Directing Disruption: AI and Cybersecurity Underline Tech Sector’s Flair for Self-renewal
Methodology
In Q2 2023, Mergermarket surveyed 300 dealmakers from around the world to gain insights into the future of technology-related M&A. Respondents were equally distributed among corporates with a minimum of $250 million in annual revenue and private equity (PE) firms with a minimum of $500 million in assets under management. With respect to geography, 30% of respondents were based in North America, 30% in Europe, 30% in the Asia-Pacific (APAC) region, and 10% in Latin America. All responses are anonymous and results are presented in the aggregate.
Executive Summary

The burden of high interest rates, challenging financing conditions, and disquiet in the banking sector contributed to a marked decline in technology M&A at the start of this year. Compared to the first half of 2022, H1 2023 saw M&A in the technology, media, and telecoms (TMT) arena drop by around a third in terms of volume and by almost two-thirds in terms of value year on year. And yet, for this innovation-rich sector, there are signs of buoyancy.

Global tech markets recaptured investors’ focus following the strong H1 performance of key stocks. The Nasdaq Composite Index rose by 32.1% through the first six months of 2023, marking the index’s best start to a year in three decades. Looking ahead, dealmakers seem to believe this improvement may presage stronger M&A performance; around half of the respondents to this survey believe tech M&A deal volumes and average deal values will rise over the next 12 months.

Regarding the key subsectors for expected tech M&A activity, survey respondents believe the cybersecurity space will offer the best opportunities for dealmaking over the next 12 months. This trend has grown in significance since early 2020, when the COVID-19 pandemic led to a boom in remote working and a subsequent increase in cyber-attacks on individuals’ less secure at-home set-ups.

However, no tech subsector has garnered more popular interest in the public sphere lately than artificial intelligence (AI), especially advances in generative AI. This was forecast in the 2022 edition of this report, when the largest share of respondents said the AI/machine learning subsector would present the best opportunities for dealmaking over the subsequent 12 months.

Consumer and investor excitement has gathered pace as AI applications begin to recalibrate existing business models and spur the creation of entirely new ones. This is not to say the market is ready to ride the AI wave to a new zenith of tech M&A; innovation in the field will inevitably precipitate a bout of regulatory pressures. Rising antitrust scrutiny and issues relating to national security also continue to weigh especially heavily on the sector.

To gain a deeper understanding of these key trends and challenges, we surveyed 300 tech dealmakers from around the globe to gain their insights into what precisely is driving M&A strategies in the near and medium term. As we’ve discussed in previous editions of this study, now in its third year, disruption is the norm for this industry; businesses understand they cannot risk falling behind the competition.

As H2 unfolds and dealmakers look to 2024, tech M&A activity may be poised for an upswing. A “soft landing” for the world economy seems more likely now than at the start of 2023, and interest rate cuts could be introduced early next year. Long-term secular trends, propelled by digital transformation and improving data analytics processes, will also continue to generate interest in tech M&A, touching all industries. Between these key M&A drivers, the end of 2023 may yet see a turnaround in global tech dealmaking.

“This year’s Tech M&A survey reflects views influenced by a choppy global technology M&A market that has been impacted by the realities of challenging financial trends,” notes Brandon Parris, San Francisco partner and co-chair of Morrison Foerster’s global M&A practice. “But as we look to 2024, despite macroeconomic uncertainties, there is much to be encouraged about, especially with the rise of generative AI and the renewed focus on cybersecurity innovation. We expect these and other technology areas to have a massive impact on global deal activity in the years to come.”
Key Findings

In the first six months of 2023, 4,840 M&A transactions targeting TMT assets were announced globally, worth a combined $247.4 billion. Though down markedly year on year—by 63% in value terms and 30% by volume compared to H1 2022—TMT continues to account for a very sizable share of global M&A. In H1, TMT contributed 24.4% of transactions announced across all sectors, and 17.8% of aggregate global deal value.

Over half of the PE firms surveyed (58%) are forecasting an increase in tech M&A deal volumes over the next 12 months, perhaps a reflection of the deep stores of dry powder available to these respondents. Meanwhile, just 38% of corporate respondents feel the same way, possibly reflecting stock market volatility and increased regulatory demands. There is some cautious optimism, however, regarding expected average tech M&A deal values, with 51% of respondents overall predicting an uptick.

Almost all PE firms surveyed (91%) expect to make use of minority investments in their tech M&A plans over the next 12 months, up from 62% who said the same in our 2022 study. Corporates, too, are leaning into minority ownership, with sizable shares of these respondents showing a preference over the next 12 months for joint ventures (73%), contingent consideration (72%), and minority investments (61%), with each of these deal structures more popular this year than they were in our 2022 study.

The primary driver of respondents’ tech M&A strategies over the next 12 months will be scaling up to increase competitiveness, which attracts 17% of first-place votes, the largest such share, and 44% of top-three votes overall. Only “keeping pace of technological advancement” garners more top-three votes (51%). A notable secondary M&A driver is securing working capital and focusing on liquidity, which accrues 19% of second-place votes, the largest share among secondary drivers.
Asked to identify the prevailing tech subsectors for M&A, a quarter of respondents believe the cybersecurity space offers the single best opportunities for dealmaking over the next 12 months. The next most popular responses include AI/machine learning (18% of first-choice votes) and enterprise/logistics software (16%).

Across all markets, there has been a notable increase in the importance of environmental, social, and governance (ESG) considerations when choosing tech M&A targets, compared to the figures published in our previous report. Overall, respondents gave a score of 7.85 out of 10 for ESG’s significance in choosing the target in their most recent tech M&A deal, rising to 8.45 with respect to selecting their next tech M&A target.

The vast majority of respondents (81%) expect antitrust scrutiny of tech M&A to become either somewhat or significantly stricter over the next three years. This would compel PE firms to look more toward expansion into different industries and/or areas of tech, while corporate respondents say rising scrutiny would deter their organization from seeking targets with a close connection to privacy and/or consumer data.

The biggest trend in tech M&A over the next three years is expected to be the rise of industry disruptors, such as, this year, generative AI specialists (19% of first-choice votes overall), followed by tech industry consolidation (16%). North American respondents specifically are also quick to cite the increasing adoption of alternative deal structures as a key trend (25%).
SECTION 1: Market Overview

Although tech M&A activity has retreated from the anomalously prodigious highs achieved post-pandemic, there are unmistakable tailwinds in the sector’s sails.

The resurgence of tech equities and buoyant sentiment around AI did not translate into higher levels of dealmaking in H1, although expectations that monetary policy might begin to loosen in the near term may help support a brighter end to 2023.

Through the first six months of the year, 19,808 transactions worth a combined $1.39 trillion were announced globally across all industries, representing declines of 14.4% and 37.7%, respectively, compared to the same period last year. Total deal volume fell considerably from the first quarter to the second, while aggregate deal value in fact rose quarter on quarter.

The TMT sector was not immune to the global slowdown. Headwinds inhibited dealmakers’ appetite for big-ticket transactions and increased the due diligence burden to ensure strategic alignment and appropriate valuations. The FDIC receivership of Silicon Valley Bank, a major lender to tech startups, on March 10 epitomized the industry’s hardships in early 2023. Regulators were able to avert contagion in the rest of the wider banking system, though other institutions, including Silvergate Bank, which had significant exposure to cryptocurrency volatility, also failed in mid-March.

