Φ BROOKS, HOUGHTON & COMPANY, INC.
Merchant Banking for the Middle Market

Pet Industry Update

August 2017

780 Third Avenue • 35th Floor • New York, NY 10017

Brooks, Houghton & Company, Inc.

Introduction

Brooks, Houghton & Company, Inc. ("BHC") is a merchant banking firm dedicated to providing corporate finance advisory services and direct investment to:

- Middle-market public and private companies
- Emerging growth companies

Founded in 1989, BHC emphasizes building long-term relationships with its clients by:

- Providing innovative corporate finance solutions and professional execution at a reasonable cost
- Taking a partnership approach with clients based upon mutual trust and responsibility
- Delivering independent, objective and discreet advice

Applying these principles, BHC has earned a reputation for providing high quality, reliable professional services to its corporate clients, investors and referral sources in the United States and internationally

BHC's merchant banking products and services include:

- Mergers and acquisitions advisory
- Debt and equity private placements through Brooks Houghton Securities, Inc. (BHS), a FINRA member
- Valuations and fairness opinions
- General corporate finance advisory
- Principal investments in interim and bridge capital

Additionally, BHC is a member of Globalscope Partners, a premier global mergers and acquisitions advisors network

Why Brooks, Houghton & Company

BHC is well suited to the task of serving as an exclusive M&A advisor

- Established and experienced merchant bank with both M&A and capital raising capabilities, as well as industry knowledge
- Provide senior-level attention to the assignment on a day-to-day basis
- Offer Wall Street-quality work product and experience
- Well versed in helping small and mid-sized business owners/operators achieve their liquidity and growth objectives
- Long-standing working relationships with third-party capital providers (i.e. senior debt, mezzanine debt and private equity) and strategic partners
- Confident in our ability to attain the best possible transaction outcome

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Industry Overview

Total U.S. pet industry revenue is estimated at almost $70 billion in 2017 with the pet food market segment projected at approximately $27 billion in 2017. An increase in pet ownership has coincided with a growing tendency to treat pets as members of the family, thereby encouraging the purchase of higher-priced premium pet food products that are marketed as possessing special benefits, formulations or specialized ingredients.

Industry Structure

Life Cycle	Mature
Revenue Volatility	Low
Capital Intensity	High
Market Concentration	Medium
Regulation Level	Very High
Technology Change	Medium
Entry Barriers	Medium
Competition Level	High

Supply Industries

- Soybean Farming
- Corn Farming
- Vegetable Farming
- Meat, Beef, & Poultry Processing
- Seafood Preparation

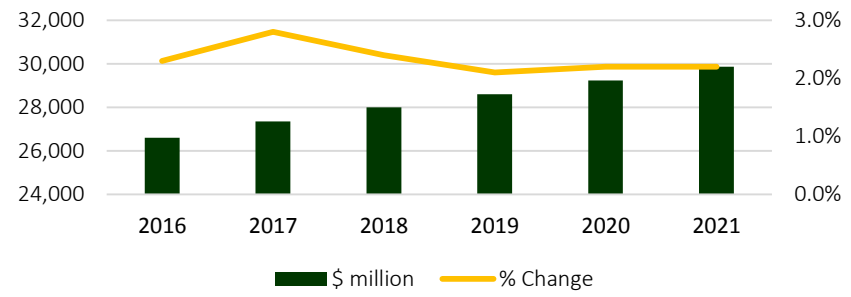
Demand Industries

- Grocery Wholesaling
- Supermarkets & Grocery Stores
- Convenience Stores
- Pet Stores
- Consumers

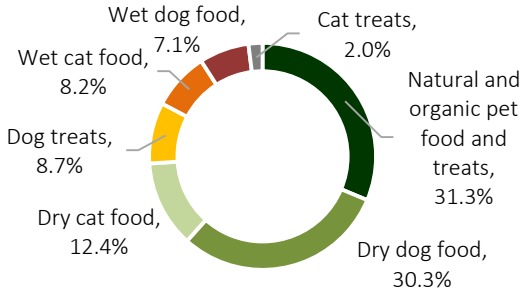
Key Success Factors

- Access to high-quality inputs
- Production of premium goods and services
- Economies of scale and scope
- Effective quality control

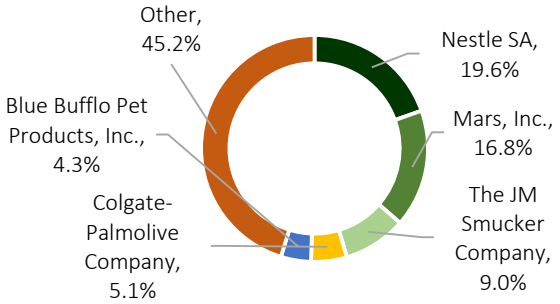
Pet Food Market – Revenue



Products Segmentation



Major Companies in Pet Food Market (Market Share)

