



## Saputo's Multibillion-Dollar Opportunity

### Description

In China, the average person drinks 9.4 kilograms of milk per year.

Over the course of a year, 9.4 kg isn't very much. It's the equivalent of about two-and-a-half four-litre jugs. To put it in perspective, in my two-person household, we go through a four-litre container in about two weeks.

In Japan and South Korea, the average person ingests more than 30 kg of milk per year. In the United States, average consumption is about 80 kg per person per year. The U.K. and Australia are the world's leaders in milk consumption, drinking more than 100 kg of the stuff per person per year.

It's obvious that China's milk consumption is set to go up, and should do so in a hurry. I'd say it's a bit of a reach for the country to catch up to the U.K.'s or Australia's love of dairy, but matching Japan's or South Korea's consumption isn't an unreasonable growth target. If China catches up to its neighbours' milk habits, that's an additional 21 kg per year multiplied by 1.36 billion people.

That's a lot of milk.

It's also a huge potential market for Canada's largest milk producer, **Saputo** ([TSX: SAP](#)). The company is very aware of this trend, and has taken steps to ensure itself access to the Chinese market by buying Australian milk producer Warrnambool Cheese and Butter. Australia and New Zealand are already major milk exporters to China, with growth expected to continue over time.

### Not just China

During the company's most recent conference call, CEO Lino Saputo Jr. spoke about the many acquisition opportunities available around the world. He openly mused about opportunities in the severely fragmented U.S. market, as well as trying to expand the company's presence in Brazil by either buying a producer in the country or exporting from its operations in Argentina.

The company also sees opportunity to consolidate more smaller producers in Canada, and perhaps make an acquisition in New Zealand. Not only does strengthening its position in the region further

expose it to the huge potential of the Chinese market, but it also gives the company access to local customers who are some of the biggest consumers of milk in the world.

There's also potential for the company to expand into markets like Russia, Taiwan, or the Middle East. These nations are all low milk consumers right now, largely because they simply don't have the infrastructure to supply milk to large portions of the population.

### **Saputo's financials**

Saputo is simply taking the earnings from its mature Canadian and U.S.-based divisions and using the money to expand internationally.

Its balance sheet is solid. The company does have more than \$1.6 billion in debt, but that compares to more than \$5 billion in assets. Revenue has increased more than 25% since the end of 2010, with earnings increasing by about 33%. Not only is the company growing substantially with these acquisitions, but it's also translating them into bottom-line growth.

Saputo's current dividend is \$0.92 per year, a yield of just 1.55%. In 2013, the company earned \$2.60 per share. That's a dividend payout ratio of just 35%, among the lowest on the TSX. Analysts are expecting the company's earnings to grow to \$2.83 in 2014, mostly due to the company's expansion into Australia. Look for Saputo to gradually increase its dividend as it digests the latest transaction.

The company is perhaps a little expensive at more than 22 times trailing earnings, but growth should bring its P/E ratio down to a more reasonable level. Besides, 22 times earnings isn't an unreasonable price to pay for a company with such obvious growth prospects.

Saputo is poised to do well in North America, where tariffs protect it from foreign competitors. Even if volumes go down, it'll be easy to raise prices. It's also well positioned to expand into some of Asia's growth markets. If the company can execute its ambitious growth plans, then Saputo deserves a spot in your portfolio.

### **CATEGORY**

1. Investing

### **TICKERS GLOBAL**

1. TSX:SAP (Saputo Inc.)

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### **Date**

2025/08/13

### **Date Created**

2014/05/27

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