M&A Forecast

2016 M&A Outlook Survey Summary

Dykema

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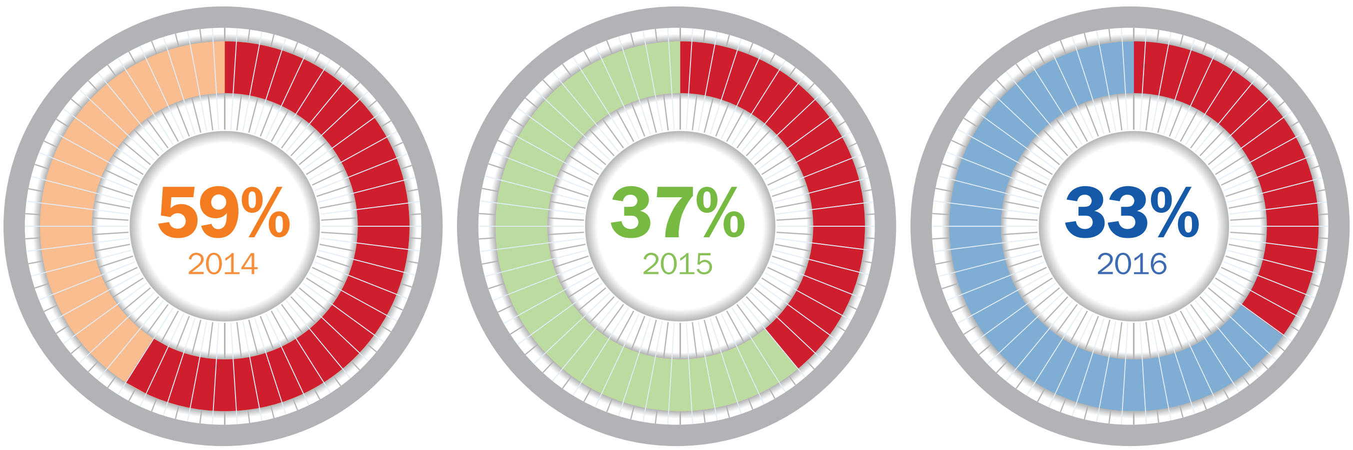
Since our inaugural report in 2005, Dykema has been conducting an annual analysis on the state of the M&A market. In our 12th annual survey, we canvassed senior executives across the nation—CEOs, CFOs, owners, managing directors and other professionals involved in M&A activity within their respective firms—to gauge their experiences and outlook on mergers and acquisitions in the coming year. The results provide a snapshot of the current M&A environment and how it compares to past years.

We would like to thank all survey respondents and interviewees for their time and the insights they shared for this report.

What Lies Ahead for M&A?



12 month outlook on a strengthening M&A market

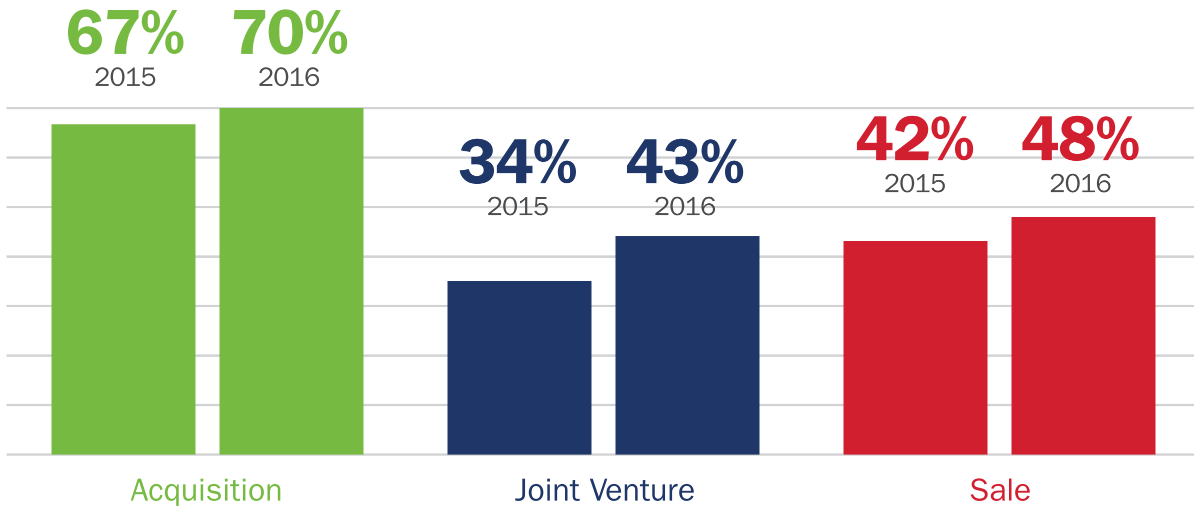
For the third consecutive year, we've seen a consistent decline in optimism, from 59 percent of respondents who predicted a strengthening market in 2014, to 37 percent in 2015, to 33 percent this year.

Dykema's 12th annual M&A Outlook Survey reveals that, while optimism about the deal market has declined, pessimism has not increased. Nearly half of respondents said they expect the U.S. M&A market will see no significant change in the coming year.

Despite the drop in optimism, the dollar volume of M&A activity in North America in 2016 rose steadily from the third quarter of 2015, peaking in this year's second quarter. At the same time, however, the number of deals has fallen sharply.

"Big picture, as the economy goes, so goes M&A."

—Thomas Vaughn, co-leader of Dykema's M&A practice



In the next 12 months

67% of respondents in 2015 said they would be involved in an acquisition, compared with 70% this year. 34% percent of 2015 respondents said they'd be involved in a joint venture, compared with 43% this year, and 42% of respondents predicted in 2015 that they'd be involved in a sale, compared with 48% this year.

Acquisitions, joint ventures and sales activity are expected to increase slightly across the board in the coming year. This is a sign of a steady market despite the overall drop in optimism in the survey's top finding.

"I was at a conference recently and there was a lot of buzz—people were saying they're busy with deals, just like we are. I think it's going to stay busy until at least the first or second quarter of 2017," said Terrel Bressler, Managing Director of Capital Prairie Advisors.

Respondents predict that small deals (under $50m) will lead the way in 2017, with an increase in M&A activity from privately-owned businesses, detailed further in this report. Bressler stated that some business owners could be trying to sell before the end of the year, concerned that tax increases (notably, capital gains) could pass in early 2017 and be made retroactive to the beginning of the year.

Were these predictions to come true, they would buck the trend of the past year in which deal volume dropped but the dollar value of deals held steady.

Sectors for Growth

For the third year in a row, energy, healthcare and technology are expected to see the most M&A activity in the next 12 months. Energy jumped two spots compared with the 2015 list, possibly because over-leveraged companies in oil and gas are seeking buyers. But after a spate of bankruptcies in 2016, that might be fading, Rick Lacher, Managing Director at Houlihan Lokey, said. "We are starting to see some signs of health in oil and gas as we're seeing private equity commit substantial dollars to exploration and production investments."

