



# INGREDIENTS MARKET UPDATE

Summer 2020



BAIRD



# EXECUTIVE SUMMARY

- The ingredients market is large, growing and increasingly important to the F&B industry and to consumers
  - \$70B industry growing at a total 5%+ per year
- Strong ingredient sector tailwinds have been amplified by COVID-19, as ingredient suppliers are increasingly:
  - Providing high-quality inputs to match the wellness demands of today's consumer at only a fraction of the end product's total cost
  - Providing value-add partnership and solutions instead of transactional vendors
  - Ensuring customers' credibility by specifically meeting end consumers' demands for traceability, sustainability, safety and function
- Investors have rewarded ingredient companies that have:
  - Defendable intellectual property (e.g., patented products, proprietary techniques)
  - Strong in-house R&D capabilities providing customers with customization, flexibility and speed
  - High quality, sophisticated and sustainable supply chains
- We believe ingredient suppliers will become even more important moving forward, and companies focusing on these trends will be well positioned in the next phase of industry growth



# INGREDIENTS ARE AT THE FOREFRONT OF EVERY KEY F&B TREND

BAIRD

## FUNCTION



- ✓ Fortifications (fiber, protein, vitamins, probiotics)
- ✓ Convenience (portability, shelf-life, re-sealability)
- ✓ Energy and weight loss (Keto, Paleo)

## ALTERNATIVES



- ✓ Meat / Dairy / Bakery (pea, soy, almond, cashew, cauliflower)
- ✓ Sweeteners (monkfruit, stevia, real fruit essence)
- ✓ Alcohol (mocktails, low/no-alcohol beer, hard kombucha)

## FLAVOR



- ✓ Global flavors, regional fusions
- ✓ Bold, spicy, umami
- ✓ Botanicals (saffron, hibiscus)

## PROVENANCE



- ✓ Authenticity and lineage
- ✓ Cage-free, pasture-raised
- ✓ Grass-fed, antibiotic-free

## SAFETY



- ✓ Supply chain traceability
- ✓ Facility certifications (SQF, BRC)
- ✓ Controls and testing (allergens, PCBs, heavy metals, herbicides)

## HEALTH AND WELLNESS



- ✓ Personalization
- ✓ Prevention > Treatment
- ✓ Sustainability and reduced waste / pollution

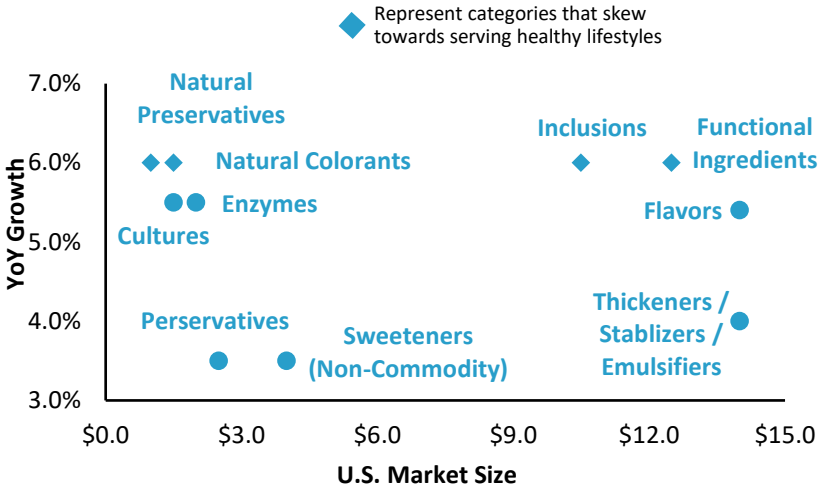
# INDUSTRY & SECTOR TAILWINDS | THE INGREDIENT INDUSTRY IS LARGE AND GROWING

## INGREDIENT MARKET IS LARGE AND GROWING <sup>(1)</sup>

- Consumers across all demographics are adopting a more holistic, healthy lifestyle
- Ingredients are a key part of the equation – **\$70B** global ingredients market is growing at **5%+**
- Breadth of functionality within the ingredient industry serves a particularly diverse set of customers and creates opportunity to capture growth

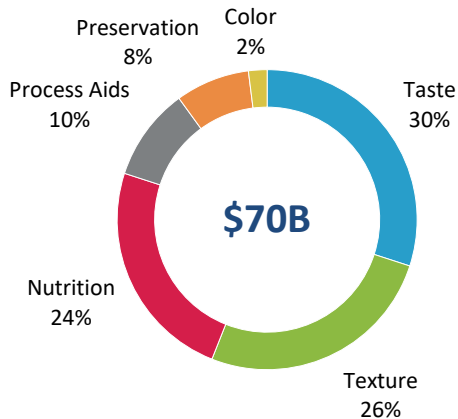
## FOOD INGREDIENT MARKET BY TYPE <sup>(1)</sup>

