



# A tough environment for deal making

**M&A trends in financial services**

**Q3'22**

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## Introduction

# FS M&A drops again

M&A activity in financial services (FS) fell in Q3'22—the third consecutive quarterly decline. Deal making slowed across the three subsectors of capital markets, banking, and insurance. Compared to Q2, aggregate FS deal volume dropped 26.6 percent to 1,386, and aggregate deal value fell 70.0 percent to \$61 billion.

Year-to-date activity through Q3 weakened versus the same period in 2021. Deal volume totaled 5,360, down 9.9 percent, and deal value declined 24.8 percent to \$462.3 billion.

**Higher inflation, rising rates.** The main reason for the drop in activity was the macroeconomic environment: the impact of higher inflation, rising interest rates, and growing recession expectations. Annualized headline inflation in August was 8.3 percent, down from June's 9.1 percent recent peak but still the highest level in four decades. The Federal Reserve raised the benchmark fed funds rate by 0.75 percent both in July and September, pushing the rate to a range of 3.0 to 3.25 percent.

These headwinds, along with a strengthening U.S. dollar, combined to pull stocks downward and sharply boost companies' cost of capital—two major negatives for deal makers. Our analysis of M&A for fintechs and insurtechs ("Time to acquire fintechs/insurtechs? Yes and no." on page 7) illustrates how weak stock prices and higher rates are hurting activity in a typically deal-intensive sector.

**Looking ahead.** There is cause for pessimism about FS M&A going forward. The KPMG Economics team forecasts that the Fed will hike rates again by 0.75 percent at each of its remaining Federal Open Market Committee meetings in November and December and by another 0.25 percent in early 2023. The result likely will be further declines in equity valuations, higher capital costs, and weaker revenue and earnings growth for many companies—all of which are unfavorable for deal making.

That said, however, the secular trends that have driven FS M&A for much of

the past decade remain solidly in place: consolidation, strategic divestitures, product-line expansion, cost synergies, and the overall quest for growth. We believe activity will continue, albeit at a slower pace.



**Timothy Johnson**

*Partner  
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## Key statistics

**-27%** decline in total FS deal volume in Q3'22 from Q2'22 (1,386 from 1,887)

**-66%** decline in total FS deal value in Q3'22 from Q2'22 (\$69 billion from \$202 billion)

**-25%** decline in YTD total FS deal value in Q3'22 from Q3'21 (\$462.3 billion from \$614.4 billion)

## Timothy Johnson on the near- and medium-term prospects for FS M&A:

The economic environment is unfavorable, yet the secular trends that have been driving deal activity remain intact. We expect activity to continue, albeit at a slower pace.

—Timothy Johnson, Partner

## By the numbers

# Breaking down Q3'22 activity

Here's the breakdown of Q3'22 M&A activity involving the three major financial subsectors we follow:

- There were 1,091 capital markets deals worth \$65.2 billion.
- There were 51 banking deals worth \$2.6 billion.
- The 244 insurance deals were valued at \$1.1 billion.

**Strategic versus private equity.** The number of strategic deals declined 25.7 percent and value dropped 68.1 percent from their levels in Q2. For private equity, the corresponding declines were 32 percent and 56.2 percent, respectively.

Of the quarter's top four transactions, two were strategic and two were private equity. The biggest—the \$14 billion acquisition of real estate investment trust STORE Capital by a Singaporean sovereign wealth fund and a real estate investment firm—was a private equity deal.

