Charting new horizons
M&A and the path to thrive

Iain Macmillan, Mark Purowitz, Sriram Prakash
A typical crisis has three acts: respond, in which a company needs to manage continuity; recover, to learn and emerge stronger; and thrive, where the company prepares and shapes itself for the new normal conditions. Globally, companies responded and recovered from the pandemic conditions by launching significant metamorphoses, and mergers and acquisitions played an instrumental role in this journey. Indeed, in 2021, against the backdrop of the most challenging conditions, corporates and private equity firms spent an unprecedented $5 trillion on M&A, the highest activity ever recorded. The emerging post-pandemic global landscape seems a world away from the past. The conflict in Ukraine and the unfolding human tragedy has fundamentally shifted the tectonic plates of geopolitics and could result in consequential changes to economies, global trade lanes, supply chain systems, and the green energy transition.

Corporate leaders need to adapt their organizations for these systemic and structural changes, against a backdrop of rising global inflation, interest rate hikes, supply chain realignment, increased regulatory hurdles, and renewed activist pressures. As part of this reset, they should also anticipate greater public scrutiny of corporate environmental, social, and governance (ESG) responsibilities and investor expectations, to deliver profits with purpose.
In retrospect: M&A wave of 2021

The M&A markets broke new ground in 2021. Around $5 trillion worth of deals were announced, easily surpassing the previous high of $3.66 trillion in 2015. Even in terms of volumes, a record 2,600 deals were announced, some 25% higher than in 2020, an upswing spread across small-, mid-, and large-cap segments. In a sure sign of confidence, around 144 megadeals ($5 billion) were announced, 65% higher than the previous year. Also, in stark contrast to 2008, when private equity firms made a dramatic retreat from the markets and deal flows dropped by 65% to $253 billion, this time they were one of the driving forces in the market, spending a record $1.7 trillion on buyouts, culminating in a growth of 124% over the previous year.

In sectors such as aviation, automotive, retail, and hospitality & leisure that were disadvantaged by the conditions, some made significant defensive M&A moves to safeguard value and stay afloat, while many made consolidation moves to safeguard their market positions. On the other hand, sectors including health, shipping, technology, and telecoms, which experienced a boost in demand, were on the offensive and initiated major M&A transactions to boost revenues and capture new markets. The standout feature of this market was all sectors and regions benefited from a surge in deal flow.

Given how the pandemic impacted each industry, sector, and region differently, the respective recovery cycles progressed at different levels of velocity. This meant the portfolio of response options was likely to be asymmetrical and was a more complex undertaking than in prior market contagions. Hence, the evaluation of an organization’s ability to act should be reframed to include not only financial considerations, but also operating model agility, strategic positioning, capital return horizon, and brand permission.

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Figure 1: Corporate M&A strategies in 2020–2021

<table>
<thead>
<tr>
<th>Defensive M&amp;A deals</th>
<th>Offensive M&amp;A deals</th>
</tr>
</thead>
<tbody>
<tr>
<td>48% Safeguard markets to maintain competitive parity</td>
<td>13% Salvage value</td>
</tr>
<tr>
<td>13%</td>
<td>28% Transform the business to safeguard the future</td>
</tr>
<tr>
<td>25%</td>
<td>11% Change the game</td>
</tr>
</tbody>
</table>

Source: Deloitte categorization of $1B+ global M&A deals during 2020–21

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At the start of 2022, the market sentiment remained highly positive, and Deloitte’s Future of M&A Trends Survey from the United States showed nearly 70% of the respondents expected to remain active in M&A markets. At the same time, the market conditions are rapidly evolving—the contagion risks of the Russia-Ukraine conflict potentially threaten globalization. The steep rise in commodity prices linked to these two countries, along with the inflationary pressures, are impacting most sectors either directly or indirectly and adding immense pressure to their already stressed supply chains. It is therefore not surprising as the IMF projects weak growth across most major economies and the threat of recession looms large.

Central bankers have indicated they will use rapid interest rate hikes to contain inflation. Companies need to recalibrate their debt strategies to reflect the changing market conditions and prepare for rising interest rates and possible lender limitations on cyclical businesses. There remain substantial levels of liquidity in the debt markets, and we expect there will be a strong lending appetite for highly defensive assets; however, lenders will also set a high bar on diligence for assets exposed to economic cyclicality, commodity prices, supply chain disruptions, and inflationary pressures.

Fund managers representing a total of $121 trillion of assets under management (AUM) have signed up to the UN Principles for Responsible Investment (PRI), and they are increasingly holding companies accountable for performance on ESG parameters. Many limited partner (LP) investors are also putting pressure on private equity and venture capital firms, and this has led to the launch of the ESG Data Convergence Project to advance standardized ESG reporting, driving more meaningful portfolio performance comparison and investment transparency. Similarly, a Deloitte survey shows 60% of CFOs believe their overall performance on ESG issues has an impact on their cost of capital.

Figure 4: Growth forecast by IMF (percentage)
Navigating toward new horizons

We anticipate the following tailwinds and headwinds to influence the M&A markets:

Harnessing the tailwinds

Record cash reserves
Since the onset of the pandemic, companies have taken decisive measures to bolster their cash piles, now amounting to a record $3.5 trillion. Collectively, this represents a very substantial arsenal. Dealmakers would be wise to heed the lessons of the 2008 financial crisis, when a compulsive cash accumulation culture emerged in the aftermath, and it inhibited the evolution of potential future-shaping investments and deals. A Deloitte study, "The cash paradox," found the markets were highly rewarding of companies that invest excess cash in the pursuit of growth, and such companies managed to grow their share price at an astonishing rate of 63%, compared to 32% growth rate of their cash hoarding counterparts.

