Baker Tilly International - Acuris thought leadership campaign

# **Global dealmakers:** European M&A market update 2020

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# Contents



## Methodology

From January to February 2020, Baker Tilly International commissioned Acuris Studios, the publishing division of Acuris, to canvas the opinions of 60 dealmakers to gauge their opinions on M&A opportunities, trends and challenges in Europe. Respondents were evenly split and based in the following regions: Asia Pacific, North America and Europe. Given the spread of Covid-19 and the ongoing pandemic, further interviews were conducted from March to April 2020 to assess changes in sentiment and intentions to invest in Europe in the year ahead.

Unless otherwise stated, survey responses reflect sentiment captured as of 22 February 2020 during initial interviews as part of this research.

Within the graphed survey results, percentages may not sum to 100% due to rounding, or when respondents were allowed to choose more than one answer. All quoted data is propriety Mergermarket data unless otherwise stated. All deals are based on announced transactions.

# Foreword

**The world certainly has changed since our 'Global dealmakers: Cross-border M&A outlook 2019' report released last October. Then, the US-China trade war and Brexit were the top concerns for dealmakers. Many were using M&A in response to tariffs and trade barriers arising between major economic powers in North America, Europe and Asia. Still others, were using cross-border M&A to mitigate risks from geopolitical uncertainty and the rising threat of protectionism.**

This was especially true of M&A in Europe, where dealmakers have been dealing with the challenges of geopolitics and economic uncertainty for several years, not to mention the shape and nature of business in the EU following the UK's planned departure. The impact of these events on M&A has been apparent: deals declined 5% in 2019 from the year before, with values dropping 21%. In the first quarter of 2020, deals dropped 33% from Q1 2019, although values went up 26% given several large cap transactions this year. Since Q4 2019, however, deals declined 36% in volume and 5% in value.

Now a new threat has arisen: pandemic and the ongoing spread of Covid-19. The uncertainty around this new challenge has shaken markets and populations globally, sending a crushing blow to stocks, corporate confidence and population centers worldwide. Europe has been particularly impacted as governments impose measures to stop the spread, with Italy and Spain suffering the brunt of European cases of the virus.

It remains to be seen what kind of impact Covid-19 will have on dealmaking in Europe and globally. However, attitudes have shifted regarding the onset of recession regionally and globally. Now, as governments around the world push stimulus measures and execute strategies in response to what has become a global health crisis, it has quickly become a question of "When will the recession be over", as opposed to "When will the recession hit?" Covid-19 and each government's response is also likely to drive some of the trends emerging in Europe, such as protectionism.

Following up from our global research in October 2019, we returned to the market to ask questions about investment intentions and views on M&A in Europe. Their feedback has helped paint a vivid picture of the trends and challenges shaping the region and markets where opportunities are waiting to be discovered.

*2020 is likely to be another record year for M&A, but not necessarily for the right reasons. Global M&A was already starting to show signs of softening – and that was before Covid-19. Now, deals are being put on hold and dealmakers are generally only cautiously optimistic that activity will increase as social distancing measures are relaxed and economies reopen. Even as governments inject record levels of stimulus into their economies, it remains to be seen how effective this will be to keeping businesses alive. If successful, it should help to reduce the level of distressed transactions that will occur over the coming 12-18 months.*

*Michael Sonego, Partner, Australia*
*Global & APAC Corporate Finance Lead,*
*Baker Tilly International*

# Key findings

**73%**
of dealmakers say they are decreasing their M&A in Europe due to the spread of Covid-19

**92%**
say a recession in Europe will unfold within the next 12 months – and 100% say a global recession is imminent

**83%**
say Covid-19 will have a negative impact on global cross-border M&A through 2020 and possibly beyond

**7,710**
M&A deals completed in Europe in 2019, a year-on-year decline of 5%

**US$775bn**
in total M&A deal value recorded in 2019, a year-on-year decline of 21%

**88%**
say acquiring new technology/IP is the top deal driver in 2020

**87%**
say there is great and growing opportunity to make investments into European medicinal cannabis

**18%**
say there are better mid-market opportunities in Europe compared to other regions globally

**Regulatory challenges and rising protectionism**
will be the greatest obstacles to investors searching for European deals

**88%**
say the DACH economies of Germany, Austria and Switzerland offer the most deal opportunities within Europe

**53%**
say they are less likely to invest in the UK given the recent Brexit decision and only 20% see the country as an M&A hotspot

**18%**
of M&A deals in 2019 were completed in the UK, followed by DACH (16%) and Nordics (15%)

# M&A in Europe: **Year in review and expectations for 2020**

**European M&A posted sharp declines in 2019 and with the spread of Covid-19 this activity may sink further yet. However, sentiments collected prior to the pandemic hold a glimmer of hope for what the dealmaking scene could look like once markets recover and confidence returns.**

European M&A may have finally found its peak. Following an upward march that lasted close to a decade, Mergermarket data shows that acquisitions in the region in 2019 slowed, posting declines of 6% in volume and 21% in value from blockbuster totals in 2018. While this is largely in line with global trends, the impact of geopolitical and economic uncertainty are one of many culprits behind the down trend.

Now, in 2020, the world is dealing with Covid-19, the spread of which is impacting dealmakers' confidence, particularly toward Europe. This is especially visible among respondents regarding their intentions to invest in Europe. In February 2020, 37% of respondents said they would increase their M&A spend in the year ahead compared with 32% who said they would be decreasing activity. By April 2020, while 26% say they will make increases, a full 73% will be decreasing M&A – and these respondents overwhelmingly say their decision is based on the impact of Covid-19.