(Market Size, YoY Growth %)



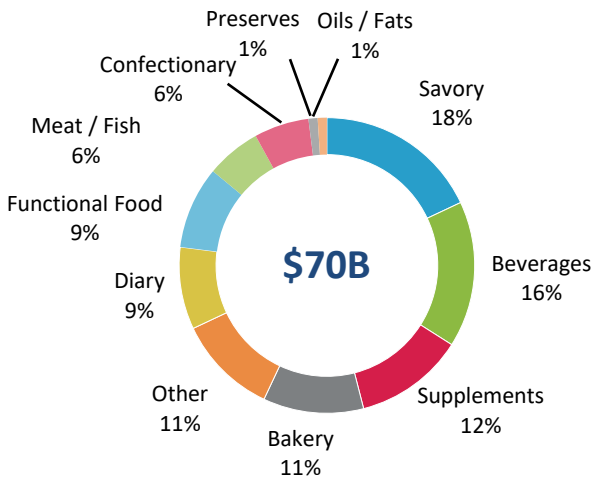
## FOOD INGREDIENT MARKET BY FUNCTION <sup>(1)</sup>

(% revenue)



## FOOD INGREDIENT MARKET BY END USER <sup>(1)</sup>

(% revenue)



(1) Baird and DB research.

# INDUSTRY & SECTOR TAILWINDS | INGREDIENTS ARE BECOMING AS IMPORTANT AS THE BRAND IN THE NEW “CLEAN LABEL” WORLD

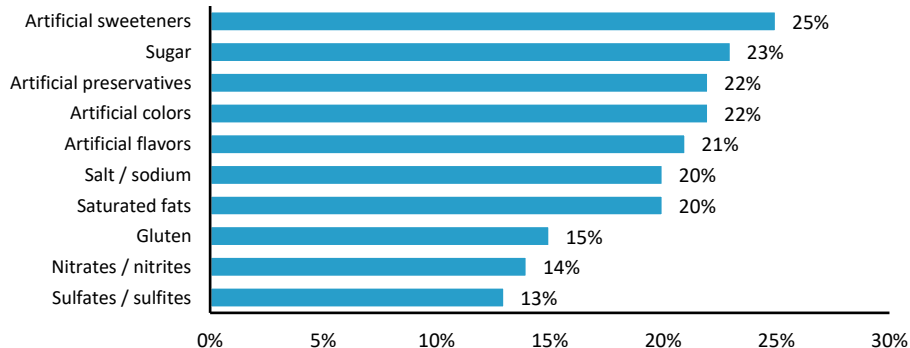
BAIRD



## Increasing Consumer Preference for Clean-Eating and Wellness <sup>(1)</sup>

- Consumers equate ‘natural’ with ‘healthy’ – **59%** of consumers expect a natural product to be healthy and **53%** also expect it to be GMO free
- **68%** of consumers agree moderation is more effective at maintaining good health than substituting with artificial sweetener ingredients
- Consumers were asked: when shopping for a new product, what do you usually read on the packaging ... **51%** said the ingredients list is the most important, while only **45%** were motivated by the brand

### Top 10 Ingredients Consumers Avoid <sup>(2)</sup>



## Companies are Delivering on Consumer Demands for Better Ingredients



*“Kraft revealed it had quietly removed artificial flavors, preservatives, and dyes from its Mac & Cheese dinners three months earlier. It was a bold move on one of its signature brands...Kraft has publicly stated that consumers had asked for a healthier version of Mac & Cheese.”*

– Chris Daniels, PR Week



*“Grocers are looking for what is new, and clean labels are the hottest thing. They are saying, ‘Give me a clean label or I am not putting it in the store’.”*

– Grace Leong, Managing Partner, Hunter PR



*“Our research results show that ingredients lists are powerful purchasing motivators for consumers and can even be more important than the actual brand of the product.”*

– Myriam Snaet, Head of Market Intelligence at Beneo

## CPG RESPONSES TO NEW “CLEAN LABEL” WORLD



*PepsiCo continues to move portfolio toward cleaner ingredients, more on-trend, more of the perimeter of the store versus the center store*



*Nestlé committing to removing artificial flavors and colors from its chocolate products*



