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Nestlé Buys U.S. Pizza Lines; Company Pays $3.7 Billion for Kraft Unit, Rules Out Bid for U.K. Candy Maker

By Martin Gelnar, 06 January 2010, The Wall Street Journal (Online and Print)

ZURICH — With two transactions in the space of two days, Nestlé SA has positioned itself as more of a pure food company, bolstering its presence in an important category in North America and pulling out of the noncore ophthalmology sector.

Nestlé said Tuesday it is buying Kraft Foods Inc.'s frozen-pizza operations in the U.S. and Canada, including brands such as DiGiorno and Tombstone, for $3.7 billion in cash. A day earlier Nestlé sold its remaining stake in U.S.-based eye-care unit Alcon Inc. to Swiss drug maker Novartis AG for $28.1 billion.

The moves underscore the transformation of Nestlé, already the world's largest food-and-beverages producer by sales, into a more focused company.

It now has just one big nonfood asset left, a 29% stake in French cosmetics giant L'Oréal SA, which, for the time being, can't be altered because of a complex contract with the other big shareholder, the Bettencourt family.

Following Nestlé's deal with Kraft, the Swiss company will become a dominant frozen-pizza player in North America, the world's largest market worth $37 billion, where it has played a marginal role so far. The transaction is expected to close this year, pending regulatory approval.

Kraft will use the proceeds from the pizza deal to sweeten its offer for Cadbury PLC. Nestlé said it wouldn't participate in a bid for the British confectioner.

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

But analysts from Zuercher Kantonalbank and Bank Vontobel doubted the takeover was a good strategic fit, saying they would have preferred acquisitions in areas such as nutrition or emerging markets.

Nestlé, 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 Nestlé'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.

Nestlé's prepared-dishes and cooking-aids division, with brands such as Maggi, Buitoni and Hot Pockets, generated sales of 18.1 billion Swiss francs ($17.57 billion) in 2008, or 16% of the group total. The division had an operating profit margin of 12.8%, below the group average of 14.3%.

Nestlé, which typically spends two to three billion francs a 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 Nestlé to increase the pace of takeovers. Among the companies believed to be on its radar screen are Mead Johnson Nutrition Co., parts of Abbott Laboratories or Fresenius SE's clinical nutrition operations. And in a recent study, Nomura suggested Nestlé may consider a bid for General Mills Inc., its joint-venture partner in cereals.

Nestlé shares closed at 49.75 francs ($48.31), down 1.20 francs, in Zurich.

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