Year in Review and 2021 Outlook

Deloitte Corporate Finance LLC

2020 began promisingly for Deloitte Corporate Finance LLC, with a huge pipeline and frothy market environment. This initial outlook was turned upside down when the pandemic hit, putting many businesses on the defensive with massive reductions in travel and hospitality spending. Companies were posed with unprecedented challenges in navigating remote workforces, disrupted supply chains, highly volatile financing markets, and unpredictable revenue outlooks.

The volatile economy, political uncertainty, and social climate contributed to companies and industries propelling into survival mode, turning to defensive M&A strategies in order to safeguard their future.(1) However, these challenges also inspired profound change such as, highlighting the importance of having a transparent organization and exploring nontraditional M&A. This dynamic, growth mindset may delineate why the M&A market made a roaring return in September 2020, driven in particular by financial investors including traditional private equity firms and more recent entrants like Special Purpose Acquisition Companies (SPACs).

By the numbers

#1 2020 Global M&A Financial Advisor by deals completed (2)

49% Clients advised were private/owner managed

487 Transactions closed in the last 12 months (2)

$110.1 Aggregate Enterprise Value (USD in Billions) (2)

Source:
(1) "M&A Trends Survey: The future of M&A", Deloitte, October 2020, https://www2.deloitte.com/us/en/pages/mergers-and-acquisitions/articles/m-a-trends-report.html
(2) "2020 Global M&A report, Merger Market", January 2021, https://www.mergermarket.com/info/mergermarket-releases-4q20-global-ma-report

The outlook remains promising with 42% of executives polled at US corporations and private equity firms expecting M&A volume to return to pre-pandemic activity levels within 12 months [(1)].

As we reflect on 2020 and look forward to the future of M&A, we explore the inextricable connection between managing the current challenges of the next "normal" and preparing agilely to succeed in the year ahead.

Surveyed M&A executives indicate that deal making—particularly alternatives to "traditional" M&A—will be an important lever as businesses recover and thrive in the post-COVID economy. Looking ahead, Deloitte Corporate Finance provides insights into how leveraging alternative M&A methods can help clients navigate the crisis, enhance organizational resilience, and pursue new and disruptive growth strategies.

Representative Deloitte Corporate Finance transactions in 2020

Undisclosed veterinary provider completed a majority recapitalization with an undisclosed private equity group.
The undersigned acted as exclusive financial advisor to the veterinary provider.
Deloitte. Deloitte Corporate Finance LLC

Vital Care Home Infusion Services has completed a majority investment with LINDEN
The undersigned acted as exclusive financial advisor to Vital Care, Inc.
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McCoy NationaLease, Inc. has been acquired through multiple transactions by Airoldi Brothers, Inc., AIM Leasing Company, Brown NationaLease, Inc.
The undersigned acted as exclusive financial advisor to McCoy NationaLease, Inc.
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DHAT Digestive Health Associates of Texas, P.A. has been acquired by GI Alliance, a portfolio company of Waud Capital
The undersigned acted as financial advisor to Digestive Health Associates of Texas.
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ethos risk services has been acquired by Carousel Capital
The undersigned acted as exclusive financial advisor to Ethos Risk Services, LLC.
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City Rise, Inc. d/b/a City Rise Safety has completed a minority recapitalization with LineageCapital
The undersigned acted as exclusive financial advisor to City Rise, Inc.
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Undisclosed foreign strategic buyer has acquired an undisclosed private operator of airport retail locations.
The undersigned acted as exclusive financial advisor to private operator.
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Nature Nate's has completed a recapitalization with Wells Fargo and Private Investors
The undersigned acted as financial advisory to Natures Nate's
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Baxters has acquired Truitt Bros Inc. a subsidiary of Seneca
The undersigned acted as financial advisory to Baxters Food Group (North America).
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neighborly, a portfolio company of Harvest Partners, has acquired HouseMaster
The undersigned acted as financial advisor to Neighborly.
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healing hands. has been acquired by Careismatic Brands, a portfolio company of New Mountain Capital LLC
The undersigned acted as exclusive financial advisor to Krazy Kat Sportswear LLC (d/b/a "Healing Hands").
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DIALEXA has completed a minority recapitalization with Alturus Strategic Capital Partners
The undersigned acted as exclusive financial advisor to Dialexa, LLC
Deloitte. Deloitte Corporate Finance LLC

