Supercharge your deals with intelligent ecosystems

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The modern dealmaking landscape

Successfully closing a deal in today's competitive market requires more than just the highest bid. Record levels of capital, along with fewer acquisition targets, are inflating asset valuations and putting pressure on future returns.

In a 2019 study, Deloitte found that corporate executives and private equity investors predict a significant uptick (51% versus 38% the prior year) in the total annual dollar value of deals between $500 million and $10 billion. Despite the deal-size optimism, about 40% of respondents said that half of their deals failed to generate their expected value or return on investment.[1]

To make matters worse, dealmakers face significant challenges related to increasingly complex relationships and opaque deal pipelines. Sourcing and closing a deal does not occur in a vacuum. In fact, it requires knowledge from a wide range of experts, including institutional investors, fund managers, lawyers, accountants, consultants, and investment bankers. The powerful combination of these dealmakers coming together, each with their unique perspective and expertise, enables the identification of high-value investment opportunities.

Although many dealmakers already rely on their networks to source deals, traditional strategies are no longer sufficient in these new market dynamics. By applying a modern approach to the dealmaking process, firms can establish a more effective strategy to close deals and gain an edge in today's competitive deal environment.

WHAT IS MODERNIZATION?

Modernization refers to any strategy, initiative, or investment that is designed to help firms prosper by enabling them to keep pace with rapidly changing demands, market conditions, and new technologies. These typically involve unifying people, process, and data.

[1] Deloitte. "The State of the Deal: M&A Trends 2019."

Sticker shock

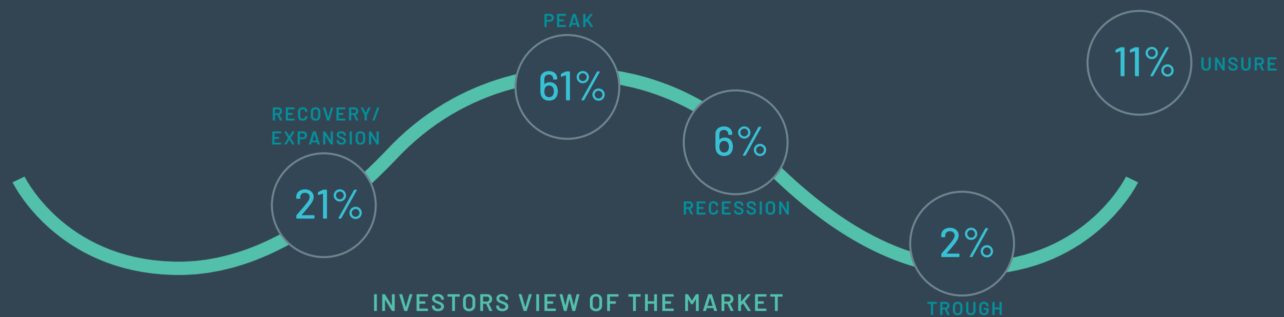
Despite record levels of dry powder and competition to close deals, investors continue to increase their allocations to the private capital markets. This trend can be seen in the number of U.S. private equity-backed companies growing 106% from approximately 4,000 in 2006 to 8,000 in 2017, while the number of publicly traded companies fell from 5,100 to 4,300 over the same period.[2] In fact, only 21% of investors believe that the market is expanding, while 61% hold the view that the market has peaked.[3]

Global private capital assets under management (AUM) has hit a record high, with $5.8 trillion as of June 2018. Similarly, the market has increased more than three-fold over the past decade to $9.5 trillion across all alternative asset managers globally and is projected to reach $14 trillion by 2023.[4] Coupled with more than $2 trillion of private capital dry powder in the market, the need to close deals is higher than ever — and there is no indication of deal activity slowing any time soon.

