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Taking Root

Plant-based beverages are tapping into mainstream channels

Evaluating "buy or build" options in the plant-based space is critical, and investors would be wise to "plant early" for what looks to be an exciting new growth opportunity in beverages.

Small business owners looking to develop eco-friendly, health and allergy friendly drinks are finding success in the plant-based sector, and large corporates are taking note of this sector's growth potential. While plant-based food has been present for several years, the beverage industry was initially slow to respond to this significant shift in consumer behavior. A few early deals in 2017, led by Nestlé's acquisition of Sweet Earth[1] and Coca-Cola's purchase of Unilever's AdeS plant-based beverage[2] business, followed by Danone's $12 billion WhiteWave acquisition in 2018[3], signaled growing investment interest in the sector.

By late 2019, the pace of investments in plant-based beverages has accelerated dramatically and is expected to continue into 2020. Plant-based beverages have become a hot category for growth that has seen increased interest from angel, venture capital, private equity, and strategic investors. Further plant-based category segmentation has opened up more new product opportunities and is attracting many new entrants.

Whether it's coconut water; soy, nut, oat, or pea milk; ready-to-drink (RTD) coffee with dairy-free milk; or plant-based protein drinks, the success of these beverages is being driven by consumer preferences for sustainability which is driving new product innovation and investment in this burgeoning plant-based consumer landscape.

The focus on plant-based products underscores the fact that consumers feel increasingly compelled to make healthier and more ethical food choices. While the number of vegetarians has not grown by more than 1 percent a year since 2010, more people are becoming flexitarians, meaning they are reducing their consumption of meat or processed foods, and are increasing consumption of plant-based foods.

Plant-based beverages are following the lead of the plant-based alternative meat market, which is booming with Tyson Foods Inc., Hormel Foods Corp, Conagra Brands Inc. and Kroger all gaining share in the plant-based, alternative meat category. Additionally, Beyond Meat[4] has been by far the best performing new issue, signaling that the disruption in the U.S. meat market is well underway.

The growth story in numbers

Between 2019 and 2023, the plant-based beverage category is projected to have a CAGR of 11 percent. Globally, RTD dairy alternatives remain the largest segment, and represented 65 percent of the plant-based beverage category or $18.2 billion[5] in 2018.

China remains the largest market for plant-based beverages with $14.1 billion in retail sales, and projected growth of 3.5 percent CAGR from 2019 to 2023[5]. The fastest-growing markets during this timeframe include France, Germany, and the United Kingdom, with projected CAGR of 14 percent, 10 percent, and 9 percent, respectively[5].

The U.S. total plant-based food retail dollar sales market is projected to be $4.5 billion in 2019, with annual growth of 11 percent over 2018[6]. For 2019, plant-based beverages' retail value is expected to reach $1.9 billion, of which dairy alternative milks will represent $1.8 billion, or nearly 95 percent of the plant-based beverage category[6].

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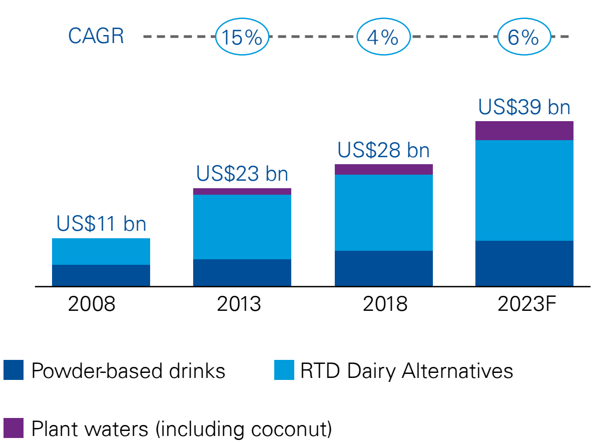
With dairy consumption on the decline for the last few decades in the United States, dairy farmers are adjusting their portfolio strategy. Americans drank 247 pounds of dairy milk in 1975 compared to 149 pounds of dairy milk per capita in 2017[7]. As a result, dairy farms are planting almond trees in former pastures and expanding their product portfolio to include nondairy alternatives. Large dairy companies have expanded their product portfolio in response to plant-based beverages. Dean Foods now has a majority stake in Good Karma and Organic Valley serves as distributor of New Barn Organics. These shifts show that plant-based beverages are not only a trend beverage for consumers today but also viewed as a strategic driver of future business growth.

An emerging beverage in the U.S. is oat milk. This beverage is rapidly growing given the fact that it capitalizes on multiple lifestyle trends. This allergy friendly, gluten free and naturally creamy dairy alternative is also more environmentally sustainable than nut-based milk due to lower water usage during production, and uses fewer gnetically modified organisms than other beverages like soy milk. Milk made from peas has similar potential for growth as it boasts a high protein content and less water usage than nuts.

Strong consumer demand for plant-based milks has led to brand line extensions across adjacent categories, including drinkable yogurt, RTD cold brew, and ice cream. Leading brands in North America and Europe such as Silk, Alpro, and Almond Breeze offer a full line-up of complimentary nondairy products, flavors, and formats, and success seems to follow the brands that offer a wide range of plant-based options.

