2017 GUIDE to Mergers & Acquisitions in Southeast Asia
Objective of this Guide

Southeast Asia has grown in importance in the world and many foreign multinationals have expanded their presence in this region. This expansion often takes the form of acquisitions of local companies, especially mid-sized ones. This guide provides practical advice on how to successfully perform acquisition projects in Southeast Asia.

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The importance of Southeast Asia in the current world economy

Southeast Asia is a region that multinationals cannot ignore. Its share in world GDP is still small (3%) but it is greater than new powerhouses like India and Russia¹. If the ASEAN group of countries was a single entity, it would be ranked the seventh largest economy in the world.

* ¹ GDP for 2015 measured in USD at current exchange rates. Source: BMI Research - Data for Southeast Asia only includes the ten countries of ASEAN.
A growing and richer population

Southeast Asia’s population represents 8.9% of the world’s total population, more than the European Union or the U.S. This population is growing rapidly and becoming richer due to economic development. Since 2010, Southeast Asia’s population and GDP have been growing annually at a compounded rate of 1.2% and 4.7% respectively.
An economic hub

From a large and relatively poor country like Indonesia to a first-world city-state like Singapore, from land-locked Laos to the thousands of islands of the Philippines, Southeast Asia is very diverse. The region is however slowly becoming more integrated and, as a group, it is taking an important place in the world economy.

From an economic and strategic perspective, the Strait of Malacca in Southeast Asia is one of the most important shipping lanes in the world¹. The Strait connects Middle-Eastern oil to Japan, China and Korea and major East Asian exporters to export markets such as Europe.

A key exporter

Southeast Asia is a key exporter to major economic blocs. It was the 4th largest trading partner of the U.S. in 2015, up from 5th place in 2009². It is also the EU’s 3rd largest trading partner³ (after the U.S. and China) and Japan’s 2nd largest source of imports⁴, just behind China.

Southeast Asia is also a major exporter of raw materials and semi-finished goods to China (Southeast Asia was China’s 3rd largest trading partner⁵) where such goods are processed and assembled before being re-exported to major developed markets. This link between Southeast Asia and China is also significant for mergers & acquisitions. Chinese companies have turned their attention to Southeast Asia and started to use acquisitions to secure their source of raw materials and other supplies.

“Chinese companies have turned their attention to Southeast Asia and started to use acquisitions to secure their source of raw materials and other supplies.”

¹ The Strait of Malacca is between Singapore and Malaysia on one side and the Indonesian island of Sumatra on the other
² US-ASEAN Business Council Inc.
³ European Commission: Trade - ASEAN (Bilateral relations)
⁴ Mission of Japan to ASEAN
⁵ ASEAN - China Centre
The Importance of Mid-Market Acquisitions in Southeast Asia

Mid-sized targets for “bolt-on” acquisitions

In 2015, the number of acquisitions of targets in Southeast Asia with a value of less than USD 100m represented close to 80% of the total number of transactions (source: MergerMarket). The relatively small size of many companies in Southeast Asia explains this predominance of mid-market transactions.

Southeast Asia’s mid-sized companies are often good targets for “bolt-on” acquisitions by foreign multinationals. In a “bolt-on” acquisition, the acquirer fills a hole in its current coverage. It might fill that hole by acquiring a target company in a country where it is not yet present, or adding a complementary product to its existing product line. Bolt-on acquisitions typically deliver higher relative synergy levels than larger transformational deals.

The idea for the acquirer is to buy something it can readily understand and that is typically small enough compared to its current business. For example, a company active in several Southeast Asian countries but not in Malaysia would buy a target in Malaysia in exactly the same business, requiring the same capabilities it has already developed elsewhere in the region.

Some owners of mid-sized targets may not be willing to sell today, reasoning that with continuing high growth their companies would be much more valuable in the future. It is indeed difficult for an owner to rationalize selling while his company is growing robustly, unless the acquirer is willing to pay an excessively high price.

However, some sellers have limited choices. Firstly, generational succession issues have become more common. In addition, an increasing number of sellers have begun to realize that in the long run, it is very difficult to continue to grow sustainably, especially when foreign competition from larger global companies starts to squeeze their profits and market share.

