AlixPartners

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FOOD FOR THOUGHT

STRATEGIC ALLIANCES

FOOD FOR THOUGHT: STRATEGIC ALLIANCES

How can strategic alliances help traditional F&B players and start-ups adapt to seismic shifts in the industry landscape?

Innovation, availability and sustainability – these worldwide macro trends are redefining the food and beverage industry.

Today's consumer demands almost instant access to new, healthier products, produced sustainably and available – or delivered – at a level of convenience never before seen, and F&B players are scrambling to meet these needs.

Adapting to these new pressures can prove difficult, as start-ups stir up a challenging competitor landscape and add to growing financial pressures in the industry, where margins continue to be squeezed, sandwiched by economy private label products and agile start-up premium brands.

HUNGER FOR INNOVATION

Fuelled by emerging enthusiasm for health, wellbeing and sustainability in the F&B industry, consumers now expect brands to deliver a breadth and pace of innovation that meets their lifestyle needs – all at a price that they are happy to pay.

€147.2BN
Predicted market value of health and wellness in Europe by 2020[1]

Consumers are willing to pay a premium for food brands that emphasise transparency, natural ingredients and health benefits. Annual retail sales for health and wellness food product categories in the EU in 2018 grew to more than €145bn, according to Euromonitor.

However, the polarisation in high demand for economy products, as well as their premium counterparts, has left mainstream brands feeling the pinch. Agile foodtech start-ups respond quickly to these consumer trends, grabbing market share and attracting huge investment from venture capital. As much as €4.2bn has been invested in European foodtech in the past four years, which still represents only 16% of global foodtech investment during this period.

Digital transformation has also significantly disrupted the industry. As food-focused apps, online grocery services, foodtech companies and ready-to-eat products disrupt every part of the supply chain, large consumer goods producers – that traditionally invest much less in R&D than newer tech companies – are finding it difficult to compete.

<2% Average R&D spend of consumer-packaged goods companies[2]

This situation is particularly relevant in the EU, which typically invests less in R&D than other markets.

R&D PRIVATE INVESTMENT OF FOOD AND DRINK INDUSTRY AS PERCENTAGE OF OUTPUT[3]

0.65%	Japan
0.44%	US
0.39%	Norway
0.20%	EU
0.10%	Iceland

A MARKET UNDER PRESSURE

Despite F&B being the largest manufacturing sector in the EU with a €1 trillion turnover, consumer demand for entry-price products, increasing costs, tariffs, trade barriers, and global events such as Brexit are generating higher levels of economic uncertainty.

Slowing growth in Western markets and burgeoning retailer power has squeezed margins further. Retailers' heavy investment in the manufacture of private label products, processing, warehousing and distribution centres, allied to their logistics expertise and access to big data, presents a formidable opponent in the market.

In Europe, private label has reached nearly 50% of market share for certain product ranges and, in the US, private label products are projected to capture 25% of shoppers' dollars in the next decade. Consumer trust has grown in "own brands", with the expectation that retailers' products will be just as good as their branded competitors.

PRIVATE LABEL MARKET SHARE IN EUROPE, 2018[4]

47.1%	44.8%
FROZEN GOODS	CHILLED GOODS

Source : 1.Euromonitor; 2.FoodDrinkEurope; 3.Eurostat, OECD; 4. IRI.

STRATEGIC ALLIANCES: A VIABLE ALTERNATIVE?

So, how can F&B brands keep the competition at bay and profit from the huge opportunities now presented by changes in the industry?

Traditionally, large multinationals would look to mergers and acquisitions (M&As) as a viable alternative to investment in new product development. As a way into the health and wellbeing market segments, they might be willing to pay a premium to widen their product offering in this way.

However, this approach still represents a significant investment cost and the benefits tend to be long-term. As M&As also present a highly complex undertaking with an inherent risk of failure – at a hefty price – we now see a waterfall effect, where strategic alliances can present an attractive solution to the many challenges faced.

The attraction is clear. As a lower-cost, lower-risk alternative to traditional M&A activity, alliances can deliver a short-cut to product innovation compared with in-house R&D investment. They can also realise a host of mutual benefits for both parties throughout the value chain, offering far-reaching and transformative impacts on a company's future, not to mention their short-term bottom line.

