Fast-Moving Consumer Goods
Post-COVID Implications
October 2020
Table of Contents

Executive Summary 2
Impact of COVID-19 3
Challenge of Maintaining Shareholder Returns 8
Impact on Indebtedness 11
What Does This Mean for Corporates? 14
Key Questions For CFOs 19
Key Contacts 20
Appendix 21
   1) Supplementary Analysis 22
   2) Assumptions & Criteria 24
Executive Summary
Life after COVID presents opportunities for growth but new challenges for capital allocation

Impact of COVID-19
- COVID-19 has accelerated structural change in FMCG, including a shift in channel strategy towards e-commerce and focus on health & wellbeing, whilst arguably exposing weakness along the supply chain
- Most sub-sectors have fared relatively well supported by favourable consumptions trends in the initial stages of lockdown and medium-term revenue and margins expectations have also stabilised
- Alcohol has taken a bigger hit due to exposure to on-trade with only Beauty expected to fare worse. However, impairments in H1 have been largely non-cash with largest players well positioned to drive M&A post 12-18 months anticipated recovery

Maintaining Shareholder Returns
- FMCG has outperformed all other sectors over last fifteen years from a Total Shareholder Return (TSR) perspective which we expect will remain an important element of the investment case for these corporates going forward
- More recent performance has wavered, undermined by share price return. However, COVID-19 may provide more advantaged sub sectors the opportunity to fine tune TSR strategy. CFOs will need to balance competing cash priorities across investment, M&A and return of surplus capital to investors
- Investment in drivers of future value across channel diversification, health and sustainability can provide a runway to top-line growth and margin expansion, alongside supporting upside in TSR

Impact on Indebtedness
- Indebtedness has steadily increased across sub-sectors driven by consistent discretionary cash commitments (capex, M&A, shareholder returns) and relative flattening of margins
- Going forward, flattening margins, higher capex and potential for increased M&A may create the perfect storm for further credit rating pressure, however corporates may use the opportunity to revisit their long-term optimal credit ratings
- Releasing capital through further working capital optimisation or disposal of non-core brands or alternative financing structures (hybrid capital) will become more important as CFOs target balance sheet flexibility

What Does This Mean for Corporates?
- Supply Chain Overview:
  i. Efficiencies: Optimising inventory remains top of the near-term agenda as corporates support retailers and suppliers facing liquidity stress to safeguard supply chain. Longer-term, focus may shift to reducing DSO and protecting DPO
  ii. Other Considerations: Pandemic has brought holistic supply chain planning into focus including diversification (localising, contingency plans), re-thinking inventory buffers, point of sale enhancements and last mile capabilities
- Portfolio reshaping: Re-alignment of portfolios to access growth will continue to gain momentum
Impact of COVID-19
COVID-19 & Key Challenges
A more structural change has been gathering momentum

Consumption Trends
- Consumption shifted to inside the home and lower demand for discretionary goods
- Evolving trends like sustainability, health and digital accelerated by crisis
- Shift from 'premium' categories to 'value' as customers trade down albeit temporarily

Supply Chain
- Pandemic exposed weakness of global supply chains to risk of disruption
- Corporates had to fund increased working capital needs whilst supporting key suppliers
- Shift to e-commerce and local supply requires review of trade-off between lower working capital needs vs. margin dilution

Investment
- Investment in intelligent supply chains which respond in real time to local market demand
- Aligning M&A to strategic goals including portfolio reshaping, technology and data
- Leveraging downward pressure on trading multiples to acquire challengers

P&L Headwinds
- Higher near term one-off costs and negative portfolio mix are likely to be margin dilutive
- Further efficiencies harder to find as margin widening has been driven by cost control as organic, top-line growth has been sluggish
- Pricing will intensify as brands compete with private labels to win or retain market share

Total Shareholder Returns
- Activist investor pressure led corporates to return surplus capital to shareholders
- Cash returns are broadly stable but limited share price growth has weighed on TSR
- Post-COVID, investing in 'future proofing' portfolios is key to sustaining TSR value

Sustainability Focus
- Customers expect even greater transparency to vet goods are safe and ethically sourced
- Developing digital capabilities across the supply chain to increase visibility
- Investors are more ESG conscious across waste reduction, emissions and recyclability which underpin the need for investment

Actions Taken in H1
- Cost Efficiencies
- Defer Capex
- Strengthen Liquidity

Actions in Progress
- Supply Chain
- Shareholder Returns
- Non-core Disposals

Sources: SCB Analysis, S&P, Moody’s
Relative Performance

While the initial impact was severe, some of the sub-sectors have recovered lost ground.

In the early stages of lockdown, both F&B and HPC have outperformed the S&P 1200, reflecting the impact of stock-piling and other favourable consumption trends. S&P 1200 has regained some momentum since May, reflected by the narrowing or reversal of the performance gap.

Haircuts to 2020 estimates have been broad based, but Alcohol has been worst hit with leading manufacturers booking mainly non-cash impairment charges. Whilst this has stressed recent share price performance, there is limited impact on credit metrics with market leaders well positioned to exploit M&A opportunities in the post-recovery phase.

