CREWE | Investment Banking

MERGERS & ACQUISITIONS MARKET UPDATE

Q1 2022

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Market Update
Q1 2022

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Market Overview

After a strong year of M&A activity in 2021, Q1 2022 was off to a slower start. The Russian invasion of Ukraine, higher levels of inflation, and rising interest rates all have contributed to market uncertainty. Market instability made a clear impact on the M&A market with total global M&A deal value down 25% in Q1 2022 compared to Q4 2022.

While M&A activity experienced a slower start in Q1 2022, momentum from 2021 is still expected to carry over. With large amounts of dry powder still needing to be invested, discounted valuations could make some acquisition targets more attractive, resulting in a boost in deal volume.

U.S. GDP decreased by 1.4% in Q1 2022, caused primarily by a swelling trade deficit. The decrease in GDP represented the worst quarter performance since Q2 2020, but economists expect a rebound with a projected 3.3% increase in U.S. GDP in Q2 2022.

Of the macroeconomic events affecting the broader market in Q1 2022, rising inflation has been the most prominent. The CPI rose 8.5%, which greatly reduced the purchase power of the U.S. dollar. This increase in inflation was largely due to severe supply chain constraints caused by the COVID-19 pandemic, excessive demands, and a relatively low cost of capital. To help combat inflation, the Federal Reserve approved a 0.25% hike in the federal funds rate, the rate at which banks and credit unions lend to each other, during its March meeting. The Federal Reserve is expected to increase the rate at each of its six remaining meetings this year, pointing to an anticipated federal funds rate in the range of 3.25% to 3.5% by the end of 2022.

The Russian invasion of Ukraine has had a sizeable impact on the global economy. Due to sanctions imposed by the U.S. and other governments, many business operations and supply chains have been disrupted. This disruption has contributed to the rise in prices of oil, metals, and grain. Oil prices increased 31% in Q1 2022, resulting in all-time high spot gas prices in Europe and Asia. Grain, the primary export of Ukraine, also reached all-time highs in Q1 2022.

U.S. IPO activity, both traditional IPOs and SPACs, have cooled since reaching record highs in 2021. IPO activity is expected to slow to more normalized levels as market volatility persists.

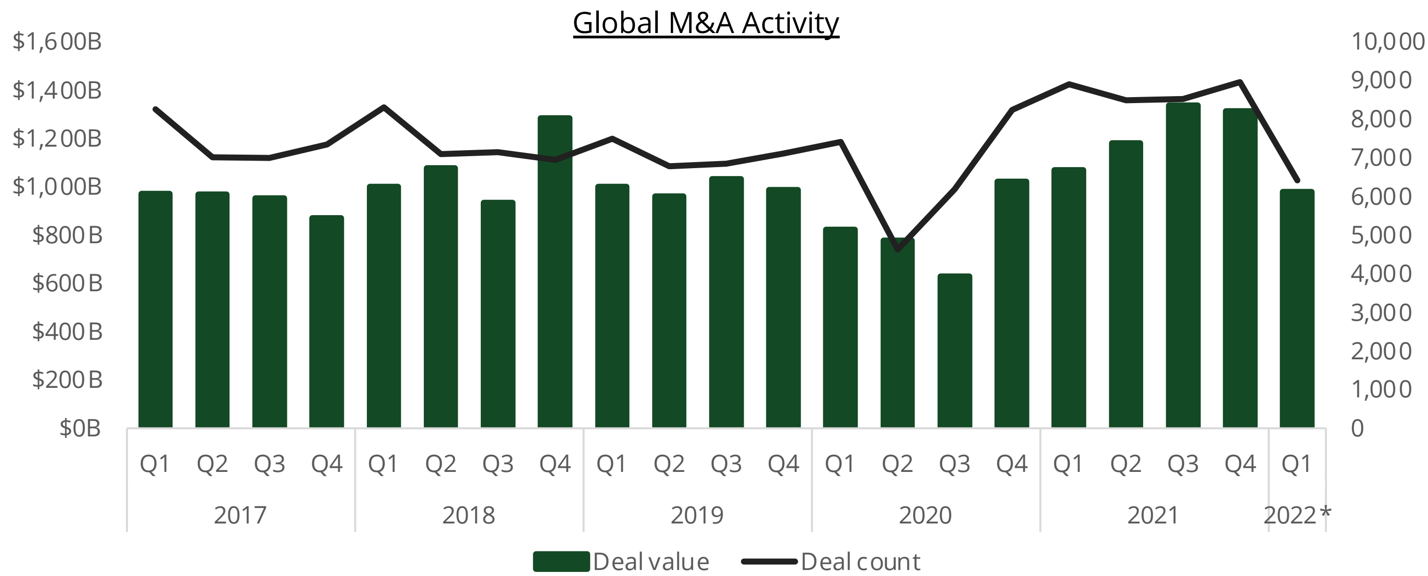
Venture capital fundraising continued to grow in Q1 2022, which is likely the result of committed capital from the bull market of 2021. Middle market private equity fundraising has decreased slightly due to record levels of dry powder and ongoing market uncertainty.