M&A Market Drivers and Obstacles

Drivers	Obstacles
Capital	Valuation
Interest rates	Availability of quality target
U.S. economic conditions	Buyer competition
	Due diligence
	Cybersecurity

Availability of capital was the primary driver of U.S. M&A activity for the third straight year. The percentage of respondents who chose favorable interest rates as fueling activity jumped for the third straight year, despite the Federal Reserve's December 2015 decision to raise interest rates for the first time in nearly a decade. In August, Federal Reserve Chair Janet Yellen announced that the case for an increase in the federal funds rate has strengthened in recent months.

"We've seen a lot of Chicken Little behavior in the past couple years and people are starting to become immune to it. I think the Fed will raise rates again by the end of the year, but that is already priced into deals—and like last time, it should mostly be a non-event," said Terrel Bressler, Managing Director of Prairie Capital Advisors

According to respondents, the most common obstacles experienced this year with regards to transactions mirror those of last year's results, with valuation leading, followed by availability of quality target, buyer competition and due diligence.

As one respondent put it, "There are a large number of private equity groups chasing a limited pool of attractive candidates. This is pushing valuations to highs."

M&A practitioners believe cybersecurity issues have become highly important during due diligence. Compared to 2015, a smaller percentage of respondents are assessing data security measures with third-party vendors this year, but a greater percentage of respondents are checking for internal policies that protect confidential or proprietary information.

Driver: The percentage of respondents who chose favorable interest rates as fueling activity jumped for the third straight year, despite the Federal Reserve's December 2015 decision to raise interest rates for the first time in nearly a decade.

Obstacle: Cybersecurity has become a critical issue during due diligence, and nearly 73% of our respondents check for internal policies that protect confidential or proprietary information.

"Attention to internal policies is up substantially, suggesting that those wishing to maximize enterprise value could benefit from a review of their data security policies and practices to be sure that they are due diligence ready."

—Stephen Tupper, Member of Dykema's Privacy, Data Security and E-Commerce practice.

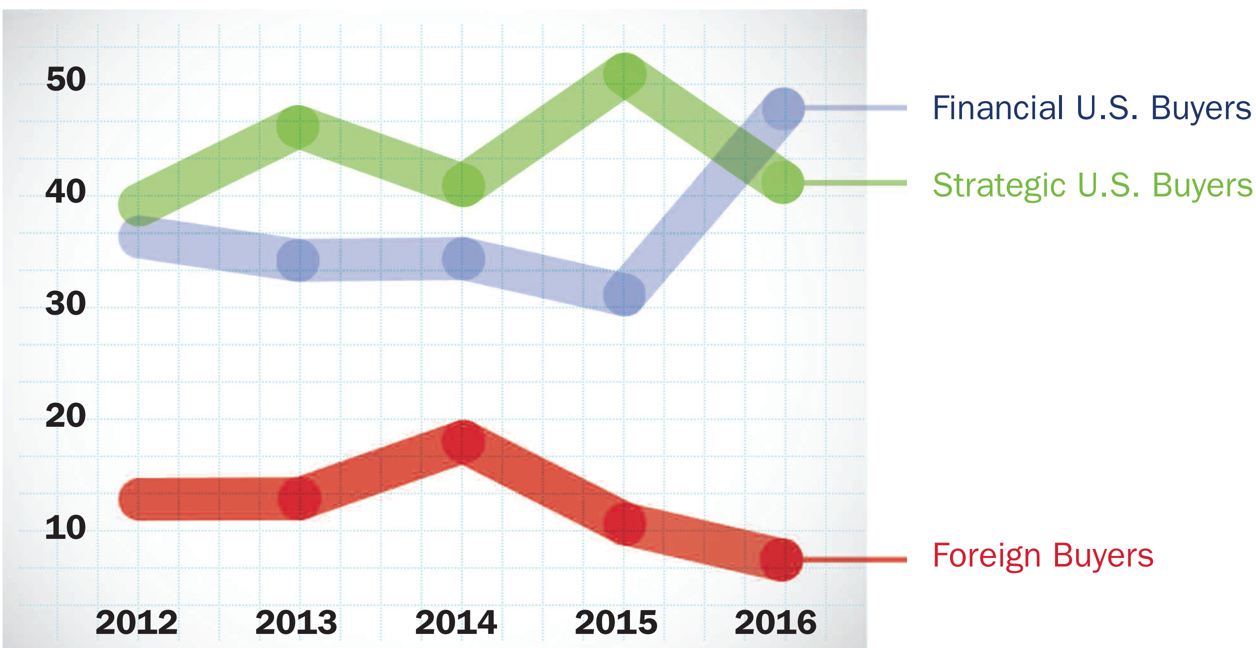
Buyers and Deal Valuation

For the first time since the 2008 survey, respondents said that U.S. financial buyers topped strategic buyers for having the most influence on U.S. deal valuation over the past year.

Financial buyers might have been more influential in the past 12 months because of increased interest in deals worth $5 million or less from private equity firms, according to Aaron Witalec of UHY Advisors. “They’re coming down-market and influencing the valuations versus strategics. As a result, strategics are slowing down their bidding and focusing more on inward operations.”

“A lot of money on the sidelines needs investing and the public markets are topping; hence private M&A will pick up.”

—Respondent



Interestingly, respondents predict a return of strategic buyer dominance in the next 12 months. One respondent said, “Strategics have the cash and liquidity to undertake M&A, and financial U.S. buyers will pull back to let the post-election dust settle.”

Another respondent said, “Strategic buyers buy on the basis of need and opportunity. Financial buyers buy only on expectations of oversized profits. With higher interest rates and tax changes, they will take a wait-and-see approach.”

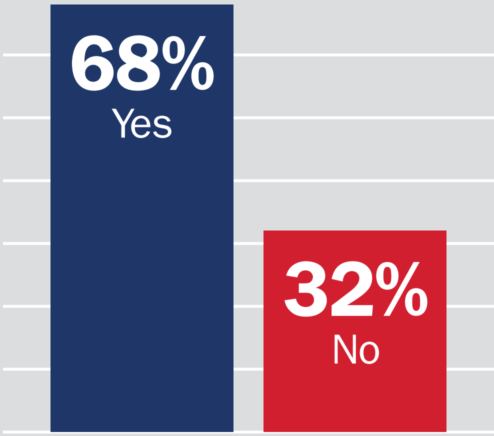
A Special Look at Sellers: Privately-Owned Businesses

Why?

Aging business owners seeking to sell

Concerns about the window closing

Concerns about declining valuations



Why not?

Current earnings are trending stable

Hoped for greater increases in value

Inertia

Do you expect there to be an increase in M&A activity involving privately-owned businesses in the next 12 months?

Based on this year's survey, respondents expect an increase in M&A activity from privately-owned businesses in the next 12 months. Aging business owners seeking to sell were seen as the top driver for growth in M&A activity from privately-owned businesses.

