M+A

SEMI-ANNUAL LEADERS SURVEY

2017

MORRISON FOERSTER

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M&A Leaders Survey

Morrison & Foerster / 451 Research

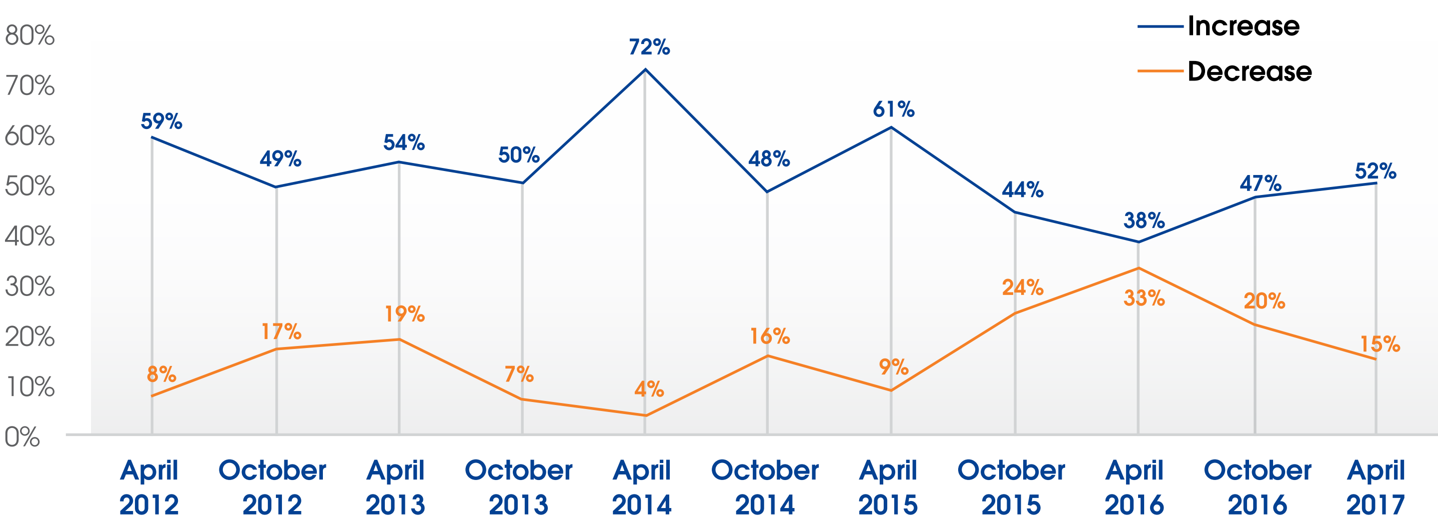
Tech M&A to accelerate, as dealmakers offer strongest forecast in two years.

Despite a slow start to 2017, tech M&A activity is expected to accelerate over the course of the year, according to the prevailing view in the semi-annual M&A Leaders Survey from 451 Research and Morrison & Foerster. Slightly more than half of the respondents (52%) forecast that deal flow will top last year's level– more than three times the 15% of respondents who indicated that year-over-year activity would decline in 2017. The projection in our just-completed survey represents the most-bullish outlook in two years.

Tech M&A Activity Outlook

Forecast Change in M&A Activity

Source: M&A Leaders Survey from 451 Research / Morrison & Foerster



If the sentiment does come through in increased activity for the rest of the year, it would also mark a dramatic reversal from the start of 2017. In the first quarter, tech acquirers announced 12% fewer transactions than they did in Q1 2016 or Q1 2015, according to 451 Research's M&A KnowledgeBase. Of course, 2017 comes after the two highest years of tech M&A spending since the internet bubble burst. Collectively, acquirers in 2015 and 2016 announced deals valued at more than $1 trillion, according to the M&A KnowledgeBase.

Trump Trade

Part of what will help M&A accelerate this year, at least in the view of a plurality of survey respondents, is the guy sitting in the White House. Four out of 10 (41%) forecast that President Trump's future economic policies will stimulate dealmaking– almost twice the 22% who said his policies will slow M&A. The results from the latest survey, which come as Trump moves toward to the end of his ceremonially important first 100 days in office, indicate a substantial reversal from the results of our previous survey last October, which came amid an acrimonious battle with Hillary Clinton for the White House. At that time, nearly one-third (31%) of respondents said the election battle had slowed M&A, which was five times the 6% who said deals had sped up.

