

INDUSTRIALS

Q3 & Q4 | 2020

M&A Activity Recovering Due to PE Sponsor Activity

M&A activity in 2020 was significantly impacted by the COVID-19 pandemic. The chart below illustrates sharp declines in the second, third and fourth quarters after the pandemic spread to North America. M&A activity in the second quarter was down 41% compared with the first quarter of 2020. In addition, M&A activity was down 39% on a year-over-year basis (Q2 2019).

Throughout the second half of 2020, M&A activity gradually resumed, but activity was still well below pre-pandemic levels. In Q3, M&A transactions increased by 24% from the second quarter. However, overall M&A activity for Q4 2020 was lower than the prior year by 20%.

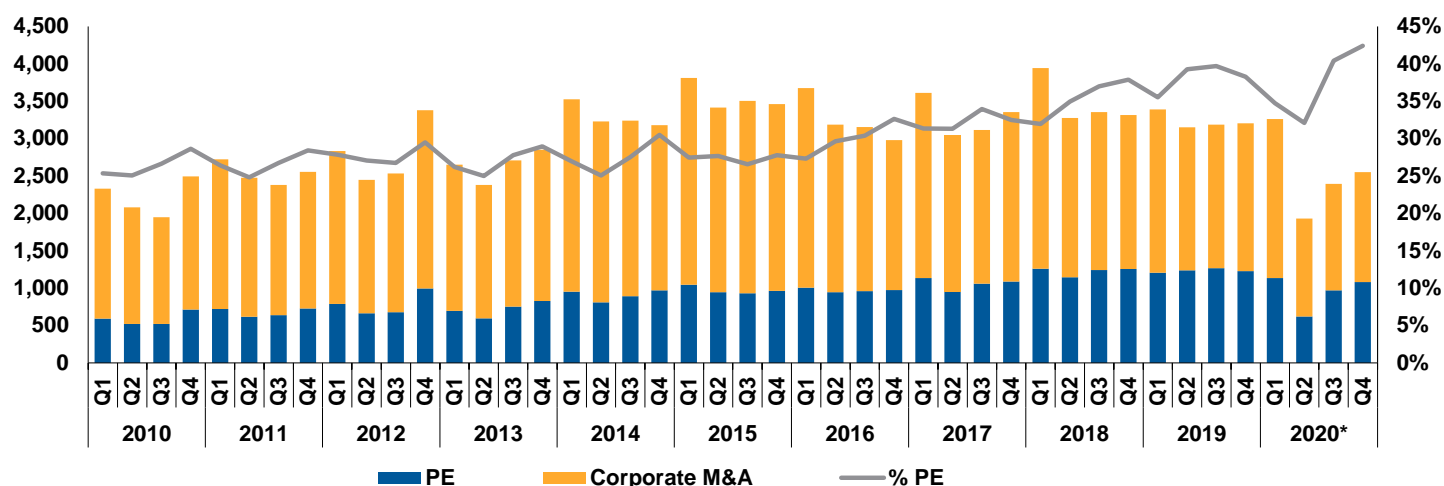
Continuing a trend over the last decade, PE buyers continue to gain an ever-increasing share of M&A transactions. As recently as 2015, PE buyers made up 25-30% of M&A transactions. During the fourth quarter of 2020, PE buyers were responsible for 42% of M&A transactions.

It is noteworthy that PE M&A activity has almost completely recovered to pre-pandemic levels. A defining feature of the current M&A environment is the record level of dry powder from private equity funds, who hold approximately \$2.4 trillion of capital that must be invested in new platform investments or used to acquire add-on companies for existing platform investments.

Corporate M&A activity remains lower than pre-pandemic levels. Corporate M&A transactions were down approximately 25% in 2020 versus 2019. Companies were less focused on M&A activity and more focused on shoring up balance sheets and existing operations.









As companies begin to re-focus on long-term strategic growth as economies around the world adjust to the new normal of a post-pandemic world, there are several positive factors that should support the deal-making landscape in 2021 and beyond.

