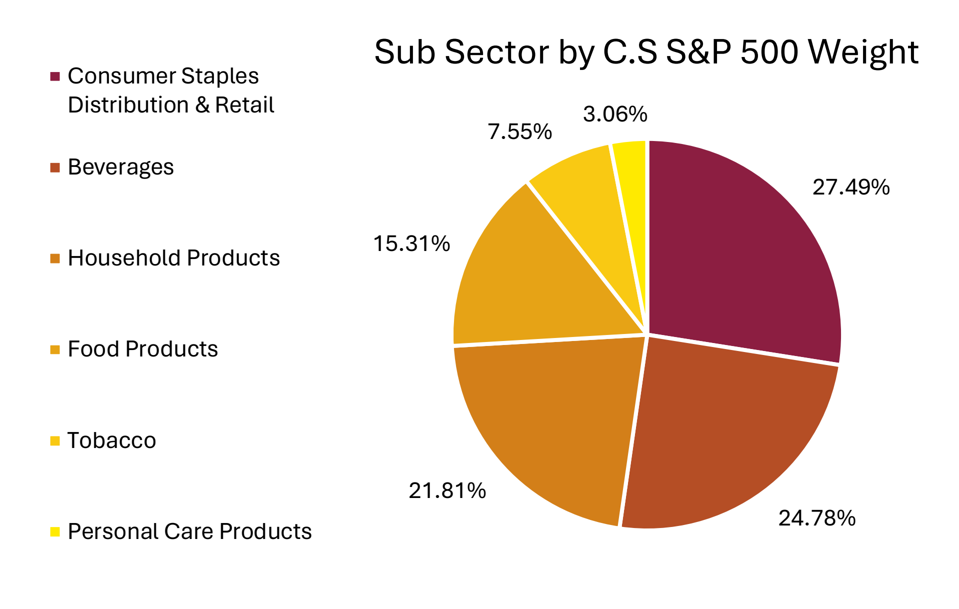
Consumer Staples Screener

Economic Overview

Based on the latest CPI report released on February 13, 2024, CPI inflation remains steady at 3.1%, showing no change from the previous report. The Federal Reserve is not anticipated to reduce rates until after the May meeting, with a 35% probability of a rate cut at that time. While unemployment has remained stable at 3.7%, indications suggest potential shifts ahead. Despite seeming tight on the surface, quit rates declined to 2.2% from the previous year's 2.6% indicating that people are less confident in their ability to get another job. Employers have been hesitant to lay off workers in anticipation of rate reductions, but the recent developments with inflation may strain their ability to maintain staffing levels. Additionally, consumer confidence is dwindling, particularly as smaller banks face the risk of collapse. Credit card debt and default rates are at a 10-year high, while delinquencies in housing payments have been steadily increasing over the past year. Pre-pandemic, banks heavily invested in mortgage-backed securities (MBS), which could pose challenges as new regulations mandate increased capital reserves, limiting profitability and increasing financial strain. The Fed focuses primarily on Core CPI inflation which is heavily affected by shelter inflation, which currently stands at 6%. Shelter inflation will decrease significantly following rate cuts, due to a more fluid housing market and higher rates of mortgage refinancing. Considering recent statements by Jerome Powell indicating a preference for average, rather than exceptional results, there remains a strong possibility of rate cuts by the May meeting. The next CPI report on March 12 is anticipated to reflect these trends, with expectations of decreasing inflation and rising unemployment rates.

Consumer Staple Sector Overview

The consumer staples sector encompasses a diverse array of products, spanning from food, beverages, household items, and personal care products to tobacco goods, which notably stand out due to their anticipated growth trajectory and enduring customer loyalty. Despite facing heightened regulatory scrutiny and concerted public health initiatives, companies within this sector maintain a strong market presence, due to their robust profit margins. For instance, the Tobacco Industry boasts a net margin of 33.43% over the industry average and a return on equity of 36.49% in Q4 2023. Alongside tobacco, the consumer-packaged goods subsector is and will continue to be a key player moving forward. As shown above, labor market conditions and potential interest rate adjustments potential cut in May can lead to a resurgence in conventional consumer spending habits. For instance, the shift away from single-serve frozen meals towards more cost-effective bulk options has caused a strain on large name-brand consumer staple companies. The reversal of this trend is expected to benefit established brand names, leading to sustained revenue growth. Focusing on large-cap, recognizable brand companies will be profitable in a lower interest rate environment. However, within the retail landscape, the rise of e-commerce is causing disruptions to traditional distribution channels, prompting widespread resort to steep price promotions and an expansion of product offerings. With a noticeable shift among consumers toward online shopping, businesses are adapting as shown by the increasing popularity of grocery shipping services. Finally, food prices have negatively affected the sector as they have been rising over the past year. The overall food price index was at an all-time high in 2022 due to an avian flu outbreak and disruptions from the Ukrainian-Russian war but then fell to 118. While lower than before, the index is still up 10.3% YTD. Overall, all sentiments seem to be positive, and the sector is returning to normal.



