

2024

# M&A Trends – Distribution Industry

CURRENT AND FUTURE STATE ACROSS 18 SUBSECTORS

## Navigating the New Normals in the Distribution Industry

The distribution industry contains 18 subsectors that contribute \$11.6Tn to the US economy

The distribution industry remains an integral component of the economy, encompassing 18 subsectors that generate over \$11.6 trillion in total annual revenue in the U.S. (see *Appendix A*). Macroeconomic pressures, including geopolitical tensions and the global pandemic have hindered the sector's growth over the last five years, reflected in a compound annual growth rate (CAGR) of 1.6% from 2018-2023. IBIS World expects the sector to rebound and grow at a CAGR of 2.2% through 2028.

Several key trends are currently shaping the distribution industry. The emergence of omnichannel sales methods, the rise of the Value-Added Distributor (VAD), and overall digitization have presented challenges and opportunities. Many companies have turned to the M&A market in response to such trends. The subsector with the most M&A activity since January 2023 is Industrial Machinery and Equipment Merchant Wholesalers. *Appendix B* lists the largest revenue-producing industry group within each subsector with key counts of M&A activity, projected growth rates, and EBIT margins. This report provides a holistic overview of the distribution industry, analyzing key trends affecting companies and how M&A is used to execute growth strategies.

### Key Trends in 2024

#### *Digitization*

Like many other industries, the distribution sector is becoming increasingly digitized through the adoption of artificial intelligence (AI), machine learning, and the Internet of Things (IoT). Utilizing these emerging technologies enables distributors to gain a competitive advantage in the marketplace, empower employees, and redesign jobs. With new predictive analytics capabilities, companies may cater more directly to the needs of their customers, which is of the utmost importance in a market subject to ever-changing consumer preferences. AI, for example, maintains the ability to unify data from multiple different sales channels and make relevant cross-sell and upsell recommendations.<sup>1</sup>

AI unifies data from each sales channel and can make cross-sell and upsell recommendations

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<sup>1</sup> <https://www.proton.ai/guides/rise-of-ai-in-distribution>

Distributors speed up project start timelines by two months using AI

AI can reduce lead times by 60%

Intense competitive pressures from technological innovation and market fragmentation will drive investment in specialized equipment as companies attempt to reduce labor costs

According to a recent report by McKinsey, digitization and AI also enhance business efficiency and enable distributors to cut unnecessary costs. A key example cited in the report includes a building material distributor utilizing generative AI to personalize marketing materials. The report also discusses an industrial and electronics distributor incorporating generative AI in procurement. The company was able utilize AI to automate supplier bid screening, which reduced review time by 90% and accelerated start times by over two months. Semiconductor and industrial distributors have entered the AI arena as well, utilizing the technology to accelerate tariff code classification and shorten shipment lead times by organizing documents more efficiently. In fact, the automation of doc-review was reported to reduce lead times by over 60% while minimizing the number of shipment delays. Evidently, the value of generative AI in the distribution industry has quickly transitioned from hypothetical to tangible, enabling companies to streamline their operations while also boosting revenue.<sup>2</sup>

The effects of digitization have made their way upstream in the manufacturing industry. The Bain & Company 2024 report on the machinery and equipment sector forecasts a significant productivity boost driven by rapid innovations and a shift towards more intelligent machines. This evolution in the industry underscores the role of technological advancements in shaping future business models and operational efficiencies.<sup>3</sup> Additionally, intense competitive pressures from technological innovation and market fragmentation will drive investment in specialized equipment as companies attempt to reduce labor costs. Such factors have buoyed revenues and deal activity in the machinery and equipment distribution subsector despite consistent margin pressures and macroeconomic uncertainty. Deloitte's 2024 manufacturing outlook report discusses a record influx of capital into the sector due to heavy investment in electrical equipment, emphasizing product electrification and smart factory solutions. This trend indicates a proactive approach to embracing advanced technology and utilizing electrical equipment wholesalers.<sup>4</sup> Additionally, as demand strengthens among downstream markets such as residential construction and utility infrastructure, the industry will experience sustained revenue growth, enabling further M&A activity.

