Industrial Manufacturing, Metals Deals Drove 2011 M&A Activity

Barry Misthal, Global Industrial Manufacturing Leader

The global industrial products [1] (IP) industry experienced an increase in deal volume over the course of 2011—801 deals worth more than $50 million compared to 783 deals in 2010—with industrial manufacturing and metals markets leading merger and acquisition (M&A) [2] activity, according to a series of quarterly M&A reports released by PwC US [3]. The majority of deals within the IP sector were driven by companies focusing on smaller deals, an increase in divestitures [4], and an uptick in local deals to create synergies [5]. In addition, while strategic investors dominated overall activity, financial investors increased their participation in 2011 compared to the prior year.

PwC's IP practice examined activity in the fourth quarter of 2011 and full year 2011 across six sectors: aerospace & defense (A&D) [6], chemicals [7], engineering & construction [8], industrial manufacturing [9], metals [10], and transportation & logistics [11].

The industrial manufacturing sector saw the largest increase in activity with deals worth more than $50 million totaling 161 deals in 2011 compared to 135 deals in 2010. The metals industry also increased in activity with 122 transactions worth more than $50 million in 2011 compared to 106 deals in 2010. Although total industrial products deal volume increased, total deal value for transactions worth more than $50 million decreased to $362.5 billion in 2011 from $462.6 billion in 2010. Mega deals, or transactions worth more than $1 billion, slightly decreased in 2011 with a total of 72, compared to 80 mega deals in 2010. This contributed to a lower average deal value for deals worth more than $50 million—$45 million in 2011 compared to $59 million in 2010.

"2011 was all about smaller deals in industrial products as dealmakers remained conservative focusing on deals that were seen as less risky and that needed smaller levels of capital in today's uncertain economy. This trend was exemplified across the sector and especially in A&D where it was a record year for volume, mostly driven by smaller transactions, though we also note that a record deal in terms of size was announced in this sector," said Bob McCutcheon, U.S. industrial products and metals industry leader at PwC [12]. "Deal activity in 2012 will depend on more stabilized financial markets, a global recovery and abatement in concerns over the European debt crisis. An uptick in action across industrial products in 2012 is anticipated, and our latest Manufacturing Barometer [13] reports that U.S. industrial manufacturers [9] are expected to continue to increase investment spending in the year ahead, including operational spending, and plans for M&A with a significant emphasis on expanding into new markets."

Divestitures became a major trend in deal activity in 2011 across all sectors of IP, as companies aimed to exit unprofitable markets and adjust product mixes to reflect changing customer demands. Divestiture deal value as a percentage of total M&A value increased to 33 percent from 30 percent from 2009-2010, and as much as 40 percent of activity in recent years has been related to spin-offs. Within the metals sector, divestitures accounted for 38.5 percent of deal activity which recorded 122 deals that were worth more than $50 million and a total value of $55.1 billion in 2011.

Spin-offs were also on the rise in 2011 as companies looked for attractive ways to separate high-growth or low-growth components of the business from more traditional pieces of the organization. The PwC IP practice released a special report in the fourth quarter of 2011 titled, "Using divestitures and spin-offs to best position an organization for growth."

Today, divestitures and spin-offs are taking longer to close than in previous years, with some companies being forced to go to market several times before successfully striking deals with buyers. In this environment, managing the divestiture process can be critical, from start to finish by assembling a team dedicated to managing and executing the deal and the operational separation simultaneously.

"To close deals and maximize the value of their assets, sellers should strive to gain a better, more comprehensive understanding of the complexities of the divestiture market, and gauge the full scope of buyer concerns and responding to the global economic crises that have changed the rules of the game," said McCutcheon. "Certain sellers are interested in acquiring capital as companies look to restructure their balance sheets by building up cash reserves or paying down debt. Selling a high-performing or high-value business unit at a desirable price can go a long way toward helping a company achieve that goal."

According to PwC's reports, the pace of local deals that were worth more than $50 million increased to 510 deals in 2011 compared to 487 deals in 2010. Industrial products cross-border deals remained flat in 2011 from the prior year—36.4 percent of deals worth more than $50 million and 37.8 percent respectively. The pace of local market consolidation hastened as IP companies sought synergies to reduce expenses. For example, in the industrial manufacturing sector, the U.S. domestic market has been very active in the fourth quarter of 2011, contributing to an overall level for local transactions of 53.8 percent of deals worth $50 million or more, compared to 46.2 percent of cross-border deals, and 55.9 percent of local market deals for all of 2011, compared to 44.1 percent of cross-border deals. For the metals industry, the majority of local deals were led by Asia and Oceania in 2011 and China-based deals were the primary driver of activity with 37 transactions in 2011, given the emphasis that the Chinese government has put on steel company consolidation in its most recent Five Year Plan.

