

Global dealmakers

M&A outlook 2023

Now, for tomorrow



Once again, we have seen the dealmaking landscape remade, this time in response to economic and geopolitical factors rather than health and social drivers. Despite the challenging market conditions, dealmakers remain optimistic, with many planning to increase deal activity over the next 12 months. Cross-border M&A remains relevant for businesses looking to expand their technical capabilities and grow their geographic reach.

Harsh Maheshwari
Head of Corporate Finance, Baker Tilly

Foreword

The last 12 months have been challenging for global dealmakers. Many have had to reset expectations and recalibrate risk appetite as macroeconomic headwinds and geopolitical uncertainty put the brakes on deal activity. Inflationary pressures have likewise weighed on decision-making.

Global M&A deal value dropped by close to a third in 2022, as the war in Ukraine, soaring energy costs, rising inflation, and climbing interest rates hit market sentiment and saw investors and corporates scale back M&A ambitions and take a more cautious approach to new investment.

The contrast with the ebullient market of 2021, when abundant liquidity and low interest rates spurred M&A activity to record highs, has been stark. Inflation – running at 40-year highs in developed economies – has left central banks with little option but to raise interest rates. Balance sheets have come under strain as a result, and financing for new deals has become more expensive and harder to source. M&A investors on the buy-side, meanwhile, have been reluctant to pay yesterday's multiples for assets that now face an uncertain future, while vendors have decided to delay sales until market conditions improve.

Yet as challenging as the market has been, corporates and private equity dealmakers have not drawn up the shutters. When assets have transacted, lower entry multiples have made for compelling investment opportunities, and M&A has been a crucial tool for unlocking synergies and building scale. Companies also continue to turn to dealmaking to digitalise their organisations and expand into new markets.

Despite all the headwinds, cross-border M&A has remained particularly relevant for businesses looking for opportunities to expand their technical capabilities and grow geographic reach.

In this research, we explore the outlook for global M&A in 2023 and beyond. Our research finds that dealmakers are overwhelmingly optimistic, with the majority planning to increase deal activity during the next 12 months. We look into the tactics and strategies dealmakers are implementing to sustain deal flow in what is still a tough market and explore some of the key drivers and challenges that will influence their decisions.

This is still a volatile period in the economic cycle, but dealmakers can't afford to sit still, and remain on the lookout for deals that further their strategic aims or offer long-term value.

We hope you find the report informative and helpful, and our partners would welcome the opportunity to discuss the findings further.

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About this report: In Q1 2023, Mergermarket surveyed 150 global dealmakers to gain insights into their investment intentions and perceptions regarding M&A trends in key markets. Respondents were evenly split across regions and domiciled in North America (33%), Asia Pacific (33%) and Europe (33%). By organisation type, 50% were corporations and 50% were PE/VC firms. All responses are anonymous, and results are presented in aggregate. 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. Data in this report comes from Dealogic and was compiled on 5 January 2023. All figures are in USD unless otherwise stated. Deal values are approximations.

Key findings



52%

of respondents say global M&A will increase in the year ahead.



46%

say rising inflation and geopolitical challenges are actually making them more likely to engage in cross-border M&A.



82%

say they have completed a cross-border deal in the past year – and 11% who have not say they are actively looking for such opportunities.



59%

say they are looking for M&A opportunities in Western Europe, and 46% say they have their sights set on North America.



73%

say increasing market share and geographic expansion is a top deal driver for cross-border M&A.



69%

say digital transformation will be a primary driver of cross-border M&A.



78%

say the mid-market (deals valued between US\$15m-US\$500m) will see the most activity in the year ahead.



55%

say their most recent mid-market deal met or exceeded expectations.



49%

say a difficult economic environment will be the top challenge facing dealmakers as they pursue cross-border deals.



52%

say due diligence is becoming more difficult compared to 12 months ago.



45%

say ESG considerations factor into every deal – and 32% say they factor it into most deals.



61%

say TMT is the most attractive sector for deals, followed by industrials and chemicals (51%).



Global M&A dealmakers anticipate a robust year ahead despite geopolitical and economic headwinds

Despite a rising tide of macroeconomic and geopolitical challenges, dealmakers are sending strong and clear signals that they will continue to pursue deals in 2023 and beyond.

In fact, most respondents say that current challenges – including inflationary pressures and uncertainties caused by the war in Ukraine – are creating opportunities for deals. As such, 52% say they will be increasing domestic M&A and close to half (46%) say they will pursue more cross-border transactions (Figure 1).

More generally, many respondents see a robust deal market through 2023 with more than half (52%) expecting global M&A to increase (Figure 2). Another third (31%) are confident levels will at least remain stable.

Indeed, respondents believe that current volatile market conditions could pave the way to acquire high-quality assets at attractive valuations. The MSCI World stock market index shed 17.73% in 2022, with the decline in equity market values dripping down into the M&A space. According to Bain & Co analysis of Dealogic data, M&A deal multiples dropped from a historic high of 15.4x EBITDA in 2021 to 11.9x in 2022. This did see some vendors pull deals out of sales processes – but for buyers, market dislocation has offered compelling value, especially for mid-market deal targets.

“In the next 12 months, there will be a significant increase in M&A activity in Europe and Asia Pacific due to valuations and the greater availability of deals in the small and mid-cap markets,” a director of strategy at an Italian business said.

Dealmakers also see M&A as a tool for reducing overheads and finding synergies at a time when corporates and consumers are reducing spending and liquidity is tight.

“Both cross-border and domestic deals will increase. We want to adapt to the changing market conditions in a systematic manner. We will be pursuing more cost synergies in the next few months,” the head of mergers and acquisitions at a German firm said.

Cross-border M&A: Driving growth in new markets

Geopolitical tensions between the West and China, the war in Ukraine, and tighter regulatory oversight of foreign investment into key strategic industries are not stopping businesses from looking beyond their home markets for attractive deal targets.

Cross-border M&A has been key to recent strategies – and this will continue as dealmakers search the globe for opportunities. Most dealmakers (82%) have completed a cross-border deal in the past year – and 7% who said they haven't are now prioritising opportunities outside their home markets (Figure 3).

"We are actively looking for cross-border deal opportunities. I think it is time that we expand our activities to new markets. A more diversified approach is needed when market conditions are volatile," the managing director of a Malaysian company said.

Only 27% said they would focus on domestic deals in the year ahead (Figure 4). Respondents cite valuations (86%) and skilled labor (67%) as the key factors that make some regions more attractive for investment than others (Figure 5).

Global ambitions: Value in key markets

Most respondents – and by a wide margin – will look for deals in Western Europe (59%) and North America (46%) when considering investments outside their home turf, with the stability and cultural similarities of the two markets appealing to dealmakers.

"We would like to invest in the UK and North America primarily. We can focus on important objectives, and it will be easier to conduct integration activities. There are few cultural challenges," a UK partner at one firm said.

Figure 1. What impact will rising inflation and the war in Ukraine have on your dealmaking appetite in the year ahead?

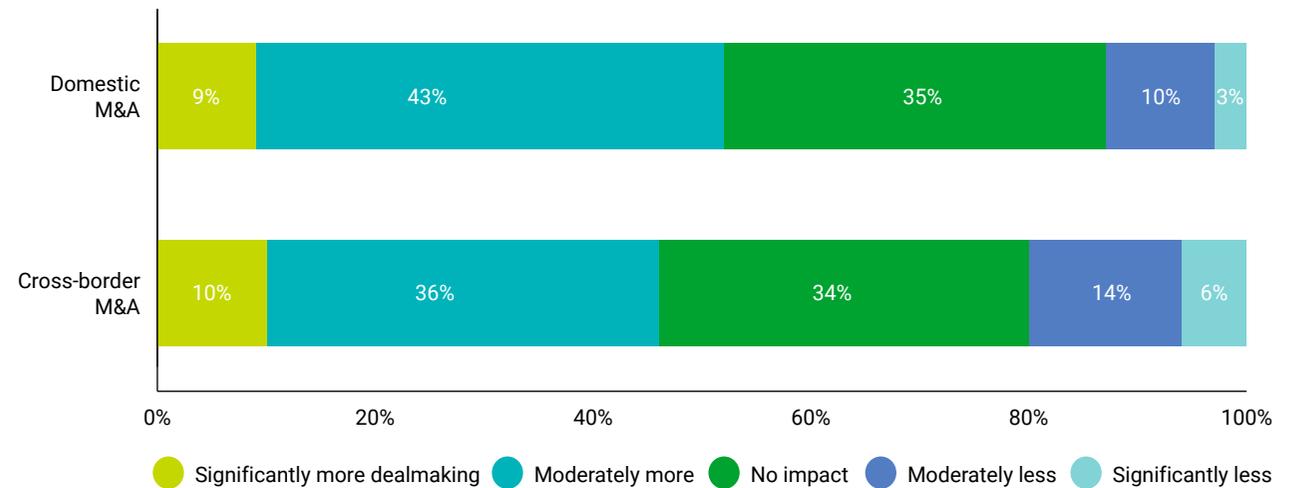
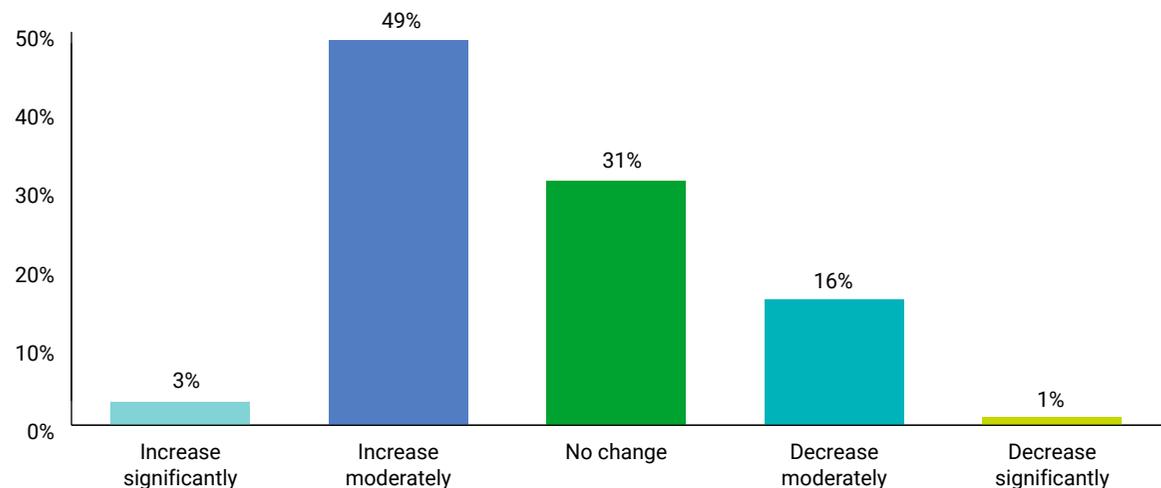


Figure 2. What do you think will happen to the level of global M&A activity in the next 12 months?



