Industries

M&A in Healthcare and Life Sciences: Why the Industry's Wait-and-See Days Will End

As they sit on cash and look for growth, more companies will return to actively participating in M&A.

By Kevin Chang, Kai Grass, Jeff Haxer, Emily Magruder, and Dale Stafford

At a Glance

- Both deal value and volume dropped in 2022 as companies across the industry paused their M&A activity amid market uncertainty.
- For the first three quarters of 2022, deal activity varied by sector, with pharma, payer, and medtech all seeing large drops in total deal value, while deal value in the provider sector was up slightly.
- We believe that two megadeals in the fourth quarter will be a harbinger of increased healthcare dealmaking to drive growth in 2023.
- We expect pharma M&A activity to rebound quickly as companies look to fill the potential growth gap from the $100 billion in patents set to expire by 2030.
- The equity and debt markets will inevitably stabilize, and the top 25 pharma, medtech, and payer companies all have cash on hand.

As the year 2022 drew to a close, the number of strategic healthcare deals had declined by more than 30% and the average deal size had fallen by around 15%. In line with the overall corporate M&A market, it was largely a wait-and-see year.

Then, two megadeals announced in the fourth quarter—namely, Johnson & Johnson's $16.6 billion acquisition of Abiomed in November and Amgen's $28 billion acquisition of Horizon in December—foreshadowed the possibility of a resumption in robust deal activity.

The long-term underlying drivers of M&A in healthcare remain strong. Across all the industry's sectors, 1 percentage point of growth (either organic or inorganic) has an average of four times as much impact on total shareholder return (TSR) as 1 percentage point of EBITDA margin expansion. Cash balances are high, with the top 25 pharma, medtech, and payer companies all having at least 15% of their last 12 months' revenues on hand in the form of cash.

Private equity funds also are sitting on a significant amount of cash. With this level of available cash, it is difficult for us to see a world where M&A values do not return in earnest once the market digests the current moment of uncertainty—even if debt markets have gotten more expensive. The speed and nature of that return, however, will vary by sector and region. We'll look at each sector separately with a special lens on Europe and Asia, where the situation is most dynamic.

Pharma/biotech

Pfizer and Amgen were the most active pharma companies to rely on M&A to spur growth in 2022. Pfizer's acquisition of Biohaven Pharmaceuticals boosted its commercialized assets in the neurological and migraine space while its purchase of Global Blood Therapeutics was a doubling down in rare hematology. Amgen's purchase of ChemoCentryx added to its inflammation and nephrology portfolio, and its pending acquisition of Horizon adds multiple on-market and pipeline assets to drive future growth.

Pfizer and Amgen were clear outliers. Across all pharma companies, deal volume and value dropped by more than 30% in 2022, even after Amgen's acquisition of Horizon. We expect deal activity to accelerate once companies become comfortable with the macroeconomic uncertainty that overshadowed 2022 and as sellers readjust current valuations. We believe pharma could be the fastest among all healthcare sectors to rebound in terms of deal value. There's available cash, with the top 25 firms holding a combined $130 billion on their balance sheets, and alternative pathways to liquidity have tightened for biotech start-ups, with IPOs all but drying up.

There's also the looming issue of patent expiry. Globally, the top 15 drugs coming off patent by 2030 generated more than $100 billion in sales in 2020. That will pressure some companies to innovate more quickly and could spark a possible increase in the number of pharmaceutical companies acquiring to catch up on R&D that was stalled during the earlier days of the pandemic. Companies in Europe will turn to M&A to enter or double down on specialty drugs and rare diseases, to perform earlier phase 2 and phase 3 trials, and to speed up expansion in the US. Some large European pharma companies will rely on divestitures and spin-offs to streamline operations.

In the US, we don't anticipate that the Inflation Reduction Act will cause substantial headwinds for dealmaking in 2023, although potential buyers should be prepared for more price scrutiny. There is some evidence of both a lengthening of the approval process and a more stringent regulatory review process for US transactions. If both continue, it could add to the cost of transactions and the time to close.

In Japan, the recent government policy to spur aggressive digital adoption in healthcare should result in substantial deal activity. That likely will play out in the form of partnerships with foreign companies in vital areas such as artificial intelligence and new drug development, including anti-cancer drugs.

Chinese biotech firms arguably are ripe for consolidation because of a sharp decline in valuations after the Covid-19 pandemic resulted in overinvestments in the sector and amid recent geopolitical tensions toward the biotech industry. China's geopolitical uncertainty, as well as intensified regulatory pressure from inside and outside the country, slowed dealmaking in 2022. But M&A could bounce back in 2023 as domestic companies turn to deals to expand overseas, or to buy new technology to update mature product lines, or to expand their portfolios with new products to introduce back to China.

In South Korea, we anticipate continued significant M&A in the biotech space and a return of private equity deals, particularly in the services and provider sectors. While strategic acquirers will account for most of the deal value (especially within pharma and medtech), financial sponsors will continue to add on to existing platforms and acquire new platforms on which to pursue a buy-and-build strategy.

Medtech

Similar to other sectors, total deal volume declined meaningfully in medtech in 2022. Until the Johnson & Johnson acquisition of Abiomed in November, there was a notable lack of the type of category leadership moves that were the impetus for a significant portion of deals between 2012 and 2021. The lack of available debt that began in the second quarter of the year and the high cost of debt made large deals less attractive. Much of the M&A that took place—such as Stryker's acquisition of Vocera Communications—was designed to provide innovative technologies for future growth rather than add products to existing portfolios. The big Johnson & Johnson-Abiomed deal was a dramatic exception, and we believe it may be a harbinger of deals to come and that medtech M&A should bounce back in 2023 based on strong cash availability and the growth prospects of buying, particularly for category leadership.

In China, in vitro diagnostics players, on the back of continuous Covid-19 testing, are actively seeking M&A opportunities to further strengthen their product offerings and expand their market share. For example, in 2021, Mindray acquired HyTest, a manufacturer of antibodies and antigens used in tests for Covid-19 and other illnesses, for more than $660 million.

Provider and services

The provider and services sector stood out for its resilience. Average transaction value rose from less than $200 million to greater than $250 million based in large part on UnitedHealth's pending purchase of LHC Group for $5.4 billion and a Remgro-led consortium's acquisition of Mediclinic International for $4.49 billion. Overall, values grew 5%, and volumes dropped 28%.

While there were no large provider network acquisitions in 2022, the highly fragmented nature of this space meant that there were multiple different investment theses at play. For example, Amazon's acquisition of One Medical gave Amazon a foothold into primary care and an opening to disrupt that part of the ecosystem. When coupled with CVS's acquisition of Signify Health, we see the continued blurring of the lines between retail and healthcare. UnitedHealth's Optum division's pending acquisition of LHC will add a large home care provider to its existing continuum of care. And a Remgro-led consortium's acquisition of Mediclinic International was a diversification play of a large shipping company acquiring a hospital operator. Meanwhile, private equity maintained its interest in alternate site provider services, such as Ares Management's investments in US Heart and Vascular.

In Australia, policy reform is leading to consolidation in home care, a trend that should continue in 2023. Given the benefits of scale in this space, larger potential buyers are likely to be home care specialists looking to scale and other senior care (and related) players, such as residential and retirement care companies seeking synergies and efficiencies. We see substantial activity as participants look for strategic bolt-ons to meet operational and financial needs or to acquire capabilities (such as digital) that will be required for long-term growth.

Consolidation is taking place in Southeast Asia, too. The region is expected to see more action affecting healthcare and hospital facilities as evidenced by Metro Pacific Hospital Holdings' driving hospital consolidation in the Philippines. Meanwhile, Singapore's regional healthcare provider, HMI Group, is discussing a potential 30% stake sale.

Given the breadth of investment types and opportunities, M&A in the provider and services space should gain momentum in 2023 on a global basis. Alternate site consolidation will continue and possibly intensify given the number of assets that have been hit hard by the Covid-19 pandemic. Nontraditional players such as Amazon will continue to invest in this space to disrupt and reinvent the healthcare market, particularly in the US. Traditional hospital network consolidation, which has been a good avenue for cost reduction, may suffer, however, from the high cost of debt near term.

The top 25 payer companies have a combined $200 billion on their balance sheets.

Payer

Large M&A activity among payers was almost completely dormant in 2022. Total deal volume was relatively flat, but with no large payer deals announced this year, the average deal size fell meaningfully from 2021. This decline is likely because of the high cost of debt and equity market uncertainty. While the payer sector is typically the most cyclical of healthcare sectors from an M&A perspective, and the one with the fewest number of transactions, we do anticipate one or two larger bets in 2023. The main reason: The top 25 companies have a combined $200 billion on their balance sheets. Given the large absolute size of payers in the US, a payer needs to buy another large company to move the needle on revenue.

The current regulatory environment makes the merger of two similar payers challenging in the US, however, which means payers must look to make acquisitions in large adjacencies or face a tough regulatory approval path. It can be hard for large US payers to find big adjacencies that both fit their strategy and will pass regulatory scrutiny. (It is this "buy big in an adjacency to move the needle" dynamic that has led to the boom-bust M&A cycle in recent years.)

Europe's providers face particularly strong challenges stemming from the pandemic and inflationary environment, which has had its biggest impact in the cost of salaries and rent. Adding to the concerns, public payers are striving to reduce provider fees. While single-payer systems slowed down activity, the continued cost pressures could make consolidation across provider networks an attractive strategic option.

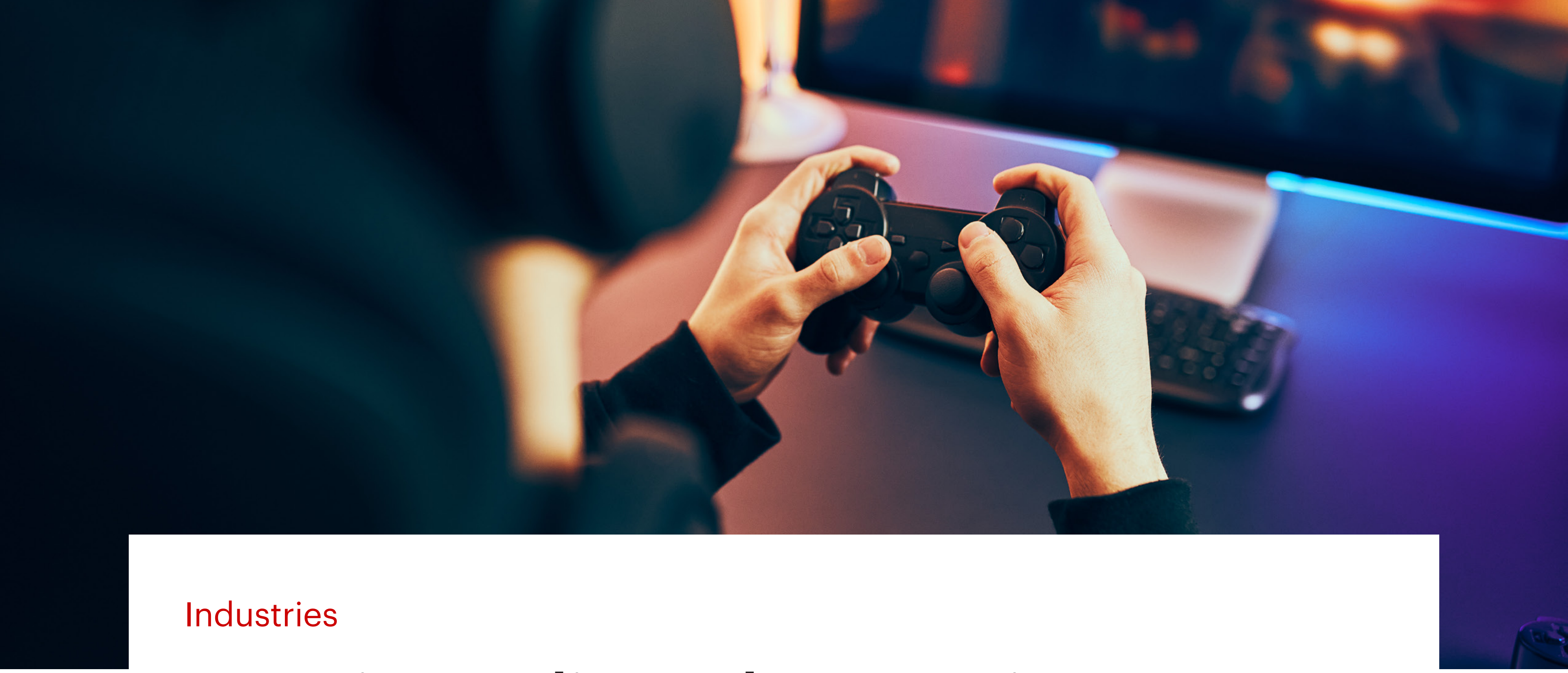
What does it all mean?