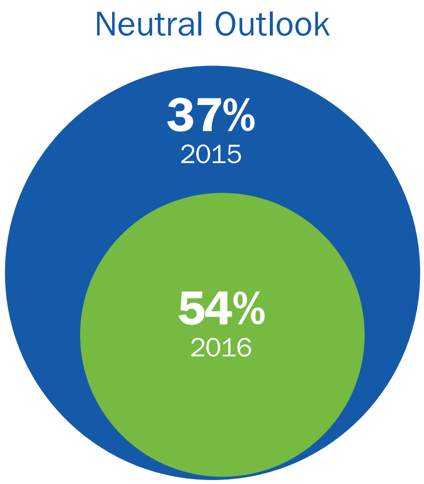
Terrel Bressler of Prairie Capital Advisors echoed these findings. In the last 12 months his company has worked with several privately owned businesses moving to sell—largely because of the owners' advanced ages. "When you're 83, you might not have 10 more years in you, so maybe you're thinking of retiring and leaving something to your family while the returns are still good."

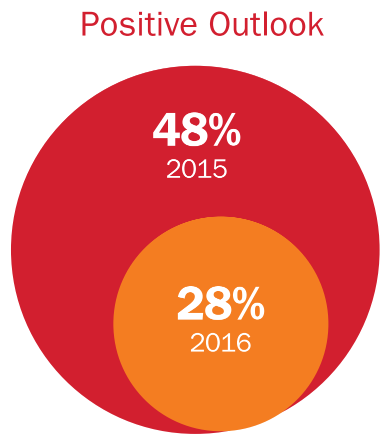
The media and market analysts speculate that the U.S. will likely see significant "baby boomer" sales of family businesses. Our respondents do not believe there will be a wave of family-owned business sales, but rather a slow trickle.

As Bressler said, when it comes to some business owners,

"80 is the new 60."

U.S. Economy





There is a marked decline from last year in the percentage of respondents who have a positive outlook on the economy. The difference can be attributed to the percentage of respondents who now have a neutral outlook on the U.S. economy in the next 12 months.

In another sign of waning optimism, just 25 percent of respondents said the U.S. economy would improve in the next year. The levels of pessimism and neutrality both rose 7 percentage points this year.

“We’ve been in an upward cycle—both for M&A and the economy—for a long time, so it doesn’t surprise me that some people are saying that, at some point, the cycle is going to end,” said Rick Lacher, Managing Director at global investment bank Houlihan Lokey. “In general, people are comfortable that the sky is not falling—and there’s nothing to suggest that a year from now, it’s going to.”

Respondents noted little effect from headline events such as Brexit, financial institution regulatory reform or the U.S. presidential election on deal-making in 2016.

A plurality of respondents predict that the election of either Republican presidential nominee Donald Trump or Democratic presidential nominee Hillary Clinton will have a neutral impact on the U.S. economy and M&A market.

As Lacher put it, “I think people view Trump as a loose cannon—and they don’t know what we would get if he’s elected. With Clinton, you’re looking at higher taxes and more antitrust review.”

The biggest concerns among respondents for the U.S. M&A market in 2017 are the possibility of corporate tax increases, increased federal regulation of business, an increase in the minimum wage, an increase in federal deficit spending, and taxation of carried interests.

Global Economy

Similar uncertainties exist in the global arena that could have a major impact on the M&A market. For the second straight year, respondents cited both the Federal Reserve's stated interest-rate outlook and economic issues in China/Asia as their top two concerns. Surprisingly, economic instability in Europe and Brexit—shorthand for Britain's June vote to leave the European Union—ranked third, despite serious concerns by dealmakers prior to the vote.

William Schulz, head of M&A for Citigroup in Europe, the Middle East and Africa, said activity levels had recovered since the June exit vote. "We haven't really seen the Brexit effect yet. The UK used to be the capital of choice for listing and incorporating a newly formed company. Now, although companies still want to be listed there, they are concerned about regulatory and tax risks."

Cross-border Deals

Leading Drivers

- Companies seeking growth via entrance in foreign markets
- Customer demand for local presence in foreign markets
- Companies seeking lower labor costs
- Companies seeking proximity to suppliers and materials
- Companies seeking lower tax rates/inversions
- Companies seeking new intellectual property
- Companies seeking access to raw materials or natural resources

Leading Impediments

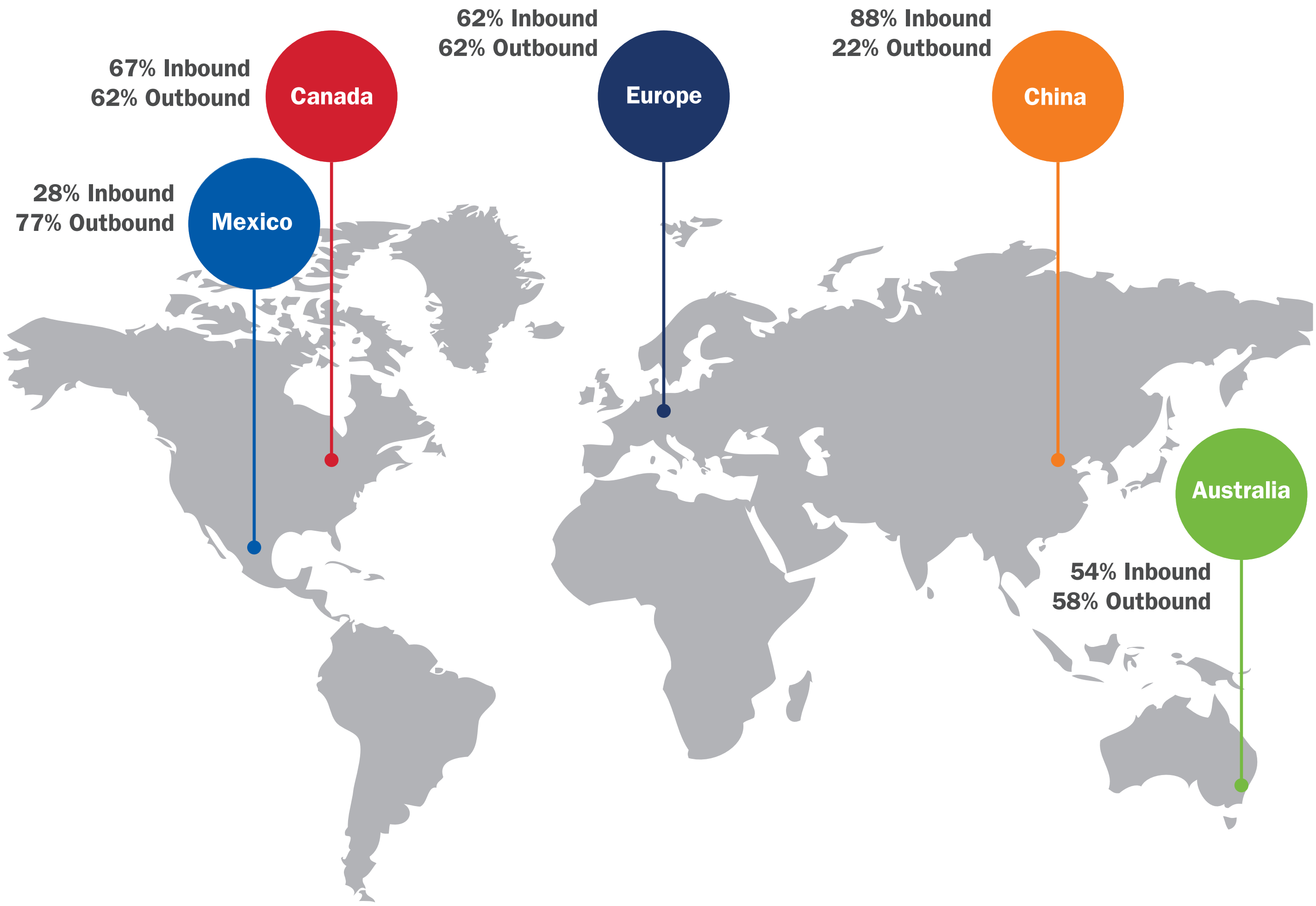
- Lack of experience managing international operations
- Foreign political instability
- Currency fluctuations
- FCPA and other compliance-related risks
- Inability to access affordable local currency financing
- Concerns about damage to public image

For the third straight year, the leading driver of cross-border deals is companies seeking growth via entrance in foreign markets.

