

CENTRAL GARDEN & PET CO  
Form 10-K  
December 11, 2014  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-K**

x **ANNUAL REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended September 27, 2014

Commission File Number 1-33268

**CENTRAL GARDEN & PET COMPANY**

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of incorporation or organization)

**68-0275553**  
(IRS Employer Identification Number)

**1340 Treat Boulevard, Suite 600, Walnut Creek, California 94597**

(Address of principal executive offices) (Zip Code)

**Telephone Number: (925) 948-4000**

**SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:**

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Title of Each Class  
Common Stock

Name of Each Exchange on Which Registered  
Nasdaq

Class A Common Stock

Nasdaq

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer, or a smaller reporting company. See definition of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer

Accelerated Filer

Non-Accelerated Filer  (Do not check if a smaller reporting company)

Smaller Reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

At March 29, 2014, the aggregate market value of the registrant's Common Stock, Class A Common Stock and Class B Stock held by non-affiliates of the registrant was approximately \$84.8 million, \$266.6 million and \$50,000, respectively.

At November 30, 2014, the number of shares outstanding of the registrant's Common Stock was 12,437,307 and the number of shares of Class A Common Stock was 36,936,817. In addition, on such date, the registrant had outstanding 1,652,262 shares of its Class B Stock, which are convertible into Common Stock on a share-for-share basis.

**DOCUMENTS INCORPORATED BY REFERENCE**

Definitive Proxy Statement for the Company's 2015 Annual Meeting of Stockholders Part III of this Form 10-K.

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**Central Garden & Pet Company**

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**FORWARD-LOOKING STATEMENTS**

This Form 10-K includes forward-looking statements. Forward-looking statements include statements concerning our plans, objectives, goals, strategies, future events, future revenues or performance, projected cost savings, capital expenditures, financing needs, plans or intentions relating to acquisitions, our competitive strengths and weaknesses, our business strategy and the trends we anticipate in the industry and economies in which we operate and other information that is not historical information. When used in this Form 10-K, the words estimates, expects, anticipates, projects, plans, intends, believes and variations of such words or similar expressions are intended to identify forward-looking statements. All forward-looking statements, including, without limitation, our examination of historical operating trends, are based upon our current expectations and various assumptions. Our expectations, beliefs and projections are expressed in good faith, and we believe there is a reasonable basis for them, but we cannot assure you that our expectations, beliefs and projections will be realized.

There are a number of risks and uncertainties that could cause our actual results to differ materially from the forward-looking statements contained in this Form 10-K. Important factors that could cause our actual results to differ materially from the forward-looking statements we make in this Form 10-K are set forth in this Form 10-K, including the factors described in the section entitled Item 1A Risk Factors. If any of these risks or uncertainties materialize, or if any of our underlying assumptions are incorrect, our actual results may differ significantly from the results that we express in or imply by any of our forward-looking statements. We do not undertake any obligation to revise these forward-looking statements to reflect future events or circumstances. Presently known risk factors include, but are not limited to, the following factors:

seasonality and fluctuations in our operating results and cash flow;

fluctuations in market prices for seeds and grains and other raw materials;

our inability to pass through cost increases in a timely manner;

risks associated with new product introductions, including the risk that our new products will not produce sufficient sales to recoup our investment;

the impact on our financial results of costs incurred to consider and respond to the unsolicited Harbinger proposals, and the impact of the Harbinger proposals on our business, employees and customer relationships;

declines in consumer spending during economic downturns;

inflation, deflation and other adverse macro-economic conditions;

supply shortages in small animals and pet birds;

adverse weather conditions;

fluctuations in energy prices, fuel and related petrochemical costs;

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access to and cost of additional capital;

dependence on a small number of customers for a significant portion of our business;

disruptions in our business arising from the implementation of our change initiatives and the resulting consequences to our business and results of operations;

increased costs and expenses associated with our change initiatives;

consolidation trends in the retail industry;

competition in our industries;

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risks associated with our acquisition strategy;

potential goodwill or intangible asset impairment;

dependence upon our key executives;

continuing implementation of a new enterprise resource planning information technology system;

our ability to protect our intellectual property rights;

potential environmental liabilities;

risk associated with international sourcing;

litigation and product liability claims;

regulatory issues;

the impact of product recalls;

potential costs and risks associated with actual or anticipated cyber attacks;

the voting power associated with our Class B stock; and

potential dilution from issuance of authorized shares.

