2015 | Canadian deals announced, sector report and more
Perspectives from your leading global mid-market M&A advisor

Capital Markets Flash

Canadian M&A Deals Quarterly

In this issue

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Large cap deals dominated, driven by pension funds

Overview of 2014

2014 365 days, 2,812 deals, $206.1 billion total aggregate value

Q1 679 deals $41.6 billion

Q2 748 deals $45.8 billion

Q3 713 deals $50.6 billion

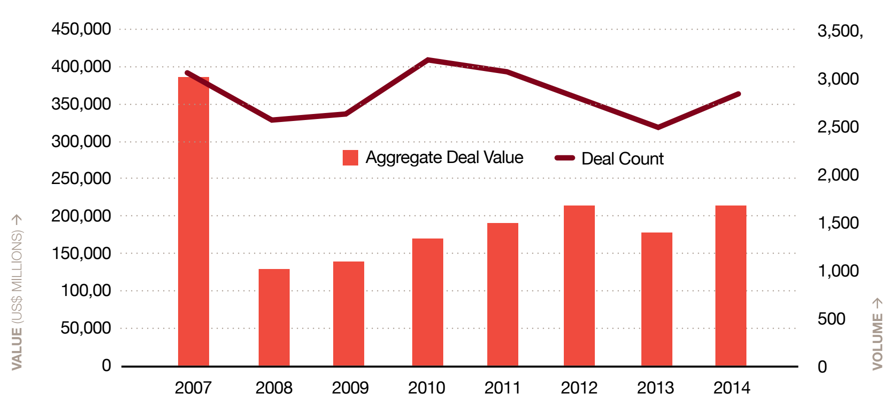
Q4 672 deals $68.1 billion

Overall, 2014 was a strong year for M&A in Canada. "With valuations increasing and the fading of the value gap that has existed in many industries since pre-crisis 2007 levels, sellers were keen to make deals," says Nicolas Marcoux, Canadian Deals Leader. "Strong valuation, evidenced by high EBITDA multiples by historical standards in many industries, continued low lending costs and growing confidence in the US market also made 2014 a good year despite sluggish activity in the mining sector."

Compared to 2013, both the number of deals and the total value of deals within Canada grew – by 12.5% and 18.5% respectively. The uptick in deal value was bolstered by a number of large deals (i.e. deals over $1 billion) and a larger average deal value for the large cap segment. Within the mid-market, deal value and total number of deals continued to be relatively stable.

Many of the 2014 large cap deals were driven by pension funds investing abroad (e.g. CDPQ, PSP, CPPIB, BC Investment, AIMCO), although private equity houses, primarily Onex, also played a role. In total, six out of the top 10 Canadian deals during 2014 involved either pension funds or private equity houses – this is compared to 2013, when the majority of deals involved the retail sector.