Despite global instability, companies still look to international deals to spur growth. Alasdair Warren, head of investment banking across Europe at Deutsche Bank, said,

"Most of the developed world is short of growth, but long (on) low-cost capital. The recent data suggest we are likely to see rate rises in the U.S., but it's clear that the pace of rate increases thereafter will be very slow. In Europe, we will be in low-growth and low- or negative-rate territory for the foreseeable future. That means corporates are going to have to continue to look at M&A to drive growth and returns."

Respondents selected lack of experience managing international operations as the leading impediment to cross-border deals.



Expectations for inbound M&A activity to the U.S. are higher this year than last year from every country except Australia and Mexico, possibly as dealmakers look for better returns in a steady U.S. economy.

This year's survey saw an increase in U.S. companies anticipating activity in Canada. "This is likely driven by investors looking to Canada as they seek safer—and more familiar—bets internationally," said Richard Goetz, who leads Dykema's International Practice Group.

Expected M&A activity from China to the U.S. rose sharply. This may indicate that Chinese investors are more accustomed to Committee on Foreign Investment in the United States requirements, and it may reflect their ability and desire to get money out of China. However, expected U.S. activity in China remained low for the second straight year—possibly stemming from a larger economic slowdown in China and some political concerns, including China's conflicts with other nations in the Pacific.

Despite some concerns about how Brexit would affect the M&A space, expected U.S. M&A activity to Europe went up. That could indicate that deal-makers are taking a short-term view, possibly in light of favorable exchange rates.

Expected outbound activity from the U.S. to Mexico increased from 2015, likely a result of proximity—even if making goods in some Asian countries is less expensive. Mexico is becoming an attractive alternative as cost differences with China diminish.

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Methodology

In September 2016, national law firm Dykema Gossett PLLC distributed its M&A Outlook Survey via email to a group of senior executives and advisers including CEOs, CFOs and other company officers. The respondents to the survey represent a cross-section of M&A professionals and advisers with a diverse group of professions and more than a dozen sectors represented, including healthcare, technology, industrial/manufacturing and financial services. Respondents represent companies whose annual revenues range from under $1 million to more than $1 billion.

M&A Forecast

2016 M&A Outlook Survey Detail

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Shifting Winds: Cooling of deal activity and optimism in 2016

Dealmakers believe the global M&A market is leveling off in 2016 – but most don't believe it is significantly weakening, even with the pace of deals slowing considerably since last year's post-recession peak.

That's one of the key findings in **Dykema's 12th annual M&A Outlook Survey**. But the survey also shows that, while optimism about the deal market has declined, pessimism hasn't yet increased. Nearly half of respondents said they expect the market would see no significant change in the coming year.

Respondents noted little effects over the past 12 months from headline events such as Brexit, financial-institution regulatory reform or the U.S. presidential election. In fact, a plurality of respondents predict that the election of either Democrat Hillary Clinton or Republican Donald Trump will be neutral for M&A – though some did express concerns going forward about the effects of corporate tax increases, increased federal regulation and taxation of carried interest.

"But big picture, as the economy goes, so goes M&A," said Thomas Vaughn, co-leader of Dykema's M&A practice. Vaughn's comment echoes the thinking of many seasoned dealmakers.

"We've been in an upward cycle – both for M&A and the economy – for a long time, so it doesn't surprise me that some people are saying that, at some point, the cycle is going to end," said Rick Lacher, managing director at global investment bank Houlihan Lokey. "In general, people are comfortable that the sky is not falling – and there's nothing to suggest that a year from now, it's going to."

Deal activity has been in a steady decline for the past year; PitchBook reported just 3,044 deals in the third quarter of 2016, a 49 percent drop from the 5,882 deals reported in the third quarter of 2015. At the same time, the $505.2 billion worth of deals in the third quarter was slightly higher than the third quarter last year, thanks to a handful of mega deals.

Cause for Concern in Asia, Fed

While respondents showed little concern about overall economic conditions, they were less sanguine about a possible rate increase by the U.S. Federal Reserve or a decline in Asian economies, especially China's. But while respondents chose those as their top two concerns, they likely do not represent serious threats, as demonstrated by the lack of serious fallout since the Chinese economy began cooling last year and by the relative lack of damage after the Fed announced it would raise rates in December 2015.

"We've seen a lot of Chicken Little behavior in the past couple years and people are starting to become immune to it," said Terrel Bressler, managing director of Prairie Capital Advisors. "I think the Fed will raise rates again by the end of the year, but that is already priced into deals — and like last time, it should mostly be a non-event. As for China, people were saying that 'Oh, my god, China's slowing.' But it really hasn't affected much."

Neutral Sentiments Prevail

Just 28 percent of respondents identified their outlook on the U.S. economy as positive, down from 48 percent in 2015. But, as with the general M&A outlook, most respondents moved to a neutral outlook – up to 54 percent compared with 37 percent last year.

These findings indicate that respondents know their history. Since the Great Depression, only one period between recessions has lasted longer than the current economic cycle. It's also likely that respondents see signs of a slowdown with their own eyes.

"Sales growth for some of the companies we work for is leveling off, but order books and projected volumes are still there," said Aaron Witalec, managing director of UHY Advisors Corporate Finance, a professional service firm. "Margins were increasing but now they're just remaining constant or ticking down a little bit. It's not an emergency situation, but we're seeing a leveling off of growth – and possibly a path toward somewhat of a downturn."

Key Takeaways:

- About half of respondents, 49 percent, said availability of capital was most responsible for fueling current M&A activity, essentially the same percentage as in 2015. Twenty-five percent of respondents credited favorable interest rates, a 7 percentage point increase from 2015, despite the Federal Reserve's December 2015 rate increase.

- In one of the report's most interesting findings, respondents said U.S. financial buyers had the most influence on U.S. deal valuation over the past 12 months. This was the first time strategic U.S. buyers weren't seen as the most influential since the 2008 survey – even if financial buyers beat out strategics by only 5 percentage points.

- Sixty-eight percent of respondents said they expect an increase in M&A activity from privately owned businesses in 2016, down from 72 percent last year. The 4 percent difference mirrors the drop in the percentage of respondents predicting M&A growth this year.