Tech M&A Activity

What Impact Has President Trump's Economic Policies Had on M&A?

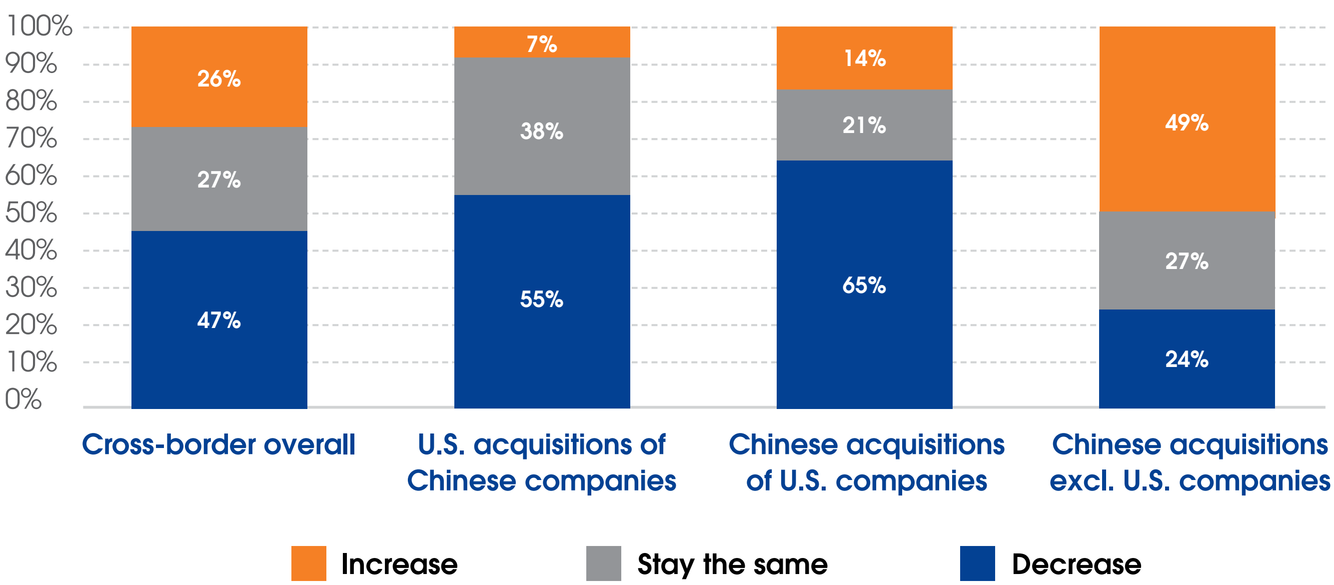
Source: M&A Leaders Survey from 451 Research / Morrison & Foerster

However, any boost that Trump and his policies might give to M&A won't extend globally, according to the survey. Quite the opposite, in fact. Nearly half of respondents (47%) said Trump being in the White House will slow cross-border acquisition activity, nearly twice the 26% who said the policies of President Trump – who campaigned on an "America First" platform – will accelerate international dealmaking. We would highlight the fact that the bearish forecast for cross-border M&A is almost exactly the inverse of the positive influence Trump is expected to have on overall tech dealmaking, according to our survey respondents.

Tech M&A Activity

What Impact Will President Trump's Policies Have on M&A?

Source: M&A Leaders Survey from 451 Research / Morrison & Foerster



Given that Trump singled out China in some of his most caustic comments (and outright threats) among all of the U.S. trading partners, perhaps it isn't surprising that M&A between the two largest economies in the world is expected to be particularly difficult during his presidency. Two-thirds of survey respondents (65%) predicted that Chinese acquirers will slow their purchases of U.S. tech companies while Trump is the CEO of America. That's more than four times the 14% who said the opposite. The forecast almost certainly means that the record spending levels by Chinese companies on U.S. tech assets will quickly and emphatically drop. In 2016, according to the M&A KnowledgeBase, buyers based in China spent more on U.S. tech vendors than the previous five years combined, including an unprecedented 10 transactions valued at more than $1 billion.

