



Bank of Ireland Sectors Team Food and Drink Review and Outlook

July 2021



Classification: **Green**

2021 H1 Insights

H1 was a challenging period for the food and drink industry as it coped with continued uncertainty around COVID-19, the administrative burdens of Brexit, and increased volatility in freight and commodity prices. Nonetheless, the industry has performed well with exports only slightly behind last year (-1% January to May¹) and evidence of strong optimism on prospects for the future².

Summary

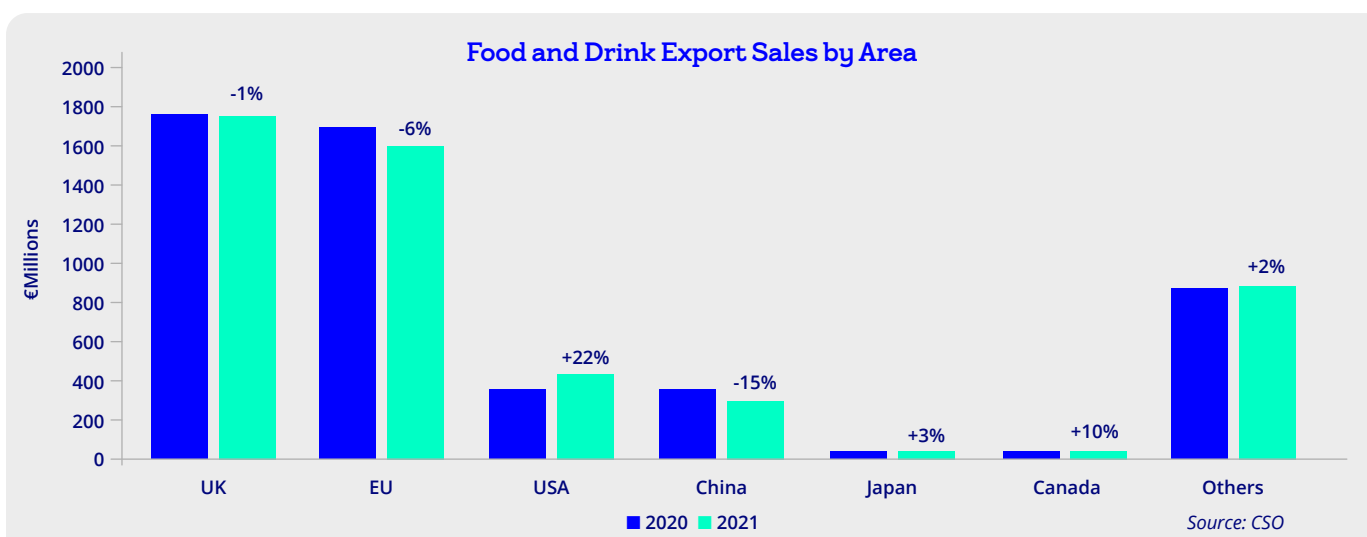
By the start of 2021, the majority of businesses in the sector had adapted well to the challenges of COVID-19. However, plans to refocus on foodservice sales took a backseat as January's lockdown extended through to quarter 2 both at home and to varying extents abroad. The news of the vaccine rollout helped drive some pipeline fill to export markets in Q2. Also during this

time, the implications of the impact of the new Brexit deal began to unfold. To date, impact on imports and availability of key production inputs has been more pronounced than the impact on exports. From a sectoral perspective, while dairy continues to dominate our export profile there were strong recoveries by COVID-19 affected sectors such as seafood and whiskey³.