- Despite the drop in overall confidence, 70 percent of respondents said they expect an acquisition involving their company or one of their portfolio companies in the next 12 months, up from 67 percent in 2015. Forty-eight percent expect a sale, compared with 42 percent last year.

- Aging business owners seeking to sell were again seen as the top driver for growth in M&A activity from privately owned businesses.

2016 M&A Survey Results and Insights

We asked respondents to complete a questionnaire designed to measure their thoughts and perspectives on the direction of the M&A market in 2016 and beyond. The following charts present their collective input as well as added insights.

Where appropriate, we also share some year-over-year data from past surveys, to show how sentiments have changed. An overview of the survey methodology can be found at the end of this report.

Q1. How will the U.S. M&A market for the next 12 months compare to the last 12 months?		
Responses	**%**	**Percentage of total respondents**
Market will strengthen in the next 12 months	33.33%	
Market will see no significant change in the next 12 months	47.22%	
Market will weaken in the next 12 months	19.44%	
		20% 40% 60% 80% 100%

- We asked this question for the third consecutive year – and we've seen a consistent decline in optimism, from 59 percent of respondents who predicted a strengthening market in 2014 to 37 percent in 2015 to 33 percent this year.
- Still, less than 20 percent of respondents this year and last said the market would weaken – and this year reveals a 4 percentage point increase in those who expect no significant change. Less than 10 percent of 2014 respondents said the market would weaken.
- Deloitte's 2016 annual surveys over the past three years have produced similar results. Each year, 84 to 87 percent of respondents to that survey predicted an increase or little or no change in the average number of deals their companies would pursue in the following 12 months.[1]
- Despite the drop in optimism, the dollar volume of M&A activity in North America in 2016 rose steadily from the third quarter of 2015, peaking in this year's second quarter. At the same time, however, the number of deals has fallen sharply.[2]

Q2. Which of the following is most responsible for fueling current U.S. M&A activity?		
Responses	**%**	**Percentage of total respondents**
Availability of capital	48.61%	
Favorable interest rates	25.00%	
Financial markets	8.33%	
General U.S. economic conditions	18.06%	
Other (Please specify)	0%	
		20% 40% 60% 80% 100%

- Availability of capital was the top choice for the third straight year.

[1] Deloitte, M&A Trends Report 2016, http://www2.deloitte.com/us/en/pages/mergers-and-acquisitions/articles/ma-trends-report.html

[2] PitchBook, M&A Report 3Q 2016, http://pitchbook.com/news/articles/a-visual-summary-of-ma-activity-in-3q-datagraphic

- The percentage of respondents who chose favorable interest rates jumped for the third straight year – despite the Federal Reserve's December 2015 decision to raise interest rates for the first time in nearly a decade.[3]
- It's possible that respondents answered this way because they believe dealmakers made moves recently so they can get in front of another rate hike before it affects valuations. In August, Federal Reserve Chair Janet Yellen said "the case for an increase in the federal funds rate has strengthened in recent months."[4]
- General U.S. economic conditions remained the third most cited reason, but it dropped from 25 percent in 2014 and 22 percent last year.

Q3. What sources of financing did you or your clients most frequently use for M&A transactions that closed in the last 12 months? (Please rank top 3)	
Answer	**Weighted Rank**
Cash	1
Investor funds (such as private equity)	2
Term loans	2
Revolving lines of credit	3
Subordinated debt	4
Seller financing	5
Stock/equity issued to seller	6
Privately placed notes	7
Publicly placed bonds	8

- This year's rankings mirrors 2014 and 2015. Only investor funds (such as private equity) and term loans have seen any movement in the past three surveys.
- Deloitte's 2016 survey found that available cash would be the top funding source for respondents' M&A investments. However, the percentage who responded that way has dropped from 58 percent in 2014 to 47 percent this year – with proceeds from new equity issuance and debt issuance gaining ground.[5]

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[3] *The New York Times*, December 16, 2015, "Fed Raises Key Interest Rate for First Time in Almost a Decade," http://www.nytimes.com/2015/12/17/business/economy/fed-interest-rates.html
[4] CNN Money, August 26, 2016, "Janet Yellen says Fed rate hike odds have 'strengthened,'" http://money.cnn.com/2016/08/26/news/economy/janet-yellen-federal-reserve-jackson-hole/
[5] Deloitte, M&A Trends Report 2016, http://www2.deloitte.com/us/en/pages/mergers-and-acquisitions/articles/ma-trends-report.html

Q4. Do you expect there to be an increase in M&A activity involving privately-owned businesses in the next 12 months?		
Responses	**%**	**Percentage of total respondents**
Yes	68.06%	
No	31.94%	
		20% 40% 60% 80% 100%

Q5. Why?		
Responses	**%**	**Percentage of total respondents**
Aging business owners seeking to sell	30.61%	
Concerns about the window closing	28.57%	
Current earnings are stable	2.04%	
Current earnings are increasing	6.12%	
Current earnings are decreasing	0%	
Improving valuations	12.24%	
Concerns about declining valuations	16.33%	
Other (Please specify)	4.08%	
		20% 40% 60% 80% 100%

Q6. Why not?		
Responses	**%**	**Percentage of total respondents**
Building retirement	4.35%	
Current earnings are trending stable	26.09%	
Current earnings are increasing	0%	
Current earnings are decreasing	8.70%	
Hoped for greater increases in value	13.04%	
Inertia	13.04%	
Other retirement savings	0%	
Uncertainty on future life transition plans	4.35%	
Other (Please specify)	30.43%	
		20% 40% 60% 80% 100%

- While the respondents answering “yes” to this question outnumbered those saying “no” by more than 2-to-1, the results showed a continued drop from the 82 percent who said “yes” in 2014.

- Terrel Bressler of Prairie Capital Advisors echoed the top answer for respondents who answered "yes." In the last 12 months his company has worked with several privately-owned businesses moving to sell – largely because of the owners' advanced ages. "When you're 83, you might not have 10 more years in you, so maybe you're thinking of retiring and leaving something to your family while the returns are still good."
- One respondent who predicts there would not be an increase in sales explained: "Companies that had been contemplating M&A activity (sales) accelerated their activity into 2014-2016. We are seeing some technical weakness as the best, strongest companies have transacted. That leaves somewhat lower-quality companies to come to market."

Q7. In recent years, the media and market analysts have speculated that as privately-owned businesses are passed to a new generation of owners, the U.S. is likely to see significant "baby boomer" sales of family-businesses. When do you believe that trend will start in earnest?

Responses	%	Percentage of total respondents
It's already happening	36.11%	
It will happen in the short term (first half of 2017)	8.33%	
It's more likely to be a mid-term trend (late 2017 to 2018)	8.33%	
It's a long-term trend (2019 or later)	9.72%	
Rather than a rush of family-owned business sales, we will see a slow trickle over the next decade	37.50%	
		20% 40% 60% 80% 100%

- This question sought to determine when respondents believe the wave of family-owned business sales would start. Although there wasn't a clear winner, a slow trickle was the most widely held belief.
- As Bressler put it, when it comes to some business owners, "80 is the new 60."

Q8. Which of the following types of buyers have most influenced U.S. deal valuation over the past 12 months?

