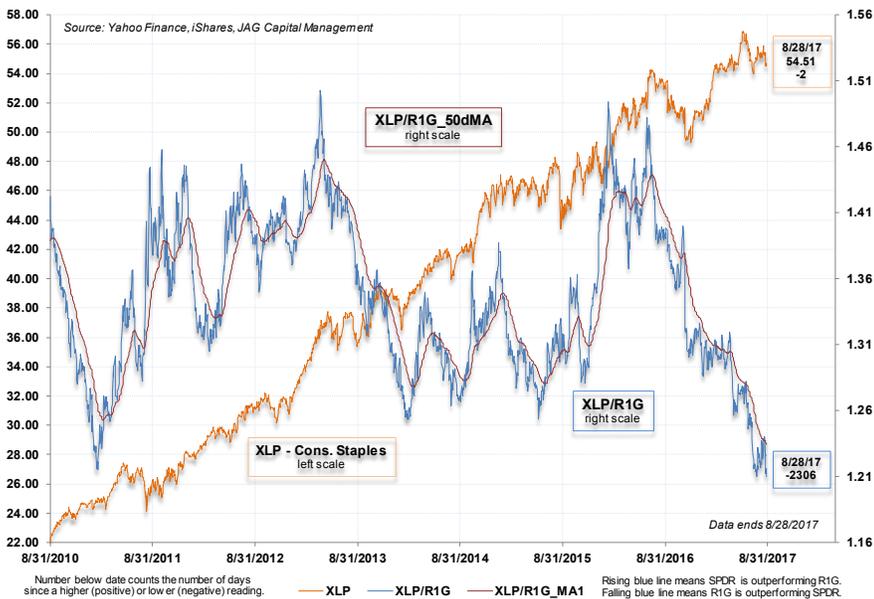


## Timely Insights from JAG's Research Team

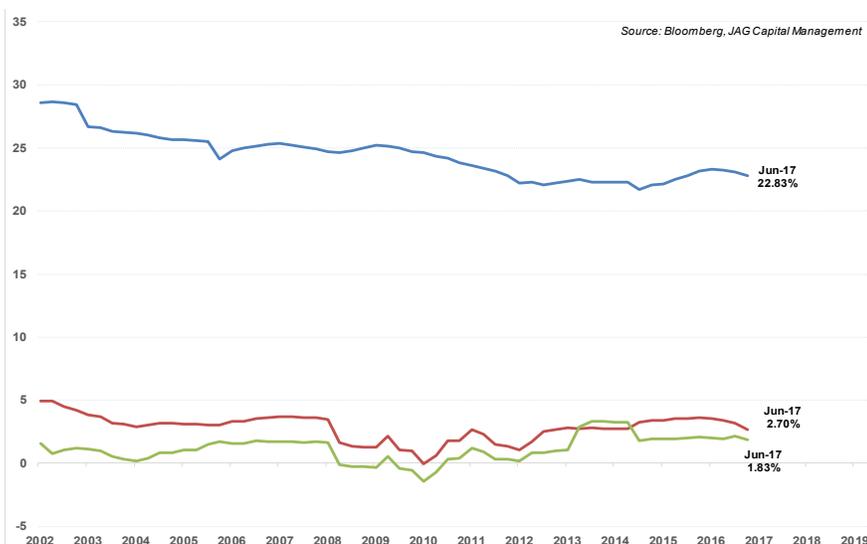
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### XLP vs. XLP / Russell 1000 Growth (R1G) with Moving Average



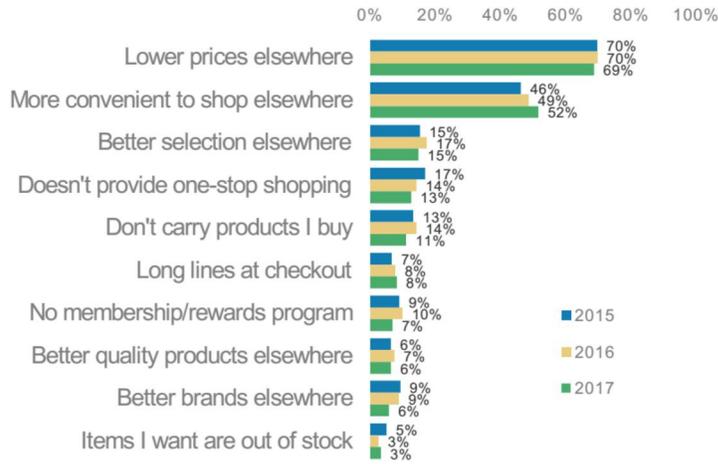
The blue line on this chart depicts the relative performance of the XLP (Consumer Staples Select Sector SPDR ETF) compared to the Russell 1000 Growth Index. The Staples sector has traditionally been popular with risk-averse equity investors, to the point that it is sometimes viewed as a comparative “safe” haven in the stock market. After all, many of the constituents boast solid balance sheets, pay competitive dividends, and sell well-known branded essentials to consumers. When the blue line is going up, Consumer Staples stocks are outperforming the index. When the blue line turns down, the opposite is true. Note that the relative performance of Consumer Staples has been horrid for much of the past year. In fact, the sector recently hit a 2,306 trading-day low in relative strength versus the index. Given that there are roughly 250 trading days each year, this means that Consumer Staples are currently enduring their worst spate of underperformance in almost 10 years (!).

