

Issue 8
July-September 2011

Consumer Products Deals Quarterly

Deal activity slowing

Analysis of transactions in Q3 2011
in the global consumer products sector



Welcome



Contents

Overview	1
Deal activity slowing	
Volume and value	5
Volume declines, but total and average deal value rise	
Top 10 deals	6
Beverage takes center stage	
Sector focus	12
Value increase driven by food and beverage	
Geographic focus	14
Japan leads surge in Asian deal activity	
Methodology	15
Contacts	16

Welcome to *Consumer Products Deals Quarterly* – a report from Ernst & Young that analyzes acquisitions and disposals in the global consumer products sector.

Many consumer products companies are currently balancing the opportunity provided by healthy cash-rich balance sheets with the risks of making acquisitions in a highly uncertain, and often volatile, market environment. While there are signs that in overall terms the M&A market is slowing down, companies continue to be prepared to grasp the nettle and deploy capital in their pursuit of future growth. In this issue, we examine the key trends driving these transactions, and take a look ahead to consider the likely course of M&A activity over the next few months.

Our analysis, is based on data collected by FactSet Mergerstat and on insight from our global professionals. We hope that this data and the perspectives we offer will be of use to the leaders of consumer products companies and to the financial investors who continue to focus on this sector. We are happy to provide further insight on request.

A handwritten signature in black ink that reads "D. a. Murray." The signature is written in a cursive, slightly slanted style.

David Murray

Global Consumer Products Transactions Leader
dmurray@uk.ey.com

Overview



Deal activity slowing

Deal volumes decreased in the third quarter and the long-term moving average also declined, but activity in Asia Pacific continued to grow. While large strategic transactions are less dependent on the economic cycle, we expect continued economic uncertainty is likely to weigh on the overall pace of deal activity.

Economic uncertainty weighs on M&A activity

In our last issue, we concluded that we would not be surprised if deal volume fell back in the coming quarter, but cautioned against reading too much into the quarter-by-quarter fluctuations in the level of deal activity. Indeed, this quarter's slackening in volume has not been accompanied by a drop in the amount of capital consumer products companies are prepared to commit to M&A.

Nonetheless, the four-quarter moving average of deal volume, which is an indicator of the longer-term trend, did decline in the third quarter, albeit only very slightly. We believe ongoing economic uncertainty and tightening debt markets are having an impact in engendering a more cautious approach among dealmakers. In the three months since our last issue, the Eurozone debt crisis and its potential to tip the global economy back into recession have continued to dominate the business headlines. It is difficult for businesses to feel confident that financial support measures to they will prove sufficient to solve the problem, given the failure of recent bailouts in stemming the crisis. There is also scant comfort to be drawn from the fact that any relief from the headwinds of input cost inflation, particularly commodity prices, is only likely to arrive in circumstances where the global economy is heading once more for recession.

Beverage companies positioning for growth

The quarter's top 10 deals were dominated by beverage transactions, both in the developed world and emerging markets. Analyzing the seven beverage deals alongside the three food sector transactions that made up the balance of the top 10, a number of recurring investment themes become apparent.

Developed market consumer products groups continue to look to M&A activity as a source of growth and are seeking to fill in the "white spaces" in their portfolios, whether those gaps are in developed markets, rapid-growth emerging markets or in new categories. Three aspects of this investment theme were evident from this quarter's top 10 deals:

- ▶ *Extension into new developed markets.* Several companies in the developed world are pursuing scale through extension into new geographic areas in developed markets. Deals that fall into this category this quarter include SABMiller's acquisition of Foster's and Asahi's purchase of New Zealand's Flavoured Beverages Group Holdings Ltd.
- ▶ *Expansion into rapid-growth emerging markets.* Kirin's entry into the Brazilian market through the acquisition of Schincariol, the Brazilian beer and soft drinks producer and Nestlé's purchase of a stake in Hsu Fu Chi, a leading Chinese confectionery manufacturer and distributor, are examples of developed world companies leveraging growth opportunities in emerging markets.
- ▶ *Sharpening portfolio focus.* Companies are looking to make acquisitions to fill gaps and to dispose of non-core assets. Ralcorp's acquisition of Sara Lee's North American private brand refrigerated dough business and its decision to spin off the Post branded cereals business fall under this category.



Emerging market challengers show their growing power

The third quarter provided further examples of the growing economic power of global challengers from emerging markets, which are looking to strengthen their positions both in their domestic markets and through overseas expansion. The theme has several elements illustrated in the quarter's largest deals:

- ▶ *Strengthening positions in domestic distribution networks or supply chains.* The purchase by CJ CheilJedang Corp. of an 18.8% stake in logistics firm Korea Express and China Resources Enterprise's acquisition of department store and supermarket chain Jiangxi Hongkelong fit into this category.
- ▶ *Expansion into developed markets.* Just outside the top 10, the purchase by China's Bright Food Group of a 75% stake in Australian branded food business Manassen Foods illustrated the theme of emerging markets companies moving into the developed world, acquiring western brands in the process.
- ▶ *Generation of economies of scale through consolidation.* This is a well-established trend in mature markets and is gaining ground in emerging markets. Coca-Cola FEMSA's purchase of Grupo CIMSA and the combination of PepsiCo's beverage operations in Mexico with those of GEUSA are two top 10 deals that demonstrate this trend in Mexico's soft drinks bottling market. The purchase by Thai Beverage, Thailand's largest beer and whiskey maker, of local Pepsi bottler Serm Suk from PepsiCo and other shareholders, also fits this theme.

Global consumer products corporate and private equity (PE) transactions scorecard by sector

Deals Announced	3Q11	2Q11	Seq % change	3Q11	3Q10	YoY % change
Corporate deals by subsector						
Beverages	62	58	7%	62	46	35%
Food	158	164	4%	158	161	-2%
HPC	22	39	-44%	22	24	-8%
Tobacco	4	6	-33%	4		
Total	246	267	-8%	246	231	6%

PE deals by subsector (based on seller sector)						
Beverages	10	7	43%	10	11	-9%
Food	28	41	-32%	28	53	-47%
HPC	7	8	-13%	7	5	40%
Tobacco	2			2	1	100%
Total	47	56	-16%	47	70	-33%

Total consumer products (CP) deals by sector, corporate and PE						
Beverages	72	65	11%	72	57	26%
Food	186	205	-9%	186	214	-13%
HPC	29	47	-38%	29	29	0%
Tobacco	6	6	0%	6	1	500%
Total	293	323	-9%	293	301	-3%



Scale no longer paramount?

