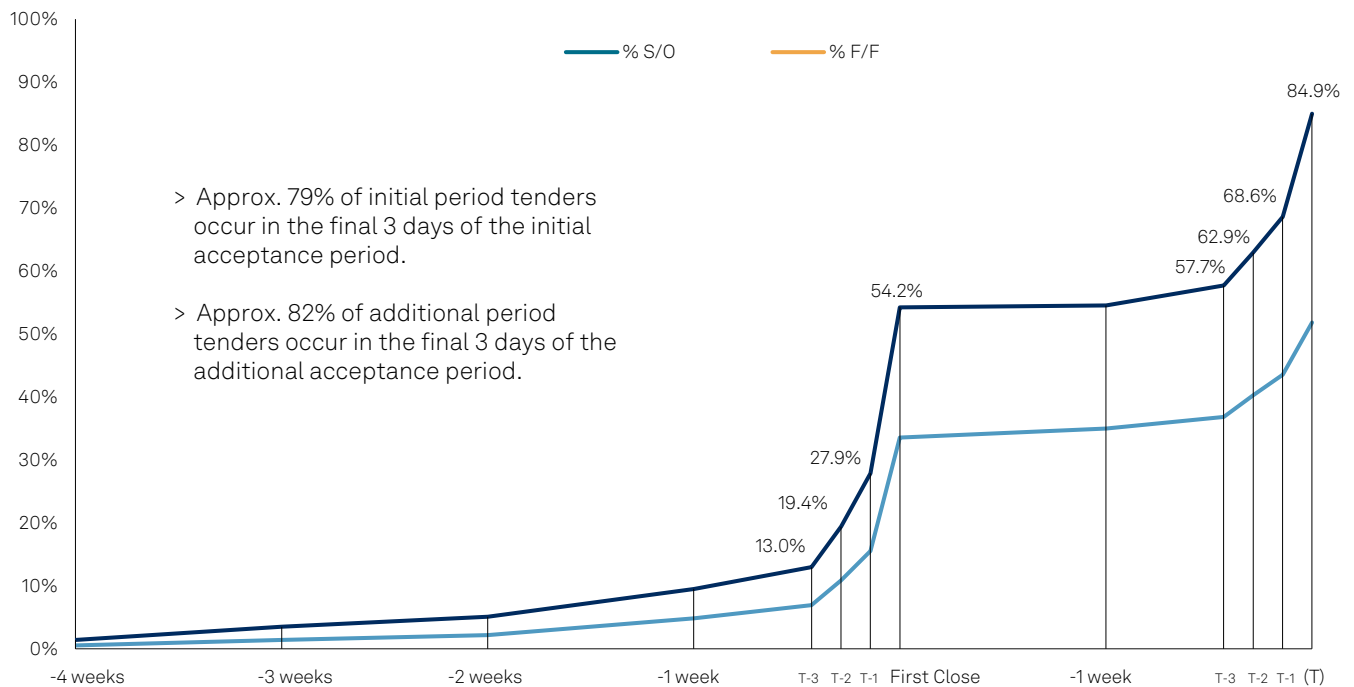
- Tender levels are typically low during the weeks leading up to the closing of the initial acceptance period, with the marginal rate of early increase usually driven primarily by retail shareholders and private wealth managers. On average, only 15% of the total shares that are tendered during the initial period have been tendered by the start of the final week of the initial acceptance period.
- Irrespective of campaign activity, tender levels typically begin to rise at an accelerating rate from the start of the final week of the initial period, driven primarily by long-only active investors who often have their internal deadlines earlier than alternative investors.

² In Germany, if the minimum acceptance thresholds are met in the initial acceptance period, a secondary acceptance period allows remaining investors to tender their remaining shares.