Pharma companies should expect to see increased M&A activity in the near future. Active pharma companies would be well served to proactively identify the therapeutic areas that they believe will generate future growth for their company. They then should look at what strategic capabilities they bring to the table. (Are they the best in the world at commercialization? Are they top tier in label extension? R&D?) They should look at targets that fall within their therapeutic area growth plans and that can take advantage of their own unique capabilities. Targets at the intersection of these two dimensions can warrant a higher multiple, allowing acquirers to lean in on valuations and extract higher value through M&A.

In medtech, 2022 was less about growth than about buying for capabilities that can complement the rest of the value chain. But even if debt remains expensive, there may be a return to using M&A both for innovation and category leadership. The best category leadership acquirers develop business unit–level strategies by call point, identify where M&A can play a role, and develop a proactive strategy for targeting specific companies. The most innovative acquirers look beyond category leadership and ask where growth will come from a decade out. They then place multiple strategic bets via M&A to try to be well positioned to take advantage of that growth.

Provider and services companies will continue to acquire for innovation (whether that's for dental offices or cardiology), with more activity from unexpected disrupters such as Amazon. We expect this space to continue to see substantial activity given the multitude of different potential deal theses available for varying deal sizes and the significant desire from many corners to experiment with disrupting healthcare in the US.

Payers tend to leverage M&A to drive growth. This often takes the form of payers pursuing M&A transactions that are outside of their traditional markets. Whether that takes the form of payers buying providers or payers going even further afield, we anticipate that cash-rich players will continue to innovate via M&A as they look for growth. The current regulatory environment in the US presents unique challenges in this sector that may lead to a delay in the recovery of deal activity compared with other healthcare sectors.



Industries

M&A in Media and Entertainment: To Interactivity and Beyond

With interactivity on the rise, everybody's betting on video games.

By Laurent Colombani, Nicole Magoon, and Daniel Hong

At a Glance

- As technologies advance and we move into a web3 world, interactive media will only gain in sophistication and reach.
- Two acquisition strategies help bolster capabilities for a more interactive future: deals to extend capabilities and deals to build next-generation megaplatforms.
- Consider where your consumers will be in the future, and make sure you maximize your M&A or partnership options to reach them there.

At the start of 2022, we talked about the rise of the megaplatform. We increasingly saw media companies turn toward M&A to become scale, go-to destinations across consumer touchpoints, and that trend remained strong throughout the year. Amazon, aiming to build strength on the entertainment side of its megaplatform, closed a deal to acquire MGM, which gave Amazon a greater intellectual property (IP) library and increased its talent base in content production. To extend its content reach, WarnerMedia merged with Discovery, broadening both its library and direct-to-consumer (D2C) base. These plays reflect the trends we've seen over the past few years—during which time, the more you could function as a one-stop entertainment shop for consumers, the more of a competitive advantage you could obtain.

Now, the most exciting growth in 2023 will be in deals that allow companies to expand deeper into interactivity. Most notably, everyone's betting on video games.

It's no secret that interactivity is redefining media and entertainment—with the rising popularity of video games and the advent of social media, consumers have grown accustomed to being part of the content. Consumers shape content as amateur creators, they forge their own paths through virtual worlds, and they increasingly view online worlds as key life touchpoints. In fact, according to Bain research, close to half of people aged between 13 and 34 years old would rather socialize with their peers in a video game setting than in the real world. As technologies advance and we move into a web3 world, interactive media will only gain in sophistication and reach. Megaplatforms and others in the media and entertainment ecosystem are realizing that they need to play here to win with consumers over the long term, which means acquiring companies that have made forays into the space.

As companies invest in gaming, we see two primary strategies for building future capabilities in a more interactive world:

- Acquire to extend gaming capabilities.
- Acquire to build the next-generation megaplatform.

Acquire to extend gaming capabilities. Microsoft announced the biggest deal of the year, with its $69 billion planned acquisition of Activision Blizzard. Although this builds on smaller gaming companies acquired in the past (as well as Microsoft's hardware capabilities), it represents a clear stake in the ground for owning both the game publishing piece of the value chain and the massive D2C reach that Activision's games support.

The next biggest deal of the year was Take-Two acquiring the mobile-focused Zynga. Given the strong growth in mobile-casual gaming, this makes sense for the publisher to diversify its reach. While it may feel like scale M&A, the deal also has a scope dimension. Mobile game development is a very different muscle than Take-Two historically has built, and extending capabilities with Zynga gives it a right to play across more consumer touchpoints in the growing gaming market.

Much less flashy but equally indicative of how gaming feels critical to the future was the *New York Times'* acquisition of simple mobile word game *Wordle* for an undisclosed sum in the low seven figures. Although it was a small acquisition by the standards of global M&A, it was a significant investment for the *New York Times*, which is banking on a more interactive future. The reach of *Wordle's* fan base and interactive format helps bolster the *New York Times'* prospects as a large consumer platform in the future.

Acquire to build the next-generation megaplatform. Growing a gaming presence is one angle, but there are many companies that are looking at gaming as the vehicle for the broader entertainment space and, therefore, the foundation for their megaplatforms. Meta has made the most noise about extending its activity across new interactive spaces, with massive investment in its vision of owning the metaverse as well as acquiring gaming targets that play in the virtual reality (VR) space (e.g., Armature Studio, Camouflaj). Forced to acknowledge declining legacy businesses, Meta is relying on investments in new modes of interactivity—namely, metaverse and VR-enabled gaming—to pull them out the other side. Companies such as Meta are why we think of these trends as not just gaming as we know it today but rather the entirety of interactive worlds.

Indeed, we're seeing heavy investment in a virtual future that crosses social networks, gaming, and other media sectors. Similarly broad in scope, Epic Games has been explicit about investing in its own metaverse with both organic development and M&A. In true megaplatform style, it is working to bring other media sectors into that metaverse, as showcased by its acquisition of Bandcamp in March. Given Epic's early forays into bringing music into gaming worlds in innovative ways, such as hosting concerts in *Fortnite*, we can expect to see more plays like this going forward.

Just as not everyone can be a megaplatform, a whirlwind of investment in interactivity has different implications for different media and entertainment companies. Those already in gaming may want to look at consolidating capabilities to compete with larger players, particularly in merging quality IP development capabilities with advancing tech capabilities that will enable new consumer interaction modes. They'll need to consider whether there's an avenue through M&A or partnerships to grow more platform scale.

For those not in a more interactive space today, consider how your sector might benefit from either M&A or partnerships in this area. For IP hubs, translating content to gaming in some form should be a key part of any franchise strategy, but licensing and partnerships might be the right model if an acquisition doesn't fit with corporate capabilities or budget. For other distribution platforms, thinking about what technologies might enable you to grow into a more interactive space, such as hosting traditional media events within a gaming world, could spark discussions regarding where acquisitions or partnerships might be more viable.

One thing that can't be ignored is that interactivity is rising—be it social, in-game as we know it today, or in a metaverse of the future. Carefully consider the right way to play that boosts your core, such as through a specific type of content (think *New York Times*-*Wordle*) or an on-brand partnership that leverages tech capabilities you don't have (think music players partnering with *Fortnite* for concerts). As always, companies need to be strategic about where they play and the partners they choose, depending on fundamental considerations such as appetite and risk/reward profile.

You don't need to be a tech innovator to take advantage of the future. But you do need to consider where your consumers will be, and make sure that you maximize your options in M&A or partnerships to reach them there. The big message for 2023: Don't get left behind in a static world.

Industries

M&A in Technology: Never Waste a Good Crisis

Why bold tech companies don't wait out the uncertainty.

By Adam Haller and Chris Johnson

At a Glance

- Despite the macroeconomic uncertainty that has curtailed M&A, bold technology companies are still minting game-changing deals to emerge stronger out of the downturn.
- Those that boldly move with speed can take advantage while valuations are down—most dramatically, for high-growth companies.
- The time for tech companies is especially ripe now as competition from private equity investors has dropped.
- This period of golden opportunity will not last forever. History tells us that ambiguity, not recessions, slows down tech M&A markets and that once uncertainty tapers, activity—and likely valuations—should return.
- To successfully take advantage of this opportunity, companies need to move with urgency, be proactive, turbocharge their diligence, and focus on accelerating synergies.

As they experienced negative headlines marked by recession fears, rising interest rates, and record-high valuations, many tech companies opted to put their M&A activity on hold in 2022. Deal value was down 45%, and deal volumes dropped by about 4% for the first 10 months of the year compared with the same period in 2021 (excluding gaming companies).

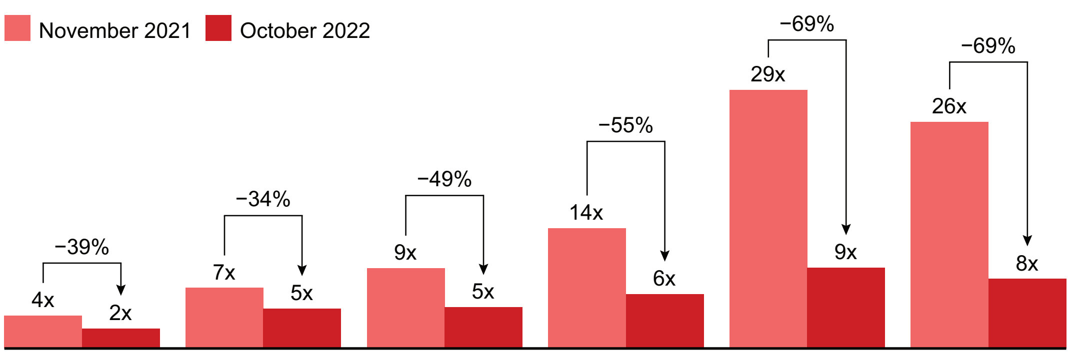
Large companies with ample cash that were willing to do the work and move quickly found opportunities for placing strategic big bets in 2022. Think of Broadcom's announced plan to acquire VMware for $61 billion to boost its software capability. That announcement occurred during the first half of the year while M&A across industries still remained fairly healthy. Yet there still were big deals later in the year, when higher interest rates cooled activity. Adobe's $20 billion bid for web-first collaborative design platform Figma (currently stalled by a US Department of Justice investigation) was announced in September. Undeterred by macroeconomic uncertainty, bold companies that eye strong assets are still willing to quickly make big moves to position themselves to emerge stronger when the fog lifts.

Our long-term analysis of M&A activity across industries has demonstrated that fortune favors the bold. Companies that we refer to as "mountain climbers"—that is, those that engage in repeated and material M&A—outperform their less-active counterparts regardless of the economic cycle. In the tech industry, mountain climbers achieve an average 15.7% annual total shareholder return compared with an average of 12.7% for all companies studied.

Let's look at what's swiftly unfolding. Month by month, assets are becoming more affordable, with tech valuations for public assets sinking across the board. High-growth companies have been hit the hardest, with an average 70% decline in valuations from November 2021 to October 2022 (*see Figure 1*).

