HEALTH & WELLNESS INVESTMENT REPORT

Q4 2022

CohnReznick
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By Daniel Teoh & Jeff Wissink

The health and wellness sector experienced slowing deal volume and investor interest as 2022 wound down and organizations began preparing for 2023. With no tax mandates or other drivers forcing investors' hands at the end of 2022, activity was flat across industries including companies operating in the fitness, beauty, food, and outdoor sports categories.

Headwinds like inflation and rising interest rates kept investors on the sidelines across most industry sectors during Q4, although some deals did close in certain sub-sectors within health and wellness. For the most part, 2022 was clearly a year of "normalization" after the extremely robust pandemic years of 2020 and 2021. By Q4 2022, investors took a breather and began regrouping and planning out their strategies for 2023.

MARKET OVERVIEW

The total amount of capital invested in health and wellness companies during Q4 was $23.3 billion across 659 deals. Deal count was lower than Q3, but the total sum invested was higher than the previous quarter's total of $16.8 billion.

One of the larger health and wellness deals to close in Q4 included Keurig Dr Pepper Inc.'s $863 million investment in Nutrabolt. Nutrabolt is one of the fastest growing health and wellness brands with a mission to innovate and make products that maximize human potential (deal excluded from PitchBook data). Other health and wellness deals that closed during Q4 included Amorepacific Group's acquisition of skin care manufacturer Tata Harper Skincare for $128.5 million, and the Healing Company's purchase of Your Super, a producer of organic food powder mixes, for $15.6 million.

Investors active in the health and wellness sector during Q4 included Eagle Private Capital, Juggernaut Capital Partners, and Morgan Stanley Capital Partners, each of which closed three deals during the quarter.

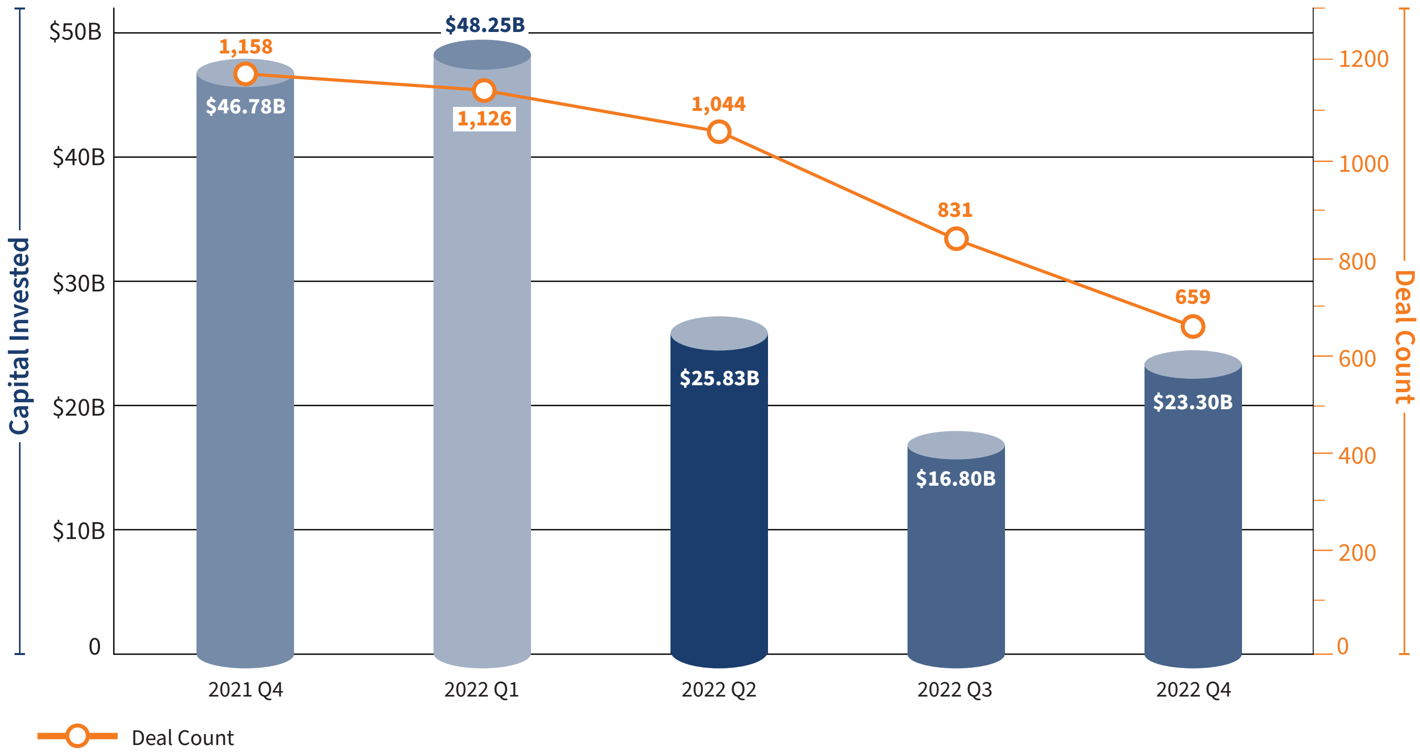
Q4 2022 top investors: Most active private equity firms based on number of deals

