

Member NASD and SIPC

*Food Products Group*

# QUARTERLY FOOD PRODUCTS REPORT

## Nutraceuticals M&A Upswing

There has been a noticeable increase in M&A activity in the Nutraceuticals category. Activity in certain sectors, such as functional foods, is to be expected given the strong consumer demand for such products. Such transactions included Fremont Investors' July 2003 acquisition of Nellson Nutraceuticals for \$300 million. Nellson, a leading manufacturer of health food snack bars, subsequently acquired Bariatrix Products Int'l. Inc. of Montreal, increasing its snack bar and powders manufacturing capacity.

The Supplements segment has also seen a marked upswing in M&A activity. Given the commoditization and flat growth of the Vitamins category and the upheaval being caused by

Ephedra health risks within the weight loss category, the Supplements industry has faced much disarray. As a result, once prominent brands have been humbled and many supplement manufacturers have been struggling. Given this backdrop, it has been interesting to see IdeaSphere's recent \$65 million acquisition of Twinlab Corporation. Self help guru Tony Robbins and several former Amway executives back IdeaSphere. Robbins, who apparently figures to apply his celebrity status to the supplements business, is not alone in his interest in the space. Other celebrities, as well as private equity groups, are actively looking  
*(Continued on page 3)*

**Inside this issue:**

**Page**

Nutraceuticals	1, 3
M&A Activity Commentary	1, 2, 3
Our Food and Beverage Practice	3
Select Food M&A Transactions	4

## M&A Trends in Food and Beverage

With a 35 percent increase over the comparable period, M&A activity in the food and beverage sector picked up significantly year to date 2003. In 2002, a total of 54 acquisitions involving U.S. based targets were announced, with 37 transactions announced in the first three quarters of the year and 17 announced in the fourth quarter. The boost in fourth quarter announcements was an indication that the pace of merger and acquisition activity was beginning to improve in the industry.

Following a lackluster first quarter in 2003, where only 10 acquisitions were announced, 20 M&A transactions were announced in both the second and third quarters. The 50 announced acquisitions in the first three quarters of this year represents a 35 percent increase over the 37 announced transactions for the year ago period. The significant rise in 2003 was driven by an upsurge in activity in the second and third quarters, which increased 54 percent and 82 percent, respectively.

Year to date 2003 transactions were also broader-based across categories versus the same period in 2002. Where growth was relatively flat overall in 2002, with the exception of a few sectors such as Frozen Food, most segments of the industry experienced a boost in acquisition activity over the year ago period.



Source: Mergerstat.

Across all industries, M&A activity increased by four percent in the quarter ended September 30, 2003 versus the year ago period. For the nine months ended September 30, 2003 deal activity was down three percent versus the prior year, a sign of similar stability following the dismal 13 percent decline in activity experienced in the similar 2002 period.

In addition, the easing of the credit markets has opened the door for more flexible financing. While not back to the frothy days of late 90's, the market has seen some increase in the amount of leverage available to borrowers for deals. This, combined

with the slight increase in lenders' willingness to lend and low interest rates has created greater opportunities for M&A. USBX is currently working with several strategic and financial buyers on acquisition strategies within the food and beverage sector in order to capitalize on this market change.

With the improvement of the credit markets, the food processing industry is seeing a pick up in interest from financial buyers. Since January 2002, 26 percent of announced acquisitions in  
*(Continued on page 2)*

# M&A Overview

(Continued from page 1)

the industry have involved a private equity (i.e. buyout fund) buyer. Food processing companies have become more attractive to private equity firms primarily due to their perceived stability in cash flow even in soft economic times. This relative strength allows financial buyers to assume high levels of debt, which, after being paid down over time, results in a high return on equity. An added attraction of food processing firms to private equity investors is the relative infancy of many of the brands in the marketplace. Financial buyers who pursue such acquisition targets look to benefit from developing young and emerging brands with the assistance of experienced and focused management teams.