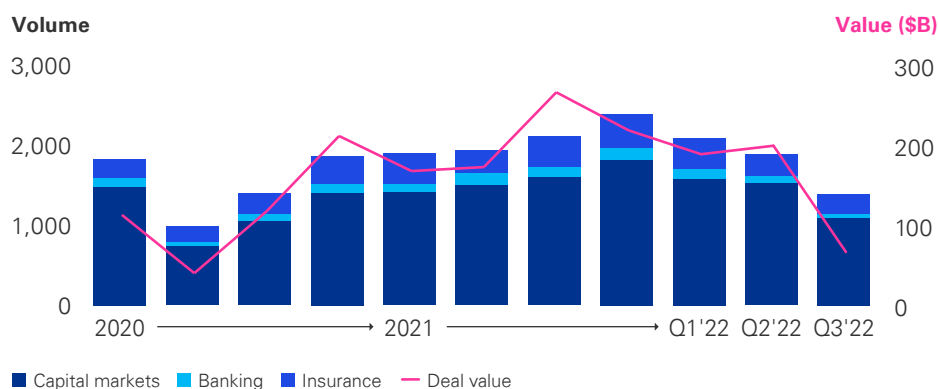
Another notable private equity deal in Q3'22 was Stonepeak Partners' \$2.4 billion acquisition of Intrado's Safety Business. Stonepeak is a private equity firm specializing in infrastructure and real assets, including communications and digital operations—making it a natural buyer for Safety, which provides critical public emergency telecom services.

**Cross-border deals.** Domestic deals accounted for 79.2 percent of FS volume, while 13.3 percent was inbound (i.e., overseas companies buying U.S. targets) and the remaining 7.5 percent was outbound (U.S.-based companies buying overseas targets).

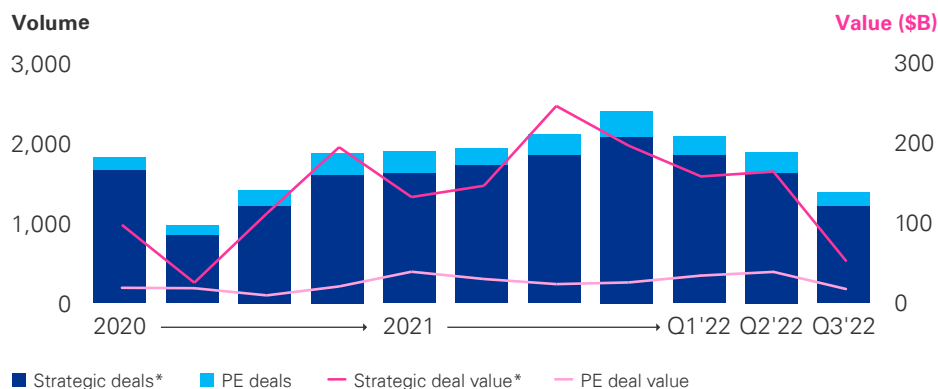
## Top FS deals Q3'22

Acquirer	Target	Value (billions)
GIC, Oak Street Real Estate Capital	STORE Capital	\$14.0
Global Payments	EVO Payments	\$4.0
AFCO Credit Corporation	BankDirect Capital Finance	\$3.4
Stonepeak Partners	Safety Business of Intrado	\$2.4

## U.S. FS activity by sector



## Strategic and PE FS deals



\*Includes SPAC deal volume and value

About the data: Data was sourced from CapitalIQ, Refinitiv, Pitchbook, and KPMG analysis. The values and volumes data cited are for U.S. deals announced during each quarter. Previously published statistics may be restated to incorporate new data and/or changes in deal outcomes.

## By the numbers



Capital markets M&A trends

# Activity slows, consolidation continues

M&A activity involving capital markets firms fell in Q3'22 versus Q2'22. Deal volume declined 28.2 percent to 1,091, and deal value plunged 64.7 percent to \$65.2 billion.