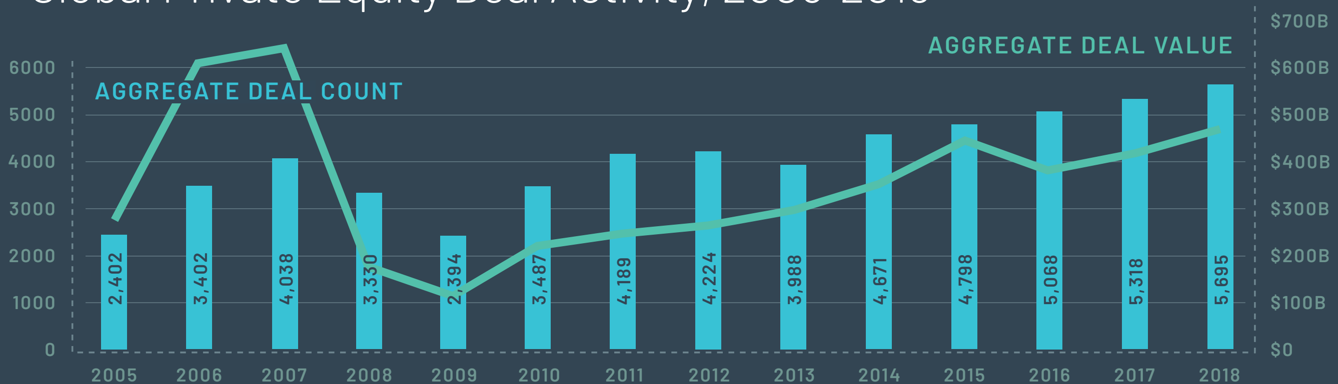
Global private capital assets under management (AUM) has hit a record high and the market has increased more than three-fold over the past decade.[4]

[2] McKinsey & Company. "Private markets come of age: McKinsey Global Private Markets Review 2019."
[3] Preqin. "2019 Preqin Global Alternative Assets Reports."
[4] Preqin. "2019 Preqin Global Alternative Assets Reports."

Where Are We in the Current Equity Market Cycle?



Global Private Equity Deal Activity, 2005-2018



This pressure to invest has resulted in more expensive deals as greater amounts of capital and fewer acquisition targets push asset valuations higher with deal multiples increasing to 11.1X in 2018 from 10.4X the previous year.[5] The costs associated with closing a deal are coming under greater scrutiny as the uptick in multiples affects dealmakers' ability to generate strong returns.

In today's competitive environment, private equity firms evaluate an average of 80 opportunities before identifying a single investment, according to research by Tenten Advisors. Furthermore, successfully closing a deal requires, on average, 20 management team meetings, four rounds of negotiations, three due diligence reviews, and more than three full-time investment team members.

In addition to the significant time and resources required to close a deal, business development professionals are increasingly stuck with the burden of allocating resources to industry events and conferences, networking opportunities, data subscriptions, proprietary search partners, and buy-side firms. These traditional methods are no longer adequate due to the changing market dynamics surrounding dealmaking.

A Private Equity Firm's Investment Dealmaking Process[6]

[5] McKinsey & Company. (2019). "Private markets come of age: McKinsey. Global Private Markets Review."
[6] Tenten, David. (2011, March 29). "Five Best Practices in Sourcing Investments." Business Insider.

FOR MANY B2B INDUSTRIES

1%-2%

OF DEALS CAN ACCOUNT FOR MORE THAN

40%

OF THE FIRM'S REVENUES[7]

WHAT IS A PROPRIETARY DEAL?

A proprietary deal is when a single acquirer approaches the target company, or the acquirer is the first of multiple bidders. Both of these scenarios provide the acquirer with significant competitive advantage.

HOW DOES AN ACQUIRER SOURCE PROPRIETARY DEALS?

Typically, it leverages its social capital to gain an edge, whether that be through using exclusive introductions, being first to get target company prospectus, obtaining knowledge of trigger events (the macro forces that will have impact on the company), and more.

The holy grail: Proprietary deals

In this incredibly competitive market, proprietary deals are an important way for firms to differentiate themselves. Buyers, lenders, and their service providers (e.g., lawyers, accountants, etc.) not only need to market their ability to land proprietary deals, but they also need to speak early and often about their strong track record of successfully executing these deals.

Although asset valuations represent the largest challenge to generating returns, sourcing the right deal has major implications for dealmakers. For many B2B industries, just 1% to 2% of deals can account for more than 40% of the firm's revenues.[7] This is why many dealmakers rely on proprietary deals and will continue to do so. However, true proprietary deals are few and far between in today's market and are highly dependent on relationships and insight.