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<sup>2</sup> <https://www.mckinsey.com/industries/industrials-and-electronics/our-insights/distribution-blog/how-generative-ai-is-disrupting-distribution>

<sup>3</sup> <https://www.bain.com/insights/topics/global-machinery-equipment-report/>

<sup>4</sup> <https://www2.deloitte.com/us/en/insights/industry/manufacturing/manufacturing-industry-outlook.html>

Today's B2B market is often unpredictable and competitive, forcing distributors to adopt innovative strategies that drive higher volumes and margins. Incorporating technology-driven solutions streamlines distribution networks, thereby fostering higher fulfillment capacity and lowering per-unit costs. Distribution technology and software also benefit a company's supplier network. By providing distributors with sufficient and credible information about changing market trends, parties may work together to identify profitable market opportunities. The distributors that outperform the rest maintain a consistent record of capital-efficient growth, which requires a business model that leverages technology. The winners in today's market apply analytics to all facets of the business, including inventory management, documentation, and fulfillment.

### *Omnichannel Distribution*

The recent explosion of omnichannel – a term used to describe a business strategy that aims to provide a seamless shopping experience across all sales channels, including in-store, mobile, and online - has generated a dynamic environment requiring distributors to pivot their strategies rapidly. As a result, distributors have become increasingly focused on last-mile delivery solutions, strategically located fulfillment centers, and seamless integration of online and offline channels.<sup>5</sup>

Omnichannel has also disrupted the traditional manufacturing sales model, which presents challenges to distributors. With an increased customer propensity to purchase online, manufacturers have increasingly bypassed distributors and sold directly to downstream markets. Manufacturers building out direct-to-consumer (DTC) capabilities maintain 100% control over pricing, inventory levels, and access to critical customer data.<sup>6</sup> As distributors experience heightened competitive pressure from suppliers, building fully integrated distribution networks and sales channels becomes necessary. Distributors that can serve customers more seamlessly and efficiently than their suppliers – online, in-store, and mobile - will solidify their position as valuable supply chain partners.

Omnichannel provides a seamless experience across all sales channels that distributors can capitalize on

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<sup>5</sup> <https://softengine.com/distribution-trends-2024/>

<sup>6</sup> <https://www.forbes.com/sites/forbesbusinesscouncil/2021/10/19/how-manufacturers-can-get-started-selling-directly-to-consumers/?sh=2fd0463a6461>

### *Value-Added Distributor*

Emergence of the Value-Added distributor reaffirms the importance of distributors in the supply chain.

Margin pressures stemming from product commoditization and omnichannel expansion have contributed significantly to the emergence of the Value-Added Distributor (VAD). These companies go beyond the traditional role of logistics and order fulfillment to provide additional services that enhance their customers' operations and improve profit margins. Although the industry has seen several more examples of these types of companies emerge over the years, the growing inclination to skip the distributor in the procurement process (brought in large by e-commerce adoption) has amplified the importance of such a strategy. Examples of these services include:

- **Technical Support and Training:** Distributors can provide expert support to customers in need. This may include product training or troubleshooting.
- **Supply Chain Consulting:** Distributors can offer consulting services to their vendors and customers that increase the efficiency of their operations.
- **Vendor Managed Inventory:** This places the responsibility of managing and replenishing a customer's inventory on the distributor. This mitigates the customer's risk of overstocking or understocking its inventory.

A deal-focused strategy has proven an effective means of repositioning oneself as a value-added distributor in the marketplace. For example, in November 2023, Safeware Inc., a mid-size emergency response and safety equipment distributor out of Lanham, Maryland, acquired Hazard3, LLC, a Florida-based company. Hazard3 was an expert provider of emergency response training services, including HazMat/CBRN planning, fireground decontamination, and much more. Safeware established a new division with its acquisition of Hazard3, which focused solely on training customers involved in high-risk sectors. As a result, purchasers of the company's products now also had access to essential training services, all through the same distributor. The efforts of Safeware to expand its operations beyond traditional distribution solidified the company's market standing and provided customers with additional incentives to utilize its services.

## M&A Volume & Projected Growth

7 of the 10 subsectors with the most M&A activity have the strongest projected revenue CAGR through 2028.

