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Disruptions to supress financing

The massive influx of economic, geopolitical and structural changes, disruptions and uncertainties are depressing M&A, equity prices and debt financing

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The downturn in chemicals stock prices, M&A and financing markets is being driven by dramatic changes in the economic, geopolitical and financial environment.

The list of challenging disruptions and structural changes is long and complex.

It includes serious economic changes (inflation, the potential for a recession globally, spiking oil and energy prices, higher interest rates, the ongoing impact of COVID-19 and the China lockdowns); geopolitical challenges (rising tensions with China, the Russian invasion of Ukraine and its impact on oil and gas prices, and availability of many commodity and food products); regulatory pressures (net zero carbon, green chemistry); and structural problems (shift to electronic vehicles, supply chain issues, shortages of semiconductors, shortages and higher cost of labor). All of these factors are contributing to an environment of great uncertainty and pressure on profits and growth.

Falling equity prices

Overall stock prices have been coming down dramatically since the beginning of the year along with chemical company share prices. Only our US Basic Chemicals and Fertilizer Indices increased in Q1. All of the others decreased and, in many cases, dropped more than the overall market.

Until the overall stock market recovers, we do not expect any consistent improvement in public chemical company share prices and valuations. Given the factors that are hurting the stock market, we do not see a turnaround for some time.

Slowdown in M&A

Based on our detailed data analysis through Q1 2022, there has been a dramatic slowdown in M&A thus far this year, driven by the torrent of economic, geopolitical, and structural disruptions. In Q1, only 13 deals greater than $25m in value closed, for a total dollar volume of $10.4bn. This compares to 85 deals worth $72.8bn for all of last year.

The slowdown in larger deals started in Q4 2021, but is shifting into a major slowdown in the number of deals this past quarter. Compared to the 13 deals closed in Q1, 24 deals closed in Q4 2021.

There is also a shift in the geographic mix of transactions away from Asia and significantly towards the US and Europe. Private

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equity's ,share of deals increased on small volume and specialty chemicals gained a higher share of transactions over commodity chemicals.

Why the slowdown? In this uncertain environment that is coupled with high valuations and higher interest rates, CEOs are less likely to pursue large deals and discretionary deals such as diversification acquisitions. Nevertheless, strategic divestitures and acquisitions will continue.

What is our prediction for Chemicals M&A in 2022? Strategic divestitures and acquisitions will continue and drive at least a moderate level of M&A activity. Overall, the pace will be slower this year than last year, but the volume will still be higher than previous trough years.

Valuations will only come down slowly since buyer demand still is stronger than the supply of businesses to buy, along with a preference for specialties over commodities.

Debt financing falls dramatically

There was a massive drop in debt financing in Q1, both for investment grade and high yield.

Global non-bank debt financing fell dramatically to $7.8bn in Q1. This compares to $51.3bn for all of 2021.

Investment grade debt issuance was $7.6bn of the total in Q1 compared to $40.4bn for all of 2021.

Only $0.2bn of high yield debt was issued in Q1 2022, a major drop when compared to the $10.8bn issued in all of 2021.

With only a modest number of M&A deals to finance, and rising interest rates, the demand for new debt or to refinance existing debt has been anemic. Debt financing is available but the needs have diminished.

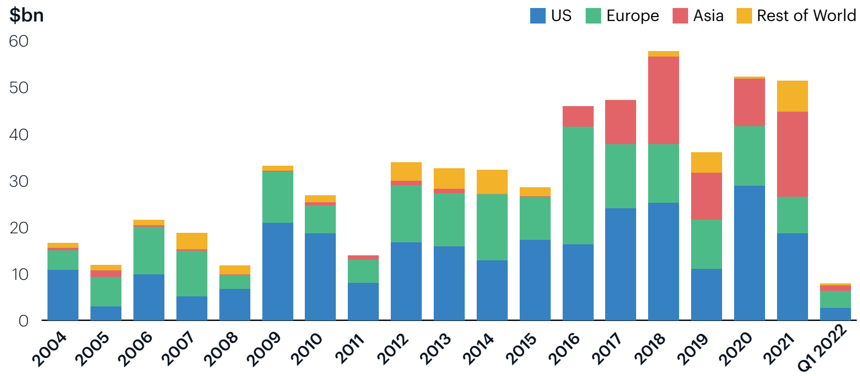
In a falling stock market environment, it is not surprising that overall chemical industry equity financing volume fell in Q1.

In Q1, $3.9bn of equity was issued via 17 offerings. This was a significant drop compared to the $22.3bn of equity issued via 116 offerings for all of 2021.

Surprisingly, the volume of chemical company initial public offering (IPOs) did not fall as much. 12 IPOs worth $3.5bn were completed in Q1 compared to 58 IPOs in 2021 worth $11.2bn. The pace of the number of IPOs fell moderately, but the dollar volume held up. This is in contrast to overall equity issuance which softened considerably. Asian issuers continued to dominate the IPO market.

We do expect, however, that chemical overall equity issuance and IPO activity will be soft for the rest of 2022 due to overall market conditions.

Global chemicals non-bank debt financing



Source: Young & Partners

Disruptions to supress M&A activity

In summary, the massive influx of economic, geopolitical and structural changes, disruptions and uncertainties are suppressing chemical industry share prices, M&A activity and debt and equity financing. None of these areas of activity are at trough levels, but they are clearly subdued versus the more robust activity in recent years.

These trends will continue through the rest of 2022. If there is any alternative scenario, it is a more pronounced downside case where economic developments (particularly in China and in Europe) are worse than current expectations, especially if there are more severe negative developments in Ukraine. ■

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