pillsbury

US M&A

State of Affairs and Outlook Under the Biden-Harris Administration

2021

Mergermarket
An Acuris company

Contents

Foreword

The past year has been one of pronounced upheaval, not only in the United States but in all countries. The COVID-19 pandemic overwhelmed the global economy, public health systems and governments the world over, and M&A was brought to a near standstill in H1 2020. But the market began to thaw sooner than some might have expected—in H2, pent-up demand was unleashed, and Q4 2020 became the highest-value quarter ever for US M&A, according to Mergermarket data.

This breakneck seesawing in deal activity came ahead of a highly fraught presidential election that concluded with President Joe Biden and Vice President Kamala Harris winning the White House. It is difficult to predict with certainty what this victory will mean for M&A dealmakers. There are numerous pros and cons that must be evaluated and which, depending on the final iteration of particular policies and regulations, will impact businesses and investors in different ways and to varying degrees.

The US$1.9tn stimulus passed by Congress in March 2021 is an obvious win for the average American and will have a meaningful stimulative effect for businesses and the economy. An ambitious US$2tn infrastructure plan is equally value additive for investors and the economy. However, growing public debt as a consequence of the pandemic will have to be addressed at some point. One of the more contentious developments under the new administration is a proposal to raise the corporate tax rate and other taxes. Higher taxes and stricter regulations are hardly favored by business but, again, the devil is in the details. "Big Tech" companies, for example, will be the likely target of heightened antitrust scrutiny and enforcement, which could put disrupted competitors at a relative advantage.

One thing on which most investors agree is that President Biden's victory is a win for political stability. Whatever the challenges that businesses must navigate under the new administration, greater certainty and predictability should lay the foundations for a more stable M&A environment. After all, investors prefer to invest when they know what to expect.

Key Findings & Methodology

Our key findings include:

Respondents largely agree on the Biden-Harris administration's expected impact on M&A: 64% of corporates and 60% of private equity (PE) firms surveyed say the administration will be either conducive or very conducive for their dealmaking in the US.

59% of corporate respondents expect to undertake between one and three M&A transactions over the next 12 months. PE respondents are more bullish, with 56% expecting to strike at least four deals over the same period.

Overall, respondents expect most of their deals over the next 12 months to be domestic. PE firms say roughly four-fifths (83%) of theirs will be domestic. Corporates suggest that one-third of their transactions will be international in nature.

99% of respondents expect to undertake middle-market deals (worth less than US$2bn). Half expect to strike large deals (US$2bn-US$10bn), and 21% expect to undertake transformative transactions (over US$10bn).

Rising regulatory scrutiny is by far the most significant risk to respondents' dealmaking over the next 12 months, with 45% identifying it as their primary concern, followed by geopolitical concerns (16%) and higher corporate tax rates (13%).

The key driver of M&A activity over the next 12 months will be pursuing digital transformation: 24% (the largest such share) of respondents identify this as the most significant factor, and a further 19% cite it as their number two concern.

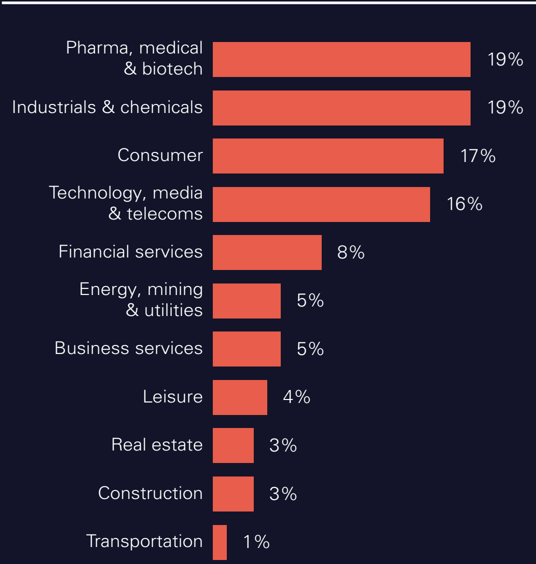
Methodology

In Q1 2021, Mergermarket surveyed 75 PE and 75 corporate executives based in the US to gain insights into how the Biden-Harris administration might impact M&A dealmaking. All responses are anonymous, with results presented in aggregate.

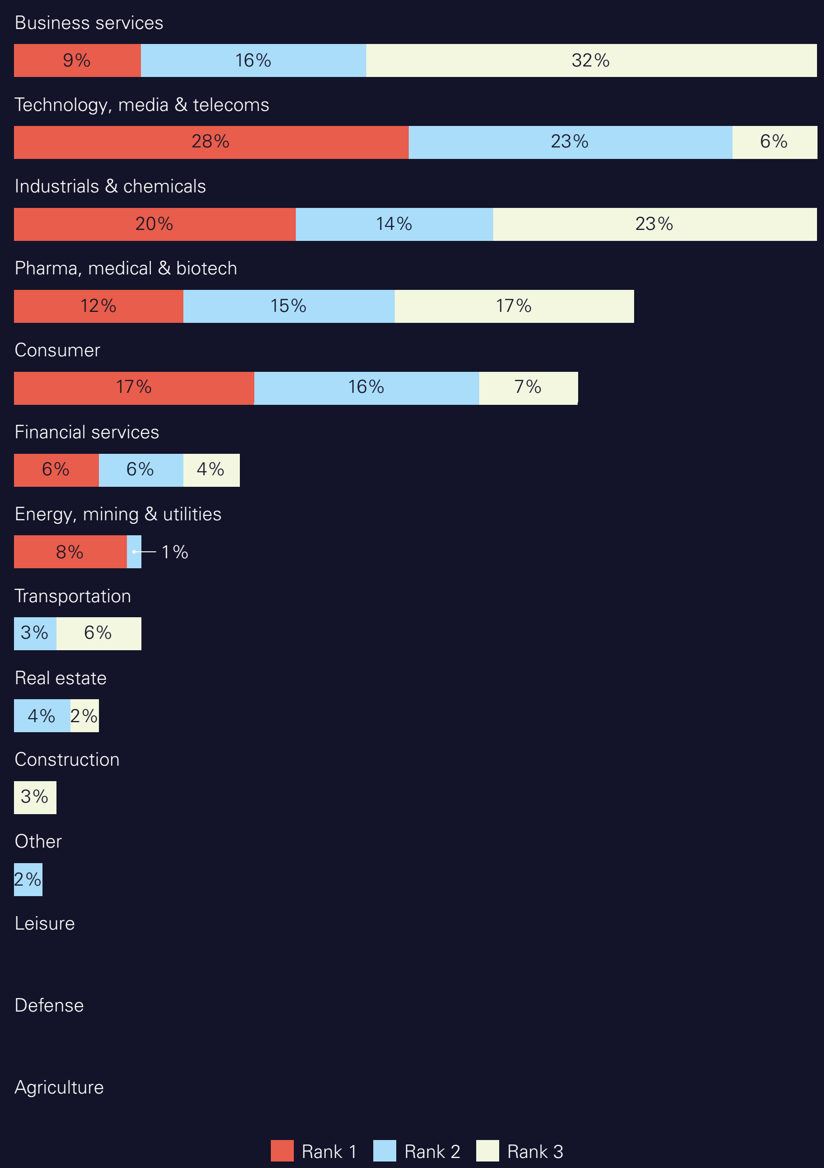
More than 70% of corporate respondents surveyed operate primarily in four sectors: pharma, medical & biotech (19%), industrials & chemicals (19%), consumer (17%), and technology, media & telecoms (16%). Financial services places a distant fifth (8%).

Among PE firms surveyed, 28% focus primarily on TMT, and a further 23% identify it as their second-most significant sector of focus. After TMT, the sectors that attract the most primary interest of PE respondents are I&C (20%) and consumer (17%).

In which of the following sectors does your company primarily operate? (Corporate respondents only) (Select one)



What are your main sectors of focus? (PE respondents only) (Select up to three and rank 1-2-3 by order of significance, where 1=most significant)



Introduction

Dealmakers have had to regain their bearings repeatedly over the past 12-16 months. Modifying business activities to function under work-from-home orders and assessing the impact of the pandemic on operations and strategic viability have put immense pressure on companies and financial sponsors. In the US, this disruption has been compounded by a change in administration following what many view as a months-long mishandling of the health crisis.

With so much uncertainty prevailing, we have prepared this report to shine a light on US M&A conditions. The goal of our research was to peer into the minds of dealmakers and better understand what they view as the greatest threats and opportunities for M&A under a Biden-Harris White House.

