William Blair

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Packaging Industry M&A Activity Surges Amid Strong Tailwinds

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Packaging

Packaging Industry M&A Activity Surges Amid Strong Tailwinds

Demand growth during the COVID-19 pandemic accelerates longer-term growth dynamics underlying the industry's attractiveness.

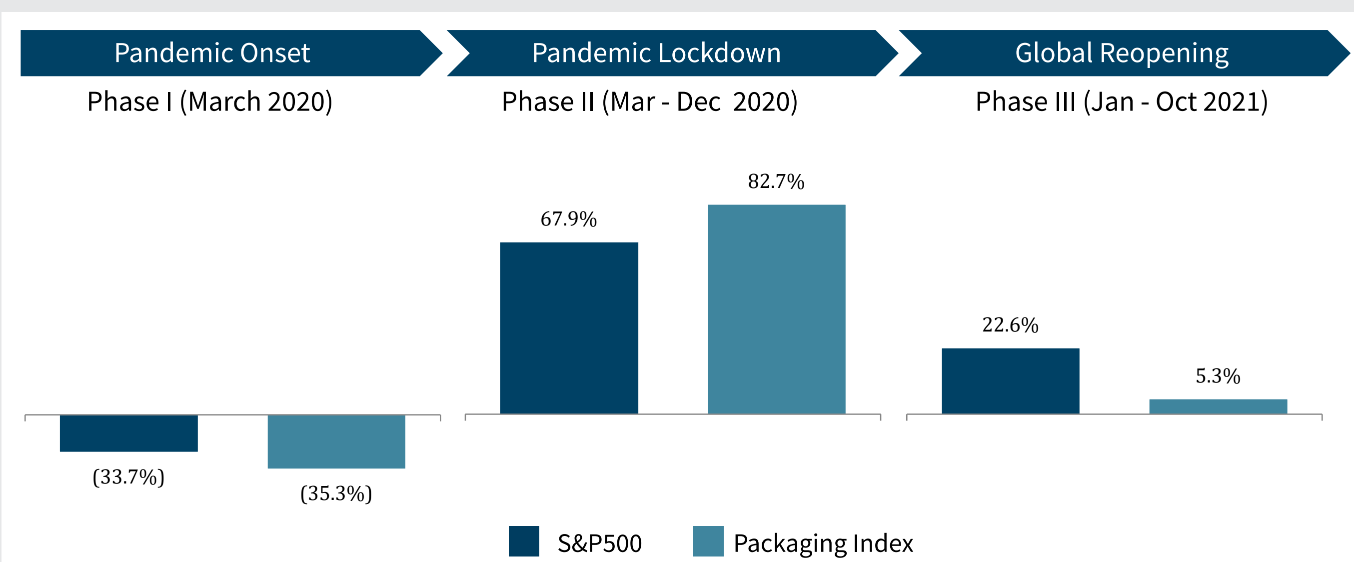
The packaging industry entered 2020 backed by several long-term secular trends that were driving increased demand, and the industry's growth accelerated as economic activity shifted to meet the challenges of the COVID-19 pandemic. The industry's strong performance drove increasing revenues and the growth of key end-markets, including food and beverage and healthcare, as well as showcased its overall stability in a period of market uncertainty.

Packaging M&A activity has surged throughout the first three quarters of 2021 as buyers and sellers eagerly returned to the market after deal-making all but stopped in the packaging sector during the initial stages of the pandemic in the first and second quarters of 2020. The strong performance of packaging companies during the pandemic validated the thesis that the industry provides stability during periods of overall market volatility. Moreover, the pandemic boosted already existing tailwinds—such as the rapid growth in e-commerce and brand owners leveraging packaging to differentiate their products on shelves—that position the industry for greater long-term growth. As a result, valuations for packaging companies today are very healthy as financial sponsors and strategic acquirers are seeking acquisition targets in this attractively positioned space.

