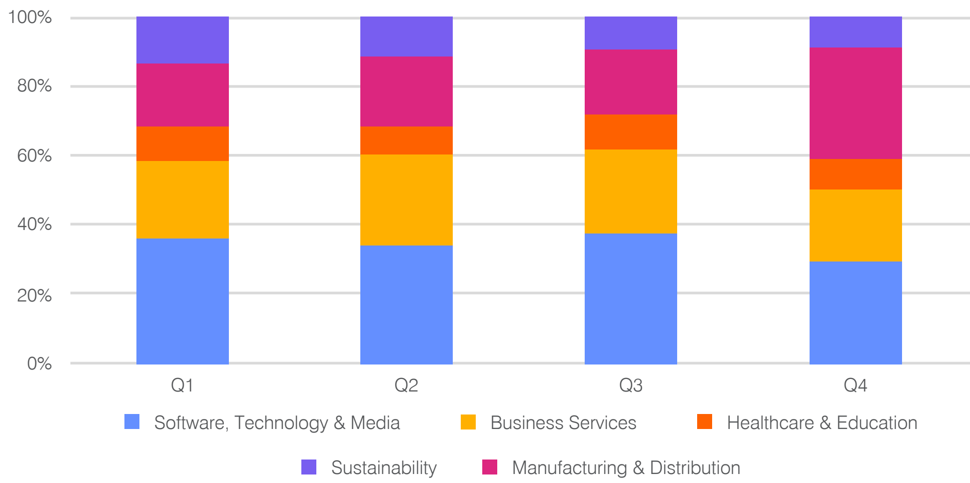
Manufacturing & Distribution

2024 Sector Review & 2025 Outlook

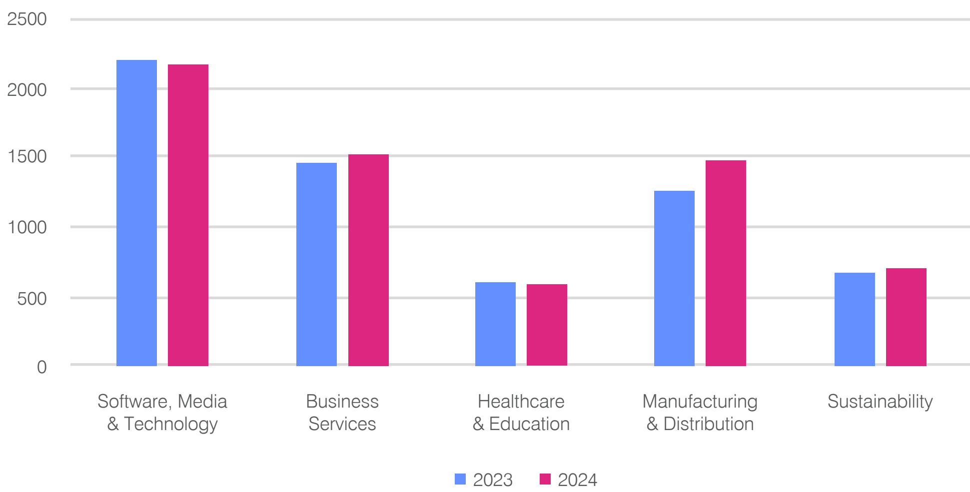
2024 Market Overview

- A major election year – the US, UK, France etc.
- Improving borrowing conditions – Table has finally turned on interest rates – both The Bank of England & The Federal Reserve cut rates in 2024
    - BofE cut rates to 4.5% in February 2025 - down from the peak of 5.25% in August 2023
    - Fed Rate down to 4.5% in December after three cuts across the 2024 from peak of 5.5% in July 2023
- UK borrowing costs are still high – Yields on Gilts almost reached same level as in 2008 – but the outlook is positive for lower and middle market dealmaking in 2025, with market confidence high that interest rates are no longer headed up.
- Key Theme of Digitalisation - continues to disrupt all industries
    - AI-enabled SaaS – enables a new category where service is delivered as a product – e.g. SmarterDx
        - Enables B2B firms to outsource entire functions – this targets operating expenses rather than the typically smaller IT and software budgets
        - Provides opportunities to leverage unstructured data
    - Investors eager to grasp opportunities to put traditional businesses on a platform
- Different impacts of regulation affecting the sustainability sector across the globe
    - In the EU, stricter reporting guidelines were introduced this year. The Corporate Sustainability Reporting Directive (CSRD) requires large and listed companies to share information on how they monitor a wide range of ESG issues and their impact
    - In contrast, since the y/e the new US administration has issued executive orders to promote domestic fossil energy production and rolling back regulations, such as departing from the Paris Climate Agreement. However, individual states such as California and New York set the blueprint for pro-ESG regulation, pushing for more transparency from large companies. The battle between state vs. federal sustainability regulation will continue into this year