Change in Market Consensus on 2020 Revenues (%) and EBITDA Margins (bps) [08/09/20 vs. 01/01/20]

<table>
<thead>
<tr>
<th>Sub-sector</th>
<th>Expected Impact</th>
<th>Change to 2020F</th>
<th>Return to Normalcy¹</th>
</tr>
</thead>
<tbody>
<tr>
<td>F&amp;B</td>
<td>Low</td>
<td>Sales (3.6)%</td>
<td>2020</td>
</tr>
<tr>
<td></td>
<td></td>
<td>EBITDA Margin (79)bps</td>
<td>2021</td>
</tr>
<tr>
<td>HPC</td>
<td>Low except ‘Beauty’ - High</td>
<td>(2.8)%</td>
<td>(88)bps</td>
</tr>
<tr>
<td>Alcohol</td>
<td>Moderate</td>
<td>(10.7)%</td>
<td>(222)bps</td>
</tr>
<tr>
<td>Tobacco</td>
<td>Low</td>
<td>(3.7)%</td>
<td>(69)bps</td>
</tr>
</tbody>
</table>

Sources: Capital IQ, Company Reports and Presentations, Broker Consensus, SCB Analysis, S&P
Assumptions: Please see slide 25 ‘Appendix: Criteria, Definitions & Assumptions’ for further details
Notes: (1) “COVID-19 Battered Global Consumer Discretionary Sectors But Lifted Staples; Recovery Varies By Subsector” (S&P, August 2020)
**H1 Corporate Results**

**Divergent impact across industry sub-sectors**

<table>
<thead>
<tr>
<th>F&amp;B</th>
<th>HPC</th>
<th>Alcohol</th>
<th>Tobacco</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Impact</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>• <strong>Defensive nature</strong> of F&amp;B industry has seen this sector emerge as a winner off the back of high-stockpiling and likely higher home consumption in the medium-term</td>
<td>• <strong>Minimal impact for home and most personal care businesses</strong> which generate sales from daily essentials</td>
<td>• <strong>Most impacted sub-sector</strong>, greater proportion of retail revenue derived from on-trade sales compared to non-alcoholic beverages. Twofold setback for corporates with travel retail exposure</td>
<td>• <strong>Resilient but adverse effect from slowdown in reduced risk and FX volatility</strong></td>
</tr>
<tr>
<td>• Adverse impact in 2020 limited to corporates with a reliance on out-of-home channels, such as food services, ice cream and certain beverages companies</td>
<td>• <strong>Long-term demand likely to be sustained by higher hygiene standards</strong> better positioning HPC relative to other sectors</td>
<td>• <strong>Margin contraction expected in 2020</strong> despite expectations for lower commodity prices. <strong>Discretionary cash commitments are being curtailed</strong> to offset free cash flow pressure</td>
<td>• <strong>Cigarette volumes continue to decline</strong> reflecting switching to reduced risk, albeit at a lower rate in 2020, alongside a marginal impact from lower duty free sales. Price increases are still considered sustainable as little evidence of trading down in recession</td>
</tr>
<tr>
<td>• Higher proportion of on-trade exposure the longer the recovery for these corporates</td>
<td>• <strong>Beauty segment most impacted due to discretionary nature and disruptions</strong> across professional beauty and travel retail. Highly leveraged companies will face pressure in 2020 as consumers defer purchases</td>
<td>• <strong>High margin, premium labels may fall out of favour</strong> requiring volumes of value brands to significantly pick up diluting margins</td>
<td>• <strong>High dividend pay-out expected to continue</strong> for most with limited capacity for large M&amp;A within current ratings</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>Challenges</strong></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Consumer Trends</td>
<td>Supply Chain</td>
</tr>
<tr>
<td>Investment</td>
<td>Consumer Trends</td>
</tr>
<tr>
<td>Supply Chain</td>
<td>Investment</td>
</tr>
<tr>
<td>Sustainability Focus</td>
<td>Shareholder Returns</td>
</tr>
<tr>
<td>P&amp;L Headwinds</td>
<td>P&amp;L Headwinds</td>
</tr>
<tr>
<td>P&amp;L Headwinds</td>
<td>Shareholder Returns</td>
</tr>
</tbody>
</table>
Mitigants & Emerging Strategies
Corporates are pulling on a number of levers to help position themselves for the challenges ahead

<table>
<thead>
<tr>
<th>F&amp;B</th>
<th>HPC</th>
<th>Alcohol</th>
<th>Tobacco</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost Efficiencies</td>
<td>Cost Efficiencies</td>
<td>Cost Efficiencies</td>
<td>Cost Efficiencies</td>
</tr>
<tr>
<td>Supply Chain</td>
<td>Supply Chain</td>
<td>Supply Chain</td>
<td>Supply Chain</td>
</tr>
<tr>
<td>Deferral Capex</td>
<td>Deferral Capex</td>
<td>Deferral Capex</td>
<td>Deferral Capex</td>
</tr>
</tbody>
</table>

