KBC Securities

Flash

Ter Beke

13 March 2007

Growth hits profits

Food Producers & Processors

Belgium

Performance over	1m	3m	12m
Absolute	-1%	4%	6%
Rel. BEL20	3%	3%	-6%
Relative to sector	-1%	4%	6%
12m Hi/Lo	€ 68.50/63.80		
Reuters	TERB.BR		
Bloomberg	TERB BB		
Market Cap	€ 117m		
Next corporate event			
Trading update 1Q07: 11 May 2007			

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Current price € 67.80

Target price € 71.00

Accumulate

Rating Unchanged

FY/e 31.12	2006	2007E	2008E	2009E
Sales	326.7	363.9	377.4	391.4
REBITDA	24.0	29.5	31.9	34.6
Net earnings	6.0	6.5	7.7	9.3
Diluted, adjusted EPS	3.70	3.74	4.42	5.30
Dividend	2.10	2.15	2.20	2.25
P/E	17.7	18.2	15.4	12.8
EV/REBITDA	8.1	6.5	5.9	5.3
Free cash flow yield	-3.5%	5.3%	5.6%	6.6%
Dividend yield	3.1%	3.2%	3.2%	3.3%

Source: KBC Securities **Adjusted for goodwill and exceptionals*

Description: Ter Beke is specialized in chilled ready meals and processed meats. It is the European market leader in chilled lasagna.

Investment arguments

- Ter Beke's margins took a severe hit in 2006 as a result of external and organic growth
- Chilled ready meals and slicing/packaging activities offer attractive growth opportunities
- We anticipate that profits will pick up in 2007 following the successful integration of Pluma.
- Target price based on sum-of-the-parts: EV/EBITDA of 5.0 for processed meats and 7.0 for ready meals

Ter Beke's margins took a severe hit in 2006 as a result of external and organic growth. The merger with Pluma resulted in extra costs, a sharp rise in financial charges and a 26% rise in the number of outstanding shares. The group's desire to gain market share in France led to the signing of sizeable but poorly-priced contracts and production inefficiencies at the Alby-sur-Chéran factory. The corporate structure of the group has been adjusted to facilitate external growth. Separate legal entities and management committees have been set up for the two divisions, which has also fuelled the rise in costs. During FY06 sales rose by 38.3% on the back of external and organic growth but the operating margin collapsed from 4.5% in 2005 to 2.6% 2006 (our forecast: 3.3%) if we exclude the impact of a provision reversal in 2006. Management is yet to provide concrete guidance for 2007 but indicated that margins will be dampened by:

- **Extra costs related to the new corporate structure;**
- **Increased sales efforts to promote Come a Casa in France;**
- **Costs related to NPC (potential acquisition).**

Given the above, we have lowered our 2007 and 2008 EPS forecasts by respectively 9% and 6%. We nevertheless maintain our Accumulate rating. The FY06 results were disappointing but management assured us that there will be an increased focus on margin improvement in 2007.

Review FY06 results

Ter Beke's FY06 net profits and turnover were in line with our expectations but operating profits and pretax profits fell far short of our forecasts. Lower-than-expected pretax profits were offset however by an exceptionally low tax rate due to the reversal of a provision. Management pointed out that until the Fall of 2006, the group was on track to report better than flat earnings but that 4Q06 results turned out to be worse than expected.

