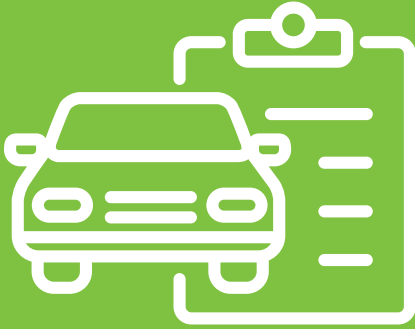




Alternative deal making in automotive

Passport to the future or temporary fix?

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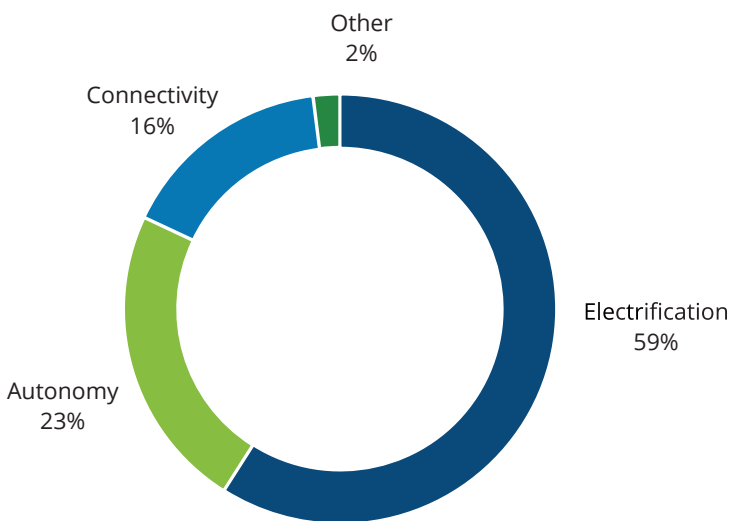


Companies up and down the automotive value chain are increasingly looking to alternative strategies in the form of strategic partnerships, alliances, and joint ventures to address near-term issues, including capability gaps and supply constraints while optimizing capital distribution, particularly in emerging areas such as electrification, autonomous and connected vehicles. At the same time, original equipment manufacturers (OEMs) and suppliers should carefully consider whether to gain capabilities through inorganic acquisitions and partnerships, invest to build them in-house, or forego activities in these emerging areas altogether to focus on legacy products.

Alternative deal-making has taken a more predominant role in the automotive industry compared to traditional merger and acquisition (M&A) activity. Analysis of over 240 transactions completed between April 2018 and February 2022 shows alternative deal-making has outpaced traditional M&A by nearly 3 times¹. In addition, at the height of the pandemic in 2020, traditional automotive M&A activity decreased by 32 percent while alternative deals increased by 11 percent.

Recent study data also suggests that the majority of “modern” alternative deal-making is being driven by a critical need to keep pace with transformative technologies shaping the global automotive industry, including electrification (59% of deals), autonomy (23%), and connectivity (16%)².

Figure 1: Percentage of alternative deals by automotive mega trend



Source: Deloitte analysis.

There are several reasons alternative deal-making strategies have evolved, including speed, certainty, and capital requirements. Alternative deal-making has also provided automakers with an opportunity to acquire capabilities they were lacking such as autonomous and connected vehicle software development. In other cases, car companies have come together to leverage each other's core strengths in order to accelerate research and development (R&D) programs and deploy capital more effectively. Alternative deal-making is helping to address a variety of emerging issues, including limited supply chain visibility and resiliency in critical components.³ In some cases, non-traditional, strategic partnerships can open up new supply opportunities, including startups, for raw materials and components used in electric vehicle (EV) battery production.⁴ Current study results indicate 1 in 5 transactions in the automotive sector involved a startup company.⁵

Alternative M&A strategies are also unlocking significant innovation potential, stimulating the creation of ecosystems to support technology development. These strategies are disrupting existing value chains and redrawing traditional industry boundaries, blurring the lines between the automotive, resources and hi-tech sectors. In fact, some hi-tech incumbents are also following more traditional M&A playbooks to acquire key targets as a way to inject themselves into the global sector transformation.⁶ Alternative deals also have the signaling power to create shareholder value. As an example, legacy automaker partnerships focused on vehicle electrification had a significantly positive impact on their stock prices and associated market valuations in 2021.⁷

However, while alternative deal-making can be a strong enabler in the short term, it should not be mistaken for a permanent solution to develop and maintain a sustainable advantage over the long run. Automakers and suppliers should invest in core capabilities to create a defensible competitive position. For example, as competition in the electric vehicle space intensifies, advantages gained via strategic collaborations and alliances may wane. In addition, alternative deals can often be as complex as traditional M&A transactions, requiring similar levels of diligence, governance, and execution discipline to realize value. Alternative deals may also fall short in providing a permanent resolution for inherent structural imbalances in the market.

Overall, the proliferation of alternative deals will likely continue to disrupt the global automotive value chain. Non-traditional partnerships involving small, agile start-ups, and large mature companies from outside the industry are accelerating the development of key technologies including

electrification and autonomous driving. It should be noted, however, that the number of suitable partners is by no means endless and a number of significant alliances have already been struck, so automakers and suppliers looking to gain an advantage through alternative deal-making should be identifying and vetting potential candidates before the opportunity closes. At the same time, inherently less agile companies risk becoming dis-intermediated from their core customers altogether, obviating the need to develop strategies to ensure they can participate in growth segments going forward.

Here are a few considerations for industry leaders:

- Prior to engaging in an alternative M&A transaction, companies should carefully consider the merits of partnering versus buying or building a solution to address a specific need (i.e., Build-Buy-Partner options), and weigh the advantages and drawbacks of each approach.⁸

- Companies should consider the “end-game” (i.e., how and when does this partnership or alliance end?) and what obligations or rights does an entity need in order to preserve long-term value at that time?



- The viability of alternative deal strategies also depends on industry maturity. When the cost of technologies is high and consumer adoption rates are low, alternative deals are a sensible approach to gain a foothold in the space. However, as the cost and adoption curves begin to invert, a “build” or “buy” approach may be a more viable option.

- It should also be noted that alternative deal strategies may not be mutually exclusive. For example, “build and partner” or “buy and partner” strategies can be pursued simultaneously. Our analysis of transaction data suggests nearly 10 percent of companies striking alternative deals were also involved in traditional M&A activities during the same period.

As the global automotive industry continues to move through a period of tremendous disruption and transformation, the option for companies to take a “wait and see” approach has definitely come and gone. Companies should already be placing their bets on the capital allocations, technologies and strategic partners needed to thrive in an emerging automotive ecosystem that will likely look very different than the one to which they have become accustomed.

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Endnotes

¹Deloitte study, sourcing alternative deals from public announcements in major media outlets, CapIQ, and Bloomberg. M&A Deals sourced from Refinitiv and Mergermarket databases and limited to the deals valued at least \$500M. Period analyzed for both alternative deals and M&A transactions was April 2018 through February 2022.

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