Deals across PCF's sectors in 2024



UK Deal Activity in 2023 vs 2024



Source: Pitchbook, Excludes deals with a stated value of >£500m

M&A Activity: Trade VS. Private Equity

Private Equity: Bounce back in 2024

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- Overdue improvement in Private Equity (PE) led dealmaking in 2024 – 2025. Focus will be on exiting accumulated portfolio companies to get cash back to LPs and recycled into new PE funds.
- Strong uptick in European activity – estimated 18% increase YoY after a lull in deals in recent years due to high borrowing costs.
    - Number of deals estimated to return to 2021-22 levels
- Similar trend in the US and globally – estimated 13% and 12% increase in deal value respectively – with a return to 2022 levels (not yet at 2021 peak)

Trade: Continued Corporate Dominance

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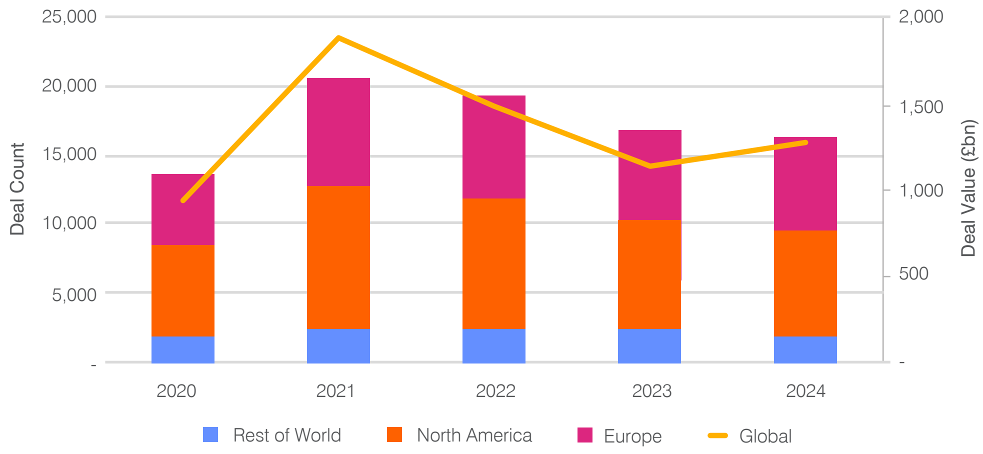
- Corporate-led activity demonstrated greater resilience during the downturn in global deal making over the past two years, and accounted for 63% of UK M&A activity in 2024.
- The gap between PE and trade has however meaningfully closed over the past decade – PE has caught up from a 49% difference in share of M&A value in 2014, to accounting for 47% of M&A activity in 2024. The expected uptick in PE exits will boost firms' confidence and appetite for new deal making in the coming decade.
- The global M&A rebound is in full swing: Recent interest-rate cuts and an uptick in buy-out activity does suggest a resurgence in both PE and Trade activity, particularly as corporate strategics maintain greater buying power impacting M&A activity in the short term.
- Recent eased recession fears amongst C-Suites also prompts acquisition confidence.

Global PE Deal Activity



UK PE Buyout Activity since 2020

Source: Pitchbook, Excludes deals with a stated value of >£500m

Investor Appetite: Key Themes

Access to Financing and Funding:

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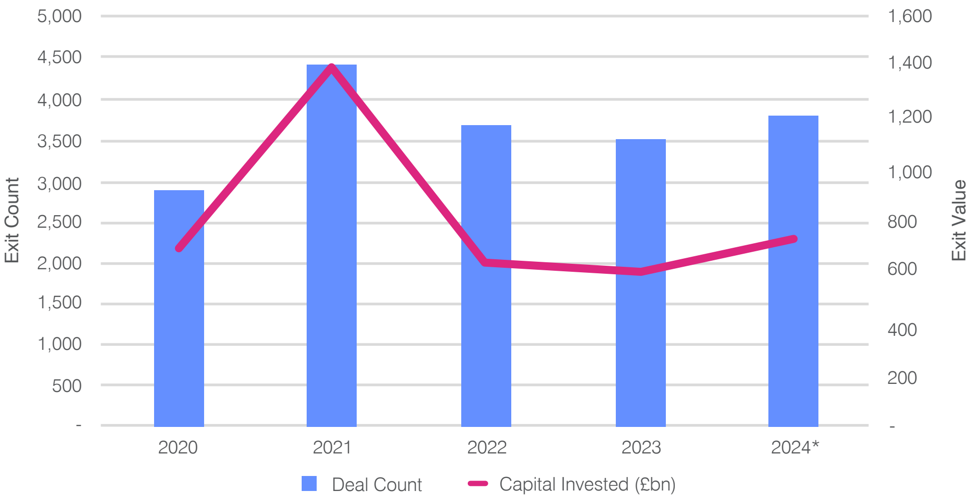
- High-interest-rate environment and recession expectations resulted in smaller growth equity transactions, with PE firms still sensitive to record-breaking rates.
- PE fundraising is a lagging indicator, and after three consecutive years of strong activity, is expected to slow in 2025 because of the disrupted cash flow cycle.
- PE dry powder by the end of July 2024 stood at £2.1tn globally – up c.4% from the start of the year.
- Corporates are cash heavy and ready to acquire
  - During the recent years of economic uncertainties, businesses have been stockpiling cash through a combination of streamlining operations and hesitancy for large spending [Kornferry]
  - Non-financial corporations in the S&P500 started last year with 56% of cash and cash equivalents, and during 2024 bolstered cash on their balance sheets to a record £2tn [JPMorgan Chase]
- Listed acquirors have also benefited from high-valuations, strengthening their financing capacity further

Global PE Exit Activity



NB: Estimated final data for 2024 exit value

Source: Pitchbook,

PE Exit Activity

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- PE firms have struggled to realise an acceptable price for their assets against the combined backdrop of Covid followed by interest rate increases, with longer hold periods evident across portfolios as a result. At the start of 2024:
  - The PE sector was sat on a record 28,000 companies (according to Bain) with a collective value of £2.5tn.
  - The proportion of those assets held for more than five years was up 18% on end of 2022.
- With 10-year funds being the norm, pressure to divest demonstrate returns in order to raise follow-on funds is increasing. Fortunately, interest rates have levelled off and the trajectory looks downwards (albeit unclear to what degree and over what timeframe). Signs of more exit activity are being seen as a result. We anticipate an uptick in exit activities in 2025, with the recycled cash driving increasing funds available for reinvestment:
  - 9% YoY increase in 2024 for the global PE exit counts
  - PE exit activity consistently increased across Europe and the US - 17% YoY for US & 19% YoY for Europe

2024 Sector Highlights

Manufacturing Continues to Support the UK Economy

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- The past 12 months have once again demonstrated how important manufacturing is to the UK's economic growth:
  - 8.1% (2.6 million jobs) of employment [ONS 2024]
  - 8.8% (£217bn) of total UK economic output (GVA)
  - 45% of UK exports
  - £38.8bn worth of investment into the sector

Sector wide implications

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- Skilled-labour shortages driving adaptations in human capital management – 'Skills England' aims to tackle the skills gap
- Geopolitical and economic instability leading to supply chain disruption and persistent export challenges
- Use of data means increased cybersecurity requirements – Half of all UK businesses experienced a cybersecurity breach in past 12 months [UK Government's Cybersecurity Survey 2024]

Innovation:

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- Despite challenges there is optimism across the sector in the UK with the Budget outlining stable R&D tax relief and the continuation of full capital expensing
- In 2024, the Hydrogen Innovation Initiative (HII), led by HVM Catapult, outlined the role hydrogen can play as a driver for that growth in the UK Hydrogen Innovation Opportunity report

Vertical Outputs:

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- Food production remains the largest subsector in the UK manufacturing scene – production-to-supply ratio of 62% for all food (74% for indigenous food) – which is up on the 2021 figures [UK Government]
- Pharmaceutical production output increased by 30% over past 10 years
- Also a rise of 40% in manufacturing of intermediary products such as fabricated metals - driven by demand from construction
- UK manufacturing is very competitive in the industrial technology & electrical components space which offers excellent R&D opportunities – especially in navigational, irradiation and electromedical & electrotherapeutic equipment [Knight Frank]

Sustainability Focus

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- With typically higher energy demands than other sectors, sustainability initiatives have come sharply into focus since the Russians entered Ukraine.
- Alongside maintaining cost efficiencies on energy, labour shortages (and the associated cost of labour) incentivise the drive to efficiency and the adoption of tech solutions e.g.: optimising routing for distribution and increasing factory automation.