A WATERFALL EFFECT

Consumer demand for innovation

Market pressures squeezing margins

Reduced margins = Less innovation

M&A replaces R&D

M&A risk

Strategic alliances

In this report, we analyse the benefits and pitfalls of strategic alliances, with real-world examples and contributions from prominent market players. We hope this report provides genuine food for thought.

WHY STRATEGIC ALLIANCES?

F&B companies are currently performing a balancing act. On one side, shifting consumer needs are forcing them to think more innovatively. Their customers want new and exciting products that align with an increasingly healthy and sustainable marketplace, but shifting their offering into healthier segments can require large investment.

On the other side of the F&B 'see-saw' is the pressure on margins that is limiting the financial reach of these companies and lowering the tolerance for risk.

With limits on available funds and a need to tap into the growth areas of healthy and ethical eating, traditional players are looking at alternative plans for adapting to this new market reality. At the same time, food start-ups are exploring the possibility of scaling up to seize the opportunities of new consumer preferences and are waking up to the possibility of allying with partners across the value chain.

C-suite perspective

"In the B2B arena, alliances are key in the food industry as companies are usually smaller and need these alliances to grow – this is particularly true when you want to move into new regions and channels."

Claudio Riva, CEO, Optima Group

STRATEGIC ALLIANCES OFFER A SOLUTION TO TWO KEY CHALLENGES

DEMAND FOR INNOVATION

PRESSURE ON MARGINS

Reduced cost – and reduced cost of failure

Strategic alliances enable companies to expand and diversify their offering without the need for a huge investment in infrastructure, such as supply chain support or manufacturing facilities. Identifying and securing a partner with the relevant capabilities enables significant cost savings. In addition, partnering with an established brand in a particular category will accelerate activities beyond the significant level of marketing and advertising spend required to build a new brand reputation. In a joint venture or strategic alliance, failure is likely to be much less costly than M&A activity, given the non-acquisitive nature of the agreement. Strategic partnerships are, by their nature, mutually beneficial. However, should things not work out as planned for one or both parties, separating is much simpler with this kind of deal. This significantly reduces the cost of failure.

Speed to market

Strategic alliances can deliver products to market quickly to respond to consumer trends.

A long period of internal R&D and new product development (NPD) incubation can prove a significant barrier to quickly identifying a trend and being first to market, ahead of the competition.

Strategic alliances enable companies to tap into existing technology or product synergies that can hugely accelerate innovation.

Try before you buy

Strategic alliances can enable brands to break into non-core markets, create short-term solutions or be used as test beds before a permanent acquisition or investment.

They allow CEOs to demonstrate success within a much shorter timeframe than M&As, and the potential always remains for acquisition if the partnership performance is positive.

Brand extensions

To aid innovation, manufacturers can improve their owned brands by becoming a brand umbrella in new categories, thanks to strategic alliances.

Sharing the profit pool

Profits can be much higher at the downstream end of the value chain, and strategic alliances enable both parties to agree a more balanced share in profits through this chain.

Critical mass

It is becoming more difficult for producers to enter the giant retailer space without critical mass. Strategic alliances can develop a level of scale that makes it easier to fight for that all-important retailer shelf-space.

Reach a broader base

Strategic alliances can enable businesses to tap into additional distribution channels, facilitating a secure, established expansion route to new markets.

TYPES OF STRATEGIC ALLIANCE

There are many different types of alliance, but broadly they are formed to help the partners enjoy some form of organisational, economic, strategic or political advantage. More companies are entering into strategic alliances to improve their competitive edge, move into growth areas or new markets, and help mitigate risk.

Strategic alliances are now a fact of life for many businesses, enabling companies to unite and take advantage of mutually beneficial opportunities. These could be between large traditional players from different markets that can share cultural expertise or provide access to well-established manufacturing sites and distribution set-ups. Smaller companies and start-ups can also use strategic alliances to gain access to the structural and logistical support of larger players, while offering an inroad to new growth areas in return.

Traditionally, alliances would be formed upstream. Procurement and distribution deals were often driving forces for partnerships, but now F&B innovation spans the entire value chain. From new product development, to procurement and supply chain agreements, as well as manufacturing arrangements to enter adjacent product categories and distribution deals, strategic alliances offer companies a flexible and effective tool for tackling a variety of challenges.

