

# Large Cash Reserves Are Fueling RF and Microwave M&A

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**T**he signals are strong and clear; in recent years, the amount of cash directed to acquisitions in the RF and microwave space has soared, leaving potential sellers with a host of options. A decade ago, owners of RF and microwave companies faced a lack of quality acquirers, as

investors' lack of industry expertise made it difficult, if not impossible, for institutional funds to finance acquisitions in the space. Today, the story unfolds quite differently. The acceleration of wireless communication, the demand for high-tech defense systems and the growing cross-functionality of radar have made the RF and microwave space particularly attractive. Players are now far more knowledgeable and have a much larger appetite to take advantage of long-term tailwinds.

As a result, the market has been flooded by potential acquirers, including many investment firms. These groups, typically private equity (PE) funds, are backed by large amounts of capital specifically meant for acquisitions. Even more importantly, their funds must be spent within a predefined time period, typically five years after being raised, meaning they are eager to make investments when quality opportunities are available in the market.

## WHO ARE ACQUIRERS TARGETING?

Increased competition within the industry has presented obstacles to organic growth and acquirers are looking to satisfy their desire to scale and solidify their competitive advantage through strategic consolidation. Consequently, smaller companies have become more enticing to acquirers than in past years. Investors have zeroed in on several common characteristics, including:

- Proprietary technologies
- Unique capabilities
- High performance, high-reliability products

- Robust, repeat customer base
- Strong in-house technical talent.

By targeting a variety of smaller companies with niche market positions, consolidators can develop a cohesive portfolio of significantly more value as a collective unit than as the sum of its parts.

## SO, WHY NOW?

There are several reasons for the build-up of acquisitions in the RF and microwave space. Primarily, there is a historically significant surplus of cash available to be spent by both corporate acquirers and investment firms. This surplus can be attributed to large amounts of PE fundraising in the past few years, as well as a recent lack of quality investment opportunities where cash can be deployed. Additionally, this supply of cash is spread across an array of acquirers with interest and experience in the RF and microwave industry. This has created a large imbalance between the number of acquirers seeking to do deals within the space and the number of quality companies entertaining a sale process. The good news is that this mismatch has afforded sellers the opportunity to engage in a variety of discrete options with buyers who are willing and able to pay a premium price.

## HOW DO ACQUIRERS THINK ABOUT VALUATION?

There is no "one size fits all" approach to valuation and it is commonplace for different acquirers to ascribe different values to the same company. Synergistic expectations or the anticipated benefits that a transaction is expected to unleash in combination are a clear



driver of this phenomenon. This is the additive mergers and acquisitions (M&A) concept that  $1 + 1$  can equal 3. Despite these variations, the one universal trait that both financial and strategic buyers focus on when thinking about valuation is the bottom-line earnings that a company generates.

The standard practice for valuing a business is to apply a multiple to its annual earnings. The magnitude of the multiple depends largely on the buyer's distinct motivations and business outlook for the sale target. Sellers that check the box of more target characteristics will achieve a higher multiple of earnings. Conversely, businesses that lack desired target qualities will be valued at a lower multiple of earnings.

### WHAT IS THE TIME FRAME?

On the individual buyer scale, acquisitions come in waves. For PE firms, a long-going strategy to drive value has been the "buy-and-build" approach, in which a PE firm acquires an initial platform with the intention of further acquiring and merging companies in a fragmented market. Recent examples of buy-and-build consolidators have included:

- Abracon (owned by Genstar Capital)
- Infinite Electronics (owned by Warburg Pincus)
- Maury Microwave (owned by Artemis Capital Partners)
- Micross Components (owned by Apollo Global Management)
- Quantic Electronics (owned by Arcline Investment Management).

More broadly speaking, the time horizon for this acquisitive environment is difficult to predict. If market growth slows or investors' access to capital dries up, the demand for acquisitions may decline. However, consolidators have exhibited a clear appetite for small- and medium-sized companies in the RF and microwave space. It is likely that the consolidators will continue to have this appetite, provided that the terms and benefits of these acquisitions remain to their advantage. ■