Private capital
As of 2021, private equity firms are sitting on an estimated $2.5 trillion of “dry powder” and we anticipate for them to be highly active in the M&A markets. Increasingly, they are looking beyond financial reengineering to favor technology platform plays, digital transformation opportunities, and investments that are aligned with macro themes such as ESG. Meanwhile, we are also seeing private equity increasingly invest in the growth capital segment, competing with traditional venture capital funds, which invested a record-breaking $612 billion in disruptive startups and increasingly expanding into emerging markets such as Africa. Pension funds, family offices, and sovereign wealth are also making their mark on M&A markets. Historically, they placed their vast resources with wealth and private equity funds; however, we are also seeing a growing number of these investments being handled directly in-house. In recent months, they have directly acquired assets in a range of sectors such as transportation and renewables sectors.

Cross-border trade lanes
In 2021, cross-border M&A reached record levels. The North America-Europe M&A corridor was the busiest with $545 billion worth of deals. In addition, North American investment into the Asia Pacific region grew by triple digits to reach $191 billion. We anticipate this trend to continue, as a recent Deloitte snap poll shows 68% of US companies are considering international markets for new growth opportunities. From Asia, Japanese companies are leading the outbound wave focusing on transformative cross-border deals aimed at reorienting their portfolio toward growth and sustainability assets.

Figure 5: Record levels of corporate cash reserves (in billions of US dollars)

Figure 6: Strong appetite from private equity (in billions of US dollars)
Maneuvering the headwinds

Rising inflation and interest rates

The sharp revival of inflation has started to put pressure on consumer spending. In response, many central banks have indicated they will tackle inflationary pressures with interest rate hikes. At the same time, the US Treasury yield curve has started to flatten, which tends to suggest investors are expecting an economic slowdown.18 Such conditions also put pressure on corporate profits, bonds, and stock prices. It could prompt companies to review cash flow forecasts and recalibrate financial strategies to factor in inflationary pressures and expectations of interest rate hikes in their business models. Some might consider divesting non-core assets to free up working capital. Others may opportunistically acquire competitors to buffer against rising input costs, through procurement synergies, digitization efficiencies, and boosted pricing power.

Interestingly, a Deloitte analysis of the nearly 40 years of historical US M&A, inflation, and Federal Reserve interest rate data shows only moderate correlation between M&A and those macroeconomic indicators. In fact, during the five years to 1999, as well as in 2017, an upward M&A cycle was undeterred by both rising inflation and hawkish rate setting. We also found strong historical evidence that M&A markets tend to recover quickly from crisis conditions once uncertainty subsides as dealmakers rapidly adapt to the new environments and prefer to create their own momentum.19

Figure 8: Impact of inflation, interest rates, and crisis periods on M&A markets

<table>
<thead>
<tr>
<th>Year</th>
<th>US Fed rate</th>
<th>US Inflation</th>
<th>US M&amp;A</th>
</tr>
</thead>
<tbody>
<tr>
<td>1980s</td>
<td>15.9%</td>
<td>11.5%</td>
<td>16.5%</td>
</tr>
<tr>
<td>1990s</td>
<td>5.5%</td>
<td>6.6%</td>
<td>6.6%</td>
</tr>
<tr>
<td>2000s</td>
<td>6.5%</td>
<td>6.7%</td>
<td>6.8%</td>
</tr>
<tr>
<td>2010s</td>
<td>0.4%</td>
<td>0.5%</td>
<td>0.6%</td>
</tr>
</tbody>
</table>


Regulatory hurdles

The elevated levels of M&A activity are catching regulators’ attention, and amid severe scrutiny, some $340 billion worth of deals were impacted since the onset of the pandemic.20 There is also constant pressure on deals from activist funds, shareholders, and even consumers, creating further uncertainties.

Companies will need to demonstrate the long-term benefits of their deals to regulators and broader stakeholders, against a backdrop of protectionist instincts that are clouding M&A. Crucially, whenever a deal is thwarted, investors will expect a “Plan B” strategy to be instigated promptly. Deloitte analysis shows that within one year of a proposed transaction’s withdrawal, around half of acquirers and targets remained active in the market and completed new deals.21

Figure 9: Mega deals (>$5B) stalled or withdrawn due to political and regulatory interventions

<table>
<thead>
<tr>
<th>Year</th>
<th>Deal count</th>
</tr>
</thead>
<tbody>
<tr>
<td>2020</td>
<td>14</td>
</tr>
<tr>
<td>2021</td>
<td>12</td>
</tr>
</tbody>
</table>

Source: Deloitte analysis based on data from Refinitiv and Mergermarket

Rising valuations

In 2021, the average price-to-earnings deal multiple rose sharply to 26.5, the highest since 2015.22 The pandemic conditions gave a boost to valuations in many sectors like home fitness and media streaming, but as the conditions and consumer habits change, recent financials may not be accurate predictors of future performance. When evaluating opportunities, companies should undertake rigorous valuation that is underpinned by dynamic modeling, scenario planning and detailed value extraction plans. This should help strike the balance between mature acquisitions targeting focused returns, and those based on the promise of exponential disruptive growth.
Path to thrive: Rethinking M&A strategies

As we move toward a post-pandemic world, through previously uncharted paths, thriving in such an environment requires companies to reimagine the future of their markets, reexamine their core capabilities, and reevaluate their competitive advantages. In parallel, as part of long-term value creation, companies also need to consider the impacts of other macro themes such as digitization, technology shifts, climate change, health care and well-being, energy transition, skills shortage, and aging populations. This will help them make fundamental choices on growth strategies, prioritize the markets and segments where they need to play, identify gaps and the skills they need to win, and determine how to transform themselves in the process.

Building on our research from the original Charting new horizons report, we have evolved the M&A framework to demonstrate a new set of defensive and offensive deal archetypes that are required to build resilient business models, accelerate transformation, unlock the potential of ecosystem alliances, and capture market leadership. Redefining M&A strategies in terms of these choices will bring much-needed clarity of purpose while paving the path to thrive.

