

In focus

What to consider when
acquiring or investing
in a food business
or product



When buying or investing in a food business, brand or ingredient, there is the need for due diligence, market insight, and regulatory and scientific support.



The food industry has always provided fertile ground for investors. The multiplicity of investment opportunities in food and beverage from individual brands and concepts to food focussed retail, wholesale, catering or online businesses offers infinite scope. In 2017, the global food and drink market was estimated to be worth over \$5650 billion, with growth over the last four years seen particularly in Asian markets.

Unsurprisingly the US was ranked the largest food and beverage market in the world in 2016 and is predicted to remain in that position until 2026, followed by China in second place, then India and the UK¹. The agri-food sector in the UK contributed £121 billion (6.7%) to national gross value added in 2017².

The size and scale of food and drink related businesses range from global conglomerates to tiny start-ups; the latter often prove appealing as they provide potential for rapid growth and return on investment by operating in an agile, innovative and disruptive way through having a closer, often more direct relationship with consumers.

For many investors, now is an unprecedented and exciting time to be entering this space. Fuelling the market are highly skilled entrepreneurs bringing edgy, innovative products to market swiftly. These factors converge to produce maximum disruption

and agitation. Strong consumer interest in challenger brands who meet the healthier eating and drinking aspirations of millennials, has caused a surge in investment interest in these brands. This is because they are perceived as being more agile to meet the discerning wants and needs of a digitally native younger generation, standing in stark contrast to many established brands who have been slower to respond to rapidly evolving and burgeoning consumer demands.



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¹ Cushman and Wakefield (2017) The Global Food & Beverage Market.

² <https://www.gov.uk/government/publications/food-statistics-pocketbook/food-statistics-in-your-pocket-summary>

The importance of market insight

Making the right FMCG investment choice - be it a brand, business or product itself - requires research; not only product analysis and segmentation but also consumer trends. Investing in a declining or stagnant sector may appear to be risky but equally could result in better returns than investing in a growing sector that is already saturated.

Consumer demand is currently driving several mega trends including sugar and alcohol reduction, gut health, 'free-from', natural products, healthy ageing, and weight and energy management. Understanding these trends and gaining insight into current and predicted future consumer preferences, is vital when contemplating both the nature and size of a potential FMCG investment. Qualifying and quantifying the sustainability factors of the trend, and ebb and flow of consumer attitudes to it; investigating the interrelationships between food trend and financial considerations of consumers are key: What does the competitor landscape look like? What are the market drivers? What is the longevity of the trend and who/what is driving it? Human insights are featuring evermore prevalently in dictating which way food trends will go in a way that has not been seen previously.

Due diligence in food and beverage investments

When evaluating the potential for a food and beverage investment, everything from the management and leadership capabilities of those involved to the scalability and quality controls embedded in the supply chain should be subject to scrutiny. Barriers to entry such as intellectual property are also commonly overlooked considerations. Whilst these may seem like classic investment due diligence considerations, engaging at an early stage of the investment lifecycle can also enable the discovery of new categories driving new trends before they hit food and beverage retail data radar. More broadly there is benefit in looking to identify products that fall within larger macro trends such as food on the go, healthy snacking or products with functional benefits.

In addition to fiscal and governance due diligence, understanding the compliance history of a Food Business Operator (FBO) is essential in evaluating the sanity of any potential investment. Simply assuming the compliance position of a product, brand or business within the supply chain is sound, could be disastrous. Compliance considerations associated with food safety, quality and food labelling and standards requirements form the baseline but may prove difficult to navigate for a potential investor unfamiliar with how the food and beverage compliance landscape works. Focussing on not just existing market compliance but also aspirational markets for a potential product or brand investment need to be thought through- just because a commodity is compliant in one market doesn't mean it will be in another.



