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### **The Industry Where We Operate: Large and Attractive**

Pet food is one of the largest CPG categories in the United States. We estimate the U.S. pet food industry had approximately \$26 billion in retail sales in 2014. According to Euromonitor, the pet food industry had \$49 billion in additional retail sales outside the United States in 2014, bringing the total size of the global pet food industry to over \$75 billion.

U.S. pet food retail sales grew 62% between 2004 and 2014, which represents a CAGR of 5%, based on data from Euromonitor. The industry growth over this period has been fueled by the “humanization” of pets, as pets are increasingly regarded as family members. This humanization trend has led pet parents to increasingly evaluate pet foods in the same way they scrutinize their own food choices. As more pet parents seek better, more wholesome options for themselves, they also seek these types of options for their pets. As a result, a significant number of pet parents have demonstrated a willingness to pay a premium for pet food that they believe will enhance the well-being of their pets. The higher demand for natural food products and more specialized formulas for different life-stages, breed sizes, special needs and diet types has fueled premiumization in the industry, leading to the faster growth of products with higher revenue per pound. This premiumization trend has impacted all market segments and product types in the pet food industry.

The pet food industry has high penetration in the United States with 63% of households purchasing pet food in 2014. Virtually all pets in the United States are fed packaged pet foods. The continued growth of the industry through the worst economic recession in recent history is a testament to the underlying consumer demand and the strength of the consumer trends driving it. Pet food is also a highly branded industry with low rates of switching due, in part, to potential digestive issues that may occur when switching between different pet food brands. As a result, brands that build a strong relationship with a pet and its pet parents realize significant value over the lifetime of the pet, especially if the pet starts on the brand as a puppy or kitten.

We believe the Wholesome Natural and Therapeutic market segments are particularly on trend as pet parents increasingly treat their pets like family. With market shares of 17% and 7%, these two market segments have become significant parts of the U.S. pet food market, and continue to grow faster than the rest of the market.

In 2014, specialty channels accounted for 45% of U.S. pet food sales, with the Food-Drug-Mass, or FDM, channel accounting for the other 55%. Specialty channels include a diverse set of retailers with over 20,000 stores (which includes national pet superstore chains (i.e., PetSmart and Petco), regional pet store chains (e.g., Pet Supplies Plus, Pet Supermarket, Petsense and Pet Valu), neighborhood pet stores, farm and feed stores (e.g., Tractor Supply Company and Mid-States), eCommerce retailers (e.g., Amazon, Chewy and Petflow, as well as websites of major retailers), military outlets and hardware stores) and 25,000 veterinary clinics. BLUE is sold across all types of specialty channel outlets, although our sales in the Vet channel, which represents 6% of U.S. pet food sales, are currently minimal. We have chosen to sell BLUE in the specialty channels as we believe these channels provide a better environment for us to interact with and educate pet parents, help position BLUE as a premium brand and dedicate more shelf space to pet food, which grants consumers access to a broader range of our products. Pet food sales in specialty channels have grown faster than pet food sales in the FDM channel for the past 20 years as a result of the pet-focused environment and superior product selection.

Starting in the second half of 2013, the largest pet food company in the United States initiated a significant increase in its promotional spending focused primarily on the FDM channel, which effectively reduced the average price per pound for its products. Other pet food companies responded by increasing their own promotional spending. Given the steady volumes consumed by pets, this heightened promotional activity drove down the pet food category growth rate in 2013 and 2014. It also reduced traffic to the specialty channels as price gaps widened and consumers stocked up on pet food products as a result of these increased promotional offers. As a result, overall pet food sales growth rate in Tracked Channels decelerated from 5% in 2012 and 4% in 2013 to 1% in 2014. However, despite these FDM-focused promotional activities, specialty channels continued to grow faster than the FDM channel during this period, with a 3% growth rate compared to a decline of 0.3% for the FDM channel as measured in Tracked Channels. As of the first quarter of 2015, sales growth rates have been improving