Sparks of interest

M&A trends in consumer and retail

Q2'23

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Introduction

A step in the right direction

While Q2'23 deal volumes in the consumer and retail (C&R) sector remained muted, it doesn't tell the full story. During the quarter, and in the weeks that followed, we continued to see increased pre-deal activity with management teams more actively prepping businesses to bring to market. This includes an enhanced focus on value creation and performance improvement activities with an eye toward boosting enterprise value. For some, this has also driven bolt-on, strategic M&A (with specific deal activity notable in the convenience store space). Meanwhile, those that are further down the path are stepping up pre-sale due diligence.

At this stage in the cycle, there is a heightened need to focus on commercial and operational diligence to best support and articulate the revenue and earnings potential for C&R businesses that have recently faced pricing and input cost pressures. To return to historical deal volumes, buyers and sellers will need to align around the C&R market dynamics and broader economic forecasts to see a path to value for businesses on the trading block. The largest deal in the quarter was the announced $18 billion merger between two agribusinesses, St. Louis-based grain trader Bunge Limited and Canada's Viterra.

One of the brighter spots was convenience store mergers, especially in the Southeast US. The deals included Majors Management agreeing to buy 192 MAPCO Express convenience stores, while Canadian firm Alimentation Couche-Tard announced the purchase of the remaining 112 MAPCO stores in the region.[1]

Companies often use slowdowns to revisit strategy. Tempur Sealy, the maker of iconic mattresses, became a vertically integrated bedding firm by announcing the acquisition of Mattress Firm Group, the nation's largest specialty mattress retailer, with a $4 billion purchase—the second-largest C&R deal of Q2'23.

Downturns in the M&A market have historically created a favorable environment for take-private transactions, where buyers see value in compressed stock prices and management sees opportunities to deliver faster growth to shareholders under private ownership. Franchise Group, which is the parent company of Vitamin Shoppe stores and a number of other retail brands, was taken private by its management in a deal worth $2.6 billion, the third-largest transaction of the quarter in the C&R sector. As this deal illustrates, despite the depressed deal numbers, work is taking place behind the scenes on both divestitures and acquisitions that can come to market once the economy picks up.

Frank Petraglia
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Q2'23 highlights

536 deals

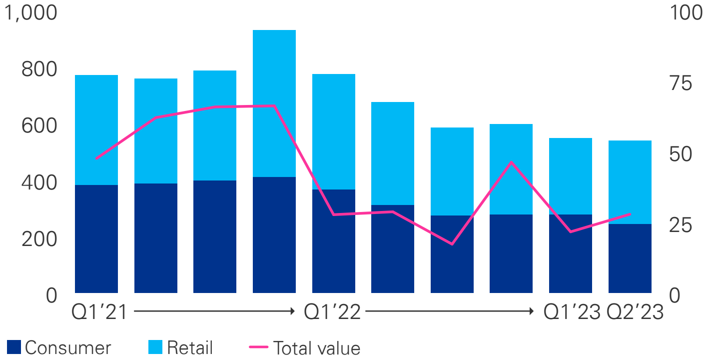
▼ **2%** decrease QoQ

$27.7 billion deal value

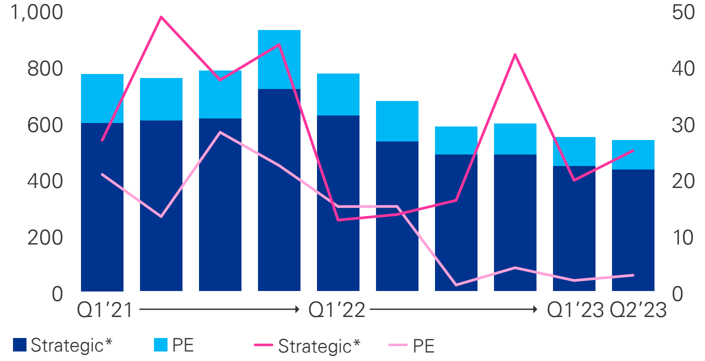
▲ **29%** increase QoQ

[1] "Alimentation Couche-Tard enters into a definitive agreement to acquire 112 fuel and convenience sites from MAPCO Express Inc.," corpo.couche-tard.com, April 27, 2023.

