Expert Talk: MARTIN BASTIAN, HOULIHAN LOKEY

Chemical industry is joining merger parties

For months, mergers and acquisitions have been on the rise again in the chemical industry. It's all about portfolio restructuring, market share and improving the ESG footprint. Financial investors and strategists are on the case.

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Supply chains, sustainability and environmental protection - the global issues of business are also driving the strategies of chemical companies. "ESG issues play a major role in investment decisions and M&A processes in chemistry. The industry is on the lookout for environmentally friendly chemical products and recycling processes as well as alternative energy sources and raw materials," explains Martin Bastian, Head of Chemicals Europe at the investment bank Houlihan Lokey.

A major issue for manufacturers of plastics, paints and fibers are prices and the availability of raw materials. Suppliers have curtailed individual productions because raw materials or precursors are not available or so expensive that production is no longer profitable because prices for customers cannot be increased in a timely manner.

Stabilization of supply chains

BASF, for example, has cut back its ammonia production at its Ludwigshafen and Antwerp sites because of higher natural gas prices. The chemical company justified this step by saying that the conditions for the economic operation of an ammonia plant for the production of fertilizers had deteriorated considerably. However, the production of ammonia remains profitable for other applications.

The industry is also stepping up investments in Europe, particularly Eastern Europe, to stabilize supply chains and shorten the long journey from China, Bastian explained. "The groups are also combing through their production structures and putting marginal sites up for sale or closing them in order to optimize processes," adds the industry expert. Evonik, for example, recently announced its intention to place its Lülsdorf site, where basic chemicals are produced, in new hands in the medium term. According to regional media, the traditional East German chemical site of Schkopau could be facing the biggest change of the century. The U.S. company Dow, which took over the Buna site after reunification, is considering divesting all activities outside its core business.

Financial investors are also showing interest in chemical plants. BASF, for example, sold its production site in Kankakee, Illinois, to the private investment company One Rock Capital Partners at the end of 2020. The DAX-listed company had acquired the U.S. plant in 2010 when it took over specialty chemicals group Cognis. An analysis had shown that the profile of the site no longer fit the corporate strategy in the long term. The buyer, One Rock, intends to develop the plant into a "strong, independent company”.

There has been an overall increase in M&A activity in the sector. Mergers and acquisitions have been increasing significantly again since summer 2020. One major transaction was the sale of Lonza's Specialty Ingredients division for sfr4.2 billion to financial investors Bain Capital and Cinven in early 2021. PTT Global Chemical of Bangkok, Thailand, also put a good 4 billion euros on the table to buy Allnex, the global market leader in binders for the paints and coatings industry. The seller is the financial investor Advent. The most recent largest deal came in September, when Standard Industries, a privately held global industrial company, completed its acquisition of W. R. Grace & Co - the world's leading supplier of catalysts and engineering materials. The transaction was valued at $6.3 billion.

The latest transaction in the industry is the acquisition of Mannheim-based MBCC Group, formerly BASF Construction Chemicals, by the Swiss Sika Group, which is buying the unit from financial investor Lone Star for sfr5.5 billion. The U.S. private equity firm had bought the world's leading supplier of construction chemicals products and solutions from the Ludwigshafen-based chemical group for €3.2 billion as recently as fall 2020.

"Private equity is active on the buy and sell side, but strategists have also become more active and are rebuilding portfolios," Bastian sums it up. "There are not many specialty chemicals assets on offer, and those options are being used." M&A has established itself as a source of growth, he says, especially since growth can currently be bought for cheap money. "It's obvious to use cheap capital for strategic targets."

Higher valuations

Company valuations have held their own in Corona times, especially as more successful assets were initially put on display during the crisis. "Multiples have settled at a still high level of around 10 to 12 times Ebitda, whereas in earlier years they tended to be between 8 and 9," explains the consultant. In the past twelve months, the highest multiple of 20.5 was achieved in the flavors and fragrances segment in the acquisition of Iberchem by Croda - completed in December 2020.

Strategic decisions in the chemical industry are also being driven by the global issue of energy transition. Both customers and investors are putting pressure on more sustainable production, Bastian explains of the scenario. "In the past, it was primarily manufacturers of tobacco, weapons, and alcohol that were on the blacklist of large funds, but now this also affects more energy-intensive businesses," the consultant summarizes.