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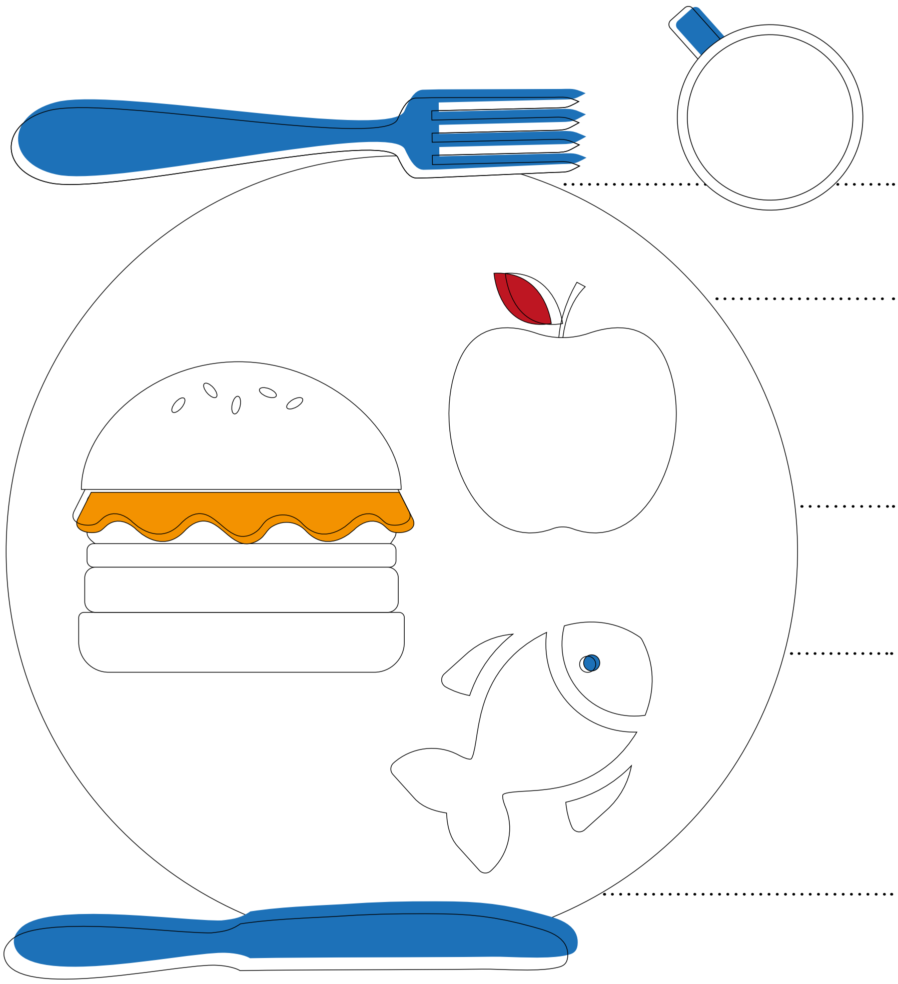
SECTOR BULLETIN: FOOD AND DRINK 2020 UPDATE

MakeUK.org

FOOD & DRINK SECTOR BULLETIN: 2020 UPDATE

Two years ago we published our first and Food & Drink specific sector bulletin. Now in 2020, we update the key figures that were presented before and highlight new developments in this important and high profile sector.



IN 2018 THE FOOD & DRINK SECTOR CONTRIBUTED £28.7 BILLION IN GVA, AN INCREASE OF 6.3% SINCE 2016.

IT REMAINS THE LARGEST MANUFACTURING SECTOR IN THE UK ACCOUNTING FOR 15.6% OF TOTAL MANUFACTURING GVA.

£85.63 BILLION IN SALES IN 2018, AN INCREASE OF 7.6% FROM 2016.

TOTAL NUMBER OF JOBS UP TO 440,000, A STAGGERING INCREASE OF 5.3% SINCE 2016 AND ALSO CURRENTLY AT ITS HIGHEST LEVEL SINCE 2004.

INVESTMENT UP BY A HUGE 10% TO A TOTAL OF £3.7 BILLION.

