M&A emerges from quarantine

M&A strategies to thrive in the post-pandemic environment
Deloitte Global M&A Services

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In a year besieged by pandemic uncertainties, M&A rode a roller coaster. In the first half of the year, lockdowns led to a sharp dive. But as soon as these began to ease, M&A soared back up. Globally, companies announced a record $1.4 trillion worth of deals in the post-lockdown months from June to October 2020, 84 per cent higher than in the first five months of the year, leading to a total value of $2.2 trillion worth of deals in the first 10 months of the year. The positive news on COVID-19 vaccines has also given a significant boost to corporate confidence – over $40 billion worth of deals were announced in the week the first news about the high efficacy of coronavirus vaccines was reported.

All regions and sectors benefitted from this resurgence. In particular, there was a strong uptick in the mega-deal (>5bn in value) category (figure 1). Many were all-stock deals, signalling that acquirers want to preserve cash, in a way acknowledging some of the integration risks brought on by economic uncertainties. These extraordinarily difficult times have created unique opportunities. While some of the M&A activity recorded was due to companies resuming deals put on hold during the economic freeze generated by the different national lockdowns, a good proportion also reflected company efforts to transform and thrive in the post-pandemic world. This is why in recent months we have seen not just traditional consolidation-driven M&A but also non-traditional deals, such as cross-sector alliances, co-investments with private equity, divestments of prized assets, deals to secure supply value-chains, and disruptive M&A deals to acquire innovative and sustainable technologies.

The long road to post-pandemic recovery has just begun. Given the high stakes, in the Autumn 2020 edition of the Deloitte European CFO survey, we asked around 1,500 CFOs across 17 countries about their M&A objectives, strategic priorities, execution risks and post-deal value-creation challenges. In this report, we examine the findings of the survey and present implications for dealmakers.
M&A during COVID-19 times

Breakdown by industry sectors

36,716 DEAL VOLUMES (JAN-OCT 2020)

$2.2trn DISCLOSED DEAL VALUE (JAN-OCT 2020)

Breakdown by deal size

321 DEALS

$500m

276 DEALS

$1bn

69 DEALS

$5bn

$100bn

Breakdown by phases

Pre-COVID-19
$557bn (25%)

Lockdown
$220bn (10%)

Post Lockdown
$1.4trn (65%)

Source: Deloitte analysis.
CFO sentiments on drivers for M&A

In order to ascertain the headwinds and tailwinds for M&A, we asked CFOs to rank the internal and external factors that will influence their M&A strategies and priorities within next 12 months (figure 2).

TAILWINDS – CONFIDENCE IN FINANCIAL STRENGTH

Around 83 per cent of the CFOs reported high levels of confidence in the strength of their balance sheets, and this was the case particularly with CFOs from the financial services, automotive and professional services sectors. The confidence can partly be explained by the long-term shift towards capital and cash preservation that followed the 2008 financial crisis. Since then, the corporate sector has been steadily increasing their cash reserves, and in Europe, at the end of the second quarter of 2020, EURO-STOXX 600 non-financial companies had a record $1.07 trillion in cash and short-term investments. On the other hand, CFOs within companies that are not confident about their financial strength indicated they are planning to pursue divestments of non-core assets to shore up their balance sheets.

In addition, with no signs of an imminent reversal of the current highly accommodative monetary policy, around 73 per cent of CFOs report that they are confident about the availability of credit. Many listed companies in Europe took advantage of the favourable credit markets to raise around $1.04 trillion in investment-grade bonds this year. Others took advantage of specific government interventions to strengthen their finances, such as emergency measures providing extended credit lines, liquidity guarantees, or deferrals of taxes and social security contributions.

HEADWINDS – THE ECONOMY AND REGULATORY HURDLES

When it comes to headwinds for M&A, it comes as little surprise that the majority of CFOs are concerned about the external environment. Around 40 per cent of CFOs are not confident that there will be an economic recovery within the next 12 months, and almost half the respondents (44 per cent) are wary about their ability to overcome political and regulatory hurdles to complete M&A transactions. Earlier this year the EU Commission announced a broadening of member state referral systems concerning mergers, while in the UK the government has also announced new proposals to safeguard sensitive UK assets from being acquired by overseas companies. Despite the tailwinds, we should expect a degree of caution and prudence as companies evaluate deal opportunities.