Figure 1: Valuations remain down vs. late 2021, and high-growth companies have been hit hardest, with as much as a 70% decline in 2022

Public market valuation multiple as of October 2022 (total enterprise value/next 12 months' revenue)



Revenue growth	Less than 0	0–10%	10%–20%	20%–30%	30%–40%	More than 40%
N	17	60	49	48	14	15
Percentage of total enterprise value	1.6%	10.7%	70.1%	10.8%	3.0%	3.8%
Percentage of total revenue	2.9%	15.2%	67.3%	10.7%	1.9%	2.0%

Notes: Company industry filtered for "Internet services and infrastructure" and "software"; companies filtered for greater than $50 million in last 12 months' revenue; revenue growth and N based on October 2022 last 12 months'/next 12 months' figures; excludes companies with incomplete data
Source: S&P Capital IQ (as of October 4, 2022)

This makes it more of a buyer's market for tech companies; they have more cash at a time when there's an abundance of attractive growth assets from which to choose. Meanwhile, competition from private equity (PE), which had gained momentum steadily over the past decade, has dropped, with PE firms representing only 38% of deal value during the first nine months of 2022, down from 43% during the same period of 2021. At the same time, the IPO market has frozen, special purpose acquisition companies have all but disappeared, and growth equity has slowed—all of which limits a target's ability to raise money and favors strategic acquisitions.

Why do so many companies still sit on the sidelines whenever times seem right for buying? Some wait for prices to further decline. They view the stark decline in activity as an indication that valuations haven't bottomed out yet and that there is still time to wait. History tells us, however, that ultimately it is ambiguity, not recessions, that slows down tech M&A markets. We learned from the 2001 and 2008 recessions and from the uncertainty of the early days of the pandemic that ambiguity is short-lived. There is a period of buyer-seller disequilibrium on what an asset is worth, with buyers expecting a deal but sellers not yet willing to lower prices. And during this time, executive attention typically is more focused on keeping the company afloat than on making deals.

But as executives become aware of the deals before them, some recognize that you can't wait until the worst has passed. Once uncertainty tapers, even if we are still in a recession, activity is likely to pick up and you will have missed a golden opportunity. For example, it was during the 2009 recession that Adobe acquired Omniture in a deal that raised some skepticism but ultimately enabled the company to become a leader in the customer experience management space and spearheaded its overall cloud growth.

It all comes down to speed

So amid the uncertainty, how does one get the conviction required to leave the sidelines?

Be quick. Tech players that forged winning deals during past periods of macroeconomic uncertainty and recessions moved quickly while the supply/demand imbalance remained and as other buyers waited. Uncertainty and recessions present temporary dips for temporary buying opportunities, and sophisticated buyers know that if they don't move quickly, somebody else will.

Be on the lookout. Know exactly what type of target you want to purchase by keeping your strategy fresh and updating priority sector scans. Then when opportunities arise, it will be easy to jump into the fray. Those without a proactive plan should be building one now.

Turbocharge diligence. Execute due diligence with speed, thoroughness, and an eye toward integration, supported by outside data sources. Have conviction in value at a granular level—thinking about the full set of levers for value creation across cost; revenue; talent; capability upskilling; competitive position; and environmental, social, and corporate governance efforts.

Diligence should thoughtfully incorporate factors such as revenue synergies and key talent retention, which may have historically been underplayed. Despite layoffs in tech, the talent market remains tight for critical roles in areas such as engineering. (For more about diligence in today's M&A market, see "Tougher Times: Putting the Diligence back in Due Diligence.")

Generate synergies at speed. Higher interest rates increase the premium of realizing synergies early. Buyers need a crisp deal integration thesis with an eye toward quick wins and accountable owners. Integration should be a focus prior to closing so that both cost and revenue synergies can be realized sooner, even within six months. This starts with due diligence—work out in advance the synergies that you can achieve on day one.

All of these adjustments to the M&A approach will provide meaningful upside as companies position themselves to grow out of the downturn. Even more important, honing their M&A capabilities will pay dividends across business cycles, long after the downturn ends.

Industries

M&A in Telecommunications: How the End of Free Money Opens Up New Opportunities

Challenger consolidation and digital infrastructure deals resulting from the rising cost of debt will reshape the industry further.

By Alex Dahlke, Kiran Karunakaran, Alberto Silva, and Mick Verhoeven

At a Glance

- M&A in the telecommunications industry declined by nearly 40% in value over the first three quarters of 2022 following strong growth in 2021.
- Fully 85% of deal value involved either in-country consolidations or infrastructure deals, with the latter fetching multiples as high as 24.7 times.
- The soaring cost of debt in 2022 further strained leveraged investments, creating the need for consolidation and divestments.
- We expect strong deal flows in 2023 for consolidation, digital infrastructure, delayering business units, and private investment.

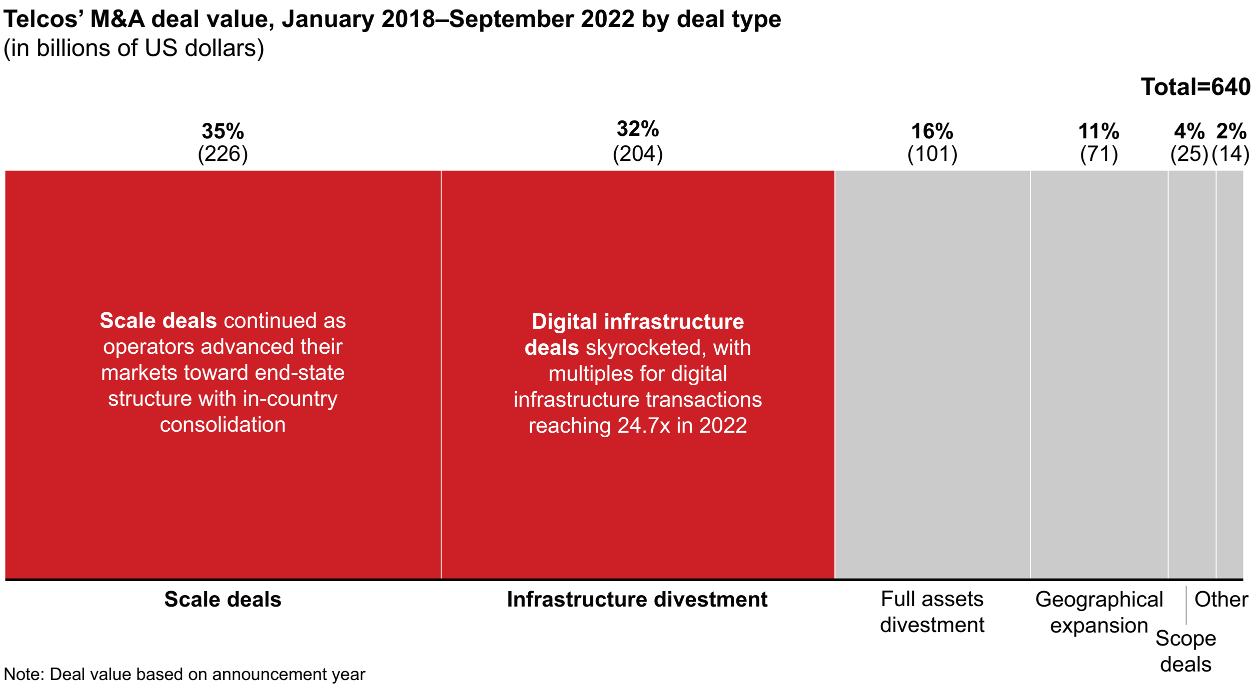
Just as the economic challenges caused by the Covid-19 pandemic abated, new global crises surfaced in the form of war, geopolitical realignments, inflation, and mounting energy concerns. The resulting macroeconomic uncertainty and rising cost of debt was reflected in telecom M&A activity, with deal value declining by about 40% and volume by about 15% during the first three quarters of 2022 following strong growth for both in 2021. As a sign of industry strength, however, deal multiples remained high across many subsectors.

M&A activity in 2022 continued to reflect five longer-term underlying industry trends that had been building over the previous years *(see Figures 1a and 1b)*.

Scale deals for in-country consolidation continued as operators advanced their markets toward that end state before competitors beat them to it. For example, consider Axiata and Axiata XL's $1.128 million deal for Link Net and Quebecor's pending purchase of Freedom Mobile for $2.2 billion.

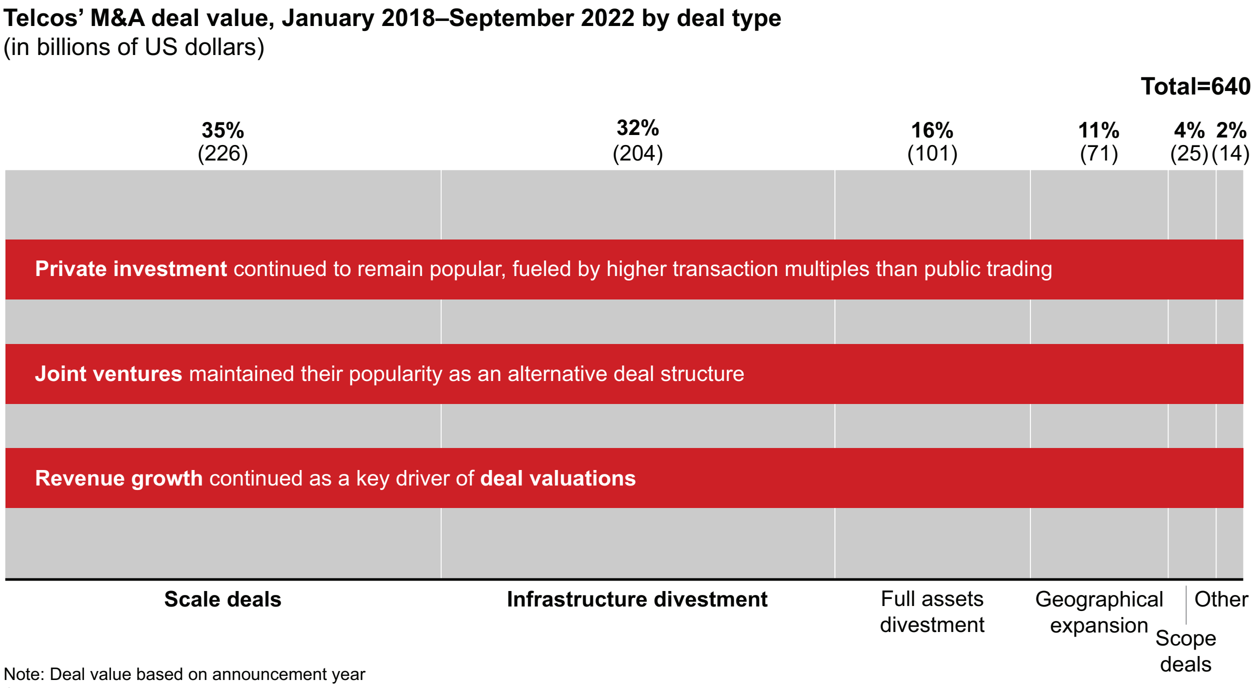
Digital infrastructure deals, particularly tower and fiber assets, skyrocketed, with multiples for digital infrastructure transactions reaching 24.7 times in 2022, up from an average of 17 time in 2021. And 2022 had some notable infrastructure deals, such as the one in which Brookfield Asset Management and US private equity group DigitalBridge bought control of Deutsche Telekom's GD Towers for $10.7 billion as well as the $2.68 billion deal in which AustralianSuper and Singtel-owned Australia Tower Network acquired Axicom, an Australian provider of telecommunications tower infrastructure.

Figure 1a: Two deal types—scale deals and infrastructure divestments—comprise about two-thirds of telecommunications deal value



Note: Deal value based on announcement year
Sources: Dealogic; Bain analysis

Figure 1b: And three other trends continued to cut across deal types



Note: Deal value based on announcement year
Sources: Dealogic; Bain analysis

Private investments continued in telcos across all deal types. Fueled by higher transaction multiples for private transactions than public trading, the total value of their investments in the industry still reached $32 billion in 2022, yet down from $35 billion in 2021. Consider CVC Capital Partners' proposal for 49% of Telecom Italia's new enterprise services unit in a deal that values the company at $6.3 billion or the Carlyle Group's $1 billion partnership with Tillman Global Holdings to ramp up Tillman Infrastructure, its independent cell tower company.

