CPG Investor Perspectives - Show 3
What is your participation in this segment so far?
What do you look for to invest here?
What else should we know about this segment?

In today's show, you'll hear investor perspectives on COVID-19's impact on the CPG sector.

This is Investor Perspectives, I'm the host of Investor Connect, Hall T Martin, where we connect startups and investors for funding.

It's the time of COVID-19. The consumer product goods space is currently undergoing tremendous change across the U.S. The lockdown has disrupted the supply chain, manufacturing, and distribution. Retail is undergoing transformation as consumer products move online and the market shifts to functional benefits prioritizing wellness. We have investors and startup founders describe the impact of COVID-19 on the consumer product goods market.

Our guests are:

1. **Ronan McGovern, Founder, Point 5 Brewing**
2. **Paul Janowitz, CEO & Founder, MANTRA Labs**
3. **Sarah Foley, Partner, SWAT Equity Partners**
4. **Richard G Riccardi, CEO, Riccardi Ventures**
5. **Cisco Sacasa, Operating Partner, Bee Cave Capital**

I hope you enjoy this episode.

For more episodes from Investor Connect, please visit the site at: http://investorconnect.org

Check out our other podcasts here: https://investorconnect.org/
For Investors check out: https://tencapital.group/investor-landing/
For Startups check out: https://tencapital.group/company-landing/
For eGuides check out: https://tencapital.group/education/
For upcoming Events, check out https://tencapital.group/events/

For Feedback please contact info@tencapital.group

Our first guest is Ronan McGovern, Founder, Point 5 Brewing

[00:09:24] **Hall Martin:** ~~S~~o far, how far have you gotten with Point 5?

[00:09:29] **Ronan McGovern:** So we launched in the Shopify store right at the beginning of August. So I would say we're certainly in the early days. We have now been accepted onto amazon.com, we've got a store on their site. We also have a store on walmart.com. We're moving past kind of what I would call our pilot production phase _________ into full production, hopefully, around early next year. We're currently in bottles, Hall, and looking to get into cans which are going to be much more favorable for doing shipping. But the nice thing is we can already hit all of us. And so, I think there are very nice scalability dynamics that are not there with beer, because you can't distribute beer easily across state lines, whereas you can distribute nonalcoholic beer much more readily, not every state, but most of the states.

[00:10:16] **Hall Martin:** So what do you find investors are looking for in this segment?

[00:10:27] **Ronan McGovern:** Well investors are looking for, they want a big market size in the future, and they want to see a competitive edge. So if you drill down in those two, it's always hard, I think, at an early stage of investment. If you've got a really big market, it probably means there's people in it already, so you probably want a market that's going to be meaningful enough, but it's got some high growth rates. And I do think that the nonalcoholic beer has got those characteristics, although I think a lot of investors would write it off because they feel that it's too small right now, and they feel that it's not going to get enough fair, enough of the market share. And maybe that's a US centric view, because I think, if you have the insight into Europe, and you see how nonalcoholic has grown there, I think maybe that informs a little bit more. I'm not saying for sure, it's going to be absolutely huge in the US, but that certainly informs my view.

[00:11:19] **Hall Martin:** Do you see a lot of trends coming from Europe to US, and I once saw hard cider really take off in the US, but it mostly came from people from Europe bringing it here, and you see that as a standard practice?

[00:11:32] **Ronan McGovern:** So I think there's a lot more transferability between Ireland and UK to the US than there is between Germany-France. I think there are closer ties there just culturally, historically between those geographies, notably language and notably probably a greater sharing of things like music and television and movies. And I think that that kind of, in some kind of a related soft way, there's better transferability of products, not saying perfect, but I think there is some.

Our next guest is Paul Janowitz, CEO & Founder, MANTRA Labs

[00:07:08] **Hall Martin:** And so what's your participation in this segment so far?

[00:07:12] **Paul Janowitz:** So yeah, so in the CPG industry, I've been involved and investing in it for about 12 years, some of the early deals were Thunderbird, EPIC bar, _________ chips, Austin Eastciders. One thing all of those had in common was a strong founder narrative, right, that they created something out of nothing, because they had a need or an itch they couldn't scratch, and they found a better way to do it. Right? So if you have that mixed with some passion and some drive and grit, you've got a company. And so, I always love to back resourcefulness over experience.

