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Merger would lead to split

Dow/DuPont commodities businesses a good fit, while combined agriculture assets would compete better with rivals

The possible merger between Dow Chemical and DuPont would lead to a three-way split if the deal goes ahead, analysts said on 9 December.

That day the *Wall Street Journal* reported that Dow and DuPont are in advanced merger talks with a public announcement expected within a few days. The merger would create a business to rival BASF in size with \$92bn (€84bn) in sales based on 2014 figures.

Chemical equity analysts at Bernstein expect the merged company would then split into three independent entities: agriculture, specialty chemicals and commodities.

“We see strong synergies in the deal, in the range of \$2.3bn - \$2.7bn, excluding positive effects of eliminating transfer pricing discounting,” the analysts said.

The merger would likely be followed by a split of the combined company into three independent entities, Bernstein said, namely a “New Pioneer” – an Agriculture company, which would be No 2 in seeds and No 3 in crop protection: a “New DuPont”, which would be the largest specialty chemicals company in North America, and a “New Dow”: a commodity company similar to LyondellBasell, but with polyurethanes (PUs) instead of propylene oxide (PO) and refining.

The merger resolves several problems, said Laurence Alexander, equity analyst at the investment bank Jefferies. He made his comments in a research note.

The combined agricultural business would better compete with Monsanto and Syngenta, if the latter two were ever to merge, Alexander said. If Monsanto cannot reach a deal with Syngenta, then the Dow-DuPont combination could make its own offer for Syngenta from a stronger position in the next few years.

For the commodities business, DuPont’s ethylene derivatives would fit nicely with Dow’s plants, Alexander said. DuPont could also help Dow bring value to any future expansions at its Sadara joint-venture project in Saudi Arabia.

The specialty-chemicals business would have a strong portfolio for infrastructure and safety markets, he said. It would be a market leader in photovoltaic materials.

Integrating and then splitting the businesses could take three to five years, Alexander said.

Other chemical companies could react to the merger in several ways, he said.

It would pressure Syngenta to step in quickly if it wishes to acquire DuPont, Alexander said. It would also pressure Monsanto to revisit its failed offer to acquire Syngenta. Smaller specialty-chemical companies may consider acquiring the individual pieces of the merged Dow and DuPont company, Alexander said. They could also strike deals among themselves so they could gain scale against the larger Dow-DuPont.

Both companies declined to comment about the reports. However, Dow and DuPont had each said they were pursuing agriculture deals. The talks started after Monsanto unsuccessfully sought to acquire Syngenta.

SYNERGIES, CHALLENGES

A possible merger will produce significant synergies in their agriculture businesses, but fewer among the specialty chemicals and commodity businesses at Dow Chemical and DuPont, an investment banker said on 9 December.

Among the three entities, the agriculture businesses would have the most overlap, causing it to receive the most regulatory scrutiny, said Peter Young, president of the investment banking firm Young & Partners.

The way anti-trust regulators



“One of the challenges will be the synergy story for the deal overall”

PETER YOUNG
President, Young & Partners

look at agriculture deals is generally quite complicated, he said. However, he indicated that there will be a path to approval that will allow the combined agriculture business to benefit from meaningful synergies.

Young sees fewer cost synergies among the specialty and commodity businesses, in part, because they are not that similar. Also, DuPont had moved significantly away from chemicals when it spun off the Chemours business earlier this year.

The modest overlap in commodity and specialty chemicals by definition will help the merger go through the antitrust review. But the other side of the coin is that there will be fewer opportunities to enhance profits through synergies, beyond the general, administrative and other overhead costs.

“One of the challenges will be the synergy story for the deal overall,” Young said.

There will be some synergies outside of agriculture in specific areas. Dow and DuPont, in certain areas, sell different products to the same customers. For exam-

ple, sales representatives could sell Dow’s polyethylene (PE) resins and DuPont’s packaging adhesives to the same customers. As a result, the combined businesses could realise some market-selling synergies by merging.

However, sharing similar customers does not automatically create synergies, Young said. “You are going to have to look into the details to see from a customer-market point view if there is a real benefit,” he said.

Young added: “There will also be a number of regulatory and tax issues that will have to be examined and dealt with if the proposed merger and subsequent break-up into three is, in fact, what the two parties are contemplating.

“This will include the structural aspects of the many joint ventures and partially owned companies of Dow and DuPont with others, as well as the impact that other previous transactions, such as the divestitures by Dow and the tax free spin-off of Chemours by DuPont, will have,” Young said.

The possible merger likely evolved from talks about the companies’ agricultural businesses, he said. Both companies had confirmed that they were considering deals for those businesses. “It is my guess that the discussions started with meetings about alternatives between the two companies. A discussion of the merger of the two companies would probably not have happened if the change in the CEO of DuPont had not happened,” he said.

Another key factor was DuPont’s new CEO Edward Breen, who replaced Ellen Kullman in October, had experience breaking up a conglomerate when he ran security systems company Tyco International.

“That created the combination of things that allowed this kind of conversation to happen,” Young said. ■