

Business and financial services M&A in CEE in 2021 and beyond

While the pandemic hit deal volume in the sector, value increased on the back of a lucrative banking deal in Hungary. Meanwhile our survey shows optimism for post-COVID dealmaking

Business and financial services M&A deal volume in the region decreased by 14% in 2020 compared to 2019. On the other hand, deal value was up by 46% over the same period to €4.3bn, almost half of which was attributable to the €2bn acquisition by Magyar Takarekszovetkezeti Bank of Budapest Bank.

However, despite the volume drop, a 61% majority of respondents in our survey believe COVID-19 will increase dealmaking appetite in the sector, 15% of whom anticipate a significant increase.

"Financial regulators strongly encourage market consolidation in the financial sector in Slovenia, Croatia and Serbia, an approach also seen across Europe", says Natasa Lalovic, partner in Wolf Theiss' Belgrade office. "We have to expect an even stronger push for consolidation due to an increase of loan losses resulting from the pandemic."

Business and financial services M&A, 2013-2020



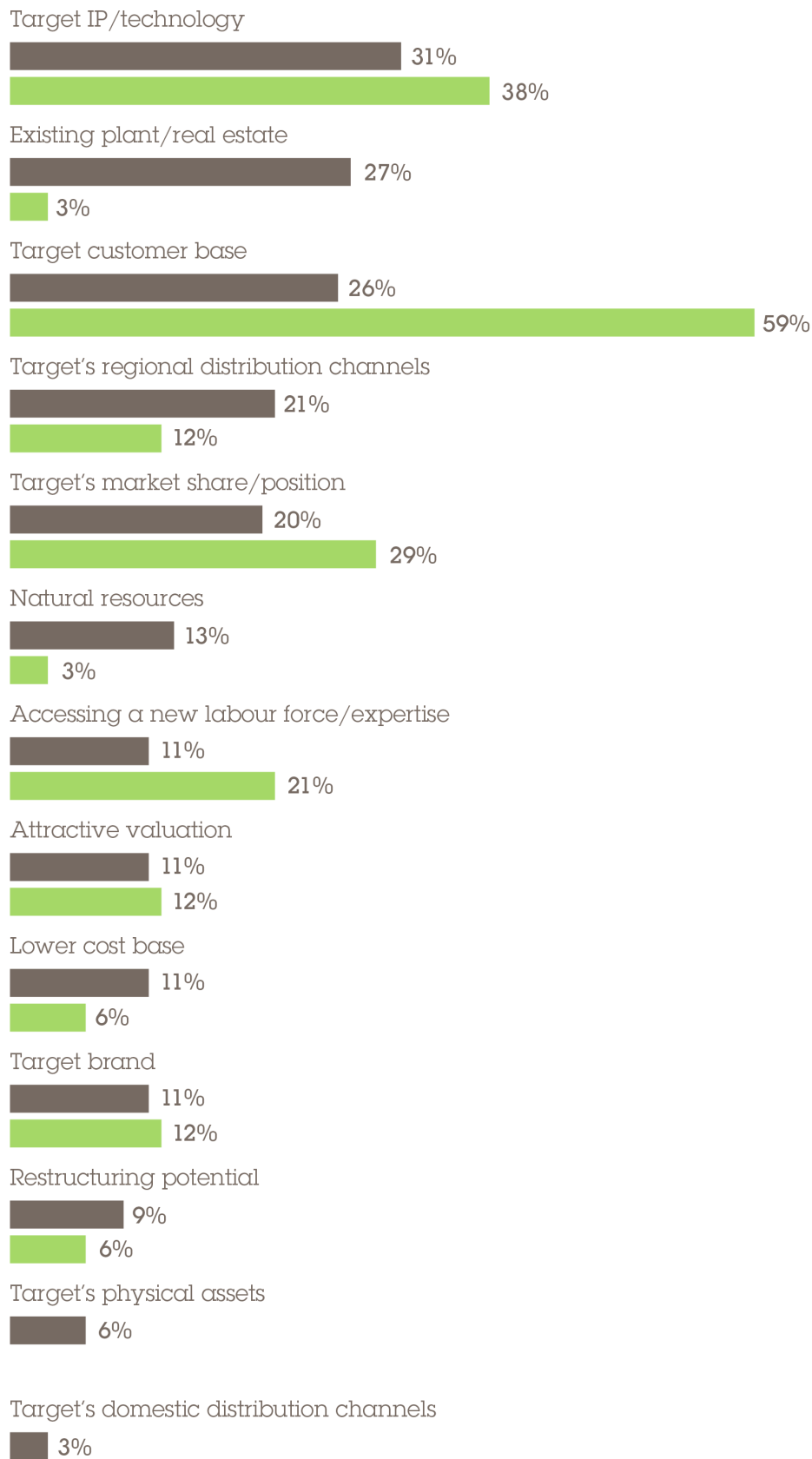
One area in which this is likely to occur is banking. CEE banks entered the COVID crisis in a strong capital position, with limited non-performing loans on their books. This relative strength stands them in good stead to weather the effects of the pandemic.