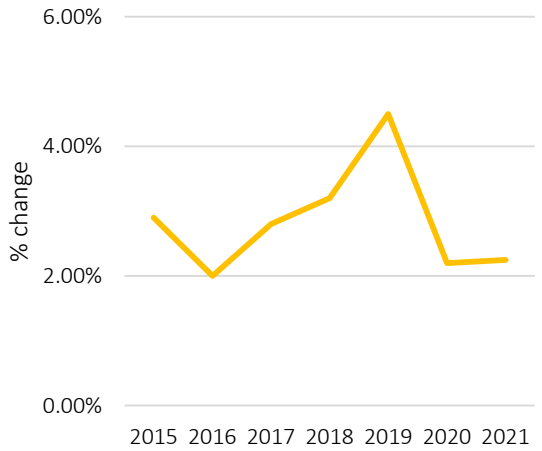


Source: IBIS World; American Pet Products Association

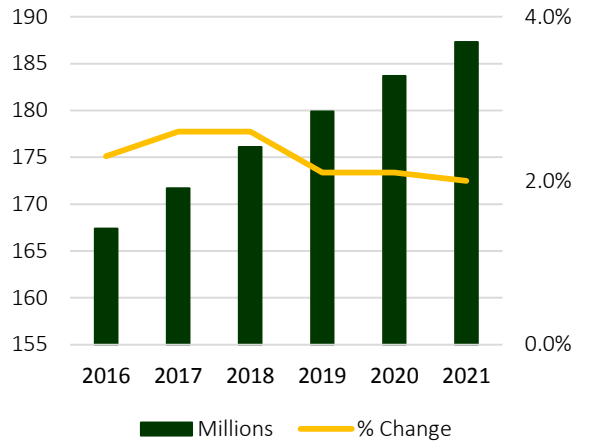
Market Overview – Key External Drivers

The U.S. pet food market's revenue growth has been driven by increasing disposable income, growing pet ownership with a tendency to treat pets as family members (growing prevalence of pet parents) and a heightened focus on organic and premium pet food products. The industry profitability has benefited from falling agricultural commodity input costs, lowering industry operators' purchase costs.

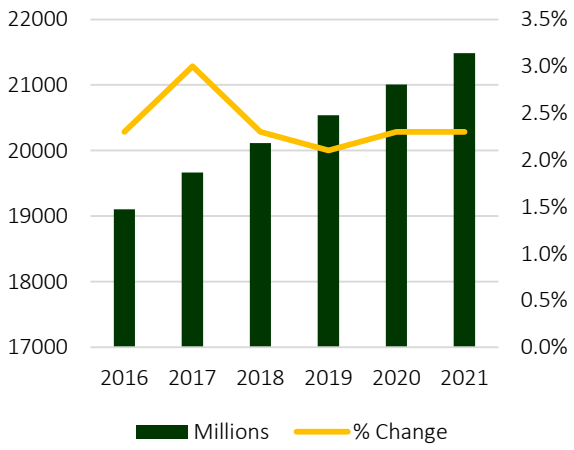
Per Capita Disposable Income



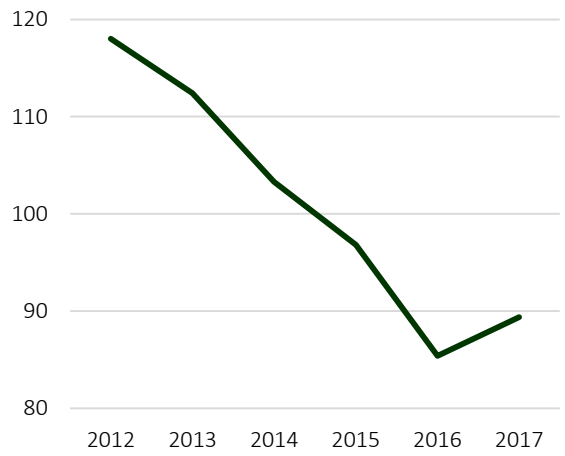
Number of Pets (Cats and Dogs)



Demand from Pet Stores



Agricultural Price Index



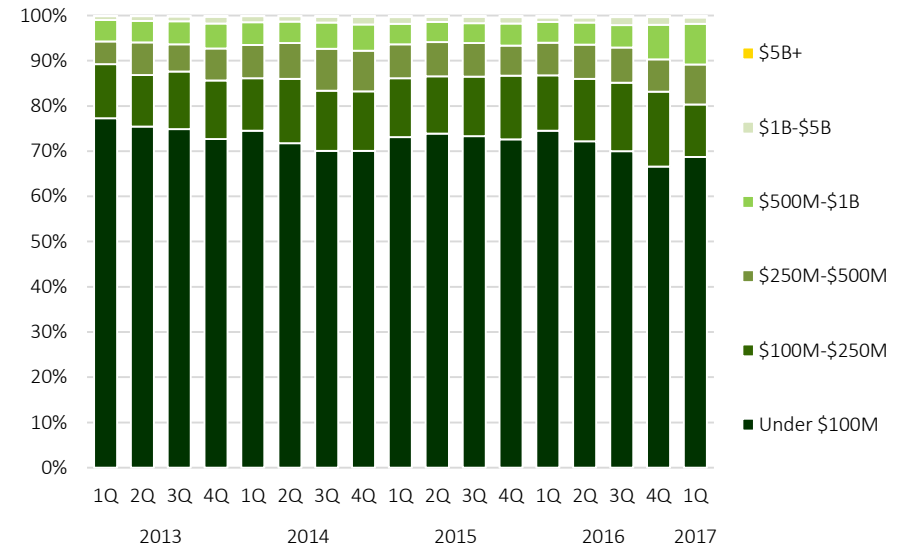
Key Takeaways

- The pet industry is recession resistant as pet owners tend not to cut back on pet food spending during an economic downturn
- Ownership of cats and dogs is a strong demand determinant for pet foods, as growth in the number of these pets drives demand for pet food
- Pet stores represent a major market for dog and cat foods, which offers consumers a one-stop shop for all their pets' needs. Online pet food and pet supply sales ($4.9 billion in 2016) are increasing, with more pet owners buying their pet food from Amazon and other websites like Chewy
- Since a variety of livestock and crop inputs are utilized in pet food production, falling agricultural prices have lowered input purchase costs

