FOCUS Finance

GLOBAL M&A OUTLOOK

Q2 2020

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Executive Summary

Who we are

Focus Finance is a student-led financial research organization, consisting of more than 25 universities and 70 members from all around the world. We bring together young professionals from top business school, that are bound with a shared vision of redefining student research. We achieve this through our dual commitment to deliver focused professional research reports and insightful real-time financial news coverage alongside building long-lasting connections between our network of analyst, partners, and members.

Our weekly and quarterly sector specific research covers the most important details on global and local trends and events as well as generating original analytics on their implications. We hand select experienced international teams to work together on each project, providing unparalleled opinion differentiation and depth of insight, that creates remarkable research we are truly proud of.

We strive to supply every *Focus Finance* member with the right technical toolkit to excel as a professional through a bespoke analyst training program. This give edge in employability by an unrivalled mentorship opportunity with members, which gained first-hand experienced at top tier firms from all around the world.

Global M&A Outlook Report

Over the past weeks, a group of ten analysts from around the world gathered together to produce *Focus Finance's* first Global M&A Outlook report. Covering the latest macroeconomic and industry trends, the report gives insight to the current conditions of the M&A market in Q2. From the replacement of the NAFTA to the continued tensions between China and India, our analysts put in countless hours of work to assess the impacts of these events in their respective regions.

We at *Focus Finance* are extremely proud of the hard-work our analysts have put into this report and are already looking forward to the next Global M&A Outlook report.

Europe, Middle East & Africa (EMEA)

M&A within the EMEA region has never been unstable as before – key determinants such as Brexit, growing regulatory barriers and the coronavirus pandemic have introduced multiple layers of unease within the M&A industry. From a regional perspective, M&A volume was down 13% across EMEA, and saw a decrease in the number of mega deal transactions.

DACH (Germany, Austria, and Switzerland) played a pivotal role in EMEA M&A deal volume in Q1 2020 as it was accounting for 4 out of the top 10 M&A deals in the region. However, in April, DACH experienced 56% year-on year drop in M&A volume which brings much more uncertainty surrounding Q2 numbers. Total Middle East M&A deal activity rose to $9.3 billion out of 95 deals in Q1 2020, up from nearly $4.0 billion out of the 89 deals in Q4 2019. According to the XBMA Quarterly Report 2020, the Middle East, unlike Europe, only experienced a modest drop off from Q1 M&A activity in Q2.

German, Austria & Switzerland (DACH Region)

Job Protection

Germany has rolled out an extensive furlough scheme called “*Kurzarbeit”* to prevent increased job losses amidst the coronavirus pandemic – a move which proved successful following the 2008-09 financial crisis. Critics argue that the “*Kurzarbeit”* will not be as successful or cost-effective as during the last recession, due to the unprecedented nature and duration of this crisis; at the height of the financial crisis, only 1.5 million workers received furlough payments, compared to 7.3 million in May 2020. German politicians’ commitment to preserving jobs may result in increased scrutiny on cross-border M&A transactions in the DACH region, which aim to achieve cost synergies by reducing employee counts, as regulators remain committed to low unemployment. The increased scrutiny will likely be reflected in depressed M&A levels, as more transactions may be cancelled or postponed due to job security concerns.

Slowdown in Takeovers

The European Union has recently increased efforts to block takeovers by companies which have “received unfair support from a foreign government”, likely diminishing foreign acquisitional demand in the region and depressing M&A activity. Further, the pace of approvals (e.g. compliance with antitrust or foreign investment acts) will be slowed down by government officials working remotely, thereby increasing the time for ongoing transactions to be evaluated. DACH regulators specifically have demonstrated their commitment to blocking takeover attempts, illustrated when German officials blocked U.S. government’s takeover of Curavec. German regulators have remained committed to blocking takeovers, particularly in key industries like healthcare and national defense, while German companies are recovering from the pandemic.

United Kingdom

Political Uncertainty

The political climate in the UK has disrupted M&A activity, yet at the same time has made acquisitions more attractive for oversea buyers. Valuations in the UK have been suppressed as COVID-19 delays Brexit negotiations and postpones the clarity that the market craves. Combined with the depreciation of the pound that was triggered by the uncertainty of Brexit, low valuations may be sufficient to attract inbound M&A. Arguably, it was found that more than half of dealmakers are less likely to invest in the UK due to the uncertainty Brexit has caused, especially against the volatile exchange rates and equity markets. On the 21st of June 2020, the UK Government also announced it will introduce the emergency legislation to block foreign takeovers and safeguard national interests, namely national security and financial stability. Therefore, despite the opportunities for overseas buyers, M&A deals within the UK will likely grow at a slow rate.

COVID-19 Outbreak

Despite the coronavirus' undoubtable impact, cross-border deal volume is expected to be high; over half of UK respondents in EY's latest survey said they expect to transact in the next 12 months. That being said, half of such respondents have annual revenues of $3.0 billion and higher and are likely to have the balance sheet strength to consolidate and make transformative deals in the year ahead. This may not be the same for struggling UK businesses – given that other economies like China are recovering quicker than the UK, we may see cash-rich oversea buyers acquiring struggling UK businesses with weak balance sheets. These cross-border transactions, however, will grow at a slow rate as acquirers are held back by strict border restrictions and formidable due diligence uncertainty. It is expected that there will be an increased focus on warranties, limitations/caps, and force majeure clauses within M&A transactions.

Sectors that will be less challenged post COVID include technology, online retail and healthcare as opposed to the more challenged sectors such as food and beverage, real estate, construction, hospitality, and leisure. Within the UK F&B sector, deal volume is down 40% year-on-year, while the deal value is down a staggering 90% as travel restrictions and lockdown inhibit growth.

Middle East

Falling Oil Prices

The Middle East (ME), renowned for their energy sector, is predicted to see a sharp drop in investments between 2020 to 2024. The region will see a $173m decline between 2020 to 2024 if Brent prices remain at its 20-year lows, within the $30-$50-barrel range. Given these constraints, oil and gas M&A deals will likely be thin on the ground in the coming months ahead as the market remains bearish. Prior to that, energy and power sector transactions were the main driving force for M&A in the ME region, accounting for 78% of the total value of deals last year. Unfortunately, analysts at Citigroup do not see fuel consumption back at last year's level until well in 2022. After months of successful teleconferencing with the existence of Zoom and other online systems, business trips that once kept planes at full capacity may also come under scrutiny. Key to improving M&A activity in ME are for oil-producing companies to potentially diversify their portfolio by investing in downstream businesses such as refining and petrochemicals whilst building beneficial long-term oil supply deals.

Vision 2030

Recently, Saudia Arabia introduced the Vision 2030 agenda to reduce the nation's dependence on oil, diversify its economy and develop public service sectors such as health, education, recreation and tourism. Healthcare and education have been important drivers of ME deal volume in recent years; in healthcare, market players have focused on building up their scale through joint ventures and acquisitions. An increasingly lucrative market in medical tourism has also been a driving move for specialized facilities such as IVF clinics and long-term care centers. As such, it is likely we will see growth within the sector. In the education industry, private equity backed commercial operators are looking to expand portfolios outside of the saturated UAE education market which was once growing up to 11% in previous years but is now at 3.5%. Egypt and Saudi Arabia have been deemed as promising candidates for expansion given that 60% of its student population now attend private schools and the nations are relaxing foreign ownership requirements.

Final Remarks

As a result of the environmental events, there are two possible scenarios for the M&A industry - the first is a further slowdown in the M&A volumes in the next two or possibly three quarters, reflecting global uncertainty, investors' anxiety and shift of priorities as companies undergo restructuring. The second is that growth will continue, yet at a much slower pace as companies are interested in joining forces to mitigate losses, and lower valuation makes acquisition more attractive to buyers.

North & Latin America

As the COVID-19 pandemic continues into the second quarter of 2020, countries in North and Latin America are taking action to combat the adverse economic effects of the disease. Many people are restricted from travelling in an effort to slow the spread of the disease, which has negatively impacted business' operations. New fiscal and monetary policies have been enacted in an attempt to counteract the economic decline, but numerous businesses still face bankruptcy regardless. The pandemic has also caused a reduction in M&A activity.

North America has seen a 3% decrease in M&A volume, with total transactions valued at $466 billion in Q2, compared to $452 billion the same time last year. Q2 deal volume for the U.S. saw a small decrease compared to the rest of the world due to several large M&A deals with transaction values over $10 billion. Latin America saw a more severe decrease, with at least a 30% to 40% decrease in M&A volume in Q2 2020, and a 77% decrease in deal value for the first half of 2020 compared to the same time last year. In the first six months, M&A volume in Latin America saw 199 deals with a total transaction value of $8.1 billion, this is down from 316 deals with a total transaction value of $35 billion in the same six month period last year.

United States of America

Travel Bans and Shelter-In-Place

The implementation of travel bans, and shelter-in-place orders has had widespread effects on daily operations and has led to numerous practical problems for companies. A myriad of M&A negotiations is slowing down or halting due to decision-makers' inability to travel and obtain important original documents in a timely manner. This coupled with the shelter-in-place mandates that have forced government officials and civil servants to work remotely, has the potential to slow the regulatory and antitrust review process. As the negotiation process drags on, so do the associated costs, increasing the likelihood of a transaction's failure.

Beyond the effects on active mergers or acquisitions, these orders are also setting the stage for a plethora of mergers and acquisitions in the future. The orders are primarily impacting the business of companies that rely on their in-person consumers for revenue. Numerous retailers are facing issues as they are forced to rely on their online offerings for revenue. These orders may force companies into bankruptcy, paving the way for future acquisitions or mergers.