Annual Canadian M&A
by volume and value , 2007–2014



Sources: S&P Capital IQ, PwC Analysis

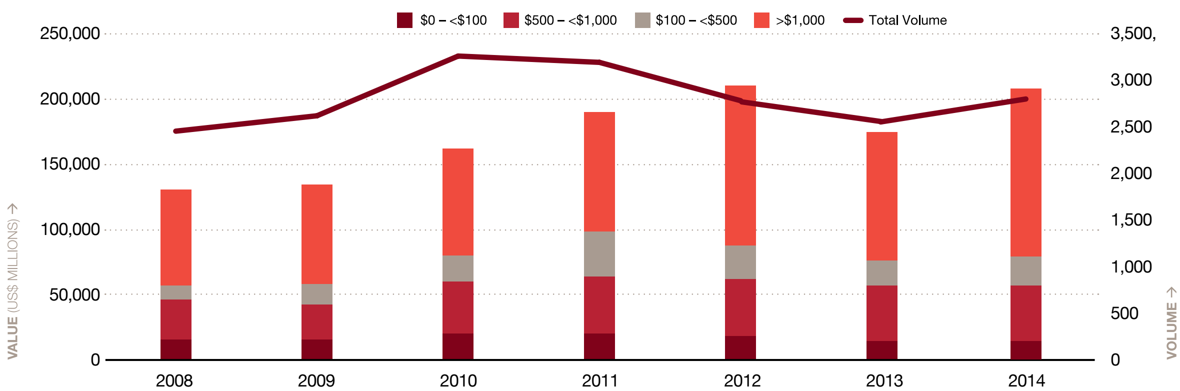
Top 10 announced deals of 2014

Top 10 transactions
by value, 2014

	Announced date	Target / Issuer	Seller(s)	Buyer(s) / Investor(s)	Total transaction value *US$mm, historical rate*
1	15 Dec 2014	Talisman Energy Inc. (TSX:TLM)	—	Repsol, S.A. (CATS:REP)	13,518
2	26 Aug 2014	Tim Hortons Inc. (TSX:THI)	—	Burger King Worldwide, Inc. (NYSE:BKW)	13,374
3	14 Dec 2014	PetSmart, Inc. (NasdaqGS:PETM)	—	BC Partners; Caisse de dépôt et placement du Québec; Longview Asset Management, LLC; StepStone Group LP	8,936
4	04 Apr 2014	Pinafore Holdings B.V.	Onex Corporation (TSX:OCX); Canada Pension Plan Investment Board; Pinafore Coöperatief U.A.	The Blackstone Group, Private Equity Group	7,340
5	29 Sep 2014	Athlon Energy Inc. (NYSE:ATHL)		Encana Corporation (TSX:ECA)	6,980
6	12 Jun 2014	Rational Group Limited	—	Amaya Gaming Group Inc. (TSX:AYA)	4,900
7	20 Oct 2014	Cleco Corporation (NYSE:CNL)	—	BC Investment Management Corporation; Macquarie Infrastructure Partners Inc.; John Hancock Financial Corporation; Macquarie Infrastructure and Real Assets, Inc.	4,704
8	24 Nov 2014	SIG Combibloc Group AG	Reynolds Group Holdings, Inc.	Onex Corporation (TSX:OCX)	4,666
9	05 Nov 2014	TDF S.A.S	—	Public Sector Pension Investment Board; Brookfield Infrastructure Partners L.P. (NYSE:BIP); Arcus Infrastructure Partners LLP; APG Algemene Pensioen Groep N.V.	4,493
10	15 Dec 2014	Riverbed Technology, Inc. (NasdaqGS:RVBD)	Accel Partners; Elliott Management Corporation; CampVentures; Eton Park Capital Management, L.P.; Orbis Investment Advisory Limited	Ontario Teachers' Pension Plan; Thoma Bravo, LLC; Ontario Teachers' Pension Plan - International Investments	3,866
				Total	72,777

Shaded: Deal involving a private equity party.
Sources: S&P Capital IQ, PwC Analysis

Annual Canadian M&A – volume breakdown
by value and volume, 2008–2014



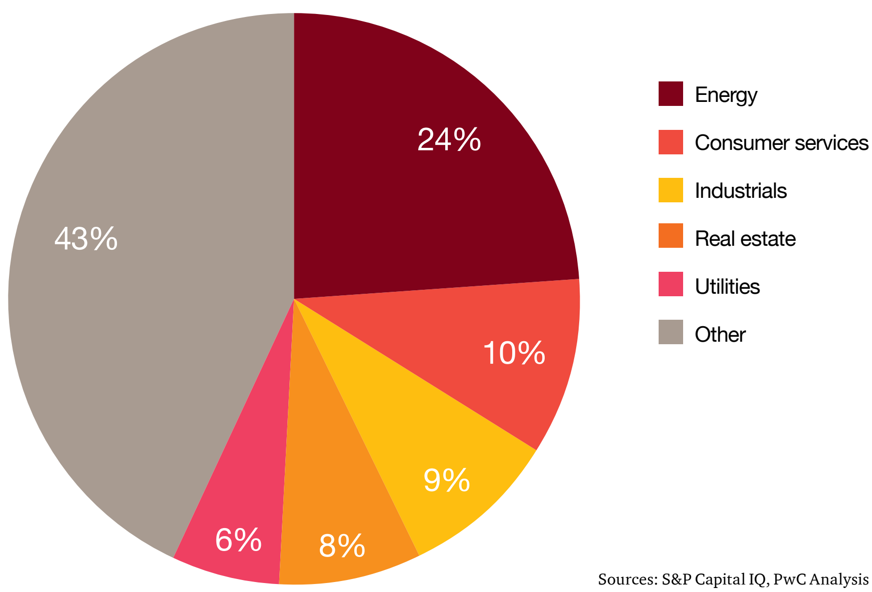
Sources: S&P Capital IQ, PwC Analysis

Industry deals

Despite plummeting oil prices, energy deals dominated in 2014, helped by Repsol's acquisition of Talisman and Encana Corporation's acquisition of Athlon Energy Inc. in Q4. Burger King Worldwide's acquisition of Tim Hortons propelled consumer services into the second spot, while industrials, real estate and utilities rounded out the top five industries by deal value in 2014.

The mining industry continued to be absent from the M&A scene in Canada, reflecting a continued lack of confidence in the sector following major write offs and the inability of several significant players to capitalize on deals made during a feverish 2010 and 2011.

Canadian deal value
by industry



Sources: S&P Capital IQ, PwC Analysis

Q4 highlights

Transactions continued at a solid pace in Q4 of 2014. While the $13.5B opportunistic takeover of Talisman Energy Inc. by Spain's Repsol SA in December led the quarter's activities in terms of deal value, pension funds and private equity stole the show in terms of overall activity – making Q4 an almost perfect microcosm of 2014.

Over the quarter, the focus of many pension funds continued to be on US and international investments as domestic opportunities involving the target assets they desire were limited.

"The challenge for many of these funds looking forward will be to continue to grow despite increasing competition from other international pension funds looking to replicate their model of success", says Eric Lemay, a Director in PwC's Corporate Finance practice.

