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Wavin: A Firm And Better Offer In A Few Days?

Facts

Wavin manufactures plastic pipe system for gas, water, sewer systems, building, land drainage, cable conducting and irrigation application in Europe. The company further provides consultation and design services, as well as product support.

Mexichem operates in the same business in Latin America and gave an unsolicited indicative non-binding proposal for Wavin which trades in the Dutch stock market.

On November 22nd, Mexichem proposed to acquire all outstanding shares of Wavin at 8.50€, which represented a premium of 115% in comparison to the last trading price. The proposition was subject to a certain number of conditions including:

- The recommendation and full support of the Management Board of Wavin
- A satisfactory outcome of a due diligence investigation.

Traders should keep in mind that, in the Netherlands, the law allows a bidder to make an indicative offer which is clearly non-binding, which means that at this stage a firm offer is not guaranteed. Furthermore, the discussions between the two parties induced the Mexican company to increase their bid twice: on December 5th, the offer was increased to 9€ and on 22nd of December, the terms were changed at 10€ because at this level, Wavin's board granted Mexichem access to their accounts.

As a result, Mexichem has until the end of this week to assess the situation by walking away or proposing a firm bid at 10€.

Comments

First of all, we want to point out the fact that granting access to the accounts of Wavin does not necessary mean that the board will recommend a firm bid at 10€. However we are very confident that it will be the case because:

- Wavin stock collapsed from 12€ in march 2011 to 4€ just before the bid and this offer is a good opportunity for the shareholders to sell their stocks.
- Mexichem has a strong rationale in this transaction because the merger would give them access to the European market where they do not have any operation. In these conditions, the bid appears to be high without any potential synergies. This merger is strategic for Mexichem which is the market leader in plastic pipes in Latin America: in addition, Mexichem is interested in the new technology developed by Wavin. On the other side, our opinion is that a cost cutting program at Wavin would be very limited in its scope because we noticed that the company has already done a lot in this area over the last few months.
- A counterbid from a potential suitor can be ruled out because of the limited financial capacities of these potential bidders (Uponor for example) and the potential antitrust issues.
- As Wavin is a traded company, it would be very strange for Mexichem to find bad surprises in their accounts. In this case, Mexichem would walk away from their transaction but we rule out this possibility.

We think that this deal is only a question of price. Therefore even if Wavin's two main shareholders, Delta Loyd and Franklin Templeton, were to consider the bid as too low, preferring a price around 13€, they described the current bid as an opportunistic offer, meaning that they are aware that it is a good opportunity to sell their stocks.

Other small shareholders welcomed the offer according to the Dutch press, which is not surprising because at 10€, the premium is above 150%!

We like this deal because Mexichem is a very serious bidder. With more than 100 plants in the world, especially in Latin America, Mexichem has the financial capacity to conduct this kind of transaction. Even at 10€, the deal will be quickly accretive in terms of EPS and we guess that Mexichem has a lot of ambition about the European market. In addition, as the European plastic pipe market is very fragmented, they prefer anticipating the future consolidations in the sector.

We noticed that Mexichem made 4 acquisitions in the last 2 years and their M&A track record appears to be very good. If they can bid 10€, it is mostly because they have a long-term strategy: an investment focused player would be unable to bid at this level and we are sure that they won't bid above 10€.

The fact that the chairman of the supervisory board of Wavin is also the chairman of the first shareholder of the company (Delta Loyd) should not be an issue because he will not take part in the decision concerning the offer. However, we easily understand why the board rejected the two first bids at 8.50€ and then 9€. The board of Wavin did a good job by pushing Mexichem to pay a high premium and by imposing certain new conditions for the offer:

- Wavin should retain a separate operating structure with headquarters in the Netherlands
- A Wavin supervisory board will be maintained with joint representation, including a majority of members from Mexichem.
- Existing rights of the employees, including pension rights, will be respected and the current Wavin employee consultation structure will be left unchanged.
- Wavin's brand is to be retained and its R&D innovation center is to be kept in the Netherlands

Conclusion

Mexichem is a serious bidder with good track record in acquisitions and good financial abilities. The deal appears to be highly strategic, rationale and accretive. The only problem is the price because they need the recommendation of the board: in the Netherlands, a hostile bid is not possible!

They accept very strong commitments for the new entity by keeping the brand, the offices and the employees in the Netherlands. Aside from the price, they cannot do anything, which illustrates their seriousness and their motivation.

We think this move is very strategic because Wavin is a fantastic opportunity for them to have access to the European market. We rule out a better offer from Mexichem or from a rival and we are convinced that Wavin will accept the offer.

As a conclusion, we advise to set up positions but to be careful of the small liquidity (2 M€ a day) and the big downside in case of issues concerning the due diligence.

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