

COMMERCIAL BANKING

# Food & Drink Research Report 2016



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**OUR CONTRIBUTORS**

Ian Wright CBE,  
Director General,  
Food and Drink Federation

James Ellis,  
Finance Director,  
Aston Manor Cider

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# FOREWORD



Andrew Connors,  
Head of Client Propositions,  
Mid-Markets, Lloyds Bank  
Commercial Banking

**Welcome to our third annual market survey of the food and drink sector in England and Wales, which aims to give a snapshot of the state of the industry today, as well as offering an informed insight into the key opportunities and challenges it faces.**

Our food and drink producers, manufacturers and traders are a source of great national pride. From historic brands, grounded in provenance and tradition, to innovative organisations at the forefront of technology, homegrown food and drink companies have a global reputation.

In 2016, the industry has been forced to face up to some unprecedented challenges with the introduction of the National Living Wage, the proposed sugar tax and the uncertainty surrounding the EU Referendum.

It is clear that the food and drink industry has proactively sought to address these challenges and those that lie ahead.

It is also heartening to see companies committed to creating jobs and finding creative ways to grow, in particular by coming together to collaborate and share the valuable skills that they have learnt.



From historic brands, grounded in provenance and tradition, to innovative organisations at the forefront of technology, homegrown food and drink companies have a global reputation.



They are considered in their approach, but also resilient and determined, and are a driving force in the UK economy.

In this new phase for Britain, Lloyds Bank stands shoulder to shoulder with the sector and is committed to supporting ambitious firms in achieving their full potential.

By sharing the insight contained in this report with the wider industry, we aim to give food and drink firms a stronger sense of the opportunities and threats they face.

We hope that it will prove both informative and encouraging.

Watch Andrew Connors talk about this report and the outlook for the food and drink industry.

Watch the video now at  
<http://resources.lloydsbank.com/insight/food-and-drink-report/>



# EXECUTIVE SUMMARY



Despite uncertainty being the overriding theme of 2016, 95 per cent of firms are forecasting growth.



**Food and drink firms have never been more important to the UK. They employ more than 400,000 people and contribute almost £22 billion to the economy every year<sup>1</sup>. That's almost as much as the automotive and aerospace sectors combined<sup>2</sup>.**

And firms in other sectors could also benefit from some of the recent success in the food and drink industry.

Perhaps reflecting recent levels of investment, they seem to have found a solution to the productivity crisis that is plaguing the UK, increasing productivity by 11 per cent over the last five years, compared to an overall UK productivity increase of just 0.5 per cent<sup>3</sup>.

It's worth noting that the field research for this report was conducted in the weeks immediately following the UK's decision to leave the EU and therefore reflects the initial thoughts of survey participants, while the medium and longer-term ramifications remain uncertain.

## Going for growth

Despite uncertainty being the overriding theme of 2016, 95 per cent of firms that we surveyed in this report are forecasting growth over the next five years, and their plans to invest and create jobs are also up on last year.

They plan to achieve growth by entering new UK markets and developing new products, while their ambition to enter new overseas markets remains undimmed, with the same proportion holding plans to target new international trading partners as in 2015.

## Brexit: boost or bust?

The EU Referendum has been the biggest story of 2016, with the vote to leave preceded by months of uncertainty.

Just over half of the firms we spoke to said the impact had been negative, affecting their ability to invest and plan for the long-term, and damaging their confidence. However, more than a third said that the referendum result had a positive impact on their growth forecasts and almost half of firms said that planned investment in their business had increased since the vote result, twice as many who said it had fallen.

That's likely to be because they are hoping for lower levels of regulation and competition from European rivals, which will now face potential disruption to their access to the UK market while new trade deals are worked out.

## Working together

One key trend that emerged from this year's research was the move to collaborate.

It seems that food and drink firms are focusing on the potential of working together to develop new products and move into new markets.

That's a really positive move that can help reduce risk by sharing the time and cost involved in pursuing new opportunities, and we look forward to seeing how it pays off for firms in future research.

## A year in provenance

One interesting shift in this year's data when compared to 2015 is the potential change in attitude towards UK provenance. Provenance is still seen as a valuable asset but it appears a challenge is emerging in how well businesses can realise its tangible value.

While food and drink businesses still see it as an opportunity and are still determined to publicise their UK provenance in their marketing and packaging, this is countered with what seems to be a rising challenge when it comes to using it to help their business in a substantial way.

Overall, the research reflects a vibrant and dynamic sector that is tackling the challenges of the broader economy head on.

