

Introduction

On September 10th, Italy's UniCredit SpA [ETR: CRIN] has acquired a total 9% stake in the German Commerzbank AG [FWB: CBK], half of it directly off the hands of the German finance agency. About a week later the stake was increased to 21%, the majority of it through derivative instruments. Immediately, questions rose, and debates sparked about how a foreign bank was able to acquire such a significant stake directly from the government and why this had not been communicated prior to the transaction. Amid the fog of opposing statements by all sides, including the government and the banks brokering the trade, the German chancellor and affiliates clearly positioned themselves against a full takeover of the nation's second biggest lender. While the Italians signalled, they would be working towards a friendly outcome, worker's unions warn about the potential loss of workplaces and others see the firm's biggest customer, the German Mittelstand, in danger. How this situation was created and why all parties and bankers involved possibly knew about each other's intentions, will be further discussed in this article.

About UniCredit

UniCredit is a Commercial Bank offering its services in Italy, Germany, Central and Eastern Europe, serving over 15m customers worldwide. Headquartered in Milan, the bank is divided in the three product categories: corporate, individual, and group payment solutions. It is listed on both the Borsa Italiana and the Frankfurt Stock Exchange and has posted record earnings in 2023, with €23.3bn in net revenues, a 26% YoY increase, marking the 12th consecutive quarter of year-over-year profitable growth. The stock is currently trading at about 100% of the book value of its net assets. UniCredit reflects on a broad history, beginning in 1870 with the foundation of the Banca di Genova, later becoming Credito Italiano. The institution, as it is known today, was formed as a result of mergers starting in the 1990s by the acquisition of many European and Italian banks. The Group's CEO is Andrea Orcel, a highly experienced deal maker, having spent 20 years in various positions at Merrill Lynch (Bank of America) [NYSE: BAC], as well as a few years at Goldman Sachs [NYSE: GS] and Boston Consulting Group, prior to that. Right before joining the Italian company in April 2021, he was member of the executive board at UBS [SW: UBSG], as well as head of investment banking. His expertise and deal experience are shining through in his operations at his current firm.

Already in 2000, the Italians acquired Bank of Austria, but the milestone in building a European heavyweight was the merger with Germany's HypoVereinsbank ("HVB") in 2005. The transaction marked the largest ever cross-border transaction in Europe at the time, structured as a €15.4bn stock swap for 100% of HVB's share capital. Key value drivers for the deal included strengthening UniCredit's position in Germany, Italy, and Austria, but mostly to improve their Central and Eastern European market share. After an initial backlash, the deal scored a 94% acceptance rate in Germany and caused the stock to trade at a 30% increase during the offer period, effectively prohibiting other competitors to join the takeover attempt. Among the advisors were Citi [NYSE: C] and J.P.Morgan [NYSE: JPM] for the target, as well as Goldman Sachs and Merrill Lynch for the buyer. Interestingly, a certain Andrea Orcel was part of the Merrill Lynch deal team during the transaction, demonstrating his long-lasting knowledge about UniCredit's strategic plans in Europe, which he is now taking into his own hands. On the other hand, J.P. Morgan became familiar with UniCredit's ambitions and has utilized its knowledge in the Commerzbank block trade that it initiated for the German finance agency this year, kicking off the takeover attempt.

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About Commerzbank

Commerzbank is a Frankfurt based German banking institution that mainly serves Mittelstand clients, including 11m private and small-business customers, as well as 25,500 corporate clients, mainly in Germany or located internationally with German connectivity. Furthermore, it serves about 5.8m customers in Poland, through its subsidiary mBank S.A. The firm has posted its highest operating profit in the last 15 years of €3.4bn for the FY 2023, however, in contrast to its possible acquirer, it is only trading at 60% of the value of its net assets. In the early 2000s, the bank had a thriving investment banking business with abnormally volatile earnings ranging from billion-dollar earnings to billion-dollar losses in the span of quarters. After some challenges, it now trades at 9% return on equity, which is close to the European average, making it a reasonable acquisition target.

Commerzbank was founded in the same year as its Italian rival, in 1870, and was the first German bank to open an office in New York in 1971. In March 2008, the German bank accepted an €8.2bn cash bailout from the German government, specifically the German Financial Markets Stabilization Fund, as well as €15bn in debt guarantees. The government ensured to be a silent shareholder to not pose any dilution threat to others and retained their 16% stake until recently. A block trade to sell off some of those in 2009 acquired shares, triggered the start of recent events.

Since January 1st, 2021, Manfred Knof was CEO of Commerzbank, after having spent a few years at Deutsche Bank [ETR: DBK] prior to his appointment. Already a few hours before UniCredit announced its acquisition of a stake in the German bank on September 10th, Knof announced his early retirement from his position, instead of his planned step down at the end of 2025. On September 30th he will officially leave the supervisory board and pass on his role to Bettina Orlopp, the bank's former CFO. She has been with the bank for 10 years and was mainly responsible for the saving's plan, significantly increasing its profitability. Shareholders and the remaining board happily welcomed the first female CEO of the company.

