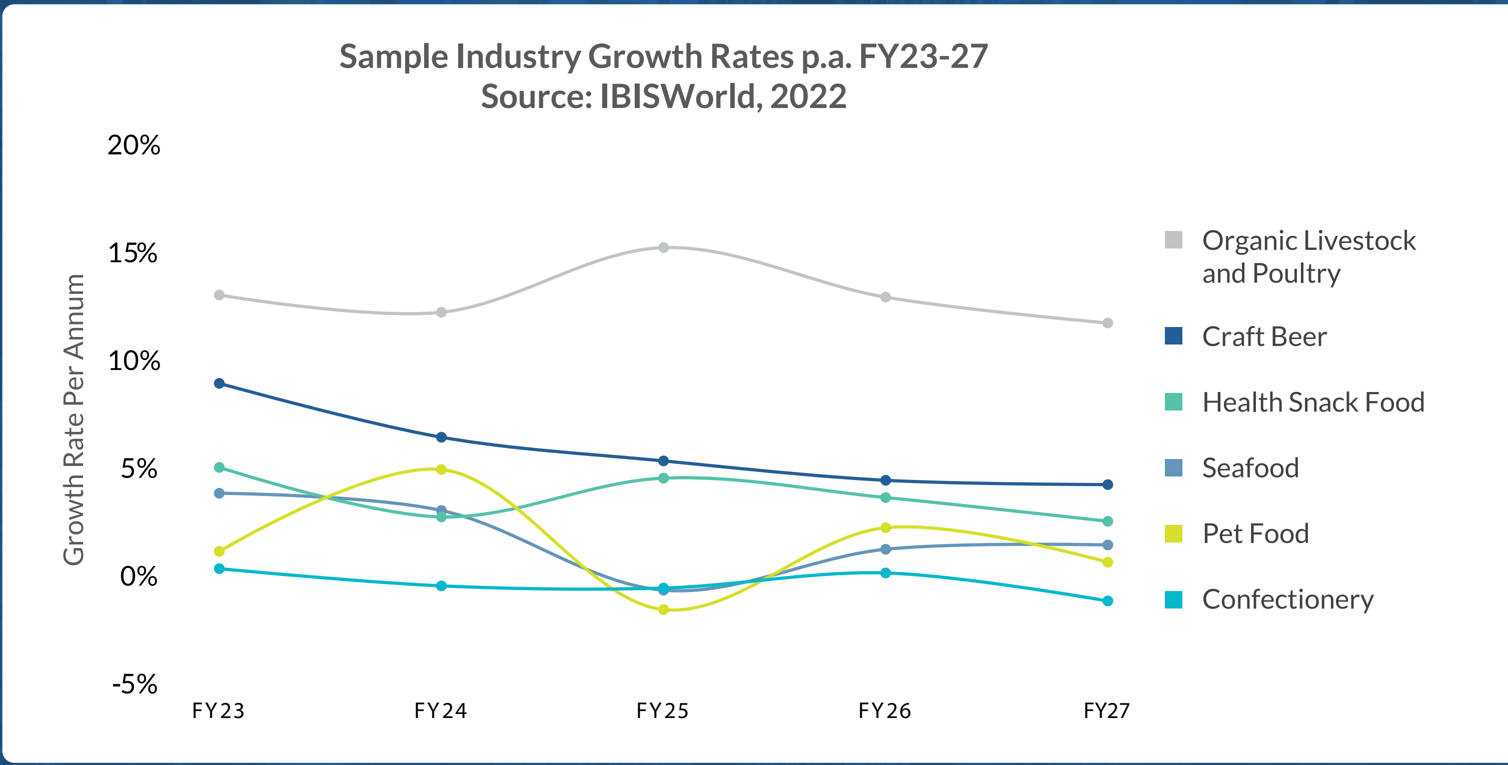
Business Sales Market Update 2023

Food and Beverage Companies

MARKET SUMMARY

Notwithstanding – or perhaps because of Covid – the overall Australian food & beverage sector has grown by an estimated 4.3% per annum in the last 2 years. However, that growth has been variable with several sub-sectors posting highly variable growth rates.



