Mike Kearney: Welcome to Resilient.
My name is Mike Kearney, the Risk &
Financial Advisory CMO. Looking back at the
Confronting the COVID-19 Crisis series, it was
a little over three months and 12 episodes
ago when we talked about precision and
divestiture execution and strategy. The topic
continues to provide challenges for leaders.
As organizations reshape their business, raise
capital, and generate value for stakeholders,
transactions remain an important and crucial
strategy. But how deals are done is vastly
different during this pandemic. That’s why
this series is so important. We explore issues
facing leaders today and help them address
questions such as, “What new complexities
have been introduced in the pandemic and
economic downturn? How are changes
in modeling and valuation taking shape?
How does the regulatory landscape and
stakeholder expectations influence deals?
And how are organizations approaching
their deals in today’s environment?”

Increased management and board
expectation on approving return on a
transaction investment, coupled with the
roller coaster financial performance over
the last two quarters, makes confidently
executing transactions even more
challenging. Today, we’ll be talking with
two partners in Deloitte’s M&A Transaction
Services practice, Jeff Bergner and David
Oberst. They will break it down for us
and provide insights on the markets and
deal complexities. Jeff and Dave, welcome
to Resilient.

We started many of our recent
conversations with a question, which in my
opinion kind of epitomizes what resilience is
and that’s about having hope for the future.
So, I just want to start off, Jeff, I’m gonna
start with you. What gives you hope for
the future?
Jeff Bergner: What gives me hope is we’re actually seeing some positive economic activity out there. And we’ll talk about this a little bit at the back end of this, but I have a role where I deal with IPOs and throughout this process, I have companies call and want to talk about going public. And when you’re talking about April and being locked down and it seems like things were going in completely the wrong direction, somebody wanting to talk to you about trying to go public and all the positivity around it in 2021 was just something that I really latched onto. And it’s a trend, as we’ll continue to discuss, that has just accelerated over the course of the summer, but you could see the people that could see on the other side of the valley of this pandemic out there and see more positive times. And it’s just been really refreshing to have conversations with companies like that.

Mike Kearney: And even back in April, because I would’ve thought, like you indicated, nobody would be thinking about an IPO at that point in time.

Jeff Bergner: No, I was having like three to five discussions a week with companies that were seeing the other side of it. Now, as we’ll talk throughout the course of this, these are companies that were not as impacted negatively by this. So, there are winners and losers in this economy, and we’re seeing that in the M&A market, we’re seeing that in the IPO market, but if you have some sort of slant, be it maybe your FSI or tech, food delivery type stuff like that, even some health care–related items or make cleaning wipes or something like that, it could be a home run for you, but if you’re travel related or something like that, it’s obviously a very difficult time.

Mike Kearney: Dave, let’s turn to you. What gives you hope for the future?

Dave Oberst: Yeah, so I guess I’ll answer it maybe in two ways. On a personal level, my daughter and my family give me a lot of hope for the future and help keep me grounded in these times. From a professional standpoint, I would say it’s really the creativity of professionals to continue to do their job, even in the midst of all these challenges. When the country first kind of shut down in March, we saw almost all the deals being put on hold, as people were trying to figure out how are they going to move forward in this environment. And I think pretty quickly people realized that it was not going to be a very short-term thing, and they’d have to come up with a way to try and still get deals done. And that’s really what we’ve seen. Starting in mid-April and onward, we just continue to see more and more deal activity because people are realizing, “This isn’t gonna stop anytime in the near future, and I still have to do my deals. So how can I get it done?”

Mike Kearney: And that’s one of the things I think is the narrative about COVID, it’s how we’ve been able to adapt to this new virtual world. You’re talking about deals. And we had previously talked to somebody about closing the books virtually, which I would have thought would have been a real challenge. But it’s awesome to see how so many of us have adapted.

Jeff, let’s start with you on, just what are you seeing on your deals, and why is it so different from the past?

Jeff Bergner: So, Dave just touched on it. We are seeing a recovery. I would describe it as a barbell recovery. On one end of it, we have distress transactions and some of these—like we saw a number of people that were investing in restaurant concepts, where they believe in the concept, but obviously the restaurant has fallen on hard times.

So again, they’re looking forward and they want to invest in those. Others, we’re seeing pure distress where they’re just selling off good assets in order to just try to avoid bankruptcy. And that’s obviously a very unfortunate situation. But at the other end, as I was talking about on the IPOs, you have businesses that are winners in this, and they are trying to capitalize on that. And right now is a little bit of an odd time where investors don’t really know where to put money. There’s low interest rates, the stock market’s a little bit probably more emotional than it typically is. So, these winners either via an IPO or an M&A transaction, they can get very solid multiples right now. And it’s an attractive time to sell for them. Because they have a story that—people just want to latch onto positive stories right now. And so they’re willing to invest.

