Baker McKenzie.

2018

GLOBAL TRANSACTIONS FORECAST

Consumer Goods & Retail

A BAKER MCKENZIE SECTOR REPORT

Shift to online shopping, rising demand for natural and sustainable products, and industry consolidation to drive deal activity in 2018.

It's nearly impossible to talk about M&A trends in the consumer goods and retail sector without mentioning Amazon's acquisition of Whole Foods. At US$13.7 billion, it was far from the largest transaction in 2017, but significant because of its implications for the future of retail. The acquisition gives the tech giant a large physical presence in the grocery sector, through which it can use its expertise to re-cast how consumers shop for core lifestyle products such as food and drink, while at the same time exploiting increasing consumer demand for natural and organic produce.

"The way we shop has probably changed more in the last five years than in the last 50," says Alyssa Gallot-Auberger, chair of Baker McKenzie's Global Consumer Goods & Retail Industry Group. "The new consumer often uses a physical shop as a place to have an experience rather than a place to buy things."

The "new consumer" is connected, global, and mindful about the origin and sustainability of the products and services they buy. They primarily shop online, and their buying decisions are influenced by what their friends and celebrities "like" on social media.

As more of these new consumers go online to purchase everything from clothes and electronics to household supplies and organic vegetables, transactions in the consumer sector are likely to continue rising. Digitization and consolidation within the industry drove M&A activity in 2017, pushing transaction values to a total of US$543.2 billion.

> "The way we shop has probably changed more in the last five years than in the last 50. The new consumer often uses a physical shop as a place to have an experience rather than a place to buy things."
>
> **ALYSSA GALLOT-AUBERGER**
>
> Chair, Global Consumer Goods & Retail Industry Group

As these trends accelerate amid a stronger global economy, we forecast consumer transactions to rise further to US$632.6 billion in 2018 — making consumer goods and retail the top sector poised for M&A growth this year, followed by financials and industrials.

"Even the big consumer companies that traditionally sell their products in the most part to wholesalers and large retailers are looking at acquisitions that can give them e-commerce platforms to move into the direct to consumer channel," says David Scott, an M&A partner at Baker McKenzie based in London.

GLOBAL CONSUMER GOODS & RETAIL M&A (US$B)						
2014	2015	2016	2017	2018	2019	2020
463	481	483	543.2	632.6	551.3	435

GLOBAL CONSUMER GOODS & RETAIL IPOs (US$B)						
2014	2015	2016	2017	2018	2019	2020
53.4	33.8	24.9	38.2	59.8	55.1	33.9

Source: Oxford Economics

An example is Unilever's reported US$1 billion acquisition of Dollar Shave Club, an online subscription service that sells razor cartridges directly to customers. Besides giving Unilever an established online platform for selling other products, Dollar Shave Club's new age advertising strategy gave rise to a large online following, with YouTube videos poking fun at how expensive shaving had become with big brand products. This is further illustration of how technology, in this case clever social media campaigns, is reshaping consumer buying habits.

Meanwhile, in the capital markets, the consumer sector was the most active by IPO volume in 2017, with 348 listings worth US$38.2 billion, up 37% over 2016. This year, we forecast consumer listings to accelerate further, rising nearly 60% in total value to US$59.8 billion.

Listings in Asia Pacific, particularly China, led the resurgence in the sector in 2017, where companies raised US$7.8 billion in capital. We expect this trend to continue as consumer and retail companies look to tap the expanding middle class, growing consumer markets, and rise of online shopping.

Consumer M&A in 2018: Key drivers

In 2018, we forecast M&A activity in the consumer sector to rise across all regions. North America will lead the pack, with transactions totaling US$304.4 billion, followed by Europe with US$178.6 billion, Asia Pacific with US$125.9 billion, Latin America with US$17.3 billion, and Africa and the Middle East with US$6.4 billion.

In addition to their quest for new technology and untapped consumer markets, retailers in North America are also pursuing acquisitions because financing is readily available and M&A is often an easier, faster growth strategy.

"There's still a lot of dry powder in the marketplace and an insatiable appetite for transactions," says Steven Canner, an M&A partner at Baker McKenzie based in New York. "What I expect to see in 2018 is a very competitive market with buyers vying for high-quality acquisitions because the money is plentiful and organic growth is not robust."

Sustainability has become another important factor in consumer buying habits, as millennials seek products that match their ethical but e-commerce lifestyles. This, in turn, is driving deals, as large global brands divest non-core assets to free up cash to chase smaller niche targets that match the new consumers' values.

> "There's still a lot of dry powder in the marketplace and an insatiable appetite for transactions. What I expect to see in 2018 is a very competitive market with buyers vying for high-quality acquisitions because the money is plentiful and organic growth is not robust."
>
> **STEVEN CANNER**
>
> M&A Partner, Baker McKenzie

"The new consumer cares about where the ingredients in their food and other products, such as cosmetics and skincare, come from, so traceability is more important than ever," Gallot-Auberger says. "And there is real pressure from consumers for businesses to be able to back that up with a factual narrative behind the product and its provenance."

This is particularly true in the skincare and beauty subsector, as well as in FMCG. Greek natural cosmetics brand Korres is a prime example. In December 2017, a Morgan Stanley-managed private equity fund and Chinese cosmetics distributor Profex acquired a 70% stake in the family-owned company for US$58 million to help take the brand from mainly niche European to global.

