

Food & Drink

2020 H1 Insights

Summary

The industry came into 2020 in a strong position, with significant export growth and broadening horizons as new markets opened in Asia. COVID-19 began to affect exports to China at the end of Q1 and this effect spread to the UK & Continental Europe from April onwards. While sales into the retail channel increased, foodservice dependent companies and sectors were badly affected. From a sectoral perspective, dairy remained more resilient than others, with the meat, fish and alcohol sectors all experiencing significant declines in exports, resulting in an overall decline in exports of 1% in the year to April. As an essential industry, most food processors remained open during even the strictest part of the lockdown; however they were at the forefront of adapting business models to the new physical distancing protocols.

2020 H1 Insights

Despite the challenges of COVID-19, the Irish Food & Drink sector has remained resilient. Looking to H2 the spectre of a no-deal Brexit remains a threat. Industry focus will continue to remain on diversifying into new markets, while preparing as much as possible for all possible Brexit outcomes.

Key Sector Trends

Change from Foodservice to Retail

The primary effect of COVID-19 on the sector was to move consumer demand from foodservice channels into retail. Food & Drink supply chains have become increasingly more complex and specialised; therefore it was not easy for foodservice oriented suppliers to change their product immediately to fit retail. For many, this proved detrimental to their overall business performance. Others managed to innovate and open new routes to market via their own website or by cooperating with new partners. Even within retail, as consumers focused on reducing their trips to the supermarkets, impulse and grab & go categories were abandoned in favour of long life take home staples. As a result of these new customer buying patterns, supermarkets reduced their range significantly with artisan producers in particular impacted by the reduced range.

Market Volatility

The rapid change of demand from retail to foodservice and the ripple effect as COVID-19 moved from China to the West caused considerable market volatility. This resulted in a significant decline in most commodity prices - creating headaches for primary producers and processors, but giving some relief to secondary processors. Commodity prices have begun to harden during the latter end of Quarter 2. Market volatility has been well illustrated by the impact

on Norwegian salmon prices as a result of fears that they were linked to a COVID-19 recurrence in Beijing. Despite Chinese authorities confirming that there was no link, markets effectively closed and at one stage €1.3Bn was wiped off Norwegian aquaculture companies listed on the Oslo exchange.

Operational Complexity

Food processors were at the forefront of process innovations to ensure their plants continued to run even during the height of the lockdown. A range of measures were implemented such as additional PPE, Perspex screens and slowing of production to allow for greater distancing. For most operations, while this added complexity and cost it was effective in terms of staying COVID free. Meat processors, particularly those with large deboning operations, struggled to avoid COVID outbreaks in the early stages and a more widespread testing regime was introduced which appears to have successfully reduced the incidence of COVID in Ireland, if not abroad.

Supply Chain Pressures

Even before COVID-19 hit, Irish chilled & frozen exporters were coming up against challenges in accessing suitable containers for export. This was due to a backlog in China, where import of frozen pig meat had increased significantly due to African swine fever. As COVID-19 lockdowns hit China this was exacerbated. Sailing schedules across the board were hit resulting in significant delays on both imports and exports. Air freight was particularly affected with prices rising fivefold during the lockdown. This supply chain disruption, allied to market closures, resulted in a significant premium for cold storage.

Changing Export Profile

Over the period Jan-April 19, the UK accounted for 38% of our overall exports. This was partly due to Irish exporters building up stock profiles at the end of Q1 2019 in the UK, in advance of that quarter's Brexit deadline. For Jan-April 2020 the UK has returned to a lower level of exports - accounting for 34% of the total number.

Exports to the USA have also declined, mainly as a result of last October's imposition of tariffs. Dairy products, such as Kerrygold Butter and Dubliner Cheese, which accounted for 21% of our exports in Jan-April 2019, are now subject to 25% tariffs in the USA. Dairy exports fell by 16% for the four months of 2020. The effect of lockdown on US whiskey sales, which are particularly exposed to the out of home sector can be seen in the 24% decline in beverage exports, with over 80% of the decline occurring in April.

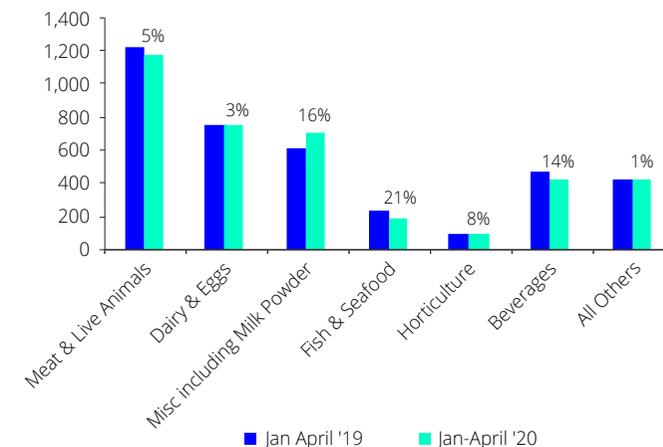
The success of market diversification strategies pursued by the industry can be seen by the fact that exports to countries outside of the USA and Europe grew by 20% in the four months to April.