Strategic buyers (i.e. industry buyers) are again pursuing acquisitions to drive top line growth and to extend into new product categories. The abundance of M&A is continuing to create fewer, but larger, food companies. The increase in activity has also resulted in strategic buyers pursuing ever-smaller deals, which has frustrated financial buyers who are being forced to compete with strategic buyers that are usually willing to pay higher multiples for acquisitions. Examples of large strategic buyers targeting smaller food processing companies include the purchase of

Acirca, Inc. buy Hain Celestial Group, the purchase of Mother's Kitchen Inc. by Rich Products Corp., and the purchase of Stefano by Smithfield Foods.

In June, Hain Celestial Group acquired privately held Acirca for an estimated \$13.5 million. Acirca, the owner of the Walnut Acres brand of organic fruit juices, soups, pasta sauces and salsa, is expected to add just \$20 million in annual sales to Hain's existing \$460 million. In July, Rich Products acquired Mother's Kitchen, a small private company that produces premium cakes and cheesecakes through a single manufacturing plant in New Jersey. Last year giant Smithfield Foods, with sales in excess of \$7 billion, surprised several financial buyers by outbidding them for Stefano, a frozen Italian convenience food manufacturer with sales of

approximately \$22 million.

Certain sectors in the food industry are worth highlighting due to heightened M&A activity:

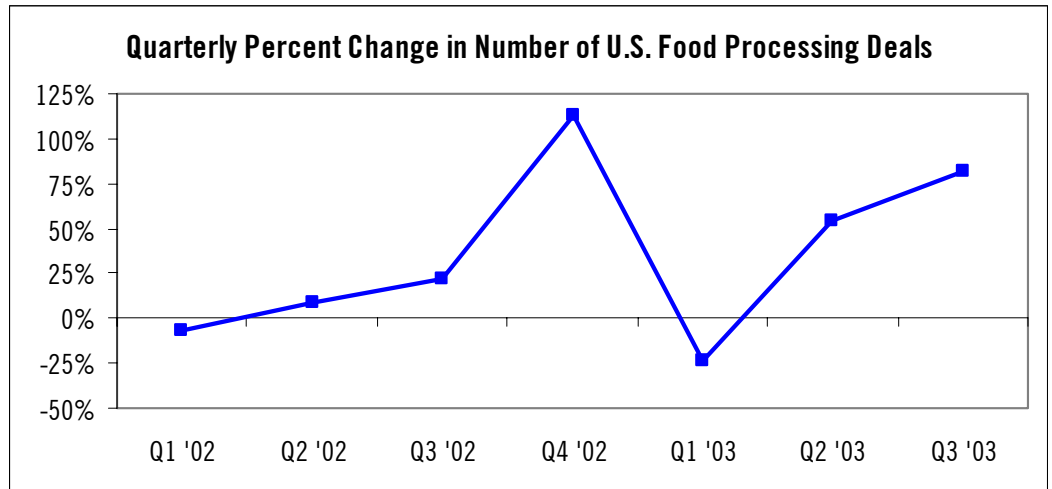
**Frozen Desserts:** The Frozen Desserts segment has continued to experience an increase in deal activity as larger distributors acquire smaller frozen dessert companies. This is primarily the result of consolidation at the grocery retail and food service distribution level, which is forcing consolidation among frozen dessert manufacturers who are finding it difficult to gain access to larger retailers and distributors. In July, CoolBrands International Inc., a Canadian producer of frozen desserts, agreed to buy a majority stake in Americana Foods, a Dallas-based frozen dessert and beverage mix manufacturer. CoolBrands

recently acquired the Dreamery ice cream, Whole Fruit sorbet brands, and the license for the Godiva ice cream brand from Dreyer's Grand Ice Cream. It also acquired the U.S. Haagen-Dazs ice cream distribution system from Nestlé. The acquisition of American Foods compliments CoolBrands' recent brand acquisitions, leverages its distribution system acquisition, and positions the company as the third largest ice-cream producer in the U.S.