Top 10 Canadian transactions
Q4 2014, by value

	Announced date	Target / Issuer	Seller(s)	Buyer(s) / Investor(s)	Total transaction value US$mm, historical rate
1	15 Dec 2014	Talisman Energy Inc. (TSX:TLM)	Templeton Global Advisors Limited; Icahn Capital LP	Repsol, S.A. (CATS:REP)	13,518
2	14 Dec 2014	PetSmart, Inc. (NasdaqGS:PETM)	JANA Partners LLC; Fidelity Management & Research Company; Longview Asset Management, LLC	BC Partners; Caisse de dépôt et placement du Québec; Longview Asset Management, LLC; StepStone Group LP	8,936
3	20 Oct 2014	Cleco Corporation (NYSE:CNL)	SSgA Funds Management, Inc.	BC Investment Management Corporation; Macquarie Infrastructure Partners Inc.; John Hancock Financial Corporation; Macquarie Infrastructure and Real Assets, Inc.	4,704
4	24 Nov 2014	SIG Combibloc Group AG	Reynolds Group Holdings, Inc.	Onex Corporation (TSX:OCX)	4,666
5	05 Nov 2014	TDF S.A.S.	Charterhouse Capital Partners LLP; Intermediate Capital Group PLC (LSE:ICP); TPG Capital, L.P.; Ardian; Caisse des dépôts et consignations; Stockwell Capital LLC; Bpifrance Participations SA	Public Sector Pension Investment Board; Brookfield Infrastructure Partners L.P. (NYSE:BIP); Arcus Infrastructure Partners LLP; APG Algemene Pensioen Groep N.V.	4,493
6	15 Dec 2014	Riverbed Technology, Inc. (NasdaqGS:RVBD)	Taccel Partners; Elliott Management Corporation; CampVentures; Eton Park Capital Management, L.P.; Orbis Investment Advisory Limited	Ontario Teachers' Pension Plan; Thoma Bravo, LLC; Ontario Teachers' Pension Plan - International Investments	3,866
7	18 Nov 2014	A 42-Story, 1.2 Million Square Foot Tower at 1095 Sixth Avenue	The Blackstone Group L.P. (NYSE:BX)	Ivanhoé Cambridge, Inc.	2,250
8	06 Oct 2014	80% of Compania Contractual Minera Candelaria and 80% of Compania Contractual Minera Ojos del Salado	Freeport-McMoRan Corporation	Lundin Mining Corporation (TSX:LUN)	2,000
9	06 Nov 2014	DSS Group, Inc.	Crestview Partners, L.P.	Cott Corporation (TSX:BCB)	1,247
10	08 Dec 2014	Ainsworth Lumber Co. Ltd. (TSX:ANS)	Brascan Asset Management Inc.; Brookfield Capital Partners Ltd.	Norbord, Inc. (TSX:NBD)	976

Shaded: Deal involving a private equity party.
Sources: S&P Capital IQ, PwC Analysis

A look ahead at 2015
Companies cautious, yet undeterred

A lot of positive forces are converging to make 2015 a good year for deal-making in Canada.

"Interest rates are low. There's an aggressive lending environment. US banks are competing in Canada quite aggressively for transaction-related financing"

Richard Pay,
Partner, Transaction Services practice

Additionally, "there's still a lot of cash on companies' balance sheets, which could be deployed for the right deal," says John Matheson, a Director in PwC's Transaction Services practice.

Each of these factors is an important driver to the availability of financing – making deals easier to get done. And borrowing costs should remain low, at least in the short-to-medium term, given the Bank of Canada's surprising decision to cut its overnight lending rate to 0.75% in mid-January as a result of plunging oil prices.

Inbound deals into Canada could be bolstered by the weakening Canadian dollar amidst the European Central Bank's quantitative easing and a strengthening US economy. "Canadian assets are becoming notably more affordable," Pay says. "If there are landmark assets out there – large and mid-sized Canadian companies with a leading market position or product – they will become more affordable to some investors."

However, big deals like the 2014 merger of Burger King and Tim Hortons and CNOOC's 2013 acquisition of Nexen may be dampened. Increased regulation and scrutiny of US tax inversions will reduce the tax advantage of big deals out of the US. China's slowing economic growth, on-going crackdown on corruption, and tougher Canadian investment rules for state-owned entities will continue to impact inbound deals from China. "For China – in particular in the resources space, with resource prices where they are right now – it's difficult to fathom inbound mega deals in the near future," says Matheson.

Governments could be major players

When it comes to deals activity, the government could be a big player in 2015 and beyond. "Across the country, almost every government, including the federal government, is looking to address revenue shortfalls," explains Matheson. That means we could see more assets on the table. In October, a commission lead by former TD Bank CEO Ed Clark recommended that the provincial government sells-down its interest in Hydro One's distribution business and Hydro One Brampton. Such moves could spur additional private sector investment within key industries with significant government ownership.

80% of Canadian CEOs plan to enter a strategic alliance or joint venture over the next year

30% of Canadian CEOs said they expect to undertake a cross-border M&A over the next year

36% of Canadian CEOs said the country was very important to their growth prospects

70% of Canadian CEOs are expecting to implement cost-reduction activities over the next year

Canadian CEOs also see M&A on the horizon

The opinion of Canadian CEOs supports the potential for further deal activity in 2015. As part of PwC's 18th Annual Global CEO Survey, released in January 2015, over half of Canadian CEOs said they expect to undertake domestic M&A over the next year. These results are much higher than last year, when only 32% expected to participate in domestic M&A. Other types of deals are also higher on the Canadian corporate agenda – 80% of Canadian CEOs plan to enter a strategic alliance or joint venture over the next year, compared to 67% last year.

The high focus on domestic M&A isn't surprising to Matheson. "I think Canadian companies can learn from the US retailer Target [which came to Canada expecting immediate success]. If you're a Canadian company…just because you are successful at home doesn't mean you'll be successful abroad," he says.