Big ticket cross-border deals between the two regions in 2022 include UK-based pharma company GlaxoSmithKline's US\$3.3bn acquisition of US vaccine developer Affinivax, and the Royal Bank of Canada's £1.6bn takeover of UK wealth manager Brewin Dolphin. These deals demonstrate the resilience and strategic value of transatlantic dealmaking.

APAC markets ranked lower, but still offer attractive emerging market opportunities for dealmakers with the right risk tolerance and deal strategies.

"There are developing economies in Asia Pacific and the cost of labour and manufacturing is quite low. These will be the main considerations when pursuing deals in Asia Pacific," the managing director of a Vietnamese corporation said.

Notable cross-border deals into the APAC region include US-based PE firm Warburg Pincus leading a US\$250m investment in Vietnamese real estate developer Novaland and the US\$7.4bn takeover of Hong Kong-based Baring Private Equity Asia by Swedish private markets investor EQT.

Figure 3. Have you completed a cross-border deal in the past 12 months?



Figure 4. Where will your company/firm look for investment opportunities in the year ahead?

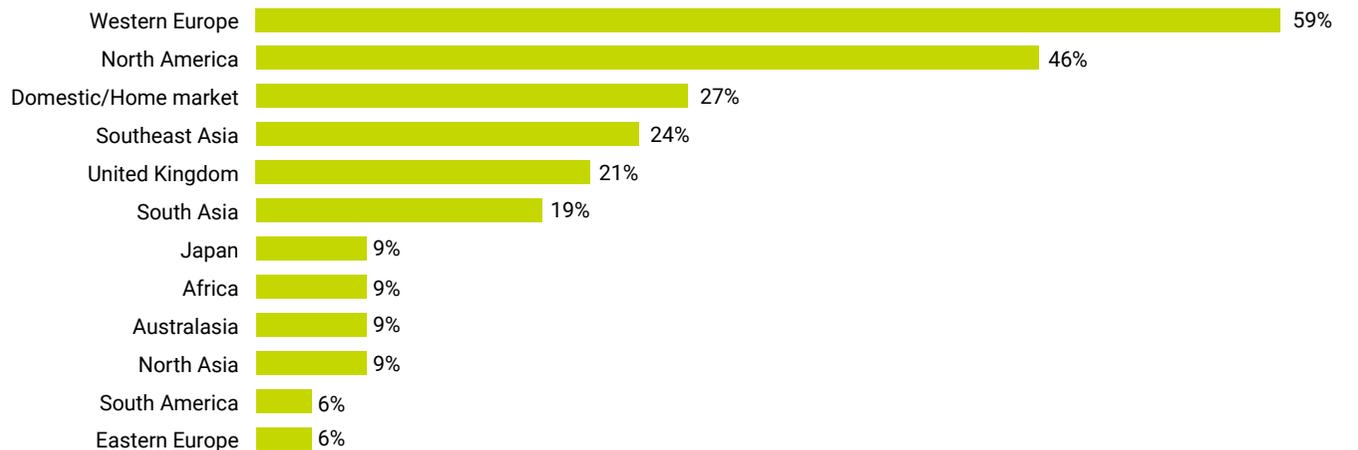
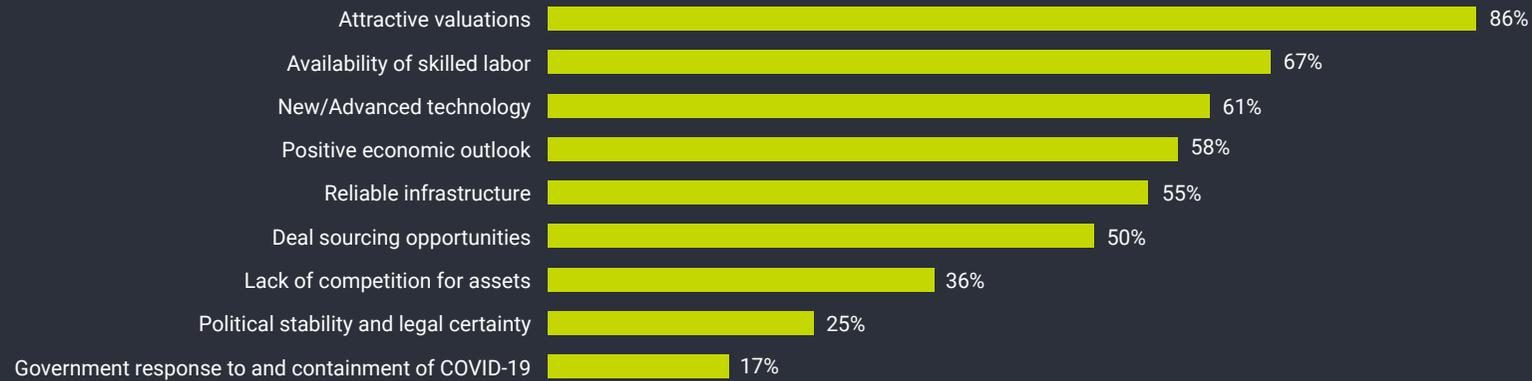


Figure 5. Regarding the geographies where you intend to invest within the next 12-24 months, which of the following makes them attractive investment destinations?



Dealmakers are being driven to find value, and they are looking beyond their domestic markets to find well-priced talent, technology and opportunities to diversify. At the same time, cross-border dealing comes with a heightened risk awareness, so we expect due diligence timeframes for cross-border activity to reflect this greater sensitivity.

Michael Sonogo
Partner, Pitcher Partners Australia

Global M&A: State of the market

Global dealmakers experienced a challenging year in 2022. The Ukraine conflict, rising interest rates, climbing inflation and choppy equity markets dampened risk appetite and put deals on the backburner after a bumper year of activity in 2021.

Global deal value declined by almost a third (31%) from US\$5.82tn in 2021 to US\$3.96tn in 2022. Cross-border deal value and domestic deal value suffered similar fates, with year-on-year declines of 36% and 29%, respectively.

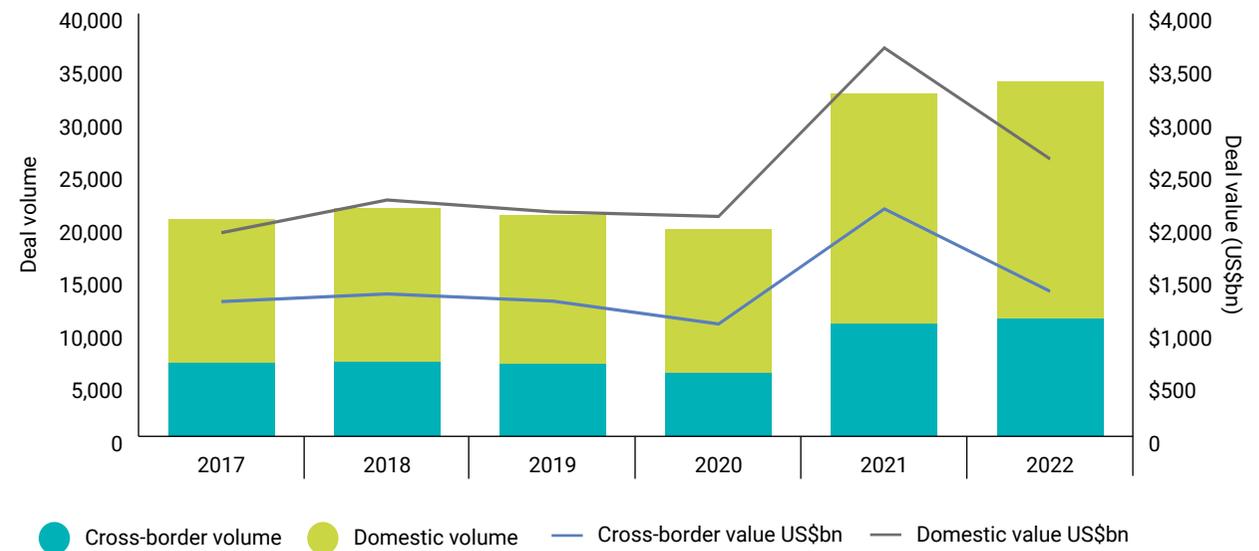
Despite this backdrop, worldwide M&A activity has on the whole held up well. Cross-border and domestic deal volumes actually increased slightly on 2021 levels, and deal value totals, although down year-on-year, are still ahead of pre-pandemic totals.

