Stress to the system

M&A trends in consumer and retail

2022

kpmg.com

Introduction

Deep drop follows robust start

After a robust start in Q1'22, M&A activity in the consumer and retail (C&R) sector experienced a dramatic and precipitous decline for the year. This occurred as dealmakers weighed the impact of high inflation, interest rate hikes by the Federal Reserve, and the likelihood of a possible recession in 2023.

Deal value for the year fell to $115.3 billion, a decline of 52 percent compared with the year before. Similarly, deal volume dropped from 3,233 transactions in 2021 to 2,486 deals in 2022, a decline of 23 percent.

Still, there were a few bright spots: Kroger's announced $24.6 billion acquisition of supermarket rival Albertsons was the largest C&R deal of the year and one of the largest ever in the sector.

When KPMG surveyed executives about their M&A activity in 2022, executives in C&R firms with a small number of deals said a majority of their deal activity was divestitures. Only when C&R companies did more than three deals did the executives report more acquisitions than sales.

KPMG analysts identified the prime motivation for M&A deals in the sector during 2022. These included strategic portfolio assessments to determine which units might be sold, taking steps to gain market share, and acquiring a key product or expanding the firm's geographic footprint. Also important was acquiring key technology or other solutions that a firm lacked to enhance its ability to connect with consumers.

Looking ahead, KPMG Economics expects a mild recession in 2023, with consumer sentiment foreshadowing a downturn because wage growth has not been keeping up with inflation. According to the Bureau of Labor Statistics, average hourly earnings increased 4.6% in December 2022 as compared to December 2021, a decline from a 4.8% increase year-over-year in November 2022. While consumer sentiment as measured by the University of Michigan increased slightly in January due to declines in gas prices, it is still below levels in 2021.

Because of inflation in such key categories as housing and food, KPMG expects consumers to feel increased financial stress in 2023, with credit card debt rising and people drawing down savings. This is squeezing consumer companies and big retailers, which are in turn passing on costs to their suppliers, pushing economic stress down to mid-sized and small businesses.

Kevin Martin
U.S. Consumer and Retail Lead
Deal Advisory & Strategy

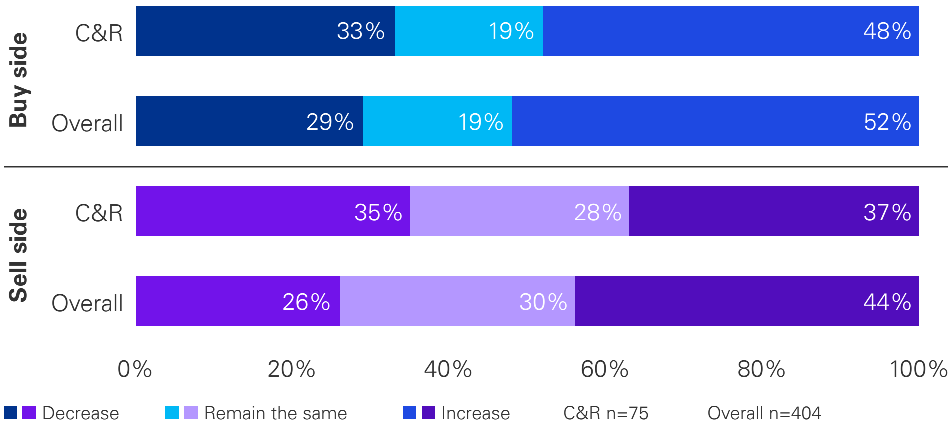
Key statistics

-23% decrease in total C&R deal volume from 2021 to 2022 (3,233 to 2,486).

-52% decrease in total C&R deal value from 2021 to 2022 ($240.7 billion to $115.3 billion).

19% PE share of C&R deals in 2022. PE buyers accounted for 30.2 percent of total value.

"Compared to the last 12 months, do you expect that deal activity in your industry will increase or decrease over the next 12 months?"