However, it is clear that the performance of credit portfolios will deteriorate over the next year as fiscal stimulus comes to an end and, once moratoria on loan enforcement are lifted, the true reality of the health crisis's impact on businesses will become visible. It should be expected that defaults will rise and banks' balance sheets will come under pressure, forcing them to seek deals and divestments to bolster their financial positions.

Customers and tech drive deals

Most commonly cited drivers for their next deal in the business and financial services sector are the target's customer base (59%) and the acquisition of IP/technology (38%). Acquiring customers is a tried and tested method of achieving growth that applies across all sectors.

What are/will be the main drivers for your next M&A deal in the CEE/SEE region?
(Select the top two)



■ Total ■ Business and financial services

Technology acquisition, however, is particularly relevant for financial services given its convergence with tech amid the fintech revolution. This has been supported by EU policymaking in the form of the Payment Services Directive 2 (PSD2), which came into force four years ago and requires incumbent lenders to provide APIs (application programming interfaces) so that fintech start-ups can access accounts and data to deliver products to benefit the consumer.

Facing higher competition from innovative young companies as a result of PSD2, banks have been compelled to either incubate innovation in partnership with start-ups or acquire them outright. Technology should continue to be a strong deal motivator for the foreseeable future, not only across CEE but the whole of Europe.

Consolidation on the cards

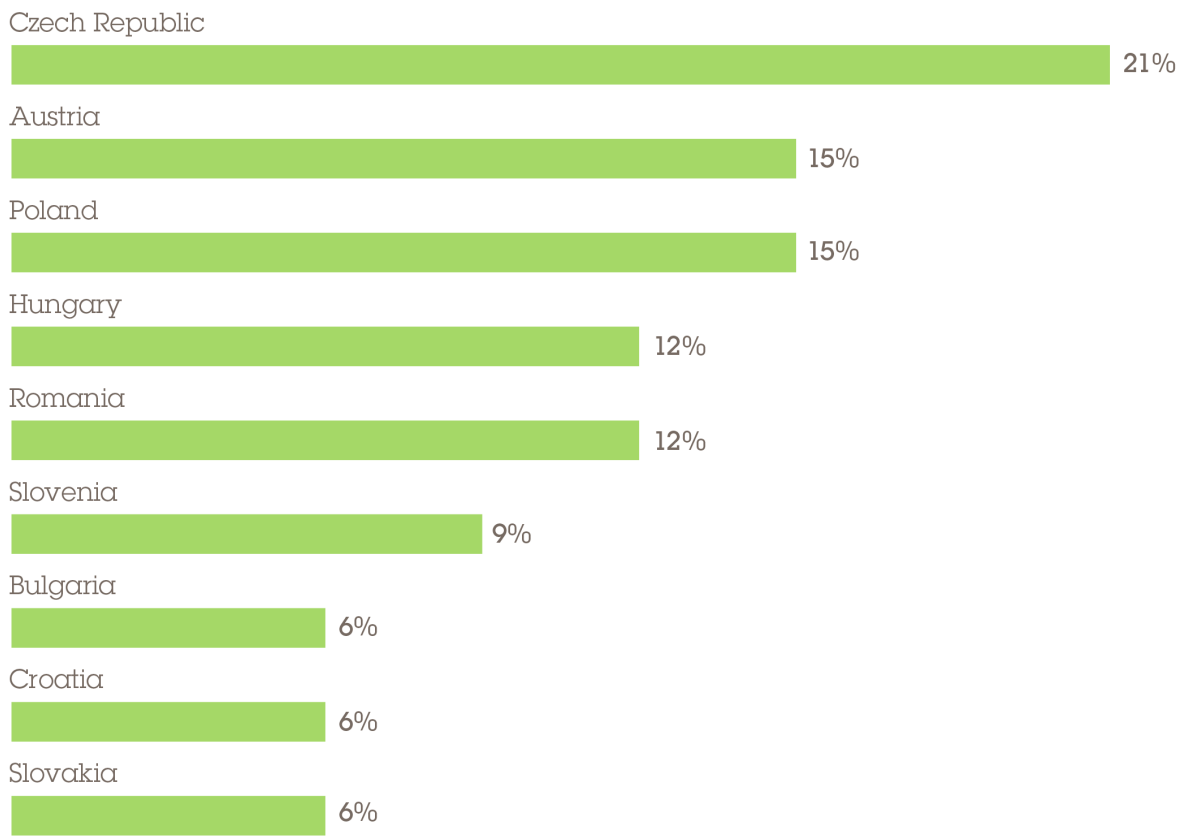
One unique factor for the region from a banking perspective is the headroom for consolidation. The largest three lenders in CEE – Erste Group, KBC Group and UniCredit Group – have a collective market share of less than 25%. The impact of the pandemic on the financial positions of these mid-cap players will almost certainly result in deal flow as they seek growth through scale and the restructuring of their loan books to become stronger, more competitive institutions.