Hub Folding Box Company, Inc. has been acquired by gpa Global, a portfolio company of EQT
The undersigned is acting as exclusive financial advisor to Hub Folding Box Company, Inc.
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TerraSmart has been acquired by Gibraltar Industries
The undersigned acted as exclusive financial advisor to TerraSmart LLC
Deloitte. Deloitte Corporate Finance LLC

Gray has acquired Anderson Dahlen Inc.
The undersigned acted as financial advisor to Gray, Inc.
Deloitte. Deloitte Corporate Finance LLC

ThirdDimension has been acquired by Green Bay Packaging
The undersigned acted as financial advisor to Third Dimension, Inc.
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Storage Solutions simple. smart. strategic. has been acquired by MFG and Merit Capital Partners
The undersigned acted as exclusive financial advisor to Storage Solutions, Inc.
Deloitte. Deloitte Corporate Finance LLC

The employees of Global Vessel & Tank have purchased 100% of Global Vessel & Tank stock through a newly formed Employee Stock Ownership Trust
The undersigned as exclusive financial advisor to Global Vessel and Tank, LLC
Deloitte. Deloitte Corporate Finance LLC

Pioneer Metal Finishing, a portfolio company of Aterian Investment Partners, has acquired Pilkington Metal Finishing LLC
The undersigned acted as financial advisor to Pioneer Metal Finishing, LLC
Deloitte. Deloitte Corporate Finance LLC

Great Mill Rock LLC dba: Mill Rock Capital has acquired TrojanLitho.
The undersigned acted as financial advisor to Mill Rock Capital
Deloitte. Deloitte Corporate Finance LLC

Pure Speed Lightwave has been recapitalized
Financial Advisor
The undersigned acted as exclusive financial advisor to PS Lightwave, Inc,
Deloitte. Deloitte Corporate Finance LLC

Drew Foam Companies, Inc. (a portfolio company of Branford Castle, L.P.) has been acquired by Wynnchurch Capital
The undersigned acted as exclusive financial advisor to Drew Foam Companies, Inc.
Deloitte. Deloitte Corporate Finance LLC

Bitcoin Depot — Lux Vending LLC (d/b/a Bitcoin Depot) has completed a recapitalization.
The undersigned acted as exclusive financial advisor to Bitcoin Depot.
Deloitte. Deloitte Corporate Finance LLC

Prodigy has completed a Series B financing of CAD $159 million with TPG Growth & CBGF
The undersigned acted as financial advisor to Prodigy Education Inc.
Deloitte. Deloitte Corporate Finance LLC

Outlook for 2021

As Deloitte Corporate Finance looks forward to the 2021 M&A outlook, it is on the heels of a roaring recovery in M&A over the past six months. According to Mergermarket[3], while the drop from Q1 2020 to Q2 2020 in deal activity was approximately 65%, the full year ended down approximately 15% in terms of deal volume, and 21% in terms of deal value. Driving the increase during Q3 and Q4 were deal-friendly attributes in many categories: interest rates, stock market pricing, private equity firms and dry powder, and stimulus packages with related liquidity. In addition, many private business owners looked to accelerate M&A processes that they were considering over the next 24 months, driven by proposed changes to capital gains taxes under the Biden administration.

As 2021 begins, many firms are recognizing that they need to adapt to the next normal. The pandemic has caused a shift in spending patterns, favoring companies that focus on virtual consumerism (e-commerce, no-contact purchases, digital, etc.). This trend in turn is driving a promising outlook for those companies that have remained flat or grown through the pandemic, with 42% of executives polled at US corporations (1) and private equity firms expecting M&A volume to return to pre-COVID-19 activity levels within 12 months.

Finally, many of the hurdles that had to be overcome to complete deals at the start of the pandemic have been turned into advantages. The inability to meet in-person has led to quicker turnaround for management meetings, site visits have been supplemented with drones and alternative technology, and stimulus programs and lower than expected bankruptcies have reopened the lending markets. While there is an expectation that there will continue to be a volatile economic, political, and social backdrop for the foreseeable future, many strategics and private equity firms are finding creative ways to deploy capital and align themselves for emerging macroeconomic trends.