M&A Transactions by Quarter



Source: EdgePoint Proprietary Database, Company Filings, Pitchbook, CapIQ, News Releases

Notable Recently Announced and Closed Industrial Transactions

Date: 7/31/2020 (Closed)		Overview / Strategic Rationale:	Precision Manufacturing
Target:		<p>Advent International and Cinven, both large international private equity firms, acquired the leading global manufacturer and service provider of elevators, escalators, and other innovative passenger transportation solutions.</p> <ul style="list-style-type: none"> <i>Thyssenkrupp AG reinvested in Thyssenkrupp Elevator through a minority stake</i> <i>The acquisition enables Advent International to grow its market position and technology leadership throughout the U.S., Europe, and Asia</i> <i>Thyssenkrupp Elevator is one of the top 4 global Elevator & Escalators players, and has a comprehensive product and service portfolio</i> 	
Acquirers:	ADVENT INTERNATIONAL 		
Key Metrics:			
Implied Enterprise Value (\$M)	\$20,400		
EV/LTM EBITDA	NA		
EV/LTM Revenue	2.2x		
Date: 12/9/2020 (Closed)		Overview / Strategic Rationale:	Precision Manufacturing
Target:		<p>Cleveland-Cliffs is the largest flat-rolled steel producer and largest producer of iron ore pellets in North America. Following its acquisition of AK Steel, the strategic acquisition of ArcelorMittal is the company's next step as it pursues vertical integration.</p> <ul style="list-style-type: none"> <i>Forms fully-integrated steel system, scale to achieve improved cost performance</i> <i>Increased exposure to highly desirable automotive end-markets</i> <i>Creates a more resilient, de-leveraged balance sheet</i> <i>Opportunity to pursue significant cost synergies through facility and supply chain optimization</i> 	
Acquirer:			
Key Metrics:			
Implied Enterprise Value (\$M)	\$3,288		
EV/LTM EBITDA	NA		
EV/LTM Revenue	0.3x		
Date: 12/20/2020 (Announced)		Overview / Strategic Rationale:	Aerospace & Defense
Target:		<p>Lockheed Martin Corporation is a global security and aerospace company. Lockheed Martin operates in four segments: aeronautics, missiles and fire control, rotary and mission systems, and space.</p> <ul style="list-style-type: none"> <i>Aerojet Rocketdyne is an aerospace and defense rocket engine manufacturer</i> <i>The acquisition allows Lockheed Martin to increase its domestic defense industrial base</i> <i>Aerojet Rocketdyne's propulsion systems are a key component throughout Lockheed's four segments, presenting an opportunity for margin improvement through vertical integration</i> 	
Acquirer:			
Key Metrics:			
Implied Enterprise Value (\$M)	\$4,069		
EV/LTM EBITDA	14.3x		
EV/LTM Revenue	2.0x		
Date: 12/28/2020 (Closed)		Overview / Strategic Rationale:	Building Products
Target:		<p>UFP Industries is a holding company with operating subsidiaries that design, manufacture, and distribute building materials and industrial products. UFP's primary products include lumber and lumber-alternative products serving the retail, industrial, and construction markets.</p> <ul style="list-style-type: none"> <i>PalletOne distributes and manufactures pallet-related products and industrial packaging</i> <i>The acquisition of PalletOne expands UFP's industrial business unit by giving the company access to new markets, value-added industrial products, and resources</i> 	
Acquirer:			
Key Metrics:			
Implied Enterprise Value (\$M)	\$232		
EV/LTM EBITDA	6.3x		
EV/LTM Revenue	0.4x		

Source: Company Filings, Pitchbook, CapIQ, News Releases, Investor Reports

Recently Announced & Closed Transactions *(select transactions, not intended to be all-inclusive)*

