

Bite Size

Recent activity in the food and beverage sector

Autumn 2013

Welcome to the latest edition of 'Bite Size', our quarterly overview of activity in the food and beverage sector.

This edition provides analysis of M&A activity in the third quarter (Q3) of 2013, which was notable for the sale of the iconic Lucozade and Ribena brands to a Japanese buyer and for a continued increase in the level of private equity acquisition activity.

In addition we provide insight into some of the changes that companies can expect under the new UK GAAP accounting standard, which becomes effective on 1 January 2015, as well as presenting a case study of Brunei Wafirah, the rapidly growing provider of high quality Halal food and drink.

We hope that you find this newsletter useful. If you have any further questions or queries, or would like to know how Grant Thornton can help you and your business please do not hesitate to contact me.

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New UK GAAP: The future is here!

From 1 January 2015 the UK's new accounting standard, FRS 102, becomes effective for all companies currently adopting UK GAAP. This transition could have significant implications for your business.

The transition date is not far off, so it's key to start planning for this change now.

The effective date is years beginning on or after 1 January 2015, with a requirement to restate comparatives. So, if you have a December year end you will need to re-state the 31 December 2014 figures, including the opening balance sheet for that year, 1 January 2014 – this is the transition date.

There are important differences in accounting treatment, as well as changes to the presentation of the financial statements.

A key accounting change relates to financial instruments. The value at which they are recognised will depend on whether they are straightforward (no change) or more complex. More complex instruments may need to be recorded at their fair value, and will include instruments such as foreign currency forward contracts and interest rate swaps.

There are also likely to be measurement differences on long term intra-group loans that are not on market terms.

There may be changes in the classification of leases, as there is no longer a 90% test but a range of indicators requiring judgement. Lease incentives will be spread over the whole lease term. Transitional provisions are in place where existing leases

will continue to be treated in the same way as they are currently, but the changes will need to be considered for future leases.

FRS102 has a requirement for an accrual to be made relating to holiday pay. If your holiday year does not align with the accounting year then this could result in an additional liability.

The above are just a few examples of issues that may impact on your business, but it is going to be important to go through your accounts line by line to identify other areas affected. Some items will impact on profits, and so wider considerations around covenants and performance related pay will also be required.

In addition there are practical considerations for example training of staff, ensuring systems can deal with the change and managing stakeholder expectations.

We encourage you to start considering your transition early and Grant Thornton will be happy to assist you, not only from an accounting perspective but also the wider business implications, please contact:

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M&A activity - Q3 2013

Q3 2013 – deal volumes decline...

After an encouraging pick-up between the first and second quarters of the year, deal volumes fell in Q3 2013^[1], dropping by 32% compared with the second quarter. Deal activity, however, was very close to the average third quarter volume recorded for the last four years. On a more positive note, disclosed deal values increased by 10% and the number of distressed M&A deals declined^[2], as the rate of business failures slowed further.

... but overseas buyers still have appetite for brands

Overall there were fewer acquisitions of UK and Irish companies by foreign entities in the third quarter. The number of deals with an overseas buyer dropped by 50% in Q3 2013 compared with Q2 2013. However, in the period's largest deal, Japan's Suntory Beverage and Food acquired the Lucozade and Ribena brands from GlaxoSmithKline for £1.35 billion. While there was speculation that Suntory's rationale was geographical diversification through improving its UK footprint, the Japanese company said that its focus was more on leveraging the two brands in overseas markets.

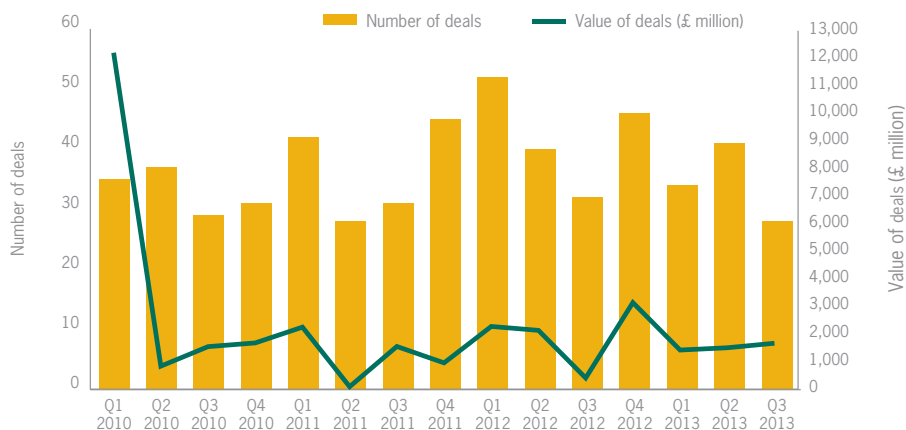
As well as overseas buyers looking at UK targets, UK-based companies are eyeing the growth potential of Asia. PZ Cussons, better known for its soap brands, moved into the Asian nutrition category, agreeing to buy Rafferty's Garden, the Australian baby food brand, from private equity group Anacacia for £42.2 million. Rafferty's Garden has a 40% market share in the Australian wet baby food market and is expanding into Asian export markets.

