Global M&A Report 2022

What the best companies did to win in a white-hot market.

Acknowledgments

This report was prepared by the leadership team of Bain & Company's Global M&A and Divestitures practice, with special direction from Andrei Vorobyov, partner; David Harding, advisory partner; Suzanne Kumar, practice vice president; Siobhan Galligan, senior manager; and an editorial team led by David Diamond.

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Letter from the M&A Team: Beneath the M&A Headlines

The world is changing for those in the trenches getting deals done.

Dear friends,

Welcome to the fourth annual edition of our Global M&A Report. Our mission remains constant: Use our unique position in the M&A world to connect what we see in our clients' executive suites with the larger trends happening across the globe. The result, we hope, is to make all of us a little better at the craft of M&A.

On the surface, the 2021 headline has to be "M&A is back." And so it was, with the highest total deal value in history. Strategic M&A, including corporate acquisitions and portfolio company add-ons, saw its second-highest year on record in 2021, fueled by all-time high deal multiples. Meanwhile, financial investors, special purpose acquisition companies, and venture capital accounts saw even higher growth. Strategic buyers are seeing a growing diversity of deal types, with alternative deal models such as partnerships increasing. And 2021 brought a renewed focus on scale deals as the disruption from Covid-19 presented opportunities for strong competitors to retrench around market leadership.

All of this made M&A more demanding for executives and deal professionals. Strategic buyers need an expanded set of skills to compete. Clarifying these broadened demands is why we write this report.

This year's report leads off with a quick year in review. We do start with the horse race statistics that many of our competitors focus on, but from there, we highlight exactly how the world is changing for those in the trenches trying to get deals done. The report discusses in greater detail several hot topics that might help you think about your job just a little bit differently.

The report contains 26 articles by Bain partners from around the world, commenting on specific industries and geographies where we think interesting things are happening. Please pick and choose as you see fit!

Finally, we have updated some of our core research underlying our belief in the concept of repeatable M&A. In a nutshell, frequent and material acquirers create greater total shareholder returns than those who don't have as robust an M&A strategy. This pattern has held up over the past two decades, despite the M&A market's evolution since.

Our report is a large undertaking. More than 280 executives from around the world spent time with us in surveys and follow-up interviews to help us understand what is really going on. More than 60 Bain partners took up their metaphorical pens to help us write the articles, and we were supported by a great team of researchers and analysts.

We love hearing from you. Send your feedback, commentary, and insights to us at M&A@bain.com.

Thank you for reading, and enjoy.

Sincerely,

The Bain M&A Team

State of the Market

As markets take off, strategic acquirers are evolving to meet new challenges.

By David Harding, Andrei Vorobyov, Suzanne Kumar, and Siobhan Galligan

At a Glance

- Total M&A deal value reached all-time highs of $5.9 trillion in 2021.
- Strategic deals (including both corporate deals and add-ons) saw value reach $3.8 trillion, an increase of 47% over 2020, fueled by record valuations.
- We are optimistic about the outlook for strategic deal activity in 2022, though there are several risks to watch.
- Strategic buyers need an expanded set of skills to compete in today's competitive market.
- Practitioners should focus on retaining talent, better underpinning revenue synergies, incorporating environmental, social, and corporate governance, leveraging partnerships and corporate venture capital, and building a repeatable M&A model.

The year 2021 brought record-breaking M&A deal values. After a down year in 2020, value rebounded to an all-time high, with soaring valuations and accommodating deal financing. Total transaction values reached an unmatched $5.9 trillion. Some buyers were motivated by the plethora of available assets and low cost of capital; others jumped into the fray to stay competitive as their peers did deals. Companies raced to acquire both transformative capabilities and to scale up in a historic land grab.

This robust market included an increasingly diverse map of dealmakers and deal types. Unlike the comparatively simple deal market of 20 years ago, which predominately comprised corporate buyers and some financial investor activity, today's M&A landscape includes significant participation not only from corporate buyers but also greater value from add-on deals (in which investors buy and combine multiple platform assets to create scale), financial investors, special purpose acquisition companies (SPACs), and venture capital (VC)/corporate venture capital (CVC). While strategic buyers (including both corporate buyers and private equity portfolio add-ons) saw total deal value rise by 47% year over year in 2021, these other forms of M&A grew about two times faster (*see Figure 1*).

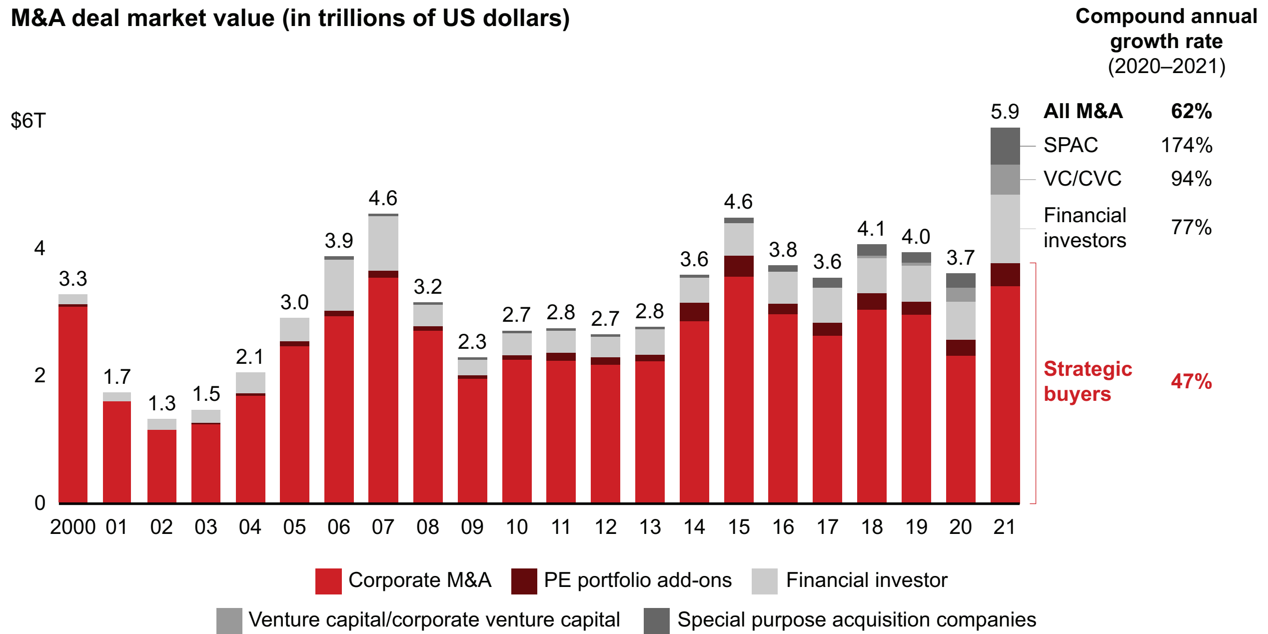
The overall story for strategic buyers was positive, with 2021 strategic deal values hitting $3.8 trillion. This makes it the second-highest year for strategic deals, a rebound from 2020 that matches feedback from strategic buyers that it has been a busy year (*see Figure 2*). In our global survey of 281 executives, a full 80% noted that deal activity was part of their broader business strategy in 2021, and more than half (52%) cited the availability of attractive assets on the market as a driver of deals this year.

For these strategic buyers, 2021 brought a nuanced and evolving market—one that demanded an expanded set of skills and a deep understanding of the deal landscape.

Within strategic M&A, some areas notably are booming more than others. Tech assets in particular have decoupled from the broader M&A market, with median enterprise value/EBITDA multiples at 25 times. This is partially explained by the broad applicability of digital capabilities required to remain competitive across sectors. Healthcare similarly saw asset prices soar, with median multiples of 20 times. In both tech and healthcare, buyers are willing to pay a premium for high-margin, high-growth assets. Meanwhile, non-tech and non-healthcare assets were also up vs. prior years, although median multiples of 14 times were well below the extremes seen in the other two industries.

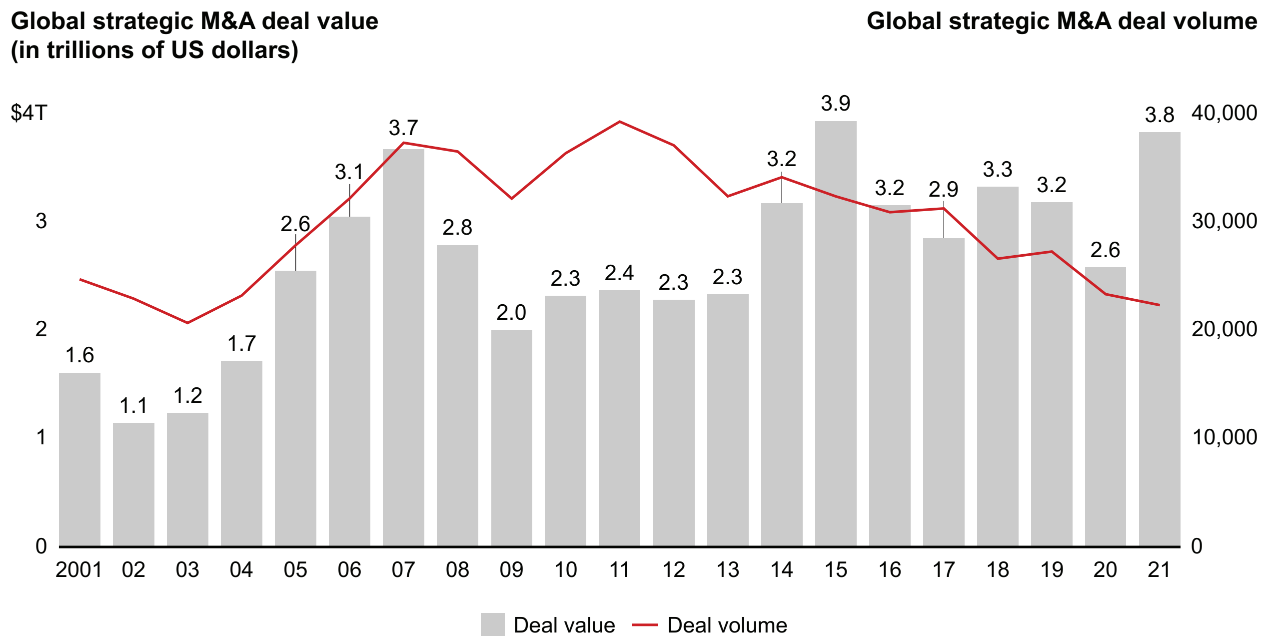
Strategic buyers across industries cited pain from these record deal prices. At the same time, public market trading multiples have risen even more quickly than strategic deal valuations, especially over the past two years (*see Figure 3*). Given this gap in valuations, companies should be able to capture returns from buying and integrating assets at lower multiples. Buyers worried about an overheated market could likewise finance their deals with stock rather than cash, yet there was not an underlying shift in stock vs. cash transactions. Deal executives have been cautious about valuations, even in a world in which public market valuations have been hot.

Figure 1: Strategic deal value grew by 47% from 2020 to 2021



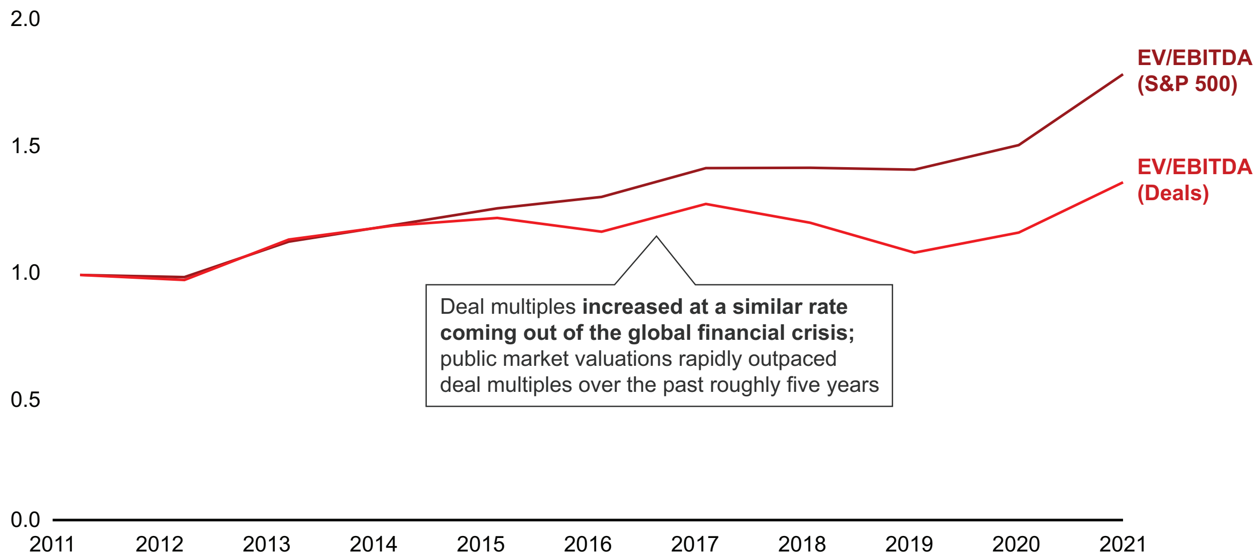
Notes: Strategic deals include both corporate M&A and PE portfolio add-ons; categorizations based on deal technique, industry, and acquirer business description
Source: Dealogic

Figure 2: 2021 saw $3.8 trillion in strategic M&A deal value



Note: Strategic deals include both corporate M&A and PE portfolio add-ons
Source: Dealogic

Figure 3: M&A deal multiples vs. public market multiples



Notes: EV=enterprise value; median deal multiples for announced strategic deals in which valuation data was available; trading multiples averaged unweighted
Sources: Dealogic; Capital IQ

Strategic buyers faced increased competition when they got into the game. Given their ability to underwrite synergies, strategics have historically had a strong hand against financial buyers. In 2021, nonstrategic buyers continued to grow their share of deal value as financial investors sought to deploy accumulated dry powder. Moreover, as public market valuations outpaced deal multiples, financial investors increasingly chose equity market alternatives such as initial public offerings and SPACs over exits to strategics. These trends challenge strategic buyers to identify, size, and underwrite synergies, including revenue synergies, to ensure competitiveness against alternative sources of capital.

Companies appeared to diversify their M&A strategy. Combined, joint venture and strategic alliance volume grew by nearly 4.6% between 2017 and 2020 (driven predominantly by strategic alliances), reaching a 20-year high in 2020. Meanwhile, CVC volume grew at a nearly 7% annual rate between 2017 and 2020, and the value of those investments increased by 24% annually over the same time period; 2021 further accelerated this growth trend. By pursuing partnerships and CVC, buyers maintain flexibility, mitigate the risks of large-scale M&A, and bring more variety to their M&A investments.

In 2021, scale deals were more common than scope deals, a partial unwinding of the trend toward deals outside the core business that we have tracked over the past several years. Scale deals accounted for more than half of large deals (those valued at more than $1 billion) throughout the first three quarters of 2021. During a year of significant supply chain disruptions, companies appeared to retrench around operational excellence and take advantage of pandemic-related dislocation in some markets. Given the high prices for assets, scale deals predicated on cost savings may have felt safer to buyers than richly valued scope deals underwritten by revenue synergies.

On top of all these factors, in a world of virtual work, social distancing, and travel limitations, companies continued to face challenges to the process of dealmaking itself. Organizational bandwidth limitations and pandemic-induced friction in the deal process did not fully subside, even as many industries got closer to business as usual.

In short, the 2021 rebound in strategic dealmaking took place in an evolving market. Companies sought to use M&A to keep pace with the trends transforming their industries (many of which were accelerated by Covid-19) while also navigating high prices and intense competition for deals.

What we are watching for in 2022

Many are wondering what lies ahead for 2022 and beyond. Bain's outlook remains optimistic, as many of the fundamentals for dealmaking remain attractive for buyers. We watch for risk factors that could change this outlook but do not yet see overarching signals of a slowdown.

Our optimism is reflected in the opinions of strategic buyers themselves. Executives have a favorable outlook: 89% anticipate that their own deal activity will either stay the same or increase in 2022. When asked to name the primary reasons why their organization pursued more potential M&A deals in 2021, 80% of surveyed executives answered that it was because M&A is part of their business strategy. So, absent significant shifts in business strategy, which we do not anticipate, it is unlikely that there would be a significant change in the relevance of M&A as a growth driver.

Additionally, while some read the high total M&A values as evidence that we are headed for a correction, our more nuanced focus on strategic M&A weeds out some of that noise. Indeed, as shown previously, strategic M&A shows positive but more muted trends than the broader deal universe, providing less credence to the notion that strategic deal value is bound for a crash.

We also anticipate a continuation of the secular trends behind the business model transformations that continue to produce deals. In particular, demand for new technological capabilities and underlying innovation will continue to grow. Additionally, in many industries, buyers face evolving strategic priorities, such as environmental, social, and corporate governance (ESG) capabilities, requiring companies to reevaluate existing portfolios and their M&A roadmaps in a new light.

Nonetheless, it's important to acknowledge several risk factors that could complicate this positive outlook. Deal activity has been amplified by expansionary macroeconomic conditions that have made capital plentiful and inexpensive. If central banks and governments phase in more neutral or austere fiscal policies, deal financing may tighten and dealmaking may level off.

Buyers face macroeconomic complications, including supply chain disruptions, inflation, labor shortages/greater competition for talent, and rising wages. If these factors intensify, that could create an environment in which companies become less expensive to acquire, even as potential buyers come under financial pressures of their own. Deals would be cheaper, but wallets would be emptier.

Strategic buyers also face evolving regulatory scrutiny that may have a chilling effect. About 44% of executives report that they already are seeing or expect to see greater scrutiny from regulators. This scrutiny has two components:

- the increasing salience of antitrust as a global political issue; and
- growing concern about the national security implications of M&A.

Even if deals are not ultimately blocked, the need to build more time and resources into M&A processes to navigate regulatory review may slow dealmaking. Some more recent actions, including UK regulators' call for Meta to divest Giphy as well as the US Federal Trade Commission's lawsuit to block Nvidia's purchase of Arm, have many wondering which regulatory interventions are one-off vs. indicative of new regulatory regimes.

Meanwhile, many are also tracking the impact of geopolitical evolutions, particularly with regard to China. China's rapidly aging population, less growth-oriented state outlook (as evidenced by state crackdowns on the country's biggest private sector firms), and strained relations with other major players in the global economy may cause its economic engine to stall. Such a slowdown could create ripple effects for global M&A in the coming years.

We anticipate some evolution in each of these risk factors in 2022, but we do not expect dramatic changes across all of them in the short term. In contrast, many of the positive drivers of deal activity will continue to create tailwinds that support dealmaking in the year ahead.

Strategic buyers face evolving regulatory scrutiny that may have a chilling effect. About 44% of executives report that they already are seeing or expect to see greater scrutiny from regulators.

What does this mean for the M&A practitioner?

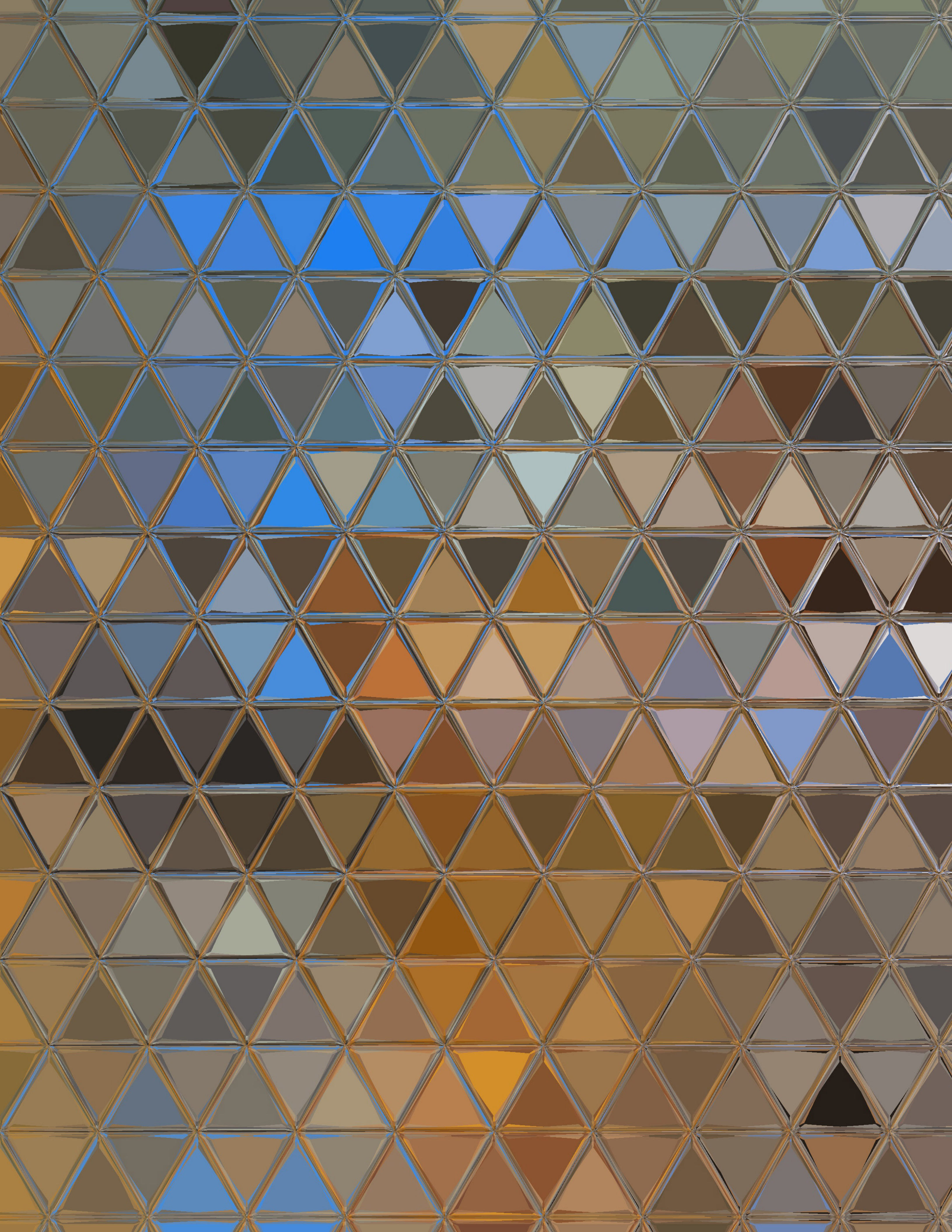
Today's buyers face an M&A environment that demands more from them than ever. Prices and competition are up, so what are the best practitioners doing to find success?

Elevate the importance of talent. Retaining talent is a critical success factor for many deals, especially for capability deals. Savvy acquirers recognize that talent is often one of the most valuable assets being acquired, and buyers run a significant risk of attrition when employees are uncertain about their future roles. Please see "Reimagining Talent in M&A" for our take on how successful companies are reimagining their hiring due diligence, reading the talent landscape, and using employee insights to inform their integrations.

Evaluate and capture revenue synergies. In a world of high valuations, evaluating and capturing revenue synergies is becoming ever more critical to today's buyers. Proprietary, data-driven diligence on revenue synergies enables companies to home in on desirable targets amid record-high multiples. Preparing to capture revenue synergies from day one and staying focused on the combined customer value proposition ensures that companies get what they paid for. See "Bringing Science to the Art of Revenue Synergies" for more details on the rigorous approach that can guide this process.

Expand the M&A playbook. Buyers are broadening their M&A playbooks to account for new business needs and deal types. ESG is becoming a growing factor in the M&A process and a source of value for buyers. This introduces new strategic questions for buyers at all stages of the ESG game, which we address in "The ESG Imperative in M&A." Beyond deal considerations, buyers also are looking to structure deals differently. Alternative deal types, such as partnerships (joint ventures, alliances) and CVC are often proving an appealing investment opportunity, but they require distinct strategic approaches. This is covered in greater detail in "Delivering Results in Joint Ventures and Alliances Requires a New Playbook" and "Harnessing the True Value of Corporate Venture Capital."

Build a repeatable M&A model. Companies that frequently and materially acquire outperform their less-experienced peers in total shareholder return. In this report, please see an updated version of "Bain's Bedrock Beliefs on How to Create Value from M&A," which continues to show that in today's environment, as before, M&A is a learned skill. Companies that make more acquisitions are more often likely to identify the right targets, develop the capabilities required to vet deals better and faster, and form the organizational muscles to more effectively integrate acquisitions.



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Hot Topics

Reimagining Talent in M&A

With survival and growth riding on a company's ability to hire the best talent, more executives are finding creative ways to solve the people equation.

By Sinead Mullen, Tim Leonard, and Marc Berman

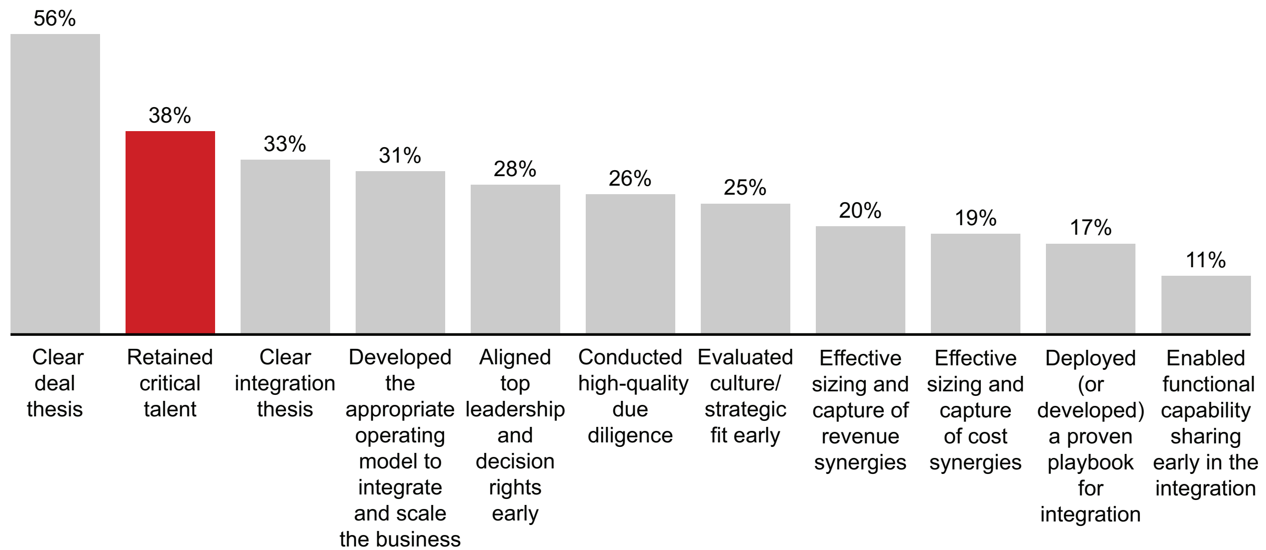
At a Glance

- Executives see talent retention as the second-biggest contributor to deal success. And with record numbers of employees actively job searching, the challenge is getting even more critical as many industries face a talent shortage.
- The best companies take critical steps in both the diligence and integration stages to ensure that talent stays put. For example, they invest to understand a target's centers of influence and perform extensive diligence pre-close to assess attrition risks and employee engagement.
- Executives who successfully retain key talent through integration say that establishing a strong and compelling vision for the future is the most important element contributing to that success.

Even in the best of times, mergers and acquisitions cause employees to worry about uncertainty and change, often leading them to consider other options. But these are not the best of times. Virtually no company has been unaffected by the Great Resignation as record numbers of employees explore new opportunities.

A March 2021 Gallup poll found that 48% of the US working population was actively job searching or watching for opportunities. It was a survey that included workers in every job category, from hourly consumer-facing roles to highly paid professionals. According to the US Department of Labor, more than 4.5 million workers quit their jobs voluntarily in November, the most in the two decades in which the government has been keeping track.

Figure 1: M&A practitioners cite talent retention as a leading driver of M&A deal success, second only to having a clear deal thesis



Source: Bain M&A Practitioners' Survey, 2022 (N=281)

These are stats that haunt any proposed talent-focused deal: People were already thinking of leaving, and a pending acquisition or merger can make that decision even easier. Our survey of executives found that talent retention is the second-biggest contributor to deal success (*see Figure 1*). When talent is a major factor in a potential deal, acquirers need to proactively address people issues throughout the diligence and integration processes. Some companies are doing a better job of this than others.

Reimagine your people due diligence

While most executives acknowledge that people issues are critical in an integration, they often examine only a few areas during the diligence process. They tend to focus primarily on the executive leadership team; they also typically explore a limited set of solutions, such as compensation packages for senior leaders. Acquirers that are surfacing as winners, however, take a robust and creative approach to people diligence when exploring a target. This approach gives them visibility into the team and culture that has propelled the target's success and can inform decisions about whether to pursue the deal and how to shape an eventual integration.

It starts by understanding a target company's centers of influence. That means quickly identifying key players across three categories:

- **Who is mission critical today?** Who drives the day-to-day success as a result of their expertise, and who is critical in the near-term to ensuring continued performance and supporting the integration?
- **Who is mission critical tomorrow?** Who can deliver the capability spikes needed to achieve full potential?
- **Who are the true people influencers?** Who do people listen to, and who will likely take others with them if they leave?

Acquirers need to ask pointed questions to build an initial list of critical talent, outlining their roles and responsibilities and specifics on how they are critical to the success of the company. Leaders should quickly craft a strawman of the combined company's future operating model, working to answer two basic questions:

- How different is it from the way they work today?
- What level of change and disruption do they anticipate for the key players?

It's important to keep a close eye on impacted populations that are both critical to future success and that are likely to undergo a significant change. Invest heavily in these individuals. As soon as possible, cultivate direct relationships with them to understand their aspirations, motivations, and career goals. Financial incentives keep people in the short term, but nonfinancial considerations around purpose, growth and development, and cultural connectivity keep them for the long term. Actively build a point of view on their likelihood to stay and potential drivers for retention, and build it into your plans from day one. It's essential to ensure that acquisitions are aligned with longer-term talent strategies—including building the new capabilities that can drive growth; unlock new adjacencies; and support diversity, equity, and inclusion efforts.

Get creative about how to read the landscape

Too many executives underinvest in people diligence simply because they don't believe they can access meaningful information until after close. Yet the best talent acquirers find ways to be proactive pre-close to determine the potential risks and accelerate the integration journey from day one. These are the steps that matter.

Get the conversation started. Don't shy away from engaging key talent. Ask to speak with a broader group of people, not just the executive team. In addition to those conversations, reach out to alumni—they may be willing to speak more openly than current employees. Remember that different sources are biased in different ways, so you need a balance of perspectives. These conversations can give you significant insights into talent, existing strengths and weaknesses, perceptions of your company, level of attrition risk, and hidden assets within the organization.

Leverage publicly available data. Digital tools can help bring visibility into a target's historical attrition rates or engagement metrics during diligence. Together, they can paint an accurate picture of the employee dynamics within the company. Glassdoor offers preliminary insights into employee sentiment, allowing you to anticipate attrition risk, change fatigue, or burnout in the target company. LinkedIn provides visibility into the organization, helping you understand the current operating model and depth of capabilities. Fishbowl includes open conversations from employees, providing insight into how the community interacts.

Use people insights to guide the integration

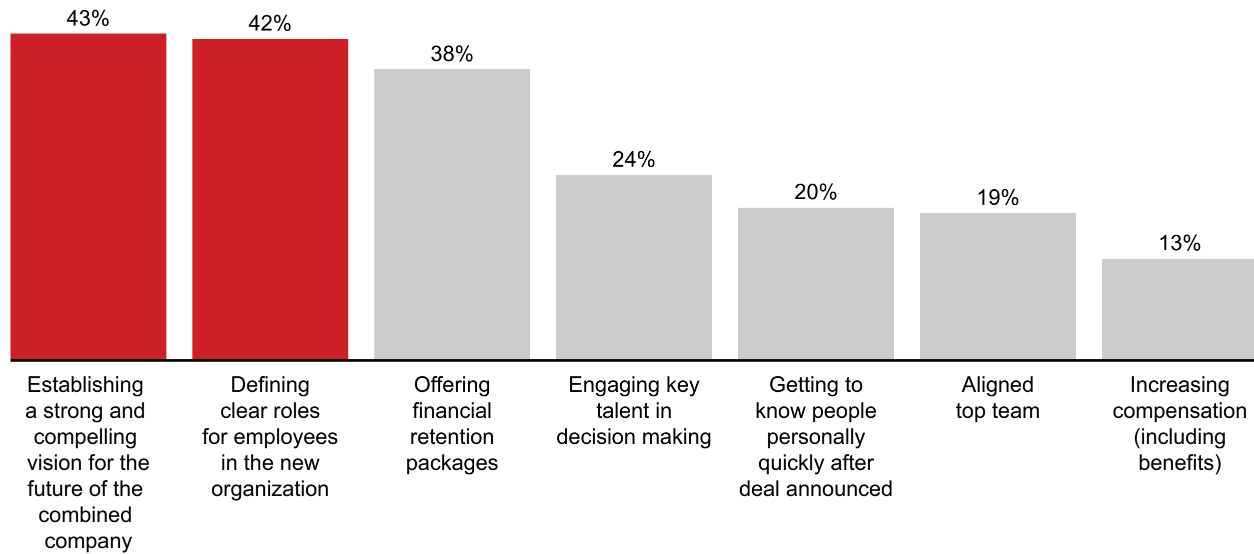
The people diligence should inform whether you do the deal. If that diligence raises too many red flags, don't hesitate to walk away. But if the people and culture issues seem manageable, the diligence should dictate how you approach integration. As soon as you mobilize for integration, translate people diligence learnings into implications for the integration. Two best practices ensure that you are engaging on people issues right from the start.

Cocreate a clear, compelling vision for the combined company. Executives who successfully retain key talent through the integration say that establishing a strong and compelling vision for the future is the No. 1 most important element (*see Figure 2*). Immediately after closing a deal, bring leaders and influencers together to craft that vision for the future organization. This narrative should include a case for change, a view of the future state, measures of success, and guiding principles—the guardrails for making key decisions. The simple act of imagining and defining a shared future so soon after close helps to align leaders, build excitement, and foster energy for the change ahead.

In the merger that created UKG, leaders from Kronos and Ultimate Software came together to shape the story of their future, clarifying their shared purpose and highlighting the opportunity to make even more impact as a combined entity. This process aligned leaders around a shared aspiration to truly put people at the center of their business. The process also alleviated concerns around cultural differences and distinctive ways of working.

Acquirers need to ask pointed questions to build an initial list of critical talent, outlining their roles and responsibilities and specifics on how they are critical to the success of the company.

Figure 2: The top two factors for talent retention, compelling vision and clearly defined roles, are nonfinancial



Source: Bain M&A Practitioners' Survey, 2022 (N=281)

Build energy from the middle. Tons of great talent sits below the executive level. Reach out to those key leaders and critical influencers, and directly engage them in the process, enlisting them as integration ambassadors. This team can provide feedback on the integration journey, identify and help solve emerging issues, and build cultural understanding and connectivity across legacy organizations. This group can help protect the blind spots of the executive team and integration leaders. They see, hear, and experience the integration (and the business) differently, and they can pinpoint risks, opportunity areas, and emerging challenges.

Such a team played a key role in accelerating the cultural integration of Caliber and Abra, supporting the rollout of store conversion and other key changes. By inviting these individuals into the process, the leadership team empowered key influencers to proactively support and shape the change journey while building advocacy within the organization.

Understand the organizations' capacity for change. The ability to navigate change through an integration is a key determinant of value in most deals. Many leaders pay limited attention, however, to change readiness—that is, an organization's capacity to effectively navigate change.

If people diligence raises too many red flags, don't hesitate to walk away.

Bain's Change Power Index® tool helps companies anticipate the change archetype of both their own company and that of the target. It serves as a starting point for planning for remedies and solutions. Clearly understanding each organization's ability to change can help determine how to structure an integration in a way to support your talent strategy and accelerate value capture while mitigating risk.

