

# Companies

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Edited by: leet@afr.com.au

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## PepsiCo peckish after NZ snack

Sue Mitchell

Beverage and snack food giant PepsiCo International is scouting for acquisitions in Australia after outlaying \$215 million to secure a major share of the New Zealand snack foods market.

PepsiCo Australia's chief executive, Alex Stevens, said the group planned to replicate its successful Australian snack foods strategy in New Zealand, following this month's acquisition of Bluebird Foods from Burns Philp.

PepsiCo was also running the ruler over second-tier snack brands for sale in Australia, amid challenging industry conditions made worse by rising input prices and the roll-out of private label products by major retailers.

"We're constantly looking at acquisitions in emerging areas as well as anything of scale," Mr Stevens told *The Australian Finan-*

### KEY POINTS

- PepsiCo is constantly looking for acquisitions in emerging areas.
- The New Zealand snack foods market is relatively underdeveloped.

*cial Review*. "PepsiCo has free cash flow in excess of \$US5 billion (\$6.4 billion) a year and for the right acquisition there's always capital available.

"There are more assets available now (than in the past 10 years) because it's getting harder to do business. The smaller guys are getting squeezed, and those guys who were making a bit of money are not making anything so they're looking to exit."

PepsiCo has achieved double-digit volume growth in snack foods in the past few years and has increased its share of the \$1.1 billion

salty snacks market from 42 per cent to 58 per cent, buoyed by its acquisition of Sakata Rice Snacks in 2005, The Smiths Snack Food Company from United Biscuits in 1998 and the launch of the Red Rock Deli brand in 2002.

It had no presence in the New Zealand market until the Bluebird acquisition, which gave it 50 per cent of the salty snacks category and about 40 per cent of nutritious and fruit snacks.

"The New Zealand market is relatively underdeveloped from an innovation, quality and consumer offer point of view and we see lots of upside in the business," Mr Stevens said.

Marketing expenditure would be increased to support key brands and sub-brands, including Bluebird and Le Snak, while gaps in the Bluebird product range would be filled with products from PepsiCo's Frito-Lay

and Quaker Foods portfolios. "The Bluebird brand is clearly the strongest brand in New Zealand and we'll build on that while leveraging, where we can, the best of local versus the best of global brands," Mr Stevens said.

Bluebird Foods and Griffins were in a margin-sapping price war last year but snack food prices have stabilised this year and industry observers believe prices are likely to rise as PepsiCo and Pacific Equity Partners (PEP) seek to build sales and earnings.

"I don't think PepsiCo will want to screw PEP but fix the (Bluebird) business and increase profitability," one source said.

PepsiCo pulled out of the race to acquire the Uncle Tobys snack foods business, which Burns Philp sold to Nestlé in May for \$890 million, but was still considering entering the nutritious snacks market in Australia.

## Sonic makes Esoteric purchase

Tracy Lee

Pathology services provider Sonic Healthcare will spend \$US180 million (\$230 million) to acquire a US-based laboratory business in a bid to add scale to its American operations.

Sonic has agreed to buy American Esoteric Laboratories from private equity firms ABS Capital Partners and Oak Investment Services.

The acquisition follows Sonic's \$US300 million purchase last year of a majority stake in America's No. 1 privately owned pathology lab, Clinical Pathology Laboratories (CPL).

"The acquisition of AEL represents an important second step in Sonic's US laboratory expansion strategy," chief executive Colin Goldschmidt said.

"When combined with CPL, AEL's size and geographical locations provide Sonic with the critical mass and reach to further accelerate its growth."

AEL has annual revenue of about \$US100 million and employs about 700 staff.

The acquisition should help allay market concern over Sonic's ability to lift its earnings per share.

The deal will be immediately earnings per share accretive but the

**"The acquisition of AEL represents an important second step."**

full earnings contribution from AEL is only expected to flow in fiscal 2008.

"Further potential synergies between the Dallas operations of AEL and Sonic's Texas-based laboratory, CPL, will likewise only impact in full year 2008," Mr Goldschmidt said.

Sonic has grown largely through acquisitions.

It has made about 50 acquisitions in its 20-year history but has recently been criticised for making lower-margin acquisitions.

AEL's purchase price of \$US180 million reflects a prospective earnings before interest, tax, depreciation and amortisation multiple of about 9.4 times.

Sonic suffered a 25 per cent price decline earlier in the year, before recovering in September. It closed 17c higher at \$13.56 on Friday.

Sonic will fund the acquisition through a six-month debt facility provided by Citigroup and Commonwealth Bank of Australia, but could refinance the facility over the coming months.

Earlier this year Sonic flagged future earnings growth of 10 per cent against a historical norm of almost 15 per cent.

Sonic plans to operate its US subsidiaries under its federation model, giving management more autonomy and leaving regionalised services in place.

The business has come under scrutiny after losing a large pathology contract in New Zealand to rival Healthscope.