Fast growth has created greater competitiveness. Well-funded newer and innovative businesses have thrived, and the market for investment capital has been buoyant. Investors have capitalised with returns on innovative food & beverage businesses that reflect consumers ever changing demands.

In Australia, business sale transactions have also increased both by volume and value of sale. Recently, large domestic and international food & beverage companies as well as private equity have shown little hesitancy paying premium prices for smaller food companies with quality assets.

How can these shifting trends in the food & beverage industry assist business owners wishing to exit over the next five years?   For such entrepreneurs eventually keen to sell, but who have the time and patience to improve their businesses prior to sale, the timing is ripe to understand:

- How larger acquirers in food & beverage determine the quality and value of as SME food & manufacturing business? And,
- What motivates such acquirers to consider transactions of these smaller food & beverage businesses?

THE FOOD & BEVERAGE MARKET – RECENT SALES

Globally the number of sales of food & beverage manufacturing businesses improved by 11.3% in 2021 over the 2019 pre-pandemic norm. In Australia, that translated to a growth of 10.1%

This volume of sales correlates with overall food & beverage industry growth in 2020-21 as throughout Covid, consumers spent more on food and durables and less on out-of-home entertainment.

Our review of more than 70 small and medium sized food & beverage transactions in Australia in 2021 revealed the following:

- By quality, the largest number of transactions came from the following food sectors: alcoholic beverages, snacks, food service distribution, plant-based foods, and seafood.
- A significant number of business sales were from larger food companies and interestingly, private equity. Normally acquisitive large food businesses such as Arnotts, Procter & Gamble and Lion were joined by private equity groups such as Quadrant, TPG Capital and Liverpool Partners to acquire business in niches like non-dairy products including plant-based creams and coconut yoghurt.
- There was a strong acquisitive focus on product and brand innovation particularly in sectors such as plant-based food products, healthy snack foods, ready to eat meals and even high quality “human grade” pet food.
- There was significant interest in positive brands, particularly catering for active, heath conscious millennial demographics.
- There was some decline in foreign buyers’ interest in Australia businesses, though this is at least partly attributable to Covid19 travel restrictions. Nonetheless Asian acquirers continue to consider Australia as a great location to grow or manufacture healthy food options that can be exported to larger, particularly Asian, markets.
- There was some off-loading of distressed food & beverage assets, particularly in dairy and desserts. Increasingly we expect that larger food companies will seek to offload underperforming divisions to other businesses more aligned with a similar market.

VALUATIONS

The most common question asked by business owners is: “what’s my business worth?”

Here are some pointers about current sales and their values. Sale values are typically gauged as a multiple of current profit. So, if a business with an EBITDA of $1.5m sells for $4.5m, the multiple is 3x.

Food & beverage businesses with sales less than $2 or 3 million whose acquirer will be a smaller operator, or an investor intending to work in the business, broadly assume a multiple of between 1.5x and 3x of average profit for the last three years.

This average does not include businesses that fail to sell. It is estimated that around 40% of businesses such as these don’t transact in a sales campaign. Also, around 20% of solvent business close without finding a buyer.

Smaller food & beverage businesses are considered riskier than larger businesses as the latter tend to be more substantial and stable. They have found a way to grow beyond the owner’s efforts and aren’t reliant on that owner.

As the turnover and the profitability of food & beverage businesses increases, deal size increases and the multiple tend to increase as well. The median EBITDA multiple for deals of a value between $20m and $50m averages 8.7x, but the range could be as low as 2.5x and as high as 12x.

Valuation multiples across food companies have increased around 5-10% over the past three years, most significantly in the more innovative alcohol sectors, plant-based food, and healthy snacks and ready to eat meals. Packaged food multiples have remained stable.

Just over 70% of all food & beverages acquirers were Australian based, with international acquirers mainly participating in higher value deals.

Groves & Partners

VALUE ENHANCERS

The greater your portfolio of revenue, profit and growth producing assets within your food & beverage business, the higher you are likely to be valued by acquirers.

FINANCIAL

Effective management systems in place to manage stock, cash flow, efficiently utilise production assets and possess a far-sighted approach to financing growth is a key driver of value.