Mike Kearney: Dave, how about you? What have you seen in the last few months?

Dave Oberst: Yeah, I would echo a lot of what Jeff said. As I said before, things really kind of came to an abrupt halt in March and slowly trickled back. First we saw businesses that had been pretty far along in a process that was put on hold. Those were kind of the first to come back to market. We’re seeing a ton of activity in the technology space and health care space. As for a lot of the business-to-business tech companies, they’re actually seeing a big uptick instead of a downturn. Now as we sit here today, some of the other industries are starting to come back. And we’re also seeing some opportunistic M&A and distressed companies. And so, for areas like consumer, energy, or some of the travel and leisure, there are still deals getting done, but it’s more to save a good company that’s just fallen on some hard times.

Mike Kearney: Maybe this is for both of you. Are there any industries that have surprised you that maybe they’re more resilient than you would have thought or where there’s more activity than you would have anticipated?

Jeff Bergner: I don’t play in FSI, but when I talked to our FSI partners, they have always sounded much more like business like usual because I think it was easier for that industry to—financial services when I say FSI—but it was much easier for that industry to go virtual.

Health care was a surprise. And again, that’s not necessarily my direct industry, but when they were shutting down all the optional type services, that put a lot of that industry in distress, and there were some transactions that needed to happen, again just so that they could keep the doors open on some of those. And that would be an industry that ordinarily would have been extremely profitable and very healthy, no pun intended.
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Dave Oberst: Yeah. I would just say I've actually been surprised by the strength of tech. I think everybody thought maybe it wouldn't be as impacted, but what we're seeing now is almost record-level activity in that industry. And so, part of it probably is people just don't know where else to put their capital, and technology seems like a good bet. But I guess I have been surprised by how strong it has been.

Mike Kearney: How do you actually factor in, though, the uncertainty, because I think we all would have hoped that we were outside of COVID, but we're still dealing with it on a daily basis, just that grave level of uncertainty. How do you start to factor that uncertainty into this in the future?

Dave Oberst: Yeah, that's a great question. I think you have to take a deep dive into your financials and really try and isolate areas that you think have not been impacted by coronavirus or kind of as it always has been and the areas that are changing. Think about whether that change is something that is temporary, or if in a new normal, things are not going to look tomorrow like they have historically. And certainly if it was just that easy, everybody could go do that and everybody could put out decent guidance and have a good idea about where things are going to go. But, obviously that's not the case and nobody really knows what things are gonna look like in four months, eight months, twelve months. And so, we're advising our clients to build a lot more dynamic models and different scenario planning into their models, because if the last four months has taught us anything, it's that we don't really know what it's gonna look like in the next few months.

Mike Kearney: And, Dave, can you talk about the magnitude of some of the losses that we've talked about caused by COVID?

Dave Oberst: Yeah. It is really daunting to look at some companies in the travel and hospitality businesses. We're seeing second quarter revenues that are 20 percent of what they were a year ago. So, that's so significant. And those are the types of businesses where they really are in the mode of survival and just understanding how they can get enough cash to pay their bills. I would say for most of the companies that I've worked with over the last several months, it hasn't been that dramatic, but certainly certain client verticals that they may have, or customer verticals, are significantly impacted. So they're seeing revenue drops. There's new costs that they didn't have previously around things like extra cleaning their facilities or hazard pay for their employees. But that said, it's not all negative. Businesses are also seeing cost savings from reduced travel and expense. And certain businesses are booming if they're helping businesses function remotely or helping them with call-in services, those types of things, those businesses are booming. So, there is no one impact that it's having to companies, but it is impacting every company.

Mike Kearney: And your point is right on also, like there's costs that have been reduced. I think travel is probably one of the easiest ones to get your mind around, like you said, or maybe Jeff mentioned that. We haven't traveled. I don't think I've traveled since early March other than for personal reasons. So those costs are significantly less as well. What about the impact on GAAP with all of this? Are there any considerations that controllers or accountants should take into consideration?

Dave Oberst: Yeah, absolutely. One of the biggest things people are questioning right now as it relates to GAAP is, “How do I do my impairment analysis?” So whether it's bill impairment or asset impairments, as we said, it's very hard to predict the future, and the models that you had for years to estimate future cash flows, well, now there's a lot of question as to whether that's a legitimate model anymore. And so I think that, from a GAAP perspective, has probably been the biggest impact we've seen, the biggest challenge for companies. And again, I think the advice there is build more scenarios into those models so you can understand how close you may be to being impaired, and that's when you're really going to get challenged by your auditors to provide documentation to support the decision to not impair or to impair, depending on where you fall out.

