

The Daily Dispatch

Weekly Special Feature

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M&A Is Expected to Pick Up in 2023 as Companies Adapt to Tougher Conditions

By: Kristin Broughton (Published on January 5, 2023 ET)



Grocery giant Kroger in October said it took out a 364-day bridge loan to fund its planned acquisition of rival Albertsons.

PHOTO: AUDE GUERRUCCI/REUTERS

Mergers and acquisitions slowed substantially in 2022 as companies faced a mix of financing challenges, including rising interest rates, a pullback in leveraged finance, bond market jitters and the possibility of a recession.

But many companies adapted, structuring deals to sidestep market volatility and minimize financing costs. In doing so, they provided a glimpse of what's likely ahead for deal making this year, bankers and advisers said.

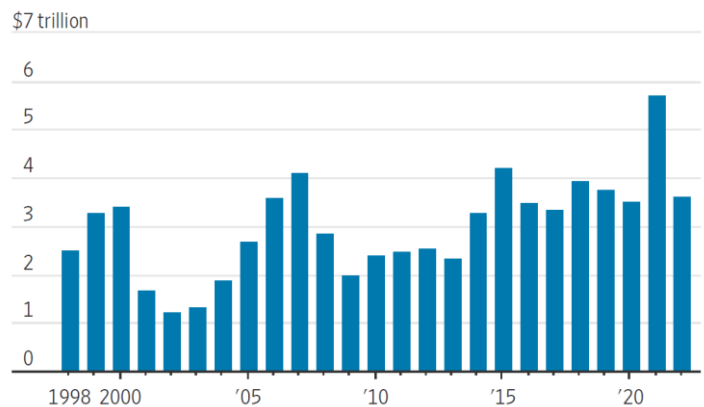
“The M&A market is not going to stop. It just doesn't work that way. What it does is it evolves,” said Christopher Auld, head of leveraged finance at investment firm Stifel Financial Corp.

The total value of deals announced globally fell 37% last year from 2021's record high, to \$3.61 trillion, according to financial data company Refinitiv. That is the biggest year-over-year percentage drop since 2001, a year when the U.S. economy slid into a recession and the value of global deal making plunged 50%, to \$1.68 trillion, according to

Deal Decline

The value of global deals announced in 2022 fell by the largest percentage since 2001.

Value of mergers and acquisitions globally



Note: Data for each year is through Dec. 28.

Source: Refinitiv

Refinitiv. Still, last year's results were roughly in line with prepandemic levels.

Deal advisers expect M&A to pick up in 2023 following last year's slump, though when that will happen remains an open question. Buyers and sellers want more certainty about the pace of further rate increases from the Federal Reserve, as well as data showing inflation continues to abate after notching 40-year highs, advisers said.

“The most important ingredient, in a way...is confidence,” said William Regner, partner in the mergers-and-acquisitions group at the law firm Debevoise & Plimpton LLP, discussing factors that sapped M&A momentum in 2022.

Multiples on strategic deals—a metric that compares a target's enterprise value to its earnings before interest, taxes, depreciation and amortization—fell to a 10-year low of 11.6 times at the median last year through Nov. 30, compared

The Daily Dispatch

with 15.4 times a year earlier, according to advisory firm Bain & Co. Lower share prices across industries, driven by a selloff in stock markets throughout 2022, made it harder for acquirers to pay up for acquisitions, according to Bain.

“As interest rates go up, valuations are coming down,” particularly for certain fast-growing companies that aren’t generating free cash flow, said Suzanne Kumar, a vice president in Bain’s M&A practice. That is especially true in the technology and healthcare sectors, where deals for high-growth companies are most common, she said.

In addition to macroeconomic pressures, companies faced a tougher regulatory environment in 2022, with antitrust enforcers globally applying greater scrutiny to large transactions.

Last year’s biggest deals included Microsoft Corp.’s \$75 billion, all-cash deal announced in January to acquire videogame maker Activision Blizzard Inc., as well as chip maker Broadcom Inc.’s planned \$61 billion takeover of enterprise software company VMware Inc., announced in May.

The companies are responding to inquiries from regulators globally. Microsoft said Wednesday it is working toward a resolution with the U.S. Federal Trade Commission, which sued the company in December to block the Activision purchase. The FTC said it is always open to considering proposed settlements.