While the search for scale appears to dominate beverage companies' deal making strategy, the opposite is true in food companies among others are getting smaller.

The Sara Lee/ralcorp transaction is an illustration of the trend for US food companies to split themselves up. At the start of the year, Sara Lee decided to split into a North American food business, focused on meat products, and an international beverage and bakery business, focused on European coffee.

In August, Kraft became the latest major consumer products company to join the trend, announcing that it will split its North American grocery business from its snacks and confectionery business only a year and a half after the takeover of Cadbury, which has yet to be fully integrated.

Activist investor and Kraft shareholder Nelson Peltz viewed the split favorably: "It's in the best interest of shareholders to create a unique consumer products business with very high growth prospects, huge emerging market exposure and one that separates itself from the slow growth, commodity related meat and cheese business."¹

Kraft's decision represents "a stark reversal of philosophy," according to analysts at Janney Capital Markets, who argue that harsh economic fundamentals are driving tough choices at the consumer level, which lead to tough choices for companies as well. Many food companies are, therefore, becoming even more creative to drive their share prices, looking at different ways of unlocking potential shareholder value, including sell-offs and spin-offs, as they accept the reality that each category is different. "We think (Kraft's) action speaks at least as loud as any words on their view of the direction of North American grocery compared with other global alternatives."²

Lateral thinking

The breakup trend is not the only example of lateral thinking in the consumer products industry. Alongside traditional M&A activity, companies will continue to look for other ways to improve earnings and shareholder value without the large balance sheet impact of M&A. These range from joint ventures and alliances to commercial contract arrangements that seek to improve the company's cost position, boost marketing strength and extract synergies.

¹ "Kraft to slice itself in two," *The Guardian*, 4 August 2011.

² "King Kraft announces the Death of scale – what it means for food stocks," *Janney Capital Markets equity research note*, 19 August 2011.

In October, for example, The Hershey Company and Ferrero in North America announced they had set up a joint warehousing, transportation and distribution initiative in the US to improve supply chain efficiency and enhance competitiveness. "Collaborative supply chain operations are a growing trend across industries as companies seek to fully leverage their logistics infrastructure," said John P. Bilbrey, President and Chief Executive Officer of Hershey. "Although we are initially focusing on one region of our business, we are excited about the full potential of this project."³

The Wall Street Journal, meanwhile, reported in October that PepsiCo is close to setting up a joint venture with German dairy company Theo Müller Group to launch a new yogurt brand in the US in an effort to break into the fast-growing yogurt market.⁴ The move would be consistent with PepsiCo's plans to expand in the healthy foods and dairy markets.

Deal activity has peaked, for now

Looking ahead to the end of the year, we expect that the level of deal activity in the fourth quarter of the year will moderate further. From our discussions with clients and observation of the current difficulties in raising finance in the leveraged debt markets, the number of deals with private equity houses as buyers is likely to continue to decrease into the end of the year. Confidence in the private equity sector surged in the second quarter, but this bullish sentiment was undermined by financial market turmoil in August.

Heightened uncertainty arising from the ongoing Eurozone sovereign debt crisis and its potential to tip the global economy into a double-dip recession is likely to weigh on the deal appetite of corporate buyers. Clearly some assets will be under pressure and present buying opportunities for financially robust competitors, but economic uncertainty will engender an even sharper focus on risk

"The question many decision makers will be asking is: Why do the deal if it doesn't have to be done right now?"

David Murray
Global Consumer Products, Transactions Leader

³ "Hershey announces warehouse and distribution alliance," *The Hershey Company*, www.thehersheycompany.com, 5 October 2011.

⁴ "PepsiCo nears JV deal to enter US dairy market for first time," *The Wall Street Journal*, 14 October focused 2011.



management. Due diligence processes will take longer and require higher hurdles to approve deals, increasing the chances that fewer deals will make it over the finish line. The question many decision-makers will be asking is: "Why do the deal if it doesn't have to be done right now?"

We do not expect, however, that deal activity will fall back close to the level reached at the 2009 trough. As we have previously argued, many consumer products companies have regained the capability to do deals. They have improved their working capital positions, reduced their reliance on bank debt and accessed the capital markets, thereby regaining the confidence and capability to put their balance sheets to work in M&A transactions. As well as being financially stronger, by operating in the uncertain economic conditions of the last three years, management teams and shareholders have also become more comfortable doing business with a higher degree of volatility in the business environment. Companies, which are struggling and lack the capital to compete, will become the targets of opportunistic M&A.

It is also important to remember that large strategic and transformational deals are less dependent on the economic cycle and can happen at any time. Economic uncertainty does not preclude megadeals, as companies grasp these rare, large opportunities when market circumstances present them.

"The quarter's activity illustrates the continuing shift in the focus of economic activity from west to east and hence the importance for developed world companies to invest in fast-growth emerging markets. Adding depth to this investment theme, the quarter also provided evidence of the growing strength of emerging market challengers and the appetite of Japanese consumer products groups for overseas deals."

Howard Martin
Global Consumer Products Leader

Data highlights Q3 11

Deal volumes decline

Deal volumes decreased in Q3 11 by 9%, to 293 deals. Volume fell in the HPC and food sectors, was stable at a low level in tobacco, but increased in beverage. Volumes declined in both corporate and private equity transactions.

But in Asia Pacific deal volume and value increase significantly

Q3 11 deal volumes with Asia Pacific as the buyer region increased by 24% to 42 deals and as seller region by 28% to 41 deals. Asia Pacific buyer region Q3 11 deal values totalled US\$7.8b and seller region US\$16.3b, compared with US\$0.7b and US\$0.5b respectively in Q2 11. The US\$16.3b seller region total represents 55% of total Q3 11 deal value.

Total deal value and average deal size both rise

Total disclosed deal value increased by 146%, from US\$12.1b in Q2 11 to US\$29.9b in Q3 11. Even if the SABMiller mega deal is excluded total disclosed deal value rose by 57% to US\$19.1b. The average transaction value for disclosed deals increased from US\$104m in Q2 11 to US\$235m in Q3 11.

