

Making Australian Food & Beverage Businesses more Valuable

- East Asian Opportunities

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Opportunities in East Asia

This is the latest in Strategic Transactions' occasional series of insights on growing the value of an Australian food manufacturing business. These insights are produced against a background of rapid global shifts. Such insights are designed to help business owners make their businesses more valuable, investment friendly or attractive to an acquirer.

This insight is based on transacting with East Asia, encompassing the rapidly developing Chinese food sector. David Thorn, the CEO of Darway Pty Ltd. is one of Australia's most experienced agribusiness practitioners and Asian deal makers.

David Thorn

CEO of Darway



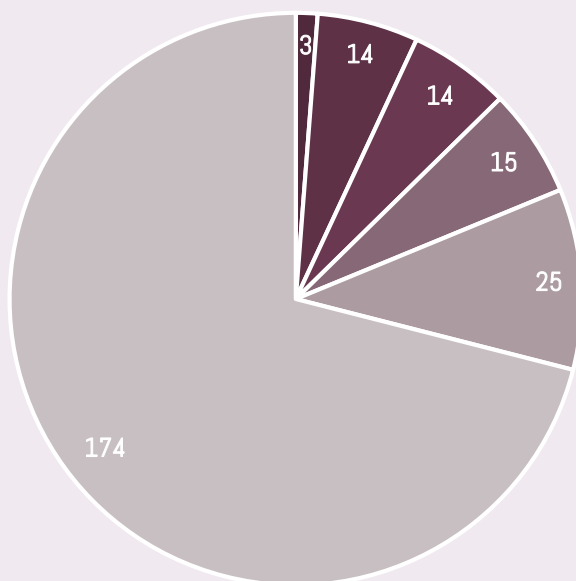
Overview

The Australian agricultural industry is highly dependent on exports – 58 per cent of total food produce is sold overseas, of which East Asia is a significant part. Asian companies are diversifying their Australian portfolios from traditional sectors such as mining and property towards food and beverages.

Australia is China's 6th largest supplier of food (behind the United States, Brazil, Canada, Argentina and Thailand) with exports valued at A\$5.3 billion in 2016. The value of Australian exports of processed foods increased by an average more than 40 percent between 2015 and 2016.

Nonetheless Australian businesses represent only a small proportion of East Asian food & beverage acquisitions, with only 15 of the 245 acquisitions in 2017 being of Australian entities, compared to 9 of the 274 acquisitions in 2016.

FOOD & BEVERAGE ACQUISITIONS
(by region) by EAST ASIAN
BUSINESSES - 2017



■ New Zealand - 3	■ USA - 14
■ Rest of the world - 14	■ Australia - 15
■ Europe - 25	■ East Asia - 174

What attracts East Asian Buyers to Australian F&B?

Three primary factors attract East Asian acquirers:

1. Food safety has been a significant problem in East Asia from melamine being discovered in baby formula in China, fake eggs in Malaysia to copper chlorophyllin found in olive oil in Taiwan. In past interactions with East Asian investors, David emphasised how “they are so keen on Australia’s clean, green, safe and plentiful image that they are willing to invest to get access to that.”
2. East Asia’s rising middle class and concurrent dietary changes have made the view Australian produce more favourably. Wagyu Beef is popular in restaurants, hotels and supermarkets in East Asia. A survey by AT Kearney suggests over 80% of Chinese consumers surveyed are willing to pay extra for safe food. This provides an opportunity for Australian business to market their clean, safe image and charge a product premium. David’s message for Australian companies is *“don’t think of yourselves as part of the food bowl for Asia. You must think of yourselves as the gourmet deli for Asia and continue to charge a premium for what you’re producing. Don’t sell your brand short because Brand Australia is arguably the best globally.”*
3. Another attraction is the Free Trade Agreements. Australia has trade agreements with China, Japan, Korea, Malaysia, Singapore, Thailand and other ASEAN countries delivering more opportunities for Australian companies. Australian products can be sold more cheaply due to lower tariffs allowing them a competitive edge over other nations.



Which industries are of primary interest?

- The beef industry has seen growth both domestically and internationally and it will continue to grow. With Wagyu beef already becoming part of the East Asian diet, it opens opportunities for other premium priced products. David noted when recently visiting the East Gippsland region of Victoria that *"you got a genuine sense that, over the past few years, there had been a movement away from dairy into beef farming."*
- However, dairy continues to be of interest to East Asia. Export of dairy products have offset the domestic slump. David considers that Australia has a large role to play in the export of high value dairy products including cheeses, yoghurts and infant formula.
- The horticulture sector is enjoying quite strong support at the moment in terms of domestic and international investment. Although it's a highly fragmented sector, *"there's a lot of small businesses that are operating in the sector, but that consolidation opportunity is now being played out quite broadly across a whole host of different fruits, vegetables and nuts."* While industry margins have been shrinking, consolidation has resulted in increased profits.
- Seafood is also of interest due to it being an alternate source of protein. David believes, *"it will become front of mind for more investors in the future as it is a very efficient form of protein. For example, a cow needs to consume 8 kilos of grain or fodder to produce 1 kilo of additional weight. In case of seafood, the ratio is one-to-one"*.