Ultimately, we expect M&A activity to stabilize throughout 2022. Although industry challenges exist, we anticipate lower valuations will provide buying opportunities for those able to navigate current market uncertainty.

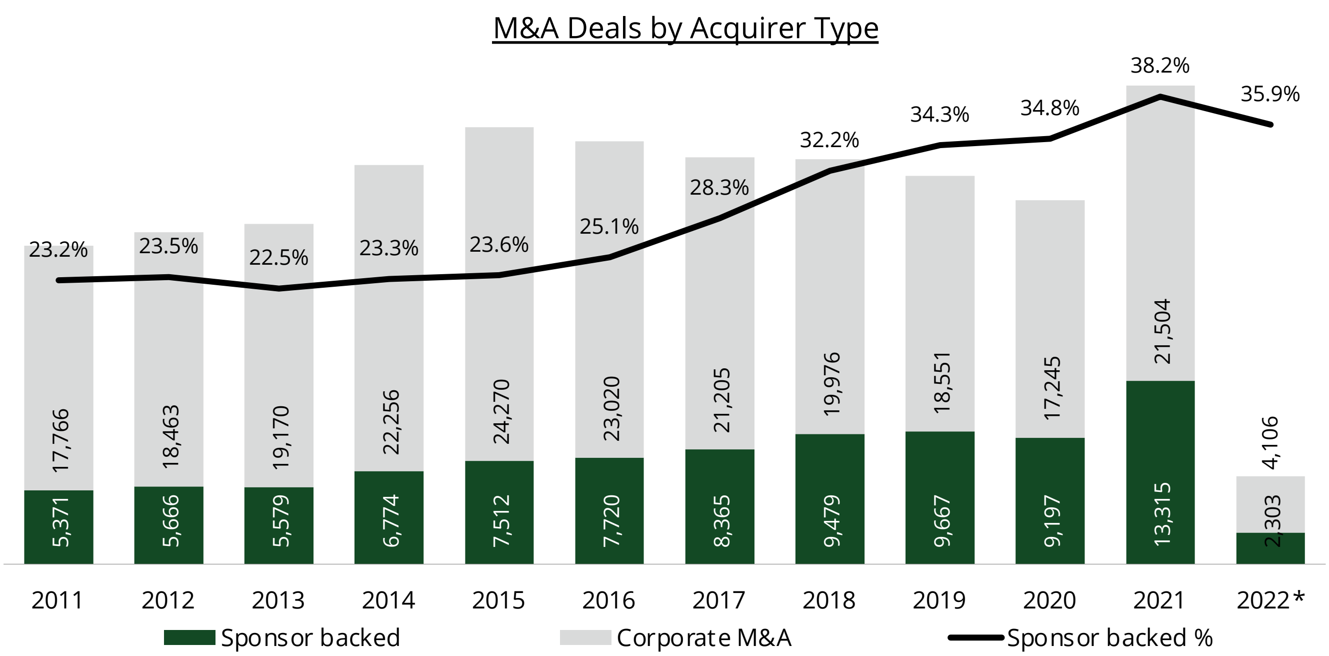
Sources: PitchBook, PwC, EY, Capital IQ, Statista, Mondrian, Bureau of Economic Analysis, USDA

M&A Activity

Q1 2022 M&A activity fell slightly from the record year of 2021, but overall activity is still strong when compared to the previous four years. Many deals that began negotiations in 2021 closed on time in Q1 2022, while others stalled, ultimately resulting in cancelled transactions due to bearish market sentiment. Globally, 6,409 M&A deals closed in Q1 2022 with deal value totaling $977.6B. The average deal size in Q1 of $153M pushed up the 5-year mean deal size to $138M.



While deal volume decreased, private equity firms continued to make up a relatively higher percentage of total deals. In Q1 2022, financial sponsors completed 2,303 deals that accounted for 36% of all M&A transactions, illustrating the high-level activity and interest that private equity continues to have in the market. The high percentage in financial sponsor deal activity is likely a combination of record levels of dry powder and the revenue contraction of strategic investors, resulting in less corporate M&A activity.