Responses	%	Percentage of total respondents
Financial U.S. buyers	48.61%	
Foreign buyers	6.94%	
Strategic U.S. buyers	43.06%	
None of the above	1.39%	
		20% 40% 60% 80% 100%

- For the first time since 2008, financial buyers topped strategic buyers, though by a slim margin.
- It's possible that the change is a result of increasingly murky distinctions between strategic and financial buyers. Financial buyers (such as private equity firms) might own several platforms in the same industry and function like strategic buyers when making further acquisitions in that space, though technically they would be considered financial buyers.

- One respondent who believes financial buyers were more influential said, “A lot of money on the sidelines needs investing and the public markets are topping; hence private M&A will pick up.” Another said, “Availability of capital (demand) in concert with the lack of quality targets (supply) coupled with historically low interest rates.”
- For strategic buyers, acquisitions were still viewed by some respondents as the best way to grow. “As the number of reasonably priced companies has declined, strategic buyers have stepped to the front of the line because they are better able to justify paying the lofty multiples being seen currently,” said one respondent.

Of the following categories of buyers, which will most increase and which will most decrease its U.S. M&A market presence over the next 12 months (as a percentage of total transactions)?		
Q9. Select one option		
	Increase Most	**Decrease Most**
Strategic U.S. Buyers	84.62%	15.38%
Financial U.S. Buyers	60.47%	39.53%
Foreign Buyers	29.41%	70.59%

- Interestingly, respondents predict a return to strategic dominance in the next 12 months. One respondent said, “Strategics have the cash and liquidity to undertake M&A, and financial U.S. buyers will pull back to let the post-election dust settle.” Another said that “private equity is overheated.”
- One respondent said, “Strategic buyers buy on the basis of need and opportunity. Financial buyers buy only on expectations of oversize profits. With higher interest rates and tax changes, they will take a wait-and-see approach.”
- “Financial buyers might have been more influential in the past 12 months because of increased interest in companies with annual earnings of less than $5 million from private equity firms,” said Aaron Witalec of UHY Advisors Corporate Finance. “They’re coming down-market and influencing the valuations versus strategics. As a result, strategics are slowing down their bidding and focusing more on inward operations.”

Q10. What are the most common obstacles you have experienced in deals in the past 12 months? (Please rank top 3)	
Answer	**Weighted Rank**
Valuation	1
Availability of quality target	2
Buyer competition	3
Due diligence	4
Financing	5
Other	6
Increased antitrust enforcement	7

- These findings were exactly in line with the 2015 results. As one respondent put it, “There are a large number of private equity groups chasing a limited pool of attractive candidates. This is pushing valuations to highs.”
- Joe Baratta, Blackstone Group LP’s top private equity dealmaker, mentioned difficulties with high valuations at a private equity analyst conference in September. “You have historically high multiples of cash flows, low yields. I’ve never seen it in my career. It’s the most treacherous moment.”[6]

Q11. Are you conducting any of the following activities during the due diligence process regarding cybersecurity? (Please select all that apply)		
Responses	**%**	**Percentage of total respondents**
Assessing data security measures with third-party vendors	31.37%	
Checking for internal policies that protect confidential or proprietary information	72.55%	
Determining whether compliance policies include breach notification protocols	33.33%	
Learning who is responsible for data privacy compliance	50.98%	
Ascertaining which types of information the company maintains	60.78%	
Verifying a target's cyber-insurance policy	33.33%	
		20% 40% 60% 80% 100%

- We asked this question for the first time in 2015, and the results have shifted in several ways.
- We were surprised by the low percentage of respondents assessing data security measures with third-party vendors, lower than the 42 percent of respondents who said they were in last year’s survey. The percentage of respondents ascertaining which types of information the company maintains also dropped.
- “Attention to internal policies is up substantially, suggesting that those wishing to maximize enterprise value could benefit from a review of their data security policies and practices to be sure that they are due-diligence ready,” said Stephen Tupper, a Dykema member who leads the firm’s Privacy, Data Security and E-Commerce practice.
- A recent survey by West Monroe Partners found that 80 percent of North America-based M&A practitioners believe cybersecurity issues have become highly important during due diligence. But 40 percent of acquirers had discovered a cybersecurity problem after a deal went through, indicating that standards remain low.[7]

[6] Bloomberg, “Blackstone’s Top Dealmaker Says Now Is The Most Difficult Period He's Ever Experienced,” September 27, 2016, http://www.bloomberg.com/news/articles/2016-09-27/blackstone-s-baratta-says-now-is-the-most-treacherous-time-ever

[7] West Monroe Partners, Testing the Defenses: Cybersecurity Due Diligence in M&A, http://www.westmonroepartners.com/Insights/White-Papers/security-survey

Q12. Please rank the following in terms of potential impact on the global M&A market. (Please rank top 3)	
Answer	**Weighted Rank**
Change in Federal Reserve's stated interest-rate outlook	1
Decline in Chinese/Asian economies	2
Eurozone economic instability and Brexit-driven changes	3
Increase in conflict in the Middle East	4
Increase in terrorist activities	5

- For the second straight year, respondents cited the Fed's stated interest-rate outlook and economic issues in China/Asia as their top two concerns, despite continued conflict in the Middle East and a spate of terrorist attacks around the world.
- Surprisingly, European uncertainty and Brexit – shorthand for Britain's June vote to leave the European Union – ranked third, despite serious concerns by dealmakers prior to the vote. Sixty-seven percent of respondents to a survey published in June by Intralinks predicted Brexit would have a negative effect on M&A levels across Europe.[8]
- UK involvement in deal making is down significantly. While it typically accounts for around 10 to 20 percent of global activity, the UK's involvement fell to around 8 percent through the first eight months of the year, according to data from Thomson Reuters.[9]
- William Schulz, head of M&A for Citigroup in Europe, the Middle East and Africa, said activity levels had recovered since the June exit vote. "We haven't really seen the Brexit effect yet. The UK used to be the capital of choice for listing and incorporating a newly formed company. Now, although companies still want to be listed there, they are concerned about regulatory and tax risks."[10]

Q13. What are the leading drivers of cross-border deals today? (Please rank top 3)	
Answer	**Weighted Rank**
Companies seeking growth via entrance in foreign markets	1
Customer demand for local presence in foreign markets	2
Companies seeking lower labor costs	3
Companies seeking proximity to suppliers and materials	4
Companies seeking lower tax rates/inversions	5
Companies seeking new intellectual property	6
Companies seeking access to raw materials or natural resources	7

- This question had some new options for answers in 2016, but companies seeking growth via entrance in foreign markets remained the top choice for the third straight year.
- While low yields remain a common challenge in the current marketplace, making acquisitions holds appeal as one sure way to spur growth.

[8] Intralinks Blog, June 20, 2016, "Brexit: Will It Sink the European M&A Ship"?, https://blogs.intralinks.com/2016/06/brexit-will-sink-european-ma-ship/?_ga=1.157169528.2132481741.1475185608

[9] *Financial Times*, September 29, 2016, "Dealmaking falls to three-year low," https://www.ft.com/content/10fb809e-8648-11e6-a29c-6e7d9515ad15

[10] Ibid.