Dealmakers are looking to a variety of sources for their investment opportunities. In a study of 162 private equity firms, more than 90% of survey respondents point out that meaningful introductions come from existing portfolio companies. Furthermore, 90% of private equity firms said that referrals from investment bankers, as well as conferences and other marketing activities, are important deal flow generators. Meanwhile, service providers, such as accountants (79.6%), attorneys (75.3%), and financial advisors (73.5%), are good sources for companies to invest in. For approximately three out of five private equity firms, business development relationships are geared toward finding middle-market company investments.[8]

What can help in this quest for the ever-elusive proprietary deal?

The most successful private equity firms have a systematic process in place to find deals that are aligned with their strategic priorities, fit their investment thesis, and have the most potential to generate high returns. Traditionally, this has been a time-consuming, expensive process that impacts the ROI of the deal itself. According to a study by Merrill Corporation, "Globally, 36% of dealmakers believe private equity's focus on speed and efficiency is driving the most change in due diligence. And no matter where you sit in the deal ecosystem, the way to achieve efficiency gains and secure ROI is through in-depth industry expertise."[9]

The most successful buy-side service providers offer tailored strategic guidance on targets while the most successful sell-side service providers advise target companies to consider select acquirers based on in-depth investor analysis. Collecting this data and turning it into actionable insights is time- and resource-intensive.

Access to data-driven insights for both financial sponsors and service providers not only increases the odds of landing a proprietary deal, but also positions these firms to do so in a much more efficient and less costly manner.

[7] McKinsey & Company. "Megadeals: How Data and Analytics Can Dramatically Boost Success."
[8] Forbes. "How Private Equity Firms Are Looking to Source High-Quality Investment Opportunities."
[9] Merrill Corporation. "The Future of Due Diligence."

You are the company you keep

Leveraging relationship intelligence to create a deal ecosystem requires dealmakers to view their network as strategic partners with complementary skills. By doing so, dealmakers can gain market access, share information, and reduce risk. According to research by McKinsey, "Partners come together to take advantage of complementary geographies, corresponding sales and marketing strengths, or compatibilities in other functional areas. This process must start before the deal is completed — but cannot stop at signing."[10]

In capital markets, building a deal-specific ecosystem liberates dealmakers and enables them to focus on their core capabilities and industry specializations, as well as creating greater value than they would individually. Through this multidisciplinary team of experts, firms can fill the knowledge gaps in a more effective manner than going it alone and replicating these capabilities in-house. The deal ecosystem builds a foundation that is equipped with mutually beneficial combined-margin systems, profit pooling, revenue sharing, and venture stakes. This arrangement aligns the goal of continuous value-creation across the entire deal ecosystem and provides an incentive for each member to adapt quickly when new technologies, market opportunities, or competition arise.

Accenture's Disruptability Index finds that more than 40% of companies across 20 industries — accounting for a combined enterprise value of $26 trillion — are highly susceptible to future disruption. In response, 63% of executives believe that participating in ecosystems allows businesses to innovate, 58% believe that participation can increase revenue growth, 55% believe that it provides access to new markets, and 55% believe participation can lead to accessing new markets.[12]

For a deal ecosystem to be fruitful, each partner in this intricate relationship web has their part to play and value to be gained by utilizing its collective expertise to the fullest extent.

WHAT IS AN ECOSYSTEM?[11]

An ecosystem is comprised of a cross-industry network that collaborates to define, build, and execute solutions by delivering a piece of the solution or contributing a necessary capability. No single member needs to own or operate all components — and the value the ecosystem generates is larger than the combined value each member could achieve individually.

SIZE

90% of ecosystems involve participants from more than five countries, and 77% of ecosystems involve both developed and emerging market players.

EXPERTISE

83% of digital ecosystems involve partners from more than three industries and 53% from more than six industries.