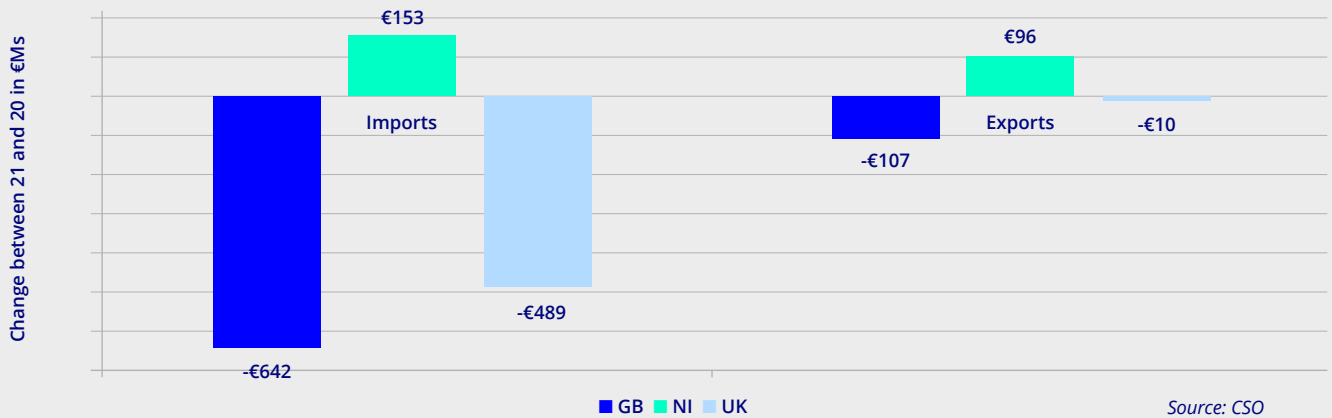
Food & Drink Export Sales by Sector

| €Ms | Jan - May 2020 | Jan - May 2021 | Difference | % |
|-----------------------------------|-----------------|-----------------|----------------|-------------|
| Alcohol | 477.40 | 593.53 | 116.13 | 24% |
| Total Meat | 1,254.38 | 1,264.07 | 9.70 | 1% |
| - Beef inc offal | 809.62 | 836.49 | 26.87 | 3% |
| - Pigmeat | 239.36 | 230.04 | -9.31 | -4% |
| - Sheep | 139.40 | 156.20 | 16.80 | 12% |
| - Poultry & Others | 66.00 | 41.34 | -24.66 | -37% |
| Total Dairy | 2,064.13 | 1,823.38 | -240.75 | -12% |
| - Butter | 413.39 | 329.41 | -83.98 | -20% |
| - Cheese | 326.09 | 318.31 | -7.78 | -2% |
| - Infant food | 441.34 | 331.27 | -110.07 | -25% |
| - Milk Powder | 497.33 | 460.40 | -36.93 | -7% |
| -Other Dairy | 385.98 | 383.99 | -1.99 | -1% |
| Prepared Consumer Foods | 972.03 | 978.54 | 6.50 | 1% |
| Horticulture & Cereals | 90.15 | 115.08 | 24.93 | 28% |
| Seafood | 213.74 | 256.87 | 43.13 | 20% |
| Total | 5,071.83 | 5,031.47 | -40.36 | -1% |

Source Bord Bia



Food & Drink UK ROI Trade 2021 vs 2020 (Jan-May)



Key Sector Trends in 2021 H1

- COVID-19 Recovery Related Growth:** The closure of foodservice had a particularly challenging effect on categories dependent on out of home consumption such as seafood and alcohol. Seafood exports to Asia were one of the first areas to be hit by COVID-19 shutdowns. Seafood exports are now up by 20% (Jan-May 21) and sales have recovered to 96% of the 2019 level. Alcohol exports for the same period are up by 24% - whiskey, which had suffered significant declines in the US market in March and April of last year as COVID-19 hit, is now at a level 6% higher than over the same period in 2019.
- COVID-19 Related Forecasting Uncertainty:** Accurate forecasting of potential customer demand has been extremely challenging as lockdowns began to lift and trade moved from retail to foodservice. This has knock on effects on product availability and has also resulted in a "just in case" rather than "just in time" mentality around stock level management, putting pressure on working capital in the sector.
- Brexit Impacts Evolving:** The Trade & Cooperation Agreement avoided many of the worst Brexit outcomes, however Brexit has led to additional complexity, uncertainty and costs, which have particularly affected the food and drink industry due to the interlinked nature of UK and Irish