As shown in the following chart, the market can be segmented into three phases since the beginning of 2020. First, markets experienced a fear-driven selloff during the early days of the COVID-19 pandemic across all sectors, including packaging. During the second phase, from late March 2020 to the end of 2020, packaging stocks recovered quickly and substantially outpaced the broader market. The strength of packaging stocks over this period was driven by widespread economic reopening, accelerating demand for packaging products in consumer/food and beverage markets as consumers stayed home at higher rates, and a massive surge in e-commerce activities that led to increased demand for protective packaging solutions. During the third phase, which covers January 2021 through the end of October, packaging stocks have been relatively flat and underperformed the broader market. This relative weakness was due to a normalization of demand favoring growth-focused stocks as well as inflationary pressures from resin, corrugate, and wages providing headwinds to packaging companies.

Stock Perfromance by Phase

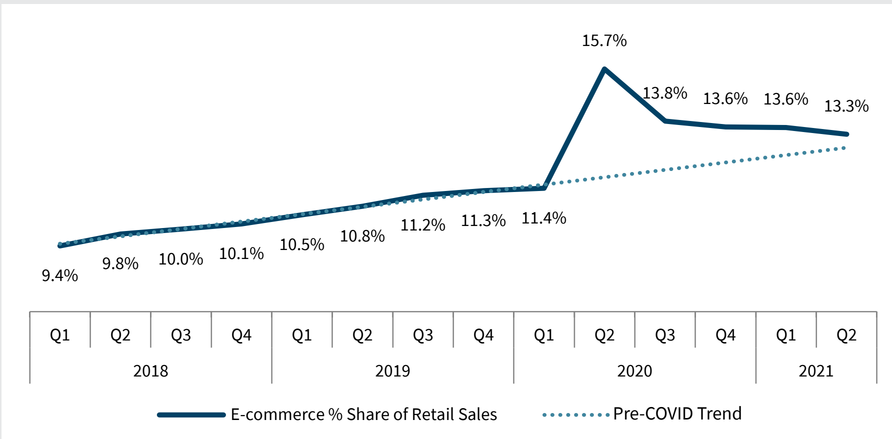
Packaging overall stability and favorable outlook led the market to outperform the S&P500 over the first two stages of COVID-19, collectively



Source: Capital IQ

Ongoing Momentum in e-commerce

Importance of e-commerce to the economy grew significantly during early phases of COVID-19; momentum in e-commerce is expected to continue, which will further evolve the manner in which goods are packaged, delivered and consumed



Source: Retail Indicators Branch, U.S. Census Bureau; Q2 2021 data is preliminary
Note: Seasonally adjusted

COVID Accelerates Existing Growth Dynamics

The packaging industry serves as a microcosm of how the COVID-19 pandemic accelerated trends that were already in place before the virus disrupted the global economy. Against that backdrop, we examine several of the dynamics that have led to the relatively strong performance of the packaging industry over the course of the pandemic.

Increased e-commerce Penetration: The pace of e-commerce purchases—which were growing steadily even before the pandemic—skyrocketed during 2020 as the rates of in-person shopping and dining plummeted. The U.S. Census Bureau estimates that e-commerce purchases grew by more than 32% in the fourth quarter of 2020 compared to the fourth quarter of 2019, and e-commerce accounted for nearly 16% of total goods sold, up from just 9% at the beginning of 2018.