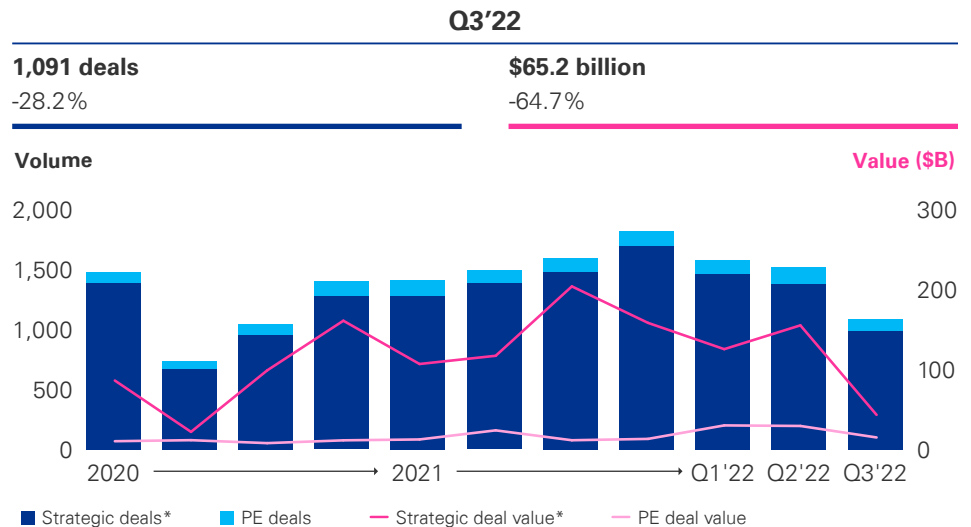
Results for 2022 through Q3 also compared unfavorably with the same period in 2021. Year to date, there were 4,193 deals (down 7.0 percent) worth \$405.3 billion (down 14.8 percent).

**Nine of the top ten.** Capital markets firms continued to account for most of the largest financial services transactions. Nine of Q3's top ten FS deals were in capital markets, slightly down from all of the top ten in Q2. These included Q3's biggest FS deal: the \$14 billion acquisition of STORE Capital, a real estate investment trust.

**Big strategic deals.** Eight capital markets deals during Q3 were valued above \$1 billion. The top strategic deal was Global Payments' \$4.0 billion acquisition of payments competitor EVO Payments. The purchase expanded Global Payments' presence to Poland, Germany, and Chile, while adding to its existing business in the U.S., Canada, Mexico, Spain, Ireland, and the U.K. It also followed the 2021 transaction in which Global Payments bought Zego, a real estate software company, for \$925 million.

Another notable strategic deal was AFCO Credit's \$3.4 billion purchase of BankDirect Capital Finance, a consolidation play. AFCO Credit, which provides insurance premium financing, bought a competitor that BankDirect's parent, Texas Capital Bancshares, divested in line with its focus on core businesses.

## Capital markets deal volume and value



## Top capital markets deals in Q3'22

Acquirer	Target	Value (billions)
GIC, Oak Street Real Estate Capital	STORE Capital	\$14.0
Global Payments	EVO Payments	\$4.0
AFCO Credit Corporation	BankDirect Capital Finance	\$3.4
Stonepeak Partners	Safety Business of Intrado	\$2.4

## By the numbers



Banking M&A trends

# Strategic banking and payments deals continue

Banking M&A fell in Q3'22 for the third consecutive quarter. Compared to Q2, banking deal volume dropped 43.3 percent to 51, and banking deal value plummeted 63.1 percent to \$2.6 billion. Both declines exceeded those for financial services as a whole (26.6 percent and 65.9 percent, respectively).

