Franklin Place Capital

Equity markets whipsawed during the second quarter as Covid-19 rocked the global economy. While many markets have returned to their former glory, on the back of an astounding level of government stimulus, the economic implications are likely far from over based on some of the comments made during Q2 earnings reports:

“Our view of the length and severity of the economic downturn has deteriorated considerably from the assumptions used last quarter.” - Charlie Scharf, Wells Fargo

“We are preparing for prolonged economic challenges.” - David Solomon, Goldman Sachs

I don’t think anybody should leave any bank earnings this quarter simply feeling like the worst is behind us.” - Michael Corbat, Citigroup

“Demand growth has largely stalled..”
- Ed Bastian, Delta

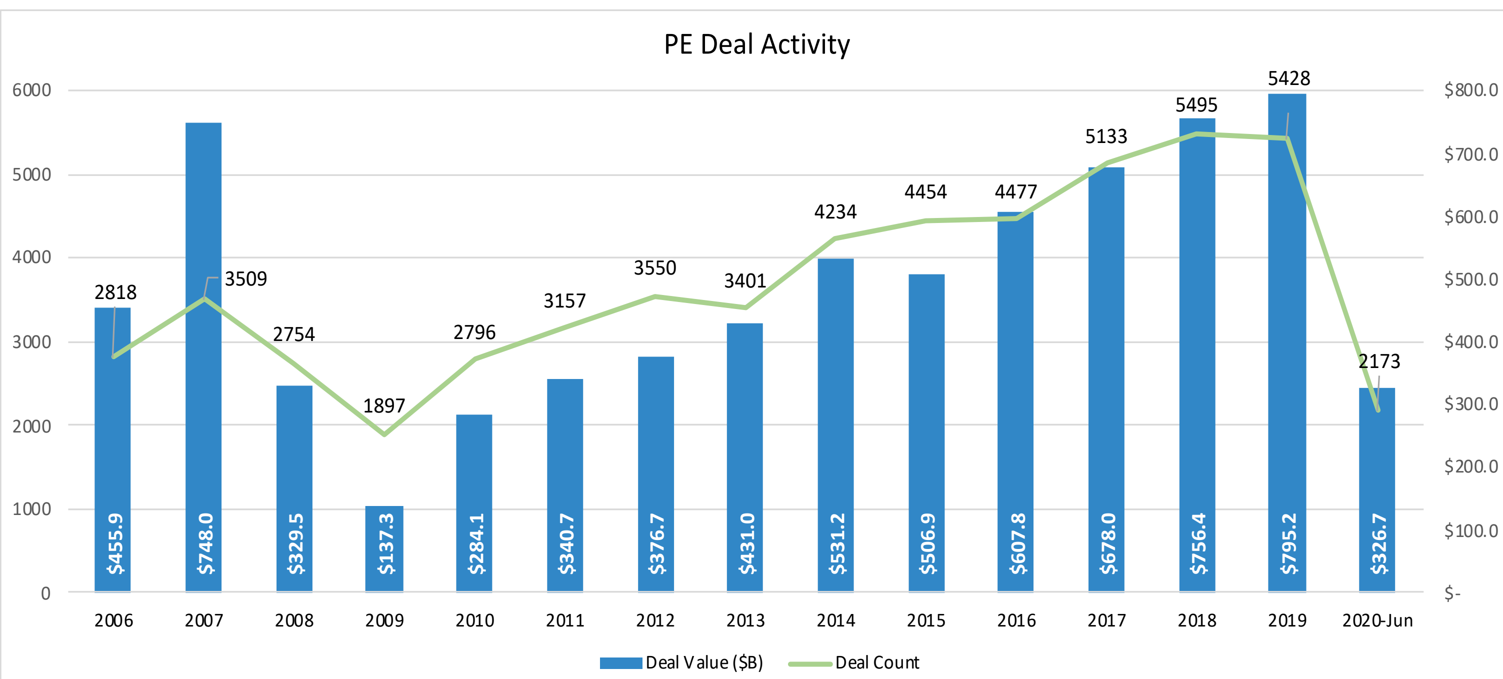
“You will see the effect of this recession, just not right away because of all the stimulus.” - Jamie Dimon, JPMorgan

Q2 2020 M&A Update

U.S. based M&A came to a near standstill during the beginning of the second quarter 2020. After an initial drop, deal activity has resumed albeit at a slower pace. It is estimated that deal activity was off nearly 30% during Q2, with some industries better/worse off. During the quarter it was common to see previously negotiated deals broken, citing the MAC/MAE clause, (material adverse event). In April there were more major lawsuits over MAC clauses than in the previous 10 years. A prime example of this is Sycamore Partners walking away from their $525M acquisition of Victoria’s Secret.

Although supported by programs such as the CARES Act and the Payroll Protection Program, companies with heavy debt burdens have become extremely vulnerable to bankruptcy. May of 2020 reported the highest number of PE-backed bankruptcies since 2016, with more likely on the way. Business forecasting and timing have also become difficult given the amount of economic uncertainty. Active deals are facing longer timelines given remote due diligence and tightening credit standards.

Dry Powder	Available capital remains robust given added government stimulus and recovering equity markets; PE entered 2020 with an estimated $1.5 trillion in dry powder / committed capital.
Private Equity	PE groups remain on the hunt for attractive deals and are willing to be creative (minority/debt position). There are however fewer sell-side opportunities in the market.
Funding & Leverage	A majority of commercial banks and other lending institutions have become increasingly conservative and are slower to jump into new deals, while increasing loan-loss reserves.



Source: Pitchbook
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