Bankruptcies Increased

During the COVID-19 pandemic, bankruptcy filings have significantly increased, averaging 600 Chapter 11 filings in the U.S. per month since January, which is up 31% compared to the average Chapter 11 filings per month in 2019. This can largely be attributed to disrupted supply chains, and a decrease in consumer spending. Several well-known large companies, like Hertz and J Crew, have filed for bankruptcy citing issues with over leveraging and a decrease in incoming cash flow due to the pandemic. These bankruptcies will cause a ripple effect for businesses and creditors. The recent filings will congest bankruptcy courts and since many of these companies have large debt balances, their creditors will have a difficult time recovering their investments or expected payments. On the brighter side, the increase in bankruptcies will open opportunities for companies with larger cash balances to acquire bankrupt firms at a discount. However it should not be expected that this will significantly increase M&A activity, as it is unlikely that large companies will look to acquire over-leveraged businesses and agree to take on a large increase in debt considering many firms are in survival mode due to the COVID-19 pandemic.

US Fiscal & Monetary Policy

Following the outbreak of the COVID-19 pandemic, the Federal Reserve and U.S. government have been forced to take unprecedented actions in order to stabilize market turmoil and support short term economic activity. The first move made by the FOMC came back in March when the federal funds rate was cut from a range of 1.50% to 1.75% percent to a range of 0% to 0.25%. Chairman Jerome Powell has stated that rates will remain at this target range until the economy is on track to achieve its maximum-employment and price-stability goals despite President Trump calling for a move to negative interest rates. In theory, the move to 0 or lower interest rates could encourage more M&A activity post-COVID as companies look to spend their larger cash balances, however this increase likely wouldn't be seen until economic conditions begin to increase, meaning it will have little effect on M&A transactions in the next one or two quarters. However, in practice, a move to negative interest rates, while unlikely, could signal low economic growth and future uncertainty causing companies to choose either to hold on to their cash or spend it on foreign deal activity. In 2015 when Japan moved to negative rates, Japanese companies were involved in $90.1 billion worth of cross-border mergers and acquisitions, more than doubling the value from the year prior.

Additionally, the FOMC has undertaken asset purchases in the form of quantitative easing and credit extensions to various economic sectors to support businesses. In June, the FOMC committed to purchasing $80 billion per month in Treasuries and $40 billion in mortgage-backed securities until further notice. These programs from the Fed, as well as over $3 trillion in Congressionally authorized coronavirus relief, have created speculation regarding a shift from a deflationary environment to one of long-term inflation. This could significantly reduce future M&A transaction volumes; such was the case throughout the 1970's when annual M&A volumes in the U.S. dropped from 5,152 transactions in 1970 to only 2,128 annual deals in 1979. However, such effects likely would not be seen for some time.

Canada & Mexico

Replacement of NAFTA

A modernized proposal for the North American Free Trade Agreement (NAFTA) entitled the United States-Mexico-Canada Agreement (USMCA) was recently ratified in March and was placed into effect as of June 1st. Specifically targeting the auto industry, the USMCA includes several new provisions targeted towards reducing the outsourcing of manufacturing jobs from the US. This coupled with the strengthening of labor laws incentivizes a return to US manufacturing. The agreement's manufacturing provisions coupled with rising tariffs on goods and materials from China could potentially lead companies to reorganize their supply chain with a focus on proximity. This presents an opportunity for vertical mergers as companies seek to lower their manufacturing costs.

Additionally, a provision was removed from the trade deal that would have required all three countries to provide at least 10 years of exclusivity for biologics. As of this report, there are no exclusivity requirements in place in Mexico outside of the current exclusivity period enforced by NAFTA. Thus, the replacement of NAFTA could potentially lead to a dissolution of Mexico's exclusivity period. Companies typically rely on their products' market exclusivity period to cover their R&D costs, and an absence of this period would create liquidity issues for many companies. These failing companies may subsequently be bought by competitors at a bargain.

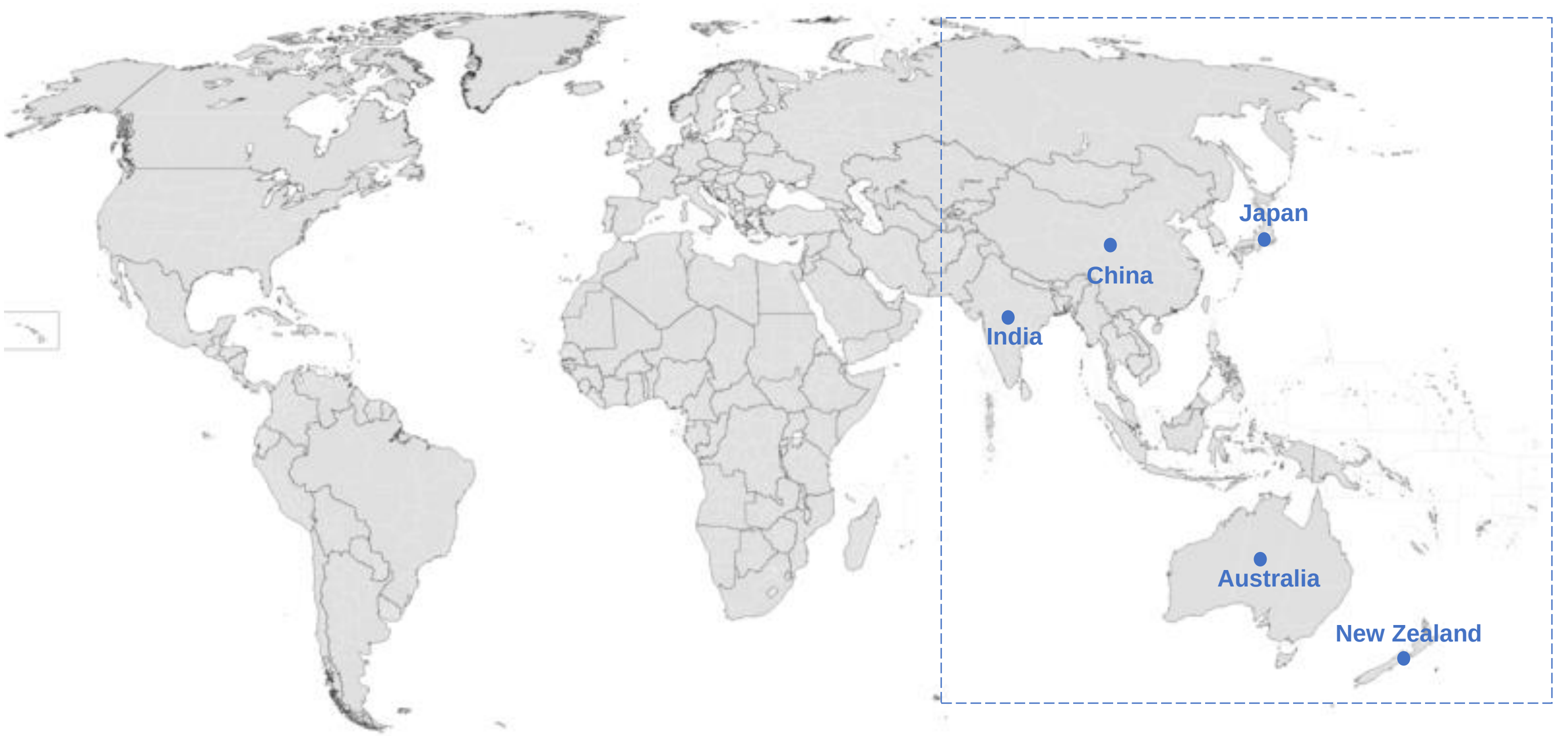
Brazil

COVID-19

Similarly, to North America, M&A activity throughout Latin American countries has reduced dramatically because of the coronavirus pandemic. With the number of deals and total transaction values falling to record lows, the situation in Latin America may be even more bleak than that of North America. Latin America was one of the last global regions to be struck by COVID-19 with the first recorded case not coming until February in Brazil. As a result of the late arrival as well as a failure of countries within the region to properly enforce lockdowns and other safety protocols early on, the region continues to experience rising case numbers. Brazil has been hit especially hard as it is now the world's second most infected country after the U.S. with 800,000 cases and 40,000 deaths. The result has been destroyed economic activity throughout the region and record low deal volumes, which will likely take longer to recover from than other more developed regions.

Final Remarks

Given the current economic environment throughout North and Latin America, it is unlikely that M&A activity will return to pre-COVID levels in the near future. Instead, most companies will look to utilize their built-up cash reserves, and possibly take on more leveraged positions, to preserve financial stability. However, given the increase in recent bankruptcy filings, certain companies with large cash balances may look to take advantage of the situation by acquiring newly bankrupt companies for discounted prices. Deal volumes over the next 2 to 3 quarters will depend on how quickly countries are capable of reopening certain industries whereas current geopolitical agreements and fiscal policies may have long-term repercussions.



Asia Pacific

Australia has entered its first recession in 29 years having borne the devastating effects of the bush fires and COVID-19 in Q1 2020. GDP contracted by 0.3% in Q1 2020, with the June quarter expected to be even worse. The Reserve Bank of Australia has implemented quantitative easing for the first time, targeting the shorter end of the yield curve, which has seen the RBA's balance sheet expand by ~59% from 1st January to 1st July. The cash rate target has also remained at 0.25%.

In Japan, March saw a 3.4% seasonally adjusted real GDP contraction, and the Cabinet Office is forecasting a contraction of 21.5% in the second quarter of 2020. Japan's fiscal stimulus packages in the face of COVID-19 total US$2.18 tn, ~40% of GDP. To help finance this, government debt issuance will rise to 212 tn Yen in FY20 (US$2 tn). Japan's debt dependency will rise to a record 56.3% following this.

India's macroeconomic outlook is bleak even after lockdowns are starting to lift, with the IMF predicting a 4.5% contraction from 2QCY2020 to 2QCY2021. Tax revenues are set to crash, and India's debt-to-GDP ratio may jump to 90%. Since March 2020, demand from urban and rural parts of the economy have collapsed, with investment activity and private consumption suffering declines. India's imports fell 60% (YoY) in April, with the Central Bank's inflation outlook remaining highly uncertain. Hence, in May 2020, India's cash rate (repo rate) was reduced by 40 bp from 4.4% to 4%. The Insolvency and Bankruptcy Code, introduced in 2016, gave rise to many distressed M&A transactions since inception, and it is expected to continue driving M&A in the future, especially after its 6-month moratorium ending late September.

