

Evenlode Global Investment View

June 2021 – Consumer Trends Part 1: Plant-based foods



The commentary below applies to both the Evenlode Global Income and Evenlode Global Dividend portfolios.

At Evenlode we believe that it is vital for companies to adapt and change over time in order to stay relevant to their customers. The global coronavirus pandemic has caused acute shifts that have affected individuals and businesses alike, with office-based workers suddenly having to work and collaborate from home being a prime example. Whilst these issues tend to grab the headlines, other longer-term movements in consumer tastes and preferences have also continued to unfurl.

The consumer goods sector is an important one for the Evenlode Global Income portfolio, currently making up over a quarter of the fund across food, beverage, home and over-the-counter health care. As such, we take a great interest in emerging trends in consumer tastes. One of these is the growing demand for plant-based foods, which we'll examine in this investment view. Next month we will take a look at how consumer attitudes to alcohol are changing.

Society is increasing activity to address greenhouse gas emissions and sustainability has risen to the top of the mainstream agenda, with initiatives increasingly becoming law. Plant-based foods are made from ingredients wholly sourced from plants, and are free from meat, dairy and eggs. Animals are fundamentally inefficient as a food source compared to plants, meaning plant-based food uses fewer resources and is therefore more sustainableⁱ. When it comes to greenhouse gas emissions and climate change, much is made of the need to decarbonise electricity generation, transportation, and the construction, heating and cooling of buildings in order to fend off the worst predicted effects of climate change. However, cattle and other ruminants present another significant challenge through the release of methane into the atmosphere. For example, of food giant Nestle's total supply chain emissionsⁱⁱ of 91.9 million tonnes of carbon dioxide equivalent per year, 37% comes from dairy and livestockⁱⁱⁱ. In the absence of a major technical breakthrough, the only way to reduce these emissions will be to reduce the consumption of dairy-based products, which will require an increase in consumption of alternatives.

The plant-based food category has been gaining market share from traditional products for many years and the COVID-19 pandemic has seen a dramatic acceleration in growth. As the category grows, the more normalised it becomes, which further increases growth. Flexitarianism (a diet based mainly on plant-based foods with the occasional inclusion of meat) is key; most purchases of plant-based alternatives are also made alongside animal products. More innovative products aim to closely mimic the experience of cooking and eating animal products and products are now a world away from the poor-quality versions of a decade ago. In the most advanced form of mimicry, pure cuts (e.g. steak) are well on their way to being made from lab-based precision fermentation of cells^{iv}. Dubbed 'cultured meat,' these products are physically identical to normal meat and production generates much less emissions than traditional meat.

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Given the size of the global food market, the growth potential has attracted a large amount of investment. Until recently, the main drivers have been niche players growing from a small base, with a correspondingly niche set of customers. However, large companies are now entering the space, either directly or through partnerships, prompted by expanding consumer interest.

This will be an inflexion point, providing the required scale in production, distribution, research and marketing that will increase penetration and decrease prices dramatically. Direct substitute products (e.g. Beyond Meat burgers) are currently priced at a sizeable premium, but price parity is expected to be achieved in 2-3 years. The consumer base is also expanding through the general population as the category becomes normalised, with demand currently highest with younger consumers.

Operational scale is key to the food & beverage industry. Scale is required to increase consumer awareness, secure shelf space, ensure availability and develop innovative products, all while maintaining satisfactory profitability with competitive prices. Research, development and marketing spend is disproportionately important when launching a new category, especially one that challenges tradition.

Consumers are, to generalise, risk averse. Plant-based foods ask them to switch away from a fundamental, entrenched way of life to something that might feel quite radical. This is, psychologically speaking, a risky switch. Therefore, customers are more likely to stick with brands once they find a product they like and trust.

Our portfolio companies Unilever, Nestle and PepsiCo, are well placed to capture the long-term opportunities that plant-based foods present. All have the key competitive advantages required to succeed in this category over time: operational scale, the ability to invest behind innovation and portfolios of world class brands and all three are investing in the development of innovative products of the future.

Nestle have recently launched plant-based brands Wunda, Garden Gourmet and Sweet Earth, along with other products under existing brands. They recently launched a vegan version of the ubiquitous Kit Kat, meaning environmentally conscious consumers can now 'Have a break' along with their non-vegan colleagues. Improving the health profile of their portfolio is also target, with a recent internal report admitting that there is work to be done in this area. Plant-based food is also one of the key growth priorities for Unilever, as part of their 'Future Foods' plan. They are targeting €1bn of revenue from plant-based meat and dairy alternatives by 2025-2027^v (c2% of 2020 revenue), through a mix of existing household names and new brands. PepsiCo have already partnered with Beyond Meat, expecting to launch new products later this year.

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An attractive feature of the globally diversified food majors is their ability to address emerging global markets across different product categories. Emerging markets are currently relatively underinvested when it comes to plant-based foods, but companies are recognising the opportunity. Tailoring the offering to local cuisine is important, but there is also high demand for ‘western’ products, such as beef burgers. Lactose intolerance is common in Asia, some religions discourage the consumption of certain animal products (e.g. Hinduism and Buddhism), and traditional protein alternatives like tofu, tempeh and seitan have been staples for centuries in some regions.

Plant-based food is but one example that demonstrates the importance of investing in quality companies for the long-term. Our focus on asset-light, cash generative companies with strong, enduring competitive advantages means that our portfolio companies can use their resources to manage the risks of ever-changing environments while capturing the opportunities that such change presents.

“The only constant in life is change.” - Heraclitus c. 535 - 475 BC.

Rob Strachan, Ben Peters, Chris Elliott and the Evenlode team

23rd June 2021

Please note, these views represent the opinions of the Evenlode Team as of 23rd June 2021 and do not constitute investment advice.

Past performance is not a reliable indicator of future results. The value of investments can go down as well as up, and investors may not get back the money they invested. Current forecasts provided for transparency purposes, are subject to change and are not guaranteed.

ⁱ Our World In Data, <https://ourworldindata.org/environmental-impacts-of-food>

ⁱⁱ The total of scope 1, 2 and 3 emissions in the jargon

ⁱⁱⁱ Source: Nestle’s Net Zero Roadmap, December 2020, <https://www.nestle.com/sites/default/files/2020-12/nestle-net-zero-roadmap-en.pdf>

^{iv} The Guardian, May 2021, <https://www.theguardian.com/environment/2021/may/11/lab-grown-meat-companies-swallow-record-investments>

^v <https://www.unilever.com/news/press-releases/2020/unilever-sets-bold-new-future-foods-ambition.html>