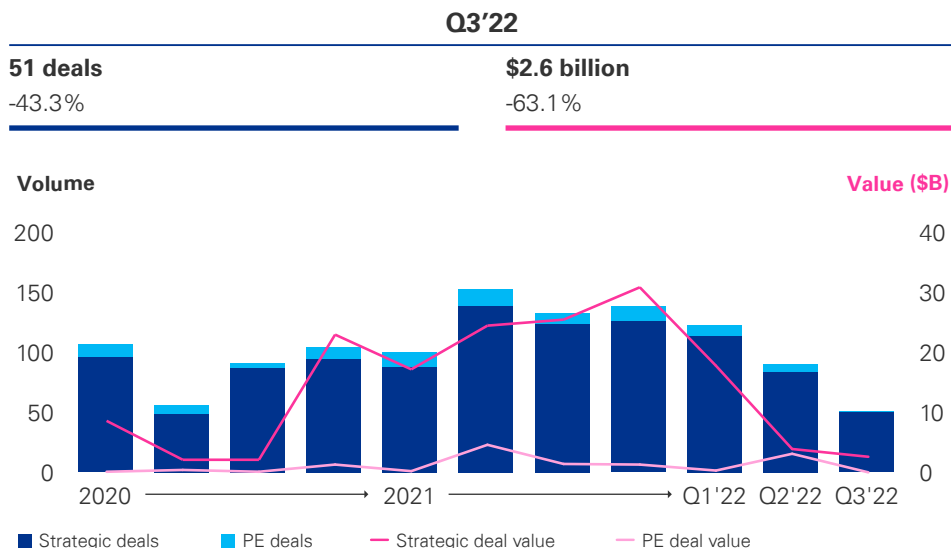
Activity also compared unfavorably for the year-to-date period through Q3'22 versus the same period in 2021. Banking deal volume fell 31.6 percent in 2022's first three quarters to 264, while banking deal value dropped 62.2 percent to \$27.7 billion.

**Consolidation continues.** Despite the weakening marketplace, Q3's largest banking deals underscored the subsector's ongoing trend of strategic consolidation.

The three biggest banking deals—the \$1.3 billion merger of Provident Financial Services and Lakeland Bancorp, Seacoast Banking's \$500 million acquisition of Professional Holding Corp., and the \$200 million purchase of Heritage Southeast Bancorporation by The First Bancshares—focused on regional U.S. banks' quest for growth via geographic expansion.

The Provident-Lakeland merger combined two New Jersey community banks to scale their similar business lines and potentially raise their growth and profitability. The new entity would become one of the state's largest super-community banks.

## Banking deal value and volume



## Top banking deals in Q3'22

Acquirer	Target	Value (billions)
Provident Financial Services	Lakeland Bancorp	\$1.3
Seacoast Banking Corporation of Florida	Professional Holding Corp.	\$0.5
The First Bancshares	Heritage Southeast Bancorporation	\$0.2

Buying Professional Holding enabled Seacoast to extend its South Florida branch network, beef up its balance sheet, and enhance its product line. The Heritage acquisition strengthened

Mississippi-based First Bancshares' presence in Georgia and Florida, and gave First Bancshares entry to the major regional markets of Atlanta and Jacksonville.

## By the numbers



### Insurance M&A trends

# A tough quarter

#### Insurance M&A weakened during Q3'22.

Deal volume versus Q2 fell 11.9 percent to 244, and deal value was relatively faint, shrinking 88.9 percent to \$1.1 billion. While the decline in volume was much less than in the FS sector as a whole, the value drop-off more than tripled the sector's percentage decline.

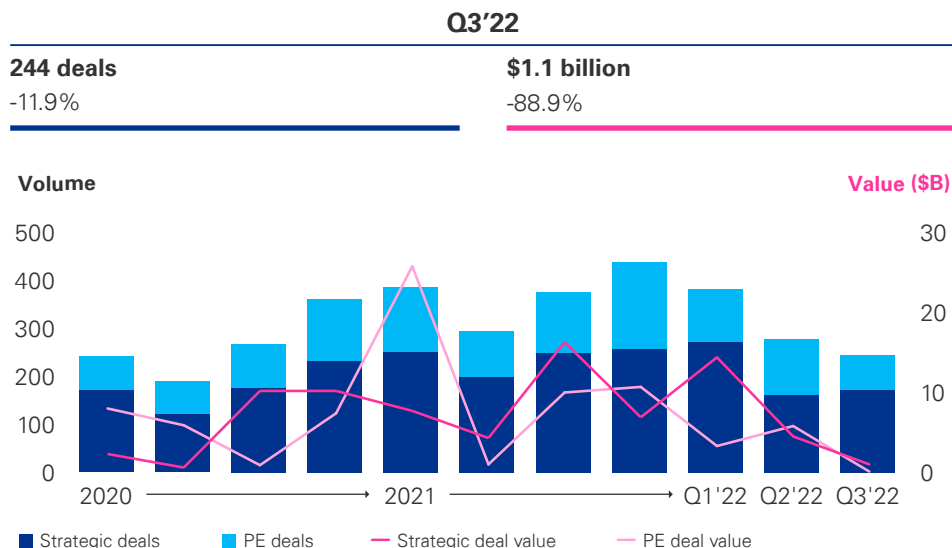
Results also compared poorly for the year-to-date period through Q3. At quarter-end, 2022 insurance M&A volume and value fell 14.5 percent and 55.3 percent, respectively, from 2021 levels. The corresponding declines for overall FS were 9.9 percent and 24.8 percent, respectively.