**Mitigants**

- Non-core Disposals
- Shareholder Returns
- Strengthen Liquidity

**Key Takeaway from H1**

"Free cash flow was CHF 3.3 billion in the first half...We continue to be disciplined in our capital allocation with positive contribution from both CapEx and working capital"  
"...driving...efficiency improvement in all facets...delivering strong cost and cash productivity...change in manufacturing...look at...appropriate number of suppliers...to ensure you have the agility to react...capacity swings that we're seeing."  
"We have taken decisive action...tightly managing our costs, reducing discretionary expenditure and reallocating resources...We have strengthened liquidity, giving us flexibility to continue to invest effectively in the business for the long term."  
"...tobacco industry was not immune to the impact of the pandemic, our performance was resilient...delivered robust growth in adjusted operating profit...driven by pricing gains in the international tobacco business."  
"...capital allocation priorities remain the same...reinvest where appropriate...grow the dividend...M&A and share buybacks unlikely to play a prominent role in the near term...remain confident in our liquidity position as we...navigate the crisis."  
"Gross margin reduced by 30bps driven by costs to adapt and run our...supply chain in response to Covid-19, ensuring the safety and continuity of our operations, as well as an adverse mix effect..."  
"The business is showing good resilience...A comprehensive cost mitigation programme has been implemented, together with active management of our cash...We have adapted our manufacturing and supply chains to ensure they remain...operational"  
"...further strengthened our liquidity position through bond issuances the establishment of bilaterals and the renegotiation of our RCF...remain focused on maximising cash generation and deleveraging..."
Challenge of Maintaining Shareholder Returns
Shareholder Returns & Expectations
FMCG sub-sectors have featured in the Top-5 for at least one component of TSR over last 15 years

- Over the last fifteen years, FMCG has outperformed all other sectors from a TSR perspective. Whilst a major part of growth has been driven by expansion into Emerging Markets (EMs), this performance reflects success of brand building, developing economies of scale and an appetite for value accretive M&A.
- Across sub-sectors, F&B has led driven by its top of the table share price return with Alcohol the only other sub-sector to feature in Top-10 for this metric. Other sectors have relied on cash returns, particularly Tobacco and HPC which feature in Top-5 for dividend and share buyback returns respectively.
- More recent performance has seen some reversal of this trend with TSR wavering across sub-sectors. This trajectory reflects the pressure CFOs face to balance competing cash priorities across investment in organic growth, acquisitions and returning surplus capital to investors.

### 15-Year Average: Top-5 Sectors by Category (2004-19)

<table>
<thead>
<tr>
<th>Share Price Return</th>
<th>Cash Dividend Return</th>
<th>Share Buyback Return</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>F&amp;B</strong> 16.8%</td>
<td><strong>Utilities</strong> 4.6%</td>
<td><strong>Tech</strong> 3.7%</td>
</tr>
<tr>
<td><strong>Non-Food Retail</strong></td>
<td><strong>Tobacco</strong> 4.4%</td>
<td><strong>Aerospace &amp; Defense</strong></td>
</tr>
<tr>
<td><strong>Consumer Durables</strong></td>
<td><strong>O&amp;D</strong> 3.4%</td>
<td><strong>Hotel &amp; Leisure</strong> 3.1%</td>
</tr>
<tr>
<td><strong>Hotel &amp; Leisure</strong></td>
<td><strong>M&amp;M</strong> 3.2%</td>
<td><strong>HPC</strong> 2.9%</td>
</tr>
<tr>
<td><strong>Aerospace &amp; Defense</strong></td>
<td><strong>Telecoms &amp; Media</strong> 3.2%</td>
<td><strong>Pharma &amp; Healthcare</strong></td>
</tr>
</tbody>
</table>

**Sources:** Capital IQ, Company Reports and Presentations, SCB Analysis

**Assumptions:** Please see slide 25 ‘Appendix: Criteria, Definitions & Assumptions’ for further details.
TSR Rankings & How These Have Moved
COVID-19 has changed the game again but the rules of winning are the same

- F&B slipped down the rankings over more recent periods reflecting challenge of generating top-line growth momentum, particularly across developed markets. On the other hand, HPC has improved over time reflecting momentum in personal care pre-COVID whilst Alcohol has been reasonably consistent.
- COVID-19 may fuel a reversal of fortunes with CFOs in more advantaged sub sector presented with an opportunity to fine tune TSR strategy. Arguably, some F&B corporates are better positioned and can capitalise on drivers of future value across channel diversification, sustainability and health.
- Cash returns are expected to remain pivotal to the medium-term equity story. Ultimately, a strategy focussed on growth and margin expansion whilst fulfilling discretionary cash commitments has proven successful and can pave the way to enhancing future TSR.