Strong growth in Southeast Asia

Southeast Asia has emerged as an attractive region to invest in. Strong domestic spending driven by the rising middle class, an increased pool of skilled workers as a result of better access to formal education, as well as improving political stability in some countries as governments in Southeast Asian countries strive for sustainable socio-economic progress have boosted the confidence of a lot of investors to grow their wealth in Southeast Asia. Such optimism is reflected in the significant increases in the region’s GDPs in the past five years.

Note: The growth represents 5-year compound annual growth rate for each country.
Source: BMI Research, Pickering Pacific analysis.
Although mid-market acquisitions in Southeast Asia can make a lot of sense for foreign acquirers, successfully performing them requires a disciplined process, which we detail below in three distinct steps:

**STEP 01**  
**EFFECTIVE DEAL SOURCING**

**STEP 02**  
**SUCCESSFUL EXECUTION**

**STEP 03**  
**SMOOTH INTEGRATION**
Effective Deal Sourcing
Finding the Right Targets
Southeast Asia presents challenges to the uninitiated. We cover the main challenges below and offer some practical steps to deal with them.

Southeast Asia is diverse and complex
As the table below shows, Southeast Asian countries are very varied. Their size, political and legal systems and levels of development are different. Although they are geographically close, the countries of Southeast Asia also have very different cultures. This diversity even extends within many of the countries with the existence of sizeable minorities (e.g. Malaysian Chinese in Malaysia, Bali Hindus in Indonesia, etc.). Because of this diversity, what works in a given country may not work in another.

<table>
<thead>
<tr>
<th>Country</th>
<th>Type of Government</th>
<th>Legal System</th>
<th>GDP (USD bn)</th>
<th>GDP per capital (USD)</th>
<th>Ethnic Groups</th>
<th>Religions</th>
<th>Languages</th>
</tr>
</thead>
<tbody>
<tr>
<td>Brunei</td>
<td>Absolute Monarchy; Sultanate</td>
<td>Common law; Islamic Sharia law for Muslims</td>
<td>16</td>
<td>36,667</td>
<td>Malay (66%) Chinese (11%)</td>
<td>Muslim (79%) Christian (9%)</td>
<td>Malay</td>
</tr>
<tr>
<td>Cambodia</td>
<td>Parliamentary Constitutional Monarchy</td>
<td>Civil law</td>
<td>18</td>
<td>1,162</td>
<td>Khmer (98%)</td>
<td>Buddhist (97%)</td>
<td>Khmer</td>
</tr>
<tr>
<td>Indonesia</td>
<td>Presidential Republic</td>
<td>Roman-Dutch Law</td>
<td>862</td>
<td>3,370</td>
<td>Javanese (40%) Sundanese (16%)</td>
<td>Muslim (87%)</td>
<td>Bahasa Indonesia</td>
</tr>
<tr>
<td>Laos</td>
<td>Communist State</td>
<td>Civil law</td>
<td>13</td>
<td>1,826</td>
<td>Lao (55%), Khmu (11%)</td>
<td>Buddhist (67%)</td>
<td>Lao</td>
</tr>
<tr>
<td>Malaysia</td>
<td>Constitutional Monarchy</td>
<td>Common law; Islamic Sharia law for Muslims</td>
<td>296</td>
<td>9,767</td>
<td>Malay (50%) Chinese (23%)</td>
<td>Muslim (61%) Buddhist (20%)</td>
<td>Bahasa Malaysia, English, Chinese</td>
</tr>
<tr>
<td>Myanmar</td>
<td>Parliamentary Republic</td>
<td>Common law</td>
<td>67</td>
<td>1,209</td>
<td>Burman (68%)</td>
<td>Buddhist (88%)</td>
<td>Burmese</td>
</tr>
<tr>
<td>Philippines</td>
<td>Presidential Republic</td>
<td>Civil law with influence of common law</td>
<td>294</td>
<td>2,891</td>
<td>Tagalog (28%) Cebuano (13%)</td>
<td>Roman Catholic (81%)</td>
<td>Filipino, English</td>
</tr>
<tr>
<td>Singapore</td>
<td>Presidential Republic</td>
<td>Common law</td>
<td>278</td>
<td>49,639</td>
<td>Chinese (74%) Malay (13%)</td>
<td>Buddhist (34%) Muslim (14%)</td>
<td>Chinese, English, Malay, Tamil</td>
</tr>
<tr>
<td>Thailand</td>
<td>Constitutional Monarchy</td>
<td>Civil law with influence of common law</td>
<td>395</td>
<td>5,864</td>
<td>Thai (96%) Burmese (2%)</td>
<td>Buddhist (94%)</td>
<td>Thai</td>
</tr>
<tr>
<td>Vietnam</td>
<td>Communist State</td>
<td>Civil law</td>
<td>191</td>
<td>2,048</td>
<td>Kinh (86%)</td>
<td>Buddhist (8%) Catholic (7%)</td>
<td>Vietnamese</td>
</tr>
</tbody>
</table>