The popularity of using M&A to obtain and retain scarce talent has introduced a new term into the business lexicon: the "acqui-hire." As the talent gap threatens growth and profits across industries, more companies will devote more energy to performing creative people diligence and enabling people insights to guide integration. How to predict the winners in the raging war for skills? They're the companies with an unwavering focus on talent before, during, and after the deal—deal after deal.

Hot Topics

Bringing Science to the Art of Revenue Synergies

High deal valuations call for a more rigorous approach to jointly boosting revenue.

By Adam Haller, Benjamin Farmer, and Suzanne Kumar

At a Glance

- Revenue synergies are becoming critical for deals in today's high-valuation environment. But unlike cost synergies, revenue synergies are difficult to size and to realize.
- Overestimating revenue synergies was the most cited reason for deal failure among the 281 executives we surveyed, yet only half of those executives said that they bake revenue synergies into their deal models.
- Successful acquirers develop a proprietary, data-driven view on revenue synergy value creation during diligence, giving them more confidence in valuation and bid strategy.
- The best acquirers also fully utilize the pre-close period to prepare the product roadmap and adjust the sales model so that they realize results from day one. They then track those results and evolve their revenue synergies playbook with each deal.

Revenue synergies in M&A have been traditionally treated as something of an art by dealmakers. Compared with the relatively industrial approach common to cost synergies, acquirers often develop a bird's-eye view on revenue synergies and stop well short of using them to underwrite the deal. Yet, in today's M&A market, record-high valuations have forced acquirers into a more rigorous approach to estimating and committing to top-line growth. Acquirers must be more scientific:

They must clearly determine in advance how and how much the deal will jointly boost revenue. Companies that commit to underwriting revenue synergies in the deal model are the most likely to meet or exceed their targets, according to a recent Bain executive survey.

The trouble is that revenue synergies are difficult to size and to realize. In fact, overestimating revenue synergies was the most-cited reason for unsuccessful deals in Bain's recent survey of 281 executives.

This isn't surprising. Maximizing revenue synergies requires a high degree of focus, execution, and commitment. Even cross-selling existing products to existing customers can be stymied by lack of data visibility (especially pre-close), poor coordination, and mismatched motivations across target and acquirer. The base business takes priority in the face of potential deal-related disruptions. Successful acquirers ensure that their newly combined salesforce is well positioned to register a few early wins, spurring conviction and positive momentum in the field.

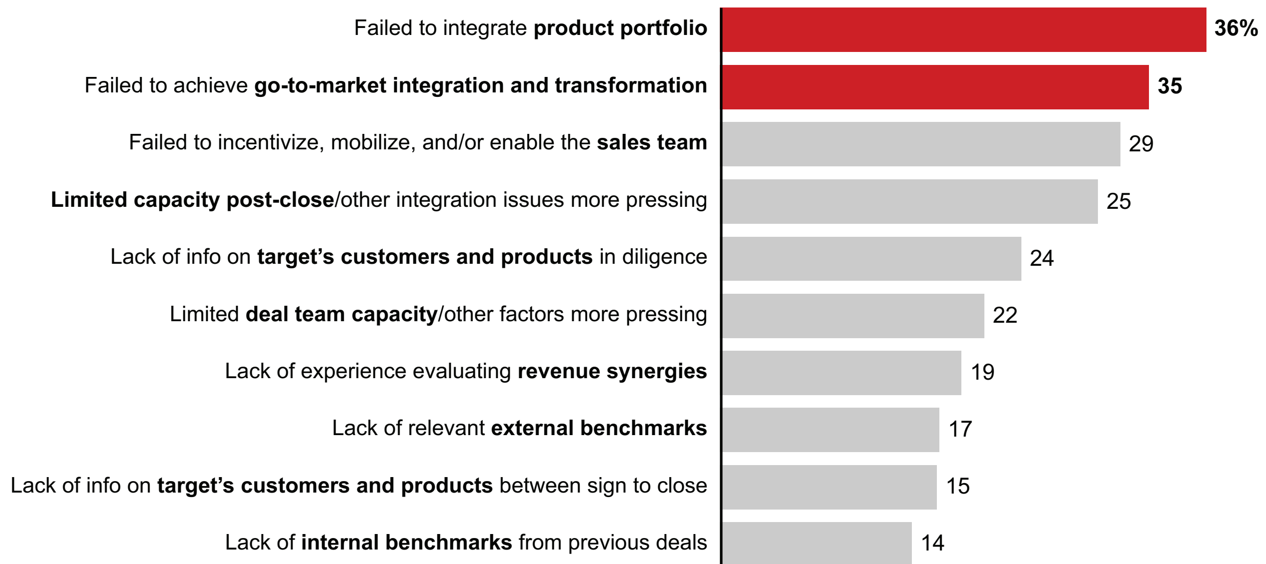
Meanwhile, transformative revenue synergies, such as new customer value propositions, combined product offerings, and updated go-to-market approaches, can be more difficult and take longer to realize. These more ambitious sources of value require extensive behavior change across the value chain, from product development to sales, as well as across business units. And it can take up to three to five years to see the full results, according to Bain benchmarks. No wonder our survey respondents cited failure to effectively integrate the product portfolio and achieve the full go-to-market transformation as the two biggest obstacles to capturing revenue synergies *(see Figure 1)*. All of this may help explain why only half of surveyed executives told us that they typically bake revenue synergies into their deal models.

Successful acquirers flip the script. These companies develop a proprietary, data-driven view on revenue synergy value creation during diligence, giving them more confidence in valuation and bid strategy. They fully utilize the pre-close period to prepare the product roadmap and adjust the sales model so that they realize results from day one. They then track those results and evolve their revenue synergies playbook with each deal.

We'll look at the four key steps to turning revenue synergies into a competitive advantage.

Step 1: Begin yesterday. Don't wait until the dust has settled to evaluate and plan revenue synergies. Sophisticated acquirers build an outside-in perspective on possible targets (and potential new products) years ahead of live deals. When performing diligence on specific targets, these companies use rigorous and creative research to detail the customer map and evaluate customer needs. Advanced analytics enable deep examination of historic customer buying behavior and modeling of future potential. Primary customer research and a review of win-loss track records from the seller can inform potential product bundles and the combined product roadmap. Such analysis can confirm (or deny) the deal thesis and provide dealmakers with more confidence in valuation.

Figure 1: Ineffective product portfolio integration was the most common reason for a failure to capture revenue synergies



Source: Bain M&A Practitioners' Survey, 2022 (N=281)

The best acquirers rely heavily on a clean room to conduct data-driven sales planning between sign and close. They share unblinded data within the clean room and use that data to go deeper on customer segmentation and account-level planning. As day one approaches, they selectively add individuals to the clean room to validate the findings.

A medtech company with a long track record of revenue growth prioritizes an early and tactical approach to revenue synergy planning. During a recent acquisition, the company's diligence detailed not only the product and customer overlap but also the channel strategy and salesforce model required to maximize growth. It found that the company's channel strategy must shift from a mixed model to more direct salesforces, with as much as 90% direct in key geographies. And it decided that with a potential 30% customer overlap, it needed to realign sales responsibilities to avoid customer confusion. Therefore, immediately upon deal announcement, a clean team began designing the future-state go-to-market model, including regional channel strategy, salesforce assignments, and a shared customer approach. Such detailed diligence and integration planning enabled reps to begin selling in new territories and across the full portfolio about 90 days post-close, the fastest launch in the business unit's history.

Step 2: Center on the combined value proposition for the customer. When pursuing growth-oriented deals, a customer-centric approach to M&A uncovers value creation opportunities that would otherwise go overlooked or deferred. The best acquirers test existing and new combined product offerings during diligence. They use the pre-close period to build a detailed customer segmentation. As deal close approaches, they look for opportunities to convey how the anticipated combined value proposition will benefit customers from day one. Winners also consider how to bundle existing offers and effectively position for cross-selling upon close. Finally, they build a long-term roadmap for product integration and joint value proposition, using it to focus the integration on key decisions that will support an improved product and service offering for customers.

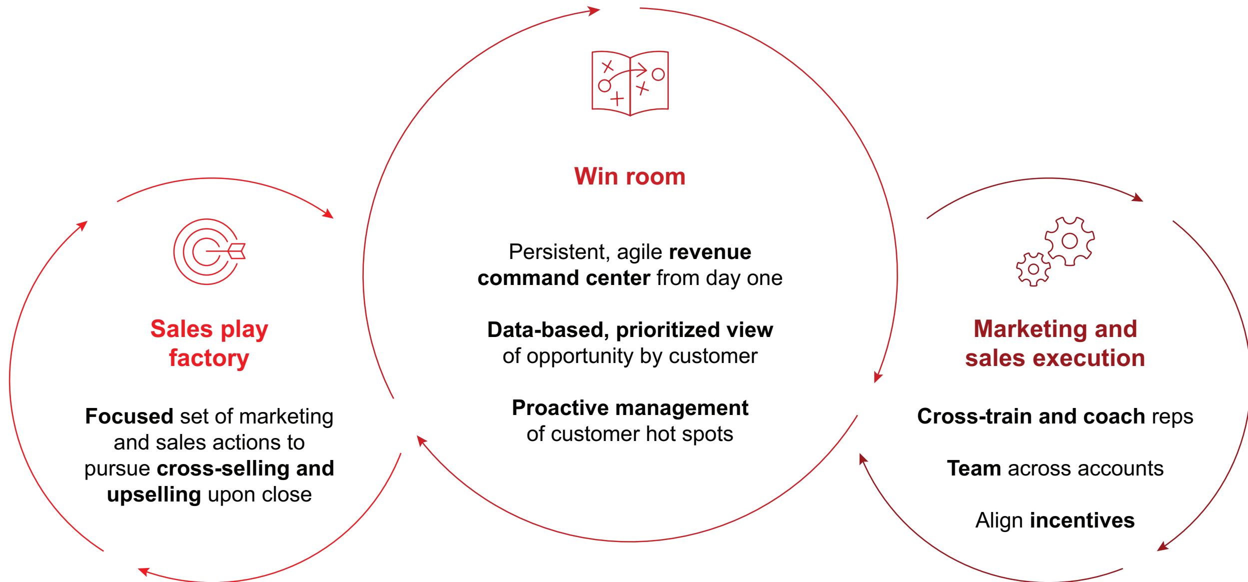
This approach helped one global technology company more than double its targeted revenue synergies when it acquired a target with a highly complementary product portfolio and go-to-market model. The acquirer executed deep customer and competitor diligence to test customer needs and the potential market for an integrated product offering that would supersede any available value proposition. Convinced that they had identified a home-run opportunity, the acquirer prioritized the joint offering in integration planning and decision making across engineering, sales, and ops.

Step 3: Enable the sales team to hit the ground running from day one. The best companies work to generate revenue synergies momentum from day one and plan for what they can kick-start in the first 90 days. They don't wait for the longer-term product and sales transformation to get started; they begin capturing upside with existing products and the current sales teams and structure. A day-one revenue Sales Play System℠ provides the focus and execution support to make this happen *(see Figure 2)*.

The first step is to prioritize plays for upselling and cross-selling. An acquirer can't expect the salesforce to take an entirely new product catalog to its full set of accounts. Instead, it's important to zero in on the target use cases, value messaging, and sales collateral that are a natural fit and can be sold today. (For more on this Sales Play System, see the HBR.org article "The Sales Playbook of Successful B2B Teams.")

As deal close approaches, look for opportunities to convey how the anticipated combined value proposition will benefit customers from day one.

Figure 2: Day-one revenue synergies enabled via Sales Play System℠



Note: Sales Play System℠ is a service mark of Bain & Company, Inc.
Source: Bain & Company

Sika, a construction chemicals company, applied focused sales plays to achieve ambitious revenue synergies. The company knew from a long track record in M&A that trying to sell everything to everyone doesn't work. In the construction industry, different trades have different product needs for different applications, and they are served by a hybrid network of local distributors and manufacturers. By acquiring Parex, a mortars company, Sika expanded its building finishing offering and gained a strong foothold in the ultra-local distribution channel in China through Parex's established relationships with thousands of professional distributors. Immediately after closing the deal, Sika systematically prioritized and introduced flagship stock-keeping units in these distribution channels, generating quick revenue synergies from a laser focus on what to cross-sell and to whom. As sales reps delivered early wins, frontline confidence and excitement about the Sika-Parex combination grew. The salesforce leaned in on the first sales plays. The first wave of synergies accelerated, and the China team moved to more advanced sales plays while transferring the approach to other high-growth markets.

Second, it's necessary to set up a "win room"—that is, a revenue command center to prioritize and manage sales plays, track results, and identify the next opportunities on an agile basis. The best companies use the win room to proactively address revenue dis-synergies, too, identifying overlapping customers or products and developing specific plans to resolve those hot spots.

Third, winning acquirers invest heavily in sales execution. They support the sales team by cross-training and coaching reps, providing clear rules of engagement, and aligning incentives.

They mobilize each rep with a simple and tactical plan that includes a list of prioritized clients, products, and sales plays for the first 12 weeks. They also use clarity and compensation to resolve hot spots around shared customers or overlapping products.

Seismic, a fast-growing PE-owned software company, recently acquired Lessonly, a scope acquisition with meaningful revenue synergy opportunity. To maximize synergies and accelerate realization into year one, Seismic followed this proven playbook. First, the company developed a series of cross-selling plays that were tailored to the needs of each customer segment, outlining what product bundles to offer, focused messaging, competitive positioning, and the winning sales cycle to close the deal. Seismic then enabled 100% of the combined salesforce on these sales plays in the first week after close through a two-day, go-to-market training session to motivate sales reps regarding the opportunity at hand. Lastly, they set up a focused win room to help navigate large and complex cross-selling opportunities in real time. As a result, the sales reps were able to build a cross-selling pipeline immediately and have meaningfully exceeded year-one revenue synergy value.

Step 4: Learn from every deal. These three steps give companies a scientific way to identify and capture revenue synergies from their deals. Yet there is one more step that helps ensure that companies make the most of this approach—namely, tracking synergies to develop a proprietary angle on the next deal.

Winning companies use each deal to learn which sources of revenue synergies ultimately materialize and which fail to deliver so that they can determine the critical activities for success and the right key performance indicators to track. They refine a repeatable revenue synergies capability that helps the M&A team focus on the right data, improves diligence on subsequent deals, and sets them up to win more deals—and with greater confidence that they can achieve revenue synergies to justify deal valuations each time.

Hot Topics

The ESG Imperative in M&A

Acquirers need to assess target companies for hidden risks and for ways to advance their environmental, social, and corporate governance agendas.

By Jean-Charles van den Branden, Axel Seemann, and Marc Lino

At a Glance

- In our survey of M&A executives, only 11% say they extensively assess environmental, social, and corporate governance (ESG) in the deal-making process on a regular basis today, but 65% expect their company's focus on ESG to increase.
- Some companies are ahead on this curve. By incorporating ESG into their M&A process, they have set themselves up with an advantage in pursuing value creation opportunities and a head start in meeting their ESG imperatives.
- By making sustainability a part of each deal thesis and using corporate priorities as a benchmark to assess each potential deal, the best companies find assets that will advance existing ESG initiatives *and* create economic value.

Environmental, social, and corporate governance (ESG) is rapidly becoming front of mind for regulators, investors, customers, and employees—and it is rising to the top of corporate agendas as well. As ESG gains in importance, it is becoming a mark of business quality. Many now view a well-devised corporate ESG strategy as a positive indicator for long-term revenue growth.

In our recent global survey of 281 M&A executives, 65% expect their own company's focus on ESG to increase over the next three years. This view extends to M&A. More than half of surveyed respondents either see ESG leadership as justifying higher deal valuations or expect this to be the case in the future, indicating a need for buyers to appropriately assess and value their targets' ESG performance.

But are corporate buyers accounting for ESG in their M&A process today?

Not yet, according to our survey. Only 11% of respondents say they extensively assess ESG during the deal-making process on a regular basis. In fact, out of 10 elements of the corporate M&A process, ESG was the least-emphasized dimension. Many are struggling to determine how to embed the process of assessing the ESG implications of an acquisition into their M&A strategy.

Some companies are ahead on this curve. By incorporating ESG into their M&A process, they have set themselves up with an advantage in pursuing value creation opportunities and a head start in meeting their ESG imperatives.

For example, when an industrial company recognized as a sustainability leader in its industry pursued a provider of infrastructure technology, energy implications were a major consideration. The sustainability edge is an important differentiator for the industrial company's real estate customers, who own assets ranging from commercial buildings to data centers. Increasingly, those customers were demanding more environmental solutions, both to manage energy costs and to meet ESG commitments of their own. The infrastructure technology company proved to be an attractive target. It provided products for an energy-intensive and growing business segment, and it had the added differentiation of being as effective as alternatives but significantly more sustainable. This type of investment is central to the industrial company's strategy, which emphasizes offering greener solutions that are good for the environment, good for its customers, and good for business.

Similarly, a European food producer known for its healthy and environmentally friendly products used the diligence process to understand a potential North American acquisition target's performance on a range of ESG factors. The diligence determined that the target, an ingredient company, had a positive environmental profile that surpassed competitors and strong positioning on consumer health that could benefit the acquirer. But the same research also unearthed risks in the target's diversity, equity, and inclusion (DEI) profile. The diligence enabled the acquirer to clearly see how the ingredient company's strengths in sustainable packaging, in particular, could be used to appeal to its own customers and emphasized this in the value creation plan; it also revealed the specific actions that the acquirer needed to take to begin addressing the target's DEI issues on day one.

By beginning to unlock ESG as an M&A priority and a factor in delivering deal value, these companies move ahead of the majority of companies that have yet to evolve their M&A models to account for the growing sophistication of ESG. They've discovered that the traditional check-the-box approach to sustainability issues falls short. When assessing targets, they dig deeper on issues ranging from greenhouse gas emissions to DEI, and from business ethics to supply chains.

Linking corporate ESG strategy to M&A

Success in this arena begins by linking overarching corporate ESG strategy to M&A strategy. It means making sustainability a part of each deal thesis. It means using corporate priorities as a benchmark to assess each potential deal and find assets that will advance existing ESG initiatives *as well as* create economic value.

This value can come from multiple sources. For instance, in the consumer products industry, 68% of our surveyed executives see ESG's value in helping them gain share by improving their brand image to appeal to changing consumer preferences. Leaders in the energy sector, meanwhile, more commonly cite ESG initiatives for helping them meet requirements or expectations of investors and financiers to lower the cost of capital. Across industries, ESG measures can also add value by helping manage costs (e.g., waste reduction) or by helping attract and retain top talent—a particularly critical goal in today's competitive talent environment.

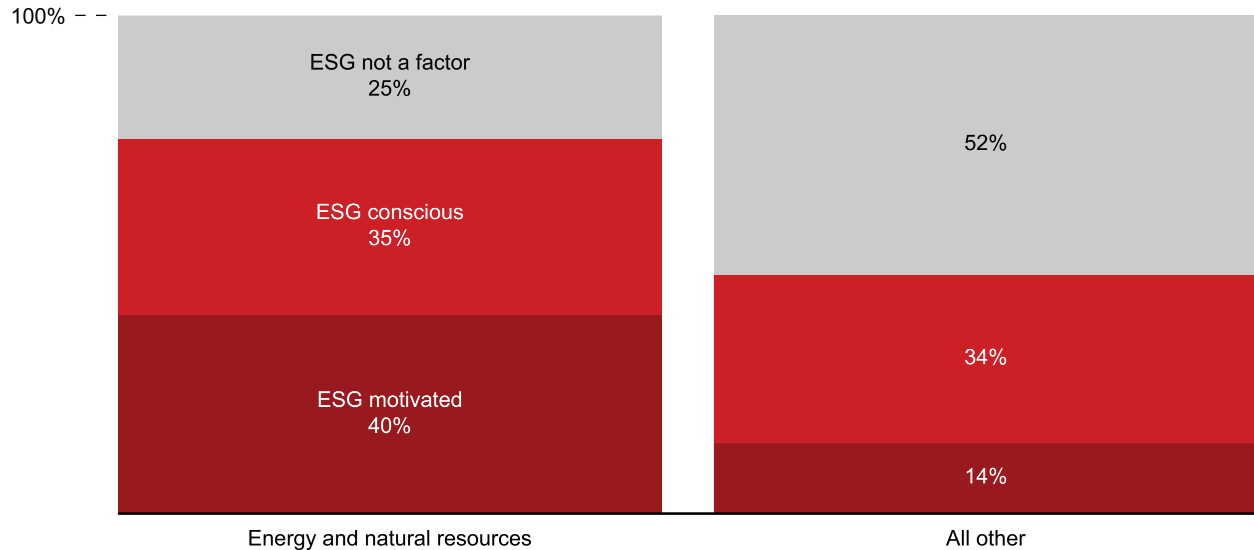
Of course, not every asset will advance an underlying ESG goal, and other business rationales will often justify pursuing a given asset, regardless of the ESG footprint. Even in such situations, performing diligence on a target's ESG record is critical to underwriting the deal. There may be real financial costs that the buyer will incur to integrate and advance the target's ESG capabilities up to the acquirer's standards, for example.

The maturity and urgency of the ESG imperative varies by industry, company, and even by specific deal. As a result, it's important that companies distinguish between ESG-*motivated* and ESG-*conscious* M&A.

ESG-motivated deals are pursued explicitly to advance the buyer's ESG agenda. Perhaps the most visible examples are in carbon-intensive industries. M&A is a driving force in the energy sector's transition to renewable sources of power. As we explore in "Energy and Natural Resources M&A: Deals to Deliver the Energy Transition," incumbents use M&A to reposition their portfolios around sustainable energy alternatives faster than they could be built organically. Meanwhile, in consumer products, the shift from animal- to plant-based proteins has prompted its own surge in M&A and partnerships. For example, to advance its mission of becoming a global leader in plant-based foods, Netherlands-based Upfield acquired leading plant-based cheese manufacturer Arivia. And other consumer goods companies are turning to M&A to address issues important to the social pillar of their ESG strategy. Consider Hershey's acquisition of health-forward food brand Lily's or the purchase by Mars of Kind and Ferrero's acquisition of Eat Natural.

Meanwhile, ESG-conscious M&A incorporates an ESG angle across the M&A value chain, even if the motivating deal thesis is not ESG related. For example, acquirers may perform due diligence to determine if a target's carbon footprint is aligned with the acquirer's sustainability goals, unrelated to the deal rationale. Companies seeking transparent and socially conscious supply chains will give extra scrutiny to a potential acquisition's vendor base. Such ESG-conscious thinking is gaining popularity across industries, though different sectors will place emphasis on different ESG topics.

Figure 1: Energy and natural resources companies are more focused on environmental, social, and corporate governance deals



Source: Bain M&A Practitioners' Survey, 2022 (N=281)

Our survey of executives found that the mix of deal type varies across industries. For example, while energy sector executives report that the plurality of deals within their industry are ESG motivated, most other industries see ESG-conscious M&A as far more relevant to their current deal makeup *(see Figure 1)*.

To strengthen their ESG efforts in M&A, we recommend buyers ask themselves several key questions that will guide the integration of ESG into the deal-making process.

- **Strategy:** What are the implications of our corporate ESG agenda on our M&A strategy? How will the board weigh ESG considerations when evaluating deals?
- **Diligence:** What are the material ESG issues for this deal, and how does the target perform in those areas? What are the potential risks and improvements to our overall ESG position and competitiveness? How do we evolve our diligence playbook to answer these questions? How do ESG considerations impact the value creation plan for this asset?
- **Integration:** How does ESG factor into our integration thesis? What governance and resourcing is required to ensure ESG objectives and value creation initiatives are met (either for improving the target's ESG performance or leveraging the target's strengths to improve our own ESG performance)? What are the specific initiatives to unlock the ESG value creation opportunities?

These questions may be tough to answer, but by asking them early, companies set themselves up to address the ESG imperative for everyone's benefit as they make the M&A moves that will boost their performance.

Hot Topics

Delivering Results in Joint Ventures and Alliances Requires a New Playbook

Alternative deals are different from typical acquisitions, and they need to be viewed with a fresh set of eyes.

By Joost Spits, Arnaud Leroi, and Dustin Rohrer

At a Glance

- In this time of accelerating disruption, many companies look beyond traditional M&A and participate in a broad range of joint ventures and alliances to access assets and capabilities.
- Frequent acquirers achieve higher total shareholder returns than their counterparts, and they are more likely to use partnerships, according to Bain research.
- Doing partnerships well requires some notable differences from M&A in approach and capability. Companies need to tailor the exploration and diligence to emphasize partner fit and trust between parties, and overinvest in creating the right governance structure and operating model.

As they grapple with the double whammy of industry turbulence and skyrocketing valuations, more companies are looking beyond traditional M&A to alternative deals, making joint ventures (JVs), alliances, and minority investments an integral part of their growth strategy.

Partnerships are a critical extension of the M&A and growth strategy. Over the past 10 years, the total shareholder return of frequent acquirers was nearly double that of infrequent acquirers, according to Bain research *(see Figure 1)*. A vast majority of frequent acquirers rely on partnerships, and they use them more frequently than infrequent acquirers.

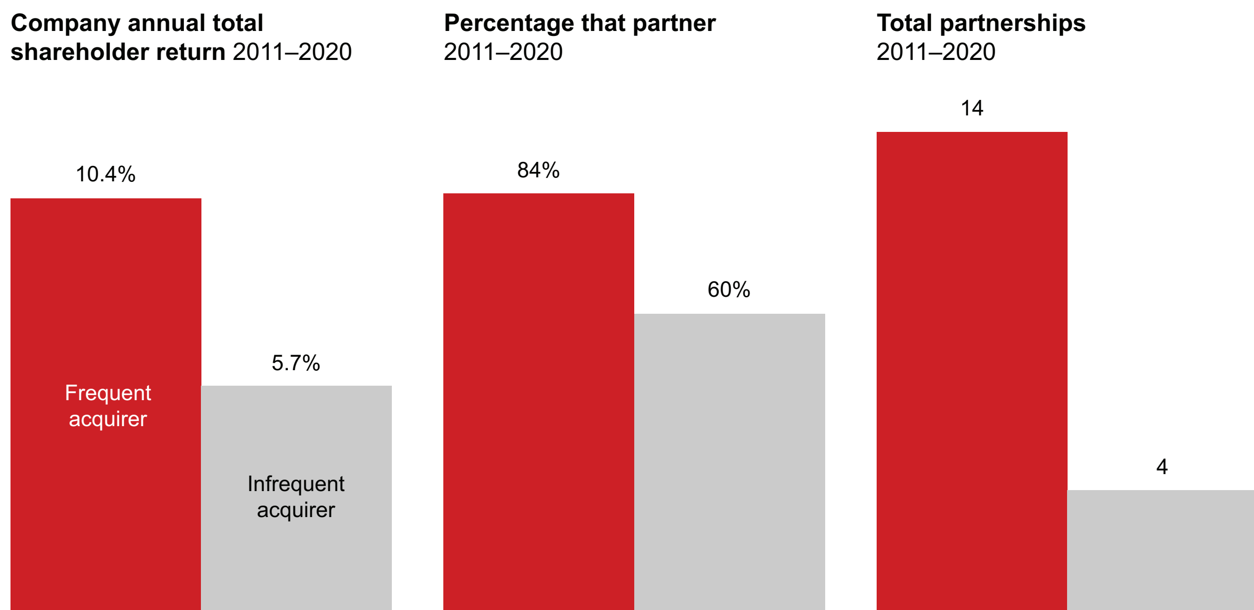
But partnerships are hard to do well. They take a lot of focus and cooperation, and they require a playbook that differs in some fundamental ways from traditional M&A. Companies need to thoughtfully address those differences.

Sharing the risk

JVs and strategic alliances have always been a way to gain access to capabilities. Now, the need has become greater as companies look for ways to get out ahead of accelerating disruption. Companies use partnerships to share risk and investment in the development of new technologies, for example. This is especially prevalent in areas such as automotive and telecom, both of which are in the midst of seismic shifts in industry standard technology.

In early 2021, telecom operator KPN partnered with pension fund APG to form Glaspoort, a joint venture to roll out fiber networks in the Netherlands. This JV allowed KPN to share the cost of building out its fiber network, and it fit with APG's infrastructure investment focus.

Figure 1: Frequent acquirers utilize and benefit from partnerships more than infrequent acquirers



Notes: Includes announced partnerships between 2011 and 2020, excluding those categorized as rumored and terminated; frequent acquirers are defined as those that made greater than 10 acquisitions between 2011 and 2020
Sources: Bain M&A value creation study, 2021 (N=1,942 companies, excluding Japan); SDC Platinum

For their part, automakers are partnering to address the challenges of electric and autonomous vehicles. General Motors (GM) and Ford both formed JVs with technology companies to manufacture battery cells and arrays for electric vehicles. GM's JV with LG Energy plans to produce Ultium battery cells for electric vehicles, and Ford's partnership with SK Innovation has a goal to produce approximately 60 gigawatt hours (GWh) annually starting in the mid-2020s.

Increasingly, partnerships are a route to addressing social and environmental challenges. In consumer products, ending plastic waste has become a core issue of sustainability. Organizations such as the Alliance to End Plastic Waste have drawn support from companies across industries hoping to combine the resources and capabilities required for delivering a solution.

The scorecard on partnerships

Most partnerships deliver value. Practitioners tell us that two out of three partnerships contributed their expected value over the past three years. Of course, that also means one out of three partnerships *failed* to deliver on expectations.

Digging deeper, we see that the difference between the winners and losers rests on execution. Clear value creation/economics and strategy are the top (and nearly equal) contributors to success, according to our survey of 281 practitioners, and a lack of these dimensions contributes to failure. Yet the top reasons for failure are execution related: poor cultural fit and a lack of strong senior management commitment *(see Figure 2)*. Execution is an ongoing process that requires up-front diligence and strong commitment over the life of the partnership. Having an effective partnership playbook can go a long way toward delivering effective execution and avoiding the fate of sinking into the bottom third of value-destructive partnerships.

Building the partnership playbook

When companies fail to achieve the full potential of a partnership or strategic alliance, it's often because they underestimate how the playbook for these alternative deals differs from the playbook required for traditional M&A.

In these M&A alternatives, there are three critical things to get right.

Tailor the exploration and diligence process to emphasize partner fit and trust between parties. Picking the right partner involves not only estimating economic value for both sides but also finding a cultural and strategic fit (in which companies can be synergistic) and working to build trust early. Specific areas of fit that can be examined during diligence include risk appetite, market perspective, and accountability preferences.

Companies with mismatched risk appetites and misaligned market perspectives on issues such as the most important segments to focus on and how to win are likely to run into conflict when new opportunities arise for the partnership.

Figure 2: Clear value creation and strategy, strong senior management, and cultural fit are key factors for joint venture and alliance deal success

Source: Bain M&A Practitioners' Survey, 2022 (N=281)

Accountability preferences, such as the level of oversight and sign-off needed for partnership activities, are another area in which it's important to reach alignment early in diligence. Finally, trust is an elusive but key component of the partnership exploration and building process.

Overinvest in creating the right governance structure and operating model. Getting a partnership's operating model and governance right up front (before signing) matters. In an acquisition, the initial operating model can be adjusted as needed post-integration. The parent company does not need to ask permission to make governance changes. In partnerships (and JVs in particular), however, making changes to the operating model after signing often turns into a complex negotiation between partners.

An effective partnership playbook can go a long way toward avoiding the fate of sinking into the bottom third of value-destructive partnerships.

The operating model considerations in a partnership are different than in M&A. There are two considerations in a partnership: the operating model of the partnership entity, such as a JV, and the operating model between the parents and partnership entity. For the parent-partnership model, companies should consider control across three dimensions: equity (share in profits/losses), investment, and management control.

There are critical questions to answer based on these dimensions. Will each parent be a portfolio manager, strategic architect, or a combination of both? Will one parent play a more dominant role in operations, or should there be an even balance between partners? What capabilities and assets will each parent contribute? What decisions need to be approved by one or both parents?

There are myriad other considerations that add complexity to the operating model. Many companies get weighed down trying to anticipate all decisions that the partnership will make so that they can build them into the operating model. Often the best path is to aim for simplicity and enable agility in the partnership.

Giving a partnership independence to make decisions while defining a few targeted areas of capability access (from one or both parents) allows the entity to grow and change with the market. Trusting a JV or alliance to learn from mistakes and grow can be the ticket to a healthy and independent value creating partnership.

Show commitment to lifetime management. Similar to any business, it's important to recognize that the future will usually be different than planned. A partnership is likely to perform well on some dimensions and underperform on others as the market evolves. To keep the partnership relevant, a periodic strategic refresh can help. This allows companies to revisit the strategic intent and align on what to stop, start, and continue based on the evolution of the partnership and market dynamics.

This is often most effective when done outside of the quarterly review process. One example of this is a partnership-focused offsite every two years, which includes both partnership leaders and some outside leaders to keep the thinking fresh. Another critical component of most partnerships is planning for the end. Initial negotiations should recognize the potential for a partnership's evolution as market dynamics shift. Should the partnership have an off-ramp after a certain period of time or when market dynamics shift? Should one or both partners have the option to acquire? What are the most likely exit rationales and trigger points? Having a clear exit plan can save both parties lots of frustration down the road.

Needed: A partnership capability

Doing this right requires being thoughtful about how to set up the internal partnership capability. Companies that maintain an active portfolio of partnerships often have a level of centralized partnership capability. This can vary from partnership knowledge management—in which guidelines, processes, and lessons learned are captured in a center of excellence—to an exclusive JV/alliance team that oversees partnership screening, setup, and management.

Companies should also be thoughtful about the overlap among the partnership team, M&A team, and business unit leadership. Several areas of the partnership process, such as screening and parts of due diligence, can build off the M&A team and playbook. But as we've mentioned, there are areas in which the JV process should be distinct.

It's also critical to be thoughtful about where business unit leadership plugs into the partnership process. If business unit leaders own the partnership once it's set up, it is important to loop them in early in the process to get input during diligence, partnership setup, and other stages.

As more companies opt for partnerships to help them deal with industry disruption and the high multiples for traditional M&A, they will discover just how different alternative deals are from typical acquisitions—and how critical it is to approach them with a fresh set of eyes.

Harnessing the True Value of Corporate Venture Capital

Companies miss out by treating corporate venture capital like traditional M&A.

By Joost Spits, Tom Wendt, and Dustin Rohrer

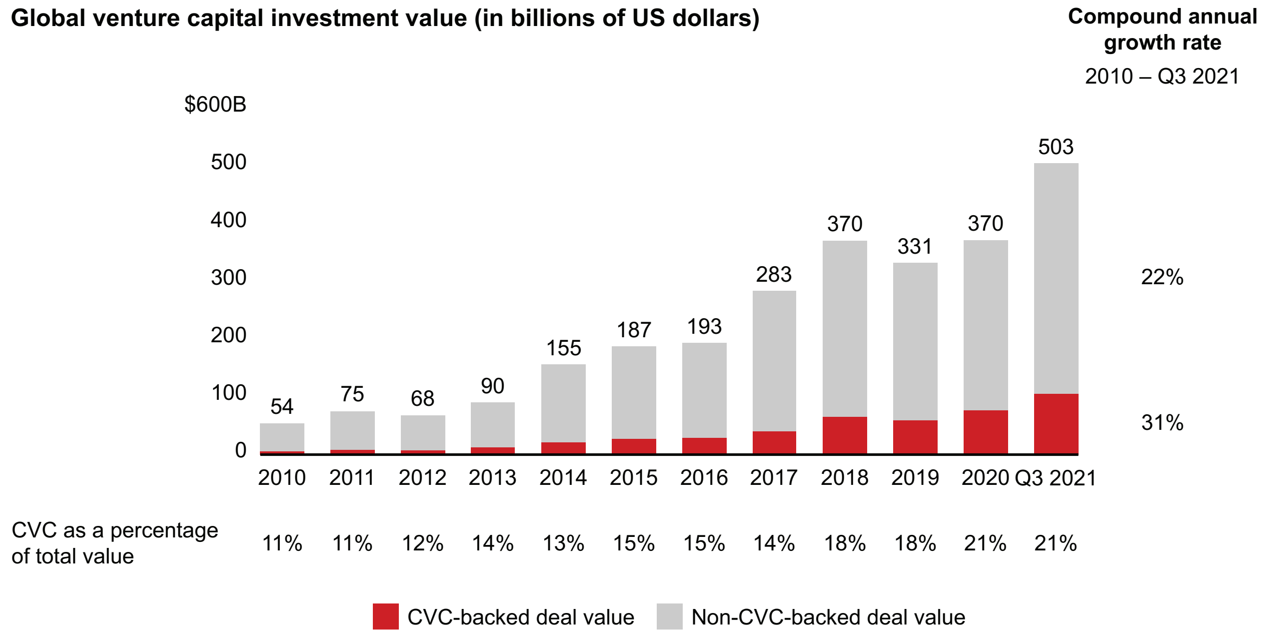
At a Glance

- Corporate venture capital (CVC) deal value has increased more than tenfold over the past decade.
- Despite its popularity, most companies are not getting the full potential value they would reap if they made early-stage CVC investments.
- By not engaging in early-stage deals, CVC investors miss out on the insights they can gain from exposure to trends several years ahead of the competition—and early-stage investment can help companies further de-risk future M&A.