10 Largest Consumer Staples	Market Cap
Walmart	$428.87 B
Procter & Gamble	$350.35 B
Costco	$287.69 B
Coca-Cola	$259.23 B
PepsiCo	$237.77 B
Philip Morris	$148.50 B
Mondelez International, Inc.	$99.73 B
Altria Group, Inc.	$73.43 B
Colgate-Palmolive Company	$66.15 B
Target Corporation	$64.75 B

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Consumer Staples Screener

Screener Breakdown

Risk Mitigation

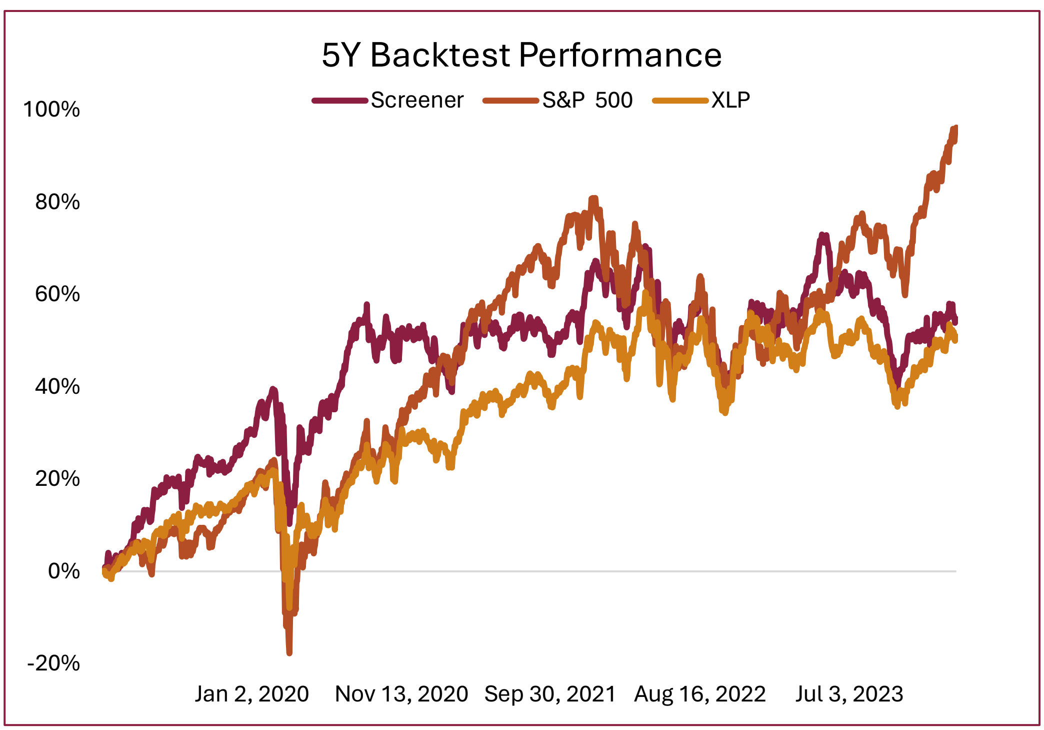
The Piotroski score looks at the overall health of a company through several factors including, lower long-term debt than the previous year, ROA, and net income. The number seven was found through a combination of intuition and trial and error. Since this screener is a quantitative analysis of the companies, going with an “unhealthy” company brings too much risk. This ties into the reasoning for the Market Cap minimum. While not exactly a measure of name recognition, a small-cap company has too much risk involved with marketing and limited exposure.

Valuation

The quarterly gross margin of at least 35% is to focus on companies with consistent returns. This is a way to direct the screener toward tobacco companies, which are known for their high-profit margins. Return on Equity is an industry-standard benchmark and 16% was found to be the highest returning result. 10% is the industry average, but my screener targets companies focused on re-investment and product innovation. The combination of strong profit margins and high reinvestment leads to a competitive advantage when compared to the rest of the sector. The final metric is the quarterly current ratio, which is used to assess liquidity and is standard across the sector. 0.5 is extremely low for the current ratio and is merely used to eliminate companies that have a good risk of not being able to pay off their short-term debt obligations. In conclusion, the screener focuses on companies that have strong margins and reinvest in the companies to continue growth through new products or advancements.

HSY, PG, MNST, CHD, GIS, CL, MO, CLX

The screener has outputted 8 companies with 6 operating within consumer-packaged goods. Church & Dwight, Clorox, Procter & Gamble, and Colgate-Palmolive all produce several cleaning products. Church & Dwight poses a significant risk due to declining performance but for the past 2 years, the stock price has been stable with a strong dividend. General Mills owns several snack brands such as Cinnamon Toast Crunch and Annie’s. Altria is a tobacco company behind Marlboro and several other cigarette and e-cigarette products.



Universe

- In S&P 500
- Classify as Consumer Defensive
- Piotroski F Score T12M > 5
- Market Cap > 1b
- Gross Margin 1Q > 0.35
- Return on Equity 1Y > 0.16
- (Current Assets 1Q ÷ Current Liabilities 1Q) > 0.5

Companies

Returns, Results and Final Thoughts

Over the past 5 years, the sector has had little to no growth, but my screener has beaten the sector-specific index by 4%. While backtesting isn’t representative of future growth, it shows potential in a stagnant sector. While still not outpacing the S&P, excess consumer spending is set to decrease, and the consumer staple sector will be a good investment moving forward. While the bulk of the growth was centered towards 2019 and 2020, the whole economy has had stagnant growth in 2022 and the recent S&P growth was led mainly by technology stocks and the AI boom.

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