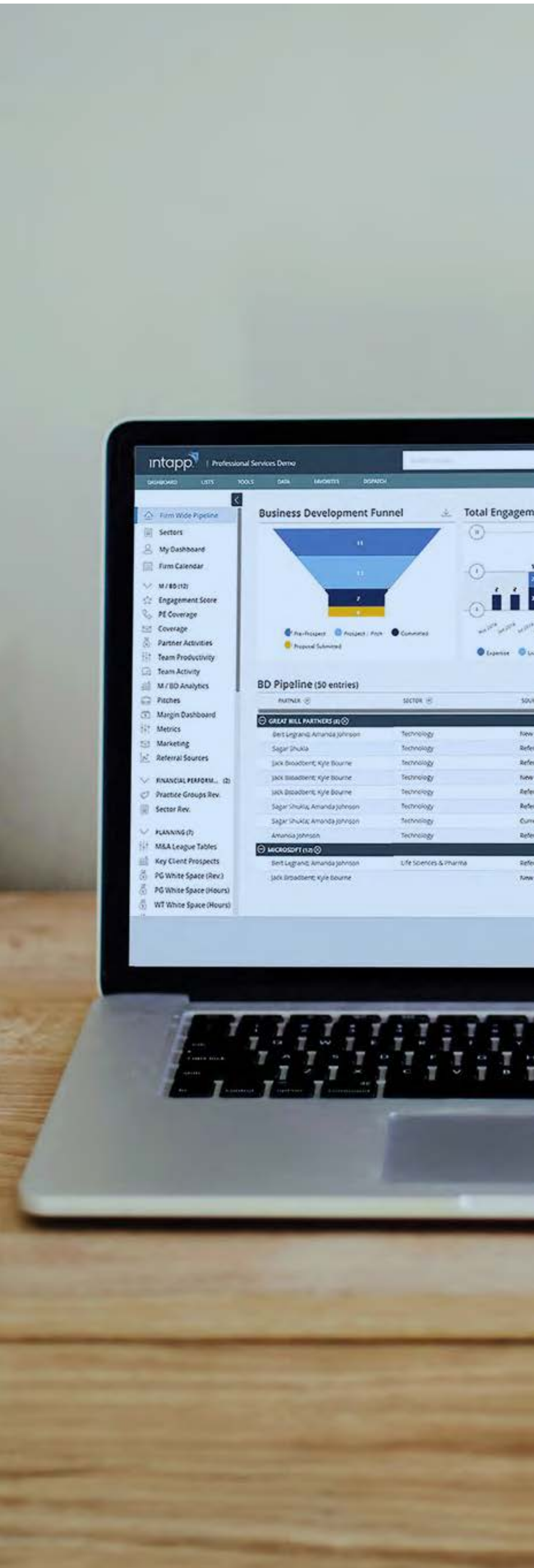
STRUCTURE

90% of digital ecosystems include three or more different deal types (e.g., contractual relationships, platform partnerships, or minority shares).

[10] McKinsey & Company. "Improving the Management of Complex Business Partnerships."
[11] Boston Consulting Group. "The Emerging Art of Ecosystem Management."
[12] Accenture Strategy. "Cornerstone of Future Growth: Ecosystems."

Roles in the Deal Ecosystem

Every firm has a part to play and value to be gained by utilizing their collective expertise.



Connecting the dots

At its core, a valuable ecosystem is rooted in relationships and insight. The key challenge is how to better evaluate and leverage these resources to increase time to value.

The dynamics in today's dealmaking environment make it difficult to fully harness the inherent value of deal ecosystems. Establishing a deal ecosystem based on insights is an important first step, but there is a need for modern technology to connect together disparate domains and experts to create mutually beneficial value. A systematic approach to harnessing the insights from both structured and unstructured data is necessary in order to benefit from "all the goodness" a dealmaking ecosystem has to offer. Phone calls and Monday morning meetings are siloed activities that do not make full use of the assembled relationships, market intelligence, and expertise.

With thousands of investment banks and M&A advisors in the U.S. and even more worldwide, it's easy to understand why most buyers and lenders have a hard time keeping track of who's who. But the fact that there are a lot of bankers doesn't mean maintaining those relationships is any less important.