PRODUCT

A wide and expanding product range, proactiveness in product innovation through a market aware approach that ensures new product development, ingredient mixes, packaging and optimisation of retailer support are all strong value drivers.

CUSTOMER

A deep awareness of market shifts and the ability to consistently excite consumers through producing the "next best thing". In pet foods the pandemic resulted in deepening bonds between people and their pets have resulted in an upsurge in quality, "human grade" dog food. Awareness of and responding to customer trends is key to driving values.

PEOPLE

A business that values its employees, motivates them, and invests in them through training, participation, involvement, and recognition is more highly valued than one that doesn't. This results in productivity, efficiency, loyalty and product and process innovation.

SYSTEM

Covid has made businesses more aware of their operational weaknesses. Integration of internal systems and cloud-based supply chain processes enables food manufacturers to grow and scale through standard operating procedures. A digital platform can assist with ingredient location tracking, storage, reduction of food waste and minimised food safety risks. These system features tend to drive higher valuations.

COMPETITIVE

Great distribution reduces dependency on the main supermarkets to stock product. Contracts and agreements with downstream markets including supermarkets, wholesaler and retailers reduces revenue volatility and guarantees demand. The best food producers become more omni-channel, implementing e-commerce, enabling direct delivery to retailers and direct to consumer via the internet.

BRAND

Positive public perception of brand established through effective marketing and a great reputation is key to value. Branding enables food producers to end customer relationships through being explicit about matters such as the ethical sourcing of ingredients, food preparation tips and techniques and expanded direct to consumer helplines and chatbots.

IP

This is a food & beverage businesses proprietary knowledge that underpins current and future products and customers. The future values of a business depend on a portfolio of intellectual property assets or trade secrets that ensure innovation and competitiveness.

WHO ARE THE BUYERS?

Large Australian and internationally owned food & beverage businesses

They'll have the financial means to acquire smaller businesses. They include the largest food businesses with multi-billion turnovers such as Fonterra, JBS, Coca-Cola Amatil and Lion.

They seek growth niches and to strengthen the niches they already occupy.

Many are active reviewing and buying small and medium Australian food & beverage businesses. One of the world's largest food companies, Mondelelez International, recently purchased small Melbourne based premium cracker manufacturer Gourmet Food Holdings, recognising the worldwide appeal of brands such as OB Finest, Olina's Bakehouse and Crispbic. Another, Procter & Gamble acquired VOOST, an Australian market of effervescent supplements.

Australian Publicly Listed businesses

As of May 2022, there are 66 publicly (ASX) listed Australian businesses. An ASX listing more likely means they are liquid and therefore more able to raise capital to fund acquisitions. Many look for "accretive" deals meaning they can increase their own value by making acquisitions that buy at a multiple higher than a typical private-to-private transaction multiple but below the trading multiple on the ASX. This transaction increases their total market valuation at above the rate paid for the target business.

In 2021 a significant proportion of the total number of acquisitions of food & beverage businesses were made by ASX listed businesses. Most notable in 2021, the ASX listed food business Maggie Beers Gourmet Food successfully raised capital to diversify into eCommerce with their $40m acquisition of Hampers & Gifts Australia.

Private Equity

Private equity uses private investor funds to acquire all or part of food & beverage businesses. They seek to improving their financial performance through operational measures or synergies with other related acquisitions prior to divesting them.

Private equity was involved in several 2021 transactions within food & beverages. These included Accolodate (Carlyle Group) acquiring Rolf Binder in premium wines and health foods where Openly Food company (Five V Capital) acquiring Annex Foods, Metro Foods and Table of Plenty.

Large non-food businesses seeking diversification

Not all strategic acquisitions came from within the food industry and there may be strategic reasons why a non-food and beverage business would do so.

In 2021, training company F45 purchased family-owned Australian nutritional supplements group True Protein, with a view to distributing product through its own network in 1,700 fitness studios globally.

Other

This category of non-strategic buyers includes private owner / operators buying food & beverages businesses and either managing them directly or appointing an operational manager. These acquisitions typically produce the lowest sale multiples.

