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Lutetia Capital Bets Tiffany, Mead Johnson Are M&A Targets

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Merger-arbitrage and event-driven hedge-fund manager Lutetia Capital SAS is betting that quality consumer stables such as Tiffany & Co. (TIF) and Mead Johnson Nutrition Co. (MJN) will be acquisition targets in the current wave of M&A activities.

"Big food producers like Danone SA (BN.FR, DANOY) and Nestle SA (NESN.VX, NSRGY) are investing in healthy food and aggressively expanding into emerging markets," said Lutetia Capital's portfolio manager, Fabrice Seiman. "Mead Johnson is an attractive target as it has a huge emerging-market presence-- emerging markets account for 60% of its turnover--and is well positioned in the attractive baby-food segment."

He added that Tiffany's global retail network would be an invaluable asset.

The manager's event-driven fund Lutetia Patrimoine has been building up positions in both Tiffany and Mead Johnson in anticipation of bids for them. Shares of Tiffany are up 11% year to date; shares of Mead Johnson are up 28.7%.

Well-known consumer brands have been drawing strong acquisition interests from private-equity firms because they are cash generators and have a good chance of riding out further economic turmoils. Sara Lee Corp. (SLE) declined an offer from buyout firm KKR & Co. (KKR) last month, The Wall Street Journal reported Tuesday. And the sale process of children's clothing retailer Gymboree Corp. (GYMB) has attracted five major private-equity firms, including Apollo Management LP, Bain Capital LLC and KKR, the New York Post said Tuesday.

Seiman said he expects cash-flush corporations would soon join the fray.

"Companies now are awash with cash. U.S. companies' cash reserves stand at $3 trillion--the highest level since the 1960s. The only three ways of deploying that cash are issuing dividends, doing share buybacks and pursuing buyout opportunities," he said.

Lutetia Patrimoine fund, relatively small at $52 million, has had a stable track record since its inception in December 2009. In September, it posted a 1.5% gain, bringing the year-to-date return to 5.5%, according to an investor letter.

On top of buying shares in announced acquisition targets as do other merger arbitrage funds, Lutetia also seeks to make gains by identifying potential targets in the market.

"Three percent or 15 out of the 500 S&P companies are acquired in any given year. Our goal is to optimize our hit rate by focusing on the most active sectors in terms of M&A and, in those sectors, identifying the most accretive targets for potential buyers," Seiman said. "Right now, we are focused on the technology, health care, energy and consumer sectors."

Identifying potential buyers and sellers was what Lutetia's two portfolio managers did at their previous jobs. Lead portfolio manager Jean-Francois Comte was a former vice president of M&A with boutique investment bank Lazard Freres. Seiman was a member of the $8 billion pan-European private-equity firm PAI Partners' investment committee and an advisor to the French government.

"We are basically doing the same thing and using the same tools as when we were investment bankers," Seiman said.

The fund profited handsomely from Oracle Corp.'s (ORCL) acquisition of Sun Microsystems Inc. (JAVA), completed in January, buying when the market expected the deal to fall through.

"The share price of Sun Microsystems plunged to $8.10 from $9.30 as the European Commission held an antitrust investigation into Oracle's acquisition. But upon detailed study of the technicalities of the matter, we found out that the issue would be dismissed sooner or later," Seiman said. Lutetia bought at $ 8.10 and the deal was completed at $9.50 a share. Lutetia also correctly tipped French defense-electronics maker Safran SA's (SAF.FR) acquisition of L-1 Identity Solutions Inc. (ID) in September for $12 a share. Investment in L-1 was Lutetia's largest position in August, accounting for 7.9% of its portfolio.

The manager still has positions in Cogent Inc. (COGT) on expectations of a bid increase either from 3M Co. (MMM) or NEC Corp. (NIPNF, 6701.TO) and in Genzyme Corp. (GENZ), believing French health-care giant Sanofi-Aventis S.A. (SNY, SAN.FR) may come back with a bid of more than $75 a share. Genzyme launched a hostile bid for Sanofi-Aventis Monday, but kept the offer at $69 a share.

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