Nonetheless, TMT dealmaking did still prop up global activity in H1, representing 24.4% of all M&A transactions announced. In total value terms, those TMT deals accounted for 17.8% of all M&A activity globally, down from the 30.1% that it contributed during the same period in 2022. Year on year, the aggregate value of TMT deals slumped by 63% to $247.4 billion in H1, a weaker showing than even at the early height of the COVID-19 pandemic, when $287.1 billion worth of TMT deals were recorded globally in H1 2020. In volume terms, TMT dealmaking slowed by 30% year on year to 4,840 transactions, the lowest six-month total since the latter half of 2015 (4,380 deals announced).

The U.S. remained the dominant market for TMT dealmaking, as conditions favored mid-market domestic tech M&A opportunities. Still, total volume and value figures were both down substantially from H1 2022, with inflation and tighter financing conditions creating burdensome valuation gaps. In H1 2023, there were 1,499 transactions targeting U.S. TMT assets announced, worth a combined $116.4 billion, down 35% and 73.1%, respectively, from the same period a year prior, plainly illustrating the dearth of larger deals over the last 12 months.

Accelerating Digital Transformation

Although activity has cooled, businesses understand that M&A represents the fastest way to maintain market competitiveness and benefit from accelerated growth, as well as to acquire talent, keep pace with new tech innovations, and support entry into new markets.

“There is more emphasis on growing the customer base in the next 12 months,” says a partner of a PE
firm based in China. “As new businesses emerge, customer attention could be drawn to new products and services, especially if they are digitally advanced. We can improve the strength of our customer base through acquisitions.”

As generative AI, robotics, automation, and other technology solutions inspire the evolution of products, services, and business models, corporates and PE firms continue to invest through M&A for the latest technology and highest returns, despite ongoing macroeconomic and geopolitical headwinds. Almost half of respondents surveyed (48%) are projecting an increase in tech M&A deal volumes over the next 12 months. Just under a third (29%) expect volumes to remain largely the same. These figures do, however, represent a decline from last year’s survey, when 76% of respondents forecast an increase in activity over the preceding 12 months.

PE firms are more bullish than their corporate peers regarding deal volume expectations because of the amount of dry powder and a divergence in strategic investment goals. Over half of PE firms surveyed (58%) project an increase in activity, compared to 38% of corporate respondents who expect the same. In H1, PE players targeted TMT assets in 1,944 deals globally, worth $141.3 billion combined, down 40.3% and 66%, respectively, year on year. The optimism expressed among our PE respondents may, in part, be inspired by a growing belief that the monetary tightening cycle is near its peak. Rate cuts in the not-so-distant future would certainly help to ease conditions for leveraged buyouts (LBOs).

Patrick Huard, co-chair of Morrison Foerster’s Global Private Equity Group, says, “There is a strong sense of optimism among PE firms for future dealmaking, particularly in the tech space as AI, robotics, and...
other emergent technology sectors continue to develop and mature.”

Regionally, overtaking their U.S. peers as the most bullish, dealmakers in APAC expect to see the most dealmaking, with 58% forecasting an increase in M&A transaction volumes over the next 12 months. Half of North American and 47% of European survey participants project an increase.

There remains cautious optimism that average tech M&A deal values will rise over the next 12 months, with just over half of all respondents (51%) projecting an increase, including 10% who expect the increase to be significant. Again, dealmakers in APAC (54%) and North America (53%) are somewhat more bullish than their peers in Europe (47%) and Latin America (40%). These figures are broadly down from our 2022 survey, when 82% of respondents overall were forecasting an increase in average tech deal values over the following 12 months and only 5% projected a decrease, versus 25% this year.

Still, the tech sector is supported by exceptional tailwinds, as we address in the next two chapters of this report. Buyers are eager to acquire companies that can accelerate their digital transformation, although valuations must be aligned to core fundamentals, rather than being unduly inflated by “hype” or broader narrative trends.
SECTION 2: The Way Forward

From AI to cybersecurity, there is no shortage of innovation to spur tech M&A, and dealmakers the world over know they must not lose ground to their competitors.

M&A is an essential pillar of strategic growth and development for businesses and investors. Dealmakers must weigh several factors, including competition with other would-be acquirers, increased regulatory scrutiny, and how to navigate the extant financing conditions, but M&A’s ability to accelerate innovation within a business through acquiring new talent and intellectual property (IP) makes the process acutely important.

All PE firms responding to our survey report that they completed at least two tech M&A deals over the last 12 months, including 68% who made four or more transactions. These figures are up compared to the last edition of this study, when 49% of PE firms reported completing four or more tech deals over the preceding 12 months. Among corporates, 14% completed four or more transactions, 63% made two or three, and 23% made just one tech deal over that period. In our previous survey, 60% of corporates reported undertaking two or more deals.

Increased dealmaking reflects a higher number of smaller domestic deals, as PE and corporate acquirers look to scale up to accelerate growth and innovation to remain competitive. The upswing in PE activity in particular aligns with a rising sense of urgency to deploy dry powder in an effort to drive digitalization and incorporate AI innovation in products and services.

How Many Tech M&A Deals Did Your Organization Complete over the Last 12 Months? (Select One)

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<td>Europe</td>
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<td>50%</td>
<td>36%</td>
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<tr>
<td>Latin America</td>
<td>17%</td>
<td>53%</td>
<td>30%</td>
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Roughly How Many Tech M&A Deals Does Your Organization Expect to Complete over the Next 12 Months? (Select One)

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<tbody>
<tr>
<td>Total</td>
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<td>Europe</td>
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<td>33%</td>
<td>43%</td>
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<tr>
<td>Latin America</td>
<td>20%</td>
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Looking ahead, the bulk of corporate respondents (46%) expect to undertake two or three tech M&A deals over the next 12 months, and almost a third (31%) forecast completing just one. More than half of PE respondents (55%) expect to make four to six transactions, and a further 15% project undertaking seven or more.

The bulk of APAC (38%), European (43%), and North American (42%) respondents all expect to undertake four to six tech deals over the next 12 months. Their Latin American peers anticipate more moderate activity, with 63% expecting to undertake two or three such transactions. These figures are up year on year from our previous survey. The U.S. market is especially rich in opportunities across digital infrastructure and AI, supported by strong pools of employee talent, with experts in innovative tech fields in very high demand.

Uncertainty Necessitates Creative Dealmaking

Responding to tighter financing conditions and broader macroeconomic uncertainty, M&A executives over the last couple of years have pivoted toward creative deal structures that protect their organizations from harm while enabling them to capitalize on innovation.

For instance, over the next 12 months, virtually all PE firms surveyed (91%) expect to make use of minority investments in their tech M&A plans, up noticeably from the 55% who said the same in our 2022 study. Additionally, almost two-thirds say they are considering employing contingent consideration/earnouts (65%), club deals (60%), and convertible debt investments (57%).
The preference for minority investments can be attributed to investors’ increased risk aversion, which has several influences. These include rising interest rates and the collapse of the debt syndication market, which make transformational acquisitions much more difficult to finance. An additional related development has been the rise of private credit markets, which may offer would-be dealmakers new sources of capital for minority ownership investments.

The sheer growth of the tech sector, as well as strengthening company valuations in H1 2023, has contributed to a high investor preference for minority ownership. In some cases, investors may also be interested in minority ownership as a way to form strategic partnerships with tech companies while limiting risk exposure and reducing their financing requirements. Corporates are taking the same factors into account, showing a preference for joint ventures (73%) over the next 12 months, followed by contingent consideration (72%) and minority investments (61%). All of these three potential avenues are more popular among respondents this year than they were in our 2022 study.