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**MARKET, RANKING AND OTHER DATA**

The data included in this Form 10-K regarding markets and ranking, including the size of certain markets and our position and the position of our competitors and products within these markets, are based on both independent industry publications, including The Freedonia Group Lawn & Garden Consumables July 2014; Packaged Facts, U.S. Pet Market Outlook 2014-2015; Simmons Fall 2013 National Consumer Survey; American Pet Products Association (APPA) National Pet Owners Survey 2013-2014; U.S. Census Bureau and our estimates based on management's knowledge and experience in the markets in which we operate. Our estimates have been based on information provided by customers, suppliers, trade and business organizations and other contacts in the markets in which we operate. We believe these estimates to be accurate as of the date of this Form 10-K. However, this information may prove to be inaccurate because of the method by which we obtained some of the data for our estimates or because this information cannot always be verified with complete certainty due to the limits on the availability and reliability of raw data, the voluntary nature of the data gathering process and other limitations and uncertainties inherent in a survey of market size. As a result, you should be aware that market, ranking and other similar data included in this Form 10-K, and estimates and beliefs based on that data, may not be reliable.

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**PART I**

**Item 1. Business**

**BUSINESS**

**Our Company**

Central Garden & Pet Company ( Central ) is a leading innovator, marketer and producer, of quality branded products and distributor of third-party products in the pet and lawn and garden supplies industries in the United States. The total pet food and supplies industry in 2013 was estimated to have been over \$42.0 billion in annual retail sales. We estimate the annual retail sales of the pet supplies and super premium pet food markets in the categories in which we participate to be approximately \$25.4 billion. According to The Freedonia Group, the total lawn and garden consumables industry in the United States was estimated to be approximately \$17.2 billion in 2013 in annual retail sales, including fertilizer, pesticides, growing media, seeds, mulch and other consumables. We estimate the annual retail sales of the lawn and garden consumables markets in the categories in which we participate to be approximately \$10.2 billion. In addition, we participate in the pottery and seasonal décor markets.

Our pet supplies products include products for dogs and cats, including edible bones, premium healthy edible and non-edible chews, super premium dog and cat food and treats, toys, pet carriers, grooming supplies and other accessories; products for birds, small animals and specialty pets, including food, cages and habitats, toys, chews and related accessories; animal and household health and insect control products; products for fish, reptiles and other aquarium-based pets, including aquariums, furniture and lighting fixtures, pumps, filters, water conditioners, food and supplements, and information and knowledge resources; and products for horses and livestock. These products are sold under the master brands including Adams™, Aqueon®, Avoderm®, Bio Spot Active Care™, Farnam®, Four Paws®, Kaytee®, Nylabone®, Pinnacle®, TFH™, Zilla® as well as a number of other brands including Altosid, Comfort Zone®, Coralife®, Interpet, Kent Marine®, Oceanic Systems®, Pet Select®, Pre-Strike®, Super Pet®, and Zodiac®.

Our lawn and garden supplies products include proprietary and non-proprietary grass seed; wild bird feed, bird feeders, bird houses and other birding accessories; weed, grass, ant and other herbicide, insecticide and pesticide products; and decorative outdoor lifestyle and lighting products including pottery, trellises and other wood products and holiday lighting. These products are sold under the master brands AMDRO®, GKI/Bethlehem Lighting®, Ironite®, Pennington®, and Sevin®, as well as a number of other brand names including Lilly Miller®, Over-N-Out®, Smart Seed® and The Rebels®.

In fiscal 2014, our consolidated net sales were \$1.6 billion, of which our Pet segment, or Pet, accounted for approximately \$846 million and our Lawn and Garden segment, or Garden, accounted for approximately \$759 million. In fiscal 2014, our income from operations before corporate expenses and eliminations of \$72.9 million was \$129.1 million, of which the Pet segment accounted for \$88.1 million and the Garden segment accounted for \$41.0 million. See Note 19 to our consolidated financial statements for financial information about our two operating segments.

We were incorporated in Delaware in June 1992 as the successor to a California corporation that was formed in 1955. Our executive offices are located at 1340 Treat Boulevard, Suite 600, Walnut Creek, California 94597, and our telephone number is (925) 948-4000. Our website is [www.central.com](http://www.central.com). The information on our website is not incorporated by reference in this annual report.