<table>
<thead>
<tr>
<th>15-Year Average TSR (%)</th>
<th>10-Year Average TSR (%)</th>
<th>5-Year Average TSR (%)</th>
<th>2019 TSR (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Ranking</strong></td>
<td><strong>Ranking</strong></td>
<td><strong>Ranking</strong></td>
<td><strong>Ranking</strong></td>
</tr>
<tr>
<td>F&amp;B</td>
<td>Alcohol</td>
<td>HPC</td>
<td>Tobacco</td>
</tr>
<tr>
<td>#1</td>
<td>#11</td>
<td>#13</td>
<td>#16</td>
</tr>
<tr>
<td>21.7%</td>
<td>14.2%</td>
<td>13.8%</td>
<td>13.1%</td>
</tr>
</tbody>
</table>

Sources: Capital IQ, Company Reports and Presentations, SCB Analysis
Assumptions: Please see slide 25 ‘Appendix: Criteria, Definitions & Assumptions’ for further details
Impact on Indebtedness
In the hunt for growth, corporates have invested in innovation, leveraged M&A to access faster growth categories or regions and responded to investor activism for higher shareholder returns leading to higher average indebtedness, arguably limiting headroom to exploit post-COVID opportunities within current ratings.

Ratings have shifted from ‘A’ or above to ‘BBB’ or lower over last ten years. Recent negative rating actions have focussed on issuers with already stretched credit metrics in the build up to the crisis. Going forward, flat margins, higher capex and possible uptick in M&A create the perfect storm for credit ratings.

Whilst the benefits of higher ratings vs. flexibility of lower ratings will come into question, capital release from areas like working capital and strategic disposals can help. Corporates may also diversify capital structure by refinancing senior debt with hybrid capital instruments, possibly offsetting ratings pressure.

### Indebtedness & Optimal Credit Ratings

Funding needs may create the perfect storm for credit ratings.

<table>
<thead>
<tr>
<th>Net Debt to EBITDA (times)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>F&amp;B</strong></td>
</tr>
<tr>
<td><strong>HPC</strong></td>
</tr>
<tr>
<td><strong>Alcohol</strong></td>
</tr>
<tr>
<td><strong>Tobacco</strong></td>
</tr>
</tbody>
</table>

- **Increase in leverage**: +56%
- **De-leveraging**: (4%)
- **Increase in leverage**: +88%
- **De-leveraging**: +23%
- **Five-year average**
  - **Avg. '04-'09**: 1.5x
  - **Avg. '09-'14**: 1.7x
  - **Avg. '14-'19**: 2.3x
  - **Avg. '14-'19**: 1.3x
  - **Avg. '14-'19**: 1.1x
  - **Avg. '14-'19**: 1.2x

### S&P Ratings Distribution Over Time (Current vs. December 2009)

#### 2009
- **AA**: 31%
- **A**: 44%
- **BBB**: 19%
- **Sub-IG**: 6%

#### 2020
- **AA**: 34%
- **A**: 71%
- **BBB**: 7%
- **Sub-IG**: 4%

**Sources:** Capital IQ, Company Reports and Presentations, SCB Analysis

**Assumptions:** Please see slide 25 'Appendix: Criteria, Definitions & Assumptions' for further details.

**Notes:**
1. Relative to average indebtedness over 2004-09
2. Ratings as of 9th September 2020
3. Includes all corporates rated by S&P in the AAA-C bands across sub-sectors (please see p.26).

Analysis includes ratings for main rated entity of larger corporate groups only; we have omitted certain entities, such as subsidiaries or holding companies, where ratings are linked to those of their parent companies.
Understanding Drivers of Future Indebtedness
Flat margins combined with stable capex and supply chain stress may stretch funding requirements

- **Margins have largely plateaued across FMCG.** Consumer staples are expected to maintain stable margins in 2020 as efficiencies from SKU rationalisation to meet a surge in demand and lower marketing spend offsets higher logistics and well-being costs across the supply chain. However, **longer-term outlook remains uncertain**
- **A key challenge for FMCG will be maintaining strong cash conversion as margins flatten or weaken.** Whilst working capital efficiencies have helped LTM CFO/EBITDA settle at five-year high for F&B and HPC, medium-term convertibility will be squeezed unless corporates deliver further margin and supply chain efficiencies
- **Corporates have maintained stable capex over recent years but COVID-19 has accelerated investment needs.** As capex becomes less discretionary and more critical, balance sheets are expected to come under increasing pressure, **requiring review of capital allocation priorities and sources of funding**

### EBITDA Margins (%)

<table>
<thead>
<tr>
<th>Year</th>
<th>F&amp;B</th>
<th>HPC</th>
<th>Alcohol</th>
<th>Tobacco</th>
</tr>
</thead>
<tbody>
<tr>
<td>2014</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2015</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2016</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2017</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2018</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2019</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2020 LTM</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Cash From Operations (CFO) / EBITDA (%)\(^1\)

<table>
<thead>
<tr>
<th>Year</th>
<th>F&amp;B</th>
<th>HPC</th>
<th>Alcohol</th>
<th>Tobacco</th>
</tr>
</thead>
<tbody>
<tr>
<td>2014</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2015</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2016</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2017</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2018</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2019</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2020 LTM</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Capex / EBITDA (%)\(^1,2\)

<table>
<thead>
<tr>
<th>Year</th>
<th>F&amp;B</th>
<th>HPC</th>
<th>Alcohol</th>
<th>Tobacco</th>
</tr>
</thead>
<tbody>
<tr>
<td>2014</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2015</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2016</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2017</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2018</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2019</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2020 LTM</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

