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The calm before the storm?

Global Business Voice: M&A Outlook I - The AGN Global Survey of how the mergers and acquisitions market has been affected by the Global Pandemic.

May 2021

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How has the Mergers & Acquisitions market been affected by the Global Pandemic?

INTRODUCTION

This edition of the AGN Global Business Voice Survey reveals the headline levels of M&A activity within our pandemic hit economies across the globe. Some of us have read reports that activity is up in some regions, other reports suggest there are some "bargain" businesses available for cash rich buyers. Well we have once again called on our global panel of business advisory accountants, spread around the world, to give us a very high level global picture based on their opinion about what's actually happening "on the ground".

CRISIS WHAT CRISIS?

The most striking thing about this research is the sense of an underlying latent crisis. On the one hand, we have the worst performing economic situation for several generations, and on the other, we have only modest increases in distressed sales and business sales values remain steady (overall).

This relatively benign set of headlines masks the wildly different fortunes of selected industry sectors. For example; the desperate state of hospitality versus boom time communications, the plummeting fortunes of leisure and retail versus the rising fortunes of technology.

All the while the big hitters of manufacturing, construction, energy, utilities and business services trundle along barely touched.

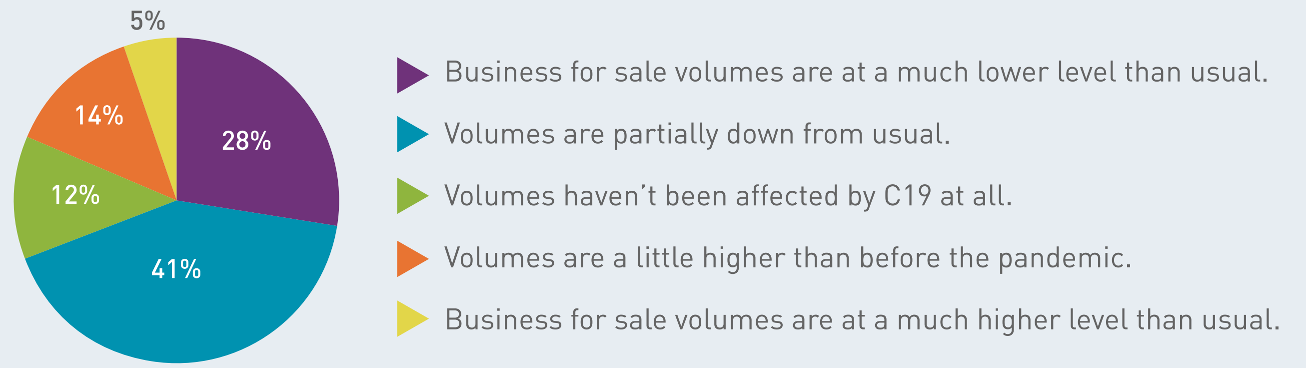
In the west, governments embraced hugely expensive financial support measures in a way not seen in the face of an economic downturn since after the Second World War. States have accumulated massive debt – it all has to be paid for, and some are predicting a much rockier couple of years for business when the plug is finally pulled.

PANDEMIC HAS HIT VOLUMES – BUT ONLY PARTIALLY

Despite stories to the contrary, activity levels are down. Nearly 70% of the panel are reporting much lower (28%) or partially lower (42%) volumes than usual. But given where we are in terms of a global recession this isn't particularly surprising – perhaps what is surprising is that this result isn't worse! Or that indeed almost another 1/3 (28%) report that volumes aren't affected or are a little higher than before the pandemic!

We are 12 months into the biggest shock the world economy has ever had to deal with – WWII levels of disruption and plummeting demand, but we are not reporting a calamitous deadening of the M&A arena – which raises further questions. What's going on? Let's go further into the findings.

Q1. What has happened to business for sale volumes in your country since the Pandemic struck?



BUSINESS VALUES IMPACTED? ... SORT OF

While the global crisis and economic collapse may have only marginally impacted volumes of mergers and acquisitions, it surely must have put a dent in business values? And our panel do indeed bear witness to a reduction in values. Some 66% are suggesting that business for sale values have reduced or partially reduced. But looking more closely at this figure only 25% are suggesting 'significant reduction'. A very substantial 41% indicating values have only 'partially' reduced.

One only has to go back to March 2020 to recall the US Fed, the ECB and the Bank of England predicting the world's worst ever economic collapse. A scenario so bad that between March 2020 and April 2020 UK GDP fell by 20.4%! A corresponding complete and fundamental collapse in business values doesn't seem to have transpired.