FUTURE TRANSACTION FORECASTS

By international standards, Australia has very deal receptive economy with the number of transactions in FY21 being the world's fifth largest. This will continue thanks to Australia's abundant natural resources and its geographical location.

Australian small and medium food & beverage businesses are increasingly sought after by larger businesses and private equity. A hot M&A market creates a hotter market as those not participating in the initial dealmaking suffer from FOMO (fear of missing out).

Well managed, growth-oriented food & beverage businesses can attract multiple potential buyers in an "in demand" niche of the industry. Often the high level of interest creates competitive tension at sale time. Eventual success does require significant alignment between the assets of the selling business and the motives of the strategic buyer.

An attractive food & beverage business will have carved out a successful niche in a part of the industry that is difficult for new entrants to copy. High growth niches include craft beer, pre-packed meals, plant-based meats, and distillers and vintners.

However, one cannot discount the current volatility of the Australian food & beverage market due to rising interest rates, inflation, supply chain challenges and the ripple effect resulting from the war in the Ukraine.

While the number of transactions is likely to grow, this optimism should be modified by several factors, namely:

- Overall political and economic volatility.
- The risk that deals remain unconsummated because seller expectations are too high.
- An increased supply of food & beverage businesses with ageing owners seeking to exit.
- Many businesses are not saleable by virtue of their lack of profitability, growth, dependence on their current owner and market positioning.

Owners often make false assumptions about the value of their business. Many overvalue it based on sentimentality. Some undervalue it based on an exaggerated view of the business' weaknesses and competitive threats. Some owners also tend to procrastinate, thereby pushing their exit plans out.

It's Strategic Transactions experience that many food & beverage businesses suffer an "asset gap" namely the difference what the owner needs the business to be worth at sale time compared to what the business is worth now.

PURCHASER APPETITE

There are eight major reasons why a larger acquirer may seek to buy a smaller food & beverage business.

IP

Established large food & beverage businesses often aren't great innovators. They may seek to buy in innovation, often from start-ups or producers of niche products. The rationale for this is clear – internal development is risky, both in terms of time, effort, and the probability of success. That risk can be defrayed by buying in technologies, processes and products that have already been proven in the marketplace.

Examples of acquiring innovative products and technologies abound. The Kombucha market has significantly grown and resulted acquisitions from the likes of Coca Cola keen to capitalise on the technology processes behind organic, natural fermentation. More recently, the Ecoganic farming methods (red tipped bananas) were a valued asset in the 2021 acquisition by Marketing Perfection Fresh of Pacific Coast Produce. The intellectual property behind plant protein-focused enterprise was valued highly in HPP's acquisition of EVR Foods and food giant Bunge invested $45.7m in Australian Plant Proteins a supplier of protein isolate powders sourced from Australian pulses.

GEOGRAPHIC

Acquirers may look for a business that is strong in a specific location so they can also sell their own products within that territory. At the same time, they can take quality product from the seller and, through their much larger marketing budget, provide those products with a much larger geographic footprint.

Mighty Craft's 2021 purchase of the Adelaide Hills Group has enabled South Australia's high-quality craft beer and wine to reach a larger market. Likewise, Tasmania's reputation for fresh, quality foods has encouraged acquisitions from local and interstate. Local producers such as Pure Foods Tasmania increased their scale in Tasmania through acquisitions including Cashew Creamery and Lauds Plant Based Foods. Also, a large acquirer may use the current geographical footprint of a smaller seller to get access to their geographical market. The acquisition of Select Fresh Group by Costa gave them access to the WA market and state of the art warehouses in Perth.

CONSOLIDATION

Consolidating operations within food & beverage product can result in significant savings or improvements in efficiency. In food & beverages merging two or more production plants, breweries or distilleries can result in improved product capacity and significant economies of scale. Additionally, specialised production facilities, for example for and acquiring vegetable grows can make access to facilities like large glass houses far more cost efficient.