FOOD SECTOR ACCOUNTS FOR **84%** **OF TOTAL SALES**

DRINK SECTOR ACCOUNTS FOR **16%** **OF TOTAL SALES**

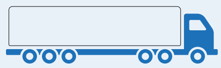
THE PRODUCTION, PROCESSING AND PRESERVATION OF MEAT AND **POULTRY MEAT ACCOUNTS FOR JUST OVER 25% OF THE ENTIRE FOOD INDUSTRY.**

Source: ONS and Oxford Economics

TRADE PERFORMANCE

Total food & drink sector yearly exports:

- **£13.9** billion exported to the EU
- **£9** billion exported to ROW (rest of the world).

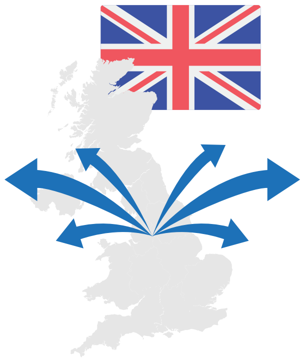


Large growth of 13% in Food & Drink exports since 2016.

EXCELLENT 2019 EXPORT PERFORMANCE HAS MEANT EXPORT GROWTH 2 YEARS TO DATE AUGUST 2019 HAS BEEN A STAGGERING 23%

UK 4TH LARGEST FOOD IMPORTER IN THE WORLD:
53BN USD

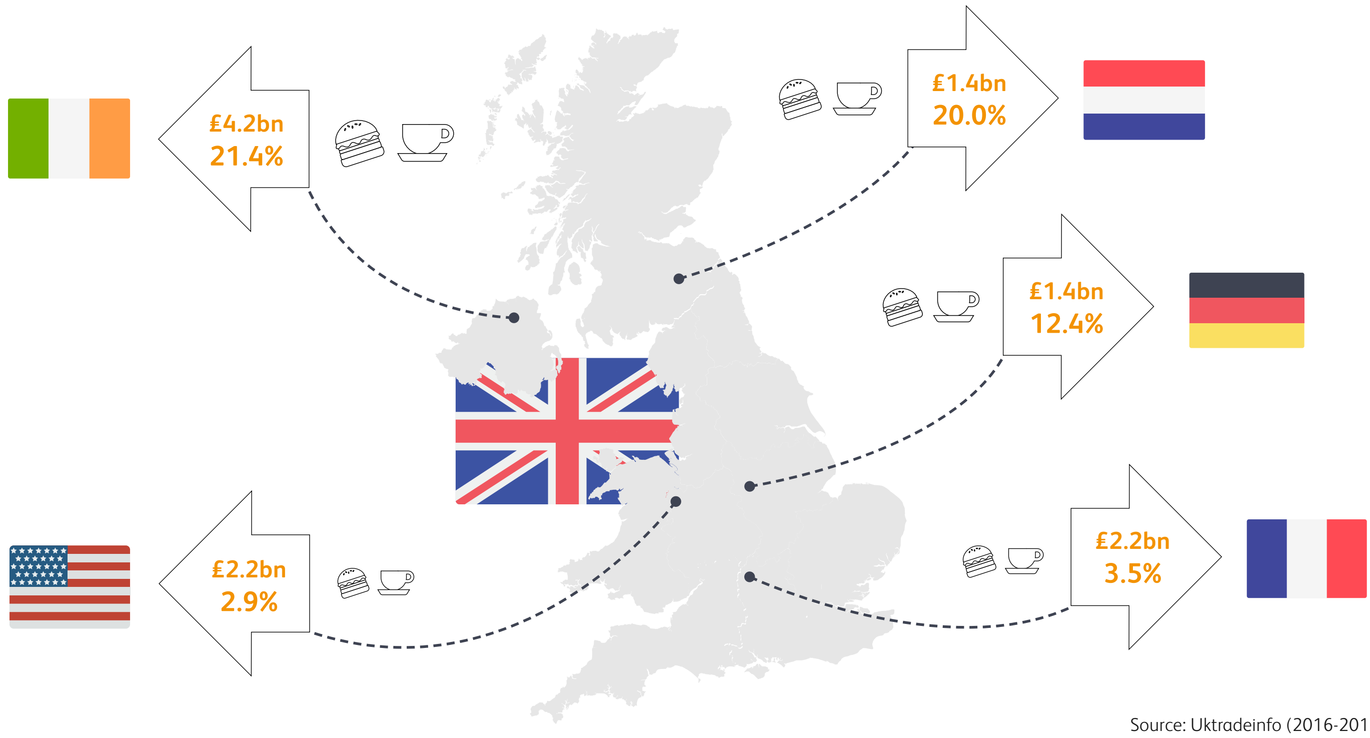
UK 2ND LARGEST DRINK IMPORTER IN THE WORLD:
8.8BN USD