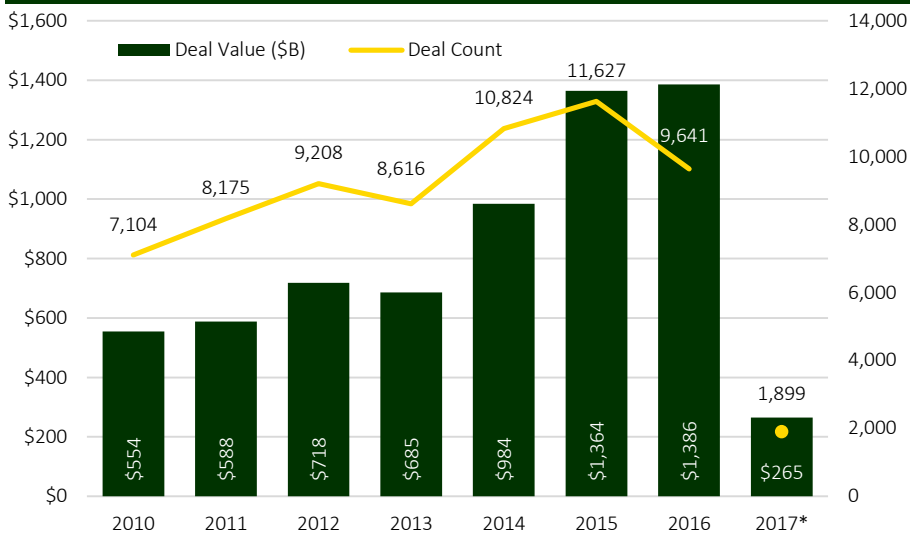
Source: IBIS World; World Bank

M&A Deal Activity – Overview

M&A Deals by Deal Size



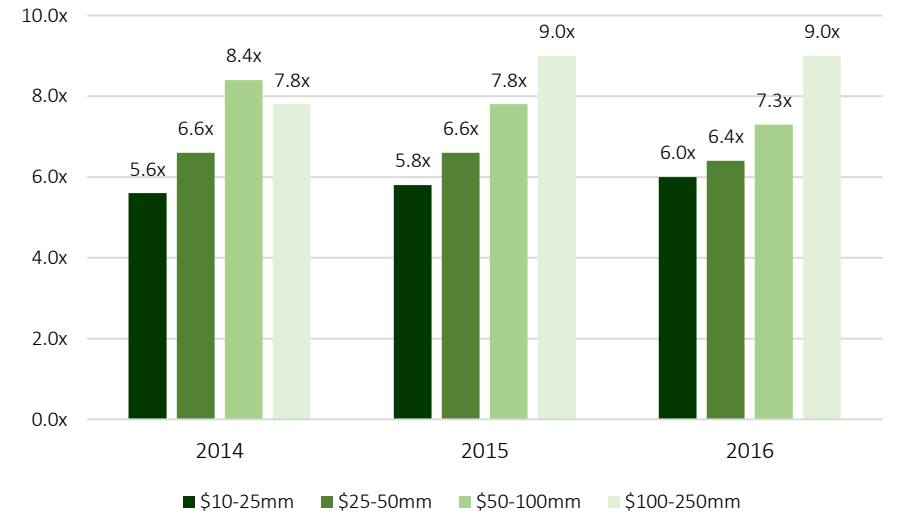
U.S. M&A Activity



U.S. M&A Activity & Transactions in the Pet Food Market

- Perceived high valuations and the anticipation of a tax reform contributed to the slow down in the U.S. M&A market during 1Q 2017
- The lower middle market remains the most active market sector despite seeing a slight decrease in terms of market share compared to 1Q 2016
- Valuation multiples for middle market transactions below $250mm remained steady
- 2016 represented a slow down in pet food M&A compared to the previous three years
- Valuations for pet food companies are historically high, so investors are looking elsewhere for values, and there is a scarcity of opportunities after the big deals in recent years

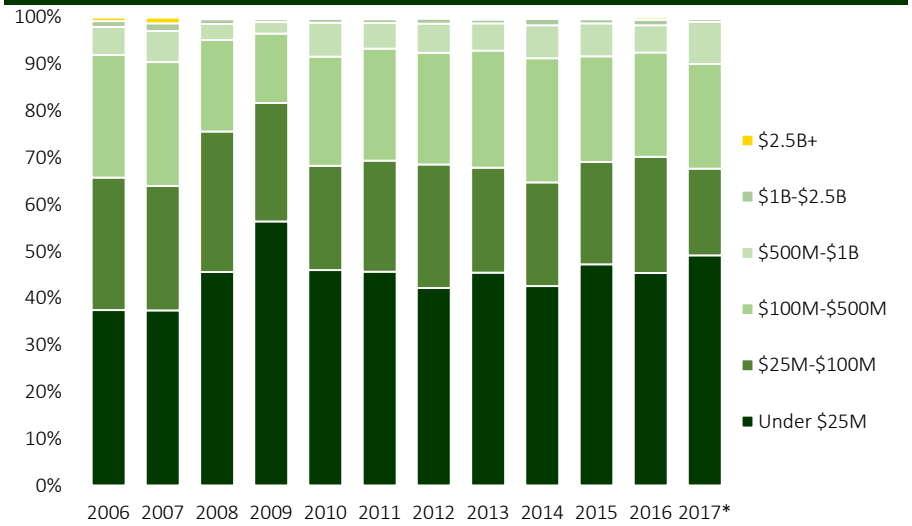
U.S. EV / EBITDA Multiples By Transaction Size



