

# M&A SPOTLIGHT: CEE

CONSUMER

INDUSTRIALS & CHEMICALS

TMT

BUSINESS SERVICES

ENERGY, MINING & UTILITIES

CONSTRUCTION

FINANCIAL SERVICES

PHARMA, MEDICAL & BIOTECH

TRANSPORT

AGRICULTURE

LEISURE

REAL ESTATE

# CONTENTS

## SURVEY FINDINGS

- 3 Foreword
- 4 Introduction
- 5 Regional overview
- 5 M&A overview
- 8 Tech takes charge
- 10 Regional focus
- 13 Finance and outlook
- 16 Conclusion
- 18 Sector spotlights
- 56 About Wolf Theiss
- 57 Contact
- 58 About Mergermarket

## SECTOR SPOTLIGHTS

### BUSINESS & FINANCIAL SERVICES

18



### CONSUMER & LEISURE

24



### ENERGY, MINING & UTILITIES

32



### INDUSTRIALS & CHEMICALS

38



### PHARMA, MEDICAL & BIOTECH

44



### TECH, MEDIA & TELECOMS

50





**Horst Ebhardt**  
Wolf Theiss

Welcome to the newest edition of the Wolf Theiss Corporate Monitor's M&A spotlight on CEE/SEE.

As in previous years, the Wolf Theiss Corporate Monitor provides an in-depth survey of the current and prospective M&A environment in Central, Eastern and South-Eastern Europe ("CEE/SEE"). Together with Mergermarket, we have analysed the M&A environment in 2017 and the outlook for 2018 in each of the countries that make up the region, with a focus on six key sectors. In order to shed more light on statistical trends and to correlate them with actual experiences in completing deals, we have interviewed dealmakers from a range of industries as well as private equity firms who are routinely involved in regional corporate acquisitions.

Although we saw a slower year for M&A activity in the region compared to 2016, our survey shows growing confidence for the year ahead. An estimated GDP growth of 2.5% for 2017 outpaces Western Europe, North America, and mature markets in Asia. Meanwhile, political and economic environments remain conducive to business. A predicted growth rate of 2.6% in 2018 would appear to support dealmaker confidence.

Infrastructure continues to improve, further strengthening the region's geographical advantages. EU membership has proved a boon for those that have joined, and an incentive for reform for candidates such as Serbia. This optimism is reflected in our survey, with the overwhelming majority of investors saying that their recent experience in the region has strengthened their appetite to conduct transactions in the CEE.

While the region has a distinct profile for investors, opportunities vary from industry to industry. The Corporate Monitor accordingly takes a new sector focus in the second part of the report, analysing the key factors that affect M&A deals on an industry-specific basis.

We hope you will enjoy reading the Wolf Theiss Corporate Monitor's M&A Spotlight on CEE/SEE and that it will provide you with practical guidance in evaluating the potential for completing deals in an increasingly competitive region.

Kind regards,

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# INTRODUCTION

After a vibrant 2016, M&A in the CEE/SEE region has slowed. This reduction in deal activity can be attributed, in part, to the impact of global political events in 2016, coupled with uncertainty over European elections in 2017 affecting sentiment in the first half of the year. Despite strong regional growth, this doubt appeared to hamper dealmaking. A total of 474 announced deals was a year-on-year fall of 55 deals. And value (€25.5bn) dropped by 35% compared with 2016.

Austria tops the table as the most-favourable market for M&A in the region. The country ranked top on all three criteria used to judge business attractiveness: openness to investment, ease of managing compliance and regulatory processes, and the quality of its infrastructure. One of the most-affluent countries in Europe, it boasts the highest GDP per capita in the region.

The Czech Republic, the region's third-biggest economy after Poland and Austria, and one of its most-developed, ranks second in favourability for M&A. Poland ranks third, following a decade in which judicious use of EU funds have helped overhaul its infrastructure. Investor concerns surrounding bureaucracy and an activist government tightening regulation on some sectors are not enough to offset the strength of its large, well-educated, and strategically positioned market.

Dealmaking within emerging markets Bulgaria and Romania is picking up pace, with the countries ranking fourth and fifth respectively. Buoyed by the strongest domestic growth in the EU, Romania's technology and tourism assets are attracting increasing attention. Meanwhile, Bulgaria benefits from its light regulation and low taxes.

The technology, media and telecommunications (TMT) sector has been one of the liveliest in terms of M&A activity for some time, with nearly two-thirds of respondents (62%) expecting it to be one of the most attractive sectors to conduct deals in 2018. CEE has a budding tech start-up scene, able to leverage high standards of technical education and funding from the EU.

More than half of those surveyed (53%) are considering acquiring or investing in a start-up in the region in the coming year. As well as burgeoning TMT start-ups, there is also increasing activity in biotech.

One of the challenges that start-ups have faced in the region is a paucity of both financing and exits for entrepreneurs but growing corporate and PE interest is starting to change this.

Almost three-quarters of our respondents believe that the fundraising environment will improve further over the next 12 months. In Poland, for example, a recent wave of funding rounds has left investors with ample dry powder and a hunger for targets. In Romania, stellar economic growth has made banks less wary of lending. Meanwhile, big corporates in Austria and Hungary are seeking more acquisitions abroad.

While cross-border deals within CEE will continue to be a major contributor to activity, the US is expected to be the largest single source of inbound acquisitions, cited by 29% of respondents, followed by European powerhouse Germany (22%). The UK comes in third in the expectation that its looming break from the EU will encourage British investors to diversify their portfolios into the growing markets of CEE. Some 13% of respondents expect China to lead the pack. Chinese companies have been increasingly active in the region in recent years, with Central Europe seen as a good-value springboard to the continent. Regional governments have competed with one another to attract investment from the world's second-biggest economy.

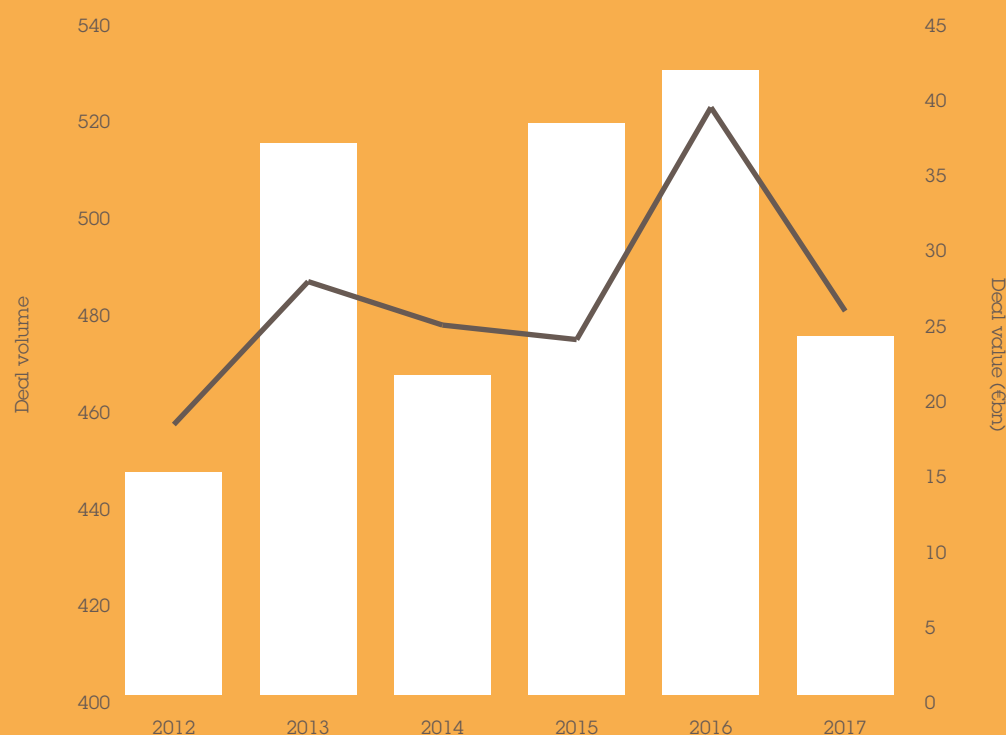
# REGIONAL OVERVIEW

Austria, the Czech Republic and Poland continue to lead the pack in terms of regional dealmaking. Emerging markets Romania and Bulgaria are increasing in attractiveness due to sharp GDP growth and a rise in the ease of doing business. Competition for assets poses the single greatest challenge for dealmakers.

## M&A OVERVIEW

While M&A activity in CEE slowed in 2017, the outlook for dealmaking is strengthening as economic growth continues and the financing climate improves. A total of 474 announced deals in the region with a total value of €25.5bn represents a 35% drop in value compared to the same period last year, with 55 fewer deals.

Overall M&A, 2012-2017



■ Deal volume — Deal value (€bn)

Announced Date	Target Company	Sector	Target Country	Bidder Company	Bidder Dominant Country	Deal Value €(m)
18/12/2017	BUWOG AG	Real Estate	Austria	Vonovia SE	Germany	5,029
24/01/2017	Raiffeisen Zentralbank Oesterreich AG	Financial Services	Austria	Raiffeisen Bank International AG	Austria	4,129
21/12/2017	UPC Austria GmbH	Telecommunications: Carriers	Austria	T-Mobile Austria GmbH	Austria	1,900
21/02/2017	Zabka Polska sp. z o.o.	Consumer: Retail	Poland	CVC Capital Partners Limited	United Kingdom	1,296
19/05/2017	PGE Energia Ciepła S.A. (former EDF Polska S.A.)	Energy	Poland	PGE Polska Grupa Energetyczna S.A.	Poland	1,015
12/12/2017	Unipetrol AS (37% Stake)	Chemicals and materials	Czech Republic	Polski Koncern Naftowy Orlen SA	Poland	997
26/10/2017	Synthos SA (37.54% Stake)	Chemicals and materials	Poland	FTF Galleon S.A.	Poland	582
04/12/2017	Netia SA (66% Stake)	Telecommunications: Carriers	Poland	Cyfrowy Polsat SA	Poland	527
04/10/2017	Griffin Premium RE. N.V. (67.9% Stake)	Real Estate	Poland	Globalworth Real Estate Investments Limited	Channel Islands	415
21/12/2017	A&D Pharma Holdings N.V.	Medical: Pharmaceuticals	Romania	Dr. Max Lekarna AS	Czech Republic	400

### POLAND & AUSTRIA ATTRACT BIG-TICKET DEALS

Poland topped the table in terms of the number of transactions, with 143 deals worth a total of €7.1bn announced in 2017. The €1.3bn acquisition of retailer Zabka Polska by Luxembourg-based private equity (PE) firm CVC Capital Partners from Mid Europa Partners topped the charts, followed by the €1.1bn takeover of electricity company EDF Polska by state-owned power company PGE Polska Grupa Energetyczna. These high-cap deals are a result of part-renationalisation of utilities across the region, as governments look to exert more control over pricing and international companies.

Yet it was Austria which attracted the highest deal value of the year following some big-ticket announcements: Vonovia acquired real estate rival BUWOG in a €5bn deal, while T-Mobile Austria purchased cable provider UPC Austria from Liberty Global for €1.9bn. As a result, deal value targeting Austrian firms closed the year at €12.1bn.

### SECTOR WATCH

Business and financial services generated the highest value in 2017, accounting for 24% of total market share, with financial sector consolidation driving dealmaking. The consumer sector was one of the liveliest in terms of volume, accounting for 21% of total activity, though only one deal – the Zabka Polska acquisition – featured in the top ten transactions of the year.

The consumer and leisure sector has benefitted from rising incomes driven both by economic growth and the moves of several governments in the region to raise minimum wages and public sector salaries. Meanwhile, competition in the low-margin retail sector has led some

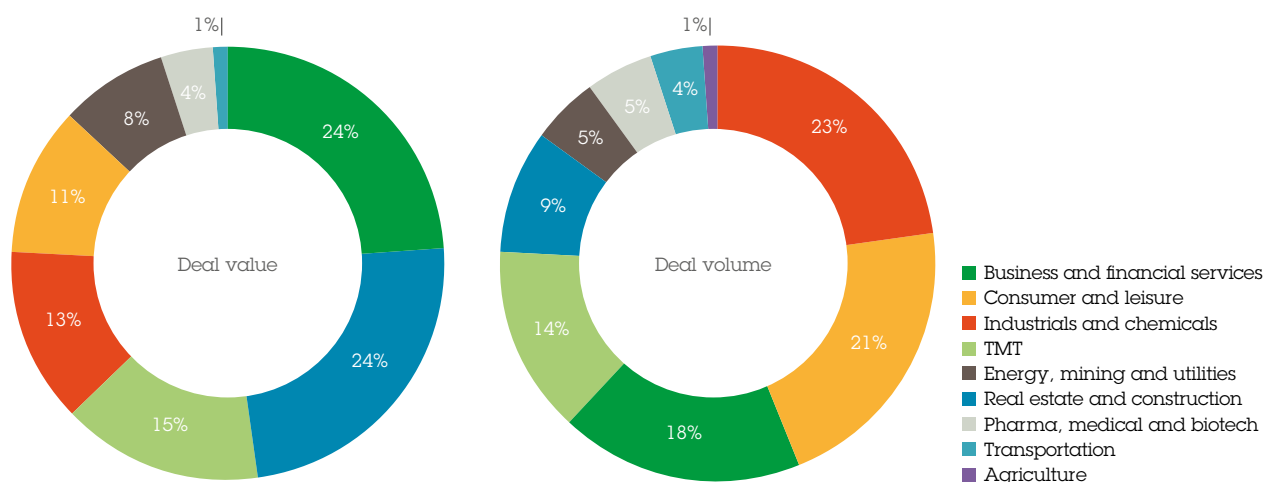
players to look for the exit. The leisure industry has benefitted from both domestic demand and the growth of tourism in hotspots ranging from the Croatian coast to city break destinations such as Budapest.

A heatmap of activity by sector and geography over the past two years shows that the single biggest hotspot of dealmaking by value was the Austrian real estate and construction sector. This was largely a result of the previously mentioned €5bn Vonovia/BUWOG transaction. This was followed by the Czech consumer and leisure sector, with transactions totalling €7.5bn. However, this was almost entirely accounted for by the acquisition of Anheuser-Busch InBev's CEE beer business by Japan's Asahi Group Holdings, part of the realignment of portfolios following ABI's takeover of SABMiller, and Asahi's moves to diversify away from the shrinking Japanese beer market.

Poland's TMT sector has generated deals totalling €4.8bn over the past two years. The €2.9bn acquisition of online marketplace operator Allegro Group by a consortium of PE funds including Cinven and Mid Europa Partners, and the €695m takeover of cable operator Multimedia Polska by US-owned UPC Polska, were among the most significant.

The energy, mining and utilities sector saw aggregate deal value of €9.8bn in 2016-17. This was partly thanks to the aforementioned process of state-led takeovers. However, it also reflected the withdrawal of some major European players as they restructured their portfolios in the wake of the financial crisis and Germany's 'Energiewende' – an EU obligation passed in 2010 to cut carbon emissions and switch to renewable energy sources.

CEE sectors by deal value and volume, 2017



M&amp;A by sector and target country 2016 + 2017 (€ million)

Country	Consumer and leisure	Real estate and construction	Business and financial services	Energy, mining and utilities	TMT	Industrials and chemicals	Pharma, medical and biotech	Transportation	Agriculture	Total
Austria	620	8871	5116	613	3128	369		548		19265
Poland	2952	1117	4548	2575	4815	1644	289	232	5	18177
Czech Republic	7465	2416	400	5194	256	1509	115	285		17640
Romania	833	29	139	1052	244	572	420		44	3333
Bulgaria	332		692	5	36	76	99			1240
Hungary	262	14	466		343	80		32		1197
Slovenia	155	18		45		845	7	7		1077
Ukraine		5	414	276	14		7		165	881
Croatia	275	5		8	230	30		49		597
Slovakia	85				21	105	370			581
Serbia	119		198	6	15	53	42			433
Bosnia-Herzegovina	61	5							24	90
Albania				11						11
Total	13159	12480	11973	9785	9102	5283	1349	1153	238	64522



### FULL STEAM AHEAD

A number of factors are expected to drive transactions over the coming year. First, the generally benign economic climate, with most countries in the region growing steadily, and some (for example, Romania) returning to growth rates not seen since the mid-2000s.

Second, a trend towards consolidation in several sectors, including retailing and banking. Many countries in the region are overbanked, and tightening regulations at the national and international level (Basel III in particular) will make the going tougher for less-healthy players.

Third, start-ups, particularly in tech, are expected to continue to flourish as efforts to boost private-sector and early-stage financing are strengthened.

And finally, the region's location, low labour costs, and generally stable political outlook will continue to draw investors in manufacturing. Added to these are local factors, such as Romania's offshore hydrocarbons, the divestment of Ukrainian assets by Russian investors, and the sale of Greek banking subsidiaries in the Balkans.



# TECH TAKES CHARGE

For some years, the technology sector has been one of the most dynamic areas of the regional economy, with both local entrepreneurs and multinationals capitalising on a talented labour pool that builds on a long tradition of excellent technical education.

Some start-ups have cited growth of up to 200% a year, while the big players have been moving to outsource operations up the value chain in recent years. The region's diaspora has also contributed both funding and knowledge transfer.

Therefore, it is little surprise that the technology, media and telecommunications (TMT) sector is seen as the most attractive by our respondents – cited by 62% as one of the top two industries to watch out for in 2018. Sub-sectors seen as particularly promising are e-commerce, fintech, and data and analytics, each cited by 31% of respondents as among the top two most-appealing areas for investment. Cloud technology was not far behind, acknowledged by 30% of respondents.

"Data will be the deciding factor in the technology space over the coming years," says the CFO of a Swedish corporate investor. "Also, the e-commerce space is in its initial phase for the CEE region and has huge growth prospects."

Poland has established a reputation as one of the leading fintech centres in Europe, leveraging its rapidly evolving and sophisticated banking sector as well as a large domestic market, and government and EU support. Deals in recent years include the acquisition of Kontomierz, which produces B2C and B2B financial information, by German consumer finance group Kreditech. Partnerships between banks and start-ups have helped catalyse growth.

The dynamism of emerging companies in the CEE tech sector is one reason that investors are increasingly turning their attention to start-ups. Some 53% of respondents said that they were interested in acquiring or investing in a start-up in the region over the coming year.