[1] "The Employment Situation – December 2022," bls.gov, Jan. 6, 2023

[2] "Surveys of Consumers, Final Results for December 2022," University of Michigan, Jan. 2023

By the numbers

Grocery bargain

Excess inventories and sinking consumer confidence helped persuade C&R firms to scale back M&A activity until at least the contours of a possible recession become clearer.

The gigantic, $24.6 billion deal between supermarket giants Kroger and Albertsons helped avoid an even more dramatic decline in the year's deal values. With 2,486 deals valued at $115.3 billion, C&R sector deals were nonetheless still far behind the 3,233 deals valued at $240.7 billion in 2021.

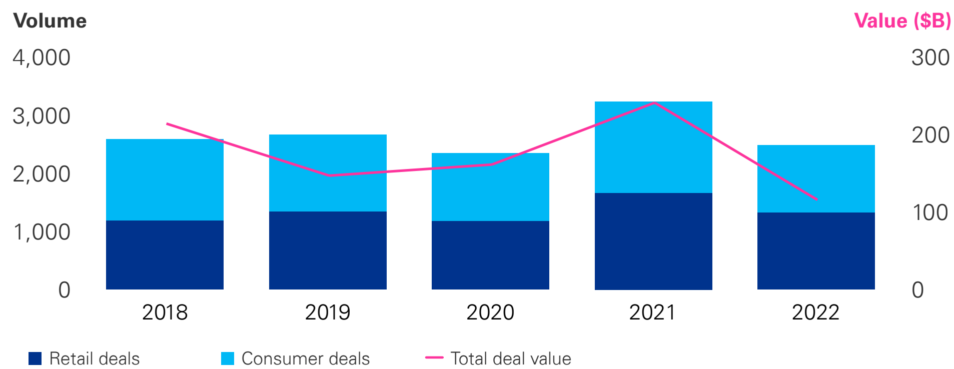
Retail deals led the way with 1,321 announced transactions compared with 1,165 consumer deals.

The 1,993 strategic deals valued at $76.0 billion were 20 percent below the number in 2021. Private equity suffered a worse fate, with the number of PE deals declining to 480 from 706 transactions the year before, a drop of 32 percent. PE deal value also fell from $84.3 billion in 2021 to $34.8 billion in 2022, a fall of 59 percent.

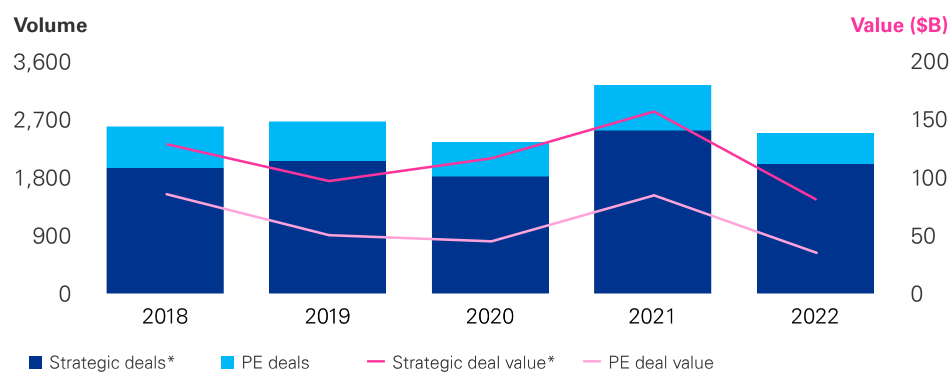
Top C&R deals 2022

Acquirer	Target	Value (billions)
Kroger	Albertsons	$24.6
Amazon.com	One Medical	$3.9
Sony Interactive Entertainment	Bungie	$3.7
Whirlpool Corporation	InSinkErator	$3.0

U.S. C&R activity by sector



U.S. Strategic and PE C&R deals



*Strategic deals and value include SPAC deals and value

About the data: Data was sourced from CapitalIQ, Refinitiv, Pitchbook, and KPMG analysis. The values and volumes data cited are for U.S. deals announced between 1/1/2022 and 12/10/2022. Deal values are only presented based on publicly available deal data and are not exhaustive. Previously published statistics may be restated to incorporate new data and/or changes in deal outcomes.

