

THE BIG STORY

B&M: The next convenience king?

B&M has acquired Northern convenience chain Heron Foods for £152m. Retail Week looks at why it has struck the deal

B&M has been the subject of much speculation this summer. The retailer made headlines last month when rumours circled that Asda was set to buy the business, while many in the City expected B&M to add a new international player to its basket.

However, the value operator has confounded expectations and picked up a bargain much closer to home in the form of Heron Foods.

The frozen food specialist has a 251-strong UK store estate across the Midlands and North – but with B&M's deep pockets and boss Simon Arora's lofty growth ambitions, this number could skyrocket before too long.

Retail Week Prospect analyst Philip Wigenraad says: "There has actually been very limited growth in Heron Foods' store network over the past five years and B&M sees potential to expand the format beyond its North and Midlands heartland.

"B&M of course has first-hand experience in transforming itself from a regional player into one with a nationwide presence."

The scale of B&M and Heron Foods' busi-

nesses are distinctly different. The average size of a B&M store is nearly 10 times the size of a Heron Foods.

Common customers

However, the two businesses have common customers in the value end of the market.

Canaccord Genuity analyst Sanjay Vidyarthi says: "B&M thinks Heron Foods is disruptive because it is not necessarily in the same towns as a Tesco or Sainsbury's convenience store.

"The areas it is in will have a very loyal customer as a result, which it can take advantage of by pricing very competitively."

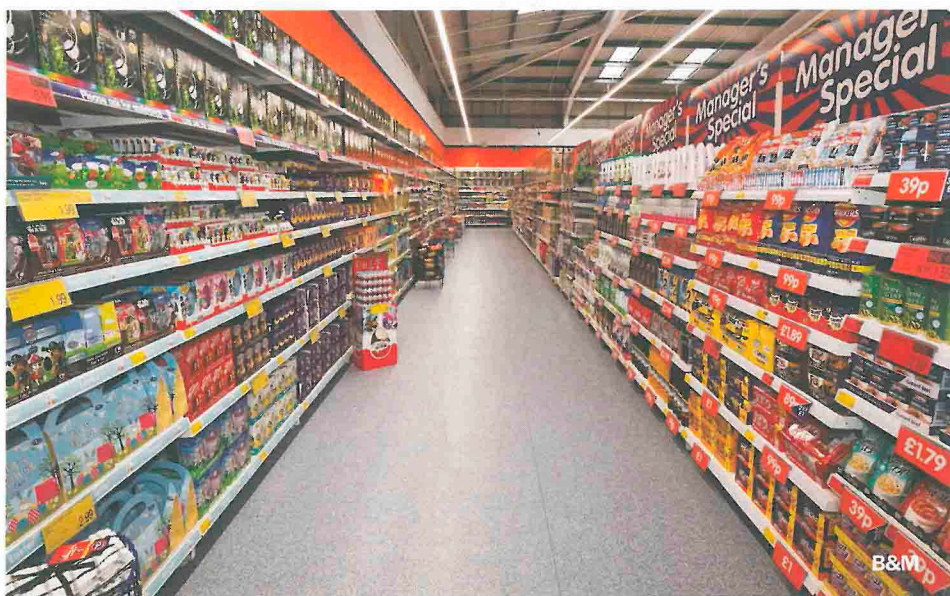
Wigenraad agrees that the two businesses' value-led offers and Northern roots make this a canny acquisition by B&M.

Culturally, the two retailers seem a good fit, he says. "Both formats focus on having a limited range, which helps concentrate their buying power, and are obsessed with keeping their costs in check," he says.

Negotiating competitive prices with suppliers is one of B&M's core strengths.

251

The number of Heron Foods stores across the North and the Midlands



It already sells ambient food and alcohol and Heron Foods could benefit from its buying expertise in these areas.

"This acquisition could see Heron Foods become more focused on providing a discounted offering across a customer's whole grocery shop, rather than just specialising in frozen and chilled," says Planet Retail's global research director Rob Gregory.

Likewise, the acquisition is expected to bolster B&M's frozen and chilled food offer across its 537-strong UK store estate.