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FIGURE 2

Factors influencing M&A decisions

How confident are you of the following factors that could influence your M&A decision?*

<table>
<thead>
<tr>
<th>Factor</th>
<th>Highly confident</th>
<th>Moderately confident</th>
<th>Not confident</th>
</tr>
</thead>
<tbody>
<tr>
<td>Your balance sheet is strong with adequate cash reserves</td>
<td>42%</td>
<td>41%</td>
<td>18%</td>
</tr>
<tr>
<td>You have the right internal capabilities for deal execution and post-deal transformation</td>
<td>30%</td>
<td>50%</td>
<td>20%</td>
</tr>
<tr>
<td>Credit will be available at favourable conditions</td>
<td>27%</td>
<td>46%</td>
<td>27%</td>
</tr>
<tr>
<td>There will be growth opportunities in your sector</td>
<td>26%</td>
<td>48%</td>
<td>27%</td>
</tr>
<tr>
<td>Targets will be available at attractive valuations</td>
<td>23%</td>
<td>49%</td>
<td>28%</td>
</tr>
<tr>
<td>Strong interest from private equity buyers</td>
<td>18%</td>
<td>42%</td>
<td>39%</td>
</tr>
<tr>
<td>Economy will recover within next 12 months</td>
<td>15%</td>
<td>45%</td>
<td>40%</td>
</tr>
<tr>
<td>Political and regulatory hurdles can be overcome</td>
<td>14%</td>
<td>42%</td>
<td>44%</td>
</tr>
</tbody>
</table>

*Percentages calculated exclude respondents answering, “Do not have a view”. The results are unweighted.
Due to rounding, numbers may not add up to 100 per cent.

Rethinking the strategic role of M&A from respond to recover and thrive

The post-pandemic world is expected to unleash structural and systemic changes, and it is widely expected that recovery will be highly asymmetric across regions and sectors. Companies will need to decide the direction of their strategy, identify the new capabilities required and prioritise the markets where they need to operate in order to drive growth and profitability.

In a recent Deloitte report called “Charting new horizons”, an M&A strategy framework was presented to help companies prioritise their strategic choices and develop a pathway through the three phases of a crisis: from responding to the shock, to recovering and finally thriving in the new business environment. Redefining M&A plans in terms of these scenarios and choices will bring much needed clarity of purpose while confronting uncertainties (figure 3).

In order to understand the role of M&A in companies’ journeys, we used the survey results to reconstruct the framework, creating two indices that measure how companies score on the two critical dimensions: ‘level of impact’ and the ‘ability to act’. We asked CFOs to prioritise M&A objectives for the short (< 6 months) and medium (6-12 months) term and then evaluated their responses against the indices. This allows for a determination of how the strategies are playing out based on the pathways different companies are choosing as they move from respond to recover and thrive.

The analysis shows CFOs are using a combination of defensive and offensive strategies to safeguard their position in the market, accelerate recovery and position themselves to achieve market leadership (figure 4).

FIGURE 3

Future of M&A strategy framework

Typical level of impact assessment: Consider the impact of pandemic on economic recovery and market supply/demand dynamics, your people, customers and competitive environment.

Typical ability to act assessment: Consider your liquidity position, balance sheet strengths and ability to raise capital from the markets in relation to the resilience of your business operating model and those of your suppliers and partners.

Source: Deloitte 2020 "Charting New Horizons".
We found that CFOs of companies more severely impacted by the crisis were focused on survival and prioritised defensive measures to salvage value through the rapid sale of assets, divestment of non-core assets and portfolio restructuring. Many companies whose business models have been adversely impacted but have the ability to respond have indicated they want to expedite synergy capture from recent acquisitions to bolster their balance sheet, acquire technology assets to accelerate digital transformation, and pursue strategic alliances with a wide range of players to set them on the path to recovery.

On the other hand, companies that were relatively less affected and also feel confident about their ability to respond, prioritised M&A objectives in line with transformation and growth aspirations. These included acquiring assets to close gaps in their portfolio, driving their sustainability agenda, building supply-chain resilience and acquiring disruptive innovation assets to enter into new growth segments.