Q14. What are the leading impediments to cross-border deals today? (Please rank top 3)	
Answer	**Weighted Rank**
Lack of experience managing international operations	1
Foreign political instability	2
Currency fluctuations	3
FCPA and other compliance-related risks	4
Inability to access affordable local currency financing	5
Concerns about damage to public image	6

- Lack of experience is likely most pronounced for small and middle-market companies making their first forays overseas, possibly forced by competitive pressures to look abroad.
- Despite global instability, companies still look to international deals to spur growth. Alasdair Warren, head of investment banking across Europe at Deutsche Bank, said, “Most of the developed world is short of growth, but long (on) low-cost capital. The recent data suggest we are likely to see rate rises in the U.S., but it’s clear that the pace of rate increases thereafter will be very slow. In Europe, we will be in low-growth and low- or negative-rate territory for the foreseeable future. That means corporates are going to have to continue to look at M&A to drive growth and returns.”[11]

Which regions will experience an increase in inbound/outbound U.S. M&A activity in the next 12 months?		
Q15. Select all that apply		
	Inbound to U.S.	**Outbound from U.S.**
Australia	54.17%	58.33%
Brazil	41.94%	67.74%
Canada	66.67%	61.54%
China	88.00%	22.00%
Europe	61.67%	61.67%
India	60.47%	60.47%

[11] *Financial Times*, September 29, 2016, “Taste remains for the big cross-border deal,” https://www.ft.com/content/3233ecde-865b-11e6-a29c-6e7d9515ad15

Iran	50.00%	60.00%
Japan	80.95%	28.57%
Korea	61.11%	44.44%
Mexico	27.91%	76.74%
Middle East	72.00%	32.00%
Russia	60.00%	53.33%
South/Central America	33.33%	72.73%

- Expectations for inbound M&A activity to the U.S. were higher compared with 2015's survey from every country except Australia and Mexico, possibly as dealmakers look for better returns in a steady U.S. economy.
- This year's survey saw an increase in U.S. companies anticipating activity in Canada. "This is likely driven by investors looking to Canada as they seek safer – and more familiar – bets internationally," said Richard Goetz, who leads Dykema's International Practice Group.
- Expected M&A activity from China to the U.S. rose sharply. This may indicate that Chinese investors are more accustomed to Committee on Foreign Investment in the United States requirements, and it may reflect their ability and desire to get money out of China. However, expected U.S. activity in China remained low for the second straight year – possibly stemming from a larger economic slowdown in China and some political concerns, including China's conflicts with other nations in the Pacific.
- Respondents think investments from Japan and Korea will also increase, likely due to lower growth in those countries and the large amounts of capital residing there.
- Despite some concerns about how Brexit would affect the M&A space, expected U.S. M&A activity to Europe went up. That could indicate that dealmakers are taking a short-term view, possibly in light of favorable exchange rates.
- Expected outbound activity from the U.S. to Mexico increased from 2015, likely a result of proximity – even if making goods in some Asian countries is less expensive. Mexico is becoming an attractive alternative as cost differences with China diminish.

Have any of the following political issues impacted your company's deal-making in 2016? Q16. Please select all that apply					
	No	**Yes, made acquisition**	**Yes, divested**	**Yes, delayed acquisition**	**Yes, delayed divestiture**
Cybersecurity Act and/or other related regulations	96.36%	0%	0%	3.64%	0%
Healthcare reform	77.59%	10.34%	1.72%	12.07%	1.72%
Brexit	85.00%	3.33%	0%	11.67%	1.67%
Uncertainty about the presidential election	78.57%	1.79%	1.79%	14.29%	3.57%
Financial institution regulatory reform	76.79%	3.57%	1.79%	17.86%	3.57%
Uncertainty about the congressional election	89.09%	0%	1.82%	9.09%	0%
Overtime regulations	78.57%	3.57%	0%	14.29%	3.57%
Antitrust enforcement	82.76%	1.72%	0%	13.79%	1.72%

- Surprisingly, most respondents answered "no" when asked whether any of the above political issues had affected deal-making in 2016.
- Financial institution regulatory reform has had the most impact of the choices on this list, with 18 percent of respondents saying it had delayed an acquisition.
- The upcoming presidential election, healthcare reform, upcoming changes to U.S. overtime regulations, antitrust enforcement and Brexit were the only other options that more than 10 percent of respondents said were responsible for delaying deals.

Q17. Which presidential candidate, if elected, do you believe would support more policies favorable to the U.S. M&A market?		
Responses	**%**	**Percentage of total respondents**
Hillary Clinton	31.15%	
Donald Trump	68.85%	
		20% 40% 60% 80% 100%

- Many respondents explained their answers by noting Trump is a businessman or that Clinton would overregulate. As one respondent said, “As an experienced business person, Trump has an understanding of what drives capital formation and economic growth.”
- Another respondent said, “Among politicians, M&A equates to consolidation. Hillary Clinton is not likely to act much in favor of that.” But some respondents clearly preferred Clinton, citing her experience and overall stability. “Clinton will support more of the same. God knows what Trump will do.” Another said, “Both candidates are extremely weak but Clinton is less likely to derail the economy or create crisis.”
- Digging deeper, while respondents may feel Trump would support more policies favorable to the U.S. M&A market, overall respondents didn’t feel either candidate would significantly impact the market in either direction. Forty-nine percent of respondents said they felt Clinton would have a neutral effect on the M&A market and 47 percent said the same for Trump.

Q18. What impact would the election of each presidential candidate have on the U.S. M&A market in 2017?		
	Hillary Clinton	**Donald Trump**
Positive	19.15%	27.91%
Neutral	48.93%	46.51%
Negative	31.91%	25.58%

- Respondents who provided more detail did so in somewhat predictable ways: Trump’s business background was mentioned by supporters, while his perceived instability, lack of understanding of issues and uncertainty around some of his positions were mentioned by detractors.
- Regarding Clinton, one respondent said, “Democrats as a whole are not pro-business, only pro-tax (both investment side and producer side).”
- As Rick Lacher of Houlihan Lokey put it, “I think people view Trump as a loose cannon – and they don’t know what we would get if he’s elected. With Clinton, you’re looking at higher taxes and more anti-trust review.”