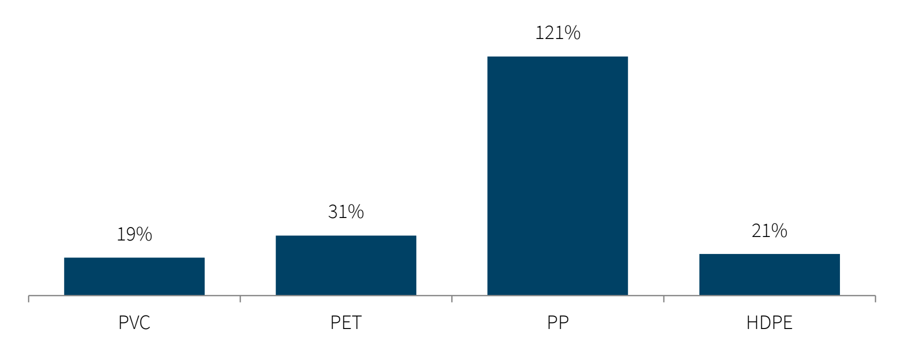
In response to the spike in e-commerce activity, demand for boxes, containers, and wrapping that could safely transport food and other products increased significantly. In particular, we see an opportunity for companies offering innovative packaging solutions to meet escalating e-commerce volumes. For instance, companies that provide products that reduce shipping costs by cutting weight and space should be well positioned. In addition, as food delivery continues to expand, companies providing safety- and sanitation-focused options, such as tamper-evident packaging, have the potential to stand out. In the last several quarters, the penetration rate has slowed somewhat due to a massive pull-forward of e-commerce activity and the overall strength of consumer purchasing power and retail activity, coupled with the general reopening of the economy. Nevertheless, we expect e-commerce volumes to remain higher than pre-pandemic levels.

Packaging's Continued Importance in Building Brand Awareness: For years, many consumer packaged goods (CPG) industry observers hypothesized that the growth of e-commerce would undermine the importance of labels and flexible packaging in terms of building brand awareness and consumer loyalty. But the so-called "brand awareness cliff" certainly did not come to fruition throughout the COVID pandemic as e-commerce penetration increased. Packaging remains an important part of the brand experience and a key path to building customer loyalty—whether the consumers are selecting items on a physical shelf or viewing options on an app and then opening the package when it is delivered to their homes. This is particularly true as start-ups and emerging CPGs try to differentiate themselves amid a proliferation of SKUs across categories such as food, personal care, and nutraceutical products, which is driving demand for high graphic labels, such as pouches, shrink sleeve and pressure sensitive formats.

Growing—But Uneven—Demand for Food Packaging: While there was broader growth in demand for packaging throughout the COVID pandemic, the impact varied both across and within industries. This was especially true in food and beverage. Demand for packaging for CPG items, fresh produce, and other products sold in retail settings surged as consumers stocked their pantries and at-home cooking increased. But demand from foodservice providers varied drastically by channel. Packaging for food delivery and takeout grew exponentially, while demand from in-person foodservice, such as cafeterias and concessions at stadiums, plummeted.

Significant Rise in Material Cost

Over the LTM period, input costs of all types have risen putting pressure on the profitability of packaging companies. Most notably, resin costs, a packaging company's large cost category, saw material rises in the LTM, which has led to some companies placing M&A ambitions on pause until calmer periods arrive.



Source: Plastics News; data is from November 2020 to October 2021
Note: Values represent increases within a pricing index

Continued Attractiveness of Healthcare Packaging: Healthcare has long been one of the most attractive end-markets for packaging for multiple reasons. An aging and increasingly health-conscious population is driving increased demand for health and wellness products, particularly vitamins and other supplements. These trends accelerated during the pandemic as health concerns dominated the public consciousness, resulting in an expanded target market as COVID pushed younger populations to refocus on their physical wellbeing and take a more proactive approach to their overall health and preventive care. Furthermore, healthcare consumption is more stable than other more price-sensitive sectors, and healthcare products often require specialized, higher-margin packaging.

Rise in Resin Prices Creates Short-Term Disruption

While the longer-term outlook for packaging appears bright, the industry is grappling with some near-term issues such as increasing costs for resin, a key input for a range of packaging materials. Heightened demand for resin had already pushed prices higher when extreme weather in February 2021 struck Texas, where many resin manufacturers are located, and has remained elevated throughout 2021 due to supply chain disruption. The storms led to a rapid, unplanned shutdown of some of the country's largest resin manufacturing plants, which were already stretched thin from increasing pandemic-driven demand. Prices for polypropylene (PP) and high-density polyethylene (HDPE) resins have been particularly affected because many PP and HDPE resin manufacturers are located in Texas.

