

DueDiligence2022

M & A IN THE DIGITAL AGE

MERRILL DATASITEONE

CONTENTS

Foreword	3
Research methodology	4
Executive summary	5-6
Section 1: Success factors in M&A.....	7-12
Section 2: The technologies transforming due diligence	13-20
Section 3: The impact of security and regulation on due diligence	20-25
Conclusion and recommendations.....	26-27
Appendix	28-30

FOREWORD

In the past couple of decades due diligence has evolved and improved thanks in large part to the advance of technology and digitisation.

Where before the process was frustrated by physical data rooms and huge volumes of paper documents, due diligence is rapidly moving into sophisticated, intelligent virtual data rooms replete with digital content libraries.

This has in turn led to greater speed, simplicity and security in the entire process, enabling practitioners to both withdraw from and close deals faster.

But if today due diligence is more advanced and efficient than in the past, how much more advanced and efficient could the process be in the future? Indeed can technology and digitisation potentially transform due diligence?

To help answer this, we were interested to know how M&A practitioners on all sides of a deal – from corporate and private equity firm executives to their investment banking, legal and accounting advisers – viewed the future of due diligence. In particular what are the main challenges today that existing and new technologies could potentially provide a solution for?

These senior executives were from across Europe, the Nordics, Middle East and Africa, but their views will no doubt resonate with their peers globally.

For instance, the single biggest challenge in due diligence, which they believe technology could provide a solution for, is being able to review and analyse hundreds and thousands of pages of contract text accurately and swiftly.

It is a labour-intensive process that is one of the most time-intensive in due diligence. But it is one in which artificial intelligence (AI), specifically machine learning, is already being successfully applied in some quarters, enhancing the accuracy and speed of the review process.

Indeed practitioners are placing great hope on the transformative impact AI and machine learning, data analytics, and even blockchain technology could have on due diligence. A transformation potentially powered by more advanced virtual data rooms.

It is these technologies, individually and collectively, that can empower and better equip practitioners, ultimately enabling far greater analytical capability, speed, accuracy, security and simplicity in due diligence.

That is what the future looks like. This is **#DueDiligence2022**.



Hilary London

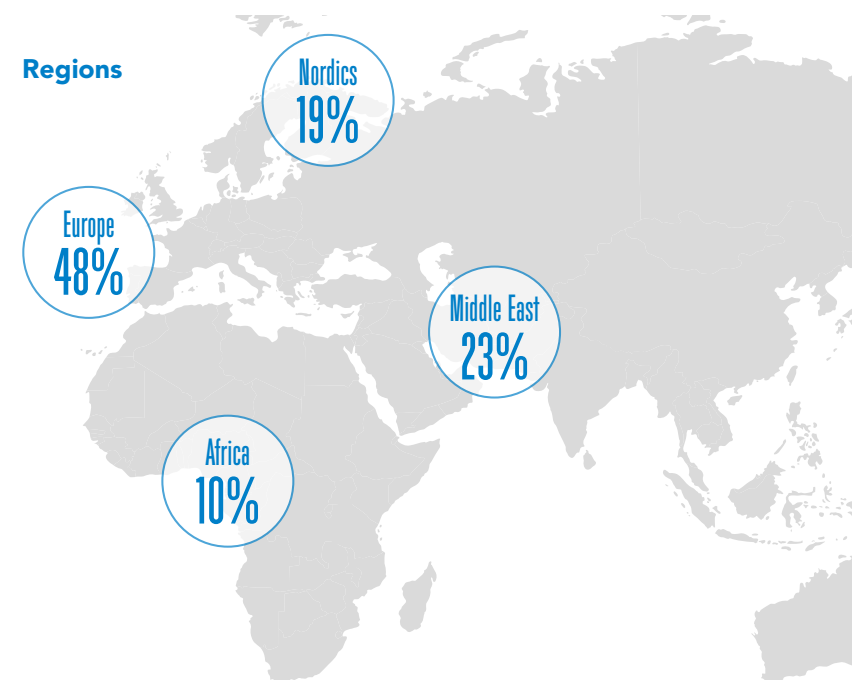
CRO & GENERAL MANAGER, EMEA
AT MERRILL CORPORATION

RESEARCH METHODOLOGY

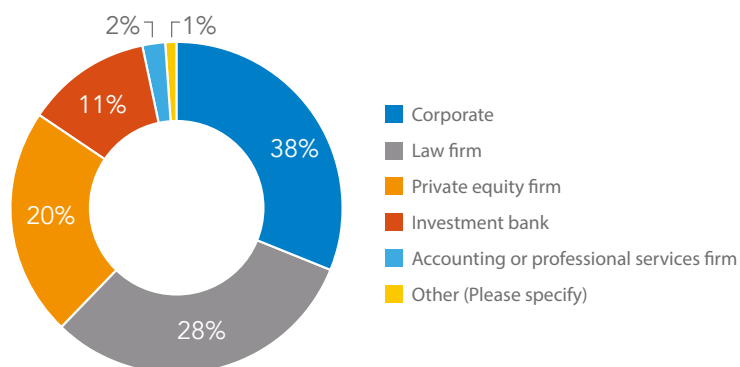
For this report, Euromoney Thought Leadership Consulting surveyed 539 professionals involved in M&A transactions. Most respondents were from corporates (38%) and private equity firms (20%). The remainder came from law firms, investment banks and accounting and professional services firms (41%).

Most respondents were at the manager (22%) and associate level (22%), followed by directors (16%), analysts (12%), board-level executives (9%), partners (9%), legal advisers (5%), managing directors (2%), financial advisers (2%) and M&A business development executives (1%). Geographically, respondents were based in four key geographies: Europe (48%), the Nordics (19%), Middle East (23%) and Africa (10%).

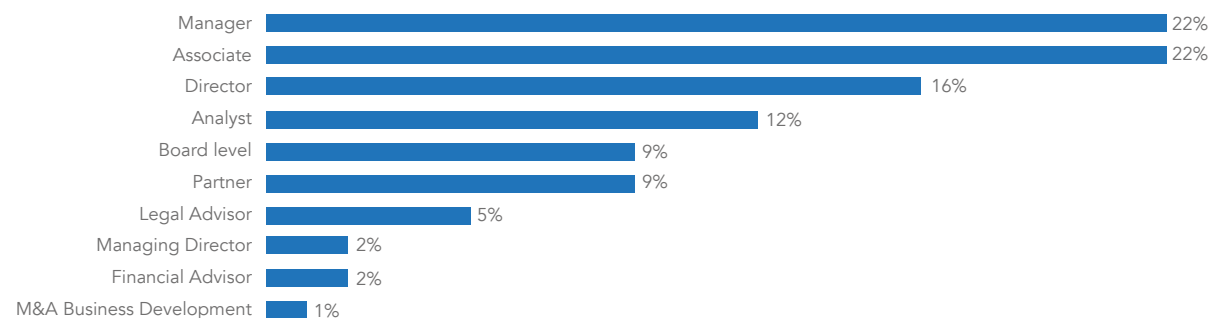
Their responses, gathered during July 2018, highlight the crucial role of due diligence as a determinant of M&A. They also provide insight into the challenges practitioners face and the potential for technological developments to take the due diligence process to the next level.



Institution type



Role



2018 > THE STATE OF DUE DILIGENCE

- 1 Realising maximum speed:** For 64% of EMEA-based M&A practitioners overall, due diligence takes on average less than three months – from sourcing a deal to deal completion – for a single successful transaction. The expectation is that the speed of the process could accelerate further if some of the main challenges in due diligence are addressed.
- 2 Data analytics the main accelerator:** Most EMEA practitioners (32%) overall believe being able to harness data analytics would accelerate the due diligence process the most, followed by a larger due diligence team (20%) and standardisation of documents and processes (14%). In Africa, however, most executives (34%) believe accessing a virtual data room enabled with AI and data analytics would accelerate the process the most.
- 3 Speed restricted by data and information management:** EMEA practitioners overall say accessing, gathering, verifying and reviewing documents, information and data is the factor that slows the due diligence process the most. Poor - or non-existent - strategy, planning and communication during the due diligence process is another drag on transactions.
- 4 Contract review the biggest challenge:** Overall 70% of EMEA practitioners say reviewing and analysing contract text is the biggest challenge in due diligence that technology could provide a solution for. Other big challenges include running multiple scenario analyses and financial modelling (52%), along with visualising financial performance data (41%).
- 5 Risk of a data breach rises:** Most corporate and private equity M&A practitioners in EMEA (35%) believe the risk of a data/privacy breach in the due diligence process over the past five years has increased. However, most investment banking, legal and accounting advisers (35%) believe the risk has decreased.

2022 > THE FUTURE OF DUE DILIGENCE

- 1 Greater security expected:** Most EMEA practitioners (63%) overall believe new technologies will enable greater security in the due diligence process over the next five years, followed closely by enabling greater analytical capability (61%) and simplifying the entire process (45%).
- 2 Larger teams supported by technology:** Overall 50% of EMEA practitioners expect the use of technology in due diligence to moderately or significantly increase the number of people involved on a transaction over the next five years. Some 31% expect the numbers to stay about the same as today, and the remainder (20%) expect numbers to decrease.
- 3 AI offers the greatest promise:** Most EMEA practitioners (42%) overall believe AI and machine learning technologies have the greatest potential to transform due diligence over the long-term, followed by data analytics (34%) and blockchain technology (15%).
- 4 Swifter due diligence:** Overall 78% of EMEA-based M&A practitioners say due diligence – from sourcing a deal to deal completion – will take less than three months on average in 2022, up from 64% in 2018. Regionally, 80% of executives in Europe believe it will take less three months (up from 72%), compared to 71% of Middle East executives (up from 48%) and 66% in Africa (up from 38%).
- 5 Regulation will impact the process:** Most EMEA practitioners (66%) overall believe the EU's General Data Protection Regulation (GDPR) will increase acquirers' scrutiny of the data protection policies and processes of target companies. However, 22% of EMEA practitioners overall believe it will have no impact on the due diligence process at all.

SECTION 1

SUCCESS FACTORS IN M&A

DUE DILIGENCE: THE FOUNDATION OF SUCCESSFUL M&A

CASE STUDY: RENTOKIL INITIAL

SWIFT EXECUTION: THE NEED FOR SPEED

CASE STUDY: DELOITTE

MANAGING COMPLEXITY: TECHNOLOGY'S ROLE

DUE DILIGENCE: THE FOUNDATION OF SUCCESSFUL M&A

Amid the rising complexity of M&A, the old and simple adage of failing to prepare then prepare to fail is as true today in dealmaking as it always has been. That is because due diligence, the time and resource intensive preparation process, can ultimately define the success or failure of M&A, which is why great importance is assigned to the meticulous practices and processes involved.