*Hershey publicly committed to prioritizing simple ingredients, transparency and responsible ingredient sourcing*



*Mars Wrigley Confectionery is mapping out a five-year plan to replacing artificial flavors with ethically and sustainably sourced natural ones*

# INDUSTRY & SECTOR TAILWINDS | INGREDIENT SUPPLIERS ARE MOVING FROM “VENDORS” TO “PARTNERS”

BAIRD



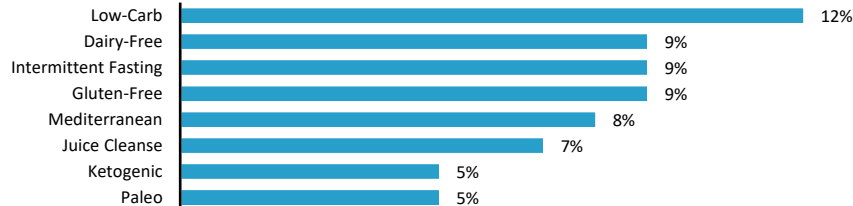
## Rapidly Changing Consumer Preferences for Tailored Products

- The way consumers think about health benefits derived from food is evolving:
  - Half of adults (**50%**) experimented with a new diet or eating approach in 2019, up from **40%** in 2017 <sup>(1)</sup>
- Consumers are using more targeted approaches to wellness:
  - In 2019, heart health fell from first to fourth place among the health benefits consumers would most like to get from foods

### Ranking of Food Health Benefits that Consumers Want



### % of Adults Experimented with a New Diet



## CPG has Increasingly Relied on Ingredient Companies to Drive R&D

- Historically, ingredients suppliers were focused on taste, flavors and cost
- Now, ingredient supplier's R&D capabilities are in the spotlight as they are driving market trends and supporting consumer preferences:



Improving Sourcing Quality



Organic Reformulation



Idea Generation Partnerships

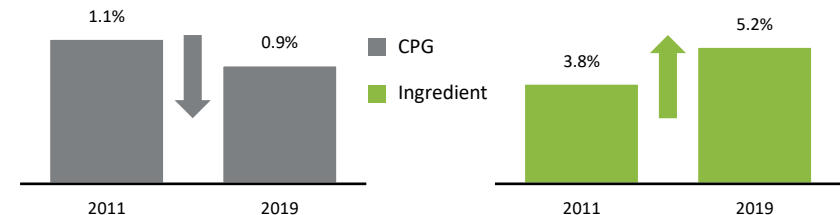


Target Market Analysis



Trademarked Inputs

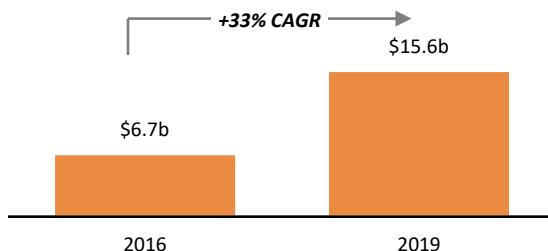
### R&D Expenditure as % of Revenue <sup>(2)</sup>



## SUPPLIER PARTNERSHIPS GROWING NEW CATEGORIES

### Total U.S. Sports Nutrition Market <sup>(3)</sup>

+8.9% Projected CAGR from 2020 to 2027

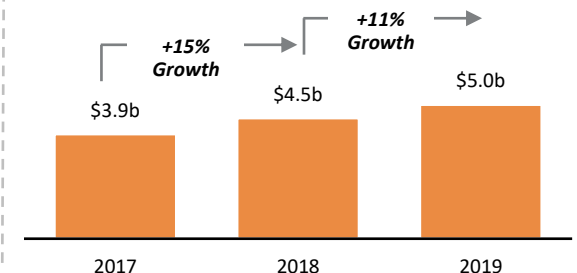


### Sparkling Water <sup>(4)</sup>

**+118%**  
Sparkling Water Market Sales Grew from 2013 to 2018

**+10%**  
2018 to 2023 CAGR;  
The Sparkling Water Market Will Continue to Grow Robustly

### Total U.S. Plant-Based Food Market <sup>(5)</sup>



(1) Hartman 2019. (2) CPG average includes HSY, NESN, KHC, GIS, K, CAG, MKC, CPB, SJM and POST. Ingredients average includes GIVN, IFF, KRZ, SY1, SXT, INGR, CHR, NZYM B, BCPC. (3) Grand View Research (4) Beverage Industry: Bottled Water Bubbles Over with Growth. (5) Supermarket News: Plant-based food retail sales reach \$5 billion.