Volatility in the bond markets, meanwhile, kept potential acquirers on the sidelines, advisers said. U.S. investment-grade bond issuance declined 20% last year compared with 2021, to \$1.31 trillion, according to Dealogic, a financial data provider. High-yield issuance plunged 71% over the same period, to \$390.37 billion, Dealogic said.

Still, companies continued to move forward with major transactions, putting together financing structures to meet the moment.

A driving factor behind last year’s decline in M&A was a pullback by big investment banks from the leveraged-loan market, advisers said. Banks last year faced hundreds of millions of dollars in losses on loans they agreed to provide

for the acquisitions of companies including cloud-computing giant Citrix Systems Inc. and Twitter Inc., before demand from institutional investors collapsed. Investment banks as a result lost their appetite for this type of financing, prompting acquirers to turn to alternative sources, including private lenders.

Blackstone Inc. relied on private lenders in a deal announced in October to buy a 55% stake in Emerson Electric Co.’s climate-technologies business, which makes compressors and other HVAC products. Under the transaction, which is valued at \$14 billion, Emerson agreed to retain a 45% stake in the business.

To fund the transaction, Blackstone raised \$5.5 billion of financing from direct lenders and a group of commercial banks with a smaller presence in the market. Typically, big investment banks would participate in this type of deal and sell the debt to a syndicate of investors.

Additionally, Emerson contributed \$2.25 billion in financing through what’s known as a seller’s note. The 10-year note carries a 5% interest rate that is capitalized twice a year, meaning it is added to the underlying principal. “We feel very confident that we’re going to get paid out on that on the accreted value at the appropriate time,” Emerson Chief Financial Officer Frank Dellaquila said during an Oct. 31 investor call. Emerson and Blackstone declined to comment further.

More acquirers also turned to short-term loans known as 364-day facilities to finance acquisitions, bankers said. Demand for such facilities in the U.S. jumped 17% in 2022 through Dec. 29 compared with the full-year 2021, to \$317.3 billion, according to Dealogic.

Finance chiefs are increasingly using 364-day loans because of conditions in the leveraged-loan markets, bankers said. “You probably have a view that within the next year, you’re going to activate in the capital markets,” said Siamak Saidi, managing director in the commercial bank at Wells Fargo & Co., discussing the uptick in demand for 364-day loans. “And if not, you’re going to reassess what the options are at that point.”

Grocery giant Kroger Co. in October said it took out a

The Daily Dispatch

a \$17.4 billion, 364-day bridge loan from Citigroup Inc. and Wells Fargo to fund its planned acquisition of rival Albertsons Cos. Kroger plans to pay off the credit when the acquisition closes, which is expected in early 2024, using cash on hand and proceeds from a new debt financing.

One way acquirers are minimizing financing costs is by negotiating deals for minority stakes in companies—for instance, buying less than 50% of a company that is majority-owned by another private-equity firm. Companies in 2022 struck \$240.4 billion of such deals, down from \$385.5 billion a year earlier, but up 4% compared with 2020, according to Dealogic.

Such deals can avoid a legal change in control, which typically requires a company to refinance its debt, bankers and advisers said. Doing so today would require the company to pay higher interest rates than before the Fed began to aggressively raise rates last year to fight inflation.

Think of the financial benefit of this type of transaction as purchasing a new house but keeping the seller's existing, low-rate mortgage in place, said Ken Wallach, co-head of the global capital markets practice at the law firm Simpson Thacher & Bartlett LLP.

“It’s all about trying to figure out how to move into that house, but keep the existing debt,” Mr. Wallach said, noting that it is a playbook more companies will likely turn to in 2023.

Source: Kristin Broughton (2023). M&A Is Expected to Pick Up in 2023 as Companies Adapt to Tougher Conditions. *The Wall Street Journal*. Available at: <https://www-wsj-com.cdn.ampproject.org/c/s/www.wsj.com/amp/articles/m-a-is-expected-to-pick-up-in-2023-as-companies-adapt-to-tougher-conditions-11672874676>

The Daily Dispatch

January 27, 2023
TODAY'S TOP NEWS

Monde Nissin acquiring 15% of Figaro Group

Monde Nissin Corp. said Thursday it is acquiring a 15-percent interest in restaurant chain operator Figaro Coffee Group Inc. for P820.3 million, a move that will enable it to expand its presence in the food sector. The price represents a 12.35-percent premium to FCG's closing of P0.89 on Wednesday.

ADB lending \$500m to aid pandemic impact in PH

The Asian Development Bank said Thursday it approved a \$500-million (about P27 billion) policy-based loan to help the Philippine government address the impact of the COVID-19 pandemic on jobs, livelihoods and the labor market.

