

## FOCUS: Kraft's Cadbury Bid Subject To Currency, Share Moves

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LONDON (Dow Jones)--An early-November deadline for Kraft Food Inc (KFT) to make an offer for Cadbury PLC (CBY) leaves the U.S. food giant plenty of time to put together a bid, but its eventual valuation of the U.K. confectioner is to some extent subject to the vagaries of equity and currency markets.

With a deadline in place for Kraft to launch a formal offer for Cadbury, the focus has returned once again to valuation, with analysts expecting a formal Kraft offer to comprise around 850 pence a share.

Still, as the U.S. food giant is expected to wait nearly six weeks to launch its bid, the ultimate valuation could depend on gyrations in foreign exchange markets and the performance by Kraft's shares.

U.K. regulator The Takeover Panel granted Cadbury its wish Wednesday and set a deadline of Nov. 9 for Kraft to make a firm bid for the U.K. confectioner or to walk away.

Nobody expects Kraft to abandon its interests. Instead analysts expect the U.S. company will sit out the next six weeks and launch its offer just before Nov. 9.

*"Kraft will see no benefit in delivering an offer before the deadline," said industry consultant James Amoroso. "It will wait and see if any other bidders appear."*

Shore Capital analyst Darren Shirley agreed. "It wouldn't surprise me if Kraft used the whole six weeks," he said.

When Kraft makes its formal bid, it is unlikely to be at its initial proposal of 745 pence-a-share, which has received a lukewarm response from the market and a flat-out rejection from the Cadbury board.

Instead analysts are looking for a bid of between 800 pence and 900pence a share.

Evolution analyst Warren Ackerman said the market will also expect cash to account for 50% of the new offer - up from the current level of 40%.

Kraft's original proposal was to pay 300 pence in cash and 0.2589 new Kraft Foods shares for each Cadbury share. The bid was originally valued at 745 pence per Cadbury share, or GBP10.2 billion, but a fall in Kraft's share price since the announcement means that valuation is now closer to 720 pence.

The valuation would be even lower if the U.K. currency hadn't fallen in value against the dollar during the last week.

The pound has suffered on fears U.K. interest rates are going to stay low for the long-term and that the Bank Of England is happy with the weakness of sterling as it will drive up exports.

Any further weakness in the pound over the next six weeks is likely to play further into Kraft's hands, as it makes the proportion of Kraft stock in the deal much more attractive to Cadbury's share holders.

The share element of the deal also means that Kraft's share price movements over the next six weeks will influence an eventual takeout price. Kraft shares have dropped more than 6% since it first approached Cadbury on Sep. 7. As Kraft is proposing to pay part of the consideration in its own stock, this fall lessened the value of the bid.

Kraft's management will hope that the negative sentiment related to its offer for Cadbury is already priced into the company's shares. Any further downward drift in the shares will hurt Kraft's eventual offer.

*"Crucial will be the reaction of the Kraft share price upon the new offer announcement," said Amoroso. "If it sinks again, it may eradicate the increase in the cash offer."*

Cadbury itself has its own opportunity to influence proceedings with its third-quarter trading update on Oct. 21.

In July, Cadbury beat expectations with a 4% rise in first-half sales and increased its margin target for the full year, after a strong performance in emerging markets and its chocolate division more than offset slow sales in North America and Europe.

If its performance has weakened since the half year, Cadbury's claim that it can generate more value as a standalone company will look hollow and Kraft's offer may not need to be so full.

Any new offer from Kraft is expected to prompt counter bidders to show their hand.

"If there is a counterbidder, I think they'll emerge quite quickly after Kraft makes its bid" said Evolution's Ackerman.

Nestle SA (NESN.VX) and Hershey (HSY) are seen as the two most likely counterbidders - possibly in combination.

While Nestle's comments so far have suggested it's cool on the idea, Hershey might make the Swiss group a proposal to good to refuse.

"I wouldn't underestimate how much Hershey needs to do something," said Ackerman. "If it doesn't, it will be left as a peripheral player."

*Amoroso, however, views a counterbid as unlikely. "I continue to expect this to be a one-horse race, but the question is whether the one horse has the stamina to finish it," he said.*

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