Similar to tracking the departures of bankers from one firm and their arrival somewhere new, private equity firms and lenders should keep a keen eye on the new firms being created and the deals they're bringing to the market. The trend is clear: most intermediaries are doing just a few deals a year. In fact, according to a recent report from Sutton Place Strategies, more than 70% of intermediaries closed three or fewer deals in 2018, making it even harder for sponsors to track and maintain relationships with these firms.

The value of tracking the formation of new firms is that sponsors and lenders can use the move as a conversation starter, and it can be used to reorient the relationship and reestablish mutual interest. Perhaps most importantly, it keeps firms top of mind. And since many of these spin-off firms include professionals from the most prominent financial advisory firms, it's important that a new coverage model be built so that a firm isn't passed over for deals.

It's always a smart idea to review the deals that are coming into the pipeline and to assess their relevance to your investment thesis. But many firms forget to review the deals that are relevant but that they *didn't* see. By looking at the total universe of deals that key intermediaries are closing, firms can better assess where they missed out.

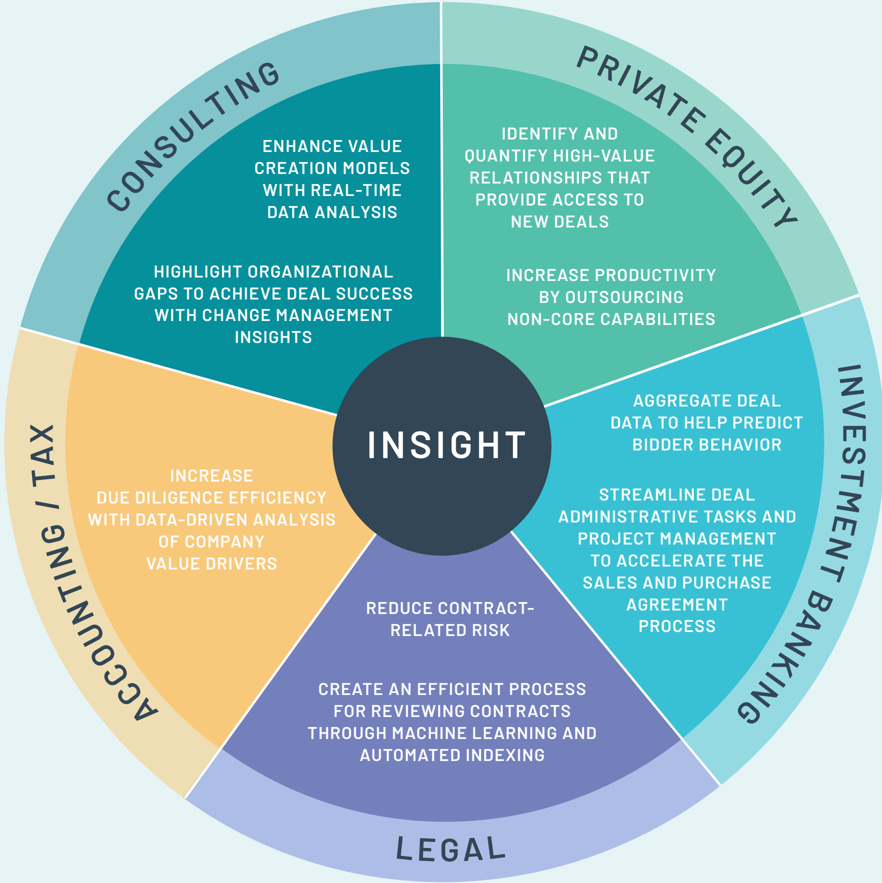
Smarter, faster dealmaking decisions

Once firms have built an insight-based deal ecosystem, how do they derive the highest value from those relationships in an efficient and cost-effective manner? Modern technology can help.

In 2018, Deloitte surveyed 1,000 corporate executives and private investors and found that 63% are using new M&A technology tools (not just spreadsheets) for reporting and integration — and to help make deals work.[13] However, the potential of technology in the dealmaking process goes well beyond reporting and integration. In Deloitte's 2019 study, 43% of respondents reported that the most important factors to achieving a successful M&A transaction include proper target identification, accurately valuing a target, and a sound due diligence process.[14]

The Intelligent Ecosystem

By bringing together business and relationship intelligence at the right time and the right place within dealmakers' daily workflows, the deal ecosystem is positioned to make smarter, faster decisions.