In fact, in each and every stage from preliminary, detailed to final, due diligence is considered the single most important success factor in M&A for almost two-thirds (65%) of respondents across EMEA overall, followed by planning and executing the integration process (49%), and identifying,

screening and prioritising targets (35%). Success, of course, can mean two different outcomes.

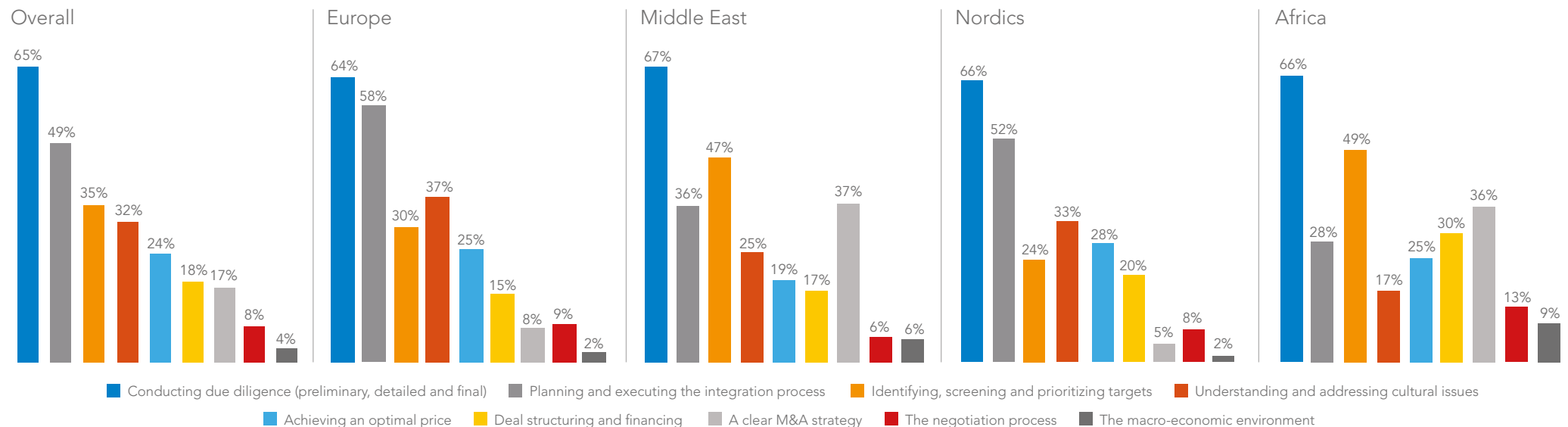
"We talk about successful M&A being when the deal is done, but success can also mean finding issues in the financial, legal or market due diligence that weren't previously obvious, which can mean the client decides the deal isn't right for them," says Matt Henderson, transaction services partner at Deloitte.

Importantly, differences in views and opinions on success factors do emerge, most evidently in the greater importance that Europe and Nordic based respondents assign to understanding and addressing cultural issues compared to their Middle East and Africa based peers.

"We talk about successful M&A being when the deal is done, but success can also mean finding issues in the financial, legal or market due diligence that weren't previously obvious."

MATT HENDERSON, TRANSACTION SERVICES PARTNER, DELOITTE

Q1. What are the three most important success factors in M&A? (Select up to three)



The power of virtual data rooms and big data

M&A has been at the heart of the UK pest control and business service group's growth strategy and a rigorous process has delivered success after success.

Central to this is M&A director Chris Hunt, who qualified as an accountant at KPMG in the 1990s, becoming a transaction services director at a time when the professional services firm was at the forefront of the drive to turn due diligence from a tick-box exercise around financials and legal to the forward-looking, all-encompassing service it is today. After seven years in finance, strategy and M&A at pharmaceutical company AstraZeneca, Hunt joined Rentokil in 2012, where he has led more than 200 acquisitions. Most have been bolt-ons, but there have been larger deals to enter new product markets and territories.

"The two big themes in the due diligence world are virtual data rooms and big data. Both will impact the way due diligence is done," says Hunt. The vast majority of businesses Rentokil buys are owner-managed and some don't even have computer records, but larger transformative acquisitions are becoming more data-rich. "We focus on the quality of the business and the quality of the customer economics. We want to know what the customer base is doing, what the churn is, where pricing is, whether revenues are contracted, who are the strong performing service

technicians and whether all of that is leading to revenue growth. On top of the financial due diligence there is a heavy overlay from the commercial, operational and technical people."

Whilst the leg-work of legal due diligence and sales and purchase agreements is contracted out to lawyers, most of the assessment is done by Hunt's team and other managers, particularly country heads: "We feel you get a crisper, cleaner, more concise answer and going through advisers slows you down. We're professional, we want to understand the data, we want to make informed decisions and we're very quick, clean and simple to deal with."

In the past three years Rentokil has completed over 130 acquisitions including market entries in Guatemala, El Salvador and Honduras, adding to its fast-growing presence in the Latin America region, where the company already has operations in Brazil, Chile and Colombia. In addition to this, Rentokil has entered new markets in Eastern Europe, Africa and the Middle East. "Our biggest challenge is getting the information we need to make a decision. We treat new markets like established ones; we still come up with a hypothesis and we still look to do the right level of diligence, but we lean more heavily on advisers if we don't have many local speakers in a particular territory," says Hunt.



Chris Hunt

M&A DIRECTOR
RENTOKIL INITIAL

Listed and headquartered in the UK, Rentokil Initial is one of the largest commercial pest control services providers worldwide. The company operates in 70 countries including 90 of the world's 100 largest cities across North America, Europe, UK and Asia.

SWIFT EXECUTION: THE NEED FOR SPEED

Speed is crucial in M&A due diligence; the longer the process runs the higher the risk the deal goes cold and potentially unravels. In the past decade due diligence has surely accelerated. The question is just how swift can the process be in the future?

Today, most respondents overall (64%) say due diligence – from sourcing a deal to deal completion – takes on average less than three months for a single successful transaction. Tellingly that percentage is higher among Europe (72%) and Nordic based respondents (78%) compared to their peers in the Middle East (48%) and Africa (38%) where the process takes longer due to the greater difficulty of conducting due diligence in developing economies. Indeed, the top five countries in EMEA where due diligence on companies is most challenging and time-intensive are Iraq, Israel, Nigeria, Turkey and South Africa, according to respondents.

In the future, due diligence is expected to accelerate, with a higher percentage of respondents overall (78%) believing that the process will take less than three months on average in five years' time. This expectation for acceleration is most evident in developing economies. More than two-thirds of respondents in the Middle East (71%) and Africa (66%) believe the process will take less than three months come 2022.

Looking deeper into the data, however, it does show some differences between the views of corporate and private equity executives (M&A clients) compared to executives from investment banks, law and accounting firms (M&A advisers).

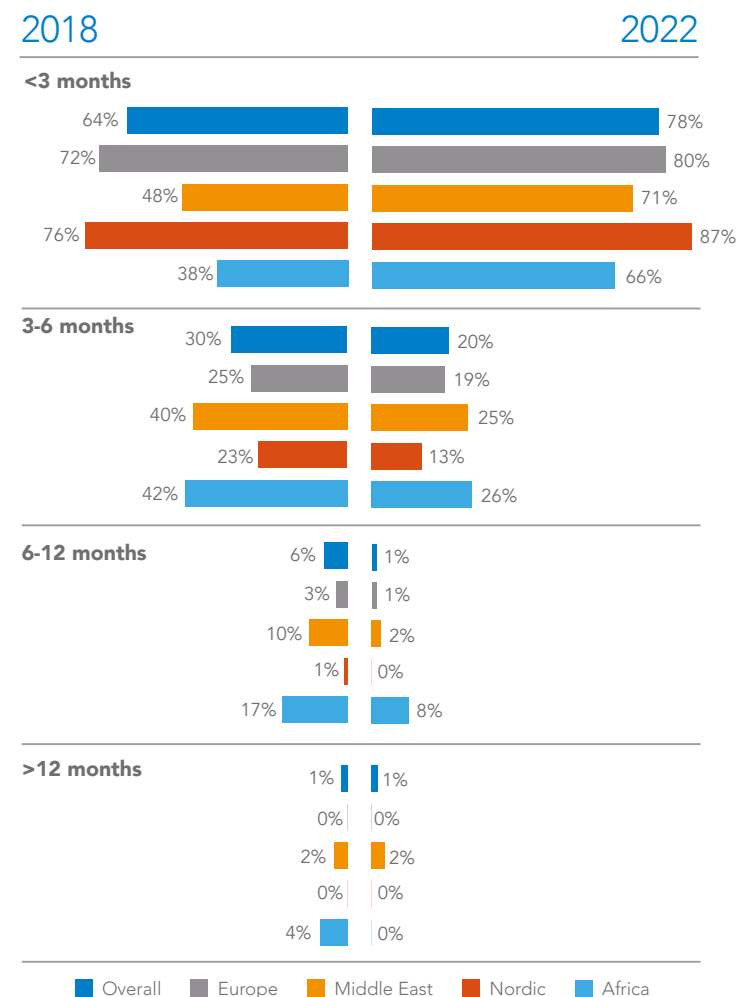
For instance, a higher percentage of advisers compared to clients believe due diligence today takes longer than three months. Though most advisers expect the process to accelerate to less than three months, they are not quite as bullish about this prediction as their corporate and private equity clients.

What's more, asked how satisfied they are with the speed of their due diligence process, respondents overall are overwhelmingly (94%) satisfied. However, only 6% of corporate and private equity executives are completely satisfied, showing there is plenty of room for improvement.

But it's not all about speed, says Alexander Becker, director of M&A at SCHOTT, an international specialty glass and technical ceramic materials manufacturer.

"In a competitive M&A process, there is always time pressure to complete due diligence and draft contracts. In a one-to-one situation, you can take more time, but if the process drags on too long, you can't keep your team focused and motivated. There is always a balance between due diligence scope and timing," says Becker.

Q5. From sourcing a deal to deal completion, how much time on average does due diligence take on a single successful M&A transaction, and how much time will it take in five years (2022)?



Next generation data analysis

Deloitte is eyeing multiple income streams from M&A, from transaction services to corporate finance, capital markets and consulting. It's intensely competitive, so firms are always looking to gain an edge.

"We've gone from being a group of individuals focused on accounting and financial due diligence to having many specialisms we can bring to a deal," says Matt Henderson, transaction services partner at Deloitte. "Not only do we have operational and technology experts who may not be chartered accountants by background, we have deep sector expertise so we can bring insight and layer it on top of the plain vanilla financial information."

