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# The Deal in Focus

Heads of M&A survey 2022



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## Foreword

After experiencing an extraordinarily robust M&A market in 2022, M&A leaders in Australia and New Zealand are now facing a very different outlook.

This fifth edition of our annual survey of corporate heads of M&A, which includes responses from New Zealand for the first time, acknowledges significant economic and geopolitical challenges facing Australia and New Zealand. Nevertheless, survey respondents are upbeat about their M&A prospects, with more than 8 out of 10 predicting that the number of transactions will increase or stay stable over the next 12 months. This is despite signs that the market is moderating from the phenomenally high deal volumes experienced in 2021. So much for battenning down the hatches!

Acquiring assets to fill gaps in the core portfolio is a priority for 80% of respondents over the next 12 months – the highest share seen for any M&A objective. The same percentage of leaders indicate that the valuation of assets will be their greatest test.

While continued M&A activity is expected, the market is evolving. Expedited synergy capture on recently completed deals is on the minds of more respondents this year than in 2021. This is because businesses are looking to deliver on the initial deal thesis, which underlines the importance of being integration ready.

This year's results also reveal that environmental, social and governance (ESG) factors are increasingly important for successful

M&A deals, with 63% of respondents factoring ESG impacts into their decision-making all of the time or most of the time, up from 52% in the 2021 survey. ESG has also become an influencer in portfolio rebalancing and redesigning, with almost 50% of respondents re-evaluating or planning to re-evaluate their portfolio to acquire or divest through the lens of ESG, including energy transition commitments. Quantifying the value of ESG in a deal is the biggest challenge. We expect this to be a major point of discussion in the year ahead.

With an eye to the next 12 months, there will still be a deep pool of money available for good quality M&A targets. Companies are looking to grow and can draw on significant cash reserves and debt markets to get deals done.

Of course, potential market disruption and economic trends will need to continue to be reviewed and managed, including the impact of changing consumer demands, supply chain risks, and higher interest rates and inflation. As M&A practitioners, we remain optimistic that the glass will remain half full – so notwithstanding the headwinds, we anticipate continued opportunity. The key question to consider for corporate heads of M&A is 'are you a prepared acquirer?' This will help you identify and realise those M&A opportunities which will create value and avoid those that will not.

## About the survey

**The Deal in Focus** is a powerful way to bring together Heads of M&A from corporate Australia and New Zealand with leading Deloitte experts into one community.

The information in this annual survey is compiled from interviews with business leaders involved in M&A, as well as insights gathered from Deloitte Access Economics and the views of the leading experts in our M&A practice.

Interviews were conducted from 9 May 2022 to 10 June 2022. Chart 1 shows the industry breakdown of the organisations included in the interviews. Chart 2 shows the location breakdown of interviewed firms.<sup>1</sup>

Chart 1  
**Industry breakdown of interviewed firms**

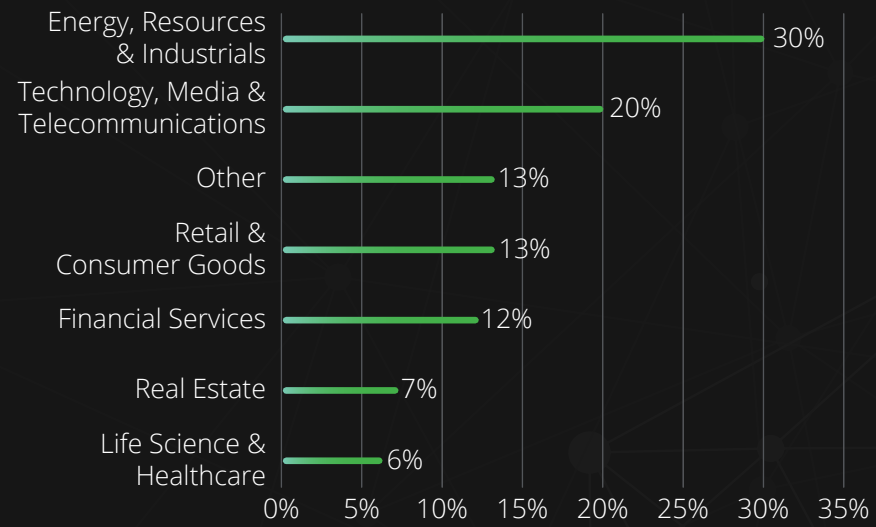
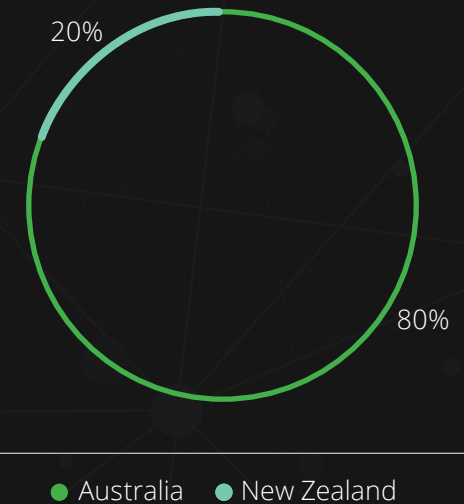


Chart 2  
**Location breakdown of interviewed firms**



<sup>1</sup> Comparisons are made to previous years' surveys in this report, noting that there are changes to the sample of survey respondents over time. The survey includes respondents from New Zealand this year for the first time.

## Key insights

**83%**

83% of respondents expect the number of deals to increase or remain stable in the next 12 months.

**40 to 51%**

Expediting synergy capture has increased as a priority over the 12 months from 40% in the previous survey to 51% in the current survey.

**80%**

80% of respondents listed valuations as the greatest challenge to M&A success.

**46%**

46% of respondents are not confident that the economy will continue to recover and thrive, but 89% are at least moderately confident that credit will be available at favourable conditions.

**50%**

Almost 50% of respondents are re-evaluating or planning to re-evaluate their portfolio to acquire or divest through the lens of ESG, including energy transition commitments.

**46%**

46% of respondents see accelerating digital transformation as an M&A priority in the next 12 months, with 74% identifying customer experience as the key area of focus for digital transformation.

## Macroeconomic outlook

M&A activity is influenced by a range of macroeconomic factors including economic growth, financial conditions, and prevailing sentiment.

The Australian and New Zealand economies have recovered rapidly from the initial effects of COVID-19, but the outlook is clouded by a range of global uncertainties. Inflation has increased, supply chain disruptions have taken longer than expected to unwind, and Russia's invasion of Ukraine has elevated energy and food prices.

Central banks have responded with faster than expected interest rate rises. While this is an appropriate response to inflation that remains above target, it hurts asset prices, and puts pressure on business and household budgets.

Inflationary pressures are more muted in Australia compared to other developed economies, including New Zealand.

Headline inflation is expected to peak in 2022 in both Australia and New Zealand, before starting to moderate thereafter. Indeed, some of the global drivers of inflation are starting to subside. Several key international prices, such as oil, will not continue to move higher at the same rate in the future, and in fact have started to fall. There are also signs that supply chain constraints are easing. For example, semiconductor prices have started to ease, and global car production is picking up. Deloitte Access Economics' view is that inflation is likely to correct at a reasonable pace over the next 18 months.

Policymakers around the world face a complex task in containing inflation without causing a hard landing. The COVID-19 period led to a large build-up in debt across both Australia and New Zealand. This means that interest rate increases today weigh more heavily on the economy than in the past. At the same

time, the large stock of savings accumulated during the pandemic means that Australian households are relatively well positioned to cope with rising interest rates.

The economic recovery is expected to slow in 2022 in both Australia and New Zealand, but the growth outlook remains positive. In the near-term, activity will be constrained by elevated inflation, rising interest rates, and relatively weak consumer and business confidence. However, consumption will be supported by tight labour markets and savings accumulated during COVID-19. Employment growth is expected to remain strong and the outlook for business investment is solid.

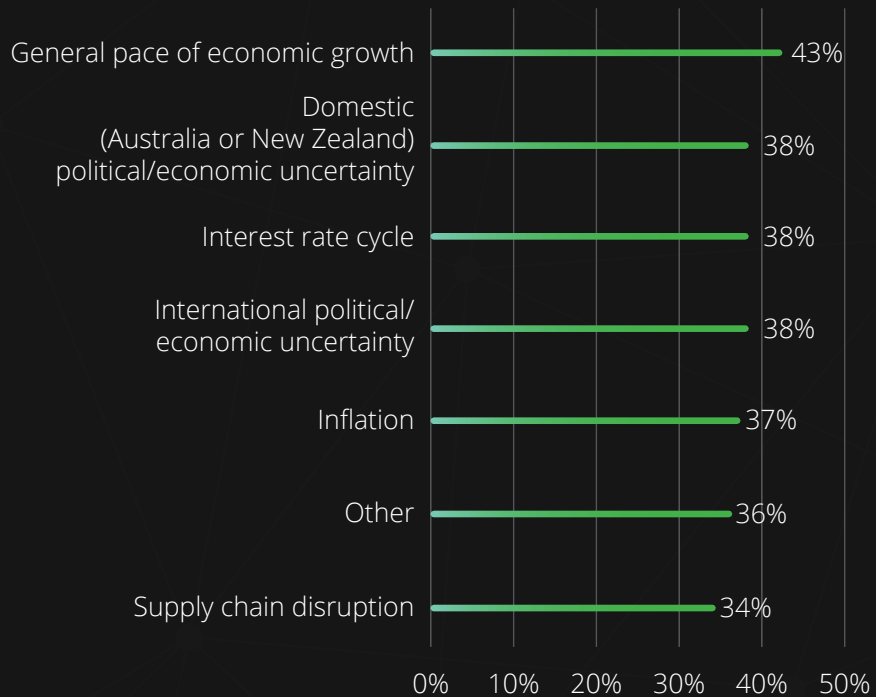
Key risks to the outlook include potential new COVID-19 variants, a sharper-than-expected slowdown in the Chinese economy, inflation that remains higher for longer, and persistent supply chain disruptions.

The continually evolving economic outlook has made the M&A outlook somewhat more challenging. Shot selection will become even more important, value chains will need to be deeply understood and longer transaction timetables should be anticipated as valuation expectations are managed.

The general pace of economic growth was cited as the most significant economic factor affecting the ability to successfully execute deals. This was above the shares seen for other economic concerns such as supply chain disruptions, high inflation, rising interest rates and policy uncertainty.

Chart 3

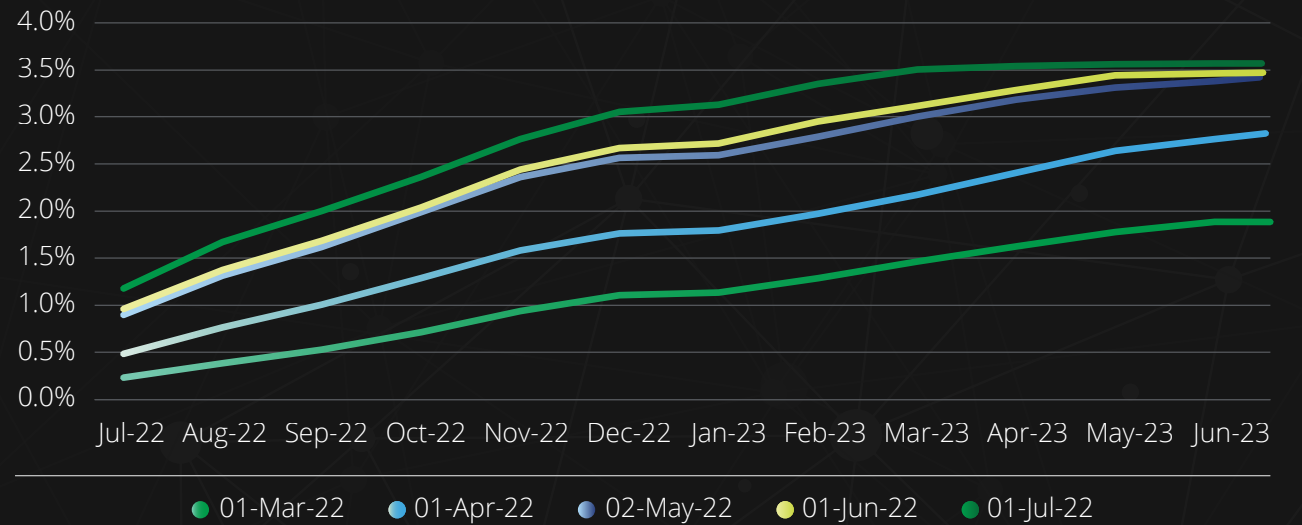
**What are the economic factors that affect your ability to successfully execute deals?**



Note: respondents were able to select all options that apply.

Chart 4

**Expected cash rate**



Source: Refinitiv

Uncertainty around the timing and scale of interest rate increases makes it harder to determine whether a deal is good value, as demonstrated by the evolution of expectations for the Australian cash rate in chart 4. This comes after an extended period

in which the supply of good quality assets has not kept up with demand. That said, the outlook may be improving, with 75% of respondents highly or moderately confident that targets will be available at attractive valuations over the next 12 months.

## What's ahead for 2022-23?

The share of respondents who expect the number of deals their organisation pursues will increase over the coming months has declined from 58% in 2021 to 44% in 2022. And although almost 2 in 10 respondents believe the number of deals they pursue will drop in the coming year, this partially reflects the staggering volume of transactions we saw in 2021.

The shadow cast by current risks over the economic outlook is understood by M&A leaders surveyed. A total of 46% of those surveyed are not confident that the economy will continue to recover and thrive over the next 12 months. Despite the weaker economic outlook and rising interest rates, a high

proportion of respondents are confident there will be growth opportunities in their sector and, to a slightly lesser extent, that credit will be available at favourable conditions. Almost 80% of respondents believe that current economic conditions are supportive of M&A activity.

A majority (52%) of respondents expect the size of deals to increase over the next 12 months and 74% are highly confident their balance sheets are strong.