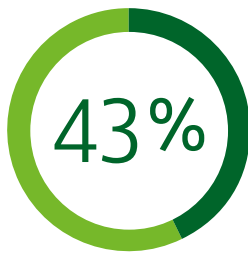
<sup>1</sup> Food and Drink Federation, Statistics at a glance, January 2016, <https://www.fdf.org.uk/statsataglance.aspx>

<sup>2</sup> Food and Drink Federation, Statistics at a glance, January 2016, <https://www.fdf.org.uk/statsataglance.aspx>

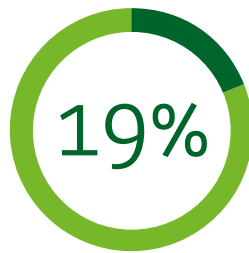
<sup>3</sup> Food and Drink Federation, Statistics at a glance, January 2016, <https://www.fdf.org.uk/statsataglance.aspx>

# KEY FINDINGS

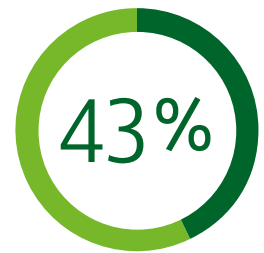
## GROWTH



average planned investment over five years as a percentage of current annual turnover



average five-year growth forecast as a percentage of current annual turnover



plan to grow by entering new UK markets

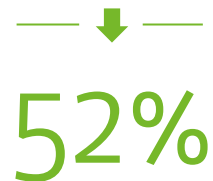
## THE EU REFERENDUM



say leaving the EU is the biggest challenge facing the industry

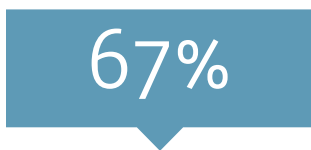


said the EU Referendum had impacted their investment

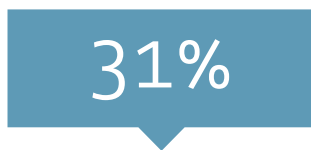


said the build up to the EU Referendum had a negative effect on their business

## CHALLENGES AND OPPORTUNITIES



say the growing awareness around public health is an opportunity



say overseas competition is a challenge for the industry



see the increased focus on provenance as a challenge for the sector

# INDUSTRY GROWTH AND EMPLOYMENT

## 29%

average planned R&D investment over five years as a percentage of current annual turnover



**It seems clear that, despite the uncertainty that has dominated during the first half of 2016, food and drink businesses in England and Wales retain a strong appetite for growth, though this has been tempered by the underlying economic conditions.**

Even given the prevailing business environment, food and drink businesses are now expecting to grow faster than last year, when the prospect of the EU Referendum and the National Living Wage were still on the horizon.

While a fifth of firms felt it was too early to comment on the potential implications of the EU Referendum decision, many more had felt hamstrung by uncertainty in the long run up to the vote and were now eager to bring their postponed plans back into action.

That helps explain why overall investment plans have actually grown since last year, with firms planning to commit 43 per cent of their current annual turnover to investing in growth over the next five years, up from 38 per cent last year.

And they believe it will pay off too, with average five-year growth forecasts growing at an even faster rate, hitting 19 per cent of current annual turnover in 2016, from 16 per cent in 2015.

That puts the sector on track to eclipse the Office for Budget Responsibility's forecasts for the broader economy<sup>4</sup> and well on track to achieve industry trade body, the Food and Drink Federation's, target of attaining 20 per cent growth by 2020<sup>5</sup>.

Recruitment plans have also increased slightly since last year, with firms holding plans to create 75,000 jobs over the next five years, a small increase from 73,738 new jobs which were planned this time last year.

<sup>4</sup> Office for Budget Responsibility, Economic and Fiscal Outlook, [http://budgetresponsibility.org.uk/docs/dlm\\_uploads/MAR16\\_EFO\\_PN.pdf](http://budgetresponsibility.org.uk/docs/dlm_uploads/MAR16_EFO_PN.pdf)

<sup>5</sup> Food and Drink Federation: 2020 growth vision, [http://www.fdf.org.uk/2020\\_growth\\_vision.aspx](http://www.fdf.org.uk/2020_growth_vision.aspx)



Firms are planning to commit 43 per cent of their current annual turnover to investing in growth over the next five years.



**Routes to growth**

Perhaps reflecting a new conservatism generated by ongoing uncertainty, firms appear more reticent to commit themselves to a particular growth strategy than they did last year.