Acquisitions in the craft beer industry have accelerated through acquirers like the giant liquor company Lion buying up craft beer brands such as Little Creatures, Four Pillars and New Belgium. Most recently, Fermentum's purchase of Two Birds Brewing and Lark Distilling Co., acquisition of the iconic Pontville Estate and Distillery has enabled these impactful brands to be produced more efficiently. Within dairy, Nature One's acquisition of Nepean River Dairy has given it access to excess capacity in manufacturing. In food services, New West Foods acquisition of Elite Food Co made it cost effective to utilise a larger site allowing for larger freezer, chiller, and dry storage for an new expanded product range in fresh, frozen, chilled, and dry goods.

MARKET SHARE

Acquirers often consider that it is easier to acquire an existing product range than to try to replicate that product range by building it themselves. The acquirer can sell more food product to their existing customers, sell their own product to new customers, or extend their product range. Greater market share also provides additional leverage for greater supermarket or bottle shop shelf space.

Acquirers are also looking to fill all spaces within a specific product category. The large company Kilcoy acquiring lamb assets to complete its meat portfolio is an example of this. Also two similarly sized business may merge in order to increase their market share, such as Booze Bud's acquisition of Get Wines Direct to form one of Australia's largest online liquor retailers while maintaining separate branding.

CUSTOMER / CHANNEL

Aside from increasing market share through acquiring the customers of the acquired food & beverage business, the acquirer also has access to their distribution channels. Commonly in the food industry, acquirers may seek to vertically integrate enabling them to control more of the supply and product chain, such "farm to market" strategies.

F45 acquired True Protein to enable sales of True Proteins product through their own network of 1700-odd fitness studios globally. Larger businesses will also acquire to diversify their customer base such as the decision by Patties Foods, the owner of Four'N'Twenty Pies and Herbert Adams and Nannas baked goods, to scoop up a ready-to-eat meals business called Fitness Outcomes.

KEY PEOPLE

The seller may have an extensive knowledge base of skilled personnel that can provide expertise to drive the buyer's business. In niches such as winemaking, capturing the expertise of the people employed are a key driver towards acquisition of a business. Fundamental to an acquirer's due diligence is to evaluate the skills, commitment and stability of the target company workforce. Typically, they seek a qualified, educated, future focussed and motivated workforce with an emphasis on employee upskilling while the leadership is supportive. This ensures continuity for the new owners and the confidence that the merged companies are likely to work together harmoniously.

Often the charismatic founder adds significant brand value to the acquirer, and the acquirer will seek to retain the founder. This is particularly so in the craft beer industry where Mighty Craft recognised the value of the key people in the Adelaide Hills Group and sought to maintain their individual personalities within the merged group.

PRODUCT / EXPANSION – DIVERSFICATION

The products marketed by the seller can be rebranded and sold by the acquirer to the customer. More significantly, many cashed up or publicly listed food & beverage corporates seek to pick "winners" early on and acquire to develop these businesses. The acquirer may also have access to some developing technologies, products, and services.

The giant JBS, traditionally a beef specialist diversified into both pork through their acquisition of Riverlea and seafood through Huon Aquaculture, Aaron Zerefos acquisition of Drinkscene has enabled a milk distributor to diversify into broader non-alcoholic beverages. Cases of diversifying into related markets are abundant, Arnotts bought Diver Foods as an entrée into breakfast cereal and snacks sector while pie market, Patties Food diversified into health food by purchasing fitness outcomes. Global food company Procter & Gamble acquired the high growth vitamins, minerals, and supplements company, Voost while alcoholic drinks manufacturer Asahi purchased Allpress to diversify into coffee.

DEFENSIVE

A buyer may acquire to remove a competitive threat, strengthen their own market position in a competitive marketplace or lock in supply. The net effect may be to reduce the number of players in a market. A defensive acquisition could be a response from a new competitor entering a market, a competitor becoming stronger, or to remove excess capacity in a market.

Chinese company, KGF's 2021 acquisition of lamb producer, Hardwicks in enabled KGF to deepen their Australian meat asset portfolio. It enabled them to pool their diverse assets to capitalise on revenue and cost synergies strengthen their positioning against adverse market conditions.

PREPARING FOR MARKET

Strategic Transactions tips for owners considering the sale of their Food & Beverage businesses in 2023 and beyond:

1.