**A PE and strategic deal.** The biggest insurance deal in Q3 was the \$400 million purchase of Transverse Insurance Group, a hybrid fronting insurance carrier, by Mitsui Sumitomo Insurance. The seller—private equity firm Virgo Investment Group—had built Transverse into a thriving enterprise from scratch.

It was a highly strategic deal for Japan-based Mitsui Sumitomo, which added to its U.S. footprint and diversified its revenues by accessing Transverse's multiple distribution channels for property, casualty, marine, and specialty insurance.

**Looking ahead.** Our outlook for insurance M&A is a mixed picture of caution and optimism. While we expect rising interest rates and the weak economy to dampen enthusiasm for deal making, we also believe that the long-running consolidation trends among carriers and brokers will continue to drive buyers and sellers alike.

## Insurance deal value and volume



## Top insurance deals in Q3'22

Acquirer	Target	Value (billions)
Mitsui Sumitomo Insurance	Transverse Insurance Group	\$0.4
Ohio Farmers Insurance Company	Argo Underwriting Agency	\$0.1





## Time to acquire fintechs/insurtechs? Yes and no.

A drop in valuations suggests fintechs and insurtechs are ripe for acquisition. Acquirers want to buy, but they're being cautious.

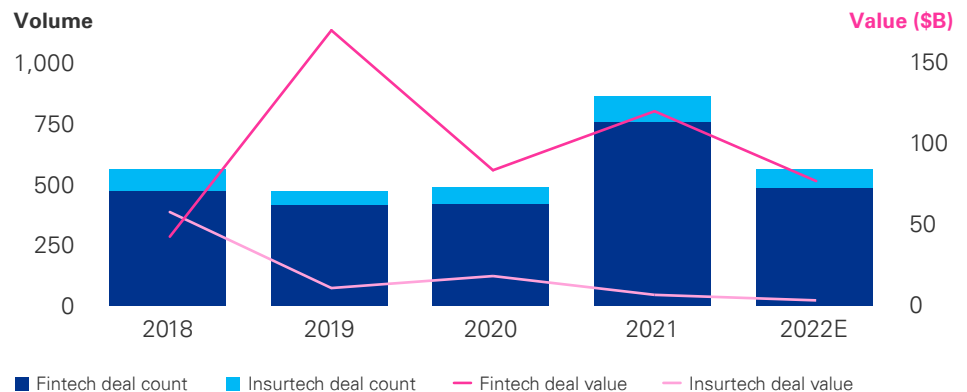
While the weak stock market has pushed valuations down across the board, the decline has been especially dramatic for younger, high-growth technology companies such as fintechs and insurtechs. Worsening economic conditions, moreover, are forcing fintechs and insurtechs to focus on generating cash flow and profits—which most haven't had to do because they have concentrated on growth for its own sake.

The latest investment numbers for fintechs and insurtechs combined—as of the end of Q3'22—reflect a clear drop in enthusiasm. If we extrapolate the year-to-date 2022 data (see chart) to a full year and then compare those figures to 2021, the results are negative: Full-year deal count falls versus 2021 by 13.2 percent to 747, and full-year capital invested sinks 16.0 percent to \$105.6 billion.

