

Morgan Stanley



The European M&A Market in the Face of Geopolitical Turmoil

IBA European Corporate & Private M&A Conference

Paris, February 2023

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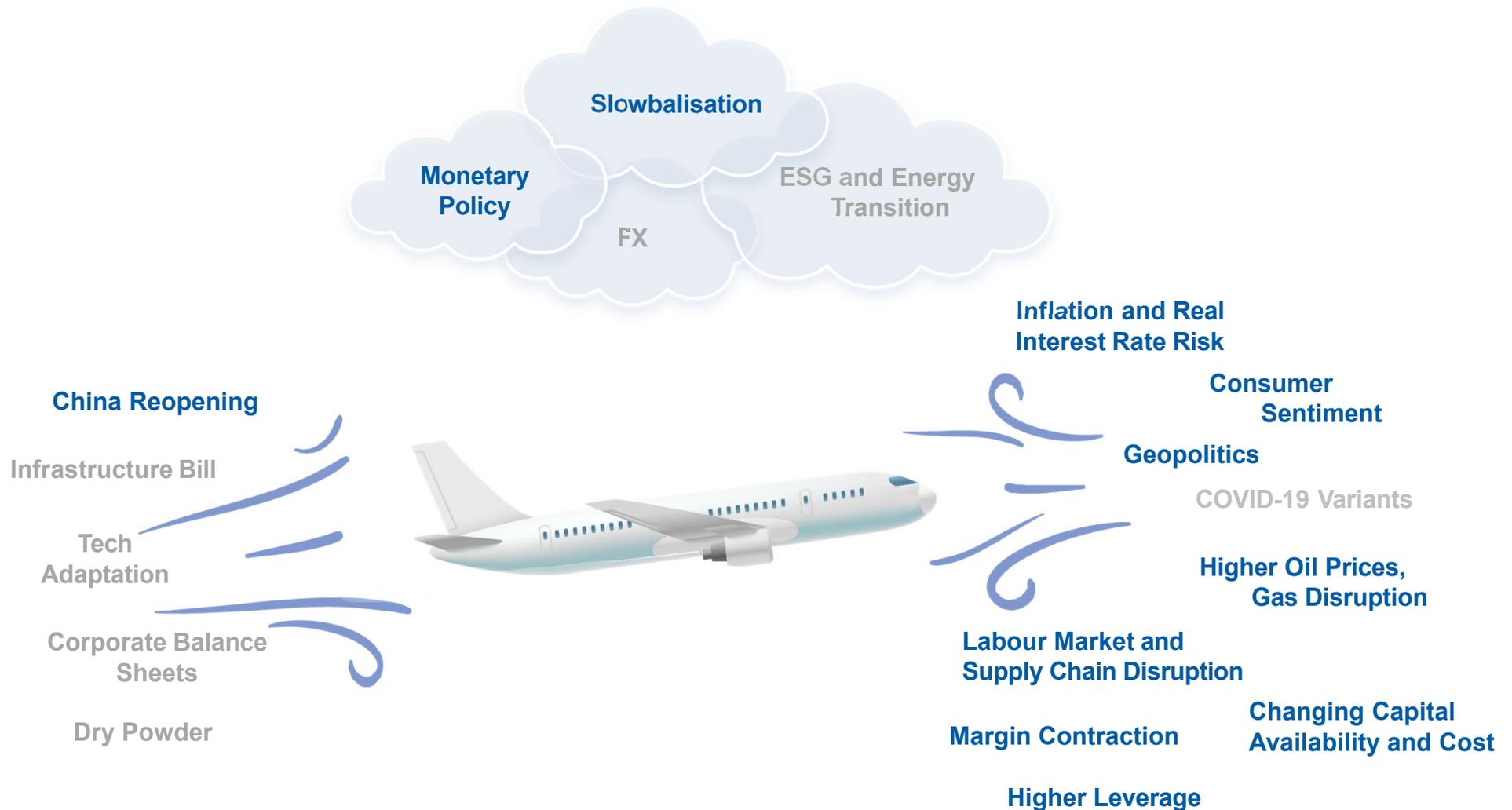
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“...today’s polycrisis has
sparked poly-innovation.”

FT FINANCIAL
TIMES

19th January 2023

Significant Turbulence to Navigate... ... But as Intricate and as Interesting a Market As We Have Seen



Agenda

1

2022: The Year In Review

2

Macro & Market Backdrop

3

2023: M&A Outlook

2022: Global M&A by Numbers

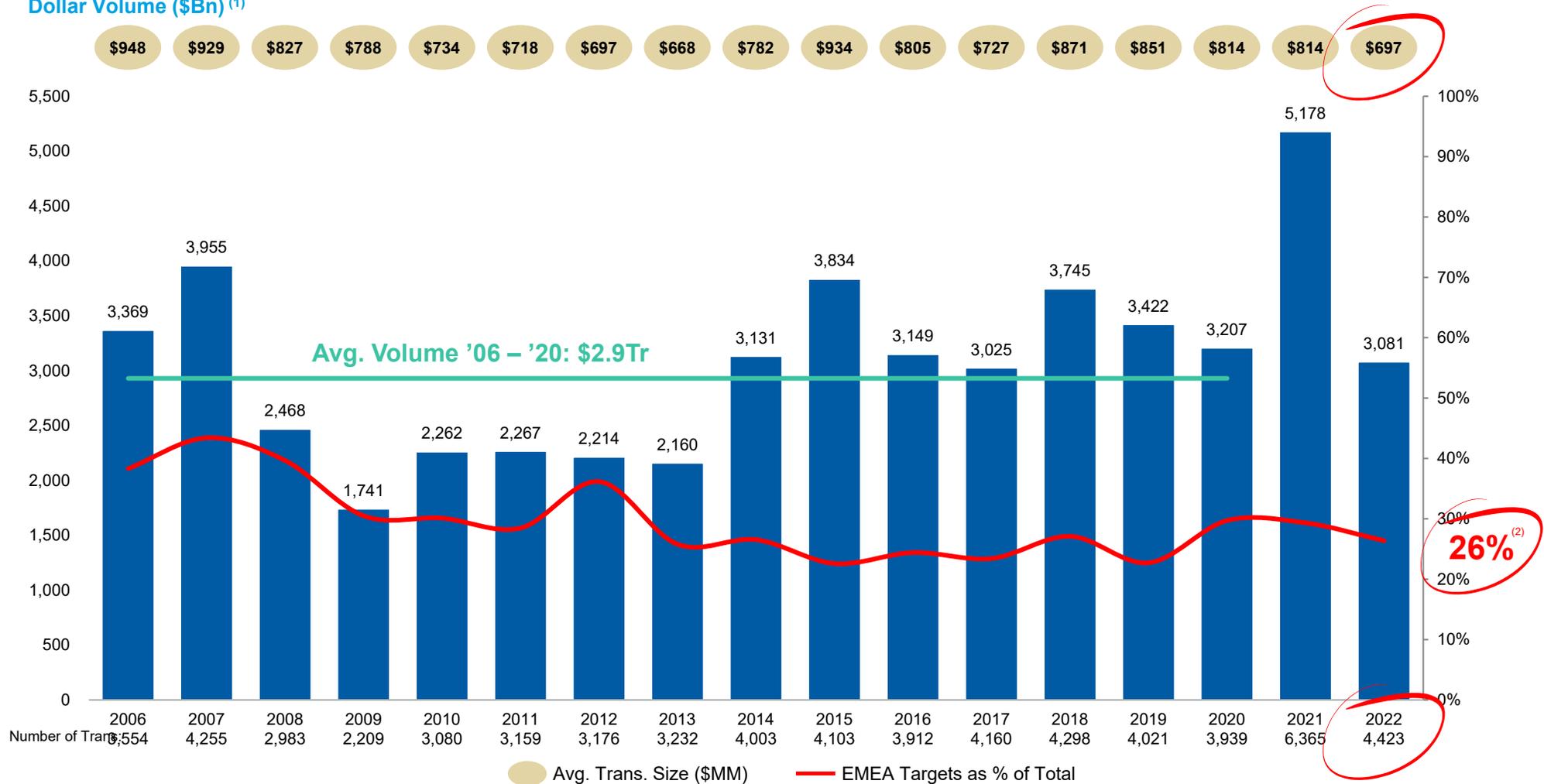
Global Volume	1H – \$1.9Tn 2H – \$1.2Tn	Down ~40%, but Ninth Year in a row > \$3 trillion
Number of Transactions	1H – 2,500 2H – 1,900	Consistent with L10Y average overall but 2H very slow
Acquiror Share Price Reaction	39% <i>positive share price reaction</i>	Lowest level in L5Y
Financial Sponsors Volume	~\$1.0Tn 33% <i>of global M&A volume</i>	Second highest annual volume in history, ~65% in 1H L5Y average of ~25%
De-SPAC Volume	\$117Bn	Down from \$536Bn in 2021
Cross Border	13% <i>of global M&A volume</i>	L10Y average of 18%
S&P 500	(20%)	Tech down ~ 34% , many companies trading down 50%+
CEO Confidence	67 → 32	Most negative since 2008; 2Q 2021 peak of 82

Source: CapitalIQ, Refinitiv as of December 31, 2022, The Conference Board

2022 Global M&A Volumes In Line With Pre-Covid Levels

Ninth Year in a Row Over \$3 Trillion

Dollar Volume (\$Bn) ⁽¹⁾

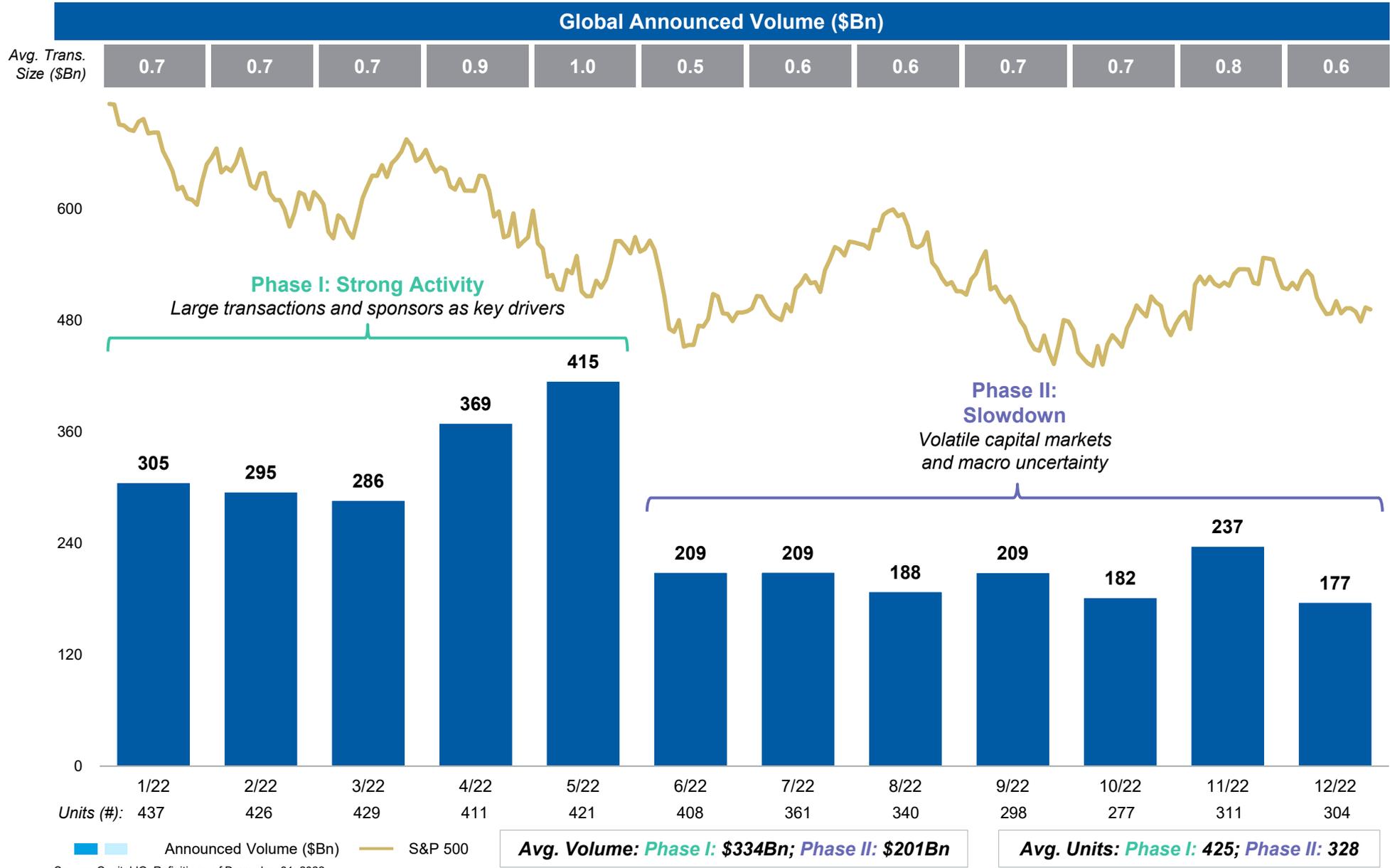


Source: Refinitiv as of December 31, 2022

Notes:

- 1. Includes global announced transactions, each with an aggregate value of \$100MM or more. Includes transactions with estimated values. Excludes terminated transactions. Future terminations of pending transactions will reduce totals shown
- 2. EMEA Targets as % of Total for 2022 largely in line with 5-year average of 27%

...But Very Much a Game of Two Halves



Source: Capital IQ, Refinitiv as of December 31, 2022

What Defined Phase I of the 2022 M&A Market?

January – May

Key Drivers

- **S&P 500** remained high – 4,530 on 3/31/2022
- **Inflation** and energy cost impacts of Ukraine not immediately felt
- **Rates** remained historically low with 10-year Treasuries at ~3% and 10-year BUND at ~1%
- **Leveraged finance markets** open for business
- **CEO Confidence** remained high
– 67 at YE 2021, 57 at Q1
- Few transactions challenged by FTC / DOJ / DG Comp

Select Transactions



The strong performance between January and May driven by two main factors – large corporate transactions and increased private equity activity



What Defined Phase II of the 2022 M&A Market?

June – December

Key Drivers

- **S&P 500** dropped ~20% from its peak
 - Nasdaq down ~34%; CAC/DAX down ~12%/~14%
- **Inflation** surged
 - Peaked at 9.1% in US and 10.6% in Euro Area
- **Rates** up sharply
 - Federal Funds Target Range went from **0.250% to 4.375%**
- **Leveraged finance market** mostly shut
 - \$75Bn+ in “hung” LBO’s
 - Direct lenders partially filled the gap
- **CEO Confidence** plummeted to 32 by the start of Q4
 - 98% of US CEOs predict a 2023 recession
- Investors reacted poorly to several large transactions
- FTC / DOJ more public / aggressive in challenging mergers

Select Transactions

Corporates Still Pursuing Transformational Deals

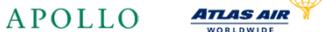


\$28Bn



\$19Bn

Financial Sponsors Finding Ways to Get Transactions Done



\$5Bn



\$12Bn

2021 IPOs As Targets



\$4Bn

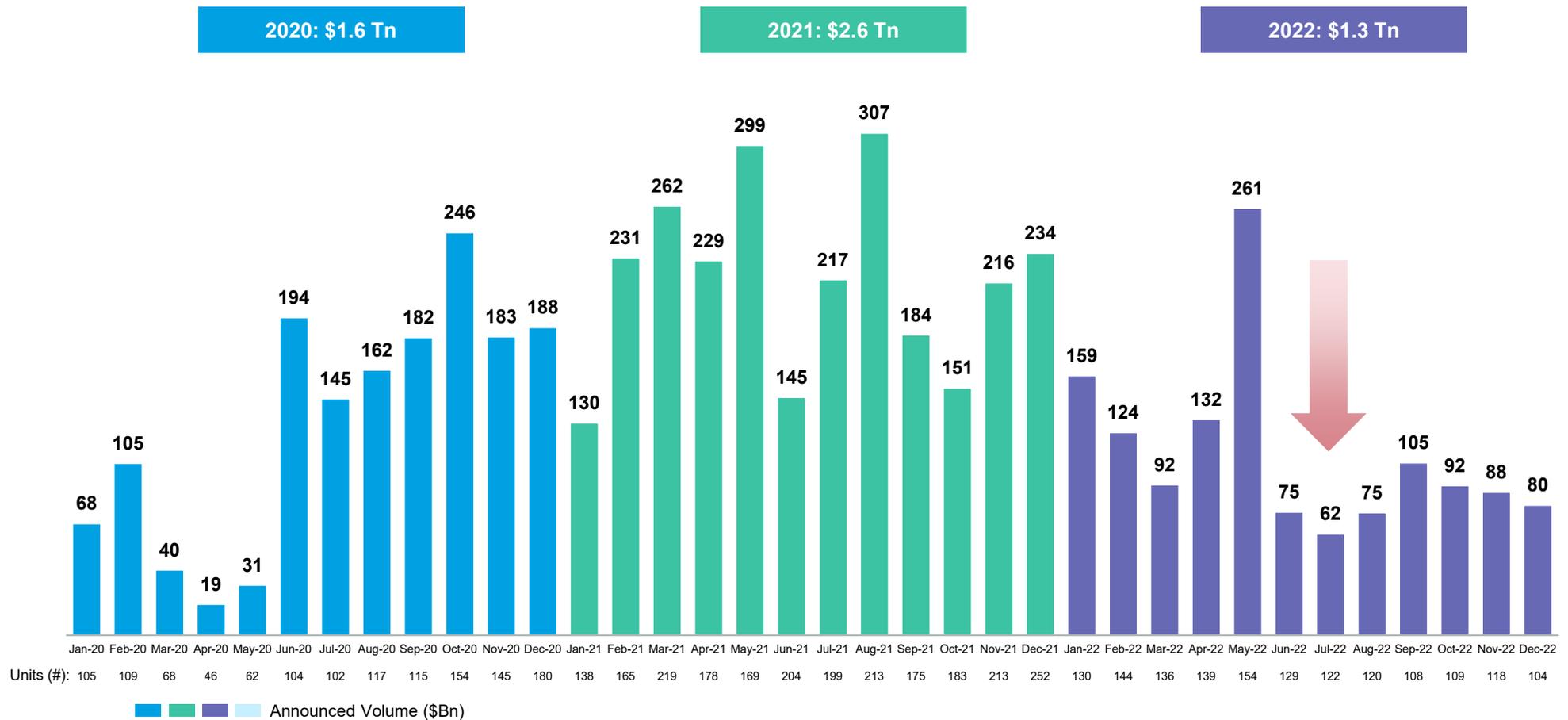


\$1Bn

Corporates Became Increasingly Selective on Strategic Deals...

H2 Corporate Activity Hit Lowest Level Since Start of COVID

Acquisitions by Publicly Listed Strategic Buyers – Global Announced Volume (\$Bn) ⁽¹⁾



Source: Refinitiv as of December 31, 2022

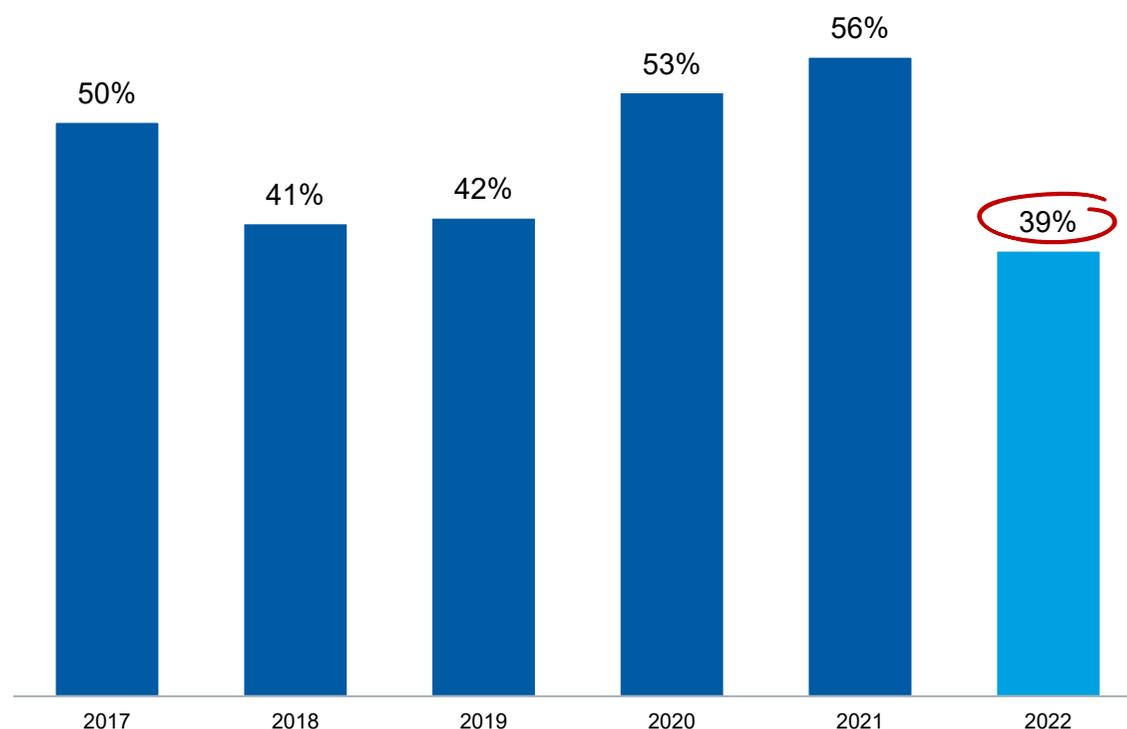
Note:

1. Includes global announced transactions by publicly listed non-sponsor acquirers, each with an aggregate value of \$100MM or more. Includes transactions with estimated values. Excludes terminated transactions. Future terminations of pending transactions will reduce totals shown

...Investors More Discerning on M&A...

Investor Communication Strategy Increasingly Critical

Percent of Announced Transactions with a Positive Buyer Share Price Reaction ⁽¹⁾



Investors Pushing Back On:

- Non-obvious investment theses
- High pro forma leverage
- Large transaction relative to buyer's market capitalization
- High multiple compared to buyer's multiple
- Timing – headed into a recession?
- Shouldn't buyers be able to acquire assets more cheaply?