---

**Sources:** Capital IQ, Company Reports and Presentations, SCB Analysis

**Assumptions:** Please see slide 25 ‘Appendix: Criteria, Definitions & Assumptions’ for further details

**Notes:** (1) LTM data per CIQ for peers where latest detailed financials are available. Excludes Pernod Ricard S.A., Meiji Holdings Co. Ltd, Yakult Honsha Co. Ltd. (2) Capex includes intangibles
What Does This Mean for Corporates?
CFOs’ Top Concerns Driven By COVID-19
Supply chain issues ranked Top-5 amongst other critical concerns

**PwC “COVID-19 CFO Pulse” survey**
**CFO’s Top-3 concerns with regard to COVID-19¹**

<table>
<thead>
<tr>
<th>Concern</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Potential global recession</td>
<td>69%</td>
</tr>
<tr>
<td>Financial impact²</td>
<td>66%</td>
</tr>
<tr>
<td>Decrease in consumer confidence reducing consumption</td>
<td>40%</td>
</tr>
<tr>
<td>The effects on our workforce / reduction in productivity</td>
<td>36%</td>
</tr>
<tr>
<td>Supply chain issues</td>
<td>31%</td>
</tr>
<tr>
<td>Difficulties with funding</td>
<td>18%</td>
</tr>
<tr>
<td>Not having enough information to make good decisions</td>
<td>14%</td>
</tr>
<tr>
<td>Cybersecurity, privacy, or fraud risks</td>
<td>9%</td>
</tr>
<tr>
<td>Impacts on tax, trade, or immigration</td>
<td>7%</td>
</tr>
<tr>
<td>Lack of a comprehensive / tested company emergency preparedness plan</td>
<td>3%</td>
</tr>
<tr>
<td>Other</td>
<td>3%</td>
</tr>
</tbody>
</table>

CFOs are considering changing supply chain strategy as a result of COVID-19³

- **52%**...will look for alternative sourcing options³
- **50%**...want to understand suppliers’ financial and operational health³
- **34%**...plan to extend visibility into their suppliers’ networks³
- **28%**...intend to use automation to improve decision making³

Notes: (1) Source of data from PwC’s “Global COVID-19 CFO Pulse” reports. Chart showing average results of the responses to the question “What are your top three concerns with respect to COVID-19?” from the 30 March 2020, 13 April 2020 and 28 April 2020 issues (2) Effects on results of operations, future periods, liquidity and capital resources (3) PwC (“PwC’s COVID-19 CFO Pulse – Insights from global finance leaders on the crisis and response” – 28 April 2020)
Supply Chain Considerations
Re-configuring the supply chain to build long-term resilience is very important

**Geographical Diversity**
- Diversifying production footprint to minimise concentration risk, e.g. vs.
- Effective contingency planning:
  - Secondary supplier activation
  - Agile production rerouting
  - Production rescheduling to prioritise items in light of raw material shortages
- Local sourcing to limit disruption risk
- Multi-source key commodities or key strategic components

**Inventory Buffer**
- Higher inventory buffer beyond historical averages may be the norm
- Dynamic capacity planning enabled via advanced demand forecasting tools and local market intelligence
- Scenario Planning:
  - Over-supply: order reduction, promotions, re-purposing of less seasonal products
  - Under-supply: secure raw materials, prioritise key client relationships

**Point of Sale**
- Rerouting sales to e-commerce / direct to customer / at-home consumption
- Tailor marketing plan to re-direct customers and achieve targeted channel mix
- Define pricing strategy to capture share of pent up demand ahead of a rebound in activity

**Last Mile**
- Automation and integration of supply chains, warehousing and distribution to achieve synergies
- Expand logistics capabilities with third parties to address shortage of last mile delivery service capacity
- Collaborating with other consumer product firms to create shared warehouses and logistics
- Increase incentives for customers to utilise in-store or dark stores¹ for collection or return of goods to reduce delivery costs

**Sustainability**
- New packaging and product design to reduce wastage
- Moving towards circular economy to minimise use of resource and turn waste into use / localised sourcing to reduce emissions from transport
- Reduce emissions via more efficient production and use of renewables

**Visibility**
- End-to-end monitoring: Leveraging digital and working with Tier 1 / 2 suppliers to predict supply chain vulnerabilities and enable back-up planning
- Intelligent Supply Chain: Accelerate digital investments such as AI, machine-learning and cloud-based database for better integrated planning

**Notes:** (1) Distribution centres that are designed for online shopping
Working Capital Evolution
Further efficiencies won’t be easily extracted from the already stretched cash cycles

- **FMCG working capital efficiencies have largely been driven by payables over last five years.** Whilst this has also been broadly supported by improving DSO, there remains pressure on trade cycles from DIO across Alcohol, Tobacco and HPC driven partly by higher levels of strategic inventory.
- **2019 results reflect a deceleration in year-on-year DPO improvement** signalling that stretching suppliers to drive efficiencies is unsustainable. COVID-19 is set to exacerbate this trend as corporates turn to supporting key suppliers to minimise risk of disruption bringing Supply Chain or Supplier Financing back into the spotlight.
- **Near-term, corporates may need to balance risk of retailer or supplier default with safeguarding distribution networks and supplies, particularly in EMs.** Investment in predictive analytics and AI promises to provide data to optimise inventory and respond quickly to changes. Longer-term, focus will shift to improving DSO and protecting DPO.

