Deals in India: Mid-year review and outlook for 2020 – pause and consolidation

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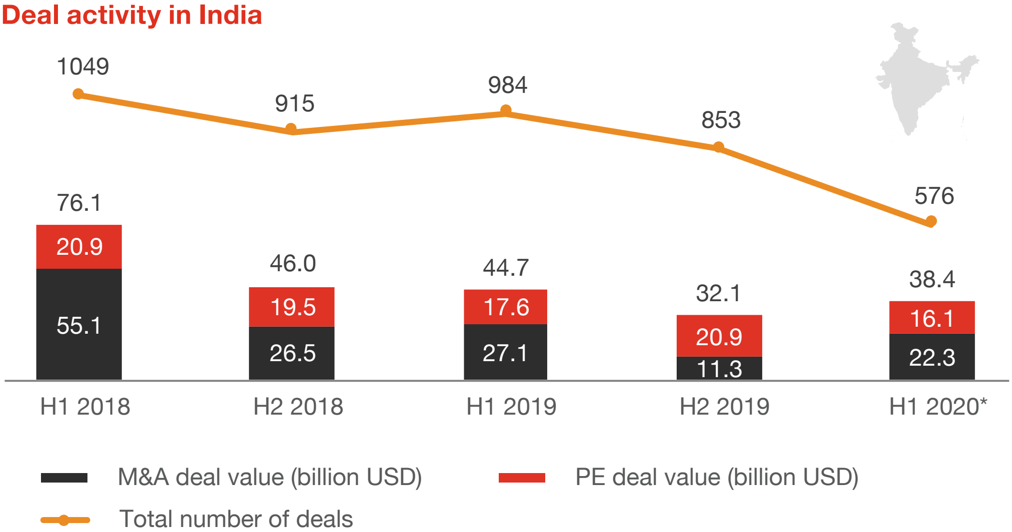
Deals in India: Mid-year review and outlook for 2020 – pause and consolidation

Deal activity in India was witnessing a slowdown towards the end of 2019 on account of a number of factors ranging from global challenges to concerns around India's macroeconomic indicators. This scenario has been further aggravated by the COVID-19 crisis that has impacted all sectors and halted the operations of several industries. Despite the crisis, investment activity in India witnessed a 19% increase in value compared to the second half of 2019, but a 14% decline compared to the same period last year. Deal value across both private equity (PE) and strategic (mergers and acquisitions [M&A]) deals amounted to USD 38.4 billion across 576 deals, with M&A accounting for a larger share.

Deal activity in India

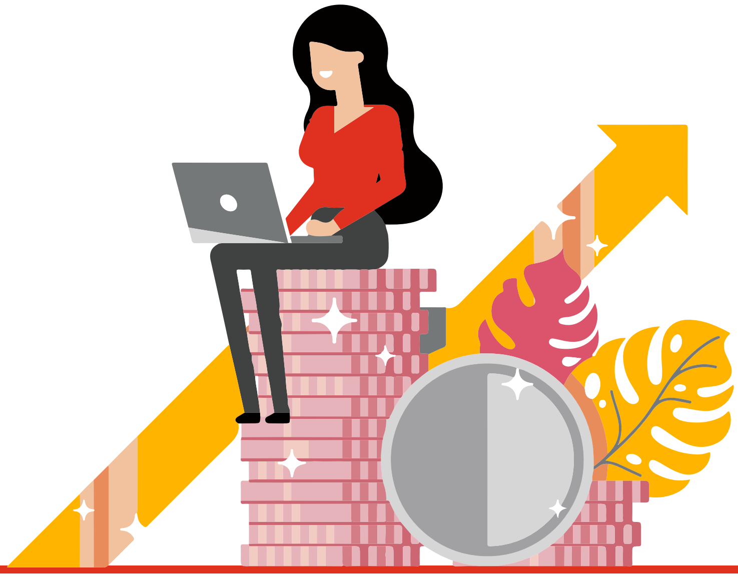


Source: Venture Intelligence (PE), VCCEdge (M&A) and PwC analysis

While PE deals witnessed a decline in comparison to 2019, M&A deals doubled in value as compared to the H2 2019. Deal volume continued on a downward trajectory, drawing attention to the increase in average ticket size.