While buyers from emerging market countries such as India, China and Africa were absent from this quarter's deal activity, companies in these geographies continue to view the UK food and beverage sector as an attractive and safe place to invest. Acquiring UK companies provides an opportunity to leverage their know-how in manufacturing, branding and quality standards in emerging markets, where consumers are becoming increasingly sophisticated, with spending patterns more similar to their developed market counterparts.

...and private equity is increasingly active

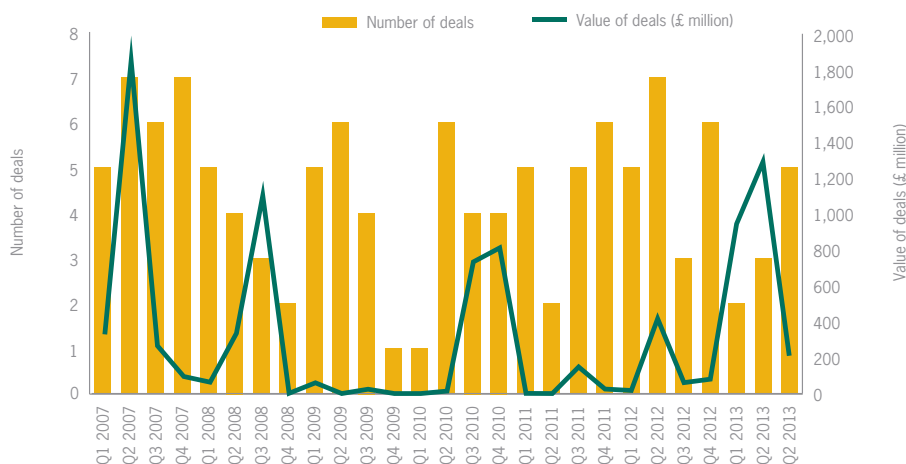
After doubling between the first and the second quarters private equity deal activity

Announced M&A activity in food and beverage - quarterly



NB: the spike in 2010 deal values is attributable to the Q1 acquisition of Cadbury by Kraft for £11.9 billion

Announced PE activity in food and beverage - quarterly



"Despite the drop in deal volumes this quarter, from my conversations with our clients I am continuing to detect an appetite for deals among food and beverage companies. In part, this reflects the need for many mid-sized companies, which historically have grown organically, to consider acquisitions because their growth is stalling as the patterns and levels of consumer spending change. The environment is tough: the 12 month period to Q3 2013 is the first year on record that UK food sales volumes have declined. Prices are rising in response to higher raw material costs, there has been a shift away from promotional activity by retailers and consumers are shopping differently; convenience and top-up shopping is increasing, which is reducing food waste, but also purchase volumes. Mid-range brands, meanwhile, face stiff competition from either side as both the discounters and the high quality offerings of the multiples continue to take market share. Against this backdrop, companies will look externally for innovations and product development skills that they don't currently have in-house."

Trefor Griffith
Head of Food and Beverage

in Q3 2013 increased by a further 25%. The acquisition of brands, particularly where there is scope to increase value through innovation, is one of the factors underpinning this continuing improvement in the level of transactions. In addition, many private equity groups are sitting on cash reserves that they need to deploy. More generally, an increase in the number of debt funds and greater appetite among lenders has led to an improvement in debt market conditions and more leverage is available for the right quality deals.