On balance, 59 per cent of the respondents selected strategies related to offensive M&A, while 41 per cent selected defensive ones. Companies are increasingly pursuing non-traditional M&A activities, such as joint ventures, alliances, disruptive M&A and venture investments in sustainable assets (32 per cent), in addition to portfolio restructuring activities leading to divestments (21 per cent) and more traditional M&A deals, such as consolidation plays (47 per cent).

We take a detailed look into all these M&A strategies in the breakout box on page 8 (figures 5-7).

Level of impact assessment: Index constructed from questions relating to expectations about growth of revenues, recovery to pre-pandemic revenue levels and macroeconomic recovery.

Ability to act assessment: Index constructed from questions on confidence about balance sheet strength, the ability to access credit, internal capabilities for deal execution and availability of targets.

Source: Author’s calculations based on data from Deloitte European CFO survey, Autumn 2020.
M&A priorities and pathways

Below we outline a range of strategies, highlighting their role in different phases of the journey from respond to recover and thrive.

From respond to recover

Companies that have been severely impacted by the crisis and are in a financially vulnerable position are taking decisive measures to secure their survival. Meanwhile, companies where the impact has been less severe have indicated they plan to use M&A to safeguard markets and build operational resilience.

FIGURE 5
Pathways from respond to recover

<table>
<thead>
<tr>
<th>M&amp;A OBJECTIVES</th>
<th>PATHWAYS FROM RESPOND TO RECOVER</th>
</tr>
</thead>
<tbody>
<tr>
<td>54%</td>
<td>Expedite the synergy capture of recently completed deals</td>
</tr>
<tr>
<td>46%</td>
<td>Acquisitions to accelerate digital transformation</td>
</tr>
<tr>
<td>43%</td>
<td>Pursue strategic alliances with corporate peers and ecosystem startups</td>
</tr>
<tr>
<td>38%</td>
<td>Portfolio optimisation and divestment of non-core assets</td>
</tr>
<tr>
<td>33%</td>
<td>Rapid sale of distressed assets</td>
</tr>
</tbody>
</table>

This objective emerged as the overall top CFO priority. Companies that have recently completed acquisitions need to deliver post-deal shareholder value under challenging conditions. They need to take decisive measures to rapidly integrate and capture deep synergies. Deloitte analysis shows well-executed integrations can deliver on average 1.3 times more benefits than the publicly announced synergies.12

This was a high priority for companies whose existing business models were adversely impacted by the pandemic. It featured strongly with companies in retail, consumer goods, travel and tourism sectors. Many will seek to acquire technologies in order to rapidly transition to digital operating models in response to lasting changes in customer behaviours.

Many have indicated they are considering alternatives to traditional M&A activities to reduce risk and capital outlays as the search for value intensifies in a low-growth environment. This objective featured strongly in the transportation and financial services sectors. In the longer term, the acceleration of sector convergence will lead to unique opportunities that can be captured through cross-sector corporate alliances, as well as with startups from the innovation ecosystem.

Portfolio optimisation is essential in times of crisis to increase capital efficiency and free up scarce resources. Well-planned divestments of non-core assets can create greater shareholder returns for both buyers and sellers and send a strong signal of intent to the markets.13

Financially stressed companies may need to consider radical actions, including distressed asset sales, to salvage value from loss-making divisions and preserve a viable core business. In times of crises, disposal of distressed assets requires the utmost speed of execution to maximise value. This objective featured strongly with companies in the transport and travel and tourism sectors.

Source: Deloitte analysis.
From recover to thrive

Companies with a strong balance sheet but expecting significant degree of structural disruption have indicated they wish to use M&A to rebuild supply-chain links and accelerate the long-term transformation of their business models. Meanwhile, for companies that are financially resilient and strategically well placed, this crisis presents unique opportunities to use disruptive M&A strategies to invest at the edge of their business and position themselves to become market leaders in years to come.

