

CHEMICAL INSIGHTS



Conversations With The Chemical M&A Industry: What Buyers/Sellers Are Saying

What just happened, and where are we going?

Providing an update on M&A trends in any industry without acknowledging the impact that the ongoing, worldwide COVID-19 pandemic has had in the past few months would be impossible. We do not yet know the full extent of the pandemic's impact on the chemicals industry. However, based on conversations within our industry network, we can explain what we've seen unfold, what we've heard in conversations from various parties in chemicals M&A, and what we expect to drive deal activity in the near term.

Despite the turmoil of the past three months, Grace Matthews has remained active, as three transactions we have advised on have closed between April 1 and the release of this newsletter. The common thread among each of these transactions: a strong strategic fit between acquirer and target.

During times like these, Grace Matthews' industry focus and expertise are valuable to our clients. We have seen firsthand that complementary acquisitions bolstering a strategic buyer's presence and/or expanding its core operations will continue to cross the finish line (note that "strategic" can also mean a private equity-backed, or "PE-backed," company within a given sector). And we have also heard numerous private equity funds pointing to the now-hesitant leverage markets, typically a key driver of PE valuations, as a primary reason that PE acquisitions of new chemicals platforms have all but ceased for the time being. With 100% of our time focused on the chemicals and materials industry, the Grace Matthews team has built a strong network of strategic buyers active throughout the space, private equity firms with experience or planned investments in the sector, and privately-held business owners. While our conversations are most often face-to-face, we've used the time "grounded" in our homes to maintain dialogue with our key contacts throughout the industry.

What We've Heard

Our vantage point has offered some insights into how companies and investors in the chemicals industry have responded to the pandemic, how acquirers have remained engaged in deals that began pre-COVID-19, and how there remains a

middle ground between buyers and sellers to complete deals in the near-term, even though the only certainty looking ahead is the constant uncertainty about the state of the world. Notable highlights from these conversations follow.

Strategics

Common themes from conversations with strategics in the chemicals space have been a focus on conserving cash and strengthening balance sheets to ensure flexibility during uncertainty, a desire to continue M&A efforts, and ongoing business unit portfolio reviews with an eye towards prioritizing “core” businesses (which may also lead to increased carve-out activity over the next 6-12 months).

- Cash conservation and balance sheet improvement: As COVID-19 unfolded, strategics quickly focused internally on conserving cash in order to strengthen their balance sheets, preserve liquidity, and position their companies to weather the pandemic that could potentially last for a long period of time.
- Desire (and a need!) to continue M&A efforts: In our conversations with various heads of M&A and corporate development teams, we have been told that, even despite the pandemic-related uncertainty, M&A remains a priority for core business segments and/or to support high-priority internal initiatives. Obstacles that strategics expect or are being faced with include: the willingness of sellers to continue conversations during COVID-19 as well as the potential for an emerging gap between sellers’ valuation expectations (anchored by pre-COVID-19 market multiples) and buyers’ willingness to pay in an uncertain and rapidly changing environment. We sense strategics recognize that continuing growth via M&A is a necessity, not a luxury—good or bad economy, strategics must grow in order to justify the “strategic premium” trading multiples (for public companies) or valuation (for large private companies) they are seeking. Similar to 9/11 and the Great Recession of 2008-2010, strategics likely now have a period of time during which they are not going to be graded on their income statement, and the companies that emphasize M&A efforts now are likely to emerge from the pandemic far better positioned than those that do not.
- Prioritizing core (and de-prioritizing non-core) businesses: Internal resources have become more scarce, perhaps due to furloughs or even job cuts, and strategics have indicated they are funneling resources to support their highest priority businesses, often at the expense of non-core segments. A side effect of this means that the businesses already deemed non-core may become even more clear candidates for carve-out processes, as these businesses likely will be valuable within a different organization. We see this as a potential driver of M&A activity in the medium-term.

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In summary, as strategics achieve internal stability and adjust to the uncertain near-term outlook driven by COVID-19, we expect those capable of engaging in M&A to deem it a necessity, not simply a goal or priority, in order to maintain premium, growth valuations. During a time when organic growth is unlikely and poor financial performance may get a “free pass,” acquisitions become the single best avenue to achieve growth. Furthermore, we anticipate a wave of carve-out businesses/assets to come to market as companies sharpen their focus on their highest-priority products and markets.