Australia & New Zealand

Pressure on the Banking sector

The past year has seen Australia's financial sector, in particular the 'Big 4' consumer banks, rocked by several scandals, first starting from the Hayne Royal Commission in December 2017. Recent RBA rate cuts have further eaten into the banks' margins, while provisions for bad debt have risen in lieu of COVID-19. Financial regulators have also urged banks to use their capital buffers as the sector deals with $236 bn of deferred loans, which will be even more vulnerable when the scheduled Government stimulus ends in September. We have seen banks divesting from other ventures to 'put banking first' - exemplified by Westpac's sale of its remaining 9.5% share in investment manager Pendal and CBA's sale of 55% of Colonial First State to KKR for A$1.7 bn subject to regulatory approval.

Foreign Investment Review Board Changes

If passed, new changes to the FIRB will see the threshold for foreign investments in sensitive national security businesses lowered to $0 as of 1st January 2021. This will effectively require the FIRB to approve any foreign investment case-by-case and provide the Treasurer with a range of new powers to unwind transactions. This comes on the back of the rhetoric to protect the 'national interest', especially from foreign investors exploiting the low AUD. All monetary screening thresholds have been temporarily lowered to $0 as of 19th March as a response to coronavirus. This will make it harder to convince foreign buyers to participate in Australian deals - a potential drag on M&A activity given only 20% of Australian M&A, by value came from domestic bidders in FY19.

Australian-China Tensions

The past quarter has seen a significant escalation in Australia's tensions with its primary trade partner. Australia's recent calls for an enquiry into China's handling of COVID-19; disagreements over Hong-Kong; and points of the Belt and Road Initiative have triggered economic and political backlash. China has imposed 80.5% tariffs on Australian barley exports, with threats of tariffs on Australian coal and the discouragement of international students from studying in Australia. Investor confidence in the real estate and resources sector will be weakened due to their sensitivity to Chinese demand; the mining sector saw a 20% drop in M&A activity in Q2 following global demand disruptions and escalating tensions.

India

Insolvency and Bankruptcy Code

The Insolvency and Bankruptcy Code (IBC) introduced in 2016, created a single law for insolvency and bankruptcy. The Code was essential as the insolvency resolution process took 4.3 years on average in India in 2015, compared to 1 year in the UK and 1.5 years in the US. The Code gave rise to many distressed M&A transactions, with the industrial sector being the most successful in resolution - Essar Steel's $5.7b acquisition of Essar Steel being the largest and most notable distressed M&A transaction. A recent amendment imposed a moratorium on insolvency applications for a period of 6 months starting March 25th, 2020. This is critical to protect corporations experiencing COVID-related distress from being pushed into insolvency proceedings under the IBC. Following this period, given some of the permanent distress caused by COVID-19, it is expected that the number of IBC-related M&A transactions should increase.

India-China Tensions

Early in the second quarter, India amended its foreign direct investment policies in anticipation of possible predatory behavior from international bidders. The rules prevent opportunistic takeovers by Chinese companies, reducing any prospects of inter-country M&A between the nations. Tensions between the nations escalated when 20 Indian soldiers died fighting at a border site, which led to the majority of Indian population adopting a nationalistic mindset. "Boycott China" is a sentiment shared by the Indian population, however, China supplies 70% of India's drug intermediates and India's smartphone sector heavily relies on cheap phones made by Chinese companies such as Oppo, Xiaomi. Hence, boycotting products or services where there are alternatives available might be more effective. As such, India recently banned 59 Chinese apps, including the popular messaging chat WeChat and video-sharing app TikTok.

Government mismanagement

Given that investment has been shrinking over the last few years, the government has been trying to increase spending to fuel economic growth, with spending rising by 12% since last year, leading to a fiscal deficit in 2019 that was 4.6% higher than the deficit six years ago. This deficit, as well as the recent policy measures have been praised as having "increased economic activity", however, the government has used their crucial tool - spending. Hence, they have few tools left for the near future and economic recovery is likely to take over two years rather than a few months. This is likely to reduce domestic M&A activity in the short-term, especially given that IBC-related M&A is also on hold for six months.

China

Tensions on the Rise

2020 has welcomed fresh tensions between China and a large proportion of the Western world, most importantly the U.S., as it faces pressure regarding an independent query into the origins of the coronavirus. China's response to Australia's query, in particular, was to impose 80.5% tariffs on Australian barley exports, with threats of tariffs on Australian coal and the discouragement of international students from studying in Australia. In particular, China has been subject to President Trump's demand that they pay for the outbreak, and a large amount of doubt is cast over the future of the first phase of the historic trade deal between the two nations. In particular, federal funds from the U.S. are blocked from entering China's markets and has effectively shut off China's capital markets to U.S. investors.

Hong Kong Security Law

Furthermore, the last three months have seen the imposition of China's new security law, which aims to crack-down on pro-democracy protests in Hong Kong. So far, over 400 protestors have been arrested. The Hang Seng Index remains volatile, and there remain questions over the robustness of the peg between HKD and USD. Such uncertainty over Hong Kong has inevitably caused business and consumer confidence to new lows, dampening M&A activity throughout the region where many of the world's investment banks operate.

China's Manufacturing Sector Under Threat

The fate of China's economy as it battles with the long-term impacts of the Coronavirus is of crucial importance to almost all countries. It will have a significant effect on M&A activity going forward. Indeed, the shut-down of a substantial proportion of Chinese factories during the pandemic welcomed depressed figures surrounding its manufacturing and service sectors, validating informal indications that the country will struggle to return to work. Nonetheless, as domestic cases fall, and China's economy slowly opens up, there remains optimism thanks to China's brutal efficiency and its ability to regain growth momentum over the last month. Industrial production and services output, China's main focus in persevering through the crisis, has resumed growth and economists believe the economy will narrowly avoid a technical recession, with GDP expected to expand at least 1.5% in the second quarter relative to 2019Q1 levels.

Japan

Olympic Postponement

On March 24th, the Tokyo 2020 Olympic and Paralympic Games were postponed. Estimates place the effect of the postponement at close to US$ 6 bn. If the games are cancelled, it will cost Japan US$ 42 bn. This has significant impacts on various venues that are forced to cancel any events they had planned for 2021 to host the Olympics; broadcasting companies globally; and the tourism sector. Domestic consumption is set to suffer from the postponement as well as the insurance sector. This is expected to further slow M&A in the insurance sector, as companies weigh the impact of COVID-19 and the postponement of the Olympics on insurers' bottom line.

Final Remarks

Around Asia-Pacific, political tensions are contributing further uncertainty to already volatile markets. Q3 should hopefully see more growth and M&A activity than in the first two quarters of the year - though this is subject to the amelioration of COVID-19. Another trend that appears to be prevalent across the region is the consolidation of industries and divestments as industries suffer for various reasons. Political tensions, embodied in various investment policy changes, will add further headwinds to cross-border M&A flow, in addition to COVID-19.

Q2 2020 - Industry Analysis

At a Glance

EMEA:
- Healthcare
- Technology, Media, Telecommunications
- Aerospace

North & Latin America:
- Oil & Gas
- Healthcare
- Automotive
- Technology, Media, Telecommunications

Asia Pacific
- Natural Resources
- Healthcare
- Financials

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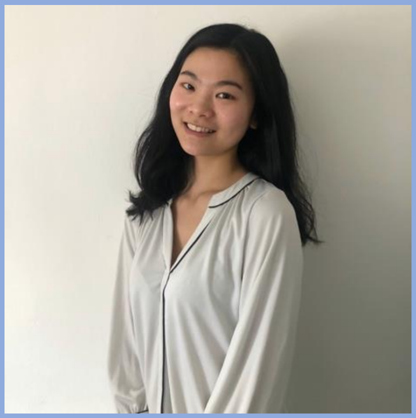

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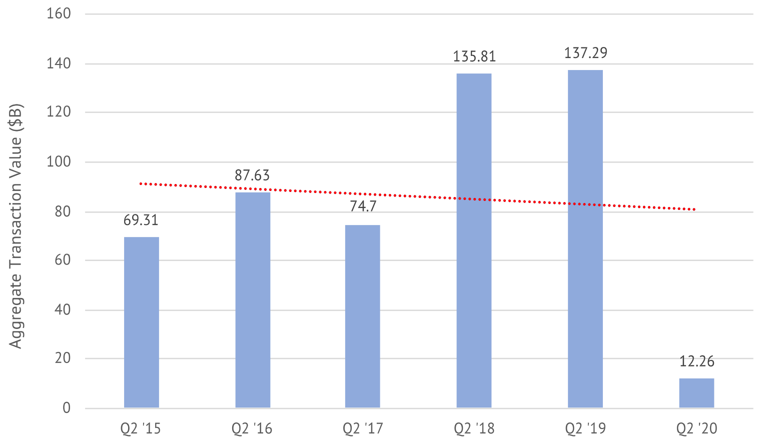
Healthcare Industry

Healthcare M&A activity in EMEA will be slowed down drastically by government hesitance to approve inbound cross-border transactions. Currently in the European Union, legislation provides governments with the right to examine deals to protect national security interests if a buyer attempts to control more than 25% of the shares of a healthcare company. Recent legislation lowered this threshold to 10%. Due to increased regulatory scrutiny, the trend of decreased healthcare M&A's foreign acquisitional demand will likely continue. The reason behind the slowdown may not necessarily only be more deals being rejected by governments. Each transaction will include a longer regulatory approval process, which will slow the rate at which deals are finalized and agreed.