Review the assets of your business - your people, your products, your customers, your brand. How can you leverage these assets for greater profitability and growth? The higher your potential profits, the higher your value.

2.

Have a defined, believable, realistic vision of how you or the future owner of your business can drive the future of the business.

3.

Partnerships and alliances are more common. Several of the 2021 acquisitions originated with alliances and were consummated because of trust and sustainability. However, be cautious that entering alliances may restrict options for exit at sale time.

4.

Don't overinvest. A niche producer of garlic bread may not need the latest and greatest high-capacity French ovens if their potential acquirers likely possess state of the art industrial bakeries. While your eventual buyer may be interested in your current profitability, the acquirer's calculation of ROI for your business is more based on your key assets under their operating model.

5.

Stay in touch with the market. Track food & beverage market trends and who else in food & beverage is buying and selling – and most important, why?

6.

Be responsive to approaches from the market to acquire your business. Understand what the potential acquirers' motives are, but do not enter any exclusive arrangements with an acquirer without involving both an advisor and approaches to other market players.

7.

Remain focus on growing your food & beverage business, regardless of distraction from acquirer approaches. Ultimately your business will be valued on its current financials and growth prospects and such parameters cannot be allowed to slip while you are buried in negotiation.

8.

Take very seriously the need for confidentiality throughout your phase of planning for sale. Employee uncertainty about their future careers may result in the loss of key people.

9.

A poorly executed campaign to sell your business can result in reputational damage and the potential loss of key personnel, suppliers, and customers. Do your own due diligence on your advisors.

10.

Consider seriously not just the price for your business, but also the terms and structure of the sale. Many sales involve earn outs, money in escrow or other acquirer proposed terms to ensure that they can maximise their future growth rates and mitigate their risks.

11.

As far as possible, attempt to eliminate any dependency that the future new owners may have on yourself or your key personnel. The more of a turnkey operation using standard operating procedures they acquire, the higher the valuation.

12.

Ensure that your website and blogs and marketing materials are kept fully up to date. Buyers will gauge a seller’s commitment to quality and growth on how the business is presented.

13.

Consider buying a smaller business to make your product range more compelling, have new customers or achieve efficiencies.

14.

Systemise everything – preferably in organised and shared electronic files and systems so that a buyer can more navigate around your business. Ensure that all paperwork is in order- particularly financial and personnel records.

15.

Attempt to correct any imbalances that could be perceived as risks for a future acquirer – use of contract manufacturers, optimised logistics and inventory management, dependencies on large supermarket chains.

16.

Increase the proportion of certainties in future revenues by contractually lock in customers or suppliers that can withstand a change of ownership.

17.

It's never too early to consider your personal post-sale personal goals. Don't regret your decision to sell.

18.

Take advice early on about your after-tax financial situation. Business owners can find themselves with major tax liabilities post-sale and these can be minimised if corrective action is taken upfront.

19.

Consider the possibility of an acquisition by your management team and how this could be financed.

20.

Remove as many skeletons in the cupboard as possible. Legal and contractual issues, whether they pertain to staff, suppliers or customers must be resolved prior to marketing the business otherwise the risks may weigh down the valuation.

21.

Be prepared for a lengthier sale process that what you may have envisaged. While eight month is the average for a food & beverage operation, many take longer particularly with buyer due diligence.

22.

Consider the broader social, sustainable, and environmental effects of your business. It's support for the wider community, its ethical standing, its branding reputation. the The most profitable businesses are often the most ethical since they attract the best employees and have the strongest relationships with ethical suppliers and customers.

THE NEXT STEPS?

Strategic Transactions really understand the food & beverage industry and we work beyond just finding deals and executing transactions. Through our Fit 4 Sale services, we'll prepare you to maximise your transaction value – even if it is several years away.

We provide critical support throughout the negotiation and due diligence process. Strategic Transactions goal is to find you the best deal terms and structure and, in the meantime, normalise your working environment so that your business can concentrate on its operations and profitability.

Contact us for a confidential consultation to find out how we can work with you.

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Mark's vast business transaction experience guides food & beverage business owners on lucrative ways to build and present their business pre-sale and during the sale process.

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