



THE DEAL HOUND

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QUARTERLY PET INDUSTRY REPORT

VOL. 5 ISSUE 4 Q4 2014

PET INDUSTRY DEAL ACTIVITY – Q4 2014

The “pet parent” trend in America and the corresponding growth in demand for premium pet products and services continued to drive high levels of industry growth in Q4 of 2014. Increasing numbers of pet-owning households are demanding all-natural, organic pet foods as well as high-end services for their pets. Among retailers, competition remains fierce between supermarkets, discount departments stores and online-only retailers. In mid-December 2014, PetSmart, the \$7 billion revenue pet retail giant, was acquired by financial buyers for \$8.3 billion. The global growth of this pet trend is also witnessed through increasing international M&A activity, such as Spectrum’s acquisition of the IAMS and Eukanuba brands in Europe. Many of the large players in the industry are seeking to expand their specialty products and services through acquisition of smaller companies, as witnessed in Petco’s acquisition of pet catalog company Drs. Foster and Smith, Inc. In addition to the premium product and service trend, the pet industry is witnessing a massive growth in the e-commerce sector. Niche players such as 1-800 PetMeds, new specialty entrants, and discount retailers such as Walmart are largely dominating the online retail sector. Despite the transactional slowdown in Q4, the pet industry continues to promise continued levels of growth and transactional activity in upcoming years.

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Pet Deal Activity Highlights

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| <p>STRATEGIC TRANSACTIONS</p> | <p>12.31.14 Spectrum Brand Holdings, an international consumer products corporation headquartered in Wisconsin, announced finalization of its acquisition of Procter & Gamble’s European pet food business, including the IAMS and Eukanuba brands. The financials of this transaction were undisclosed.</p> <p>11.19.14 PETCO Animal Supplies, Inc., a specialty retailer of pet supplies with \$2 billion in revenue, announced intent to acquire Drs. Foster & Smith, Inc., a catalog retailer of pet healthcare supplies, for an undisclosed amount.</p> |
| <p>FINANCIAL TRANSACTIONS</p> | <p>12.4.14 PetSmart, Inc. announced intent to be acquired by a group of investors led by BC Partners for \$8.25 billion. The transaction was unanimously approved by the PetSmart Board and is pending shareholder and regulatory approval with closure expected in the first half of 2015.</p> <p>11.11.14 Pershing Square Capital Management invested \$182 million in Zoetis Inc, a global animal health medicine manufacturer.</p> <p>10.6.14 Freshpet Inc, a natural fresh and refrigerated pet food and treat company, raised approximately \$156 million in an initial public offering, pricing the company at \$15 per share. The company’s total enterprise value is 9.6x total revenue.</p> |

Sniffing Out a Deal – PETCO Acquisition of Drs. Foster and Smith



Acquisition Type:
Strategic

Top 4 Value Drivers:
*Increasing Pet Portfolio
Market Access
Robust Growth Opportunities
Online Service Expansion*

- ❑ PETCO sells specialty pet supplies and offers pet grooming, training, clinics, luxury accommodations and boarding services throughout North America.
- ❑ Drs. Foster and Smith sells pet supplies to consumers via their website and catalogs.
- ❑ Online pet retail represents one of the industry’s fastest growing sectors and is currently offering one of the highest valuation multiples in the industry. PETCO was willing to offer such a high price for Drs. Foster and Smith in order to expand their online and catalog market access.

Source: CapIQ

The information contained herein is based on sources we believe reliable but is not guaranteed by us and is not to be considered all inclusive. It is not to be construed as an offer or consultation of an offer to sell or buy any securities.





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SPOTLIGHT

Marco Gianinni, Founder of Dogswell & Protein for Pets
An Interview with SDR's Carol Frank

CAROL: Please give us a brief history of how you founded Dogswell

MARCO: Shortly after graduating from the University of Southern California with my MBA, I had a wealth of ideas but little means to fund them. Realizing there was an untapped market for healthy dog treats, I founded Dogswell in 2003 with my own, albeit modest, savings to cover the manufacturing of the product. With that I started selling door to door to retailers to get commitments to buy. Once I had about 50 commitments per region, I took that to the distributors and told them that if they bought my product I could guarantee them the first 50 customers. It all worked out pretty well for everyone.