The reappearance of the megadeal

There was one megadeal (value greater than US\$5b) in the quarter – the purchase of Foster's by SABMiller for US\$10.8b. This transaction was the first megadeal since the Q1 11 purchase of Danisco by E.I. du Pont de Nemours for US\$6.1b.

Japan active in cross-border trade

The top 10 deals contained two transactions in which Japanese beverage companies (Asahi and Kirin) made significant overseas acquisitions. Japan was the third most active country for corporate deals in Q3 11, with 14 deals, whereas in the second quarter, it did not feature in the top 10 countries.



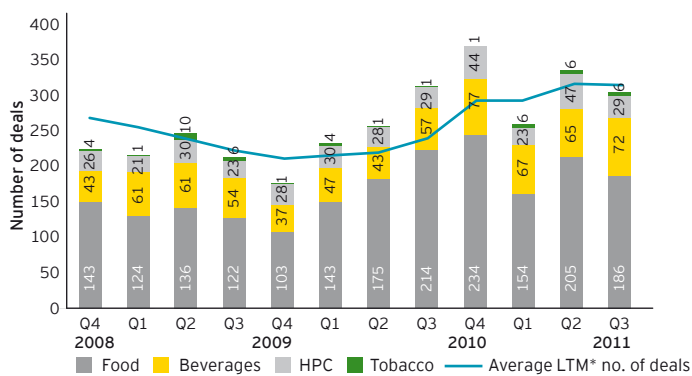
Volume and value

Volume declines, but total and average deal value rise

Deal volumes decreased by 9% (30 deals) in Q3 11 from Q2 11, with activity declining in both the HPC and food sectors. Beverage bucked the trend, recording an 11% increase and providing the quarter's only megadeal, which helped increase Q3 11 total deal disclosed value to US\$29.9b from US\$12.1b in Q2 11.

There were 293 deals in Q3 11, a 9% decrease from the 323 deals in Q2 11. The slackening in the pace of deal activity pulled down the four-period long-term moving average, but only by two deals (to 306 from 308). Both corporate and private equity deal volumes declined during the third quarter.

Deal volumes, Q4 08 to Q3 11



Source: Ernst & Young's analysis of FactSet Mergerstat data from Q4 08 to Q3 11.

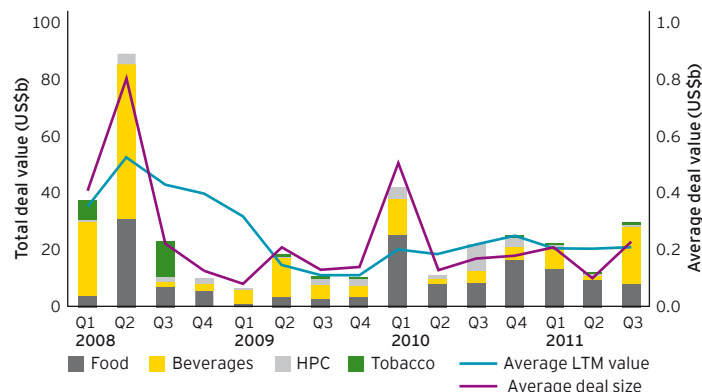
*LTM = Last twelve months

SABMiller megadeal boosts total deal value

SABMiller's purchase of Foster's for US\$10.8b helped push Q3 11 total deal value to US\$29.9b, a 146% increase on Q2 11. However, even if this megadeal is excluded, total disclosed deal value rose from US\$12.1b in Q2 11 (in which there were no megadeals) to US\$19.1b in Q3 11, a 57% increase.

Of the 293 total announced deals, 127 (43%) have disclosed values, compared with 117 of 323 (36%) in Q2 11. Average disclosed deal value also rose, to US\$235m (an increase of 146%).

Disclosed deal values, Q4 08 to Q3 11



Source: Ernst & Young's analysis of FactSet Mergerstat data from Q4 08 to Q3 11.

Top 10 deals

Beverage takes center stage



The top 10 deals in the third quarter were dominated by the beverage sector, which accounted for 7 of the 10 transactions, including the megadeal acquisition of Foster's by SABMiller. Of the others, two deals involved overseas expansion by Japanese brewers and two more represented further consolidation within the Mexican soft drink bottling market. Private equity was notably absent as a buyer in the top 10.

SABMiller swallows Foster's

The third quarter's largest transaction and its only megadeal was the purchase of Foster's by SABMiller in September for US\$10.8b in cash. A takeover had been expected following Foster's demerger earlier this year of its loss-making wine business into a listed group, Treasury Wine Estates.

According to analysts at Investec, the price SABMiller paid was "reasonable" at a 12.6x prospective EV to EBITDA multiple and "comfortably in the range of historical M&A in the sector."⁵ The deal is unusual for SABMiller, which has been more focused on acquisitions in the emerging markets in recent years, but Investec also notes: "In spite of the market clamor around this deal, Foster's would only represent c.16% of the combined group's EV and 8% of group sales. Further, SAB's emerging market sales profile would dilute by just 6% to a still dominant 71%."

While the scope for cost synergies is low, Australia is an attractive high-margin market. Also, as one of the last available developed-world assets, Foster's was likely to prove attractive to established players such as SABMiller, which have grown by acquisition to become global businesses. The Daily Telegraph, meanwhile, highlighted that Graham Mackay, SABMiller chief executive, has been with the brewer for over three decades and "an acquisition of Foster's could well mark his last hurrah before retirement."⁶

But the deal may also have defensive properties. The Financial Times, for example, argued: "It's difficult to see the logic of the bid for Foster's, unless of course it's trying to make itself takeover-proof. Several analysts reckon AB Inbev should buy SABMiller and bring an end to the consolidation of the brewing industry."⁷ Analysts at MF Global, for example, believe that post-acquisition, "ABI buying SAB is materially less likely."⁸

After the end of the quarter, SABMiller also announced an emerging markets transaction, combining its Russian and Ukrainian beer business with Anadolu Efes in return for a 24% stake in the Turkey-based beverage group. The deal creates a strong number two player in the Russian beer market and gives SABMiller an important position in Turkey – Anadolu Efes dominates Turkey's beer market, with 89% volume share.⁹

⁵ "SABMiller," *Investec equity research note*, 22 September 2011.