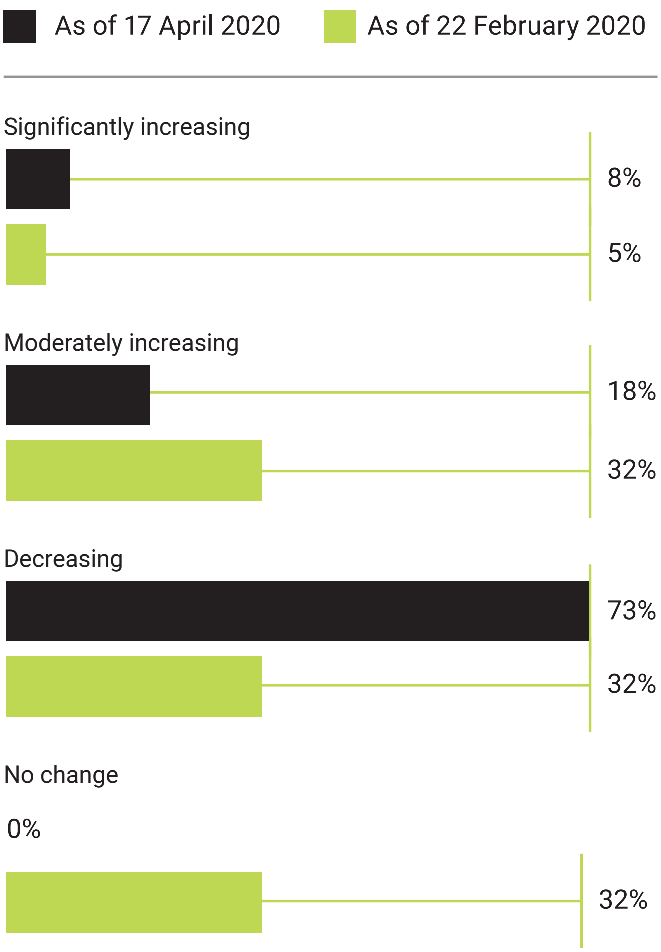
"With regards to investing in Europe, we've had to modify our investment criteria to fit the current conditions. The spread of the virus at such an alarming rate and its impact on business cannot be taken lightly," says one respondent who plans to abandon plans to invest in Europe.

*We think that whereas deal flow is in a paralyzed state, talks are merely being suspended and deal activity is expected to pick up gradually as the virus spread slows down. However, the real question here is what kind of deal terms will be reached in a post-Covid-19 economy?*

*Olivier Williems, Partner, Baker Tilly Belgium EMEA Corporate Finance Lead*

Another respondent agrees with this sentiment, adding that "Europe will take a temporary hit and there will be significant time needed to reinvigorate conditions and see economic growth prospects once again. As such, our current intentions have been negatively affected due to the increase in the number of risk factors."

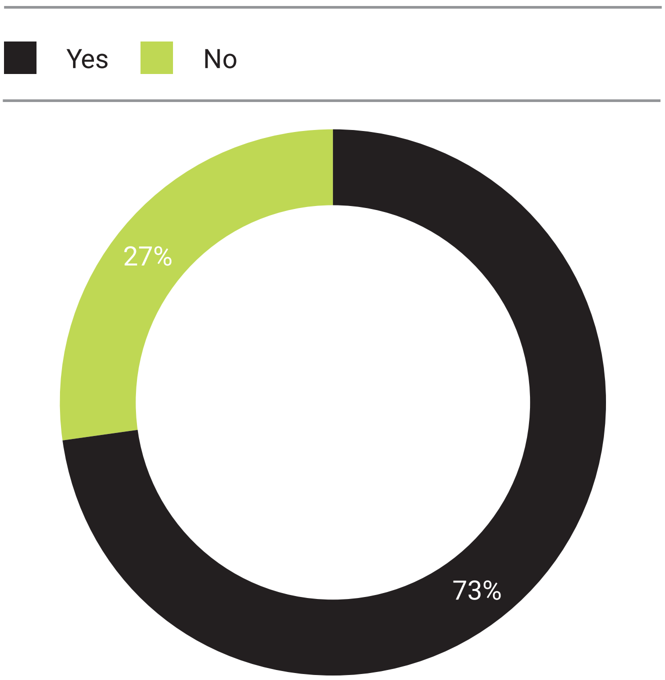
**Figure 1**. Which of the following best describes your intentions with regard to investing/M&A into Europe in the year ahead?



Perhaps the operative word in that last comment is "temporary." Indeed, despite the overwhelmingly negative reactions to Covid-19, impressively the number of respondents who say they will significantly increase investment in Europe actually improved since the start of the pandemic, rising from only 5% in February to 8% in April. It seems, then, that a small but determined minority of investors are realizing that the timing may be right to take action and several mention that the number of opportunities in Europe could increase amid favorable valuations now and into the year ahead.

Indeed, while European M&A has begun to decline and despite the ongoing pandemic, the region is certainly not off the agenda of global dealmakers. Pre-pandemic sentiments show recognition in the market for deals and while M&A timelines may need to be extended to reflect the impact of Covid-19 on market confidence, it does serve as a benchmark from which investing could pick up once the dust of the current pandemic settles.

**Figure 2.** Is the current spread of Covid-19 causing you to reconsider or cancel planned investments into Europe in the year ahead?*




*Results reflect sentiment captured as of 17 April 2020

## European M&A: Shifting gears

Deal values in Europe took the biggest hit, dropping from a record US$986bn in 2018 to US$775bn in 2019. The value decline was due to a noticeable absence of megadeals: compared to the previous year when 10 transactions valued greater than US$10bn were brought to market, there were only four similar deals in 2019.

Slowing economic growth and the possibility of a recession has helped drive deals down over the past year. Growth across Europe was just 1.5% in 2019, compared to 2.2% the year prior. Among dealmakers, many anticipate this growth to slow further, with a recession more than likely in the year ahead, according to 92% of respondents (compared to 46% from opinions collected in February). Respondents likewise now agree that a global recession is imminent, although notable that they were split on this issue only two months ago.

Heightened geopolitical and economic uncertainty has also weighed heavily on dealmakers' confidence. While a Brexit decision has finally been reached, the veil of uncertainty remains thick as the UK goes through a transitionary period in the process of leaving the EU. Likewise, ongoing trade disputes are causing unease, specifically the trade war between the US and China but increasingly tensions between the US and Europe.

Rising protectionism and nationalistic turns in key European markets also caused many corporations to reconsider spending, specifically into neighboring markets. The result has seen a drop in cross-border M&A from 53% of total European deals in 2016 to 50% in 2019, as dealmakers increasingly look within their home markets for opportunities.