Investors Still Supporting:

- Well telegraphed acquisitions (or divestitures), with clear synergies
- “Bolt-on” transactions in core business lines
- Lower risk business models / consistent cash flow generation

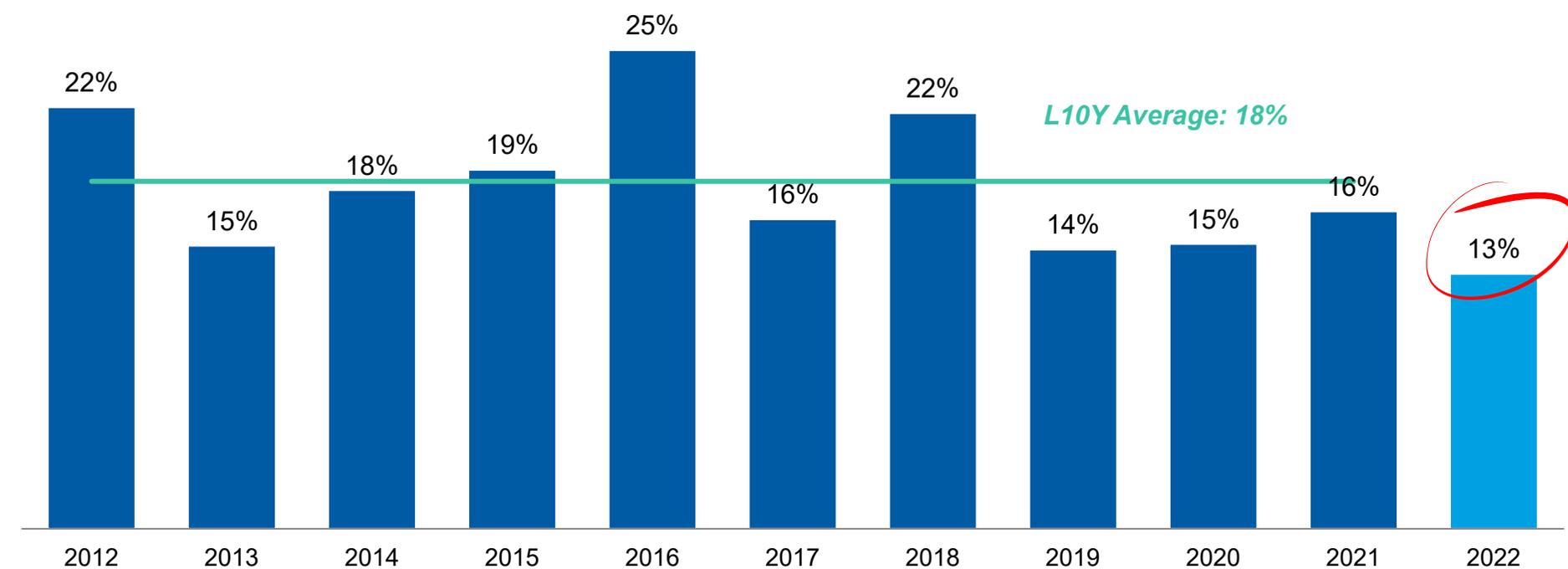
Source: Refinitiv, Capital IQ

Note:

1. Includes U.S. public acquirer announced transactions, each with an aggregate value of \$1Bn or more. Excludes, spins, restructurings, exchange offers.

...Resulting in Cross Border M&A at Lowest Level in Past Ten Years

Cross-Regional M&A by Corporates ⁽¹⁾⁽²⁾



■ % of Global M&A Dollar Volume

Source: Refinitiv as of December 31, 2021

Notes:

1. Includes announced transactions, each with an aggregate value of \$100MM or more. Includes transactions with estimated values. Excludes terminated transactions. Future terminations of pending transactions will reduce totals shown
2. "Cross-Regional" defined as transactions between acquirers and targets in Americas, Europe, Middle East/Africa, Japan and Asia Pacific. Excludes financial sponsor and SPAC acquirers

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3 2023: M&A Outlook

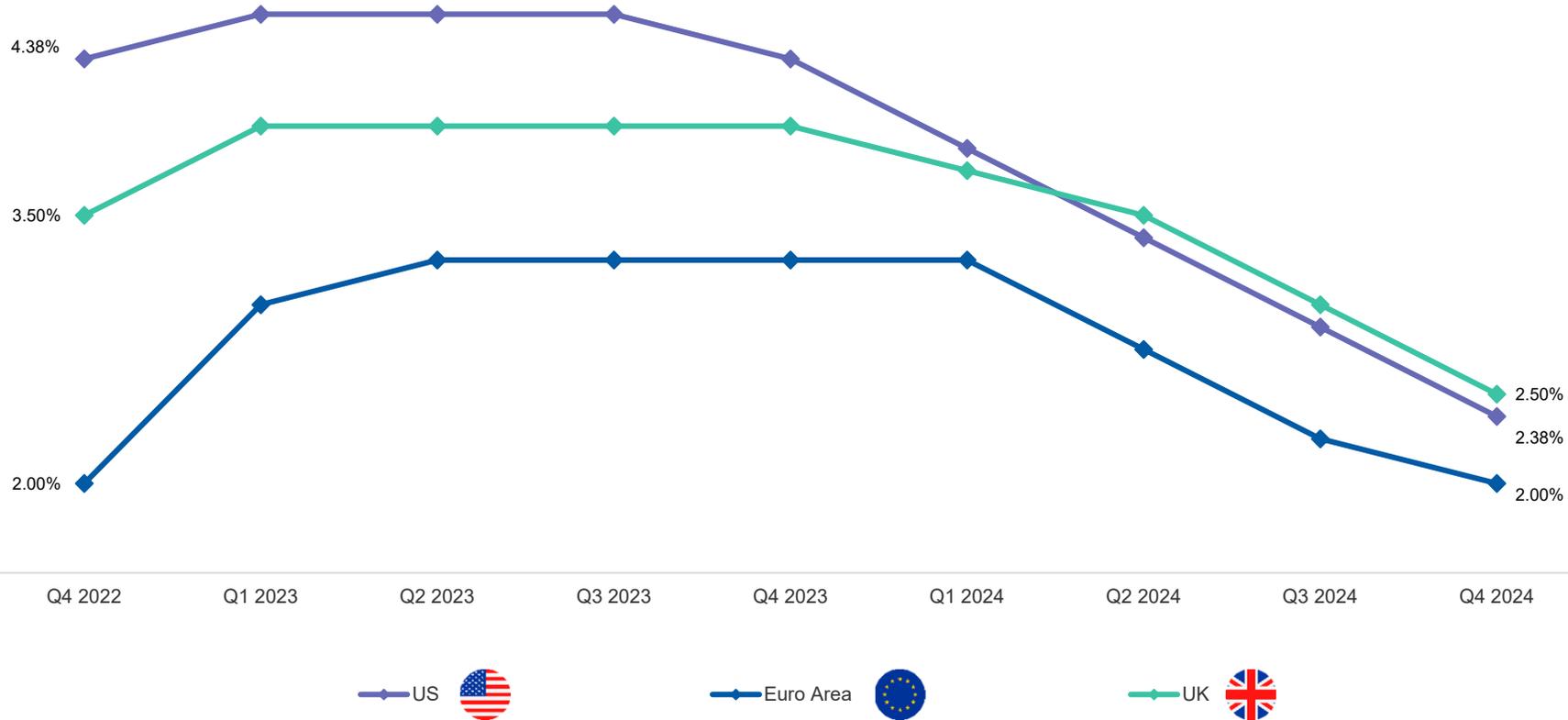
Today, The Macro Picture Remains Mixed

	Current	MS Research View at 2023 YE	Potential Impact to M&A Activity
Inflation	<ul style="list-style-type: none"> 6.5% Crude Oil: \$86 	<ul style="list-style-type: none"> 2.5% Crude Oil: \$110 	 <ul style="list-style-type: none"> Lower inflation could lead to Fed pausing, increased Macro certainty
Interest Rates	<ul style="list-style-type: none"> Fed Funds: 4.375% 	<ul style="list-style-type: none"> Peak at 4.625% in Q1 Year end 4.375% 	 <ul style="list-style-type: none"> M&A levels to increase when the Fed pivots following lower inflation / recession clarity
U.S. Economic Growth	<ul style="list-style-type: none"> GDP (quarterly, Q4): 1.0% Unemployment: 3.6% CEO Confidence: 32 S&P 500 EPS: \$219 	<ul style="list-style-type: none"> GDP (quarterly, Q4): 0.3% Unemployment: 4.4% CEO Confidence: N/A S&P 500 EPS: \$195 	 <ul style="list-style-type: none"> Potential "earnings recession" could result in valuation resets, acquisition activity over time Greater clarity on overall economic prospects a positive, recession obviously a negative
Debt & Equity Markets	<ul style="list-style-type: none"> UST: 3.5% S&P 500: 4,071 	<ul style="list-style-type: none"> UST: 3.15% S&P 500: 3,900 	 <ul style="list-style-type: none"> Equity valuations to season in 1H 2022 leading to opportunistic M&A Leveraged finance markets improving
Regulatory	<ul style="list-style-type: none"> Significant enforcement activity 	<ul style="list-style-type: none"> Same intense focus 	 <ul style="list-style-type: none"> Large transactions impacted in 2023
Currency	<ul style="list-style-type: none"> EUR/USD: 1.09 	<ul style="list-style-type: none"> EUR/USD: 1.15 	 <ul style="list-style-type: none"> Historically low exchange rates typically spur cross border activity
Other Factors to Consider	<ul style="list-style-type: none"> Ukraine War China / Taiwan China Re-opening Recession in Europe Gas Shortage Brexit Impact 		

Source: Morgan Stanley Research, The Conference Board, The Federal Reserve, CapitalIQ

Rates May Be Close To Peak...

Morgan Stanley Forecasts, (%)

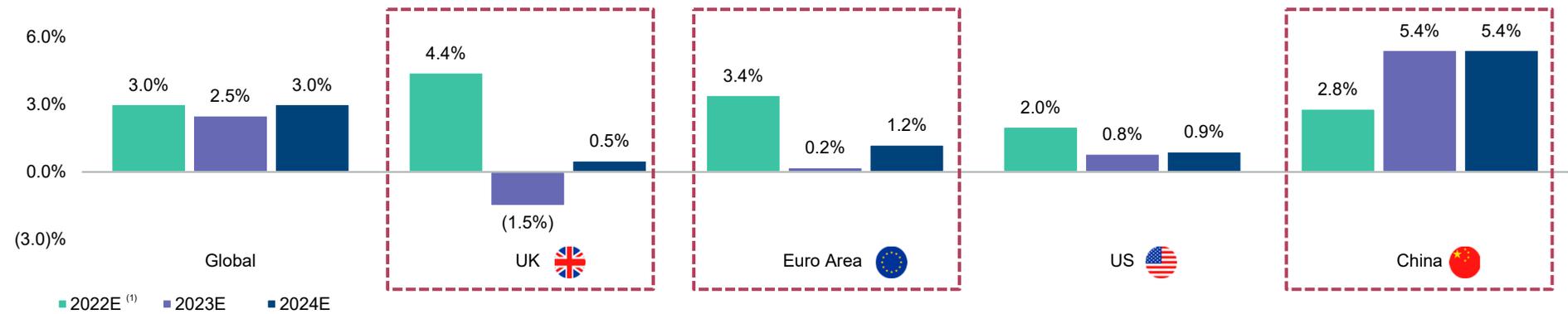


Source: : MSCI IBES, Morgan Stanley Research Forecasts January 2023

... But Inflation and Recession Concerns (Should) Continue to Weigh

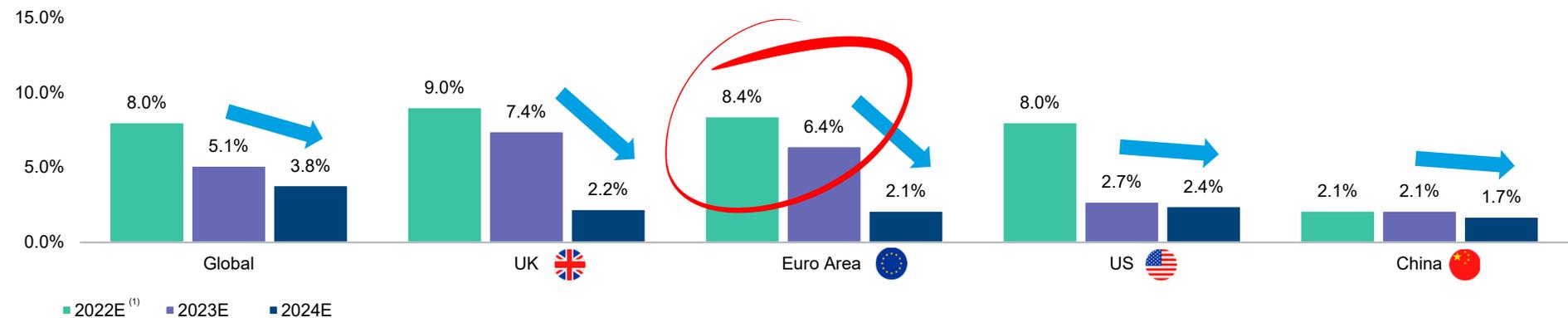
Growth

Morgan Stanley Real GDP Forecasts, (Y%)



