

The North American Injection Molding Industry

“How to Survive in 2009 to see the ‘Light’ at the end of the ‘Tunnel’”

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THE CURRENT CLIMATE FOR INJECTION MOLDING-AN OVERVIEW

The global economy is in the midst of possibly the worst recession since the great Depression of 1929. Business values are tumbling, company earnings are declining, many companies are either in foreclosure, bankruptcy (or on the way to it) closing plants, are laying off workers and cutting costs wherever possible. Credit markets have nearly disappeared, exacerbating the problem of obtaining the capital that companies need to survive during these trying times.

Our firm tracks plastic industry foreclosures, plant closings and bankruptcies in addition to acquisitions and have determined that during the 2nd half of 2008 bankruptcies and foreclosures nearly doubled-from 13 to 24-the first six months of the year. So far in the first half of 2009 this unhappy trend is continuing and is expected to increase a notch among Tier 1, 2 and 3 suppliers to GM and Chrysler in June, July and August if these two onetime global automotive powerhouses indeed file for bankruptcy in June.

The current general economic snapshot certainly applies to the injection molding industry-especially in certain market segments such as automotive, construction, major home appliances and any other segments that manufacture “big ticket” items the purchase of which can be postponed in a recession. Business values of publicly owned companies have also declined to 45% of their high based on the Dow Industrial Average highs and lows for the past 15 months and senior lending for business financing has nearly dried up, especially for acquisition financing. By 2010 we predict that the population of plastic processors will decline by as much as 20%. While many consumer markets and products are relatively immune from the recession the majority of us are facing a ‘disaster of biblical proportions’ in 2009 to rob a quote from the famed adventure movie “*Ghostbusters*”.

WHAT YOU CAN DO

Our clients are continually calling us for advice on how to weather the storm during this crisis. But what is to be done/what can be done?

If your company is threatened by foreclosure or bankruptcy we recommend the following multi pronged short term approach:

1. **Manage your costs as carefully as possible.** Eliminate or postpone any expenses that can be avoided.
2. **Minimize capital expenditures that merely increase capacity**-unless you have strong contractual agreements in place with financially strong customers.
3. If you have substantial debt and are in danger of violating or are already in violation of your loan covenants, **become good friends with your banker.** In most cases, companies in trouble with their banks are solidly managed but are victims of a poor market such as automotive or construction where demand has declined dramatically. Most banks are reluctant to foreclose on a company in this kind of position since a restructuring or work out group would be unable to accomplish much more than the existing management team and if the company is liquidated in today’s market the bank would recover only a few pennies on the dollar on the sale of

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Company receivables, inventory and fixed assets. Simply put, the bank is more likely to recover more of its debt if it can assist your company in surviving the recession than it can via foreclosure.

4. **If you are taking substantial distributions out of the Business-Don't!! Similarly, strongly consider reducing your lease payments if you own your land and building separate from the Company.** In general, your major value lies in your company not in the real estate so your first interest should be to preserve the good health of your Company wherever the needs of the two conflict.
5. Your customers may be in greater financial trouble than you are-yet your success depends on their financial health. Unfortunately, in business downturns credit reports are often inaccurate and optimistic based on the understandable reluctance of companies to disclose their financial circumstances if they are in decline. **Our clients are visiting key customers-and suppliers-to get a better fix on their business health-rather than rely on credit reports.**
6. **Consider strategic partnering with similar businesses** to consolidate raw material purchases and lower costs. If possible, get your major customers to pay for raw materials entirely and price your product based only on your conversion costs, if possible. In some cases, your major customers are also huge users of resins, additives and fillers and can be persuaded to buy these materials for you at their price. We are seeing more strategic alliances that involve co- and cross- manufacturing for example to better utilize available capacity.
7. **Paradoxically, this is the best possible time to acquire a company, plant site and/or product line.** If you have the financial wherewithal and can conceive of a business strategy to take advantage of the economy when it turns up we strongly recommend that you consider doing so. Consider that an automotive supplier who has “leaned down” to survive the current crisis in the Big Three who may then experience a 30-40% upturn in business when the auto industry stabilizes. The bottom line here is the stronger you are coming out of a recession the better prepared you will be to reap the rewards. Broadening your product offering, diversifying into other markets, expanding geographically, increasing your products’ value added and making consolidating acquisitions still make good sense when you consider the additional value you may capture when the economy turns up.

We are seeing continued acquisition interest in: (1) **diversification** as a hedge against the risk of serving only one or two major markets; (2) strong interest in **consumer markets**, and (3) a continuing interest in **higher value added and proprietary products** in markets less threatened by cost and price pressure such as **medical** and **aerospace**.

While we note that acquisition prices as a multiple of prior 12 month’s EBITDA (“**E**arnings **B**efore **I**nterest, **T**axes, **D**epreciation and **A**mortization”) have declined by a multiple 2x or more in certain distressed industries we are finding that multiples are holding firm in more attractive markets.

THE GOOD NEWS

The good news is that many economists are beginning to believe that the economy has bottomed out and will rebound later this year. Why?

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1. **The Dow Jones industrial average has risen from a low of 6,400 in March to roughly 8,500** as of May 8-a gain of nearly one third over the low. With the Dow as a leading indicator of economic performance, this would indicate that the economy has indeed bottomed out and is in the early stages of a recovery.
2. **We are seeing the beginnings of an oil Bull Market** with oil prices increasing 18% during the past two months. Either the oil “Bulls” are going to take a beating or they have identified rising demand in 3-6 months which would also imply a US and global economic recovery.
3. **First quarter COMPANY earnings are better than predicted** with 65% of reported company earnings that exceed Wall Street’s estimates.

These three indicators make us cautiously optimistic that the economy will begin a turnaround later this year. The trick will be to manage costs and hang in until the inevitable upturn occurs later this year and-if possible-expand and strengthen your business to take advantage of the recovery that will follow.