Another source of activity has been the restructuring of large insurance groups. In 2020, AXA divested its CEE operations in Poland, the Czech Republic and Slovakia to Austria's UNIQA Insurance Group for €1bn, and Dutch insurer Aegon sold its regional business to Vienna Insurance Group for €830m. The pandemic is an inflection point at which multinationals have been forced to review what is core to their future business. Anything that is no longer strategically aligned represents a potential M&A opportunity for both PE and corporates committed to the region.

Business checks into the Czech Republic

Investors continue to look at the Czech Republic as a gateway for their next deal opportunity in the business and financial services sector. More than one in five (21%) also have the Czech Republic as their top national market, ahead of any other. The country has a lot going for it from a growth perspective, with around a fifth of the population without a bank account, the fourth-highest proportion across the EU. Romania, however, tops the table with as many as two in five Romanians being unbanked, leaving plenty of upside for growth.

For the most important sector for your next M&A deal in the CEE/SEE region, in which country are you currently looking for new opportunities? (Select most important)

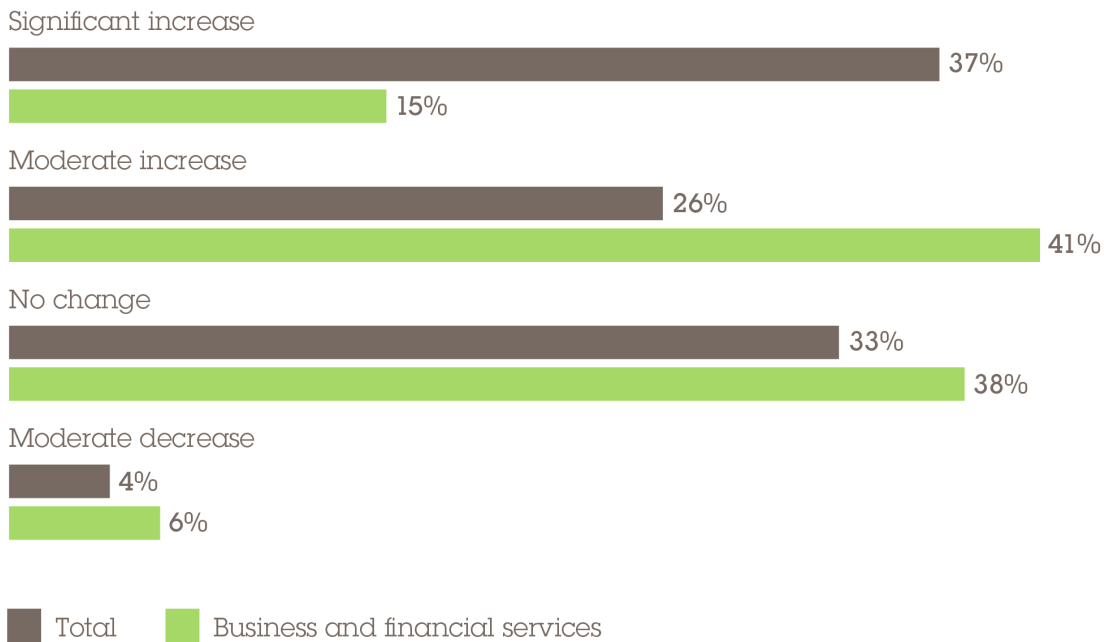


Notably, the Czech Republic has the highest GDP per capita of any country in Eastern Europe and is second only to Austria across CEE/SEE. This helps to explain why the country is the first choice for investors in the sector: 26% cited growth prospects and 24% pointed to GDP per capita as their key determinants for selecting which country to make their next business and financial services sector deal in.

ESG – not on the radar for services

For the first time in our survey, we examined ESG issues across the whole survey pool and within specific sectors. ESG issues do not impact services companies in the same way as heavy industry, extractive sectors or even consumer and only 15% of respondents expect ESG scrutiny to significantly increase in deals in the sector over the next three years. That is compared to 37% of all respondents.

How do you expect ESG scrutiny to change in deals over the next three years?



While the energy efficiency of operations and social factors are an important consideration, especially in light of the EU's push towards higher standards of integrated reporting for listed companies, the primary ESG consideration for banks is the environmental credentials of the businesses they lend to.

A bright future for M&A – pandemic permitting

CEE's highly fragmented financial services sector is ripe for consolidation and this will be a core M&A driver over the coming 12-24 months. The pandemic has only increased pressure on medium-sized banks to seek acquisitions to improve their financial strength.

Coupled with the need for retail lenders to digitise their offerings through tech-centric deals, there is high potential for elevated M&A in the sector amid the recovery. The ongoing review of operations by multinationals seeking to improve their balance sheets, as seen recently in the insurance space, could deliver further opportunities.