

Quarterly Review

Chemicals & Materials Q3 2019



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CapitalRoundtable – Private Equity Investing in Specialty Chemicals Companies

Adam Hunia (Director, Lincoln International) spoke on a panel at the 2019 CapitalRoundtable – Private Equity Investing in Specialty Chemicals Companies chaired by Brian Orkin (Investment Partner, Arsenal Capital Partners). Below is a summary of the key questions discussed and Adam’s comments.

Buyers are increasingly looking for stable and recession resistant businesses. What sub-sectors and end-markets are garnering the most attention in today’s market?

The end-markets getting the most attention are those benefiting from favorable secular trends and those expected to perform well through a recession. Examples include food related chemicals (flavors and fragrances; bio-based ingredients) and packaging (all across the value chain...from films to finished goods). CASE assets continue to be of strong interest generally given the market fragmentation and ability to do add-ons. Within specialty materials, aerospace and defense focused assets are trading at premium multiples given the long-term favorable trends, product differentiation and customer stickiness.

What other business attributes are driving buyer interest?

For strategic acquirers, product differentiation is key – if they are going to add a product to their portfolio, it needs to fill a gap and be a leader in its niche. Also important is increasing exposure to growth end-markets that align with the strategy they have communicated to investors.

For private equity groups, organic growth remains the most important attribute driving buyer interest. Ideally there are favorable end-market trends supporting continued growth. Buyers want to see volume growth paired with margin sustainability. Sponsors are also looking for a viable add-on strategy. Increasingly sponsors are underwriting add-ons (assuming multiple arbitrage) in order to meet return targets given the premium multiples required to win “A” quality assets in this market.

Financial sponsor sellers are increasingly considering exiting businesses after shorter hold periods.

What calculus are sellers thinking through on whether to sell now vs. potentially double down and continue to invest in their businesses?

Sellers should be thinking about exiting now if you believe your business will decline meaningfully during a recession and you don’t want to hold it for several more years. A 2x to 3x multiple compression will be hard to overcome with EBITDA growth. This also must be weighed vs. the 3-year holding period to achieve capital gains vs. ordinary income tax treatment.

One consideration we hear often from sponsors is the reluctance to sell a platform that still has ample additional

What sub-sectors and end-markets are experiencing the most headwinds currently? Is buyers’ interest in these end markets binary or are businesses with this exposure viewed to be potential “value” opportunities in today’s market?

For many private equity groups it is binary – they hear automotive exposure or building products exposure and the immediate answer is no. Taking a contrarian view and finding assets that will continue to perform well could be an opportunity to buy at a better value in a highly competitive market.

- **Auto:** Thus far the dire forecasts of a few years ago of a 30% volume drop and the off-lease tsunami haven’t come true. Increasing focus on light weighting through adhesives and use of specialty materials (particularly around electric vehicles) will continue even if volumes decline.
- **Building products:** Opportunities to take share will remain despite uncertain end-market trends. For example, innovative delivery mechanisms for adhesives or coatings that save contractors time, or alternative materials that offer a better value proposition (aesthetics, low / no maintenance, long-term value).

add-ons to target. Given the high valuations for platform deals and the potential multiple arbitrage from add-ons, it can be difficult to let go of a platform that is successfully consolidating an industry.

Sellers’ are often marketing aggressively adjusted earnings bases. How are buyers reacting to these adjustments?

Let’s start with some interesting data points. Lincoln’s Valuation & Opinion Group values over 1,200 companies a quarter, primarily for BDCs. In this data set, adjustments have increased from ~17% of adjusted EBITDA in Q4 2013 to almost 25% in Q2 2019.

That being said, we don’t see much change in how buyers are reacting. Buyers and their third-party accounting advisors will do detailed diligence on each adjustment and make a determination as to its validity. In cases where it is justifiable, we have seen an increasing ability to get credit for pro-forma adjustments.

The Sale of StyroChem, a Subsidiary of WinCup, Inc., to PMC Capital

WinCup, Inc. signed an agreement with PMC Capital, an affiliate of PMC Global, Inc., to sell its StyroChem subsidiary. Headquartered in Montreal, Quebec, StyroChem is a leading manufacturer of expandable polystyrene (EPS). The company is the only North American producer of all four grades of EPS, including T-grade (food grade), block molding, shape molding and “lost foam”.