Inflation

Morgan Stanley Global CPI Forecasts (%)



Source: : MSCI IBES, Morgan Stanley Research Forecasts January 2023

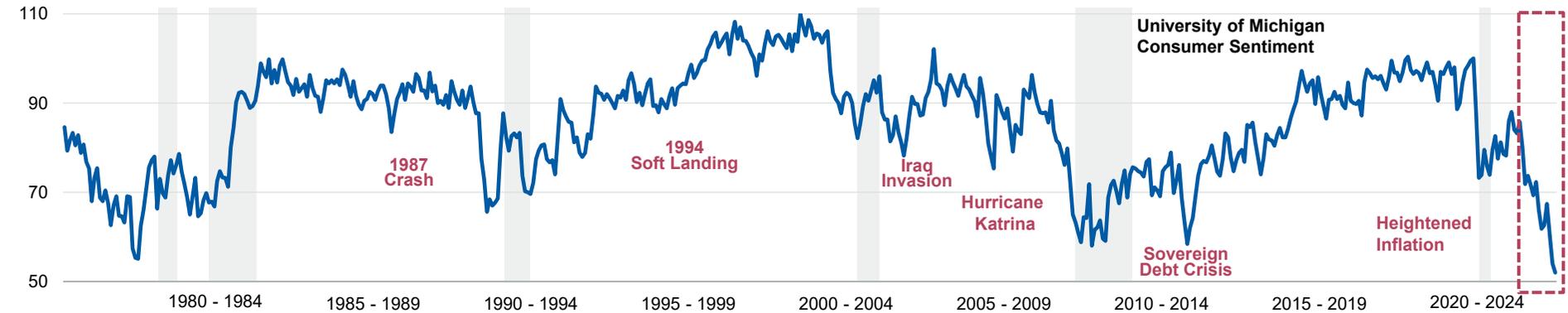
Notes:

1. 2022 CPI and Real GDP growth data is expected to be published in Q1 2023

...And The Consumer Remains Significantly Challenged

Consumer Sentiment Has Fallen To An All-Time Low

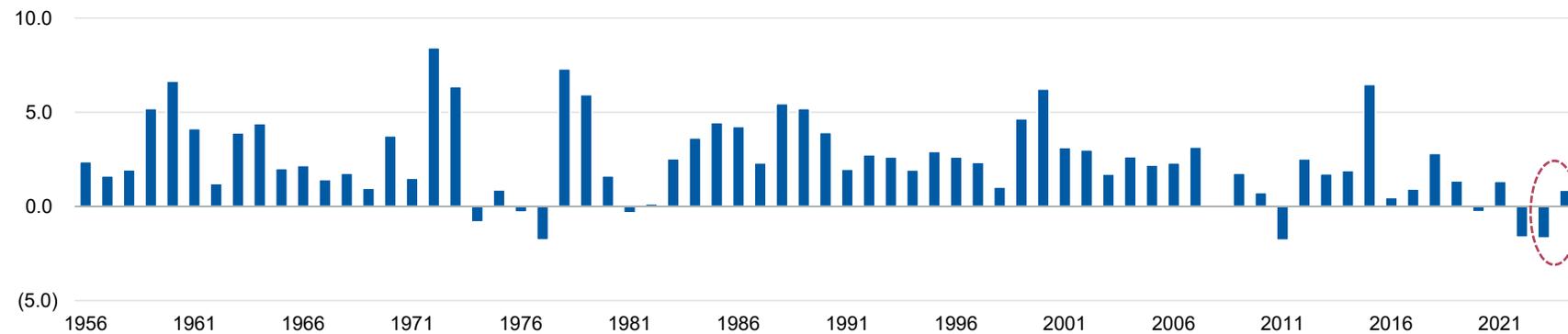
University of Michigan Consumer Sentiment Index



Source: Bloomberg

There Is Likely To Be a Record Hit to Disposable Income

Real Disposable Income, % Change YoY

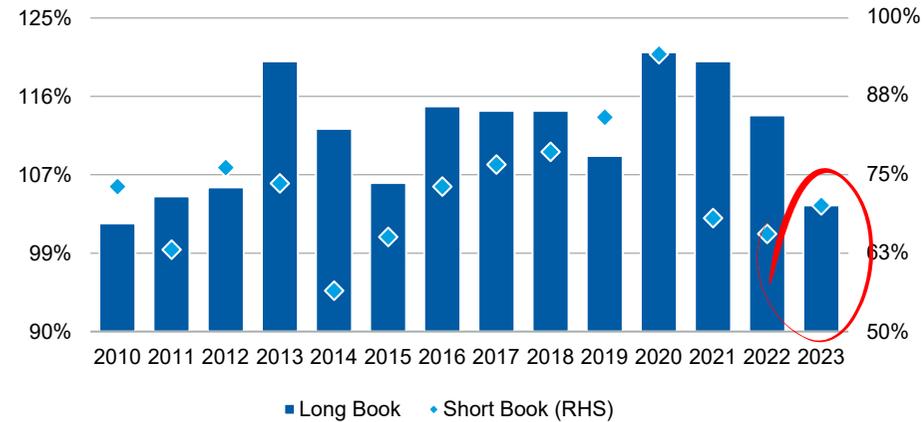


Source: Morgan Stanley Research, ONS

Reflected in the Lightest Cash Long Book in Europe in Over 10 Years (and Well-Hedged Too)

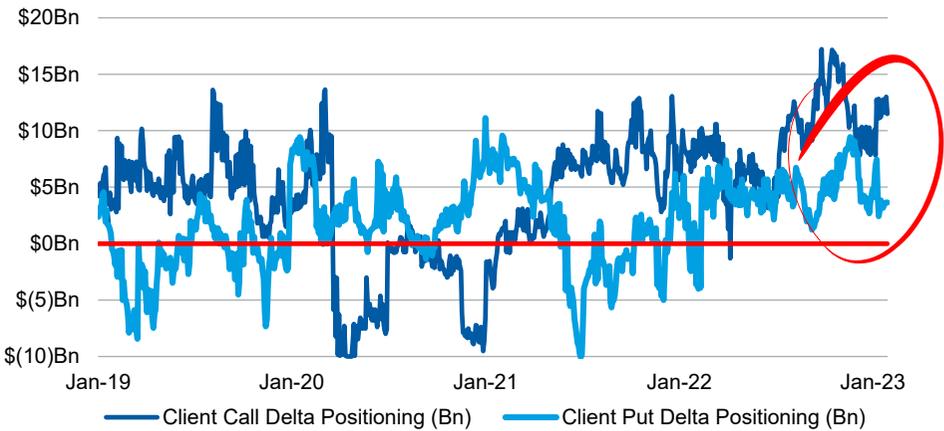
European Long/Short hedge Funds Enter 2023 With the Lightest Cash Long Book in over 10 Years

European Long/Short Hedge Fund Exposure Entering the Year



Well Hedged European Futures Protecting the Downside

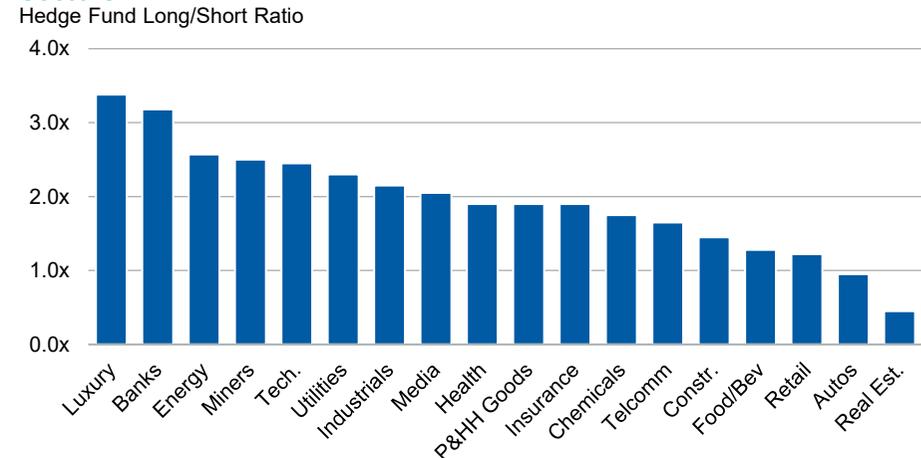
Client-Side Delta Positioning in European Equities



2022 Saw a Record Level of ETF/MF Outflows; Passive Flows Typically Reverse After Periods of Extended Weakness



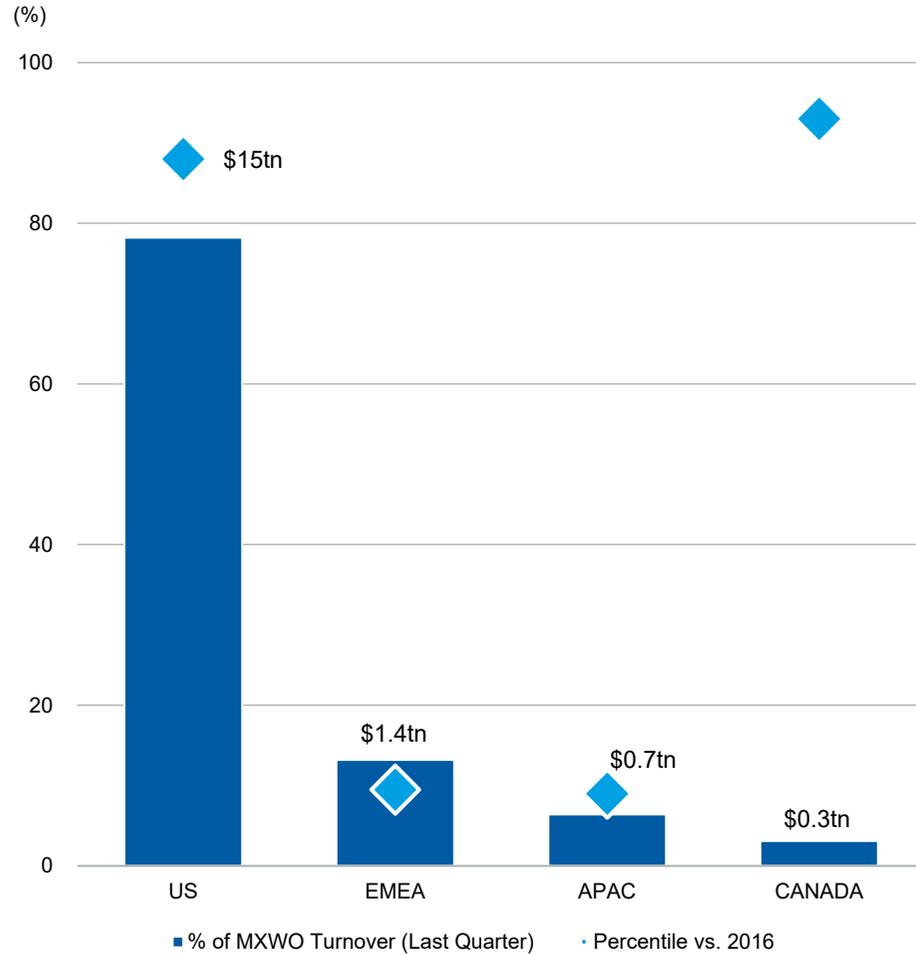
Hedge Fund Long Exposure Heaviest in China and Inflation Exposed Sectors



