CREDO WEALTH

Bunge beginning to budge

Getting food from the farm to our plates is complicated but agribusinesses try to simplify the process. Bunge's operations include agricultural commodity trading, storage, transportation, processing, packaging and distribution. These are all capital intensive and difficult to break into. This doesn't mean there aren't market pressures for those who are already in it to perform on behalf of shareholders. However, it does mean that competitors are less likely to replicate assets. They generally buy market share rather than build it.

Bunge is the smallest of the big 4 "ABCD" global players (along with Archer Daniels, Cargill, and Dreyfus). Due to the structure of the market, economies of scale, and network effects, there tends to be regional dominance amongst large players. Relative to peers, Bunge is differentiated by its outsized exposure to Brazil and to soybeans; whereas Archer Daniels has relatively more exposure to the United States and to corn.

Dominance doesn't automatically mean good times. It simply provides an opportunity. On paper, Brazil is one of the largest, and fastest growing, agricultural economies. Bunge's unique position should enable the company to benefit over the long term. Despite this, earnings have disappointed this year, and the share price has significantly underperformed peers. Trucker strikes in Brazil weighed and Chinese tariffs on US Soybeans have dampened sentiment. The truckers strike is now over and the Chinese recently resumed buying US soybeans.

Unsurprisingly, underperformance in an industry where the physical capital is still attractive leads to increasing outside interest. Activist investors start pressuring shareholders and management, and competitors get their wallets out. Bunge has reportedly been approached, and has rebuffed, two prospective buyers in the last two years (Glencore and Archer Daniels). There are significant regional, product and scale synergies available for a prospective buyer.

Despite sustained resistance and continued pressure, management has recently given some ground. After another profit warning, several new board members have been added and an "all options" strategic review has started. It is being chaired by Paul Fribourg from Continental Grains. The Fribourg family are one of the few successful dynasties to have dominated the agribusiness since the 1800s. Having sold their grain unit to Cargill in 1999, the Fribourgs have since been involved in some of the most prominent mergers in the industry.

Whilst a sale is not guaranteed, the underperformance has meant we were given the opportunity to buy a share of the underlying assets at a cheap price. We believe the changes already made by management, and those that will take place even if there isn't a sale, provide downside protection. Meanwhile, if the company, or even parts of the company, are sold that will provide us with upside. Like spinning a coin where heads you win, and tails you don't lose. Old school tangible assets provide a significant margin of safety.

Since we purchased the stock, Bunge has announced the departure of the CEO, Soren Schroder. This removes another hurdle to talks with would be buyers. At roughly half the market capitalisation as it was 10 years ago, the Company has said they are open to reengaging in discussions with Glencore and Archer Daniels.

We don't know what will happen. We know something will happen. Having done our homework, we watch with interest, and calm confidence.

Important notice