The same environment is compelling many financial and strategic acquirers (i.e., private equity firms and corporations, respectively) to be more selective, raising the question: What will fintech/insurtech M&A look like in the near-to-medium term?

**Financial buyers.** PE firms have been active buyers of fintechs and insurtechs, often aggregating them to build larger platforms that could become acquisition targets or acquirers in their own right. But rising interest rates are boosting PEs' cost of capital and making it more expensive

### Investment in fintech and insurtechs is falling



Source: Pitchbook. Data as of September 30, 2022. E = estimate.

for them to do their traditional leveraged deals—and the economic downturn could force them to wait longer for initial public offerings and other desirable exit options to materialize. As a result, PEs are turning down more opportunities, being more methodical than usual with due diligence, and with a greater focus on improvements to the operating performance of portfolio companies.

PE buyers have two major advantages versus corporations in the current market. First, they have a ton of dry powder—\$1.2 trillion as of June 30—that they are contractually obligated to spend, some of it in the next year or two. Second, PEs encourage fintechs' and insurtechs' entrepreneurial business culture, the integration of which can be a significant obstacle for corporate deals.

It's worth mentioning that PE firms with portfolio companies coveted by strategic buyers are in a unique position to sell. While PE owners generally prefer to hold when valuations are down, they might be able to attract relatively high prices from

strategic buyers eager to add potentially high-growth businesses, achieve pricing and operating synergies, or both.

**Strategic buyers.** Lower stock prices weaken corporates' balance sheets and make their shares a less attractive currency for deals. Yet falling valuations have made strategic deals that previously were out of reach more feasible, especially for small/mid-sized tuck-ins which can be acquired with cash. And while rising rates hinder corporates, they also help to level the playing field compared to PE firms. Insurance carriers, for instance, have all-time-high capital levels that allow for deal making even as rates go up.

Ongoing consolidation among banks, insurers, asset managers, and wealth managers could provide an additional edge for strategic acquirers. Bigger players will have greater financial and marketplace muscle both to buy targets and elicit interest from sellers.

<sup>1</sup> Source: "What dry powder levels mean for investors in a changing market," pitchbook.com, August 20, 2022

**Fintechs and insurtechs.** On one hand, many fintechs and insurtechs are unlikely to draw bidders if they can't generate the positive cash flow that buyers require, or at least demonstrate that they're moving in the right direction.

Such companies may find themselves forced to sell or enter partnerships simply to stay in business. On the other, they may choose to stay independent if they have the financial strength to do so. Another possibility is for larger players to exploit the environment and acquire weakened competitors. Global Payments, which recently announced the acquisition of EVO Payments for \$4 billion, is a good example.

**The bottom line.** While we expect financial and strategic buyers to remain cautious about purchasing fintechs and insurtechs, this hardly means that activity will stop. Acquirers still want to add the digital expertise, new or complementary products, advanced technologies, and strong management teams that fintechs and insurtechs can offer. Most would find it easier to buy than build.

Many PE firms, banks, and insurers, furthermore, have positioned themselves to be opportunistic. They are eager to compete for strong assets that will help them achieve their respective goals, and will move prudently and systematically to get deals done.



**Michael Bradshaw**

*Principal  
FS Advisory*

## Michael Bradshaw on private equity acquisitions of fintechs and insurtechs:

PE firms have ample dry powder to spend, but rising interest rates are raising their cost of capital. We expect them to compete for strong assets even as they become more selective about pursuing targets.

— Michael Bradshaw, Principal





## Outlook

# A time for caution and opportunism

We believe macroeconomic conditions will be the primary determinant of financial services M&A activity in Q4'22 and extending into 2023. Our conclusion is that FS companies generally will exercise caution about doing deals, while those with healthy balance sheets and strong competitive positioning will be opportunistic at a time when many potential targets are vulnerable.