The distribution industry's M&A volume (measured as the total number of transactions closed) displayed a noteworthy correlation to projected revenue growth in 2023. *Appendix A* shows that 7 of the 10 subsectors with the most M&A activity have the strongest projected revenue CAGR through 2028. The median projected revenue CAGR for these subsectors is 1.0% compared to just 0.11% for the bottom eight subsectors. These results suggest that distributors within higher-growth subsectors are more attractive targets to acquirers, offering more potential for ROI capture. A similar correlation exists between M&A activity and average EBITDA margins. Also illustrated in *Appendix A*, 70% of the subsectors with the most M&A activity maintained the strongest profit margins.

## Distribution Industry M&A Strategies

Significant market fragmentation and margin pressures have acted as catalysts in the emergence of the geographic roll-up. This M&A strategy enables larger firms to make numerous acquisitions of smaller, similar firms in adjacent territories, thereby expanding market presence and scale. Take Audax Private Equity's platform company, Colony Hardware, for example. As a B2B distributor of tools, supplies, and safety products to construction and industrial customers, Colony has made 12 acquisitions since partnering with Audax approximately five years ago. Employing their sponsor's "buy-and-build" approach to M&A, the firm rolls up smaller regional companies that offer similar products.<sup>7</sup> Adopting a roll-up strategy has enabled Colony to grow to over \$260MM in annual revenue while expanding its distribution network and achieving economies of scale.

M&As have been rooted in both geographic rollup and market /product extension strategies.

Another key M&A strategy used by distributors proved to be market and product extension M&As. Companies adopting this strategy seek to make acquisitions in markets where the firm is not currently operating, which may be a new geographic region or an entirely different product segment with new customers. Market extension has emerged as a popular M&A strategy among distributors constantly experiencing pressure from suppliers to expand their geographic reach and influence.

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<sup>7</sup> <https://www.audaxprivateequity.com/news/audax-private-equity-announces-the-acquisition-of-colony-hardware>

Watermark recently advised Lintech International in its first-ever acquisition. Lintech is a specialty chemicals distributor headquartered in Macon, GA, and has nationwide capabilities. The industry has experienced pressure from suppliers to expand from national to international service coverage and increase the different types of value-added services to suppliers. Large distributors such as Univar and Brenntag North America have embarked on aggressive acquisition sprees. This has put pressure on others to expand their services and footprints to compete effectively. Lintech recognized the need to expand into Canada and successfully acquired Andicor Specialty Chemicals based in Mississauga, Canada, in December 2023. Market extension acquisitions can offer attractive revenue and cost synergies.

### **Subsector M&A Volume and Multiples**

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688 total distribution M&A transactions occurred during 2023 and 1Q'24 in the United States. As explained above, market fragmentation is a driving factor behind this trend, as companies with adequate scale often find it easier to make acquisitions when the market is comprised of many smaller firms. Margin pressures also permeate the distribution sector, driving further consolidation as companies attempt to achieve economies of scale and scope through M&A.

Almost 45% of all M&A activity in the distribution industry in 2023 & 1Q'24 was attributable to three subsectors: (1) Machinery, Equipment, and Supplies (2) Household Appliances and Electrical Goods, and (3) Grocery and Related Products. Each subsector contains multiple industry groups in a similar way that sectors contain subsectors – see *Appendix B* for a breakdown of key industry groups.

Average EBITDA multiples varied across distribution subsectors, with a high of 8.2x for Chemical and Allied Product Wholesalers and a low of 5.1x for Metal and Mineral (except Petroleum) Wholesalers (see *Appendix A*). EBITDA margins and projected revenue growth both drove above-average valuations. Out of the top ten subsectors with the highest average EV/EBITDA multiples, 80% had the highest projected revenue CAGR through 2028, and 70% had the strongest profit margins. Maintaining strong profit margins *or* strong revenue growth prospects doesn't

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guarantee a higher valuation multiple. Instead, the optimal balance of the two is the most attractive to investors.