⁶ "Profile: Graham Mackay looks for legacy sealer in Foster's," *Daily Telegraph*, 21 June 2011.

⁷ "Foster's – the amber nectar?" *www.ft.com/alphaville*, 21 June 2011.

⁸ "Strewth! Foster's Falls," *MF Global equity research note*, 22 September 2011.

⁹ "SABMiller matches Turkey with beer," *Just Drinks*, *www.just-drinks.com*, 19 October 2011.



Top 10 deals Q3 11

Buyer name	Seller name/Unit name	Disclosed value (US\$m)	Announced	Deal type	Sector
SABMiller PLC	Foster's Group Ltd.	\$10,793	21/09/2011	Corporate	Beverages
Kirin Holdings Co. Ltd.	Aleadri-Schinni Participações E Representações SA (Schincariol)	\$2,523	01/08/2011	Corporate	Beverages
Nestle SA	Hsu Fu Chi International Ltd.	\$1,698	11/07/2011	Corporate	Food
Asahi Group Holdings Ltd.	Pacific Equity Partners Pty Led./Unitas Capital Pty Ltd./Flavoured Beverages Group Holdings Ltd.	\$1,260	07/08/2011	Corporate	Beverages
CJ Cheiljedang Corp.	Asiana Airlines, Inc./Daewoo Electronic Components Co., Ltd./Korea Express Co., Ltd.	\$867	08/07/2011	Corporate	Food
Formendo Economic Mexicano SAB de CV (Coca Cola FEMSA)	Grupo Embotelladoras CIMSA SA de CV/ Corporacion de los Ángeles SA de CV	\$834	19/09/2011	Corporate	Beverages
PepsiCo Inc.	Grupo Embotelladoras Unidas/Geusa SA de CV-Beverage	\$625	18/07/2011	Corporate	Beverages
China Resources Enterprises Ltd.	Jiangxi Hongkelong Investment Group Co., Ltd./ Jiangxi Hongkelong Department Store Investment Co., Ltd.	\$573	29/07/2011	Corporate	Beverages
Ralcorp Holdings, Inc.	Sara Lee Corp./North American refrigerated dough business	\$545	09/08/2011	Corporate	Food
Thai Beverage Public Co. Ltd.	PepsiCo, Inc./SS National Logistics Co., Ltd./Serm Suk Public Co. Ltd.	\$513	09/09/2011	Corporate	Beverages

Kirin's Brazilian entry

The second-largest deal in the quarter illustrates the ongoing expansion into faster-growing emerging markets by developed world beverage companies.

Japan's Kirin Holdings announced that it had paid US\$2.5b for Aleadri-Schinni Participações e Representações, which holds a 50.45% stake in Schincariol, the Brazilian beer and soft drinks producer.

The deal is Kirin's first big takeover in Brazil, but press reports note that it follows a pattern in which the Japanese company moves aggressively into big emerging markets where a single takeover can instantly deliver significant market share. Schincariol is Brazil's second-largest beer maker and third-largest producer of soft drinks. "In the beer market there is not such a large number of opportunities available," said Kirin President Senji Miyake. "Globally it wouldn't be a long list, so when this very good investment opportunity came up in Brazil, a large market with high growth potential, we decided to invest."¹⁰

The Japanese beer market is shrinking, under pressure from falling corporate entertainment budgets and stagnant wage growth, while the strength of the yen also makes overseas deals more attractive. But, while the rationale is clear, such opportunities come at a price and analysts expressed the opinion that Kirin had paid a high price. According to Credit Suisse, for example: "The multiple paid is 15.7x EV/EBITDA (trailing last 12 months), which is above the 10 year average of global M&A transactions at 12.5x."¹¹

¹⁰ "Strong yen gives Kirin a taste for Brazilian beer," *The Times*, 3 August 2011.

¹¹ "Global Beer," *Credit Suisse equity research note*, 3 August 2011.



Asahi builds out its Asian network

On a similar theme, Japan's Asahi Group Holdings agreed in August to buy New Zealand's Flavoured Beverages Group Holdings Ltd for US\$1.3b from private equity firms Unitas and Pacific Equity Partners.

Asahi is pursuing a regional expansion strategy. In July, the beverage group bought Permanis, Malaysia's second-largest soft drink maker, for US\$274m and during the quarter also gained regulatory approval for its purchase of the bottled water and juice business of Australia's P&N Beverages.

While currently focusing on building up its network in South East Asia, Asahi also recognizes that it will have to look further afield for growth opportunities.

At a news briefing, Asahi President Naoki Izumiya said: "There is obviously a limit to expansion in Southeast Asia, and Asia as a whole, and if we only do it in Asia, it will not be enough to meet our goals. So our first consideration is seeing what more can be done in China, Asia and Oceania, but after that, we will of course need to make efforts to consider good offers available outside of those areas."¹²

"Faced with a weak domestic market, Japan's large brewers are taking advantage of the strength of the yen to realize their expansion plans through acquisitions in both the developed and emerging markets."

Andrew Cosgrove

Global Consumer Products Lead Analyst

Further consolidation among Mexico's soft drink bottlers

The third quarter provided further evidence of the pursuit of economies of scale through consolidation in the Mexican soft drink bottling market. Coca-Cola FEMSA, a bottling joint venture of Coca-Cola Co. and Mexican drinks group FEMSA (which bought the beverage business of privately owned domestic bottler Grupo Tampico in June), announced the purchase of Corporación de Los Ángeles, SA de CV (Grupo CIMSA) in an all-share transaction worth US\$834m.