- **Eagle Private Capital**
- **Juggernaut Capital Partners**
- **Morgan Stanley Capital Partners**

Q4 2022 TRENDING NUMBERS

All data gathered from PitchBook Data, Inc. as of Jan. 16, 2023

Capital invested by deal count



MARKET FACTORS IMPACTING THE DEAL SPACE

Consumers are prioritizing their health and putting more effort into eating well, exercising, and otherwise taking care of themselves. These and other trends are driving the global wellness market, which is on track to reach nearly $7 trillion by 2025 – a 25% increase over 2022, when the market was worth $5.59 trillion. Also, Shopify says spending on personal wellness is increasing, with one leading product segment being vitamins, minerals, and supplements.

"As consumer interest climbs and purchasing power increases, there are huge opportunities for brands," Shopify points out. "This is at a time when spending on personal wellness is rebounding after stagnating or declining during the COVID-19 pandemic."

According to Forbes, wellness experts at the ness, a dance-based and movement focused fitness method, say these wellness trends are poised to make waves during the year ahead including:

- **Earlier dinner times.** People of all ages are making earlier dinner reservations and are eating their final meal of the day hours before bedtime to allow their bodies ample time to digest. The ness credits the use of wearables with making people more conscious of the impact late dinners have on their sleep patterns.
- **Beauty treatments at home.** Consumers are performing more beauty treatments on their own instead of going to the salon. In response, companies are offering more online how-to classes and products that can be managed at home, without the help of an esthetician.

- **Digital detox.** Taking social media breaks and disconnecting from technology is a therapeutic and reachable self-care goal. Expect to see more of this in 2023, particularly as the need to improve mental health increases in priority.
- **Shorter bursts of exercise.** Breaking up an exercise regimen into smaller, digestible bites helps keep the metabolism going throughout the day. It also makes exercise more accessible for busy people who do not have time for lengthy workouts. Virtual workouts, particularly during lockdown, have given the consumer an understanding of the benefits of exercising based on their schedule and the time they have available. Boutique fitness businesses and gyms are starting to introduce shorter class times to cater to this demand.
- **More sustainable options are hitting the market.** Companies are making beauty, skin care, and other products with natural ingredients. Their formulas work as promised, but they do it in an environmentally safe manner. This is a continuation of trends we have seen through 2022, particularly in the food and beauty categories. We also expect that this will be a focus for companies and investors as they try to boost their ESG credentials.
- **Wellness apps for the masses.** Wanting to reach a large audience, wellness-focused platforms are now offering services in Spanish and American Sign Language. This will put the power of wellness into the hands of a much larger and more diverse group of consumers.

TRENDS AND TRANSACTION ACTIVITY BY CATEGORY

Fitness

Investment in the fitness sector rose to $15.2 billion during Q4 compared to $6.0 billion the previous quarter. Some of the top fitness deals that closed during Q4 included the $26 million capital raise for Katalyst Fitness, developer of an electro muscle stimulation system; the $8.8 million venture capital raise for CLMBR, developer of a vertical high intensity climbing machine; and Velvet Sea Ventures' $7.6 million seed funding for arketa.

One of the quarter's higher profile deals was MW Fitness Holdings LLC's October acquisition of KickHouse Fitness LLC for an undisclosed sum. MW Fitness is the parent company of Mayweather Boxing + Fitness, which was co-founded by pro boxer Floyd Mayweather. The transaction combines the 65 Mayweather Boxing + Fitness franchise locations with the 26 KickHouse kickboxing franchise locations into a single group under MW Fitness.

The KickHouse acquisition is one more example of the need for brands in the fitness space to achieve scale, diversify their offerings, and attract new customers. We saw this taking place through much of 2022 and expect this trend to continue in 2023.

We are also seeing numerous deals focused on helping consumers take control of their own health and wellness either by connecting them to personal trainers, infusing gamification into the experience, and/or offering rewards for hitting fitness goals.

During Q4, the deals involving Ongo, FlexIt, and Agon all fell under this "motivational" umbrella. For example, Agon has developed a fitness application designed to reward users based on fitness challenges. The company's application utilizes artificial intelligence (AI) to make personal training accessible, engaging, interactive, and rewarding. At CohnReznick, we recently worked with another fitness company in which the user contributes to a pool of money and then motivates participants to work toward their goals to win their money plus more back.