As an alternative to traditional acquisitions, companies are making more minority investments, especially in the form of corporate venture capital (CVC), hedging their bets and de-risking later M&A. They're picking winning players, getting early access to companies they might want to buy, and learning more about the cutting edge of their industry.

Annual CVC volume has grown at about 7% between 2017 and 2020, with value increasing more than tenfold over the past decade as companies invest in innovations and new business models that will lead them into the future. CVC now accounts for nearly a quarter of all venture capital (VC) investing; 10 years ago, it represented only 11% *(see Figure 1)*.

Figure 1: Corporate venture capital–backed investments have grown to more than a fifth of total venture capital value



Note: Volume of CVC investments denotes unique set of corporate venture capital investments within funding rounds
Sources: Bain analysis; Crunchbase; Startup Investment Cruncher

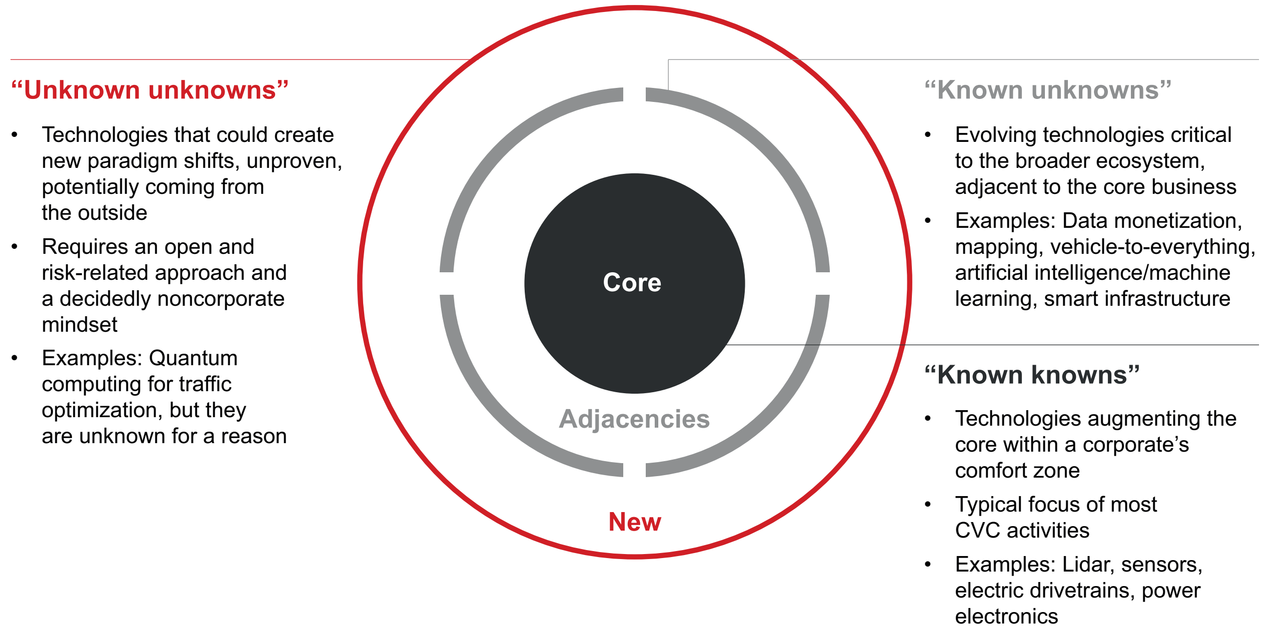
CVC ideally is deployed as a market-sensing mechanism, and at times, it can open the door for future M&A. But most companies focus on late-stage investments, treating CVC more like traditional M&A. They look for companies that they can bring into the core business right now and feel more comfortable performing diligence on those with an existing product or market fit.

While beneficial, this approach misses a critical part of the value that comes from exposure to early-stage companies.

Consider that the best venture capital firms engage in hundreds of discussions with start-ups each year. They are exposed to hundreds of business plans, and, as a result, they start to see emerging disruptive trends four or five years earlier than the general public. While a venture capital fund's team may invest only in 2 out of 100 companies they meet with, a critical part of the value lies in the insights gleaned from the other 98.

Indeed, these conversations expose companies to trends several years ahead of competitors. Venture activity often precedes market disruption, giving in-the-know investors an opportunity to actively course correct. The learnings often are about the ideas and trends that companies did not know to expect—the "unknown unknowns" *(see Figure 2)*.

Figure 2: Companies need to strike the right balance between the "known knowns" and "unknown unknowns"



Source: Bain & Company

Another big benefit of early-stage investing is that it can further de-risk future M&A. With small check sizes in the early stages, investors can buy themselves a seat at the table and watch a company or technology grow over time. If the company becomes an acquisition target, the parent company has two to four years of diligence from exposure through the early-stage investment. This brings in valuable information to diligence that can significantly de-risk the investment and integration. Compare that with the typical three- to four-week diligence.

In terms of investment required, some companies initially balk at the idea of setting up a $100 million to $200 million venture fund. While this is a large sum to commit, a VC fund's dynamics are laid out over a 10-year life cycle, making the annual investment closer to $10 million to $20 million. And if executed well, there is potential for significant rewards. Even if a fund only returns the initial investment, the company basically has a window into the future—and a way to extend and ensure its strategy.

Some companies initially balk at the idea of setting up a $100 million to $200 million venture fund.

Implications for practitioners

But getting it right isn't easy. To harness the value of early-stage investments, companies need to adjust their mindset and operating models.

CVC requires a higher risk tolerance, faster decision making, and a longer investment horizon than most corporate acquirers are accustomed to. For these and other reasons, the most successful companies set up separate VC entities that can operate independently from corporate bureaucracy and deploy a decidedly noncorporate mindset.

This mindset shift and the intelligence value from exposure to early-stage companies has several implications for the CVC operating model.

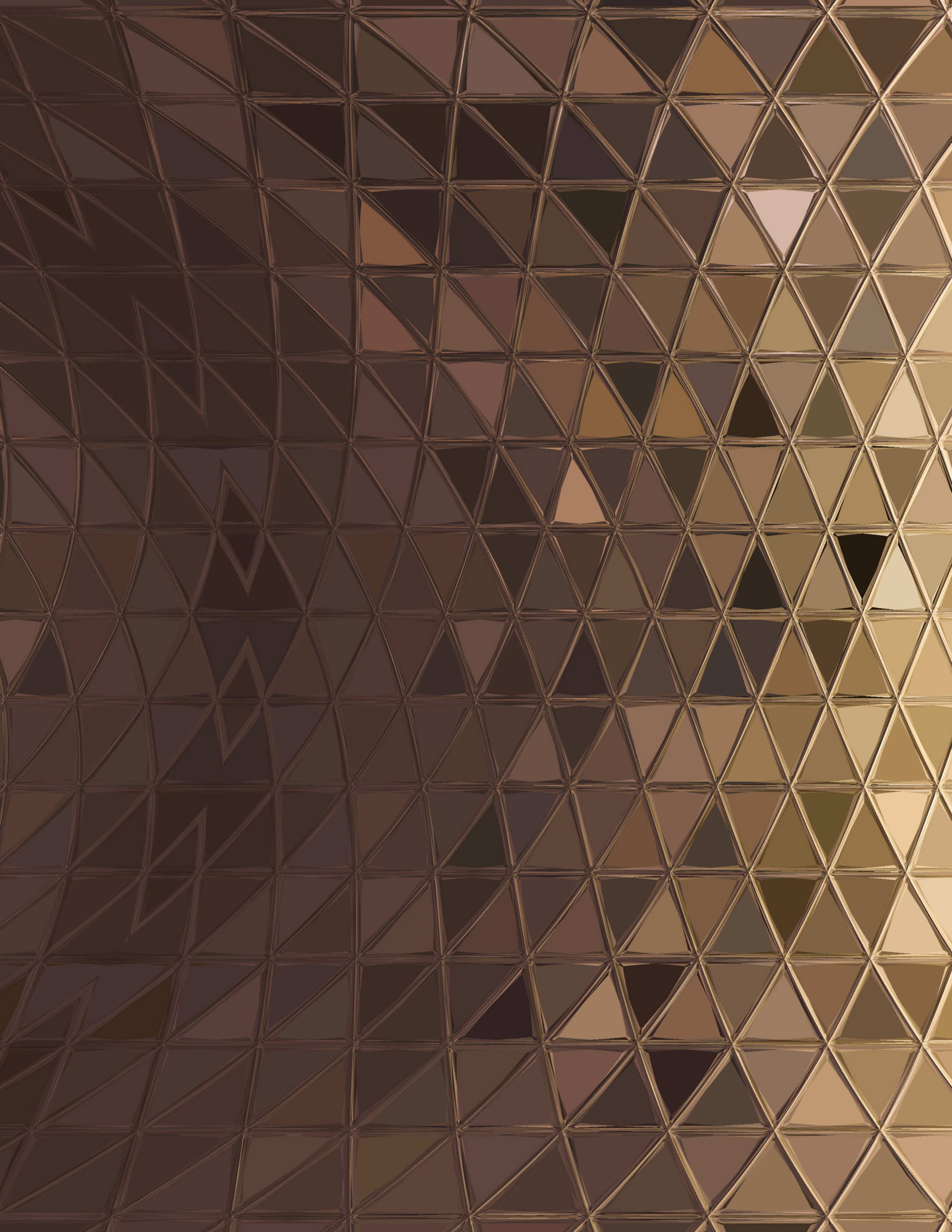
A dedicated investment team with critical expertise is the first key component for companies pursuing CVC. Bringing in individuals with deep venture capital experience will help to more quickly build the CVC muscle, and it will have a positive impact on the company's reputation in the VC world.

Venture capital is all about your network and reputation as a trusted investor. While later-stage companies look for VC investments to scale their business, early-stage companies put a premium on reputation, reliability, and long-term focus. Corporates usually have a hard time seeing the good early-stage deals because often they are not seen as a reliable investor—for instance, they come and go, they want strings attached, or something else—so they need to earn their seat at the table. That takes time and is often easier with a fund set up outside of corporate and other well-known practitioners running it.

In the hope of having access to the hot early-stage deals, some companies chose to engage in VC through a fund-in-fund model, essentially investing in a financial-driven VC fund as a limited partner. This approach might have its merits over building out a company's own VC operations, but consider it carefully since it has a lot of limitations, including high cost (management fee and carry), lack of control over where to invest, and limited visibility into new companies after year four when the fund has deployed its initial capital. Though building reputation takes time, companies that do it right see the benefits of earning their seat at the table.

The second key component of the operating model is building an operating or platform team between the investment team and the corporate parent. While recognizing the value of intelligence gleaned from early-stage exposure is easy, bringing that intelligence back to the corporate parent is not.

Companies need to capture insights in a structured way and play them back to corporate so that they are valuable and actionable. Again, some VC experience is important. This team needs to know how to work with start-ups. Its members also need to speak the language of the business as they will be the critical link that brings new insights back into the business.



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Industries

Consumer Products M&A: Creating Value by Acquiring Insurgent Brands

Large companies are buying insurgent brands to regain their growth momentum, but they need a new playbook to make them succeed.

By Peter Horsley, Allison Snider, and Charlotte Apps

At a Glance

- Small brand deals account for 75% of M&A volume among top consumer goods companies, up from less than 50% a decade ago.
- By focusing on the few things they need to get right, some large consumer goods companies have built successful portfolios through serial small-brand acquisitions that have outperformed their base business.
- Winners recognize how insurgent brand deals are unique, they tailor their M&A playbook accordingly, and they build the repeatable capabilities to do those deals frequently and successfully. Clarity on the distinctive parenting advantage is critical to unlocking value creation.
- Consumer goods companies that are frequent acquirers outperform their peers, with twice the sales growth rate, 1.8 times profit growth, and 1.2 times TSR growth than the industry average.

Large consumer goods companies have been losing out in the race for growth, and M&A is high on their agenda as they seek to reignite top-line performance. Despite overall annual market growth of 4% from 2012 to 2019, the 30 largest consumer goods companies grew less than 1%, a growth gap further widened by Covid-19. Meanwhile, prior to the pandemic, insurgent brands captured more than 30% of the growth across the categories in which they exist, despite accounting for only 3% of market share.

Growth is key to boosting shareholder returns in consumer products. Our research shows that every additional percentage point of growth acquired is rewarded by higher enterprise value (EV). That's why large consumer goods companies are buying small, high-growth brands in record numbers. These growth-focused scope and capability deals now account for 75% of M&A volume among top consumer goods companies, up from less than 50% a decade ago. This increased activity is driving greater competition for attractive assets.

With increased competition comes higher price tags. Average multiples for consumer product deals have increased from 14 times EV/EBITDA in 2020 to 16 times EV/EBITDA in 2021. And because the cost synergies are lower than they are with larger scale transactions, there is extra pressure on these deals to deliver.

Unsurprisingly, many acquirers are asking, "How do we make sure that these small, expensive deals deliver their full potential?"

Tapping into insurgent brand growth

With high-growth synergies baked into the deal thesis of small-brand acquisitions, acquirers often are disappointed with post-acquisition growth rates. We analyzed the performance of 56 insurgent brands that were acquired between 2014 and 2019 and found average growth rates slowed by 50% post-acquisition *(see Figure 1)*.

While that slower average growth still represents 15 times that of incumbent brands, it falls short of what acquirers expect. Some of the slowdown is natural as brands become larger. Much of it, however, is preventable.

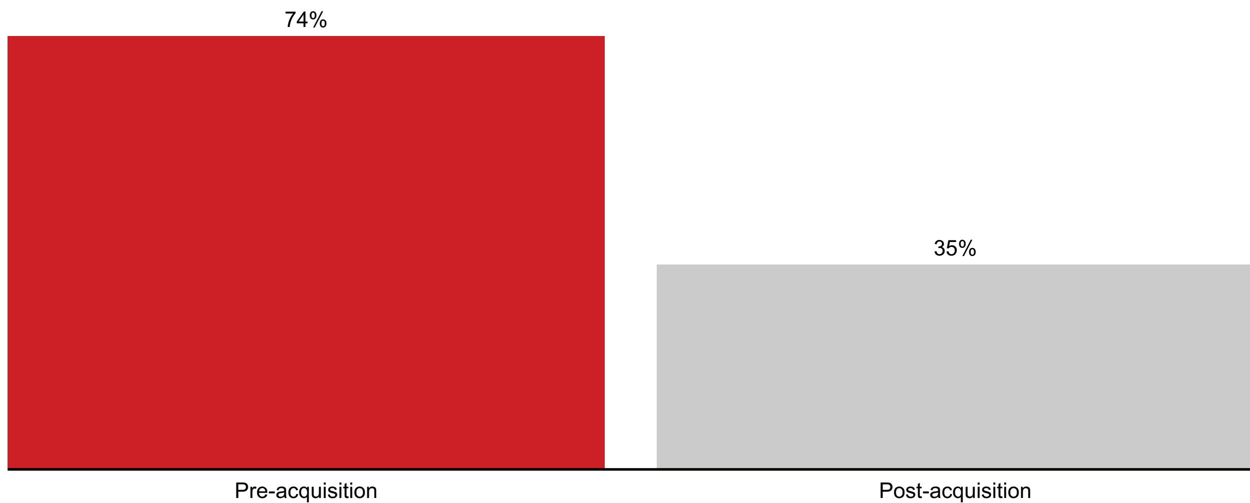
When done right, we see these deals generate substantial value and improve an incumbent's core organic growth profile. L'Oréal, AB InBev, and others have built successful portfolios through serial small-brand acquisitions that have either outperformed their base business or disproportionately increased overall growth rates relative to their size.

The successful acquirers of small high-growth assets have a tried-and-tested approach that focuses on getting a few key things right: They recognize how insurgent brand deals are unique, they tailor their M&A playbook accordingly, and they build the repeatable capabilities to do those deals frequently and successfully. We'll walk through each of these elements.

Recognizing that insurgent brand deals are unique

"We cannot treat small acquisitions as one-size-fits-all. Each has its own attributes and objectives that should inform what will work for that acquisition. Understanding what makes each deal unique is the key to successful acquisition," says Bob Chernoff, senior vice president with Acelerada, Bimbo Bakeries USA.

Figure 1: Insurgent brand growth rates slow down post-acquisition, but performance remains high



Note: Insurgent brands are those that have grown at 10 times their category average over the past five years and that have more than $25 million in sales
Sources: IRI Reviews US MULO; Bain analysis

First, the deal thesis is predicated on growth. Assessing and delivering revenue synergies is much harder than doing so for cost and requires having unique parenting advantages in place (see "Bringing Science to the Art of Revenue Synergies"). For example, for many large beverage players, access to nationwide cold-chain distribution enables acquired brands to reach new geographies and channels. Also, insurgent acquisitions often are part of a broader portfolio or platform strategy, making the deal harder to assess on a standalone basis.

Second, the acquirer needs to embrace the mission of the insurgent brand and gain a deep understanding of its growth model before it can design a suitable value creation and integration plan. Growth ambitions must balance the desire for aggressive expansion with the need for sustained brand health. Overexpanding the target's brand too quickly to benefit from the parent's distribution advantage often results in lower long-term growth. Bernardo Novick, head of ZX Ventures at AB InBev, says, "We believe strongly in founders. We are disciplined about giving small, rapid-growth businesses the breathing space to be entrepreneurial, and we have a system in place to make sure that they benefit from the scale of AB InBev where and when that becomes valuable."

Third, talent and culture are critical to any deal, but they can be hard to assess. "There needs to be a good cultural fit between the two companies informed by shared values and compatible purposes," says Chernoff.

Identifying key talent to retain is particularly critical in capability deals in which that talent forms the core of the deal thesis. “The challenge with managing the talent at insurgent brands is that the skill sets and personalities that lead to these brands breaking through and creating the early consumer connections and buzz are not typically the same skill sets and personalities that will make the most sense as those needed when the game shifts from securing new accounts, doors, and awareness to growing (and even defending!) the footprint you have,” explains Glenn Pappalardo, managing director with JPG Resources. “Creating and operating are two very different disciplines. Most people who are extremely good at one are not extremely good at the other.”

Understanding the longer-term intentions of the founder and how critical they are to the success of the business is key. Broadly communicating the reasons for the acquisition and the integration plan going forward helps avoid unwanted talent churn.

Finally, insurgent brand deals often are more complex and don’t tend to follow a typical deal process. For example, a small brand’s shorter track record means that performance data availability may be limited (and often in untracked alternative channels), requiring creative diligence techniques and data tools to compensate, such as Pyxis for online performance analytics. Increased competition from other buyers, such as private equity, and the availability of other forms of investment, such as initial public offerings and corporate venture capital, have led to higher multiples and therefore the need for greater conviction to make a deal work.

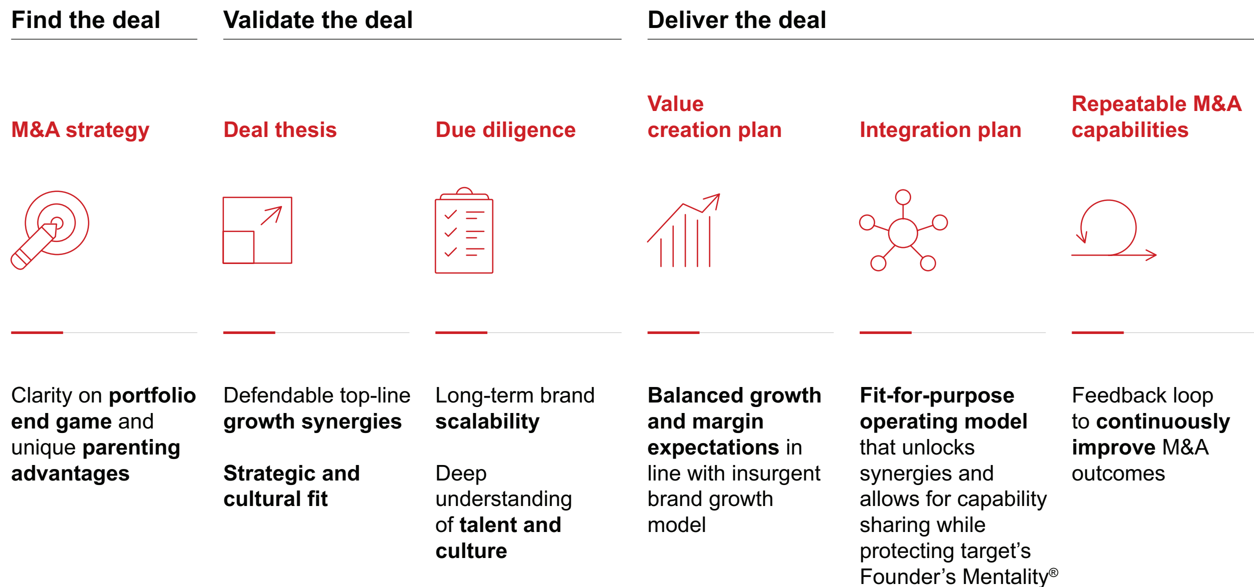
Tailoring the M&A playbook

To account for these differences, successful acquirers have tailored their traditional M&A playbook across each element of the value chain *(see Figure 2)*.

M&A strategy must be grounded in a future-back view of how the sector will evolve in order to determine the right portfolio play, assess a target’s potential to meet new consumer needs, and defend against emerging competitors in the long run. A few years ago, Hershey identified the disruption that reduced sugar and healthier eating habits would have on its business if it didn’t respond. The company set a larger vision for what Hershey could offer consumers by forming a better-for-you snacking platform alongside its core business, anchored with the acquisition of Amplify Brands, which has since bolstered its growth. Other confectionary players have reached similar conclusions. Recently Mars bought Kind, and Ferrero purchased Eat Natural.

The deal thesis should be tailored to the uniqueness of insurgent brands. Clarity on the distinctive parenting advantage is critical to unlocking value creation. Top-line growth synergies and expectations for capability transfers need to be defendable, and costs associated with scaling small-brand supply chains must be considered. The target’s culture, purpose, and strategic values in areas such as environmental, social, and corporate governance must fit with the acquirer’s own (see “The ESG Imperative in M&A”). There should be a clear plan for the founder’s future role as well as what should be integrated and what should be kept separate.

Figure 2: Our insurgent brand M&A playbook is tailored to account for the uniqueness of these deals



M&A strategy	Deal thesis	Due diligence	Value creation plan	Integration plan	Repeatable M&A capabilities
Clarity on **portfolio end game** and unique **parenting advantages**	Defendable top-line **growth synergies** **Strategic and cultural fit**	Long-term brand **scalability** Deep understanding of **talent and culture**	**Balanced growth and margin expectations** in line with insurgent brand growth model	**Fit-for-purpose operating model** that unlocks synergies and allows for capability sharing while protecting target's Founder's Mentality®	Feedback loop to **continuously improve** M&A outcomes

Note: Founder's Mentality® is a registered trademark of Bain & Company, Inc.
Source: Bain & Company

Due diligence must stretch beyond the traditional financial boundaries to test a target brand's long-term growth potential and scalability. Among the questions to answer:

- Is this a true consumer need or just a fad?
- Can the brand stretch into adjacent markets?
- How strong are the target's commercial capabilities?
- What competitive threats exist, particularly among newer emerging brands?

And at a time when so many deals rely on the ability to retain talent, the diligence needs to rigorously assess talent and cultural issues, identifying departure risks early (see "Reimagining Talent in M&A").

The value creation plan should set realistic growth expectations to avoid the risk of overpaying and overstretching the brand to compensate. Acquirers need to apply the insurgent growth model, which includes an emphasis on driving velocity and not just distribution. This requires planning for how capability transfer can improve the base business—and what it will take. And margin expectations must be managed, recognizing that there may be higher initial costs and that price pressures will come into effect as distribution scales.

The integration plan should ensure that the resulting operating model protects and even strengthens the target's Founder's Mentality® while unlocking parenting advantages. "The biggest learning is the need to be very thoughtful in the approach to integration, making sure to leverage the skills and benefits of the larger company without negatively impacting the nimbleness and entrepreneurial spirit that are key to the growth and authenticity of the acquired brand," explains Chernoff. "At times, that means very limited integration and keeping a dedicated leadership team in place for the business. In other instances, this means integrating elements of the business where they can benefit from our capabilities while locking in key talent early enough to ensure a smooth transition."

Building repeatable M&A capabilities

Consumer goods companies that are frequent acquirers outperform their peers, with twice the sales growth rate, 1.8 times profit growth, and 1.2 times total shareholder return (TSR) growth than the industry average. The benefit to building repeatable M&A capabilities is even more true for acquirers that are generating a regular flow of small deals. "Over the past six-plus years, we have developed a proprietary set of metrics to assess potential acquisitions based on their stage of growth and their business model. Learnings from other deals we've done is part of what makes us a successful investor," explains Novick.

Incumbents need to apply an always-on approach to scanning the market and deal flow activity. "Consumer goods companies that do this well create the deal flow," says Pappalardo. "They build relationships with promising insurgents long before they even know they want to sell." And they can quickly assess a target's potential fit, often with limited data. This requires tapping into alternative data sources, building a broader ecosystem of experts, and developing creative primary research solutions. Post-deal, protecting the asset from a large company's bureaucracy requires running lean, targeted, decision-driven integrations rather than traditional broadscale M&A processes.

Given that many insurgent deals are part of a series of acquisitions to build a broader portfolio, creating those repeatable capabilities pays off over time. Winning acquirers establish learning loops and regularly reassess to improve their M&A performance.

Ultimately, at a time when the growth gap is widening, incumbent brands need small-brand deals to recapture top-line growth and boost TSR. While challenging to get right, these acquisitions can deliver substantial value. Success requires a clear understanding of what makes insurgent assets unique; an updated M&A playbook; and new, repeatable capabilities.

Industries

Retail M&A: Keeping Pace with the Rise of Quick Commerce

Companies are swiftly pursuing deals and choosing partners to get on the quick-commerce express train.

By Vincent Vandierendonck, Sam Rovit, and Mike Parshley

At a Glance

- Consumer interest in rapid delivery of food, groceries, and other goods has risen dramatically since the beginning of pandemic lockdowns.
- Emerging quick-commerce players and incumbent retailers are both turning to M&A and partnerships to gain the capabilities needed to compete.
- Established retailers can help quick-commerce companies scale, and they can provide extensive existing customer bases and core retail capabilities, such as product assortment, that will attract and retain customers.
- Partnering with or acquiring quick-commerce companies provides incumbent retailers with hyperlocal delivery strength, established driver networks, and delivery logistics capabilities outside of the typical retail wheelhouse.

To see the future of retail, step into almost any elevator in China, where you're likely to stand shoulder to shoulder with delivery folks bearing meals, groceries, personal care products, and virtually anything else you can think of that can be ordered online and transported on a scooter to your door in 30 minutes or less.

In China, where e-commerce penetration is around 30% in almost all categories—well ahead of the US and Europe—foot traffic to retail outlets is down 10% compared with pre-pandemic levels. Many believe that traffic is not coming back as consumers shift their buying behavior, opting for the super-fast delivery of goods in what is now being referred to as "quick commerce." Meituan, China's pioneer in quick commerce, makes an estimated 32 million express deliveries every day, relying on millions of drivers for around 670 million active users.

Now part of daily life in China, quick commerce is taking root in the rest of the world as consumers become accustomed to—and then demand—increasingly short delivery times for a widening array of purchases. To build out the businesses that will serve this market, funding for quick-commerce delivery providers is at record highs across the globe, with investments now coming in at a rate that is more than eight times the 2020 level.

As businesses iterate on operating models, consumer value propositions, and new strategies to serve the quick-commerce demand, many are finding that M&A is the fastest way to develop the capabilities they need to stay competitive. The year 2021 brought with it a flurry of deals and partnerships in quick commerce.

Doordash bought Finland-based delivery app Wolt for $8 billion to expand its global reach. Wolt contracts out couriers to deliver takeout, groceries, and other goods to customers in 23 countries mainly throughout Europe. Germany-based Delivery Hero acquired food and grocery delivery platform Hugo to expand into Central America. Boston-based Drizly and 7-Eleven teamed up to deliver alcohol in under an hour. Kroger and Ahold-Delhaize announced partnerships with Instacart that build out both grocers' 30-minute delivery options. Meanwhile, Carrefour invested in Cajoo while Tesco and Gorillas partnered to offer 10-minute delivery in London.

As these deals get inked, traditional retailers and emerging quick-commerce companies both are looking for a path to scale economics. Undoubtedly, the economics are more attractive in dense urban settings, but quick commerce is beginning to reach suburban consumers, too. As long as the per-order economics are close to breakeven on average, scale players are likely to have a viable model in time, fueled by additional sources of value to fund the gap. This includes data monetization, ad sales on digital media, partner subsidies/vendor funding, and robust private label offerings—similar to the path that Amazon, Alibaba, and Instacart have taken.

The pressure to provide retail customers with near-immediate convenience is here to stay and will expand across verticals and customers. Today's model focuses on the urban, young, and affluent customer segments, not because of a lack of broader customer demand but because of limited supply. We've seen this story play out in retail before. Two-day shipping and online grocery delivery were originally targeted at much the same customer segments. Now they are table stakes, with broad appeal across geographies and customer segments.

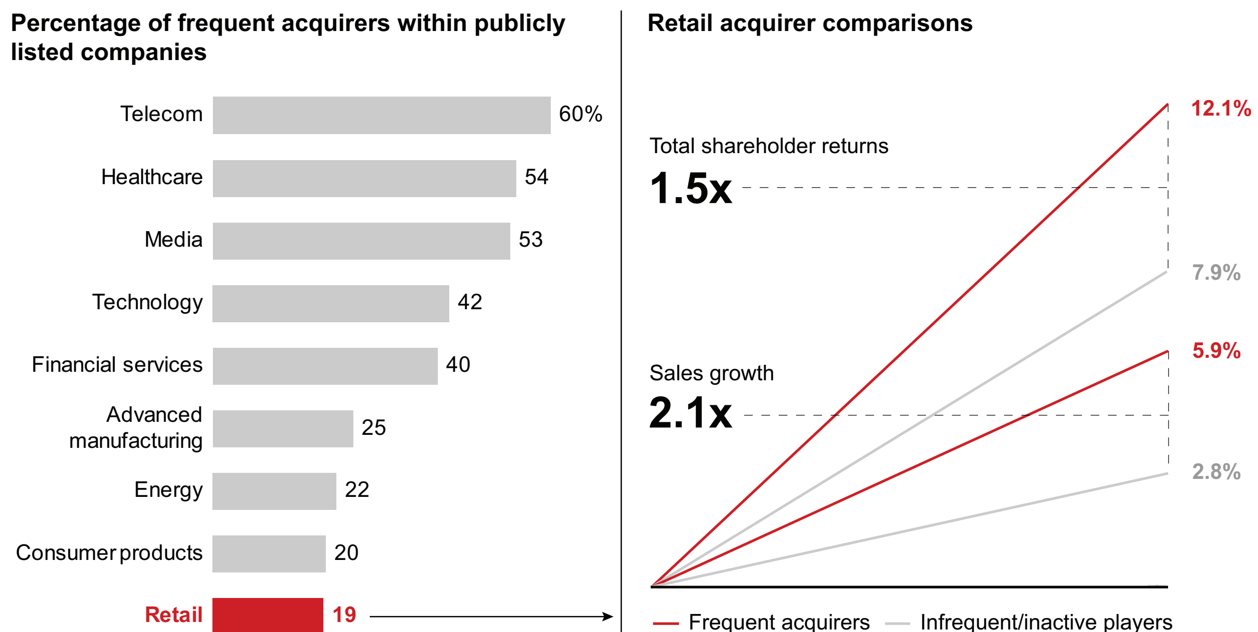
For both the emerging class of quick-commerce players and existing retailers looking to evolve with changing customer expectations, M&A and partnership expansion should be at the top of the executive agenda.

For new entrants, growth means expanding geographically as fast as funding is available, optimizing assortments, and building a network of both couriers and customers. Winners will be those with a loyal fleet that can deliver (almost) anything to anyone at any time. Established retailers can help new entrants accelerate customer acquisitions and product-portfolio perfection, and they offer access to the benefits of scale and experience.

Meanwhile, traditional retailers can look to quick-commerce partners as the fastest path to establishing delivery capabilities that truly wow their customers. Partnering for or acquiring these services will provide hyperlocal delivery strength, with established courier networks and delivery logistics capabilities outside of the typical retail wheelhouse—not to mention access to the agility that these young companies bring to the table.

The link between M&A and corporate performance is especially strong in retail. Our research has found that retailers with a track record of frequent and material M&A significantly outperform infrequent or inactive buyers (see *Figure 1* and "Bain's Bedrock Beliefs on How to Create Value from M&A").

Figure 1: One in five retail companies is a frequent acquirer, and these organizations see growth benefits as a result



Note: Frequent acquirers are defined as those that made greater than 10 acquisitions between 2011 and 2020
Source: Bain M&A Success Study, 2020

The best companies use deals to test and learn in the early innings, positioning themselves for success as the market evolves. The institutional insights they gain will be critical as quick commerce expands across geographies and as the number of players rapidly multiplies. Not all quick-commerce providers will survive. We do expect meaningful consolidation, but we also see room for several players to win over time.

Winners in this new model will focus on three areas:

- **Provide a differentiated offering.** Leaders will find their niche and create their strategy around it. This can be assortment or private label. It can be price, quality, or reliability. Or it can be employee loyalty or customer personalization. Having a clear view and maintaining focus on the company's sweet spot will be critical for success.

- **Leverage data.** As these new offerings evolve, companies that use their data to rapidly understand the changing environment will be best positioned to win. Strong performers will leverage data across multiple dimensions—customer facing, supplier facing, and logistics, for example. Data can help retailers locally tailor inventory and product offerings. It also can be sold to suppliers for an additional source of revenue. And data can be used to optimize routing, batching, and delivery economics.

- **Accelerate M&A.** As we mentioned, leaders will use M&A to find and integrate new capabilities, whether through outright acquisitions or alternative approaches such as minority investments and partnerships. This will require frequent and continuous dealmaking as the market swiftly evolves and grows. Retailers should plan for opportunities long before specific deals are on the table. That means aligning the logic for target screening, building a pipeline of priority targets with customized deal theses, and cultivating relationships with those high-potential targets.

Partnerships, in particular, will give incumbents speedy access to new capabilities while providing optionality in a world where many new disrupters are still emerging. Indeed, the long-term winners in quick commerce might not yet be in sight, but the best companies know that's not a reason to delay entering the race.

The best companies use deals to test and learn in the early innings, positioning themselves for success as the market evolves.

Industries

Healthcare M&A: Record-High Valuations Are Forcing Acquirers to Get Creative

Across all five healthcare sectors, buyers are finding new ways to achieve focus, scale, and specialization.