C&R deal activity by sector



C&R deal activity by type

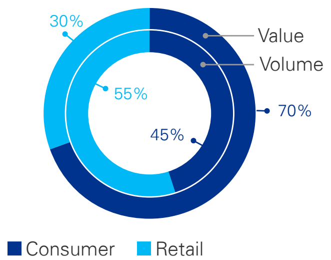


*Includes SPAC deal activity

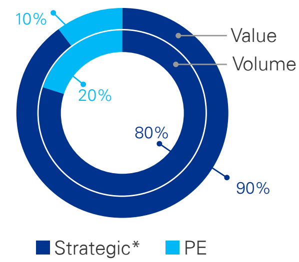
Q2'23 deal mix

Outer ring represents value. Inner ring represents volume.

Sector mix

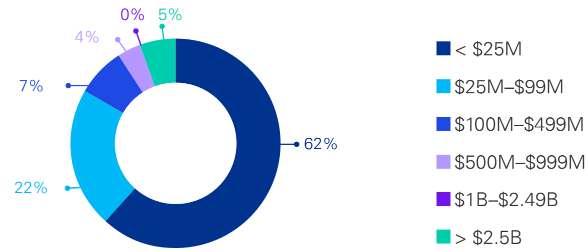


PE/Strategic mix



*Includes SPAC deal activity

Value size mix



Notable strategic deal activity

Acquirer	Target	Value (billions)
Bunge Limited	Viterra Limited	$18.0
Tempur Sealy	Mattress Firm Group	$4.0
Unilever	Yasso Holdings	undisclosed

Notable PE deal activity

Acquirer	Target	Value (billions)
B. Riley Financial, Irradiant Partners	Franchise Group	$2.6
Express, WHP Global	Bonobos	$0.1
L Catterton	Drools Pet Food	$0.1

Deal data has been sourced from Capital IQ, Pitchbook, and KPMG analysis and excludes asset purchases/minority purchases. Q2 2023 covers all U.S. deals announced from April 1, 2023 to June 30, 2023. Deal values are presented based on publicly available deal data and might not be exhaustive. Previously published statistics may be restated to incorporate new data and/or any changes.

On Tempur Sealy – Mattress Firm deal:

"This combination will accelerate our growth trajectory and enhance operating cash flow"

—Scott Thompson, Chairman and CEO of Tempur Sealy

At a glance

Consumer

Feeling their oats

Consumer sector M&A saw emerging signs of life in Q2’23, thanks in large measure to the $18.0 billion announced deal between grain dealer Bunge Limited and Canada’s Viterra. Bunge is paying $6.2 billion in stock and $2 billion in cash, as well as assuming more than $9.8 billion in debt. The combined company is expected to bring increased competition to existing market leaders, such as Conagra.

While this deal helped drive the value of consumer M&A from $8.9 billion in Q1’23 to $19.3 billion in Q2, a 118 percent increase, volume continued to lag behind. The number of deals fell from 277 in Q1 to 243 in Q2, a decline of 12 percent.

Excluding the Bunge-Viterra deal, announced M&A deal value declined in the food, beverages, and tobacco subsector to $900 million in Q2. Deal volume in the subsector declined from 136 deals to 121 transactions.

A bright spot in the consumer sector and an indication that deal activity is bubbling behind the scenes was Unilever’s announced acquisition of Yasso holdings, a maker of frozen Greek yogurt products. Yasso joins the company’s legacy frozen treat brands, including Ben & Jerry’s, Magnum, and Talenti. Financial details were not disclosed.[2]