Source: Morgan Stanley EU Equity Derivatives as of January 2023

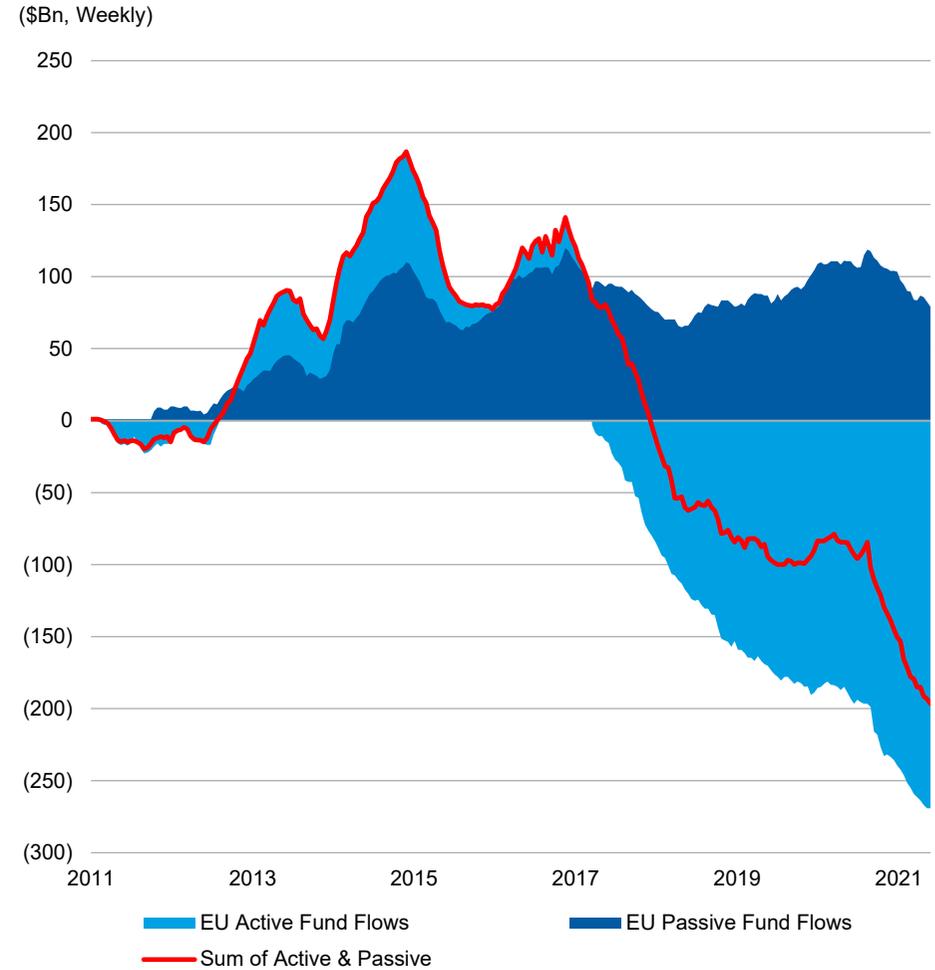
...And Unfortunately Reflecting a Long Trend in European Equities

World Equity Traded Value by Region (MXWO)



Source: MS EU Equity Derivates

Equity Fund Flows



Source: MS EU Equity Derivates, EPFR

Agenda

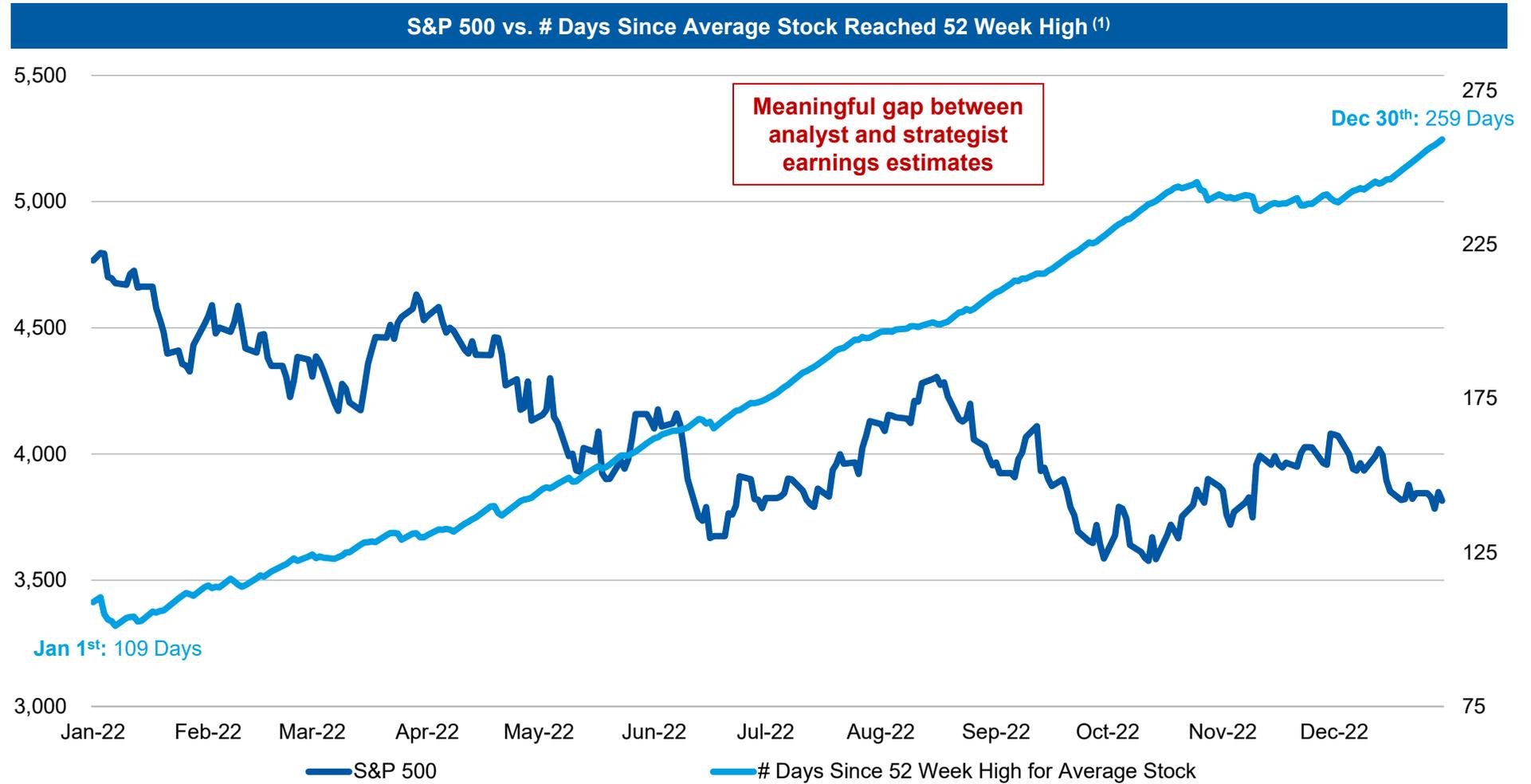
1 2022: The Year In Review

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Public Market Valuations Seasoning at Lower Levels

Notwithstanding Recent Rally – Potential for Sellside Capitulation?



Source: Capital IQ

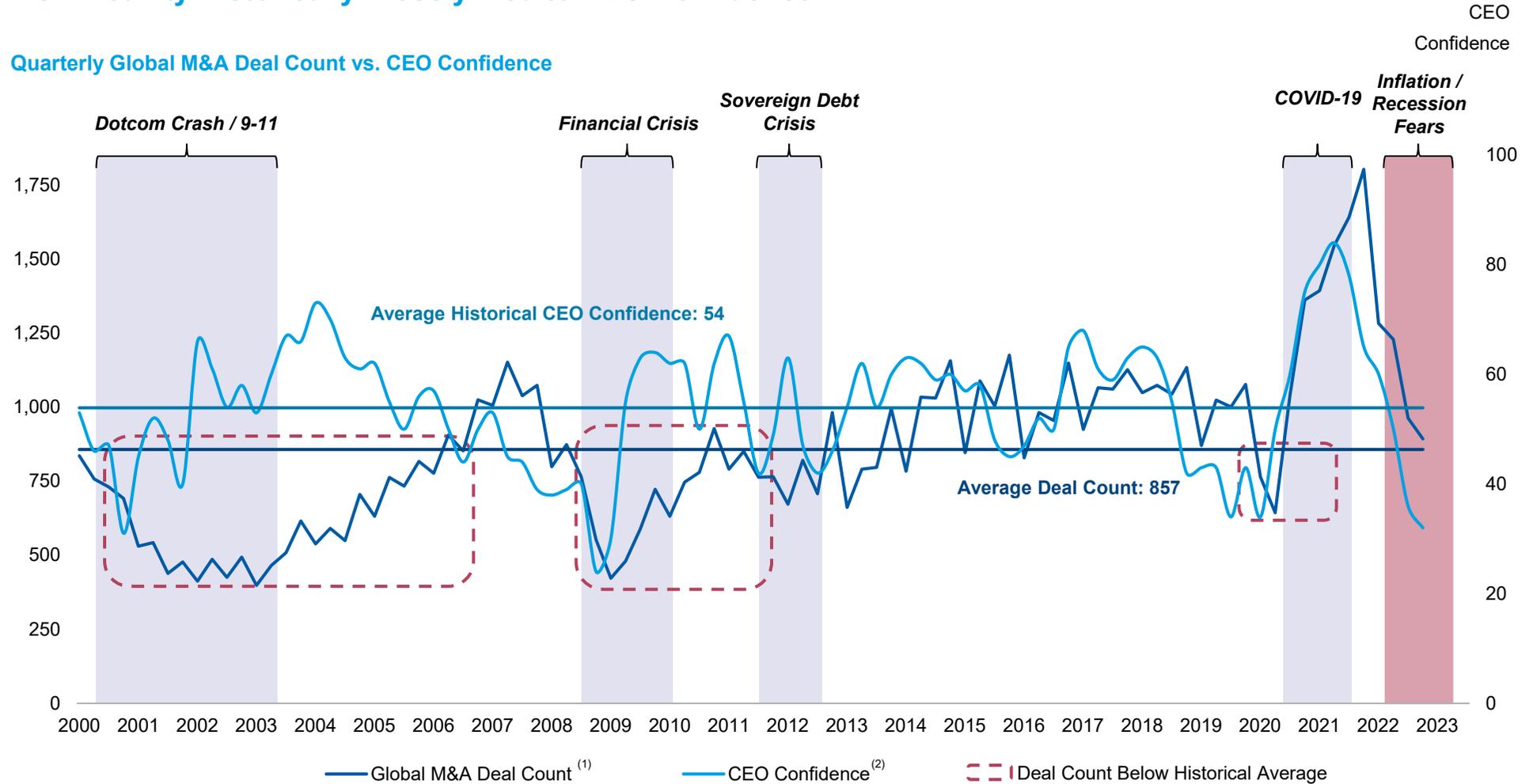
Notes:

1. Market data and S&P 500 constituent list as of December 30, 2022

CEO Confidence May Be Troughing?

