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***Opportunities
in the GCC food
landscape***

**Strategies for
success**

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Executive summary



After a long period of double-digit growth, per capita spending in the Gulf Cooperation Council (GCC)¹ food sector is leveling off. Regional players are seeking mergers and acquisitions (M&A) opportunities to expand their portfolios and sustain growth, but there is a lack of viable targets. Nevertheless, it is still possible for companies in the sector to grow by tapping into changes in the way people spend money on food. As in other countries at this point in their development, the consumption mix in the GCC is shifting away from staple products and toward value-added, convenient, and healthier alternatives. Moreover, some government policy initiatives, such as Saudi Arabia's 50 percent tax on carbonated soft drinks and 100 percent tax on energy drinks, will make healthier options even more attractive to consumers. This represents a significant opportunity for established food players in the region, along with startups, entrepreneurs, and companies in related segments such as food distribution.

To better understand the opportunity, we analyzed the dynamics of the food and beverage sector in the region and compared the results to the same sector in several relevant countries. Based on that analysis, we identified the four most promising categories — snacks, spreads, prepared meals, and ready-to-drink (RTD) beverages — along with an overarching theme that cuts across categories: healthier diets. These areas and the theme offer attractive investment prospects in the GCC region regardless of the maturity and industry structure of the various categories.

To capitalize on this opportunity, regional players have several strategic options. They can build their offerings organically, although this approach is time-consuming and requires strong in-house innovation capabilities. Alternatively, companies can agree joint ventures with international players to localize some of the innovations in these categories, or they can invest in successful startups abroad and then help these firms expand in the GCC.

Slowing growth

The food and beverage sector in the GCC is developing, due to increased participation in the workforce and a government push for healthier diets. Long term, rising prosperity is also a factor (although the recent decline in oil prices has slowed the increase in income levels). For food and beverage companies, understanding these trends and how they affect consumer purchases can help unlock growth.

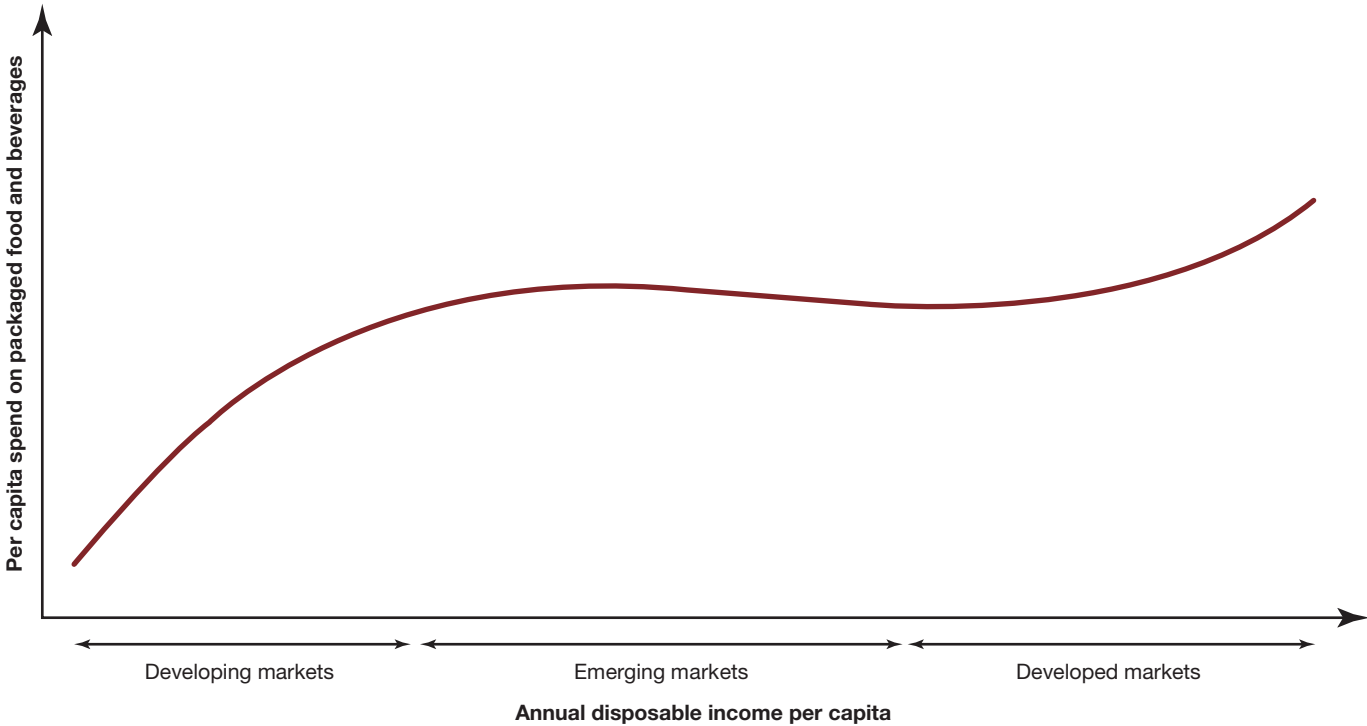
As economies develop, food spending follows a predictable pattern: it initially rises dramatically for people in developing markets, then levels off for consumers in emerging markets, and finally rises again in developed markets (*see Exhibit 1*). For example, per capita spending on food and non-alcoholic beverages in emerging markets such as Croatia, Poland, and Turkey was essentially flat over the past five years, according to Euromonitor. Much of the GCC is at this same point in its development, in which overall spending is steady and is unlikely to increase in the near term.

