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# 7 Ways The Pandemic Will Shape M&A In The 2nd Half Of 2020

By **Benjamin Horney**

*Law360 (July 17, 2020, 11:44 AM EDT)* -- The icy market for mergers and acquisitions has started to thaw, but lawyers will still need to adapt to a landscape fraught with the uncertainty spurred by the coronavirus pandemic.

No matter which source you use, the data shows the pandemic has contributed to an extreme slowdown in global M&A.

According to Dealogic, there were fewer than 7,000 deals announced in the second quarter of this year compared to almost 9,300 during the second quarter of 2019. Another deal data tracker, Mergermarket, also notes that between the first and second quarters of this year, both the volume and value of mergers and acquisitions globally plummeted by almost 50%.

"M&A activity has really dropped pretty dramatically," said Spencer Klein, co-chair of Morrison & Foerster LLP's global M&A group and head of its corporate department in New York.

COVID-19 isn't going to magically disappear, but dealmakers are desperate to get back to business. Here, Law360 explores seven issues M&A attorneys will have to grapple with in the second half of 2020.

**One Thing's for Certain: There's Tons of Uncertainty**

When the pandemic hit, companies of all kinds pressed pause on deal activity and looked within in order to make sure they wouldn't succumb to a perilous market. Many deals that were being negotiated got put on ice, and a number of transactions that had already been inked were terminated by parties wary of whether it still made sense to do any deals at all.

Even well-capitalized, large-cap companies with significant stockpiles of cash determined that the time was not right for mergers and acquisitions.

"They were making sure everything was in place so they could get their businesses through the pandemic," said Laurie Cerveny, a partner at Morgan Lewis & Bockius LLP and deputy-leader of the firm's M&A practice. "There was very little focus on M&A."

Though clients may be looking to increase their focus on M&A, even where there are buying opportunities, unless the target is in a sector that was not as negatively affected by the pandemic, many

dealmakers simply aren't ready to push forward with deals because there is still a risk that the virus will cause another shutdown.

"Yes, there are buying opportunities, but a lot of companies have decided that if you're not going to get rewarded by the market for using up a significant portion of your cash stockpile right now, you're better off sticking to your knitting, building up cash and keeping your eyes open for the best opportunities," Klein said.

Still, while there are immediate challenges causing clients to think twice about doing deals today, Klein has confidence the M&A markets will eventually rebound.

"Given the structural need for growth through acquisitions across so many industries, the strong equities markets and the availability of cash for many companies, I do expect we will see the M&A market rebound strongly as the overall economy continues to recover," he said.

**Deal Terms are Reflecting the Uncertain Environment**

Those clients that want to try to do deals during this uncertain time will come to find that terms are morphing to fit the moment. Agreements are being negotiated with less upfront cash and more deferred payments. Earnout provisions and clauses denoting that some portion of the price tag is contingent upon the achievement of future milestones are becoming increasingly popular.

According to Alison Johnson, a M&A partner at Holland & Hart who counsels businesses and venture capital firms, the use of variable pricing mechanisms like contingent consideration and performance based earnouts are one way in which clients are trying to price into deals the risk that comes with economic uncertainty.

"There are new challenges buyers and sellers are facing, but it's an interesting environment to do deals in," she said.

Additionally, attorneys should not be surprised to see clients considering the use of stock in M&A, assuming the markets don't suddenly take a nosedive, leading to an even more serious economic downturn.

"I think both [earnouts and use of stock] are intuitively sensible," Klein said.

Depending on which market you reference, the stock markets are at or near all-time highs, explained John Kaercher, a partner at Baker Botts LLP and a member of the firm's oil and gas, technology, media and telecommunications and financial restructuring M&A teams.

"So you end up with people thinking maybe the value of stock will continue to go up, and since there's a lot of risk in the market, they want to make acquisitions using stock," he said.

Still, attorneys are going to be tasked with figuring out how to make the specifics of any given agreement meet the wants and needs of their clients. Expect to hear that it's necessary to be creative in structuring deals.

"Words I've heard more in the last three months than in probably the entirety of my career are 'creative' and 'creativity,' or some derivation of that," Kaercher said.

**Debt Financing is Difficult to Obtain**

Speaking of the need to get creative, one result of the pandemic that is affecting dealmakers of all kinds is that debt financing has become more difficult to obtain. While deals come in all shapes and sizes, one thing they all have in common is that someone has to foot the bill.

Transactions can be financed in many ways, whether it's use of cash on hand, debt, equity or a combination of all three. Though the traditional banking giants are normally involved in M&A deals, in the aftermath of the coronavirus they have been less willing to provide debt financing, in part for fear that a given company will collapse and then be forced to default on their loans.

Private equity firms in particular have been forced to get creative when it comes to financing the deals they have been able to strike, according to Barbara Shander, a partner at Morgan Lewis & Bockius and co-leader of the firm's private equity practice. In one deal Shander worked on, for instance, the PE sponsors themselves put up the financing with the expectation that they'll be able to refinance once the credit markets open back up.