Similarly, but on the other side of the trade, survey respondents also overwhelmingly forecast that U.S. companies won't be nearly as active acquiring in the world's most-populous country during Trump's presidency. More than half (55%) said U.S. companies will do fewer tech deals in China, compared with just 7% who predicted an uptick. That sentiment is already coming through in the actual deal flow, where Chinese acquirers of Chinese tech assets have outnumbered U.S. buyers of Chinese tech assets three to one, according to the M&A KnowledgeBase.

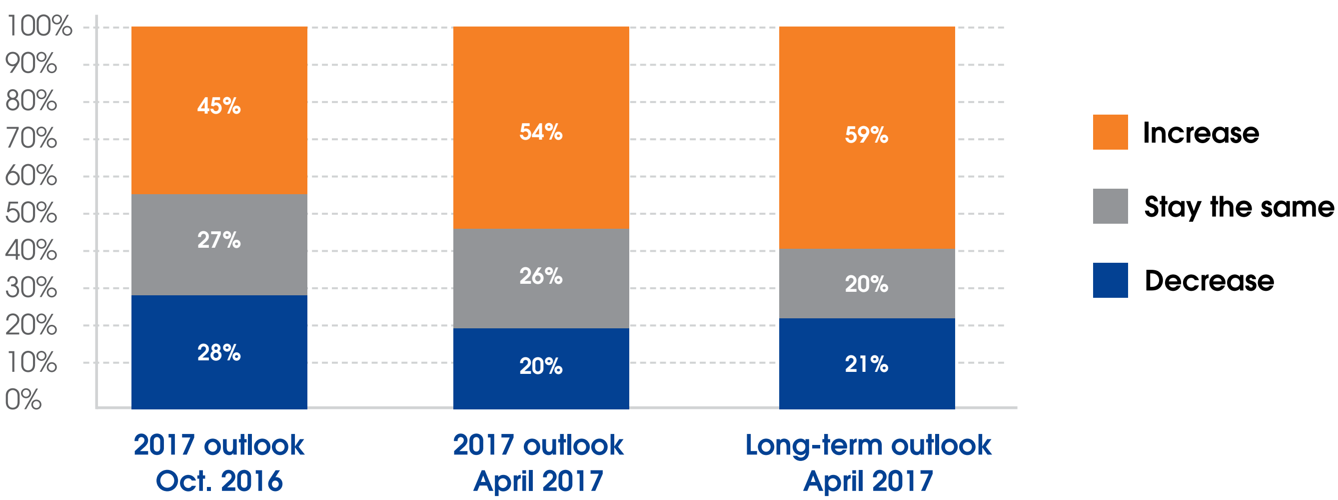
The Buyout Boom

This year's slumping deal volume is almost entirely attributable to less shopping by corporate shoppers. (Incidentally, that segment of buyers – including both C-level executives and corporate development officers – is the largest single group of respondents to our survey.) Further indicating the waning influence of corporate acquirers on the tech M&A market, survey respondents were slightly more likely to project that financial buyers – the rivals to tech vendors for many targets – would outpace overall market activity. That was true both for this year (with 54% forecasting an increase in private equity activity compared with 2016) and even more so when we extended the timeline out to 2020 (with 59% anticipating an increase in PE activity compared with 2016).

Private Equity Outlook

Forecast Change in PE Activity

Source: M&A Leaders Survey from 451 Research / Morrison & Foerster



The near-term outlook for PE, in the view of the survey participants suggests that financial acquirers will further narrow the gap with their corporate rivals. Already, the number of PE deals has increased for four consecutive years, hitting a record level of 659 transactions in 2016, according to the M&A KnowledgeBase. And the pace so far in 2017 has been running even higher.

