Food and Beverage Industry Outlook Survey:
Executives Plan to Spend and Invest in Recipe for Growth

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KPMG LLP, (KPMG) the audit, tax, and advisory firm, surveyed 103 C-suite and other top-level executives in the food and beverage industry during the second quarter of 2012. Participants were asked about business conditions in their sector, the most significant revenue growth opportunities, and any barriers to growth that may exist. They were also asked a variety of questions about the economy, including factors they perceive might impede or support their sector’s recovery, and to assess the impact advancing technologies may have on their business model.

These responses were compared to the findings of a similar survey conducted among food and beverage executives in the second quarter of 2011.
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Foreword
Faced with a stagnant economy, food and beverage executives plan on investing more in new products and technology, while seeking out merger and acquisition activity to fuel sector growth. Yet, due to the current environment, companies will also likely need to keep their focus on eliminating costs and improving operational efficiencies while placing an increased emphasis on talent management and regulatory compliance.

Technology is expected to continue to play a vital role in food and beverage business strategies, with many executives looking to increase their use of data analytics to gain customer insight, promote brands and products, and make better pricing decisions. By embracing data analytics as a business imperative, sector executives will likely be in a better position to gain a competitive advantage in the rapidly evolving global digital economy. Meanwhile, the impact of social media and other digital marketing channels continues to gain ground, being utilized more by food and beverage companies for brand promotion, customer insight, and recruiting purposes.

In contrast to last year, this year’s results reveal an increasing awareness of the challenges presented by an evolving regulatory landscape, with many executives reporting progress in proactively addressing regulatory and risk-related issues. Additionally, they indicate a greater focus on talent management and retention initiatives, citing a lack of qualified labor as a significant challenge to growth, leading to an increased focus on compensation and training over the next year.

Overall, 2012 survey results reveal slow and steady sector progress as evidenced by revenue increases and hiring activity over the last 12 months. Executives believe that such trends will continue, with modest gains expected in these areas for the year ahead. However, respondents are less enthusiastic over the longer-term outlook, with many pushing back their predictions for a complete U.S. economic recovery until 2014 or beyond.

On behalf of KPMG, I would like to thank those who participated in this survey. I hope the findings are useful to you in addressing market challenges and opportunities. I also welcome the chance to discuss this study and its implications for your business in the year ahead.

Patrick Dolan
National Line of Business Leader—Consumer Markets
KPMG LLP
Key findings from KPMG’s 2012 Food and Beverage Industry Outlook Survey

KPMG’s survey reflects the responses of 103 food and beverage sector executives from large, U.S.-based companies with $100 million or more in annual revenue. Forty-two percent of respondents worked for companies with annual revenue of $100 million to $1 billion, while 34 percent represented companies with annual revenue of $1 billion to $10 billion, and 23 percent worked for companies with revenue exceeding $10 billion. One percent represented companies with less than $100 million in annual revenue. Sixty percent of these companies are privately held, and 40 percent are publicly held.
**Survey key findings:**

- Sixty-eight percent of executives surveyed indicate that their companies have significant cash on their balance sheet, up from 63 percent in 2011. The majority indicate they will look to make investments over the next 18 months, while 27 percent say investment is already underway.

- More than half (59 percent) of survey respondents plan to increase capital spending over the next year, with the highest-priority investment areas being new products or services (39 percent), and the acquisition of a business (38 percent). In fact, 62 percent of executives believe their companies are likely to be involved in a merger or acquisition in the next two years.

- Technology will be a key investment area, with 36 percent citing it to be a top investment priority over the next year. Many acknowledge that technology, such as data analytics and cloud computing, will help reduce costs, enhance interactions with customers and suppliers, and accelerate time to market.

- Forty percent of executives cite operational improvements and making significant cost reductions as top initiatives for their companies over the next two years. Most point to pricing concerns and input costs as the most significant threats to revenue growth and profit margins.

