William Blair

# Key Themes for Public Company Board Agendas to Close Out 2022

## William Blair's Corporate Advisory team examines how shifts in the equity markets, macroeconomic environment, and M&A landscape are affecting public company board agendas for the months ahead.


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Public companies faced an extremely challenging equity market during the first nine months of 2022, with the S&P 500 and Nasdaq declining approximately 25% and 33%, respectively through September 30.[1] Signs of stabilization were beginning to emerge in late July before stocks abruptly retreated again in August and September. Looking ahead, public companies still face a difficult mix of positive and negative market signals.

Positive signs include better-than-feared earnings in many instances, "green shoots" in selected areas of equity issuance activity, and some evidence of slowing inflation in the United States. On the negative side, U.S. recession fears have grown as interest rates have risen sharply, and the economic outlook in Europe—as well as China—is even more bleak.

Across the mergers and acquisitions (M&A) landscape, appetite and engagement are subdued and buyers are recalibrating valuation expectations. Public boards are still trying to contextualize how to address several factors, including: the ongoing convergence of private and public company valuations, the disconnect between first half 2022 M&A activity vs. the outlook for the rest of the year, headwinds accessing additional equity and debt capital, and a generally more risk-averse mindset and focus on cash preservation from large strategics.

Amid this challenging backdrop, what themes should be on the radar for the rest of the year? Below, William Blair's Corporate Advisory team highlights three key areas of attention for public company boards and executive management teams.

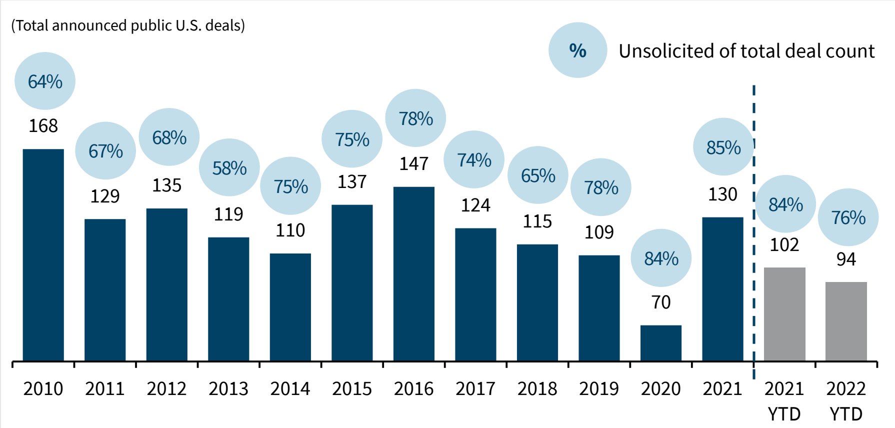
### Take-Private and Public Company Sale Activity Is Still Elevated

Despite the broadly subdued M&A environment, public company sale activity for the first nine months of 2022 has remained broadly intact. For example, U.S. public company sale activity has only decreased 8% on a year-over-year basis, while broader M&A activity is down approximately 30%.[2]

There continue to be numerous noteworthy sales of U.S. public companies across all sectors of the economy, with both private equity firms and a select group of strategics seeking to capitalize on the broader public equity market dislocation. A few recent examples in the latter part of the third quarter include the $3.0 billion acquisition of Ping Identity (technology) by Thoma Bravo; the $5.2 billion acquisition of Atlas Air (industrials) by an investor group led by Apollo; and the $8.0 billion acquisition of Signify Health (healthcare) by CVS.

1. Source: CapitalIQ.
2. Source: CapitalIQ as of September 30, 2022. Represents all U.S. transactions with a transaction value greater than $50mm.

## Public Company Sale Activity[3]




### Selected Q2-Q3 2022 Take-Private Transactions[4]

| Announcement Date (2022) | Transaction Value (Approximations, $ billions) | Target | Acquirer |
|---|---|---|---|
| April 25 | 44.0 | Twitter | Elon Musk |
| May 11 | 11.0 | Switch | DigitalBridge, IFM |
| June 24 | 10.2 | Zendesk | Hellman & Friedman, Permira |
| August 8 | 8.4 | Avalara | Vista |
| April 7 | 8.3 | CDK Global | Brookfield |
| April 11 | 6.9 | SailPoint Technologies | Thoma Bravo |
| August 4 | 5.2 | Atlas Air | Apollo, JF Lehman, Hill City |
| May 16 | 4.2 | ManTech | Carlyle |
| May 25 | 4.0 | Covetrus | TPG, CD&R |
| August 3 | 2.8 | Ping Identity | Thoma Bravo |