Clients are much more demanding today, with the emphasis shifting to more forward-looking analysis and hypothesis testing. They want more analysis, they want it sooner and they want it better presented. "We are bringing data scientists into our organisations to identify the data inside and outside of the business that will help us prove or disprove those hypotheses," says Henderson.

Whilst elapse times for the whole diligence process have not increased, clients are demanding more detailed information quicker. "Clients are better at identifying and prioritising their own questions when they're on the buy side," says Mark Steele, partner and lead of the M&A technology practice. "They are trying much harder to get their key questions answered earlier. They want really robust answers and that is very challenging because the answers can be very difficult to get to or dependent on a complex set of items."

Technology plays a key role in delivering faster answers and increasing productivity. "Technology is helpful in identifying outliers and red flags," says Steele. "It allows you to identify the obvious issues quicker, but most deals aren't done on those issues. Where technology is far more useful is in helping us present and communicate what we find. Our focus is on delivering a richer analysis and presentation tool that's more agile than Excel so we can deliver insight on a business our clients are looking to buy."



Mark Steele

PARTNER AND LEAD OF THE M&A
TECHNOLOGY PRACTICE
DELOITTE

Deloitte is one of the world's largest global professional services firms, providing clients across industries globally with advice and services in audit and assurance, consulting, financial advisory, risk advisory and tax.

MANAGING COMPLEXITY: TECHNOLOGY'S ROLE

Over the past two decades the scope of due diligence has widened considerably. Where once a check of the financial and legal documentation was considered a thorough job, diligence today routinely covers human resources, information technology, environmental impacts, regulatory and compliance, commercial (or market), tax, insurance, property, intellectual property, customer and operations.

This information explosion has created its own challenges and created more potential hurdles to speedy due diligence. Indeed asked what factor slows the due diligence process down the most, the standout response among respondents across EMEA was accessing, gathering, verifying and reviewing all

the documents, information and data related to a transaction. The lack of or poor strategy, planning and communication between all parties involved in the process is another key factor.

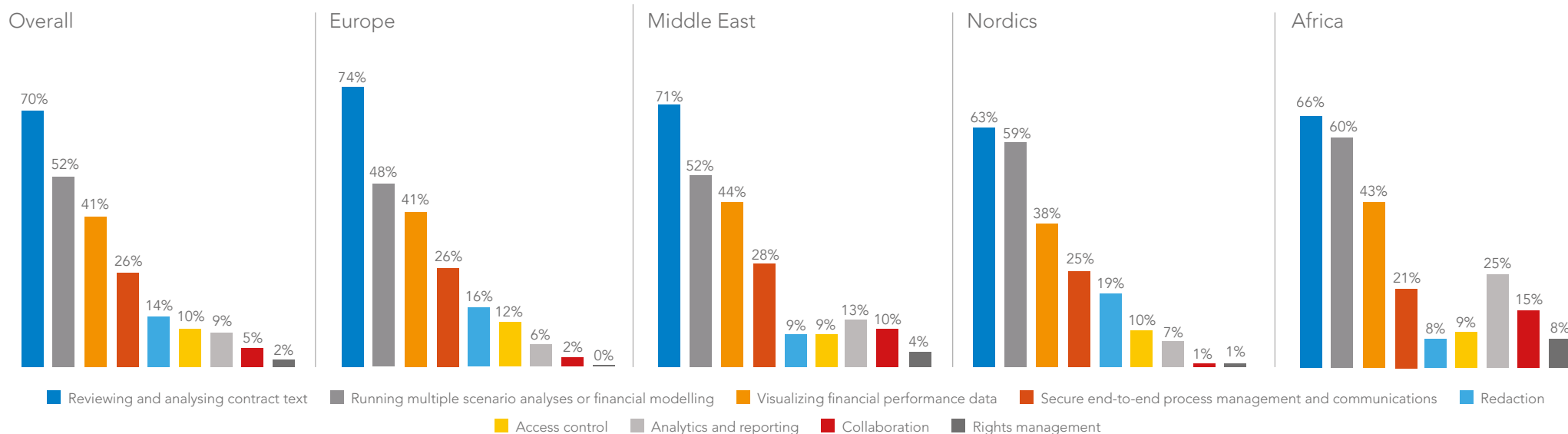
The advance of technology and digitisation has naturally enabled practitioners to better manage and speed up this increasingly complex operation.

The hope is that new technologies – from AI and machine learning to data analytics and more besides – can help solve some of the main challenges and potentially transform the operation entirely. Asked what are the biggest challenges in due diligence that technology could provide a solution

for, a resounding 70% of respondents overall said reviewing and analysing contract text, followed by running multiple scenario analyses or financial modelling (52%), and visualising financial performance data (41%).

“Technology is everywhere and you use it for every question, but there’s also a lot of legwork. You have to get the right request in, get the right information out and then use technologies to drive insight,” says J Neely, managing director, global M&A lead, Accenture Strategy.

Q15. What are the biggest challenges in due diligence that you believe technology could provide a solution for? (Select up to three)



SECTION 2

THE TECHNOLOGIES TRANSFORMING DUE DILIGENCE

THE EVOLUTION OF DUE DILIGENCE: FASTER, DEEPER INSIGHT AND ANALYSIS

AI AND DATA ANALYTICS: THE FUTURE OF DUE DILIGENCE

CASE STUDY: 3I

SOCIAL MEDIA: A NEW RESOURCE IN IDENTIFYING RISK

VIRTUAL DATA ROOMS: SIMPLIFYING COMPLEXITY SWIFTLY

CASE STUDY: CLIFFORD CHANCE

THE EVOLUTION OF DUE DILIGENCE: FASTER, DEEPER INSIGHT AND ANALYSIS

Over the past two decades technology has brought change to due diligence. For experienced M&A professionals physical data rooms are a fond memory, though they do still exist on some smaller deals. However in the coming years practitioners expect to see substantial – if not transformational – changes to the process, much of which will be driven by the application of existing and emerging technologies.

So where and how do practitioners expect technology to change the due diligence process?

Technology certainly plays a big part in speeding up the entire process, but in addition to that most respondents overall (63%) say technological advancement will also enable greater security, an issue of paramount importance in a digitally connected age. Together with this, some 61% of respondents say technology will also enable greater analytical capability and 45% believe it will help simplify the process from beginning to end.

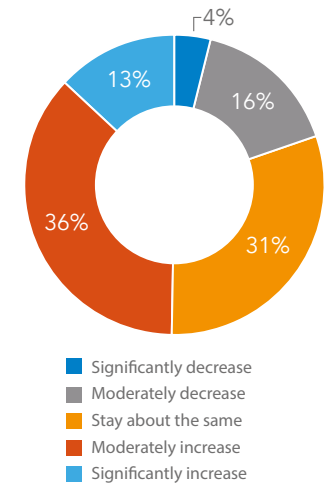
So technology should enable greater speed, security, analytics and simplicity in the process, which should in turn help reduce the time

and resource cost (according to 25% of respondents) and ultimately help close deals faster (according to 23% of respondents) in the future. However, the greater use of technology in due diligence does not seemingly reduce the need for human capital.

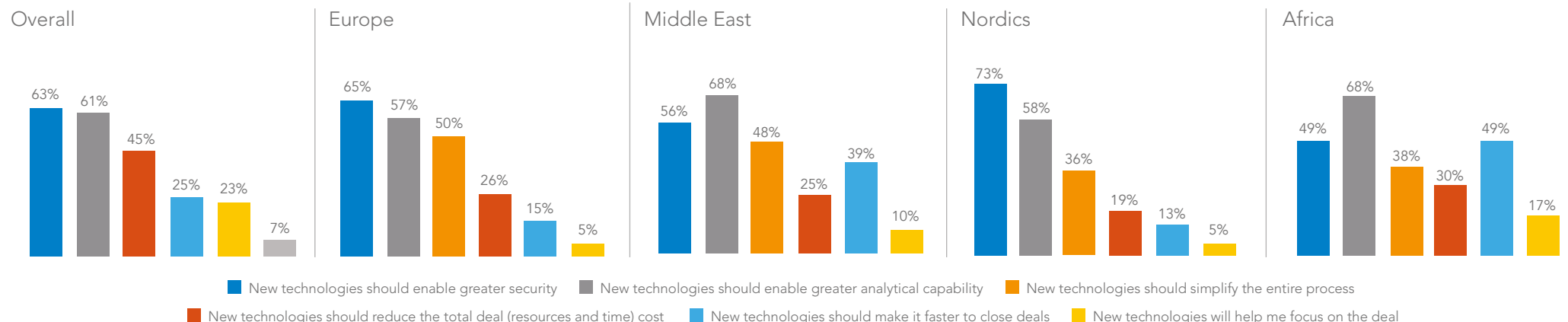
Overall 49% of respondents across EMEA expect the use of technology in due diligence to moderately and significantly increase the number of people involved on a transaction over the next five years. Only in the Middle East do most respondents (37%) believe that the number of people will moderately and significantly decrease.

“Historically technology has been a blunt instrument, but it is increasingly helpful in identifying outliers and red flags that may mean one of our experienced staff doesn’t have to go through a thousand documents to find outlier issues. Technology will pick that up earlier, which is important because clients want faster, deeper analysis earlier in the process,” says Mark Steele, lead partner for M&A technology at Deloitte.

Q3. In the next five years, how do you expect the use of technology in due diligence to impact the number of people involved in a M&A transaction compared to today?



Q2. In the context of a M&A transaction, how do you expect technology to change the due diligence process over the next five years (to 2022)? (Select up to three)



AI AND DATA ANALYTICS: THE FUTURE OF DUE DILIGENCE

The application of AI and machine learning in due diligence has only really just begun. But most respondents overall (42%) believe it could have the most transformative impact over the long-term, followed by data analytics (34%) and blockchain technology (15%).

To be sure, there is great hope and expectation for AI's application across many areas of business and finance and beyond. But there are few areas where its use and potential value are more obvious than M&A due diligence.