### Cash Conversion Cycle (CCC): 2019 vs. 2014 (Days)

<table>
<thead>
<tr>
<th>DPO</th>
<th>Improving</th>
<th>Outstanding</th>
<th>Worsening</th>
</tr>
</thead>
<tbody>
<tr>
<td>FMO</td>
<td>Improving</td>
<td>Outstanding</td>
<td>Worsening</td>
</tr>
<tr>
<td>15</td>
<td>10</td>
<td>8</td>
<td></td>
</tr>
</tbody>
</table>

Size of bubble represents decrease in CCC days.

### Working Capital Solutions

**DSO**
- Buyer Financing
- Receivables Discounting (Debt Factoring)
- Bills / BAD Discounting
- Migrating Collections into Electronic Transfers

**DPO**
- Supply Chain / Supplier Financing
- Post-Dated Cheque or BAD
- Instant Payment (payment on invoice due date)
- Real Time Cross Border Book Payment

### COVID Impact – Cash Conversion Cycle to Sales (%)

<table>
<thead>
<tr>
<th>Category</th>
<th>LTM '19</th>
<th>LTM '20</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>F&amp;B</td>
<td>10%</td>
<td>10%</td>
<td>0%</td>
</tr>
<tr>
<td>HPC</td>
<td>8%</td>
<td>7%</td>
<td>-1%</td>
</tr>
<tr>
<td>Alcohol</td>
<td>13%</td>
<td>14%</td>
<td>1%</td>
</tr>
<tr>
<td>Tobacco</td>
<td>24%</td>
<td>24%</td>
<td>0%</td>
</tr>
</tbody>
</table>

**Sources:** Capital IQ, Company Reports and Presentations, SCB Analysis

**Assumptions:** Please see slide 25 ‘Appendix: Criteria, Definitions & Assumptions’ for further details

**Notes:** (1) In some instances, receivable and/or payable balances include other assets or liabilities as more granular data was not available as part of quarterly filings. Additionally, two corporates from our sample have been adjusted in line with FY2019 results due to data limitations.
Portfolio Reshaping
Trends, Drivers and Enablers of future value

**Consumption**
- Health & Sustainability Conscious
  - Global pandemic tragedy triggered consumers to rethink impact of consumption decisions
- Prioritise Value & Essentials
  - Lower consumer confidence whilst trajectory of economy recovery remains unclear

**Channel**
- E-commerce
  - Lockdowns triggered accelerated acceptance of purchasing via online channels
- Last Mile Delivery Capabilities
  - Speed & reliability are key aspects of customer satisfaction in e-commerce

**Supply Chain**
- Upstream Integration
  - Integration with critical suppliers to increase long-term resilience in light of acute disruptions
- Downstream Partnerships
  - New ways of engagement required to capture the up-tick in e-commerce

**Innovation & Technology**
- Customer Experience via Digital
  - Tailoring customer experience for products & services through digital media
- Digital, Data & Infrastructure
  - Greater visibility and insights required to enable faster, reliable and more precise decision making

**Incubator**
- Which specialises in cultivating & accelerating start-ups or smaller brands to realise their true potential

**Crowdsourcing**
- Leveraging ideas generated or resource provided by ordinary customers or online communities

**Renovation**
- Transforming existing products or services to help them stay relevant in an evolving environment

**Balance Sheet Flexibility**
- Ensure sufficient headroom to fund the investments required

## Key Questions For CFOs

<table>
<thead>
<tr>
<th>Question</th>
</tr>
</thead>
<tbody>
<tr>
<td>How can I expand my portfolio to make the business more resilient?</td>
</tr>
<tr>
<td>Which acquisition targets (e.g. challenger brands) provide strong synergies / growth prospects?</td>
</tr>
<tr>
<td>What investments are required to grow my e-commerce and last mile capabilities?</td>
</tr>
<tr>
<td>Has the pandemic created an opportunity to acquire key suppliers?</td>
</tr>
<tr>
<td>Which partnerships can help strengthen my downstream presence?</td>
</tr>
<tr>
<td>What technology capabilities are required and how should these be acquired (R&amp;D vs. M&amp;A)?</td>
</tr>
</tbody>
</table>

**Sources:** SCB Analysis, Company News and Presentations, McKinsey, BCG, Deloitte, PwC
## Key Contacts

### Financing Solutions & Advisory

<table>
<thead>
<tr>
<th>Name</th>
<th>Position</th>
<th>Tel</th>
<th>Email</th>
</tr>
</thead>
<tbody>
<tr>
<td>Shoaib Yaqub</td>
<td>Global Head</td>
<td>+44 207 885 6723</td>
<td><a href="mailto:Shoaib.Yaqub@sc.com">Shoaib.Yaqub@sc.com</a></td>
</tr>
<tr>
<td>Raza Piracha</td>
<td>Director</td>
<td>+44 207 885 5761</td>
<td><a href="mailto:Raza.Piracha@sc.com">Raza.Piracha@sc.com</a></td>
</tr>
<tr>
<td>Carolyn Liao</td>
<td>Associate Director</td>
<td>+44 207 885 8529</td>
<td><a href="mailto:Carolyn.Liao@sc.com">Carolyn.Liao@sc.com</a></td>
</tr>
</tbody>
</table>