M&A Activity Historically Closely Tied to CEO Confidence

Quarterly Global M&A Deal Count vs. CEO Confidence



Source: Refinitiv as of December 31, 2022, The Conference Board Measure of CEO Confidence Report Third Quarter 2022

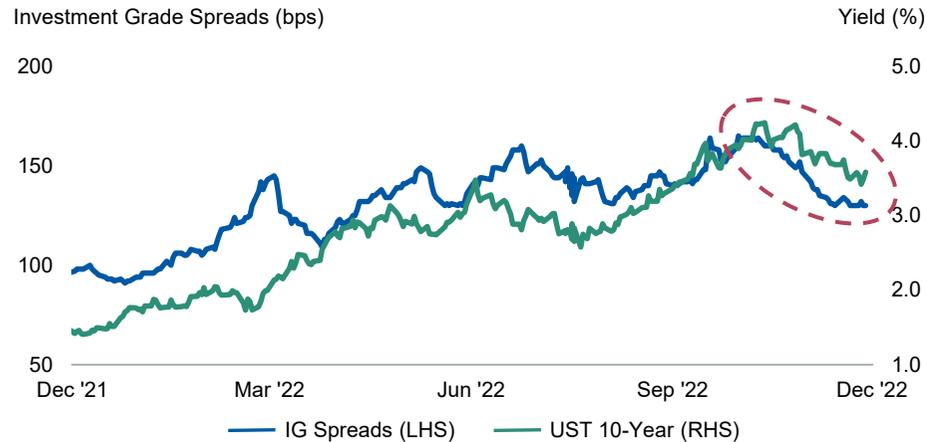
Notes:

- Includes global announced transactions, each with an aggregate value of \$100MM or more. Includes transactions with estimated values. Excludes terminated transactions. Future terminations of pending transactions will reduce totals shown
- The Conference Board Measure of CEO Confidence is the average of survey scores for three questions asked to approximately 100 global CEOs in a wide variety of industries. The score for each question is determined by assigning the following values to the replies: Substantially Better - 100; Moderately Better - 75; Same - 50; Moderately Worse - 25; Substantially Worse - 0. The score for each question, and the Measure of CEO Confidence, thus can range from 0 to 100

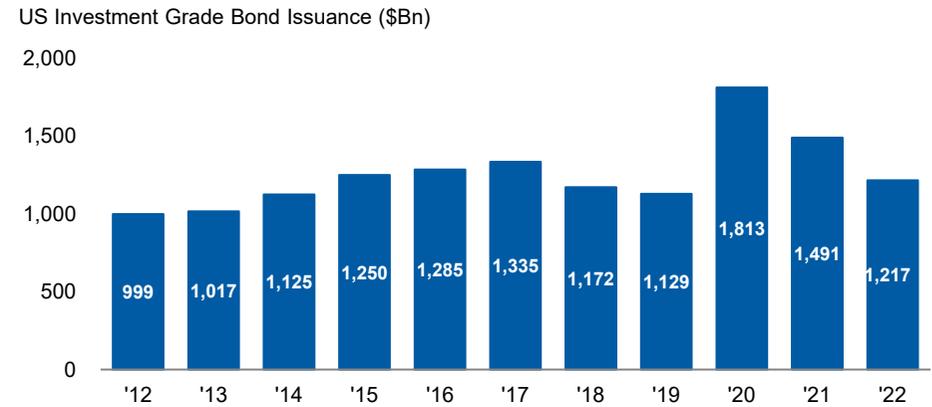
Investment Grade Market Demonstrably Stronger in Recent Weeks...

Technicals Showing Real Improvement As We Move Through Q1

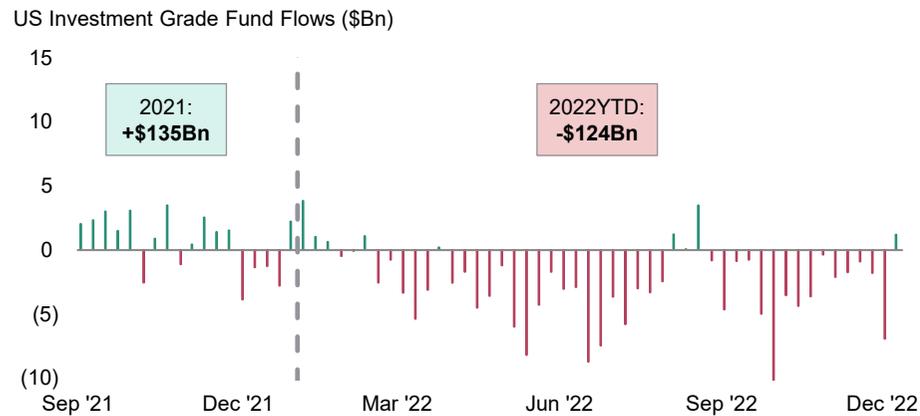
IG Spreads And Treasury Yields Continue To Drop From YTD Highs



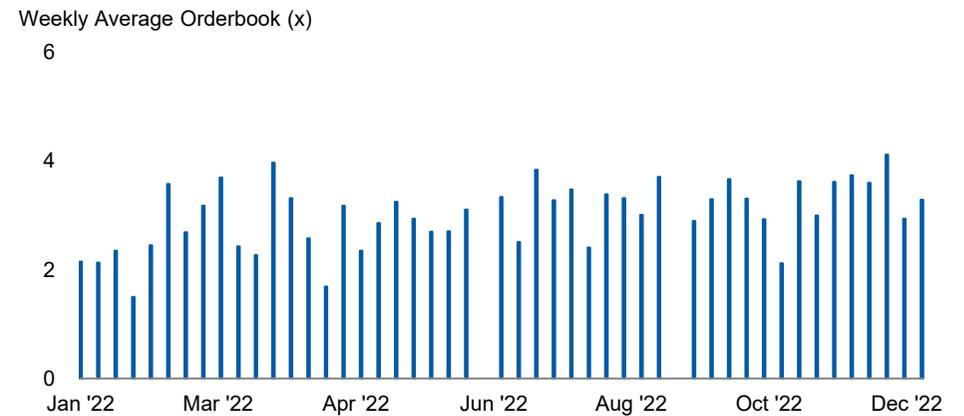
Issuance In Line With Historical Averages



IG Market Sees Inflow After 15 Consecutive Weeks Of Outflows



Orderbooks Remain Healthy In 2022

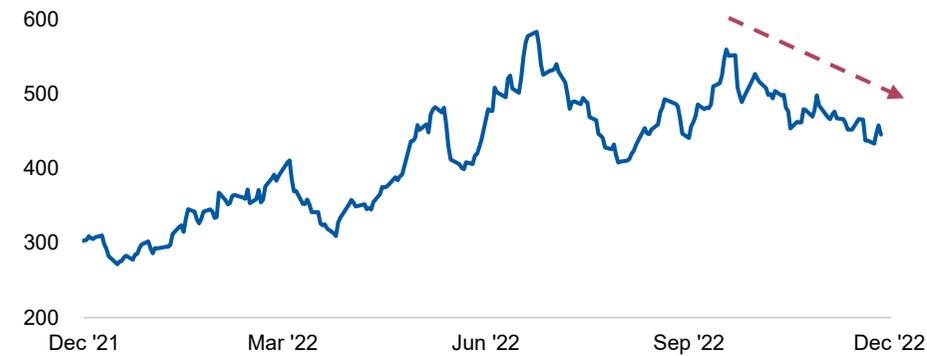


...And Non-Investment Grade Market Showing Signs of Life

Committed Backlog Beginning to Clear and Issuance Picking Up Following Modest Stability

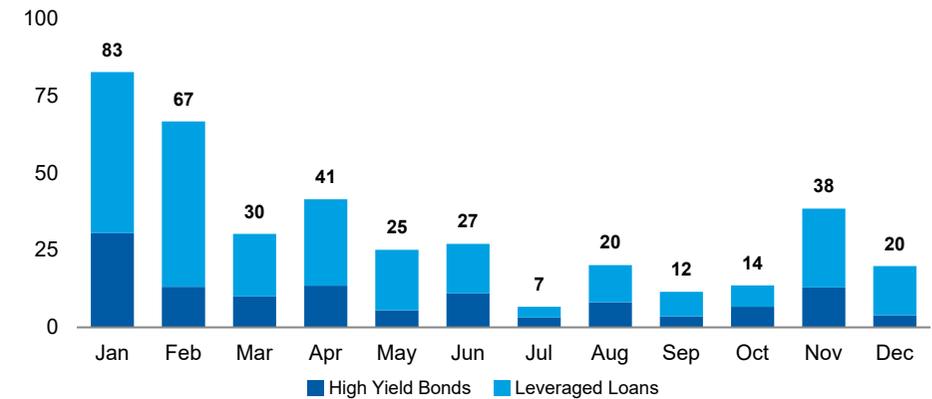
Spreads Remain Elevated, But Off Wides

High Yield Spreads (bps)



Active Issuance Through Year-End Following Slow Third Quarter

2022 High Yield Bond and Leveraged Loan Issuance (\$Bn)



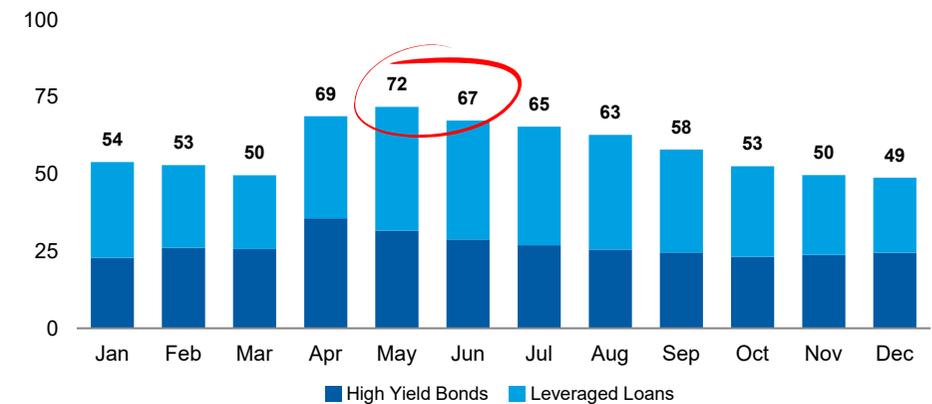
\$6.3Bn Of Inflows In Fourth Quarter

US High Yield/Leveraged Loan Fund Flows (\$Bn)



Backlog Slowly Clearing Post Mid-Year Peak

2022 High Yield Bond and Leveraged Loan Public Backlog (\$Bn)



Early 2023 Activism Outlook – A Meaningful Catalyst

- The number of activism campaigns in 2022 **exceeded 2021 levels by ~15%**

- M&A and improvement in operations were the most common financial demands in 2022

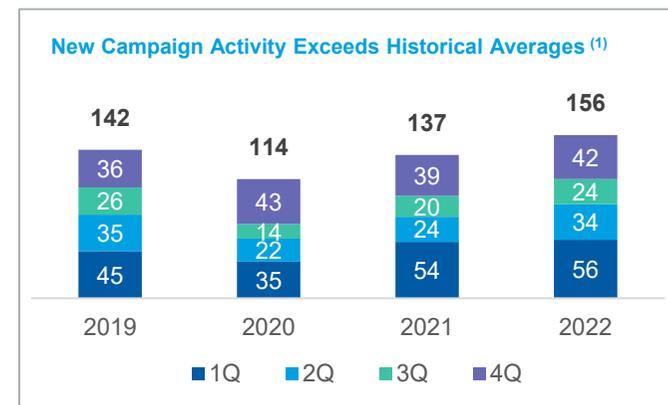
- Bayer, Unilever, Vantage Towers already a focus in 2023**

- Currently an **uptick in activists privately doing diligence** and preparing to take new stakes or launch campaigns in the new year

- Uptick in private engagement due to a combination of activists taking the view that the equity market is stabilising, or is about to, at lower valuation levels

- Campaigns in 4Q (and those expected in 2023) have been more **focused on management changes and operational themes**

- New "pass-through voting" frameworks** from BlackRock, Vanguard, and State Street among other institutional investors are starting to be rolled out



Source: FactSet

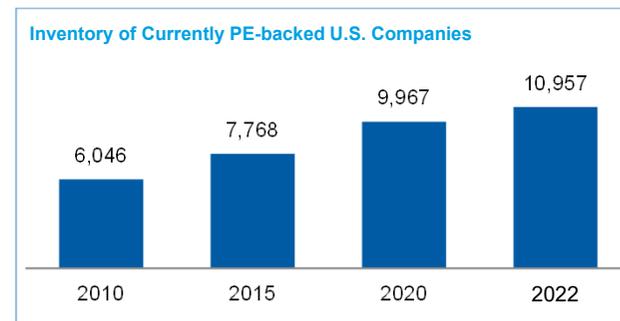
Note:

1. Includes campaigns targeting U.S. companies with market capitalizations above \$500MM as of December 31, 2022; companies may be targeted by more than one campaign per year. Excludes public short campaigns, hostile takeovers without activist campaign, 13Ds filed with no publicly disclosed activism, campaigns supporting management, and exempt solicitations

“Private Equity Will Find a Way to ‘Return’ in 2023...”