"The deals we have been seeing that are getting done are definitely more creative with respect to how they are being financed," she said.

**There Will Eventually Be a Rash of Distressed M&A**

An eventual uptick in distressed M&A is inevitable as struggling companies either find themselves insolvent or determine that shedding certain units or assets might help them remain profitable. Many attorneys anticipate that the increase in distressed M&A will begin in earnest in the coming months, with private equity firms and other asset managers among those likely to be deal-hungry.

"Buyers are looking for bargains," Cerveny said.

The idea that distressed M&A will pick up in the aftermath of a major economic shakeup should not come as a surprise, and the fact that it didn't happen immediately can be attributed to the fact that companies wanted to wait and see whether they could survive.

"Bankruptcies are just now hitting," Kaercher said. "The asset sales that will come out of that will maybe come a little later."

Those that come to see their best option is shedding non-core units will eventually look to deal, so attorneys should advise clients to prepare for there to be distressed assets available before the year is through.

"I think some level of distressed M&A is inevitable," Klein said. "There's just going to be distressed assets that are attractive and available that were not available prior to the crisis."

**Activists Won't Remain On the Sidelines Forever**

Proxy season usually begins in April and lasts through June, and in any given year there can be dozens of proxy fights between activist investors and the companies in which they're invested. During that time period this year, however, many activists refrained from pushing for companies to make major changes

or seek to sell.

"I think it was almost viewed as unsavory to try to distract companies from figuring out how to keep employees safe and keep their businesses afloat," Klein said.

He cautioned not to assume that activists took a step back because of a kind-hearted nature, however.

"I think they probably calculated that being too aggressive in the midst of this crisis would not have been viewed very positively," he said.

As the year goes on, and especially if the coronavirus crisis can be brought under control in the U.S. like it has in some other major countries, Klein said to expect an uptick in hostile takeover attempts.

"We haven't seen it yet, but I do expect there will be an increased number of hostile M&A deals," he said. "It just stands to reason that as we emerge from this crisis, there are going to be companies that have the ability to do things and companies that are weakened."

That hypothesis is based, in part, on what happened during and after the 2008 global financial crisis, which was the last major economic downturn. In a late March client alert titled "The Potential Impact of the Coronavirus (COVID-19) Pandemic on Hostile M&A and Shareholder Activism in the U.S.," MoFo noted that in 2008 and 2009, activist shareholders launched 126 and 133 proxy fights, respectively, against U.S. companies. Each of those numbers is more proxy fights than have happened in any year since.

"I'd be surprised if we didn't see that happen late 2020, early 2021," he said.

**Remote Work Isn't Going Away**

Even if more businesses begin to open as the second half goes on, the consensus seems to be that law firms are in no rush to force their attorneys back to the office. People were forced to adapt abruptly when the coronavirus hit; in-person meetings with clients and colleagues were replaced by video conferences, and instead of commuting lawyers realized they could log on minutes after waking up.

"In some ways, adapting to remote working and finding creative alternatives to traditional ways of interacting could promote more deals," said Hogan Lovells M&A partner Elizabeth Donley. "The practice of M&A has been gradually shifting over the last 10 years to more and more remote dealing. Today, you often do a deal start to finish and never see people face-to-face."

If most people remain remote, there will be no need to coordinate the logistics of in-person meetings. Instead, the focus can be on the actual deal work.

"The pandemic has accelerated a trend that was already in play," Donley said.

That said, Donley stressed that dealmaking is about building relationships and trust, and seeing eye-to-eye on important issues.

"There will always be those deals where there really is no substitute for face-to-face, in person interaction," she said. "So while I expect remote working during the pandemic will have a lasting impact

on the way we do deals, personally I think the convenience of remote dealmaking can only take us so far."

**Few Are Thinking About the US Presidential Election**

Even under normal circumstances, this year would have contained discussion about uncertainty in the market heading into the second half of the year because there's a U.S. presidential election coming up. This year, much of that discussion has hit the backburner for dealmakers as they focus on the immediate needs of their business.

"On the list of things people are anxious about, right now the impact of the election is a couple of pegs down," Cerveny said.

According to Brian Richards, a partner in the Paul Hastings LLP private equity and M&A practices and chair of the firm's global PE practice, the coronavirus-caused chaos has led to one potential outcome falling under the radar for many dealmaking folks: If Donald Trump loses to Joe Biden and the Democrats also take the House of Representatives and Senate, there may be nothing standing in the way of serious change.

"The Senate Democrats have talked about doing away with the filibuster, in which case they would only need 50 votes to enact their agenda," Richards said.

That agenda is unlikely to be kind to private equity buyers, Richards explained, as corporate income tax rates and capital gains rates for individual investors could go up. Such a scenario could lead to a rash of attempted activity at the end of the year as people look to exit businesses before the new regime takes hold. Especially if the likes of Sens. Elizabeth Warren, D-Mass., or Bernie Sanders, I-Vt., are appointed to positions of power within the Biden administration.

"That's going to be a major driver of activity," Richards said. "It's going to be chaos at the end of the year."

--Editing by Kelly Duncan.

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