There is of course a certain uniformity of the business elites in each country. To a large extent, elites in all the countries and communities use international standards of doing business. In many of the larger companies, executives (especially younger ones) would have been trained at the same top business schools all over the world. But despite this growing trend, one must still take into account the diversity of Southeast Asia in order to succeed in this region.

**Difficulties in finding relevant information and processing them**

Many companies in Southeast Asia do not disclose much information. This applies to both listed and unlisted companies.

For listed companies, the inadequate disclosure results from several factors:

- With few exceptions, the stock exchanges in Southeast Asia do not have a good track record of enforcing proper disclosure practices.
- Many listed companies are owned by local owners who also own a separate unlisted group. There are often many transactions between the listed and unlisted groups for which disclosure may not be complete.
- There is not yet a culture of active shareholders seeking to compel listed companies to achieve higher levels of transparency.

For unlisted companies, there is often little information that is publicly available. In some Southeast Asian countries, it is possible to access the accounts of unlisted companies when they are filed with the relevant public registry. However, even for these countries, the information may be filed late or be inaccurate. In many cases, the inaccuracy is due to the desire of the company to minimize taxes. Language can also be a barrier due to the region’s many official languages.
Local sellers are difficult to approach

Many of the successful mid-sized companies in Southeast Asia are owned by families or recently formed entrepreneurial teams. In both cases, the initial approach by a potential acquirer may not be welcomed.

Owners often do not want to sell the family company, often perceived as an heirloom to be passed on to future generations. In ethnic Chinese families, which are very common in the business world of Southeast Asia, it can be perceived that selling the business is an insult to the memory of the ancestor who founded the company a few generations back.

Entrepreneurial teams are also difficult to convince. Like elsewhere in the world, entrepreneurs tend to be very attached to the company they founded. It is often difficult for them to let go. Selling may also be perceived to be a loss of “face” within the local community. In addition, many Southeast Asian entrepreneurs see a public listing as the pinnacle of a career. Quite a few would rather do a mediocre listing than a good trade sale. As Southeast Asian stock exchanges tend to accept listing by relatively small companies, the IPO route is perceived as a credible exit strategy for many of the region’s medium-sized companies.

Case study

In one case, we were dealing with a Malaysian conglomerate founded two generations back. The conglomerate had diversified into many businesses, some of which were totally unrelated to the core businesses of the group and would have been of much more value to a focussed acquirer. The current generation of family owners, all with MBAs from major business schools, fully understood the need to divest these non-core businesses. However, they could not bring themselves to sell anything that had been bought or started by the previous generations. They were only happy to sell the parts of the business they had started themselves.
Key Recommendations
for finding good acquisition targets in Southeast Asia

i. **Good strategy, well conceived and adapted to the local context**
   The first step to finding good acquisition targets is for the acquirer to know exactly what it is looking for. The overall expansion strategy of the acquirer needs to be adapted to a specific acquisition strategy for Southeast Asia.

ii. **Good understanding of how the strategy translates into criteria for the right targets**
   Once a specific acquisition strategy has been developed for Southeast Asia, it is useful to translate it into a set of key criteria that any suitable acquisition target must meet. For example, the size criteria must take into account that in certain industries typical company size will be smaller in Southeast Asia than in some other markets.

iii. **Skills and knowledge to find the targets**
   Finding suitable targets is not easy. It requires a good knowledge of the region and specific skills. M&A intermediaries can help by initially talking to people in the relevant industry on a no-name basis: people are much more open to talk in this manner. Acquirers should also not stop at the feedback that “target X is not available for sale” or “the owners will never sell”. Knowing how to probe further can result in convincing owners to sell targets that were initially “not for sale”.

iv. **Pro-active approach to targets**
   Most targets which are already “for-sale” are being marketed as the result of defects in their business. Good targets are “not for-sale” and most often their owners do not know that they will ultimately sell when we first approach them for our clients.

