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Corporate M&A 2024

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South Africa: Trends and Developments

Burton Phillips, Gareth Driver, Mlungisi Mahlangu and Safiyya Patel
Webber Wentzel

Trends and Developments

Contributed by:
Burton Phillips, Gareth Driver, Mlungisi Mahlangu and Safiyya Patel
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Authors

Burton Phillips is a partner at Webber Wentzel specialising in competition law. He has advised on all competition law aspects of transactions, from due diligence reviews and protocols to engagements with the competition authorities in South Africa and other African jurisdictions. He has advised on transactions involving regional competition authorities such as the COMESA Competition Commission and the Commission de la CEMAC. His expertise has been recognised by international research organisations.

Gareth Driver is a partner at Webber Wentzel with 30 years of experience in the areas of corporate law and mergers and acquisitions, specifically dealing with securities law, corporate finance and structuring, governance, Black Economic Empowerment transactions, financial services, international transactions, joint ventures, listings/IPOs, leveraged and management buy-outs, mining transactions, private equity, public offerings and private placements, and real estate/property. Gareth has advised on many significant transactions (both solicited and unsolicited) in South Africa and across many other jurisdictions. Gareth's corporate/M&A expertise has been recognised by various international research organisations.

Mlungisi Mahlangu is a partner at Webber Wentzel specialising in all aspects of corporate law, corporate governance and mergers and acquisitions. He has particular experience in the mining, healthcare, energy, infrastructure and financial services sectors. Mlu previously served as a researcher for Justice Jafta of the Constitutional Court of South Africa and has worked for leading firms in New York and the United Kingdom. Mlu is a trustee of the FirstRand Foundation and serves as a member of the foundation's audit, risk and compliance, and financial resources management committees.

Safiyya Patel is a partner at Webber Wentzel with over 22 years of experience specialising in general commercial law, M&A and transactions related to Black Economic Empowerment. She previously headed up the firm's corporate department. She has advised on transactions relating to joint ventures, company formations and reorganisations and has worked across the mining, financial, and construction sectors. Her expertise includes advising local and international clients on aspects of media, telecommunications, broadcasting, and information technology law. Her expertise has been recognised by international research organisations. She is an Executive Committee Member of the Johannesburg Chapter of the Indian Bar Association.

Webber Wentzel

90 Rivonia Road
Sandton, Johannesburg
2196
South Africa

Tel: +27 11 530 5000
Fax: +27 11 530 5111
Email: info@webberwentzel.com
Web: www.webberwentzel.com

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Contributed by: Burton Phillips, Gareth Driver, Mlungisi Mahlangu and Safiyya Patel, **Webber Wentzel**

Corporate M&A 2024: Key Trends and Insights

Navigating the complexities of 2024's M&A market requires an informed strategy. This article provides a comprehensive analysis of key trends shaping corporate and private equity transactions and delve into critical areas, including public interest, energy and infrastructure considerations, shareholder activism, and the environment for listed companies.

The levels of M&A activity in South Africa decreased markedly from 2022 to 2023, but commentators have noted that valuation levels of publicly listed companies are significantly below long-term averages. This, coupled with amendments to Regulation 28 of the Pension Fund Act, 24 of 1956, which brought with them the separation of the investment limits on hedge funds and private equity assets, and the 5% increase in the allocation to private equity funds means that the market is therefore ripe with opportunity.

Public interest as a key requirement for competition law merger approval

From a competition perspective, the main trend observed in the last year is an added focus on the public interest requirements for merger approval.

Pursuant to the Competition Amendment Act of 2019, which required the specific consideration by the competition authorities of the impact of transactions on a greater spread of ownership by historically disadvantaged persons (HDPs) and workers as an aspect of the public interest, the Competition Commission (the "Commission") has increasingly focused on this aspect.

The Commission interprets that requirement as placing a positive obligation on merger parties to promote ownership by HDPs or workers, with the result that it is no longer sufficient to simply say that transactions do not have an adverse impact on HDP or worker ownership as with other public interest factors, such as employment. To remedy HDP or worker ownership concerns, if not already a result of the transaction, the Commission generally seeks to impose conditions, often aimed at improving HDP and worker ownership through the use of an employee share ownership plan.

In some transactions, a strategic HDP shareholder is introduced to the business to satisfy this requirement. In circumstances where these types of remedies are not possible, the Commission is also asking parties for an explanation justifying this and then exploring potential equally weighted alternatives, all of which tend to result in more conditions being attached to merger approvals. The Commission's view is often shared by the Department of Trade, Industry and Competition (DTIC), which is participating in many more transactions than it has done in the past, weighing in particularly on HDP and worker ownership aspects of the public interest assessment.

Uncertainty as to the exact requirements has led to more protracted merger reviews, with extensive engagements needing to be had with the Commission and the DTIC, often concurrently. To provide greater certainty, the Commission published its revised public interest guidelines in March 2024, The guidelines, although non-binding, will hopefully lead to greater certainty for parties. However, the approach adopted by the Commission in the guidelines, in as far as it relates to the Commission's interpretation of the HDP and worker ownership requirements, is a contentious issue at the moment.