By Jeff Haxer, Ben Siegal, Kai Grass, and Sarah Yanes

At a Glance

- Healthcare M&A volume was up 16% in 2021, and value rose by 44% after last year's steep decline. Across the five sectors, deal value totaled $440 billion in 2021, with multiples at an all-time high.
- More companies are underwriting the revenue synergies that are becoming increasingly critical to justify high valuations. They are pursuing more cross-border deals, buying new capabilities, and continuing to acquire both carve-outs and full companies.
- Activity varied by subsector, with pharma companies purchasing to boost top-line growth and add to their portfolios and medtech companies pursuing deals that give them category leadership.
- While deal volume dropped among payers, the deals that did occur added scale and platforms or diversified offerings—and in a growing trend, payers bought providers to better control members' costs.

Strategic healthcare M&A rebounded in 2021 from a down year in pandemic-ravaged 2020, with volume up 16% and total deal value rising by 44%, to $440 billion.

The year 2021 brought with it a return to pre-pandemic trends across all five sectors: pharmaceuticals, medtech, payers, providers, and healthcare services. What's different this time, though, is that the cost of acquisitions has become dramatically more expensive in most areas, with deal multiples reaching the highest level in decades. The median healthcare deal fetched 20 times forward-looking enterprise value (EV)/EBITDA in 2021, a full five turns higher than in 2019, the last time that volumes were as high.

Paying for these inflated multiples requires companies to get more creative in their deal theses and focus on better execution to deliver on deal value. Here's what the best acquirers are doing.

- Healthcare acquirers are increasingly thinking about revenue synergies in their deals. It's a trend that is happening in other industries, too. Across all industries, the percentage of large deals (that is, deals greater than $1 billion in value) with announced synergies that included revenue synergies rose from 4% in 2016 to 16% in 2021.
- Successful healthcare companies are not shying away from looking outside their borders for growth.
- Many companies are continuing to opt for carve-out acquisitions (vs. full-asset acquisitions), which maintained their decades-long average of 30% to 40% of total transaction volume.
- The number of transactions aimed at adding a new capability have risen dramatically from 11% of healthcare deals among the top 250 largest transactions across industries in 2017 to 18% in 2021.

Overall, 2021 saw a continued push for focus, scale, and specialization across all healthcare sectors. This is most evident in the announcements by General Electric and Johnson & Johnson to split up to form separate entities, each with a standalone healthcare business, or GlaxoSmithKline's recent decision to split into pharmaceuticals and consumer healthcare businesses. Those companies hope to replicate the successful separations of companies such as Abbott/AbbVie and Baxter/Baxalta, which created bespoke strategies, financials, and organizations tailored to their standalone equity stories.

We'll show how pursuing deals for focus, scale, and specialization plays out in each of the five healthcare sectors.

> Midcap pharma companies took a page from their large-cap competitors' playbooks and went after large acquisitions to broaden their access to new products and therapeutic areas.

Pharma: Midcap companies get in on the action

Pharma continues to be the healthcare sector with the largest M&A transaction value and volume. After experiencing declining volumes and values during the early months of the pandemic, pharmaceutical companies saw big gains for both in 2021.

Companies continued using M&A to boost their top-line growth and add products and therapeutic areas to their portfolios. For example, Roche bought GenMark Diagnostics for $1.8 billion to increase its testing and diagnostics business. We expect this trend to continue for as long as the market rewards pharma companies for top-line growth more than it does for profitability.

In 2021, midcap pharma companies took a page from their large-cap competitors' playbooks and went after large acquisitions to broaden their access to new products and therapeutic areas. Among the activity, examples include Horizon Therapeutics' more than $3 billion acquisition of Viela Bio to continue to expand its position in autoimmune diseases, Jazz Pharma's $7.2 billion acquisition of the leading cannabinoid-based therapeutics company GW Pharmaceuticals to enter the CBD therapeutic game, and Servier's $2 billion carve-out purchase of Agios Pharmaceuticals' oncology business to enhance its position in that area.

Given the rising importance of specialty drugs and biosimilars as well as a general sense that the best way to stay independent is to reach sufficient scale, we expect small-cap and midcap pharma companies to continue to play a significant role in the market going forward. These small caps and midcaps are testing the waters with small acquisitions and developing playbooks to consider potentially larger deals down the line.

Medtech: Category leadership comes roaring back alongside investments in digital

After a down year for medtech in 2020, both values and volumes saw increases in 2021, though no return to 2019 levels.

Acquirers are going after deals intended to give or enhance category leadership positions. Steris's acquisition of Cantel Medical for $3.6 billion expands its offerings to dental customers. Boston Scientific's carve-out purchase of Lumenis is another example—the deal strengthens its position in urology. Meanwhile, Thermo Fisher Scientific's attempted acquisition of Qiagen is an example of a medtech with a diagnostics business that grew significantly during Covid-19, prompting it to try to increase its leadership positions via acquisition.

In the same vein, some medtech companies divested or spun off noncore categories to focus on those in which they could become leaders while also freeing up cash flows and driving up aggregate top-line growth percentages. For example, Zimmer Biomet's spin-off of its spine and dental businesses was done to drive higher growth and focus in the remaining Zimmer Biomet portfolio.

Finally, medtech companies continue to prepare for their uncertain access to operating rooms in the post-pandemic world. As they do, they are investing in the digital and point-of-care technologies that will keep them critically relevant to physicians. Baxter's $10.5 billion acquisition of Hillrom is intended to drive a more connected care experience for patients. Another example is Stryker's OrthoSensor purchase for an undisclosed amount; OrthoSensor's technology enables doctors to receive feedback on how the knee is performing in the patient's body post-surgery.

Payers: Muted deal volume recovery, with a focus on scale and access to new populations

Payer transaction volume fell about 30% after increasing from 2019 to 2020. Those deals that did occur in 2021 tended to focus on adding scale and platforms, or diversifying offerings to different member populations.

For example, Centene's $2.2 billion purchase of Magellan Health added new members and enabled the company to enter behavioral health in a meaningful way. The deal also gave Centene a specialty pharma provider for Medicaid. Cigna's Evernorth division bought MDLive for an undisclosed amount, adding scale to its telehealth offerings. Evernorth is taking advantage of the lasting effect of Covid-19 lockdowns: More members are now comfortable with telehealth options.

In another continuing trend, payers bought providers in an attempt to better control members' total costs. Humana completed its $5.7 billion purchase of Kindred at Home and also bought One Homecare Solutions for an undisclosed amount. Meanwhile, Walgreens continued its push into the provider space with its $5.2 billion investment in VillageMD, with the goal of opening an additional 600 primary care clinics in its stores. Should these strategies prove successful, we anticipate additional transaction activity that crosses the payer-provider line. And with strong profit pools and cash positions, we expect to see deal activity accelerate across the payer landscape in 2022.

Providers: M&A rebounds, with deal activity focused on continued consolidation

The impact of Covid-19's associated margin pressures on providers led to declines in M&A volume in 2020. Provider M&A transaction volumes and values both recovered in 2021, exceeding pre-pandemic levels. Likewise, transactions with financial sponsors in the sector increased as well, with a 43% increase vs. 2020.

As it was pre-pandemic, one of the main catalysts for transaction volume in this sector in 2021 was the consolidation of healthcare systems to build scale and cost efficiencies. The announced merger of Brazil's Hapvida with NotreDame Intermédica for about $9 billion and Intermountain's merger with SCL Health are two examples of consolidation in 2021. Given the ongoing margin pressures on providers, we anticipate continued deal activity aimed at building scale.

Healthcare services: Opportunistic deals to capitalize on outsourcing

In healthcare services, companies used creative deal theses with the objective of entering new markets. There were multiple scale transactions among providers of outsourcing services to pharma companies, for example. The goal is to enter the pharma market without becoming a direct marketer and developer of pharmaceuticals. Thermo Fisher Scientific bought PPD for $17.4 billion to expand its clinical research outsourcing offering, and Danaher acquired Aldevron for $9.6 billion to add mRNA manufacturing to its life sciences portfolio. We anticipate M&A activity for healthcare services companies will remain robust in 2022 and beyond as they get more creative in an effort to reap the value of high-multiple transactions.

Spotlight on Europe: A growing share of global healthcare deal value

Unlike other industries, in which cross-border deals are becoming less popular, healthcare is experiencing a steady rise in deals that stretch across geographies. And nowhere is healthcare cross-border deal value as high as it is in Europe.

After two years of declines, transaction value from corporate healthcare acquisitions of European targets increased by 224% in 2021. The European pharma sector used M&A to fill pipelines and boost top-line growth. That was the case with Sanofi's purchase of Translate Bio and Roche's acquisition of GenMark Diagnostics, for example.

In medtech, Tecan bought Paramit, and Philips acquired Capsule, with both deals reflecting the multiyear global trend of pursuing category leadership through M&A.

Covid-19's ongoing impact on elective surgery has led to consolidation among Europe's providers, a trend that is likely to continue for the near term on a domestic basis in nursing homes, mental health, hospitals, and ophthalmology, with medium- to long-term consolidation across geographies possible in nursing homes.

Healthcare services saw high deal activity in contract development and manufacturing organizations (CDMO), especially CDMOs with a differentiated or specialized offer. Icon's $12 billion purchase of PRA Health Sciences is an example of an acquirer adding scale and breadth by buying a differentiated outsourcing provider. Pharma and medtech companies will continue to look for outsourcing, both to secure supply continuity and to absorb demand peaks for fill and finish services in vaccines, for example, providing a tailwind for CDMO deal volume.

What does it all mean?

Healthcare companies will continue to look to M&A to spur growth across all sectors. Should deal multiples remain at 2021 levels, companies will be forced to make the deal economics work by relying on more creative deal theses with value drivers that have key implications.

When carefully devised and planned, a creative deal thesis can deliver tremendous value to acquirers. But that upside is not risk free. With a creative deal thesis comes increased integration risk. For example, achieving the value of a transaction may require the acquirer to behave in a way that is counter to its current norms—for instance, if a cost-driven organization needs significant revenue synergies. Acquirers need to anticipate these added challenges.

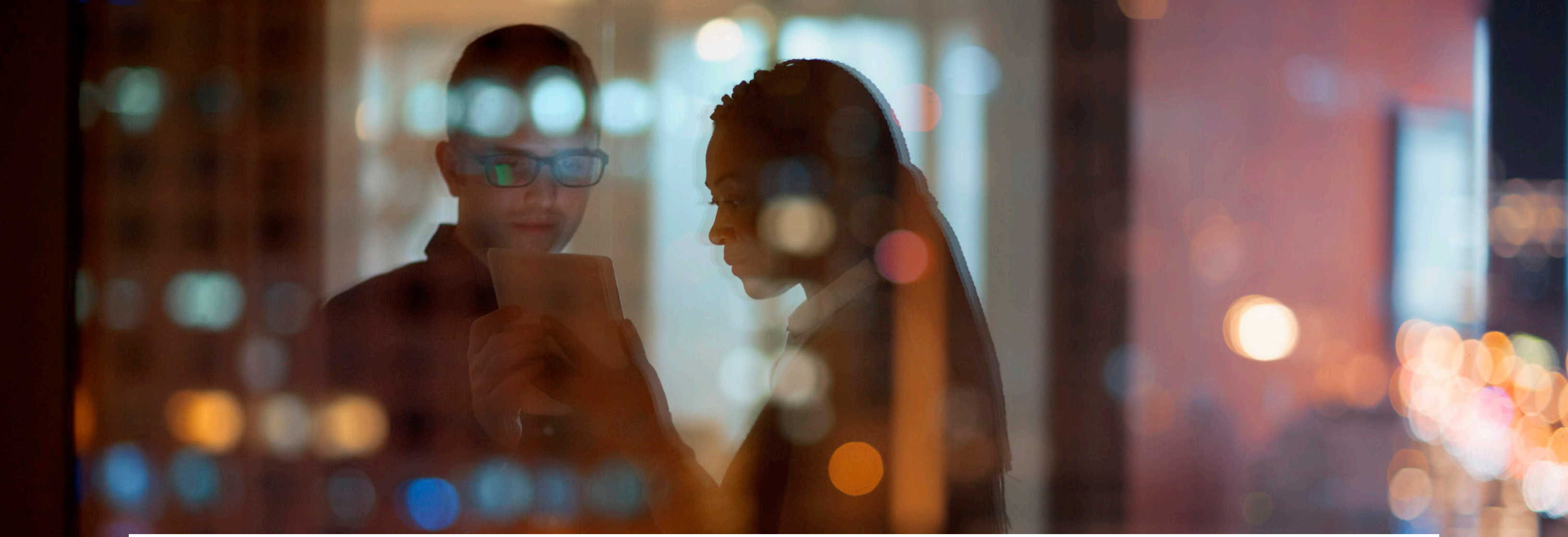
That means using diligence to pressure test a bespoke deal thesis and outlining what must happen for the deal to add value. It is unlikely that cost synergies alone will suffice to make the deal economics work in the current environment. Yet revenue synergies are inherently riskier because they are more reliant on market conditions and customer behavior. Also, as revenue synergies become more significant, so does retention. An increased focus on people and cultural integration will be important for realizing deal value.

For companies acquiring a carve-out, the first order of business is to stabilize and then prepare to exit transition service agreements (TSAs)—both objectives require significant time and focus for the first 90 to 120 days post-close. Companies need to plan accordingly with cost and revenue synergies, prioritizing their limited bandwidth on the highest value areas.

The best companies take the time to articulate where, how deep, and how quickly to integrate different parts of the organization. They are clear about where integration is crucial for achieving the value of the deal (e.g., combining salesforces to achieve revenue synergies) vs. where a slower integration approach may work (e.g., combining sales and operations planning may be more valuable after systems integration is complete).

Companies that buy a capability or talent pool need to think long and hard before changing any part of that organization; many acquirers learn that the best course of action is to leave that group alone. Another critical step is to overinvest in the handoff between diligence and integration planning so that the focus is on key value drivers during integration.

In a market with record-high deal multiples and with companies leaning in to make the economics work, every item in the M&A capability toolkit is critical. That's why the best companies work to clearly understand where they excel in M&A capabilities and where they need to improve to boost the odds of successful deals.



Industries

Technology M&A: How Hyper Acquirers Integrate New Capabilities

Big tech's thirst for small deals means finding ways to realize a given deal's value while also integrating a new deal that closes maybe two weeks later.

By Adam Haller and Chris Johnson

At a Glance

- Major technology companies acquire dozens of small companies, with deals costing less than $500 million representing about 96% of all big tech M&A, requiring an efficient approach to integration.
- The best acquirers do deep customer and product diligence during pre-signing to better understand the value available in a target and how it can add to the existing business. This allows them to create granular cost and revenue synergy plans pre-close that they can execute from day one.
- More than 75% of the tech M&A practitioners we surveyed felt that talent retention is now more difficult than it was three years ago. The best tech acquirers go beyond retaining talent by finding ways to grow the target's talent base even faster than it could on its own.
- With some tech acquirers doing as many as 30 deals per year (or one every two weeks), the best tech acquirers build an integration chassis that will allow them to streamline the integration process and adapt the approach to focus on value creation in each unique deal.

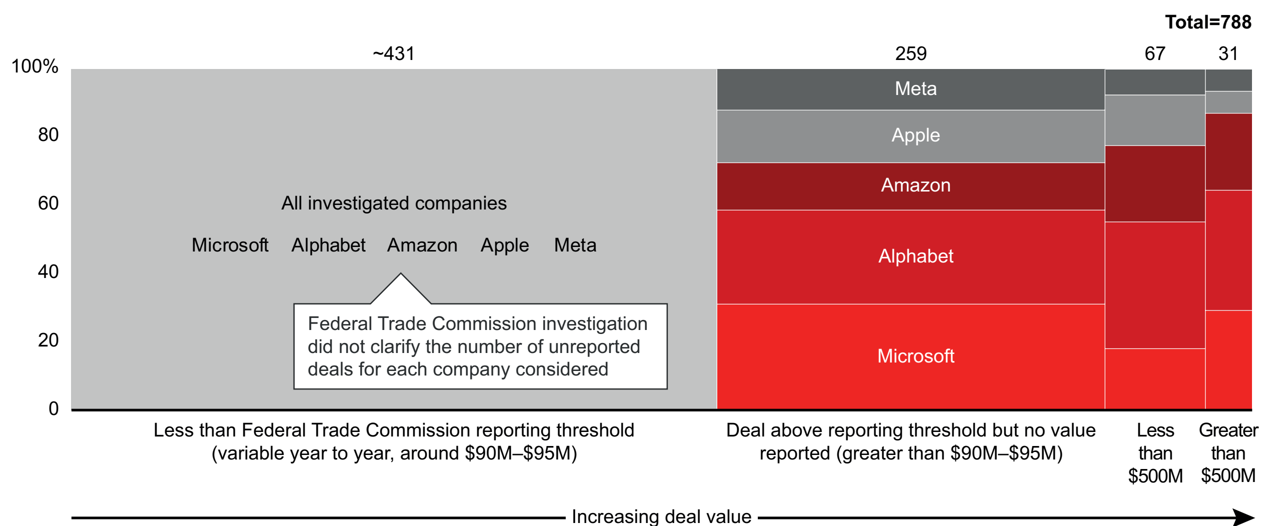
When Microsoft acquires Nuance Communications for $19.7 billion, it makes headlines. But what's become far more common is when a tech giant such as Microsoft pays undisclosed amounts for significantly smaller companies such as TakeLessons or Clipchamp. Major tech companies buy dozens of small targets each year, usually with the goal of adding valuable capabilities that will improve their core business or seed new Engine 2 businesses. It's to the point that deals costing less than $500 million now represent about 96% of all big tech M&A *(see Figure 1)*.

While these deals come with the promise of access to the talent and cutting-edge innovation needed to help acquirers grow and lead the next wave of industry transitions, delivering on that promise isn't always a sure thing, especially as some tech companies are acquiring more than 30 companies a year. Too often, the aggregate focus required to address this volume of deals causes great possibilities to give way to a distracted base business, cultural tensions, and talent attrition.

Big tech companies now face the dual challenge of realizing the deal value in any given capability deal while also building a repeatable, high-velocity integration competency to manage the steady flow of deals coming in at a rate of one every two weeks. Some companies are surfacing as leaders in this high-stakes challenge of successfully integrating a steady flow of capability acquisitions.

Figure 1: Big tech companies have predicated their M&A strategy on large numbers of small deals

Deal count by deal value and acquirer (2015–2021)



Notes: 2020 Federal Trade Commission investigation into unreported deals by these companies revealed 616 deals from 2009 to 2019; similar rate of dealmaking assumed to estimate activity from 2015 to 2021
Sources: Dealogic; FTC investigation, 2020

These companies are learning the factors that contribute to deal success. A clear deal thesis and integration thesis grounded in detailed customer and product diligence and aligned with the overall strategy, maniacal focus on retaining all critical talent (not just top leaders), and building a repeatable model with granular tracking of performance to both source and integrate capability deals stand out as priorities for companies ramping up this important type of organic growth.

Deal thesis aligned to strategy and grounded in deep diligence

At the most fundamental level, a company's strategy for acquiring capability targets must be tightly linked to its overall strategy. Amid the industry's relentless disruption, those strategies are constantly changing. So, M&A objectives and priorities need to shift accordingly, requiring frequent (often monthly) reviews of segment and target priorities.

Deep customer diligence and product diligence then position acquirers to understand the value available and how it can add to the existing business. Customer diligence requires rigorous primary research, something that few companies do well. For product diligence, some companies become a customer of the target (and potentially its competitors) to work out the product glitches internally before completing a deal. Acquirers also clearly understand their parenting advantage for a particular capability deal. They entice a target by articulating the benefits of joining forces, such as access to the parent's go-to-market capabilities or its technical talent.

These deep insights from diligence then lend to another key requisite when integrating capability deals—namely, keeping a keen eye on revenue synergies. Tech acquirers articulate at a granular level where the synergies will come from and set aside funds to invest behind them. They focus on quick wins, often in areas in which the acquirer can help the target accelerate its growth ambitions, thus demonstrating why the combination is good for all (see "Bringing Science to the Art of Revenue Synergies"). These companies also keep a tight, highly agile connection between the acquired business and the strategy team to make sure that both are moving in tandem.

Retaining and growing all critical talent

The top priority in a capability deal is retaining the individuals and teams that underpin the desired competency. This is no easy feat, and more than 75% of the tech M&A practitioners we surveyed felt that retention is now more difficult than it was three years ago—and it was more commonly cited as difficult in tech than in other industries.

The biggest retention risks mentioned by tech respondents include employees' uncertainty about their role in the future organization and attractive alternatives in the labor market. As a result, it no longer suffices to focus on cash retention bonuses to ensure that critical talent stays. That's why some acquirers structure capability deals differently than scale deals, with the goal of retaining the top people. For example, earn-outs, stock-for-stock acquisitions, or other methods to keep senior executives in place typically are more important for deals in tech than in other industries.

Another critical element for tech capability deal acquirers is that they invest heavily up front to define an operating model that strikes a balance, giving it autonomy to continue to innovate, grow the base business, and retain talent while also defining the required connection points to propagate the capability more broadly.

Furthermore, the best tech acquirers don't focus only on top leadership retention; they identify the frontline talent critical to creating the capability purchased, and they ensure that talent is appropriately motivated, rewarded, and ultimately retained. They go beyond simply retaining talent by also finding ways to grow the target's own talent base. They allow the target to maintain its talent acquisition policies and processes in a way that would build out the talent pool even faster than it could on its own. Finally, they embrace the target's start-up mentality. Its product cycles are likely to be faster and its tolerance for failure higher, so accepting the new culture is a way to avoid stifling innovation (see "Reimagining Talent in M&A").

Building a repeatable integration chassis

When you manage this volume of acquisitions annually, there is no room for wasted energy, and tech hyper acquirers have learned to create a repeatable integration chassis that builds on lessons learned and drives continuous improvement. This starts with sourcing capability deals. The best companies keep a regular pulse on the market by comprehensively scanning relevant segments for emerging, venture-backed players; monitoring assets; and building a future acquisition pipeline.

Their steady volume of deals also creates the need to act quickly and efficiently in each integration. The best integrators stay focused on the critical few decisions that truly unlock value, and they disproportionately invest in those areas. Again, talent retention is paramount. Some companies also define repeatable processes, systems connections, and talent models that allow them to efficiently adapt their integration approach for any given deal. They build integration bench strength in the form of a team of resources across functions (often residing within the functions) that are trained in integrating different types of deals.

Finally, the tech acquirers that make the most of their small company acquisitions develop an effective feedback mechanism, with regular deal reviews aimed at understanding what's working (and what's not working) and transferring such learnings into subsequent acquisitions.

Doing this well with an aim toward continuous improvement requires granular tracking and codification of synergies (targets and realized), implementation timelines, and investments to use as benchmarks for subsequent deals.

Indeed, learning and continuously refining the integration approach should be the goal of any hyper acquirer hoping to fuel its growth and lead industry transitions. As in so many other areas, the tech industry is one lap ahead in this trend. That's why many companies across industries are now tracking how the successful tech acquirers build muscles for high-velocity integration and learning from the best.

Industries

Telecommunications M&A: A Year of Resilience and Possibilities

Scale and infrastructure deals are quickly reshaping the industry while companies and investors explore creative partnerships.

By Alex Dahlke and Jacob Wennerdal

At a Glance

- M&A in the telecommunications industry rebounded dramatically in 2021, with deal value rising by 48% and record-high multiples reported across most subsectors. Fully 56% of deal value was realized by either in-country consolidations or infrastructure deals.
- Private investments also grew in 2021, by 100%, with private investment multiples rising faster than public trading multiples. Private investment momentum will continue for as long as private telco valuations stay significantly higher than listed telco valuations.
- Amid high valuations, more companies are devising new ways to structure joint ventures (JVs): Some engage in scale deals in which no company wants to relinquish control; others capture cost synergies by consolidating networks while still retaining their independence at the retail level.

The year 2021 helped us clearly see the telecommunications industry's resilience. While the economic uncertainty created by the Covid-19 pandemic caused M&A activity to decline in early 2020, the new year brought with it a resurgence, with deal value growing by 48% and record-high multiples across most subsectors.

The 2021 telecom M&A activity reflects five longer-term underlying industry trends that have been building over the past three to five years, as well as some emerging themes resulting from the accelerated transformation caused by the pandemic *(see Figure 1)*.

Scale deals. Scale deals, such as in-country consolidation, continued to make up the bulk of telecom M&A. Operators hoping to advance their markets to their end state are consolidating before competitors beat them to it. Consider Rogers Communications' $21 billion acquisition of Shaw Communications in Canada in March and the $2.2 billion Indosat-Hutchison deal in Indonesia.

Infrastructure deals. Infrastructure M&A, particularly in tower and fiber assets, is skyrocketing as companies and private investors are eager to join the infrastructure party while the music still is playing. Multiples for infrastructure transactions reached 18 times in 2021, up from an average of 14 times in 2020. By comparison, multiples for integrated operator acquisitions averaged 9 times. Among the notable infrastructure deals of 2021, we have American Tower's $9.4 billion purchase of Telxius and the $1.3 billion CDC-Orange deal for French fiber assets. Infrastructure assets have proven particularly robust and offer a clear path to revenue growth. Additionally, many operators face balance sheet and rating constraints as they accelerate the build-out of new networks, making off-balance sheet joint ventures (JVs) with private investors an attractive alternative to self-funding.

Private investments. Private investors maintained their growing interest in telecommunications across all deal types. Fueled by higher transaction multiples for private transactions than public trading, the total value of their investments in the industry reached $79 billion in 2021 from $39 billion in 2020, and now consistently constitutes 29% to 39% of total deal value, up from around 5% prior to 2019. In one such deal, French billionaire Xavier Niel, controlling shareholder and founder of iliad, bid €3.1 billion to take the company private. In another, global private equity firms Apax Funds and Warburg Pincus agreed to buy T-Mobile Netherlands from Deutsche Telekom for €5.1 billion. And finally, private equity firm KKR in November announced a takeover bid for Italian incumbent telco TIM for €10.8 billion. As they see this trend escalating, operators are rethinking their portfolios with an eye toward divesting underperforming and noncore assets.

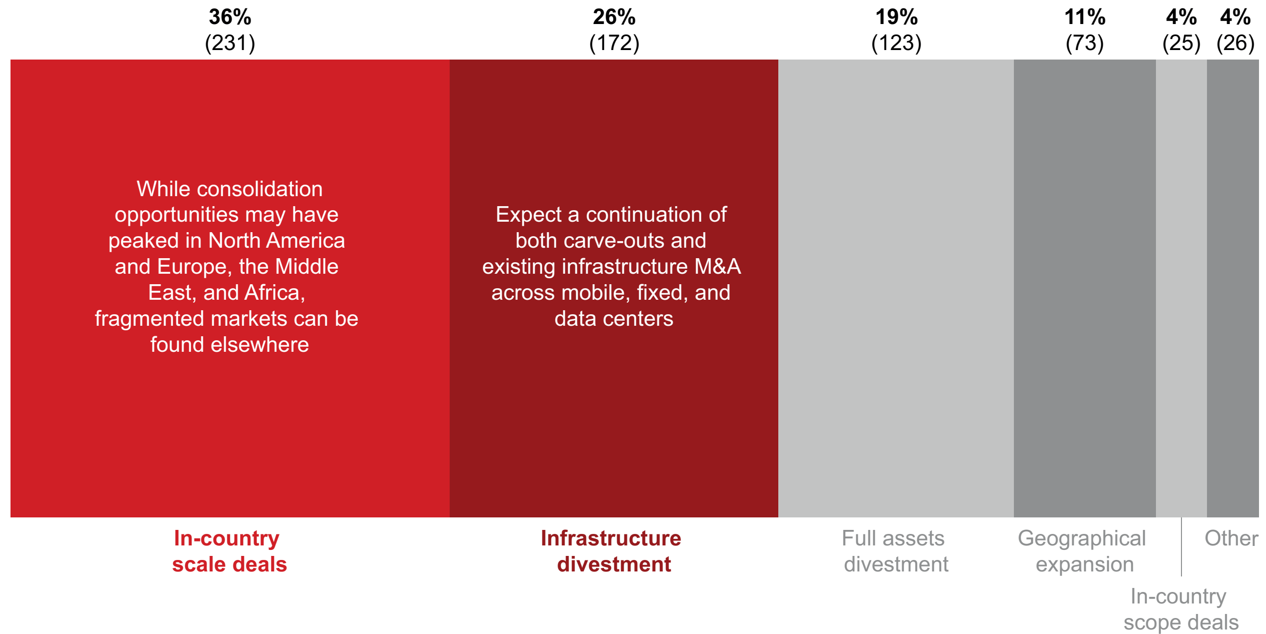
Joint ventures. Alternative deal structures accelerated substantially in 2021. To meet specific objectives, more companies are turning to different flavors of JVs rather than pursuing traditional M&A.

Companies are participating in joint ventures for scale deals in which neither shareholder wants to relinquish control. In September, Chile's VTR and Claro struck a JV that the companies anticipate will generate synergies of $180 million. Partial scale JVs help telcos capture significant cost synergies by consolidating networks while still retaining their independence at the retail level. Another variant involves using JVs between telcos and private investors to carve out existing infrastructure assets or to build new infrastructure, mostly for funding or balance sheet considerations.

Figure 1: Five key themes in telecom M&A

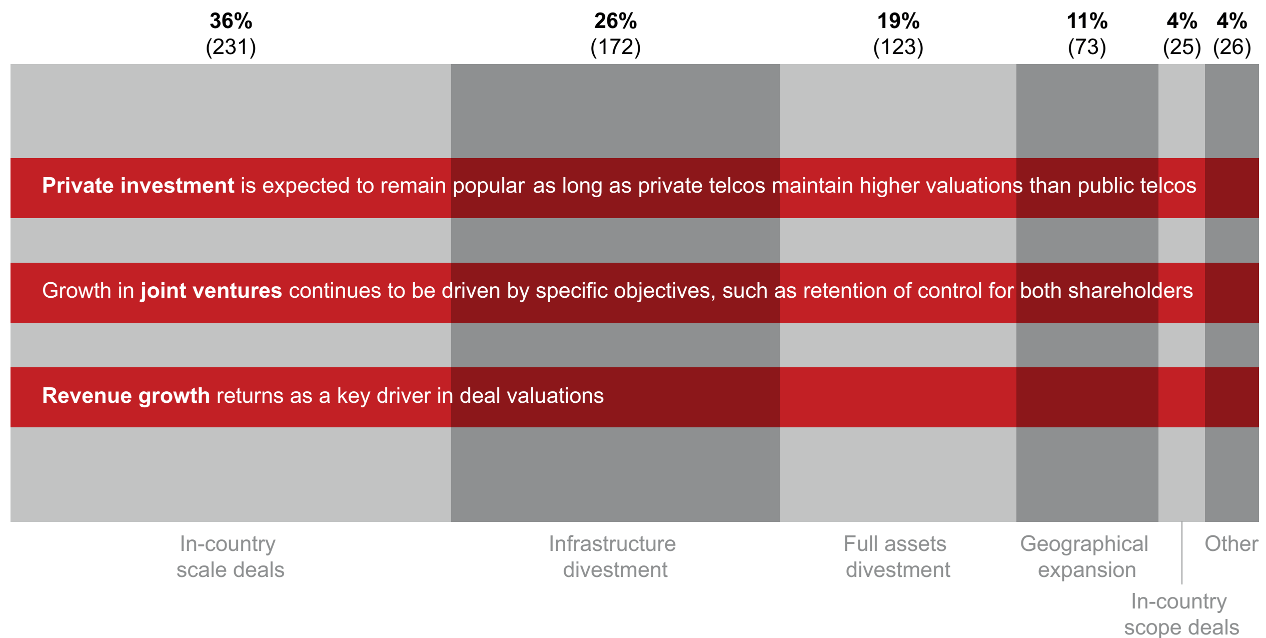
Two deal types command the lion's share and show no signs of abating . . .

Telcos' M&A deal value, 2018–2021 by deal type (in billions of US dollars)



. . . Three other trends have emerged, cutting across deal types

Telcos' M&A deal value, 2018–2021 by deal type (in billions of US dollars)



Notes: Deal value based on announcement year; excludes financial transactions
Sources: Dealogic; Bain analysis

Revenue takes a front seat. In 2021, revenue growth returned as a key driver in deal valuations. In scale deals, revenue synergies (fixed-mobile synergies) through cross-selling to different products' customer bases add to cost synergies. Revenue synergies also are baked into the investment theses of deals in which private equity companies acquire growth challenger telcos, for example. And increasingly, a clear path to top-line growth is becoming a requirement for infrastructure JVs, too.

What's ahead?

Here's how these M&A trends and themes will prevail in 2022 and beyond.

Scale deals will continue in the still fragmented and less strictly regulated markets of Latin America and Asia-Pacific and potentially reemerge in Europe, depending on regulatory changes. But mobile/fixed-mobile consolidations will gradually decline in Europe, where companies have already taken advantage of most opportunities. One potential hot new area for scale acquisitions is in maturing fiber alternative network, or "altnet," assets as we expect more activity in the horizontal and vertical integrations of newly created fiber-to-the-home altnets and JVs.

Infrastructure deals will continue to be propelled by high demand, with high valuations and high supply. Similarly, we anticipate a continuation of both carve-outs and existing infrastructure M&A across mobile, fixed, and data centers.

While the decline in interest rates has contributed to the rise in infrastructure investments, stable or even further declining interest rates would likely result in a selloff of infrastructure investors' stakes to other types of investors.

Perhaps most important, we predict a wave of fiber altnet consolidation reminiscent of the cable roll-ups that were popular two decades ago. The contributing factors are in place: There's abundant capital, overbuild situations, and incumbents pursuing accelerated growth. All of that, combined with the alternative scenario of possible inflation and higher interest rates, could provide the catalyst for accelerated fiber altnet consolidation.

Private investments will maintain momentum for as long as private telco valuations stay significantly higher than public (listed) telco valuations. For example, there are challengers looking for growth and margin expansion by moving wholesale-based businesses onto their own infrastructure.

Private investors will show interest in telcos in other ways: In some situations, controlling shareholders will act on the belief that there is higher value in private telecom investments than in capital markets. Private investors will go after stranded assets within telcos' portfolios. Finally, private investors will show interest in incumbents with strong, still-integrated infrastructure assets and little overbuild risk.

JV deals will also be a popular choice for as long as the wide gap between private and public valuations remains, regulators maintain their stance of opposing full-scale consolidation of markets, and the current infrastructure dynamics continue.

Revenue growth and synergies will also continue to be a theme in the years ahead, justifying high valuations. In a recent survey of telecom M&A executives, a revenue synergies assessment was ranked highest in importance among 10 due diligence elements, with 50% of the respondents predicting that revenue synergies would be significantly more important or somewhat more important in the future.

Five basic questions for telecom players

In 2022 and beyond, telcos need to develop new strategies and capabilities to take advantage of rising M&A opportunities, chances to partner, and possibilities to divest selected portfolio assets. For many, the decision about when to participate, where to participate, and how to participate will come down to answering versions of these five fundamental questions:

- Will we actively drive our markets to end-state structure, or will we allow others to do it to us?
- Are we joining the infrastructure party while the music still plays?
- Is now the time to rethink our portfolio and consider divesting underperforming and noncore assets—or partial assets?
- Which of our markets, infrastructures, and capabilities could lend itself to a JV approach as opposed to traditional M&A?
- Have we discounted revenue synergies and growth too much in our M&A considerations?

In a recent survey of telecom M&A executives, a revenue synergies assessment was ranked highest in importance among 10 due diligence elements.

Media M&A: Deepening Customer Engagement through Adjacencies

Media companies are pursuing deals to expand their offerings well beyond audio and video.

By Daniel Hong, Laurent Colombani, and Nicole Magoon

At a Glance

- To retain customers, media and entertainment companies are buying companies that allow them to move beyond their video and audio roots.
- Cross-sector growth will look different in different geographic markets. Farthest along on the curve, China's WeChat blends social media, gaming, and retail experiences into a single platform.
- Media companies that reach across consumer sectors with a global network for content creation and consumption will be best positioned to capture, retain, and monetize high-volume consumer engagement.
- The tail of single-sector consolidation continues, with deals such as the announced Microsoft acquisition of Activision and WarnerMedia-Discovery merger.

