Local Transactions Drive Global Chemicals M&A

While merger and acquisition [1] (M&A) activity in the global chemicals sector rose slightly in 2012 due to an increase in smaller acquisitions, continued uncertainty around the state of the global economy probably constrained growth and contributed to a decrease in total deal value compared to the prior year. Despite ongoing global concerns, M&A activity in advanced economies including North America is growing, according to *Chemical Compounds* [2], a quarterly analysis of M&A activity in the global chemicals industry [3] by PwC US [4].

The total volume of chemical transactions (worth $50 million or more) increased year over year, with 38 deals totaling $17 billion in the fourth quarter of 2012, compared to 31 deals totaling $8.2 billion in the same quarter in 2011. However, the combination of slow growth and smaller transactions continued to suppress the overall value of transactions, as deal value declined more than 18 percent on a quarterly and annual basis.

“The deal environment in the chemicals industry continues to be adversely affected by a number of global economic concerns, including slow growth in Asia, a potential recession in Japan, weakness in the Eurozone, and uncertainty over the outlook for the U.S. economy,” said Anthony J. Scamuffa, U.S. Chemicals Leader for PwC [5]. “However, despite muted M&A activity overall, we are seeing growing interest in the U.S. market, with all five of the fourth quarter mega deals involving domestic-based entities. With demand impacted by a sluggish economy, many producers are divesting underperforming and non-core assets, resulting in greater operational efficiencies and strengthened liquidity. This gives us some optimism for a recovery in M&A activity in the chemicals sector over the longer term.”

With the general decline in values, mega deal (transactions worth more than $1 billion) values fell more than one-third to $7.8 billion in the fourth quarter of 2012. While the number of mega deals remains similar annually, with 17 mega deals in 2012 and 16 in 2011, all of the transactions in 2012 ranged between $1 billion and $5 billion, while four of the deals in 2011 valued above $5 billion – contributing to the decrease in overall 2012 deal value.

In the fourth quarter of 2012, deals were largely done by strategic investors, as companies looked to enter more specialized markets and diversify their product portfolios. Many potential chemicals acquirers have become financially stronger over time, as average debt-to-equity ratios have declined, and cash balances have increased. As a result, many companies utilized cash payments and debt acquisitions to complete the smaller deals in the fourth quarter of 2012.

According to PwC, more than 71 percent of targets in the fourth quarter and 62 percent in all of 2012 were from advanced economies, a significant jump from the five-year average of 59 percent. Despite concerns regarding the economies in many of the advanced regions, local activity in these areas is growing, as participants chase new lines of business such as electronic materials, or geographic expansion. Targets in North America drove local deal volume, followed by Asia and Oceania. These two regions combined were responsible for almost 90 percent of the quarter's local deal volume.

"Construction and consumer goods manufacturing, which are two major end-user industries that drive chemical demand, have been facing considerable challenges," continued Scamuffa. "While we do not anticipate significant growth in M&A in the sector in the near term, large deals within specialty chemicals are possible, with the deal environment remaining flat until end-user industries improve. In addition, the expansion of the shale gas market [6] could potentially drive significant benefits to the U.S. chemicals industry, providing optimism regarding M&A for the region."

Activity in the BRIC targets almost doubled in the fourth quarter of 2012 compared to the third quarter, with deals related to targets in China leading most of the activity. On an annual basis, BRIC target activity declined 12% percent over 2011, likely due to a cooling economy in China, India and other emerging economies. The majority of the deals stemmed from China in the fourth quarter of 2012, with activity tripling to nine deals compared to the third quarter. Smaller deal activity increased as well in the fourth quarter of 2012 compared to the third quarter. PwC found that despite economic concerns, BRIC-related transactions continue to see growth.

For a copy of Chemical Compounds, PwC's quarterly analysis of M&A activity in the chemicals sector, visit: www.pwc.com/us/industrialproducts *[7].*

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