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Defensive M&A: Building resilience

One of the lessons from the pandemic is that all companies, large or small, will need to firmly establish resilience at the heart of their business model and organizational culture. Building resilience can help ensure an organization is agile and adaptable, able to ward off threats from the marketplace, and prepared to deal with complex and unpredictable events in the future. We anticipate these defensive moves will materialize in several different ways:

Cleaning the stables

Accelerate synergy realization and deliver value

In 2021, shareholders gave approval for nearly $5 trillion worth of deals, and now the dealmakers involved can anticipate significant investor pressure to accelerate synergy realization and deliver value.

Investor reactions matter. In their new book, The Synergy Solution: How Companies Win the Mergers and Acquisitions Game (Harvard Business Review Press), Deloitte authors Jeff Weirens and Mark Sinoway studied 1,267 deals over a 24-year period, collectively representing $5.37 trillion of equity value. They found that initial market reactions, positive or negative, are powerful predictors of how deals will eventually turn out. The authors identified clear evidence that acquirers who begin with a positive market reaction, enjoy returns some 60 percentage points higher than acquirers who start by facing a negative reaction and go on to realize those negative forecasts. 26

Additionally, based on Deloitte's work on thousands of deals, we estimate that tax synergies regularly represent more than 20% of available deal gains. Significant benefits can be found in tax alignment in the value chain—including among suppliers—and through improved operating footprints and integration strategies. Strategies such as capturing local tax credits and shifting some software to the cloud can contribute to the self-funding of digital transformations. Companies should be equally mindful of potential tax risks, with careful consideration given to the location of intellectual property rights and profit generation, as well as local presence stipulations. 27

Most integration programs follow a consistent pattern of three phases: integrate to close, establish an interim operating state while investing for the future, and deliver the realization of the business case. The fundamental problem is most programs never go beyond an interim state due to changes in market conditions, insufficient management attention, and a business-as-usual mentality taking over. The longer post-close execution takes, the less likely management will be able to deliver the promised returns.

Sophisticated acquirers transform as they transact, to accelerate the time-to-value of business case realization. Leveraging tools, such as predictive analytics, robotic process automation, and digital platforms, can help capture both cost and revenue synergies, ensuring a merger is far more than the sum of its parts. 28

In addition, many companies are reexamining their existing business through an ESG lens and identifying problematic assets to divest. Potential buyers are increasingly sensitive to risks around workplace inclusion and diversity, the supply chain, brand perception, and the impact of climate change. Given these shifts, ESG-related diligence and compliance are becoming key components of deal execution and post-deal transformation. 29

Recently, when a large private equity firm acquired the beverage division of a major consumer business company, it undertook additional diligence specific to ESG considerations and made it central to the investment process. 30

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Defensive M&A

Optimize the portfolio

Many companies are facing pressure from activist hedge funds for portfolio restructuring, from regulators pressing for asset carve-outs as a condition for merger approval, and from their own boards, which are keen to ensure companies remain on track with sustainability and net-zero commitments.

The 2022 Deloitte Global Divestiture survey found that seven in ten companies are considering making two or more divestments in the next two years, as they continue to focus on building resilience. The survey also shows that four in ten businesses are already selling carved-out assets at higher than expected prices, in part due to increased pressure from private equity buyers. 31

Becoming a prepared seller is more important than ever. The one-time cost of preparing to shed a business is rising, and two thirds of the survey respondents say the cost of the atypical divestiture is 4% to 7% of the revenue of that asset, in sharp contrast to the less than 3% figure from our equivalent 2020 report. 32

In addition, many companies are also reassessing their existing business through an ESG lens and identifying problematic assets to divest. Potential buyers are increasingly sensitive to risks around workplace inclusion and diversity, the supply chain, brand perception, and the impact of climate change. Given these shifts, ESG-related diligence and compliance are becoming key components of deal execution and post-deal transformation. 33

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Optimize the portfolio

Explore opportunistic deals to safeguard supply chains and competitive positioning

Global supply chain disruptions are impacting every sector, either directly or indirectly. In addition, changing stakeholder expectations toward ESG are putting pressure on businesses to fundamentally redesign their supply chain systems to improve transparency and reduce their carbon footprint.

M&A activities can play a key role in shaping the response. Companies could explore opportunistic deals to safeguard existing supply chains and consider innovative options such as backward or forward integration with suppliers. For instance, a major global retailer is considering starting a captive shipping company and acquiring its own containers to maintain seamless flow of goods. 35

Companies could also consider strategic acquisitions of suppliers to maintain competitive positioning in the market. In response to the global semiconductor chips shortage crisis, a major chipmaker recently acquired a specialist chip contract manufacturer to boost its production capacity and safeguard its customer base. 36

Businesses may look at consolidation to firm up competitive positioning. Among those already doing so is a major Canadian bank that acquired a competitor in the United States as it provided entry into growth markets, complementary capabilities to drive efficiencies, and the ability to capture powerful economies of scale. 37

It is also important to consider co-investment and partnership opportunities with suppliers or even private equity firms, to pool capital and expertise toward investing in value-enhancing opportunities. For instance, a major global logistics company recently sold a minority stake in one of its subsidiaries to a private equity firm to tap into the fund’s significant investment strength and expertise, jointly implementing a transformational value plan with new freight forwarding trade routes, additional growth verticals, and fresh M&A activities. 38

Strengthening the fortress

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Offensive M&A: Charging the growth engine

As the first US President George Washington observed, “the best defense is a good offense.” Bold moves involving transformative acquisitions, ecosystem alliances, and disruptive investments will be required to charge the growth engine and lay the groundwork to capture market leadership. Companies clearly need to play offense to gain momentum, and we anticipate those efforts to materialize in several different ways:

**Accelerating business model transformation**

**Capture the digital future**

The pandemic conditions ruthlessly exposed companies that lagged in digital investment, omni-channel capabilities, and agile operating models, and at the same time they established new market opportunities for companies that were digitally prepared.

