

# Chemicals Newsletter

March 2015

## Increased bonding in Chemicals market

### Overall M&A Activity

The global M&A market strengthened in 2014, although perhaps not quite hitting the heights that were hoped for at the start of the year. While the increase in the overall number of deals was modest (c. 6%), the average value of each deal increased significantly (for example, Q3 2014 average deal values were on average c.52% higher compared to the same period in 2013). Overall, Mergermarket's year-end analysis showed transaction activity totalling \$3.23 trillion, up 47% on 2013 and only 11.8% less than the 2007 peak.

### Private Equity returns to the Chemicals sector

Over the last 20 years Private Equity has taken an increasingly important role in the M&A market, and the Chemicals sector is no exception with PE accounting for 20% of all deals since 2000. Successful fund-raises and a scarcity of quality investment opportunities in previous years has created significant levels of 'dry powder' within the investment community. Current key dynamics include:

- Plentiful funding options mean 2015 transaction values and volumes are expected to approach levels last seen in 2006;
- A scarcity of mid-market assets (enterprises worth £25-£250m) is driving premium prices for available quality opportunities;
- Prevailing conditions for PE houses seeking to exit (a key consideration when buying) are favourable. In 2014 the volume of exits increased by 15% with the total value of exits increasing an impressive 67% against 2013 values.

PE firms are particularly attracted to the Chemicals sector due to the relative stability in demand for products compared to other more "fashion-dependent" sectors,

allowing cash generation even in periods of weaker economic performance. Comparatively high barriers to entry and fragmentation in some areas also increases the attractiveness of opportunities in this sector. Potential hurdles within the Chemicals sector for PE investment remain the overall maturity of the market and therefore the limited opportunities for explosive growth, the high levels of regulation and the need for ongoing investment.

### Increase in corporate activity will drive M&A in 2015

Driven by consolidation, a relative excess of cash-rich international corporate acquirers, increased funding availability and continued pricing pressure, 2015 is expected to see further growth in M&A activity.

Sentiment from within the M&A industry is broadly positive. According to a recent Private Equity Wire survey of European business executives:

- 66% (47% at end of 2013) of respondents expected European M&A activity to increase and 11% expected a "significant" increase (versus 1% in the prior year);
- A similar US survey of business executives revealed that 59% of respondents expected further strengthening of the M&A market to a greater or lesser extent.

The current wave of positive M&A activity varies compared to previous bull markets, such as 2007. Eight years ago, cash-rich companies were often purchasing companies to utilise trapped cash balances without a clear strategic rationale. Fast-forward to 2015 and, in general, corporate acquisitions appear far more considered and strategic with boards more willing to return cash to shareholders if high quality opportunities are not available.

## Chemicals - Positive Market Dynamics

The Chemicals sector is characterised by a number of trends supporting continued expansion and driven by new technologies and enhanced environmental standards. The total value of Chemicals M&A grew by 13% in 2014 and this increase is expected to gather pace in 2015 with a number of international trade buyers active.

Key trends and dynamics within the sector pointing towards increased levels of M&A include;

- Energy prices. Developments in non-conventional oil and gas markets in North America (i.e. fracking) and a lower oil price have driven reduced energy costs in a sector where these can comprise up to 75% of end product price, furthermore;
  - o Lower energy prices can free up money in customer R&D and capital budgets, allowing greater resources for new product development; and
  - o High level of “value-add” (actual or perceived) provided by more specialist chemical companies creates a relative price insensitivity despite lower input costs.
- Corporate restructuring. 73% of respondents to a January 2015 Mergermarket survey believe Oil & Gas M&A will increase as larger companies restructure and re-focus on core competences making available for purchase non-core, but potentially highly valuable assets.
- Weaker upstream companies may be vulnerable to acquisition approaches as their margins diminish, while downstream in the Chemicals sector, lower input costs may create margin opportunities.
- Legislative Advances. Tightening legislation and developing technology is driving investment

in new and ever more efficient products. For example within the fuels and automotive additive space; Ford, JLR and BMW have all announced increased investment in new “efficient” engine development programmes in the last two years driving demand for new lubricant additives and fuels; and

- Barriers to entry in areas such as Health & Safety and operations continue to increase the significant capital investment and operational and technical expertise required to enter the sector. This makes M&A the optimal, and in some cases, the only viable entry strategy. Criticality of delivering consistent product means even with investment there is a requirement for extended trial periods with customers and the securing of Health and Safety approvals.

