"Play On" – Investing in the Post-COVID-19 Pandemic Experience Economy

As we come to terms with the lasting impacts of the COVID-19 pandemic, it's fair to say we have entered a new age in the consumer economy. While nearly all consumer facing companies dealt with uncertainty during the pandemic, it was a roller coaster ride for experience-based businesses, such as theme parks and live entertainment, recreation and travel companies. Now that COVID-19 vaccines are on the rise and consumers are increasingly eager and able to get back to in-person entertainment, what does it mean for mergers and acquisitions (M&A) activity in the experience marketplace?

The Experience Boom of Pre-2020 Will Continue

Prior to the pandemic, consumers in the established e-commerce world valued experiences and making memories above spending money on "things." In fact, with the experience economy in the U.S. projected to be worth $12 billion by 2023, consumer spending on experiences was growing nearly four times faster than dollars spent on goods.[1] It was a trend that transcended every age bracket and socioeconomic status; 78% of Millennials preferred to spend money on experiences over material goods, Generation Z (Gen Z) focused on community and authenticity and Baby Boomers took a "less is more" approach to retirement.

This was echoed in the market as well. In recent decades, expansion of major theme parks and family entertainment centers, such as Disney and Great Wolf Resorts, took place alongside a proliferation of music festivals and experiential retail offerings, including escape rooms and pop-up concepts. This translated to an increasing share of gross domestic product growth and job creation. Employment in the leisure and hospitality industries grew about 30%, reaching a peak of nearly 18 million jobs in February 2020, according to the Bureau of Labor Statistics.

Entering the COVID-19 pandemic, live entertainment, location-based experiences, travel and recreation all but vanished overnight. Employment in leisure and hospitality fell by 8.2 million jobs in March and April of 2020. Yet, as social beings, people still craved interaction during mandated shutdowns and the demand for experiences continued. With social distancing in effect, consumers quickly embraced innovation through digital experiences. This need for digital dexterity was seen in many facets of pandemic life, especially in music streaming, film and television streaming, video sharing and virtual reality simulations.

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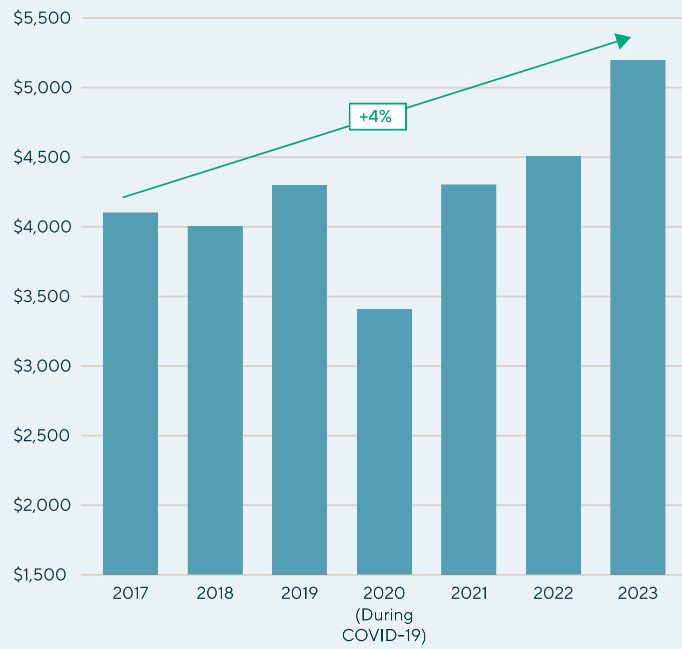
COVID-19 Vaccinations Drive the Bounce Back

In early 2021, vaccines became increasingly available and new daily cases of COVID-19 steadily decreased. This allowed many experience- and location-based vendors to open their doors and welcome back eager customers. While the later emergence of the COVID-19 Delta Variant did set back the transition towards pre-pandemic normalcy, prospects remain high as vaccines prove highly effective. As of October 2021, 67% of Americans were vaccinated against COVID-19, with the Centers for Disease Control and Prevention's models predicting a steady decline in cases through March 2022. This has led to many consumers becoming increasingly optimistic, both about their health as well as new opportunities to make authentic, in-person connections. In a recent survey, 94% of Gen Z and Millennials said they plan to attend in-person experiences in the near term and around half of American travelers say they plan to take a trip in the next three months.[3]

The experience economy is poised to benefit from immense, pent-up demand, with expectations set for a strong rebound in festivals, sporting events, amusement parks and gyms. We expect that consumer spending on experiences will likely eclipse or even surpass pre-2020 numbers.