In a recent CEO survey by Fortune magazine and Deloitte, nearly two out of three executives indicated digital was their number one transformation priority. Such changes are an enterprise-wide long-term commitment that cuts across business departments and technologies. Some companies will actively seek alliances and partnerships for these efforts, while others will acquire technologies and capabilities to accelerate their transition. In response to the significant growth in online shopping, a major heritage shipping company made multiple e-commerce logistics acquisitions in a relatively short space of time to rapidly scale its digital and integrated logistics capabilities.

**Identify portfolio gaps and expand the value chain**

Corporations need to regularly reevaluate their sources of competitive advantage, identify portfolio gaps, and consider opportunities for expansion. In a recent Deloitte survey of CFOs, opportunistic deals to fill gaps in product and service portfolios were rated the top M&A priority.

Establishing a pipeline of deals can expand a company’s value chain and make it easier to capitalize on adjacent market spaces. Companies may also explore platform business models to expand and unlock the value of their customers and networks. For instance, a major technology business that specializes in financial software has acquired a marketing platform to significantly expand its service offerings and continue its transformation to become the leading AI-driven expert platform for small businesses.

**ESG—delivering returns with purpose**

Businesses are increasingly expected to demonstrate they can deliver returns with purpose and create value not only for their shareholders but also for their stakeholders, including employees, customers, suppliers, and societies where they operate. In turn, many companies are aligning their investment strategies with UN Sustainability Goals, a universally accepted framework for measuring progress against ESG goals. Impact investing is fast becoming a dedicated M&A strategy, and in 2021 around $188 billion was spent by corporations on acquiring relevant assets, the highest figure on record.

**Unlocking value from the ecosystem**

**Collaboration as a competitive advantage**

One of the enduring legacies of the pandemic is how corporates embraced collaboration, forming the bedrock of global recovery. The post-pandemic transition will continue to bring significant challenges such as supply chain disruptions, skills shortage, climate change complexities, cross-sector convergence, and many others that cannot be solved unilaterally.

These dynamics have necessitated the need to expand the scope of traditional M&A strategies to include collaborative structures such as ecosystem alliances, partnerships, and other similar constructs that are not bound by traditional industry boundaries, but instead coalesce around common purpose and create shared value for the businesses, their clients, and their communities. It seems that every opportunity now needs to be considered through the lens of whether to build, buy, or collaborate.

Companies should actively reach out to a multiplicity of partners to build such purpose-led alliances and partnerships. This could include aligning with a diverse range of collaborators including suppliers, private equity firms, innovative startups, cross-sector specialist peers, or even traditional competitors. Among those already doing so, in the aviation sector, a progressive alliance of an aircraft manufacturer, industrial gas supplier, and airport operator has been formed to promote the use of hydrogen infrastructure and accelerate decarbonization of the aviation industry.

**Investing in ESG pathways**

Investing in ESG pathways requires companies to adopt a multidimensional M&A strategy. These could involve product plays by investing in businesses whose core product and services drive ESG improvement, such as those in waste management, infrastructure plays by investing in companies that provide the underlying infrastructure for sustainable solutions, such as those in vertical farming, and technology plays by investing in businesses that are using disruptive technologies to displace the market by creating new product categories, such as those using cell-based biotechnology to cultivate meat in laboratories.

**Scaling at the edge**

Corporate venturing is a springboard to test new technologies, market offerings, and talent that can shape the future of sectors. As ecosystems mature, it is important that companies develop corporate venturing strategies and aligned capabilities such as horizon scanning and ecosystem engagement as an integrated approach to innovation-led business transformation. Such capabilities can give companies the confidence to build a portfolio of investments at the edge of their existing markets and establish strategic positions in transformational growth segments. For instance, a major consumer business company was using its venture arm to closely monitor scientific trends and technologies around conventional meat alternatives, and this informed its investment in a cultivated-meat startup.

Bold moves involving transformative acquisitions, ecosystem alliances, and disruptive investments will be required to charge the growth engine and lay the groundwork to capture market leadership.
M&A and the path to thrive

Sectors will evolve at different trajectories and paces. At the same time, technology-enabled convergence is blurring traditional sector boundaries and creating new market opportunities and customer segments. Companies need to reframe their growth options to include not only financial considerations but also operating model agility, competitive positioning, capital return horizon, and brand permission to enter new markets.

M&A strategies are now firmly cemented as a fundamental part of the corporate arsenal, both in defense to preserve value, as well as in offense to drive transformative growth. This framework can help companies articulate a new combination of M&A strategies to fortify their gains, accelerate business model transformation, and make horizon investments to capture lasting market leadership.

Defensive M&A strategy

02 Cleaning the stables
Do you have a non-core asset divestment program in place? Do you plan for rapid asset transformation to enhance the sale value?

01 Accelerate synergies
Are you well-positioned to accelerate both cost and revenue synergies and demonstrate the wider stakeholder benefits?

03 Strengthen the fortress
How can you use M&A as a strategic response to shape responses to optimize the operating model and supply chain resilience and enhance your customer-centricity?

04 Safeguard competitive positioning
Are you actively monitoring the markets and prepared to move fast on opportunistic deals to consolidate segments?

05 Portfolio transformation
Are you undertaking a portfolio review and considering the implications of the “new normal” factors such as technology transformation and ESG on your current and future portfolio?

Offensive M&A strategy

06 Digital acceleration and portfolio expansion
Are you considering M&A deals to accelerate digital transformation and develop platform and “as-a-service” plays to capture new revenues by expanding your portfolio into value chain adjacencies?

07 ESG and impact investing
Businesses are expected to demonstrate they can deliver returns with a purpose. Do you have a multidimensional view of ESG investment aligned with product, infrastructure, and technology plays?

08 Alliances
Are you exploring value creation opportunities through purpose-led alliances with a diverse range of collaborators, including nontraditional peers and innovative startups?