In some quarters business values and volumes of transactions (deals) are still being sustained in what was predicted to be a near economic Armageddon. How is this possible? There is anecdotal evidence that deals are being concluded on the more resilient businesses – businesses not just coping but thriving – and these deals are keeping multiples healthy.

Q2. Are local business valuations being suppressed by the C19 Pandemic?

UNLUCKY SECTORS?

However, one doesn't have to look far to see the actual day to day effects of the pandemic on our economies, but it would appear that some sectors have been harder hit than others. Again, our panel were asked to think where a reduction in values was most keenly felt....

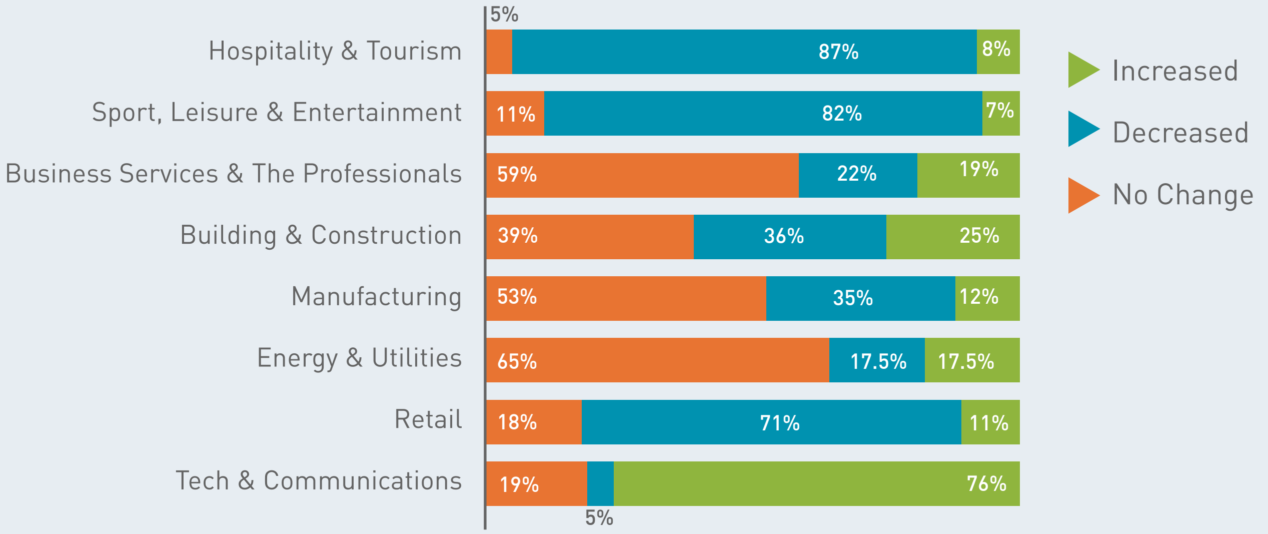
The blue and green bars tell a dramatic story of pandemic impact. The panel are not reticent to indicate the very contrasting fortunes of different parts of their local economies.

At 86% and 82% respectively, hospitality and tourism, and sport, leisure and entertainment have decreased in value. Clearly a consequence of 'social distancing' and the various lockdowns around the world. The severe drop in demand combined with great uncertainty towards recovery will trigger many solvency challenges, with potential for consolidations, restructurings and bankruptcies. Retail is clearly another big victim of lockdown.

Conversely the 'Tech and Communications' sectors have boomed. 76% of the panel have seen an increase in the value of these businesses. As more and more people have worked from home, shopped from home, met with friends online – and have, whether cognitively or not, increased demand for a whole raft of technological ancillary services or products.

Perhaps more interesting than both of these results are the bars coloured orange. Very broadly speaking ..."no-change" in values for business and professional services, building & construction, manufacturing and energy and utilities. These sectors continued to operate and values remain steady - remarkably against the backdrop of an economic contraction like we've never seen before.

Q3. Are there any sectors in particular where values have been impacted?



FIRE SALES - DAMP

The next question sheds some light on how much of the near recent M&A activity has been about a distressed sale, restructuring or the realisation of cash, and in line with the rest of this survey the results are muted. Roughly 70% of the panel would say that less than 30% of the sales they have witnessed have been brought about through emergency or distressed circumstances.

