

Investing into Slow Moving Consumer Goods

Globalization at a turning point?



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Executive Summary

The rising wealth of the BRIC countries has changed the global value chain – vertical integration along all dimensions has entered the master plan

- The rising wealth of the BRIC countries (approx. 1.4 bn people entering the middle class between 2000 and 2020), in particular China, is challenging the consumer goods value chain along two dimensions: (1) rising demand (for consumer goods) hits limited supply of raw materials and (2) formerly established value chain relationships are being redesigned without any rules
 - Many raw materials have become strategic and a bottleneck. Rising prices and volatiles put pressure on (supplier) margins and question existing business models
 - Consolidated supplier industries regain strategic negotiation power, driven by additional/new demand from formerly untapped BRIC countries without established (quality) supply chains
 - Formerly export driven BRIC capacities are being redirected to satisfy domestic demand
- To remain part of the global game, there are five different key strategies companies start to follow resp. need to implement
 - Secure supply chain and win global fight for resources and technology through a strategic set of measures (e.g. backward integration, long-term supply contracts, partnering)
 - Compensate for higher supply cost through forward integration (cash-in part of the retail margin of products with high customer price sensitivity) or fully outsource production (OEMs) and switch to pure "Design & Sales" business model (retail margins give plenty of room to compensate for higher supply costs)
 - Switch business models to a "cost plus" logic (suppliers, products with limited customer price sensitivity)
 - Drive R&D/innovation to reduce dependency from limited raw materials (increase efficiency, switch from natural to synthetic materials, recycling, end-of-life product management, autarchy)
 - Develop and implement an international growth strategy to build a sustainable competitive position also in BRIC countries

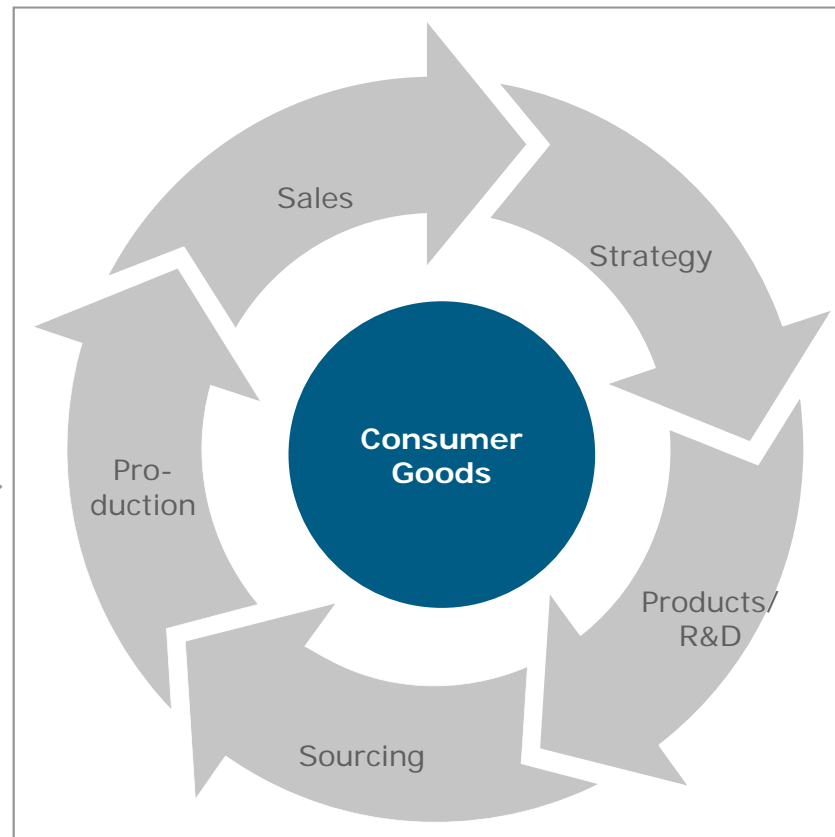
Consumer goods industry | Selected mega trends

The two mega trends (1) globalization through diminishing trade barriers and (2) shortage of resources combined with rising wealth challenge companies' business models

Shortage of resources

Key challenges:

- Avoidance of (physical) raw material bottlenecks
- Sourcing stability
- Innovation for technology/ material substitutes
- Change in business model



