



Forever young?

Why manufacturing and automotive companies must invest in technology and what to look out for

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Introduction

To gain or maintain a competitive advantage, manufacturers must adopt new technologies to transform their operations.

And they know it... Technology is increasingly becoming a key factor driving investment in the manufacturing and automotive sector.

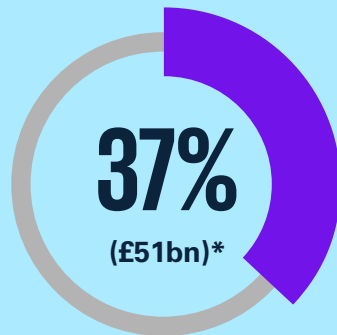
Technology led acquisitions now account for a quarter of investments by Manufacturing companies each year.

This proportion is even higher when you look at deal values given the higher price point for technology companies.

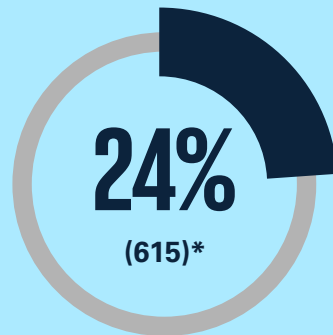


Manufacturers' acquisitions with a technology theme

By Deal Value



By Volume



*2022

Source: Refinitiv, Dealogic



To stay current, manufacturers must invest in technology. To accelerate delivery of new technologies, manufacturers are increasingly looking to acquire or partner with other businesses. Successful outcomes are critically dependent on cultural fit and compatibility between the organisations, underpinned by a clear integration strategy to leverage capabilities and the best from both organisations.

Gavin Combe
Partner & Head of KPMG UK M&A for Industrials



Why

Manufacturing and automotive businesses are investing in technology businesses, largely, to transform their own business and operations.

The aim is to gain a sustainable, competitive advantage, by:

Adapting to changing consumer behaviour	e.g. the transition to electric and autonomous vehicles, requires new technology investment or acquisitions
Leveraging data and insights to support strategic decision making and connect more closely with customers	e.g. using AI for predictive demand and production planning based on customer trends, seasonality, asset performance, energy costs, and supply chain disruption
Diversifying into new markets with new services and products	e.g. subscription models through a direct-to-consumer offering enabled by technology platforms
Driving cost and operational efficiencies to help ease inflationary pressures	automation of key manufacturing processes e.g. using generative AI in product design
Commercialising their own technology products	e.g. selling technology and services to other businesses and industries



Technology has transformed the way we work at Pharmacy2U with innovation in every aspect of our business. We have developed a range of advanced systems and tools, such as robotic warehouse automation, algorithmic-based prescription dispensing, cloud-based clinical software and API driven inventory management systems.

By automating warehouse processes, we have been able to streamline our fulfilment processes, reduce order processing times, and further increase accuracy in order fulfilment. This has led to improved delivery times, more efficient packaging, resulting in fewer deliveries, which is better for our customers, business, and the environment.”

Kevin Heath
CEO, Pharmacy2U



Where have we seen this happening?

These three examples illustrate the diverse drivers for technology investment by manufacturers and automotive businesses.

Exploit Data & Insights

Acquisitions of technology platforms and skilled teams to help businesses better collect, understand and exploit data from their operations

KPMG advised a manufacturing client on their acquisition of UK-based technology organisation, whose proprietary and customised software platform generates critical insights, which are used to help its industrial customers to reduce waste and drive efficiencies in their operations through more effective management of energy use.

The acquired organisation consisted of engineers and software specialists, providing its global customer base with consulting, digital connectivity and monitoring of energy intensive processes.

CEO's view: "The important role of digital technologies, which provide remote, real-time monitoring and data-driven insights has never been clearer than during the pandemic."

Changing Consumer Behaviours

Acquisitions and Joint Ventures to provide new products and services to address changing consumer demands

In August 2023, it was announced Toyota and Pony.ai are partnering to mass produce autonomous taxis in China. It is expected over \$140m will be invested into the venture.

The Chinese market has already seen the launch of autonomous taxi services from Pony.ai across Beijing, Shanghai, Shenzhen and Guangzhou.

Toyota China CEO's view: "This is not only an important step for Toyota to carry out 'Chinese-style succession and evolution' but also a new stage in our business cooperation with Pony.ai,"

Selected Acquisitions of Technology Businesses

- Harris Corp acquisition of L3 Technologies Inc (Deal Value **£12.3bn**)
- Emerson Electric Co acquisition of Apen Technology Inc (Deal Value **£8bn**)
- Xylem Inc acquisition of Evoqua Water Technologies Corp (Deal Value **£5.3bn**)

Source: Refinitiv

IoT Connectivity

Acquisitions of IoT platforms to provide total connectivity and valuable monitoring and control solutions

Generac, a leading global designer and manufacturer of energy technology solutions and other power products, recently acquired Blue Pillar, an industrial internet of things (IoT) platform developer that designs, deploys, and manages Industrial IoT network software solutions to enable distributed energy generation monitoring and control in a more seamless and easier-to-use format.

