

Company Watch: Cadbury weighs up options against industry consolidation

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The spin-off of its beverages division and the recently announced proposed merger between Mars and Wrigley have put Cadbury in a precarious position at the head of the world's confectionery market. In order to retain its leading position it will need to accelerate growth, either organically or via acquisitions, or it could easily become a takeover target itself.

Cadbury is the number one confectionery company in the world with a 10.1% market share in 2006. After the divestment of its beverages division Cadbury is trading as a stand-alone company with a complete focus on its core confectionery activities. The firm posted 14% growth in 2007 in gum, which is the fastest growing segment of confectionery, and is expected to grow at a CAGR of 3.1% over 2007-2012. Cadbury was second in the global gum market in 2006 with a 27% share, behind Wrigley with a 34% share. Around 35% of Cadbury's sales are generated in emerging markets, providing a good platform from which to expand further in these fast growing regions. Cadbury is well positioned to grow in line with the industry but to keep its top position in this rapidly consolidating market it will need to do more.

Past plan to acquire Hershey could work now

Pursuing a merger with Hershey Co is the most talked about option. The two companies' brand portfolios and geographical market strengths would complement each other well. Cadbury's strong presence in European and emerging markets would offer instant international growth to Hershey, while Cadbury would leap to number one position in the North American market. Combined Cadbury-Hershey shares could reach 30% of the US\$32.2 billion North American market. However, the reasons why Cadbury and Nestl 's joint bid in 2002 was turned down have still not changed.

In 2002 the deal fell through mainly because Hershey's controlling shareholder, Milton Hershey School Trust, did not want to dilute its control and was also pressurised by workers' protests against the sale. In October 2007 the Trust issued a statement in which it emphasised its intention to retain its controlling interest in the Hershey Co. However, market conditions have changed since 2002 and the merger could make more commercial and strategic sense. Mars and Wrigley's proposed merger will knock Hershey off its number one position in the North American market. Some 93% of Hershey's sales come from the very mature North American market. The North American confectionery industry expects to achieve a low CAGR of 1.2% over the forecast period and other macroeconomic conditions, such as the weakness of the dollar or current credit restrictions, will affect Hershey's performance.

In order to stay competitive Hershey will need to increase its presence in the faster growing gum sector, in which it currently commands only a 1.3% share of the global market, and enter new emerging markets. A merger with Cadbury would fit well with part of this strategy.

Other potential targets for Cadbury

On the list of potential target companies Ferrero and Lindt both rank highly for different strategic reasons.

Ferrero, unlike Hershey, would not offer the number one position in the North American chocolate confectionery market but it has a strong position in another market in which Cadbury itself has little presence. Ferrero commands a respectable 4.8% share of the Latin American chocolate confectionery market, only fractionally behind Hershey's 4.9% share. In the same market Cadbury has only a 0.7% share. Buying Ferrero would also make Cadbury the number one chocolate confectioner in Western Europe with combined shares of 22.5%, overtaking current leaders Nestl ' (13%) and Mars (12.6%). But as Ferrero is a well performing, family-owned company it is hard to see the real possibility of an acquisition.

Lindt's premium and super-premium chocolate range would enable Cadbury to expand into the fastest growing segment. Premiumisation is currently the driving force of the global confectionery industry. Acquiring premium brands increases value growth and allows higher margins.

However, both Ferrero and Lindt performed markedly above industry level over the review period. Lindt has been the fastest growing among the top 10 chocolate confectionery companies with a CAGR of 14.6% over 2001-2006, while Ferrero achieved a CAGR of 10.2% compared to a 7.8% CAGR for the world market. For this reason, the price of these companies could be high.

Cadbury could become an acquisition target itself

The sequence of events in the confectionery market and Cadbury's own restructuring process suggest it could become

an attractive target for a number of other industry players.

Kraft's confectionery performance over the last few years has been declining, and its number four ranking in the global market in 2001 fell to sixth place by 2006. This is partly the result of Kraft's weak presence in the emerging markets, therefore hindering its growth prospects. Cadbury is the second biggest confectionery company in Asia-Pacific with a 5.1% share, which would significantly boost Kraft's 0.4% share in the region. The other weakness of Kraft is being under-represented in the main growth areas, such as gum. Buying Cadbury would offer a 27% share of the global gum market. Cadbury is in a position to increase Kraft's international presence as well as its brand portfolio with truly global brands.

Cadbury's gum portfolio might also be tempting for Nestl  . Nestl   is the third largest confectioner, commanding a 7.7% share of the global market. However, it has very little presence (0.1% share) in the fast growing gum segment. In order to restore growth to its confectionery division, Cadbury or its gum range represents an attractive option.

Following the recent consolidation in the global market Cadbury has found itself at a crossroads and will need to act aggressively to stay ahead of its competitors, especially given its intention to focus its business on confectionery. As consolidation has increased there are fewer targets for acquisition or merger and none will be without hurdles to overcome. If Cadbury is not able to find a solution to this it might become an acquisition target itself.

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