1.1 – Slowdown of M&A Activity

Regulatory behavior to stop deals has already been demonstrated in Q2 in Germany. German cabinet members prevented the acquisition of Curavec, a German biotech firm working on a COVID-19 vaccine, from a U.S. buyer. This pattern of regulatory intervention will likely continue to exert downward pressure on M&A activity, particularly in important national security relevant industries like healthcare.

Figure 1.1 – Global Healthcare M&A Deals in Q2 since 2015



While regulations played a moderate role in depressed M&A activity this quarter, the slowdown can be largely attributed to the coronavirus pandemic. In Q2 2020, global healthcare M&A volume dropped 19% to 327 transactions, compared with the previous quarter's 404 announced deals. The most negatively hit sectors were the Behavioral Health Care, Home Health and Hospice. This is because hospitals experienced major distress and restructuring as elective surgeries were put on hold to deal with the critically ill COVID-19 patients.

1.2 – Major Industry Deals

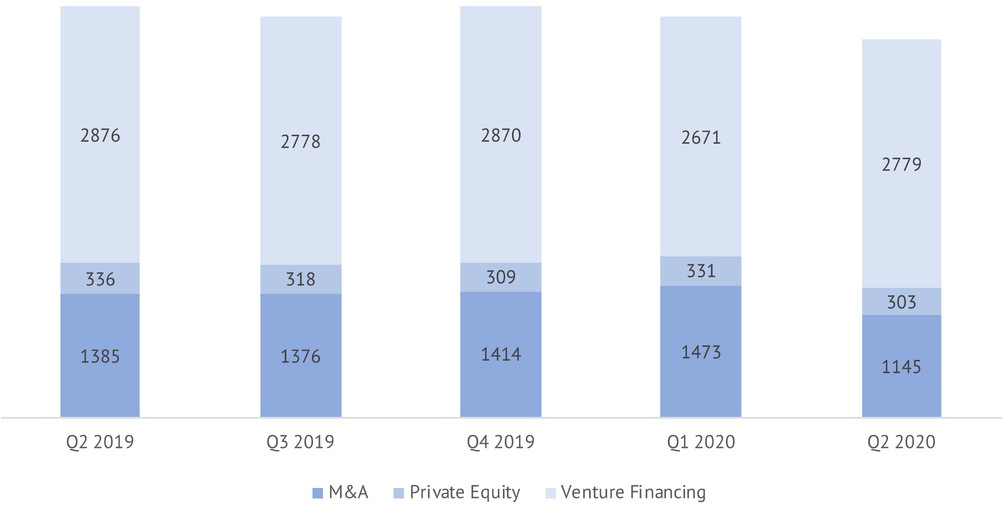
Even though there may be a dip in M&A in the short term, health executives are expecting a resurgence of appetite down the road. In fact, according to MergerMarket, UAE-based Foundation Holdings is planning to buy a 50% stake in healthcare and education companies within the Gulf Region. If struck, the deal size could head towards the USD 40M range. Additionally, Danish pharmaceutical giant Novo Nordisk A/S has recently acquired Corvidia Therapeutics Inc. for a total consideration of up to USD 2.1B. The acquisition will add zilitivekimab, an experimental treatment for certain patients with kidney diseases who are at risk of major adverse cardiovascular events, to Novo's pipeline. As such, reasonable advice for companies within the industry would be to diversify their portfolio for a post-pandemic environment and reinvest.

The reward that healthcare companies would enjoy by finding a COVID-19 vaccine would be like winning the lottery, and there has been a heavy M&A focus in EMEA on firms with exciting prospects. Most notably, British-Swedish pharma firm Astrazeneca announced a partnership with the University of Oxford "for the global development and distribution" of a coronavirus vaccine. There may be a surge in M&A activity within healthcare aimed at distributing a working vaccine. Matching firms with strong research and development with pharma companies that can produce on scale will become increasingly important in the race for a COVID-19 cure, as the demand for a vaccine is massive. There may also be a surge in joint partnerships between research institutions and pharma companies, similar to Astrazeneca and Oxford's relationship, as a potential alternative to M&A.

Technology, Media & Communication

Despite the recent deterioration of global and sector economic confidence, technology executives have been rather optimistic about the speed of recovery for the TMT industry with 63% expecting a V-shaped recovery, compared with the 38% of non-tech respondents.

Figure 1.2 – UK M&A TMT: Volume Trend (in $ Bn.)



2.1 – Current Deal Landscape

EMEA Telecom M&A is expected to get a boost by the new EU ruling. In 2016, the European Commission blocked the planned merger of mobile network operators Three and O2 in the UK. However, recently, CK Hutchison Holdings Ltd. won its European Union court fight to overturn the rule, making it easier to get deals past the merger of watch dogs. It is likely there will be more M&A activity within the telecom industry due to the relaxed regulations. In Q2, O2 agreed to merge with Virgin Media in a deal worth an estimated USD 38.8B. The transaction will create the UK's largest phone and internet operator.

Spain's Telefonica is also currently in talks with Liberty Global over a possible merger of their U.K operations in a deal that would create a new television and mobile company. Collectively, the two companies are valued at £28B including debt and anticipated synergies. The deal will radically reshape the UK's telecoms industry, creating a competitor to the country's current top operator BT Group. British telecoms operator Vodafone has also been engaging in numerous cross-border M&A activities; in March 2020, they acquired 100% holdings of Monaco Telecom for EUR 242M and in Jan 2020, Vodafone signed with Saudi Telecom to pursue a 55% holding for EU 2.2B. As mentioned in their Q2 report, Vodafone are looking to reduce their cost base through the deployment of technology. Therefore, recent activity has exhibited the resilience of the telecommunications industry and increasing buyers' appetite amidst the pandemic.

While total deal volume decreased over Q1 2020 and Q2 of last year, the total deal value was high largely due to massive M&A deals like O2-Virgin Media. There was a moderate decrease in the number of transactions which reflects less momentum behind increased deal values. M&A levels may come under pressure from the lack of deal activity if bigger telecoms companies slow down their M&A levels. Moreover, heightened cyber-attacks and a 66% increase in GDPR data breach notifications across the European markets (Belgium, France, and Germany) may also inhibit the growth of telecoms M&A through 2020.

2.2 – Middle East Tech Growth

Middle East deal activity within the TMT industry remained stable in Q2, backed by 27 deals worth a total $2.5B. The number of tech deals constituted 21.7% of the total deal amount for the Middle East, rising from 17.6% during Q2 2019. What is notable about this is that coronavirus seems to have modestly sped up activity in the high-tech industry, which aligns with M&A trends in the U.S. The growth in deal value in the Middle East was not backed by one or two mega-deals, rather, by increasing deal volume. This suggests a positive outlook for the rest of 2020 in terms of deal activity for the region, compared to their European and African counterparts.

Smaller TMT companies were less likely to have immediate cash needs compared to firms in other sections, resulting in a lack of eager sellers in M&A. TMT firms have been more resilient to or even benefited from the pandemics. On the 23rd of June 2020, co-chairman of Global M&A for Goldman Sachs Tim Ingrassia described the impact of COVID-19 on companies' M&A strategies, which partly explains depressed TMT M&A activity in Q2. Ingrassia characterized the current deal making environment as a buyer's market. He highlighted that cash-ready acquirers were opportunistically looking for deals while smaller firms were reluctant to sell at lower relative valuation levels.

2.3 – Rise in Sell-side Deals

Within sectors like energy, which were massively affected by the pandemic, numerous deals have been fueled on the seller-side by the financing needs of targets. For example, smaller energy companies who experienced overnight shocks in both commodity prices and volume demanded faced massive liquidity shortages they had to resolve to avoid bankruptcy. For the most part, smaller TMT companies were far more resilient through the pandemic and were less desperate compared to other sectors to sell at low valuations. As the stock market has rebounded sharply and valuations of some tech companies have even begun to exceed pre-pandemic levels. Consequently, a return to seller-side motivation to enter deals at higher valuations will likely return, if tech valuations remain at an elevated level.

Aerospace Industry

3.1 – Collapse of the Airline Industry

The European commercial aviation industry has taken an especially strong hit in the past quarter, mainly driven by the spread of the COVID-19 pandemic and the accompanying global groundings. Q2 included the most severe outbreaks of the pandemic in EMEA particularly. International travel restrictions caused by virus-related concerns led to both a collapse in air traffic for business and touristic purposes. These factors led to large uncertainty around the future of commercial aviation and created the belief that aviation will take years to recover, as supported by the IATA.

However, even before COVID-19, the scandal around the 737MAX airplane model as well as slowdowns in important markets were contributing to the decline in M&A activity and overall industry health. The effect on the defense industry, which is heavily interlinked with the aerospace sector, has been less significant and of a different nature. However, both industries shared an ecosystem that brings upon important implications on M&A activity.

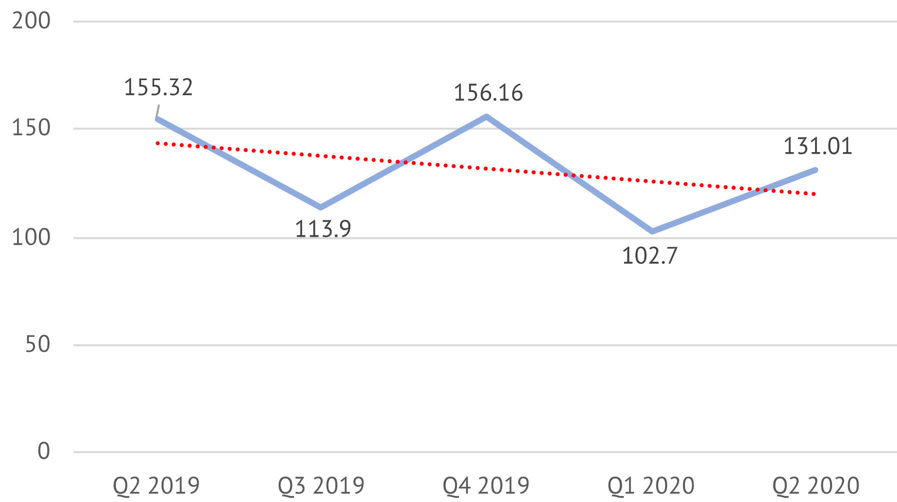
3.2– M&A Activity Overview

As like other sectors, M&A activity in the aviation industry following the outbreak of COVID-19 has sharply declined by 100% in EMEA. According to S&P Market Intelligence, in Q2 2020, we have seen no M&A deals in EMEA aviation. That being said, deal making will likely resume going forward, driven by divestitures, activity by financial sponsors, and portfolio reshaping. The changing industry landscape will provide lucrative M&A opportunities in Europe. In Q3, we have already observed a first announcement of a deal between TAP and Atlantic Gateway, possibly setting in motion a series of follow-on M&A in the industry.

