

Market Intelligence

PRIVATE EQUITY 2020

Global interview panel led by Simpson Thacher & Bartlett

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3.35

4.25%

375.69

278

58

6.35

5.35%

248.36

8.56

458

1321

8.35%

898.33

354

71

1.20%

282.80

21

2453

9.33%

255.36

21

825

6.35%

375.69

814

4.25%

248.36

Global Trends

Atif Azher is a partner in Simpson Thacher's corporate department and is based in the firm's Palo Alto office. His practice focuses on M&A where he represents private equity firms and public and private companies in a variety of domestic and cross-border transactions. Atif has experience across an array of corporate matters, including acquisitions, dispositions, carve-outs, leveraged buyouts, venture financings, strategic investments, joint ventures and other direct investments.

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During the first half of 2020, global M&A deal volume and value measured in dollars experienced a significant reduction from 2019 levels, with less cross-border M&A activity in large part due to the direct and indirect business impacts of, and market uncertainty stemming from, the covid-19 pandemic. Deal value in the United States over the first half of 2020 decreased 72.4 per cent year-over-year by value to US\$274.5 billion, compared to US\$996 billion for the first half of 2019, according to Mergermarket. Much of the overall drop in deal value can be attributed to a collapse in 'mega-deals' valued at over US\$10 billion. For example, according to data supplied by Bloomberg, there were only 10 mega-deals in the United States in the first half of 2020, compared to 19 for the same period in 2019, a 47 per cent decrease in volume. Global deal value reached US\$901.6 billion, representing a 52.7 per cent decrease relative to the first half of 2019, according to Mergermarket. Meanwhile, worldwide deal activity levels trailed about 32 per cent less compared to the first half of 2019, with 6,938 deals announced in the first half of 2020 compared to 10,115 deals during the same period last year (Mergermarket). The Americas, dominated by the United States, experienced dramatic slowdowns relative to 2019 while the rest of the world saw their global market share increase. According to Mergermarket, the Americas share of global M&A declined to 33.4 per cent, while Europe saw the largest market share gains of 32.3 per cent, slightly edging out Asia at 27.7 per cent. The first half of 2020 saw a massive decrease in announced transactions of US\$2 billion or greater, with a nearly two-thirds decline in volume quarter-on-quarter in 2020 (54 of such deals in the first quarter of 2020 compared to 18 in the second quarter of 2020), according to Mergermarket. US private equity sponsors closed 392 exits valued at a combined US\$134.8 billion through the first half of 2020 (PitchBook). Globally, private equity exits were down 70 per cent in May 2020 compared to the same period in 2019 (PitchBook). This decrease is, in large part, the result of business impacts and market uncertainty stemming from covid-19, which has contributed to a decrease in portfolio company valuations.

Americas

M&A deal volume in the Americas totalled US\$391.8 billion in the first half of 2020, reflecting a decrease of 68 per cent from the first half of 2019, the lowest M&A activity in the region since 1998 (Bloomberg). According to Bloomberg, the United States continues to drive M&A activity in the Americas, accounting for 87.2 per cent of the region's total. US-based transactions fell 72.4 per cent by value to US\$274.5 billion, compared to US\$996 billion during the same period last year (Mergermarket). During the first half of 2020, there were 2,139 US-based transactions, compared to 3,174 US-based transactions in the first half of 2019 (Mergermarket).

Private investments in public equity (PIPE) deals and 'blank check' special purpose acquisition company transactions (SPACs) gained increased prominence



as investment tools in the first half of 2020. PIPE transactions in the first half of 2020 almost doubled in value compared to the same period in 2019. PrivateRaise recorded 83 PIPE deals in the first half of 2020 that amounted to US\$10.2 billion in total value, compared with 99 such transactions worth a combined US\$5.3 billion in the same period last year. According to PitchBook, during the second quarter of 2020, SPACs had the most active quarter on record.