Considering the many practical challenges posed by the pandemic, M&A figures have been more robust than many expected. There were US$1.27tn worth of deals in the US in 2020, down 20% from the US$1.59tn recorded a year earlier, according to Mergermarket figures. This was shared between 5,570 deals, down 11% year on year. All things considered, this is a strong performance, spurred largely by a resurgent closing quarter. Indeed, the US$554bn logged in Q4 represented a record quarterly high. This momentum may have staying power. Most corporates (64%) and PE firms (60%) surveyed for this research say the Biden-Harris administration will be either conducive or very conducive for their dealmaking plans in the US.

As Jonathan Russo, co-leader of Pillsbury's M&A group, explains, "An overwhelming number of corporate and PE executives expect US M&A dealmaking to continue to grow in the near term, with significant tailwinds from stimulus measures, the low cost of capital and a strong US vaccine rollout combined with proposed infrastructure investments and the need to deploy capital. While some executives may view a higher corporate tax rate with concern, proposals to increase the GILTI and capital gains tax rates may further accelerate US M&A deals in the short term."

> "Executives expect US M&A dealmaking to continue to grow in the near term, with significant tailwinds from stimulus measures, the low cost of capital and a strong US vaccine rollout."
>
> Jonathan Russo, Pillsbury

The stimulus measures that have been enacted to date have been positively received for helping to support the public as well as the economy. A greater emphasis on infrastructure spending is also seen as a positive, with almost all respondents (94%) saying their dealmaking appetite will increase or increase significantly if funding for public infrastructure projects increases, as is expected.

A central theme in this planned infrastructure investment drive will be energy efficiency and sustainability, with the latter anticipated to be a core element of the administration's agenda. This is likely to result in higher compliance and operational costs. With that in mind, three-quarters (75%) of corporates we surveyed say it would be either difficult or very difficult for their organization to respond to stricter standards. PE is more optimistic about rising to this particular challenge, with 61% saying they are either neutral or think meeting this change will be simple. The Securities and Exchange Commission (SEC) has already made clear its intention to update mandated ESG investor disclosure, so companies should be prepared for this eventuality.

Another closely watched item will be the headline corporate tax rate. Currently set at 21% following the sweeping tax reforms of the previous administration, President Biden has indicated that this will jump, perhaps to as high as 28%. Most of the respondents we spoke to believe it is either likely or highly likely that President Biden will be able to raise the corporate rate, and more than half say this tax hike would decrease their M&A appetite significantly.

With this in mind, it may be that M&A activity slows somewhat once the effects of the recent historic stimulus have tapered off, interest rates begin to rise again, and companies potentially contend with a more highly-regulated and -taxed environment. Until then, US M&A should be expected to continue its strong growth. Amid cheap financing and a sense of opportunism following a strong US vaccine rollout, bold companies and sponsors are turning the pandemic and its aftereffects to their advantage, remodeling themselves and their portfolios to stay ahead of the competition.

Section 1:
M&A in the Current Environment

Following a year that no one will forget, M&A market sentiment appears to be improving among US investors. Over the next 12 months, 59% of corporates expect to undertake between 1-3 M&A deals, and 25% anticipate completing four or more, whereas just 7% report they had undertaken that many deals in 2020. This implies that corporates are very much growing in confidence.

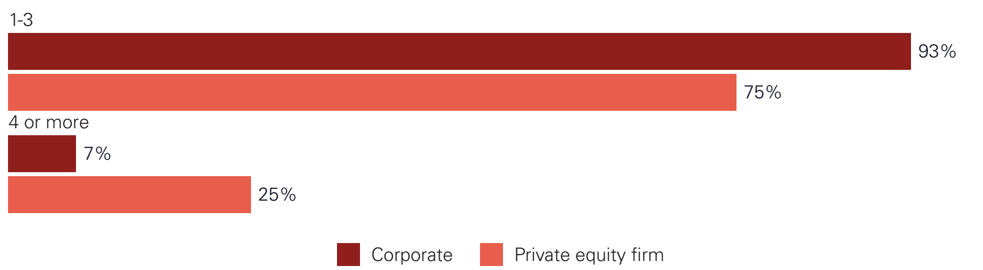
Those on the PE side are even more bullish. While one-quarter of those respondents say they undertook four or more deals in 2020, 56% expect to meet or exceed that threshold in the next 12 months. Overall, these figures point towards an increase in deal volume in 2021.

The proportions of domestic versus international deals in 2020 were roughly equal for both respondent groups: 84% domestic versus 16% international for corporates, and 86% versus 14% for PE. Over the next 12 months, both groups again expect most of their deals to be domestic in nature, though in each case the share of international transactions is also expected to rise from the year before.

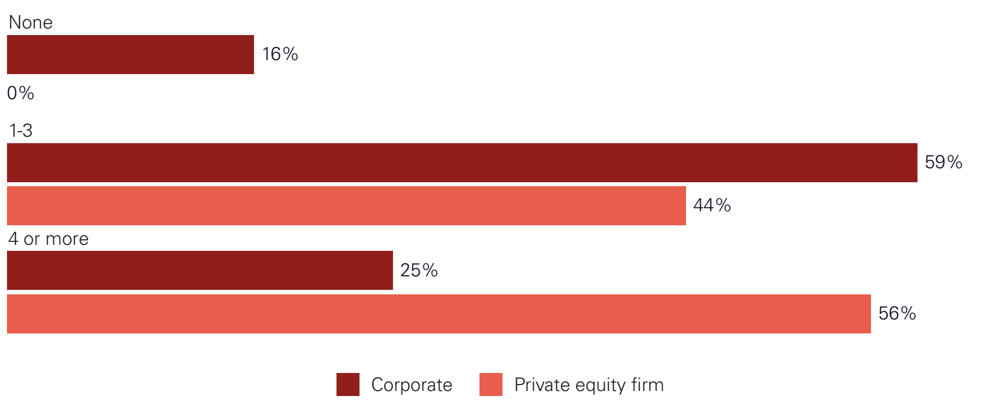
PE firms say roughly four-fifths (83%) of their deals will take place in the US. Corporates have a more cross-border attitude, with these respondents reporting that one-third of their deals will be international.

Outside of their primary territory of North America, the regions in which the largest shares of corporate and PE respondents expect to transact are Europe (identified by 42%

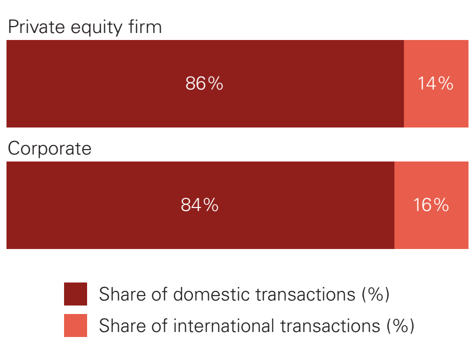
How many M&A deals did you undertake in 2020? (Select one)



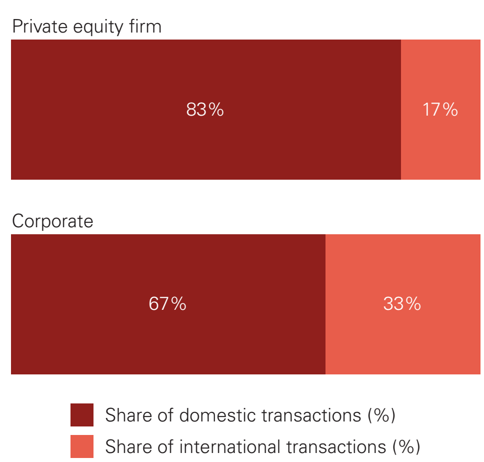
How many M&A deals do you expect to undertake over the next 12 months? (Select one)