Enduring Appeal of Early-Stage Assets
Higher borrowing costs and reduced access to credit have stifled megadeals and increased the attraction of smaller transactions, with investors becoming even more selective about the startups in which they choose to invest. According to Mergermarket data, the 10 largest TMT M&A deals announced in H1 2023 were worth a combined $83.8 billion, significantly below the equivalent of $267 billion logged in the same period in 2022.

Are You Considering Employing Any of the Following Deal Structures in Your Tech M&A Plans in the Next 12 Months? (Select All That Apply)

<table>
<thead>
<tr>
<th>Deal Structure</th>
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<tr>
<td>Minority Investments</td>
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<tr>
<td>Contingent Considerations/Earnouts</td>
<td>72%</td>
<td>65%</td>
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<tr>
<td>Joint Ventures</td>
<td>27%</td>
<td>27%</td>
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<tr>
<td>Convertible Debt Investments</td>
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<td>57%</td>
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<tr>
<td>Club Deals</td>
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<tr>
<td>Equity Clawbacks</td>
<td>31%</td>
<td>43%</td>
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<tr>
<td>Private Investment in Public Equity (PIPE Deals)</td>
<td>13%</td>
<td>47%</td>
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As was the case in last year’s survey, there is a marked preference among our respondents for targeting younger tech companies in acquisitions; in our 2022 study, only 15% of respondents said they primarily target mature companies (those operating for five years or longer), with that share remaining largely unchanged at 14% this year.

Instead, almost half of respondents overall (46%) say they primarily target companies that have operated for between two and five years, and a further 40% primarily target startups (companies operating for less than two years). Interestingly, this is an inversion of last year’s findings when startups were favored by the largest shares of corporate and PE respondents.

Younger tech companies serve as strategic investments for buyers seeking to acquire specific technological capabilities, valuable IP, and patent portfolios, as well as highly skilled professionals aligned with innovative and disruptive cultures. In addition, younger tech companies are also seen as having higher growth potential, while their earlier development stage commands a smaller price tag that requires lower levels of financing.

However, this enduring acquisition preference for younger companies is set against a backdrop of declining early-stage and venture capital funding for startups. According to Crunchbase data, early-stage funding slumped by 45% year on year to $27 billion in Q2, which followed a 54% annual drop in Q1 to $25.6 billion, marking four consecutive quarterly declines. This is the weakest funding quarter for early-stage companies since 2021.

Late-stage funding, including corporate rounds and PE to venture-backed companies, stood at $31 billion in Q2 2023, the lowest quarterly total since 2018, according to the same dataset. It follows Q1’s $43 billion tally, which represents a very dramatic fall from $93 billion in Q1 2022.

Overall, global venture funding dropped to $130.2 billion in H1 2023, according to CB Insights data. The $60.5 billion of venture capital invested globally in Q2 represented the lowest levels since the peak of the pandemic, in Q2 2020. The picture in the U.S. is even less rosy, with funding there falling by 27% quarter on quarter to $31.3 billion in Q2 of this year.

### Flight to Familiarity

Aside from global economic unpredictability and difficulty in securing financing, the tech sector must also contend with increased regulatory demands, particularly with respect to consumer data and privacy, to say nothing of concerns related to national security and key tech infrastructure. The European Commission is set to introduce new rules to ensure stronger enforcement of its far-reaching General Data Protection Regulation, and India passed a landmark data protection bill in August 2023. Challenges relating to these sorts of regulations are only exacerbated when trying to execute cross-border M&A.

For the moment, buyer hesitation in cross-border deals is most acute in U.S.-Sino transactions. As a partner in a Chinese firm puts it, “There is still a sense of uncertainty when we speak about international deals. The sanctions and protectionist views can be stressful, especially when these hindrances are revealed when we are mid-way through the deal.”
Many of these headwinds are absent or considerably less disruptive when conducting transactions domestically. In the domestic middle-market segment, acquirers point to the greater opportunity for value creation, familiarity in due diligence, and speed with which they can finalize decisions, all of which help to expedite deal closure, minimize risk, and maximize returns.

This near-term preference for domestic dealmaking is borne out in our survey. Among our overall respondent pool, just over two-thirds (68%) of their projected tech M&A activity on average over the next 12 months is expected to be domestic in nature.

This trend is broadly consistent globally, with respondents in North America, Europe, and APAC expecting around a third of their tech dealmaking to involve international targets, in line with the findings from last year’s edition of this study. Their peers in Latin America, meanwhile, are much more likely to emphasize domestic tech M&A, with these respondents expecting just 10% of their dealmaking to be cross-border in nature, down from 20% last year.

Randy Bullard, Morrison Foerster partner and co-chair of the firm’s Latin America Desk, notes: “Due to regulatory and size-of-market concerns, large Latin American acquirers are only beginning to reach across borders to explore technology M&A outside their home jurisdictions, so it is not surprising that LatAm survey respondents anticipate a higher level of focus on the domestic tech M&A transactions.”

North America is the world’s largest tech market, being home to some of the most important global players in the space and benefiting from a mature venture capital ecosystem. It is unsurprising, given these factors, that the bulk of our survey respondents continue to identify North America as presenting the best opportunities for tech M&A over the next 12 months. Around one-third of all respondents (32%) cite North America as their number-one market globally, while a further 30% selected it as second or third.

“Looking at the latest deal sourcing opportunities, we would like to consider more international deals. There are many technology hubs in the U.S., and we are confident about finding targets in the region. The target pool in tech hubs in the U.S. is attractive,” says the CFO of a Canadian corporate.

Europe, meanwhile, accrues 25% of first-choice votes, as well as 22% of secondary ballots and 16% of tertiary votes. This may reflect resilience in the TMT M&A space in core European markets such as the UK and Germany. As mentioned previously, global TMT M&A activity declined considerably, by 32% in volume terms and 48.1% in aggregate value terms, between H1 2023 and the same period the year prior. By comparison, the drop-offs in TMT M&A in the UK and Germany were not as chilling given the financial and macroeconomic context.

In H1 2023, 356 deals targeting UK TMT assets were announced, worth a combined $160 billion, down 15.2% and 45%, respectively, from the same period in 2022. In Germany, 214 transactions worth $6 billion were announced, representing declines of 27.5% and just 27%, respectively, from H1 2022.

“These results correlate with the deal flow we have seen in Germany,” says Dirk Besse, managing partner of Morrison Foerster’s Berlin office and head of the Germany M&A practice. “While global activity slowed from the historic highs of prior years, German and international acquirers alike continue to show a strong appetite for tech M&A in Germany and throughout Europe.”
We’ve seen relatively consistent deal flow within the UK M&A market, although we have noted an increase in complexity,” notes Andrew Boyd, managing partner of Morrison Foerster’s London office. “Technology companies are navigating a more volatile M&A and regulatory environment, and as the survey draws out, we are seeing an increased focus on ESG and sustainability in international dealmaking.”

Europe’s reputation as a hotbed for tech M&A reflects not only the strength of major metropolises, such as London, Berlin, Paris, and Amsterdam, but also how other markets at the edges of Europe readily punch above their weight, with the Baltic nations setting the best example for their peers elsewhere in the world. For instance, Estonia, with a population of around 1.3 million, is home to 7.7 unicorns—startups with valuations exceeding one billion—per million inhabitants, the highest per capita rate in Europe and second-highest in the world, behind only tech-titan Israel.