Yet, the 7,710 deals valued at US$775bn that were completed (compared to 8,186 at US$986bn) is still impressive and has secured its place among the top years for M&A since 2010. Safe to say, while dealmaking has slowed – as most dealmakers and market participants knew it would – it is far from stopping altogether.

And indeed it hasn't. While deals were down 33% in Q1 2020 from the same period in 2019 (with just 1,301 transactions), deal values of US$193bn placed it as one of the highest quarters in recent years. This was due to several megadeals tipping the value scales.

Despite this, Covid-19 and the focus boards and management will place on business as usual activities that will inevitably impact dealmaking through the rest of the half-year, with volume and values likely to decline until markets and overall confidence stabilizes.

**Figure 3.** European M&A trends

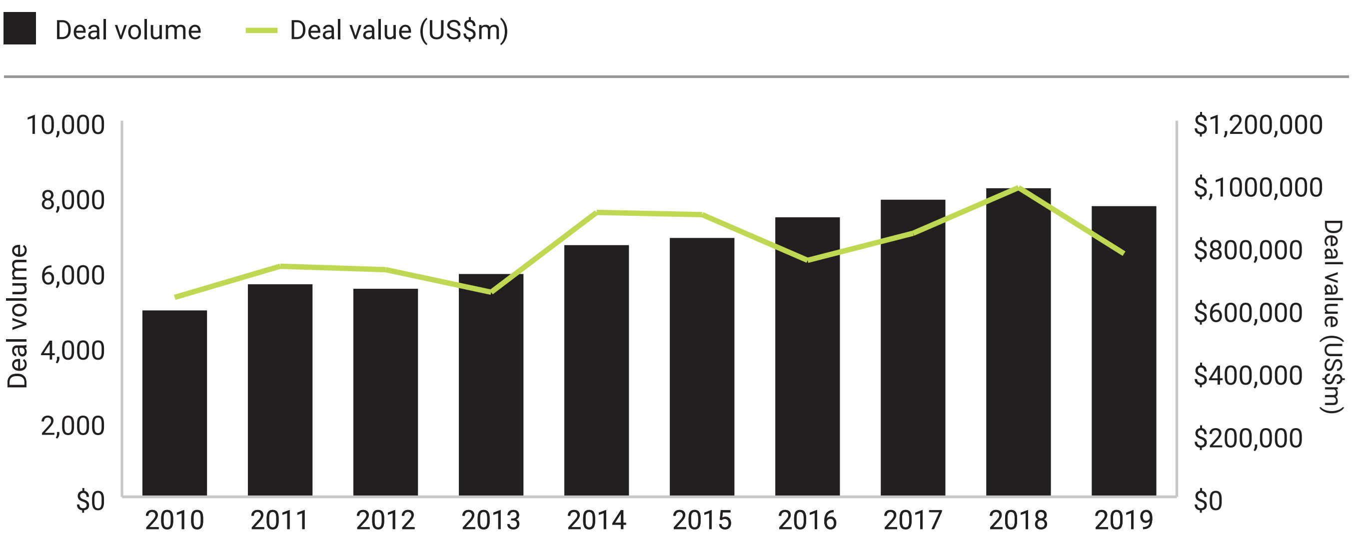
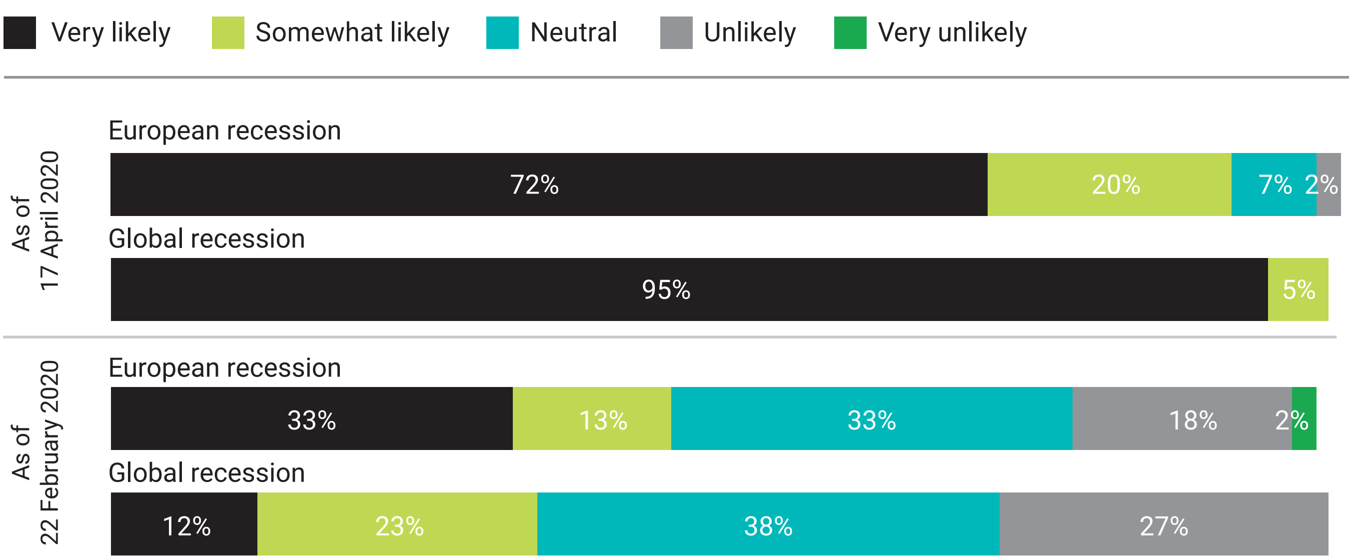



**Figure 4.** Which of the following best describes the likelihood of a global recession and a European recession within the next 12 months?



## Inbound interest

Inbound dealflow decreased in line with regional trends. For 2019, volume was down 10% with value declining 30% since 2018, totaling 1,225 transactions worth US$316bn. While one of the lowest years in inbound volume since 2013, foreign buying maintained some of its strength and still ranks as the highest over the past decade. Indeed, foreign capital remains a deal-driving force in the European M&A market, accounting for 40% of deal values and 16% of volume in 2019.