Joint ventures maintained their popularity as an alternative deal structure in large digital infrastructure deals such as Indosat Ooredoo Hutchison's $224 million joint venture with PT Aplikanusa Lintasarta and Big Data Exchange to establish an enterprise and hyperscale data center business in Indonesia, as well as in market consolidations such as MásMóvil and Orange Spain's $19 billion deal to combine businesses in that country.

Revenue growth continued as a key driver of deal valuations in 2022. In scale deals, companies sought revenue synergies by cross-selling to different products' customer bases while most digital infrastructure deals were aimed at generating revenue growth from higher asset utilization.

What's changing and what lies ahead?

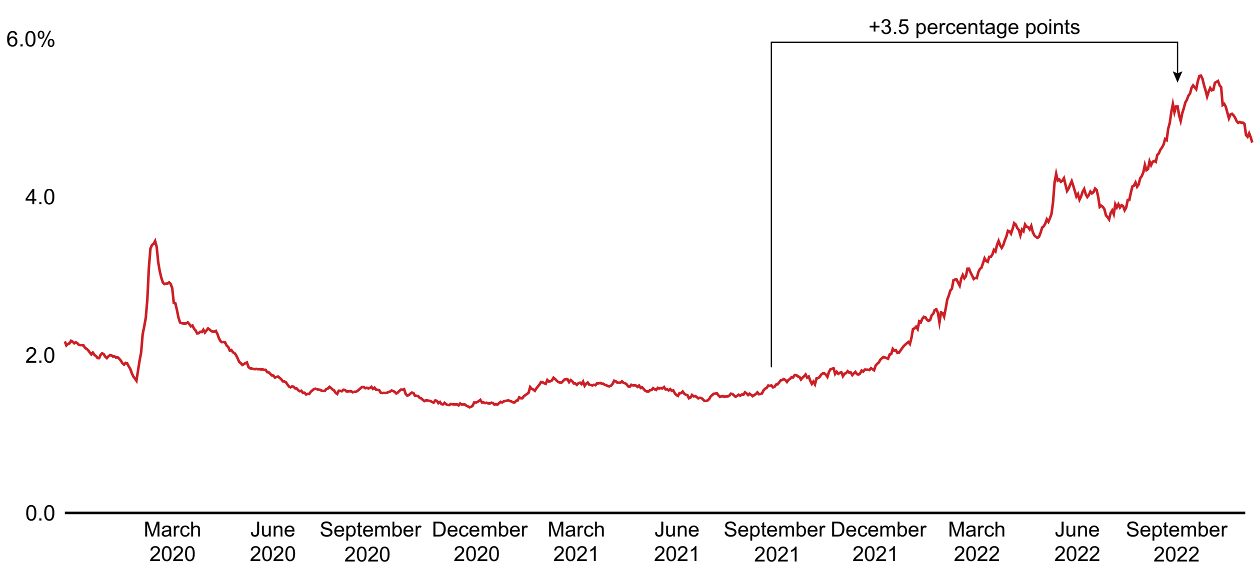
The macroeconomic uncertainties and various crises of 2022 led some governments to respond with rescue and stimulus packages such as the European Recovery Fund—and some of the benefits will flow to digital infrastructure investments. Additionally, regulators in places as diverse as Thailand and Chile showed a favorable stance toward industry consolidation.

While the impact started being felt only during the last half of 2022, these and other factors are likely to affect deal activity in 2023 and beyond in multiple ways.

Scale deals will remain robust in the still fragmented and less strictly regulated markets of Latin America, Africa, and Asia, with more consolidation of traditional mobile-mobile and fixed-mobile assets. In maturing fiber markets, alternative networks (or "altnets") will be hurt by the high cost of debt (*see Figure 2*). Some will need to find an exit strategy soon as they fall behind on their investment plans, fail to capitalize on their builds, or miss milestones critical for their debt-financing banks. Meanwhile, some challenger telcos (the No. 3 or No. 4 players in their markets) that had benefited from inexpensive capital will hit a wall as debt comes up for refinancing. They, too, will find it necessary to consolidate.

Figure 2: The cost of debt soared by about 3.5 percentage points between September 2021 and September 2022

S&P Global Developed Corporate Bond Index (yield to maturity)



Note: Comparison of yield to maturity on September 30, 2021, with September 30, 2022
Source: S&P Global Developed Corporate Bond Index (from January 2, 2020, to December 7, 2022)

Digital infrastructure deals will continue despite the rising cost of debt. That activity is propped up by the available dry powder of longer-term investors, strong underlying demand trends, government support, and the many high-quality tower and fiber assets that are still expected to come to market. Tower deals performed particularly well during the last half of 2022 despite the higher cost of debt. High digital infrastructure investor demand will create a wave of particular interest in data centers.

The technology-enabled "great delayering" of the telecom business model into infrastructure, services, platform, and vertical businesses will further inspire M&A activity. A final impetus behind deals: Private investments will maintain momentum for as long as private telco valuations stay significantly higher than public telco valuations. In particular, listed challenger telcos and listed telcos with large controlling shareholders are expected to see further public-to-private bids and de-listings.

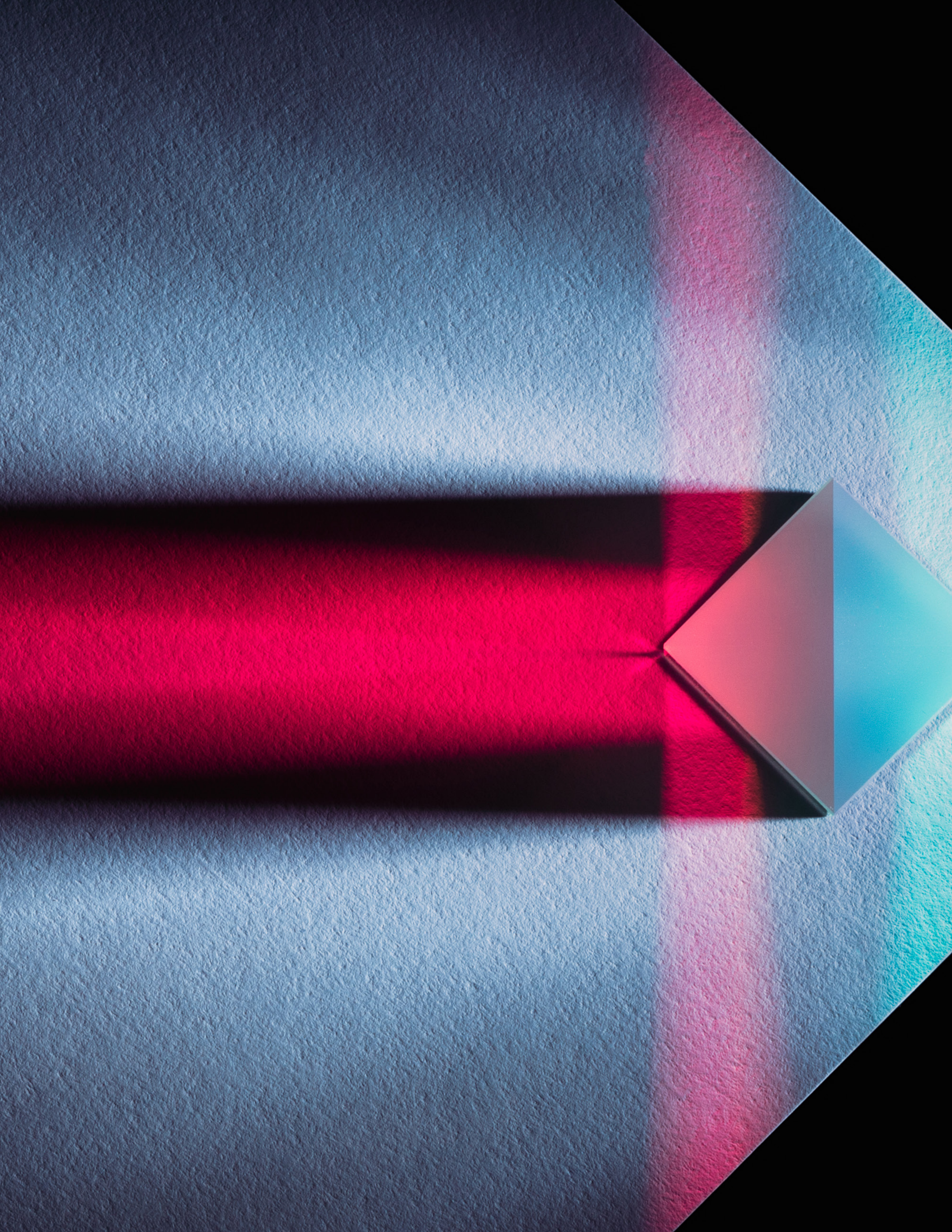
Joint ventures maintained their popularity in large digital infrastructure deals.

Five basic questions for telecom players in 2023

In 2023 and beyond, telcos (as well as their investors) need to develop new strategies and capabilities to take advantage of these M&A opportunities, chances to partner, and possibilities to divest or invest in selected portfolio assets. For many, the decision about when, where, and how to participate will come down to answering their respective versions of these five fundamental questions:

- What market consolidation options are left, and how can they be achieved via M&A?
- Can we be front-runners for fiber, tower, and data center rollup and consolidation?
- Which challenger telcos will be most impacted by inflation and the rising cost of debt, and how will that impact M&A action?
- With the great delayering of the telecom business model underway, can infrastructure assets such as edge data centers and mobile Internet companies still be created?
- Where are the undervalued, listed telco assets that could create more value as a private company?

The authors would like to thank Clara Kessler and Marlene Kessler for their contributions to this chapter.



Regions

Regions

M&A in Brazil: A Nation Prepares for Changes

A new government's policies and the world's reaction will define Brazil's M&A environment in 2023.

By Luis Frota, Felipe Cammarata, and Leonel Lima

At a Glance

- Even with a slowdown in activity and a reduction in deals valued at greater than $5 billion, overall deal value remained steady in 2022.
- Businesses are scenario planning for different potential outcomes while they wait to see what changes the newly elected government will make.
- Will international buyers seeking a safe haven from inflation as well as those motivated by a more climate-conscious new government invest in Brazil?

If ever there were a country in which M&A practitioners need to double down on scenario planning, it is Brazil. As former president Luiz Inácio Lula da Silva returns to power, business leaders know that substantial yet unpredictable policy shifts will be implemented. But until those new moves are made and until it's clear how the world will react, the best dealmakers are systematically laying their game plans for the multiple scenarios that could occur—whether that's a bump in inflation caused by an increase in government debt, for example, or a rise in foreign investment by those who feel the country is more stable than developing markets in Asia, or continuing political tensions such as those recently witnessed in the storming of the main institutional buildings of the country's capital. Brazil's economic trajectory could move in any number of directions, and the key to successful dealmaking will be rigorous preparation.

Brazilian companies are discovering the benefits of scope deals.

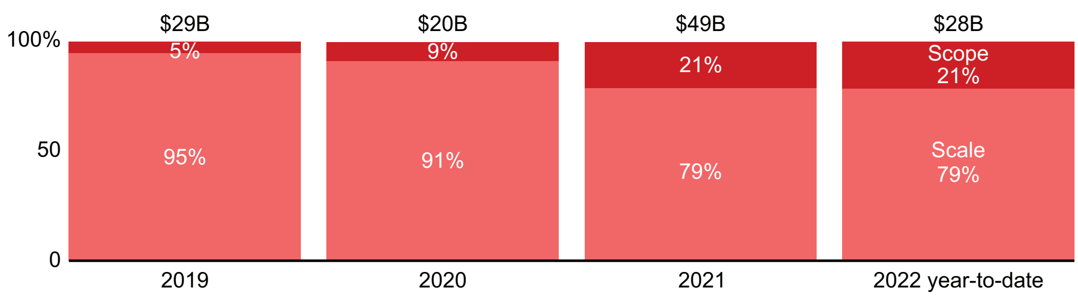
Similar to many other places, Brazil saw a dramatic rise in M&A in 2021. But that activity slowed in 2022 amid macroeconomic uncertainties, both global and local. Even with the slowdown and a drop in the number of deals valued at greater than $5 billion, overall deal values remained in line with pre-pandemic levels. While 79% of the M&A activity involved scale deals, there has been a rise in the number of scope deals, which represented 5% of all deal value in 2019 but 21% of that value in 2021 and 2022 (*see Figure 1*).