[00:07:48] **Hall Martin:** Great. Well, what else should we know about this segment?

[00:07:51] **Paul Janowitz:** So I think you're going to see a lot of, you know, we'll almost skip over CBD in a way. CBD has grown huge, and that's kind of a no-brainer, nothing new to say there. But what you're going to start seeing is more functional beverages in spaces like alcohol. So you're actually seeing functional alcoholic beverages pop on the market now. One that's super interesting, I've got no financial interest in it, is Pulp Culture. It's actually from Brendan Brazier who's the founder of Vega sport nutrition has created a line of purely fermented fruit beverages that have functional benefits and adaptogens in them. So very – if anyone could do alcohol and better for you and nutrition, it was Brendan, so super interesting there. And then you're starting to see cannabis infused beverages pop up, so both CBD, but also with THC. So you're seeing the kind of full spectrum and you could argue alcohol is a functional beverage in a way, it provides something. So you're starting to see the better for you version of even alcohol showing up on the market. So if you look at that, it's going to trickle on through to hydration. So, so much of what we all have been taking in terms of hydration, whether it's even the new powders, they have a lot of sugar in them, they have a lot of cheap salt. So you're starting to see different better for you versions of hydration. Same thing with Rest formulas and focus. So you're going to start seeing a lot more time specific and activity specific beverages that will be replacing everything from standard water to your standard buck and tonic in the after – well, early afternoon in COVID, evening in normal times.

[00:09:48] **Hall Martin:** What kind of price increase do you think these products will have over their non-functional counterparts?

[00:09:55] **Paul Janowitz:** Yeah, I mean, so you will see anywhere from a 20% to sometimes almost a 100% in the ready to drink category, and even in the powder category. I mean, you could look at water in a way as a functional beverage, and flavored water is costing you 3-4x, and it's got a drop a flavor in there. Right?

[00:10:19] **Hall Martin:** So you have very good margins on these products, it sounds like.

[00:10:23] **Paul Janowitz:** Yeah, the margins are good, I mean, it also depends on the type of ingredients, whether you're doing organic or premium ingredients. Volume is obviously huge in the CPG space, so whether you're producing 100,000 units or a million units your cogs drop significantly.

[00:10:40] **Hall Martin:** Are these products regulated in any way compared to their non-functional components?

[00:10:45] **Paul Janowitz:** Super good question. The short answer is no. The FDA regulates more about what you say versus what the product is or what's in the product. So the US is well behind the EU in terms of regulating nutritional supplements. They are actually not regulated in the US. So when you see that little star on all your vitamins that says these statements have not been evaluated by the Food and Drug Administration, not designed to treat, cure or prevent any disease, that's a standard blanket statement that you have to have on them. It doesn't mean the product doesn't work. It means there's not a third-party governmental entity that is saying that it does or does not work. So the FDA, you can kind of look at them more as advertising police, when it comes to nutrition. They do a lot of work in food and beef industry and all of that stuff, but when it comes to your supplements, your powders, your protein powders, there is not a governmental agency. That's why it's super important to look for products that have a third-party certification. So there's informed-sport, there's safe for sport, NSF certified, there's lots of third-party certifications. So our entire product line is informed sport certified. So that means everything it follows, quality guidelines for both sourcing, end product testing, quality control, and testing for banned substances as well. So it's super important that consumers really know who they're buying from, where it's manufactured, and that it does have a third party certification because the government does not do that.

Our next guest is Sarah Foley, Partner, SWAT Equity Partners

[00:10:01] **Hall Martin:** Great. And so what's your participation in this segment so far in the fund?

[00:10:07] **Sarah Foley:** We have, let's see, I'm just remembering, we've got one company that does have beverage products as part of its product portfolio. They're focused around protein and making sure that you're getting a healthy amount, and it's more of a kind of a very convenience oriented, but snack oriented product that's both shelf stable which is a very big decision to make if you're starting a beverage business. The more shelf stable it is, obviously, the better for the retailer, and better for your kind of inventory, and I think unit level economics; versus something that's pressed or HPP that has to be in the refrigerated section of the store. So we've looked at a lot, I think the beverage category is challenging, to be honest, because it's very crowded. So you've really got to figure out how do I tell a story around the purpose for this product coming into being that other consumers will not only recognize and appreciate, but I can really grow a market for it. It's just not another kombucha flavor, if you will, or not another sparkling or carbonated water, if you will. There's some other real benefit to it. But it's a category that experiences a lot of velocity, as you know, around how quickly we drink beverages and just pull them off the shelf in a ready to drink kind of fashion.