Globalization

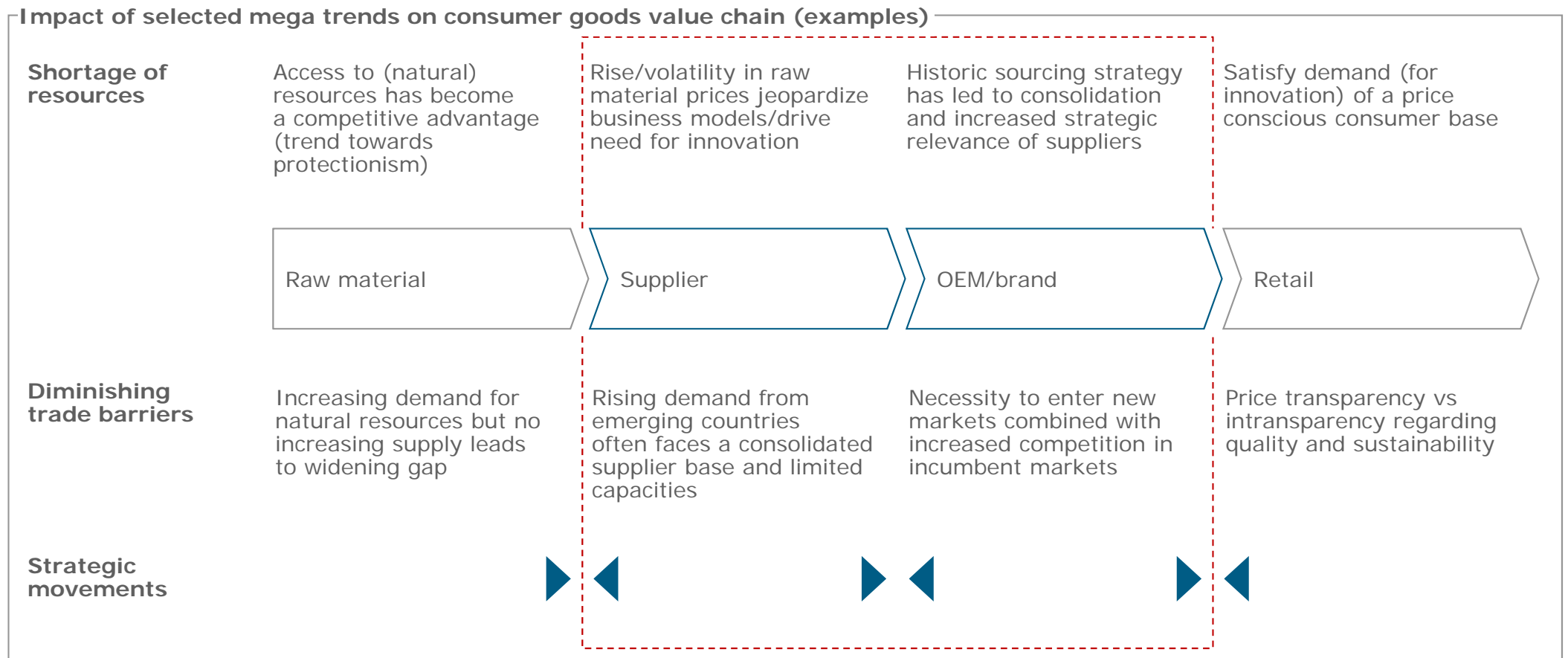
Key challenges:

- Internationalization
- New market entrants/ competitive environment
- Adaption of products to local requirements
- Secure intellectual property

These two mega trends influence the main corporate functions

Impact of mega trends on consumer goods value chain

Dramatically rising wealth in (BRIC) countries leads to increasing demand-supply-gaps along the value chain driving vertical integration strategies



Truly global fight for resources, technology and margins

Source: goetzpartners analysis

Case Study – Shoe industry

Global shoe industry plays all possible value chain models to counter supply chain challenges and increasing demand from BRIC countries

Changing industry dynamics

1. Shortage in leather supply

Demand for leather goods, shoe saddlery, upholstery, aviation and automotive is constantly rising over-proportionately to slaughtering the bovine population, mainly driven by BRIC countries and their growing demand for luxury goods. This is faced by an under-proportional development in beef consumption in BRIC countries (except for Brazil, pork, chicken and lamb are preferred).

