2 Reasons Grocers Will Enter 2018 on a Sour Note

Description

In an early December article, I'd discussed why Canadian grocery stocks will likely be under pressure as we head into 2018. Some of the headwinds facing Canadian grocery companies in 2018 include the retail challenge from **Amazon.com, Inc.** after its acquisition of **Whole Foods Market, Inc.** as well as the minimum wage hike that will affect companies with large footprints in Ontario.

Today we're going to look at two developments that may work to sour investor sentiment heading into 2018.

Bread price-fixing controversy

On December 19, **Loblaw Companies Ltd.** (TSX:L) and its parent company, **George Weston Limited**, revealed that employees had participated in an industry-wide bread price-fixing scheme. The stock price for Loblaw was mostly unaffected, as both companies were granted legal immunity in alerting the competition watchdog. The arrangement allegedly spanned from 2001 to 2015.

On its part, Loblaw is offering eligible customers a $25 gift card to use at its locations. The company will book a $75 million to $150 million quarterly charge for the program.

Metro Inc. (TSX:MRU) and Sobeys, a subsidiary of **Empire Company Ltd.** (TSX:EMP.A), are both co-operating fully. Based on its own internal investigation, Metro stated that it found no evidence of any violation of *The Competition Act.* Sobeys has also denied any wrongdoing.

The story arrives at an inopportune time for Canadian grocery companies, as rising food prices have perturbed some consumers in 2017. The changing retail environment makes the reputational damage sustained even worse over the long term.

Food price report shows drive to food service

In December, Dalhousie University and the University of Guelph published the *Canada Food Price Report* forecast for 2018. I'd covered the marginal rise in meat and seafood prices in a recent article. Much of the report's data could impact grocers in the New Year.

Prices for vegetables are expected to increase between 4% and 6% in 2018 due to dry weather conditions in North America, while fruits are projected to rise between 1% to 3%. Broadly, food prices are forecast to increase between 1% and 3%. The report also detailed the shift in the retail environment. The annual food expense for a Canadian family of four is projected to rise by $348 in 2018.

"The recent purchase of Whole Foods by Amazon is having a significant impact on the Canadian food retail sector," said Simon Somogyi, co-author of the report. "The other major food retailers such as Loblaw, Sobeys and Metro are now changing their business models, particularly in how they sell to consumers, including online offerings."

Perhaps the most interesting finding was the increased spending on restaurants by Canadian families. The report estimated that Canadian households spend almost 30% of their food budget on food service, the highest proportion in history. Price increases at restaurants are also expected to rise between 4% and 6%.

It remains to be seen whether or not grocery retail will be subjected to the same disruptive forces that have changed the face of retail in clothing and big-box stores.

CATEGORY

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

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