**Recent Developments**

*Fiscal 2014 Operating Performance.* Earnings per share increased \$0.22 per share and our operating earnings increased 40% as compared to fiscal 2013 due primarily to increased earnings in our Garden segment. The Garden segment was impacted in both fiscal 2014 and 2013 by individually significant items (i.e., charges in



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fiscal 2014 and 2013 related to the discontinuance of certain products introduced in 2013, the gain on sale of manufacturing plant assets in 2014 and the impairment of goodwill in 2013) which are excluded for purposes of non-GAAP presentation elsewhere in this Form 10-K.

Financial summary:

Net sales for fiscal 2014 decreased \$49.2 million, or 3.0%, to \$1,604.4 million. Our Pet segment sales decreased 4.8% and our Garden segment sales decreased 0.8%.

Gross margin increased 20 basis points in fiscal 2014 to 28.3%, from 28.1% in 2013.

Our operating earnings increased \$16.0 million, or 40.0%, to \$56.2 million in fiscal 2014, and increased as a percentage of net sales to 3.5% from 2.4%.

Net income was \$8.8 million, or \$0.18 per share on a diluted basis compared to a net loss in fiscal 2013 of \$1.9 million, or \$0.04 per share on a fully diluted basis.

Our net cash provided by operating activities was \$126.5 million, an increase of \$154.8 million, in fiscal 2014. In fiscal 2013, we had \$28.3 million of cash used in operating activities. Our cash and short term investments at September 27, 2014 were approximately \$88.7 million, compared with approximately \$33.0 million at September 28, 2013.

*Organizational Change.* In fiscal 2011 and 2012, we were focused on transforming the company from a portfolio of separately run businesses into an integrated, multi-brand company. During fiscal 2013 and fiscal 2014, we adopted a balanced approach to improving profitability through a focus on increasing sales and improving margins, providing superior customer service and delivering innovative new products. We expect to continue this balanced approach in the future and to continue to focus on eliminating inefficiencies and on increasing consumer take-away of our products.

*Harbinger Proposals.* In June 2014, we received an unsolicited letter from Harbinger Group Inc. requesting that we discuss with Harbinger a possible acquisition by Harbinger of all outstanding shares of Central's common stock at \$10 per share in cash or, alternatively, the acquisition of our Pet segment for \$750 million in cash, subject to due diligence. Our Board retained independent financial and legal advisors to assist it in its review of the two proposals. With the assistance of its advisors, the Board of Directors engaged in a comprehensive review which included consideration of current and expected operations, capital structure, and market opportunities. In addition, the financial advisor and our outside legal counsel met with Harbinger representatives to provide an opportunity to supplement or clarify their proposal. After this extensive review, the Board of Directors unanimously concluded in October that it would not pursue either of the two proposals received from Harbinger Group Inc. We incurred significant legal expenses and advisory fees during fiscal 2014 in connection with the review and expect to incur significant additional fees and expenses in the future. In addition, the uncertainty created by the proposals could cause current and prospective employees to experience uncertainty about their future roles with us, which may materially adversely affect our ability to attract and retain key employees and could continue to have a negative impact on our customer relationships, which could adversely impact our sales and financial results.

## **Competitive Strengths**

We believe we have the following competitive strengths, which serve as the foundation of our business strategy:

*Market Leadership Positions Built on a Strong Brand Portfolio.* We are one of the leaders in the premium branded U.S. pet supplies market and in the U.S. consumer lawn and garden supplies market. We have a diversified portfolio of brands, many of which we believe are among the leading brands in their respective U.S. market categories. The majority of our brands have been marketed and sold for more than 25 years.



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*History of Innovative New Products and Customer Service.* We continuously seek to introduce new products at a reasonable cost, both as complementary extensions of existing product lines and as new product categories. Over the last three years, we have received a number of awards for innovation, customer service and marketing. For innovation, the Pet segment received back to back Product of the Year awards in 2014 for the Adams Flea and Tick Home Spray and in 2013 for the Adams Smartshield innovation. For customer service, in 2013, we received awards for PetSmart Vendor of the Year in Canada for Specialty (Aquatics, Small Animal, Pet Bird), PETCO's 2013 Best Business Performance Award for Aqueon & Zilla brands, Wal\*Mart's Outdoor Living Supplier of the Year and Wal\*Mart's People Award for its home division. In 2012, we were named the Wal\*Mart Home Division Replenishment Team of the Year. For marketing, in 2013, the National Agri-Marketing Association (NAMA) recognized our professional products group for outstanding marketing communications for the new product introduction of Centynal as well as a W3 Award, in the Consumer Goods category, for the Adams website.