**Recession is likely.** KPMG Economics forecasts that the U.S. economy will enter recession in Q4'22 and persist for the first half of 2023. The nonmonetary factors that have combined to cause this year's downturn—supply chain issues, war in Ukraine, soaring energy and commodity prices, shortages of key components such as semiconductors and economic slowdown in the U.K. and Europe—are unlikely to reverse course soon.

**The Fed remains aggressive.** The Federal Reserve has set its sights squarely on braking the economy to decelerate the pace of inflation. According to KPMG Economics, the Fed is poised to raise its fed funds rate 1.5 percentage points by year-end after hiking the rate by three percentage points year to date through Q3. More tightening could happen in Q1'23, which could bring fed funds to a range of 4.75–5.25 percent—essentially double the 2.5 percent level for the prior business cycle of 2009–2020.

**A strong dollar doesn't help.** The U.S. dollar has significantly strengthened this year versus most other leading currencies, notably the euro and pound sterling. While this might prompt U.S. companies to go on an overseas shopping spree, it also means that many non-U.S.

## Key considerations as we look ahead

We suggest three strategies for deal makers to consider in today's uncertain business environment:

- 1 Be proactive about M&A.** Start identifying potential M&A pipeline targets that could be a sensible tuck-in, have an attractive valuation, and/or might be open to a non-auction sale directly with a strategic buyer rather than PE. Start hunting and do your work where you want to target. The cycle evolves, so there will be opportunities both at the bottom and when the market starts to open up again.
- 2 Digital transformation.** Banks and insurers have been slow to digitize their businesses. Great progress has occurred, but many still have much farther to go (automation cost savings would be valued in the current market). Those that successfully transform will sit in the M&A driver's seat, while those that don't might not be targets for acquisition.
- 3 Due diligence.** We cannot emphasize enough the importance of thorough, well-planned due diligence. It is vital to accurately appraise a target's capabilities and competitive positioning, and confirm your deal theses: Doing so can help you understand which future scenarios lead to growth and profits versus red ink. It is also vital to conduct regulatory diligence to avoid red flags given the Biden Administration's intention to closely examine deals in all industries.

targets are having trouble growing revenues and margins—and are less appealing to potential acquirers.

**Corporate rollovers could hurt.** KPMG Economics points to corporate rollovers of maturing debt as an under-the-radar factor that could hurt growth and profitability. The yield on the 10-year U.S. Treasury note—which serves as the benchmark for most corporate and consumer loans—has more than doubled in 2022, from 1.52 percent to 3.83 percent at September 30. As companies roll over their debt, their cost of debt service will be much higher accordingly. And as borrowing becomes more expensive, many companies could be forced to make deep cuts to inventories and other items in order to afford their debt.

### Action steps to take now:

While one might expect the tough economic environment to be uniformly negative among financial subsectors, it isn't—and companies that are well prepared could benefit in the short term while positioning themselves for stronger growth in the future.

Here's what KPMG specialists think about what companies in key financial subsectors should do:

- Asset managers face the double whammy of declining assets under management as markets fall combined with an increasing cost of capital as interest rates rise. What's more, a downturn likely will reduce investor inflows and exacerbate existing pressure to cut fees. To fight back, asset managers should redouble their efforts to slash costs, add scale through complementary acquisitions, or consider joining forces with a competitor.
- Rising rates generally help banks by enabling them to charge more for loans and attract more deposits via higher-yielding savings accounts. But these benefits are offset by slower economic activity and less demand both for consumer loans and corporate financings. Banks should cut costs, reduce credit risk, and divest noncompetitive businesses. Those with strong balance sheets have an opportunity to make strategic acquisitions—notably of fintechs—at beaten-down valuations.