- This year’s survey results show greater attention toward regulatory changes, with 67 percent reporting they are most concerned with how the Food Safety Modernization Act may affect their businesses.

- Respondents indicate that they are more focused on talent management/retention initiatives compared to last year’s survey results, with an increased emphasis on compensation and training.

- More than half (57 percent) of executives surveyed say that revenue is up from last year, and 72 percent expect revenue to continue to climb this year. Similarly, 53 percent believe their companies will increase the number of U.S. employees in the year ahead. However, 31 percent do not anticipate their company’s headcount to ever return to pre-recession levels.
An increasing appetite for growth

In pursuit of growth, food and beverage companies will likely look to ramp up investment and spend more over the next year, particularly in the areas of new products, mergers and acquisitions, and technology. With significant cash on their balance sheets and many respondents reporting improved cash positions over the last year, companies are well positioned to be more aggressive to drive growth—organically and inorganically. At the same time, challenging market factors will likely demand that they not only focus on growth, but also continue to focus on cost reduction and operational efficiency while maintaining an emphasis on talent management and regulatory changes.

Capital spending and investing

Food and beverage companies have significant cash on their balance sheets and are ready to invest. In fact, 68 percent of survey respondents report that their company has significant cash on its balance sheet, of which 27 percent acknowledge that investment is already significantly underway.

Sixty-eight percent of respondents feel their company has a great deal of cash on their balance sheets; and the majority indicate they will look to make investments in the next 18 months.

Among those whose companies have significant cash on their balance sheets

Ready to spend
Moreover, 59 percent of survey respondents expect their company’s capital spending will increase over the next year, while 26 percent anticipate that it will stay the same.

The majority of respondents indicate an increase in capital spending over the next year

Much of this spending will be in the areas of new products and services (39 percent), acquisition of a business (38 percent), and information technology (36 percent).

Developing new products or services and acquisitions Continue to be the primary focus for capital spending

Q. What is the outlook for capital spending by your company over the next year?

Q. In which three areas do you expect your company to increase spending the most over the next year?
Pursuing M&A to fuel growth

The sector will see continued merger and acquisition activity according to most survey respondents. As part of their quest for growth, 62 percent of the executives surveyed think it is likely that their company will be involved in a merger or acquisition either as a buyer or seller over the next two years. **Sixty-two percent of the executives surveyed indicate their company will be involved in M&A activity.**

Initiatives garnering attention

When asked about the top initiatives on the minds of management, more than a quarter of survey respondents cite the need to improve operational processes and related technology followed by significant investment in organic growth. Unlike last year, navigating significant changes in the regulatory environment is clearly on the radar this year and due to the increasing complexities surrounding regulation, will likely garner more attention from management moving forward.

**While investment in organic growth is a top Initiative, 47 percent of the executives indicated operational improvements and making significant cost reductions to their top initiative.**

Q. What is the likelihood that your firm will be involved in a merger/acquisition in the next two years?

Q. What is the top initiative from a management perspective for the next two years in terms of energy, time, and resources?
Building on positive sector momentum

Most executives believe the food and beverage sector will continue to grow over the next year. Eighty-two percent of survey respondents expect sector growth during the next year, of which 60 percent predict only gains of about 10 percent or less.

**Similar to the 2011 survey, respondents anticipate sector growth to be 1–5 percent over the next year.**

### Revenue growth

Most food and beverage companies saw revenue rise during the last 12 months. Fifty-seven percent of survey respondents report an increase in revenue over the last year, while 35 percent remained the same. Interestingly, these results fell short of the executives’ expectations in last year’s survey, in which 68 percent expected higher revenue in 2012, while 27 percent predicted they would remain flat.