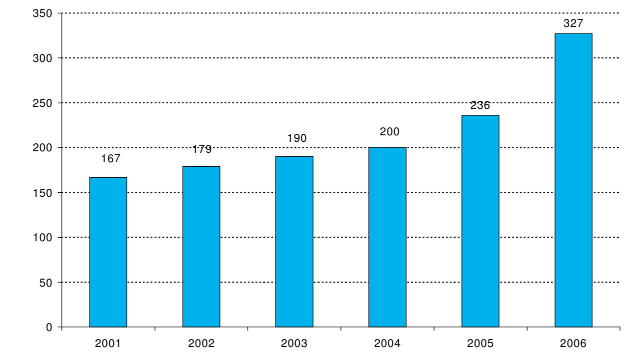
Ter Beke

€ m	1H05	2H05	FY05	1H06	2H06	FY06
Sales	115.5	120.7	236.2	149.3	177.4	326.7
% growth	15.6%	20.6%	18.1%	29.2%	47.0%	38.3%
EBITDA	9.3	12.3	21.6	11.1	12.9	24.0
% of sales	8.0%	10.2%	9.2%	7.4%	7.3%	7.3%
EBIT	3.9	6.8	10.7	4.2	5.9	10.1
% of sales	3.4%	5.6%	4.5%	2.8%	3.3%	3.1%
Financial result	-0.6	-0.8	-1.4	-0.8	-1.6	-2.4
Pretax profit	3.3	6.0	9.3	3.4	4.3	7.7
Taxes	-1.2	-2.2	-3.4	-1.1	-0.7	-1.8
Tax rate	36.2%	36.3%	36.3%	31.1%	16.3%	22.8%
Net profits	2.1	3.8	5.9	2.3	3.6	6.0

Source: Ter Beke

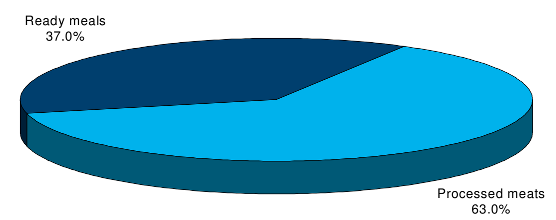
Sales rose by 38.3% to € 326.7m (our forecast: € 323.6m), thanks mainly to the merger with Pluma, which has been consolidated since 1 April 2006. Organic sales growth reached 8%.

Sales evolution (€ m)



Source: Ter Beke

Sales breakdown



Source: Ter Beke

We got a nasty surprise from the 140bp decline in the operating margin from 4.5% in 2005 to 3.1% in 2006. All the more since the FY06 margin was positively impacted by the reversal of a € 1.5m provision. If we exclude the impact of this reversal, the group's operating margin would have collapsed to 2.6% in FY06. Operating profits declined from € 10.7m to € 10.1m (our forecast: € 10.8m).

The decline in operating margin is due to:

- Higher energy and raw material prices especially in 3Q06;
- Integration costs related to Pluma;
- Costs related to the legal separation of the two business lines;
- Low margin contracts (ready meals) in France;
- Production inefficiencies in Alby-sur-Chéran (ready meals) as a result of strong volume growth;
- Extra expenses to increase the technical reliability of the factory in Wanze (ready meals).

The net financial charge rose by € 1m to € 2.4m, mainly due to the Pluma merger. The cash portion of the deal was financed through external debt. The tax rate fell from 36.3% to 22.8% as a result of the realisation of previously unrecognised deferred tax claims, the positive impact of notional interest deduction and a lowered tax rate in the Netherlands. Net profits were almost flat at € 5.97m.

The group's net debt rose from € 28.9m in 2005 to € 56.5m in 2006. Gearing was 79% at the end of 2006 and capex for the year amounted to € 16.7m. Investment projects included:

- New slicing and packaging lines for processed meats;
- The renovation of the maturing and drying facilities in Waarschoot;
- Installation of cooling systems that comply with new regulations;
- Further automation of the production lines for ready meals at Wanze and Marche-en-Famenne;
- Additional capacity in ready meals production.

The board will propose a flat DPS of € 2.10 for FY06. As the number of outstanding shares has risen by 25.9% following the merger with Pluma, the dividend payment should rise from € 2.87m for 2005 to € 3.62m for 2006.

Processed meats

FY06 sales rose by 58.5% to € 206.1m on the back of the merger with Pluma and 3.7% organic sales growth. Top-line growth of sliced and packaged products more than offset the continuing decline in over-the-counter products. Costs related to the integration of Pluma had an adverse impact on margins. Operating profits rose from € 8.2m in 2005 to € 9.8m in 2006 but the operating margin declined sharply from 6.33% in 2006 to 4.78% in 2006, despite the reversal of a € 1.5m provision related to a claim from SDF after Pluma terminated a contract. SDF has been active for more than two decades in the sale and distribution of chilled foods to the English retail sector. The company has been acting for several years as Pluma's agent in the UK. Without the reversal of the provision, the operating margin would have collapsed to 4.1%.

The integration of Pluma's and Ter Beke's processed meat activities is proceeding according to plan.

