Creating Silver Linings through M&A During a Downturn

Part 3: Transformational Investing for Success

What to watch on Netflix while social distancing during the coronavirus pandemic

What's New on Netflix, Hulu, HBO and Amazon in April: A Streaming Guide for Coronavirus Quarantine

PANDEMIC PICKS

Netflix adds PIN-protected profiles as usage surges during coronavirus quarantine

10 Netflix series to binge while in self-quarantine

One of the most successful businesses during the '08/'09 recession is unsurprisingly generating media headlines again during the current COVID-19 lockdown. Streaming movies from Oscar nominees and fictional pandemics to the country's most recent obsession, *Tiger King*, Netflix has experienced a strong rise in stock as quarantined consumers are utilizing substantial portions of their at-home time (and bandwidth) watching popular movies and TV shows.

In this article, Carleton McKenna analyzes the transformational investments that help businesses come out of recessionary periods with some of their highest growth rates. We will then discuss what transformative investment opportunities may exist in the current environment to help position companies to achieve strong growth coming out of the COVID-19 crisis.

Strategic investment (or lack thereof) in the present will shape the next 3 years.

Netflix gained 3 million subscribers in 2009, the peak of the Great Recession. As new video-on-demand services became available though Comcast and Apple, Netflix identified opportunity to release its own tv/movie streaming plan that would provide an "unlimited" amount of entertainment. Despite a mortgage crisis, major company bankruptcies and a highly depressed stock market, Netflix did not halt its growth plans and made one of the riskiest moves in its history. In 2008, after spending years of development on the Netflix Player (a digital media player and hardware for at-home streaming), the Company decided to spin the project into a separate company known as Roku. Netflix felt producing its own hardware would conflict with its device maker partnerships (e.g. Sony, Samsung, LG) and decided to focus its business model on licensing (digital content) and related services. After multiple capital investments into Roku and releasing the new Netflix streaming plan with Roku's partnership, the Company grew with their customer service reputation and high-quality brand. Netflix achieved its highest annual revenue growth rate just two years after the Great Recession.

Figure 1: Netflix YOY Revenue Growth (2008-2011)

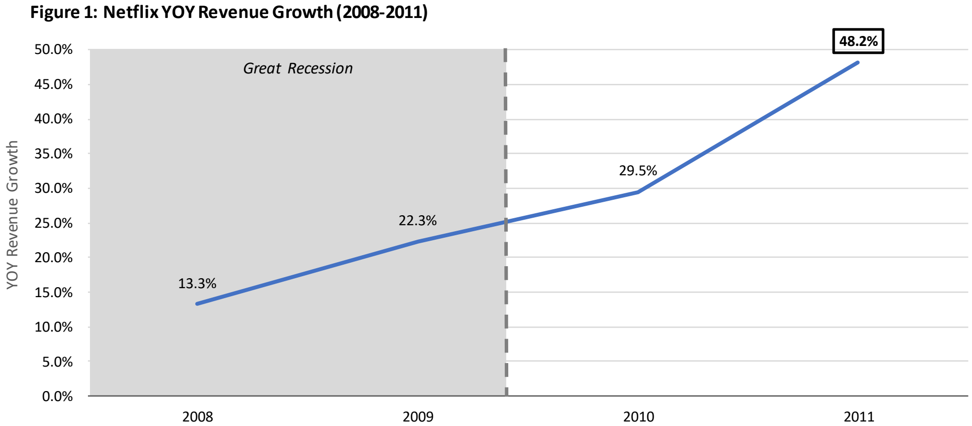

Chart (left) demonstrates Netflix's annual revenue growth rate (%) from 2008 to 2011. Netflix has not reached 40% annual revenue growth since 2011. The company achieved their next highest growth rate in 2018, at 35.1%.

Sources: Forbes, MacroTrends, Pitchbook, Fast Company

Economic Disruption may trigger the "New," but Industry Disruption creates the "Norm."

