NewsRoom

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Mergers and acquisitions on hold as pandemic disrupts markets

Corporate merger and acquisition activity is taking a big hit from the global COVID-19 pandemic, as businesses reassess their priorities and brace for what could be an extended period of economic turbulence.

The pandemic is paralyzing business operations and disrupting commerce worldwide, causing many companies to think twice about moving forward with M&A transactions. The aggregate value of worldwide M&A transactions totaled $730.5 billion during the first quarter of 2020, a 25 percent decrease from year-ago levels, according to financial market data provider Refinitiv.

Deals worth more than $10 billion declined 53 percent in overall value. The trend will likely continue until the economy is back on track and businesses have more certainty, deal analysts said. In the meantime, measures such as the $2 trillion economic rescue legislation (PL 116-136) that was enacted by Congress last month can only help but so much, they said.

"I don't think the stimulus package is going to be a cure-all," Bryan Brewer, a partner in the M&A practice of Crowell & Moring LLP, told CQ Roll Call. "We need to get back to the ability to have businesses and consumers acting in a much more normal state than where we are right now."

Checks that are expected to be disbursed by the federal government to individuals and businesses as a result of the legislation will be like putting "a lot of ointment on wounds," according to Louis Lehot, founder of L2 Counsel PC, a Palo Alto, Calif.-based law firm specializing in business transactions. "Until we get back to work, you're going to see a continued free fall in the markets."

U.S. unemployment skyrocketed in March as nonessential businesses were forced to temporarily close their doors in compliance with state orders and White House guidelines aimed at slowing the spread of the virus. President Donald Trump predicted on March 29 that America will be well on its way to recovery by June 1. Just days before that, he indicated that he was eager to have the nation "opened up and just raring to go by Easter," which was met with widespread skepticism.

"Obviously, a big debate going on right now is how to turn the economy back on after having shut it down, and when do you do that, and what signals do you get from the health care community before you proceed," Douglas Cogen, co-chairman of the M&A practice at Fenwick & West LLP, told CQ Roll Call.

Last week, Xerox Holdings Corp. announced that it was withdrawing its proposed hostile takeover of HP Inc. as a result of the "turmoil" caused by the pandemic. Xerox said it decided to prioritize the health, safety and well-being of its employees, customers and partners above other considerations.

Meanwhile, other transactions are slowing down in the wake of the crisis, including Mylan NV's agreement to combine with Pfizer Inc.'s Upjohn and Flushing Financial Corp.'s plan to merge with Empire Bancorp Inc. Those deals are expected to close later than originally planned.

Unfinished deals stay that way

Generally, M&A agreements that have already been signed have a good chance of progressing due to legal hurdles involved with terminating them, while deals still in the negotiating stage are largely on pause, according to Carine Stoick, a partner at Hogan Lovells LLP.

"Where the parties haven't yet signed, buyers are rethinking whether now is the right time to move forward," she said in an interview. "In a situation where there's so much uncertainty, you can probably see how there's not going to be a meeting of minds when it comes to questions like purchase price and transaction value."

Similar issues came up during an April 2 meeting convened by members of a committee charged with advising the Securities and Exchange Commission on small business concerns. The panel met via video conference to discuss COVID-19 challenges.

Catherine Mott, who runs venture capital and angel investor funds BlueTree Venture Fund and BlueTree Allied Angels, said the purchase of one of the companies she invested in fell through at the "11th hour" when the buyer pulled out of the deal.

Greg Yadley, a partner at Shumaker, Loop & Kendrick LLP, said he noticed companies abandoning or delaying deals amid the crisis, and he predicted that transactions will continue to be affected for the next few quarters, even as the virus itself begins to subside.

"A number of deals where we've even had signed term sheets, people have put their pencils down or asked to renegotiate," he said. "If deals aren't close to the finish line, they are getting postponed. People want more visibility before committing."

Interest has cooled in previously busy sectors, including hospitality, real estate and retail, Yadley said. As companies look to future acquisitions, the focus is on technological advances in health care and communications, as well as tech start-ups with little exposure to supply chain risks, he said.

Jeff Solomon, CEO of the investment bank Cowen Inc., said that for the most part M&A deals that were close to closing were going through, though new deals would likely be delayed.

"If you're about to launch a process to sell a small business, you're probably going to wait," he said.

Last year was a dynamic period for M&A activity, with more than 46,000 deals announced globally, amounting to an aggregate deal value of $3.9 trillion, according to Hogan Lovells. In the year ahead, however, uncertainties around events such as the coronavirus and the presidential election could dampen deal volume and values "to a substantial degree," the firm said in a report on global M&A activity in 2019 and the year ahead.

In light of the virus, some parties involved in M&A contracts are weighing the possibility of invoking "material adverse change" clauses that can be used to terminate the transaction or trigger a renegotiation of terms, Hogan Lovells said. A material adverse change, or material adverse effect, is a shift in circumstances that significantly reduces the value of a company. However, the bar to satisfy a material adverse change condition is very high, according to Michael Szlamkowicz, another Hogan Lovells partner.

"Generally speaking, to have a material adverse effect, you need something that has a long term impact on a company," he told CQ Roll Call. "You're talking about something that would have almost a permanent impact -- something that has fundamentally changed the business."

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