VALUE CHAIN	Procurement	Manufacture	Distribution	Sales & marketing

PROCUREMENT

Procurement is a more traditional arena for alliances, enabling companies to strategically manage the sourcing of raw materials and handle contracts and relationships with suppliers. Procurement deals are coming under increasing scrutiny as the transparency of supply becomes more and more important to consumers. Ethical sourcing, including use of blockchain technology, is forming a larger part of companies' thinking when approaching supply chain management.

CASE STUDY: PROCUREMENT

Burton's and Barry Callebaut

Towards the end of 2018, Barry Callebaut formed a strategic alliance with Burton's Biscuit Company for the annual supply of more than 12,000 tonnes of chocolate and compound. As part of the deal, Barry Callebaut acquired Burton's chocolate manufacturing assets, expanding its production into the UK. Barry Callebaut also has a partnership agreement with Unilever to provide the chocolate for its Magnum ice creams, enabling them to make long-term agreements with cocoa farmers. Through this it fosters more sustainable farming practices and improved livelihoods for cocoa farmers.

MANUFACTURING

Manufacturing alliances enable F&B players to quickly enter a new product segment without the need for infrastructure investment or R&D. They can also be simple ways to increase scale or enter new markets. Some deals can be a means of improving a company's carbon footprint by moving manufacturing closer to distribution. They can also enable companies to test a market before setting up their own manufacturing capacity once the market has been sufficiently developed.

CASE STUDY: MANUFACTURING & DISTRIBUTION

illycaffè and JAB

Responding to innovations in technology within the coffee industry – particularly home-owned coffee capsule machines – illycaffè has agreed a manufacturing and distribution deal with JAB to produce and distribute illy-branded Nespresso-compatible capsules globally, hugely expanding consumer reach. Production of illy-blend coffee will continue at the illy plant in Trieste, after which it will be sent to JAB's plant for encapsulation.

Meanwhile, JAB has added another premium brand to its portfolio, which also includes Jacobs Douwe Egberts and Caribou Coffee Company. Illy's consolidated revenue for 2017 was reported at €467m, while JAB has invested more than $58bn in mergers and acquisitions since 2012.

C-suite perspective

"Illy remains a 100% family-owned company run by managers. With JAB, we show that it is possible to make agreements with major players without being bought."

Massimiliano Pogliani, CEO, illycaffè

DISTRIBUTION

Distribution deals allow for expansion and access to new markets, enabling partners to tap into existing networks and cultural knowledge. Start-ups that lack broader market knowledge can also follow the trail blazed by others who are seizing the opportunities of developing health and wellness trends.

C-suite perspective

“You can look at it [the partnership] and you can say, ‘That’s my livelihood. That is stealing market share from me. That is attempting to sort of end my industry.’ And maybe that is the reflexive way to look at it.

“Or maybe you can look at it another way if you step back and say, ‘Wait a minute. What am I doing? What is my purpose? Why did I start an egg company? What am I interested in doing every day?’

“I think as folks engage in it a little more, away from just the quick headline, ...the interest is figuring out a way to build a better company, figuring out a way to sell more protein to more consumers, figuring out a way to sell more product to more consumers.”

Josh Tetrick, CEO, JUST

CASE STUDY: MANUFACTURING & DISTRIBUTION

JUST Egg, Eurovo and PHW Group

US-based company JUST found a prime partner in summer 2018 when it entered into a production and distribution agreement with Eurovo, Europe’s leader in packaged, pasteurised and dried eggs. Its vegan JUST Egg product will be manufactured by Eurovo in Europe, improving JUST’s global environmental footprint. Through the agreement, Eurovo will manufacture the product through its existing facilities, potentially under a different name, paying JUST royalties on sales. The European distribution will be carried out by German poultry producer PHW Group. This three-way partnership enables Eurovo to enter the vegan market without having to invest in developing its own product range.

