Key Ingredients of Highly Valued Food & Beverage Brands

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In 2018, there were more than 600 mergers and acquisitions in the food and beverage sector. A lot of buzz is created when a food or beverage brand is acquired for a big valuation. Owners of other brands want to know how they stack up: What valuation might they expect to achieve?

A significant part of achieving a premium valuation is crafting the story, positioning the brand and articulating the future growth potential. The fundamental question then becomes: which attributes of a food and beverage brand really drive value?

Brands that command high multiples often have nine core attributes in common. These are the key ingredients for maximizing value in a sale or capital raise scenario.

- **Strong sales velocity** – Retailers curate their shelf space with products that sell-through the best and generate the highest sales and profit per linear inch of shelf space. Sales velocity, measured as units sold per SKU per store per week, is one of the most important metrics for a brand because it validates performance at the point of sale. A brand generating sales velocities above its competitive set will be viewed as a strong performer and is likely to win more shelf space and greater distribution. The combination of high velocity and significant distribution whitespace is compelling for acquirers.

- **Brand equity** – Consumers want to feel good about the brands they purchase. Brands that sell for big valuations often have an authentic founder's story, a clear mission and a loyal following of consumers who feel passionately about the brand. These factors can make it much more difficult for other brands to compete and, ultimately, win share.

- **High gross margins** – Differentiated brands and products can often command superior gross margins. Investors generally like to see gross margins in excess of 40% for branded food and beverage companies, but each category is different. For instance, frozen food margins may be lower. A high gross margin is evidence of a brand offering something unique or value-add to a retailer.

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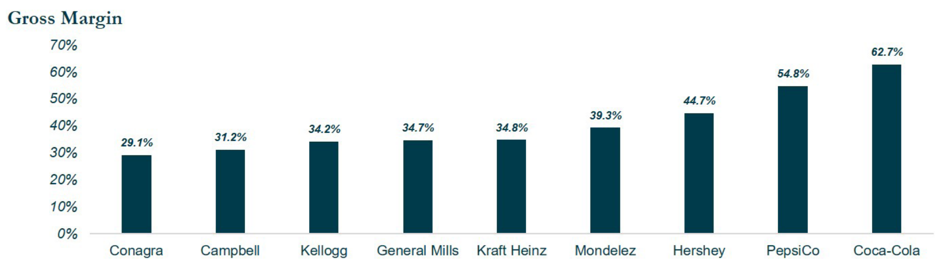
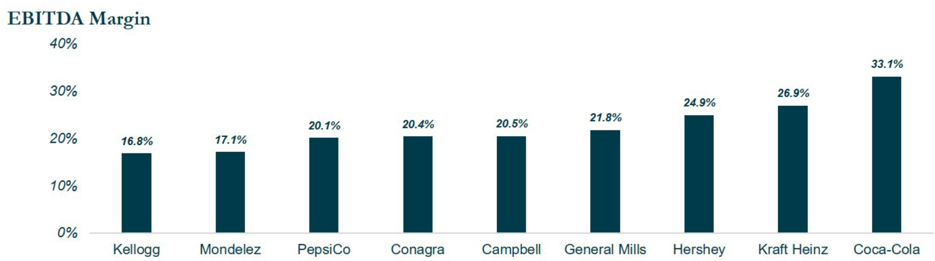
When it comes to EBITDA margins, scale matters. Many fast-growing brands spend heavily to market and promote their continued growth. Strategic acquirers understand these dynamics, so for smaller emerging brands, showing positive EBITDA is helpful, but not paramount. Explaining the path to profitability is critical. For brands with greater scale, demonstrating healthy EBITDA margins becomes more important. Factoring in synergies with a strategic buyer, the contribution margin of an acquired brand is a key metric. Post-acquisition, will there be a near-term, realizable contribution to earnings?

A review of the gross and EBITDA margins of selected publicly traded, food and beverage companies offers a helpful set of benchmarks. A brand that generates margins that are accretive to those of a strategic acquirer will be viewed favorably.





Source: CapitalIQ, Last Twelve Months as of 5/1/2019

- **Power SKUs** – Many successful brands begin with a focus on their core power SKUs before extending into other product categories. This approach demonstrates a proven track record. It also tells a cleaner story for a strategic buyer to achieve synergies. Demonstrating a near-term core product focus with a long-term product roadmap can help buyers get conviction about a bigger, broader market opportunity.

- **Unique product differentiation** – Brands that are acquired for premium valuations have scarcity value. They possess something truly special. But what makes a product one-of-a-kind? It may be a combination of factors, such as taste, flavor, quality, ingredient profile (clean label, simple ingredients), nutritional profile, form factor, mouth-feel, packaging, functional benefits, portability, convenience, shelf life or a proprietary production process that is difficult or costly to replicate.

- **Consumer loyalty** – When consumers try a product, do they become repeat purchasers? How frequently do they purchase it? Do they recommend it to their friends? When a brand enjoys high consumer loyalty, people love the products. High loyalty gives a buyer confidence that the brand will continue to perform well as its distribution becomes ubiquitous.

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- **A strong, visionary leader** – The founders and leaders of successful brands bring energy, passion and an entrepreneurial hustle. They build talented teams and inspire greatness. In an M&A transaction, strong leaders can effectively articulate their vision to a prospective buyer and "sell" the sense of inevitability that their brand can be three, five or more than 10 times bigger under the acquirer's ownership.
- **Strong growth profile** – Big food and beverage companies have a growth problem due to declining sales of legacy brands. Most industry-wide sales growth is generated by emerging brands. Instead of greater investment in research and development to launch new brands and products, many big food and beverage players have turned to acquisitions as the solution. In this environment, a brand generating exceptional growth can achieve an attractive valuation multiple. Ultimately, the price will reflect the many factors covered in this article.
- **Ability to scale** – A buyer must believe an acquisition target can scale to a meaningful level. For a brand that is currently generating $50 million or $100 million in sales, this might mean having conviction that it can reach $300 million, $500 million or greater. To realize a brand's future potential, buyers must take into consideration the distribution whitespace and potential extendibility of the brand platform. When a strategic buyer believes a brand will scale and they see the potential to leverage their vast internal resources to drive both sales and cost synergies, then they are more willing and able to pay a premium price to acquire the brand.

Common Traits of Highly Valued Food and Beverage Brands

1 Strong Sales Velocity Performance is validated at the point of sale	**2 Brand Equity** The brand resonates with consumers	**3 High Margins** There is a strong gross margin profile
4 Power SKUs A winning product is established before extending into new categories	**5 Unique Product Differentiation** It is clear that the brand is special and authentic	**6 Consumer Loyalty** Consumer data show repeat customer purchases
7 Strong, Visionary Leader The founder/CEO displays passion, hustle and conviction that align with a vision for the future	**8 Strong Growth Profile** The brand is generating exceptional growth	**9 Ability to Scale** A strategic acquirer believes in the vision and that brand has potential to generate $300M+ in sales

These nine attributes are, to some degree, controllable by a brand. However, some drivers of valuation are outside of a brand's control. For example, there may be strategic priorities that are completely unique to one buyer and if a target brand is a great fit, then that buyer might be willing to pay a big price. When a brand possesses the attributes covered in this article and there is a motivated buyer who views the brand as a "must-have" acquisition, then the foundation is set for a premium, outlier valuation. So how does your brand stack up?

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