From 2010-11 raw material prices for bovine leather increased up to 100%, even higher for other skins like sheep, goat and lamb.

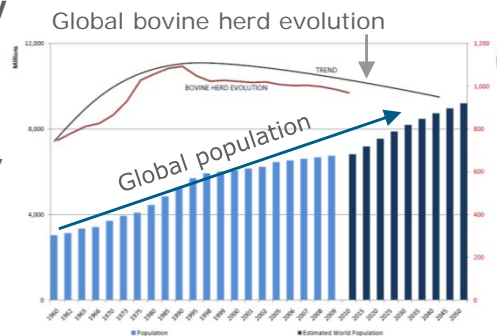
Skin is just a by-product of meat production, i.e. price increases do not compensate for constantly rising kettle production cost and fading margins.

2. Consolidated leather shoe supplier industry

Leather shoe industry has shrunk dramatically over the last 25 years. In Europe an estimated 80% of factories have vanished and partly been shifted to Asian countries.

3. Increased demand from new markets

Strong demand from local markets has increased attractiveness of domestic markets for Asian entrepreneurs, compared to export.



Challenges and selected trends

- Leather shoe industry is facing two key challenges:
 - Secure supply chain
 - Secure margin
- The shoe industry is reacting with a number of different strategies, depending on their value chain and price position.
 - Approx. 50 global players like Clarks, Ecco, Ara have built or own factories in Asian/BRIC countries, as well as own tanneries and in some cases even slaughterhouses in order to have control over rawhides (backward integration)
 - Retailers like the German Deichmann have integrated vertically backwards and bought a number of brands.
 - Less price sensitive luxury brands pass on raw material price increases or just bear higher prices as they hardly impact their margin
 - Midsize to larger industrial shoe brands (Clarks, Timberland, Ecco, Gabor, etc.) open own shops or point of sales to take some of the retail margin (forward integration)
 - Some cheaper brands transform into “very lean design and sales only” business models
 - Some brands move to non-leather and partly even explicitly promote “animal free” products



Case Study – Palm oil production and consumer goods manufacturers

European manufacturers purchasing raw materials from emerging countries can consider acquiring their suppliers to weather commodity price increases and address sustainability issues

Changing industry dynamics

1. Increasing consumer demand for palm oil

Palm oil is used in a large range of products from cooking oil to soap. It is the most affordable edible oil. Palm oil production has increased at 8% CAGR over the last decade to meet the demand growth driven primarily by China and India.

In 2010, the global demand for palm oil exceeded production by 2%, putting an upward pressure on prices. Demand is expected to grow at an average of 9% per annum in the next 3 years.

2. Limited agricultural land

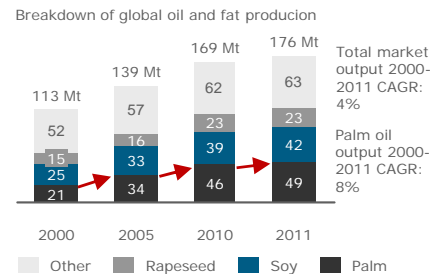
The global supply of agricultural land is limited. Any increase in use of land for one agricultural crop means a corresponding drop in use for another crop. Malaysia and Indonesia account for 85% of global palm oil production. Especially in Malaysia, agricultural land is increasingly being converted into land for property.

3. Sustainability issues

There is mounting concern about converting virgin rainforests into oil palm plantations, especially in Indonesia.

4. Increasing demand for ethanol

Brazil and US are increasingly converting food crops into ethanol to use as fuel, putting an upward price pressure on food prices.



