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Kicking the tires for deals

Stars align for even more auto supplier integration

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Market conditions seem ripe for increased mergers and acquisitions among Michigan's automotive suppliers.

Production volume is on track to hit 16.2 million units this year — up 88 percent over 2009 — and new model launches are coming in droves in 2014. Profits are solid, as lean suppliers crank out parts and try to keep up with demand.

Not surprisingly, a growing number of auto industry executives expect to pursue an acquisition during the next year, especially deals of more than $50 million.

In effect, "the industry is growing faster than most suppliers are able to grow," said Jim Carter, Americas automotive transaction advisory leader with **Ernst & Young**.

While credit is improving, cash is dominating near-term deal financing, according to EY's auto industry Capital Confidence Barometer report, which Carter co-authored. More than half of respondents to EY surveys pointed to cash as their primary source of deal financing, and reported that their debt-to-capital ratios were expected to creep up.

Even among suppliers that have cash to fund strategic acquisitions, many have been prudent in approaching deals because of the steep increase in valuations that's corresponded with the recovery. That's created a value expectations gap, Carter said.

Sellers wanted to sell based on precrash multiples and their current historically high earnings, but buyers have had a difficult time letting go of the expectation that they could pay the lower multiples that were available during the crash.

"Because there's a significant difference between tho That gap appears to be closing as buyers move toward seller valuations and more companies open up to the idea of divesting non-core divisions or subsidiaries, he said.

"Right now, there are a lot of factors coming together to suggest it's a good time to be a seller," Carter said.

That's good news for companies like Auburn Hills-based **TI Automotive**, a global supplier of fuel delivery and storage systems that had about $3 billion in revenue last year. According to reports, the company is working with **Deutsche Bank AG** to identify potential suitors for a deal that's expected to fetch about $1.5 billion.

That's also good news for private equity firms that gambled on distressed auto supplier assets during the depths of the recession and are now exiting those deals.

One of the largest deals involved **The Carlyle Group** selling Plymouth-based **Metaldyne LLC**, a $1 billion maker of engine and transmission components to **American Securities LLC** for $820 million in December 2012.

American Securities in October 2012 also picked up forged parts supplier **HHI Group Holdings** of Detroit from **KPS Capital Partners LP**.

Other recent private equity deals include the sale of legendary piston-ring maker **Hastings Manufacturing** by Bloomfield Hills-based **Anderson Group LLC** to **RFE Investment Partners** of New Canaan, Conn., and the merger of **Platinum Equity**-owned **Diversified Machine** and **SMW Automotive**. The new entity is expected to have combined revenues of $1.2 billion.

A few strategic buyers are stepping up to add capacity.

Valley City, Ohio-based **Shiloh Industries Inc.** acquired aluminum die-cast component supplier **Contech Castings** for $54.4 million from **Revstone Transportation LLC**, a carve-out from former parent company Revstone Industries, which filed for Chapter 11 bankruptcy last December.

While activity has been slow for the larger deals, the lower middle-market has been busy in the past two years, said Matt Miller, managing director at **BlueWater Partners LLC** in Grand Rapids. Deal volume in that size doubled in 2012, and activity this year is remaining roughly on pace with last year, according to Miller.

"We've seen heightened interest in the auto supply chain, which a few years ago was out of favor," Miller said. "I dare say that now it's in favor."

Average transaction size is up, while valuation multiples for motor vehicle parts manufacturers dipped slightly to 5.6 times earnings before interest, taxes, depreciation and amortization (EBITDA), according to proprietary data Miller tracks.

Unlike in previous cycles when buyers really honed in on certain segments of the automotive market, deals among strategic buyers have been spread across the supply chain, said Carter of EY. That said, buyers tend to covet powertrain-related technologies and electronics, particularly those that help create a long-term, sustainable competitive advantage, he said.

The attractiveness of the technology and a desire to put some of its nearly $600 million in cash to work led Zeeland-based **Gentex Corp.** (Nasdaq: GNTX) a tier-one automotive supplier of auto-dimming rearview mirrors, to acquire the **HomeLink** business from **Johnson Controls Inc.** (NYSE: JCI) of Milwaukee, Wis. Gentex funded the deal with $400 million of its own cash and $300 million in debt financing.

Miller of BlueWater Partners said the capacity constraints should start to spur more deals as suppliers have been stretching their plants and their workers.

At the same time, more private equity funds are forming in Michigan, and outside funds are again starting to take notice of opportunities in the state as its economy and its manufacturing sector continue to improve, Miller said.

"A few years ago, if you were sitting in California and picked up a national paper and read about Michigan, most people wouldn't be interested in investing in Michigan," he said. "The auto turnaround and the overall economic turnaround (has) renewed interest in Michigan. To say we're thriving might be a stretch, but I think the worst is behind us; we've survived, and the trend is positive."■