09 Convergence
Are you actively looking to capture cross-sector convergence opportunities to create new products, customers, and market segments and position for market leadership?

10 Scaling at the edge
Do you have horizon scanning capabilities? Are you looking to build a portfolio of disruptive investments at the edge of your business to establish strategic positions in transformational growth segments?

M&A strategies

- Defensive M&A strategy
- Offensive M&A strategy

Building resilience
Unlock value from the ecosystem
Change the game

Strong
Weak
Strategic positioning in the marketplace
Sector M&A pathways
Energy, Resources & Industrials

Observations

After a year of subdued M&A activity in 2020 due to the pandemic, Energy, Resources & Industrials (ER&I) rebounded in 2021 with a 67% YoY growth in deal value to $1,037B and 17% YoY growth in volume to 13,429 transactions.

North America with $931B worth of deals was the most active region with respect to deal value, while Asia Pacific with 4,692 deals led in terms of deal volume in 2021.

Among subsectors, Power, Utilities & Renewables saw the highest deal value and volume in 2021.

Energy transition is the primary driver of M&A activity as oil and gas companies look at shifting their portfolios toward clean energy.

ESG growth areas such as carbon capture, hydrogen, renewables, and other clean technologies are expected to be key focus areas.

The sharp rise in global energy prices fueled by the Russia-Ukraine conflict may drive consolidation within the Oil, Gas & Chemicals subsector.

Industrial Products & Construction M&A activities are anticipated to pick up as companies invest in new capabilities such as digital and supply chain.

Increased demand and constrained supply are driving changes

• A combination of supply constraints and geopolitical tension has resulted in energy price increases and is putting pressure on operating models that had become lean in recent years offset with low prices.

Active portfolio monitoring

• Companies will need to monitor their portfolios to avoid carrying stranded assets as well as to avoid unnecessary divestment of assets that may prove profitable in other supply/demand environments.

Importance of customer-centricity will increase

• To thrive throughout the energy transition, fuel companies will need to offer a full suite of products and services.

• Companies will look to draw closer to end customers and incorporate convenience as key to the customer experience.

Short-term responses

1. Portfolio restructuring to drive energy transition
Companies are fundamentally rethinking their portfolio, seeking to divest higher carbon-intense assets, pursuing acreage consolidation, and acquiring assets aligned to energy transition.

2. Investments to build future capabilities
Companies could use of the current high energy prices to make significant investments and acquisitions related to digitization and integrated value chain driving new revenue streams.

Medium-term responses

3. Energy transition alliances
The energy transition is attracting investments from nontraditional competitors in other sectors, as well as private capital. Companies should consider cross-sector alliances with companies in automotive, technology, and other sectors to gain direct access to customers and explore new revenue models.

4. Sustainability-aligned growth segments
Companies should actively seek opportunities in adjacent markets such as chemicals, advanced plastics recycling and others where they can leverage existing expertise such as R&D and customer networks.

Forces shaping new normal conditions

Increased demand and constrained supply are driving changes

Decarbonization across industries is enabling new energy era

Green jobs will require new skills in the workforce

M&A strategies

Defensive M&A strategy

Building resilience

Accelerate business model transformation

Unlock value from the ecosystem

Change the game

Strategic positioning in the marketplace

M&A and the path to thrive
Industrials

Forces shaping new normal conditions

Technology driving industrial connectivity
• Advancements in the Industrial Internet of Things (IIoT) and digital twin technology are driving significant innovation in solutions and business models.

Supply chain disruption impacting production times
• Long lead times for critical components are creating uncertainty in production planning and forecasting.
• Delays in manufacturing and port congestion will drive companies to identify resilient solutions for supply networks.

Digital solutions will lead to workforce evolution
• Digital-first solutions will impact the skillsets required from the workforce.
• Industrial companies will compete with tech firms for talent, while simultaneously upskilling their current workforce.

ESG pressures will continue to grow
• Stakeholders will increasingly call for ESG commitments.
• Creating the factory of the future through smart technology and green energy will remain in focus.

Rising raw material costs impact margins
• Shortage of supply along with increases in raw material costs and shipping rates have created pricing pressures.
• Unless contained, these cost rises threaten to outstrip the productivity gains and could significantly impact profit margins.

Short-term responses
1. Strengthening of value chain
   Acquisitions and investments related to vertical integration could help companies secure long-term suppliers and mitigate supply chain disruptions.

2. Shifts in core competencies
   The inevitable shift toward sustainable processes and products is likely to impact the core competencies of many companies, and they should drive this change through targeted acquisitions.

Medium-term responses
3. Technology alliances
   Industrial companies should consider alliances with the technology sector to boost innovation and leverage specialist digital skills expertise.

4. Investing in disruptive technologies
   Industrial companies should consider growth acquisitions in focused areas such as IoT, robotics, automation, digital twin, and AI to drive long-term transformation.
### Consumer & Automotive

#### Observations

The Consumer sector saw YoY growth of 70% in M&A value to $909B in 2021. North America was the most targeted region with $365B worth of deals in 2021. Europe was at a distant second, with deals worth $261B during the same period. In terms of M&A volume, Europe was the most active region with 6,263 deals, followed by Asia Pacific (5,406 deals) and North America (3,893 deals).

Transportation, Hospitality & Services was the most active subsector with $381B worth of deals, while Automotive saw the highest YoY growth at 166% to reach $152B in 2021.

Some of the likely drivers for M&A activity in 2022 include:
- Increase in divestments of Automotive dealer networks, technology components, and non-core divisions
- Increase in deals from Logistics and Transportation sectors
- Building resilience against supply chain disruptions
- Rising interest in geographical expansion and product innovation
- Evolving preferences in retail and consumer goods (e.g., omnichannel, delivery logistics, sustainable products, emerging tech, hot markets such as health and wellness)

#### Pressures on margins

- Surges in inflation, customer demand, supply chain disruptions, and higher labor costs are leading to rapid increases in production costs and pressure on margins.

