The Intelligize M&A Report: M&A Went MIA in 2022

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A deteriorating environment for mergers and acquisitions sent dealmaking activity toppling downward in 2022, an Intelligize analysis of filings with the Securities and Exchange Commission reveals. The number of M&A deals announced by SEC registrants in 2022 fell by 26.5% from the previous year. As inked deals went down, the number of terminated M&A deals shot upward, nearly doubling year-over-year in 2022.

The message from this Intelligize data is unmistakable: corporate dealmaking got harder in 2022.

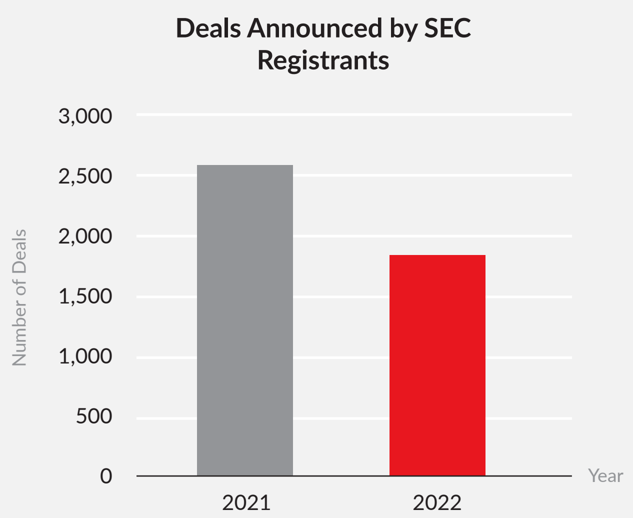
To gain a deeper understanding of the forces affecting M&A activity, we used the Intelligize platform to research companies' deal-related SEC disclosures and analyzed material from the Department of Justice, Federal Trade Commission, and SEC. In addition to studying year-over-year trends in transactions, we drilled down to study data on special purpose acquisition companies (SPACs) — including so-called de-SPAC transactions, proposals for the extension of SPAC termination dates, liquidations and IPOs.

The analysis identified a series of factors that choked the pipeline for deals in 2022, including tightening in the equity and credit markets, geopolitical tensions, a gloomy economic outlook, and increased regulatory scrutiny. Meanwhile, a review of more than 700 comments in letters from the SEC to companies over the course of a year offered insights into some of the agency's most important areas of concern regarding pending M&A transactions.

All of this Intelligize research informs our first-ever M&A report. It isn't just an exercise in looking back, either; the factors that slowed the M&A market in 2022 appear likely to have a lingering effect on dealmaking in 2023.

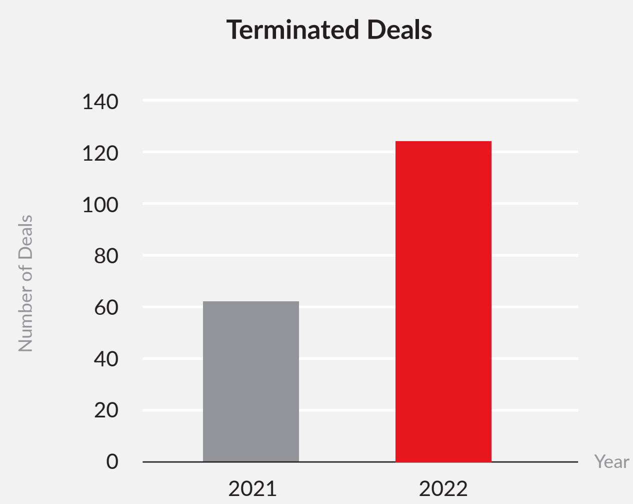
Changes in 2022

M&A activity dropped significantly in 2022 from the previous year, based on a search of SEC filings using the Intelligize platform. The drop represented a decline of 26.5%.



Data based on companies' SEC filings

Additionally, the number of terminated deals nearly doubled from 2021 to 2022.



Data based on companies' SEC filings

Case Study: NVIDIA and Arm Limited

Among the deals scuttled in 2022 was what would have been the largest semiconductor chip deal in history. That acquisition fell apart after regulatory opposition—a common factor, as we'll see, among potential M&A deals that were terminated or delayed in 2022.

