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Trends and Developments

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Trends and Developments

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Introduction

The year 2020 was indeed a peculiar year for the M&A market in Poland. The original assumptions and prognoses made in late 2019 or even at the beginning of 2020 had to be substantially revised when the COVID-19 pandemic hit Europe and, ultimately, Poland. Practically everyone was horrified then with what the new "flu" could bring about and how it might affect the market. There was a lot of fortune-telling (much more than usual) in M&A market prognoses released in March–April 2020. What did most of them have in common? Virtually all of them were wrong.

Not only did the M&A market fail to fall, but it actually grew. While it is always hard to rely on M&A statistics (as different sources tend to present different figures), it seems that the overall number of transactions in Poland grew by almost 30%! That sort of transactional activism might seem to be surprising, but as will be discussed, in fact it is not a surprise at all.

The Polish M&A market has prospered continuously over recent years. It has been one of the most active in Central & Eastern Europe, and has generated growth for a long time (in both deal number and value). This may not have been visible in every single sector, but with a certain oversimplification, on a macro scale it has applied to the whole economy.

Market Structure

In 2020, the market was continuously dominated by sector investors, who accounted for a vast majority of transactions, with PE funds awaking towards the year-end. It is difficult to indicate a single dominant sector, with the Polish M&A market being rather scattered, however, some kind of duality was observed. While some sectors were struggling to survive, in particular HoReCa, others thrived. There is no doubt that the broad media/IT/telecom/e-commerce/logistics sectors have been practically untouched by the effects of the pandemic, and even grown.

The growth of those sectors was reinforced by an increase in e-commerce itself. Thus, it accounted for a substantial portion of the market and also produced some of the top deals of the year. Second place was taken – also no surprise – by the financial services sector. Transactions in these sectors accounted for nearly a third of all M&A projects in 2020.

It was specifically in the second half of 2020 when a certain revival was observed in terms of both quantity and value of M&A transactions in Poland. This trend seems to be continuing, with the energy sector (in particular renewables) also gaining momentum through the first quarter of 2021 (when this article is being written) and (presumably) going forward. This is specifically attributed to the rather wide access to capital on the investors' side (specially PE).

The Implications of COVID-19

At first the coronavirus pandemic caused fear over its impact on deals recently completed or still being negotiated. It was believed that certain boilerplate provisions in M&A agreements, such as force majeure, might be commonly triggered, causing chaos and effectively jeopardising neatly sewn-up deals. Likewise, it raised concerns over occurrence of circumstances expressly provided for in contracts, particularly material adverse change or impact, typically giving the parties (or one of them) the ability to terminate the contract due to the worsening situation of the target (eg, a certain decline in turnover or increase in debt). There might have been individual instances where that did happen, but no general tendency was observed.

Categorical, universal conclusions cannot be drawn for either of these aspects of M&A projects. Just as the transaction agreements are drafted through a process of bilateral or multilateral negotiations, and thus greatly individualised, so the measures the parties should pursue in the current situation must be determined on a case-by-case basis. In certain instances, unilateral action may be considered to renounce the contract (eg, if the transaction has entirely lost its purpose for one of the parties), or modify the contract due to a change in circumstances. But it seems that most often the solution has been dialogue between the parties, seeking solutions through good-faith negotiations.

From the perspective of negotiation and drafting of transactional agreements (which can also be conducted remotely), it should nonetheless be borne in mind that concluding new contracts during a pandemic may in certain circumstances be regarded as imprudent and deprive the parties of protection in the future (as we write here). Thus it cannot be excluded that the other party will allege that a rational undertaking concluding a contract during a pandemic must foresee difficulties related to the current situation and take them into account when incurring new obligations, to ensure that they can be performed.

Thus, in contracts currently being negotiated, provisions should be included addressing potential inability to perform contractual obligations due to the COVID-19 pandemic. This may involve in particular appropriate framing of provisions on force majeure or circumstances excluding the parties' liability.

Technological boost...

Practically, and paradoxically, the timing of the COVID-19 outbreak could not have been better. The key reason is technology.

In an age of progressive digitalisation, there is no barrier to continuing due diligence already begun, or even beginning new due diligence projects. Such processes may be conducted on an entirely remote basis. But the review must appropriately reflect circumstances related to the pandemic and their impact on the current and future condition of the target.

This very much extends to negotiations and technicalities of running transactional processes. While virtual signings and closings have never been customary in Poland (and are not likely to entirely replace physical ones, specifically due to Polish legal requirements for notarisation of most types of share transfer agreements and mandatory notarisation of contracts involving real property), they were pretty swiftly implemented, limiting physical interaction between the parties and their lawyers to an absolute minimum.

The art of virtual negotiations has been developed, replacing not only the old-style conference call, approaching in-person interactions in their effectiveness, but also generating the significant benefit of not spending time on the road for meetings. To some extent this has also forced both parties to take a reasonable approach, as much more balancing and compromise are required to close the deal.

...and analogue threats

Certain practical threats cannot be disregarded, nor consequences of the pandemic, such as the illness of employees and legal consequences (in extreme instances resulting in the restriction or temporary shutdown of activity), which may still impact the economic assumptions underlying a contract signed by the parties. This primarily concerns the valuation of the target and the mechanisms for setting the final price (whether based on a closing-accounts model or a locked-box model). For now, after over a year of pending lockdowns and restrictions, the actual impact of COVID-19 on the Polish M&A market has been rather limited (despite all the inconveniences).