CAROL: Why do you think Dogswell grew so quickly to become one of the leading pet treat brands in the U.S. today?

MARCO: I think there were many factors that contributed to why Dogswell grew so quickly, beginning with the fact that people love their pets. In a health-conscious country such as the United States, it made sense that the benefits of eating healthy applied to pets. We kept the product line simple, but full of healthy ingredients and nutrients and made educating people about Dogswell treats and their many benefits a priority.

CAROL: What are some valuable lessons you have learned during the process of selling your interest in Dogswell to TSG Consumer Partners?

MARCO: The whole industry has evolved dramatically over the last 10 years and private equity has become an increasingly influential fixture within it. My experience with TSG was a tremendous learning experience that taught me a great deal about myself and my abilities. I think there are so many different private equity outfits to partner with and it's important that if you go that route you choose the right fit for you personally and for your company.

CAROL: Why do you think there has been so much interest in the pet industry from private equity groups?

MARCO: The pet industry has experienced strong and steady growth for the last 10+ years. Many industries outside of pet have done quite well, but with great peaks and valleys such as tech or oil/gas. With the advancing age of our population and the delay in Generation X'ers getting married, pets have become an important part of the family, which has translated to steady growth and opportunity.

(Continued on page 3)

To start a successful company with little more than an innovative idea and an entrepreneurial passion is quite an accomplishment. To do it twice before turning 40 is extraordinary.



Marco Gianinni

Enter Marco Giannini, Founder and CEO of Protein For Pets, who at age 38, is leaving an indelible print on the world of natural pet food and supplies while reinventing how people shop for them.

Giannini founded Protein For Pets in early 2014 to fill a void in the retail landscape for an independent pet food and supply store driven by customers' needs and convenience.

Giannini's forward-thinking commitment to enhancing the health and well-being of pets began while pursuing his MBA at USC. Shortly after completing the program, Giannini founded his first company, Dogswell in 2003. After a modest beginning selling dog treats out of his car, Giannini went on to establish a national brand specializing in nutrient and supplement-filled dog food and treats. The company grew from a half-million-dollar business within its first year to tens of millions when he sold it at the end of 2008. Giannini remained CEO of Dogswell until leaving the company in 2013 to create Protein For Pets.



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SPOTLIGHT (CONTINUED)

CAROL: What is the largest change the industry has undergone since you began working in it 11 years ago?

MARCO: There has been a tremendous amount of consolidation within the distributor community. When I started, there were over 50 distributors to choose from in the independent pet sector. Now there are less than 20 and really only a handful of super regionals. That dynamic has changed the complexity of manufacturers and opportunities for retailers.

CAROL: What advice would you give to the small or mid-sized pet product distributor or manufacturer in terms of maximizing the value of their business?

MARCO: The most important feedback you can receive is from someone who buys your product. Giving the product away for testing is good, but not as good as selling the product. When they buy it, they feel they have the right to tell you the truth, good or bad. What's that quote, "make a little, sell a little."

CAROL: Tell us about your next venture, Protein for Pets.

MARCO: I founded Protein For Pets in early 2014 to fill a void in the retail landscape for an independent pet food and supply store that is strictly driven by customers' needs and convenience. At the same time, with the recent boom of trendy high-end specialty pet stores, I wanted to make the increasingly important natural pet food and supply concept more accessible to people regardless of their income levels. I opened the *first* store in March of 2014 and the *ninth* in January of this year.



Unlike most pet supply stores that organize product by brands, Protein For Pets has a no-nonsense, less than 1,500 square foot setup that mirrors that of a supermarket with foods organized by protein and product type. Providing a unique, easy and customer-friendly shopping experience, each store boasts poultry, meat, fish and exotic sections that are filled with a carefully researched and hand-selected assortment of more than 150 natural formulas. Each contains the highest-quality dry, raw and wet foods - all of which have no corn, soy, wheat or animal by-products.

The stores are stocked with national and specialty brands including Blue Buffalo, Merrick, Natural Balance, Stella & Chewy and Primal, all organized within each section by varying price points to meet every budget.

The Protein For Pets business model also allows for giving back while moving forward. Protein For Pets makes an impact in each community it is part of by donating to local animal shelters and schools.