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**Case study**
A few years ago, we approached a target in Thailand for a client. We were told by people close to the company that its owners were not willing to sell. After reviewing the overall situation of the seller’s group, we considered that the likely reason was the potential high tax on the proceeds of the sale. We devised a simple structure with the help of the local office of a large tax firm that could greatly (and legally) reduce the taxation of the proceeds. During the first meeting, the owners indicated that the company was not for sale. We acknowledged this but stated that if the reason was taxation, there was a structure that could help the sellers. The owners said that this was not possible in Thailand. We showed them a short memorandum from the tax firm confirming what we had said. The owners asked for a break and after a few minutes re-appeared telling us that they were happy to start working on a sale.
Successful Execution

Lack of M&A Sophistication

In many Southeast Asian markets, the market for acquisitions is still not very developed. In these countries, the lawyers, accountants and other advisers that are likely to be chosen by the sellers do not properly understand M&A techniques and rationales. Although this could sometimes be perceived as a good thing for the acquirer, we generally find that it makes the successful completion of the transaction less likely as the owners, wrongly advised, ask for things that are impossible or do not make sense.

Relationships with government and local authorities

Many businesses in Southeast Asia rely on good relationships with the government and local authorities. Acquirers must be careful that these relationships subsist after the acquisition and can be sustained lawfully. In addition, the acquisition by foreign interests could lead to a potential loss of business. This could be due to the foreign acquirer’s different way of doing business. As an example, one of our clients had to abort a transaction in Vietnam when it became apparent that the target was achieving its sales using practices that the foreign acquirer could not condone (i.e., bribing doctors to prescribe the relevant health products).

“In order to properly assess the prospects of a target, the acquirer will need a good knowledge of the local market.”

Knowledge of the local market

In order to properly assess the prospects of a target, the acquirer will need a good knowledge of the local market. This is not always easy to obtain. We advised a European-based industrial group looking to make an acquisition in Thailand in a sub-sector of the industry where it is a world leader. However, contrary to what senior management expected, the local team did not have a good grasp of the Thai markets for the products of the target. Unfortunately, but as is frequently the case in Southeast Asia where the markets are less well researched than in Europe or the U.S., there was no easy way to gain a quick overview of the relevant markets: none of the existing consulting reports covered well these markets and no specialized consulting firm seemed to be able to supply market intelligence at the desired level of precision. In the end, the client decided not to pursue the opportunity.
Due diligence issues

In many countries of Southeast Asia, there will usually be significant issues with the targets themselves. For example, in countries like Indonesia, Thailand, and Vietnam, the targets might be operating without having all the necessary licences or sufficient levels of insurance coverage. This is a risk that many local owners may be prepared to take. Foreign acquirers are reluctant to take such risks and are often held to higher standards than the local owners they replace. Another example is corruption.

The chart below shows the place of major Southeast Asian countries on the World Corruption Perception Index published by Transparency International. With the exception of Singapore, the major Southeast Asian countries are not well placed.

![World Corruption Perception Index](chart.png)
KEY RECOMMENDATIONS
for effective deal execution in Southeast Asia

i. Good team with the right external experts if they are not available in-house
The first key to the successful execution of an M&A transaction is to have a good team in place. In Southeast Asia, this means making sure that the relevant internal and external experts understand the region well. There are many traps in doing transactions in certain parts of Southeast Asia and people with relevant local experience are irreplaceable in terms of making sure the acquirer avoids these traps. Simply wanting to apply a standard European or U.S. approach to a deal in Southeast Asia will usually not work.

ii. Good process: Do not skip steps
Following a good M&A process is critical to reaching a successful outcome. Skipping steps is usually not a good idea. Despite the small size of many targets in Southeast Asia, executing a transaction here is a complex process and it is prudent to make sure that all steps of the process are carried out.

iii. Timing
Negotiation techniques must be adapted to the local context, especially with regards to timing. Although it is difficult to generalize, we find that a “slow then fast” process often works best with the acquisition of mid-sized companies in Southeast Asia. First, the approach to the sellers and arriving at an understanding on the proposed acquisition and its price must be slow. Usually the owners need a fair amount of time to come to the final decision to sell and to be convinced that the terms cannot be further improved. Once this milestone is reached however, it is advisable to go as fast as possible through the due diligence, the execution of the final agreements, and the completion of the transaction as the owners could change their mind or try to negotiate for more. Although this sequence could be generalized to the acquisition of mid-sized companies in other countries, we consider that this is even more relevant in developing Asia (including most of Southeast Asia) than in Europe or the U.S.
iv. **Objectivity**