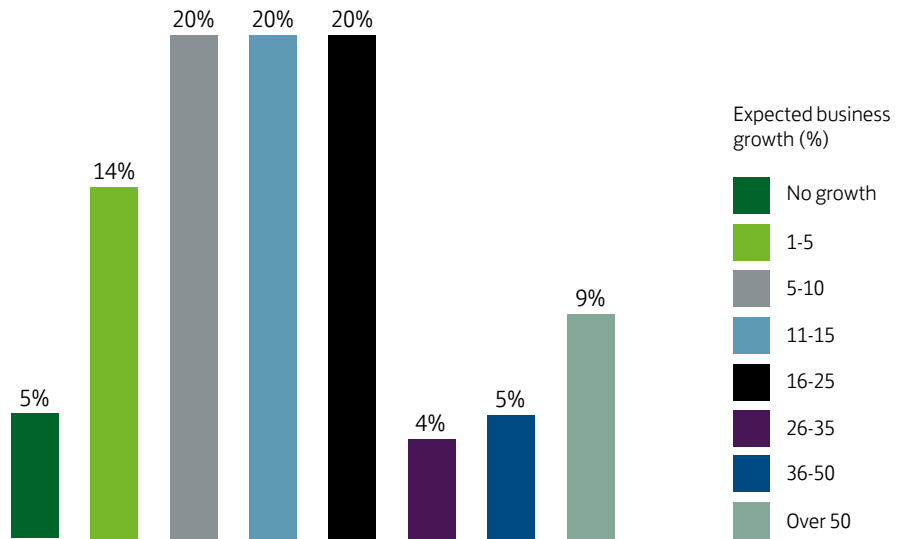
Entering new UK markets remains the most popular route to growth, but this year it was flagged by just 43 per cent of firms, compared with 56 per cent last year.

A potential concern is that risk-averse firms appear to be losing their appetite to innovate too. In 2014, 77 per cent were pursuing new product development, which dropped to 55 per cent last year and 40 per cent in 2016.

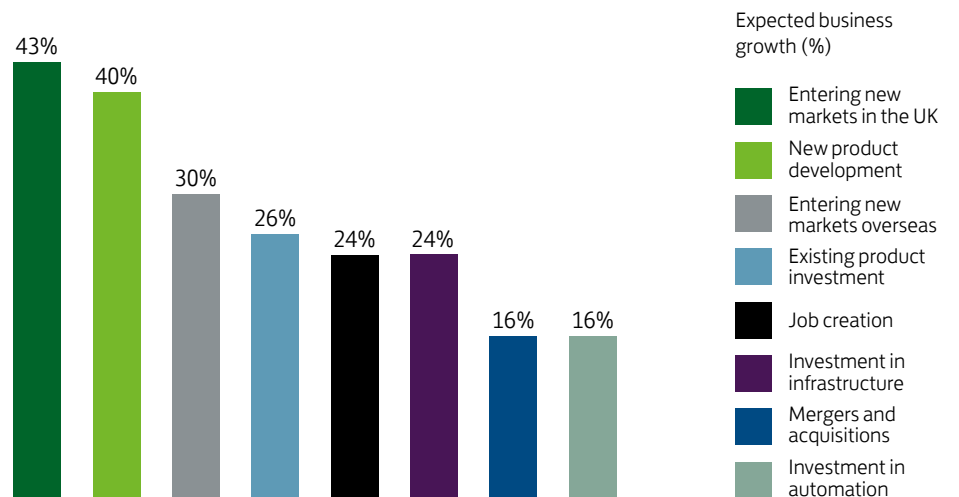
Existing product development has also fallen back considerably, and has now been leapfrogged by plans to enter new markets overseas. This is now the third most popular strategy, compared to sixth last year, though it was highlighted by 30 per cent of firms in both surveys.

It is likely to have become a higher priority because of concerns that barriers may be put up to existing overseas markets in Europe because of the EU Referendum result.

What is your expected business growth forecast as a percentage of current annual turnover for the next five years?



How do you plan to achieve business growth in the next five years?



### Productivity and partnering

An interesting shift has also occurred in how firms plan to fund their growth strategies.

The most popular method, jointly with the traditional method of using cash reserves, is now through a joint venture (both 32 per cent), suggesting businesses are seeking lower-risk growth options.

Cash flow finance remains a popular route to growth (31 per cent), as does using equity (21 per cent), though working capital efficiencies have also entered the fray for the first time, flagged by a fifth of firms (19 per cent).

We have already mentioned how food and drink firms are a shining example to the rest of the UK when it comes to pushing productivity.

So we asked them what steps they are taking to make their businesses more productive, and it was clearly an issue that they were putting time and effort into.

Making efficiency savings was the top priority (42 per cent), followed by streamlining processes (37 per cent), which could raise potential implications for job security.