Challenges and selected trends

- There are two key challenges for consumer good manufacturers using palm oil in their products:
 - **Crude palm oil price increase:** Average price increased 33% in 2010, putting a downward pressure on margins
 - **Sustainability:** Greenpeace, WWF and Friends of Earth are putting pressure on consumer companies to use palm oil from sustainable sources. Currently only ca. 9%¹ of palm oil is globally produced in a sustainable manner
- Consumer goods manufacturers which use palm oil in their products are responding to the sustainability challenge in a variety of ways
 - Some of the world's largest purchasers of palm oil such as Unilever have started to buy Green Palm certificates to signal their commitment to sustainability in their production. Green Palm certificates, however, do not guarantee that the palm oil actually purchased comes from a sustainable source
 - A better solution is to purchase palm oil from fully sustainable producers such as New Britain Palm Oil ("NBPO"), a palm oil producer in Papua New Guinea
 - It is conceivable that largest global purchasers of palm oil may need to acquire sustainable palm oil plantations to secure their raw materials and address sustainability issues
- On the other side, NBPO, opened a refinery in Liverpool, UK, in 2010 to supply sustainable palm oil to companies such as United Biscuits and Jordans

[1] RSPO certified

Source: goetzpartners analysis, broker reports, Factiva

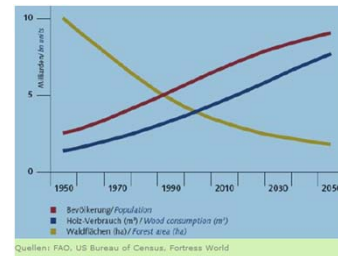
Case Study – Furniture and kitchen industry

The fast growing worldwide competition in wood markets forces furniture and kitchen manufacturers to tackle three major challenges: Innovation, supply chain and profitability

Changing industry dynamics

1. Shrinking forest area

The UN has calculated that global forest cover shrinks by 7.3 m hectares per year. That corresponds to an average annual loss of 0.2 % or 20,000 hectares a day. A particularly large amount of forest area has been cleared in recent years in tropical countries, especially Brazil, Indonesia and Sudan



2. Increasing wood demand from wood working industry

Over the last 15 years, the global demand for wood has increased by 60%. It is foreseeable that it will continue to grow dramatically, up to 8bn cbm by 2030. China alone is expected to double wood consumption by 2030

3. Increasing wood demand for energy production

Presently, more than 50% of global wood supply is used for energy production. To meet the implications from renewable energy policies in the EU, the gap of approx. 480 m cbm between supply (820 m cbm) and demand (1300 m cbm) in 2020 must be closed

Challenges and selected trends

- Due to the increasing demand and already visible shortage of wood raw materials, the global furniture and kitchen industry faces three major challenges:
 - Reduce dependency from wood raw materials through development of new technologies and production methods, e.g.
 - AirMaxx Worktops¹: 50% less timber and 30% less weight
 - Eurolux Doors²: Based on MDF, Honeycomb core
 - Secure supply with wood raw materials
 - Develop highly flexible sourcing strategies, since global wood trade will become more and more dynamic
 - Backward integration along the supply chain
 - E.g. Rauch Möbelwerke and Nolte kitchens have invested into own chipboard production
 - Steinhoff goes even further back the value chain and runs own forest land
 - Secure margin through forward integration into retail
 - Nobia took over kitchen franchiser Plana in Germany with 36 own stores, Hygena in France with 140 own stores and Poggenpohl with 35 own stores

[1] Nolte Küchen GmbH & Co.KG [2] Eurocomponenti SpA

Source: goetzpartners analysis, US Census Bureau, Fortress World, Mantau, Interviews with industry experts

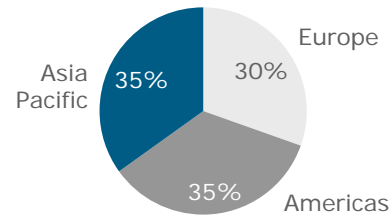
Case Study – White goods industry

Managing the supply chain risks has become a leading key success factor in the global white goods industry

Changing industry dynamics

Growing markets, globalization of manufacturing and supplier base as well as high-tech products have increased the supply chain risks

- The white goods market is driven by Asia-Pacific and other BRIC countries market growth: world-wide market volume CAGR 2005-2009 was 4.5% vs. Europe 2.6% and Asia-Pacific 4.9%
- Development of specific product ranges per geographical triad as consumption patterns differ fundamentally
- Due to cost pressure and sales development, white goods manufacturing footprint has moved to BRIC countries
- BRIC countries manufacturing footprint has fostered the development of a competitive BRIC supplier base
- Product ranges have extended including green products and product life-cycles have shortened, leading to higher supply variety followed by a higher complexity in spare parts management
- Use of noble earths has increased due to development of high-tech products
- Raw material costs have tremendously increased due to finite nature of resources and increasing financial speculation



