

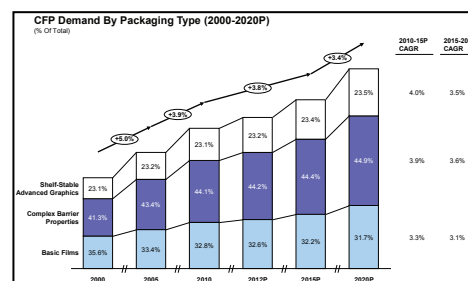
## Customer & Market Due Diligence Of Snack Foods Flexible Packaging Converter: Assessing Risk And Validating Management's Growth Projections

**The Challenge:** Our client, a middle-market PE firm, was evaluating a proprietary deal to acquire a flexible packaging converter primarily serving the snack foods industry. Following a stagnant period during the 2008/2009 recession, the target experienced impressive 25% annual growth in the subsequent 2 years and management was projecting 13% CAGR over the next 5 years based on the success of its current product portfolio. Attracted by the target's recent success, its high-profile client base, and its optimistic growth outlook, our client asked us to conduct a 4-week customer & market due diligence to validate management's projections and evaluate several potential investment risks: (1) the threat from larger packaging companies; (2) potentially high replacement CapEx requirements given the \$3-5MM cost of flexographic presses; and (3) the target's reliance on 9 key customer accounts.

**Snack Foods Flexible Packaging Market & Risk Analysis:** Gotham developed a reliable market and customer fact base from: 50+ interviews with key competitors, with snack foods customer brand and packaging managers, with printing equipment OEMs, and with industry experts; extensive secondary research (e.g., packaging/customer end-market industry associations) on printing press equipment technologies, snack foods end-market dynamics, and flexible packaging market and competitive dynamics; and analysis of company and market data (e.g., customer-level sales projections, SymphonyIRI snack foods sales data).

### Target Well-Positioned As A Strong Player In Its Snack Foods Packaging Market Niche...

Gotham conducted a robust analysis of the flexible packaging market – by material type (aluminum foil, paper, plastic), by packaging type (e.g., bags, pouches), by function (e.g., moisture control, overwrap, marketing appeal), and by end-market (e.g., snack foods, frozen foods, dairy). After segmenting the product landscape into basic films, complex barrier properties, and shelf-stable advanced graphics, and assessing the target's capabilities, we established that the target competes exclusively in the \$3.8B shelf-stable advanced graphics segment, requiring the highest degree of printing expertise. From Gotham interviews with customers and our profiling of 30+ large and small converters, we concluded that while the overall market for flexible packaging is dominated by several large players (e.g., Bemis, Printpack) vertically integrated through the entire value chain (including film making), the target has successfully carved out a strong position in its snack foods packaging niche through a focus on superior service and product innovation, minimizing competitive threats.



### ...However, Investment In Pouch-Making Capability Likely Required For Target To Remain Competitive

From our thorough analysis of the pouch market/competitive dynamics, we determined that stand-up pouch demand was large (~\$1.5B) and growing (7% CAGR), with target's snack foods end-market representing 25% of total demand. Currently, the target produces rollstock for pouches, but outsources its pouch-forming business to 3rd party companies. Through extensive interviews with target's competitors, we found that a majority of mid-size and all large converters already have in-house pouch-forming capabilities. Gotham then performed a make vs. buy analysis of the target's outsourced pouch-forming volumes, pouch suppliers' margins, associated costs, and required investment, and established that at the target's current volumes, bringing the capability in-house is the more economically attractive option, with a 2-3 year payback on equipment investment.

### Target's Flexo Presses Reflect Major Advances In Printing Technology, Providing Likely 8-10 Year CapEx Window

To assess the CapEx risks from flexographic press replacement, Gotham analyzed the printing press technology landscape (e.g., flexographic, rotogravure, lithographic, digital) across multiple performance/feature dimensions (e.g., web-width, print quality, speed). We found that digital printing, the only potential challenge to flexography's leading position (75% share), is unlikely to be a viable alternative in wide-web printing for at least another 10+ years due to its current constraints in speed and web-width. Our review of the technological evolution of wide-web flexography and our interviews with leading press manufacturers (e.g., W&H) established that major industry revolutionizing technologies (e.g., the 8-color press, gearless operation, sleeve-based rolls) came about in the 1980s and 1990s, with more recent (e.g., 10- and 12-color presses) and expected technology advances primarily of the incremental variety. The target's presses reflect revolutionary advances and are in-line with the equipment utilized by its competitors in snack foods packaging and should remain competitive for the next 8-10 years, and converters routinely use presses of different generations for jobs of different lengths to optimize operations – making significant CapEx requirements for the target unlikely in the near-term.

### Target's Top "Snack Food" Customers' Growth Outlook More Tempered Than Management's Projections

To validate target's projected revenue from each of its 9 top customers (97% of projected growth), Gotham determined the growth outlook for each top customer's products/brands for which target supplies packaging. To do so, we established market size, customer's brand positioning, and key trends (e.g., decline in cookie vending machine sales, continued growth in private label snacks) for each snack segment (e.g., cookies, crackers, chips, pretzels, other salted snacks, dried fruits). While a few of target's top customers were well positioned in growing markets (e.g., kettle chips, rice crackers), several of the target's largest customers were facing challenging market conditions which were likely not reflected in target's growth projections.

**The Outcome:** As a result of Gotham's customer & market and risk due diligence findings, our PE client moved forward to close the deal.