TRUSSBRIDGE

A Look into the M&A Landscape in *"A Post Pandemic World"*

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Strategic Financial Advisory | Mergers & Acquisitions Advisory
Capital Markets Advisory | Capital Restructuring Advisory

In Brief…

Sellers / Targets | Buyers / Investors

Deal Lifecycle

Origination

M&A activity has been adversely affected by the widespread deterioration of the global economy with several announced transactions being pulled or delayed.

… Private market opportunities will principally originate from businesses who adapted well to the changing market dynamics or those who have been significantly affected by COVID-19…

… governments to focus more on Privatizations and Public Private Partnerships going forward, which will represent another driving factor for M&A activity.

We are seeing firsthand a growing adherence to the motto that 'Cash is King'….

… which further pushes the M&A landscape towards an opportunistic buyer's market.

Evaluation

As economic conditions continue to deteriorate, cost of capital will increase, reflecting the overall sentiment of uncertainty, and subsequently result in more depressed valuation levels.…

… adding another hurdle to the overall M&A landscape as valuation gaps between transaction parties will continue to widen.

Execution

Accordingly, we believe more transactions will be based on risk-adjusted investment structures.

Furthermore, transaction execution will entail more scrutinized due diligence processes.…

… and increased reliance on non-physical / virtual aspects of the transaction execution…

Completion

Transaction parties would also need to consider a longer post signing / closing period.

Convincing transaction financiers may prove to be tougher with longer approval periods.…

… and securing regulatory approvals or consent may take longer in the near term.

The economic impact of COVID-19 only really started to be felt in February 2020, when China virtually shut down. From that moment on, significant uncertainty was introduced into the global economy.

M&A activity has been adversely affected by the widespread deterioration of the global economy with several announced transactions being pulled or delayed.

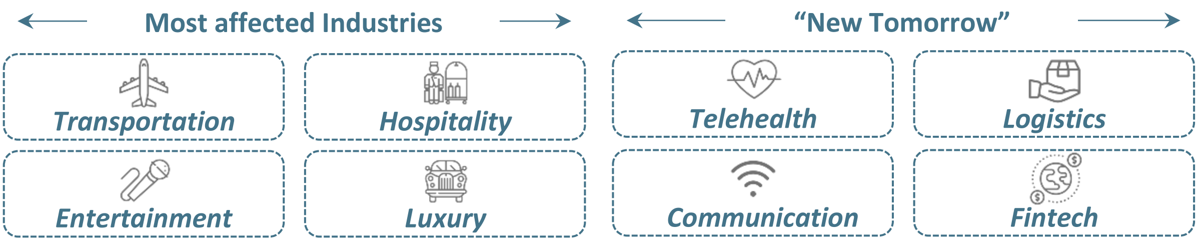
Only ***30%***
Cross-Border M&A Globally

27% *Decline in Transaction Value*

Over US$217 billion worth of M&A transactions were announced globally in the first quarter of 2020 – a 27% decline in value compared to the same period in 2019 and arguably the slowest performance in the past 6 years. Moreover, the market saw less mega deals, cross-border and private equity driven transactions.

Until economic conditions stabilize and start to recover, **private market opportunities will principally originate from businesses who adapted well to the changing market dynamics or those who have been significantly affected by COVID-19.**

Indeed, a gradual return in economic activity is expected by year-end 2020 with a relatively long recovery period as the full economic and business impact from the pandemic will take time to be captured and addressed. As companies increasingly come to grips with the impact of COVID-19 on their operations and capital requirements, M&A opportunities will arise especially from cash-strapped companies operating in sectors that have been directly affected by COVID-19 (i.e. transportation industry, hospitality, social entertainment or the luxury industry). Simultaneously, we expect more growth opportunities arising from sectors perceived to be drivers of the “New Tomorrow” (i.e. telehealth, logistics, last mile connectivity, digital technology, fintech, etc.…) as investors seek to capitalize on the growing demand expected in those relevant sectors.

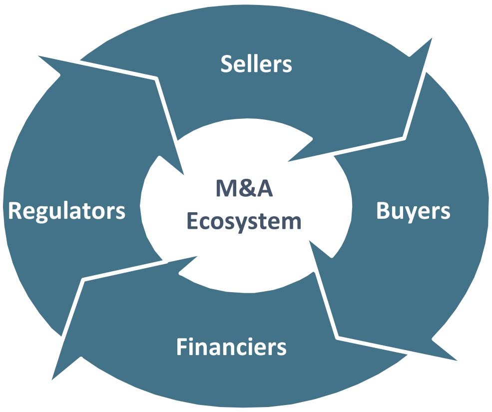


We have been observing governments pouring billions of dollars into the economies in emergency stimulus packages to help offset the impact of the COVID-19 outbreak. Gulf Arab states are also facing additional challenges arising from the declining oil prices, which have been driving them to tap international markets to raise debt to meet their funding needs.