FIGURE 6
Pathways from recover to thrive

<table>
<thead>
<tr>
<th>M&amp;A OBJECTIVES</th>
<th>PATHWAYS FROM RECOVER TO THRIVE</th>
</tr>
</thead>
<tbody>
<tr>
<td>49% Acquisition of assets to fill gaps in the core portfolio</td>
<td>Nearly half the CFOs indicated they want to pursue opportunistic deals to fill gaps in their product and service portfolio. Companies should also consider co-investments with private equity to pursue deals that align with core strategic priorities. This objective featured strongly with companies in the energy/mining/utilities and life sciences sectors.</td>
</tr>
<tr>
<td>41% Acquisitions to consolidate the sector</td>
<td>Companies should actively scan the market for underperforming peers and high potential startups that are struggling under market constraints. Valuations for many such businesses are down, and sellers have readjusted expectations, thus providing a unique opportunity to acquire and consolidate the market at attractive prices. This featured strongly with companies in the industrials and life sciences sectors.</td>
</tr>
<tr>
<td>39% Acquisitions to drive the sustainability agenda</td>
<td>The pandemic marked a step change in corporate expectations with regards to impact on sustainable agenda, from ethical sourcing and production to mitigating environmental impact and showing community leadership. M&amp;A activities provide an expedited pathway for companies to progress their sustainability goals. This objective featured strongly with companies in the construction and consumer business sectors.</td>
</tr>
<tr>
<td>31% Acquisitions of assets to build supply-chain resilience</td>
<td>In the post-COVID-19 environment, restarting and normalising the supply chain will be of importance to most companies. M&amp;A activities can help restore and protect vital supply-chain links, as well as help build new and sustainable supply-chain systems. This objective featured strongly with companies in the consumer business sector.</td>
</tr>
<tr>
<td>30% Acquisition of disruptive innovation assets to enter new growth segments</td>
<td>Disruptive technologies will have a major influence on post-pandemic structural change in all sectors. Disruptive M&amp;A strategies will not only help businesses acquire such innovative assets, but also give them access to talent and digital operating models, which are essential for the long-term transformation of their businesses. This objective featured strongly with companies in the technology and financial services sectors.</td>
</tr>
</tbody>
</table>

Note: The respective percentages denote total respondents who selected this option as a priority within next 12 months and was calculated excluding respondents answering, “Do not have a view”, as well as respondents answering “not a priority” to all the strategies.

Source: Deloitte analysis.
M&A priorities and pathways
CFO M&A objectives in order of priority (over next 12 months)

- **Defensive M&A strategy**
  - High priority (< 6 months)
  - Medium priority (6-12 months)

- **Offensive M&A strategy**
  - High priority (< 6 months)
  - Medium priority (6-12 months)

**SECTORS**

<table>
<thead>
<tr>
<th>Sector</th>
<th>Top 3 M&amp;A Objectives by Priority</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Tourism &amp; travel</strong></td>
<td>Expedite the synergy capture</td>
</tr>
<tr>
<td></td>
<td>for recently completed deals</td>
</tr>
<tr>
<td></td>
<td>Acquisition of assets to fill</td>
</tr>
<tr>
<td></td>
<td>gaps in the core portfolio</td>
</tr>
<tr>
<td></td>
<td>Pursue strategic alliances with</td>
</tr>
<tr>
<td></td>
<td>corporate peers and ecosystem</td>
</tr>
<tr>
<td></td>
<td>startups</td>
</tr>
<tr>
<td></td>
<td>Acquisition of competitors to</td>
</tr>
<tr>
<td></td>
<td>accelerate consolidation</td>
</tr>
<tr>
<td></td>
<td>Acquisition of assets to drive</td>
</tr>
<tr>
<td></td>
<td>the sustainability agenda</td>
</tr>
<tr>
<td></td>
<td>Portfolio restructuring and</td>
</tr>
<tr>
<td></td>
<td>divestment of non-core assets</td>
</tr>
<tr>
<td></td>
<td>Sale of distressed assets to</td>
</tr>
<tr>
<td></td>
<td>rapidly strengthen balance sheet</td>
</tr>
<tr>
<td></td>
<td>Acquisition of assets to build</td>
</tr>
<tr>
<td></td>
<td>supply-chain resilience</td>
</tr>
<tr>
<td></td>
<td>Acquisition of disruptive</td>
</tr>
<tr>
<td></td>
<td>innovation assets to enter new</td>
</tr>
<tr>
<td></td>
<td>growth segments</td>
</tr>
</tbody>
</table>