PE Shops Mix it Up

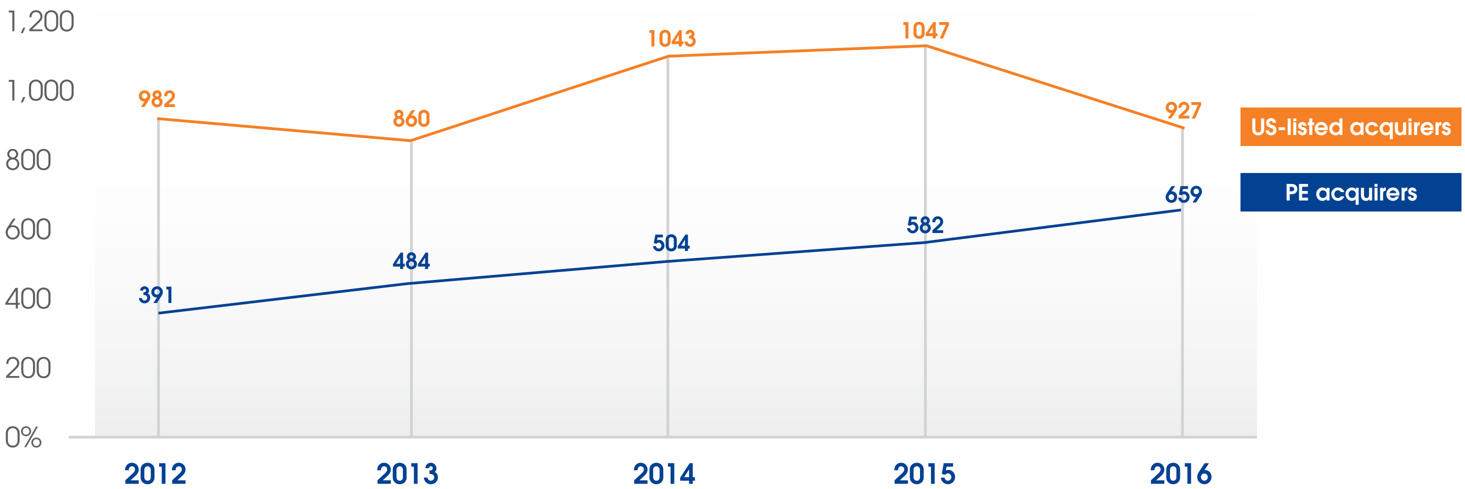
To continue their record-setting activity, PE firms are expected to focus on a mix of old and new M&A strategies, according to the survey. Respondents predicted that 'bolt-on acquisitions' would see the largest increase in activity from buyout shops through 2020. The selection of this tried-and-true strategy – one that involves, generally speaking, smaller and less-risky transactions – isn't all that surprising, given the number of platform companies that PE firms have already acquired and are looking to enhance. The pace varies, of course, but buyout shops typically acquire two or three times as many bolt-ons as platforms in any given year.

However, our survey respondents' second-ranked strategy of recapitalizing VC-backed startups comes as a relatively novel driver of PE activity. So far, we haven't seen many of those types of transactions, but as companies that are inside venture portfolios continue to age beyond the eight-to-ten year holding period for most VC firms, the startups may seek new backers. Certainly, the demographics of the startup ecosystem appear to support this trend. The remaining picks for the types of financial-sponsor transactions, in descending order, are: purchases from fellow PE firms; carve-outs; take-privates; and acquisitions of non-controlling stakes of companies.

Tech M&A Activity

PE vs. U.S.-listed Strategic Acquirers*, Deal Volume

Source: M&A Leaders Survey from 451 Research / Morrison & Foerster



Note: PE includes deals done by portfolio companies; acquisitions by NYSE- and NASDQ-traded companies.

Looking a little more deeply at the relatively low ranking of carve-outs in the coming year, we would be more likely to attribute that to supply constraints rather than declining demand. In a separate-but-related question, fewer than half of survey respondents (46%) forecast that tech vendors would be doing more divestitures and spinoffs in 2017. That was down a full 10 percentage points from the level that said the same thing in the previous survey last October. Of course, 2016 featured a number of tech giants -- including Hewlett Packard Enterprise, Dell and Intel, among others – doing multibillion-dollar divestitures last year. In contrast, tech companies haven't sold off as many significant businesses so far in 2017.