Chart 5

**Are you expecting the number of deals that your organisation pursues to increase or decrease over the coming 12 months?**

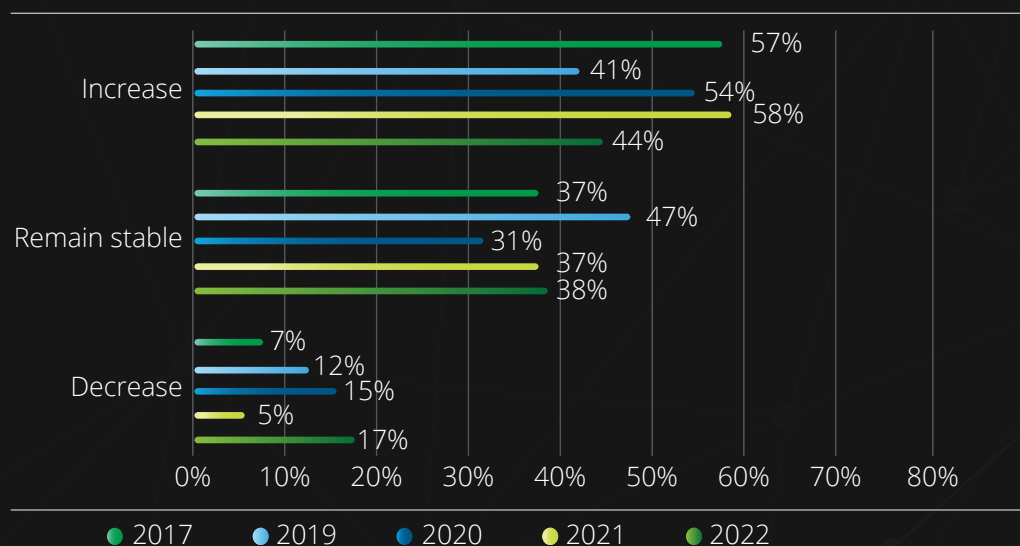
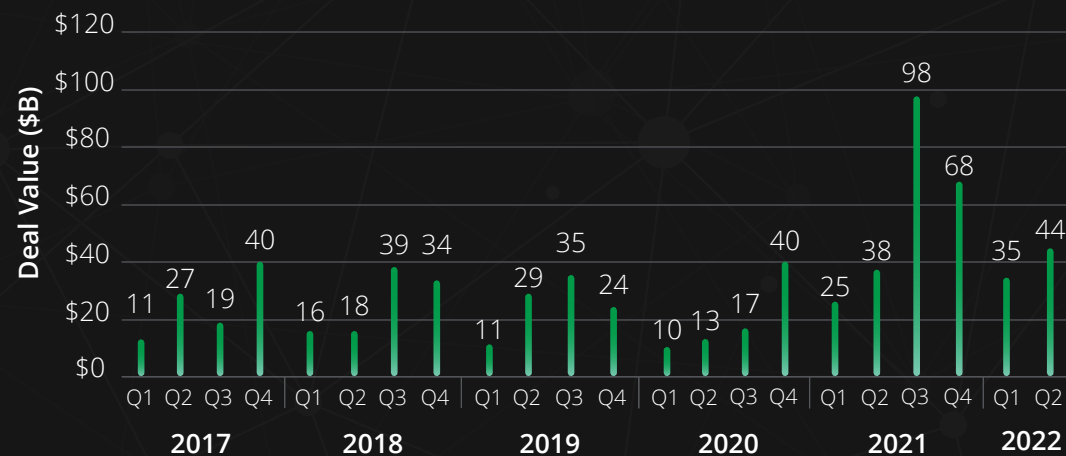


Chart 6

**Australia & New Zealand M&A activity (Announced in billions of US dollars)**



Source: Refinitiv and Deloitte analysis



Chart 7

**How confident are you of the following factors that could influence your M&A decision over the next 12 months?**

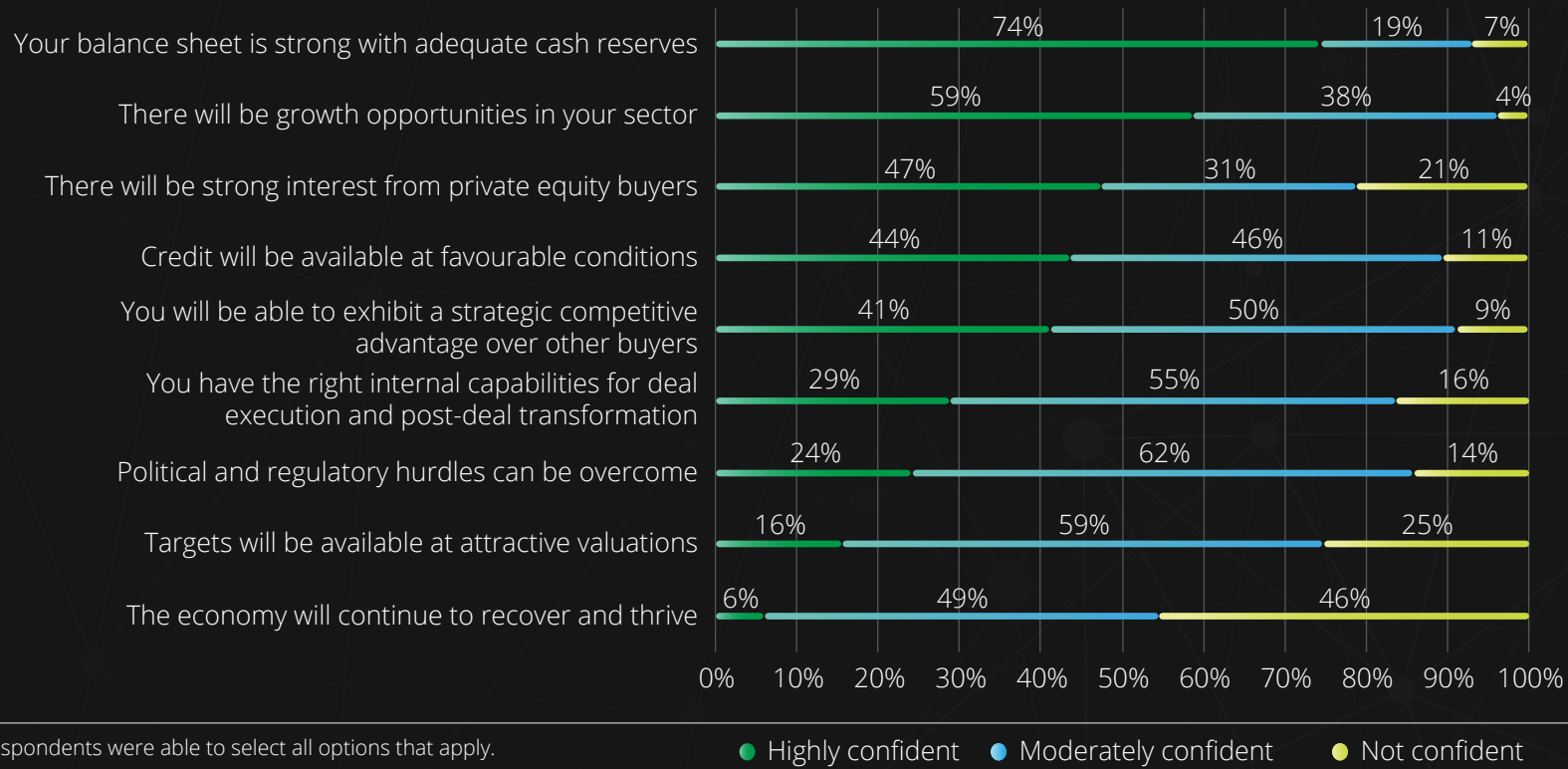
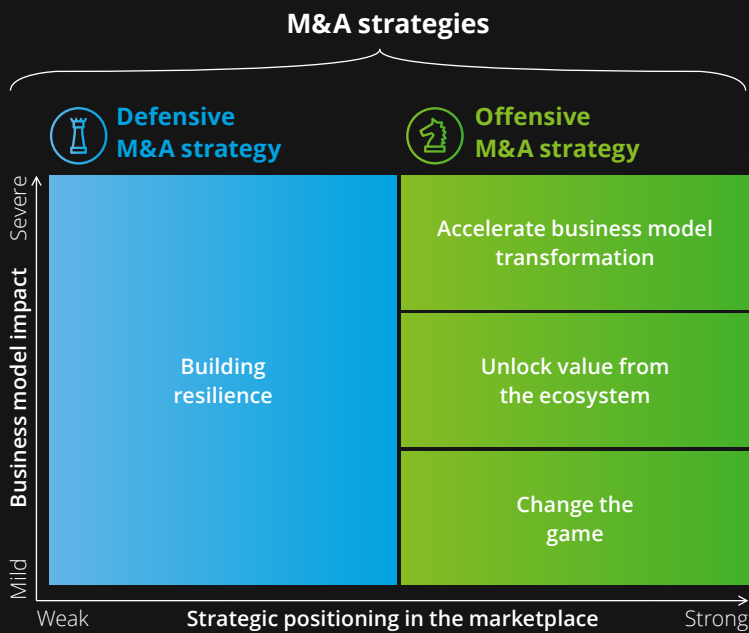








Chart 8  
**Charting new horizons M&A framework**



### Building a resilient company

-  Accelerate synergy realisation from recent deals, evaluate your current portfolio, and divest assets that are not aligned to long-term growth.
-  Optimise your portfolio and strengthen your core by acquiring competitors to consolidate the marketplace.
-  Consider opportunistic deals to secure your supply chain systems, safeguard your customer channels, and enhance market positioning.

### Charging the growth engine

-  Transform your business model by acquiring value-enhancing products and capabilities. Identify portfolio gaps, and consider expanding towards market adjacencies through acquisitions in digital, ESG, and platform plays.
-  Capture opportunities through purpose-led alliances and partnerships involving non-traditional peers and scale-ups from the ecosystem.
-  Invest in disruptive innovation assets to scale at the 'edge.'

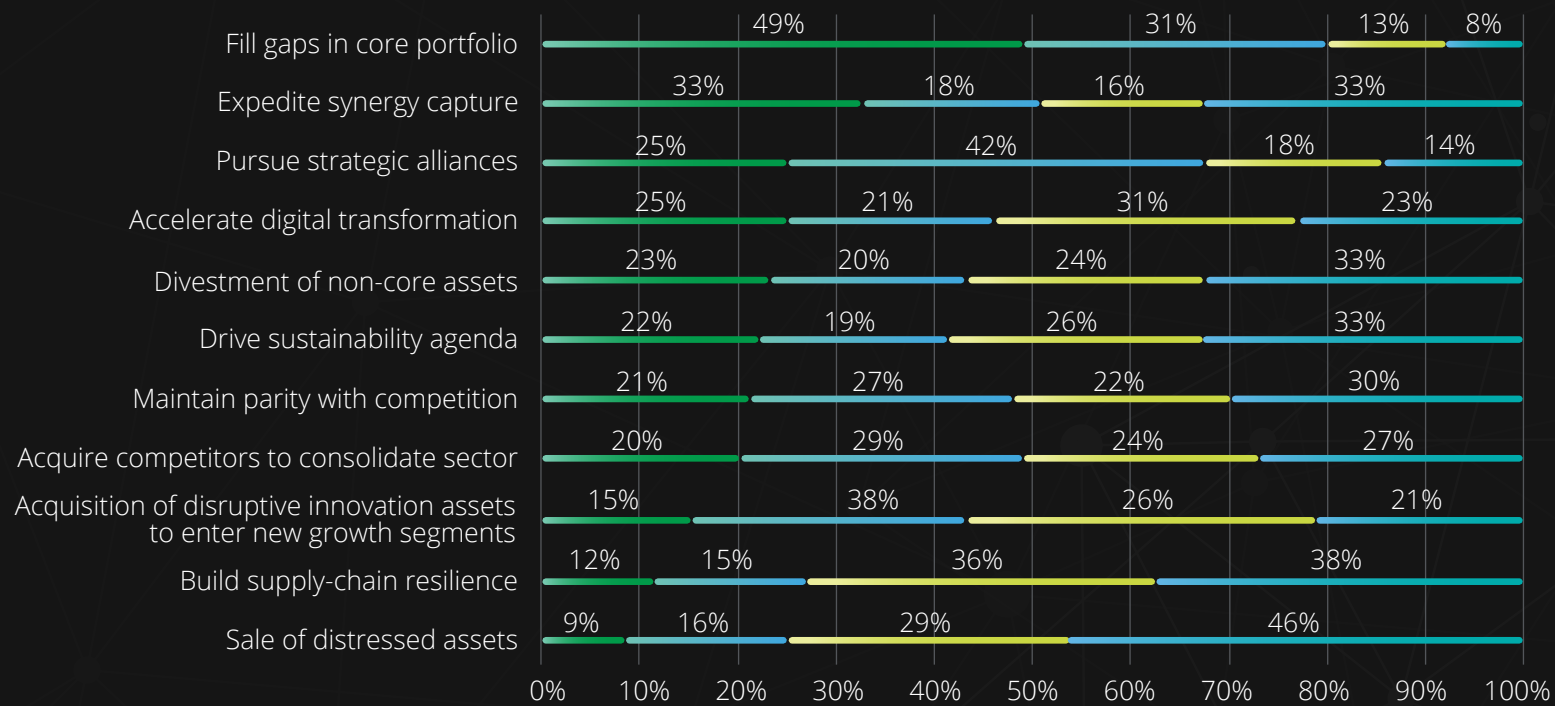
**Business model impact:** Consider the impact of the post-pandemic structural changes on your employees, customers, suppliers, and operating model.

**Strategic positioning in the marketplace:** Consider your liquidity position, balance sheet strengths, ability to raise capital, competitive environment, threats of disruption, and drivers of competition in the marketplace.

As M&A leaders navigate the 'new normal' market conditions, Deloitte believes M&A will continue to be a fundamental part of the corporate arsenal, helping businesses build their resilience and withstand evolving economic conditions while also accelerating business transformation (as outlined in chart 8 from [Charting new horizons 2022](#)).

Chart 9

**To what extent are the following M&A objectives a priority for your company?**



Note: respondents were able to select all options that apply.

● Highly confident ● Confident ● Moderately confident ● Not confident

The strength of existing balance sheets and the economic outlook are shaping M&A priorities. The majority of the priorities over the next 12 months reflect defensive strategies to build the resilience of the organisation, with the highest M&A objective being the acquisition of assets to fill gaps in the core portfolio at 80% compared to the prior year of 65%. Interestingly, this focus on protecting and nurturing core business was also identified as a top priority for strategy executives in Deloitte's [2022 Chief Strategy Officer Survey](#).

Expediting synergy capture has also increased as a priority over the next 12 months from 40% in the previous survey to 51% in the current survey, reflecting the importance of realising the value from deals completed in the past year.

Despite the uncertain global economic outlook, 54% of respondents considered cross-border M&A transactions in the previous year, down only slightly from 58% in last year's survey. The Asia Pacific region remains the most attractive geography for acquisitions, and facilitating entry into new markets is the key driver of interest in foreign targets.

