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Dealmakers See Robust Year Of Tech M&A Ahead

By **Chelsea Naso**

Law360, New York (May 2, 2017, 12:09 PM EDT) -- Technology M&A may have gotten off to a slow start in 2017, but dealmakers anticipate a surge in tie-ups in the coming months amid economic confidence, the pursuit of innovation in other industries, and growing interest from financial sponsors.

About 52 percent of respondents — which includes a pool of corporate development officers, lawyers, bankers and other tech-focused dealmakers — anticipate an increase in U.S. tech M&A throughout the rest of 2017, according to the semi-annual M&A Leaders Survey produced by Morrison & Foerster LLP and 451 Research.

The upbeat outlook comes in spite of a slow start to the year for tech M&A in terms of deal flow. There were 912 deals worth $77 billion announced during the first quarter of 2017, down from the 1,065 deals worth $74 billion inked in the first three months of 2016, according to the report.

With the positivity embraced by a majority of tech-focused dealmakers stemming from a variety of sources, it's more than likely that the coming year will yield a tech M&A boom.

"It's a mix of factors that are hitting the tech industry from a global basis, and then you've got some drivers that are more particular to tech that are playing out and will probably result in more dealmaking activity as we go further into 2017," said Luke Bergstrom, global co-chair of Latham & Watkins LLP's M&A practice.

Here, Law360 outlines some of the major factors poised to fuel a tech M&A frenzy in the coming year.

Economic Outlook Spurs M&A Confidence

Despite a bit of a slowdown in M&A activity in the first quarter of the year, a generally positive outlook for the economy is laying the groundwork for a healthy year of dealmaking across multiple industries. Financing is available to do deals, and a strong stock market is helping to buoy valuations.

"What is driving technology transactions is first of all the same thing that drives general transactions. We have an economy where money continues to be available at extremely attractive rates based on competitive history; we have many sellers that are coming to market because valuations remain high," said Tracy Larsen, co-chair of Honigman Miller Schwartz & Cohn LLP's M&A practice.

The positive outlook is also supported by the election of President Donald Trump. Although Trump's election initially came as a shock and caused a bit of a pause as companies and dealmakers tried to evaluate what that would mean for M&A, there's a feeling that his role in the White House will open up conditions for even more deals, as well as even more transformative deals.

About 41 percent of the respondents to the M&A Leaders survey believe that Trump's economic policies stimulated dealmaking, while just 22 percent said they inhibited dealmaking. That positivity due to Trump is somewhat limited to U.S. activity, however, as headwinds are anticipated for foreign investors in the U.S. and even outbound deals.

"We've had two years of record M&A," said Robert Townsend, co-chair of Morrison & Foerster LLP's global mergers and acquisitions practice. "In our survey six months ago, people thought maybe we reached the peak of the M&A market and now in this survey, notwithstanding the Trump uncertainty, we've had the most optimistic response that we've had in a long time."

Tech's Anticipated Role In Economy Spurs M&A

Technology is also a hot commodity for other industries, making those with innovative offerings prime targets for companies looking to get ahead of the curve. This rings true for industries like automotive, which is working toward autonomous vehicles, and consumer goods, which is eyeing the so-called Internet of Things, or the connectivity of everyday items.

"Those are all areas where tech is seen as having a disruptive force in established industries and people are working very hard to figure out how to get to the next level," said Bergstrom.

Interest in those areas is expected to encourage not only domestic transactions, but also cross-border deals as companies hunt for the best technology, regardless of where it is located.

"We do expect to see a lot of inbound cross-border work continuing in areas where it traditionally hasn't been as big a focus in the value, but now when you're looking at Internet of Things or autonomous or connected vehicles, you are seeing a greater push from older, more established companies to pick up technology out here so they can get ahead of the game for the next generation of products in the industries," Bergstrom said.

But Trump's "America First" platform is also expected to weigh on cross-border deals. Of the respondents to the survey, 47 percent anticipate a decline in cross-border tech deals, while 26 percent expect an increase.

Cross-border activity between China and the U.S., going in both directions, is also expected to take a hit, given U.S. politics, concerns about gaining approval from the Committee on Foreign Investment in the United States and China's new capital regulations, which make it more difficult to move money out of the country.

"A lot of increases in Chinese investment in the U.S., there's a very real question as to how much we'll see this year and whether China will redivert investments to Europe and other more welcoming markets," Townsend said.

PE Firms Continue To Eye M&A Opportunities

Private equity firms are slated to invest more in tech opportunities, particularly as more tech companies are maturing and reaching a point in their life cycle where their venture capital backers are looking to move on but they still wish to remain private.

Of the respondents to the M&A Leaders survey, 54 percent believe there will be an increase in private equity activity in the tech industry in the coming year and 59 percent believe there will be an increase in long-term activity through 2020.

"There's a lot of tech-related businesses that are no longer development stage but are in fact operating businesses with revenue and earnings that can be used to amortize debt so they fit within the typical private equity model. That wasn't the case in the early 2000s. There weren't a lot of companies like that out here that were of interest to PE funds," Bergstrom said.

While recapitalization of venture-backed companies are expected to pick up, dealmakers also anticipate a large number of bolt-on transactions.

The expectation for an uptick builds off the steady rise in private equity activity in the tech industry in recent years. According to the survey, there were 659 private equity deals in the tech space in 2016, up from 582 in 2015 and 504 in 2014.

The interest in the sector is also highlighted in the handful of funds recently raised with plans to focus on technology opportunities. Just last month, Silver Lake Partners LP amassed $15 billion for the largest technology-focused private equity fund in history. The fund, called Silver Lake Partners NV, soared beyond its $12.5 billion target, with limited partners pledging $14.5 billion and roughly $500 million coming from the general partner itself.

"The enthusiasm and optimism behind tech investing is certainly at or near all-time highs. People have a tremendous appetite. Capital is chasing this particular sector, and it's certainly encouraging to have so much dry powder," said Atif Azher, a Simpson Thacher & Bartlett LLP corporate partner.

--Editing by Rebecca Flanagan and Emily Kokoll.
