The state of the deal
M&A trends 2018
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About this report
This report is the result of a survey of more than 1,000 executives to gauge their expectations for M&A activity in 2018 and to better understand their experience with prior transactions.

All survey participants work in either private or public companies or private equity firms with annual revenues of $10 million or greater. The participants consist of senior executives (director-level or higher) involved in M&A activity. One-third of corporate respondents work in the C-Suite, while half of private equity respondents are involved in fund management.

For more detailed information about this report see: About this survey (page 19)
Executive summary

Corporations and private equity firms foresee an acceleration of merger and acquisition (M&A) activity in 2018—both in the number of deals and the size of those transactions.

In Deloitte’s fifth M&A trends report, we heard from more than 1,000 executives at corporations and private equity firms about the current year and their expectations for the next 12 months. The results point to strong deal activity ahead: About 68 percent of executives at US-headquartered corporations and 76 percent of leaders at domestic-based private equity firms say deal flow will increase in the next 12 months. Further, most respondents believe deal size will either increase (63 percent) or stay the same (34 percent), compared with deals brokered in 2017.

Since our previous annual survey, the environment for domestic M&A has been muted due to concerns about, among other things, the economy, political and regulatory uncertainty, market volatility, and valuations. While those concerns are all diminishing according to findings from our new survey, 1 in 8 respondents cites delayed legislation as a potential obstacle ahead. That concern could abate if significant pro-business legislation, including tax reform, materializes in the coming months.
## Key findings

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<th>Description</th>
<th>Details</th>
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<tr>
<td><strong>Tools and technology are making an impact</strong></td>
<td>Almost two-thirds of respondents (63 percent) are going beyond the spreadsheet and using new M&amp;A technology tools to assist with reporting and integration. Respondents say the tools help reduce conflicts, costs, and time—likely key factors in making more deals work.</td>
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<td><strong>In it for the technology</strong></td>
<td>Technology acquisition is the new No. 1 driver of M&amp;A pursuits, ahead of expanding customer bases in existing markets, or adding to products or services. Talent acquisition continues to trend upward as a motivation for M&amp;A strategies. In a new question in this year’s survey, 12 percent of respondents cite digital strategy as the driving force behind M&amp;A deals for the coming year; combined, acquiring technology or a digital strategy accounted for about a third of all deals being pursued.</td>
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<td><strong>Bigger firms are more confident</strong></td>
<td>Corporate executives and private equity investors from the largest firms—with revenues and investments in excess of $1 billion—are considerably more confident than their smaller counterparts that they will engage in bigger deals in the coming year.</td>
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<td><strong>Deals are working better</strong></td>
<td>Only a handful of corporate respondents (12 percent) say that a majority of their M&amp;A deals are not generating the expected return on investment. This is down from just under 40 percent in spring 2016. An even slimmer number of private equity survey respondents (6 percent) say that a majority of their deals are missing the mark—this is consistent with what respondents reported a year ago and continues the downward trend from a high of 54 percent back in spring 2016.</td>
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<td><strong>Full speed ahead for divestitures</strong></td>
<td>Divestitures should persist as a major focus in 2018. Seventy percent of survey respondents plan to shed businesses next year—driven by financing needs and strategy shifts.</td>
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<td><strong>Driven by convergence</strong></td>
<td>Industry and sector convergence continue to be major themes, with a strong bias toward vertical integration. Top industries that respondents predicted to experience convergence are life sciences and health care, technology, and financial services.</td>
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The survey is full of additional revealing insights. Corporations have spending firepower; more companies say their cash levels have increased, and M&A remains the No. 1 intended use of those funds. There also is a marked downtick in interest in global deals, with far fewer US-based acquirers looking to Asia (China and Japan), Brazil, Italy, and Spain for acquisitions. For these five countries alone, interest among deal seekers is down an aggregate of 26 percentage points compared to a year ago.

As you delve deeper into these findings, you will see what drives entities to pursue deals, what’s considered critical to their success, and how new analytic tools are making a difference. Our objective behind these reports remains to provide you with insight into the M&A ecosystem so that your next transaction can be as successful as possible.