*Strong Relationships with Retailers.* We have developed strong relationships with major and independent retailers through product innovation, premium brands, broad product offerings, private label programs, proprietary sales and logistics capabilities and a high level of customer service. Major retailers value the efficiency of dealing with suppliers with national scope and strong brands. Our ability to meet their unique needs for packaging and point of sale displays provides us with a competitive advantage. Independent retailers value our high level of customer service and broad array of premium branded products. These strengths have made us one of the largest pet supplies vendors to PetSmart, PETCO and Wal\*Mart and among the largest lawn and garden supplies vendors to Wal\*Mart, Home Depot and Lowe's, as well as a leading supplier to independent pet and garden supplies retailers in the United States.

*Favorable Long-Term Industry Characteristics.* The pet and lawn and garden supplies markets in the U.S. are expected to grow over the long-term due to favorable demographic and leisure trends. The key demographics bolstering our markets are the growth rates in the number of children under 18 and the number of adults over age 55. Households with children tend to own more pets, and adults over 55 are more likely to be empty nesters that keep pets as companions and have more disposable income and leisure time available for both pets and garden activities. According to the 2013-2014 APPA National Pet Owners Survey, the number of U.S. pet owners in recent years has reached record highs, with 82.5 million households, or 68%, owning a pet.

*Sales and Logistics Networks.* We are a leading supplier to independent specialty retailers for the pet and lawn and garden supplies markets through our sales and logistics networks. We believe our sales and logistics networks give us a significant competitive advantage over other suppliers. These networks provide us with key access to independent pet specialty retail stores and retail lawn and garden customers that require two-step distribution for our branded products facilitating:

acquisition and maintenance of premium shelf placement;

prompt product replenishment;

customization of retailer programs;

quick responses to changing customer and retailer preferences;

rapid deployment and feedback for new products; and

immediate exposure for new internally developed and acquired brands.

We plan to continue to utilize our team of dedicated sales people and our sales and logistics networks to expand sales of our branded products.

*Experienced and Incentivized Management Team.* Our senior management team has significant experience in the consumer goods, pet, and lawn and garden supplies industries. John R. Ranelli, our

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President, Chief Executive Officer and President – Pet Segment, has extensive experience leading mid- to large-sized consumer companies. William E. Brown, our Chairman, has over 30 years of industry experience. Mr. Brown also owns approximately 12% of our outstanding stock.

### **Business Strategy**

Our objective is to increase market share, revenue, and cash flow by enhancing our position as one of the leading companies in the U.S. pet supplies and lawn and garden supplies industries. To achieve our objective, we plan to capitalize on our strengths and favorable industry trends by implementing the following key elements of our business strategy:

*Balanced Organizational Change.* We have adopted a balanced approach to improving profitability through a focus on increasing sales and improving margins, providing superior customer service and innovative new products while improving our operations and reducing costs. We expect to continue this balanced approach in the future and to continue to focus on profit, our customers, and eliminating inefficiencies.

*Build Existing Brands.* With our broad product assortment, strong brand names, strong sell-through and innovative products and packaging, we believe we can further strengthen our relationships with existing retailers to increase shelf space and sales. Under our master branding strategy, we have consolidated certain brands and expanded others. At the same time, we are developing private label programs for key retailers to complement our proprietary brands, strengthen our relationships with key retailers and increase sales and profits. We believe that the strength of our major customers provides us with a solid foundation for future growth. We intend to gain market share in the home centers, mass market, grocery, specialty pet store and independent channels. We intend to add new retailers through marketing and sales personnel dedicated to these channels, as well as our innovative product introductions and packaging. We will continue to focus on using our sales and logistics network to emphasize sales of our higher margin, proprietary brands and to use efficient supply chain capabilities that enable us to provide retailers with high service levels and consistent in-stock positions.

*Continue New Product and Packaging Innovation.* We will continue to build and leverage the strength of our leading brand names by introducing innovative new products and packaging, extending existing product lines and entering new product categories. Our product strategy seeks to capitalize on fulfilling consumer needs, leveraging our strong brand names, utilizing our established customer relationships and continuing our history of product innovation.

