

M&A: a limited appetite

Bermuda Re/insurance





Bermuda:Re spoke with Ernest Morrison, director and head of the corporate and commercial department at CHW, about the desire for M&A within Bermuda and the recipe for deal success.

What is the appetite for mergers and acquisitions (M&A) among Island re/insurers at present?

I am getting the sense as things stand right now that there may well be an appetite, but that it is not being satisfied. The market has gone a little quieter in the last six to nine months, with far less activity than in 2012 and 2011. A notable recent deal in Bermuda was the acquisition of Alterra by Markel, which was a fairly marquee deal. There may be others around with Bermuda companies as targets or acquirers—we are aware of White Mountains considering a target in Israel—but right now the appetite for M&A looks to be relatively quiet. There is a lot of corporate activity in the ILS space.

Is rising interest on the convergence ILS side muting M&A?

It probably is. It is hard to imagine that it would not be connected. Clearly those funding sources that have an appetite for the risk space are finding ILS deals—and to some extent sidecars—an attractive opportunity to enter the market. Investors are evidently attracted to this kind of uncorrelated risk, drawn by the low frequency-high severity risks that constitute the convergence space. If you consider the likes of Validus—which has traditionally been very active in the M&A space—like some of their peers, they are investing in the convergence space in recent months.

Could ILS business help to build up firepower for M&A?

It is hard to say at this stage. The sense I have is that industry players are utilising first class underwriting expertise and selling it in a different way. To that extent they are fully utilising capabilities that they have built up organically as well as through acquisitions. The rise of convergence teams is perhaps a by-product of their activity in the market—both as underwriters and through their buying of underwriting platforms. With most of the big players now in the convergence space, there is a belief that this business will increase

revenues and exposure to new opportunities. A lot will depend on how these vehicles perform and how successful they are for investors, with appetite for further activity reflecting catastrophe-driven results.

Rising levels of convergence activity help to underline the importance of Bermuda as a market for its intellectual capital and underwriting expertise, as well as financial engineering. M&A will form a part of this convergence of capital, thinking and expertise over time.

Are current conditions conducive to M&A and what are the major drivers of such deals?

Availability of capital to make acquisitions, a perception that prices are cheap for the capital you are buying, and the drive to increase critical mass from a capital perspective are all leading considerations. When it comes to scale, companies are looking to establish platforms in all the key markets—Lloyd's, the US, Europe, South America, Asia—and moving away from being mono-line players. Where opportunities to enlarge arise through the acquisition of key platforms, I don't think that will change. Prices may have changed, as has the availability of capital—particularly in the last 12 to 18 months..

Will strengthening share prices help drive M&A?

Whether that is instrumental remains to be seen. It is more about seizing opportunities when they arise. M&A is very much an opportunistic proposition. Opportunities tend to present themselves to groups that want to grow out their platforms and service offerings and position themselves in their respective markets.

It is hard to say that share price alone will dictate play, but companies are clearly trying to maximise returns for investors in circumstances where traditional investment returns simply aren't there. Companies are therefore considering other avenues to deliver returns to investors. While opportunities for M&A may be fairly limited at present, these guys won't hesitate if an opportunity presents itself, particularly where capital is cheap.

What is perhaps the biggest challenge facing players considering M&A?

One of a number of pitfalls in M&A is when a company decides to sell itself and goes through a fairly long and time-consuming process to present itself for sale, such that it places a significant burden on management, to the detriment of the operation of that company. This is something that should be avoided.

How does Bermuda help with the M&A process?

Bermuda has sought to adapt conditions on the ground to develop a set of processes that enable a variety of M&A activity. Traditionally, where listed entities are involved, we have offered the amalgamation process as well as the 'bid and tender'-type process. We have recently added the merger to the amalgamation to account for situations where companies want to acquire another entity and their target is purchased

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by way of a merger into the acquirer. This has proved attractive in a number of instances.

We also have schemes of arrangement through the courts. Generally, the offering in Bermuda is beneficial and conducive to M&A and there is a high degree of confidence in the legal system and its infrastructure to get deals done efficiently. Economic issues will, however, remain the main drivers of M&A and will be what drive decision-makers to pull the trigger.

What are the major contributing factors in successful and failed M&A?

The ultimate accolade for an acquirer is that in investors' eyes—and accordingly in the share price—the rationale for the acquisition was validated following the acquisition and that the management and business are fortified. That then encourages management to proceed with M&A again should the right circumstances arise.

When a M&A has not gone well, it can have fairly disastrous effects on the merged entity even if the deal goes through. Worse, it is a failed bid that is either resisted or is not supported by the investors, which disrupts or prejudices management on both sides at the expense of the investors.

How can CHW help companies navigate a way through the M&A process?

We are confident that CHW is on par with the best law firms on the Island. We have assembled a team of highly experienced individuals who have developed extensive experience of all kinds of corporate activity. In the context of a large listed entity, we will work with overseas counsel in the US, the UK and other jurisdictions and we have developed very good lines of communication and confidence with those firms.

We are able work alongside them to get the deal done. Our experience enables us to be ahead of the game and speak to boards with authority regarding all the issues that might confront them and we have developed the level of experience and expertise to be a source of first rate legal advice and guidance for Island players considering their M&A options. ■