UK THE LARGEST EXPORTER OF WHISKY IN THE WORLD BY A FACTOR OF 6.
6.4BN USD

UK 3RD LARGEST DRINK EXPORTER IN THE WORLD:
10.2BN USD

Top 5 Export Countries and their growth



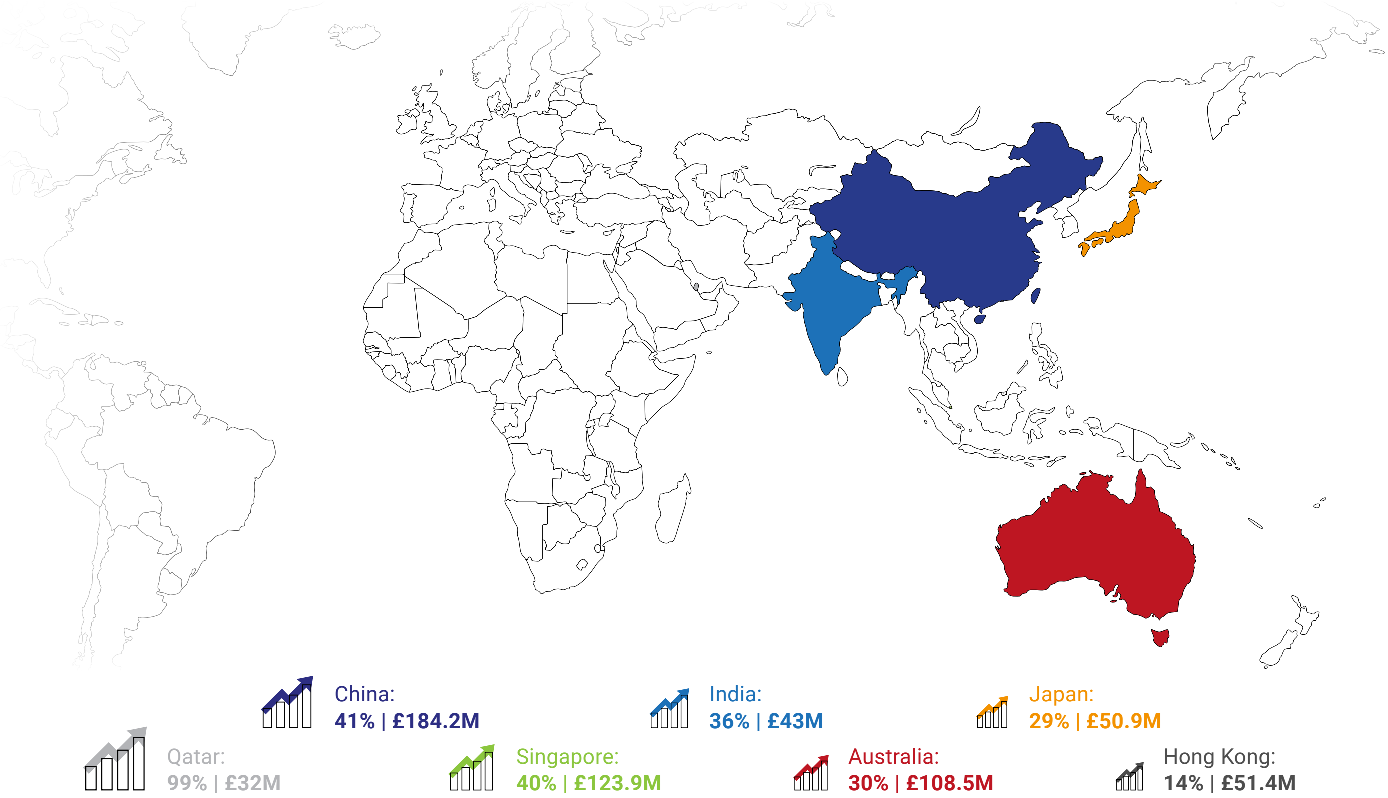
Source: Uktradeinfo (2016-2018)

Even since the Brexit referendum in 2016, the EU remains the food and drink sector's most important trading partner with 61% of all exports destined for their shores.