The past five years of media M&A have been dominated by scale deals that enabled the direct-to-consumer (D2C) and streaming shift. Now, sustained economics will depend on retaining these D2C customers and deepening engagement with them by extending the boundaries of media well beyond audio and video and into areas such as video gaming, fitness, betting, and location-based entertainment.

Some of the largest video platforms have already begun moving in this direction. For example, Netflix's foray into video gaming is just the beginning of the next wave of media M&A.

In this race to add new media offerings, consumer engagement types, and geographies, some companies find themselves well positioned to expand organically to large user bases and dip their toes into other sectors. That's particularly the case among companies with a strong technological orientation and a history of successful cross-sector expansion. Others need to selectively grow with partnerships, particularly if some of the most exciting intellectual property tie-ins are well beyond their core. And there is growing interest in scope M&A.

We expect the shift to result in an uptick of M&A activity in the media and entertainment industry and especially in smaller deals. But as companies pursue scope deals or partnerships to enter new businesses, they are learning that the rules for such deals are different than they are for acquisitions aimed at building scale in a similar business.

Giving consumers blended, unified experiences

This trend starts with the recognition that consumers increasingly multitask across media forms and enjoy blended, unified experiences and that mega-platforms will look differently in different parts of the world. In the US, it will take the form of social media tie-ins with popular TV shows or gaming experiences that link to favorite musical artists, for example. In China, where the mega-platform trend first surfaced, it looks like completely integrated in-app universes, such as WeChat's blending of social media, gaming, and retail experiences into a single platform.

In addition to cross-sector growth there is cross-regional activity. Consumers connected to a global online community now have increased exposure to a diverse base of content. Think about the rise of K-pop on the US music charts or the popularity of Turkish dramas on Spanish-language television. In this new age, the media companies that reach across consumer sectors with a global network for content creation and consumption will be best positioned to capture, retain, and monetize high-volume consumer engagement.

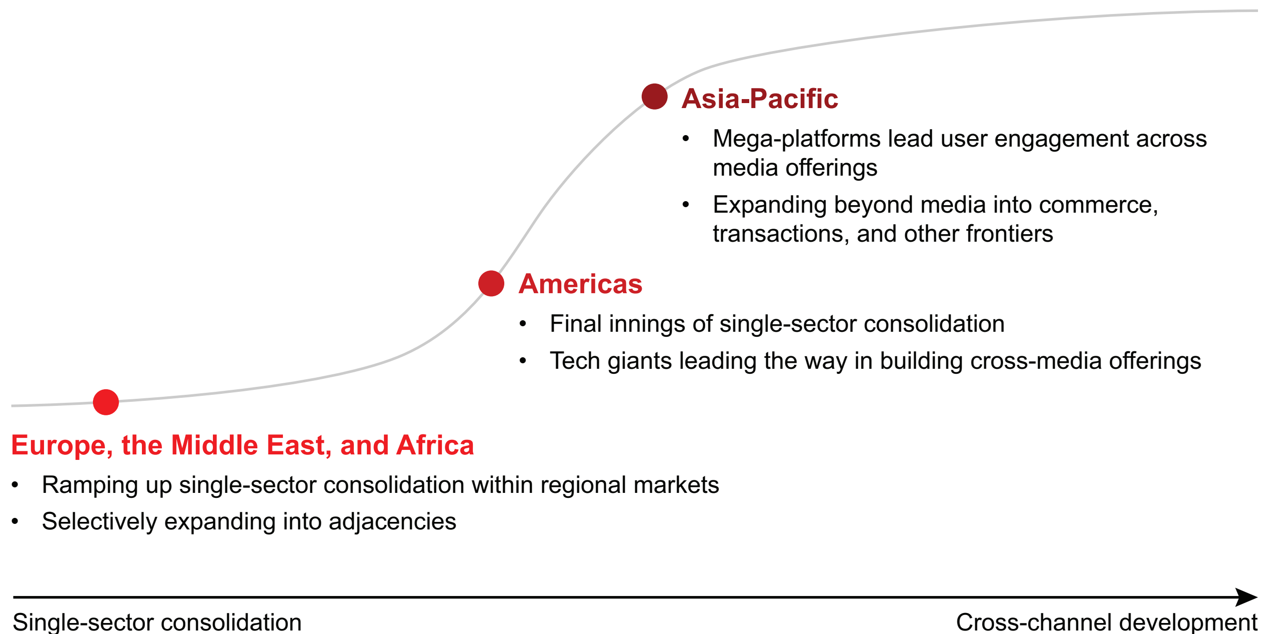
The regional view

Although all regions are moving in the same direction, different markets are further along in this journey *(see Figure 1)*.

Asia is the birthplace of the mega-platform. Again, WeChat's ecosystem offers social media functions, gaming, and even sectors outside of media, such as retail. With more than 1 billion active monthly users, WeChat has created highly unified sources of market power.

The trend to think not just cross-sector but globally for the best assets extends within more specialized companies in Asia, too. For example, South Korean music powerhouse HYBE, which already spans recording, live entertainment, publishing, and more, acquired Scooter Braun's US-based Ithaca Holdings to expand its global reach.

Figure 1: Asia is furthest along in expanding the boundaries of media M&A



Source: Bain & Company

While not quite as far along the curve as some of the largest Asian conglomerates, big US media and entertainment companies are acknowledging the need for new platforms, technology, and the blurring of sector boundaries. The tail of single-sector consolidation continues, with deals such as the announced Microsoft acquisition of Activision and WarnerMedia-Discovery merger as well as the Televisa-Univision merger. Near adjacencies also are still rife, with deals such as the Madison Square Garden Entertainment acquisition of MSG Networks. But the most forward-thinking media and entertainment companies know that retaining a competitive edge with consumers means thinking more broadly and looking farther afield.

Social media companies are making some of the boldest moves with their heavy investment in augmented reality/virtual reality, the metaverse, and social commerce—Facebook's recent rebrand to Meta is a giant step in this direction. In video, consider Netflix's expansion into gaming. Although its initial gaming efforts involved organic tie-ins to video content, Netflix appears to be ramping into what will likely be a broader offering with its proposed acquisition of Night School Studio.

Europe, the Middle East, and Africa are in the early days of building cross-media platforms. Many of the biggest deals are still pulling the region toward that first step, the single-sector consolidation.

In video, the merger of Groupe TF1 and Groupe M6 came with stated plans for investing in live streaming and subscription video on demand. Eventually, these deals will broaden and move not only into the digital future for their specific sector but also across other new media forms. In 2021, Bertelsmann combined its TV and publishing divisions, Mediengruppe RTL Deutschland and Gruner + Jahr, in Germany to support the expansion of its streaming platform, RTL+, beyond video into a variety of digital content.

Asking the right questions

Whichever geography you're in, the trend is toward bigger platforms that can offer consumers a broader suite of experiences, whether with a mega-platform or consolidated single sector. As regions reach the mega-platform stage, however, executives must make the transition from the scale deals that have historically driven industry growth to the scope deals that are likely to fuel growth in the future. Indeed, companies interested in scope M&A beyond adjacencies need to acknowledge that these deals require different approaches than acquisitions aimed at building scale in an existing business.

That starts by asking a fundamental question: From a brand and consumer equity standpoint, are you really a credible seller of the new service?

Next, invest to clearly understand the deep consumer need in your region—the customer base as well as the available acquisition targets. Which offerings go together with which consumer segments? For example, consumers of a company's gaming services will not necessarily want the same offerings as Netflix's subscribers.

Understand what enablers (beyond bundling) are required for the cross-sector experience. If you have video and music, what is the integration that will make it seamless for consumers? Are the recommendations the same for each? Also, be prepared to change your operating model to enable the cross-pollination and deeper integration required.

Assess your own actual realistic technology expansion capabilities. Some management teams lack the experience to expand from video to music, for example. They're just not well equipped to acquire a company in a scope deal and merge it to create a seamless platform. They need the training that can come from joint ventures and partnerships.

You need conviction from the financial markets. If you're buying a gaming company, it likely has a different investor profile than a video company. Make sure that you're not pulling down the multiple—you can destroy value.

Ultimately, the best M&A strategy includes knowing when not to do deals. So, instead of jumping on the M&A bandwagon, the better answer may be to consider partnerships or joint ventures as an initial move toward building a mega-platform. Ultimately, M&A activity must work to build on a company's strengths and not to create a mega-flop.

Industries

Energy and Natural Resources M&A: Deals to Deliver the Energy Transition

More companies will pursue deals that bring them closer to a lower-carbon future.

By Whit Keuer and Arnaud Leroi

At a Glance

- Despite low deal activity in 2021, more companies will turn to M&A to make more progress on the energy transition that will hasten them to a lower-carbon, sustainable future.
- Energy transition deals accounted for about 20% of all energy sector deals greater than $1 billion in 2021.
- In 2022, more companies will use deals to green existing operations and strengthen environmental, social, and corporate governance assets; build green energy hubs; build an integrated value chain to deliver energy transition products and services; reshape business models; and invest in start-ups to acquire disruptive technology.

M&A activity in the energy and natural resources industry saw continued lows in 2021, rebounding only around 20% when compared with 2020 and not yet recovering to pre-pandemic levels. Partly, this was the result of companies looking for demand to stabilize. Then, as stabilization largely took place, a second factor came into play: Companies began sharpening their capital discipline, which slowed dealmaking as fewer deals met their higher hurdle rates.

At its heart, the energy transition requires all companies to reinvent themselves.

We believe that conditions are primed for an upswing propelled by a resurgence in industry consolidation and portfolio management. The oil and gas industry remains highly fragmented in many sectors, and multiples remain depressed, setting the stage for consolidation to unlock new levels of efficiency. Meanwhile, there will be growing opportunities for portfolio management across energy and natural resources, especially in chemicals. Over the years, companies have expanded their portfolios to the point that there's now a lack of natural synergies among assets and a high degree of complexity.

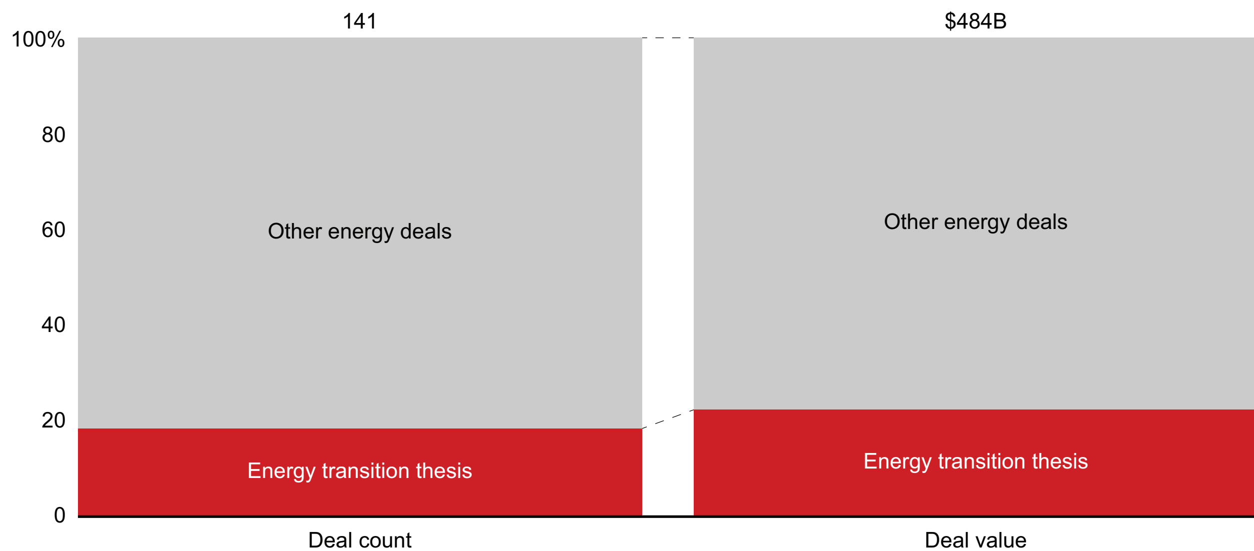
Above all, though, companies will turn to M&A to make more progress on the monumental journey of moving the world closer to a lower-carbon, sustainable future while also keeping their current businesses running. Many large companies have already pursued deals that accelerate them in the energy transition that, at its heart, requires all companies to reinvent themselves.

In 2021, energy transition deals accounted for about 20% of all energy sector deals greater than $1 billion *(see Figure 1)*.

The energy and natural resources industry's reliance on M&A in 2022 to deliver the energy transition will play out across six themes.

Figure 1: Energy transition theses accounted for about 20% of large deals in the energy industry in 2021

2021 energy deals with deal value greater than $1 billion



Source: Dealogic

Greening existing operations and strengthening environmental, social, and corporate governance (ESG) assets: Companies are aggressively making deals aimed at reducing carbon production from their operations to meet net-zero targets. For example, Occidental Petroleum, one of the top producers in the US's Permian Basin, is acquiring solar generation assets to power its drilling and completions operations. At the same time, Suncor is partnering with other oil sands producers while investing to commercialize carbon-capture technology.

Building green energy hubs: Deals are also fueling companies' efforts to move beyond greening their existing operations to fundamentally changing their inputs, production processes, or products. BP and Equinor's strategic partnership, Northern Endurance Partnership, was formed together with Eni, National Grid, Shell, and Total to create a refinery of the future that will act as a green energy hub within an industrial cluster. It will maintain integrated sourcing and production of renewable energy, with new feedstock streams and lower greenhouse gas fuels and products.

Repositioning portfolios toward the energy transition: Companies are using M&A to accelerate shifts in their portfolios. This involves both divestments of high-carbon assets as well as investments in the energy transition. An example is Shell, which sold acreage in the Permian Basin to ConocoPhillips for $9.5 billion in a move to help accelerate the company's portfolio shift driven by the energy transition. Another example is LyondellBasell's joint venture with Suez (now Veolia) and acquisition of European plastics recycling company Quality Circular Polymers to mechanically convert consumer waste into 25,000 tons of polypropylene and high-density polyethylene per year. Private equity firms play a big role in this shift to green operations by buying energy companies' traditional high-carbon assets.

Building an integrated value chain to deliver energy transition products and services: Another strategy is to seek ownership of the full energy transition value chain. BP made a move in this direction when it acquired the UK's largest electric vehicle charging company, which at the time operated more than 6,500 charging ports.

Using M&A to reshape business models: Some companies have found that fully monetizing energy transition assets requires them to buy new capabilities for transformed business models. For example, Shell has a license to sell power to industrial customers in the UK electricity sector.

Making strategic investments in start-ups to acquire disruptive technology: Finally, more companies will make early-stage investments in, or partner with, young companies that can help them become disrupters themselves. That's the goal of a large petrochemical company's investment in a blockchain company, or BASF's corporate venture capital investment in LanzaTech, a carbon recycling company.

How winning companies do it

In their effort to rely on deals to deliver the energy transition, some companies will emerge as leaders. Here's how M&A practitioners in energy and natural resources can boost the odds of success.

Take an activist approach to portfolio management. As portfolios change and become more diverse, companies need to undertake more frequent asset reviews to manage their business through this change. This review is critical in ensuring that the existing business continues to meet current goals and that it would clear the same hurdles for investment today. Leaders need to be prepared to either make the necessary investments for improvement or divest those areas in which performance is falling short of what is needed for today's corporate strategy.

Set a capital allocation strategy that is tied to the corporate strategy, and posture toward the energy transition. That means adopting an approach to capital allocation that recognizes that renewables are reaching competitive scale for new capital expenditures, and it means being disciplined about exploring profitable growth options in low carbon across multiple growth horizons.

Incorporate ESG considerations into due diligence. Buyers need to actively understand and assess the relative performance of the target across critical ESG dimensions. This benchmarking exercise allows companies not only to understand the target's true value but also to anticipate any unexpected costs in which the target is disconnected from the buyer's desired corporate ESG strategy. This needs to feed into value creation planning and integration in order to unlock the full potential of the combination (see "The ESG Imperative in M&A").

Evolve the joint venture playbook to accelerate an energy transition strategy. This is a historic area of strength for many energy and natural resources companies as they have used joint ventures to partner in the development of oil and gas fields or large petrochemical complexes, often with state-owned enterprises. In addition to these traditional uses of joint ventures, companies increasingly are seeing the need to use joint ventures to accelerate energy transition strategies and combine expertise along the value chain as it is difficult for one company to have all the capabilities required. For example, there are several joint ventures globally related to the chemical recycling of plastic waste. These joint ventures involve three parties: traditional waste companies with expertise in the collection and preparation of waste and recyclable materials, a company with proprietary mechanical or chemical recycling technology, and a traditional chemical company with experience in processing and operating hydrocarbon and chemical plants.

Fluid M&A market dynamics will provide myriad opportunities for resilient companies to transform their portfolios and reposition themselves for the great energy transition. The best companies view the industry's era of complex uncertainties and unprecedented change for what it is: a time of historic possibilities.

Industries

Diversified Industrials M&A: Shaping Portfolios via M&A

Dealmaking bounces back as industrial players continue to rebalance portfolios and pursue growth.

By Clark Herndon, Magnus Konberg, Sachin Kotak, and John Sequeira

At a Glance

- M&A reached a new high in 2021 as industrial companies used portfolio management to balance leadership in their core with aggressive growth in new markets.
- While two-thirds of the deals involved a shift back to scale M&A, industrial companies went after scope deals that will help them expand into a new business or geography, or develop a needed capability.
- The year 2021, similar to most of the past five years, saw a higher divestiture volume in diversified industrials than other sectors as companies exited noncore or underperforming businesses.
- Our survey of executives found that industrial dealmakers were far more likely than all other execs to rank a clear deal thesis and clear integration thesis as the most important aspects of successful scope deals.

In 2021, strategic dealmaking among industrials reached new heights as industrial companies accelerated portfolio reshaping in the face of evolving industry dynamics. Deal value was up 50% year over year, and appetite remains for more, with two-thirds of industrial executives anticipating that deal volume will grow in 2022, according to a recent Bain survey *(see Figure 1)*.

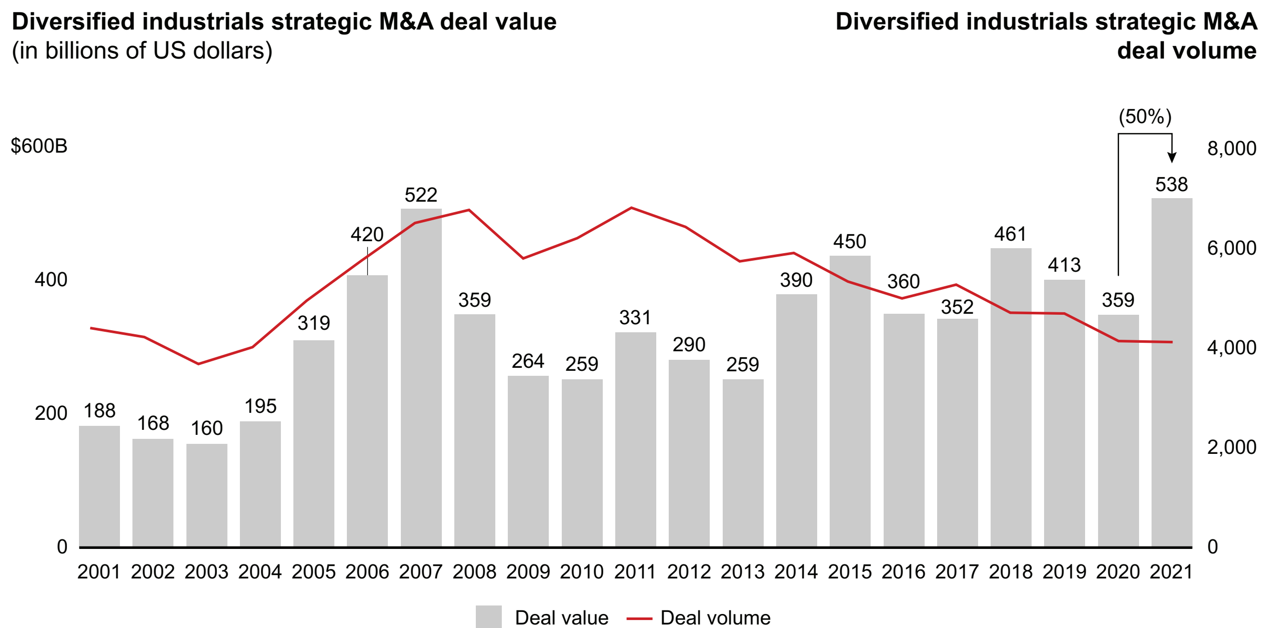
Since the pandemic, large deal activity among industrial companies has shifted back to scale.

Market fundamentals suggest why industrial M&A is so active. In many sectors, the underlying market growth is low (GDP-plus), but leading companies have higher growth aspirations. Many market leaders have done a good job in past years to build No. 1 and No. 2 positions in their core, and further share gain is increasingly difficult. M&A provides access to higher-growth, more attractive, and strategically important markets.

Balancing the pursuit of leadership in the core against growth in adjacent markets amplifies the need for industrial companies to maintain a robust and evergreen portfolio strategy.

Dynamic portfolio reshaping is reflected in the balance between scale and scope deals. Since the pandemic, large deal activity among industrial companies has shifted back to scale, as seen in deals such as bearing manufacturer RBC's acquisition of Dodge from ABB, Goodyear's acquisition of

Figure 1: After a period of stagnant deal value, 2021 deal activity exceeded recent history for strategic M&A in diversified industrials



Note: Excludes real estate and services
Source: Dealogic

Cooper, and Cargotec's announced merger with Konecranes. Scope and capability deals continued at a good pace as well, accounting for more than one in three large deals. For example, Uber expanded its freight offering with the purchase of Transplace and its shipper technology. Holcim Group (formerly LafargeHolcim) bolstered its energy-efficient buildings business by buying Firestone Building Products and its sustainable roof offerings early in 2021, announcing a second deal in the same roofing segment in late December with the acquisition of Malarkey.

Industrial players leaned in to acquire critical new capabilities around software, the Internet of Things (IoT), artificial intelligence, and connectivity at high valuations. Rockwell Automation's acquisition of Plex Systems, a cloud-based manufacturing solution, and Siemens' acquisition of IoT start-up Wattsense both point to the ongoing industrial digitization journey common in this sector. Notably, targets with attractive capabilities are highly valued tech assets that trade, on average, at 25 times EBITDA vs. 13 times for targets in the industrial core (and acquirers' own valuation). Hitachi's acquisition of digital engineering and design firm GlobalLogic at $9.6 billion implies an EBITDA multiple of more than 37 times. In light of these multiples, many companies are taking a portfolio approach to developing these capabilities through corporate venture capital, joint ventures, and partnerships.

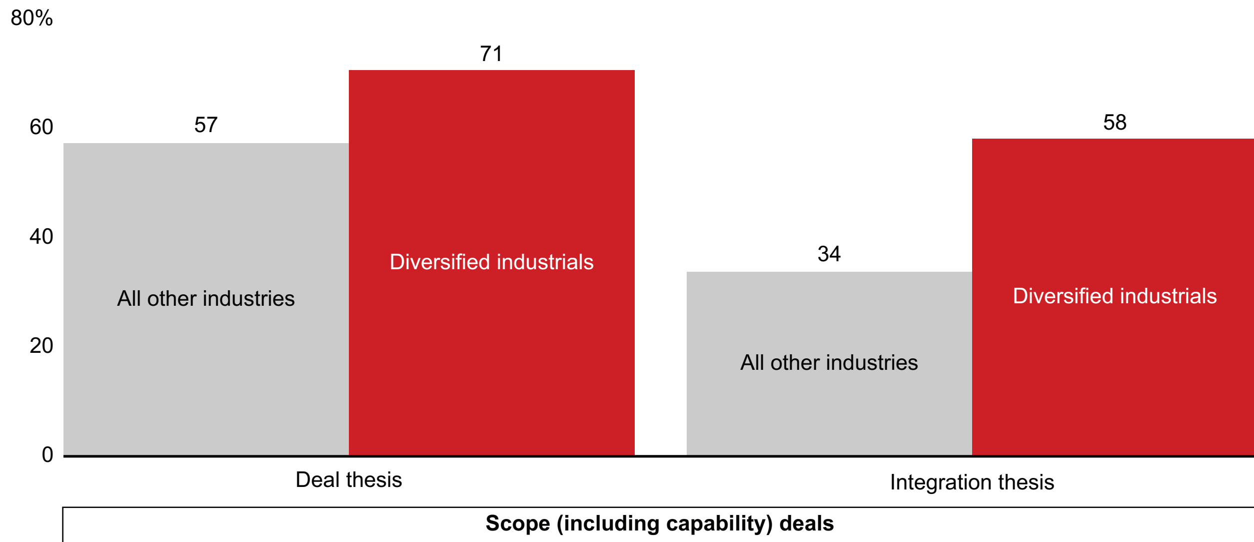
Active portfolio management is also evident in the high rate of divestitures among industrial companies. Successful companies act as decisively to exit noncore or underperforming businesses as they do to invest behind their growth strategies. The year 2021, similar to most of the past five years, saw a higher divestiture volume in diversified industrials than other sectors; recent divestitures from large industrial leaders, such as Siemens (Flender), ABB (Dodge mechanical power), ThyssenKrupp (mining technologies), and Hitachi (metals), are more representative of the trend than some may realize. These divestitures are often used to fuel deals in more attractive segments.

Evolving the industrial M&A playbook for scope and capability deals

Successful industrial companies have adapted and changed how they approach M&A to make scope and capability deals as successful as scale deals. In a recent Bain survey of executives, industrial dealmakers were far more likely than all other execs to rank a clear deal thesis and clear integration thesis as the most important aspects of successful scope deals *(see Figure 2)*.

Successful companies act as decisively to exit noncore or underperforming businesses as they do to invest behind their growth strategies.

Figure 2: Industrial executives cite clear deal and integration theses as the most important aspects of successful scope M&A



Source: Bain M&A Practitioners' Survey, 2022 (N=281)

Many industrials with a successful M&A track record excel at integrating scale acquisitions and driving cost synergies. What these executives recognize, however, is that scope and capability deals present a new set of challenges. Acquirers lack intuitive knowledge on the rules of the game or on key players in these new markets and industry segments. Valuations are higher, and the value creation logic is different. Rather than cost reduction, scope deals' success often comes down to revenue synergies through integrated offerings and cross-selling of emergent capabilities and products or services. The integration approach must reflect these unique sources of value and risk that comes from acquiring an adjacent business.

With this in mind, we observe three key adjustments that scale-oriented industrial firms must make for successful scope and capability dealmaking.

First, proactively link corporate strategy and the M&A roadmap. Firmly establishing strategic rationale and fully aligning the organization top to bottom ahead of a potential scope or capability deal is key. Scale-oriented industrial buyers typically set up a centralized governance model to ensure a strong link between M&A and corporate strategy. Yet the decision clock speed of many industrials becomes a blocker if strategic intent is reevaluated in a short diligence phase. Conviction will be tested in an environment of high valuations and rapid deal processes, and leaders must adapt their diligence processes (including board approval, for example) to make decisions quickly in less traditional and more competitive markets.

Second, update the diligence playbook for scope deals—build on all the traditional best practices, but increase emphasis on what matters for scope and capability. Rigor must be added to revenue synergies diligence to assess customer willingness to pay for new, not-yet-available, innovative offerings—or to validate cross-selling potential (see "Bringing Science to the Art of Revenue Synergies"). Leaders also recognize that as deals move further afield, internal market and industry expertise will be insufficient, and they build an ecosystem of partners and advisers to support with capabilities and expertise not available in-house.

Third, tailor the integration thesis for each deal. Understand the ambition for how the integration will protect and develop the acquired business while enhancing the existing one. A scope deal predicated on combining product portfolios requires a different focus and roadmap than a capability deal for an innovative technology to embed in existing products. Aligning management teams may require more attention (and intention) to preserve the unique capability of the target company. Leading companies adopt key elements from the value creation plan concept, common within private equity, to set up a merger integration program that accelerates value capture. This often leads to targeted integration and even retaining the acquired company as a separate entity while also defining the critical few areas of collaboration that are crucial for the deal thesis and value creation plan. Successful companies must shift to a mentality of integration by exception rather than by default.

One industrial company adapted its M&A approach when acquiring an attractive but premium-priced asset that offered a foothold in a desirable new line of business. The acquirer had a successful track record of integrating small to medium targets in its core business. When a refresh of corporate strategy called for adjacent moves, however, leadership recognized that a new M&A playbook was needed. During diligence, they used extensive customer research to evaluate both the target's standalone growth and how technology capabilities could enhance the acquirer's core products, building comfort that the deal would lead to both share gains and margin improvements. Convinced of the full potential, the company had the confidence to make the winning bid. Then, after closing the deal, they applied a limited integration model that emphasized product development collaboration for the integrated offering while leaving the acquired entity to operate on a standalone basis beyond those critical few areas. As a result, the acquired company continued its rapid growth trajectory while in parallel delivering on the rapid development and time-to-market benefits of the joint offerings that constituted the majority of the synergy case.

Rather than cost reduction, scope deals' success often comes down to revenue synergies through integrated offerings and cross-selling of emergent capabilities and products or services.

Outlook

Looking ahead, we do not expect the momentum to slow for M&A activity within the industrial sector, and we believe that trends toward aggressive scale theses and scope and capability deals will persist. High valuations are making the deal market more challenging, and some companies will decide to sit on the sidelines. Those that want to grow must take a more proactive stance, and this will accentuate the need for robust end-to-end management of the M&A value chain. Deals require a clear strategic rationale, well-defined deal and integration theses, modern diligence across cost and revenue synergies, and stringent planning, realization, and follow-through of value creation post-close. In the chapters that follow, we observe many of these trends in the automotive and aerospace and defense subsectors.

Automotive and Mobility M&A: How Companies Tune Up Their M&A Engines

Manufacturers and suppliers are racing to secure leadership positions in an industry in which high-tech and software capabilities are critical for success.

By Ralf Kalmbach, Klaus Stricker, Pedro Correa, and Dominik Foucar

At a Glance

- After a pandemic-induced dip in 2020 and the chip crisis in 2021, strategic M&A deal volume in the automotive and mobility industry is expected to return to a growth trajectory.
- The share of growth-oriented scope deals continues to rise. Manufacturers, in particular, are expanding their existing businesses and entering new business areas.
- Disruptive changes such as electrification, digitization, and automation are requiring manufacturers to intensify M&A to acquire newly critical capabilities on a faster timescale than feasible via organic growth.
- M&A becomes a strategic core competence. The industry can exploit the full potential with five levers.

For years, the automotive and mobility industry undervalued M&A capabilities. As recently as 2016, most activity involved traditional scale deals aimed at enabling manufacturers and suppliers to get bigger and to generate the cost synergies that come with economies of scale. The skills required were fairly straightforward to develop and rely on, deal after deal.

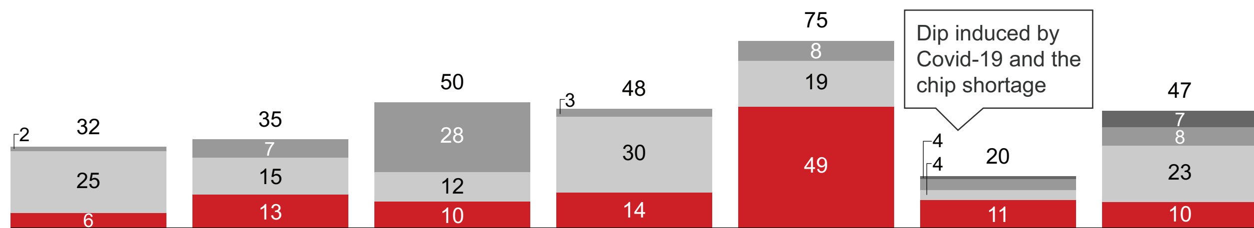
Now the industry finds itself deep in the biggest period of disruption in its history. In addition to consolidating for leadership, companies increasingly need to expand into new businesses and acquire new technology and innovation capabilities, especially in what we refer to as the "5 RACES":

- **R**eal customer focus;
- **A**utonomous driving;
- **C**onnectivity and digitization of vehicles;
- **E**lectrification of powertrains; and
- **S**hared mobility.

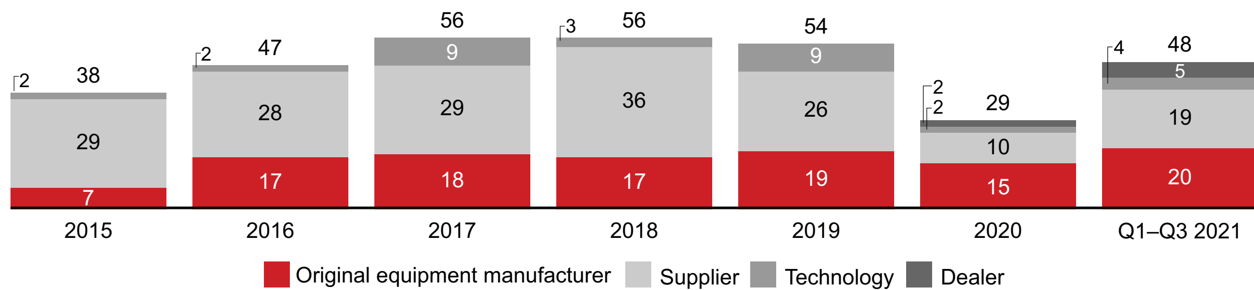
Despite a global semiconductor chip shortage and other lingering effects of the Covid-19 pandemic, as of October 2021, there were 48 deals valued greater than $100 million totaling $47 billion compared with 29 deals and $20 billion in 2020 *(see Figure 1)*. It was a year in which private equity showed more interest, pumping up the competition; also, the number of special purchase acquisition companies increased.

Figure 1: Automotive and mobility industry M&A accelerated following a pandemic-induced dip in 2020

Deal value (in billions of US dollars)



Deal count



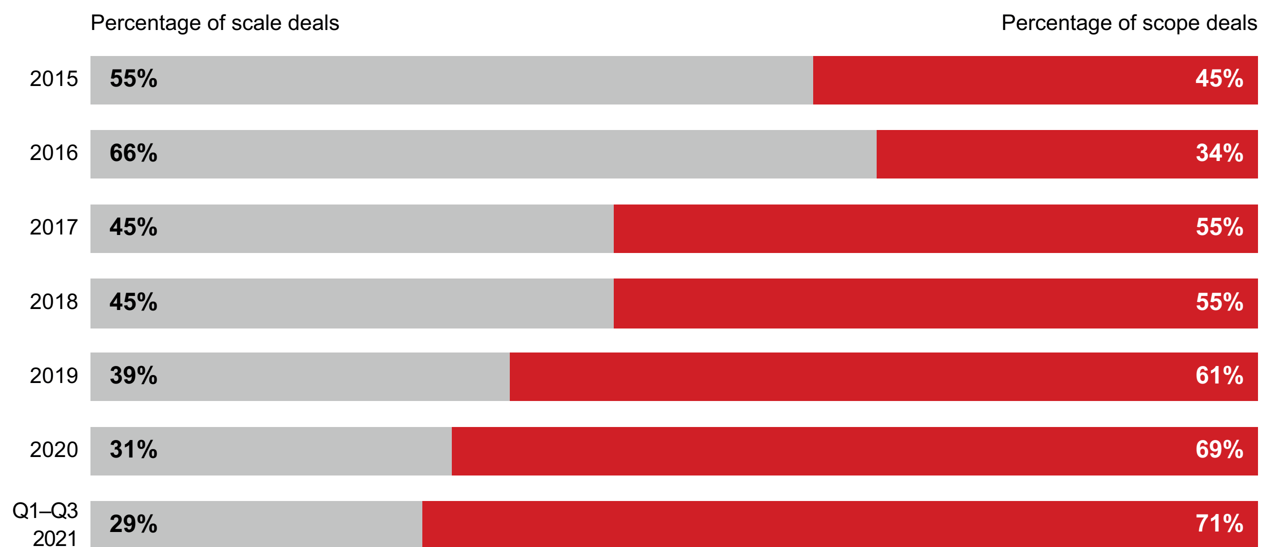
Note: 2019 includes Stellantis deal
Sources: Dealogic; Bain analysis

Even with record volumes, automotive and mobility companies have been comparatively slow to pursue inorganic growth. As the pace of change intensifies, inorganic acquisition enables companies to quickly develop required new capabilities. Hence, they need to make M&A strategy a key part of their business strategy and aggressively sharpen their M&A muscles. That requires perfecting new approaches in screening, diligence, and integration for different kinds of deals.

