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Nutritional riches

Area firm hopes to profit on rice bran

By Jim Wasserman -- Bee Staff Writer

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The beverage is a pale tan color, sweet and tasty like a vanilla milkshake. Rice bran products such as this nutrition drink are how El Dorado Hills-based NutraCea aims to help feed the world's hungry - and earn millions for its shareholders.

For five years the small public company has touted its agricultural innovation that uses the most nourishing part of a rice kernel, but it's never made a profit. After a corporate merger that became final last week, NutraCea officers now think it's positioned for a serious role in the business of food.

NutraCea and RiceX Co., two El Dorado Hills firms that jointly developed how to stop rice bran from going rancid after milling, have combined intellectual property and become one company. Operating now as NutraCea, the company is marketing a product typically worth pennies per pound - as a waste product or animal feed - for dollars per pound as a human nutritional supplement.

The bran coating, removed to make the white rice that's most widely eaten globally, makes up 8 percent of the rice kernel but accounts for 65 percent of its nutritional value.

More than half the world depends on rice, but 60 million metric tons of rice bran are discarded annually, NutraCea officials say.

"We take stuff that's thrown away and turn it into food that's more nutritious than the rice they're eating right now," says Bradley D. Edson, appointed president of the company in December and named chief executive officer on Tuesday. "We are the only company in the world that has that."

NutraCea is primarily focused on developing countries and wants to be known for "really making a significant impact on ending world hunger," says Senior Vice President Margie Adelman.

In September, NutraCea announced a \$21.6 million deal with the Dominican Republic's largest rice mill to supply rice bran drink to thousands of Dominican schoolchildren through a government feeding program. Company executives say the product, not yet commercially available in the United States, could bring in as much as \$2 million a month for NutraCea in three to four years. The firm is exploring a similar deal in Panama.

"Our goal is to replicate that model. There are many companies throughout the world, several dozen, that have potential to (partner with us)," says Edson, 46, the former CEO of Phoenix-based Vital Living Inc., which develops and licenses nutritional supplements.

NutraCea's nutritional drink, made in flavors ranging from cinnamon and vanilla to chocolate and grape, has already proven itself in pilot projects run by international aid groups in Guatemala and El Salvador, says Ike Lynch, a former H.J. Heinz Co. executive who's now NutraCea's chief operating officer.

The newly merged company also wants to expand domestic licensing revenue from its raw rice bran product and intellectual properties. Already, some companies buy stabilized rice bran from NutraCea and market products that contain it under their own names.

In August, NutraCea signed a \$2 million sales deal with Massachusetts infomercial maker ITV Global Inc. The firm runs 30-minute television commercials selling two of NutraCea's 20 products.

Most recently, NutraCea announced its bran products were being added to anti-diarrhea formulas at Folsom's Mercy Hospital.

Edson foresees more licensing revenue from food and pharmaceutical companies looking to distinguish their products by adding stabilized rice bran. Retail chains also could distribute their own products.

"We have tens of millions of dollars in research and development that's been put in over the last number of years to create numerous patents and formulation products," he said. "We feel corporately we're better positioned to align ourselves as a partner to companies with more money, better distribution and with existing products they may want to enhance using our proprietary technology."

Edson begins his new CEO stint with a NutraCea that is recapitalized and debt free for the first time. Last week the company sold \$7.8 million in convertible preferred stock to several mid-to large-size private investment funds. The names will be disclosed soon in SEC filings, says Edson.

"We have been appropriately capitalized and now have the opportunity, through both international feeding programs and through domestic licensing deals and partnerships, for a huge ramp up in growth," he says.

The company's stock closed Friday at 89 cents a share over the counter, down 11 cents, or 11 percent. The stock has fallen 14 cents a share since the merger became final Tuesday. NutraCea has traded between 30 cents and \$1.81 over the past 52 weeks.

The merger came after nearly a quarter-century of product research on a patented manufacturing process called rice stabilization. The work, initially conducted with the U.S. Department of Agriculture, resulted in a way to deactivate a lipase protein that causes rice bran to become rancid after it's milled from the kernel. The technology, launched at a Farmers' Rice Cooperative mill in West Sacramento and a NutraCea mill in Dillon, Mont., gives rice bran a shelf life of up to two years, the company says.

The process does not involve genetically modified organisms.

"It's just concentrated brown rice. That's what it is," says Patricia McPeak, 65, who created the process with her husband, Daniel, a former Lockheed Martin Corp. engineer.

On a recent tour of the company's milling operation in West Sacramento, she boasted of the bran product's health benefits and called it "the next Microsoft of the food world."

McPeak, who stepped down as NutraCea CEO Tuesday but remains a director and major shareholder, says stabilized rice bran can slow degenerative conditions like diabetes and heart disease and will eventually compete with pharmaceutical products.

"I think we are really going to become a pharmaceutical-sized nutraceutical company," she said after the merger last week.