Over the past four decades, StyroChem has earned its reputation as a high-quality producer of EPS products for global customers ranging from small businesses to Fortune 500 companies. StyroChem has over \$100 million in revenues and over 40 years of industry experience. The company’s management team has developed leading engineering, design and manufacturing expertise across the platform to manufacture EPS for foodservice, packaging, construction, casting and specialty applications.



has sold



to



CAPITAL GROUP

Sell-Side



Lincoln’s Key Process Preparation Tactics:

- Designed a broad, highly coordinated sale process leveraging the firm’s industry expertise across a wide range of end markets to accommodate shareholders’ objectives
- Articulated StyroChem’s ability to operate as a standalone asset with the resources and personnel to continue to grow the company
- Developed unique, granular forecast tied to growth plan that highlighted achievable upside and attractive cash conversion

Key Insights from the Transaction and Market:

- Sustainability and relationships with suppliers and customers are critical to providing comfort to buyers
- Having industry expertise gives potential buyers crucial advantages in niche markets when it comes to getting a transaction to the finish line in an accelerated fashion
- Key ingredient manufacturers to diverse end markets remain attractive assets to in the market



Market Intelligence

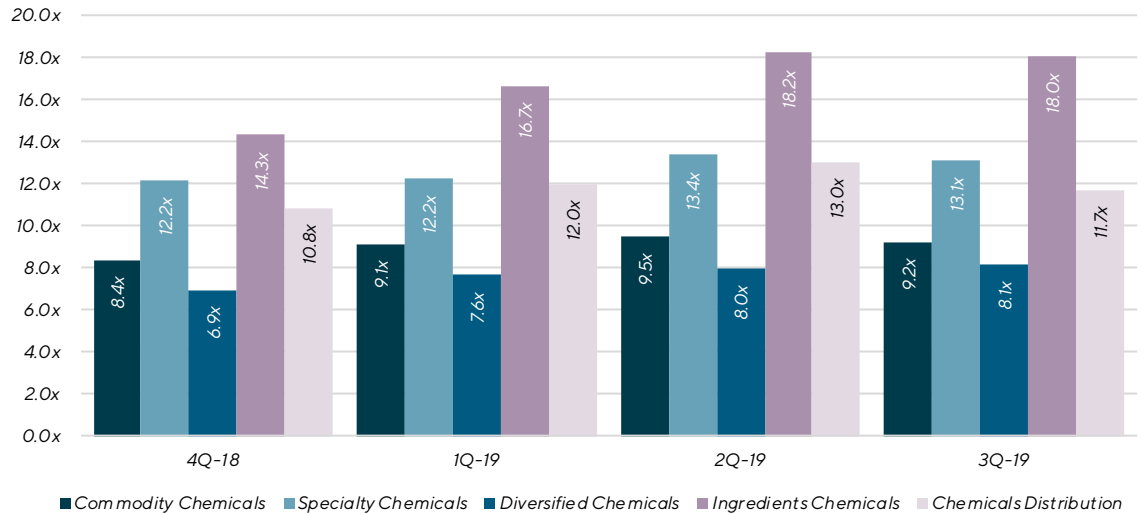
During Q3 2019, the Lincoln International chemicals & materials indexes and S&P 500 remained relatively in line with the prior quarter. Positive tailwinds in the U.S. during the quarter included slight gains in housing activity, which benefited construction-related resins, pigments and related performance materials. Headwinds in Q3 2019 included global performance chemistry easing, which signals a slight slowdown in manufacturing activity, continued trade tensions and the overall outlook on the economy. Due to an overall flat performance in the chemicals & materials industry, EV / EBITDA multiples showed similar trends to the first two quarters of 2019.