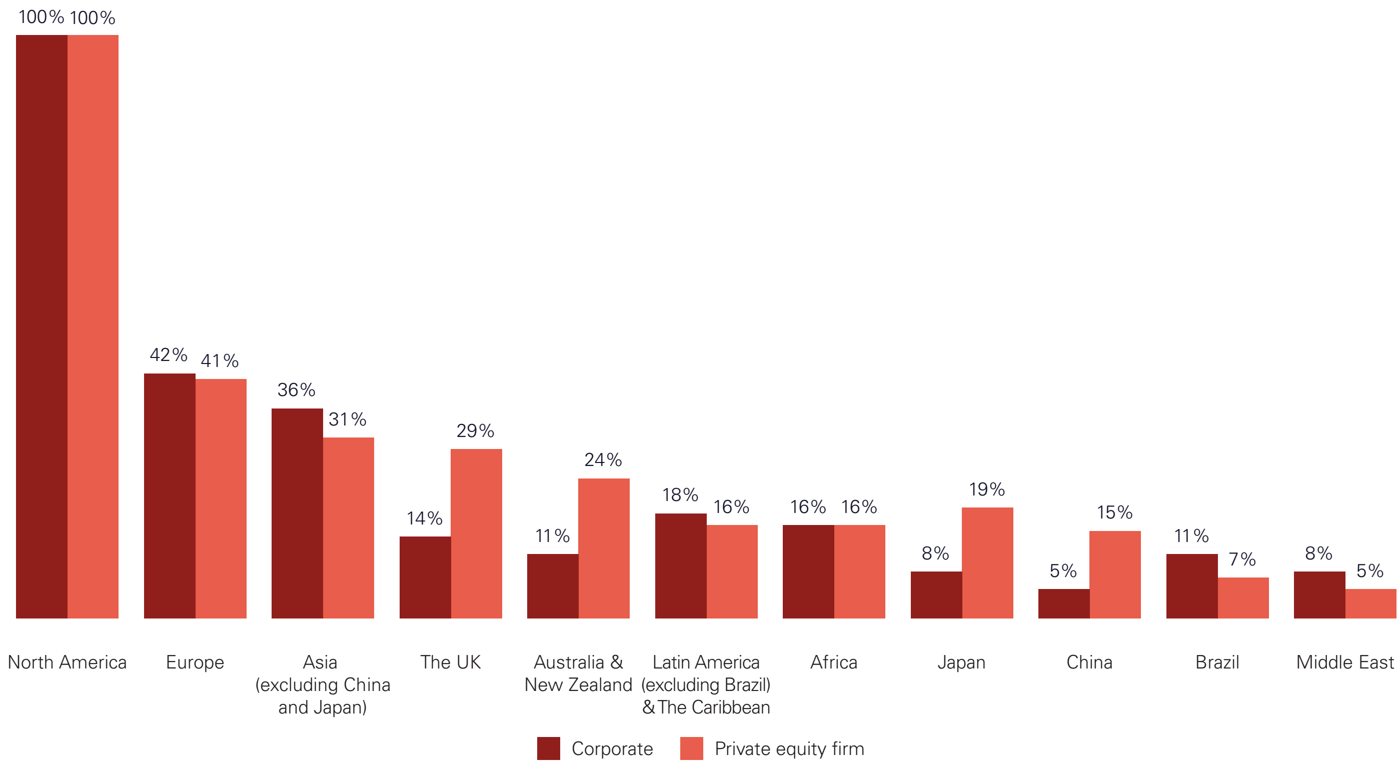
Approximately what proportion of those deals were domestic (i.e. primarily involving another US-based company) versus international (i.e. primarily involving both a non-US-based company and a US-based company, or multiple non-US-based companies)?



Approximately what proportion of those forecasted deals will be domestic versus international?



In which of the following regions do you expect to execute deals? (Select all that apply)



56%

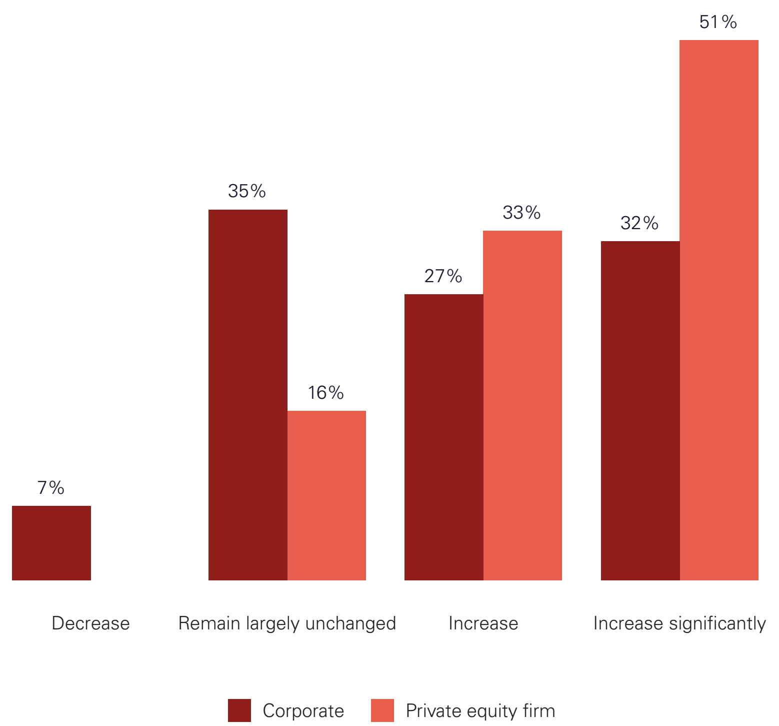
Share of PE respondents who expect to undertake at least four M&A deals over the next 12 months

of corporates and 41% of PE firms) and Asia (36% and 31%, respectively). A large share of PE respondents (29%) also identify the UK as a key market, though less than half that proportion of corporates (14%) share this view.

Clearly Brexit is a key risk for UK businesses, as exports to the European Union have become more complicated and costly, with relevant input costs also rising for businesses sourcing supplies from continental Europe. However, PE has the potential to turn this to its advantage by acquiring businesses and improving their profitability, or by assisting in restructuring their operations, including by establishing a presence on the continent to mitigate trade restrictions.

Most respondents anticipate capital resources for deals to increase in the short term, with greater expectations among financial sponsors. Indeed, 84% of PE respondents, compared with 59% of corporate respondents, expect capital resources allocated to M&A in the US to increase or increase significantly over the next 12 months. The largest single share of corporate respondents (35%) expect capital resources to remain largely unchanged.

How will capital resources allocated to M&A in the US rise or fall over the next 12 months? (Select one)



"We are going to see continued growth in areas like video conferencing, streaming and e-commerce, as well as in a number of essential technologies, including cybersecurity and software-as-a-service platforms. This reliance on tech translates directly to M&A interest."

Allison Leopold Tilley, Pillsbury

Broadly speaking, an economic recovery should result in higher profits for corporates and, all else being equal, this should equip them with more cash for acquisitions. Moreover, the improving macroeconomic outlook, combined with depressed interest rates, is good news for all dealmakers seeking debt financing.

Of course, these "all else being equal" conditions are not guaranteed. The possible introduction in the near term of a higher corporate tax rate is a major consideration under the new Biden-Harris administration and will undoubtedly impact dealmakers' M&A appetite.

On the PE side, fundraising held up well in 2020 despite the complications of managing investor relations at a distance under stay-at-home guidelines. Preqin estimates that US$299bn was raised for buyout strategies alone and US$989bn across private capital strategies, the third-highest total in history.

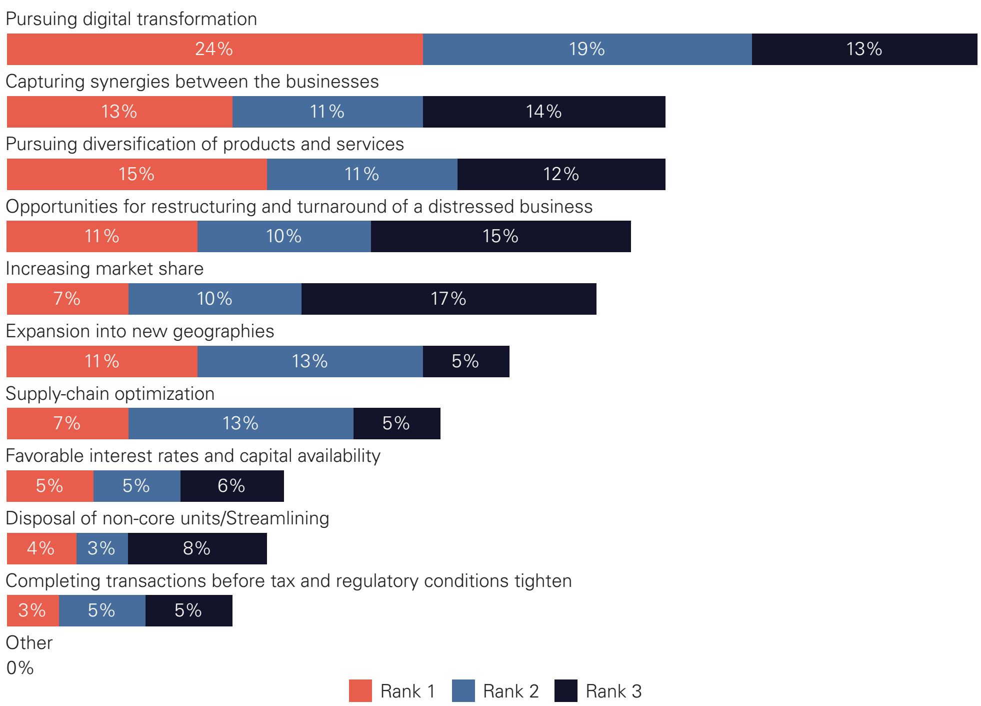
Most of this is earmarked for the US market. It is expected that fundraising will continue to follow this trend in 2021, stoked by the absence of yield in safer asset classes, pushing investors towards public equities and into alternative assets such as PE.