Beauty and Personal Care

About $9.1 billion was invested in 194 beauty deals during Q4, including Peace Out's $20 million infusion from 5th Century Partners; Fisk Industries' acquisition of Betty Beauty, a cosmetics manufacturer; the purchase of mascara maker Create Happy by three different investors; and toxin-free haircare product manufacturer Dae's $8 million round of series A venture funding.

Consumers also want products and services that help them feel better both physically and mentally. For example, Aescape, which raised a $33.7 million series A venture funding round during Q4, has developed robotics-enabled technology that automates soft tissue treatment and brings actionable measurements to massage therapy using a system of sensing, AI, and robotics. This technology not only delivers personalized massage therapy but also addresses the labor shortage that is impacting most industries.

Mood Connect, which raised an undisclosed sum of venture funding, offers a wellness platform that provides resources, workshops, support groups, and discussions led by a community of licensed therapists, counselors, and coaches. This platform helps address the increasing need, enabling consumers to take control of their mental health and wellbeing.

Q4 was beauty's highest performing quarter in 2022 despite the issues the industry faces with compressed margins due to inflation and supply chain issues. Based on current data and outlooks we expect this health and wellness category to remain strong as companies develop new technologies, introduce more non-toxic/environmentally friendly formulas, and use more sustainable ingredients in their products. These are just some of the key "must haves" that consumers are asking for, and brands are responding with new options that meet these needs.

Food

For Q4, the volume of capital invested in the food space fell to $546 million – down from $5.6 billion the prior quarter. The total number of deals fell to 107 (from 159 during Q3), making the overall deal size much smaller during the most recent three-month period. The deals that closed included Atrium Innovation's purchase of AquaCap, which makes the liquid filling of hard two-piece nutritional capsules; Golden Grail Technology's acquisition of energy drink maker, Sway Energy; and USANA Health Services' acquisition of Rise Bar, which makes protein bars.

Throughout most of 2022, we saw continued interest in companies that make healthy nutrition, vitamins, supplements, and plant-based foods. In Q4 we observed multiple transactions in the children's-focused nutrition niche – a trend that is a natural progression from health-conscious parents who want to take better care of their families' health through high quality nutritional habits.

We are also seeing activity pick up in the "food as medicine" category; for example, kombucha is becoming an extremely popular option for consumers who are seeking to help prevent or treat certain medical conditions as well as take advantage of the benefits kombucha offers for gut health. This trend showed up in Q4's M&A activity with Beloit Kombucha Company, Jiant, and Aqua ViTea Kombucha among those companies that raised new capital during the quarter.

Q4 2022 Top Deals

Company Name	Deal Size (millions)	Investors	Deal Type
Tata Harper Skincare	$128.5	Amorepacific Group	Merger/Acquisition
Liquid Death	$70.0	Hinge Capital, Live Nation Entertainment	Later Stage VC
Charlotte's Web Hemp	$56.8	British American Tobacco	PIPE

WHAT'S NEXT?

As we move further into 2023, expect to see more bolt-on deals and smaller deals taking place within the health and wellness category. The focus may also narrow to more specialty and niche deals as companies seek to address strategic needs and gaps to remain competitive. Above all, expect to see deals requiring less debt and that are immediately accretive to EBITDA.

We also expect health and wellness M&A in the middle market to remain robust during 2023, despite the headwinds, and for trends like the convergence of healthcare with health and wellness to continue. Finally, look for an increased focus on technology including augmented reality (AR) and virtual reality (VR), plus an increased focus on companies that provide men's beauty products and that support positive mental health.

PRE- AND POST-ACQUISITION STRATEGIES FOR HEALTH AND WELLNESS COMPANIES

The purchase of a business is based on an investment thesis for which success is not guaranteed. In this tightening economy it is vital that a buyer utilize best practices to ensure that the transaction is successful and the investment thesis is met.

When we think about transaction best practices, it is useful to segment those best practices into pre-transaction and post-transaction activities, the focuses of which are different. Pre-transaction activities are focused on fact finding, risk mitigation, and integration planning, while post-transaction activities are largely focused on execution, value creation, and the resultant achievement of the investment thesis.

Due diligence

If you are on the buy side, due diligence efforts minimally focus on the quality of earnings (QofE), which is an assessment of the accuracy of historical earnings. However, there are many other kinds of due diligence that may take place pre-transaction, including (but not limited to) human capital, finance operations, IT, operational, privacy, cybersecurity, ESG, data, commercial, regulatory risk, and compliance risk.

The type of due diligence performed is dependent upon the nature of the business that is being bought or sold, the desired timing of the transaction, costs associated, tolerance for risk, and other factors that could impact the deal. For example, if a private equity fund is acquiring a business where the primary asset is consumer data, the fund may decide to spend additional time and money understanding the quality and security of that asset by running a thorough data and cybersecurity due diligence process.