[13] Deloitte. "The State of the Deal M&A Trends 2018."
[14] Deloitte. "The State of the Deal M&A Trends 2019."

Indeed, leveraging data and analytics across the deal lifecycle is becoming more commonplace. A poll conducted by Intralinks found that dealmakers use data and analytics to reinforce an investment case (54%), target specific organizations or sectors (41%), identify over- and under-performing businesses (39%), and improve price by maximizing parties involved in an auction process (23%).[15] In many cases, however, dealmakers are not yet harnessing the true potential of data. By layering structured data (e.g., contact information, email conversations, business development activities, etc.) and unstructured data (e.g., Dun & Bradstreet, Preqin, PitchBook, etc.), dealmakers can identify more rewarding deals and more fruitful relationships. Additionally, through increased transparency across the ecosystem, firms can efficiently assess which information is relevant through contextualized data and trends. For example, the health of a relationship can be assessed by accessing a single view into the quantity and quality of deals sourced, the fees paid, the quality of the relationships with contacts involved in the transaction, and how many meetings are held.

The insights you gain from your relationships allow for fast action with more confidence. With the application of artificial intelligence and natural language processing, activities that previously took months can now be completed in days, often with more accuracy. The resulting deals are more lucrative and executed in a more efficient and cost-effective manner. With this intelligence, dealmakers can create blueprints for success and replicate best practices moving forward.

By forming an intelligent ecosystem, firms will be well-positioned to expand their footprint with existing clients and create relationships with new clients. Private equity firms can source more proprietary deals, successfully deploy capital, and generate higher returns for investors. Similarly, the service providers in a deal ecosystem can boost their reputation, increase market share, and move up the league tables while demonstrating their value to clients.

[15] Intralinks. "Data-Driven Dealmaking: Impact of Data and Analytics on the M&A Process."

HOW DEALMAKERS USE DATA AND ANALYTICS[15]

TO REINFORCE AN INVESTMENT CASE
54%

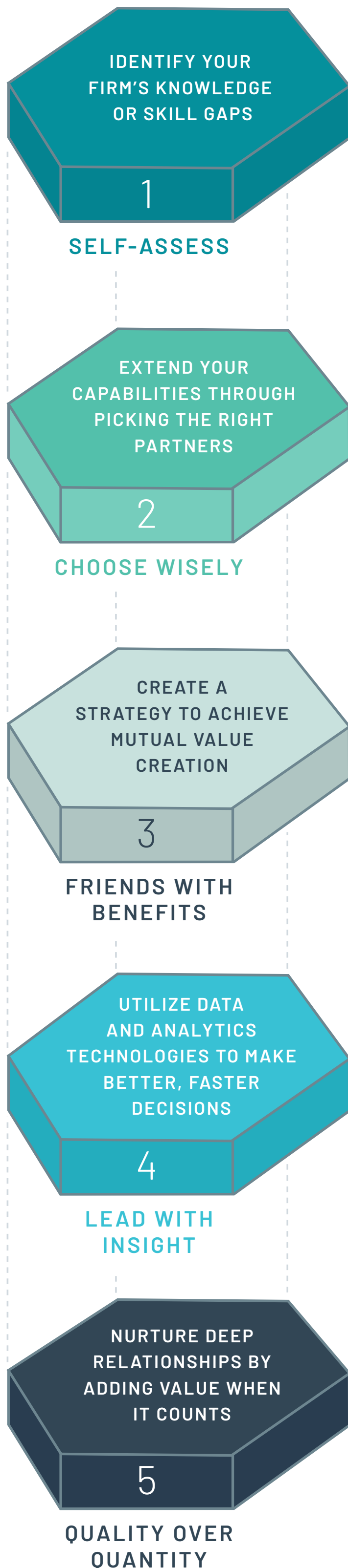
TO TARGET SPECIFIC ORGANIZATIONS OR SECTORS
41%