The figures indicate that although mega-deals may have been put on hold for now, M&A has remained a strategic imperative in turbulent times. Private equity firms and corporates alike continue to pursue smaller bolt-on acquisitions and deals that open new markets and cost synergies.

Steady transaction volumes and stable, long-term deal value totals through the current period of dislocation have given dealmakers confidence in the M&A market's resilience, placing dealmaking firmly on the radar for the next 12 months.

"Continued dealmaking is needed even in this unpredictable situation. We have to reach new customers in new markets, and acquisitions in the next year can help us achieve these goals," the managing director of a US business said.

Figure 6. Global M&A



Investors have become highly selective and are investing more resources in due diligence to ensure that deal targets pass muster, but companies that clear the quality will continue to trade.

"We have not let the conditions impact our dealmaking appetite. In the next year, we will think about new deals objectively. Assessing the target company thoroughly will be important," a partner at a Dutch investment firm said.



Legacy technology remains a challenge for many companies, but M&A presents a swift solution for restructuring and repositioning, as long as a suitable target can be identified. More broadly, VC funding for technology may be dwindling, and some investors are downgrading their investments in the sector. Although this may pose challenges for TMT companies, it could be favourable for those seeking market consolidation and bolt-on technology buys.

Xavi Mercadé
CEO, Baker Tilly Spain

Deal drivers: Preparing for macro challenges and boosting digital transformation are core priorities

Global dealmakers see cross-border M&A as vital to achieving growth strategies and restructuring efforts in 2023. Indeed, as they prepare for challenging market conditions ahead, strategic drivers and investment objectives are focused on several key themes:

Restructuring for growth and efficiency

Boosting growth and restructuring business models are top of mind for dealmakers and many are using their cross-border investments to achieve these goals. Recent deals have been driven by the search for increasing market share and geographical expansion – and 73% expect this to be the top priority going forward (Figure 7).

Likewise, supply chain resilience is another key theme informing cross-border deal rationales, with 60% focusing on expanding supply chains. A surge in demand for goods as economies reopened after lockdowns, coupled with the impact on the supply of energy, chemicals and foodstuffs as a result of the Ukraine war have put supply chains under severe pressure, resulting in bottlenecks and inflation.

Companies have responded by acquiring targets that strengthen their logistics capabilities and give them control of production, as seen with clothing retailer American Eagle Outfitters buying fulfilment technology business Quiet Logistics and engine maker Cummins acquiring parts supplier Meritor.

“We will be sourcing deals to expand our product range and also ensure that the supply chains are more flexible,” the vice president of a Belgian corporate said.

Improving economies of scale (45%) is also driving deal strategy, as companies position to weather inflationary pressures and macro uncertainty. This emphasis on stability is further underscored by the finding that more dealmakers are focused on strengthening their industry position through consolidation (43%) than ambitious transformational acquisitions (16%).

The digital agenda

Digital transformation and buying IP was the second greatest strategic priority, according to 69% of respondents. “Digital transformation has become important to increase the profitability from operations in many sectors. Integrating automation and other favourable technologies helps derive more profits in the long term,” the managing director of an Australian corporate said.

The senior managing director at a US business added: “We will be sourcing new targets in cross-border markets to acquire new technology. Digital transformation strategies do work well to accelerate growth and also meet client expectations.”

Examples of companies turning to M&A to upgrade digital capabilities include US block chain security group Fireblocks paying US\$100m for Israeli digital asset payments platform First Digital to broaden its payments offering and develop tools that embed digital asset technology in day-to-day back-office processes. US fintech platform Shift4, meanwhile, agreed to pay US\$575m for Israel-based Finaro to upgrade its cross-border payments functionality.

Mid-market M&A

Respondents also say mid-market deals (those valued between US\$15m-US\$500m) will drive M&A in the year ahead. Overwhelmingly, 78% say the mid-cap transactions will account for the majority of deals (Figure 8).

“The consistency of financial output from mid-market companies will drive more deal activity. In most regions, mid-market deals are completed systematically as compared to the small- and large-cap space,” an Italian strategy director said.

Unlike mega-deals, which require large debt packages and liquid capital markets for funding, mid-market deals have been shielded from dislocation in syndicated loan and high-yield bond markets. Buyers have been able to finance deals entirely with equity or with support from private debt providers, who have remained open for business despite interest rate and inflationary pressures.

Respondents also point out that in a period of uncertainty, dealmakers are more cautious about writing big cheques to fund blockbuster transactions, preferring to back a more diverse spread of mid-market assets and add-on acquisitions. The risk of large deal negotiations breaking down in an economic downturn, coupled with antitrust regulatory risk, has seen dealmakers pivot toward more mid-market deals too.

“There are fewer risks investing in mid-markets, so the number of deals will be higher. Large-cap companies are not very stable and deals in the large-cap market will be scrutinised more by regulators,” a partner at a UK investment firm said.

Figure 7. Which of the following best describes the main strategic driver of your most recent cross-border acquisition? What do you anticipate will be the main driver of future cross-border acquisitions?

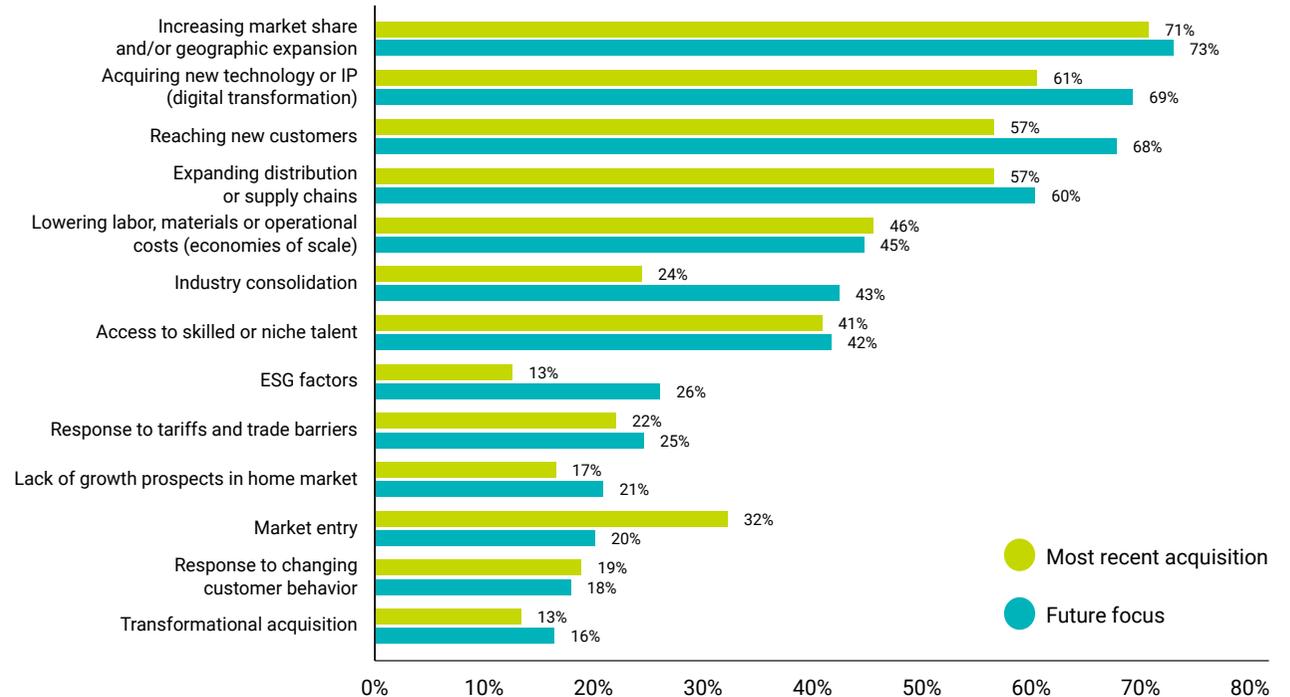


Figure 8. Which deal segment will see the most M&A activity (by deal volume) over the next 12 months?





It is tempting to see the decline of mega-deals as a broader symptom of a challenging market, but global mid-market M&A had a record year for volumes in 2022, and only saw a minor decline in value. We can see that mid-market M&A continues to be a sweet spot for dealmakers, while dealmakers are highly attuned to looking beyond their domestic borders for opportunities.

William Chapman
Partner, Baker Tilly US

Deal focus: The mid-market opportunity

Dealmakers are increasingly turning to the mid-market to capture value and harness synergies. Every respondent in this research completed at least one mid-market investment in the past two years – and more than half (55%) say these deals met or exceeded expectations (Figure 9).

Key drivers and trends

Mid-market deal flow is supported by a range of strategic drivers:

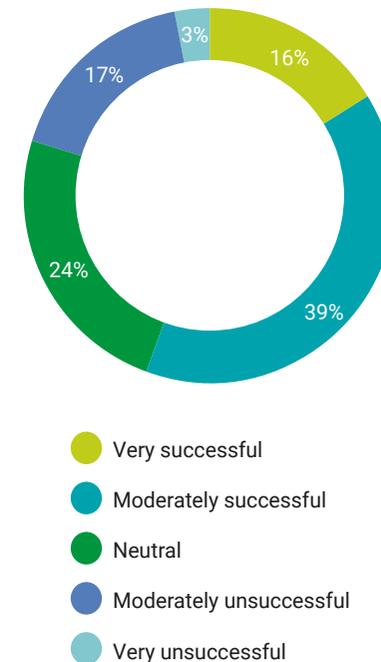
Digital transformation

Dealmakers are not only focused on valuation, and many will turn to mid-market M&A to help with digitalisation and facilitate change across the broader organisation. As such, 23% say digital transformation will be the top driver of mid-market M&A (Figure 10). “Digital transformation will be the main driver of dealmaking activity. Companies want to differentiate their services, providing more advanced digital solutions to their clients,” a managing director at a US corporate said.