That's still less than the global average, in which roughly half of all M&A deal value is scope, but it is a sign that Brazilian companies are discovering the benefits of these deals. In fact, the biggest acquisition in 2022 was a scope deal: Brazilian hospital chain Rede D'or purchased insurer SulAmerica for around $2.6 billion, combining the country's largest hospital network with one of its major independent insurance companies. Two types of deals were particularly popular in 2022: those in which a company bought a supplier, client, or partner to better control the value chain; and deals for digital capabilities.

Figure 1: In Brazil, scope deals are slowly gaining share on scale deals

Scope deals have increased their share in total value since 2019

Percentage of Brazil's M&A total deal value per category type (in billions of US dollars, 2019–2022 year-to-date)



	2019	2020	2021	2022 year-to-date
Scale				
Average deal value (in millions of US dollars)	$257M	$154M	$244M	$233M
Number of deals	107	119	158	94
Scope				
Average deal value (in millions of US dollars)	$78M	$58M	$170M	$91M
Number of deals	19	30	60	65

Notes: M&A deals by announcement date; 2022 year-to-date includes deals announced until mid-November 2022
Source: Dealogic

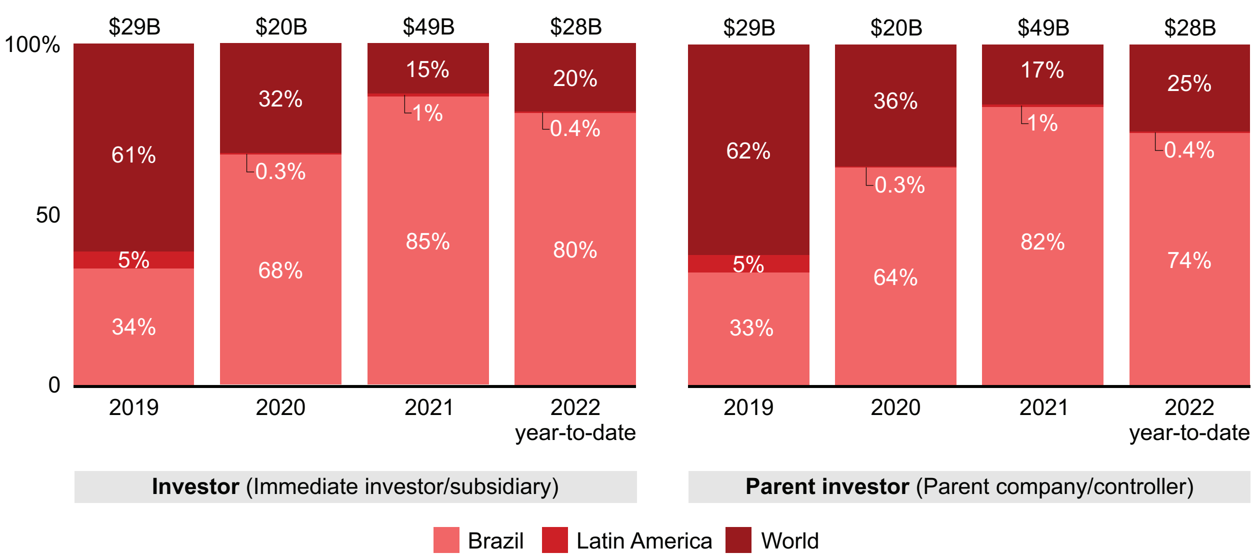
In 2022, two sectors accounted for 66% of deal value: energy and natural resources, and manufacturing and services. But a year earlier, health and retail deals were popular, too. It's a shift that reflects companies' concerns about the country's economic ambiguity. Now, as companies prepare for an uncertain future, more deals will likely continue to be in industries that are more dependent on exports (such as energy and natural resources) than domestic consumption.

Another big factor in Brazil's M&A prospects involves foreign investment. During pre-pandemic 2019, 67% of the country's deals were fueled by foreign capital. That portion is now 25%, indicating a lack of international confidence in Brazil's economic future—although that share did rise from 17% in 2021 (*see Figure 2*).

And some dealmakers are optimistic about foreign investment returning. For one thing, Brazil has been able to get a handle on inflation faster than many other major economies, largely because it has extensive expertise in combating inflationary pressures with a relatively agile central bank. Also, some US and European investors may view Brazil as a more geopolitically stable alternative for investing than many countries in developing Asia. Finally, a potential environmentally friendly agenda from the new government could make the country more attractive. Smart companies are preparing for the possibility that a further rise in foreign investments could present opportunities for divesting nonperforming or noncore businesses.

Figure 2: International capital is gaining share in Brazil's total strategic deal value, but it has not returned to pre-pandemic levels

Percentage of Brazil's M&A total deal value per origin of investment
(in billions of US dollars, 2019–2022 year-to-date)



Notes: M&A deals by announcement date; 2022 year-to-date includes deals announced until mid-November 2022
Source: Dealogic

But it's just one of the many uncertainties regarding Brazil's market outlook and one more thing pressuring M&A practitioners to make deals more carefully than ever. That's why concerns about the country's growth forecasts, inflation levels, and interest rates (among other factors) will require extensive use of multiscenario planning.

For example, revenue synergies have become increasingly important in justifying valuations paid. In the present uncertain macroeconomic environment, valuations based on revenue synergies will be under more scrutiny. That makes it even more important to conduct extensive due diligence of the market and the business being acquired, considering multiple scenarios.

The best companies will use scenario planning at two stages: first, to help them understand the situations in which they should buy, hold, or sell; second, if the answer is to buy, to perform due diligence that considers different scenarios, thus enabling potential buyers to adjust their valuations according to the future world they envision. It also helps them to be better positioned at negotiations.

Regions

M&A in India: How Long Can This Hotspot Buck the Global Downturn?

In India, deals are flourishing like nowhere else.

By Karan Singh and Vikram Chandrashekhar

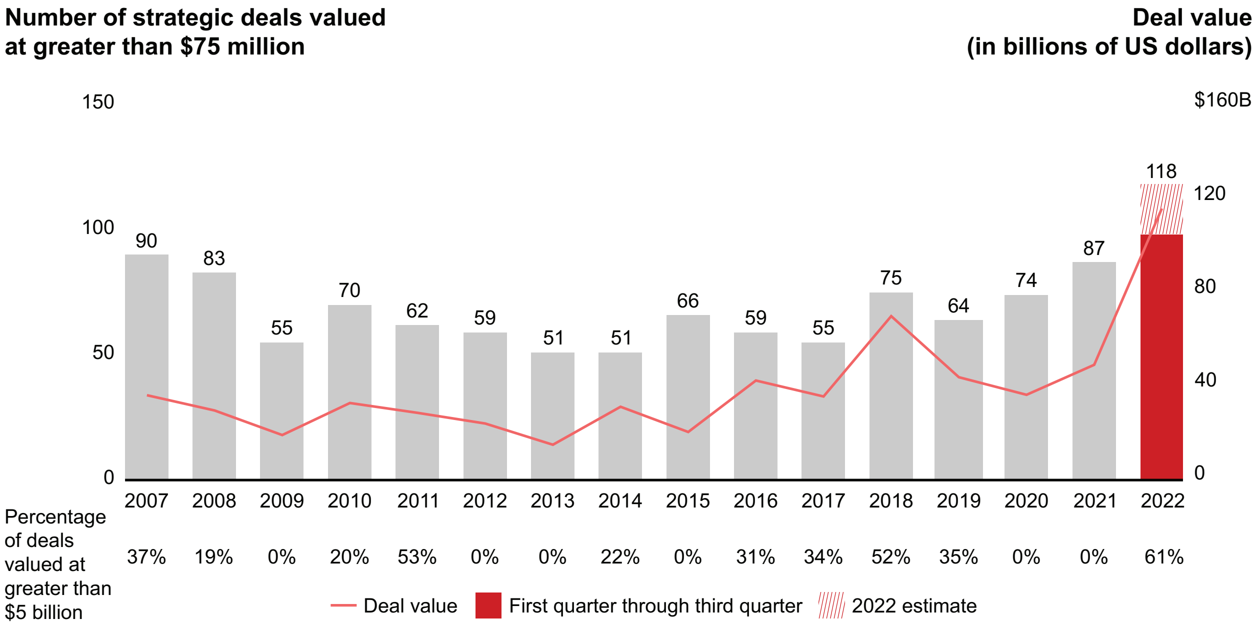
At a Glance

- The country's record levels of cash and availability of assets helped deliver a boom in deal volume, with deal value rising by 139% in 2022.
- Conglomerates are looking for Engine 2 businesses, insurgents for consolidation, and multinationals for diversifying their supply chains.
- Even if India's economy changes course, executives feel optimistic about the prospects for deals, and they are not pausing M&A.

Strategic M&A deal volume and value reached all-time highs in India in 2022, while dealmaking dropped off in much of the rest of the world.

Several factors have converged to create a robust environment for M&A. Corporate balance sheets are solid, with cash now at record levels. Private equity has ample dry powder to deploy. Foreign direct investment has held steady to the point at which India is a global hotspot as an attractive non-US destination for capital. Sellers are responding to high multiples and bringing more assets (and more quality assets) to the market—and acquirers are ready to move on them. Conglomerates and other traditional businesses are turning to M&A to win future profit pools. In its fourth straight year of steadily growing volume, deal value rose by 139% in 2022 (*see Figure 1*).

Figure 1: India is bucking the global trend, with strategic M&A deal volume and value at all-time highs



Notes: 2022 estimate annualized based on data through October 31, 2022; historical numbers (deal value and volume) have been updated after removing financial investors
Sources: Dealogic; S&P Capital IQ

Several key themes emerge from our analysis of deals last year. First, established domestic companies turned to M&A to consolidate. For example, in India's biggest merger announcement ever, HDFC, the mortgage firm, has signed on to merge with HDFC Bank in a deal valued at $40 billion.

Second, there also were many scope deals. For example, Adani's $10.5 billion deal for Ambuja Cements and ACC makes it the second-largest cement manufacturer in India. Torrent Pharma bought skin care player Curatio Healthcare to strengthen that part of its portfolio.

What's behind the scope activity? India's conglomerates are making bets on new growth engines and future profit pools that offer higher multiples than their traditional businesses. Also, many companies are buying online businesses and combining them with their offline presence to create omnichannel offerings for consumers. Aditya Birla Fashion and Retail bought controlling stakes in Bewakoof, Urbano, and multiple other brands as part of its effort to create a new digital-first house of brands.

Third, the Indian government's ambitious energy transition policies (e.g., the Ministry of New and Renewable Energy's National Solar Mission and National Green Hydrogen Mission) open up business opportunities and push conglomerates as well as traditional energy companies to invest in renewables. For instance, in line with the government's mission, Adani turned to M&A to pursue a goal of becoming the world's largest integrated hydrogen producer. And the company is acquiring its way to building a presence across the value chain in its ambition to become one of the world's largest solar/renewables companies, from producing renewables and green energy equipment to creating downstream facilities that produce green hydrogen derivatives such as nitrogenous fertilizers. Multinationals are making similar plays—for example, consider Shell's purchase of Solenergi Power and the Sprng Energy group of companies.

Fourth, India is becoming a prime alternative for global companies that are eager to diversify their supply chains. In a way, India stands to ultimately benefit from recent supply chain disruptions. The shift is fueling deals in areas such as active pharmaceutical ingredients, specialty chemicals, and contract manufacturing, where private equity players are acquiring serial assets and rolling them up to create one large platform. In November, Advent International bought a controlling stake in Avra Laboratories, combining that company with RA Chem Pharma and ZCL Chemicals, two companies it had previously purchased. In another deal, global investment firm PAG led a consortium that bought a controlling stake in the pharmaceutical firm Optimus Group.