The global Chemicals industry is increasingly moving East, in both production and demand. By 2030 it is anticipated that 66% of global chemical sales will be in Asia, with the region (in particular China) being the hotspot for Chemicals M&A in the medium-term. North American M&A activity is also expected to increase driven by falling energy costs and consolidation of product offerings in complementary areas.

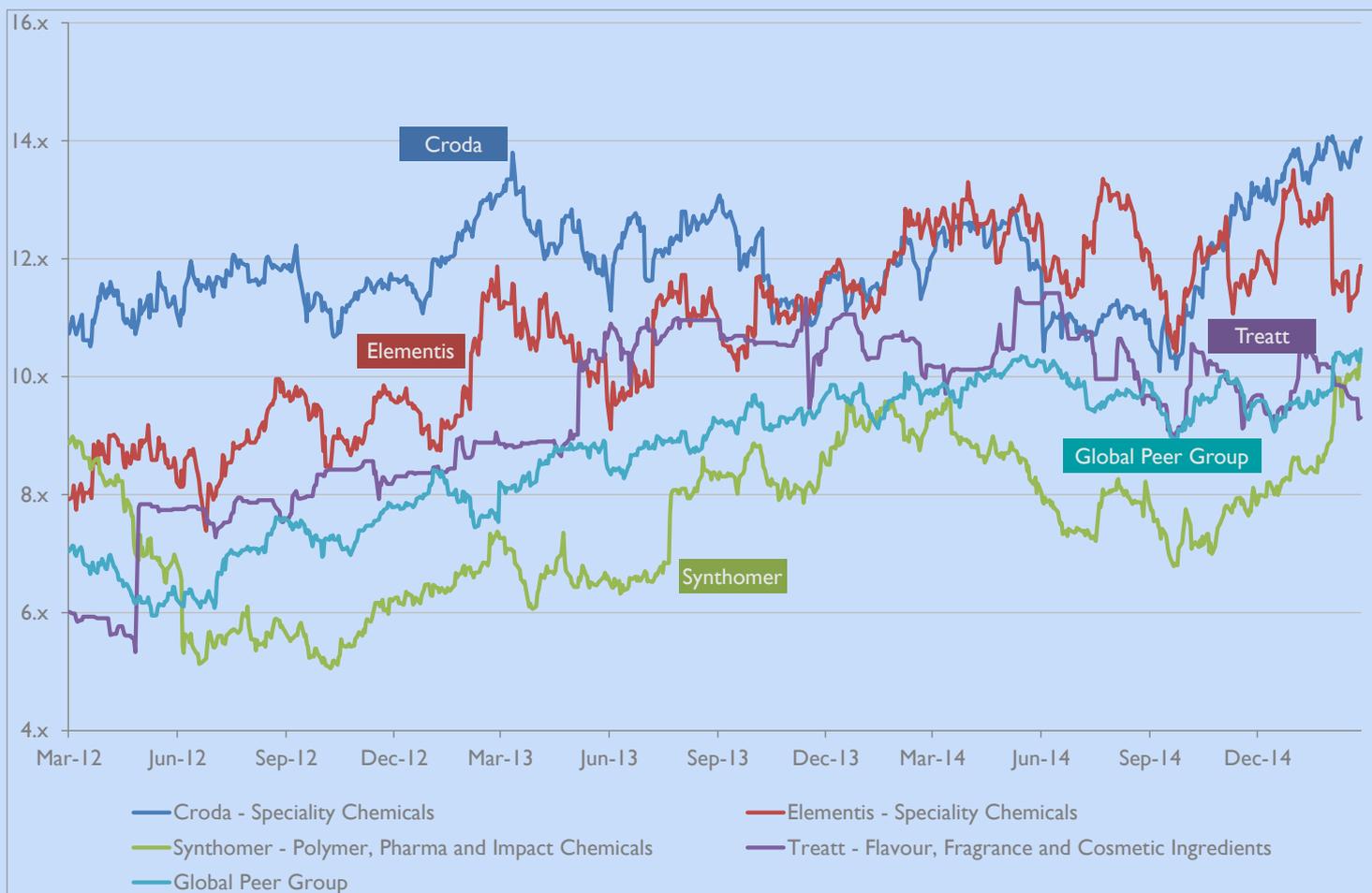
In Europe, the most successful Chemicals companies in the coming years are likely to be players able to leverage size and scale to remain competitive against Asian players, as well as smaller companies with high value-add products in technical niches and a focus on service and delivery first. Success can be found on a global scale via both innovation and a willingness to facilitate overseas growth via M&A outside of core markets.