The nature of M&A deals in the industry is also likely to change. Due to changes in expected growth and build rates in the aviation industry, firms pursuing vertical integration may re-evaluate business cases, shifting the type of M&A activity observed in the industry. Additionally, in desperation for short-term liquidity, struggling airlines seek cash injections which can be achieved by divesting non-essential assets.

In contrast to commercial aviation, the defense industry has seen a decent amount of M&A activity in Europe in Q2. Shifting geopolitical tensions and heightened uncertainty in general means demand for defense has not fallen off. However, it could not completely offset the strong negative trend in M&A activity in the aviation industry.

Figure 1.3 – Aerospace & Defense M&A Deal Value in EMEA (in $ Bn.)



To name an example, Russian arms manufacturer Motovilicha Plants has recently been acquired by Paslentia Investments. M&A activity has been particularly strong in Eastern Europe, with Russia leading.

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Oil & Gas Industry

The current state of the North and Latin American oil & natural gas industry is rather distressed. The months of March and April of 2020 saw crude oil prices plummet to lows below $20 per barrel driven by the combined effects of COVID-19 lockdowns and the decision by Saudi Arabia, Russia, and other OPEC based countries to not cut production volumes. This environment created an extreme case of oversupply in global oil markets worsening an already damaged situation as companies struggled with the impacts of coronavirus.

1.1 – New Competitive Environment

Looking back to the M&A landscape of 2019, deal count within the oil and gas industry has been declining along with the continuous fall of commodity prices. There were almost 400 global O&G transactions in 2019, which represented a substantial drop from 2018, despite deal value rising over 30% to $370 billion. This is indicative of the current trend shaping the industry in that large players continue to make deals in a wave of consolidation, but smaller companies have struggled to adapt to challenging market conditions since prices began falling in late 2018. In Q1 of 2020, there was $770 million worth of U.S. announced O&G deals, a 72.3% decline from the previous quarter. Surprisingly however, deal volumes increased in Q2 with $2.6 billion in newly announced deals within the U.S. That being said, this still ranks as the third lowest quarterly value since 2009. Companies within the sector have struggled to maintain financial stability and M&A activity as a result of lower prices. Additionally, unlike other industries, cash reserves among oil and gas companies were at low historical levels leading up to the events of 2020. In 2019, O&G companies' average total cash on hand over total debt was at 25%, an 18% decline from 2018 levels. This has left little room for companies to justify a strategic rationale for current deal opportunities, with cash being better used to maintain current operations and stability.

While few deals are currently being made, recent transactions have come largely from upstream gas-producing assets. Although crude prices have risen from lows to back around $40 per barrel, the uncertainty around oil has limited the market for new deals. Instead, strong future prices are driving some demand for gas assets leading to a resurgence in gas-based M&A and total Q2 transactions. Overall, natural gas has increased its share of U.S. based oil and gas M&A volumes from 5% in 2019 to 30% YTD.

Given the improbability of a strong rally in oil prices in the near future, the little transaction activity there is in the industry is likely to remain concentrated in gas-based assets over the next 2-3 quarters.

1.2 – Situation in Latin America

In Latin America, the overall landscape remains similar to the situation in North America. Most activity in the region is concentrated between the countries of Mexico, Brazil, and Venezuela, which account for 75% of Latin American oil production. Mexico and Venezuela offer mostly onshore drilling, and companies operating there will be forced to endure the same conditions as elsewhere. However, the present situation provides an opportunity for further investment and transactions within Brazil. Brazil benefits from a large production base of high quality, low cost oil from the pre-salt located offshore. This will be beneficial for companies operating there due to the low breakeven costs associated with drilling. Currently 10 of the 14 pre-salt fields in the region under concession are operated by the state-owned company Petrobras. The remaining 4 fields are operated by other companies such as Shell, ExxonMobil, Repsol Sinopec, and others. This could lead to economic growth for the Brazilian economy as a result of Petrobras' operations as well as other companies that will look to operate in the region in the future.

1.3 – Future Outlook

Looking at the future of oil and gas, North and Latin American based companies will be forced to undergo significant changes in order to survive a post-COVID environment. Given the uncertainty and speculation surrounding oil prices, it is likely that commodity prices of crude and natural gas could remain depressed for the foreseeable future. Companies will be forced to operate at lower margins unless they are able to evolve through improved efficiency and use of technology. As of now, 70% of O&G companies that are undergoing a significant business or technology transformation program may decide to put it on hold while they address liquidity issues. While companies certainly need to account for short-term stability, the importance of creating long-term efficiency through innovation must be balanced in the present. Whereas previously companies could plan for long-term pricing assumptions of $60 per barrel, moving forward companies will likely be forced to compete at prices in the $35 to $45 range. Additionally, the industry will experience further consolidation around large players as more companies file for bankruptcy. The larger players that have dominated M&A volumes over the past two years are likely to benefit from this landscape as a result of their ability to create economies of scale, whereas smaller companies will be more prone to distress.

Healthcare Industry

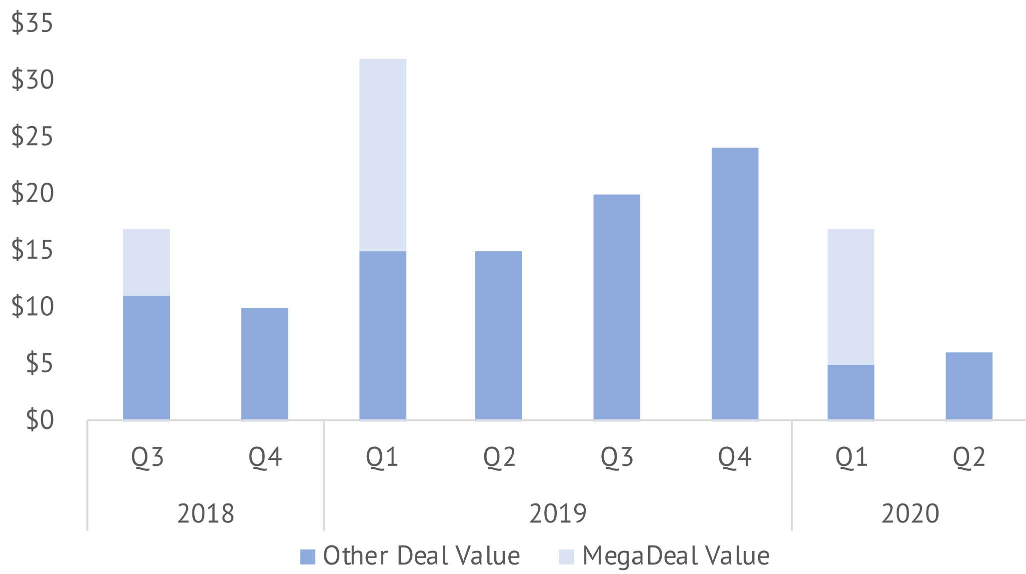
Perhaps the industry most largely impacted by the COVID-19 pandemic has been healthcare, which has been disrupted throughout the United States as coronavirus cases continue to rise. The global health crisis has forced all healthcare practices, from general hospitals to physician and specialty practices to drastically alter the manner in which they conduct their business as well as halting other forms of medical research. Like most industries, this has created a challenging environment for M&A activity in what had previously been an industry experiencing rapid consolidation. The future of healthcare M&A deals will be altered as a result of the changing practices and innovation that is being experienced across the industry.

2.1 – Previous Quarters Overview

Looking back to 2019, healthcare was among the most active sectors for mergers and acquisitions in the U.S., with deal-making hitting $533 billion over the year. This trend of consolidation can be attributed to several factors including high levels of dry powder among private equity firms and corporations, industry innovation and evolving forms of technology, and historically high levels of return on invested capital, among others. This environment, combined with the fact that healthcare typically proves to be a recession resistant sector, was driving M&A activity and company valuations within the industry higher throughout 2019 and into the first quarter of 2020.

Despite national lockdowns going into effect in the latter half of Q1 2020, M&A volumes within the sector remained relatively elevated with investment into the space increasing. There were 29 announced healthcare transactions in the first quarter of 2020, which is consistent with Q1 volumes from 2018 and 2019. Additionally, the average deal value increased 21% from Q4 2019 to $31.4 million that quarter.

Figure 2.1 – Total Healthcare Deal Value (in $USD Bn.)



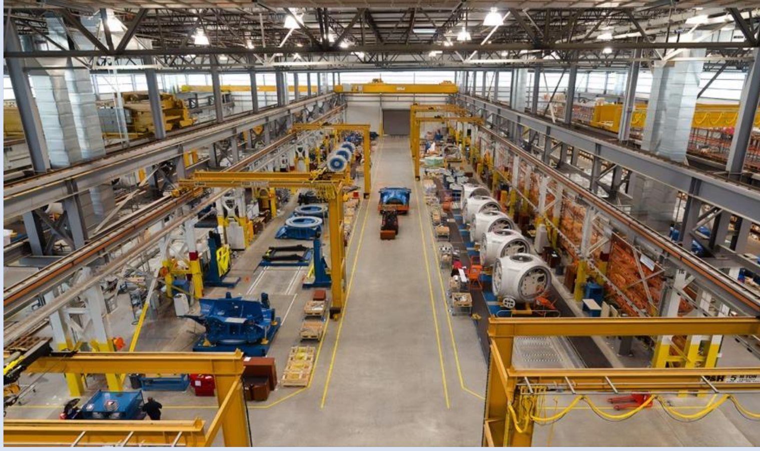
2.2 – The Current Situation

Looking at Q2 data, it is clear that deal volumes have fallen off from the levels reached in 2019, but the decline has been less dramatic than was initially predicted. Many expected that the effects of COVID-19 would prevent further consolidation as hospitals and other medical facilities shifted their focus to managing the crisis. This fear was upheld by the fact that hospital operating EBITDA margins had fallen 174% YOY in April. However, even given lower revenues and operating margins, there were still 14 new transactions announced in Q2.