**Russell Thomson**
National Managing Partner
Mergers & Acquisitions Services
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### Deals are working better
*For transactions your company has completed within the past 2 years, what percentage has not generated their expected value or return on investment?*

<table>
<thead>
<tr>
<th>Percentage Range</th>
<th>Corporate Executives (n=766)</th>
<th>Private Equity (n=250)</th>
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<tbody>
<tr>
<td>0% or none</td>
<td>6%</td>
<td>0%</td>
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<tr>
<td>1%-25%</td>
<td>19%</td>
<td>66%</td>
</tr>
<tr>
<td>26%-50%</td>
<td>16%</td>
<td>19%</td>
</tr>
<tr>
<td>51%-75%</td>
<td>4%</td>
<td>6%</td>
</tr>
<tr>
<td>76%-100%</td>
<td>2%</td>
<td>6%</td>
</tr>
<tr>
<td>Don't know/not sure</td>
<td>10%</td>
<td>12%</td>
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Survey respondents remain generally optimistic that the number of M&A deals will increase over the next 12 months. Sixty-eight percent of corporate respondents and 76 percent of private equity respondents anticipate an uptick in the number of transactions. This year’s figures have edged down slightly compared to 2016, when 71 percent of corporate respondents and 86 percent of private equity respondents projected an increase in the number of deals.

Roughly a quarter (26 percent) of corporate respondents and 20 percent of the private equity respondents expect deal flow to stay the same as the prior year. Both the expectation of higher deal volumes and larger deals is in sharp contrast to the trends seen over the past few months of 2017.
Deal size

Expectations also are high for heftier deals: Sixty-three percent of respondents anticipate the average enterprise size of transactions in the next 12 months will exceed those in the past year. Meanwhile, 34 percent of respondents expect that deal size will hold steady.

Deal volume

Respondents from larger organizations—both on the corporate side and the private equity side—anticipate doing more deals in the next 12 months than they did in the past year. More than a third (35 percent) of corporations with revenue in excess of $1 billion intend to pick up the pace on acquisitions, compared with 22 percent of smaller companies. At private equity firms investing more than $1 billion, 29 percent expect deal activity to step up significantly in the year ahead, compared with 12 percent among their smaller counterparts.

Corporate respondents acknowledge they were more selective in striking deals in the trailing 12 months. The number of companies that closed six or more deals declined slightly (down to 52 percent from 60 percent a year ago). The number of companies that closed five or fewer deals increased slightly (up to 45 percent from 38 percent a year ago). The aggregate value of deals fell; respondents closed fewer deals in the $500 million to $1 billion range and fewer deals of more than $1 billion.

The findings mirror overall market results. While deal activity was brisk for the first three quarters of 2017, companies were cautious and focused on deals at the more modest end of the spectrum. The number of domestic transactions rose 19 percent from the start of 2017 through the end of September, compared to the same period in 2016. The value of these transactions in the first three quarters of the year declined 15 percent to about $869 billion, according to Thomson Reuters.
Deal type

Corporate respondents report diverse motivations for pursuing deals. The most cited reasons were looking to acquire technology and looking to build out a digital strategy (19 and 16 percent, respectively). Some plan to seek major, transformational deals (17 percent). Others say they are on the hunt for smaller, strategic opportunities (15 percent).

On the private equity side, 60 percent of respondents expect a greater focus on bolt-on acquisitions to build scale in the next year. More than half (53 percent) see strategic sales as the main driver of portfolio exits. About 26 percent anticipate a sale to another private equity firm and 19 percent expect to tap the public markets for an initial public offering to exit a position.

Divestitures

Divestitures are on track to remain in vogue in 2018. Some 70 percent of both corporate and private equity respondents say they plan to sell units or assets in 2018, up from 48 percent in the spring of 2016.

On the corporate side, survey respondents cite a change in strategy as their top reason to divest businesses. Corporations with revenue over $1 billion expect an unsolicited bid for one of their non-core business units, by more than a two-to-one margin, as compared to smaller companies.
Strategic drivers

Acquiring technology assets now ranks number one as a strategic driver of M&A deals. Twenty percent cite the acquisition of technology assets as the principal reason behind deals, up from 6 percent in the spring of 2016.

Expanding customer bases in existing markets, and adding to product offerings or diversifying services, rank as the next two strategic imperatives.

Two other notable drivers that corporate respondents cite as a rationale behind dealmaking are:

1. Digital strategy, a new response option for what is driving deals, ranked number four in importance, with 12 percent citing it as the most important driver.

2. Talent acquisition has more than doubled in importance from the spring of 2016, growing from 4 to 9 percent.

What’s less important? There continues to be less emphasis on obtaining bargain-priced assets, with only 6 percent of respondents citing this as the most important driver. Entry into new geographic markets remained the same at 11 percent.
Deal success
and the emergence of new diagnostic tools

Companies and private equity firms appear to be getting better at achieving their goals for their deals. There continues to be a decrease in respondents who say that a majority of their deals fall short of expectations. Overall, only 1 in 10 respondents say that more than half their deals did not deliver the return on investment they had anticipated. That is unchanged from the 10 percent level a year ago, but significantly down from the 40 percent who said more than half their deals did not deliver back in our spring 2016 survey.