Industry outlook

Life Science & Health Care

Beginning in March 2020, COVID-19 triggered significant volume declines in elective procedures that did not rebound until Q4 2020.[4] Nevertheless, healthcare M&A activity and valuation multiples have been robust, returning to pre-pandemic levels.

Accelerated momentum continues for telehealth and digital health solutions as the patient-provider relationship evolves due to convenience and a lower cost setting outside the acute arena. At its Q2 peak, telehealth solutions were utilized for ~50% of telehealth eligible encounters. Since, telehealth visits have steadied at 11% of eligible visits -- more than 10x pre-pandemic levels.[5] We view this accelerated adoption as a long-term, normalized trend.

In parallel, the pandemic has hastened the transition of care into the home setting. After its Q2 2020 dip[6], home-based care such as home health, home infusion, hospice, and personal care quickly recovered and has sustained pre-COVID levels.

Inside the hospital, evaporation of elective surgeries, increased length of stay, and a case mix skewed toward lower margin procedures all contributed to significant pressure on hospital finances. The Coronavirus Aid, Relief, and Economic Security (CARES) Act provided a needed lifeline. However, over the long term, we expect the pandemic will drive, and possibly accelerate, the consolidation of systems nationally.

Longer term, the dynamic nature of the Life Sciences and Health Care (LSHC) industry will likely continue to drive M&A. Ultimately, services in and around LSHC are essential to the well-being of the population, with the digital transformation being a critical piece in the paradigm shift toward value-based care. US health care spend reached $3.8 trillion or 17.7% of Gross Domestic Product.[7] Efficiencies should be found to enable long-term economic sustainability. These forces catalyze capital deployment which typically leads to consolidation. Our view remains that further M&A activity will continue in areas such as:

- Home health and personal care
- Hospitals
- Ambulatory and outpatient clinics
- Physician groups
- Animal health
- Healthcare information and technology
- Medical distribution and equipment
- Pharmaceutical manufacturing, outsourcing and services

Source:

[3] "2020 Global M&A report", Merger Market, January 2021, *https://www.mergermarket.com/info/mergermarket-releases-4q20-global-ma-report*

[4] "Elective surgery volume near normal in late July, analysis finds", Healthcare Financial Management Association, July 2020, *https://www.hfma.org/topics/news/2020/07/elective-surgery-volume-near-normal-in-late-july--analysis-finds.html*

[5] "Six Month Update: National Patient and Procedure Volume Tracker, Strata Decision Technology", September 2020, *https://www.stratadecision.com/wp-content/uploads/2020/09/6-Month-Summary_National-Patient-and-Procedure-Volume-Tracker-and-Report_FINAL.pdf*

[6] "COVID-19 Shocks The US Health Sector: A Review Of Early Economic Impact", Health Affairs, December 2020, *https://www.healthaffairs.org/do/10.1377/hblog20201214.543463/full/*

[7] "National Health Expenditure Data", Centers for Medicare & Medicaid Services, January 2021, *https://www.cms.gov/Research-Statistics-Data-and-Systems/Statistics-Trends-and-Reports/NationalHealthExpendData/NationalHealthAccountsHistorical#:~:text=U.S.%20health%20care%20spending%20grew,spending%20accounted%20for%2017.7%20percent*

Business and Financial Services

Buyers are looking for differentiation through technology and the readiness of management teams to evolve with the increasing need for security and automation.

Fragmented segments continue to consolidate. Small business owners increasingly need to either invest in technology and infrastructure to serve clients, making strategic alternatives necessary and comparatively attractive.

Private equity groups continue to gravitate toward companies in niche segments with recurring revenue, strong and expanding margins, and compelling acquisition pipelines.

Strategic buyers continue to acquire where they can create cross selling opportunities and integrate nimble, innovative ways of doing business.

In 2020, strong business performance was highly correlated with nimble operations and leadership teams. Winning attention from investors were specialized industry players with the scale and infrastructure to manage the unknown with the smaller operations playing catch up.

Technology, Media & Telecommunications

Automation/Artificial Intelligence (AI)/Machine Learning (ML)
Automation, AI, and ML are some of the biggest technology trends; during 2021, they will likely become some of the most valuable tools to quickly and accurately interpret information. The volume of data being generated and collected on all aspects of the economy will continue to increase. AI/ML algorithms will become better informed and increasingly sophisticated in their problem solving. Beyond mission critical applications, human-oriented and human-driven workflows are being automated at a rapid clip.