Q19. Rate the likely impact of each of the following potential issues on the U.S. M&A market in 2017.					
	Significant positive impact on M&A Market	**Somewhat positive impact on M&A market**	**No notable impact on M&A market**	**Somewhat negative impact on M&A market**	**Significant negative impact on M&A market**
Corporate tax increases	5.97%	4.48%	14.93%	43.28%	31.34%
Corporate tax decreases	31.25%	51.56%	12.50%	3.13%	1.56%
Personal income tax increases	8.96%	7.46%	34.33%	35.82%	13.43%
Personal income tax decreases	16.92%	41.54%	33.85%	6.15%	1.54%
Taxation of carried interest	4.69%	14.06%	21.88%	42.19%	17.19%
Increase in federal deficit spending	2.99%	14.93%	32.84%	40.30%	8.96%
Increased federal regulation of business	2.99%	10.45%	17.91%	43.28%	25.37%
Increase in the minimum wage	2.99%	10.45%	32.84%	47.76%	5.97%
Partisan gridlock in Congress	6.06%	4.55%	50.00%	27.27%	12.12%
Increased U.S. trade barriers and/or repeal of trade treaties	4.48%	17.91%	19.40%	34.33%	23.88%

- Respondents were most concerned about the possibilities of corporate tax increases and increased federal regulation on business. They also noted the possibility of raising the minimum wage – which Clinton supports. She has said she would sign a bill that would gradually increase the rate to $15 an hour.[12]
- Interestingly, many respondents were concerned that federal deficit spending – which some experts say can provide short-term benefits to the economy – would have a negative effect on the U.S. M&A market. This could stem from a belief that a net effect would be to artificially inflate the value of companies with already high valuations, or that taxes would eventually be increased to pay down deficits.
- The possibility of taxation of carried interest also caused consternation, possibly because both candidates support repealing the deductions. But the candidates' stance hasn't seemed to shake venture capitalists. Repealing carried-interest deductions is "politically expedient to talk about. But I think there are bigger and better things for the candidates to focus on after the election," said Yael Hochberg, an associate professor of entrepreneurship at Rice University.[13]

In the next 12 months, do you believe your company, or one of your portfolio companies, will be involved in any of the following transactions?			
Q20. Select one option for each.			
	Yes	**No**	**Not applicable**
Acquisition	70.31%	10.94%	18.75%
Joint Venture	42.59%	31.48%	25.93%
Sale	48.39%	29.03%	22.58%

- Compared with last year, positive responses went up across the board on this question, though only slightly. Sixty-seven percent of 2015 respondents said they would be involved in an acquisition, compared with 70 percent this year. Thirty-four percent of 2015 respondents said they'd be involved in a joint venture, compared with 43 percent this year, and 42 percent predicted in 2015 that they'd be involved in a sale, compared with 48 percent this year.
- This is a sign of a steady market, despite the overall drop in optimism about M&A in the survey's top finding. "I was at a conference recently and there was a lot of buzz – people were saying they're busy with deals, just like we are. I think it's going to stay busy until at least the first or second quarter of 2017," Terrel Bressler said.

[12] *The Huffington Post*, April 17, 2016, "Hillary Clinton Clarifies Her Stance on Minimum Wage," http://www.huffingtonpost.com/entry/hillary-clinton-minumum-wage_us_57139f45e4b06f35cb6fd5da

[13] *TechCrunch*, August 11, 2016, "Both Trump and Clinton are taking on carried interest, so why aren't investors nervous?" https://techcrunch.com/2016/08/11/both-trump-and-clinton-are-taking-on-carried-interest-so-why-arent-investors-nervous/

Q21. What is your outlook for the U.S. economy, generally, over the next 12 months?		
Responses	**%**	**Percentage of total respondents**
Positive	27.78%	
Neutral	54.17%	
Negative	18.06%	
		20% 40% 60% 80% 100%

- There was a marked decline from last year in the percentage of respondents who were positive about the economy – from 48 percent in 2015 to 28 percent this year. But most of the difference stems from the percentage of respondents who chose neutral – which jumped from 37 percent to 54 percent.
- Rick Lacher said this is another reason to believe no one thinks the sky is falling, despite some concerns. “When I look at the market today, there’s nothing that would give you a strong feeling either way about what’s going to happen. Even in 2005-06 – a year or two before the recession began – we knew it could not last.”
- The U.S. economy grew at 1.4 percent in the second quarter of 2016, following two quarters of sub-1 percent growth.[14]

Q22. How will the U.S. economy for the next 12 months compare to the last 12 months?		
Responses	**%**	**Percentage of total respondents**
U.S. economy will improve over the next 12 months	25.00%	
U.S. economy will see no significant change over the next 12 months	50.00%	
U.S. economy will worsen over the next 12 months	25.00%	
		20% 40% 60% 80% 100%

- In another sign of waning optimism, just 25 percent of respondents said the U.S. economy would improve, compared with 38 percent in 2015 and more than 50 percent in 2013 and 2014.
- The levels of pessimism and neutrality both rose 7 percentage points this year.

[14] ABC News, September 29, 2016, “US Economy Grew at 1.4 Percent Rate in Spring,” http://abcnews.go.com/Business/wireStory/us-economy-grew-14-percent-rate-spring-42444346

Q23. Record M&A reports over the past few years were driven largely by megadeals rather than small- and mid-market transactions. What is your prediction for the volume of small, mid-market and megadeals in the next 12 months compared to the previous 12 months?				
	M&A deals under $50m	**M&A deals $50m-$100m**	**M&A deals $100m-$1b**	**M&A deals over $1b**
There will be an increase in deals over the next 12 months	72.22%	55.56%	31.48%	35.19%
Deal volume will not change significantly	32.73%	47.27%	61.82%	45.45%
There will be a decrease in deals over the next 12 months	20.69%	13.79%	27.59%	48.28%

- Small deals are expected to lead the way over the next 12 months, according to 72 percent of respondents. This could tie into the general belief that family business owners are more likely to sell.
- Terrel Bressler said some business owners could be trying to sell before the end of the year, concerned that tax increases (notably, capital gains) could pass in early 2017 and be made retroactive to the beginning of the year. "One of my clients doesn't want to wait until March to sell," Bressler said.
- Were these predictions to come true, they would seem to buck the trend of the past year, in which deal volume has dropped but the dollar-value of deals has largely held steady.

Q24. Of the following sectors, in which one do you expect to see the most M&A activity in the next 12 months?	
Answer	**Weighted Rank**
Energy	1
Healthcare	2
Automotive	3
Technology	3
Industrial/Manufacturing	4
Financial Services	5
Medical Devices	6
Pharmaceutical	6
Consumer Products	7
Real Estate and Construction	7
Insurance	0
Law	0
Logistics and Transportation	0
Media and Entertainment	0

- Energy jumped two spots compared to 2015 results, possibly because over-leveraged companies in oil and gas are seeking buyers. But after a spate of bankruptcies in 2016, that might be fading, Rick Lacher said. “We are starting to see some signs of health in oil and gas as we’re seeing private equity commit substantial dollars to exploration and production investments.”
- Healthcare, technology and automotive continued to generate optimism, as did the industrial and manufacturing sectors. “The majority of what we’ve been working on has been in manufacturing and distribution. Those areas are pretty good and pretty strong,” Terrel Bressler said.

Methodology

In September 2016, national law firm Dykema Gossett PLLC distributed its M&A Outlook Survey via email to a group of senior executives and advisors including CEOs, CFOs and other company officers. The respondents to the survey represent a cross-section of M&A professionals and advisors with a diverse group of professions and more than a dozen sectors represented, including healthcare, technology, industrial/manufacturing and financial services. Respondents represent companies whose annual revenues range from under $1 million to more than $1 billion. Percentages in questions 11, 15 and 16 exceed 100 percent because respondents were asked to check “all that apply.” Due to rounding, percentages used in some questions may not add up to 100 percent. A few minor edits were made to individual responses to correct spelling, punctuation and verb tense.