CASE STUDY: DISTRIBUTION

Raisio and Dr. Schär

In early 2019, Italian gluten-free pasta manufacturer Dr. Schär entered into a strategic alliance with the Finnish low-cholesterol food company Raisio. As part of the deal, Raisio will have access to Dr. Schär’s established distribution networks in Germany, Italy, France and Spain. The deal does not allow Dr. Schär to distribute in Finland but will enable the Italian company to develop its existing distribution network by offering Raisio’s oat products. Both companies have clearly expressed ethical approaches that align well and allow them to exploit the growing trend for healthy eating.

SALES AND MARKETING / NPD

Sales and marketing deals are becoming more popular. They enable access to a greater share of the profit pool and align with consumer-packaged goods in more traditional areas of spend. These deals enable access to new market areas without the huge upfront investment in R&D and manufacturing capacity. They also enable the creation of new products in complementary segments that build on already established brands.

CASE STUDY: SALES AND MARKETING & MANUFACTURING

Unilever and Ferrero

Unilever has entered into a deal with Ferrero for the European manufacture and distribution of ice cream under the Italian company's Kinder brand. This is a huge partnership from two F&B giants, and one that has clear mutual benefits. Here, Ferrero has harnessed Unilever's expertise in the ice cream category to take its Kinder brand into attractive new non-core product territory, without the cost of developing its own frozen production capabilities. Unilever benefits significantly, too. It is able to add a hugely popular 50-year-old brand to its ice cream portfolio, which already includes the likes of Cornetto, Carte D'Or and Ben & Jerry's. This deal is part of Ferrero's push into adjacent product categories, with Nutella & Go! and Nutella B-Ready examples of new formats for well-known brands.

VIEW FROM THE MIDDLE EAST

Strategic alliances can offer an increasing range of benefits to local and multinational F&B players in ME markets.

The food and beverage industry in the Middle East is also experiencing change. After long periods of growth, regional players are facing a slowdown and are looking to adapt their offerings. Margins are shrinking and multinationals and local players are changing their business strategies and seeking alternative ways to grow.

Alliances have always existed in the Middle East but have almost solely focused on particular models of distribution. Traditionally, multinationals would link up with local players who would distribute other companies' brands, providing access to regional markets. The distributor would usually be the full representative of the multinational, but this is changing as Middle Eastern markets grow in importance. The region is becoming a greater focus for international brands. Multinationals are taking greater control of their activities in the Middle East, and thus reshaping their engagement model with distributors. They are outsourcing certain services to specialised operators that are able to provide better service at a lower cost – for example merchandising and third party logistics. This is reducing the role of distributors to a narrower logistics role.

In this context, these traditional alliances are evolving, with more sophisticated 'performance-based contracts' and new service-based pricing models.

MAINTAINING GROWTH

M&As have typically been seen as a source of growth and a way to expand product ranges, but finding the right opportunities has proven difficult. While the shift in consumer expectation is not as pronounced as in Western markets, there has been a move towards healthier and more convenient products. Against a background of governments imposing taxes on some unhealthy segments, this shift is likely to gain momentum. Local and regional players are well placed to seize the opportunity presented by these changing patterns of consumption but need to think strategically in order to take full advantage.

In the Middle East, M&As proved enduringly popular, despite showing little success. Now, however, new forms of alliance are emerging, offering a means of meeting the challenges facing both local and international players. For local manufacturers, distribution alliances could be hugely beneficial. They can provide the scale to compete effectively with market leaders, without the complexity of M&A. For multinationals, alliances offer a low-risk way of entering Middle Eastern markets, taking advantage of local knowledge and infrastructure without the timescale and complexity barriers represented by M&As.

BRIDGING THE GAP

Strategic alliances also offer a solution to the huge gap in introduction for new products in the Middle East. There are two aspects to this. First, the audience for new and healthier products is at an earlier stage of development and is affected by different models of consumption in the Middle East. This complicates product launches and has led to innovative companies shying away from ME markets, as the risk and size of audience do not justify large scale investment. The second aspect is the R&D gap, where local and regional players do not invest in innovation themselves as this is very cost- and time-intensive.

Strategic alliances offer an ideal tool for innovative companies looking to move into new regions, and local and regional players who need to diversify their product offering if they are to enjoy the benefits of these new growth segments. Taking advantage of combining with multinationals who enjoy established R&D knowledge and capacity can allow local players to create innovative product ranges that align fully with regional consumer preferences. Whether as a shortcut to innovation or a means of achieving scale without large investment, alliances could be of huge benefit to players from across the Middle East's entire F&B landscape.

