INTUITION

15 MARCH 2024

Mondelez - Life is Sweet

"My mama always said, 'Life was like a box of chocolates; you never know what you're going to get.'" This iconic quote from the beloved movie and character, Forrest Gump, serves as a reflection on the unpredictable nature of life. While some aspects of life may remain unknown, there are some I would argue are known, tried and true.

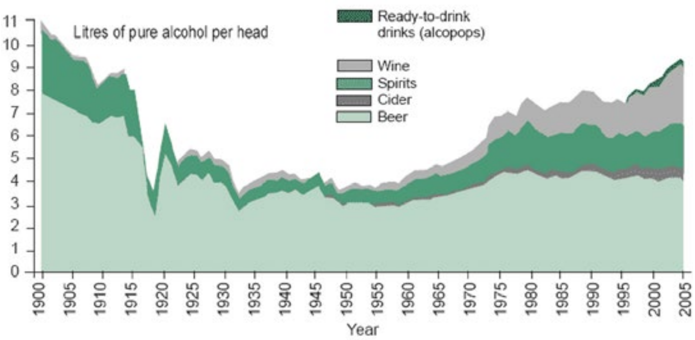
Lebogang Malatji

GLP-1 agonists, initially designed for treating Type 2 diabetes, have been unexpectedly found to discourage food intake, thereby aiding in weight loss. This discovery has raised concerns within the food sector regarding its potential impact on valuations. Reflecting on historical trends, over 200 years ago in Great Britain, a period marked by widespread alcohol consumption was evident. Thora Hands, in her book "Drinking in Victorian & Edwardian Britain," highlights the growing societal concerns regarding alcohol, as evidenced by various inquiries by committees such as the Select Committee on Habitual Drunkards and the Select Committee on Intemperance in 1877. During this period, a notable trend emerged. The consumption of beer, the primary alcoholic beverage, declined significantly from 30 gallons per capita to below 20 gallons. This decline was obviously attributed to efforts from religious societies and social movements, as some historians argue. Additionally, as income per capita rose and alternative beverages gained popularity, beer consumption decreased further. However, from the 1850s onwards, there was a resurgence in the consumption of beer, spirits, and wines, coinciding with the increased popularity of tea as a substitute beverage. The temperance movement gained significant traction from 1900 to 1915, but its impact was short-lived due to the outbreak of wars in the early 20th century, and since then the upward trend in alcohol consumption has continued. During the temperance movement in 1824, John Cadbury, a devoutly religious individual also embarked on a mission to discourage alcohol consumption. His solution was the creation of drinking chocolate. Armed with basic tools—a mortar and pestle—he began selling his concoction to locals in Birmingham. Through continuous taste and packaging innovations over the century, Cadbury's venture eventually evolved into a major part of Mondelez when Kraft Foods acquired Cadbury in 2010 for $19 billion. Kraft then subsequently split into two companies, Mondelez being one of them.

SPEED READ

- **A study of alcohol consumption in the 1800s and early 1900s highlights an interesting trend, which has relevance today as investors grapple with a new threat – weight loss drugs!**
- **The current macroeconomic landscape mirrors in certain aspects the turbulent era of the 1970s.**
- **The Q4 results showed volume growth in Latin America (+2.1%) and Europe (+3.3%) despite aggressive price increases in those geographies. But it was volume declines of 5% in North America that caught the market's attention.**
- **Fortunately, there is no cure for being human. We love to reward ourselves, with snacks and chocolates a perennial favourite.**

UK PER CAPITA ALCOHOL CONSUMPTION



Source: Statistical handbook 2007 (British Beer and Pub Association, 2007)