The deal is expected to settle in the second week of January but is still subject to vetting by US competition authorities.

Sonic will retain AEL founder Brian Carr as a consultant.

## Forestry investors see way out of woods

Tracy Lee

Australia's forestry investment scheme promoters are set for an early Christmas present this week as the federal government prepares to release a review, expected to be largely positive, on the tax treatment of the sector.

Because the investment schemes are largely tax driven, with investors able to claim deductions on the subscription funds at the time of the initial investment, speculation that the government review could upset the model threw a cloud over the industry.

But last week federal cabinet agreed to give investors a 100 per cent tax deduction on the schemes as long as the promoter can prove that 70 per cent of the investment cost would be spent on tree husbandry.

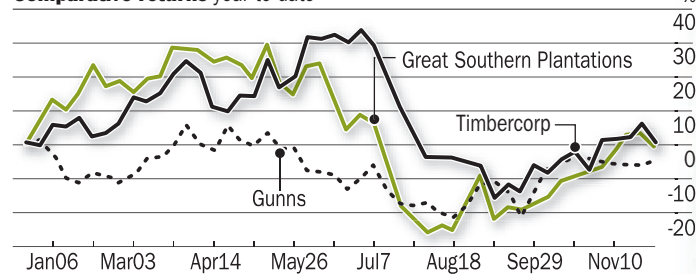
Shares in Gunns, Great Southern Plantations, Timbercorp, Forest Enterprises Australia and Willmott Forests are expected to steadily rise this week on the expectation the requirements will do little to change the way most promoters operate.

Fund manager Karl Siegling of Cadence Asset Management said the release of the review this week should lift a "cloud of uncertainty" that had been depressing the shares of companies in the sector since mid-year.

"The cloud of uncertainty

### TROUBLE IN TREES

Comparative returns year to date



### Market share of agribusiness investment sector

Company	Market share (%)
Great Southern Plantations	38
Timbercorp	27
Integrated Tree Cropping (Futuris)	4
Forest Enterprises	5
Gunns	*6
Other	20

\*Estimate

disappears and immediately the stocks will go a bit higher," said Mr Siegling, who has a stake in Forest Enterprises.

Great Southern Plantations, Timbercorp and Forest Enterprises all recorded modest price rises on Friday.

Timbercorp deputy chief executive Sol Rabinowicz said the requirement to show 70 per cent of funds were being spent on the investment would do little to change the way his company now operated.

"Our overall margin over the life of the project is less than 30 per cent, we can show we spend more than 70 per cent of what we take in running the forestry project," he said.

"We're cautiously optimistic [about the review], but we really need to see more detail behind what's proposed."

Almost \$300 million was wiped from the value of major companies in the sector in the middle of the

year when the government first announced the review and fears abounded that the tax concession on deductions could be scrapped.

Timbercorp, Great Southern and Gunns have diversified their investments into horticultural schemes such as grapes and avocados but this segment of agribusiness could also be the subject of a review by the government next year.

## Coles on track with Bi-Lo conversion

Simon Evans

Coles Group has converted 80 of its 210 Bi-Lo supermarkets to the Coles banner and has now temporarily frozen the \$132 million conversion program for a few weeks, while also bringing forward the expected finishing date in 2007.

The retailer is under pressure to lift sales and profits in its supermarket division after its board rejected an \$18.2 billion buy-out proposal from a private equity consortium.

The scrapping of Bi-Lo was one of the planks to lift margins in supermarkets.

The conversion program was suspended last week to avoid disruption during the busy Christmas

trading period and will recommence in early January. The expected completion date has been brought forward by a month to May.

This comes as officials from the Australian Competition and Consumer Commission spent the past week interviewing representatives from Coles, Woolworths and Metcash's IGA network as part of their preliminary inquiries in a review of whether supermarkets are profiteering on fresh meat prices.

The ACCC is checking whether supermarket chains are extracting unfair profits. Farmers who have sold livestock because of the drought have watched the prices they receive plunge but meat prices in supermarkets have remained constant.

ACCC officials have also been interviewing meat processors and farmers as part of the review requested by the federal government.

ACCC chairman Graeme Samuel declined to comment on the timetable for the review but confirmed it

**"The completion date has been brought forward to May."**

was taking place. "We are conducting the review and will report back to the minister," he said.

The review is separate from an investigation which Coles is undertaking internally into contracts and

practices in its meat purchasing division which relate to the dismissal of its supermarkets merchandise manager Peter Scott.

There are allegations Mr Scott had related-party property dealings with the owner of one of Coles's meat suppliers, Tasman Group. Mr Scott has declined to comment.

Coles chief executive John Fletcher promised a \$1.6 billion increase in sales over the next five years from changing Bi-Lo stores to Coles supermarkets. The group is assuming that each store will lift turnover by 7 to 8 per cent.

A Coles spokesman declined to comment on specifics, saying only that the converted stores had all recorded a "sales uplift".