As elsewhere, the acquirer’s team must maintain an objective view of the target at all times. Southeast Asia has a lot of potential and it is easy for the team to be carried away in making future projections of market growth. This can lead to dangerous overestimation of the target’s value and to paying a price that is too high. A good example of this issue was the boom and subsequent bust in Vietnam in 2007.

v. **Proper structure**

Many of the mid-sized companies we come across in Southeast Asia are managed by their family owners or the founding entrepreneurs. In many cases, a significant portion of the value of the company lies with these managers, through their knowledge and contacts in a tightly-linked local community. To ensure that the value of the company is not diminished by the departure of these managers, it is prudent to put in place some form of earn-out scheme whereby the owners or the entrepreneurs are paid more if the company remains successful in the two or three year period after the acquisition is completed. These schemes must be devised very carefully to (i) make sure that they align the interests of the sellers with those of the acquirers, (ii) avoid any future legal disputes, and (iii) if legal dispute cannot be avoided, lead to enforceable recourse for the foreign acquirer. In a case that was discussed with us, the European acquirer had agreed to a minimum earn-out payment. When it became clear that the target company was no longer doing well due to an unforeseen external event and that no more than the minimum payment would be obtained, the sellers lost all interest in helping the target, at a great loss to the acquirer.
**Smooth Integration**

Successful integration of the target into the acquirer’s group is not always easy. Many issues may affect the integration process.

**Cultural differences may be important**

Southeast Asia is a complex and different place for many outsiders. Imposing the acquirer’s new way of working is difficult and may not be readily understood by the staff of the target. Those cultural issues often apply to timing. Compared to New York, London, Frankfurt or Paris, everything seems to go slower in large parts of Southeast Asia. The level of urgency is not the same. This is exacerbated in some countries by tedious and time-consuming red tape, although this is generally diminishing with time.

The sellers themselves may slow down the integration when they stay as part of an earn-out process. Sometimes, they are not comfortable with the business plan of the acquirer. The acquirer may invest to develop the company and reap significant financial benefits. The sellers may mainly see the extra costs that are affecting the calculation of their earn-out. In other cases, the sellers will have non-financial issues, such as “keeping face”. They may insist in participating in all key meetings. This can delay the integration.

“...Compared to New York, London, Frankfurt or Paris, everything seems to go slower in large parts of Southeast Asia.”

**Local authorities taking a much closer look**

Finally, when a company becomes foreign-owned, the local authorities usually take a much closer look at its operations. Suddenly, the tolerances that were in place are removed, grey areas are decided against the company, inspections take place, etc. This leads at best to time-consuming delays, at worst, to significant losses of value.
KEY RECOMMENDATIONS
for smooth integration in Southeast Asia

i. Prepare, prepare, prepare
The first advice that we give to acquirers integrating a Southeast Asian company is to “prepare, prepare and prepare”. This is similar for integrations around the world. Many of the issues mentioned above can be effectively dealt with if they do not come as last minute surprises. Plans must be in place to, inter alia, facilitate cultural integration, organize the integration teams so that they can work fast, align the sellers’ interests with the acquirer’s, and pre-empt any legal or regulatory issues.

ii. Understand each other and explain:
Communication is key
Despite the general availability of local managers who understand the ways of working of large European and U.S. multinationals in Southeast Asia, there is still a significant cultural gap at least at the middle and lower echelons of mid-sized companies in Southeast Asia. For example, it might be difficult to make a middle-ranking Malaysian manager offer alternatives to the decisions of his superiors. A U.S. manager keen on participative management may fail in this environment if he or she is not aware of the cultural differences at play. Clear and open communication is always useful in this case, as well as cultural knowledge and awareness.

iii. Move as fast as possible
We consider that the integration should normally proceed as fast as possible. This reduces the time of uncertainty for employees. It also reduces the risk for the acquirer as some existing practices may need to be stopped immediately (e.g., issues around corruption, improper tax filings, etc.)

Acquisitions in Southeast Asia can represent very large value creation opportunities for multinational acquirers. However, as we have seen, these transactions are also fraught with dangers. Pickering Pacific can guide you, as we have guided our many clients since 2004, in navigating these dangers and realizing successful acquisitions in Southeast Asia.