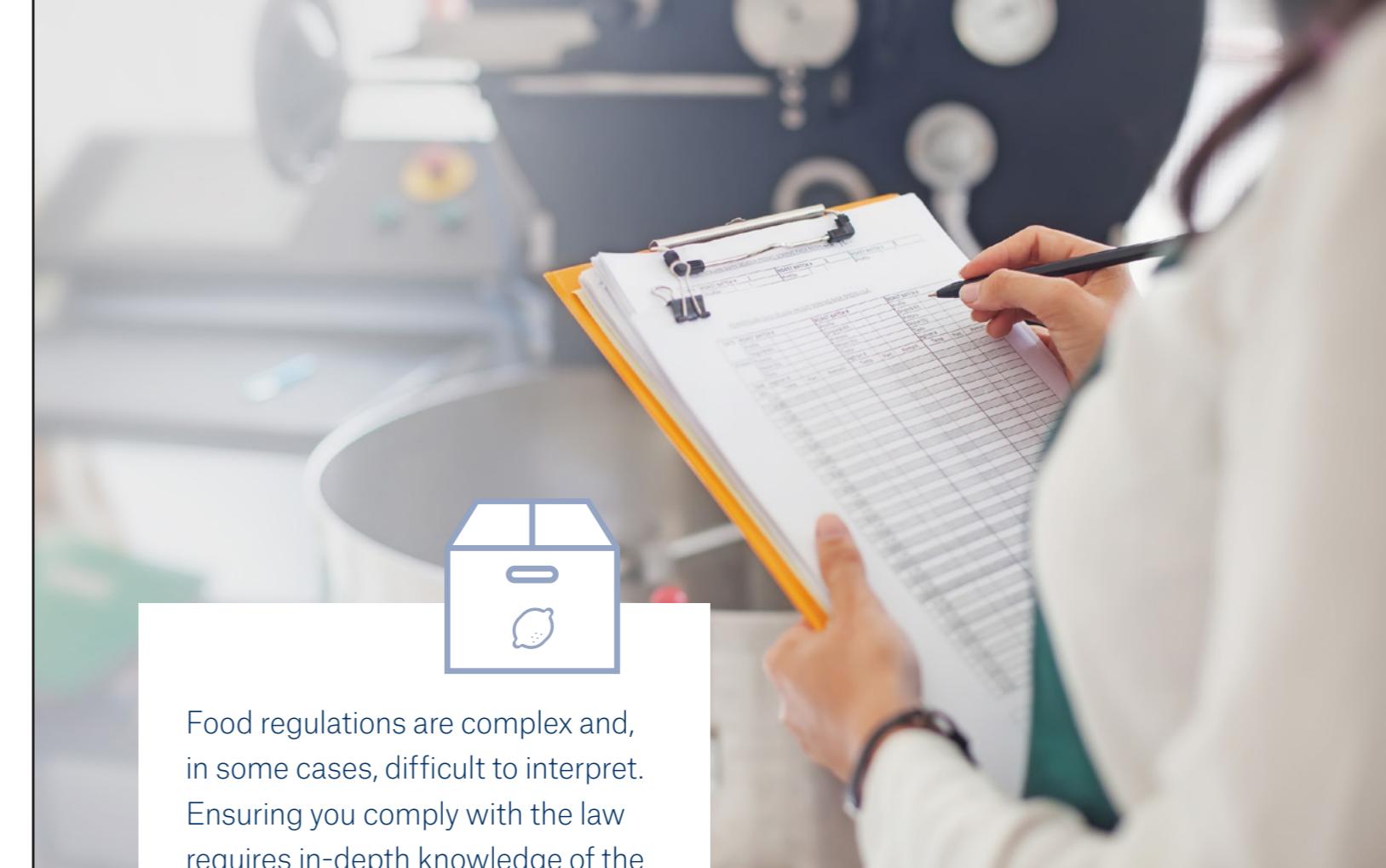
Food regulations are complex and, in some cases, difficult to interpret. Ensuring you comply with the law requires in-depth knowledge of the legislation, in all markets in which you are producing, exporting or importing foods.

FBOs at all stages of production, processing and distribution within the business under their control, are responsible for meeting the requirements of relevant food law. The due diligence defence forms the foundation of food safety law in the EU and the UK; in general terms this means that a person must prove that they took all reasonable precautions and exercised due diligence to avoid the commission of an offence by themselves or by a person under their control. The maximum punishment for offences under the General Food Regulations in the UK are an unlimited fine and/or two years custodial sentence for the responsible individual.

