Chemicals

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Investment Banking

Drivers of Strong 2016 Chemicals M&A Activity Poised to Continue in 2017

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Drivers of Strong 2016 Chemicals M&A Activity Poised to Continue in 2017

A series of megadeals pushed M&A activity in the chemicals industry to record levels in 2016 and set the stage for ongoing dealmaking in 2017.

Against a backdrop of sluggish GDP growth and low interest rates, cash-rich strategic acquirers in the chemicals industry became increasingly aggressive in their pursuit of high-quality assets. While megadeals involving industry giants such as ChemChina, Bayer, and Praxair dominated headlines and accounted for a majority of 2016’s record deal values, middle-market dealmaking has continued at a robust pace as companies look to achieve the scale and growth necessary to remain competitive amid ongoing consolidation.

Many of the factors that drove 2016’s record-breaking M&A activity should remain in place in 2017, but trade policy changes in China and the United States could alter the dealmaking landscape for cross-border transactions. We examine these and other trends that are driving M&A activity in the global chemicals industry.

Strong Fourth Quarter Caps Historic 2016

Global chemicals M&A activity was robust throughout 2016, shattering 2015’s previous record for deal value. In all, there were 631 deals announced in 2016 with a total deal value of $252 billion, figures that represent increases of 4% and 60%, respectively, over 2015 totals. The average deal size leapt from $259 million to $399 million, thanks in large part to a handful of industry-altering megadeals that accounted for nearly three-quarters of the total deal value: ChemChina’s acquisition of Syngenta, Bayer’s acquisition of Monsanto, Sherwin-Williams’ acquisition of Valspar, Praxair’s acquisition of The Linde Group, and the merger of Agrium and Potash Corp.

The fourth quarter saw an already thriving M&A market finish 2016 on an upward swing, with total disclosed deal values reaching $64 billion. With a total of 179 deals completed in the fourth quarter, deal volume was 23% higher than the third quarter and 38% higher than the fourth quarter of 2015.

Throughout the year, M&A multiples remained at historically high levels. Strategic buyers, a group that represented 83% of the global M&A deal volume in 2016, continued to demonstrate their willingness to pay premium multiples for tier-1 assets. These industry consolidators have become increasingly aggressive in using synergies to push valuations

Global Chemicals M&A

While the total number of transactions in the chemicals industry has remained relatively stable over the past decade, total deal values have surged over the last two years. Driven by blockbuster deals such as ChemChina’s acquisition of Syngenta and Bayer’s acquisition of Monsanto, the average deal size for chemicals M&A in 2016 increased to nearly $400 million.

($ in billions)

Source: Dealogic

Q1 ’14 Q2 ’14 Q3 ’14 Q4 ’14 Q1 ’15 Q2 ’15 Q3 ’15 Q4 ’15 Q1 ’16 Q2 ’16 Q3 ’16 Q4 ’16
Deal Value $10 $23 $41 $14 $16 $21 $27 $70 $130 $146 $161 $33
No. of Deals 158 172 179 195 144 177 155 $93 $85 $64 179
higher in competitive processes. We have also seen strong demand from financial sponsors, whose total deal value increased from $1.6 billion in the third quarter of 2016 to $13.6 billion in the fourth quarter. This fourth-quarter uptick suggests that private capital could continue flowing into the chemicals industry in 2017.

To succeed in a highly competitive environment, financial sponsors are increasingly looking to preempt deals or complete due diligence work early so they are prepared to move quickly and aggressively once a process begins.

**Consolidation Likely to Continue in 2017**

The factors that spurred the consolidation wave and robust valuations in 2016 are projected to continue into 2017. Slow GDP growth and low, albeit rising, interest rates mean that M&A will continue to be a primary driver of growth in the chemicals industry. As oil and other input costs have remained low, chemical companies have been able to strengthen their balance sheets and improve margin profiles. M&A valuations should continue to be supported by an overall supply-and-demand imbalance, as the deal flow is relatively low compared with the amount of capital that strategic and financial acquirers are looking to put to use.

Many large corporations, in addition to aggressively acquiring assets in high-value markets, are simultaneously streamlining their portfolios and focusing on niche markets that drive higher profits. This trend is partly the result of the megadeals, as companies seek to divest assets to gain regulatory approval or to sell off noncore businesses and product segments that no longer fit the company post-acquisition. This divesting activity also is being driven by activist shareholders pushing management teams to unlock value trapped in overly complex business structures.

The surge in megadeals is affecting M&A activity in the middle-market as well. In an acquire-or-be-acquired environment, small to midsize companies are using M&A to compete with the scale and breadth of product offerings and customer service provided by their larger multinational competitors. For financial sponsors, robust cash reserves and access to low-cost financing should continue to drive high demand and strong valuations across the M&A market.

The prospect of rising interest rates, however, may cause some financial sponsors to put assets up for sale earlier in 2017 than would otherwise be the case.

**Trade and Tax Policy Could Shape Dealmaking in 2017**

Despite the continued tailwinds driving M&A activity, policy shifts regarding trade and taxes could significantly alter dealmaking—although it is too early to tell what the net effect will be. Headlined by ChemChina’s acquisition of Syngenta, Asian buyers accounted for 26% of all chemicals M&A by deal value in 2016. This figure could drop significantly in 2017, however, as the Chinese government reportedly is applying more regulatory scrutiny to outbound deals in an effort to reduce the amount of capital leaving the country. In the United States, President Donald Trump’s proposed trade policies may make it more difficult for foreign buyers to acquire U.S.-based companies.