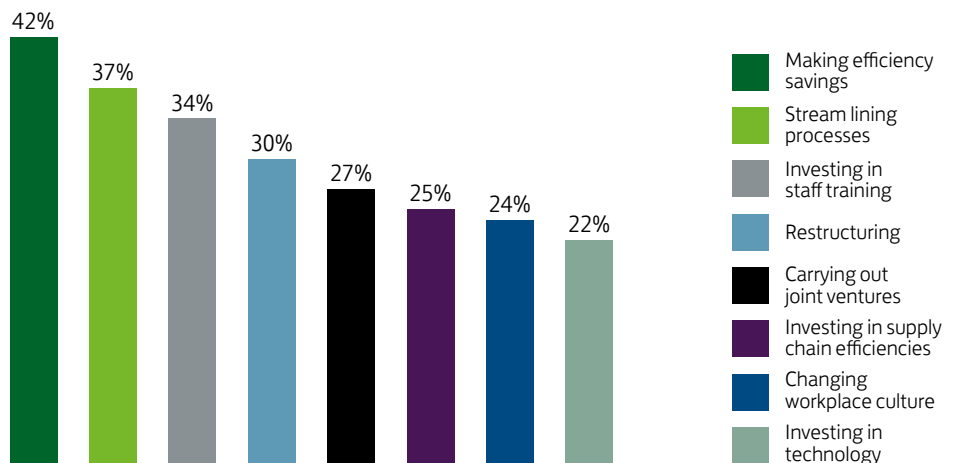
But firms also told us they will invest in staff training (34 per cent), restructuring (30 per cent) and forming joint ventures, which was being pursued by more than a quarter of respondents (27 per cent).



Perhaps reflecting a new conservatism generated by ongoing uncertainty, firms appear more reticent to commit themselves to a particular growth strategy than they did last year.



What steps are you taking to make your business more productive?







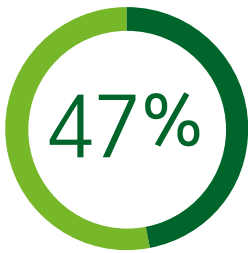
42%

are making efficiency savings

27%

are planning to fund growth  
through a joint venture

# INTERNATIONAL EXPANSION AND EXPORTS



of companies are investing or planning to engage new customers in Western Europe

## Despite the global economic instability that has characterised the last few years, the food and drink sector has proved an inspiration.

In the decade to 2014 it doubled exports, bucking the decline in total UK overseas sales<sup>6</sup>.

Unfortunately, this long-term trend came to an end in 2015, when food and drink exports fell for the first time in 11 years, dipping 4.4 per cent to £12.3 billion<sup>7</sup>.

That was primarily driven by a six per cent drop to the EU<sup>8</sup>, largely as a result of the strength of the pound against the Euro during the period<sup>9</sup>, though it remains the sector's primary trading partner.

Unsurprisingly, we found the number of firms targeting Western Europe has retreated from 60 per cent last year to 47 per cent this year, though it remains the top target.

In fact, intentions to target all the major markets have declined slightly, likely as a result of the extended period of uncertainty, with the exception of Eastern Europe and Russia, which has tripled, despite the Russian embargo on EU food imports.

This bump in the road does not appear to have impacted firms' intentions to trade with partners overseas, though it has caused fewer of them to make practical moves to further this ambition.



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## Plans pared back?

A substantial 30 per cent still plan to achieve growth by entering new overseas markets, the same level as last year.

But when we asked firms whether they were investing or planning ahead to engage new international customers in the next five years, the number had fallen back from 72 per cent in 2015 to 55 per cent in 2016.

And firms flagged a broad-based spectrum of factors stopping them investing or planning to engage new international customers, with funding, finding a suitable retail or distribution partner, logistics complexity and lack of knowledge of international markets all given an equal weighting (29 per cent).

Once these problems have been overcome, just over half (52 per cent) said they would be able quickly to ramp up production if an opportunity arose to expand into a new international market, which is down slightly on last year (58 per cent).



The proportion of companies that think English and Welsh produce has a good reputation internationally has held firm at 86 per cent.



### What's the challenge with provenance?

One particularly intriguing finding from this year's research was the emerging trend around provenance.

In 2015, almost three quarters of respondents (73 per cent) felt that the increased focus on provenance was an opportunity for their business and 88 per cent of firms said they were deriving a benefit from the UK provenance of their produce.

By 2016, less than half (44 per cent) said it was an opportunity and those saying they were drawing advantages from their UK provenance had fallen to 69 per cent.

At the same time, those who saw provenance as a challenge for the industry doubled from just over a quarter (27 per cent) to more than half (54 per cent).

The proportion of companies that think English and Welsh produce has a good reputation internationally has held firm at 86 per cent, so quite why the potential of provenance has seemingly failed to materialise is unclear.

It seems likely that, during a period of increased global economic uncertainty, cost-conscious consumers have prioritised the price over the provenance of their food.

Clearly this is still an area of opportunity for the sector but there is a rising challenge as to how to capitalise in any substantial way.