- The acceleration of tender levels intensifies during the final days before the end of the first acceptance period, driven by alternative investors as quantitative funds or event driven/merger arbitrage investors with high conviction in the transaction tender alongside the remaining long-only and retail holders. The final day of the initial acceptance period usually sees the greatest increase in tender levels throughout the entire offer period.
- ETF holdings are still generally constrained by benchmark rules governed by their index providers at this stage, though some of the investors with passive strategies, ETFs, or enhanced-index benchmarks have been identified to have tendered in the first acceptance period.
- The additional acceptance period is usually off to a slow start; however, the acceptance level accelerates again in the closing stages, driven mainly by passively managed funds such as ETFs or investment vehicles with index-benchmarks who depend on their index provider's decision making as well as the remaining merger arbitrage funds and prime-broker collateral which might be held for derivatives and is usually unwound late in the process.

Exhibit 2:

Development of Average Acceptance Level



Source: S&P Global

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A Focus on Conditionality - Acceptance Level Milestones

This section focuses on the timing around when key conditions to the offer are satisfied as well as when the usual 50%, 75% and 90% milestones are achieved.

Exhibit 3 illustrates how all the analysed transactions reached their conditional thresholds exclusively during the final week of the initial acceptance period, with 42% of transactions turning unconditional in terms of tender thresholds on the final day of the initial period.

Transactions that achieved their thresholds earlier than others generally shared the following characteristics:

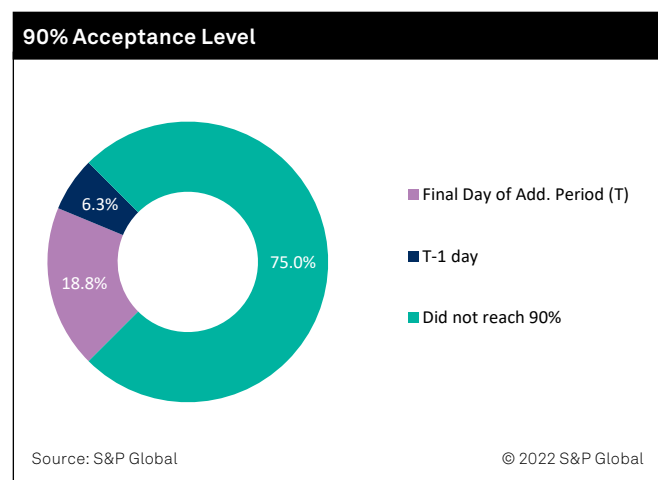
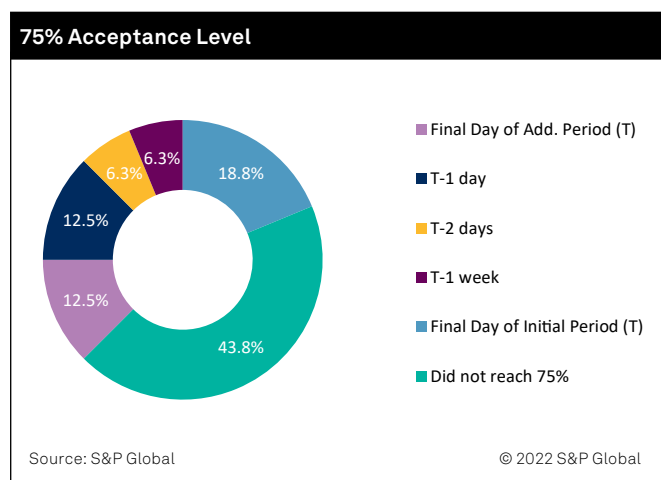
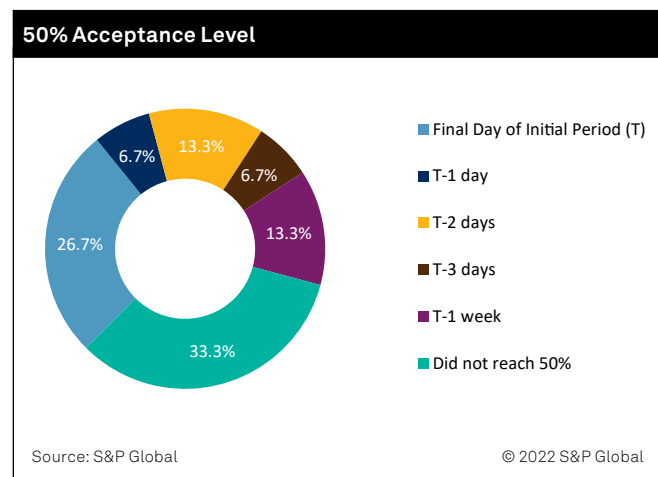
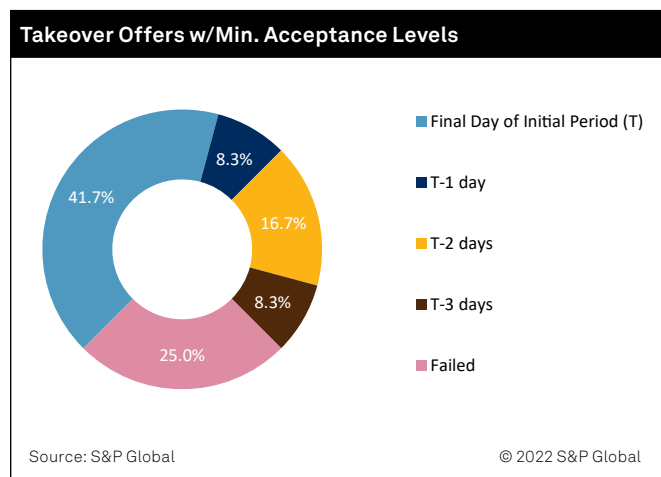
1. premiums considered highly attractive by the market and target shareholders,
2. the bidder managed to secure irrevocable undertakings from top shareholders in addition to potentially building up positions during the offer period, and
3. the absence of opposition in the form of activists or dissidents in the target company's ownership base.