[00:11:39] **Hall Martin:** Great. Well, a moment ago, we talked about what makes for a successful company, and you mentioned many things like brand DNA, but what do you look forward to invest in, what's the specific criteria you're looking for to make a decision to pursue it?

[00:11:53] **Sarah Foley:** In the beverage category, beyond just true differentiation of why the product exists, we look at consumer engagement, as I kind of mentioned as well. So that can be measured in a variety of ways too, from its social channels to different types of marketing activations, the way in which the brand is reaching its customer outside of digital channels – for example, are they finding them pre or post workout, or pre and post event, what other ways in which the consumer's kind of gathering, if you will, to share in that beverage. That certainly plays a bigger role as you move into, I think, more spirits and alcohol types of beverages, but we're talking about functional kind of beverages, which may include that category, depending on your mood and day of the week. So that's another big area. We look and spend a lot of time on financials. I'm a finance trained professional, so I don't ignore the fact that you do have to have a strong gross margin in your product in order to build a business underneath, meaning have the marketing budget to go continue messaging that group and community of consumers, but also the right infrastructure on team that can execute across a lot of functional areas. _________ the stage businesses are typically investing ahead of the sales, as you know, so we're going to see an EBITDA or net income number that's negative. But I like a strong gross margin, because it's only going to kind of get picked away at as you grow and scale, and you're working across a lot of different types of channels of distribution. We also like to understand that the founders are focused on getting to profitability, and not purely by raising more and more capital. We'd like to understand the difference between what's the breakeven level of revenue that you can reach before you start actively making true investments in growth, largely funded by marketing dollars across a variety of different budgets and channels. But I need to know that the founders are focused on getting there, not that it's a five-year plan or a 10-year plan. That's important, especially, I think today. We like to see omnichannel forms of distribution. I don't like investing purely in a single channel, certainly not a single customer type of model. It's just too much concentration, and I think more channels require more brand awareness opportunities. And that's another way you'll benefit from building a brand in the long run and growing that tribe of consumers. I am trying to think of what else we will need to pay attention to. I think the last thing I like to work at, look at is, are they really – is the team really focused on the working capital that's going to be required to support the growth, because it's one thing to kind of study your expenses required to build business, but you also need to make sure you have enough inventory to reach those sales goals. And sometimes that may get lost in the shuffle, but it truly is a use of cash in the beginnings of building a business. So we like to make sure that that part of the financial analysis is really reviewed well with founders.

[00:15:43] **Hall Martin:** You mentioned margins, what's your baseline gross margin number you look for to even continue the discussion?

[00:15:49] **Sarah Foley:** That's a great question, and it's a bit of a function of what channels that company is really operating. And so, if they are just starting and they are kind of very ecommerce oriented, whether it's their own site or it may be some of the other very strong e-tailers, whether it's Amazon or Thrive or others, that margin should be 50%, in my opinion, where you're getting that, you're getting the benefit of the retail price point. The wholesale channels, however, _________ going to be lower than that, in some cases a lot lower. I've generally seen beverages in the low 30% gross margin, partly a function of the price point that the retailer wants to carry the product on their shelves for, but you also make up for that a bit lower gross margin and velocity. So there's more volume kind of flowing through the company's system, if you will. So the dollars at the end of the day may be similar that they generate in gross profits, but the margin is generally a bit lower. So if they're below 33-35% wholesale gross margin, then I need to understand is there something specific to that customer, that kind of grocery retailer or mass retailer, if you will, that makes sense. But that's generally the kind of zone – now, there are definitely exceptions, we've definitely seen companies that have higher than 50%, definitely higher than 30 to 35 too, but if it gets much below 30, it's just really, really hard to extend your runway to continue building and building a business without raising a lot more capital.

[00:17:34] **Hall Martin:** Do you look at category growth rate, and how much weight do you put on that if you do?