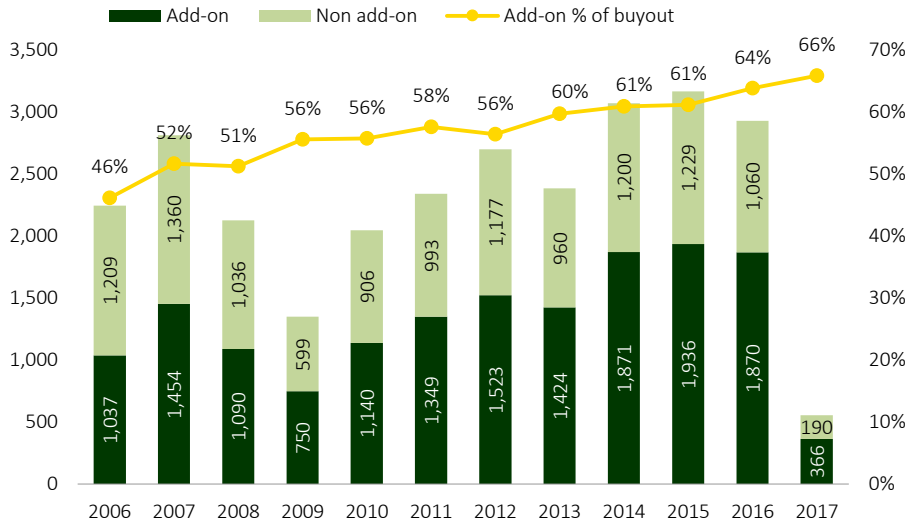
Source: Pitchbook, Thompson One, GF Data **As of 3/31/2017*

Private Equity Deal Activity – Overview

U.S. PE Deals by Deal Size



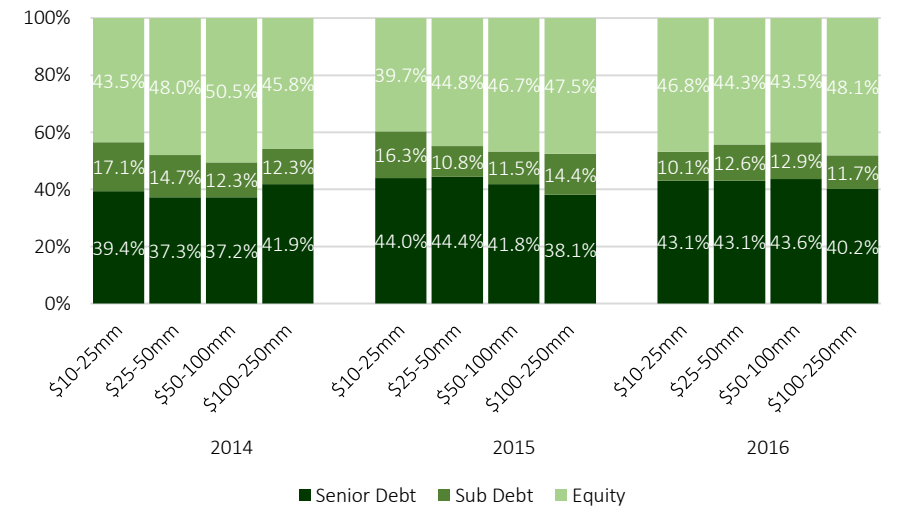
U.S. add-on % of Buyout Activity



U.S. Private Equity Deal Activity

- Across industry sectors, PE-backed transactions have slightly decreased compared to the same period in 2016 for the same reasons as the overall M&A market
- Transactions up to $100mm still account for about 70% of all U.S. PE deals with a focus on add-on transactions
- The percentage of add-on transactions has been growing at a steady pace since 2009
- The middle market transactions below $250mm have been stacked up with a large portion of equity and senior debt, a small portion of subordinated debt for the past three years