Conversely, limitations on the work of courts, state offices, banks and other institutions have led (and presumably will continue to lead) at least to delays in fulfilling conditions for closing the transaction (eg, obtaining approval from competition authorities) or carrying out activities foreseen by the parties during the interim period (eg, corporate changes requiring entry in the National Court Register, deletion of pledges or mortgages, and the like).

This certainly presents a risk that the transaction cannot be closed by the long-stop date set by the parties, which in turn gives rise to a risk of automatic dissolution of the contract or termination by one of the parties.

Political Environment

The impact of the political situation in Poland on the business environment, including the M&A market in particular, is still a vital issue. No one would deny that some changes in law, tied to destabilisation, affect state institutions whose task is to help maintain stability, and thus exert a negative impact on the economy. This specifically applies to the judicial system, which has been subject to special concerns over the last few years. For one thing, these changes make the legal environment less predictable, and thus riskier for investors.

Of course, Poland is not an utterly isolated case. It is one element of a Central European trend – or perhaps an even wider one. That is why such political impact on the economy is not apparent, at least not at this stage, when analysing the situation from a high vantage point.

Politically driven attempts to influence or even take control of certain markets have not been too excessive. But one cannot exclude a risk (which is not dormant) of the government's plans to take over (or, as it is being called, to "nationalise") particular areas of economy, as COVID-19 has accelerated a trend of protectionism and regulatory restraints.

One of the main obstacles mentioned by investors, alongside merger clearance, is the new regime for oversight of foreign investments. It was introduced to protect companies and critical assets during the pandemic from capital flows from non-EU countries, when the acquisition could increase security risks. Thus, it seems inevitable that contracts will be subject to more conditionality.

Other Considerations

The M&A processes functioning in Poland do not display many country-specific issues. The country simply follows worldwide trends.

A story of due diligence

Once upon a time, behind the scenes of Polish M&A practice, there was a disturbing tendency to regard legal due diligence as little more than a technical exercise, which should be limited or even skipped if possible. This tendency could be observed in some deals, especially ones involving Polish entities or assets as part of global mega-deals, where this approach meant that due diligence was increasingly truncated. This was due to major limitations in scope and time of the review, an inadequate sample of material for review, etc. As a result, such an examination often failed to serve a larger purpose – and this may still be the case in deals where this limited approach to due diligence is taken.

Fortunately, this tendency has not developed into a standard approach, and an extensive and thorough review of the legal standing of transaction targets is still the norm. Even the anticipated decline in significance of due diligence review in cases where parties seek transaction insurance proved unjustified, as underwriters are all the more anxious to have a clear understanding of what they are underwriting.

Simultaneously, the growth in technology has sparked a discussion of how this will impact due diligence. On the one hand, the ability to access source documents online has been a game-changer, but on the other, even further-reaching change lies ahead. This involves the use of artificial intelligence in the process of digesting and analysing documents.

Changes going forward

Work on the relevant technologies is already well advanced, but it will still be some time before they displace lawyers from involvement in the due diligence process to any great degree. While technological support may indeed change due diligence as it is perceived now, it is a long path ahead before technology can substitute for analysis of identified issues by professional advisers.

These trends undoubtedly affect the way transactions are handled in Poland, and there is reason to believe that they will continue to have a growing impact on transactional processes. Notably, the decline in Polish GDP in 2020 was just 2.8%, one of the smallest in the EU. Simultaneously, Poland generated a 2.8% increase in exports, with a corresponding 2.0% decrease in imports.

Despite the decline in the manufacturing sector, in 2020 the number of bankruptcies declined as well.

The Prospects Ahead

The long-term legal consequences of the COVID -19 pandemic can hardly be predicted at this point, as the situation is highly dynamic and depends on too many factors.

However, irrespective of the fears or threats highlighted above, on the broader horizon (ignoring the turbulence caused by the pandemic) there should be no doubt that there will be numerous interesting transactions on the Polish market. This applies to both “ordinary” transactions and COVID-19-driven ones. The latter may specifically involve distressed-asset transactions (particularly in business sectors severely affected by the pandemic and resulting regulations), which, although expected, were not really visible in 2020, mainly because of some short-term and mid-term measures and relaxed insolvency rules introduced by the government to protect companies from going bankrupt.

Conversely, it is expected that some companies that have benefitted from the pandemic and are now overvalued may be subject to revaluation, thus leading to numerous interesting acquisition opportunities. The TMT sector as well as life science, healthcare, automotive, green energy and companies supporting remote working are listed among these industries that will be in demand in 2021.

Increased activism of private equity and venture capital investors is another factor that may boost the market in 2021.

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Wardyński & Partners was established over 30 years ago. It is particularly noted among clients and competitors for its services in corporate and M&A, dispute resolution, intellectual property, employment, private client, real estate and title restitution and provides comprehensive multidisciplinary legal advisory services. The firm has over 100 lawyers and has offices in Warsaw, Kraków, Poznań and Wrocław. The corporate and M&A team has 27 lawyers in the core team. Its transactional experience is well established and covers the entire spectrum of industries, sectors and areas of expertise. Apart from building client and peer relations both in Poland and abroad and being busy with a significant number of M&A projects, the team strives to be active in the implementation of e-solutions in the fields of M&A processes in Poland (such as machine learning software and automatised document review solutions for due diligence projects).

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Izabela Zielińska-Barłożek heads the firm's corporate and M&A practice. She is also the head of the Poznań office. She provides legal support for M&A transactions and ongoing advice on corporate law. In her long practice, she has advised on and co-ordinated legal support for transactions involving the acquisition and sale of enterprises, assets and shares, including in co-operation with foreign law firms on global transactions. She has taken part in many enterprise restructuring projects, including mergers and reorganisations.

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