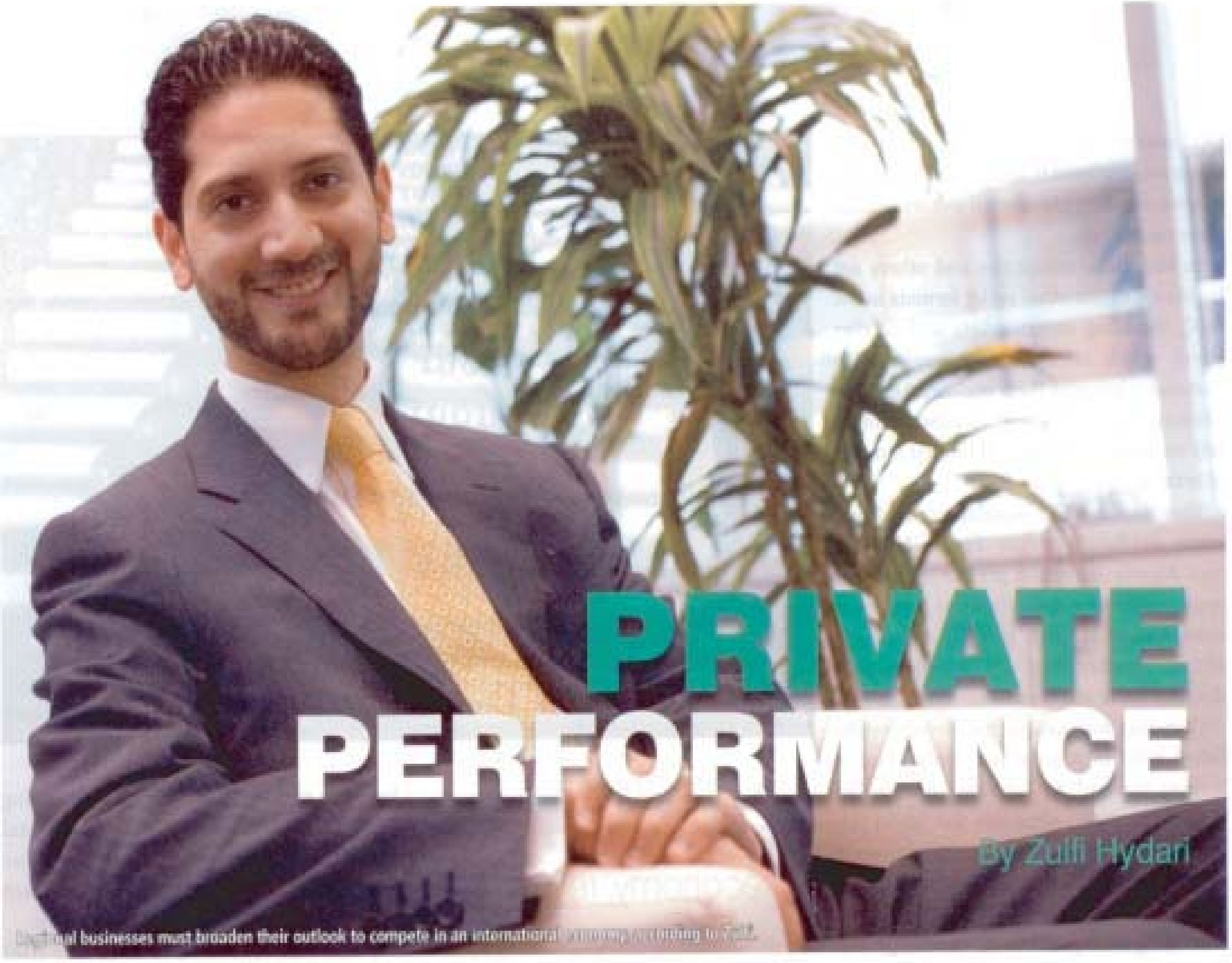

Regional businesses must broaden their outlook to compete in an international economy, according to Zulfi.

PRIVATE PERFORMANCE

By Zulfi Hydari

FMCG COMPANIES IN THE REGION MUST CONSIDER CONSOLIDATION AND EXPANSION TO SURVIVE IN THE FRAGMENTED RETAIL SECTORS

Private equity can support the expansion of regional FMCG companies.

Traditionally, the national economies within MENA have had different characteristics. However, several common local and regional factors have emerged, including rising and young populations, government deregulation and reforms, increasing economic integration and record high oil prices are now dramatically reshaping the region's business environment.