### Client Coverage

<table>
<thead>
<tr>
<th>Name</th>
<th>Position</th>
<th>Tel</th>
<th>Email</th>
</tr>
</thead>
<tbody>
<tr>
<td>Robert Newell</td>
<td>Managing Director</td>
<td>+44 207 885 2281</td>
<td><a href="mailto:Robert.Newell@sc.com">Robert.Newell@sc.com</a></td>
</tr>
<tr>
<td>Pontus Davidson</td>
<td>Executive Director</td>
<td>+46 845 102 18</td>
<td><a href="mailto:Pontus.Davidson@sc.com">Pontus.Davidson@sc.com</a></td>
</tr>
<tr>
<td>Kathleen Alpguner</td>
<td>Director</td>
<td>+44 207 885 8768</td>
<td><a href="mailto:Kathleen.Alpguner@sc.com">Kathleen.Alpguner@sc.com</a></td>
</tr>
<tr>
<td>Maximilien De Dieuleveult</td>
<td>Executive Director</td>
<td>+331 5375 8316</td>
<td><a href="mailto:Maximilien.Dedieuleveult@sc.com">Maximilien.Dedieuleveult@sc.com</a></td>
</tr>
<tr>
<td>Daniel Maas</td>
<td>Origination Banker</td>
<td>+49 69 770 750 377</td>
<td><a href="mailto:Daniel.Maas@sc.com">Daniel.Maas@sc.com</a></td>
</tr>
</tbody>
</table>
1) Supplementary Analysis

Appendix
Splitting the Components of TSR

Dividend yield alone is unlikely to satisfy investors across the board

- Unsurprisingly, volatility in average annual share price growth has undermined TSR. Whilst trajectory had improved in recent years for most, COVID-19 may stifle this momentum for corporates exposed to discretionary products or disrupted channels, such as Beauty and Alcohol, or those undergoing structural change like Tobacco.
- FMCG has historically relied on restricting cash returns to investors at times of stress. Whilst cash dividends returns have been broadly stable, with variations driven by the Global Financial Crisis (GFC), share buybacks have been considered a relatively flexible return paid out of surplus capital.
- Dividend yield will still play an important role, particularly where recovery is gradual as this represents the main return for equity investors. However, CFOs across all sub-sectors will be expected to walk a tight-rope between protecting cash returns and investing in growth plays to drive long-term TSR value.

### Annual Average Share Price Growth

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>GFC</td>
<td>80%</td>
<td>60%</td>
<td>40%</td>
<td>20%</td>
<td>0%</td>
<td>-20%</td>
<td>-40%</td>
<td>-60%</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Dividend Return

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>GFC</td>
<td>7%</td>
<td>6%</td>
<td>5%</td>
<td>4%</td>
<td>3%</td>
<td>2%</td>
<td>1%</td>
<td>0%</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Share Buyback Return

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>GFC</td>
<td>7%</td>
<td>6%</td>
<td>5%</td>
<td>4%</td>
<td>3%</td>
<td>2%</td>
<td>1%</td>
<td>0%</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Sources:** Capital IQ, Company Reports and Presentations, SCB Analysis

**Assumptions:** Please see slide 25 ‘Appendix: Criteria, Definitions & Assumptions’ for further details.
2) Assumptions & Criteria

Appendix
Criteria, Definitions & Assumptions

Criteria

• **S&P 1200**: Based on 728 companies across 17 sectors from the S&P Global 1200 Index filtered for Market Capitalisation greater than USD10bn as at the latest full year financial reporting date. Analysis excludes Financial Services, Real Estate and Insurance sectors, as well as a few corporates with limited financial data during the period of analysis.

• Trends were based on average of individual corporate’s ratio.

• **Sources of Financial Information**: Company Reports & Presentations, Capital IQ and SCB Analysis.

• Financials are reported in USD based on historical exchange rates from Capital IQ.

