



Cameron Partners Insight Series

Food Industry Acquisitions Set to Continue

Hugh Cotterill, Director | November 2007

Introduction

Cameron Partners believes the recent surge in transactions involving New Zealand food companies is likely to continue.

Over the last 12 months Cameron Partners has led a number of deals in the food industry sector involving local food companies including Old Fashioned Foods, Hansells, Bernard Matthews and Taura Natural Ingredients.

Cameron Partners has a comprehensive database of all M&A transactions in New Zealand since the introduction of the Takeovers Code in 2002 and it shows that in that time, the food / beverage industry has topped the list for number of transactions completed.

This is not purely a private equity phenomenon - indeed trade players are still the most prolific acquirers, accounting for over 80% of deals completed over the period from 2003-2006. In 2006, private equity transactions still only accounted for 18.6% of all deals. Many of the transactions are "roll-ups" as existing firms seek greater scale - either to cut unit costs or in an attempt to get greater market power in the face of the concentrated supermarket industry that exists in New Zealand. Many of the firms undertaking the consolidating have private equity parents providing the funding.

Cameron Partners believes there are two major drivers of the current activity in the sector. These are:

1. The perception of the food industry as a high growth sector combined with the global focus on health that is leading to the "mainstreaming" of healthy / high quality foods.
2. Industry consolidation as firms look for scale economies (especially in distribution) to lower unit costs or to improve their channel power in response to dominant retailer (supermarket) power.

The first driver (high growth) is receiving more attention as a result of rapidly rising prosperity and urbanisation in China and India, which is impacting on global demand for "western-style" goods and services.

Healthy / higher quality foods

The global mainstreaming of the trend towards nutrition and health in foods is a powerful force and one which has reached a "tipping point" where "Functional Foods" is no longer a separate category describing foods with a health benefit - health and nutrition are now factors that every firm must take into consideration. The health trend is also driving demand for higher quality food products in general.

This health and high quality foods trend is one where New Zealand is well placed to excel. New Zealand has a great platform in our science / research and food technology skills and also in the supply of produce.

Cameron Partners Insight Series

Combine this with our clean green image and we as a country are well placed to capitalise on this trend.

While much of the media focus is on our larger food producers, the likes of Fonterra and Zespri, there are numerous New Zealand based SMEs which are well placed to ride the health wave.

An example is **Taura Natural Ingredients**, recently acquired by Sydney based CHAMP Ventures which Cameron Partners advised. Taura is a Mt Maunganui based company providing fruit pieces and paste for the nutritional snack market (like muesli bars). Taura's customers include some of the world's largest food companies in Europe and America. The company uses unique intellectual property to extract moisture but retain nutritional flavour, colour and texture. It is activities like this - with the market for inputs into things like muesli bars now stratifying into different nutritional segments – that creates opportunities for niche New Zealand companies to go global.

It is clear these developments are bringing global opportunities to New Zealand firms, and one of the drivers of recent transactions that is likely to continue is for New Zealand companies seeking the funding and capabilities to exploit these international opportunities.

Consolidation Benefits

In simple terms, industry consolidation or “roll-ups” involve integrating a number of small businesses in the same industry to create one larger company. The food industry in New Zealand is ideal for this type of transaction, with a large number of “cottage industry” businesses – often set up by owner / operators and focusing on a particular segment of the food market. The minimum key ingredients for a successful roll-up are the existence of a strong and capable “platform” business to aggregate the smaller firms and acquisitions which generate cost synergies.

The primary driving force for roll-ups in the food industry has come from companies that are owned and funded by private equity funds. Examples include

Food Holdings (owned by CHAMP Private Equity) which has recently acquired Hutchinson's, one of New Zealand's largest food importers and distributors; Gourmet Food Holdings (owned by Crescent Capital Partners) which recently acquired Simply Squeezed; and the Food Group (a vehicle of PEP).

The emergence of increasingly powerful supermarket chains in New Zealand is also requiring local food suppliers to build distribution power, occupying larger areas of shelf space, to counter retailers who are using their market power to squeeze suppliers' margins. This dynamic is not merely a local one – Woolworths' presence on both sides of the Tasman mean it exudes huge market power and has the ability to force suppliers to compete not just with other local suppliers but on a Trans-Tasman basis.

In 2006 a Cameron Partners client, **Old Fashioned Foods**, acquired Hansells Foods, a good example of a New Zealand company building scale and a better position on supermarket shelves – not just in New Zealand but also in the UK where the company has strong supermarket relationships with the likes of Tesco.

A secondary reaction to strengthening supermarket power is the acquisition of brands that provide food companies with multi-channel distribution. Examples include:

- Healthieries' acquisition of Nutralife last December means they have supermarket distribution via Healthieries brands and Health Food / Pharmacy distribution via Nutralife brands.
- Goodman Fielder's acquisition of Huntly-based River Mill Bakeries gives Goodman Fielder a greater share of the bread shelf at the supermarket, but it also gives them better distribution to local corner dairies and other small format stores.

Outlook

Cameron Partners does not see any likelihood that the trends observed in the food industry are likely to slow in the medium term. The global interest in health and the opportunities that offer to take New Zealand companies to the world will only get stronger.

Cameron Partners Insight Series

Matching New Zealand ideas with the funding and capability required for international expansion will be a continuing source of transactions in this sector.

Similarly, the consolidation trend in the food sector is likely to continue. The business case for scale economies and distribution power is very strong. There is no shortage of small and medium-sized food companies in New Zealand that are potential targets and there is no shortage of funding or capability in the firms doing the consolidating.

Cameron Partners Limited

Auckland level 16, vero centre, 48 shortland street, po box 1277, tel +64 9 912 8580

Wellington level 12, hp tower, 171 featherston street, po box 10 307, tel +64 4 499 6650