In response to this plateau in per capita spending, many regional companies are seeking to sustain growth and widen their portfolios through M&A. Yet that is a difficult path. The industry is still relatively fragmented in the region, which means there are few attractive targets. Numerous companies still focus on staples for lower-income segments and have not caught up with changes in demand. In addition, a number of companies have complex ownership structures, often linked to large family conglomerates that are not interested in selling. As a result, the GCC has seen only about two deals per year on average in each country from 2007 to 2016, far fewer than in larger and more developed markets such as France, which had 59 deals per year, the U.K., with 52 deals per year, or the U.S., with 136 deals per year.²

In response to this plateau in per capita spending, many regional companies are seeking to sustain growth and widen their portfolios through M&A.

Exhibit 1
Average spend per capita tends to be flat in emerging markets

Average spend per capita in US\$, adjusted for purchasing power parity at constant 2015 prices



Source: Euromonitor; Strategy& analysis

Changing consumption patterns

Although overall spending is flat, the consumption mix in the GCC is changing in a manner that is both predictable and promising for consumer packaged goods (CPG) companies. As disposable incomes rise in emerging markets, consumers become more sophisticated, and their attitudes regarding food change. They shift their purchases away from staples and toward more value-added products. For example, rather than buying powdered milk (as they have in the past), they buy fresh milk. Rather than juice from concentrates, they buy fresh juices or smoothies.

These shifts happen in part because consumers become more health-conscious and are willing to spend more for higher-quality, fresh products. A second factor is that the retail landscape becomes more complex. As economies advance, there is greater penetration of modern retail trade outlets, such as supermarkets and convenience stores, which can carry a wider range of refrigerated products. As a result, value-added products proliferate at this middle stage in a country's development.

In the GCC, Kuwait and Saudi Arabia are emerging markets, with other GCC members not far behind. Qatar and the UAE are exceptions as they have income levels in line with developed markets. The difficulty is that local CPG manufacturers have not yet begun to adapt their product portfolio to meet the changing nature of demand. Many of these companies are relatively strong in terms of supplying staples, but they do not offer the value-added products that GCC consumers increasingly want.

Five promising options

The context of strong fundamentals and an immature industry means that there are specific product and thematic opportunities for regional manufacturers, investors, and entrepreneurs. To better understand these opportunities, we analyzed product launches in several relevant countries over the past 10 years. The analysis specifically looked at product categories that showed strong growth and innovation, with a low penetration of private-label offerings. In addition, we assessed the potential and likelihood of success for a new player to enter a category and differentiate itself among established players.

The analysis revealed four promising categories in the GCC over the next 10 to 15 years — snacks, spreads, prepared meals, and RTD beverages — plus one attractive theme that cuts across categories: healthier diets.

Snacks

The snacks category includes mainly candy, gum, bars (including cereal and energy bars), salty and fruit snacks, and chocolate. Among the countries we considered, this category presented the highest number of new product launches over the past 10 years, primarily in two main segments:

Health-oriented products

Much of the growth in the snacks category comes from a shift among consumers toward healthier products, which is just beginning to take hold in the GCC and is likely to play out for the foreseeable future. Rather than candy bars, people are seeking low-sugar alternatives. Similarly, fitness-oriented consumers are opting for high-protein bars, usually marketed to boost energy or help people recover from a workout.

Various health-related government initiatives in the GCC should spur this demand for healthy snacks. For example, the Ministry of Health in Saudi Arabia is launching awareness campaigns to combat obesity (which afflicts roughly 30 percent of the population over age 15) and diabetes (roughly 18 percent of the population between 20 and 79).