*Improve Margins.* We believe there are opportunities to improve our gross and operating margins through increased sales of our higher margin, innovative branded products, timely price increases and cost reductions and leveraging our existing infrastructure. Although gross margins improved from fiscal 2004 through fiscal 2010, they have declined significantly since then as we continued to experience fluctuations in the costs of raw materials and incurred costs in our Garden segment in fiscal 2014 and 2013 related to the discontinuance of certain products introduced in 2013. During fiscal 2013, we conducted a systematic review of pricing in our Pet segment and selectively raised prices consistent with market conditions. We will continue to work with our key retail partners to implement appropriate price increases on our products as we strive to strike the right balance between pricing and delivering value to the consumer.

*Pursue Strategic Acquisitions.* We plan to continue to make selected strategic acquisitions of companies that complement our existing brands and product offerings. By leveraging our marketing, manufacturing and sales and logistics capabilities, we believe we can increase the sales and improve the operating efficiencies of acquired companies. We look for companies with the potential to have the top one or two brands in their respective categories. The characteristics we generally seek when evaluating target companies are strong brand names, high quality and innovative product offerings, an experienced management team and a history of organic earnings growth.

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*Reduce Our Investment In Working Capital.* We believe there are opportunities to reduce our investment in working capital over the long term by focusing on specific balance sheet metrics. In particular, we believe that the improvement in our fill rates as a result of tighter linkage between our businesses and supply chain will enable us to substantially reduce our investment in inventory without compromising the level of the service we provide to our customers. During fiscal 2014, we reduced our inventory level from \$391.9 million to \$326.4 million while maintaining high fill rates.

**Products General**

The following table indicates each class of similar products which represented more than 10% of our consolidated net sales in the fiscal years presented (in millions).

Category	2014	2013	2012
Pet supplies (excluding wild bird feed)	\$ 774.2	\$ 807.4	\$ 847.1
Garden controls and fertilizer products	262.5	274.9	281.7
Wild bird feed	202.1	210.8	205.1
Other garden supplies	182.5	183.5	185.7
Grass seed	183.1	177.0	180.4
Total	\$ 1,604.4	\$ 1,653.6	\$ 1,700.0

**Pet Segment****Overview**

We are one of the leading marketers and producers of premium branded pet supplies in the United States. In addition, our Pet segment operates one of the largest sales and logistics networks in the industry strategically supporting its brands. In fiscal 2014, the Pet segment accounted for \$846 million of our consolidated net sales and \$88 million of our consolidated income from operations before corporate expenses and eliminations.

**Industry Background**

According to the Simmons Fall 2013 National Consumer Survey, the number of U.S. households with dogs or cats hit a new high in 2013 of 53.3%, up from 51.3% from the prior year.

The pet industry includes food, supplies, veterinarian care and services and live animals. We operate primarily in the pet supplies segment of the industry. This segment includes: products for dogs and cats, including edible bones, premium healthy edible and non-edible chews, toys, pet carriers, grooming supplies and other accessories; products for birds, small animals and specialty pets, including food, cages and habitats, toys, chews and related accessories; animal and household health and insect control products; products for fish, reptiles and other aquarium-based pets, including aquariums, furniture and lighting fixtures, pumps, filters, water conditioners and supplements, and information and knowledge resources; and products for horses and livestock. According to Packaged Facts, the pet supplies segment was \$14.1 billion in revenue in 2013, up 4.2% from 2012 with dogs accounting for 61%; cats at 31% and 8% all other animals. We also operate in the super premium category of dog and cat food and treats.

We believe this industry growth is due in significant part to favorable demographic and leisure trends, which we expect to continue, albeit potentially at a slower rate due to recessionary pressures in the broader U.S. economy. The key demographics bolstering the U.S. pet supplies market are the growth rates in the number of children under 18 and the number of adults over age 55. According to 2010 U.S. census data, approximately 40% of the population is 45 years or older. Households with children tend to own more pets, and adults over 55 are more likely to be empty nesters who keep pets as companions and have more disposable income and leisure time available for pets. In addition, many pet supplies products (e.g., dog and cat food, dog chews, bird food, grooming supplies, pest control, etc.) are routinely consumed and replenished.

