



Industry Outlook

Consumer Staples



ITIC

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Summary



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The consumer staples sector encompasses many of the different everyday necessities that are used by consumers daily. This category includes hygiene products, food, beverages, hypermarkets, tobacco, alcohol, and retail medical drugs.

This sector is non-cyclical because the products in this space are always in demand at a rather constant level, regardless of one's personal financial situation or the economic situation, causing this industry to have very low-price elasticity of demand. This therefore allows for many companies within this industry to be stock picks for a portfolio due the stability and over time growth they provide.

In this industry outlook, we aim to provide a balanced evaluation of this ever-growing industry which may have much potential for further upside even with the ongoing pandemic.

Environmental Analysis



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Political

Regarding the political aspect, some factors influence companies' performance. One of them is the rising government support for e-commerce. Nowadays, with the evolution of technology, is it easier for companies to implement new ways of commerce, and in this industry that is essential. Therefore, the support of governments for companies to promote online commerce will contribute to their success.

Another important aspect in the consumer goods industry is the quality of commercialized products. In Europe, the Consumer Sales and Guarantees Directive was created to establish the legal guarantee for consumer goods and to regulate commercial guarantees, being responsible to guarantee that the goods conform with the contract.

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Economical

Nowadays, economic growth is a reality, and it shows that more and more companies are having success and good results. This is a very important factor for the consumer staples industry because it gives new opportunities for companies to innovate and develop new products. Furthermore, the majority of the developed markets are stable, giving also space to free competition and growth opportunities.

Despite that, due to the pandemic situation, the unemployment rate increased all over the world. This means that consumers will search for cheaper options instead of buying expensive consumer products. With that in mind, companies should adapt their strategy and try to understand their target.

Social

With the current pandemic situation and the online work and classes, consumers are spending more time at home. This is a positive aspect for companies of this industry, as clients are buying more food and drinks to consume at home rather than going out for lunch or dinner. Apart from that, consumers are demanding new healthier products, giving consumer staples companies space to promote new habits and develop new products.

Besides that, in developed countries the population is declining, while in countries like China and India the population growth rate is very high. With that in mind, it is expected to increase the volume of consumer goods bought in developing countries and decrease the ones bought in developed countries.

Technological

The industrial revolution completely changed the way companies work in this market. While decades ago the production was mainly artisanal, currently companies produce in mass, reducing costs and being able to keep up with demand.

Another technological aspect that has an influence on consumer goods companies, is the evolution of technology because it created the possibility of online sales and online markets. Additionally, nowadays companies can transport their products to different countries and even produce their products outside their location.

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Legal

Regarding the legal factors, in this market companies must follow product safety regulations, in order to guarantee that the commercialized products are of quality and follow all established norms. In addition, it is also essential for companies to act in accordance with environmental protection regulations, so as not to cause pollution or waste of natural resources. Finally, companies must follow corporate sustainability regulations, so that the conduct of their workers inside and outside the organization is responsible and sustainable.

Environmental

As it was said before, the environmental factor is crucial in the consumer goods industry. While we have more and more consumers concerned about the environment and pollution phenomena, companies have a challenge resulting from climate change.

Currently, as a result of changes in climate, the agriculture cycles themselves have changed, thus impacting the final products. Moreover, with the overuse of certain natural resources, it has become more difficult or expensive to produce some products.

Despite this, new renewable resources have appeared today, which could be a bet for cleaner and more environmentally friendly production.

Industry Competitiveness



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Porter's 5 Forces

Threat of New Entrants

- **Weak Force**
- The industry presents several difficulties to the entry of new competitors, given the existence of large economies of scale. Thus, only with a large investment does the entry of a large competitor become possible.
- There is also a high customer loyalty to established brands, something that makes it substantially difficult for new entrants to win over consumers.

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Threat of New Substitutes

- **Moderately low competitive force**
- At Staples consumer industry, brands are successful when it comes to gaining a competitive advantage. In addition, since companies have a big structure and therefore a lot of financial power, some choose to add such substitute products to their portfolio.
- However, the threat, although small, exists, as there are some substitute products branded by the big retailers and therefore with a lower price, which leads to some consumers opting for these alternatives.

Bargain Power of Customers

- **Moderately highly competitive Force**
- There is a high power of consumers, as they are quite sensitive to price changes and there is also a lot of information available about the products, with consumers having the opportunity to make a conscious choice and evaluate the alternatives.
- However, given that the competition is high, the prices turn out to be very identical, which is why this competitive force is not strong.
- If we consider the customers as the big retailers, it can be said that they have a high power as there is a monopolization of the sector.

Bargain Power of Suppliers

- **Moderately low competitive force**
- In the consumer Staples, there are numerous suppliers and having the big multinational competitors of the industry, their production in various locations in the world, the power of suppliers is diminished.
- However, they have some power to the extent that the degree of involvement with suppliers is already quite massive, with the change to the new one being expensive and having serious difficulties to restructure the new system.

