Three paths large food companies may follow for growth

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CHICAGO — Small and mid-size food and beverage companies have seen sales increase at the expense of the industry's 25 largest companies. The top 25 food manufacturers in the United States, which include companies with annual revenues of more than $4 billion, have ceded 300 basis points to small and medium-size competitors since 2012 and have grown revenue at 1.8% compared with 11% to 15% for smaller companies, according to a report published by A.T. Kearney and The Hartman Group.

Randy Burt, partner with A.T. Kearney

"Large established food manufacturers need to give consumers real reasons to remain loyal," said Randy Burt, a partner with A.T. Kearney and co-author of the report. "This includes providing innovative products that meet consumers' current and emerging needs, delivered when and where they shop and with transparency and authenticity in sourcing, production, and marketing."

Changing consumer core values amplified by social media and the rise of celebrity chefs and food bloggers are rewarding small and mid-size companies, according to the report. Consumer values that have shifted include a focus away from dieting and toward health maintenance; more functional foods being introduced; consumers embracing free-from foods; consumers shifting their purchases from the center of the store to the perimeter; and increased consumer demand for transparency.

Laurie Demeritt, c.e.o. of The Hartman Group

"Consumers, led by millennials and gen Xers, will continue to press companies and retailers for more information and accountability about how ingredients are sourced and processed, how real their food products are, and how responsive they are to consumers' desire for choice and customization," said Laurie Demeritt, chief executive officer of The Hartman Group and co-author of the report.

Based on industry projections, large food companies may tap into a $70 billion opportunity in overall food and beverage sales growth over the next three years, according to the report.

"What we looked at is where the market today in the U.S. is based on various research and how it will grow over the next few years to 2020," said Mr. Burt in an interview with *Food Business News*. "There is approximately $70 billion in growth that does not require taking share. It's new revenue, if you will."

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To access that growth, the report recommends three strategies companies may follow. The first involves taking cost out of the equation through efficiency programs or divestitures in order to enable investment in growth activities. Second, use controlled acquisitions of smaller, established players and external venture capital developments to add trending categories to a company's portfolio. Finally, create venture funds to invest in start-up companies and technologies that may position companies to take advantage of consumer trends with a lower entry cost.

"Fifteen years ago people said the only grocery store in America would be Wal-Mart," Mr. Burt said. "The consumer has shifted and that has led to fragmentation throughout the market.

"Today, companies need to pay attention to where their products resonate and really focus on a development strategy. It's a matter of placing strategic bets on products and customers, whether they are retailers or food service companies."

"Fifteen years ago people said the only grocery store in America would be Wal-Mart," Mr. Burt said.

A challenge facing manufacturers is acquiring companies has become more expensive.

"Five years ago we saw multiples of 8x EBITDA," Mr. Burt said. "Now we are seeing multiples of 14x, 15x EBITDA. I think we are going to see these multiples stay where they are, but the pace of acquisitions may drop a little bit."

The high cost of acquisitions is what is driving such companies as The Coca-Cola Co., General Mills, Inc., Campbell Soup Co. and The Hain Celestial Group, Inc., to create seed funds in order to get on the ground floor of food and beverage startups.

"We are seeing companies invest a lot earlier into smaller firms," Mr. Burt said. "It will be interesting to see how it develops, because it will take a while for those investments to develop."

Mr. Burt added that the industry's largest players are in a period of transition.

"If you look at the large manufacturers, they are set up to produce safe food at scale," he said. "They have invested a lot to perfect that model, and they have been less focused on innovation and variety. And then the trends changed. Now they are starting to figure out what to do about it."