William Blair

# Private Label Growth Trends Drive Increased M&A Interest

## On the heels of the Private Label Manufacturers Association's annual trade show, we examine the opportunities for increased penetration for private-label goods.

## Industry Commentary


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The private label industry continues to enjoy a strong financial outlook, driven by growth opportunities in the U.S. market and increasingly positive consumer sentiment toward private-label products. According to an investor presentation from TreeHouse Foods, private label saw 24.6% growth between 2009 and 2014. As the industry evolves, private-label companies are looking to build on those gains by expanding into premium categories and increasing the diversity and quality of their product offerings.

At the PLMA's 2016 Private Label Trade Show at the Rosemont Convention Center in Chicago, industry insiders got a taste of the future of private label and a look at how these companies are positioning themselves to take advantage of changing economic conditions. The November 13-15 event featured exhibits from more than 1,300 companies, ranging from small and midsize companies to well-known national brand makers that also supply store brands. At the conference, we met with leading executives and investors from across the industry to discuss some of these recent trends.

**Expansion Opportunities in the United States**

Private-label products have traditionally offered excellent value to consumers in a variety of categories; IRI estimates that U.S. shoppers could save $44 billion per year buying only private-label products over national brands. In addition, private-label brands are increasingly viewed by retailers as a profit driver and point of differentiation, because they require lower inventory investment and achieve a turnover rate that is generally on par with that of name brands.

Growth in the private label industry surged during the last recession as consumers looked to maximize purchasing power. While growth eventually plateaued during 2014 and 2015, private label's ability to maintain market share as the economy improved is a reflection of consumers' positive attitudes toward private-label products. According to IRI, more than 80% of consumers today believe that private-label goods offer as good as or better quality than their name-brand counterparts.

In the United States, private-label dollar sales reached $123 billion in

2015, according to IRI. That record-high total, however, represents a value market share of only 16.4%—far lower than overall totals in Europe, which saw private label penetration achieve a value market share of 38.3% in 2015. Based on these figures, it is clear that there is substantial room for additional penetration in U.S. markets.

**Moving Into New Premium, Specialty Categories**

The private label category has traditionally been focused on commodity categories that feature little product differentiation, high price sensitivity, high purchase frequency, and limited innovation. Going forward, the category will evolve to include more innovative premium and specialty categories that retailers and their consumers are demanding.

Consumer demand has shifted toward healthier brands, a movement that is being driven largely by the Millennial generation. According to William Blair equity research analyst Jon Anderson, Millennials are significantly more concerned with health and wellness in their purchasing decisions than prior generations. According to IRI, big-box retailers such as Walmart and Target and specialty grocers such as Whole Foods are finding success creating multiple private-label brands targeting specific consumer needs such as organic, gluten-free, clean label, all natural, low-cal, or preservative-free. Expansion into premium products and specialty categories beyond the traditional private-label categories will continue to drive growth in the industry.

**Expanding Private Label-Only Retail Formats**

Retailers looking to trade on private label value, such as Aldi and Trader Joe's, are continuing to expand their footprints in the United States. Aldi is in the midst of a five-year plan that will result in the opening of 650 new stores across the United States by 2018. This will bring Aldi's U.S. presence to approximately 2,000 stores, or roughly 44% the number of Walmart stores, according to *The Wall Street Journal*. Meanwhile, Lidl, which like Aldi is based in Germany and focuses on carrying private-label products, plans to open its first U.S. stores by 2018.

While stores such as Aldi and Lidl are viewed primarily as low-cost alternatives for shoppers looking for more basic products, grocery chains