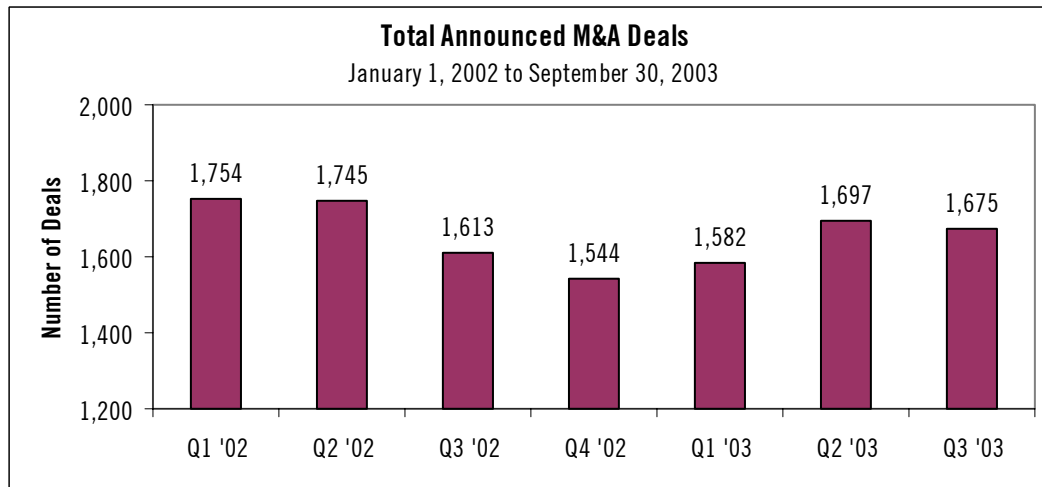
**Ethnic Foods:** Acquisitions in the Ethnic Foods segment continue to outpace most other industries. In August, Bruckmann, Rosser Sherrill & Co., a New York-based private equity firm, finalized the purchase of the Ortega brand from Nestle SA for \$116 million through its platform company B&G Foods Inc. B&G already had a Mexican food presence with its Las Palmas Mexican sauces and numerous ethnic sauces and seasonings brands. Bruckmann Rosser is looking to take advantage of strong market interest in ethnic foods businesses by selling B&G foods. There remains particularly strong market interest for Hispanic and Asian food producers.

**Refrigerated Foods:** The Refrigerated Foods category has seen solid deal activity as

(Continued on page 3)



Source: Mergerstat.



Source: Mergerstat.

# Nutraceuticals

*(Continued from page 1)*

at opportunities in the sector.

While the Supplements industry is currently navigating through turbulent times, consumer demand in certain categories remains very strong. As seen in the chart below, Weight Loss Supplements have grown at a compound annual rate (CAGR) of 13 percent for the last five years followed closely by Sports Nutrition products, which has had a five-year CAGR of nine percent. Demand within these two segments of Supplements is being driven by Americans' increasing focus on health and weight loss, which is not expected to abate any time soon. The Supplements industry is very fragmented; it is populated by numerous small to mid-sized companies, many of whom are undercapitalized and possess brands with limited consumer awareness. For years these companies have competed on the basis of improving the science behind their products, ever so slightly, in order to gain an advantage over a competitor. As a result, little emphasis has been placed on creating brand value and, consequently, very few Supplement brands currently carry value. This is a clear example of an industry ripe for

consolidation. Accordingly, celebrities are looking to deliver brand awareness and acceptance while private equity groups are looking to consolidate supplement contract manufacturers and put their resources behind undercapitalized brands.

The recent Ephedra scare will not eliminate the weight loss supplement category. Americans' continued focus on personal health and self-image will continue to drive demand in these categories, as evidenced by consumers purchasing Ephedra Free weight loss products. Look for further consolidation in 2004 in the Supplements and Weight Loss categories and for the emergence of a number of players with significant capital looking to build dominant category brands.

Supplement Market Segment	Retail Sales (\$ millions)	CAGR (1997-2002)	CAGR (2002-2005)
<b>Weight Loss</b>	<b>\$4,550</b>	<b>13%</b>	<b>15%</b>
Vitamins	\$6,140	3%	1-3%
Multi-Vitamins	\$3,254	4%	2-4%
Herbals/Botanicals	\$4,260	4%	1-2%
Sports Nutrition	\$1,851	9%	6-9%
Minerals	\$1,460	7%	4-6%

Source: Nutrition Business Journal.

