



## 2 Reasons Why Consumer Staples Looks Overvalued

### Description

The consumer staples sector is less economically sensitive than the rest of the market, as companies within this sector deal with consumers' essential needs. Stuff that we have to buy regardless of the economy, such as food and drugs. Not surprisingly, this sector has performed extremely well over the last 2 years, as economic uncertainty has been high and investors have been looking for a "defensive" place to hide. The **consumer staples index** (^GSPTTCS) of the **S&P/TSX Composite** has increased almost 50% over the last 2 years, and the top 10 stocks in the index are trading at an average trailing P/E of over 18 times. Here are two reasons why I think this performance has left the space overvalued:

#### 1. Intensifying Competition Becoming Evident in Results

U.S. retailers, such as **Walmart** and **Target** have intensified their push into the Canadian market. And we're not just talking the market for merchandise. These retailers are encroaching on the food business as well as the pharmacy business. With this, we are seeing price competition and eroding profits. **Loblaw's** ([TSX: L](#)) third quarter profit declined a whopping 29% due to reduced margins as the company attempts to win customers in an increasingly competitive marketplace. Loblaw is trading at a P/E ratio of over 18 times. Given the headwinds that this company is facing, this valuation appears very rich. **Metro** ([TSX: MRU](#)) is trading at a trailing P/E of 8 times, but this company is facing extremely rough times. Its latest quarter saw profit slide a shocking 40%.

#### 2. Uncertainty Due to Changing Consumer Food Preferences

There are definitely those in the food industry that are reaping the rewards of this change in consumer preferences. **Whole Foods** (NYSE: WFM) is the best example of one such company, who is tailoring to the more health conscious consumer. Although the company's latest results were below analyst expectations, profit increased 7% and revenue increased over 2%. But for many food companies and grocery stores, this shift in consumer preferences is presenting major challenges and risks.

**George Weston** ([TSX: WN](#)) faces a double threat because of this. The company's most significant asset is Loblaw, but Weston is also one of the country's biggest bakers. The competitive angle is hitting Loblaw, while the shift in consumer preferences has negatively impacted the bakery business

(gluten free products). Weston's posted a lower third quarter that was \$0.07 below analyst estimates and 6% lower than last year's third quarter.

### **Bottom Line**

Given the headwinds that this sector is facing and the corresponding hit to profitability they have caused, it seems clear to me that valuations are too high and should be expected to fall over time. Though many feel that consumer staples offer a way to play defense, there may be other areas of the market that are showing more value at this time.

### **CATEGORY**

1. Investing

### **TICKERS GLOBAL**

1. TSX:L (Loblaw Companies Limited)
2. TSX:MRU (Metro Inc.)

### **Category**

1. Investing

### **Date**

2025/08/27

### **Date Created**

2013/12/02

### **Author**

karenjennifer

default watermark

default watermark