Which sectors do you think will be the most attractive in the CEE region over the next 12 months? (Please select the top two)

Technology, media and telecommunications



62%

Consumer and leisure



44%

Pharma, medical and biotech



32%

Business and financial services



28%

Construction and real estate



18%

Industrials and chemicals



8%

Energy, mining and utilities



4%

Transportation



2%

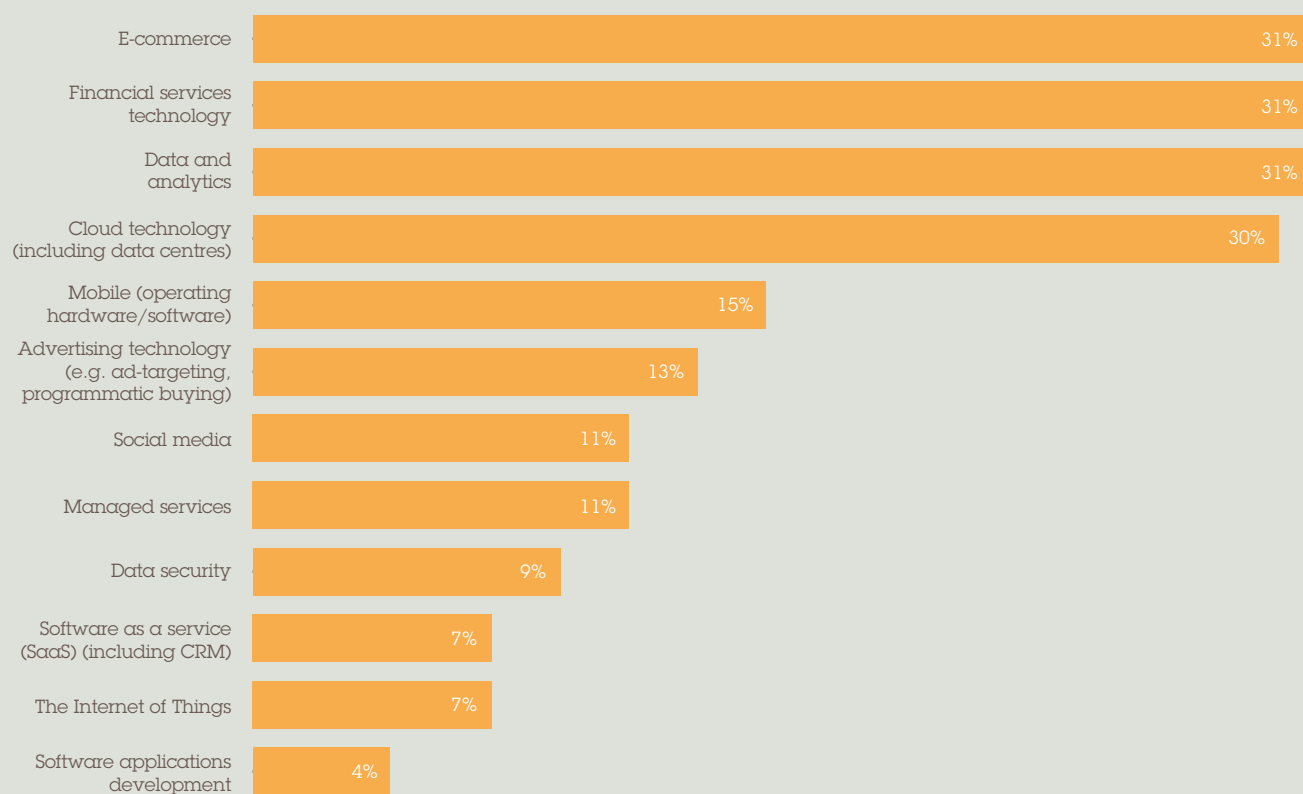
Agriculture



2%

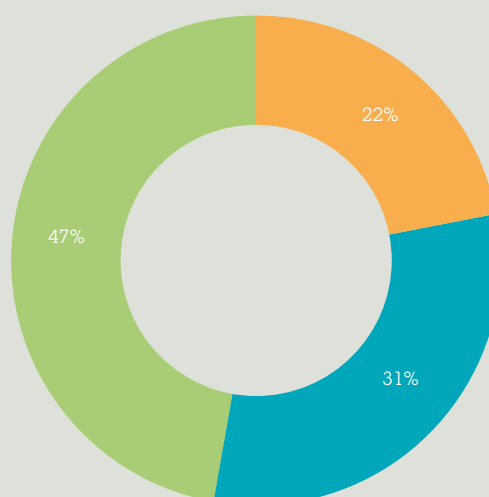


Within the technology sector, which sub-sectors will be most appealing to acquirers of companies in the region in 2018?  
(Please select the top two)



Are you considering acquiring or investing in a start-up company in the region?  
(Defined as a business which was created within the previous three years)

- Yes, acquiring a start-up
- Yes, investing in a start-up
- No, neither acquiring nor investing in a start-up



## REGIONAL FOCUS

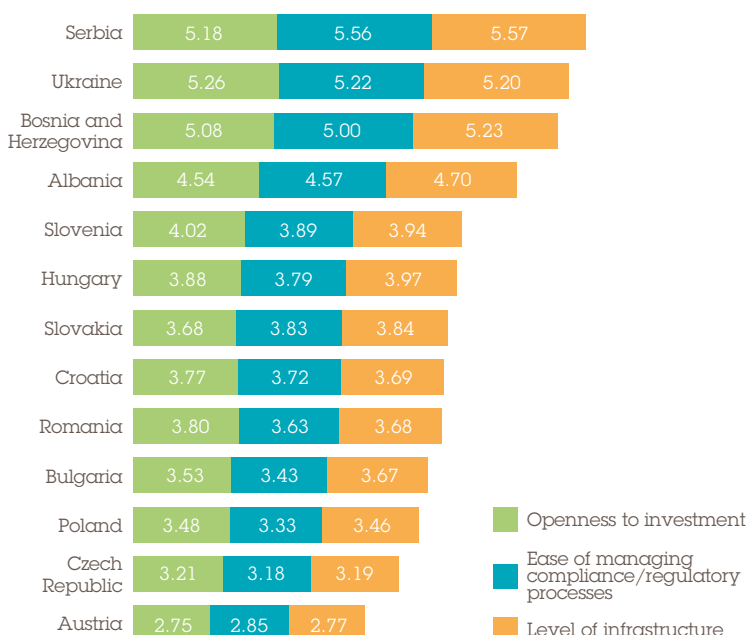
Austria was rated as the most favourable market for investment in CEE, followed by the Czech Republic. Both countries have the advantage of positive growth rates, as well as lower regulations, which make expanding and engaging in business activities easier than other regional markets.

Poland ranked third; the second-largest market in the region by population, the country has enjoyed steady growth for many years, even avoiding recession in 2009 when most of the rest of Europe saw economic contraction. Years of judicious use of EU funding appear to be taking effect, with the country pulling in some high-profile deals in 2017. "We regard governmental support in investments as one of the most important factors to choose an investment location and Poland is one such region," says the CFO of a Belgian corporate. "Further reforms in the tax and legislative procedures are also expected in the years to come, so setting up a strong base now would be ideal for us."

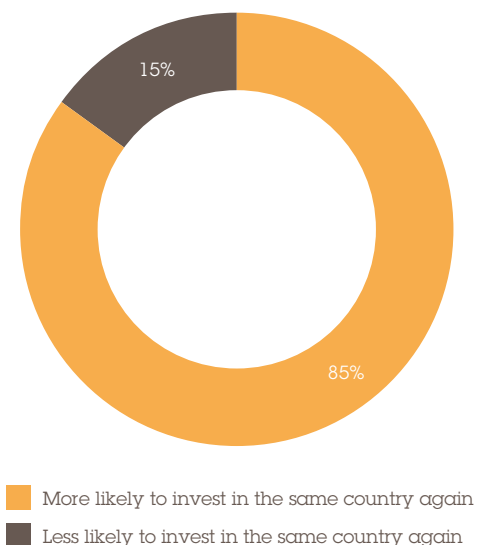
Bulgaria and Romania ranked fourth and fifth, respectively. Bulgaria benefits from its 'light-touch' regulation and low tax regime, which has attracted investors from elsewhere in Europe. "Low minimum wages and low social insurance costs are benefits that we are considering as we are active in the manufacturing sector and need a strong employee base," says the CEO of a Czech corporation.

Meanwhile, Romania's relatively diversified economy is one of Europe's fastest-growing, racking up 8.8% GDP growth in the third quarter of 2017, despite political tensions and concerns about governance. Particularly promising sectors include technology and tourism, though investors continue to wait for a long-awaited wave of privatisations.

Please rate the countries in the CEE region according to the following factors. (Please rate 1 to 10, where 1=most favourable, 10= least favourable)



How has your previous M&A experience in your most recent country impacted upon your CEE strategy?

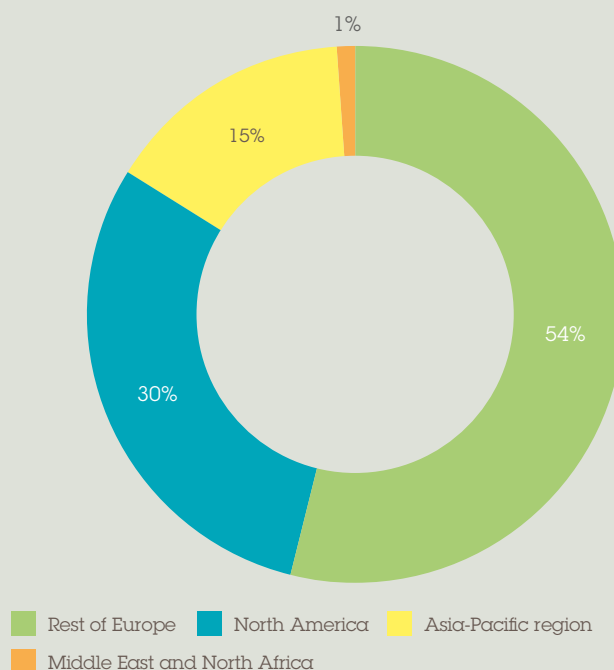


### INBOUND INFLUX

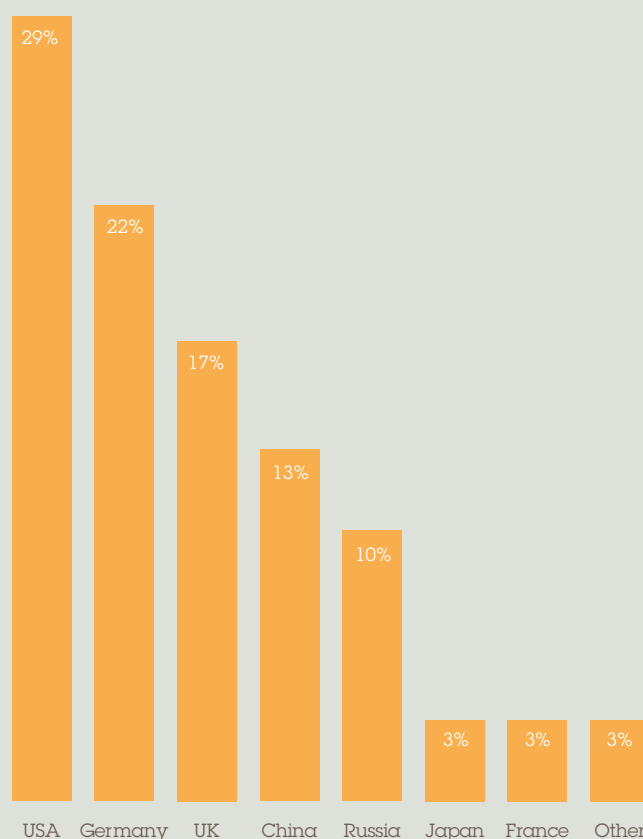
Countries from elsewhere in Europe are expected to continue to take the lead in inbound dealmaking in CEE in 2018, with 54% of respondents saying that the rest of Europe would undertake the majority of non-domestic M&A. North American investors are expected to generate a substantial share of deals with 30% anticipating that the region will be the biggest inbound contributor to activity. While attention continues to focus on Chinese investment in the region, particularly in terms of infrastructure and manufacturing, and although Japan's Asahi made a splash with multi-billion acquisitions in 2016, only 15% of respondents expect the Asia-Pacific region to bring the most deals.

The US is expected to account for the largest proportion of inbound deals over the coming year, cited by 29% of respondents, followed by Germany (22%) and the UK (17%). According to the CFO of a US-based corporate: "In the US, there is a lot of consolidation taking place restricting growth and profits. Companies will look to markets such as the CEE where they can expect higher returns."

From which region do you think the majority of inbound deals into the CEE region will come in 2018? (Please select the most important)



Please specify which country will be the most active inbound acquirer



### CHALLENGES ON THE HORIZON

However, this growing interest in the region has a downside – namely the increasing competition for assets. Our survey reveals that this is the biggest challenge to investment in the region, identified by 79% of respondents.

"The sudden increase in the cost of assets has pushed up the cost of investing," says the managing partner of a Polish PE firm. "With competition growing and costs rising, getting access to companies has become expensive, in turn affecting the efficiency of our business plans."

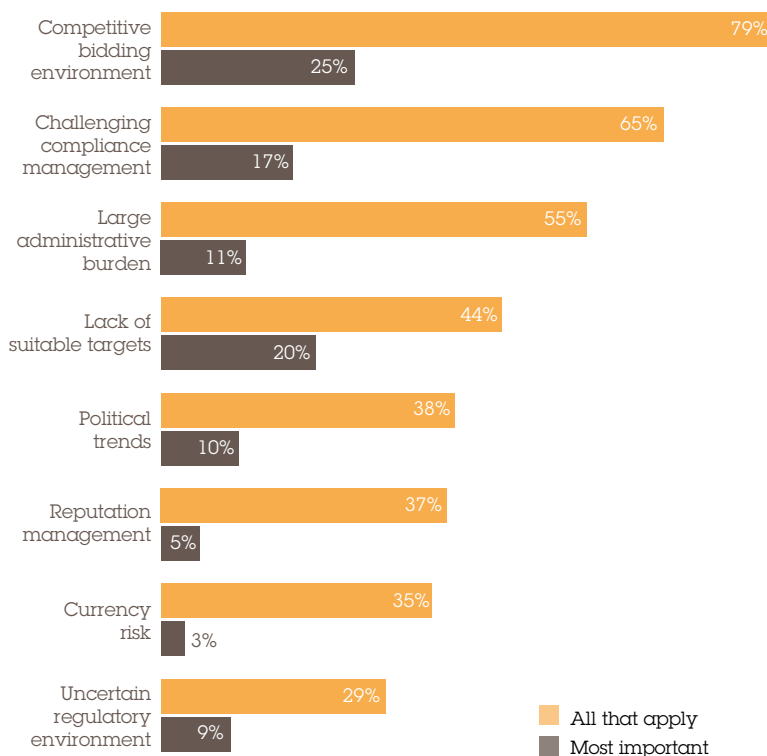
Challenging compliance management and administrative burdens continue to be obstacles for many investors, though competition for investment in the region between countries has pushed many, such as Serbia and Slovenia, to accelerate reform.

### THE BREXIT QUESTION

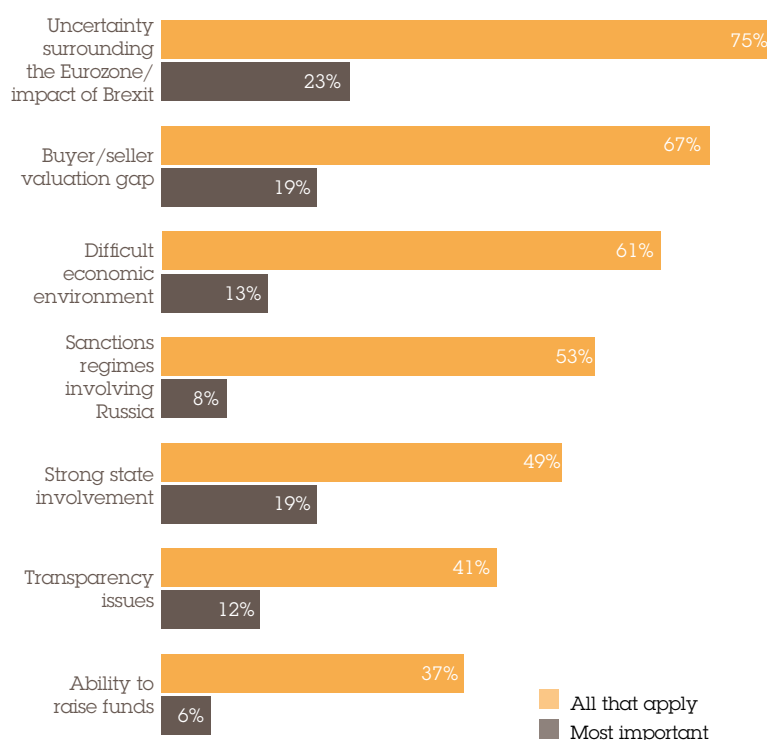
While the economic outlook in 2018 for individual CEE countries ranges from good to excellent, investors are aware of downside risks. Perhaps the biggest of these is looming uncertainty over the European economy, particularly from the UK's impending departure from the EU, and unresolved issues in the eurozone. Our survey reflects this trepidation, with 75% of respondents identifying this as a challenge to implementing their CEE strategy.

London's role as a base for financial investors has led to considerable PE activity in CEE from British-based firms, while some major corporates such as retailer Tesco have a presence in the region. But more significant is the potential shock of a 'hard' Brexit to the European economy, and prior to the exit itself, the uncertainty over what the outcome of negotiations may be.

What do you perceive as the biggest challenges to investing in your specific country of choice? (Please select all that apply and the most important)



What do you perceive as the biggest challenges to implementing your CEE strategy in general? (Please select all that apply and the most important)



## FINANCE AND OUTLOOK

With interest rates remaining low across Europe, and funds in some countries having completed major funding rounds recently, the outlook for fundraising in CEE is positive. Indeed, 56% of respondents expect the fundraising environment to improve 'somewhat' over the next year, while only 2% expect it to become slightly harder to raise funds.

"The overall dealmaking situation is going to improve, because raising capital is going to become easier," says the MD of an American PE fund.

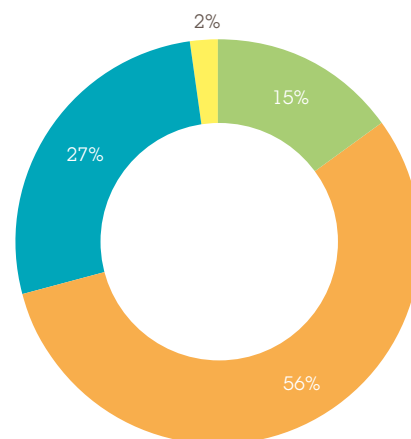
A relatively low inflation environment has also given central banks in CEE the space to keep interest rates low, and in some countries such as Hungary to even consider further cuts. In Poland, a number of PE funds completed financing rounds towards the second half of 2017, and are now keenly eyeing targets. The increased availability of funds from a range of sources also allows investors to pursue a mixed strategy for raising capital.

### DEALS IN DISTRESS

Investors generally see a stable or improving outlook for distressed debt opportunities in CEE, with 32% expecting an increase in targets, and 42% saying that the environment will stay much the same. The process of dealing with distressed assets and non-performing loans (NPLs) in the region in the years since the crisis has been a slow one. Some countries, such as Serbia and Hungary, do not have fully developed legal mechanisms for repackaging and selling NPLs, while in other jurisdictions sales of distressed assets have been held back by concerns that they will further depress asset values. Furthermore, several respondents state that recovering economic growth would ease the levels of distress and lower opportunities for distressed debt-driven acquisitions.

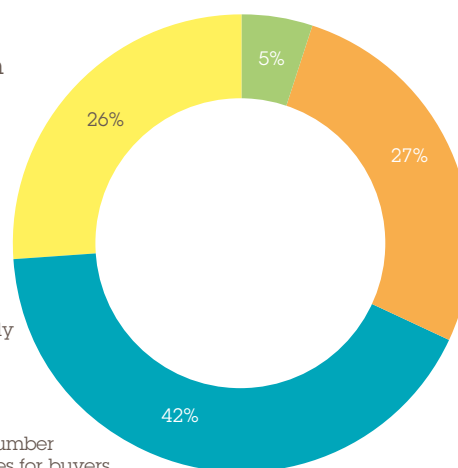
How do you think the fundraising environment for dealmaking in the CEE region will change over the next 12 months?

- It will improve significantly
- It will improve somewhat
- It will remain the same
- It will become slightly more difficult to raise funds



What do you think will happen to distressed debt opportunities in the region in 2018?

- They will increase significantly
- They will increase somewhat
- Remain the same
- There will be a decreasing number of distressed debt opportunities for buyers



### CHASING YIELD

Restructuring activity continues to drive M&A in the region as risk appetite among investors hunting yield is sharpening. On the supply side, several years of slower growth and the likelihood that interests will rise in the medium term will put a squeeze on struggling companies. Meanwhile, time is finally running out for 'zombie companies' that exist in a number of markets.

The sector seen as most likely to see restructuring activity is energy, mining and utilities, cited by 63% of respondents, after a period of lower commodity prices inflicted casualties on the industry. A tighter regulatory and taxation environment under both EU legislation and international treaties such as the Paris climate agreement is also having an impact on the costs of fossil fuel-driven utilities and related extractive industries. Large institutional investors are becoming wary of financing fossil fuel-based industries such as coal-fired power station development.

These trends are also affecting the industrials and chemicals sector, which was cited by 45% of respondents as likely to be among the top two for restructuring activities. "Industrials are facing growth challenges especially with stricter rules and regulations. With the signing of treaties such as the Paris agreement, countries need to turn to green alternatives. This increases overall costs and makes it difficult to achieve growth," says the CFO of a Czech corporate.

Ukraine is seen by some margin as the most target-rich market for restructuring opportunities, cited by 69% of respondents when asked to name the top two. Conflict and economic instability in Ukraine have caused serious difficulties for companies in a range of sectors, and not only those with exposure in the war-torn east of the country. However, the market's size, resources, and pool of skilled labour mean that many investors are willing to stomach downside risks in order to make acquisitions.

"I think Ukraine will offer the most restructuring opportunities for companies, as the Ukrainian market was very badly affected by the Russian crisis," says a partner at a Polish PE firm. "This has forced the government to open the market to help companies affected. Major businesses were left in need of help to get the capital required to pay back shareholders and debt."

Poland, meanwhile, ranked second, cited by 37% of respondents. Changes to the regulation of renewable energy following a collapse in the price of 'green certificates' paid to producers may put operators in the sector under further pressure, leading to potential restructuring opportunities.