The technology sector remained popular among financial sponsors, accounting for just under 20 per cent of all private equity deals during the first half of 2020 and representing just over 30 per cent of private equity deal value (PitchBook). US private equity exit volume increased to US\$134.8 billion over 392 deals in the first half of 2020, relative to US\$110.1 billion over 371 deals in the first half of 2019 (PitchBook). Private equity median deal size ticked down for the first time in five years, with the median private equity buyout size in the US reaching US\$135 million during the first half of 2020 (PitchBook).

Notable private equity transactions in the Americas in the first half of 2020 include the US\$22.0 billion merger of Kronos Incorporated and Ultimate Software, backed by Hellman & Friedman, and the US\$14.3 billion take-private of Zayo Group

Holdings, Inc by affiliates of EQT Infrastructure IV fund and Digital Colony Partners, which represents the largest syndicated private equity investment and the second largest leveraged buyout since 2008.

Europe, Middle East and Africa

Driven by political and economic uncertainty, including the covid-19 pandemic, that has discouraged M&A activity in Europe, the Middle East and Africa (EMEA), M&A deal volume in the region decreased in the first half of 2020 to its lowest level since the first quarter of 2010, totalling US\$332.2 billion, a 27 per cent decrease in deal volume from the first half of 2019 (Bloomberg). M&A deal volume in the Middle East and Africa remained strong, primarily as a result of several high-value deals such as the US\$20.3 billion TAQA acquisition of a majority stake in certain assets of ADPower (Mergermarket). According to Bloomberg, the United Kingdom, Germany and France were EMEA's most acquisitive regions, accounting for about 44.4 per cent of its total deal volume with US\$147.4 billion in value. Due to the covid-19 pandemic, European outbound M&A activity levels dropped to US\$42.9 billion in the first half of 2020, a 68.1 per cent decrease from the first half of 2019 and its lowest year-to-date value since 2013 (Mergermarket). EMEA private equity deal flow accounted for US\$127.3 billion in the first half of 2020, a 40.1 per cent decrease from the first half of 2019 and the number of private equity deals in the region decreased by 17.4 per cent over the same period (Bloomberg).

Notable private equity transactions in the first half of 2020 include the US\$5.3 billion acquisition of Masmovil by a consortium of Cinven Partners, KKR and Providence Equity Partners and the US\$2.6 billion sale of Coty's beauty business to KKR (Mergermarket).

Asia-Pacific

Announced M&A deal volume in the Asia-Pacific region (excluding Japan) totalled US\$336.4 billion in the first half of 2020, which represents a 8.4 per cent decrease from comparable deal volume in the first half of 2019 (Bloomberg). Similarly, Japan also experienced a decrease in M&A deal volume, totalling US\$10.7 billion and representing a 17.5 per cent decrease as compared to the first half of 2019 (Mergermarket). Despite the negative economic impacts from the covid-19 pandemic, China and Hong Kong accounted for 54 per cent of M&A deal activity in the Asia-Pacific region (excluding Japan) during the first half of 2020, representing the largest M&A contributors in the region (Mergermarket). In addition, the Asia-Pacific region experienced a wave of take-private acquisitions of China-based, US-listed companies following the Trump administrations' threats to restrict Chinese companies' access to the US capital markets (Mergermarket). Outbound M&A value in the Asia-Pacific region

“In the first half of 2020,
leveraged loans and high yield
bond issuances reached more
than US\$1 trillion globally.”

(excluding Japan) totalled US\$24.8 billion, representing a decrease of 42.7 per cent relative to the first half of 2019 (Mergermarket). Private equity activity in Asia-Pacific in the first half of 2020 was valued at US\$82.7 billion, which represents a less than 1 per cent increase as compared to the first half of 2019, according to Bloomberg. Sequoia Capital was the most active private equity investor and General Atlantic LLC recorded the highest transaction value total in the first half of 2020 in the Asia-Pacific region (Bloomberg). Notable M&A deals include the US\$10.6 billion sale of Tesco Plc's Thailand and Malaysia business to a consortium of companies within CP Group and the US\$8.1 billion acquisition of CapitaLand Commercial Trust by CapitaLand Mall Trust.