Drivers and Risks

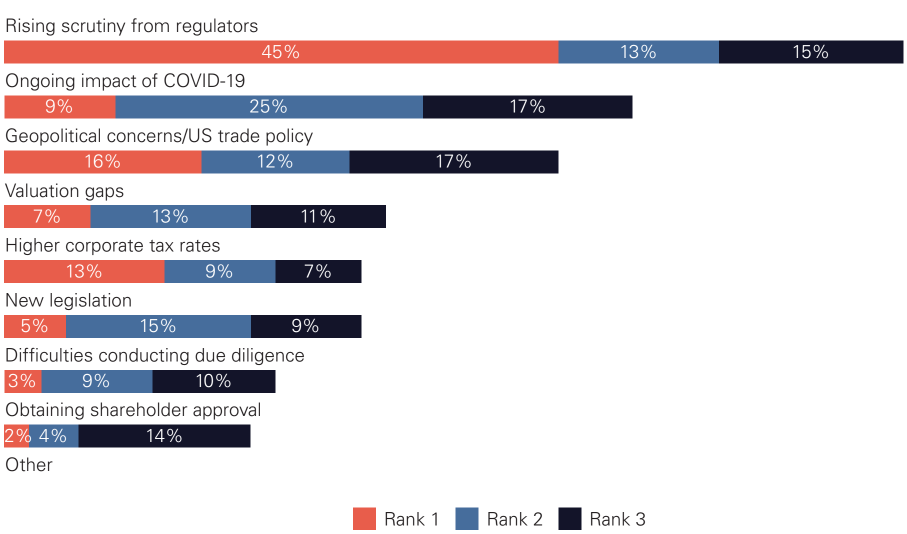
Digitalization was already rising up the corporate agenda, but the pandemic has placed it firmly at the top for most businesses. Those dependent on analog functions were at a huge disadvantage in 2020, and still are today. Recognizing this, companies have put their foot on the gas in their efforts to digitalize operations and remodel their online strategies to meet consumer trends.

A recent study from consultants McKinsey found that, since the onset of the pandemic, the share of digital or digitally-enabled products in companies' portfolios was accelerated

What will be the key drivers of your M&A activity over the next 12 months?
(Select top three and rank 1-2-3 by order of significance, where 1=most significant)



What will be the biggest risks for or potential impediments to your dealmaking over the next 12 months?
(Select top three and rank 1-2-3 by order of significance, where 1=most significant)



by seven years. Furthermore, companies had accelerated the digitalization programs for their customer and supply-chain interactions, as well as their internal operations, by three to four years in just a few months.

As Pillsbury partner Allison Leopold Tilley, who is based in Silicon Valley, puts it, "Work-from-home rules accelerated digital transformation in order to adjust to the pandemic and now it is, in many respects, here to stay. So not only are we going to see continued growth in areas like video conferencing, streaming services, and e-commerce solutions, but also in a number of technologies that have proven to be absolutely essential. This would include subsectors like cybersecurity and software-as-a-service platforms. We're also seeing another boom in the semiconductors space, driven largely by the Internet of Things. This reliance on tech translates directly to M&A interest, and so investment opportunities in TMT are going to continue to be in high demand."

Digital is at the heart of business change, including M&A, a point that is supported by our research. The key driver of M&A activity over the next 12 months that respondents cite is pursuing digital transformation: 24% (the largest such share) of people surveyed identify this as the most significant driver, and a further 19% cite it as their number two concern.

"The cross-sector deals that we'll pursue will be aimed at acquiring technology companies," says the senior vice president of a corporate respondent. "As new laws and policy changes come about, we need to build our capabilities in research and analysis. Solutions have to be future-ready."

After pursuing digital transformation, the next most important M&A drivers for respondents are pursuing diversification of products and services (15% of first-place votes) and capturing operational synergies (13% of first-place votes).

> "Rising scrutiny will be the biggest impediment to dealmaking. As the use of technology has increased in transactions, regulators want more control over the transfer and sharing of information."
>
> Managing Director, Private Equity Survey Respondent

From a risk perspective, respondents believe rising regulatory scrutiny is by far the most significant threat to their dealmaking plans over the next 12 months, with 45% identifying it as their primary concern. This view is aligned with the expectation that the Biden-Harris administration will propose stricter business regulation, although exactly what shape this will take is not yet clear. Technology is also being employed to increasing degrees in transaction processes, which is prompting greater demands on access to deal parties' data. "I expect rising scrutiny to be the biggest impediment to dealmaking. Since the use of technology has increased in transactions, regulators want more control over the transfer and sharing of information," says the managing director of a PE respondent.

Moreover, digitalization as a deal driver on the one hand and regulatory and geopolitical risk on the other are not entirely unrelated. Under the previous administration, the powers of the Committee on Foreign Investment in the United States (CFIUS) were expanded to vet and block deals into sensitive technologies. While this is a concern for overseas investors transacting in the US from a CFIUS perspective, there may be scope for greater tech protectionism under the Biden-Harris administration by other means. For instance, President Biden has vowed to take further aggressive trade enforcement actions against China. In this survey, geopolitical concerns/US trade policy are the primary risk factor for 16% of respondents.

According to Nancy Fischer, who leads Pillsbury's public practices and public policy teams, "We expect CFIUS will return to its more traditional role and will closely collaborate with foreign allies in developing foreign investment policy. That said, we also expect continued scrutiny of transactions involving certain sectors—such as semiconductors, autonomous vehicles, emerging technologies, energy, and infrastructure, among others—companies with access to sensitive personal data, and countries of concern, largely China and Russia. To that end, we have already seen a significant uptick in CFIUS inquiries in connection with 'non-notified' transactions, and CFIUS continues to assert its expanded jurisdiction over certain types of investments. We expect CFIUS to target its focus on transactions of concern which may not necessarily be readily apparent to the transaction parties, thus requiring a well-reasoned and thoughtful CFIUS risk assessment in advance of a transaction in order to determine how best to navigate the CFIUS process."

Beyond these factors, one is left to address the elephant in the room: tax. Perhaps surprisingly, only 13% of respondents view higher corporate tax rates as the top risk to their dealmaking over the next 12 months. Under consideration is the proposal to raise the top rate from 21% to 28%, which could have a chilling effect on M&A. There is also the impact that a proposed rise in the capital gains tax (CGT) could have, which may incentivize sellers either to sell their businesses now before a higher CGT takes effect or wait for a more lucrative time to sell, a decision that many founders only make once in a lifetime.

Rather than being unconcerned by tax rises at all, 53%

Share of PE respondents who expect to be involved in at least one transaction involving a SPAC

respondents indicate it is more the case that this is not yet an imminent risk. Companies are still negotiating the challenges posed by the pandemic, and hitting them with tax rises in the immediate future could prove untimely.

"An increase to 28% is highly unlikely, because President Biden will not receive the necessary support. Other than that, he has to think about the negative impact of COVID-19," says the head of strategy of a corporate respondent. "Increasing the taxes right now is not feasible for businesses to continue operations productively."

SPACs and Minority Investing

Investors were calling 2020 "the year of the SPAC," but 2021 has already eclipsed its predecessor. Special purpose acquisition companies (SPACs), also referred to as "blank-check companies," raise capital in an initial public offering (IPO) and use the cash to merge with a private company and take it public. In less than three months, funds raised by US SPACs totaled US$87.9bn in early 2021, already exceeding the US$83.4bn issuance through all of last year, according to data from SPAC Research.

One of the reasons for SPACs' recent popularity is the ease with which they can be floated. As cash shells, SPACs have brief and simple financial statements and no operations to speak of, nor do they have to make the same level of S-1 disclosures to the SEC as operating companies.

In contrast, traditional IPOs can take companies many months to prepare. They must sound out investment banks, run an IPO roadshow, and negotiate the price of the offering amid a high degree of valuation uncertainty. Blank-check-company listings can often take just a matter of weeks from fundraising to float. They then typically have two years to find a deal target, at which point investors can redeem their cash or participate in the deal. The simplicity of the process, combined with investor appetite for high-growth assets, helps to explain why more than 70% of IPOs in Q1 2021 were accounted for by SPACs.

For PE players, the SPAC phenomenon can be looked at from a number of angles. On the dealmaking side, they pose direct competition for private assets. This may prove to be problematic, given the already huge sum of private capital seeking a home. But SPACs are also a potential exit option. What's more, PE firms themselves are diversifying by establishing their own SPACs, meeting investor demand to deploy capital. Apollo Global Management, TPG Capital LP, CC Capital Management and Neuberger Berman Investment Advisers have all priced their own blank-check companies.