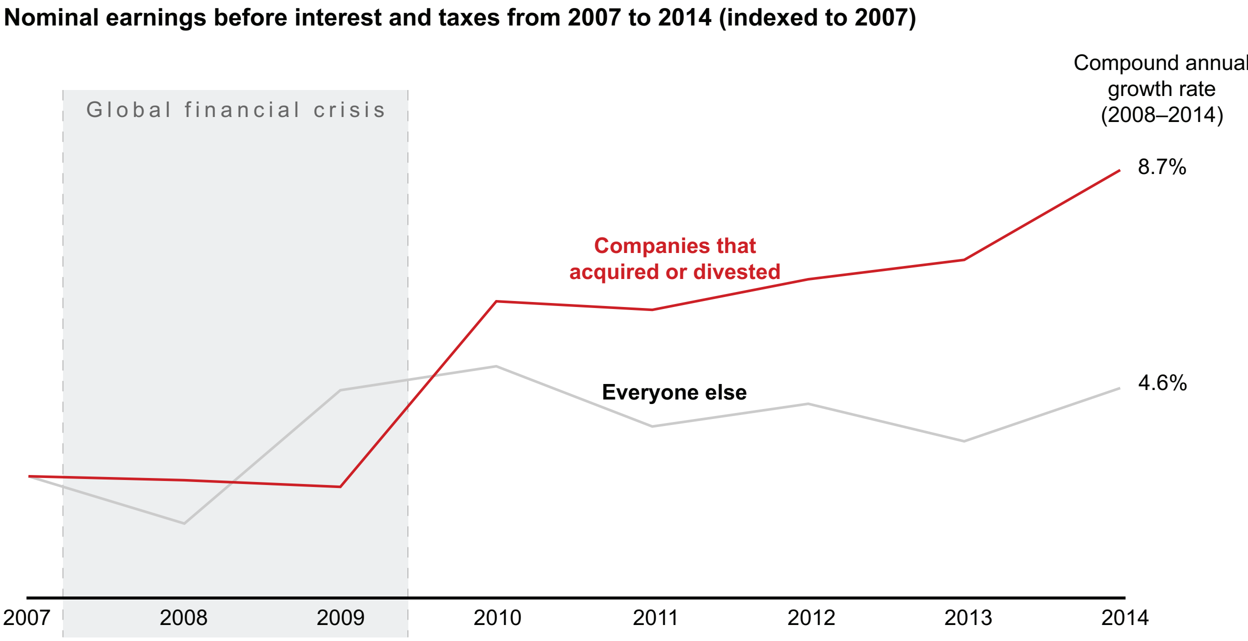
And fifth, in a trend we reported on last year, fast-growing insurgents are aggressively buying start-ups. Much of the activity is in consumer tech, edtech, and fintech. For example, eight-year-old Razorpay, which is quickly building a financial ecosystem for businesses around payments and banking, completed its purchase of loyalty and engagements solutions start-up Poshvine in 2022—its seventh acquisition to date.

India-based executives remain optimistic that the M&A train will continue its forward momentum, with 75% of them telling us they expect that there will be more attractive assets available in 2023, according to our M&A Practitioners' 2023 Outlook Survey. This is higher than the global average of 53%. Meanwhile, 64% of those India executives say that they expect the likelihood of closing an acquisition will increase in 2023, which is more than the global average of 37%. Global companies also appear poised to double down on India as an attractive long-term market.

There is one potential situation that could make dealmakers step back. While India has already hiked interest rates, further aggressive increases could result in M&A activity slowing down. As we've seen in the US and other markets, the large increase in interest rates starting in mid-2022 played a big role in M&A activity contracting by 36% globally. This may not be as severe in India, but we should be forewarned about the cause and effect of rising inflation and interest rates.

Even if India's economy changes course, its executives clearly are positioned to make the bold moves that would help them emerge stronger. That's what they did last time around. During the 2008–2009 global financial crisis, companies in India that took portfolio actions outgrew their peers two to one in nominal earnings before interest and taxes over the next five years (*see Figure 2*). Across all economic cycles, companies that engage in frequent and material M&A achieve almost twice the total shareholder growth of nonacquirers, according to Bain's 20-year assessment of corporate performance.

Figure 2: Downturns are opportunities for bold moves that pay off when markets recover



Note: Companies that acquired or divested include India-listed companies that were active in M&A between 2007 and 2009
Sources: S&P Capital IQ; Bain analysis

Yet history tells us that each time has its own unique challenges, and acquirers in India need to pay heed to the special requirements of deals in 2023.

- With the potential for a downturn, companies need to develop a highly tailored integration approach that foremost protects the target's business but that also lays the appropriate integration playbook for realizing synergies that will bolster the top line—this includes proactive, customer-centered, and data-driven sales playbook integration, product portfolio integration, and go-to-market integration.
- With talent experiencing a moment of profound disruption, companies need to prepare for the reality that merger integration only increases the risk of attrition. And 38% of India-based executives say that they often or always experience challenges with talent retention after deal completion. This is higher than the global average of around 30%. So, executives need to expand people diligence, creatively read the talent landscape, and design integrations with retention in mind. The best companies begin to assess culture and strategic fit before diligence begins. Here, India's executives can play some catch-up with their counterparts elsewhere. According to our M&A practitioners' survey, 30% of India-based executives say they begin to assess culture/strategic fit before diligence begins, lower than the global average of 44%.

- Finally, in a time of increasing environmental, social, and corporate governance (ESG) mandates and relentless digital disruption, companies need to combine both ESG and digital capabilities in dealmaking to drive multiple expansion. Both will remain long-term value creation hotspots over the next decade, and the best companies will make them key considerations in their M&A activity.

In the years ahead, companies that build M&A capabilities and use a systematic approach to deals will be those that win in the race to revamp India's industries and capture an outsized share of the country's impressive growth.

Regions

M&A in Japan: Pressing Pause on Transformative M&A

As Japan sees a drop in the number of big acquisitions aimed at transforming businesses, the best companies are preparing for what's next.

By Takashi Ohara

At a Glance

- Unlike 2021, few Japanese companies engaged in large cross-border deals intended to transform their business portfolios in 2022.
- Similarly, few companies continued the trend of selling noncore and nonstrategic businesses.
- While deal value dropped by 20% in the first nine months of 2022, deal volume remained at the same level as 2021, suggesting a rise in small deals.
- Transformative M&A should return as Japanese companies revise their portfolios and more stable financial investors buy carved-out businesses.

If 2021 was the year of big cross-border deals aimed at making substantial changes to Japanese companies, 2022 was a year of scaling back on the size of deals and changing focus.

Japanese executives say it's not a matter of *if* a deal will happen but *when*.

On the one hand, Japanese companies, similar to their counterparts elsewhere, are hesitant to make larger deals in the current uncertain macroeconomic environment. Among the big considerations, the high multiples that typically accompany transformative deals, combined with the significant depreciation of the Japanese yen, made potential acquirers hold out. But while deal value dropped in 2022, with the country seeing a 20% decline in deal value in the first nine months, M&A volume was at the same level as 2021.

This means that even as Japanese companies took a pause on transformative M&A, it was time for smaller deals, such as Nippon Steel's cross-border deal for G Steel and G J Steel, two Thai steelmakers, for about $763 million. Nippon Steel's move was part of its strategy to expand overseas amid a declining domestic market. A few transformative deals did take place in 2022, but all of them were domestic and much smaller in scale compared with 2021. For example, industrial and testing equipment company Shimadzu acquired Nissui Pharmaceutical to expand into the healthcare business.

As part of their transformative M&A focus in 2021, Japanese companies also divested some original businesses that no longer were considered strategic for their future to financial investors. But the smaller size of divestiture deals meant the total value of divestitures was lower. A few notable ones, however, did take place: Olympus sold Evident, its century-old microscopy business, to Bain Capital, and Hitachi divested Hitachi Transport Systems to KKR.

So, are Japanese companies experiencing a temporary pause or a fundamental shift in approach to M&A? Executives tell us it is the former, not the latter, and that it's not a matter of *if* a deal will happen but *when*. Indeed, there are some underlying trends that indicate Japanese companies are likely to resume deals.

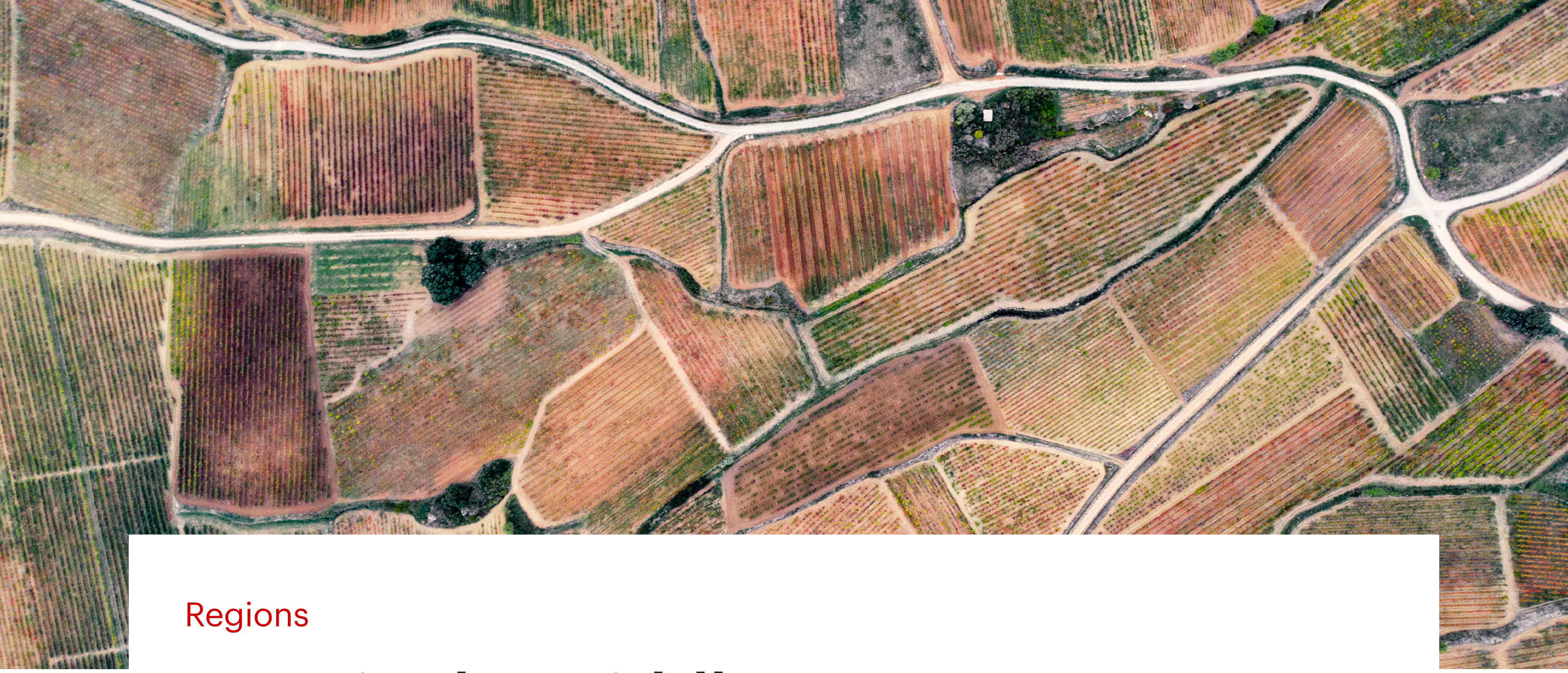
Many Japanese companies will need to clarify and articulate their growth strategies in the years ahead. And that will result in companies deciding to shed nonstrategic assets to streamline their business portfolios. At the same time, enterprise value multiples of public companies in Japan remain substantially lower than in the US and other markets, partly because of their lack of a well-defined growth strategy. That makes them attractive for acquirers.