2025 Road Map

Optimism:

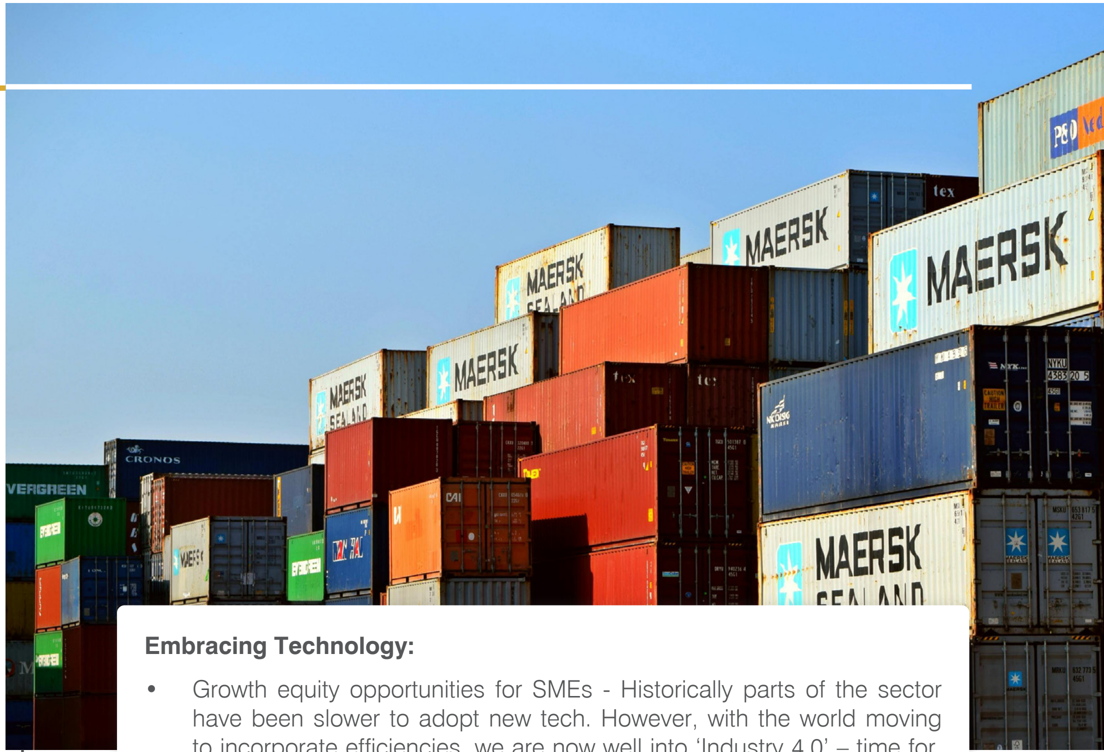
- Consistent outlook among UK manufacturers of both optimism and realism - 63% of companies think the opportunities in the sector outweigh the risks, despite only 37% expecting economic conditions to improve this year. [Made UK's Executive survey 2024]
- Firms eagerly await the Industrial Strategy due to be released by the UK Government in the Spring

Opportunity:

- Emerging technologies such as wide-bandgap semiconductors and lightweight composites are set to revolutionise manufacturing processes
- Growing focus on onshore capabilities promises to reduce reliance on international supply chains, enhancing resilience and security
- Larger industry players to adopt smart factories and cutting-edge tools first – this will help determine the most efficient opportunities for smaller manufacturers to integrate into their operations at a lower risk eg:
    - Coca Cola announced a planned £42m investment into a new Automated Storage Retrieval System (ASRS) warehouse at its Wakefield site
- Compliance with new regulations such as NIS2, DORA, PCI 4.0, the UK Cyber Resilience Act, and the EU AI Act will be crucial

Continued momentum in sustainable operations:

- Anticipated crackdown on ESG monitoring and reporting requirements
- Opportunities for innovation to support this. Eg:
    - Temperature-sensitive packaging across food, beverage and pharmaceutical distribution to reduce loss from spoiled product
    - Possibility of large firms (like Coca Cola) implementing a Deposit Return Schemes (DRS) to incentivise proper recycling
- Advanced recycling methods, reducing waste and allowing for valuable materials to be economically recycled for new product.