The deal, announced in September 2020, would have brought together Silicon Valley-based NVIDIA Corp. with Arm Limited, a jewel in the crown of SoftBank Group Corp. Both NVIDIA and Arm are towering presences in the semiconductor industry: NVIDIA, the acquirer, as a major chip supplier, and Arm, the target, as a company that develops and licenses CPU designs to other companies. The deal had a price tag fit for the companies' profiles: $40 billion.

Yet in December 2021, the FTC filed a lawsuit to halt the deal. The FTC's complaint alleged that "the transaction is likely to substantially lessen competition in relevant antitrust markets" including markets for "Arm-Based Datacenter CPUs for Cloud Computing Service Providers."

NVIDIA announced in February 2022 that the Arm Limited deal was dead. In NVIDIA's 10-K filed in February 2023, the company said it reached an agreement with SoftBank to terminate the sale as a result of regulatory objection, with the termination costing the company $1.35 billion.

> In February 2022, NVIDIA and SoftBank Group Corp., or SoftBank, announced the termination of the Share Purchase Agreement whereby NVIDIA would have acquired Arm Limited, or Arm, from SoftBank. **The parties agreed to terminate because of significant regulatory challenges preventing the completion of the transaction. We recorded an acquisition termination cost of $1.35 billion in fiscal year 2023 reflecting the write-off of the prepayment provided at signing.**

Case Study: Lockheed Martin and Aerojet

A proposed deal involving Lockheed Martin Corp. dissolved in similar fashion.

Lockheed, the world's largest defense contractor, had agreed in December 2020 to buy Aerojet Rocketdyne Holdings Inc. for $4.4 billion. As the FTC would later emphasize, Aerojet has a unique status in the defense industry: it is the "last independent supplier of key missile inputs" in the U.S. It wasn't hard to imagine Lockheed using its hold on Aerojet to the detriment of rivals—or at least not hard for the FTC.

Thirteen months after the deal's announcement, the FTC sued to block the acquisition, with the FTC Bureau of Competition Director stating that the United States "cannot afford to allow further concentration in markets critical to our national security and defense."

In February 2022, Lockheed Martin opted against defending the deal and terminated the agreement. According to an 8-K filing by Aerojet:

> On February 13, 2022, Lockheed Martin Corporation ("Lockheed") delivered notice of termination of the Agreement and Plan of Merger (the "Merger Agreement"), dated December 20, 2020, by and among Aerojet Rocketdyne Holdings, Inc. (the "Company"), Lockheed and Mizar Sub, Inc. ("Merger Sub"), pursuant to which Merger Sub would have merged with and into the Company, with the Company being the surviving entity and a wholly-owned subsidiary of Lockheed (the "Merger").
>
> Consummation of the Merger was subject to various customary closing conditions, including regulatory approval under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, and the absence of any legal restraint making illegal or preventing the consummation of the Merger.
>
> As previously disclosed, on January 25, 2022, the Federal Trade Commission (the "FTC") filed a lawsuit (the "FTC Lawsuit") to enjoin the Merger and sought a preliminary injunction in U.S. federal court to prevent the parties from closing. **The Merger Agreement provided that Lockheed could elect to defend against the FTC Lawsuit within 30 days or terminate the Merger Agreement. On February 13, 2022, Lockheed notified the Company that it had elected to terminate the Merger Agreement.**