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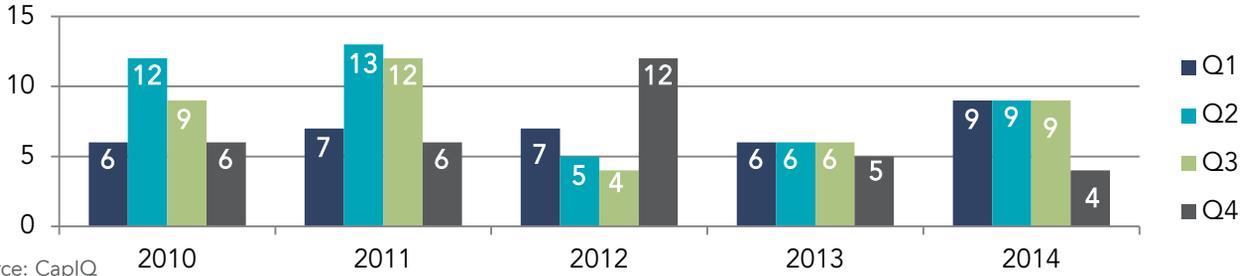
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M&A MARKET OVERVIEW

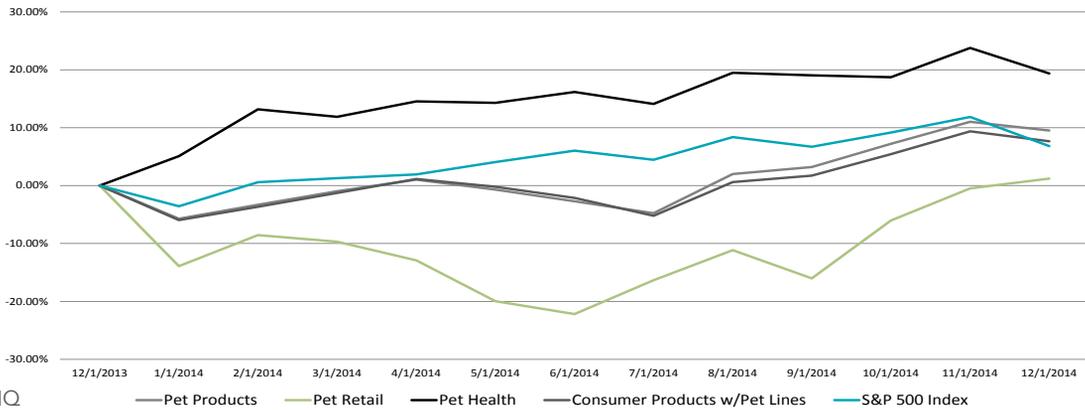
Pet Transactions

of Transactions by Quarter



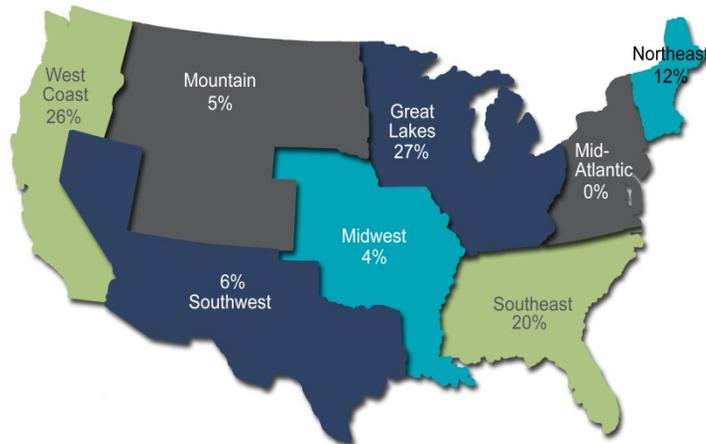
Source: CapIQ

Public Pet Segments: AVERAGE STOCK PRICE CHANGE BY SEGMENT



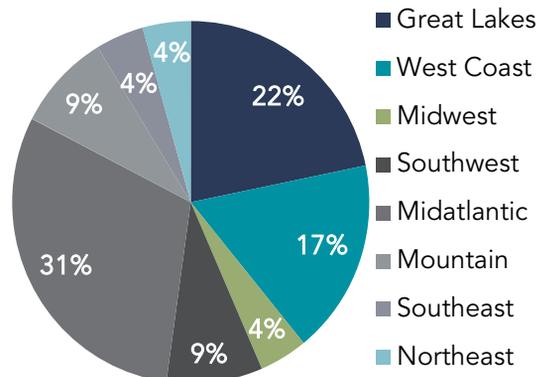
Source: CapIQ

All Pet Companies by Region



Source: CapIQ

Pet Transactions by Region (2014)