Asia (excluding China and Japan) comes in third place overall, with 13% of first-place votes for preferred region for tech M&A over the next 12 months. Asia’s placing represents a fall from being the second-most popular market overall after North America in last year’s survey. This is perhaps indicative of the degree to which more-familiar Europe has grown in cross-border tech dealmakers’ estimations in this complicated macroeconomic climate, rather than suggesting that Asia has become less hospitable to tech M&A over the last 12 months.

Indeed, there is much to recommend Asia, with developing economies including Vietnam, Malaysia, and Indonesia, among others, emerging as tech hubs. As one head of strategy of a U.S. corporate says, “There are better prospects in Asian markets, which include the talent capabilities. The valuation of targets in markets in Asia would be more favorable. We look forward to completing more deals in the region.”

Although Greater China and Japan accrue only middle-of-the-pack scores—with our overall respondent group identifying them as the fifth- and seventh-ranked regions, respectively, in terms of offering the best opportunities for tech M&A over the next 12 months—both of these larger and more mature markets have shown resilience in the space.
As mentioned previously, global TMT M&A activity declined considerably, by 30% in volume terms and 63% in aggregate value terms, between H1 2023 and the same period the year prior. Over the same period, deals targeting Chinese TMT assets fell by around the same degree in volume terms (by 33.7% to 252 deal announcements), though the aggregate value of those transactions declined by less than 50% year on year to $19.1 billion, a marked drop-off but still better than the sector’s global performance.

“Chinese M&A activity has seen consistent declines in recent years, due in part to tensions between China and the U.S., actions taken by the PRC government focused on technology companies, and volatile market conditions in China and throughout the world. Meanwhile, regions in Southeast Asia such as Vietnam and Thailand have seen increases in deal activity, an interesting trend to keep an eye on in the coming years,” says Marcia Ellis, co-chair of Morrison Foerster’s Global Private Equity practice.

Figures relating to deals targeting Japanese TMT assets were even more positive; deal volume was down just 11.5% to 639 deal announcements, while aggregate value in fact doubled over the same period to more than $25 billion, owing in large part to a spike in total deal value in Q1 2023.

“We continue to see significant TMT deal activity in and involving Japan,” notes Nozomi Oda, partner in Morrison Foerster’s Tokyo office, “In particular, we’ve recently seen a number of high-profile take private transactions led by PE firms, part of an interesting trend that PE firms are leading dealmaking in Japan.”

**Engaging All Sectors**

As industries undergo digital transformation, broader ranges of companies are looking to acquire tech firms to help them compete in the new economy. Accelerated investor interest in generative AI and “deeptech,” among other innovations, is bringing these disruptive technologies into practically every sector to gain a competitive edge.

Acquiring companies in sectors that can most quickly and effectively deploy new technologies to expand product offerings, reach new customers, improve operational efficiency, and increase scale, is a top priority for investors. This trend is reflected in our survey, which shows comparable interest across

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**When Acquiring a Tech Company, Which End-User Industries Hold the Most Interest For Your Organization? (Select Top Three and Rank 1-2-3, with 1 Being the Industry in Which You Are Most Interested)**

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<th>Rank 2</th>
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<td>Business Services</td>
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<td>11%</td>
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<td>18%</td>
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<td>Pharma, Medical &amp; Biotech</td>
<td>9%</td>
<td>16%</td>
<td>18%</td>
</tr>
<tr>
<td>Mobility</td>
<td>6%</td>
<td>7%</td>
<td>6%</td>
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<tr>
<td>Energy, Mining &amp; Utilities</td>
<td>1%</td>
<td>3%</td>
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<td>Real Estate</td>
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<tr>
<td>Construction</td>
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<td><strong>Total</strong></td>
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</table>

**Which of the Following Tech Subsectors Do You Expect to Present the Best Opportunities for Dealmaking over the Next 12 Months? (Select Top Three and Rank 1-2-3, with 1 Being the Subsector Presenting the Best Opportunities)**

<table>
<thead>
<tr>
<th>Subsector</th>
<th>Rank 1</th>
<th>Rank 2</th>
<th>Rank 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cybersecurity</td>
<td>25%</td>
<td>18%</td>
<td>17%</td>
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<tr>
<td>Artificial Intelligence (AI)/Machine Learning</td>
<td>18%</td>
<td>16%</td>
<td>16%</td>
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<tr>
<td>Enterprise/Logistics Software</td>
<td>16%</td>
<td>16%</td>
<td>19%</td>
</tr>
<tr>
<td>Business Intelligence &amp; Data Analytics</td>
<td>13%</td>
<td>12%</td>
<td>12%</td>
</tr>
<tr>
<td>Robotic Process Automation</td>
<td>8%</td>
<td>9%</td>
<td>9%</td>
</tr>
<tr>
<td>Customer Relationship Management</td>
<td>7%</td>
<td>9%</td>
<td>4%</td>
</tr>
<tr>
<td>Cloud Technology</td>
<td>6%</td>
<td>6%</td>
<td>6%</td>
</tr>
<tr>
<td>E-Commerce</td>
<td>4%</td>
<td>7%</td>
<td>9%</td>
</tr>
<tr>
<td>Communications Solutions</td>
<td>2%</td>
<td>6%</td>
<td>6%</td>
</tr>
<tr>
<td>Semiconductors</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
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</tbody>
</table>
multiple industries. The financial services sector ranks first, with 21% of first-place votes, while business services is the most commonly selected sector overall, with 58% of survey participants overall (including 20% of first-place votes), nudging ahead of financial services (47% overall) on the back of stronger second- and third-place vote shares.

These figures invert last year’s survey when financial services accrued the most top-three selections and business services garnered the most first-place votes. Increased M&A interest within the business services sector reflects the opportunities in business intelligence and data analytics unleashed with generative AI. This is creating greater interest among larger corporates in tech companies that specialize in enterprise software, to support faster and more precise decision-making.

The consumer sector is the bronze medalist for the second year in a row, with 18% of first-place votes. There has also been a notable uptick in interest in industrials and chemicals as an end-user industry, with the sector accruing 14% of first-place votes and 36% of top-three selections overall, compared to just 5% and 15%, respectively, in last year’s survey.

Acquirers across a broad swath of industries continue to lean into M&A to accelerate business transformation, with the help of technologies including AI, “Big Data” analytics, robotics and automation, inventory and network optimization, and the “industrial internet of things.” These technologies can also help to resolve the protracted shortage of skilled labor, future-proofing companies’ ability to grow at scale in a tight labor economy.

Considering key subsectors, our survey shows the prevailing sentiment is safety first, innovation second. A quarter of respondents believe the cybersecurity space offers the best opportunities for dealmaking over the next 12 months. The subsector accrues a combined 60% of top-three votes, more than any other subsector, a notable change from last year’s survey, when it attracted just 28% of top-three votes and only 8% of first-choice selections. As geopolitical events remain top-of-mind, cybersecurity emerges as the fastest growing subsector. Dealmakers are evaluating macroeconomic trends against the promise of attractive returns in this subsector across small and mid-sized targets.

“Cybersecurity has become a very important part of most operations,” explains a corporate head of strategy based in Australia. “After the digital transformation move that many companies have emphasized after the pandemic, cyber threats increased, thereby providing more opportunities for cybersecurity firms to flourish.” A Finnish PE partner adds: “There will be bidding wars for top-performing companies in cybersecurity. There will be plenty of dealmaking opportunities.”