U.S. Household Spend on Recreational Activities[2]



COVID-19 related factors caused households to reduce their budget on experiential activities. Yet, consumers expect to resume steady increases in their recreational spending going forward.

LINCOLN PERSPECTIVE

As circumstances continue to improve, Lincoln expects several trends to rapidly pick back up and drive steady growth in the experience economy due to a combination of the pent-up demand for services, permanent shifts in consumer spending patterns and a change in the consumer landscape. These trends include:

A resurgence of in-person experiences
Consumers will return in droves to restaurants, theaters, sporting events, concerts and other leisure activities that they missed in the last 18 months. This will be bolstered by higher-than-average savings; in the U.S., personal savings rates at the end of 2020 were nearly double the year prior.

Emotional wellbeing
The events of 2020 exponentially increased reports of anxiety and stress. Consumers will now uncompromisingly prioritize their wellbeing, with positive implications for the experience economy. Experiences will no longer be viewed simply as an enjoyable way to spend time, but as an investment in longer-term emotional fulfillment.

Shifts to remote and hybrid work
Many consumers are adapting to a mix of in-person and remote work. The absence of daily commutes will translate to higher personal savings that can be spent on vacations, dining out or other social activities.

A new life for brick-and-mortar
With the continued trend toward e-commerce retail, experience-based businesses are increasingly able to take advantage of the influx of available commercial real estate, particularly malls. Escape rooms, movie theaters, fitness clubs and family entertainment centers all need physical space. Businesses offering experiences are setting up shop with attractive lease terms in compelling locations vacated by retailers.

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Accelerated innovation
In recent years, innovation has breathed new life into the experience economy, including a surge in immersive art and Instagram-friendly, pop-up venue concepts. As entrepreneurs re-emerge, they will bring with them 18 months' worth of new ideas and content to satiate and excite consumers across the board.

Key M&A Takeaways

Despite the COVID-19 pandemic, corporate and private equity investors in the experience sector have continued to pursue opportunities to deploy capital or seek opportunities in line with their strategies. Recent examples include:

- Callaway's acquisition of Topgolf, the market leading, technology-enabled golf company in March 2021 at 15x 2022E EBITDA
- The acquisition of Bowlero, the market leading operator of bowling and entertainment centers via a special purpose acquisition company for ~10x 2022E EBITDA in July 2021

While the current environment continues to present some challenges in valuing companies in the experience sector, sellers expect pre-pandemic valuations to hold. Certainly, there will be opportunities to acquire companies negatively impacted by recent factors, at compelling valuations with long-term fundamentals remaining unchanged. Similarly, acquirers are willing to pay premium valuations for opportunities that can substantiate an advanced recovery.

For businesses considering a potential sale, it is critical to evidence a permanent return of customers supported by consumer comfort levels with COVID-19-related concerns and to demonstrate long-term, sustainably strong margins.

For buyers in the near-term, some uncertainty concerning buyer appetite, valuation and the prospect of a successful transaction is still expected. However, investors are recognizing that consumers are progressively ready and able to spend more on highly coveted, long-awaited experiences while vendors are ready and eager to meet demand.

Connection to new capital will increasingly play a role in this reinvigorated, post-pandemic experience marketplace. Lincoln expects strong valuations going forward and an especially active M&A market for businesses that have returned to or exceeded pre-pandemic performance.

> Memorable experiences are about triggering sensations. People will always crave the adrenaline rush of a theme park ride, shared experiences with friends and family or the excitement of exploring new places. With the U.S. economy returning to pre-COVID-19 pandemic levels due to increasing vaccination rates and strong market demand drivers, the experience economy will shift into a new era of explosive growth. Are we ready to finally jump-start the Roaring 2020s?

[1] *McKinsey Report*
[2] *Lincoln Insights*
[3] *U.S. Travel Association*

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