"Faced with substantial uncertainty, companies appeared to be opting for growth within their familiar domestic markets. Such moves limit the legal and cultural risks typically associated with cross-border transactions. We're also seeing higher growth prospects within emerging markets, which will likely keep Asian acquirers focused on targets within their borders. Mature markets such as the U.S. and Europe also continue to seek domestic consolidation as a tool for growth and competitor elimination," added PwC's McCutcheon. "One example of an exception was in the A&D space where European dealmakers increased activity, driven by both local market deals as well as outbound transactions. The increase in European outbound deals also contributed significantly to the overall rise in cross-border deals and foreign acquisitions of U.S. targets in 2011, totaling 20 local market transactions that were worth more than $50 million compared to 40 cross-border deals."

While strategic investors continued to lead activity across the IP industry, financial investors have started to gain steady momentum in 2011. Across all the sectors of industrial products, 26.3 percent of financial investors were involved in deals that were worth more than $50 million in 2011, a slight increase from 25.7 percent of deals in 2010. According to PwC's reports, A&D, engineering & construction, and metals sectors have all experienced a slight increase of financial deals in 2011 compared to 2010.

"Strategic investors sought inorganic growth through acquisitions to stay current with global macro trends such as increasing global infrastructure," added McCutcheon. "While financial investments did increase in 2011, this was mostly pertained to smaller deals. In 2012, financial investors are expected to continue their steady climb into deals in the space, but strategic investors will remain well positioned, given healthy liquidity levels, to drive a high volume of deals."

A breakdown of PwC's analysis of M&A activity and outlook for IP follows:

- Aerospace & Defense [14] – In 2011, there was a big increase in both deal volume and value for aerospace targets and when considered alongside the higher sales multiples awarded to aerospace, rather than defense, this part of the sector has a more favorable outlook for 2012. Mega deals also made a comeback in this sector with six mega deals in 2011, up from four in 2010. A&D continues to globalize as non-US entities increase their competitiveness, which is supported by increasing defense budgets and air travel in several overseas regions. Foreign countries, particularly emerging markets, are seeking to take advantage of this demand shift by fostering their own domestic industries. China seems well-positioned to advance its national aerospace industry given the relative level of domestic demand as well as technological help from Western suppliers. Deal volumes are expected to continue their gradual shift toward non-U.S. parties while large deals involving the U.S. continue to drive overall deal value in this sector.
- Chemicals [15] - Overall deal volume and deal value were down in the fourth quarter of 2011, but in all of 2011, deal volume increased slightly with a declined deal value from 2010. There was only one mega deal during the fourth quarter of 2011, which contributed to a total of 17 mega deals in 2011 with a combined value of $59.7 billion compared to 16 deals in 2010

valued at $91.4 billion. North America drove local deal value in 2011 with $31.5 billion and deal volume was driven by 41 local deals that were worth more than $50 million in Asia and Oceania, many involving China. Europe was the primary driver for outbound volume and value with 19 transactions worth more than $50 million and a total value at $11.7 billion in 2011. The dominant chemical end-user industries such as automobiles, durable goods and construction showed improvement in 2011, but have not returned to pre-recession levels.

- Engineering & Construction [16] – The majority of deal activity in the fourth quarter of 2011 was from small, bolt-on acquisitions, which dropped the average deal value to 2009 low levels of $354 million, but recorded two mega deals during this period. With the combination of a sluggish U.S. recovery, reductions in federal and municipal spending and political gridlock, non-U.S. affiliated deals took the lead in deal activity during the fourth quarter of 2011. Asia and Oceania led deal activity with China as a major player as a result of the Chinese government's infrastructure and energy efficiency activities. While many companies in this sector might employ a "wait and see" strategy in the first half of 2012, shareholders' pressure to deploy cash abundances and generate greater returns are likely to spur activity in the second half of the year.
- Industrial Manufacturing [17] – After a strong start at the beginning of 2011, deal activity in the second half of the year softened with a shift away from larger, more transformative and impactful transactions. There was one mega deal in the fourth quarter of 2011 where both companies operated within the same semiconductor machinery manufacturing/chip equipment segment, indicating another trend in the market: a company's desire to pursue acquisitions to establish a technological edge over its peers. The U.S. maintained its position as one of the most active countries in activity, followed closely by China and Japan, and interestingly, new emerging markets such as Mexico, surfaced as players in the deal arena in the fourth quarter of 2011. Global industrial manufacturing deals in the first half of 2012 are expected to remain fairly even with 2011 activity, but if the Euro crisis is resolved, companies hungry for growth along with strong fundamentals and cash-rich balance sheets could spur an increase in activity in the second half of 2012 and early 2013.
- Metals [18] – In 2011, there were 16 more deals that were worth more than $50 million than in 2010, but deal value declined to $55.2 billion from $92.6 billion. This 40 percent decline in value drove a decrease in average deal value as well, from $874 million to $452 million. Asia and Oceana drove overall deal value in 2011 with the majority of local deals also led by Asia and Oceania. This region is expected to continue to drive local deal activity in 2012 as China makes progress in consolidating its domestic metals industry. Given the current economic environment, the metals sector could see a moderate deal growth into 2012. However, the general collapse of aluminum prices impacting the bottom lines of large producers, accumulating stock levels and soft economic conditions further impacting pricing and the potential of a slowdown in the steel industry in 2012, given weakening global demand and the tighter control of the Chinese real estate market.

