

Animal Instinct

There continues to be significant investor interest in the area of animal health. In the last 12 months, the private equity press has reported a number of UK mid-market deals across a range of sub-sectors including veterinary services, online pharmacies, pet food, wearable technology for the animal health sector and diagnostics. There are a number of factors which make this market attractive for investors:

Large and Highly Stable Market

Pet ownership in the UK is both large and stable, with just under 50% of the UK's 26 million homes owning a companion animal. It is estimated that Britons spend an astonishing £4 billion per annum on feeding, caring for and entertaining their pets. Recent research from the Pet Food Manufacturers Association estimated that there are around 16 million cats and dogs in the UK, and a further 3 million smaller animals such as birds, chickens, snakes and hamsters. Whilst propensity for pet ownership varies by region (the South West of the UK and Wales having the highest concentration), statistics point to a highly stable pet population over the last decade. The industry has proven remarkably resilient during the recession, with

UK spend on pet food outstripping GDP by 1.5%. Recent research found that families have cut back on expenditure on eating out, holidays and utilities, rather than reducing their spend on family pets.

“Humanisation” of the Family Pet

The pet care industry increasingly refers to the “humanisation” of family pets, whereby the family dog and cat are now seen as companions / part of the family unit rather than just pets, and require “parenting” rather than “ownership”. This has manifested itself in a huge increase in the amount of pet accessories and toys purchased, with an estimated £145 million alone spent each year on Christmas presents for pets, and 15% of pet owners sending their pet a Christmas card. Reasons for this are complex but academic studies by the British Psychological Society point to the emergence of smaller families, single-person households, and a rise in the elderly population. In short, companion animals are filling the emotional and physical void left by people. There is now far more understanding and interest in areas such as animal psychology (several brands of dog antidepressants are now on the market), preventative pet



health plans and the nutritional content of food given to pets. In relation to food, whilst sales of pet food globally are growing by circa 4% per annum, growth of natural and organic pet food is expected to be three times this - over 12% per annum - between now and 2015, with many of the current products in the market having greater nutritional constituents than that of human food.

The Protein Problem

Whilst much of the investment to date has been on companion animal care, the role of food producing animals has also come into sharp focus in recent years. With the global population expected to exceed nine billion by 2050 (seven billion currently) and an increasing desire from emerging markets for more Western based diets, analysts predict a 70% increase in protein output is required to meet demand. Such an increase in output is only achievable through agricultural yield efficiencies, improved veterinary provision and medicine innovation. Add to this significant public health concerns driving government, consumer and food producer focus on food security and traceability and the scene is set for a number of innovative businesses models to emerge which fundamentally challenge the status quo. In the UK context, the Governments re-organisation of the TB testing regime coupled with the end to milk quotas in 2016 looks set to reshape the structure of the domestic production animal landscape.

Advances in Veterinary Care

Over recent years there has been significant innovation in the range of treatments and medicines available to the veterinary profession to treat animals. Some of this has been driven by the continued growth in pet insurance, which is now purchased by approximately 25-30% of pet owners according to Pet Plan, the UK market leader in pet insurance. Whilst older conditions such as rickets and distemper have now been largely eradicated, there has been significant growth in drugs and services which treat conditions such as diabetes, arthritis and more acute conditions such as renal failure. Specialist referral centres are now able to offer a range of treatments across orthopaedic care, ophthalmology, soft tissue conditions and spinal injury, all of which are increasing the life expectancy of companion animals and indeed the lifetime cost to a pet owner. Whilst animal health represents just 2.5% of the global pharmaceutical market, consolidation in this market continues as the large players innovate in new drug development to offset the fall in the number of high-volume patented products which can be produced on a generic basis. This year has seen the industry consolidate further with the acquisition of Novartis by Eli Lilly for \$5.4 billion, following quickly on the back of the Zoetis IPO in 2013. Such activity will also inevitably drive deal activity and deal flow for larger buy-out players as product portfolios are divested and the animal health pharmaceutical companies focus on a smaller and more concentrated portfolio of brands.

In summary, the animal health market continues to be

a highly rated and highly sought after area for investors. Whilst the defensive characteristics of the market are well documented and understood, changing demographics, global demand for protein, a consolidating supply chain and an increasingly scientific approach to animal health are leading to new opportunities and niche areas of growth for investors.



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