

## Looking South for shelter from economic woes

**The promise of a higher quality of life draws many to the US, both legal and illegal immigrants, and it is argued that the US economy would become uncompetitive without the constant flow of cheap labour from south of the border.**

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Although the US still has a tremendous pull, there are very clear signs that Latin America in general (Brazil and Mexico now joined by a group of rapidly developing economies such as Argentina and Colombia) are increasingly standing on their own two feet and offering their own economic miracle. Growth across the region in 2011 would appear to be made of more solid foundations than in the past, meaning the balance of power does appear to be slowly shifting. For example, the Brazilian finance minister Guido Mantega recently stated "It's a big satisfaction for us that this time around the IMF comes to Brazil not to give us money like in the past but asking us to lend money to developed nations". The rapid pace of growth has seen a much broader range of companies across FMCG (Fast Moving Consumer Goods) looking to strengthen their position in Latin America or for those not already in the region looking to develop one quickly through acquisitions.

**INCOME GROWTH AND PURCHASING PARITY.** Looking at North and Latin America as a whole there are three distinct groups; the US, Mexico and Brazil, with Argentina perhaps a more recent arrival to the power structure. Traditionally, Mexico and Brazil represent the powerhouses of Latin America, with GDP per capita of US\$9,000 in Brazil and US\$8,000 in Mexico, the latter a clear US\$1,000 ahead of the regional average. As such, consumers in these countries continue to enjoy much higher purchasing parity than their peers in other territories, although this gap is narrowing as the likes of Argentina and Chile have enjoyed their own accelerated period of economic development over the past five years. Dollar income is crucial to market development across FMCG and to tissue and hygiene products in particular, but for Mexico and Brazil higher incomes mean that consumers can, for the most part, afford staple products. Subsequently, toilet paper, sanitary protection and nappies/diapers are all mainstream purchases and well within the grasp of the majority of consumers.

**TISSUE AND HYGIENE SALES.** The balance between tissue and hygiene sales is an interesting one, with toilet paper easily one of the most affordable products; consumers in the developing world tend to prefer basic products or commonly substitute these with other items, such as newspapers, rather than buying branded toilet paper. For this reason, per capita consumption, even in Mexico - the most "Americanised" of Latin American countries - is just a fraction of that found in the US. Mexicans consume a third less in volume per capita terms, with value spend less than half of their American counterparts, illustrating a large amount of substitution as well as a penchant for the cheapest products available.

At least in terms of tissue, the majority of territories which make up Latin America offer great potential for growth, especially amongst the burgeoning middle classes who are most likely to trade into or up through the tissue market. In Brazil for example, kitchen towels continue to perform well with middle income households as an aid for cooking, especially with fried foods.

**CAN POTENTIAL TURN INTO REALITY?** Although there is a great deal of potential in the Latin American market as a whole, it does provide significant challenges to manufacturers, inasmuch as the 500 million or so consumers in Latin America are widely dispersed and the retail environment is often far from developed. In 2011, the US market for tissue products of all types was worth US\$16.5 billion, compared to US\$8.5 in Latin America. Certainly, growth is forecast to be much more rapid south of the border, with a compound annual value growth rate expected to be around 14% over the medium term, with the US trailing at 3% or possibly lower, given current economic difficulties.

Also, the likely wider development of private label products in Canada and the US, which still lag behind the levels typically found in Western Europe, could well be a further barrier to value development. In 2010, the penetration for private label hit 20% by value in the US in 2010 whilst in Latin America this was just 4% compared to the 50%+ reported across most of Western Europe, illustrating the potential there still is for private label in the US market.

Certainly in the US development of private label - which is perhaps more in keeping with the age of austerity developed markets now find themselves in - could have a significant effect on value sales, as the position of brands is slowly undermined. Latin America is a different prospect, where in tissue the development of private label could have a significant influence on developing per capita consumption, with a product offer which is of reasonable quality and - most importantly - affordable. Private label appears to be a long term goal for the tissue industry in Latin America. Although supermarkets account for 60% of value sales, the vast majority of these outlets are not chained, which has significant implications for distribution. The use of wholesalers and middlemen ultimately undermines the price position of private label, meaning 'take off' will likely be delayed until retail distribution is sufficiently modernised.

