2023 TransAct Middle East

Mid-Year Update

All eyes on mid-market M&A to drive strategic transformation and accelerate growth

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Introduction

Despite the global economic slowdown, subdued oil prices and high inflation during the first half of this year, the Middle East continues to be an attractive hub for mergers and acquisitions.

Compared to other regions globally, 2023 began optimistically for the Middle East, with upbeat expectations about regional growth potential and business prospects. A highly motivated leadership across the GCC is the driving force behind the progress of long-term economic visions in the region, including the newly framed goals of moving towards net zero domestic emissions. While growth in the GCC is likely to be moderate for the rest of the year, largely driven by the slowdown in the oil sector, the non-oil sector is expected to remain resilient, further enabling reinvestment in national visions, as reported in PwC's latest Middle East Economy Watch.

This bright outlook was also highlighted earlier in the year in the Middle East findings from the PwC 2023 CEO Survey, that showed 63% of Middle East CEOs to be confident about revenue growth prospects over the next 12 months, and 71% expressed confidence about the outlook for the next three years – albeit tempered by caution.

Cautious optimism, a more selective deal decision making

Amid a post-pandemic boom in the Middle East, bolstered by a strong pursuit of economic diversification initiatives - particularly in technology and infrastructure - the prevailing sentiment for this year has been one of cautious optimism.

Despite facing global macroeconomic uncertainty, reasonable levels of Merger & Acquisition (M&A) activity persisted during the first half of the year (H1-2023), with 186 completed deals in the Middle East. But this signals a 40% decrease in noted deal volumes compared to the same period last year as high interest rates, concerns about a potential recession, and inflationary pressures have culminated into an uncertain environment, further heightened by the downturn in oil prices in the first half of the year.

Consequently, investors were seen to be more selective in deal decision-making, with strategic buyers assessing valuations and potential returns closely, focusing on enhancing their positions in key sectors. That said, M&A-related activity on the ground across the region remains high, even though it may not be reflected in the volume of completed deals during the half-year period under review.

Sovereign Wealth Funds (SWFs) continue to lead deal activity, capitalising on more attractive valuations during global economic uncertainty to support their economic diversification initiatives. Cash-rich corporations are also coming to the fore of transactions, with an enhanced focus on integration synergies and value creation underlying deal motivation. Inorganic growth via acquisitions is commonplace among strategic buyers looking to fast-track market share growth, extract synergies, and access capabilities or talent. This strategy particularly appealed to corporates due to their strong access to cash and synergy extraction abilities. Consequently, corporates accounted for 57% of deal volume in the region, with investments across the financial services, technology, industrial manufacturing, energy, and healthcare sectors.

In terms of deal size, the region has a greater indication towards small (US$100mn or less) and mid-sized deals (US$100mn - US$500mn). These collectively accounted for 52% of disclosed value deals within the half-year period, which is no surprise given the reduced susceptibility of such deals to market fluctuations compared to larger transactions.

When it came to large deals valued at a minimum of US$500mn, the Middle East saw seven of these recorded in H1-2022 alone. Further, no megadeals – with values of at least US$5bn – were registered in the 2023 half-year period, compared to two such deals recorded during the same period last year. This highlights the global macro environment and financing challenges currently marking the deal-making universe – in line with half-year global M&A trends.

The need for transformational change is greater than ever, as businesses are under increased pressure to demonstrate growth and innovation, along with shareholder returns.