Meanwhile, financial investors—the primary purchasers of carved-out assets—are well positioned to buy. We expect deal value by financial investors to remain steady, despite an overall decline in Japan's M&A market. Why do we say that? Unlike other countries, Japan's private equity market remains hot. Funds created for investing in Japan are growing, and many Asia funds are shifting focus from China to Japan. So, the amount of dry powder to be invested in the country will remain substantial. Another big factor: Interest rates are comparatively low in Japan, making it affordable to borrow for deals.

Yet while financial investors are poised to buy, it's unclear when conditions will ripen for Japanese companies to resume their acquisitions. In the meantime, they can prepare by proactively looking for targets so that they can act fast when the time is right. Below are three critical moves:

- Consider this a perfect time to step back to articulate the company's M&A strategy and to thoroughly review the company's growth strategy. That means answering some basic questions, such as: Do I have the right business portfolio mix (growth engine and cash generator)? Do I have a clear business unit–level growth strategy? And how can M&A accelerate the growth?
- Prepare a list of potential assets that should be divested to improve the balance sheet. Number the noncore/nonperforming assets in order of divestiture priority.
- Screen targets, putting more emphasis on an asset's attractiveness as opposed to its feasibility. Deal multiples will change, and the short-term performance of the company will vary. So, the asset will fluctuate in price. While it's always wise not to pay too much of a premium too late, it's also critical not to walk away from large deals too early, especially in this uncertain environment.

On the surface, it may appear as if Japanese companies are in a wait-and-see mode for M&A, but the best and most strategic dealmakers are thoughtfully making plans for their next move.



Regions

M&A in the Middle East: How a Region Grows with M&A

Sovereign wealth funds are using M&A to transform economies.

By Tom De Waele and Grégory Garnier

At a Glance

- Fueled in large part by government-owned sovereign wealth funds, M&A activity rose by about 39% in 2022 in the region.
- Combined, sovereign wealth funds and corporations represent 84% of deals, with private equity investors doing relatively few deals.
- Sovereign wealth funds are using M&A to scale into new verticals, strengthen partnerships, invest in the future, bolster the region, and build local champions.

With a strong economy buoyed by high oil prices, the Middle East is well positioned to rely on M&A to further advance the region's long-term push to expand beyond hydrocarbons as well as globalize its companies. Most of the deal activity is fueled by sovereign wealth funds and local corporations, with the potential for foreign investors to start deploying capital in the region.

Indeed, these are good times for the local economy, with expected regional GDP growth of 6.5% (it's 7.6% in Saudi Arabia), the highest it's been in more than a decade. The Middle East's sovereign wealth funds are growing, too, and with a new government mandate, they have become a treasure chest for much of the M&A activity. For example, Saudi Arabia's state-owned Public Investment Fund (PIF) invested $1.3 billion in four Egyptian companies in August 2022, including Abu Qir Fertilizers and Alexandria Container and Cargo Handling.

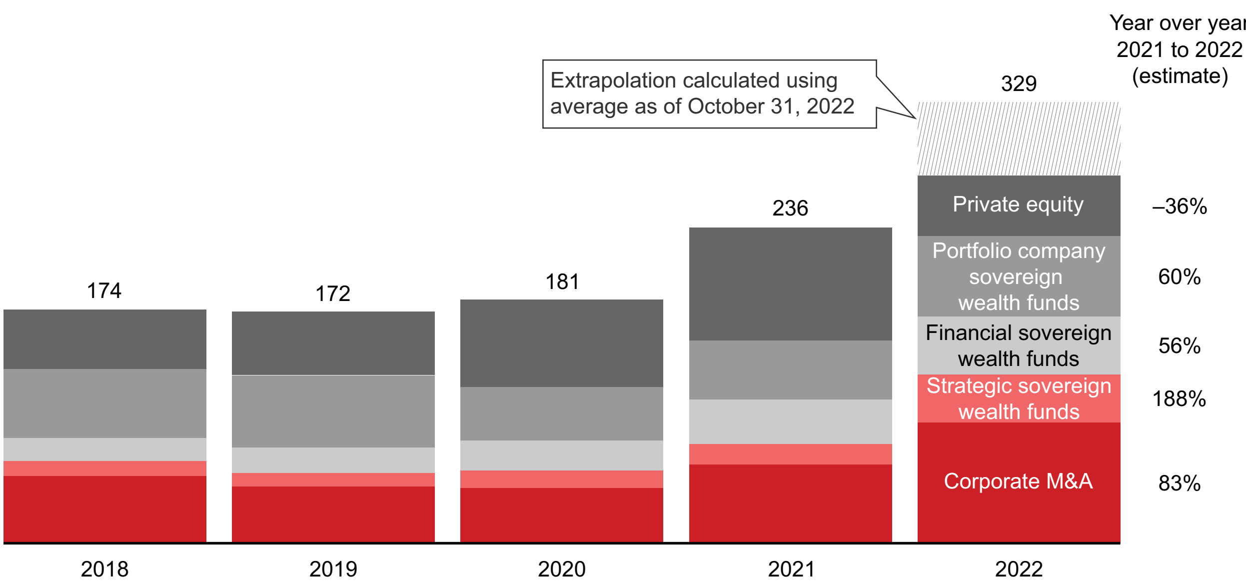
Sovereign wealth funds are where most of the action is.

The big move by governments to use sovereign wealth funds to transform the economies includes other dimensions that involve dealmaking. They are consolidating, attracting direct foreign investment, and encouraging local companies to grow internationally and enter underdeveloped sectors such as pharmaceuticals, media and entertainment, and renewables. They are investing in strategic deals to enhance local capabilities, and they are consolidating sectors to create local players that are regionally and globally competitive.

While these pieces have been in place for years, M&A activity reached an inflection point in 2021, which is reflected in an expected 39% rise in deal volume (including both strategic and financial M&A) in 2022 (*see Figure 1*).

Figure 1: 2022 deal volume from Middle East acquirers is expected to surpass 2021 levels

Deal volume for Middle East acquirers (number of deals)



Note: By announcement date
Source: Dealogic as of October 31, 2022

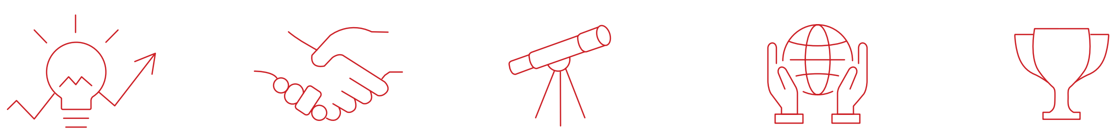
Private equity activity, on the other hand, is limited in the region and has actually dropped by 36% in first 10 months of 2022. Yet there are some signs of reviving interest from firms preparing for IPOs, which are booming.

Combined, sovereign wealth funds and corporations represent 84% of deals. Corporations are buying companies or forming partnerships to consolidate local markets in strategic sectors, such as the deal between Saudi British Bank and HSBC Saudi Arabia or the Etihad-Air Arabia joint venture. Meanwhile, regional companies are expanding internationally through cross-border M&A or through overseas investments. For example, Abu Dhabi's FAB merged its Egyptian operations with Bank Audi Egypt, creating one of Egypt's largest banks.

But sovereign wealth funds are where most of the action is. We identified five archetypes of how they invest in deals (*see Figure 2*).

Enter new verticals at scale. Sovereign wealth funds are building local platforms in underdeveloped sectors. That was the aim of Abu Dhabi-based ADQ's acquisition of Swiss pharmacy company Acino and its 45% purchase of Louis Dreyfus, a leading merchant and processor of agricultural goods based in the Netherlands.

Figure 2: Five archetypes for sovereign wealth fund M&A in the Middle East



1	2	3	4	5
Enter new verticals at scale	**Strengthen ties with partners**	**Invest in industries of the future**	**Increase visibility**	**Build local champions**
Build local platforms in sectors currently underdeveloped following local development agenda	Support **development of regional economies** or **biggest hydro-carbon partners/ buyers**	**Acquire assets in emerging industries** (e.g., renewables, sustainability, digital)	Acquire **high-visibility international assets** for "nation branding"	**Scale domestic leading companies breaking out from the Gulf** into higher-population/ higher-growth markets

Source: Bain & Company

Strengthen ties with partners. Sovereign wealth funds also are doing deals to strengthen cross-border partnerships with hydrocarbon buyers as well as to support the development of regional economies. In addition to Egypt, PIF has established investment companies in Jordan, Bahrain, Sudan, Iraq, and Oman.

Invest in industries of the future. Abu Dhabi-based Mubadala Investment has invested in Sweden-based GlobalConnect and the UK's CityFibre.

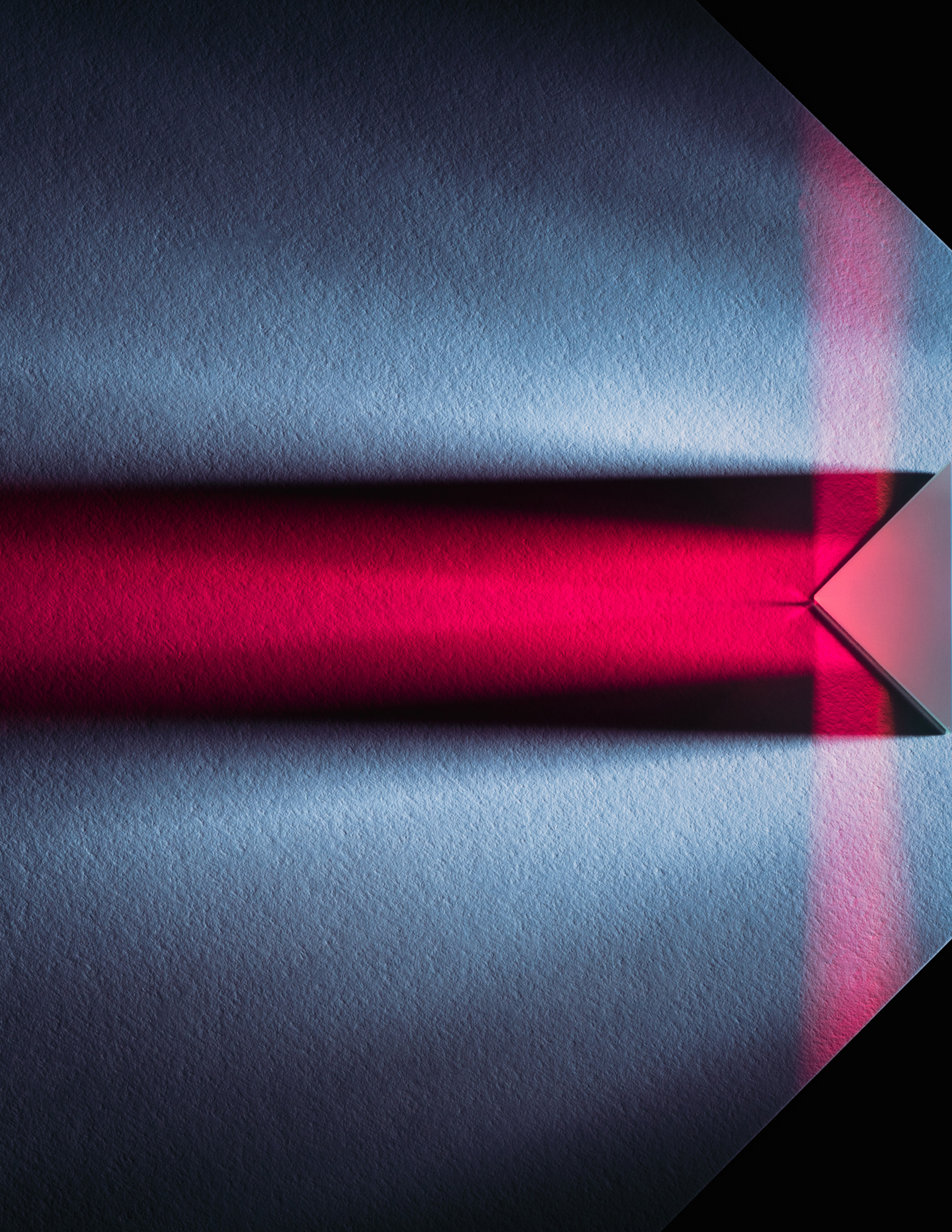
Increase visibility. Sovereign wealth funds have been purchasing high-visibility assets internationally. Consider Qatar Investment Authority's acquisition of the St. Regis Hotels in New York and San Francisco, as well as making investments in Rolls-Royce.