Earlier this year the group announced the acquisition of the above-mentioned SDF Foods Ltd for +/- € 2.7m, with the aim of developing Ter Beke's commercial activities in the UK. Ter Beke-Pluma is SDF's main client. We therefore do not expect the acquisition to have a significant impact on the group's top line. It is not yet clear whether the other clients (e.g. processed meat producers) will continue their distribution contracts with SDF, whose management will be replaced. Note that the UK is an important market for Ter Beke, on which the group has 50% of the market for continental pâté.

Ready meals

Ter Beke continues to invest heavily in the Come a Casa brand to gain market share both in France and Belgium. In France, Ter Beke opted for in-store promotional campaigns rather than nationwide campaigns. This strategy proved to be effective as it led to new introductions and strong volume growth. Divisional sales rose by 13.5% to € 120.6m in 2006. Ter Beke realized solid sales growth both in private label products and Come a Casa, although operating profit declined sharply from € 5.0m in 2005 to € 3.7m in 2006. During 4Q06, sales climbed sharply in France as a result of Ter Beke's efforts to gain market share. The resulting steep rise in volumes led to considerable inefficiencies at the production site of Alby-sur-Chéran and poor service levels. For example, temporary workers had to be employed to cope with the surge in orders. Some large orders were poorly priced however. This also contributed to margin pressure in 4Q06.

Ter Beke might acquire Normandie Plats Cuisinés (NPC), a French manufacturer of fresh pasta meals for the food retail and out-of-home market. The company was created in 2002 and produces private label products. Clients include food retailers (60% of sales) such as Champion, Carrefour and Auchan and out-of-home sector clients such as Sodexho. Last year, production was transferred to a brand new factory located in Falaise (Calvados). The French market represents 80% of sales. The factory has a surface of 7,000 m^2 and is located on a 3-hectare site which offers further expansion possibilities. The construction of the factory was financed by the regional authorities in an effort to create employment following the closure of a Moulinex plant. NPC has an option to acquire the building at a significant discount. An article in "Les Echos" mentioned that € 10m has been invested in the factory (€ 6m for the building and € 4m for the equipment). The production facility has a capacity of 12,000 tonnes and capacity utilisation stands at 30-40%. NPC uses the same technology as Ter Beke's factory in Wanze. Last year NPC realized a turnover of about € 12m in 2006 with a headcount of 100. The acquisition of NPC would fit perfectly with Ter Beke's Fresh Meals division given the group's aim to increase its market share in France. Furthermore, NPC has excess capacity while Ter Beke's production facilities are operating at close to full capacity. Without this acquisition, Ter Beke would have to build a new plant next year. An exclusive purchase option agreement has been signed and due diligence should be finalized during the course of 2Q07. We have not yet included NPC in our forecasts.

Outlook

Management has not yet provided concrete guidance for FY07 but indicated there will be a focus on improving profitability. Even though raw material prices have eased during 4Q06 and 1Q07, we are cautious about the margin outlook for FY07 because of costs related to:

- The potential acquisition of NPC;
- The establishment of two separate management committees;
- The reallocation/optimisation of production between sites;
- Increased sales efforts to promote Come a Casa.

Forecasts per division					
€ m	2005	2006	2007E	2008E	2009E
Sales					
Processed meats	130.06	206.11	237.30	244.42	251.75
Ready meals	106.18	120.60	126.63	132.97	139.61
Total	**236.24**	**326.72**	**369.93**	**377.38**	**391.36**
Sales growth %					
Processed meats	35.7%	58.5%	15.1%	3.0%	3.0%
Ready meals	1.9%	13.6%	5.0%	5.0%	5.0%
Total	**18.1%**	**38.3%**	**11.4%**	**3.7%**	**3.7%**
EBIT					
Processed meats	8.24	9.85	10.68	11.98	13.34
Ready meals	5.02	3.70	5.07	5.58	6.28
Unallocated costs	-2.56	-3.44	-3.00	-3.00	-3.00
Total	**10.70**	**10.11**	**12.74**	**14.56**	**16.63**
EBIT margin					
Processed meats	6.33%	4.78%	4.50%	4.90%	5.30%
Ready meals	4.73%	3.07%	4.00%	4.20%	4.50%
Total	**4.53%**	**3.09%**	**3.50%**	**3.86%**	**4.25%**