Chart 10

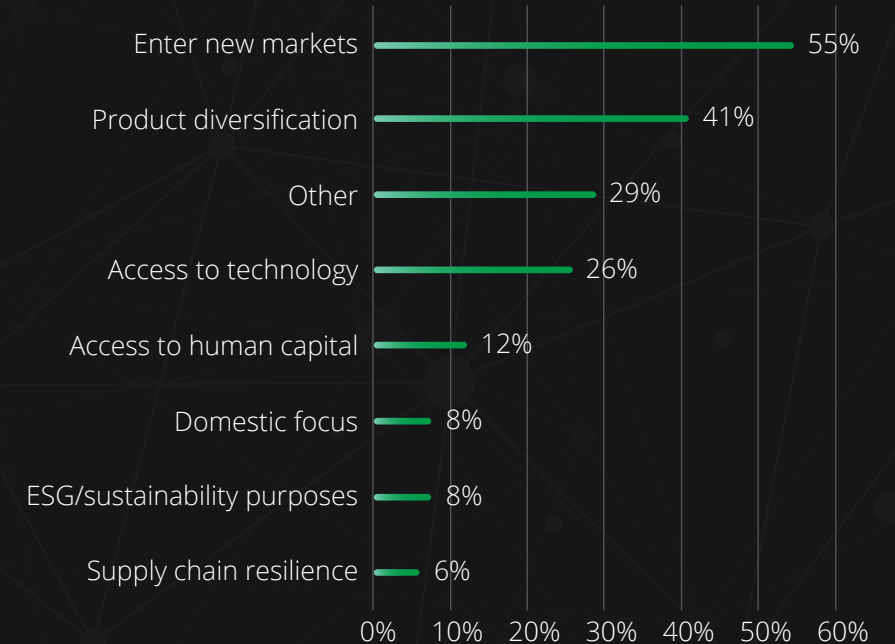
**Top 3 M&A objectives by sector**

	High priority (<6 months)		Medium priority (6-12 months)
Energy, Resources & Industrials	Fill gaps in core portfolio	Drive sustainability agenda	Divestment of non-core assets
Financial Services	Expedite synergy capture	Fill gaps in core portfolio	Pursue strategic alliances
Life Science & Health Care	Fill gaps in core portfolio	Acquire competitors to consolidate sector	Accelerate digital transformation
Retail & Consumer Goods	Fill gaps in core portfolio	Accelerate digital transformation	Drive sustainability agenda
Technology, Media & Telecommunications	Accelerate digital transformation	Fill gaps in core portfolio	Expedite synergy capture
Real Estate	Fill gaps in core portfolio	Expedite synergy capture	Divestment of non-core assets

● Defensive M&A strategy ● Offensive M&A strategy

Chart 11

**If you are considering cross-border M&A transactions in calendar 2022, what is driving your organisation's interest in foreign targets?**



Note: respondents were able to select all options that apply.

## Differences across the Tasman

The views of M&A survey participants were broadly consistent across the Australian and New Zealand markets. The most notable differences in responses included:

- Almost 50% of Australian respondents are expecting an increase in the number of deals compared to last year whereas the majority of New Zealand respondents expected deal activity to hold broadly constant.
- New Zealand respondents did not expect there to be as many growth opportunities within their existing sectors as their Australian peers.
- Australian respondents were more optimistic on the broader economic outlook.
- New Zealand respondents expected the divestment of non-core assets to feature more prominently in M&A than Australian respondents.
- New Zealand respondents are looking more at alternatives to traditional M&A (alliances, joint ventures) than Australian respondents.

Chart 12

**Are you expecting the number of deals that your organisation sees or pursues to increase or decrease over the coming 12 months?**

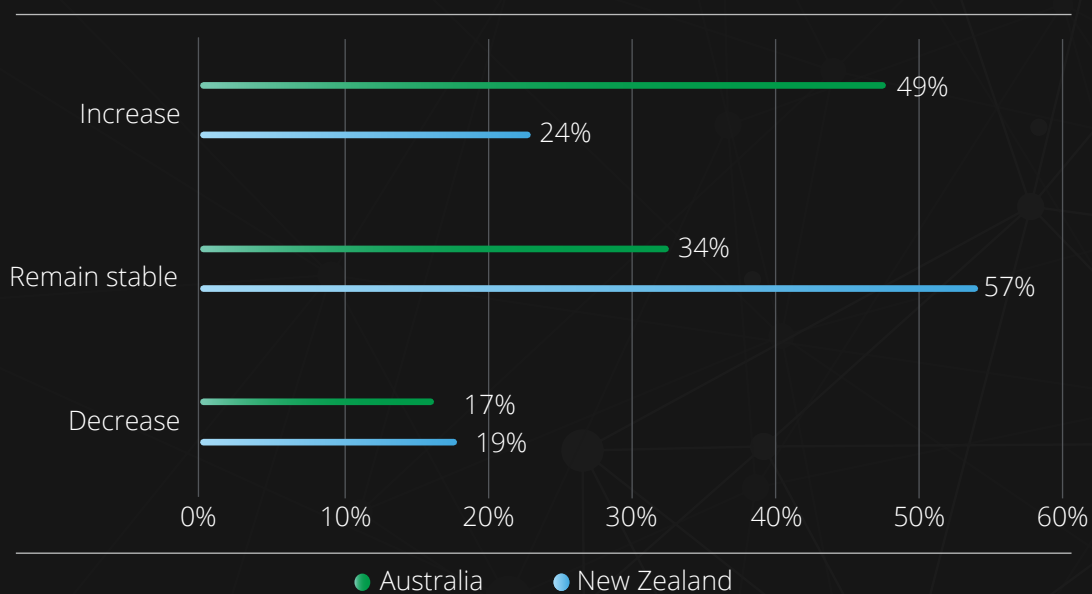


Chart 13

To the extent that your company is currently pursuing transactions, which of the following are you most interested in exploring?

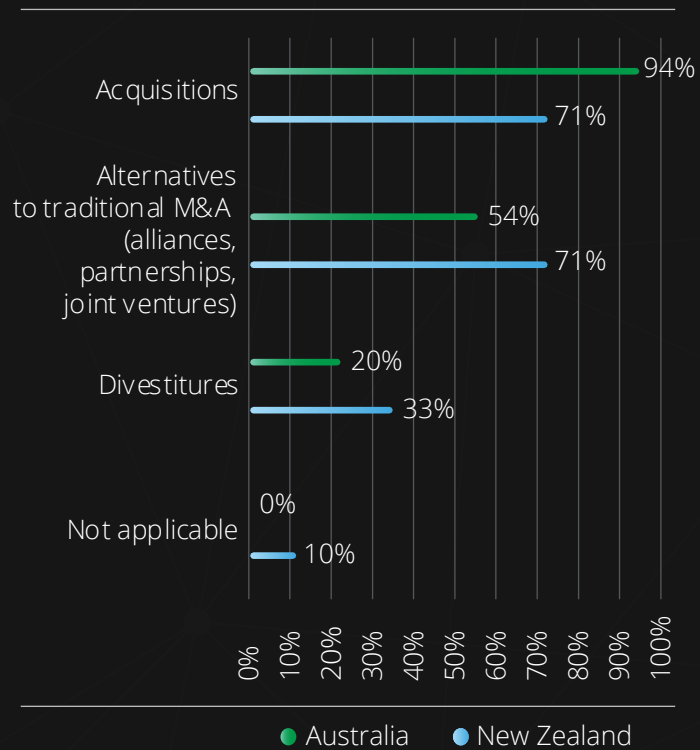
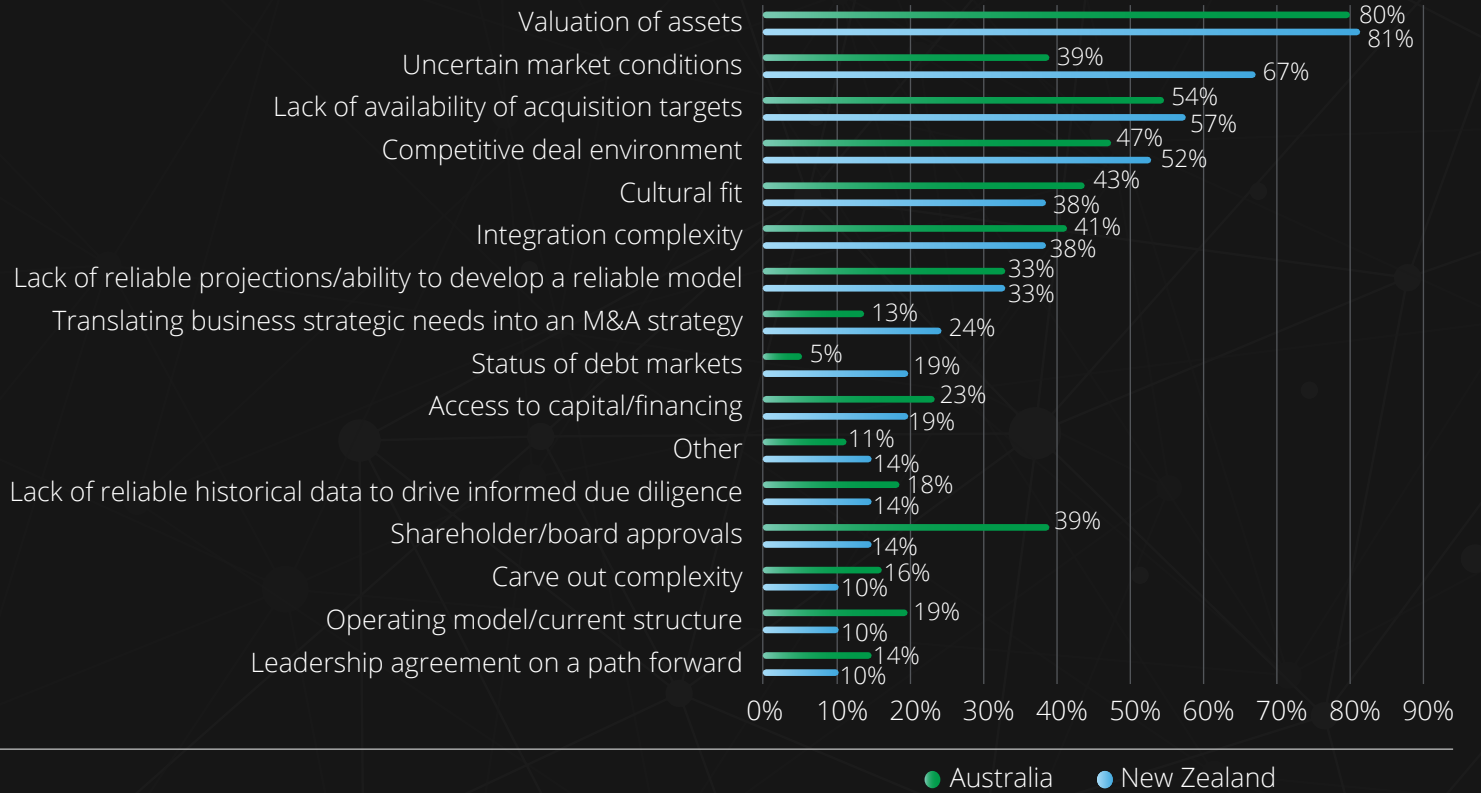
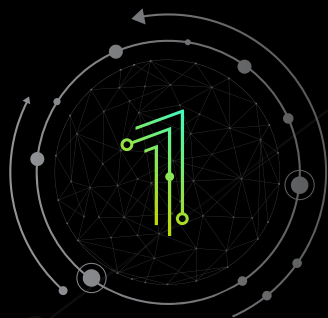


Chart 14

In the current economic environment, what is your company's greatest challenge to M&A success?



## Key themes summary



### **The M&A future looks bright, but valuation is the biggest challenge**

Corporates are looking to grow the core or accelerate transformation, but the uncertain economic outlook makes valuation a challenge, which may affect the speed of the transaction process.



### **Delivering on the deal**

The competitive deal environment over the past two years has increased the focus of corporates on delivering the deal thesis, highlighting the importance of integration and the realisation of synergies.



### **Accelerating business transformation**

Several corporates have identified M&A as an accelerator to transform their business model, be it digital transformation, driving the sustainability agenda or pursuing strategic alliances to access new markets and adjacencies.



### **Why scenario planning has never been more important**

M&A can serve as a catalyst for companies to combat disruption, which in turn can enable business growth and reduce operational costs.



### **Spotlight on ESG shows no signs of dimming**

Companies are increasingly incorporating ESG factors into M&A deals, but valuing the ESG component remains complicated.

## **Theme 1 – The M&A future looks bright, but valuation is the biggest challenge**

In a strong show of confidence, 83% of survey respondents said that they expected M&A deals to rise or stay stable in the year ahead. Though economic clouds are looming, this indicates that the strong run of deals is far from over.



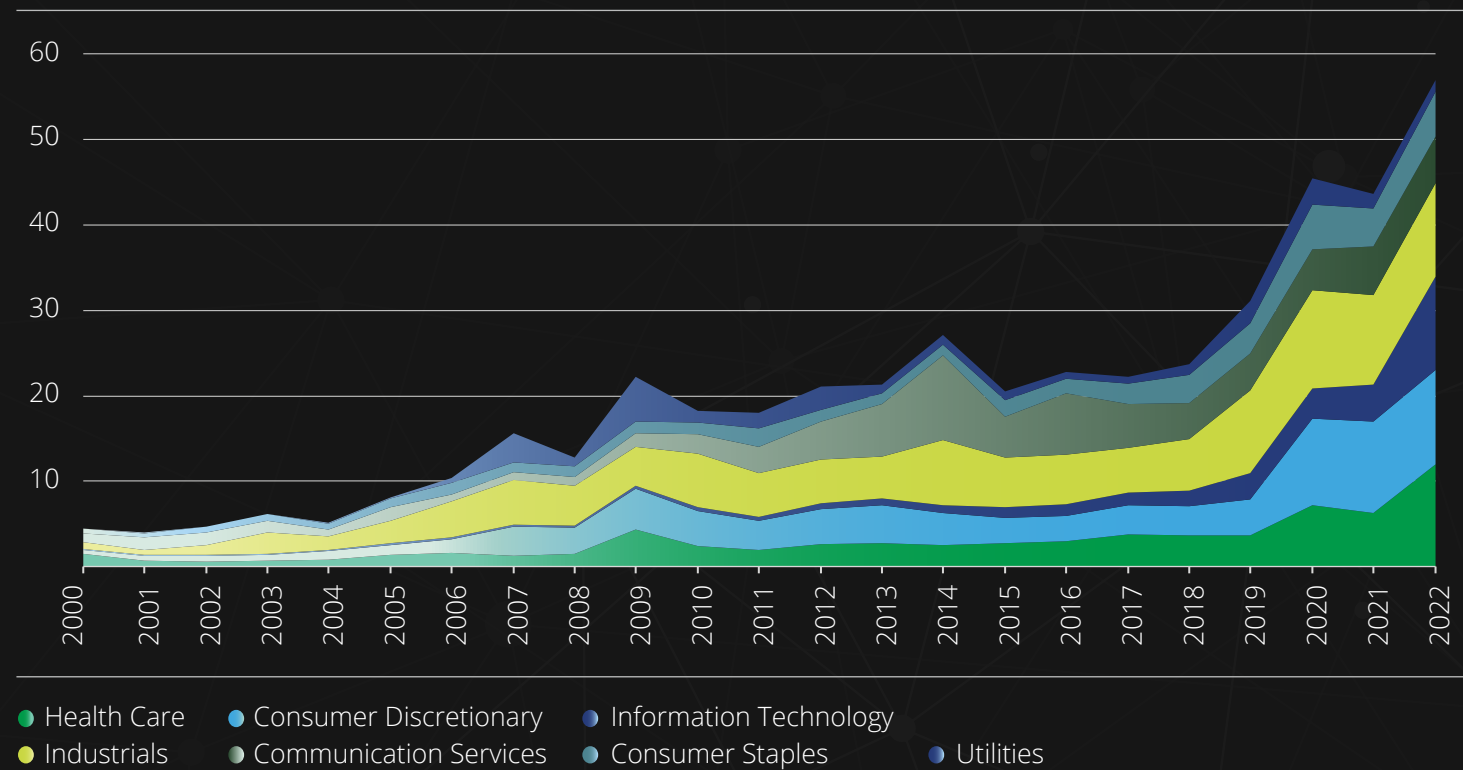


## Outlook

The Australian and New Zealand economies are facing a number of challenges including inflationary pressures, interest rate hikes, supply chain resilience and valuation volatility. But there are also some strong tailwinds for M&A, with large cash reserves on balance sheets (refer chart 15), plenty of private equity dry powder and strong debt markets (with the rise of alternative lenders as interest rates increase).