In which sector do you expect to find the most opportunities for restructuring over the next 12 months? (Please select the top two)

Energy, mining and utilities



63%

Industrials and chemicals



45%

Construction and real estate



40%

Business and financial services



21%

Pharma, medical and biotech



15%

Transportation



13%

Agriculture



2%

Consumer and leisure



1%

Technology, media and telecommunications



0%

In which sector do you expect to find the most opportunities for restructuring over the next 12 months? (Please select the top two)

Ukraine



69%

Poland



37%

Austria



25%

Romania



16%

Czech Republic



15%

Serbia



11%

Bosnia and Herzegovina



9%

Hungary



9%

Bulgaria



5%

Croatia



4%

Albania



0%

Slovakia



0%

Slovenia



0%



# CONCLUSION

Despite a slower year for dealmaking in 2017, the outlook for M&A in CEE is brightening thanks to sustained growth, greater political stability, and an improving fundraising environment. Indeed, 85% of our survey respondents say they are more likely to invest in the same country again, given their recent experience. The region offers investors greater stability and security than many emerging markets elsewhere in the world, while often providing higher returns than highly developed markets in North America and Western Europe.

EU membership has brought the significant benefit of regulatory harmonisation as well as access to the world's largest single market for most of the countries in our survey. This has promoted the modernisation, expansion, and diversification of industries including automotive manufacturing and pharmaceuticals, both of which continue to develop despite rising competition. While Serbia and Albania face a long path to accession, their gradual integration with the Union is supporting judicial and economic reform that strengthens the investment environment. Energy reform and privatisation in Albania, and the sale of a major state-owned bank and pharmaceutical company in Serbia are both on the horizon for 2018.

Region-wide, TMT continues to go from strength to strength thanks to a tech sector built on high standards of education and generous EU financing. The energy, mining and utilities sector has gone through a tougher period due to regulation and rising costs, but is seeing activity driven by diversification and growing interest from financial investors in cash-generating businesses, as well as ownership changes as companies reassess their portfolios. Tightening regulation will create opportunities in the financial sector, driving consolidation in banking as smaller and less efficient players are affected by capital and liquidity requirements.

Inbound activity looks set to continue apace. Dealmakers are drawn to CEE from around the world, with the US and Germany expected to continue to take the lead in 2018. Chinese investment will continue to flow into the region. This is largely due to its '16+1' approach – an initiative by the Chinese government to intensify co-operation with 11 EU members

and five Balkan countries – which will lead to greater investment, particularly in the infrastructure and manufacturing sectors.

One downside of the resurgence of CEE economies is the growing competition for targets within relatively small and often fragmented markets. This has pushed up valuations and stalled some transactions, including privatisations.

There are also looming downside risks from uncertainty surrounding the UK's impending exit from the EU. Meanwhile, the Eurozone's challenges from Greece and Italy have not been entirely resolved. Domestic politics also play a role, though in many cases investors have now come to an accommodation with populist governments increasing state interventions in certain industries.

Tightening environmental regulations on heavy industry and energy will raise costs, though they may also catalyse investments in renewable energy after a period in which the sector has stalled in several countries thanks to regulatory uncertainty.





#### METHODOLOGY

In H2 2017, Mergermarket surveyed 150 senior-level executives about their experiences and outlook on M&A in the Central Eastern European region. Half of the respondents were based in the CEE region, while the other half was drawn from outside of the region. One third of the respondents are part of private equity firms, while the remainder is comprised of corporate respondents.

All participants in the survey have made at least one acquisition in the CEE region over the past 12 months or were considering making one in the next two years.

The survey included a combination of qualitative and quantitative questions and all interviews were conducted over the telephone by appointment. Results were analysed and collated by Mergermarket and all responses are anonymised and presented in aggregate.



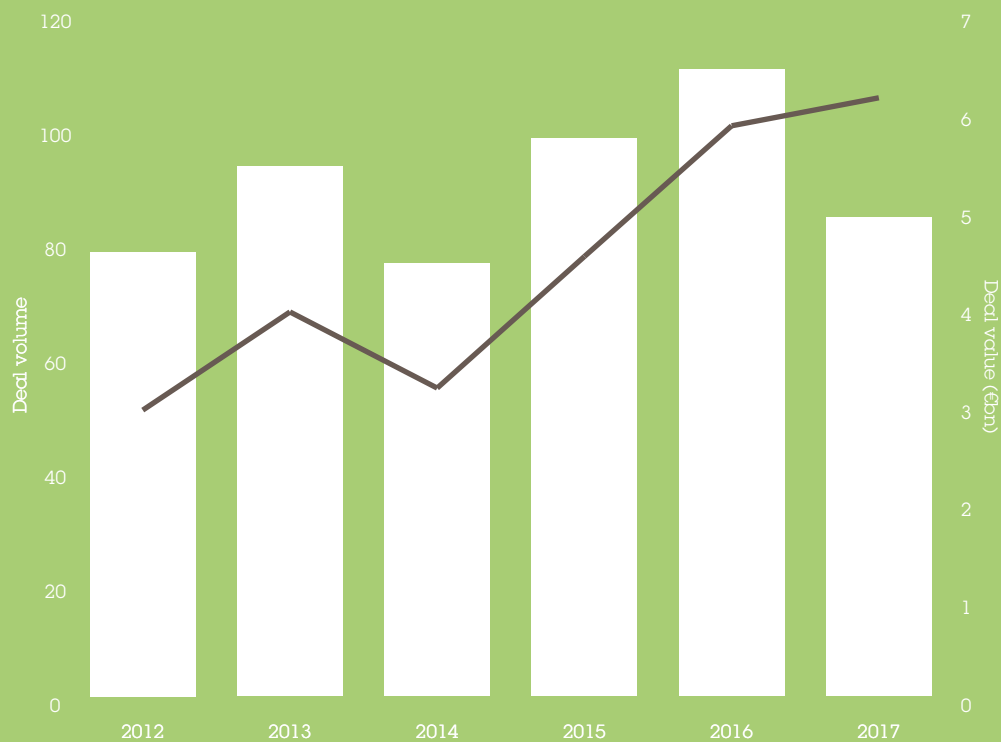
# SECTOR SPOTLIGHTS

We explore the dealmaking environment in six major sectors – from business and financial services to technology, media and telecommunications

## BUSINESS AND FINANCIAL SERVICES

The business and financial services sector is set for a busy year. The rollout of Basel III regulations on capital adequacy and liquidity management is expected to increase cost pressures on banks worldwide, and produce a wave of consolidations. Many markets in CEE are overbanked, sometimes with dozens of banks competing for small market shares while a few big players dominate.

BUSINESS AND FINANCIAL SERVICES M&A, 2012-2017



■ Deal volume — Deal value (€bn)





### POLISH POWER

Some 60% of respondents focusing on the sector are seeking opportunities for investment in Poland, a large and advanced financial services market that is seen as a leading candidate to attract business leaving London in the wake of Brexit. Poland is also seen as the best gateway to CEE for financial services investors, cited by 53% of respondents, followed by Austria (27%), suggesting that Warsaw may be eclipsing Vienna as the region's financial capital.

"The Polish banking sector is one of the most advanced in the world in terms of technical solutions and offerings," says Jacek Michalski, partner at Wolf Theiss, Warsaw. "The clash between fintechs and traditional banks leads to a situation where services offered by the banking sector in general become more and more sophisticated."

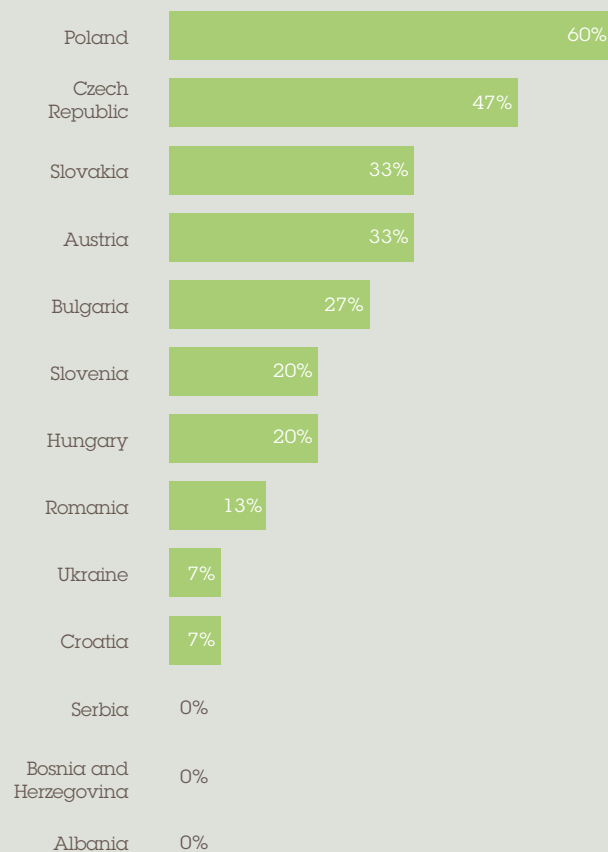
Further consolidation in Poland's banking sector is expected in 2018. In November 2017, the head of Poland's banking regulator said that he would welcome further consolidation in the sector. This followed the announcement of a potential merger between Bank Pekao, the second-largest bank, and smaller rival Alior. Meanwhile, the growing but fragmented mutual fund segment is also ripe for consolidation.

### CZECH FIRMS EYE FINTECH DEALS

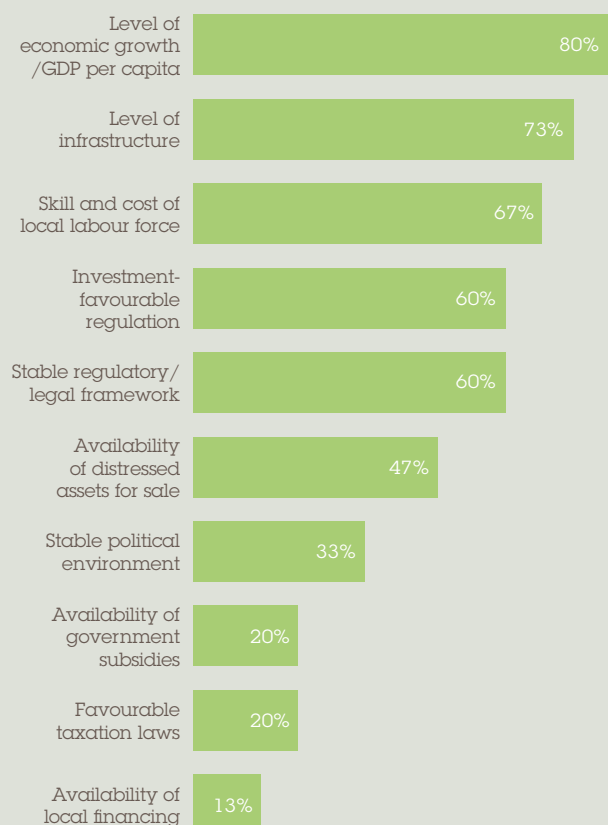
The Czech Republic is ranked as the second most attractive market in our survey, with 47% of respondents seeking a deal in one of the region's most-affluent countries. Jan Kotous, counsel at Wolf Theiss, Prague, says that fintech is a particularly dynamic segment, despite caution from established banks. "We are also seeing movement in trading with crypto-currencies and with crypto-currencies settlement engines or payment platforms," Kotous adds. "This is being pushed forward by fintech organisations in the Czech Republic, which are very active."

The Czech Republic's appeal is unsurprising, given that 80% of respondents in the sector cite the level of economic growth and GDP per capita as one of the most important factors in dealmaking. The Czech economy grew by 4.5% in the year to the second half of 2017, and the economy is expected to top 4% expansion for the full year.

In which country/ies are you currently looking for new opportunities? (Please select all that apply)



What are the factors that will most impact your choice of country for your next deal? (Please select all that apply)



The second most important factor for investors is the level of infrastructure (cited by 73% of respondents), followed by the skill and cost of the local labour force (67%) – the latter being one of the competitive advantages of the CEE region as a whole.

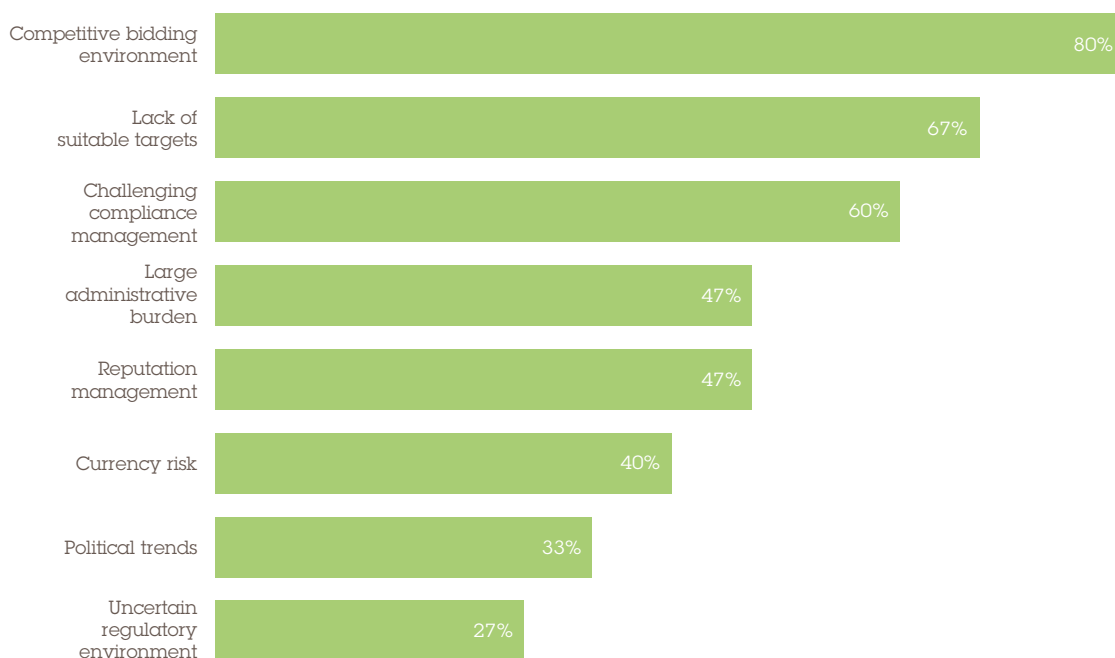
#### GREEK CRISIS FUELS BANKING SELL-OFF

The competitive bidding market is seen as the biggest challenge to dealmaking in the business and financial sector, with 80% of respondents saying that they viewed it as an issue, followed by a lack of suitable targets (67%), and challenging compliance management (60%).

A shortage of targets is less of an issue in South-Eastern Europe, including Bulgaria, Albania, and Romania, where the impact of the Greek crisis of recent years has still fully to play out in the sale of Greek banks' regional subsidiaries. In June 2017, Belgium's KBC completed the acquisition of National Bank of Greece's United Bulgarian Bank (UBB) and leasing company Interlease for €610m, a deal agreed in December 2016.

Katerina Kraeva, partner at Wolf Theiss, Sofia, highlights the influence that the Greek banking sector has on Bulgarian M&A activity within the sector due to the ongoing economic adjustment programme. "There are expectations that some other big banks will be also offered for sale and UBB will not be the only example of these banks exiting our market," she says.

What do you perceive as the biggest challenges to investing in your specific country of choice? (Please select all that apply)







### COMPLIANCE COSTS

Money laundering regulations are seen as the most challenging compliance or regulatory process faced by sector investors in their target countries, cited by 67% of respondents. This reflects both regulation of financial institutions across the world and historic concerns about the source of money in some CEE countries.

In terms of strategy implementation, the buyer/seller valuation gap is seen as the biggest challenge for financial sector investors (73% of respondents), followed by uncertainty surrounding the eurozone and impact of Brexit (67%), and the difficult economic environment (67%).

"There exists a large buyer/seller gap that is further intensified because of the lack of proper ways to agree on the value of a company," says the CFO of a Czech corporate. "Sellers are charging more because of the growth rates of the region and the rate at which new buyers are flocking to the market and engaging in M&A activities."

### ALL EYES ON BREXIT

Uncertainty about how the final Brexit deal will affect the European economy is an immediate challenge facing dealmakers. While it may lead to more UK-based financial investors looking to diversify their portfolios by investing in CEE, a 'hard Brexit' could potentially slow growth across the continent. It may also lead to new regulatory barriers to investment from British companies, and prove very damaging to the few companies in the region which export large amounts to the UK.

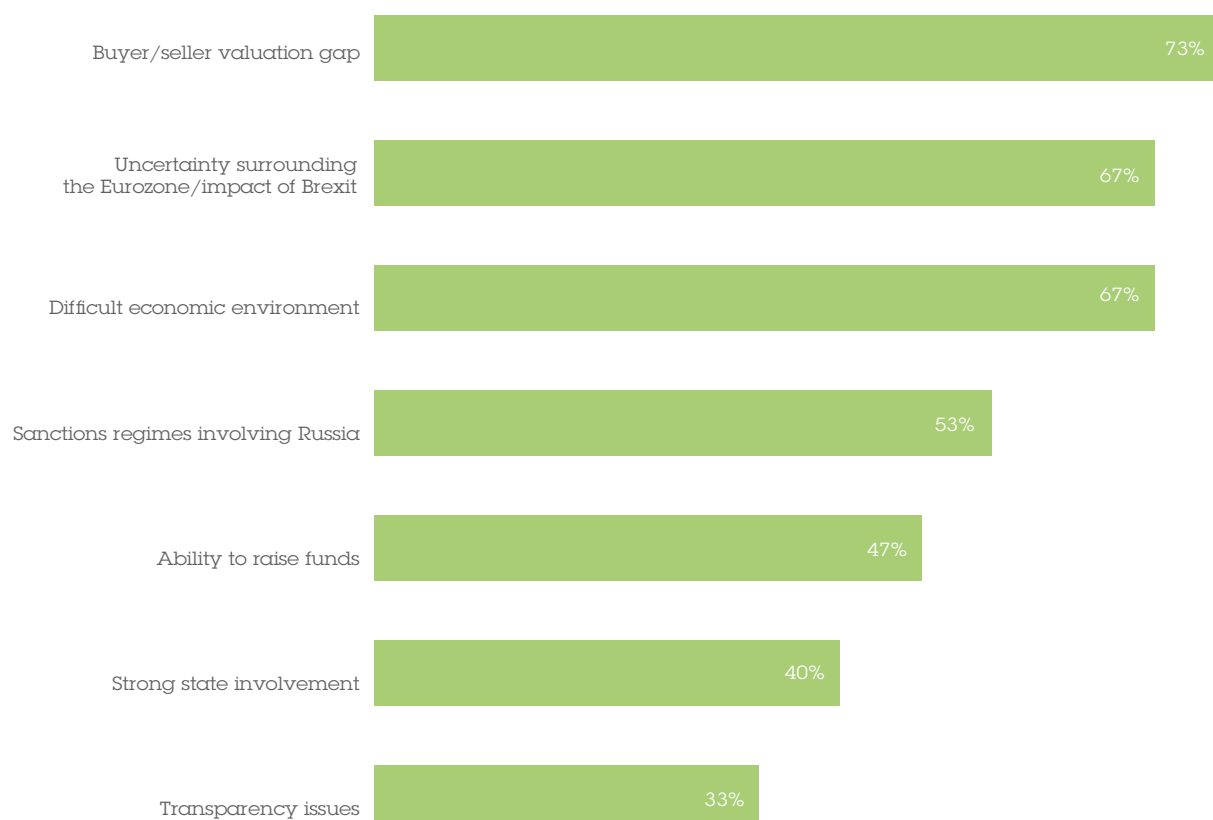
Yet the UK's divorce from the EU could also bring opportunities to the leading financial centres in CEE. "The effect of the aftermath of Brexit, as far as Warsaw is concerned, is the arrival of a number of large, primarily financial institutions," says Przemysław Kozdoj, partner at Wolf Theiss, Warsaw. "Credit Suisse has moved to Warsaw. This year, we know that JP Morgan is moving into Warsaw, and planning to employ over 2,500 people. Other similar institutions are likely to follow."



