SOMPO INTERNATIONAL

Thomas Mannsdorfer
Executive Vice President,
Head of European Specialty
Insurance Underwriting

The Value Of M&A Insurance

After a sustained period of growth over a number of years, mergers and acquisitions (M&A) – like many other business activities – hit something of a brick wall in the first half of 2020. The impact of coronavirus dragged global deal-making to its lowest level in more than a decade, according to data provider Refinitiv. During the period April to June, M&A value reached US$485 billion, down more than fifty percent on the same period last year, when close to US$1 trillion in deals were agreed.

This is not to suggest that M&A is dead in the water, far from it. With adversity comes opportunity. Dealmakers had to assess the impact of the pandemic on their operations initially, putting potential transactions on hold. Now there is optimism about the second half of the year, despite concerns about the impact of a second wave of COVID-19. There are a lot of companies and private equity houses with money to spend who will be eyeing potential targets, and valuations have declined enough to make some of the companies affected by the pandemic attractive.

Activity will rise again as deals that were put on hold are resurrected, although some may try to renegotiate in an attempt to push the price down. We will see a number of distressed deals as well as sell-offs or carve-outs as some bigger companies look to get rid of non-core operations.

As the level of transactions picks up again, so too will demand for M&A insurance. This is a product that has been gaining in popularity in recent years, not just because of the increase in deal activity, but because all participants in the market understand better the benefits that it can bring.

Unsurprisingly, savvy investors are looking at how best to mitigate the risks they face through the transaction process and beyond, to achieve greater certainty and peace of mind.

A range of benefits

A transaction is by no means a risk-free process. Both buyers and sellers face a range of exposures during the deal negotiation and after it has been completed. Regardless of the thoroughness of the due diligence undertaken, there is always an element of the unknown. Issues manifesting after closing could range from legal to intellectual property and environmental concerns, which could seriously damage the business, to irregularities in financial statements, allegations of fraud and tax liabilities, which could have even more serious repercussions. M&A is a comparatively long-tail class of insurance and although most claims are notified within 12 to 24 months of the deal completing, others can run on for years beyond that. In general, M&A policies have a duration of five to seven years, although in rare cases this is extended up to 10 years (matching the legal statute of limitations). General (operational) warranties are usually given for 24 to 36 months.

Unsurprisingly, savvy investors are looking at how best to mitigate the risks they face through the transaction process and beyond, to achieve greater certainty and peace of mind. M&A insurance provides the ability for a buyer or seller to reduce their exposure to claims against the representations and warranties contained in the sale documentation.

It can bring other benefits too. Buyers can use it in an attempt to differentiate themselves in a competitive bid process, part of 'dressing up the bride' to make them more attractive to the seller. Given the amount of dry powder ready to be deployed by dealmakers when the time is right, the number of bidders may be high in comparison to the number of targets available, so the presence of an M&A policy can serve as an advantage.

On the other side, M&A insurance can give sellers greater control over the sales process, leading to a much cleaner exit, enabling them to realise the proceeds of a sale and distribute them to investors as soon as possible. There is value in putting the policy in place early on as its presence will give a potential buyer confidence that the seller means business and is keen for a smooth sale.

The Value Of M&A Insurance

It is also worth noting that third-party advisers are increasingly involved in transactions and often require the presence of M&A insurance. It is important that they understand what is insurable and what is not, to avoid any unnecessary hold-ups in the deal process.

Careful insurer selection

M&A insurance is still a relatively young class of business. A decade ago, insurance buyers could only choose between four or five insurers who were offering the product. Today, that number is somewhere between 30 and 40, including Managing General Agents (MGAs) as well as carriers. As competition in the market has increased, pricing has come down. Meanwhile, the size and frequency of claims has been steadily rising. This is something that will in all probability accelerate in the economic fallout out from the pandemic as the downturn leads to more distressed deals.

Dealmakers need to choose their insurance provider carefully. The reputation and longevity of a well-established insurer like Sompo International are important, as are knowledge of the sector and the local market. Stable teams and good staff retention provide another advantage, giving the insured client a lot of comfort on both the underwriting and claims sides. But most critical are established claims service experience and financial strength. In these uncertain times dealmakers need to have the confidence that their insurer will still be around and have the means to pay valid claims, years down the road.

LEARN MORE

Our specialised underwriters, claims professionals and risk control specialists can help you address the exposures created by today's rapidly changing marketplace.

Thomas Mannsdorfer
Executive Vice President, Head of European Specialty Underwriting, Sompo International
M +34 830 830 970
E tmannsdorfer@sompo-intl.com

ABOUT SOMPO INTERNATIONAL

Sompo International Holdings Ltd., a global specialty provider of property and casualty insurance and reinsurance, underwrites agriculture, professional lines, property, marine, energy, casualty and other specialty lines of insurance and catastrophe, property, casualty, professional lines, weather risk and specialty lines of reinsurance. Sompo International is a wholly owned subsidiary of Sompo Holdings, Inc., whose core business encompasses one of the largest property and casualty insurance groups in the Japanese domestic market.

A+
FINANCIAL RATINGS
Standard & Poor's (Strong)
A.M. Best (Superior)