In the UK, the population of publicly quoted chemicals companies spans a wide range of both products, including speciality chemicals, high performance solutions, additives, foams, specialist films, surface coatings; and end markets such as healthcare, construction, oil & gas, automotive, consumer etc.

Within our UK quoted peer group, the past year has seen mixed performance, with some companies improving their trading multiples (Croda and Synthomer) while others have diminished (Elementis and Treatt). It should be noted that the majority of improvement has been in the past six months and has in part been driven by lower energy prices and the expectation of the effect that this will have on margin achieved. In terms of trading multiple, Croda has consistently been the strongest performer in the UK peer group. Croda's performance is driven by a reputation for innovation, a niche at the top-end of its market and a diversified base of end customers.

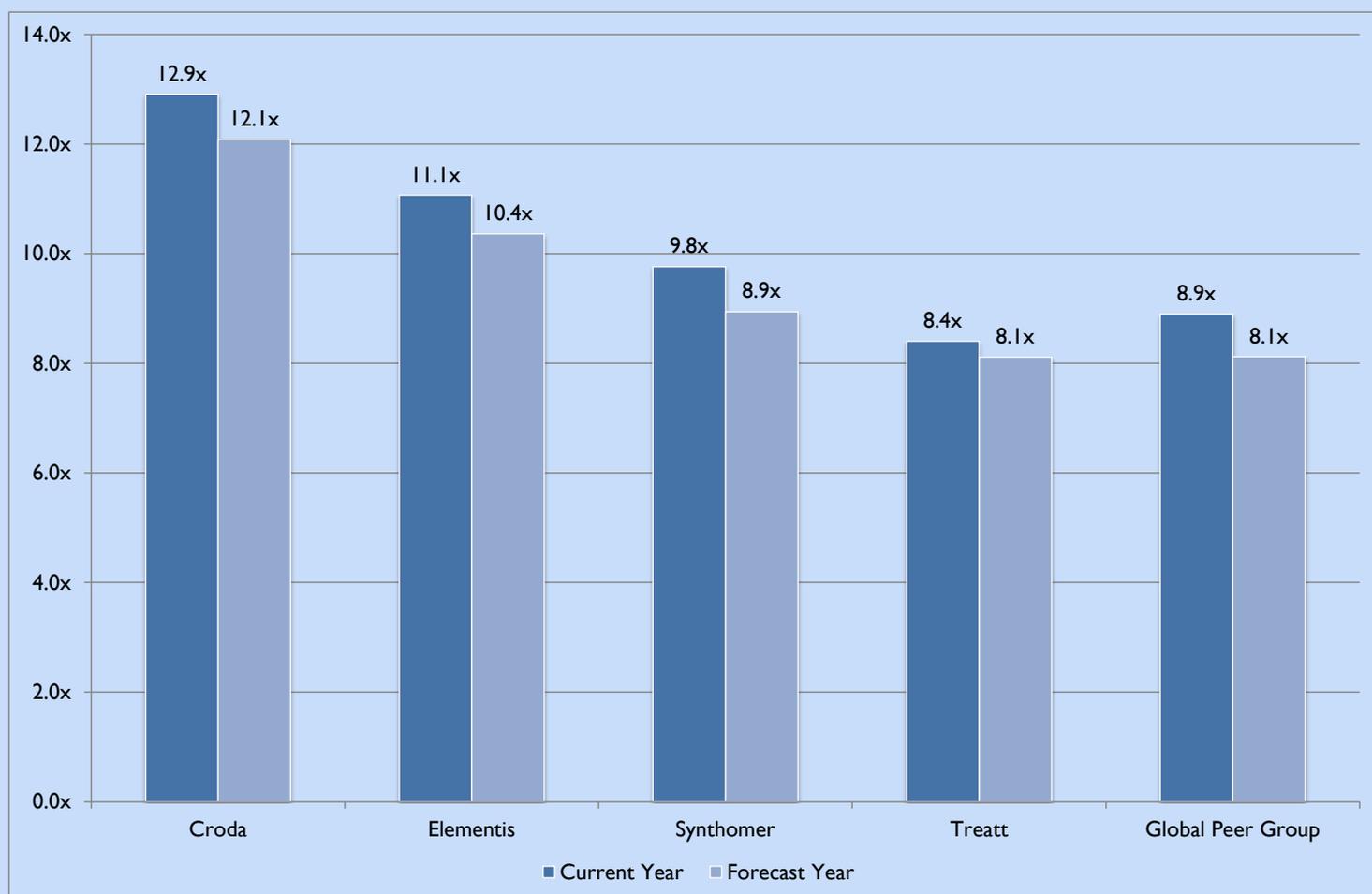
The macro-trend over the past three years is more consistently positive, both in the UK and across our global peer group. The UK companies in our analysis, in general, trade at higher multiples than the average of the global group given their offerings tend to be at the upper end of the value chain. UK companies are currently fighting conflicting headwinds, with positive momentum in the UK economy and a bounce back in Asian demand being offset by continuing weakness in Europe.