#### Slower recovery in some subsectors

- Post-pandemic uncertainty continues to impact the leisure, travel, and hospitality sectors.
- Revenue losses in these sectors, originally from the pandemic but now from inflation, could contribute to an increase in sales of distressed assets and restructurings.

#### Direct-to-consumer (D2C) purchases will increase

- D2C models will enable companies to increase customer-centricity through personalization, loyalty programs, and increased customer service levels.
- More companies will look to be active in the D2C space and acquire platforms to increase scale of distribution.

#### Sustainability and wellness influences purchasing behavior

- Consumers are increasingly willing to pay a premium for socially conscious products, ethical supply chains, and wellness-focused offerings.
- This trend is creating opportunities for new revenue streams.

#### M&A strategies

### Short-term responses

1. **Supply chain resilience**
   - Companies could consider investing in contingency supply chains, this includes considering partnerships with new suppliers, as well as with private equity to bolster supply chain systems.

2. **Technology-led transformation**
   - Digital transformation is fundamental to success. In addition to omnichannel capabilities, companies should consider investments in predictive demand analytics, fulfillment, and dynamic pricing.

### Medium-term responses

1. **Pursue alliances**
   - Companies could consider alliances with their peers to alleviate supply side pressure, as well as cross-sector arrangements with sectors like technology to enhance customer experience.

2. **Growth investments**
   - Companies could consider an ESG-aligned investment strategy to target assets such as sustainable product design and packaging, as well as, in emerging growth segments such as personalized nutrition and carbon-neutral travel.
**Connectivity is becoming standard**
- The majority of cars are expected to have smart connectivity by 2035, driven by consumer demand and regulation.
- Data generated by 5G connectivity will be valuable and utilized by OEMs, dealers, fleet owners, and consumers.

**EV and fuel-cell ecosystems**
- The EV market and associated ecosystem are expected to grow in double digits driven by customer preferences, favorable regulation, private capital investment, and the strategic push by OEMs.
- Hydrogen fuel-cell powered vehicles are starting to make up a more meaningful portion of the market.

**Short-term responses**
1. **Safeguard supply chain**
   Supply chain disruptions may prompt OEMs to vertically integrate critical aspects such as chips and divest auxiliary services such as auto-financing, retail insurance, etc. to facilitate these critical investments.
2. **Agile business models**
   Companies should consider investments across the entire value chain to make the business more agile; these include opportunities for digitization, flexible manufacturing, and smart factories.

**Medium-term responses**
1. **Software-centric partnerships for CASE development**
   Access to a comprehensive software suite is critical to success for driving Connected, Autonomous, Shared, and Electric (CASE) products. OEMs should explore alliances and partnerships to drive this forward.
2. **Future portfolio realignment**
   Companies need to continue building a future portfolio that aligns major shifts in consumer trends. This could include value chain opportunities such as smart infrastructure, recycling, and sustainable materials.
Life Sciences & Health Care

Forces shaping new normal conditions

**Digitization of health care**
- The potential for new variants, speed of vaccination, and changing government approaches all contribute to pandemic uncertainties.
- Consumers got used to alternative service delivery methods during the pandemic, and there could be an increased demand for virtual care and automated medication management.

**AI will fundamentally impact business models**
- AI and big data create the opportunity to further tailor care to specific patients and treat diseases earlier in their life-cycle.
- The rise of virtual and lower-cost sites of care means that some providers may be stranded with more physical assets than needed.

**Mental health will continue to be a priority**
- Demand for mental health treatments is growing due to reduced stigma, pandemic effects, and other behaviors.
- Models of care that incorporate mental health into existing treatment centers will increase.

**Industry economics may shift**
- A focus on value-based and outcome-based care may change the way companies generate revenue.
- New business models would focus on early-detection and preventive care.

Observations

Life Sciences & Health Care (LS&HC) recorded a 45% YoY growth in deal value to reach $482B in 2021.

The rise in value was primarily driven by the strong 132% YoY growth in the large deals segment (≥$1B to $10B) to a total $217B in 2021.

North America was the largest contributor among the regions with 2,315 deals worth $303B. Europe, with $94B worth of deals, was a distant second in terms of values, while Asia Pacific was second with 1,907 transactions, in terms of volume.

Among the subsectors, Health Care saw the highest YoY increase in M&A value and volume. Deal values rose by 121% to reach $213B and deal volume rose by 33% to reach 3,463 transactions.

**Short-term responses**

1. **Mitigating uncertainties**
   Companies need to potentially divest non-core assets and invest in capabilities such as supply chain, alternative service delivery, and next-gen therapeutics.

2. **Technology-led business model transformation**
   Investments in digitalization and remote service capabilities will reduce delivery costs, increase patient access, and augment inpatient services. LS&HC companies are likely to invest in R&D enabling technologies such as AI-driven drug discovery.

**Medium-term responses**

3. **Integrating patient-care value chain**
   Integrating with insurers, providers, and retailers would improve patient care and provide cost efficiencies; data sharing and trust will prove to be critical in delivering value from such ecosystem partnerships.

4. **Technology-enabled preventive care**
   The convergence between technology and health is enabling new business opportunities in areas such as health monitoring, preventive and predictive care. LS&HC companies should have an active investment strategy for such emergent spaces.
Financial Services

The Financial Services sector recorded $1,117B worth of deals in 2021, registering a 62% YoY growth, the highest growth rate in the last five years.

This rise was primarily due to a 105% YoY growth in the US, to $407B in 2021.

Deal volumes also saw a YoY rise of 17% to 9,688 transactions in 2021.

Europe emerged as the most active region in terms of deal volume by recording 3,221 transactions followed by Asia Pacific (2,914 deals) in 2021.