The elevated resin prices have adversely impacted the performance of select packaging companies in the short term, which is impacting how packaging companies approach M&A. Select packaging companies are pushing forward with sale efforts and attempting to capture normalized earnings via an EBITDA add-back for "one-time" resin cost inflation, which is receiving a mixed reception from investors. Other packaging companies are electing to delay launching M&A processes until input prices stabilize. Despite uncertainty on the exact timing, we expect resin prices to decrease in the near term as manufacturing capacity is restored and demand moderates. As a result, packaging companies should regain visibility on input prices, allowing for a resumption of M&A activity and potentially leading to even more opportunities in 2022 following a highly active 2021 year-to-date.

Sustainability Concerns Continue to Evolve

Before the COVID-19 pandemic, plastics had come under increasing scrutiny as consumers, investors, and industry participants began to question the sustainability profile of plastics relative to alternative substrates. The pandemic, however, seems to have caused many people to take a more balanced view of plastics' overall impact on society and the environment. Plastics are playing an essential role in stopping the spread of the virus and are key materials in the production of masks, gloves, and other personal protective equipment (PPE).

The Biden administration's focus on climate change, however, could restore pressure on plastic manufacturers. We expect these efforts to focus on increasing recycling capabilities, pursuing alternative materials in select applications, and finding other ways to use plastics in a more environmentally sustainable way—rather than eliminating plastics from many everyday applications. Over the longer term, though, plastics will continue to face environmental sustainability pressure, so packaging manufacturers that are aligned with this trend will be well positioned to benefit both commercially and during potential sale processes.

Key Sustainability Observations

Bark Lacking Bite

- Ongoing sustainability pledges from CPGs running out of time for action; timeline to 2025 continues to shorten
- Pledges focus on outcomes without means to an end; significant investment required to achieve goals

No Forum for Change

- U.S. recycling infrastructure woefully behind Europe and took steps backward in 2020; billions required to enhance U.S. recycling infrastructure to support sustainability pledges
- Consumers lack education in recycling and desire to recycle at store fronts
- Until consumers accept price increases, necessary investments not likely to occur

Biobased Resins Remain Nascent

- Generally compelling physical properties augmented with an attractive sustainable offering
- Industry transition to PLA resin requires meaningful capex; PLA's preferred cast extrusion process serves as headwind to adoption (blown film represents majority of industry's current asset base)
- Lack of scale in PLA and PHA and an unfavorable cost profile (~2x more expensive than traditional resin) will further limit near-term adoption

Five-Year Outlook

- Plastic reduction (rather than elimination or migration away) appears to be the most likely path (e.g., downgauging, Machine Direction Oriented film (MDO), post-consumer resin (PCR) adoption)
- Advancements in recycling and biobased resins; however, infrastructure gaps and comparative price vs. traditional plastic will stymie traction
- Potential risk of "plastic tax" and/or bans for nonsustainable plastics (Europe); legislation in U.S. appears disjointed/non-imminent

Recent William Blair Packaging Transactions

We completed several transactions for packaging companies during 2021 with specialties in the food and health and wellness industries that exemplify these trends. In October 2021, we advised on the sales of Mold-Rite Plastics and Alpha Packaging to Clearlake Capital and Pretium Packaging (Clearlake-backed), respectively. Mold-Rite and Alpha are leaders in their respective segments of rigid packaging and continue to benefit from favorable health and wellness macro trends (e.g., gummy vitamins) and their unique operating models to address ongoing market demand shift toward short-run production due to continued SKU proliferation.

Also in October 2021, we advised on the sale of PPC Flexible Packaging, a leading flexible packaging converter, to GTCR. PPC received strong interest from the investor community due to its status as an M&A platform following several successful add-on transactions and its dedication to providing brand defining solutions to attractive, high-growth subsegments of the flexible packaging market (e.g., emerging CPGs).

In February 2021, we advised AMB, a leading manufacturer of rigid and flexible films for use in food packaging, on its sale to Peak Rock Capital. AMB, based in Italy and with operations in a number of major European markets, specializes in food-grade recycled plastic. The company has emerged as a leader in developing sustainable and recyclable plastic packaging.

Further insights into each of William Blair's 2021 year-to-date transactions are included on pages 9 and 10.