Among corporate respondents, 12 percent said that more than half their deals did not meet expectations, down from 40 percent back in the spring 2016 survey. For private equity respondents, only 6 percent said deals didn’t deliver as anticipated, down from 54 percent last spring.

A similar proportion (11 percent) of respondents say they are not sure their deals are meeting or exceeding expectations. And it is important to note that more than half (55 percent) of all respondents say that up to a quarter of all deals fall short of meeting or exceeding expectations.
Our surveys consistently show that well-planned, carefully-executed integrations yield transaction success.

More than 6 in 10 respondents (63 percent) say they now incorporate the use of non-spreadsheet-based M&A technology tools as part of their deal processes. The respondents cite a raft of benefits. These analytical tools make post-deal integration smoother and faster, reduce costs and conflict, and shorten the time it takes to complete them.

Those who have not used M&A technology tools yet would like to do so going forward: Sixty-two percent of those who still rely on spreadsheets want to tap into these new M&A tools to integrate their acquisitions faster and more smoothly and to reduce costs and conflicts.

For the second straight year, respondents cited effective integration, accurate valuation, and economic certainty as the three most important factors for a deal’s success. A stable regulatory environment climbed into a tie for fourth place with proper target identification.

Change management, the quality and timeliness of data, and capturing synergies have persisted as top concerns upon striking a deal. This year, respondents cited the speed of decision making and added aligning cultures as key areas of concern.

Our surveys consistently show that well-planned, carefully-executed integrations yield transaction success.
In our prior report—completed in fall 2016—global economic uncertainty, capital market volatility, deal valuations, and interest rates ranked sequentially as the leading obstacles to M&A activity by corporate and private equity respondents combined.

All four of these categories were cited by fewer respondents in our current survey, demonstrating diminishing worries about these topics.
Global economic uncertainty still tops the list of potential deal obstacles over the next 12 months, though only 20 percent cite it as a concern, down from 26 percent in our fall 2016 report. This perhaps demonstrates the increased resiliency of companies and private equity firms to navigate through major global economic shifts.

Capital market volatility was cited by 17 percent of respondents in this year’s survey, down from 21 percent a year ago. This aligns with recent developments in financial markets, where the CBOE Volatility Index recently traded at its lowest historic level, amid relative economic calm.²

Deal valuations ticked down nominally as a leading obstacle, cited by 15 percent of respondents compared to 16 percent a year ago. Expectations around deal multiples have remained relatively steady, as 41 percent (up from 40 percent a year ago) of respondents believe price multiples will rise for both private and public deals in the year ahead.

Interest rate concerns dropped the most precipitously, down to 11 percent from 17 percent. That decline might be tied to the fact that today’s rates—despite a series of hikes by the Federal Reserve this year—are still quite low from a historical perspective.³

While macroeconomic concerns have softened, our current survey highlights apprehensions about the potential for delays in key business-related legislation; 13 percent of corporate respondents and 11 percent of private equity respondents cite the delays as a concern. This may reflect challenges that Washington policymakers have faced with passing key business-related legislation.⁴
Industry convergence

As revealed in previous M&A trends reports, survey respondents continue to have high expectations for industry convergence in the year ahead—though mainly in related businesses or vertical integration.

There were some areas with increasing expectations for convergence, such as those between construction and energy companies and those between energy concerns and manufacturers. Respondents also anticipate more deals among retailers and technology companies.

Financial services, in aggregate, ranks high as an industry likely to experience convergence, with 38 percent of respondents predicting the sectors of private equity, asset management, insurance, real estate, and banking and securities as likely to converge. Life sciences and health care also rank high.

None of these industries emerge as surprising choices. Changes in the financial services industry are driven by the costs of technology and compliance. Another factor is margin pressure as a result of reduced fees on professional services. The situation is similar with health care, where consolidation is also being driven by pricing pressure, in some cases tied to regulatory changes.

Among the highest expectations for sector convergence are some that continue an ongoing move toward consolidation within their industries. These include health care plans and health care providers and technology companies merging with telecommunications providers.
Which industries are converging

- Energy and construction
- Construction and manufacturing
- Retail and technology
- Health care providers and plans
- Telecommunications and technology
Looking abroad

A year ago, US-based investors were looking abroad for deals in a diverse set of markets. While enthusiasm remains high this year, the areas of geographic interest appear to be shifting.

More than 90 percent of respondents say they’ll continue to engage in deal activity across borders. But dealmakers indicate they will be more selective going forward. In our most recent survey, 34 percent of respondents say they expect one-fifth or less of their deals to be internationally focused. That’s up from 26 percent of respondents from a year ago.

