M&A in Portugal after Covid: what’s next

Back to Corporate and M&A Law Committee publications (/LPD/Corporate_Law_Section/Corporate_MA_Law_Committee/Default.aspx)

Manuel Santos Vitor
Abreu Advogados, Lisbon
manuel.s.vitor@abreuadvogados.com (mailto:manuel.s.vitor@abreuadvogados.com)

Cláudia Santos Malaquias
Abreu Advogados, Lisbon
claudia.s.malaquias@abreuadvogados.com (mailto:claudia.s.malaquias@abreuadvogados.com)

Upcoming trends in the M&A market: the post-pandemic reopening

> ‘The times, they are a-changin’.

Surely you have heard or used this famous expression more than once. Yet, it is safe to say that no one could predict the gigantic change that 2020 would bring to the world, society, individuals and, consequently, to all types of relationships between them.

Human relations *per se* aside, the Covid-19 pandemic had a huge impact on the Portuguese and worldwide M&A markets during 2020. M&A markets went through a bit of everything thanks to the coronavirus outbreak: transactions were immediately cancelled, others were suspended and resumed several months later, and others simply dragged on. The lack of regular mobility and physical contact had an impact and created an absence of the necessary confidence that needs to be built between the players involved in M&A transactions for them to take place. In the end, everything just got a lot harder and slower.

All of this led to fewer transactions taking place worldwide, at least until the last quarter of the year. In fact, 2020 ended with strong positive signals in the M&A sector, with a significant number of transactions taking place. This was a period in which the pandemic had less of an impact and a time when companies, banks and consultants had already been able to somewhat adapt to the ‘new normal’. Indeed, globally 2020 showed a higher transactional value than in the previous year, as the fewer transactions that did take place closed for very significant values.

More than a year since the outbreak began, we now know that certain Portuguese sectors continued to operate within levels of a certain normality and that activity even improved in certain areas. According to publicly available information, the sectors with the most M&A transactions in Portugal in 2020 were:

- real estate;
- financial and insurance;
- health; and
- technology.

In the first two months of 2021, the most dynamic sectors appear to continue to be these four, plus retail and modern distribution.

However, these exceptions – where things went well or almost well – were far from the rule. In most sectors, activities were suspended or significantly reduced. Companies – many of them small and medium-sized businesses (SMEs) or micro-enterprises, often family-owned and unsophisticated when it comes to M&A – were severely affected. Many became insolvent or pre-insolvent, clinging to 'life supports' such as credit moratoriums and the scarce financial support from the state that was made available, mostly in the form of furlough programmes.

2021 began in Portugal with the country in a period of lockdown. However, if everything goes according to plan, this ongoing confinement will cease in several weeks and stages, the rate of vaccination will accelerate and, by summer, the economy will have resumed a certain normality, generating greater confidence in companies, investors and sellers. In fact, looking back at 2020, the recovery of the M&A sector was almost immediate each time there was an opening of the economy.

We optimistically anticipate that 2021 will be better for Portuguese and worldwide economies – and the M&A sector in particular – when compared to 2020 but the difficulties that surfaced in 2020 will remain, even if with a more limited impact. For this to happen, states and political decision makers have to understand that these are times in which full and unconditional support to the economy and the private sector are necessary, with a view to facilitate and help, and not to complicate or hinder market opportunities.

Governments cannot forget that private companies are the entities generating wealth, employment, economic growth and paying taxes and that they should let them normalise their activities and grow.

What's next in the Portuguese M&A market?

The 'bazooka': the Recovery and Resilience Plan and its impact on the M&A sector

Portugal, like other EU Member States, will receive a flow of community funds at an extraordinary and unrepeatable level: the so-called EU Recovery and Resilience Plan, aka the 'bazooka'.

As we become more aware of the 'bazooka' plan – though we still know too little – we realise that the most significant part of the funds will be injected directly into the Portuguese state sector and into public administration, and not so much into private companies or players. The EU support plan was drawn and designed in that way, even though there is a certain margin of discretion for each Member State to aim its own bazooka.

Even so, the massive injection of funds into the public economy should lead to greater public investments, such as in services, equipment and innovative tools required for the increase of digital qualification, energy and climate transition, decarbonisation of the economy, strengthening of the health system and so on. Those investments will then naturally lead to increased opportunities for the private economy in such areas.

Companies that manage to (1) have access to funds directed to the private economy and/or (2) participate in the flow of funds to the public economy (either in Portugal or in other European countries) will then be under the M&A sector's radar. They will certainly become interesting targets for investment by foreign players who either already have know-how and a track record in the abovementioned areas or who wish to establish or strengthen their presence in Portugal to have a more expedite access to and benefit from the Portuguese 'bazooka'.

Moreover, Portuguese companies have here a unique opportunity to grow outside the country's borders, either by joining forces with others to access other Member State bazookas or by building up their presence in such markets. We have already seen interesting signs of Portuguese investment in countries like Spain and France, for instance.

Which sectors will be the champions of M&A activity?

Portugal has always been a target for global or multinational companies attracted by the country's geographical location, weather and high quality of life, political and social stability, a reasonable taxation stability and an attractive legal framework for investment.

