



VMS CDMO Market

Assessing Key Value-Drivers in a Dynamic Market

September 2023

These materials are intended to supplement a discussion with L.E.K. Consulting. These perspectives will, therefore, only be meaningful to those in attendance. The contents of the materials are confidential and subject to obligations of non-disclosure. Your attention is drawn to the full disclaimer contained in this document.



Within the large and growing U.S. nutritional supplement market, the VMS CDMO market is an attractive investment opportunity with strong market fundamentals

Market fundamentals



- The U.S. nutritional supplement market is large (~\$61B RSP in 2022) and is expected to continue growing, driven by several factors such as the growing interest from the next generation of consumers (e.g., millennials, Gen Z) and product innovation
- Gummies, liquids and other **non-pill formats have historically outpaced overall market growth**; expansion of formats has increased the need for CDMOs' manufacturing expertise

Customer dynamics



- VMS CDMOs serve **multiple customer segments**, each with different priorities and propensities to outsource VMS production
- **Outsourcing to CDMOs is expected to increase** due to increased regulations, manufacturing expertise, & speed to market

Competitive landscape



- The **CDMO competitive landscape is fragmented**, segmented largely by modality type (e.g., tablets, gummies) and breadth of services
- As contract manufacturers aim to gain scale and breadth to better serve customers' needs, the **desire to serve as a one-stop shop has continued to push consolidation**

Investor implications



- **Investor interest in the space has been high**, contributing to **high deal valuations**, with many recent deals focused on companies that offer format differentiation (e.g., gummy), in-house R&D, customer lists that include access to growth brands, and turnkey capabilities

The U.S. Nutritional supplement market is large (~\$61B) and grew at record rates during COVID before slowing down in 2022; growth is projected to return to pre-COVID rates by 2024