A potential deal between UniCredit and Commerzbank had been in the talks as far back as 2017, when talks were not started due to the Italian bank's own restructuring. Although only two years later, they prepared a bid to buy out the Frankfurt-based bank as alternative to a theoretical approach by Deutsche Bank AG, who showed interest in their domestic rival. Already at that time, potential synergies between HypoVereinsbank and Commerzbank were identified and even a potential listing of the combined entity was discussed. Those talks fell through, and the German government was left with its 16% stake in the company at the time.

9% stake acquisition

On September 11th, 2024, UniCredit announced the acquisition of a 9% stake in Commerzbank and signalled its intention to further increase this holding. The Italian Bank acquired approximately half of this stake (4.45%) by outbidding the other participants in a block sale offered by the government. The total amount paid was €700m, or €13.20 per share, which is approximately half of what the government had spent on Commerzbank's bailout in 2009 following the global financial crisis. Still, the acquisition price of €13.20 was significantly higher than Commerzbank's market price of €12.60 at the closing on Tuesday, September 10th. After having accumulated the other half of the 9% stake on the open market, UniCredit announced its intention to increase its shareholding. The Company is currently seeking regulatory approval to perform this transaction, but did not provide further details on the period and size of the next acquisition. Andrea Orcel, stated on Bloomberg TV that "all options are on the table", suggesting that various options, including a potential merger between the companies, are possible.

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After the investment, Commerzbank's share price increased significantly, reaching a high of €15.22 during the day, and closing at €14.69. This reflected investors' positive sentiment regarding the implications of the transaction. Investors value the two banks' shared geographic location, the stability of their financial data, and their assumption that the deal is "collaborative" in nature. Moreover, they appreciate the strategic impact that the transaction could have, with some analysts considering Commerzbank to be undervalued, as the missed cost reductions in Q2 led to a significant decline in share price. However, a common opinion among analysts is that immediate financial benefits of the transaction would be limited and that there are some risks associated with the cross-border deal.

The 4.5% stake acquisition by UniCredit from the German government has also had some political backlash, mostly due to its lack of transparency. It appears that UniCredit had communicated its interest to German officials prior to the sale, casting doubts whether the government was aware that the stake would have fully gone to the Italian bank. This has led to speculation regarding accountability within the German Finance agency. Among the different agencies involved in the sale, no one is willing to take responsibility for what is viewed as a poorly executed strategy, that allowed a foreign entity to gain significant control over a major German bank.

UniCredit increases its stake

On September 23rd, 2024, UniCredit increased its stake in Commerzbank to 21% and announced its plans to raise it further to approximately 29.9% by submitting a request that is currently subject to regulatory approval. This increase was facilitated through financial derivatives, allowing UniCredit to acquire shares without immediate direct purchases. Many analysts speculate about the possibility of a potential merger between the two banks. In a recent meeting with investors in London, Orcel presented three possible strategies: expanding UniCredit's ownership and going for a full merger; collaborate to maximise the value of both institutions; or selling its stake if favourable conditions cannot be met.

As this move was defined as an "unfriendly attack" by the German Chancellor Olaf Scholz, investors reevaluated the likelihood of a full takeover and Commerzbank and UniCredit shares declined by 5.9% and 3.3% respectively. Despite this political resistance, Citi analysts predict that the approval for UniCredit's stake increase is likely, assigning a 70% probability to the occurrence of a merger. UniCredit's request to further increase its stake is currently under review by the ECB, that has up to 60 days, extendable to 90. Commerzbank responded by raising its profit targets and shareholder payouts, aiming to bolster investor confidence and showcase its independent growth potential. The bank projects a net profit exceeding €3bn by 2027.

Rationale

A potential merger could create significant synergies, both from the financial and the operational standpoint. According to a recent analysis by Goldman Sachs, the transaction could result in approximately €800m in savings for Commerzbank, reducing its operating costs by more than 15%. Additionally, Commerzbank's profit before taxes is projected to increase by €3.4bn, driving a 37% increase in UniCredit's profit before taxes and a 29% surge in net profit. If the merger proceeds, the new entity would control almost €1.3tn in assets, nearly €700bn in loans, and €875bn in deposits. The combined firms are expected to generate an estimated €12.3 billion in net profit, with Germany playing a crucial role in the entity's operations.

By increasing its stake, UniCredit also aims to enhance its market positioning, reinforcing its leadership capabilities in the European banking sector. UniCredit's management believes that Commerzbank holds considerable value that can be unlocked, either as a standalone entity or part of UniCredit, benefiting both Germany and the bank's larger stakeholders.