One benchmark example, Snyder's-Lance, a major salty snacks company in the U.S., recently repositioned its overall portfolio to focus on healthier products. In 2015, the company launched a new division, called Clearview Foods, to produce innovative and healthy snacks such as multigrain quinoa tortilla chips. Snyder's-Lance has also conducted a series of strategic acquisitions, including Diamond Foods in 2016. Diamond is a leading snack company that develops innovative, natural snacks such as organic barbecue-flavored potato chips.

Those measures have helped the company outperform its competitors. Of the eight core brand categories in which Snyder's-Lance competes, it holds the first and second positions in five of them.³

Premium products

In addition to healthy snacks, there is a growing demand for products that have higher-quality ingredients. This is especially true in categories such as chocolate bars, where consumers are seeking more expensive and cocoa-rich products for their higher quality and natural ingredients. In response, chocolate companies are differentiating themselves through unusual cocoa sources and ingredients that provide more complex flavors. For instance, luxury ice cream brand Magnum recently launched premium chocolate bars made from high-quality Rainforest Alliance Certified cocoa.

Spreads

The spreads category includes savory products such as dips, meat pastes, vegetable pastes, and sandwich fillers, along with sweet spreads from caramel, fruit, honey, nuts, and syrups. The snack category showed the highest overall number of launches over the past 10 years, and spreads showed the highest growth in new product launches, as well as a higher penetration of new players.

The trend of greater health awareness is spurring stronger demand for certain types of spreads, such as those that contain antioxidants and high protein levels, or spreads that are fortified with vitamins and minerals. Some manufacturers are adding new flavor profiles to healthy spreads, such as almond butter with garlic, or peanut butter with maple syrup.

In the U.S., Yumbutter is a fast-growing startup that launched in 2011. The company's packaged nut butters are made with nuts (peanut, cashew, and almond, among others), seeds, and organic superfoods such as chia seeds, hemp seeds, goji berries, and lucuma powder. The company recently began offering the product in portable pouches, an innovation that has boosted sales growth. The number of stores carrying the new version has grown significantly, and the company is on track to double its production volume.⁴

Meals

The meals category includes prepared meals that only require heating, meal kits (in which the consumer needs to assemble some prepared ingredients), sandwiches/wraps, ready-to-eat salads, and instant noodles, pasta, and rice.

This category shows the widest gap between developed markets and the GCC, where the market for prepared meals is at the earliest stages. That gap will likely close a decade or so from now. In Saudi Arabia, the increasing participation of women in the workforce will almost certainly lead to greater demand for convenient products such as prepackaged meals.

This trend is already well-established in developed markets, where new products reflect this demand. For instance, U.K.-based BOL Foods is a fast-growing startup launched in 2014 that produces and sells packaged healthy, ethnic, ready meals. BOL Foods has a line of globally inspired meals, such as Italian tomato courgetti, Moroccan chicken tagine, and salads based on Japanese, Californian, Persian, and Mediterranean flavors.

RTD beverages

The RTD category includes RTD coffee, RTD tea, meal replacement drinks, and carbonated drinks based on juice or water. It does not include soft drinks such as colas.

As with prepared meals, there is a significant dearth of RTD offerings in the GCC compared to developed markets, especially in chilled products. Soon, however, some regulatory trends could stimulate activity in the market. Saudi Arabia and the UAE are imposing steep taxes on sugary soft drinks and energy drinks, as part of their efforts to fight obesity and diabetes. Other countries in the GCC may launch similar measures. These taxes have led to an uptick in sales for RTD beverages in other markets that took similar measures, such as Mexico.

In addition, the maturing retail sector, which is bringing greater penetration of modern trade outlets carrying greater ranges of chilled products, should lead to growth in this category. (Many RTD beverages require refrigeration.)

In addition to healthy snacks, there is a growing demand for products that have higher-quality ingredients.

In developed markets, there is a growing demand for RTD beverages. For instance, Talking Rain is a leading U.S.-based beverage company that produces carbonated water drinks in several flavors. To achieve sustainable growth, the company has repositioned its marketing strategy in recent years, to focus on “healthy refreshment.” According to the company, sales exceeded US\$650 million in 2015, up from about \$10 million in 2010. Similarly, VitHit is an Irish company that develops fruit- and plant-based vitamin water with a focus on healthy and exotic flavors, using plant-based sweeteners.

Developed markets have seen growing demand for meal-replacement drinks. These products help people gain weight (by supplementing meals), lose weight (by skipping meals), or meet other nutritional needs.

Last, in the coffee segment, RTD cold-brew coffee has seen significant growth between 2011 and 2016, from both emerging brands (such as Cold Brew, Two Bears, and others) and established players (Starbucks). These products are particularly popular among millennials.

Cross-category health








There is also an attractive theme that spans the four categories: healthier diets. Looking at new product launches over the past 15 years, many are based on attributes such as organic, vegan, low sugar, or gluten-free (*see Exhibit 2*).