U.S. Middle Market Capital Stack

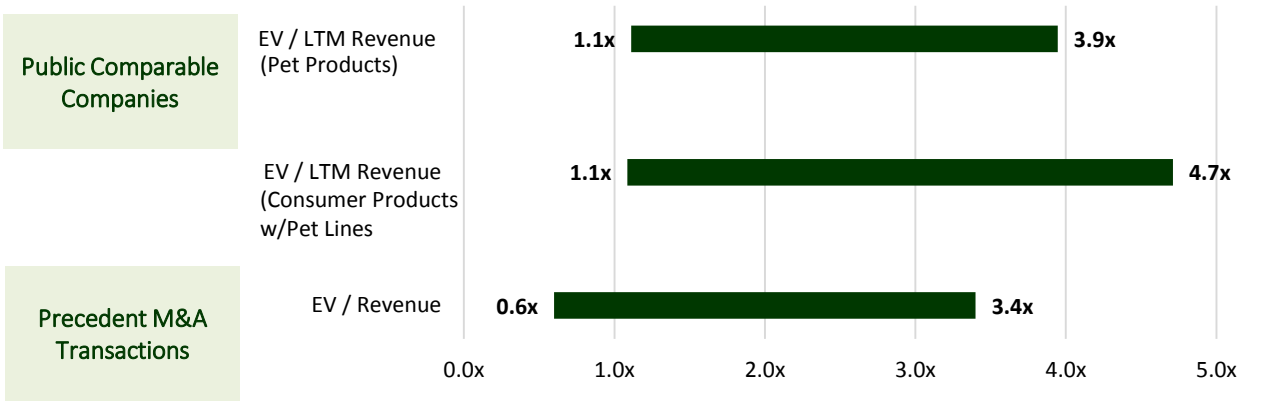


Source: Pitchbook, Thompson One, GF Data

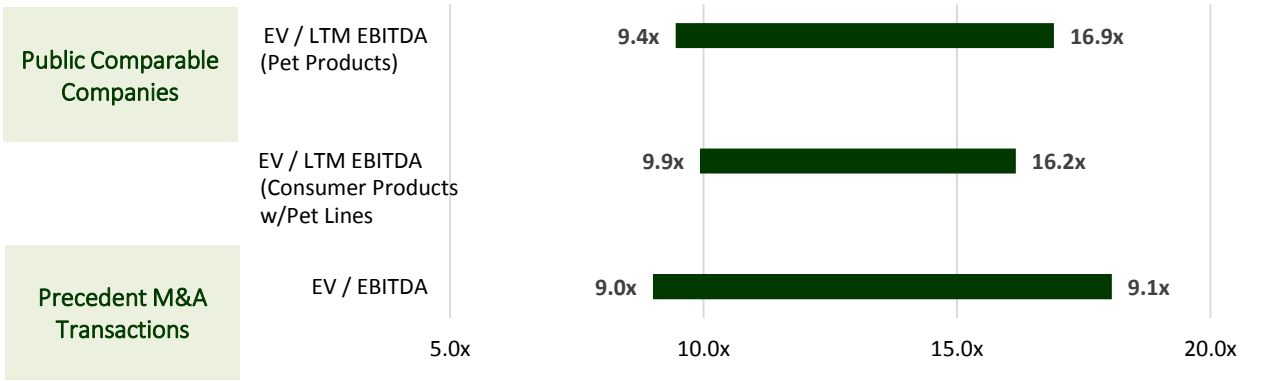
Valuation Summary

With most companies in the pet food space being private, this valuation summary is based on the limited data available on precedent transactions, four pet products public companies, and six consumer products public companies with pet lines. In general, valuations remain high due to robust M&A activity fueled by private equity interest, mainstream food companies looking to participate in the pet food market and companies within the space looking to consolidate over the past few years.

EV / Revenue Multiple Range



EV / EBITDA Multiple Range



Source: CapitalIQ

Key Takeaways

- The two powerful consumer trends, the humanization of pets and growing demand for premium and natural foods, in the pet food sector have significant impact on the valuations
- Based on precedent transactions since 2012, the EV / Revenue range is 0.6x to 3.4x, while the valuation range based on public comparable companies ranges from 1.0x to 3.9x (pet products) and from 1.1x to 4.7x (consumer products with pet lines)
- EV / EBITDA multiples of public comparable companies range from 9.4x to 16.9x (pet products) and from 9.9x to 16.2x (consumer products with pet lines)
- The assessment of the EV / EBITDA multiple for precedent transaction yields a broad multiple range as a result of too few data points, however, the average of the transactions was 12.8x

Public Comparable Companies – Detailed Overview

$ in millions

Company Name	Ticker	Business Description	Share Price	Enterprise Value	LTM Revenue	LTM EBITDA	LTM Gross Margin	LTM EBITDA Margin	LTM Revenue Growth	LTM EBITDA Growth
Pet Products										
Blue Buffalo Pet Products, Inc.	NasdaqGS: BUFF	Dog and cat food made with whole meats, fruits and vegetables, and other high-quality, natural ingredients	$22.9	$4,624.8	$1,171.9	$273.4	45.3%	23.3%	10.7%	18.6%
Central Garden & Pet Company	NasdaqGS: CENT	Edible bones, edible and non-edible chews, dog and cat food and treats, toys, pet carriers, grooming supplies	31.7	2,130.8	1,917.4	190.3	30.7%	9.9%	9.8%	22.7%
Freshpet, Inc.	NasdaqGM: FRPT	Natural fresh, refrigerated meals, and treats for dogs and cats	16.4	554.4	136.1	7.5	45.0%	5.5%	12.9%	48.2%
OurPet's Company	OTCPK: OPCO	Various accessories and consumable pet products for improving the health, safety, comfort, and enjoyment of pets	1.4	32.1	27.4	3.4	33.0%	12.4%	12.4%	15.7%
			Mean	$1,835.5	$813.2	$118.7	38.5%	12.8%	11.4%	26.3%
			Median	1,342.6	654.0	98.9	39.0%	11.2%	11.6%	20.6%
			Low	32.1	27.4	3.4	30.7%	5.5%	9.8%	15.7%
			High	4,624.8	1,917.4	273.4	45.3%	23.3%	12.9%	48.2%

Source: CapitalIQ

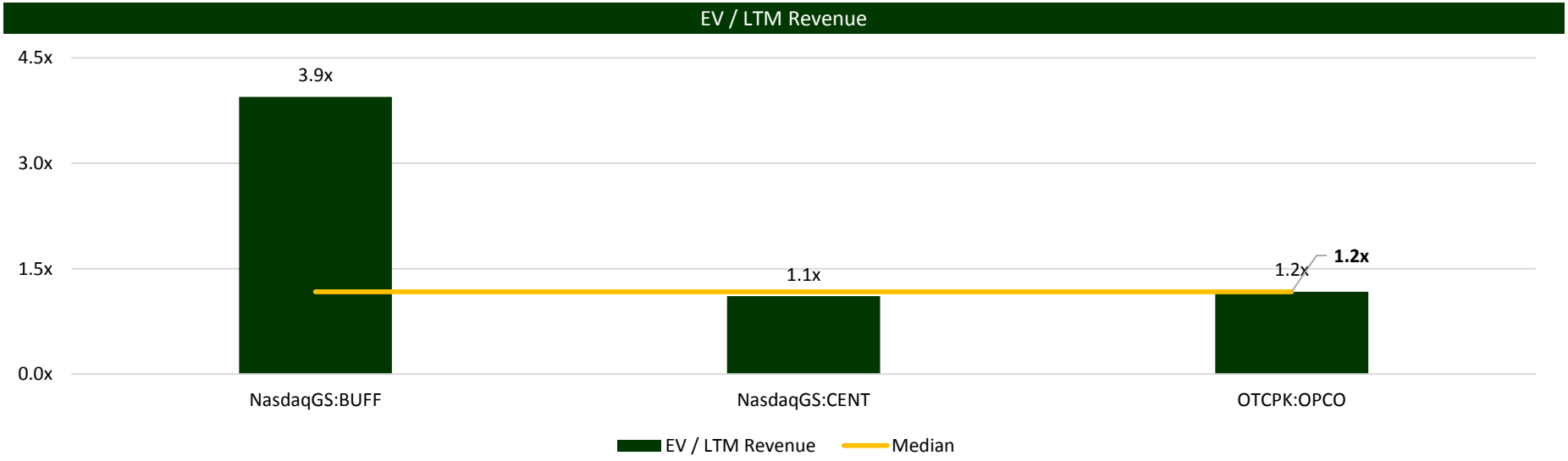
Public Comparable Companies – Detailed Overview (cont'd)