6 Food and Drink Federation, Statistics at a glance, January 2016, <https://www.fdf.org.uk/statsataglance.aspx>

7 Food and Drink Federation, UK Food and Drink Export Performance, <https://www.fdf.org.uk/exports/ukexports.aspx>

8 Food and Drink Federation, UK Food and Drink Export Performance, <https://www.fdf.org.uk/exports/ukexports.aspx>

9 Food and Drink Federation, UK Food and Drink Export Performance, <https://www.fdf.org.uk/exports/ukexports.aspx>

# 82%

say the referendum impacted their investment

# INDUSTRY FOCUS – BREXIT: BOOST OR BUST?

89%

said the EU Referendum had impacted their long-term planning

**The EU Referendum has been the defining event of the first half of 2016.**

For food and drink businesses it has brought both challenges and opportunities, but despite the initial uncertainties many businesses appear to be looking forward to a positive impact from the EU Referendum result.

Almost half of firms (44 per cent) said that investment in their business had increased, 18 per cent said they would ramp up activity, and more than a third (37 per cent) said their job-creation plans had grown since the EU Referendum result, perhaps after being put on hold in the run up to the vote.

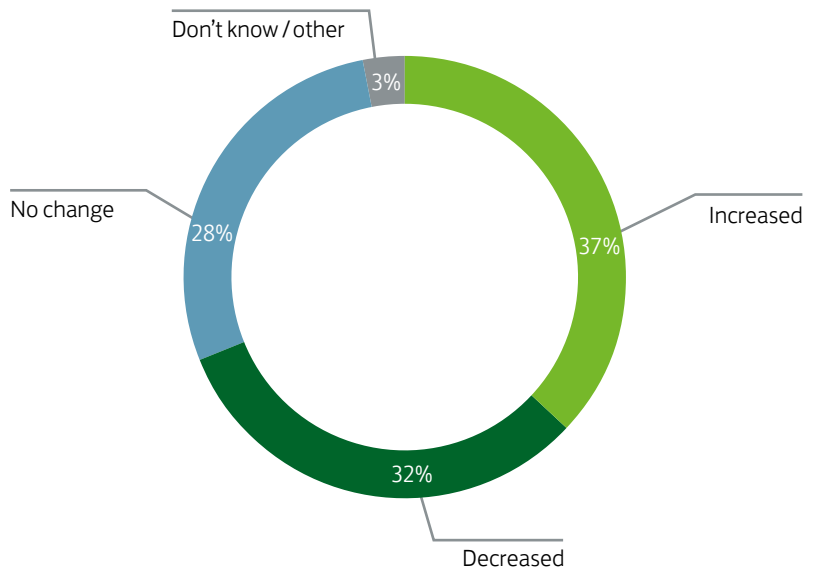
By the same token, a third (33 per cent) of firms are planning to increase R&D activity, with just 17 per cent reducing it, though those that are looking to increase activity are looking to de-risk the process by collaborating.



Almost half of firms (44 per cent) said that investment in their business had increased, since the EU Referendum result – twice as many as those who said it had decreased.



How has your growth forecast changed in response to the Referendum vote to leave the EU?



And a narrow balance of businesses said that their expectation of growth was higher now that the vote had been held, with 37 per cent expecting increased growth in the wake of the EU Referendum against 32 per cent who had shifted their growth predictions down.

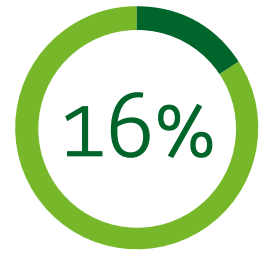
A fifth (21 per cent), however reserved judgement, arguing that it was still too soon to tell.

Meanwhile, a third (33 per cent) had already decided to cut investment plans for their business as a result of the vote and almost a quarter (23 per cent) said confidence within the industry and their company had decreased.

Businesses were less positive about the run up to the EU Referendum. Though more than a third (38 per cent) reported a positive impact, just over half (52 per cent) said that the build up to the vote had a negative impact on their business.

