

« THE KEY TO DIFFERENTIATION LIES IN THE PARTNERSHIP WITH MANAGEMENT »



*Interview with Alexandre Margoline,
Partner and head of Permira's Paris office*



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The screening of foreign investment in France has emerged as a third pillar of M&A operations, alongside merger control and compliance. What is your view of this phenomenon? Are we witnessing the intensification of earlier trends or a fundamental shift (regarding the areas concerned or the spirit of FDI screening)?

Alexandre Margoline: It is clear that the question of screening foreign investments in France is being scrutinized more closely today. I think that the prominence of this issue varies enormously from one industry to another, depending on their sensitivity. For example, screening is not the same if the operation involves the pharmaceutical industry as opposed to other industries. It is easy to understand this difference, which is due to the strategic nature of the target.

Do you think that in the area of foreign investment screening in France and elsewhere that there will be a before and after Covid? Do you think that such a crisis is likely to change the philosophy of screening?

Alexandre Margoline: Yes, I do think that the health crisis we have been living through is bringing about a change in the philosophy of FDI screening. Nowadays, screening takes into account the strategic interests and sovereignty of the State, and sometimes European sovereignty also. All investors are not viewed equally. Non-European investment funds, for example, may be less well perceived than European funds. There is an implicit favouritism towards French or European investors, despite the friendly relations between France and a non-European country.

In your view, how is the French system perceived by foreign investors? Is it seen as welcoming and professional, as a deterrent that pushes investors towards more welcoming or more transparent systems, or as a happy medium?

Alexandre Margoline: Without getting into the content of the legal system, I think that unfortunately everything is a matter of perception, i.e. the perception that foreign investors have of our legal arsenal. In our profession as investors, perceptions very often become reality, regardless of the content of legislation, which is often misunderstood. And the perception is that in France a certain form of protectionism is used by the government in certain industries (e.g. automotive, tourism, health, etc.). I think that this perception is real and that any investor, whether a industrial corporation or an investment fund, will be aware that a barrier may be raised at any moment. To protect themselves and to mitigate the risk, foreign investors will seek to give the operation a French flavour, highlight their connections and roots in France – for example, through the Permira team based in France – or enter into a partnership with purely French entities like BPI or Ardian. There may also be clear agreements or contracts between the seller and buyer on future commitments regarding employment, maintaining business operations, R&D and other issues that "reassure" the State.

Have you already faced this type of issue in your career as an investor? Have you ever needed to make a pre-selection of industries that are less likely to come under the purview of such investment screening?

Alexandre Margoline: We do not tend to make our selections on the basis of the sensitivity of the industry. However, when we know that the industry in question is a sensitive one, we anticipate the situation by establishing a constructive dialogue with the relevant stakeholders to avoid any setbacks.

I remember a deal that was aborted in the tourism industry which was rather paradoxical in terms of the way the investment screening was done. On one hand, the French tourism company wanted to expand in Asia and had the clever idea to bring in Chinese investors. On the other hand, the French government sought to preserve French assets, but had nevertheless approved the operation, in spite of the increase in Chinese investors. Their goal then was to make sure that the Chinese investors would only hold a minority share and have virtually no control in terms of governance. I think that nowadays, in the context of a health crisis, that such a transaction would be much more complex, if not impossible, to implement.

Do you think that investment funds receive noticeably different treatment from industrial investors? If so, what are those differences?

Alexandre Margoline: I think that as an investment fund we are in a much more favourable position than a foreign strategic industrial actor regarding the seller, the government, and even the French population or media. A fund operates in a cold and unemotional way. Funds may therefore play the role of a trusted third party that will operate in a rational, expected and predictable way. Moreover, in the past five years there has been a real opening up to financial investors, for operations of every magnitude and at any level of maturity, which is truly encouraging for this type of investment and shareholding.

However, investment funds are not all the same. Their strategies may be very different, even in the world of large-cap companies. Each fund has its own positioning. Once this positioning has been verified, stakeholders will believe in the positioning and draw the corresponding conclusions. If we take the example of Permira, we do not do any company restructuring or any massive layoffs, but we do position ourselves with a view to supporting the growth of a company that is already in good shape. We get management and shareholders involved. Naturally, we are better perceived than other investors that might take a much more offensive approach. The investment thesis is extremely important, because it shapes the government's perception of the fund. The investment thesis is different depending on whether we are talking about a thriving company in the technology or pharmaceutical industries or a heavily industrialized company where questions of employment and outsourcing are the focus of attention.

Does the fact that an investment fund only holds its equity stake for a limited period of time, unlike a corporate investor, work against it in terms of the perception the government may have of the fund?

Alexandre Margoline: Not necessarily. But it has happened in the past that we had to agree not to resell the target to strategic rivals. Then we found ourselves in a partnership with the founding family and the agreement stipulated that we could not sell the company to foreign competitors, but could opt to sell to the family or to take the company public.

It is therefore possible to limit the scope of the exit strategy. But it is not always so easy, when we have control of the company, because the impact on prices and on the competitiveness of our offer is automatic. It is very hard to do in practice.

In order not to hinder its chances in a bidding process, what can a fund do? How can you work on the legibility of your approach? Does the fund have to bear the risk of investment screening alone or can it involve the seller?

Alexandre Margoline: Differentiation is achieved rather naturally because a fund has very clear and well delineated advantages and disadvantages. The advantage is that a fund behaves as a third party which has no interests beyond the investment in question. Therefore, there will be no question of synergies or strategic influence that would come with another company, only the investment thesis, which is that of the fund and which must be in line with the management of the target company. The choice is therefore known, rational, and aligned with management. On the other hand, the downside is that the identity of the fund may at times be less clear; there is a somewhat nebulous aspect.

The key to differentiation lies in the partnership with management. When both management and the seller are convinced of our positioning and the truth of our investment thesis and when the fund is aligned with their future strategy, the price may be slightly lower, but the parties will have avoided the central question of strategy.

In the case of a build-up, does being a fund change the circumstances by making you more of a strategic actor than a financial one ?

Alexandre Margoline: I will give you a nuanced answer to that question. While it is true that in such a case the fund appears to behave as a strategic actor would do, the fact remains that in the end we are an investment fund and we always have an exit timeframe.

In any case, the positioning is clear. It may require the implementation of an equity package.

The definition of foreign investors increasingly takes into account the chain of control, beyond the corporate headquarters. Does that change the way that funds are structured and how they approach their operations?

Alexandre Margoline: The advantage for the company of having an investment fund as a shareholder is that it can remain independent. The goal is not the absorption of the target, which will continue to function as a standalone. Wherever the funds are located, operations are not predatory and the French targets remain based in France. We adopt and pursue a purely financial approach and have no intention of building an empire here or there, in this or that jurisdiction !