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Competitive rivalry within industry

- **Strong Force**
- This is a force to take in account in Staples consumer industry, since there is a very fierce competition, characteristic of aggressiveness in price strategy. The fact that customers can choose any company in the market with no switching costs, highlights the high competition.
- It is a several competitors industry, however it is a not very fragmented market, since large multinationals hold a significant portion of the industry in some regions due to high start-up costs. Competition exists but is among few companies.



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SWOT Analysis

<p>Strengths</p> <p>S1 – An Essential Sector</p> <p>S2 – High and Inelastic Demand</p> <p>S3 – Diverse and persistent products</p> <p>S4 – Economies of scale</p> <p>S5 – Efficient product distribution network</p> <p>S6 – High margins</p> <p>S7 – Consumer Defensive stocks</p>	<p>Weaknesses</p> <p>W1 – High environmental impact</p> <p>W2 – Imitable products</p> <p>W3 – Low and limited online presence</p> <p>W4 – Substitute products</p>
<p>Opportunities</p> <p>O1 – Growing industry</p> <p>O2 – Online present development and demand</p> <p>O4 – Growing concern with sustainability</p>	<p>Threats</p> <p>T1 – COVID-19 Recession</p> <p>T2 – Global and Local competition</p> <p>T3 – Increase in the value of taxes and fees in the industry</p> <p>T4 – Trade Barriers in some countries</p> <p>T5 – Decline of consumer spending</p> <p>T6 – Rapid evolution of Consumer demands</p>

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Crossed SWOT

S2 &O2 &T1:

Due to the pandemic, a large proportion of people worldwide search for home delivery options, not only for its ease, but also for its security. Companies have allied and have been increasing their online goods and delivery performance and despite the successful vaccine distribution and an improvement in global health, it is expected that the demand and use of this type of solutions will not decrease, as it increases more and more, taking into account the prosperity of consumers.

O3 &W1:

With the growing concern of consumers to environmental issues and for the quality of this, it becomes crucial that companies in this industry and not only, provide innovative and environmentally friendly options, from the creation process to the final product or service. Companies are increasingly committed to developing the types of options in their product diversity, decreasing their ecological footprint, in order to become more sustainable in the long term.

O2 & W3:

Nowadays, the need for brands of each company to bet on the communication channels of its products has been growing, using differentiated marketing in relation to its competitors. The investment in these strategies will result in greater awareness and loyalty of consumers towards the brand, promoting the realization and experiences as well the increase in market share.

The Big Players



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Procter & Gamble

Description

Procter & Gamble (P&G) is an American consumer staples company that focuses on a wide range of consumer goods. The company was founded in 1837 by William Procter and James Gamble, with the headquarters in Cincinnati, Ohio. P&G became publicly traded on the New York Stock Exchange in 1890 and is currently part of the Dow Jones Industrial Average and S&P 500.

Strategy

P&G has 65 individual brands which are organized into 10 product segments including fabric care, home care, baby care, feminine care, family care, grooming, oral care, personal health care, hair care, skin & personal care. The company aims on establishing superiority in their brands through their packaging, communication, and retail execution, while also focusing on innovation.

Financials

The company has a market cap of 337.88B and a current quarterly revenue of 18.109B. P&G has been on a steady rise over the past years in terms of revenue, growing more than 7% since 2017. Also, the company has a gross profit margin of 50.73% and a free cash flow margin of 18.95%, their Enterprise Value/EBITDA is 17.18.

P&G's ROA is currently 11.04% and is currently operating above the industry average of 3.03%. Their ROE is also very efficient, currently at 27.04, which is operating way above the industry average of 6.53.

In terms of liquidity, the latest quarterly data (Q3) show that the company had a current ratio of 0.71x and a quick ratio of 0.52. These ratios are both operating below the industry average which may indicate that P&G may be having troubles meeting its current obligations.

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The stock price (PG) has grown over 45% since the March 2020 crash and is currently priced at \$136.96 11/05/21. This year's stock high was made today with price touching 138.72 and its low was in early March with price touching \$120. Additionally, P&G current quarterly EPS is at \$1.26

Costco Wholesale Corporation

Description

Costco Wholesale Corporation is the fifth biggest retailer in the world with over 782 locations. This company is known for selling bulk quantities of consumer staple products at discounted prices to members who pay an annual membership fee. Costco is headquartered in Issaquah, Washington and was founded in 1976. The company went public in 1985 and is listed on the NASDAQ and is part of the S&P 500.

Strategy

Costco's main source of operating profit does not come from the goods they sell. Most of the products they sell are sold at a loss or just breakeven. Over 70% of the company's operating profit comes from their annual membership. The reason is because Costco sells these products at very competitive prices which the usual retailers cannot keep up with. This provides a good unique selling point for the company and is marketed as such, driving many customers to their store. With the use of a membership, brand loyalty is created which leads to Costco growing and expanding year after year. The membership comes with different packages with the price ranging as little as \$60 to \$120.