## *Our Food and Beverage Practice*

*The USBX Advisory Services' Food Products Team combines the operational knowledge of seasoned industry executives with experienced investment bankers. Our team has a thorough understanding of each segment of the Food Products supply chain from manufacturing and distribution to retailing.*

*We couple our industry expertise with strong relationships with hundreds of major strategic and financial acquirers of middle market food companies, most of which are actively seeking acquisition opportunities for companies that meet specific criteria.*

*For more information on our food and beverage practice, please contact Patrick Turpin.*

# M&A Overview

*(Continued from page 2)*

consumers continue to demand more fresh food alternatives. The July 2003 acquisition of Harry's Fresh Foods, the maker of refrigerated and frozen soups, sides and entrees for retail and foodservice, by The Shansby Group is an illustration of private equity interest in the sector. The sector is populated with numerous small to mid-sized players who are ripe for consolidation. Look for more activity in this sector heading into '04.

**Ingredient and Flavoring Companies:** As consumers demand greater variety and boldness of flavors, there is an increased demand for specialty products produced by the highly fragmented ingredient and flavoring industry. The Kerry Group has been voraciously acquiring flavoring and ingredient companies in the U.S. this year, including Guernsey Bel, a manufacturer of inclusions for frozen desserts, Pacific Seasonings, a manufacturer of seasonings to the meat, prepared foods and foodservice industries, Da Vinci Gourmet, a

manufacturer of flavored syrups, confectionery sauces and tea concentrates, and Crystals International, a producer of natural fruit and vegetable flavors.

**Natural/Organic:** The Natural/Organic Food Products Industry is populated primarily by small, emerging companies. As a result, many potential deals in this space are overlooked due to the fact that potential target companies are smaller than the typical size requirements of both strategic and financial buyers. Although supply of Natural/Organic food companies with revenues in excess of \$25 million is low, demand for such companies remains very high. Few deals in this segment are worth mentioning, however Kraft foods recently acquired the Back to Nature brand of privately held Organic Milling. Organic Milling will continue to produce the brand of cereal and granola, which registered sales of approximately \$10 million in 2002, under a co-manufacturing agreement with Kraft. Produce and dairy companies continue to remain the largest players in this segment and, in July, Dean Foods acquired the remaining 87 percent

interest in Horizon Organic Holdings for approximately \$256 million.

**Nutraceuticals:** See spotlight article on Nutraceuticals on Page 1

**Confection:** Favorable category dynamics continue to draw strategic and financial buyer demand. Recently, Farley & Sathers Candy Company, a portfolio company of Catterton Partners, purchased orphan brands Fruit Stripe and Rain-Blo from Hershey Foods Corp. Other prominent deals in the space involve family-owned confection manufacturers such as Just Born acquiring Goldenberg Candy Company, Marlow Candy acquiring Skinners, and Brachs Confections acquiring Klaus Jacobs Holdings.

**Contacts:**

Patrick Turpin, Managing Director  
 (310) 315-6705  
[pturpin@usbxadvisory.com](mailto:pturpin@usbxadvisory.com)

Pejman Sabet, Associate  
 (310) 315-6731  
[psabet@usbxadvisory.com](mailto:psabet@usbxadvisory.com)

Matthew Magnuson, Analyst  
 (310) 315-6755  
[mmagnuson@usbxadvisory.com](mailto:mmagnuson@usbxadvisory.com)

**An Investor Group**

has completed the financing of

**Forza Nutrition, LLC**

a producer and marketer of leading edge nutraceuticals and functional foods for active lifestyle consumers

January 2004



*We initiated this transaction, recruited the senior management team and served as exclusive financial advisor to the investor group*

*USBX Advisory Services is a full-service investment bank providing the highest quality advice and execution to middle market businesses and their owners. USBX offers a full range of M&A solutions: Exclusive Sales and Divestitures, Acquisition Advice, Management Buyouts, Recapitalizations, Valuation Services and Acquisition Finance. In addition, USBX Advisory Services provides clients with a host of Private Placement Services, including Private Equity, Subordinated Debt, Senior Debt, Growth Capital and Refinancings. Our professionals have negotiated, structured and managed over 500 transactions of varying size and complexity for some of the most successful corporations and private equity groups in the world. To learn more, please visit our website: [www.usbxadvisory.com](http://www.usbxadvisory.com).*