Lessening focus on US for international growth

While the weakening Canadian dollar will likely help increase the focus on domestic deals and economic activity, a number of Canadian companies plan to continue looking internationally for growth. In fact, 30% of Canadian CEOs said they expect to undertake a cross-border M&A over the next year, compared to just 17% last year.

Such international M&A may not be easy – at least not for Canadian companies. "International acquisitions suddenly got a lot more expensive," cautions Pay. "While it might be a good idea to grow internationally, the already strong purchase price multiples, when combined with the weaker Canadian dollar, may make it notably more challenging to achieve the required returns from an international acquisition. However, for those that are well capitalized and have a longer time horizon, we would expect to continue to see notable international acquisition activity."

One thing that has changed for Canadian CEOs is the role of the US in their international growth strategies. While the US is still a predominant force for the international growth of Canadian companies, only 50% of Canadian CEOs said that the United States was very important to their growth prospects, compared to 69% in last year's survey. Meanwhile, China was seen as increasingly important; 36% of Canadian CEOs said the country was very important to their growth prospects, compared to under a quarter last year.

CEOs are acting with more caution

Despite Canadian CEOs being optimistic about deal activity in 2015, caution is still a driving factor when it comes to their investment priorities. Managing costs was identified as a critical priority, with 70% of Canadian CEOs expecting to implement cost-reduction activities over the next year.

And, while many Canadian CEOs expect their headcount to increase over the same time period, over 40% say that they've already increased their reliance on alternative service delivery (e.g. contractors, part-time workers, outsourced functions or service agreements). This suggests that, while many Canadian companies are pressing ahead with their strategic plans, they are also embedding a higher degree of flexibility into their operational models in the event the future is more tumultuous than anticipated.

Pay isn't surprised companies are being cautious. When it comes to deal-making, he's already seen it. "Over the past twelve months, I've seen companies being very focused during the due diligence of the companies they are acquiring," he explains. "They are also being careful about modelling scenarios and sensitivities. Interest rates. Foreign exchange rates. Commodity prices. We are seeing buyers willing to pay full prices for great businesses but being a lot more circumspect / cautious when looking at less well positioned acquisition opportunities."

More than ever, companies want to be confident in their investment decisions. They want to be sure a transaction will work, even with some flexing of market factors.

"Companies won't be afraid to walk away," Pay says about what's ahead for 2015. "It's a competitive deal environment. We'll probably see, particularly financial investors, looking for opportunities in different areas – sectors that may not have been traditional focus areas…but they will continue to be very careful not to go where they are not fully comfortable and when they do move into unfamiliar sectors to structure deals to best protect their downside risk."

SPOTLIGHT ON

Oil and gas: The impact of the oil price plunge on Canadian M&A

Even with the drop in oil prices, 2014 was a reasonably robust year for transactions in both the oil and gas industries. "Both commodities, oil and gas, had a decent run through 2014," explains Clinton Roberts, PwC's Alberta Deals Leader. "There was renewed optimism in gas and, while oil was pretty consistent …through the summer, and even into the fall, we were seeing good deal flow."

Gas outlook is Moderately Optimistic

On the gas front, the deals forecast is relatively stable, except when it comes to liquid natural gas (LNG). "The pace of liquid natural gas (LNG) deals is slowing in Canada," says Roberts. And with no final investment decision (FID) on LNG in Canada, increasing international supply and decreasing demand, Canada is not likely to be seen as a significant LNG market in the short-to-medium term. As a result, "The M&A that came from investors trying to pick up LNG reserves has slowed," says Roberts. "We expect to see that trend continue through 2015."

But traditional natural gas should be more stable than the last few years, from a deals perspective, despite the recent decline in prices. "The current price is $2.62. But, if you look at the average price for the past year," Roberts explains, "It has been above the average production cost in Western Canada."

The weakening Canadian dollar has somewhat buffered the impact of price reductions, both for natural gas producers, and for producers the oil industry - where market prices have plummeted far more dramatically. "The majority of contracts involve US dollar based revenue and Canadian dollar based expenses," says Dave Planques, National Leader of PwC's Corporate Advisory and Restructuring practice. "So the industry is definitely benefiting from the lower Canadian dollar."

In late December, Spain-based Repsol SA acquired Talisman Energy Inc., making it Canada's biggest deal for 2014. After a drawn out sales process and multiple rounds of offers and negotiations, Repsol and Talisman agreed on a purchase price. This price may be lower than what some would have expected in the summer, however, given the current price environment, it's anticipated the shareholders will approve the deal at a vote in late February.

Oil price plunge likely to result in both distressed and strategic M&A

Oil prices may have plunged, but the impact on deals in the oil patch will be a lot different than when prices plummeted in 2009. "In '09, we had a global crisis and no one was certain about what was going to happen," describes Roberts. "Everything just stopped. Restructuring didn't happen. Deals didn't happen."

The current decline in prices is occurring in a vastly different economic environment. Oil prices might be down, but the rest of the North American economy is doing quite well. Even within the oil industry, there are positives. "The volume of oil exports is in good shape," says Roberts. "In fact, in December 2014, we had a record month of oil exports from Canada. The highest monthly volume ever."

Looking ahead, forward price curves suggest oil prices will remain under $60 a barrel into December 2015, with a $15 differential on average for Western Canada Select (WCS). "This is going to create a number of distressed deals, primarily in oilfield services," suggests Roberts. "There will be a handful of exploration and production (E&P) companies that you will see transactions on as well."