Food must be safe, not fraudulent or adulterated, and food information must be accurate and not misleading to the consumer. For example, any

marketing claims made on food labels, online and in advertising must meet strict rules to inform the consumer on their purchase. This is particularly important where consumer safety may be compromised as a result of omission, false or inaccurate information.

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Approaches to informed investment

As with any major investment, financial due diligence will loom large in the mind of any potential investor. However, whilst fiscal governance issues surrounding any business acquisition will be front and centre of an investors mind, integrating a business risk profiling strategy that incorporates intrinsic assessment of the compliance of a potential acquisition or investment in food and beverage is essential.

A risk analysis is recommended to determine if the business, product(s) or processes are compliant with relevant food law in all of the markets in which an investment is being considered and that the foods produced are safe and genuine. This should include auditing of the business from a food safety and legislative perspective, incorporating a site visit, as well as liaising with the relevant enforcing authorities to understand their attitudes to the compliance of the target business and the permissibility of the products of interest.

The permissibility of products in the target markets should also be considered. Often new products or ingredients are considered novel and require a lengthy approval process. For example, cannabidiol which is currently trending very heavily in food and beverage in multiple markets, is considered a novel food in the EU. Companies wishing to use this ingredient must submit a dossier to the European Commission, including review of microbiological, chemical, physical and toxicological risks associated with the product and its processing, to demonstrate safety for the end consumer. Approval, which is not guaranteed, can take several years, during which time the product cannot be sold.

Patent searches may also be necessary; being informed of the potential hurdles should help you protect your investments.

Making a success of your investment

The success of a food business or product and therefore profits, depends largely on the consumer drive to purchase. Consumer insights driving intelligent marketing is key here; understanding consumer opinion and benchmarking products against those of competitors can help position your product optimally in the marketplace, including price point and packaging.

Maintaining these profits requires brand protection. It goes without saying that the safety of consumers is paramount, however a food safety breach can also be extremely costly to a brand, particularly if it involves withdrawing or recalling products from the market. Safety of products can be compromised through numerous mechanisms including pathogenic bacteria or their by-products, harmful chemicals, allergens, and physical hazards. Food fraud can similarly cause brand damage; the horse meat scandal caused sales of red meat to slide by ~8,000 tonnes in the UK in 2013³, and one retailer's stock value to fall by £300 million⁴.

Therefore, ensuring product safety, authenticity and quality not only satisfies legislative requirements, but also minimises the risk of customer complaints and harmful media coverage which can damage a business. Food safety and fraud need to be managed via a robust quality system, which covers all stages of production, from raw ingredients, supply chain, manufacture, packing and distribution. Implementation and maintenance of this quality system should be a primary concern of any food business.