However, trade growth for the sector has been largest with newer emerging food and drink trade partners in Asia and Oceania.

Large export market growth in Asia and Oceania

% and £ growth in food & drink exports to destination 2016-2018



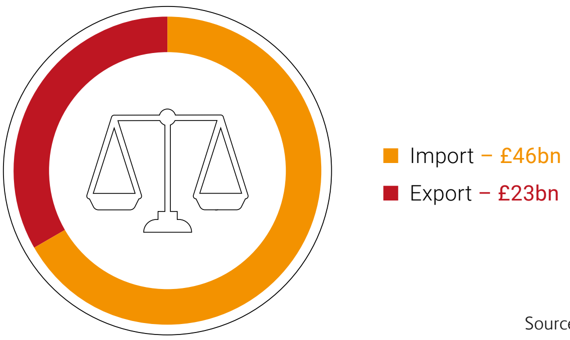
Source: UKtradeinfo

Fostering continued growth with these export destinations will be of utmost importance given the new international trade hurdles and opportunities faced by a United Kingdom outside of the European Union. This export growth has been on a strong positive trend for the past 20 years, with export value to Asia & Oceania increasing by 295% and to North America by 260% since 1999. (UKtradeinfo)

The export growth in the high-income countries of Singapore and Hong Kong can be partially attributed to the expanding demand for quintessentially British food & drink products from these regions.

Notwithstanding the sector's positive export growth, the UK is a net importer of food & drink by quite a margin, with a total import value of £46 billion compared to a total export value of £23 billion in 2018, meaning that the UK imports approximately twice as much food & drink as it exports.

Large trade defecit in food & drink



Source: UKtradeinfo

SECTOR INSIGHTS

"The hardiest on the field"

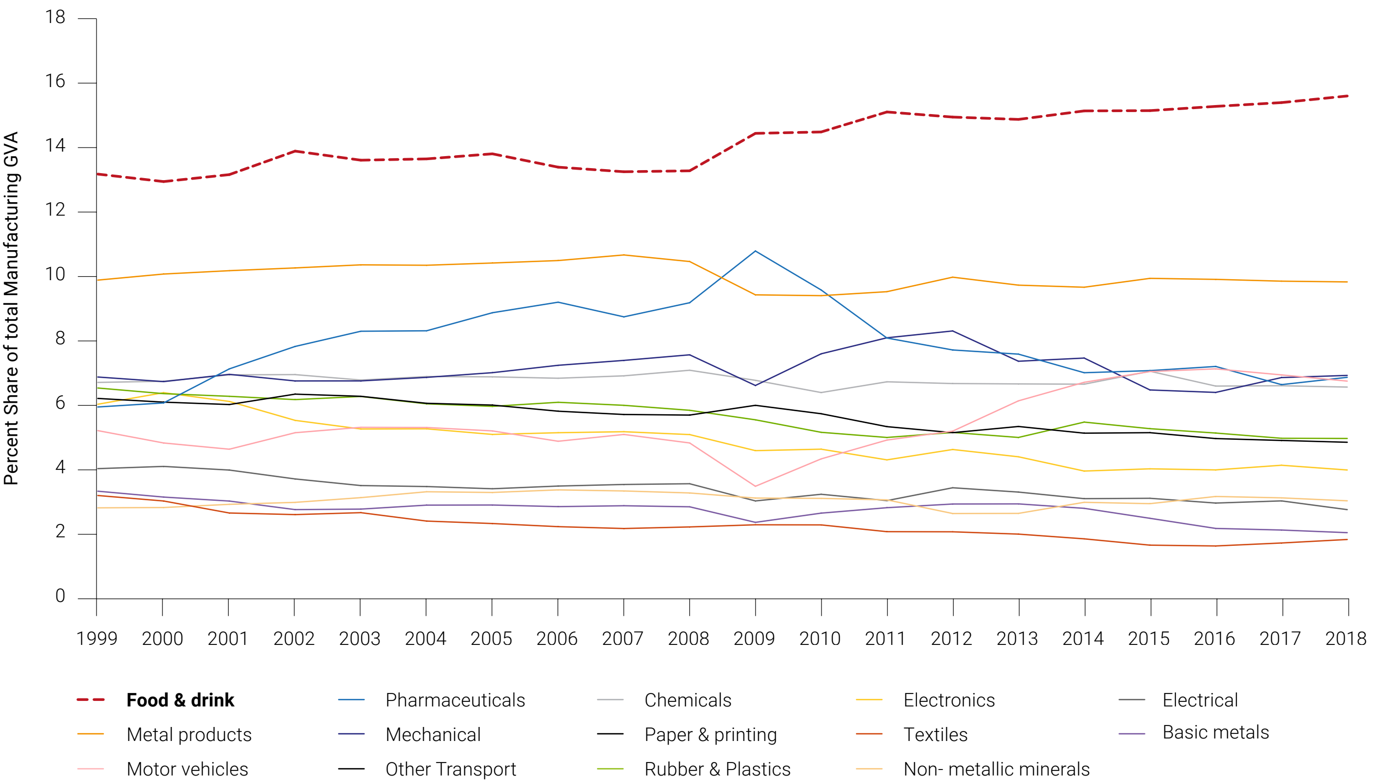
The food & drink sector has continued to demonstrate its staying power amongst British manufacturing. The sector has steadily increased its representation in the GVA of total UK manufacturing, rising from 13% of total manufacturing output in 1999 to 16% in 2019, whilst also maintaining the most consistent growth trajectory of any manufacturing sector.