[00:17:46] **Sarah Foley:** I do, but I don't want to limit myself to the categories that are just 1 to 3% kind of very mature, because that generally indicates to me a strong incumbent or two in the category that could be ripe for disruption. And that's where so many of these amazing founders have a great idea on how to make a much better for you, lower sugar, lower calorie, lower caffeine, hydration drink, for example, that the millennial Gen Z and even I on the other end of that spectrum are looking for. I want to stay hydrated during the day after a workout, but I don't want to consume a beverage that has 25 grams of sugar in it. And so, I think that a category that may be slower growing doesn't mean it's not something interesting to me – actually, it means that there could be a great opportunity to disrupt that big incumbent brand. But on the other hand, looking at a cold brew coffee market, which, five-six years ago was hundreds of millions of dollars and growing at a fast clip, that's going to attract a lot of new entrants as well. And so, the competition factor starts to heat up even more quickly, and that's where I need to really focus on how do you dig through and kind of rise above the clutter of noise around a bunch of other new entrants and brands of cold brew coffee that are coming to market.

[00:19:19] **Hall Martin:** If you ask the startup, what their category growth rate is, and they don't know what category growth rate means...

[00:19:26] **Sarah Foley:** That would be an issue.

[00:19:27] **Hall Martin:** Okay. How would you interpret that or how would you treat that, is that a showstopper?

[00:19:30] **Sarah Foley:** No, I would expect them to do, some of, you know, like, they should understand their market, even if the kind of product was kind of developed out of pure need by that individual, but they should definitely be studying the competition in their market so that they understand how they would pitch, how is my cold brew coffee different from the other five when the wholesaler I need to pitch to, the buyer, says how is your product different from the other three I'm caring. I mean, that's a classic 101 type of question that they will be prepared for, but along with that work and study and analysis comes an idea of how big the category is growing, and what's driving growth.

[00:20:14] **Hall Martin:** Right. I often talk to people with organic natural products, and there's not a lot of data on some of those sectors just yet, but there is plenty of data on the traditional sector, and those traditional sectors are pretty low, 3, 4, 5%, or what have you. And so there's always the question is the organic growth rate going to be a lot higher, and we have to go and try to figure that out, look at the competition and gather it up and see if we can put a hand on that number to see what that disruption might be looking like. So we're often doing some very basic primary research to try to figure out, do they have the disrupter here that's coming up in a very staid marketplace.

[00:20:54] **Sarah Foley:** And the growth, you have to make sure you break down between price and volume, because the organic markets, as you know – those products have been at a premium price to the non-organic or all natural products, typically. Therefore, they may have lower volume, but the dollars may look similar, if not higher. So what is driving the growth, is it just price point or is it volume, is it some combination and get down into the next layer.

Our next guest is Richard G Riccardi, CEO, Riccardi Ventures.

[00:14:27] **Hall Martin:** Great. And so, what do you look to invest in here, or what do you consider as a criteria to get into a deal?

[00:14:34] **Richard Riccardi:** Okay. So I think it's a little bit along the lines, I'd say, given the marketing cost, I just wouldn't even look at any sort of startup. Like, for instance, the energy drink that I invested in, large company, extremely well-funded deal by someone who has a great amount of expertise already in beverage marketing. And the only reason why I got into it as an angel investor is I had a contact with that person who was putting the deal together. So I think obviously, as I've said, you want to have a good product to begin with, but I think that's just table, if you will, that's just table stakes in the whole thing. You got to have the right brand with the right brand positioning that appeals to a good target customer. But unless, the real key here is, unless you've got the money behind it and the expertise, people who can capitalize upon the opportunity, so if the brand and the product is the opportunity, then you need the money and the people to capitalize on the opportunity. It's all marketing strength. So that's what I would look for in any beverage deal, what's the marketing _________ expertise and funds.

[00:15:43] **Hall Martin:** Great. Well, what else should we know about this segment?