We expect these governments to focus more on Privatizations and Public Private Partnerships going forward, which will represent another driving factor for M&A activity.

The appetite of the private sector to participate in these opportunities might not be robust in the short-term due lack of clarity of the impact from the pandemic on the business environment as well as uncertainty from regulatory frameworks. However, as the impact from the pandemic wanes, these would become more attractive investment opportunities in the medium-to-long-term.

These evolving dynamics will result in fundamental changes to the M&A ecosystem, impacting all stakeholders.



We are seeing firsthand a growing adherence to the 'Cash is King' motto.

In response to the market situation, more companies are preserving and building cash reserves which, in our view, will help them manage and minimize the financial and liquidity risks ahead. This will also support their position to undertake acquisitions.

'Cash is King'

Moreover, the market is already witnessing pockets of capital being raised globally to identify and fund investment opportunities as and when they arise, **which further pushes the M&A landscape toward an opportunistic buyer's market.**

For a while, sellers have enjoyed the ability to dictate and push their commercial terms to buyers. We foresee a switch to a market favoring buyers. Well-equipped equity investors, who possess strong balance sheets and are cash rich will enjoy a strong position in evaluating and undertaking M&A opportunities.

As economic conditions continue to deteriorate, cost of capital will increase, reflecting the overall sentiment of uncertainty, and subsequently result in more depressed valuation levels.

This surge in cost of capital will not fully soften until we witness less volatility and a more stable outlook. Until then, we expect valuation discussions to be based to the extent possible on projected cash flows, with considerable scrutiny and discount applied to forecasted levels, rather than public comparable peers or pre-COVID-19 precedent transaction pricing.

Valuation gaps will add another hurdle to the overall M&A landscape and limit the ability to agree middle grounds, especially when dealing with family-owned businesses. Accordingly, we believe more transactions will be based on risk-adjusted investment structures.

Buyers will increasingly seek mezzanine and / or other structured equity structures as a way to offer more "clear-cut" returns to investors while allowing sellers to raise the sought capital at the time needed. These financial structures would allow both parties to simultaneously address market concerns and prevailing risks while meeting the various parties' valuation expectations.

Risk-Adjusted Transaction Structures

Mezzanine Investments	Structured Equity Investments	Deferred Payments / Earn-Outs

Additionally, the ability of sellers to utilize locked-box pricing mechanisms and essentially push the economic risk of the business onto the buyer until the completion of the transaction will increasingly wane. Pricing adjustment mechanisms reflecting the state of the business as at the date of closing will become a more likely transaction structure given buyers' inability to fully predict near future conditions under COVID-19. Therefore, sellers may have to bear the economic risks until the completion of the transaction.

Similarly, buyers may also be more inclined to request a deferred payment or earn-out types of structures based on the achievement of future agreed terms, forcing sellers to remain committed to the business. These structures would allow both buyers and sellers to share the inherent potential market / external risks of the business.

Likewise, sellers will seek to minimize their exposure to unpredictable market conditions and demand that COVID-19 or similar pandemics are excluded from Material Adverse Clauses to ensure buyers cannot easily withdraw from previously binding commitments.

These conditions would result in more likely disagreements in the adjustments computation and increase the risk of any transaction closing.

Furthermore, transaction execution will entail more scrutinized due diligence processes and increased reliance on non-physical / virtual aspects of the transaction execution.

In particular, buyers will need to increasingly focus on certain due diligence matters:

Contractual Arrangements	▪ *Ascertain any exposure to non-performance or termination of third-party contracts under any force majeure or material disruption clauses.*
Financing Contracts	▪ *Scrutinize financing agreements in more detail in order to avoid any future breach of covenants or inadvertently triggered acceleration of repayment clauses.*
Workforce Disruption	▪ *Ensure that any new commitment toward the workforce considering COVID-19 measures, although not incurred yet, are fully reflected in any valuation exercise clauses.*

On the back of more complex transaction execution and structures being negotiated, **transaction parties would also need to consider longer post signing / closing period.**

Convincing transaction financiers may also prove to be tougher with longer approval periods. Hence buyers should evaluate the impact of higher cost of financing and / or alternative sources of funding.

Additionally, securing regulatory approvals or consent may take longer in the near term. However, we appreciate that it is in the regulator’s interest and indirectly the government, to stimulate a healthy and attractive transactional environment rather than hindering any potential economic exchange.

In Summary…

Despite a growing number of well capitalized investors with an adequate risk appetite, uncertain global economic conditions and market outlook will result in selective M&A opportunities in the near future.

We expect several opportunities to present themselves however they will require more "scrubbing" and experienced M&A deal makers to leverage their expertise to adequately structure, deeply scrutinize and secure transactional agreements which minimize risks for both sellers and buyers, to the extent possible.

We remain available to share more insights and answer any questions related to your specific situation.

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