Opinion **Lex**

# Nestlé: Third Point has a point

Activist investor puts Kit Kat maker under pressure to increase margins

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In the activist playbook, patience is not a virtue. So weaker than expected results from Nestlé will do nothing to soothe sharp-tongued investor Dan Loeb, who last month told the world's largest food company to move with "greater alacrity".

It is now more than seven months since his US hedge fund Third Point called for a shake-up of the world's biggest food company, in which it took its biggest stake yet.

Nestlé has met Mr Loeb more than halfway. It swiftly announced a share buyback and has started to rejig its portfolio, most notably with a $2.8bn sale of its slow-growing US confectionery business. Acquisitions are in the offing although investors should not count on big deals to boost returns. Despite the reputation of Nestlé's newish chief executive, Ulf Mark Schneider, for dealmaking he is rightly cautious given the high valuations in the sector.

The biggest disagreement concerns Nestle's 23 per cent stake in L'Oreal. Nestlé is loath to get rid of the stake, although at least it said on Thursday it would not increase it. Its reluctance to sell is unsurprising. The beauty company is a valuable asset, its shares having risen almost 60 per cent over the past five years. That compares with just 22 per cent for Nestlé.

But in calling for a sale, Mr Loeb makes a valid point. The investment, makes little strategic sense. Shareholders should be able to choose to invest in it directly rather than hold a second-hand stake.

He might also be right to argue for more ambitious margin goals. Nestlé wants to push up operating margins towards 18.5 per cent by 2020, up from 16.4 per cent last year. Not enough, says Mr Loeb, who wants to see margins of 18 to 20 per cent.

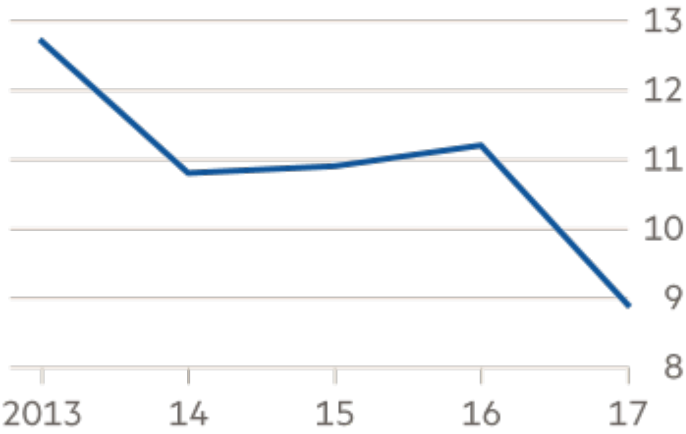
That would be the same sort of improvement being targeted by Unilever and Danone, two other consumer goods companies that have been targeted by activists. There is a case for Nestlé to follow suit with these rivals. The added earnings, assuming they flow through to the net line, would justify a significantly higher share price. Failing that, Mr Loeb might need to learn some patience after all.

## Share prices

Rebased in € terms

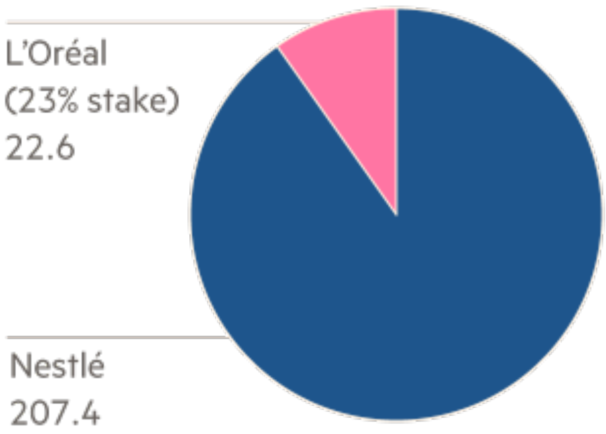

## Nestle return on invested capital

After goodwill and intangible assets (%)




## Nestlé and its stake in L'Oréal

€bn




Source: Sources: Thomson Reuters; company; S&P Capital IQ
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