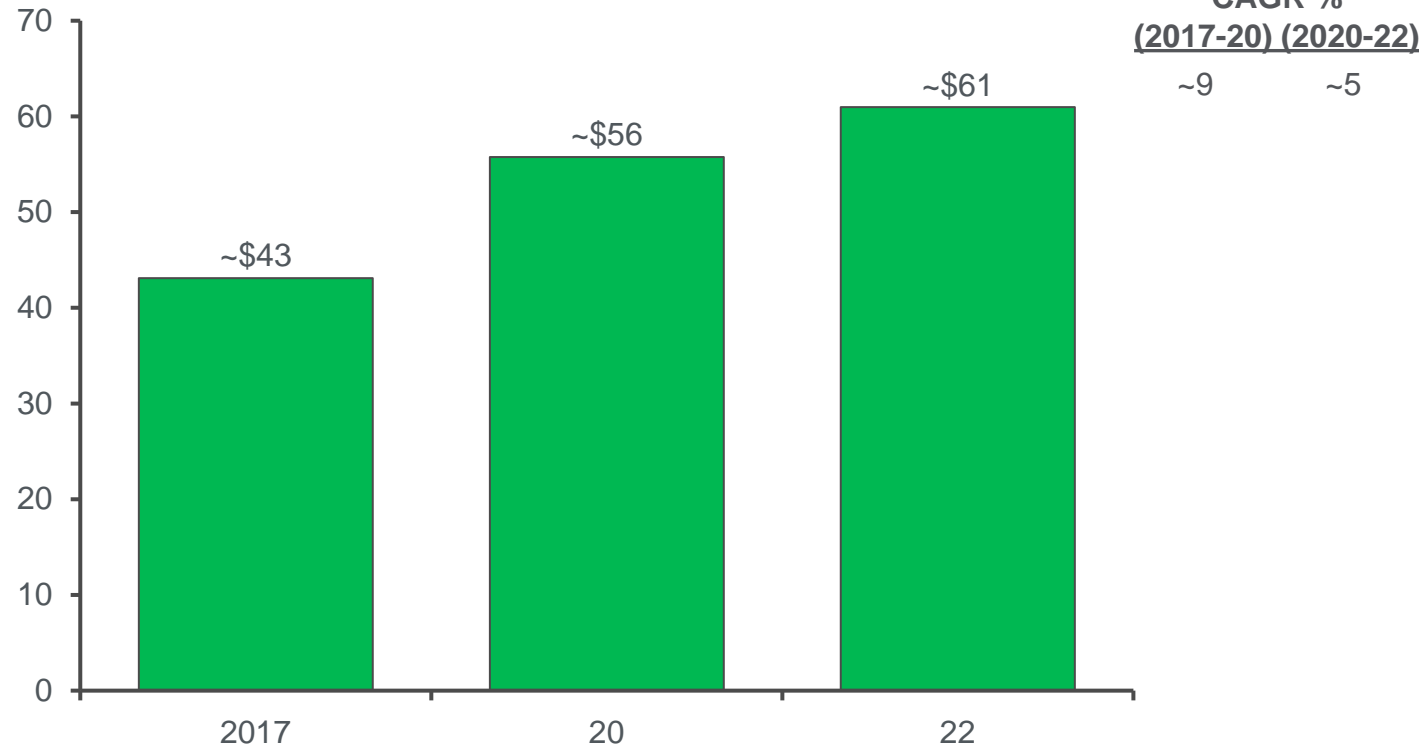


Market fundamentals

U.S. nutritional supplement market size*

(2017-22)

Billions of USD (\$RSP**)



- Nutritional supplement sales in the U.S. have **historically experienced mid-single digit annual growth**; however, during the **pandemic, sales increased substantially** as consumers focused on their health and well-being
- Even after record pandemic-driven growth in 2020, **sales continued to grow in 2021**. However, in **2022, the market normalized**, driven by **inflation** and other economic concerns
- Market participants expect **growth to return to pre-COVID projections by 2024**

“... Coming off the record growth in 2020, NBJ had projected a normalization in 2022, but the reality of the year was a further slowdown than anyone had previously anticipated ... Even with this slowdown, NBJ expects sales will be back on track with pre-COVID projections by 2024 and pulling back ahead by 2025 ...”

- Nutritional Business Journal, April 2023

Note: *PR Newswire press release based on NBJ data **Retail sale price

Source: NBJ; PR Newswire: “Supplement market more than \$5B higher than pre-pandemic expectations, according to NBJ’s 2022 Supplement Business Report”; L.E.K. research and analysis

There are several enduring trends that are expected to continue driving U.S. VMS growth

Market fundamentals

U.S. VMS market: Growth trends

Trend	Commentary
Secular	1 Aging demographics <ul style="list-style-type: none"> Older consumers have the highest frequency usage of supplements, and an aging U.S. population (50+ expected to grow at 1.1% p.a. from 2020-30 vs 0.7% p.a. for overall population) will continue to grow at the VMS consumer base
	2 Millennial and Gen Z segment growth <ul style="list-style-type: none"> Millennials have the highest average annual VMS spend and have experienced faster median earnings growth than older generations (4.5% p.a. for millennials vs <3% p.a. for boomers), making them strong contributors to VMS growth Gen Zs are increasingly entering the category driven by the proliferation of digital-native brands and increased social media presence
	3 Growing focus on health and wellness <ul style="list-style-type: none"> The COVID-19 pandemic and increasing prevalence of chronic health conditions are contributing to a shifting consumer mindset towards prevention and purchases of supplements; there was a 7 percentage point increase in percent of the population that consumed dietary supplements from 2020-21
Consumer trends	4 Growth of digital native brands <ul style="list-style-type: none"> Digital native brands have been growing (Amazon sales of VMS have increased at 25% p.a. from 2019-23), and they have used social media heavily to engage potential consumers and broaden the VMS category's exposure and appeal; this has led to increased awareness of the category, especially among younger generations
	5 Experiential well-being <ul style="list-style-type: none"> Condition-specific supplements, which have become more prevalent broadly within the VMS market, are increasingly permeating into experiential well-being applications, such as sleep, stress, mind and mood, cognition, thus enabling VMS extension to a broader consumer population
	6 Clean label <ul style="list-style-type: none"> Within VMS, consumers are increasing seeking clean label and other health attributes (e.g., organic, non-GMO) and many are willing to pay a premium for these products, driving premiumization within the market
Product / brand trends	7 Innovation <ul style="list-style-type: none"> Product formats: Consumers continue to seek non-pill formats such as gummies, liquids, and single-serve powders (e.g., stick packs), which are easier and / or more enjoyable to consumers Ingredients: VMS companies are becoming more innovative with their use of natural ingredients such as Ashwagandha, broadening VMS's appeal among consumers looking for more natural or herbal remedies Science-first: Brands such as Thorne and Nutrafol are taking a science-first approach as consumers are increasingly seeking more scientific evidence of efficacy (e.g., clinical trials)