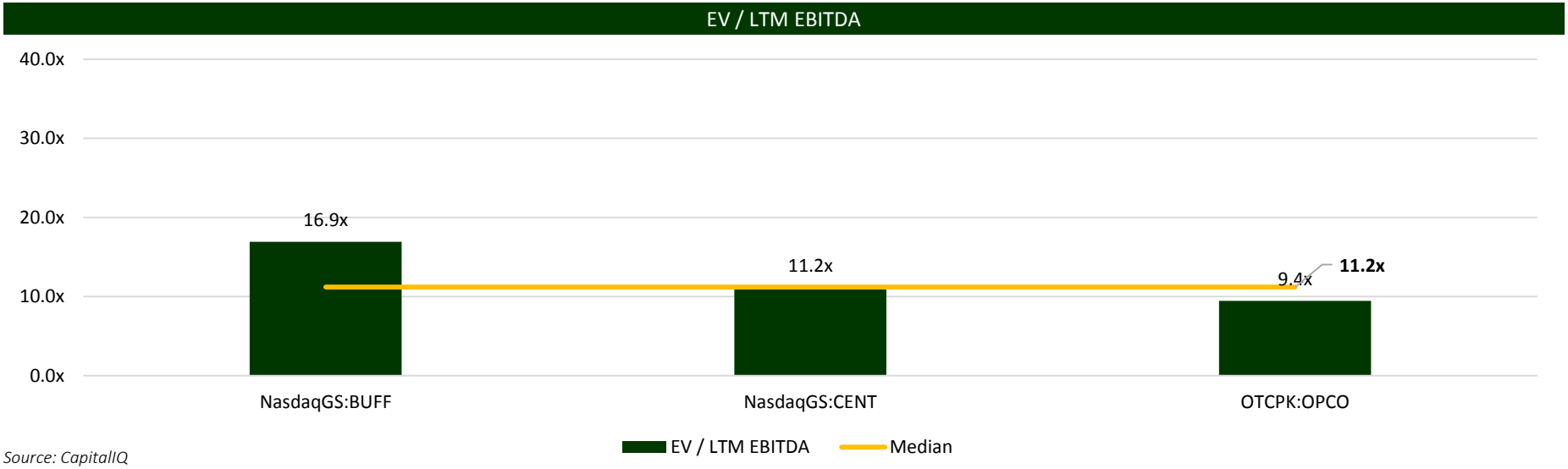
$ in millions

Company Name	Ticker	Business Description	Share Price	Enterprise Value	LTM Revenue	LTM EBITDA	LTM Gross Margin	LTM EBITDA Margin	LTM Revenue Growth	LTM EBITDA Growth
Consumer Products w/Pet Lines										
Nestlé S.A.	SWX:NESN	Pet food, treats and litter under the brands including Purina Pro Plan, Purina Dog Chow, Friskies, Beneful and Purina ONE	$85.4	$281,021.9	$93,012.6	$17,955.9	50.8%	19.3%	0.8%	2.0%
Colgate-Palmolive Company	NYSE:CL	Pet nutrition products for everyday nutritional needs and markets its pet nutrition products for dogs and cats; owns Hill's Pet Nutrition	73.9	71,580.6	15,195.0	4,429.0	60.5%	29.1%	-3.4%	2.1%
Unicharm Corporation	TSE:8113	Pet care products that include pet foods, excrement cleanup sheets, system toilets, and disposable diapers	24.9	15,403.1	6,042.5	991.1	45.5%	16.4%	-6.8%	2.2%
The J. M. Smucker Company	NYSE:SJM	Pet products comprising dry and wet dog food, dry and wet cat food, dog snacks, and cat snacks; owns Big Heart Pet Pet Brands	118.2	18,887.5	7,392.3	1,666.3	38.4%	22.5%	-5.4%	-3.1%
Spectrum Brands Holdings, Inc.	NYSE:SPB	Specialty pet supplies including dog and cat treats and small animal foods through its Global Pet Supplies business	125.3	11,151.1	4,993.0	897.0	38.6%	18.0%	0.2%	8.7%
Oil-Dri Corporation of America	NYSE:ODC	Petcare products from clay minerals; a broad range of litters and liners.	42.6	284.1	261.4	28.6	29.3%	10.9%	-0.6%	-4.3%
			Mean	$66,388.0	$21,149.5	$4,328.0	43.9%	19.4%	-2.5%	1.2%
			Median	17,145.3	6,717.4	1,328.7	42.1%	18.6%	-2.0%	2.0%
			Low	284.1	261.4	28.6	29.3%	10.9%	-6.8%	-4.3%
			High	281,021.9	93,012.6	17,955.9	60.5%	29.1%	0.8%	8.7%