The sector's share of GVA did not experience a drop during the Global Financial Crisis in 2008, in fact it quickly gained ground raising its share by a whole percentage point, and by the end of 2009 the sector had a larger share of manufacturing GVA than it had ever had in the decade before.

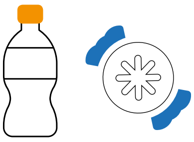
Partially responsible for this outcome is the food & drink sector's inherent resilience to recession. Domestic demand for products from the sector is consistent, as food & drink products are necessary goods for individuals, so variations in price have reduced effects on the overall quantity demanded compared to products from other sectors – this is known as being demand inelastic. Consumer preferences will adjust during an economic downturn toward options that offer a higher value proposition. Fierce competition in the grocery retail sector keeps prices down for consumers, something discussed further on in this bulletin update, whilst also motivating these retailers to offer products that span the range of consumer quality preference.

Individual retailers often meet this demand by selling products that span the consumer preference spectrum, with Sainsbury's "Taste the Difference" and "Basics" range as an example, protecting their revenue in times of price and quality preference variation. All members of the Big 4 offer these premium and economy groupings of products as a way of addressing demand from consumers with opposed quality preferences. In the event of national financial turbulence, consumers will typically be observed cutting back on non-consumable products, such as cars and electronics, from other manufacturing sectors to a much greater degree than they do with food & drink. During the 2008 financial crash the food & drink sector saw output fall by only 1.7%, whilst the rest of manufacturing experienced a much more severe decline of 9.4%.