### Gross Margin (blue line), Operating Margin (red line), Net Margin (green line) for the S&P 1500 Food Retailing Sub-Industry



The S&P 1500 Food Retailing Sub-Industry is ground zero for the troubled Consumer Staples sector. Note the gentle but persistent downtrend in gross margin for this group since 2005 – from almost 30% down to the low-20%’s this year. Part of this is probably due to the entry of Walmart into the grocery business over roughly the same timeframe. As the original big-box disruptor in retail, Walmart has spent several decades aggressively squeezing margins and offering low prices to consumers. But now there is an even more aggressive disruptor entering the food retailing business. Amazon’s just-completed acquisition of Whole Foods is sending shivers down the spines of grocers everywhere – including Walmart. (Note: we own positions in both Amazon and Walmart in our managed portfolios).

## Barriers of Shopping at Whole Foods Market



Source: AlphaWise, Morgan Stanley Research

Prior to being acquired by Amazon, Whole Foods had been struggling for several years. The stock had traded as high as \$107/share back in 2013, before beginning a long slide south that finally ended with Amazon's recent deal to buy them out at only \$42/share. This chart highlights some of the main reasons Whole Foods fell on hard times. From the perspective of many consumers, Whole Foods' prices were just too high, especially once competing grocers began offering organic goods at lower prices (the popularized nickname for the stores became "Whole Paycheck"). We think Amazon plans to counter consumers' price perceptions aggressively with a "new" Whole Foods business model that emphasizes high quality food at affordable prices.

## Prices for Selected Items at Whole Foods

Product	Thurs., Aug. 24	Mon., Aug. 28
Whole Trade Organic Bananas	99 cents per pound	69 cents
Whole Trade Bananas	79 cents per pound	49 cents
Responsibly-Farmed Atlantic Salmon Filet	\$14.99 per pound	\$9.99
Responsibly-Farmed Tilapia	\$11.99 per pound	\$7.99
Organic Large Brown Eggs	\$4.29 per dozen	\$3.99
Animal-Welfare-Rated 85% Lean Ground Beef	\$6.99 per pound	\$4.99
Organic Avocados	\$2.79 each	\$1.99
Organic Baby Kale (packaged)	\$3.99 per package	\$3.49
Organic Baby Lettuce (packaged "Sweet Baby Lettuces")	\$3.99 per package	\$3.49
Creamy Almond Butter	\$7.99 per pound (1 jar)	\$6.99
Crunchy Almond Butter	\$7.99 per pound (1 jar)	\$6.99
Organic Gala Apples	\$2.99 per pound	\$1.99
Organic Fuji Apples	\$3.49 per pound	\$1.99
Organic Rotisserie Chicken	\$13.99 each	\$9.99
365 Everyday Value Organic Butter (salted and unsalted)	\$5.29 per pound (four sticks)	\$4.49

Amazon closed the deal for Whole Foods on Monday 8/28/17, and immediately slashed prices on a variety of common grocery items. This "before and after" price matrix has received wide coverage in a variety of media outlets, and we think it shows just how competitive Amazon is going to be with Whole Foods' new pricing strategy. As one example, consider the 29% price slash for Lean Ground Beef. According to the Bureau of Labor Statistics, the average price for Lean Ground Beef in July 2017 was approximately \$5.75/lb. By cutting their prices to \$4.99/lb., Amazon/Whole Foods appears to be undercutting the rest of the grocery industry on this key staple. Although Whole Foods' 468 locations currently generate only 1.2% of U.S. grocery sales, we think Amazon's maneuvers are likely to have broad ramifications for the entire industry.

## Disclosures

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9841 Clayton Road | St. Louis, MO 63124

**800.966.4596** [www.jagcapm.com](http://www.jagcapm.com)

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