

Nestle Raises Buyback Target as Sales Slip, Alcon Sale Looms (Update 3)

By Thomas Mulier



Oct. 22 (Bloomberg) -- Nestle SA, the world's largest food company, raised this year's buyback target and repeated its forecast that profitability will increase, mitigating a sales decline as consumers turned away from bottled water.

The Vevey, Switzerland-based producer of Perrier water and Nespresso coffee said it plans to buy back 7 billion Swiss francs (\$6.9 billion) of shares this year, up from a previous 4 billion-franc target, citing "solid operational performance." Nine-month revenue dropped 2.2 percent to

79.55 billion Swiss francs, also hurt by the franc's strength against the euro.

Nestle has an option to sell its majority stake in eye-care company Alcon Inc. to Novartis AG as early as January, prompting analysts to speculate whether the company will buy back more stock or make acquisitions with the proceeds, which may approach \$30 billion. Roddy Child-Villiers, head of investor relations, said today that Nestle will likely get the Alcon cash near the end of the first half if it exercises the option in January. There's a "strong likelihood" of an Alcon sale, Nestle said.

The food maker is "stoking expectations of a large new buyback after the Alcon sale next year," said Barbara Ambrus, an analyst at Landesbank Baden-Wuerttemberg in Stuttgart.

Credit Rating

Nestle is budgeting 2 billion francs to 3 billion francs for acquisitions a year, Chief Executive Officer Paul Bulcke said today. That's higher than the 1.5 billion-franc to 2 billion-franc range Nestle gave for this year on Aug. 12. Bulcke said Nestle is always open to "strategic" and "economically viable" acquisitions.

Bulcke has said Nestle plans no major takeovers this year and next, following Kraft Foods Inc.'s \$16.5 billion bid for U.K. candy maker Cadbury Plc. Nestle won't comment on confectionery takeover "rumors," spokesman Robin Tickle said today.

Child-Villiers said the company isn't aiming for a higher credit rating. Nestle slipped below the top ratings at both Moody's Investors Service and Standard & Poor's following the announcement of the current, 25 billion-franc buyback program in August 2007.

That buyback program will probably be complete around the end of the first half, and then Nestle's board will consider its options, Child-Villiers said.

'The Right Thing'

The buyback indicates "management think the shares are undervalued," said Andy Lynch, who manages \$1.8 billion at Schrodgers Investment Managers in London. It also suggests "they're not going to do hugely value-destructive acquisitions. From the shareholders' perspective, they seem to be doing the right things."

Bulcke said he has no "firm" answer as to when Nestle may exercise its option to sell its Alcon stake.

Under the terms of the option, Novartis would pay a 20.5 percent premium to Alcon's share price when the option is exercised, up to a maximum of \$181 a share. That means the maximum amount Nestle can get is linked to a share price of about \$150 a share. Alcon shares yesterday closed at \$145.72.

The timing of the exercise depends on the price, Child-Villiers said after Nestle's press conference. There's "no reward" in waiting to exercise the option if the shares are at \$150 in early January, Child-Villiers added.

Shares Rise, Forecast Repeated

Nestle rose 78 centimes, or 1.7 percent, to 46.66 francs at 11:53 a.m. in Zurich trading, the highest in almost a year. The stock is up 12 percent this year, outpacing the 2 percent gain by its nearest rival, Kraft Foods.

Nestle repeated its forecast for a higher 2009 operating margin, excluding currency fluctuations.

Excluding acquisitions, divestments and currency swings, sales advanced 3.6 percent and sales by volume rose 1 percent. Both figures matched the median analyst estimate.

"Nestle's business model is intact, and the slowdown that it has seen in 2009 will prove to be an exception driven by similarly exceptional economic circumstances," said James Amoroso, a food consultant in Walchwil, Switzerland.

Total sales were below the 80.14 billion-franc median estimate of seven analysts surveyed by Bloomberg News, constrained by the euro's decline against the Swiss franc. The strength of the franc cut 5.2 percentage points from sales growth, Nestle said, given that the company's food and beverage unit got 45 percent of its revenue from Europe last year.

Bottled Water

The euro was on average 6.1 percent lower against the Swiss currency in the first nine months, compared with the year-earlier period.

Third-quarter revenue fell 3.6 percent to 27.28 billion francs, below analysts' 27.88 billion-franc estimate.

Bottled water remained among Nestle's worst-performing businesses, with sales excluding currency movements and acquisitions declining 1.8 percent in the first nine months, while shipments dropped 2.3 percent. Nestle gets more than a tenth of its sales from bottled water following the 1990s acquisitions of Perrier and San Pellegrino, which sells at four times the price of a generic alternative in Swiss Coop stores. Both the recession and anti-bottled water campaigns by environmentalists have hurt demand for the product.

"Bottled water is facing the perfect storm right now," Andrew Wood, an analyst at Sanford C. Bernstein, wrote before today's results.

To contact the reporters on this story: Thomas Mulier in Geneva at tmulier@bloomberg.net.

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