So far, there's little science on stabilized rice bran, says Dr. Betti Burri, research chemist with the U.S. Department of Agriculture's Western Human Nutrition Center.

"I think the generally recognized thinking is that it does have possibilities," says the University of California, Davis, professor. "There have been some studies that suggest cholesterol lowering, and that's probably the strongest issue. There's not a whole lot of science on it, but not a whole lot against it, either. In general, what little research there is is positive."

At Farmers' Rice Cooperative in West Sacramento, spokesman Bill Huffman says Sacramento Valley rice growers may benefit if NutraCea's business plan succeeds. "As the market develops for various products that can be made with rice bran, that, of course, will increase the value of the raw bran back to us," he says.

Few analysts have weighed in on the company's future. El Dorado Hills-based Dutton Associates gave NutraCea a one-year target price of \$1.80 per share, with analyst Gerald LaKarnafeaux saying a new post-merger report coming this month could upgrade his July rating of "strong speculative buy."

LaKarnafeaux has expressed long-term confidence in NutraCea despite its "protracted" development stage which has included \$70 million in combined startup costs with RiceX, losses and management turnover common to startups.

NutraCea reported losses of \$2.6 million in the first six months of 2005; RiceX reported six-month losses of \$1.2 million.

NutraCea reported \$5.5 million in revenue between the two companies for the fiscal year ending June 30 but declined to offer estimates for the new year.

Edson and LaKarnafeaux both call it a credit to the founders that the companies survived to merge.

LaKarnafeaux, citing Edson's experience, new medical advisers and ability to raise cash says the company is "permanently" beyond development stage.

"Over the past year there's been some pretty impressive progress with marketing initiatives," he says, "but the bulk of the story is the international opportunities they have. It's great to feed schoolkids, but it's also great to feed the schoolkids and make a lot of money at the same time."

STABILIZED RICE BRAN

Rice bran is the portion of the rice kernel that lies beneath the hull and over the white rice. Though it contains 65 percent of the rice kernel's nutritional value, it is removed by a milling process to make white rice. The milling process causes the bran to quickly become rancid. NutraCea owns a proprietary manufacturing method to deactivate the lipase protein that causes rancidity and keep the product stable for up to three years. The process is carried out at Farmers Rice Co-op mill in West Sacramento and the company's processing facility in Dillon, Mont.

NUTRACEA AT A GLANCE

President and CEO: Bradley Edson, former president and CEO of Vital Living Inc.

Chief operating officer: Ike Lynch, former RiceX CEO.

Chief financial officer: Todd Crow, former RiceX CFO.

Senior vice president, corporate secretary: Margie Adelman, former president of TransMedia Group and Adelman Communications.

Employees: 30.

Products: Powdered and capsule-form nutritional products made from stabilized rice bran; rice bran cooking oil.

Deals: \$21.6 million agreement with Dominican Republic's largest rice mill to supply nutritional drink to 200,000 schoolchildren daily and to as many as 800,000 children within several years. Talks in progress with Panamanian rice mills for a similar deal.

Trading symbol: Trades as NTRZ.OB over the counter.

Share price: Closed at 89 cents on Friday, down 11 cents. Range: \$0.30-\$1.81.

Sources: NutraCea, Yahoo Finance

NUTRACEA THROUGH THE YEARS

NutraCea's merger with RiceX is the latest development in a 24-year effort to profitably produce nutritional products from stabilized rice bran:

1981: Patricia Mayhew and the U.S. Department of Agriculture team up to stabilize rice bran. Mayhew forms Torrance-based Brady International and begins developing a stabilizing machine with Daniel McPeak, a former Lockheed Martin Corp. engineer.

1989: Investors assume control from the two, who found El Dorado Hills-based Food Extrusion Inc. to compete with Brady.

1990: Food Extrusion Inc. stabilizes its first rice bran.

1992: Brady goes out of business. Mayhew and McPeak marry.

1997: Food Extrusion Inc. buys Montana specialty foods processor Centennial Foods Inc. Agribusiness giant Monsanto Co. invests \$5 million with plans to market rice bran oil globally. Investors hire new CEO to replace Daniel McPeak. Patricia McPeak remains president.

1998: Food Extrusion Inc. reincorporates in Delaware as RiceX Co. and begins trading shares over the counter.

2000: Patricia McPeak leaves to found NutraStar Inc., formed to market nutraceutical products and vitamin supplements made from RiceX's stabilized rice bran.

2001: NutraStar completes reverse merger into the shell of formerly bankrupt Alliance Consumer International LLC and begins trading publicly. RiceX completes pilot project to supply nutritional rice bran drink to Guatemalan children. NutraStar enters 15-year agreement with RiceX to be sole U.S. distributor of stabilized rice bran products.

2002: RiceX terminates agreement when NutraStar doesn't meet sales targets.

2003: NutraStar begins trading over the counter as NutraCea.

2005: NutraCea and RiceX agree to merge, effective Oct. 4, with the new company to be known as NutraCea.

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