

## In the Spotlight – The outlook for Danone

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**At first glance, a portfolio centred on probiotic yoghurts and bottled water may not be the best recipe for success in a recession. However, a booming baby food business could ensure Danone's rides out the downturn. Dean Best reports.**

For Danone, it seems that, for 2009 at least, the children are the future.



There had been a mood of apprehension in the run-up to the publication of the French food giant's 2008 results today (11 February).

Just how had the Activia-to-Evian group been affected by the undoubted consumer downturn in the fourth quarter of 2008? And just what would Danone's view of 2009 be?

Two weeks ago, Danone chairman and CEO Franck Riboud had hinted at a somewhat cautious mood flowing through the company when he attended the World Economic Forum in Davos.

"Like everyone else, I am putting brackets around 2009," Riboud said in an interview with French news channel France 24. Riboud said Danone was keeping its medium-term targets but said it would be wrong to set objectives for 2009.

An assessment, Riboud said, should be made at the end of January because "everything is moving in every direction". Instead of setting targets, Riboud said management should have the right tools to handle every situation that could come before it. "We must have a foot on the accelerator where things go well and a foot on the break where things go wrong," Riboud said.

For some, Danone's portfolio, centred on probiotic yoghurts and bottled water, two categories buoyant in a boom but difficult in a downturn, is perhaps ill-suited to navigating a recession when consumers switch to private-label products or reach for the tap.

Today, Danone admitted that the final three months of 2008 had been tough as consumer spending tightened. However, the company booked a set of solid annual results and maintained its earnings targets.

The economic downturn, Danone said, had weighed on consumers in most of its markets but the company insisted it expects consumption patterns to remain stable in 2009. The group Danone kept an earnings forecast issued in November. The company said it expects like-for-like sales to grow by "a few points below" its medium-term guidance of 8-10%.

Danone has also forecast a 10% rise in underlying fully diluted earnings per share on an organic basis and at constant exchange rates.

Chairman and CEO Franck Riboud said: "Our focus in each of our business lines will be simple: grow wherever the growth is, continue to perform above the category and strengthen our market shares."

*Industry watchers shared Riboud's optimism. James Amoroso, director and consultant at Amoroso Strategic Insights, said Danone had issued "solid results and a solid outlook". "The company has continued to give strong guidance for 2009. This demonstrates management's confidence in the robustness of Danone's business model," Amoroso said. "Like all other food companies to date, Danone experienced a weakening of sales growth in the final quarter of the year. But growth has remained strong."*

Sales growth did remain strong during the fourth quarter, rising 6% on a like-for-like basis. However, not all parts of Danone's business remained buoyant. Fresh dairy volumes dipped 0.3%, although sales did rise 3.8% in value terms. Danone's bottled water business, meanwhile, saw sales fall 1.5% due to falling volumes in Western Europe.

It fell to Danone's baby food and clinical nutrition businesses, acquired in 2007 following the EUR12.3bn takeover of Dutch firm Royal Numico, to post the most buoyant performance in late 2008.

Danone's baby nutrition business, which includes the Cow & Gate and Milupa brands, benefited from an easy comparison on 2007 and gains in China. Sales jumped 20.8% and by 14.8% in volume terms. Nevertheless, Danone was quick to point to "above-average market growth" from its baby food business, with growth in Western Europe, Eastern Europe, Russia and China.

Looking at figures for 2008 as a whole, Danone's baby nutrition business posted a 17% rise in revenue on a like-for-like basis to EUR2.8bn, just shy of the EUR2.9bn in sales generated by Danone's bottled water business.

Cedric Lecable, an analyst at Kepler Capital Markets in Paris, said Danone's moves into baby food and clinical nutrition set the business apart from some of its peers in the food industry. "Numico is a clear differentiator," Lecable told just-food. "Danone has more exposure to these niches than some of the other food players." Lecable said Numico now accounts for 30% of Danone's EBIT and he forecast further growth from the business in 2009. "In baby food, there is no serious private-label alternative," he said.

Private label however remains a formidable foe for Danone's dairy brands. Lecable argued that the company remains "very challenged" at the lower end of the dairy categories in which it operates. Danone has looked to counter that pressure by launching a cut-price range of yoghurts in France, although Lecable said the move had only had limited success due to the reluctance of some retailers to list a product competing with their own-label lines.

**Amoroso**, however, said the launch of the Ecopack line "seems to have had some success: i.e. new growth without cannibalisation. In my view, Ecopack is a brilliant piece of product segmentation. It's a shame that certain retailers have blocked consumers' access to this product".

One problem that could preoccupy Riboud and his management team in the months ahead is the performance of Danone's bottled water business. While bottled water is popular in some emerging markets of the East and Latin America, in Western Europe and Japan the business is struggling.

Lecable argued that Danone could look to sell its bottled water businesses in Western Europe. "My perception is that if they could dispose of the Western European bottled water business they would probably do it," Lecable said. "The problem is finding an acquirer. The big US guys would not want it in my view. They want to be in fast-growing niches to offset the decline of cola in the US."

The baby food market, meanwhile, remains child's play for Danone.

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