## **Conclusion**

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In conclusion, the distribution industry, critical to the global supply chain, continues to evolve in the face of macroeconomic challenges and an ever-changing technological backdrop. Despite a modest growth rate over the past five years, the sector is poised for a more robust performance through 2028, driven by strategic M&A and the adoption of cutting-edge technologies like AI. Key trends such as the rise of Value-Added Distributors and the shift towards omnichannel and digitized operations are redefining the landscape, offering both challenges and significant opportunities for growth. Companies that strategically leverage these trends through innovative M&A strategies, like geographic roll-ups and market/product extensions, are well-positioned to thrive in this dynamic environment. The correlation between M&A activity, projected revenue growth, and profitability underscores the importance of strategic acquisitions in achieving scale and efficiency, making it a pivotal time for stakeholders to invest in transformation and innovation within the distribution sector.



Watermark Advisors, a 22-year-old FINRA member M&A advisory firm, serves clients in all three phases of M&A: Preparation Phase, Transaction Phase, & Integration Phase through a unique approach called “The M&A Bridge.” If you are contemplating an M&A transaction, please contact Hagen Rogers, Executive Managing Director at 864-527-5960 to learn more about Watermark’s unique collaborative, comprehensive approach to M&A services.



Hagen H. Rogers  
Executive Managing Director  
Greenville, SC  
864-527-5960

## Appendix A: \$11.6Tn Distribution Industry Ranked by M&A

Subsector	Revenue Growth	Projected Revenue Growth	Projected Revenue Growth	CAP IQ	CAP IQ	GF Data	IBIS World	
	2019-2023	2023-2028	Rank	Count of M&A	M&A Activity Rank	Average EBITDA Multiples	EBITDA Margins	
Top 10 M&A Activity	Machinery, Equipment, and Supplies Merchant Wholesalers	1.50%	1.80%	1	156	1	7.1x	5.36%
	Household Appliances and Electrical and Electronic Goods Merchant Wholesalers	0.57%	1.53%	2	86	2	6.8x	4.03%
	Grocery and Related Product Merchant Wholesalers	0.92%	0.63%	11	63	3	7.7x	2.40%
	Professional and Commercial Equipment and Supplies Merchant Wholesalers	1.46%	0.94%	9	54	4	7.4x	5.44%
	Lumber and Other Construction Materials Merchant Wholesalers	1.21%	1.22%	6	47	5	6.1x	3.97%
	Apparel, Piece Goods, and Notions Merchant Wholesalers	-3.13%	-0.24%	14	39	7	6.4x	3.70%
	Metal and Mineral (except Petroleum) Merchant Wholesalers	3.01%	-2.13%	18	39	7	5.1x	6.55%
	Drugs and Druggists' Sundries Merchant Wholesalers	1.57%	1.29%	5	33	8	7.6x	0.90%
	Chemical and Allied Products Merchant Wholesalers	0.45%	0.69%	10	30	9	8.2x	4.05%
	Motor Vehicle and Motor Vehicle Parts and Supplies Merchant Wholesalers	-0.25%	1.48%	3	29	10	6.7x	4.33%
Bottom 8 M&A Activity	Hardware, and Plumbing and Heating Equipment and Supplies Merchant Wholesalers	-0.28%	1.08%	8	22	11	7.6x	4.67%
	Furniture and Home Furnishing Merchant Wholesalers	-1.48%	1.43%	4	20	12	6.4x	3.15%
	Paper and Paper Product Merchant Wholesalers	-3.38%	-2.07%	17	19	13	6.2x	2.90%
	Beer, Wine, and Distilled Alcoholic Beverage Merchant Wholesalers	1.91%	1.14%	7	16	14	8.2x	4.35%
	Miscellaneous Durable Goods Merchant Wholesalers	1.98%	0.36%	13	15	15	6.7x	4.17%
	Miscellaneous Nondurable Goods Merchant Wholesalers	-1.43%	-0.63%	15	11	16	7.6x	3.18%
	Petroleum and Petroleum Products Merchant Wholesalers	2.73%	-0.86%	16	6	17	6.1x	2.00%
	Farm Product Raw Material Merchant Wholesalers	9.47%	0.46%	12	3	18	6.1x	2.90%