Grupo CIMSA, one of the nine family-owned private bottlers remaining in Mexico, operates in territories adjacent to FEMSA's operations, offering the potential for extracting synergies from the combined entity. The deal's valuation is in line with other recent sector transactions. According to Credit Suisse: "In what appears to be a benchmark for Mexican bottlers now, FEMSA is acquiring CIMSA for 10x (current year) EV/EBITDA, slightly above the 9.4x multiple implicit in the Arca Contal transaction and 9.6x in FEMSA-Tampico, with the small premium justified by slightly higher synergies."¹³

Further consolidation in the market is expected. According to JP Morgan, for example: "Coke bottlers' consolidation in Mexico is likely to continue as third generation owners of smaller Coke bottling operations swap their controlling equity stakes for minority positions in a larger bottler. This way they can diversify their risk while remaining as beneficiaries of Coke bottling operations as passive investors."¹⁴

¹² "Asahi buys NZ firm for \$1.3 bln in pre-mixed drinks push," *Reuters*, www.reuters.com, 18 August 2011.

¹³ "Coca-Cola Femsa," *Credit Suisse equity research note*, 19 September 2011.

¹⁴ "Coca-Cola-Femsa," *JP Morgan Latin American equity research*, 19 September 2011.



Rival soft drinks manufacturer PepsiCo also consolidated its bottling operations in Mexico during the third quarter. In a transaction valued at US\$625m, a new joint venture has been created which combines PepsiCo's own beverage manufacturing and distribution operations in Mexico with those of GEUSA, the other Pepsi bottler in Mexico, which is a subsidiary of Grupo Embotelladoras Unidas, SA de CV (GEUPEC). Empresas Polar, PepsiCo's leading Venezuelan bottler, has also been brought in as an equity partner with a 20% stake. GUEPEC will have a 51% stake in the joint venture and PepsiCo 20%. The newly expanded GEUSA will offer a collection of carbonated and non-carbonated drinks, including brands such as Gatorade, Lipton and Pepsi.

According to analysts at Credit Suisse: "The deal will finally create a national bottler that will afford (PepsiCo) one voice, greater speed, a better game plan for soft drinks and jug water as well as new access to talent."¹⁵ Credit Suisse also highlights that GUESA has a differentiated model in Mexico, based on its market-leading jug water business, which delivers product straight into the Mexican home – a model it now hopes to leverage across a wider portfolio of brands.

Local power on display at Serm Suk

Elsewhere in its global bottling empire, PepsiCo appeared as a seller. In September, Thai Beverage, Thailand's largest beer and whiskey maker, agreed to buy Serm Suk, the local bottler of Pepsi beverages, for US\$513m. Thai Beverage has bought PepsiCo's 42% stake for THB58 per share and launched a tender offer for the remaining shares at the same price.

The transaction brings to an end the battle for control of Serm Suk, which started in March 2010 with PepsiCo's hostile tender offer at THB29 per share as part of its strategy to take its bottling operations in-house. Serm Suk rejected that offer as too low, and in October 2010 Somchai Bulsook, the President and Chief Executive of Serm Suk, and his son subsequently sold their combined 20.6% stake to SS National Logistics, a Thai company. In April, Serm Suk and PepsiCo terminated their exclusive bottling agreement, which local news reports attributed as the reason behind the US company's subsequent decision to sell its stake.¹⁶ The deal is interesting as an example of emerging market companies flexing their economic muscles when in competition with the big international consumer products players.

"Emerging markets players, who occupy a successful position in their domestic markets, are broadening their horizons and developing larger regional or even global ambitions."

Emmanuelle Roman
Global Consumer Products Markets Leader

¹⁵ "Global Beverages," *Credit Suisse equity research note*, 19 July 2011.

¹⁶ "Thai Beverage to buy PepsiCo bottler for \$513m," *Intell Asia*, www.intellasia.net, 12 September 2011.



Nestlé's sweet tooth

In July, Nestlé announced that it had agreed to buy a 60% stake in Hsu Fu Chi, a leading Chinese confectionery manufacturer and distributor, from the founding Hsu family for US\$1.7b. The Hsu family will hold the remaining 40% and continue to manage the company in the new partnership. The deal is Nestlé's second in China this year: in April, the Swiss manufacturer bought a 60% stake in Yinlu Food Groups, which makes peanut-flavored drinks and canned rice porridge.

The market received the deal positively. "The valuation at around 14 times earnings may be a bit expensive, but they would be paying for the vast potential," said Jon Cox, an analyst with Kepler Capital Markets.¹⁷ According to data from research group Euromonitor,¹⁸ annual sales in China's confectionery market grew by 63% to more than US\$9.2b from 2005 to 2010.

Access to Hsu Fu Chi's 129 sales offices across China will strengthen Nestlé's distribution capability. "There are very few national brands. Hsu Fu Chi is well established in lower-tier cities. It has brands across China. It's in both modern and traditional channels. It's a good opportunity from that perspective," said Dave Hofman of InterChina Consulting.¹⁹

Alongside the Yinlu acquisition, the Hsu Fu Chi deal is an illustration of Nestlé's push into local brands. In the press statement accompanying the announcement, Paul Bulcke, chief executive of Nestlé, said the deal: "Demonstrates our long-term commitment to China and enhances our ability to grow our portfolio of international and local brands in this dynamic market." Hsu Fu Chi's product portfolio includes, for example, cucumber and sweet-onion flavored confectionery.

"The stake in Hsu Fu Chi will further broaden Nestlé's reach within the fast-growing Chinese market."

Mike Sills
Global Co-Leader, Food

¹⁷ "Nestle potential China buy looks sweet," *Dow Jones International*, 4 July 2011.

¹⁸ "Nestlé shows taste for Chinese treats," *The Wall Street Journal*, 12 July 2011.

¹⁹ "BRICs and beyond: Hsu Fu Chi could sweeten Nestle's Chinese business," *Just food*, www.just-food.com, 9 July 2011.



Show me the dough

Ralcorp Holdings, the US private label food group, in August announced that it had purchased Sara Lee's North American private brand refrigerated dough business for US\$545m. For Ralcorp, the deal represents part of its strategy to increase its focus on private label, having announced in July plans to spin off its Post branded cereals business. For Sara Lee, the transaction follows its decision at the start of the year to split into two publicly traded companies (see overview for more detail).