Financials

When looking at financials, the company's revenues have been on a steady increase annually. Revenues went from \$121,194,000 in 2017 to \$178,626,000 by the end of 2020, an increase of 47.3%. This continuous increase in revenues reflects that the demand for the company's services and products remain on a continual rise.

From the 2nd quarter of 2017 to the third quarter of 2019, the ROA was mainly roaming around 6.58%-8.42%, however, currently the ROA is currently operating at 7.81% which is

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above the industry average of 2.94%. The company's ROE mainly fluctuated from 22.40% to 25.80% throughout 2017 up until now. This ratio currently operates at 25.8% which is above the industry average of 8.23%. Both the ROA and ROE have increased when compared to previous years and both ratios continue to operate above their industry's mean.

In terms of liquidity, The company's current ratio has mainly fluctuated from 0.81-0.99 from 2017 up until now. Currently, the ratio is now operating below the industry average of 1.29. Also, the company currently has a quick ratio of 0.77, indicating that Costco has weak short term financial strength.

The debt to equity ratio (D/E) is currently at 0.47. Since 2018 this ratio has been fluctuating 0.54-0.30. The company's D/E currently is below the industry's average of .87.

The stock (COST) price has grown over 42% from the crash in March of 2020. Currently the price is at \$385.13 (10/05/2021), this year's stock high was \$385.13 today in the month of May and its low was \$311.25 in the month of March



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Philip Morris International

Description

Philip Morris International (PMI) is a swiss-American multinational producer of tobacco and derivatives, with products sold around the world and with a very significant workforce of 71,000 people.

The PMI is the leader of the tobacco industry and its best-seller product is Marlboro, however there are other famous brands within their portfolio, such as Chesterfield or L&M.

In March 2008, PMI spun off of Altria Group, being until that year, was an operating company of the multinational Altria, previously known as Philip Morris Companies, Inc. With a market cap of 152.83B, PMI is on the 107th ranking position in the Fortune 500 as of 2020, the list of the biggest companies in the world.

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Strategy

With the increasing sensitivity to the health hazards of tobacco, PMI is radically changing its strategy, replacing cigarettes with smoke-free products. The company, in 2017, PMI sold around 791 billion cigarettes and other tobacco products and 36 billion smoke-free products. As said by PMI, around 14 million adults have already stopped smoking due to these products.

PMI has developed several products of smoke-free products, which are mostly e-vapor products like the very known brand IQOS, a heated tobacco system. As stated by the company, "our business vision is to replace cigarettes with less harmful and non-smoking products as quickly as possible".

Financials

As far as PMI Revenue is concerned, it has remained steady, with \$29,625B in 2018 and \$29.80B in 2019, having had a slight drop in 2020, probably due to the pandemic, passing revenue to \$28,694B by 2020. It should be noted that in the first quarter of 2021 the PMI Revenue was 7.58B, which is equivalent to an increase of 6.04% compared to the same period of the previous year.

The ROA has grown, with 14.37% in the first quarter of 2018, and then increased substantially to 19.48% in the same period of 2019 and with a slight decrease in the first quarter of 2020 to 18.90%, supplanted by 21.18% of the same period in 2021. This increase is explained by the fact that the company's net income is rising and the decrease of assets.

For ROE it is negative, since the value of shareholders equity is negative. The same has decreased, as net income has increased over the years. In the first quarter of 2019 the ROE was -74.98%, in the same period of 2020, this was already -77.90% and lastly in 2021 with a more substantial decrease this consumption was -85.05%.

In terms of liquidity, from the analysis of the Current ratio, it is possible to verify that the PMI is below the tobacco industry, with a value of 1.10 in 2020 compared to 1.72 of the industry in the same year. However, you can see an increase in it for the first quarter of 2021,

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where the Current ratio is 1.18. The Quick ratio was 0.61 in 2020 and also it is below the industry, which had a value of 0.73. In the first quarter of 2021 the Quick ratio decreased to 0.58.

The D/E ratio has decreased slightly, with -2.27 in the first quarter of 2019, -2.26 in the same period in 2020 and -2.85 in 2021. This has been the case as long-term debt decreased between the periods under evaluation.

Finally, the Stock price was 97.41 on May 7th 2021, and this is the value of the Year to date high, while the value of the Year to Date low was the January 2nd with 78.01.

Conclusion



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Nowadays, the population increase is a reality. Countries like China and India are the example of places where the population grows at a very fast level. Thus, the consumer staples market has an opportunity.

In this way, this market, particularly characterized by high levels of competition and with great global players, has had marked growth. It is undeniable that this market is attractive and has several strengths. However, as a result of several global phenomena, it also presents different challenges.

On the one hand, consumer goods trading companies have very high levels of competition, and many times it is necessary to reduce costs to become more attractive. In addition, companies with less healthy goods, such as tobacco retailers, have been challenged to find new healthier solutions. On the other hand, with the recent concern with sustainability, companies in this sector have the opportunity to innovate and find new products or ways to produce more environmentally friendly.

Concluding, despite the pandemic and all the recent situations that affect this market, the market is stable and shows great growth potential for the future.

Consumer Staples Industry Outlook

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