While many transacting parties are amenable to engagements with the Commission and DTIC with a view to getting deals over the line, the

continuing uncertainties and potential disagreements on the approach and interpretation of the ownership requirements relative to certain mergers can make the merger approval process more complex and could lead to more contested proceedings in future. This is particularly relevant in respect of black private equity sellers who may look to exit their portfolios to entities that may not be as empowered.

Consequently, it is vital to address the public interest aspects of a proposed transaction (in addition to its implications for competition) at the outset.

Energy transition and infrastructure

The global shift towards sustainability and decarbonisation has a profound impact on business's needs and opportunities, with a consequent impact on M&A strategies.

Companies are increasingly evaluating their sustainability practices and possible sustainability outcomes as an integral part of a potential transaction. The integration of renewable energy assets, carbon footprint reduction initiatives, and alignment with ESG goals have been drivers of M&A activity.

Despite significant development and secondary market activity within the South African energy sector, the prevailing market conditions and regulatory environment have not facilitated large-scale private participation in infrastructure development. To address this, the draft Integrated Resource Plan (IRP) that was published for public comment in January 2024 contains a two-phased approach for procuring South Africa's future energy requirements in a manner that facilitates economic growth.

The first phase offers a plan for the sector up until 2030 and focuses on stabilising South Africa's electricity supply and ending rotational power cuts, better known as loadshedding. The second, spanning 2031 to 2050, aims to ensure that South Africa has sufficient generating capacity to meet energy demand, encouraging economic growth for the coming decades.

In addition to the long-term horizon planning for South Africa's energy security, there has already been an increased focus on the restructuring of state-owned enterprises (SOEs), particularly within the economic infrastructure cluster and improving the framework for public-private partnerships. Attracting and encouraging private investment is key to meeting South Africa's growth ambitions and making SOEs more sustainable. To date, the government has announced initiatives in which it has secured private investment in transport, infrastructure and electricity.

In particular, investment in the battery sector could provide opportunities for investors, with a request for proposal (RFP) out to procure battery capacity through the Battery Energy Storage Independent Power Producers Procurement Programme (BESIPPPP). There is likely to be a continued focus here, particularly as South Africa looks to reach its decarbonisation and carbon emission targets.

Ultimately, as the world transitions to cleaner energy sources and more sustainable practices, investors must adapt swiftly to manage the risks of transition and seize new opportunities, which may present themselves in non-traditional ways.

Shareholder activism

Shareholder activism in South Africa continues to evolve and increase, with notable examples

illustrating a focus on ESG. Activists' proposals have included:

- enabling or frustrating mergers and acquisitions;
- influencing executive remuneration;
- requiring greater diversity amongst the board and senior management; and
- pushing for greater efforts to combat climate change.

There are a number of notable examples of institutional investors that use shareholder activism as a key component of their strategy to enhance or safeguard their investments, particularly in pursuit of better governance and economic performance. One prominent shareholder activist in South Africa is the Public Investment Corporation (PIC), a government-owned fund manager and major shareholder in many South African companies. Recently, legislation governing the PIC was amended to require the PIC to take account of "sustainable development" in its investments. The PIC continues to actively engage with companies to address issues such as board diversity and executive pay.

In the financial sector, regulation 28 of the Pension Funds Act of 1956 continues to hold sway. In terms of that regulation, a pension fund must "consider any factor which may materially affect the sustainable long-term performance of the asset including, but not limited to those of an [ESG] character" before investing in an asset and during its holding of an asset.

ESG matters have also been influenced or pursued by non-profit organisations (NPOs), with recent campaigns by NPOs seeking to table resolutions at annual general meetings of listed companies, particularly banks, to compel disclosure about the impact of their operations or investments on climate change.

Delistings from the JSE

Delistings from the Johannesburg Stock Exchange (JSE) have continued, with 27 companies delisting in 2023, 24 on the JSE and three when ZARx closed.

In an attempt to reverse the tide of delistings and to make a listing on the JSE more attractive, in July 2023 the JSE implemented the following changes to its listing requirements (the "Requirements"):

- introducing dual-class share structures;
- reducing the free-float requirement for new listings and changes to the free-float assessments for institutional investors;
- amending the JSE's current Special Purpose Acquisition Company offering; and
- making financial reporting disclosures less onerous.

In September 2023, the JSE announced its intention to go even further and completely overhaul the Requirements in an attempt to simplify them and "cut red tape".

These amendments may be successful in lessening the burden of a listed company and consequently making a listing more appealing, but of course, that does not automatically improve the traded prices of listed shares and make buy-out offers less attractive. For this reason, private equity, remains an attractive manner in which investors can seek to earn better returns than can be achieved in the listed environment.

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