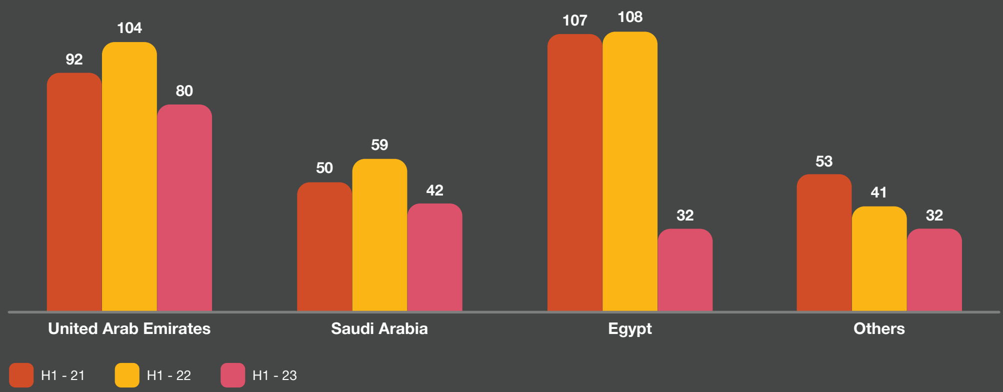
In the current environment, value creation will need to consider a wider transformation agenda that may include changes in operating models, digital transformation and partnerships. Businesses that may not have time to achieve this, internally or organically, can pursue transformational acquisitions to acquire new capabilities. Deals that can support strategic transformations are becoming more relevant in the current market. We expect this to be an ongoing theme in the coming months.

Romil Radia, Deals Markets Leader

Country highlights

Our analysis showed that during the first half of the year, the UAE, Saudi Arabia, and Egypt were at the centre of deal activity in the Middle East. The three countries collectively accounted for 154, or 83% of total deal volume in the region (Figure 1).

Figure 1: Deal Volumes by Country (H1-2021 to H1-2023)



Source: PwC Analysis based on Refinitiv (LSEG) data

In line with global mid-year M&A patterns, these countries experienced a reduction in deal volume compared to H1-2022. The UAE and Saudi Arabia's drop was relatively modest at 23% and 29% respectively, while Egypt witnessed the sharpest decrease of 70% during the same interval – notably with several deals remaining incomplete in 2022 and 2023. The rest of the region also saw a 22% decrease in deal activity, with deal volume falling between H1-2022 and H1-2023.

> **The relative decline in the number of completed deals in KSA in H1-2023 does not reflect a slowdown in the M&A market, but rather a more cautious and balanced investment approach adopted by CEOs and CIOs who are scrutinising value creation opportunities and exit returns more closely before concluding on deals. The announced listings in KSA in H2-2023, alongside the oversubscription of approved IPOs in the past few months, further supports listings as a favourite exit option for selling shareholders.**
>
> **Imad Matar, Transactions Services Leader**

In the UAE, deal activity within industrial manufacturing and financial services persisted from the previous year, while technology-focused deals also gained prominence. A similar trend was seen in Saudi Arabia, with most of the recorded deals concentrated in the technology and industrial manufacturing sectors, while energy deals saw a slowdown. In fact, Saudi's current construction boom has driven a surge in infrastructure-related deals, aimed at supporting its more than US$1tn project pipeline. Moreover, agreements at the recent G20 Summit between Saudi Arabia, the UAE, India and the USA could potentially pave the way for significant multi-country infrastructure deals.