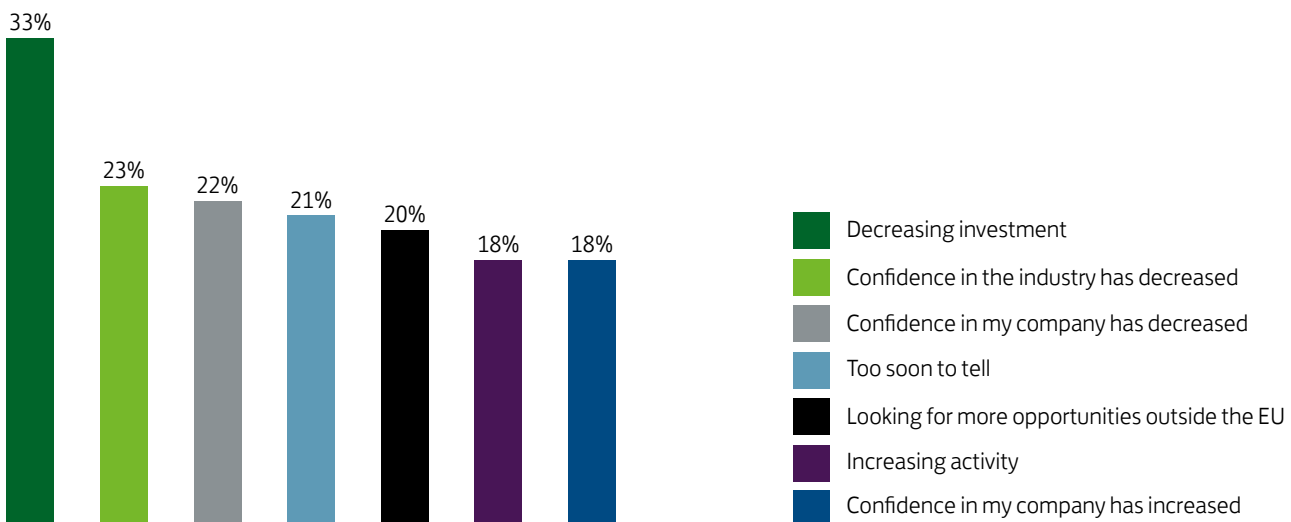


37 per cent said their job creation plans had increased since the EU Referendum result



have increased recruitment since the EU Referendum result

How has the Referendum result to leave the EU affected your business?



They told us they had held back from making decisions affecting their future, including long-term planning (89 per cent), investment (82 per cent), confidence (78 per cent), recruitment (72 per cent) and strategic vision (57 per cent).

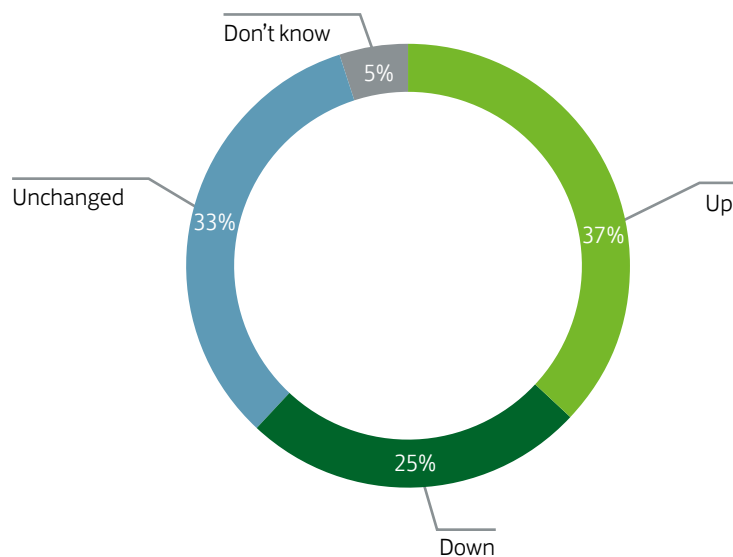
Now that the vote has been held, leaving the EU and its raw material supply, was still highlighted as the biggest potential threat to the industry as a whole, a view which remains unchanged year on year.

Many producers will be thinking through a number of issues linked to the EU, including any changes to EU financial support, the security of raw materials coming from the region and the supply of migrant labour.

# 21%

said it is too soon to tell if the EU Referendum result has affected their business

How have your job creation plans over the next five years changed in response to the EU Referendum result?





# CHALLENGES AND OPPORTUNITIES



A growing number of firms are reporting that the depressed oil price is having a positive impact on their business, up from 19 per cent to 32 per cent.



**The strong growth and investment plans of UK food and drink manufacturers highlight the industry's resilience in what has been one of the most difficult trading periods in living memory.**

As well as the uncertainty surrounding the EU Referendum, which looks set to lead the agenda for years to come, the spectre of depressed oil prices has loomed large over the global economy.

A growing number of firms are reporting that the depressed oil price is having a positive impact on their business, up from 19 per cent to 32 per cent, and concerns about agricultural price volatility seem to be easing too.

But there are a number of other looming issues, including the introduction of the so-called sugar tax, announced by the government in the 2016 Budget and scheduled to come into effect in 2018<sup>10</sup>.

The 20 per cent tax is primarily aimed at producers and importers of soft drinks<sup>11</sup> and is designed to help combat obesity.