This continues a theme of the less than dramatic consequences of operating in a Covid battered economy.

Perhaps this is a matter of timing. Is it possible that we simply haven't seen the real impact of Covid .... just yet?

To re-cap...

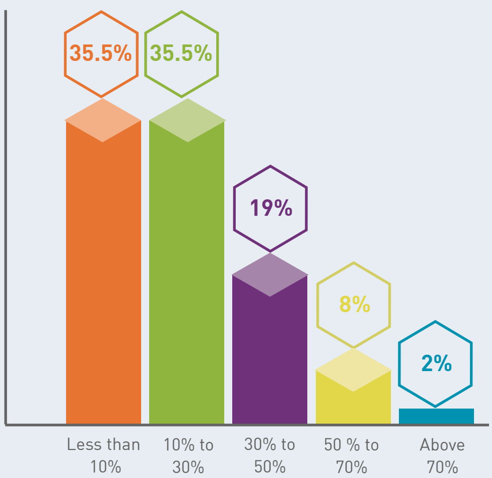
- Volumes are down – but not out!
- Values are muted – but not crashed
- Sectors are mixed – there are clear winners and losers, but a remarkable group of major sectors are continuing barely affected.
- And distressed sales are higher than normal but still a relative rarity.

We went on to ask the panel to predict when their economies would turn around and consequently bring on the surely inevitable rise in bankruptcies and fire sales – as companies outstretch their ability to generate any more credit. Something like 71% predict anything between 6 to 18 months.

Surely a wide timeframe, no doubt dependent upon a whole range of local factors – not least of which will be the closing date for state sponsored financial support programmes, and the rafts of legal protection and deferred payment schemes for taxes and rent currently supporting layers of qualifying business.

Many of AGN's own insolvency specialist members are privately forecasting that we are 'in the calm before the storm' and that all these schemes have done is delay the inevitable and sooner rather than later the bill will have to be paid.

Q4. What proportion of business sales have been 'distressed'. due to emergency restructuring (say) or to generate liquidity and cash?



IN CONCLUSION

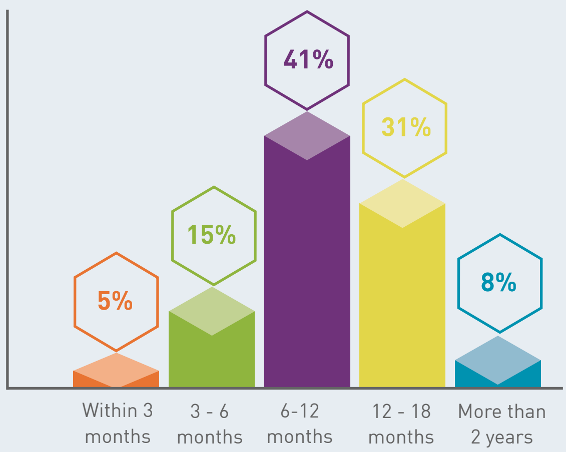
Our survey has reported a troubled but not catastrophic landscape for M&A activity – volumes and values often holding up. But members are also quietly predicting a more dramatic radical change of circumstances when the clock runs out on government support.

Other surveys conducted in 2020 indicated that up to 70% of respondents will continue with M&A and in some cases accelerate their deal activities over the next twelve months. And it's also true that smaller deals continue as companies shed assets and distressed businesses seek M&A solutions to solvency.

In the coming months, M&A activity will respond differently by sector and geography depending on how severely each is impacted. But the positive moves that we, as corporate financiers and deal makers support, may include some or all of the following:

- Watch out for the sector losers – High street retail, venues, hospitality, the arts, sport and aviation – Are they on your client list? What's their next move?
- Consolidation in key sectors – Hard hit sectors consolidate into smaller cabals and groups.
- Rapid move to e-commerce – Further acceleration of the move from high street to internet. There will be/are some big players looking for perhaps niche (smaller) online business to complete its value chain.
- Who are the sector winners? – Amongst others tech hardware, home entertainment, healthcare, software and home office.
- It's said that the businesses achieving good values right now are the more resilient, well run, growing concerns. If this is the case then current market conditions would suggest there's likely to be a large body of less attractive, less benign businesses waiting in the wings ready to do deals at perhaps reduced values and reduced multiples. Only time will tell.

Q5. Conventionally, we see an increase in 'fire sales' and disposals as an economy comes out of recession - when do you think this will happen?



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