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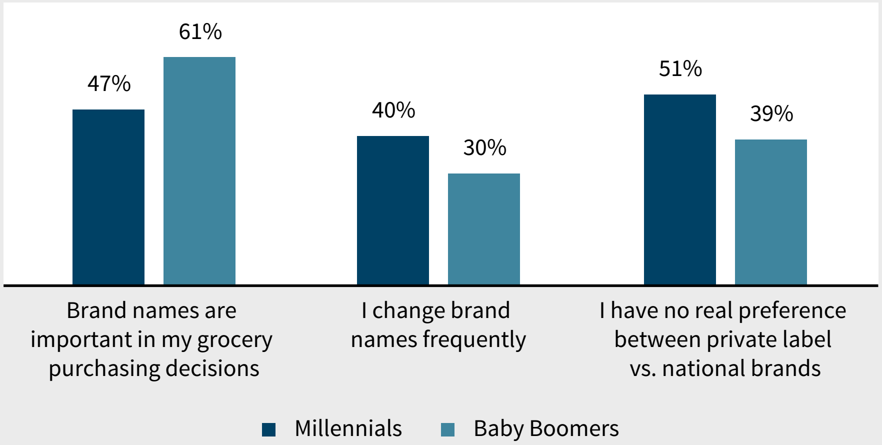
**Millennials Are Brand Agnostic**

Millennials will be responsible for the bulk of consumer purchasing decisions over the next decade, and they are more receptive to private-label products than baby boomers.




Source: TreeHouse Foods Investor Presentation that offer natural, organic, and other premium private-label products are seeing ample growth opportunities, as well. Trader Joe's, which is owned by Aldi, now has approximately 500 stores in the United States and was ranked as the No. 1 grocery store in the United States for customer loyalty each year from 2012 to 2015, according to surveys conducted by Market Force Information. Whole Foods continues to expand its private-label-only 365 by Whole Foods concept, which features lower prices on the natural and organic products consumers have come to expect from the parent store. Whole Foods recently announced the expansion of its 365 by Whole Foods stores to new locations in California and Virginia, with 19 more locations currently in development.

**M&A Perspective**

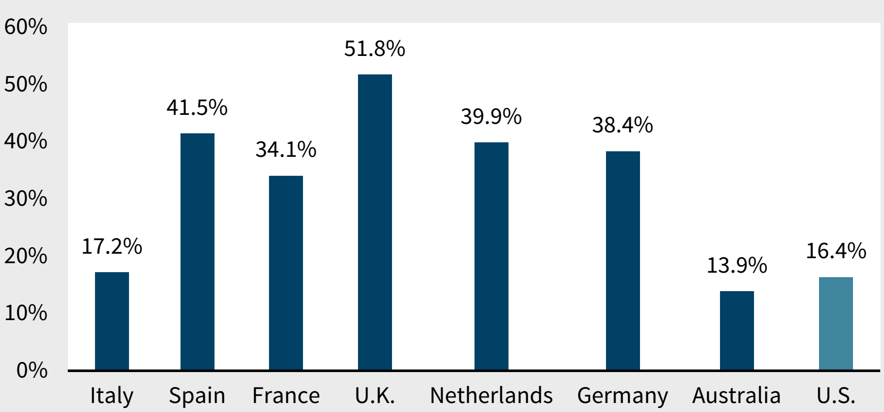
Despite leveling off during the past few years, the growth of the private label industry has significantly outpaced growth in the broader food and beverage industry over the last decade. The growth of the food and beverage industry as a whole generally mirrors GDP growth rates, so the opportunities for private label to increase market share in the United States and expand into additional product categories and tiers are very attractive to strategic buyers.

As a result, companies across the food and beverage industry have become increasingly aggressive in their pursuit of leading private-label companies. This M&A activity has been occurring across product categories and across the private-label production chain. Since 2014, William Blair has completed several sell-side transactions that illustrate the growing interest from strategic acquirers in private label. William Blair's recent work in this space includes serving as sell-side advisor to Sunrise Growers, the leading private-label frozen fruit producer, on its October 2015 acquisition by SunOpta for $450 million. William Blair also managed the sales of other highly strategic private-label businesses, such as American Blanching Company's sale to Post; Baptista's Bakery's acquisition by Snyder's-Lance; Protenergy Natural Foods' sale to TreeHouse Foods; and Lettieri's sale to Greencore.

Given the continued penetration of private label and the meaningful white space opportunities for additional penetration in U.S. markets, we expect continued M&A interest in this space. If you have questions about these or other trends affecting the private label industry, please do not hesitate to contact us.

**Private Label Market Share, 2015**

Private label has greater market penetration in many European countries than it has in the United States, leaving ample opportunity for growth in the domestic market.




Source: IRI Private Label Report