**THE COMPETITIVE LANDSCAPE.** The fragmented nature of retailing, disparate populations and lower incomes in the region have an obvious and major influence on the competitive landscape in Latin America. This sees the top three manufacturers take a 50% value share of the tissue market, with the same figure closer to 80% in the US, illustrating the more compact and efficient distribution which exists north of the border. This difficult environment in Latin America sees local players such as Empresas, Santher Fabrica and Papeles all continuing to be significant players, with other household names such as Georgia Pacific and Procter & Gamble still largely absent. With strong growth forecast across the region, it would seem likely that acquisitions will take place especially in the most developed markets, where the retail structure is more conducive to the business practices of Western companies. Indeed, with the emphasis still likely to be on local distribution to a myriad of local retailers, the prospect of any company being able to set up in Latin American alone, and without acquisition, is very limited, especially for lower margin tissue products.

**HYGIENE OFFERS FURTHER RAPID GROWTH POTENTIAL.** While the tissue market looks likely to take some years to modernise in Latin America, the key growth over the last decade and for the foreseeable future has come from hygiene products. Demographically, Latin America has significant advantages over the US, with some 52 million babies reported in 2011, compared to just 22 million in the US. Similarly, Latin America has 195 million women aged 14-64 years, compared to 116 million in the US. By sheer weight of numbers, as well as complimentary income levels, which on average were US\$7,000, 2011 saw that sanitary protection and nappies/diapers product categories were both mainstream and affordable for the majority of consumers across Latin America. There is also evidence that personal care wipes (specifically baby wipes) are becoming commonly used amongst the urban middle classes. A combination of need, rising incomes and positive demographics saw the Latin American market for hygiene products top US\$16 billion in 2011, some way ahead of sales in North America which stood at US\$12.5 billion. Both sanitary protection and nappies/diapers saw very strong 12% compound annual value growth over the last five years, clearly overshadowing the 2% CAGR seen in the US across similar categories.

Growth is likely to be as strong if not stronger in Latin America, as income levels in second tier markets such as Argentina, Chile and Colombia continue to develop, encouraged by manufacturers keen to expand into the region. Significantly though, the higher margins offered by hygiene products have been a key motivator for expansion, something which has not been the case in the tissue category. To this end, the top four companies in Latin America all hail from the West with Kimberly-Clark, Procter & Gamble, Johnson & Johnson and SCA Group representing 70% of value sales in 2010, which is a comparable share to what the top four take in the US and in most other developed markets.

The key to the rapidly developing market is the presence of international players, although recently, local manufacturers have also looked to develop their position with Hypermarcas in particular, developing a significant position based on acquisition. But the key factor remains income levels; the best example of this has been the development of incontinence products.

**INCONTINENCE PRODUCTS BOOM HINTS AT MODERNITY.**

Typically US\$10,000 per capita income is a prerequisite for the retail sale of incontinence products to be affordable/accessible for the majority of consumers. Although the majority of Latin American countries lie some way behind this level, by 2015 Brazil, Mexico and Argentina are expected to have broken this barrier. With national health systems less developed than in other parts of the world such as Western Europe, the provision of healthcare for non-life threatening problems will be pushed back to the consumer. As a result, manufacturers are now

attempting to take advantage of a potential boom in sales across the continent. Whilst Hypermarcas is the only clear challenger to Kimberly-Clark's position, both SCA Group and Unicharm have been looking to strengthen their position in the region. Incontinence products are likely to be a key part of their strategy to help unlock the potential of this rapidly developing region with some 285 million over 65 year of age (compared to just 45 million north of the border) and a further 100 million will join these ranks over the course of the next decade.

A HISPANIC FUTURE? Latin America, both demographically and economically, is a rapidly developing region capable of being a true economic powerhouse over the coming decades. Critically, Latin America has none of the consumer cultural barriers which have made growth in other high potential territories such as India difficult to achieve. As for the US, economic difficulties and a prospective age of austerity are expected to hinder sales of tissue and hygiene. However, as essential items for the most part, manufacturers can rely on steady sales growth in accordance with further population growth. Interestingly, this population growth will stem largely from the North American Latino community, which already has grown into a significant socio-political force in US society, meaning that Hispanics will be grabbing the headlines both north and south of the border for some time to come. •

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