Linda Clark, a partner in Morrison Foerster’s Privacy + Data Security practice, notes: “Cybersecurity companies are becoming more attractive in the M&A space, especially those that have niche technologies aimed at preventing a cyber incident or quickly detecting one. Companies want a broad understanding of their networks and evolving threats. Companies that cover the full lifecycle—from controls design to threat detection to incident investigation—and bring to bear unique insight will continue to grow.”

Julie O’Neill, Morrison Foerster Privacy + Data Security partner, comments: “Cybersecurity has become an area of focus for a growing number of companies. To comply with increasing regulation and protect its personal and other confidential data against unauthorized or accidental loss and other threats, companies are likely to continue to turn to third-party solutions.”

The next most popular subsectors that are expected to offer the best opportunities for M&A include AI/machine learning, which garners 18% of first-choice votes and 50% of top-three selections, followed by enterprise/logistics software, with 16% and 51%, respectively.

AI was the top subsector from last year’s report and was borne out by the explosive interest and investment in generative AI and machine learning at the start of 2023. While the M&A impact of generative AI on industries is still in its infancy, investors view these technologies as foundational for future competitiveness in their ability to improve decision-making, efficiency, and task automation, and to accelerate creation of new products and services.

“The excitement from survey respondents around the generative AI space is far from surprising and mirrors the enthusiasm we’re hearing from clients across sectors,” says Tessa Schwartz, co-chair of the firm’s AI Group and co-head of the firm’s Transactions
“I would expect to see an increase in M&A activity and deal size as the AI sector matures.”

“Dealmakers do stand to benefit well from AI and machine learning deals. There are many new prospects in the subsector which companies are exploring. There is a need for growth capital, and it’s ideal for minority investments or acquisition deals,” says a U.S.-based corporate vice president of finance.

Potential M&A activity for companies focused on AI and machine learning will only grow stronger in the years to come. However, there are also some potential challenges that must be addressed before AI and machine learning can reach their full potential.

According to 29% of our survey respondents, the single biggest obstacle to the continued growth and uptake of AI and machine learning is the lack of transparency. It is often difficult to know how AI and machine learning systems are making decisions, and what data they are using, leading to concerns about copyright infringement, bias, and privacy. The next biggest hurdle (with 23% of first-choice selections) is expected to be “industrial capture,” which refers to the risk of rapid consolidation, where a small number of companies gain an outsized degree of control over AI and machine learning technologies.

Finally, there is also the potential for increasingly strict regulation and consumer skepticism, both of which emerged as significant secondary hurdles (21% and 19% of second-choice votes, respectively). As governments around the world are starting to regulate AI and machine learning technologies to protect consumers and businesses, regulation risks are stifling AI and machine learning adoption as policymakers deliberate over how to ensure that these technologies are used responsibly.

Despite these challenges, the potential benefits of AI and machine learning are vast. These technologies have the potential to improve lives in countless ways, from making businesses more efficient to accelerating breakthroughs in medicine. It is crucial to address the concerns that AI and machine learning raise, so that consumers and industries can both reap the full benefits of these technologies.

What Are the Greatest Obstacles to the Continued Growth and Uptake of AI Technologies? (Select Top Two and Rank 1-2, with 1 Being the Greatest Obstacle)

- Lack of Transparency: 29% (Rank 1), 21% (Rank 2)
- “Industrial Capture” (i.e., Accumulation of Power, Knowledge & Resources by a Small Number of Private Companies): 23% (Rank 2), 17% (Rank 1)
- Absence of Shared Safety Protocols: 18% (Rank 1), 13% (Rank 2)
- Increasingly Strict Regulation: 14% (Rank 2), 21% (Rank 1)
- Cuts to AI Ethics Teams: 10% (Rank 2), 9% (Rank 1)
- Consumer Skepticism: 6% (Rank 2), 19% (Rank 1)

The excitement from survey respondents around the generative AI space is far from surprising and mirrors the enthusiasm we’re hearing from clients across sectors.”

Tessa Schwartz, Morrison Foerster
Outlook

Faced with a challenging macroeconomic picture and unyielding competition, dealmakers know they must join the race to adopt ground-breaking tech advancements.

Dealmakers in the tech space are having to navigate a maelstrom of obstacles, with prospects of a higher-for-longer interest rate environment weighing especially on their minds. Simultaneously, though, they understand that the tech sector presents a wealth of innovations and dealmaking opportunities on which they must capitalize.

There is no shortage of drivers to motivate companies’ inorganic growth strategies. For large corporates and PE funds, bigger ticket M&A deals may enable them to acquire a strong product portfolio, build up their in-house talent pool, and/or introduce themselves to a larger customer base or perhaps even an entirely new market in which to expand. Strategic bolt-on acquisitions, too, give dealmakers the means to complement or fill gaps in their product or geographic portfolio while taking on less risk.

“Keeping pace with tech advancements without an M&A strategy would be quite challenging,” admits the managing partner of a PE firm located in Mexico. “We are prioritizing M&A dealmaking for a structured approach toward digitalization. Moreover, the customer base can be enhanced systematically.” Another PE partner, based in Finland, says: “We hear about new solutions and different companies working on ground-breaking research in the tech segment. These advancements cannot be ignored. We need to be a part of the race.”

These sentiments are echoed in dealmaking motivations worldwide. In our survey, the key driver of tech M&A strategies over the next 12 months is expected to be scaling up to increase competitiveness, which attracts 17% of first-place votes (the largest share) and 44% of top-three votes overall.

“Scaling up requires good strategic decisions as our sector has become very competitive,” says a senior vice president of corporate development at a U.S. corporate. “Competitors are constantly implementing strategic growth decisions. We need to be proactive in this regard, and reduce the business continuance risks.”

Keeping pace of technological advancement garners more top-three votes combined (51%), but it has fewer first-place selections (12%) than either scaling up to increase competitiveness or growing a corporate’s customer base (15%). In last year’s survey, these factors likewise featured among the four key drivers, in addition to portfolio streamlining/refocusing on core operations.

A notable secondary M&A driver is securing working capital and focusing on liquidity, which accrues 19% of second-place votes, the largest share among secondary drivers. “Securing working capital is a functional strategy that suits the financial conditions in present markets,” explains a PE partner based in the Netherlands.
What Will Be the Key Drivers of Your Tech M&A Dealmaking over the Next 12 Months? (Select Top Three and Rank 1-2-3, with 1 Being the Most Important Driver)

- Scaling Up to Increase Competitiveness: 17%, 17%, 10%
- Grow Customer Base: 15%, 9%, 11%
- Keeping Pace of Technological Advancement: 12%, 12%, 27%
- Refocusing on Core Markets/Regions: 11%, 4%, 4%
- Streamlining of Our Portfolio/Refocusing on Core Operations: 11%, 5%, 7%
- Talent or Acquihire: 9%, 11%, 12%
- Diversification of Our Product Offering: 8%, 6%, 1%
- Focusing on Liquidity/Securing Working Capital: 6%, 19%, 8%
- Increase in Distressed Opportunities: 6%, 5%, 5%
- Entering/Expanding Presence in New Growth Markets: 5%, 10%, 10%
- Responding to Regulatory Developments: 2%, 20%, 5%
- Keeping Pace of Technological Advancement: 26%, 48%, 67%
- Entering/Expanding Presence in New Growth Markets: 25%, 30%, 25%
- Focusing on Liquidity/Securing Working Capital: 23%, 33%, 50%
- Scaling Up to Increase Competitiveness: 46%, 46%, 46%
- Diversification of Our Product Offering: 17%, 17%, 19%
- Refocusing on Core Markets/Regions: 14%, 24%, 20%
- Streamlining of Our Portfolio/Refocusing on Core Operations: 28%, 27%, 22%
- Talent or Acquihire: 28%, 33%, 36%
- Grow Customer Base: 47%
- Increase in Distressed Opportunities: 6%, 6%, 23%

Directing Disruption: AI and Cybersecurity Underline Tech Sector’s Flair for Self-renewal | 19
By geography, Latin American respondents are considerably more likely than their peers elsewhere in the world to cite securing working capital and keeping up with the pace of technological advancement as key drivers. “Focusing on liquidity is our primary aim,” says the chief strategy officer of a Brazilian corporate. “We’ve been reviewing our capital requirements and determined that creating more liquidity in the next 12 months would really help achieve our business targets. It’s essential that we optimize technology within the company, too.”