This was one of the reasons for a tourism boom in Portugal in recent years. In fact, sectors such as tourism, hotel and restaurant sectors were decisive in the growth of Portuguese economy and the recovery from the crisis of 2011–2014. Companies in sectors such as agribusiness, logistics, transport, services, finance and construction also benefited from such growth – a reason why the M&A activity in such sectors saw a significant increase in the last few years in the country.

Energy, particularly renewable energies, technological companies, technology, media and telecoms (TMT), exporting companies, retail, the agribusiness sector, commercial areas and logistics, were also some of the most dynamic sectors in regards to M&A transactions in Portugal between 2015 and 2019. Yet, those were precisely some of the sectors that suffered the most and received very little support during the pandemic from the Portuguese state. These sectors are therefore eager for private investments in order to allow a somewhat more instant recovery and growth.

The recovery of the worldwide economy, particularly of the many countries that are strategic for the Portuguese market, will be decisive for the recovery of the Portuguese economy. Such joint growth will be crucial for Portuguese enterprises that sell and export products or services to foreign markets, as well as for those that are already part of international and global groups also established in strategic foreign markets.

For obvious reasons, the Portuguese economy is and will continue to be a small open economy, very sensitive to what happens in the global markets. The good news is that some countries are very used to investing in Portugal and are expected to continue to do so, especially EU Member States.

The most striking example is Spain. The interconnection of Portuguese and Spanish economies is enormous, as is the presence of Spanish companies in Portugal, and many global companies treat their Iberian businesses in an integrated way. Thus, the recovery of the Spanish economy will be important for new investments to take place in Portugal not only by Spanish companies, but also by other foreign companies that intend to establish a presence or strengthen their position in the Iberian Peninsula. For this reason, it is reasonable to anticipate that Portugal and Spain will continue the existing dynamic between the two economies, especially in sectors that already have a significant flow of foreign investment, mature sectors and/or with assets that ensure long-term profitability.

We also hope to see more investments from other institutional investors that have been interested in the Portuguese economy for quite some time, such as pension funds from economies as different as Australia, Canada and the United Kingdom.

Other target sectors: the strengthening of the Portuguese health system and decarbonisation of the transport system

There is a current political and social consensus on the need to strengthen the Portuguese health system, which has been weakened by consecutive public strategies to reduce investment. This is evident in the low levels of operation affected by the lack of means, infrastructure, equipment and, in general, qualification. There is the expectation that the state will invest significantly in the National Health Service, as well as support complementary means of private medicine (for example hospitals and clinics) and the pharmaceutical sector.

The public and private transport system is also one of the most sensitive sectors in the Portuguese economy. Portugal is currently waiting for the announced national railway plan as an alternative to short-distance air transport and road transport, which will allow the strengthening of connections within the territory and between Portugal and other European countries. Such consolidation will of course reinforce mobility and facilitate cargo transportation logistics (goods, equipment) and their export (and obviously import) and is essential for the decarbonisation of the transport sector and for the Portuguese economy.

With all this happening, companies that are players in the health and transport sectors will certainly grow and become natural targets of M&A transactions. Given the difficulties most Portuguese companies have been facing since the outbreak of the pandemic, there will be interesting investment opportunities for those wishing to enter into the Portuguese market or to strengthen their position in the country.

What can be done to boost the M&A market?

The severe impact of the coronavirus pandemic in the Portuguese and global economy will not be solved overnight. Economies will slowly recover and open gradually to players keen to benefit from the investment opportunities raised by the crisis.

State aid to enterprises is essential for a steady recovery of the Portuguese economy. The levels of indebtedness have grown significantly and many companies have benefited from formal or informal moratoria, as well as from the tolerance of many creditors (particularly banks), who are now starting to receive payments – or who cannot wait much longer to be paid. Even so, moratoria are likely to be maintained for a considerable period of time and be gradually reduced. Two interests must therefore be taken into consideration: to support those benefiting from moratoria but also the respective creditors.

Bearing this in mind, the Portuguese government has publicly announced that it is analysing, and has already proposed to the European Commission, the approval of mechanisms that would allow the state to boost the economy through the reinforcement of companies' capital (equity or quasi-equity).

The government has also decided to move forward with the formalisation of the state-owned development bank (*Banco de Fomento*) that will support and be the vehicle (or the main vehicle) used in such public investment in the private economy.

From a private perspective, enterprises must adjust themselves to the 'new normal' imposed by the coronavirus. Even though the pandemic swept away many of the artificial barriers to live and transact online, enterprises will have to invest in new technology and personnel training to continue this new normal of virtually meeting, discussing, negotiating and closing transactions. This will certainly create interesting opportunities for businesses that already have the required know-how as to how to deal with this new normality.

Conclusions

Although we cannot anticipate how the Portuguese M&A sector will react in 2021, the last quarter of 2020 and the first quarter of 2021 show a positive evolution when compared with the first quarters of 2020, with an increase in the number of M&A transactions.

The need that the Portuguese economy has to grow, particularly in certain sectors, will certainly create very attractive M&A opportunities for players wishing to enter or reinforce their position in the national market. Players wishing to implement M&A transactions need to be prepared and organised to deal with a volatile and online market, surround themselves with legal, technical and financial consultants, become familiar with the new normality of processes and adjust their expectations to the 'new normal'.

Similar topics

Business Human Rights (/Search/Taxonomy.aspx?Taxonomy=Business Human Rights&TaxonomyUid=39211378-f48e-47da-8e38-4ed739d99a8e)