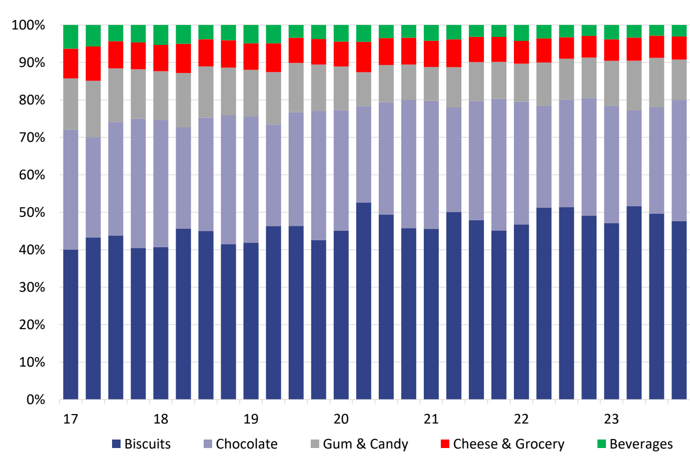
After initial declines in the early 1900s, consumption of alcohol has trended upwards ever since.

Within the Mondelez portfolio lie several iconic brands, each with a rich history and a tale of organic growth spanning the globe. The revenue mix encompasses various business segments: Biscuits (48%), showcasing classics like Oreo and LU biscuits cherished by French households; Chocolates (32%), featuring Cadbury, Milka, and the Swiss chocolate excellence of Toblerone; Gum and Candy (11%), focusing on developing markets through brands like Stride in China; Cheese & Grocery division (6%), including staples Philadelphia cream cheese, Belvita, and Ritz; and lastly Beverages (3%), with global brands like Tang and Clif Bar. Revenue streams are also geographically diverse, reflecting both the origin of the products and their expanding presence in new markets. Mature markets in Europe (38.0%) and North America (30%) contribute over half of the revenues. The AMEA region (19%) and Latin America (14%) exhibit promising growth. Management has identified that long-term growth potential will be in niche products within these segments, with Africa emerging as a significant growth driver over the next decade, which is why locally listed AVI was considered a potential acquisition target two years ago. Unfortunately, and maybe unsurprising, in their recent investor engagements, Dirk Van De Put, the CEO of Mondelez, noted that South Africa is slightly less interesting than other African markets. Increasingly, the focus is on Brazil, India, China, and Mexico as growth drivers. The company's long-term vision (2030) targets organic sales growth of 5%, accompanied by continued investments in biscuits and chocolate to fortify their competitive advantage. In the short term, volume driven growth may prove overly ambitious given the prevailing market conditions.

The current macroeconomic landscape mirrors in certain aspects the turbulent era of the 1970s. In West Africa, crop failures caused by dry and scorching weather might evoke memories of similar agricultural setbacks in 1977. Back then, as noted by the New York Times, cocoa prices surged by 50%, prompting chocolate bar manufacturer Hershey to announce a 33% increase in wholesale prices for some of their products. During the 1970s, sugar prices peaked. Fortunately, when cocoa prices skyrocketed, sugar prices plummeted by 90%. This delicate balance allowed them to weather the storm, benefiting manufacturers with a diversified mix. However, currently, sugar prices have only marginally pulled back from highs in December. The International Sugar Organization has increased its forecast of sugar deficit from 335kt to 689kt. This caused by increased demand and worsening supply issues, which might not offer a buffer as it did in the 1970s. On the consumer side, the 1970s witnessed the infamous "Great Inflation." The Federal Reserve grappled with soaring inflation rates, pushing interest rates to nearly 20% to rein it in. The Fed is currently contending with similar inflationary shocks, and the results of which have left interest rates across developed markets at a high level. Atlanta Fed

"During the 1970s, sugar prices peaked. Fortunately, when cocoa prices skyrocketed, sugar prices plummeted by 90%."

MONDELEZ: CONTRIBUTION TO REVENUE



Biscuits is the largest segment of the Group, contributing $4 billion in revenues, nearly 50% of the total. Together with Chocolate, these two divisions account for 80% of revenues. This is a company for anyone with a sweet tooth.