Inbound M&A has been predominantly trans-Atlantic, with buyers from the United States and Canada accounting for 71% of inbound deals and 75% of inbound values in 2019. Year on year, deal volumes declined 3% and values 5% from 2018.

Interest from Asia Pacific buyers has waned recently. Following several years of growth since 2013, dealmaking started a downward trend starting in 2016 that has yet to reverse. Since 2018, deals have declined 17% with value likewise dropping a dramatic 67% as Asia Pacific buyers reconsider Europe. In 2019, buyers from Asia Pacific accounted for 25% of deals and 20% of values.

## Global M&A snapshot

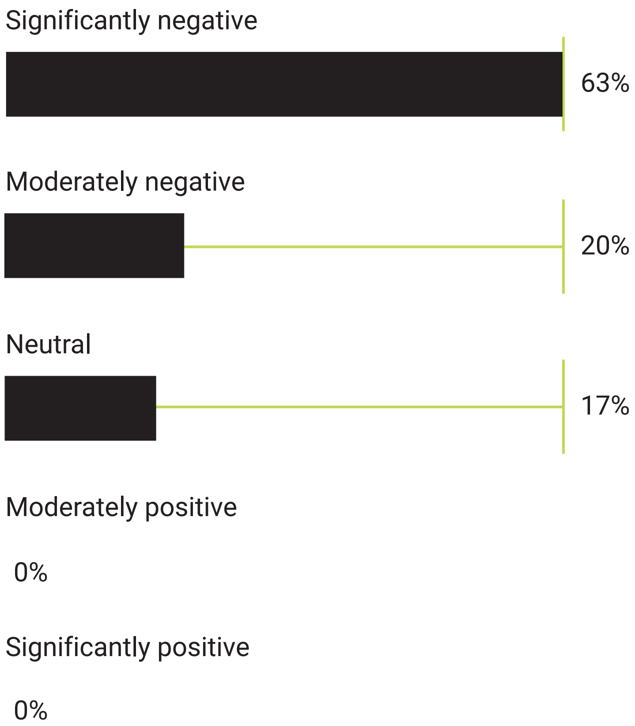
European M&A activity is not completely detached from global trends. Year on year, deal volumes globally declined 5%, although values only subsided 6%. The noticeably smaller decline in global values compared to Europe was due to an uptick in large cap transactions in North America. Indeed, 15 of the top 20 deals of 2019 were the result of domestic consolidations among US-based corporations.

For the year, North American M&A accounted for 51% of global deal values, increasing from 47% in 2018. Comparatively, Europe saw its value contribution to global totals decline, accounting for 23% of values (compared to 28% in 2018).

However, in volume terms, Europe remains an attractive region for dealmakers and accounted for 39% of global deals in 2018 and 2019. North America by contrast accounted for 33% for both years, with Asia Pacific at 23% in 2018 and 21% in 2019.

In Q1 2020, deal volume declined 30% with values following with 41% declines from Q1 2019. Since the final quarter of 2019, M&A globally declined 34% in volume and 33% in value. M&A markets were already showing declines ahead of the virus spreading and Covid-19's full impact on deals may not show for some time, as M&A transactions take months to come together and the economic effects after the virus may be felt by regions and countries for some time. At present, however, respondents feel the near-term impact will be negative, with 83% expecting declines on global M&A, particularly among cross-border dealmakers.

**Figure 5.** Generally, what kind of impact will the current pandemic have on cross-border M&A globally in the year ahead?*




*Results reflect sentiment captured as of 17 April 2020

# Opportunities and challenges

**Investors are drawn to Europe's tech advantages and growing medicinal cannabis opportunities. Mid-market deals are likewise playing into this sentiment. Yet challenges large and small will create obstacles as dealmakers seek growth and value creation in their investments.**

Europe offers significant upside potential and investment opportunities into key sectors. This is particularly true for dealmakers looking to acquire new capabilities and instill transformative growth within their organizations. Respondents highlight many of their reasons to invest in Europe.

## Deal drivers: Tech is top priority

Overwhelmingly, acquiring tech/IP (88%) is the top driver for European M&A. According to one respondent, "We are seeking better and advanced innovations, for which European markets are well known to provide. European [tech] assets are strong in terms of value generation."

Unsurprisingly then, technology, media and telecommunications (TMT) was the top opportunity sector (according to 80%) among dealmakers. It also ranks among the top sectors for deals in 2019, accounting for 18% of volume and 16% of values.

Also, 65% of respondents are also being drawn to Europe's pharma opportunity. While the sector only accounted for 7% of deal volume in 2019, it assumed 21% of values and respondents looking to the sector see its potential for growth and acquisition of IP and expertise.

"Opportunities will continue to be available in pharma and biotech given the sophisticated methods of research and production facilities in Europe," says one respondent. Another expands on this idea by saying that "Constant research and development in pharma and medical sectors and higher return potential is driving the sector forward."

**Figure 6.** Which of the following best describes the main rationale/strategy driving your investment into Europe? (Select all that apply)