Challenges and selected trends

- **Main trend is shift to BRIC countries:** for a leading white goods manufacturer, the BRIC share of the procurement volume has increased from 20% to 45% between 2005 and 2010
- **Mastering the identified supply chain risks has become a major task of supply chain management**
 - Manage global manufacturing footprint by completing economical reasons of choice with ecological and political reasons
 - Manage global supplier with best practice from supplier identification through qualification supplier down to supplier development processes
 - Consider logistics risks beyond working-capital-employed issues in order to prevent production fail-outs
 - Lower raw material dependence by increasing procurement implication during product development processes
 - Increase financial and natural hedging activities in order to lower supply risks on raw materials
- **Master non-identified supply chain risks: strengthen the resilience of the supply chain organization by focusing on**
 - Make/buy decisions with focus on supply chain risks
 - Modularity concepts in product development in order to increase redundancy
 - Latest possible customizing of final products in the supply chain
 - Manage supply diversity by opening multiple sources

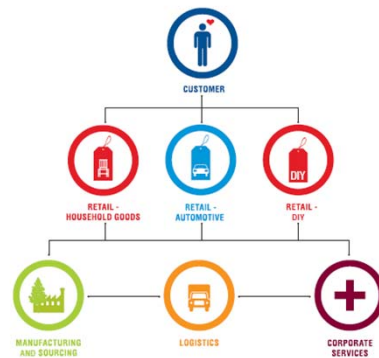
Source: goetzpartners analysis, Datamonitor

Recent M&A deal* case study | Steinhoff GmbH expanding in Europe

Steinhoff acquired Conforama, Europe's second largest furniture retailer, to forward integrate its operations and expand in Europe

Transaction overview

- Steinhoff is a vertically integrated furniture retailer listed on the Johannesburg Stock Exchange. Company's business interests comprise of furniture retail, manufacturing and sourcing, transportation and logistics services, motor vehicle retail and rental, and timber and other raw material supply
- Conforama is Europe's second largest furniture retailer after Ikea with 236 stores in 7 European countries, 186 of which are located in France (15% market share)
- Steinhoff acquired Conforama for €1.2bn in March 2011
- Conforama had ca. €3bn revenue and ca. €200m EBITDA in 2010, implying that the transaction valued the company at 6x EBITDA
- The acquisition transformed Steinhoff into Europe's second largest furniture retailer



Underlying rationale

- Forward integration: enhance Steinhoff's ability to retail its manufactured goods in Europe, particularly in France, where it was only a supplier



- Access to new markets: Steinhoff gains a strong retail footprint in France, Spain, Italy and Switzerland
- Product sourcing: Conforama gains access to Steinhoff's merchandising suppliers in Europe and Asia. There is also potential for scale procurement benefits
- Alongside integration of European logistics: reduce the costs of distribution for Conforama and Steinhoff
- Regional diversification
- Capitalise on Conforama's online sales channels

* no goetzpartners transaction

Source: goetzpartners analysis, MergerMarket, Factiva, broker reports

goetzpartners | Selected consumer goods projects

Selected case studies Corporate Finance

- Advised SchneeKoppe on its sale of a minority stake to Delvena Lebensmittel-Kontor
- Advised AXA Private Equity on its acquisition of Home Shopping Europe
- Advised REWE on its acquisition of the remaining 50% of the Joint Venture with Otto in Fegro-Selgros
- Advised Nutrition & Santé on the sale of its Infant and Baby Food division to Lactalis
- Advised Monoprix on its acquisition of Naturalia
- Advised Industri Kapital and Management Team on their acquisition of Gardena Holding



Selected case studies Management Consulting

- Development of a European market entry strategy for built-in kitchen appliances [leading Asian White Goods OEM]
- Various Commercial Due Diligences on furniture/upholstery manufacturers
- Internationalization strategy for a leading European manufacturer of kitchen and home appliances
- Supply Chain Globalization Programme for a leading kitchen manufacturer
- Best cost country sourcing project for a leading white goods manufacturer
- Securing Asian and Eastern European Supply Base for a leading white goods manufacturer

