The Deal WEBCAST

Tech M&A Trends in 2021

Presented By

Tech M&A in 2021: How Companies Are Dealing In and With Disruption

A global pandemic, a fully remote workforce, record-breaking vaccine development, supply chain meltdowns and a special purpose acquisition company explosion – the year 2020 brought a whole new meaning to the word disruption.

For many in the tech sector, that disruption has been a good thing.

After the Covid-19 pandemic initially disrupted sales and caused massive delays for Amazon.com Inc. (AMZN), the book-retailer-turned-tech-behemoth nearly doubled its full-year earnings per share on a diluted basis in 2020 and saw its sales climb 38% from the previous year to $380 billion.

Movie theater shutdowns and country-wide lockdowns helped drive a record 36.6 million new subscribers to Netflix Inc.'s (NFLX) platform in 2020, bringing its total worldwide viewership over 200 million.

And as companies sent employees home to work across the globe, concerns over IT infrastructure and security became omnipresent, helping catapult cybersecurity firm CrowdStrike Holdings Inc.'s (CRWD) full-year sales 82% higher in 2020 and its stock price more than 320% higher on the year.

The momentum hasn't yet stalled in 2021.

> **"In 2021, the developing theme appears to be navigating the ripple effects of the previous year's disruption."**

Amazon's first quarter sales came in at $108 billion – up 44% from the same quarter in 2020 and representing about 39% of its total 2019 sales; streaming services provided by Netflix and others made up 26% of TV usage through the first half of 2021 versus 14% in all of 2019, according to new tracking technology developed by cable television data provider Nielsen Holdings plc (NLSN); and CrowdStrike's stock is up another roughly 20% year-to-date.

So what does all this mean for tech M&A in 2021 and beyond?

For one, many of these companies have unprecedented levels of deal currency. Global tech M&A registered its highest ever aggregate deal value of $303 billion across 871 deals during the first quarter of 2021, according to KPMG Corporate Finance LLC.

On the other hand, tech companies also are being forced to carefully consider the logic and rationale behind the types of deals they're making, in no small part due to the uncertainty surrounding the post-pandemic world.

In 2021, the developing theme appears to be navigating the ripple effects of the previous year's disruption, key deal advisers

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and dealmakers suggested during a web panel presented on June 15 by leading global law firm Pillsbury Winthrop Shaw Pittman LLP and The Deal.

Top of mind for C-suite executives and corporate development professionals today is deciphering how to sort out the temporary measures and the lasting repercussions of a drastic shift in the way companies have done business over the past 18 months, Pillsbury partner Allison Leopold Tilley explained on the panel.

"We're starting to see people, particularly those attempting to buy, try to understand what the return to work is for a company," Allison Leopold Tilley said of recent due diligence processes. "Do [targets] have excess real estate? If they're going to let all their people work from home, what are they going to do with all those empty office buildings? If you're a buyer, are you going to have to pick up all this basically empty real estate?"

These considerations are intensified when considering cross-border M&A, as each country is making different progress with vaccinations and combatting the deadly Covid-19 disease.

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"We have a lot of clients who are buying or selling things overseas – a lot of clients that have operations in India, which, as we all know, has been so hard hit," Allison Leopold Tilley said. "It's a very delicate dance to ask questions about what is going on with the work force of a company in India but still being very considerate of the fact that there are human lives involved.

"So we're seeing a real difference in how people are doing due diligence and planning for the return to work in these different countries, especially for the buyer, who is trying to understand how they're going to integrate that work force and what they're really going to get at the end of the day."

Beyond the effects the pandemic has had on how tech companies look at deals, it also has temporarily transformed how these businesses make deals happen.

In the U.S., powerhouse dealmakers are starting to venture back in the world for at least some in-person deal talks.

"In a few hours, I'm getting on a flight for my first in-person management meeting since the pandemic started," Vista Equity Partners LLC senior managing director Rene Yang Stewart said during the mid-June web panel, adding that the firm is going to take its cues on in-person meetings from the companies with which it partners. "Every CEO I've begun to offer an in-person meeting to has taken me up on it."

Investing is a people- and relationship -driven business, after all, Stewart argued.

"At the end of the day, you are at a disadvantage if you're not willing to fly and meet with a CEO in person," she said. "When people see competitors doing it, they're going to start doing it as well because no one wants to lose a deal because [they refused to meet in person]."

Nevertheless, Stewart sees some elements of the pandemic dealmaking universe surviving in the long-term, particularly when it comes to early stage investments.

"There I think folks are getting used to writing checks never having met face to face, so I think that's here to stay," she said. "On later stage investments, where you're actually acquiring companies, maybe travel won't go back to the same degree as before with some introduction meetings done virtually."