What’s driving this? Enthusiasm appears consistent with regard to Canada (39 percent) and the United Kingdom (29 percent), as those English-speaking countries continue to top the list of foreign targets for private equity respondents and corporates combined. Private equity respondents, however, ranked Central America (32 percent) and Australia (29 percent) as their next two targets. Interest in Central America saw a sizable jump from a year ago, when 19 percent of private equity respondents selected the region as a foreign target.

There is, however, a sharp decline in those looking to China and Japan. Only 18 percent of all respondents said they would pursue deals in China, down from 25 percent a year ago. This year, 20 percent of corporate respondents and a mere 10 percent of private equity respondents say they will look to China. Only 14 percent of all respondents say they will look to Japan, down from 24 percent in last year’s survey.

Respondents said that Europe, as a whole, is less likely to draw investment interest in the year ahead, despite consistent interest in the United Kingdom and France. Interest in investing in Germany declined marginally and there were sharp declines in those targeting companies in Italy and Spain.
For corporate respondents with revenues over $1 billion, about half (49 percent) are pursuing more than 40 percent of their deals primarily in foreign markets. That compares to one-third (34 percent) of smaller corporate respondents whose targets operate principally in foreign markets. There is a similar spread among private equity respondents. While 43 percent of firms with at least $1 billion in investments are involved in foreign deals for more than 40 percent of their transactions, only 32 percent of smaller entities are looking abroad for the same proportion of deals.
Deal spending firepower

Over the past two years, 65 percent of corporate respondents said their cash reserves have increased (up from 58 percent), and the primary intended use of that cash is for M&A deals.

In our spring 2016 report, respondents ranked organic investments as the most likely use of their cash reserves. That’s no longer the case. Predominately, companies now say they are seeking M&A opportunities, with 40 percent citing that as their number one intention. This is consistent with responses from last year. The number of respondents saying they plan to earmark the cash to invest organically in their businesses also remains high, with 33 percent of respondents citing that as a primary intended use—up from 30 percent a year ago. Markedly fewer respondents (14 percent) expect to use their cash to buy back stock.

Not only are companies more flush with cash and eager to use it to strike deals, but many also realize that they have additional financing firepower in stocks and bonds. Stocks remain at high levels, while interest rates are only modestly above their historical lows.\textsuperscript{5}
Conclusion

Companies are sending strong signals that they intend to aim for bigger M&A targets in 2018; sizable majorities of corporate respondents and private equity investors anticipate brisker activity over the next 12 months. If the legislative environment yields substantive changes, that could also lead to additional deal activity.

This could help get the M&A train back on track—both in terms of deal volume and aggregate deal size. Corporations did maintain their appetite for deals in 2017, as the overall volume of transactions increased, though the aggregate value of deals was smaller.

Looking ahead, it appears that corporate respondents are narrowing the geographic field of potential targets as significantly fewer are looking abroad for deals. In another indication of mixed signals, cash reserves are up for the second year in a row for two-thirds of corporate respondents. Corporations say that the primary intended use of their cash reserves is for M&A deals.

Acquiring technology assets now ranks number one as a strategic driver of M&A deals, and is also a major factor for industry convergence activity.

The dealmaking process will look dramatically different as innovations in diagnostic tools continue to develop. The introduction of new technology for M&A transactions has moved deals out of the spreadsheet age both for companies that have adopted the tools and those that are considering using them. These developments comprise just some of the many indicators that M&A transactions have evolved in meaningful ways.
Meet the team

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Between September 6, 2017, and September 24, 2017, a Deloitte survey conducted by OnResearch, a market research firm, polled 1,016 executives—766 at US-headquartered corporations and 250 at domestic-based private equity firms—to gauge their expectations for M&A activity in the upcoming 12 months as well as their experience with recent transactions.

All survey participants work either in private or public companies or private equity firms with annual revenues of at least $10 million. The participants hold senior ranks at least as a director in the firm and all are involved in M&A activity.

The corporate respondents represent 18 industries; technology, construction, professional services, banking and securities, and industrial and consumer products account for about half the total in aggregate. Most of the corporate respondents (57 percent) work in private concerns. One-third of the respondents work at a company with more than $10 billion in revenue, and an equal number work in a company with revenue less than $250 million, with the rest in the middle.

The private equity respondents come from a variety of funds. Almost 4 in 10 (38 percent) of the respondents work at funds with more than $1 billion in assets, and 1 in 6 (18 percent) work with funds of $3 billion and up. Almost half (46 percent) of the private equity firms have 20 or more in their portfolio; 22 percent have more than 40.
Endnotes

1. Thomson Reuters data through September 30, 2017


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