A quarter of the transactions reviewed did not achieve their minimum acceptance thresholds, mainly due to one or more of the following factors:

1. insufficient offer price perceived by the target shareholders,
2. minimum acceptance thresholds set above average by the bidder (>50%), and
3. public opposition and collaborative action against the transaction by activists/dissidents in the target company's ownership base.

Our analysis further illustrates in exhibit 2 how common acceptance level milestones, defined as 50%, 75%, and 90% in this case, were generally achieved late in the acceptance periods and how higher thresholds were achieved less frequently – only 25% of transactions reached an acceptance level of 90% compared to 56.2% of transactions that reached a 75% acceptance level during the offer period. Furthermore, it should be noted that whilst none of the transactions reviewed achieved an acceptance level of 95% during the offer periods, several transactions did go on to achieve an acceptance level of more than 95% during the de-listing tender offers.

Exhibit 3:



Shareholder base Ownership Development

This section explores how the composition of the target company's shareholder base evolves during the various stages of a takeover offer. These changes are driven by two distinct factors:

1. institutional investors' buying and selling activities shortly after the announcement of the transaction (event-driven prepositioning vs. long-only investors with attractive cost base selling upon announcement), and
2. the tendering of shares into the takeover offer by specific types of investors towards the latter stages of the acceptance period while, for example, certain investment styles such as ETFs are usually restricted to tender until the offer is considered unconditional.

Exhibit 4 highlights the flow of active funds from investors with long-only investment styles and strategies to event driven or merger arbitrage funds as well as the related increase in collateral holdings by custodians and prime brokers, usually for their alternative clients, soon after the announcement of the transaction. On average, the exposure of hedge funds to the target's remaining free float almost doubles from pre-announcement (12.7%) to post announcement periods (24.4%), with prime-broker collateral and trading positions shooting up from 4.8% to 13.2% (+175%) during the same period, making alternative investors the largest investor group remaining in the free float towards the end of the acceptance period. The ownership composition of the target company typically remains relatively stable during the first number of weeks of the acceptance period, with the next major shift occurring during the final week of the initial acceptance period. What follows is a description of the key developments during the various stages of an acceptance period.

Final week of the initial acceptance period:

- During this period, active long-only and merger arbitrage investors usually drive-up tender levels based on their degree of conviction. This results in a relative increase in ownership by passive funds, who's proportion of the remaining free floats steadily increases from 7.3% to 12.8% at first-close.