Build local champions. Finally, sovereign wealth funds are making strategic portfolio investments to build local companies into businesses capable of competing outside the region. In its effort to become a powerhouse in the world of eSports and gaming, PIF-funded Savvy Games bought more than 8% of Swedish gaming company Embracer. The investment comes on the heels of Savvy's 5% stake in Nintendo and its $1.5 billion purchase of ESL Gaming and FaceIT.

This hyperactivity to expand and globalize opens up opportunities for companies and financial sponsors both within and beyond the Middle East. Family-owned businesses and conglomerates will have opportunities to divest noncore assets and reallocate capital for long-term strategic investments in their core business. Some will sell assets to companies looking to grow internationally while others will use it as a chance to grow in the Middle East market. Either way, M&A in the Middle East requires a different approach than most dealmakers take in other parts of the world.

Regional investors need to gradually deploy more feet on the ground to source proprietary deals in target geographies and sectors of interest. For sovereign wealth funds, that means leveraging general partner relationships to source deals, either directly or as coinvestments. It also requires coordinating local and international units to create synergies across investments. For corporations, this would involve identifying sources of differential synergies that give them an edge over sovereign funds. The best investors carefully consider what a regional or global platform should be in order to generate synergies among groups. They also revisit their portfolio on a regular basis.

International financial sponsors need a separate range of considerations, such as how to gain access to proprietary deals, how to transfer capabilities, and how to localize a portfolio for the Middle East. In the years ahead, we expect more international companies will explore the cross-border possibilities of partnering with sovereign wealth funds and local authorities to create new sectors through joint ventures.



Methodology

State of the market, industry, and regional M&A data

Deal details and aggregate statistics (such as value, volume, multiples) were sourced primarily from Dealogic's M&A database for this annual report. Full-year 2022 data was updated as of January 2023.

This report's focus is on strategic M&A, which includes deals inked by corporate buyers (including via sponsor exits) or private equity add-on acquisitions, because both M&A types have fundamentally strategic objectives. All other types, including financial sponsors, special purpose acquisition companies, and venture capital, are classified as nonstrategic. Together, these two categories equal Dealogic's total M&A market.

Scope vs. scale

To understand the nature of M&A activity, we first identified the top 250 strategic deals for each year (top 197 strategic deals for 2022 year-to-date through September, since the analysis was concluded in October). From the initial list of deals with values greater than $1 billion, as reported by Dealogic, we excluded nonstrategic deals. These include asset or property acquisitions, financial investments, internal reorganizations, and minority stake acquisitions.

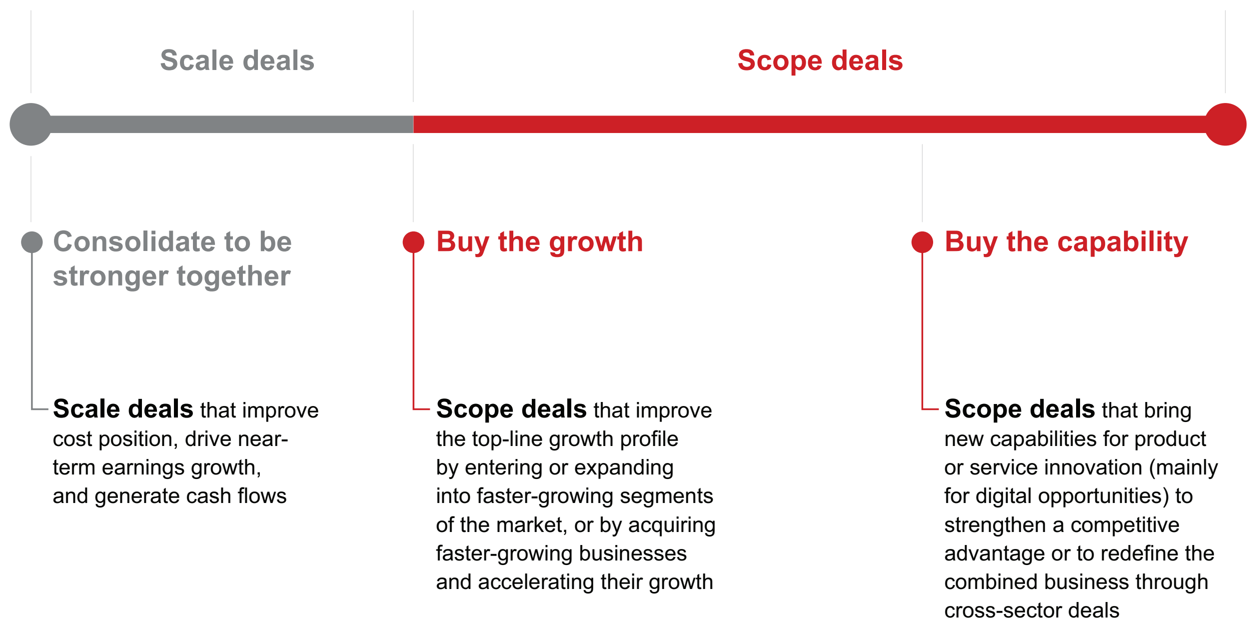
We then classified the strategic deals into scale or scope deals based on our proprietary framework applied consistently across the years. The proprietary framework uses the stated strategic rationale by the acquirer at the time of announcement to identify the key elements of the deal thesis. Based on these elements, the deals were categorized as scale or scope deals.

Scale deals are intended to strengthen market leadership and lower cost position through benefits of scale, such as cost synergies. Scope deals are intended to accelerate top-line growth by entering or expanding into faster-growing market segments, or by bringing in new capabilities. In reality, some deals are a blend of both scale and scope; the vast majority, though, lean toward one or the other *(see Exhibit A)*.

The M&A Practitioners' 2023 Outlook Survey

In partnership with the Gerson Lehrman Group, AlphaSights, Dynata, and IncQuery, we conducted a survey of 294 M&A practitioners. The survey ran in October 2022 in the US, Canada, Brazil, UK, Germany, France, Greece, Italy, Switzerland, Japan, India, and Australia. Survey participants held senior executive roles with the title of vice president, senior vice president/executive vice president, director, C-suite, or owner at companies with greater than $100 million in annual revenue, and they were responsible for M&A decision-making processes at their company.

Exhibit A: About the methodology



Source: Bain & Company

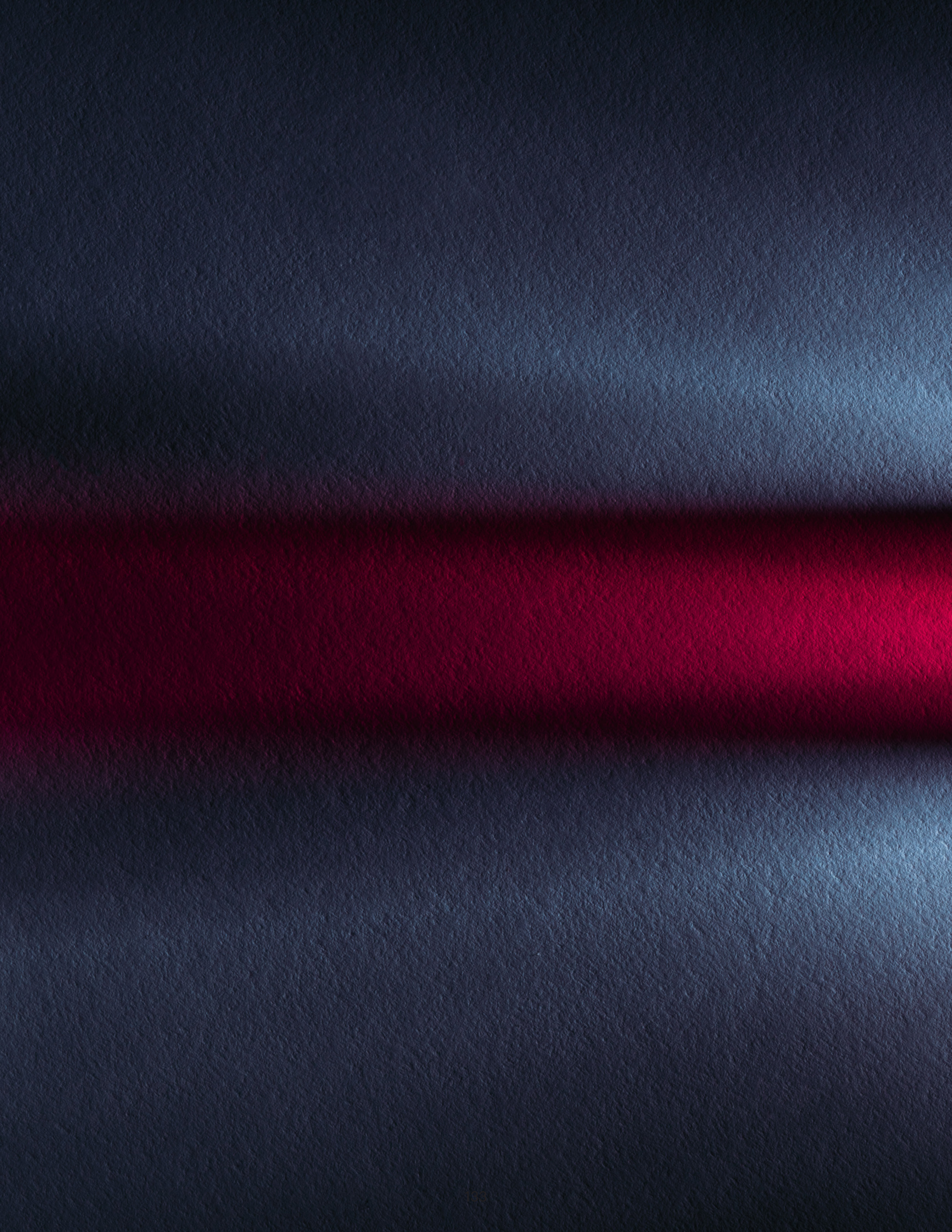
About Bain & Company's M&A value creation study and M&A in times of turbulence

Bain has been studying corporate M&A activity for two decades. We conducted our first quantitative study of company performance as it relates to acquisition activity in 2011 and 2012 and have updated the study multiple times over the years. The findings were confirmed across both studies spanning two decades.

For this year's analysis, the quantitative research reviewed the financial performance and M&A activity of 2,845 publicly listed companies. The initial sample included all publicly listed companies from 15 developed markets for which full financial data was available. We then excluded companies with revenue lower than $500 million in 2007 and those with major swings in their earnings before interest and taxes margin at the beginning or the end of the panel.

To compare company performance, we used total shareholder return (TSR), defined as stock price changes assuming reinvestment of cash dividends. We calculated average annual TSR using data reported by S&P Capital IQ. We analyzed M&A activity by including all deals announced by the companies in the sample between the beginning of 2007 and the end of 2017. The data was based on information provided by Dealogic and included all deals in which a company had made an outright purchase, an acquisition of assets or of a majority interest, or in which multistep deals have been consolidated into a single deal. Deal size for deals with undisclosed value is estimated using median deal value benchmark, calculated for each sector from disclosed deal values as a percentage of acquirer market capitalization.

We then analyzed the acquisition activity for each company by calculating the acquisition frequency and cumulative relative deal value. Acquisition frequency was calculated as the average number of acquisitions per year over the period from the beginning of 2007 to the end of 2017. Cumulative relative deal value was calculated as the sum of deal value divided by market capitalization three months prior to announcement for all deals from the beginning of 2007 to the end of 2017. These metrics characterizing deal activity were then related to the TSR performance of various acquirer cohorts.



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