2.3 – Future Outlook

The stability in healthcare M&A volumes is representative that consolidation within the industry is likely to continue and potentially increase post-COVID. Moving into Q3, we expect the number of deals to increase as shelter-in-place orders continue to be removed withstanding a resurgence in cases that would lead to another wave of national lockdowns. Additionally, there will be an increasing number of distressed and bankrupt medical facilities that will facilitate further deal-making. While the pandemic has led to short-term slowdowns in North American healthcare M&A, it may serve as a catalyst for more transactions over the coming quarters and years. Now more than ever, companies can utilize their advantages of scale and innovation to strengthen the rationale for future mergers and acquisitions. However, the pandemic will also bring about a transformation in healthcare operations. Looking to the future, the industry will be reshaped by an increased reliance on new forms of innovation and a normalization of telemedicine practices as companies will look to increase physician efficiency and reduce costs. The companies that are most capable of adapting to this landscape will benefit from future consolidation trends.

Automotive Industry



3.1 – Industry Decline

Like most other industries, the automotive industry has taken a pretty big hit during the COVID-19 pandemic. On the whole, there has been a large downward trend in sales volume with overall car sales being down 40% due to the pandemic. General Motors reports that for the first three months of the year, its sales were down by about 7 percent compared to the same period a year earlier. Nissan sales fell drastically, with a 30% year over year decline in sales. Since cars are typically considered a luxury good, it logically follows that with an overall economic decline, a similar decline in car sales would follow. Many of these car manufacturing companies have excess manufacturing capacity, and these unused factories have become deadweight liabilities. The decline in sales coupled with the excess manufacturing capacity may lead to an increase in the volume of factory sales as selling off unused factories will bolster on-hand cash as well as cut down on costs as these companies attempt to survive the pandemic.

3.2 – Positive Outlook for Car Manufacturers

Despite all the negative effects of COVID-19 on the automotive industry, a silver lining has appeared for electric car startups. The decline in overall sales volume is putting pressure on more established car manufacturers to push traditional SUVs on their customers, giving electric startups some time to establish themselves in the market before having to take on competitors head to head. SUVs provide carmakers with more profits, and the new low fuel prices make them the logical choice for leading products as carmakers now struggle to make ends meet. This newfound market space for electric car startups also provides an opportunity for Chinese investors, as industry-wide low valuations afford them the chance to get a foothold on North or Latin American soil via purchasing one of these comparatively smaller startup manufacturers.

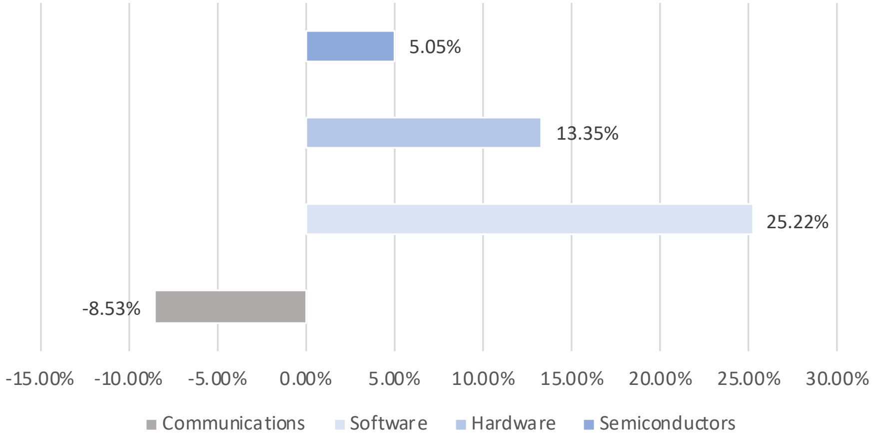
Additionally, some auto-manufacturing companies such as Ford were able to catch a break from the effects of the virus with the adoption of the new USMCA trade agreement. US president, Donald Trump, had previously threatened to impose tariffs on automobiles going from Canada and Mexico to the US, which had the potential to drastically disrupt car manufacturing supply chains. While many in opposition of the USMCA claimed the burden of higher production costs resulting from the agreement would be too high, it is largely believed that Trump’s promise to not impose these tariffs will offset those production costs. Ford also managed to get lucky with the implementation of this agreement because in 2017, they pledged to build new facilities in Michigan and renovate old ones, so this new agreement that encourages US manufacturing will increase the value of those investments. Like with the declining car sales, the adoption of the USMCA gives auto manufacturers even more of an incentive to sell factories with excess capacity. This is largely due to a provision in the USMCA that requires car manufacturing workers to get paid at least $16 an hour. That means existing factories with excess capacity will cost even more to maintain, further encouraging auto manufacturers to sell unused factories.

Technology, Media & Communication

4.1– Winners & Losers in TMT

Typically, the technology industry is adaptive to changes in the economy, but as with most businesses there are winners and losers. The COVID-19 pandemic has increased the value of cloud-based companies as well as subscription-based services, while hurting others like communications companies. The performance of different technology sectors varied, with YTD performance of software up 25.22%, hardware up 13.35%, semiconductors up 5.05%, and communications equipment down -8.53%. What are the reasons behind this varied performance? The sectors outperforming are ones whose business models can already operate remotely, hence why cloud-based services and subscription services were able to maintain or even increase their business during the stay-at-home orders of the pandemic. The important question is what is going to happen to the industry when stay-at-home orders are removed, and people get back to in person work and school? Analysts estimate that there will be a -5.1% decrease in Q3 for the technology industry, but by Q4 we will see a 0.5% recovery, followed by strong growth for 2021. The top performers in the following quarters will be the companies producing interactive home entertainment, software applications, and semiconductor equipment.

Figure 2.2 – Technology Sector: YTD Performance



The COVID-19 pandemic has accelerated the growth of some technology sub-sectors, slowed the growth of others, and has popularized a growing trend for employees to work remotely. Video-conferencing companies like Zoom have seen tremendous growth as a result of stay-at-home orders with the sector growth rate estimates increasing from 13.6% (pre-COVID-19) to around 30% up through 2023. Similarly, telecommunications companies like Verizon and AT&T reported an increase in the use of their wireless and broadband networks of 1000% and 400% respectively, citing companies, universities, and schools operating remotely as the driver. Conversely, hardware and semiconductor companies, although still seeing sector growth, have experienced supply chain difficulties due to the pandemic.

Supply chains disrupted by government work-from-home orders, and the quarantining of several cities in China who provide significant technology manufacturing, has made it difficult for hardware and semiconductor firms to meet their production needs. For example, Apple (NASDAQ: AAPL) announced it would delay the release of its new iPhone, citing issues with consumer demand and supply chain delays. Supply chains have since begun to recover, but it will take some time to fully rebuild back to their previous levels. Many large tech companies have been allowing some of their employees the option to work remotely since before the pandemic, however that notion has now gone mainstream. Considering that companies have found productivity is not hindered by working from home, and in fact has remained constant or even increased, technology companies are poised to allow their workforces the option to work remotely permanently. The tech companies who can successfully implement a fully remote workforce stand to gain value with reduced operating expenses (i.e. office rent, utilities, maintenance, etc.), and having access to a global talent group of potential employees.

4.2 – Space for Growth

M&A activity in the technology industry has slowed but could see an increase in the latter half of 2020. Historically, large tech companies have subscribed to the growth strategy of acquisitions with companies like Google, IBM, Facebook, Microsoft, and Oracle being the most active acquirers in the past decade. Since March 1, 2020, M&A activity in the technology sector declined by 30% compared to the same time last year. However, deal activity could pick back up in the latter half of 2020 as tech companies with large cash balances and/or access to liquidity look to buy out smaller firms at a discount. Besides growth-by-acquisition, tech companies have focused on research and development spending, not showing any signs slowing amidst the pandemic. R&D spending from the five large tech firms totaled $28 billion last quarter, up 15% from the same time last year.

4.3– Future Outlook

While the COVID-19 pandemic has significantly impacted the global economy, the technology industry in North America has remained relatively robust, with some sub-sectors like conferencing and telecommunications seeing unprecedented growth, while others like hardware and semiconductors have seen a decline due to supply chain disruption. Moving forward, the industry could see an uptick in M&A activity in the last half of 2020, with large tech firms looking to buy out smaller firms at a discount, and the industry outlook remains optimistic for 2021.

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Financial Industry

1.1 – Restructuring within Banks

In ANZ, the conclusion of the Financial Services Royal Commission, combined with the changing dynamics in things such as ‘open banking’, will serve to drive significant change within banking and the financial sector at large. We have already seen a divestment trend as financial institutions have sought to off-load their foreign divisions over the past years and sell off life insurance divisions to foreign buyers who can exploit their lower cost of capital and scale synergies. Banks have also to re-assess their Wealth Management arms, with a number of sell-offs (such as CBA’s sale of Colonial First State to KKR for A$3.3 bn in May) already occurring, and it is expected that others may find the future compliance costs greater than any derived revenue. In general, financial institutions in ANZ are looking to identify and carve out any potential areas where there may be issues with compliance and regulation.