food chains. 90% of Businesses surveyed by Bord Bia stated that Brexit had increased their cost base⁴. The UK remains our single biggest export destination and the Republic of Ireland was the number one destination for food and drink exports⁵ from the UK in 2020. As the UK delayed full border control, exports have generally flowed freely and additional non-tariff related costs have been offset by stronger sterling. However, food and drink imports are down significantly (-30%), resulting in opportunities for import substitution, particularly in the SME sector, where operators may have been previously uncompetitive against UK product. Irish operators are also picking up additional business on the continent, where British operators have been struggling to cope with the additional customs paperwork and attendant delays. However, in the case of some imports, such as specific ingredients or machine parts, British suppliers have been more difficult to replace, causing increased input costs and delays for affected manufacturers. Trade with Northern Ireland has also increased. Exports to Northern Ireland are up by 26% and imports are up by 44%⁶. This reflects the way in which the Single Market for goods is now operating on the island of Ireland as a result of the Northern Ireland Protocol, but it also may reflect operators' perception on relative ease of transit via Northern Ireland compared to the Republic, particularly in the case of imports from Britain.

- Commodity & Freight Increases:** The price of a range of agricultural commodities have reached their highest level in a decade with an average increase of 34% in June compared to the same month last year⁷. Freight costs have also increased⁸ and there is an increasing shortage of HGV drivers both here and particularly in the UK. This is having an impact on margins in the sector. Many operators had been holding high stock levels or had hedged commodity pricing forward in 2021, however these positions are now unwinding. Inflation is likely to be a key feature of H2 2021 as operators look to pass on price increases to address margin erosion.



Key Sector Activity

Investments relating to warehousing development, both on and off home sites featured heavily in 2021. Due to the rules of origin in the Trade & Cooperation Agreement and increased customs paperwork, using warehouses in Britain for 'just in time' deliveries to Ireland is no longer feasible. COVID-19 and Brexit delays in the supply chain mean operators are holding more stock. This has increased the cost and reduced the availability of third party warehousing, so increasingly, food operators are extending their warehousing capacity on site.

COVID-19 and Brexit related uncertainty have also put pressure on cash flow, due to forecasting challenges and the need to

carry more stock. Companies are increasingly looking to build resilience into their operating models by incorporating flexible sources of working capital. For example invoice discounting is being increasingly used by companies to ensure liquidity in the face of uncertain cash flows.

Due to the growth of the industry over the last decade, equity investments – particularly state sponsored investments such as those by Enterprise Ireland or the EIS schemes – have become prevalent. As companies become more established we are increasingly seeing refinancing of this equity by debt as established companies seek to take advantage of low interest levels.



H2 2021 Outlook

The H2 outlook is broadly positive. A recent Bord Bia report indicates 82% of businesses are optimistic about future prospects. As post COVID-19 volumes stabilise and companies begin to understand the longer term opportunities around Brexit related import substitution, this optimism should translate into more strategic capital investments in processing and product development. We also anticipate continued investments in warehousing capacity.

Key Trends 2021 H2

Continued Brexit Impacts: The UK is due to implement full border controls in January 2022. This will be phased in with Export Health Certificates and pre-boarding notification needed for animal products starting October 2021. There are concerns in the UK, at present, on the twin impacts of the shortage of HGV drivers and COVID-19 on food availability and it is feared that full border control might exacerbate shortages. From an Irish exporting perspective, many exporters are already comfortable with this documentation as they export outside of the EU. However, while 82% of respondents to the Bord Bia Readiness Radar Survey said they were well prepared to deal with the impacts of Brexit, this drops to a 54% when asked whether they were confident about sign off processes on export health documentation between Ireland and the UK. There are significant efforts in place by state agencies to prepare for this change, through training and increased personnel, however the quantum of documentation due to relative importance of the UK for our market will be challenging. This is likely to cause stockpiling before the deadline. It is also likely to have a significant impact on groupage, which may affect smaller SMEs that rely on mixed loads for frequent delivery.

Sustainability Focus: COVID-19 has brought sustainability challenges to the fore. Staying ahead on sustainability credentials is seen as a risk by 60% of Food and Drink Businesses⁹ surveyed by Bord Bia with 80% considering it an investment rather than a cost. The focus at present is very much around the twin pillars of carbon and packaging waste reduction, however potential impacts extend to all areas of the food chain including responsible sourcing and biodiversity improvement. For example, we have seen recent focus on ensuring animal feed in the meat supply chain is not contributing to Amazon deforestation. Key retail customers have set science based targets¹⁰ and supplier companies are likely to accelerate investment in innovation that will give them a competitive climate related advantage when pitching for sales. Increasingly, data capture of a company's climate based impacts by product will be necessary when seeking product listings with major retail customers. In addition, focus is likely to continue on increasing the amount of plant based food in consumers' diet.