Mobile Commerce & Ad Tech
The shift of consumers using their smartphones to search for and make purchases rather than switching to a computer will likely continue to increase. Moreover, with increased use of smartphones, they have become ideal tools for targeted and personalized advertising – technology companies will likely continue to create business opportunities in this ecosystem.

Enterprise Apps
With both consumer and enterprise applications generating more integrations and application programming interface (API) connectivity, we expect to see more enterprise integrations borrowed from mainstream consumer tech, such as push notifications, voice search options, and intelligent suggestions from AI/ML algorithms.

Consumer

COVID-19 drove a ~5 year acceleration in the expected E-commerce share of grocery sales, rising to more than 10%.[(8)A] We expect new shopping habits to endure even as vaccine distribution begins. Beneficiaries of the new economic climate will likely be retailers with strong E-Commerce platforms, grocery delivery businesses, and brands with developed Direct to Consumer (DTC) strategies. Well- capitalized Consumer Packaged Goods (CPGs) will continue to seek acquisitions of strong DTC brands.

Due to gym and other non-essential business closures, fitness out of the home has largely replaced group exercise. This will likely persist in 2021 and benefit companies and products that allow users to exercise by themselves while still connecting with instructors or others that aren't co-located.

Plant-based foods continue to grow in popularity. More than 50% of consumers have tried plant-based meat and oat milk has experienced the fastest growth of any food category, at more than 200%, according to Nielsen. [(8)B] Investment capital continues to flood into the plant-based nutrition space.

Mission-driven businesses continue to attract interest from both private equity and strategic acquirors. According to a recent Wunderman Thompson survey, 85% of Gen Z consumers believe brands should be about something more than profit[(8)C].

Source:
[(8)ABC] "Consumer Trends 2021", The New Consumer, January 2021, https://newconsumer.com/trends/

Industrials

2021 indicates strong investor interest in growth capital opportunities and partnering with business owners that have the ability to take advantage of the current economic environment to grow.

Large industrial companies remain active in M&A, but largely focused on highly strategic investments and portfolio realignment. Private equity groups are also showing a high level of interest, similar to pre-COVID levels.

Generally, it appears that strategic acquirors are more open to share strategy and thought process than previously. This may provide opportunities to discuss specific acquisition ideas before a seller makes a decision on how and when to go to market.

Many industrial sectors slowed in early Q2 2020 and while some sectors have ramped back up with notable resiliency or were unaffected, others have experienced a slower recovery. We are continuing to see a focus on a firm's operational agility and a material emphasis being placed on a firm's ability to forecast with quality and accuracy.

Private Equity

Private Equity Groups continue to sit on an unprecedented amount of dry powder[9A], which they will need to deploy in the coming year in order to fulfill limited partnership commitments. We expect this dynamic will drive strong buyout activity through 2021.

While many sponsors did finish the year with a healthy number of acquisitions completed, most preferred to deploy capital though add-on acquisitions rather than platform investments. In 2020 add-ons accounted for 72.5% of all buyouts[9B]. We believe Private Equity groups will look to deploy more capital in platform companies through 2021.

Due to a competitive deal making environment and a scarcity of high-quality pandemic resistant companies for sale, we believe median valuation multiples will remain elevated, driven by frothy valuations in the Technology and Consumer sectors. In 2020, valuations for Private Equity buyouts in the Consumer sector posted an annual increase in valuations of 95%[10].

In addition to elevated valuation multiples, Private Equity Groups are differentiating themselves through highly developed sector thesis, streamlined diligence processes, and aggressive timelines from bid to close.

Given many transactions were put on hold in 2020, we expect to see an increased level of Private Equity exit activity, specifically in the Business Services, Consumer, Healthcare, and Technology sectors.

Source:
[9AB] "2020 Annual US PE Breakdown", Pitchbook, January 2021, https://pitchbook.com/news/reports/2020-annual-us-pe-breakdown
[10] "Private Equity Ends 2020 on a High", White & Case, January 2021, https://mergers.whitecase.com/highlights/private-equity-ends-2020-on-a-high

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