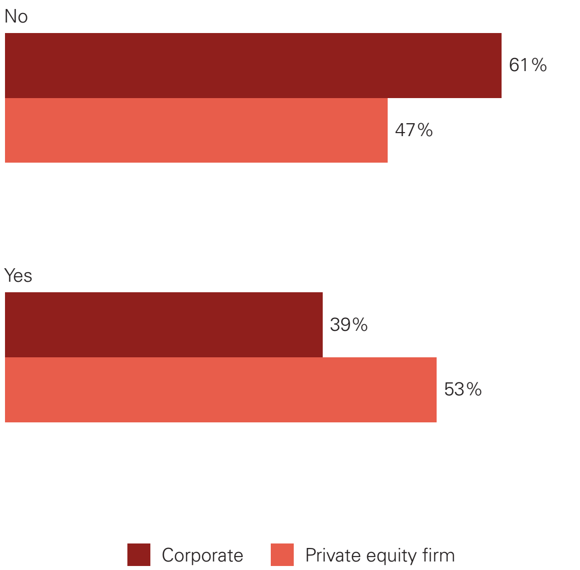
Our research shows that PE has caught the bug. More than half (53%) of PE respondents say they expect to undertake a deal in the US involving a SPAC. This puts these investors notably ahead of strategics in their acceptance of this investment approach: 61% of corporates we surveyed do not expect to be involved in a US deal connected to a SPAC over the next year.

That, though, still leaves close to two-fifths (39%) of corporates who do see themselves participating in such a deal. Though still in the nascent stages, SPACs are beginning to be employed by strategics as M&A vehicles. Liberty Media Acquisition Corp, a SPAC backed by Formula One-owner Liberty Media, broke ground this year when it raised US$500m in its January IPO. Other corporates have since raised their own SPACs, including real estate services firm CBRE, Group Nine Media, and packaged goods group Post Holdings.

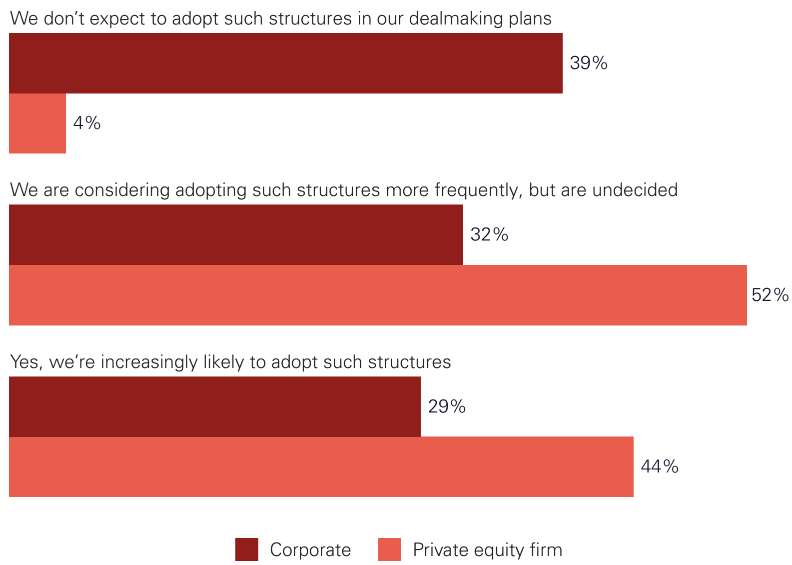
Beginning in December 2020, the SEC and the staff of the Division of Corporate Finance issued guidance and made a series of statements, most recently in April 2021, causing the volume and market value of SPAC transactions to be significantly impacted. In the short term, deal activity may slow as companies assess the impact of the SEC's actions. The longer-term view of the SPAC market is difficult to predict.

As Davina K. Kaile, a corporate partner in Pillsbury's Silicon Valley office, explains, "It remains to be seen what the future holds for

Do you expect to be involved in at least one M&A transaction in the US involving a special purpose acquisition company (SPAC) over the next 12 months?



Over the next 12 months, are you more likely to consider entering into long-term commercial agreements, joint ventures or minority investments in your dealmaking plans than you were previously? (Select one)



SPACs. It is true that the pace of SPAC activity on both the IPO and de-SPAC side of things has slowed as the market adjusts to increased regulatory scrutiny—the SEC's recent staff statement regarding the accounting treatment for warrants, for example—as well as increased market volatility and a fairly saturated SPAC PIPE market. However, this should be viewed in the context of the extraordinarily high levels of SPAC deal volume prior to the slowdown."

There are, as well, other deal approaches for investors to choose from. Minority investing, for instance, has become increasingly popular among PE houses. Equipped with historic levels of uninvested capital, PE funds have sought to get creative with their deal structures and—provided they can exercise certain powers, such as exit control rights and debt incurrence vetoes—minority deals have offered a solution to the superabundance of dry powder.

When asked about their likelihood of incorporating long-term commercial agreements, joint ventures or minority investments in their dealmaking plans, 52% of the PE respondents surveyed are considering adopting such structures (versus 32% of corporate respondents), and 44% say they are firmly in the affirmative and are increasingly likely to adopt them (versus 29% of corporates).

This demonstrates the willingness and readiness of PE firms to adapt to market conditions, with strategics more usually sticking with what they are familiar. Indeed, 39% of corporate respondents (the largest share for that respondent type) say outright that they don't expect to adopt such novel deal structures.

Section 2 :

M&A Outlook Under President Biden

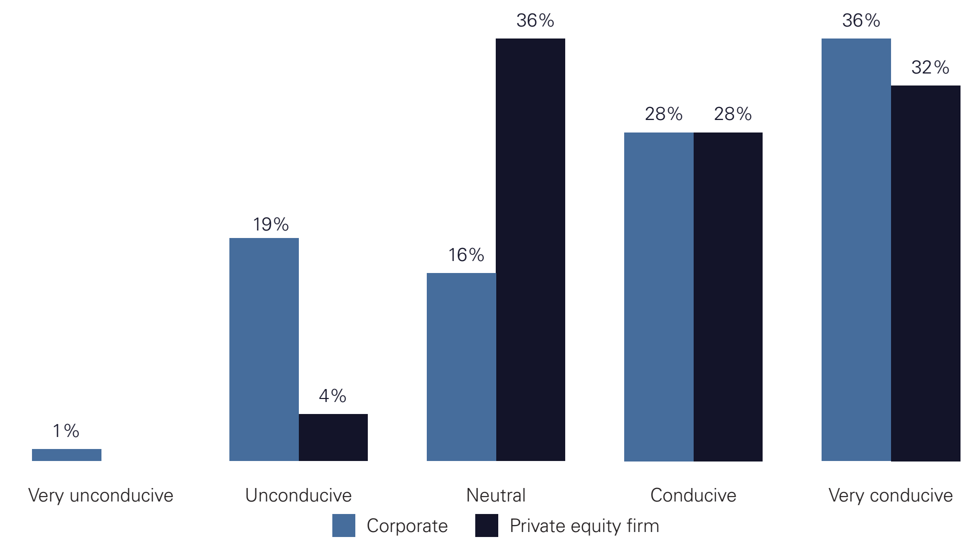
On balance, our survey respondents see the Biden-Harris administration as a win for their dealmaking activities. On the surface, this may seem contradictory in light of the previous administration's light-touch regulation and low tax policies. However, recent years have also been marked by unrest. In comparison to its immediate predecessor, the new administration is largely viewed as more predictable, and investors prefer predictably. This is reflected in our research, which shows that most corporates (64%) and PE firms (60%) believe the administration will be either conducive or very conducive for their dealmaking in the US.

"Under Biden, global and US dealmaking will be somewhat more favorable. During the previous administration, there were tax cuts for businesses, but without business stability, companies could not capitalize," says the head of strategy and corporate development of a corporate respondent.

There is also a common view that this greater political certainty will extend to foreign investment. "Appointments at the Foreign Investment Division will make a difference," says the managing director of a PE respondent. "There have been major risks for foreign investors involved in dealmaking in the US. The uncertain political situation has changed now under Biden."

In respect of specific scenarios unfolding under the Biden-Harris administration, 96% of all respondents say their appetite for M&A will increase or

On balance, how conducive do you believe President Biden's administration—considering potential appointments at the DoJ, FTC, FCC, SEC, CFIUS and other agencies—will be for your dealmaking in the US? (Select one)



increase significantly in correlation with the pandemic stimulus package being deployed. This has been the first major win for this White House. In March 2021, President Biden's US$1.9tn relief bill cleared its final hurdle in Congress.

