Fluid Handling Industry M&A Update
June 2023

Overview

The M&A activity in the fluid handling industry remains robust. Valuations in the middle and lower middle market have rebounded from a dip in Q4 2022. The interest by corporate and private equity buyers in making acquisitions remains strong driving competition for quality opportunities**.**

Activity Level

Year	2018	2019	2020	2021	2022	YTD 2023*
Transactions	67	71	69	102	105	42

Figure 1 - Fluid handling activity level by number of transactions in prior years and YTD 2023
Source: Global Equity Consulting, LLC research
* 5 months ending May 2023

Period	Q1 2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023
Transactions	23	24	37	21	25

Figure 2 - Fluid handling activity level by number of transactions quarterly
Source: Global Equity Consulting, LLC research

M&A activity in the fluid handling industry (FHI) remains very strong - YTD we are at a run-rate that is on par with the prior two years (2021 and 2022), which both saw historically high levels of transaction activity. On a quarterly basis Q1 2023 was up slightly YOY and sequentially.

The activity level in the FHI in the second half of 2022 and Q1 2023 stands in contrast to the general M&A activity worldwide where the YOY transaction activity is off by 40% and about flat with a low activity level in Q4 2022 according to data from PitchBook's Q1 2023 Global M&A Report.

The FHI activity was helped with a step up in private equity activity YTD 2023 (5 months ending 2023) accounting for 31% of the acquisition activity vs. a typical percentage in the low 20s.

There was a significant shift in mix of types of businesses targeted - in 2022 62% of the targeted businesses were manufacturing businesses. YTD 2022 only 36% of the targeted businesses are in manufacturing with a significant shift toward distribution and services businesses.

There are probably multiple factors at work driving this shift -

- The distribution and services sectors are fragmented with smaller players. This fits with buyers looking for aftermarket opportunities - an uncertain economic outlook is perhaps causing buyers to be cautious in making aggressive moves to acquire capital goods manufacturers, while at the same time looking to create ongoing inorganic growth opportunities.
- The smaller companies typically trade at lower valuation multiples and thus are easier to finance during this period of tighter liquidity and higher cost of debt.
- The smaller tuck in acquisitions may be easier to assimilate and may have more cost synergy benefits of being part of a larger organization.

Valuations

There is not a notable change in valuation multiples in the FHI. Since most of the transactions are private or small enough that public companies are not required to disclose the deal terms there are only a small number of transactions where the terms are disclosed. Those tend to be the larger public transactions for which the deal terms are not representative of the broader middle and lower middle market. However, GF

Data® does track middle and lower middle market private equity transactions. Their data shows that for transactions in the range of $10 - $500 million enterprise value, the transaction multiple averaged 8x the trailing twelve months adjusted EBITDA in Q1 2023 vs. 6.8x in Q4 2022 and an average of 7.6x for all of 2022 with approximately the same number of transactions reported.

The Q1 2023 average rebounded despite higher borrowing costs that drove deals to be done with more equity and less debt than has been the case in recent years. This would indicate there is an ongoing demand and competition for quality acquisitions.

Below are the median FHI transaction values for the prior three years. As we get additional data through 2023, we will add that information in future articles.

Year	# of Transactions	EV/Revenue	# of Transactions	EV/EBITDA
2022	**12**	**1.4x**	**5**	**10.0x**
2021	**13**	**1.7x**	**4**	**10.4x**
2020	**10**	**0.9x**	**3**	**10.8x**

Notes:
EBITDA - earnings before interest, taxes, depreciation and amortization
EV - enterprise value is the combined amounts of market capitalization, minority interests, preferred stock and net debt;
Revenue - amount recorded as net sales for the period

Notable Transactions:

1. **Xylem acquired Evoqua in an all-stock transaction that valued Evoqua at approximately $7.5 billion.** Prior to the transaction Evoqua had an annual revenue of $1.7 billion with an adjusted EBITDA of $300 million. The combined Xylem and Evoqua business will have an annual revenue of $7.1 billion and adjusted EBITDA of $1.2 billion. The company expects to achieve $140 million in run-rate cost synergies within three years of the transaction.

   The parties state the transaction creates the World's most advanced water solutions and services business at scale and their complementary capabilities unlock organic and inorganic growth opportunities.

   The transaction was announced in January 2023 and has closed.

2. **Chart Industries Inc. acquired the UK based Howden Group Limited from private equity firm KPS Capital Partners.** The transaction consideration will be a combination of cash and preferred stock that values the Howden business at $4.4 billion. Howden had revenues of $1.8 billion for the trailing 12 months ending August 2022 with an adjusted EBITDA of $340 million.

   The company states the transaction is strategically compelling:

   - Approximately doubles Chart's revenue and further enhances their differentiated position in energy transition
   - Enhances Chart’s business mix by adding new core capabilities in gas compression, increasing aftermarket capabilities and expanding global footprint
   - Enhances Chart’s alignment with secular mega trends

   The transaction was announced in November 2022 and closed in March 2023.

3. **Honeywell has agreed to acquire Compressor Controls Corporation (CCC) from Indicor, LLC (owned by Clayton, Dubilier & Rice and Roper Technologies) for $670 million.** CCC is a leading provider of turbomachinery control and optimization solutions, including control hardware,

software and services, and primarily serves the LNG, gas processing, refining and petrochemical segments. The purchase price is approximately 15x 2023E EBITDA on a tax adjusted basis,

The company states the combination of the company's existing offerings will provide the most complete end-to-end portfolio of products for operational control, safety, and asset performance management of compressors, turbines, generators and other turbomachinery in the LNG, gas processing, refining and petrochemical segments.

The transaction was announced in April 2023 and is expected to close in the second half of 2023.

Outlook

Based on a sampling of Q1 earnings reports it seems the FHI had a very good start to 2023 with a number of companies improving their guidance for the year. However, there is also a high degree of cautiousness regarding the second half of the year. While supply chain inflation and disruptions are improving, they are still headwinds to a certain extent. The highest level of concern is with the economic outlook and the potential impact on demand in 2024. Many companies have sufficient backlog to get them through 2023 so the concern is more about a possible recession and the impact that could have on demand in 2024.

The impact of that concern as well as continued high interest rates and the somewhat restricted availability of debt to finance acquisitions would logically create a slow-down in M&A activity - but it has not had that impact to date in the FHI activity, except perhaps at the higher end of the middle market. Given the uncertain economic outlook and financial market conditions, the current buyer reaction of focusing on smaller companies with a significant aftermarket component makes sense. Consequently, I would expect the current level of activity to continue with a focus on the lower middle market and competition for high quality businesses to provide support for valuations - unless interest rates or other factors push the U.S. economy into a recession that buyers believe is going to last for an extended period. Given the current level of activity and valuations it seems the buyers are not expecting a hard landing and therefore I would expect the current level of activity and valuation to persist.

About the Author:

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