Mid-market momentum

Mid-market M&A continued its upward trajectory in 2022, reaching historical highs as the deal segment continues to deliver value for dealmakers (Figure 11). Deal totals rose 9% year on year, greater than the 4% for global totals. Similarly, value only declined 7% from 2021, compared to the 31% drop for global values. Across the deal spectrum, mid-market deals accounted for 32% of all M&A in 2022, the highest percentage since 2017.

Figure 9. How successful was your most recent mid-market acquisition in yielding the intended value from the deal or achieving business objectives?



- Very successful
- Moderately successful
- Neutral
- Moderately unsuccessful
- Very unsuccessful

Succession planning

Planning for the next generation of leadership as founders and owners look to exit their businesses will be the second greatest driver of mid-market M&A. As the baby boomer generation retires, many mid-cap businesses will be put up for sale, creating opportunities for strategic and private buyers to add to existing portfolios. The partner of a UK investment manager added: "Succession planning is required in many established companies in the mid-market. There will be more emphasis on involving partners who can drive innovation and customer engagement in the future."

Distress-driven deals

Respondents recognise, however, that mid-market businesses are not immune to macroeconomic headwinds. Smaller mid-market assets are more likely to have single supplier and customer exposure. In a tight labor market, mid-market companies are also more vulnerable if key staff depart. A fifth of respondents expect to see rising financial distress and insolvencies in the mid-market as a result, which will drive M&A.

"Distress-driven opportunities will drive activity. There are many companies in the mid-market segment that have not been able to manage their cash flow adequately. This has resulted in an increase in insolvency numbers," a managing partner at a US-based investment firm said.

Figure 10. Which of the following will be the main driver of mid-market M&A in the next 12 months?

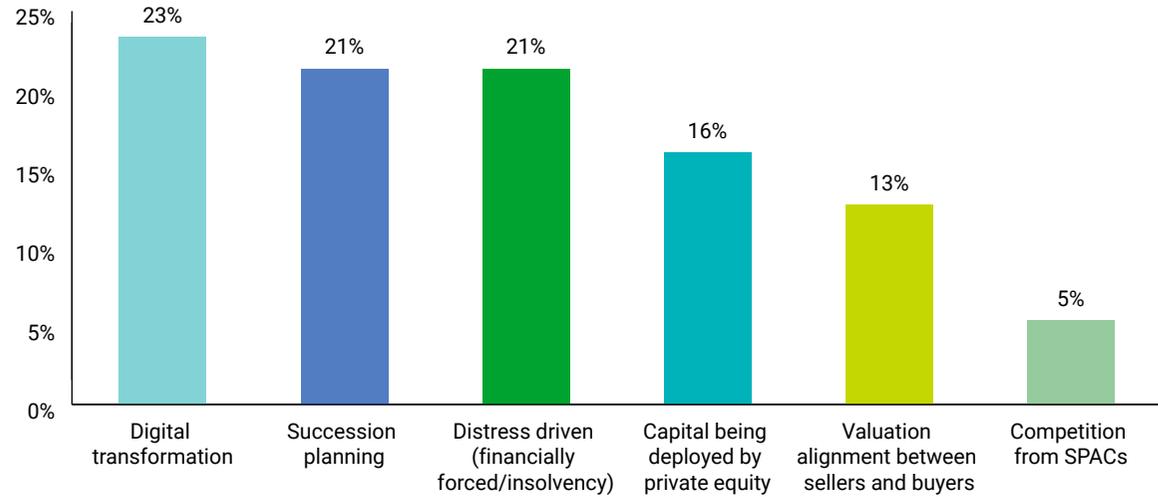
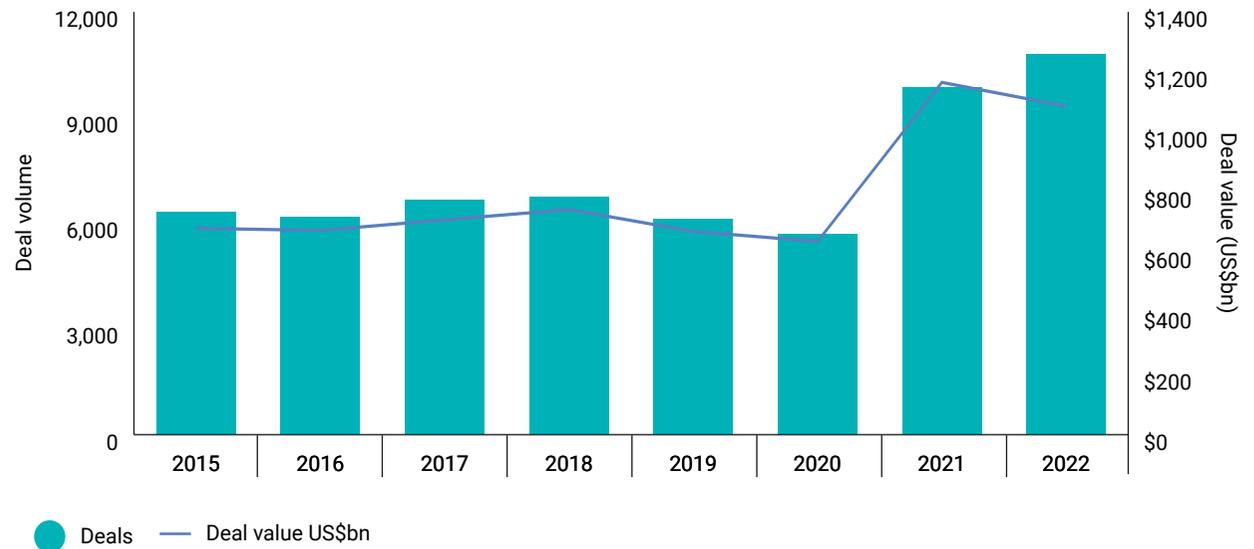
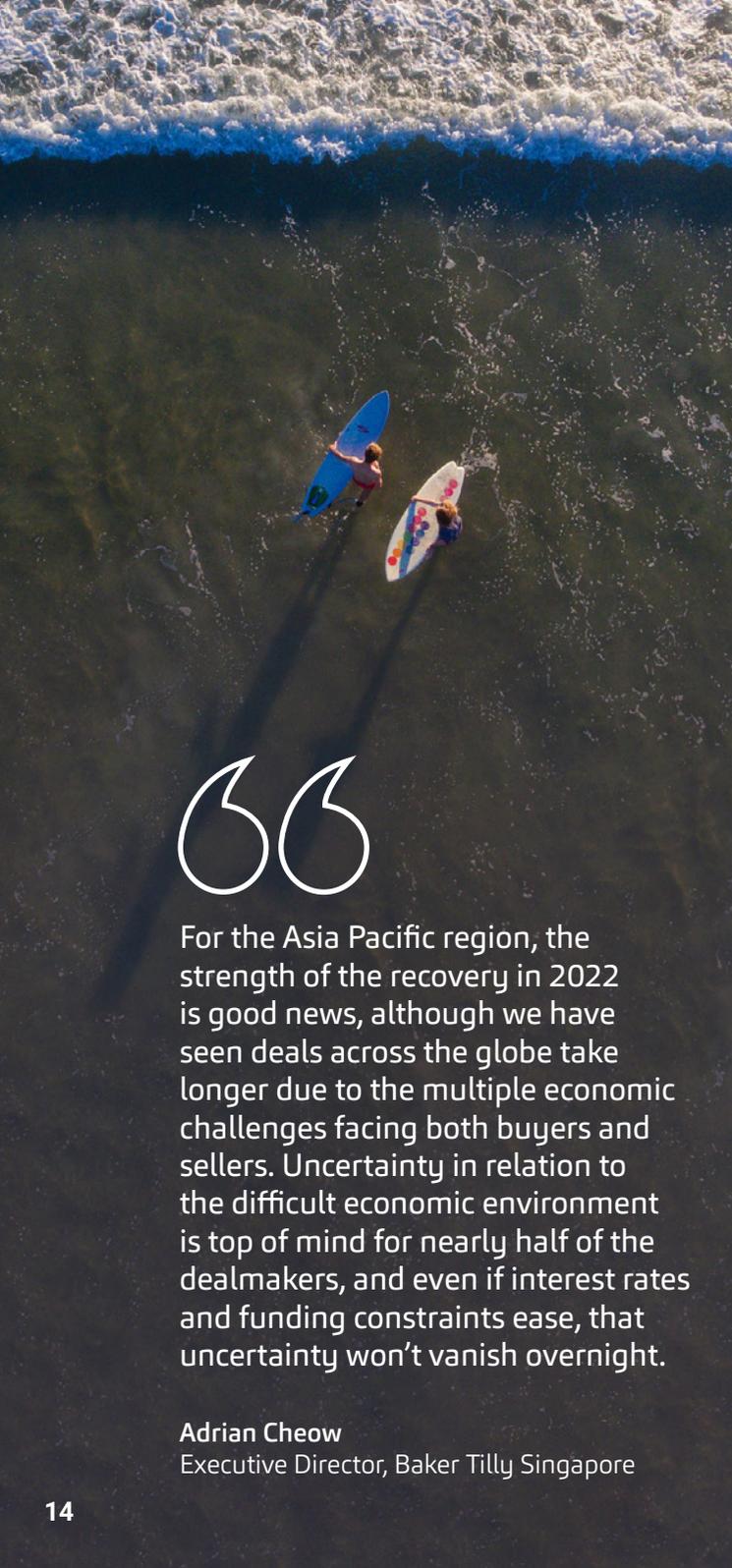


Figure 11. Global mid-market M&A





For the Asia Pacific region, the strength of the recovery in 2022 is good news, although we have seen deals across the globe take longer due to the multiple economic challenges facing both buyers and sellers. Uncertainty in relation to the difficult economic environment is top of mind for nearly half of the dealmakers, and even if interest rates and funding constraints ease, that uncertainty won't vanish overnight.