Uncertainty appears to be the underlying theme for 2020, with several PE houses and strategic players shelving their investment plans. However, a number of investors continue to view India as a key investment destination, echoing confidence in India's potential. Deal activity in 2020 is expected to remain uncertain and largely dependent on how quickly the economy would recover. While the COVID-19 crisis continues to grow in India, deal activity could pick up towards the end of the year if business operations regain some normalcy, provided the spread of the disease is adequately contained.

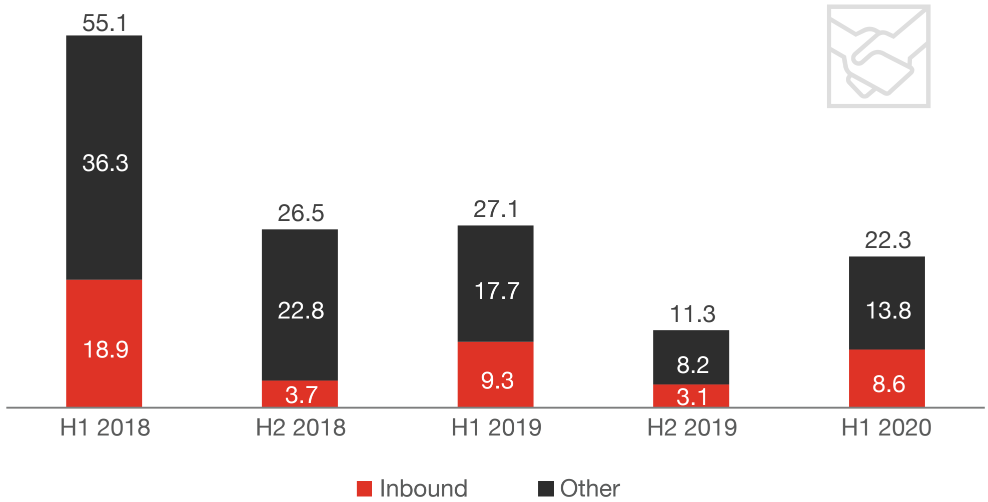
*H1 2020 refers to the period from 1 January 2020 to 15 June 2020



Continued interest from foreign investors

Facebook's investment worth USD 5.7 billion in Jio Platforms was the largest deal in the first half of 2020.[1] Facebook has highlighted India's maturing e-commerce space and attracted the interest of several global investors who then jumped on the bandwagon.

M&A activity by deal type (USD billion)



Source: VCCEdge and PwC analysis

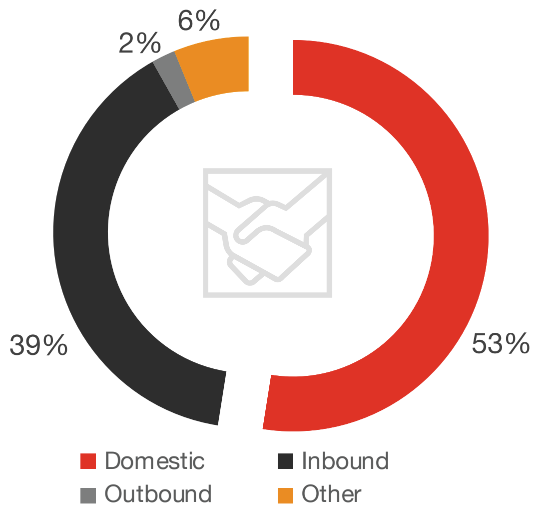
Inbound activity amounted to nearly USD 9 billion in the first half of 2020, a marginal decline in comparison to the first half of 2019. In addition to Facebook, Groupe ADP also contributed to inbound activity this year as it finalised its USD 1.5 billion investment in GMR Airports.

With supply chains being disrupted worldwide, companies could look at India as the next global supply chain hub amongst Asian countries. This could boost inbound activity in India and also provide much-needed support to the manufacturing space, including micro, small and medium enterprises (MSMEs).

1 Data gathered from Venture Intelligence

Consolidation continues to drive M&A

M&A activity by deal type (USD billion) in H1 2020



Source: VCCEdge and PwC analysis

Domestic deals have accounted for a majority of the M&A deal value in the last 30 months. The first half of 2020 has seen domestic deals worth nearly USD 12 billion – more than half of the total M&A value over the last six months.

