The merger and acquisition wave in the pet industry

By: Bob Hanson

Over the past few years, mergers and acquisitions (M&A) have been one of the hot topics in Western European countries and one of the major influencers and agents of change in the economies and economic development of many countries.

The strategies behind M&A

The growth of private equity companies and their impact on the corporate landscape, also in the pet industry, has been significant, driving companies to review their operations as well as their financial performance. They have been variously seen to be 'value creators' where they seek to rejuvenate underperforming companies after takeovers. On the other hand, many politicians and trade union leaders in particular have called them 'locusts' as they are seen to be short-termist and only interested in sucking money out of their targets to the detriment of the company, staff and other stakeholders.

Whatever your view of private equity, one thing is certain: M&As are a fundamental part of the world of business – and that applies to the pet business too! In recent times, there has been an increase in the number of deals as well as the value of the deals in the pet industry (see also the article on page 58-59).

Private equity and the pet industry

To make a deal, there have to be both buyers and sellers. But what are the reasons and strategic background to companies' decisions to acquire another company, or for a company to put itself up for sale? Let's look at some of the reasons and circumstances.

The pet industry is currently attracting growing interest from investment funds and other institutions outside the pet industry. As we all know, the industry is profitable and growing, as the number of pet owners around the globe is increasing and, consequently, more money is being spent on pets each year. Whilst perhaps not being crisis-resistant, the industry is certainly more resilient than many others, as we have seen during the recent recession.

Kohlberg, Kravis & Roberts (KKR) are one of the best known private equity investors and they acquired the UK pet retail chain Pets at Home in 2010. This year, they are in the middle of a $4 billion (€2.8 billion) acquisition of Del Monte. Del Monte had also built a big pet food business themselves through acquisition, by buying the pet food business from HJ Heinz (which includes the former Quaker Oats pet operations), the Milk Bone dog biscuit brand, as well as the Meow Mix Company.

There are other examples of similar investments too. A couple of years ago, Penta Investments, a Czech investment group, bought the Gimborn cat litter (Biokat's) and cat food and snack business (under the Gimborn and Gimpet brands) and the now 142-strong Pet Center retail business in Eastern Europe from another finance investor. In addition, only last year, Perusa, a Munich based fund, bought Karlie, one of the leading accessory companies across Europe. These are unlikely to be the last moves from investment groups in Europe and elsewhere.

These investment companies see opportunities to rationalise businesses when combining them together to achieve cost savings, as well as the opportunity to drive top-line growth and profits through a more aggressive sales and distribution push, often into new markets and categories.

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Strategic rationales

Let's start with companies and owners who want to sell all or part of their company. Why do they do that and what are the reasons behind this?

Retirement

After World War II, lots of companies were formed by entrepreneurs and many of those owners are now in their 60s or 70s. Many want to retire and where there is no obvious family member with the skills or interest to take the company forward, the company is often put up for sale.

Change of strategy

In this changing world, companies adapt to their changing circumstances and reflect on their future direction and strategy. This sometimes means that products, brands or whole divisions or factories are no longer core to the business. An example here is Affinity Pet Care of Spain, who took over various brands and plants from Mars when they acquired the Royal Canin business some years ago. Part of that was a plant in France concentrating on private label pet foods. Affinity took the decision to focus on their branded portfolio and disposed of the plant business area successfully.

Shortage of resources

In other circumstances, there may be a shortage of resources, either people or cash, to invest in all parts of the business, and then it often makes sense to sell the brand or business area to someone else where the strategic fit is better. Then the capital value can be better invested in the core business areas.

Change of focus

Similarly, a change in direction or focus can create a situation where disposing of a business makes real sense. For example, a pet food importer also sells a range of pet accessories where they have the exclusive rights for their home country. They decide to focus on foods and extend the snack range as they see better long-term opportunities. The accessory business is no longer core to the business and, rather than close it down, they decide to sell the business to another accessory company where they value the exclusive distribution rights.

Buyers

For buyers, M&A deals are the fuel for a company's growth in two particular ways. Firstly, when they strengthen the current core business and secondly, where they provide the means to expand into closely related businesses that reinforce the core.

These deals may enable companies to enter new markets or channels, expand their range into allied areas, enter new product categories or develop the strength and scale of their business, enabling them to become a bigger player, achieving economies of scale and increased profitability.
Buying a company is often also a way to get hold of new technology or production capabilities and capacity, which would otherwise take a long time to achieve or cost too much to do alone. The right acquisition can speed up the process and achieve the goal quicker, cheaper and indeed, better!

M&A should be part of each company's strategic reflections and plans. There are some key strategic evaluations that are necessary to ensure that the right acquisitions or disposals are made and these include:

- clearly articulating the growth aspirations and the company's basis of competitive advantage
- deciding where to invest and also where to divest
- clearly prioritising where growth opportunities exist – organic, M&A, joint ventures/partnerships
- developing an M&A programme with clear objectives for the process and for deals, as well as the frequency, size and timing of deals. ■