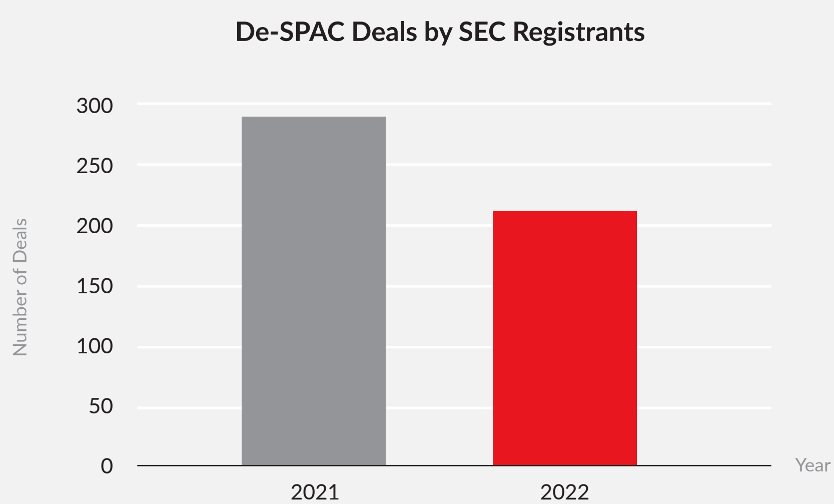
Lockheed Martin added further context to the collapse of the deal in commentary included in its FY2022 10-K filed in January 2023, noting a pattern among regulatory agencies:

> U.S. regulators have increased their scrutiny of mergers and acquisitions in recent years, which could continue to limit our ability to execute certain transactions that we might otherwise pursue, such as the termination of our proposed acquisition of Aerojet Rocketdyne in 2022.

The statement suggests that antitrust regulators' aggressive posture did not just stop the Aerojet deal but will continue to be a concern for Lockheed in other tie-ups going forward.

SPAC Deals Fall Off

SEC filings data illuminates the pressures weighing on beleaguered special purpose acquisition companies. While SPACs were once the hottest vehicle on Wall Street, deal volume fell 28% year over year in 2022.



Data based on companies' SEC filings

Case Study: Pershing Square Tontine Holdings, Ltd.

The disintegration of the ballyhooed SPAC Pershing Square Tontine Holdings, Ltd. (PSTH), led by billionaire hedge fund manager Bill Ackman, illustrates the sector's ongoing problems. In 2022, two years after a fanfare-rich launch, PSTH liquidated.

SPACs, of course, are "blank check companies" typically formed with the goal of consummating a business combination. PSTH raked in a whopping $4 billion through its IPO in July 2020—a record for a SPAC. However, in a twist on the typical SPAC business combination, PSTH earmarked its capital to take only a 10% stake in its target, Universal Music Group, a subsidiary of Vivendi S.E., entering into an agreement with Vivendi in June 2021.

After the Universal deal fell apart about one month later, PSTH continued scouring the marketplace for attractive acquisition targets but in July 2022, the SPAC decided to fold. In its July 2022 8-K filing, PSTH submitted a letter by CEO Bill Ackman to shareholders, twice pointing to the SEC as a significant reason for the SPAC's demise. He noted that SEC concerns dashed the original Universal Music Group deal, and also that new proposed SPAC rules put forward by the SEC in March 2022 made the search for alternative investment targets difficult:

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> Despite these unfavorable market conditions for PSTH, we were fortunate in quickly identifying and engaging with a highly attractive target, Universal Music Group, that met all of our investment criteria. The circumstances of UMG's public listing and the requirements of the company's controlling shareholder, Vivendi, made PSTH an ideal transaction partner, as our scale, structure, and sponsorship addressed our counterparties' unique requirements.
>
> **Unfortunately, Vivendi's structural and legal requirements dictated a transaction structure that was somewhat unconventional for SPACs, and ultimately, one that could not be consummated given concerns raised by the SEC.** As a result, the board terminated the transaction and assigned its obligation to acquire UMG to the Pershing Square Funds. The Funds in turn assumed the UMG transaction costs and the related Vivendi indemnity obligations so that PSTH would be returned to its original position to enable it to immediately pursue a new transaction, albeit with one year remaining to do a deal. We thereafter immediately went back to work to find a replacement transaction.
>
> We have been unsuccessful in consummating a deal over the last year largely due to the adverse market for SPAC merger transactions which has been driven by: (1) the extremely poor performance of SPACs that have completed deals during the last two years which has damaged market perceptions of going public by merging with a SPAC, (2) the high redemption rates of SPACs which has reduced the capital available for the newly merged company, increased the dilution from the shareholder warrants that remain outstanding, and heightened transaction uncertainty, and (3) risk and uncertainty created by the Investment Company Act litigation brought against PSTH, particularly when coupled with **new SPAC rules proposed by the SEC on March 30, 2022.**

No single SPAC tells the whole story of the SPAC landscape, but PSTH feels like something of an avatar. It formed as the SPAC trend was accelerating in 2020, and the energy around it may have helped fuel the record number of SPAC IPOs that occurred in 2021. PSTH's 2022 liquidation, likewise, reflects the decline in SPAC IPOs that occurred that year.

