

Planning for HVACR Market Consolidation

Distributors should look at scenarios as more business change hands



PLANNING AHEAD: Distributors should think about how they would react under different scenarios to prepare for the possibility that a longtime business customer comes under new ownership.

Barely a week goes by that doesn't bring news that an HVACR company has been purchased — sometimes by another business in the industry that's looking for a competitive advantage, sometimes by an investment firm whose officers might be new to HVACR and may bring new ideas about how the business should be run.

At Heating Air-Conditioning & Refrigeration Distributors International (HARDI), mergers and acquisitions are among three major topics of conversation — the other two being supply-chain problems and the labor shortage, said Zachary Perge, the organization's vice president of distribution strategies.

"It's something that's top of mind for every discussion we have," said Perge, who was a mergers and acquisitions specialist at a large professional services company before coming to HARDI.

Indeed, the numbers show a significant jump in mergers and acquisitions in the HVACR market just last year. Transactions averaged about 50 a year in 2019 and 2020, but moved closer to 100 last year, said Len LaPorta, managing director at The DAK Group, a mergers and acquisitions advisory firm in Rochelle Park, New Jersey. LaPorta expects that level of activity to continue this year.

“About 70% of the transactions,” LaPorta said, “involve private equity firms seeking to invest in what’s seen as a growing sector, while the remaining roughly 30% are strategic purchases by HVACR-related companies.”

“If you’re steadfast in what you’re doing, then you should have the confidence you need to succeed.” – Zachary Perge, Vice President of Distribution Strategies, HARDI

Different Scenarios

When a distributor finds a HVACR customer to which it has long supplied equipment and parts suddenly under new ownership, it can raise uncertainties and questions about the future with that company, said Perge. Will the new owners demand more favorable pricing? Will they still be interested in the products we carry or change course? Will changing dynamics shake up established business-to-business relationships?

The HVACR industry includes a lot of smaller companies, particularly among contractors. Perge said these companies tend to be family owned, multigenerational, and have strong ties in their communities.

“The uncertainty around any consolidation, or the entrance of PE (private equity), can throw people off kilter,” said Perge.

Perge recommends distributors take a “measured” approach to what the acquisition of a business customer might mean for them, and to plan for different scenarios just as they would for changing economic conditions, changing demographics, work force issues, or new regulations.

“It’s amazing what you can do with a few hours of scenario-planning,” he said.

Most importantly, he said, distributors should be confident in their employees, their business plan, and the value proposition they bring to customers.

“The outside noise of the market should be tertiary to what you’re trying to accomplish in your business,” Perge said. “If you are steadfast in what you’re doing, then you should have the confidence you need to succeed.”

“Rarely a Blank Check”

According to Perge, private equity, or PE, firms are new to HVACR and may have a learning curve in the industry. However, when a PE firm makes an acquisition, he said, its officials will typically be looking for greater efficiencies at their new purchase.

“Someone has to run these businesses. They may have to run it extremely differently,” Perge said. “PE is very rarely just a blank check.”

Perge said that while the recent level of industry consolidation is high, it’s not unique to HVACR.

“It’s not specific to one industry,” he said. “It’s just the way things are going throughout the entire economy.”

Some of the drivers of increased HVACR consolidation, said LaPorta, include the increased demand fueled by new energy-efficiency standards and greater attention to indoor air quality, advances in technology that companies strive to be a part of, and a shortage of technicians that might be filled by acquiring another company and its work force. Another factor, said Perge, is the greater number of owners who, since the beginning of the coronavirus pandemic, are looking to retire.



About Len LaPorta

Len LaPorta is a managing director of The DAK Group, an investment bank specializing in middle-market, privately held companies. Len advises business owners on sell-side and buy-side transactions, capital advisory and valuations. He is a veteran of the U.S. Navy and former owner operator of a contract manufacturing company. He can be reached at llaporta@dakgroup.com.