Proposed tax and regulatory reforms under the Trump administration, on the other hand, could be very beneficial to domestic chemicals companies, giving some companies in the industry more cash with which to make acquisitions and making others more attractive acquisition targets. House GOP leadership has proposed using “border adjustment” (i.e., taxing imports and excluding exports) to make up for part of the revenue that would be lost by lowering the corporate tax rate from 35% to 20%. U.S.-based companies that are net exporters would benefit if this border adjustment is passed into law. The administration’s promises to rollback regulations would directly improve profitability for many chemicals companies.

To learn more about these and other trends that are shaping dealmaking activity in the chemicals industry, please do not hesitate to contact us.
Notable Chemicals Acquisitions in Q4 2016
In addition to a series headline-grabbing megadeals, Q4 2016 saw a high number of significant transactions across all market segments. This consolidation wave should lead to further M&A activity in the middle market in 2017, as companies look to remain competitive in an acquire-or-be-acquired environment.

($ in millions)

<table>
<thead>
<tr>
<th>Announced Date</th>
<th>Buyer Name/Target Name</th>
<th>Deal Value</th>
<th>Enterprise Value / Sales</th>
<th>EBITDA</th>
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<tbody>
<tr>
<td>12/22/16</td>
<td>Nippon Paint Holdings Co Ltd/Dunn-Edwards Corp</td>
<td>N/A</td>
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<td>12/20/16</td>
<td>Praxair Inc/Linde AG</td>
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<td>NMF</td>
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<td>12/19/16</td>
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<td>Platte River Equity LLC/Tiger-Sul Products LLC</td>
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<td>American Securities LLC/Chromaflo Technologies Corp</td>
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</table>

Source: Dealogic
Chemicals M&A Valuations
Valuations, on an EBITDA basis, surged to recent highs in 2016. Valuations should continue to be supported by an overall supply-and-demand imbalance, as the deal flow is relatively low compared with the amount of capital that strategic and financial acquirers are looking to put to use.

**EV/EBITDA**

[Graph showing EV/EBITDA values from Q1 '14 to Q4 '16 with Median: 10.9x]

Source: Dealogic

**EV/Revenue**

[Graph showing EV/Revenue values from Q1 '14 to Q3 '16 with Median: 1.29x]

Source: Dealogic

Chemicals M&A – Acquirer Location
In 2016, 43% of acquisitions in the chemicals industry were by foreign buyers, and much of this cross-border activity involved Asian acquirers. Inbound activity from Asian buyers could slow in 2017, however, as the Chinese government reportedly is applying more regulatory scrutiny to outbound deals in an effort to reduce the amount of capital leaving the country. In the United States, President Donald Trump’s proposed trade policies may make it more difficult for foreign buyers to acquire U.S.-based companies.

[Graph showing acquisitions from Q1 2014 to Q4 2016 with Cross-Border and Domestic categories]

Source: Dealogic
Commodity Prices
Relatively low prices for oil and other inputs have allowed chemicals companies to strengthen their balance sheets and improve margin profiles in recent years. These dynamics have made chemicals companies more attractive acquisition targets and given strategic buyers more cash that can be deployed for M&A.

Value of Shipments
Seasonally Adjusted (Millions of Dollars)

Activity Barometer
(2012 = 100 Index)

Source: Manufacturers' Shipments, Inventories, and Orders
Source: American Chemistry Council and Federal Reserve Board

Crude & Natural Gas
(USD/barrel)

Natural Rubber & Palm
(USD/pound)

Source: Bloomberg
Source: Foundation for Intl Business & Economic Research/Haver Analytics and Bloomberg

Ethylene & Propylene
(USD/pound)

Benzene & Styrene
(USD/Pound)

Source: Bloomberg
Source: Bloomberg and Haver

Plastics (PP, PS, PVC)
(USD/pound)

Plastics (HDPE, LDPE)
(USD/pound)

Source: Plastics News
Source: Plastics News
Drawing on our deep sector expertise and the strength of our relationships with buyers around the world, William Blair has built a leading chemicals banking franchise. Business owners turn to us for outstanding execution for their M&A and capital raising objectives.

Recent transactions include:

- Not Disclosed
  - MALET
  - a portfolio company of ICV Partners
  - has been acquired by
  - Advantage
  - a portfolio company of The Jordan Company

- Not Disclosed
  - KBC KODIA
  - has been acquired by
  - Elevance

- Not Disclosed
  - PLASKOLITE, INC.
  - has been acquired by
  - Charlesbank Capital Partners LLC

- Not Disclosed
  - Wisconsin Film & Bag
  - has been acquired by
  - Novolex

- $885,500,000
  - UNIVAR
  - Initial Public Offering

- $225,000,000
  - Performance Fibers
  - has divested its Asian Operations and Brand Name to
  - Indorama

- €83,000,000
  - VETRINERMACI
  - has been acquired by
  - Ferro

- Not Disclosed
  - FRAMO
  - has been acquired by
  - VanDeMark

- $795,000,000
  - Old World Chemicals
  - A division of Old World Industries, Inc. (dba PSL)
  - has been acquired by
  - Indorama Ventures

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Drawing on the collective intellectual capital and deep sector expertise of a global team that reaches across more than 20 cities on five 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 2012 to 2016, the team advised on more than $230 billion in completed transaction volume.