There will be an exclusion for small operators<sup>12</sup> and the full detail of how the tax will be applied has yet to be confirmed.

Perhaps for this reason the jury is still out, with roughly a third of respondents predicting the levy will have a negative

impact (38 per cent), and a similar proportion expecting it to present an opportunity (35 per cent).

Respondents were far more certain about the broader growing awareness of healthy eating among consumers, which the majority continue to see as a major opportunity, though there are doubts creeping in.

Two thirds (67 per cent) said health awareness presents an opportunity for producers, down from 74 per cent, while those who think it will have a negative impact more than doubled from eight per cent to 20 per cent.

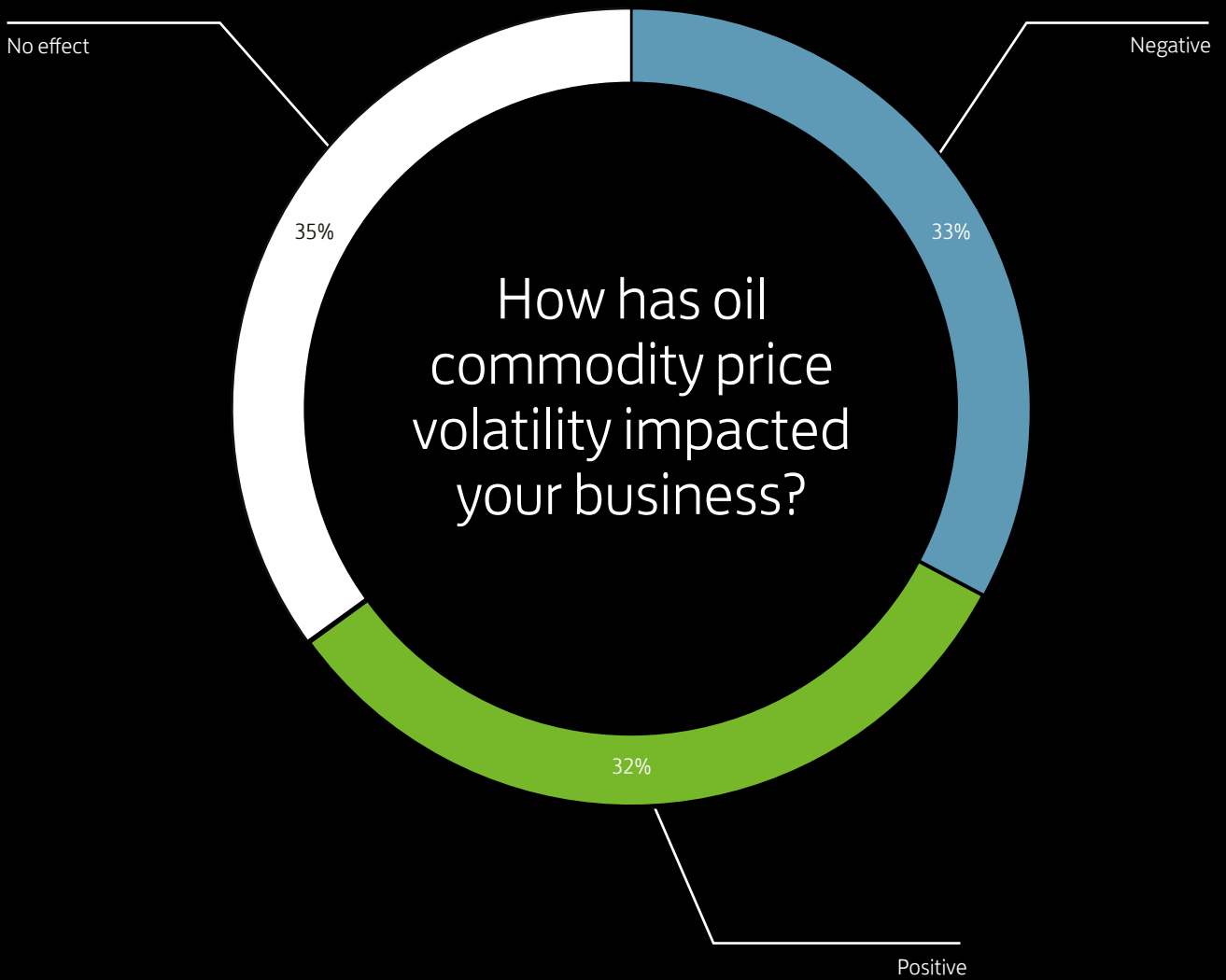
Anecdotally, those who think it presents an opportunity argued that consumers would be willing to pay extra for higher-quality produce and that there would be a greater ability for start-ups to prosper, while the counter arguments include worries over increased regulation.