Table - Export Size & Growth by Geography

€000s	Jan-Apr 19	Jan-Apr 20	Diff	% Ch.
UK	1,545	1,384	-161	-10%
EU	1,356	1,356	0	0%
China	272	299	28	10%
USA	333	287	-47	-14%
Others	604	748	145	24%
Total	4,110	4,075	-35	-1%

Source: CSO

Food & Drink Exports by Sector (Jan - April 2020 vs a year ago)



Source: CSO

Key Sector Activity

The continuing desire by consumers for healthier food lead to a number of strategic mergers, acquisitions and launches at the start of 2020, before COVID-19 broke. Kerry announced the acquisition of two North American companies that focus on the area of clean label ingredients. Strong Roots, the Irish vegan frozen brand, announced the expansion of its US footprint with a new office and extended distribution. There were a significant number of plant based product launches in all segments of the market from artisans to larger players.

Whiskey investment and development continued apace. There were a number of cask club launches as distilleries looked to interest investors in the potential returns for more mature Irish whiskey offerings. Enforcement of tightened restrictions on labelling, put pressure on brands that bought in and marketed whiskey from other distilleries, as the FSAI ruled that brands now need to be very transparent with consumers as to whether the whiskey was bought in or made on site.

Larger, internationally focused, Irish Food businesses continued to expand their global footprint, with the expectation that new trade deals would increase opportunities particularly in Asia.

Government support was vital to food & drink businesses during lockdown. The wage support scheme allowed businesses affected by the foodservice shutdown to retain skilled staff. Bord Bia launched a COVID-19 Response Marketing support package which awarded grant support to COVID-19 affected businesses in order to go online, develop new products & packaging and to open new customer channels.

Food & Drink

2020 H2 Outlook

Summary

While COVID related market disruption is likely to continue, the outlook for H2 is broadly positive. The outcome of Brexit trade negotiations will be a key focus of attention for the industry as we move into quarter 3.

Recovery in Food Service

The recovery in foodservice demand is critical to improvement in industry margins. Bord Bia has forecast a decline of 45-60% in turnover for the foodservice industry for 2020. Although, restrictions on restaurants have now lifted in many countries, foodservice demand is unlikely to return to previous levels as greater numbers continue to work from home, mass gatherings are restricted and consumer confidence is reduced. Food companies with a foodservice focus, while welcoming the improvement in demand, will need to reengineer their business models to cope with the changing profile of customer.

Online Growth

Looking ahead to H2, large numbers will continue to work from home and queuing for supermarkets in more wintry conditions is likely to be unpalatable, therefore the desire for in-home delivery is likely to remain strong. Supermarket delivery slots are likely to remain at a premium, so there may be opportunities for unmet consumer need. Covid related disruption resulted in businesses from foodservice wholesalers to artisan producers setting up direct to consumer models. Businesses will need to decide whether this is a core sales channel or an expensive distraction from their main business model.

Continued turbulence

With many health organisations predicting a second wave, businesses will need to be prepared for disruption. Disruption may be in the form of currency or commodity volatility, supply chain issues and or reoccurrence of lockdown. Therefore, food organisations will need to build in resilience into their model via increased cash reserves, strategic mergers or partnerships or through diversifying their product or customer range.

Brexit

As the UK government has not sought an extension to their current EU trading agreement, an EU/UK Free Trade Agreement will need to be concluded by the 31st of October, in order to avoid a no deal

Brexit. In May, the UK published its proposed tariffs in the event of no agreement being reached. Under previously published terms, 87% of imports would be tariff free, however under the more recent proposal that amount had dropped to 60%. With 34% of all Irish Food & Drink exports going to the UK, Irish companies will be particularly impacted. The lack of clarity also affects UK exporters, with many expecting to lose European contracts in September if there is no clarity on a deal. The areas of contention regarding Food & Drink are primarily around fisheries and minimum standards - the so called "level playing field".

While the threat of a hard border has largely been removed due to the Northern Irish Protocol, clarity is still needed on many of the finer points of trade. This is particularly the case with regard to imports into NI from Britain. While the EU asserts that these imports should attract tariffs by default with any exceptions going through a justification process, the UK is taking the opposite position.

Market Diversification

Due to the continued threat of Brexit, Irish companies will continue to look further afield for opportunities. The Free Trade Agreement with Vietnam has now been ratified and exports to China continue to increase. Pig culls due to swine fever have continued to happen in 2020 in China, therefore demand for Pork remains high.

Sustainability

The disruption of COVID-19 has brought increased focus on the importance of food security and overall sustainability as it relates to food. The 2020, EU Farm to Fork Strategy also places sustainability at the heart of food production. From an Irish perspective we are likely to see a focus on shorter supply chains with alternative growing techniques such as hydroponics and vertical farming offering opportunities to replace some air freight imports. The Programme for Government also includes a new Food Ombudsman whose remit will be to improve transparency in the sector, particularly as it relates to price.

Funding Activity - What we expect to see

The focus on sustainability is likely to drive continued capital investment around renewable energy and waste reuse. Issues related to COVID-19 distancing will also increase the focus on automation. As businesses review their post COVID models, we expect an increasing amount of mergers and acquisitions as the industry adjusts to new demand and cost models.

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 hEireann 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.



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Roisin joined Bank of Ireland in 2019 as Head of the Food & Drink Sector to support the Bank's business and customers in this strong, indigenous industry. She brings an in depth understanding of the sector, having held a number of senior commercial positions in both local and multinational consumer goods companies in Ireland & the UK. These included PepsiCo, Valeo Foods, Carbery, Boyne Valley and Robert Roberts Ltd. Her knowledge base spans end to end product development, including procurement and innovation, branding, marketing and sales achievement. Her most recent role was in the rapidly growing 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.

Sources: Bord Bia, Central Statistics Office (CSO), Intrafish.com

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