Among the subsectors, Investment Management & Real Estate registered the largest absolute value growth to $572B, primarily driven by a large rise in REIT deals to $471B in 2021 from $260B in 2020.

The Financial Services sector is expected to continue witnessing robust M&A due to strong top-line growth, high profitability, and positive macro trends such as high savings rates and anticipated high inflation.

Observations

Forces shaping new normal conditions

Stakeholders demand ESG commitments

- Increased scrutiny from clients, regulators, investors, and employees on companies’ ESG commitments will impact business models for financial institutions.

Regulation will continue to influence the market

- Regulators are expected to respond to the rapid developments in the sector with the introduction of new rules, especially in the areas of digital assets, climate, and financial inclusion.
- Regulatory convergence is increasingly desired by central bankers and could have a major impact on competition and market strategies.

Digital assets, blockchain technology, and cybersecurity are increasing in importance

- The introduction of new, disruptive products and technologies has led to banks investing heavily in new technologies and creating alliances with partners that have broader digital capabilities.
- Banks are shifting toward integrated platforms and cloud solutions to improve cybersecurity and enhance analytical capabilities.

Skewed balance sheets are resulting in declining ROEs

- Banks have divested non-core assets from their portfolios, resulting in a skewed balance sheet with legacy products.
- Growth will be required to deliver more stable ROEs.

M&A strategies

Short-term responses

1. Divestment of non-core assets
   Companies could consider divesting underperforming loan portfolios and non-core divisions to raise capital and improve efficiency.

2. Technology-led business transformation
   Investments and acquisitions of new technologies (e.g., digital payments, e-trading platforms) will be critical to position banks to compete in the future.

Medium-term responses

3. Cross-selling opportunities
   Banks need to establish alliances outside of their core sector with players from technology, retail, health, and others to cross-sell new services to a wider customer base, introduce new capabilities, and improve utilization of their current assets.

4. Growth investments
   Banks also need to consider acquiring High-growth, innovative businesses in areas like cybersecurity, fintech platforms, blockchain, AI, and others in adjacencies that could, in time, become the new core.
Portfolio rebalancing

Market consolidation

Consolidation

Future portfolio

Bolt-on capabilities

Platforms (robo-advisors).

Technologies such as automated portfolio

Such as ESG investment specialism and

Pursuing M&A to acquire new capabilities

Investment management firms are

Firms are using digital channels and

Process automation to enhance

Client interactions.

ESG will impact

Asset allocation

The focus on ESG will impact

Investment allocation decisions, investment transparency, regulatory

Reporting, and product marketing decisions. It will also likely drive

Product innovation in this segment.

Performance pressures are impacting allocations

The alternatives market has gained wide

Acceptance as it offers portfolio diversity

And higher returns. This is placing further

Pressure on allocations and integration

With traditional asset classes.

Regulators are focusing

On customer protection

Regulators are likely to focus on increased

Client protections in areas such as data

Privacy, fee transparency, product

Unbundling, and ESG offerings.

Lack of alignment could result in regulation

Asymmetry across jurisdictions.

Demand for digital

Assets will require

New capabilities

Increasing interest in digital assets

(eg, crypto, NFTs) requires firms to

Develop or acquire new technologies

And product offerings.

These new offerings will also increase the

Importance of cybersecurity capabilities.

Insurance

Forces shaping new normal conditions

Reduction in property and casualty (P&C)

Business volumes will drive innovation

Reduction in traditional volumes and

Pricing pressures are forcing P&C insurers to focus on innovative offerings such as

Usage-based insurance and sensor-enabled analytics.

Customer centric

Business models

Customers are increasingly expecting an elevated customer experience, forcing investment

In analytics and new product development.

Convergence of insurance with digital health platforms is giving rise to

New customer product categories and untapped market segments.

ESG is more than a ‘brand’ play

For insurance companies, ESG principles will underpin the new emotional contract.

Insurance companies are uniquely placed to influence ESG mandates on global

Businesses given role underwriting

Industrial activities for other companies.

Forces shaping new normal conditions

Emerging talent model

Pressure on growth is forcing insurers to develop innovative operational solutions.

This is leading to investment in and hiring of skilled workforce in new areas such as digital,

Cloud, automation, risk controls, and customer analytics.

Insurers need to foster a flexible and agile workplace culture for such fresh talent to thrive.

Short-term responses

Consolidation

Sector is ripe for further consolidation and in recent months, major players have been

Rapidly consolidating in response to falling fees and lack of growth.

2 Bolt-on capabilities

Investment management firms are pursuing M&A to acquire new capabilities such as ESG investment specialism and technologies such as automated portfolio platforms (robo-advisors).

Medium-term responses

3 Nontraditional alliances

Firms need to consider alliances outside of their core activities to expand their current

Client base, skills, and product offerings.

4 Future portfolio

Firms also need to consider acquisitions of high-growth, innovative businesses in

Adjacent growth areas such as crypto funds, NFTs, crypto asset management platforms, and others.

3 Portfolio rebalancing

Market uncertainties resulting from geopolitical conflict and the need for

Capital optimization may prompt insurers to divest non-core assets and exit

Underperforming markets.

Market consolidation

Costs of legacy business models and operating pressures are likely to drive

Consolidation in the market in order to capture economies of scale and accelerate

Transformation by investing in digital assets and analytics capabilities.

Charting new horizons | M&A and the path to thrive
Technology, Media & Telecom

Observations

Technology, Media & Telecom (TMT) was the most active sector with $1.3T worth of deals in 2021.

North America was the most active region for TMT deals, with $829B worth of deals in 2021. Asia Pacific was at a distant second, with deals worth $268B.

Among the subsectors, Technology (8972B; 13,660 deals) accounted for 72% by value and 81% by volume of the overall deals within the sector.

Private equity investors were highly active in the Technology subsector with deals worth $503B, the highest among all the subsectors.