Elsewhere, North American respondents are more likely than others to emphasize talent acquisition, while European dealmakers emphasized refocusing on core markets/regions. APAC buyers are most concerned with growing their customer base.

Inflation Weighs on Proceedings
This year’s bull run in stock markets has recentered tech as the engine of global growth, pushing up sector valuations despite persistent core inflation and interest rates running at multi-decade highs. The macroeconomic picture has also created a difficult financing environment and widened the valuation gap between buyers and sellers.

“The unsupportive financing conditions would mean that we have to look for non-traditional choices to fulfill our capital requirements,” says a corporate CFO in the U.S. “When deals are being conducted, we’re usually aware of the financing options that could be used, but now there’s a lot of uncertainty here.”

According to our survey, the greatest challenge to tech M&A over the next 12 months is expected to be inflation, which garners 21% of our overall respondent group’s first-choice votes, the largest share, and 44% of top-three votes combined. In the 2022 edition of this study, inflation was only the sixth-biggest challenge identified by our respondent group.

“The inflation threats have already limited the dealmaking options to some extent,” says a PE managing director in Sweden. “Sellers want to reconsider the valuation offer, and inflation will affect negotiations further.”

Only the issue of wide valuation gaps accrues more top-three votes overall, at 48%, with this also having been identified as the greatest challenge overall in our 2022 report. However, only 5% of the total this year is comprised of first-choice votes, suggesting that valuation gaps are largely a secondary or even third-order concern for dealmakers at the moment.

A corporate head of strategy in Spain says: “We have to deal with wider valuation gaps in the next 12 months. Sellers are bound to insist on a certain price because they have confidence in their asset quality. Due to this factor, the negotiation process could be quite long.”

Dealmaking in Wartime
National security concerns present a major risk factor in cross-border tech dealmaking. Governments around the world are increasingly scrutinizing proposed acquisitions in the tech, security-related, and data sectors.

Of particular significance are Sino-U.S. interactions, with decisions made in Washington and Beijing typically influencing regulators elsewhere in the world. Aside from scrutiny of inbound investments in certain subsectors, an important recent development saw the Biden
What Will Be the Greatest Challenges to Tech M&A over the Next 12 Months?
(Select Top Three and Rank 1-2-3, with 1 Being the Greatest Impediment)

Wide Valuation Gaps
- Asia-Pacific: 50%
- Europe: 47%
- Latin America: 41%
- North America: 52%

Inflation
- Asia-Pacific: 39%
- Europe: 49%
- Latin America: 53%
- North America: 37%

Competition for Assets
- Asia-Pacific: 7%
- Europe: 33%
- Latin America: 38%
- North America: 37%

Interest Rates Staying Higher for Longer
- Asia-Pacific: 21%
- Europe: 31%
- Latin America: 28%
- North America: 43%

Unsupportive Financing Conditions
- Asia-Pacific: 24%
- Europe: 29%
- Latin America: 23%
- North America: 27%

Market Volatility
- Asia-Pacific: 23%
- Europe: 21%
- Latin America: 27%
- North America: 33%

Lack of Attractive Targets
- Asia-Pacific: 24%
- Europe: 25%
- Latin America: 19%
- North America: 34%

Increased Difficulties in Obtaining Reliable Projections
- Asia-Pacific: 20%
- Europe: 24%
- Latin America: 23%
- North America: 30%

Weak Growth Outlook
- Asia-Pacific: 19%
- Europe: 22%
- Latin America: 25%
- North America: 30%

Unstable Geopolitical Environment
- Asia-Pacific: 14%
- Europe: 17%
- Latin America: 11%
- North America: 17%

Stricter Regulatory & FDI Environment (Including Tech ‘Protectionism’ in Key Markets)
- Asia-Pacific: 0%
- Europe: 12%
- Latin America: 17%
- North America: 11%
administration announce in August 2023 that it would ban outbound U.S. investments in sensitive subsectors in China, including the country’s AI, chipmaking, and quantum computing arenas, on security grounds. The regime—which onlookers are referring to as the “reverse CFIUS,” with reference to the long-armed Committee on Foreign Investment in the United States—is likely to enter into effect in 2024, though details are still to be confirmed by the U.S. Treasury.

But stricter enforcement of foreign direct investment regulations is a global trend, reflecting the strategic importance of tech in relation to national security, the increased sophistication of cyber threats, and the rising prevalence of data breaches. The additional scrutiny has made deals more difficult and time-consuming to complete and can lead to higher prices.

“We’ve seen several years of evolution when it comes to global regulatory mandates and enforcement around dealmaking,” notes Chuan Sun, M&A partner in Morrison Foerster’s Shanghai and Beijing offices. “While some changes have challenged global dealmaking, others have presented opportunities. What’s critical for today’s acquirer is to stay informed about regulations that could impact them.”

“There are many countries where the investigations into proposed acquisitions have increased,” says a corporate head of strategy based in the U.S. “It has taken place in Europe and part of APAC also. We cannot pursue deals in these regions as government interference in dealmaking will be high.”

A partner in a PE firm based in Finland also admitted national security concerns had deterred their firm from pursuing M&A in security, privacy, and data-related companies: “If officials in the region feel that we are conducting a deal with the intent of stealing information or there’s another hidden motive, then it affects our chances of getting an approval.”

The war in Ukraine has magnified national security concerns and increased scrutiny of cross-border deals in Europe especially. This may lead to further regulatory tightening in the years ahead, in addition to more deals that see companies divest themselves from Russia.

As a result, buyers are focusing cross-border investments in regions and regulatory environments that feature a more welcoming foreign investment environment. In our survey, more than half of all respondents (60%) say that national security-related issues and legislation deter their organizations from pursuing M&A in certain countries and regions. However, only around a quarter (26%) say these types of issues deter them from pursuing deals in particular tech subsectors.

“In Europe, the national security-related legislation will be tightened further in the coming years,” explains a senior partner at a PE firm in Hong Kong. “I am certain that the current war conditions will magnify national security concerns beyond what’s real. This will affect dealmaking decisions widely.”
Also in the sphere of regulatory inquiry and governmental priorities, more than half of respondents (57%) expect antitrust scrutiny of tech M&A to become somewhat stricter over the next three years. A further 24% expect it to become significantly stricter, with these figures aligning with the findings of last year’s survey.

For over a fifth of PE respondents (22%), the biggest impact of a tightening of antitrust law and/or scrutiny on their future tech M&A transactions would manifest in influencing their organization to look more toward expansion into different industries and/or areas of tech as an alternative to horizontal/vertical expansion.