Chart 15

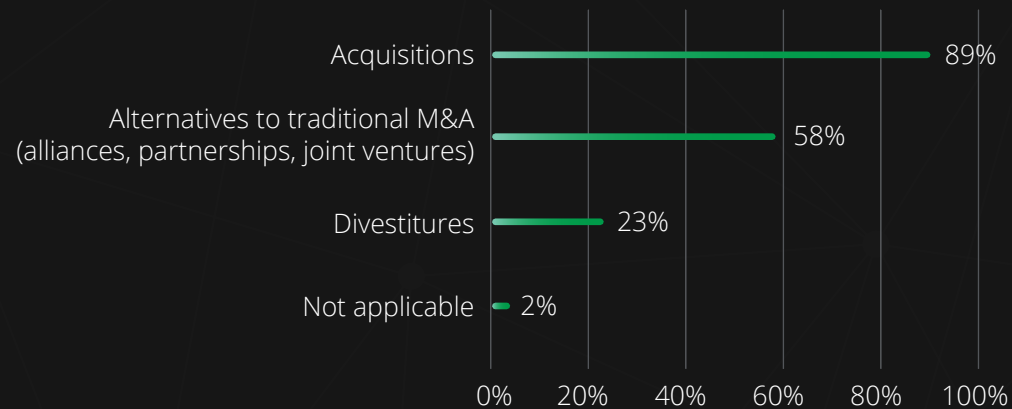
### Reported cash holdings S&P/ASX 200 (\$B)



Source: Capital IQ, Deloitte analysis. Excluded companies in the Financial, Real Estate, Energy and Materials sectors (only considers reported cash balances).

Chart 16

**To the extent that your company is currently pursuing transactions, which of the following are you most interested in exploring?**



Note: respondents were able to select all options that apply.

Deals may be harder and take longer to execute, but impressive volumes are still likely. The priority for many will be to acquire assets at the right price to fill gaps in core portfolios.

Acquisitions remain highly attractive to M&A leaders despite concerns over elevated valuations. A total of 89% of respondents who are currently pursuing a transaction, are interested in acquisitions, compared to 23% for divestitures, and 58% for alternatives such as alliances, partnerships and joint ventures.

#### **Divestitures are less of a priority in 2022**

There is muted appetite for divestments with almost 60% of respondents reporting that restructuring their portfolio and divesting non-core assets isn't a priority over the next 12 months. This may reflect the fact that 51% of respondents undertook one or more divestitures in 2021.

89% of respondents who are currently pursuing a transaction, are interested in acquisitions.

### Challenges to M&A success

80% of those surveyed listed the valuation of assets as a challenge to M&A success, 55% of respondents identified a lack of available acquisition targets as a key challenge, and 48% noted that the competitive deal environment is affecting their ability to successfully execute deals.

Most respondents also noted that their leadership agreed on the path forward, pointing to alignment among M&A leaders and the ability to translate M&A into growth strategy.

When valuing a target there are several factors to which M&A leaders are paying close attention. Almost 60% of those surveyed expect customer demand to have a positive impact on deal value over the next 12 months, while 74% expect cost inflation to have a negative effect, and approximately 50% expect interest rates and the cost of capital to have a negative effect.

Chart 17

**What factors are you likely to be particularly cognisant of when valuing a target in the coming 12 months and how do you expect them to impact on value?**

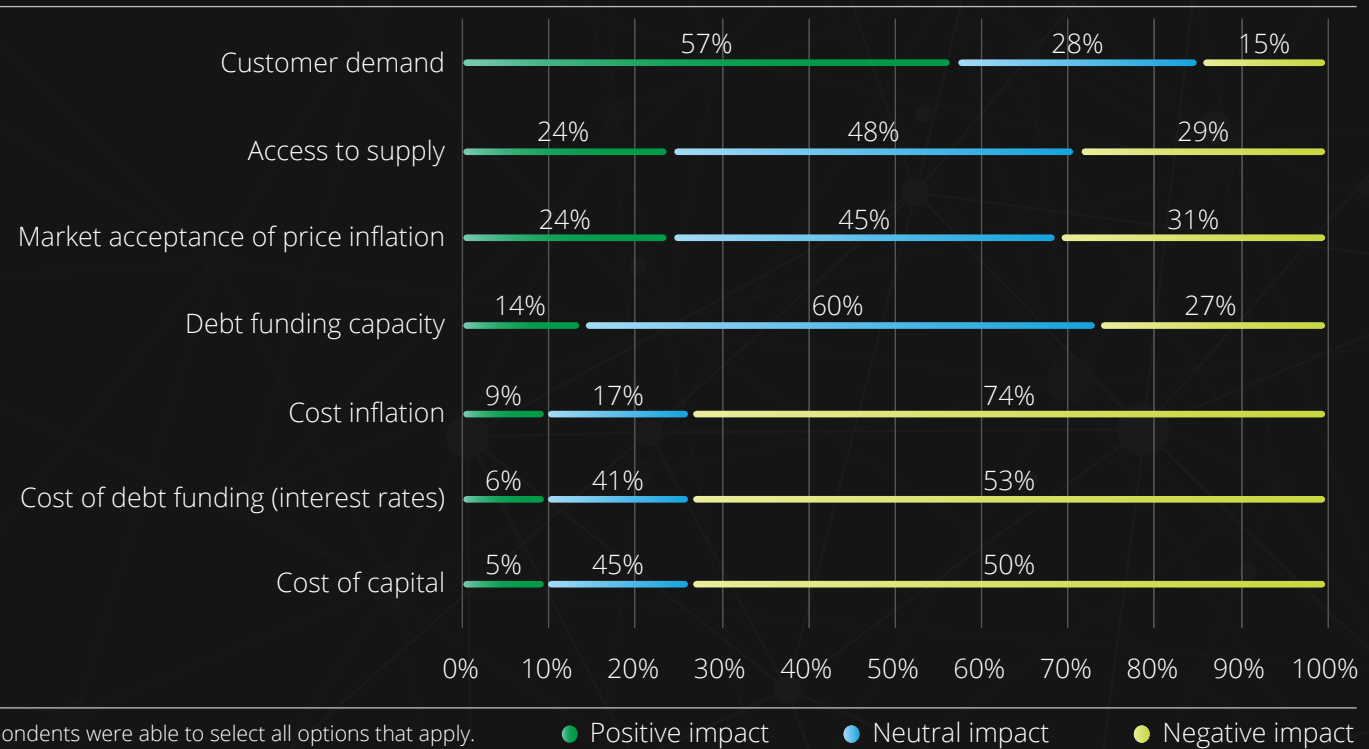
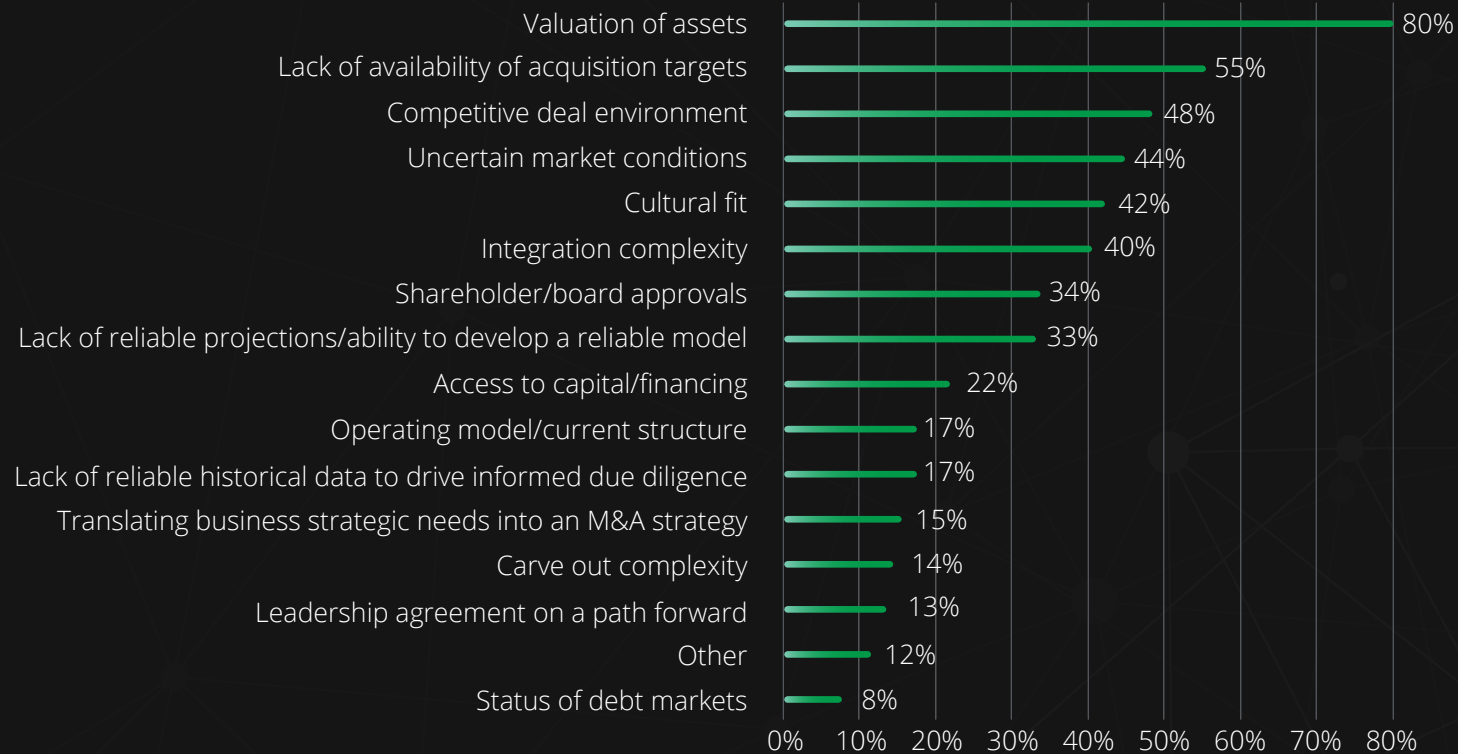


Chart 18

**In the current economic environment, what is your company's greatest challenge to M&A success?**



**Valuations challenging**

With low interest rates contributing to high M&A volumes in 2021, all eyes will be on the impact of rate hikes in 2022. Continuing availability of debt seems likely, but there is little doubt that higher borrowing costs could affect deal valuations.

The survey reveals that 80% of respondents believe the valuation of assets will be their greatest challenge in 2022 and 2023. This confirms market sentiment in the current environment.

The flip side is that rising interest rates should create M&A opportunities for companies with strong balance sheets. Despite borrowing costs inevitably increasing, M&A leaders should be able to access assets in a less competitive environment and at reasonable prices.

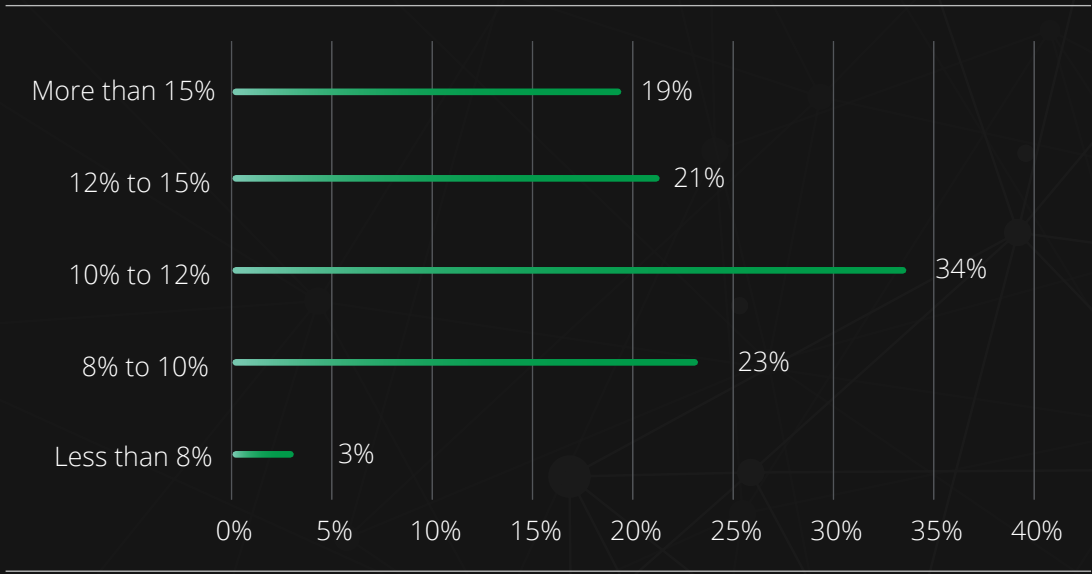
Our surveys were undertaken during an unusually volatile period for the Australian and New Zealand market.

A total of 40% of respondents are targeting a hurdle rate of more than 12% and only 3% are targeting a rate of less than 8%.

It is interesting to note that a decreasing number of respondents were using hurdle rates lower than 8% while an increasing number were using rates greater than 15%. With an uncertain environment and recent volatility, it is not unusual to see that uncertainty factored into 'buffers' which push hurdle rates higher. However, higher hurdle rates may also reflect expectations of future increases in the cost of capital.