## QUOTED CHEMICAL COMPANIES - LIVINGSTONE COVERAGE TRACKING EV/EBITDA



source: S&P Capital IQ

## CURRENT & FORECAST YEAR EV/EBITDA MULTIPLE



source: S&P Capital IQ

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International  
Mid-Market M&A and  
Debt Advisory Firm

*Livingstone*

## MARKET OVERVIEW

A summary of relevant transactions in the Chemicals sector is shown below. The size of acquirers relative to target companies means a general paucity of publicly available transaction information.

We expect an increase in both the volume of transactions and multiples achieved in the short-to-medium term, driven by an increase in the M&A appetite of cash-rich international acquirers.

## COMPARABLE CHEMICAL TRANSACTIONS

DATE	TARGET	ACTIVITY	ACQUIRER	EV	EBITDA (X)
Dec-14	Farrow & Ball	Manufacture of decorative paint and wallpaper	Ares Management LLC	275	15.1
Nov-14	Warwick International	Manufacture and distribution of specialty chemicals	The Lubrizol Corporation	n.a	n.a
Nov-14	Pentagon Chemicals	Manufacture of specialty and fine chemicals	Vertellus Specialties Inc	n.a	n.a
Oct-14	Solvents with Safety	Distributor of packaged virgin and recovered solvents	Tradebe S.A.	n.a	n.a
Oct-14	Subsea Fluid Technologies	Provider of hydraulic and storage fluids	Platform Specialty Products Corporation	n.a	n.a
Sept-14	AmegA Sciences plc	Developer and manufacturer of specialty chemicals	ICL Fertilizers	7	8.9
Aug-14	Seal It Services	Manufacture of sealants and adhesives	Astral Poly Technik Limited	n.a	n.a
Aug-14	Doeflex Compounding	Producer of thermoplastic materials	INEOS Group	n.a	n.a
July-14	Farmura	Manufacture of liquid organic fertilisers, turf products and surfactants	Aquatrols Corporation of America Inc	n.a	n.a
June-14	Batoye Freedom Group	Manufacture of specialist lubricants, greases and oils	Fuchs Petrolub AG	10	n.a
June-14	Fine Industries	Supplier of fine chemical custom synthesis services	De Sangosse SAS	n.a	n.a
May-14	Scientific and Technical Gases	Manufacture of high quality calibration gases	Air Liquide SA	n.a	n.a
May-14	Gower Chemicals	Process of chemicals and associated services	Scheruhn Industrie-Mineralien	n.a	n.a
Apr-14	Harp International	Supplier of refrigerants, lubricants and oils	Groupe Gazachim	n.a	n.a
Mar-14	Amber Chemical	Manufacture of silicones	ICM Products, Inc.	23	n.a

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