A Look at Factors Affecting M&A Activity

2021: A Downturn Signaled

To be sure, developments in 2021 suggested a rockier road ahead for the M&A market.

Namely, regulatory scrutiny of SPACs began to tighten. In April 2021, the SEC issued its "Staff Statement on Accounting and Reporting Considerations for Warrants Issued by Special Purpose Acquisition Companies." The SEC stated that, for some fact patterns, SPAC warrants should be classified as a liability.

A significant number of SPACs consequently had to restate their financial statements to account for the change in classification.

Enforcement stiffened along with the guidance, and one particular case in July 2021 pointed to the SEC taking a stronger enforcement stance against SPACs. In relation to the proposed merger of Stable Road Acquisition Company (a SPAC) and Momentus Inc., the commission brought charges against the SPAC and other entities, including the merger target, Momentus Inc.

The SEC stated that the case concerned "materially false statements, omissions, and other deceptive conduct by Momentus, a privately held space company that aspires to provide space infrastructure services . . . as it sought to go public through a business combination with Stable Road Acquisition Corp. ('SRAC'), a publicly traded special-purpose acquisition company."

Notably, regarding a test by Momentus of its water based propulsion technology, the SEC stated that "by characterizing the mission as a 'success' without explaining that the mission did not meet any of Momentus's pre-launch evaluation criteria, Momentus made false statements and omitted facts necessary to make their statements not misleading."

The enforcement action didn't stop the merger from eventually going through, but Momentus noted in its 10-K filed in March 2023 that it did cost the company millions of dollars in penalties:

> On July 13, 2021, the Company agreed to a settlement with the SEC on a "neither admit nor deny" basis, in anticipation of cease-and-desist proceedings relating to certain violations of antifraud provisions of the federal securities laws alleged by the SEC. As a result of the settlement, the Company agreed to a civil penalty of $7.0 million, $2.0 million of which was paid immediately and $5.0 million which was paid on July 8, 2022.

2022: Reality Sets In

In 2022, the global financial picture joined regulatory action as a further drag on dealmaking. SEC filings suggest four factors depressed M&A activity throughout the year: (i) challenges in obtaining attractive financing; (ii) growing geopolitical uncertainty; (iii) a negative economic outlook; and (iv) increased regulatory scrutiny.

Challenges in Obtaining Attractive Financing: Equity and Credit Markets

High inflation persisted throughout the year, topping 9% at one point in June 2022. As a result, acquiring debt at favorable terms became increasingly difficult. Private equity giant The Carlyle Group Inc. could have been speaking for all companies when it summed up the state of the equity and credit markets in its FY2022 10-K filed in February 2023:

> The availability and cost of financing for significant acquisition and disposition transactions could be impacted if equity and credit markets experience heightened volatility. For example, in the United States, equity market volatility persisted throughout 2022, as relentlessly high inflation readings motivated the U.S. Federal Reserve to aggressively increase short-term interest rates. Over the twelve months ending December 31, 2022, 10-year Treasury yields rose 235 basis points (bps) and high yield credit spreads widened by 265 bps and obtaining financing in both the high yield bond market and the leveraged loan market is currently challenging. **If credit markets weaken further in the future, it is possible that we and our investment funds may not be able to consummate significant acquisition and disposition transactions on acceptable terms or at all if we or our funds are unable to finance these types of transactions on attractive terms or if the counterparty to the transaction is unable to secure suitable financing.**

Growing Geopolitical Uncertainty

The Carlyle Group's annual report also offered timely commentary on rising geopolitical uncertainty around the world:

> The current U.S. political environment and the resulting uncertainties regarding actual and potential shifts in U.S. foreign investment, trade, taxation, economic, environmental and other policies under the current Administration, as well as the impact of geopolitical tension, such as a deterioration in the bilateral relationship between the U.S. and China or a further escalation in conflict between Russia and Ukraine, could lead to disruption, instability and volatility in the global markets, which may also have an impact on our exit opportunities across negatively impacted sectors or geographies.

