



SECTOR SCOPE: In 2005, the U.S. **Pet Products & Services** market eclipsed \$36 billion, approximately doubling its size over the last ten years. The industry is comprised of five major categories: (1) food (40.2% of total market); (2) veterinary care (24.0%); (3) supplies and over-the-counter medicines (24.0%); (4) services, including grooming and boarding (6.9%); and (5) live animal sales (4.7%).

GROWTH OUTLOOK:

- ▶ Total U.S. pet industry spending is expected to reach \$38.4 billion in 2006, an increase of over 30% from 2002 and a 6.8% CAGR.
- ▶ Capstone expects the market to grow between 4% and 6% annually over the next three to five years.
- ▶ According to the American Pet Product Manufacturers Association (APPPMA), approximately 69 million U.S. households, or 63% of total, have at least one pet, an increase of more than 35% since 2002. Approximately 45% of U.S. households own more than one pet.

Sources: Company reports and the APPMA.

TRENDS & DEMAND DRIVERS:

- ▶ **Demographic Shifts Driving Market** – The number of pets and total industry spending has increased as the Baby Boomer generation ages and seeks home companionship through pets. The number of “empty-nesters” and dual-income households without children has also been on the rise since 1998 and represents a growing number of households spending more on pets than in the past.
- ▶ **Pet “Humanization” Driving Sales** – New pet products and services have emerged from the “humanization” of companion animals, including pet gift purchases; special travel accommodations; niche accessories and clothing; and various services traditionally reserved for humans such as behavioral or mental consultation.
- ▶ **Advancements in Pet Medical Care** – Advancements in over-the-counter therapies, as well as enhanced veterinarian services, continue to drive demand for pet health products and services. The APPMA reports that an increasing number of pets are provided nutritional supplements at home. In addition, many human medical procedures have recently been adapted for pet care, broadening the scope of pet care alternatives and augmenting segment growth.
- ▶ **Retailers and Distributors Expanding Vertical Integration** – Big-box retailers and pet product distributors, such as Central Garden and Pet, are making strategic acquisitions of manufacturers with strong brands. Other retailers and distributors are also private labeling more products to improve margins, reduce their dependency on other third party manufactures, and gain market share.
- ▶ **Mergers and Acquisitions on the Rise** – Attractive macro-economic and demographic factors, coupled with a highly fragmented competitive landscape, are driving increased consolidation. Recent acquisitions by Del Monte and Spectrum Brands, as well as Central Pet’s sustained M&A activity, exemplify current market behavior. Capstone expects consolidation activity to remain robust over the next 12 to 24 months.

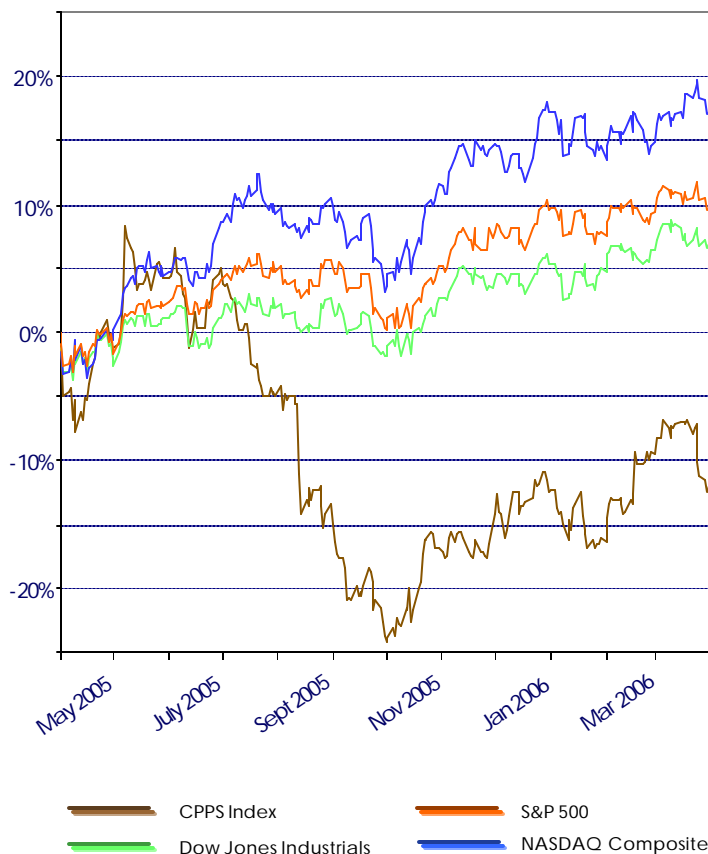
MARKET PERFORMANCE:

Public Equity Markets

Company Name	Ticker Symbol	Enterprise Value/ LTM		
		Revenue	EBITDA	EBIT
Central Garden & Pet Co.	CENT	1.0x	10.8x	12.8x
Petco Animal Supplies Inc.	PETC	0.7x	6.3x	9.7x
Petsmart Inc.	PETM	1.0x	8.7x	12.5x
Spectrum Brands, Inc.	SPC	1.2x	9.1x	11.5x
VCA Antech Inc.	WOOF	3.3x	15.5x	17.4x
Virbac Corp. *	VBAC	1.4x	10.6x	13.7x
Average		1.4x	10.2x	12.9x
Median		1.1x	9.9x	12.7x
Harmonic Mean		1.2x	9.5x	12.5x

* Virbac was acquired by Interlab, S.A.S on 12/13/05
Enterprise Value = Market Capitalization + Debt - Cash.
Source: Capital IQ and company reports.

