

FMCG and Covid-19: Sector set for considerable change

It's clear that the coronavirus has changed the landscape for FMCG - in some ways permanently. However, despite its similarities, the impact has not been the same across its subsectors and through the supply chain.



Getty

"The lockdown has hit the economy hard and despite efforts by the government and Reserve Bank to mitigate the effects, ultimately only a medical solution is likely to provide lasting relief to consumers and businesses servicing those consumers," says Itumeleng Merafe, head of interest rate structuring, Investec Corporate & Institutional Banking.

The market for fast-moving consumer goods faces considerable changes – impacted by demand for consumer-packaged goods, changes in household spending, increase in e-commerce and frequency of shop visits. And while there can be no doubt that consumer staples have been affected, the picture has not been uniform across the FMCG universe.



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Not all made equal

Anthony Geard, food and beverage analyst at Investec pointed out that not all companies have been equally exposed to Covid-19 risks. In fact, some consumer staples businesses around the world have done relatively well.

“Some consumer goods are considered necessity products and thus do not react to slowdowns as much as products in other sectors. However, some companies are proving to be bulletproof. Companies like P&G, Kimberley Clark and Mondelez have done particularly well. However, it has not been the same for others in the sector where beverage and brewing companies, for example, have held up less well.”

Companies in the tourism, leisure and car rental industries, as well as sectors previously considered resilient, such as food services, have been hard hit by the lockdowns across countries. “The rand certainly has had its role to play here,” says Geard.

“Every consumer good in South Africa is either imported or is impacted by import prices in some way. For example, items such as tea or wheat were either imported or the local prices were set upfront according to the imported price. The much weaker rand therefore means higher input costs for many in the sector – costs that they have been unable to recoup. Therefore, we are likely to see some form of food inflation down the line.”

In terms of identifying winners and losers, Geard pointed out that businesses with a strong export component to their earnings, would likely benefit from the weaker rand going forward. But it's all about timing.



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Serena Ho 22 Apr 2020



Scoping scenarios and impact

“We need to understand and scope for different scenarios and time frames when it comes to FMCG retailers,” says David Smith, retail analyst at Investec.

“Over the short term, there was what the so-called ‘toilet paper effect’, during which consumers stocked up on staples going into and during lockdown. On a medium-term view, as social distancing measures become entrenched, it was likely that, especially at the higher end, spending that used to be directed at restaurants would likely be directed towards meals at home - a move that could benefit the food retailers.

“However, on a longer-term view, weaker wage and salary growth, as well as job losses, would weigh on retail sales, both for FMCGs and durable goods,” said Smith.

While the food and drug retailers may show resilience over the short term, there’s likely to be a notable impact over time. Such impacts and breakdown in activity have, and will continue to, impact supply chains, having a knock-on effect for FMCG firms.

“Supply chains were certainly an issue, but the bigger concern is the longer-term impact on demand,” says Geard. “There might well be a quick recovery in beverage and alcohol sales once lockdowns are lifted, but how long will it take for social distancing measures to be removed, for people to regain confidence and before consumer behaviour goes back to normal?”

According to Smith, businesses should not expect a major upswing in demand in May and June, particularly as consumers come under increasing strain. “This could result in even well-run businesses needing to shore up their cash balances, which could see some needing to come to market to raise capital,” he added.



3 key trends going forward

With no playbook in hand, each sector is carving its own pathway to “a new normal”, complete with restrictions, health-safety protocols and changed consumer behaviour in mind, and the FMCG sector is no different.

Smith pointed to three clear trends – a shift to online, growth in pre-cooked meals at supermarkets (vs restaurant meals), and greater market consolidation among retailers.

The current crisis has also highlighted the advantages accruing to those food and staple producers who have invested heavily in their businesses over the years. Those that have invested, and continue to invest, in digitalisation, in their brands, supply chains and innovation, are the ones that will emerge stronger.

Geard concludes, “There are opportunities for FMCG firms in the current crisis. There has been a lot of drive in recent years towards premium brands. I see an opportunity going in the other direction – with businesses innovating down and not just up.

“The weaker currency benefits exporters, but it can also benefit producers in their home markets. It creates an opportunity for local producers and manufacturers to compete in the South African market against imports from foreign producers.”

For more on this topic, listen to Investec's podcast 'Go big or go online: Retail's uncertain post-Covid future':