Sub-Sector share of Manufacturing Gross Value Added



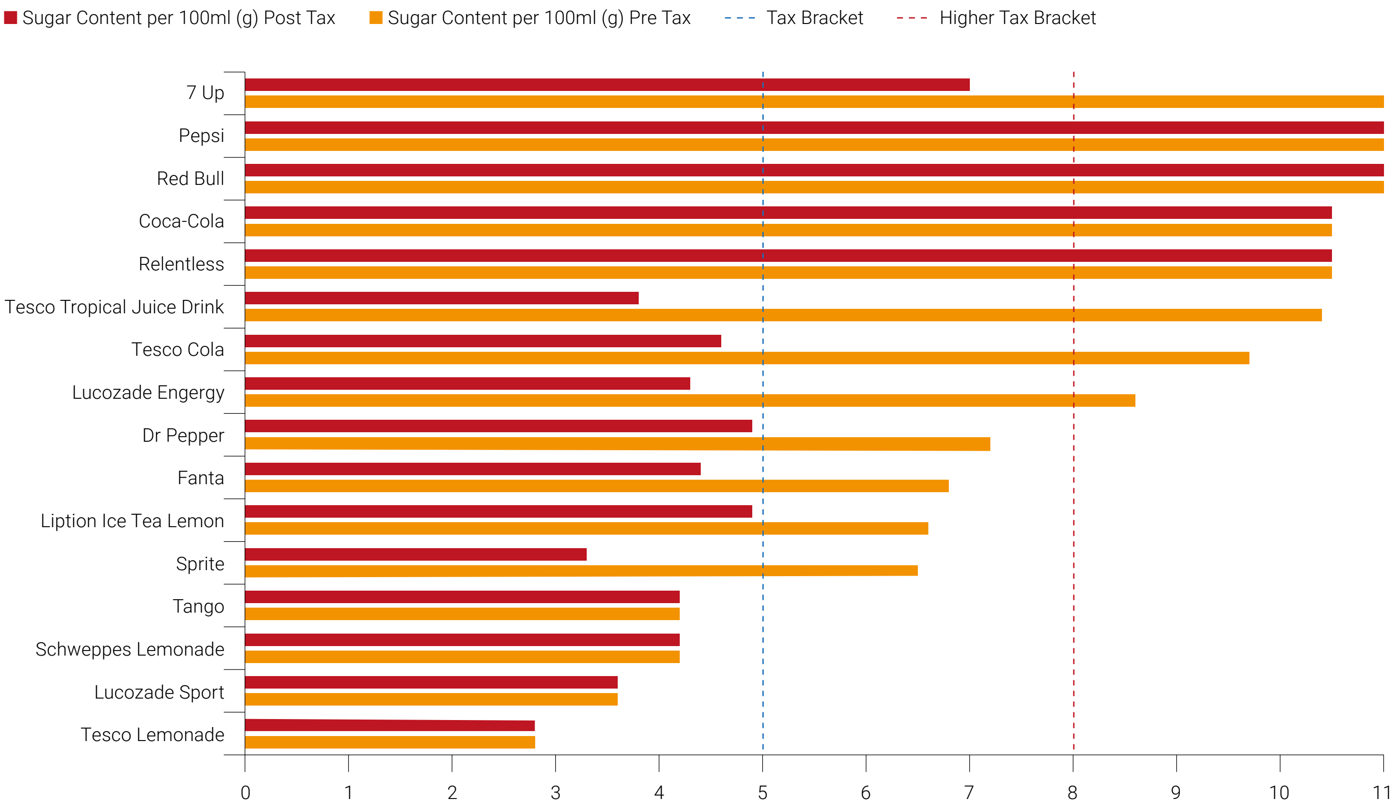
Source: Oxford Economics



“A sweet deal?”

The sugar tax, formally known as the Soft Drinks Industry Levy, has come into effect since the publication of our last food & drink sector bulletin and has had some unexpected effects from the government’s point of view. The levy was introduced in April 2018, with the beverage industry given two years’ advanced notice so that it could prepare. There are two brackets for the tax, one for drinks with sugar content above 5g/100ml and a higher rate for those with sugar content above 8g/100ml. However, even before its imposition, the effect on beverage manufacturer’s recipes was immense. Over 50% of manufacturers took action to cut sugar in their products, and soft drink giant AG Barr, of IRN-BRU fame, announced that 99% of their product offering would fall below the taxable threshold before the levy came into effect. Coca-Cola Great Britain announced that 60% of their portfolio would fall below the threshold, and Britvic likewise with 72% of their products. In the most extreme case, Lucozade Ribena Suntory adjusted the recipe in every one of its drinks so that they all fell below the taxable level.

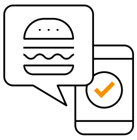
The introduction of the sugar tax has significantly impacted the sugar content of popular drinks



Source: Behavioural Insights

However, Public Health England’s September 2019 report on sugar reduction in food and drink has found that we are in fact eating more sugar overall. While the sugar content in many products has been successfully reduced: yoghurt by 10.3%, breakfast cereals by 8.5%, cakes by 4.8% and in sweet spreads and sauces by 4.6%, this same progress hasn’t been observed in people’s habits, with PHE suggesting the cause of this boost in consumption results from increased retail availability of sugary products and the particularly hot summer of 2018 fuelling sales of ice-creams.