Date	Acquirer	Target	Target Description	Price (\$MM)	Revenue Multiple	EBITDA Multiple
AEROSPACE & DEFENSE						
12/30/2020	Mercury Systems, Inc.	Physical Optics Corporation, Inc.	Physical Optics Corporation, Inc. designs, develops, and manufactures avionics solutions for both military and commercial aircraft.	\$ 310	2.6x	13.0x
12/21/2020	Raytheon Technologies Corporation	Blue Canyon Technologies, Inc.	Blue Canyon Technologies, Inc. designs and manufactures spacecraft for government, commercial, and academic missions.	\$ 426	-	-
12/18/2020	Moog Inc.	Genesys Aerosystems Group, Inc.	Genesys Aerosystems Group, Inc. designs and manufactures autopilot and avionics systems and solutions for rotorcraft and fixed wing aircraft.	\$ 78	-	-
11/20/2020	Pacific Architects and Engineers, LLC	CENTRA Technology, Inc.	CENTRA Technology, Inc. provides aerospace engineering services for clients with critical defense, intelligence, and security missions.	\$ 208	-	8.8x
7/31/2020	BAE Systems plc	Military Global Positioning System Business Of Collins Aerospace	As of July 31, 2020, Military Global Positioning System Business Of Collins Aerospace was acquired by BAE Systems plc.	\$ 1,925	-	-
BUILDING PRODUCTS						
12/16/2020	Armstrong World Industries, Inc.	Arktura, LLC	Arktura, LLC design and manufactures acoustic design solutions.	\$ 121	3.3x	-
12/14/2020	Fortune Brands Home & Security, Inc.	Larson Manufacturing Company, Inc.	Larson Manufacturing Company, Inc. manufactures storm doors and storm windows in the United States.	\$ 740	1.9x	-
12/9/2020	Chattanooga Renaissance Fund; Brick & Mortar Ventures; EquipmentShare.com Inc.	Branch Technology, Inc.	Branch Technology, Inc. builds walls through Cellular Fabrication technology using 3D printers.	\$ -	-	-
7/27/2020	Armstrong World Industries, Inc.	Turf Design Inc.	Turf Design Inc. designs and manufactures ceilings and wall products primarily used in commercial building applications.	\$ 118	4.7x	-
CHEMICALS, PLASTICS, & SPECIALTY MATERIALS						
12/31/2020	INEOS Olefins & Polymers USA, LLC	Gemini HDPE LLC	Gemini HDPE LLC manufactures high density polyethylene chemicals.	\$ 808	-	-
12/21/2020	Aceto Corporation	IsleChem, LLC	IsleChem, LLC manufactures performance chemical products, such as phosphate esters, epoxy resin systems, specialty monomers, polymers, and conformal coatings.	\$ -	-	-
ENERGY, POWER, & INFRASTRUCTURE						
12/31/2020	Golden Gate Capital	Covia Holdings LLC	Covia Holdings LLC provides diversified mineral-based and material solutions for the industrial and energy markets in the United States, Argentina, Mexico, Canada, China, and Denmark.	\$ -	-	-
12/23/2020	Riverstone Holdings LLC	International-Matex Tank Terminals, Inc.	International-Matex Tank Terminals, Inc. owns and operates bulk liquid storage terminal facilities for petroleum, biofuels, commodity/specialty chemicals, and vegetable/tropical oil products in North America.	\$ 2,685	-	-
SPECIALTY DISTRIBUTION						
12/31/2020	Headwater Companies, LLC	Gicon Pumps & Equipment, Ltd.	Gicon Pumps & Equipment, Ltd. operates as a wholesale supplier of pumps and other water-handling and water-processing equipment.	\$ 28	0.4x	-
12/31/2020	CPS Performance Materials Topco LLC	Handy Chemicals (U.S.A.) Ltd.	Handy Chemicals (U.S.A.) Ltd. distributes poly naphthalene sulfonates.	\$ 9	-	-
12/1/2020	Graybar Electric Company, Inc.	Shingle & Gibb Company, Inc.	Shingle & Gibb Company, Inc. distributes industrial automation, motion control, machine safety, and power transmission products.	\$ -	-	-
12/9/2020	S.W. Anderson Company	O. E. M. Parts & Tools Co.	O. E. M. PARTS & TOOLS CO., doing business as O.E.M. Fastening Systems, distributes specialty fasteners, custom components, and application tools to the automotive, appliance, and outdoor power equipment market.	\$ -	-	-

Source: EdgePoint Proprietary Database, Company Filings, Pitchbook, CapIQ, News Releases

