

Pursuing opportunities in a challenging environment - insights from the Food and Agribusiness sector

by David Leydon

In this article, IFAC considers the many factors affecting the AgriBusiness Sector and gives practical advice for Food and AgriBusiness SMEs.

From Brexit and climate change to trade deals and changing consumer behaviour, Irish food and agribusiness owners have much to contend with.

The sector is one of the most outward looking in the Irish economy with 90% of our dairy and beef produce exported globally. In 2018, Irish exports were €13.6bn from the agri-food sector, providing 7.9% of national employment. 71% of the raw materials for the agri-food sector are sourced from Irish suppliers. To put it mildly, farming is vital to Ireland's rural economy.

Additionally, the agri-engineering sector exports across the world with the likes of McHale in Mayo (specialist farm machinery) and Dairymaster in Kerry (hi-tech dairy equipment) among the most noteworthy but there are many others.

Within the farm gate there are some significant challenges with an exceptionally low beef price causing financial pain and significant levels of disillusionment. The dairy sector has grown rapidly since the abolition of milk quotas in 2015. This growth has brought economic activity and vibrancy to the dairy regions of Ireland. However, inside the farm gate debt levels have risen and some growing pains are being experienced.

Given this context, our 2019 Food and AgriBusiness Report set out to take the pulse and sentiment of the sector. Working with Amárach Research we engaged 200 owners, MDs and CEOs of SME businesses in the sector.

A range of indicators are pointing to a less positive outlook among leaders in the sector when compared to this time last year:

- 20% decrease in optimism
- Brexit concern up 100%
- Businesses seeking bank finance down 30%
- 4 out of 5 businesses are experiencing static or decreasing margins.

Sentiment

Despite a 20% decrease in optimism compared with our 2018 report, it's not all negative with 59% of companies still optimistic about the future. 25% of companies are looking to employ more staff and 70% are expecting to retain the same number.

John Grennan is the Managing Director of J Grennan and Sons, a significant agribusiness in Offaly. He sums up the sentiment of agribusinesses dealing with farmers, "We are optimistic about the long-term future for the sector.

However, we are very concerned about the significant short-term challenges both we and our customers are facing" Beef and grain prices are under significant pressure while Brexit is a cloud hanging over the entire sector. And, in this period of uncertainty and challenge there appears to be a growing recognition that farmers need to be compensated fairly for the work they put in, something that wasn't always acknowledged.

Brexit

There is a 100% increase in businesses concerned about the impacts of Brexit, rising from 21% to 42% of total businesses surveyed. While this remains surprisingly low, it reflects a range of Government surveys about the preparedness of this sector for Brexit. This is corroborated by the relatively low number of businesses who had applied and received their EORI number.

This is the most basic of measures a company should take to prepare for Brexit and as of July only 51% of companies who had traded with the UK in 2018 had an EORI number. Increased costs, the potential of a hard border and loss of sales in the UK are all causing concerns but there is still lingering hope among business leaders that a deal will be done at the last minute.

Some businesses have been very proactive. Take the example of Prodig, a company which manufactures equipment for the agri and construction sectors. Donny Nolan, one of its Directors told me, "Forward planning has definitely been key to our preparations for Brexit.

The UK was a big percentage of our sales up until 2016. In mid-2016, we took the decision to look at markets away from the UK. Now we no longer use the UK as a land bridge and all our shipping goes from Dublin directly to mainland Europe which definitely eases concerns."

Our Food and AgriBusiness Report 2019 contains lots of advice for businesses. Some key questions that business leaders must ask themselves include:

1. Is your supply chain ready?
2. Do you understand the new rules and regulations around tariffs, including ensuring you have an Economic Operators Registration and Identification (EORI) number at a very minimum?
3. Have you looked at a range of scenarios, including the increased costs of doing business?
4. Working capital is critical – have you adequate working capital in place?
5. Have you a currency strategy in place?
6. Do you need a company structure in both ROI and UK?
7. Have you reviewed your UK contracts?
8. Are you communicating frequently with all stakeholders, suppliers, customers, and staff?
9. Have you maximised state supports?
10. While late in the day, have you looked at diversification and new opportunities?

Climate Change

While Brexit is dominating the conversation climate change is not too far behind. It is clear from our latest research that food and agribusinesses are taking their social responsibility seriously with 74% of businesses taking action on climate change.

Over half (51%) of those surveyed view managing waste and by-products as a key action to help them deal with this challenge. Other steps businesses are taking towards carbon neutrality include: purchasing sustainable packaging (43%); choosing environmentally conscious suppliers (31%); and investing in energy-saving initiatives (28%). Solar and renewable energy options are also experiencing some

uptake with 21% of businesses viewing these green energy options as an opportunity to help reduce their carbon footprint.

