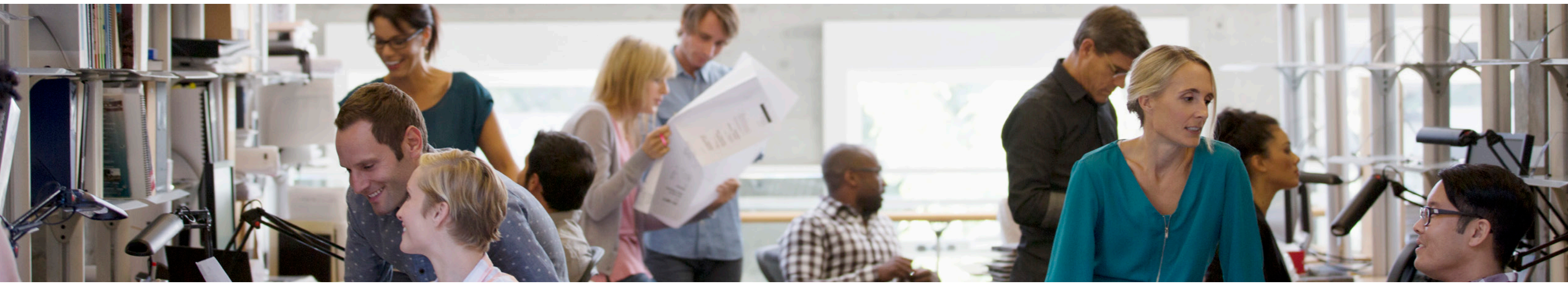
MID-MARKET INVESTMENT BANKING

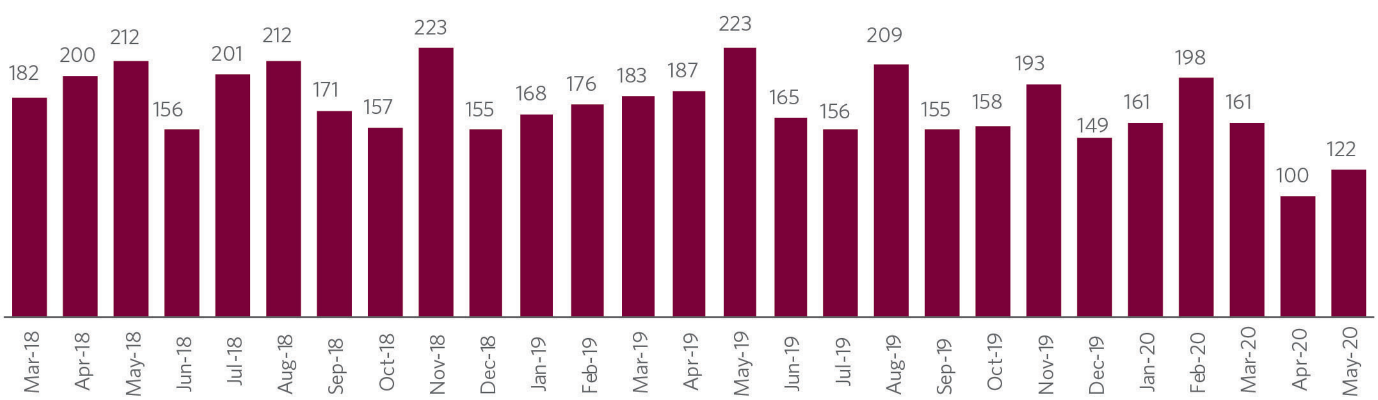
June 2020



We have experienced quite a dramatic change in tone over the last few weeks with respect to the COVID-19 pandemic. Following months of a constant stream of dire predictions, focus rapidly shifted towards positive developments, such as early indications of efficacy from clinical trials evaluating potential vaccines and treatments, lockdown measures being lifted around the world and renewed optimism for a swift economic recovery. Visibility remains dim however, with many economic indicators signaling that we are still in the thick of the storm. The M&A environment, which thrives on good visibility and solid growth prospects, remained soft in May, as expected. The volume of transactions in Canada and the US was slightly higher than April's low, but remains at approximately half the level of activity seen in May 2019.