Source: Ter Beke, KBC Securities

The previous table shows our sales and operating margin assumptions for 2007-2009. Our FY07 sales forecast for Processed Meats is based on 3% organic growth and the full year contribution of Pluma. We assume that top line growth of Ready Meals will slow down this year because of increased focus on profitability. A close look will be taken at the large and poorly priced contracts in France and some might be terminated if Ter Beke fails to obtain better prices from retailers. Furthermore, following the surge in volumes in France during 4Q06, spare capacity has become limited. Note that our forecasts do not include the potential acquisition of NPC.

The reported operating margin of Processed Meats reached 4.78% in 2006. If we exclude the reversal of the above-mentioned provision, we arrive at an underlying operating margin of 4.05%. We are assuming 4.5% for 2007 on the back of management's increased focus on profitability. Ter Beke's net financial charge rose from € 0.8m in 1H06 to € 1.57m as a result of the Pluma merger. We are assuming € 3.1m for FY07 and have lowered our tax rate estimate from 34% to 32%. **Our EPS forecast has been lowered respectively 9% and 6% for 2007 and 2008.**

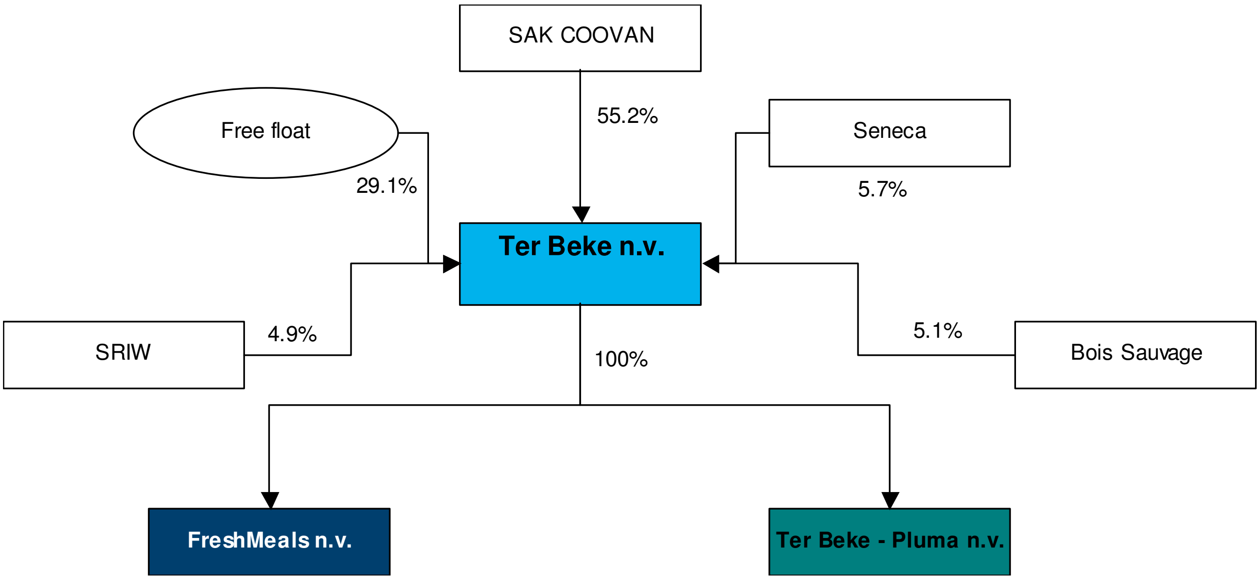
Ter Beke							
€ m	2005	2006	2007E Old	2007E New	2008E Old	2008E New	2009E
Sales	236.2	326.7	355.1	363.9	367.5	377.4	391.4
EBITDA	21.6	24.0	29.5	29.5	31.6	31.9	34.6
EBITDA margin	9.2%	7.3%	8.3%	8.1%	8.6%	8.5%	8.8%
Operating profits	10.7	10.1	13.1	12.7	14.7	14.6	16.6
Operating margin	4.5%	3.1%	3.7%	3.5%	4.0%	3.9%	4.2%
Financial result	-1.4	-2.4	-2.3	-3.1	-2.2	-3.2	-3.0
Pretax result	9.3	7.7	10.8	9.6	12.5	11.4	13.6
Taxes	-3.4	-1.8	-3.7	-3.1	-4.3	-3.6	-4.4
Tax rate	36.3%	22.8%	34.0%	32.0%	34.0%	32.0%	32.0%
Net profits	6.0	6.0	7.2	6.5	8.2	7.7	9.3
Avg number shares	1,366,698	1,588,088	1,719,371	1,722,971	1,719,371	1,722,971	1,722,971
EPS (€)	4.35	3.76	4.16	3.79	4.79	4.49	5.38