Over time, we expect a greater focus on understanding the impact of these risks on future cash flows and greater diligence on the underlying drivers such as customer demand and sustainability of margins. This should see a reduction in any attempts to mitigate these risks through the use of 'buffers' in hurdle rates.

Chart 19  
**What equity hurdle rate do you target?**



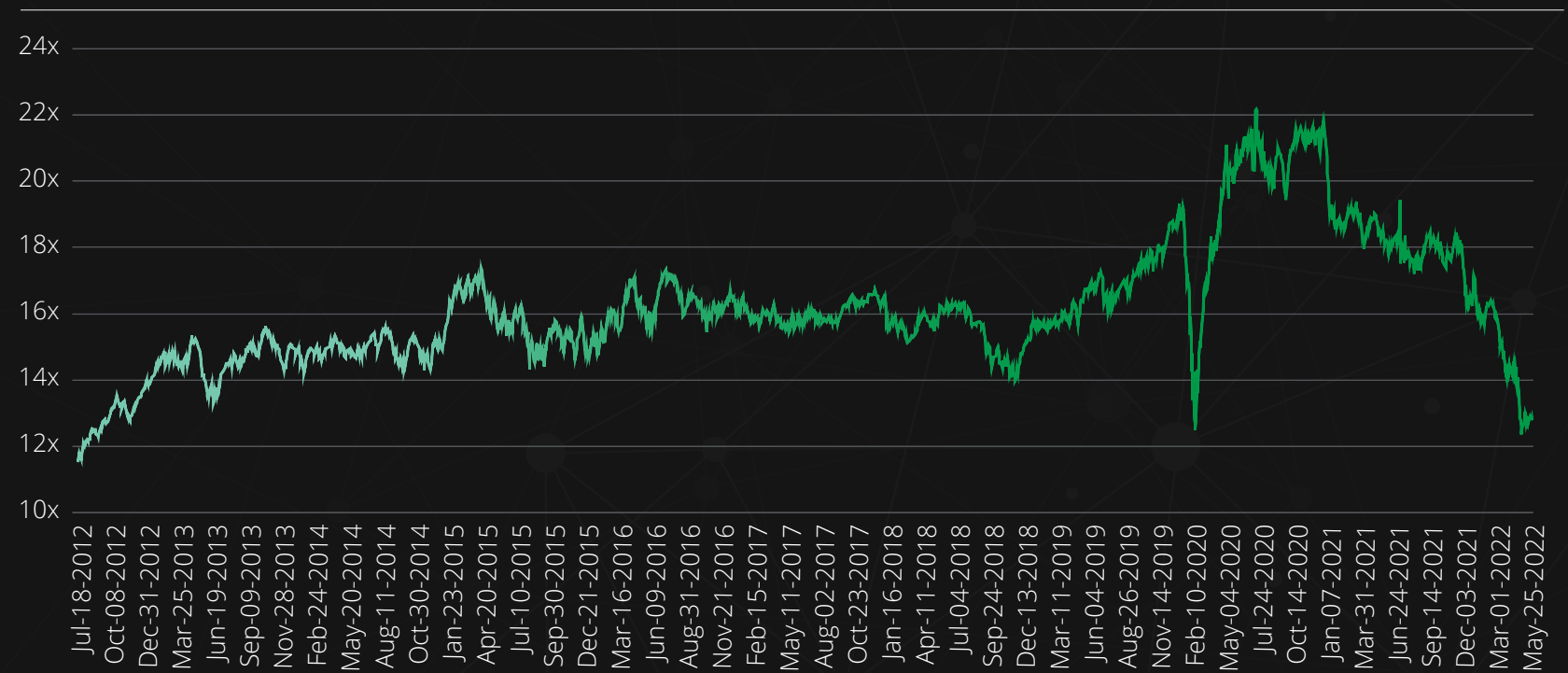
With higher than anticipated inflation and the Reserve Bank of Australia's response through larger interest rate increases, the valuation multiples of the ASX have come down substantially on a headline basis.

However, it's important to recognise that more recently, and somewhat counter-intuitively, the P/E multiple of the S&P/ASX 200 index has been influenced by the strong short to medium-term earnings levels of companies in the resources sector that weigh heavily on the index.

Equally, the greatest negative re-rating in the market has been in respect of companies in the information technology sector while companies in the utilities and consumer staples sector have experienced much lower negative ratings.

This only goes to highlight some of the findings of the survey which indicate that the current volatility and economic environment are not equal for all and there will be winners and losers from the current re-rating.

Chart 20  
**S&P/ASX 200 index price to earnings multiple**



Source: Capital IQ, Deloitte analysis

An aerial photograph of a coastal city. On the left, a wide, sandy beach meets the ocean. To the right, a dense urban area features a mix of buildings, including several tall, modern high-rise apartment complexes and smaller residential structures. The city is interspersed with greenery and palm trees. The overall scene is captured from a high angle, looking down at the city and beach.

## Theme 2 - Delivering on the deal

Organisations are more complex than ever, and so are integrations. Delivering cost synergies is now par for the course – to succeed in this competitive landscape, M&A leaders must identify integration risks and opportunities earlier and get more technologically and culturally sophisticated in the delivery of deal value.

## Going for growth

High valuations in recent years have affected M&A execution priorities, driving an increased focus on profits and deal synergies. A majority of respondents (51%) listed expedited synergy capture on recently completed deals as a priority over the next 12 months. This is up from the 40% of respondents that listed synergy capture as a priority in the 2021 survey.

When a possible target does emerge, it is important that organisations are 'integration-ready'. M&A leaders should be ready to mobilise quickly to harvest the returns of the deal thesis and synergy targets to ensure the transaction is accretive for shareholders.

Diligence therefore not only needs to understand risks and how such risks will be managed, but also to identify and validate growth synergies.

In the past, companies were often reluctant to price in M&A cost synergies, typically preferring to instead recognise cost synergies as 'additional upside'. Things have changed. Now, cost synergies such as headcount reduction and harmonisation of procurement contracts are par for the course.

Truly 'integration-ready' organisations have embedded the thinking and people responsible for executing on the integration early in the deal process. A clearly articulated, well-considered deal thesis, or business case,

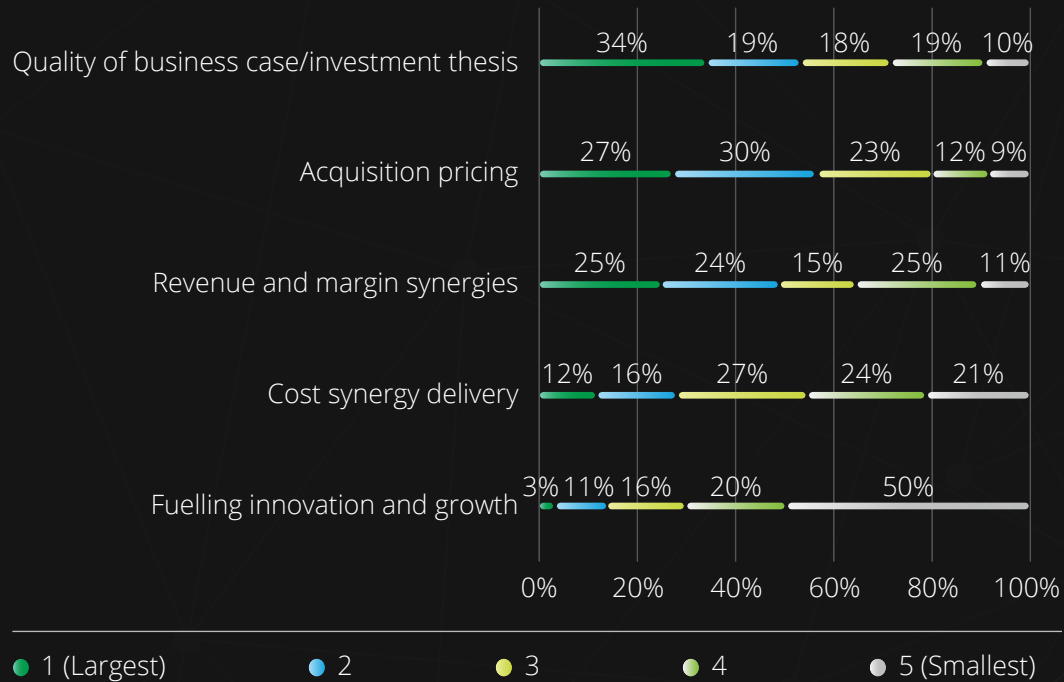
is fundamental to deal success. It provides the integration team and broader organisation clarity on the purpose of the deal and how the two organisations will come together over time.

Its importance is underscored when considering most M&A leaders conduct post-acquisition reviews (35% conducting reviews after 100 days, 6 months and 12 months), and 34% citing quality of the business case as the biggest challenge to delivering on acquisition returns, 27% citing acquisition pricing, and 25% noting revenue and margin synergies. Few respondents found fuelling innovation and growth a challenge in delivering on business case returns.



Chart 21


**What do you think is the biggest challenge in delivering on acquisition business case returns?**



**Culture can determine (or derail) the ultimate success of a deal**

Today, some integration failures are attributable to culture: that is, not recognising cultural differences and bringing both cultures together to deliver on the strategic intent of the deal. It is clear that culture and value upside are connected, and organisations need to win hearts and minds to realise the value that delivers on the deal thesis.

Ultimately, culture comes down to leadership; it is well understood that when there is good definition and articulation of purpose, organisations will attract and retain more people. A strong culture puts you in a better position to execute on transactions, to deliver synergies and to work on integration opportunities. You must be able to articulate why the divestment or acquisition is important to the organisation, and how it helps fulfil a wider purpose.

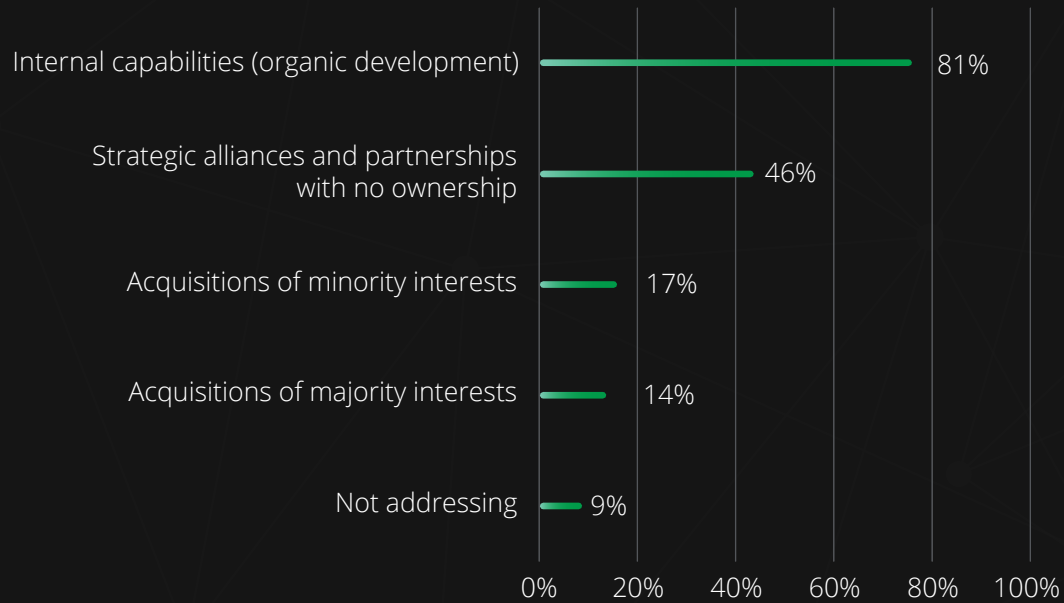
A city skyline at sunset, featuring a prominent tower and various skyscrapers. The scene is overlaid with a network of white lines and dots, suggesting digital connectivity. The sky is a mix of orange, yellow, and grey, with the sun low on the horizon. The foreground shows a marina with many boats and some residential buildings.

### **Theme 3 - Accelerating business transformation**

Most businesses understand that they need to embark on their digital transformation journey – the question is, what does transformation look like for you and how will you do it. A holistic approach is required, along with clarity about what the end goal looks like.

Chart 22

**In relation to digital transformation of your business, are you addressing this through**



Note: respondents were able to select all options that apply.

The survey results indicate that about four out of five respondents plan to use internal capabilities, while a small proportion are considering acquisitions (of majority or minority interests). The former approach depends on acquiring and keeping the right talent within the business, which is not easy in the current environment.

So, what does transformation look like for a business, digital or otherwise? It covers the full tech stack from addressing the core systems, improving Enterprise Resource Planning (ERP) systems through to focusing on customer service. A holistic approach is required, along with clarity about what the end goal looks like.

If a business lacks the capabilities of a competitor and has to close the gap quickly, an acquisition is a proven way to achieve that goal.

## The case for M&A

As the call for business transformation gets louder, some technology leaders will opt to disrupt themselves. Uber's acquisition of Australian car-sharing business Car Next Door is an example which, in part, recognises that some ride-share customers are looking for more sustainable solutions. This ability to assess the core of a business and understand how it needs to evolve will be especially crucial in the years ahead.

M&A can serve as a catalyst for companies to pursue digital transformation, which in turn can enable business growth, simplify business processes, reduce operational costs and enhance the value of any future M&A deals.

Deloitte has seen this first-hand through hygiene and health company Essity's

acquisition of Australian company Modibodi, a provider of leakproof apparel for periods and incontinence, including underwear, swimwear, activewear and maternity wear. The deal delivers on many fronts – it strengthens Essity's position in the fast-growing reusable segment; it builds brand strength; it enhances sustainability credentials by having access to a new range of reusable and biodegradable products; and it draws on Modibodi's excellent digital marketing and e-commerce capabilities.

In essence, through one M&A deal, Essity has responded to disruption at the core of its business and recognised changing consumer preferences in the intimate hygiene space. Such a blueprint is relevant across other businesses and sectors.

## Consumers shake things up

A total of 74% of M&A leaders selected customer experience as a high priority area of digital transformation. This was followed by operational agility at 60% and the integration of technology at 50%. Only 9% of those surveyed listed culture and leadership as a high priority area of digital transformation.