# INDUSTRY & SECTOR TAILWINDS | SUPPLY CHAIN INTEGRITY IS BECOMING INCREASINGLY IMPORTANT

BAIRD



Consumers Demand Increasing Traceability, Sustainability and Credibility of the Supply Chain



**Purity & Credibility** – 73% percent of consumers are happy to pay a higher retail price for a food or drink product made with ingredients they recognize and trust <sup>(1)</sup>



**Environmental Sustainability** – 72% percent of consumers are happy to pay a higher retail price for a food or drink product made sustainably <sup>(2)</sup>



**Safety & Reliability** – 11% CAGR in USDA recalls, political risk (tariffs) and pandemics (COVID-19) driving 38% of companies to change food safety procedures and standards <sup>(3)</sup>

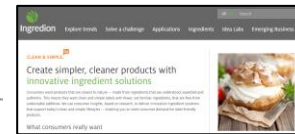


Ingredient Suppliers are Demanding More from their Supply Chains

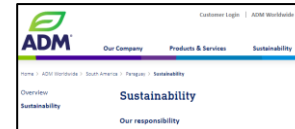
## Select Private Sector Initiatives



- KnownOrigins program allows ingredients to be identifiable and traceable back to producers
- Non-GMO Project Verified ingredients include: cane sugar, various vegetable oils, syrups and dry corn products



- Since 2004, TRUETRACE program has protected non-GMO purity through global and third-party-audited best practices
- Complete traceability to farmers and land of agricultural products



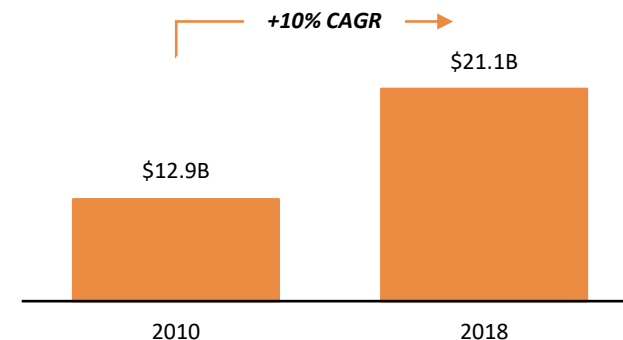
- To meet the growing demand for high quality plant-based proteins, ADM expanded production of non-GMO soy proteins
- ADM is looking to meet consumer trends by developing gluten free, clean label, organic, lower sodium, plant-based protein and high fiber

## SELECT ADVANCEMENTS DRIVEN BY SUPPLY CHAINS



## Sales of Organic Foods Has Skyrocketed <sup>(4)</sup>

**#1**  
Ranked Criteria by Consumer; All Natural, Non-Artificial and Non-GMO Products <sup>(1)</sup>



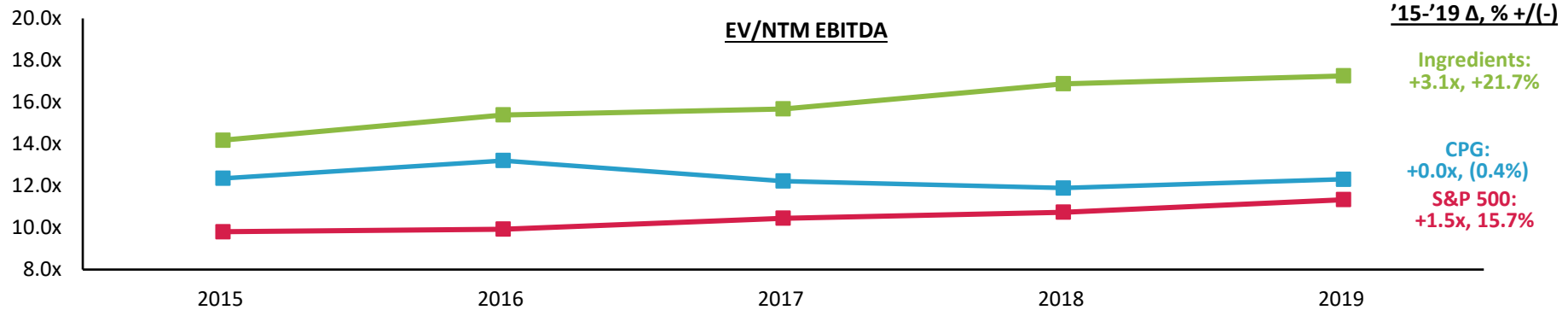
Source: Kerry Future of Food.