Deals will come from two sides. "First you will have healthy companies that run out of capital and need new capital to keep producing, exploring and developing," says Planques. "And

then you will see some companies running into debt covenant and servicing issues, being forced into transactions."

Despite the current price of oil, there is a considerable amount of interest in western Canada for deals, – from private equity and corporate investors, both domestic and international. As a result, there's likely to be consolidation in both oilfield services and E&P. "Many of these will be strategic buys, but there will be some forced distressed sales," says Planques.

The winners are likely to be investors with deep pockets who are willing to take a long-term view. "People who will look at western Canada and say we've had an average cost of production of $65," describes Roberts.

"If a company is pressed for cash flow, now is the time to buy it, knowing that we [Western Canada] will get above $65 in a year and a half-to two years."

Clinton Roberts,
Alberta Deals Leader

SPOTLIGHT ON

Emerging trends in real estate M&A

The Canadian real estate industry has been a good bet for investors in recent years – a trend that is expected to continue into 2015. "Real estate as an asset class has performed extremely well for its investors," says Lori-Ann Beausoleil, Partner and Co-Leader, Forensic Services practice and Real Estate Advisory Leader. "It is a safe investment with good value and steady cash flow."

That's one reason why pension funds have been as active in the real estate space as they chase yield. They have historically owned the majority of trophy assets (i.e. Class A assets) in Canada largely because of the lower cost of capital afforded to them. However, with vacancy rates being low, good rents and good tenancy, locked-in Class A assets are providing a nice yield for their owners. This means there's little chance that the owners of these assets will be selling in the near future.

So in order to chase yield, Canada's pension funds, operations and REITs have gone global to acquire assets that can provide the return they're looking for. Even globally, however, there's no certain bet when it comes to Class A assets. Increased competition – including sovereign wealth funds – means the Canadian plans aren't always winning their target assets.

With few Class A assets available, Beausoleil is seeing another big trend emerge in the industry. "If you can't buy it – build it," she explains.

According to PwC's Emerging Trends in Real Estate 2015 report, urbanization is no longer an emerging trend in Canada; it's the new normal. With people flooding the downtown core in major cities to live, work and play – it comes as no surprise that developers are following as there is a demand for real estate in our urban cities. Commercial, residential and retail opportunities abound and with many traditional investors and developers working together, we are seeing a new real estate class emerge, being mixed–use facilities.

Immigration and demographic trends only enhance the business case for all types of urban developments. Both aging baby boomers and millennials are demanding residential options in the heart of Canada's major cities, which, in turn, increases demand for retail and services. At the same time, major companies are relocating from the suburbs in order to attract the millennial talent they need to be sustainable.

"The traditional transactions market has changed over the past 3 years," Beausoleil says. "It is really shifting to the development side."

Lori-Ann Beausoleil,
Partner and Co-Leader, Forensic Services practice and Real Estate Advisory Leader

With such trends spurring new developments in major cities across Canada, Beausoleil expects 2015 to be another good year for the industry. "A net new asset class is emerging [mixed-use]. Cap rates are still very low. Interest rates are low," she says. "These are great converging trends for those looking to buy or develop real estate."

That's not to say the industry won't have its challenges. The dropping price of oil, Target's withdrawal from Canada – these could both impact the real estate industry, although it might not be as negative as some expect. "While oil prices are plummeting, we're not seeing mass impact on tenancies," Beausoleil explains. "No one is taking their foot off the gas pedal yet."

Beausoleil believes the biggest challenge ahead for the industry could be interest rate changes – a topic that has dominated conversation in the industry for several years. "A number of landlords are still leveraged," she says. "If they had to renew at higher interest rates, it could have a very negative impact on their bottom line and profits could be wiped out in a heartbeat."

With the Bank of Canada's decision to lower its key overnight lending rate to 0.75% in January, interest rates are likely to remain low, at least in the short term. Yet, the possibility of interest rate increases will continue to be a significant industry threat.

"I'm bullish on real estate for the next few years as long as interest rates stay the same," Beausoleil says when asked about the future. "But, if interest rates change – all bets are off."

For a detailed look at the trends in the Canadian real estate market, see PwC's Emerging Trends in Real Estate – Canada and the US, 2015

www.pwc.com/ca/realestate

SPOTLIGHT ON

Retail – The impact of Target missing its mark

In mid-January, successful American retailer Target announced plans to liquidate its 133 stores in Canada—a mere 22 months after opening. On the same day, Japan's Sony Corporation also announced plans to shut its Canadian retail outlets. More recently, Jones New York announced that it will close its 36 Canadian stores by the end of 2015. Given 2014 included a number of other high profile closures, liquidations and bankruptcies (e.g. Mexx, Jacob, Benix, Bombay Company), you can't help but wonder what 2015 has in store for retailers.

"Increased competition and continuing pressure on margins will lead to increased deal activity," expects Michelle Pickett, Partner in PwC's Corporate Advisory and Restructuring practice. "You will see more deals because companies will either need to source additional capital, or a partner or purchaser with greater financial resources and/or synergies, or they won't be able to survive and may be sold through a liquidation or restructuring process."