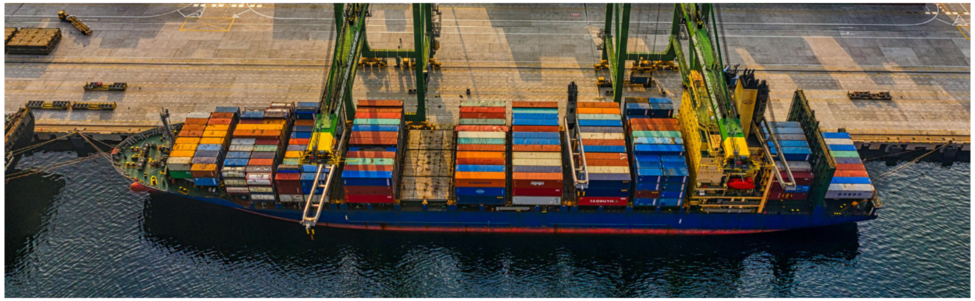


Embracing Technology:

- Growth equity opportunities for SMEs - Historically parts of the sector have been slower to adopt new tech. However, with the world moving to incorporate efficiencies, we are now well into 'Industry 4.0' – time for, particularly the smaller, players to start investing in their tech stacks to stay competitive & aid quality control processes. Hopefully as some of the technology platforms mature, there will be increased clarity on appropriate investments in the area. However with the onset of AI into businesses, those businesses avoiding decisions are likely to fall behind at an ever quicker rate.
- Currently 29% of firms will look to technology, cloud and AI to succeed in 2025 - hopefully this will grow as the sector becomes comfortable with risk levels and address inefficiencies
- Reduce headcount by automating unskilled tasks - 92% believe staff will be their highest cost for the year ahead
- Cloud-first approach to unlock flexibility and scalability – players need to consider proactive cybersecurity strategies
- Manufacturers will now invest heavily in merging operational technology (OT) with information technology (IT). Wireless systems and edge servers will secure and process data in real time, essential for effective automation planning.

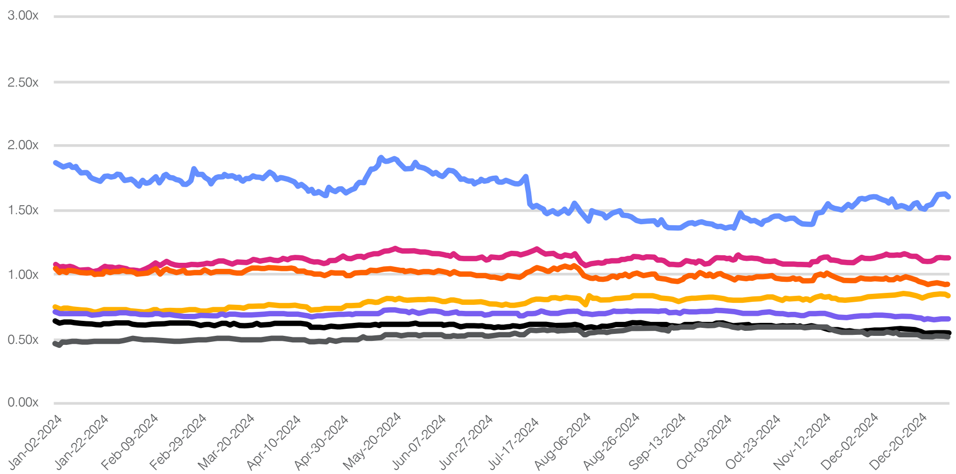
Public Market Overview

- Valuation multiples within the relatively mature manufacturing space remain fairly stable in general, with the exception of aerospace, and, on occasion, specialist manufacturing. In these verticals, technological advances caused an element of disruption
- In aerospace, drones are still emerging and likely to cause market fluctuations in valuation as their practical uses and limitations are determine