### Selected Q2-Q3 2022 Strategic Acquisitions of Public Companies[5]

| Announcement Date (2022) | Transaction Value (Approximations, $ billions) | Target | Acquirer |
|---|---|---|---|
| May 26 | 69.0 | VMware | Broadcom |
| May 4 | 16.0 | Black Knight | Intercontinental Exchange |
| May 10 | 11.6 | Biohaven Pharmaceutical | Pfizer |
| September 5 | 8.0 | Signify Health | CVS Health |
| July 28 | 7.6 | Spirit Airlines | JetBlue Airways |
| April 11 | 6.2 | Datto | Kaseya |
| May 10 | 4.1[6] | Tingo | MICT |
| July 21 | 3.9 | One Medical | Amazon |
| August 4 | 3.7 | ChemoCentryx | Amgen |
| June 3 | 3.2 | Turning Point Therapeutics | Bristol Myers Squibb |

M&A activity has remained elevated at public companies for a few key reasons:

- Many public targets are growth-oriented but require capital to fund investment and a runway to profitability. Such companies have begun to recalibrate valuation expectations in the face of an extended downturn in equity markets and are no longer benchmarking to 2021 share prices, as many start to appreciate the time horizon and execution risk (including cost of capital) to re-achieve such valuations.
- Although recent results were better than expected, medium-term operational headwinds remain for many strategics, posing challenges for management teams seeking to perform in accordance with stand-alone management plans. In third quarter 2022, 154 companies lowered guidance compared to 78 in third quarter 2021 and a third quarter average of approximately 90 companies from 2012–2019.[7]
- Private equity sponsors still have an enormous amount of dry powder to deploy—estimated at approximately $1.3 trillion globally[8]—and many PE firms are coordinating dedicated "SWAT teams" to evaluate public opportunities amid ongoing market volatility. A significant portion of the dry powder has been raised over the last few years, requiring financial sponsors to demonstrate to LPs their ability to continue to deploy capital across various economic cycles.
- While strategics generally are being more cautious in this market environment, many are still willing to act opportunistically for must-have assets in order to avoid losing out to sponsors or competitors.

Going forward, tailwinds for public company sale activity remain in place, including a sizable universe of recent IPOs that have underperformed the broader market and, in certain instances, still have meaningful private equity ownership.

3. Source: CapitalIQ as of September 30, 2022. Represents total transactions announced and unsolicited offers for public U.S. companies with market capitalization greater than $50mm. Excludes cancelled transactions and transactions in Real Estate, Oil & Gas, and Financial Institutions sectors.
4. Source: Company SEC filings.
5. Source: Company SEC filings.
6. Transaction value quoted is the value of the combined company.
7. Source: CapitalIQ.
8. Source: PitchBook Data, Inc. as of September 30, 2022.

Further, buyers are viewing take-private opportunities in three thematic categories in the current market environment:

1. Misunderstood equity stories (i.e., attractive relative valuation plays)
2. Cost take-out and operational enhancement opportunities
3. Transformation stories that require capital and are better executed in the private markets

## Portfolio Optimization Remains a Focus for Large Corporations

In William Blair's April 2022 report, we discussed the importance of portfolio optimization this year. Investors have rewarded streamlined businesses, and corporations have capitalized on the record M&A environment to execute such transactions.

Nine months into 2022, tailwinds remain for portfolio optimization and divestiture activity despite the more subdued M&A environment. What is maintaining this momentum?

**From the perspective of strategics looking to potentially sell assets, factors contributing to portfolio optimization activity include:**

- Pure-play businesses are still being rewarded in the market, and they remain well-positioned operationally.
- Rather than pursuing growth aggressively, public companies have taken a more conservative turn in their capital allocation frameworks toward both maximizing cash flow and prioritizing cash investments.
- Barriers to entry and requisite investment between winners and midtier players have widened, partly due to companies' varying abilities to develop differentiating technology.