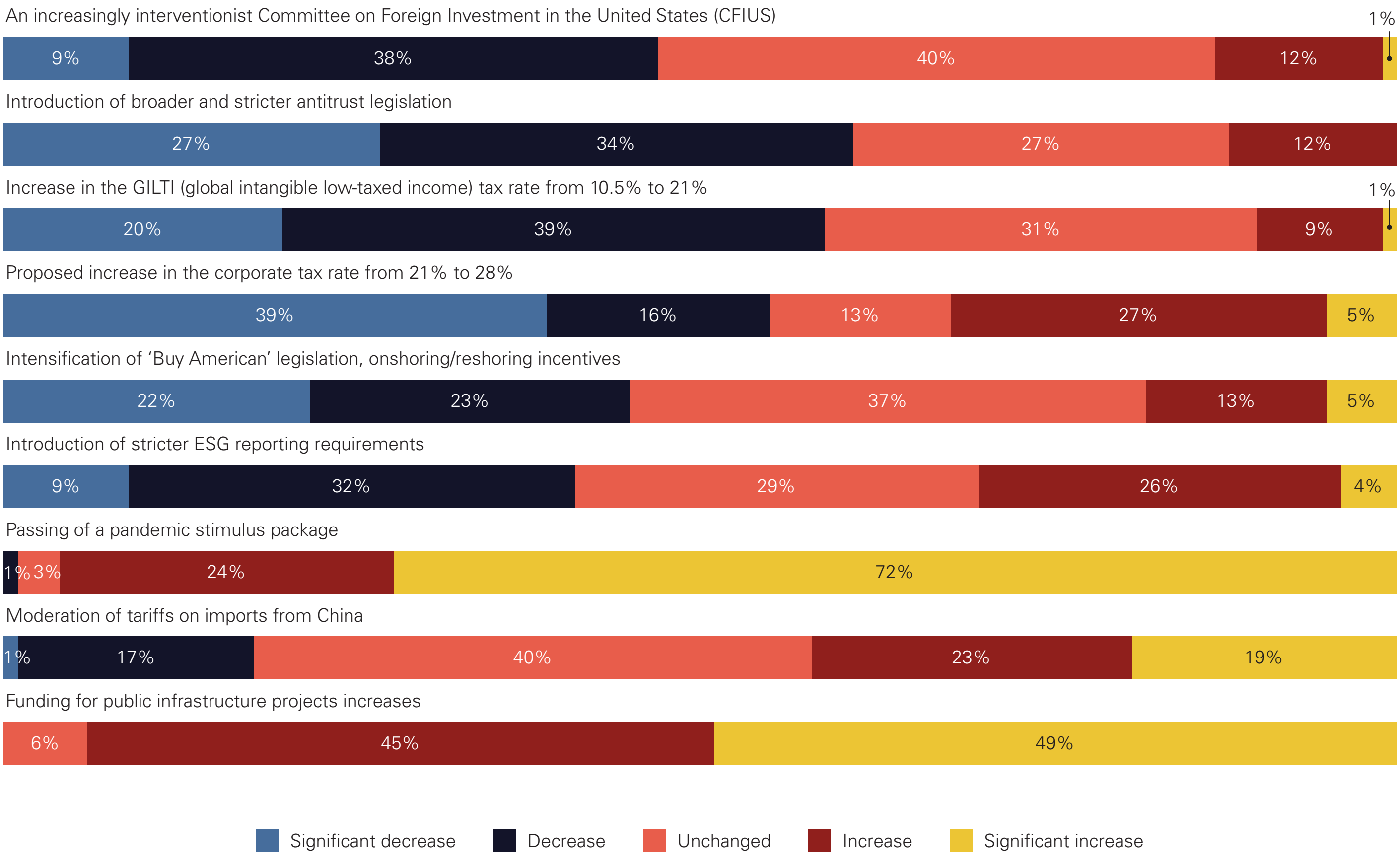
The bill included one-off direct payments worth US$1,400 for most Americans, as well as an extension to weekly jobless benefit payments of US$300 until September. In addition to helping everyday Americans cope with the effects of the pandemic, the move will help to stimulate the economy and capital markets.

Also stimulating appetite for deals will be the government's infrastructure spending plan. The proposal is to invest up to

>60%

Share of all respondents who believe it is either likely or highly likely that President Biden will be able to raise the rate of corporate tax in the US

What would be the impact on your organization's appetite for dealmaking if, under the Biden administration, each of the following scenarios unfolded? (Select one answer per scenario)



> "There is emphasis on reducing Big Tech companies' market share. They are the only ones flourishing, even under the rough market conditions, and regulators have noticed."

Managing Director, Private Equity Survey Respondent

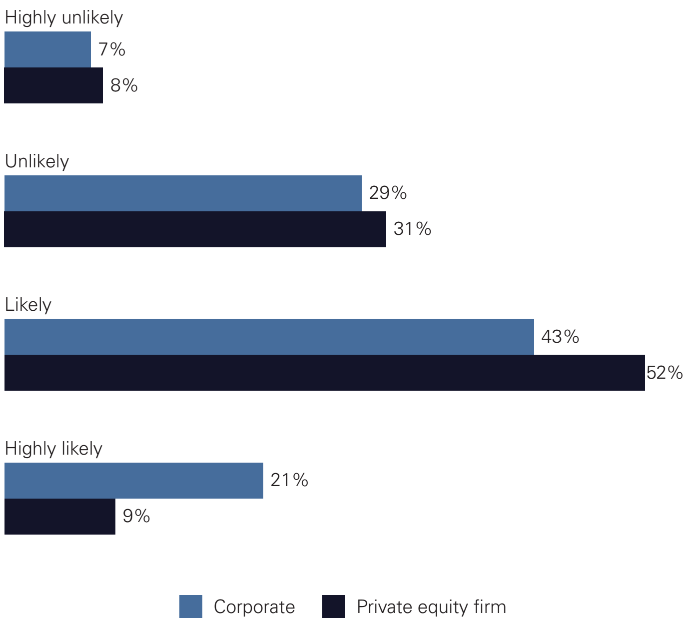
US$2tn in much-needed hard infrastructure projects, such as roads and bridges, as well as high-speed broadband networks and charging networks for electric vehicles, along with tax incentives and point-of-sale rebates for consumers purchasing American-made electric vehicles.

It is expected that the plan, if approved in its current scope, would help create millions of jobs and galvanize the post-pandemic economic recovery. This is also likely to have a knock-on effect on M&A sentiment. The incredible majority of respondents (94%) say their dealmaking appetite will increase or increase significantly if funding for public infrastructure projects grows.

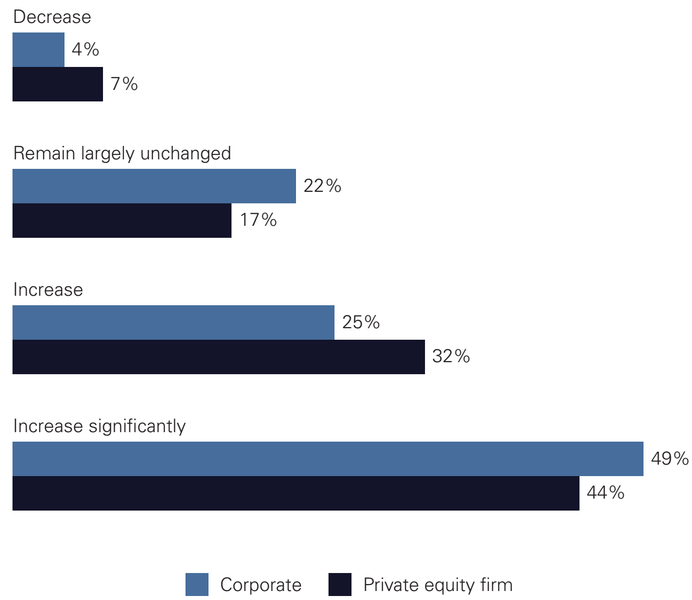
Tax Attacks

Of course, the funding for these historic stimulus and infrastructure programs has to come from somewhere. Governments cannot just create public debt without some plan to pay it down, and on this point President Biden has