There still is opportunity to consolidate for scale leadership. In fact, among the major deals of 2021 was Goodyear's acquisition of Cooper Tire & Rubber to strengthen Goodyear's global positioning, one of 14 scale deals totaling $13 billion last year. That consolidation takes place beyond manufacturing and suppliers. In October, Asbury Automotive Group bought Larry H. Miller Dealerships, the eighth-largest dealership group in the US, for $3.2 billion, stretching Asbury's reach from coast to coast.

The number of scale deals is overshadowed, however, by scope deals aimed at entering a new market or acquiring a new capability. Scope deals now represent about 70% of automotive and mobility transactions with deal values greater than $100 million *(see Figure 2)*. For example, French car parts supplier Faurecia's acquisition of German auto lighting company Hella in 2021 helps Faurecia further expand its activities as a systems provider, increasing exposure to fast-growing segments in light of industry trends.

Figure 2: Scope deals have risen in the automotive and mobility industry



Note: Deals classified by rationale using a proprietary classification framework, as per stated strategic rationale at the time of deal announcement
Sources: Dealogic; Bain analysis

Suppliers such as Faurecia face growing competition from the technology companies that they seek to acquire. Qualcomm is a company better known for semiconductors, software, and services related to wireless technology. This year, however, it teamed with investment group SSW Partners to buy Swedish automotive tech company Veoneer to expand its offering for advanced driver-assistance systems.

Not all capability expansions can be managed via acquisitions, so building smart partnerships and joint ventures will be an important tool as well. As manufacturers and suppliers seek proximity to specialists in fields such as autonomous driving, these partnerships will play an important role across industries and geographies. That's why established automobile manufacturers are now cooperating with Silicon Valley giants while European top dogs team with Chinese climbers and billion-dollar companies. For example, Stellantis and Samsung SDI entered into a memorandum of understanding to form a joint venture to produce battery cells and modules for North America (see "Delivering Results in Joint Ventures and Alliances Requires a New Playbook").

As manufacturers and suppliers seek proximity to specialists in fields such as autonomous driving, these partnerships will play an important role across industries and geographies.

Unleash the full potential of M&A transactions

Companies in the automotive and mobility industry can only take advantage of the opportunities on the market if they have the right structures and processes in place. The best companies rely on five important levers.

- **Strategic embedding of M&A:** The industry has traditionally relied on organic growth and its own innovations. Pioneers follow the example of players in the healthcare and high-tech industries, making takeovers and collaborations an integral part of corporate strategy and anchoring them within their organizations.
- **Fast M&A processes:** Companies that only buy on a situational basis usually only put together teams on a situational basis. The resulting lag times cause them to lose out to faster competitors in the automotive and mobility industry or frustrate potential targets in high tech, as the younger companies typically have little tolerance for lengthy coordination processes.

- **Extended deal focus:** Electrification, digitization, and automation of vehicles are changing the business of manufacturers, suppliers, and service providers. As a result, companies need to expand their purview of possible investments and partners (and the types of M&A transactions) that can strengthen or expand a core business.

- **Improved post-merger integration:** Integrating acquired targets is even more challenging than identifying suitable targets. Post-merger integration is about maintaining and promoting the core business of acquired companies while also realizing the expected added value. In some situations, the acquired companies initially should remain independent. Agile methods facilitate collaboration, and joint management teams can identify and eliminate points of friction at an early stage.

- **Capturing full value:** Traditionally, the focus in the automotive and mobility industry is on integrating the new know-how and the acquired competencies into the development of the acquirer's own products. But especially with acquisitions in hardware and software, it also is advisable to assume the marketing of the acquired company's intellectual property or use the acquirer's business model.

For both manufacturers and suppliers, it's a huge shift to begin viewing young hardware and software companies as potential competitors, partners, takeover candidates, or acquirers. But broadening one's view, making M&A strategy core to business strategy, and rigorously expanding M&A competence are the automotive and mobility industry's keys to the future.

Industries

Aerospace and Defense M&A: Finding Footing in an Era of Downturn and Disruption

As the industry resets growth expectations amid an uncertain future, many are turning to dealmaking.

By Jim Harris, Pierluigi Serlenga, Michael Sion, and Austin Kim

At a Glance

- Commercial aerospace is struggling with the shape of the Covid-19 recovery and the new normal of air travel, while defense companies face budget uncertainty and growing competition from new entrants. Both sectors are turning to M&A to strengthen their fundamentals and positioning for growth.
- With original equipment manufacturers, primes, and tier 1 suppliers already heavily consolidated (plus suppliers feeling the yo-yo effect of ramp up, downturn, and ramp up), we expect to see heavier M&A activity in the lower-tier, fragmented supplier base.
- The shape of the defense and space sectors is rapidly evolving because of the geopolitical environment and pace of innovation. New entrants are ready to make their own deals, and competition with financial sponsors is heating up.
- Companies that effectively use acquisitions, divestitures, and partnerships to improve their portfolios and gain capabilities and talent will emerge as winners.

Downturn and disruption

Even during relatively stable times, the aerospace and defense industry generally sees a healthy dose of M&A activity. Now, recovering from a historic downturn and growing disruption, the industry is poised to experience even more deals. The best companies will pursue M&A that will help them to emerge from these turbulent times with stronger fundamentals—namely, leadership economics, innovative capabilities, and greater diversification.

Nearly two years into the biggest decline in commercial aviation history, the industry globally is only back to around half its pre-pandemic levels—and the prolonged recovery may never include a full return of one key ingredient: profitable business travel that feeds industry profit pools. If this chain of events were to happen, airlines and lessors would be pressured to squeeze original equipment manufacturers (OEMs), which in turn would pass this down through each layer of the supplier base. Adding to the pressure, a rising sustainability agenda will require greater levels of investment among potentially competing technologies, further straining balance sheets.

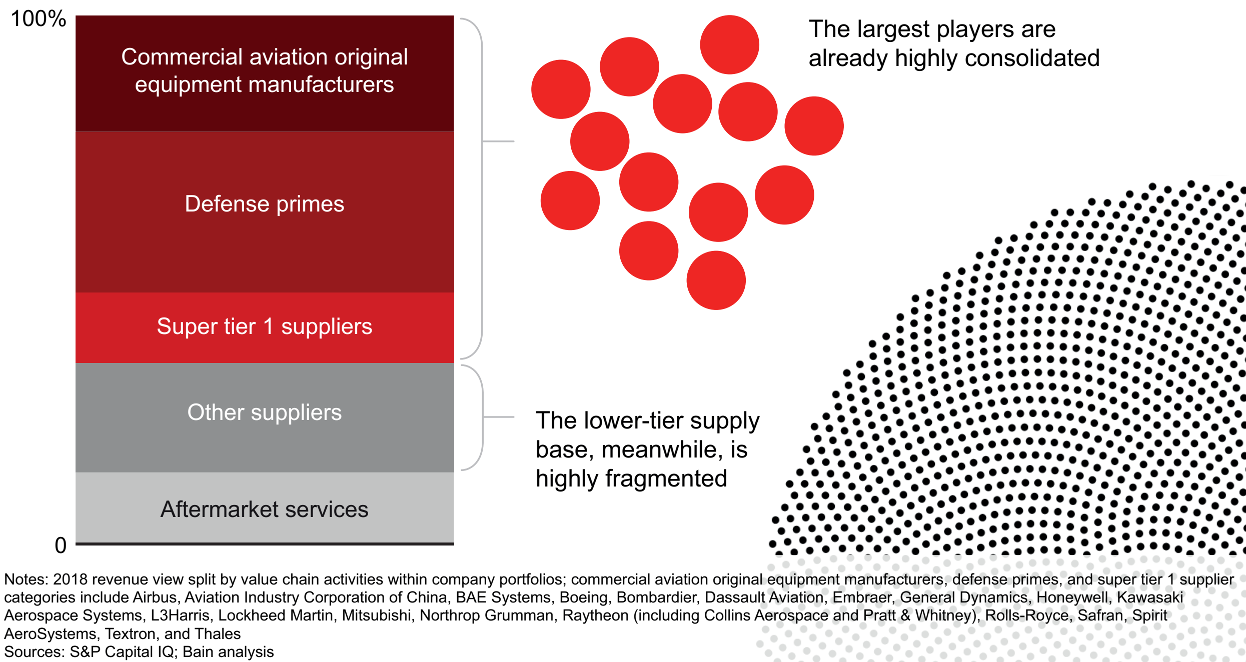
Meanwhile, defense has recently gone through its own reset in growth expectations. After being the more resilient half of the industry throughout the pandemic, it now faces an uncertain future that may include reductions in program spending as a result of other massive fiscal spending priorities. At the same time, mounting geopolitical threats have set off an arms race in areas including hypersonics, space, and artificial intelligence (AI). Contractors are looking for ways to innovate and do more, but in a smaller cost envelope. Thus the shape of the industry continues to evolve, with new entrants such as SpaceX, Palantir, Epirus, and others flush with investor cash ready to make their own moves. And increasingly in the mix are nontraditional contractors such as Microsoft and Amazon that are looking to grow their share of public sector spending in hot areas such as cloud services.

Nearly two years into the biggest decline in commercial aviation history, the industry globally is only back to around half its pre-pandemic levels.

Consolidation continues to shape the game board

Consolidation had already shrunk the game board before Covid-19 disrupted the industry through massive deals such as the L3-Harris and Raytheon-United Technologies mergers. While the industry is likely to see some headline deals, such as the pending Lockheed Martin-Aerojet Rocketdyne acquisition as well as activities leading to and resulting from a standalone GE Aviation, there is now

Figure 1: : Original equipment manufacturers, primes, and tier 1 suppliers make up nearly two-thirds of the industry's marketplace



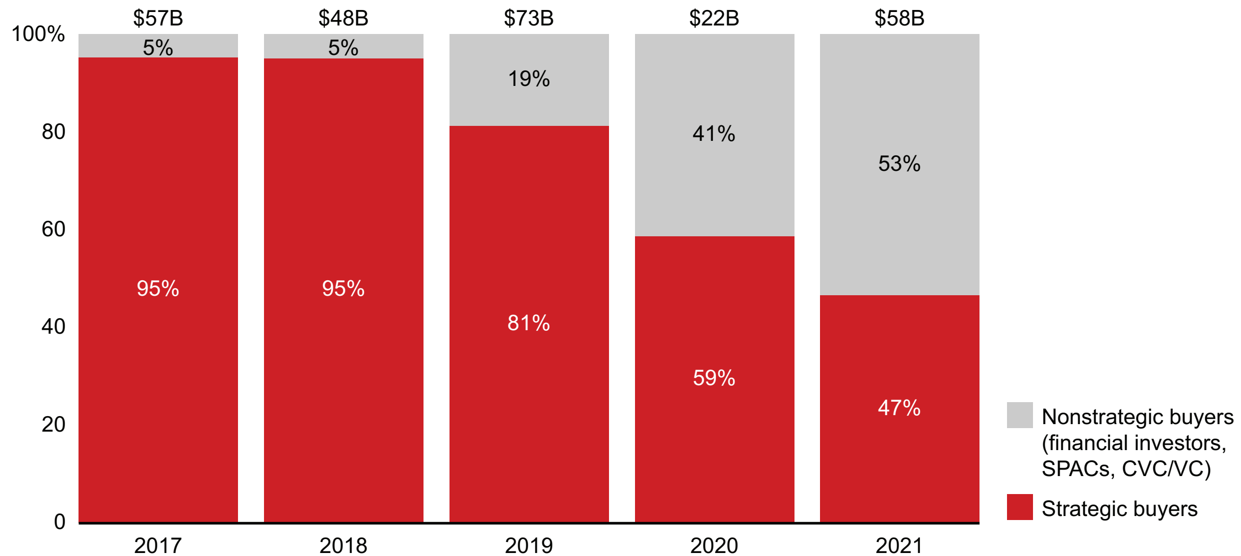
Notes: 2018 revenue view split by value chain activities within company portfolios; commercial aviation original equipment manufacturers, defense primes, and super tier 1 supplier categories include Airbus, Aviation Industry Corporation of China, BAE Systems, Boeing, Bombardier, Dassault Aviation, Embraer, General Dynamics, Honeywell, Kawasaki Aerospace Systems, L3Harris, Lockheed Martin, Mitsubishi, Northrop Grumman, Raytheon (including Collins Aerospace and Pratt & Whitney), Rolls-Royce, Safran, Spirit AeroSystems, Textron, and Thales
Sources: S&P Capital IQ; Bain analysis

a palpable sense of greater regulatory scrutiny. With OEMs, primes, and tier 1 suppliers already heavily consolidated, most of the M&A activity going forward will be in the lower-tier, fragmented supplier base (*see Figure 1*). Sizable and attractive assets will be fewer and farther between and in high demand.

Last fall's bidding war that Parker Hannifin won to acquire Meggitt, creating a tier 2 supplier at scale, reflects the willingness to pay a premium for opportunities amid changes brought on by the pandemic, steep narrow-body rate swings, acute supply chain and inflationary stresses, and a future that will be tied to aggressive sustainability commitments.

In Europe, product champions across the defense industry have continued to emerge through cross-border M&A. For example, last year, Italian defense group Leonardo purchased a 25.1% stake in Germany's Hensoldt, fending off rivals, to create a leading European player in defense electronics. And this follows examples paved over the years in the ground segment, with KNDS emerging from French and German national champions Nexter and KMW and Germany's Rheinmetall taking a controlling stake in UK-based BAE's armored vehicle business. While cross-border joint ventures have been common against a backdrop of nationalistic protectionism, mergers and acquisitions are poised to continue.

Figure 2: Share of non-strategic transactions in aerospace and defense has increased since 2017



Note: Transactions with targets in aerospace/aircraft or defense/contractors, products, and services, according to Sourcing Industry Group classification
Source: Dealogic

Revisiting parenting advantages

Buoyed by growth prospects, multiples in 2021 remained strong, particularly in buzzworthy segments such as space, hypersonics, AI/machine learning, and defense electronics. Throughout 2021, EBITDA multiples in the teens have been common in an industry in which high-single-digit price tags were the historical norm.

Moreover, the competition for these deals is heating up from both corporate acquirers and financial sponsors (*see Figure 2*). Armed with seemingly limitless dry powder, the roster of private equity players exploring and buying assets in aerospace and defense has expanded.

As opportunities emerge, particularly out of the commercial aviation recovery, there will continue to be a greater role for private equity funds as both buyers and sellers. Sophistication and industry knowledge will be a key differentiator between the winners and losers.

In this environment, the best companies won't buy merely to unlock absolute growth, nor will they let high multiples distract them from the fundamentals. Instead, they'll lean in with a disciplined approach, paying a premium for deals that help advance their strategy, including greater

diversification in end markets and product life cycles. This requires a clear thesis of the value (cost and revenue synergies) to be unlocked through integration and an ongoing conviction gained from appropriate due diligence. Without inherent parenting advantages, companies will be outbid or, worse yet, winners of bids for which they are unable to unlock long-term value in their portfolios.

Innovation outside the four walls

A big factor in the M&A equation is the widening innovation gap between incumbents on the one hand and the growing pool of new entrants (young insurgents as well as the likes of Microsoft and Amazon) on the other hand. While new entrants have traditionally not been a major threat to this industry, we've seen cracks form in which greater technical capabilities have opened up markets in everything from space launch and observation to the cloud and advanced data analytics.

In addition to clearly outpacing incumbents in R&D, newer entrants also are winning on another major front: the battle for technical talent. It's no secret that the industry faces a generational shift along with a severe talent shortage, and there are few signs of improvement as technology players have taken up greater real estate across places such as the Washington, DC metro area.

A company's ability to collaborate and partner may be the best way to open up access to the skill sets capable of delivering the required best-of-breed technologies, including for quantum computing, 5G connectivity, and AI (see "Delivering Results in Joint Ventures and Alliances Requires a New Playbook" and "Harnessing the True Value of Corporate Venture Capital"). But where acquisitions are needed and justified, companies must avoid killing the golden goose—that is, the stifling of innovation and loss of talent that too often happens when integration in a capability deal follows the integration script of a typical scale deal.

The bottom line?

Now is not a time to be passive on the M&A and partnering front. Nor is it a time to bulk up for the sake of scale. As we have seen demonstrated during prior downturns and periods of disruption, those able to effectively shore up their portfolios and gain capabilities and talent will likely emerge as winners. M&A should work toward that goal and not be a knee-jerk attempt to build (or rebuild) elusive top-line growth.

Industries

Banking M&A: A Push for Scale in a Competitive Market

As banking M&A continues to heat up, acquirers must deal with a more dynamic environment and a new set of rules.

By Seow-Chien Chew, Joe Fielding, Roberto Frazzitta, and Pierre de Raismes

At a Glance

- M&A could account for 50% of revenue growth in banking in the years ahead, an increase from the already high 35% rate.
- While an average of 75% of that activity from 2015 to 2020 has involved scale deals, there will be a rise in scope deals as banks face a growing need to broaden their reach.
- As the M&A environment heats up, traditional banks are facing increasing competition from private equity firms, well-funded digital-native banks, and technology firms buying banks.
- The old "integrate first and transform later" M&A mantra is being replaced with "buy and transform now."

The banking industry is primed for heated M&A activity.

In an era of persistent low interest rates and economic uncertainty, it has been challenging for banks to grow their revenue organically. They rely on acquisitions to pick up attractive customers and valuable assets. Scale deals accounted for an average of 75% of all large deals (more than $1 billion) activity in banking from 2015 to 2020. Also, unlike other industries in which regulators discourage consolidation, this is one in which authorities ranging from the Financial Services Authority of Indonesia to the European Central Bank are creating conditions that favor the building of local banking champions.

This comes at a time when scale is even more important than ever as banks seek to manage margin compression caused by a host of pressures, including competition from nontraditional players; rising compliance costs; larger capital expenditure requirements for digital/technology investments; and the coming impact of environmental, social, and corporate governance (ESG) commitments. Consider that many banks have committed to net zero in 2030, which stands to significantly affect their traditional lending business.

Given all these factors, M&A is expected to rise. In our global survey of M&A executives, 72% of financial services respondents expect their company's M&A activity to increase over the next year.

Here's how that will play out in the market.

Local players will continue to buy competitors to build positions of scale. That was the impetus behind US Bancorp's agreement in September to buy MUFG Union Bank as well as local portfolio deals such as AIB's purchase of €4.2 billion of corporate and commercial loans from Ulster Bank in June.

Also, multicountry global banks will continue to reevaluate their core vs. noncore businesses and exit subscale markets. That's what Citi did by selling most of its Asia retail business, except for the financial centers of Singapore and Hong Kong. And HSBC sold its retail activities in France and the US.

While M&A in financial services remains predominantly scale oriented, there is still space for scope deals as banks look to increase their reach both geographically and across service offerings.

Scale is even more important than ever as banks strive to manage margin compression.

Banking M&A gets more dynamic

As banking M&A continues to heat up, acquirers will need to deal with a more dynamic environment and a new set of rules.

Among the biggest changes: M&A is getting more competitive with new players entering the game. In the past, private equity (PE) firms focused on aggregating subscale, noncore banking businesses, such as payments, fund administration, and factoring. Now they have extended their reach by buying banks directly. It was PE firm Cerberus that purchased HSBC's retail activities in France, for example. Private equity firms are well placed to absorb underperforming bank assets as they bring fresh equity, strategic focus, strong management, and are willing to make bold investments in technology and digital capabilities.

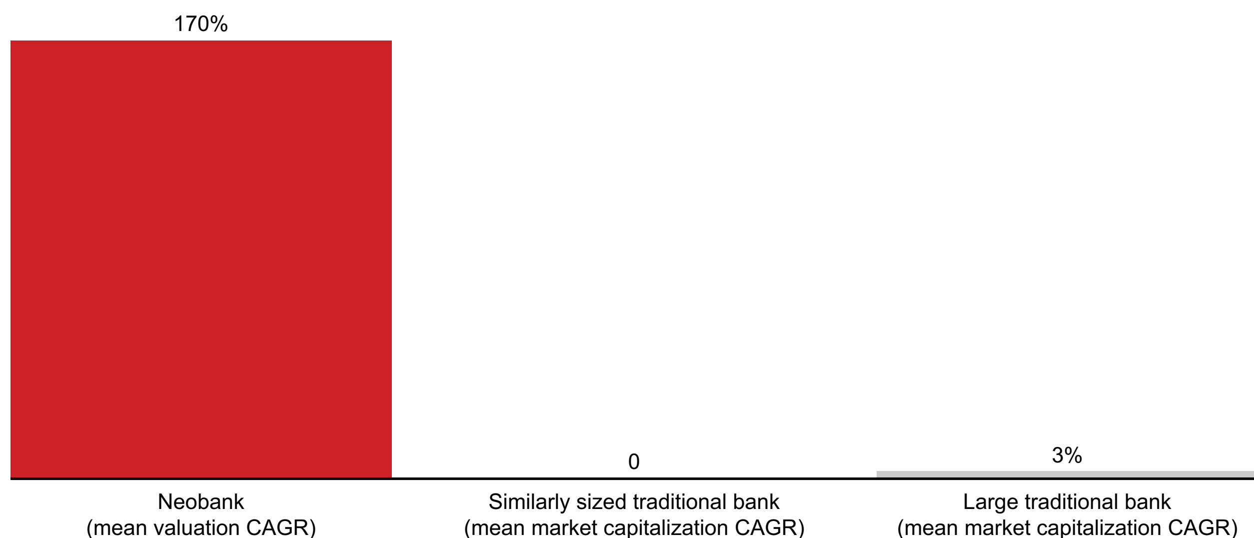
Meanwhile, venture capital firms' funding of innovation at a robust pace is leading neobanks and new digital players to achieve higher valuations than those for large traditional banks (*see Figure 1*). For example, Europe's Revolut is valued at $33 billion, N26 (headquartered in Berlin) is valued at $9 billion, and Brazil-based Nubank went public in an IPO that gave the company a $41.5 billion valuation. Such price tags put them out of the reach of many traditional bank acquirers—and even make them competitors for purchasing the most attractive technology capabilities. In November, Sweden-based neobanking service Klarna paid $124 million for PriceRunner, a comparison-shopping service in the Nordics and UK.

Further pumping up the competition, technology players are directly buying banks. That's what happened when Shopee, Sea Group's e-commerce arm in Southeast Asia, bought Indonesia lender Bank Kesejahteraan Ekonomi.

This changing game will make it more challenging for traditional banks to grow via M&A. To succeed, many will explore alternative methods. For example, more banks will turn to strategic partnerships to build scope and scale. That's what is happening in Asia, where many banks have entered joint ventures with nonbanks to deliver more integrated "banking inside" solutions.

Figure 1: Neobank valuations grew rapidly between 2019 and 2021 while traditional bank market capitalizations saw limited growth

Compound annual growth rate (CAGR), 2019–2021



Notes: CAGR is annualized from monthly capitalizations and valuations; neobank CAGRs are normalized for the relevant valuations occurring between 2019 and 2021; similarly sized traditional banks studied have a market capitalization between $8.5 billion and $15 billion
Sources: Dealogic; Tech Crunch; S&P Capital IQ

For example, Standard Chartered entered a joint venture with National Trades Union Congress of Singapore (NTUC) to set up a digital bank. NTUC owns the largest supermarket chain in Singapore as well as a top insurance company and businesses in healthcare, childcare, and property management. The joint venture will embed Standard Chartered banking in NTUC's ecosystem.

In another growing trend, banks are setting up their own corporate venture funds to invest directly in technology players, as Citi has done with its Citi Ventures unit.

Banking's three big imperatives

Whether they pursue integrations or partnerships, traditional banks will need to focus on delivering strong client solutions at a faster pace if they want to succeed in M&A. That means ending their reputation for being slower and more bureaucratic than technology players.

Success rests on three imperatives.

- Banks need to implement corporate development scanning and due diligence capabilities on par with private equity and venture capital firms, which have turned this into a science. Winning banks will be those able to evaluate targets and opportunities with the right value investment thesis and develop and document the business case. Investment theses will be increasingly centered on revenue generation vs. costs synergies. The best banks will anticipate disruption from the impact of technology players and ESG on the profit pool over the next 5 to 10 years so that they can anticipate long-term sources of value.

- Banks need to have a comprehensive and holistic view of all potential sources of value beyond economic value to identify how to generate the most of it. For example, in Boston Private's acquisition by SVB, technology and talent created additional sources of value beyond growing wealth offerings. The best bank acquirers will invest to assess and identify hidden jewels that can be leveraged for sustainable value creation.

- Finally, banks need to prepare for transformation. With technology and digital accelerating the pace of change, more banks are using acquisitions as a platform or a catalyst for their own transformation. NAB bought Citigroup's Australian consumer banking business to scale its cards platform, for example. In the past, "integrate first and transform later" was a common M&A mantra. The best bank acquirers have already replaced that with "buy and transform now."

Insurance M&A: How Deals Are Changing the Shape of an Industry

Insurers are finding the deals that help them diversify and grow ahead of competitors.

By Simon Porter and Sean O’Neill

At a Glance

- In 2021, more insurance companies acquired capabilities to help them to diversify their offerings.
- More insurers also turned to M&A to reshape their distribution footprint.
- Despite the blockbuster deals of 2021 that never came to fruition, insurers will continue to pursue scale deals that will help them adapt to the industry’s rapid changes.

In recent years, when insurers acquired or divested, it usually was a move to reinforce their core and streamline their businesses. The tide began to shift in 2021 as more insurance companies pursued deals that helped them build out capabilities and broaden their business objectives. It also was a year in which insurers turned to M&A to expand their distribution reach. And it was a year in which blockbuster scale deals ran into big hurdles, reinforcing the importance of tackling regulatory issues upstream.

We’ll look at these themes one by one.

M&A to accelerate and diversify capabilities

In auto insurance, both newcomers and incumbents are accelerating usage and behavior-based offerings, requiring technical capabilities to develop algorithms and effective customer interfaces

as well as a body of data. Most major players have tested the waters. For example, in 2018, USAA launched its SafePilot telematics product, expanding coverage to 34 states last year. To further advance and accelerate its ability to personalize pricing that fits drivers' risk and use profiles, USAA acquired insurtech Noblr in June 2021, with plans for the start-up to run alongside its SafePilot product.

German insurer HDI acquired insurtech Community Life (founded in 2014) to accelerate its digital capabilities for direct-to-consumer and sales partners as well as innovative capabilities such as biometric insurance.

US insurer Lemonade has been steadily expanding beyond its core renter's product, with recent additions of pet and life insurance. Having long foreshadowed its entry into auto, Lemonade officially launched its auto product in November and then quickly announced the acquisition of struggling pay-per-mile car insurer Metromile. The acquisition allows Lemonade to take a big leap forward in technology. More important, however, is the access to customer driving data that Metromile has accumulated since its founding in 2011. Also, Lemonade benefits from Metromile's 49 state licenses, a key to rapidly scaling its business.

German insurer Nürnberger Versicherung became lead investor in insolvent insurtech Getsurance to gain access to innovative products and enhanced digital sales capabilities.

In Asia, digital start-up Singlife merged with incumbent Aviva's Singapore operations, combining Singlife's digital capabilities with Aviva Singapore's product history and advisory services. The merger will combine established financial products and professional financial advice with mobile-first customer engagement. It will bring Singlife's mobile savings and protection solutions to Aviva's large, strong customer base while enabling the company to offer existing Singlife customers a much deeper product range and advisory capabilities.

In the commercial market, American Family's purchase of digital exchange Bold Penguin bolstered its ability to provide options to agents and brokers. Recognizing that its proprietary AmFam or Main Street products will not always be the best solutions for customers, AmFam purchased Bold Penguin's marketplace so that it can offer a range of choices that enhance the customer value proposition while also expanding distribution capabilities.

Covid-19 changed the dynamics of both in-person and direct distribution, leading several companies to turn to M&A to reshape their distribution footprint and capabilities.

M&A to evolve distribution

Distribution remained a critical strategic topic for insurers in 2021. Covid-19 changed the dynamics of both in-person and direct distribution, leading several companies to turn to M&A to reshape their distribution footprint and capabilities.

Liberty Mutual was particularly active in this area. Its announced purchase of State Auto in July positions Liberty Mutual as the second-largest carrier in the independent channel. Liberty quickly followed this move by shifting its exclusive agents into multicarrier digital agency Comparion. Both moves reflect a belief that consumers increasingly will value choice and that in-person selling will remain a strong part of the multichannel distribution landscape.

Allstate's acquisition of National General, which closed in January 2021, was another deal intended to expand the independent agent footprint. At the heart of Allstate's move was a view that the role of the agent will change to involve more in-depth discussions aimed at understanding customers' unique needs and providing them with relevant choices instead of processing information. This strategy requires better data and technology, and it refutes the notion that most consumers will be best served through purely digital channels.

Meanwhile, bancassurance deals continue apace in Asia-Pacific. Allianz Australia completed its acquisition of WestPac's general insurance business and commenced a 20-year exclusive deal to distribute insurance products to WestPac customers. Similarly, AIA formed a 15-year strategic partnership with Bank of East Asia to distribute life and long-term savings products to Bank of East Asia customers.

M&A to build scale

The insurance industry headlines in 2021 were dominated by blockbuster deals that never happened. Chubb's $23 billion to $25 billion offer for The Hartford failed to get off the ground in The Hartford's boardroom. Aon's attempted $30 billion acquisition of Willis Towers successfully navigated European regulators only to be grounded by the US Department of Justice.

While shareholders and regulators may hold a high bar, the insurance industry will continue to see such transformative deals in the years ahead as it grapples with rapid changes. The regulatory environment for scale deals is likely to get tighter. That requires acquirers to think through regulatory review and contingency planning upstream in the deal process vs. downstream. A lengthy deal process generates distraction (real or perceived) and disruption. Key employees leave for more stable pastures, customers can be wooed away in the wake of the uncertainty, and critical strategic priorities and innovation are stalled waiting for the deal outcome. All of this reinforces the need to deeply understand the regulatory hurdles early in the process, ensuring that the deal thesis and market value proposition of the combination will clear the bar and taking a proactive posture to enable an accelerated path.

Why are we doing this deal?

As insurers evaluate their position in the changing marketplace, M&A practitioners need to be clear about how M&A will advance the corporate strategy. That starts by asking three basic questions: How are we going to compete and win in the future? What capabilities and operating model do we need to achieve that? What's the better way to acquire those capabilities and build that model—organic or inorganic?

With that clarity, insurers can effectively pursue deals that will help hasten the achievement of their objectives, giving them capabilities to expand distribution or build scale.

Industries

Payments M&A: The Deals behind the “Buy Now, Pay Later” Boom

After years of megadeals, companies are going for smaller and more selective tuck-in deals.

By Sen Ganesh and Glen Williams

At a Glance

- Following a year of megadeals, 2021 likely will be remembered for tuck-in acquisitions designed to spur growth by adding a diversity of service offerings. Payments-related deal activity rose to $60 billion in value in 2021 from about $40 billion in 2020.
- “Buy now, pay later” is the hottest trend in payments, and companies that provide these service capabilities are rapidly being acquired.
- Visa and Mastercard continue to diversify business away from core cards with a number of tuck-in investments.
- Citigroup’s divestiture of much of its retail banking business (including cards) provides a unique opportunity for local/regional players to dramatically gain market share.

“Buy now, pay later” players also are adding more capabilities to bulk up their offerings and boost growth.

Buying now in "buy now, pay later"

The hottest business in payments is "buy now, pay later" (BNPL). For consumers, it's an interest-free way to defer payments on purchases. For retailers that subsidize the offering, it's a way to encourage conversion and higher average ticket sizes. BNPL has grown at an annual rate of 60% to 70% in the UK in recent years, and it now accounts for 5% of all e-commerce sales. In the US, it is expected to grow 10 to 15 times over the next three years, representing $650 billion to $1 trillion in transactions.

Not surprisingly, incumbent companies in payments are rushing to get into the act. And when they evaluate whether to build or buy, many are discovering that despite high valuations, the fastest way is with M&A. Out of all payments deals, BNPL deals represented 50% of value in 2021, a boom year for M&A in payments.

The megadeal of 2021 was Square's all-stock acquisition of BNPL company Afterpay for $29 billion. Square (now renamed Block) will integrate Afterpay with its seller ecosystem and Cash App, which has about 70 million users. But also there were a number of smaller deals, including PayPal's purchase of BNPL firm Paidy in a $2.7 billion largely cash deal to enable access to its base of more than 6 million customers across Japan.

BNPL players also are adding more capabilities to bulk up their offerings and boost growth. Sweden-based fintech Klarna made six acquisitions in 2021 alone, everything from online trip planner Inspirock to Apprl, a software-as-a-service platform provider that allows content creators and retailers to work together. Klarna also picked up mobile wallet company Stocard, social shopping platform Hero, and artificial intelligence–enabled personalized shopping tool Toplooks during its 2021 shopping spree.

Visa and Mastercard diversify beyond cards

Meanwhile, payments companies must deal with the prospect of credit cards losing share as consumers move to digital and account-to-account payments. One option for them has been to diversify beyond traditional cards by acquiring new payments players, not only in BNPL but also companies offering account-to-account and wallet payments as well as ancillary services such as know-your-customer solutions.

Visa has been pushing into consumer payments with Visa Direct, its global real-time platform for peer-to-peer and business-to-customer payments. The company made two major acquisitions in 2021: European open banking platform Tink and cross-border payments platform CurrencyCloud.

Mastercard has focused its acquisitions on payments infrastructure. It acquired Danish open banking fintech company Aiia, digital identity management company Ekata, blockchain analytics company CipherTrace, and bill pay solutions player Arcus, for example.

Piling up such tuck-in deals, however, is not going to be easy. There is increased regulatory scrutiny involving antitrust concerns in markets in which these companies hold leadership positions. For example, Visa abandoned its $5.3 billion deal for Plaid before it even had a chance to succeed following a US antitrust lawsuit alleging that Visa's acquisition would eliminate a competitive threat to its online debt business.

Using selective deals to scale up

The year 2019 saw large deals among payments companies, with Fiserv's acquisition of First Data, Fidelity National Information Services' acquisition of Worldpay, and Global Payments' purchase of Total Systems Services. This continued in 2020, with deals such as the Worldline and Ingenico merger and Italian payments processor Nexi's $9.2 billion deal for rival Nets, creating Europe's biggest payments firm by volume. There were scope deals, too, such as American Express's purchase of small business online lending platform Kabbage.

In addition to Square-Afterpay, one of the bigger deals involved PayU's acquisition of Indian payment gateway BillDesk for $4.7 billion to help it expand into emerging markets. More common, though, was larger techs pursuing tuck-in acquisitions, such as Fiserv's $206 million purchase of Pineapple Payments and Stripe acquiring India's Recko.

Smaller payments fintechs also selectively acquired to bulk up and penetrate new markets. That was the case with payments-as-a-service platform Rapyd's $100 million deal for Icelandic payment company Valitor, for example.

US technology firms expanded into payments in 2021. Bill.com, an accounts payable and receivable management company, acquired Divvy, a payment and business budgeting platform, while Tyler Technologies, a technology provider, acquired government payments company NIC, to name a few.

In an effort to increase focus on its global corporate, commercial, and wealth businesses, Citigroup has divested its retail banking business in 13 markets, most of them in Asia, providing a unique opportunity for local and regional banks to scale up their credit card business and gain share in the consumer space. National Australia Bank (NAB) took advantage of the opportunity by buying Citi's consumer business, a move that put NAB in the No. 2 position in the country's credit card business. Similarly, in the Philippines, UnionBank purchased Citi's consumer business to boost growth in its retail banking sector. And UOB Group acquired Citi's consumer banking franchises in Indonesia, Malaysia, Thailand, and Vietnam to increase its scale across Southeast Asia.