Source: L.E.K. research, and analysis

Experiential well-being, personalized nutrition, and women's health segments are among some of the sub-markets that are projected to outpace broader market growth

Market fundamentals

Faster growing areas within nutritional supplements

Experiential Well-Being

Sleep: A significant portion (~30%) of U.S. adults experience insomnia, leading to higher demand for sleep support

Mood and mental: Growing rates of anxiety, depression, and awareness of stress and mood management have been tailwinds

Brain health: An aging population coupled with increased awareness of cognitive health VMS offerings has driven demand for this segment

Women's Health

Recent interest in women's health has been exacerbated by heightened awareness / education, product innovation, the rise of digitally native brands, a broader preventative health movement, and societal trends decreasing the taboo nature of certain women's health (e.g., UTIs, menopause, sexual health, beauty)



Microbiome Health

Tailwinds from increasing consumer awareness / interest in digestive health, innovations in microbial research & digestive supplements, and a shift towards personalized nutrition provide an opportunity to capitalize on microbiome health (e.g., probiotics, prebiotics, immunity support)



Beauty from Within

Heightened demand for organic and natural sources from the health-conscious aging population and a greater focus on holistic skin health has led to a growing interest in nutricosmetic products (e.g., collagen hair vitamins, biotin, Omega-3)



Personalized Nutrition

Given a renewed consumer focus on self-care and accelerated awareness of personalized services, brands are investing in the space (e.g., AI driven recommendations, online quizzes, tele-health consultations, digital tracking apps, personalized supplement subscriptions) to create more personalized solutions



Source: Forbes Health, NBJ, Nutraceuticals World, New Hope Network, L.E.K. research and analysis

