Deutsche Bank
Research

M&A outlook 2024: The recovery begins

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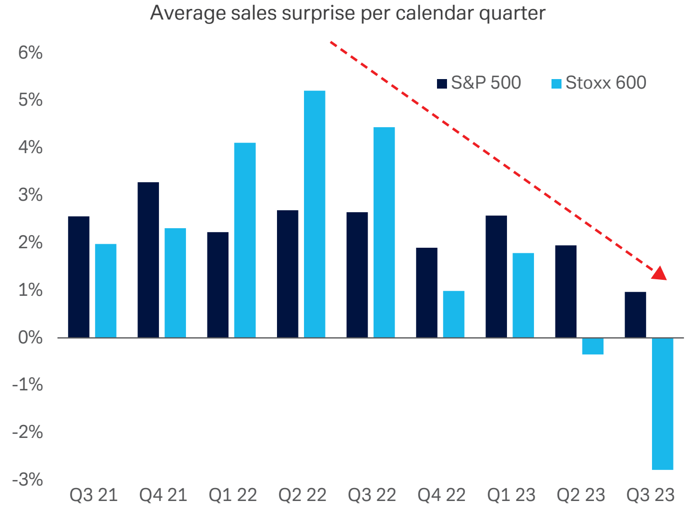
It has been a brutal two years for dealmaking. Following the M&A boom of 2021, the value and volume of deals remains well below historical averages in the US and Europe. Yet, we see 2024 as a year of recovery for M&A activity, and there are three key themes we believe will catalyse it:

1. Eager buyers and valuation dislocations
2. The need for large firms to supplement declining organic profit growth
3. Greater certainty in the financing backdrop

There is pent-up demand from cash-rich buyers. In fact, aggregate and median cash balances are near their historic highs in both the US and Europe. Many corporates have strong balance sheets and want to increase market share now that there is more market certainty. At the same time, larger buyout funds have plentiful dry powder and investors pushing them to deploy it.

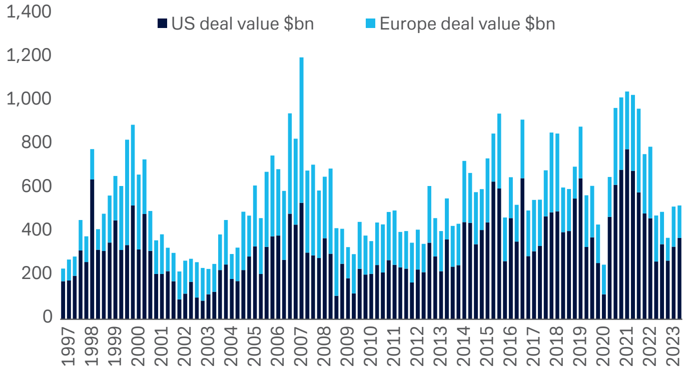
There is also a bountiful universe of targets. The median large US company trades with a valuation at 2019 levels. Multiples in healthcare and communications have been especially hard-hit. Yet, many firms now have stronger earnings. Some of the potential targets are fundamentally good companies that simply struggle with bad capital structures, so the rising cost of capital has outweighed the return on invested capital. These companies are relatively cheap and their current owners will likely be open to offers to release value.

Slowing organic growth to incentivise dealmaking



Source: Bloomberg Finance LP, Deutsche Bank

M&A volumes remained subdued in 2023



Source: Dealogic, Deutsche Bank

Some investors are concerned that higher-for-longer interest rates will continue to stymie dealmaking. They are concerned that approaching debt maturities will weigh on financially-weak firms. This may be true, but our analysis shows that M&A cycles depend more on investor sentiment than the level of borrowing costs, so this year's equity market recovery augers well. In addition, when financially-weak firms are under pressure, it can create valuation distortions that can make for attractive targets. Cyclical and consumer firms across the US, Europe and Asia are among those most affected by these themes.

Aside from the means and opportunity to do deals, corporate buyers also have strong motivations. Organic sales growth and profit margins continue their medium-term down trend not least due to slowing economic growth and inflation. Supplementing this with M&A is a logical step.

Most importantly, 2024 will likely be a year of greater market certainty – borrowing costs have likely peaked; inflation is receding. This applies to the funding backdrop as well. Many large corporates have debt capacity and can divert some cash to M&A from buybacks. The fundraising wave in private credit will also support dealmaking. True, recession may strike but it is predicted to be mild and, in some ways, that has already been priced in.

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