The rise in spend toward information security and enterprise software driven by remote working is expected to propel drive to Technology M&A in 2022, while in the Telecom sector, many have divested their towers and now will be looking for fresh growth opportunities.

However, going forward, tighter foreign direct investment controls and national security screening may pose a challenge to technology deals.

Technology

Forces shaping new normal conditions

Data sharing creates value but raises security concerns
- Cloud and digital transformation have led to data sharing within and across companies.
- Increased concern around data privacy and security creates a headwind for new business models.

Flexible working is forcing companies to innovate
- ERP, Finance, HR, and other specialist software are becoming more strategic and less administrative.
- Businesses will need to innovate on functionalities and protection as remote working becomes more prevalent.

Semiconductor chip shortage likely to last through 2022
- Digital transformation is driving demand for chip designs with innovative technologies.
- This increased demand, coupled with the pandemic, has resulted in a supply shortage likely to last until 2023.

Green technology
- The ICT sector is under pressure to reduce emissions and make its products more sustainable. This is likely to spur greater investments in green data centers, fresh product design, and other sustainability areas.

M&A strategies

Short-term responses
1. Consolidation across the cloud value chain
   Technology companies need to improve their competitive positioning through holistic platform solutions as opposed to point-based solutions. This could drive M&A consolidation across the cloud value chain and supplier base.

2. Specialist software vendors
   Scaled HR and other ERP specialist technology companies may look to expand their offering to adjacencies such as ESG, mental health, and wellbeing.

Medium-term responses
3. Proliferation of alliances
   Technology is driving innovation across all sectors, and technology companies could explore alliances and JV models as an alternative pathway to access opportunities arising from technology-enabled convergence across sectors.

4. Frontier investing
   The technology sector is likely to drive innovation through investments in green data centers, material science, spatial computing to drive AR/VR, AI, quantum computing, and many others.

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Media & Entertainment

Forces shaping new normal conditions

Competition in D2C could drive spending on exclusive content creation
- Proliferation of streaming platforms is resulting in increased churn, forcing providers to tailor content and pricing models.
- Saturation in the US market driving streaming providers to push further into international markets.

Data integration should create value
- DTC content creates the ability for companies to gather additional customer information.
- Data integrations across different offerings will enable a unified view of the customer that will drive content recognition and increase ad value.

Generational divide regarding alternative types of entertainment
- Gen Z have higher preference for video gaming and user-generated content over traditional TV and movies.
- Increased preference for user-generated content changes consumption patterns and gives rise to new platforms.

Metaverse to drive convergence in content
- Media and entertainment companies will be central to the metaverse, which will result in a convergence in traditional video content, video games, technology, and advertising.
- Immersive franchises with owned IP will be able to create deep engagement and new monetization mechanisms.

Socially conscious media
- The media sector is directly exposed to shifts in social trends, and there is heightened customer pressure for the sector to become, as well as to produce, content that is socially aware, equitable, and diverse.

Medium-term responses

3 Alliances and partnerships
Emerging areas such as the metaverse are increasingly dependent on multiparty marketplaces and ecosystems that span content creators, platforms, and consumers. The need for scale across customers, platforms, franchises/content, and technology is likely to drive landmark partnerships in the future.

4 Future portfolio
Advances in technologies like AI, machine-recognition, etc. are rapidly changing the media production and consumption landscape and are likely to spur greater investments in these areas.

M&A strategies

1 Customer retention
Companies could use M&A activities to secure premium content, acquire/retain customers, and bolster technological capabilities.

2 Investment in new capabilities
To capitalize on the disaggregation of traditional distribution networks resulting from migration to DTC media, M&E companies should acquire new capabilities to allow them to capitalize on their new relationship with the customer.

Telecom

Forces shaping new normal conditions

Governments driving the growth of global fixed wireless access (FWA) connections
- Regulators now view wireless as an acceptable alternative to wired and governments have increased funding of broadband, resulting in more operators considering 5G enhanced FWA.

5G gaining traction
- Global carriers are expected to show distinct 5G performance improvements in the coming months.
- Improved performance will result in increased demand for 5G-enabled devices and service.

Subscriber growth and smartphone adoption likely to be sustained at elevated levels
- Underpenetrated demographics (<13 and >50 years old) are likely to gain new subscribers and increase use of smartphones to facilitate remote learning and video calling.
- Government subsidies are providing for connectivity needs.

M&A strategies

1 Competition for telecommunications infrastructure assets
Both financial and strategic buyers are competing for infrastructure assets; carriers will likely divest non-priority assets, potentially including large scale data centers, to fund other initiatives (e.g., 5G, IoT).

2 Telecom companies will continue to divest media assets
Following a run on acquisitions of media companies, telecom companies are refocusing on core capabilities.

Medium-term responses

3 Adoption of 5G and cloud
Greater adoption of 5G should drive new products and services and, in turn, could spur telecoms to acquire new capabilities such as ones to make cloud migration more feasible and accelerate adoption of multi-cloud environments.

4 Partnerships
Telecom companies may increasingly partner with their peers as an alternative to M&A to drive operational efficiency and increase investment in areas like FTTH. In addition, they should also explore cross-sector partnerships with health and financial sector to drive new consumer opportunities.
Conclusion

In the past decade, leaders had to navigate their companies through momentous change, from the great financial crisis to the pandemic. The months and years ahead do not promise an easy ride; the ongoing geopolitical tensions and economic challenges will likely require corporate leaders to display vision and decisiveness. They may be expected to inspire their organizations to embrace change in a way that opens new strategic possibilities and inspires trust.

The importance of M&A as an enabler of change has been demonstrated by the record-breaking activities during one of the most difficult times in business history. Looking ahead, we demonstrate by the record-breaking activities during one of the most difficult times in business history. Successful companies will meet new expectations and conditions. Successful companies will require corporate leaders to display vision and decisiveness. They may be expected to inspire their organizations to embrace change in a way that opens new strategic possibilities and inspires trust.

Endnotes

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