



## Industry Commentary

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## COVID-19's Immediate Impact on the Food and Beverage Industry

### Six Themes We are Closely Monitoring

Few industries have been affected as immediately and drastically by the COVID-19 pandemic as the food and beverage industry. From our daily conversations with business owners, management teams, investors, and analysts throughout the industry, we know that these people and their teams are working diligently around the clock to ensure that the global food supply chain continues to meet the demands of this unprecedented challenge.

We have identified six initial themes that we will be closely monitoring as the COVID-19 response progresses. These preliminary themes and related insights are based on our real-time conversations with professionals throughout the food and beverage industry, as well as preliminary data we have gathered through March 22, 2020.

#### 1. **Bifurcation between grocery/retail and foodservice.**

Most companies in grocery and food retail are performing relatively well, as the “pantry loading” phenomenon has caused short-term revenue to spike across nearly all grocery categories. Walmart and Costco, for example, have outperformed broad equity indexes, with modest declines of 3.9% and 9.8%, respectively, for the month ending March 20.

It will be interesting to see how grocery sales respond once the initial wave of pantry loading subsides, as well as how brick-and-mortar grocers fare relative to e-commerce grocery channels, whose ability to offer contactless delivery (i.e., at-door drop off) provides a new and valuable benefit for many consumers. Some physical grocery stores are offering special hours for the elderly to help mitigate risk and enable sales. It is also worth noting that the near-term delineation between traditional and online grocery will be mitigated by the fact that food retailers and convenience stores will remain open as “essential” businesses for communities with shelter-in-place restrictions.

Meanwhile, demand for restaurants and many aspects of foodservice has fallen off a cliff. In the near term, we will be watching how readily consumers begin to tire of home-cooked meals and begin to replicate their dining-out experiences with increased rates of ordering takeout. Over the intermediate term, we will be closely watching to see if restaurant traffic returns to pre-pandemic levels once health officials lift the social distancing restrictions. With closures of

in-restaurant dining, restaurants have significant excess capacity and are leaning heavily on delivery and carry out to cover wages and overhead expenses.

**2. Consumer staples are performing relatively well.**

Given their less-discretionary nature, it is no surprise that consumer staples have outperformed other sectors since the start of the pandemic. Within grocery stores, household cleaning, paper products, barbeque, water, first-aid, and personal cleansing categories all saw year-over-year sales increases of more than 30% for the week ending March 8, according to IRI.

Consumer staples brands and retailers are expected to see an additional boost from the Trump administration's plan to send checks directly to Americans as part of an economic stimulus package. The question is whether this relative outperformance will last once the panic- and stimulus-related activity subsides; the answer may depend on how long consumers are forced to remain in their homes and how well supply chains can keep up with demand.

**3. Immense opportunity—and operational pressure—for food delivery.**

As social distancing and mandatory shutdowns force consumers to eat all of their meals at home, this has created a huge opportunity for all aspects of food delivery. This includes online grocery, curbside pickup and home delivery for traditional grocery, restaurant delivery, and meal-kit and meal-prep services. But how quickly can delivery-focused companies respond to massive increases in demand, and how well can supply chains and distribution networks keep up?

To help alleviate the bottlenecks, foodservice distributors are diverting trucks and other resources to grocery channels. Amazon, which has reported growing backlogs for its grocery

delivery services, announced that it would hire an additional 100,000 temporary workers to meet coronavirus-related demand. Instacart announced that it plans to hire 300,000 additional workers, and Blue Apron's stock has surged when the meal-kit provider announced that it was increasing capacity.

Consumer staples have seen strong performance in brick-and-mortar grocers as well as in e-commerce and online delivery channels such as Amazon, Walmart.com, Instacart, and direct-to-consumer. It is possible that stay-at-home measures could prove to be a long-term inflection point in e-commerce's penetration of the food and beverage industry.

**4. Private label's market-share gains are poised to accelerate.**

Over the past decade—against a backdrop of continued economic expansion—private-label products have steadily gained market share from branded CPG products. This has been driven by a multitude of factors, including consumers' improved perception of the quality of store brands, grocers using expanded store-brand offerings as a point of differentiation, and decreased loyalty to national brands among younger shoppers. Now that we have entered a downturn that will likely turn into a recession, private label's market-share gains should accelerate as consumers look for ways to cut costs.

According to IRI, consumption of private-label foods increased more than 10% on a year-over-year basis for the week ending March 8, the most recent available data. This number is almost certain to surge as data for the rest of March becomes available. It is too early to tell whether this initial increase is primarily driven by the rising tide of pantry loading lifting all boats or shoppers rotating to less expensive alternatives. But as consumers transition into bracing for a prolonged downturn, we expect private label's importance in

grocery, both in-store and online, to continue building on its already elevated state.

**5. Value-focused, better-for-you options are well-positioned.**

Consumers' growing concern about what they eat and drink has been one of the dominant megatrends in food and beverage over the past decade. This is reflected in the robust growth of natural, organic, clean-label, plant-based, and other better-for-you products. While a recession may cause some consumers to prioritize value over better-for-you, we expect a more likely outcome is consumers prioritizing value and better-for-you. We believe that companies offering better-for-you products at price points that appeal to value-focused shoppers will be well-positioned during the upcoming downturn.

**6. Shelter-in-place could be a longer-term catalyst for increased in-home cooking among younger consumers.**

A 2017 study by the U.S. Department of Agriculture found that millennials spend less money on groceries, spend less time on food preparation, and spend more money eating out than older generations. It is unclear how much of this difference is a result of millennials' current stage of life versus a generational shift in eating habits. Regardless, it will be interesting to see if an extended period of forced eating at home—as well as heightened budgetary concerns during a recession and reluctance to eat in crowded restaurants even after the pandemic ends—creates any durable changes in millennials' enthusiasm for cooking and in-home meal-preparation.

## Grocery Categories With the Largest Year-Over-Year Sales Increases for the Week Ending March 8, 2020

Grocery Category	Sales Increase
Household cleaning	65.4%
Paper products	59.4%
Barbeque	49.4%
Personal cleansing	41.8%
Non-fruit drinks	37.9%
Water	36.0%
First-aid	35.2%
Health remedies	27.2%
Meals	26.9%
Nutrition/weight loss	26.5%
Water treatment	25.2%
Laundry	24.7%

Source: IRI

Underpinning all of these themes is the question of whether the current shutdown will result in sustained changes in how people shop for, prepare, and consume food. It will take a long time before that fundamental question can be answered with much precision.

Certainly, many additional themes that merit close attention will emerge as the COVID-19 response progresses. We are committed to closely monitoring all of these developments and sharing our perspective based on our ongoing conversations with business leaders and their teams at the front lines of the food and beverage industry, as well as with investors and analysts who support this critical part of the global economy.

If you have any questions about what any of these themes mean for your business, please don't hesitate to contact us.

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