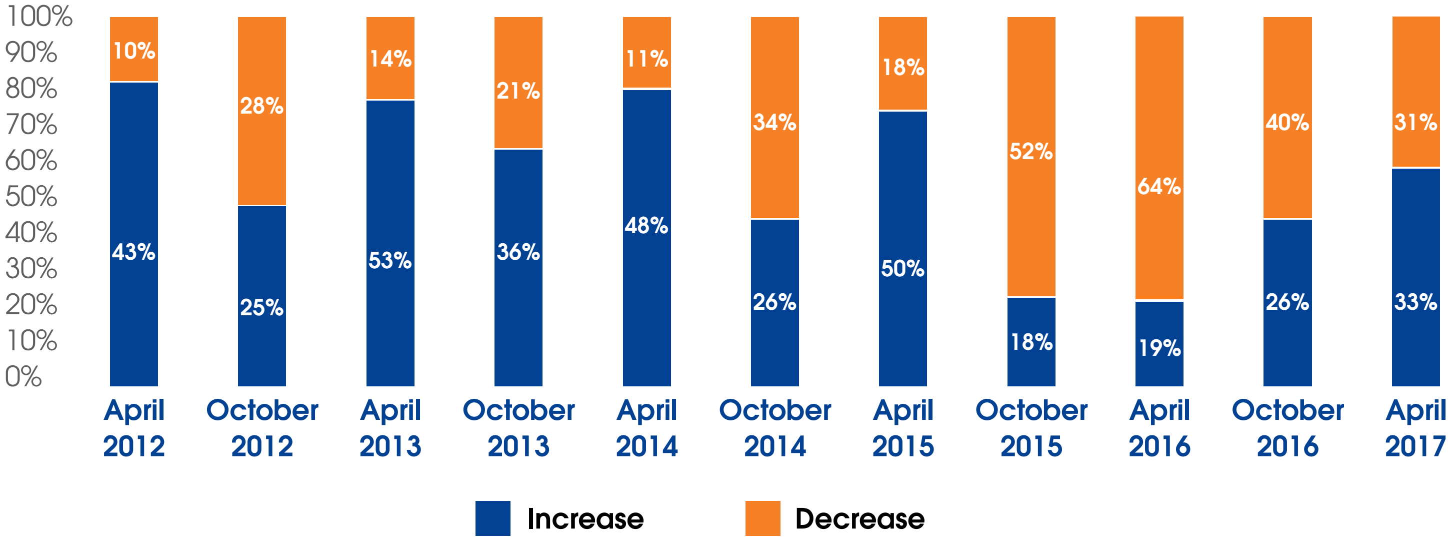
A Rare Bit of Balance

Shifting from M&A activity to valuations, respondents gave their most-balanced outlook for private companies pricing in the five-year history of the M&A Leaders' Survey from 451 Research and Morrison & Foerster. Specifically, 33% forecast increasing valuations for startups looking to sell this year, compared with last year; 36% predicted that the level would hold steady; and 31% projected that startups would be selling for lower valuations this year.

Tech M&A Valuation Outlook

Forecast Change in Private Company M&A Valuations

Source: M&A Leaders Survey from 451 Research / Morrison & Foerster



Typically, when it comes to valuation forecasts, one single view dominates, with the past three surveys heavily tilted toward a bearish outlook for startups. That sentiment reached its nadir in our survey last April, when tech vendors were still trying recover from the hammering their stocks took during the opening six weeks of 2016. In our survey last April, nearly two-thirds of respondents (64%) said startup M&A valuations would tick lower in the coming months. Fast-forward to this April, and just half as many respondents predicted declining valuations for startups.

About the survey: Now in its 11th edition, the M&A Leaders Survey from 451 Research and Morrison & Foerster drew 157 responses, primarily from corporate or M&A executives (44% of respondents) and investment bankers (42%), with the remaining responses coming from lawyers, VCs, PE professionals, and others in the M&A community. Roughly nine out of 10 responses came from dealmakers and advisers based in the United States; Silicon Valley represented the largest single location, accounting for some 40% of the total. This survey was conducted during the time period of March 29 through April 10, 2017.

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