Strong Opportunities for Future M&A Activity

In the early stages of the pandemic, most packaging transaction processes were put on hold because of widespread uncertainty. As attempts to mitigate the effects of COVID-19 took center stage, many management teams shifted their focus from deal-making to maintaining safe working conditions and protecting their employees.

Starting in the fourth quarter of 2020, however, M&A activity began surging as business conditions started to normalize, leverage markets returned to and even exceeded pre-COVID levels, and management teams were able to turn their attention back to potential transactions. This momentum continued throughout the first three quarters of 2021, and the packaging industry is poised to maintain these high levels of transaction activity throughout the rest of 2021 and beyond.

The packaging industry remains highly attractive to both strategic and financial acquirers as a result of packaging companies' ability to generate cash flow and the relative stability of end-markets given the longer-term trends described above. M&A transactions today are being completed at or above pre-COVID valuations, reflective of the large pent-up demand from buyers that were forced by the pandemic to spend much of 2020 on the sidelines. Financial sponsors, in particular, have been particularly aggressive in looking to deploy capital in the packaging industry, thanks to extensive equity capital available for investment and favorable debt markets amid low interest rates. Moreover, many investors find the stability provided by packaging companies to be compelling, particularly as a constituent within a broader portfolio.

Many sellers are looking to capitalize on the strong current M&A market and higher valuations for growing companies. Sellers that experienced a surge in sales during the pandemic need to be prepared to show which portion of this increase will be sustainable after the pandemic; determining the magnitude of a target's "COVID bump" has been a major focus area of buyer diligence in recent processes.

The result of these factors is a fertile environment for sellers seeking to monetize their businesses and/or partner with new owners and buyers eager to add attractive assets to their portfolios.

To learn more about the trends shaping the M&A and capital-raising environment in the packaging industry, please do not hesitate to contact us.

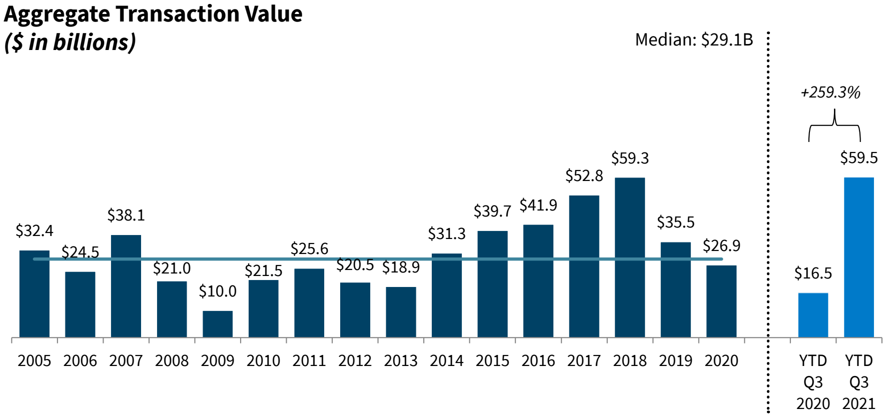
Packaging Market Analysis

We look behind the numbers to examine the market dynamics that are driving dealmaking trends in the packaging industry.

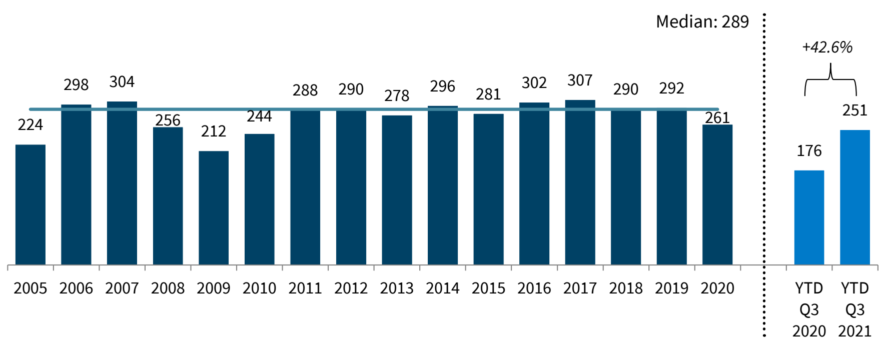
Packaging M&A - Global Value, Volume, and Valuations

M&A activity in the packaging market roared back in 2021 following a slowdown in activity in 2020 as a result of the COVID-19 pandemic. Through the first nine months of 2021, packaging M&A has already created new all-time high watermarks in transaction value and transaction multiples, with top-tier packaging companies receiving EV/LTM EBITDA multiples well into the teens.