- In the near term, volatility in financial markets should help capital markets firms in the form of higher trading volumes. Underwriting of corporate debt, furthermore, tends to increase as companies seek to lock in current rates in anticipation of tightening by the Fed. Extraction of costs should be a priority for capital markets firms: Leaner players should not only see wider profit margins, but also become stronger acquirers or more attractive acquisition targets.
- The good news for insurers is that rising interest rates allow them to invest premium inflows at higher yields, and that the industry has significantly improved its risk profile in the past decade. The bad news, though, is that higher inflation and increasingly harsh weather events will force them to pay claims that are both larger and more numerous. M&A offers insurers an opportunity to optimize their portfolios and most effectively deploy their capital. Whether deals are offensive (e.g., buying businesses that can boost growth) or defensive (e.g., selling units that are unprofitable or have low growth prospects), insurers can use M&A to their advantage in a weak economy.

## Ram Menon on action steps that financial services companies should take now:

Cutting costs is vital for everyone. If possible, use M&A as an opportunity to make additive acquisitions or divest noncompetitive businesses.”

— Ram Menon, Partner



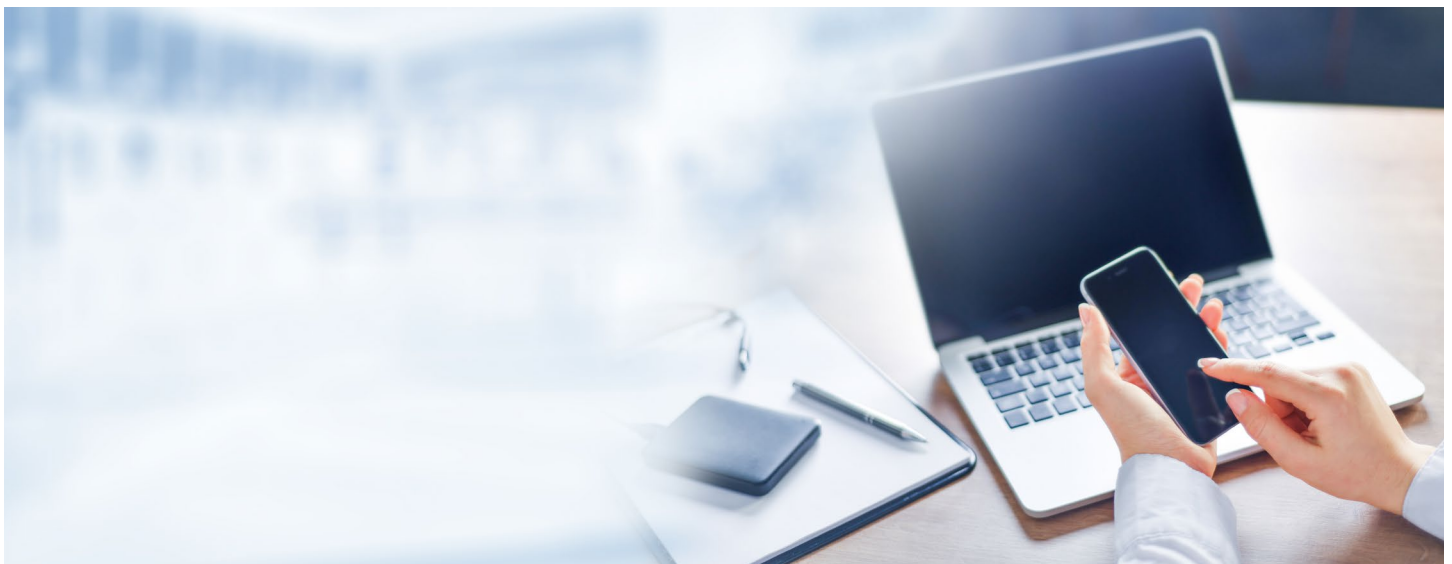
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## How we can help you

KPMG helps its clients overcome deal obstacles by taking a truly integrated approach to delivering value and by leveraging its depth in the financial services industry, data-supported and tools-led insights, and full M&A capabilities across the deal lifecycle.

With a FS specialization, our teams bring both transactional and operational experience, delivering rapid results and value creation.

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