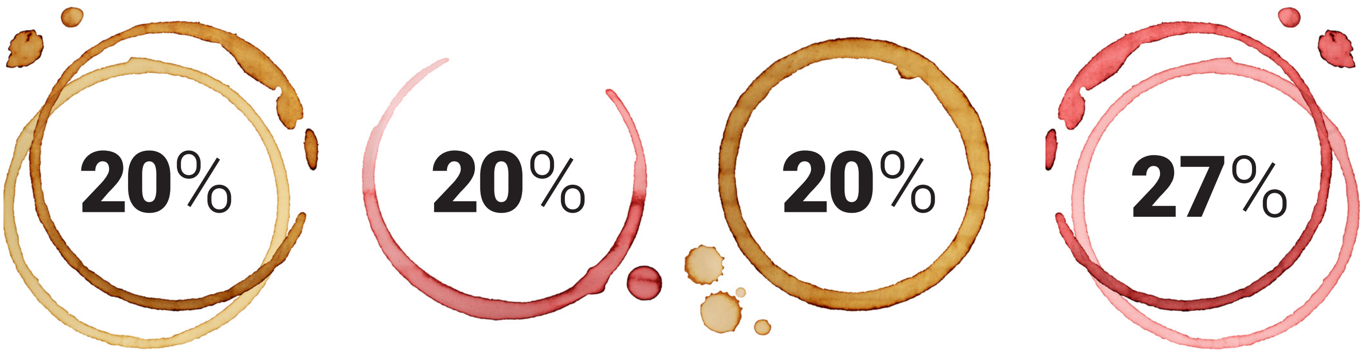
CASE STUDY: SALES AND MARKETING & MANUFACTURING

Al Safi and Danone

A long-standing example of a successful alliance in the Middle East is the 2001 partnership between Al Safi and Danone. A leading Saudi Arabian dairy company, Al Safi used its local taste and market knowledge to offer a broad range of dairy and fruit-based products developed using Danone's capacity for innovation and expertise. Al Safi pays royalties to Danone to use brand names, such as Actimel and Activia, and has been able to successfully localise the international company's innovations for the Middle Eastern marketplace.

STATE OF PLAY – EUROPE

The types of innovation from EU food and drink companies come in four main categories. (Note: This data is a percentage of all companies surveyed across 2012-14, so some companies may appear in two or more categories.)[1]



NPD
(product innovation)

MANUFACTURING
(process innovation)

DISTRIBUTION
(organisation innovation)

SALES AND MARKETING
(marketing innovation)

STATE OF PLAY – ITALY

Of the 13 partnerships AlixPartners identified in the past two years in Italy, more than half involved co-distribution elements to the agreements, as organisations look to expand their global footprint. Three-quarters involved either co-manufacturing or co-distribution elements.[2]

Distribution **54%**

Manufacturing **38%**

Sales and marketing **23%**

Procurement **8%**

(% of all alliances analysed by AlixPartners)

Source : 1.FoodDrinkEurope; 2.AlixPartners research and analysis, Italy, Feb 2017-Mar 2019.

THE VIEW FROM ITALY

In April, CEOs and other senior representatives from some of Italy's biggest food and beverage players gathered in Parma for the Food Summit 2019. AlixPartners surveyed 100 attendees during the summit, asking three questions on key issues facing the country's F&B sector.

Which of the options below do you consider critical to your company's success in the next five years? (Multiple choices selected)

44% New technology / digitisation

39% International expansion

32% New products / entry into new categories / innovation

24% Entry into new channels

6% Increase in market share in the domestic market

Where do you think strategic alliances could potentially benefit your business? (Multiple choices selected)

54% Supply chain *(logistics and distribution)*

27% Co-branding and co-marketing

20% Distribution abroad

16% Co-manufacturing *(sharing of different phases of the production process)*

13% Purchasing synergies

12% Gaining critical mass to leverage opportunity with major retailers

Which options do you consider the biggest hurdles in progressing with strategic alliances today? (Multiple choices selected)