Private Equity Investors

Common themes from private equity firms with holdings and experience in the space have centered on an initial “triage” phase to assess near-term outlook for portfolio companies, incoming deal flow declining by 90-95%+ relative to pre-COVID-19 levels, a shift to ‘add-ons’ for platforms in the near-term, and a very cautious approach from lenders evaluating new debt placements.

- March - April 2020 “Triage” mode: Funds with existing portfolio companies in the industry (and likely every industry) indicated that resources in March and April were focused almost entirely on evaluating every portfolio company’s position and near-term outlook. Unlike many industries, we saw that companies in the chemicals & materials industry were typically deemed “essential” businesses in North America and therefore had operations continue, at least to some extent. Many indicated they drew as much capital as possible to prepare for the uncertainty, typically via existing lines of credit.
- Evaporation of incoming deal flow: Funds indicated that inbound deal flow effectively declined to zero, which suggests very few processes were launched in the March-May 2020 timeframe. Note that this data point would not be a proxy for any proprietary, non-represented deals these funds are pursuing and would not pick up any strategic-focused processes that did not involve PE funds.
- Focus on ‘add-ons’: M&A activity does continue at the PE-level, though, as many funds and their portfolio companies indicated ongoing conversations with potential add-on acquisitions for existing platforms. Add-on acquisitions enable a PE-backed company to effectively function as a strategic buyer and can often be financed with the company’s underlying balance

sheet (using cash on hand or leveraging existing credit facilities). PE funds suggested a preference for add-on acquisitions that were relatively smaller in size (compared to the size of the platform) as these deals tend to be less risky.

- Challenging leverage environment: Unsurprisingly, the debt world was also turned upside-down, and funds indicated that securing financing for new platforms has become increasingly challenging due to lenders offering more conservative leverage and less attractive pricing/terms compared to pre-COVID levels. In other words, the financing pendulum has swung from a PE/buyer's market to a lender's market in terms of leverage and availability.

In short, PE firms in the chemicals industry will continue to evaluate attractive businesses that come to the market as platforms, but valuations will likely be hampered by conservative leverage levels from lenders. To compete with the strategics that may have interest, we expect PE funds will need to 'over-equitize' deals to support a higher valuation, or find other areas in which they can be more competitive, such as legal terms or speed to closing. Should there be a strong fit between an existing platform and an add-on, we expect funds will be able to behave more like strategics and overlook near-term uncertainty to acquire these targets. Make no mistake: PE will continue to place capital. Funds are graded on a curve, relative to their peers, and not on absolute returns; moreover, PE investors themselves are financially rewarded for completing acquisitions. We simply believe these next couple quarters are likely to be far more challenging for PE platform acquisitions than any point in the previous several years.



Privately Held Businesses

Common themes from privately held businesses have centered around repositioning assets to serve markets (such as sanitary/anti-microbial) that are in high demand, taking a patient approach to outlast the uncertainty, fielding continued inbound inquiries from strategics, and for some businesses, developing a newfound appetite for M&A to potentially acquire select targets. Moreover, we sense that some, but not all, owners may be recalibrating the definition of "value" in a possible sale process.

- Repositioning of assets to meet high-growth markets: Many owners have indicated they were quickly able to shift production to meet the demands for hand sanitizer, other anti-microbial equipment, and other segments of the industry that saw exponential growth related to COVID-19 and consumer reactions.
- Patience: Many owners are taking a wait-and-see approach and focusing on maintaining ongoing operations. Without public shareholders to answer to or a ticking-clock investment horizon resulting from a traditional PE ownership period, private companies are taking advantage of the luxury of flexibility and patience.
- Inbound inquiries from strategics: Even in the face of the pandemic, some owners have indicated strategics continue to express interest in a partnership or acquisition. Multiple business owners have told us that these solicitations even come with a stated willingness to overlook pandemic-related underperformance, though we do not yet have the data to tell you how many times companies have held true to such a statement.
- Appetite to become an acquirer: Multiple companies we have spoken to have indicated a first-time desire to potentially acquire competitors or add-on businesses that would complement their existing presence. In normal times, privately held businesses struggle to compete from an M&A perspective; over the next several months, we sense privately held businesses may have the "intangibles" that resonate with sellers.
- Recalibrating what "value" means: We recognize that not every private business owner wants to sell his or her business. Yet, for those that considered it, particularly in the past decade of high-growth, private business owners that chose not to sell often perceived a gap between what their businesses were "worth" and what value they could achieve in a sale (typically, this came down to a single number: purchase price). Now, having emerged from a multiple-week lockdown into a still-ongoing pandemic, business owners have intimated "value" may have a new meaning. Purchase price in an exit will always be important, but other factors, such as improved lifestyle changes, more favorable fit for employees in a given buyer, or a faster transition out post-transaction, are being mentioned. For some, what was a narrow definition of "value" is likely to broaden.