(1) Label Insights and the Food Marketing Institute. (2) International Food Information Council. (3) Clean label customers, subset of all label-conscious consumers. (4) Consumer Reports: GMO Foods: What You Need to Know.

# ENTERPRISE DRIVERS | KEY VALUE DRIVERS FOR INGREDIENT SUPPLIERS

BAIRD

## INGREDIENTS SUPPLIERS VALUATION IMPROVING FASTER THAN CPG AND S&P500 COMPANIES <sup>(1)</sup>



### Patented Products & Proprietary Techniques

- Patented products & proprietary techniques drive pricing power, higher gross margins and improved valuations



### Strong In-House R&D Capabilities

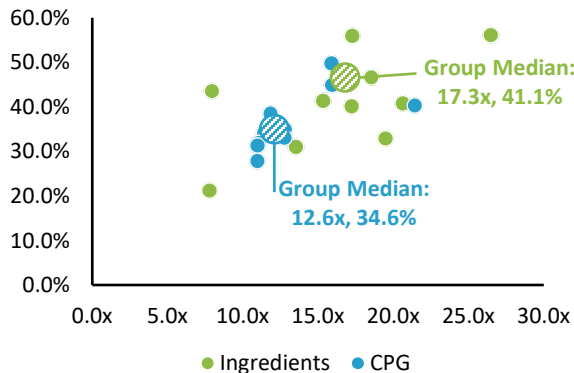
- The rapidly evolving landscape and expansion of importance in the supply chain has driven rapid expansions of IP portfolios



### High-Quality, Sophisticated and Sustainable Supply Chain

- Companies are actively reviewing and modifying their existing supply chains to cater to changing demands

### Gross Margin vs. Valuation <sup>(1)</sup>



### Rapid Expansion of IP Portfolios



Granted **415** patents in the United States since 2000



**2,000+** patents granted or pending



Filed **45** new patent applications in 2019



**6,500+** patents granted or pending



Over **3,600** active patents



**110+** patents in the U.S and overseas

### Top Actions Taken to Address Food Safety

(% of companies responding, 2017)





*Please Contact the Baird Team for Potential Ingredients Opportunities  
Related to the Themes Outlined in this Document*

Robert W. Baird & Co. Incorporated

227 West Monroe Street, Suite 5500  
Chicago, IL 60606

15 Finsbury Circus, Eldon St.  
London, United Kingdom

North American Team

European Team

**Glen Clarke**  
Managing Director  
+1 (312) 609-4481  
GClarke@rwbaird.com

**Mike Gilkes**  
Vice President  
+1 (312) 609-4490  
MGilkes@rwbaird.com

**John Bastian**  
Vice President  
+1 (312) 609-7067  
JBastian@rwbaird.com

**Dan O'Brien**  
Associate  
+1 (312) 609-2554  
DPOBrien@rwbaird.com

**Boris Partin**  
Director  
+44 7880 850 869  
BPartin@rwbaird.com

## DISCLAIMERS

This is not a complete analysis of every material fact regarding any company, industry or security. The opinions expressed here reflect our judgment at this date and are subject to change. The information has been obtained from sources we consider to be reliable, but we cannot guarantee the accuracy.

Baird is exempt from the requirement to hold an Australian financial services license. Baird is regulated by the United States Securities and Exchange Commission, FINRA, and various other self-regulatory organizations and those laws and regulations may differ from Australian laws. This report has been prepared in accordance with the laws and regulations governing United States broker-dealers and not Australian laws.

**Copyright 2020 Robert W. Baird & Co. Incorporated. No part of this publication may be reproduced or distributed in any form or by any means without our prior written approval. However, you may download one copy of the information for your personal, non-commercial viewing only, provided that you do not remove or alter any trademark, copyright or other proprietary notice.**

## OTHER DISCLOSURES

UK disclosure requirements for the purpose of distributing this report into the UK and other countries for which Robert W Baird Limited holds an ISD passport.

This report is for distribution into the United Kingdom only to persons who fall within Article 19 or Article 49(2) of the Financial Services and Markets Act 2000 (financial promotion) order 2001 being persons who are investment professionals and may not be distributed to private clients. Issued in the United Kingdom by Robert W Baird Limited, which has offices at Finsbury Circus House 15 Finsbury Circus, London, EC2M 7EB, and is a company authorized and regulated by the Financial Conduct Authority.

Robert W Baird Limited ("RWBL") is exempt from the requirement to hold an Australian financial services license. RWBL is regulated by the Financial Conduct Authority ("FCA") under UK laws and those laws may differ from Australian laws. This document has been prepared in accordance with FCA requirements and not Australian laws.