COCOA AND SUGAR PRICES

Whilst sugar prices have declined from their peaks late last year, cocoa prices have sky-rocketed due to crop failures in key regions. This mirrors to some extent the conditions in the 1970s, although sugar declines are likely insufficient to offset the impact of higher cocoa prices. Expect your next treat to cost a little more.

CADBURY’S CHOCOLATES

Modelez’s Cadbury’s brand includes some of South Africa’s best loved chocolates including Crunchie and Lunch Bar.

President Bostic in recent comments stated that “I need to see more progress to feel fully confident that inflation is on a sure path of averaging 2% over time” Moving inflation within their targeted range will need a series of positive data points. This could leave interest rates higher for much longer than initially anticipated, affecting consumption spending.

The tough macro environment was reflected in some of Mondelez’s numbers. The Q4 results showed volume growth in Latin America (+2.1%) and Europe (+3.3%) despite aggressive price increases of 26.5% and 8.3% respectively. However, it is the volume declines in North America (-5.5%) and AMEA (-0.5%) that portend what investors might have to grapple with in 2024. Investors are concerned that the volume declines in North America are due to increased usage of the new weight-loss drugs and might impact other regions as drugs are rolled out globally. However, management pointed out that the weak North America performance was linked to poor performance in the biscuits category and other minor one-off events. Aggressive marketing campaigns have been rolled out to arrest the decline. Even with that, pricing is expected to underpin revenue growth, so be prepared to pay a little extra for that impulse treat. Ultimately, gross margins were stable at around 38% - suggesting that management is getting the balance right between inflationary cost pressures and price increases. But there is always room for improvement. In the past Cadbury chocolate bars were sold as unwrapped blocks, then broken down and sold individually as penny bars. Today, Mondelez has been right sizing their products and coming up with innovative pack sizes to stabilize volumes. Management expects volumes to be mildly positive in 2024, which would provide a much-needed sentiment boost given the drug concerns.

Sentiment within the sector is sobering as many companies grapple with declining volumes, shrinking margins, and lowered earnings expectations, in part due to consumer pressure from higher interest rates. However, amid these challenges, Mondelez shines as a company that consistently surpasses earnings expectations. Though management is not prioritizing debt repayment, the balance sheet remains sound, with Net Debt / EDITDA Ratio at 2.6x (vs 5x just two years ago) and supported by a healthy cash balance. While short-term concerns may centre on volume fluctuations, in the long run, it is the underlying narrative that truly drives price movements. While it is conceivable to view GLP-1 drugs as a potential long-term threat, it is important to bear in mind, as history has pointed out, that there is no active cure for being human. We “reward” ourselves as often as possible - snacks and chocolate fall firmly into that category and have proved defensive for generations because they are also affordable and easily available on impulse. The Lindy effect offers some reassurance for the food staples and confectionery companies when it comes to modelling human behaviour — “the older something is, the longer it’s likely to be around in the future.”

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TOTAL RETURN VS PEERS

Investors will agree that current market commentary is dominated by tech and AI – to the detriment of everything else. It is therefore refreshing to note that old habits die hard – snacking habits, that is. Over the past three years, Mondelez has delivered a similar total return to the S&P 500, proving that solid investments come in many shapes and sizes.

By the time of our next Insight seminar, our election will be out of the way. We will take the opportunity to review market performance for the first five months of the year, and look ahead to what the second half might hold.

Please note that we will be hosting both a morning and evening presentation in Cape Town. The venues will be communicated once finalised.

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Topic:	**Taking Stock: Mid Year Update**
Natal Midlands	
Date:	20 June, 2024
Venue:	Oasis Conference Centre, 72 Main Road, Howick
Morning Time:	10am for 10.30am
Evening Time:	5.30pm for 6pm
Johannesburg	
Date:	11 June, 2024
Venue:	Rosebank Union Church, Cnr William Nichol and St Andrews Road, Hurlingham
Time:	7am for 7.30am
Cape Town	
Date:	13 June, 2024
Venue:	To be confirmed
Time:	5.30pm for 6pm

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