

Chemical M&A down but not out

Activity is poised for a rebound in 2013 as the pipeline fills up and confidence about the US and China improves. But valuations and dollar volume will remain well off the peak

Chemical
M&A down
but not out



PETER YOUNG YOUNG & PARTNERS

Although knowing and running your businesses well is the most important task for senior management, taking strategic actions with the right timing and being an adept financial engineer also has become an important part of the job.

Up through last summer, most investment bankers considered the chemical industry merger and acquisition (M&A) market “healthy” and “robust” with “no indication of valuations slipping yet”.

Given the substantial excess cash balances of chemical companies, the pressure to grow, and the availability of acquisition financing at very low rates, it was plausible that the M&A market was strong and that one could sell businesses easily and for peak valuations.

Based on that view, many pursued divestitures that did not achieve the results that they were promised or expected.

UNCONVENTIONAL WISDOM

However, the truth has been quite the opposite. The reality was that the chemical M&A market peaked much earlier in the second

quarter of 2011, began to slide in the fall of 2011, and fell precipitously in early 2012. Even the pipeline of deals announced but not closed shrank dramatically.

We were quite aware of this and shared this view with our clients and ICIS Chemical Business readers in December 2011, writing at the time: “As strong as the M&A activity has been for the first three quarters of the year, we believe that the chemical M&A market has peaked both in terms of numbers of deals and valuations. There are clear signs of slowing M&A volume as the number of deals has slipped each quarter: from 27 in the first quarter, to 18 in the second quarter, and now 16 in the third quarter. The pipeline is also dwindling.”

What happened? Although the M&A cycle was part of the picture, the key driver was the large number of uncertainties facing the global economy that affected the thinking of industry executives – the European economic and financial crises, the elections and fiscal cliff in the US, and the signs of possible slowing of the Chinese economy.

If only one or two of these had been factors, the slowdown might have been more modest. The reality was that CEOs were concerned

There will be a partial recovery of M&A market volume to around \$40bn-50bn

PETER YOUNG

President and managing director, Young & Partners

that if they did acquisitions of any significant size, they could have become a disaster if one or more of the uncertainties (all of which are outside of their control) became a negative reality and caused earnings or cash flows of the acquired business to plunge.

2012 DOLLAR VOLUME PLUNGED

For that reason, worldwide chemical M&A in dollar terms in 2012 was only \$22bn (€17bn) in completed deals, dramatically less than the \$82bn completed in 2011.

This major slowdown in dollar terms, a 73% drop, was the result of both a reduced number of deals and very few large deals. There were only seven deals over \$1bn in value completed in 2012 compared with 17 for all of 2011. The number of deals alone fell by 23%.

There was also a pronounced softening of the average valuation multiples, particularly in specialty chemicals. Valuations fell the most for average and weaker businesses and only modestly for high quality businesses.

There are also a few side observations. The Asia/Rest of World category was the most active with 39% of the total number of deals completed. The overall increase in Asia/Rest of World activity over the past few years has been astonishing compared to just a few years ago. That region has led in four of the last five years, and tied for the lead in the fifth.

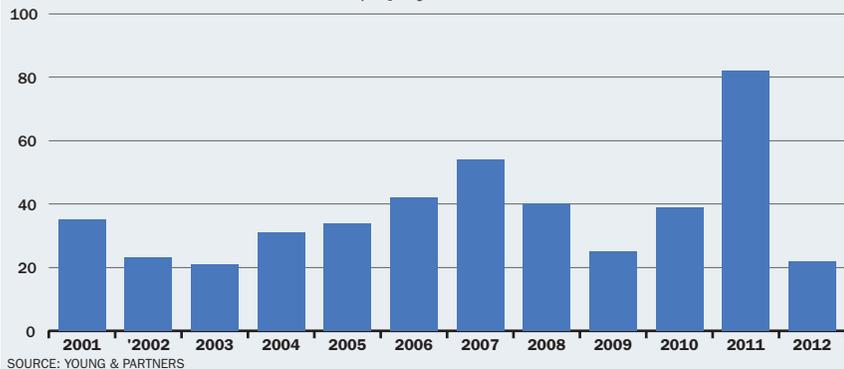
This is just a reflection of the growing importance of Asia/Rest of World in chemicals and the gradual maturing of the emerging market chemical companies.

FINANCIAL BUYERS

How about the financial buyers? Financial buyers revived modestly and accounted for 14% of the number of deals in 2012, well off

ACQUISITIONS OF WORLDWIDE CHEMICAL COMPANIES

Dollar volume of disclosed deals in \$bn, equity value



SOURCE: YOUNG & PARTNERS

their normal 20-25% share of the number of deals. On the other side of the ledger, financial buyers have been heavy sellers of chemical businesses now for the last three years and this selling activity continued in 2012.

OUTLOOK

What will the future bring? Young & Partners believes there will be a partial recovery of the chemical M&A market volume from \$22bn

last year, to a stronger, but not yet robust level in the \$40bn-50bn range.

This is evidenced by the growing pipeline of deals that have been announced, but have not closed.

Although a lot of uncertainty remains in the global economy, there are signs that the Chinese economy is growing solidly and we have survived at least part of the US fiscal cliff threat.

Valuations, however, will continue to be

weak for most businesses until there is a stronger level of buyer interest, but will stay solidly high for high quality businesses being sold.

IMPLICATIONS

So what are the implications for chemical executives and private equity investors?

For sellers of businesses the news is positive if the business being sold is of high quality since valuations are holding up for quality businesses.

Although the market is still open for weaker businesses, the valuations are lower and will continue to be disappointing for sellers. In many cases, the deals will not go through at all.

For these situations, the sellers face the decision whether to sell now at a lower valuation or to wait for the next revival of the M&A market, which could take some time to develop.

For buyers, the valuations are better, but not necessarily for the highest quality businesses. ■



Peter Young is president and managing director of Young & Partners, an international chemical and life science investment banking firm headquartered in New York. He has more than 26 years of experience in chemical and life science investment banking.



Chemicals Energy Fertilizers
Prices | News | Analysis | Consulting

Your strategic partner for identifying medium-to-long term business opportunities

ICIS offers analysis and consulting services for the global petrochemical, energy and refining industries to help you navigate the complex global markets.

Analysis services

ICIS has a range of data services and market insight reports which give you multiple views of the marketplace, enabling you to steer your business forward with skill and confidence.

- **Supply & Demand (S&D) database service** – fully reconciled data across 160 countries and 100 markets, with historical data and projections from 1978 – 2030
- **Annual Studies** – global studies, as well as dedicated reports on domestic China markets, which provide detailed expert analysis and forecast data on supply, demand, production and capacity for specific markets

Global consultancy services

ICIS provides bespoke advisory services to support your individual business goals - from expert research analysis to strategic consulting services that will guide you through every phase of your planned investments or operational expansions.

To find out more about these services, visit www.icis.com/services or email enquiry@icis.com