Plant-based beverages expected to reach $39 billion globally[5]



Growth drivers: Micro to macro

Consumers relate to plant-based beverage consumption from various motives—from guilt-free, all-day snacking to global humanitarian efforts to climate change activism.

Climate-conscientious consumers believe that switching to a plant-based diet can help fight climate change. A recent report from the United Nations suggests that high consumption of animal-based products is fueling global warming[8]. Many plant-based beverages have also opted for eco-friendly packaging like cardboard cartons instead of plastic containers.

This shift to plant-based alternatives is a major trend promoted by many social media influencers and fitness experts. Consumers are told that plant-based beverages are much healthier options over conventional drink options due to their no or low-sugar content, a lack of artificial agents, and a low impact on the planet.

In the ever-evolving beverage industry, soda is no longer king. Innovation and health have become some of the biggest factors in a product's success. Today's consumers expect great taste, but also consider what value a beverage brings to their overall health and its impact on the environment.

All these factors make plant-based beverages the drinks of choice over traditional beverages.

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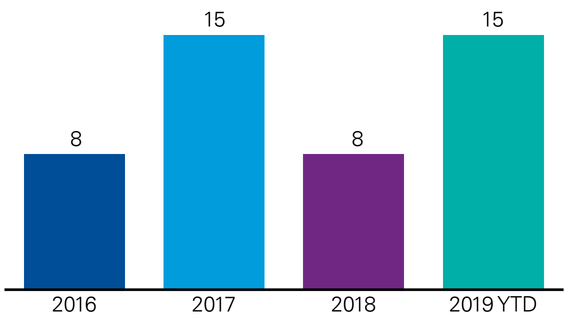
Plant-based beverages are driving M&A

The surge in consumer demand for plant-based beverages has triggered a wave of mergers and acquisition (M&A) activity from investors. Deal volume in the category has nearly doubled in the first 10 months of 2019 compared to 2018, and will likely exceed all other beverage categories by this year's end.

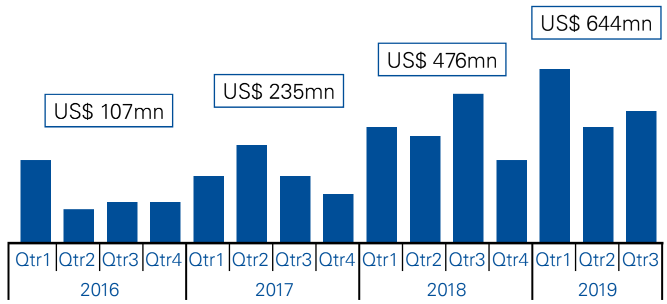
Deal volume in plant-based beverages (2016–2019[9])



** 2019 YTD as of October 2019*

Venture capital (VC) continues to play an important role in the sector's development, as VCs invested in nearly 35 percent of the sector's transactions from 2016 to 2019[9]. The VCs have been focusing more and more on smaller start-ups that offer unique, functional benefits such as such as Perfect Day Foods—which uses fermentation to create *"flora-based dairy protein."*

VC investments—Volume and value (2016–2019[8])



Larger corporations are utilizing M&A to build vertical integration with technology providers and ingredient suppliers such as Cargill's acquisition of plant-based additive provider Delacon Biotechnik GmbH in Austria. Other corporations are investing through their incubators to keep up in the market. Kraft Heinz's latest project, "Springboard Brands," is incubator program that focuses on funding disruptive start-ups with a $50,000 investment. The incubator recently invested in Blake's Seed Based, BRAMI, Ka-Pop! Ancient inGRAINed Snack Co™, Origin Almond,® and Tiny Giants.

Given the category's strong growth outlook and fragmented value chain, the outlook for further industry consolidation remains very favorable. As a result, transaction value multiples have been ranging upwards 18x LTM EBITDA[10] in the plant-based beverage sector, with equal interest from both corporate and financial buyers.

Looking ahead, we expect that increasing demand from thirsty, flexitarian consumers will drive large-cap food and beverage companies to embrace plant-based beverages. Developing the required product knowledge, cold-chain infrastructure, and consumer insights to succeed in this growing space will require significant time and investment capital.

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[1] Source: Nestle.com, Nestlé USA agrees to acquire Sweet Earth (September 7, 20017).

[2] Source: Coca-colacompany.com, Coca-Cola closes acquisition of AdeS Plant-Based Beverages (March 28, 2017).

[3] Source: Whitewave.com, Danone to acquire WhiteWave, a USD 4bn sales global leader in organic foods, plant-based milks and related products (July 7, 2016).

[4] Source: CNBC.com, Beyond meat's massive run may be getting young investors into some bad stock market habits (June 18, 2018).

[5] Source: KPMG analysis, Euromonitor.

[6] Source: The Good Food Institute, Plant-based market overview.

[7] Source: Here & Now, Nobody is moving our cheese: American surplus reaches record high, Samantha Raphelson (January 9, 2019).

[8] Source: BBC.com, Plant-based diet can fight climat change – UN, Roger Harabin (August 8, 2019).

[9] Source: Pitchbook, accessed October 2019.

[10] Source: Thomson Deals, accessed October 2019.

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