As another example, if the proposed transaction is a carve-out, where assets from another business – or, multiple businesses – will be stood up as a standalone entity in the future, more emphasis should be placed on operational due diligence, where attention can be paid to determining how the business will operate successfully as a standalone entity.

Pre-transaction integration planning

Integration planning is paramount to the success of the deal and often something that is not considered until the deal is closer to completion. Integration planning starts with questions like, “What is my long-term goal for this business?” and “How quickly do I want or need to achieve the investment thesis?” The answers to these, and other high-level strategic questions about the entities in question, typically serve as guard-rails for post-transaction planning.

Integration planning is a key step that usually comes after appropriate due diligence activities have been completed with satisfactory results. It takes time and money, neither of which should be expended until the buyer is reasonably sure that the deal will close. As such, integration planning typically starts to ramp up as you get closer to definitive documentation – legal contracts between the buyers and sellers that detail specific terms of the transaction.

Integration timelines always vary. We have worked with companies that plan to integrate an acquired asset to a larger entity, and believe that they have the best products, people, processes, and systems. When those companies acquire, they typically want to integrate as fast as they possibly can. This is likely part of the investment thesis: “Company X has an excellent product – imagine how much more profitable they could be if they had the benefit of our supply chain strength/procurement power/brand strength/executive team/<insert other perceived competitive advantage here>.”

In other situations, someone will buy a company and then run it for a period of time before beginning a significant integration, not wanting to disrupt its current model or unintentionally destroy value. In these cases, companies will slowly begin seeking targeted opportunities that help them achieve the investment thesis while causing less overall disruption to the acquired entity. Regardless of which approach is used, there are a host of detailed and practical matters that must be contemplated in advance of Day One.

Transition Service Agreements (TSAs)

The definition of necessary TSAs is also a critical component of pre-transaction integration planning and are of particular importance for carve-out transactions. A TSA is an agreement between buyer and seller where the seller agrees they will support certain functions of the sold entity that, for whatever reason, are impractical to disentangle from the seller immediately upon the closing of a deal. For example, if the seller is running sophisticated Enterprise Resource Planning (ERP) software to support the entire business, it may not be practical that the buyer begin operating its own ERP software with all acquired customer, vendor, and other critical transaction data on Day One.

However, as sellers generally dislike supporting business operations they no longer own, sellers will often negotiate shorter time periods to support affected functions, or propose higher costs to the buyer to encourage the buyer to stand up their own capabilities as quickly as possible post-closing. Some TSAs can be large in scope, and some are limited, but in all cases TSA terms impact integration planning. When TSAs are a part of a transaction, they are often negotiated throughout the process and up to deal closing, which means that keeping a watchful eye on those terms and adapting integration planning and budgets quickly is critical.

Day One planning

Regardless of the aggressiveness and timing of the integration, there are a host of practical items on the to-do list that must be completed immediately upon closing the deal. There will be more Day One activities for aggressive integrations, and less so aggressive integrations. In either case, it is important to ensure employees are being paid, continuity of employee benefits are maintained, appropriate retention plans are communicated and executed, and that an appropriate integration budget is defined. Again, regardless of integration philosophy, appropriate Day One activities must be carefully considered during integration planning such that they can be executed flawlessly on deal closing.

Finally, it's important to remember to define communication protocols – both internally (for both buyers and sellers) and externally (for the market). This is an area that a lot of buyers get wrong. Internally, people are not good at dealing with uncertainty and upheavals, so taking the time to define stakeholder groups and crafting a thorough communication plan is critical. It is important to know what is going to be said, when, and to whom. The last thing you want is for affected employees to learn details about the transaction by reading the *Wall Street Journal*. Externally, making sure that the proverbial *Wall Street Journal* is appropriately reflecting the deal also takes effort, and is at least equally important. A good public relations (PR) firm can be useful in this regard.

The post-transaction phase

Once the transaction has closed, the post-transaction phase is reached, and it is all about execution. As with anything, the more time spent on thorough integration planning that encompasses product, people, processes, and systems, the easier the post-transaction portion will be. For example, if an integration management office (IMO) has been set up to manage Day One and downstream activities, the integration plan will more likely be executed well (especially if the right time and budget is associated). CohnReznick has written extensively about value creation strategies around acquisitions, and now is the time to implement those strategies.

Post-transaction is also the time to begin vigilant tracking of the investment thesis (e.g., "We purchased the company for X reason, it's going to generate X number of dollars in EBITDA, and we're going to do X with it"). Report on the progress against the original investment thesis, and make sure the whole team is aligned with any changes or challenges.

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