**From the perspectives of private equity firms and strategics looking to potentially buy assets, factors contributing to portfolio optimization activity include:**

- The universe of private equity parties with deep expertise in carve-outs has been growing rapidly.
- In addition to the number of parties involved, today's private equity community is characterized by greater sophistication in potential transaction structuring (e.g., seller financing and partial ownership stake roll-overs). A recent example of this trend is Treehouse Foods' August 2022 divestiture of its meal prep unit to Investindustrial, which included seller financing.
- Both strategic and private equity portfolio companies are continuing roll-up and consolidation strategies by taking advantage of carve-out opportunities.

In this environment, public company boards are taking a refreshed stance regarding the potential categorization of assets when conducting strategic portfolio reviews. More specifically, when companies are evaluating "semi-core" assets (i.e., business units that will either receive accelerated investment or be divested of), there is an increasing inclination to designate assets as non-core (exit opportunities) versus core (opportunities to deploy growth capex). The return threshold for corporates to invest in these sub-businesses has increased along with a more acute focus on cash preservation. That being said, designating a clear value-accretive use of proceeds remains a key factor when evaluating portfolio optimization candidates.

Turning to divestiture activity, carve-out activity remains substantial this year relative to last year. In the United States, there have been 803 corporate divestiture transactions in the first three quarters of 2022 compared to 838 divestitures during the same period in 2021.[9] Recent transactions of note include Whirlpool's acquisition of Emerson Electric's InSinkErator business for $3 billion and New Mountain Capital's acquisition of Perkin Elmer's Applied Food and Enterprise Services business for $2.5 billion.

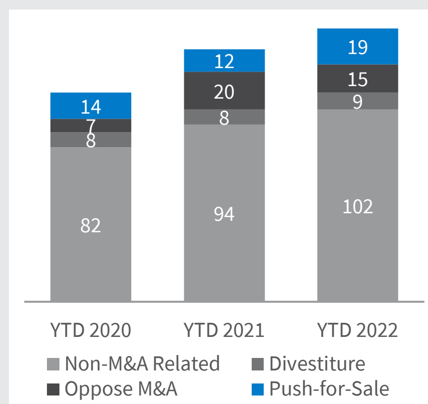
## Activism Activity Persists as Macro Headwinds Reshape the Playbook

Throughout 2022, activism activity has remained elevated. In the first three quarters of the year, there were 1,223 activist campaigns globally versus 1,026 campaigns during the same period in 2021.[10]

A key factor driving this year's activism activity is that 10 quarters of post-COVID results have fully revealed which companies are operational laggards. Many operational underperformers are at further risk today because they lack the protection of an elevated valuation environment.

In addition to private equity firms and well-capitalized strategics, activists also are trying to capitalize on this year's equity market dislocation. As a result, "push-for-sale" activist campaigns have been elevated in year-to-date 2022. There have been 19 such campaigns thus far in 2022 compared to full-year totals of 25 campaigns in 2020 and 22 campaigns in 2021.[11] Moreover, activists tend to move quickly on push-for-sale campaigns, with over half of such campaigns being initiated within 90 days of an activist's position being made public.[12] Many activists see the recent market sell-off as an entry point and are seeking opportunities to catalyze attractive returns in the near term with robust M&A premiums.

### Elevated Activism Activity in 2022 Includes Heightened Focus on Push-for-Sale [13]




Another noteworthy recent trend is the convergence of private equity and activism. Recent examples include Elliot Management/Evergreen Coast Capital's campaigns and ultimate acquisitions of Nielsen Holdings and Citrix earlier this year. With dry powder still seemingly robust, tailwinds remain for private equity firms to deploy the activist toolkit to unlock potential take-private opportunities.

9. Source: Dealogic. Only includes U.S. divestments; excludes SPACs and spin-offs. Includes only 100% acquisitions. Excludes financial sponsor exits. Excludes deals in the real estate/property operators sector. Excludes deals where the divestor's primary industry is finance, acquisitions, or restructurings.
10. Sources: Insightia.
11. Sources: Insightia and William Blair. Includes U.S. companies with a market cap greater than $500 million.
12. Source: Insightia, "Opportunity knocks for dealmaking activists," August 26, 2022.
13. Source: Insightia as of September 30, 2022. US companies only with a market cap of $500M+. Non-M&A related campaigns excludes campaigns categorized as ESG and renumeration.

## How Do These Themes Affect Your Company?

William Blair's Corporate Advisory team would welcome the opportunity to share our perspectives and discuss how these opportunities and challenges apply to your company. Please do not hesitate to reach out if you are interested in continuing the conversation.

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