In Which of the Following Ways, If Any, Would a Tightening of Antitrust Law and/or Scrutiny Impact Your Future Tech M&A Transactions? (Select the most Important or Leave Blank If None Are Applicable)

- Make Meeting Regulatory Requirements More Challenging and/or Costly
  - Total: 19%
  - Private Equity Firm: 19%
  - Corporate: 18%
  - Asia-Pacific: 14%
  - Europe: 16%
  - Latin America: 3%
  - North America: 17%

- Influence Our Organization to Look More Toward Expansion into Different Industries and/or Areas of Tech as an Alternative to Horizontal/vertical Expansion
  - Total: 56%
  - Private Equity Firm: 56%
  - Corporate: 59%
  - Asia-Pacific: 59%
  - Europe: 54%
  - Latin America: 50%
  - North America: 62%

- Influence Our Organization to Look Increasingly Toward Cross-border M&A as Opposed to Deals in Our Home Market Where Antitrust-Related Scrutiny is Stricter
  - Total: 19%
  - Private Equity Firm: 19%
  - Corporate: 23%
  - Asia-Pacific: 27%
  - Europe: 30%
  - Latin America: 3%
  - North America: 21%

- Influence Our Organization to Acquire Smaller Startups as Opposed to Larger Targets That May Attract More Antitrust-Related Scrutiny
  - Total: 19%
  - Private Equity Firm: 19%
  - Corporate: 16%
  - Asia-Pacific: 16%
  - Europe: 11%
  - Latin America: 15%
  - North America: 14%

- Increase Confidence That Strong Competition Within the Target Industry Might Be Less of a Potential Threat In the Future
  - Total: 19%
  - Private Equity Firm: 19%
  - Corporate: 10%
  - Asia-Pacific: 10%
  - Europe: 11%
  - Latin America: 10%
  - North America: 12%

- Deter Our Organization from Seeking Targets with a Close Connection to Privacy and/or Consumer Data That We Might Otherwise Have Pursued
  - Total: 21%
  - Private Equity Firm: 21%
  - Corporate: 25%
  - Asia-Pacific: 18%
  - Europe: 16%
  - Latin America: 3%
  - North America: 11%

- Deter Our Organization from Seeking Targets That Would Increase Market Share That We Might Otherwise Have Pursued
  - Total: 16%
  - Private Equity Firm: 16%
  - Corporate: 11%
  - Asia-Pacific: 16%
  - Europe: 15%
  - Latin America: 11%
  - North America: 15%

- Deter Our Organization from Seeking Targets for Vertical Expansion That We Might Otherwise Have Pursued
  - Total: 4%
  - Private Equity Firm: 4%
  - Corporate: 6%
  - Asia-Pacific: 6%
  - Europe: 5%
  - Latin America: 6%
  - North America: 7%
costly (versus just 10% who say the same this year). A slightly larger proportion, 22%, last year said rising antitrust scrutiny would compel their organizations to target smaller startups as opposed to bigger companies, falling to 15% in this latest study.

Among corporates, tighter antitrust scrutiny would especially deter their organization from seeking targets with a close connection to privacy and/or consumer data that they might otherwise have pursued (21%), with this also having been this respondent group’s primary concern in the 2022 edition of this report.

Alex Okuliar, co-chair of Morrison Foerster’s Antitrust Group, says, “Antitrust and regulatory scrutiny is higher than it has been in a generation, especially for the tech sector. Moreover, the FTC and DOJ are trying to implement sweeping changes in both the substance and process of merger review, which could have dramatic implications for M&A. It will be important for dealmakers to stay informed of evolving trends.”

ESG Comes to the Fore
ESG remains one of the highest priorities among shareholder activists and has become a high priority for regulators. As investors and consumers become more conscious about sustainability, companies are increasingly examining how to steward their management teams to ensure that they meet new regulatory requirements regarding corporate action and disclosure (like cybersecurity and human rights) and that they are also on course to achieve net-zero/carbon neutral and other ESG objectives.

During the spring U.S. proxy season in 2023, 335 shareholder votes seeking disclosures and action on ESG issues were proposed, according to shareholder resolution data specialist Proxy Preview. The number of climate change proposals surged to 144 filings, this year’s largest category. Most were concerned with greenhouse gas emissions and related risk management, target-setting timeframes, and net-zero goals.

In our survey, when asked to give an answer on a scale of 0 to 10, respondents gave a score of 7.85 for the degree of importance of ESG considerations in choosing the target in their most recent tech M&A deal. That figure rises to 8.45 with respect to their expectations for ESG’s significance in selecting their next tech M&A target.
European respondents give the highest scores (8.13 for degree of importance in selecting their most recent target, and 8.73 in selecting their next target). Latin American respondents give the lowest scores but log the largest increase between the two (rising by 0.9 points), suggesting that the market is more quickly factoring ESG considerations into its M&A decision-making.

Across all markets, there has been a notable increase in the importance of ESG considerations when choosing tech M&A targets, compared to the figures published in our previous report. In the 2022 survey, respondents gave a score of just 6.96 out of 10 in relation to ESG’s significance in picking their most recent target, and a score of 7.88 for their next target.

Suz Mac Cormac, Morrison Foerster partner and co-chair of the firm’s ESG and Social Enterprise + Impact Investing practices, notes: “With the rising tide of regulation—from the new CA climate disclosure rules to CSRD and SFDR in the EU—we expect that ESG factors will come into even sharper focus in mainstream (in addition to “impact”) deals and that creative tools that can be used to protect and enhance ESG will be more broadly adopted.”

Almost three-quarters of all survey respondents (72%) expect shareholder activism connected with tech M&A to increase over the next three years, including around a quarter (26%) who are forecasting a significant increase. That overall figure is broadly in line with the results of last year’s survey (71%), though in that study a notably larger share (41%) projected the increase in activism to be significant, suggesting there has been some degree of mellowing out over the past 12 months; improved performance in equity markets goes a long way toward appeasing potential activists.

In this year’s survey, 75% of PE buyers expect higher shareholder activism in the next three years, compared to 68% of their corporate peers. By region, there is a higher degree of conviction in APAC and Europe, with almost one-third in both regions (32% and 31%, respectively) expecting significant shareholder activism. By comparison, only 21% of respondents expect activism to increase significantly in the U.S.

“Do You Expect Shareholder Activism Connected with Tech M&A to Increase or Decrease over the Next Three Years? (Select One)"

<table>
<thead>
<tr>
<th>Region</th>
<th>Increase Significantly</th>
<th>Increase</th>
<th>Remain the Same</th>
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<tbody>
<tr>
<td>Total</td>
<td>26%</td>
<td>46%</td>
<td>28%</td>
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<tr>
<td>Private Equity F</td>
<td>27%</td>
<td>48%</td>
<td>25%</td>
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<tr>
<td>Corporate</td>
<td>23%</td>
<td>45%</td>
<td>32%</td>
</tr>
<tr>
<td>Asia-Pacific</td>
<td>32%</td>
<td>42%</td>
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<tr>
<td>Europe</td>
<td>31%</td>
<td>47%</td>
<td>22%</td>
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<tr>
<td>Latin America</td>
<td>0%</td>
<td>63%</td>
<td>37%</td>
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<tr>
<td>North America</td>
<td>21%</td>
<td>53%</td>
<td>26%</td>
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“Directing Disruption: AI and Cybersecurity Underline Tech Sector’s Flair for Self-renewal” by Spencer Klein, New York partner and co-chair of Morrison Foerster’s global M&A practice. “We’ve seen a global uptick in shareholder activism activity in 2023, particularly outside of the U.S. and in vulnerable sectors like financial institutions. And we’ve seen an increase in U.S. activists looking abroad. I would expect to see U.S activism with an M&A thesis to increase again as the market stabilizes and deal activity bounces back.”
Conclusion

Disruption defines the tech sector, which is in a near-constant state of revolution, from the emergence of generative AI to new regulatory developments. Dealmakers cannot afford to fall behind.