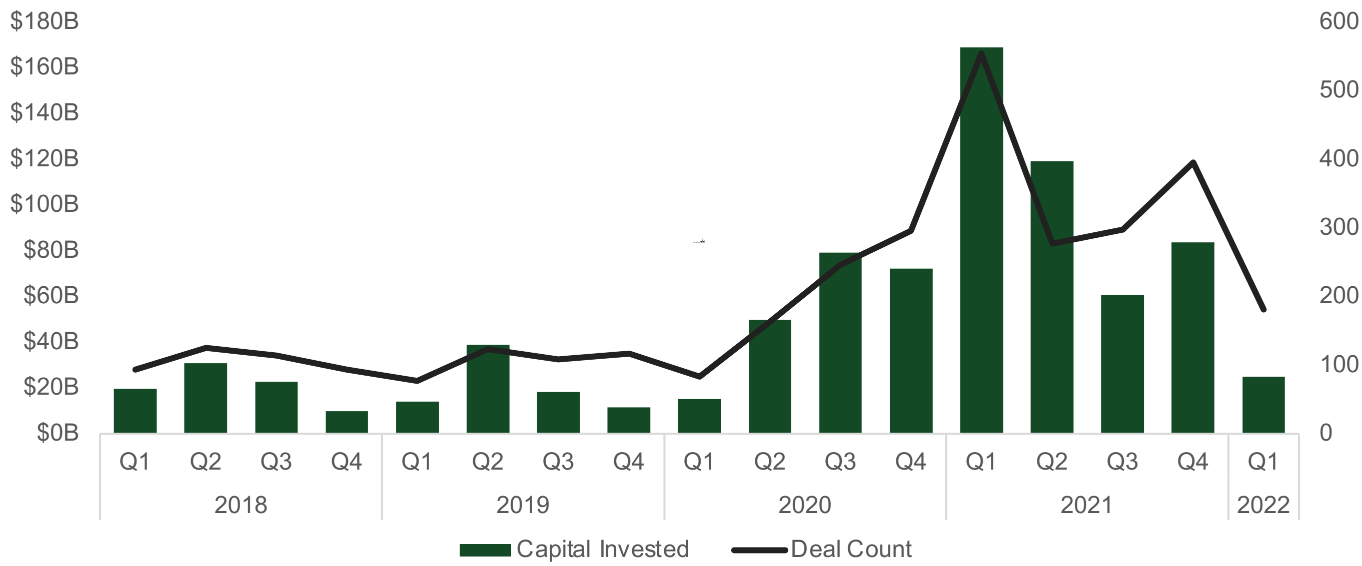
*Values through 3/31/2022

Sources: PitchBook, PwC, J.P. Morgan

IPO Activity

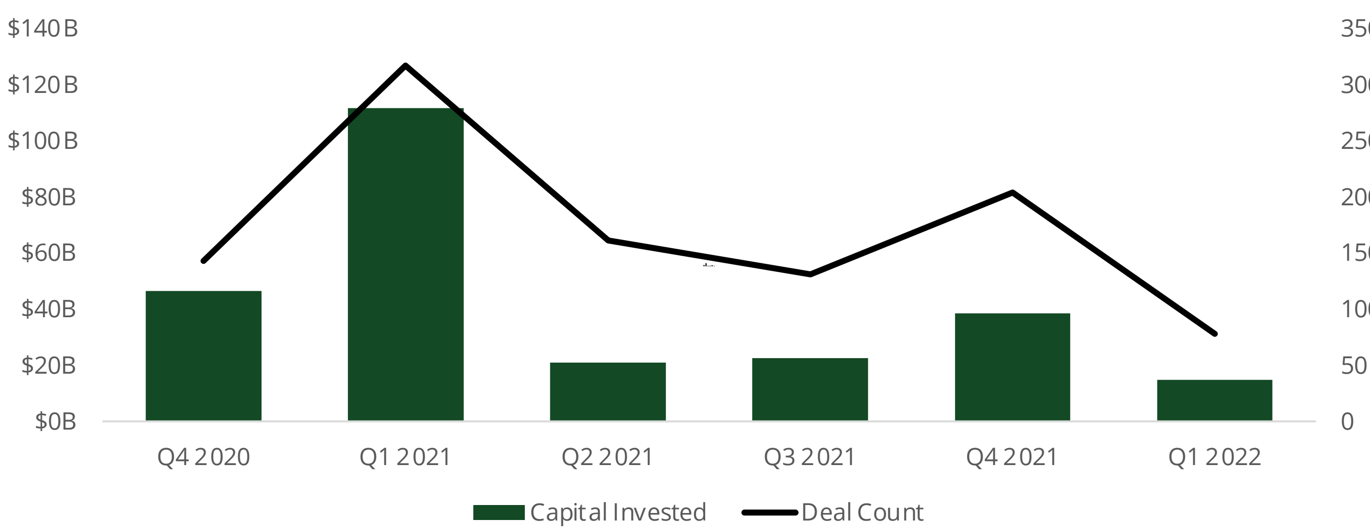
After a record year of IPO activity in 2021, market uncertainty caused a significant slowdown through Q1 2022. This retraction came even after the momentum in 2021 carried over into the first few weeks of 2022. Globally, the technologies and materials sectors led the way for total number of IPOs in Q1 2022 with 58 each, while the energy sector led in total proceeds with $12.2B. In the U.S. IPO markets, 181 listings raised $25.0B in proceeds in Q1 2022. Total listings were down 54% from Q4 2021 and 67% from Q1 2021.

Recent IPO Activity: U.S. Markets



U.S. SPAC IPOs raised $14.7B through 78 listings in Q1 2022. After an 87% decrease in deal value from Q1 2021, both SPAC IPO volume and capital invested are officially at their lowest points since Q2 2020. With 609 public SPACs still searching for an acquisition, the market appears to be oversaturated and the number of new SPAC listings should remain low.