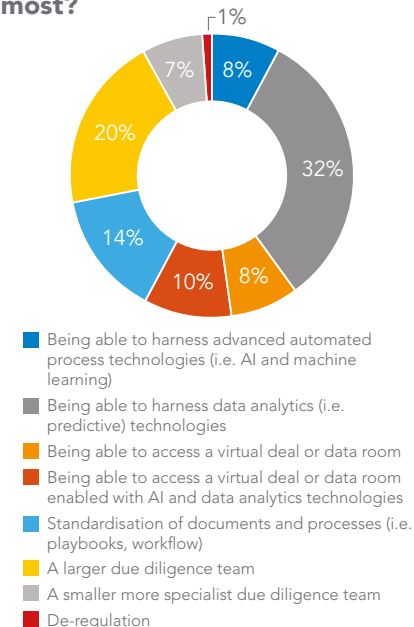
"The use of AI in legal due diligence is quickly gaining traction and has the potential to be the biggest change in the due diligence process over the next 10 years, because clients will demand it and will expect to see cost benefits from it." says Jon Kenworthy, co-chair of M&A, DLA Piper. "In the long term, lawyers may see it as a threat to their jobs but I believe that there is a long way to go before that becomes a realistic prospect. Forward looking firms see it as an opportunity. The current suite of AI products remove some of the more routine review work and allows lawyers to focus their efforts on where they can best add value."

It is for these reasons that some law firms, including DLA Piper, are already using AI – specifically machine learning technology that is pre-trained to recognise legal concepts such as change-of-control, assignability and term – to systematically review, identify and classify important content contained in swathes of contracts, thereby cutting the time and costs typically involved in the review process. Importantly, AI programmes can significantly enhance accuracy in the contract review and analysis process too.

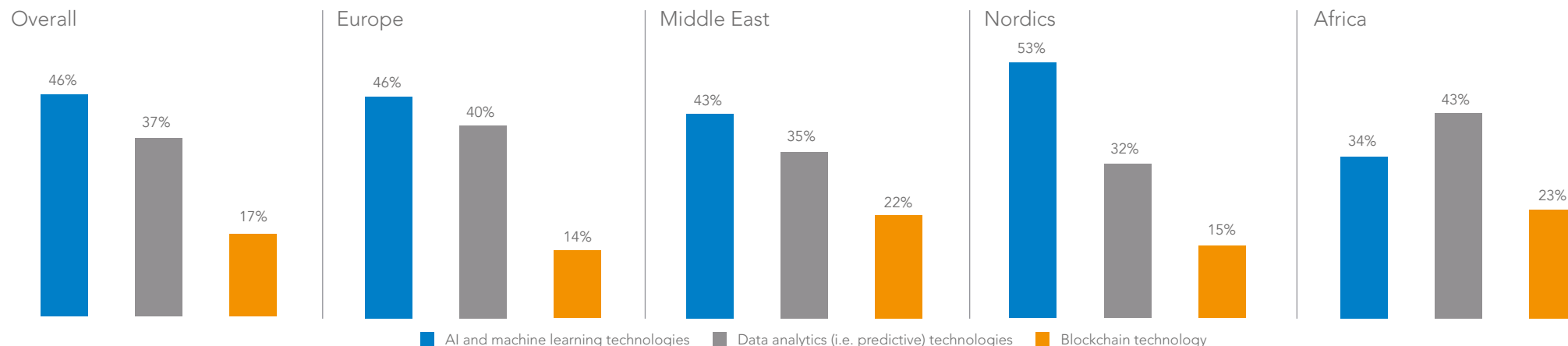
Together with this is another big challenge – being able to successfully analyse multiple data sets and draw sound conclusions quickly. Increasingly companies and their advisers are using data analytics to do so. At its simplest this involves using company, target and third-party data sets, along with statistical algorithms and quantitative analysis, to drive better insight and quicker decision-making in the M&A process.

This is why most respondents overall (32%) said being able to harness data analytics would help accelerate the due diligence process the most, followed by a larger due diligence team (20%) and the standardisation (14%) of documents and processes (i.e. playbooks, workflow).

Q8. What would help accelerate the due diligence process the most?



Q17. Which of the following technologies do you see as potentially having the most transformative impact on M&A due diligence over the long-term?



Seeing the value in AI

Private equity firms have been big beneficiaries of the broadening and deepening of the due diligence remit. It has gone hand-in-hand with increasing sector focus at most houses, a trend driven in part by the value creation strategies of the firms themselves and partly in response to competitive and time pressures.

"We try to be very focused on what we are trying to test but flexible about how we test it," says Pete Wilson, head of UK private equity at 3i. "In any transaction, everybody is working extremely hard and it's very easy to submit a generic information request list or insist the data is cut a certain way, but really this is about working with the company or its advisers to get to a sensible, pragmatic way of addressing your key issues and being realistic about the level of information you're going to get. It's a real win win if you can get that right."

Experience is a huge benefit. For example, 3i has invested in seven testing and inspection businesses in the past 10 years, including Stork Materials Technology, Trescal, ESG, Labco and Carso. "Each time we've gone into diligence we've been more sophisticated on identifying the things

that really make a difference, which are not necessarily the generic things you might expect," says Wilson. "Whilst we don't have the same depth of knowledge as trade buyers in the testing & inspection space, we do know what really drives these businesses."

To be fast and focussed you need to be efficient and 3i is an early - if healthily sceptical - adopter of new technologies: "With virtual data rooms you can get your whole advisory team instant access simultaneously and have them poring through the relevant documents within hours of the data being made available, which is quite powerful."

Wilson adds: "I've not seen any AI in VDRs yet, but diligence advisers are developing tools that can crunch through a very significant amount of complex data and pick out trends and analysis more easily, faster and in a less subjective way. I expect we will see it in financials and legal first, but the products will have to be good because people will be sceptical. The biggest challenge will be the quality of data that companies have."



Pete Wilson

HEAD OF UK PRIVATE EQUITY
3i

UK-listed 3i Group is a leading international investment manager focused on mid-market private equity and infrastructure investment. 3i's core investment markets are northern Europe and North America.

SOCIAL MEDIA: A NEW RESOURCE IN IDENTIFYING RISK

Social media and online networking has exploded in use over the past decade and is expected to continue to grow and develop in the years to come.

What's interesting is the value and importance it has in due diligence. Indeed most respondents overall (59%) say that social media's use in due diligence is very important and even critical, providing the acquirer with valuable insight about a target as well as identifying areas of risk that have potential to impact the commercial negotiation of a deal.

"We do look at social media and we will get the target's permission to talk to their customers," says Hunt at Rentokil. "You get a lot from conversations and meetings that you might not see in the Excel spreadsheets."

When analysed regionally, the importance of using social media does differ – most Europe (67%) and Nordic (71%) based respondents see it as very important and critical

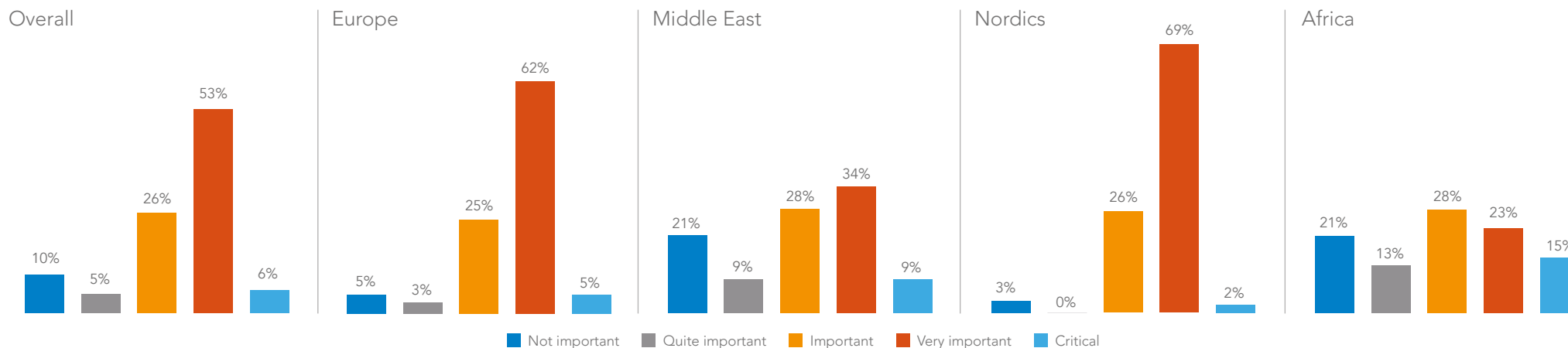
compared to the Middle East and Africa respondents, who assign much less importance to its use. And yet from blogs to LinkedIn, Twitter, Instagram, Facebook and Pinterest, what is published on these accounts can and does provide valuable insight about the target company's business, its staff and its general interactions with its customer client base, which may highlight some reputational challenges.

However, while social media can have clear benefits, Matt Henderson at Deloitte cautions about its use. "I can see social media related data such as brand sentiment analysis starting to be used to supplement other data sources. We have technologies that can be used to track consumer sentiment regarding new product launches or service quality but it has to be benchmarked quite carefully as there can be a tendency for social media to focus on negative sentiment. It is something we'd use as incremental evidence to test deal hypotheses rather than to replace traditional due diligence information sources.

"If everybody just looked at social media no-one would do any deals because it can look like customers hate the product or service."

MATT HENDERSON, TRANSACTION SERVICES PARTNER, DELOITTE

Q16. As part of the due diligence process (i.e. assessing potential targets, customer perception analysis), how important to you is the use of social media?



VIRTUAL DATA ROOMS: SIMPLIFYING COMPLEXITY SWIFTLY

In the past decade VDRs have come to be seen as an important, if not critical, piece in the M&A due diligence process, essentially equipping practitioners with the digital platform and tools they need to swiftly, simply and securely analyse and interrogate complex deal data and documents.

“VDRs have made a big difference in terms of how the information is collated, distributed and reviewed,” says DLA Piper’s Kenworthy. “If I have a knotty issue and my colleague who will be best at dealing with it is in Hamburg, I can get them on the phone and we can look at it live on the screen and get a view. It’s a live and dynamic process. Information is uploaded to the data room every day so the review team is trying to hit a moving target. General disclosure of everything in the data room has become very common in European M&A meaning that the diligence team being organised, keeping on top of new documents and Q&A and making

sure the team has reviewed all the documents going into the data room is crucial.”