German company expanding Batangas facility

ZAMA Precision Industry Manufacturing Philippines Inc., a unit of Germany's ZAMA Group, is expanding its production capabilities in the Philippines by adding a 11,000-meter-square facility in Sto. Tomas, Batangas.

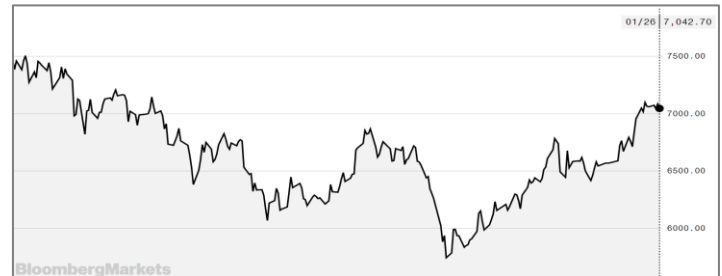
Vivant unit, JDC tie up for solar project

JEG Development Corp. (JDC) and Vivant COREnergy Inc. (COREnergy) announced their partnership for a solar power project. The firms launched the 37kWp (kilowatt peak) rooftop solar installation that powers the daytime energy demand of 22-storey JEG Tower, One Acasia, the first commercial high-rise building in Cebu.

Megawide bags 3 contracts

Listed Megawide Construction Corp. has secured three new supply-and-build contracts from affordable residential developer Phirst Park Homes Inc., a unit of Century Properties Group Inc.

Philippine Stock Market Update



Previous Close:

7,042.70

Open:

7,062.63

52-Week Range:

5,699.30 - 7,552.20

1 Yr Return:

-0.88%

YTD Return:

7.60%

Source:

Bloomberg

Foreign Exchange

As of January 26, 2023

US Dollar	Philippine Peso
1	54.48

BVAL Reference Rates

As of January 26, 2023

Tenor	Rate
1Y	5.391
3Y	5.550
5Y	5.784
7Y	5.901
10Y	6.022
20Y	6.359

Daily Quote

“There’s no way around hard work. Embrace it.”
– Roger Federer

The Daily Dispatch

MORE LOCAL NEWS

Meralco to start sourcing 670 MW from spot market

ABOITIZ Power Corp. (AboitizPower) will no longer supply power to electricity distributor Manila Electric Co. (Meralco) as their emergency power supply agreement (EPSA) ended on Wednesday. "We confirm the end of our 30-day emergency power supply agreement with Meralco which takes effect today, Jan. 25," AboitizPower said.

RLC Residences launches 50-floor upscale condo

THE residential division of Robinsons Land Corp. (RLC) has launched the first tower of Le Pont Residences located in a 31-hectare master-planned estate in Pasig City. The 50-storey tower, which is set to rise in Bridgetowne estate, will house 431 condominium units with varying sizes.

Cebu Pacific expects return to profitability in Q1

BUDGET carrier Cebu Pacific (CEB) said it is aiming to turn profitable in Q1 of this year as it is set to restore pre-pandemic network and capacity levels by March. "By the first quarter, we aim and we hope to be profitable. It really depends [as] fuel prices started coming up again," CEB President and CEO Alexander G. Lao said.

ACEN starts building solar project in Zambales

ACEN Corp. announced on Wednesday that it recently started the construction of its P16 billion 300-megawatt (MW) Palauig 2 solar farm in Zambales. In a regulatory filing, the Ayala-led listed energy company said the solar farm will be located within the proximity of ACEN's 63-MW Palauig 1 solar project.

Agricultural production dips in 2022

AGRICULTURAL production shrank by 0.1% in 2022, marking the 3rd straight year of contraction, as crops and fisheries output declined, the Philippine Statistics Authority (PSA) said. Data from the PSA showed the full-year value of production in agriculture and fisheries declined at a slower pace than the 1.7% contraction in 2021.

PH economy grows 7.6% in 2022, beats expectations

The Philippine economy ended 2022 on a high note amid roiling external headwinds that forced consumers to endure high inflation. In a briefing on Thursday, the Philippine Statistics Authority reported the country's gross domestic product expanded 7.6% year-on-year in 2022, exceeding the government's target of 5.8%.

SPNEC eyes more private placements I

SP New Energy Corp. (SPNEC) plans to undertake more private placements. "We are open to further broadening SPNEC's shareholder base, to build a more widely-held company and accelerate the development of solar in the Philippines," said Solar Philippines founder Leandro Leviste.