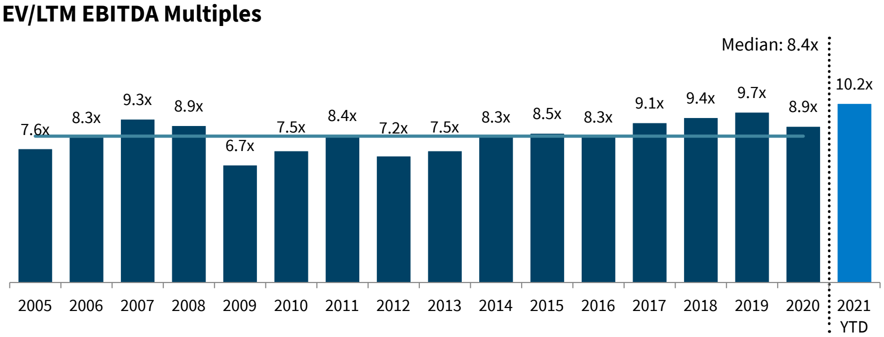
Aggregate Transaction Value
($ in billions)



Number of Transactions



EV/LTM EBITDA Multiples

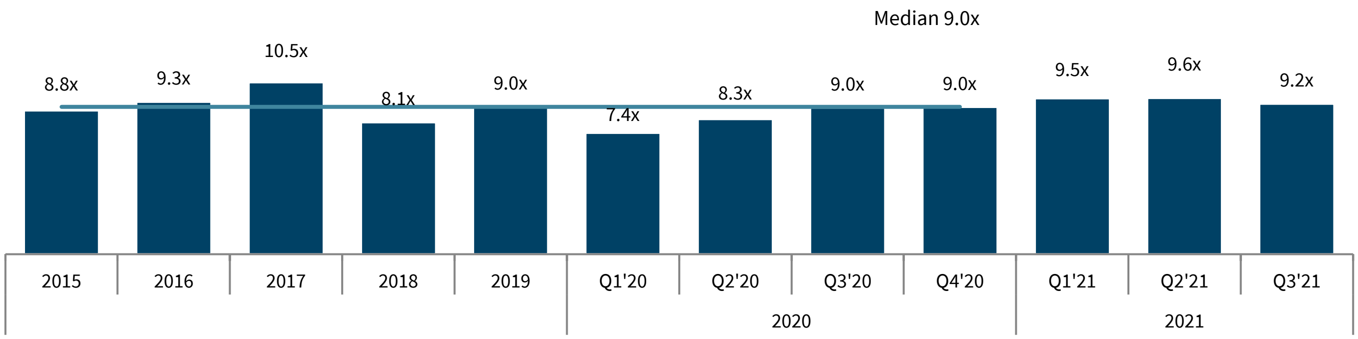


Sources: Dealogic and William Blair market analysis; aggregate volume and value includes all announced deals

Public Company Valuations in Packaging

Publicly traded packaging companies continue to trade near the long-run median multiple of 9.0x since 2015. As discussed earlier, publicly traded packaging companies outperformed the broader market during the bulk of the COVID-19 pandemic, following the initial market sell-off in Q1’20. Recent quarters are witnessing a pull back in valuations for public packaging companies as investors continue to rotate towards more growth-focused stocks.