**Over half of the respondents report their company’s revenue is higher compared to one year ago**

![Bar chart showing revenue growth](chart)

**Key**

- Increase by more than 10%
- Increase by 6% to 10%
- Increase by 1% to 5%
- No change
- Decrease by 1% to 5%
- Decrease by 6% to 10%
- Decrease by more than 10%

**Q. Compared with this time last year, how would you describe your company’s current revenue?**

1 = Significantly worse and 5 = Significantly improved

<table>
<thead>
<tr>
<th>Category</th>
<th>2012</th>
<th>2011</th>
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<tbody>
<tr>
<td>Significantly higher</td>
<td>47%</td>
<td>68%</td>
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<tr>
<td>Moderately higher</td>
<td>35%</td>
<td>27%</td>
</tr>
<tr>
<td>About the same</td>
<td>8%</td>
<td></td>
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<tr>
<td>Moderately lower</td>
<td>0%</td>
<td></td>
</tr>
<tr>
<td>Significantly lower</td>
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</table>

Mean 2012: 3.6
Looking ahead this year, executives expect revenue to continue its upward climb. When asked to describe their revenue expectations a year from now, 72 percent of executives predict that revenue will increase, while 24 percent believe revenue will stay flat.

**Respondents anticipate revenue to be moderately higher one year from now.**

![Revenue Expectations Chart]

It’s all about the customers

Retaining and adding customers remains the key to driving revenue growth in the food and beverage sector, according to 47 percent of executives surveyed. Other top revenue drivers cited by respondents include expansion in core and new markets (38 percent) and product innovations (29 percent). These results were in line with the responses from last year’s survey.

**Executives indicate retaining and adding new customers, expansion in core and new markets, and product innovation to help drive growth.**

![Revenue Growth Drivers Chart]
Challenging market factors

Despite the momentum and growth investments food and beverage has experienced over the past year, executives point to costs of inputs and discounting as the most significant threats to profit margins, with regulatory compliance becoming an increasing threat as well.

Q. Which of the following items pose the greatest threat to your company’s profit margins in the next 12 months?

<table>
<thead>
<tr>
<th>2012 Top 5 threats to profit margins</th>
<th>2011 Top 5 threats to profit margins</th>
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</thead>
<tbody>
<tr>
<td>1. Costs of inputs or merchandise</td>
<td>1. Costs of inputs or merchandise</td>
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<tr>
<td>2. Discounting and other sales incentives</td>
<td>2. Discounting and other incentives</td>
</tr>
<tr>
<td>3. Decreased sales volumes</td>
<td>3. Decreased sales volumes</td>
</tr>
<tr>
<td>4. Regulatory compliance</td>
<td>4. Administrative and marketing costs</td>
</tr>
<tr>
<td>5. Inventory carrying costs</td>
<td>5. Regulatory compliance</td>
</tr>
</tbody>
</table>

Overcoming growth obstacles

Meanwhile, similar themes resonated when considering obstacles toward achieving growth. Pricing pressures, volatile commodity/input prices, and a lack of consumer demand rounded out the top three answers listed as the most significant growth barriers over the next year. Notably, a lack of a qualified workforce is a growing concern for the industry as indicated by this year’s results over last year.

Q. Which of the following are the most significant growth barriers facing your company over the next year?

<table>
<thead>
<tr>
<th>Top Growth Barriers – 2012</th>
<th>Top Growth Barriers – 2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Pricing pressures</td>
<td>1. Pricing pressures</td>
</tr>
<tr>
<td>2. Volatile commodity/input prices</td>
<td>2. Volatile commodity/input prices</td>
</tr>
<tr>
<td>3. Lack of customer demand</td>
<td>3. Labor costs</td>
</tr>
<tr>
<td>4. Labor costs</td>
<td>4. Lack of customer demand</td>
</tr>
<tr>
<td>5. Energy prices</td>
<td>5. Energy prices</td>
</tr>
<tr>
<td>7. Regulatory and legislative pressures</td>
<td>7. Inflation</td>
</tr>
<tr>
<td>8. Inflation</td>
<td>8. Lack of a qualified workforce</td>
</tr>
</tbody>
</table>
**Strategies to combat costs**

Volatile merchandise costs continue to create a variety of challenges for food and beverage companies. To help combat these costs, 67 percent of executives report optimizing sales, general and administrative (SG&A) and supply chain costs, while 53 percent are implementing commodity hedging strategies.