Further, the status-quo of a ‘portfolio approach’ by large financial institutions is being forced to change as smaller entrants to the market are specializing in niches and forcing the entrenched players to deliver market leading services and products. This could further add to M&A divestment activity as financial institutions seek to make their operations simpler.

Similarly, to the majority of the APAC region, Chinese commercial banks are seeing lower interest rates drag on earnings, whilst there is expected to be lower revenues from credit cards and personal lending. Smaller and mid-sized institutions are naturally facing the brunt of this, but the government has continued its policy of containing financial-sector risk by providing recapitalization to struggling banks and more opportunity for lending to state-owned corporations. This further increase opaqueness in the Chinese commercial banking system and should slow any domestic consolidation within the industry, given the government appears to be willing to prop up struggling firms.

Another prominent M&A trend in the near future for Chinese banks is the acquisition targets that virtual banks present. COVID-19 has drastically accelerated the pace and importance of digital banking transformation. Traditional banks will be tempted to look at acquiring companies that have developed new technology that can be applied to their current product offerings, or at companies that have developed customer their own ‘virtual’ customer bases across different areas and present an opportunity to cross-sell services such as insurance.

In July 2019 it was announced that China will open up its financial sector to foreign investment through a number of measures, which included the removal of foreign ownership restrictions for securities firms, funds, life insurance and futures firms in 2020.

1.2 – 2020 at a Glance

The start of 2020 has seen numerous banks indicate interest and initiate taking managing control of their mainland financial ventures. Earlier in the year, JPMorgan Chase took control of China International Fund Management Co. for an undisclosed price. Some of the largest global financial institutions such as Goldman Sachs and BlackRock are now following suit in attempting to reach the US$13 trillion worth of assets held by Chinese households. The entrance of global players into the recently opened Chinese financial sector should be a major driver of M&A activity. It is expected that despite political tensions, foreign demand for Chinese assets will remain strong - especially given the potential addressable market in mainland China.

Whilst there is expected robustness in inbound M&A activity, Chinese outbound investment is likely to be directed towards countries with greater deal certainty for Chinese investors. 2019 saw India record its slowest annual economic growth of 4.9%, a major reason for this was the country's credit slowdown that hampered domestic demand. Banks had a high-level of bad debt on their balance sheet, with 9% of total bank lending in 2019 being non-performing loans. This has been accentuated by the economic shutdown from COVID-19. Former Reserve Bank of India governor Raghuram Rajan, the former Reserve Bank of India Governor, commented that the pandemic would lead to unprecedented levels of bad debt in 6 months' time. Accordingly, there has been little activity in the banking sector and financial sector at large in India- a trend that is likely to continue in the coming months as banks present risky investments and firms in the industry are conserving capital to brace for loan defaults.

Within the financial sector, it seems that fintech presents the best opportunity for a resumption of M&A activity. Due to local regulations, it is difficult for foreign players to develop their own operations from scratch. This makes local companies tempting takeovers for foreign firms looking to enter India. Recent legislation and tensions with China would however dissuade investment from India's largest neighbor, another headwind for financial sector M&A activity in India.

1.3 – Negative Outlook in Japan

The banking industry in Japan has a negative outlook. This is driven by incredibly low interest rates, as well as an ageing and shrinking population. Japanese financial institutions have typically looked abroad to generate growth in such an environment, with South East Asia typically being one of the preferred geographic locations for investment, given the economic growth in the area and large proportion of the population currently without bank accounts. Japanese M&A in general has been dominated by outbound M&A transactions, with outbound M&A reaching US$ 205 billion in 2019, a lower value than 2018 but still a very high level historically.

This environment, coupled with COVID-19, has put additional pressure on small and medium sized institutions and even the larger, better-capitalized banks, such as Sumitomo Mitsui Financial Group Inc. and Mitsubishi UFJ Financial Group Inc. are likely to conserve capital as a buffer against any further economic downturn. As a result, this will curtail outbound Japanese activity in the coming months, though there should still be a trickle of high-conviction acquisitions.

The Japanese insurance sector, arguably in a better position than the banks, is also likely to continue to see a slow-down in M&A activity in the short to medium term. The Japanese insurance market is one of the largest in the world. By total annual premium, Japanese Life Insurance is the second largest in the world, after the US, whilst its Property and Casualty insurance market is the fourth largest in the world. The sector is predicted to see a double-digit decrease in new business in the coming months and a single digit decrease in annual premiums following that. This, in combination with insurers having to rethink their business models to adapt to the new state of the industry, should again slow outbound Japanese insurance M&A. Nonetheless, there should still be activity as firms may be drawn by lower valuations in markets with gradually ageing demographics, such as Asia and Western Europe to expand their operations on relatively ‘safe’ investments. Japanese insurance firms will be looking to tap into their expertise with an ageing population in these markets.

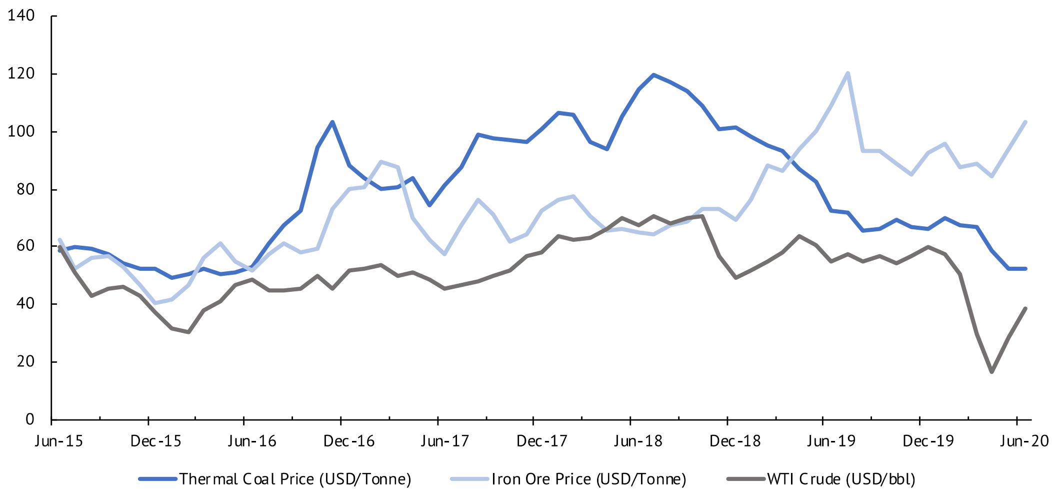
Natural Resources

2.1 – Market Volatility in the Natural Resource Sector

Activity in the resources industry has dominated the ANZ public M&A market for at least the last decade, representing ~25% by deal volume, on average. This is mainly due to the fact that around 60% of Australia's exports compose resources, namely iron ore, coal briquettes, petroleum gas, gold, and many others. Further, mining in particular has consistently constituted 10% of Australia's output over the last few years. Of Australia's total exports, just under 40% are destined for China, with a further 25% being split between Japan, South Korea, and India. Therefore, volatility for M&A in this particular industry is unsurprisingly due to ongoing global uncertainty regarding economic development post-COVID. Further, trade and geopolitical tensions between Australia, the U.S., and China, also threaten the robustness of the ANZ M&A space within resources in particular.

Indeed, the recent mega-mergers of Barrick and Randgold and Newmont and GoldCorp have composed a bulk of the industry deal volume, but the highest value deal in the resources sector recently was Wesfarmers' acquisition of Kidman Resources in the battery metals sector, which was completed in September of 2019. Even outside of public M&A, the Australian market saw Santos' A$2.15bn acquisition of Brookfield-controlled Quadrant Energy and Abermale's A$1.3bn acquisition of a majority stake in Mineral Resource's lithium-producing Wodgina project. Nonetheless, despite the resources sector historically dominating the ANZ M&A landscape, there has been a decline in total deal volume over the last year, as healthcare and financials have increased their share of deal volume on the back of increased activity by financial sponsors, namely KKR and BGH Capital. Indeed, this is partly due to the persistence of low commodity prices globally, and in particular, many companies with core efforts in oil and gas are struggling to adapt to these new market conditions. This difficult environment, coupled with restricted access to financing, has dampened deal making. This common theme of volatile and low commodity prices is likely to persist given COVID and overall geopolitical uncertainty, as seen in Figure 3.1. Rising iron-ore prices have cushioned the negative impact to this sector, but the M&A outlook for the resources sector is still uncertain in the short run.

Figure 3.1 – Natural Resources 5-Year Price Comparison



Commensurate with the struggling sector, less capital is flowing throughout natural resources. Outside of Saudi Aramco in late 2019, IPOs in this space have been close to zero, and both fixed-income and follow-on equity offerings have also decreased largely due to the limited access to capital markets, as well as high barriers to entry and considerable required capital expenditures. Smaller players have and will continue to find it difficult to acquire competitors to consolidate fragmented markets. As stated briefly earlier, private equity has presented itself as a recent driver of public M&A in Australia, but the amount of new money flowing in has targeted investments that look to be price-resilient and backed by real assets, and thus both investments and exits by financial sponsors have proved challenging in the current commodity markets.

In all, we expect aggregate distressed acquisitions to increase in this space throughout ANZ, but this is also largely dependent on the state of future commodity prices and the geopolitical tensions that have such a large impact on said prices. As China, Australia's biggest export destination of natural resources, begins to resume its industrial expansion, we expect greater deal volume more broadly, could be paused for the rest of 2020 if Coronavirus cases globally don't begin to slow or a vaccine isn't introduced commercially by Q1 2021.

2.2 – China Remaining Strong

Consistent with China's strong growth, aggregate M&A across all sectors has been strong over the past few years. In particular, Chinese outbound M&A has largely been concentrated on energy and natural resources, followed by the establishment of China as a net importer of many raw materials amidst their housing and infrastructure booms. Chinese companies have been the largest buyers of overseas mining assets throughout

2018 and 2019, increasingly targeting minerals needed for electric car batteries and clean energy technologies. Although broader M&A volumes have declined, some of China's mining companies have been acquiring domestic gold mines and strategic mineral producers on the back of depressed asset prices. In particular, Shandong Gold Mining Company in May of 2020 offered US$165m to buy Canada's TMAC Resources, and also offered US$221m for Ghana-focused miner Cardinal Resources in June. In the same month (June), Zijin Mining Group agreed to buy Toronto-listed Guyana Goldfields for US$238m, which is subject to approval. Hence, it is clear that the resources sector remains active in outbound mergers and acquisitions.