It has been a bittersweet victory for the government. On the one hand, the philosophy behind the tax was always to motivate the manufacturers to reduce sugar content in their drinks (the primary goal was not to influence consumer behaviour), which has indeed occurred, but on the other hand the government had done some amount of grandstanding that the tax revenue from this levy would be exclusively earmarked for school’s sports programmes and breakfast clubs. Initially, it was thought that the levy would bring in £520 million for these initiatives, yet that figure was swiftly revised down to £275 million and then £240 million for 2018 as the levy had been almost too successful in influencing manufacturer’s recipes, bringing their product offering’s sugar content below taxable levels. Consumer preferences for healthier food and drink options have compounded this effect, with health-food sales rising by a whopping 37.5% in year ending September 2018 and demand for health-centric and free-from items at a record high.



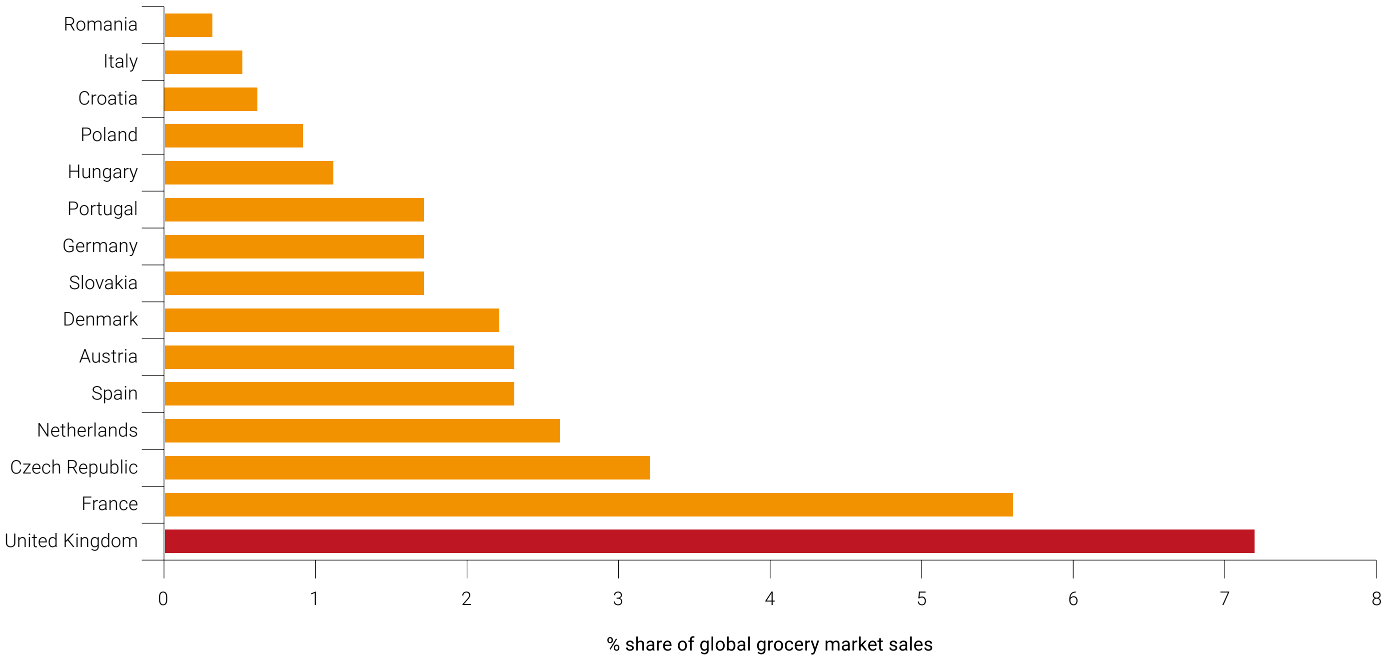
"The last mile's digitisation"