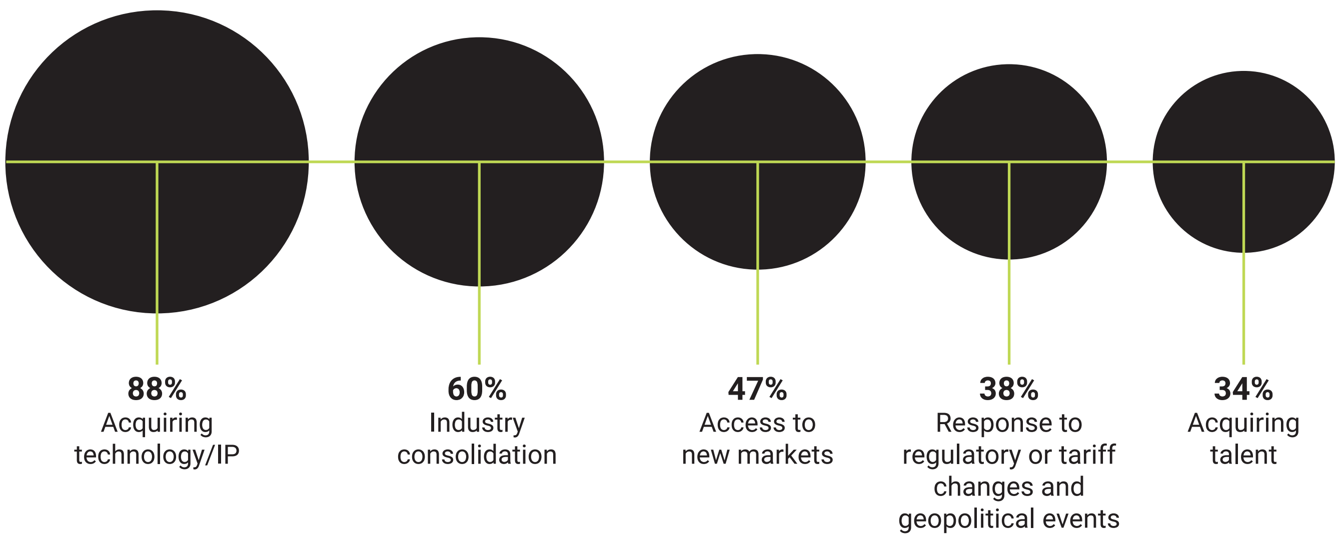
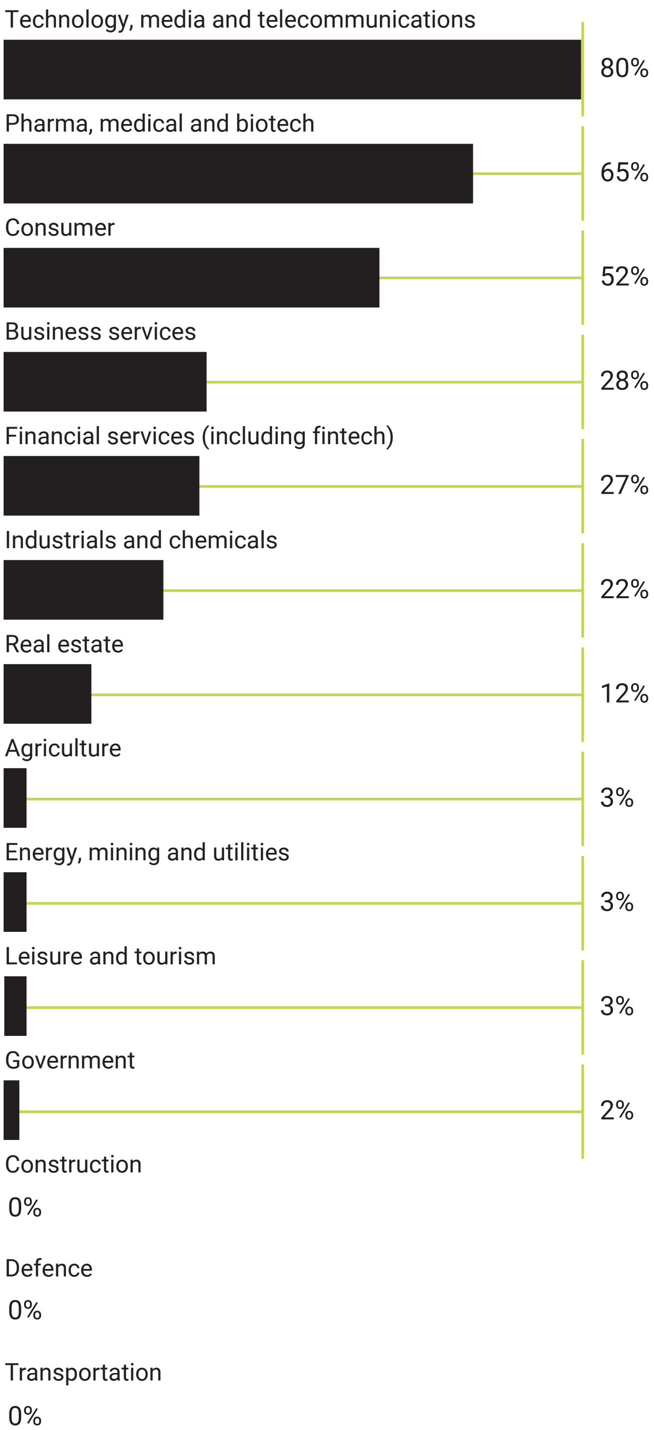


**Figure 7.** Which of the following sectors in Europe do you think will be most attractive over the next 12-24 months? (Please select up to 3 for each column)




## Sector spotlight: Medicinal cannabis

Globally, the fast-growing legal marijuana industry has seen a surge in interest in recent years. Cultivation and distribution has expanded rapidly and countries around the world are beginning to legalize cannabis for medical use, a turn of events that has set investors circling the industry. The medical cannabis market globally was worth US$11bn in 2018 and is expected to grow rapidly to reach US$56bn by 2026. Some estimates hold that this figure could be at least three times larger.

While the North American market accounts for much of the medical cannabis market, Europe is poised to take up a larger piece of the pie. Indeed, legalization across the region, with Germany legalizing medical cannabis in 2017, has triggered a snowball effect as other European countries follow suit. While still in its infancy, dealmakers see the emerging industry's potential and 87% say there is great and growing opportunity to make investments into European medicinal cannabis cultivators and distributors.