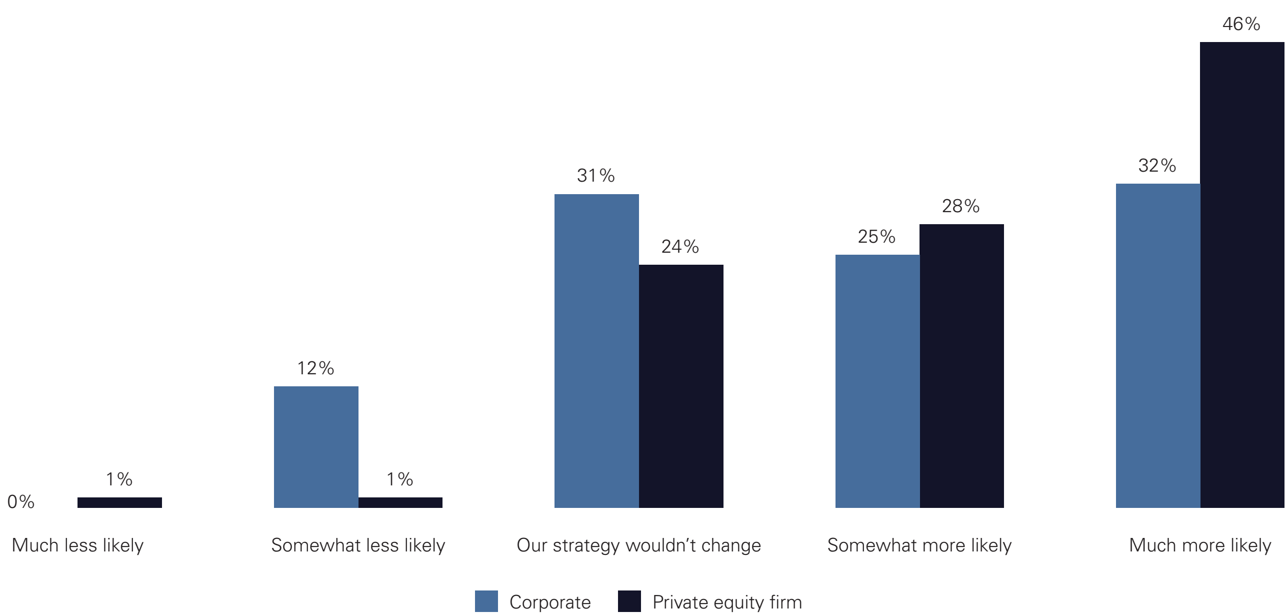
How likely do you think it will be that President Biden is able to raise the corporate tax rate? (Select one)



How do you expect the degree of antitrust scrutiny towards 'Big Tech' companies and technology M&A in general to change over the next 12 months? (Select one)



If federal policies designed to increase onshoring of business operations were enacted, how much more likely would you be to acquire or build more domestic production? (Select one)



> “The administration wants to reduce offshoring, which will create sudden changes, and the capital requirements of companies will increase.”
>
> Director of Corporate Strategy, Corporate Survey Respondent

made his intentions clear—this spending will be paid for by rolling back elements of the 2017 tax cuts made under the previous administration.

The biggest of these is the proposed hiking of the corporate tax rate from the current 21% to 28%. If successful, this is likely to have a damping effect on M&A, with 39% of respondents saying their appetite for deals would decrease significantly.

The individuals we surveyed mostly agree that this tax hike will come to fruition. Our research shows that 64% of corporates and 61% of PE respondents think it is either likely or highly likely that President Biden will be able to raise the corporate tax rate.

A more pertinent question may be, when will the corporate tax rate rise and by how much? The administration will have to balance funding its investment plans with supporting the economic rebound, since introducing taxes too early may stifle investment and growth at a time when companies most need both.

“There are contrasting opinions in the market regarding the corporate tax rate. However, most believe the increase is inevitable to provide funds for other planned government projects,” says the senior strategy director of a corporate respondent.

Following corporate tax as a damper on M&A appetite is a potential increase in antitrust regulations. The Federal Trade Commission (FTC) had a record year for merger enforcements in 2020 under the previous administration; however, this followed several quieter years for enforcement from the Department of Justice (DoJ). Both the DoJ and FTC are already on high alert for antitrust violations in the context of the pandemic and economic disruption, which have been highlighted as potential catalysts for collusion between businesses.

It is also generally held that antitrust enforcement tightens under Democrat administrations. Therefore, it should be expected that investigation and enforcement activity will increase over the coming years. Almost two-thirds (61%) of respondents say the introduction of broader and stricter antitrust regulation would decrease their M&A appetite, with 27% saying it would significantly decrease their appetite.

Not all companies would be equally affected by a more hawkish approach. Big Tech is firmly in the new administration’s sights, and this is a welcome development for many companies whose business models are being undermined by technology giants that many perceive as holding oligopolistic control of various markets. Last year, a Congressional committee heard evidence from the leaders of Apple, Amazon, Facebook, and Google in defense of claims they quash competition.

The outperformance of large technology companies during the pandemic has only served to drive home these concerns. "There has been a lot of emphasis on reducing the market share of Big Tech companies. They are the only ones flourishing, even under the rough market conditions, and it has been noticed by regulators," says the managing director of a PE respondent.

Unsurprisingly, our research shows that 76% of PE firms and 74% of corporate respondents expect the degree of antitrust scrutiny towards Big Tech companies and technology M&A in general either to increase or increase significantly over the next 12 months.

Buy American

One of President Biden's first items of business was to sign a "Made in America" executive order. The order focuses on the approximately US$600bn in federal government contracting in the private sector and aims to channel this to companies that manufacture in the US and with US components.

There were already rules in place that governed how taxpayer dollars are spent, but the latest steps seek to close loopholes and remove waivers that have seen companies import foreign goods and make small changes to them in order to qualify for domestic preferences. The executive order has also created a new senior role at the Office of Management and Budget in charge of the government's Made in America policy and to oversee the implementation of these efforts.

This is aimed at reshoring production to create more domestic growth and jobs for American workers. "The dealmaking challenges will increase in the US. The administration wants to reduce offshoring," says the director of corporate strategy of a corporate respondent. "This will create sudden changes, and the capital requirements of companies will increase."

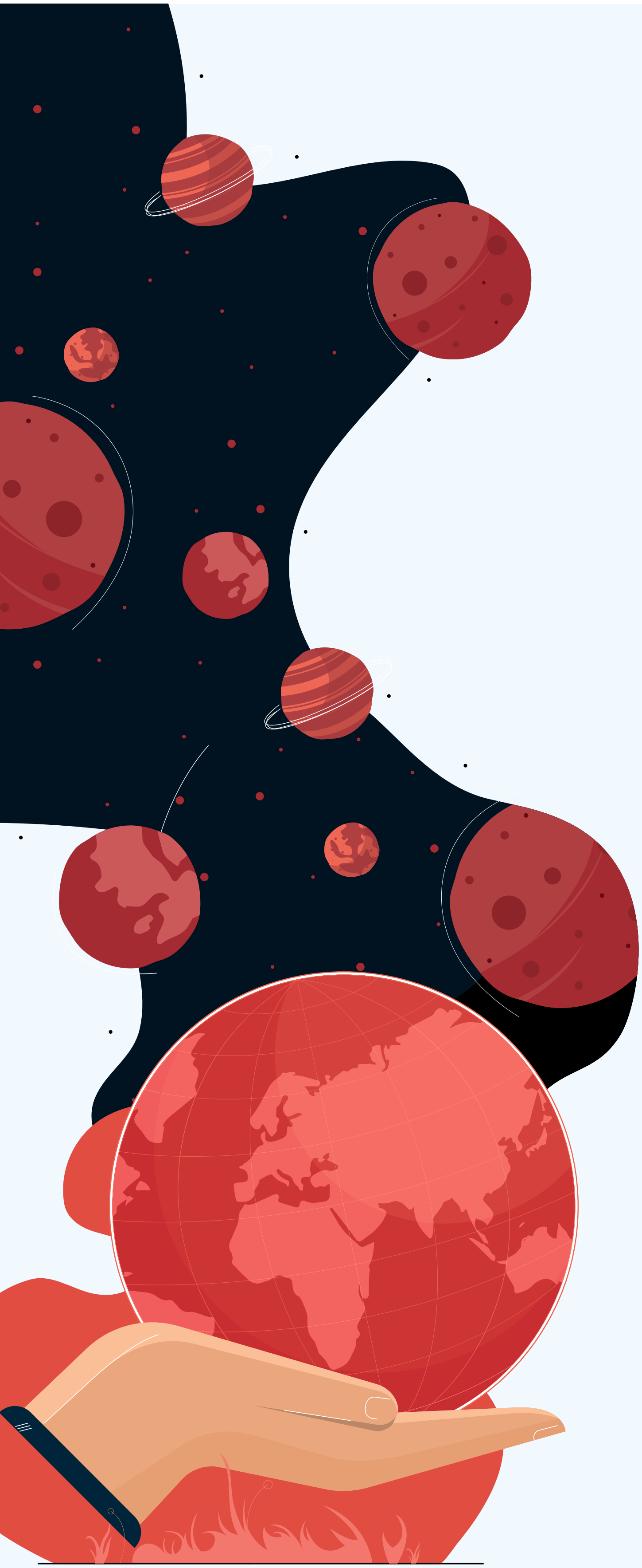
In respect of the possible impact of "Buy American" legislation, 45% of our survey respondents anticipate this weakening their appetite for deals, 22% significantly so. That does, however, leave a sizable 37% who take a neutral view, which may reflect the fact that the rule changes specifically relate to federal contracting and will therefore have a limited scope.

The key proposal to address offshoring is to increase the global intangible low-taxed income (GILTI) tax rate, which currently sits at 10.5% for US corporations, well below the regular US corporate tax rate. President Biden's proposal is to raise the rate on GILTI to 21%, thereby doubling the tax burden on offshore operations of US-corporate parented businesses.