At close of initial acceptance period:

- The composition of the remaining free float is usually driven by alternative investors holding 25.0% and their prime brokers controlling 18.7% of the remaining shares. The behavior of alternative investors depends on the factors initially mentioned, with transactions that require lower thresholds excluding a domination agreement (DPLTA), or a perceived attractive offer price usually leading to higher support even in the initial acceptance periods.
- Long-only strategies account for about 31% of the remaining shares.
- The relative exposure of passive investors increases to 12.8%, due to their tender-restrictions, and retail investors account for about 10% of the remaining free float.

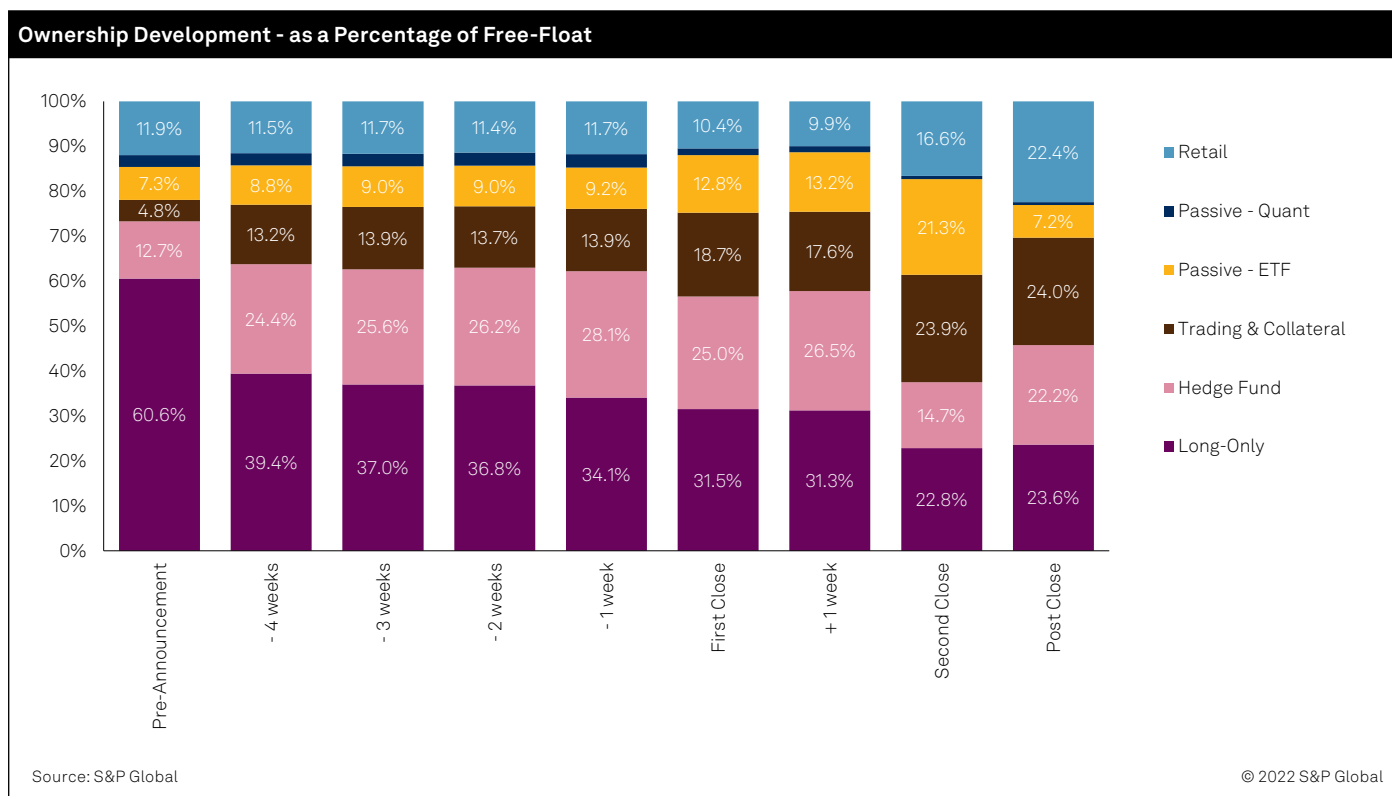
Secondary acceptance period:

