

KEYNOTE INTERVIEW

Delivering the goods



*A long-term approach and a 'don't panic' mentality are key in an industry that is particularly vulnerable to macroeconomic headwinds, says **Rupert Howard**, head of 3i's UK private equity team*

Private-label businesses that manufacture products sold under a retailer's brand name – from food to furniture; cosmetics to computers – will always represent a key part of the economy. While the perceived volatility of the sector makes some investors nervous, Rupert Howard, head of 3i's UK private equity team, believes experienced firms can access a host of growth opportunities from consumer businesses.

Q Why has 3i adopted consumer and private label as a focus area?

We've recently shifted from a country-first, sector-second model to being a sector-led organisation. In particular, we decided to focus on consumer and private label because we have deep experience already in the sector – at least

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half of our portfolio in private equity is in these types of businesses – and we've carved out private label specifically because we have a distinguished track record with such companies. We find there isn't an inherent conflict between private-label and branded assets – after all, they can happily coexist on your shelf at home.

Additionally, internationalisation is a core tenet of value creation in our portfolio. We invest in businesses that are either international already or are looking to internationalise. Some of our consumer businesses have started in one country, and we've helped them expand internationally.

Q What characteristics do you look for in businesses in this space?

The most important factor to us is that we want to invest in companies that have some sort of winning proposition compared with their peers. The micro vertical is a secondary consideration, though we do tend to look for slightly niche businesses.

We focus on finding interesting businesses that are the right size for us and are in a consumer or private-label category, that we like and understand. Then we ask: why does this business have the right to win? What is its *raison d'être*? Why are consumers buying its products? Why are retailers stocking its products?

Another thing we find useful is around multi-unit roll-out. If you have

a winning proposition in any particular niche and are able to identify a multi-unit roll-out opportunity, it's a great way to create value. You can take an attribute or a business model and apply that in order to create a winning proposition across many verticals.

We stay away from businesses that rely on highly discretionary spending. Of course, there's always some element of discretion in consumer industries, but some subsectors are ficker than others. For example, fashion: you could have the perfect blue T-shirt, but suddenly everyone decides they want red T-shirts. That's a risk that's completely outside your control.

Q How do you manage your exposure to cyclical trends?

You intuitively know whether something is highly cyclical or not. For example, it's pretty easy to see that travel is highly correlated to disposable incomes: when people have money, they tend to travel more, and when they're feeling a bit poorer, they cut back on travel.

On the other hand, there are businesses that can operate within a sector that are much less cyclical, or much less exposed to cyclical variances. For example, we're invested in a travel business called Audley Travel that skews towards a customer base that has higher disposable income and is less exposed to cost-of-living pressures. For this specific subset of customers, travel is something they will protect and prioritise.

The other way of dealing with cyclicity is through a balanced portfolio. If you've got a business that's especially exposed to a discretionary element, you can try and balance your portfolio by having businesses that are less exposed.

Having some cyclicity in your portfolio isn't always the worst thing – investors across our industry have done well in cyclical categories from riding the upside.

Q How do you manage macroeconomic and geopolitical disruption?

A thread that runs through our organisation is a 'don't panic' mentality. We've been through Brexit, we've been through covid-19. We've been around since 1945 as an institution, and in that time, we've learned that having a cool head and a longer-term outlook pays dividends. You can jump up and down about tariffs, for example, but then a month later the tariff numbers change, and all that stress is redundant.

You do need to have management teams that have expertise in managing supply chains in their respective subsectors. In the pet food industry, for example, there has been supply chain dislocation almost continuously over the past few years, for a variety of reasons – covid, trouble in the Red Sea, ports being congested, and so on. So, what do you do? You take a longer-term approach. One example here is to build up inventory levels, so if there's a shock, you have a buffer and it's not going to impact your customers.

Disruption can also present opportunities. A lot of people at the moment are focused on artificial intelligence. There is a new Industrial Revolution on our doorstep, and it's important for us to ask what that is going to do to our portfolio companies. We must be sure we can help them reposition and leverage these technologies.

We've seen businesses come unstuck as if they've underinvested in proper systems and processes. A lot of people have invested in businesses they thought were mature, but actually turned out to be relatively undeveloped when they looked under the hood. We've passed on a number of opportunities that from the outside looked super attractive because, as we've gone through due diligence, we've realised a significant amount of day-one investment would be needed to support future growth.

Specific to supply chains, if you don't have the right systems and

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forecasting processes in place – if you don't know what your stock levels are – how are you going to adapt quickly when ports are closed? The strength of the IT backbone is integral to our investment decision-making process. It's definitely an increasing area of focus.

Q How optimistic are you that opportunities will continue to grow over the next 10-plus years?

I'm bullish. Consumer and private label is a huge part of the economy, for the simple reason that people will always need to eat and drink. They will always need to spend their money on goods and services.

What's really interesting about the sector is that it's constantly evolving. There's always an opportunity for new businesses to emerge and new trends to evolve.

People do, of course, change their priorities on how they spend their money: 20 years ago, nobody would have thought about buying premium pet food. But over time, because of other macro factors – people having children later, people working from home more – pets became an integral part of the family, and so people want to provide them with better food. A whole new multibillion-dollar sector has emerged, when previously you fed your dog scraps off the table. ■