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Adhesives and sealants M&A keeping a strong pace

By Kyle Brown



Andy Hinz, managing director for Grace Matthews Inc.

MILWAUKEE—Mergers and acquisitions likely will continue at a rapid pace in the adhesives and sealants industry for the foreseeable future, according to Andy Hinz, managing director for Grace Matthews Inc.

Most of the deals are bolt-on acquisitions, Hinz said, generally between \$20 million to \$200 million in enterprise value. At that level, acquisitions tend to be lower risk.

"Strategic buyers historically have had a generally stronger appetite for bolt-on deals that can be very valuable to them, but also can carry somewhat lower risk, just due to their size," he said.

Another major reason that much of the action centers on that price range is the overall complexion of the market, as assets between \$100 million and \$500 million have

become scarcer, he said.

"You have the large strategic players, approaching \$1 billion in revenue and above. Then you have a large number of smaller companies generally under \$100 million in revenue," Hinz said. "But really there are not very many companies remaining in that middle-size range."

Hinz said the market is likely to continue to consolidate, and many companies left in the middle-size range will be sold. As that happens, it tends to drive up the prices of those companies in that market as they attract a lot of strategic buyer attention.

"It continues to be a strong seller's market, and owners of high quality companies tend to have the upper hand when selling their business," Hinz said. "Because of that, high quality companies can often expect interest from multiple strategic parties, and more broadly from private equity buyers as well. In today's market, sellers often have the ability to choose their own destiny to a greater degree than in the past."

In this market, strategic buyers should be decisive and ready to pay high prices for acquisitions, Hinz said.

"The simple advice we give to companies is that if you want to be a successful acquirer, you have to play by today's rules. You have to be prepared to pay a high value, and you have to be prepared to move quickly," Hinz said. "In most cases, you have to be prepared to participate in an auction process."

Hinz said he expects the market to continue at a high level of activity into the future.

"It's probably fair to say we are near or at a cyclical peak in M&A," he said. "But that's not to say a market correction is imminent. We believe M&A activity could remain elevated for some time."

One reason for that level of activity is the health of the overall economy, as the U.S. and most other major economies seem to be healthy right now, he said. The lending environment also is encouraging both in terms of interest rates and the banks' appetite to continue to lend money to support deals. Though interest rates are starting to creep up, they're not yet at a level that could significantly dampen M&A, though that could be an issue in upcoming years.

U.S. tax reform also will likely be supportive of M&A this year and beyond, Hinz said.

"I don't necessarily think it's going to be a big push, but I do think it could help support, or even possibly drive up, valuations a little bit, and also support some incremental activity," he said. "Acquirers can get some pretty attractive tax breaks in the first year of their acquisition."

Hinz said private equity groups have a huge desire to acquire companies in adhesives and sealants, and in the broader specialty chemicals market, but that is not necessarily translating into completed transactions. Many private equity groups struggle to pay the valuation that strategic buyers are more willing to pay for a business.

"A good example of that, for high-quality companies today, it's not uncommon for us to see double-digit multiples, or a buyer paying 10 times EBITDA or more," Hinz said. "Private equity buyers just tend to struggle to get to that level of valuation on a business."

Valuations continue to remain high, encouraging some adhesive and sealant company owners who normally would not be planning to sell to reconsider, Hinz said.

"I think what's happening, is the values that are being contemplated are so high that they're getting sellers who historically may not have ever considered selling their business to think much harder about the possibility," he said.

An aging population of adhesive and sealant company owners also is a fairly significant driver in the level of activity, as private company owners are getting ready to retire without having a natural transition in place with another generation, Hinz said.

He doesn't see signs of company valuation amounts coming down significantly anytime soon, as the current market backdrop supports high values into the foreseeable future. But it does add a level of risk to acquirers who are paying high prices.

"There's certainly going to be less margin of error with how they operate their acquired businesses going forward," he said. "Particularly in the first couple of years, there's zero tolerance when you're paying a double-digit multiple for a company."

Grace Matthews is a middle-market investment bank that provides M&A and corporate finance advisory services for chemical companies.

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