Unpredictable macroeconomic and geopolitical concerns and tepid tech M&A in H1 2023 show that powerful narratives alone are insufficient to support dealmaking. Companies understand that M&A can play a crucial role in their digital transformation plans, especially in a fast-moving and increasingly competitive market in which organizations everywhere are looking to tech to bring about operational efficiencies.

But tech deals are also reliant on supportive financing conditions and a relatively stable geopolitical environment; in their absence, M&A suffers, irrespective of the fever pitch enthusiasm around cutting-edge technologies. National security concerns over sensitive tech assets have escalated and valuation gaps have widened. Simultaneously, higher interest rates have made it more expensive to finance deals, creating a challenging environment for LBOs.

What Will Be the Key Trends in Tech M&A over the Next Three Years? (Select Top Three and Rank 1-2-3, with 1 Being the Most Important Trend)

<table>
<thead>
<tr>
<th>Trend</th>
<th>Rank 1</th>
<th>Rank 2</th>
<th>Rank 3</th>
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<tbody>
<tr>
<td>Rise of Industry Disruptors</td>
<td>19%</td>
<td>14%</td>
<td>14%</td>
</tr>
<tr>
<td>Tech Industry Consolidation</td>
<td>16%</td>
<td>19%</td>
<td>13%</td>
</tr>
<tr>
<td>Rise in Distressed Deals</td>
<td>14%</td>
<td>10%</td>
<td>6%</td>
</tr>
<tr>
<td>Tightening of Global Regulatory Environment</td>
<td>13%</td>
<td>11%</td>
<td>10%</td>
</tr>
<tr>
<td>Increased Cross-border Deals</td>
<td>11%</td>
<td>13%</td>
<td>7%</td>
</tr>
<tr>
<td>Onshoring of Business Operations</td>
<td>10%</td>
<td>13%</td>
<td>15%</td>
</tr>
<tr>
<td>Cross-industry Convergence</td>
<td>10%</td>
<td>12%</td>
<td>12%</td>
</tr>
<tr>
<td>Increasing Involvement of Alternative Funds (e.g., Sovereign Wealth Funds, Mutual Funds, Hedge Funds)</td>
<td>5%</td>
<td>6%</td>
<td>17%</td>
</tr>
<tr>
<td>Increasing Adoption of Alternative Deal Structures (e.g., Spacs)</td>
<td>27%</td>
<td>2%</td>
<td>6%</td>
</tr>
</tbody>
</table>

The stages in the economic cycle are quite unpredictable, and it is affecting dealmaking conditions. We cannot find the required value through dealmaking as per our initial expectations.”

U.S.-based senior vice president of corporate development and M&A
What Will Be the Key Trends in Tech M&A over the Next Three Years?
(Sum of Top Three)

- Increasing Adoption of Alternative Deal Structures (e.g., Spacs)
  - Total: 9%
  - Asia-Pacific: 2%
  - Europe: 31%
  - Latin America: 4%
  - North America: 25%

- Rise in Distressed Deals
  - Total: 31%
  - Asia-Pacific: 30%
  - Europe: 28%
  - Latin America: 33%
  - North America: 34%

- Tech Industry Consolidation
  - Total: 48%
  - Asia-Pacific: 47%
  - Europe: 50%
  - Latin America: 50%
  - North America: 49%

- Rise of Industry Disruptors
  - Total: 47%
  - Asia-Pacific: 44%
  - Europe: 48%
  - Latin America: 50%
  - North America: 48%

- Tightening of Global Regulatory Environment
  - Total: 34%
  - Asia-Pacific: 38%
  - Europe: 38%
  - Latin America: 38%
  - North America: 30%

- Increased Cross-border Deals
  - Total: 31%
  - Asia-Pacific: 40%
  - Europe: 31%
  - Latin America: 34%
  - North America: 13%

- Cross-industry Convergence
  - Total: 33%
  - Asia-Pacific: 36%
  - Europe: 47%
  - Latin America: 33%
  - North America: 30%

- Onshoring of Business Operations
  - Total: 38%
  - Asia-Pacific: 38%
  - Europe: 43%
  - Latin America: 40%
  - North America: 33%

- Increasing Involvement of Alternative Funds (e.g., Sovereign Wealth Funds, Mutual Funds, Hedge Funds)
  - Total: 29%
  - Asia-Pacific: 29%
  - Europe: 26%
  - Latin America: 33%
  - North America: 28%

Directing Disruption: AI and Cybersecurity Underline Tech Sector’s Flair for Self-renewal | 27
Advances in tech are rapidly transforming entire industries, creating new opportunities and displacing antiquated operating models. Asked to consider the trends that will define tech M&A over the next three years, respondents most frequently cited the rise of industry disruptors and tech industry consolidation, which accrued 19% and 16% of first-choice votes, respectively, and 47% and 48% of top-three votes overall, considerably ahead of other answer options, though interesting differences appear when breaking our respondent pool down by region.

Tech M&A continues to be an over-invested segment of total dealmaking over the long term. With the survey’s findings in mind and evaluating what lies ahead, we offer the following takeaways that may help investors assess their priorities as they look to the future.

“We expected the interest rates to decrease by now,” admits a U.S.-based senior vice president of corporate development and M&A. “The stages in the economic cycle are quite unpredictable, and it is affecting dealmaking conditions. We cannot find the required value through dealmaking as per our initial expectations.”

Nevertheless, it is the cumulative effect of these headwinds, and not a lack of appetite for tech deals, that has throttled tech M&A. As these issues are resolved, dealmaking will recover, as the survey shows. In the interim, buyers must take even more care than usual in their target selection and due diligence, as well as consider creative deal structures that can help circumvent the hardships posed by tighter economic conditions.
Key Takeaways:

1. Although generative AI may be claiming all the headlines, our survey participants believe the cybersecurity space offers even better M&A opportunities in the near term. In light of pervasive digitalization, rapidly changing IT infrastructures, and strict data protection requirements—in addition to, on the policy side, always-rising concerns about national security and cyber warfare—bidding wars in the cybersecurity subsector will inevitably break out.

2. Amid mounting geopolitical tensions and competition over essential tech equipment resources, organizations may find themselves targeting assets on an increasingly short list of amenable countries, echoing the broader trend toward near-shoring and “friend-shoring” in how supply chains are managed around the world.

3. With markets being so volatile and interest rates still rising at the time of our report, financing is currently much harder to come by. In response, dealmakers are mitigating risk by partnering up on investments, as our respondents’ partiality for club deals and joint ventures makes clear. While transformational transactions remain on ice, strategic bolt-on deals will help sophisticated dealmakers separate their organizations from the pack.

4. Today, every company is a tech company, with organizations across industries, market segments, and global regions capitalizing on advancements in tech to gain an edge on the competition. Generative AI has burst onto the tech scene and captured the imagination of corporates and PE investors alike. As generative AI startups mature, we are likely to see M&A activity rise in this subsector.

5. Robust ESG credentials are no longer just “nice to have”; they have become an essential component of dealmaking the world over and are expected to continue to grow in significance over the coming years, especially as regulatory demands increase. Performing thorough ESG due diligence, and being prepared to abandon a deal if a target doesn’t meet increasingly high standards for sustainability and other governance attributes, will be prioritized.
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