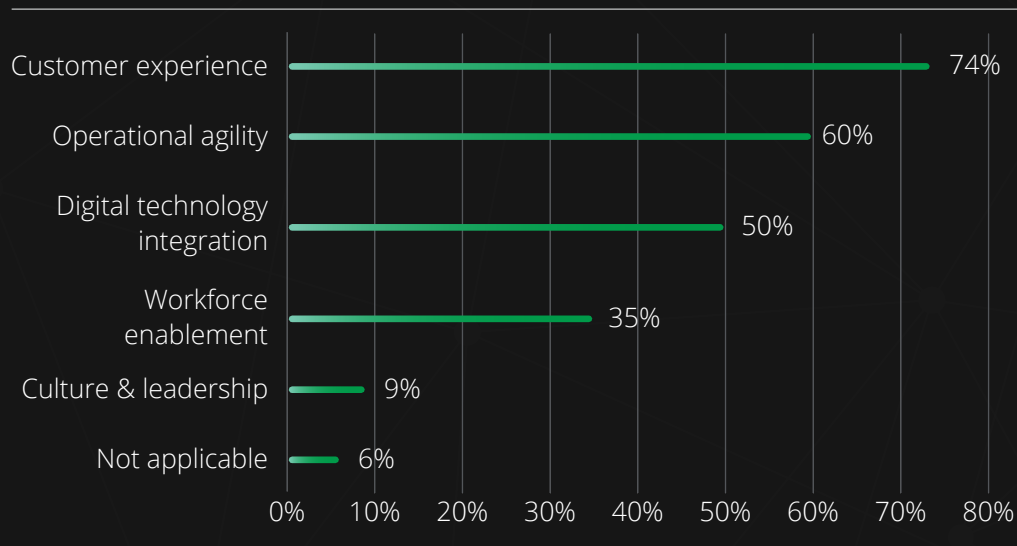
Empowered consumers are insisting on change, as well as technology enhancements, as they force business leaders to adapt to ever-changing market demands. In such an environment, companies need to understand their evolving industry landscape and determine the best way forward. That may mean partnering with others to offset threats and maximise synergies.

Limitless Technology's acquisition of Australian online flower and gift-delivery service LVLY is a case in point. Through its same-day metropolitan delivery of beautiful, sustainably sourced flowers, LVLY has created a best-in-class customer experience that others want to replicate, and Limitless Technology wants to learn from and repeat that strong buyer experience with other arms of its business.

The challenge for Limitless Technology and other acquiring companies pursuing similar strategies will be to preserve the culture of their acquisition.

Chart 23

**Which areas of digital transformation are a high priority for you?**



Note: respondents were able to select all options that apply.

**Responding to disruption**

As companies weigh up their transformation options, challenges will emerge. The survey results show that the biggest disruptive forces, or risks, that will affect the drivers of M&A for business performance in the next 24 months are the changing economic cycle (50% see it as a high risk), technology (37%), environmental and climate factors (35%), supply chains (31%) and changing consumer habits (30%).

There is pressure on businesses to address these five factors, and any M&A deals must tick the box on some or all of these elements. Leaders can no longer think about these factors in isolation.

Modibodi and LVLV highlight the point. They are purpose-led businesses that have paid attention to ESG principles while also addressing other key elements of their businesses. Such strengths and values are being recognised in the market and should be rewarded with premium prices, despite difficult economic conditions.

In the next 12 months, many companies will move to acquire assets to fill gaps in their core portfolios. At a time when deals are taking longer than before and with more detailed due diligence in certain areas, rapid integration is recommended.

This is where M&A comes into its own.



#### **Theme 4 - Why scenario planning has never been more important**

We are in an era of disruption for businesses and M&A. Focusing on the big picture, a three-decade period of post-Cold War geopolitical stability in the Asia-Pacific region is ending and the economy is moving back into a phase of uncertainty. The M&A market in Australia and New Zealand is facing the prospect of headwinds as it confronts higher interest rates and lower economic activity.

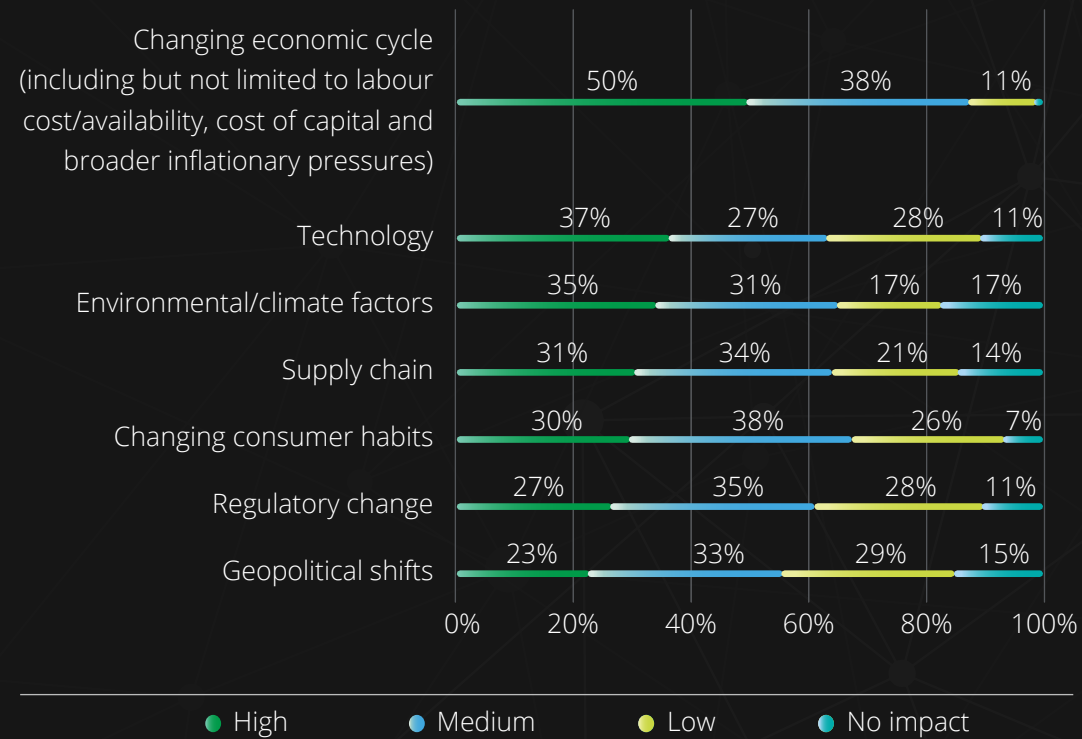
A total of 88% of respondents listed the changing economic cycle as a high or medium risk affecting the drivers of M&A for business performance over the next two years. This includes factors such as the cost and availability of employees, the cost of capital and the impact of inflationary pressures in the economy.

More than 60% of respondents listed other disruptive forces such as technology, the changing climate, evolving customer habits, supply chain resilience and regulatory change as high or medium risks over the next two years.

In volatile markets, M&A valuations become more difficult.

Chart 24

**What do you see as being the biggest disruptive forces/risks impacting the drivers of M&A for your business performance in the next 24 months?**



## Risks on many fronts

Businesses are facing more disruptions now than they have in the past – in addition to traditional business and economic disruptors, factors such as supply-chain risk, labour force changes and consumer demands have come to the fore. Broad ESG and globalisation threats are also increasingly relevant.

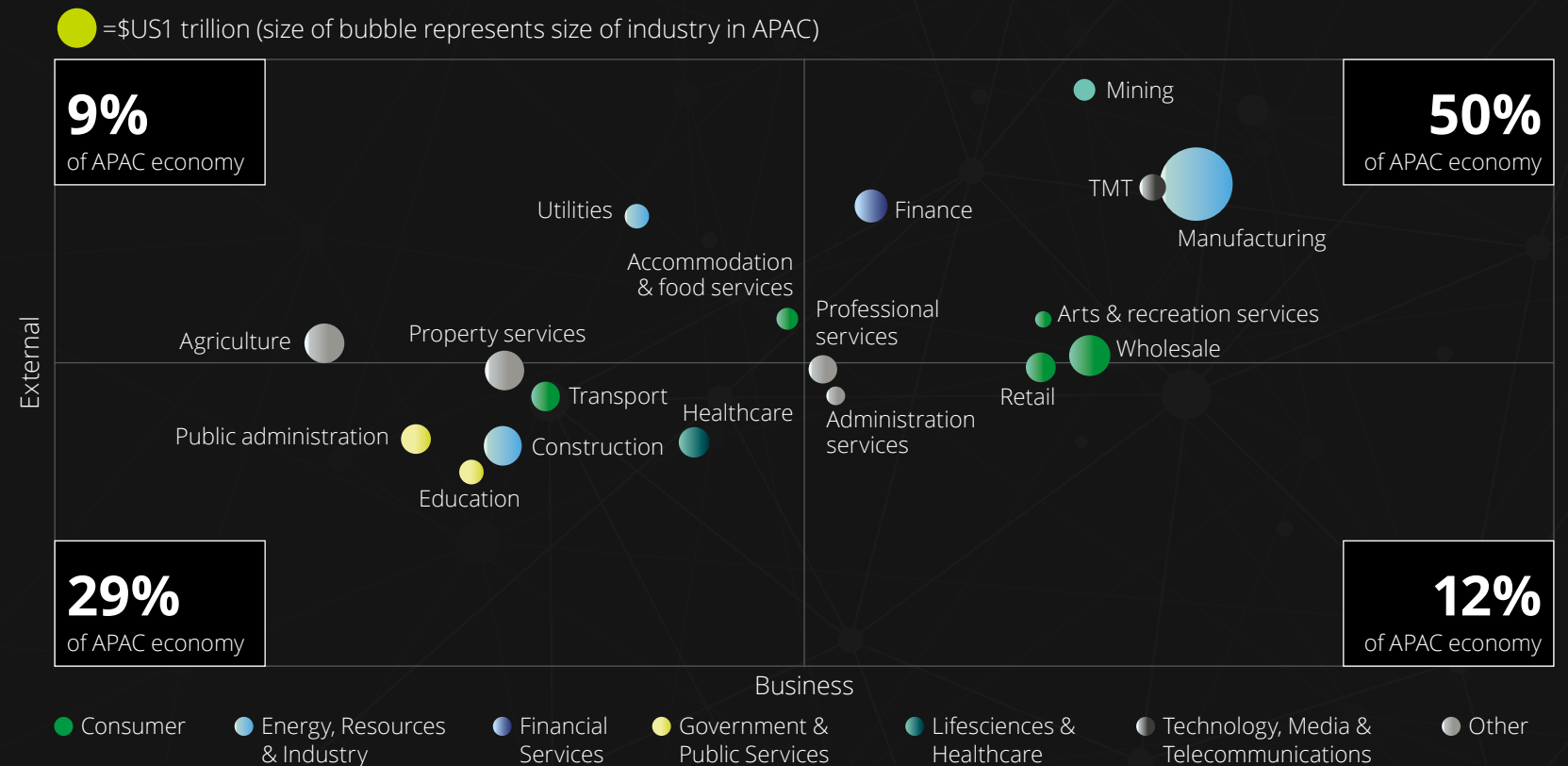
Value is far more contested in a highly disrupted and volatile market; in short, there is plenty of disagreement between buyers and sellers over valuations. Cryptocurrency markets are an extreme example of how tricky it is to value assets in the emerging digital economy.

Against such a backdrop, M&A gives businesses a chance to quickly respond to testing environments and disruption.

Our analysis shows the sectors experiencing the highest levels of disruption are mining, manufacturing, finance and telecommunications (TMT).

Chart 25

### Who's being hit hardest?





Achieving strong valuations in sectors such as oil and gas, critical minerals and rare earths in coming years will be challenging as they face regulatory uncertainty and investor risk because of climate change.

As the sector that creates and first uses technology, TMT typically experiences more tech disruption than most. Media entities may face challenges as streaming services jostle for poll position, while telecommunications businesses will be affected by growing consideration over the mix between assets and services provided by telco companies, with divestitures already occurring.

Consumer retail continues to face supply-chain disruptions on the back of the war in Ukraine and changes to transport globally. This could lead to more M&A activity as businesses try to own more of their supply chain.

### **How to combat disruption**

For businesses facing disruption, a comprehensive risk plan that maps risk responses is crucial.

Businesses also need to build up their internal capabilities and diversify as much as they can. For example, they should have different sourcing options for general merchandise and fresh produce to reduce supply-chain challenges and consider how to de-risk global supply chains. In such volatile times, agility is key.

The sectors experiencing the highest levels of disruption are mining, manufacturing, finance and telecommunications.



**Theme 5 – Spotlight on ESG shows no signs of dimming**

ESG is already being considered in more M&A deals than not and looking ahead to the next three- to five-year horizon, value creation is anticipated to become the dominant motivator for embedding ESG in M&A strategies.

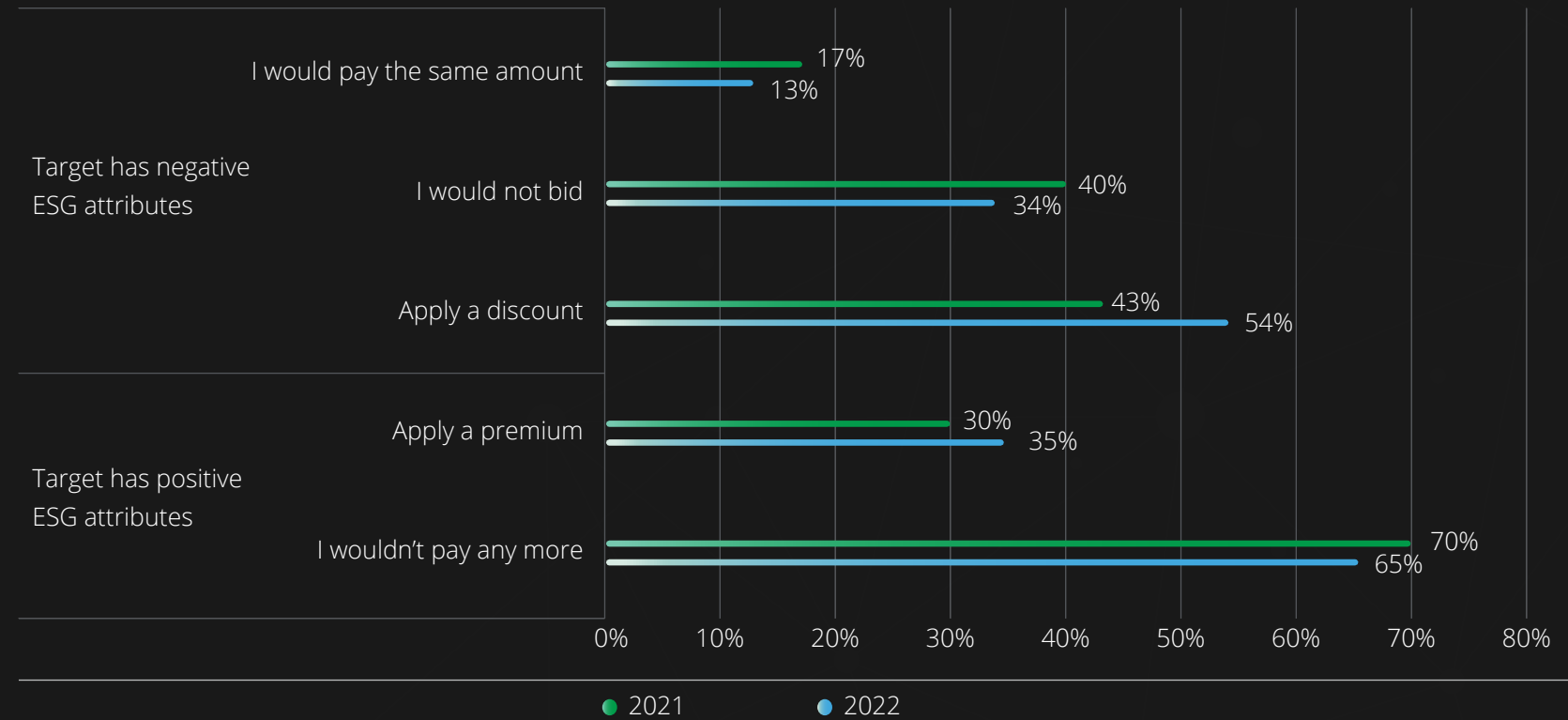
An increasing share of survey respondents are factoring ESG into their decision-making either all the time or most of the time – with 63% of respondents doing so in 2022, compared to 52% in 2021.