The challenges ahead

Payments deals are coming with increasingly high valuations, making it more challenging to do large-scale deals. In the fourth quarter of 2020, the median enterprise value (EV)–to–trailing 12-month revenue multiple was 15 times. The Square-Afterpay deal carried a 42 times EV/revenue

multiple. At the same time, the growing popularity of stock deals has made it difficult for banks to participate. As a result, players need to be clearer and more selective on the strategic rationale for acquisitions (e.g., geographical expansion, new payments capabilities, or value-added services).

Deals intended to provide a specific capability come with their own challenges. Because of the complexities involved with integrating diverse payment platforms, players may struggle to realize the intended benefits. Combining companies' infrastructures can create redundancies in functionality and operations. It can also make maintenance more expensive, which in turn can boost processing costs.

As companies struck deals, private equity (PE) investors showed increasing interest in payments industry M&A. For example, Advent International and Eurazeo, a French-based PE and venture capital firm, bought Planet, an international payments and transaction processing service provider. Private equity firms' involvement increases the competitiveness for deals. Corporate buyers need to focus on integrating payments players to their core business to add value through sales and costs synergies.

Finally, as deals in BNPL grow in number and as this business takes shape, regulatory scrutiny for consumer protection concerns will continue to become more of an issue in markets around the world. Companies acquiring to expand a geographical presence need to be prepared to address possible regulatory issues—and, when necessary, be prepared to walk away from deals.

Industries

Asset Management M&A: Building Scale and Differentiation

Deals are one way to avoid this sector's valley of death.

By Matthias Memminger and Avishek Nandy

At a Glance

- Winners in the asset management industry are succeeding either by building scale or differentiating offerings, using M&A for both.
- 2021 will be remembered for a big shift in asset management as large banks move back into the space after a two-decade hiatus.
- Strategic acquirers create scale and differentiation, even as they outsource and sell infrastructure, while private equity acquirers are building infrastructure platforms.

They call it the "valley of death," and its inhabitants are asset management companies that either are subscale or have undifferentiated products.

Large and differentiated asset management companies continued to emerge as winners in 2021. Large-scale players outgrew the market, while differentiated players further expanded their margins. Their differentiation came through a variety of means: access to alpha; environmental, social, and corporate governance (ESG); or specific investment themes. Meanwhile, companies that are neither large nor differentiated—those trapped in the valley of death—fell behind despite the tailwind boost of a bull market driving top-line growth across the entire asset management industry.

This dynamic delivered a clear narrative for asset management M&A in 2021. Strategic acquirers, such as banks and insurers, sought to build scale and differentiation. Meanwhile, private equity (PE) investors were snapping up the opportunity to invest in outsourced architecture, focusing on rolling up infrastructure platforms and building out "multi-boutique" differentiated firms.

Banks get back in the game

The year 2021 will be remembered for a paradigm shift in asset management. For the first time in two decades, many large banks looked to reenter asset management after most had deprioritized the business in the 1990s and 2000s.

Why now, after such a long hiatus? The rationale for reentering may be linked to asset management's capital-light infrastructure and the potential for high returns on equity. Following recent regulatory pushes to increase capital requirements for most core banking activities, this has become a highly attractive segment for bank portfolios.

Large banks are using M&A to quickly scale up their asset management offering. In a $7 billion deal, Morgan Stanley acquired Eaton Vance's $500 billion portfolio of assets under management, strengthening its leadership in the US market. Meanwhile, JPMorgan Chase, UBS, Deutsche Bank, and others are actively in the market for asset management deals, having been on the losing end of several large acquisition attempts.

Banks also are increasingly looking to differentiate their offerings in terms of geographies and products, and M&A is a key avenue. For instance, Goldman Sachs' acquisition of NN Investment Partners expands its footprint into ESG, the European market, and the insurance asset management business.

While the American and European banks are further along in this trend, the Asian asset management market remains a collection of smaller, localized battlefields. Global asset managers have yet to establish a meaningful position outside regional hubs such as Singapore and Hong Kong, so the market remains highly fragmented. That said, consolidation continues, though on a smaller scale than in the US and Europe.

For instance, Allianz Group announced in July that it would acquire PT RHB Asset Management Indonesia, an asset manager with $480 million under management. In India, Sundaram Asset Management announced its acquisition of the asset management business of Principal India, and HSBC is in talks to purchase the India-based L&T Mutual Fund. In China, the China International Capital Corporation is on the lookout for acquisition targets in Asia as global banks make inroads into the Chinese market.

Private equity is paying attention, too

Private equity investors also are showing interest in this field, though they are taking a different tack. While corporate acquirers focus on building scale and accessing new markets, many PE investors are investing in scalable infrastructure, such as platforms, administration, software, or data.

These models are attractive as banks and insurance asset managers are selling and outsourcing their infrastructure capabilities. The scalable platform businesses also lend themselves well to PE roll-up strategies. For example, leading fund Hellman & Friedman showed the attractiveness of this investment strategy with its acquisition, management, and eventual $8.7 billion IPO of Allfunds in spring 2021.

Takeaways for M&A practitioners in asset management

All things considered, asset management is becoming an increasingly attractive M&A market. The sector achieves strong top-line growth, high profitability despite some margin erosion, and overall positive macro trends, such as high savings rates, low interest rates, and anticipated high inflation—all of which contribute to inflows to the industry. In such a market, leaders will continue to position themselves for success by building scale or differentiating their offerings.

M&A will be especially competitive as strategic acquirers look to build and expand over the next few years. If valuations continue to rise and as M&A becomes an even more attractive option in the asset management sector, it also will become more strategically important. Those that sit out are likely to be left behind.

Wealth Management M&A: Scale Up and Digitize

Even as companies race to consolidate, they learn that scale is not enough.

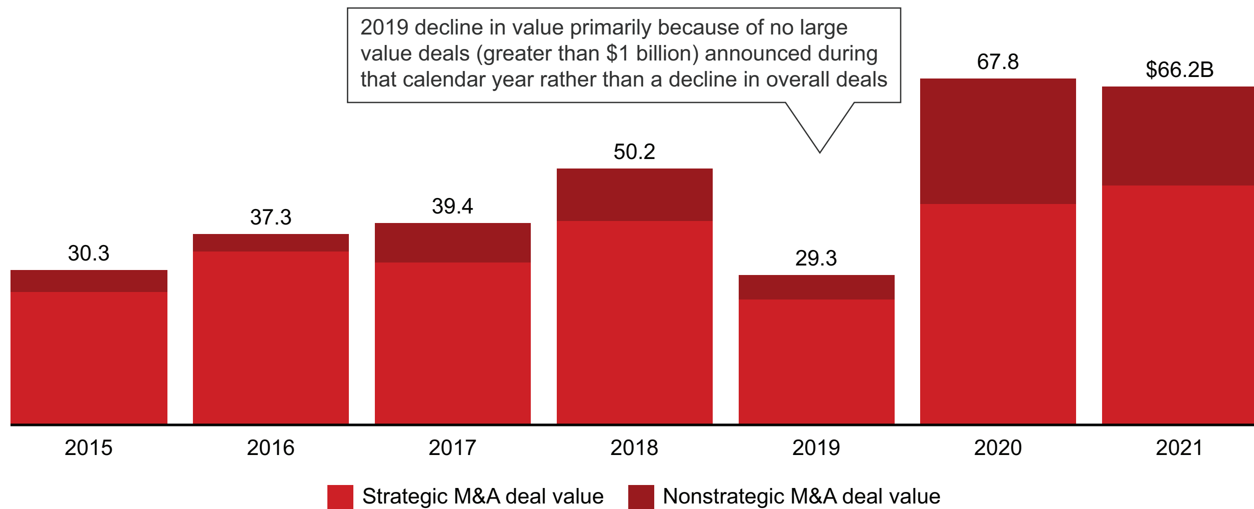
By Antonio Rodrigues and Markus Habbel

At a Glance

- The wealth management industry has seen prolific M&A activity in all sectors over the past few years as it trends toward market consolidation. And 2021 set a record in strategic deal value.
- Strategic buyers are pursuing both scale and scope deals to expand their businesses and acquire new wealth-tech capabilities.
- While much of the activity is in the US, dealmaking in Europe and Asia is not far behind.
- Many of these trends are expected to continue, propelled by private equity's interest in wealth-tech companies, the financial strength of incumbents, and the critical need for digital capabilities.

The wealth management industry has entered a phase of accelerated M&A activity. Deal value records were set in 2020 and 2021 as companies sought to reshape the industry across major sectors (*see Figure 1*). Corporations looking to stay current with the market are using both scale and scope deals to get ahead of the emerging disruption in the industry.

Figure 1: Another record year for strategic deal value in Wealth Management M&A



Source: Dealogic

Continued consolidation in wealth management

The North American market is leading the global industry in M&A activity, with clear deal theses around both scale and scope plays.

Many companies find that scale is a necessity to remain competitive. Consolidation provides access to brand and marketing benefits as well as the capital needed to invest in large-scale technical improvements to keep capabilities current.

M&A has proven the most efficient way to build scale across the industry's main sectors.

- The fragmented North American Registered Investment Advisor (RIA) sector is home to so much activity that there's a consolidation deal taking place nearly every week. It's to the point that some platforms are starting to achieve true scale. For example, in early December, Toronto-based aggregator CI Financial announced that it is buying both RegentAtlantic, a $6 billion New York-based registered investment adviser, and Columbia Pacific Wealth Management, a $6.4 billion adviser based in Seattle and San Francisco. The deals represent two of CI's 30 acquisitions in the US, pushing the company's total US RIA assets to $115 billion.

- Similarly, the large US retirement market also is turning to M&A to consolidate. Empower Retirement completed no fewer than four scale acquisitions over the past two years.

- And in US brokerage, market leaders are consolidating to create efficiencies in an increasingly competitive business. Consider Schwab's acquisition of TD Ameritrade.

But even as they grow via acquisitions, companies are finding that scale alone is insufficient for leadership. Scope deals are becoming more critical with the emergence of wealth-tech players that serve new and adjacent wealth management markets. Funding for wealth-tech assets reached a record $12.7 billion during the first three quarters of 2021, more than doubling the amount invested in all of 2020.

Incumbent wealth managers are reacting to the new competition and its new technology capabilities by turning to M&A. JPMorgan Chase bought Nutmeg, a UK online wealth management platform in 2021. Goldman Sachs got in the game with its acquisition of United Capital in 2019, followed fast by its purchase of Folio Financial in 2020.

In the retirement sector, scope deals are aimed at giving buyers retail capabilities. For example, Empower's 2020 acquisition of Personal Capital created an end-to-end financial planning service for customers. Meanwhile, Creative Planning is buying Lockton's US retirement business to expand the range of services it offers.

Europe and Asia are a few years behind

Much of the recent wealth management deal activity has taken place in the US, but companies in Europe and Asia are just a step behind. Many of the same themes are playing out in those markets, with companies turning to dealmaking to scale up and to digitize their customer and adviser journeys.

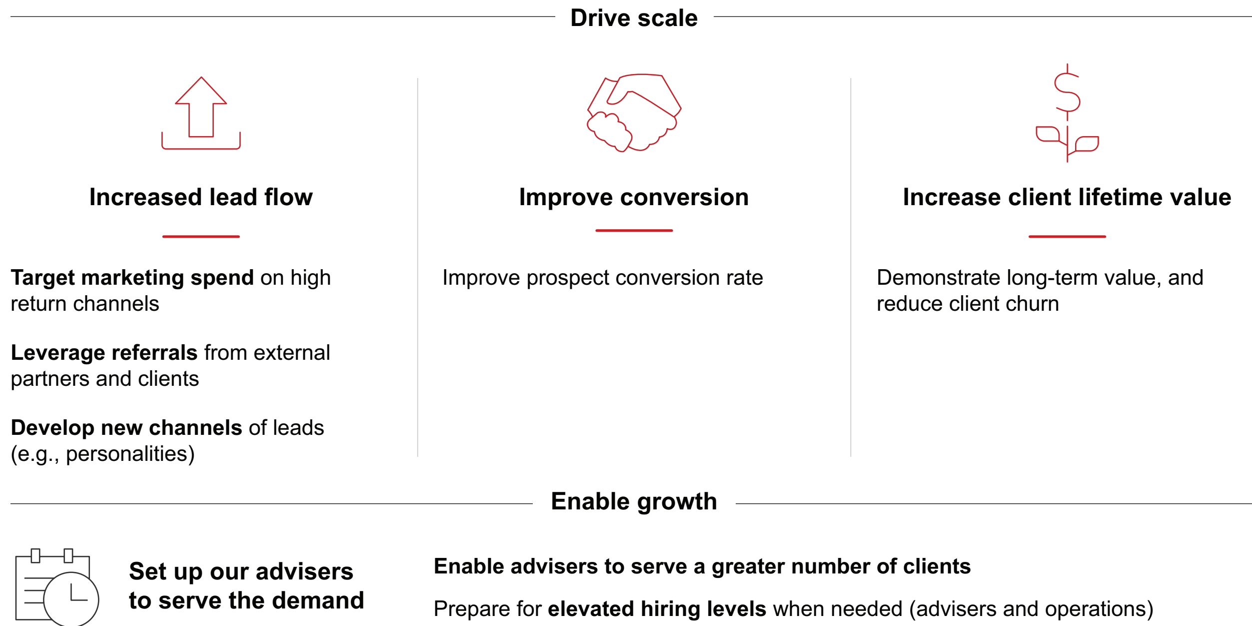
In Europe and Asia, deals are aimed at building regional growth as well as both upmarket and down-market expansion. Some of the activity takes the form of partnerships or investments instead of traditional M&A. For example, UBS expanded its product offerings by partnering with wealth-tech platform Envestnet, while LGT's stake in digital LIQID gives it access to new customer groups.

Three market forces to watch

Wealth management M&A practitioners should expect to see a prolonged period of activity ahead. Three market forces are at play: increased private equity interest, incumbents' continuing search for higher growth adjacencies, and the ongoing need for technological innovation.

Private equity has been a major force in market consolidation, especially in the US RIA sector. In 2016, the sector saw 68 private equity deals; by 2020, that nearly doubled, to 122 deals. Strategic buyers must anticipate continued competition from private equity firms, which are sitting on significant dry powder and are eager to acquire wealth-tech companies.

Figure 2: A multifaceted value creation plan is key to wealth management M&A success



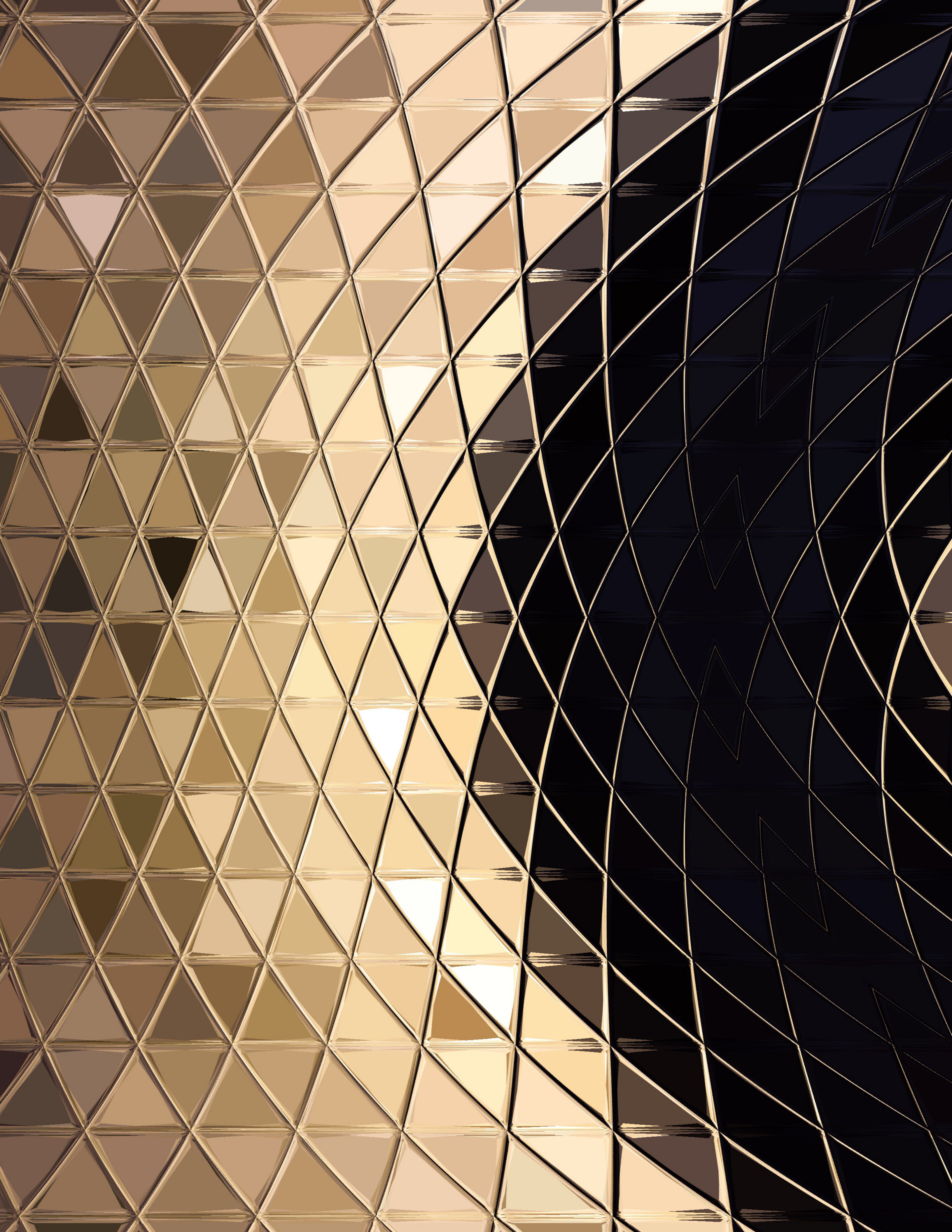
Source: Bain & Company

Meanwhile, incumbent players are continuing to enjoy a profitable period. They have the financial power for acquisitions that provide higher growth platforms and that widen their scope and build regional scale.

Finally, technological innovation will continue to propel M&A activity. It's becoming increasingly critical for companies to deliver key digital capabilities, such as digital advisers and client experiences, while simultaneously relying on technology to increase productivity. These demands will continue to lead companies to the M&A arena, with players acquiring capabilities through scope deals as they also seek deals that will give them the scale needed to fund growing tech investments.

Heightened activity turns up the pressure on buyers. The mounting competitiveness delivers higher valuations, and buyers need to work harder than ever to justify deals and make them succeed. The best companies work to develop a clear deal thesis, look to all sources of value creation as part of the deal, and then execute with a well-devised integration plan (see *Figure 2*). As part of this effort, more buyers will look beyond cost synergies to revenue synergies and take a disciplined approach to achieving them (see "Bringing Science to the Art of Revenue Synergies").

Above all, companies need a clear view on M&A strategy and a willingness to jump into the fray. As more companies use M&A to build scale economics and acquire today's capabilities that will become tomorrow's table stakes, those that sit on the sidelines are likely to end up staying there.



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Regions

India M&A: Insurgents Are Going Shopping

First-time buyers have taken over dealmaking in India.

By Vikram Chandrashekhar and Karan Singh

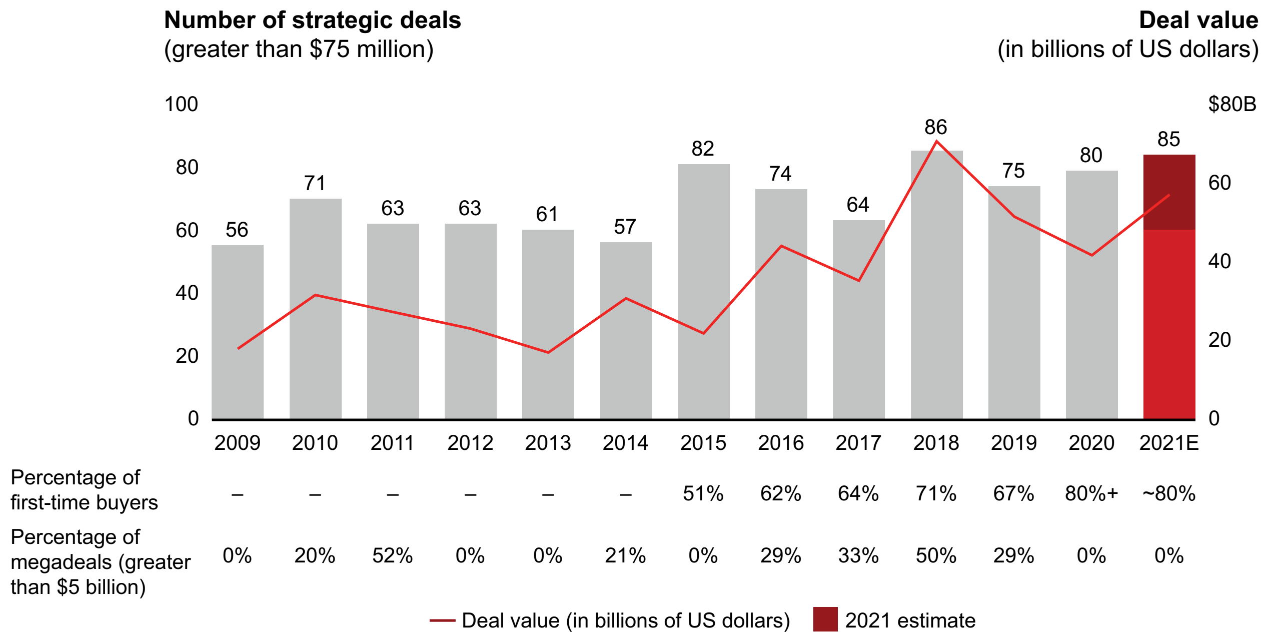
At a Glance

- First-time buyers represented about 80% of all M&A in India. In 2015, they accounted for 51% of deals.
- More companies doing more deals means that average deal size is now smaller, with fewer $5 billion or more megadeals and more deals in the $500 million to $1 billion range.
- Scope acquisitions outside a company's core business now account for 4 out of 10 transactions.
- Financial investors are betting big in M&A. Private equity investment doubled in the first half of 2021 over the same period a year earlier.

The past two years have seen more first-time buyers of companies than ever in India; they now account for about 80% of the country's M&A vs. 51% in 2015 (*see Figure 1*). These purchasers are aggressively buying to meet shareholders' expectations of 27% annual growth in India, a sevenfold increase over the past three years.

First-time buyers have abundant capital and historically low interest rates on their side. Many of them see acquisitions as a way of getting ahead of disruption in a fast-paced market in which 46 of the country's 69 unicorns emerged in 2020 and 2021 alone, affecting sectors from finance to retail to technology.

Figure 1: More first-time buyers in India are turning to M&A to drive growth



	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021E
Percentage of first-time buyers	–	–	–	–	–	–	51%	62%	64%	71%	67%	80%+	~80%
Percentage of megadeals (greater than $5 billion)	0%	20%	52%	0%	0%	21%	0%	29%	33%	50%	29%	0%	0%

Note: 2021 estimate annualized based on data through mid-October
Sources: Dealogic; S&P Capital IQ

Many among this new breed of acquirers are insurgents buying to build scale rapidly, enter new geographies, add new lines of business, or deliver a full omnichannel experience to customers. For example, education tech insurgent Byju has been on a buying spree, investing more than $2 billion into 11 acquisitions, including its $1 billion purchase of Aakash Educational Services, an offline test prep company. Byju bought the company to build an omnichannel offering for its test prep vertical.

PharmEasy, India's leading e-health player, made multiple acquisitions to enter new verticals, including a 66% stake in Thyrocare to strengthen its high-margin testing business by tapping into Thyrocare's wide network of collection centers.

In India, more deals are designed to transform a business, not just grow it.

These and other deals reflect a shift in the type of M&A sweeping India. More companies doing more deals means that average deal size is now smaller, with fewer $5 billion or greater megadeals and more deals in the $500 million to $1 billion range. Also, more deals are designed to transform a business, not just grow it. In India, scope acquisitions outside a company's core business aimed at entering a new market or gaining a much-needed capability are steadily advancing to match the volume of scale deals. Scope deals now account for 4 out of 10 transactions.

Another huge theme involves reshaping portfolios through M&A. Over the past 18 years, we have analyzed the performance of more than 100 conglomerates in India and Southeast Asia. During that time, we tracked a gradual erosion in shareholder returns among conglomerates. The big culprit? A large portion of a typical conglomerate's business is in unattractive or lower-multiple industries. Conglomerates that have reshaped their portfolios using acquisitions and divestitures, however, have delivered three times the total shareholder returns as those that failed to actively manage their portfolios.

Indian conglomerates are taking note and overhauling their portfolios through M&A, betting on profit pools of the future in areas such as digital, renewables, electric vehicles, and fintech. To fund these moves and manage their portfolios, they are pruning ownership in legacy assets or in subscale positions that could be more valuable in another parent's hands. For example, the Mahindra Group has reshaped its portfolio and exited loss-making businesses, with multiple divestments, including a potential sale of its stake in SsangYong. The Tata Group is actively reshaping its portfolio and has completed 21 deals over the past two years, including multiple acquisitions to build out its super app and to consolidate its position in consumer goods.

This comes at a time when competition for deals is getting hotter. Among the reasons: Financial investors are betting big on M&A. For example, private equity investment doubled in the first half of 2021 over the same period a year earlier.

Implications for dealmakers

India's M&A trends have important implications for dealmakers.

Don't sit it out. The year 2022 should be a bumper year for M&A in India. Executive teams know this is a unique moment of transformation and that M&A has an important role to play. Our research clearly indicates that winners reshape portfolios in times of turbulence. During the 2008 financial crisis, for example, Indian companies that acquired or divested outperformed their peers two to one in earnings before interest and taxes growth over the subsequent five years.

Companies sometimes feel constrained not by a lack of capital but rather by an executive team's limited bandwidth and its lack of confidence in successfully integrating a scope acquisition. This is particularly true for first-time buyers, but it also is the case for more seasoned dealmakers doing first-time scope deals. The good news is that the risks in scope deals are known and understood and that a strong playbook can be deployed for value creation.

Reshape the portfolio. Future growth engines (what we call "Engine 2") can hedge against disruption of a core business, or they can help a company take advantage of shifting business boundaries in newly accessible adjacent markets. Leadership teams must make resource allocation decisions between businesses that will generate cash, drive growth, and boost valuation—and they must use this moment to reshape portfolios through acquisitions and divestitures.

Deploy the appropriate M&A playbook. Done correctly, scope deals can unlock tremendous value. That was the case with Tata Consumer Products, which generated an 84% excess return above the Sensex. Scope deals can be difficult to execute, however, and they can destroy value without the right playbook. First-time buyers need to build a repeatable M&A model for success.

For example, in scope deals, it is not sufficient just to understand the standalone value of a target and joint value creation potential. Dimensions such as culture, sustainability, and consumer sentiment should also be evaluated as a standard part of due diligence. Also, the best companies have a clear integration thesis and an equally clear understanding of the critical few decisions that will make or break the success of the deal. The integration thesis needs to translate the deal thesis into a roadmap of what needs to be integrated (or not integrated), when to integrate, and how to go about the integration.

Regions

Japan M&A: The Emergence of Transformative M&A

More Japanese companies are willing to shed businesses and embrace a new version of themselves.

By Takashi Ohara

At a Glance

- Among Japan's 50 biggest deals of 2021, eight were outbound deals aimed at transforming the acquirer's portfolio.
- At about the same rate, companies in Japan are selling original businesses that are not core to their future strategy. With their growing interest in Japan, private equity firms are eager buyers of divested assets.
- Transformative deals are challenging because they are both scope/capability as well as cross-border deals.

Japan is in the midst of a boom in outbound M&A. Deals for companies outside of the country have grown to represent as much as 40% of total deal value over the past five years. While many of these deals are aimed at expanding a company's geographic reach or product offerings, a surprising number now reflect a different trend: transformative M&A.

Transformative M&A comes at a time of digitization, business model disruption, and sluggish domestic market growth for many companies' core businesses.

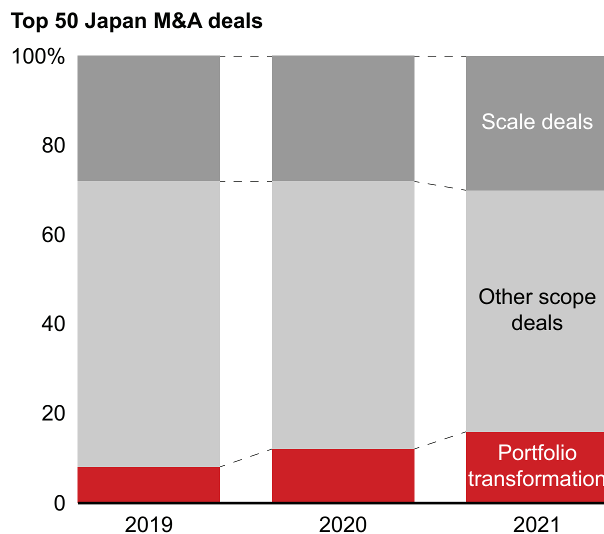
After years of resisting the need to sell unrelated assets, Japanese companies are taking steps to reshape their portfolios.

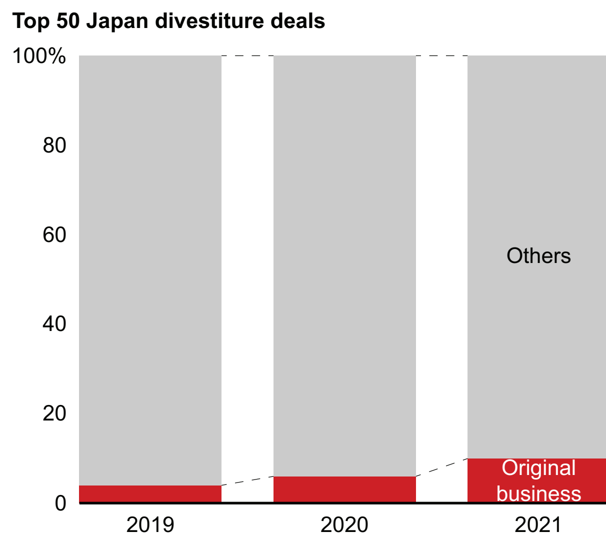
Among Japan's top 50 outbound deals in 2021, eight were intended to transform the portfolio of an acquirer (typically a conglomerate) to create a path to sustainable profit growth (*see Figure 1*). The pursuit of transformative M&A comes at a time of digitization, business model disruption, and sluggish domestic market growth for many companies' "Engine 1" core business. Contributing to the transformative M&A trend, companies selling assets to fund the acquisitions have a ready buyer in private equity, which has expanded its interest in M&A in Japan.

To see examples of transformative deals, look no further than Hitachi's $9.6 billion acquisition of GlobalLogic, a US-based digital solutions provider. It was Japan's largest deal of 2021, and its purchase had significant implications for Hitachi's portfolio. Hitachi bought GlobalLogic as a catalyst to accelerate the growth of its Lumada Internet of Things (IoT) solution by gaining access to the target company's differentiated digital engineering capabilities.

Portfolio transformation also was the impetus behind the country's second-largest outbound deal of 2021, Panasonic's $7.1 billion purchase of Blue Yonder, a US-based digital supply chain management solutions provider. The deal is aimed at helping Panasonic hasten the shift from hardware to software in the supply chain management field.

Figure 1: Transformative M&A deals became more prevalent in Japan in 2021





Notes: The top 50 Japan M&A deals are domestic and outbound deals only. The top 50 Japan divestiture deals are domestic and inbound deals only; original business refers to business present during inauguration/early stages of a target company; 2021 represents from January to October
Sources: Recof; Nikkei; companies' investor relations/websites; Bain analysis

Unlike typical scale M&A, these deals aren't purely focused on generating short-term cost synergies. Also, they typically are bought at high deal multiples that make it difficult to justify only by EBITDA growth. Instead, buyers hope to grow their own EBITDA multiple by sending a clear message to the capital market that these acquisitions will help transform their business portfolio for the midterm to enable future sustainable growth.

Divestitures of original businesses

Business portfolio transformation cannot be a one-sided matter of adding new assets. It needs to be balanced by carve-outs or divestitures. While Japanese conglomerates have been eager to acquire, they have been slower to divest their original businesses, which sometimes represent a substantial portion of their revenue and are often viewed as sanctuary businesses.

Yet more companies are now making the decision to jettison businesses that are no longer in accord with their future strategy. After selling Hitachi Chemicals and other major assets, the Hitachi conglomerate announced selling Hitachi Metals, one of its original businesses, to a consortium led by Bain Capital for $7.5 billion in 2021. Hitachi Metals was viewed as a noncore asset as the parent company shifted its focus to IoT solutions as a key driver of growth. Another example is Japanese chemical conglomerate JSR selling its elastomer business to Eneos, a Japanese energy conglomerate. Divestitures of original businesses represented 10% of Japan's 50 top deals in 2021.

What it takes to make transformative M&A successful for companies in Japan

Transformative deals can be more challenging because they are both scope/capability deals as well as cross-border deals. But buyers can boost the odds of success by focusing on three key areas:

- **Devote more effort to developing a clear deal thesis**. Because these are not typical scale deals aimed at generating cost synergies, it's critical to build a clearly articulated strategic rationale and hypothesis for how the deal will deliver top-line synergies. That rationale needs to be clearly set as shared strategic guidelines among buyers as well as target companies.

Companies selling assets to fund the acquisitions have a ready buyer in private equity.

- **Protect the acquired company's business momentum, culture, and talent**. Too often, Japanese acquirers take the instinctive route of pulling target companies into their traditional corporate culture, and as a result, they destroy the unique culture that fostered the innovation and made the target so attractive. The better option often is to preserve the target's standalone business momentum, culture, and talent—and subsequently to foster cross-polarization.

- **Execute deals with a well-devised M&A strategy and sufficient M&A capabilities**. Japanese companies have somewhat bitter experiences when it comes to cross-border deals. In our analysis, 20% of such deals end up with book value impairment while another 10% end up with withdrawals or are sold at lower values. An underlying reason is that Japanese companies tend to overpay—they usually pay 40% more than the global average. Winning companies have a clear M&A strategy and deal playbook with rigorous capabilities for screening targets, performing disciplined diligence, and integrating where it matters. They learn from each deal, honing their capabilities for repeatable success.

Regions

China M&A: Tighter Regulations Mean New Rules for Deals

Multinational companies need to proactively evaluate their existing footprint and portfolio strategy as it relates to China.

By Hao Zhou

At a Glance

- New government moves are creating challenges in industries such as e-commerce, education, and ride-hailing. For instance, Alibaba was fined $2.8 billion for antitrust violations.
- Even with a stricter regulatory environment, opportunities can be found for dealmakers hoping to grow along with China. In some industries, regulations favor M&A and joint ventures.
- For both multinationals and domestic companies, successful deals will take more time and rigorous planning.

Here are the three big moves by the Chinese government in 2021 that everybody is watching:

- After years of a hands-off approach toward e-commerce super-platforms and their required exclusivity from small merchants, the government has suddenly cracked down. The State Administration of Market Regulation penalized Alibaba, JD.com, and Meituan with historic fines, citing antitrust concerns. It was a move that significantly increased costs for the super-platforms and changed business approaches for small merchants as well. This reflects the evolution of Chinese policy over the past year.