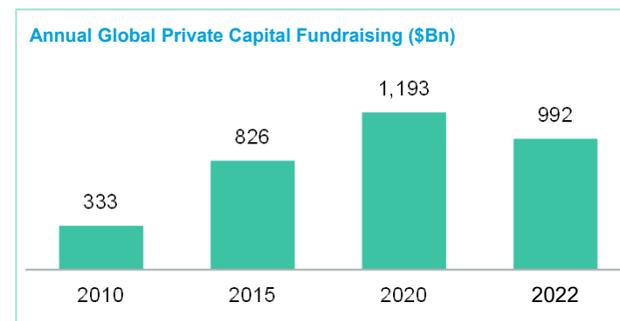
Record Number of Portfolio Companies

- ~11,000 portfolio companies in the U.S. alone
- Aging sponsor portfolios and proliferation of financial sponsors are a few key factors that will continue to drive sponsor exit activity
- Continuation fund transactions expected to grow



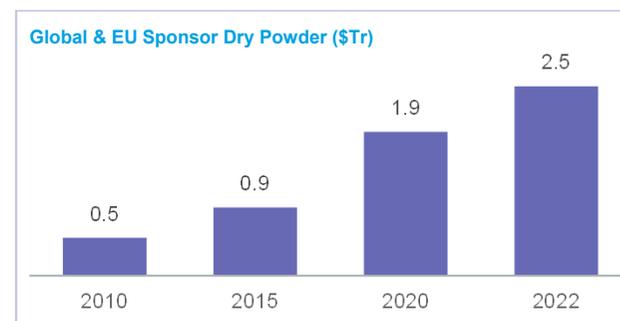
Fundraising Continues at Pace

- ~\$1 trillion raised in 2022 – even in a tougher market
- Fundraising volumes have remained relatively constant at ~\$1 trillion annually since 2016
- Four new ~\$20 Bn funds being raised / closed with European focus



Dry Powder Needs to Be Invested

- Accumulated dry powder for buyouts has reached peak levels at ~\$3.0 trillion
- Increasing specialization improves the ability to invest at all points in the cycle



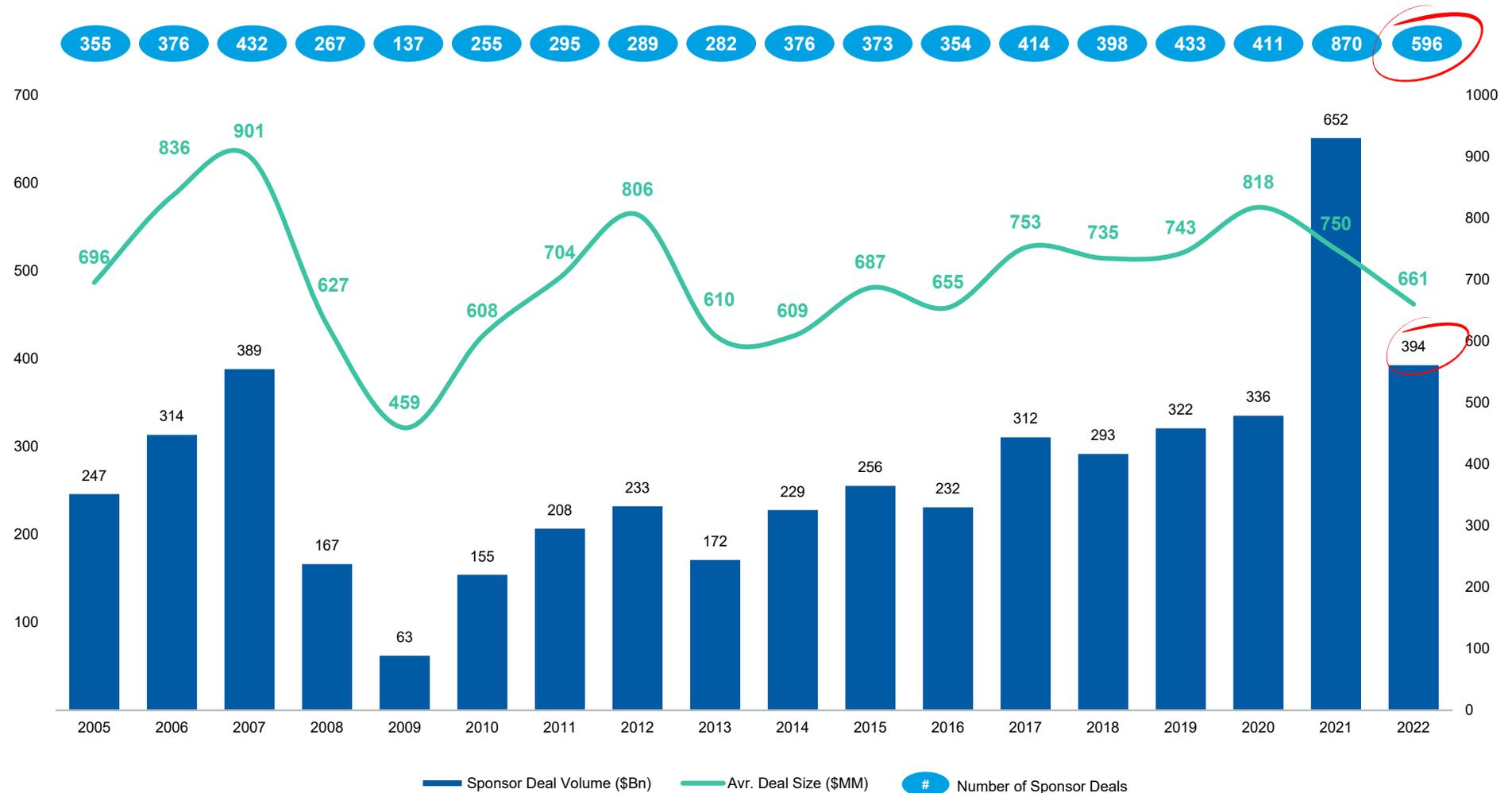
Sources: PitchBook, Preqin

...Having Cooled from Record 2021, But Actually Remained Very Strong

EMEA M&A – Financial Sponsors Deal Activity ⁽¹⁾⁽²⁾

M&A Volume (\$Bn)

Average Deal Size (\$MM)



Source: Refinitiv as of 31 December 2022

Notes:

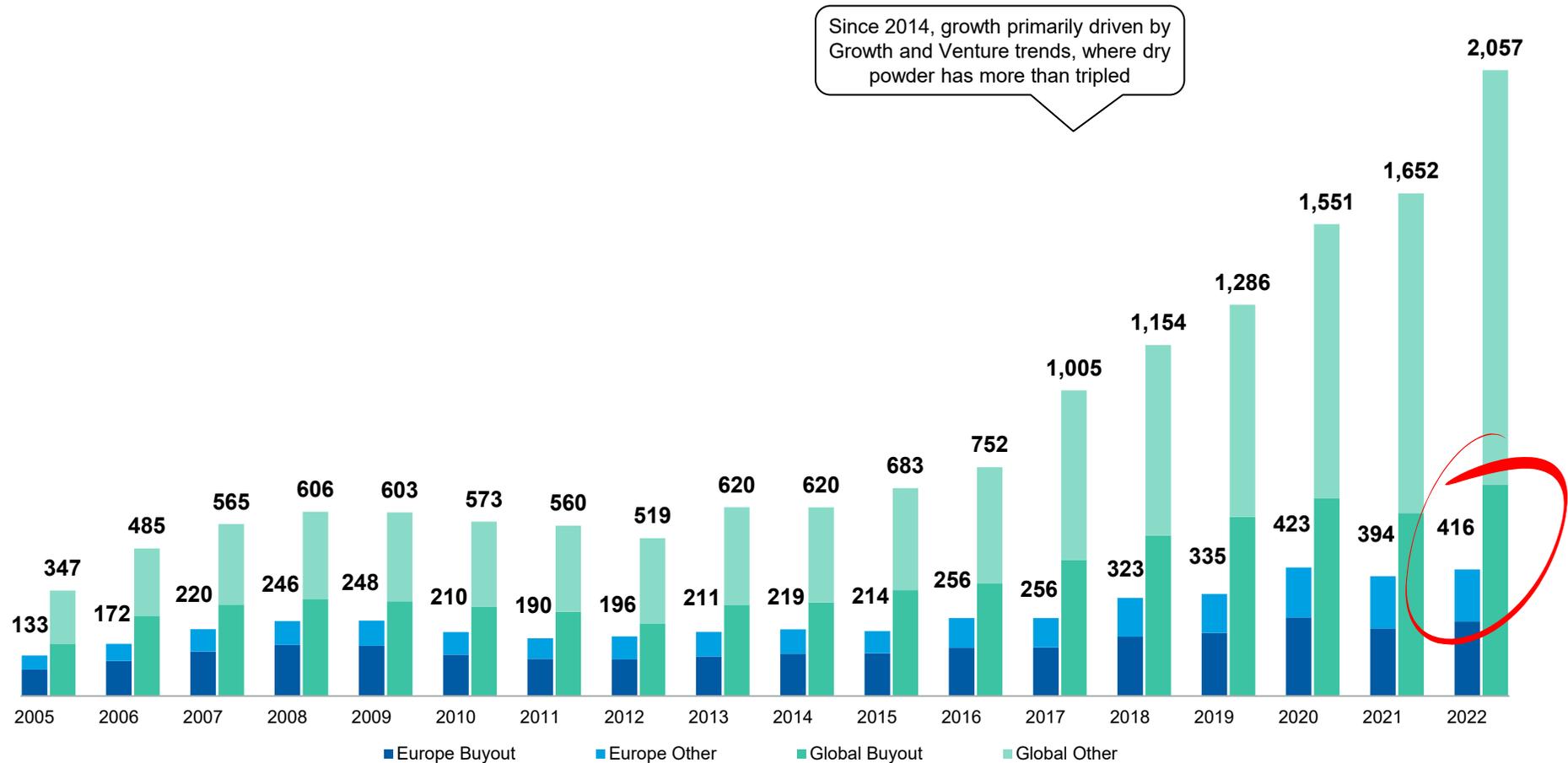
- 1. Includes transactions >\$100MM in size
- 2. Financial sponsor universe consists of private firms and their portfolio companies

