BMI Mergers & Acquisitions

M&A Market Report

MANUFACTURING | Q3 2022

Macro Economics

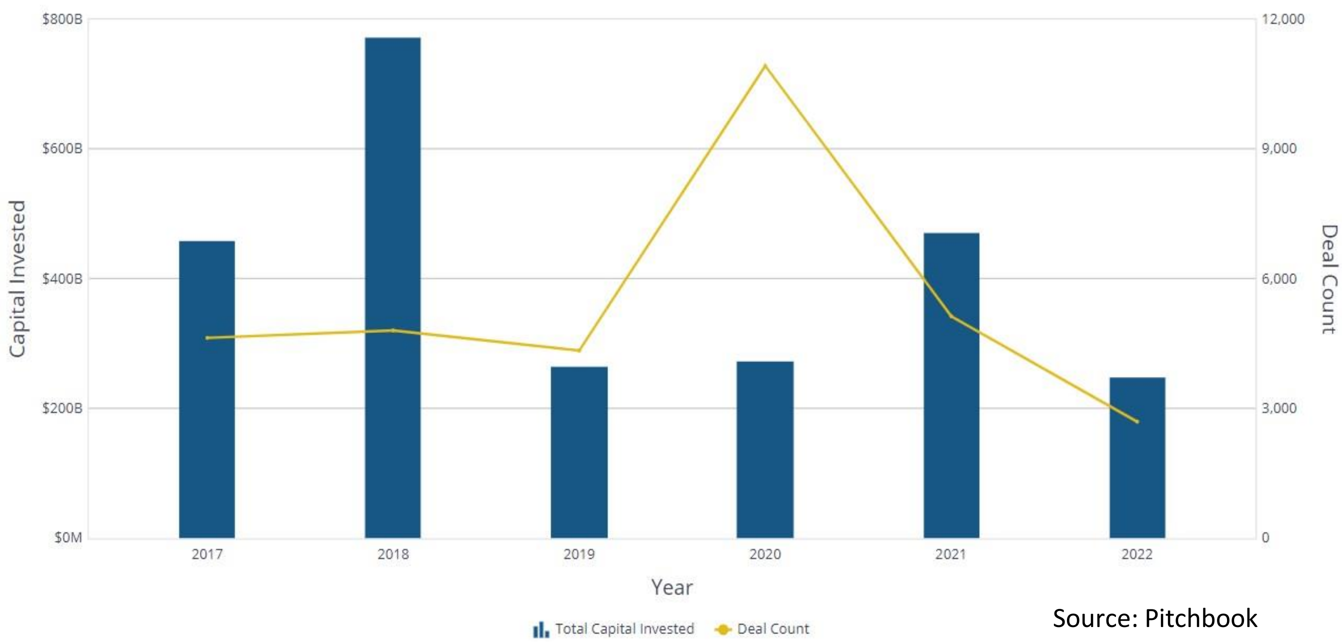
Interest Rates, as measured by the federal funds rate, increased 2.75% this year, which appears daunting. However, the rate is still historically low as fed funds data shows (chart below). The key takeaway is that we are coming off unusually low interest rates and we do not see the current interest rate environment having a major impact on manufacturing M&A, except to give buyers some pause to consider the changes and recalibrate valuations based on the cost of money. We see interest rates as pushing marginal buyers to the sidelines, but most quality buyers will remain active.

Other macroeconomic factors such as supply chain issues and cost pressures have been an issue for the past year and seem to be abating somewhat as buyers and sellers adjust and panic buying lessens. We have seen high order backlogs as well as high inventories and both scenarios have led to higher valuation expectations or deal term issues for manufacturers. These are now working through the system.

Federal Funds Rate - Selected Data	
September 2022	3.00%
June 2006	5.25%
May 2000	6.50%
March 1991	6.00%

Deal Volume

Manufacturing deal volume as reported by Pitchbook is on track to match or exceed the volume for 7 of the last 9 years with an extraordinary 2021 being the outlier at 25% higher than 2019. So even though deal volume will be down in 2022 by about 10%, on a historical context it will still be a very good year.



Source: Pitchbook

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Valuations

We have recently witnessed some pushback on higher end valuations over the past 60-90 days, which was an uncommon practice in 2021. Buyers site the increasing interest rates along with fears of recession. However, economic data is not currently supporting a serious downturn, and the buyer valuations have not been dramatic shifts.

GF Data, tracking private M&A lower middle market deal transactions, reveal in their June 2022 YTD manufacturing M&A report higher than average valuations across all deal size classifications from $10 - $250 million. For example, in the $10 - $25 million enterprise value range, the average EBITDA multiple is 6.0x which is just below a 2021 average of 6.1x and above the long-term average of 5.7x. The lower market in the range of $2 - $10 million has slightly slimmer multiple ranges between 4.0x and 5.0x depending on the overall health and attractiveness of the business.

We believe the strength of the 2022 M&A market is a result of deal carryover. Many of these deals were sealed before the fed started ramping up interest rates in earnest, and before the Ukraine war started. Lower valuation deals will not show up in GF Data research until 2022 or 2023.

Despite evidence of valuation weakening, we do not see dramatic drops nor lack of buyer interest. Keep in mind that the global private equity industry is reporting record high dry powder nearing $2 trillion. Strong companies will continue to attract strong valuations even though we may see fewer outliers at the upper end of the valuation range for a given market segment.

Summary

Over the past year, the federal government has passed legislation that will directly and indirectly affect manufacturing positively, and we believe it will be a supportive catalyst for further interest in US manufacturing deals.

Most, and certainly the best buyers, are still in the market and looking to acquire quality manufacturing companies.

Continued interest rate increases and global recession threats will be a concern and buyer reactions will need to be monitored by M&A professionals and companies preparing for an exit.

Ample cash for deals means any pause will probably be short lived with minor impact on valuations.

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About BMI Mergers & Acquisitions

For over twenty-five years, we have been successfully engaged in the practice of buying, selling and managing the business acquisition process. Our professionals have been engaged in transactions in a multitude of industries. They have completed multi-million-dollar deals, and they have also successfully integrated businesses post-merger. Whether your business is worth $2 million or $100 million, this experience is put to work to achieve your desired result.

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- Multi-industry experience, specializing in Manufacturing
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