In 2022, 54% of respondents say they would pay less if the target company had negative ESG attributes, up from 43% in 2021, while 35% of respondents would pay more if the target company had positive ESG attributes, up from 30% in 2021.

Digging a little deeper, there are some interesting nuances emerging across Australia and New Zealand, with fewer respondents factoring ESG issues into their decision making all of the time in New Zealand (33%) compared to Australia (43%). Despite this, 43% of respondents in New Zealand factor ESG issues into their decision making most of the time, compared to 17% in Australia. Only 5% of New Zealand respondents stated that they do not consider ESG issues, compared to 12% in Australia.

Chart 26

**If a target had positive or negative ESG attributes, how would that influence the price you would pay?**



Despite this progress, the market is still grappling with the relationship between ESG and value. A total of 58% of respondents listed quantifying the value of ESG as a pain point, with 55% citing issues around the quality of ESG data.

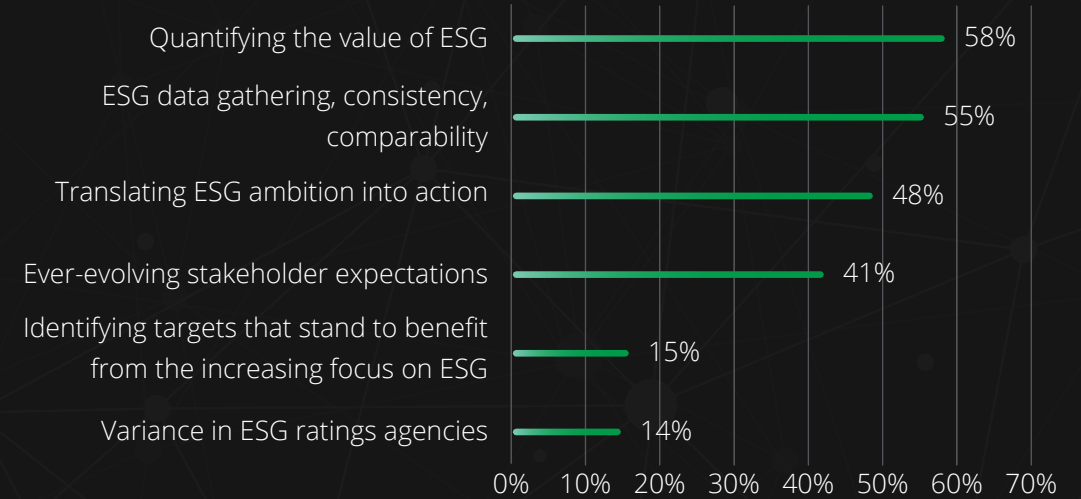
These difficulties extend to the question of how ESG concerns can be captured within valuation models. Some 35% of respondents apply a qualitative overlay or adjustment, yet the proportion of respondents using other methods such as discount rates or cashflow adjustments has increased from 25% in 2021 to 38% in 2022.

Notwithstanding this, there are already examples of companies walking away from deals as a result of ESG issues. There is also an increasing number of examples where indemnity insurances and discounts are being applied by buyers in the context of inadequate ESG practices.

As there is a continual maturing in the market on what embedding ESG in the context of a deal entails, how it is connected to core business priorities and as ESG data becomes increasingly standardised, it is expected that quantification practices between ESG and value will continue to evolve. At the same time, there will also be increased acceptance that just like some attributes of an attractive deal cannot be quantified, not every ESG issue should, or can be, quantified.

Chart 27

**Acknowledging the complexities associated with ESG, where are the biggest pain points for your company?**



Note: respondents were able to select all options that apply.

### A strategic edge

Although different levels of maturity apply, smart companies are now discussing and embedding ESG at the board level and in corporate strategy, with a resultant widespread convergence expected between corporate and ESG strategies in the future.

Integration of ESG factors into corporate strategy is also being driven by regulators, employees and the general public. This trend is unlikely to dissipate as companies pay more attention to issues such as climate change and the journey to net zero emissions, resource efficiency and the circular economy, creating ethical, resilient and transparent supply chains, as well as addressing a desire for competitive business advantage and commitments to having a positive social impact.

In this environment, ESG opportunities and risks abound, including the rise of the ethical customer in the Consumer Sector, combined with the growth of climate tech, clean energy and the circular economy fuelled by the low

carbon transition. These are already becoming dominant themes in the deal environment, particularly in the Financial Services and Energy & Resources sectors, in both Australia and New Zealand.

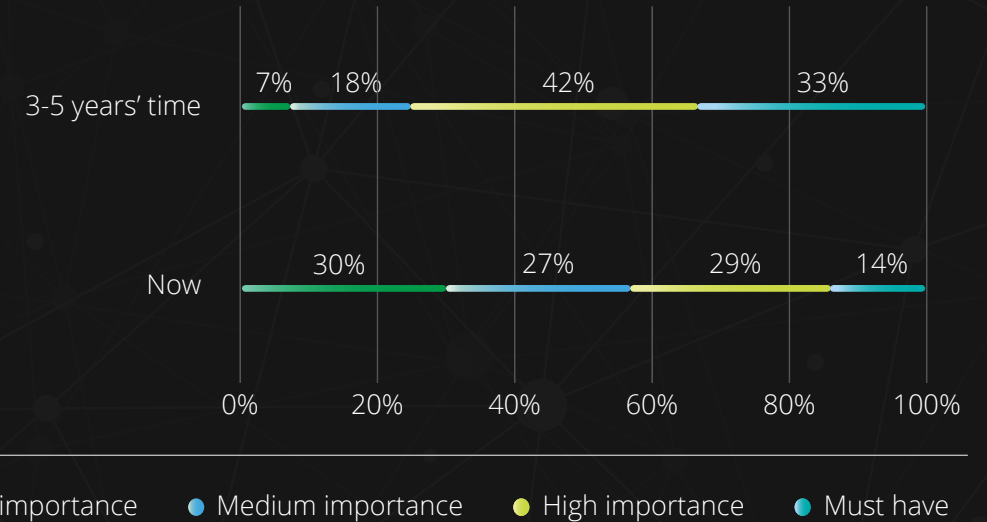
### What it means for M&A

ESG is being considered in M&A deals more often than not. While 43% of those surveyed described ESG performance as currently of high importance or a must have, three-quarters of respondents expected this to be the case in three to five years. Only 7% of respondents anticipate that ESG will be a low priority in the M&A due diligence process three to five years from now. These results demonstrate that we are witnessing incremental steps in the right direction.

The share of respondents who have walked away from a potential M&A transaction because of the target company's ESG performance increased from 20% in 2021 to 26% in 2022.

Chart 28

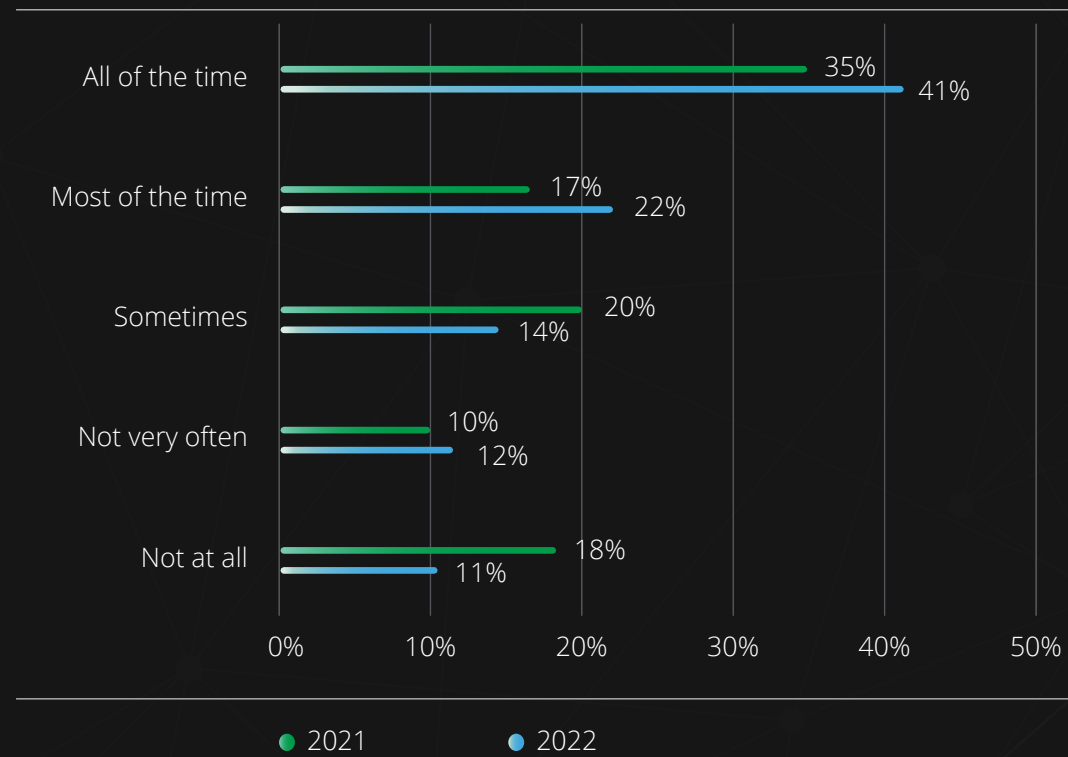
### How important is ESG performance as a consideration in the M&A due diligence process?



Note: percentages calculated exclude respondents answering, "Do not have a view".

Chart 29

**To what extent are you factoring ESG - including climate change - impacts into your planning and decision making on M&A matters?**



Attitudes towards the role of ESG in M&A are expected to continue to change. Around one third of respondents (32%) see ESG as an opportunity for value creation and competitive differentiation in 2022, and 63% expect that ESG will present this opportunity in three to five years.

ESG has also become an influencer in portfolio rebalancing and redesigning. Almost 50% of respondents are re-evaluating or planning to re-evaluate their portfolio to acquire or divest through the lens of ESG, including energy transition commitments. However, using divestment as an option to improve the ESG credentials of a company will probably become increasingly challenging as market awareness and education grows.

As organisations seek to pivot their corporate strategies and undertake large-scale strategic transformation, key questions will emerge around their portfolio mix; do we need to grow, acquire or partner to deliver on renewed strategies?

So, two sides of the ESG coin come into play; first, it is an opportunity to foster strong growth and, second, it comes with risks that require consideration. Currently, the market is trying to balance the response to ESG risk - and what it means for a company's overall strategy and financial outcomes - with stakeholder expectations.

This juggling act is expected to settle during the next five years. Risk and expectations will be more soundly managed, and value will be driven up while delivering competitive differentiation.

### Buyer beware

Similar to last year, ESG performance is an issue of low to medium importance for 57% of respondents when considering the M&A due-diligence process.

In M&A strategy, there is currently an equal split between those that view ESG as a source of value creation, those that are embedding ESG to manage stakeholder expectations, and those still viewing ESG as a set of risks to be managed.

Looking ahead to the next three- to five-year horizon, value creation is anticipated to become the dominant motivator for embedding ESG in M&A strategies. Buyers do not want their businesses to be undermined by unsound ESG practices,

and similarly, do not want to miss out on investment opportunities in an increasingly competitive market underpinned by clear tailwinds driving towards a more sustainable, lower carbon future.

What is clear is that ESG impacts should not be a post-acquisition consideration because at that point they can be challenging and expensive to accommodate.

An opportunity exists for forward-looking, astute M&A teams. Do not wait three to five years to act. Search for and understand ESG opportunities now to drive value creation, innovation and competitive differentiation.

Fast, decisive action should pay off in the long-term.

Looking ahead to the next three- to five-year horizon, value creation is anticipated to become the dominant motivator for embedding ESG in M&A strategies.

## Industry focus – Power, Utilities & Renewables

### Once in a generation transition

As we emerge from the haze of debating 'why we need to change' towards a far more productive dialogue around 'how' and 'when', fortune may well favour the brave looking to lead the energy transition in Australia and New Zealand. With greater alignment between the trilogy of the public, private and social sectors, the imperative for change has never been greater. The stakes have also never been higher.

No one is insulated from this once in a generation energy transition. As energy prices reach unprecedented highs in Australia and supply risks escalate across both Australia and New Zealand, the conviction to create a more sustainable framework and solution has extended beyond the board room and into the family room. We all are far more educated on the state of play and recognise the need for substantive change.

These social priorities are also aligning with economic rationalism as technologies evolve, associated cost curves decline and legacy generators fast approach their retirement.

With increased public sector impetus, the Power, Utilities and Renewables sector is promising to be awash with opportunities for wise investors of all shapes and sizes.

We anticipate that the current environment provides something for everyone. Below are five related themes from an M&A perspective:

**Premia for operational assets:** We have previously commented that fortune would favour the brave who take a leading position in addressing the energy conundrum. This has played through in recent months with strong demand shown for operating portfolios as evidenced by the breadth of bidders and ultimate transaction values realised. With finite onshore solutions, particularly with regard to wind and the state of supporting transmission and distribution networks, we expect businesses with a mix of blue-chip operational sites will continue to command a healthy transaction premium.

**Size still matters:** We anticipate that the increased funding demands to manage electricity and gas price volatility could lead to consolidation among Australia's retailers.

While we all hope subscale retailers do not face the same fate as in the UK recently, there is a risk that those retailers that achieved customer growth through competitive pricing will find it challenging to meet increasing capital requirements. Larger retailers have been better equipped to absorb the current market shock-waves and will continue to benefit from the broader distribution of their fixed costs bases. This may provide an opportunity to capitalise on their existing position.