48% Difficulty in clarifying and sharing goals between companies

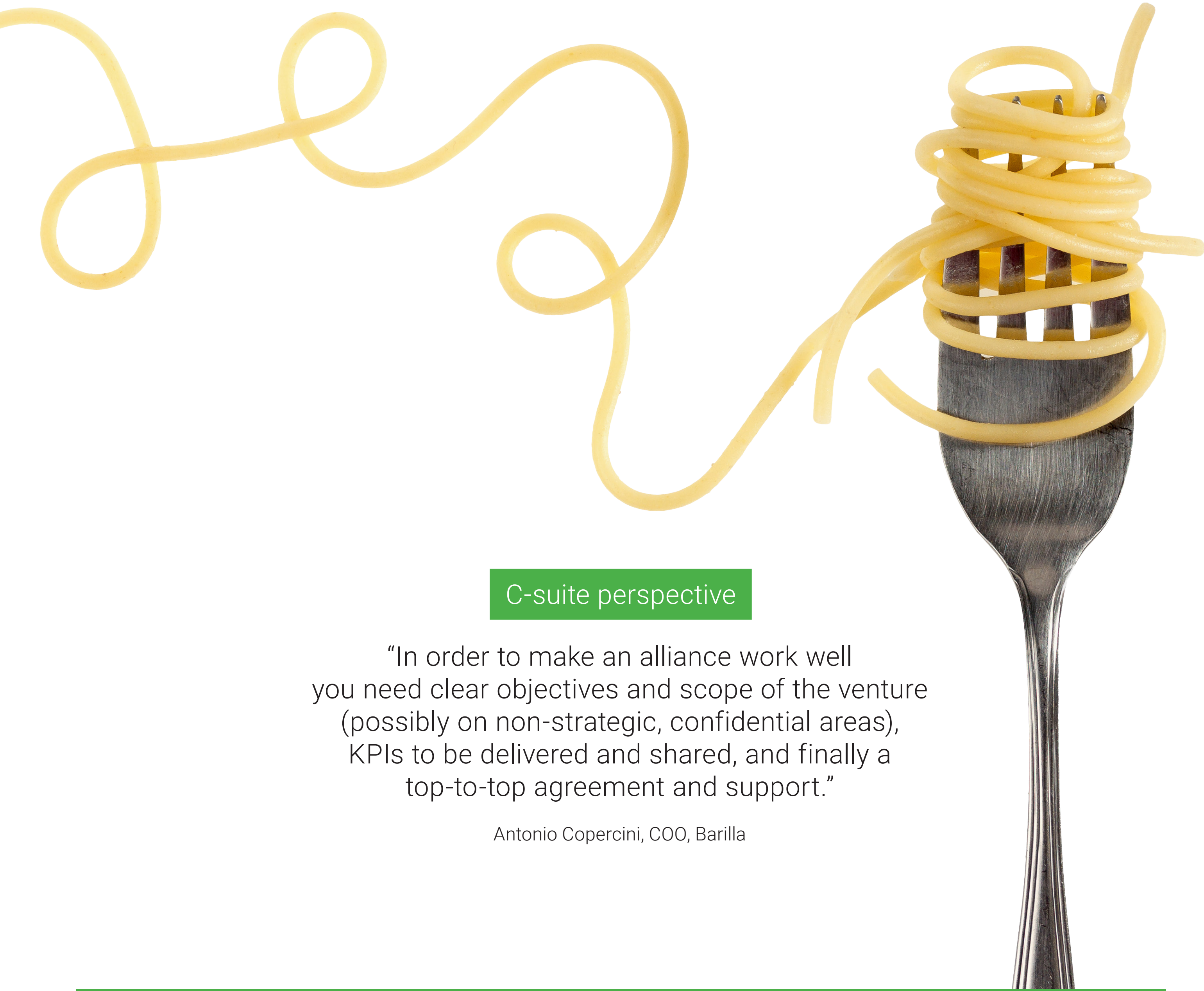
30% Difficulty in giving a substantial form to the alliances

27% Little openness of entrepreneurs

19% Finding the way to share financial earnings

19% Low capacity for working in teams on projects

Source : 1.AlixPartners interactive survey of 100 attendees at the Food Summit 2019, Parma, Italy.



