M&A: A critical tool for growth

Global merger and acquisition (M&A) activity hit a record high of $4.7 trillion in 2015 and continued its momentum in the first half of 2016 reaching $1.7 trillion.[1] Although that may prove to be the high-water mark for deal flow, a majority of corporate executives and private equity (PE) professionals nonetheless expect deal activity to remain strong in 2016.[2] Conducive macroeconomic conditions have helped fuel the boom, but astute observers can see an evolving strategic rationale for deal-making.

M&A can be an important means for building scale, improving a target's performance, or removing excess industry capacity, and can fuel long term, profitable growth. M&A's numerous potential benefits dictate that it be viewed as an important arrow in the corporate quiver; ready to be loosed when needed. However, companies should not wait until an attractive target is in view to sharpen their M&A capabilities; proactive planning can improve the odds of hitting a strategic bulls-eye. In fact, Deloitte's *M&A Trends Report 2016: Our annual comprehensive look at the M&A market*,[3] found that corporations are placing more emphasis on developing an M&A strategy in 2016.

The sluggish pace of global economic growth enhances the attractiveness of M&A. In addition, sustained low interest rates, strong US equities markets, cash-rich balance sheets, and increasing business confidence give companies the ability and attitude to pursue deals as a means to grow. In fact, executives' most commonly cited reasons for engaging in M&A are growth-oriented: accessing new customer bases, gaining entry into new geographic markets,[4] and expanding products and services.[5]

Access to new intellectual property (IP) is also an important driver of growth-oriented deals, especially in highly innovative industries such as pharmaceuticals and technology, where IP is a company's lifeblood. Case in point: Over the past five years, the cost to develop a pharmaceutical asset has increased by roughly a third, while average peak sales for the industry have fallen by 50 percent over the same period.[6] M&A provides an additional means of bringing promising therapies into a pharma company's portfolio.

Meanwhile, big technology firms are making headlines for their deal activity (and a fair number of deals are not disclosed or publicized). For instance, a major social media platform company has completed more than 50 deals in its short history, with recent acquisitions adding capabilities in e-commerce, virtual reality, speech recognition, and other fields. Some companies' portfolio of IP-related acquisitions is even more eclectic. Adding credence to this trend, Deloitte's latest corporate development survey reveals that the pursuit of innovation is transforming the M&A landscape. Roughly two thirds of corporate development leaders who responded to the survey said their function has become a more important source of innovation over the past two years, and nearly 60 percent of executives believe that the volume of innovation-centered deals will increase over the next two years.[7]

In the midst of this boom, it is worth remembering that not all M&A deals add value. Thirty-nine percent of corporate respondents and 56 percent of private equity (PE) respondents said that more than half of their transactions completed over the past two years had not generated expected returns.[8] However, reported failures should not necessarily discourage companies from pursuing M&A. Well-developed due diligence, valuation, and integration capabilities can anchor an effective risk mitigation strategy. There is enough knowledge and experience among the M&A community and associated professionals that properly prepared acquirers can expect to gain considerable financial and competitive value from their M&A pursuits.

M&A is expected to remain a critical tool for growth and long-term shareholder value-creation. Management teams planning to engage in strategic deal-making should focus on building internal M&A capabilities and partnering with experienced advisors to improve their chances of hitting a bulls-eye.

End Notes

1. "Will the New Year be 'Sweet '16' for Deals?" The Wall Street Journal, December 31, 2015, http://www.wsj.com/articles/will-the-new-year-be-sweet-16-for-deals-1451557804. Cited in M&A Trends Report 2016: Our annual comprehensive look at the M&A market, Deloitte, 2016
2. M&A Trends Report 2016: Our annual comprehensive look at the M&A market, Deloitte, 2016
3. From February 19 through March 15, 2016, a Deloitte survey conducted by OnResearch, a market research firm, polled 2,292 executives at US companies and private equity firms to gauge their expectations, experiences, and plans for mergers and acquisitions in the coming year.
4. M&A Trends Report 2015: Our annual comprehensive look at the M&A market, Deloitte, 2015
5. M&A Trends Report 2016: Our annual comprehensive look at the M&A market, Deloitte, 2016
6. Measuring the return from pharmaceutical Innovation 2015: Transforming R&D returns in uncertain times, http://www2.deloitte.com/us/en/pages/life-sciences-and-health-care/articles/measuring-return-from-pharmaceutical-innovation.html
7. Corporate development strategy: Thriving in your business ecosystem, Deloitte University Press, 2016, http://dupress.com/articles/corporate-development-strategy-survey/
8. M&A Trends Report 2016: Our annual comprehensive look at the M&A market, Deloitte, 2016

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