<sup>10</sup> Gov.uk, Budget 2016, March 2016, <https://www.gov.uk/government/publications/budget-2016-documents/budget-2016#policy-decisions>

<sup>11</sup> Gov.uk, Budget 2016, March 2016, <https://www.gov.uk/government/publications/budget-2016-documents/budget-2016#policy-decisions>

<sup>12</sup> Gov.uk, Budget 2016, March 2016, <https://www.gov.uk/government/publications/budget-2016-documents/budget-2016#policy-decisions>





# TURNING RISK INTO REWARD



Ian Wright CBE,  
Director General, Food and  
Drink Federation

**This year's food and drink report is as useful as ever for revealing the challenges and opportunities faced by the sector. Occupying a deeply personal role for us as individuals, food and drink are pivotal to our society and our culture. It is not always remembered that food and drink is the UK's largest manufacturing sector.**

It makes an enormous economic contribution to our country, providing jobs for some 400,000 people and adding nearly £23bn in value to the UK economy each year. Since 2009, productivity performance in food and drink has increased by eleven per cent.

Bringing the right people with the right skills into the business is central to our future success. At the heart of each food and drink enterprise lie shoppers and consumers. In the UK today shoppers and consumers enjoy access to a wider range of safe, high-quality and nutritious foods and drinks – at all price points – than ever before. The industry recognises that safety, quality and authenticity are the cornerstones of consumer confidence.

Of course issues about the nation's health and wellbeing and the role of diet and nutrition remain center stage. Our industry accepts its responsibility to play the fullest part in tackling obesity. That involves constantly reformulating products to remove fat, salt and sugar, marketing responsibly and promoting active healthy lifestyles.

Finally, we must address the biggest business challenge of our times – the decision to leave the European Union. This poses a major challenge to most food and drink businesses, yet we are a resilient and resourceful industry. We are now focused on transforming those very real risks into real opportunities.

We are already working with the government to secure the best possible future UK and European Union relationship for food and drink and, more widely, to ensure that the operating environment for business here continues to be favourable.

I am confident that UK food and drink can continue to be a success story of which we are all proud.

## References:

- Food and Drink Federation: Statistics at a glance
- Food and Drink Federation: Open to export
- Food and Drink Federation: Export snapshot
- Food and Drink Federation: 2020 growth vision
- Gov.uk, Budget Policy Paper, March 2016
- Office for Budget Responsibility, Economic and Fiscal Outlook
- Gov.uk, Budget 2016

## Methodology

Field research for this report was undertaken in June and July 2016 by Coleman Parkes Research.

To gather representative data from this diverse industry, a broad cross-section of 100 food and drink manufacturers, producers and retailers in England and Wales were interviewed from companies ranging in size from less than £25m, £25-£750m and more than £750m annual turnover.

Business owners, managers, senior managers, directors and department heads took part in the survey.

Our survey questions focused on growth and export plans, job creation, capacity and investment, international markets and challenges.

# HELPING BUSINESSES TO GROW

Our teams of local financial experts have the experience and know-how to help make your growth, investment and export plans a reality. We're proud to work closely with some of England and Wales' leading and up-and-coming food and drink producers, and can tailor a range of solutions for your business.

For more information, get in touch with us.

**ANDREW CONNORS**

HEAD OF CLIENT PROPOSITIONS, MID-MARKETS  
0121 625 6552  
[andrew.connors@lloydsbanking.com](mailto:andrew.connors@lloydsbanking.com)

**DAVID ATKINSON**

UK HEAD OF MANUFACTURING, SME  
07764 625666  
[david.atkinson@lloydsbanking.com](mailto:david.atkinson@lloydsbanking.com)

**ANDREW NAYLOR**

HEAD OF AGRICULTURE, SME  
07725 446923  
[andrew.naylor@lloydsbanking.com](mailto:andrew.naylor@lloydsbanking.com)

**ELENA PAITRA**

MANAGING DIRECTOR, HEAD OF FOOD,  
BEVERAGES AND TOBACCO, GLOBAL CORPORATES  
0207 158 6097  
[elena.paitra@lloydsbanking.com](mailto:elena.paitra@lloydsbanking.com)

**GORDON RATE**

HEAD OF FINANCIAL MARKETS, SCOTLAND,  
0207 158 1889  
[gordon.rate@bankofscotland.co.uk](mailto:gordon.rate@bankofscotland.co.uk)

**ANDREW CHARNLEY**

HEAD OF TRADE & WORKING CAPITAL,  
GLOBAL TRANSACTION BANKING  
07909 872922  
[andrew.earnley@lloydsbanking.com](mailto:andrew.earnley@lloydsbanking.com)

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Reference: LBFD2016



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