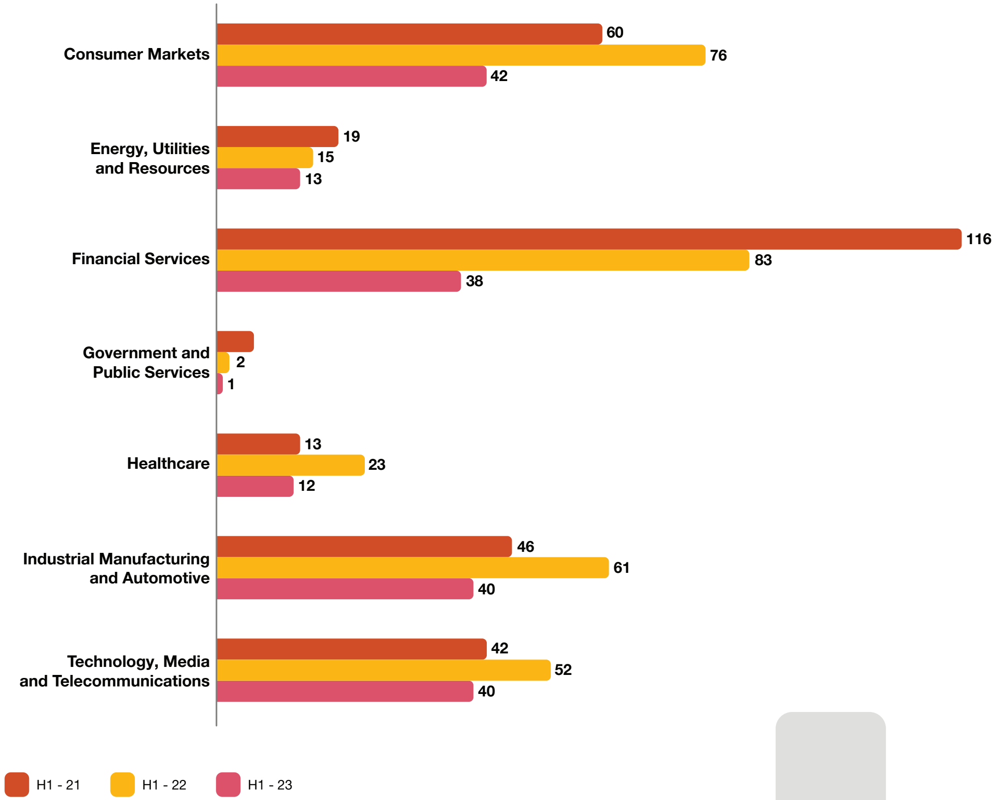
> **The UAE continues to dominate M&A activities in the region, thanks to progressive government policies and efforts to boost the ease of doing business. Despite the slower start to deal-making in 2023, the UAE remained the favoured investment destination for the first half of the year in the region with 80 deals, thereby accounting for a significant part of the GCC's total deal values and volumes.**
>
> **Zubin Chiba, Corporate Finance Leader**

Meanwhile, Egypt's sector diversification initiative, which started in 2023, continues at pace, with deals covering the technology, consumer markets, healthcare, financial services, and energy sectors. Its privatisation drive in the second quarter – a trend exacerbated by the devaluation of the Egyptian pound – is poised to see the sale of stakes in 32 state-owned enterprises valued at US$1.9bn. The pharmaceutical sector particularly appeals to foreign investors, owing to Egypt's industry prominence and government-led modernisation initiatives. In addition, the country's strategic focus on renewable energy, particularly solar power and green hydrogen, positions it as a burgeoning hub for such projects.

[1] https://www.reuters.com/world/africa/egypt-has-contracts-sell-19-bln-worth-state-assets-pm-2023-07-11/

Sector highlights

Figure 2: Middle East Deal Volumes by Sector (H1-2021 to H1-2023)



Source: PwC Analysis based on Refinitiv (LSEG) data

Technology, media and telecommunication

Technology continues to underlie deal activity across all major sectors in the Middle East, such as retail and consumer markets, e-commerce, payments, healthcare, and industrial manufacturing. This has also been bolstered by the sector's relatively buyer-friendly valuation environment, which has been a significant draw to local and international corporates seeking to expand their technology operations. Deal activity has cut across all company sizes – from start-ups to conglomerates – with fintech and e-commerce poised to emerge as stand-out growth sectors in upcoming months.

Consumer markets

E-commerce is a growth catalyst in the region's consumer sector and is driving retail deal activity to improve affordability, digital interaction, and sustainability. As the trend of multichannel shopping, particularly among cost-conscious consumers, gains momentum, retail firms have opportunities to increasingly adopt a 'phygital model' that integrates physical stores, online ordering, shipping services, quick-commerce options, rapid delivery, and in-store promotions to meet the diverse demands of their customer base effectively. Notable acquisitions that illustrate this include UAE e-commerce company Noon D Holdings' US$335.2mn acquisition of online fashion retailer Namshi General Trading LLC.

In June this year, UAE-based Instashop, an on-demand delivery and e-commerce platform serving a diverse array of businesses in the Middle East, announced its acquisition of GroCart, a wholesale marketplace service that streamlines retail supply logistics for retailers in the fast-moving consumer goods (FMCG) space.

Energy, utilities and resources

Despite the impact of falling oil prices noted at the beginning of the year on deal momentum, the energy, utilities and resources sector continues to see some activity, focusing mainly on green and renewable energy investments. The UAE leads the charge in this endeavour, with Abu Dhabi National Oil Company For Distribution PJSC (ADNOC) completing a 50% acquisition of Egypt's TotalEnergies Marketing LLC.