Adrian Cheow
Executive Director, Baker Tilly Singapore

Regional views: Opportunities in all corners of the globe

Respondent sentiment is positive that M&A in key regions will be robust in 2023 as dealmakers foresee abundant prospects in both advanced and emerging markets.

Asia Pacific: From strength to strength

Dealmaker sentiment is strongest for a major rebound in M&A in Asia Pacific, with 74% saying deals in the region will increase in the year ahead (Figure 12). Just under a third (31%) expect this wave to be at a significant scale.

The outlook for APAC dealmaking has been boosted after China, the dominant market in the region, ended a prolonged period of COVID lockdowns and reopened its economy. This has helped to lift domestic demand and drive growth.

Respondents, however, also see huge potential in India (25%), which ranks among the top 10 markets where dealmakers will be searching for M&A (Figure 13). Southeast Asia is also firmly on the radar for overseas investors, many of which have recognised the long-term growth dynamics in the region.

"Southeast Asia has a positive economic outlook. Even though there are developing economies, they are building a stronger presence in global markets. This has increased their scope," the managing director of a Vietnamese corporate said.

Respondents also see potential in the Australian market. Australia has a sophisticated M&A ecosystem, and its strong mining and energy sector has already generated significant transactional activity during the last year. High-profile deals include BHP Billiton's plans to carve out its petroleum business in a sale to Woodside and a US\$18.4bn bid from Brookfield and MidOcean Energy for energy retailer Origin Energy.

"Investing in Australia would be more comfortable. The reliable infrastructure and positive economic outlook are the main factors driving our decisions to invest here. We also have a ground presence and better experience conducting deals here," a managing director said.

Meanwhile, the rise of the private debt asset class in APAC, although positive in the long term, could slow the flow of deals in the region over the next 12 months. Private debt offers vendors an additional source of funding where M&A would previously have been the only option for companies under financial pressure. As such, close to half (47%) say this financing option will result in decreasing M&A (Figure 14).

"There will be fewer deals due to the rise of private debt offerings. This creates more opportunities for companies to address their cash flow concerns. They can avoid financial distress," a Japanese managing director said.

North America and Europe: Developed markets dominate

While respondents are optimistic that deal activity in emerging markets will surge, most are still focused mainly on investing in developed markets in 2023. More than half of respondents say deals will increase in Europe and North America, with 55% signaling that they will be looking for deal opportunities in the USA, specifically, followed by the UK (45%), Germany (41%), and France (31%).

The survey responses suggest that dealmakers continue leaning toward more established markets, where there are mature deal targets in the relatively advanced healthcare and technology sectors that offer stability in the current period of volatility.

Jumbo tech deals continued to come to market through the year. Microsoft put in a US\$68.7bn bid for gaming developer Activision Blizzard to accelerate its entry into the gaming space, although the transaction has been held up by antitrust regulatory concerns. Elon Musk's US\$44bn purchase of Twitter and Oracle's US\$28.3bn acquisition of health tech company Cerner also boosted deal totals for the year.

Supply chain and logistics resilience also drove deals in North America, with warehouse operator Prologis seeking to build, scale and expand its warehouse estate with a US\$26bn bid for market rival Duke Realty.

In Europe, strong inbound interest sustained activity, with private equity and corporate buyers seeing value in European assets. US-based Thermo Fisher acquired UK diagnostics company The Binding Site in a US\$2.6bn deal. This was one of many UK assets sold to US buyers investing dollars and taking advantage of weak sterling.

Figure 12. What do you think will happen to the level of M&A activity in the following markets in the next 12 months?

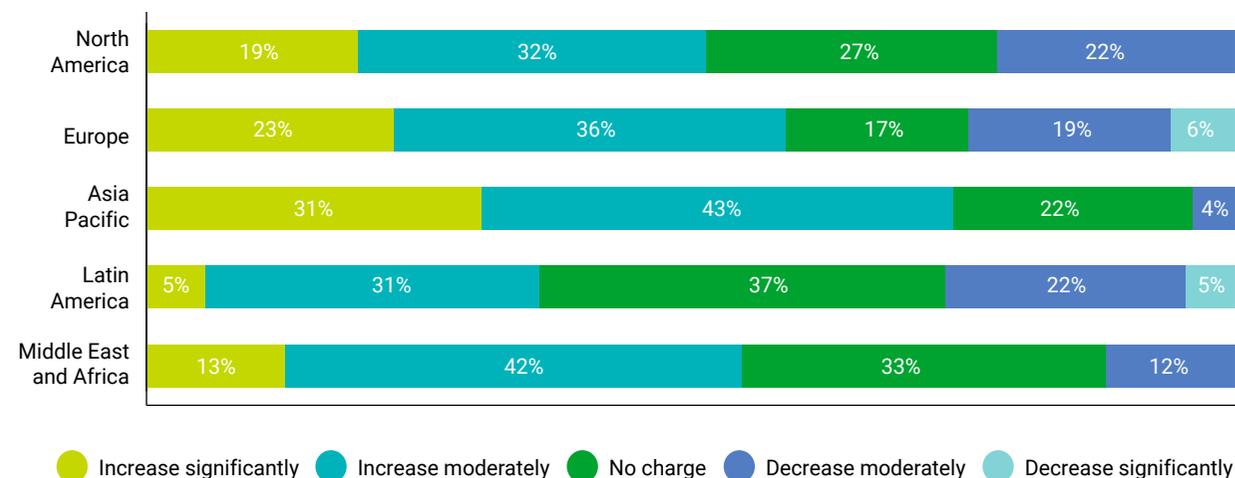
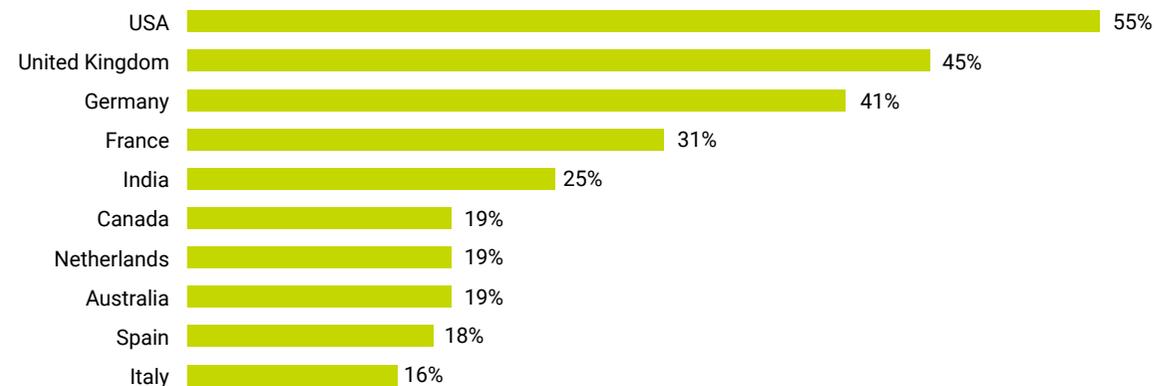


Figure 13. Specifically, in which markets will your company/firm be looking for investment opportunities in the year ahead?



Private equity firms, meanwhile, were drawn to stable European services and infrastructure assets, as observed in Clayton, Dubilier & Rice's acquisition of French-headquartered facilities management group Atalian, and Blackstone and the Benetton family's joint bid for Italian infrastructure group Atlantia.

Although high levels of dry powder indicate that private equity will remain a force in European dealmaking in 2023, respondents are factoring in potential for a dip in private equity activity after a decline in fundraising in 2022. As Figure 14 shows, 68% say this will negatively impact M&A with declines likely to ensue.

In the face of macroeconomic dislocation and declines in portfolio value, investors took pause before making commitments to new funds and sold off existing fund stakes in the secondary market to rebalance portfolios as the denominator effect (when the value of one part of a portfolio declines faster than others) kicked in.

"The slowdown will impact dealmaking activity immensely. Private equity firms have seen promising growth numbers in the past, and only the past year has been challenging for fundraising," a M&A vice president said.

Middle East, Africa and Latin America: Promising horizons

Respondents also see opportunity in the Middle East and Africa, with 55% anticipating a spike in activity. To a lesser but still important extent, 36% say M&A will increase in Latin America.

In recent years, these regions have emerged as some of the most attractive investment destinations for dealmakers looking to gain exposure to developing markets. All three regions are experiencing rapid economic growth, driven by a range of factors including demographic changes, urbanisation, and political and economic reforms.

For instance, with a young and increasingly educated population, these regions are ripe for innovation and entrepreneurship, making them attractive destinations for venture capital and private equity investors. Likewise, a rapidly expanding middle class is driving demand for consumer goods and services, while significant investments in infrastructure are unlocking new opportunities across sectors including energy, agriculture, and manufacturing.

Figure 14. Sentiments regarding private equity fundraising in Europe and private debt markets in APAC

What impact will a slowdown in private equity fundraising (especially in Europe) have on deal activity in the next 12 months?



What impact will the rise of private debt (particularly in APAC) have on deal activity in the next 12 months?



- Deals will decrease significantly
- Deals will decrease moderately
- There will be no change
- Deals will increase moderately
- Deals will increase significantly



Acquisitions in technology are now a recognised path to support digital transformation and obtain a competitive advantage, which can be seen in the ongoing interest in the TMT sector. While the poor performance of a lot of technology giants this year might weigh against some of the mega-deals in this sector, the mid-market understands it needs to leverage technology to broaden business models, improve efficiencies and offer consumers a point of difference.