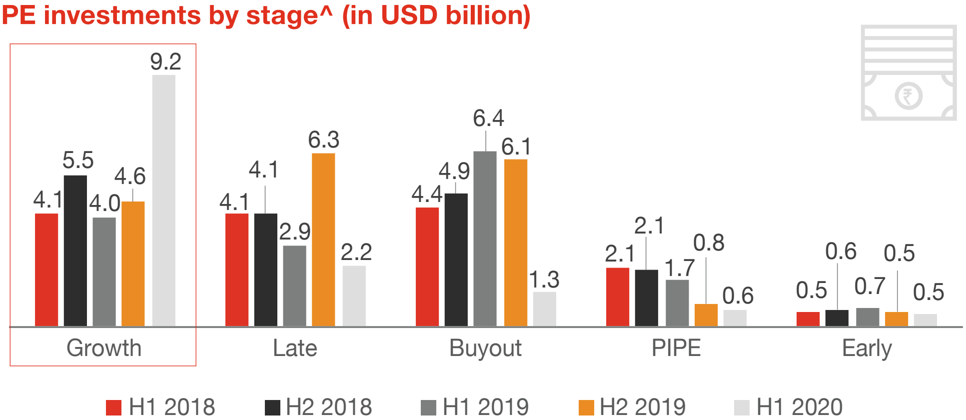
A significant portion of this consolidation is driven by stressed situations, a trend that is likely to continue for the rest of year. With a number of businesses facing challenges related to cash flows and investors looking for assets at attractive valuations, consolidation is likely to continue driving deal activity this year.

A majority of the consolidation this year took place within the banking space. The infusion of USD 1.4 billion into Yes Bank by the consortium of banks led by the State Bank of India (SBI) was one of largest deals this year.[2] Similarly, Adani Ports agreeing to invest USD 1.4 billion in Krishnapatnam port was another key stressed acquisition in H1 2020.[3]

Growth capital versus buyouts

2019 was a standout year for buyout deals which recorded investments worth over USD 12 billion across the year. Buyouts have been on an upward trend over the last few years due to rising governance concerns and investors are expected to continue to look for control transactions.

PE investments by stage^ (in USD billion)



^Excludes Real Estate, pre-IPO and others

Source: Venture Intelligence and PwC analysis

2 https://www.livemint.com/industry/banking/sbi-board-approves-purchase-of-725-crore-shares-of-yes-bank-11584011870976.html

3 https://economictimes.indiatimes.com/markets/bonds/adani-ports-plans-to-raise-1-billion-in-long-term-debt-overseas/articleshow/76740921.cms

However, the last six months have witnessed a significant increase in growth transactions, mainly due to the investments made in Jio Platforms. Investments in Jio Platforms accounted for 78% of the growth stage investing in terms of value and were also among the top PE investments in H1 2020.

While buyouts declined by 80% in terms of value as compared to the same period last year, control would be a key element for most investors, given the current challenging circumstances. PE players have begun to focus on value creation and enhancement, and are increasingly moving towards a buy-and-build approach. Divestments of stressed segments, control on exit timing and the need to maximise returns could make buyouts a preferred investment mode in the future.

Shifting focus for venture capitalists (VCs)

The COVID-19 crisis posed a number of challenges for VC-backed start-ups, particularly in the e-commerce space. These companies have been coping with changing revenue projections, layoffs, decline in discretionary spending and restrictions imposed by the Central Government and state governments. Simultaneously, several funds have been focused on the performance of their existing portfolios, with the hope of an exit. However, given the lack of visibility for the rest of the year, the possibility of exits, including secondary sales, would be subject to pricing and quality of these assets.

The concept of social distancing has brought about significant changes for a number of industries, including retail, as consumers are increasingly opting for online channels. The education sector has been significantly affected by the COVID-19 crisis as well and the use of EdTech for continuation of education is gaining importance. Early stage investments in the education space amounted to USD 80 million in the first six months of 2020, compared to USD 65 million invested throughout 2019.[4]

The border dispute between India and China and subsequent trade tensions, coupled with changes in the foreign direct investment (FDI) regulations,[5] could present another challenge for the start-up space in India particularly for tech companies. Big-ticket Chinese investors have been a part of some of the largest investments in India's start-up space and the current Indo-China tensions could impact future investments.

