

Nestle Sharpens Food Portfolio With Kraft, Alcon Transactions

By Martin Gelnar of DOW JONES NEWSWIRES

With two transactions in the space of two days, Nestle S.A. (NESN.VX) has positioned itself as more of a pure food company, bolstering its presence in an important category in North America, and pulling out of non-core ophthalmology.

Nestle said Tuesday it's buying Kraft Foods Inc.'s (KFT) frozen pizza operations in the U.S. and Canada, including brands such as DiGiorno, Tombstone and California Pizza Kitchen, for \$3.7 billion in cash. That was just a day after it sold its remaining stake in U.S.-based eyecare unit Alcon Inc. (ACL) to Novartis AG (NVS) for \$28.1 billion.

The moves underscore the transformation of Nestle, already the world's largest food and beverages producer by sales, into a more focused company. It now has just one big non-food asset left, a 29% stake in French cosmetics giant L'Oreal S.A. (OR.FR), which for the time can't be altered due to a complex contract with the other big shareholder, the Bettencourt family.

Following Nestle's deal with Kraft, seen as an opportunity buy as Kraft is struggling to keep its Cadbury Plc (CBY) takeover hopes alive, the Swiss company will become a dominant frozen pizza player in North America, the world's largest market worth \$37 billion, in which it has played a marginal role so far. The transaction is expected to close this year, pending regulatory approval. Nestle also said it wouldn't make or participate in any bid for Cadbury.

Many analysts welcomed the acquisition as an important step in a key category. "The deal, giving Nestle a fast-growing business with a potential 20% margin at an attractive price, would be seen as a good bit of business. Unfortunately it comes as Kraft is in the middle of a bruising battle for Cadbury, which takes the gloss off it," said Kepler analyst Jon Cox.

However, analysts from Zuercher Kantonalbank and Bank Vontobel doubted the takeover was a good strategic fit, adding they would have preferred acquisitions in areas such as nutrition or emerging markets. Nestle, which portrays itself as a company focused on health and wellness, said the acquisition is in line with its strategy.

"We try to improve the nutritional value of all of our products including prepared dishes," a spokeswoman said.

Independent food industry analyst James Amoroso said Nestle's bolstering of a traditional food category is compatible with its goals. "If Nestle produces the tastiest and 'best for you' pizzas, that is fulfilling its mission to the maximum," he noted.

Nestle's Prepared dishes and cooking aids division with brands such as Maggi, Buitoni and Hot Pockets, in 2008 generated sales of 18.1 billion Swiss francs (\$17.6 billion), or 16% if

the group total. The division had an operating profit margin of 12.8%, below the group average of 14.3%.

Nestle, which typically spends CHF2 billion to CHF3 billion each year for bolt-on acquisitions, has recently sized up in areas such as baby food, most notably the Gerber brand, and clinical food.

Late last year, the company strengthened its frozen pizza operations in Europe, buying a majority stake in Wagner Tiefkuehlprodukte GmbH, a company with an estimated market share of 33% in Germany.

Many market watchers now expect Nestle to increase the pace of takeovers. Among the companies believed to be on its radar screen are Mead Johnson Nutrition Co. (MJN), parts of Abbott Laboratories (ABT), or Fresenius SE's (FRE.XE) clinical nutrition operations. And in a recent study, Nomura suggested Nestle may at some stage consider a bid for General Mills Inc (GIS), its joint-venture partner in the area of cereals.

On the Swiss bourse at 1110 GMT, Nestle shares were down 0.5%, or CHF0.25, at CHF50.70 in an overall slightly lower general market.

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Dow Jones Newswires 05-01-10 11:25 GMT

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