Which compliance/regulatory processes do you consider to be the most challenging to manage in that country? (Please select all that apply)



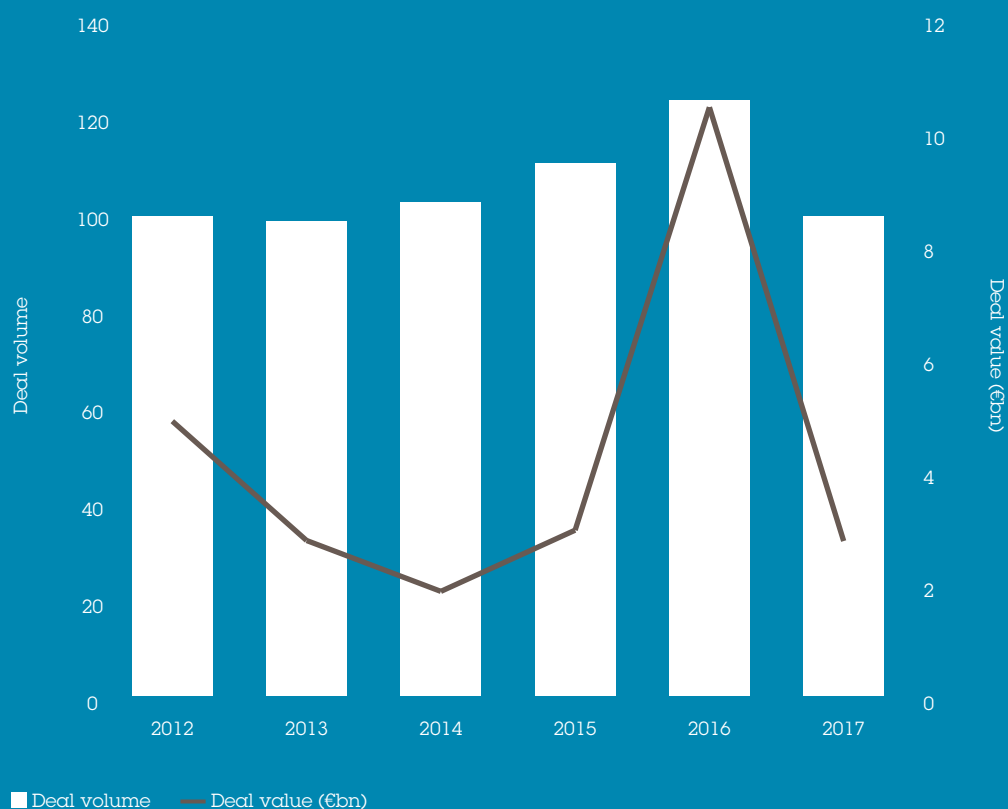
What do you perceive as the biggest challenges to implementing your CEE strategy in general? (Please select all that apply and the most important)



# CONSUMER AND LEISURE

Rising incomes and growing tourism have seen a revival in the consumer and leisure sector within the CEE over the past few years. The growing optimism surrounding dealmaking within the sector is reflected in our survey, with the industry ranking as the second most attractive in the region among respondents.

CONSUMER AND LEISURE M&A, 2012-2017







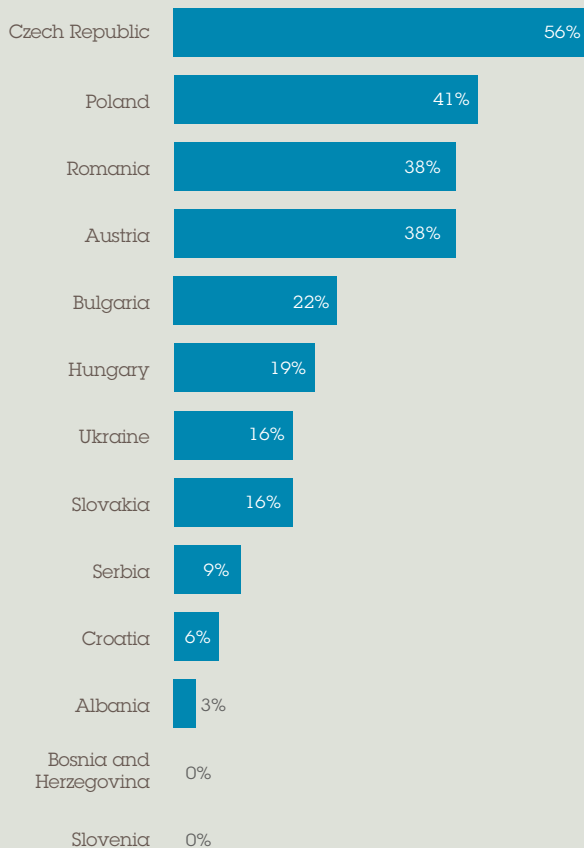


### CZECH MATE

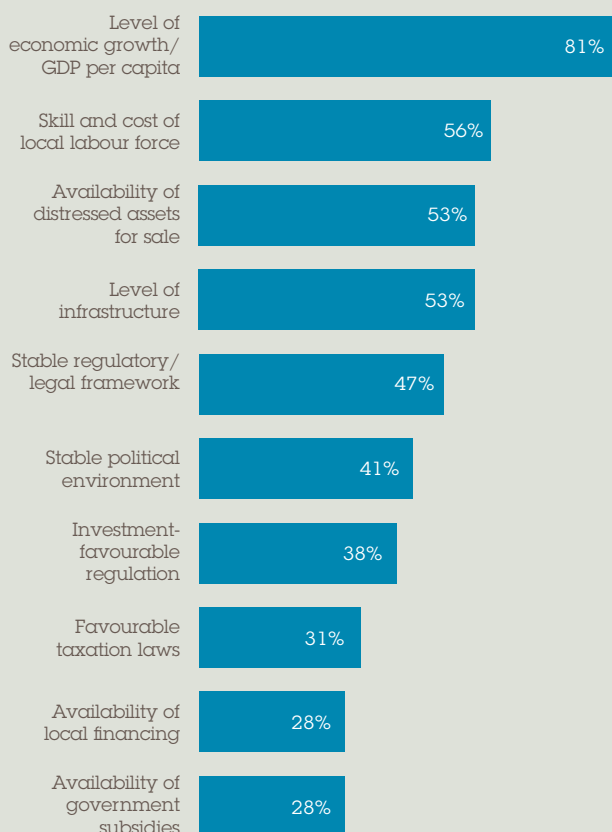
The Czech Republic is seen as a particularly attractive market, with 56% of all investors focused on consumer and leisure eyeing opportunities there. The country has among the highest income per capita in CEE, and clocked up impressive growth of 4%-plus in 2017. This is significant, considering 81% of respondents state that the level of economic growth and GDP per capita is an important factor for selecting a country for a deal. Meanwhile, Prague is one of the region's most popular tourism destinations.

The skill and cost of the local labour force is seen as the second most important factor among respondents (56%). The level of infrastructure development and the availability of distressed assets were each cited as an important factor by 53% of sector-focused respondents. The Czech Republic has excellent infrastructure by regional standards, helping support regional tourism development as well as broader economic growth.

In which country/ies are you currently looking for new opportunities? (Please select all that apply)



What are the factors that will most impact your choice of country for your next deal? (Please select all that apply)



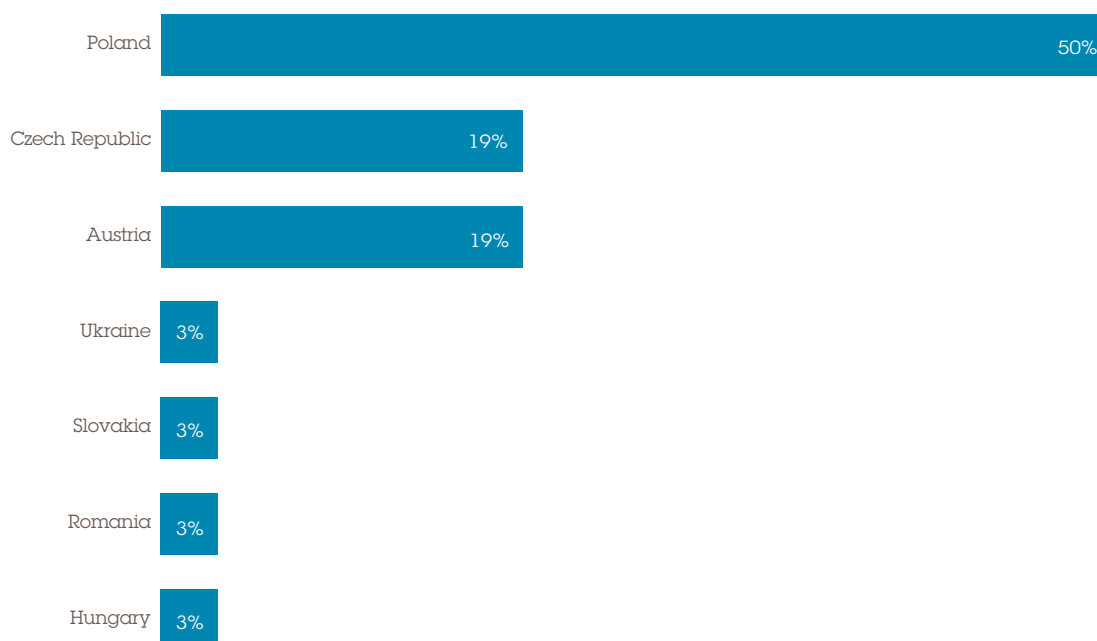
### POLAND PROSPERS

Poland ranks second in our sector survey, with 41% of respondents looking for opportunities in the country, the second most-populous in the region and the largest economy. Growth within the consumer sector has been buoyed by modern retailing developing across the country, while the tourism sector is expected to grow by 6% in 2017, according to the World Tourism and Travel Council.

"The consumer and leisure sector has witnessed rapid growth and also increased the interest of investors," says Jacek Michalski. "In particular, PE houses are looking for new acquisitions, primarily in consumer-related services because of the high returns and rapid growth potential."

Poland is seen as the best gateway for expansion across the region by half of all respondents, followed by the Czech Republic and Austria, both cited by 19%. This is indicative of the strength of Poland's domestic market.

Which country do you consider to be the best gateway for expansion in the CEE region? (Please select only one)



#### SUPERMARKET SWEEP

The Polish consumer sector attracted the €1.3bn acquisition of supermarket company Zabka Polska by CVC Capital Partners from Mid Europa Partners. Joanna Wajdzik, associate at Wolf Theiss, Warsaw, says that the coming years will see more sales of mid-sized family-run businesses in the sector, as entrepreneurs who established their companies in the 1990s look to succession, in some cases with a view to retirement.

Similar transactions are taking place in Ukraine, a market of nearly 45 million people, as some foreign investors withdraw and others look to expand their presence, despite the economic and political difficulties of the past few years.

"Supermarket chains are generating a lot of activity," says Taras Dumych, partner at Wolf Theiss, Kiev. "One such example is the holding company for Billa Supermarkets, Rewe, selling its real estate assets and operations to a Ukrainian group, Varus. We also have Karavan, a Ukrainian operation of supermarkets, selling itself to Auchan, a French retail group."

#### ENTER ROMANIA

Romania ranks third in terms of market appeal, with 38% of sector investors considering targets in the country, the region's third most-populous and one of Europe's fastest-growing economies.

"Growth is projected to be around 5.6% in 2017," says Ileana Glodeanu, partner at Wolf Theiss, Bucharest. "That is tremendous. And this increase in the power to purchase is reflected in consumer finance, where we are seeing a lot of transactions."

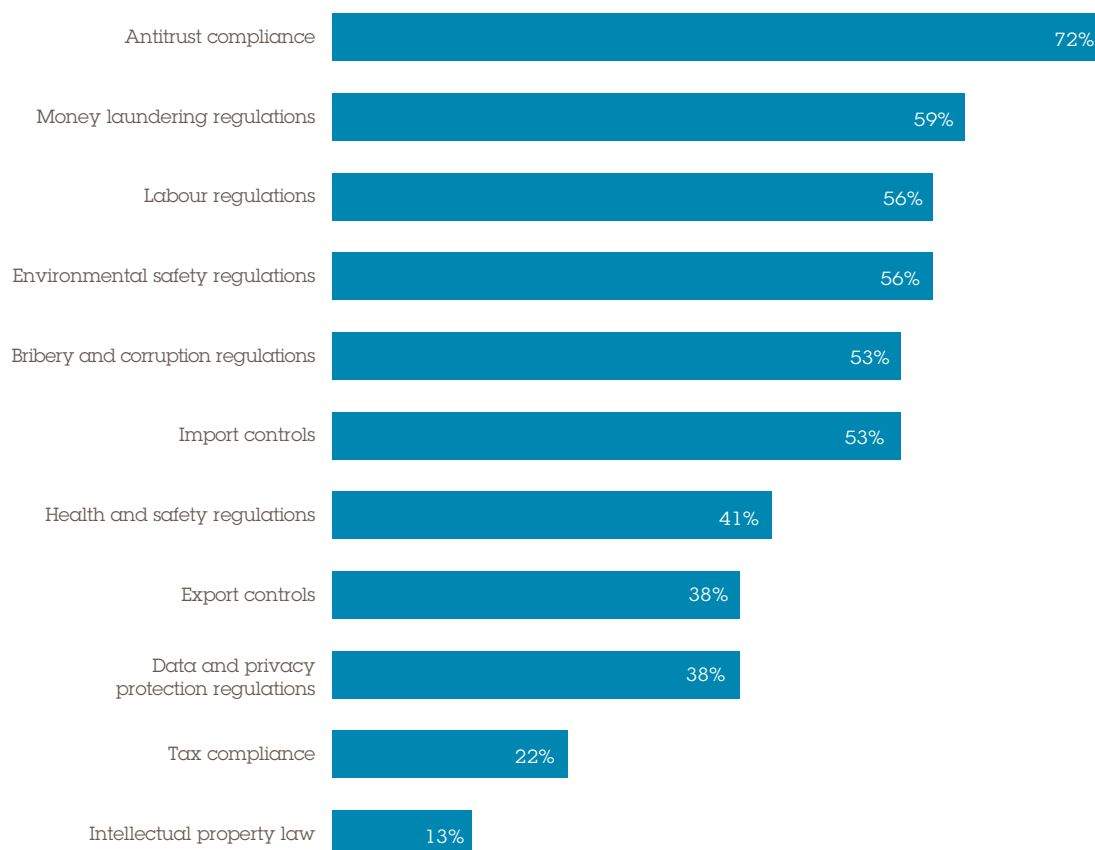
Glodeanu also points to lively activity in the hospitality sector, with international chains opening hotels throughout the country, including a new Radisson in Brasov, and an economic and tourism centre in Transylvania. Romania finally seems to be capitalising on its tourism potential, including its mountains, historic sites, and thermal spas.

#### COMPETITION REACHES BOILING POINT

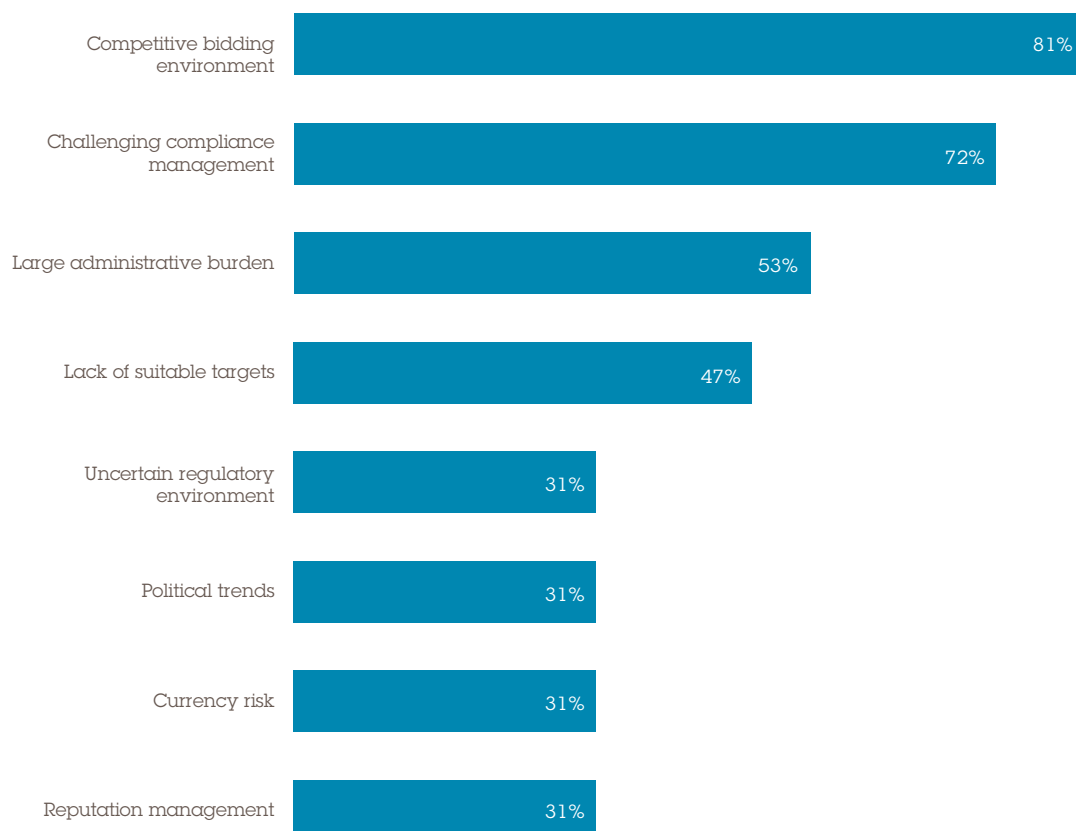
The biggest challenges for sector investors in the markets that they are targeting are the competitive bidding environment (cited by 81% of respondents), challenging compliance management (72%), and a large administrative burden (53%). Antitrust compliance is the biggest regulatory challenge (72%), followed by money laundering regulations (59%), and labour and environmental safety regulations (both 56%).

The competitive bidding environment is particularly acute in the supermarket retail segment, where markets are nearing saturation, and the scope for greenfield entry with new brands is minimal, leading incoming investors to seek established chains to acquire. Antitrust compliance is also a challenge in this segment as regulators seek to avoid the development of oligopolies – and in some cases, raise barriers to entry for foreign entrants.

Which compliance/regulatory processes do you consider to be the most challenging to manage in that country? (Please select all that apply)



What do you perceive as the biggest challenges to investing in your specific country of choice? (Please select all that apply)



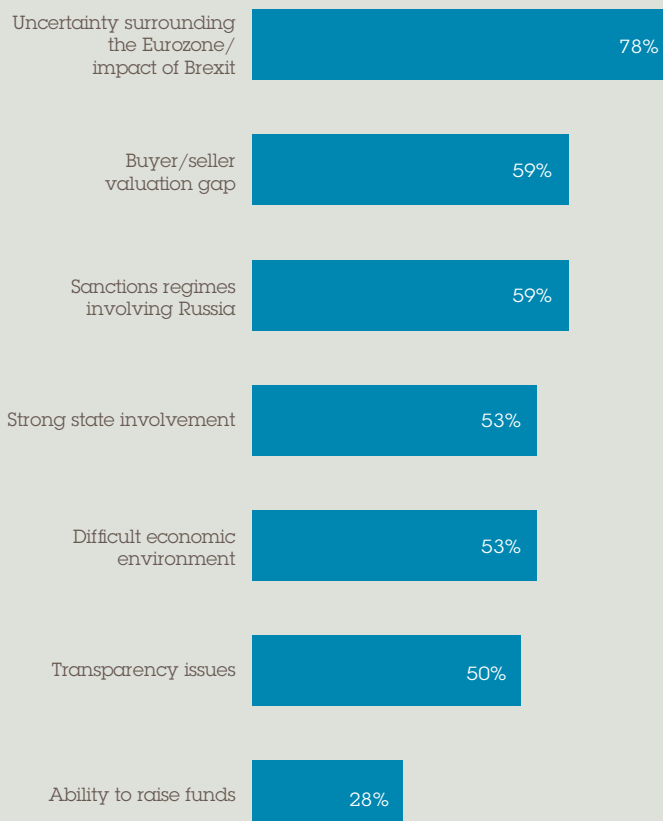


### PLAYING THE GAME

In the profitable and lively but often-overlooked gaming segment, regulation is stringent and varies considerably from jurisdiction to jurisdiction. This has a significant impact on major regional players looking to expand. One such example is the Czech-based Sazka Group, which in August 2017 took its stake in Casinos Austria from 11.3% to around 34%, and announced its intention of taking sole control of the company.

"Regulations may have an impact on who can buy and who can operate casinos in various countries," says Jan Myška, partner at Wolf Theiss, Prague. "When you have a global operation you have to gain local regulatory approvals in all the countries where they are operating. So, acquiring a global casino operation is certainly not easy from a regulatory perspective."

