Poultry industry challenges shape Sovereign Foods results

Sovereign Foods recently released their annual audited financial results for the 2017 financial year, reporting that revenue increased by 25% to R2,2 billion in the period under review. While the financial results for the group were better than expected, a number of factors lead to subdued results. According to Chris Coombes, Sovereign Foods CEO, three unusual events converged to create one of the most difficult trading years in the history of the company.

Sovereign Foods reports increase in revenue despite difficult trading year
18 May 2017

Chris Coombes, Sovereign Foods CEO

Coombes said the three factors affecting the results this year were the once-off corporate activity costs, high feed costs as a material manifestation of the 2015 and 2016 drought and the subsequent ripple effect on soft commodity prices during the period under review, and EU dumping of bone-in chicken portions in South Africa.

Once-off corporate activity costs

Coombes said that corporate activity costs of R30.7m or 41.2 cents per share were incurred during the year under review which included:

• Costs (including legal, advisory, regulatory, printing and venue costs) associated with Sovereign's empowerment transaction. The transaction was approved by more than 85% of Sovereign shareholders, but was withdrawn as a result of the actions of Country Bird Holdings Limited ("CBH") and its related and concert parties;

• Costs associated with the legal proceedings instituted by CBH related and concert parties against Sovereign in the High Court;

• Legal costs associated with dealing with numerous and frequent correspondence from CBH and its concert parties and their attorneys (including further litigation threats);

• Costs associated with various Competition Commission processes occasioned by the actions of CBH and its concert parties, including a merger filing and submissions relating to the offer made by CBH to acquire the entire issued share capital of Sovereign (excluding treasury shares);

• Costs associated with the hearing before the Special Committee of the Takeover Regulation Panel, which ruled that CBH's purported waiver of the condition as to minimum acceptances under the CBH Offer was unlawful and that the CBH Offer had terminated.

Historic drought increased feed costs with 24% during FY2017

The historic drought also weighed in heavily this year. "El Niño weather patterns produced the driest year on historic records. As a result, feed costs, which represent 50 – 55 % of input costs in our business, increased when SAFEX white maize, yellow maize, and soya bean prices respectively increased by 24%, 12% and 20% in FY2017," he said.

However, Coombes said that the group's maize import procurement strategy in the Eastern Cape resulted in the group's feed cost on a rand per ton basis increasing by only 16% compared to the previous year. The situation will turn around in the 2018 financial year, and it is expected that the price of feed in the forthcoming financial year will decline substantially.

"The South African Crop Estimates Committee's latest estimate indicates that South Africa will have its second largest maize crop and largest soya bean crop with the maize crop estimated at 14.5m tonnes and the soya bean crop estimated at 1.2m tonnes."

"This has caused a 55% decline in the price of the single biggest cost in poultry production, with July 2017 white maize reaching a low of R1,700 per ton on 23 March 2017 after reaching a high of R3,786 on 19 January 2016. Similarly, July 2017 soya beans have declined by 24% from a high of R6,325 to R4,808 on 27 March 2017."

EU dumping takes toll too

"The effect of dumping in South Africa has been well documented and debated. While our risk portfolio is diversified through value-added, fully cooked and fresh chicken products, we too felt the burden and corrosive effects of dumping especially on revenue streams from our commodity product lines," Coombes said.

"We are, however, pleased with the will demonstrated and speed of efforts between government, business and organised labor to find, devise and implement strategies of trade support, higher tariffs on imported chicken and an improvement in policies and regulations."

Private-public sector efforts to find solutions for poultry industry woes welcomed
7 Apr 2017

Group optimistic about financial 2018

Coombes said Sovereign Foods was confident for the new financial year for a variety of reasons:

• Exports of fully cooked and raw products continue to increase and Sovereign Foods continues to build a solid export sales channel into the food services and retail channels in the Middle East.

• Cost reduction remains a strong focus for management and despite a 6% depreciation in the R/$ exchange rate and increases in the costs of energy and labour, group non-feed costs (excluding once-off costs and recoveries in both reporting periods) only increased by 8% per kg sold.

• A number of factors have led to a decline in the volume of poultry imports in the fourth quarter of 2016:

- Avian Influenza in the EU and the US which meant that certain countries are precluded from exporting to South Africa
- The recently imposed provisional 13.9% TDCA tariff against the EU has increased the landed cost of poultry from the EU
- The international price of poultry, as measured in dollars, has started to increase
- The recent meat “scandal” in Brazil has meant that certain consignments of product have been rejected by the South African authorities.

• Local production volumes have also recently been reduced due to the recent well-publicised industry production cutbacks, the shutting down of several smaller producers in 2015 and 2016 and the implementation of the brining cap in October 2016.