Xavi Mercadé
CEO, Baker Tilly Spain

Sector watch: Digital transformation and distress drive sweeping changes across industries

Tech: Digital deals

With digital transformation a core priority, the technology, media and telecommunications (TMT) space stands out as the top sector for M&A. In 2022, TMT deal value came in at just over US\$1tn, accounting for close to a third of overall global value. Interest is set to remain steady and strong: close to two-thirds of respondents (61%) say they will focus investments in TMT over the next two years as they use these deals to catalyse change and inject a dose of innovation into business operations (Figure 15).

- **Maintaining a competitive edge:** One key driver of TMT M&A is the rapid pace of technological change. Companies in this sector are constantly looking to acquire new technology or innovative startups to stay ahead of the competition. The increasing importance of digital transformation is also leading companies to expand their offerings and capabilities in areas such as cloud computing, artificial intelligence and cybersecurity. "The TMT industry will see strong growth trends in the future. Specifically, technologies in cloud, AI, analytics, blockchain and robotics are improving the effectiveness of businesses overall," says the managing director of a Vietnamese company.
- **Cross-sector opportunities:** From healthcare to finance to manufacturing, digital transformation is revolutionising the way companies operate. As a result, companies across all industries are investing in digital initiatives to stay ahead of the curve and

achieve long-term success. As the head of M&A at a Chinese company highlights, "Technology caters to a lot of industries. This includes hardware and software companies. Investments will prove to be highly profitable."

- **Mergers and the mid-market:** A number of respondents point out that mergers and consolidations within the TMT space are a developing theme and opportunity area for dealmakers. This is a particularly strong case in the mid-market, where companies may be facing financial pressures but present M&A opportunities at attractive valuations. "Market consolidation [in the mid-market] will be one of our intentions of completing deals in the telecom and media segments," says the head of M&A at an Italian firm.
- **A challenging outlook:** The technology space, however, has not been without its difficulties. The volatile valuations that have hit the sector, as well as the large-scale layoffs at some technology businesses, are set to impact the industry during the next year according to most respondents. Some see these pressures extending even longer (Figure 16). "Investors are withdrawing their support from TMT companies. The cash crunch is causing a lot of volatility in financial markets. I feel that these risks cannot be mitigated very soon," the senior director of strategy and development at a business in Singapore said.



Traditional sectors like real estate and energy continue to have an uncertain outlook. Some commercial real estate investments have been left stranded by the changing nature of work, transport and operations during the COVID-19 years. There's an ongoing need in Europe, particularly to shed older-style buildings that have high-energy requirements. Real estate is expected to bear the brunt of an increase in distressed sales, with construction not far behind. Energy and resources sector companies also face ESG headwinds; however, the opportunity remains strong for those that have been reducing their emissions and improving sustainability performance.

Olivier Willems
Partner, Baker Tilly Belgium

Industrials and chemicals: Manufacturing change

The industrials and manufacturing sector is also tipped to see a surge in M&A. More than half (51%) of respondents say they will focus on dealmaking in this space, with many mentioning the significant changes shaping the industry and creating new opportunities.

- **Adopting advanced technologies:** Automation, robotics and AI are greatly improving efficiency, reducing costs and enhancing productivity among manufacturers. With the increasing demand for customised products and services, these companies are leveraging technologies to enhance their capabilities.
- **ESG:** Increasingly, industrials and manufacturing companies are focusing on sustainability and environmental responsibility. With rising awareness of the negative impact of manufacturing on the environment, companies are investing in green technologies and practices to reduce their carbon footprints, improve energy efficiency and minimise waste.
- **Consolidation and divestitures:** With the increasing competition and pressure to reduce costs, many companies in this sector are pursuing consolidation to achieve economies of scale and enhance their market position. The trend is expected to continue, as companies seek to expand their capabilities and achieve greater efficiencies, particularly in response to rising commodity prices and supply chain bottlenecks. According to the director of strategy at an Italian company, "Although supply chain challenges have impacted the industry in the past couple of years, there are vertical acquisition opportunities pursued by larger companies." Likewise, portfolio optimisation could be a key driver as industrial companies reassess and offload businesses that are non-core or underperforming.

Real estate and energy: Distress on the horizon?

Respondents think real estate (53%) and energy, mining and utilities companies (41%) will experience a certain degree of pain going forward, with both of these capital-intensive sectors feeling the impact of rising interest rates and higher working capital costs.

Even with the COVID-19 pandemic behind it, the real estate industry has struggled to find its footing. The pandemic led to a decrease in demand for commercial and residential properties, resulting in a decline in property values and revenues for real estate companies. As a result, some companies have been forced to restructure their operations or seek bankruptcy protection. The real estate industry is also facing ESG pressures, as building stock has to be refurbished to reduce emissions and energy usage.

For energy and resources companies, many are facing similar cost pressures as they respond to energy transition demands. "Few sectors will be more challenging to invest in. Dealmakers hesitate to invest in companies having lower ESG ratings. Many real estate, energy and construction sector companies have not devised practical ESG strategies," the partner at a Japanese firm said.

Figure 15. Which of the following sectors do you think will be most attractive over the next 12-24 months for general M&A and specifically mid-market transactions?

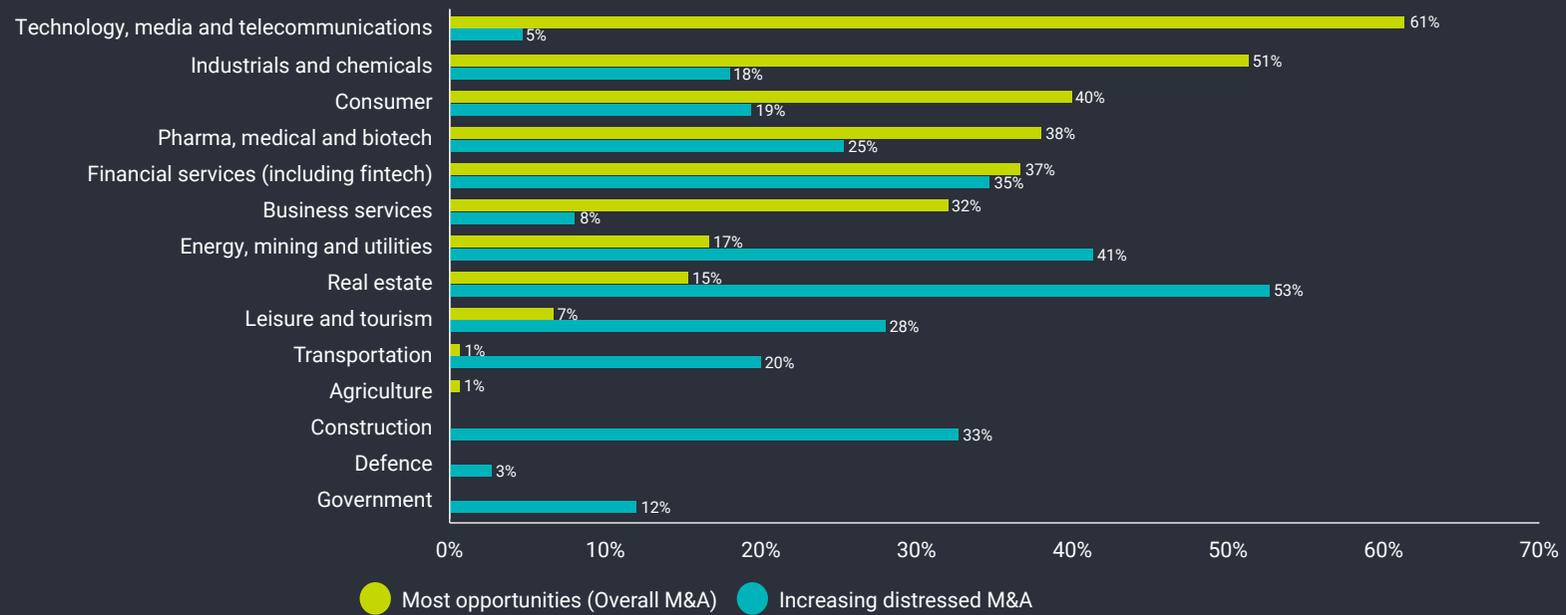
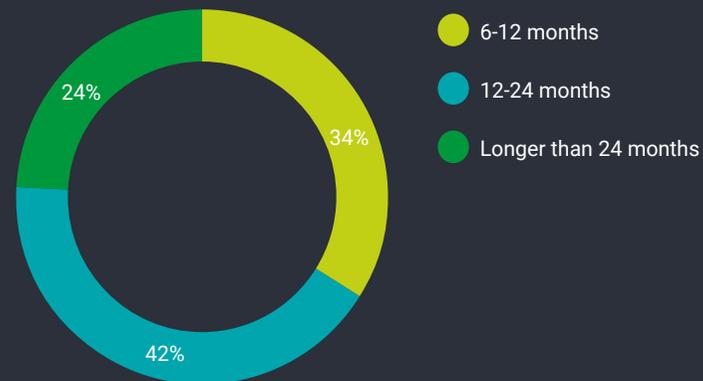


Figure 16. How long do you anticipate current low/volatile valuations and widespread layoffs to impact the TMT sector?





Risks outlook: Macro uncertainties and inflation create challenges in forecasting and due diligence

The M&A outlook in 2023 may be broadly positive after a disruptive 2022, but there is nevertheless a recognition that deal execution will be difficult.

Economic uncertainty

Close to half (49%) of dealmakers say a challenging economic environment will be the top short-term risk – and many foresee conditions worsening as the year progresses (Figure 17). “The economic situation will worsen in the next 12 months. This will affect dealmaking decisions overall. Even if the deal pipeline is strong, it would take a significant amount of time to assess the true potential of deals,” a US investment manager partner said.