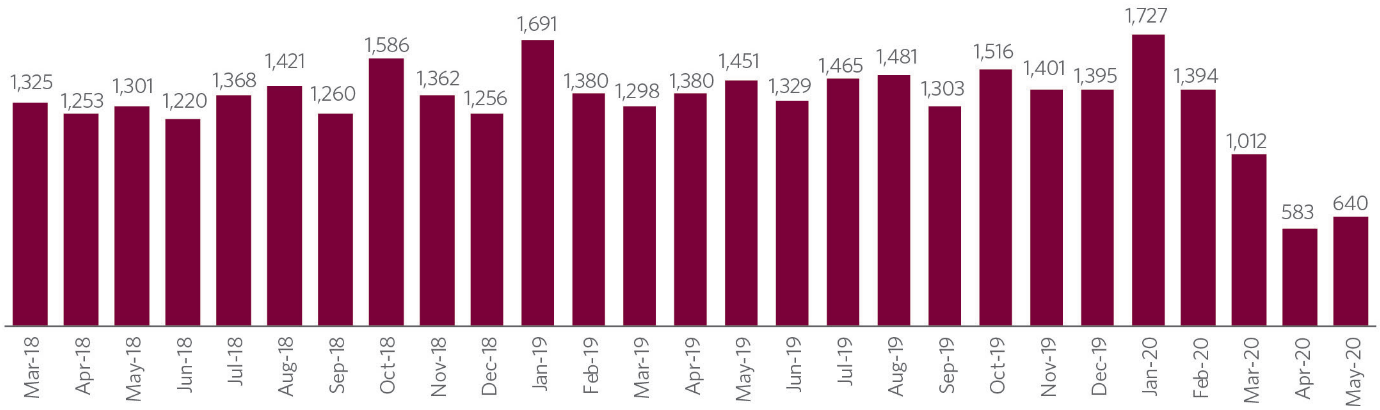
Canadian and US M&A activity update

Monthly M&A transactions in Canada



Source: Capital IQ.

Monthly M&A transactions in US



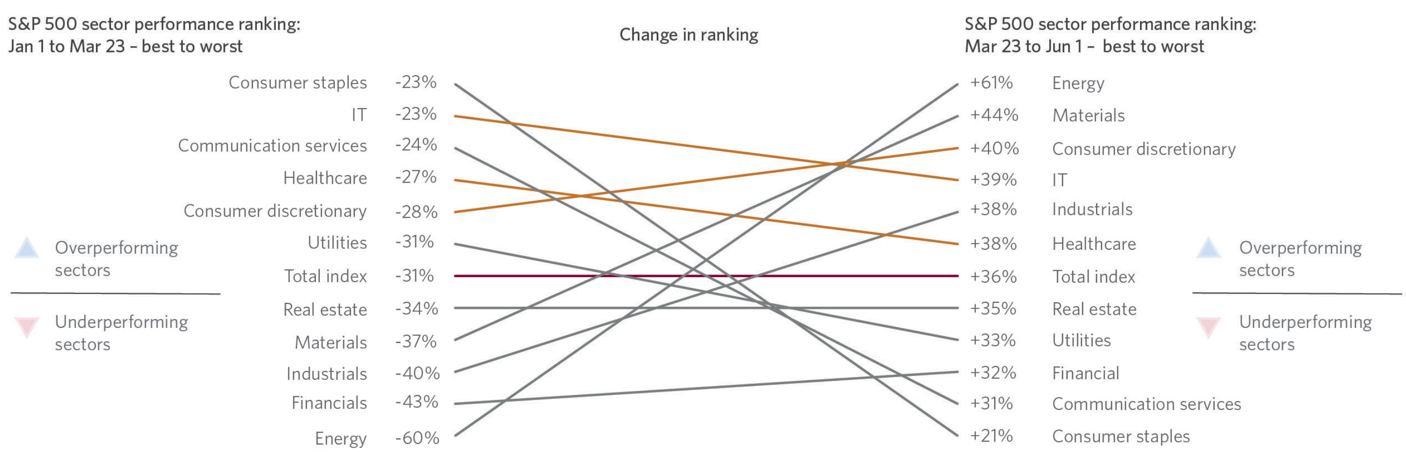
Source: Capital IQ.

Given the length of a typical M&A process, we will likely not see the impact of the recent optimism until a few months, if it persists. In the meantime, we can turn to the public markets to gather evidence on shifts in investor optimism which can guide us to anticipate future M&A trends.

It's happy hour on Zoom in the equity markets

Investors avidly embraced the silver lining offered by the first positive developments since the beginning of the outbreak, driving US and Canadian equities up approximately 36% since the low reached on March 23rd 2020, erasing nearly three quarters of market losses year to date. More interestingly, when dissecting sector performance, we can clearly observe some of the paradigm shifts in investor interest that we were anticipating in our last market pdate.

Below is a visual representation of the relative performance of the 11 sectors in the S&P 500 for the year-to-date period leading to the low reached on March 23 (the "Downtrend") and for the period of the recovery until June 1st (the "Uptrend").