Austrade Data: Export Opportunities

Overall, Austrade lists the main export opportunities to China in the following product markets:



Milk powders



UHT and pasteurised milk,
cheese and butter



Seafood



Fresh fruits



Wheat and barley



Chilled or frozen meat



Processed foods



Australian Government

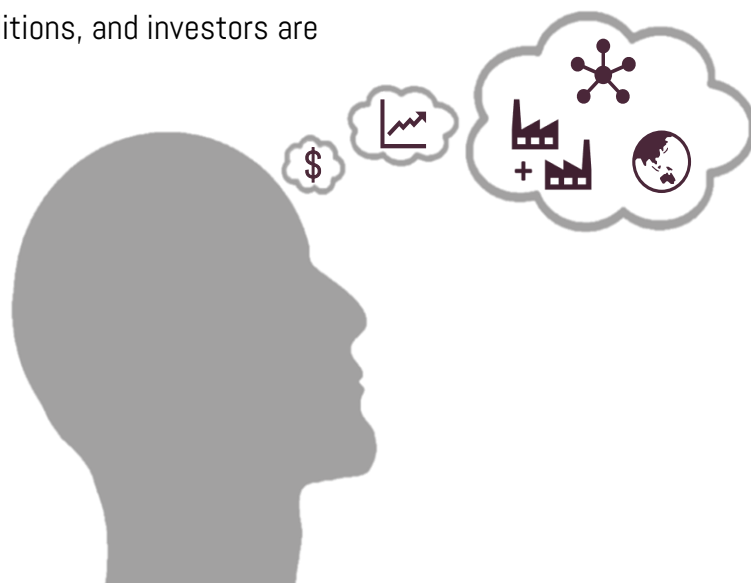
Australian Trade and Investment Commission



What motivates East Asian Acquirers?

The main factors listed for acquiring and managing Australian agribusinesses include:

- Consistent growth of 5% to 10% per annum of rural land values combined with the operational returns from its primary produce.
- East Asian investors are reliant on the expertise and experience that Australian food and agribusiness managers deliver. This is particularly relevant within Australia's huge landmass with varied climate and growing conditions, and investors are cognisant of the value of technology to mitigate risk and increase yield.
- Acquirers and investors need to be seen to be ethical about their investment philosophy and don't want to be viewed as coming in and buying up huge swags of land. They show a preference for co-investment.



In order to facilitate the best acquisition and / or investment opportunities, David believes there are three areas that Australian agribusiness owners seeking acquisition interest from East Asian businesses need to focus on:

- Have a compelling product that attracts premium pricing and can differentiate (and protect) itself in the market.
- Ensure you have the capital and patience required to succeed internationally.
- Do your research on a variety of routes to market and be aware of downside risks when exporting.

Recent Acquisition Analysis

Product Expansion & Diversification

Product expansion & diversification was the motivation for several acquisitions in 2017. This was the most common for transactions in the food services space where private equity firms have been looking to invest in and grow mid-market businesses.

Much of the product expansion was driven by access to intellectual property (IP). David worked recently with an Australian sugarcane producer that had attracted investment from an Indonesian strategic investor. The investors' primary motive was to get access to the technology and farm management expertise utilised by the investee in Australia thereby improving the efficiency of their Indonesian operations.



Recent Acquisition Analysis

Economies of Scale

Economies of scale and obtaining market share combined was the motivation for several acquisitions. Most were by Asian companies which already have a presence in Australia and wanted to expand that presence as a countermeasure to shrinking margins.

Agrocorp International Pte Ltd, the Singapore-based global agriculture commodity trading house, has acquired Associated Grain Pty Ltd, the Australia-based processor of pulses and seeds, for an estimated consideration of AUD 25 million.

The transaction is in line with Agrocorp's strategy to expand its processing business and access more of the value chain. The transaction will balance Agrocorp's operations allowing it to procure grains directly from Australian farmers as well as supply them with seed ahead of the planting season.

Geographic Expansion

Geographic expansion was the motivation for several acquisitions. Australia provides security for investment given the rule of law that prevails and its proximity to Asia make it a lucrative option for East Asian countries.

Legend Holdings Corporation, the China based conglomerate acquired family-owned Australian seafood company Kailis Bros. Legend Holdings was looking to expand into Australia for its strong market economy and stable business environment.



Contributors



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David Thorn is the founder and CEO of Darway Pty Ltd. David works with companies to help grow their businesses in domestic and international markets via trade and investment. David also arranges debt finance for his clients and undertakes equity investments (as principal or agent).



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Mark Ostryn is the founder and CEO of Strategic Transactions. Mark's focus is to transact the sale or acquisition of a business at the optimal value and terms for the owner. This involves detailed market search, financial decision support and project management throughout the transaction.

Strategic Transactions

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