Jeff Bergner: And, Dave, to add onto that, impairment has always been seen by the market as a lagging indicator. It's usually a year or two behind the curve, but if somebody comes out with a much larger impairment in this market than what the investors were expecting, it could be seen as a future indicator and it could really affect the company negatively. So, it's kind of a little bit of an odd dynamic on that vis-a-vis historical times because otherwise, but the pressure in this would be to blame COVID and just try to write off all your good will and intangibles so you don't have to deal with it in the future.

Mike Kearney: You guys have brought up scenario planning and the models. Is scenario planning experiencing a Renaissance now, or has it always been kind of a critical aspect of it, or is it just being ramped up just given the amount of uncertainty?

Jeff Bergner: So a lot of what we do when we do a diligence is we look backwards and you try to, as you talked about earlier, about normalizing EBITDA, and then trying to mirror that up with the starting point of any financial model. Everything now is much more focused on the future, like what is going to be the term everybody's using, the new normal. And if you look at a company or due diligence on there, that may be corporate-wide, or you may have to go market by market on there, as people are experiencing shutdowns and be in hotspots at different times. It's not like everyone's being impacted equally in all places. So, scenario planning and really looking at the data. Analytics is going to be a huge focus around this on a go-forward basis. And that's what we're working on with people, and we're helping them on selling a company, is being able to have as wide a net on your data as possible so that you can support any type of position. And so, scenario planning is, as you said, it's going to be absolutely critical for getting the right price.

Mike Kearney: Jeff, I want to stay with you. What do you think leaders can do? And I think we've touched on this a bit, but what can they do to evaluate their position and determine how to actually set a realistic valuation?
Jeff Bergner: So again, that goes to what I started with, with this barbell. So, if you’re in one of the winning industries right now, it’s a great time to sell because it’s been a great M&A market for the last several years. It’s probably been the longest continuous trend I’ve experienced in my 20-plus years in M&A. And right now, those winners are probably even getting a premium to what was already a robust multiple. The distressed-type scenarios, it goes to exactly what we were just talking about, the scenario planning and how long are you going to be in distress, when you’re going to come out of it, and when you come out of it, what are you going to look like? Are you going to be at a hundred percent of what you were before? Or are you going to be in some sort of 60 to 70 percent of what your revenues and earnings were in a different scenario. And what your plan is to get back to it, what you think the market’s going to be is going to absolutely drive what your purchase price is. The other aspect of it, and this would normally just be something minor, although it gets fought on every single transaction, but most transactions have a purchase price and adjustment mechanism all around working capital, and the standard has always been a 12-month average of going backwards for what it’s going to be. Well, nobody wants to average what it was pre-COVID anymore. So, some of the transactions we’re seeing, it’s almost like a fist fight around this trying to negotiate the final working capital. It’s not necessarily the most material item for the overall purchase price, but it’s become a gating item to actually try to be able to get something to the finish line. What we’re starting to see a bunch of people try to do is split the difference and say, “Okay, we’ll give you so many months pre-COVID, so many months post-COVID, and we don’t know what it’s going to come out at, but neither one of us is happy.” But it seems like a fair answer for both sides. But this has been fascinating. I’m used to working capital fights, but I’ve never seen them like what we’re seeing right now.

Mike Kearney: And, Dave, what are we hearing from the regulators? And in particular the SEC?

Dave Oberst: So, the SEC put out some guidance right at the front end of this, as you recall, it kind of happened right before most businesses’ end of Q1. And they said, there’s certain things they’re looking for from registrants in their in their disclosures. And their focus is that companies are putting out transparent information, related items, such as an entities’ financial position, their liquidity and capital resources. And so they really want the companies to tell investors, “How much cash do I have? How much access to cash do I have? And how close am I to hitting my debt covenants?” And that is maybe no different than it always has been, but this is something everybody’s very, very focused on. They also put out some guidance, on this concept of EBITDA plus C through some increased guidance on non-GAAP measures.

And as we’ve said, a lot of companies are trying to struggle with, “How do I frame my historical results given this unprecedented event?” Well, they have said that you can make adjustments to your non-GAAP measures for coronavirus items, assuming that they’re directly related to COVID-19 or the associated economic downturn, they are incremental to normal operations and non-recurring. And when we say non-recurring, there may be certain things like cleaning costs, for instance, that a lot of companies now have increased cleaning costs, but it’s hard to speculate that that’s non-recurring because this just may be a new part of life. Lastly, any adjustment has to be objectively quantifiable as opposed to an estimate or a projection.