In Asia Pacific, we forecast M&A activity in the consumer sector to reach US$126 billion in 2018, up 21% over last year's total of US$104 billion. The predicted growth will be driven by rising GDP throughout the region, and retailers' pursuit of younger, increasingly internet savvy consumers.

"There is pent up demand that will drive deal activity, not just from strategics, but also private equity funds that are cashed up and have ample dry powder," says Brian Chia, an M&A partner at Wong & Partners, the Malaysian member firm of Baker McKenzie, based in Kuala Lumpur. "Private equity will be a key driver of deal activity in the consumer sector, as fund sizes get bigger and more focused on specific Asian markets."

Although outbound Chinese investment slowed in 2017 because of restrictions on capital outflow imposed by the Chinese government, those restrictions have since eased and Chinese acquirers are expected to regain their focus on targets in Europe and North America.

"Consumer remains one of the top sectors for outbound investments by Chinese companies that are looking for growth beyond the domestic market," says Tracy Wut, an M&A partner at Baker McKenzie based in Hong Kong. "Factors such as rising disposable income, the demand for high-quality branded products, and vertical integration in supply chains will all contribute to increased deal activity."

GLOBAL CONSUMER GOODS & RETAIL M&A BY REGION (US$B)

	2017	2018	2019	2020
North America	270.1	304.4	221.2	166.4
Europe	152.1	178.6	159.4	128.1
Asia Pacific	103.7	125.9	141.2	118.8
Latin America	13.4	17.3	22.9	17.6
Africa & Middle East	2.9	6.4	6.6	4.1

Source: Oxford Economics

"Private equity will be a key driver of deal activity in the consumer sector as fund sizes get bigger and more focused on specific Asian markets."

BRIAN CHIA

M&A Partner, Baker McKenzie

Consumer IPOs in 2018: Key drivers

Consumer activity is expected to drive the IPO rebound in 2018. Second only to the finance sector, it is set to accelerate by almost 60% on 2017. With household spending remaining strong globally, consumer companies should also benefit from positive market conditions.

This year, we forecast consumer listings to grow in total value to US$59.8 billion, up from US$38.2 billion in 2017. China remains the top destination for listing by consumer companies, which raised US$7.8 billion worth of capital in 2017.

"The projected increase of online shopping in China underscores the appetite of the Chinese consumer for what's new, including new share issuances."

ALYSSA GALLOT-AUBERGER
Chair, Global Consumer Goods & Retail Industry Group

"The booming IPO market there can be linked to the increasing strength of the Chinese consumer, together with the pure size of the market," Gallot-Auberger says. "The projected increase of online shopping in China underscores the appetite of the Chinese consumer for what's new, including new share issuances."

In Latin America, Brazilian retailer Atacadao's listing on the Brasil Bolsa Bacao (B3) stock exchange in Sao Paulo was the sector's largest in the world by value, raising a total of US$1.4 billion. Atacadao, the Brazilian subsidiary of French retail giant The Carrefour Group, embarked on the IPO to accelerate its expansion in Brazil, which is Carrefour's second-largest market after France.

The second largest consumer listing of 2017 was tequila maker Becle SAB de CV's listing on Mexico's Bolsa Mexicana de Valores, which raised US$910 million. The transaction was placed on hold twice in response to US President Donald Trump's threats to tax Mexican imports and pull out of NAFTA.

Cross-border IPOs in the consumer sector climbed sharply in 2017, both in terms of activity, which increased 60% to 40, and in deal value which rose 34% to US$4 billion. Chinese companies accounted for six of the top 10 cross-border deals in 2017, half of which listed in New York and half in Hong Kong.

The largest cross-border consumer IPO last year was Chinese logistic firm Best Inc.'s listing on the New York Stock Exchange. In the initial public offering, Best Inc., which is backed by Chinese e-commerce company Alibaba, raised US$518 million.

Beyond 2018

Following a peak in deal activity in 2018, we forecast that M&A and IPO transactions in the consumer sector will drop by 13% and 8% respectively in 2019 in line with a larger, worldwide trend of cooling deal activity in developed markets.

We forecast M&A values in the sector to drop to US$551.3 billion in 2019 and US$435 billion in 2020. After reaching a high in 2018, we forecast IPOs will decline slightly to $55.1 billion in 2019, before falling further to US$33.9 billion in 2020.

Looking forward, analysts predict the sector will continue to undergo increased consolidation and greater integration of traditional and digital retail to improve the online shopping experience for the new consumer. Innovation, especially across premium product lines, will remain a key theme through 2020 and beyond, particularly in the food and drink subsector.

— KEY CONTACTS —

Alyssa Gallot-Auberger
Global Chair, CG&R Industry Group
T + 33 1 44 17 53 61
alyssa.gallot-auberger@bakermckenzie.com

Steven Canner
M&A Partner
T + 1 212 626 4884
steven.canner@bakermckenzie.com

David Scott
M&A Partner
T + 44 20 7919 1989
david.s.scott@bakermckenzie.com

Brian Chia
M&A Partner
T + 60 3 2298 7999
brian.chia@wongpartners.com

Tracy Wut
M&A Partner
T + 852 2846 1619
tracy.wut@bakermckenzie.com