Interest rates and inflation

Rising interest rates and inflation have been constant pain points for dealmakers over the past year – and most dealmakers foresee these as key risks into 2023. Primarily, dealmakers have been concerned that these twin challenges have made it difficult to forecast earnings and growth at prospective targets, a concern that was already an issue due to disruption caused by the pandemic.

“Rising inflation does not allow us to gauge the valuation of companies accurately. Whether we decide to buy or sell, there will be valuation gaps that affect the dealmaking negotiations,” a director at a US corporate said.

Over a third of respondents (39%) say rate increases will be the second greatest risk to deals and to a lesser extent, 24% say inflation will be a challenge. All things considered, these numbers could be much higher and perhaps reflect that dealmakers are finally adapting to an environment where both factors could remain volatile for the near term.

Fundraising and deal financing

More than a third (37%) in Figure 17 say raising funds will be a challenge and many more (70%) think financing market conditions will turn negative in 2023 compared to the past two years, with capital markets effectively shuttered as increasingly risk-averse lenders take a more cautious approach to underwriting (Figure 18).

“Companies cannot leverage their assets for additional financing as they usually do. The lender attitude has changed a lot in the past couple of months due to rising insolvencies,” a managing director at a US company said.

Figure 17. What deal challenges/risks do you expect to face in the next 12-24 months?

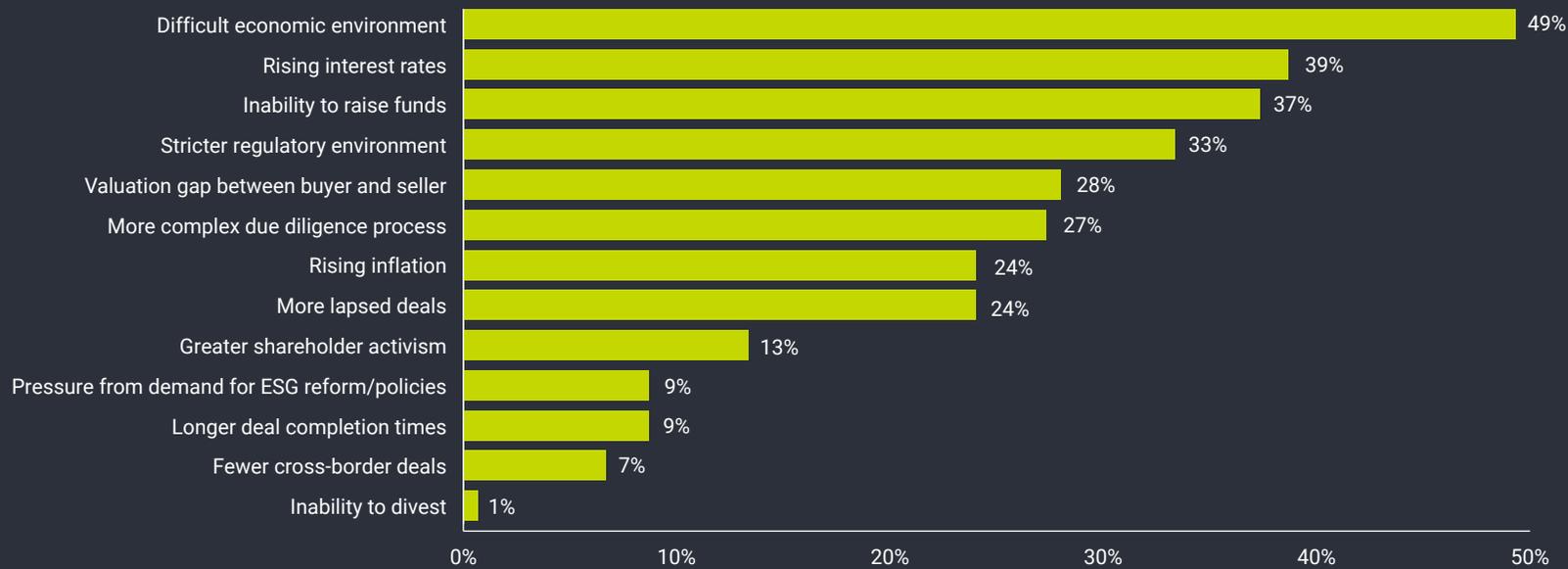
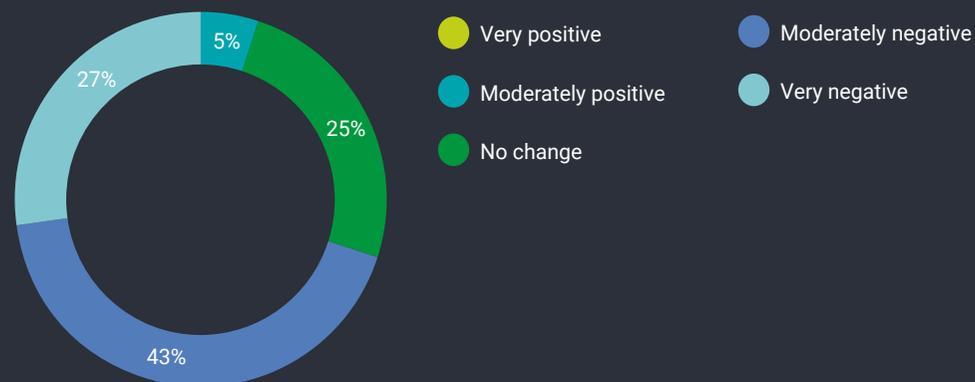


Figure 18. What do you expect financing market conditions to be like in 2023 compared to the past 12-24 months?



Due diligence

The challenging market backdrop has made it more difficult to conduct due diligence. Although only 27% in Figure 17 say due diligence will be their main challenge, most agree (52%) that investigations are more difficult to complete today compared to 12 months ago (Figure 19).

Unpredictable stock markets and choppy company earnings have made it difficult for dealmakers to model valuations against future earnings. This is prolonging due diligence periods and increasing costs.

As a result, 49% say they have added resources to bolster due diligence efforts – and another 21% say they will in the near future (Figure 20). “In the current environment, completing due diligence is significantly more challenging. The financial records are not consistent. Inflation and interest rate risks have affected the value of most businesses,” the director of a US business said.

As dealmakers adjust to the higher demands of diligence projects, more are seeking support from advisors. Only 49% consulted advisors in the past year, but 74% say they will use advisors in future transactions (Figure 21).

“In future deals, we will continue to rely on the advice of consultants. They have expertise about local market cultures, deal feasibility, and risk management ideas that are all helpful,” a US vice president of corporate strategy and development said.

Dealmakers are also moving to harness technology to improve the efficiency of the due diligence process. Data rooms (89%) and video/teleconferencing (87%) will be the top used resources.

Figure 19. How difficult is it to complete due diligence in the current environment compared to 12 months ago?

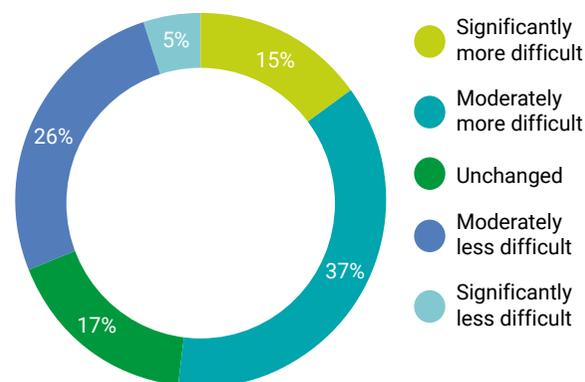


Figure 20. Have you added additional resources to assist with due diligence in the past 12 months?