Many privately held businesses indicated their flexibility and responsiveness were tools used to effectively make their businesses better during this time, while others have indicated the steep decline suffered in the past three months will require a long-term, steady recovery to reach previous activity levels. From an M&A perspective, while we expect some private business owners to become first-time buyers in the near-term, we still expect certain private business owners may sell in the near and medium-term, particularly those with strategics knocking on their door.

Where We're Headed

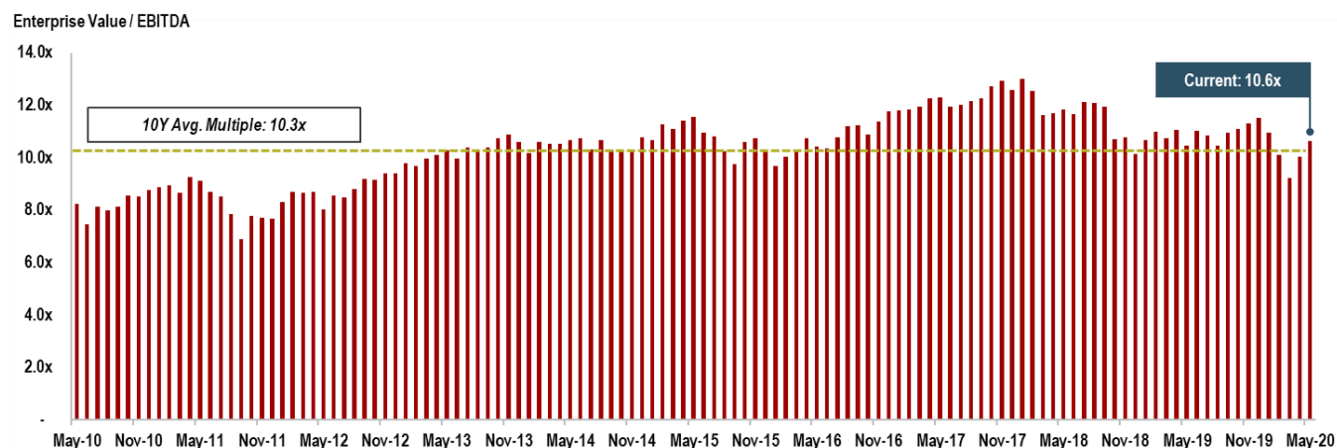
As we stated before, the only certainty we expect in the near-term is constant uncertainty as the world continues to develop a response and go-forward plan to overcome the pandemic.

From an M&A perspective, we remain confident that deals will continue to be done, though we are unlikely to see M&A activity rebound significantly in the near-term and reach overall deal levels that mirror recent years. We expect to see continued interest from buyers, ranging from strategics with cash to deploy and resources to evaluate select opportunities to PE funds seeking add-ons for existing portfolio companies, as well as well-capitalized privately held businesses that may use this as an opportunity to engage in M&A conversations. Right now, most strategics will need M&A to achieve growth. For PE funds, M&A is their living-capital needs to continue being deployed.

From a potential sellers' perspective, the businesses that have continued to perform (or perhaps even outperformed due to increased demand in end markets served) and those that see minimal impact (quickly becoming referred to as "COVID-blips") will be well positioned to engage in sale process discussions and will likely have the best probability for a successful outcome. Finally, as strategics adjust internally and conduct internal portfolio reviews, we expect to see more carve-out opportunities that will serve dual purposes – allowing sellers to focus more on core businesses and providing buyers an opportunity to grow inorganically.

Despite the near-term uncertainty, we expect certain owners (whether private, strategic, or PE-backed) will still want to sell. When considering a sale, we believe that competitive dynamics in a transaction process are more important now than ever. The rationale for having multiple people at the table in a competitive process is that buyers can change terms, lose interest, and/or have resource constraints that force them to pause acquisitions. A well-run process, whether a broad auction or targeted towards the highest potential buyers, can achieve this competitive tension and force buyers to compete on the variables of speed, certainty, terms, and valuation. Moreover, COVID-19 has shown that certain aspects of a sale process that were traditionally done in person, such as management presentations and/or diligence meetings, have shifted to "virtual" meetings, which has provided the necessary flexibility for processes to move ahead during this pandemic.