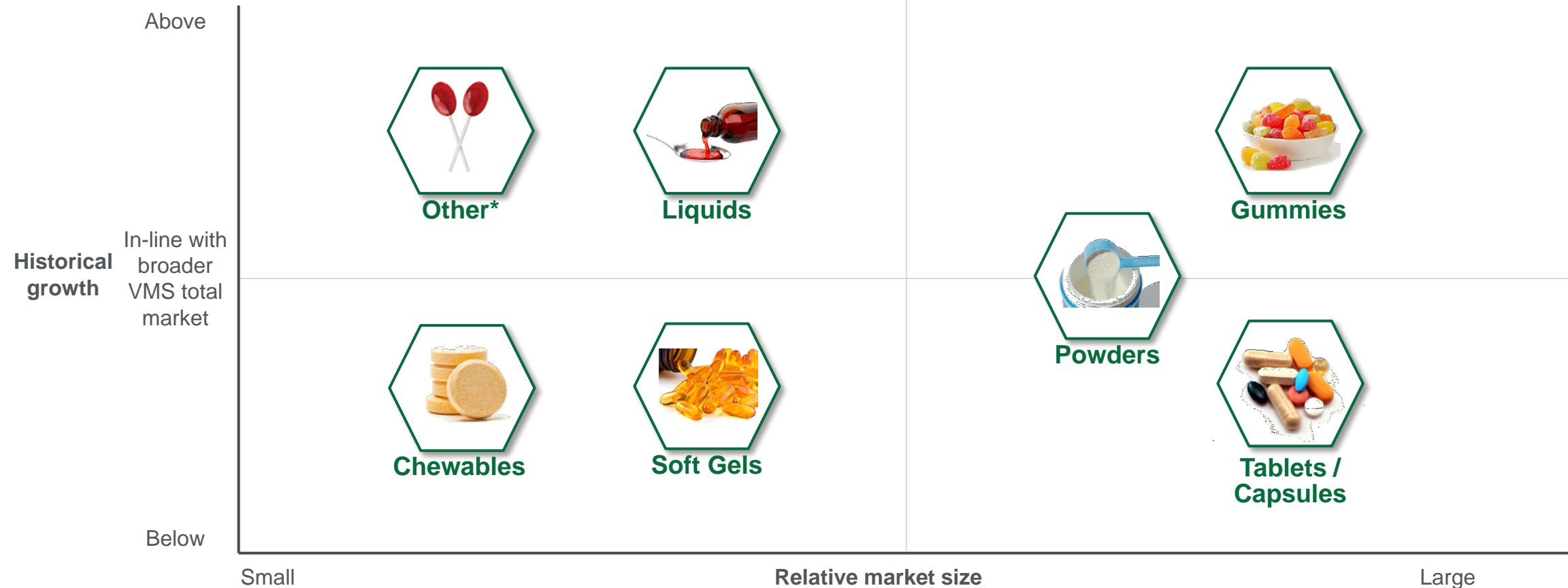
Gummies, liquids, and other non-pill innovative formats (e.g., candies) have driven strong historical growth in the VMS market; expansion of formats supports the need for CDMOs' manufacturing expertise



Market fundamentals

DIRECTIONAL

Nutritional supplement modality segments[^]
(2022)








Note: *Other includes formats such as effervescent, candies, lozenges, lollipops; ^ Modalities placed into each quadrant based on relative size and historical growth relative to broader market; however, positioning within a given quadrant is illustrative and not indicative of relative performance

Source: L.E.K. research, and analysis

CDMO market growth is expected to outpace the broader VMS market as manufacturing is increasingly outsourced to reduce regulatory burdens, increase speed to market, and manage complex products



Customer dynamics

 <p>Reduces regulatory compliance burden</p>	<p><i>The FDA has increased VMS manufacturing requirements and inspections with the development of the Office of Dietary Supplement Programs which will likely lead to greater outsourcing to CDMOs</i></p>
 <p>Provides manufacturing expertise</p>	<p><i>For all customer types, CDMOs provide an attractive option with their manufacturing expertise in R&D, sourcing, testing, formulation, and production across modalities</i></p>
 <p>Enables focus on core competencies</p>	<p><i>Outsourcing work to CDMOs frees up internal resources to focus on critical drivers of revenues (e.g., ideation, marketing, sales)</i></p>
 <p>Increases speed to market</p>	<p><i>Enables customers to swiftly test product concepts and move quickly from idea to finished product when they lack the robust internal manufacturing capabilities to do so</i></p>
 <p>Allows for excess / spillover capacity</p>	<p><i>VMS brands that cannot handle the full capacity of production demands may outsource to CDMOs who can manage larger order quantities</i></p>

VMS CDMOs serve multiple customer types with propensity to outsource differing for each major segment; MLM / specialty and private label brands account for the majority of VMS outsourcing



Customer dynamics

U.S. VMS market, segmented by customer type

Integrated manufacturers

- Vertically integrated companies that manufacture the majority of their own products
- Typically utilize external CDMOs for a select modality or capacity needs to supplement in-house capabilities

Example brands:



Propensity to outsource:

Low (30-40%)