**Sectors**

- **Tourism & travel**
  - Expedite the synergy capture
  - Accelerate digital transformation
  - Divestments of non-core assets

- **Transport & logistics**
  - Pursue strategic alliances
  - Expedite the synergy capture
  - Acquisitions to accelerate digital transformation
  - Sales of distressed assets

- **Construction**
  - Expedite the synergy capture
  - Fill gaps in core portfolio
  - Drive the sustainability agenda

- **Retail**
  - Accelerate digital transformation
  - Expedite the synergy capture
  - Pursue strategic alliances

- **Consumer goods**
  - Expedite the synergy capture
  - Accelerate digital transformation
  - Build supply-chain resilience

- **Energy, utilities, mining**
  - Fill gaps in core portfolio
  - Expedite the synergy capture
  - Acquire competitors to consolidate sector

- **Automotive**
  - Expedite the synergy capture
  - Divestments of non-core assets
  - Pursue strategic alliances

- **Business & prof. services**
  - Expedite the synergy capture
  - Acquire competitors to consolidate sector
  - Pursue strategic alliances

- **Industrial products & serv.**
  - Expedite the synergy capture
  - Fill gaps in core portfolio
  - Acquire competitors to consolidate sector

- **TMT**
  - Expedite the synergy capture
  - Fill gaps in core portfolio
  - Innovation assets to enter new growth segments

- **Life sciences**
  - Fill gaps in core portfolio
  - Acquire competitors to consolidate sector
  - Accelerate digital transformation

- **Financial services**
  - Expedite the synergy capture
  - Pursue strategic alliances
  - Divestments of non-core assets

**FIGURE 7**

M&A priorities and pathways
CFO M&A objectives in order of priority (over next 12 months)

Source: Deloitte analysis.
Execution priorities – How will your next deal differ?

The pandemic has fundamentally changed the environment for transacting M&A deals. Well-enshrined features such as onsite visits for the purposes of conducting operational due diligence and face-to-face conference-room negotiation marathons will probably no longer be standard. Instead, the use of digital and analytical tools is likely to remain an integral part of the entire M&A process, from sourcing and execution, all the way to post-deal value creation. We asked CFOs about deal execution priorities, and their responses show they are adapting to these shifts (figure 8).

**FIGURE 8**

M&A deal execution priorities

<table>
<thead>
<tr>
<th>Must-have</th>
<th>High importance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Confidence in financial projections and growth plans of the target</td>
<td>17%</td>
</tr>
<tr>
<td>Robust post-COVID scenario planning</td>
<td>18%</td>
</tr>
<tr>
<td>Establishing trust with stakeholders (e.g. consumer, governments, regulators etc.)</td>
<td>19%</td>
</tr>
<tr>
<td>Effective remote deal diligence and risk management process</td>
<td>15%</td>
</tr>
<tr>
<td>Accelerated post-merger integration and realisation of synergies</td>
<td>16%</td>
</tr>
<tr>
<td>Cultural integration amidst changing working patterns</td>
<td>14%</td>
</tr>
<tr>
<td>Safeguard against threats of cyber-attack and deal leakages</td>
<td>15%</td>
</tr>
</tbody>
</table>

*Percentages calculated exclude respondents answering, “Do not have a view”.
Source: Deloitte European CFO survey, Autumn 2020.

The use of digital and analytical tools is likely to remain an integral part of the entire M&A process, from sourcing and execution, all the way to post-deal value creation.
FORECASTING MAY REQUIRE NEW MATHS:
Nearly 60 per cent of CFOs acknowledge that gaining confidence in the finances and growth plans of possible targets, and robust post-COVID scenario planning, are top execution priorities. Indeed, given the current unprecedented circumstances, historical financial data may become less reliable for forecasting purposes. Instead, companies may want to focus on scenarios and projections across a range of pandemic/recession durations. The due diligence process may also need to be extended, focusing on areas where vulnerabilities may have been exposed, including the impact of changing scenarios on valuations, supply chains or IT infrastructure.