Key Metrics

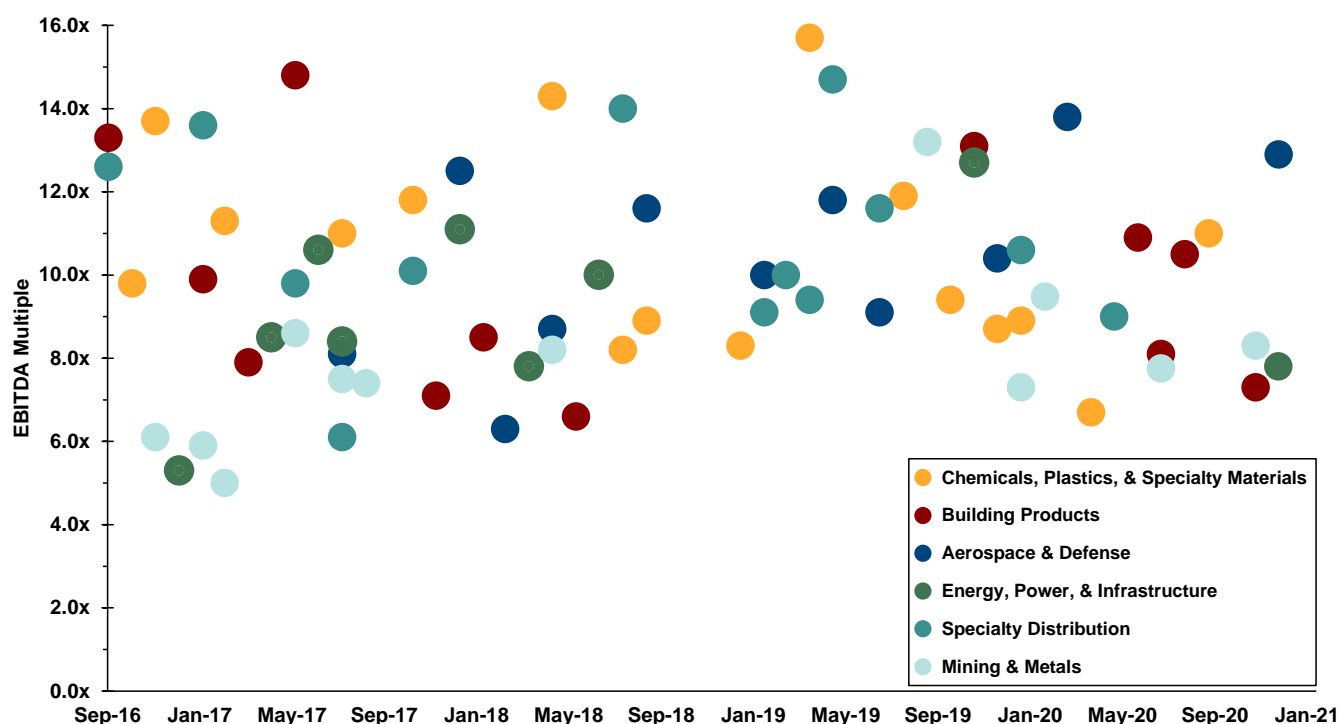
The majority of transaction activity in the industrial landscape during the second half of 2020 occurred in two primary sub-sectors: building products (27%), and specialty distribution (22%). These sub-sectors benefited from strong customer demand as a result of the pandemic. Strong demand in construction and the pandemic's impact on supply have created strong interest in these two sectors.

As evidenced in the table below (Select Transaction Multiples), transaction values across key sub-sectors of the industry have not deteriorated materially despite market volatility as strategic consolidators aggressively bid for high quality acquisition

targets. The average reported EV/EBITDA multiple paid by buyers across the industrial landscape deteriorated slightly from 2019 levels (10.0x) to 9.4x (average transaction size \$250 million), highlighting the ongoing trend of buyers aggressively pursuing high-quality targets.