Blue Pillar founder's view: "Now, as part of the Generac team, we will be able to best use our skillsets and leverage the capabilities of our platform to redefine and shape the future of connectivity solutions."

Source: (a) FinancialTimes (2022) (b) Reuters (2023) (c) GlobeNewswire (2022)



Where next?

As we look to the future, the scale and pace of technology change, combined with core macroeconomic objectives, will only increase the rate at which manufacturing and automotive companies need to embed advanced technology into their own operations. For example, the advent of generative AI provides transformative opportunities for manufacturers to innovate at pace, interact more closely with customers and fundamentally transform their business models.



Factories of the future

Additive Manufacturing and 3D printing are enabling manufacturers and automotive businesses to transition towards decentralised business models where they produce goods closer to the place of consumption, reducing distribution costs, environmental footprint, and lead times. By integrating AI with machine and product operations, manufacturers can predict when a machine is likely to fail and the optimal time for maintenance.



Solving the climate crisis

Manufacturers and automotive businesses are increasingly leveraging clean technologies and improving efficiencies to reduce energy consumption and carbon emissions. For example, the use of clean energy in production and distribution. Buyers are increasingly considering the impact on their emissions as part of a wider ESG lens when making acquisitions.



Autonomous vehicles and flying taxis

The Society of Automotive Engineers (SAE) forecasts a 216% YoY increase in semi- autonomous vehicle sales during 2023. In Lithuania, the grocery chain IKI has partnered with Clevon (an autonomous delivery specialist) to launch autonomous robot carriers onto public roads. Automotive businesses and manufacturers will have to proactively consider changing consumer behaviours to maintain a competitive edge.



We are on the cusp of large scale disruption powered by digitisation and AI. It will impact every industry and every business every process. Those that thrive will make smart acquisitions to fast forward their journey to the new world or invest significantly in their own internal development and transformation. Those that don't... won't. We have already seen large, established and mature industries turned upside down by new entrants who start from a very different base.

Sunil Harji
Partner & Head of Technology in M&A at KPMG UK

Source: (a) World Resources Institute (b) Fortune (c) SAE International (d) ADAS & Autonomous Vehicle International



Buyer considerations

As you can imagine, there are myriad challenges with investing in technology businesses, especially for manufacturers who are not used to investing in these type of organisations.

Overpaying, value erosion and cultural misfits are key reasons for acquisitions failing to return value. These are increasingly likely when buying a business with a different operating model, culture, products, and business ethos.

Incumbent organisations in the manufacturing sectors must consider the following key challenges when thinking about strategic technology acquisitions:

1. Deciding What To Pay

Manufacturing and automotive businesses are used to valuing organisations like themselves. These new technology acquisitions can be pre-profit and even pre-revenue. How do you determine where the value is in these businesses, and then put a figure to it?

2. Technology & Security

It is critical to understand how the technology you are investing in works at a technical level and whether it is scalable and agile enough to enable your own strategic goals. Technology acquisitions may bring about new risks for manufacturing businesses. How can buyers be certain that the business they're investing in is 'safe'?

3. Talent and Culture

Key contributors to successfully delivering deal value are retaining key talent and preserving the culture that comes with a technology company. How do you retain your critical talent, the ones who hold the knowledge and made it an attractive proposition in the first place?

4. Change Management and Business Adoption

A common point of failure in these acquisitions is the incumbent business failing to adopt the new technology, rendering it worthless. It is easy to buy innovation but is key businesses create an environment where it can thrive. How will the businesses work together to establish and encourage this environment?

The speed at which the benefits explained previously can be realised through technology investment and the best methods to achieve this must be front of mind.

However, if these challenges are insurmountable, buyers can look at other options for technology investment, for example, developing technology in-house or partnering with a technology provider.

These approaches will also encounter a share of the challenges described previously. However, doing nothing or "standing still" is no longer an option.



The adoption of technology has brought challenges both internally and externally to face into. Internally, to overcome these challenges, we have invested in comprehensive training programs for our employees, provided ongoing support and guidance, and fostered a culture of innovation and continuous improvement in our core values. Externally, Pharmacy2U works closely with the NHS, Department of Health and Social Care and industry bodies to bring about positive changes and support innovation in the digital pharmacy space"

Kevin Heath
CEO, Pharmacy2U



How to get it right

Once the Target, or a shortlist of Targets, has been identified, there are several areas buyers must get right to ensure the transaction is successful and returns value for the acquirer.



1. Valuation

Undoubtedly, there is a risk of overpaying for early-stage technology assets, especially when the business may not yet be profitable or revenue generating – so how do you put a sensible value on it?