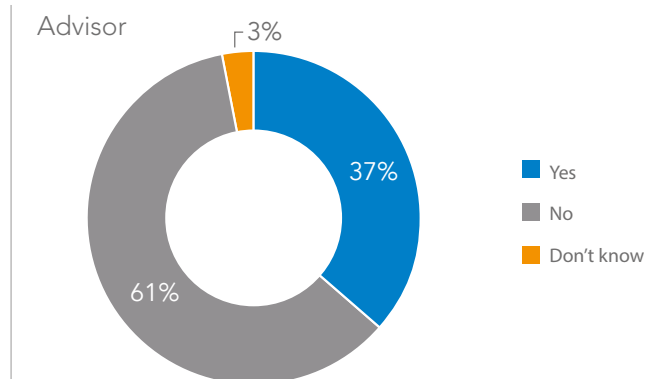
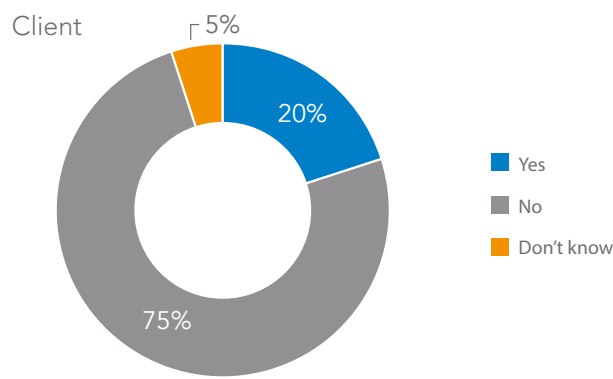
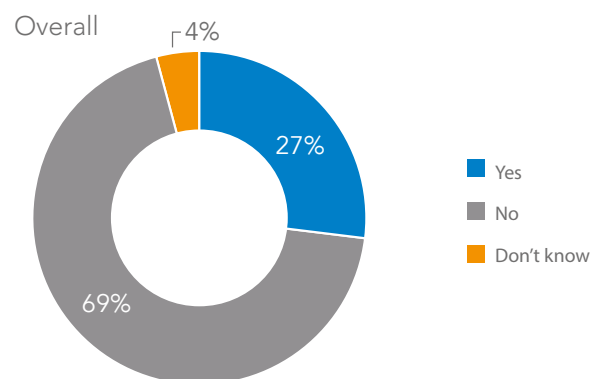
VDRs have arguably helped enhance due diligence more than any other technological innovation since Microsoft Excel. Over the next five years, the use and importance of VDRs will surely continue to grow as technological innovations continue apace. Indeed, soon will come a time when VDRs provide practitioners with the full suite of advanced AI and data analytics capabilities, which could in turn truly transform and propel the due diligence process.

In the meantime, many practitioners would like to see enhancements such as greater security through encryption and even facial recognition, as well as improved document search and analytics functionality, and better access to the VDR via multiple digital platforms, particularly smartphones.

The use of VDRs today may not be widespread in EMEA – some 27% of practitioners overall say they have used one before, most of which being investment banking, legal and accounting advisers – but the trend is upwards. Continuous innovation around service and technological capabilities will only support usage growth among advisers and their corporate and private equity clients.

“People are expecting technology to support them far more effectively than historically. It’s very much being driven through technological capabilities and being able to create real efficiency in the process. People are looking for improved speed and efficiency through the whole cycle,” says Hilary London, general manager, EMEA, Merrill Corporation.

Q18. Have you used a Virtual Deal or Data Room before?



Harnessing AI's power

Competition is driving law firms to explore ways of delivering services of the same - or even higher - quality, faster and more cheaply. "Technology that is available today is greatly improving the speed at which we can do a due diligence exercise and deliver our service at a lower cost," says Melissa Fogarty, joint head of corporate at Clifford Chance. "We make sure we are using the appropriate resource for the work that is being done at the right price point."

This means offering a broader spectrum of resources at both the premium and commodity ends of the spectrum. Clifford Chance recently acquired an office in Newcastle, northern England, bringing in a large pool of paralegals and, crucially, expertise in process management. The firm was an early adopter of AI. "At first some were cynical that this could be in any way additive, but already AI is delivering efficiencies and saving money for everyone through process improvement. There is no doubt that it will develop into something even better," says Fogarty.

Clifford Chance is one of a number of law and professional services firms working with US technology start-up, Kira

Systems, to explore and use AI in due diligence. Specifically, Kira is a machine learning software that identifies, extracts, and analyses text in legal contracts and other documents. The software is already pre-trained to find specific provisions in a due diligence review – from assignment and pricing to change of control and exclusivity/non-compete clauses – but can also be customised and trained.

Fogarty says: "One of the key areas in M&A is to identify whether the deal triggers any change of control clauses that are detrimental to the target company. The technology today is very good at homing in on those. It is very good at finding the needle in the haystack, but then the lawyers have to look at the needle and decide whether it matters to the client, which is where the legal expertise comes in. There might be technology that can do that legal analysis in the future, but I am not sure one will emerge in the near future to replace humans because ultimately legal expertise is required to assess the implications for the client."



Melissa Fogarty

JOINT HEAD OF CORPORATE
CLIFFORD CHANCE

Headquartered in London, Clifford Chance LLP is a leading multinational law firm and one of the top 10 largest firms globally by annual revenues and number of lawyers.

SECTION 3

THE IMPACT OF SECURITY AND REGULATION ON DUE DILIGENCE

DATA SECURITY: CONSTANT RISK MANAGEMENT

CASE STUDY: SCHOTT

REGULATORY CHANGE: ASSESSING THE IMPACT OF GDPR

DATA HOSTING: LOCATION, LOCATION, LOCATION

CASE STUDY: 3 SEAS

DATA SECURITY: CONSTANT RISK MANAGEMENT

Data security has never been more of an important issue, having moved to the top of the political and corporate agenda in recent years.

But on whether the risk of a data or privacy breach has increased, decreased or stayed the same over the past five years, respondents across EMEA overall are broadly split. On taking a closer look, however, some striking differences emerge.

For instance, regionally most Europe based respondents (40%) believe the risk has decreased and significantly decreased, while most Nordic (43%), Middle East (38%) and Africa (37%) respondents believe the opposite – that it has increased and significantly increased. What's more, over half of the corporate and private equity respondents (52%) believe the risk has increased while most (35%) of their advisers –

investment banking, law and accounting firm respondents – believe it has decreased.

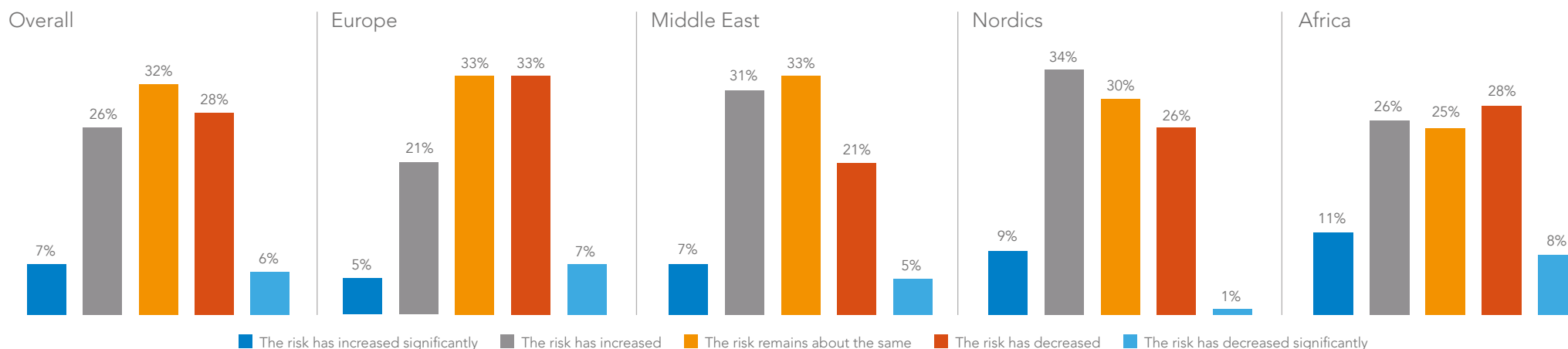
The risk is of course constant and continuously changing. The differences in the views of respondents seem to show this and perhaps the varying levels of success companies in different regions have in mitigating the risk.

“Data protection is critical,” says Drew Koecher, managing director and head of transaction advisory services at Houlihan Lokey. “In healthcare, for example, you have regulatory standards regarding confidential patient data where the consequences of a breach can be significant. Even where a business such as a low-tech manufacturer or distributor may hold less sensitive data, you still have to remain vigilant and mindful of data protection regulations,”

“In healthcare, for example, you have confidential patient data and the consequences of a breach or leak will be very significant.”

DREW KOECHER, MANAGING DIRECTOR
AND HEAD OF TRANSACTIONS ADVISORY
SERVICES, HOULIHAN LOKEY

Q9. How has the risk of a data/privacy breach in the due diligence process changed over the past five years?



A focused understanding of targets

From its founding in Germany over 130 years ago, SCHOTT has grown into an international specialty glass and technical ceramic materials manufacturer with operations in 34 countries, 15,500 employees and sales of 2.05bn in 2017.

While much of the growth has come organically, cross-border M&A has played an important role in the company's rise to where it is today. Dealmaking is expected to help drive the company's future growth too and particularly in the US where it plans to expand its business through focused, strategic acquisitions. More specifically, SCHOTT is on the hunt for US companies, with sales up to around \$175m, operating in areas including pharma and electronic packaging, optical components and materials, lighting components and solutions, glass powder and fibre. The ambition is to strengthen its sales in what is already a strong, fast-growing market for the company.

For all the benefits cross-border M&A can deliver, it can present challenges too. In 2008, for instance, SCHOTT acquired a majority stake in Moritex, a Tokyo-listed manufacturing technology company. "They didn't disclose much data and due diligence was limited," says director of M&A Alexander Becker, who joined SCHOTT in 2013 after starting his career in investment banking at Citi and advisory boutique Doertenbach & Co in Frankfurt. "On the face of it,

they were a machine vision company that we could well integrate with our lighting and imaging business, but we overestimated their competence in LED technology and the strategic fit with our operations. What we bought was different from what we thought it was." The Moritex stake was sold in 2014.

Lessons have been learned. Achieving a full and clear understanding of the target company in the due diligence process is critical.

"We focus on the commercial due diligence," says Becker. "Obviously, we still do detailed financial, legal, environmental, and IT due diligence, but for us the key point is about understanding what a company actually offers, how they manufacture it, how their processes are structured and what, from a corporate perspective, we can learn from them. Apart from challenges, digitisation and the increase of data offer also great opportunities. It allows for a much more careful analysis if you ask the right questions. We have applied this approach successfully on various acquisitions projects in the last years, always having in mind how we can integrate the company post-merger."



Alexander Becker

DIRECTOR OF M&A
SCHOTT

SCHOTT is a leading international technology group in the areas of specialty glass and glass-ceramics products for the home appliance, pharma, electronics, optics, life sciences, automotive and aviation industries. The parent company, SCHOTT AG, has its headquarters in Germany and is solely owned by the Carl Zeiss Foundation.