And so, with that guidance given to registrants, what we’ve actually seen is that a lot of companies are not making very significant non-GAAP adjustments for coronavirus. And it’s really because of that last part that you can’t include estimates. And for most companies, other than some discrete costs, such as asset impairments, severance that they did some sort of restructuring, the impact is still kind of being estimated. And so I think at the beginning of this, we may have thought there was going to be more non-GAAP measures around coronavirus. It just hasn’t really come to fruition yet.

Mike Kearney: Jeff, you’ve talked earlier about the fact that we’re starting to see more exit strategies or organizations disposing of certain businesses. What are you seeing? Are you thinking that there’s going to be a greater uptick, and what should companies be thinking about when they’re contemplating both kind of doing it and potentially executing it? If you could maybe just touch on that for a minute?

Jeff Bergner: We are seeing a variety of different things that have changed in this. One of the things from an exit is the emergence of these Special Purpose Acquisition Companies (SPACs). There’s a $4 billion one that was raised over the course of the summer. A SPAC only has like two years to get a deal done, and so they’re on the clock. And so, they’re very active in the market and they’re one of the buyers. So that has created some market demand, it has helped with some valuations. As I said, we are still seeing IPOs. IPOs are fairly active on there and it’s, again, it’s that people don’t know where really to put money. Now the election, and I don’t mean this from a political standpoint, but just it creates a little bit of uncertainty. So that may cause the IPO market to pause a little bit.

But it’s been robust. And one of the things that’s been positive over the last couple of years around IPOs is there was a regulation change that was put out by the SEC, and it allows people to file for an IPO confidentially. And so, what you could do is you could file, start the SEC review process, but nobody sees your financial information. So you’ve maintained that process. But once you file for an IPO, the SEC has got the most regulation. You can relax that and take that IPO document and say, “Okay, let’s start a sale process,” and put out a confidential information memorandum and start that process. And you could do what we call a dual path transaction, where you tell people, “Hey, if you want to buy my company, you got to pay me more than what I’m going to get on this IPO.” And it puts a lot of stress on a company because you have your day job, you got the IPO registration to do, and you’re trying to sell a company. So it’s basically like three full-time jobs at the same time. But if you’re a VC-backed company,
a PE-owned company on there, that natural tension between the two transactions is an absolutely great way to maximize your proceeds. And it’s a trend that we’ve seen just really continue over the last couple of years, and the pandemic did not slow that trend down at all.

**Mike Kearney:** That’s very cool. I’ve got about four more questions, and I call this the lightning round. So basically, the way that I do this is I will ask a question, both of you get to answer, and the only ask, given the lightning, is that you answer quickly—two to three sentences. So, the first one is, and I’m going to start, Dave, with you. How do you do deals and diligence virtually? And then how do you actually even get confidence in management without being able to meet them face to face? I have to imagine that’s a challenge. So, Dave, I’m gonna start with you.

**Dave Oberst:** Yeah, that is a big challenge. And I’ll handle maybe the second part of that question first. The reality is, there is no way to meet management or get to know them better than doing it face to face. And so how do you get confidence in management without being able to do that? First, it’s about setting expectations with yourself, just knowing that I’m not going to be able to meet them, and I’m just going to have to get over that. But the way we’re seeing these deals getting done is just lots of time spent on video conferencing and being very clear in what you’re asking for and really not beating around the bush. I think everybody kind of has less access. So you need to do more with less time.

**Mike Kearney:** Jeff, what’s your thoughts?

**Jeff Bergner:** I would say that the majority of what we do in diligence was virtual pre-this. It’s that last piece that you talk about. It’s the confidence in the management team and that’s really where our clients are. But it’s literally like, how would you, to put it in perspective, not M&A people, how do you hire a whole crew virtually? Do you feel the same degree of confidence today as you did when you could do that one on one and take somebody to lunch and spend time with them? You probably don’t. I think people have gotten better at it, but I think this will be the first thing that comes back in a non-virtual world. People will figure out how to go meet someplace remotely, safely, and get to know one another so they can finalize a deal.

**Mike Kearney:** Jeff, I’m going to stay with you for this next question. What advice do you have for leaders managing deals in a virtual environment? And maybe just like, if there’s just one thing, like your number one piece of advice, what would it be?

**Jeff Bergner:** I don’t want this to sound self-serving. But David and I work on this, and we do buy side and we do sell side, and with all the uncertainty out there, having somebody help you on the sell side—legally, tax, accounting, investment banking standpoint—to really help position you, should be, it’s expenses for the company, but it should be money that you get a substantial ROI on. This is not the time to try to do something, sell your house for sale by owner and not hire a real estate person on there. So that would be the one thing I would tell people to do. Make sure you get professional assistance.