According to Robert Moskow, equity analyst at Credit Suisse, Ralcorp's acquisition is logical. "This is a good retail business with 70% market share of private label dough. ... We have always thought that this business made more sense in Ralcorp's portfolio than in Sara Lee's, and we believe that Ralcorp paid a reasonable price for it through auction (8.0x EBITDA, or 6.5x EBITDA including the present value of a US\$100m tax benefit)."²⁰

The planned spin-off of Post and the dough acquisition also need to be seen in the context of Ralcorp's defense against a hostile bid from ConAgra. In September, ConAgra dropped its bid, which had already been raised to US\$94 per share from an initial US\$82, because Ralcorp would not enter negotiations. Some analysts have been critical of Ralcorp's decision. According to the Financial Times Lex Column, for example: "With some analysts reckoning ConAgra might have gone as high as US\$104, management has to boost the share price by 35% before investors break even in terms of value creation. That is an awfully high hurdle, and the one idea Ralcorp came up with to bridge the gap – spinning off or selling the Post cereal business it bought just three years ago from Kraft Foods – is unlikely to do the trick."²¹

Capturing more of the value chain

The third quarter top 10 deals provided two examples of emerging market consumer products conglomerates making non-consumer product acquisitions aimed at strengthening their position in local distribution networks or supply chains.

In July, CJ CheilJedang Corp., a food and beverage manufacturing affiliate of South Korea's CJ Group, acquired an 18.8% stake in logistics firm Korea Express for US\$867m. This represents one half of a 37.6% stake being sold by Asiana Airlines and Daewoo Engineering and Construction. CJ GLS, an unlisted logistics unit of CJ Group, bought the other half, bringing the total deal value to US\$1.75b. Analysts, however, expressed concern at the deal's price: "Investors think the bid price is too high," said Judy Kim at Woori Investment and Securities.²²

Also in July, beverage, food and retailing conglomerate China Resources Enterprise Ltd. (CRE) announced it had agreed to buy department store and supermarket chain Jiangxi Hongkelong Department Store Investment Co. for US\$573m in order to expand its retail division. CRE produces China's leading beer brand, Snow, in joint venture with SABMiller and is the country's biggest supermarket operator. The deal will help CRE penetrate Jiangxi province where it does not currently have a presence, and analysts at Goldman Sachs said the deal is consistent with the company's strategy that "emphasizes regional leadership and penetrates the markets by multi-format stores."²³

"It is very hard to run a business successfully that is a mix of branded and private label products. The former needs a focus on marketing and building pricing power, the latter a ruthless focus on lowest cost everywhere."

John Rothenberg

Chair of the Ernst & Young European Corporate Development Leaders' Network and former Head of M&A at Unilever

²⁰ "Weak earnings quality, but a good acquisition," *Credit Suisse equity research note*, 10 August 2011.

²¹ "Ralcorp/Conagra: rich offer spurned," *The Financial Times*, www.ft.com/lex, 20 September 2011.

²² "CJ shares down after Korea Express bidder selection," *Dow Jones Newswires*, 29 June 2011.

²³ "Market Talk: CRE +3.4%, On expansion track," *Dow Jones Newswires*, 1 August 2011.



Sector focus

Value increase driven by food and beverage

HPC and food volumes fell during the third quarter, while tobacco activity was stable at low levels. Only beverage activity rose. Value, however, was higher across the board, most markedly in beverage and food, which accounted for all of the top 10 deals.

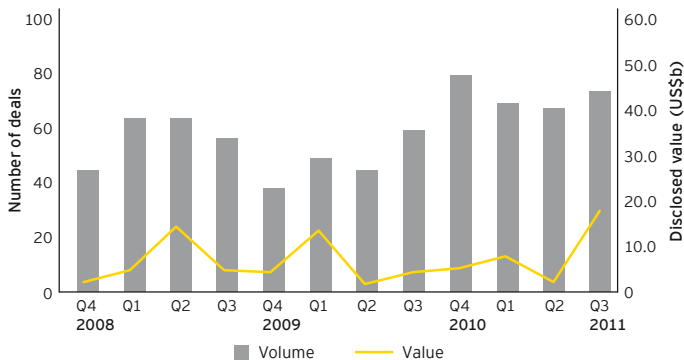
Beverage

Deal volumes in the beverage sector in Q3 11 increased by 11% to 72 deals from 65 in Q2 11. Total disclosed deal value rose sharply to US\$19.8b in the quarter, pulled higher by the presence of seven beverage transactions in the top 10 deals, including one megadeal of US\$10.8b. By comparison, in Q2 11 the largest beverage deal was only US\$0.8b – Mexico's Coca-Cola FEMSA acquisition of the La Puraza operations of Grupo Tampico.

Food

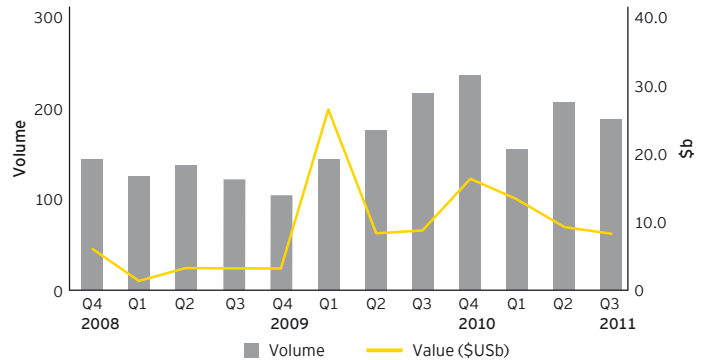
There were 186 food transactions in the period, with a total disclosed deal value of US\$8.4b, a decrease of US\$0.9b (10%) over the prior quarter. Total deal value was bolstered by the fact that 3 of the top 10 deals were in the food sector. The food sector was once again the largest sector in terms of deal volume, despite a 9% decline from Q2 11.

Volume and value of beverage deals, Q4 08 to Q3 11



Source: Ernst & Young's analysis of FactSet Mergerstat data from Q4 08 to Q3 11.

Volume and value of food deals, Q4 08 to Q3 11



Source: Ernst & Young's analysis of FactSet Mergerstat data from Q4 08 to Q3 11.