By the numbers

Consumer M&A trends

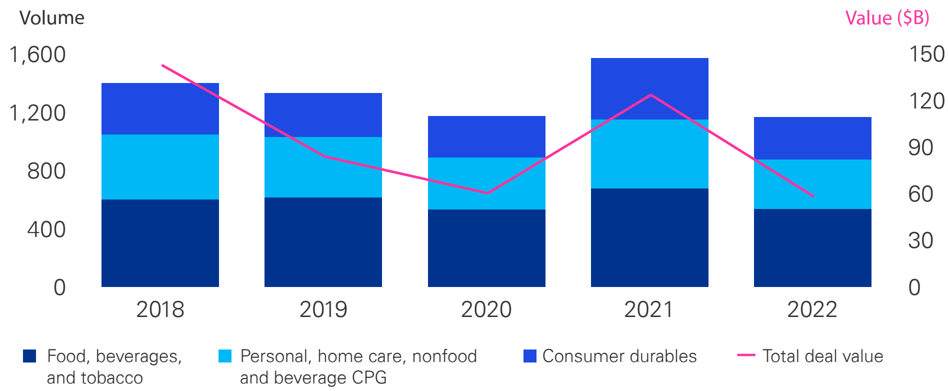
In the consumer sector, M&A activity was dampened by many firms being forced to raise prices to maintain profits at a time of high inflation. Food, beverage, and tobacco accounted for 533 deals—down from 675 in 2021, a decline of 21 percent. Personal, home care, and nonfood and beverage consumer packaged goods companies announced 341 deals, down from 473 in the previous year. There were 291 consumer durable deals announced, a decline from the 424 transactions in 2021.

Consumer deal volume and value by subsector

2022

1,165 deals
-25.9%

$57.9 billion
-53.1%



Retail M&A trends

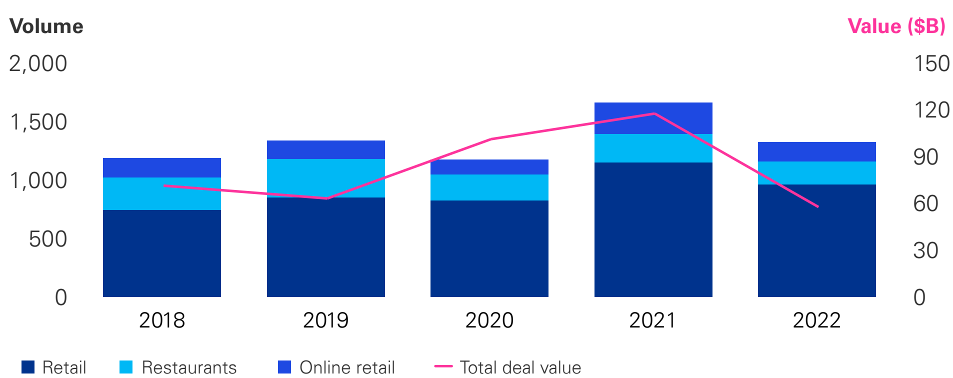
While the retail sector got hit with excess inventory ahead of the Christmas shopping season, there were 1,321 retail transactions announced, a 20 percent fall from the 1,661 reported in 2021. There were 167 deals in the online-only retail space announced, down from 271 the previous year. In restaurants, announced transactions declined from 243 in 2021 to 194 in 2022.

Retail deal volume and value by subsector

2022

1,321 deals
-20.5%

$57.4 billion
-51.1%



By the numbers

PE M&A trends

Although PE firms are reported to have more than $1 trillion in capital available, many seemed headed to the sidelines until the recession question is resolved or the Fed begins to cut rates as a sign that inflation has been addressed. This uncertainty is what worries them the most.

Total PE deal value in 2022 was a paltry $34.8 billion, compared with the massive $84.3 billion in acquisitions by PE firms in the year before. The decline was particularly sharp in Q4'22, when PE deal volume fell to just 88 transactions, compared with 149 in Q1'22, a drop of 41 percent.

