Low maize price boosts food producers

Food producers' shares have proved a good bet this year, producing market-beating returns. What's fuelled their winning streak has been the plunging price of the sector's key inputs: maize and wheat.

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The risk of input prices spiking higher is low. The US maize and wheat crops will set records in 2014, as will global production, the US agriculture department predicts. South Africa's (SA) maize crop is also heading for a record.

Lower input prices have brought relief to Tiger Brands, SA's largest food producer. From a weak first half in which headline EPS (HEPS) lifted only 6%, Tiger recovered in the second half to end its year to September with HEPS up 11%.

Yet to recover fully is Tiger's reputation, hit by its loss-making Nigerian unit, Dangote Flour Mills (DFM). Acquired in October 2012 for R1,5bn, DFM has since run up losses of over R650m, prompting Tiger to impair its investment by R954m in its latest reporting period.

Adding to Tiger's woes has been falling market share in its key SA grocery business, home to brands such as All Gold, Koo, Jungle and Black Cat.

But Tiger CE Peter Matlare believes the worst is behind it. Of DFM he says: "New management is in place and losses are falling. It should be profitable in one to two years."

In SA, Matlare points to Tiger's grocery business, which upped sales 23% to R3,97bn, 18% of group sales. "We are regaining lost market share," he says.

"Tiger is starting to do the right things," says First Avenue CIO Hlelo Giyose That said, First Avenue has cut its exposure to Tiger from 10% to 4%.

There is reason for caution. Tiger faces tough opposition, not least from a resurgent Pioneer Food Group, headed since

April 2013 by Phil Roux, Tiger's former consumer brands head.

Tiger and Pioneer are archrivals in many key sectors, including groceries, bread, pasta, rice, cereals and beverages. Pioneer's brand line-up includes Bokomo, Heinz, Sasko, Ceres, Wellington and Safari.

Roux is fast making his mark. Pioneer's HEPS jumped 37% in its year to September. This is just the start, says Old Mutual fund manager Warren Jarvis "We will see good growth from Pioneer for many years."

At work is far more than improved efficiency. "Pioneer has been completely re-engineered and has a new business model," says Roux.

Pioneer's market share in key segments is also rising, a trend Roux predicts has a long way to go. "There is a lot of scope to leverage our brands," he says.

An "African food business of scale"

Oasis Group CE Adam Ebrahim says RCL is another challenger in the food sector with big potential. "It is an undervalued share with great management," he says.

A 73%-owned unit of Remgro, RCL has evolved rapidly off its Rainbow Chicken base. First came Foodcorp, acquired in May 2013. It provided entry into groceries through brands such Nola, Pieman's, Yum-Yum, Sunbake and Dogmor.

The acquisition of Remgro's TSB Sugar followed in January 2014, adding one of SA's biggest sugar producers.

Ebrahim expects a big profit kicker from Rainbow, now enjoying a lower maize price and higher chicken prices. Rainbow's operating margin on sales of R8bn has the potential to lift from 1% to 7,5%, he says.

But the big growth opportunity for RCL is in Africa, says Ebrahim. Indeed, RCL's goal is to be an "African food business of scale". Through its Vector unit, one of SA's largest logistics firms, RCL is well positioned to achieve its goal, says Ebrahim.

In a three-way contest between Tiger, Pioneer and RCL, Pioneer appears set to remain the market favourite. But RCL is also worth attention.

RCL is not popular at present, says Ebrahim. But he predicts: "Its next results will spark market interest."