Our report indicates that a significant number of businesses are moving in the right direction in terms of dealing with climate change. Programmes such as Origin Green, Ireland's food and drink sustainability programme by Bord Bia, and Enterprise Ireland's GreenStart give businesses additional support and parameters to help measure, control and reduce the impact their operations have on the planet, as well as outlining some of the necessary steps to help secure a sustainable future for the sector.

Food Trends

Sustainable packaging is the top trend for Irish food businesses. It reflects a short-term opportunity for businesses to differentiate by using sustainable materials but also a growing responsibility for food suppliers to respond to changing consumer concerns. It also helps to address the stark reality that Ireland must increase its plastic packaging recycling by up to 80 per cent by 2030 if it is to meet strict new EU targets (Repak, 2018).

Although Ireland is a market where a low single digit percentage of people would identify as vegan, national campaigns have helped to push this trend to the fore of the public's mind. In the short term it's clear that food businesses are taking note of how emerging diet trends (including flexitarian diets and meat free days) are becoming more popular. This is a significant challenge for many in the agri sector. However, food businesses must be alive to the trend and seize any opportunity it presents.

In the wider market context, local provenance represents an opportunity for Irish food businesses. As part of Fáilte Ireland's Food and Drink Strategy 2018-2023, there will be increased opportunities for Irish food businesses to build on Ireland's reputation for high-quality produce and authentic experiences.

Private label focus

While direct sales is the most common route to market, the growing interest in private label is noteworthy. 62% of food businesses who use private label retail as a route to market have seen double-digit growth in their private label sales over the last five years. However, this increasing priority for private labels is double-edged. On the one hand it provides food businesses with scale if national contracts can be secured and it provides good cashflow potential if terms agreed are favourable. However, on the other, it can also reinforce the position of a food business as a price taker and limit the businesses medium-to-longer term ability to maximise net margins.

Nicholas Dunne, the Managing Director of Killowen Farm told me, "We use both branded and private label routes to market. This works well for us as our private label partnerships provide us with significant scale while at the same time, we are investing resources to build our own brands like Killowen Farm Yogurts. The opportunity is large as 70% of yogurt is imported while the main challenge is building the Killowen brand on a small budget."

Research and Development (R&D)

Despite a range of supports being available to engage in R&D, many indigenous companies are not investing in this area. This is a missed opportunity as R&D and the associated Intellectual Property (IP) can enable companies to compete very successfully abroad. The benefits of the R&D Tax Credit, which rose to 30% in the recent Budget, as well as the Knowledge Development Box, which reduces tax on profits earned by qualifying IP income to a reduced tax rate of 6.25%, need to be made as easy as possible for SMEs to avail of.

Where a company invests in R&D correctly, it can be a driver of success. Pat Fitzgerald, Founder and CEO of Beotanics, a plant-based food ingredient business says, "Innovation

has been the key driver in the success of our export focused business to date. By investing in patents, plant breeders' rights and securing exclusive licenses, we have created a barrier to entry to competitors and added value for our customers. In addition, understanding how to maximise our tax credits and focusing our company structure towards specialised activities has allowed us to claim back some of our R&D costs and optimise revenue streams. These strategic considerations helped us reinvest in the growth of our business."

Creating an environment which encourages and creates conditions for more SME's to invest in R&D should be a Government priority.

Technology

Technology continues to play a greater role in business across the food and agribusiness sector. In the last 24 months, some companies have shown a willingness to engage with new technologies like Robotics, Sensors and Data

analytics while they were less likely to invest in technologies like Wearable Technologies and Artificial Intelligence (AI).

Food businesses (25%) are more likely than agribusinesses (13%) to have invested in these potentially game changing technologies. Prohibitive costs, including the upfront investment required, and a difficulty in delivering practical applications from some emerging technologies is limiting companies' willingness to invest.

Social media continues to grow as a communication medium with Facebook dominating and Instagram making strides in perceived effectiveness. In Cork an excellent engineering business focussed on the farmer, O'Donovan Engineering, is experiencing the benefits. Deirdre O'Donovan, General Manager, says, "In the past year we've engaged heavily in Instagram. We find that highlighting our products in a photo and using the click to buy functionality is helping drive lead generation and ultimately sales. An increasing

number of our farmer customers are now on Instagram and it's one of the channels we use to market our products."

Succession

When it comes to personal finance, only 49% of respondents have a pension plan in place. Given the effort that goes into running a business, pension planning and a secure financial future should be top of the agenda for all business owners. It is also noteworthy that only 19% of companies have a clear succession plan in place. This is similar with farmers where 86% of farmers do not have a clear succession plan in place, according to the ifac Farm Report 2019. Documenting a clearly thought-out succession plan is a piece of work the other 81% of respondents should try and address over the coming 12 months.

Finally, as a business providing specialist advice and support to the farming, food and agribusiness community, we greatly admire and respect the entrepreneurs who create and build their own business. These businesses make a significant contribution to the Irish economy and their local community. We wish you every success over the coming 12 months and are here to support you on your journey.



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