Health and Wellness Focus: If anything, COVID -19 has accelerated this trend, as obesity was highlighted as a significant risk factor for COVID -19 related mortality. The UK government has moved to restrict the promotion of HSS (High Sugar and

Salt Foods)¹¹ and is looking to bring legislation into force by October 2022. This will require manufacturers to calculate a nutrient score for their products and will remove their ability to promote, either via display or price, unhealthy food. The lack of promotion is likely to drive additional inflation in these categories and it may restrict the opportunity for new entrants to attract consumer attention. From an EU perspective, major manufacturers have signed up for a voluntary code (EU Code of Conduct on Responsible Food Business and Marketing Practices) that aims to increase the availability and affordability of healthy food¹². The code however falls short of defining what a healthy diet means in an EU context and does not cover restrictions on promotions in the same way as the proposed UK legislation. However, the direction of travel by the larger industry players is likely to set a benchmark for SMEs to follow.

Technology: COVID-19 has accelerated the use of technology in a number of areas including the facilitation of shorter supply chains, online ordering and process automation. This will continue. Artificial intelligence has also been playing a role in speeding the development of plant based foods and innovation around cellular cultured animal products, such as lab grown meat and fish. The role of CTO will become increasingly pivotal in food companies as technology's ability to change the playing field, in the competitive world of food production becomes more evident. As technology becomes more prevalent, so too do the risks of cyber-crime and demonstration of acceptable cyber security standards is likely to play an increasing part in quality audits.





Bank of Ireland

Bank of Ireland is committed to its role as a key partner for Ireland's largest indigenous industry. This is amply demonstrated by our ongoing support of the Blas Na hÉireann food quality awards and our deep sectoral knowledge. COVID-19 has highlighted the necessity for companies to have an in market, long term, stable, finance partner that can offer timely support, dedicated relationship managers and an understanding of the cyclical nature of the various sub sectors.

- ¹ CSO
- ² https://www.bordbia.ie/globalassets/bordbia.ie/industry/readiness-radar/readiness-radar_report_webversion.pdf
- ³ CSO data Jan – May 2021 compared to same period 2020
- ⁴ https://www.bordbia.ie/globalassets/bordbia.ie/industry/readiness-radar/readiness-radar_report_webversion.pdf
- ⁵ <https://www.fdf.org.uk/globalassets/resources/publications/reports/exports-reports/exports-snapshot-2020-full.pdf>
- ⁶ CSO Jan- May 2021 vs 2020
- ⁷ <http://www.fao.org/worldfoodsituation/foodpricesindex/en/>
- ⁸ <https://www.irishexaminer.com/opinion/columnists/arid-40329236.html>
- ⁹ https://www.bordbia.ie/globalassets/bordbia.ie/industry/readiness-radar/readiness-radar_report_webversion.pdf
- ¹⁰ <https://www.tescopl.com/sustainability/taking-action/environment/climate-change/>
- ¹¹ <https://www.gov.uk/government/consultations/restricting-promotions-of-food-and-drink-that-is-high-in-fat-sugar-and-salt/outcome/restricting-promotions-of-products-high-in-fat-sugar-and-salt-by-location-and-by-price-government-response-to-public-consultation>
- ¹² <https://www.just-food.com/news/food-majors-sign-voluntary-eu-code-on-health-sustainability/>



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Roisin joined Bank of Ireland in 2019 as Head of the Food & Drink Sector, in order to support the Bank's business in this strong, indigenous industry. She brings an in depth understanding of the Food & Drink sector to the role due to her wealth of experience in both Ireland and the UK, across a number of companies and product categories. She has held senior commercial positions in both indigenous and multinational consumer goods companies including PepsiCo, Valeo Foods, Carbery, Boyne Valley and Robert Roberts Ltd. Her knowledge base spans end to end product development, from procurement and new product development, to branding, marketing and sales achievement. Her most recent role was in the Sports Nutrition Industry. Roisin holds an undergraduate Law Degree from UCC, an MBA from Warwick Business School and Post Graduate qualifications in Digital Business and Digital Marketing.

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