Source: CapitalIQ

Public Comparable Companies – Pet Products

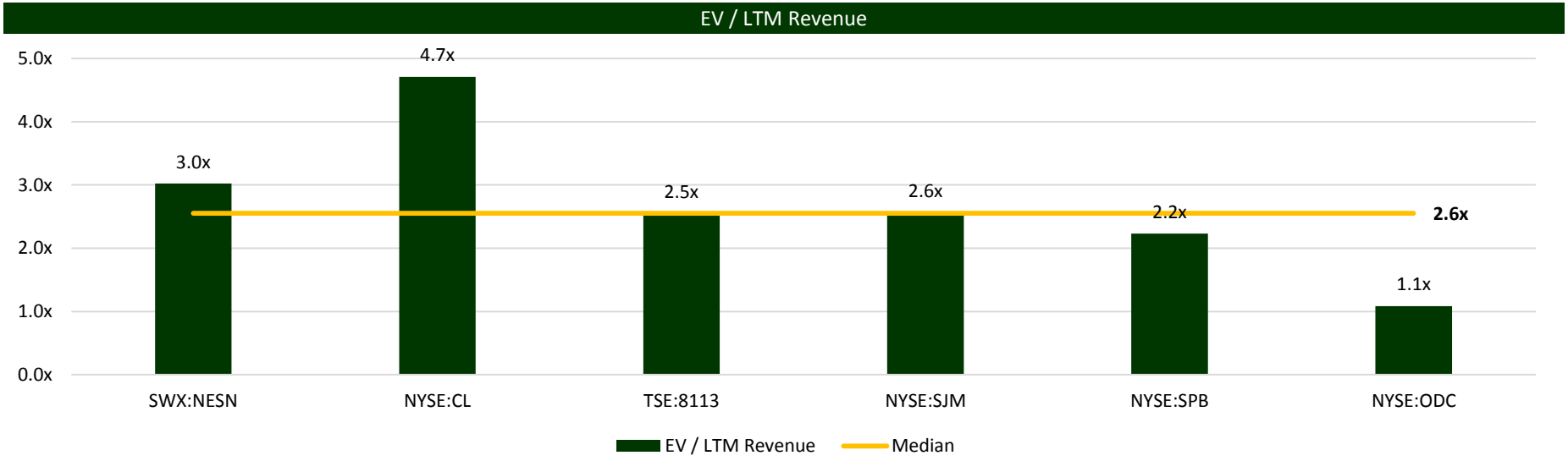


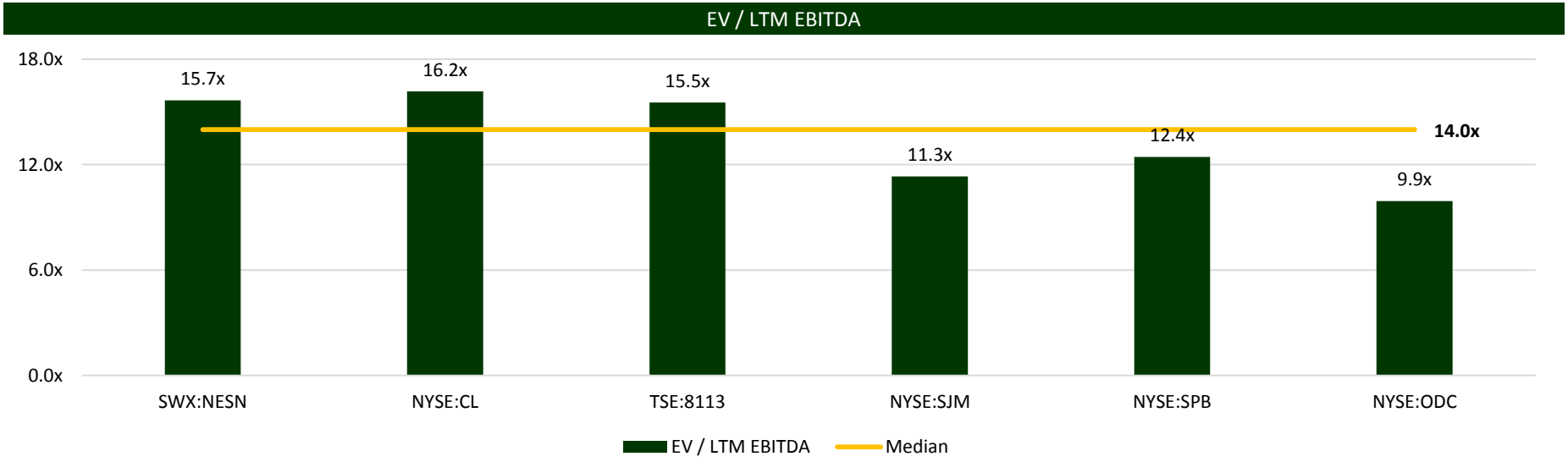


Source: CapitalIQ

Notes: (1) FRPT has relatively high valuation multiples due to its strategy to drive annual sales growth in excess of 20% through 2020, resulting in EBITDA margin of 20% compared to its LTM EBITDA margin of 5.5%

Public Comparable Companies – Consumer Products w/Pet Lines





Source: CapitalIQ

Select U.S. M&A Precedent Transactions

$ in millions

Select Active Strategic Buyers

Strategic Buyer	Acquisition Date	Select Corporate Acquisitions
Spectrum Brands Holdings, Inc.	04/28/17 01/20/15 09/23/14	• Petmatrix, LLC from Friend Skoler & Co. (a private equity firm) • Salix, LLC • P&G, Remaining European Pet Food Brands
Nestlé Purina PetCare Company	07/21/15 01/20/14	• Merrick Pet Care, Inc. • Performance Pet Nutrition, LLC
The J.M. Smucker Company	02/03/15	• Big Heart Pet Brands (Big Heart Pet Brands acquired Natural Balance Pet Foods, Inc. on 05/22/13)

Select Sponsors with Active Portfolio Holdings

Financial Sponsors (Portfolio Companies)	Acquisition Date	Select Corporate Acquisitions
Frontenac Company (Whitebridge Pet Brands: formerly known as Cloud Star)	04/18/17 01/06/15 07/16/14	• Arthur Dogswell, LLC (Arthur Dogswell acquired Natural Pet Products on 03/09/2015) • Tiki brands of Petropics Gourmet Whole Foods • Cloud Star Corporation
Graham Partners, Inc. (Bright Pet)	11/11/16 04/28/16	• Mercer Foods, LLC • Ohio Pet Foods, Inc.; Southern Tier Pet Nutrition, LLC; Blackwood Pet Food, LLC
Berwind Corp. (WellPet)	02/07/17 01/07/16	• Whimzees • Sojourner Farms, LLC
J.H. Whitney & Co. (C.J. Foods)	02/16/16 06/04/14	• Day Six Pet Nutrition, LLC • C.J. Foods, Inc.