In addition, there continues to be a disconnect forming between public and private sector valuations for packaging companies (+1.0x EV/LTM EBITDA). The valuation spread can partially be attributable to the depth of focus on the packaging market from private equity investors, debt markets favorable view of the packaging market supporting LBOs (several transactions receiving +7.0x total debt/LTM EBITDA), high levels of market fragmentation for inorganic growth strategies, and strong organic growth prospects from smaller, more specialized private packaging businesses.. Going forward, this valuation spread may lead to an increase in take-private activity, similar to Madison Dearborn Partners’ take-private of IPL Plastics in Q4 2020.



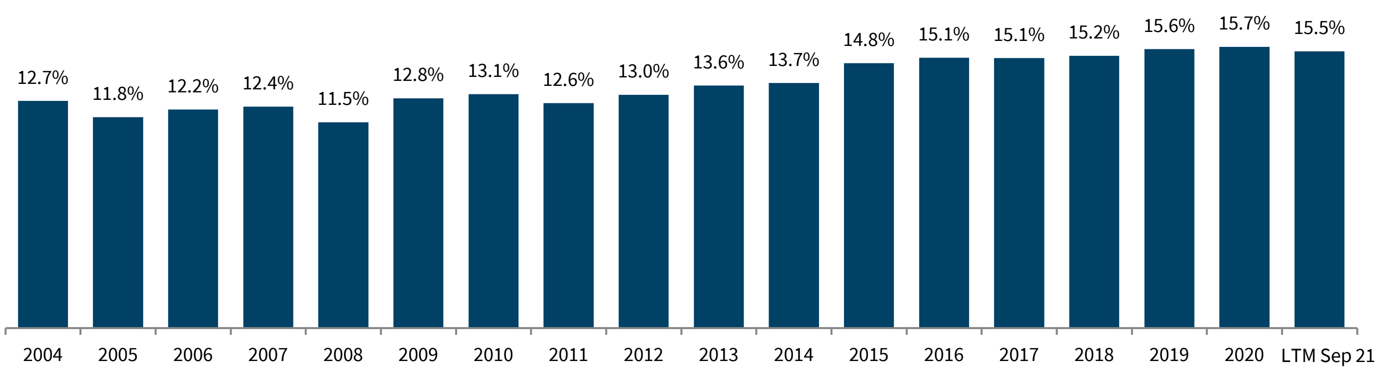
Source: Capital IQ and William Blair market analysis
Note: Median includes year-end values between 2015 and 2020

Profitability Trends Face Headwinds in Near-term

LTM EBITDA margin for William Blair’s group of publicly traded packaging companies contracted in Q3 2021 YTD for the first time since 2011. Ongoing profitability pressure from dramatic, rapidly rising input costs across materials. (e.g., resin), transportation and labor drove the decline in LTM EBITDA margin.

To offset the rise in production costs, packaging companies typically pass through material cost increases either through contractual agreements or market-based pricing. These pass-through mechanisms tend to be effective in maintaining stable profitability over the long-term in most market environments. The rapid velocity of increases in input costs over 2021 resulted in a lag in profitability “catch-up”, which is yet to fully work its way though the income statement of packaging companies.

Over the near-term, we expect material cost profitability to increase as the resin markets stabilize, while non-material production costs will continue to create headwinds for profitability of packaging companies.



Source: Capital IQ and William Blair market analysis

Our leading packaging investment banking franchise is built on deep sector expertise and our strong relationships with buyers around the world. William Blair's long history of advising business owners across packaging substrates and end-markets provide a differentiated view on the key drivers of value for packaging businesses.

Recent William Blair Packaging Transactions

ALPHA PACKAGING
has been acquired by
PRETIUM
a portfolio company of Clearlake Capital

MRP MOLD-RITE PLASTICS
has been acquired by
CLEARLAKE

PPC FLEXIBLE PACKAGING
has been acquired by
GTCR

OAK HILL CAPITAL
has acquired
Technimark

Karat
Initial Public Offering

amd
has been acquired by
PEAK ROCK CAPITAL

Berry
U.S. Flexible Packaging Converting Business
has been acquired by
ABX
INNOVATIVE PACKAGING SOLUTIONS

CLARIANT
Healthcare Packaging International
has been acquired by
ARSENAL CAPITAL PARTNERS