Definitions

• **Cash Dividend Return** = (Common & Preferred Stock Dividends + Special Dividends) / Opening Market Capitalisation (90-Days Averaged)

• **Share Buyback Return** = Repurchase of Common Stock / Opening Market Capitalisation (90-Days Averaged)

• **Share Price Return** = Year-End Share Price (90-Days Averaged) / Year-Opening Share Price (90-Days Averaged)

• **Total Shareholder Returns** = Cash Dividend Return + Share Buyback Return + Share Price Return

• **Leverage** = Net Debt / EBITDA

• **Days Sales Outstanding (DSO)** = \([[(\text{Trade Receivables Beginning of Year} + \text{Trade Receivables End of Year}) / 2] / \text{Sales}] \times 365\)

• **Days Inventories Outstanding (DIO)** = \([(\text{Inventories Beginning of Year} + \text{Inventories End of Year}) / 2] / \text{Sales}] \times 365\)

• **Days Payables Outstanding (DPO)** = \([(\text{Trade Payables Beginning of Year} + \text{Trade Payables End of Year}) / 2] / \text{Sales}] \times 365\)

• **Cash Conversion Cycle (CCC)** = DSO + DIO – DPO

Assumptions

• Our review of cross-sector indebtedness includes company reported debt over time which has been muddied by the recent adoption of IFRS-16 and the optionality for corporates to choose between the full or modified retrospective approaches. Our estimates are based on company reported debt numbers to provide an indicative view of the overall trajectory of sector indebtedness over time.

• Where corporates have ‘net cash leverage’ or ‘negative EBITDA’ positions, we have taken ‘zero’ for our average calculations.

• For the sake of consistency, we have removed relevant data for our calculations for corporates with data limitations in corresponding periods as follows: two instances where cash flow data is not available in 2004; one instances where cash flow data is not available in 2019; instances where dividends or buybacks were paid prior to public listing which affects around 10% of our sample of corporates.
## Sector Classifications

1. **Consumer Durables**  
   - Consumer Electronics, Homebuilding, and Leisure Products

2. **Hotels & Leisure**  
   - Restaurants, Casinos and Gaming, Hotels, Resorts and Cruise Lines, and Leisure Facilities

3. **Metals & Mining**  
   - Diversified Metals and Mining, Steel, Gold, Copper, and Silver

4. **Non-Food Retail**  
   - E-Commerce, Home Improvement, Apparel, Accessories, Luxury Goods, General, Automotive, Electronics Retail, Department Stores etc

5. **Oil & Gas**  
   - Integrated Oil and Gas, Exploration and Production, Storage and Transportation, Refining and Marketing, and Equipment and Services

6. **Pharma & Health**  
   - Pharmaceuticals, Health Care, Biotechnology, Life Sciences, Related Services and Facilities, Supplies, Distributors, and Technology

7. **Tech**  
   - Systems Software, Hardware, Data Processing and Outsourced Services, IT Consulting, Semiconductor, Related Manufacturing, Internet Services and Infrastructure etc

8. **Telecoms & Media**  
   - Interactive Media and Services, Telecommunication, Movies and Entertainment, Cable and Satellite, Broadcasting, Advertising, and Alternative Carriers

9. **Utilities**  
   - Electric Utilities, Multi-Utilities, Gas Utilities, Water Utilities, and Independent Power Producers and Energy Traders

10. **FMCG2**  
    - F&B (Packaged Foods and Meats, Soft Drinks, and Agricultural Products); HPC (Household Products and Personal Products); Alcohol (Brewers, Distillers and Vintners); Tobacco

### FMCG Sub-Sector Constituents

<table>
<thead>
<tr>
<th>Food &amp; Beverage</th>
<th>Household &amp; Personal Care</th>
<th>Alcohol</th>
<th>Tobacco</th>
</tr>
</thead>
</table>
| Meiiji Holdings Co., Ltd.  
Yakult Honsha Co., Ltd.  
Fomento Económico Mexicano, S.A.B. de C.V.  
Uni-President Enterprises Corp.  
Nestlé S.A.  
The Coca-Cola Company  
PepsiCo, Inc.  
Mowi ASA  
Mondelez International, Inc.  
Monster Beverage Corporation  
The Kraft Heinz Company  
General Mills, Inc.  
Danone S.A.  
The Hershey Company  
Hormel Foods Corporation  
McCormick & Company, Incorporated  
Kellogg Company  
Tyson Foods, Inc.  
Kerry Group plc  
Conagra Brands, Inc.  | Chocoladefabriken Lindt & Sprüngli AG  
Campbell Soup Company  
Associated British Foods plc  
Saputo Inc.  
The J. M. Smucker Company  
Lamb Weston Holdings, Inc.  
Kao Corporation  
Unicharm Corporation  
Shiseido Company, Limited  
The Procter & Gamble Company  
Essity AB (publ)  
L’Oréal S.A.  
The Unilever Group  
The Estée Lauder Companies Inc.  
Colgate-Palmolive Company  
Reckitt Benckiser Group plc  
Kimberly-Clark Corporation  
Henkel AG & Co. KGaA  
The Clorox Company  
Church & Dwight Co., Inc.  | Beiersdorf Aktiengesellschaft  
Kirin Holdings Company, Limited  
Asahi Group Holdings, Ltd.  
Ambev S.A.  
Carlsberg A/S  
Anheuser-Busch InBev SA/NV  
Diageo plc  
Heineken N.V.  
Pernod Ricard SA  
Constellation Brands, Inc.  
Brown-Forman Corporation  
Heineken Holding N.V.  
Molson Coors Beverage Company  
KT&G Corporation  
Japan Tobacco Inc.  
Philip Morris International Inc.  
Altria Group, Inc.  
British American Tobacco p.l.c.  
Imperial Brands PLC |