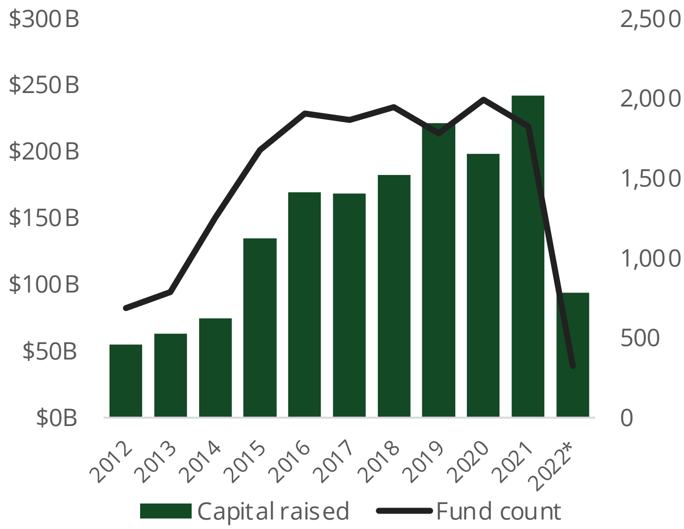
U.S. SPAC IPO Volume



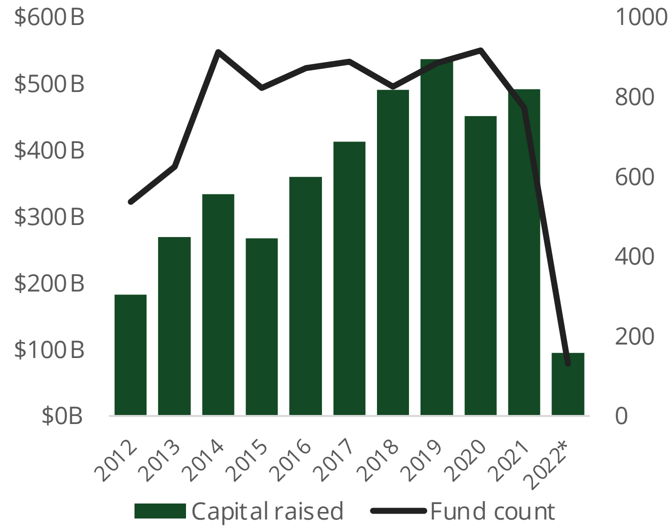
Fundraising

Global venture capital fundraising was strong in Q1 2022. Over $94B of capital was raised in Q1 2022, equating to almost 40% of the total capital raised in 2021. It is likely that a significant portion of this capital was committed in 2021 but wasn't called until 2022. While fundraising in Q1 2022 decreased 12% from Q4 2021, it was still more than double the $41.7B raised in Q1 2021. VC fundraising is expected to normalize in Q2 2022 as funds become more risk averse navigating market uncertainty.