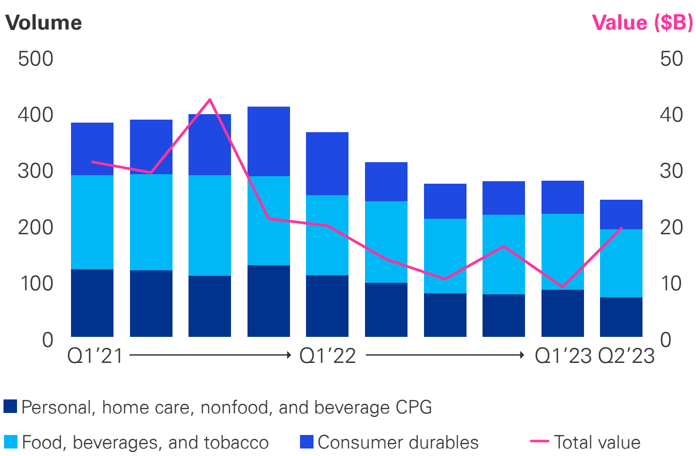
In the personal, home care, and nonfood subsector, deal value declined marginally from $370 million to $350 million, reflecting a decline in deal volume from 83 in Q1 to 70 in Q2. Consumer durable deals fell from $300 million in Q1 to $100 million in Q2, with deal volume declining from 58 to 52, a 10 percent fall.

Consumer durables are often big-ticket items that require financing, and many consumers have already replaced major appliances, thanks to an infusion of pandemic relief funds. One cautionary note: Consumer spending that requires financing could be showing signs of decelerating as the Fed continues to raise interest rates. This showdown between the consumer’s resilience in a time of Fed tightening is one to keep your eye on.

Q2’23 highlights

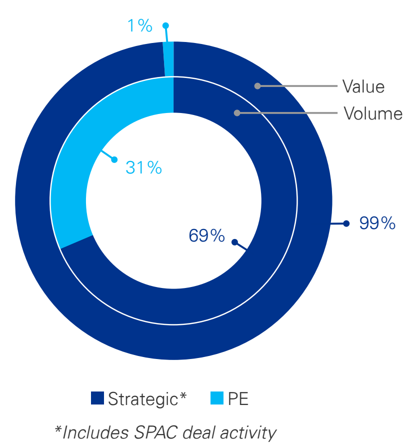
243 deals ▼ **12%** decrease QoQ | **$19.3** billion deal value ▲ **118%** increase QoQ

Consumer deal activity by subsector



Q2’23 Consumer PE/strategic mix

Outer ring represents value. Inner ring represents volume.



*Includes SPAC deal activity

[2] “Unilever to acquire Yasso in North America,” unilver.com, June 14, 2023.

On Bunge Limited – Viterra Limited deal:

"Our highly complementary asset footprints will create a network that connects the world's largest production regions to areas of fastest growing consumption, enhancing the geographical balance and adaptability of our global value chains and benefitting farmers and end customers"

—Greg Heckman, CEO of Bunge Limited

Notable consumer deal activity

Acquirer	Target	Rationale	Value (billions)
Bunge Limited	Viterra Limited	Enhanced global network, geographic diversification	$18.0
Bite Acquisition Corp	Above Food	SPAC merger	$0.3
Unilever	Yasso Holdings	Premiumization, expand ice cream portfolio to the 'Better For You' segment	undisclosed

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At a glance

Retail

Time-saving convenience

Despite the overall decline in M&A activity in the C&R sector, retail began emerging from the doldrums by showing signs of life in select subsectors.

The overall value of retail deals declined from $12.7 billion to $8.4 billion, a fall of 34 percent, however, still at a healthy level considering the impact of higher interest rate environment. By subsector, the greatest decline was in brick-and-mortar M&A, falling from $12.1 billion in Q1'23 to $7.6 billion in Q2, down 37 percent. There was a noticeable absence of significant deals reported in online retail. Restaurant M&A posted a gain from $300 million to $730 million, in large part due to Darden Restaurants acquisition of Ruth's Hospitality Group, owner of the Ruth's Chris Steakhouse brand, for $715 million.

Strategic versus PE

Deal market dynamics continue to be very different for the strategic players versus the pure-play financial sponsors. Recently, corporates, particularly those with strong balance sheets, have been able to explore M&A opportunities with less PE competition for assets; however, as the steep increase in interest rates plateaus, we expect the PE funds to aggressively return to deal making.