Q3 2019 U.S. chemical production was lower in all regions compared to a year ago, with the largest region declines being the Gulf Coast, Midwest and Mid-Atlantic. On a global basis, chemical production showed positive signs in Africa, Latin America and the Middle East, with production falling in all other regions. Output gains experienced in Q3 2019 included consumer products, synthetic rubber, manufactured fibers and coatings. There was slight softness experienced in inorganic chemicals, plastic resins and other specialty chemicals when being compared to the previous quarter.

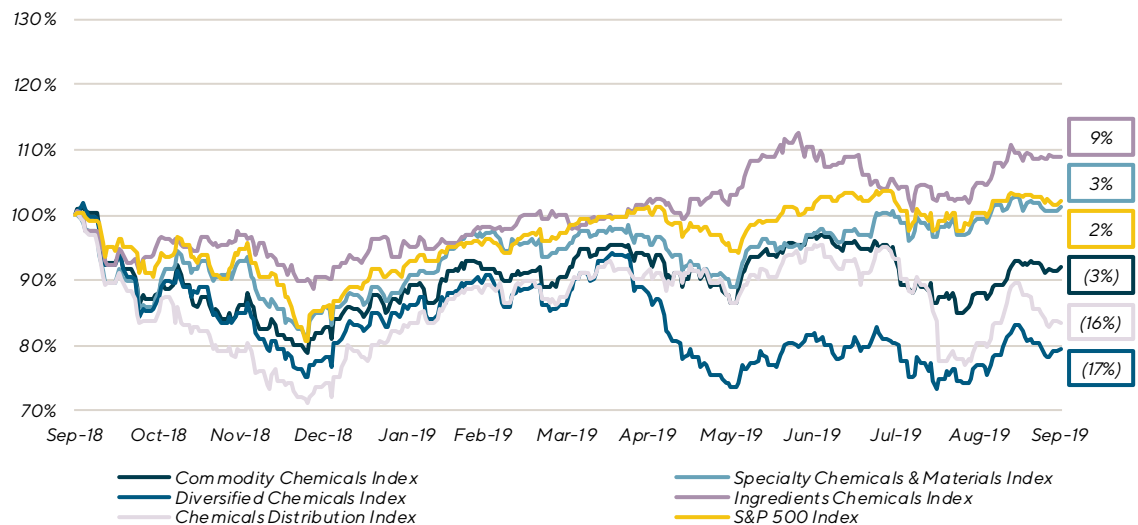
Source: American Chemistry Council, CapitalIQ, Lincoln International

Chemicals & Materials Market Update

Enterprise Value / LTM EBITDA



Stock Market Performance



Public Company Valuation Statistics (9/30/2019)

Sector	Number of Companies	Quarterly Stock Performance	% of 52 Week High	EV / CY19E		P / E Multiple	Net Debt / CY19E EBITDA	CY19E Growth		CY19E Margin	
				Revenue	EBITDA			Revenue	EBITDA	Gross	EBITDA
Commodity Chemicals	16	(6.3%)	69.9%	1.79x	11.1x	19.2x	2.1x	4.5%	11.1%	16.5%	17.0%
Specialty Chemicals	33	(1.3%)	87.2%	2.29x	14.1x	17.8x	1.9x	(2.3%)	7.0%	28.4%	16.7%
Diversified Chemicals	13	(0.1%)	79.9%	1.52x	9.3x	13.5x	2.0x	(3.7%)	(3.2%)	27.3%	14.5%
Ingredients Chemicals	7	(0.8%)	86.5%	4.26x	19.4x	28.0x	2.8x	3.4%	9.1%	37.3%	19.7%
Chemicals Distribution	4	(6.4%)	77.5%	0.99x	13.2x	14.7x	2.9x	8.8%	13.4%	22.2%	6.8%
Median				1.79x	13.2x	17.8x	2.1x	3.4%	9.1%	27.3%	16.7%

Source: Capital IQ, ThomsonONE, Wall Street research and company data

Select Q3 2019 M&A Transactions

(\$ in millions)