Venture Capital Fundraising



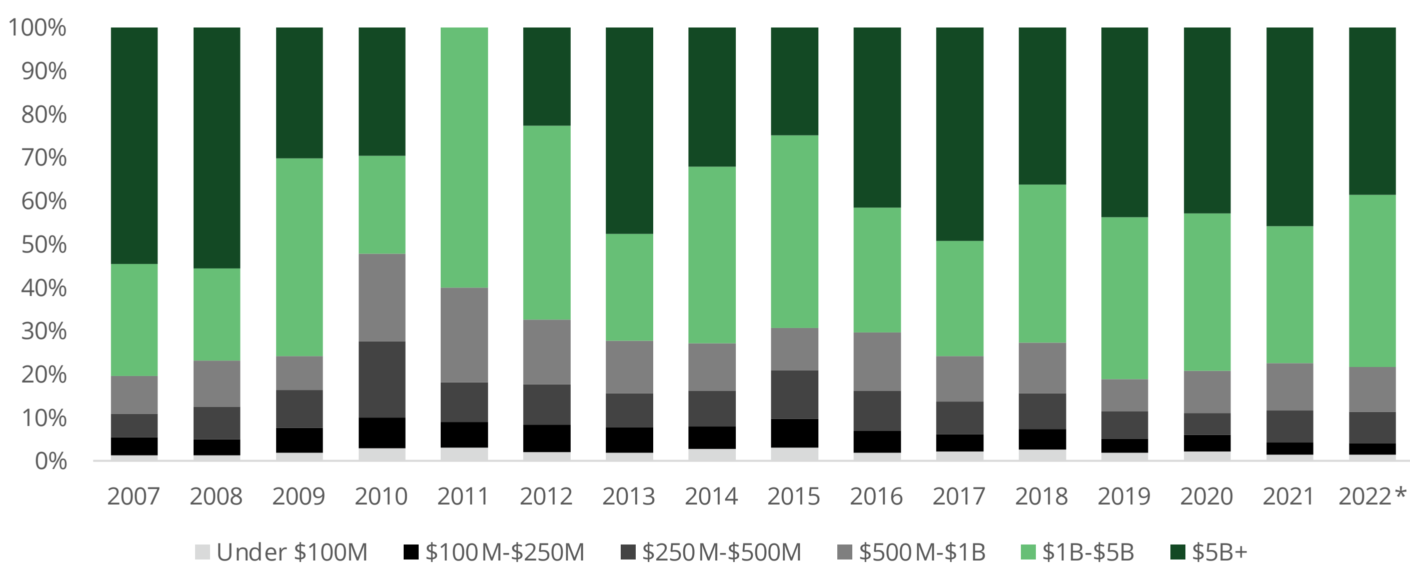
Private Equity Fundraising



Private equity fundraising has experienced a slower start in Q1 2022 and is expected to be slower than 2021. Investors have begun to hold assets due to poor market conditions. Much of the capital raised has been directly invested in healthcare or technology businesses.

Although average private equity fund size has decreased since 2021, middle market private equity firms are staying afloat and many newcomers are finding traction. Private equity funds will continue to look for ways to deploy capital as dry powder remains at all-time highs.

Private Equity Fundraising by Fund Size



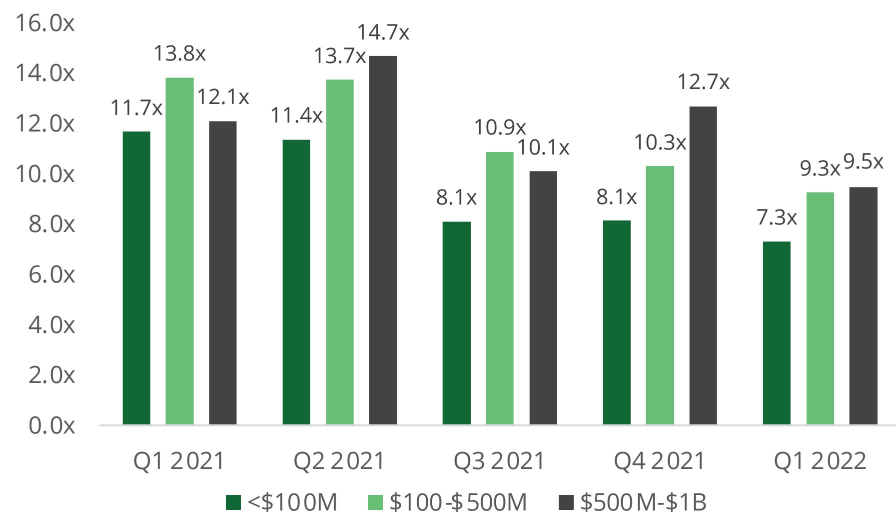
*Values through 3/31/2022

Sources: PitchBook, Capital IQ, EY, Stock Market MBA

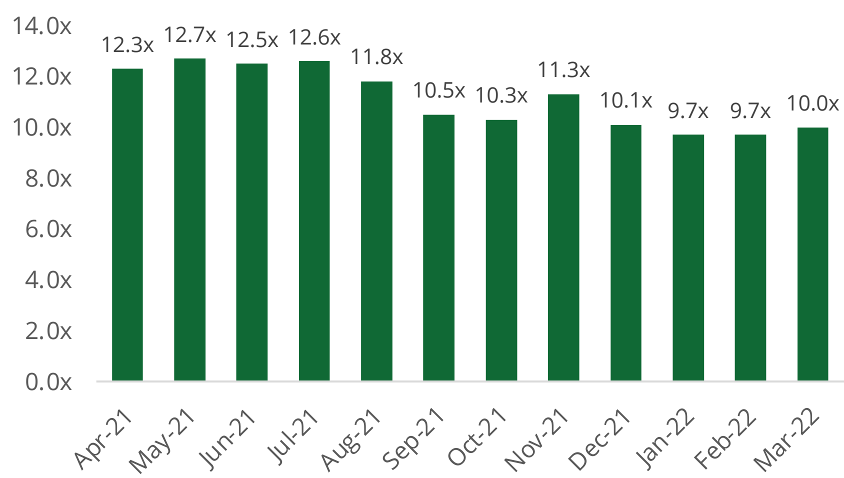
Multiples Overview

M&A transaction multiples fell in Q1 2022 as market uncertainty played a factor into what acquirers were willing to pay. While transactions for larger companies between $500M and $1B saw a 25% decrease in EV/EBITDA multiples from Q4 2021, transaction multiples for companies in the middle-market ($100M-$500M) and lower middle-market (less than $100M) experienced more moderate declines. The spread of multiples for the largest and smallest companies narrowed as less of a premium was assigned to more stable targets.