If these measures are passed, they are likely to have a major impact on offshoring, particularly for companies owned by PE firms. In our survey, 57% of corporates and 74% of PE respondents say they would be either somewhat or much more likely to acquire or build more domestic production if the Biden-Harris administration enacted federal policies designed to increase onshoring.

74%

Share of corporate respondents who expect the degree of antitrust scrutiny towards tech M&A either to increase or increase significantly over the next 12 months



Going Green

The US is the second-biggest emitter of greenhouse gases after China. The Biden administration is very much "talking the talk" on climate change. In April during a virtual summit with 40 world leaders, President Biden pledged to reduce America's greenhouse emissions by over 50% by 2030 (relative to 2005 levels). Central to America's climate plan is cutting greenhouse emissions from the power sector to net zero by 2035 and ensuring the country achieves a 100% clean-energy economy and net-zero emissions no later than 2050.

One of the first steps towards achieving these goals is the development and implementation of a mandatory ESG disclosure framework. Acting SEC Chair Allison Lee said in March that these steps were already being taken and announced the opening of a consultation period regarding climate change disclosures to help the government to draw up future guidance.

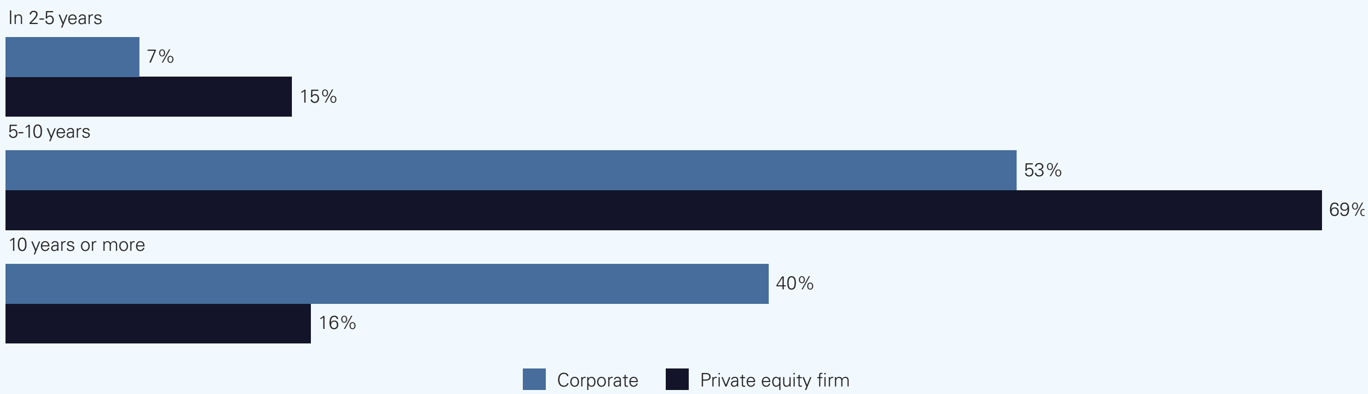
As Stephen Amdur, leader of Pillsbury's PE team, explains, "ESG is part of an evolving landscape of metrics to assess the long-term success of a corporation. As companies and investors increasingly tie growth and investment strategies to ESG metrics, dealmakers will need to focus on new criteria as they assess potential opportunities. We expect the M&A economy to increasingly establish benchmarks for ESG performance and develop methodologies for monitoring progress over time. While there will certainly be M&A activity targeting companies with high ESG scores, we expect also to see significant M&A activity involving companies that are underperforming in these areas as dealmakers seek to create value through operational improvement and sustainability measures."

Cognizant of this overall momentum, 53% of corporates and 69% of PE respondents believe a functional and standardized ESG reporting system will be installed in the US within 5-10 years' time, though 40% of corporates suggest it will take at least 10 years to implement.

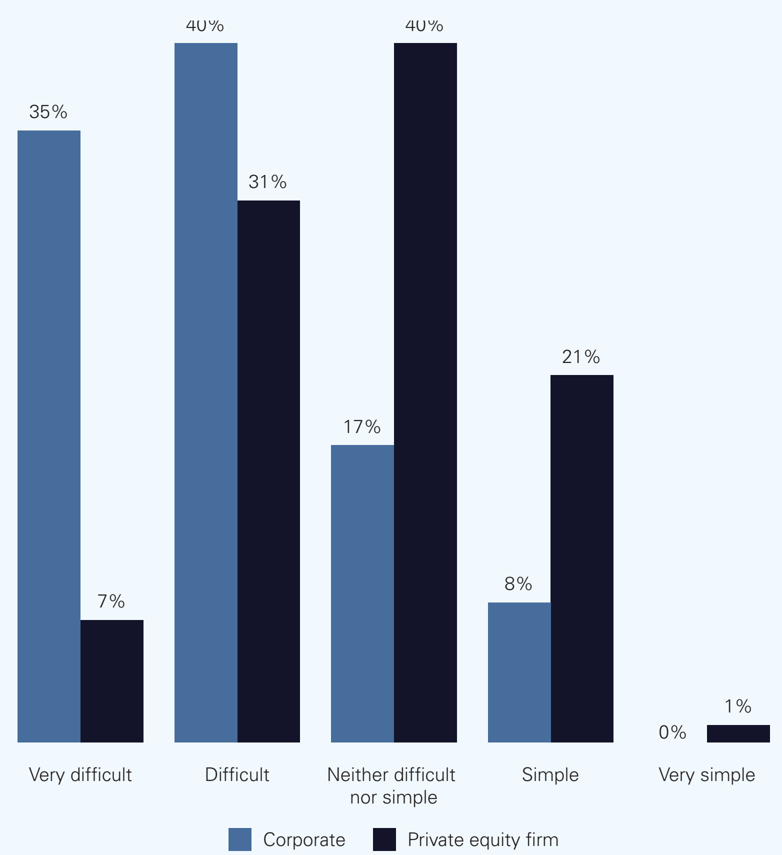
Corporates are generally more pessimistic about their capacity to meet stricter environmental regulations, with 75% saying it would be either difficult or very difficult for their organization to respond, compared with just 38% of PE respondents who say the same. Further, the largest share of the PE respondent group is neutral (40%), with that group saying it would be neither difficult nor simple, and more than one-fifth (21%) of PE executives surveyed say it would be simple to meet this challenge.

Given its value-creation mandate, which often involves improving governance standards, PE may even stand to benefit from increased ESG regulation by swiftly bringing investee companies up to standard, thus making them more attractive investment prospects once it comes time to profitably exit these businesses.

How long will it be before a functional and standardized ESG reporting system is installed in the US? (Select one)



How difficult would it be for your organization to respond to stricter environmental/sustainability regulations? (Select one)



"As companies and investors increasingly tie growth and investment strategies to ESG metrics, dealmakers will need to focus on new criteria as they assess potential opportunities."

Stephen Amdur, Pillsbury

Conclusion

Overall, the prognosis for US M&A in 2021 is quite positive. The dust has settled on the election and the new administration has already started its work by passing its stimulus bill, fending off short-term risks. The US also has the highest inoculation rate among the world's largest countries, which points to a swifter return than in other parts of the world to something resembling normality and pre-pandemic economic activity. Combined with a currently ascendant stock market and benign financing conditions, the newfound sense of political calm should set the stage for high levels of M&A.

That, at least, is the short-term outlook. Over the longer term, there are risks that may become more prominent as the recovery progresses. At some point, the Biden-Harris administration should be expected to try and pass tax hikes, a move that will be common the world over.

The intended rise of the top corporate tax rate from 21% to 28% may be softened to an increase of 2%-3%. This compromise was reportedly discussed at a White House meeting in mid-April as a means of gaining bipartisan support. A proposed increase in the CGT rate from 20% to 39.6% for top-bracket earners also has big implications for M&A, namely the net proceeds that sellers will receive. This may incentivize lifelong company founders either to accelerate or delay sales to PE firms and corporates or to seek tax-deferred deal structures.

More likely, however, is that additional tax liabilities will affect deal valuations. Regarding CGT, vendors may seek a higher earnings multiple to cover the additional money lost to the increased rate. With regard to corporate tax, companies are typically valued at a multiple of EBITDA. However, with a loan interest deductibility cap in place since 2017, this rate hike could significantly impact net income, especially for highly levered companies, and therefore may influence investors' price and risk calculations when weighing up new deals.

For now, the sharp rebound in deal activity that began in H2 2020 maintains serious momentum. Corporates and PE firms spent much of last year in triage mode and now have the will, the capital and the debt financing to transact. Assuming no major setbacks along the way, the first 12 months of the Biden-Harris administration are shaping up to be a promising year for US dealmakers.

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