TRUST TAKES CENTRE STAGE:
The pandemic has firmly put the spotlight on trust, and it has emerged as a fundamental corporate objective. Nearly a fifth of CFOs have identified it as a must-have, the highest share across the ‘must-have’ priorities. In our recent study, “Future of Trust”, we have identified the four human dimensions of stakeholder trust: physical, emotional, financial and digital. Building trust while conducting deals in a virtual environment is difficult, and so leaders need to inspire confidence by engaging with the financial, well-being and safety concerns of their teams – and trusting them to do their jobs. If done well, this approach has the potential to accelerate a company’s recovery and enable it to thrive and shape the future.

The pandemic has firmly put the spotlight on trust, and it has emerged as a fundamental corporate objective.

REINVENTING THE M&A PROCESS:
About 52 per cent of respondents have highlighted having effective remote deal diligence processes as a priority. The virtual environment is expected to remain central to deal-making for the foreseeable future. The sheer volume of deals done this year means companies have already started using virtual and digital tools in the M&A process. The consistent use of predictive analytics, artificial intelligence and automation technologies in the post-deal value-creation process can help extract deeper insights in business domains, identify risks and uncover new synergy opportunities. Leaders need to pay particular attention to ensure cultural integration is handled sensitively in the virtual environment.

CYBER RESILIENCE:
Protecting against cyber risks is, by contrast, not particularly high on the agenda, with fewer than half the European CFOs considering it an important priority. In our recent Future of M&A Trends survey, in which we surveyed over 1,000 M&A executives at US companies, around 51 per cent identified cybersecurity threats as their top concern during the M&A process. The growth in virtual execution means cyber data breaches could have dire implications for M&A. If sensitive data is compromised, it could impact deal assessment and valuations, and increase the risk of operational disruptions, regulatory fines, loss of stakeholder trust – and potentially scupper the deal itself. As M&A activities continue to increase, we expect European companies will start giving cyber risk management a higher priority.
Conclusion

The COVID-19 pandemic has unleashed a process of Schumpeterian ‘creative destruction’ to which no sector is immune. The dismantling of old structures and business models is opening up new growth opportunities.

In order to thrive in the post-pandemic world, companies therefore need to reinvent themselves. The survey results confirm that M&A is likely to play a major role in this transformative process. Companies have the daunting task of navigating their core businesses amid major uncertainties, while remaining alert to new growth M&A opportunities. They must also integrate these acquisitions and deliver returns under challenging conditions.

In a post-pandemic world, companies will also be under pressure to demonstrate the long-term benefits of their M&A activities through stakeholder value creation. In addition to traditional M&A, a wide range of inorganic growth strategies, such as cross-sector alliances, co-investments with private equity, venture investment in disruptive technologies and partnerships with governments, have become important in this process.

Industry leadership needs to consider, too, the environmental and societal impact of their actions and the ethical use of data in order to inspire trust across a wide coalition of stakeholders, including shareholders, governments and regulators. Well-planned, bold moves will enable companies to cement market leadership together with lasting societal benefits.
1. The actual disclosed deal value was $776.69 trillion for the period January to May 2020 and $1,425.25 trillion for the period June to October 2020, which gives an increase of 83.5045% rounded off to 84%. Deloitte analysis based on data from Thomson One database, accessed 13 November 2020.


5. Since 2015, Deloitte has conducted the European CFO survey, giving voice twice a year to chief financial officers from across Europe. Besides providing an overview of business sentiment in Europe, each edition focuses on a topical issue. The Autumn 2020 edition focused on M&A. The data was collected in September 2020, and 1,348 CFOs in 18 countries and across 12 major industries responded to the questions in this article. For further detail please visit: www.deloitte.com/europeanCfosurvey


11. To assess the level of impact, we constructed an index from questions on expectations about growth of revenues, recovery to pre-pandemic revenue levels and macroeconomic recovery. To assess the ability to act, we constructed an index from questions on confidence about balance sheet strength, the ability to access credit, internal capabilities for deal execution and availability of targets.


17. The economist Joseph Schumpeter coined the term ‘creative destruction’ in 1942 to draw attention to the incessant product and process innovation mechanism where status quo is replaced by the new, but over time this process accounts for more than half of the productivity growth in an economy. Ricardo Caballero, Creative destruction, MIT, 2010, https://economics.mit.edu/files/1785, accessed 18 November 2020.
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