Source: Capital IQ.

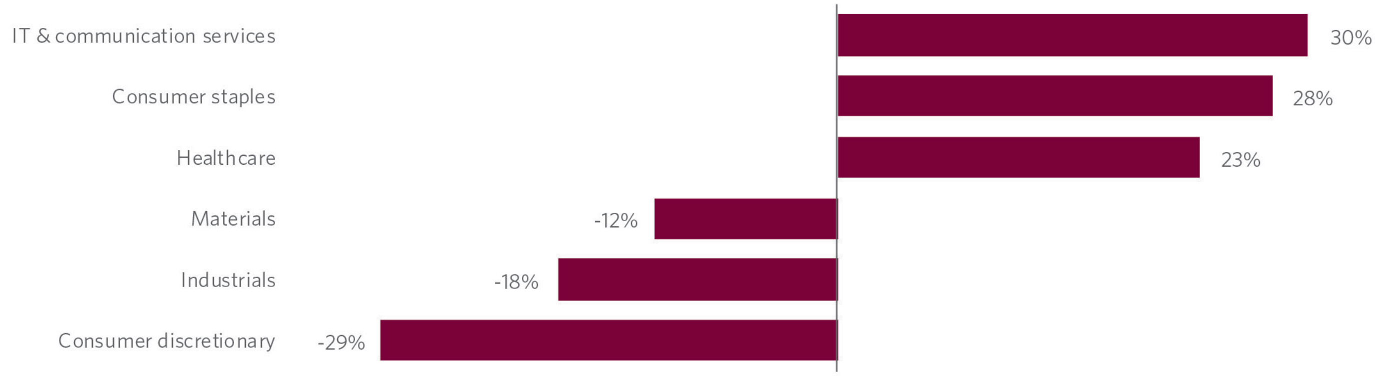
As expected, most of the worst performers during the Downtrend, such as Energy stocks, were the best performers during the Uptrend, and vice-versa – consumer staples, a defensive sector heading into a crisis, underperformed the index the most during the Uptrend. Sectors highlighted with blue lines show those that have outperformed the index both during the Downtrend and the Uptrend. IT and Healthcare firms, as noted in our last market update, are actually experiencing tailwinds due to the crisis. The consumer discretionary category, on the other hand, would have been expected to underperform during the Downtrend. When analyzing further, we notice that this category is being distorted by Amazon, which represents nearly 40% of the sector weight. Amazon overperformed the S&P 500 by 33% during the Downtrend, in stark contrast to the other sector constituents. Excluding Amazon, the sector would have been the index' second-worst performer after Energy.

Public equities market data confirms that investor interest is shifting towards sectors with a bright outlook in the context of a post-pandemic world, where healthcare is a primary concern and the digitization trend is accelerating. Zoom is the embodiment of this shift – as millions of social-distancing families were holding Zoom birthday parties, investors were fighting over their shares, driving up their value by over 200% year-to-date.

M&A acquirers are stock-pickers too

We expect strategic and financial acquirers will identify the same trends and focus their attention on those sectors until appropriate visibility returns in other industries. Analysis of April and May transaction data supports this hypothesis.

Change in sector % of total M&A volume April & May 2020 vs year to March 2020



Source: Capital IQ.

M&A transactions involving IT & communications, consumer staples and healthcare firms represented a greater % of total volume during the last two months compared to more cyclical sectors such as materials, industrials or consumer discretionary. This trend is also observed in our own deal flow – most transactions involving targets operating in cyclical sectors were put on hold until there is more clarity on the timing and magnitude of a broad economic recovery.

An ounce of preparation is worth a pound of due diligence

The repurposed quote from Benjamin Franklin carries a weight of significance in the present context. With strategic and financial acquirers holding record amounts of capital eager to be deployed, the M&A market could recover very quickly. The best prepared sellers will be better positioned to capture their share of this capital. In most cases, disruptions experienced by businesses over the last few months will not be recurring and should be normalized when assessing historical profitability. Preparing ahead of a sale process by building a solid case for normalizations and post-crisis run-rate performance will save substantial time and resources during due diligence and will inspire confidence with potential buyers, ensuring a smoother transaction and achieving maximum value.

We would be pleased to discuss your particular context and strategize on the best timing and preparation for a potential transaction.

About us

CIBC Mid-Market Investment Banking is a leading M&A advisor, providing services to private companies:

- Divestitures
- Acquisitions and management buyouts
- Raising equity capital and securing debt financing

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