Bemis Healthcare Packaging Europe
European Flexible Packaging Assets
has been acquired by
KOHLBERG & COMPANY
Nelipak healthcare packaging

WARBURG PINCUS
has acquired
Pregis
Protective Packaging Solutions

Automated PACKAGING SYSTEMS
has been acquired by
SealedAir Re-imagine

Revolution
BELIEVE IN BETTER PLASTICS
has been acquired by
ARSENAL CAPITAL PARTNERS

William Blair By the Numbers

550+
bankers globally with local cultural knowledge

20+
offices worldwide

$600 billion+
*in advisory and financing transactions**

* In the past five years as of September 30, 2021

Spotlight on Select 2021 YTD William Blair Packaging Transactions

PPC FLEXIBLE PACKAGING

has been acquired by

GTCR

- Leading flexible packaging converter dedicated to providing differentiated solutions to attractive, high-growth sub-segments of the flexible packaging market
- Proven M&A growth strategy compelmented with strong organic growth momentum driven by purpose-built operations serving short-to-medium run customers
- William Blair introduced PPC to the investing community during its 2020 Private Equity Conference; high interest in PPC coming out of the conference augmented with robust, upfront preparation enabled the process to be pre-empted at the initial indication stage

ALPHA PACKAGING

has been acquired by

PRETIUM

a portfolio company of Clearlake Capital

- Leading manufacturer of bottles and jars serving the health and wellness markets as well as other attractive growing markets
- Flexible, efficient, short-run production capability well aligned with industry trend towards SKU proliferation
- Transaction represents a highly synergistic acquisition creating a leading rigid packaging platform

MRP MOLD-RITE PLASTICS

has been acquired by

CLEARLAKE

- Leading manufacturer of caps, closures, and jars primarily serving the health & wellness market, as well as other attractive, growing markets
- Flexible, efficient operations with unmatched short-run production capabilities to address ongoing SKU proliferation trend
- Clearlake was attracted to Mold-Rite's leading positions in health-and-wellness markets and the opportunity to accelerate its M&A growth to supplement its leading organic growth momentum

William Blair Packaging By the Numbers

100+

Packaging-related Transactions Completed

95%

Closure Rate for Sell-side Transactions

10

International Transactions (Since 2017)

Spotlight on Select 2021 YTD William Blair Packaging Transactions

OAK HILL CAPITAL

has acquired

Technimark

- Leading manufacturer of custom plastic components for applications in the medical, consumer packaged, goods, and specialty industrial markets
- Oak Hill was attracted to Technimark's engineering and innovation capabilities yielding a proven track record of long-term growth, as well as the potential to continue expanding its platform organically and/or via M&A
- Oak Hill leveraged William Blair's long-term familiarity with Technimark and experience in the packaging and medical manufacturing markets to successfully pre-empt the sale process

Karat

Initial Public Offering

- Rapidly growing specialty distributor and manufacturer of environmentally-friendly, disposable foodservice products and related items for the foodservice industry
- William Blair acted as a co-lead bookrunning manager for the offering and the shares trade on the Nasdaq Global Select Market under the symbol "KRT"

amb

has been acquired by

PEAK ROCK CAPITAL®

- Leading international provider of sustainable (primarily PET) film solutions (rigid, flexible, printed, laminated) for food packaging applications
- Long-term track record of above-market, double digit growth with proven resiliency through COVID via dedication to the food end market
- William Blair's robust upfront preparation and global buyer insights enabled a competitive, multiple-party due diligence process predominately conducted virtually throughout COVID

Packaging Investment Banking

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About William Blair Investment Banking

William Blair's investment banking group enables corporations, financial sponsors, and owner/entrepreneurs around the world to achieve their growth, liquidity, and financing objectives.

Drawing on the collective intellectual capital and deep sector expertise of a global team that reaches over 20 cities on four continents, the investment banking group brings a rigorous and innovative approach to corporate board advisory projects, mergers and acquisitions, and equity and debt financing. From 2016 to 2020, the team advised on more than $430 billion in completed transaction volume.