Target's failure has broad impact

Target's liquidation will have a resonating impact on others in the industry – starting with the remaining low-cost retailers who will still be competing during the process. "Target projects up to $500 million in revenue [from the liquidation] over the next three months," says Pickett. "So anyone competing with Target will be affected over this period."

The closure of Target stores could also have a significant impact on industries beyond retail. "Target had leased approximately 15 million square feet of retail space and 5 million square feet of office and warehouse space," explains Nadia King, a Partner with PwC's Private Company Services practice. "This will result in unforeseen supply in the real estate market."

Recognize Canada is a distinctive market

Does Target have a lesson for other international companies or investors considering the Canadian market? "Don't take Canada for granted," suggests Pickett. "Many US retailers are surprised to find that retailing in Canada is not the same as the US, and that the Canadian consumer may be different from the US Consumer. International investors need to understand the nuances of the Canadian retail market prior to investing - look before you leap."

King agrees. "Canadian consumers have certain expectations of existing international retailers, and they expect that those expectations will be met here," she says. International retailers or investors must understand what Canadians expect and make sure they can deliver those expectations while achieving their target return, or they may find themselves following in Target's footsteps.

King also suggests retailers consider investing in an omni-channel presence. "Canadian online retail sales are at $25 billion a year and are expected to reach $40 billion in 5 years, resulting in a significant opportunity for retailers to gain market share in a competitive market landscape."

Canadian retailers well-positioned

But Target's failure in Canada doesn't necessarily mean that Canadian retailers will become more cautious. In fact, many Canadian retailers are looking at how they can become more relevant in an ever increasingly competitive market. For many, that means increasing deal-making to drive diversification efforts. "Drug stores are selling electronics and a much broader range of food products," Pickett provides as an example.

And now could be an opportune time for smart retailers. "With the Canadian dollar expected to remain low for the foreseeable future – there should be less cross-border shopping, which should increase the number of consumers looking to shop at home," says King. "If retailers can identify ways to differentiate themselves, keep their costs down and meet the consumers' expectations, they should be successful in the retail market going forward."

But the competition in the retail industry may keep some deal-makers away. "While's there's significant liquidity in the private equity market, I don't think the retail sector is where they will invest in 2015." Pickett explains.

Total Retail 2015
For a more in-depth view of what's happening in the retail industry in Canada – look for PwC's Total Retail report

www.pwc.com/ca/retail

BY LORI-ANN BEAUSOLEIL

Required to Report

Preparing for the new *Extractive Sector Transparency Measures Act*

WITH THE INTRODUCTION of the *Extractive Sector Transparency Measures Act* (ESTMA), the Canadian government is taking its commitment to anti-bribery and corruption (ABC) to the next level. Resource and mining companies that have interests in Canada need to be prepared.

"This Act will make it compulsory for companies to report government payments to the public," says Kelly Ohayon, a partner in PwC's consulting and deals practice who specializes in ABC matters. Reporting requirements will include payments to foreign and domestic governments, government bodies and, subject to a two-year transition period, Aboriginal groups.

Given the broad scope of the Act, legal advisors should speak with their clients about potential exposure. "This proposed legislation isn't limited to Canadian headquartered companies," explains Michael Dixon, a partner with Blake, Cassels & Graydon LLP. "Foreign-headquartered companies operating in Canada can also be affected by this Act."

Indeed, even non-extractive companies could be affected. "A lot will hinge on the definition of control, which is broadly worded in the Act and will likely be set out in more detail in the regulations," says Brian Graves, co-leader of the global mining group at McCarthy Tétrault LLP. "Private equity firms and other financial institutions with substantial stakes in Canadian companies could potentially find themselves subject to these reporting requirements, even though they're not operators."

While many companies are already required to track and record payments to public officials as part of the *Corruption of Foreign Public Officials Act* (CFPOA) and similar legislation in other jurisdictions, the scope of the ESTMA is unique.

"It will be important to have properly structured internal controls and compliance systems … to ensure all payments are properly recorded and reported," says Dixon. "Ultimately, a director, officer or internal auditor is going to need to sign off on the report, so having a system in place that gives those individuals confidence is essential, particularly because, if there's a false statement, there can be personal liability."

To enhance the reliability of any statements, legal counsel should work collaboratively with accounting and compliance advisors who have expertise developing and evaluating compliance programs and conducting related compliance audits.

One design challenge will be making sure companies can track information at the level of granularity required under the Act. "Companies will need to look at the different payment categories that need to be reported on," explains Krista Mooney, leader of PwC's ABC group in Alberta. "They will need to undertake an exercise to review who they make payments to in the various categories and what systems and processes may require enhancement in order to ensure completeness of their reporting obligations."

Though reporting is only required for payees when cumulative amounts are greater than $100,000, companies will need to track, review and record all payments to specified payees to ensure they are meeting their reporting obligations.