HPC

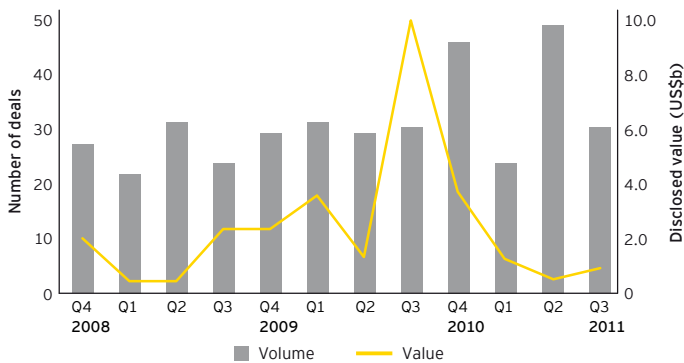
The number of HPC deals decreased by 18, to 29 deals (a 38% decline). The total disclosed transaction value, however, increased slightly, by US\$0.5b, to US\$0.9b in the quarter. The top 10 deals have not contained an HPC deal in either Q3 11 or Q2 11, and the largest HPC deal in the third quarter was the US\$315m acquisition of Attends Healthcare, a maker of incontinence undergarments, by Canadian paper producer Domtar.

After the end of the quarter, however, Unilever announced in October that it had agreed to buy 82% of Russian skincare maker, Kalina for US\$540m as part of its focus on emerging market growth.

Tobacco

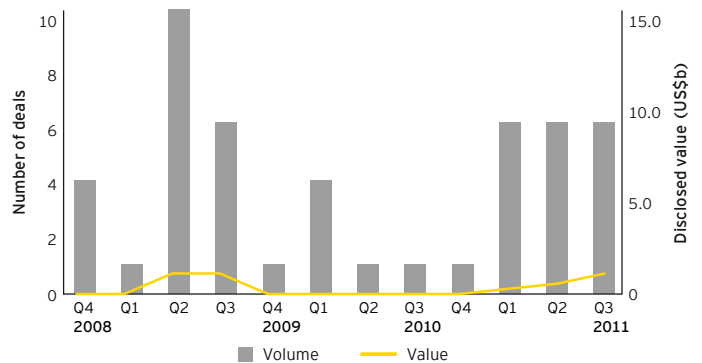
There were six tobacco deals in the quarter, the same number as Q2 11, with a disclosed transaction value of US\$0.8b. The largest disclosed deal value was Japan Tobacco's US\$450m acquisition of Haggar Cigarette and Tobacco Factory Ltd., which controls 80% of the market in Sudan.

Volume and value of HPC deals, Q4 08 to Q3 11



Source: Ernst & Young's analysis of FactSet Mergerstat data from Q4 08 to Q3 11.

Volume and value of tobacco deals, Q4 08 to Q3 11



Source: Ernst & Young's analysis of FactSet Mergerstat data from Q4 08 to Q3 11.

Geographic focus



Japan leads surge in Asian deal activity

There were 133 cross-border deals in Q3 11, an increase of 10 deals (8%) compared with Q2 11, in contrast to the 9% fall in total deal volume. Asia-Pacific cross-border deal activity increased markedly in volume and value terms, both as buyer and seller.

One of the third quarter's clearest geographic themes is the increase in cross-border buying activity in Asia Pacific, despite a decrease in the overall volume of deal activity.

Q3 11 deal volumes with Asia Pacific as the buyer region increased by 24% to 42 deals and as seller region by 28% to 41 deals. Compared with the same period a year ago these deal volumes were 68% and 41% higher respectively.

Asia Pacific buyer region Q3 11 deal values totalled US\$7.8b and seller region US\$16.3b, compared with US\$0.7b and US\$0.5b respectively in Q2 11. The US\$16.3b seller region total represents 55% of total Q3 11 deal value.

The top 10 deals contained two transactions in which Japanese beverage companies (Asahi and Kirin) made significant overseas acquisitions. More broadly, Japan was the third most active country for corporate deals in Q3 11 with 14 deals, whereas in the second quarter it did not feature in the top 10 most active nations. (The US was most active in Q3 11 with 33 deals, and China second with 16).

This activity looks set to continue, as it is underpinned both by the weakness of the Japanese domestic market and the strength of the yen. The former clearly points to the need to look abroad for new sources of growth, while a strong currency makes overseas purchases more attractive financially.

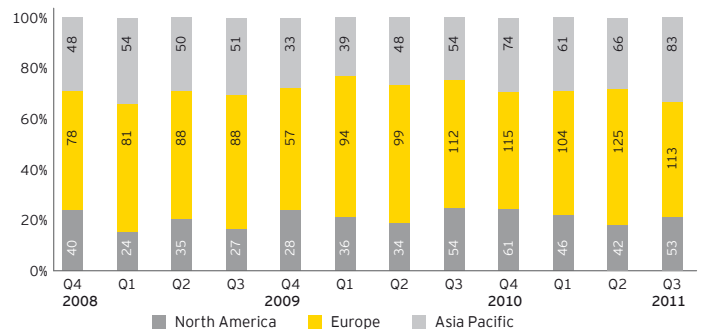
From our client relationships, we are aware of a number of Japanese food sector groups, which are actively looking to do deals in Europe in the coming months. Press reports in October, meanwhile, speculated that Danone, which owns the Volvic and Evian brands, has held talks with Japan's Suntory regarding a sale of its bottled water assets. It is unclear whether Suntory would buy Danone's water assets in Asia or the entire business.²⁴

In volume terms Asia Pacific/cross border activity increased by 24% (buyer region) and 28% (seller region). Europe once again,

however, dominated the cross border deals in terms of volume in Q3 11, both as the buyer and seller.

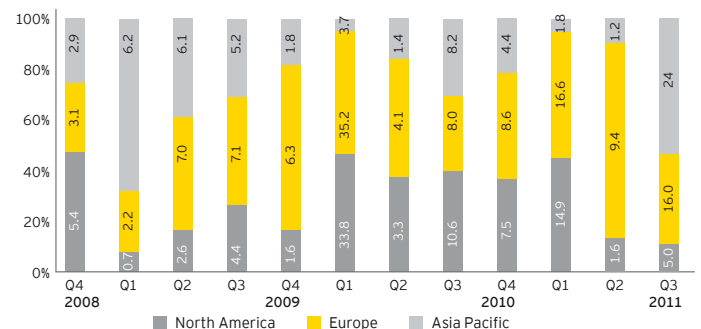
In Q3 11, 66 of the 133 cross-border deals had a disclosed value (50%), while in Q2 11, only 48 of the total 123 cross-border deals had a disclosed value (39%). As a result, the increase in total value is in part attributable to increased information in the quarter.