Source: IBIS World, S&P CapIQ, GF Data

## Appendix B: Industry Groups with the Most M&A Activity per Subsector

Industry Group	Subsector	Count of M&A	Industry Group Revenue(\$ in Bn)	Historical Annual Growth '18-'23	Projected Annual Growth '23-'28	EBIT Margin	Industry Revenue Breakdown
Industrial Machinery and Equipment Merchant Wholesalers	Machinery, Equipment, and Supplies Merchant Wholesalers	113	\$303.0	-0.4%	1.9%	5.4%	General purpose machinery and equipment (34.6%); Material handling equipment (10.6%); Hydraulic and pneumatic machinery and equipment (8.2%); Oil well, refinery and pipeline machinery equipment (7.8%); Metalworking machinery equipment (6.9%); Food processing machinery (1.9%); Other (30.0%)
Lumber, Plywood, Millwork, and Wood Panel Merchant Wholesalers	Lumber and Other Construction Materials Merchant Wholesalers	39	\$145.5	2.2%	2.2%	2.9%	Wholesaling lumber and boards (36.2%); Wholesaling plywood and panels (23.0%); Wholesaling wood millwork (22.0%); Other (18.8%)
Metal Service Centers and Other Metal Merchant Wholesalers	Metal and Mineral (except Petroleum) Merchant Wholesalers	38	\$270.4	2.8%	-1.8%	4.0%	Iron and steel products (53.0%); Aluminum products (16.0%); Stainless steel and alloys (15.0%); Copper and brass products (2.0%); Other nonferrous metals and products (14.0%)
Piece Goods, Notions, and Other Dry Goods Merchant Wholesalers	Apparel, Piece Goods, and Notions Merchant Wholesalers	37	\$13.2	-3.2%	0.2%	3.6%	Synthetic fibers (27.6%); Cotton fabric (15.3%); Notions (12.0%); Piece goods and other miscellaneous knit fabrics (39.5%); Other items (5.6%)
Drugs and Druggists' Sundries Merchant Wholesalers	Drugs and Druggists' Sundries Merchant Wholesalers	33	\$1,300.0	1.6%	1.3%	0.9%	Brand-name prescription drugs (69.1%); Generic prescription drugs (15.5%); Nonprescription pharmaceuticals and nutritional supplements (6.0%); Cosmetics, toiletries and other (9.4%)
Other Electronic Parts and Equipment Merchant Wholesalers	Household Appliances and Electrical and Electronic Goods Merchant Wholesalers	32	\$486.9	1.1%	2.2%	4.5%	Communications Equipment (47.0%); Semiconductors (19.7%); Computers and software (6.5%); Integrated circuits (5.3%); Other electronic components (16.6%); Other (4.9%)

Industry Group	Subsector	Count of M&A	Industry Group Revenue(\$ in Bn)	Historical Annual Growth '18-'23	Projected Annual Growth '23-'28	EBIT Margin	Industry Revenue Breakdown
Medical, Dental, and Hospital Equipment and Supplies Merchant Wholesalers	Professional and Commercial Equipment and Supplies Merchant Wholesalers	27	\$345.0	2.8%	2.6%	5.2%	Surgical, medical and hospital instruments and equipment (53.4%); Surgical, medical and hospital supplies (24.1%); Orthopedic and prosthetic appliances and supplies (10.4%); Dental equipment, instruments and supplies (6.5%); Pharmaceuticals, cosmetics and toiletries (1.4%); Other (4.2%)
Other Chemical and Allied Products Merchant Wholesalers	Chemical and Allied Products Merchant Wholesalers	27	\$254.9	1.1%	0.0%	4.3%	Cleaning chemicals (i.e., soaps and detergents) (17.8%); Adhesives, automotive and plastic chemicals (8.2%); Biofuels (7.0%); Industrial gases (6.0%); Laminate, raw plastic materials and crude rubber (2.6%); Other chemicals (58.4%)
General Line Grocery Merchant Wholesalers	Grocery and Related Product Merchant Wholesalers	25	\$272.1	-0.1%	0.8%	2.1%	Fresh meat and meat products (22.0%); Canned food (16.0%); Frozen food (14.2%); Dairy products (9.8%); Specialty food (7.0%); Fresh fruits and vegetables (6.2%); Paper and plastics products (5.1%); Other (19.7%)
Motor Vehicle Supplies and New Parts Merchant Wholesalers	Motor Vehicle and Motor Vehicle Parts and Supplies Merchant Wholesalers	22	\$278.7	1.7%	1.0%	4.2%	Mobility systems (24.6%); Thermal systems (23.2%); Powertrain systems (22.6%); Electrical/electronic components (20.6%); Other (9.0%)
Furniture Merchant Wholesalers	Furniture and Home Furnishing Merchant Wholesalers	14	\$61.1	-1.4%	1.7%	3.2%	Office furniture (54.6%); Household furniture (33.4%); Commercial furniture (7.7%); Other furniture and services (4.3%)
Industrial and Personal Service Paper Merchant Wholesalers	Paper and Paper Product Merchant Wholesalers	13	\$135.8	1.2%	0.7%	2.9%	Industrial paper and plastic products for packaging (49.1%); Carboard boxes (27.4%); Disposable plastic boxes, containers, cups and dishes (1.9%); Paper dishes and cups (1.6%); Household paper and plastic products (1.2%); Janitorial equipment and supplies (0.5%); Other paper products, including personal sanitary products (9.3%); Other products (9.0%)

