

Sector update

Pet care



Private equity and debt capital markets underpinning a sellers' market

The pet industry across the UK, Europe and the US is thriving. The increasing trend to humanise pets is leading owners to prioritise spending on veterinary care and to seek out pet products that support this trend. UK consumers alone are spending over £4.5bn a year on their pets, underpinning the growth of a range of businesses including specialist retailers, food and pet accessory manufacturers, and veterinary services. This highly fragmented sector is demonstrating growth and resilient consumer spending, making it attractive to both private equity and debt lenders.

Key observations

Private equity increasing investment

Many areas in pet care remain highly fragmented with opportunities for private equity (PE) to invest in growth platforms. Significant capital and the support of a competitive financing market are underpinning activity. Examples include Linnaeus Group, AniCura, Independent Vetcare and Medivet in veterinary services, and Armitage Pet Care in pet products.

Buy and build strategies

In many cases, strategic acquirers are prepared to pay a higher price for quality assets. Those that command the most attraction are specialist services including large animal diagnostics, technology providers and premium brands. Veterinary clinics that offer multidisciplinary capabilities are particularly sought after, with the ability to expand service offering whilst presenting buy and build opportunities. This was demonstrated by the recent acquisition of Davies Veterinary Specialists by Linnaeus Group.

Sustainable spending

A huge driver in this market is the growth in the humanisation of pets. The small outlay per item and potentially less discretionary nature of spend demonstrates the resilience of the sector through the economic cycle. With a plethora of healthier pet food options and health-conscious consumers extending their 'free-from' eating habits to their pets, we expect to see continued activity in this space, with opportunity for more innovative products to emerge.

New opportunities attracting attention

Increasing competition for assets and rising valuations mean some investors are starting to look at fast-growing ancillary markets such as pet insurance, practice solutions and analytics IT, grooming, nutrition, health biotech, devices and pet pharmacy businesses. The lifestyle of pets is becoming more sophisticated and so will the investment platforms.



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It's been an intriguing year in the pet market. Unlike in the past, we haven't seen the usual trend of one pet food company acquiring another, but instead it has been well-known manufacturers and marketers of human food decisively crossing over into the pet industry through purchases of iconic pet food businesses and brands. Even established pet market players are branching out into new segments of this lucrative industry.

SIMON PEACOCK,
PARTNER

How lenders are looking at the pet care sector

Many lenders are attracted to the sector's positive market trends and the favourable credit characteristics of speciality retailers, niche product manufacturers and veterinary services (see Figure 1). They are supporting private equity investment and acquisition activity across the sector with a range of capital structures.

- Crescent Capital provided the unitranche funding to support Rutland Partners' acquisition of pet product specialist Armitage Pet Care
- EQT Partners' acquisition of Independent Vetcare was supported by £250m of facilities provided by a range of senior lenders including HSBC, SEB, SMBC, Bank of Ireland and Royal Bank of Scotland
- Alcentra provided unitranche term debt to support Sovereign Capital-backed Linnaeus Group's acquisition of Village Vet. Investec later provided additional super senior facilities to the combined group to further support their growth.