Buyout Dry Powder Levels Have Continued to Increase

European Funds At Record Levels

Global ⁽¹⁾ & European Dry Powder

\$Bn



Source: Preqin as of 31 Dec 2022

Notes:

1. Global dry powder includes funds based in all geographies excluding Europe. These funds can invest globally, including in Europe

And Global Fundraising Persists, Though Has Slowed from Recent Highs

Recent Fund Raises

Investor	Vintage	Fund Size	Focus
 THOMABRAVO	2022	\$24.3Bn	US
 Advent International GLOBAL PRIVATE EQUITY	2022	\$26.0Bn	Global
 VERITAS CAPITAL	2022	\$10.7Bn	US
 PERMIRA	2022	\$16.0Bn	Europe
 FP FRANCISCO PARTNERS	2022	\$13.5Bn	US
 KKR ⁽¹⁾	2021 / 2022	US \$19.0Bn / EU €8.0Bn	US / Europe
 H&F	2021	\$24.4Bn	US
 Blackstone	2021	\$11.0Bn	Global
 TA ASSOCIATES	2020	\$12.0Bn	US

Open and Upcoming Fund Raises

Investor	Vintage	Target Size	Focus
 TPG	2022	\$15.0Bn	Global
 Blackstone	2022	\$30.0Bn	Global
 H&F	2022	\$30.0Bn	US / Europe
 THE CARLYLE GROUP	2022	\$22.0Bn	US
 IEQT	2022	€18.0Bn	Europe
 Vista Equity Partners	2022	\$20.0Bn	US
 CLAYTON DUBILIER & RICE	2022	\$20.0Bn	US / Europe
 Brookfield	2022	\$25.0Bn	Global
 APOLLO INVESTMENT CORPORATION	2021	\$25.0Bn	US / Europe

Source: Preqin, Fund Sources

Notes:

1. Indicates the two recent KKR flagship funds: KKR North America Fund XIII and KKR European Fund VI

 EMEA Funds

Continuation and Minority Sale Deals Are Increasingly Popular

Recent Continuation & Fund to Fund Sales

  <p>Deal Value: n.a. <i>December 2022</i></p>	  <p>Term Loan: €260 MM RCF: €84.5 MM <i>June 2022</i></p>	  <p>Deal Value: n.a. <i>June 2022</i></p>	  <p>Deal Value: n.a. <i>January 2022</i></p>
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● Continuation Fund Transfer ★ Fund to Fund Sale

Recent Minority Sale Deals

  <p><i>January 2023</i></p>	  <p><i>November 2022</i></p>	  <p><i>November 2022</i></p>	  <p><i>September 2022</i></p>
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Source: S&P LCD News, Debtwire, Public Sources

Key Private Equity Themes in The Current Environment

1 Recent large fund-raisings mean record high levels of dry powder...

- >\$3 Trillion Dry Powder Globally⁽¹⁾
-

2 ... However tougher current fund-raising environment

- Pressure on sponsors to slow levels of deployment
 - Need to return money to LPs will drive exits
 - Expect acceleration of monetisation of public stakes post 2021 IPO wave
-

3 Sponsors are planning for return of leveraged financing markets

- Hiring banks for exits with no set timetable — “When the market is back”
 - P2P watchlist — multiples have already derated, now want to find the bottom on earnings
 - Fund all equity or with bank financing ahead of financing market returning
-

4 “Better the Assets you know”

- Battle for AUM will fuel partial exits, private stake sales and continuation funds
 - Buying back IPO'd companies previously owned
-

5 Increasing GP Activities

- Monetising the GP for founder partners (IPO, Stake sales)
 - Growing the GP to become more diversified (M&A to add new verticals, fund level debt raisings)
-

What to Expect for Broader M&A in 2023?

Expect 2023 to Start Slow but Accelerate in the Second Half



Well capitalized corporates will continue to make acquisitions to gain capabilities and adjacencies

- As valuations continue to “season”, buyers will execute on acquisitions with strategic logic/ necessity
- Need to re-wire supply chains and reduce logistics/ geopolitical exposure
- Stock-for-stock deals will increase meaningfully
- Regulatory environment continues to dampen large scale M&A



Corporate clarity remains a theme – spin-offs and divestitures to continue

- Lower valuations make separations more likely – especially for high value assets trapped in larger corporates



The “return” of financial sponsors

- \$3 trillion of dry powder needs to be deployed; \$400+ Bn in Europe
- Leveraged finance markets, albeit more expensive, will re-open



Unsolicited activity should increase

- Valuation expectations will reset and shareholders may push Boards to transact
- Synergies increasingly valuable in lower valuation, lower margin environment



Activism to continue apace

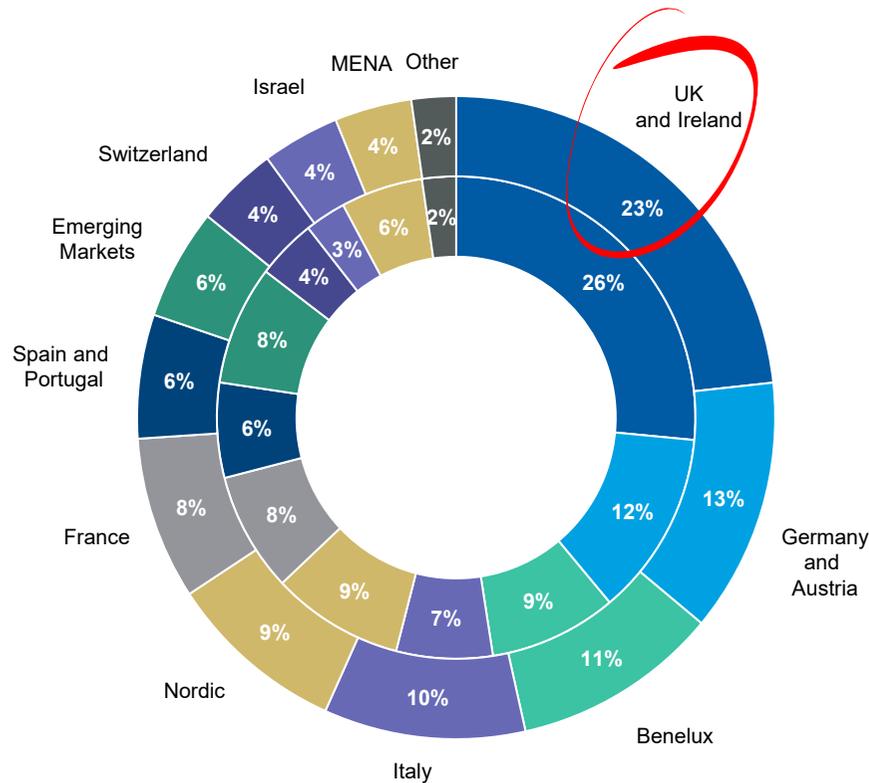
- Highlighting separation alternatives and “Sale of the company” theses
- Operating performance within sectors remains uneven

By Region and Sector – Where Might the Activity Happen?

UK, EM Volumes Down; Utilities & Transport Up

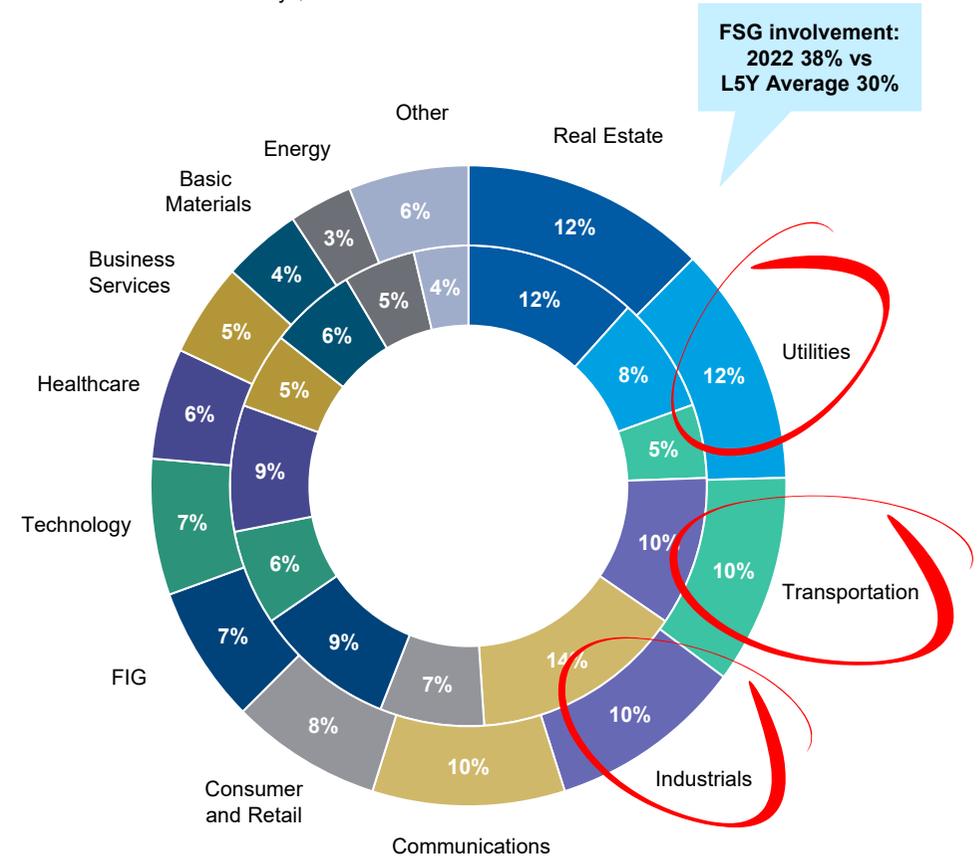
EMEA Announced by Region ⁽¹⁾ ⁽²⁾

Outer Circle: 2022 EMEA % by \$ volume
 Inner Circle: L5Y EMEA % by \$ volume



EMEA Announced by Industry ⁽¹⁾ ⁽²⁾

Outer Circle: 2022 EMEA % by \$ volume
 Inner Circle: L5Y EMEA % by \$ volume



Source: Refinitiv as of December 31, 2022

Notes:

- Includes announced transactions with EMEA participation, each with an aggregate value of \$750MM or more. Includes transactions with estimated values. Excludes terminated transactions. Future terminations of pending transactions will reduce totals shown. Q4 2022 figures preliminary and potentially subject to revision
- 2020 excludes Unilever \$107Bn dual-head collapse. Next acquisition of Altice adjusted to \$2.7Bn. 2021 excludes BHP \$86Bn dual-head collapse

How Do We Reset For This Environment

The Challenges For All of Us...



Identifying Actionable Opportunities & Clients with the Need/ Opportunity to Transact

- Leaders less obvious/ non-traditional and now often at the further edges of the coverage footprint
- Significant bifurcation between winners & losers, and within industries (e.g. B2B versus B2C)
- Corporates looking to reduce logistics and geopolitical exposure & bring supply chains in-house/ closer to home
- Challenge of needing both a broader footprint but a deeper understanding of the client



Managing Execution Risks and Maximising Deal Certainty

- Regulatory remedies increasingly challenging when you don't know the problem you are trying to solve...
- Financing visibility and certainty of funds
- Flexibility on due diligence (heavy preparation), but then bespoke and flexible processes



Financing Structures Will Continue to Evolve Meaningfully

- Bank processes will be tougher and Private Equity will need to be nimble and ready to hit windows
- Hedging and rate/ inflation swaps/ locks under utilized/ appreciated
- Increasing use of alternative capital, large side pockets and equity bridges to re-financing when debt windows open



A Great Opportunity for Differentiated Advice and New Ideas

- Structures
- Speed and opportunity (including “national interest”)
- Alternative sources of capital