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FDI Regimes - The impact of COVID-19 on deal-making

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FDI restrictions have been on the political agenda in Europe and further afield for at least the past year, and following the outbreak of COVID-19 and the changed economic landscape, the approach in jurisdictions across the world has mutated.

FDI restrictions are no longer being used solely as a tool to address issues of national security, but also to combat so-called "adversarial capital", typically from jurisdictions perceived as potentially hostile, pursuing opportunistic M&A when asset prices are depressed as a result of the pandemic. At the same time, there are calls for Western governments to support "national champions", protect a wider range of industries and the COVID-19 crisis may also make it easier for acquirers to invoke a "failing firm defence". We have collated the key takeaways from our recent webinar on this topic below. Should you wish to view the webinar on demand, you can find a link to the recording here.

Key Webinar Takeaways:

1. Clear trend towards strengthening FDI protections

Globally, FDI measures are becoming more stringent, with COVID-19 only accelerating the shift. National examples include both COVID-19-specific regimes to protect businesses critical to economic activity and recovery (e.g., medical research and biotech) and more general measures that are not limited to any particular sector. Whichever option Governments have chosen to adopt to address issues relating to adversarial capital, FDI is now one of the top 5 considerations for investors, and the increasing importance of "big data" across all sectors means that the trend is only going to continue.

2. Investors beware

Tougher FDI restrictions mean investors should expect to have more of their transactions probed from an FDI perspective. When doing deals, investors will need to think about possible exit routes and the universe of possible buyers in the future, especially as rules may have changed again by the time they want to exit. There is no uniform definition of "adversarial capital" and Governments can (and do) interpret it in different ways to achieve their policy objectives, so the issues require careful consideration. Investors should seek advice early on in the process. Further, the definition of "national security" is flexing: it will grow as more data driven businesses are deemed sensitive not for what they do but due to the data they work with and their access to citizens' confidential information. It may also extend to any functions that are considered particularly important, such as the food supply chain.

3. Understand the politics

FDI regulation is driven by politics. Investors will look for clear answers based on the rules, but understanding the political angle will also be a fundamental key factor - the rules must be read and interpreted in their political context for investors to be given clear advice. Businesses need to have an understanding of the political environment in which their investments are operating – right from the moment the investment is made, until exit. Depending on the jurisdiction, an understanding of local politics can also be vital (in Germany, for example, regional governments wield significant influence). Notwithstanding the EU's new FDI Screening Regulation that takes effect in October, the approach from different European jurisdictions will vary as it is dictated by the underlying national agendas. It's key that the development of FDI rules is managed to ensure the clarity and stability needed for investor confidence. The UK's decision to reverse its approval of (albeit limited) Huawei involvement in Britain's 5G network highlights the impact of politics in the process.

4. Be willing to "campaign"

FDI is both politicising transactions and making them public. Investors need to be prepared to engage in public debates to defend and/or justify their choices. Engagement with key stakeholders should form part of overall transaction planning.

5. Consider the reputational impact of your investments

As FDI becomes more controversial, regulators will become increasingly eagle-eyed. Investors should ensure that they are seen as trusted sources of capital. This will require careful management of both existing investments and new ones.

6. Be bold (as well as mindful)

Increasingly stringent FDI regulation will invariably scare off some investors. Those that are shrewd can exploit opportunity in areas where rivals fear to tread.

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