- During the two-week secondary acceptance period, alternative investor - hedge fund ownership is mainly comprised of funds with a more strategic approach that opt to maintain some form of optionality, often holding on until the very last deadline before instructing their prime brokers about their tender decision. Hence, holdings by prime brokers who service these strategic funds also remain elevated and together with hedge funds, they account for the largest share of remaining free float exposure, on average 38.7%.
- At this point, ETF funds, which are typically restricted from tendering early, represent a significantly larger proportion of the remaining free float, on average 21.3%. Depending on conditionality and acceptance threshold development, most of these holdings are usually tendered into the offer at closing auction or when index-benchmarks or their providers adjust their compositions.

Post-close:

- Alternative investors are by far the largest investor group after completion of a tender period and post close. They account for almost half of the remaining free float shares (46.1%), mainly driven by event driven strategies focused on squeeze out or back-end trades.
- Long only investors account for 23.6% of the remaining free float shares, usually with the main rationale of not being convinced about the attractiveness of the offer or having alternative options.
- Passive investors and ETF ownership at that point decline significantly, triggered by minimum free float requirements of index providers, resulting in the deletion of the stock from the benchmark index. While most large ETF-providers usually have policies that allow them to hold up to 5% of unlisted stock in their portfolios, most positions are tendered at the closing auction, showing a steady decline of passive investments at that point.
- Retail investors remain a large group of who do not tender into the offer. The reasons are numerous, from lack of conviction to simply not being aware of the public takeover offer or uncertainty about the process to instruct and accept the offer.

Exhibit 4:



Conclusion

In this analysis we aimed to illustrate the capital market dynamics behind public tender offers in Germany and focused on some of the most critical and commonly queried themes by the deal teams around the topic.

As demonstrated in this report, acceptance levels almost exclusively experience a late uptick in the final week of both the initial and additional acceptance periods, with the final three days in each period accounting for most of the total shares tendered into the offer.

Naturally, the lack of tender activity during the initial stages of the offer period can be a cause for concern for the relevant parties in a transaction as they assess the chances of success and seek visibility over whether or not the necessary thresholds will be secured. There are however proactive tried and tested measures that can be taken in order to improve the visibility around investor behaviour during the offer period, such as carrying out a thorough analysis of the target company's shareholder base on an ongoing basis and conducting a well-executed shareholder engagement campaign to obtain investor sentiment and project the overall outcome of the transaction.

Furthermore, the report identified that conditionality is achieved late in the initial acceptance period and that transaction characteristics such as irrevocable undertakings, market sentiment towards the offer price, a potential domination agreement (DPLTA) and the presence of activist investors play an important role in determining the outcome of German public takeover offers.

We find that the shareholder base of a target company changes significantly during the various stages of a takeover offer. The first significant shift occurs shortly after the public announcement of the transaction, with active funds flowing from long-only to alternative investors. As a result, alternative ownership, collectively, can drive the success of a takeover offer. Through direct engagement with this group of investors, we determine early on what the main objectives of the event-driven community are and assess to what extent they would impact the overall outcome of the transaction.

Depending on the deal progression, ETF ownership may begin to account for a larger portion of the remaining free float before declining rapidly if triggered by minimum free float requirements of index providers, resulting in the deletion of the stock from the benchmark index. Daily monitoring of ETF flows provides a means to track the overall level of ETF ownership in the target company and understand at what stage of the offer period these funds can be expected to tender.

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About M&A Advisory Team at S&P Global

The M&A Advisory team at S&P Global takes a data driven approach which combines market intelligence, shareholder tracking, investor engagement, and tender analytics solutions. This, together with our deep experience and understanding of issues surrounding public takeovers, enables us to provide a comprehensive offering that complements the efforts of the deal team towards securing the success of the transaction.

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