

## Will Cadbury's optimism prove short and sweet?

26 February 2009 | Source: Dean Best

**Cadbury, the UK confectioner, injected a tone of optimism into the gloomy business climate yesterday (25 February) with a set of robust 2008 figures. The company also signalled its confidence by sticking to a key margin target but, as Dean Best reports, not everyone is convinced that Cadbury will meet its goal.**



[view image](#)

Amid all the doom and gloom over the economy, to hear a food company express confidence in its business yesterday (25 February) was something of a treat. And, perhaps fittingly, it fell to a chocolate maker to bring a tone of optimism to the bleak economic mood.

For Cadbury, the UK-based confectionery giant, the publication of its 2008 results - and its outlook for 2009 - was an indication that the business, after a tumultuous 12 to 18 months, is on track. Since the summer of 2007, when Cadbury CEO Todd Stitzer unveiled plans to revitalise the business with an overhaul of the company, the group has faced questions over its strategy.

Cadbury was accused of deserting its Quaker origins by angry UK employees upset at the closure of the Somersdale chocolate factory. Disgruntled investors, chiefly activist US shareholder Nelson Peltz, publicly demanded the company improve. The credit crunch and turmoil in the financial markets meant Cadbury had to de-merge, and not sell, its beverage operations in the Americas. And, meanwhile, Cadbury witnesses the creation of the world's largest confectioner when Mars and Wrigley sealed their US\$23bn deal last autumn.

However, in London yesterday, Stitzer was able to publish a set of strong numbers for 2008 and, in contrast to some of its food industry peers, speak optimistically about the outlook for Cadbury despite the global economic turmoil.

Cadbury posted rising sales, earnings and margins for 2008, helped in part by the weakness of sterling but also by rising prices and a 1% gain in volumes. Crucially, Cadbury maintained its 2011 "mid-teens" margin target - a goal the business set when Stitzer laid out that overhaul; of the business in 2007.

Stitzer spoke of the "resilience" of the confectionery market and said Cadbury's status as a "pure-play" confectioner would stand the business in good stead. Chocolate sales had been boosted as consumers stayed at home and treated themselves.

And, while gum sales had suffered as the downturn meant people travelled less often, Stitzer said Cadbury is looking to launch a series of gum lines in the US and the UK this year in a bid to boost sales. "The gum market is driven by innovation and marketing and we aim to continue that in 2009," Stitzer said.

A possible cloud on the horizon - and obstacle to meeting its margin target - could be the rising price of cocoa, which reached a 23-year high last month.

Ken Hanna, Cadbury's outgoing CFO, said cocoa prices had risen by 40% year-on-year in 2008 but insisted the company had already covered the higher cost through price increases. "We have taken sufficient pricing already in 2009 to cover input cost pressures," Hanna said.

*Industry watchers praised Cadbury's business model. "The performance looked rock solid," James Amoroso, director and consultant at Amoroso Strategic Insights, said. "They are doing a good job and they have become more efficient at it as well."*

Yann Gindraux, an analyst at Bank Vontobel in Switzerland, agreed that Cadbury had put in a good performance. "Organic growth was slightly above what we expected. Cadbury was able to compensate for raw material prices and the other restructuring programmes under way have started to yield results."

But just how sweet does the future look for Cadbury? Confectionery, and particularly chocolate, is a relatively defensive sector but, as consumer sentiment weakens in many markets, the jury is out on whether Cadbury will be able to enjoy the price increases it saw in 2008 to offset pressure on raw material costs.

Marco Gulpers, an analyst at ING in the Netherlands, said the economic downturn could make it difficult for Cadbury to meet sales targets and, as a consequence, hit that 2011 margin target. "In a difficult environment, volumes will come under pressure and it may not be as easy to get prices through as it was in 2008," Gulpers said. "If volumes are under pressure and pricing disappears, it will be a challenge to reach the low end of the 4-6% range for sales growth in 2009. This means that their operational leverage will come under pressure."

Gindraux argued that Cadbury's mid-teens margins target is "very ambitious" given that margins will have to continue to rise over the next two years. "[The target] implies over 100 bps per year, which is much lower than 2008 but it is tough to maintain such a high margin improvement over [a number of] years. Cocoa prices remain quite high and there are no signs of that easing either."

ING's Gulpers said he was "in the same camp". Cadbury, he argued, benefited from the fluctuations in exchange rates in 2008, which had been a "big positive" for the company. Given the weakness of sterling, Cadbury would again be boosted by currency in 2009, Gulpers said. However, he added: "This would reverse quite quickly if currency moves the other way."

Away from foreign exchange, Cadbury faces a formidable competitor in the combined Mars/Wrigley behemoth - and it is in gum that some industry watchers believe competition will be most fierce. Gulpers argued that Cadbury's gum margins are already high and should Wrigley - which will be a stand-alone company running the new company's gum business - decide to lower prices, particularly in the US, Cadbury could face problems hitting that 2011 margin target.

"In gum, the pricing component is crucial," Gulpers said. "The big driver for [Cadbury's gum business] is the US. We have not yet seen a more aggressive stance from Mars and Wrigley [in the US] since they joined forces in October. They have been more aggressive in the UK and the first signs there are not good for Cadbury."

"If Mars and Wrigley become more aggressive in the US, and there are no signs yet that they will, but you cannot rule it out, especially from a private company, they will catch market share."

However, as far as Mars and Wrigley are concerned, the big question surrounds how smoothly the two businesses will be combined. The deal was sealed in October and while the companies plan to divide its combined operations - Mars handling chocolate and Wrigley in charge of gum and sugar confectionery - the likelihood is that integration will be the key focus for the two groups in the months ahead.

*Amoroso agreed. "No integration, certainly not one of that size, is going to be that clean or that quick," he insisted. "How will the sharp end of things in the field work together?"*

For all Cadbury's progress in 2008, and optimism over 2009, the UK group will be no doubt hoping the Mars/Wrigley integration proves a sticky period for both its rivals.

© 2009 All content copyright just-food.com.  
Published by Aroq Ltd. Address & registered office:  
Seneca House, Buntsford Park Road, Bromsgrove, Worcs, B60 3DX, UK.  
Tel: Intl +44 (0)1527 573 600. Toll Free from US: 1-866-545-5878. Fax: +44 (0)1527 577 423.

Aroq publish [just-auto.com](http://just-auto.com) | [just-food.com](http://just-food.com) | [just-drinks.com](http://just-drinks.com) | [just-style.com](http://just-style.com)  
VAT No: GB785642391. Registered in England No: 4307068.