### Capital recycling and re-prioritising:

The shifting market and political landscape in Australia may provoke existing operators to assess their portfolios and restructure either their operations or ownership interests. The backdrop of geopolitical priorities also remains in the shadows. We expect that there could be an ongoing reshuffling of the deck chairs as European and Asian shareholders reassess their longer-term strategies in the context of their broader portfolios. The prospect of further large-scale transactions remains a possibility while Australia's new Federal Government seeks to recalibrate relationships. In New Zealand, we are seeing

a similar re-prioritisation – the sale of retail portfolios and proposed sale of regulated assets to redirect capital to renewable energy developments are recent examples.

### Following the leader could have a silver lining:

While it's widely viewed that Australia is paying the price of many years of inertia, the absence of developing utility scale energy solutions could work in our favour. Australia and New Zealand are well positioned to benefit from the learnings from other geographies in testing new technology solutions such as offshore wind and solar, tidal generation and hydrogen. Global leaders will seek new geographies to expand their operational footprint and Australia is emerging as a sound candidate as state and federal governments alike roll-out the enabling legislation and policies. Ongoing inbound cross border activity is likely.



**Beware the left of field:** We anticipate the ongoing emergence of disruptive business models. This may take the form of corporates broadening their portfolios into energy solutions such as Telstra Energy. Consumers also have an important role to play if a sufficient scale is to be harnessed. Australia's uptake of rooftop solar on a per capita basis is among the highest globally and is collectively the largest virtual power generator in Australia at producing 17 GW of electricity. To realise the opportunities available through Australia's energy transition, unlikely alliances could emerge that win the hearts and minds of the increasingly sophisticated and socially conscious consumer.

### Survey responses

All Energy, Resource and Industrials (ER&I) respondents to the survey were confident that growth opportunities will arise over the next 12 months, with more than 87% anticipating the number of deals they pursue will remain steady or grow further from a buoyant 2021. The highest priority M&A objectives are filling capability gaps in their existing portfolios, driving the sustainability agenda, acquiring competitors to consolidate and the opportunity to consolidate the sector, and divesting non-core assets. With 77% of respondents highly confident of their balance sheet strength and 61% highly confident of favourable credit conditions, the ER&I sector is well positioned for another active year for M&A.

Consistent with market trends, 58% of respondents noted the desire to explore joint ventures and alliances in the year ahead. Divestments were identified as a priority for 13% of respondents, which aligns with our expectation of capital recycling or downsizing of investment holdings. The overwhelming majority of participants (94%) are focused on acquisitions over the coming year. But we are not without headwinds – 81% of respondents highlighted valuations and 65% noted the competitive deal environment as the greatest challenges in delivering a successful M&A outcome, with the uncertain market conditions noted as the third greatest challenge. We suspect these challenges will not disappear quickly as gas and electricity

wholesale price volatility and supply chain risks remain a challenge. We are, therefore, buoyed by the continued focus of corporates on delivering their longer-term strategies. Strong balance sheets and a burning platform requiring more capital to help solve our energy and supply chain predicaments underpin our expectation of continued M&A activity for quality opportunities.

## Industry focus – Financial Services

As the rising interest rate environment causes angst for many Australian and New Zealand businesses, they may well look on with envy at the financial services sector. Put simply, rising rates should increase profitability for banks and the return on investments for insurers in the year ahead.

The overwhelming viewpoint within the financial services industry – driven mainly by big bank respondents to our survey – is that the current environment will also be quite favourable from an M&A perspective.

Some noteworthy trends are already emerging. Many banks have been divesting their non-core businesses in recent years and are now pivoting to acquisitions. In doing so, they are trying to acquire both new capability and talent – and the current environment may present opportunities to acquire well run and established non-bank financial institutions or fintech platforms.

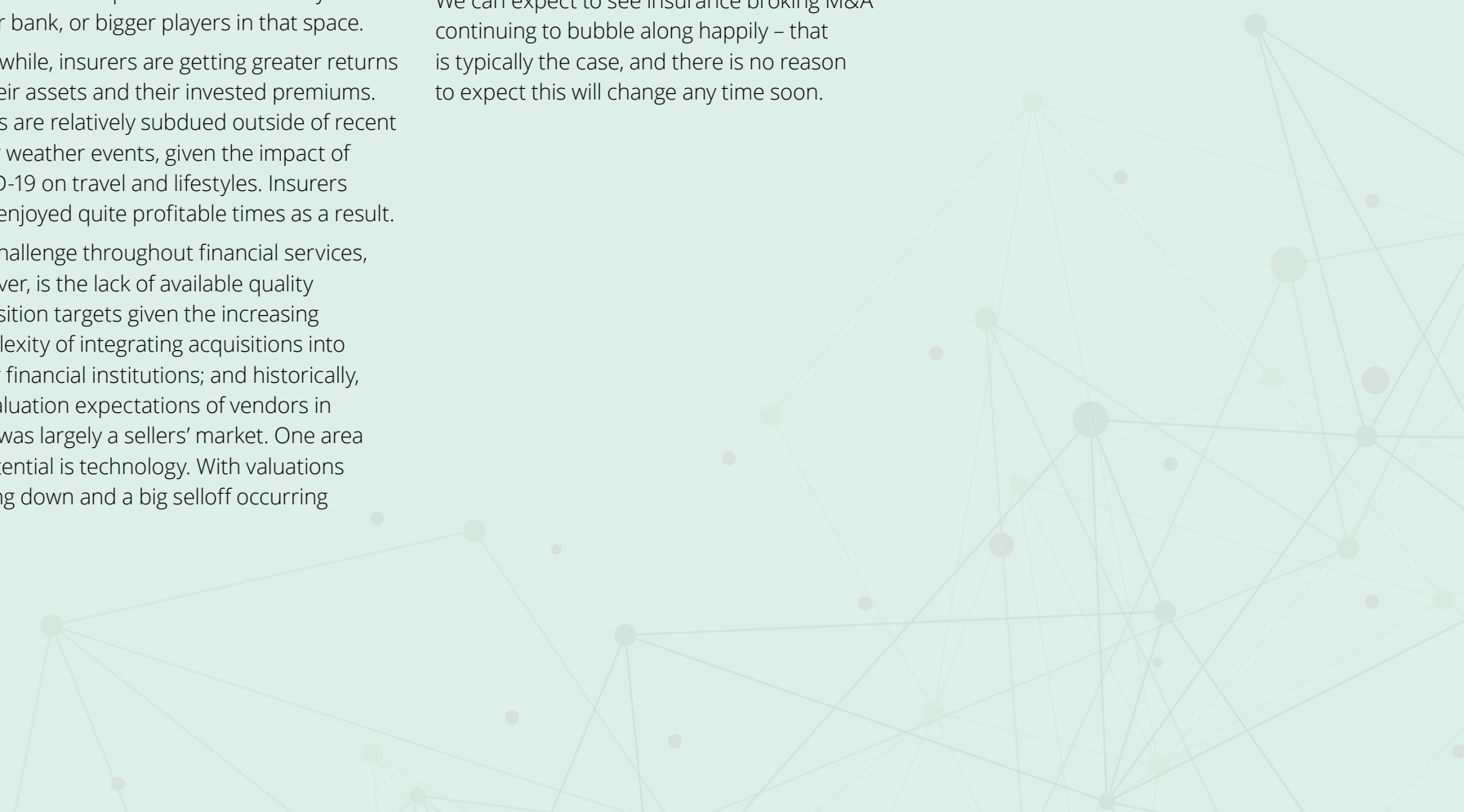
Non-bank lenders, in general, are seeing their profitability squeezed through tightening net interest margins as base rate rises are ahead of product repricing, which potentially makes them more susceptible to a takeover by a bigger bank, or bigger players in that space.

Meanwhile, insurers are getting greater returns on their assets and their invested premiums. Claims are relatively subdued outside of recent major weather events, given the impact of COVID-19 on travel and lifestyles. Insurers have enjoyed quite profitable times as a result.

The challenge throughout financial services, however, is the lack of available quality acquisition targets given the increasing complexity of integrating acquisitions into major financial institutions; and historically, the valuation expectations of vendors in what was largely a sellers' market. One area of potential is technology. With valuations coming down and a big selloff occurring

in tech globally, the pool of potential fintech targets may broaden in this space, particularly if some become distressed or are unable to raise additional capital.

We can expect to see insurance broking M&A continuing to bubble along happily – that is typically the case, and there is no reason to expect this will change any time soon.



## Steering the right course

Three-quarters of survey respondents are highly confident there will be growth opportunities in their sector, which will impact M&A activity during the next year.

That is predictable – in this type of interest rate environment, well capitalised financial services businesses look for capability they can bolt on, as well as growth opportunities where they can buy competitors that are smaller or facing challenges. For larger incumbents, the market conditions allow them to capitalise on what they are already doing. We saw this in 2008-2009 with major bank mergers and expect we may see it again through this interest rate cycle.

Many respondents also want to expedite the synergy capture for recently completed M&A deals, with 75% looking to do that in the next year. Lots of banks have been doing deals to capture synergies because they want to fill gaps in their portfolio – adding teams, systems or products into their existing core business. Previously, they had been shedding assets as they sought to redetermine what was their core.

One of the most staggering survey results is that just 42% of respondents carry out 100-day, six-month, or 12-month post-acquisition reviews. The majority of businesses fail because they are not correctly integrated – and this risk heightens if strategic and integration objectives are not analysed early on.

## Explore new opportunities

Although the financial services sector is well placed, there is no room for complacency. M&A and business leaders should be thinking about ecosystems, partnerships, alliances and global trends, including cryptocurrencies and millennials as a cohort and climate/net zero, which is seeing an increasing focus from financial institution stakeholders.

The power of the consumer is important. It's time for banks to explore how they can enhance customer experience, possibly through M&A. Interestingly, our research, [The mortgage battlefield: why customers switch banks \(and how to win them back\)](#), shows that 13.7% of the estimated 3.9 million owner-occupied mortgages in Australia are in motion every year. That means more than 1 in 10 homeowners are open to changing their

mortgage provider annually. How do you make sure you capture more of these customers than your competitors? Having a customer lens and trying to create the bank of the future, or the insurer of the future, that addresses customer needs – socially or through products – is essential to sustainable business success.

## Positive market forces

The biggest risk for financial services in the next 12 months will be if negative sentiment reduces consumer confidence, people stop spending and unemployment increases – leading to credit issues and defaults for banks or claims for insurers.

However, we are still experiencing historically low interest rates and low unemployment, and Australia's underlying economy is strong. As a result, the sector should remain robust.

As strong players become even stronger, consumers should benefit. They will have access to bigger, well-capitalised financial institutions that provide the best customer experience and product suite.

M&A is a tool to help financial institutions achieve such outcomes.

## Industry focus – Consumer

### Winning the consumers

There is still a deep pool of money for businesses in the consumer sector even though rising interest rates and other economic headwinds have dampened consumer confidence. Businesses that have well-known brands, strong margins and growth potential will continue to be of interest to both trade buyers and financial sponsors.

As the sector prepares for more uncertainty in this new volatile market post-COVID-19, businesses can prosper if they get things right on two fronts – first, by offering strong value to prospective buyers and, second, by differentiating their product offering to win over customers.

The latter point is crucial. True differentiation allows a business to request a higher price point, to be a market mover, and to receive strong M&A attention.

Without such differentiation, success relies more on product pricing and having absolute clarity on your business proposition. If organisations do not differentiate, or if they cannot put forward a strong enough value proposition, they will struggle in this new market environment of ever-increasing competition.

So, how can consumer organisations differentiate? They need to have a direct dialogue with their customers, and increasingly that will be through effective social media strategies. Consumer business also need to address sustainability, whether it is via the products they make, the ingredients they source, the packaging they use or the way they think about recycling.

Regardless of the approach, M&A should be a powerful instrument in a business's differentiation toolbox.

### Defiant M&A outlook

Expect the consumer sector to be active in the M&A market during the next 12 months. Of course, an inflationary environment, rising interest rates, and supply-chain bottlenecks will pressure margins.

However, private equity investors are still hungry for good deals, while cashed-up corporations want to keep growing. The overall volume of M&A deals may fall in the year ahead, but that simply reflects extraordinarily high activity in 2021.

Although interest rates are on the rise, they are still largely manageable, and positives such as the reopening of state and national borders will be a boost for the market.

Organisations that have good access to customers, including through diverse online channels, should continue to do well and attract the interest of investors.

## The changing consumer

The sector is recognising and responding to a shift in consumer behaviour.

COVID-19 disruption has accelerated consumers' embrace of digital channels over in-store purchases and forced retailers to fast-track their transformation plans. As a result, all eyes will be on consumers and what they choose to spend their money on. This, in turn, will influence M&A decisions as leaders in this space seek to keep pace with accelerating retail transformation and deploy their capital intelligently.

In this environment, businesses have some choices to make. Do they switch manufacturers and move production to provide more certain supply chains? Do they target new markets and geographies? Do they target the metaverse that enables customers to experience their brand through virtual reality?

The answers to these questions and others will be different for each business, but they should not be ignored. To make the right choices, business leaders must truly know their customers. One of the best ways to do so is through consumer engagement. Let them know what you stand for – and offer a diverse range of exciting customer channels.

## Trends to watch

As consumer businesses emerge from the pandemic, product and service innovation and digital transformation should be on their agenda. The best businesses will use their existing capital wisely and seek new avenues to generate more growth opportunities as they continue to evolve their business models and customer channels. Data and technology will naturally help educate businesses about customer trends, and they should capture the imagination of consumers and guide

them to try their products, rather than simply counting on market research to try to guess what they want. Those days are gone.

Looking ahead, if businesses have a robust capital framework and take advantage of targeted M&A activity, there is every prospect that they can succeed in what will at times be challenging markets. May the best businesses prosper.



## Conclusion

With M&A activity forecast to remain strong in 2022, albeit at a lower level than 2021, business leaders will face a juggling act.

On one hand, they should be focusing on synergy realisation from recent deals in an effort to make their businesses more resilient. On the other, they must be on the front foot as they seek to transform their operations through digital acceleration and portfolio expansion.

According to the results of our 2022 survey, there will be significant opportunities for business growth in the coming year, and

most respondents expect the size of M&A deals to increase. This sets the scene for an exciting M&A market, even though economic headwinds will present headaches.

In this environment, a clear message to emerge from this year's survey is that M&A leaders should be decisive. They need to act quickly to deliver on the strategic returns of an acquisition at a time when disruption is rapidly transforming economies and companies. The challenge will be to maintain deal momentum and focus on the long-game in a market facing a myriad of distractions.

M&A has long been a smart tool to help companies grow and reach their potential, especially in challenging markets. The year ahead is set to prove that reality once again.

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