MLM and specialty brands

- Branded companies that outsource formulation, sourcing, manufacturing, and packaging for most / all products
- Value CDMOs that offer order flexibility, short lead times and have robust / innovative R&D capabilities

Example brands:



Propensity to outsource:

High (75-85%)

Private label brands

- FDMC / ecommerce retailers that sell their own private label brand alongside branded competitors
- Retailers almost always outsource formulation & manufacturing given their lack of manufacturing expertise

Example brands:



Propensity to outsource:

Very High (90%+)

Broader market trends such as increasing VMS regulations, growth of digitally native brands, and expansion of innovative formats are impacting brands' higher propensity to outsource to CDMOs



Customer dynamics

Trends impacting outsourcing propensity



Increasing VMS regulations

- Regulatory agencies are setting increasingly stringent requirements for approval, including the need for independent lab testing apart from the CMO
- International regulatory agencies have also set stricter requirements for VMS products, forcing manufacturers to adapt to these new standards or stop selling to certain global markets entirely

Dynamic



Growth of digitally native brands

- Digitally native VMS brands have increasingly emerged in recent years, selling DTC / on Amazon, with a focus on brand identity & marketing, and a higher likelihood to outsource manufacturing



Expansion of innovative formats

- Non-pill formats (e.g., gummies, liquids) have gained significant share of supplement sales in recent years, increasing the need for brands to manufacture across modalities

- Increasingly complex requirements from governing bodies will make regulatory compliance more difficult, resulting in higher outsourcing rates to CDMOs who have the expertise and personnel to keep up with regulatory changes

Impact on CDMO outsourcing

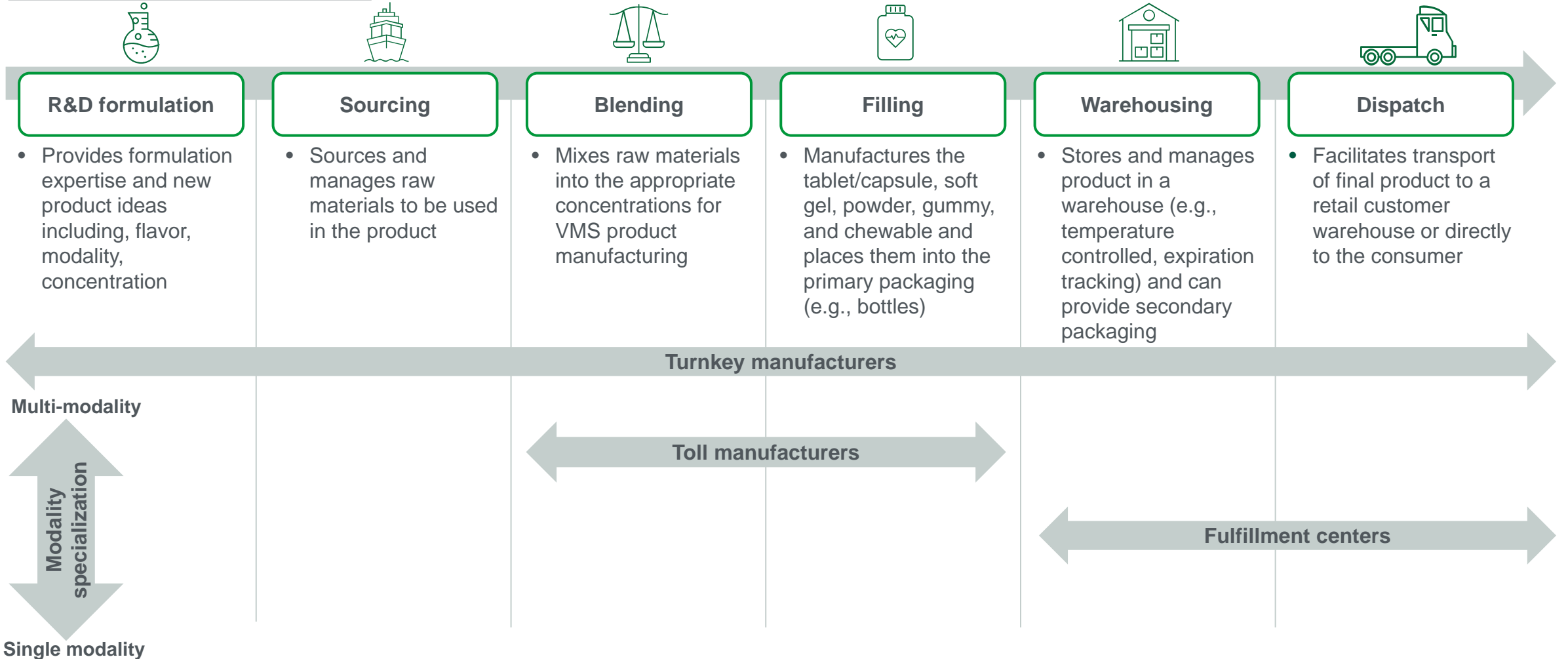
- Digitally native VMS brands often do not have manufacturing capabilities and rely on CDMOs