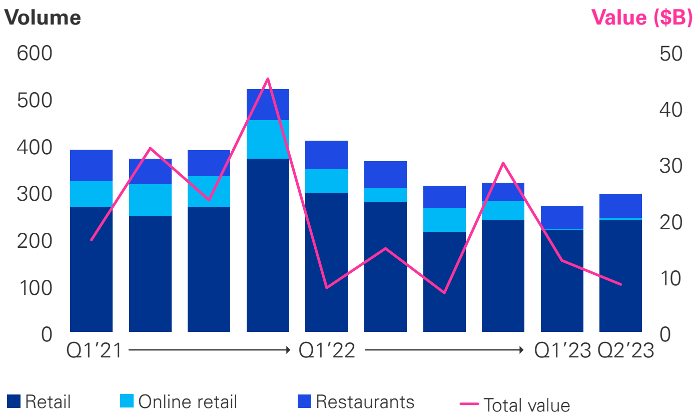
Strategic M&A increased in volume but decreased in value from Q1'23 to Q2, with 263 deals worth $5.8 billion, from 246 deals worth $11.9 billion in Q1.

PE deals increased from 23 transactions in Q1 to 30 deals in Q2, and the value of PE deals rose to $2.6 billion from $800 million in the first quarter.

Q2'23 highlights

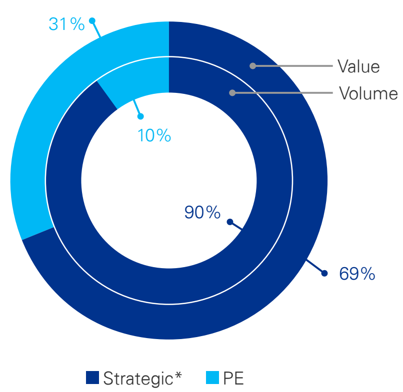
293 deals ▲ **9%** increase QoQ | **$8.4** billion deal value ▼ **34%** decrease QoQ

Retail deal activity by subsector



Q2'23 Retail PE/strategic mix

Outer ring represents value. Inner ring represents volume.



*Includes SPAC deal activity

Notable retail deal activity

Acquirer	Target	Rationale	Value (billions)
Tempur Sealy	Mattress Firm Group	Vertical integration	$4.0
B. Riley Financial, Irradiant Partners	Franchise Group	Take-private	$2.6
Majors Management, Alimentation Couche-Tard	MAPCO Express	Increase footprint in the Southeastern U.S.	$0.7

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Grocery shopping

Disrupted by the announced mega-merger of Kroger and Albertsons, players across the grocery value chain are weighing their options. We expect this is good news for both M&A activity in the regional grocery space, as well as for the grocery consumer, with business models adapting to meet the changing competitive landscape and consumer demand.

As described in the 2022 KPMG report, Stress to the system – M&A trends in consumer and retail, one key driver of sector activity is the likelihood that Kroger and Albertsons, which combined operate almost 5,000 stores nationally, will be required to divest hundreds of stores to mollify US lawmakers, who have expressed concerns that the merger would create a monopoly and could otherwise cause grocery prices to increase.[3]

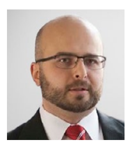
The Federal Trade Commission continues to assess the merger, which would give the combined company the kind of market clout currently enjoyed by Walmart and Amazon. As a result, smaller regional players are realizing they have to change their strategy and either bulk up or specialize if they want to remain competitive:

Pool resources. One reason for regional players to seek consolidation is that bigger firms have greater power to negotiate lower prices with suppliers, such as CPG companies. Another reason is the shift to online shopping that gained traction during the COVID-19 pandemic requires regional players to invest substantial capital to roll out e-commerce platforms that enable pickup and delivery options. Once established, the platforms can earn merchants additional profits through digital advertising.