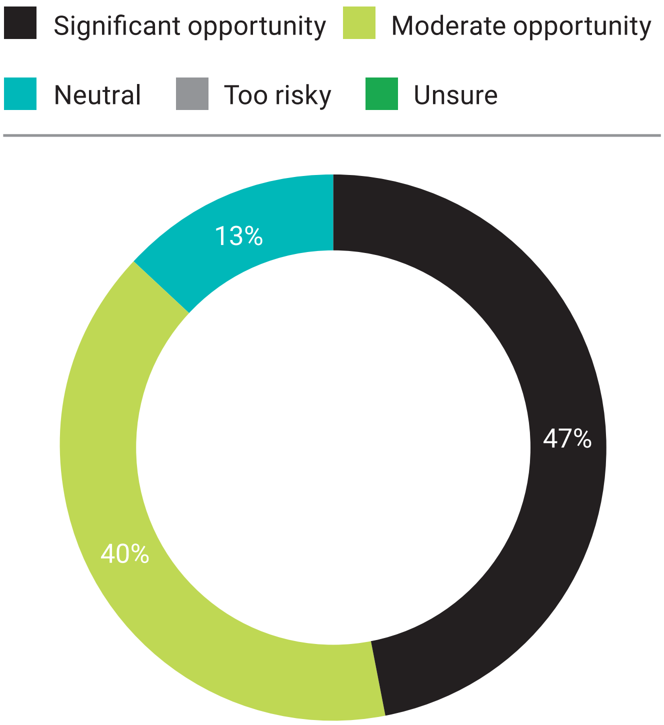
"The number of medicinal cannabis companies has increased significantly and demand is growing. Research and production of medicinal cannabis products have become normalized in few countries, but widespread use across Europe will take time," says one respondent.

*Interest in medical cannabis grows as we steadily move toward a new regulatory paradigm. Even with transcendental legislative challenges ahead, 10 years of unprecedented governmental practice in Europe have provided the necessary room for the industry to emerge and a reliably regulated global marketplace looks today as a fair expectation.*

*José Luis Martín, Partner, Baker Tilly (Spain)*

Another says that “the demand for medicinal cannabis products has gone up significantly and increase in the number of production units is also attractive for investments. Europe has been a stable market for this segment, unlike others where there is lack of clarity with restrictions and applicable laws.”

**Figure 8.** How great is Europe’s medicinal cannabis opportunity?



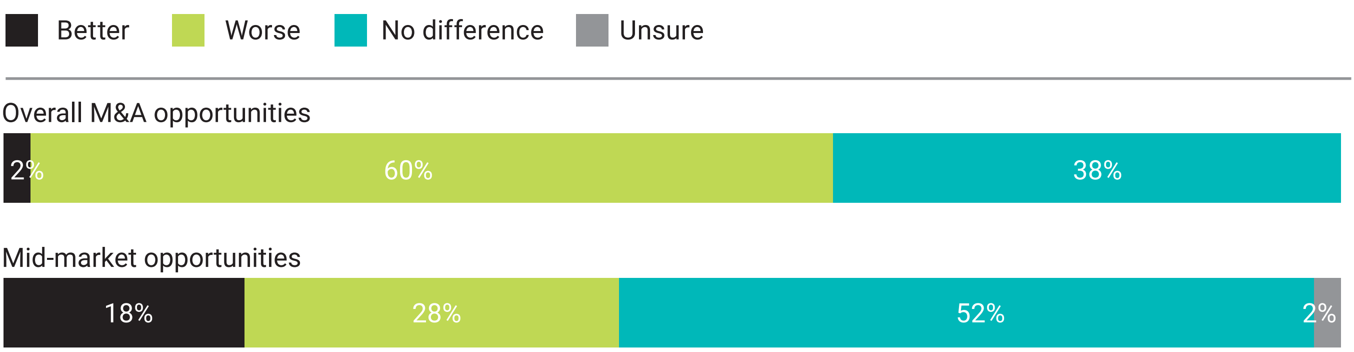

## Europe’s mid-market opportunity

Europe’s mid-market (deals or companies valued between US$15m and US$500m) may be the region’s most compelling reason to invest. According to dealmakers, 18% say there are better mid-market opportunities in Europe compared to other regions globally. While still relatively small, these sentiments are significantly larger than the 2% who say the same for the overall M&A in Europe.

Mid-market companies offer several other advantages. Acquiring these firms can create easier entry points to European markets as there are fewer regulatory hurdles compared to mega deals. They also offer more reliability than small cap firms with untested business processes and uncertain financial stability.

In recent years, the mid-market has accounted for more than 70% of deals, reaching as high as 75% in 2019. Dealmaking in this segment could pick up in the year ahead as mid-market companies undergo financing and revenue strains as consumer demand dries up amid the pandemic. The result could see distressed M&A at depressed valuations or consolidations within industries.