In light of these ongoing changes, regional enterprises must pursue consolidation and expansion, not only as a business strategy to cope with the rapid pace of change, but as their means of survival, particularly in MENA's fragmented consumer goods and retail sectors.

Furthermore, in order to manage and finance such expansion, these firms, large and small, can benefit tremendously from the business and financial expertise of regional private equity firms, who are flush with cash and seeking to invest in growing companies and sectors.

» Local companies are coping with changes in government regulations and the WTO's impact.«

Given that MENA economies are just beginning to reach critical mass and achieve significant growth rates, it is no surprise to see that family-run enterprises and conglomerates are the norm in the region. However, in order to compete in an increasingly complex and globalised international economy, regional businesses must look to broaden their outlook and increase their scale and scope.

For example, in the Middle East and Africa, the top 30 grocers accounted for only 29% of overall grocery sales in 2006, which is far below the 59% share enjoyed by the top 30 grocers in Western Europe.

This picture, however, becomes murkier when analysing trends within the MENA region, which contain many lessons for regional firms. The arrival of hypermarkets and international retailers in the GCC states, characterised by high GDP per capita and disposable income, is perhaps a harbinger of the region's retail future.

Carrefour and Casino, two French retailers, and their two larger regional competitors, Panda and Emke Group, have popularised the hypermarket concept in the

GCC markets and are introducing several major international brands, highlighting the relative maturity of the retail sectors in all of these countries.

In fact, these companies and others are beginning to test other outlet formats in the GCC, including supermarkets and smaller stores which offer more convenience to customers, bringing them into direct competition against smaller businesses which often rely on a single market and limited number of brands.

Though the GCC population is richer, larger markets such as Egypt, Morocco and Algeria currently present significant opportunities for many firms to seek value enhancement through mergers and acquisitions, whether they are manufacturers, distributors or retailers.

Carrefour, for example, has already established itself in Algeria and Jordan and is looking forward to entering the Iranian market in 2008, alongside the Majid Al-Futtaim group. Furthermore, these larger retailers are investing in local manufacturing and production capacity, made easier by the increasing local presence of knowledge and skilled human capital, which allows them far greater flexibility than retailers who are dependent on imports. Regional players need to follow suit, if they are to remain a viable presence in this industry.

In addition to new market entrants, local retailers are coping with changes in government regulations and the impact of MENA countries' ascension to the WTO.

For example, Dubai has abolished agency rights held by companies that import basic foodstuff items like condensed and powdered milk, flour, rice, sugar and tea. These developments clearly favour larger retailers with the financial and operational wherewithal to directly import these products from manufacturers abroad or produce them locally, making it an even more difficult business environment for smaller players.

So far, Dubai has been the centre of gravity for international and regional retailers, but due to saturation these larger firms are looking towards other markets like Abu Dhabi, Jordan, Kuwait and Saudi Arabia and

Zulfi: The arrival of hypermarkets and international retailers could be a harbinger of the region's retail future

» To compete in an increasingly complex economy, regional businesses must increase their scale. «

local retailers there must quickly learn to compete with their larger competitors.

There is hope for other players, though, since the hypermarkets and supermarkets only account for 50% of FMCG retail in the UAE, which shows that there is potential for other firms to expand and gain scale, even within the most competitive and developed retail sector in MENA.

However, in order to expand, these other retail players will not only require significant financial resources to compete with large international and regional names, but also market and industry-savvy advisors and sponsors on their side to help improve operations and make the right acquisitions. R

Regional private equity firms can provide significant benefits on both these counts. Since 2005, PE firms have raised over $20 billion in assets in MENA and nearly 2/3 of those assets have yet to be invested.

Almost 90% of PE funds are focusing on buy-outs with average deal size approaching $158 million. However, only 9% of total investments have focused on consumer goods, highlighting the untapped investment potential and need in this growing sector.

Furthermore, local PE firms such as HBG Holdings, bring together tested management experience in relevant sectors and a better understanding of the industry through their investors and partners. These individuals can present acquisition ideas based on their personal knowledge of the industry and the parties involved.

In addition, PE firms can help regional operators develop the appropriate business strategy for a changing landscape while introducing newer technologies and management styles to create value and higher returns.

To conclude, regional and smaller players in MENA's consumer goods sector will face an increasingly difficult competitive environment, necessitating expansion and consolidation, and local private equity firms bring the financial capital and the expertise to help put these companies on a sustainable growth path.

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