Capstone Pet Products & Services Index



The Capstone Pet Products & Services Index is a market capitalization weighted index that includes the following companies: CENT, PETC, PETM, SPC, WOOF, VBAC (April 2005 to April 2006).



Capstone Partners LLC is a leading national investment banking advisory firm dedicated to assisting middle market entrepreneurs through complex M&A and financing transactions.



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HIGHLIGHTS FROM GLOBAL PET EXPO 2006 – Industry Participant Feedback

- ▶ **Rising International Presence** – Exhibitors and participants alike reported a noticeable increase in the number of international competitors, partnerships and strategic sourcing options. This trend presents a competitive threat to some and growth opportunities for others.
- ▶ **Increasingly Competitive Environment** – The larger manufacturers and distributors are gaining share through acquisition. Large retailers continue to streamline their supply chains and increase private label portfolios, limiting available shelf space. These trends have significantly increased competition and pricing pressure, negatively affecting small, independent companies.
- ▶ **Continued Capital Markets Activity** – The recent up tick in capital markets activity and greater attention from financial services providers have focused the interest of many market participants. Strong market fundamentals and strategic considerations will continue to drive interest in the space from both strategic and financial buyers over the next 12 to 24 months.

Source: Industry participants, company reports, and Capstone Partners research.

DEAL ACTIVITY:

Selected M&A Transactions

Date	Target	Buyer	Description	Deal Size (\$mm)	Enterprise Value / Revenues
3/15/2006	Kraft Foods: Milk-Bone Dog Food	Del Monte Foods Co.	Manufactures and markets biscuits, chewy treats, and crunchy treats for dogs, under the brand name Milk-Bone.	\$580.0	3.2x
3/1/2006	The Meow Mix Company	Del Monte Foods Co.	Manufactures dry, specialty, and indoor & outdoor foods and snacks for cats.	705.0	2.8x
2/2/2006	Aspen Pet Products, Inc.	Doskocil Manufacturing Co. Inc.	Manufactures and distributes products for pets including functional pet accessories, such as leashes, collars, and dog toys; dog, cat, and bird toys; pet care products; dog chews; and rawhides.	N/A	N/A
1/19/2006	Farnam Companies, Inc.	Central Garden & Pet Co.	Provides animal care products including horse products, such as leather cleaner and conditioner, moisturizer with solar guard, digestive upset, conditioner, mosquito control, feeds treats, and equine health supplements.	287.0	1.8x
01/03/2006	Pet Zone Products Ltd.	OurPets Co.	Produces pet products for dogs, cats, and wild birds including feeder/feeding products and other pet accessories.	1.8	N/A
02/23/2006	Breeder's Choice Pet Foods Inc.	Central Garden & Pet Co.	Manufactures and markets pet foods for dogs and cats including foods, treats, skin products, and coat care products, as well as fur care products.	25.0	N/A
12/13/2005	Virbac Corp.	Interlab, S.A.S.	Manufactures pet and companion animal health products including dermatological, parasitocidal, dental, and certain pharmaceutical products.	36.9	1.4x
10/27/2005	Gutwein & Co., Inc.	The Scott's Miracle-Gro Co.	Provides wild bird food, including black oil sunflower seed, bird mix, thistle seed, suet, and socks.	77.0	2.9x
9/27/2005	Buckeye Feed Mills, Inc.	Mars, Incorporated	Engages in the manufacture and marketing of animal feed.	N/A	N/A
9/2/2005	Jungle Laboratories	Spectrum Brands, Inc.	Manufactures aquarium and pond products for fish care.	29.0	2.5x
8/29/2005	Doane Pet Care Enterprises, Inc.	Teachers' Private Capital	Manufactures dry pet food for dogs and cats in the United States.	840.0	2.6x
8/1/2005	Healthy Pet Corporation	Allied Capital Corporation	Provides animal care services, including education and preventive care, surgical treatments, boarding, and grooming.	64.4	2.3x
7/7/2005	Stylette, Inc.	Doskocil Manufacturing Co. Inc.	Offers pet products, including bowls, feeders, waterers, scoops, litter box, litter mat, and pet carriers.	N/A	N/A
6/14/2005	Pet Pal Corp.	JAKKS Pacific Inc.	Provides pet toys, pet treats, and other related products.	10.6	N/A
6/2/2005	Pets International, Ltd.	Central Garden & Pet Co.	Supplies pet care products, including cages and home accessories, cages and homes, and carriers for pets.	35.0	1.0x
5/23/2005	Pet's Choice	VCA Antech Inc.	Engages in the ownership and operation of companion animal veterinary hospitals in the United States.	60.0	1.7x
5/2/2005	My Pet, Inc.	The Hartz Mountain Corporation	Engages in designing and producing pet toy products.	N/A	N/A
4/26/2005	CP Medical, Inc.	Theragenics Corp.	Designs, manufactures, and supplies medical equipments for surgical, veterinary, and brachytherapy markets.	25.6	4.3x
4/15/2005	Summit Anesthesia Solutions	Molecular Imaging Products Company	Manufactures and markets reconditioned medical equipment for research and private practice veterinarians.	N/A	N/A
3/15/2005	Tetra GmbH	Spectrum Brands, Inc.	Manufactures and markets aquarium and pond products.	558.5	2.1x
3/11/2005	Harper Pet Products, Inc.	The Hartz Mountain Corporation	Engages in the manufacture and distribution of pet chews.	N/A	N/A
3/2/2005	LEO Animal Health A/S	Montagu Private Equity	Engages in the development and marketing of veterinary diets, care products, and medicines for cats and dogs in Denmark and internationally.	N/A	N/A
				Mean	2.0x
				Median	2.2x
				Harmonic Mean	1.8x

Sources: Capital IQ, company reports and SEC filings.