Source: CapitalIQ

U.S. M&A Precedent Transactions from 2012 through 2017

$ in millions

Date	Target	Acquirer	Transaction Value	LTM Revenue	LTM EBITDA	EV / Revenue	EV / EBITDA
04/28/17	Petmatrix, LLC	Spectrum Brands Holdings, Inc.	$255.0	$75.0	-	3.4x	-
04/18/17	Arthur Dogswell, LLC	Frontenac Company; Whitebridge Pet Brands, LLC	-	-	-	-	-
04/04/17	Complete Natural Nutrition	Parkers Pet Provisions	-	-	-	-	-
03/28/17	Nature's Logic	VisioCap, LLC	-	-	-	-	-
03/24/17	Omnipet, LLC (dba “Petflow”)	Phillips Feed Service, Inc.	-	-	-	-	-
02/28/17	Gambol Pet Group Co Ltd.	KKR & Co. L.P.	-	-	-	-	-
02/07/17	Whimzees	Berwind Corp.; WellPet, LLC	-	-	-	-	-
01/10/17	Crosswind Industries, Inc.	Archer Daniels Midland Company	81.0	-	-	-	-
11/11/16	Mercer Foods, LLC	Graham Partners, Inc.	-	-	-	-	-
05/11/16	Nature's Variety, Inc.	Agrolimen SA	-	-	-	-	-
04/28/16	Ohio Pet Foods, Inc.; Southern Tier Pet Nutrition, LLC; Blackwood Pet Food, LLC	Graham Partners, Inc.	-	-	-	-	-
02/24/16	Texas Farm Products Co.	Kodo, Inc.	-	-	-	-	-
02/16/16	Day Six Pet Nutrition, LLC	J. H. Whitney Capital Partners; C.J. Foods, Inc.	-	-	-	-	-
01/07/16	Sojourner Farms, LLC	Berwind Corp.; WellPet, LLC	-	-	-	-	-
07/31/15	IMS Trading Corp.	Central Garden & Pet Co.	25.0	-	-	-	-
07/22/15	Harrison Pet Products, Inc.	Bosch Tiernahrung	-	-	-	-	-
07/21/15	Merrick Pet Care, Inc.	Nestlé Purina PetCare Company	-	-	-	-	-

Source: CapitalIQ

U.S. M&A Precedent Transactions from 2012 through 2017 (cont'd)

$ in millions

Date	Target	Acquirer	Transaction Value	LTM Revenue	LTM EBITDA	EV / Revenue	EV / EBITDA
04/02/15	Partner in Pet Food	Pamplona Capital Management, LLC	339.0	260.8	37.7	1.3x	9.0x
03/13/15	Manna Pro Products, LLC	Broad Sky Partners	-	-	-	-	-
03/09/15	Natural Pet Products	Arthur Dogswell, LLC	-	-	-	-	-
03/03/15	Protein For Pets	Undisclosed Private Equity Firm	-	-	-	-	-
02/03/15	Big Heart Pet Brands	The J.M. Smucker Company	5,769.2	2,266.5	319.5	2.5x	18.1x
01/20/15	Salix LLC	Spectrum Brands Holdings, Inc.	148.0	98.7	-	1.5x	-
01/06/15	Tiki brands of Petropics Gourmet Whole Foods	Frontenac Company; Cloud Star Corporation	-	-	-	-	-
09/23/14	P&G, Remaining European Pet Food Brands	Spectrum Brands Holdings, Inc.	116.0	193.3	-	0.6x	-
07/16/14	Cloud Star Corporation	Frontenac Company	-	-	-	-	-
07/01/14	Cat-Sip Real Milk Treats for Pets	PET-AG, Inc.	-	-	-	-	-
06/04/14	C.J. Foods, Inc.	J.H. Whitney & Co LLC	-	-	-	-	-
06/04/14	Scotts Miracle-Gro Company	Global Harvest Foods	-	-	-	-	-
04/09/14	P&G, Pet Food Brands (Lams, Eukanuba, Natura)	Mars Petcare US, Inc.	2,900.0	1,611.1	200.0	1.8x	14.5x
03/26/14	Three Dog Bakery	Undisclosed Private Equity Firm	-	-	-	-	-
02/10/14	Pet Carousel Inc.	Cargill, Incorporated	-	-	-	-	-
01/20/14	Performance Pet Nutrition, LLC	Nestlé Purina PetCare Company	-	-	-	-	-
12/04/13	Solid Gold Pets, LLC	VMG Partners	-	-	-	-	-

Source: CapitalIQ

U.S. M&A Precedent Transactions from 2012 through 2017 (cont'd)

$ in millions

Date	Target	Acquirer	Transaction Value	LTM Revenue	LTM EBITDA	EV / Revenue	EV / EBITDA
11/06/13	PetAg, Inc.	PBI/Gordon Corporation	-	-	-	-	-
06/20/13	Hare Of The Dog	Treat Planet, LLC	-	-	-	-	-
05/22/13	Natural Balance Pet Foods, Inc.	Big Heart Pet Brands	331.0	-	-	-	-
01/11/13	Phelps Industries, LLC	Wafra Investment Advisory Group	-	-	-	-	-
09/13/12	Sergeant's Pet Care Products, Inc.	Perrigo Co.	285.0	142.5	30.0	2.0x	9.5x
08/31/12	Petmatrix, LLC	Friend Skoler & Co., Inc.	-	-	-	-	-
08/21/12	Prestige Pet Products, Inc.	For The Earth Corp.	-	-	-	-	-
		Mean	$1,024.9	$664.0	$146.8	1.9x	12.8x
		Median	270.0	193.3	118.8	1.8x	12.0x
		Low	25.0	75.0	30.0	0.6x	9.0x
		High	5,769.2	2,266.5	319.5	3.4x	18.1x

Source: CapitalIQ