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PUBLIC BASKET

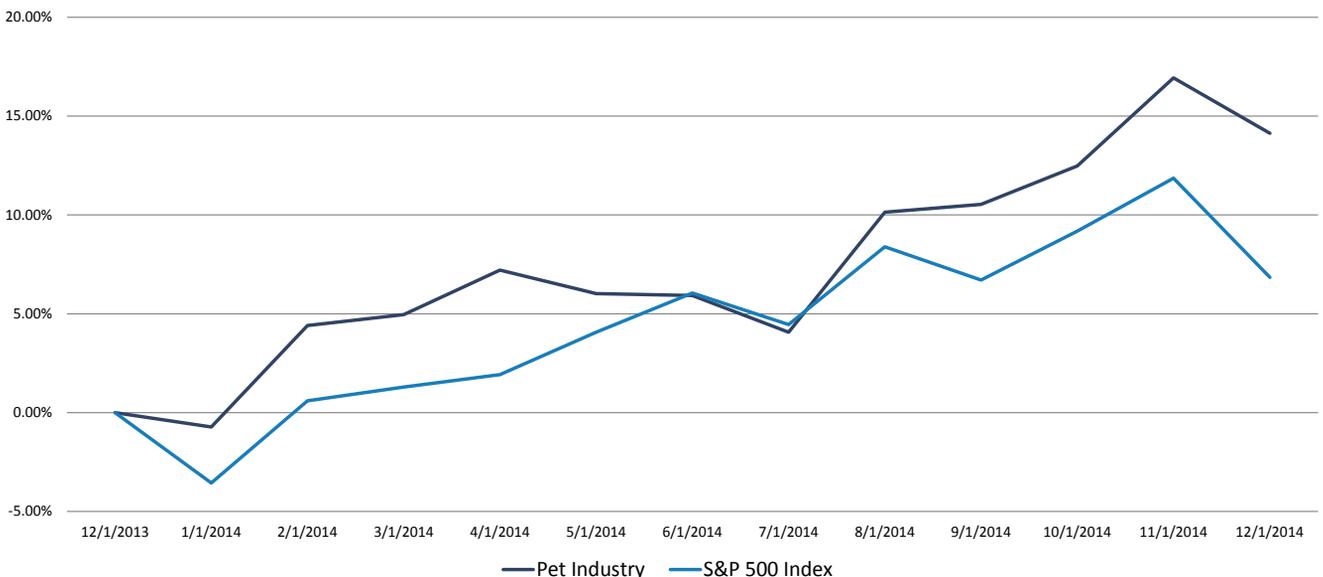
Every sector of the pet industry experienced overall stock price growth in Q4 2014, resulting in the industry greatly outperforming the S&P 500 average in Q4. Pet retail experienced a massive stock price climb beginning in September of this year and continuing to rise through the end of the year. Retailers such as PetSmart, Spectrum Brands, and Central Garden & Pet Company witnessed stock price increases of over 8% within Q4 2014. Average industry valuation multiples were also higher than S&P 500 average. In particular, pet health companies were valued approximately 40% higher on average than the S&P 500 average. The pet health segment outperformed every other industry sector as well as the S&P 500 average throughout 2014, closing the year at slightly below 20% growth. Overall, the pet industry closed 2014 with average stock price growth of over 14% and high average valuation multiples, finishing the year out strongly and offering evidence for continued growth in performance and M&A activity in 2015.