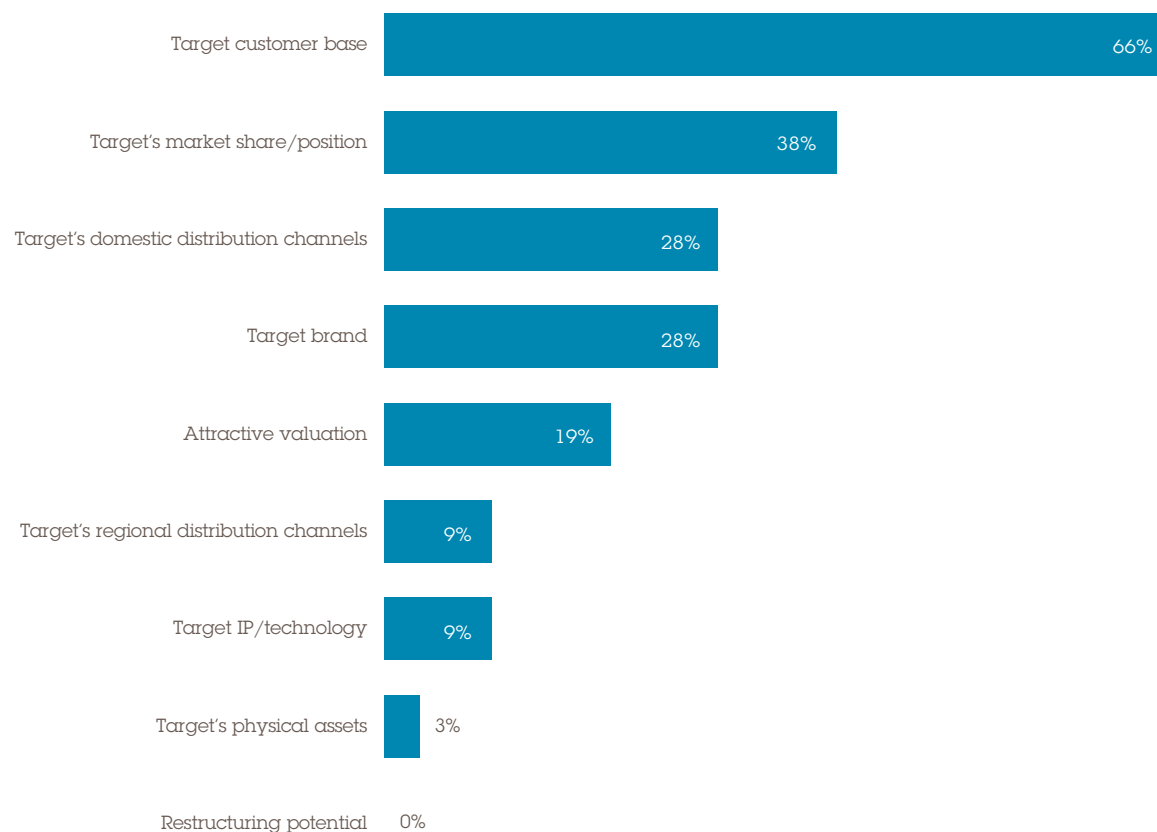
What do you perceive as the biggest challenges to implementing your CEE strategy in general?  
(Please select all that apply)



### LOOKING AHEAD

Uncertainty surrounding the eurozone and the impact of Brexit is seen as the biggest downside risk to investors in consumer and leisure implementing their strategies, raised by 78% of respondents. This is followed by the buyer/seller valuation gap, and sanctions regimes involving Russia (both 59%). Indeed, the impact on sanctions may be one factor that has led to Russian companies pulling out of Ukraine in particular. "For sure eurozone concerns, Brexit and sanctions regimes are very much on investors' minds in this segment, but in the end basic pricing issues often determine whether a particular deal goes forward or not," says Ron Given, partner at Wolf Theiss, Warsaw.

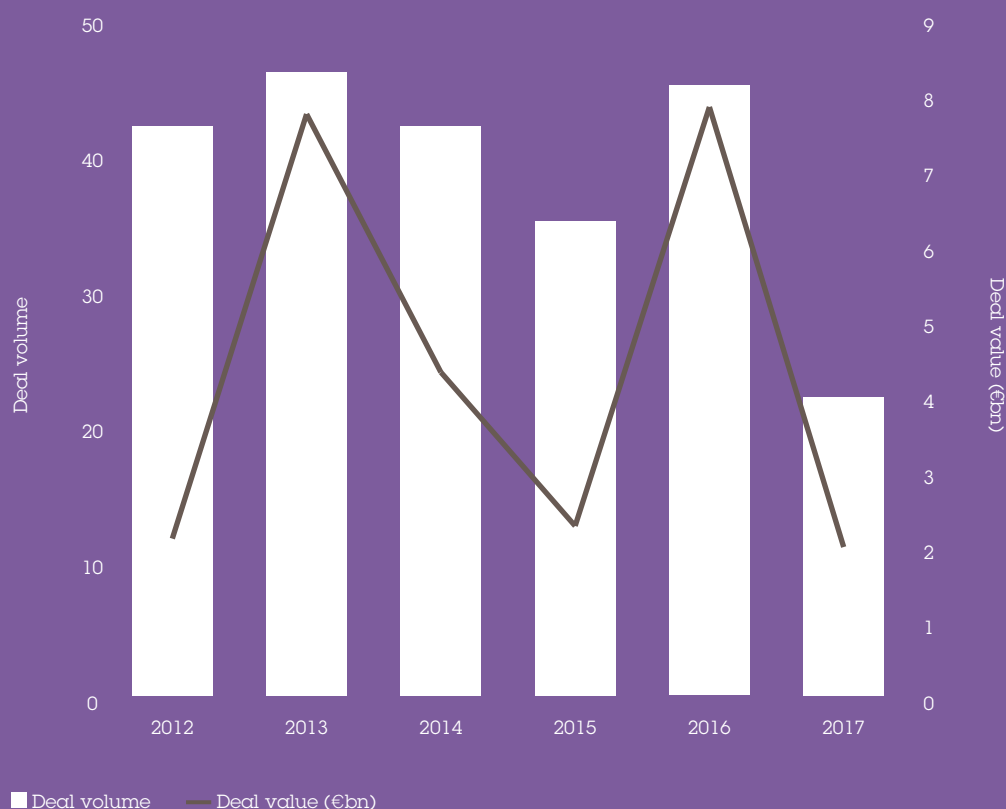
What will be the most important driver for your next acquisition in the CEE region? (Please select the top two)



# ENERGY, MINING AND UTILITIES

The energy, mining, and utilities sector has undergone a challenging period, with low commodity prices, increasing regulation, and government intervention all having an impact on dealmaking. Thus, only 4% of respondents saw it as likely to be the most attractive area for investment in 2018. Nonetheless, opportunities exist. Restructuring of distressed companies will continue, while state-enterprise-led takeovers of some businesses are providing exits for foreign investors and business for dealmakers. Meanwhile, an uptick in oil prices in 2017 bodes better for beleaguered upstream businesses.

ENERGY, MINING AND UTILITIES M&A, 2012-2017







Poland is seen as the most appealing country overall to conduct M&A transactions, with almost half (47%) of investors looking for targets in the coal-rich country which boasts a growing natural gas sector. This was followed by the Czech Republic and Austria (both chosen by 33% of respondents). Some 20% are seeking opportunities in Romania and Croatia, which both have significant offshore oil and gas potential along with part-state-owned companies in the sector in need of investment. Poland is seen as the best gateway to the region (chosen by 40% of investors), followed by Austria (33%), and the Czech Republic (27%).

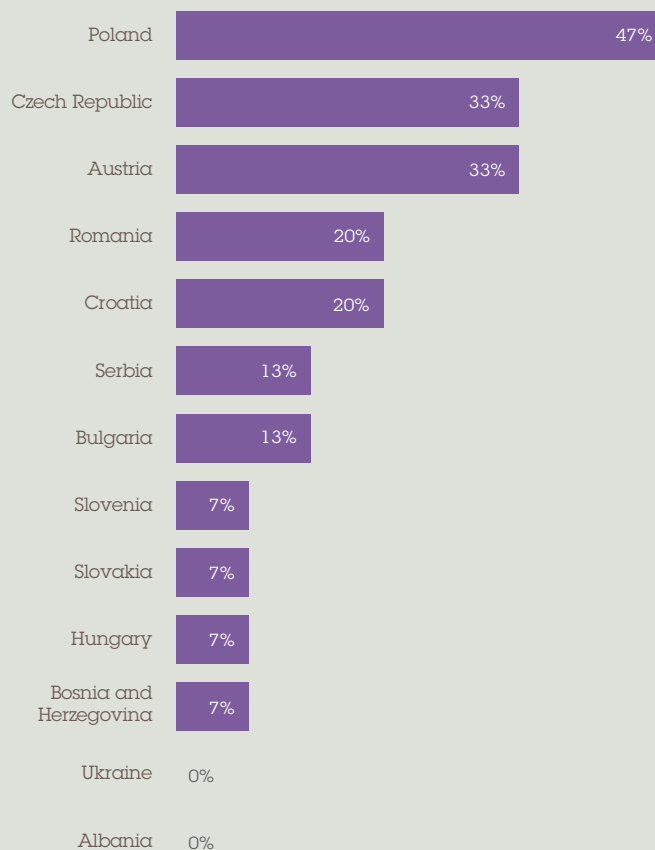
In a heavily regulated sector in which the government has a stake in leading companies in many countries, a stable political environment is the most-important factor determining the choice of investment destination. The level of economic growth or GDP per capita is equally important, however, while the skill and cost of the local labour force and the level of infrastructure were cited by 60% of respondents.

#### RISE IN RENEWABLES

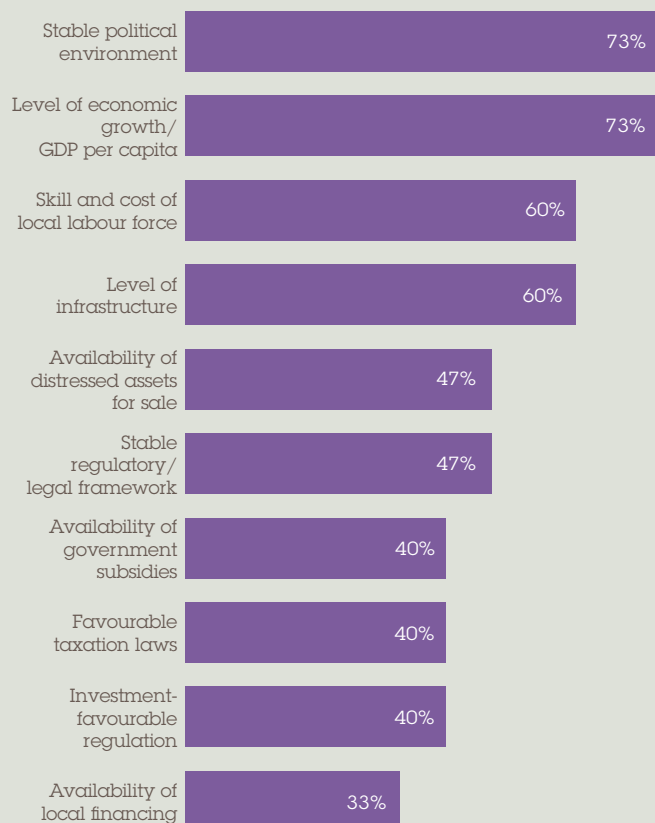
Several countries in the region, including Romania, Bulgaria, Poland, and Croatia, have seen changes in regulation deflate the renewable energy sector in recent years. In Bulgaria's case, retroactive cuts to feed-in-tariffs angered investors in a previously booming sector that had drawn investment from China as well as across Europe. The changes stalled a range of projects and called into question Bulgaria's security as an investment destination. However, legal challenges to the changes and government efforts to tackle much-needed energy reform may now be bearing fruit.

"We are seeing a stabilisation of the framework related to renewable energy investments, due to the litigation undertaken by existing investors," says Katerina Kraeva, partner at Wolf Theiss, Sofia. "And now we are seeing interest from foreign companies acquiring existing projects in wind, solar and biomass."

In which country/ies are you currently looking for new opportunities? (Please select all that apply)

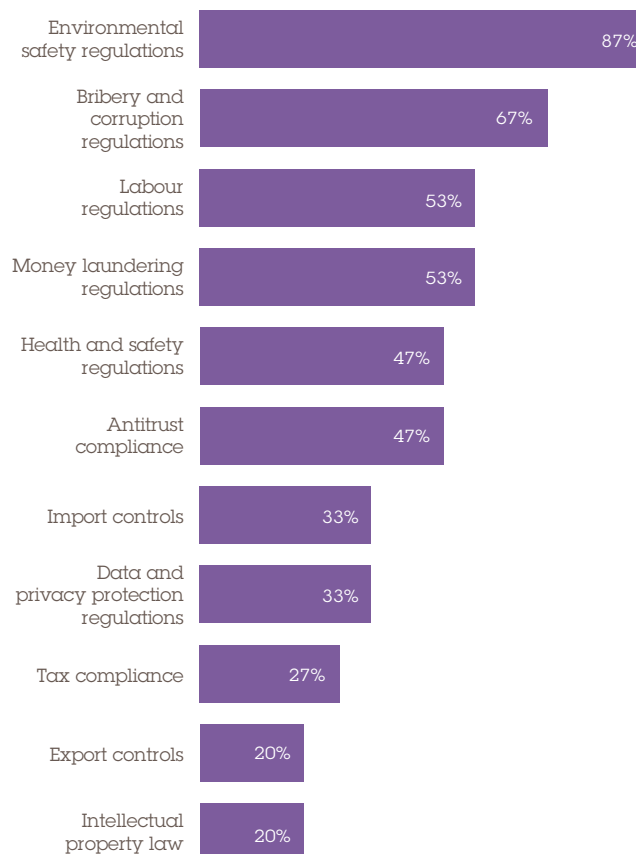


What are the factors that will most impact your choice of country for your next deal? (Please select all that apply)





Which compliance/regulatory processes do you consider to be the most challenging to manage in that country?  
(Please select all that apply)



In Croatia, however, renewables investment remains "at a standstill," according to Sasa Jovicic, counsel at Wolf Theiss, Zagreb, following the failure of successive governments to create sustainable incentives. Meanwhile, in Poland, changes to the green certificate regime among other legislation governing renewables has caused serious problems for companies in the wind power industry in particular, with knock-on effects for banks which had lent to them.

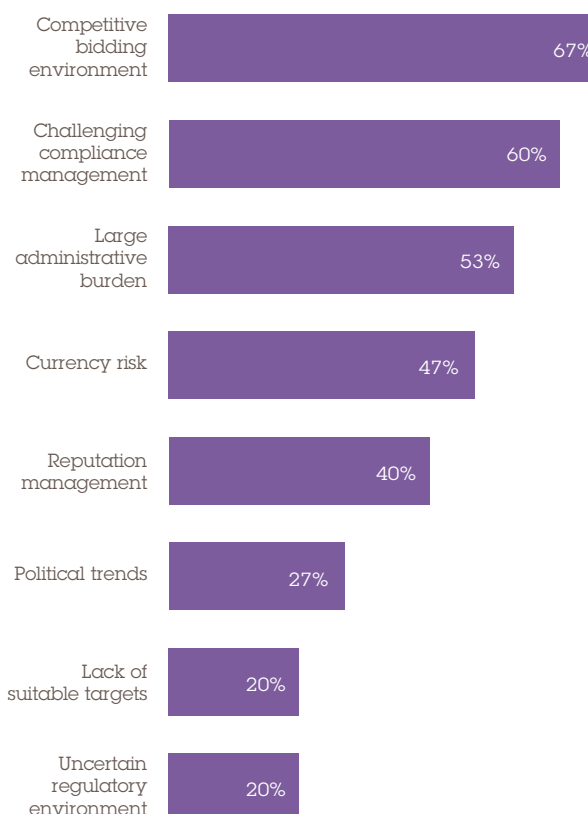
#### OBSTACLES REMAIN

The competitive bidding environment is the biggest challenge perceived by investors in their target countries (raised by 67% of those surveyed), followed by compliance management (60%), and the large administrative burden (53%) in this heavily regulated sector.

Environmental safety regulations are the biggest compliance challenge in the sector, cited by 87% of respondents as an issue; the Paris climate agreement is expected to increase costs for fossil fuel-related industries. Bribery and corruption regulations are the second-biggest challenge (67%), again indicating the important role of government in the sector in licensing and public contracting. "Although environmental and corruption issues are indeed a concern in this sector, with a transaction that is otherwise on target, the parties usually find a way to get comfortable with the issues with thorough due diligence and strong contractual protections," notes Zoltan Faludi, partner Wolf Theiss, Budapest.

The biggest downside risk to implementing investment strategies in the region is uncertainty around Brexit and the Eurozone (cited by 93% of respondents), the difficult economic environment (60%), and the buyer/seller valuation gap (53%). The rise in oil prices above \$50 a barrel in 2017 should ease some economic pressures on hydrocarbons-focused businesses, though commodities prices as a whole seem unlikely to soar to the levels seen earlier in the decade.

What do you perceive as the biggest challenges to investing in your specific country of choice?  
(Please select all that apply)



## UTILITIES ON THE UP

Changes in sector dynamics are leading players to develop new business lines and restructure shareholding structures, a trend that looks set to continue.

"Utilities, especially energy utilities, are the hot topic in the Czech Republic," says Jan Kotous, counsel at Wolf Theiss, Prague. "One such example is CEZ ESCO, which has been targeting utilities in the energy sector in an attempt to break into non-core services such as co-generation."

Jan Myška, partner at Wolf Theiss, Prague, adds that consolidation is underway as bigger players acquire smaller competitors, while financial investors are showing increasing interest in stakes in cash-generating utilities, a model seen elsewhere in CEE.

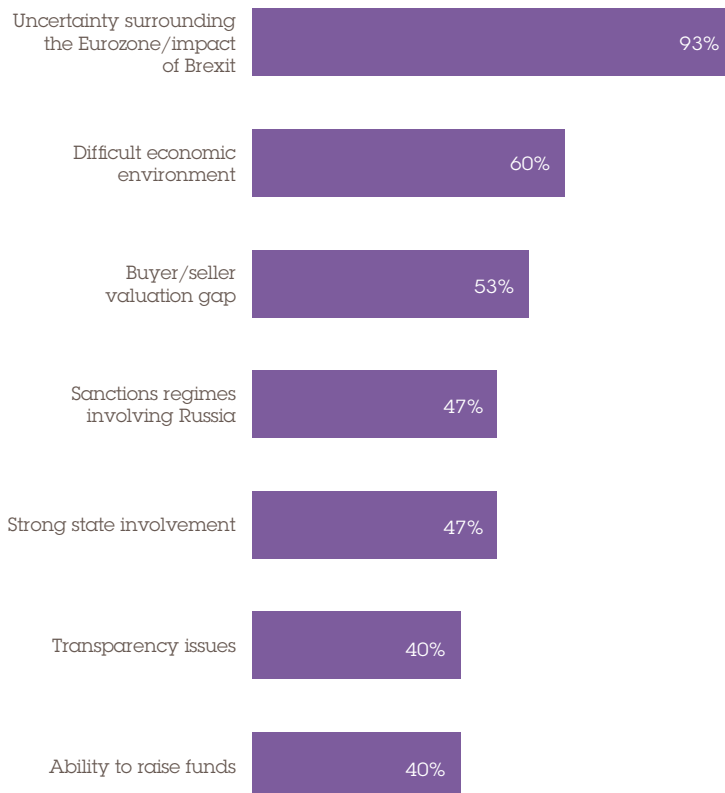
"An interesting trend is that regional utilities are increasingly looking to bring in minority shareholders, so that the municipalities that own the utilities can deleverage," says Horst Ebhardt, partner at Wolf Theiss, Vienna. "This is very interesting for infrastructure funds that like to go into more passive investment structures by taking around 25% of total capital with limited minority rights. That way they participate in the relatively steady income streams that utilities provide."