Implied EV/EBITDA Multiples



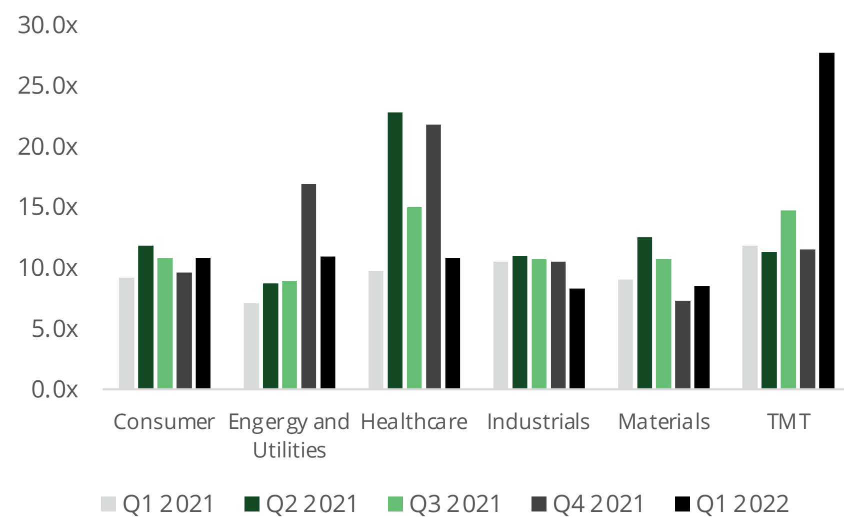
U.S. Middle-Market Trading EBITDA Multiples



Publicly traded middle-market companies saw EV/EBITDA multiples peak in March 2021, before falling 19% over the past 12 months. Since the end of 2021, multiples have leveled out as the economy has contracted. Multiples are expected to remain relatively stable moving forward.

For M&A transactions in the U.S. during Q1 2022, the energy/utilities and healthcare sectors saw a sharp decrease in EV/EBITDA transaction multiples from the high multiples of Q4 2021. In contrast, TMT valuations exploded from 11.5x in Q4 2021 to a staggering 27.7x in Q1 2022. Globally, every sector except consumer saw valuations fall. As the Federal Reserve raises interest rates to combat inflation, valuations across the market are expected to normalize.

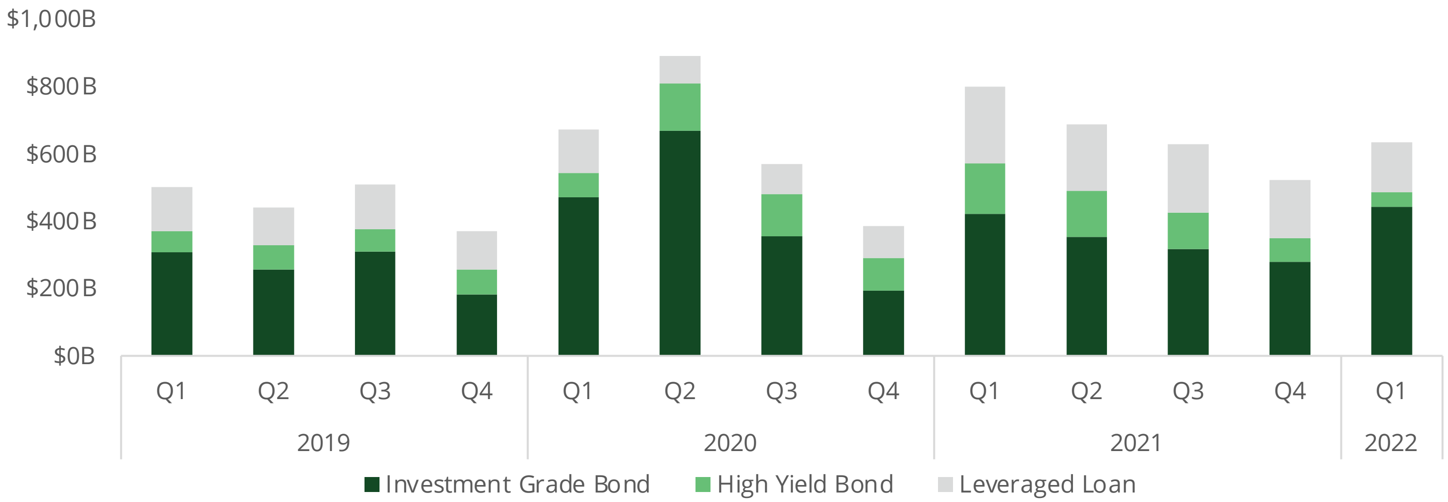
U.S. M&A EV/EBITDA Multiples by Industry