- With higher demand for emerging VMS modalities (e.g., gummies, liquids), brands have increased their propensity to outsource as they don't have the internal capabilities across modalities

The VMS contract manufacturer space is very fragmented with most players offering multiple services and modalities to customers, with several of the larger players offering a broad suite of solutions

Competitive landscape

VMS contract manufacturer services



Source: L.E.K. research and analysis

The industry continues to see consolidation, as contract manufacturers look to gain scale and breadth to better serve the needs of customers

Competitive landscape

Customer preference for one-stop-shops

- Consolidation has, in part, been driven by customer preference for **working with CMOs** that can produce products **across various modalities**
- Small brands want to **reduce vendor management time** and **volume risk concerns**, whereas large brands care about **mitigating capacity risk** through a broader supply base

“... The industry has experienced consolidation as brands seek greater stability. They value a CMO with a large range of modalities ...”

- Former VP, Natrol LLC

Consumer demand for innovation

- Consumers are demanding **increasingly sophisticated products** to support their health & wellness goals
- **Many capabilities** around the **latest science**, **access to new ingredients**, **better delivery format technologies** and **improved efficacy** can be **acquired through a CDMO** that has narrow and deep expertise versus created in-house

Recent transactions of contract manufacturers have primarily been driven by players already in the VMS space looking to gain capacity or capabilities

Competitive landscape

Transactions within U.S. VMS contract manufacturing (2021-22)






Target	Acquirer	Date	Target details	Acquirer details
 USPharmaLab <i>Innovative Natural Solutions</i>	 Biofarma group	May 2023	US Pharma Lab is a fast-growing and innovative CDMO that specializes in the custom development, manufacturing and distribution of nutraceuticals (e.g., vitamins, minerals)	Biofarma Group is a global CDMO with six manufacturing sites and five R&D labs where they develop, produce and package supplements, probiotics and cosmetics
 BEST FORMULATIONS	 SIRIO	Jul. 2022	Best Formulations is a contract manufacturer of products including nutraceuticals and dietary supplements; the company also offers services including packaging and formulation development	Sirio is a global nutraceuticals contract manufacturer for the supplement industry, with global operations, development, and manufacturing capabilities spanning most dosage forms, including soft gels
 HEALTH WRIGHT PRODUCTS	 iff	Apr. 2022	Health Wright Partners is a contract manufacturer of products in capsules and has been manufacturing IFF's probiotics products for years	IFF is a multinational conglomerate that merged with DuPont health and wellness divisions in 2020 expanding its offering in Health & Biosciences probiotics and natural extracts / botanicals
 bettera brands	 Catalent	Aug. 2021	Bettera Brands is a private label and branded manufacturer of gummy vitamins	Catalent is a multinational corporation and global provider of delivery technologies, development, drug manufacturing, biologics, gene therapies, and consumer health products
 CAPSTONE NUTRITION LIFE IMPROVED	 INW (Backed by Cornell Capital)	Jun. 2021	Capstone Nutrition manufacturers vitamins, supplements, and general wellness products	INW is a manufacturer of dietary supplements, sports nutrition, and personal care products, providing contract manufacturing, product development, and formulation using automated processes
 FoodScience	 WIND POINT PARTNERS	Mar. 2021	FoodScience provides formulation and private labeling for vitamins, minerals, probiotics, and other product offerings; the company also provides contract manufacturing for modalities including tablets, soft gels, powders, and creams	Wind Point Partners is an American private equity firm focused on growth capital investments and leveraged buyouts in middle-market companies across the consumer products, industrial products, and business services sectors