## BALKAN PROMISE

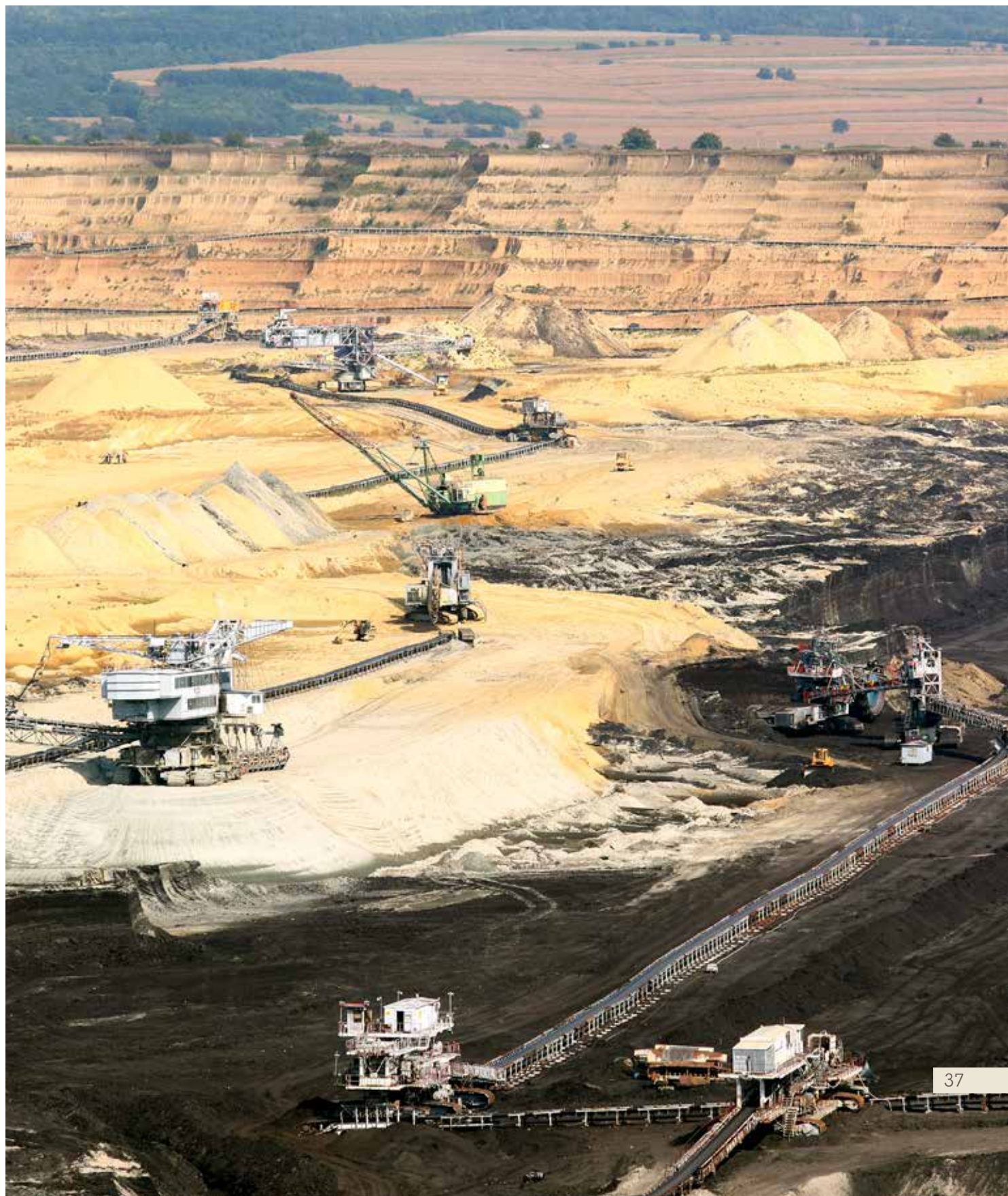
In the Western Balkans, activity is also picking up. Nikolaus Paul, partner at Wolf Theiss, Sarajevo, points out that the country has seen increasing investments in major energy projects from foreign players, including Chinese companies. This has included boosting capacity at existing coal-fired plants, and developing hydroelectric capacity, though licensing issues have held back the development of other promising renewable sources. With respect to those licensing issues, Naida Custovic, also partner at Wolf Theiss, Sarajevo, adds: "There is significant international pressure on the government to deal with a number of regulatory roadblocks and we may see a reaction in 2018, hopefully for the better."

Meanwhile, opportunities may arise from wide-ranging reform in Albania, which has attracted investment in both upstream oil and hydroelectricity in particular in recent years. "We have seen recent legislative development regarding renewables, and the government is heavily involved in imposing rules regarding the market model that requires a huge revamping of current major players, which, of course, are state-owned," says Sokol Nako, partner at Wolf Theiss, Tirana. However, Nako adds that "much will depend on the market rules, because only after a market model is set will there be the stability to allow investors to make an informed decision about entering the Albanian market."

What do you perceive as the biggest challenges to implementing your CEE strategy in general?  
(Please select all that apply and the most important)









# INDUSTRIALS AND CHEMICALS

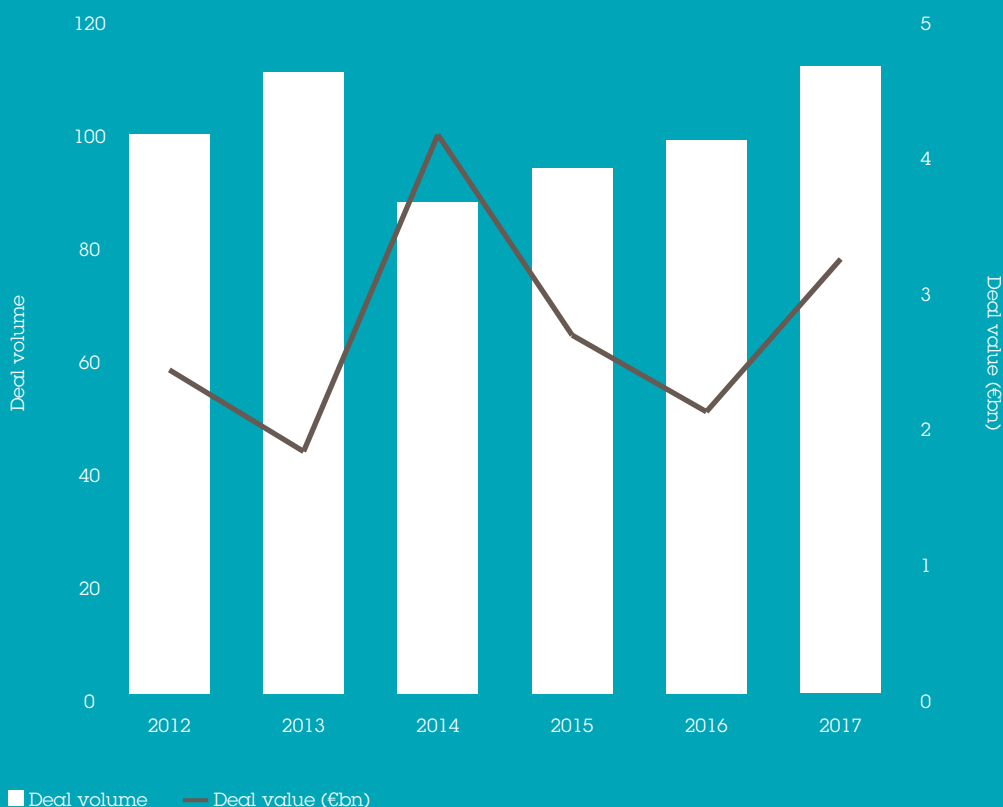
Central and Eastern Europe's combination of location, low costs, and a skilled labour market have made it a locus for industrial investment for several decades. Legacy industries from the communist era including automotive manufacturing and petrochemicals have, in a number of cases, been overhauled and expanded since the transition began in the late 1980s.

Reflecting this tradition of activity, the sector attracted some significant deals in 2017. These included the €582m acquisition of a 37.45% stake in Poland's Synthos SA by businessman Michal Solowow's investment vehicle FTF

Galleon, which already had a controlling stake in the company. Meanwhile, Polski Koncern Naftowy Orlen acquired a 37% stake in Czech firm Unipetrol for €997m.

Other notable deals consisted of investment company R2G Rohan Czech's acquisition of an 89% stake in Czech textile manufacturer Pegas Nonwovens for €270m, and the €250m takeover of German chemical company SGL Carbon, which has substantial operations in Poland, by Jersey-based PE fund Triton Partners.

## INDUSTRIALS AND CHEMICALS M&A, 2012-2017









### AUTOMOTIVE DEALS DRIVE ACTIVITY

The Czech Republic, home to a range of sophisticated industries, is the most popular destination for investors seeking new opportunities in the sector, with 56% of respondents looking for targets in the country. "The automotive and manufacturing industry is crucial to our economy, with a significant part of the population employed within this sector," says Jan Kotous, counsel at Wolf Theiss, Prague. "We are seeing a lot of M&A activity in this space."

International automotive companies present in the country include Volkswagen, which owns Skoda Auto, once part of Czech national manufacturing champion Skoda Works, as well as Toyota and Hyundai. An "automotive cluster" of components suppliers has grown up around these businesses, developing into part of the global automotive supply chain.

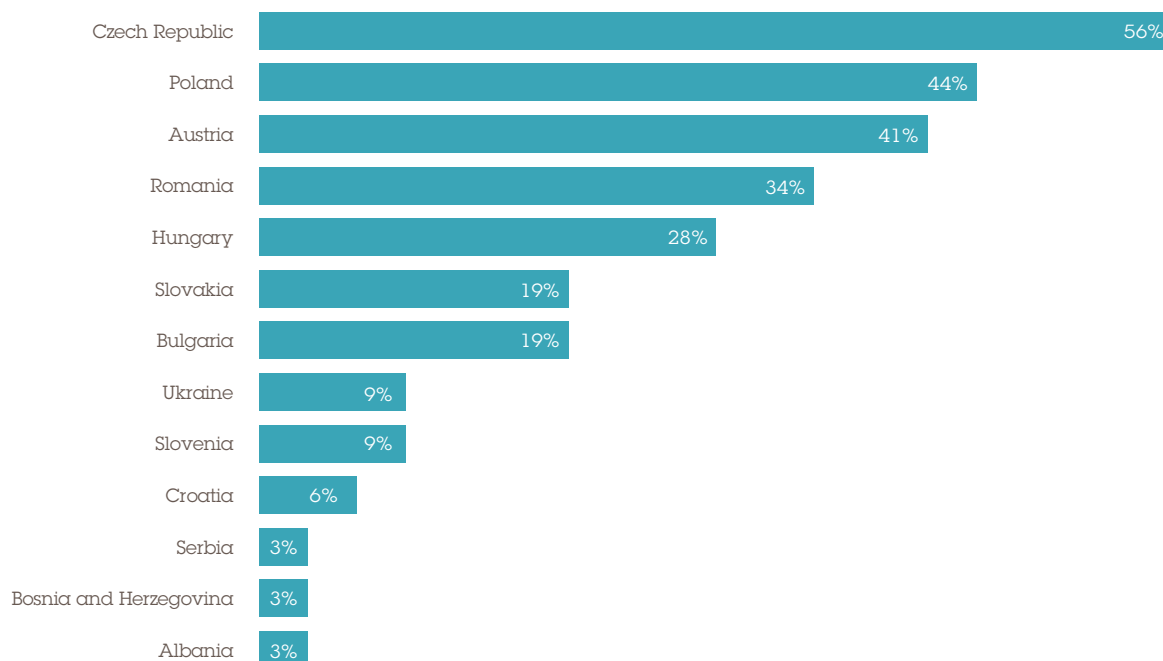
Poland, which ranks second after the Czech Republic, has also developed a strong vehicle and component manufacturing industry that has benefitted from EU membership

and proximity to Germany. Poland is one of Europe's leading steel producers, with output dominated by Luxembourg-based, London-listed ArcelorMittal.

Generally, the view across the region is that this is an area of traditional strength and is continuing to develop steadily. Richard Clegg, partner at Wolf Theiss in Sofia, says that "the industrial manufacturing sector isn't sexy but it certainly provides steady work". Bulgaria-based manufacturers continue to benefit from "incredibly competitive" production costs, he adds.

While 2017 saw the likely end of the Bulgarian joint venture between Chinese automaker Great Wall with a local investor thanks to bankruptcy, Chinese interest elsewhere in the region continues to grow. In April 2017, Hong Kong-based PE fund AGIC Capital acquired Slovenian medical laser company Fotona, with a view to developing its exports to the Chinese market. The '16+1' China-CEE summit in November 2017 is likely to increase the momentum behind Chinese investment in the region.

In which country/ies are you currently looking for new opportunities?  
(Please select all that apply)



### AUSTRIA REMAINS ATTRACTIVE

The most important factor for investors in the industrials and chemicals sector is the level of economic growth and GDP per head, cited by 63% of sector respondents, one reason that Austria – a relatively expensive country by CEE standards – ranks as the third most attractive country for investment in the region.

Indeed, 41% of respondents are currently seeking investments in the country, leveraging its high skills base and location. Ebhardt points to success stories including Chinese-owned aeroplane component manufacturer FACC, which debuted on the Vienna Stock Exchange in 2014. He further noted, "Although we used to see more talk than action, there is no doubt that the Chinese are now becoming important and established M&A players in the Austrian market."

### AGRICULTURE PROVIDES OPPORTUNITIES

Activity in Ukraine has been picking up, with local investors increasingly active. In February, the authorities cleared the acquisition of Karpatneftekhim, the country's largest petrochemicals plant located at Kalush in western Ukraine from Russia's Lukoil. Investors continue to eye the planned privatisation of the Odessa Port Plant, one of Europe's largest fertiliser producers.

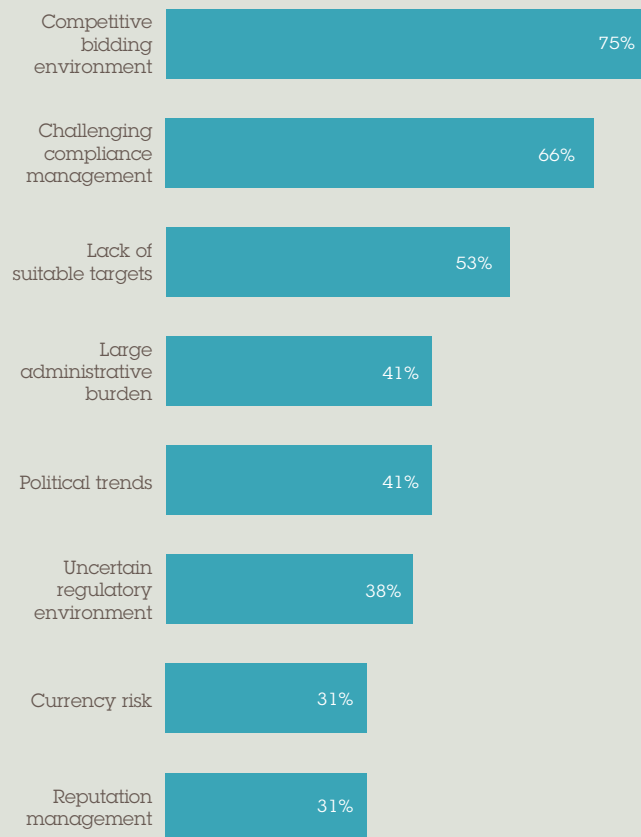
"Ukrainian agricultural companies are the largest in Europe, and some of the largest in the world by their arable land holding," says Taras Dumych, partner at Wolf Theiss, Kiev. "Some of them are among the largest exporters – companies such as Kerne, Astarta or MHP. These companies are continuing their growth, and Kernel made two major acquisitions this year, while Astarta has been benefiting from the Canadian financial group Fairfax increasing its shareholding in the company."

### ROADBLOCKS AHEAD

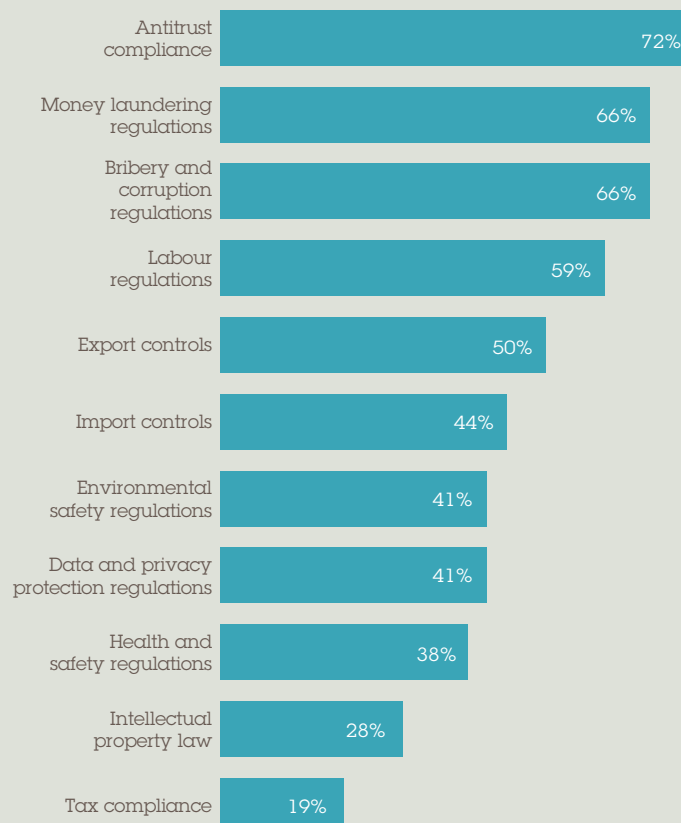
As in several other sectors, the competitive bidding environment is seen as the biggest challenge to investment in respondents' country of choice (highlighted by 75%), followed by challenging compliance management (66%), and lack of suitable targets (53%).

Digging deeper into the compliance challenges cited by many investors, antitrust rules are seen as the most challenging (72%), followed by

What do you perceive as the biggest challenges to investing in your specific country of choice?  
(Please select all that apply)



Which compliance/regulatory processes do you consider to be the most challenging to manage in that country?  
(Please select all that apply)



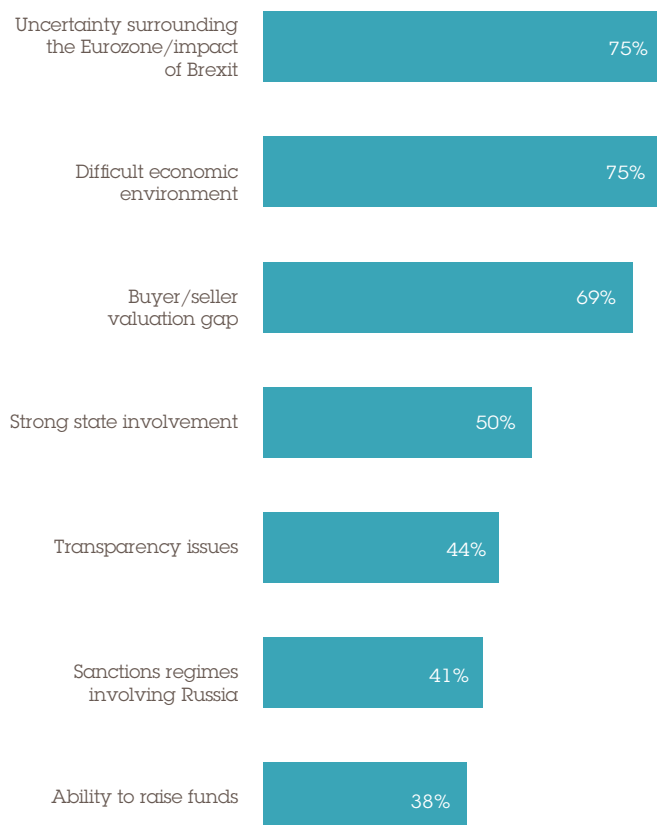
money laundering regulations, and bribery and corruption regulations (66%). Regulations around factory construction and operation make industrials more vulnerable to corruption than some other sectors, an issue that still arises in some of the less-developed countries in the region.

Even in EU member Slovakia, one of the reform champions of the past decade and a half and a success story for industrial investment from automotives to steel, there is room for improvement on business legislation and legal certainty. "Gradual steps are being taken in order to improve the business environment in Slovakia. However, there is still a way to go before foreign investors completely trust the Slovak legal system," says Katarina Bielikova, partner at Wolf Theiss, Bratislava.