Debt Capital Markets Overview

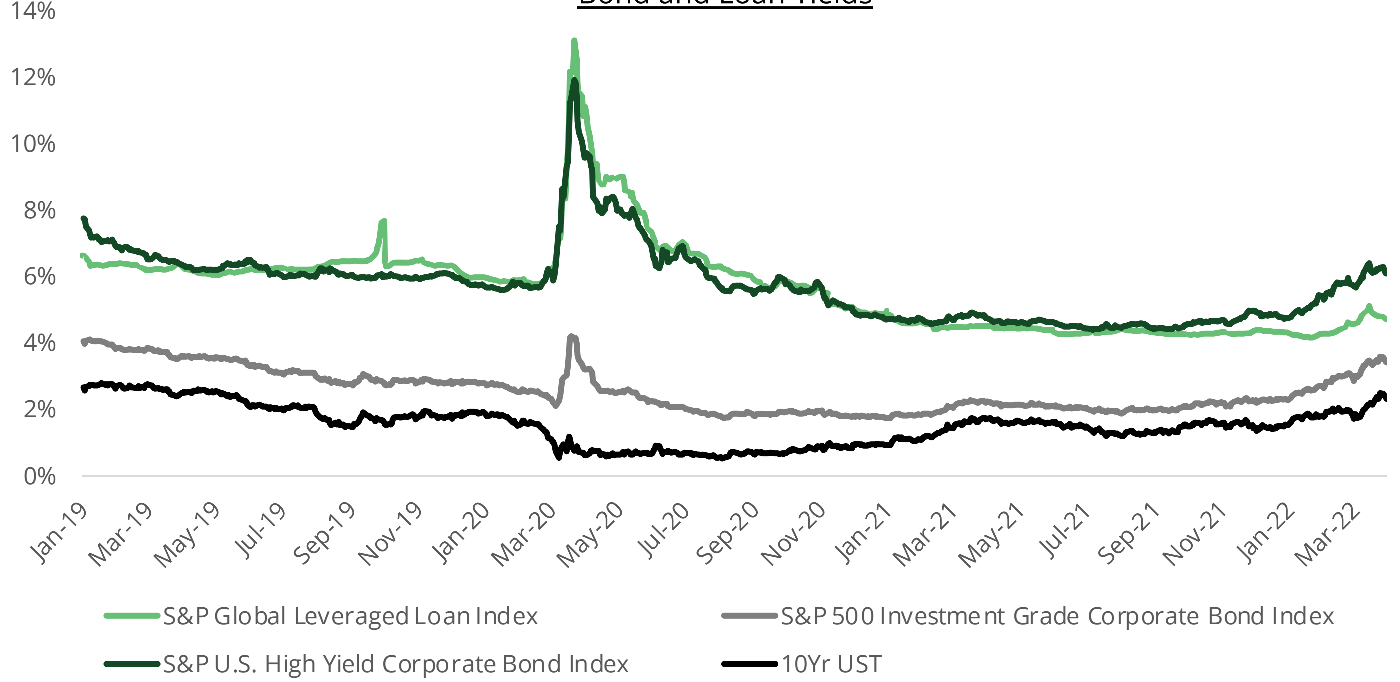
Debt markets in the U.S. started the year strong but saw a significant slowdown seven weeks in as the Federal Reserve began discussions of rate hikes. Even with a two-week shutdown, $634B was raised in the first quarter, a 22% increase over Q4 2021. Investment grade bond deals led the way with $442B in capital raised, the most since the peak in Q2 2020 caused by the onset of COVID-19. Issuers are wanting to lock in lower costs of bonds ahead of the anticipated rate hikes by the Federal Reserve.

U.S. Capital Market Issuance



Bond markets have priced in six more rate hikes in 2022, with an anticipated federal funds rate in the range of 3.25% to 3.5% by the end of 2022 and 3.5% to 3.75% by the end of 2023. Spreads in the S&P 500 Investment Grade Corporate Bond Index and S&P U.S. High Yield Corporate Bond Index widened by 33bps and 55bps through the first quarter of 2022, respectively. Spreads are expected to continue widening as higher rates and inflation persist. Higher cost of debt could make equity a more attractive option for capital raises.