**Over half of the respondents have implemented some form of hedging strategies for commodities to help combat the impact of volatile input costs on margins.**

**Factors hindering recovery**

More than half of survey respondents view decreased consumer confidence (58 percent) and the continued high national unemployment rate (52 percent) as the two top factors hindering the food and beverage sector’s recovery. Other top factors cited include increased government regulation (30 percent) and the distressed real estate market (17 percent).

**Decreased consumer confidence and high national employment continue to hinder sector growth.**

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**Q. What strategies has your organization implemented to help combat the impact of volatile input costs on margins?**

- Optimizing SG&A and supply chain costs: 67%
- Hedging strategies for commodities: 53%
- Customer-centric pricing strategies: 41%
- Enhancing trade spend efficiency: 22%
- Revisiting service delivery models (offshoring/shared services): 18%

**Key**

- Optimizing SG&A and supply chain costs
- Hedging strategies for commodities
- Customer-centric pricing strategies
- Enhancing trade spend efficiency
- Revisiting service delivery models (offshoring/shared services)

Multiple responses allowed

**Q. What are the top factors most likely to hinder sector growth?**

- Decreased consumer confidence: 58% (2012) 57% (2011)
- Continued high national unemployment: 52% (2012) 59% (2011)
- Increased government regulation: 30% (2012) 24% (2011)
- Distressed real estate market: 17% (2012) 19% (2011)
- Limited access to credit for consumers: 16% (2012) 12% (2011)

Multiple responses allowed
Data analytics and cloud computing

More and more companies are realizing the value of data analytics to support strategic decision making throughout the organization. In fact, nearly two-thirds (65 percent) of survey respondents say that data analytics play a key role in helping provide customer insight, as well as in the areas of brand and product management (57 percent) and in pricing decisions (54 percent).

Respondents indicated they use some form of data analytics to help gain insight on customers, brand, and product management and to help make pricing decisions.

However, when asked to describe the organizational maturity regarding usage of data analytics, more than half of executives rate their company’s data analytics literacy as average or behind their competitors. Meanwhile, 22 percent admit that they’re rapidly moving toward high analytical literacy, and 17 percent say they are already there.

Cloud computing

Respondents indicate cloud offers many advantages, including reduced costs, accelerated time to market, and increased interaction with customers/suppliers. Yet, when asked, the potential of adopting cloud usage in their companies over the next three years, survey respondents cite cost and technology complexity as key challenges.

Q. Which of the following best describes the potential impact of cloud computing on your business model/operations?

Q. What do you see as the biggest challenges for your business to adopt cloud usage in the next three years?
Exploring digital marketing channels

As food and beverage companies explore new ways of doing business and reaching more customers, 63 percent of survey respondents acknowledge that social media is having a significant impact on the industry. Other digital marketing channels are also making their mark, including e-mail campaigns (31 percent) and mobile promotions (23 percent).

Social media continues to have the most significant impact on business as it relates to digital marketing channels.

Food and beverage executives plan to use digital, social, and mobile technologies in a variety of ways over the next 12 months. In fact, 52 percent have plans to use social media for external brand promotion, and 51 percent will use social media to gain customer insight.

Use of social media, mobile technology, and digital media

Q. Which of the following digital marketing channels is having a significant impact on your business?

Q. How is your company planning to use digital/social/mobile technologies over the next year and for what purpose?
Risk and regulatory challenges

Evolving regulation and changing marketplace dynamics have added to the need for companies to implement a strong internal risk framework. When asked to identify any existing challenges preventing the adoption of a formal risk policy, half (53 percent) of survey respondents believe culture and behavior pose significant obstacles.

Half of the respondents feel that their company’s internal culture and behaviors are the main challenges to adopting a risk policy.

The Food Safety Modernization Act has attracted the greatest regulatory focus as indicated by 67 percent of the food and beverage executives surveyed.

