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Nestlé to buy Chef America for $2.6bn

By William Hall in Zurich, FT.com site
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Nestlé, the world's number one consumer food company, has taken another big step into the fast food business with the $2.6bn acquisition of Chef America, a privately held US company, and the market leader in producing frozen sandwiches and other convenience foods.

Chef America, a Denver-based company owned by the secretive Merage family, is best known for its Hot Pockets and Lean Pockets frozen sandwich line and its Croissant Pockets brands. It dominates the frozen hand-held food market in the US with a market share of about 50 per cent.

Chef America's sales have been growing at a compound rate of 10 per cent a year since 1996 and are expected to top $720m in the current year. Earnings before interest, tax, depreciation, and amortisation (ebitda) have grown at 16 per cent a year over the same period.

James Amoroso of Zurich's Bank Vontobel, said that the price looked very high as a multiple of sales but it was more than compensated for by Chef America's profitability and growth rates. He estimates that Chef America has a 27 per cent ebitda margin. After adjusting for the tax benefits, which reduces the purchase price to $2bn, Mr ***Amoroso*** estimates that Nestlé is paying around 10 times ebitda. "Chef America's margins are the highest we have ever seen in the food industry", said Mr ***Amoroso***, a veteran Nestlé watcher. "It is a high margin, high growth business which Nestle can take internationally".

The US market for hand-held frozen foods is estimated to be growing at 7 per cent a year and is being driven by the changing eating habits of American consumers with an emphasis on greater convenience, "eating on the go", smaller and more frequent meals.

Glen Lee, Chef America's chief financial officer, said in a recent interview that the group wanted to expand internationally because "research shows that the lifestyle trends in Europe and Latin America are similar to those in this country 10 years ago".

Nestlé has been struggling to meet its own 4 per cent internal growth targets which have been held back by it heavy reliance on mature markets for products, such as soluble coffee and chocolate confectionery, where it is the market leader.

The cash acquisition is the latest in a series of aggressive moves by the Swiss food group which has been taking advantage of its Triple A credit rating, the weakness of world stock markets and the strength of the Swiss Franc, to build up its position in faster-growing segments of the US food industry.

Over the last 18 months it has paid $10.3bn for Ralston Purina, to become the world leader in pet food, and is in the process of finalising the takeover of Dreyer's, which will make it number one in the US ice cream market.

Mr ***Amoroso*** said that the latest acquisition did not reduce the likelihood that Nestle would bid for Hershey, the biggest US chocolate manufacturer, which has been put up for sale by the trust which controls it. "We reckon that Nestlé will generate free cash flow, post-dividends and capital expenditure, of SFr4bn ($2.69bn) this year, and that is going to increase next year", said Mr ***Amoroso***. It had plenty of scope for more acquisitions.

Rhone Group, a private New York investment boutique which advised Nestlé on the Dreyer's acquisition, was the Swiss company's adviser on the current deal.