Previous Intelligize research has detailed growing apprehension in the corporate world over the impact of Russia's invasion of neighboring Ukraine. As the United States and its European allies continue to aid Ukraine and sanction Russia, the military conflict emerged as one of the top risk factors disclosed by SEC filers during the 12 months ending in February 2023.

Meanwhile, the escalating tensions between the U.S. and China are sending ripples throughout the global economy. The rivals have replaced tough talk with sanctions that directly affect companies themselves. For example, the U.S. Department of Commerce in October of 2022 instituted export controls on advanced computing chips and semiconductor manufacturing items that are crucial to China.

A Negative Economic Outlook

Outlook on the economy began to sour in 2022 as predictions of a forthcoming recession grew louder. Additionally, with inflation spiking, a prolonged period of quantitative easing gave way to interest-rate hikes.

In September 2022, Michael Smolyansky, principal economist at the Board of Governors of the Federal Reserve System, authored a gloomy forecast that fit the broader mood in economic circles:

> Over the past two decades, the corporate profits of stock market listed firms have been substantially boosted by declining interest rate expenses and lower corporate tax rates. This note's key finding is that the reduction in interest and tax expenses is responsible for a full one-third of all profit growth for S&P 500 nonfinancial firms over the prior two-decade period. I argue that the boost to corporate profits from lower interest and tax expenses is unlikely to continue, indicating notably lower profit growth, and thus stock returns, in the future.

Increased Regulatory Scrutiny

Federal regulatory agencies did some notable flexing in 2022, much of which zeroed in on the SPAC sector. In March 2022, the SEC proposed rules "intended to enhance investor protections in initial public offerings by special purpose acquisition companies" and also "in subsequent business combination transactions between SPACs and private operating companies." The package included measures "that would deem any business combination transaction involving a reporting shell company, including a SPAC, to involve a sale of securities to the reporting shell company's shareholders" and rules designed "to amend a number of financial statement requirements applicable to transactions involving shell companies."

Additionally, the Federal Trade Commission and Department of Justice unveiled a joint public inquiry to "better detect and prevent anticompetitive deals." In announcing the effort, the FTC and DOJ suggested industries were growing "more concentrated and less competitive – imperiling choice and economic gains for consumers, workers, entrepreneurs, and small businesses."

The FTC did more saber rattling throughout the year. At a hearing of the Senate Judiciary Subcommittee on Antitrust, Competition Policy and Consumer Rights, FTC Chair Lina Khan highlighted the agency taking "many steps to vigorously enforce the law," with the agency looking at cases through a "broader lens" when considering the effects of proposed mergers.

What did "robust antitrust law enforcement" look like in practice? Some of the biggest brands in video gaming found out when the FTC sought to block Microsoft Corp.'s acquisition of Activision Blizzard Inc., the largest deal ever announced in the video gaming industry.

The companies publicized their $68.7 billion deal—which would also be the largest ever undertaken by Microsoft—in January 2022. In it, Microsoft, maker of the popular Xbox gaming console, would gain control of Activision Blizzard's library of hit games.

In December 2022, the FTC highlighted its opposition to the deal when it announced the issuance of its complaint alleging that the transaction would be illegal. "With control over Activision's blockbuster franchises," the FTC spelled out, "Microsoft would have both the means and motive to harm competition by manipulating Activision's pricing, degrading Activision's game quality or player experience on rival consoles and gaming services, . . . or withholding content from competitors entirely, resulting in harm to consumers."

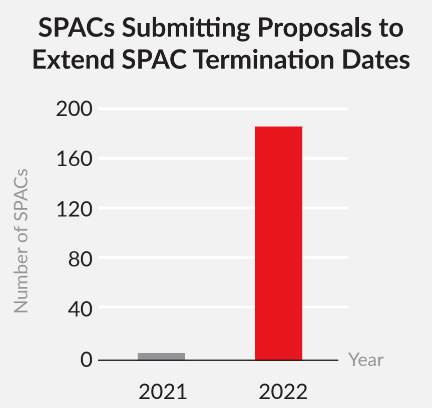
Microsoft's disclosures in its quarterly report filed in January 2023 showed that it still hoped to close its deal with Activision Blizzard:

> The acquisition has been approved by Activision Blizzard's shareholders. We are continuing to engage with regulators reviewing the transaction and are working toward closing it in fiscal year 2023, subject to obtaining required regulatory approvals and satisfaction of other customary closing conditions.