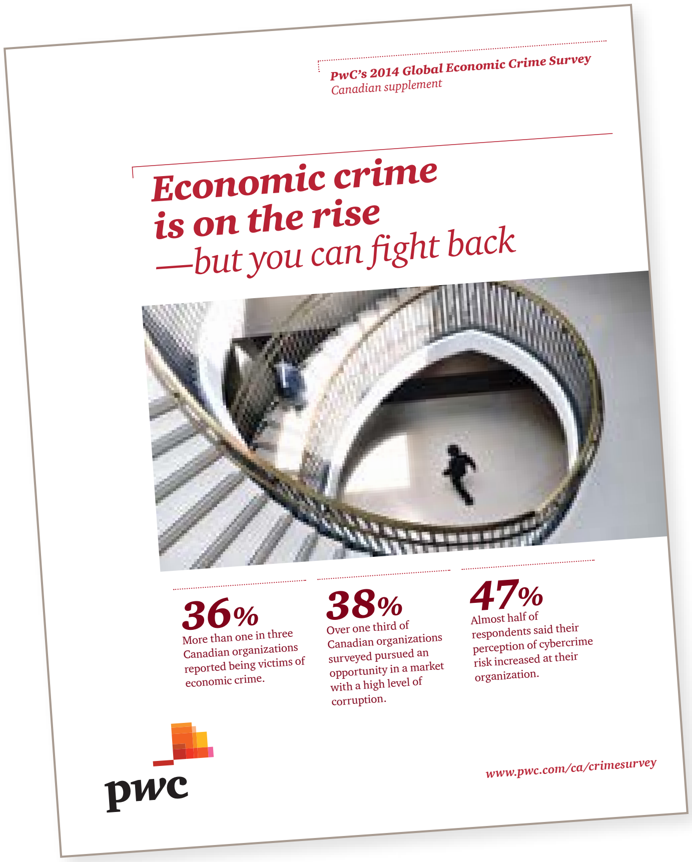
"A lot of companies may think they are covered because their external auditors look at significant payments," says Ohayon. "But there is no materiality threshold associated with this Act." As a result, companies may need to enhance their records and incorporate new controls into compliance programs. For example, companies can incorporate payment categories defined in the Act into their general ledger structures and into their compliance audits.

Companies considering M&A transactions in the sector will need to pay particular attention to the new legislative requirements. "You wouldn't want to acquire a company and then be liable for after-the-fact financial penalties for a target's failure to disclose properly under the Act," says Graves. "A violation could result in an initial penalty of up to $250,000, but since each day that the violation persists is considered to be a separate offence, this initial penalty can multiply quickly and the potential financial hit to a company for non-compliance is very substantial."

With ESTMA expected to be enacted in spring 2015, there isn't a lot of time for companies to get prepared. Companies need to start now if they want to make sure their systems, processes and compliance programs are aligned with the proposed requirements. "Don't wait for the regulation to come out to think about what measures you, or your client, need to put into place. No company wants to be scrambling at the last minute to ensure they are meeting their reporting obligations under the Act," Mooney advises.

Lori-Ann Beausoleil, CA, Deals Partner, is National Co-leader of PwC's forensic services practice.

Global Economic Crime Survey 2014 – Canadian Supplement



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PwC survey shows up-and-down 2014 IPO market outpacing year-ago levels

The market for initial public offerings (IPOs) on Canadian exchanges produced just five new issues in the third quarter, the same volume of new equity issued in the previous quarter but enough to push total proceeds from the first three quarters of 2014 to the same level as all of 2013, the quarterly PwC survey of IPO markets shows.

Two issues on the TSX in the third quarter and three IPOs on the TSX Venture brought the total for the quarter to $531 million, the PwC survey revealed. In the first three quarters of 2014, issuers generated more than $2.6 billion in new equity vs $2.7 billion for all of 2013.

The third quarter of 2013 saw seven new offerings on all Canadian exchanges with a total value of $802 million.

The largest issue in the third quarter of 2014 came from the oil and gas sector — the $500 million placement on the TSX by Northern Blizzard Resources Inc.

Dean Braunsteiner, national IPO services leader at PwC, points to the Northern Blizzard issue as an example of two notable trends in 2014. "It's a classic 'good news/ bad news' story," Braunsteiner says. "The higher volume of new issues we have seen in previous years has been swapped for fewer issues of a larger deal size. While that speaks to the quality of the issues reaching the market, the number of issues is less encouraging. Then there's the activity in the oil and gas sector: four new issues this year compared to just one last year suggests the sector has replaced REITs as a driver of the market. That's good for Canada but a broader market with issues from a variety of sectors would be more reassuring."

It is not unusual for a single sector to drive the IPO market, Braunsteiner points out. The US market has relied heavily on the technology industry to drive its IPO activity this year while consumer products have dominated in Europe and Hong Kong. The larger IPOs from the tech sector in the US have yet to ignite activity in Canada, Braunsteiner notes.

The departure of the mining industry from the TSX Venture exchange has left a gap that could be filled by companies in medical technology and healthcare, says Braunsteiner, industries where early stage funding from public markets can propel growth.

PwC has conducted its survey of the IPO market in Canada for more than 10 years. The reports are issued on a quarterly basis to provide information to the corporate sector, investors, the media and others that will help them put the market into better perspective.

For the purposes of the survey, investment vehicles such as structured products are not considered IPOs because they do not represent new equity raised for operating companies.

"Relative to last year's equity markets, 2014 saw Canadian IPO value driven by fewer larger offerings across a wide sector range, with multiple IPOs seen only in the oil & gas and mining sectors."