Source: Ter Beke, KBC Securities

Strategy

The group's structure has been adjusted to prepare both divisions for further external growth. Separate legal entities (Ter Beke-Pluma n.v. and Fresh Meals n.v.) and management committees have been set up for both divisions. Each management committee consists of a commercial, operating, financial and HR manager. This led to higher costs in 2006. Note that there is also an executive committee at the group level. A further rise in costs is expected for 2007 as additional staff are hired for the divisional management committees. This split has led to a duplication of certain functions but management is confident that the benefits will outweigh the costs. The separation of the two business lines will facilitate external growth. If a major merger or acquisition were to take place in the future, it would probably take place through Ter Beke-Pluma n.v. or Fresh Meals n.v. rather than the parent company (Ter Beke n.v.), which would avoid dilution of Ter Beke's controlling shareholders.

Ter Beke's corporate and shareholder structure



Source: KBC Securities

Financial data

Income statement (€ m)	2004	2005	2006	2007E	2008E	2009E
Sales	200.0	236.2	326.7	363.9	377.4	391.4
Gross profit	110.5	122.2	166.6	178.3	184.9	191.8
EBIT	10.2	10.7	10.1	12.7	14.6	16.6
Pre-tax earnings	9.4	9.3	7.7	9.6	11.4	13.6
Net earnings	5.0	5.9	6.0	6.5	7.7	9.3
EBITDA	20.9	21.6	24.0	29.5	31.9	34.6
REBITDA	20.9	21.6	24.0	29.5	31.9	34.6
REBITA	11.9	10.7	10.1	12.7	14.6	16.6

Balance sheet (€ m)	2004	2005	2006	2007E	2008E	2009E
Intangible assets	12.6	20.1	28.2	28.4	28.7	29.0
Tangible assets	52.6	61.5	103.2	103.1	103.5	104.2
Financial assets	0.0	0.1	0.1	0.1	0.1	0.1
Net other assets & liabilities	1.3	2.1	3.1	3.1	3.1	3.1
Net working capital	0.1	4.4	15.4	15.4	16.0	16.6
Net debt	13.7	28.9	56.5	53.8	51.0	47.1
Provisions	11.9	14.0	21.7	21.7	21.7	21.7
Minorities	-	-	-	-	-	-
Equity	41.1	45.4	71.7	74.6	78.7	84.1
Capital employed	66.6	88.1	149.7	150.1	151.3	152.9
TOTAL ASSETS	111.9	134.4	208.2	209.4	212.7	216.4

Cash flow statement (€ m)	2004	2005	2006	2007E	2008E	2009E
Cash flow from operations	13.2	12.1	12.6	23.2	24.5	26.7
Net capital expenditure	-17.3	-12.9	-16.7	-17.0	-18.0	-19.0
Free cash-flow	-4.1	-0.8	-4.1	6.2	6.5	7.7
Acquisitions / disposals	0.0	-11.6	-6.0	0.0	0.0	0.0
Dividend payments	-1.6	-1.8	-2.9	-3.6	-3.7	-3.8
Shares issues	0.0	0.2	0.0	0.0	0.0	0.0
New borrowings / reimbursements	6.9	13.8	13.1	-2.6	-2.8	-3.9
Other	-0.1	-0.1	0.0	0.0	0.0	0.0
CHANGE IN CASH & EQUIVALENTS	1.1	-0.3	0.1	0.0	0.0	0.0