In addition to dealing with opposition from U.S. regulators, Microsoft must also keep an eye on foreign regulators such as Britain's Competition and Markets Authority which on April 26, 2023 announced its decision to block the deal.

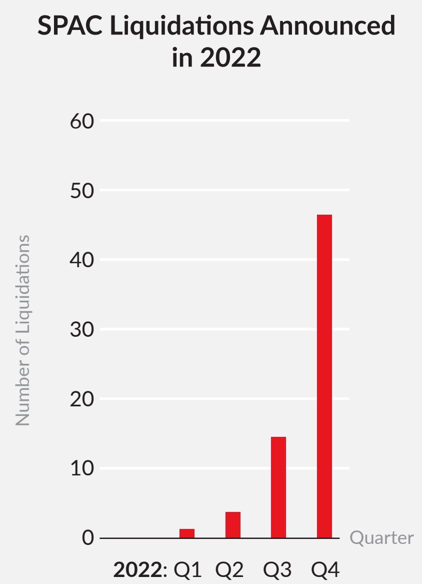
SPACs Need More Time

Many SPACs, unable to close a deal within their initially intended time frame, are asking for more time to find viable acquisition targets. SPAC definitive proxy statements seeking approval from stockholders to extend the date by which they are required to consummate a business combination ballooned in 2022.



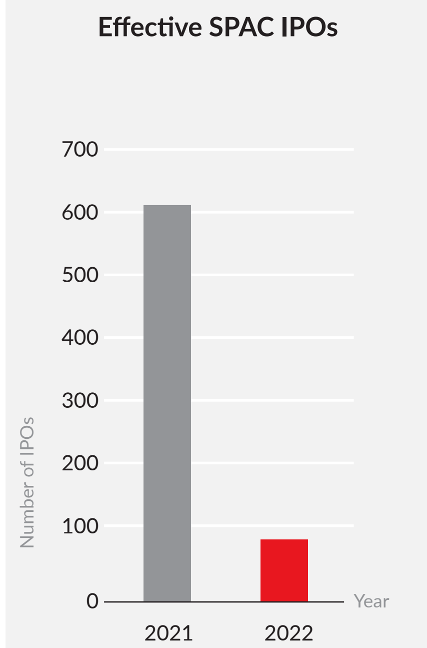
Data based on companies' definitive proxy statements filed with the SEC

Nevertheless, SPAC liquidations grew throughout the year. From the most modest beginnings at the start of the year, liquidations swelled in the final three months.



Data based on companies' SEC filings

As more SPACs folded, the SPAC IPO pipeline dried up.

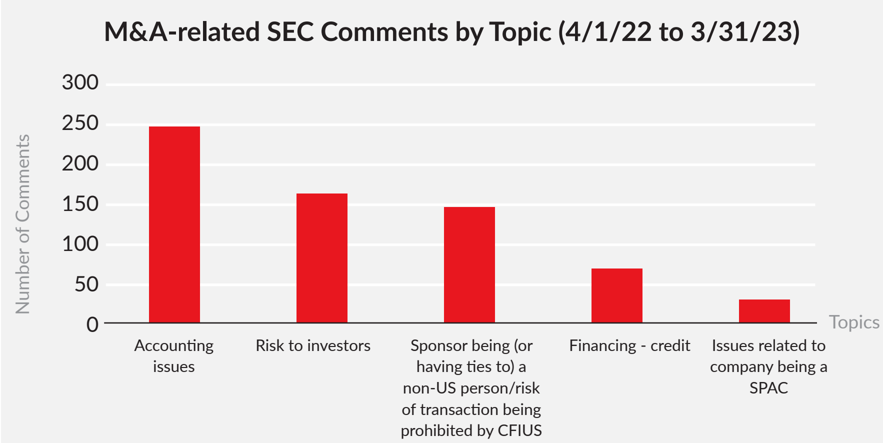


Data based on companies' SEC filings

None of these trends in the SPAC market should ultimately come as a surprise. Aside from sources of financing disappearing, the actions of federal agencies in 2022 made it clear that SPACs would face uphill regulatory battles going forward.

