Foodcorp purchase puts RCL Foods under pressure

By Zeenat Moorad

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RCL Foods, formerly Rainbow Chicken, on Tuesday (27 August) reported a 93.2% decline in full-year headline earnings from continuing operations to R18.1m, as funding costs from its Foodcorp deal and an effective tax rate of 113.5% weighed down its results.

The company's name change reflects its goal to broaden the range of brands and product categories in produces to counter the cyclical nature of the chicken industry, which had seen a deluge of cheap chicken imports from Brazil and the European Union.

This had put pressure on domestic poultry producers, forcing them to diversify into other markets. The group now consists of Rainbow, its chicken business, the logistics business, Vector, and Foodcorp, the producer of, among others, Yum Yum peanut butter and Ouma Rusks.

The Foodcorp deal was approved in May. Subsequent to its year-end, a further 23.9% stake was purchased by RCL Foods from Foodcorp's management to bring its total holding to 88.1%.

"The acquisition of Foodcorp has had a significant impact on the financial position at RCL with International Financial Reporting Standards 3 requiring recognition of net assets acquired at fair value. This resulted in assets and liabilities purchased on 1 May amounting to R6.6bn and R7.8bn respectively. The purchase price of the acquisition was R1bn resulting in goodwill of R2.6bn being recognised after the completion of a preliminary purchase price allocation exercise," the company said.

Extremely difficult year

RCL Foods' revenue for the 12 months to June grew 28.7% to R10.1bn, largely due to the inclusion of two months of Foodcorp's results. A loss after tax from continuing operations of R8.9m was recorded from a profit of R266.8m previously.

Rainbow experienced an extremely difficult year with high import volumes and record feed input costs decimating margins. individually quick frozen products sold below cost for most of the financial year. The company recorded a R3.7m operating loss for the period.

Droughts in Argentina and the US in the previous season had a significant effect on the international maize and soya prices, with the extremely low stock levels in the US heightening price volatility. This translated into escalated feed costs.

"In view of the losses being incurred in Rainbow, and in compliance with the requirements of IAS 36 (Impairment of assets), the board and RCL Foods have considered the need for an impairment of assets. Based on the outcome of the discounted cash-flow model and the need to await the outcome of the application for anti-dumping protection, the boards have decided that it would be inappropriate to impair poultry assets at this point. If there is not a notable improvement in operating margins within the next 12 months then an impairment of assets will become necessary," it said.

Vector's operating profit decreased by 15.1% to R143.3m due to investment in additional capacity and a slowdown in principals' volumes in the second half.

Looking ahead, RCL Foods said the poor state of the global and local economy meant a sustainable improvement in consumer sentiment and spending was unlikely in the near future.

"The poultry industry is at crisis point and anti-dumping protection will be key to its survival. The group continues to explore opportunities in strategic growth markets in the food sector in South Africa and sub-Saharan Africa in line with its long-term aspirations," it said.

Following its purchase of a stake in Zam Chick from Zambian agricultural producer Zambeef, Rainbow Chicken reached an agreement with Zambeef to establish a joint hatchery for the supply of day-old chicks.

Avior Research equity analyst Jiten Bechoo said many of SA's poultry producers were looking to Africa, and Zambia in particular, for the next wave of growth.