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Advanced Manufacturing
Global Capital Confidence Barometer

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A note from David Gale, EY Global Advanced Manufacturing Leader, Transaction Advisory Services

Search for new markets and technology fuel M&A, but quality targets harder to find

Advanced manufacturing (Mfg) companies continue to have a solid M&A appetite as they seek out new geographic markets, the right technology to offer customers comprehensive solutions and the people who understand that technology. In fact, half of the Mfg sector executives surveyed for the 19th edition of our *Capital Confidence Barometer* said they plan to actively pursue M&A in the next 12 months, exhibiting a stronger inclination for dealmaking than shown by their global peers.

More than a quarter (28%) of executives said entering new markets was the strategic driver behind M&A. Another 20% cited changing customer behavior and 18% noted the need to acquire talent.

That need for talent is not only a reflection of tightening labor markets, but also a sign of how technology and digital are changing the sector. When looking at the major themes in M&A over the next 12 months, an increase in cross-sector M&A driven by technology and digital, and an increase in private equity as a major acquirer of assets, are tied (28%) as the most frequently cited theme.

Divestiture activity is helping to drive dealmaking as the sector continues to respond to the push by investors for companies to focus on their core capabilities. Two-thirds (66%) of Mfg executives said their companies now review their portfolio more than once a year to seek divestment opportunities and almost three-quarters (72%) said that they identified an asset to divest as a result of their latest review. The risk of disruption from forces such as technology, convergence or geopolitical uncertainty was cited by 40% as the reason for the divestiture, while 32% cited underperformance of the asset.

Rapid changes in global trade policy in 2018 have introduced a level of unpredictability to M&A, so it is no surprise that regulatory and political uncertainty were named by nearly half of executives as the leading risk to dealmaking. Companies are also looking for more cross-border deals to mitigate potential trade policy impacts on operations, market access and supply chains. More than one in five executives (21%) said they were focusing on more cross-border opportunities as a result of the current trade climate.

Meanwhile, 23% cited difficulty in finding high-quality assets. As I talk with sector executives, the general sentiment is that the quality of available assets is medium, at best. At the same time, the record level of PE dry powder is helping drive up valuations.

This makes it imperative for companies to maximize synergies when they integrate an acquisition. But almost half (48%) said they failed to achieve the level of projected synergies. When asked what they are doing differently to increase the likelihood of capturing synergies, 52% said they planned to start integration earlier and 25% said they were being more aggressive in setting synergy targets. Our recent Buy & Integrate series examines the leading practices for capturing synergies.

Successfully onboarding and retaining talent was one of the biggest integration challenges mentioned by Mfg executives. Many Mfg companies are looking outside their sector to acquire technology companies. However, cultural differences in cross-sector deals can lead many executives and skilled workers to leave their careers at the newly merged entity.

There is plenty of uncertainty in the M&A environment as Mfg companies face challenges in finding assets, retaining talent and adapting to an uncertain regulatory environment. But the M&A appetite remains stronger in the sector than for companies as a whole.

With current valuations, it is essential for companies to regularly review their portfolios to determine what to divest and where to invest — whether through M&A or otherwise.

Strength in global markets

Strong corporate earnings and open credit markets point to a continued upswing in equity markets.

85%
see the global economy as improving.

86%
see global corporate earnings improving.

78%
expect equity valuations and the stock market outlook to improve.

Confidence in dealmaking

Sector executives see the M&A cycle continuing at elevated levels. An ongoing focus on core operations is increasing the rates at which portfolios are reviewed. Executives are confident about demand for divested assets.

91%
expect the global M&A market to improve.

66%
are reviewing portfolios more than once a year for divestment opportunities.

57%
expect deal completion rates to improve.

Challenges from talent, synergies

With intense competition for skilled talent in the Mfg sector, successful onboarding and retention after an acquisition is key. Synergies are falling short of targets for many companies, leading some to start the work of integration sooner.

23%
named the onboarding and retention of talent as the leading challenge in post-deal integration — the top challenge noted.

48%
did not achieve the synergies expected after completing their most recent acquisition.

52%
plan to start integration processes earlier during their next deal to capture greater synergies.

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