PE firms announced 127 deals in retail, down from 169 transactions in 2021, while PE deals in consumer companies declined from 537 in 2021 to 353 in 2022. Consumer PE deal value was cut in half over the year, falling from $42 billion in 2021 to just $21 billion in 2022.

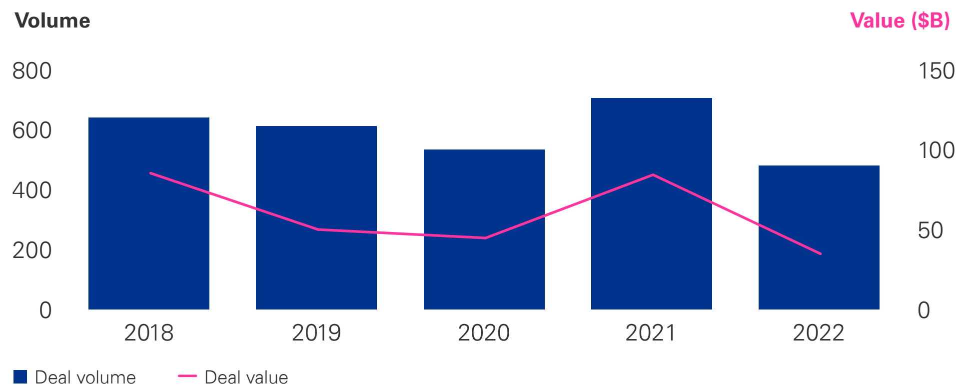
The top PE deal in the C&R space was AM Fresh Group's announced acquisition of International Fruit Genetics for $1.7 billion, with plans to merge it with its Special New Fruit Licensing to develop their breeding capacities and add to their portfolio of table grapes. In the second largest transaction, sports licensing company Fanatics raised $1.5 billion in new funding from a consortium including Fidelity, BlackRock, and MSD Capital.

PE deal value and volume

2022

480 deals
-32.0%

$34.8 billion
-58.7%



Top C&R PE deals in 2022

Acquirer	Target	Value (billions)
AM FRESH Group and SNFL Group	International Fruit Genetics (IFG)	$1.7
Fidelity, BlackRock, and Michael Dell's MSD Partners (in a new funding round)	Fanatics	$1.5
Advent International	IRCA Group	$1.1
Investindustrial	Meal Preparation Division of Treehouse Foods	$1.0

Consolidating food giants

Kroger's proposed $24.6 billion bid to acquire smaller rival grocer Albertsons would create the third largest U.S. grocery retailer with sales of a combined $208 billion (trailing only Walmart and Amazon's Whole Foods).[3] Albertsons store locations complement Kroger's national grocery footprint and will assist Kroger in regaining market share that had dropped to a three-year-low of 6.7 percent by 2022. In addition, the union of the companies will broaden Kroger's Our Brands private label product portfolio and will potentially accelerate shareholder value (through cost efficiencies and added pressure to suppliers and labor unions).

Consolidation in the grocery industry has been accelerated recently by the COVID-19 pandemic, during which many shoppers opted to order online and get delivery through apps like Instacart rather than visiting stores. Big retailers such as Walmart and Amazon have been investing billions to improve their online shopping experience and automate to reduce costs, giving the larger firms an advantage because of their deeper pockets for technology investments.

In addition, high inflation in 2022 caused consumers to seek out retailers offering cheaper private label goods. These retailers tend to be the biggest in sales: Kroger, for example, boasts over 10,000 Our Brands products and said its private label sales surged by 10.4 percent in the third quarter of 2022.

Recently, most of the M&A activity in the sector has been among smaller regional players, such as Tops Markets' February 2021 merger with Price Chopper/Market32.[4] The continuing consolidation in the grocery business is expected to put renewed pressure on such regional players that don't have the financial heft to expand nationally or acquire expensive technology. Even within regions, it can be expensive to roll out the logistics to move items like meat and fresh vegetables from one city to another. Either they go into new markets or pick up distressed grocers that have only one or two outlets.