Against this backdrop, the third quarter provided further evidence of rising private equity interest for larger mid-market deals. In a competitive secondary private equity transaction, Langholm Capital sold Tyrrells, the leader in the niche gourmet crisp market, to Investcorp for £100 million. Under Langholm's ownership, Tyrrells

Deals summary - Q3 2013

has diversified into other snacks, such as popcorn, and has expanded into export markets. Investcorp, which is experienced in growing premium brands, is expected to continue Tyrrells' expansion into overseas markets, focusing on France, Germany, the Netherlands and the US.

In another auction dominated by private equity, European Capital sold dried fruit products firm Whitworths to Equistone Partners for £90 million. Whitworths is an established brand that has already extended into the higher-growth higher-margin children's lunchbox market and it will be interesting to see where Equistone takes the brand next.

Turnaround private equity group Rutland Partners took a controlling stake in Bernard Matthews, the biggest producer of branded turkey, for an undisclosed sum reported to be in excess of £20 million. With the injection of fresh funds Rutland hopes to reinvigorate Bernard Matthews, which returned to the black in 2012 after struggling financially in recent years.

Consolidation is an important deal driver



English wine is a fast growing, but fragmented market and M&A activity in the third quarter was focused on consolidation as a precursor to further expansion in the sector. Shellproof Wines, which listed on AIM in 2012, agreed to buy Gusbourne Estates vineyards for £7 million and plans to increase its planted acreage of vines over the next two years. Chapel Down Group bought the remaining 30% minority stake it did not already own in Curious Drinks and plans to invest in both its vineyards and its beer business.

There was also consolidation activity in the dairy sector. Müller Dairy, which bought Robert Wiseman Dairies in 2012, has been keen to drive further consolidation and in Q3 2013 bought Nom Dairy UK for an undisclosed sum. Finally, in the deli sector, SHS Group, whose herbs and spices division trades as British Pepper and Spice, made a complimentary acquisition of The Crucial Sauce Company, also for an undisclosed sum.

Large deals with disclosed values (>£250m deal value) ^[3]

Sector	Date	Target	Acquirer	Deal value (£ million)
 Soft Drinks / Functional	Sep-13	GlaxoSmithKline plc's Lucozade and Ribena brands	Suntory Beverage & Food Limited	1,350.0

Mid market deals with disclosed values (£50m - £250m deal value)

Sector	Date	Target	Acquirer	Deal value (£ million)
 Dry Grocery	Sep-13	Whitworths	Equistone Partners	90.0
 Confectionery	Aug-13	Tyrrells Potato Crisps	Investcorp	100.0













Small deals with disclosed values (<£50m deal value)

Sector	Date	Target	Acquirer	Deal value (£ million)
 Alcoholic Drinks	Sep-13	Gusbourne Estates	Shellproof Wines	7.0
 Meat, Fish & Poultry	Aug-13	Bernard Matthews	Rutland Partners	20.0*
 Alcoholic Drinks	Jul-13	Curious Drinks	Chapel Down Group**	4.3
 Functional	Jul-13	Rafferty's Garden Pty Limited	PZ Cussons	42.2

* estimates put this at £20m but it's possible that the deal value is in excess of this amount.

** Chapel Down acquired the 30% in Curious Drinks that it did not already own

Key undisclosed deals

Sector	Date	Target	Acquirer	Deal value (£ million)
 Meat, Fish & Poultry	Sep-13	Bramley Foods	Underwood Meat Company	ND
 Meat, Fish & Poultry	Sep-13	McCarren Meats	Kepak Group	ND
 Dairy	Sep-13	Nom Dairy UK	Müller Dairy	ND
 Soft Drinks	Aug-13	Pride Foods	Refresco Group BV	ND
 Bakery	Aug-13	Pooles of Wigan	Midland Bakery	ND
 Dairy	Aug-13	St Helen's Farm	Primula	ND
 Functional	Aug-13	Charles & Alice	"CM-CIC Capital Finance Equistone Partners Europe Limited"	ND
 Meat, Fish & Poultry	Jul-13	Young's Seafood Ltd's Stornoway operation	Macduff Shellfish (Scotland) Ltd (owned by Change Capital)	ND
 Functional	Jul-13	Jiangsu Howbetter Food Co., Ltd	Tate & Lyle	ND
 Catering	Jul-13	Bite Catering	Catermasters Contract Catering	ND
 Deli	Jul-13	The Crucial Sauce Company	SHS Group	ND
 Wholesale & Distribution	Jul-13	Peter Lowrie & Company	AF Blakemore & Son	ND

Notes

[1] All deal activity is based on announced date of the deal and includes deals where there has been any UK or Ireland involvement (target or acquirer). Administrations, liquidations and receiverships are collated but not counted as M&A unless they have subsequently been acquired.