Geoff Leverton,
Partner, Transaction Services

Red light
Green light

Canada's IPO Market 2010–2014

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Getting Ahead of the Activists

How boards can use financial analysis to be ready for hostile takeover bids and shareholder activism

BY SEAN ROWE AND STEVEN COLLIA

WHEN IT COMES TO mergers and acquisitions, most boards have a strategy for evaluating any transactions proposed by their management teams. They recognize the need for appropriate due diligence and will often engage third party financial advisors. The big challenge for boards comes when transactions are proposed under less than optimal circumstances, such as a hostile takeover bid or a targeted move by an activist shareholder. In these cases, boards have very little time to evaluate options and respond in a manner that best reflects their fiduciary obligations.

In the case of a burgeoning issue like shareholder activism, some boards may be less ready to act than others. Shareholder activism typically refers to a play by a shareholder, or group of shareholders, to force a change in the strategic direction, operations or financial structure of a company. Their goal is to increase the value of their investments.

In the United States, there's been a significant increase in shareholder activism over the last five years. Between 2009 and 2013, the amount of assets under management by activist investors rose from approximately $36-million to $89-billion.[1] Surprisingly, however, the majority of companies may not be ready for an activist's call. A 2014 PwC poll of senior management, C-suite executives and directors found that only 30 per cent of respondents believed that their company or management team was currently prepared to respond to an activist's interest.[2]

Regardless of the instrument that might force its hand, the best way for a board to be prepared is to be proactive. Directors should follow a strategy that focuses on maximizing shareholder value and conduct regular portfolio analysis so they can make strategic adjustments long before their company comes into play.

"If you're the target of a hostile takeover, you're in play," says John Clappison, an independent director of Rogers Communications Inc., Sun Life Financial Inc. and Cameco Corp. "The board must ensure they know the most value they can get out of the deal."

When it comes to responding to hostile action, the most effective boards are the ones that consider such actions as a part of their governance. This means conducting periodic financial analysis and proactive portfolio optimi-

John Clappison

> "When it comes to responding to hostile action, the most effective boards are the ones that consider such actions as a part of their governance."

1 Avi Salzman. "How to Profit from Today's Shareholder Activism." *Barron's*. December 2, 2013.
2 PwC's Deals Webcast Series. "Embracing Shareholder Activism: Strategy through Tactical Execution." March 31, 2014.

> Boards need to ensure they are comfortable with the market's valuation of their organization and its components or take appropriate measures.

zation to understand what the company and its components are worth and where there might be unrealized value or, in some cases, overvaluation. While boards receive a lot of information from management on company operations, it's also important for them to conduct their own independent financial analysis. This should include benchmarking performance against industry competitors, monitoring share price movements and reviewing analyst opinions. Directors should take an outside-in perspective for each business, asking whether the company is still the optimal owner for that business, or whether it would generate more value by selling it.

Often, target companies are seen as underperforming by the market – whether that's with respect to share price or their performance compared to industry benchmarks. "It's important to understand if there is hidden value we aren't communicating well enough to the [shareholder] community," says Clappison. Boards need to ensure they are comfortable with the market's valuation of their organization and its components or take appropriate measures. Sometimes that's as simple as enhancing the company's communications strategy, but it could also mean requiring management to take a closer look at the performance of specific divisions or operational areas through a robust portfolio analysis.

Boards should also consider conducting scenario analysis in order to further understand potential risks and how they might respond. Directors need to be aware of, "who they [the shareholder activist or potential acquirer] are, how they might approach it and what they might ask for," Clappison says. But at the same time, management and board members need to focus their efforts on the most likely scenarios. "Don't be paranoid," he advises, "you have a business to run."

CSA INCREASING BREATHING ROOM FOR BOARDS

In September, the Canadian Securities Administrators, proposed amendments to the take-over bid regime in Canada which would give the board of a target organization additional time to evaluate and respond to the action. Among other changes, the CSA proposed a minimum 120-day period for hostile bids to remain open, as opposed to the current minimum of 35 days.

If approved, the amendments would provide target boards with more breathing room to evaluate take-over bids and to seek out alternatives. It would also provide them with time to conduct additional analysis and to gain confidence that any actions they take reflect the best interests of their shareholders. "[The changes] would give us more time to ensure we get the maximum value," says Clappison.

When it comes to making strategic changes, a board should always want to be in the driver's seat. By using a mix of shareholder value-focused strategic planning and regular financial and portfolio analysis, boards can stay ahead of the game and make their company less of a target for a hostile takeover or activist shareholder.

Using independent advisors to help evaluate proposals is essential, Clappison adds. “It’s a key component of a director’s fiduciary responsibilities and good governance.”

Getting independent advice can become even more crucial during hostile activity because events are typically time sensitive and highly visible in the market. “When these guys come knocking, it will cause a lot of trouble. It diverts an enormous amount of management and board time,” Clappison says.

During a hostile takeover attempt or shareholder bid, management must continue to operate the business. Otherwise it runs the risk of losing what leverage it has with its shareholders and the market. An independent advisor can help a board conduct any necessary financial analysis to evaluate the bid or proposed action and identify alternatives, while in the process supporting the board from a governance standpoint. In the case of small or mid-sized companies that do not have mature corporate development functions, obtaining such advice could be instrumental for making sure any actions undertaken reflect the best interests of the company’s shareholders.

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Achieving deal success— from concept to close and beyond

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- Total Transaction Value: Equal to Total Consideration to Shareholders + Total Other Consideration + Total Deferred/Earnout/Contingent Payments + Total Rights/Warrants/Options + Cash and Short Term Investments + Net Assumed Liabilities + Adjustment Size.

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