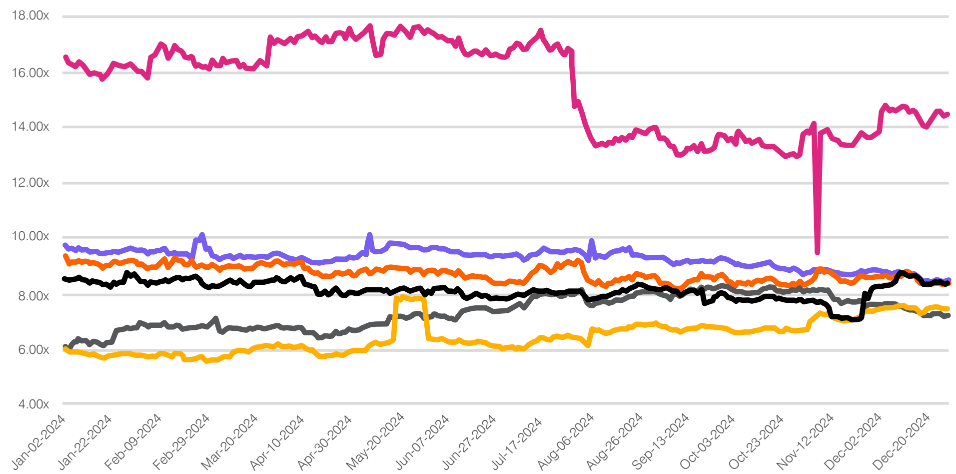


- Specialist Manufacturing is an innovative vertical including entities in the growth stage with consequently lower EBITDAs than other more mature verticals, conversely boosting the EBITDA multiples for a given value. Entity values have remained fairly stable over 2024, with significant changes more linked to revised EBITDA metrics. Two outliers affected the set:
  - Ichor Holdings'(Manufactures critical fluid delivery subsystems) started the year with a TEV/EBITDA of 70x, then in August 2024 this significantly decreased to c.40x where it roughly remained for the rest of the year. This reflects the maturing and development of the business, with increased EBITDA and a largely static entity value.
  - In November, FlowTech Fluidpower (Supplier of technical fluid power products) saw a temporary crash in its market cap, causing the drop seen in specialist manufacturing TEV/EBITDA multiples – this occurred in the period between expected earnings releases and actual earnings filing

Revenue Multiples



EBITDA Multiples



Aerospace - TEV/Total Revenue | Printing and Packaging - TEV/Total Revenue | Food Production - TEV/Total Revenue | Specialist Manufacturing - TEV/Total Revenue | Industrial Technology - TEV/Total Revenue | Consumer and Branded - TEV/Total Revenue | Construction - TEV/Total Revenue

Revenue and EBITDA mutliples for the past year

Source: CapIQ, PCF tracks companies with market cap. <£1bn

NB: Insufficient data to plot EBITDA multiples for Aerospace

Private Transactions Overview

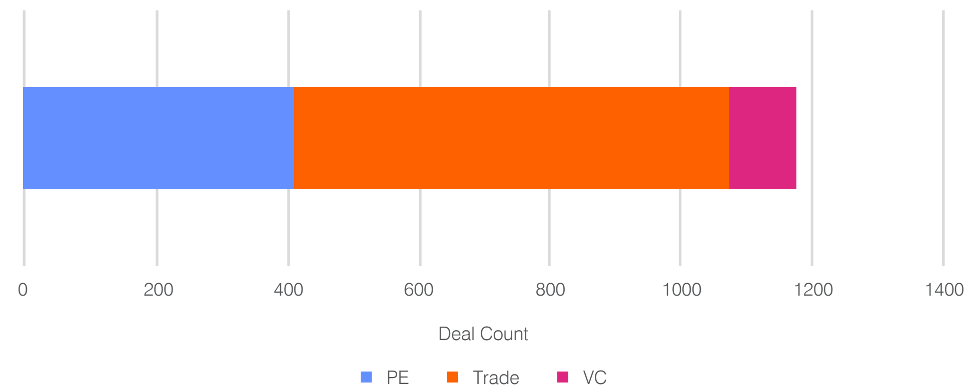
- Sector sentiment impacted by elections around the world, with a small uplift in the number of Consumer & Branded and Construction deals compared to 2023, but all other verticals experiencing a drop
- Trade acquirers continue to dominate the space with international players particularly in evidence. Here at Polestar, two of our deals this year were in Manufacturing and Distribution, both of which were sold to international buyers.