To that end, will the two retailers launch a wider bricks-and-mortar tie-up, like Pep&Co shop-in-shops in Poundland stores?

Wigenraad has his doubts.

"I don't think it will launch Heron Foods-branded food concessions in stores as B&M has already established itself as a credible source for groceries and as a regional player Heron Foods lacks brand recognition," he says.

Keep up to date on the latest deals in the sector at Retail-Week.com/Grocery



What the analysts say

“Many expected that B&M’s next strategic move would be in mainland Europe, but the acquisition of the 251-store Heron Foods chain makes strategic and P&L sense.

“Heron trades as a discount c-store retailer, and was initially a freezer centre that has evolved into offering a fuller grocery range. The stores run an EBITDA margin of about 7% (which B&M may be able to improve) although there will be learnings going the other way as well on frozen, a gap in the B&M armoury.

“All in all a sensible deal, which is helpfully earnings-per-share enhancing to the tune of 5-7%.”
Jonathan Pritchard, retail analyst, Peel Hunt

“This deal gives B&M another growth channel which is in a structurally favourable segment of the market and we can see why this would be appealing to the group.

“There is much consolidation in this segment of the market, with Tesco potentially acquiring Booker, McColl’s having signed a new supply agreement with Morrisons and Sainsbury’s rumoured to be wanting to buy Nisa. B&M state that much of the growth in this market has been achieved at premium pricing and it sees an opportunity here.”

Wayne Brown, analyst, Liberum

“Heron Foods has significant expansion potential and will also bring synergy benefits in terms of general scale and expertise in frozen foods.

“B&M gains an additional discount brand operating in small stores. The acquisition enables it to enter the new but related product categories of frozen and chilled. There is a shared culture with both businesses being founder-led [and] focused on a limited SKU count of big brands at discount prices rather than own-label grocery.

“Although the two are largely complementary, synergies should be available from improved buying power and scale in ambient food, the potential to trial B&M’s alcohol ranges and selected FMCG products in Heron and the transfer of B&M’s expertise in logistics, store roll-out and IT systems.

“Heron is a regional player growing at 15-20 new stores per annum, but there is scope to expand nationally at a faster rate, acting as a disrupter in a mainly premium-priced market segment.”

Matthew Taylor, analyst, Numis

“While we were expecting any M&A to have been overseas, the strategic rationale does make sense.

B&M is targeting one of the growth areas in food retail (online being the other), with a small store format (2,500 sq ft vs circa 20,000 sq ft for new B&M stores) that has some, but not much, overlap.

“Convenience product historically has a price premium, allowing a discount format room to grow, with the business targeting 10-20 store openings per annum. With an offer geared towards chilled and frozen (50% of sales), Heron allows B&M to target a new product category.”

Alistair Davies, analyst, Investec



Heron Foods at a glance

- Heron Foods was founded in Hull in 1979 and the company now has a presence throughout the North and the Midlands
- Heron Foods reported £274m sales and £19m EBITDA in the year to December 2016
- It operates 251 stores, which measure 2,500 sq ft on average
- Most of those stores are in town centre high streets (153 stores) and local neighbourhoods (80 stores) with 20 in shopping centres
- Heron Foods was founded by Malcolm Heuck, who is now retired. His sons Andrew and David Heuck will remain in their roles leading trading and finance
- Its customers generally fall into the CDE socioeconomic group, with 34% visiting every day and 46% every week. They spend an average of £5 per visit



Snapping up Heron Foods is a clear statement of intent by B&M about its ambitions in the discount convenience grocery market

B&M's convenience ambitions

Snapping up Heron Foods is a clear statement of intent by B&M about its ambitions in the discount convenience grocery market.

Discounters Aldi and Lidl have expressed interest in the convenience format in the past and, along with online, it is one of the fastest-growing sectors across retail.

However, Shore Capital head of research Clive Black says that B&M should proceed with caution if it is eyeing a full assault on the convenience market.

“Heron Foods has grown from a standing start and B&M is a master in its field, but general merchandise is very different to the grocery sector and it is up against guys that know an awful lot,” he says.

There’s no doubt that B&M has lofty ambitions and the capital to realise them. The Heron acquisition could see it soar ahead of its value rivals. **RW**