Grace Matthews Chemical Index: Enterprise Value / EBITDA (Last 10 Years)



Source: Grace Matthews and Capital IQ

The *Grace Matthews Chemical Index* tracks the Enterprise Value / EBITDA ratios ("EV/EBITDA multiples" or "EBITDA multiples") of 100 publicly traded chemical companies that span multiple sub-sectors and geographies. The Index aggregates the latest reported financial data and stock prices, and tracks valuation trends and operating metrics across different industry sectors. Index averages are equally weighted, as opposed to weighting by market capitalization.

Select 2020 Industry Transactions

Transaction values in \$US millions					
Closed Date	Acquirer / Target	Target Description	Enterprise Value	EV / Sales*	EV / EBITDA*
Jun-20	The International Group / Rheogistics	Manufactures hydrocarbon wax-based additives and lubricant systems for rigid PVC			
Jun-20	Sika / Modern Waterproofing Group	Manufactures self-adhesive waterproofing membranes, synthetic roofing, and thermal insulation foams (Egypt)	\$33	1.1x	6.1x
Jun-20	H.I.G. Capital / USALCO	Manufactures aluminum-based chemicals			
Jun-20	Altivia / KMCO (Ethoxylation manufacturing and substantially all other assets)	Provides specialty chemical manufacturing and custom and toll processing products			
May-20	SK Global Chemical / Arkema (functional polyolefins business)	Manufacturing ethylene copolymers and terpolymers for the food packaging, cable, electronics, and coatings markets (France)	\$369	1.3x	
May-20	Givaudan / Indena (Cosmetics business)	Manufactures cosmetic ingredients (Italy)			
May-20	Huntsman Corporation / Emerald Performance Materials (CVC Thermoset Specialties business)	Manufactures specialty epoxy resins	\$300	2.6x	10.0x
Apr-20	Bodycote / Ellison Surface Technology	Manufactures thermal spray coatings and performance coating solutions	\$200	3.4x	16.7x
Apr-20	Synthomer / OMNOVA Solutions	Provides specialty solutions and performance materials for various commercial, industrial, and residential end uses	\$752	1.0x	10.6x
Apr-20	Elkem / Guangdong Polysil Technology	Manufactures silicone rubber (China)	\$135		
Apr-20	Tank Holdings / Tingle, Brown & Co. (Meese business)	Rotomolds custom and proprietary plastic products			
Mar-20	DuBois Chemicals / Milacron (Cimcool business)	Manufactures metalworking fluids	\$250		
Mar-20	The Riverside Company / National Flavors	Manufactures flavoring materials			
Mar-20	Daelim / Kraton Polymers (Cariflex business unit)	Manufactures isoprene rubber latex	\$530		13.6x
Mar-20	PPG / Alpha Coatings Technologies	Produces powder coatings for industrial applications			
Feb-20	Altana / Schmid Rhyner	Manufactures primers, overprint coatings, and laminating adhesives (Switzerland)			
Feb-20	Huntsman Corporation / Icyne-Lapolla	Manufactures spray polyurethane foam insulation products (Canada)	\$346	1.5x	10.0x
Feb-20	One Rock Capital Partners / Innophos Holdings	Produces specialty ingredients with applications in food, health, nutrition, and industrial markets	\$1,004	1.3x	8.6x
Feb-20	PPG / Industria Chimica Reggiana	Manufactures coatings and composites (Italy)			
Jan-20	Domo Chemicals / Solvay (Performance Chemicals business)	Produces engineering plastics (France)	\$557		
Jan-20	Milliken & Company / Borchers USA	Manufactures additives for colorants, paints, and printing inks			
Jan-20	Fuchs Petrolub / Nye Lubricants	Manufactures synthetic lubricants, thermal coupling compounds, and index-matching optical gels			
Jan-20	Indorama / Huntsman Corp. (integrated oxides and derivatives businesses)	Produces oxides and derivatives	\$2,006	1.0x	5.7x
Jan-20	Cornerstone Chemical (Littlejohn & Co) / Chemours (methylamine business)	Manufactures methylamines			