[00:15:46] **Richard Riccardi:** Yeah, I think what you might want to think about in this segment, certainly, in the next 12 months, and I think about COVID, I mean, that's the elephant in the room, well, there's some things going on, and one is a can material shortage. So there's shortages in materials making cans, and the demand spikes, because there's not food service, and fountain drinks, people are buying their drinks at the grocery store. So that's placed an incredible demand on the raw material, let's say, for instance, the can, and then plus placed, thankful, an incredible demand upon the packers of these products. But it's such a lot of supply disruptions, which can be fatal to an emerging brand. I mean, think about it, even Coca-Cola has curtailed products that they make, products that they want to keep – try to find caffeine free Coca-Cola, you can't find it right now. And they've even discontinued some brands, including an old line one called Tab. So because of the supply disruptions, I mean, if Coca-Cola is experiencing this, I know, emerging brands are experiencing this, so I think you'll see some brands slip away because of it. And so, not only because COVID, they can't get in and make the presentations or whatever, there will just be supply chain disruptions. Well, of course now, for every little problem, there's an opportunity. And so, those who can persevere during this time will be, and have the funds, will be able to come out the other side with a reduced landscape, a competitive landscape. Now, then that also leads to the second opportunity would probably be is that it would also lead, you know, there's some space now for some more competitors. But I always say small because, gosh, this market, the beverage market is so saturated, and like I said, go to any grocery store, go to a convenience store and see what you see. But that's kind of what I may see over the next 12 months impact of COVID if you would ask me.

Our final guest is Cisco Sacasa, Operating Partner, Bee Cave Capital

[00:12:20] **Hall Martin:** What's been your participation in segments so far, what have you dealt with?

[00:12:24] **Cisco Sacasa:** Yes, I've seen it from various different angles. I've been an operator of CPG companies. I've been an investor and advisor and mentor through the incubator programs. And then even in my day job at HireBetter, a lot of our clients are CPG. So I'm also a vendor in this space. So I get to see it from 360 degrees, from every different angle. I've been in the salty snacks business. We've been – we've invested in various drinks. And it's just fun to see a lot of the innovation that's happening in the space.

[00:13:03] **Hall Martin:** Great. And so, what do you look for when you invest in a CPG company, what's your criteria?

[00:13:10] **Cisco Sacasa:** Yep. First and foremost, it has to be differentiated. If it's a me-too product, not interested. It needs to be differentiated, but it also has to fill a need. And that's the challenge, right? How do you find something that the consumers want and desire, but it's different from somebody that's in the marketplace? So that's the starting point, and that's true from just about any investment. The second thing we're looking at is how big can it be. It might be so nichey niche that it just, there's just not enough, it's not – the pie is just not big enough, right, who can make it interesting. So we're looking at the addressable market and how big can this thing get. And you never know, right? When you're innovating, you're creating a new space, and you just never know how big that is. But is there a compelling story of how big that space can get and is it interesting, right? Is it measured in millions or is it measured in billions? It's measured in billions, it's a lot more interesting. The third thing is just to have access to distribution or is it a strategy on how you're going to get the distribution. We've seen many investments come, opportunities come in, they have this great widget, this great product, but they don't know how to bring it to market. Right? And you don't have to exactly have it figured out _________ to have a compelling story on how you think you're going to figure out and show just enough traction that you can see it, right, you have line of sight to get in that distribution. And then finally, kind of the final litmus test we look at is margins. Can you sell your product and make a decent margin to make it interesting, right? We see many products that look great, they have distribution, they can't make any money at it, their margins are too thin. So it's really hard to scale a CPG company with skinny margins. When we look at something that is sizable, has potential distribution, and they have line of sight to healthy margins, that's a winning combination.

[00:15:16] **Hall Martin:** Great. What else should we know about CPG and investing in it and operating it?

[00:15:22] **Cisco Sacasa:** You know, it takes time, right? Particularly when you're working through retailers and groceries, it takes a long time for them to make their buys and their product _________. So everything in CPG takes longer than you expect. So when you're investing in a CPG company, you have to be patient. This is not like software that you can go from one user to a billion users overnight. But with CPG, it takes a long time to bring the product to market, it has to get your claims, get the packaging, get production up and running, shipping it, getting distribution, getting your turns, getting the refill orders, all that takes time. So as an investor, you have to come in knowing that, in CPG, it's a longer cycle than if you're used to investing in things like software that might be a shorter term, and it's just a different risk profile and a different... But once the consumers are in that buying cycle, it's a beautiful thing to see it.