Dow Jones Newswires

FOCUS: As Recession Bites, Cos Turn To Pet Owners For Growth

12 August 2009 11:48 (16:48 GMT)

By Goran Mijuk and Anita Greil of DOW JONES NEWSWIRES

ZURICH (Dow Jones)--Companies making consumer products and pharmaceuticals are increasingly focusing on pet owners, who have shown themselves willing to spend more and more on their animals, despite the economic downturn.

The main beneficiaries are companies selling pet food. But the growing market for products targeted at pet owners is drawing increasing interest from players in sectors ranging from healthcare to insurance.

Reflecting the market's ability to shrug off the recession, Switzerland's Nestle SA (NESN.VX), one of the biggest producers of pet food, along with Mars Inc. of the U.S., Wednesday reported a 9.1% increase in sales to 6.4 billion Swiss francs ($5.9 billion) at its pet food division in the first half.

This compared with a 1.5% fall in Nestle's overall sales in the period. And despite the tough economic times, consumers weren't deterred by price hikes for pet food, which lifted the division's profit margin by 10 basis points to 12.4%.

"Growth in pet care remains resilient" across the globe, said Chief Financial Officer Jim Singh. "We're also rationalizing underperforming and mainstream products that are being replaced with products that are delivering improved nutritional benefits for pets," he said.

This strategy has paid off. Nestle's pet food division makes up roughly 12% of the company's overall sales, which reached 52.2 billion Swiss francs in the first half of 2009. Its key pet food brands include Alpo, Gourmet and Felix. Brands such as Purina and Friskies are among its fastest growing large brands, which Nestle terms "Billionaire Brands". Sales of both products have risen by more than 6% over the past six months.

Dog Chow, which saw sales growth of more than 16%, is Nestle's second-fastest-growing large product, outstripped only by coffee system Nespresso, which has growth rates of above 20%.

"Pet owners are renowned for spending the same amount on their pets whilst saving in other areas," said independent Switzerland-based food industry analyst and consultant James Amoroso.

This makes the business attractive in the economic downtrend, especially in the U.S., where customers tend to spend lavishly on their pets, whether on food, health care or luxury items.

Based on 2008 sales, industry body the American Pet Products Association lists among its top product trends toy gyms and cat spas. And according to the trade group, U.S. pet owners are unlikely to curb their spending during the downturn. It forecasts spending on pets to rise to $45.4 billion this year, from $43.2 billion in 2008.

This includes $17.4 billion for food and more than $22 billion for over-the-counter medicine and vet care, explaining why drugmakers are eager to gain a bigger share of the animal health market.

Sanofi-Aventis SA (SNY), a French pharmaceutical company, put $4 billion on the table last month to buy the 50% of animal health company Merial it didn't already own from U.S. peer Merck & Co. (MRK). The deal includes an option to buy the veterinary business of Schering-Plough (PGH) once the two U.S. firms complete their pending merger.

Sanofi Chief Executive Chris Viehbacher said sales at Merial had grown 50% over the past five years, to nearly $2.7 billion in 2008, while delivering an operating margin of close to 30% - a level of profitability only a handful of makers of human medicine can boast.

Viehbacher told analysts that sales of medicines for pets, including parasiticides that kill fleas and ticks, were less affected by the economic crisis than medicines for farm animals, such as vaccines and antibiotics.

In 2008, worldwide sales of animal health products increased at a healthy 7.3% pace to $19.2 billion, with pets by far the largest segment, Sanofi said in a presentation to detail its deal to buy the rest of Merial. Citing data from several research firms, Sanofi concluded the market will probably expand by around 4% a year until 2013.

And more deals could be in the making. Eli Lilly & Co. (LLY) Chief Executive John Lechleiter has also expressed interest in building up his company's animal-health business.

The bright outlook for pet products is also luring insurers into the market. Underdeveloped in some key countries, pet insurance offers more lucrative growth rates than traditional car and life insurance.

For example, Swiss property and casualty insurer Mobiliar earlier this year launched Switzerland's first pet insurance product in Switzerland.

Switzerland is considered one of the most lucrative markets for pet insurance in Europe, after the U.K., Germany, France and Sweden. Every third household in Switzerland owns a cat or a dog, putting the potential customer base around 1.8 million, said Stephan Guenther, product manager at MobiCasa, Mobiliar's household unit.

"Demand was very strong after the first few months and beat our expectations," he said. "The market hasn't been tackled by anyone before and we expect strong growth in the future."

And in the U.S., there is a huge untapped market, with only 0.3%, or around 800,000 animals, of all cats and dogs currently insured, according to Ohio-based insurer Embrace Pet Insurance. The company says the market has grown by 18% between 2003 and 2008.

In Europe, growth could be even stronger. According to market research company Datamonitor, the U.K. pet insurance market will probably grow to around GBP700 million in 2012, from GBP440 million in 2007.

"Increased consumer uptake of the product, along with premium rate increases to cover high claims inflation, have combined to make this one of the fastest growing insurance markets in the U.K.," said Andrew Haslip, financial services analyst at Datamonitor and author of the report.

By Goran Mijuk and Anita Greil, Dow Jones Newswires; +41 43 443 8047; goran.mijuk@dowjones.com; anita.greil@dowjones.com