In aggregate, resource M&A in China has and will continue to be impacted by the introduction of the PRC Foreign Investment Law, which came into effect on the 1st of January 2020. The law will mean that foreign-invested enterprises will be subject to new corporate governance and capital systems, and so cross-border M&A with foreign capital providers will prove marginally more difficult from a regulatory point of view. In particular, as mineral-rich countries Australia and Canada tighten restrictions on foreign investment, players in the natural resources industry have seemed to enact a buying spree, as illustrated previously by the acquisitions undertaken or planned by Shandong Gold and Zijin Mining Group. Hence, geopolitics will likely play an important role in the activity of cross-border M&A in the natural resources sector, given that many Western countries are considering or have already implemented capital controls both to and from China.

With China a net importer of natural resources, it is evident that broader companies benefit from globally low commodity prices. As such, it is likely that short-term sentiment regarding commodity prices will increase volume in domestic M&A within the natural resources sector, particularly those with primary activities in thermal coal and petroleum, both of which have experienced a sharp drop in bulk prices as per Figure 3.1. However, it is also likely that the only companies with the capacity to engage in cross-border or domestic M&A will be strong domestically or state-backed with sufficient capital, expected that particularly in the natural resources space, we will see large deals, but fewer transactions in terms of aggregate quantity and volume.

2.3 – Rise of Indian Natural Resource Sector

Similar to the situation described in China, India has emerged as a net importer of natural resources, with over 30% of its imports coming from natural resources (~20% Crude, ~5.5% Coal Briquettes, ~6.6% Gold, etc). Their biggest export remains refined petroleum (~13%) to China and the UAE, however, with exports and imports representing ~20% and ~24% of India's GDP respectively in 2019, it is abundantly clear of the importance of natural resources to India's economy. In particular, India is one of the largest developing economies, alongside China, and so we expect the importance natural resources have on India to grow even stronger as it undergoes housing and infrastructure improvements.

M&A in the natural resources space has increased in recent times, consistent with the rapid growth in M&A activity throughout India more broadly in distressed deals, enabled through the aforementioned corporate insolvency resolution process under the Insolvency and Bankruptcy Code. In particular, 2019 saw BP's USD900m investment on a retail venture with Reliance, and an acquired stake in Adani Gas for USD870m. In addition, Saudi Aramco acquired a 20% stake in Reliance's oil-to-chemicals division for USD15bn in August. Hence, it is clear that there remains strong demand growth for refined products and an interest in privatizing assets, and so we expect downstream deal activity throughout India to remain active throughout the next few years.

With global commodity prices at major lows, it is clear that net exporters of these commodities are and will continue to suffer, and so given the improved and modern legislation surrounding distressed acquisitions, we expect that both domestic and cross-border M&A in distressed oil & gas assets in particular to increase as commodity prices continue to suffer from geopolitical volatility. This is supported through the fact that an overall economic downturn and an amplified oversupply have all the bearings of ushering in the next phase of consolidation.

Healthcare Industry

3.1 – Race for the Cure

Healthcare is the industry most largely impacted by the COVID-19 pandemic, which is facing disruptions across Australia. The increased demand for healthcare during the period has caused the Government to partner with private healthcare providers such as Ramsay Health Care to ease the burden on the public health system. This has created a challenging environment for M&A activity to take place, especially in the first quarter of 2020 during the initial coronavirus shock. Despite this, there are a number of ASX-listed healthcare companies that are currently under the spotlight for being critical players in the fight against coronavirus. Resmed, a California-based medical equipment company that has manufacturing facilities in Australia, is a global top-5 manufacturer of ventilators which are required to treat coronavirus patients. Ansell, a medical and industrial glove manufacturer is also facing high demand for surgical gloves. Fisher and Paykel Healthcare is also facing a demand spike for respiratory humidifiers, again important in the treatment of COVID-19.

3.2 – Healthcare Spending in Australia

Historically, Australian healthcare spending has grown at a much faster pace (~50% growth from FY07 to FY16) than population growth (~17% growth in the same period). Healthcare spending in 2019 was at $6,661, 9.2% of GDP, which was higher than the OECD median of $5,107 which made up 8.2% of GDP on average. Hospital expenditure was at 39% of the total, followed by primary health care being 35%. During the initial stages on the coronavirus pandemic (Q1CY20), healthcare M&A deal value declined by 70% to $918m compared to Q1CY19; at a median Q1CY20 EV/EBITDA multiple of 10.8x, lower than the 11.8x multiple in Q1CY19. 90% of the acquisitions in Q1 were from trade buyers, but PE activity increased in Q2 and is expected to continue increasing given the developing PE interest in Australian healthcare (Brookfield acquiring Healthscope and Aveo in 2019).

The lockdowns have reduced demand for pathology and general healthcare. People are delaying routine visits to the hospital, fearing that they might catch the virus. This is likely to have disastrous consequences in the future, with an expected increase in the number of people dying by preventable diseases or a delay in cancer detection. In this space, M&A activity has particularly increased during Q2. BGH Capital (Australian PE firm) is acquiring Healius' 70+ medical practices for ~$500m (10x EBITDA), after which it will become one of the largest operators of medical centers. GenesisCare (cancer care and heart disease specialist) acquired 21st Century Oncology for $1.6b (7x EBITDA), increasing GenesisCare's EV to $5b and increasing EBITDA to $450m. Crescent Capital Partners is planning to sell Australian Clinical Labs (Australia's 3rd largest pathology player) for ~$600m, expecting to attract interest from top-2 players Sonic Healthcare and Healius (or BGH Capital).

With long-term drivers of increasing population, ageing population, elective-surgery demand growth, and MedTech innovation, healthcare M&A is likely to increase post-pandemic. Moving into Q3, it is expected that the number of deals and deal size should increase. This may include distressed M&A for sectors facing incredibly low demand at the moment (such as pathology, ironically, given pathology is critical in preventing illnesses).

3.3 – What Happened in China During the Outbreak?

In China, the outbreak of COVID-19 brought the healthcare industry under spotlight, with vaccines, antiviral drugs, medical protection, IVD, etc. likely to affect M&A going forward. 2019 was an active year for China's healthcare M&A markets, with M&A deals in the pharmaceuticals sector totaling U$22.1b, highest in 4 years. The medical device sector was also active, with 12 companies listing and total M&A transactional value at U$2.7b. However, given the economic shock of coronavirus, total deals in China (incl. Hong Kong) totaled only U$8.4b, down 54% compared to the same period last year. Chinese outbound investment plummeted, with total deal value falling 93% to U$1.4b from Jan to May in EU and falling 89% to U$700m in North America. For the first time in a decade, inbound investment was higher than outbound, with inbound investment in the first five months of the year totaling U$9b.

The drop in outbound investment was due to governments around the world adopting stricter FDI policies to avoid predatory acquisitions during the health crisis. For example, the European Union released guidance for FDI urging states to protect companies and critical assets in health-related industries from foreign buyout. Similarly, Australia announced measures to drop investment review thresholds to 0 for all economic sectors, with a focus on preventing Chinese investment. This has made M&A in 2020 difficult for Chinese firms as compared to their activity in 2019, especially in the medical consumables space (one-time-use devices for medical purposes). Zhende Medical, one of China's largest low-value medical consumables providers, acquired a 55% equity stake in Rocialle Healthcare for U$6m in 2019 to create synergies in surgical sense control by integrating technology, production and sales channels. Similarly, Blue Sail Medical, a low- and high-value medical consumables provider, acquired NVT AG for U$193m to obtain market-leading heart-valve tech to expand their product line.

There are some key themes prevalent in China's healthcare market. China's pharmaceutical market is currently at the edge of shifting to innovative products and more efficient solutions through industry integration. Additionally, Investments in life sciences and healthcare are being driven by innovation and through use of technology. Online medical consultation, 5G, AI and big data are the current technology focus. Similarly, consolidation of providers to execute buy-and-build strategies and rising digital platforms and innovation investment are major investment themes which are likely to continue in the future.

3.4 – Healthcare in India

Healthcare is one of India's largest sectors (in terms of revenue and employment), growing quickly due to strengthening coverages, rising income levels, improved access to insurance and increasing public and private expenditure, with the sector reaching ~U$280b at the start of 2020. However, given India's high-density population, the country has had a difficult time dealing with the rising number of COVID-19 cases, entering a strict lockdown regime in early March, with more than 587,000 cases and 17,400 deaths confirmed by July.

M&A deals jumped a record 155% in the hospitals sector to U$1.1b in FY19, but M&A deals during COVID-19 faced many disruptions. Transactions in the structuring stages will likely to be deferred, and seller-driven processes will likely see bidders drop out. We are also seeing an increase in M&A in essential sectors within healthcare, with Maddison Dearborn Partners' proposed 55% acquisition of Quadrant PE-backed Advanced Personnel Management (injury management, allied health intervention) for U$825m being the largest transaction in Q1. Additionally, in May, Carlyle Group acquired a 74% stake in SeQuent Scientific (animal health-focused pharmaceutical company) for U$224m.

In the future, M&A activity in the healthcare sector is expected to increase as a proportion of total activity. In FY20, government spending on healthcare grew to being 1.6% of GDP, and government aims to increase spending to 3% of GDP by 2022. Health insurance will be a key driver of activity in the sector, given that currently, a large proportion of the Indian population is without any insurance. A crisis such as COVID-19 highlights the importance and need for insurance and should result in a significant uptick in the insurance sector and increased M&A activity.

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