Abu Dhabi National Energy Company (TAQA) has also secured a 5% ownership stake in ADNOC Gas Plc in a transaction aimed at strengthening renewable energy initiatives and ensuring innovative, eco-friendly solutions.

Financial services

The Middle Eastern financial services sector has seen greater consolidation among financial services firms and entities in other sectors looking to expand their capacities or benefit from synergies. For example, UAE-based Etisalat Digital has acquired a majority interest in the peer-to-peer financing platform Beehive in a US$35mn transaction, allowing the technology conglomerate to delve into the SME lending sector.

Meanwhile, surging investor interest in transformative fintech drives cross-border M&A activity across the region's financial services sector. For example, Abu Dhabi's Chimera LLC completed a US$200mn deal for a 20% stake in the Egyptian fintech company MNT- Halan, which offers loans, consumer financing, and e-commerce solutions to low-income Egyptian banks. Bahrain has particularly gained prominence in this context, with the Central Bank of Bahrain's endeavours to scale local and regional fintech growth adding to this dynamic. This rapidly positions the country as the likely target for outbound fintech deals in the upcoming months.

Industrial manufacturing and automotive

As countries in the Middle East double down on economic diversification initiatives, industrial manufacturing continues to play a pivotal role – bolstered by technology. Saudi Arabia's Military Industries (SAMI) for instance, aims to localise 50% of the Kingdom's defence spending by 2030 through acquisitions and joint venture partnerships with local equipment manufacturers. Saudi's Steel Pipe has also expanded its ownership stake in Global Pipe with a substantial investment of US$6.3mn to reach a total ownership of 57.3%. The country's PIF is also planning a 100% acquisition of the Saudi Iron & Steel Company (Hadeed) from Saudi Basic Industries Corporation (SABIC), with Hadeed also acquiring 100% of AlRajhi Steel Industries Company (Rajhi Steel) in a cross-conditional share agreement.

Key themes

Based on our country and sector analysis, the key themes we are witnessing in deal-making across the Middle East in H1-2023 are as follows:

01 Initial deal optimism offset by global macro uncertainties

02 On-ground deal activity remains robust despite declining volume

03 Mid-market deals are the staple of deal-making

04 Business transformation becomes central to deal strategy

05 Outbound deals stay strong as large investors pursue global asset exposure

Key themes

Initial deal optimism offset by global macro uncertainties

Despite its relatively bullish outlook and macroeconomic resilience, the region did not see a corresponding increase in completed deals during the first half of 2023. The devaluation of the Egyptian pound and macroeconomic uncertainty significantly delayed deals in Egypt, a historically large contributor in terms of deal volumes in the region's deal-making, contributing to the decline in deal volume. This was exacerbated by a significant outflow of indirect investments due to global interest rate increases. Additionally, increased investor caution in the fintech and e-commerce sectors, despite being preferred choices, further reduced deal volume in these sectors by 22% and 69% respectively, according to our analysis, impacting overall deal volumes in the region.

On-ground deal activity remains robust despite declining volume

Although deal volumes decreased in the first half of 2023, we note a significant uptick in on-ground deal and IPO-related activity. Nevertheless, many planned transactions remain unrealised, due to various factors including extended closing timelines, especially for sell-side activities, which tend to involve lengthier and more intricate processes. Higher capital and debt costs have also prompted investors to closely focus on assessing how they will generate their required returns.

Mid-market deals are the staple of deal-making

Amid the current economic uncertainty, small and mid-market size deals have gained popularity among deal participants, given that these are less affected by market volatility. Moreover, this prudent approach enables companies to take more measured steps on their transformation journey rather than attempting significant leaps.

Business transformation becomes central to deal strategy

Against the backdrop of remarkable growth within its tech start-up scene, the Middle East is seeing a stronger emphasis on transformational technology and digital acquisitions, aligning with ongoing regional and business transformation initiatives. This surge in activity has been fuelled by the emergence of SWFs as major investors. Persistent digitalisation across many sectors is expected to sustain this momentum due to the SWFs' growing interest along with cash-rich corporates and private equity (PE) firms looking to optimise their portfolio companies' transformation in the current macroeconomic environment. Fintech, renewable energy and healthcare continue to be the dominant targets of such initiatives, spurring investor interest.