Figure 1: How lenders are assessing the pet sector
Introduction

<p>SPECIALTY RETAIL CREDIT POSITIVES</p> <ul style="list-style-type: none"> • Less discretionary nature of spend • Highly resilient segment in UK retail • Integrated offering of other higher margin services, for example vet and grooming 	<p>NICHE PRODUCTS – FOOD AND ACCESSORIES CREDIT POSITIVES</p> <ul style="list-style-type: none"> • Positioning typically in premium end of market, favourable due to strong growth • Typically sticky customer base • Strong margins throughout niche markets • Online exposure 	<p>VETERINARY AND OTHER PET SERVICES CREDIT POSITIVES</p> <ul style="list-style-type: none"> • Highly resilient • Non-discretionary spend • Very sticky customer base • Strong buy and build opportunity • Economies of scale
<p>CREDIT FOCUS AREAS</p> <ul style="list-style-type: none"> • Financial performance through the cycle • Margins, cash generation and rent obligations • Brand strength and differentiation • Competitive position / threats • Online position 	<p>CREDIT FOCUS AREAS</p> <ul style="list-style-type: none"> • Customer concentration and relationships • Competitive position and differentiation • Exposure to raw material costs and foreign exchange (FX) movement • Supplier concentration / barriers to entry • IP ownership and brand strength 	<p>CREDIT FOCUS AREAS</p> <ul style="list-style-type: none"> • Overly ambitious roll-out • New entrants into market, for example specialty retail offering co-located vet and grooming services • New entrants into more commoditised higher margin services
<p>ACHIEVABLE LEVERAGE: 2.0x-3.0x*</p>	<p>ACHIEVABLE LEVERAGE: 3.0x-4.5x*</p>	<p>ACHIEVABLE LEVERAGE: 5.0x+++*</p>

Recent pet and vet related debt transactions

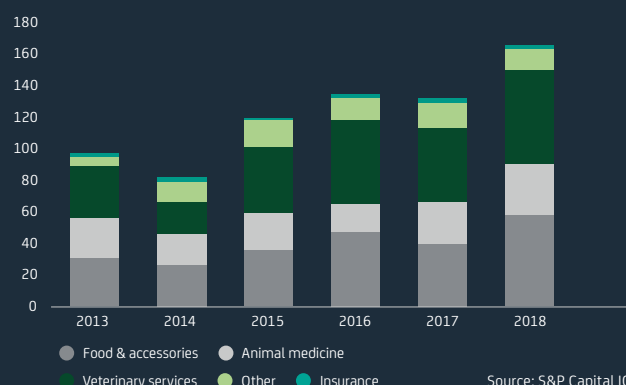
COMPANY	SPONSOR	LENDER	DATE	AMOUNT
VetPartners	BC Capital	Ares	2018	£420m
Jollies	Kester Capital	HSBC	2018	ND
Independent Vetcare	EQT Partners	U/W	2018	£150m
Lintbells	Inflexion	ND	2018	ND
Armitage Pet Care	Rutland Partners	Crescent Capital	2017	ND
Linnaeus Group	Sovereign Capital	Investec	2017	ND
Village Vet ⁽¹⁾	Sovereign Capital	Alcentra	2017	ND
MPM Products	ECI Partners	HSBC	2016	£10m

* As an EBITDA multiple

1 Village Vet is part of the Linnaeus Group

Source: Company websites

Figure 1: M&A volumes increasing across pet care



CASE STUDY: JOLLIES – DEBT-FUNDED MANAGEMENT BUY-OUT

Founded in 1935, Jollies is the UK's second largest pet retailer with over 70 superstores and concessions. It sells pet products and services, and has expanded its offering to include grooming and veterinary services in store.

Kester Capital wanted to secure lending to support the acquisition of Jollies and implement the management team's business plan.

UK retail is not currently favoured by lenders. However, the overall market backdrop of the sector and the quality of both the Kester Capital business plan and the management buy-in team provided material credit support to outweigh concerns over UK consumer spending.

We achieved a flexible and durable market-leading lending package with HSBC.

Private equity – scale through consolidation

PE continues to be an important investor across the sector, attracted to the combination of organic growth and consolidation opportunities in a fragmented and recession-resilient sector.

Veterinary practices in the UK are largely independently owned and operated by individual vets. PE are acquiring strong platforms and growing these rapidly to achieve economies of scale, for example, by investing in professionalising drug procurement and funding multiple acquisitions in premium locations.

- Examples include Linnaeus Group, the veterinary group established in 2014 following Sovereign Capital's platform investment in Willows Veterinary Centre and Referral Services; EQT Partners' acquisition of pan European provider Independent Vetcare from Summit Partners; and Inflexion Private Equity's acquisition of Medivet.