**Figure 9.** Generally, do you feel Europe offers better or worse M&A opportunities compared to other regions?



## Challenges

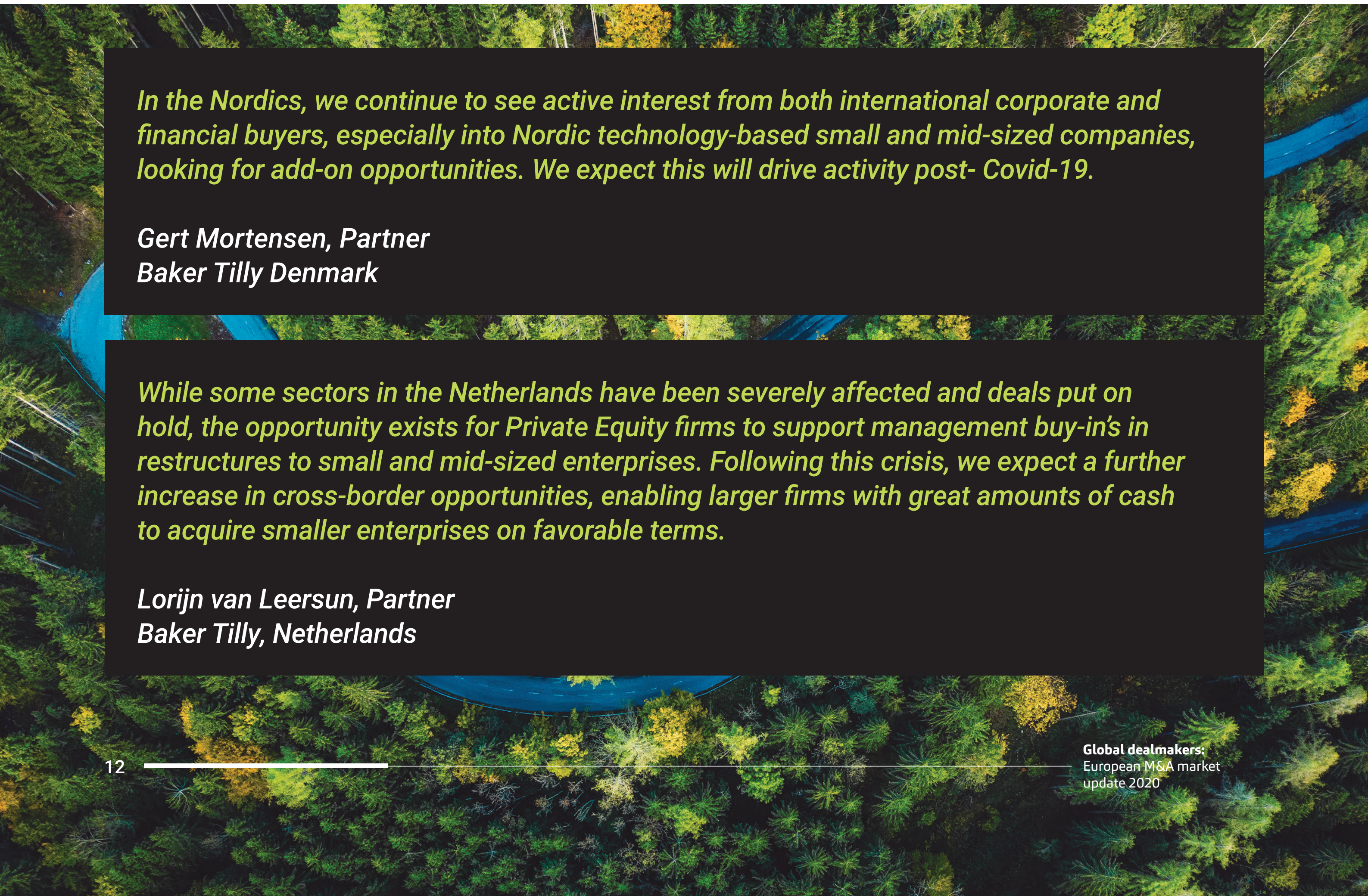
Recession may have been the one factor keeping dealmakers awake at night when our survey was conducted earlier in the year. That issue is now being joined with the nightmare of pandemic. While the pandemic will pass (although how long that will take is uncertain), other factors will create long-term challenges for investors.

Regulatory concerns are one such issue. Respondents were most outspoken about the unpredictable regulatory climate as policymakers increasingly keep corporate leaders and dealmakers on their toes through various reforms and new laws.

Expanding on this theme, respondents say there is no single area where regulation is impacting their businesses. Rather, it seems spread and likely to force many businesses to adjust. According to one respondent, "Environmental and ethical scrutiny has not only increased, but have started to interfere with investment perception entirely." Another says that "anti-trust rulings have been deterring larger companies from entering European markets" followed by another who is convinced that "recent events have been very clear as to how competition laws are being enforced and the financial losses it is causing to companies who have already invested time and effort recently."

Rising protectionism is also inhibiting dealmaking, with one respondent saying that "I think the geopolitical challenges will prevail when trying to complete deals in Europe. Political preferences have changed and protectionist attitudes are also affecting how the target prospects are viewed in terms of future growth."

The confluence of these issues is, in turn, making it challenging for investors to complete accurate, timely and effective due diligence on potential targets and geographies. "Thorough research and evaluation of target potential is not possible since there are economic and geopolitical uncertainties in the market. Market fluctuation and currency depreciation will also be challenging to evaluate when completing M&A," says one respondent.



*In the Nordics, we continue to see active interest from both international corporate and financial buyers, especially into Nordic technology-based small and mid-sized companies, looking for add-on opportunities. We expect this will drive activity post- Covid-19.*

*Gert Mortensen, Partner*
*Baker Tilly Denmark*

*While some sectors in the Netherlands have been severely affected and deals put on hold, the opportunity exists for Private Equity firms to support management buy-in's in restructures to small and mid-sized enterprises. Following this crisis, we expect a further increase in cross-border opportunities, enabling larger firms with great amounts of cash to acquire smaller enterprises on favorable terms.*

*Lorijn van Leersun, Partner*
*Baker Tilly, Netherlands*

# Regions at a glance

**Within Europe, DACH (Germany, Austria and Switzerland) and Central and Eastern Europe are likely to see the most M&A when normality returns. Unsurprisingly, the UK ranks low, although historical trends show that investors have continued to do deals there despite the ongoing uncertainty around Brexit.**

Europe offers diverse advanced and emerging market opportunities. Respondent optimism and historical M&A trends shows strong opportunity for investments across the region.

## DACH (Germany, Austria and Switzerland)

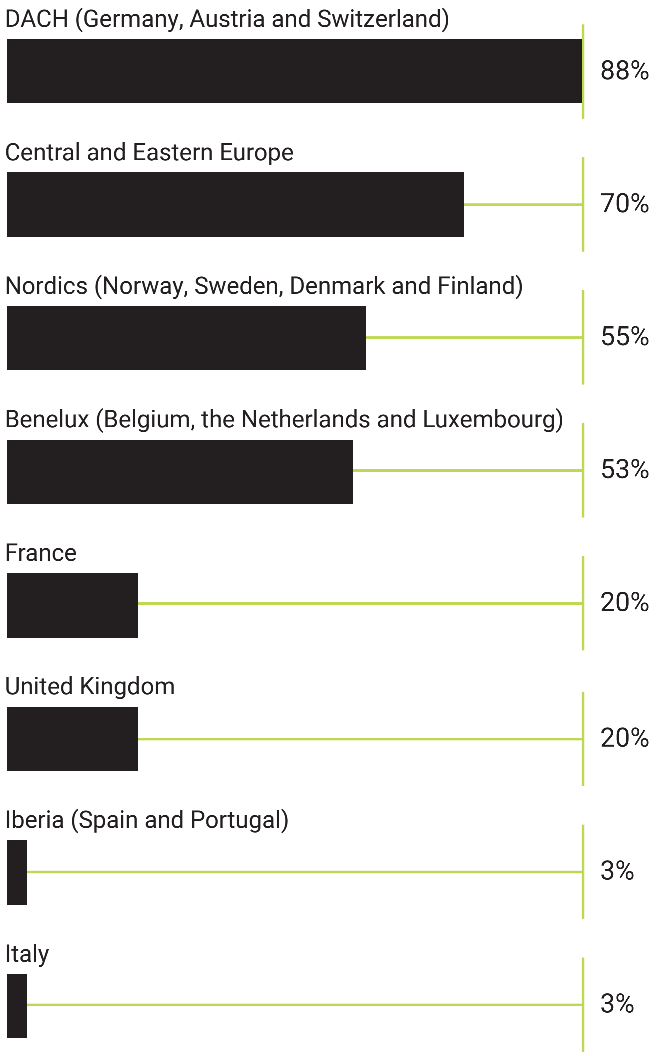
Most respondents (88%) say the DACH economies offer the most deal opportunities within Europe. Despite growing political and economic pressures, dealmaking has held up surprisingly with totals of 1,251 deals valued at US$145bn for 2019. While this was a decline of 6% by volume and 16% by value from 2018 (1,327 deals valued at US$172bn), they were some of the smallest declines across Europe and speak to the German-speaking regions versatility and resilience to uncertainty. For 2019, DACH accounted for 16% of deal volumes and 19% of deal values in Europe.