Grace Matthews: Select Chemicals and Materials Transactions

 <p>has been acquired by</p>  <p>THE INTERNATIONAL GROUP, INC.</p>	 <p>a wholly owned subsidiary of Tingue, Brown & Co. has been acquired by Olympus Partners' portfolio company</p>  <p>TANK HOLDING</p>	 <p>has sold its methylamines business to Belle Chemical Company, an affiliate of</p>  <p>Cornerstone Chemical Company</p>	 <p>has been acquired by</p>  <p>Italmatch Chemicals</p>
 <p>has been acquired by Arsenal Capital Partners' portfolio company</p>  <p>Meridian Adhesives Group</p>	 <p>has sold its Specialty Fluids business to</p>  <p>SINOMINE</p>	 <p>has divested its surfactants, thickeners and dispersants business to</p> <p>Tiarco, LLC</p> <p>a subsidiary of</p>  <p>Textile Rubber & Chemical Co., Inc.</p>	 <p>has been acquired by</p>  <p>VANSEAL</p>  <p>BLUEPOINT Capital Partners</p>
 <p>has been acquired by</p>  <p>Yushiro</p>	 <p>has been acquired by</p>  <p>GOLDEN GATE CAPITAL</p>	 <p>has been recapitalized by</p>  <p>PLATTE RIVER EQUITY</p>	 <p>has been acquired by The Jordan Company's portfolio company</p>  <p>borchers</p>
 <p>and its subsidiaries</p>  <p>GENESIS CUSTOM CHEMICAL BLENDING</p>  <p>PANHANDLE EXPRESS ENERGY SERVICES LLC</p> <p>have been recapitalized by a chemicals-focused investor group</p>	 <p>AAKASH CHEMICALS</p> <p>THE SKY IS THE LIMIT</p> <p>has been recapitalized by</p>  <p>CENTEROAK PARTNERS</p>	 <p>has been acquired by</p>  <p>GABRIEL</p>	 <p>has sold its subsidiary CiDRA Chemical Management Inc. (CCMI) to</p>  <p>Buckman</p>
 <p>has sold its Automated Fueling Stations business</p>  <p>QUICK FUEL</p> <p>to</p>  <p>FLYERS Energy</p>	 <p>has sold its global Polyolefin Catalysts business to</p>  <p>GRACE</p>	 <p>APPLIED adhesives</p> <p>has been acquired by</p>  <p>GHJ&M GOLDNER HAWN JOHNSON MORRISON</p>	 <p>has sold its pressurized polyurethane foam adhesives business to</p>  <p>ICP</p>

Grace Matthews Clients Listed First

Grace Matthews Overview

Grace Matthews is recognized globally as a leader in transaction advisory services for manufacturers and distributors throughout the chemical and material value chain. Grace Matthews' clients include privately held businesses, private equity funds, and large, multinational corporations.

Grace Matthews' practice is global in scope, and focuses on several areas: sell-side transactions and divestitures for private companies, private equity holdings, and multinational corporations; buy-side work for large public companies, major multinationals, and sponsor-backed chemical platforms; leveraged transactions and recapitalizations, strategic advisory analysis, and transaction fairness opinions. Areas of expertise include:

- Adhesives, Sealants, Tapes
- Catalysts, Petrochemicals
- Construction Chemicals, Building Products
- Contract Manufacturing, Custom Synthesis
- Distribution, Equipment, Infrastructure
- Food Ingredients, Flavors, Fragrances
- High Purity, Electronic Chemicals
- Industrial Minerals, Inorganic Chemicals
- Intermediates, Industrial Chemicals
- Lubricants, Greases, Metalworking Fluids
- Oilfield & Water Treatment Chemicals
- Paints, Coatings, Inks
- Personal Care, Soaps, Medical Materials
- Plastics, Colorants, Additives
- Tolling, Private Label Products
- Additional Chemical Sectors

Grace Matthews is a privately held investment bank with successful chemical industry transactions dating back to the early 1990s. Grace Matthews principals have completed over 100 transactions involving global corporations. Our team approach is unique in investment banking, with a combination of extensive industrial, financial and M&A experience.

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Grace Matthews, Inc. (www.gracematthews.com) is an investment banking group providing merger, acquisition, and corporate finance advisory services for chemical companies both in the U.S. and internationally. Grace Matthews is global in scope and well known for its strong track record of success dating back to the early 1990s.

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