Outbound deals stay strong as large investors pursue global asset exposure

While this update looks at deal volume data solely in the context of Middle East targets, it's essential to highlight the significant outbound activity noted in the region in the review period. This is primarily driven by major Middle East investors, such as Portfolio Investment Entities (PIEs) and SWFs, seeking to diversify their risk through increased investments in foreign businesses and assets globally.

Looking ahead

Robust expansions of non-oil sectors in the Middle East have effectively offset the impact of decreased oil revenues, showcasing moderate growth in the second half of 2023 and ensuring a resilient GCC economy.

As seen in the latter part of H2-2022, ongoing efforts to attract increased foreign investments to key economies like Saudi Arabia and the UAE continue to propel capital market dynamics within the Middle East.

The momentum behind technology-related M&A is also expected to persist as businesses increasingly embrace digital transformation-centred strategies. In this evolving landscape, a number of programmes and initiatives have been launched to support tech start-ups within the region, such as the Dubai Chamber of Digital Economy Initiative, the Dubai Centre for Artificial Intelligence's (DCAI) Accelerator Programmes, and Qatar Development Bank's co-investment initiative for start-ups. These have created a thriving ecosystem of technology companies and start-ups, attracting ever-growing interest from foreign investors and further propelling deal and fundraising activity within the technology sector.

In this context, it is worth mentioning that initial public offering (IPO) activity has maintained its momentum into H1-2023 with 22 IPOs generating US$5.3bn, including a mega IPO by UAE's ADNOC Gas PLC that raised US$2.5bn. Top IPOs in the region were driven by the oil and gas, food processing, technology, and pharmaceutical sectors. Similar to the trend in 2022, Saudi Arabia has witnessed the highest number of listings, 17 in total in the first six months of the year. These included Jamjoom Pharmaceuticals' US$336mn IPO, the country's largest IPO on a year-to-date basis, which was oversubscribed 67.2 times.

The upcoming months will likely witness increased capital market activity in the region, supported by a vibrant IPO pipeline, with SAL Saudi Logistics set to sell 30% of its stake through an IPO, and PIF-backed ADES Holdings seeking to raise up to US$1.2bn in what could be the country's largest IPO this year.

[2] https://www.worldbank.org/en/news/press-release/2023/05/17/gcc-economic-growth-expected-to-slow-to-2-5-in-2023

Meanwhile, the trend of cross-border transactions shows no signs of abating, contributing to the emergence of distinguished national and regional champions in different key sectors. Against a backdrop of uncertainty in the geopolitical landscape in the Middle East, there may be some headwinds as investors may adopt a cautious approach.

The priorities, drivers, and commitment to fiscal discipline and sustainability that governments in Saudi Arabia and the UAE have will continue to be of key importance, supporting the deals landscape. There may also be new business opportunities for outbound deals as a result of the growing interaction between South East Asia, China and certain Gulf nations, such as the UAE and Saudi Arabia.

Corporations, such as family offices and other conglomerates, are also expected to discover opportunities to deploy excess capital from non-core asset divestitures. Regardless of the chosen approach, the current landscape is conducive to mid-market deal-making on both an intra-regional and cross-border basis, making the Middle East a bright spot for M&A activities.

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About the data

This edition of our TransAct report covers the H1-2023 period ending June 2023.

Our commentary on M&A trends is based on data from industry-recognised sources. Specifically, deal volumes referenced in this publication are based on officially completed and partially completed deals – excluding pending and announced deals – with data sourced from Refinitiv as of 30 June 2023 and accessed on 13 July 2023.

Data on IPO listings is sourced from S&P Capital IQ. This has been supplemented by additional information from our independent research.

To provide a clearer view of the level of deal activity in the Middle East region, the source data was modified to correspond with PwC's industry mapping, and the target nations were mapped to PwC Taxonomy. Furthermore, industry and geography classifications are based on the target company, and all reported amounts are in US$mn.

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