Comment Letter Concerns

What caught the attention of the SEC when it reviewed pending M&A deals? Based on an analysis of 763 comments in letters sent by the SEC to companies for the 12 months ending March 31, 2023, we identified five of the most important topics. The last two of those topics relate directly to the challenges we've discussed above, and others have overlap.



Data based on SEC comment letters

Outlook for the Immediate Future of M&A

Looking back at the M&A trends that defined 2022, we can identify a handful of factors that are continuing to impact dealmaking now and for the foreseeable future. The equity and credit markets remain wary of inflation. The Federal Reserve has maintained its policy of higher interest rates. Likewise, a sense of pessimism about the economy continues to fuel talk of a possible recession.

On an international level, there's no end in sight to the ongoing conflict between Ukraine and Russia that has played a role in snarling the global supply chain. The United States and European nations continue to layer on new sanctions against Russia and its allies as a result. Meanwhile, the U.S. and China are still rattling their sabers at each other, eroding relations between the two nations.

Deal-seeking companies also must keep a watchful eye on news from government agencies. The SEC, DOJ, and FTC have all indicated they will continue to take a vigorous approach to policing dealmaking. In fact, the FTC has already upped the ante for simply attempting to consummate a transaction. Fees for filing premerger notifications and report forms increased this year, with transactions valued at $5 billion or more requiring payment of $2.25 million, up from $280,000 last year.

Moreover, the regulators are seeking more resources from the federal purse. The FTC's budget request for the 2024 fiscal year of $590 million signifies an increase of $160 million over its enacted level for the 2023 fiscal year. The SEC is asking for a raise of more than $200 million in 2024 that would bring its overall funding to more than $2.4 billion. The DOJ requested $324.8 million for its Antitrust Division, an increase of roughly $100 million over the division's enacted level of $225 million for the 2023 fiscal year.

Finally, the market is still processing a recent spate of bank failures. The high-profile failures of Silicon Valley Bank and Signature Bank remain top of mind for the public at large, and some companies have responded to the developments by filing disclosures with the SEC detailing how the fallout from the financial institutions might impact their businesses.

Until we have a clearer picture of the overall damage to the banking system, we can only speculate that the already difficult task of finding M&A financing may get even harder in the year ahead. In the meantime, for those who want to stay on top of M&A developments, the Intelligize platform will continue to collect the most recent SEC filings, comment letters, and relevant regulatory material.

Methodology

The data on M&A activity in this report is based on companies' SEC filings and was gleaned from the Intelligize platform. We analyzed data and M&A related developments up to April 26, 2023.

To analyze M&A deals in 2021-22, we used the Intelligize Mergers & Acquisitions module. We looked at Asset Purchases/Sales, Stock Purchases/Sales, Mergers/Business Combinations, Joint Ventures, and Tender Offers that were over $1 million in value. We reviewed announced deals as well as terminated deals.

To analyze SPAC liquidations and proposals for extension of the SPAC termination dates, we used the Intelligize SEC Filings module.

To analyze SPAC IPOs in 2021-22, we used the Intelligize Registered Offerings module.

To analyze SEC comment letters, we used the Intelligize Comment Letters module. We studied a sample of 763 M&A deal-related comments from SEC comment letters sent to companies in the 12-month period ending March 31, 2023. The comments applied to all deals, including de-SPAC transactions, and were limited to forms S-1, S-4, and 10-K.

About Intelligize

Intelligize is the leading provider of best-in-class content, exclusive news collections, regulatory insights, and powerful analytical tools for compliance and transactional professionals.

Intelligize offers a web-based research platform that ensures law firms, accounting firms, corporations, and other organizations stay compliant with government regulations, build stronger deals and agreements, and deliver value to their shareholders and clients.

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