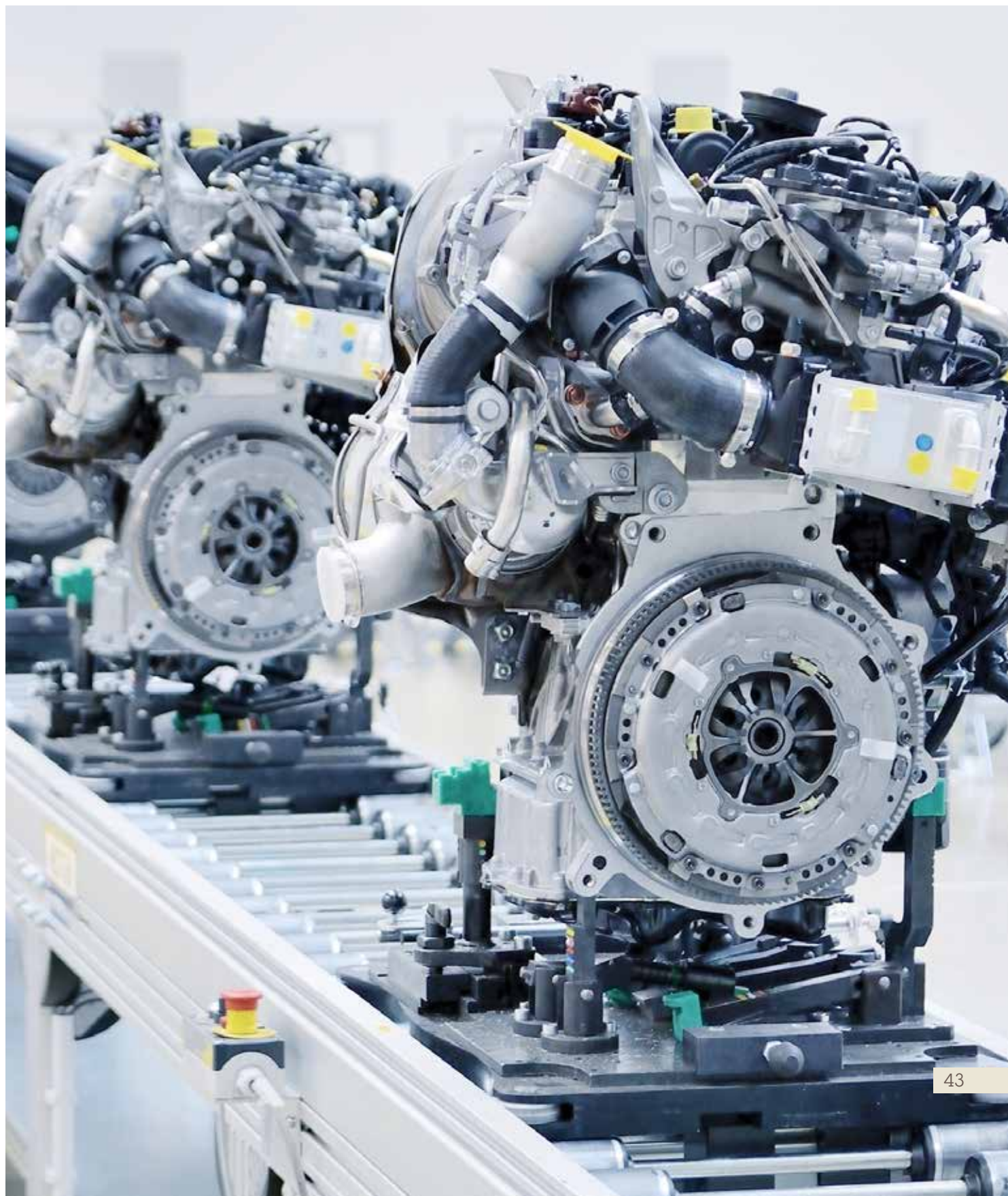
Looking ahead, investors see uncertainty around the eurozone and Brexit, and the difficult economic environment, as the biggest challenges facing the sector, with three-quarters of those surveyed highlighting these related issues. The likelihood that the UK will leave the European single market and customs union, as well as the depreciation of the pound, are likely to make exporting to Britain more difficult once Brexit is completed.

Investors are also aware of the potential vulnerabilities inherent in the global economy. Interest rates are set to rise in the medium term, which could have an impact on heavily leveraged industrials. The moderate recovery in oil prices may also raise costs both for producers and consumers, reversing the lift given to the energy-importing economies of CEE by the 2015-2016 price drop. "Firm-wide, our clients seem to be generally presuming both interest rate and oil price increases but believe the improvement they have made to their balance sheets post-crisis will help weather them," says Luka Tadic-Colic, partner at Wolf Theiss, Zagreb.

What do you perceive as the biggest challenges to implementing your CEE strategy in general?  
(Please select all that apply)



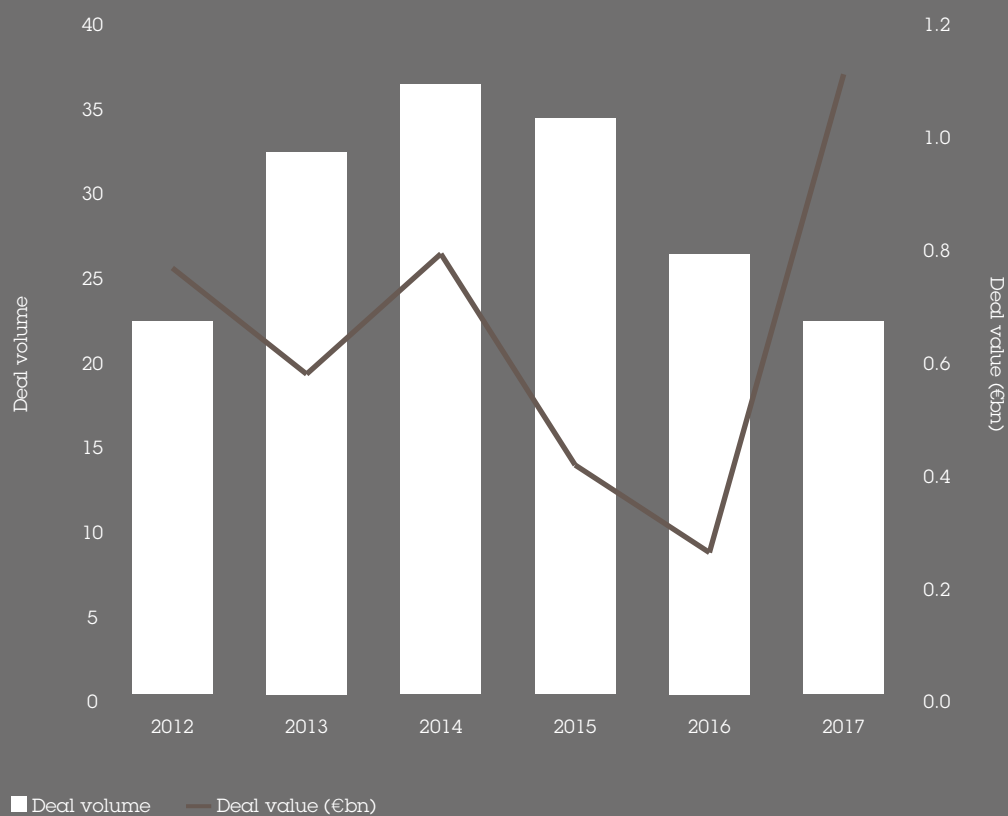




# PHARMA, MEDICAL AND BIOTECH

The pharma, medical and biotechnology sector is seen as one of the most promising for CEE over the coming year, with 32% of all respondents saying that it would be one of the top two industries for dealmaking. Aging populations are driving demand, while a number of local producers across the region are showing promise, benefiting from a pool of highly educated graduates and access to EU markets.

PHARMA, MEDICAL AND BIOTECH M&A, 2012-2017







The Czech Republic is seen as the most attractive market for investors specialising in the pharma, medical and biotech industries, with 57% of respondents saying that they were seeking opportunities in the country. Its strengths include a relatively high income per head, political stability, EU membership, and strong infrastructure. Activity in the sector has been driven in part by cash-rich businesses looking to diversify their portfolios and tap into new sources of growth.

"Pharma, medical and biotech is a hot sector," says Jan Myška, partner at Wolf Theiss, Prague. "Financial groups are making acquisitions quite frequently. Almost any company operating in the sector can be targeted."

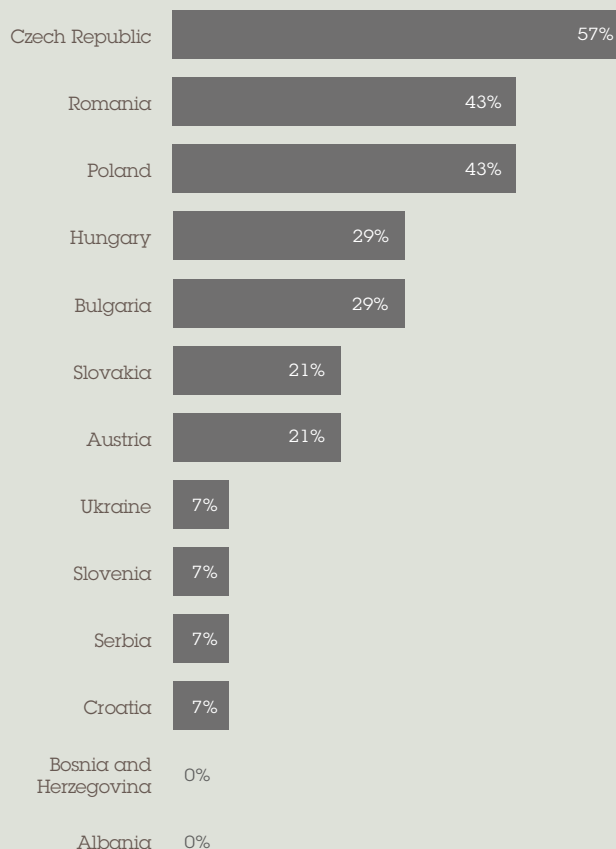
#### SEEKING SCALE

Some 43% of sector investors are seeking opportunities in Poland, and the same proportion in Romania. Both are sizeable markets that have achieved strong economic growth in recent years, with spending power boosted further by government action to raise incomes. Poland is also rated as the best gateway for expansion in CEE by 36% of respondents, followed by the Czech Republic (29%), and Romania (21%).

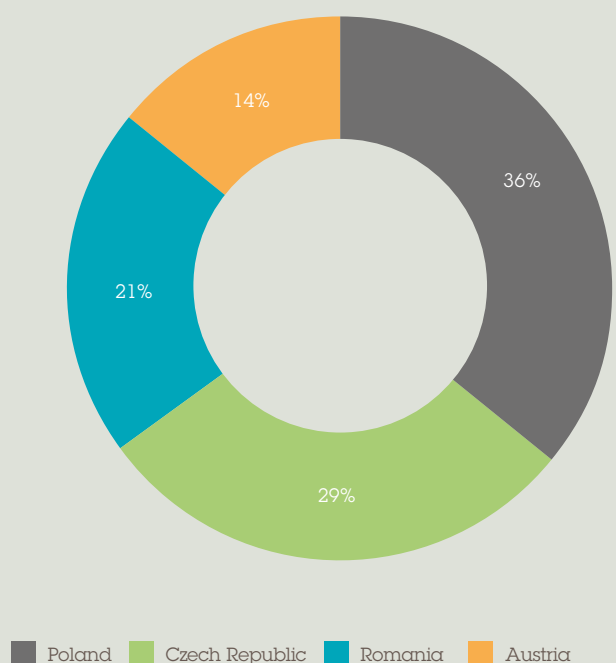
"There are a few privately owned pharma companies in Poland or biotech companies that are developing very fast," says Joanna Wajdzik, associate at Wolf Theiss, Warsaw. "There are also a number of smaller companies which are not only developing very quickly in the local market, but are expanding internationally."

Rules governing the establishment and operation of pharmacies in Poland have historically been restrictive, though were liberalised over the past two decades. New legislation introduced in June 2017 tightened regulation again, making opening new pharmacies considerably more difficult, and putting an emphasis on healthcare rather than retailing. The new rules are expected to lead sales of existing chains, given the curbs on expansion.

In which country/ies are you currently looking for new opportunities? (Please select all that apply)



Which country do you consider to be the best gateway for expansion in the CEE region? (Please select only one)





## BIOTECH BOOM

In Romania, the pharmacy market is more dynamic, with reports that several of the big chains are being assessed by investors, and consolidation likely in the coming years, says Ileana Glodenau, partner at Wolf Theiss, Bucharest.

"The pharma, medical and biotech sector has been extremely active," she adds. "There are a lot of biotech deals – small in terms of value, but quite important nonetheless. There doesn't seem to be a month that passes without us being involved in some global deal in the biotech sector. We expect a lot more investment and consolidation."

The main driver for M&A in the sector in Romania is the low-cost but highly skilled local labour force, including biotech engineers. Challenges come from the regulatory regime, particularly in pricing of generics, with the government keen to rein in prices to shield consumers. However, this has affected the availability of some drugs in Romania, as pharma companies have concerns that pricing in other markets could be affected by offering discounted drugs in Romania.

Hungary ranked fourth – equal with Bulgaria – for sector investors considering their next acquisition, with 29% of respondents looking at options in the country. Government intervention in a range of sectors has led to a degree of uncertainty about long-term investment

prospects in Hungary. This poses a particular challenge for an industry which is both politically sensitive and requires long lead-times for development. But, in this sector, state action may in fact help strengthen the investment case.

"Biotech is an area which is being actively incentivised by the Hungarian government," says Laszlo Kenyeres, partner at Wolf Theiss, Budapest. "There's a governmental scheme running in order to bring Hungary up to speed in terms of biotech capability. As such, this is an area with healthy biotech prospects."

The pharma, medical and biotech sector has traditionally been a mainstay of the Slovak economy, and continues to offer potential for investors. "Slovakia has become an increasingly attractive investment destination for single-use medical equipment production as well as the large-scale production of drugs, says Katarina Bielikova, counsel at Wolf Theiss, Bratislava. The Slovak sector benefits from the country's relatively low costs, a highly productive industry labour force and EU membership. Biomedicine and biotechnology are priorities for Slovakia's three-pronged R&D development strategy. The most notable transaction was the €370m acquisition by Swiss-based Unilabs of laboratory diagnostics company Alpha Medical and its brand Aeskulab from Mid Europa Partners in a deal that will have an impact on markets across Central Europe.





#### MITIGATING RISKS

Concerns about political and regulatory risk in this heavily regulated sector are reflected in our survey.

Region-wide, sector investors say that a stable regulatory and legal framework is the most important factor influencing their choice of jurisdiction for their next deal (cited by 79% of respondents), followed by economic growth and GDP per capita (71%), and favourable regulation (64%). The biggest individual regulatory challenges are environmental safety regulations and antitrust compliance (71%).

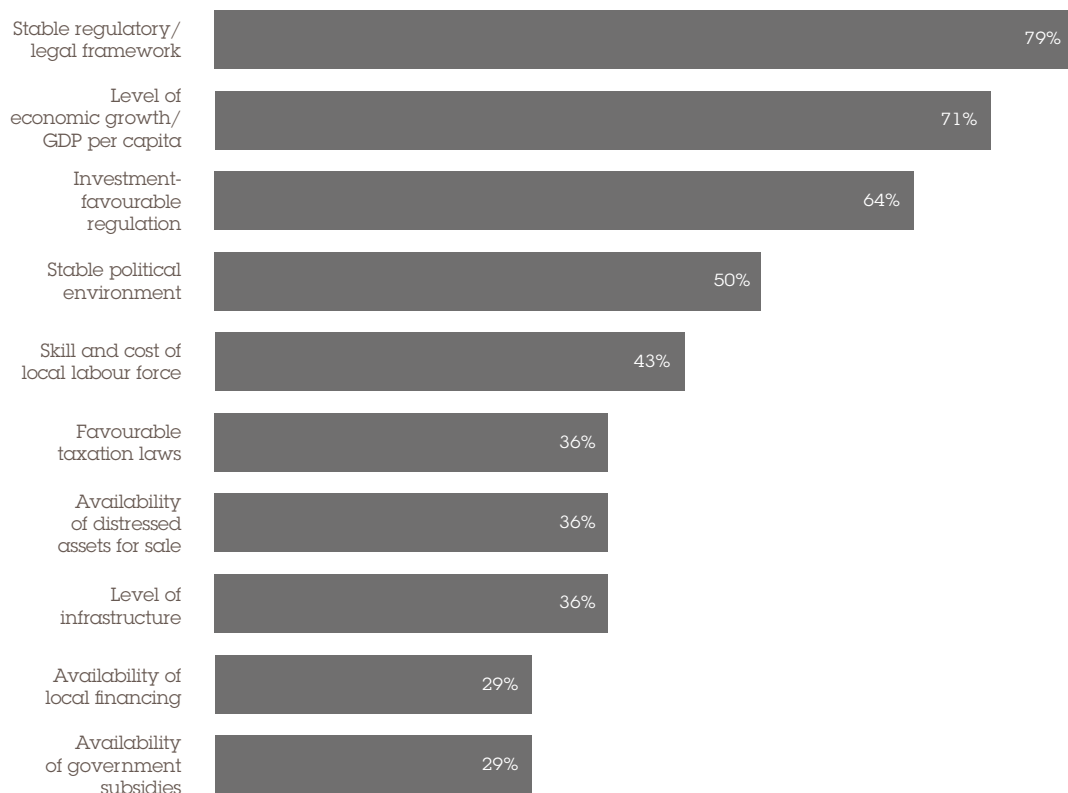
Compliance management and the administrative burden are cited as among the biggest challenges to investing in the respondents' CEE target markets. However,

the competitive bidding environment is the biggest challenge and a related lack of suitable targets (64%) is also a barrier to investment.

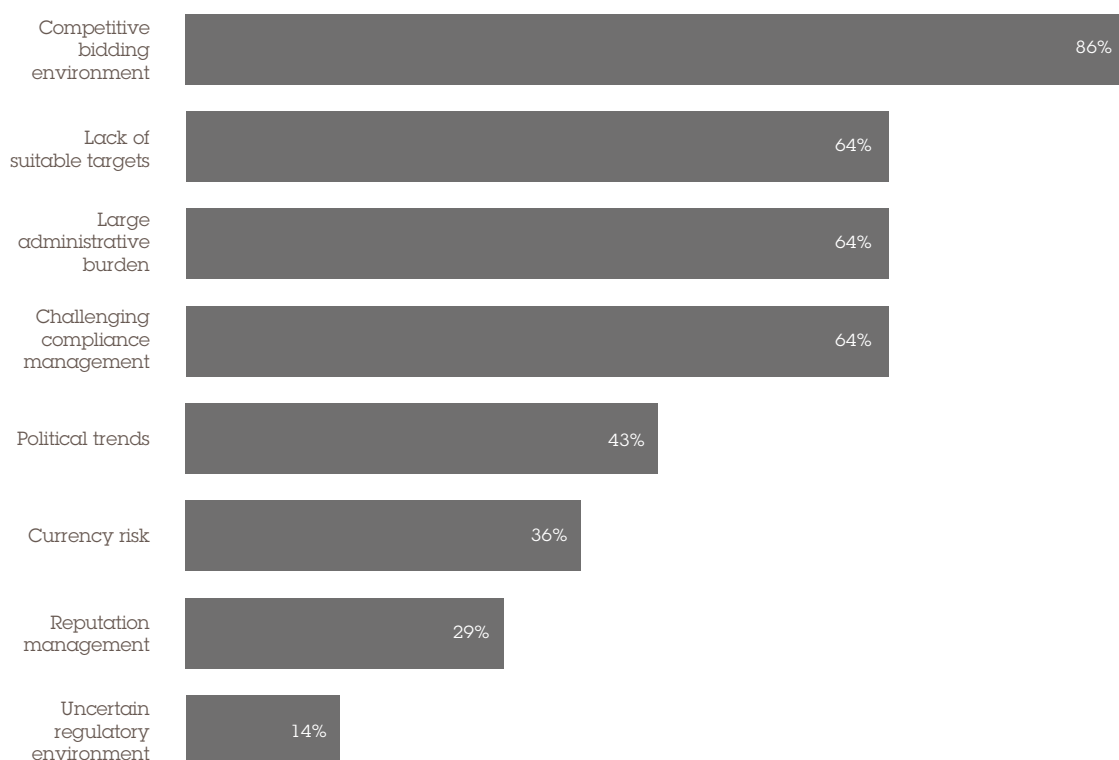
"Our business requires people with a skill level that is not readily available, and it is difficult for us to find suitable targets," says the CFO of an Austrian corporate in the sector, which has most recently made an acquisition in the Czech Republic. "It's very rare to find businesses similar to ours that are also considering a shift in ownership."