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The U.S. pet supplies market is highly fragmented with approximately 1,400 manufacturers, consisting primarily of small companies with limited product lines. The majority of these manufacturers do not have a captive sales and logistics network and must rely on us or other independent distributors to supply their products to regional pet specialty chains and independent retailers. According to Packaged Facts, pet supplies sales are up 14 percent over the last five years. Sales are expected to increase an additional 13% by 2018, indicating the strength of this category.

The pet food and supplies industry retail channel also remains fragmented, with approximately 6,800 independent pet supply stores in the United States and only two national specialty retailers, PetSmart and PETCO. These two pet superstores have grown rapidly, and pet products have also become a growing category in mass merchandisers, discounters and grocery outlets. PetSmart and PETCO typically offer the broadest product selection with competitive prices and a growing array of pet services. Mass merchandisers, supermarkets and discounters have historically carried a limited product assortment that features primarily pet food, but we believe these retailers are devoting more shelf space to meet increased consumer demand for premium pet supplies. Independent pet stores typically have a relatively broad product selection and attempt to differentiate themselves by offering premier brands and knowledgeable service.

### ***Proprietary Branded Pet Products***

Our principal pet supplies categories are dog and cat, aquatics, bird and small animal food and animal health products.

*Dog & Cat.* The dog and cat division, featuring the brands Nylabone, Four Paws, TFH Publications, Pet Select, Pet Love and Mikki®, is an industry leader in manufacturing and marketing premium edible and non-edible chews, interactive toys, super premium dog and cat food, grooming supplies and pet-care print and digital content.

Nylabone is made in the United States and has a strong history of developing innovative products such as NutriDent® Edible Dental Brush Chews, as well as numerous other award-winning dog toys and healthy chews.

Four Paws Products include industry leaders in grooming and waste management products under the Wee Wee and Magic Coat Brands.

TFH Publications is a globally recognized publisher of both pet books and an aquatics magazine.

Breeder's Choice, featuring the Pinnacle®, AvoDerm®, Simply Natural® and Active Care® brands, is a manufacturer of super premium natural pet food and treats.

*Aquatics.* We are a leading supplier of aquariums and related fixtures and furniture, water conditioners and supplements, sophisticated lighting systems and accessories featuring the brands Aqueon, Zilla, Oceanic Systems, Kent Marine, Coralife and Blagdon.

*Small Animal & Wild Bird Feed.* We are a leading marketer and producer of specialty pet food for pet and wild birds and small animals, vitamins and nutritional supplements, bird and small animal cages, habitats, transportation devices, toys and other accessories designed for the small animal marketplace featuring the brands Kaytee®, Super Pet®, Critter Trail® and Canopy Scientific®. Kaytee is one of the largest producers of specialty bird feed.

*Animal Health.* We are a leading marketer and producer of flea, tick, mosquito and other insect control products produced by Wellmark International and sold primarily under the Bio Spot Active Care™, Adams, Altosid, Pre Strike and Extinguish® brand names. Wellmark is the only domestic producer of (S)-Methoprene, which is an active ingredient to control mosquitoes, fleas, ticks, ants and mites in many professional and consumer insect control applications. We also sell (S)-Methoprene to manufacturers of other insect control

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products, including Frontline Plus. In addition, through our Farnam operations, we are a leading manufacturer and marketer of innovative health care products for horses. Farnam's portfolio of industry leading brands includes the Farnam umbrella brand, IverCare®, Bronco®e, Super Mask® II, Endure®, Horseshoer's Secret® and Vetrolin®.

### ***Sales Network***

Our domestic sales network exists primarily to promote our proprietary brands and provides value-added service to approximately 4,300 independent specialty retail stores for our branded products. This includes acquisition and maintenance of premium shelf placement, prompt product replenishment, customization of retailer programs, quick response to changing customer and retailer preferences, rapid deployment and feedback for new products and immediate exposure for acquired brands. The network also sells many other manufacturers' brands of pet supplies and combines these products with our branded products into single shipments enabling our independent customers to deal with us on a cost effective basis to meet their pet supplies requirements. We also operate a sales and logistics facility in the United Kingdom.

### ***Sales and Marketing***

Our sales strategy is multi-tiered and designed to capture maximum market share with retailers. Our customers include retailers, such as regional and national specialty pet stores, independent pet retailers, mass merchants, grocery and drug stores. In addition, we also serve the professional market with insect control and health and wellness products for use by veterinarians, municipalities, farmers and equine product suppliers. PetSmart accounted for approximately 10% of our Pet segment's net sales in fiscal 2014, 11% in fiscal 2013 and 12% in fiscal 2012. PETCO is also a significant customer.