REGULATORY CHANGE: ASSESSING THE IMPACT OF GDPR

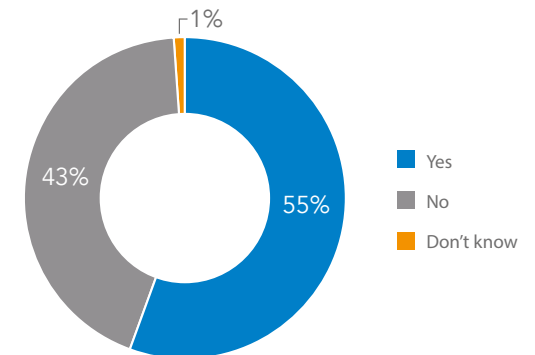
In May 2018 the European Union's General Data Protection Regulation (GDPR) came into effect. As well as containing stringent provisions on the sharing of personal data and the threat of substantial fines for companies that breach the new rules, GDPR has sharply focused attention on data protection issues in M&A.

Indeed nearly two-thirds (66%) of respondents across EMEA overall expect that GDPR will increase acquirers' scrutiny of the data protection policies and processes of target companies, and more than half (54%) said they had already worked on transactions that did not progress because of concerns around a target's data protection policies and compliance with GDPR.

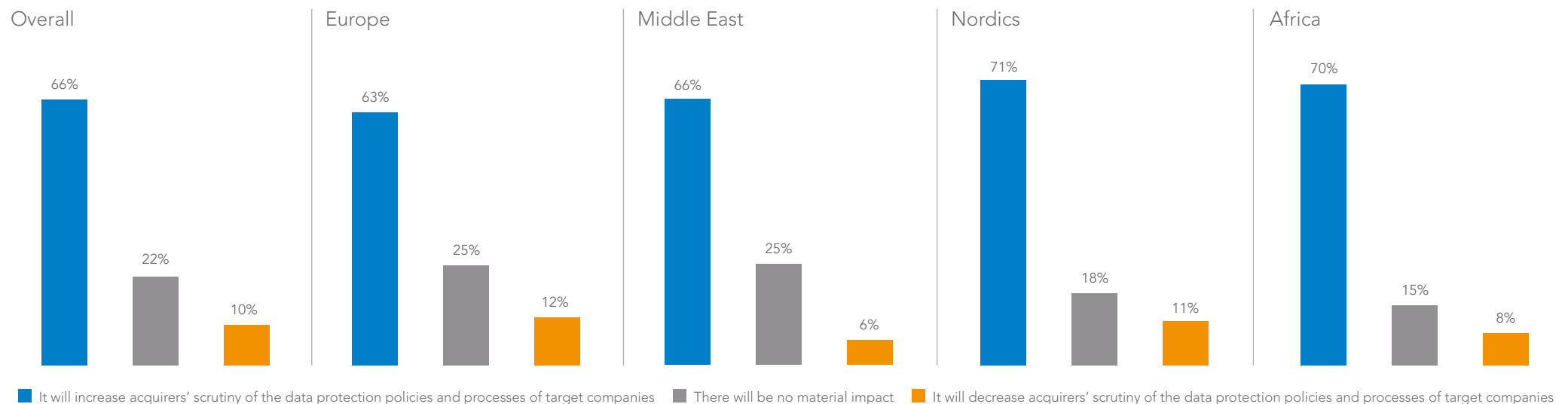
However, while most do believe GDPR will have an impact on M&A due diligence, some 22% of respondents overall believe it will have no impact at all, including 25% of Europe and Middle East based respondents – the highest percentage of the four key regions.

"Data security and privacy are a real issue. We take it very, very seriously. On the vast majority of deals we sign up to confidentiality clauses, non-disclosure agreements and our engagement letters have very clear wording around use of data, which we've updated to capture GDPR rules. We recognise that there are very serious reputational risk around data," says Matt Henderson, transaction services partner at Deloitte.

Q12. Have you worked on M&A transactions that have not progressed because of concerns around a target company's data/privacy protections and compliance with GDPR?



Q11. In the next five years what impact do you expect the EU's General Data Protection Regulation (GDPR) to have on M&A due diligence?



DATA HOSTING: LOCATION, LOCATION, LOCATION

Where transaction data is hosted may be seen as a procedural issue, but it is important to the due diligence process according to 87% of respondents overall.

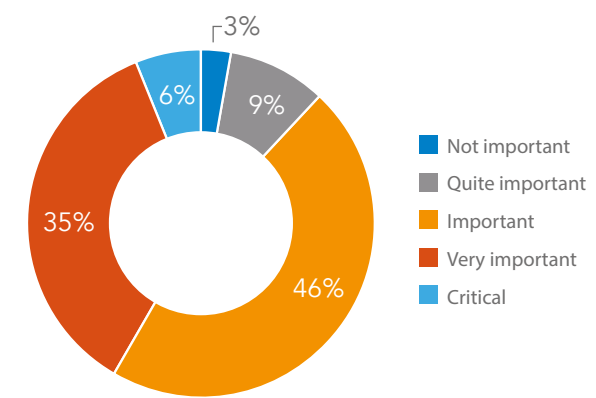
Asked what geography is preferred to host the data, and most respondents (47%) said in the country of the transaction, with 26% expressing no preference and 18% stating the EU.

“What matters is the speed of access and stability of the [data hosting] platform,” says DLA Piper’s Kenworthy. “If it’s quick enough no one cares where the data is hosted, but if it is not quick enough that is often because the data room is a long way away.” Interestingly, professional M&A advisers are markedly keener on hosting data in the EU (24%) than their clients

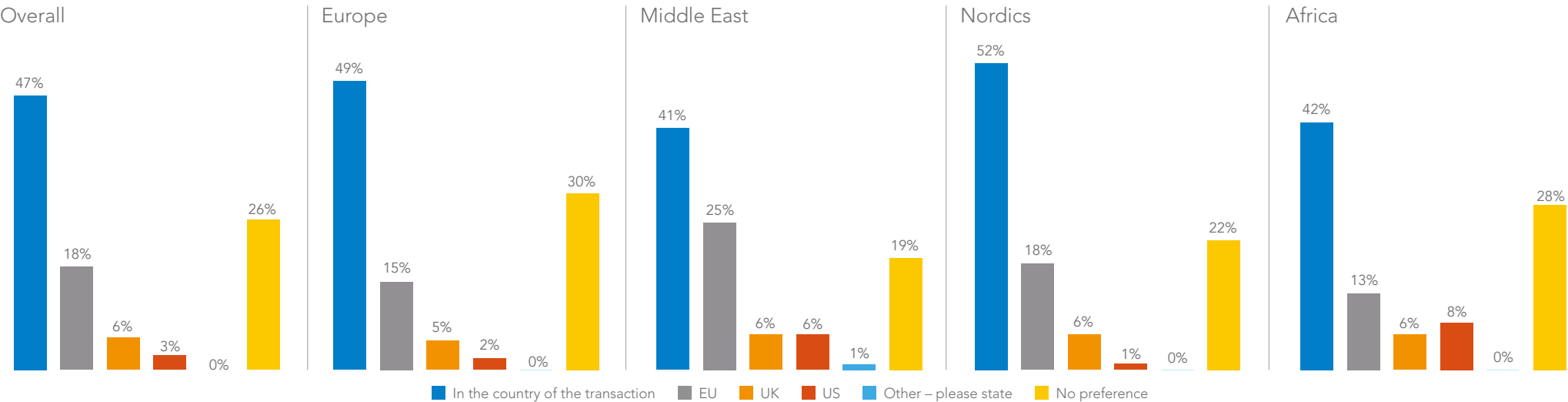
(13%). With customer bases – and hence valuable, sensitive data – increasingly international the most effective way of reducing risk is to comply with the highest standards of data protection, which are currently in the EU and specifically countries such as Germany.

“There are challenges around differing data protection laws in different jurisdictions, with certain markets having far stronger and more stringent rules. For example, how will Brexit impact a company that stores its data in the UK but is doing business or a transaction with a company in Europe? We put our data centre in Germany because they have the most stringent rules,” says Merrill Corporation’s Hilary London.

Q13. In your experience, how important to the due diligence process is the location where the seller’s transaction data is hosted?



Q14. Of the following regions, which is the preferred geography to host transaction data?



The changing face of due diligence

Istanbul-based 3 Seas Capital Partners represents something of a victory for small, independent players in M&A advisory.

No other firm has advised on more deals in Turkey over the past 10 years than 3 Seas, which is no mean feat considering there is competition in the market from the big US investment banks, global professional services firms and local banking powerhouses.

Across industries – from industrials and logistics to financials, energy, healthcare and technology – 3 Seas has advised large and small companies and private equity firms on over 100 successful M&A transactions, and many more besides that did not complete.

For Tarik Şarlıgil, managing partner at 3 Seas, there have been many M&A trends to have emerged, not least in due diligence.

Interestingly, he sees the opposite trend to that which is playing out in Europe. “Due diligence is taking longer,” he says. “Before 2009 due diligence was a risk assessment of the accuracy of the numbers and a check on tax and legal liabilities. Now buyers want to know about the viability and sustainability of the business model and market.”

Private equity investors in Turkey have particularly demanding information requirements, with corporates finding it easier to get comfortable with the unknowns. The quality of available data is improving and now it is rare for companies to have two sets of accounts, while an amnesty has helped eliminate historical risk of tax liabilities in most situations.

Şarlıgil is, however, optimistic that due diligence in Turkey can accelerate, and for good reason. “I think due diligence will speed up because, as companies grow and regulations tighten, the amount of risk associated with balance sheets has diminished significantly over the last ten years,” he says.

That is a positive development. But while it is beneficial to due diligence, Şarlıgil says the interrogation of a target doesn't always determine whether a deal succeeds or fails. “Buyers in Turkey pay close attention to a company's performance during the due diligence phase. We've worked on around 3-400 transactions in Turkey, including 2-300 that didn't close. I can only count a handful that didn't close because of due diligence. More often it has been because companies have not been able to reach their targets during the due diligence period.”



Tarik Şarlıgil

MANAGING PARTNER
3 SEAS CAPITAL PARTNERS

Founded in 2003, 3 Seas Capital is an independent M&A advisory firm. Since 2008 it has been the leading M&A adviser in Turkey by the number of completed deals. The firm has advised on over 100 successful M&A transactions.

CONCLUSION

Advances in technology have without doubt made M&A due diligence faster, more accurate and secure today than it has been in the past. The question we wanted to explore is what does due diligence look like five years' time?

What we found is that M&A practitioners across Europe, the Middle East and Africa not only believe due diligence will accelerate to 2022, they also believe advances in technology will bring even greater analytical capability, accuracy, security and simplicity to the entire process.

