

"M&A in mechanical engineering takes off"

Corona increases pressure on German SMEs to go digital - pandemic as driver of development

While cautious optimism is already prevailing elsewhere, the German mechanical engineering industry is showing a bleak picture. But it is not only the lack of orders and scarce liquidity that is causing stress. In the long term, the crisis will increase the pressure for digitalization. This could lead to mergers and acquisitions.

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ds Frankfurt - German mechanical engineering companies could come under pressure from the corona crisis to invest more in digitization or to place themselves in the hands of a new owner. "In the short term, the focus is on the liquidity situation, but in the long term, the corona crisis will increase the pressure for digitization in the German mechanical engineering industry," says investment banker Steffen Leckert in an interview with the Börsen-Zeitung. Leckert is Managing Director at the US investment bank Houlihan Lokey, where he is responsible in Corporate Finance for industrial companies with a focus on industrial automation and the packaging industry.

"Supply chains have been interrupted by the lockdown, companies have realized that they have to diversify their supply and in some cases build up additional onshore supply alternatives," says Leckert. This has increased cost pressure and the compulsion to make processes more efficient with the help of intelligent software. "Medium-sized companies that lack the financial means for rapid digitization risk being left behind in the medium term," he warns. The costs of digitization are difficult to shoulder for many machine manufacturers - especially in corona times. "Smaller medium-sized companies that rely on cheaper internal digitisation solutions will often be too slow, external growth is often only sensible and financially viable for larger companies". Some medium-sized machine manufacturers will therefore consider whether now is not the time to sell. "The selection process in mechanical engineering will become pick up speed", Leckert is convinced and expects that this will trigger mergers and acquisitions.

Is a sell-out imminent?

"M&A in mechanical engineering will be spurred on," he says. On the one hand, there is pressure to sell in mechanical engineering due to cost pressure, and on the other hand, as he says, there is "pressure to buy" to add software capabilities. Leckert estimates that this could lead to a sell-off of medium-sized mechanical engineering companies to large domestic and foreign corporations. "Selling out always sounds a bit negative, of course, but I think it could be an opportunity for one or the other medium-sized company to develop further as part of a larger group in the future. The necessary capital and skilled workers to master the challenges of digitization are, after all, not available to the necessary extent at some mechanical engineering companies.

Increased activity by financial investors in the capital goods industry can now also be expected. "Private equity could also selectively acquire some key companies and turn them into market leaders with investments. The interest of Chinese buyers could also pick up again after the sharp decline in recent years". According to the investment banker, there could be interest, especially in industrial technology, in some German pearls that are well positioned in sub-segments. "Prospective buyers could, for example, focus on the motion control segment, i.e. manufacturers of drives, control technology and mechatronic components that play an important role in the overall automation technology," explains Leckert. There are many medium-sized companies there, which are often privately owned and which are very interesting for foreign companies. "The packaging and process machinery sector could also be interesting for buyers," he says. Germany is the technological leader

in this sector, and several transactions have already been seen here in recent months, such as the sale of Bosch Packaging Technology to CVC, the sale of Wolf Verpackungsmaschinen to HQ Equita, or the sale of BMS Maschinenfabrik to the portfolio company End of Line Packaging Experts.

Chinese come back

Leckert also considers a revival of interest from China, which had recently been slowed down, among other things, because of political obstacles to takeovers. "The Chinese have been reluctant in recent years after Midea took over the German robot manufacturer Kuka. But that could change," says Leckert. After all, the Chinese had come out of the Corona crisis better than the rest of the world. On the other hand, he admits, the regulatory restrictions on technology transactions, which could hamper purchases from China, still apply. In addition to sales, the investment banker is also focusing on M&A through purchases by capital goods manufacturers. The focus here is mainly on industrial software for the interface between machines and higher-level ERP systems, which comes from Oracle or SAP, for example.

"Make or Buy" in software

Such integration and control of the individual machines is often developed by the larger machine manufacturers themselves, but there are also specialised software companies that offer such integration, control and data analysis. "This software is becoming increasingly important. There the question Make or Buy basically arises for machine-builders. For Make you need know-how, and this is often not available and also difficult to build up due to the lack of skilled workers in the IT industry", Leckert's observation.

For example, the Körber company has bought the IT service provider Werum IT Solutions which offers software for production control and monitoring in the pharmaceutical and biopharmaceutical industry. "Körber could afford to do so, but smaller medium-sized companies may not have the resources to purchase or build up the IT competence themselves, and therefore it might be interesting for smaller machine manufacturers to join a good partner," concludes Leckert.