Private equity activity contributed heavily to this dealmaking and respondents feel private capital will continue to play a role in DACH and European M&A into the year ahead. Other drivers will involve inbound interest given the perception that DACH companies are more “global” and integrated with worldwide supply chains and markets. Respondents also say that DACH companies may be ahead of the curve, having adopted advanced tech and best practices to make them regional, if not global, leaders in their industries.

## Central and Eastern Europe

Respondents (70%) also say Central and Eastern Europe (CEE) offers some of Europe’s best M&A opportunities. While CEE only saw 672 deals worth US$49bn in 2019, it was one of the few sub-regions in Europe to experience growth in these totals, increasing 6% in volume and 5% in value from 2018. However, CEE still accounts for a smaller portion of the European M&A pie: just 9% for deal volume and 6% for deal value.

**Figure 10.** Which of the following countries/sub-regions offer the best investment opportunities? (Select all that apply)



Even so, CEE offers advantages that respondents recognize as key to driving deals. Most notably, CEE's economic growth has consistently outpaced other European markets in recent years and is projected to continue through 2020 and beyond. Equally, according to one respondent, "Central and Eastern European markets are also stable enough for investors to consider in the next two or three years" while another says that because of its growth potential and relatively untapped market potential "CEE offer good testing grounds for financial and technology solutions, which makes it an attractive destination, apart from it being stable economically."

## The Nordics and Benelux

The Nordics (55%) and Benelux (53%) are also favored to see increasing investment. The Nordics subregion (Norway, Sweden, Finland and Denmark) saw the third-most M&A within Europe for 2019, accounting for 15% of deals and 11% of values. However, this was a year-on-year decline of 3% in deals and 18% in values. According to respondents, "Nordics has been developing at an impressive rate, with their industries being enhanced with technological guidelines and increasing capabilities." Other respondents note that the Nordics economies lack the political drama that has become commonplace in many of Europe's more dominant markets.

Benelux (Belgium, Netherlands and Luxembourg), too, offers this sense of security. While some respondents point to its stability in political terms, others note the business advantages these economies offer. "The Netherlands and Luxembourg have been attractive investment destinations for small to medium enterprise sectors. The rate of development has been higher in these countries," says one respondent.

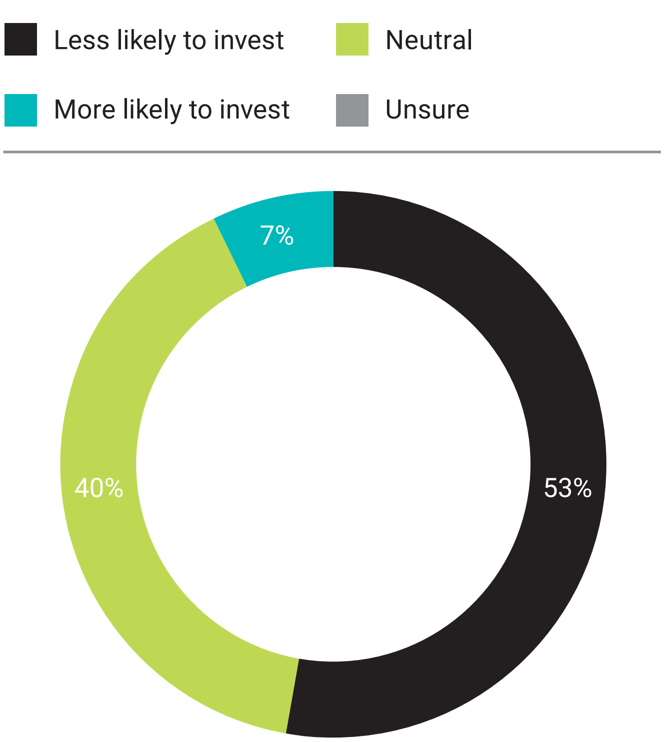
Already, dealmakers seem to be taking notice. While Benelux only accounted for 11% of deals and 9% of values in 2019, it did see the greatest increase in overall dealmaking since 2018. Year on year, deals increased 7% by deals and 47% by values to reach 850 transactions worth US$68bn in 2019.

## UK and Ireland: The Brexit issue

While ranking low among potential investment targets in 2020 (only 20%), the UK remains Europe's top market for M&A. The country accounted for 18% of deals (1,444) and 20% of values (US$157bn) in 2019. Notably, however, these totals declined precipitously from the year before, sinking 13% in deals and 37% in values from 2018.

Will this decline in dealmaking become the trend? Possibly, especially since the UK's future remains uncertain even after a Brexit decision was reached earlier in 2020. Indeed, this clouded future seems to be weighing on respondents, with sentiments largely in the negative regarding their investment intentions toward the UK: 53% are less likely to invest given the Brexit decision and 40% are undecided.

**Figure 11.** What impact will Brexit have on your decision to invest in the UK within the next 12 months?



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