Regional volume comparisons, Q4 08 to Q3 11



Source: Ernst & Young's analysis of FactSet Mergerstat data from Q4 08 to Q3 11.

Regional value comparisons (US\$b), Q4 08 to Q3 11



Source: Ernst & Young's analysis of FactSet Mergerstat data from Q4 08 to Q3 11.

²⁴ "Danone said to be in talks to sell bottled water assets to Japan's Suntory," *Just Drinks*, www.just-drinks.com, 18 October 2011.



Methodology

Data source and industry scope

Consumer Products Deals Quarterly is based on Ernst & Young's analysis of FactSet Mergerstat data from Q4 08 to Q3 11. Data was pulled from the FactSet Mergerstat database using standard industrial classification codes.

For the purposes of this publication, our definition of consumer products is only those companies in the food, beverages, tobacco and HPC subsectors.

Deal activity and valuations may fluctuate slightly based on the date that the FactSet Mergerstat database is accessed.

In January 2011 we reorganized the data set so that it can be segmented globally into four regions (Europe, Asia Pacific, Middle East and Africa, and the Americas). All data in the charts from previous quarters reflects this reclassification.

Qualifying deals

- ▶ Deals include transactions between companies in the four consumer products subsectors; consumer products companies acquiring businesses in other subsectors; and non-consumer products companies acquiring consumer products companies.
- ▶ PE deal activity includes both full- and partial-stake transactions and was analyzed based on acquisitions by firms classified as PE, alternative investment management groups, certain commercial banks, investment banks, venture capital and other similar entities.
- ▶ For non-consumer products acquirers, deals were classified based on the consumer products sector of the seller.
- ▶ Equity investments were included (corporate and PE).
- ▶ Joint ventures were not included.
- ▶ The value and status of all deals highlighted in this report are as of 30 September 2011.
- ▶ All dollar amounts are in US\$ unless otherwise indicated.
- ▶ There is no minimum US\$ deal threshold.
- ▶ Only disclosed deal values (as per FactSet Mergerstat) are used in all value analyses.
- ▶ As used in this report, "total value" refers to the aggregate value of deals with disclosed values for the period under discussion.

Contacts



Region	Contact	Email/telephone
Global/EMEIA	David Murray Global Consumer Products Transactions Leader	dmurray@uk.ey.com +44 (0) 158 264 3248
Asia Pacific	John Hope Transaction Advisory Services Leader	john.hope@hk.ey.com +852 2846 9997
Americas	Gregory J. Stemler Consumer Products Transactions Leader	gregory.stemler@ey.com +1 312 879 3351
Latin America	Jeremy Barnes Transaction Advisory Services	jeremy.barnes@br.ey.com +55 11 3055 0115
Country	Contact	Email/telephone
Brazil	Alfredo Della Savia Consumer Products Leader	alfredo.dellasavia@br.ey.com +55 11 2573 3788
Russia	Dmitry Khalilov Retail and Consumer Products Leader	dmitry.khalilov@ru.ey.com +7 495 755 9757
India	Ajay Arora Transaction Advisory Services	ajay.arora@in.ey.com +91 124 464 4000
China	Robert Partridge Transaction Advisory Services Leader	robert.partridge@hk.ey.com +852 2846 9973
Sector	Contact	Email/telephone
Global	Howard Martin Global Consumer Products Leader	hmartin@uk.ey.com +44 (0) 20 7951 4072
Global	Emmanuelle Roman Global Consumer Products Market Leader	eroman@uk.ey.com +44 (0) 20 7951 1651
Global	Andrew Cosgrove Global Consumer Products Lead Analyst	acosgrove@uk.ey.com +44 (0) 20 7951 5541
Beverages	Steve Wills Global Leader	swills@uk.ey.com +44 (0) 20 7951 1336
Food	Patricia Novosel Global Co-Leader	patricia.novosel@ey.com +1 31 2879 6715
Food	Mike Sills Global Co-Leader	mike.sills@ch.ey.com +41 58 286 5538
HPC	Anastasia Economos Global Co-Leader	anastasia.economos@ey.com +1 201 750 0919
HPC	Mark Twine Global Co-Leader	mtwine@uk.ey.com +44 (0) 20 7951 0735
Tobacco	Ed Hudson Global Leader	ehudson@uk.ey.com +44 (0) 20 7951 4816

About Ernst & Young

Ernst & Young is a global leader in assurance, tax, transaction and advisory services. Worldwide, our 152,000 people are united by our shared values and an unwavering commitment to quality. We make a difference by helping our people, our clients and our wider communities achieve their potential.

Ernst & Young refers to the global organization of member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. For more information about our organization, please visit www.ey.com.

How Ernst & Young's Global Consumer Products Center can help your business

The global recession has reset the consumer products landscape. Value-seeking consumers, intensified competition, increased commodity costs, and growth opportunities in emerging markets are driving change. Consumer products companies now need to be leaner and more agile, with a relentless focus on execution. If you lead a consumer products business, you need to anticipate trends, identify implications and make informed decisions that support your business goals. Our Global Consumer Products Center enables our worldwide network of over 13,000 industry-focused assurance, tax, transaction and advisory professionals to share powerful insights and deep sector knowledge with businesses like yours. This intelligence, combined with our technical experience, can help you accelerate and improve your execution. We can help you to realize the full value of your transactions, improve customer and brand profitability, drive down costs and build an agile and resilient supply chain. If you want to compete powerfully in your market, we'll help you achieve your potential today and tomorrow.

© 2012 EYGM Limited.
All Rights Reserved.

EYG no. EN0329



In line with Ernst & Young's commitment to minimize its impact on the environment, this document has been printed on paper with a high recycled content.

This publication contains information in summary form and is therefore intended for general guidance only. It is not intended to be a substitute for detailed research or the exercise of professional judgment. Neither EYGM Limited nor any other member of the global Ernst & Young organization can accept any responsibility for loss occasioned to any person acting or refraining from action as a result of any material in this publication. On any specific matter, reference should be made to the appropriate advisor.

ED None

1145794.indd (UK) 03/12. Creative Services Group.