- Transportation & Logistics [19] – Overall deal volume and deal value stayed steady with 170 deals valued at $50 million or more in 2011 compared to 186 deals in 2010 but saw a drop in the fourth quarter of 2011 when compared to the previous quarter. The fourth quarter of 2011 produced three mega deals, which included a transaction valued at $4.2 billion that was also the largest for the full year. Emerging markets returned in the fourth quarter of 2011 with a majority of activity being driven by Europe and Asia as companies focus on consolidating to build economies of scale. Shipping and infrastructure deals are strategically positioned to lead the transportation & logistics industry in deal activity in 2012 as a result of shipping companies consolidating due to ongoing capacity issues and emerging markets investing in airport, ports, and roads.

About PwC's Industrial Products Practice

PwC's Industrial Products [1] (IP) practice provides financial, operational, and strategic services to global organizations across the aerospace & defense [6] (A&D), business services [20], chemicals [7], engineering & construction [8] (E&C), forest, paper, & packaging [21] (FPP), industrial manufacturing [9], metals [10], and transportation & logistics [11] (T&L) industries. For more information please visit www.pwc.com/us/en/industrial-products [22]

About the PwC Network
PwC firms help organizations and individuals create the value they're looking for. We're a network of firms in 158 countries with close to 169,000 people who are committed to delivering quality in assurance, tax and advisory services. Tell us what matters to you and find out more by visiting us at www.pwc.com [23].

Source URL (retrieved on *01/28/2015 - 4:47am*):
http://www.impomag.com/articles/2012/02/industrial-manufacturing-metals-deals-drove-2011-m-activity?qt-most_popular=0

Links:
[1] http://www.pwc.com/us/en/industrial-products/index.jhtml
[2] http://www.pwc.com/us/en/transaction-services/index.jhtml
[3] http://www.pwc.com/us/en/index.jhtml
[4] http://www.pwc.com/us/en/transaction-services/divestitures.jhtml
[5] http://www.pwc.com/us/en/transaction-services/synergies.jhtml
[6] http://www.pwc.com/us/en/industrial-products/aerospace-defense.jhtml
[7] http://www.pwc.com/us/en/industrial-products/chemicals.jhtml
[8] http://www.pwc.com/us/en/industrial-products/engineering-construction.jhtml
[9] http://www.pwc.com/us/en/industrial-products/industrial-manufacturing.jhtml
[10] http://www.pwc.com/us/en/industrial-products/metals.jhtml
[11] http://www.pwc.com/us/en/industrial-products/transportation-logistics.jhtml
[12] http://www.pwc.com/us/en/industrial-products/leadership/robert-

mccutcheon.jhtml
[13] http://www.pwc.com/manufacturing-barometer
[14] http://www.pwc.com/us/en/industrial-products/publications/mission-control.jhtml
[15] http://www.pwc.com/us/en/industrial-products/publications/chemical-compounds.jhtml
[16] http://www.pwc.com/us/en/industrial-products/publications/engineering-growth.jhtml
[17] http://www.pwc.com/us/en/industrial-products/publications/assembling-value.jhtml
[18] http://www.pwc.com/us/en/industrial-products/publications/forging-ahead.jhtml
[19] http://www.pwc.com/us/en/industrial-products/publications/intersections.jhtml
[20] http://www.pwc.com/us/en/industrial-products/issues.jhtml
[21] http://www.pwc.com/us/en/industrial-products/forest-paper-packaging.jhtml
[22] http://www.pwc.com/us/en/industrial-products
[23] http://www.pwc.com/