**Mike Kearney:** Got it. Dave, what would be your one thing?

**Dave Oberst:** Yeah, I would say making sure you have really clean and clear documentation because we don’t have the opportunity to go sit with people and work through issues with them face to face. I think that the expectation if you’re not going to be with them is that you can figure it out on your own. And the only way you’re able to do that is by having very clean, detailed information.

**Mike Kearney:** Dave, I’m gonna stay with you. How is COVID impacting the traditional M&A timeline? Is it shortening it, elongating it, or is it basically the same?

**Dave Oberst:** Yeah, I think it’s—I’ve seen it is elongating it a little bit. Again, typically you might have a week of management meetings, eight hours a day, back to back to back to back. In a video conferencing environment that’s just not an option. And so these meetings are kind of being laid out over a longer period of time. Another issue that I’ve seen on some of my deals is that if you’re doing a big worldwide deal, there needs to be a lot of regulatory approvals around the world while a lot of governments are being shut down for periods of time, and people can’t get anything done. And so, one of my projects we almost couldn’t close the deal on time because one government was late giving approval because they had to shut down for three weeks because of COVID. And so, I’d expect it to be a little bit longer, and you may just have to build some time to take into account that not everything’s gonna go as it usually would.

**Mike Kearney:** Is that what you’re seeing as well, Jeff?

**Jeff Bergner:** Yeah, what used to get done in three-plus weeks for us is taking four to five. And Dave’s right, you can’t have the back-to-back meetings, and because you don’t have to have the back-to-back meetings, there’s a lot of times, things used to be done parallel on there, and now people have the ability to participate in every single meeting on there. And so the schedules have just stretched it out. Now, there are some transactions that are just pure distress that you’re on the clock because they’re trying to avoid some bankruptcy or other types of situations. But most of them, it seems like it’s added an extra at least minimum two to three weeks to the process.

**Mike Kearney:** So, our last question. Jeff, I’m going to start with you. And then, Dave, you’re going to end it for us. And it really kind of goes back to the platform for this podcast: resilience. And the question that I have for you is, what would you say leaders can do to build better resiliency into their M&A strategies?

**Jeff Bergner:** I think if you start with resiliency, people are going to be saying, “What do I need to do differently so I don’t get as impacted by something like this again?” And so that’s their starting point. And then out of that point then, is it something you build organically, or is there someplace you could speed this up and maybe you go out and you do an acquisition.
It might be something globally; it might be something with your supply chain; it may be a different market. But I think the M&A is going to be one of the key tools in everybody's toolkit to think about how we don't get into the same place that we were in 2020. And so, I think this is going to actually cause an uptick in M&A as we come out of this.

Mike Kearney: Dave, what are your thoughts?

Dave Oberst: Yeah, I think about that question more of, how can we be more successful in doing M&A in this environment and as a result of this environment. And I think it's two things. One, as we talked about, allowing for more different scenario outcomes when you're doing your forecasting and building your plans. I think people are going to be really interested now to understand what the downside risk is. And whereas before, you might think of worst case is 3 percent growth versus best case of 10 percent, now maybe worst cases is 20 percent decline. And what does that look like? The other thing I think businesses can do to be more successful and resilient in their M&A is something I talked about before, but being really detailed and clear in the information that you provide to people because I think both buyers and sellers are going to get down into a lower level of detail using data analytics than maybe they ever have before. And so, you need to think about building things from the bottoms up as opposed to the top down.

Mike Kearney: Awesome. I really appreciate, Jeff and Dave, your time. I always learn something new, and our goal is hopefully we sussed out some things that our listeners hear. But you guys are absolutely on the front line. Some great insights. So, thank you very much.

Dave and Jeff, thank you for sharing your two cents with our listeners, as they navigate the uncertainties of today's world. Doing deals won't stop just because of the pandemic. And it's clear that deals are an important part of many organizations' strategies to remain competitive and to supplement innovation. I hope the information shared provides some potential signals, as well as considerations when addressing the evolving impact of this crisis.

We've covered a lot of topics over the last several months. We still have many more to cover. Want to hear something that we haven't covered yet? Hit me up on LinkedIn or Twitter. For more insights across all aspects of COVID-19, just go to deloitte.com on our COVID page. You can also listen to the Resilient podcast on Apple Podcast, SoundCloud, Stitcher, Spotify or anywhere you listen. Just search the keyword Resilient.

Until next time, stay safe and remain resilient.