4 Data gathered from Venture Intelligence

5 https://economictimes.indiatimes.com/news/economy/policy/new-fdi-policy-can-india-manage-to-stem-chinese-predatory-trade-practices/articleshow/75361718.cms?from=mdr

Sovereign wealth funds (SWFs) are taking a breather

A number of SWFs and pension funds have deferred their investment plans or are renegotiating the terms of proposed deals. Canadian pension funds, which were at the forefront of deal activity in India over the last few years, are currently in a wait-and-watch mode. On the other hand, SWFs from the Middle East have invested sizeably in India over the last few months.

Investments from SWFs and pension funds have been increasing over the last few years, particularly in core sectors such as infrastructure, renewable energy and real assets. These funds continue to express interest in these segments and consider India's investment landscape as promising. Despite the temporary hiatus in investments from SWF and pension funds, we could expect investments from these funds to regain momentum. The Central Government's move to grant 100% tax exemption[6] to SWFs on investments in infrastructure could also boost investor sentiment and drive investments in this space.

Top five M&A transactions (by deal value) in H1 2020

Company	Buyer(s)	Deal value (in USD billion)	% sought
Jio Platforms Ltd.	Facebook Inc.	5.73	9.99
GMR Airports Ltd.	Groupe ADP	1.51	49
Krishnapatnam Port Co. Ltd.	Adani Ports and Special Economic Zone Ltd.	1.43	75
Yes Bank Ltd.	State Bank of India, Axis Bank Ltd., Bandhan Bank Ltd., Housing Development Finance Corporation Ltd., ICICI Bank Ltd., IDFC First Bank Ltd., Kotak Mahindra Bank Ltd., The Federal Bank Ltd.	1.35	-
Corporation Bank Ltd.	Union Bank of India Ltd.	0.99	100

Source: VCCEdge

Top five PE transactions (by deal value) in H1 2020

Company	Investors	Deal value (in USD billion)	% sought
Reliance Jio	Vista Equity Partners	1.50	2.32
Reliance Jio	KKR	1.50	2.32
Reliance Jio	Mubadala Investment	1.20	1.85
RMZ Corporation	Mitsui	1.00	-
Reliance Jio	General Atlantic	0.87	1.34

Source: Venture Intelligence

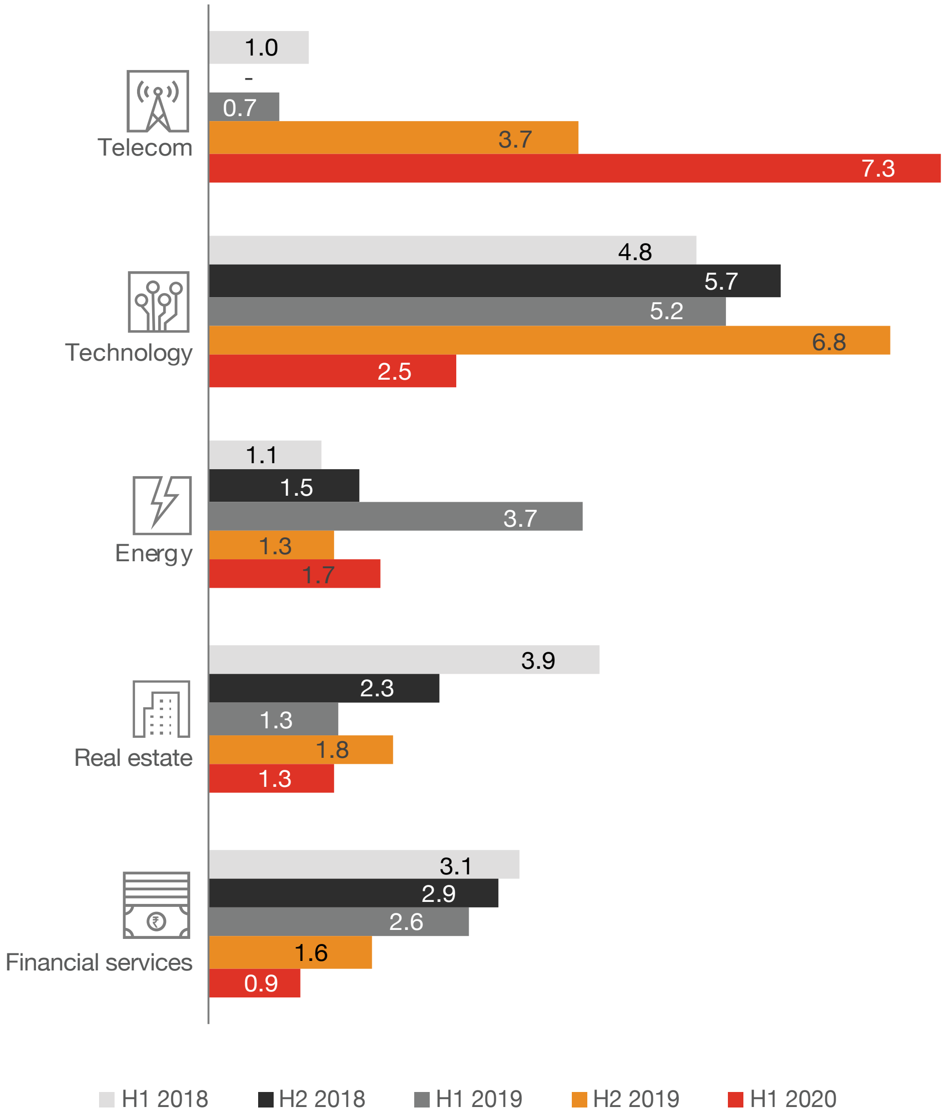
6 https://economictimes.indiatimes.com/news/economy/infrastructure/budget-2020-tax-exemption-for-sovereign-funds-to-boost-india-infra-play/articleshow/73839614.cms?from=mdr