As demand for veterinary practices grows, it is likely that valuations will rise and PE will increasingly look to ancillary markets with high levels of growth such as pet insurance, grooming, accessory products, pet nutrition and medicine. For example, Inflexion's investment in pet nutritional supplements producer Lintbells will be used to develop new products, accelerate international expansion and gain scale in a fragmented market.

Rising spending on premium food and accessories

The UK is the second largest pet market globally worth £4.5bn, with UK sales of dog food worth £1.1bn and UK sales of dog treats worth £487m in 2018. The demand for pet food and treats which emphasise wellbeing and nutritional benefits using high quality ingredients is rising.

Brands such as Piper-backed Barking Heads are gaining market share and high levels of customer loyalty through continued investment in brand marketing, international expansion and developing their e-commerce platforms.

Unlike the major FMCG players, PE is prepared to invest early in the lifecycle of innovative brands. Secondary and even tertiary buy-outs are common as specialist investors use their skills to invest in brand marketing and product development, and to professionalise the underlying business. Nestle's recent acquisition of tailor-made dog nutrition business Tails.com marks the first acquisition by a major player of a direct-to-consumer pet food producer. Tails.com was originally backed by venture capital fund Draper Esprit.

PE has a successful exit track record

The last few years have seen a number of successful exits to financial investors and strategic acquirers to support future growth.

- Summit Partners acquired Independent Vetcare from August Equity and tripled EBITDA before exiting to EQT. Cinven's recent acquisition of Partner in Pet Food from Pamplona followed Pamplona's €315m acquisition of the business from Advent International.
- Mars Petcare, a serial acquirer in the US, is using its recent acquisitions of Nordic Capital-backed AniCura and Sovereign Capital-backed Linnaeus Group to gain access to the European and UK markets. Both deals are significant and represent two of the largest transactions in the sector the AniCura exit was an estimated 7x EBITDA return for Nordic Capital.

CASE STUDY: ARMITAGE PET CARE – ACQUISITION

Rutland Partners made a significant investment to back the £44m buy-out of Armitage Pet Care. We advised on the buy-out and debt raise.

Armitage Pet Care is a leading UK brand name in fun and indulgent treats for dogs and cats. It manufactures and sources a wide range of products from treats through to toys and accessories for cats, dogs and small animals, sold under a variety of well-known brands.

Our M&A role encompassed advising Rutland on bid tactics, deal structure and entry pricing. Rutland was also keen to raise unitranche debt to help maximise returns and cashflow flexibility. Our sector insights, robust business planning support and rapport with management were crucial in helping Rutland evaluate the future business opportunities supporting their offer price and overall investment structure in the business.

Selected private equity investors with pet-related portfolio companies














Private equity investor	Investment date	Select acquisitions	Business area
AAC Capital	2016	Yarrah	Organic dog and cat food
August Equity	2018	Hallmarq Veterinary Imaging	Veterinary services
	2015	Pet Cremation Services	Pet cremation
BC Partners	2018	VetPartners	Veterinary services
Bridges Ventures	2013	The Vet	Veterinary services
Cinven	2018	Partner in Pet Food	Pet food manufacturer
EQT	2016	Independent Vetcare	Veterinary services
	2014	Evidensia	Veterinary services
ECI	2016	MPM	Natural pet foods

Private equity investor	Investment date	Select acquisitions	Business area
Inflexion	2018	Lintbells	Nutritional supplements
	2017	Medivet	Veterinary services
	2016	Kynetec	Market data to the agriculture and animal health market
Piper	2017	Pet Food UK	Natural pet food
	2015	Forthglade	Natural wet food
Rutland Partners	2017	Armitage Pet Care	Pet treats and accessories
Waterland Private Equity	2016	United Petfood	Dry cat and dog food

Source: Company websites

Selected deals









Pet care

  THE PET SUPERSTORE ACQUISITION FINANCING 	  MBO 	  Passionate about animal care PLACING 
  SALE TO 	  SALE TO 	  ACQUIRED 

Other Consumer

  SALE TO 	  MITSUI & CO. ACQUIRED 	  innovative british chocolate SALE TO 
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