Industry Group	Subsector	Count of M&A	Industry Group Revenue(\$ in Bn)	Historical Annual Growth '18-'23	Projected Annual Growth '23-'28	EBIT Margin	Industry Revenue Breakdown
Wine and Distilled Alcoholic Beverage Merchant Wholesalers	Beer, Wine, and Distilled Alcoholic Beverage Merchant Wholesalers	12	\$137.7	1.1%	1.2%	3.7%	Table wine (33.5%); Whiskey (17.4%); Vodka (11.6%); Tequila (8.2%); Rum (4.0%); Dessert wine (4.0%); Gin (1.6%); Other wine and spirits (19.7%)
Hardware Merchant Wholesalers	Hardware, and Plumbing and Heating Equipment and Supplies Merchant Wholesalers	11	\$91.1	1.5%	0.8%	6.2%	Power tools (25.8%); Hand tools (12.3%); Plywood, panels and millwork (3.8%); Paint, paint supplies and wallpaper (1.2%); Cutlery (0.8%); Bolts, nuts, rivets and other fasteners (excluding nails) (32.1%); Other (24.0%)
Sporting and Recreational Goods and Supplies Merchant Wholesalers	Miscellaneous Durable Goods Merchant Wholesalers	10	\$78.9	3.6%	0.8%	5.5%	Hunting equipment (30.9%); Bicycles (18.5%); Pools and pool equipment (13.7%); Marine pleasure craft (8.5%); Camping and fishing equipment (8.1%); Athletic exercise and fitness equipment (4.7%); Skiing and snowboarding equipment (2.1%); Billiards and other (13.5%)
Petroleum and Petroleum Products Merchant Wholesalers (except Bulk Stations and Terminals)	Petroleum and Petroleum Products Merchant Wholesalers	6	\$948.2	3.8%	-0.6%	2.0%	Gasoline (38.0%); Crude oil (18.37%); Distillate fuel (12.1%); Lubricating oil and greases (7.1%); Jet fuel (4.0%); other (20.1%)
Flower, Nursery Stock, and Florists' Supplies Merchant Wholesalers	Miscellaneous Nondurable Goods Merchant Wholesalers	4	\$19.7	2.9%	0.7%	3.5%	Bedding/garden potted plants (50.3%); Potted flowering plants (15.5%); Herbaceous perennials (11.8%); Flats (10.3%); Cut flowers (9.0%); Cut greens (1.1%); Hanging baskets (0.4%); Other supplies and growing materials (1.6%)
Grain and Field Bean Merchant Wholesalers	Farm Product Raw Material Merchant Wholesalers	3	\$254.6	5.3%	-1.0%	2.9%	Corn (49.2%); Soybeans (34.2%); Seeds, beans and rice (7.7%); Wheat (7.3%); Sorghum (0.9%); Oats and barley (0.7%)

Source: IBIS World