| Company | Symbol | State | Market Cap | | Stock Price Change | | Price/ LTM EPS | Price/ Book | Price/ Rev | Price/ EBITDA |
|----------------------------------|---------------|-------|------------------|----------------|--------------------|---------------|-------------------|----------------|---------------|------------------|
| | | | (\$ in Mil) | Price | Month | YTD | | | | |
| PetSmart, Inc. | NasdaqGS:PETM | AZ | \$ 8,083 | \$ 81.3 | 3.22% | 11.75% | 19.0x | 6.5x | 1.2x | 8.6x |
| Tractor Supply Company | NASDAQ:TSCO | TN | \$ 10,715 | \$ 78.8 | 2.46% | 1.60% | 31.7x | 8.8x | 2.0x | 16.1x |
| Central Garden & Pet Company | NasdaqGS:CENT | CA | \$ 476 | \$ 8.8 | 19.95% | 27.80% | 38.3x | 0.9x | 0.5x | 8.2x |
| Phibro Animal Health Corporation | NasdaqGM:PAHC | NJ | \$ 1,229 | \$ 31.6 | 3.24% | NA | 34.6x | 56.9x | 2.1x | 15.5x |
| Eli Lilly and Company | NYSE:LLY | IN | \$ 73,598 | \$ 69.0 | 1.28% | 35.27% | 35.1x | 4.2x | 3.7x | 15.4x |
| VCA Inc. | NasdaqGS:WOOF | CA | \$ 4,103 | \$ 48.8 | 3.04% | 55.52% | 28.4x | 3.2x | 2.5x | 13.4x |
| Zoetis Inc. | NYSE:ZTS | NJ | \$ 21,572 | \$ 43.0 | (4.23%) | 31.63% | 33.9x | 15.8x | 5.2x | 18.2x |
| Freshpet, Inc. | NasdaqGM:FRPT | NJ | \$ 571 | \$ 17.1 | 2.09% | NA | NM | NM | 9.7x | NM |
| Harbinger Group Inc. | NYSE:HRG | NY | \$ 2,846 | \$ 14.2 | 3.21% | 19.49% | 22.8x | 1.9x | 1.2x | 7.9x |
| Oil-Dri Corp. of America | NYSE:ODC | IL | \$ 231 | \$ 32.6 | 20.63% | (13.77%) | 34.3x | 2.2x | 0.9x | 10.6x |
| Average | | | \$ 12,342 | \$ 42.5 | 5.49% | 21.16% | 30.9x | 11.2x | 2.9x | 12.6x |

Source: CapIQ

PET INDUSTRY VS. S&P 500

INDUSTRY AVERAGE STOCK PRICE CHANGE: RUNNING 12 MONTHS



Source: CapIQ



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SDR VENTURES: THE INVESTMENT BANK TO THE PET INDUSTRY

Carol Frank (cfrank@sdrventures.com), *Managing Director*



Prior to joining SDR Ventures in 2009, Carol developed three multi-million dollar pet companies in retail, manufacturing, and distribution. She successfully built and sold all three companies, and possesses the rare combination of investment banking expertise, transactional and operational experience in the pet industry.

Carol began her career as a CPA with Ernst & Young and also spent three years as an executive recruiter for Robert Half International. She has a BBA in accounting from The University of Texas at Austin and an MBA from Southern Methodist University. Carol is a former board member of PIDA, PIJAC and The Pet Care Trust. As a registered investment banker, she also holds Series 79 and 63 licenses.

SDR Core Services

Pet Industry Sell Side

As former owners and operators, our principals have experienced the M&A world from the trenches. As investment bankers, our principals have gained the experience necessary to maximize value and facilitate a successful transaction. We know how to run an efficient and effective process, how to avoid pitfalls, how to maximize shareholder value and how to minimize operational distractions.

Pet Industry Buy Side

Our buy-side search process has proven extremely effective at generating responses, identifying "off-the-radar" opportunities, negotiating favorable deal terms and closing deals in a timely manner.

*"SDR can be your outsourced
Mergers & Acquisitions team."*

Transaction Advisory

Capital Formation

Placement Agent

SDR can act as a finder for private debt and equity capital in post-revenue situations. Our goal is to identify the right capital and the right capital provider based on your needs.

Strategic Advisory

Unlike many traditional investment banks, SDR views each client as a relationship rather than a transaction. Our passion is helping business owners maximize value in their business. While this often takes the form of advising on acquisitions, sales and recapitalizations, we realize that not every business is ready for such a transaction.

Our advisory services are designed to add value. Advisory engagements include (but are not limited to):

- Company Valuation
- Capital Strategy
- Exit Planning
- Shareholder Strategy

RECENT TRANSACTIONS