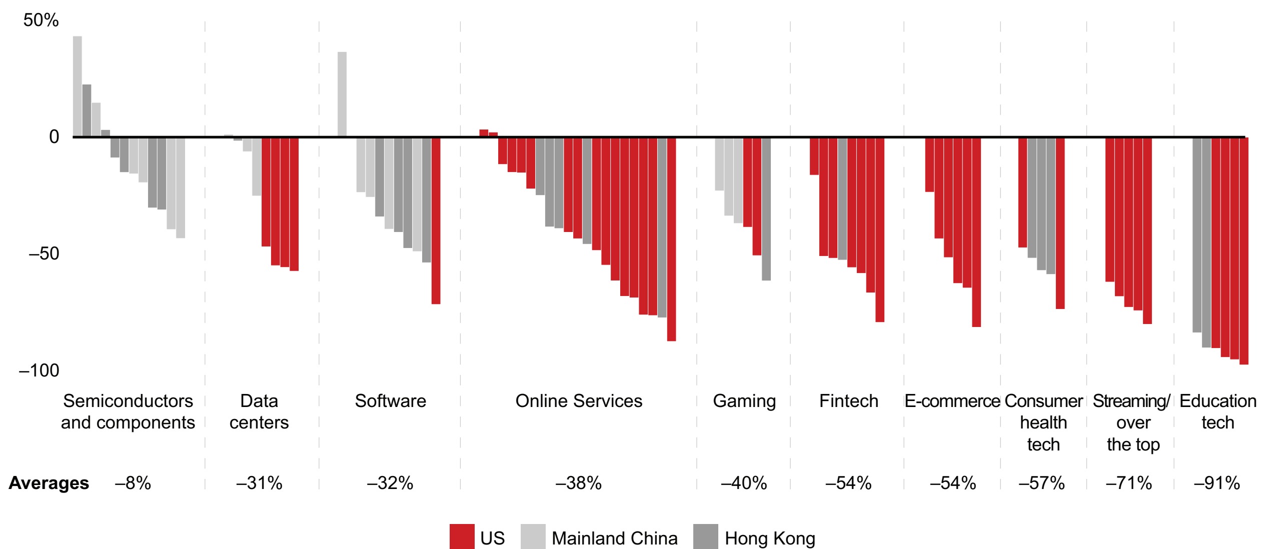
- Common prosperity is now a top priority for the Chinese government, which is aiming to narrow the country's wealth gap and expand the middle class. Among the steps taken: imposing price caps on new housing, expanding medical insurance coverage, and eliminating off-school K–12 tutoring (a huge business that was available only to wealthier parents).

- China has been a leader on the frontier of digital innovation, yet data privacy has been relatively loosely controlled up to this point. In the interest of national security and privacy, the government has recently taken steps to protect sensitive data, ranging from geolocation data to the financial data of state-owned enterprises. This was most dramatically demonstrated when, days after the massive ride-hailing platform Didi's IPO on the New York Stock Exchange, the Chinese government conducted a sweeping crackdown on the company for misuse of customer data.

These and other sudden regulatory developments took an immediate toll on China-related publicly listed equities, especially tech stocks (*see Figure 1*). While the impact has yet to be felt on M&A, there's a general concern about the near-term viability of deals.

Figure 1: Stock prices were hit in 2021 across all tech sectors in China

Percentage of price changes in China tech stocks
(February 11, 2021–September 23, 2021)



Note: Each bar represents stock price impact for a single company in the relevant sector
Sources: Wind; Bloomberg

Implications for corporate M&A

While dealmaking has slowed in recent years, cross-border and domestic M&A is still an option, with deals such as China International Marine Containers' (CIMC) $1 billion acquisition of A.P. Møller-Maersk's box manufacturing unit, Maersk Container Industry, a deal that confirms CIMC as the world's largest container producer, and China Resources Capital's purchase of Viridor, a leading British waste disposal company. Other deals included Germany's BASF's joint venture (JV) with Hunan Shanshan Energy Technology and Chinese dairy company Mengniu's acquisition of Milkground, a popular insurgent cheese maker that has grown at an annual rate of 112% since 2018.

China's changing regulatory environment, however, requires dealmakers to adapt accordingly.

All dealmakers need to plan for longer approval times, and they also need to be prepared for extensive information disclosure requirements to address antitrust and data security issues.

Multinationals need to treat their China business separately from the rest of the corporation. For example, new regulations require many of the critical infrastructure elements (such as data centers) to be placed locally. That means multinationals must assess their current operations and add necessary backbone operations for China when looking to acquire within the country.

In fact, all multinational companies need to proactively evaluate their existing footprint and portfolio strategy as it relates to China. Corporations need to heighten the separation of personal data or company data related to their products or services that could pose security risks, and they are seeing the growing importance of collaborating with local authorities on these data privacy issues. While many companies have treated China as a separate business region to comply with the local requirements, for some companies, a carve-out could be the best option for preserving value. Companies should be continually revisiting their business strategy and understanding both the investments needed to comply with new regulations in China as well as the alternatives available via divestment.

Winning means taking advantage of areas in which the government is encouraging deals. New opportunities are emerging for investments in sectors such as fast-moving consumer goods. Strategic investors in these sectors should double down and more aggressively allocate resources to identify and invest in attractive targets.

Indeed, more strategic investors are actively making early-stage investments in China through corporate venture capital or by teaming up with venture capital (VC) or private equity firms. For example, Nestlé established its China incubator in 2018 and, two years later, committed $30 million as a cornerstone investor for Tiantu, a renowned local VC fund.

There was a time when the only way to gain entry into China was by establishing a JV with a local company. When foreign companies were permitted to operate on their own, some found great success while others encountered difficulty adapting to China. Now, more multinationals are revisiting the JV option, especially with domestic companies that have advanced technology or critical capabilities and resources to accelerate local R&D, approval, and route to market.

For example, in 2017, AstraZeneca established a JV with Chinese Future Industry Investment Fund (FIIF), a biopharma-focused private equity fund that is partly owned by the China State Development & Investment Corporation. The JV company, Dizal Pharmaceutical, incorporates all the scientific and technical capabilities of AstraZeneca's Innovation Center China, while FIIF contributes funding and expertise toward establishing strategic partnerships in China. Conceived as part of a regulatory push to produce pharmaceuticals in China, Dizal has since achieved exponential growth.

China's regulations may have tightened in various sectors and created stricter measures to protect sensitive data and national security, but this does not diminish the importance of this market for strategic buyers. Even as the country moves into a new era of regulation, China will remain an attractive market for growth and investment. For many industries, it's still the world's hottest market.

Regions

Brazil M&A: A Year of Strong Activity

Macroeconomic factors, proceeds from initial public offerings, and government sales of state-owned assets kept M&A activity roaring.

By Luis Frota and Felipe Cammarata

At a Glance

- M&A activity in Brazil reached a 10-year peak in 2021.
- The majority of large deals were scale deals for consolidation across diverse industries, such as utilities, healthcare, and retail.
- While macroeconomic forces contributed to the high deal activity, two factors were specific to the Brazilian market: a record-setting number of initial public offerings generating proceeds for acquisitions and the government's aggressive sale of its assets and state-owned businesses.

In line with global trends, Brazil's deal activity reached a 10-year peak after a strong 2020. Transaction value totaled $66 billion in 2021, which is less than the value reached in 2010, but that was a banner year in which the concession of pre-salt to Petrobras and multiple consolidations in the telecom industry pushed the numbers sky-high. The 10-year record total deal value in 2021 even considers Brazilian real depreciation against the US dollar.

Large deals (those valued at more than 10 billion Brazilian real) accounted for about 50% of the total deal value in 2021. Most deals were scale deals aimed at consolidation, and they cover a diverse set of industries. For example, in healthcare, Hapvida Participacoes e Investimentos and Notre Dame Intermedica Participacoes merged. In utilities, Cedae concession, the Rio de Janeiro sanitation company, was acquired by Iguá and Aegea. The energy industry's big deal was Raizen's purchase of Biosev. In auto rental, Localiza merged with Unidas, and retail saw Carrefour acquire Grupo BIG.

Meanwhile, small deal activity got a boost from the increased number of acquisitions in the tech sector. Tech deals, which have doubled in count since 2016, currently account for around 30% of the existing number of deals, but they account for only about 5% of total deal value.

What's behind these numbers? A positive macroeconomic environment propelled by low interest rates and a favorable currency for international investors is at the top of the list. Also, 2021 saw a rise in the amount of capital raised through initial public offerings (IPOs) and used for acquisitions. There was a constant push for innovation via the acquisition of new technology capabilities. And successful, well-capitalized companies acquired less-strong competitors, many of which were weakened during the pandemic. A final yet important factor was the government's push to sell state-owned assets, such as refineries, and its sale of water, sewage, and other concessions.

While all these forces played a critical role in sustaining M&A activity, two of them are specific to the Brazilian situation and merit special attention:

- the rising number of IPOs; and
- the government agenda of selling state-owned assets.

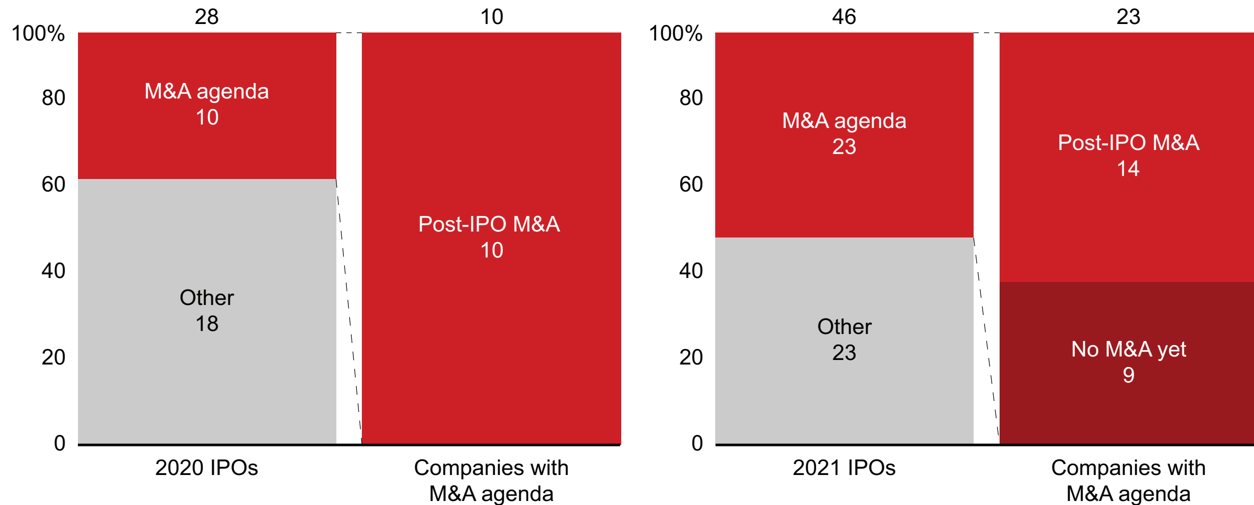
The IPO factor

After a 12-year historic high in 2020, with nearly 43 billion Brazilian real raised in 26 IPOs, 2021 set a new record, with 64 billion Brazilian real raised in 46 IPOs. This positive scenario is also influenced by macroeconomic factors, such as high liquidity, low interest rates, and a steep increase in the number of local investors looking for higher returns in capital markets.

According to IPO prospectuses, 50% of the companies that had an IPO in 2021 planned to deploy part of the proceeds toward acquisitions, with 61% of them ultimately involved in acquisitions *(see Figure 1)*. Yet there is evidence that more purchases may be forthcoming in 2022: All the companies that went public in 2020 and that planned to use those IPO proceeds for M&A eventually made at least one acquisition.

Successful, well-capitalized companies acquired less-strong competitors, many of which were weakened during the pandemic.

Figure 1: 50% of Brazil's IPOs in 2021 had an M&A agenda compared with 36% in 2020



Note: IPOs without a registered prospectus were considered in "other"
Sources: Public offerings and IPOs available at B3's website; companies' IPO prospectuses; Bain analysis

The government agenda factor

The year 2021 has brought an uptick in the purchasing of government-owned companies. Since 2016, the Brazilian government has pursued an ambitious program to raise private capital across several initiatives, including concessions, sales of public assets, and private-public partnership projects. This program has fueled a number of M&A deals and boosted the value of those deals. New legislation and regulations were approved to enable access to private capital, such as the new "Marco do Saneamento" legislation. Additionally, there was a shift in the overall strategy in which state-owned companies sell assets, such as Petrobras refineries.

Although the overall result of 64 billion Brazilian real is less than initial expectations, it represents the impact of the state agenda. Examples include the regional concessions in water supply and sewage (in Alagoas, Amapá, and Rio de Janeiro) representing around 30 billion Brazilian real, airport concessions totaling 3.3 billion Brazilian real, and Petrobras' refineries sales for 9.1 billion Brazilian real. And more concessions are in the government agenda, including:

- Eletrobras (energy) privatization already was approved by Congress and could begin in the first half of 2022, with the Brazilian government diluting its majority stake by issuing new shares.

- Eight port terminals were added to the current infrastructure concessions to be auctioned in 2022, including a terminal from Porto de Santos, the largest port in Brazil.
- At least three more auctions are already planned for water supply and sewage concessions facilitated by "Marco do Saneamento."

2022 outlook

While these tailwinds could continue to propel M&A activity in Brazil, there are some potentially significant headwinds that could derail efforts. In addition to global risks, such as supply and demand shocks and pandemic uncertainties, Brazil faces a much higher rate of inflation than its international peers, which could require further intervention from the central bank. Growth estimates point to lower growth rates for 2022.

Moreover, presidential elections will be held in 2022. That could bring additional instability and make companies more cautious—to the point at which they might postpone major strategic decisions.

Bain's Bedrock Beliefs on How to Create Value from M&A

A repeatable model helps to generate higher total shareholder returns.

By David Harding and Joerg Ohmstedt

This report necessarily spends most of its time on what is new and different in the world of M&A. For example, we have argued that executive teams need to modify their playbooks to retain critical talent; account for new business needs, such as environmental, social, and corporate governance; and capture revenue synergies.

All of that said, there are some fundamental truths about M&A that have withstood the test of time. The analyses discussed below have been replicated multiple times over the past 20 years. The answer remains the same across all the different cohorts we have studied.

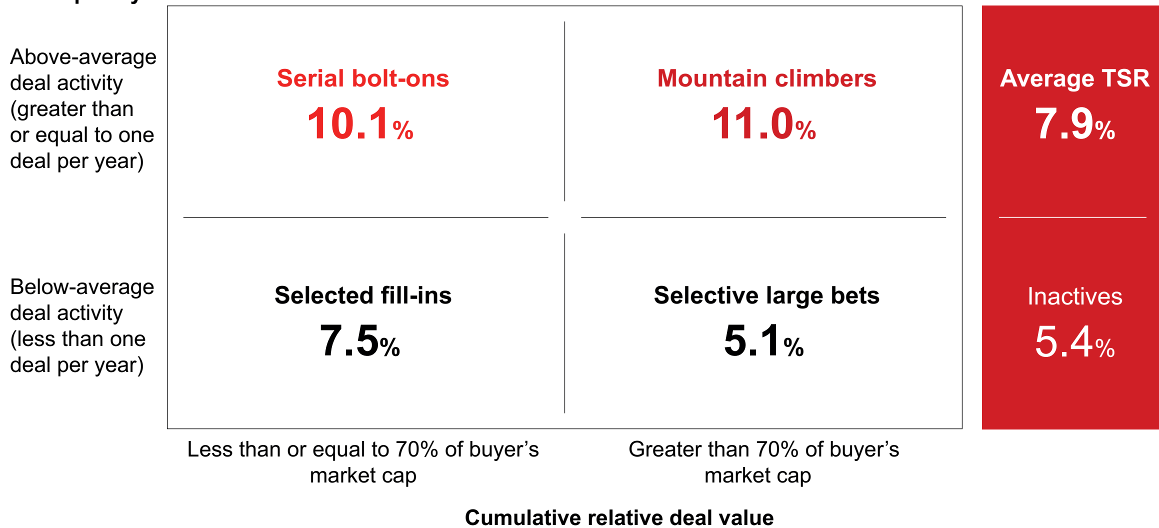
Headline: If you want to be successful at M&A, develop a repeatable model. Do it often, learn from your mistakes, and make it a material part of your business. Done right, it will generate higher total shareholder returns (TSRs).

Fast fact: About 84% of publicly listed companies have participated in M&A over the past decade.

We have assessed the returns to shareholders of the different M&A strategies employed by a universe of 2,897 publicly traded companies from around the world.

It turns out that two axes define a lot of what differentiates M&A performance—frequency (how many deals you do) and materiality (how much of it you do). We have outlined the 10-year compound annual growth rates for the TSRs of four groups of acquirers by deal frequency and materiality. The 16% of companies that did no deals reported an annual TSR of 5.4% (*see Figure 1*).

Figure 1: Repeatable M&A is the winning strategy



Note: Cumulative relative deal value is the sum of relative deal size (deal value divided by market capitalization three months prior to announcement) across all deals between 2011 and 2020
Sources: Dealogic; Bain M&A database, 2021 (N=2,897)

It does not take a lot of deals to become a frequent acquirer, about one per year. To be a material acquirer does require heft—namely, 70% or more of your market cap from acquired companies over a decade. Still, 18% of all the companies in our sample were considered material acquirers.

So what do these trends tell us?

First, consistent M&A activity over economic cycles contributes to higher TSR. This finding holds up year after year, across industries. Deal success and deal failure is more a matter of cumulative experience and capability in making a deal and less a function of standalone deal circumstances.

Second, similar to most things in life, you get better at what you do when you do it repeatedly. Companies that acquire frequently (serial bolt-ons) tend to outperform the average company on TSR (10.1% annual).

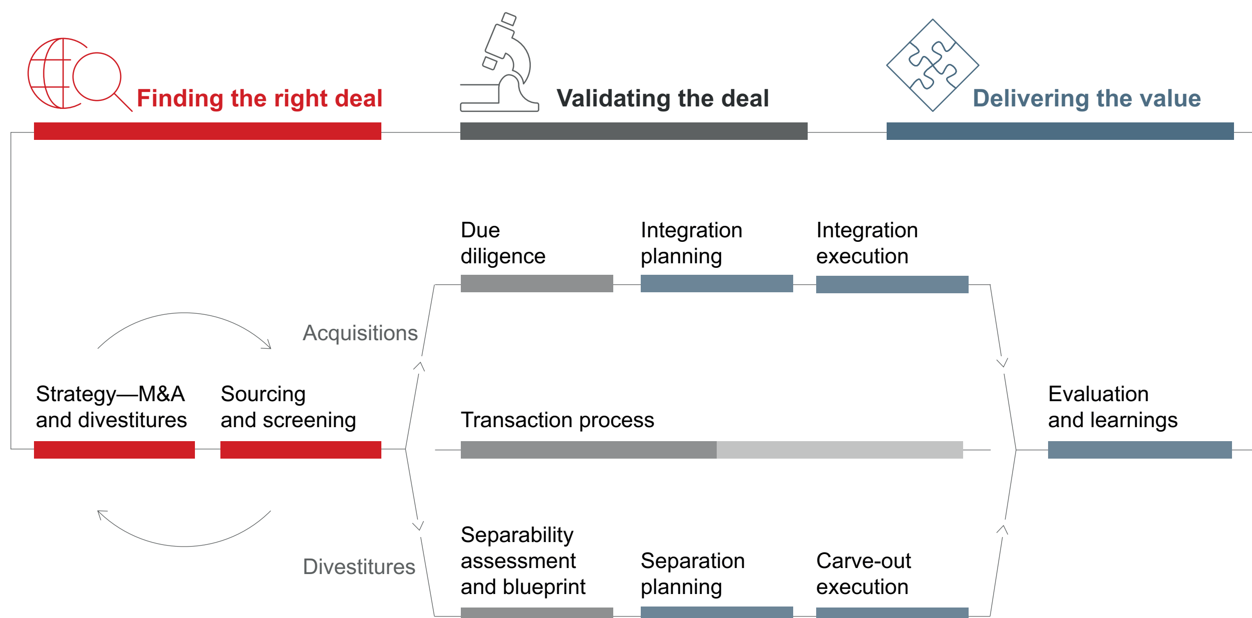
Third, companies that not only acquire frequently but that also develop the capabilities to undertake larger deals do even better. We call these companies mountain climbers, and their 11.0% annual TSR leads the class. Investors have come to recognize this.

We spend a lot of time studying mountain climbers to understand their distinguishing capabilities. Two mountain climbers, Thermo Fisher Scientific and Hitachi, are highlighted in the following section. More broadly, we have identified and track 334 mountain climbers. Many are well-known success stories, including Ahold Delhaize, Alimentation Couche-Tard, Assa Abloy, Bristol-Myers Squibb, Broadcom, Charter Communications, Cigna, Melrose Industries, Qualcomm, Salesforce, Schneider Electric, Siemens, Sony, Stanley Black & Decker, Symrise, Toyota, Tyson Foods, UnitedHealth Group, and so on.

Mountain climbers follow an integrated approach to managing M&A from strategy to integration, which strengthens and reinforces their repeatable M&A capability with each deal (*see Figure 2*).

In addition to being frequent and substantial acquirers, mountain climbers also proactively manage their portfolios by pruning noncore businesses. It's another big factor that contributes to their success. According to our analysis, more than 90% of mountain climbers divest, and the average mountain climber will divest about 27% of its market capitalization over a 10-year period. These companies deploy a repeatable process for systematically identifying assets for divestiture and preparing them for sale.

Figure 2: If done right, M&A creates value—especially with a repeatable model built upon a disciplined M&A capability



Source: Bain & Company

Another big learning from our study comes from the failure of companies that make infrequent, big bets. We refer to such companies as "selective large bets": They are infrequent acquirers, but they undertake large deals relative to their market capitalization. Among all companies studied, these are the worst performers over time as their limited acquisition experience, combined with investment in a large deal, usually results in poor deal outcomes. They generated only 5.1% in annual TSR from 2010 to 2020.

Going forward, an even higher premium will be placed on building a repeatable M&A capability that delivers successful outcomes across multiple deal types—small and large, scale and scope. The leap from small deals to large deals is a big one as is the one from scale deals to scope deals. We believe that the new wave of M&A—in particular, those involving capability-driven scope deals—will require a fundamentally different approach to realize the value. Companies will need to adapt and modify their diligence and integration playbooks as they pursue scope deals for growth and potentially more transformative, capability-driven scope deals.

Infrequent acquirers that undertake large deals relative to their market capitalization are the worst performers over time.

What mountain climbers do differently

While every company will have a distinct strategy and M&A roadmap that accounts for its industry and competitive dynamics, we've distilled some of the practical actions mountain climbers take to underpin their repeatable M&A capability. What we have learned is that there is no silver bullet that guarantees success. Instead, we see the best rigorously applying learnings from past deals across the entire M&A process to increase their chance of success. Here we show two fairly distinct approaches that have powered two companies toward winning in their respective industries.

Thermo Fisher Scientific, a leading US biotechnology product development company, has brought together several acquisitions over the past 10 years to deliver a more than tenfold increase in its share price. Its M&A capability is widely recognized as a strong differentiator and a sustainable growth lever.

After experiencing an $8 billion loss in 2009, Japan's Hitachi announced that it would shift away from its comprehensive electronics conglomerate portfolio. In 2015, Hitachi began restructuring its portfolio. To that end, the company acquired to fortify its new core, systematically divesting unrelated businesses to fund the acquisitions.

What drives Thermo Fisher Scientific's repeatable M&A capability?

Finding the right deal	• **Using organic and inorganic levers for growth:** Thermo Fisher Scientific redeploys 60% to 75% of its capital to M&A, 10 points to 25 points more than competitors, while driving above-market organic growth of 4% to 6%. Capital deployment incorporates the impact from active portfolio pruning through divestitures. • **Building new growth vectors through M&A:** The company consistently uses M&A to enter growing technological segments through large platform deals and then builds scale through smaller tuck-ins to round out capabilities. With each successive acquisition of leading assets in targeted growth markets (for instance, microscopy, contract development and manufacturing, and bioproduction), Thermo Fisher Scientific has built a more comprehensive and integrated offering for customers. • **Ongoing target screening and relationship building:** The company proactively develops deal perspectives on a broad range of companies within its core markets as well as attractive adjacencies. This comprehensive, thesis-driven approach to deal screening allows Thermo Fisher Scientific to move quickly and sometimes exclusively to strike attractive deals.
Validating the deal	• **Confidence in synergy assessment:** With its accumulated experience, Thermo Fisher Scientific can identify and quantify potential revenue synergies in addition to cost synergies with strong conviction. • **Being open to new sources of value:** After the deal close, Thermo Fisher Scientific stays open to discovering new sources of value beyond revenue synergies and joint R&D through capability sharing that has often unlocked higher growth in acquired companies.

What drives Thermo Fisher Scientific's repeatable M&A capability?

Delivering the value	• **Strong connections between deal team and integration team:** The integration team is supported by leaders that were part of the deal/due diligence team, ensuring that the deal thesis and sources of value translate into an integration thesis that guides planning. • **Integrating at speed:** Thermo Fisher Scientific has built a repeatable and rapid approach to integrations, often reporting cost and revenue synergies ahead of schedule. Successful integrations near the core (Life Technologies, Affymetrix, IntegenX) enabled successful replication of the approach to adjacencies (FEI, Patheon, Brammer Bio). • **Reusing a common but customized approach:** Thermo Fisher Scientific has codified common processes into repeatable integration playbooks that are tailored and applied differently to each acquired company, depending on the integration thesis and situation.

What drives Hitachi's repeatable M&A capability?

Finding the right deal	• **Multiyear M&A roadmap:** Hitachi's transformation of the business portfolio is guided by a multiyear strategic roadmap involving both acquisitions and divestitures. Revisited and realigned every three years, Hitachi's most recent midterm management plan saw respective four times and five times increases in investment from the previous two midterm plans. • **Focus on growth deals:** Strategic investment areas include the IT, energy, and industry sectors as well as North America and Asia-Pacific as focus regions

What drives Hitachi's repeatable M&A capability?

Validating the deal	• **Validating the growth potential:** A key purpose of the company's acquisition activity is access to global/international customer bases and high-growth business areas, such as the robotic systems integration business that the JR Automation together with the acquisition of KEC Corporation provided. • **Limiting capital outlays while strengthening the business:** A creative leadership team used a cash-free merger between Hitachi's automotive supplier business and three Honda affiliate suppliers, creating a leading global components supplier and doubling Hitachi's scale in the parts business.
Delivering the value	• **Realizing synergies while leveraging the global talent gained through acquisition:** With the strategic objective to win in the global market, Hitachi moved its railroad headquarters to Europe and put executives from its subsequent acquisition on Hitachi Rail's management team. Even as Hitachi improved the acquired business's technology and operations, it stressed the need to learn from the acquired business as well. • **Transforming into a truly global company:** Hitachi is strengthening the group-wide standardization of global operations—for instance, by adopting enterprise resource planning templates that are based on Hitachi ABB Power Grids' global operations, expanding shared services using its core business systems and infrastructure service platforms, and building a group-wide customer relationship management system.

Methodology

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

Deal details and aggregate statistics (such as value, volume, multiples) were sourced primarily from Dealogic's M&A database for this annual report. Full-year 2021 data was updated as of January 2022.

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

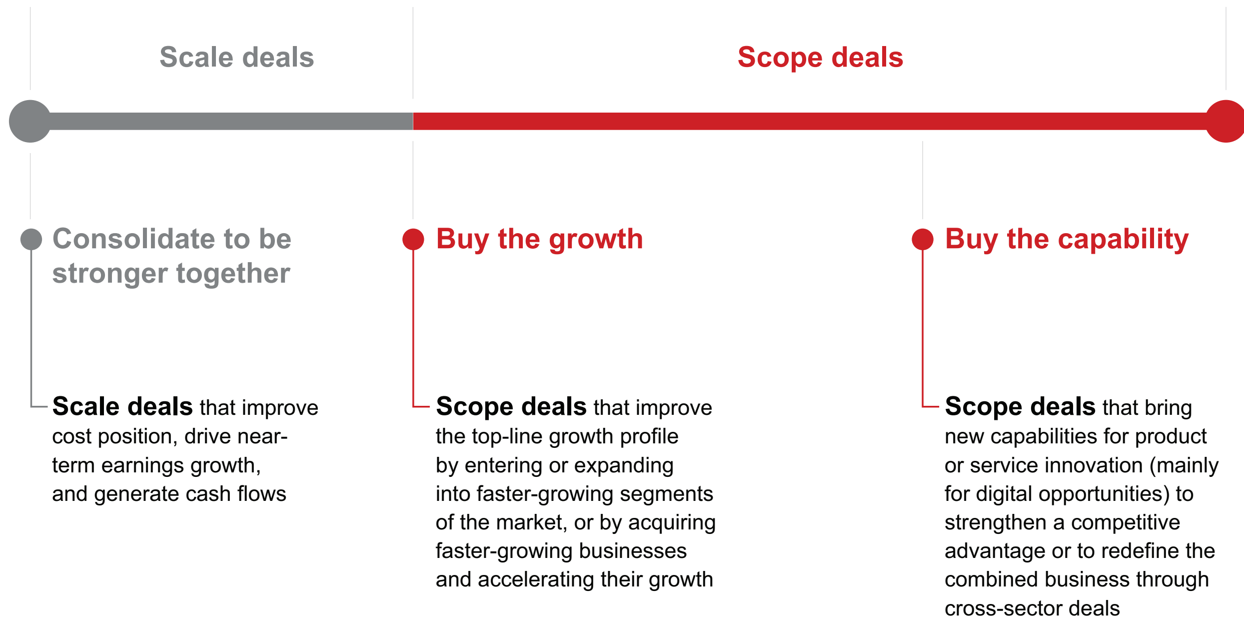
Scope vs. scale

To understand the nature of M&A activity, we first identified the top 250 strategic deals for each year (top 190 strategic deals for 2021 year-to-date through September, since the analysis was concluded in October). From the initial list of deals with values greater than $1 billion, as reported by Dealogic, we excluded nonstrategic deals. These include asset or property acquisitions, financial investments, internal reorganizations, and minority stake acquisitions.

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

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

Exhibit A: About the methodology



Source: Bain & Company

The 2021 M&A practitioners' survey

In partnership with the Gerson Lehrman Group and AlphaSights, we conducted a survey of 281 M&A practitioners. The survey ran in October 2021 in the US, Canada, Brazil, UK, Germany, France, Croatia, Sweden, Switzerland, Japan, India, and Australia. Survey participants held senior executive roles with the title of vice president, senior vice president/executive vice president, director, C-suite, or owner at companies with greater than $100 million in annual revenue, and they were responsible for M&A decision-making processes at their company.

About Bain & Company's M&A value creation study

Bain has been studying corporate M&A activity for two decades. We conducted our first quantitative study of company performance as it relates to acquisition activity in 2011 and 2012 and have updated the study multiple times, including in 2021. The findings were confirmed across both studies spanning two decades.

The quantitative research reviewed the financial performance and M&A activity of 2,897 publicly listed companies from the end of 2010 through the end of 2020. The initial sample included all publicly listed companies from 17 developed markets for which full financial data was available. We then excluded companies with revenue lower than $500 million in 2010 and those with major swings in their earnings before interest and taxes margin around 2010 or 2020.

To compare company performance, we used total shareholder return (TSR), defined as stock price changes assuming reinvestment of cash dividends. We calculated average annual TSR using data reported by Capital IQ. We analyzed M&A activity by including all deals—approximately 32,750—announced by the companies in the sample between the beginning of 2011 and the end of 2020. The data was based on information provided by Dealogic and included all deals in which a company had made an outright purchase, an acquisition of assets or of a majority interest, or in which multistep deals have been consolidated into a single deal. For deals with undisclosed deal values, we apply a median deal value benchmark, calculated for each sector from disclosed deal values as a percentage of acquirer market capitalization, capped at $750 million.

We then analyzed the acquisition activity for each company by calculating the acquisition frequency and cumulative relative deal value. Acquisition frequency was calculated as the average number of acquisitions per year over the period from the beginning of 2011 to the end of 2020. Cumulative relative deal value was calculated as the sum of deal value divided by market capitalization three months prior to announcement for all deals from the beginning of 2011 to the end of 2020. These metrics characterizing deal activity were then related to the TSR performance of various acquirer cohorts.

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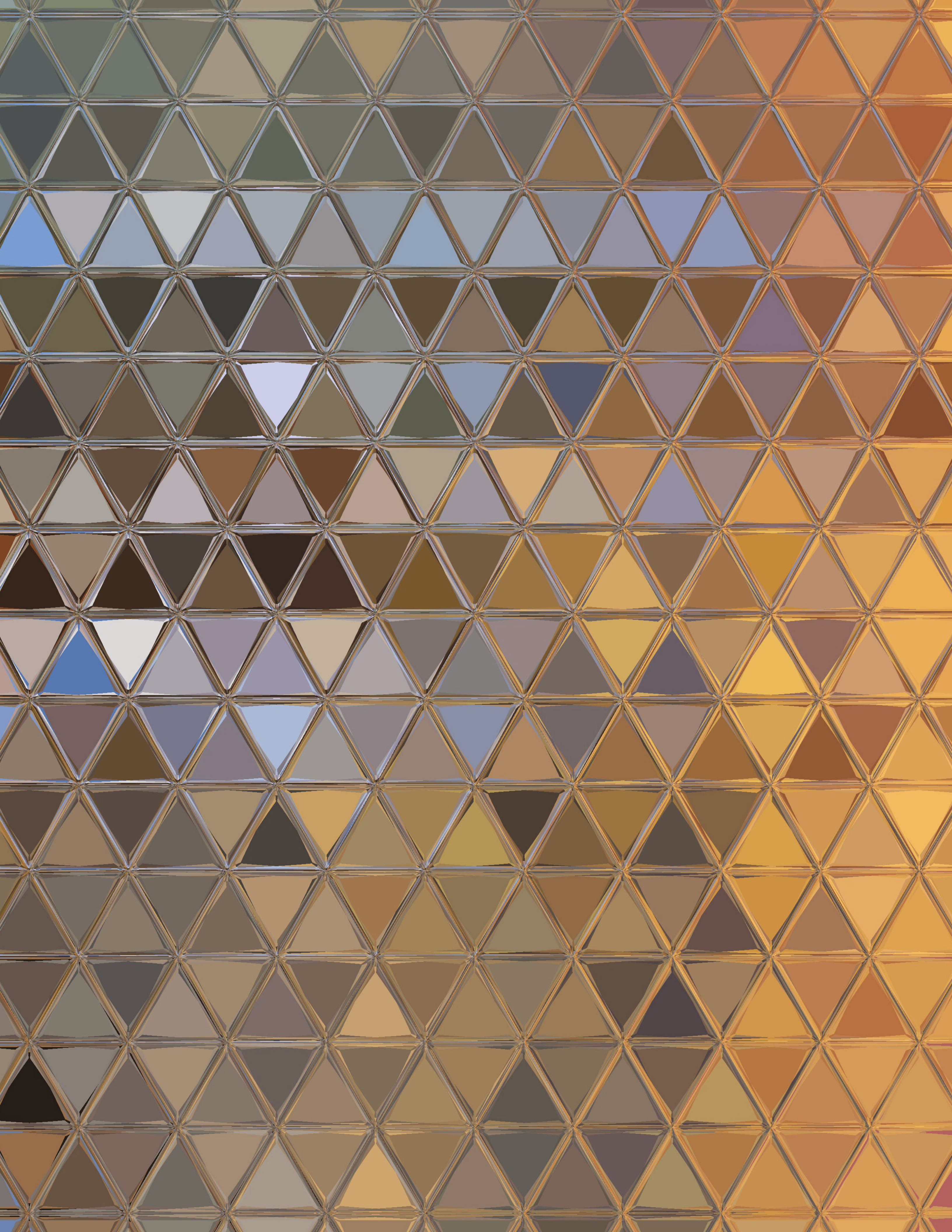

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Across 63 offices in 38 countries, we work alongside our clients as one team with a shared ambition to achieve extraordinary results, outperform the competition, and redefine industries. We complement our tailored, integrated expertise with a vibrant ecosystem of digital innovators to deliver better, faster, and more enduring outcomes. Our 10-year commitment to invest more than $1 billion in pro bono services brings our talent, expertise, and insight to organizations tackling today's urgent challenges in education, racial equity, social justice, economic development, and the environment. We earned a gold rating from EcoVadis, the leading platform for environmental, social, and ethical performance ratings for global supply chains, putting us in the top 2% of all companies. Since our founding in 1973, we have measured our success by the success of our clients, and we proudly maintain the highest level of client advocacy in the industry.

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