C-suite perspective

"In order to make an alliance work well you need clear objectives and scope of the venture (possibly on non-strategic, confidential areas), KPIs to be delivered and shared, and finally a top-to-top agreement and support."

Antonio Copercini, COO, Barilla

STRATEGIC ALLIANCE CHECKLIST

HOW TO LOOK FOR THE RIGHT DEAL:
- Identify potential alliances based on company strategic development guidelines
- Map and select alliance partners
- Define and immediately exploit cost and revenue synergies.

HOW TO FINALISE THE AGREEMENT IN THE BEST WAY:
- Define the operational business arrangement and way of working
- Study the ideal form for the alliance (joint ventures, contractual agreements)
- Define the profit pool sharing and the resulting financial agreement.

HOW TO MANAGE THE AGREEMENT FOR SUCCESS:
- Ensure the right people are dedicated to making the partnership a success
- Create an active transformation office
- Agree robust KPIs to measure the success of the initiative
- Maintain constant tracking of the economic-financial data.

CONCLUSION – HOW ALIXPARTNERS CAN HELP

A successful alliance strategy must include four crucial elements:

- A business strategy which shapes the design of the alliance
- A dynamic view to guide the management of each alliance
- A clear approach to manage the alliance firms
- An organisational infrastructure to build and support the ability of the alliance.

SHAPING THE DESIGN

A clear vision of a company's strategic development forms the roadmap for arriving at the right alliance. Performing due diligence on potential partners before entering into an alliance is essential to getting the most out of any deal. This will also enable both partners to understand and profit from any short-term cost and revenue synergies that can be achieved, giving quick benefits that can form the platform for ongoing activity. A lack of clarity and consistency can be extremely detrimental to an alliance, and ensuring a well-defined and mutually understood financial and business direction is a solid basis for a successful deal.

A DYNAMIC VIEW

Both sides of an alliance should have a clear view of how the alliance is progressing, with the C-suite fully invested in supplying resource and guidance. This means well-defined KPIs, and ongoing measurement and analysis are needed to ensure that informed decisions are being made and responsibilities met. Strategic alliances benefit from their flexibility and even their temporary status. While representing a potential stumbling block if either or both partners have one eye on the exit, this flexibility is an advantage if management is actively involved in guiding the alliance.

A CLEAR APPROACH

Once agreement on the strategic and financial direction has been reached, the defined management view and responsibilities must be translated into a detailed and mutually-supported approach. A full business plan that outlines markets, clients, and share of the profit pool is fundamental to a strategic alliance's success.

GET ORGANISED

Forming an active transformation office that offers centralised structure and guidance can be the difference between victory and failure for a strategic alliance. Many companies have a dedicated M&A resource, but do not have an equivalent for strategic alliances. Embedding this capacity internally isn't viable for everyone, but setting up a dedicated team and infrastructure is crucial to give clear direction.

Knowing what you and your partner want is the firm basis for any deal. Using the benefits of strategic alliances is a viable means for F&B players to navigate their way through a shifting market landscape. For those looking to find a balance between the increased pressure on margins and the growing need for innovation, strategic alliances can offer a flexible and effective approach.

C-suite perspective

"In a low-growth market like consumer goods in Europe, companies are pushed to innovate to remain alive, and make alliances to leverage critical mass and lower costs while they are reducing investment in factories and R&D. This is not strategy, it is a way to survive."

Anonymous, CEO, unnamed food company

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ABOUT US

For nearly 40 years, AlixPartners has helped businesses around the world respond quickly and decisively to their most critical challenges – circumstances as diverse as urgent performance improvement, accelerated transformation, complex restructuring and risk mitigation.

These are the moments when everything is on the line – a sudden shift in the market, an unexpected performance decline, a time-sensitive deal, a fork-in-the-road decision. But it's not what we do that makes a difference, it's how we do it.

Tackling situations when time is of the essence is part of our DNA – so we adopt an action-oriented approach at all times. We work in small, highly-qualified teams with specific industry and functional expertise, and we operate at pace, moving quickly from analysis to implementation. We stand shoulder to shoulder with our clients until the job is done, and only measure our success in terms of the results we deliver.

Our approach enables us to help our clients confront and overcome truly future-defining challenges. We partner with you to make the right decisions and take the right actions. And we are right by your side. When it really matters.