Debt financing markets

Overall, the debt financing markets in the United States have remained open, with sponsors finding ready access to debt financing in the first two months of 2020 prior to the covid-19 pandemic. In the first half of 2020, leveraged loans and high yield bond issuances reached more than US\$1 trillion globally, with approximately 44 per cent taking place in the second quarter of 2020 (Mergermarket). Also, as of the

end of the second quarter of 2020, median debt-to-earnings before interest, taxes, depreciation and amortisation multiples for private equity buyout transactions was 5.4x, compared to 5.9x for the same period in 2019 (PitchBook). The leveraged loan market was largely shuttered for business in the second half of March 2020 through May 2020, although the high yield debt market was resurgent during this time. The market seemed to open up near the end of May 2020 with certain select credit being able to syndicate non-fungible deals and continued market improvement throughout July 2020. Committed financing remained rare through July 2020, although there were limited committed financings signed up in June and July 2020.

Slower first half in private equity fundraising

Although global private equity fundraising had a strong first quarter with an approximately 19 per cent increase over the first quarter of 2019 in aggregate capital raised (Preqin), the economic impact of the covid-19 pandemic took effect in March 2020 and disrupted private equity fundraising. In the second quarter of 2020, aggregate capital raised decreased 23 per cent and the number of funds closed also declined 47 per cent, in each case over the second quarter of 2019 (Preqin).

We believe this disruption disproportionately impacted first time funds and funds that had not yet begun fundraising. Nevertheless, large, blue chip sponsors with strong pre-existing limited partner relationships and fundraisings in process at the beginning of 2020 remained successful. This reflects continued consolidation within the private equity fundraising market in favour of such established sponsors with strong track records.

Moreover, the fundraising process slowed over the first half of 2020 with only 39 per cent of the funds closed doing so within 12 months (as compared to 52 per cent in 2019) (Preqin). Although the number of funds in market currently fundraising has increased over the first half of 2020 by approximately 6 per cent (from 3,524 in January 2020 to 3,754 in July 2020), the amount of aggregate capital targeted has decreased approximately 5 per cent (from US\$926 billion in January 2020 to US\$884 billion in July 2020) (Preqin).

Global macroeconomic uncertainty and difficult economic and political conditions in certain regions have continued to shift fundraising dynamics in favour of North America and Europe with 116 North-America-focused vehicles and 45 Europe-focused vehicles closings during the second quarter of 2020, according to Preqin. Additionally, there has been a continued focus in private equity fundraising on strategic relationships and alternative fundraising strategies.

Outlook for second half of 2020

We would expect deal activity in the second half of 2020 to continue the downward trend and roughly mirror overall activity levels in the first half of the year, with a significantly reduced volume (measured in numbers) and reduced value of deals (measured in US dollars) compared to recent years, with the potential for more stabilised activity depending on how the covid-19 pandemic progresses. Until the world finds a way to meaningfully manage the risks stemming from covid-19, we will likely see significant softness in M&A activity.

We expect that the trends and developments witnessed in the first half of 2020, with respect to fundraising, will continue as the consolidation and the 'flight to quality' in the private equity industry continues in response to covid-19. We believe competition for investor capital among private equity funds will continue to increase, with alternative fundraising strategies and strategic relationships continuing to play a substantial role. Likewise, we believe that allocation decisions by risk-averse limited partners will continue to favour larger, established sponsors with strong track records and the ability to absorb incremental burdens associated with today's market environment, as well as the continued scrutiny and enhanced regulation of the private equity industry. In addition, we believe that private equity funds will encounter valuation issues as uncertainty and volatility within the markets remains.

Finally, a decline in public market values could result in an imbalance in investors' portfolios, causing such investors to sell their private fund stakes to maintain certain asset allocations and it is possible that funding defaults by such investors will increase. Political, regulatory and economic uncertainty, including as a direct or indirect result of, and market uncertainty stemming from, the covid-19 pandemic, may also temper deal flow as dealmakers wait to see whether the administration in the United States will continue to provide fiscal stimulus to key industries, as well as anticipation of the outcome of the US presidential race in the fall of 2020. Each of these factors creates uncertainty for the direction of private equity deal activity in the second half of 2020.

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