American Metal Market

SSS: Sentiment upbeat for M&As, financing

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NEW YORK — Sentiment has ticked up in recent months for metals financing and steel mergers and acquisitions (M&A) activity, according to a panel of investment and commercial bankers.

With better steel market conditions in 2017, it's easier for steel companies to access bond and institutional loan markets, which showed virtually no activity as recently as June 2016, BMO Harris Bank managing director Andrew Pappas said, speaking at a June 27 panel during *AMM*'s Steel Survival Strategies XXXII conference in New York.

As steel companies are growing again, it's a good time to be a lender and a borrower. "Companies are growing again. They're taking their profits, they're trying to increase (and expand) their facilities, partly because of metals price increases," he said. "It's a good time to be a lender and actually it's a very good time to be a borrower, in my opinion."

Valuation multiples are high, too, as companies look for inorganic ways to grow, investment banker Vincent Pappalardo, managing director of Browns Gibbons Lang & Co., a major metals investment bank, told delegates.

With the economy at roughly 2% gross domestic product growth, it's hard to score strong organic growth, he explained. Steel companies have lately ventured further into downstream manufacturing sectors, including parts production, he said, citing service center acquisitions in particular.

"The service center industry is kind of invading the fabrication industry quite a bit recently," Pappalardo said. "They're moving downstream, meaning they're looking for higher margins and more processing."

Steel companies that are systematic in such purchases—with big and frequent acquisitions—have tended to outperform peers in revenue, earnings growth and shareholder return, at least from 2007 to 2017, according to an analysis by Headwall Partners, an independent corporate finance firm.

Indeed, they typically beat steel companies that are more hesitant in acquisitions, namely those that make smaller acquisitions less often.

One reason for this: There's been little fundamental growth in steel demand from 2007 to 2017, Headwall managing partner Peter Scott said.

In 2007, apparent US steel consumption came to 130 million tonnes. That figure shrank to 106 million tonnes by 2016, Scott said, citing American Iron and Steel Institute (AISI) data, but noting that period takes a pre-recession boom as a starting point.

Acquisitions can be a way of gaining new customers without sacrificing margins, as a result of intense market share competition, Scott said. In addition, pro-manufacturing rhetoric from President Donald Trump has spurred confidence in capital outlays, both for investors and for industry executives.

Trump's agenda, which includes some trade protectionism, has encouraged investors to be more cheerful about the metals sector and executives to be more optimistic about betting on American operations, such as with capital expenditures.

"They feel as though things are going to get better. They don't know exactly what it's going to look like. But that confidence about things getting better, about a focus on fair trade and a focus on manufacturing in general, gives them the confidence to go out and place those bets," Scott said. "And that is good … in terms of having capital at our disposal to pursue growth."