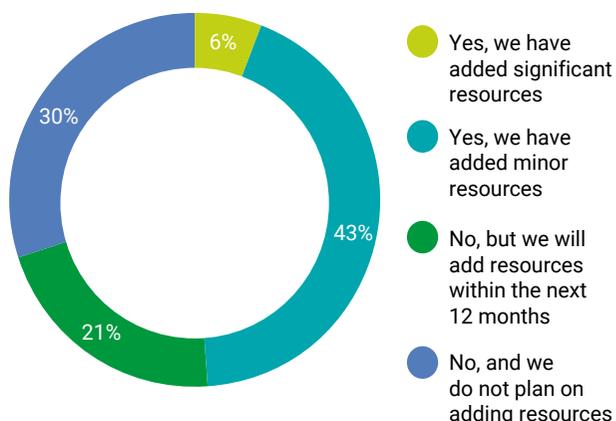
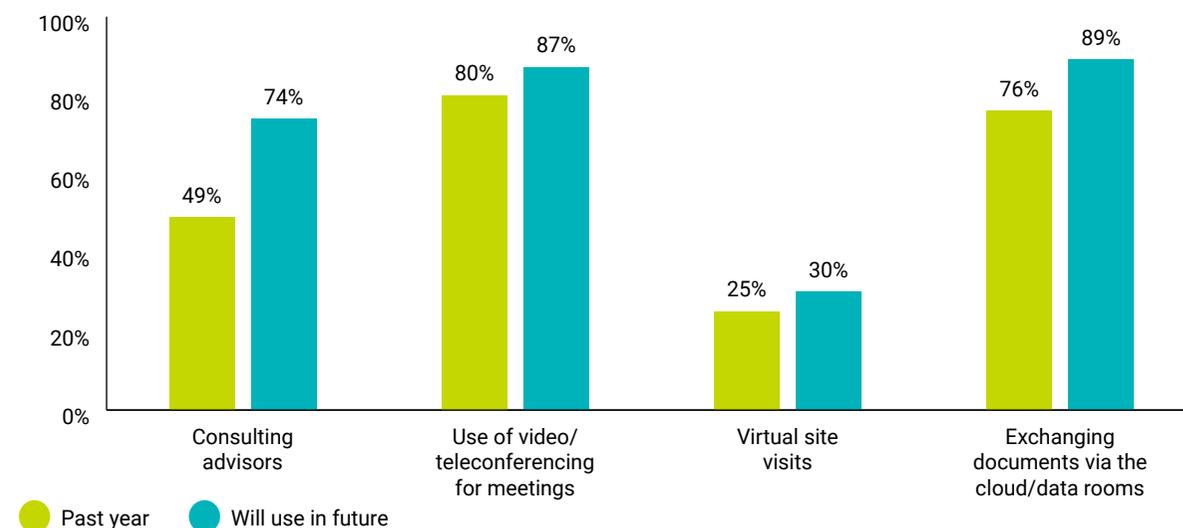
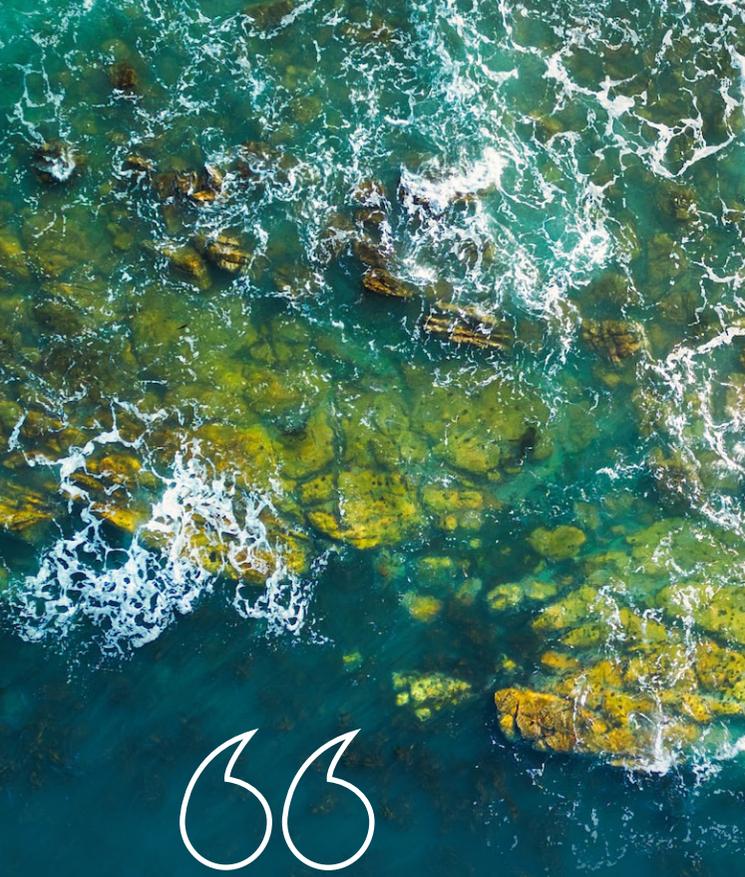


Figure 21. Which of the following did you use as part of your due diligence efforts within the past year? Which will you continue to use in the future? (Select all that apply for each column)





When it comes to ESG, dealmakers seem to have stiffened their spines and are accepting the role of ESG in deals. Although three out of four dealmakers say ESG features in all or most deals, it no longer ranks on top of the list of risks to dealmaking. This suggests sophisticated private equity and M&A teams have learned to anticipate regulation risk, have become better at ESG due diligence and are confident they can manage this area of exposure.

Andrés Magna
Partner, Baker Tilly Chile

Focus: ESG

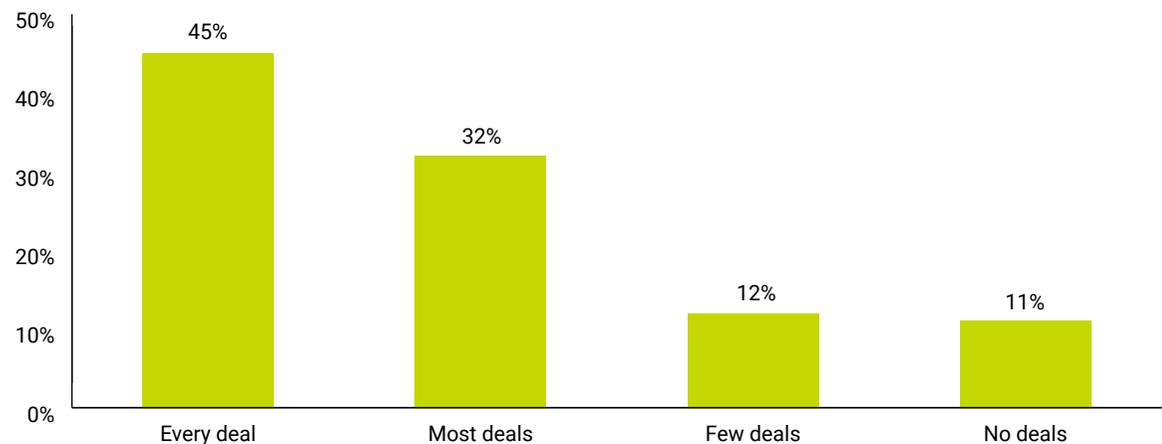
ESG is now a central issue in M&A, as deal parties respond to investor and customer demand to put best ESG practice into place. “The ability to attract finance is dependent on the sustainability potential of companies. Financiers who have high expectations in this regard do not approve funds unless the target’s ESG performance is positive,” a US managing director said.

Almost half (45%) say ESG considerations arise in every deal they’ve done within the past year, and another 32% say it factors into most deals (Figure 22). Only 11% say it’s not an issue.

Indeed, ESG has become so prominent that gaps in ESG compliance and performance can prove to be a deal-breaker. More than half (53%) say they had to turn down an investment due to ESG concerns (Figure 23).

“We turned down an opportunity to invest in a company because it was not consistent in implementing ESG plans. The ESG strategy itself was very weak and impractical. Even further dedication from our teams would not have worked,” the chief financial officer of a French company said.

Figure 22. How often have ESG considerations factored into the dealmaking process regarding your M&A/investments within the past year?



ESG due diligence challenges

Even though respondents signal that ESG is a priority, there are still numerous challenges encountered in the ESG due diligence process. Confusion and a lack of clarity around the standards and benchmarks used to measure ESG performance is a recurring theme, with dealmakers having to navigate myriad standards and kitemarks that are difficult to compare and vary from region to region (Figure 24).

“When we cannot obtain the required information on time, we cannot proceed with reviewing the information. All the further due diligence procedures are delayed, and decision-making is uncertain,” a Canadian director of M&A said.

Integrating information with financial data is also an area that has proven challenging.

“It was a significant challenge trying to integrate information with financial data. There were several specifics missing in the ESG information. ESG risks could not be identified fully,” a vice president of M&A at a US company said.

Figure 23. Within the past 12 months, have you had to turn down an investment due to ESG concerns?

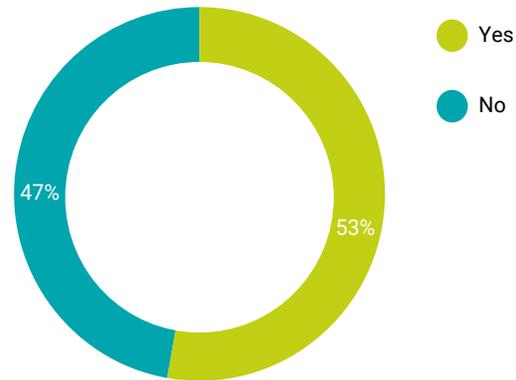
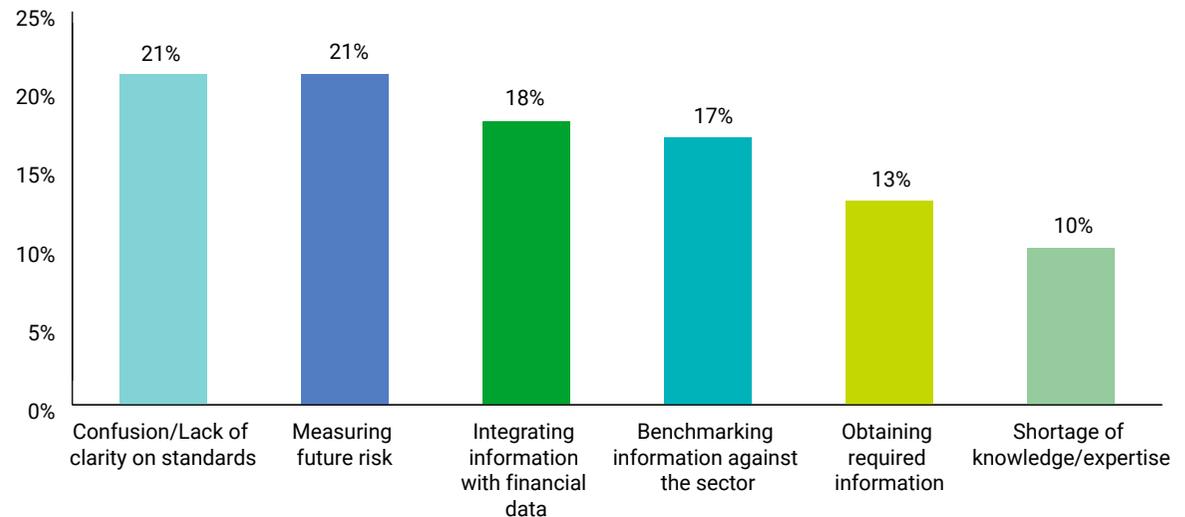


Figure 24. What was the most significant challenge you faced when conducting ESG due diligence in your most recent deal?



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