Meanwhile, at least for the moment, local investors are experiencing a bit of an advantage over cross-border suitors due to the varying stages at which countries sit on the path to Covid-19 recovery.

"In the U.S., I think we're entering a period where travel is starting to come back," Sun Capital Partners managing director Elizabeth de Saint-Aignan said. "We're seeing that a little bit across our business in Europe, although I'd say because vaccination rates have lagged in Europe versus the U.S., it's coming back a little more slowly. So there has been a bit of a trend toward a benefit for local investors, but just as we're seeing things roaring back with interest in in-person in the U.S., I would expect we'll see that internationally as well within the next three to six months. So we'll see any benefit for local investors washout relatively quickly."

Another bifurcation of the pandemic's temporary and permanent effects on dealmaking may develop between the due diligence and negotiation phases of a transaction, Pillsbury's Allison Leopold Tilley explained.

"What appears to be a management headache and potential public relations nightmare to some industries may be a blessing in disguise for the tech sector. "

"Right now, we can be negotiating a deal, and in three hours, we can be negotiating a deal in a different country," she explained. "I think parts of that will stay in the M&A practice. But I do think in-person diligence will come back before in-person negotiations because in diligence meeting people face-to-face and seeing operations in person makes a difference."

As a result of the varying benefits and drawbacks of remote working that companies have discovered during the Covid-19 pandemic, many industries are grappling with whether to consider remote working a permanent change or a temporary measure.

But the tech sector may see less of an issue over that debate, at least to some degree.

Companies in which the majority of the workforce spends all of its time at a computer writing software code may see less controversy in allowing said workforce to work remotely than companies in which some or most of the workforce spends its time on a plant floor producing chemicals or industrial machinery.

The latter's companies' executives may find it hard to force those plant workers to commute to work, and potentially risk their lives, while its management team and sales and support staffs sit comfortably at home.

"It's so much easier when you have tech assets," Ansys Inc. deputy general counsel Patrick Belville said during the panel. "We can collaborate online; we can demo our products. It's just a much easier environment when everyone is virtual and working on a computer to start with compared to manufacturing, for example, where someone has to be at the facility on the floor. There, it feels less fair to the people who have to show up every day and still make the commute in when you have all of the executive team and the back-office staff working remotely."

In other words, what appears to be a management headache and potential public relations nightmare to some industries may be a blessing in disguise for the tech sector.

"For Ansys, in the legal department, the last five hires we've made have been during the Covid period, and none of those hires are located where our corporate headquarters is," Belville said. "And I think that's a trend that will probably continue. Most of my team is spread out from Colorado to Korea, and we feel like we can now go after our first pick – even though they were located in New Jersey – as opposed to whoever the person is that is local and available within commutable distance.

From a transaction perspective, Bellville explained that his team now can look at acquiring businesses across much broader distances because concerns such as whether the distance between offices would affect integration of teams have been removed.

"The idea that we might have a five-person office in Denver, or a small office in Detroit or France, is much less important," he added. "It's now much more about 'Where is the talent? How do we get access to that talent?' "

Of course, remote working is not the only thing disrupting the tech market in 2021.

The number of special purpose acquisition vehicles, or SPACs, to IPO exploded to around 250 in 2020 from around 60 in 2019, according to PrivateRaise, The Deal's proprietary data service tracking U.S. SPAC activity.

Conversation around SPACs so far in 2021 has remained robust, with the number of the so-called blank-check companies coming to market through the first half of the year approaching 350.

> **"People have lost value over time to private equity and late-stage growth funds."**

"From a late-stage perspective, one of the phenomena we've seen over the last 12 to 18 months is this late-stage public financing of private companies, also known as the SPAC," Jefferies LLC managing director Storm Duncan said. "The thing I think is unusual about today's SPAC versus previous iterations of it is that it is actually mostly high-quality companies that might or might not have been able to get public at that exact moment in time, but were on strong path to getting public, as well as companies that are high-capital needs companies in very large [total addressable market] industries that are displacing of other industries."

The automobile industry can provide such an example, where most companies that are public are focused on fossil-fuel vehicles that are neither autonomous nor shared.

As a public investor, people have lost value over time to private equity and late-stage growth funds as this industry shifts toward autonomous vehicles and the subscription-based model of vehicle ownership and these companies don't want to be public anymore before reaching the critical mass needed to deal with the strains of being a public company today, Duncan explained.

Whereas 30 years ago, a company could launch a $50 million IPO with a $250 million valuation, that is not possible anymore, he said. This has left the alpha produced by these companies in the hands of private investors.

"Companies don't want to be public anymore," Duncan explained. "What SPACs did is they opened up that possibility for public investors to invest in these late stage private companies that are displacing industries and potentially recapture some of that alpha."

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