Polestar Deals

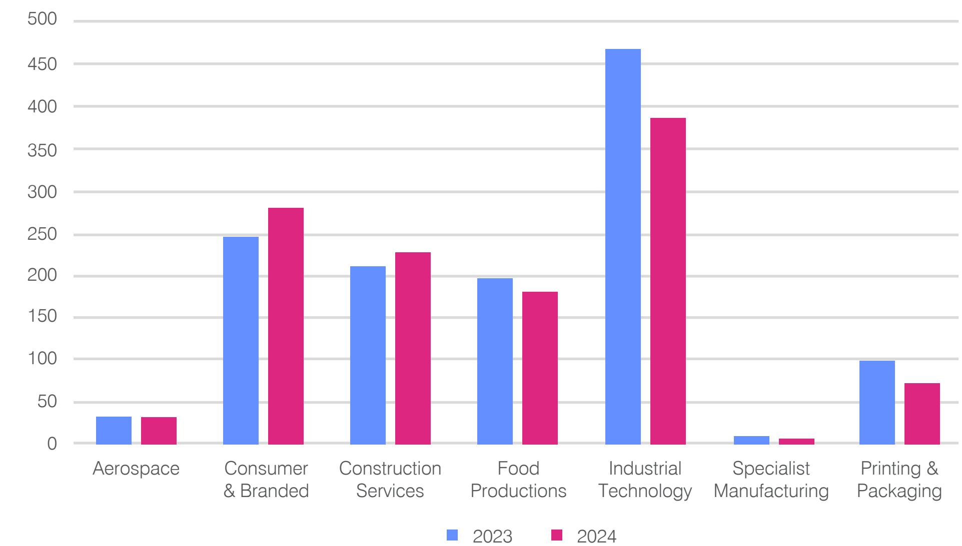
Sale of		Sale of	
semmco to	HAKI SAFETY	schoolblazer to	HANCOCK & GORE

- In 2024, 37% of all investors and strategic acquirors were international
- As most manufacturing businesses are more well-established, family-owned businesses, compared to other industries such as technology, we can anticipate the number of deals increasing in the coming years as owners look to retire and exit

2024 Deal Activity in Manufacturing & Distribution by Type



Number of UK Deals Across UK Manufacturing



Source: Pitchbook, excludes deals with a stated value >£500m

Investor Appetite

PE Investors	Number of UK Investments 2024 (<£500m)	Example Investment
BGF	7	**Metpro** - £21.5m Buyout - Manufacturer of mechanical and electrical components
Foresight Group	4	**Sprint Electric** - £1.6m growth funding – Manufacturer of variable-speed drives for industrial motors)
Aurelius Group	2	**Trinny London** - £15m growth funding - Manufacturer of make up

Private Equity finds the manufacturing sector highly attractive; it offers:

- Steady Cash Streams
- Untapped Potential: Targets often possess valuable assets with deep-rooted expertise but lack capital or strategic vision to fully unlock their potential – PE can bridge this gap with fresh resources and innovative approaches and fuel sustainable growth through buy-and-build strategies, operational improvements, and investments in cutting-edge technologies.
- Resilience and Growth: Despite facing headwinds like global competition and economic downturns, manufacturing remains a crucial cog in the global economic engine.

Strategic Acquirors	Number of UK Acquisitions 2024 (TTM)	Example Acquisition
Frasers Group	6	**Mulberry Group** - £83m – Manufacturer of luxury leather goods
BAE Systems	3	**Malloy Aeronautics** - £60m – Manufacturer of drones designed to solve logistical challenges
Luceco	2	**CMD Limited-£30m-power distribution systems** **D-Line(Europe) Limited-£9.4m-cable management solutions**

Strategic acquirors look to inorganic growth, especially in the mature verticals:

- Look for opportunities to acquire assets, supply chains & customers
- Resilient tech stacks are highly attractive
- Increased pressure on large corporates to report on ESG aspects means that sustainable practice commands a premium for those looking to exit to trade

Select Transactions

Air Control Entech

Manufactures remote-access inspection tools for use within aviation products – acquired by SRJ Technologies Group for c.£15m in July 2024

Crosta & Mollica

Producer of artisanal Italian bakery products – Bought out by Perwyn for £78m in January 2024, then partially sold to Connection Capital in October (undisclosed amount)

PAR Group

Manufacturer of sealing plastics – acquired by R&G Fluid Power for c.£37m in April 2024 (2.9x Revenue)

Codeology

Manufactures and designs inkjet coders and printers, and automated end-of-line labelling – 50.5% acquired by Control Print for £1m in Feb 2024