Performance criteria	2004	2005	2006	2007E	2008E	2009E
Sales growth	-	18.1%	38.3%	11.4%	3.7%	3.7%
Gross margin	55.3%	51.7%	51.0%	49.0%	49.0%	49.0%
REBITDA margin	10.4%	9.2%	7.3%	8.1%	8.5%	8.8%
REBITA margin	6.0%	4.5%	3.1%	3.5%	3.9%	4.2%
EBIT margin	5.1%	4.5%	3.1%	3.5%	3.9%	4.2%
Net debt / Equity + Minorities	33.3%	63.6%	78.7%	72.1%	64.9%	56.0%
Net debt / EBITDA	0.65	1.33	2.35	1.83	1.60	1.36
EBITDA / net interest	25.45	15.82	10.12	9.42	9.99	11.56
Pay-out ratio	36.3%	48.3%	60.6%	56.7%	49.0%	41.8%
= Return on Equity (avg)	-	13.8%	10.2%	8.9%	10.1%	11.4%
Return on Capital Employed (avg)	-	8.8%	6.6%	5.8%	6.6%	7.4%

Per share data (€)	2004	2005	2006	2007E	2008E	2009E
weighted average # shares, diluted	1,401,979	1,401,840	1,615,210	1,750,093	1,750,093	1,750,093
Basic EPS	5.32	4.35	3.76	3.79	4.49	5.38
Diluted EPS	3.59	4.24	3.70	3.74	4.42	5.30
Diluted, adjusted EPS	4.84	4.24	3.70	3.74	4.42	5.30
Net book value / share	30.15	33.16	41.65	43.35	45.68	48.86
Free cash flow / share	-4.37	-0.58	-2.57	3.62	3.78	4.46
Dividend	2.00	2.10	2.10	2.15	2.20	2.25

Valuation data	2004	2005	2006	2007E	2008E	2009E
Reference share price (€)	57.44	66.30	65.59	67.80	67.80	67.80
Reference market capitalisation	78.3	90.8	113.0	116.8	116.8	116.8
Enterprise value (€ m)	102.3	131.9	189.4	190.6	187.8	183.9
P/E	11.9	15.6	17.7	18.2	15.4	12.8
EV/sales	0.6	0.6	0.6	0.5	0.5	0.5
EV/EBITDA	5.6	6.2	8.1	6.5	5.9	5.3
EV/Capital employed	1.8	1.5	1.3	1.3	1.2	1.2
P/ NBV	2.3	2.0	1.6	1.6	1.5	1.4
Free cash flow yield	-4.5%	-0.8%	-3.5%	5.3%	5.6%	6.6%
Dividend yield	2.9%	3.1%	3.1%	3.2%	3.2%	3.3%

Source: KBC Securities

*Historic valuation data are based on historic prices

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Disclosure & Disclaimers section

The company disclosures can also be consulted on our website http://www.kbcsecurities.be/disclosures.

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Stock rating	Definition
BUY	Expected total return (including dividends) of 10% or more over a 6-month period
ACCUMULATE	Expected total return (including dividends) between 0% and 10% over a 6-month period
REDUCE	Expected total return (including dividends) between –10% and 0% over a 6-month period
SELL	Expected total return (including dividends) of -10% or worse over a 6-month period

Due to external factors and in exceptional cases, KBC Securities allows the use of ratings such as Accept the Offer, Black Out, No Recommendation or Suspended.
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Stock rating	% of covered universe	% of covered universe with investment banking relationship during last year
BUY	36.70%	75.00%
ACCUMULATE	45.30%	25.00%
REDUCE	15.80%	0.00%
SELL	2.20%	0.00%

Ter Beke is specialized in chilled ready meals and processed meats. It is the European market leader in chilled lasagna.
The price target for Ter Beke is based on following parameters: Discounted Cash Flow (DCF)
The risks which may impede the achievement of our price target are: Food scares. Increasingly stringent health regulation. Price pressure from retailers.
Any reference made to a DCF valuation for Ter Beke is based on the following parameters: a forecast period from 2007 until 2014, a perpetual growth rate of 1% and a calculated WACC of 6.8%.

Below is an overview of the stock ratings and target price history in the last 12 months for the stock described in this report.

Date	Rating	Target price
21-SEP-06	Accumulate	€ 71.00
27-APR-06	Buy	€ 80.00

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