

International Flavors & Fragrances: Story Structure In M&A Situations

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Story Structure

Best investments are just like good stories or movies: with three-part story structure (complication, development, resolution), important turning points, intrigue, drama, and surprises.

Strictly analytical approach to investment management does not provide us with tools for dealing with uncertainty.

The closed and fixed form of analytics leaves no place for imagination.

And without imagination, we are just not capable of fathoming uncertainty, fathoming the future.

Narrative, by its nature, allows us to understand the time dimension better: order of events, their length, and different time periods.

For example, George Soros, in his book "Alchemy of Finance" describes how he analyzed certain investment situations.

In order to see the big picture and analyze the case he uses terms borrowed from the world of literature, movies, and theatre. He calls the overall cycle "scenario" and different stages of the cycle "act one", "act two", "act three", "act four", and puts an emphasis on main "actors": the shareholders.

I think that the use of such terms is not a coincidence: it serves well the purpose of looking at how the situation develops over time.

M&A Situations

Some M&A transactions present opportunity to develop a good investment thesis.

Large merger is an important, transformative corporate event.

It can change investment thesis and story of a company.

It just takes time for company's story structure to develop and for share prices to reflect fundamental changes and developments.

As a result of this, shares can decline or trade sideways despite the fact that transaction has great fundamental logic and benefits for shareholders.

All of this creates opportunities for investors. After certain period of time it is easier to take a step back and look at company's story and story structure.

International Flavors & Fragrances

In October 2018, IFF completed a combination with Frutarom in a \$7.1 billion transaction.

The acquisition of Frutarom solidified company's position as an industry leader across an expanded portfolio of products, resulting in a broader customer base across small, mid-sized and large companies and an expansion to new adjacencies that provides a platform for significant cross-selling opportunities.

In December 2019, IFF agreed to merge with DuPont's Nutrition & Biosciences business.

DuPont Nutrition & Biosciences applies expert science to advance market-driven, healthy and sustainable solutions for the food, beverage, dietary supplement and pharmaceutical industries. It also uses cutting-edge biotechnology across a range of markets to advance bio-based solutions to meet the needs of a growing population, while protecting the environment for future generations.

DuPont shareholders will own 55.4% of the combined company.

Together with cash component and at the current IFF share price, transaction reflects total value for DuPont's division of \$20.9 billion.

Based on Pro-Forma FY 2019 EBITDA of \$2,600 million and IFF's FY 2019 EBITDA of \$1,174 million, transaction reflects a x14.7 EV/EBITDA valuation multiple.

Assuming \$395 mil synergies (estimated to be achieved 3 years post-closing), transaction reflects a x11.5 EV/EBITDA multiple.

IFF is currently valued at an EV/EBITDA valuation multiple of x13.07 (based on LTM Q2 2020 EBITDA).

On a combined basis, IFF is currently valued at an EV/EBITDA valuation multiple of x13.79 based on Pro-Forma FY 2019 EBITDA and a multiple of x11.97 including synergies.

Company's size and scale had changed significantly after Frutarom transaction and will change even more after completion of DuPont's division acquisition.

We believe that IFF shares provide investors an attractive investment opportunity due to the stable nature of company's business while two large mergers over the past 3 years provide opportunity to enjoy growth as well.