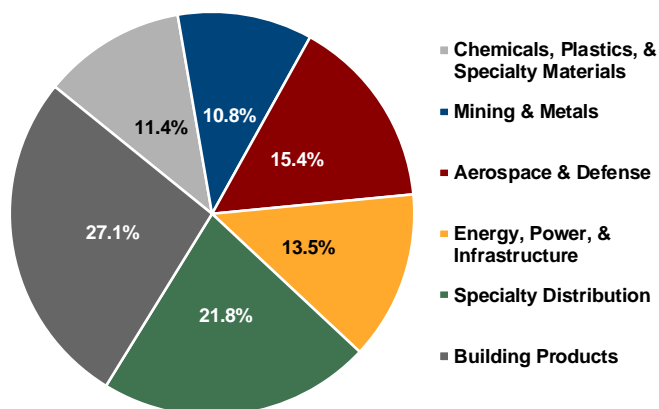
Strategic and private-equity-backed portfolio companies accounted for the majority of transaction activity during the last 12 months. These buyers view the current market dislocation as an opportunity to use M&A to achieve increasing operational efficiencies and scale through targeted acquisitions.

Select Transaction Multiples



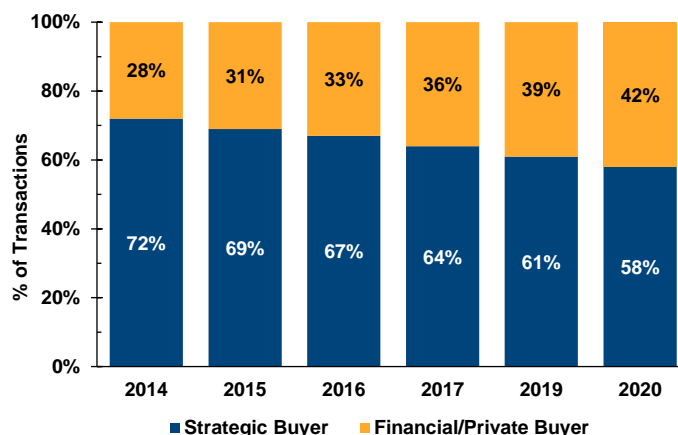
Source: EdgePoint Proprietary Database, Company Filings, CapIQ, News Releases

Transactions by Sub-Sector (2020)



Source: EdgePoint Proprietary Database, Company Filings, CapIQ, News Releases

Share of Transactions by Buyer Type



Sub-Sector Profile: Industrial Distribution

The industrial distribution sub-sector continues to experience robust deal flow from large and middle-market strategic buyers as the economy begins to rebound from the COVID-19 pandemic. The industry is being driven by the ongoing need for consolidation and margin improvement as manufacturers work to increase control and resilience within their supply chains.


As buyers continue to utilize M&A as a means to drive growth and margin expansion, larger and aggressive players will seek to acquire wholesalers with complementary product lines or adjacent geographic coverage. Expect buyers to continue to be highly active as they seek incremental profits through future deals.

Brady Industries, a distributor of janitorial supplies, industrial paper products, and cleaning chemicals, was one of the most active acquirers in the second half of 2020, adding to a long string of acquisitions by closing four transactions between July and December.

Propane and distillate distributor Superior Plus closed two transactions in late 2020 as it fortified its business and prepared to exploit the COVID-19 inspired wave of propane demand in winter 2020-2021. Consumer and commercial demand for the flammable gas was forecast to be up significantly as Americans spend more time outdoors social distancing while awaiting availability of the coming vaccine this winter.

The macro trends behind the ongoing wave of M&A in the industrial distribution sector are expected to continue into 2021, further buoying strong demand for business in the fragmented industry. The deal outlook is expected to remain particularly healthy in the middle and lower-middle markets as private business owners may be encouraged to transact due to potential changes in U.S. fiscal and tax policy decisions made by the incoming Congress and President Biden.