This is the view overall across EMEA and among M&A practitioners from corporates and private equity firms to investment banks, law and accounting firms. Indeed, there was much similarity across all their views, but there were some key differences in certain areas too.

For instance, practitioners in Europe and the Nordics give far greater importance to the use of social media in due diligence than their Middle East and Africa based peers. What's more, practitioners overall are split on whether the risk of a data breach has increased or decreased, and a quarter of Europe and Middle East based practitioners believe there will be no impact on due diligence from the EU's GDPR.

Yet overall, practitioners across EMEA are united in their view of the future of due diligence and the important role technology can play.

They see technology solving some of their biggest challenges – from reviewing and analysing contract text to visualising financial performance data – and place greatest hope in AI and data analytics to help them do so.

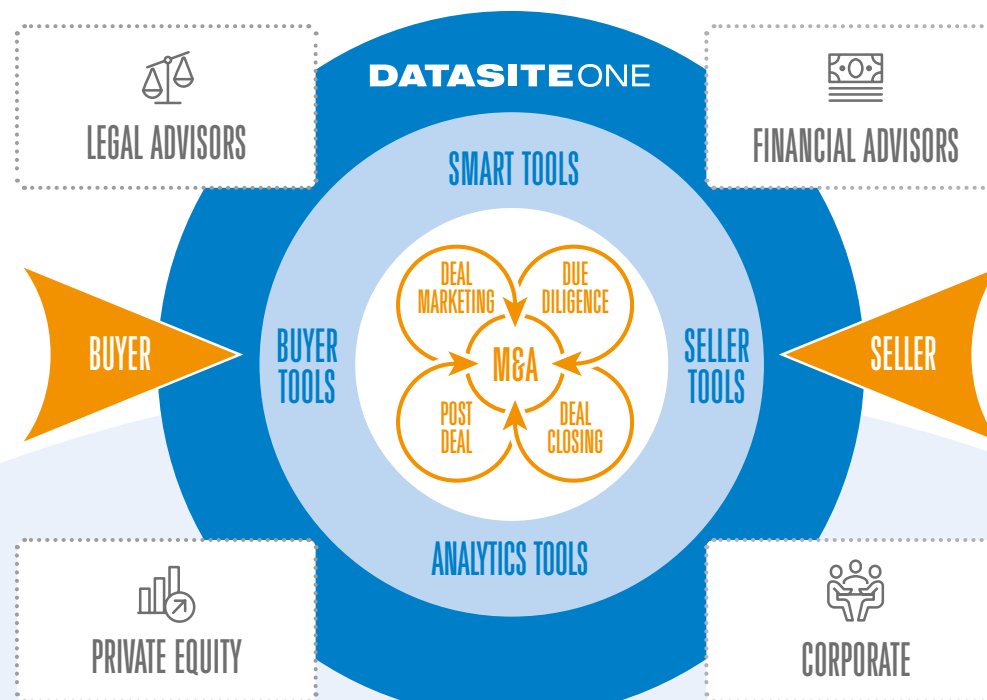
In fact, practitioners believe that these technologies will help accelerate due diligence the most in the short-run, and will have the most transformative impact over the long-term.

To be sure, VDRs – arguably the biggest advance in M&A due diligence in the past decade or more – and even blockchain are seen as playing an important role too. The reality is that a combination of these digital technologies, together with and led by human experience and expertise, will most likely transform due diligence and M&A over the coming years.

Recommendations

- 1 Technology is driving changes across all stages of the due diligence process and can no longer be ignored when it comes to successful M&A. Enhancing your productivity and speed using AI, machine learning, analytics, redaction and other smart tools and technologies can easily be achieved by selecting an application for due diligence that fully supports the digitised due diligence process.
- 2 Gain a competitive advantage by generating advanced analytics and insights via secure, flexible, algorithm-based reports and dashboards to drive better, faster decisions throughout the due diligence process.
- 3 Deals have been cancelled because of data privacy issues. Ensuring your application for due diligence is fully compliant with international and local regulations as well as the country where your data is hosted, gives you the flexibility and security you need to conclude your due diligence process successfully.

MERRILL DATASITEONE VISION



Merrill DatasiteOne is on the journey to bring relevant innovations and technologies under one platform to enrich the due diligence process

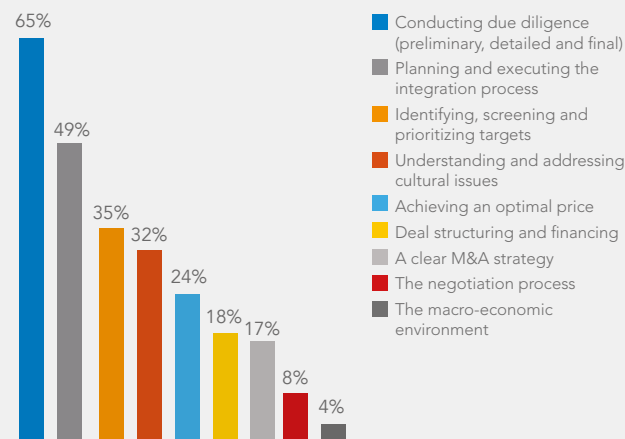
Drive efficiency, productivity and velocity within the due diligence process by adding Analytics, Automation, AI and Machine Learning (Intelligent Due Diligence)

Extend the value add to the different stages of the M&A process from deal marketing to due diligence, to deal closing and post deal integration (Intelligent M&A)

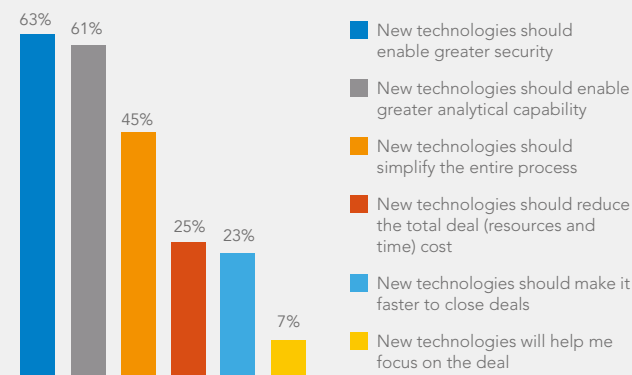
Build an M&A ecosystem that brings together the best deal makers, advisors, buyers and sellers with deep market data and deal insight

APPENDIX

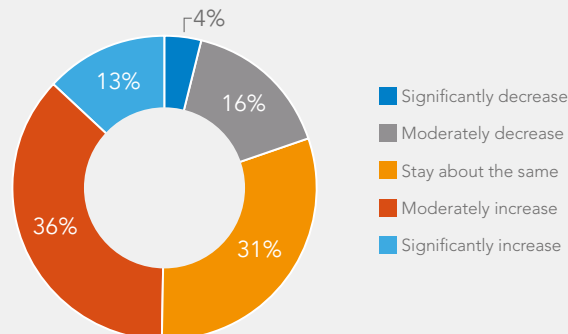
Q1. What are the three most important success factors in M&A? (Select up to three)



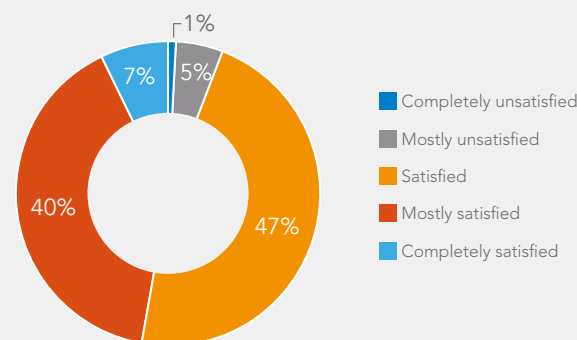
Q2. In the context of a M&A transaction, how do you expect technology to change the due diligence process over the next five years (to 2022)? (Select up to three)



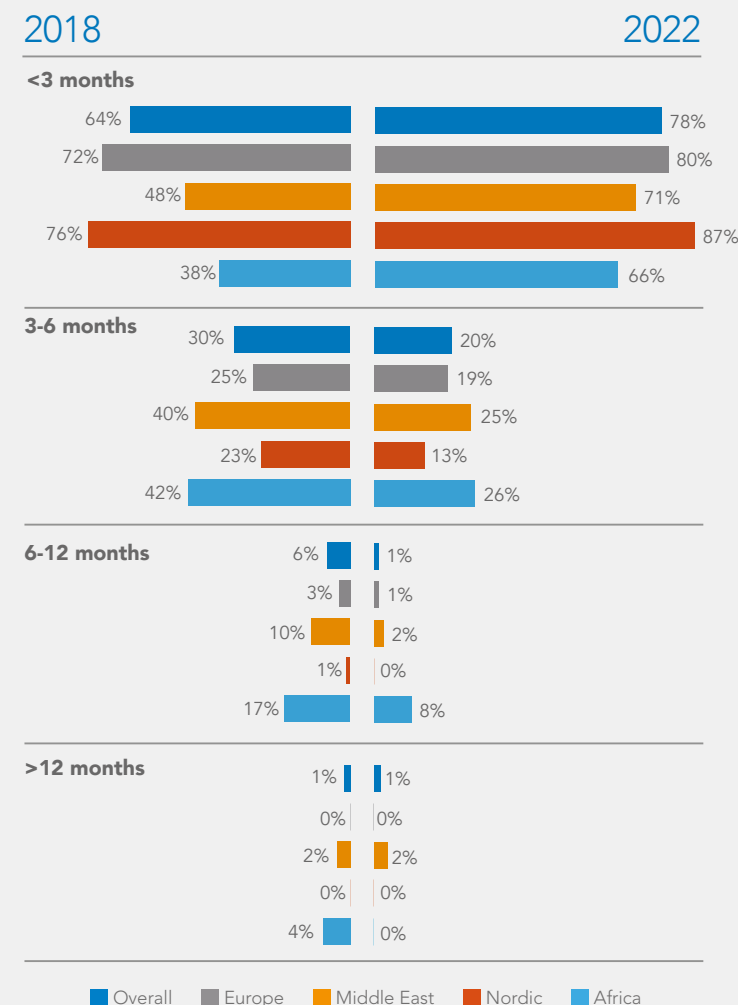
Q3. In the next five years, how do you expect the use of technology in due diligence to impact the number of people involved in a M&A transaction compared to today?



Q4. Based on your personal experience, how satisfied are you with the speed of the due diligence process?