Source: goetzpartners

About goetzpartners

goetzpartners is a leading independent European consulting company that combines M&A (mergers & acquisitions) advisory and management consulting under one roof. With this unique service offering goetzpartners advises companies along their whole value chain, thus creating sustainable value for them. The Group is represented with offices in Munich, Düsseldorf, Frankfurt, London, Madrid, Moscow, Paris, Prague and Zurich, and maintains international cooperation ventures. goetzpartners Management Consultants concentrates mainly on the fields of strategy, operational excellence, and business transformation. goetzpartners Corporate Finance focuses on M&A advisory services. goetzpartners was classed a "Hidden Champion" 2009 in the fields of strategic due diligence, financial and merger strategies as well as post-merger integration (result of the latest "Hidden champion" study carried out by Professor Fink in collaboration with the magazine "Capital").

Service Line Strategic Due Diligence/Transaction Services

Transaction service advisory needs to go beyond pure deal making. It requires an in-depth knowledge of the target industry, its competitive landscape, trends and value levers. With our deep understanding their respective investment strategies, we have long-standing working relationships with all types of investors, i.e. Strategic Players, Private Equity, Venture Capital, Distressed Debt, and Hedge Funds. We offer our clients interdisciplinary teams combining industry, functional and process intelligence focusing on key value drivers to create highest possible impact.

Service Line Supply Chain Management

The goetzpartners supply chain model offers a clear and structured means of identifying and implementing strategic and operational optimization potentials along the product lifecycle, starting with issues such as integration of procurement and logistics into the new product development process to direct bottom-line cash and savings-generating issues, such as procurement cost optimization or working capital optimization. goetzpartners supports their clients generating substantial savings in their organization or with their suppliers, by an efficient and sustainable supply chain management

Industry Line Consumer Goods and Retail

goetzpartners provides assistance with acquisitions, divestitures and in attracting outside financing for restructuring and growth. In addition, we support our clients in strategically adjusting their value chain up to expanding, developing and implementing international growth strategies. Our attention to detail combined with our industry expertise and extensive network enables us to exceed the expectations of our clients on a regular basis.

Service Line Marketing & Sales

Our in-depth understanding of the challenges in our core industry sectors and the needs of their distributors and clients enables us to provide our clients with sustainable strategies along the entire value chain: from client acquisition to customer retention in the B2B, B2B2C and B2C markets. In this way, we play a huge role in the creation of sustainable value for the companies of our clients.

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Contact details

goetzpartners
MANAGEMENT CONSULTANTS
GmbH

Marc Staudenmayer – Managing Director
goetzpartners MANAGEMENT CONSULTANTS
Head of Supply Chain Management
Mobile +49 – 151 – 1714 1104
staudenmayer@goetzpartners.com

Michael Hommert – Partner
goetzpartners MANAGEMENT CONSULTANTS
Head of Strategic Due Diligence and Private Equity
Mobile +49 – 151 – 1714 1012
hommert@goetzpartners.com

Marc von Braun – Partner
goetzpartners MANAGEMENT CONSULTANTS
Head of Sales & Marketing
Mobile +49 – 151 – 1714 1005
braun@goetzpartners.com

Arnold Holle – Managing Director
goetzpartners CORPORATE FINANCE
Head of Consumer Goods and Retail
Mobile +49 – 151 – 1714 1106
holle@goetzpartners.com

Prinzregentenstraße 56
80538 Munich, Germany
Tel. +49 – 89 – 29 07 25 – 0

Königsallee 60 b
40212 Dusseldorf, Germany
Tel. +49 211 – 600 42 – 570

Bockenheimer Landstrasse 24
60323 Frankfurt, Germany
Tel. +49 – 69 – 2 47 50 48 – 0

32 Brook Street
London W1K 5DL, UK
Tel. +44 – 20 – 7647 7700

Gta. Rubén Darío 3, 3º
28010 Madrid, Spain
Tel. +34 – 91 – 745 13 13

Prechistsensky per. 14/1
119034 Moscow, Russia
Tel. +7 – 495 – 981 07 91

19, Avenue George V
75008 Paris, France
Tel. +33 – 1 – 70 72 55 00

Melantrichova 17
110 00 Prague 1, CZ
Tel. +420 – 221 632 451

Schwerzistrasse 6
8807 Freienbach
Tel. +41 – (0) 55 – 4102 294

www.goetzpartners.com