Active Industrial Distribution Buyers

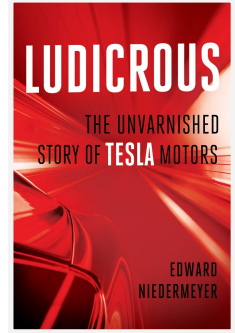
Select Strategic Buyers	Date of Investment	Acquisition Activity
	07/21/2020	<ul style="list-style-type: none"> Praetorian Operating, Inc.
	10/05/2020	<ul style="list-style-type: none"> The Carlson Company
	12/01/2020	<ul style="list-style-type: none"> Topmost Chemical & Paper Corporation
	12/21/2020	<ul style="list-style-type: none"> Kerr Paper & Supply, Inc.
	08/03/2020	<ul style="list-style-type: none"> Champagne's Energy, Inc.
	09/01/2020	<ul style="list-style-type: none"> Rymes Propane & Oils, Inc.
	10/27/2020	<ul style="list-style-type: none"> Petroleum Heat & Power Co., Inc.
	10/16/2020	<ul style="list-style-type: none"> All Products Automotive, Inc.
	12/04/2020	<ul style="list-style-type: none"> IEH Auto Parts LLC
	12/18/2020	<ul style="list-style-type: none"> Irrigation Station LLP
	12/18/2020	<ul style="list-style-type: none"> REAMS Sprinkler Supply Co., Inc.

Interview with Edward Niedermeyer, Author, *Ludicrous*

In 2019, automotive journalist, Edward Niedermeyer published *Ludicrous: The Unvarnished Story of Tesla Motors*. The book profiles the history of Tesla under its high profile leader, Elon Musk. Niedermeyer compiled the book through his own research and hundreds of hours of interviews with current and former Tesla employees.

Niedermeyer recently sat down with EdgePoint to discuss Tesla and other big questions facing the automotive industry.

Since the publishing of Ludicrous in 2019, Tesla has continued to grow in terms of hype, market cap and even unit production. What do you make of the company's progress since the book was published?



As always with Tesla, you have to separate the stock from the underlying reality of the business. The stock growth is not mirroring a similar trajectory in the business, which has continued to grow steadily but has not fundamentally transformed its prospects. In fact, a close and clear-eyed look at Tesla's business shows more signs of weakness than were evident when *Ludicrous* was published in the summer of 2019.

"Time bombs" still tick placidly away and could blow up Tesla's all-conquering image at any time. Chief among these is "Full Self-Driving," but regulatory action, design and manufacturing defects, "stealth recalls," customer revolts at price drops and poor service, and a number of other simmering problems addressed in my book could all turn perceptions upside down at any time. So, while Wall Street apparently sees Tesla's success as being more certain than ever, I see it as being in a riskier place than ever before. Thanks to Wall Street's unique vision, Tesla does have one major bulwark against these looming problems: a bank account swollen by billions in new capital raises.

There is a great deal of conversation around EV's given their limited market penetration. Over the next 10 years, do you see EV's capturing a significant share of the market?

This is a very difficult question, because history has so few relevant examples to draw on. I certainly think that the popular perception has run away from reality, as there are simply very few (if any) signs that the US market is in the midst of a wholesale, organic, consumer-driven shift to pure electric. Perception does often become reality, and the more meaningful shifts in the EU and China could help nudge the US in that direction. But the growth of EV share in both of those markets also helps identify the missing factor in the US: meaningful policy support. Given the dysfunctional state of the US political system it's difficult to predict a truly paradigm-altering EV stimulus package any time soon, and without that I would expect slow, steady growth in the US, mostly in the premium segment, and mostly driven by new product introductions. Of course, the "wealth effect" of the EV startup "meme stonk" phenomenon could have an unpredictable impact on the political equation, as could climate change-tied natural disasters and other "black swan" events. Another factor to keep an eye on is the growing chatter around national security and EV supply chains, which could also ramp up dramatically in the event of a global confrontation between the US and China or a strong Pentagon move toward zero-emissions. All that said, it's just as likely that something causes the "meme stonk" bubble to burst which could in turn set back EV investment and adoption. This is simply a moment when the future direction is particularly difficult to predict with any certainty.

How will legacy supply chain will be impacted if EV's comprise a meaningful share of the market?