Without merging, the next phase for these regional players is likely to be combining forces in loose tie-ups rather than M&A to make technology investments in shared platforms that can accommodate customers who want to shop for groceries online.

Rohan Agarwal
Managing Director
C&R Advisory

[3] "The PG 100: Ranking Top Food Retailers in North America," progressivegrocer.com, June 15, 2022.
[4] "Tops and Price Chopper to merge. What it means for customers," Feb. 8, 2021, DemocratandChronicle.com

Outlook

An uncertain picture

Inflation is clearly moderating from its peak in mid-2022, and consumer sentiment is less negative. Even with those trends, M&A activity in the C&R sector is likely to be constrained in 2023 until the scope of a possible recession—and the Federal Reserve's response—become clearer. KPMG Economics noted that the labor market is showing signs of cooling, while goods inflation is easing. Services inflation continues to rise, a concern for the Fed. It said it expected the federal funds rate to hit 5.25 percent in 2023 before falling to 4.25 percent at year's end, which would be better than the Fed's own scenario of keeping rates elevated for the entire year. For C&R firms, sales figures from the all-important Christmas shopping period surprised to the upside with an increase of 7.6 percent, indicating that consumers still have money to spend. But after inflation was taken into account, sales actually declined about 1 percent compared with the previous year.

Looking ahead, nearly half of C&R executives surveyed by KPMG indicated that they will be active buyers of other firms this year, while another 37 percent said they planned both acquisitions and divestitures. At the same time, a survey of PE firms active in C&R showed that 80 percent of respondents expected a decline in deal activity over the next 12 months. These PE executives cited the macro situation, access to capital, and debt requirements as the most prominent headwinds affecting their deal decisions.

KPMG C&R specialists believe deal activity will continue to be soft in FY23, particularly in the first half of the year. We see many companies sitting on the sidelines waiting to know how resilient consumers will be in the face of rising costs. While the Fed's rate hikes and a possible recession are likely to put a damper on deal decisions, M&A activity will persist in key areas, such as divestments of non-core assets, as well as PE firms and corporates looking to acquire bargains while valuations are depressed.

Some corporate deal teams remain cautious because of the many macroeconomic uncertainties. They also realize that some assets may offer better long-term strategic value at a time when financial investors are sitting on the sidelines, causing valuations to become more attractive, especially when potential synergies offer the chance to create value.

Key considerations as we look ahead

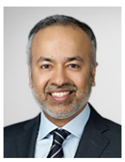
In pursuing M&A in an economic downturn, C&R deal makers will need to recalibrate their focus to ensure success:

1. Management must carefully monitor working capital.
2. Have a clear focus on cost contingencies to gain efficiencies.
3. Preserve margins to ensure long-term strategy.

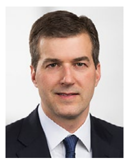
Authors

Kevin Martin
Partner
U.S. Consumer and Retail Lead
Deal Advisory & Strategy
212-945-8401
kevinmartin@kpmg.com

Julia Wilson
Principal
C&R Advisory
404-222-3511
juliawilson@kpmg.com

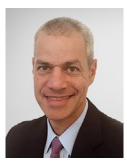


Sunder Ramakrishnan
Principal
C&R Advisory
617-905-6397
hsramakrishnan@kpmg.com



Bob Glowniak
Managing Director
C&R Advisory
312-550-8018
rglowniak@kpmg.com

Rohan Agarwal
Managing Director
C&R Advisory
917-592-5526
rohanagarwal4@kpmg.com



Robert Gaida
Managing Director
C&R Advisory
551-208-0498
rgaida@kpmg.com

With special thanks to:
Geoff Lewis, Ralph Park, Montana Sannes, Amanda Kendall, Heather Vo, Kathy Wheeler, Anshita Tripathi, Amitoj Singh

KPMG helps its clients overcome deal obstacles by taking a truly integrated approach to delivering value and leveraging its depth in the C&R industry, data- supported and tools-led insights, and full M&A capabilities across the deal lifecycle.

With a C&R specialization, our teams bring both transactional and operational experience, delivering rapid results and value creation.