Source: Capital IQ; Company websites; Highlander Partners; Nutra Ingredients-USA; L.E.K. research and analysis

Key:	
	Target acquired by CMO / corporation
	Target acquired by PE

Investor interest in the space has been high, with many recent deals focused on companies with format differentiation, in-house R&D, customer lists with high-growth brands, or turnkey capabilities

Investor implications

-  **Diverse customer list** with a mix of **long-term relationships** & track record of attracting **emerging brands**
-  **Exclusivity agreements** with customers or **difficult-to-replicate formulas** to minimize churn
-  **In-house R&D** that acts as an **external innovation engine** for customers
-  **Value-add capabilities** (e.g., turnkey, R&D) that enable **strong gross margins** above category players
-  **Track record of growth and stability** with demonstrated ability to **absorb macro shocks** (e.g., input pricing volatility, inflation, etc.)

The VMS CDMO market has attractive fundamentals and potential value creation opportunities for prospective investors

Investor implications

Key reasons to invest

- ✓ **Large and growing** underlying VMS market
- ✓ Segments, such as **non-pill formats** (e.g., gummies, liquids) or **experiential well-being** product categories (e.g., sleep, mind and mood) have **above average market growth**
- ✓ Brands are **increasingly outsourcing to CDMOs** due to factors such as increased regulation, CDMOs' expertise, and speed-to-market
- ✓ The **highly fragmented** competitive landscape **creates opportunity for roll-up M&A**

Ways to create value

- ✓ Creating **one-stop-shop solutions** for customers across a breadth of modalities and / or service offerings
- ✓ Investing in sales infrastructure to **acquire new customers** as VMS is a dynamic market and having a pipeline of new business as consumer preferences evolve is critical
- ✓ Investing in a team that is focused on **improving efficiencies, capacity utilization, and customer management / prioritization** to maximize gross margins
- ✓ Driving efficiencies through **supply chain optimization** and scaled **back-office operations** (e.g., HR, Finance, IT)
- ✓ Introducing **AI-powered solutions** to potentially streamline more manual aspects of business (e.g., quoting, sourcing, QA)

L.E.K. and Houlihan Lokey contacts



Alex Evans
Managing Director
Los Angeles
a.evans@lek.com
+1 310 435 0533



Geoff McQueen
Managing Director
Los Angeles
g.mcqueen@lek.com
+1 310 209 9822



Anna Ondik
Senior Engagement Manager
Chicago
a.ondik@lek.com
+1 312 229 6803



Houlihan Lokey



Susan Roddy
Managing Director
New York
sroddy@hl.com
+1 212 497 4195



Preetam Talukdar
Vice President
New York
ptalukdar@hl.com
+1 212 497 7925

See subsequent pages to learn more about L.E.K. Consulting and Houlihan Lokey

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in 1983

 **21**
offices

 **~200**
partners

 **~2,200**
staff



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Worked on some of the **most significant** Health & Wellness **deals** in recent years

Worked with **all 3** of the largest **VMS specialty** retailers & brands

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#1 Global Advisory Firm

Corporate Finance

- No. 1 Global M&A Advisor Under \$1 Billion
- Leading Capital Markets Advisor Raising Approximately \$25 Billion Over the Past Two Years

2022 M&A Advisory Rankings Global Transactions Under \$1 Billion		
Advisor	Deals	
1 Houlihan Lokey	381	
2 Rothschild	369	
3 JP Morgan	217	

Source: Refinitiv. Excludes accounting firms and brokers.