Obviously, anyone who is dependent on internal combustion-specific components will need to diversify or face long-term constraints on growth. The more specialized lower "tier" suppliers tend to face the most risk in this regard, as well as the biggest challenges in diversifying into new businesses. Even if pure EVs don't immediately take a meaningful share of the market, electrification will continue (see: hybrid sales growth is continuing organically) so supplying electrification-related components that can be used in everything from 48V mild hybrids through pure BEVs will be especially appealing as targets for diversification in this uncertain moment. A strong premium EV market in the US (with an emphasis on performance), and the success of the Porsche Taycan, also suggests that EV- and electrified drivetrain-specific transmissions may become more of an opportunity than many had anticipated. The current chip shortage roiling the industry also confirms that anything used in both cars and computers/gaming consoles/smartphones/devices are an appealing business to be a supplier in ... but of course, there are few opportunities for established automotive suppliers to move into those kinds of spaces.

What We are Reading:

Covid-19 Propelled Businesses Into the Future. Ready or Not. (Wall Street Journal)

The changes brought on by COVID-19 in the workplace and elsewhere are here to stay. The digital age has been in effect for the past decade but has only been accelerated in the last 11 months. Consumers and businesses are choosing internet, software, and the cloud over material items and experiences. This is evident in their spending and how they are conducting business. Economic output is even lighter due to this dramatic shift to digitalization. Technology is now making virtual experiences possible and more life-like for the e-commerce industry. The shifts from fossil fuels to renewable energy and information technology are also getting increased attention.

The National Center for the Middle Market 4Q2020 Middle Market Indicator (Middle Market Center)

2020 created uncertainty for the world and the middle market. The adverse effects have had lasting impacts, which will continue throughout 2021. Revenues on average are down 1.2% and employment has decreased by 2.2% over the last 12 months. The middle market currently has a better handle on the economy than it did six months ago and is continuing to adapt. 2021 is expected to feature revenue and employment growth. 44% of firms expect to have an increase in sales in 2021. The main challenge will be to increase sales and promptly fill orders.

Emerging Opportunities in 3D Printing (Middle Market Growth)

Additive manufacturing provides a variety of opportunities for manufacturers, especially in the space industry. Additive manufacturing is used to create and build prototypes, satellites, and other equipment used in space. It can also be used to design jewelry and medical products, among other applications. The challenge additive manufacturing must overcome is to change the way people currently build products and think about building those products. Petrochemical firms in the middle market can use additive manufacturing to their advantage by finding new ways to develop the powders and resins they sell. Manufacturers should focus on identifying applications for additive manufacturing in their businesses.

Shell Hits Peak Oil, Plans to Reduce Output (Wall Street Journal)

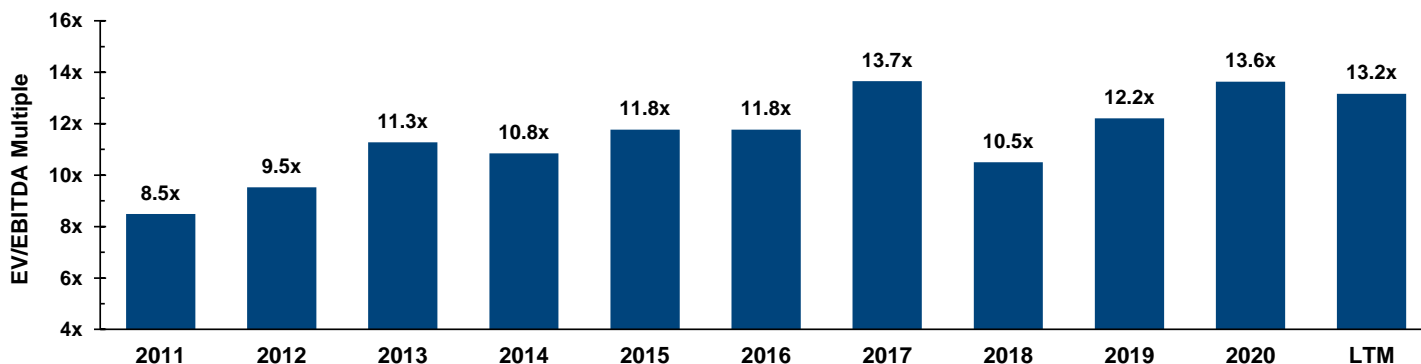
Shell is following suit with other big players in the energy industry and has decided to shift its focus on renewable energy. Shell foresees the decline in oil demand and oil production in years to come. To get ahead of this change, Shell has decided to decrease its oil output by 1-2% per year and instead invest in building out EV charging stations. The company acknowledged that fossil fuels will continue to be a focus in the short-term, but it is only a matter of time until momentum swings further towards renewable alternatives. Shell's recent statements are reflective of its plans far into the future. The company expects fossil fuel production to continue to be its main source of revenue into the 2030s. In the short-term, Shell plans to invest as much as 25% of its expenditures on initiatives related to renewable energy.