For example, Hain Celestial, a leading U.S.-based company with products in food and beverage categories (including tea, soy milk, biscuits, bread, baby food, and soup), has positioned itself as a seller of organic and natural products through innovation and acquisitions. In 2014 and 2015 alone, the company closed six acquisitions. Both revenue and earnings have grown steadily. (Hain Celestial is publicly held on the Nasdaq exchange.) As a result, the company reported net sales in 2015 of more than \$2.7 billion, a 25 percent increase over the previous year.

Exhibit 2

New product launches increasingly have healthy attributes

Percentage of new products launched with healthy features, 2001–2016

Product attribute	2001	2003	2005	2007	2009	2011	2013	2015	2016
 Low/no/reduced allergen	2%	3%	3%	4%	7%	9%	15%	20%	23%
 Gluten-free	2%	2%	3%	3%	6%	8%	14%	18%	21%
 No additives/preservatives	7%	8%	8%	14%	16%	17%	21%	21%	21%
 Organic	9%	7%	7%	10%	11%	11%	15%	15%	16%
 GMO-free	1%	1%	2%	1%	2%	3%	6%	8%	11%
 Vegan	1%	0%	1%	1%	2%	3%	5%	7%	9%
 Low/no/reduced sugar	2%	5%	6%	6%	5%	5%	6%	6%	8%

Note: Data are for France, Malaysia, Turkey, U.S., and U.K.

Source: Mintel; Strategy& analysis

Strategic options to seize the opportunity

Companies seeking to enter the promising categories discussed in the preceding section have several strategic options.

Building up offerings organically

In developed markets, a number of startups have entered these categories and succeeded. For example, Kind, a U.S. manufacturer of snack bars, launched in 2004. The company now controls 12 percent of the U.S. snack bar market, according to Euromonitor.

Entrepreneurs in the GCC can follow a similar approach. Established food manufacturers can also use a greenfield strategy, or seek co-packing agreements to limit up-front manufacturing investments. However, building innovation capabilities within established organizations can be time-consuming and costly.

Establishing joint ventures with international players

Regional players can also strike joint ventures with international players to localize some of these innovations and get them onto store shelves in the region. For example, Al Safi, a leading dairy company in Saudi Arabia, partnered with Danone in 2001 to form Al Safi Danone. The new venture offers a wide range of dairy and juice products based on Danone's expertise and tailored for local tastes. Today Al Safi Danone has a leading position in the value-added segment in dairy and is the market maker in a number of sub-categories, including drinking yogurt, ready-to-eat desserts, and beverages that combine fruit juice and milk.

Our analysis of product launches in relevant countries over the past 10 years shows that highly innovative companies (characterized by the number of new product launches) are not present in significant numbers in the GCC region yet and could be targets for joint ventures. For example, in the snacks category, 40 percent of the top 50 innovative companies in our analysis have no presence in Saudi Arabia. For RTD beverages, meals, and spreads, that number increases, to 74 percent, 80 percent and 84 percent, respectively.

In order to accelerate the formation of a joint venture, investors and regional players can also invest in emerging players or startups in other markets and help them get established in the GCC. This play was deployed in the fashion industry in late 2016, when Dubai-based Mohammed Alabbar, through his Symphony Investments, acquired a 4 percent stake in Milan-based online retailer Yoox Net-a-Porter and later announced that they would form a joint venture to create a new platform for online luxury retail in the Middle East.

Conclusion

The food and beverage industry in the GCC is at an inflection point. By looking at markets that are further along in their economic development and studying successful product launches in those markets, it is possible to identify the most promising growth opportunities for the region over the next five to 15 years. Companies that want to target these categories will need to understand consumer preferences in the region and quickly build up the necessary innovation capabilities, potentially by partnering with established players in other markets and leveraging their expertise. Those that do so will be able to capitalize on this unique opportunity.

Endnotes

¹ The GCC countries are Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates.

² Strategy& analysis of data from Thomson Reuters.

³ Eric Schroeder, “Five Achievements Drive Momentum at Snyder’s-Lance,” *Food Business News*, February 14, 2017 (http://www.foodbusinessnews.net/articles/news_home/Financial-Performance/2017/02/Five_achievements_drive_moment.aspx?ID=%7B53F1A161-3571-41B7-B27D-248BA3EDAF4D%7D).

⁴ “Branson quick-solves a sticky problem and lays groundwork for dramatic Yumbutter growth,” Emerson Industrial, press release, 2015 (<http://www.emersonindustrial.com/en-US/branson/news-and-events/news/Pages/Branson-quick-solves-a-sticky-problem.aspx>).

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