Sixty-seven percent of respondents indicate that they are most focused on the Food Safety Modernization Act in terms of regulations and mandates.

Taxing regulation

Survey respondents also note that evolving tax regulation may impact their business strategy, with 28 percent believing it will result in less capital investment.

Over one in four executives indicate that evolving federal tax policies are having an impact on capital investments and hiring.

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Economic outlook

Executives believe that modest improvements in U.S. business conditions will continue but have pushed back their estimated time line for economic recovery to 2014 or later, with concerns that decreased consumer confidence, continued high national unemployment, and increased government regulation are hindering a full U.S. economic recovery.

Business conditions

More than half (56 percent) of food and beverage executives surveyed believe that U.S. business conditions will improve in a year’s time. These results closely mirror the results from 2011, when 54 percent anticipated economic conditions to improve in a year’s time.

Executives expect improved U.S. business conditions one year from now.

<table>
<thead>
<tr>
<th>Expectation</th>
<th>Percentage</th>
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<tbody>
<tr>
<td>Significantly improved</td>
<td>52%</td>
</tr>
<tr>
<td>Moderately improved</td>
<td>28%</td>
</tr>
<tr>
<td>About the same</td>
<td>14%</td>
</tr>
<tr>
<td>Moderately worse</td>
<td>2%</td>
</tr>
<tr>
<td>Significantly worse</td>
<td>4%</td>
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</table>

Mean: 3.4

U.S. economic recovery

Taking a broader view, hopes for a substantial U.S. economic recovery seem to have been pushed back for at least another full year, according to the food and beverage executives surveyed. While 40 percent predict that it is possible for 2013, more than half (59 percent) believe it will take longer to achieve. Twenty-eight percent anticipate a full recovery in 2014, while 31 percent predict it will take until 2015 or beyond.

Executives expect the time line for overall U.S. economic recovery to be delayed by one full year.

<table>
<thead>
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<th>Timeframe</th>
<th>Percentage</th>
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<tbody>
<tr>
<td>End of 2012</td>
<td>1%</td>
</tr>
<tr>
<td>First half of 2013</td>
<td>11%</td>
</tr>
<tr>
<td>End of 2013</td>
<td>29%</td>
</tr>
<tr>
<td>End of 2014</td>
<td>28%</td>
</tr>
<tr>
<td>End of 2015 or later</td>
<td>31%</td>
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</tbody>
</table>

Q. When do you think the U.S. economy as a whole will recover? Recovery will be substantially complete by:

Key

- Dark blue: End of 2012
- Light blue: First half of 2013
- Green: End of 2013
- Dark blue: End of 2014
- Purple: End of 2015 or later

1 = Significantly worse and 5 = Significantly improved

Q. A year from now, what are your expectations for the U.S. economy?
Headcount

Companies in our survey added more U.S. employees over the last year, with 50 percent of respondents reporting an increase in headcount, a significant jump from 2011 results, which reported a 35-percent increase in personnel.

Fifty percent of the executives indicate employment is higher for their companies compared to one year ago.

Furthermore, food and beverage executives expect the hiring momentum to continue, with 53 percent of respondents predicting they will add employees over the next year, up from 46 percent that held these expectations the previous year.

Executives anticipate improved employment conditions for their companies one year from now.

Notably, 30 percent of survey respondents said that their U.S. headcount has already reached or is greater than pre-recession levels, but 16 percent think that it may never return to those levels.

Almost two-thirds of respondents indicate employment has not returned or may never return to pre-recession levels.