Lumber Prices Notch Records on Building, Remodeling Boom (Wall Street Journal)

Even in its offseason, and despite COVID-19, the lumber industry has continued to thrive. Many Americans turned to home improvement during the pandemic, pursuing renovations and DIY projects. Popular engineered wood products are in short supply, causing the price of lumber to remain at elevated levels. High prices and high demand can also be attributed to the increase in building permits and housing affordability driven by the current low-interest rate environment.

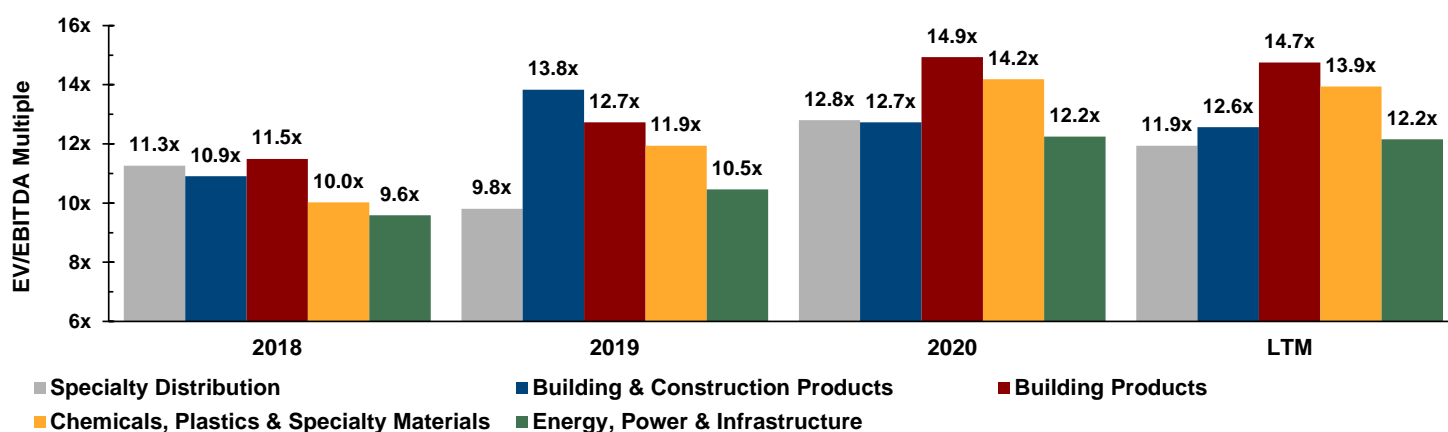
Public Company Comparisons Trading Multiples

Industrial Public Comparables Composite: EV/EBITDA Multiples



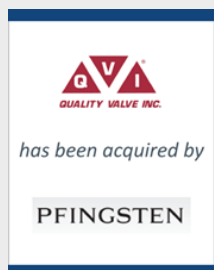
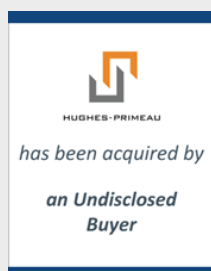
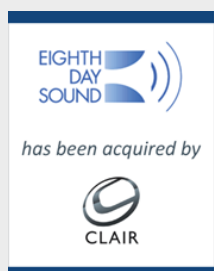
Source: CapIQ, public trading data as of January 31, 2021

Industrial Sub-Sector Public EV/EBITDA Multiples



Source: CapIQ, public trading data as of January 31, 2021

Representative EdgePoint Industrial Transactions



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