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Political reactions and implications

The efforts by UniCredit to significantly increase its stake in Commerzbank have not been well received in German politics. German Chancellor Olaf Scholz told Reuters that "unfriendly attacks [and] hostile takeovers are not a good thing for banks and that is why the German government has clearly positioned itself", thereby attempting to obstruct a potential takeover. Surprisingly, politicians in Berlin, across the entire political spectrum, seem to agree on this issue, expressing unified disapproval of what they view as Orcel's overly aggressive approach. Friedrich Merz, leader of the opposition, went even further and commented on UniCredit's recent actions, stating that a potential takeover of Commerzbank by the Italian bank would represent a "disaster for the German banking sector." The potential loss of numerous jobs that could be eliminated due to synergy effects in the event of a takeover, as well as the likelihood of worsened credit conditions for German small and medium-sized enterprise (SME) customers, are arguments frequently raised against the proposed acquisition.

A similar sentiment is shared by trade unions, such as Verdi (one of the largest in the country), and many representatives from the business sector, who emphasize the importance of Commerzbank's independence as a key financier for SMEs in Germany. In an interview with the Handelsblatt, TUI [ETR: TUI1] CEO Sebastian Ebel highlighted that Commerzbank is even part of the critical infrastructure, asserting that especially during challenging times, it is one of the most essential banks providing financing to German companies. Other stakeholders believe that a potential takeover could weaken the financial hub of Frankfurt, which plays a vital role in supporting the entire German economy, warning against a "fire sale of German flagship companies".

The attempted takeover appears to come at a highly inopportune moment for the German government. The country's economy remains in crisis, with negative news from companies becoming increasingly frequent. Should Commerzbank lose its independence, it could become, alongside the Volkswagen [ETR: VOW3] crisis, a second emblem of the decline of Germany as an economic hub. Politically, the issue would only benefit Chancellor Scholz if he could position himself as a saviour of jobs by blocking the takeover and thus protecting Commerzbank's autonomy. Nevertheless, according to banking experts, the German authorities do have little to no leverage on the situation, as the European rules on competition, bank supervision, and capital markets apply, which are out of German authorities' control.

In Brussels, the German government's resistance to the proposed takeover has been met with criticism, particularly due to its apparent contradiction with Germany's advocacy for progress on both the European banking union and capital markets union. Experts like Nicolas Véron from the Brussels think tank Bruegel suggest that Germany's stance, in which it opposes an Italian bank acquiring a German bank, calls for further explanation. This inconsistency raises questions about the country's position on cross-border banking within the European framework.

As Europe is known for its highly fragmented banking system, where mergers are often confined to entities within the same country and lending activity remains largely home-biased, this transaction could pave the way for stronger cross-border cooperation and ignite consolidation across the continent. The report of the former Italian prime minister Mario Draghi concluded that Europe needs to raise capital expenditures by €800bn a year to remain competitive, showcasing the enormous amount of financing required. In order to raise these sums, the EU must leverage the combined financing power of its banking system by scaling up among the continent's lenders. As the EU's single market includes 23 million businesses and 450 million people, European banks have significant potential to raise capital at scale. However, they have been constrained in fully realizing this potential through consolidation or expanding regional lending.

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Banks looking to expand across national borders face numerous bureaucratic challenges, including varying tax systems, accounting standards, insolvency laws, labour regulations, and securities markets. These obstacles contribute to the sluggish pace of cross-border lending and mergers. Additionally, European banking authorities are often seen as more stringent compared to their international counterparts, which further limits such expansion efforts. Brussels is therefore urged to take greater action in reducing barriers to commercially viable cross-border M&A, and lending opportunities. At the same time, domestic politics is encouraged to move beyond its protectionist stance in favour of advancing a unified European banking union, or risk widening the economic gap with the United States and China. Therefore, a takeover of Germany's Commerzbank by the Italian UniCredit could signify a pivotal transaction for Europe and potentially lead to further mergers within the banking sector.

Conclusion

UniCredit's acquisition of a significant stake in Commerzbank has ignited a complex web of political, economic, and strategic discussions within Europe. While the move has potential benefits, such as operational synergies and enhanced market positioning, it has also raised significant concerns among German officials, labour unions, and industry stakeholders about the implications for jobs, lending practices, and the integrity of the German banking system. The resistance from German politics, especially amidst the ongoing economic difficulties, underscores the fragile balance between national interests and the push for greater European integration in the banking sector. As this situation unfolds, it not only highlights the intricacies of cross-border M&A but also serves as a critical juncture for the future of banking in Europe. Ultimately, the outcome of this endeavour could shape the competitive landscape of the European banking sector, influencing future consolidation efforts and cross-border cooperation in a fragmented financial environment.

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