Telecom in the lead

PE investments in telecom amounted to USD 7.3 billion by June 2020, surpassing investments made in this sector across all previous years. This was on account of investments made by traditional PE houses and SWFs in Reliance Jio.

Investments in technology recorded a decline in terms of value but retained its position among the top five sectors attracting PE investment in H1 2020. A majority of the investments in this sector were concentrated in the online services space.

Top five sectors attracting PE investments (in USD billion)



Source: Venture Intelligence

The energy segment secured the third position with investments worth USD 1.7 billion across eight deals, of which seven were in the renewables segment.

As tensions related to international trade between countries become widespread, a heightened sense of nationalism in a number of countries is compelling them to reduce their dependency on oil imports and giving an impetus to green-energy and sustainable solutions.

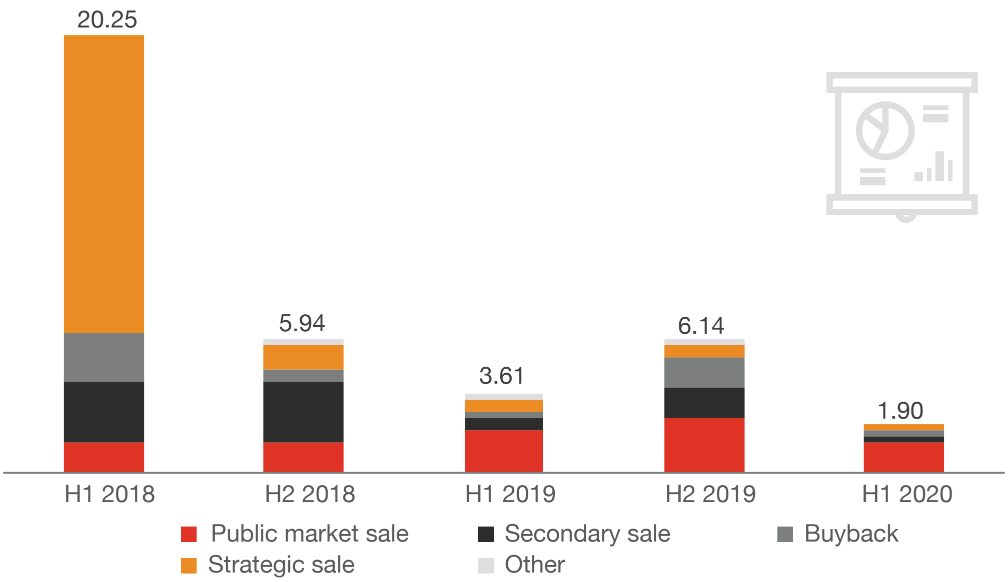
There have been investments worth USD 1.3 billion in real estate in H1 2020, with 98% of the investment value being recorded in the first quarter of the year. This segment is currently facing a number of challenges, ranging from labour shortages to liquidity issues, and could struggle to recover in the near term. Financial services recorded investments worth USD 900 million in H1 2020, with non-banking financial companies (NBFCs) and microfinance institutions (MFIs) attracting over 60% of the investment value. The COVID-19 crisis has significantly impacted the financial ecosystem in India and the fallout could result in an increase in non-performing assets (NPAs).