ACEN investing P2.8 billion for Pangasinan project

ACEN Corp. is set to start construction of its first development in Pangasinan, which will require an investment of P2.8 billion. ACEN said the 60-megawatt (MW) Pangasinan solar farm, which is expected to generate 94 gigawatt hours (GWh) of renewable energy per year, is targeted for completion by next year.

GCash partners w/ Grab: 'no transfer fee' payment

Globe-backed mobile wallet GCash has partnered with rides and delivery platform Grab to unburden their users with transfer fees. In a statement, GCash said that under the partnership, Grab users can soon choose GCash as a payment method for GrabCar, GrabFood, GrabMart, GrabExpress, and other Grab services transaction.

Higher credit card rate cap to aid PH bank profits

Global credit watcher Fitch Ratings said that the Bangko Sentral ng Pilipinas (BSP)'s decision to adjust the interest rate cap on credit card transactions will boost local banks' profits. Fitch said raising the interest rate ceiling on cardholders' unpaid balances to 3% from 2% per month "will buoy banks' net interest margins."

The Daily Dispatch

TODAY'S TOP ASIAN NEWS

FCT, Frasers Property to acquire 50% stake in Nex

The manager of Frasers Centrepont Trust (FCT) and sponsor Frasers Property Limited (FPL) announced on Thursday the joint acquisition of a 50% stake in suburban mall Nex for S\$652.5 million. The stake was bought from a subsidiary of NTUC unit Mercatus Co-operative, which had put it on the auction block back in June 2022.

Marina Bay Sands: record gaming, retail Q4 revenue

Amid robust tourism and travel spending recovery across all of Las Vegas Sands' (LVS) markets, its Singapore integrated resort Marina Bay Sands (MBS) reported a record performance in both mass gaming and retail revenue for the fourth quarter of last year. MBS' net revenue nearly doubled in Q4 2022 to US\$682 million.

Air India to seal half of jumbo plane order

Air India will on Friday seal half of an order worth billions of dollars for some 495 jets with Boeing and engine suppliers General Electric and CFM International, two industry sources said, as its new owner seeks to revive the airline and compete with much larger rivals.

Sea said to eye sale of Phoenix Labs to cut costs

Sea Ltd is considering the sale of Vancouver-based indie developer Phoenix Labs as the South-east Asian internet giant slashes costs and focuses on its core business, according to people familiar with the matter. The Singapore-based gaming and e-commerce company is working with an adviser on the potential divestment.

SoftBank deals hit record low in Q4

SoftBank Group's new start-up bets hit a record low last quarter as valuations continued to slide, chilling an already frosty start-up winter. The world's largest technology investor participated in just eight investment rounds totalling US\$2.1 billion in the three months ending in December, data compiled by Bloomberg showed.

TODAY'S TOP GLOBAL NEWS

Bank of CA: 1st major central bank to signal pause

The Bank of Canada on Wednesday hiked its key interest rate to 4.5 per cent, the highest level in 15 years, and became the first major central bank fighting global inflation to say it would likely hold off on further increases for now. The 25-basis-point increase was in line with analysts' expectations.

AUS dollar jumps, inflation shoots to 8.4% in Dec.

The Australian dollar jumped on Wednesday after a surprisingly red-hot inflation report all but cemented the case for another interest rate hike from the Reserve Bank of Australia (RBA) in February. Going the other way, the kiwi sagged and swap rates tumbled.

Global phone shipments plunge by most ever in Q4

Global smartphone shipments have seen their worst quarterly drop on record in a clear sign of cooling consumer demand that signals more pain for manufacturing hubs such as South Korea and Vietnam. Shipments declined 18.3 per cent in the December quarter compared with a year earlier to a little more than 300 million units.

Intel gives dire forecast on PC demand, flags loss

Intel said on Thursday it expects to lose money in the current quarter, surprising investors with a bleaker-than-expected outlook for both the PC market and slowing growth in its key data centre division. The company's shares fell 9.5 per cent in trading after the bell.

Luxury group LVMH's sales defy downturn

Luxury goods group LVMH's sales rose 9 per cent in the fourth quarter as shoppers in Europe and the United States splurged over the crucial holiday season, helping partly to offset Covid-19 disruptions in China. Sales at the world's biggest luxury group reached 22.7 billion euros in the final three months of the year.