Innovators are flexible and adaptable by nature, even when they are unsure as to how a cycle will turn out. Not only was this demonstrated by Netflix in their risky spin-off and streaming launch decision, but we see this innovation and adaptability daily in the current COVID-19 environment. It is remarkable how quickly these innovators — from tech, connectivity and healthcare companies to the universes of government, academia and philanthropy — are collaborating to advance medical treatments and healthcare delivery to address the immediate challenges due to COVID-19. This sense of urgency to find solutions ***now*** will likely set the stage for future rapid innovation. Furthermore, when the COVID-19 crisis ends, companies will be able to apply these new collaborative models to other multi-stakeholder problems.

As we consider how quickly this pandemic has shaped our daily routines to include telemedicine, distance learning and new habits of professional and personal communication, we can likely expect a catalyst of **(i) long-term investment in various remote technologies and systems, and (ii) the formation of partnerships as a means for quicker and lower-risk adoption.** Companies who are proactive and strategic in incorporating these innovations into their business models are more likely to find success coming out of the current economic downturn. Companies who choose to delay these investments and partnerships could find themselves competing in a "New Normal" with a less-relevant business model.

The following emerging technology verticals should become highly valuable across many industries heading into a post COVID-19 landscape:

Vertical: Supply Chain Technologies

Description: COVID-19-related supply chain disruptions are highlighting the need for technology that can help ensure business continuity, mitigate the impacts of economic shocks and diversify value chains. Companies providing increased visibility, flexibility and automation to supply chains present strong investment opportunities as they offer data analytics and real-time monitoring services to help companies identify and react quickly to changes.

Key growth categories:

- Supply chain sourcing/ visibility and freight technology
- Digital warehousing marketplaces
- Mobile robots and autonomous technology
- Last-mile delivery apps
- Logistics enabling platforms

Who's already investing:

3/20/2020: aptean acquires Paragon via its financial sponsors TA ASSOCIATES VISTA EQUITY PARTNERS

Source: Pitchbook

Vertical: Artificial Intelligence & Machine Learning

Description: AI's ability to fortify and streamline workforces is a long-term trend that will likely be accelerated due to cost-cutting and labor restrictions as a result of COVID-19. As manufacturing and retail have been hit hard, enterprises have increased their inquiries into AI-enabled robotics and service capabilities. Job cuts will likely start in large enterprises, but may cushioned by increasingly prevalent Robotic Process Automation and AI assistants for sales support, marketing optimization and routine back-office tasks. With the creation of these new human positions, there will be a need for retooling and increased learning and development within organizations.

Key growth categories:

- AI in healthcare, financial services and industrial
- Robotic process automation
- AI support assistance
- Skill training processes

Who's already investing:

3/5/2020: salesforce ventures invests in A5 along with existing investors C3 CAPITAL Jefferson Capital Partners

Vertical: Foodtech

Description: Widespread government-mandated restaurant closures and consumer quarantining are driving unprecedented demand for grocery and food delivery services. These are likely to expand permanently as more consumers become accustomed to food delivery. There may be increased interest across the food delivery ecosystem for technologies that improve the speed, transparency capabilities and efficiency of delivery, such as ghost kitchens, delivery robots and other KitchenTech.

Key growth categories:

- Online grocers, apps and marketplaces
- Ghost kitchens
- Delivery robots
- KitchenTech and robotics

Who's already investing:

3/17/2020 Costco Wholesale acquires Innovel

Vertical: Cloudtech, DevOps & Data Security

Description: An environment now filled with quickly evolving consumer demands could cause firms to increase investment in digital products or pivot to new ones, particularly those involved in online commerce. The need for work-from-home capabilities could drive short- and long-term demand for DevOps collaboration and communication tools as well as IT automation tools that help scale infrastructure. Should remote work continue to increase in popularity, there will be a need for even greater data protection as more information travels through cloud data centers.