In one regional deal, Food Lion, a supermarket chain owned by Netherlands-based Ahold Delhaize and predominantly located on the US East Coast, purchased 62 stores from rival Southeastern Grocers for an undisclosed price. Southeastern, a Jacksonville, Florida chain, emerged from bankruptcy in 2018 and was reported by the *Wall Street Journal* in November 2022 to be seeking a buyer for the remainder of its stores, which includes the Winn-Dixie chain.[4]

Focus on fresh. Finally, a notable trend, particularly among smaller supermarket chains, is the move toward a broader offering of fresh products. While the typical grocery store has between 60 and 80 percent shelf-stable goods and 20 percent fresh products, we are seeing firms add substantially more fresh SKUs to their product assortment in an effort to keep in step with the consumer's health and wellness trend, and to stand out from the bigger players. For example, when Seattle's Yoke's Fresh Markets acquired Missoula Fresh Market stores in June 2022, it said it would transform the combined business with Yoke's model of natural, organic, and specialty products.[5]

The consolidation by regional players suggests they have looked at the changing grocery landscape and cannot afford to sit idle while bigger competitors like Kroger take their most profitable business.



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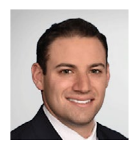

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[3] "Albertsons, Kroger reiterate store divestiture plan ahead of merger," reuters.com, March 15, 2023
[4] "Winn-Dixie Owner Southeastern Grocers Weighs a Sale," wsj.com, November 22, 2022
[5] "Missoula Fresh Market stores to be acquired by Yoke's Fresh Markets," nbcmontana.com, June 22, 2022

Outlook

Consumers' growing stress

With the chances of a recession declining in the second half of 2023, KPMG economists have dubbed the downturn—the most predicted recession ever—as a "slow session" because of how long it is taking to materialize. While consumers continued to spend their pandemic relief savings in the first half of the year, that trend is expected to slow in Q3 and grind to a halt in Q4 as consumers' savings dwindle, student loan payments resume, and banks rachet up the standards for getting a loan or a new credit card. However, retail sales rose moderately in June, a sign that the consumer still has spending power despite 500 basis points of interest rate raises by the Fed.

The consumer retrenchment is likely to be a headwind for M&A in both retail and consumer goods sectors, but there is likely to be considerable subsector divergence. For example, travel, restaurants, and leisure are currently strong but may not be sustainable. On the other hand, consumers are trading down in essentials such as groceries and staple CPG products. Another obstacle is the uncertainty surrounding business performance and profitability in this climate. While valuations for many continue their slow decline, some may remain elevated and the market has most recently yielded gains across a broader group. All of these factors will continue to drive value gap discussions, but this recent movement is a welcome shift from an overall environment of pressured value.

The uncertain economy and sharply higher interest rates to make leveraged buyouts have prompted many private equity sponsors to hit pause in their deal making. While waiting for the opportune moment to reenter the market, some PE firms have formed consortia with other firms to spread the risk for an acquisition and have even teamed up with strategics to work complementary aspects of a particular deal.

Even for strategic investors with solid balance sheets providing the wherewithal to make acquisitions at a time when PE firms are largely sitting on the sidelines, corporate teams tell us that they are challenged by the dearth of attractive targets in the market—and when something attractive surfaces, the market players clamor and drive value up, at times beyond comfort levels for buyers. At the same time, sellers tell us they are delaying sales until they see more willing buyers in the pool of bidders.

Many companies are using the slow deal activity to work with KPMG on synergy assessments, commercial due diligence, and performance improvement, while keeping powder dry for when the M&A market begins to thaw.

Key considerations

In pursuing M&A in a forthcoming economic downturn, C&R deal makers should consider the following:

1 Long-term goals

Before moving forward with a deal, buyers should consider incremental analysis around value creation opportunities during their due diligence for assets that may have been underperforming during the downturn.

2 Plan now for future sales

Corporates should prepare noncore businesses for eventual sale and have a strategy in place to drive value creation for a transaction when the market comes back in the future.

3 Adopt a protection mechanism

Buyers could require things like earn-outs or JVs with the sellers taking a larger stake.

How we can help you

KPMG helps its clients overcome deal obstacles by taking a truly integrated approach to delivering value and leveraging its depth in the C&R industry, using data-supported and tools-led insights, and providing full M&A capabilities across the deal lifecycle.

With a C&R specialization, our teams bring both transactional and operational experience, delivering rapid results and value creation.

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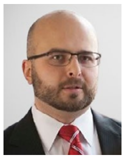

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