- **Cash is king.** Get under the skin of the forecasts both in terms of commercial diligence and scenario / sensitivity analysis

- **What's in it for you?** Consider the value of transforming your own business
- **Think longer term** - returns could be up to 7-10 years, well outside the usual corporate timeframe.
- **Articulate!** Articulating the equity story clearly to your stakeholders and investors is vital, especially for listed businesses



We identified the areas that were prime for tech transformation through consistent focus on performance data. Reviewing real-time our operations, analysing our existing processes, and identifying areas where we could increase efficiency and productivity through the adoption of advanced technology solutions”

Kevin Heath
CEO, Pharmacy2U



The view from a start-up...

As an earlier stage business, we're at the forefront of rapid innovation and value creation. To ensure the continuity of this momentum, it's absolutely crucial to protect and preserve these attributes well beyond the scope of any deal.”

Michael Lowe, CEO, Sunswap



2. Thorough Due Diligence


Understanding the growth strategy, financial position and technology fundamentals is critical. Clearly these must be linked to the valuation. In particular, you should consider:


Technology


- The Technology strategy & roadmap – ensuring these align with the business strategy and acquisition hypothesis
- Benchmarking technology functionality and features against competitors

- Technology, process and people scalability including:

 Platform architecture, code quality, product management and software development processes

 Security risks (e.g. connected devices, code vulnerabilities)

 Key people, skillsets and culture, and the availability of these in the market

 Changes required to fully integrate into current operations

Growth and Commercial

- Current and future market opportunities (for the buyer and target)
- Pricing for any customer facing services and annual recurring revenue

Financial

- Total cost of ownership (TCO) – including ongoing maintenance, support, and upgrade costs, to determine if it is a financially viable option for your growth plans
- Level of debt in the business and future funding requirements / cash burn



How to get it right



With Technology acquisitions, the value leakage during integration or onboarding is heightened. This is driven by the entrepreneurial, start-up nature of these businesses often being stark opposite to their acquirer. Each situation is different and the integration strategy needs to reflect this, such as degree of autonomy, governance and group reporting. These strategic conversations with the target should start well before deal sign to establish a common view."

James Albert, KPMG UK Director of Integration & Separation in Industrials



3. Integration Planning

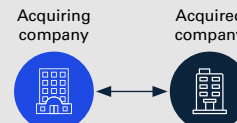
To ensure the acquisition is successful and delivers sustainable value for the acquirer, a robust integration plan and scalability strategy is required. To achieve this, you should:

- Define the design principles that will govern the integration in line with the acquisition objective. For example, defining the level of integration, Target Operating Model and risk appetite to ensure maximum value is derived from the acquisition
- Identify areas of duplication and potential for cost optimisation. When acquiring a technology business, it is more likely consolidation opportunities will be back-office technologies (e.g. payroll, HR, ITSM) and hosting
- Develop detailed integration plans considering any planned synergies, inflight programmes and how technology will support future customer journeys
- Proactively identify and track interdependencies across workstreams to manage delivery, cost and risk
- Assess and iterate the Target's technology roadmap against the business strategy and growth plans.
- Assess similarities and differences of culture between the businesses, including the extent to which the Target's innovative culture should be preserved. As part of this, identify critical talent and develop a retention strategy

Integration options

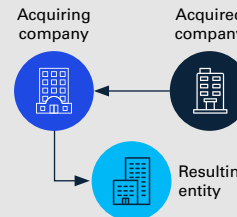
1. Bolt-on

Technology supports individual companies or business units in retaining their unique capabilities and cultures. There is minimal standardisation.



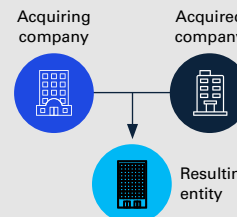
2. Consolidation

The acquired entity rapidly and efficiently adopts the parent's strategy, structure, processes, governance, compliance standards and systems.



3. Transformation

Integration is used as a catalyst for wider technology-led transformation across both entities whilst combining operations.



4. Beyond the deal

Post acquisition and initial integration, you need to think about technology adoption and continuous improvement across both organisations.

Depending on the level of integration undertaken, there may be opportunities to further embed technology into operations across the wider Group. However, it is critical to understand the value in each case.

Key areas to consider for further value creation:

- Investigating use cases for new technologies e.g., generative AI, could amplify or fast-track the business strategy
- Further technology integration – connecting systems and platforms across the Group for richer data and control
- Leveraging data and insights for improved decision making, understanding production and supply chain issues earlier, advanced operational reporting, and to identify cost optimisation areas
- Re-selling or franchising – to generate additional revenue through licensing to other organisations not just other manufacturers
- And finally, evaluate further investment opportunities
- The business vision and objectives, which should be clearly communicated at the outset and refined throughout the transformation



We would love to hear from you.

Get in touch to speak with our experts about how to get the most value out of your technology acquisitions.

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