Key growth categories:

- Communication and collaboration tools
- Infrastructure automation
- Software building, deployment and management tools
- Data protection/ cybersecurity

Who's already investing:

4/7/2020: accenture acquires Revolutionary Security

Vertical: Retail Health & Wellness

Description: Telemedicine startups in the U.S. are experiencing a surge in demand amid the COVID-19 outbreak, aided by a push from the federal government. As adoption grows and providers encourage its use, telehealth is experiencing significant growth. Increased social distancing and pandemic anxieties have caused mental wellness and at-home fitness applications to gain traction. We expect COVID-19 to have major implications on healthcare technology, spurring rapid adoption and innovation of remote diagnostics, robotics and remote patient monitoring devices.

Key growth categories:

- Telemedicine
- Hospital robotic and remote monitoring devices
- Mental wellness applications
- At-home fitness applications and devices

Who's already investing:

3/20/2020: New Capital Partners invests in Telehealth Solutions

Vertical: Insurtech

Description: Insurers will likely see an increase in claims due to the COVID-19 crisis, while managing the effects of a delay in elective procedures—catalysts to drive adoption of claims automation and fraud management technology. The nature of this health crisis is also likely to spur interest in risk analytics technologies that incorporate disease and outbreak data to help underwrite policies.

Key growth categories:

- Claims management and automation
- Fraud management technology
- Risk analytics technologies

Who's already investing:

3/20/2020 Majesco acquires InsPro Technologies

Source: Pitchbook

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"There is no such thing as luck, merely opportunity meeting preparedness." —George S. Patton Jr.

While we can estimate the technological investments and actions that may help a company exit the COVID-19 crisis on a positive trajectory, there is no certainty around the long-term economic impact of this pandemic. Our firm advises our clients and prospects with evidence and experience-based research, strategies and best practices that are relevant to businesses navigating the current environment. As demonstrated throughout the *Creating Silver Linings Through M&A During a Downturn* series, there are various strategic and financial approaches that businesses should consider during these challenging economic times to support future growth:

1. The unique opportunities associated with large amounts of available capital, both private equity dry powder and corporate cash, in combination with quickly changing consumer trends;
2. The ability to use divestitures to refocus management teams and operations on the true core of your business, while also improving financial positions; and
3. Proactively analyzing and investing in the transformational technologies that are anticipated to re-shape various industries following this economic downturn.

Successful companies like Netflix did not thrive after the Great Recession due to a matter of luck—they stayed true to their core competencies and made strategic moves to enhance their position in a post-recessionary environment.

At Carleton McKenna, we are here to help the middle market business owners of 2020 to find and create their own Silver Linings. If you are a business owner (or know one) looking to sell, raise capital, make acquisitions, or simply gain a better understanding of what strategic alternatives may exist for you, we can help.

M&A Advisory Team:

Paul H. Carleton
Managing Partner
phc@carletonmckenna.com

Christopher J. McKenna
Managing Director
cjm@carletonmckenna.com

Nora T. Mahoney
Vice President & Counsel
ntm@carletonmckenna.com

Brooke A. Hradisky
Vice President
bah@carletonmckenna.com

Alexis M. Becker
Associate
amb@carletonmckenna.com

Andrew W. Lease
Analyst
awl@carletonmckenna.com

David W. Kuhr
Financial Operations Principal
dwk@carletonmcknna.com

Carleton McKenna & Co:

We believe businesses are the economic engine of our society, and that business owners deserve and require a proactive advocate throughout life changing transactions.

Firm Overview:

Carleton McKenna & Co. is an independent investment banking firm providing M&A Advisory, Capital Raising, and Pre-Transition Advisory services. We deliver hands-on transaction execution, with clear, insightful strategy to drive extraordinary success.

We work with middle market closely-held businesses, multi-generational family businesses, portfolio companies of financial sponsor firms and divisions or subsidiaries of public companies focusing in Manufacturing & Specialty Chemicals, Consumer Products, SaaS, Healthcare and B2B Services.

Our Team is made up of finance and accounting experts, operators, C-Suite and Board professionals, lawyers, consultants, and marketing professionals. These diverse experiences and skills drive extraordinary results for our clients.