TO IDENTIFY OVER- AND UNDER-PERFORMING BUSINESSES
39%

TO IMPROVE PRICE BY MAXIMIZING PARTIES INVOLVED IN AN AUCTION PROCESS
23%

An Intelligent Deal Ecosystem

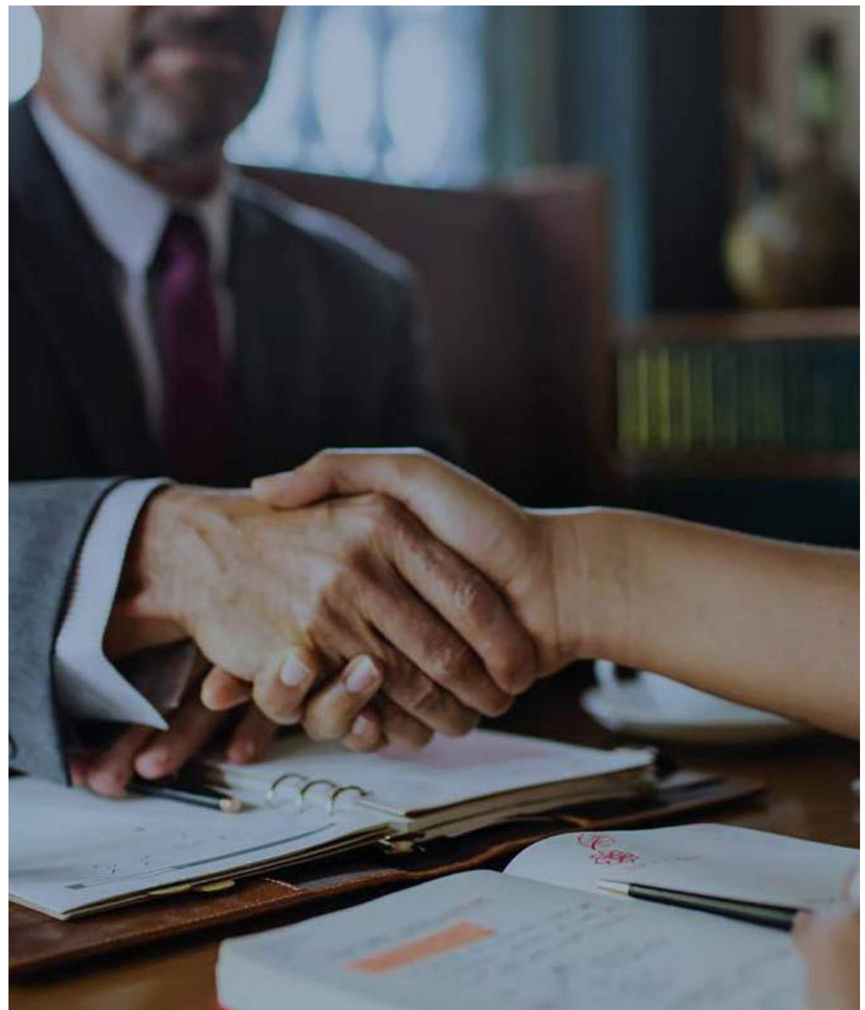
5 Steps to Building a Smart Deal Ecosystem



Where to start

Deal ecosystems become intelligent by combining their data, talent, and expertise. Dealmakers can quickly assess who they should be targeting for their next deals, which firms they should engage with more, and, overall, which intermediaries generate the highest ROI. Additionally, participation provides significant benefits as dealmakers can pool their talent to create a best-in-class ecosystem that increases access to experience, expertise, and differentiated capabilities.

With competition and dry powder more prevalent than ever, it's critically important for dealmakers to keep their strategies close and their relationships closer. Because of the increasingly complex nature of these relationships, traditional systems are no longer sufficient. Modern technology supercharges the deal ecosystem, allowing dealmakers to focus on their priorities, streamline existing workflows, reduce time spent on manual tasks, and accelerate the time to value. By utilizing data and analytics in the run-up to a closed deal, firms that engage in deal ecosystems can expect higher returns and are better positioned for success than their competition, especially in today's difficult dealmaking market.



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OnePlace for Leaders and Partners leverages today's most powerful technology to provide professional services leadership with intelligence from activities across the entire client lifecycle, from sourcing through origination and execution.

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