What are the factors that will most impact your choice of country for your next deal? (Please select all that apply)



What do you perceive as the biggest challenges to investing in your specific country of choice? (Please select all that apply)

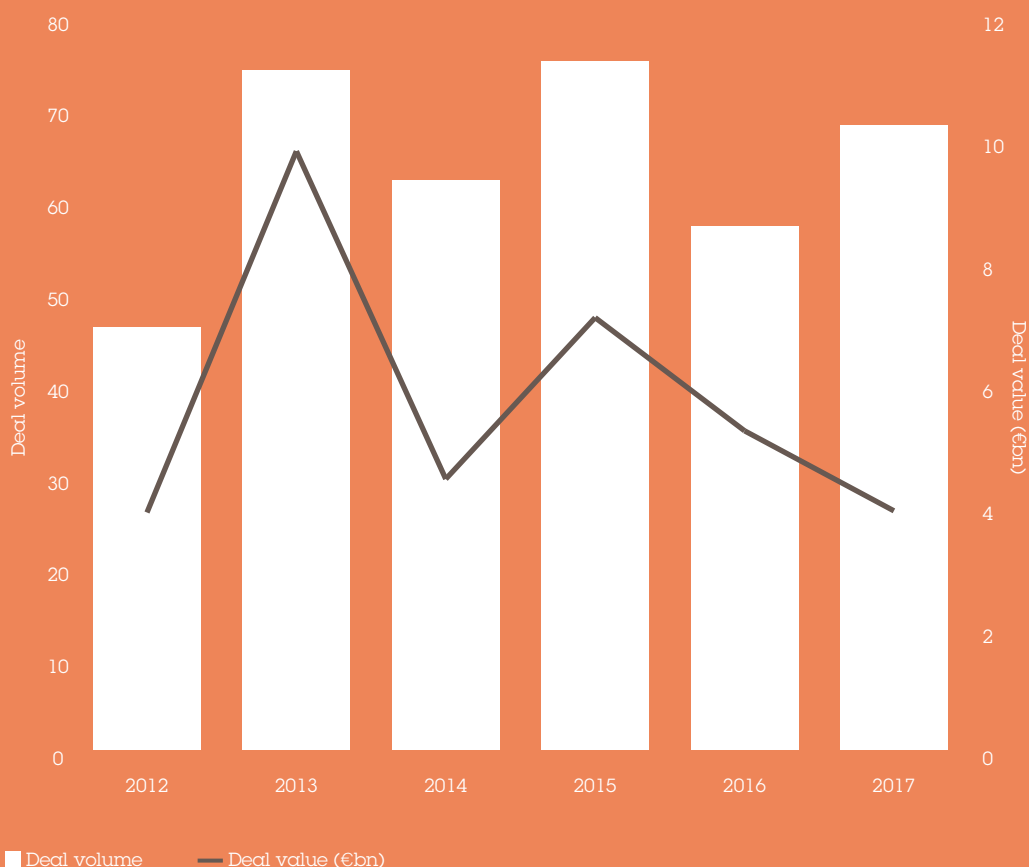


# TECH, MEDIA AND TELECOMS

The tech, media and telecoms (TMT) sector has been one of the liveliest in CEE for several years, with budding start-ups, legacy telcos, and major media owners at the centre of dealmaking. The tech start-up scene will continue to be lively in 2018, largely unencumbered by the political and regulatory risk that affects some other sectors. A strong tradition of technical education, low overheads, access to EU financing, and proximity to major markets are all strong competitive advantages. Some significant telcos in the former Yugoslavia are still to be privatised, but it is far from certain that sales will push forward in 2018, despite a benign macro environment.

Poland and Austria are the leading jurisdictions for those seeking deals in TMT in 2018, with nearly two-thirds (63%) of respondents looking for targets in each of the countries. Romania and the Czech Republic are also seen as attractive (47%).

TECH, MEDIA, AND TELECOMS M&A, 2012-2017







## SOURCING TALENT

"There are two key drivers behind M&A in the technology sector," says Jacek Michalski, partner at Wolf Theiss, Warsaw. "One is that they offer high growth potential and high margins. But second, because of the high quality of talent here in Poland, more and more companies work for international clients or, in some cases almost exclusively for foreign clients."

In Austria, tech start-ups are starting to attract attention from Chinese investors, says Jiayan Zhu, senior associate, at Wolf Theiss, Vienna. The start-up ecosystem has benefitted from Austria's top-quality universities, high GDP per capita, and favourable regulatory framework.

Michalski notes that outsourcing is a fast-growing sector which has evolved from a focus on basic back-office functions to highly complex operations over the past decade, and now employs hundreds of thousands of people. Fintech is another highly dynamic segment, where development has been supported by partnerships with major players in Poland's large and sophisticated banking sector.

Michalski also sees potential for dealmaking from controversial planned changes to Poland's media law which aim to reduce concentration of ownership in the sector. This could lead to media owners reshuffling their portfolios, affecting such big international players as US-based Scripps Network Interactive and Germany's Ringier Axel Springer Media and Bauer Media Group.

The tech sector has become an important contributor to growth in Romania in recent years, with the January 2017 acquisition of two-year-old start-up Vector Watch by US wearable technology leader Fitbit one of the most significant recent transactions. Romania, with a population of around 20 million, has the benefit of a larger human resource pool than many of its neighbours, while having the stability and access to financing provided by EU membership, unlike more-populous Ukraine.

"What is noteworthy in Romania is that we are seeing interest both from strategic and private equity firms," says Ileana Glodeanu, partner at Wolf Theiss, Bucharest. "Strategic investors are very strong and have a large presence in Romania. Amazon and Google just entered the market. All the big names are here."

## TELECOM TARGETS

Whereas the telecoms markets are fairly stable in most EU member states, in Ukraine, the sector is evolving. As Russian investors exit other sectors in Ukraine due to geopolitical tensions, economic pressure, and sanctions, there has been speculation that Russian telco MTS will sell its wholly owned Ukrainian operator Vodafone, the second-biggest operator. The expected launch of 4G in 2018, with the three leading telcos expected to bid for licences, will also shape competitive dynamics in the market for years to come. On 4G, Taras Dumych, partner at Wolf Theiss, Kiev, notes: "You have two very strong drivers to getting something done here – the government's desire to obtain the expected high licensing fees as well as its desire to bring this modern technology to Ukraine as soon as possible."

In Slovakia, one of the most notable transactions of the year was the merger of broadband operator Swan, which focuses largely on the residential market, with Benestra, which mainly serves business customers. The natural strategic fit between the companies drove a merger creating the largest domestically owned alternative telecom operator in the country.

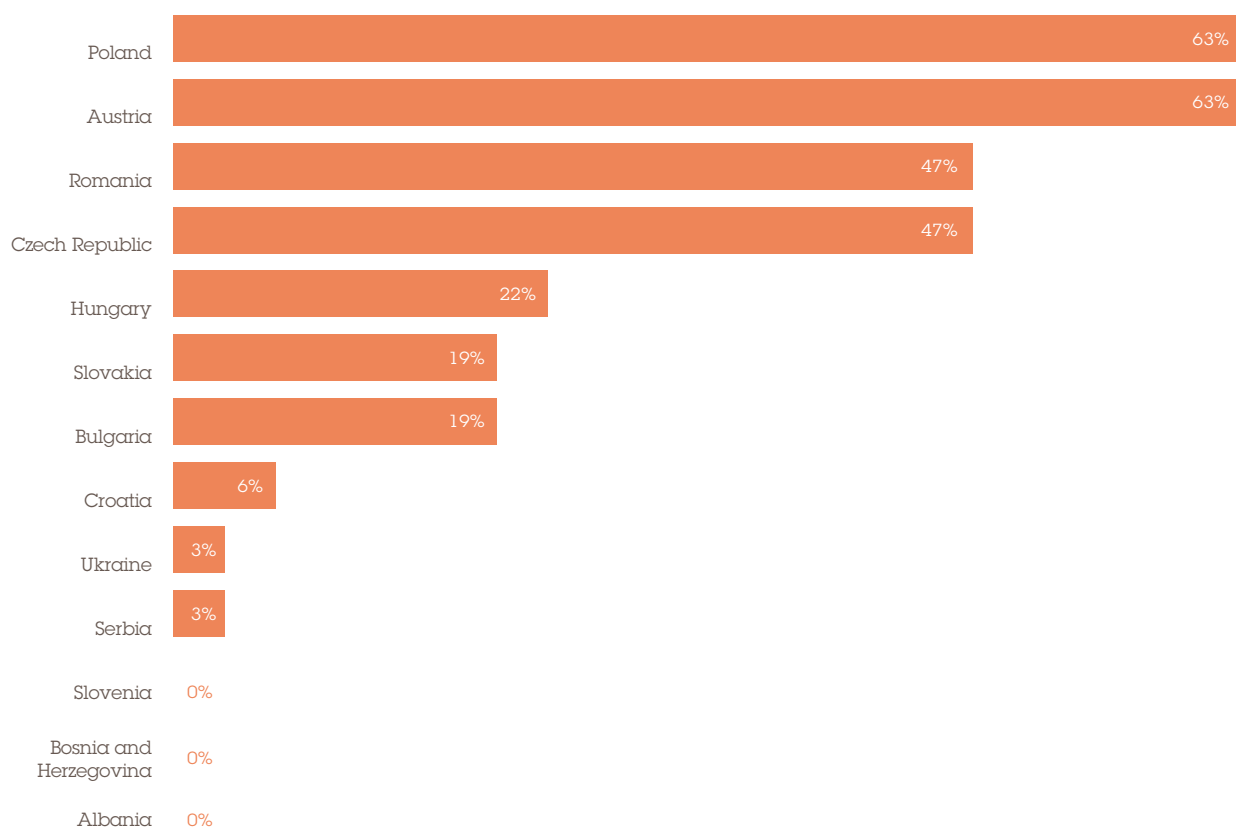
## CHALLENGES AND SENSITIVITIES

Specific compliance challenges that are particularly acute include bribery and corruption regulations (mentioned by 69% of respondents), money laundering regulations, and data and privacy protection rules (66%). Furthermore, 63% of investors say that antitrust compliance is a challenge in their target jurisdiction.

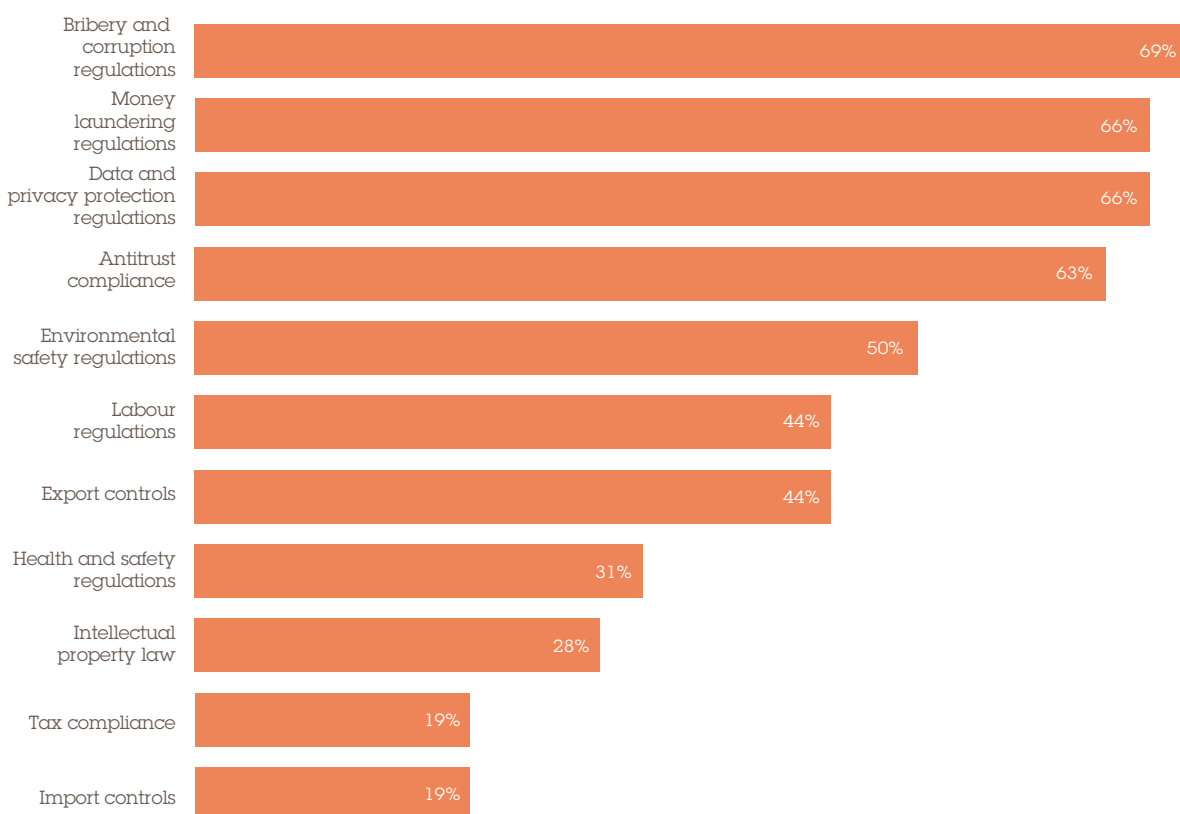
"Antitrust regulation is increasingly playing a very big role when companies consider doing deals," says Ebhardt. "Regulators are scrutinising transactions in a lot of detail, and it's very time consuming. For the parties involved, there is a risk that you may have to make certain concessions in order to get approval, which is making transactions complex and lengthy."

A wave of activity in the CEE TMT market in recent years has pushed up valuations both for start-ups and established companies. In 2015, the Serbian government rejected all bids for the privatisation of legacy telco Telekom Srbija after investors failed to meet its valuation, which many analysts felt was inflated.

In which country/ies are you currently looking for new opportunities?  
(Please select all that apply)

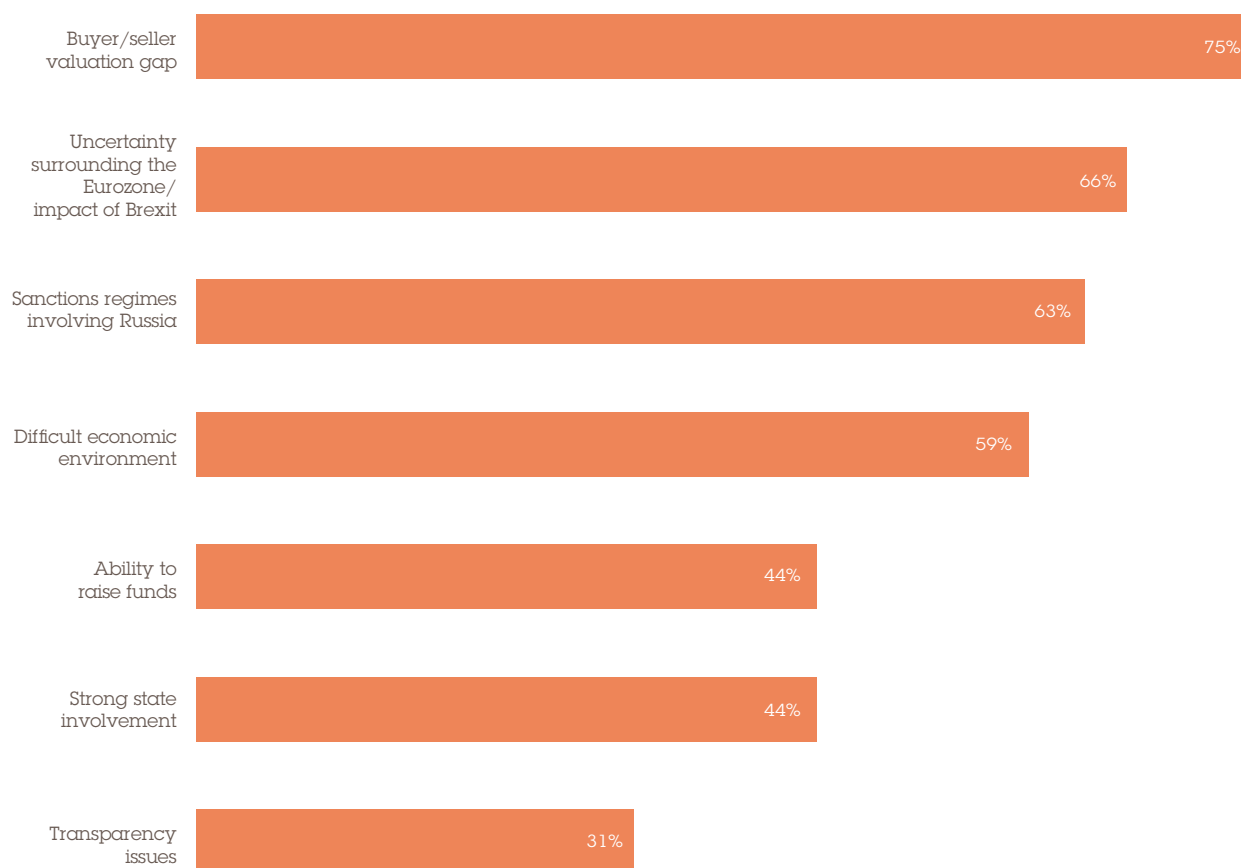


Which compliance/regulatory processes do you consider to be the most challenging to manage in that country? (Please select all that apply)



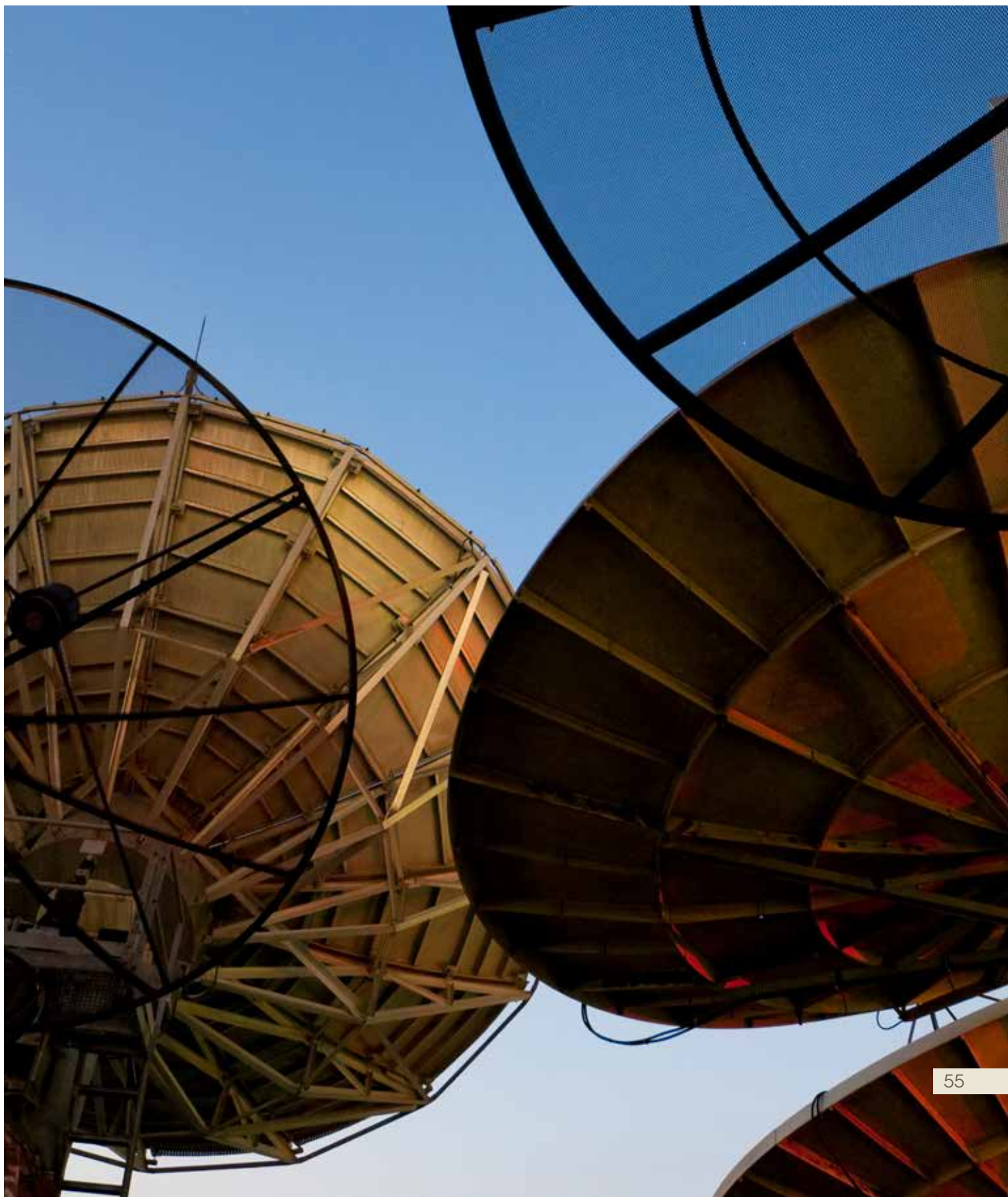


What do you perceive as the biggest challenges to implementing your CEE strategy in general?  
(Please select all that apply)



Despite interest from both strategic and financial investors, the sale of Telekom Srbija and Slovenian counterpart Telekom Slovenije failed to materialise in 2017. With parliamentary elections due in Slovenia and a snap poll possible in Serbia, these politically sensitive privatisations may not move forward in the next year. Similarly, the privatisation of two regional telcos in Bosnia and Herzegovina has gained little traction, despite pressure from the IMF and EU.

Indeed, the buyer/seller valuation gap is perceived as one of the biggest challenges to dealmaking in the region, cited by 75% of TMT investors. The uncertainty generated by the eurozone crisis and the impact of Brexit is also a major concern (66%), as are sanctions involving Russia (63%).



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