The last mile in food & drink product delivery to consumers has been changing at an exponential rate. The rise of both prepared food delivery – the likes of Just Eat and Deliveroo – and online grocery delivery have disrupted the traditional retail grocery market. Brick and mortar sales to consumers still control the lion's share of the market accounting for 93% of total sales, yet the online grocery market has seen sizable expansion, up from 6.1% in 2016 to 7% in 2018. (Mintel, 2019) The British people are the most prevalent users of online grocery shopping out of any EU country, spending £141.9 million a week on it and responsible for the largest share of the global e-commerce market out of EU members. (Statista, 2019)

Despite this, the retail grocery market itself has been experiencing internal turbulence as the disruptive discount retailers such as Aldi and Lidl have been clawing away market share from the incumbent Big 4 supermarkets of Tesco, Asda, Sainsbury's and Morrisons. In response to changing consumer preferences, along with the evidenced success of discount retailers expanding their market share at the Big 4's expense, Big 4 members are seeking to lower prices to regain customers they may have lost to the likes of Lidl and Aldi. Manufacturers' margins will be under attack as members of the Big 4 will look to establish price-setting behaviour – dictating to manufacturers what they will pay for their product – to protect their own squeezed margins and pass on the loss to the manufacturer.

Aldi, on the other hand, has seen exponential levels of growth in their UK operation. They are currently on a trajectory to open a new store in the UK every week for the next 2 years. They have also managed to achieve this while supporting the British supply chain, sourcing 100% of their everyday meat and poultry products and 40% of their fruit and vegetable products from Britain. Discount retailers are expected to continue to eat away at the Big 4's market share in the coming years.

Share of global online grocery sales based on value in leading European Union (EU) countries in 2017/2018



Source: Statista

FOOD & DRINK MANUFACTURERS' RISK OUTLOOK

No-Deal Brexit

The overarching concern, a No-Deal Brexit would realise a step-change in how food & drink businesses operate, affecting all aspects of the industry. The ability of UK businesses to hire EU workers will be hindered, particularly so in a no-deal arrangement where there may be no preferential agreement towards the movement of people for agreed employment. Seasonal work in the agricultural food industry is often filled by EU workers, roles these manufacturers think they will be unable to fill with British workers if they lose access to the EU labour market.

The concern regarding access to labour has quadrupled in 2019 since the same time in 2018 according to a Food & Drink Federation survey, with over a third of food & drink businesses expecting to have trouble in accessing both permanent and temporary labour in 2019, even before the UK has exited the EU.

Customs Issues

With the UK leaving the EU customs union, there is a heightened risk that regulatory discrepancies will arise between both UK, EU member states, and those states which have preferential trade agreements with the EU, which by extension the UK has access to while it is an EU member. When the UK is no longer a member of the EU, packaging, mechanical methods, storage methods and a host of other processes that are subject to regulation will need to change.

55% of food & drink businesses think that there will be increased packaging producer responsibility costs and 37% think there will be an increase in costs relating to label changes (FDF, 2019). This is unsurprising, as there is a bevy of requirements that need to be met when the UK becomes a 'third country', including removing any reference to EU standards. Products that contain EU component inputs will now have to reference 'Non-UK' after the exit date. Other EU standard markings, such as the EU organic certification and logo, will need to be removed.

Conclusion

The performance of the Food & Drink sector has been excellent overall, bucking the trend of decline so many other manufacturing sectors are facing. High GVA growth, new job creation and export expansion into new markets have all meant that the sector has had its best foot forward when it came to grappling with Brexit, among the other challenges that have faced it. Although the threat of losing access to the EU single market will weigh heavily on many of the sector's manufacturers, strong domestic demand coupled with resilient order books leaves the sector well equipped for the road ahead.

The Manufacturers' Organisation

We're delighted to introduce Make UK, the new name for EEF, and our family of new brands including Make Business and Make Venues. Together they will support the needs and requirements of our vibrant sector and ever-changing marketplace.

We stimulate success for manufacturing and technology related businesses, enabling them to meet their objectives and goals. We empower individuals and inspire the next generation.

We create the most supportive environment for UK manufacturing growth and success and we represent the issues that are most important to our members, working hard to ensure UK manufacturing remains in the government and media spotlight.

Our extensive knowledge of manufacturing that means we're able to influence policy-making at local, national and international levels. We push for the policy changes that our members want to see. We are the voice of manufacturing.

MakeUK.org

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