To optimize our product placement and visibility in retail stores, our focused sales resources are segmented as follows:

a sales organization operating by category and channel;

dedicated account teams servicing our largest customers;

a group of account managers focused on regional chains;

a geographic based group of territory managers dedicated to the independent retailer; and

a specialized group of account managers dedicated to the professional and equine markets.

These sales teams deliver our marketing strategy that is consumer, brand and channel driven. We provide value creation with a focus on innovation, product quality and performance, premium packaging, product positioning and consumer value. We collaborate closely with our customers to identify their needs, jointly develop strategies to meet those needs and deliver programs that include print, broadcast, direct mail and digital execution.

### ***Competition***

The pet supplies industry is highly competitive and has experienced considerable consolidation in recent years. Our branded pet products compete against national and regional branded products and private label products produced by various suppliers. Our largest competitors in most product categories are Spectrum Brands and Hartz Mountain. The Pet segment competes primarily on the basis of brand recognition, innovation, upscale packaging, quality and service. Our Pet segment's sales and logistics operations compete with Animal Supply Co., Phillips Pet Food & Supplies and a number of smaller local and regional distributors, with competition based on product selection, price, value-added services and personal relationships.





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### **Garden Segment**

#### ***Overview***

We are a leading company in the consumer lawn and garden market in the United States and offer both premium and value-oriented branded products. We market and produce a broad array of premium brands, including Pennington, The Rebels, AMDRO, Lilly Miller, Ironite, Sevin, Over-N-Out, and GKI/Bethlehem Lighting. We also produce value brands at lower prices, including numerous private label brands. In addition, our Garden segment operates a sales and logistics network that strategically supports its brands. In fiscal 2014, the Garden segment accounted for \$759 million of our consolidated net sales and \$41 million of our consolidated income from operations before corporate expenses and eliminations.

#### ***Industry Background***

We believe that gardening is one of the most popular leisure activities in the United States, although in recent years our garden segment has been adversely impacted by fluctuations in input costs and weather. The Freedonia Group predicts that household participation in lawn and garden activities will rebound slightly through 2018. The key demographic bolstering our lawn and garden market is the growth rate in the number of adults over age 55, who are more likely to be empty nesters and have more disposable income and leisure time available for garden activities. As the baby boom generation ages, this segment is expected to grow faster than the total population. According to 2010 U.S. census data, approximately 40% of the population is 45 years or older. We believe that this demographic should increase the number of lawn and garden product users. With more people gardening in their yards and the potential trends of food gardening and organic gardening, we perceive this market as staying intact and showing slow positive growth. We estimate the retail sales of the lawn and garden supplies industry in the categories in which we participate to be approximately \$10.2 billion. In addition, we participate in the pottery and seasonal décor markets. We believe that the industry will continue to grow, albeit at a slower rate in the near term due to industry dynamics.

Lawn and garden products are sold to consumers through a number of distribution channels, including home centers, mass merchants, independent nurseries and hardware stores. Home and garden centers and mass merchants typically carry multiple premium and value brands. Due to the rapid expansion and consolidation of mass merchants and home and garden centers in the last 15 years, the concentration of purchasing power for the lawn and garden category has increased dramatically. We expect the growth of home and garden centers, such as Home Depot and Lowes, and mass merchants, such as Wal-Mart, to continue to concentrate industry distribution.

#### ***Proprietary Branded Lawn and Garden Products***

Our principal lawn and garden product lines are grass seed, wild bird feed, insect control products, lawn and garden care products, decorative outdoor patio products and Christmas products and lighting. Our Pennington brand is one of the largest in grass seed, pottery and wild bird feed, and our Amdro brand is a leading portfolio of ant control products.

*Grass Seed.* We are a leading marketer, producer and distributor of numerous mixtures and blends of cool and warm season turf grass for both the residential and professional markets, as well as forage and wild game seed mixtures. We sell these products under the Pennington Seed, Pennington, Penkoted<sup>®</sup>, Max-Q<sup>®</sup>, ProSelect, Tournament Quality CM, MasterTuff, The Rebels and Smart Seed<sup>®</sup> brand names. We also produce numerous private label brands of grass seed. The Pennington grass seed manufacturing facilities are some of the largest and most modern seed coating and conditioning facilities in the industry.