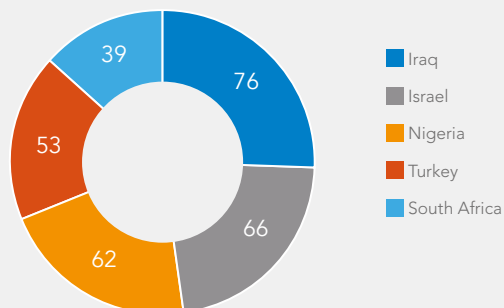


Q5. From sourcing a deal to deal completion, how much time on average does due diligence take on a single successful M&A transaction, and how much time will it take in five years (2022)?



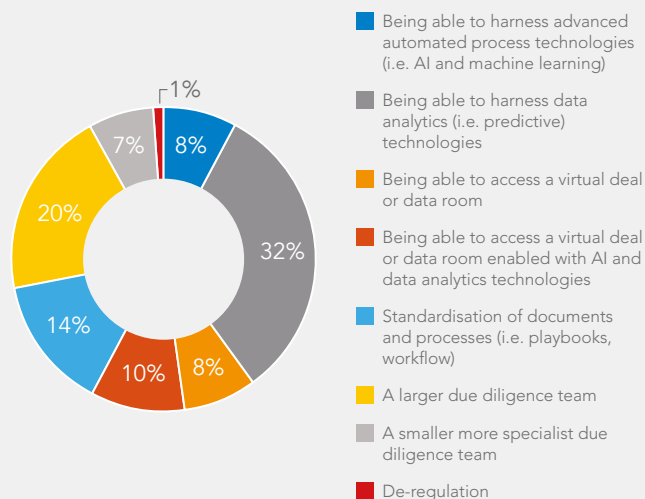
APPENDIX

Q7. In which country of Europe, the Middle East and Africa is due diligence on companies most challenging and time-intensive?

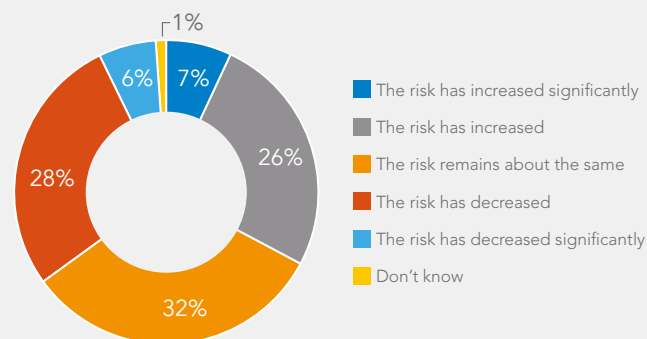


(Respondents were asked to list top three countries. The ranking is based on an aggregated score which is calculated by adding the number of points each country receives)

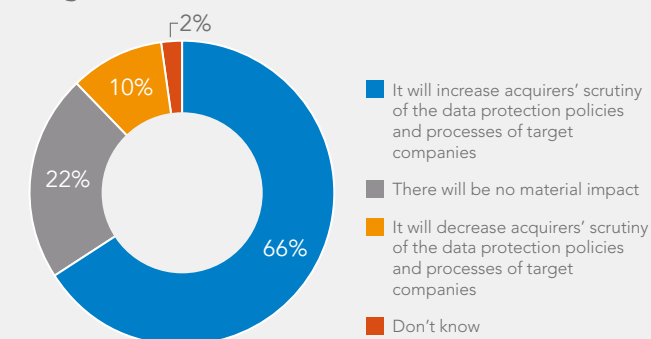
Q8. What would help accelerate the due diligence process the most?



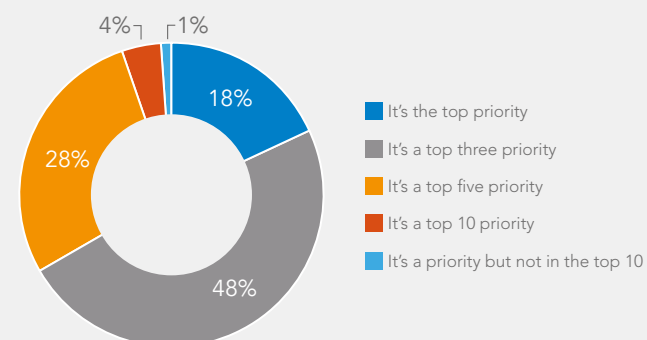
Q9. How has the risk of a data/privacy breach in the due diligence process changed over the past five years?



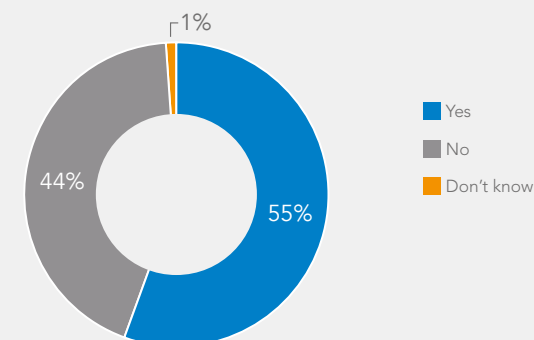
Q11. In the next five years what impact do you expect the EU's General Data Protection Regulation (GDPR) to have on M&A due diligence?



Q10. To what extent is data security a priority in the due diligence process?

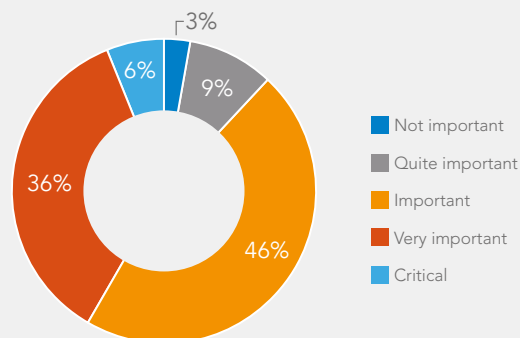


Q12. Have you worked on M&A transactions that have not progressed because of concerns around a target company's data/privacy protections and compliance with GDPR?

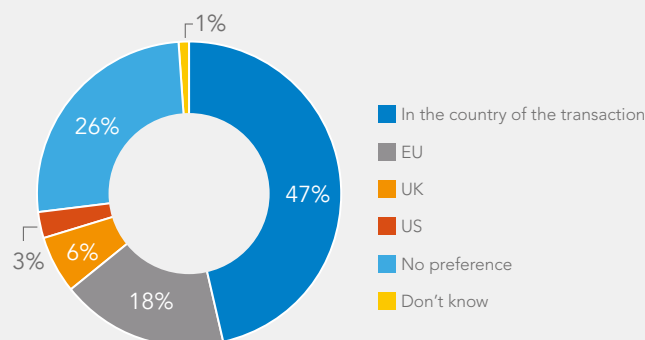


APPENDIX

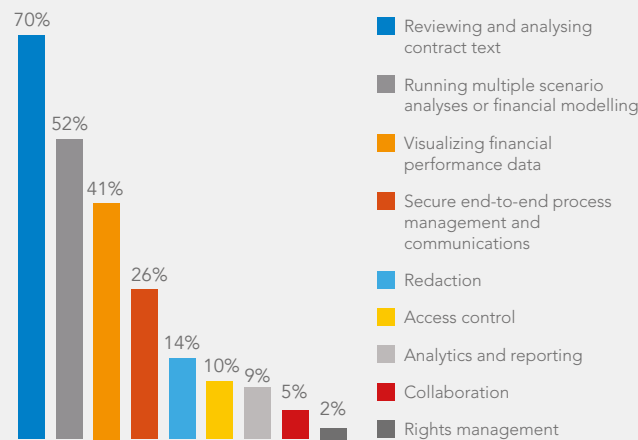
Q13. In your experience, how important to the due diligence process is the location where the seller's transaction data is hosted?



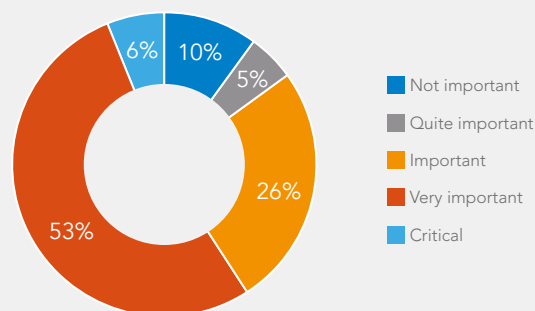
Q14. Of the following regions, which is the preferred geography to host transaction data?



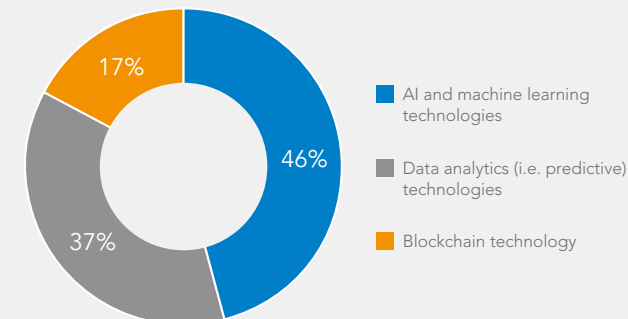
Q15. What are the biggest challenges in due diligence that you believe technology could provide a solution for? (Select up to three):



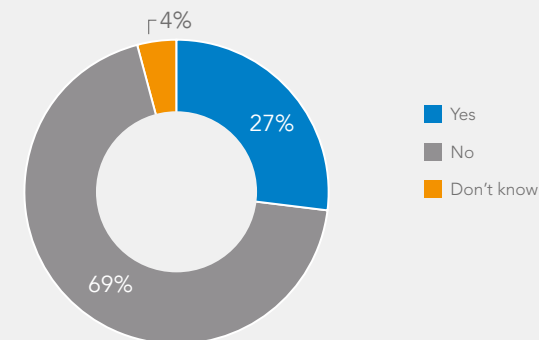
Q16. As part of the due diligence process (i.e. assessing potential targets, customer perception analysis), how important to you is the use of social media?



Q17. Which of the following technologies do you see as potentially having the most transformative impact on M&A due diligence over the long-term?



Q18. Have you used a Virtual Deal or Data Room before?



ABOUT MERRILL CORPORATION

Merrill Corporation is a global leader in SaaS solutions for M&A, communications and secure business collaboration. Clients trust Merrill's innovative applications, excellent customer service and deep subject expertise to successfully navigate the secure sharing of their most sensitive content. Their flagship product, DatasiteOne, helps users in over 170 countries close more deals, faster.

EMEA +44 (0)20 3031 6300 US 888.311.4100 APAC +852 2536 2288

email info@merrillcorp.com web merrillcorp.com

Produced by: Euromoney Thought Leadership Consulting

Writer: Grant Murgatroyd

© Merrill Communications LLC. All rights reserved. All trademarks are property of their respective owners.



#DatasiteOne