Both real estate and financial services could present opportunities for stressed investors and asset reconstruction companies (ARCs).

Exits remain lacklustre

Amidst market volatility, PE exits in H1 2020 witnessed a 47% decline as compared to the same period last year and a 69% decline as compared to H2 2019. Public market sales accounted for 80% of the exit value in H1 2020, mainly due to the SBI Cards IPO.[7]

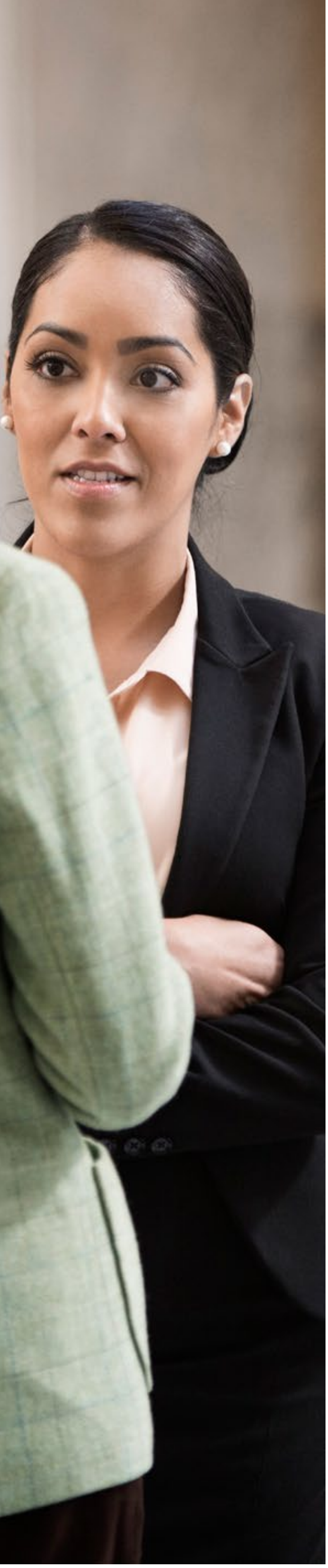
PE exit activity (USD billion)



Source: Venture Intelligence and PwC analysis

Considering the sharp decline in equity markets, a number of companies have postponed their initial public offering (IPO) plans, consequently placing a number of PE exits on hold. Exit activity levels could remain muted this year till there is some form of recovery in asset prices. The need for liquidity could drive some amount of secondary sales and consolidation could also spur strategic sales. However, we could expect some conflict between buyers and sellers on the valuations front.

7 https://m.economictimes.com/markets/ipos/fpos/indias-sbi-cards-is-on-track-to-pull-off-1-4-billion-ipo/articleshow/74493412.cms



Future of deals in the wake of the current crisis

Strategic and PE investors have entered uncharted waters and are trying to cope with a highly dynamic situation. Survival, sustainability and organisational growth are amongst the top priorities for chief executive officers (CEOs) and chief financial officers (CFOs). Strong balance sheets, steady cash flows, lower debt levels and dependable management teams are key areas chief experience officers (CXOs) and investors would look for during acquisitions.

Simultaneously, it important to adopt a cautious and vigilant approach in the wake of the current crisis. The overall construct of deals is going through a massive change as physical meetings are being replaced by virtual interactions. and due diligence will be a vital factor in closing potential deals.

In the current VUCA (volatile, uncertain, complex and ambiguous) world, CFOs would need to adopt an open mindset, adapt quickly to changing scenarios, focus on crisis management and develop a contingency plan.

While investment activity currently appears to be in a slump, deal levels would eventually pick up with investors tapping into opportunities emerging from the COVID-19 crisis. Protectionism and nationalism could impact cross-border deals; however, as an emerging economy, India remains a lucrative destination for foreign investors.

The impact of COVID-19 on the global economy has been far reaching and caused a realignment of priorities, drawing renewed attention to sectors like education, healthcare and pharmaceuticals, including medical research. Investor interest in these sectors could increase in the future. Economic recovery from the COVID-19 crisis would largely depend on the Government's response to the situation and the execution of the reforms it has announced to tackle the crisis.

Note: All deal values and related data presented in this report, unless otherwise indicated, are based on PwC analysis of data sourced from VCCEdge (for M&A deals) and Venture Intelligence (for PE deals).

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