Financial Restructuring

- No. 1 Global Restructuring Advisor
- \$3.0 Trillion of Aggregate Transaction Value Completed

2022 Global Distressed Debt & Bankruptcy Restructuring Rankings		
Advisor	Deals	
1 Houlihan Lokey	58	
2 PJT	30	
3 Lazard	29	

Source: Refinitiv.

Financial and Valuation Advisory

- No. 1 Global M&A Fairness Opinion Advisor Over the Past 25 Years
- 1,000+ Annual Valuation Engagements

1998 to 2022 Global M&A Fairness Advisory Rankings		
Advisor	Deals	
1 Houlihan Lokey	1,232	
2 JP Morgan	1,030	
3 Duff & Phelps (Kroll)	938	

Source: Refinitiv. Announced or completed transactions.

Financial Sponsors Coverage

- No. 1 Global Advisor to Private Equity Firms
- 1,000+ Sponsors Covered Globally

2022 Most Active Global Investment Banks to Private Equity Firms		
Advisor	Deals	
1 Houlihan Lokey	242	
2 Lincoln International	192	
3 Deloitte	190	

Source: Pitchbook.

#1 M&A U.S. Advisor in Consumer, Food & Retail

2022 M&A Advisory Rankings All U.S. Consumer, Food & Retail Transactions		
Advisor	Deals	
1 Houlihan Lokey	21	
2 Goldman Sachs & Co	18	
3 William Blair & Co	17	
4 JP Morgan	16	
5 Lincoln International	13	
5 Robert W Baird & Co Inc	13	

Source: Refinitiv. Excludes accounting firms and brokers.

14
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Worldwide

130+
CFR
Financial Staff

100+
Total CFR Deals
Past Three
Years

600+
Cross-Border
Transactions
Since 2011



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Transaction Pending

Qunol[®]

has agreed to be acquired by

sanofi

Sellside Advisor

Trufood
MANUFACTURING

has been acquired by

MUBADALA
CAPITAL

Sellside Advisor

LifeStyles SINCE 1905 **SKYN**[®]

has been acquired by

LINDEN⁷

Sellside Advisor

ARDIAN

has acquired

Biofarma
group

Financing Advisor and M&A Co-Advisor

Deerland
Probiotics & Enzymes

has been acquired by

ADM

Sellside Advisor

ARCADIA
CONSUMER HEALTHCARE

has been acquired by

Bansk

Sellside Advisor

Zesty Paws[®]

has been acquired by

H&H Group
inspiring wellness

Sellside Advisor

mommy's
BLISS[®]

has been acquired by

SPC
SWANDER PACE CAPITAL

Sellside Advisor

nuun

has been acquired by

Nestlé
HealthScience

Sellside Advisor

SMARTY
PANTS[®]
VITAMINS

has been acquired by

Unilever

Sellside Advisor

care/of

has been acquired by

BAYER

Sellside Advisor

ZARBEE'S
NATURALS

has been acquired by

Johnson & Johnson
CONSUMER INC.

Sellside Advisor

Perrigo

has sold its VMS business to

IVC
INTERNATIONAL
VITAMIN CORPORATION
ENRICHING YOUR HEALTH

Sellside Advisor

CAPTEK[™] | Softgel
International
ENCAPSULATING QUALITY

has been acquired by

SPC
SWANDER PACE CAPITAL

Sellside Advisor

SANTA CRUZ
NUTRITIONALS

has been acquired by

ROUNDTABLE
HEALTHCARE PARTNERS

Sellside Advisor

Note: Tombstones included herein represent transactions closed from 2013 forward

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