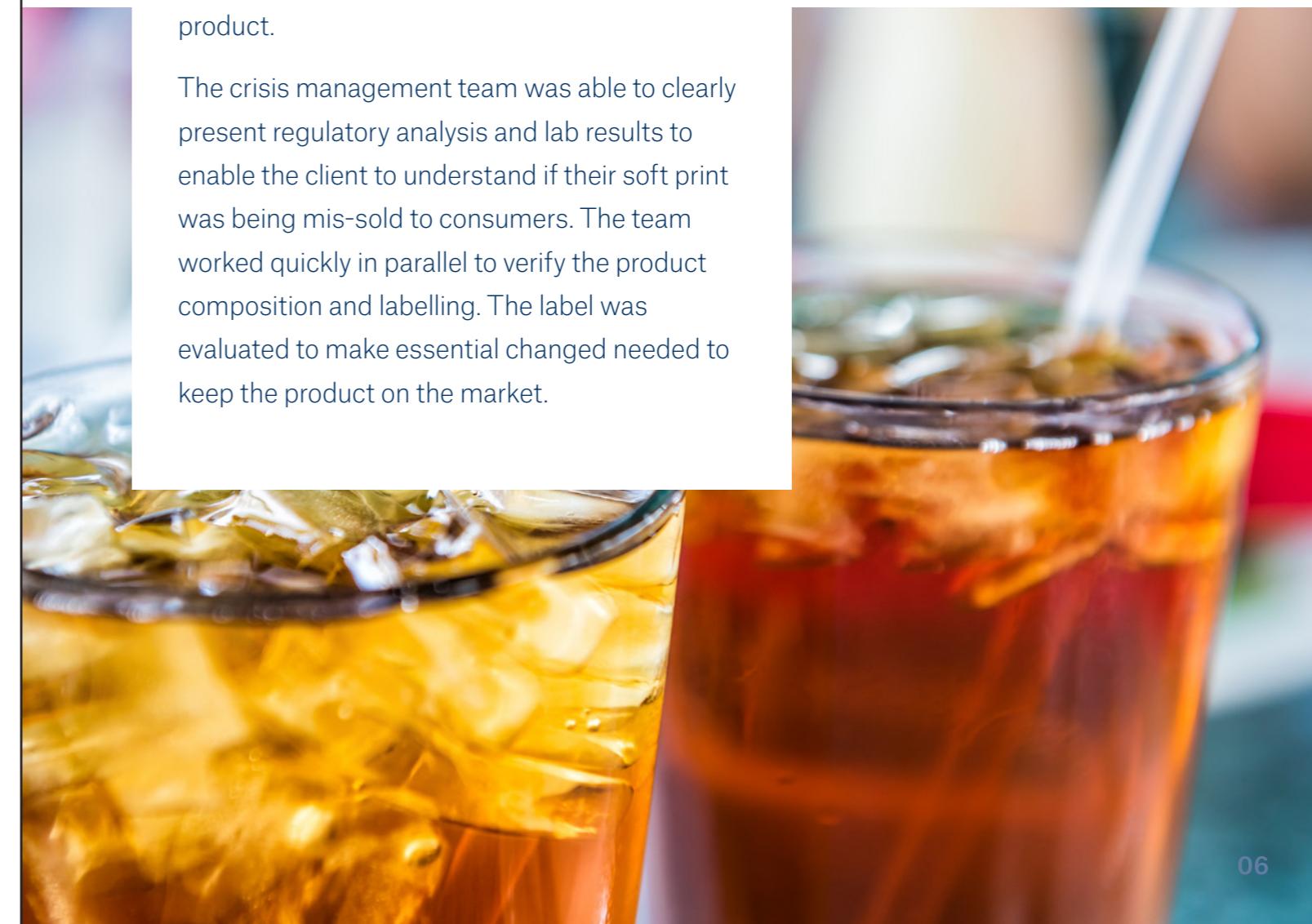
Conclusion

Doing your homework can prevent bad investments in the food industry; which means being armed with specialist knowledge, both from a regulatory and technical standpoint. If sufficient in-house expertise is not available, advice should be sought from external consultants, both pre-investment and on an ongoing basis to protect yourself, your brand and consumers.

Helping an investor in crisis

Leatherhead supported a non-food and beverage business investor by summarising complex food legislation and food chemistry to enable a risk-based decision on a mis-labelled product.

The crisis management team was able to clearly present regulatory analysis and lab results to enable the client to understand if their soft print was being mis-sold to consumers. The team worked quickly in parallel to verify the product composition and labelling. The label was evaluated to make essential changes needed to keep the product on the market.



³ <https://www.theguardian.com/uk-news/2014/jan/10/horsemeat-scandal-sales-red-britain>

⁴ <https://www.theguardian.com/business/marketforceslive/2013/jan/16/horse-meat-tesco-market-value-shares>

About Leatherhead Food Research ▾

Leatherhead Food Research provides expertise and support to the global food and drink sector with practical solutions that cover all stages of a product's life cycle from consumer insight, ingredient innovation and sensory testing to food safety consultancy and global regulatory advice. Leatherhead operates a membership program which represents a who's who of the global food and drinks industry. Supporting all members and clients, large or small, Leatherhead provides consultancy and advice, as well as training, market news, published reports and bespoke projects. Alongside the member support and project work, our world-renowned experts deliver cutting-edge research in areas that drive long term commercial benefit for the food and drink industry. Leatherhead Food Research is a trading name of Leatherhead Research Ltd, a Science Group Company.

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Founded in 1986, Science Group was one of the founding companies to form the globally recognised Cambridge (UK) high technology and engineering cluster. Today the Group has 12 European and North American offices.

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