Closed	Target Company	Acquiring Company	Enterprise Value	EV / LTM	
				Revenue	EBITDA
Sep-19	Synnovia PLC	Camelot Capital Partners LLC	\$80	0.81x	10.0x
Sep-19	Chongqing Dahao Electronics Co., Ltd.	Chongqing Anjie Electronics Co.	2	1.91x	-
Sep-19	Composites Business of Ashland	INEOS Enterprises Group Limited	1,015	0.92x	-
Sep-19	Hangzhou Xinyang / Qidong Jinmei / Fujian	Shanghai Pret Composites Co.	223	3.36x	-
Sep-19	NanoXplore, Inc.	Martinrea International Inc.	122	2.30x	-
Sep-19	SP Group A/S	Gadinvest A/S	467	1.57x	10.3x
Sep-19	Sun Line Precision Ltd.	Yu Canxiang	2	8.62x	-
Aug-19	Chemgrit Cosmetics (Pty) Ltd	Brenntag AG	-	-	-
Aug-19	Pigments Business of BASF	DIC Corporation	1,272	1.16x	-
Aug-19	Epoxies, Etc.	Meridian Adhesives Group LLC	-	-	-
Aug-19	Oxides and Derivatives Business of Huntsman	Indorama Ventures Holdings LP	2,076	-	5.7x
Aug-19	Performance Products Business of PolyOne	SK Capital Partners	775	1.11x	-
Aug-19	Performance Polyamides Business of Solvay	DOMO Chemicals GmbH	334	-	-
Aug-19	Abercorn Kaolin Pty Ltd	Metalsearch Limited	2	-	-
Aug-19	Eviana Health Corporation	AgraFlora Organics International Inc.	7	-	-
Aug-19	Shantou Paiya Ink Co., Ltd.	Shantou Wanshun New Material Group	10	0.84x	-
Aug-19	European Polyurethane Business of Covestro	H.I.G. Capital, LLC	-	-	-
Aug-19	StyroChem Canada Ltée	PMC Capital Group	-	-	-
Jul-19	OMNOVA Solutions Inc.	Synthomer USA LLC	752	0.99x	10.6x
Jul-19	Chematur Technologies AB	Wanhua Chemical Group Co.	134	11.10x	-
Jul-19	MPD Chemicals, LLC	Entegris, Inc.	165	-	-
Jul-19	All Assets of NanoMech, Inc.	Vinmar International, Ltd.	13	-	-
Jul-19	Surfactants, Thickeners and Dispersants Business	Tiarco, LLC	71	2.84x	8.9x
Jul-19	CA Specialities Ltd / Custom Ingredients, Inc.	Charkit Chemical Company LLC	-	-	-
Jul-19	Sichuan Nengtou Dingsheng Lithium Industry Co.	Chengdu Chuanneng Lithium Equity	51	-	-
Jul-19	Green Seal Holding Limited	Great Plan International Limited	210	1.84x	-
Jul-19	Sasol-Huntsman GmbH & Co. KG	Huntsman Corporation	185	-	-
Jul-19	Interplasp, S.L.	Sheela Foam Limited	50	1.42x	-
Jul-19	Prochimir S.A.S	Bostik SA	-	-	-
Jul-19	Sanders Industries Holdings, Inc.	Arcline Investment Management LP	-	-	-
Jul-19	Preferred Compounding Corporation	HEXPOL AB	232	0.97x	-
Jul-19	ArrMaz Custom Chemicals, Inc.	Arkema S.A.	570	1.97x	10.8x
Jul-19	Hanbang (Jiangyin) Petrochemical Co., Ltd.	Jiangsu ChengXing Phosph-Chemicals	-	-	-
Jul-19	Milliken Infrastructure Solutions, LLC	Clock Spring Company, Inc.	-	-	-
Jul-19	Hengshui Kaiya Chemical Co.	Rianlon Corporation	103	2.45x	-
Jul-19	Carbosynth Holdings Limited	Biosynth AG	-	-	-
Jul-19	Sanyo Chemical Industries Ltd.	Nippon Shokubai Co.	-	-	-
Jul-19	Covia Lime LLC	Mississippi Lime Co.	135	2.81x	-
Jul-19	Granite Hacarmel Investments Ltd.	Elco Ltd.	289	5.43x	-

Source: Capital IQ, Mergermarket, Pitchbook and company data

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