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Food and beverage executives indicate the biggest expected challenges in coming months include the ability to recognize and respond to customer needs and trends, responding to market competition, and managing the volatility of the price of raw materials. The sector as a whole is still challenged by continued high national unemployment and decreased consumer confidence, including limited ability to gain access to capital and increased government regulation. Executives tell us that they do not feel that employment has fully turned around in the sector and there is a mixed reaction as to what the job picture may look like next year.
Growth in a stagnant economy
However, there are opportunities for growth, including responding to the new economic, social, and technological dynamics impacting the industry. Executives indicate that a key revenue driver over the next few years for the industry will be product innovations, both in services and in branding and promotion. We continue to see a shift towards customer and supplier collaboration which is allowing a better understanding of the needs of consumers as well as helping to share potential risks, costs and rewards throughout the supply chain, and more importantly, accelerating the speed to market.

Inorganic growth, such as acquisitions, are offering a faster route to growth for some organizations than home-grown innovation as evidenced by the two-thirds of respondents who indicated that their company will be involved in a merger or acquisition over the next two years, with much of that expansion fueled by the significant cash reserves that companies have built up.

Companies in the industry also have an opportunity to leverage the change in U.S. demographics and focus on specialty trends, such as and organic food and beverage products, ethnic foods, and products considered to help promote health and wellness. Companies taking advantage of these niche segments are hoping to help increase share-of-wallet and top line revenues in an otherwise slow-growth market.

Leveraging the use of technology, such as the use of cloud computing, business intelligence tools, and social media could be a strategic way of gathering information to refine customer segmentation and marketing efforts. In addition to providing visibility to customer insight, access to “big data” is providing executives with insight to help optimize operating models and rationalize portfolios, as well as revealing information related to new markets and pricing strategies.

Rebuilding business models and operations to improve margins
While growth seems to be a top initiative for food and beverage companies, executives continue to focus on cost reductions and identifying ways to streamline operational and financial processes. In our experience, budget cutting can take organizations only so far. To sustain working capital improvements, companies need to consider deeper, more systemic changes to drive down costs and increase standardization. Food and beverage companies are demanding more of technology to help automate processes as well as improve supply chain transparency and agility.

Companies in our sector are also exploring strategies to help deal with rising input costs and the impact to margins, including implementing hedging strategies, working with retailers to enhance trade spend efficiencies, and revisiting service delivery models such as creating shared service centers and offshoring a variety of back office functions.

Managing risk and addressing regulation
This year’s survey results also indicate companies are proactively addressing changes in the regulatory environment, such as the Food Safety Modernization Act, as well as federal tax policies and healthcare reform. They are also proactively addressing risk management-related issues. Food and beverage companies have an opportunity to take advantage of tax cash savings and available government credits and incentives to benefit the bottom line. Examples include exploring state and local incentive opportunities for expansions and relocations; capturing eligible R&D tax credits and tax credits related to supporting energy-saving; or environmentally sensitive upgrades to facilities, physical plant, and equipment.

Attributes of successful companies
Key priorities for companies in the industry will be to create a customer-facing organization through value differentiation, growth and innovation, and better channel management. Also, companies will need to streamline and standardize key processes such as creating an optimized supply chain while implementing effective risk management practices. We believe that companies that will succeed in the long run will be those that have a true understanding of who their customers are and what they want, as well as those who develop a strong brand that provides clear positioning in the marketplace and differentiation in the eyes of the consumer.
Food and beverage companies continue to face a demanding market environment that requires them to actively manage change that may impact sales and performance. Having the right professional services firm is critical to addressing these challenges and achieving financial goals. KPMG in the United States is a leading accounting, tax, and advisory firm for the consumer markets industry and working with our network of member firms, we serve clients worldwide. Our Food, Drink, and Consumer Goods practice is comprised of accomplished professionals, from top food, drink, and consumer goods companies that possess the knowledge, experience, and skills necessary to sort through today’s complex business problems. By developing insights into industry trends and approaching market opportunities with a fresh perspective, we offer company-specific guidance that helps our clients become or remain market leaders.

### How KPMG can help

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<th>Advisory Services</th>
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<td>Management Consulting</td>
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<td>Audits of Internal Controls over Financial Reporting</td>
<td>Business effectiveness</td>
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<td>Other Attestation</td>
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<td>Corporate finance</td>
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