**Selected Recent Food M&A Transactions**

Closed	Seller (Unit Sold)	Buyer	Target Business Description:	Enterprise Value (\$mm)	EV / Revenue	EV / EBITDA
<b>Nutraceuticals</b>						
Announced Nov-03	TwinLab Corporation	IdeaSphere, Inc.	Manufacturer of science-based nutritional supplements	\$65.0	0.2x	NA
Announced Oct-03	Atkins Nutritionals, Inc.	Parthenon Capial and GS Capital Partners	Leader in controlled carbohydrate information, food products and nutritional supplements	NA	NA	NA
Announced Sep-03	Beneficial Holdings Inc	Smart Kids Inc	Manufactures dietary supplements	NA	NA	NA
Announced Jul-03	Century Foods International	Hormel Foods Corporation	Major supplier of ingredients for whey protein powders, ready-to-drink protein beverages and nutrition bars	\$115.0	0.9x	NA
Jul-03	Bariatrx Products Int'l, Inc.	Nellson Nutraceuticals, Inc.	Produces nutritional bars	NA	NA	NA
Jul-03	NBTY, Inc.	ReXall Sundown Inc	Manufactures and sells vitamins and supplements	250.0	0.6x	6.4x
Jul-03	Nellson Nutraceuticals, Inc.	Fremont Investors	Formulates and manufactures nutrition bars and powders	300.0	1.4x	6.0x
May-03	Elan Nutrition	Sun Capital Partners Inc	Manufactures sports and nutritional bars	NA	NA	NA
Apr-03	Nutraceutical Clinical Laboratories International (Health Care Direct Services)	Private Group Led by Management of Health Care Direct Services	Markets and distributes specialty nutraceutical food	NA	NA	NA
<b>Flavorings and Ingredients</b>						
Oct-03	Crystals International Inc	Kerry Group PLC	Manufactures freeze-dried powders for fruit beverages	\$62.0*	NA	NA
Oct-03	Da Vinci Gourmet	Kerry Group PLC	Manufactures flavored syrups, confectionary sauces and tea concentrates	NA	NA	NA
Apr-03	Pacific Seasonings	Kerry Group PLC	Manufactures seasoning products	\$57.5**	NA	NA
Apr-03	Guernsey Bel	Kerry Group PLC	Manufactures inclusions for frozen desserts	NA	NA	NA
Mar-02	Stearns and Lehman	Kerry Group PLC	Manufactures beverage flavorings, Italian-style syrup, sugars and toppings for the beverage and specialty coffee industries	24.8	1.1x	8.1x
<b>General Food</b>						
Nov-03	Bakery Chef	Ralcorp, Inc.	Manufactures frozen griddle products such as pancakes, waffles and French toast and frozen pre-baked biscuits	\$287.5	1.7x	NA
Jul-03	Mother's Kitchen Inc.	Rich Products Corp.	Manufactures premium desserts including gourmet cheesecakes and cakes	\$28.0	NA	5.5x
Jun-03	Acirca Inc.	Hain Celestial Group Inc.	Markets and distributes organic fruit juices, soups, pasta sauces and salsas	\$13.5	0.7x	NA
Announced Jul-03	Aurora Foods Inc	Childs (JW) Associates LP	Produces assorted food products including syrups, bake mix and frozen foods	\$304.3	0.4x	3.0x
Jun-03	Bumble Bee Seafoods LLC	Centre Partners	Manufactures canned seafood products	NA	NA	NA
Jun-02	Stefano, Inc.	Smithfield Foods, Inc.	Manufactures Italian convenience foods, including stuffed breads, calzones, stuffed pizza rings, and pizzas	\$44.8	NA	6.8x

\*Enterprise Value includes value placed on both Crystals International and Da Vinci Gourmet.

\*\* Enterprise Value includes value placed on both Pacific Seasonings and Guernsey Bel.

Source: Mergerstat and USBX research.