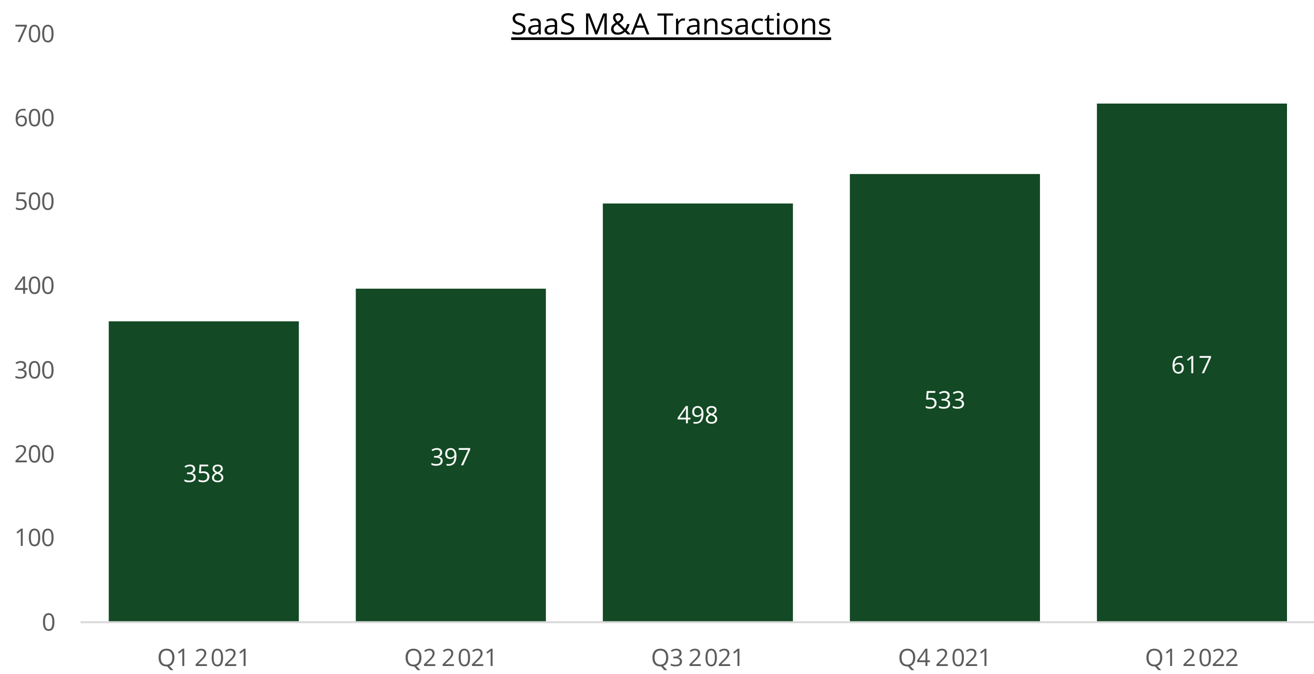
Bond and Loan Yields



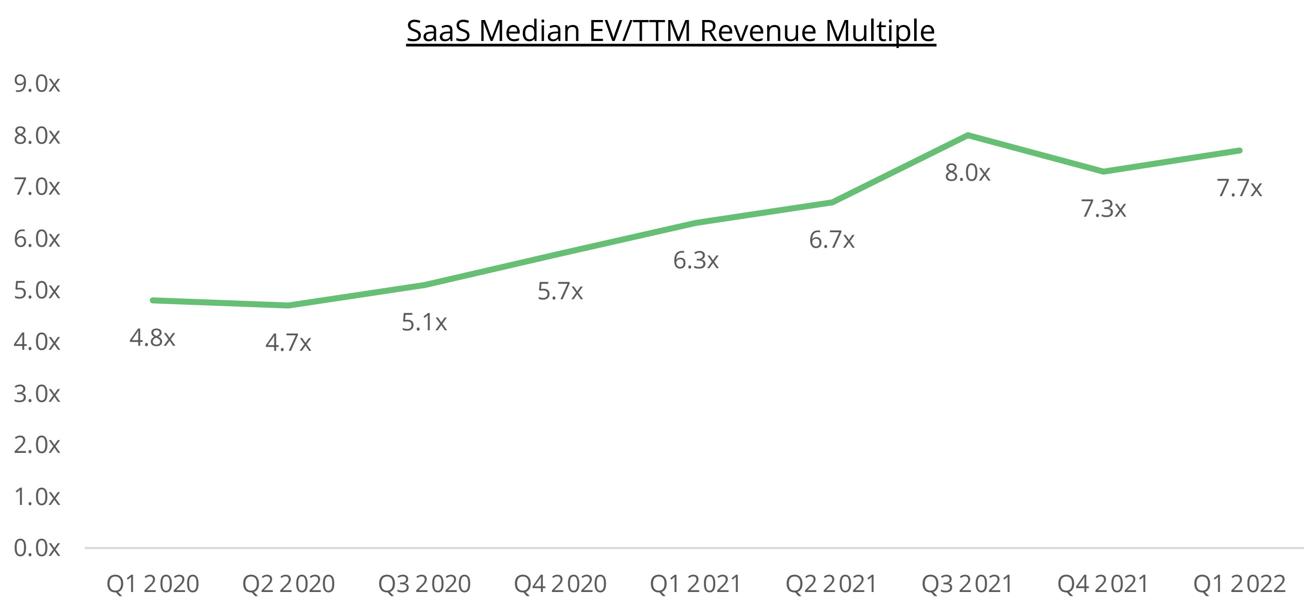
Sources: Refinitiv, PWC, S&P Global, FRED

SaaS Overview

Though overall M&A activity has slowed slightly, M&A activity in the SaaS vertical in Q1 2022 has seen continued momentum from 2021 with a record high 617 SaaS transactions, which represents a 72.3% increase over Q1 2021. A portion of these transactions, however, may have been a spillover from 2021 after concerns of capital gains tax diminished. Regardless, plenty of capital flowed into the sector as dealmakers continued to look for growth amid adjusting valuations.



With the significant tailwind of private equity dry powder and strong corporate balance sheets coming into 2022, SaaS multiples have remained strong. Although 2021 showed record high multiples, Q1 2022 is still strong with the median EV/TTM revenue multiple at 7.7x. Since this multiple is based on a trailing twelve months basis, the trends in 2021 have played a factor in the Q1 2022 multiple.



Sources: Software Equity Group, PitchBook

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