[2] Business failure data includes administrations, receiverships and liquidations. For the purposes of collating failure statistics, all 'failures' are counted irrespective of whether they were subsequently acquired. Only business failures announced in the press are included in the count for years 2007-2011. For 2012 onwards London Gazette data will also be included.

[3] Deal values are primarily sourced from corporate websites, however if no press release is available they are sourced from deal database BvD Zephyr or from press commentary released at the time of the deal. Deal values may subsequently be amended pending earn outs or other finance arrangements or / and as further detail is released by the acquirer.

Sources: All deal data is gathered as it takes place from numerous sources including trade press, BvD Zephyr and ThomsonReuters.





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Tomorrow's Lifestyle

Case study: Brunei Wafirah UK

Birmingham-based Brunei Wafirah UK is the fast-growing subsidiary of Brunei Wafirah Holdings, which owns the Brunei Halal brand. The company is undergoing a rapid period of expansion, which will broaden its business model from distribution to manufacturing and export of high quality halal food and drink products.

Brunei Wafirah Holdings was founded in 2009 by the Brunei government to create a global halal brand. Its UK subsidiary plans to be a consolidator in the fragmented UK Halal market, creating an affordable, high-quality range of food and drink products supplied through a fully integrated supply chain in which Brunei Wafirah controls and guarantees the process at every stage.

Halal, however, is much more than slaughtering according to muslim religious guidelines. "Halal has a broader meaning," says Dr Mohammad Nazir, Brunei Wafirah UK's CEO. "It's all about good healthy eating, which has a positive impact on mind, body and spirit." Halal, therefore, is very well aligned with the trend towards healthy eating evident in the food and beverage sector. The brand will appeal to people of any ethnicity, not just muslims and 20% of Brunei Wafirah's initial customer base is non-muslim. Equally, as second and third generation muslims become more integrated into UK culture there is demand for a range of European style dishes, such as lasagne and cottage pie, produced according to Halal standards.

Brunei Wafirah UK started by building a distribution network for products manufactured by third parties. In the autumn

Looking forward

Inevitably, the timing of transactions leads to fluctuations in deal volumes from quarter-to-quarter and despite the drop in activity in Q3 2013, the M&A outlook is generally positive. Against a better economic backdrop the companies that we talk to are more optimistic. Recent government efforts to support exports by SMEs are also particularly welcome.

Of course, companies still face a number of challenges. For example, our latest sector report, *Hunger for growth*; Food and Beverage looks to the future, highlights among other things companies' concern over the on-going volatility of raw material prices. There is also evidence that vendors' value aspirations are providing a hurdle to completing

acquisitions. The repercussions on supply chain management from the horsemeat scandal, too, have yet to fully filter through the sector. As the multiple retailers re-focus on their supply chains and testing procedures, this creates knock-on effects on investment by food producers.

In this issue we have already discussed the changing patterns of consumer spending as a driver for M&A. More broadly, companies must also address the challenges raised in producing food and beverage solutions for a UK population that is both increasingly ethnically diverse and growing older. Challenges, however, also create opportunities and we expect to see more deal activity in the coming months.

of 2013 the brand will be rapidly rolled out to 1600 Costcutter stores and then launch with one of the major multiple retailers. The company is now looking to jointly produce products with third parties and in the next 18 months to build or acquire manufacturing facilities. With growth via acquisition high on the company's agenda, Grant Thornton's local corporate finance team have been working with Brunei Wafirah, using their sector knowledge to seek out possible acquisition opportunities. The firm also has an audit relationship with Brunei Wafirah, which given the rapid pace of change, places emphasis on being responsive to the company's needs.

Over the next six months Brunei Wafirah will also expand into export markets, both in Europe and the MENA region. "There is an opportunity for the UK to become a hub for the export of Halal products into the MENA region and ultimately back into Asia," says Dr Nazir.

What do you think?

Your thoughts and opinions are important to us. Please let us know what you think of this newsletter by contacting:

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